Equity Research Pakistan

In Focus

Fertilizer

Overweight

ENGRO- BUY

TP Dec-12: PKR 231

Current Price: PKR 134

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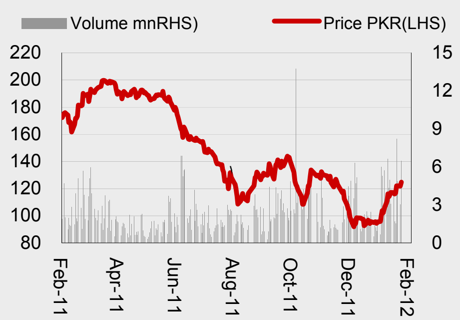
Stock Statistics

Ticker		**ENGRO**
Mkt Cap	USD mn	586
12M ADT	mn shares	2.3
Shares Outstanding	mn	393

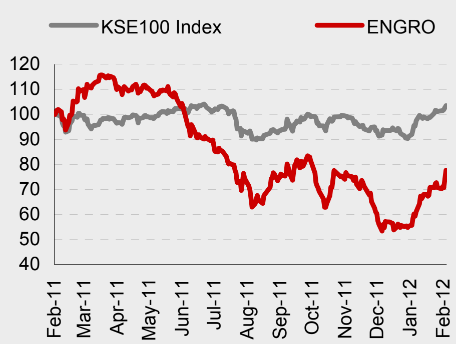
Stock Performance

	1M	3M	12M
Absolute %	40%	2%	-22%
Relative to KSE %	27%	-2%	-26%

Price and Volume Graph



Engro vs KSE100 Relative Index Chart



ENGRO: Analyst Briefing Takeaways

- **ENGRO reported top line growth of 43% primarily driven by the new urea plant in Fertilizer business and 22% volumetric growth in UHT milk segment of Foods business**
- **The management disclosed that ENGRO made gross debt repayment of PKR11.2bn in CY11, with Fertilizer business retiring PKR6.0bn. ENGRO is on track to retire over PKR16bn of debt on gross level in CY12, of which PKR10bn will be paid off by the Fertilizer business**
- **Current urea price incorporates 5 to 6 months of gas supply at EnVen 1.3 for CY12. ENGRO expects gas to resume in mid Mar12 post winter shutdown**
- **Engro Foods has planned a capital expenditure of ~PKR6bn in CY12. The company will procure subordinated loan of PKR3bn from ENGRO**
- **ENGRO has decided to move out of automation business by divesting its interest in Avanceon and has recognized entire investment as impaired in its CY11 statements**
- **We have a BUY call on ENGRO with our Dec12 TP for the company standing at PKR231/share**

Engro Corp. (ENGRO) held its analyst briefing on Friday to discuss its CY11 results. The company reported revenues of PKR114.6bn, up 43% YoY, and PAT of PKR8.06bn, recording a YoY growth of 19%. The top line growth was primarily driven by new urea plant in Fertilizer business and 22% volumetric growth in UHT segment of Engro Foods.

Debt Retirement: Putting all concerns to rest

The management disclosed that ENGRO made gross debt repayment of PKR11.2bn in CY11, with Fertilizer business retiring PKR6.0bn. However, Engro Foods and EXIMP remained the net borrowers to finance their respective expansion projects in UHT milk, ice cream and rice segments. Subsequently after these gross retirements, company's Debt to Equity has come down to 71% compared to 75% in CY10.

The management further informed that ENGRO will retire over PKR16bn of debt in CY12 from which PKR10bn will be paid off by fertilizer business.

Fertilizer: At the heart of growth…

Amid gas curtailment issues Engro's new plant effectively produced at 33% capacity in CY11. Thus urea price hikes and additional urea volumes from the new plant led the net sales of the company to increase by hefty 65% to PKR31.4bn. EnVen contributed 440k tons (34%) to total urea volumes for the company, having been shut down for 220 days in the year. Thus, PAT for fertilizer business clocked in at PKR4.6bn, up 23% YoY.

The management disclosed, in line with our estimates, that the current urea price incorporates 5 to 6 months of gas supply at EnVen 1.3 for CY12. ENGRO expects gas to resume in mid-Mar12 post winter shutdown.

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Rice: Expansion to lead to breakeven

Rice business posted revenue growth of 2.6x to 1.6bn and loss after tax of 805mn. This loss was higher than anticipated because of delays in commissioning of new plant. The company is near completion of expanding capacity to 120k tons of wet paddy from 56k tons previously. The business will continue to focus on expanding volumetric sales and stabilizing plant operations to gain economies of scale.

Foods: UHT volumes drive growth

Engro Foods reported bottom line growth of 4.1x to PKR891mn, primarily driven by 22% rise in UHT volumes. UHT segment reported bottom line of PKR1.4bn, with strong contribution from Tarang and Omung whereas Olpers continued to perform well, management disclosed. Moreover, Ice cream revenues increased by 62% to PKR2.6bn, driven by 43% volumetric growth to 47.9k liters per day. However ice cream segment reported loss of PKR405mn due to continuous infrastructure development expenditure.

Engro Foods has planned a capital expenditure of ~PKR6bn in CY12. The company will procure subordinated loan of PKR3bn from ENGRO.

Polymer & Chemical: Stable VCM operations key to profits

VCM plant operations for Engro Polymer & Chemical (EPCL) have stabilized post Oct11, which enabled the company to export excess VCM of 3ktons in 4QCY11. The company reported loss of PKR770mn in CY11 due to unstable VCM operations in 9MCY11 and bottoming out of integrated margins and sharp PKR devaluation against USD in 4QCY11. However, since then the integrated margins are returning to stable. Continued stable VCM plant operations hold the key to profitability, which is the key focus of management.

A subordinated long term loan of PKR1bn will be provided by ENGRO to EPCL to replace a PKR950mn loan to be repaid to banks in lump sum this year.

Other businesses continue to support earnings

The power business achieved load factor of 90% v/s 83% last year and dispatched 1,657GWh power. The business reported net profit of PKR1.7bn. Engro VOPAK took a one time gain of PKR2bn (of which 1bn is reflected in ENGRO's earnings) due to a tax reversal. Keeping the one time gains aside, recurring earnings grew by 32% to PKR1.4bn.

Goodbye to Automation business

Engro has decided to move out of automation business by divesting its interest in Avanceon. ENGRO has recognized as impaired its equity investment and subordinated loan to Avanceon on its standalone accounts. Therefore, no future impact of losses from Avanceon will appear on ENGRO books.

Outlook: BUY with Dec12 TP of PKR231

Our Dec12 TP for ENGRO stands at PKR231/sh, representing a 72% upside from current levels. We have a BUY call on ENGRO stemming from our expectation of earnings to bottom out in 1QCY12 and significant growth post resumption of gas supply to EnVen in Mar-Apr12.

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Glossary

- *TP: Target Price*
- *EPS: Earning per share*
- *PER: Price to earnings ratio*
- *PBV: Price to Book ratio*
- *DY: Dividend Yield*

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