

September 30, 2009

Pakistan Market**MORNING BRIEFING**
Monetary policy review (Sep–Nov): Rates unchanged KSE100 Index: Closing 9475.48 ↑ (+65.90)

Inline with consensus estimates, Monetary Policy Committee (MPC) has decided to keep Policy rate unchanged at 13%. The 'wait and watch' approach was due to the consideration of inflationary risks, resolution of electricity tariff, timing of foreign inflows and in turn risk related to fiscal consolidation. Though the current policy rate is adequately addressing the aforementioned risks, SBP's reaction to addressing liquidity woes is yet muted, in our view.

The prevailing tight liquidity situation can also be verified from yesterday's discounting of Rs28bn. We believe this should have a major bearing on the market interest rates and all tenors are expected to go up by 10-15bps.

MPS key takeaways:

- Pakistan's inflation (YoY) and balance of payment position has improved, while fiscal and real sector performance remains fragile.
- The outlook for real sector can be gauged from weak credit disbursements to the private sector. However, SBP expects improvement in the external account and reversal in the global economic growth should augur well for the economy.
- The positives mentioned above are unlikely to make a major difference until electricity shortage and stressed fiscal position are overcome.
- The upbeat foreign inflows led by IMF disbursement helped strengthened reserves, but will remain the source of concern for government borrowing. Non realization of official flows could pose a serious dent to fiscal consolidation. This can be seen from last year's revenue, expenditure and in turn fiscal deficit slippage of 0.9% to 5.2%.

The impact:

1. Reversal of interest rates expectation is likely to faint the chances of reversal in fix investments.

2. Higher appetite of government borrowing should shift yield upwards by 10-15bps.
3. High Leverage Company's profitability will be undermined due to higher KIBOR.
4. Risk of defaults amid higher financial charges, lower domestic demand and inflation.

JS interest rate outlook

Recent higher MoM inflation is likely to reverse due to the arrival of sugarcane crop and consolidation in the fuel prices. This should keep full year inflation at 8-9% in FY10 compared to 21% in FY09. The disbursements of approximately US\$1.0bn from Friends of Democratic Pakistan and continuation of foreign portfolio investments should ease the liquidity concerns and prompt SBP to ease monetary stance. We expect 100bp cut each in November and January policy reviews.

Table: Monetary aggregates

(Rs mn)	since 1st July to	
	12-Sep-09	13-Sep-08
Broad Money (M2)	(37,214)	(60,591)
Net foreign assets of Banking system	125,918	(143,453)
Net domestic assets of Banking system	(163,131)	82,862
Net govt. sector borrowings	159,634	126,342
from SBP	88,208	179,443
from scheduled banks	75,756	(32,445)
Credit to private sector	(68,788)	(2,494)
Credit to public sectors enterprises (PSEs)	(19,640)	48,132

Source: SBP

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Also in focus**Local oil price review today**

Government is likely to reduce retail oil prices of petroleum products with effect from October 1, 2009. Prices are expected to go down by Rs1.5-4 per litre in line with the reduction in international oil prices. Currently crude oil prices are hovering in the range of US\$67. The downward revision in oil prices would be slightly negative for OMC's and refineries since their margins are linked with the international oil prices. We maintain our 'Market-weight' stance on OMC's and refineries.

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