

October 30, 2009

## Pakistan Market

## Economy FY09: SBP's perspective

MORNING BRIEFING



KSE100 Index: Closing 9169.00 ↓ (-82.84)

Yesterday, SBP released its assessment for Pakistan's macros in FY09. SBP claims tight fiscal and monetary policies have tampered aggregate demand pressures in the economy. The decline received a further push from energy shortages, risk-averse behavior of financial institutions and weak investor confidence. The slowdown in aggregate demand can be gauged from the 8.2% contraction reported by LSM, highest since 1991. The weak domestic demand coupled with fuel and energy price pass through has resulted in a massive reduction in twin deficits to 10.5% of GDP in FY09, compared to 16% reported in FY08. As a consequence of contained deficit and in turn low budgetary borrowing from SBP, inflationary pressure began easing and thus provided SBP room to ease its monetary stance by 100bps in April and then again August 2009. However, the risk of resurgence in commodity prices, fiscal slippages and delay in foreign inflows has deterred SBP from further easing its policy stance.

### SBP macro expectations for FY10

Inline with our estimate, SBP expects 2.5-3.5% GDP growth in FY10 vs IMF's projection of 2%. The recovery is led by 1) pick in domestic demand, 2) easing of LSM contraction, and 3) resolution of circular debt. Additionally, the re-stocking of low inventory levels coupled with export growth recovery will lead to gradual recovery. The external sector outlook is set to improve, aided by a robust trend in remittances and gradual export recovery. However, the risks related to higher commodity prices and delays in anticipated external flows remain intact. SBP anticipates fiscal slippages led by a surge in expenditures due to security related operations and below par tax revenue collection. The central bank expects a current account deficit and a fiscal deficit at around 5.2%, a level we have seen in FY09. However, its inflation outlook for FY09 stands at 10-12% relative to 20.8% reported in FY09.

### SBP's view on price level & our DR expectation

SBP admits in the report that "A very encouraging development in the latter half of FY09 was that the core

inflation has also began to ease, although it is still high". However, there are risks that commodity prices and fiscal stimulus from budgetary expenditures may yet spark inflationary expectations again; hence, restricting itself from easing interest rates from here. Our view on inflation is slightly different from SBP's and we rule out the threat of inflation will be mitigated through keeping rates higher. Pakistan's inflation woes are expected to strengthen further unless we work on the supply side of the economy. This can be achieved only through rise in real investments in the agriculture, power and infrastructure of the economy. As highlighted earlier, current decline in aggregate demand was boosted by risk-averse financial institutions and a lower private sector appetite. Therefore, to stimulate investment demand, SBP should soften its policy stance. We expect SBP to reduce discount rate by 1ppt each in November and January policy reviews, as the balance of risk clearly favors monetary easing.

#### Major Economic Indicators: Annual Plan

	FY09	FY10	
		Targets	Projections
<b>Growth rates in percent</b>			
GDP	2.0	3.3	2.5 - 3.5
Avg. CPI inflation	20.8	9.0	10.0 - 12.0
Monetary assets (M2)	9.6	-	12.0 - 13.0
<b>Billion US Dollars</b>			
Workers' remittances	7.8	7.0	7.5-8.5
Exports (fob-BoP data)	19.2	19.9	18.0-19.0
Imports (fob-BoP data)	31.7	28.7	30.5-31.5
<b>Percent of GDP</b>			
Fiscal deficit	5.2	4.9	4.7 - 5.2
Current a/c deficit	5.3	5.3	4.7 - 5.2

Source: SBP Annual report FY09

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### Also in focus

#### PTCL expected to post EPS of Rs0.46 in 1QFY10

PTCL is expected to announce its 1QFY10 earnings today. We expect the company to post earnings of Rs2.35bn (EPS Rs0.46) as compared to Rs3.16bn (EPS Rs0.62) in the corresponding period last year, down 26% YoY.

We believe the decrease in earnings to be attributable to the declining fixed line revenues, which is the largest contributor to the company's top line. However, this is expected to be negated partially by the rising revenues from the broadband, WLL and other value added services offered by the company. Moreover, international revenue is expected to improve on the back of lower APC rates (thus higher volumes & lower grey traffic) and rupee depreciation against the US\$.

We expect revenue to show improvement from 2Q onwards on the back of rigorous media campaign and seasonal effect. We maintain our 'Buy' stance on the scrip which currently trades at an FY10E PE and EV/EBITDA of 9.5x and 2.4x respectively. We expect no payout with the result.

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