

January 30, 2009

Pakistan Market**MORNING BRIEFING****Car Assemblers: Downward revision/'UW' maintained** KSE100 Index Closing 5183.22 ↑ (+43.29)

The current fiscal year ending in June 2009 will turn out to be more depressing and challenging for the local car assemblers than initially estimated by us. With the weakening economic fundamentals and credit crunch, auto demand is likely to remain depressed in the short run.

In our report titled 'Weakening Demand' dated Aug 29, 2008 we estimated 30% decline in car sales in FY09. After looking at the trend of last 6 months, we now believe that car sales will decline by 46-48% in FY09. Thereafter in FY10 a recovery of around 12% is likely. Declining sales and rising input costs amid appreciating yen will cause earnings of our sample companies to decline sharply in FY09. Moreover, a positive impact of falling steel prices (a major cost constituent of the automobile industry) has also been offset by Rupee devaluation. We have revised down earnings of our two auto companies in the range of 5-32%.

Car sales already down 48%

Political and economic instability, hike in car financing rates and most importantly increase in the car prices are the major contributor in the massive decline of auto demand. In the first 6 months (Jul – Dec 2008) of FY09 car sales have performed dismally depicting a decline of 48% to 36,079 units over the corresponding period last year. Therefore, we believe local car sales to decline more than our initial estimate. In the long term, we expect things to improve and expect a CAGR of 14.6% over FY10-13 as car penetration is lowly at only 11 cars per 1000 people in Pakistan.

Imported car sales will also decline

With government looking to harmonize its policies to curb luxury spending with the aim to reduce import bill, sales of imported cars have also depicted a major decline. One such measure taken recently by the government was the reduction in the monthly depreciation rate of imported cars from 2% to 1%. This measure will make imported cars more expensive which will dent the already sluggish demand of imported cars.

Though it bodes well for the local car assemblers, the impact is expected to be minimal as the current market share of imported cars is a meager 4-5%. Considering the above mentioned factors, we expect FY09 imports to decline by 40%, from our initial estimates of 29%.

Revised earnings forecast for Indus and Pak Suzuki

After incorporating our demand assumptions for the auto sector, we have revised our forecasts for Indus Motor and Pak Suzuki as given below:

Table: Revised Earnings forecasts (EPS Rs)

	Old	New	%Δ	Old	New	%Δ
	2008E			2009F		
Pak Suzuki Motor	8.6	8.2	-5%	8.8	6.3	-29%
	FY09E			FY10F		
Indus Motor	11.6	8.0	-31%	14.8	10.1	-32%

Source: JS Research

We maintain our 'Underweight' stance on local car assemblers due to their falling demand and increase in cost of production. Moreover, we have downgraded our 'Buy' recommendation to 'Hold' for Indus Motor while maintaining our 'Sell' recommendation on Pak Suzuki.

atif.zafar@js.com

92 (21) 111-574-111(Ext. 3118)

Also in focus**China's US\$500mn boost reserves to US\$10.2bn**

According to latest data released by State bank (SBP) forex reserves rose by US\$260mn in the week ending Jan 24, 2009 to US\$10.2bn. While SBP reserves rose by US\$270mn to US\$6.9bn on account of US\$500mn received from China for Balance of Payment support, reserves of the commercial banks declined by around 11mn to US\$3.4bn. With IMF officially announcing that Pakistan has met initial targets set by fund, probability of second tranche of around US\$800 in March 2009 has increased considerably. We believe further inflows from IMF and other multilateral donors in the coming months would help stabilize forex reserves to around US\$11bn by June end 2009.

JS Global Capital Limited

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

Research:

Tel: +92 (21) 2799005

Fax: +92 (21) 2800163

js.research@js.com

Fixed Income Sales:

Tel: +92 (21) 2799541-44

Fax: +92 (21) 2800165

tariq.usman@js.com

Equity Sales:

Tel: +92 (21) 2799513

Fax: +92 (21) 2800166

junaid.iqbal@js.com

Corporate Finance:

Tel: +92 (21) 2799005

Fax: +92 (21) 2800166

azhar.iqbal@js.com

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