

June 02, 2010

## Pakistan Market

## MORNING BRIEFING

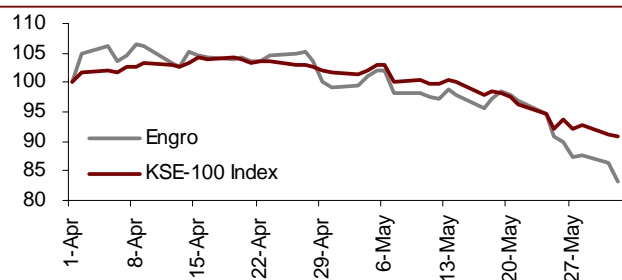


## Engro: attractive on exciting long term plays – Buy

KSE100 Index: Closing 9294.18 ↓ (-32.24)

The recent dip of 13% from its April 15, 2010 peak of 10,677 level has seen many of the blue chip companies slide down to even more attractive levels. Engro, being one of the blue chip companies, has lost 20% during the period. We believe, the underperformance in the scrip is mainly attributable to heavy foreign selling. Post the emergence of Greece debt crisis, selling has been witnessed in highly leveraged countries and stocks regionally, with Engro seemingly fitting the bill at the local bourse. Moreover, with no major budgetary concerns for the fertilizer or the foods business and compelling valuations of the stock, we remain bullish on the scrip. Based on yesterday's closing, the scrip is trading at post expansion 2011F and 2012F PE of 7.3x and 6.3x, respectively. We recommend investors to 'Buy' Engro on exciting long term plays (Foods, Fertilizer & Power) as it offers an upside of 41% (to our target price of Rs235 per share) to the investors. However, ongoing gas curtailment issue and cost overruns on expansions remain key risks to our valuation.

## KSE-100 index versus Engro



Source: KSE

## Key expansion updates

- **New urea plant** – The project is expected to come online in 3Q2010.
- **Qadirpur power plant** – It has already been commissioned in 1Q2010 and in a short span of less than

a month contributed 2.4% to Engro Corporation's consolidated profits.

- **Foods business** - The food business has continued to progress well and after achieving profitability in the dairy segment, Engro is aggressively marketing its ice cream business with strong results expected during the current summer season. Moreover, packaged juices are expected to be brought in to the market, in the current month.
- **Rice Business** - Expansions into the rice processing and trading business are also on track, with the rice processing plant likely to be operational by November 2010.

## Outlook: 'Buy' reiterated

Post this 20% decline and in the wake of impressive 1Q2010 results (a YoY growth of 176%), along with Engro's long term investments in the energy, foods and storage business, we reiterate our 'Buy' call on the scrip. Based on our target price of Rs235 per share, the scrip offers an upside of 41% to investors. Currently, Engro is trading at 2011F and 2012F PE of 7.3x and 6.3x respectively. However, the gas curtailment issue and timing & cost overruns on major expansion projects remain key risks to our thesis.

## Engro's SoTP valuation

| Company                  | Valuation (Rs/share) | Contribution | Valuation Method |
|--------------------------|----------------------|--------------|------------------|
| Engro Fertilizer & Eximp | 130                  | 55.3%        | FCF & DDM        |
| Engro Foods              | 65                   | 27.7%        | Price to sales   |
| Engro Polymer            | 15                   | 6.4%         | DCF              |
| Engro Energy             | 13                   | 5.5%         | DDM              |
| Engro Vopak              | 11                   | 4.7%         | DDM              |
| Engro Avanceon           | 1                    | 0.4%         | Valued at cost   |
| <b>Engro Corporation</b> | <b>235</b>           |              |                  |

Source: JS Research

## Also in focus

## Federal and Sindh govt. reach agreement on VAT

In a major breakthrough, a tentative agreement between the Federal and Sindh government was reached over VAT, with power to impose this tax on services to lie with provinces while collection power will be delegated to the federation on at least eight services. Further, the federation will not impose or collect tax on any service, except on the categories for which the provinces allows federation to collect it on their behalf. The tax on services collected by the federation would not form part of the divisible pool but will be distributed in accordance to disbursement terms agreed in the NFC award.

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