June 08, 2010

Pakistan Market

MORNING BRIEFING

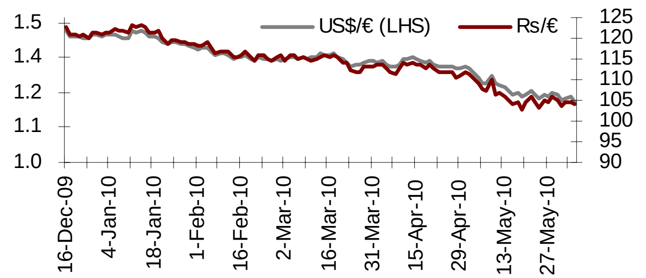
JS Research

Falling Euro a concern for Pak textile exports?

KSE100 Index: Closing 9791.64 ↑ (+154.76)

The prevailing debt crisis in Europe has led to persistent depreciation of Euro against US$ and PKR as it has weakened by 16.3% and 14.2%YTD, respectively. The fact that Pakistan derives approximately 27% of its total textile exports from this region, has triggered concerns over potential dampening of the textile sector's earnings courtesy potential foreign exchange losses. We believe, the impact of this decline will vary from company to company depending on its export revenue mix (which is either Euro or US$ denominated). For our analysis, we have selected a sample of four export oriented textile companies with exposure in the European market.

Euro against US$ & PKR



Source: JS Research

Euro depreciation: concerns appear exaggerated

We believe the impact of Euro's depreciation would be muted as many of the exporters have their pricing set in US$ even for their exports to Europe. Our view is backed by our study of the available numbers and discussions with the management of four leading textile companies namely, Nishat Mills Limited (NML), Nishat Chunian Limited (NCL), Azgard 9 (ANL) and Kohinoor Textile Mill (KTML). Based on our discussion with these companies, only KTML has its export revenues denominated in Euro while the rest use US$ as their foreign transaction currency. KTML does not use currency hedging, and therefore, we believe the impact of this Euro depreciation would be reflected in its earnings.

On the contrary, this depreciation can be also advantageous for companies having Euro denominated loans. ANL is such an example in our sample selection, with a ~€7mn loan (original amount €15mn) on its book and would definitely benefit from both lower interest payments and revaluation gains. Similarly, PKR's 1.3% YTD depreciation against the US$ will benefit companies that are earning export revenues in the latter currency.

Company	Export sales % of T.Sales	% of T.Exports to Europe
NML	82%	37%
NCL	80%	15%
ANL	84%	70%
KTML	65%	20%

Source: JS Research & Company accounts

** approximate % values*

Outlook: 'Over-weight' maintained

The textile sector has performed commendably during the current fiscal year owing to high cotton and yarn prices. However, on account of better crop estimates and price rationalisation of cotton and yarn, we expect the spinning segment's (top performer during FY10) margins to be squeezed, going forward. Nevertheless, we can see home textile segment to be amongst the top performers in the future. At current levels we continue to like NML and NCL, not only due to their sound business models, but their investments in the power sector as well. The scrips currently trade at FY11F PEs of 5.4x and 4.2x respectively, and we reiterate our 'Buy' call on both the stocks.

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Also in focus

Broadband subscribers rise to 772k

Broadband subscribers as of March have risen to 772k, growing by a significant 87% in the current fiscal year. In March alone, operators saw an addition of another 56k to the total. DSL continues to be the leading technology, as subscribers rose to 434k, up from 263k in June 2010. WiMax retains its second position, as subscribers have jumped a massive 159% to 229k since the beginning of the fiscal year. Moreover, cellular subscribers rose by 0.55% or 535k in Apr to cumulatively reach 97mn. Mobilink was the clear winner of the month, as it gained 255k subscribers, increasing its market share to 32.6%. Telenor too witnessed its market share rise to 24.1%, with 176k new additions in Apr. With these developments, cellular teledensity has inched up to 59.4%.

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