

March 08, 2010

Pakistan Market**MORNING BRIEFING**
NCL: Gateway to Pakistan's textile export potential

KSE100 Index: Closing 9626.29 ↑ (+114.76)

We initiate our coverage on Nishat Chunian Limited (NCL) with a 'Buy' stance and a target price of Rs21 per share. The company's fundamentals appear to be strong as the government's focus has shifted towards increasing textile exports, reflective from the latest textile policy and continued efforts in acquiring Generalised System of Preference (GSP) plus status from the EU. Therefore, we expect NCL to achieve a 3-year (FY10-13) revenue CAGR of 11.7%. Resultantly, the stock outperformed the market by 79% since July 2009. Interestingly, even after the price surge, NCL is available at FY11E PBV of 0.6x which is at a deep discount of 55% to the market. Our optimism for NCL is also driven by the company's 57.8% equity investment in Nishat Chunian Power (NCPL) which is expected to provide a stable dividend stream post FY11. The key risks to our thesis are: (1) Delay in the commissioning of 200MW power plant & (2) Slowdown in the EU's economy, post economic fallout of Greece.

Recent initiatives reflect GoP's focus on textiles

Since Pakistan's export meltdown in 2008, the government renewed its interest in the textile sector evident from its efforts to acquire greater market access in EU and the textile policy (Aug 2009). In the past six months, the government has made serious efforts to acquire a GSP plus status from the EU. The probability of achieving this status is very high as Pakistan was successful in negotiating a removal of anti dumping duty last year. The government also resumed drawbacks of 1%, 2%, and 3% on fabrics, home textiles and garments, respectively. These initiatives will augur well for export oriented entities like NCL.

NCPL to bolster earnings

A major addition to NCL's business profile is the addition of a 200MW power plant (RFO) which is due to come online in June 2010. According to our estimates, this investment would contribute dividend income worth of Rs213mn (EPS impact of 1.54 per share) in FY13, ultimately reducing the company's earnings volatility, as 24% of the total income would comprise

these dividends in FY13.

Focus on value addition to boost revenues

We expect NCL's top line to register a 3-year (FY10-13) CAGR of 11.7%, predominantly on the back of higher proportion of home textile exports. Given the hike in cotton prices, NCPL's sales were skewed towards yarn exports in 1HFY10, a trend which is likely to continue in the second half of FY10 as well. However, amid expectations of improved international cotton supplies and in turn comparatively low cotton prices in FY11, NCL is likely to focus more on the value added segment. This will also help contain pressure on margins.

Valuation: attractive upside of 14%

Using the FCFE methodology with a cost of equity (Ke) of 15.8% and terminal growth of 3%, our sum of the parts (SoTP) target price of NCL arrives at Rs21 per share. NCL's valuation from core operations stands at Rs13 per share, whereas Rs8 per share is contributed by the power arm. Hence, we recommend 'Buy' on the scrip which currently trades at FY12E PE and PBV of 4.4x and 0.6x respectively, which is at a 30-51% discount to the market.

NCL - Key Statistics

	FY10E	FY11F	FY12F
EPS (Rs)	1.5	2.4	4.1
PE (x)	12.5	7.5	4.4
Div. yield (%)	5.4%	5.4%	6.8%
PBV (x)	0.6	0.6	0.6
ROE (%)	5%	9%	14%

Source: JS Research

For more details please refer to our detailed report titled "NCL: Gateway to Pakistan's textile export potential".

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Also in focus
NEPRA raises power tariff by Rs1.02 per Kwh

As per a notification, Nepra has allowed the power distribution companies to raise power tariffs by Rs1.02 per Kwh, mainly on account of a fuel adjustment charge. We believe, this would lead to incremental revenue of Rs40bn on an annualized basis, which could slow down the accumulation of the energy sector's circular debt.

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