

September 01, 2010

## Pakistan Market

## KSE: Index down 7% in August

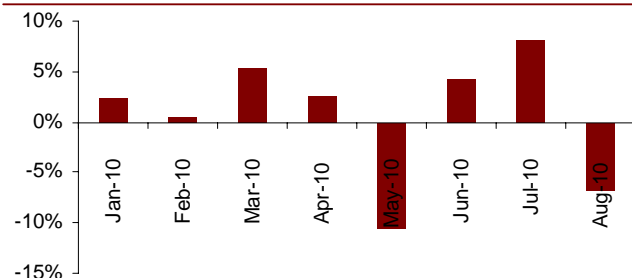
MORNING BRIEFING



KSE100 Index: Closing 9,813.05 ↑ (+296.63)

The KSE 100 Index declined by 6.7% in Aug; shedding the bulk of 8.2% gains witnessed in July 2010 and underperforming the regional market by an average 7%. The discount to the regional markets has now risen to 46% compared to 41% at the beginning of the month and the historical average of 33%. Interestingly however, net foreign portfolio investment during the month stood at US\$41.3mn, raising YTD investment to US\$360mn. SBP's unexpected increase in the discount rate (DR) by 50bps, a difference of opinion emerging between the authorities over the proposed Margin Trading System (MTS) and widespread floods were key performance dampeners. This is also reflective from investor activities which for the month remained dull with average daily volumes declining by 18%MoM, a dismal trend compared to an average increase of 4% witnessed in the region.

## KSE-100: Monthly returns in 2010



Source: KSE

With this downturn, the market appears highly attractive from a valuation perspective – trading at a 2011 PE of 7.1x, and we flag HUBCO, FFC, FFBL and PPL as key defensive scrips. We believe re-introduction of the leverage product and liquidity stimulus prompted by foreigners and government borrowing to be key triggers ahead for the market.

## Local bourse activity dull relative to regional peers

Not only did the Index underperform the region by 7%, average daily volumes too remained poor compared to peers,

declining by 18%MoM. Due to low volumes, this Ramadan's (Holy month) performance has also remained dismal compared to the 10-year average return of 6%. We believe the hike in the DR, dissent over MTS and widespread floods were key turn-offs for the investors.

## Corporate results largely ignored

Though corporate results were a mixed bag, the market largely failed to get excited even at a few impressive results announced. The banking and auto sectors, which registered an increase of 42%YoY and 100%YoY, respectively in their profitability during Apr-Jun 2010, saw their market capitalization dip a respective 11%MoM and 16%MoM. Power utilities (Electricity), amongst key sectors, outperformed the Index by 5% primarily owing to a higher than expected payout by HUBCO.

## Outlook: Stay defensive!!

Though the market remains highly attractive from the valuation perspective, we recommend investors to focus on defensive plays given the recent volatility witnessed in the market. Our top picks are as follows:

**HUBCO:** The scrip offers an FY11F dividend yield of 14.3%, making it our top defensive pick in the Pakistan market. Its predictable dividend stream governed by the Power Purchase Agreement and the company's commitment towards capacity expansions enhances our liking for the scrip. The scrip trades at a discount of 19% to our target price of Rs45.

**FFC:** The scrip trades at a 2011E dividend yield of 13.3%. Moreover, the possible acquisition of Agritech should allow an exposure to the SSP market and bring in cost efficiencies. The company currently has a market share in Urea business of 39%. The scrip offers a potential upside of 24% to our target price of Rs132.

**FFBL:** We premise our liking of the scrip on its 2011E dividend yield of 13.9%. The company is expected to post earnings of Rs4.4 per share in 2011, with an investment of

Rs5bn in the power sector to bode well for the company, going forward. Our target price for the scrip stands at Rs34 and offers a likely return of 17%.

**PPL:** Being least affected by oil price volatility among listed E&Ps, we believe, PPL is well set to offer a potential 15% return (excluding dividends) to investors in the next 12 months. Moreover, an attractive dividend yield of 10.1% expected for FY11F further strengthens our liking for the stock. PPL's well balanced exploration plan with particular focus on JVs with local and foreign operators, has yielded success in the form of discoveries and reserves addition notably in Nashpa, Tal, Hala and Latif.

## Top defensive picks

	FY11 EPS	FY11 Div. Yield	Target Price
HUBC	5.5	14.3%	45
FFC *	14.4	13.3%	132
FFBL *	4.4	13.9%	34
PPL	32.1	10.1%	240

Source: JS Research \*2011 estimates

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