

## Engro Polymer & Chemicals Ltd

### Result Review

PSX: EPCL Bloomberg: EPCL: PA Reuters: EPCL.PSX

Pakistan Research

## EPCL: 3QCY21 EPS recorded at PKR 3.42; DPS PKR 3.00

- Engro Polymer & Chemicals Ltd (EPCL) announced its 3QCY21 financial results, wherein the company reported consolidated EPS of PKR 3.42/share, up 65% YoY compared to PKR 2.07/share in 3QCY20. Cumulatively for 9MCY21, net earnings of the company clocked in at PKR 11.41 (up 3.9x YoY).
- Along with the result, the company also announced an interim cash dividend of PKR 3.00/share taking 9MCY21 payout to PKR 10.80/share. No dividend was announced during the same period last year.
- Net sales grew by 87% YoY during the 3QCY21 due to possible volumetric growth coupled with 57% YoY jump in the PVC prices.
- The earnings were slightly lower than our expectation owing to higher than anticipated cost of sales. Significant increase of 99% YoY in cost of sales could be due to higher commodity prices worldwide and increased raw material consumption.
- During 3QCY21, other income remained on higher side, up by 53%YoY; however, down by 4% YoY during 9MCY21.
- Higher other charges during 3QCY21 also deviated our earnings expectations, which were up by 6.7x YoY to PKR 789mn.
- Effective tax rate for 3QCY21 came in at 25% as compared to 30% during same period last year.
- We have a 'Buy' stance on EPCL with June-22 price target of PKR 79/share. The stock is offering an upside of 38% along with a dividend yield of 5%.

### Key Data

|                         |          |
|-------------------------|----------|
| PSX Ticker              | EPCL     |
| Target Price (PKR)      | 79       |
| Current Price (PKR)     | 57       |
| Upside/(Downside) (%)   | 38%      |
| Dividend Yield (%)      | 5%       |
| Total Return (%)        | 43%      |
| 12-month High (PKR)     | 65.45    |
| 12-month Low (PKR)      | 39.30    |
| Outstanding Shares (mn) | 909      |
| Market Cap (PKR mn)     | 52,063   |
| Year End                | December |

Source: Company Accounts, Akseer Research

### Financial Highlights (PKR mn)

|                          | 3QCY20       | 3QCY21       | YoY        | 9MCY20       | 9MCY21        | YoY         |
|--------------------------|--------------|--------------|------------|--------------|---------------|-------------|
| Net Sales                | 10,057       | 18,827       | 87%        | 22,932       | 49,323        | 1.2x        |
| Cost of Sales            | 6,840        | 13,585       | 99%        | 17,892       | 32,627        | 82%         |
| <b>Gross Profit</b>      | <b>3,217</b> | <b>5,242</b> | <b>63%</b> | <b>5,039</b> | <b>16,695</b> | <b>2.3x</b> |
| Distri. & Admin. Exp.    | 88           | 90           | 2%         | 201          | 258           | 29%         |
| Other Income             | 243          | 373          | 53%        | 1,014        | 970           | -4%         |
| Other Charges            | 103          | 789          | 6.7x       | 743          | 1,500         | 1.0x        |
| Finance Cost             | 454          | 487          | 7%         | 1,821        | 1,402         | -23%        |
| <b>Profit Before Tax</b> | <b>2,694</b> | <b>4,122</b> | <b>53%</b> | <b>2,920</b> | <b>14,043</b> | <b>3.8x</b> |
| Taxation                 | 813          | 1,016        | 25%        | 817          | 3,671         | 3.5x        |
| <b>Net Income</b>        | <b>1,881</b> | <b>3,107</b> | <b>65%</b> | <b>2,103</b> | <b>10,372</b> | <b>3.9x</b> |
| EPS                      | 2.07         | 3.42         | 65%        | 2.31         | 11.41         | 3.9x        |
| DPS                      | 0.00         | 3.00         |            | 0.00         | 10.80         |             |

Source: Company Accounts, Akseer Research

### Key Financial Ratios

|                | CY18A | CY19A | CY20A | CY21E | CY22F | CY23F |
|----------------|-------|-------|-------|-------|-------|-------|
| EPS            | 6.22  | 4.07  | 6.30  | 15.89 | 7.23  | 7.84  |
| EPS Growth     | 112%  | -35%  | 55%   | 152%  | -54%  | 8%    |
| DPS            | 1.10  | 0.80  | 1.25  | 9.50  | 3.00  | 3.25  |
| P/E            | 9.20  | 14.09 | 9.09  | 3.61  | 7.92  | 7.30  |
| Dividend Yield | 2%    | 1%    | 2%    | 17%   | 5%    | 6%    |
| EV/EBITDA      | 5.71  | 8.56  | 6.24  | 2.76  | 4.43  | 3.82  |
| P/B            | 2.70  | 2.93  | 1.99  | 1.63  | 1.46  | 1.30  |

Source: Company Accounts, Akseer Research

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**Valuation Basis**

Our PT for Engro Polymer & Chemicals Ltd (EPCL) has been computed using Free cash flow to equity (FCFF) method. We have used a risk-free rate of 11%, beta of 1.0 and market risk premium of 6% to arrive at cost of equity of 17%.

**Investment Thesis**

We have a 'BUY' recommendation on the stock based on our Jun-22 PT of 79/share. Our price target indicates an upside of 38% along with a dividend yield of 5%. Our investment case is based on 1) healthy PVC-Ethylene margins, 2) Commissioning of new plants adding to capacity, 3) Diversification strategy to enter Hydrogen Peroxide market.

**Risks**

Key risks to our investment thesis include 1) earlier than expected reduction in PVC-ethylene spread, 2) saturation of Hydrogen-peroxide market 3) caustic soda market remaining flattish.

**Company Description**

Engro Polymer & Chemicals Ltd. (EPCL) is engaged in the manufacturing of PVC resin, chlor-alkali products like Caustic Soda, Sodium Hypochlorite and Hydrochloric Acid. EPCL sells, markets and distributes PVC under the brand name "SABZ". It is further exploring other avenues such as Hydrogen Peroxide.

**Financial Highlights - EPCL**

| Income Statement (PKR mn) |              |              |               |               |               |               |
|---------------------------|--------------|--------------|---------------|---------------|---------------|---------------|
|                           | CY18         | CY19         | CY20          | CY21E         | CY22F         | CY23F         |
| Net sales                 | 35,272       | 37,837       | 35,331        | 64,268        | 44,514        | 47,626        |
| Cost of sales             | 26,536       | 29,731       | 24,382        | 40,938        | 31,642        | 34,293        |
| <b>Gross Profit</b>       | <b>8,736</b> | <b>8,106</b> | <b>10,949</b> | <b>23,330</b> | <b>12,872</b> | <b>13,333</b> |
| SG & A                    | 2,044        | 962          | 845           | 940           | 850           | 866           |
| <b>Operating Profit</b>   | <b>6,692</b> | <b>7,144</b> | <b>10,105</b> | <b>22,390</b> | <b>12,022</b> | <b>12,467</b> |
| Other income              | 1,249        | 930          | 1,180         | 1,343         | 1,136         | 1,161         |
| Other charges             | 872          | 1,241        | 859           | 2,312         | 1,655         | 1,580         |
| Finance cost              | 606          | 1,794        | 2,191         | 1,955         | 2,246         | 2,009         |
| <b>Profit before tax</b>  | <b>6,463</b> | <b>5,039</b> | <b>8,234</b>  | <b>19,465</b> | <b>9,257</b>  | <b>10,039</b> |
| Taxation                  | 1,533        | 1,343        | 2,504         | 5,027         | 2,685         | 2,911         |
| <b>Profit after tax</b>   | <b>4,930</b> | <b>3,696</b> | <b>5,730</b>  | <b>14,439</b> | <b>6,573</b>  | <b>7,128</b>  |

Source: Company Accounts, Akseer Research

| Balance sheet (PKR mn)                |               |               |               |               |               |               |
|---------------------------------------|---------------|---------------|---------------|---------------|---------------|---------------|
|                                       | CY18          | CY19          | CY20          | CY21E         | CY22F         | CY23F         |
| PPE                                   | 19,398        | 31,433        | 37,614        | 40,520        | 41,112        | 38,704        |
| Non-Current Assets                    | 1,065         | 710           | 192           | 191           | 8,436         | 7,098         |
| Current assets                        | 16,434        | 17,650        | 24,382        | 39,036        | 38,679        | 39,070        |
| <b>Total Assets</b>                   | <b>36,023</b> | <b>57,519</b> | <b>69,094</b> | <b>86,019</b> | <b>86,803</b> | <b>85,441</b> |
| Non-Current liabilities               | 7,890         | 23,933        | 27,579        | 33,861        | 32,523        | 27,001        |
| Current liabilities                   | 11,337        | 15,810        | 15,388        | 20,227        | 18,505        | 18,490        |
| <b>Total Liabilities</b>              | <b>19,228</b> | <b>39,743</b> | <b>42,968</b> | <b>54,089</b> | <b>51,028</b> | <b>45,491</b> |
| Equity                                | 16,796        | 17,776        | 26,126        | 31,930        | 35,776        | 39,950        |
| <b>Total Equity &amp; liabilities</b> | <b>36,024</b> | <b>57,519</b> | <b>69,094</b> | <b>86,019</b> | <b>86,803</b> | <b>85,441</b> |

Source: Company Accounts, Akseer Research

| Cashflow statement (PKR mn) |              |                 |                |               |               |               |
|-----------------------------|--------------|-----------------|----------------|---------------|---------------|---------------|
|                             | CY18E        | CY19F           | CY20F          | CY21E         | CY22F         | CY23F         |
| Net Income                  | 4,930        | 3,696           | 5,730          | 14,439        | 6,573         | 7,128         |
| Non-cash Charges            | 4,798        | (8,147)         | (884)          | 5,704         | 2,622         | 3,721         |
| <b>Operating Cash flows</b> | <b>9,728</b> | <b>(4,451)</b>  | <b>4,846</b>   | <b>20,142</b> | <b>9,194</b>  | <b>10,849</b> |
| <b>FCFF</b>                 | <b>5,843</b> | <b>(19,372)</b> | <b>(1,113)</b> | <b>15,879</b> | <b>6,920</b>  | <b>11,135</b> |
| Net borrowings              | (1,250)      | 15,035          | 172            | 7,084         | 675           | (5,954)       |
| <b>FCFE</b>                 | <b>4,131</b> | <b>(5,652)</b>  | <b>(2,466)</b> | <b>21,512</b> | <b>6,000</b>  | <b>3,755</b>  |
| Net change in cash          | 679          | (570)           | 154            | 12,877        | 3,273         | 801           |
| <b>Closing cash</b>         | <b>1,362</b> | <b>792</b>      | <b>946</b>     | <b>13,823</b> | <b>17,097</b> | <b>17,898</b> |

Source: Company Accounts, Akseer Research

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To arrive at our 12-months Price Target, the JV uses different valuation methods which include: 1). DCF methodology, 2). Relative valuation methodology, and 3). Asset-based valuation methodology.

**Ratings Criteria**

JV employs a three tier ratings system to rate a stock, as mentioned below, which is based upon the level of expected return for a specific stock. The rating is based on the following with time horizon of 12-months.

| <b>Rating</b> | <b>Expected Total Return</b>  |
|---------------|-------------------------------|
| Buy           | Greater than or equal to +15% |
| Hold          | Between -5% and +15%          |
| Sell          | Less than or equal to -5%     |

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