

May 21, 2010

**Pakistan Market****MORNING BRIEFING**
**Pre-Budget FY11: Deficit containment to be ensured** KSE100 Index: Closing 9993.40 ↓ (-56.64)

Despite a fair number of reforms carried out under the Stand-By Arrangement (SBA) in FY10, IMF is still not pleased with the current pace of the programme's implementation by the Government of Pakistan (GoP). Fiscal deficit is the top most concern, along with delay in the energy price pass-through and tax related reforms. This has also raised a question mark on the completion of the US\$10.6bn Stand-By facility of IMF, expiring in December 2010, which has seen almost all tranches coming in, late by at least a month or two (see table). Despite the delays, we believe the government is committed to complying with IMF's conditionality so as to ensure the reduction of Pakistan's macroeconomic risk premia. We believe the upcoming budget will be formulated with an objective of containing the deficit through elimination of subsidies and broadening of the tax base with implementation of the Value Added Tax (VAT).

**What is in store?**

- Electricity price pass-through of another 6%.
- Imposition of capital gains tax on stock market transactions and VAT nationwide.
- Enhancement of excise tax net to include a number of services (e.g. banking and insurance); increase in WHT charged on imports.
- Removal of exemptions to textile and agriculture.

**Upcoming budget: Immunization of the economic system**

Unlike the previous budgets, the government will refrain from announcing ambitious development and budgetary targets and the focus will be on relieving the poor through targeted subsidies, giving higher pay increments to government employees and an increase in the minimum wage level. While the focus is clearly on raising taxes by broadening the base, imposition of CGT on stock trading and the likely introduction of the Wealth Tax Ordinance may spark some confusion amongst retail investors. However, we continue to expect

quality long-term institutional inflows from local and foreign sources in the stock market.

**Market outlook: Positive**

We continue to remain upbeat on the stock market on grounds of the macro economic recovery. The GDP growth is expected to be around 4.0% FY10, up from 1.2% in FY09. Interestingly, the balance of macro risk points towards policy easing than tightening in the year to come. Pakistan was amongst the few countries in the world, which have undergone massive re-structuring and did not implement any stimulus package in order to revive the economy. Relatively speaking, the Pakistani market is the cheapest in comparison to its regional and frontier peers. The KSE-100 index is trading at a 2011F PE of 7.1x, and is offering a steep discount of 43% to the regional peers. It is interesting to note that, Pakistan is also trading at a deep discount to its frontier market peers. The Sri lankan and Bangladeshi markets are trading at PE of 16.6x and 30x, respectively. The Budget FY11 is expected to be a nonevent for the Oil, Telecom, Banks & Fertilizer sectors, while it could carry good news for the cement sector. In contrast, Chemicals, Autos and Textiles may be negatively impacted.

[js.research@js.com](mailto:js.research@js.com)  
92 (21) 111-574-111

**Also in focus****Foreign Exchange Reserves decline to US\$15.05bn**

The foreign exchange reserves have declined by 2% to US\$15.05bn in the week ending on 14, May 2010. Reserves held by the State Bank of Pakistan fell to US\$11.27bn while those held by the commercial banks also declined to US\$3.78bn. Moreover, \$1.13bn released by the IMF will be reflected in the next week's Forex reserve numbers.

**JS Global Capital Limited**

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

**Research:**

Tel: +92 (21) 32799005  
Fax: +92 (21) 32800163  
[js.research@js.com](mailto:js.research@js.com)

**Equity Sales:**

Tel: +92 (21) 32799513  
Fax: +92 (21) 32800166  
[junaid.iqbal@js.com](mailto:junaid.iqbal@js.com)

**Fixed Income Sales:**

Tel: +92 (21) 32799541-44  
Fax: +92 (21) 32800165  
[tariq.usman@js.com](mailto:tariq.usman@js.com)

**Corporate Finance:**

Tel: +92 (21) 32799005  
Fax: +92 (21) 22800163  
[azhar.iqbal@js.com](mailto:azhar.iqbal@js.com)

**JS RESEARCH IS AVAILABLE ON BLOOMBERG, CAPITALIQ & THOMSON REUTERS**