

December 31, 2009

Pakistan Market

MORNING BRIEFING



Global recovery through the commodity eye

KSE100 Index: Closing 9507.95 ↑ (+97.29)

Typical economic theories teach us that commodity prices surge during the period of over heating, when inflation tends to pick up in tandem with growth. This is contrary to what we saw in 2009, as the global economy continued to encounter a deflationary scare with growth and inflation persistently heading south. Typically, central banks as well as governments should opt for stimulus policies to deal with this scare and by default, bonds should be the best asset class and commodities should be least preferred. As we close down 2009, we note unusually higher returns in global stock and commodity markets; the former providing a 32% return, while the latter surged by 22%. Infact, a few commodities, mainly leading indicators of global recovery, have outperformed the equity and bond markets by a wide margin (e.g. oil +95%, copper +125%, sugar +93%, cotton + 30%, and gold + 23%). This suggests that 2009 has turned out to be a year of "stabilization" instead one of "great or deep recession" as was widely anticipated. As Pakistan's economy is in the recovery mode, the increase in commodity prices (which comprise over 69% of total imports), mainly of oil and industrial metals is not good news in general.

Global economy: the year 2009 revisited

The financial markets were close to collapse, economic activity, industrial production and foreign trade activities diminished even faster than the 1930 Great Depression, post the panic sown by the Lehman Brothers' bankruptcy. Interestingly, the meltdown occurred within a span of a few months and off late, leading industrial economies are showing signs of recovery following the resilience demonstrated by emerging economies like China, India, Brazil and Indonesia. This was only made possible due to a well coordinated, timely and a broad based government response, which remains unparalleled. The central banks slashed interest rates, sovereign guarantees were being granted to commercial and investment banks, while a massive injection of liquidity in toxic companies took place. Moreover, fiscal stimulus in shape of

cash coupons and/or unemployment benefits had a great influence on the reversal of the global panic, in our view.

Future risks to watch out for

Though recovery is on the cards, massive stimulus plans have raised question marks on different industrial economies ability to retire their extra-ordinary compounded debt levels, given their falling output, declining consumption, and ageing population. The governments of Britain, Spain, Ireland, Greece, Latvia and the US are already under massive pressure to maintain their credit worthiness. The Dubai debacle and its effects on global financial markets is just a trailer, we saw recently. We believe, global economies have played their last wild card and having run out of further rescue options, any upset or default may lead to another collapse. Therefore, careful consideration is required to withdraw the stimulus packages alongside balancing the threat of global inflationary scare in the back drop of rising commodity prices.

Pakistan Macro: A year of stabilization

Post the commodity shock, Pakistan has undergone massive structural adjustments mainly led by IMF's guidelines. Though the fruits of reforms are evident from the recent macro data as well as the 'Stable' outlook given by the sovereign rating agencies, the deteriorating law & order situation and ongoing global recessionary woes have prolonged the prospects of recovery, in our view. The expected liquidity stimulus was delayed due to the non-fulfillment of Friends of Pakistan's commitments, US's late approval of the Kerry-Lugar bill and a lag in the release of the Coalition Support Fund. This in turn affected domestic liquidity and kept short-term rates at higher levels, despite SBP reducing the policy rate by 250bps in 2009. Nevertheless, we term year 2009, as a year of achievement, as Pakistan's establishment has taken bold macro economic initiatives to eliminate long-standing structural flaws by doing away with fuel & electricity tariff subsidies, introducing banking and tax sector reforms and more. Interestingly, the reforms carried out in 2009, have strengthened Pakistan's economic governance when

compared to global economic power houses like China and India, as both continue to subsidize power & fuel in their respective countries. The International Finance Cooperation assigned Pakistan the 85th rank vis a vis China's 89th and India's 133rd among countries in terms of 'ease of doing business' in 2010.

Global Financial Markets vs Commodities performance

Commodities	YTD Δ	Goobal Fin. Mkts	YTD Δ
Oil	94.5%	MSCI EM	73%
Sugar	93.3%	MSCI EM Asia	68%
Cotton	29.6%	Asia Ex Japan	66%
Gold	22.7%	Asia Pacific Ex Japan	66%
CRB Index	21.6%	Asia Pacific	34%
Coal	-23.5%	MSCI World	32%

Source: Bloomberg & MSCI Barra

muzzammil.aslam@js.com
92 (21) 111-574-111 (ext. 3035)

Also in focus

Manzalai production up 17%WoW due to base effect

As per weekly production numbers released by PPIS (Pakistan Petroleum Information Service) yesterday, average oil and gas production from Manzalai for the week ending on December 22, 2009 stood at 3,874bpd (up18%WoW) and 210mmcf/d (up 16%WoW), respectively. We believe, this WoW growth was mainly due to the 1-2 days forced shut down of the field's operations during the week ending December 15, 2009. Assuming the field to be operational for 6 days in the week ending December 15, the average oil and gas production arrives at 3,843bpd and 211mmcf/d, respectively indicating a relatively flat production flows in the last two weeks.

JS Global Capital Limited

6th Floor, Faysal House, Main Shahrah-e-Faisal, Karachi
JS RESEARCH IS AVAILABLE ON BLOOMBERG, CAPITALIQ & THOMSON REUTERS