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Abdul Samad Khanani

Investment Analyst

abdul.samad@imsecurities.com.pk

+92-21-37131600 – Ext 303

Transfer of coverage

Pioneer Cement Limited

Price (Pkr/sh)	82.12
TP (Pkr/sh)	103.10
Stance	Buy
Upside	25.5%
Fwd D/Y	7.6%
Total Return	33.2%
Bloomberg / Reuters	PIOC PA / PION.KA
Mkt Cap (US\$m)	178.2
52wk Hi-Low (Pkr/sh)	95.04-74.86
3m Avg. Daily Vol ('000 shrs)	420
3m Avg. Traded Val (US\$m)	0.35

Core valuation	96.74
WHR Pkr/share	6.35
Target Price (Pkr)	103.10

PIOC - Valuation Snapshot

	FY15A	FY16F	FY17F	FY18F
EPS (Pkr)	10.99*	10.01	11.26	12.70
EPS Growth (%)	41.1%	-8.9%	12.5%	12.7%
P/E (x)	7.47	8.20	7.29	6.47
PBV (x)	2.24	1.94	1.65	1.32
DPS (Pkr)	6.25	6.25	6.75	7.25
DY (%)	7.6%	7.6%	8.2%	8.8%
ROE (%)	33.0%	25.3%	24.5%	22.7%
EV/EBITDA (x)	5.18	4.87	4.30	3.43

Source: IMS Research

*Liabilities written back worth Pkr567mn, adjusted FY15 EPS is Pkr9.19.

PIOC vs. KSE100 Index & Cement Sector



Source: PSX

Inter Market Pulse

Pakistan Cements

PIOC: Production growth & cost efficiencies to underpin rerating

- We resume coverage of PIOC with a Buy rating and a TP of Pkr103/share, which offers a potential upside of 25.5% along with a DY of 7.6%. We expect EPS of Pkr10.01/11.26 in FY16/17F, along with DPS of Pkr6.25/6.75.
- Improvement in core operations due to (i) uptick in local cement demand, (ii) reduction in power tariffs, and (iii) commencement of WHR (12 MWs by 2HFY17) will be the triggers for PIOC, going forward. Since peak operating levels on Line-I has been as high as 115% (FY05) and 78% on Line-II (FY08), we highlight company's low utilization levels in the last six years was a consequence of demand patterns only.
- PIOC posted 2QFY16 EPS of Pkr2.45, up 7.5%YoY/29%QoQ (ex-liability reversals of Pkr557.8mn booked in 2QFY15), mainly due to (i) 5pptYoY/6pptQoQ rise in GP margins to 42.5%; (ii) 21%YoY growth in off-take (97% were high-margin local sales), and (iii) 69% dip in finance cost due to better liquidity position. PIOC also announced first interim cash dividend of Pkr2.5/share.

Resume coverage with a TP of Pkr103/share

We resume coverage of Pioneer Cement (PIOC), with a Buy rating; our DCF based target price of Pkr103/share offers a potential upside of 25.5%. We believe PIOC is yet to fully capture the fruits of: (i) lower grid power tariffs; (ii) ample unutilized capacity (utilization: 60% in FY15) to cater local demand; and (iii) installation of WHR (expected to commence operations in FY17), which will further boost energy savings. We revise our earnings estimate to Pkr10.01/11.26 in FY16/FY17F, along with DPS of Pkr6.25/6.75. The stock is trading at a FY16F P/E of 8.2x (4.2% discount to peers) and yielding 7.6%.

Lower utilization a matter of demand, not plant's inefficiency

PIOC is currently running at capacity utilization of 63%, which came down from 82% in FY08. The company lost market share in local sales, from 5.9% to 4.1%, amid spree of expansions between FY08-FY12; particularly, Fauji Cement (in close vicinity; now operating at 79%) caused the greatest attrition, in our view. Historically, PIOC has operated its Line I at as high as 115% utilization (FY05), whereas Line II operated at 78% in FY08; which is contrary to concerns on company's ability to produce more. We think modest utilization levels were more an outcome of limited local demand and thus competition and not because of operational inefficiencies obstructing higher utilization levels. Going forward, however, we think the foreseeable uptick in demand given CPEC projects in KPK, will serve to elevate PIOC's utilization levels – in turn driving volume and earnings growth.

Commencement of WHR supporting margins in the long run

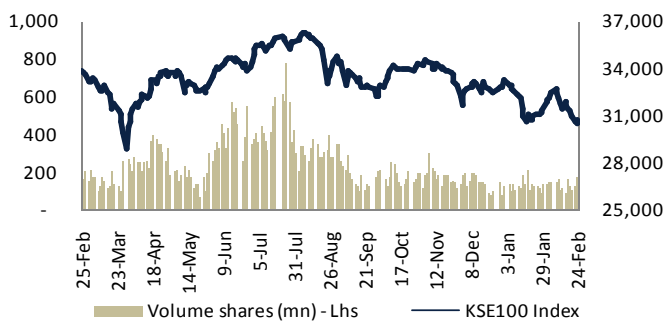
PIOC plans to install Pkr1.5-1.7bn 12MW WHR plant (to be financed largely with internally generated cash), which is expected to commence operations by the start of FY17. The company has already paid in advance for the purchase of plant; however, we have incorporated the same from 2HFY17 in our estimates. We believe effective utilization of the WHR plant will be lower, because it will be installed on Line II, whereas coal fired system built-in on WHR will allow the company to operate the captive facility at a certain cost of coal if Line I kiln is utilized. We believe potential after-tax savings from the WHR project can be close to EPS of Pkr0.88/1.72 in FY17/18F, translating into valuation impact of Pkr6.3/share.

2QFY16 Result Review: As expected, energy cost savings trigger earnings growth

PIOC announced 2QFY16 EPS of Pkr2.45, up 7.5%YoY (Ex-liability reversals of Pkr2.46/share before tax, booked in 2QFY15), mainly due to lower energy tariffs through fuel price adjustments, 21%YoY/QoQ dispatches growth, less than 3% share of exports in sales mix, and 69%/37% YoY/QoQ reduction in finance cost. Broadly, the result was in line with ours and market expectations. The company also announced an interim DPS of Pkr2.50.

Morning News

- **GoP raises PkR152bn vs. target of PkR50bn via PIBs:** Major participation was in 5yr PIBs (PkR81bn), followed by in PIBs with 3yr (PkR63bn) and 10yr (PkR8bn) maturities. Cut off yields for 3/5/10yr PIBs dropped by 16/50/60bps to 6.34/7.04/8.25%.
- **Ministry of Commerce considering removal of RD on fine yarn:** While keeping in view the domestic demand and supply conditions, the Ministry of Commerce is considering removal of RD on fine yarn (mainly imported from India); while that on coarse yarn would remain effective.
- **Outstanding spreads decline to 5.12% as of Jan'16:** Outstanding spreads declined by 7bps MoM to 5.12% during Jan'16; meanwhile fresh spreads increased by 35bps MoM to 3.05%.

KSE100 index & volume

Source: PSX

World Indices

	Close	DoD Δ	DoD Δ (%)	CYTD Δ (%)	FYTD Δ (%)
Pakistan	30,786.6	222.1	0.7%	-6.19%	-10.5%
China	2,928.9	25.6	0.9%	-17.24%	-31.5%
Hong Kong	19,192.5	-222.3	-1.1%	-12.42%	-26.9%
India	23,088.9	-321.3	-1.4%	-11.60%	-16.9%
Indonesia	4,657.7	3.7	0.1%	-12.10%	-5.2%
Malaysia	1,664.2	-13.1	-0.8%	-1.67%	-2.5%
Japan	15,915.8	-136.3	-0.8%	-16.38%	-21.3%
Singapore	2,620.0	-52.1	-2.0%	-9.12%	-21.0%
Korea	1,912.5	-1.7	-0.1%	-2.49%	-7.8%
Taiwan	8,282.9	-51.8	-0.6%	-0.66%	-11.2%
Bangladesh	4,579.5	-18.8	-0.4%	-1.08%	-0.1%
Sri Lanka	6,217.6	-11.3	-0.2%	-9.82%	-11.4%
Philippines	6,769.3	-50.1	-0.7%	-2.63%	-10.5%
Thailand	1,331.9	6.1	0.5%	3.41%	-11.5%
Vietnam	568.0	6.8	1.2%	-1.90%	-4.2%
USA	1,929.8	8.5	0.4%	-5.58%	-6.5%
UK	5,867.2	-95.1	-1.6%	-6.01%	-10.0%
Germany	9,167.8	-249.0	-2.6%	-14.66%	-16.2%

Source: Bloomberg

Forex & Money Market

	Close	DoD Δ	YoY Δ bps	CYTD Δ bps	FYTD Δ bps
6m Tbill yield (%)	6.22	-0.01	-2.15	-0.17	-0.73
10Y PIB yield (%)	8.60	-0.07	-1.28	-0.73	-1.37
6m Kibor (%)	6.11	0.01	-2.13	-0.15	-0.68

	Close	DoD Δ	DoD Δ (%)	YoY Δ (%)	CYTD Δ (%)	FYTD Δ (%)
PkR/US\$	104.68	-0.115	-0.11%	2.8%	-0.1%	2.8%
PkR/EUR	114.98	-0.367	-0.32%	-0.2%	0.5%	1.4%
PkR/JPY	0.936	0.000	0.01%	9.8%	7.5%	12.2%

Source: Bloomberg

Commodity Prices

	Close	DoD Δ	DoD Δ (%)	YoY Δ (%)	CYTD Δ (%)	FYTD Δ (%)
Gold - US\$/oz	1,228.75	3.15	0.3%	2.4%	15.8%	4.8%
Oil (WTI)- US\$/bbl	30.40	0.33	1.1%	-37.4%	-16.9%	-48.9%
Cotton US\$/lb	57.70	-0.47	-0.8%	-10.9%	-8.8%	-14.5%
Coal - US\$/MT	51.90	0.30	0.6%	-17.2%	7.1%	-13.6%
CRY Index	161.49	1.06	0.7%	-27.3%	-8.3%	-28.9%

Source: Bloomberg

Portfolio Flows

(US\$m)	Current	WTD	MTD	12M	CYTD	FYTD
Total FIPI	-1.8	-6.2	-33.4	-349.3	-83.2	-323.9
Individuals	2.1	11.1	24.4	98.5	17.4	70.3
Companies	1.2	5.1	15.9	60.1	41.0	105.7
Banks / DFI	-0.6	2.7	-4.9	5.6	25.5	46.9
NBFC	-0.2	0.6	11.1	125.5	36.6	100.0
Mutual Funds	-0.6	-12.5	-14.2	46.6	-32.6	10.3
Other Organization	0.1	1.4	6.6	61.1	16.2	27.4
Broker Trading	-0.2	-2.1	-7.2	-48.2	-20.9	-36.8

Source: NCCPL

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Ratings Guide*

Buy	Upside more than 20%
Accumulate	Upside more than 10% but less than or equal to 20%
Neutral	Upside from 0% to 10%; Downside from 0% to -10%
Reduce	Downside more than 10% but less than or equal to 20%
Sell	Downside more than 20%

*Based on 12 month horizon unless stated otherwise in the report. Upside/Downside is defined as the percentage difference between the Target Price (TP) and the Market Price (last close).

Valuation Methodology: We use multiple valuation methodologies in arriving at a Target Price including, but not limited to, Discounted Cash Flow (DCF), Dividend Discount Model (DDM) and relative multiples based valuations.

Risks: (1) Disruption in local pricing discipline; (2) reversal in commodity prices; and (3) dumping of Iranian cement.

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