JS Research

July 16, 2009

Pakistan Market

MORNING BRIEFING

Pakistan: Key positives for today

KSE100 Index: Closing 7686.15 ↑ (+54.49)

Market has been worried about delay in IMF tranche, return of IDPs and Supreme Court reaction to petition against Presidential petroleum ordinance. In fact few pundits' highlight these issues, as potential end of Pakistan's recently lodge honey moon period. But with today's news flow regarding, 1) government agreement with ADB and World Bank on electricity subsidy, 2) SC's return petition against Presidential ordinance and 3) return of more than 500 IDP's families back home are all pointing towards a Pakistan E return to its heydays.

This is also reflected in yesterday's T-bill auction, where participation overwhelmed pre-auction size of PRs45bn and SBP opted for 92bp cut in yields. We expect equity market will factor in these positives in days to follow.

IMF tranche on its way

In a recently held meeting with IMF delegates at Istanbul, IMF remained tight lipped and barred of issuing any statement, however, feedback from finance ministry indicates that IMF raised concern on continuation of electricity subsidy and tax targets. As a result, fresh dialogues on subsidies were initiated among Government, ADB and World Bank in the current week. The good news is that initial agreement has been reached among stake holders and Government of Pakistan has agreed to eliminate electricity subsidy by April 2010 through increasing tariffs in 3 phases by 22-26ppt. This highlights government seriousness regarding structural issues and commitment with IMF program. We believe with this agreement the next IMF tranche of US$840mn will be on its way to Pakistan.

Return of IDPs

More than three million Internally Displaced Pakistanis (IDP's) have started to return home on successful completion of the military operation against local militants. This carries a huge positive, as it will help ease burden on government expenditure on IDP's. Additionally, we expect reconstruction of SWAT Valley and improve domestic demand.

SC returns Petition against Presidential Ordinance

On imposition of Presidential Ordinance regarding petroleum levy, few recalled it, as clash of Judiciary and Executive body, however, we highlighted this as a key positive when Presidential Ordinance was imposed. Because this was the first time we saw checks and balances irrespective of influences. Initially, SC issued decree against Carbon tax and termed it unnecessary which was dually followed by the government. The President subsequently imposed levy on petroleum products by 17% to meet revenue expenditure gap, which was challenged again in SC. But off late, SC on the basis of jurisdiction refused to entertain the petition seeking reversal of the Presidential Ordinance pertaining to imposition of Petroleum levy. This would be a huge relief for the government as they are struggling to raise revenues in the depressed economic environment.

What does this mean for markets?

With the easing concerns we believe market will react positively, as reflected from yesterdays T-bill auction where SBP has opted to reduce T-bill yields by 70-92bps. Recent renewed foreign interest in local equity market also highlights reduction in country risk premia. We expect equity market will excel from here and reach 9,000 levels by December 2009.

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Also in focus

PSMC reduce prices on 800cc segment vehicles

Elimination of 5% federal excise duty (FED) on 850cc and above vehicles had resulted in reduction in prices with the exception of vehicles in the 800cc segment. In a bid to boost sales Pak Suzuki (PSMC) has now reduced prices of 800cc vehicles i.e. Mehran, Bolan & Ravi by 5-7%. Post elimination of FED, we saw PSMC post 7%MoM growth in the month of June 2009. Upon further analysis, we saw 800cc segment grow by only 1% compared to 19% by 850cc segment and above. Hence, going forward we expect sales to pick up in the 800cc segment as well. We currently have a 'Hold' recommendation on the scrip trading at FY10F PE of 8.3x.

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