

Engro Foods Limited

1QCY15: EFOODS profits up 5x, 'Buy' maintained

In its 1QCY15 results, announced yesterday, EFOODS reported marked improvement in profitability on the back of improving margins. During the quarter, consolidated earnings surged by around 5x YoY to PKR1.1bn (EPS PKR1.4) compared to PKR190mn (EPS PKR0.25) in SPLY. Improvement in results is in line with our broad estimations as projected in our report titled 'Historic low milk powder prices to restore margins' on January 21, 2015. On quarter on quarter basis, company profits improved by 93%.

During the quarter, company sales revenues improved by 24% YoY while gross margins stood at 27.3% (up 7pps YoY). We attribute the revenue increase to higher volumetric sales while lower milk prices augmented the margins.

For CY15, we expect 3x profit growth in EFOODS to PKR4.9/share and maintain 'Buy' on the scrip with the TP of PKR166/share. At current prices, the scrip offers 16% and is trading at CY15F PE of 29.2x and PS of 2.1x.

1Q profits increased 462% YoY to PKR1.4/share

In 1QCY15, EFOODS sales increased by 24% YoY to PKR12.6bn while gross margins stood at 27.3% (up 7pps YoY). We attribute the revenue increase to higher volumetric sales especially Olper's and Tarang. On the other side, margins would have expanded because of lower powder milk prices and cheaper local milk procurement. To highlight, milk powder prices have crashed to USD2,446/ton from CY14 average of USD3,496/ton. Further, admin cost declined by 19% to PKR326mn while finance cost showed an increase of 4% to PKR267mn despite lower interest rate.

Profits to grow manifolds in CY15, TP revised up to PKR166/share

CY15 profitability is likely to increase manifolds to PKR3.8bn (EPS PKR4.9) compared to PKR0.9bn (EPS PKR1.1) last year. Revenues are likely to grow by 18% to PKR51.4bn as we expect 17% volumetric growth in liquid dairy. Plus, margins would also fatten by 7pps to 25.8% on the back cheaper input milk prices (liquid & powder). Lower fuel prices would be another benefit for the company.

We have revised our model assumptions to incorporate excellent 1Q results & lower discount rate and come up with the target price of PKR166/share. At current levels, EFOODS is trading at CY15 PE of 29.2x and PS of 2.1x while on CY16 profits, its PE stands at 21.8x and PS at 1.6x. Maintain 'Buy'

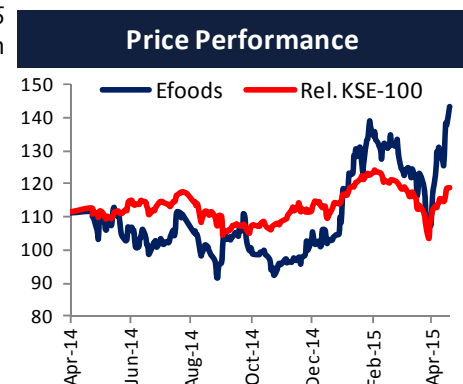
| PKRmn | 1QCY14 | 4QCY14 | 1QCY15 | YoY | QoQ |
|--------------------------|--------------|--------------|--------------|-------------|-------------|
| Net Sales | 10,168 | 12,402 | 12,576 | 24% | 1% |
| Cost of Sales | (8,103) | (10,015) | (9,142) | 13% | -9% |
| Gross Profit | 2,065 | 2,387 | 3,435 | 66% | 44% |
| Distribution Expenses | (1,068) | (1,145) | (1,250) | 17% | 9% |
| Admin expenses | (405) | (404) | (326) | -19% | -19% |
| Other Income | 11 | 81 | 92 | 728% | 14% |
| Operating profit | 542 | 936 | 1,827 | 237% | 95% |
| Finance Cost | (256) | (297) | (267) | 4% | -10% |
| Profit before Tax | 285 | 639 | 1,560 | 447% | 144% |
| Profit after Tax | 190 | 617 | 1,069 | 462% | 73% |
| EPS (Rs) | 0.25 | 0.81 | 1.39 | | |

Source: KSE, Taurus Research

| EFOODS PA | BUY |
|----------------------------------|--------------|
| Stock price | 143.4 |
| Target price (Dec-15) | 165.9 |
| Current upside/(downside) | 16% |
| Outstanding shares (mn) | 767 |
| Market Cap (PKR bn) | 110.0 |
| Free float | 15% |
| 3M Avg. daily volume (PKRmn) | 403 |
| 3M Avg. daily volume (shares mn) | 3.1 |
| 3M High | 143.4 |
| 3M Low | 105.4 |

| Key Financials | in PKRbn | | |
|------------------|----------|-------|-------|
| Year end | CY14A | CY15F | CY16F |
| Net sales | 43.4 | 51.4 | 67.8 |
| Cost of sales | 35.3 | 38.1 | 51.1 |
| Gross Profit | 8.1 | 13.3 | 16.7 |
| Operating profit | 2.3 | 6.4 | 7.5 |
| Financing costs | 1.2 | 0.9 | 0.3 |
| Net Profit | 0.9 | 3.8 | 5.0 |

| Key Metrics | CY14A | CY15F | CY16F |
|-----------------|-------|-------|-------|
| EPS | 1.1 | 4.9 | 6.6 |
| DPS | - | - | - |
| BVPS | 15.1 | 20.0 | 26.6 |
| P/Ex | 126.6 | 29.2 | 21.8 |
| P/BVx | 9.5 | 7.2 | 5.4 |
| Dividend Yield | 0% | 0% | 0% |
| Earnings growth | 0% | 334% | 34% |
| ROA | 4% | 16% | 19% |
| ROE | 8% | 28% | 28% |
| Net debt/Equity | 64% | 24% | 4% |



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About the company

Engro Foods Limited was officially launched as a fully owned subsidiary of Engro in 2004. Using dairy as a stepping stone to enter into the food business, the Company has established state-of-the-art processing units in Sukkur and Sahiwal, along with an ice cream production facility in Sahiwal.

Top quality brands like Olper's, Tarang and Omore have been successfully launched under the helm of Company's dairy products. To support these brands and their highest standards of quality, Engro Foods has invested heavily in milk processing and milk collection infrastructure. The company has 767mn shares outstanding and is listed on Karachi and Lahore Stock Exchange. Engro Corporation holds around 85% shares of EFOODS.