

Fertilizer Sector Update

FERTILIZER SECTOR KEY DATA

Sector PE	11.55
Sector Market Cap (Full OS)	578,512,705,981
Sector Market Cap (Full FF)	274,510,569,344
Avg Daily Volume (From: Jan 2018)	5,903,660
Sector Float	37.44%
KSE100 Market Cap (FF)	1,991,770,655,112
Fertilizer Sector Weightage	13.78%
Sector Price to Book	35.33

Jan 2018 to Date

Sector Return	14.78%
Index Return	2.83%

Source: PSX, Company Financials, DSL Research

PAKISTAN FERTILIZER OFF-TAKE (JULY 2018)

INDUSTRY

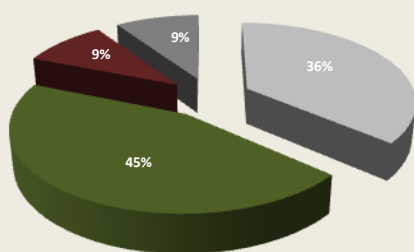
'000 Tons	7M-CY'18	7M-CY'17	YoY %
UREA	3,225	3,040	6%
DAP	984	873	13%
NP	305	414	-26%
CAN	429	445	-4%
NPK	35	39	-11%
TOTAL	5,061	4,882	4%

Company	Exports	Market share
EFERT	236kt	39%
FFC	232kt	39%
FATIMA	132kt	22%
Total Allowed	600kt	

Source: Company's Account & DSL Research

7M CY18 Market Share of Urea Off-take

■ EFERT ■ FFC ■ FFBL ■ FATIMA



A "Pressure Tactic" or a "Serious Problem" ?

The matters discussed in the first meeting held by the ECC of the Cabinet on 29th August 2018 turned out to be punitive for the "Fertilizer Sector" as it was believed in the meeting that the fertilizer manufacturers earned PKR 10bn windfalls by exporting urea, taking advantage of the subsidized and regular supply of gas and government's permission to export 300kt of urea which later further increased to 300kt more, making the total export permitted to 600kt. Nevertheless, the meeting remained inconclusive but also tried to shed some light on the discussed summary which demands 600kt urea import to the country for the upcoming Rabi season. Therefore, it was debated that the fertilizer manufacturers had earned PKR 10bn extra "windfall" which now needs to be returned back and eventually passed on to the local farmers.

As per the discussion in the ECC's meeting and impression taken from the meeting, it is believed that the subsidized feed gas availability on urea production was for only local consumption, whereas, the export condition did not specifically mentioned this condition, however, the subsidized feed gas was to maintain price in the local market.

How we understand the situation:

- ❖ DSL views this as a "pressure tactic" used by the government to stabilize urea prices which was recently increase by urea producers.
- ❖ The differentiated amount of subsidized feed gas and the industry's average of feed gas on total industry export of around 600kt of urea translates into PKR ~6bn, where the government's claim stands at PKR 10bn.
- ❖ We also believe that urea export has contributed significantly to the foreign reserves of the country, but that's being said there is also a chance that the government will re-operationalize the three closed plants by providing them subsidized gas rather than importing urea in the long-run.
- ❖ The three plants include Dawood Hercules, Pakarab fertilizers Limited and Agritech (formerly Pak-American Fertilizers Limited). The plan is to supply 28% domestic gas and 72% RLNG to above mentioned plants, which will increase competition within the industry.
- ❖ The discussion in the ECC's first meeting spread like a wildfire and created downward trend in fertilizer sector, but we maintain a "Positive" stance for the sector with our top picks EFERT and FATIMA.

Symbol	Shares (MN)	LDCP	CY17 EPS	P/E	BVPS	Free Float (MN)	Free Float (%)	P/B
FFBL	934	42	1.08	38.86	14.08	327	35%	2.98
FFC	1,272	97	8.42	11.52	23.07	700	55%	4.20
EFERT	1,335	78	7.6	10.23	30.71	601	45%	2.53
FATIMA	2,100	34	5.04	6.65	25.59	315	15%	1.31

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Rating System:

- | | |
|---|---------------------|
| If; | |
| • Expected return >15% | - Buy Call |
| • Expected Return is in between 0% to 15% | - Neutral/Hold Call |
| • Expected Return <0% | - Sell Call |

Valuation Methodology

To arrive at our period end target prices, DSL uses different valuation methodologies including:

- Discounted cash flow (DCF, DDM)
- Justified price to book (JPB)
- Relative Valuation (P/E, P/B, P/S etc.)
- Equity & Asset return based methodologies (EVA, Residual Income etc.)

SECP JamaPunji Portal link: www.JamaPunji.pk

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