Company Update | Pakistan Research

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PPL: Deriving value from improved cash positions

Pakistan Petroleum Limited

PSX: PPL | Bloomberg: PPL PA | Reuters: PPL KA

We revise our stance to "Buy" on Pakistan Petroleum Limited (PPL) with our Dec-25 price target (PT) of PKR 278/sh, which projects a capital upside of 44% along with a dividend yield of 3.3%. The stock is currently trading at a discounted P/B of 0.7x along with a FY26 P/E of 5.6x against its historical 10-year average of 1.5x and 6.8x, respectively.

- **Improved cashflow amid structural reforms:** Under the IMF agreement, the Government of Pakistan implemented multiple price hikes to eradicate the long-standing issue of circular debt. Consequently, the gas system went from an OGRA estimated shortfall of PKR 171.2bn in FY24 to a projected surplus of PKR 78.9bn in FY25.
- **Reko Diq – A tier-one asset ready to be realized:** Reko Diq's enormous copper and gold reserves yield a project NPV of USD 18.5bn, which may improve both PPL and Pakistan's future prospects. Utilizing Barrick's projections and timelines regarding the project, our base case for Reko Diq estimates a valuation impact around PKR 191bn (PKR71/sh) for PPL.
- **Unlocking value with cash reserves: As of Sep-24,** PPL carries receivables amounting to PKR 574bn (PKR 210/sh). Given increased probability of surplus cash in the system, we believe the payments for outstanding receivables to the gas chain will continue. Assuming the cash is realized in equal installments over 10 years, the discounted value is estimated at PKR 88/sh.
- **BLZ – A diversification effort:** PPL has been developing its mining business as a diversification measure to decrease its concentration of earnings originating from energy resources. The joint venture (JV) currently produces approximately 250,000 MT p.a. of barytes and is poised to achieve greater operational efficiency over time.

Summary	FY22A	FY23A	FY24A	FY25E	FY26F	FY27F
EPS	20.0	36.0	42.0	32.3	36.0	34.5
EPS YoY	3.9%	80.3%	16.7%	-23.1%	11.6%	-4.1%
DPS	2.0	1.5	6.0	6.5	7.0	7.0
BVPS	159.8	198.7	235.1	260.8	289.9	317.4
PER	10.1	5.6	4.8	6.2	5.6	5.8
Div. Yield	1.0%	0.7%	3.0%	3.2%	3.5%	3.5%
EV/EBITDA	4.0	2.6	2.4	2.4	1.8	1.5
P/B	1.3	1.0	0.9	0.8	0.7	0.6
ROE	13.2%	20.1%	19.4%	13.0%	13.1%	11.4%

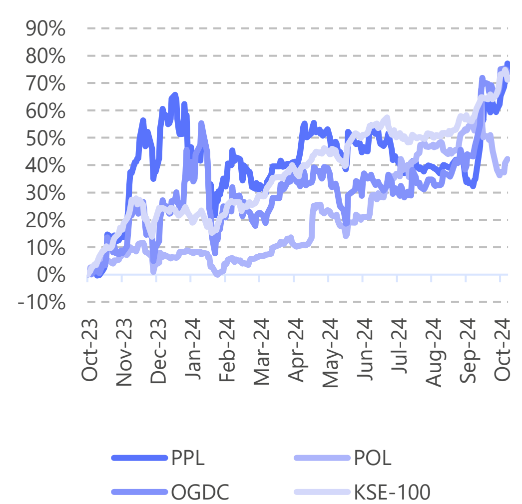
Source: Company Accounts, Akseer Research

Key Data

PSX Ticker	PPL
Target Price (PKR)	278
Current Price (PKR)	198
Upside/(Downside) (%)	40%
Dividend Yield (%)	3.3%
Total Return (%)	44%
12-month High (PKR)	215
12-month Low (PKR)	94
Outstanding Shares (mn)	2,721
Market Cap (PKR mn)	538,425

Source: PSX, Akseer Research

Relative Price Performance



Source: PSX, Akseer Research

Improved cashflow amid structural reforms

Timely tariff adjustments in Nov-23 and Feb-24 slowed down the accumulation of circular debt in the system from PKR 21.8bn/month in 1HFY24 to PKR 0.5bn/month in 2HFY24. 1QFY25 has bolstered our faith in the potential of a circular debt resolution with a staggering attrition rate (surplus) of PKR 9.2bn/month, thereby, resulting in a 0.6% QoQ decline in trade debts for PPL during 1QFY25.

The reforms to the gas system aided PPL's gas sale recovery to climb to 109% during 1QFY25 against a meagre 3-year average of 34%. With the significant recovery in gas sales, PPL now has the financial flexibility to invest in exploration, aiming to counterbalance its production decline (a 5-year CAGR of -5% YoY) and potentially extending one of the shortest reserve lives (9 years) in the listed equity space.

While improved cash flows are expected to support a 30% dividend payout ratio, the financial obligations related to the Reko Diq project could restrict the company's ability to achieve this target in the short term. Therefore, our base case assumes a more conservative 20% payout ratio.

Phasing out captive supply: The government's decision to phase out captive power supply from Jan-25 could significantly exacerbate existing challenges within the gas system. While reduced offtakes aggravate the ticking transmission pipeline bomb, the government is actively considering adopting a uniform gas pricing mechanism that is bound to wrench domestic consumption, adding fuel to the fire.

Phasing out captive supply and implementing a uniform gas pricing mechanism are likely to slow down unwinding circular debt stock.

OGRA's revised petition addresses these concerns, balancing the system even without captive through another rate increase.

Third-party gas sale - a way for sustainable growth: Recent developments on the third-party gas sale framework are poised to allow E&P companies to sell a maximum of 100mmcfd of gas from incremental production to parties other than the federal and provincial governments. The enactment of this framework under the Petroleum Policy 2012 will alleviate the transmission pipeline risk and incentivize increased production flows through a premium chargeable on zonal pricing.

Reko Diq – A tier-one asset ready to be realized

The current projections of rising automotive electrification reflect the global shift toward green energy sources, thereby driving copper demand. At a time when the 10-year transition to electric vehicles plan is the buzz, and current copper resources are only expected to meet 80% of the global copper demand by 2035, Reko Diq boasts massive reserves of copper and gold - 14.1mn tons and ~17.5mn oz, respectively. Given that EV production requires 60-80 kg per unit, the surge in demand, driven by the EV revolution increases the potential for a sustained 40-year CAGR of 5% (1984-2024). This, in turn, presents additional upside potential for earnings from Reko Diq.

Scenario Analysis	PKR/sh
Scenario 1	
Core – PPL	208
Reko Diq - Retention	71
Target Price (TP)	**278**
Scenario 2	
Core - PPL	208
Reko Diq Stake Sell (25% Discount)	53
Target Price (TP)	**261**

Source: Company Accounts, Akseer Research

Barrick estimates Phase 1 to operationalize by 2028 with an annual output of 260kt and 300koz for copper and gold, respectively. The project's development entails a capital expenditure of ~USD 9.5bn (Phase 1 – USD 6.0bn, Phase 2 – USD 3.5bn). PPL's cash calls for Phase 1 capital outlay are anticipated between PKR 13/sh and PKR 14/sh for FY25 to FY27.

Our base case (project's retention) assumes a conservative price CAGR of 4% for both gold and copper, resulting in a project value of USD 18.5bn and a projected ROE of 48% in the first year of operations. This translates into an earnings impact of PKR 17/sh for FY29, while the overall valuation impact is estimated at PKR71/sh.

PPL may exit Reko Diq, potentially freeing up cash for aggressive exploration.

PPL, like all other E&Ps, is looking to diversify its operations. However, Manara Minerals' intent to acquire the asset may force PPL to exit if the government decides to liquidate it to Saudi Arabia to generate foreign exchange. OGDC and

PPL's exit from the venture may alleviate the entities' strained liquidity positions, making room for a relatively aggressive exploration campaign, as announced for FY25.

Reko Diq Feasibility Study Snapshot		
Mine Life (yrs)	37	
	Phase 1	**Phase 2**
Copper (kt)	260	400
Gold (koz)	300	500
Strip Ratio	0.5	1
Construction Capital (USD bn)	5.5 – 6.0	3.0 – 3.5
Cost of Sales (USD/lb)	1.1 – 1.4	1.1 – 1.4
C1 Costs (USD/lb)	0.5 – 0.7	0.6 – 0.8

Source: Barrick Gold Investor Day Presentation, Akseer Research

Unlocking value with cash reserves realization

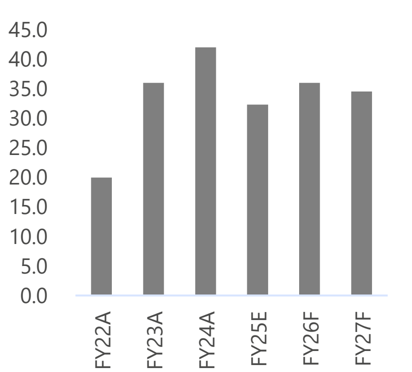
As of Sep-24, PPL holds PKR 574bn in outstanding receivables, equivalent to PKR210/sh, representing its robust financial position. With recent reforms aimed at improving the gas sector and circular debt resolution, there is a growing likelihood of surplus cash entering the system, facilitating the continued payment of these receivables. Assuming a 10-year payment cycle, the discounted value of these receivables is estimated at PKR 88/sh. As these receivables are realized, PPL will likely benefit from improved liquidity, enabling reinvestment in growth initiatives and potential dividends.

Falling reserves, curtailed production, and earnings outlook

The energy sector carries a plethora of interlinked problems, the solutions to which require holistic yet phased reforms. Currently, the gas transmission pipeline runs the risk of implosion owing to reduced offtakes from the power producers. With the impending phase-out of captive offtake, PPL might experience curtailed production, which will ultimately impact its earnings in the short term. We anticipate that the deferment of LNG cargoes and the return to normal operations will mitigate this risk by FY26, following the approval of the third-party gas sale framework.

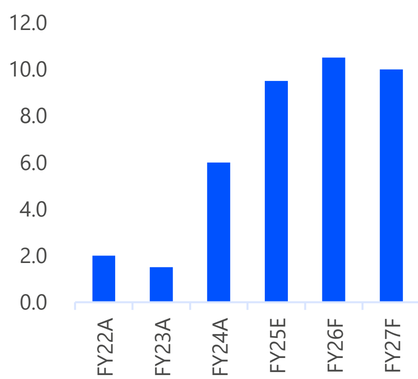
PPL faces production challenges but aims to reverse exploration declines with new investments and enhancement campaigns, despite security hurdles in frontier regions.

Earnings Outlook (PKR/sh)



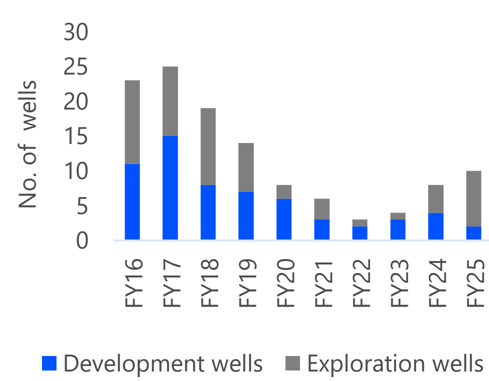
Source: Company Accounts, Akseer Research

Dividend Payout (PKR/sh)



Source: Company Accounts, Akseer Research

Drilling activities - PPL



Source: PPIS, Akseer Research

A decline in exploration activities between FY17 and FY22 has contributed to a 5% YoY decline in the R/P ratio between FY22 and FY24. However, the improved cash position signals a reversal in this trend, with the hope of replenishing the company's reserves through high risk/high reward spud-ins while exploring other business avenues.

Production enhancement campaigns and maturing fields: Owing to the natural decline of mature fields like Adhi, the company's management undertook production enhancement campaigns for Sui, through feeder line optimization and surface network capacity enhancement, ensuring the decline was arrested at 7% for FY24 compared to 11% for FY23.

Abu Dhabi's offshore Block 5: The company has submitted the Field Development Plan for three fields (2 of which were drilled to verify hydrocarbon volumes and reserve estimates) to ADNOC (operator) and expects the approval for the third exploratory well by Dec-24. PPL's cash calls for this campaign are expected to total USD 304.7mn over the next 5 years. Any developments on the commercial operations of this block will act as a further positive trigger to the company's earnings and valuation.

Frontier regions: Despite the company's consistent liaison with law enforcement agencies to improve law and order, security concerns continue to obstruct the Magnetotelluric (MT) survey for Margand's promising reserves. Gas was discovered at Margand X-1 in Dec-19, with testing flows reported at 10.7 mmscfd. The additional flows are expected to post an additional PKR 0.9/sh to the company's bottom line.

Any positive developments in the third-party gas sale framework are expected to ramp up production from fields that were previously economically unfeasible.

BLZ - A diversification effort

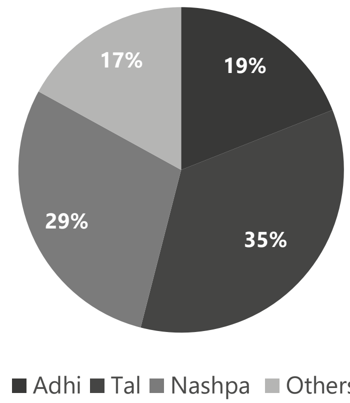
BME (50:50 JV between PPL and the Government of Balochistan) acts as the domestic price setter due to its control of 90% of the country's baryte reserves.

Gunga (near Khuzdar) is home to 5 million proven and ~50-100 million tons of probable baryte reserves, which will allow Pakistan to rank in the top 10 producers.

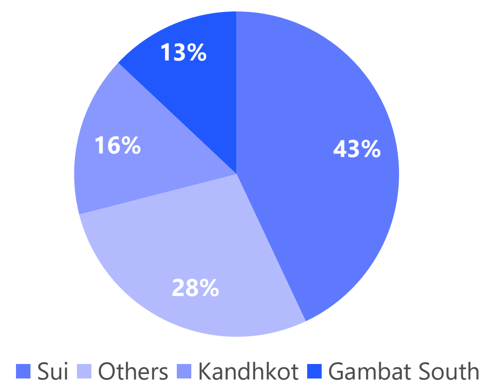
Rank	Country	Production (000 tons)	Share 2022 (%)
1	India	2,000	24.16
2	China	2,000	24.16
3	Morocco	1,100	13.29
4	Kazakhstan	650	7.85
5	Mexico	498	6.02
6	United States	362	4.37
7	Türkiye	344	4.16
8	Laos	303	3.66
9	Russia	260	3.14
10	Iran	225	2.71
11	Pakistan	128	1.55
12	Bulgaria	75	0.91
13	Canada	50	0.6
14	Bolivia	49	0.59
15	Algeria	45	0.54

Source: World Mining Data, 2024

Oil Production

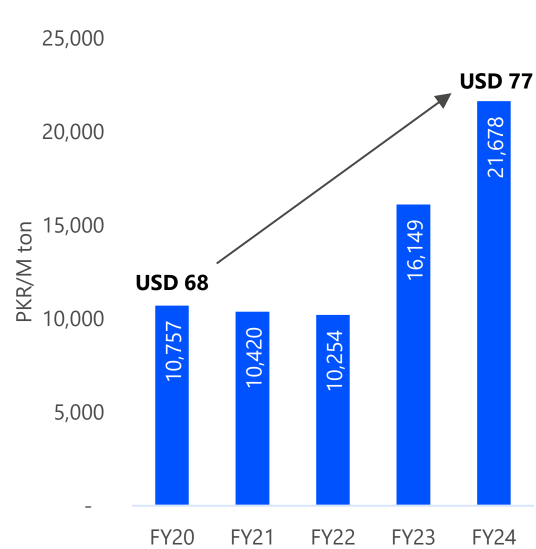


Gas Production



Source: Company Accounts, Akseer Research

Baryte Realized Price



Source: Company Accounts, Akseer Research

Even though Pakistan fails to capture the maximum return from this commodity owing to low-quality produce, for FY24, the nation's baryte exports amounted to USD 15.9mn (PKR 4,506mn), most of which were exported to Kuwait, Oman, and the UAE.

The joint venture (JV) currently operates a grinding plant with a capacity of 200 tons per day, specifically for oil drilling barytes, positioning it well to benefit from rising global baryte prices.

The company has stated that the financing agreement for the BLZ project is yet to be finalized. However, in light of the recent meetings with the Government of Balochistan on mineral excavation, we expect rapid progress on this development.

Company Description

Pakistan Petroleum Limited, together with its subsidiaries, engages in the exploration, prospecting, development, and production of oil and natural gas resources in Pakistan, Iraq, and Yemen. It produces natural gas, crude oil, natural gas liquids (NGLs), and liquefied petroleum gas (LPG) from fields located in Sui, Kandhkot, Adhi, Mazarani, Chachar, Adam, Adam West, and Kinza regions.

Sum of Parts Valuation	PKR/sh
PV of Reserves	162
Cash	18
Short Term Investments	28
Projects	
Reko Diq	71
Target Price	278

Source: Company Accounts, Akseer Research

Valuation Basis

Our PT for PPL has been computed using the reserve-based free cash flow to equity (FCFE) method. We have used a risk-free rate of 12% and a market risk premium of 6% to arrive at a cost of equity of 20%.

Investment Thesis

We have a 'Buy' recommendation on the stock based on our Dec-25 PT of PKR 278/share, which results in an upside of 44% along with a dividend yield of 3.3%. Our investment case on PPL is based on (1) recovery of circular debt stock and (2) incremental production from discoveries.

Risks

Key downside risks to our investment thesis include (1) a decrease in oil prices, (2) delay in development of discoveries, (3) low success ratio of drilling activities, (4) application of expected credit losses for receivables due from GoP, (5) a lower-than-estimated life of main reserves, (6) continued production curtailment due to RLNG line pressure, and (7) further delays in the resolution of circular debt.

Income Statement (PKR mn)	FY22A	FY23A	FY24A	FY25E	FY26F	FY27F
Net sales	203,811	286,480	288,797	265,491	300,782	289,792
Field expenditures	40,776	48,453	54,727	55,064	59,836	62,059
Royalties	31,018	46,478	44,689	39,592	46,991	45,056
Gross profit	132,017	191,549	189,381	170,834	193,956	182,676
Other income	14,232	17,539	16,977	21,800	22,876	27,825
Other charges	13,929	15,771	18,340	16,417	18,639	17,555
Finance cost	1,297	1,485	1,580	1,345	1,382	1,419
Profit before tax	**98,917**	**165,601**	**159,782**	**151,406**	**169,672**	**164,204**
Taxation	44,585	67,664	45,473	63,528	71,629	70,203
Profit after tax	**54,333**	**97,937**	**114,309**	**87,877**	**98,043**	**94,001**

Source: Company Accounts, Akseer Research

Balance Sheet (PKR mn)	FY22A	FY23A	FY24A	FY25E	FY26F	FY27F
PPE	139,578	135,860	134,020	150,716	171,132	190,919
Other LT assets	36,467	59,503	68,079	68,168	68,250	68,384
Non-current assets	176,045	195,363	202,099	218,884	239,382	259,303
Current assets	452,634	594,749	705,349	693,721	756,162	815,259
Total Assets	**628,679**	**790,112**	**907,448**	**912,606**	**995,544**	**1,074,563**
Non-current liabilities	65,305	71,605	71,334	73,420	75,571	77,788
Current liabilities	128,670	177,758	196,541	129,420	131,213	133,060
Total Liabilities	**193,974**	**249,364**	**267,874**	**202,841**	**206,784**	**210,848**
Equity	434,704	540,747	639,573	709,764	788,760	863,715
Total Equity & Liabilities	**628,679**	**790,111**	**907,448**	**912,605**	**995,544**	**1,074,563**

Source: Company Accounts, Akseer Research

Cashflows (PKR mn)	FY22A	FY23A	FY24A	FY25E	FY26F	FY27F
Net income	54,333	97,937	114,309	87,877	98,043	94,001
Non-cash charges	17,308	20,818	22,184	23,228	26,264	29,557
Operating cash flows	859	2,090	79,524	70,960	128,846	129,399
FCFF	**(7,228)**	**(13,467)**	**60,693**	**31,757**	**82,875**	**80,733**
Net borrowings	-	-	-	-	-	-
FCFE	**(8,526)**	**(14,952)**	**59,113**	**30,976**	**82,076**	**79,921**
Net change in cash	(17,086)	(6,846)	43,630	13,289	63,029	60,874
Closing cash	**5,427**	**6,106**	**7,074**	**48,695**	**81,150**	**109,921**

Source: Company Accounts, Akseer Research

Disclaimer

Valuation Methodology

To arrive at our 12-months Price Target, the JV uses different valuation methods which include: 1). DCF methodology, 2). Relative valuation methodology, and 3). Asset-based valuation methodology.

Ratings Criteria

JV employs a three-tier ratings system to rate a stock, as mentioned below, which is based upon the level of expected return for a specific stock. The rating is based on the following with time horizon of 12-months.

Rating	Expected Total Return
Buy	Greater than or equal to +15%
Hold	Between -5% and +15%
Sell	Less than or equal to -5%

Ratings are updated to account for any development impacting the economy/sector/company, changes in analysts' assumptions or a combination of these factors.

Research Dissemination Policy

The JV endeavors to make all reasonable efforts to disseminate research to all eligible clients in a timely manner through either physical or electronic distribution such as email, fax mail etc.

Analyst Certification

The research analyst, denoted by 'AC' on the cover of this report, has also been involved in the preparation of this report, and is a member of JV's Equity Research Team. The analyst certifies that (1) the views expressed in this report accurately reflect his/her personal views and (2) no part of his/her compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this report.

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