

March 24, 2010

Pakistan Market**DGKC: Earnings revised down / 'Buy' intact****MORNING BRIEFING**

KSE100 Index: Closing 9963.35 ↓ (-37.58)

DG Khan Cement (DGKC) reported profits of Rs470mn (diluted EPS of Rs1.29) in 1HFY10, up 270% from Rs127mn (diluted EPS of Rs0.35) earned in the corresponding period last year. The company also announced a right issue of 20% at Rs20 (a premium of Rs10) with the results. Lower financial costs and absence of exchange losses were the primary catalysts for the growth in profitability. However, for 2QFY10, DGKC reported a loss of Rs115mn (diluted loss per share of Rs0.31) owing to subdued margins during the period.

As a result, we have revised down our FY10E and FY11F earnings estimates to Rs2.19 and Rs3.51/share (fully diluted) and arrive at a post right target price of Rs37. With the scrip still offering a potential upside of 26% to our revised target price and trading at a FY11F PBV of 0.3x, we maintain our 'Buy' stance.

1HFY10: Earnings grow despite lower margins

Net sales for the company registered a decline of 8% on account of 30% decrease in retention prices, despite 32% higher volumetric sales during the period. Hence, the gross margin slipped 855bps to 21.4%, regardless of the 22% lower COGS/bag amid lower coal prices. However, substantial reduction in distribution (52%) and finance costs (34%) along with absence of exchange losses during the period helped enhance the bottom-line.

As a result the company reported net earnings of Rs470mn (diluted EPS of Rs1.29) in 1HFY10, a growth of 270% from the corresponding period last year.

2QFY10: Weak margins drag earnings into the Red

Substantially weak margins (down 1,846bps to 11.5%) on account of lower retention prices pulled down gross profit by 70%YoY to Rs388mn in 2QFY10. Hence, despite lower operating and financial costs, the company reported a net loss of Rs115mn (diluted EPS of Rs0.31) during the period.

1HFY10 Financial Highlights

(Rs mn)	1HFY10	1HFY09	Δ%
Net Sales	7,958	8,652	-8%
Gross Profit	1,705	2,594	-34%
Gross Margin	21.4%	30.0%	
Administration & Distribution exp	605	1,156	-48%
Finance cost	956	1,457	-34%
Other operating income	471	432	9%
Other operating expenses	140	658	-79%
(Loss)/Profit Before Taxation	475	(246)	NM
Profit After Taxation	470	127	270%
Diluted earnings per share (EPS)	1.3	0.3	270%

Source: Company accounts

Recommendation: 'Buy'

We have revised our FY10E and FY11F earnings to Rs2.19 and Rs3.51/share, respectively on the back of a lower than expected 2QFY10 result announcement. Hence, our target price for the scrip arrives at Rs37 adjusted for the 20% rights issue announced by the company for funding its Waste Heat power generation and Refused Drive Fuel (RDF) projects. Waste Heat Recovery project is likely to reduce power costs in the range of 25-30%.

Gradual recovery in local prices, an anticipated rise in domestic demand and higher than expected export sales, endorse our bullish view on the sector's fundamentals. With the scrip offering a likely upside of 26% to our revised target price and trading at a FY11F PBV of 0.3x, we reiterate our 'Buy' call.

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Also in focus**FBR to recover Rs134mn in tax refunds from WTL**

According to news reports, the Federal Board of Revenue (FBR) is yet to recover Rs337mn from four pay phone companies in relation to illegal claim's on account of excise duty refunds. FBR has already recovered Rs34mn out of the total amount of Rs371mn from Worldcall Ltd, Dancom (Pvt) Ltd, Global Telecom and Unicom Communication Ltd. The recovery of this amount has been due for some time, with FBR expected to take strict action this time around. Remaining claims on Worldcall total Rs134mn, which we estimate can cause an adverse EPS and cashflow impact of Rs0.16/share.

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