



AKD Securities Limited

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Pakistan Stock Exchange

Equity Research / Pakistan



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Today's Daily

■ Pakistan Fertilizer: Export key to clearing excess inventory

Recent recovery in international urea price to US\$240/ton (up 42% since Jul'16) presents a lucrative opportunity for local manufacturers to export excess urea inventory (Nov'16 urea inventory in the system stands at 1.45mn tons, down 15%MoM/ up 56%YoY). Weakening demand (poor farm dynamics) along with record level urea production has led to high inventory build-up in the system which we expect to persist in the near-term with urea inventory forecasted at 1.2mn/1.8mn tons by the end of CY16/CY17 respectively. In this backdrop, the GoP is expected to allow export of 0.8mn tons of urea in line with a proposal of Ministry of Industries. Our sensitivity analysis of urea export highlights incremental profitability on our AKD Fertilizer Universe in the range of 6%-20% at different export levels. In such a scenario, EFERT remains a key beneficiary on account of its low cost/bag and healthy market share, followed by FFC owing to market leadership in urea sales.

KSE100 - Index

Current 48,713.63
Previous 48,704.99
Chg. 0.02%

Mkt Cap. (PKRbn/US\$bn)

Current 9,754 / 93.07
Previous 9,752 / 93.04
Chg. 0.03%

Daily Turnover (mn)

Current 329.24
Previous 403.81
Chg. -18.5%

Value Traded (PKRmn/US\$m)

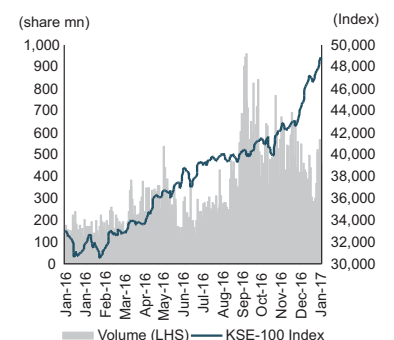
Current 18,004 / 171.78
Previous 21,768 / 207.69
Chg. -17.3%

AKD Daily

Friday, Jan 06, 2017

News and Views

- KEL shelved 420MW BQPS-1 coal conversion project after the utility failed to secure cost-effective tariffs from the regulator.
- Total cement dispatches grew 8.65%YoY to 19.81mn tons in the 1HFY17. Domestic dispatches registered growth of 11.07%YoY in 1HFY17 while exports fell by 3.53%YoY in 1HFY17. On monthly basis, total cement dispatches rose by 3.33%YoY to 3.555mn tons in Dec'16 where local dispatches were up 6.74%YoY to 3.186mn tons and exports were down 18.98%YoY to 0.369mn tons.
- PSO has asked the government to release Pkr30bn immediately to meet its payment obligation as the company receivable to the power companies reaches to Pkr219.4bn.



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Pakistan Fertilizer: Export key to clearing excess inventory

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Urea Export-Sensitivity Analysis: If GoP allows export of 0.8mn tons of urea, export offtake for FFC/EFERT/FATIMA/FFBL works out to be 374k/226k/51k/70k tons based on current market shares of 47%/28%/6%/9%. Consequently, our EPS estimates for FFC/EFERT/FATIMA/FFBL/ENGRO can go up by PkR 0.63/1.04/0.23/0.16/1.50 (per share), assuming urea is exported at the international price of US\$240/ton. Moreover, an incremental earnings impact of PkR 0.31/0.18/0.03/0.08/0.25 (per share) on FFC/EFERT/FATIMA/FFBL/ENGRO is estimated for every US\$10/ton increase in export price.

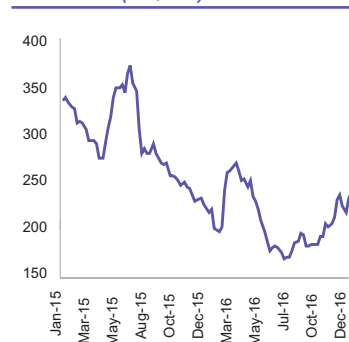
Sensitivity analysis: Urea export

EPS(PkR)	800k tons			900k tons		
	US\$240/t	US\$250/t	Inc. US\$10/t	US\$240/t	US\$250/t	Inc. US\$10/t
FFC	0.63	0.94	0.31	0.71	1.05	0.34
EFERT	1.04	1.22	0.18	1.17	1.37	0.20
FATIMA	0.23	0.25	0.03	0.25	0.28	0.03
FFBL	0.16	0.24	0.08	0.18	0.27	0.09
ENGRO	1.50	1.75	0.25	1.68	1.97	0.29

Source: Co. report & AKD Research

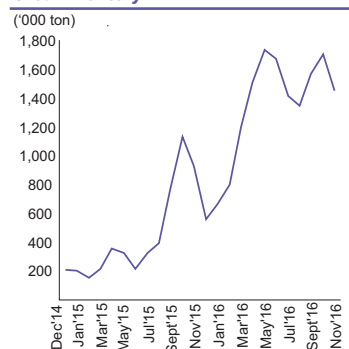
Urea Inventory Outlook: Significantly weak demand on account of poor farm incomes along with record level production from local players has led to high inventory build-up in the system. However, after the announcement of the subsidy package in budget FY17 and strong Rabi season, urea inventory levels have started to ease after peaking in May'16 (1.73mn tons). In this regard, Nov'16 urea inventory currently stands at 1.45mn tons (down 15%MoM/ up 56%YoY). That said, end of Nov'16 urea inventory levels were still equivalent to 2.9x of one month's average production for urea. In this backdrop, we are expecting CY16 to end with

Urea Prices (US\$/ton)



Source: Bloomberg & AKD Research

Urea Inventory



Source: NFDC & AKD Research



a stockpile of 1.2mn tons against the historical avg. of 300k tons. Going forward, after the end of current Rabi season, we expect demand to remain subdued in CY17 as well (i.e. ~5.7mn tons). On the production front, with improved gas supply situation along with LNG availability, local manufacturers have kept urea production high (up 14%YoY in CY16), a trend which we expect to continue in CY17 as well, with supply forecasted at 6.3mn tons next year. Consequently, with increased production coupled with relatively soft demand, we forecasted urea inventory to hover around 1.8mn tons by the end of CY17. Accordingly, with urea price rebounding to US\$240/ton after bottoming out in Jul'16 along with sufficient domestic inventory available, it provides a lucrative opportunity to local players to look for the export market in order to clear excess inventory in the system.

Outlook & Investment Perspective: Having lost 14% in CY16, the fertilizer sector remained under pressure on account of weak fertilizer dynamics, weak commodity prices and depressed farmer incomes. However, the price reduction of fertilizer products (Urea: PkR390/bag, DAP: PkR300/bag) in budget FY17 via reduction of GST (from 17% to 5%) & cash subsidy coupled with a promising Rabi season has resulted in a good recovery in fertilizer offtake in the latter part of CY16. That said, we continue to maintain our Marketweight stance on the sector until a sustainable improvement in the demand scenario. In this backdrop, FFC remains our top pick with our TP of PkR122.6/share, implying a total return of 20.9% (includes dividend yield of 10.7%).



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Neutral	≤ 5% to ≥ -5% potential
Reduce	< -5% to > -20% downside potential
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