Foundation Securities
A Fauji Foundation Group Company
REP-095

PAKISTAN

FSL Fertilizer universe 2QCY21E Profitability Highlights

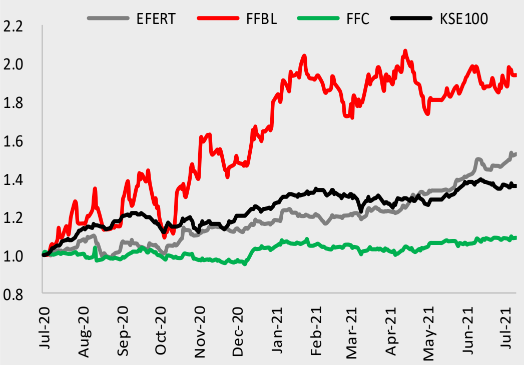
	2QCY21E	2QCY20	YoY	QoQ
FFBL	1.7	(0.2)	N/A	95%
FFC	4.3	3.8	12%	-6%
EFERT	3.2	2.9	11%	-25%

	1HCY21E	1HCY20	YoY
FFBL	2.6	(2.2)	N/A
FFC	8.9	7.2	23%
EFERT	7.5	3.3	126%

Dividend expectations (Rs/sh)	
FFBL	-
FFC	3.5
EFERT	3.0

Source: Company accounts, Foundation Research, July 2021

FSL Fertilizer universe V/S KSE100 Index



Source: Bloomberg, Foundation Research, July 2021

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Pakistan Fertilizer

Better retention prices amid improved liquidity uplifted profitability

Event

- Increased pricing power amid better pricing for wheat and sugarcane crop given constrained supply allowed fertilizer companies to witness ~41% YoY increase in profitability in 2QCY21. We attribute higher profitability to (1) better DAP margins given constrained supply in international markets, (2) ~5% YoY increase in Urea prices, (3) decline in finance cost and (4) higher other income due to strong cash position amid advances from customers and dividend receipts. FFBL would outperform others by posting EPS of Rs1.7/sh in 2QCY21 as compared to loss in 2QCY20.

Impact

- **Better retention prices and improved liquidity to uplift profitability:** FSL fertilizer universe profitability is expected to increase by 41% YoY in 2QCY21. However, universe Urea offtake is expected to decline by 20% YoY (industry offtake declined by 10% YoY) in 2QCY21 due to higher offtake in earlier months given expectation of further gas price hike amid resumption of IMF program. Furthermore, Urea prices increased by 5% YoY in 2QCY21.

- Lower application of phosphate fertilizer in cash crops due to increased landed cost of imported DAP resulted in offtake declining by 34% YoY in 2QCY21 (FSL universe DAP offtake down by 18% YoY). To highlight, domestic DAP prices increased by 62/16% YoY/QoQ in 2QCY21 due to 59% YoY increase in average international prices.

- **FFBL to post highest ever 2Q profit:** We expect FFBL to post EPS of Rs1.7/sh in 2QCY21 as compared to loss in corresponding period last year. FFBL profitability is attributable to (1) better primary margins (up 69% YoY in 2QCY21, (2) higher Urea retention prices, (3) 40% YoY decline in finance cost and (4) lower losses of food businesses. To highlight, FFBL profitability share from AKBL is expected to increase by 48% in 2QCY21 while FFL/FML loss contribution would decrease by 47/12% YoY to Rs0.17/0.19/sh in 2QCY21. Furthermore, PMP is expected to provide contribution of Rs0.25/sh in FFBL profitability as compared to Rs0.2/sh loss contribution in 2QCY20.

- **FFC profitability to increase amid higher Urea retention prices:** Higher DAP offtake and better Urea retention prices would allow FFC to post EPS of Rs4.3 (up/down 12/6% YoY/QoQ) in 2QCY21. To highlight FFC Urea/DAP offtake decreased/increased by ~19/35% YoY in 2QCY21. Furthermore, FFC would benefit from (1) 20% YoY decline in finance cost and (2) dividend income from PMP.

- **Better DAP trading margins to support profitability:** EFERT profitability is expected to increase by 11% YoY in 2QCY21 despite ~22/32% YoY decline in Urea/DAP offtake. To highlight, on sequential basis EFERT profitability would decline by 25% QoQ due to ~9% QoQ decline in Urea offtake. We attribute YoY increase in EFERT profitability to (1) better DAP trading margins (2) ~59% YoY decline in finance cost, (3) higher Urea retention prices and (4) absence of onetime expense.

Outlook

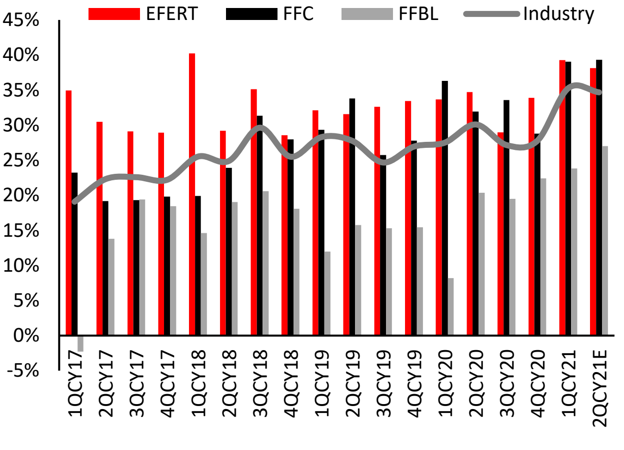
- We have an "Outperform" stance on the sector given government's efforts for food security amid better pricing of wheat and sugarcane. Moreover, payment of GIDC in 48 monthly installments along with likely adjustment of payable amount against Sales tax and subsidy receivables would ease cash flow concerns of FFBL.

Fig 1: Fertilizer sector financial highlights 2QCY21E

Rs(mn)	2QCY21E	2QCY20	YoY	QoQ	1HCY21E	1HCY20	YoY
Net sales	70,620	71,670	-1%	3%	139,108	115,968	20%
COGS	17,407	11,055	57%	103%	25,976	28,856	-10%
Gross profit	**23,597**	**21,572**	**9%**	**-2%**	**47,744**	**33,756**	**41%**
S&A expense	1,240	1,092	14%	-12%	2,650	3,200	-17%
Financial charges	1,392	1,886	-26%	-4%	2,840	4,171	-32%
Other operating expenses	1,144	(414)	-376%	192%	1,536	273	463%
Other operating Income	3,721	3,020	23%	-15%	8,123	6,043	34%
PBT	**16,658**	**12,326**	**35%**	**-10%**	**35,205**	**16,903**	**108%**
PAT	12,012	8,438	42%	-6%	24,791	10,371	139%
PAT att to owners	**11,948**	**8,503**	**41%**	**-6%**	**24,626**	**10,714**	**130%**
GM	**33%**	**30%**			**34%**	**29%**	
NM	**17%**	**12%**			**18%**	**9%**	

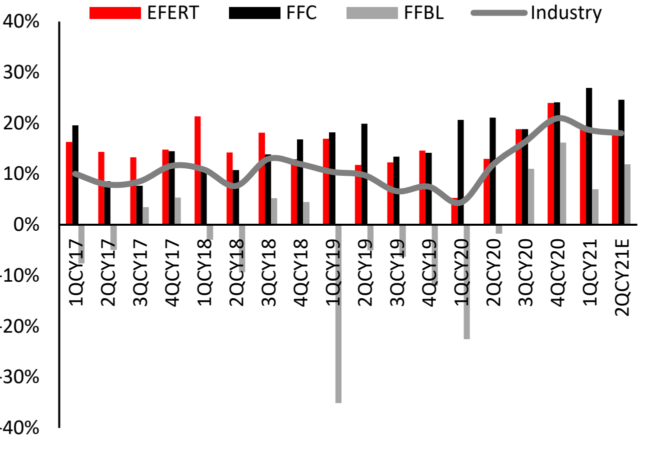
Source: Company Accounts, Foundation Securities, July 2021

Fig 2: FFC gross margins increased to record level….



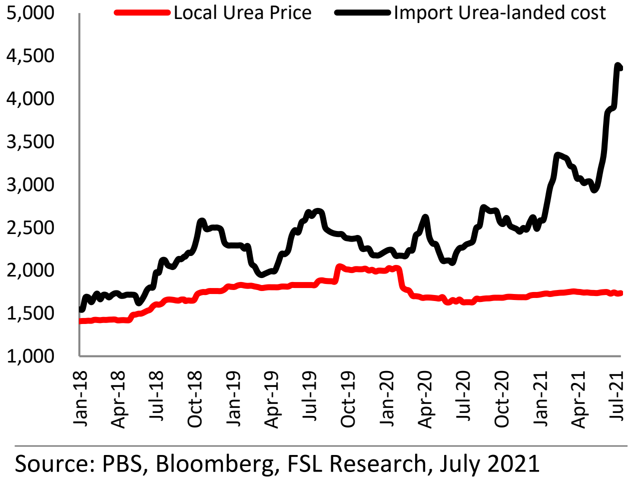
Source: Company acc, FSL Research, July 2021

Fig 3: …..FFC takes the lead in net margins



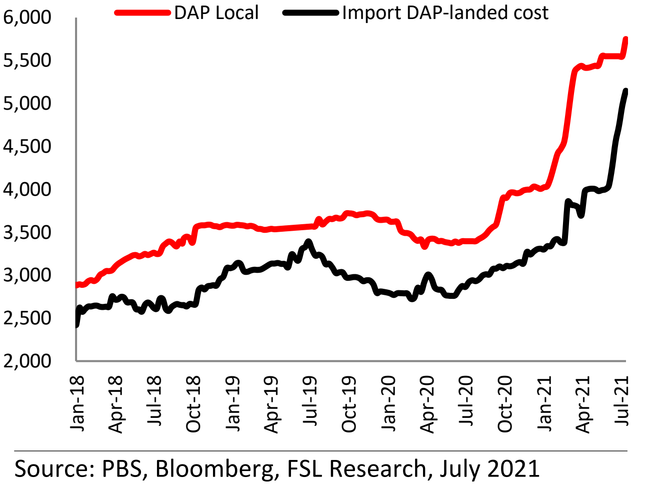
Source: Company acc, FSL Research, July 2021

Fig 4: Local prices still lower than int'l (Rs/bag)



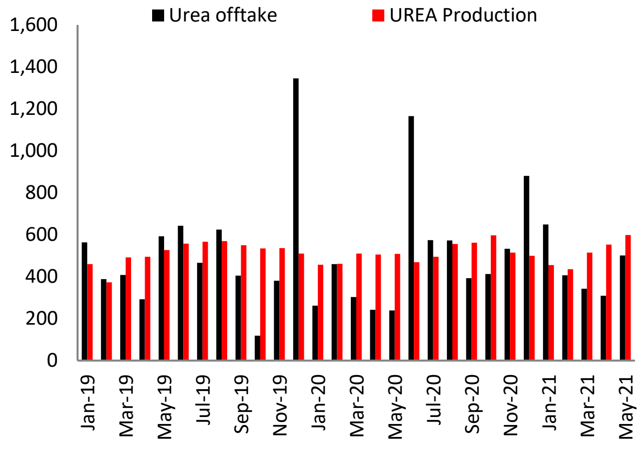
Source: PBS, Bloomberg, FSL Research, July 2021

Fig 5: Lower production by China to support prices



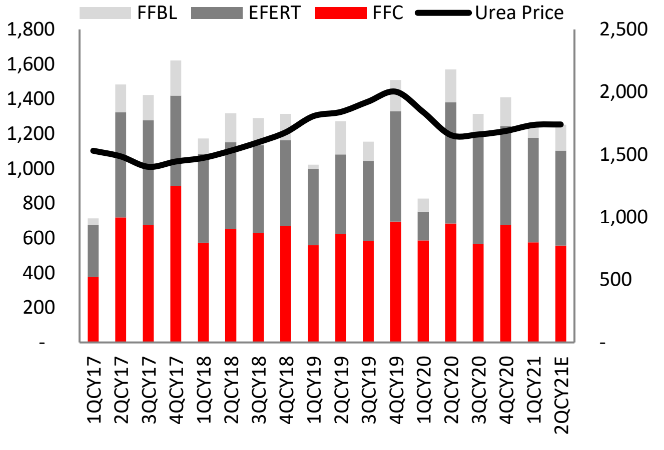
Source: PBS, Bloomberg, FSL Research, July 2021

Fig 6: EFERT production recovered in June (K tons)…



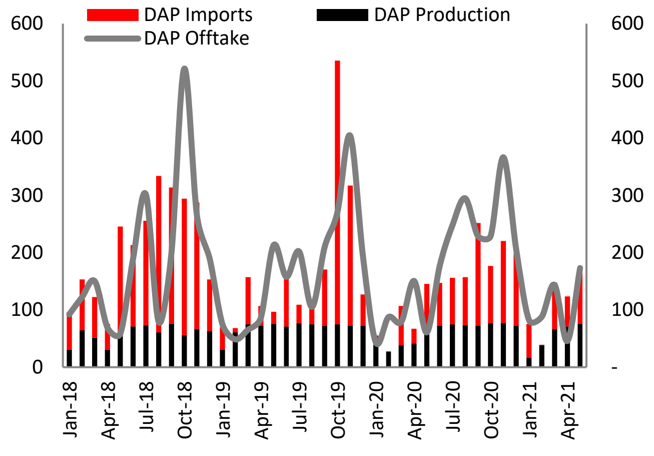
Source: Company acc, FSL Research, July 2021

Fig 7: …EFERT taking lead in Urea offtake growth



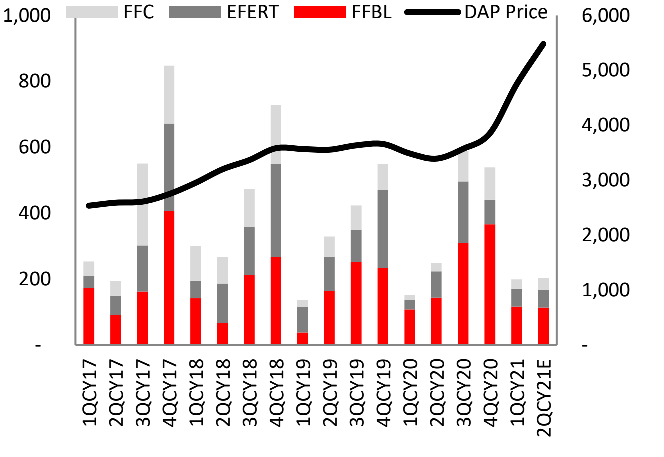
Source: Company acc, FSL Research, July 2021

Fig 8: Lower DAP imports to enhance pricing power



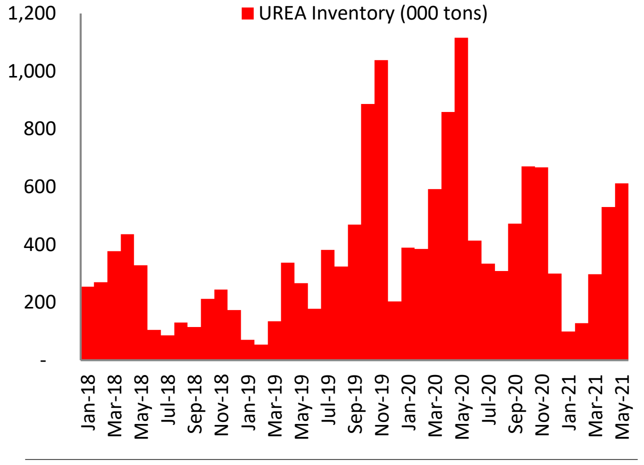
Source: Company acc, FSL Research, July 2021

Fig 9: EFERT/FFC DAP offtake to remain on lower side



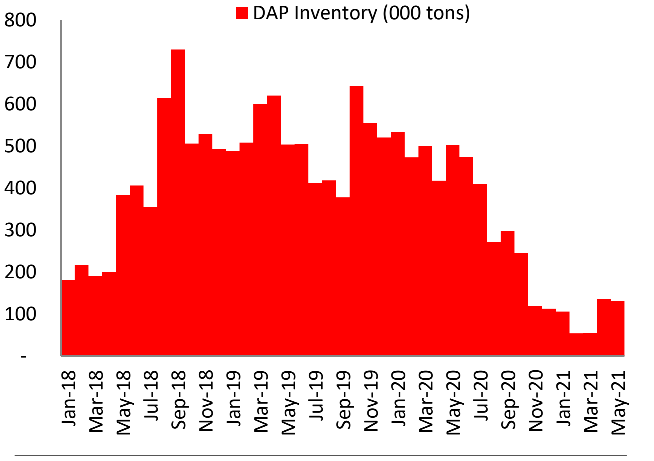
Source: Company acc, FSL Research, July 2021

Fig 10: Inventory to remain on lower side during CY21



Source: Company acc, FSL Research, July 2021

Fig 11: DAP inventory lower given reduced imports



Source: Company acc, FSL Research, July 2021

Abbreviations

CY	Calendar Year
DAP	Di-ammonium Phosphate
FFL	Fauji Food Limited
FML	Fauji Meat Limited
FPCL	Fauji Power Company limited
GIDC	Gas Infrastructure Development Cess
GM	Gross Margin
NM	Net Margin
SPLY	Same period last year
YoY	Year-on-year

Recommendations definitions

If

Expected return >+10%	Outperform.
Expected return from -10% to +10%	Neutral.
Expected return <-10%	Underperform.