

Day Break

Thursday, 28 July 2016

Company Update

Engro Foods Ltd.

Food & Personal Care Products

Recommendation	BUY
Target Price	166.4
Last Closing	146.0
Upside	14%

Market Data

Bloomberg Tkr.	EFOODS PA
Shares (mn)	766.6
Market Cap (PKRbn USDmn)	111.9 1,067.3
Exchange	KSE 100

Price Info.	90D	180D	365D
Abs. Return	(5.8)	3.6	(13.7)
Low	144.9	119.5	119.5
High	170.8	170.8	175.2

Key Company Financials

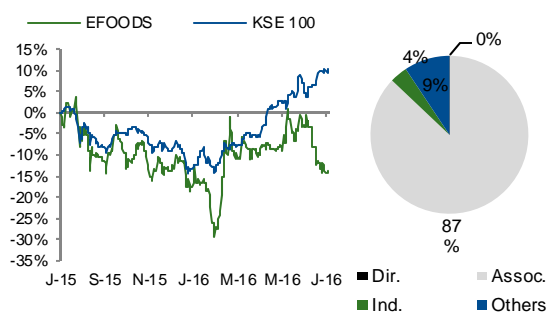
Period End: Dec

PKRbn	CY15A	CY16E	CY17F	CY18F
Total Revenue	43.0	49.8	53.2	58.7
Net Income	0.9	3.2	3.8	4.2
EPS (PKR)	1.2	4.1	4.9	5.5
DPS (PKR)	-	-	-	-
Total Assets	25.8	26.3	27.9	29.8
Total Equity	11.6	14.9	18.7	22.9

Key Financial Ratios

ROE (%)	8%	21%	20%	19%
P/E (x)	125.8	35.4	29.7	26.3
P/B (x)	9.7	7.5	6.0	4.9
DY (%)	-	-	-	-

Relative Price Performance & Shareholding



About the Company

The Company is a public limited company incorporated in Pakistan. The principal activity of the Company is to manufacture, process and sell of dairy, beverages, and frozen desserts.

Source: Bloomberg, KSE 100 & IGI Research

Analyst

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Engro Foods Limited

Profitability to go down by 25%YoY in 2QCY16 to PKR 0.86/share

- Engro Foods (EFOODS) is scheduled to announce its 2QCY16 financial result on 29th Jul-16. We expect earnings to drop by 25%YoY to PKR684mn (EPS PKR 0.89) in 2QCY16, as compared to PKR 909mn (EPS PKR 1.19) reported in the same period last year.
- Friesland Campina entering into Sale and Purchase Agreement (SPA) with ENGRO to buy 51% stake in Efoods is game changer for the company, we believe. With Acquirer Company's vast and rich experience in dairy business, we think Efoods will likely go through a phase of changing business model in next few quarters.
- The scrip is currently trading at CY16E P/E of 35.4x and with our Dec-16 TP of PKR 166/share, the stock offers upside of +14%, hence we maintain 'Buy' call on the scrip.

Earnings to clock in at PKR 0.89/share in 2QCY16

Engro Foods (EFOODS) is scheduled to announce its 2QCY16 financial result on 29th Jul-16. We expect earnings to drop by 25%YoY to PKR684mn (EPS PKR 0.89) in 2QCY16, as compared to PKR 909mn (EPS PKR 1.19) reported in the same period last year. We calculate gross margin to hover around 24% in 2QCY16 as compared to 25% in 2QCY15. We attribute this feeble performance to fierce competition in UHT milk and Tea Whitener segment, affecting volumetric growth and propensity to price.

However, financial charges are likely to drop by 53%YoY to PKR 129mn in 2QCY16, on the back of timely debt repayments and lower interest rates. As per latest financial statements, company's long term debt has come down to PKR 4.7bn in 1QCY16 from PKR 5.2bn in 4QCY15. Efoods is also foreseen to account for 3% super tax liability in 2QCY16, taking effective tax rate to 41%.

For the 1HCY16, we anticipate Efoods' profitability to decline by 9%YoY to PKR 1.8bn (EPS PKR 2.34). Margins on the other hand is expected to remain at same level despite decline in international skim milk prices, lower power costs and milk price increase in Jun-16.

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Exhibit: Financial Highlights

PKR mn	2QCY16E	2QCY15	YoY	1HCY16E	1HCY15	YoY
Revenue	10,966	12,322	-11%	22,709	24,898	-9%
Gross Profit	2,607	3,098	-16%	5,911	6,532	-10%
Selling and Admin	1,283	1,606	-20%	2,867	3,182	-10%
Financial Charges	129	272	-53%	231	539	-57%
PBT	1,163	1,554	-25%	2,717	2,734	-1%
Tax	479	265	80%	925	757	22%
Net profit	684	909	-25%	1,792	1,978	-9%
EPS	0.89	1.19		2.34	2.58	
Key Ratios						
Gross Margin	24%	25%		26%	26%	
Net Margin	6%	7%		8%	8%	
Effective Tax Rate	41%	17%		34%	28%	

Source: IGI Research, Company Financials

Outlook

FrieslandCampina entering into Sale and Purchase Agreement (SPA) with ENGRO to buy 51% stake in Efoods is game changer for the company, we believe. With Acquirer Company's vast and rich experience in dairy business, we think Efoods will likely go through a phase of changing business model in next few quarters. However, it can't be quantified at this point in time, so we await further management disclosure on the transaction and process.

Recommendation

The scrip is currently trading at CY16E P/E of 35.4x and with our Dec-16 TP of PKR 166/share, the stock offers upside of +14%, hence we maintain '**Buy**' call on the scrip.

Analyst Certification

The analyst[^] hereby certify that the views about the company/companies and the security/securities discussed in this report are accurately expressed and that he/she has not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report. The analyst is principally responsible for the preparation of this research report and that he/she or his/her close family/relative does not own 1% or more of a class of common equity securities of the following company/companies covered in this report.

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Rating system

IGI Finex Securities employs three tier ratings system, depending upon expected total return (return is defined as capital gain exclusive of tax) of the security in stated time period, as follows:

Recommendation	Rating System
Buy	If return on aforementioned security(ies) is more than 10%, from its last closing price(s)
Hold	If return on aforementioned security(ies) is in between -10% and 10%, from its last closing price(s)
Sell	If return on aforementioned security(ies) is more than -10%, from its last closing price(s)

Valuation Methodology

The analyst[^] has used following valuation methodology to arrive at the target price of the said security (ies):

- FCF (Free Cash Flow)

Time Horizon

- Dec-16

Risk

- Changes in State Bank of Pakistan Policy Rate
- Changes in country (Pakistan) macro-economic environment
- Changes in Company(ies) operating structure

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