

March 04, 2009

Pakistan Market**Textile: Sector Update & outlook****MORNING BRIEFING**

KSE100 Index Closing 5596.49 ↓ (-84.80)

Pakistan's textile sector is going through challenging times with international recession, slowdown in local economy and political & security issues affecting industry dynamics. Moreover, due to shortfall in cumulative cotton arrivals in the current crop season, recent jump in cotton prices coupled with declining export orders have aggravated the current situation.

International cotton prices falling

World cotton demand is expected to exceed production next year for the first time since at least 2004 as farmers switch to more profitable crops and a rebounding global economy revives textile demand. However in the current crop year, there will be excess production (fifth straight annual surplus). Thus, international cotton prices have showed a downward trend since the turn of the year depicting a fall of about 12%.

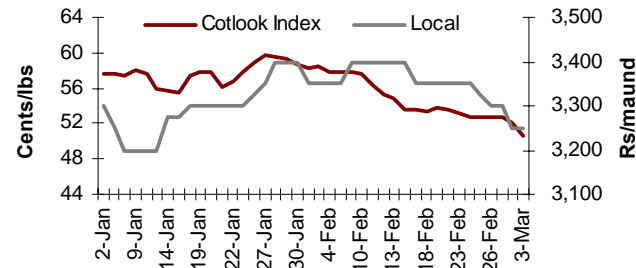
Local short production, another cause of concern

According to the latest numbers released by Pakistan Cotton Ginners Association (PCGA), cumulative cotton arrivals stood at 11.221mn bales in FY09 as of Feb 28, 2009. After five consecutive fortnights of decline in arrivals prior to the month of Feb, cotton arrivals Feb 2009 have performed relatively better to stand at 0.59mn bales depicting an increase of 5.3%. This has been due to release of cotton bales by farmers as they were hoarding earlier in the season due to unattractive prices. However recent rally in cotton prices have resulted in increased arrivals. We expect cotton arrivals for FY09 to be about 11.5mn bales versus 11.4mn bales last year and 5% lower than government's revised target of 12.1mn bales.

Due to lower than expected cumulative cotton arrivals, local cotton prices have shot up by 4% in the local market since Jan 1, 2009 and currently stand at Rs3,250/maund. Prices for (Jul-Feb) FY09 have averaged Rs3,500/maund, up 17%.

Moreover, according to industry sources, due to high cotton prices in the local market textile mills prefer to buy imported cotton rather than local cotton as they look to check their shrinking gross margins which are already under pressure

due to decline in sales orders.

Graph: Cotlook 'A' Index vs Local cotton prices

Source: JS Research, Thomson Reuters

Textile exports decline by 4% in Jul-Jan FY09

According to data released by Federal Bureau of Statistics (FBS), in the first 7 months (Jul-Jan FY09) Pakistan's textile exports have depicted a decline of 4% in US\$ terms however posting an increase of 22% amid Rupee devaluation. Textile's share in Pakistan's total exports has declined by 633bps to 54%. Moreover, Pakistan textile exports to USA, largest importer of Pakistan textile products, stood at US\$3.1bn in 2008 depicting a decline of 2.83%. Pakistan managed to maintain its share in US textile exports at 3.02%.

Table: Textile Exports

	Jul-Jan FY09	Jul-Jan FY08	%Δ
US\$ (mn)	5,827	6,057	-4%
PKR (mn)	448,740	369,141	22%

Source: JS Research

Nishat Mills: 'Buy' maintained

We only cover Nishat Mills amongst the textile sector due to limited trading volumes of other stocks. NML is currently trading at PE of 3.7x for FY09, 38% discount to the market's PE of 6.0x. Hence, we maintain our 'Buy' stance on NML.

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Also in focus**PSMC expected to post EPS of Rs8.15**

Pak Suzuki Motor Company (PSMC) is expected to announce its full year 2008 results today. We expect PSMC to post profit after tax of Rs670mn (EPS of Rs8.15) as against profit after tax of Rs2,978mn (EPS of 36.18) last year depicting a decline of 77%. In the last quarter alone, PSMC is expected to post profits of Rs33.5mn (EPS of Rs0.41) versus Rs426mn (EPS of Rs5.17) recording a decline of 92%. Decline in volumetric sales along with rising cost pressures amid yen appreciation and higher average steel prices during the period are the major reasons behind the decline in the profitability of PSMC.

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