

Exploration & Production Companies

OUTPERFORM

OGDC/PPL Attractive Beyond Circular Debt Stock

20 February 2024

- Compelling valuations amid unrestricted cash flows.** Amid the impasse over CD stock settlement, OGDC/PPL are trading at unjustifiably low P/E ratios of 2.5/2.6 compared to MARI's 3.7. In light of the recent gas price hikes, E&Ps are expected to realize 100% cash sales moving forward. However, their stock prices have been pushed further below their justified fair values. We anticipate payouts of OGDC/PPL to rise to ~50/40% from FY25 onwards, with dividend yields reaching record highs of approximately 19/15% in FY25.
- Efforts towards CD stock clearance will likely continue.** We believe that the resolution of the CD stock issue is inevitable, and the substantial trade debts on the balance sheets of OGDC/PPL should not be overlooked. Considering recent developments and assuming that the only hindrance is the IMF or a supplementary grant, there's a possibility of its inclusion in the Budget for FY25, particularly since it would not impact the fiscal deficit. We discount overdue trade debts by 60%, assuming gradual settlement over a span of 10 years.
- OGDC/PPL upping their exploration momentum.** While, MARI's high P/E can be explained by its aggressive exploration efforts in the sector, which is a catalyst of future growth. However, in line with the recent energy reforms in the sector, OGDC and PPL have both enhanced their capex requirements for the ongoing year, and currently have 2/4 & 1/1 exploratory/development wells, respectively, in process. Whereas, MARI has 1/1 exploratory/development well in progress.
- Valuations.** We reiterate our outperform stance on OGDC, PPL, and POL, with upside potentials of 90/66/46%, respectively. While, we have a neutral stance on MARI with an upside of 14%.

FV (PKR/sh)	OGDC	PPL	MARI	POL
PV of FCF	82	105	1,594	311
Cash	28	24	504	413
Remaining Reserve Value	24	9	309	12
Other WC*	11	(36)	104	(147)
MARI stake value	10	-	-	-
Fair Value (ex CD)	155	102	2,511	590
Trade debts	162	180	-	-
Trade debts realized at 40%	65	72	-	-
Fair Value	220	174	2,511	590
P/E (on FY24E)	2.52	2.62	3.72	3.32

Source: Company Accounts, Optimus Research

*Excluding Overdue Trade debts of OGDC/PPL

*Discount rate used at 22%

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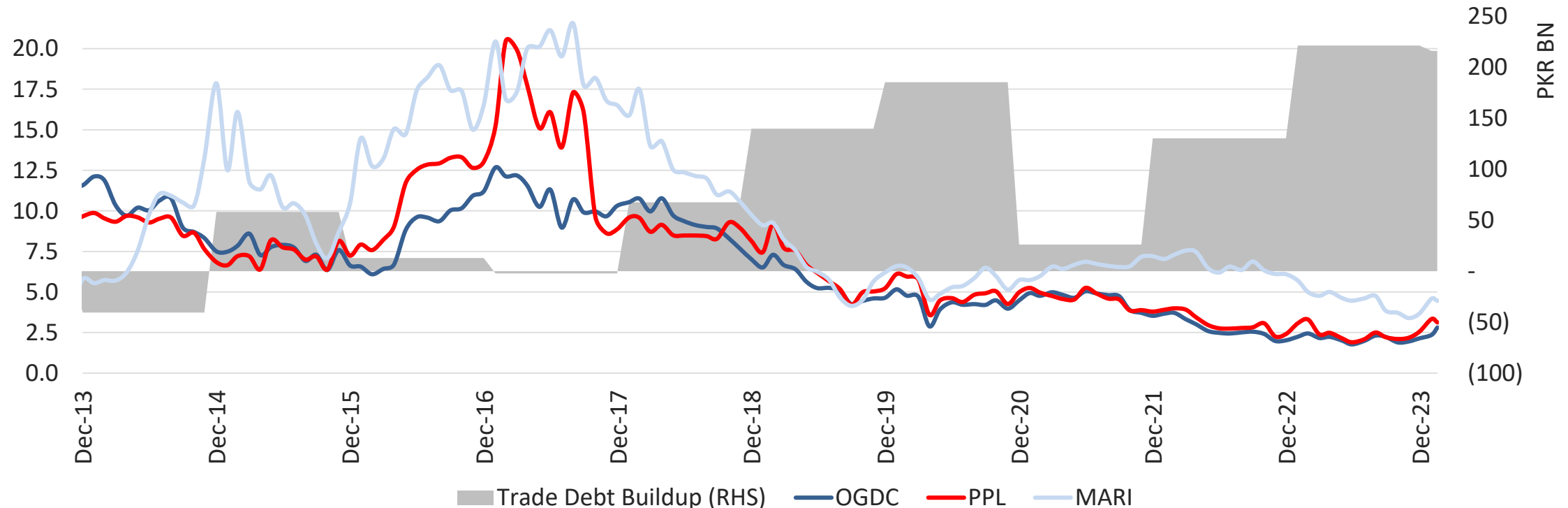


E&Ps Trading at Appealing Valuations, Despite Sharp Gas Price Hikes

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OGDC and PPL are trading at unjustifiably low forward P/E ratios of 2.52 and 2.62, respectively, despite significant gas price increases warranting a complete stoppage of further flow of CD at this point. Meanwhile, MARI is still trading at a comparatively better P/E ratio of 3.72, based on FY24 estimates.

P/E vs Trade Debt Buildup

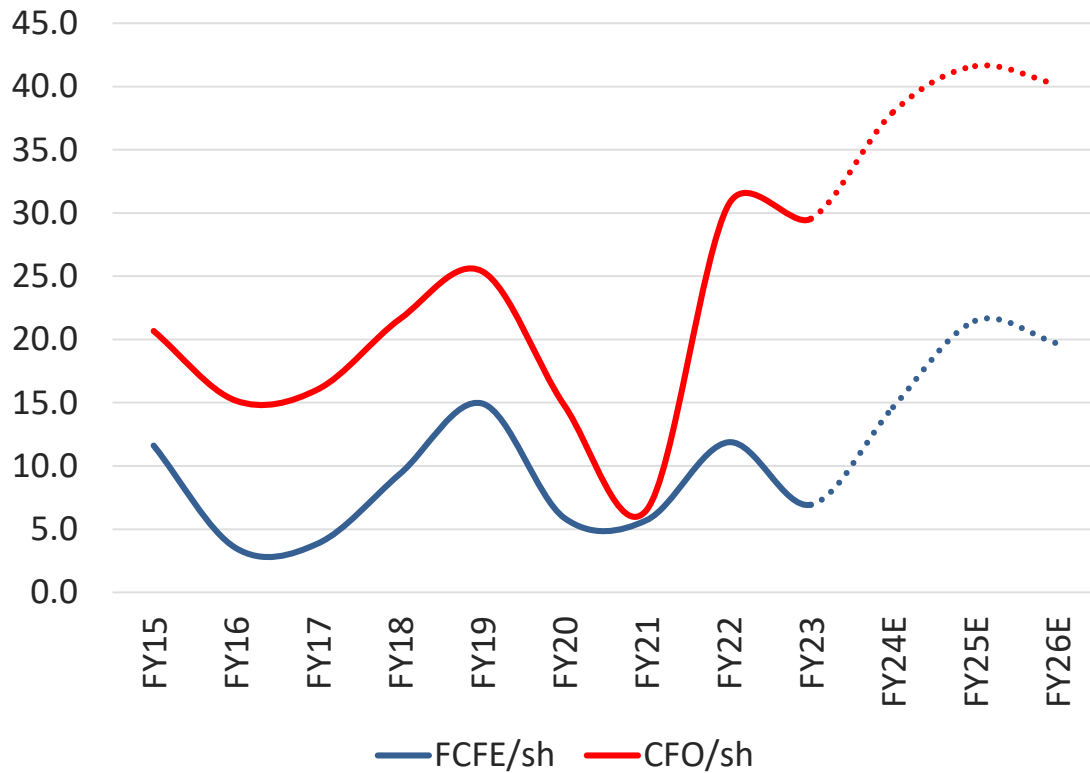


Source: Zakheera, Optimus Research

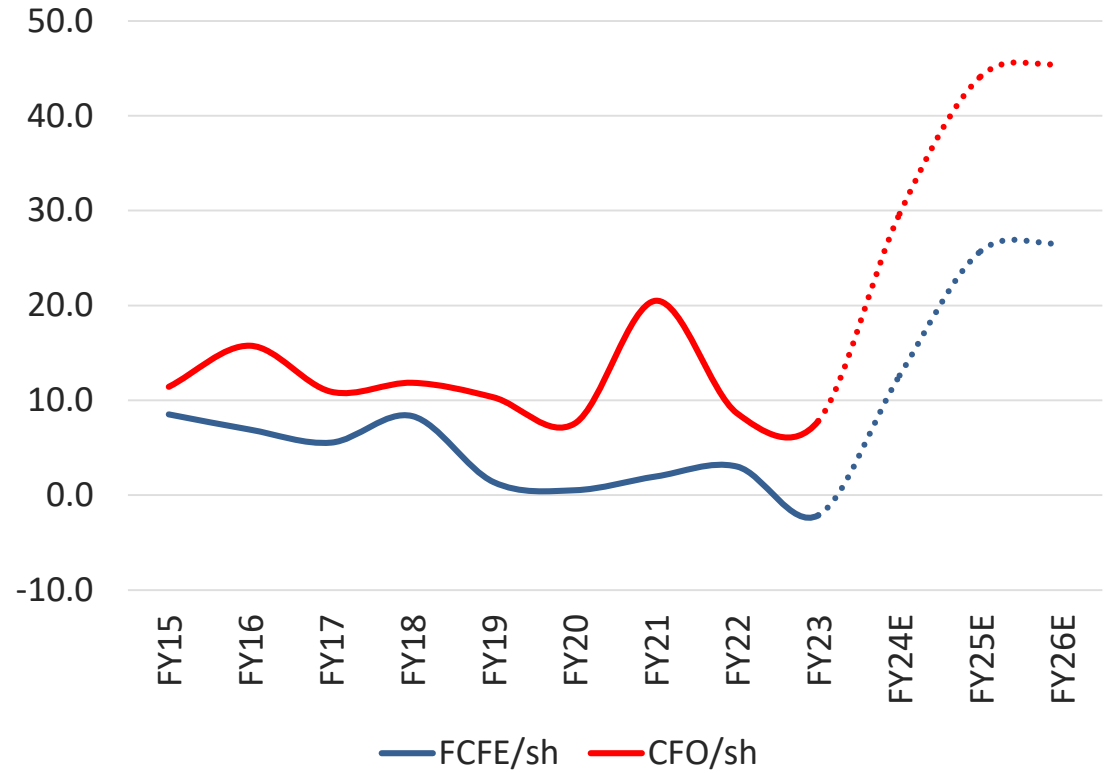
Note: Trade debt build-up is the sum of increase in trade debts of OGDC and PPL

Enhanced Cash Sales to Improve E&Ps Financial Positions

OGDC's increasing cash flows expected in future (PKR/sh):



PPL's enhanced cashflows expected moving forward as well (PKR/sh):

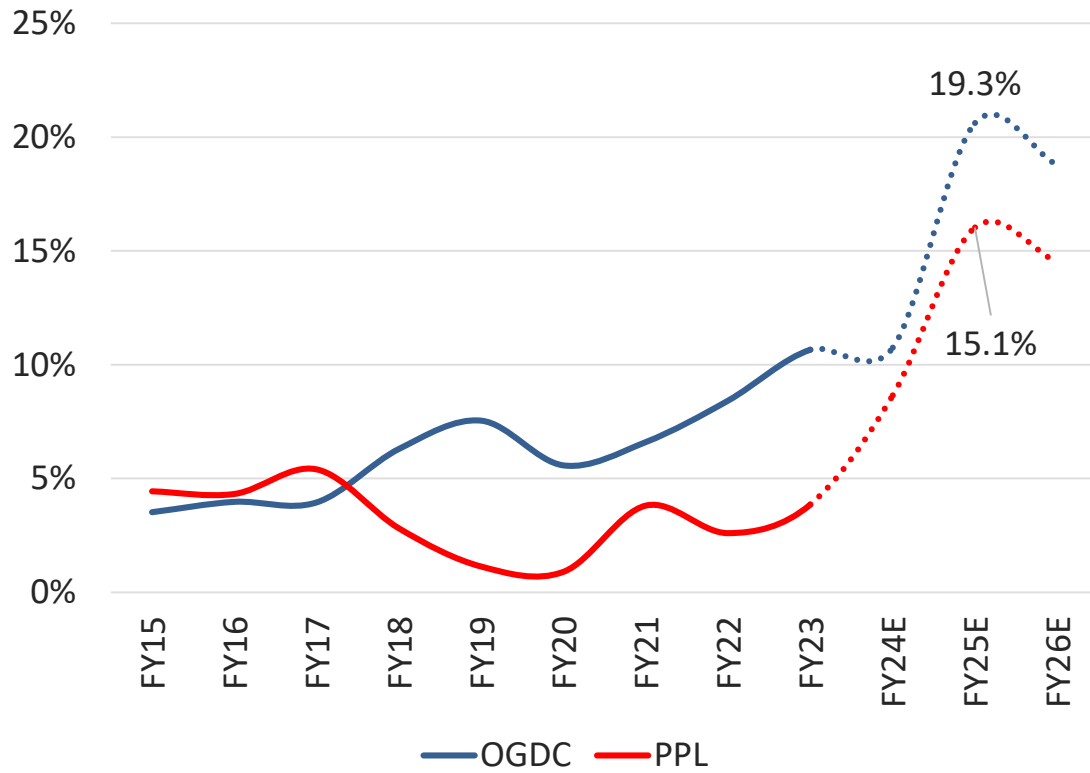


Source: Zakheera, Optimus Research

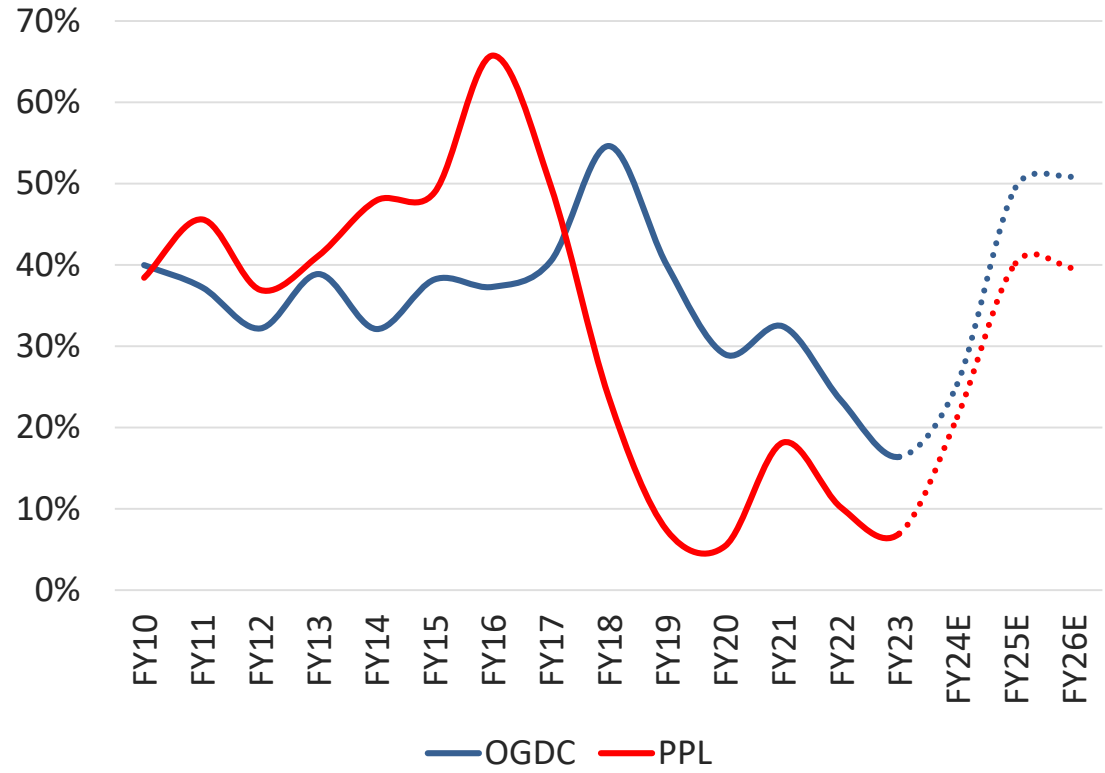
Source: Zakheera, Optimus Research

Stronger Cash Positions to Easily Support Enhanced Payouts

Dividend yields to reach all time high in FY25E:



Payouts of OGDC/PPL to reach pre CD issues level of 50/40% in FY25E:



Source: Zakheera, Optimus Research

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OGDC/PPL Trading Significantly Below Their Historical Prices

OGDC's adjusted price reached its peak of PKR 288/sh in FY14 & has been lower since:



PPL's adjusted price also reached its peak of PKR 260/sh in FY14 & has been lower since:



Source: Zakheera, Optimus Research

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Analyst Certification

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