

Sector Performance

	1M	3M	12M
Absolute %	(4.5)	(32.4)	(26.7)
Relative to KSE %	(1.5)	(17.0)	(21.7)

Valuation Comparison

	Rating	Jun'18 TP	Current Price	Upside
ACPL	Buy	239	174	37%
DGKC	Buy	218	136	60%
FCCL	Buy	36	29	24%
LUCK	Buy	580	510	14%
MLCF	Buy	90	69	30%

Cement Sector D/Y Estimates

	FY17	FY18	FY19	FY20
ACPL	6.20%	4.68%	3.80%	1.87%
DGKC	5.31%	5.10%	6.27%	5.04%
FCCL	3.21%	5.40%	5.81%	7.45%
LUCK	2.48%	2.17%	2.17%	1.86%
MLCF	3.71%	4.26%	4.60%	4.92%

Cement Sector EPS Estimates (PKR/sh)

	FY17	FY18	FY19	FY20
ACPL	26.5	32.5	17.9	9.8
DGKC	18.2	20.1	21.8	17.5
FCCL	1.9	2.5	2.9	2.2
LUCK	42.3	39.2	36.5	30.7
MLCF	8.0	7.2	10.7	9.9

We initiate coverage on cement sector covering ACPL, DGKC, FCCL, LUCK and MLCF with a BUY stance. Though we have a BUY stance on all of the mentioned cement companies, given steep price correction in the past couple of months, our inclination remains towards North based players. Cement industry is undergoing expansionary cycle, enhancing production capacity by ~25mn MT (north/south: 17/8) till FY21. Based on our assumption of 9% CAGR in local dispatches during FY18-21, we anticipate local utilization level (local dispatches as a % of total capacity) to remain relatively at a comfortable level (average FY21: 73%) compared to FY10's desperate times (average FY10: 52%), limiting the threat of a full blown price war. Region wise, we prefer north based players since expansions are scheduled to come online over multiple years, with lower risk of further drop in prices until the new lines are commissioned. However, with the bullet expansion of 5.5mn MT in South in 2HFY18, we foresee a 5-10% price drop that may considerably erode gross margins. Our top picks include MLCF (Jun'18 TP: PKR90/sh), FCCL (Jun'18 TP: PKR36/sh) and DGKC (Jun'18 TP: PKR218/sh).

Robust local demand to trigger volumetric growth: Our base case involves a 9% CAGR in local volumetric growth with constant exports from FY18-21. Growth in local dispatches is accredited to 1) improving GDP, 2) commencement of CPEC based projects, 3) hefty allocation of PSDP due to heightened focus on infrastructural projects and 4) better law and order situation.

Capacity addition by 53% till FY21: Cement industry is anticipated to raise production capacity by ~25mn MT (addition of 53%) during FY18-21 from the current industry's annual cement capacity of 46.9mn MT. Region wise analysis shows that north/south are adding 17mn MT/8mn MT respectively.

Healthy utilization level amid expansionary phase: We believe that the threat of a price war amid expansionary wave is low on the back of 9% CAGR in local dispatches, translating into relatively safer local utilization levels (average FY21: 73%) compared to FY10's debacle (average FY10: 52%).

North; well poised compared to South: In the present scenario, North has a regional advantage over South on account of lower risk of price competition since additional capacities are spread across different years, commencing from 2HFY19 and may create a short term price competition in FY20. For south, 70% of the additional capacity is commissioning in FY18 and the rest in FY20 which may put the prices under pressure in both time periods. Moreover, we believe that northern players may exploit southern market owing to 1) current price differential of ~PKR42/bag between both regions and 2) lower transportation cost from N-S vs. S-N since Pakistan's exports are lower than imports, resulting into higher freight cost for imported goods from the sea port.

Key Risks: 1) Intensifying price war, 2) rise in input prices especially coal prices, and 3) demand slowdown.

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The rating system

Rating	Definition
Buy	Total stock return \geq 15%
Hold	$0\% \leq$ Total stock return $<$ 15%
Sell	Total stock return $<$ 0%

* Total stock return = capital gains + dividend yield

Valuation Methodology

To arrive at our period end target prices, BIPL Securities uses different valuation methodologies including

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