JS Research

June 22, 2010

Pakistan Market

MORNING BRIEFING

SSGC: Hopes for positives dashed

KSE100 Index: Closing 9651.32 ↑ (+5.61)

Rumours that had kept investor interest alight in SSGC's scrip off late have all been dispelled, with the request for relaxation in UFG targets and revision in the profit formula having been rejected by OGRA. Further, the US is in the process of imposing fresh sanctions on Iran which may jeopardize the progress on the Iran-Pakistan (IP) gas pipeline. This loses SSGC an opportunity to incur more CAPEX and thus earn higher profits in the future. Yet another cause for concern for the company is the change proposed in the turnover tax rate (from 0.5% to 1%) in the Budget FY11. We have also revisited our FY10 UFG loss assumption following discussions with the management and upgraded it to 8.6% from 7.6% previously. Based on our revised target price of Rs12 we retain our 'Sell' stance on the scrip.

IP project in peril

US's special representative for Pakistan, Mr.Holbrooke has advised the GoP to reconsider participation in the IP project which is worth US$7.6bn, and the GoP has agreed to abide by any sanctions placed on Iran. The US is considering placing fresh restrictions on dealing with Iran's financial sector. This may naturally affect the funding of this project by international institutions and the progress of the project itself, which would have been a major trigger for SSGC otherwise. We had not included the materialization of this project in our projections and therefore, our present valuation remains unaffected in the event this project does not come through.

Turnover tax: Final decision awaited

The Government in the recently announced Federal Budget for FY11 has raised the minimum turnover tax rate from 0.5% to 1%. This, if implemented would bode negative for SSGC's earnings outlook. From our discussions with the management, the company has sent in a request to the Ministry of Finance (MoF) to deliberate on this issue and is hopeful of a positive response from the latter. We are not incorporating this change though, till a decision on the final tax rate is made. Running a sensitivity analysis on the possible tax rates, we arrive at the following results:

Possible change in turnover tax rate

Turnover Tax	EPS/LPS (Rs)	
	FY11F	FY12F
0.5%	0.59	0.83
1.0%	(0.27)	(0.05)

Source: JS Research

FY10 UFG loss estimate revision

UFG loss levels during winters predictably tend to be elevated however, the same were abnormally higher in 3QFY10 – arrived at 10.9%. This accounts for the loss of Rs0.79 per share recorded in the 3QFY10. Given the unexpectedly high UFG losses in the 3QFY10, we have adjusted our full year estimates to 8.6% from 7.6%. We consider the 4Q's UFG loss percent to be of a lower quantum in comparison, since the seasonality effect is absent and because the management is making efforts to contain losses in this period as learnt through discussions with the same. This in turn brings our FY10E estimate down to a loss of Rs0.23 per share.

Recommendation: 'Sell' maintained

The stock is currently trading at a 37% premium to our revised target price of Rs12 (from Rs14 previously) offering an FY11F P/E of 28x and PBV of 1.15x. Dividend payout during FY10 and FY11 appears to be a bleak possibility owing to the persisting circular debt and the inflated finance cost the company has been paying as a consequence. We therefore reiterate our 'Sell' stance on the scrip.

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Also in focus

Agri disbursement target may fall short of target

Agri credit disbursements rose 6.4%YoY to Rs215bn in the 11MFY10 (Jul-May) compared to Rs202bn lent out in the same period last year. Overall disbursements by the five major banks jumped 9% to Rs107bn, while loans from Zarai Taraqiati Bank Ltd rose 7%YoY to Rs67.7bn. With just one month left in the current fiscal year, SBP's target of Rs260bn now seems difficult to achieve. Overall disbursements in FY09 stood at Rs233bn.

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