

December 17, 2009

Pakistan Market**NRO, Democracy & Freedom of Speech****MORNING BRIEFING**

KSE100 Index: Closing 9253.66 ↓ (-12.38)

Yesterday can be termed as a historic day for Pakistan, where one could feel the essence of true democracy prevailing in the country. The Supreme Court has issued a short-order in favor of the petition challenging the controversial National Reconciliation Ordinance (NRO). Key takeaways from yesterday's verdict reinforce 1) the rule of law, 2) freedom of speech, and 3) the evolving patience of the government. This should help build institutions, contain corruption and achieve economic development goals in the years to follow. The KSE's initial positive response to the verdict highlighted this as the market rose by 129pts (or 1.4%) in the first 30 minutes.

The SC's short order

The 17 member bench of the Supreme Court on Wednesday, declared the National Reconciliation Ordinance (NRO) unconstitutional and ab initio (never to have existed) by reviving all cases and reversing acquittals of its beneficiaries. The Chief Justice of Pakistan has ordered the federal government to take immediate steps to restore the originally filed charges and deal with requests for mutual legal assistance in pursuing money laundering cases pending in foreign countries. We believe, with this decision, bulk of the political uncertainty has eased off, reiterated by the President's spokesperson who stated, "The PPP and the Presidency respect the court and its verdict". Additionally, he referred to Article 248 of the Constitution, which gives immunity to the President, the Governor and the Prime Minister. Hence, they shall not be answerable to any court with regards to the exercise of power and performance of their respective offices.

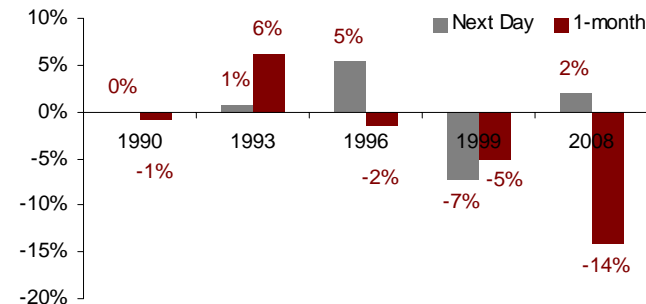
The impact and likely future political scenario

We rule out the possibility that the President will resign on grounds of yesterday's verdict, as he enjoys immunity under the Constitution. Regarding the international cases, we believe, the President will also enjoy Sovereign immunity, in which the Head of State is not answerable to any international court. However, we believe, other beneficiaries of the NRO

will have to face the apex courts and may have to sacrifice their incumbent offices. This should not hinder the performance of the government's day to day functionality, as Pakistan follows the Parliamentary system, where the Prime Minister is responsible for daily affairs. On the positive side, we expect the President of Pakistan to repeal the 17th amendment and transfer his powers to Prime Minister in the ensuing days. This should send a positive signal to the international community and investors.

Markets: Revisiting history

Political instability is not unusual for Pakistani markets and for reference's sake, we have picked 5 instances from the past 20 years when political governments were either dissolved or over thrown by a Military dictator and observed the market's reaction to it. In the most extreme case, the market fell by 7% when the former Prime Minister Nawaz Sharif was deposed by General Musharraf in 1999 and subsequently settled (see chart below). On the basis of this, we expect that the market will not react in an extreme manner and may continue to weather this political development. Currently, our recommendation for the market is 'Hold' with top picks including POL, PPL, ENGRO and HUBCO.

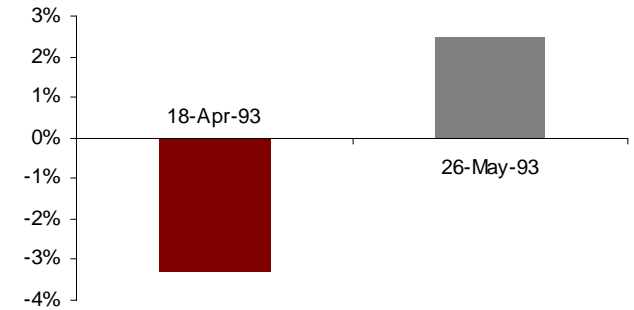
Graph: Market performance post removal of Government

Source: JS Research, KSE

1990: Benazir Bhutto (5-Aug); 1993: Nawaz Sharif (18-Jul)

1996: Benazir Bhutto (5-Nov); 1999: Nawaz Sharif (12-Oct)

2008: Musharraf (18-Aug)

Graph: Dissolution and reinstatement of Nawaz Govt.

Source: JS Research, KSE

18-Apr-1993: Nawaz Sharif's govt. dissolve

26-May-1993: Nawaz Sharif's govt. reinstated

muzzammil.aslam@js.com
92 (21) 111-574-111 (ext. 3035)

Also in focus**FDI drops to US\$744mn; PI up in 5MFY10**

According to the foreign investment figures released by the State Bank, FDI dropped by 52% in 5MFY10 to US\$744mn compared to US\$1.62bn in the same period last year. This, we believe, is on account of the prevalent slowdown in the international as well as the domestic economy. However, the decline is magnified due to the inflow of investment in MCB Bank from Maybank in Aug 2008. Interestingly, Portfolio Investment figures have shown a huge rise in the period as US\$311mn was directed inwards as against outflow of US\$162.9mn in the same period last year.

JS Global Capital Limited

6th Floor, Faysal House, Main Shahrah-e-Faisal, Karachi

Research:

Tel: +92 (21) 32799005

Fax: +92 (21) 32800163

Equity Sales:

Tel: +92 (21) 32799513

Fax: +92 (21) 32800166

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