

January 27, 2009

Pakistan Market**FFC: Result preview / 'Buy' maintained****MORNING BRIEFING**

KSE100 Index Closing 4815.34 ↓ (-114.21)

Another important company, Fauji Fertilizer Company (FFC), will be announcing its full year 2008 results on Jan 29, 2008. We expect the company to post an EPS of Rs14.3 per share, an increase of 31%. Looking at the current market conditions, we like FFC due to its high dividend pay out ratio and low business risk. We maintain our 'Buy' recommendation on the stock.

FFC 2008 EPS likely at Rs14.3

FFC took full advantage of farmers substitution from DAP to urea fertilizer as DAP prices increased drastically in the local market. FFC's urea volumetric sales increased by 2% in the period under review and stood at almost 1.8mn tons. However major increase in top line will come from higher urea prices. Weighted average ex-factory urea prices (after removing tax) in 2008 stood at Rs581 per bag as compared to Rs486 per bag in 2007, up by 19.5%. Both these factors are expected to considerably increase the revenues for the company by around 8%.

We expect gross margins to improve by 700 bps to 43% and earnings to depict a considerable growth of 31% (or 32% verify) to Rs7.0bn (EPS Rs14.3) compared to Rs5.4bn in 2007. Along with the results, we expect company to announce Rs3.5 per share cash dividend in addition to cumulative dividend of Rs10.5 per share announced in the first three quarters. This will take full year dividend to Rs14.0 per share.

| Rs mn | 2008E | 2007 | % Δ |
|----------------------|---------------|---------------|-----|
| Net Sales | 30,562 | 28,429 | 8% |
| COGS | 17,309 | 18,312 | -5% |
| Gross Profit | 13,253 | 10,117 | 31% |
| <i>Gross Margins</i> | 43% | 36% | |
| Operating Profit | 10,680 | 7,699 | 39% |
| Profit Before Tax | 10,658 | 7,815 | 36% |
| Tax | 1,527 | 1,011 | 51% |
| Profit After Tax | 7,037 | 5,361 | 31% |
| EPS (Rs) | 14.3 | 10.9 | 31% |

Source: JS Research

Recommendation: 'Buy' maintained

Due to guaranteed offtake amid urea shortage in the country, Pakistan being an agricultural economy and government having pro agriculture policies, business risk is low in case of FFC. In addition, since FFBL has announced Rs2.25 per share dividend for 2008, the risk of FFC's dividend income declining in 2009 is now aside. However, the risk of no dividends by FFBL during 2009 still remains which can affect earnings of 2010 for FFC. Moreover, the company at present is trading at 2008E dividend yield and PE of 20.2% and 4.6x respectively. The dividend yield is much higher than the market's dividend yield of 14.8% for FY09. Hence, we advise investors to accumulate FFC at current levels.

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| Fauji Fertilizer Company | |
|--|----------------------------------|
| Market Price: Rs76.71 | Kats Code: FFC |
| Market Cap: Rs37.9bn (US\$479mn) | Bloomberg Code: FFC PA |
| 1-yrs Avg. Daily Volume: 1.4mn shares, Rs170mn (US\$2.2mn) | Reuters Code: FAUF.KA |
| 1-year High/Low: Rs147.90/57.11 | |

Also in focus**Fall in inflation to lead SBP to cut interest rates**

Finance Advisor Mr. Shaukat Tarin has reiterated that with a declining trend in CPI inflation, pressure on interest rates would ease, which would propel State Bank (SBP) to cut interest rates going forward. While CPI inflation has seen a downward trend it is still hovering around 23.3% (Dec 2008) with core inflation at 18.9%, hence any rate cut in Jan 2009 policy seems unlikely. We expect CPI to fall below 15% in April 2009, which could trigger a rate cut by SBP in 2Q or 3Q 2009. Our full year CPI forecast for FY09 stands at 20%.

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