

# PAKISTAN CEMENT

# MARKET VISTA

## All set for good days ahead!

- Local cement dispatches declined by 5%YoY for Oct'21 where Northern region witnessed a decline of 8%YoY while South posted an increase of 11%YoY. Sequentially, 15%MoM increase was witnessed in local dispatches.
- Overall we expect the local demand to remain strong for FY22 as economic activity continues to pick up where private sector is expected to provide the major support to demand. However, exports are expected to take a hit in near term particularly as cost of manufacturing continues to increase courtesy coal prices.
- Although margins can take a hit in near term, given our view of coal prices retreating post winter, we expect profitability of the sector to improve significantly in medium term because cement prices have historically proved to be sticky.
- Recent volatility is a good opportunity to accumulate in our view as coal prices are expected to ease off post winter. In this backdrop, we advocate for building positions in stocks having strong balance sheet and opting for an expansion in the next expansion cycle hence our top picks include LUCK (TP: PkR1289.2/sh) and MLCF (TP: PkR80.1/sh).

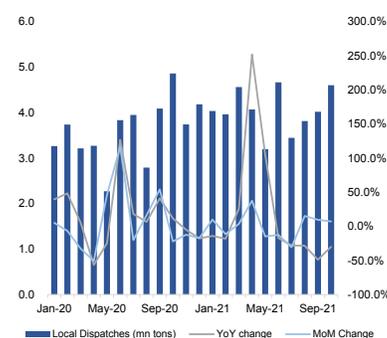
**Local demand increased by 15%MoM for Oct'21:** Local cement dispatches declined by 5%YoY for Oct'21 where Northern region witnessed a decline of 8%YoY while South posted an increase of 11%YoY. On sequential basis, across the board increase was witnessed (+15%MoM) where dispatches in North witnessed a sequential increase of 11%YoY while South posted sequential increase of 36%MoM. The YoY decline in dispatches for North was partly a result of high base as local dispatches in North stood at all-time high in Oct'20. However, sequential improvement is in line with historical trend where local demand picks up post monsoon season however moving forward, demand can witness a slight dent as we approach winter. Overall we expect the local demand to remain strong for FY22 as economic activity continues to pick up where private sector is expected to provide the major support to demand. However, recent legal cases and uncertainty around legality of some areas witnessing heavy construction poses a downside risk to our estimates in the Southern region. On the other hand, exports are expected to take a hit in near term particularly as cost of manufacturing continues to increase courtesy coal prices, making exports infeasible, particularly clinker exports.

**Profitability of the sector to improve in medium term:** Coal prices continue to remain volatile where after touching all time high of USD238/ton during Oct'21, they retreated to USD121/ton however lately, they are again on an uptrend and currently trade around USD149/ton. The volatility comes on the back of varying news coming out of China and other developed economies where price controls in China amid country asking local miners to scale up production resulted in decline in prices however concerns over gas shortage in Europe during winter have again resurfaced, providing support to prices. Local manufacturers have reacted to the increase in coal prices, albeit late, by increasing prices of cement by PkR50-60/bag in last 1-2 months. Although the move can dent margins in near term, given our view of coal prices retreating post winter, we expect profitability of the sector to improve significantly because cement prices have historically proved to be sticky.

**Outlook:** Cement stocks have also remained volatile lately with AKD cement universe retreating 36% from its CY21 peak on the back of upsurge in coal prices while recent decrease in coal prices has infused a rally with AKD cement universe increasing 22% from the recent low. Moving forward, we expect the volatility to continue as coal prices remain directionless while newsflow also suggests gas supply to captive power plants being discontinued and increase in power tariff. However the volatility is a good opportunity to accumulate in our view as coal prices are expected to ease off post winter. In this backdrop, we advocate for building positions in stocks having strong balance sheet and are opting for an expansion in the next expansion cycle hence our top picks include LUCK and MLCF. LUCK provides exposure to various sectors apart from cement where upcoming ventures like Lucky Electric Power Limited (LEPL) and manufacturing of Samsung phones are expected to be strong triggers. MLCF on the other hand i) has a strong balance sheet, ii) is going for an expansion to maintain its market share, and iii) will be among major beneficiaries of decline in coal prices.

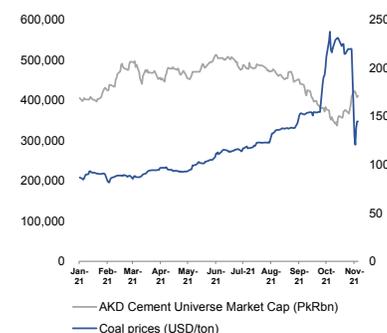
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Local cement dispatches



Source: APCMA & AKD Research

Market cap. of AKD Cement Universe vs. coal prices



Source: Bloomberg, PSX & AKD Research



AKD Securities Limited

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- Discounted Cash Flow (DCF, DDM)
- Relative Valuation (P/E, P/B, P/S etc.)
- Equity & Asset return based methodologies (EVA, Residual Income etc.)

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Buy	> 14.5% expected total return (Rf: 8.5% + Rp: 6%)
Neutral	> 8.5% to < 14.5% expected total return
Sell	< 8.5% expected total return (Rf: 8.5%)



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