



Today's Daily

■ Pakistan Cements: Fundamental Challenges Continues

In-line with recent negative developments, we have downward revised our Cement Universe TPs by an average of 20%. The new estimates incorporate i) recent interest rate hikes with avg. FY19 KIBOR at 8%, ii) avg. PkR/US\$ parity at 131.75 and iii) increased coal price (revised to US\$95/90 per ton for FY19/onwards). Despite the obvious negatives, we believe recent sector underperformance (down 31% over the past 3M vis-à-vis KSE-100 at -ve12.8%) has already reflected much of the adverse developments where keeping in view overall market performance, staggered build-up in selected names is recommended. In this regard, favored names include LUCK (TP: PkR666/sh – current price at PkR478/sh down 52% from peak), DGKC (TP: PkR118/sh – current price at PkR96/sh down 61% from peak), MLCF (TP: PkR65/sh – current price at PkR42/sh down 70% from peak) and PIOC (TP: PkR70/sh – current price at PkR70 down 74% from peak). Tailwinds include a continued increase in cement prices as well as sustained / increasing demand while headwinds including cost escalations including increased coal prices, currency deval as well as increased interest rates.

KSE100 - Index

Current	39,932.98
Previous	39,665.77
Chg.	0.67%

Mkt Cap. (PkRbn/US\$bn)

Current	8,275 / 64.52
Previous	8,192 / 63.87
Chg.	1.02%

Daily Turnover (mn)

Current	141.97
Previous	147.48
Chg.	-3.7%

Value Traded (PkRmn/US\$m)

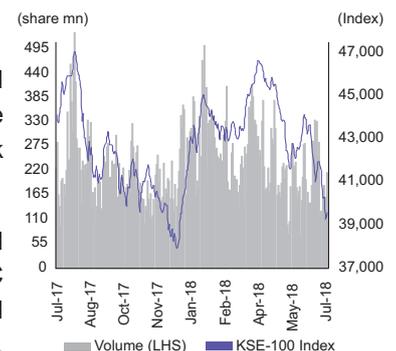
Current	6,021 / 46.94
Previous	6,086 / 47.45
Chg.	-1.1%

AKD Daily

Wednesday, Jul 18, 2018

News and Views

- A division bench of the Islamabad High Court (IHC) on Tuesday adjourned the matter of Nawaz and family (against their convictions by the Accountability Court-I in the Avenfield Apartments case) till the last week of July after issuing separate notices to NAB.
- Ministry of Finance (MoF) has reportedly expressed willingness to extend Rs 20 billion credit facility for establishing revolving account for CPEC project. China maintains that eight energy projects have been completed but are facing financial crises due to non-payment of dues.
- The inflows of Foreign Direct Investment in Pakistan stood at US\$2.767bn in FY18 as compared to US\$2.746bn received in FY17, up only 0.8%, lowest in the region



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Continuous pressure on input cost - suppressing margins: Declining consistently every quarter, gross margin for AKD cement space has come down to as low as 26% by the end of 3QFY18 (vs. 37% in FY17) owing to persistent upward pressure on input costs. In this regard, the sudden currency adjustment is another drag on margins that are already struggling on account of persistent rise in input costs (relentless increase in int'l coal prices to currently stand at US\$107/ton – up 32%YoY/13%CYTD). After reconsidering our assumptions for PkR depreciation (where our average PkR/US\$ parity now stands at 131.75 for FY19 vs. 124.11) and coal prices (revised to US\$95/90 per ton for FY19/onwards), we revise down our GM estimates for AKD cement universe by an average 4.5ppts to 22.5% for FY19F. Consequently, our earnings estimates go down by an average 15% for FY19F bringing down our Jun'19 TPs for the universe by an average 19%.

Higher debt servicing cost – another dampener: With the anticipation of more rapid interest reversal than expected, cement sector remains exposed to sizeable debt financing costs, considering current financial leverage of the sector (D/E: 35% in Mar'18) owing to ongoing expansion cycle. In this regard, our sensitivity analysis suggests bottom-line impact of 4-8% (FY19F) on AKD cement universe for every 100bps further hike in interest rate. In this regard, CHCC and DGKC being highly leveraged (D/E reached 50% by the end of Mar'18) stand more exposed to interest rate hikes than the rest.

Cement prices posted decent recovery: With the recent price hike of PkR10/bag yesterday, cement prices in the North region have posted a

Cement Sector: Earnings & TP revision

		EPS(PkR)	FY19F	FY20FTP- Jun'19	
LUCK	New	32.51	36.17	666.0	
	Old	35.72	39.93	790.0	
	Change	-9%	-9%	-16%	
DGKC	New	15.10	16.63	118.0	
	Old	18.64	20.11	158.0	
	Change	-19%	-17%	-25%	
MLCF	New	5.10	5.99	65.0	
	Old	6.17	7.17	89.0	
	Change	-17%	-16%	-27%	
FCCL	New	1.95	2.50	25.5	
	Old	2.45	3.04	32.4	
	Change	-20%	-18%	-21%	
CHCC	New	7.27	9.49	88.0	
	Old	9.18	11.78	117.0	
	Change	-21%	-19%	-25%	
PIOC	New	6.39	8.33	70.0	
	Old	8.03	10.12	91.0	
	Change	-20%	-18%	-23%	
GWLC	New	2.25	3.13	36.0	
	Old	2.94	3.92	47.0	
	Change	-24%	-20%	-23%	

Source: AKD Research

AKD Cement Universe: Financial Leverage

Mar'18	D/E Ratio	D/A Ratio
LUCK	-	-
DGKC	50%	24%
MLCF	32%	25%
FCCL	7%	5%
CHCC	50%	44%
PIOC	37%	30%
GWLC	27%	19%

Source: APCMA & AKD Research

Sensitivity Analysis: 100bps rise in discount rate

Universe	EPS Impact	% of FY19 EPS
LUCK	-	-
DGKC	0.66	4.1%
MLCF	0.23	4.1%
FCCL	0.01	0.5%
CHCC	0.64	7.8%
PIOC	0.32	4.7%
GWLC	0.11	4.2%

Source: APCMA & AKD Research



decent recovery from Feb'18 (cumulative increase of PkR85/bag in North), where prices are now up by almost 2.5% since its peak in Jun'17. Post the recent price recovery, we expect cement prices to remain at current levels for the remainder of the year. That said, pricing pressure can trickle down to the Southern region once DGKC's expansion comes through, further dragging regional utilization to ~65% by FY19 from 78% in FY18.

Investment Perspective: The cement sector has corrected 17% since May'17 on the risk of pricing indiscipline and higher coal prices. Despite the obvious negatives, we believe recent sector underperformance (down 31% over the past 3M vis-à-vis KSE-100 at -ve12.8%) has already reflected much of the adverse developments where keeping in view overall market performance, staggered build-up in selected names is recommended. In this regard, favored names include LUCK (TP: PkR666/sh – current price at PkR478/sh down 52% from peak), DGKC (TP: PkR118/sh – current price at PkR96/sh down 61% from peak), MLCF (TP: PkR65/sh – current price at PkR42/sh down 70% from peak) and PIOC (TP: PkR70/sh – current price at PkR70 down 74% from peak).



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



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