

January 08, 2010
Pakistan Market

OGDC: US\$ based returns attracting foreigners

MORNING BRIEFING



KSE100 Index: Closing 9737.47 ↑ (+10.11)

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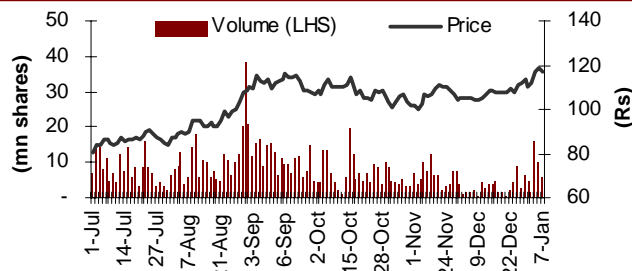
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Low real interest rates and excess global liquidity after stimulus packages offered by various governments have propelled foreign investors to seek investment opportunities in the emerging markets. Using low cost funds, the investors are taking exposure in high dividend yielding stocks and benefiting from carry trade. Based on similar grounds, renewed foreign interest has been witnessed in Pakistan Market as well where foreign led recovery has brought some momentum and improvement in trading volumes.

Pakistan Market offers an arbitrage

Benchmark interest rates under US FED, BOE, ECB and BOJ are all settled below 1% with 1 year US\$ Libor standing at 0.98%. With excess liquidity owing to the government led stimulus packages, global fund managers are heading towards equity markets with attractive dividend yields offering an arbitrage like opportunity. In such a scenario Pakistan Market with FY10 dividend yield of 7.4% remains an ideal investment avenue for such investors.

Graph: OGDC market performance in 1HFY10



Source: KSE & JS Research

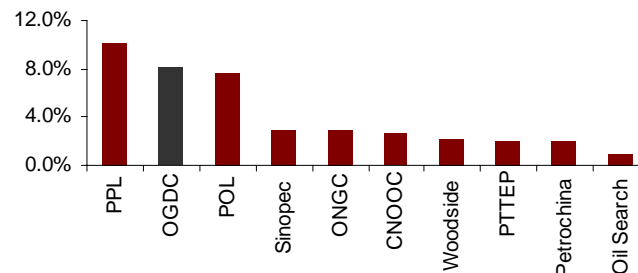
We opine the recent stock specific rally is driven by foreign players capitalizing this arbitrage opportunity. OGDC in this rally remained in the limelight with share price up 11% during last 1 month and average trading volume of 4.4mn shares (US\$5.8mn). We believe interest in the stock was particularly

driven on the back of attractive dividend yield, US\$ based revenues (providing hedge against Rupee depreciation) and its decent market float (US\$870mn) which provides an ease of exit to the investors. Though the stock appears fairly valued to us, foreign interest in OGDC could continue till this arbitrage opportunity remains in the stock.

How far is OGDC attractive?

According to our valuation, the stock is fairly valued with target price of Rs118 per share, however the stock remains an attractive investment opportunity for foreign yield hunters as it offers FY10E dividend yield of 8.1%. Based on a sample of regional oil and gas producers (see graph), the average 2010 dividend yield is 4.2%. Even if the investors keep the cutoff yield for OGDC at 5.5% (30% higher than sample average), their interest would remain intact till the stock price appreciates to Rs174 per share.

Graph: Regional E&P's Dividend yield



Source: Reuters & JS Research

What other options are available

Critically evaluating our Universe, we believe there are other picks also having a potential to attract foreign inflows based on their attractive dividend yields and sizable float. Keeping a psychological benchmark of US\$450mn as free float, PPL and FFC are two stocks offering dividend yield of 10.2% and 13.3%, respectively. Out of the two, the similar kind of foreign interest is more likely in PPL due to its US\$ denominated revenues. We recommend 'Buy' on PPL and 'Hold' on FFC.

Also in focus

IMF releases detailed review

IMF has released a detailed note on the country after completing its review and disbursing the fourth tranche of US\$1.2bn late last month. Although IMF has highlighted that risks to the economy still remain, improving external account data and structural initiatives by the government were stated as key positive developments. Importantly, the fund has maintained the real GDP growth target for FY10 at 3% while it has revised the inflation target upwards by 2% to 11% - on rising electricity tariffs and higher fuel prices. IMF, also taking in account the improving external position on the back of rising remittances, projects the current account deficit at 4.2% of the GDP from 4.7% earlier.

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