

## Company Update

### Engro Fertilizer Limited

Fertilizer

<b>Recommendation</b>	<b>BUY</b>
Target Price	97.0
Last Closing	79.0
Upside	23%

#### Market Data

Bloomberg Tkr.		EFERT PA	
Shares (mn)		1,330.9	
Market Cap (PKRbn   USDmn)	105.1	1,010.0	
<b>Price Info.</b>	90D	180D	365D
Abs. Return	(4.2)	(16.2)	(8.8)
Low	77.0	77.0	70.9
High	86.2	99.4	99.4

#### Key Company Financials

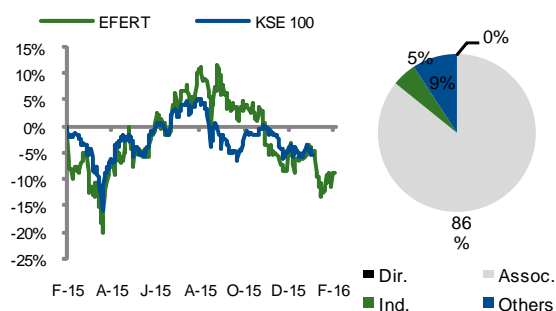
Period End: Dec

PKRbn	CY14A	CY15E	CY16F	CY17F
Total Revenue	61.4	87.6	82.5	90.9
Net Income	8.2	15.0	11.0	15.4
EPS (PKR)	6.2	11.3	8.2	11.6
DPS (PKR)	3.0	6.0	3.3	4.8
Total Assets	111.5	102.6	97.4	101.1
Total Equity	34.5	42.5	49.1	58.1

#### Key Financial Ratios

ROE (%)	24%	35%	22%	27%
P/E (x)	12.8	7.0	9.6	6.8
P/B (x)	3.0	2.5	2.1	1.8
DY (%)	3.8	7.6	4.2	6.1

#### Relative Price Performance & Shareholding



#### About the Company

The Company is a public limited company incorporated on June 29, 2009 in Pakistan as a wholly owned subsidiary of Engro Corporation Limited. The principal activity of the Company is manufacturing, purchasing and marketing of fertilizers.

Source: Bloomberg, KSE 100 & IGI Research

Analyst

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## Engro Fertilizers

### Weak Urea Prices to Deteriorate Profitability in CY16

- Engro Fertilizers (EFERT) posted remarkable +83%YoY growth in its profitability to PKR 15.03bn (EPS PKR 11.29) in CY15 compared to PKR 8.21bn (EPS PKR 6.17) in same period last year. Company also announced a final cash dividend of PKR 3.00/share, taking the full year payout to PKR 6.00/share.
- Despite expiration of 60mmcf contract in Dec-15, company continues to receive the said quantum of gas.
- With recent decline in international Urea prices, we consider local Urea fertilizer prices are likely to come under pressure. Gas price increase which took place in Sept-15, forced the manufacturers to take a hit on margins despite the efforts to pass on the impact to farmers.
- We have revised our earnings forecasts downward based on feeble urea prices and expected decline in DAP prices as well. Our Dec-16 TP has also been revised down from PKR 116/share to PKR 97/share, which provides an upside of +23% from its last close. Thus we recommend a Buy call on the scrip.

#### Profitability augmented by +83%YoY to PKR 11.29/share in CY15- DPS PKR 6.00/share

Engro Fertilizers (EFERT) posted remarkable +83%YoY growth in its profitability to PKR 15.03bn (EPS PKR 11.29) in CY15 compared to PKR 8.21bn (EPS PKR 6.17) in same period last year. Company also announced a final cash dividend of PKR 3.00/share, taking the full year payout to PKR 6.00/share, which is +100%YoY jump compared to dividend of PKR 3.00/share last year.

The extraordinary financial performance of the company is attributed to a) +3%YoY increase in urea offtake, b) 70 cents gas provision for Enven Plant from 2QCY15, c) continued flow of 60mmcf gas to new urea plant, d) PKR 300/bag subsidy announced in Oct-15, and e) 31%YoY decline in finance cost due to lower interest rates and debt prepayments. However, other income declined due to drop in cash balances as company made due GIDC payments to government in 1HCY15.

Earnings augmented by +90%YoY in 4QCY15 to PKR 5.12bn (EPS PKR 3.85), however gross margins declined to 32% as compared to 37% in 4QCY14, due to lower urea prices despite the gas hike in Sept-15.

**Exhibit: Financial Highlights**

PKR mn	CY15	CY14	YoY	4QY15	4QCY14	YoY
Revenue	87,615	61,425	43%	35,687	17,733	101%
Gross Profit	32,180	22,603	42%	11,477	6,687	72%
Selling and Distribution	5,453	4,441	23%	2,265	1,378	64%
Other Income	1,707	2,449	-30%	268	-162	-265%
Finance Cost	4,588	6,625	-31%	1,028	1,664	-38%
Profit before Tax	21,169	11,895	78%	7,557	3,722	103%
Tax	6,141	3,687	67%	2,434	1,025	137%
Profit after tax	15,027	8,208	83%	5,123	2,697	90%
EPS	11.29	6.17		3.85	2.03	
DPS	6.00	3.00		3.00	3.00	
<b>Key Ratios</b>						
Gross Margin	37%	37%		32%	38%	
Net Margin	17%	13%		14%	15%	
Effective Tax Rate	29%	31%		32%	28%	

Source: IGI Research, Company Financials

**Gas Availability Expected to Continue**

Despite expiration of 60mmcf contract in Dec-15, company continues to receive the said quantum of gas. Regardless of absence of any firm commitment by government to continue the gas flow to EFERT for foreseeable future, the company anticipates to receive newly discovered gas by Mari network, later in the year. Our base case assumption incorporates continuation of 60mmcf gas in CY16 and onwards.

**Bleak Urea Pricing Power**

With recent decline in international Urea prices, we consider local Urea fertiliser prices are likely to come under pressure. Gas price increase which took place in Sept-15, forced the manufacturers to take a hit on margins despite the efforts to pass on the impact to farmers. In our view a USD 20-30/ton further decline in international urea prices can aggravate pricing pressure on domestic producers. Currently MRP is hovering around PKR 1,860/bag; we anticipate a drop would be required in prices to augment sales due to weak commodity prices and weaker farm economics.

**Recommendation**

We have revised our earnings forecasts downward based on feeble urea prices and expected decline in DAP prices as well. Our Dec-16 TP has also been revised down from PKR 116/share to PKR 97/share, which provides an upside of +23% from its last close. Thus we recommend a **Buy** call on the scrip.

### Analyst Certification

The analyst<sup>^</sup> 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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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<sup>^</sup> has used following valuation methodology to arrive at the target price of the said security (ies):

- Free Cash Flow (FCF)

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
- Gas shortage
- Gas Price Hike
- Decline in International Urea Prices

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