January 2012

Pakistan Strategy 2012

'In the middle of difficulty, lies opportunity'

- Albert Einstein

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Content

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Pakistan Politics 2012

'We are all Revolutionaries now, addicts of change'

Pakistan Politics 2012

A 'Change' in the offing … amid extreme Noise!

- After an increasingly noisy few years, Pakistani politics enters a thrillingly suspenseful phase (last year of present setup's term) with a change in its run-of-the-mill and repeatedly-tested-and-failed political party-theme as new political alliances flex muscles for political power.

- Although the current political setup has been mired in political and financial scandals and unable to deliver on its election promises, there seems low possibility of a change through any extra unconstitutional measures.

- Though better than the entire series of all of the civilian government regimes since country's independence, most of which fell prey to dictatorship, and given current political circumstances (Memogate scandal), completion of the current Parliamentary setup looks increasingly vulnerable either.

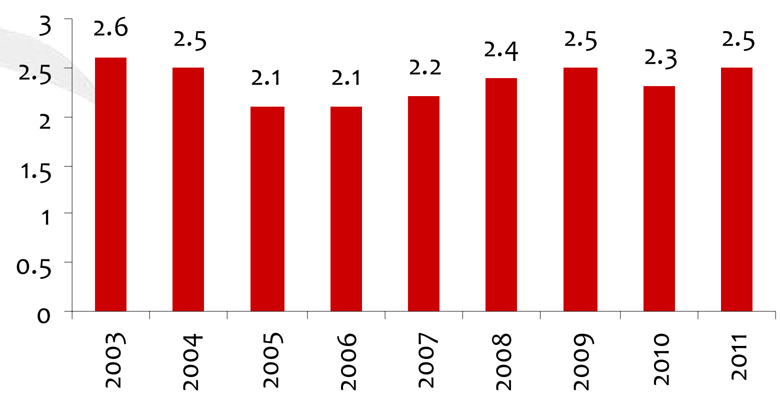
- A considerably improved law & order situation, a not so bad showing on TI's corruption index now, a few tax reforms beginning to yield results and an increased accountability by vibrant media, bode well for the country in the coming year.

- However, there are more bitter pills yet to be swallowed - electricity price gap more with structural shifts, low and weak tax regime, gradual phase-out of subsidies and large non-productive expenditures that need to be cut inevitably.

Recent Civilian Government Terms in Pakistan

Premier	From	To	Term
Zulfiqar Ali Bhutto	14-Aug-73	05-Jul-77	3.8 years
Benazir Bhutto	2-Dec-88	6-Aug-90	1.6 years
Mian Nawaz Sharif	6-Nov-90	18-Apr-93	2.5 years
Mian Nawaz Sharif	26-May-93	8-Jul-93	1.4 months
Benazir Bhutto	19-Oct-93	5-Nov-96	3.0 years
Mian Nawaz Sharif	17-Feb-97	12-Oct-99	2.7 years
Syed Yousaf Raza Gillani	**25-Mar-08**	**Till Date**	**3.8 years**

Pakistan's Score on TI's Corruption Index



Higher score denotes lower overall corruption

Pakistan Politics 2012

Foreign Relations, Overall Governance are the Key!

- Relations with the US have already been categorized as a marriage gone sour, which needs to be redefined at this critical juncture that will restore Pakistan's relationship equilibrium not only particularly with the US but the West as well.

- After having provided MFN status to India, regional cooperation and politics will significantly improve while economic coordination is expected to improve documented trade and commerce amongst the ever-growing Asia Pac region including Iran and Afghanistan.

- Though a combination of the so-called new lot of politicians is widely anticipated to rein in country's charge next while repairing relations with the West, it will however need a sound economic team to address economic woes facing Pakistan.

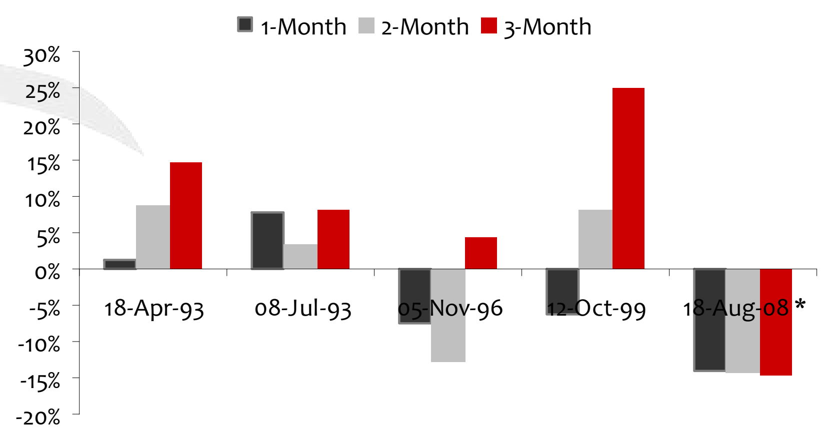
- Dictatorship regimes in Pakistan have always been good at delivering better economics. However, the stated position of the current military leadership being supportive of democracy is encouraging.

- Interestingly, over the last two decades, Pakistan equities have reacted positively, for the most part, to any significant change in country's political setup that has taken place.

Government Regime vs Economic Growth

Decade	Regime	GDP Growth (%)
60s	Military	6.8
70s	Democracy	4.8
80s	Military	6.5
90s	Democracy	4.6
00s	Military	5.4
10s	Democracy	2.6
60s	Military	6.8
Average Growth	**Military**	**6.2**
Average Growth	**Democracy**	**3.8**

KSE100 Historical Behaviour to Gov't Falls



* Plunge in KSE during Aug08-Jan09 was primarily due to imposition of price floor at KSE and foreign outflows amid global economic fall triggered by collapse of Bear Sterns in late 2008

Pakistan Economy 2012

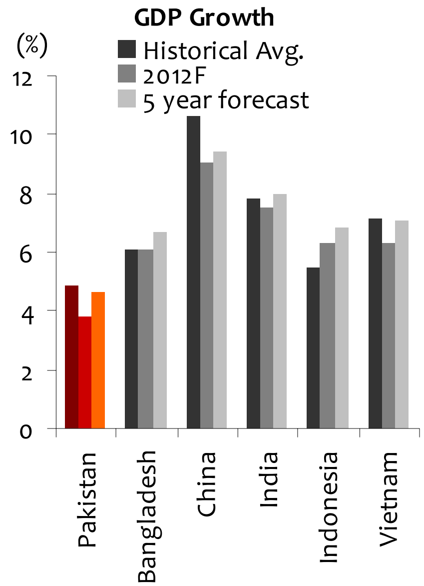
The edge of the road

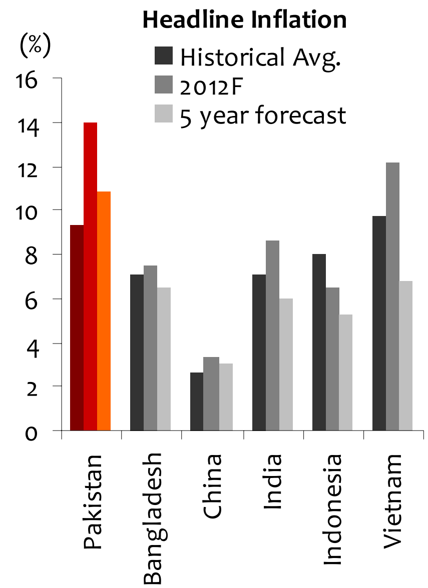
Underperforming the Region

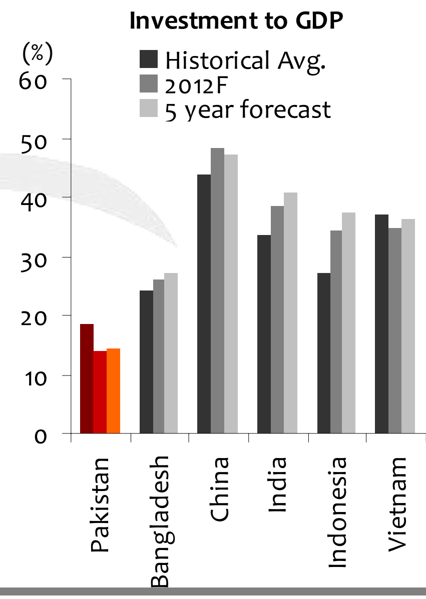
- Challenged by its own set of problems, sustained economic growth remains a far cry in Pakistan, as it continues to lag region's. Initially targeted to grow by 4.2% during FY12, persistence of numerous issues including partial floods in the country coupled with ongoing energy crises makes it difficult to achieve this target. The estimate was later revised to 3.6% while SBP also projects the same to stay in the range of 3-4%.

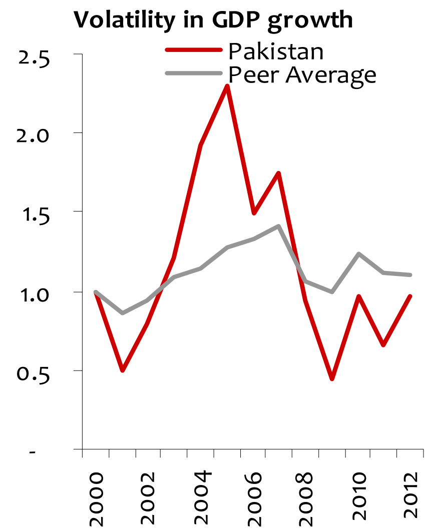
- In terms of comparison with the region, Pakistan has been underperforming in many ways. A persistently high inflation scenario chained with a lower investment-GDP ratio has kept the country behind regional peers in terms of growth. Consistency in growth has also remained in question as during the past decade, Pakistan's real GDP growth remained twice as volatile as that of regional peers'.

- Contribution of private consumption has been rising much more rapidly in the overall aggregate demand. On the other hand, investment has been showing persistent decline, leading to widening gap between demand and supply. During the last three years, the contribution of private consumption in aggregate demand growth surged to average 97% compared to 2001-08 average of 69%. Near panicky rise in consumption is also an indication of greater uncertainty associated with future inflation in the country.









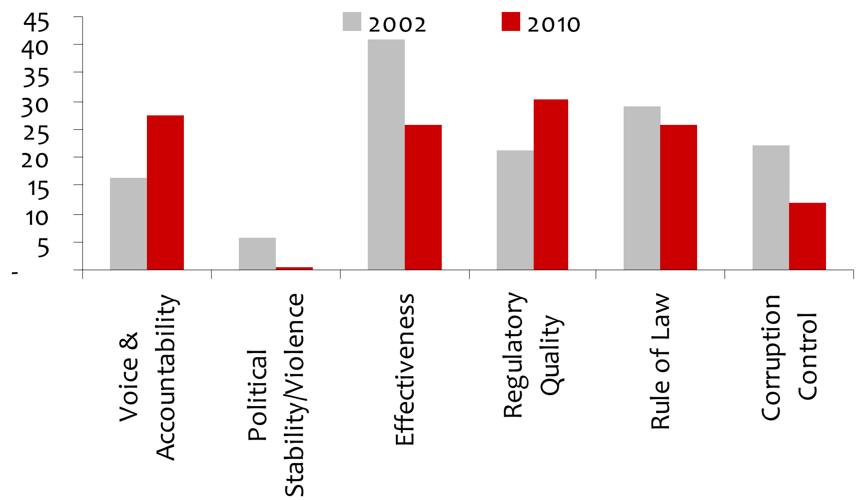
Governance – a Key Source of Distortion

- We have been arguing time and again that subdued economic performance in comparison with the region is not necessarily an indication of resource mismatch. Instead, Pakistan continues to stay rich in terms of favorable geography and demographics, indigenous agriculture resources, untapped energy potential and a strong service sector.

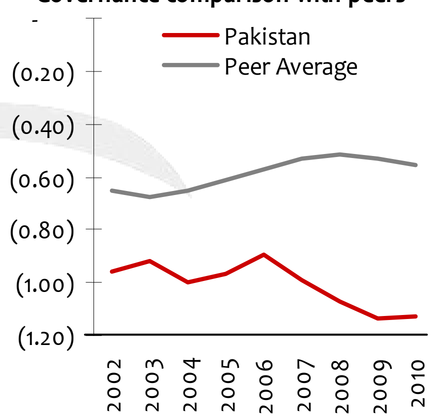
- The problem, in our view, lies in the ability to mobilize resource in a timely and efficient manner. Evidence could easily be traced to analyze the poor economic performance with lack of governance. As per 'Governance Indicators' compiled by the World Bank, various governance indicators have deteriorated in the country, foremost being 'political stability and absence of violence and terrorism'. Under the said category, country's ranking dropped to second lowest in the world in 2010, reaching almost zero (indication of being lowest in the world).

- Although none of the regional peers shows exceptional governance under the indicators mentioned (-2.5 being weakest, while peer average stays negative), Pakistan has generally stayed behind countries including China, India and Bangladesh, in terms of governance. Furthermore, the relationship between GDP growth and governance, although weak, still shows positivity (i.e. higher growth marked in years with better governance).

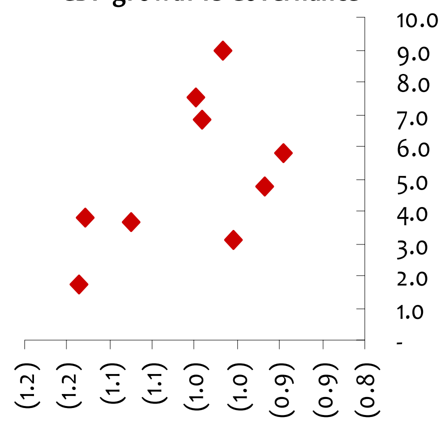
Pakistan Governance Indicators



Governance comparison with peers



GDP growth vs Governance



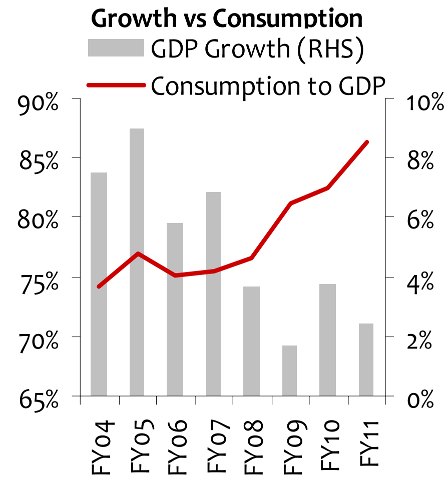
Hope at the Edge!

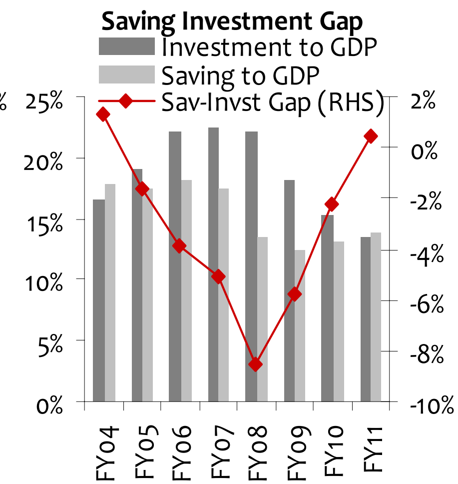
- Lengths could be filled with how directions of fiscal and monetary policies along with performance of real and external sectors, have impacted Pakistan's performance in recent times.

- Factors that have been truly distressing include persistently high inflation (general prices inflated by 54% during the last four years, against 30% in previous relative period and 18% earlier than that). Next in line is the rising pressure on currency, which is linked more closely to the energy shortage. Perhaps the bigger question is not 'why' such problems have emanated, but 'how' these should be addressed in the future.

- Steps have been taken to revive the economy's energy output including investment initiative in generation through coal, import of natural gas from Iran or Turkmenistan, measures to conserve fuel through additional surcharges, investment initiatives by local refineries and introduction of new policies to encourage exploration and production of gas. But at a time when gas demand-supply gap is estimated to have reached ~2500mmcfd, damage to growth prospective would already be done by the time new investment initiatives are materialized.

- We expect the country to continue to lag the region in terms of economic performance at least in the near term. However, our long term view on the economy is bullish, backed by our conviction in better governance ahead and efficient utilization of indigenous resources, as a result.





Projected Demand Supply Gap of Natural Gas

mmcfd	FY12	FY13	FY14	FY15	FY16
Net Demand	5,497	5,670	5,788	5,820	5,970
Add: UFG, T&D Losses	279	307	320	322	330
Internal consump.	49	55	57	54	54
Gross Demand	5,825	6,032	6,165	6,196	6,354
Total Supply	3,367	3,380	3,860	3,583	3,333
Shortfall	**2,458**	**2,652**	**2,305**	**2,613**	**3,021**
Expected Imports	300	500	763	987	1,250
Shortfall after imports	**2,158**	**2,152**	**1,542**	**1,626**	**1,771**

Economic Indicators

(USD bn)	FY11A	FY12T	FY12E
GDP Growth	2.4%	4.2%	3.6%
Average CPI	13.7%	12.0%	12.0%
M2 Growth	15.9%	N/A	14.0%
Remittances	11.2	12.0	12.7
Export	25.4	25.8	25.0
Import	35.7	38.0	40.5
Fiscal Deficit	6.6%	4.0%	6.0%
C/A Deficit	-0.2%	0.6%	2.0%

Capital Markets 2012

In a world of pessimism, search for what could go right!

Capital Markets Investment Theme 2012

Pessimism all around-Search for what could go Right

- These are remarkable times to become an investor and investment professional! Following decades of overspending, we are watching Europe melt down and the American realm decline faster than expected. Their unimaginable debt burden has accelerated the power shift from the West to the East.

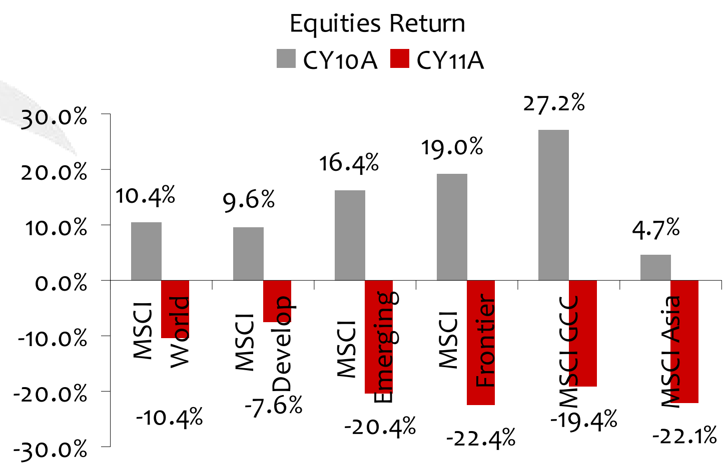
- High-risk investment returns in CY11 have either been red or were too low to cover even transaction costs and the pessimist continued to chuckle while expecting more negatives ahead. Point of nervousness today however is not the same as it was in 2010 when portfolios excitingly included Gold (so-called safe heaven), U.S. (immune economy) and China (the Salvationist).

- In recent decades, markets probably have hardly seen a time when common views are so universally pessimistic. Certainly, this pessimist's feel is all valid given the macro events of the day (both local and global) and the extreme market instability affecting all investment classes' returns, as a result.

- Although the value-loss fear is very much logical and real as well, it is no less valuable for investors either. Thus, a balanced perspective has to find its way through. So, we recommend investors to consider all the information to see what could go right in 2012, as it is always the negative stuff that finds you the right path, the positive doesn't!

Return of various Asset Classes during 2011

Asset Class	CY11	CY10	Cumulative
Equities			
MSCI Developed	-8.8%	9.6%	0.8%
MSCI Emerging	-20.7%	16.4%	-4.3%
MSCI Frontier	-22.5%	19.0%	-3.5%
Currencies			
USD/EUR	3.6%	7.0%	10.5%
YEN/USD	-11.2%	50.7%	39.5%
Commodities			
World Commodities	5.5%	35.9%	41.4%
Fixed Income			
JP Morgan GBI	6.7%	6.4%	13.1%



Capital Markets' Regional Assessment

Pakistan Market still at an Advantage to the Region!

- Despite equity sell-off all across the globe, especially the emerging Asia Pacific region, which attracted most of the foreign flows last year, Pakistan equities managed to holdback foreign investors' sell-off to such an extent that it was the lowest-foreign-outflow market amongst regional peers in 2011.
- Though foreign outflows from the Asia Pacific region in 2011 were recorded at a noticeable scale, they fell deeply short to catch up with the level of inflows that flooded regional markets in 2010. Foreign inflows in CY10 were at a whopping USD63,5bn while outflows during 2011 were only ~one-fifth or USD14.3bn.
- Reasons for the low-scale foreign outflows during 2011 can be cited as better fiscal balances, higher as well as sustained economic growth, strong corporate earnings and payouts in the Emerging Asia region, which remains a blessing given grim economic outlook of the US and Europe for foreseeable future.
- Thus, foreign outflows from the region have been more currency-led temporary-phenomenon than due to any shift in economic fundamentals. It is quite evident from the fact that, most of the emerging markets' currency depreciation vs USD led to fund outflows with exception of Vietnam and India while inflows destined at countries with lower currency depreciation.

FOREIGN FLOWS (USD mn), RETURNS (in USD) ASIA PACIFIC REGION

	Foreign Flows		Equity Returns	
Country	**CY11A**	CY10A	CY11A	CY10A
India	(496)	28,425	-38.0%	25.2%
Indonesia	2,853	2,195	4.0%	68.2%
Pakistan	(127)	514	-17.1%	18.6%
Philippines	1,329	1,211	-3.2%	85.5%
S. Korea	(8,584)	19,657	-12.8%	31.1%
Taiwan	(9,246)	9,076	-23.3%	25.4%
Thailand	(167)	1,881	-5.6%	58.5%
Vietnam	95	602	-39.7%	14.9%
Total/Average	(14,342)	63,561	-16.9%	40.9%

Regional Currency Depreciation vs. USD vs. Foreign Flows (USD mn)

Country	Currency Depreciation	Foreign Flows
India	18.7%	(496)
Indonesia	0.9%	2,853
Pakistan	5.0%	(127)
Philippine	0.2%	1,329
South Korea	2.3%	(8,584)
Taiwan	4.1%	(9,246)
Thailand	5.3%	(167)
Vietnam	7.9%	95
Average/Total	5.5%	(14,342)

Reasons underpinning Growth in Pak Equities

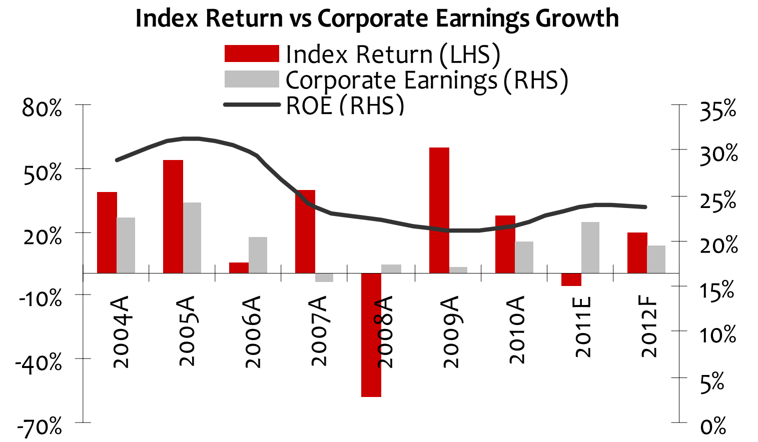
Real Index Growth to outshine Real GDP's in 2012

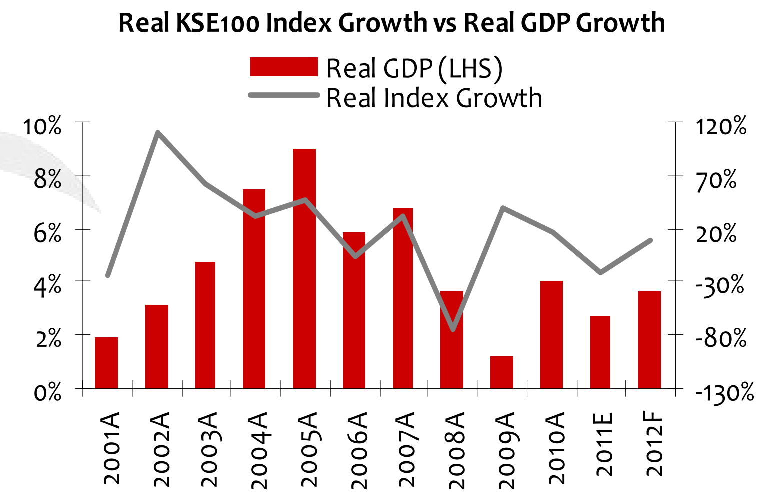
- Dusting through historical records reveals nominal GDP of the country averaged at 15% during CY01-CY11A period while the real GDP stood at an average 5%. As a result, the KSE100's real return also stood at a solid 18% on average in the last decade.

- In addition, RoE and cash payouts have also been stable during the period. Similarly, with slightly higher GDP growth in FY12 despite double-digit inflation (amid floods and towering energy shortages), we expect earnings' outperformance to continue in 2012 with corporate earnings estimated to grow by 13% YoY while KSE100 index is forecast to provide a 9% real capital gain versus the real GDP growth projection of 3.6% for FY12.

- Thus, we expect Pak equities to rebound this year albeit with heightened volatility on the back of the same but increased noise on the political front, but with an expected resolution of the lingering issues of the CGT to an extent, and an effective implementation of the margin financing product.

- It was interesting to see that despite higher expected earnings growth last year (24% YoY), KSE100 ended with a negative return (5.6%), lending enough credence to the resolution of key issues of CGT and MTS that massively chopped down average volumes while making price discovery difficult for investors.





Fundamentals underpinning Growth in Pak Equities

Earnings Growth to continue with E&Ps, Ferts, Banks

- It is interesting to note that corporate earnings growth has kept momentum (8% CAGR in the last 6 years) despite economy not catching up with its underlying potential and scaling energy issues, stubbornly high inflation and double-digit interest rates. This is understandable taking into account market capitalization-GDP ratio (currently at 22%), which signifies very low economic coverage by the listed sectors at the KSE.

- Entering 2012, we expect earnings growth to turn even better than the last 6-year average (13% in 2012 versus 6Y CAGR of 8%), which is expected to be largely triggered by key bluechip sectors i.e. Oil & Gas (E&Ps), Fertilizer, Cement and Banking.

- Rising oil prices will benefit oil sector, while improving volumes of fertilizer sector will yield better earnings and payouts. Cement sector will reap benefits amid improving local prices and relatively higher amount of development expenditures that is expected to be incurred by the gov't in last year of its term.

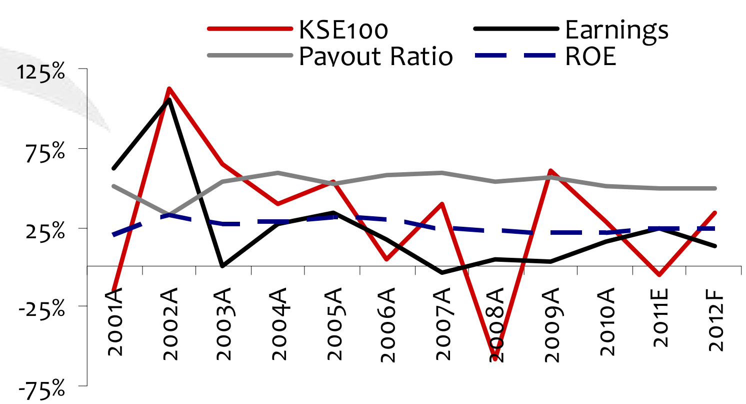
- Despite swelling circular debt, higher or extraordinary cash payouts from the gov't-owned entities i.e. PPL, PSO, OGDC, PTC, NBP and few others are expected owing to rising fiscal deficit and the need to finance it. This is expected to attract the large portion of the dividend-loving investors to the market.

CORPORATE EARNINGS GROWTH

	Years*							
Sector	**2006A**	**2007A**	**2008A**	**2009A**	**2010A**	**2011E**	**6Y CAGR**	**2012F**
Power	-40%	-5%	38%	-11%	13%	12%	8%	-3%
E&P	44%	4%	14%	19%	-3%	18%	10%	35%
Fertilizer	0%	11%	27%	20%	47%	64%	32%	13%
OMCs	41%	-40%	155%	-95%	1353%	47%	12%	-19%
Banking	32%	2%	-9%	14%	16%	23%	8%	7%
Textiles	-11%	-46%	249%	-77%	186%	61%	15%	-29%
Cement	43%	-23%	-29%	102%	-41%	26%	-4%	55%
Refinery	8%	33%	146%	-79%	34%	157%	19%	-30%
Chemicals	-35%	23%	4%	10%	19%	-10%	8%	-17%
Telecom	-22%	-25%	-85%	324%	2%	-20%	8%	-10%
Sample	**18%**	**-4%**	**4%**	**3%**	**16%**	**25%**	**8%**	**13%**

*Based on InvestCap Universe **Fiscal Year used for the Companies not following Calender Year

KSE Return vs Corporate Fundamentals



Relative Magnetism for Pak Equities

KSE offers high Risks, but Returns are even Greater!

- While global equities are experiencing severe battering, KSE100 still trades at deep discounts to regional peers (49% on PE, 28% on PBV, 23% on PCF while 67% on DY and a massive 87% on PEG). This is mainly due to greater perceived risks of i) double-digit inflation and interest rates, ii) one of the lowest GDP growth rates, and iii) soaring currency and political risks, along with low price discovery amid lingering CGT and MTS-related issues.

- Recall that higher risk entails greater return opportunities at the same time. While we expect a conservative 13% YoY earnings growth in 2012 (based on InvestCap Universe), Bloomberg's consensus earnings forecast for KSE100, stands at a vigorous 42% YoY for 2012 (at a wide margin to peer average). This is besides KSE's providing highest ROE at 33% and offering deepest discount at PEG multiples compared to regional rivals.

- As the earnings growth is primarily accounted for by investors above all and is an integral part of the emerging markets' fundamentals, KSE100's earnings growth is expected to substantially jack up this year too, while most of the peer countries like Taiwan, India and Sri Lanka, now seem to be exhausted in terms of earnings growth. Therefore, we expect KSE100's re-rating by the investors whereby market discounts may substantially narrow to their historical averages.

REGIONAL PEER COMPARISON 2012

Country*	P/E	PBV	PEG	PCF	DY	EV/EBITDA
Indonessia	11.50	2.33	0.75	5.85	3.06%	6.63
Vietnam	7.96	1.21	0.21	7.01	5.57%	6.37
India	10.70	1.82	0.29	7.41	2.23%	7.21
Philippines	11.63	1.81	0.44	8.05	3.30%	7.25
Sri Lanka	13.29	2.22	0.92	16.49	1.89%	8.88
Thailand	9.48	1.58	0.44	6.49	4.52%	7.06
China	10.49	1.77	5.00	8.30	1.04%	7.60
Taiwan	10.28	1.42	0.35	6.87	4.96%	2.93
S. Korea	7.31	0.93	0.15	4.30	1.75%	6.89
Peer Average	10.29	1.68	0.95	7.86	3.1%	6.76
Pakistan	**5.22**	**1.20**	**0.12**	**6.04**	9.45%	**4.13**
(Disc.)/Prem	**-49%**	**-28%**	**-87%**	**-23%**	**-67%**	**-39%**

REGIONAL PEER COMPARISON 2012

Country*	Egrow	ROE	DY	RGDP	CPI YoY	DR
Indonessia	38.5%	28.4%	3.06%	6.1%	14.35%	6.8%
Vietnam	47.6%	25.0%	5.57%	5.9%	18.13%	13.0%
India	15.4%	23.0%	2.23%	8.5%	9.14%	8.5%
Philippines	21.7%	23.5%	3.30%	10.9%	4.80%	4.0%
Sri Lanka	14.4%	20.5%	1.89%	8.4%	4.70%	7.5%
Thailand	29.4%	22.0%	4.52%	7.8%	4.19%	2.5%
China	37.1%	18.9%	1.04%	10.4%	3.30%	6.6%
Taiwan	2.1%	17.1%	4.96%	10.7%	1.01%	1.9%
S. Korea	26.5%	16.3%	1.75%	3.5%	4.20%	3.3%
Peer Average	25.9%	21.6%	3.1%	8.0%	7.09%	5.99%
Pakistan	42.2%	33.4%	9.45%	3.9%	12.00%	12.0%

*Bloomberg Consensus Forecasts (Pakistan Includes KSE-100 Companies)

KSE100's Target Return in 2012

Target Return Hinges upon Resolution of Key Issues!

- In 2012, investors need to stay close to where valuations are and should not repeat the same oversight made by those who missed rally in CY09 (KSE100 returned 60%), when investors focused exclusively on the bad political and economic news and eventually lost sight of the compelling valuations.

- Adjusting regional discounts to historical levels (avg disc 30-35%) laced with justified PE/PBV, EGrow and the Target Price models, gives us a weighted average index target of 13,656, 2,308pts higher by CY12-end, with a capital growth of 20% YoY.

- Since in 2012, higher volatility is expected to encircle KSE100's expected double-digit growth amid greater political clamor, we reiterate, KSE100 should provide at least 20% YoY returns in 2012, based on InvestCap Universe performance with a select of risk-adjusted fundamentally-stronger and potentially outperforming portfolio of stocks (given on the next page) .

- However, should the hanging sword of CGT-issue remain coupled with no positive development on the existing financing product, contrary to latest commitment of the SECP to put a resolve on both issues, and as other risks come into play as highlighted ahead, index should settle with a nominal growth of 9% YoY with year-end index target expected at 12,331.

Index Target 2012

Valuation Basis	Weight	Target
Justified PBV	10%	15,732
Justified PE	10%	16,592
Current PE Basis	5%	11,348
Earnings Growth	10%	13,268
Target Price Based	10%	15,267
PEG Ratio	10%	16,170
Regional PBV	10%	12,516
Regional PE	10%	13,504
Regional DY	10%	14,412
Regional PCF	10%	9,868
Regional EV/EBTIDA	5%	12,369
Average		**13,731**
Weighted Average		**13,656**
Index at Dec-11 end		**11,348**
Expected Return 2012		**20%**
Index Target with no CGT Resolution		**12,415**
Expexted Return with no CGT Resolution		**9%**

INVESTCAP UNIVERSE VALUATION SNAPSHOT

(%)	2007A	2008A	2009A	2010A	2011A	2012F
Earnings growth	-3.7%	4.1%	3.5%	15.9%	24.8%	13.4%
PER (x)	13.6	9.3	8.2	7.5	7.2	5.8
Dividend Yield	4.4%	5.7%	6.8%	6.8%	6.9%	8.6%
Earnings Yield	7.4%	10.7%	12.1%	13.3%	14.0%	17.3%
ROE	23.8%	22.3%	21.0%	21.5%	23.8%	23.8%
PBV (x)	3.0	2.0	1.6	1.5	1.6	1.3
Payout Ratio	59.1%	53.3%	56.3%	51.1%	49.6%	49.7%

Model Investment Portfolio 2012

Search for undervalued Stocks backed by strong long-term Fundamentals with timely Portfolio shift!

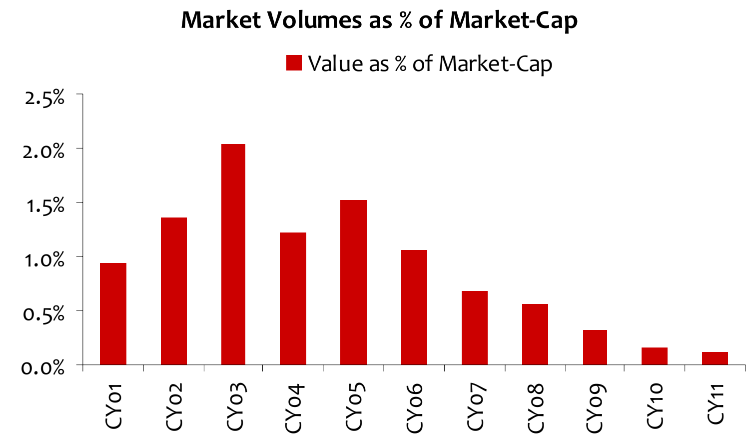
- Investors are recommended to hold stocks that are grossly undervalued, or at least relatively cheap at key multiples, with respect to their long-term fundamentals. On the contrary, investors need to have limited exposure to scrips that have become overvalued and risky for the short term. Investors should focus on two strategies at different timeframes in CY12. For 1HCY12, we recommend a mix of high-beta and defensive sectors i.e. Oil (E&Ps, OMCs, Refineries), Fertilizer (Faujis only), Cements, with a steady tilt towards few more interest rate-sensitive sectors like Textiles, Banks, Autos, Fertilizer (Engro) and Chemicals in the 2HCY12 (as monetary easing may be expected in 2HCY12) to outperform market expected returns in 2012.

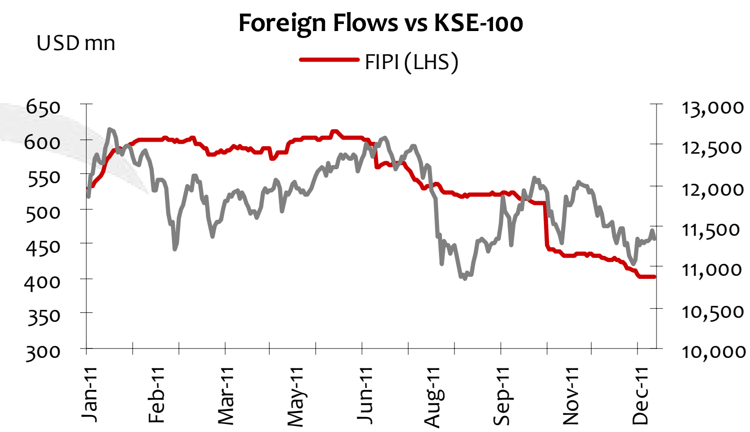
Scrip	Last Closing	Target Price	Upside Potential	Dividend Yield	Scrip	Last Closing	Target Price	Upside Potential	Dividend Yield
E&P					**Power**				
OGDC	151.62	173.95	14.73%	4.29%	HUBC	34.2	52.00	52.05%	15.32%
PPL	168.32	262.48	55.94%	8.91%	KAPCO	41.32	60.00	45.21%	12.17%
POL	346.45	485.60	40.17%	11.55%	**Textile**				
Refinery					NML	40.45	62.00	53.28%	5.63%
ATRL	107.65	149.94	39.29%	1.86%	NCL	17.86	37.00	107.17%	9.55%
NRL	242.69	322.66	32.95%	6.18%	**Cement**				
OMCs					LUCK	75.04	101.00	34.59%	5.33%
PSO	227.21	277.00	21.91%	6.60%	DGKC	19.03	27.00	41.88%	2.63%
APL	412.5	484.00	17.33%	10.91%	**Telecom**				
Fertilizer					PTC	10.39	23.36	124.84%	14.44%
FFC	149.54	251.00	67.85%	17.72%	**Banks**				
FFBL	42.43	76.00	79.12%	17.09%	UBL	52.39	67.00	27.89%	7.64%
ENGRO	92.7	210.00	126.54%	7.55%	MCB	134.6	185.00	37.44%	10.40%
Chemicals					NBP	41.05	50.00	21.80%	20.84%
ICI	120.27	153.00	27.21%	7.48%	ABL	53.87	73.00	35.51%	11.23%

Opportunities to keep an Eye on in 2012

Investment Drivers 2012

- First and foremost trigger would be early resolution of the CGT-related issues, which has been dragging market activity to dead levels. It would not only throw required volumes at the bourse for reasonable price discovery, but would also unlock index growth potential with earning-payout to have effective impact.
- Much-awaited financing product, Margin Trading System (MTS), has so far been almost absent to spur any volumes and provide impetus to the KSE100, mainly due to unrealistic margin requirements. SECP's commitment to make it usable in the coming days will surely provide recovery to equities in 2012.
- Though looks improbable in the near future, any cut in discount rate will provide support to equities while continuity of rate cut on gov't saving schemes will help pull investor back to equities.
- Foreign funds outflows may continue for a while. However, fresh foreign flows are expected to eventually flock back to the emerging Asia Pac region given better fiscal, external and growth profiles of the region, where Pak equities may also receive a chunk given its much cheaper valuations than peers'.
- Expected Privatization process and M&As in banking sector (for MCR) will definitely attract investor interest to equities in CY12.





Risk Premiums to account for in 2012

Investment Risks 2012

- Again, the drag on market volumes, and thus on overall equity returns, will continue should there be no required resolution of the CGT-related concerns of the investors and / or no margin relaxation on the available financing product (MTS) in 2012.

- Continuity of foreign outflows from Pakistan (due to on-going concerns) and regional markets (amid currency depreciation versus USD, may increase investor anxiety on local front while equity market will continue downward drift with larger falls.

- Increased distortion on country's political canvas may keep equities under stiff grip from going north. Thus, a political crisis could lead to faster-than-expected foreign pullout (foreigners hold ~USD2.2bn whereas high-weighted stocks representing over 71% of KSE100 contain USD1.30bn of foreign holdings).

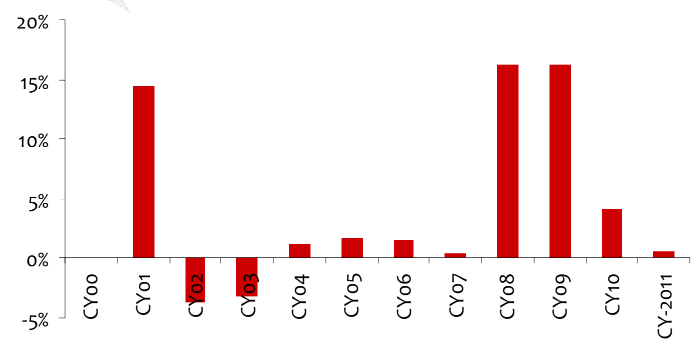
- Any immediate PKR depreciation against the greenback on account of country's higher debt servicing in FY12 and any downward shift in sovereign ratings as a result of economic deterioration, may put extra burden on equities' return in CY12.

- Last but not the least, no resolution on the notorious circular debt issue will affect companies' payout while upward reversal in interest rates (least expected) may drag equities lower.

FOREIGN INVESTORS HOLDINGS

Scrip	Market Weight			Est. Foreign Holding		
	CY11	CY10	Chg. YoY	CY11	CY10	Chg. YoY
OGDC	24%	25%	-0.4%	70%	75%	-4.7%
PPL	8%	9%	-0.4%	23%	38%	-14.8%
PTC	1%	3%	-1.4%	3%	28%	-24.7%
MCB	5%	6%	-1.3%	27%	66%	-39.4%
HUBC	2%	1%	0.2%	29%	22%	7.3%
UBL	3%	3%	0.1%	16%	55%	-39.2%
NBP	3%	3%	-0.4%	5%	18%	-12.8%
FFC	5%	3%	1.4%	3%	10%	-6.7%
ENGRO	2%	2%	-0.4%	8%	10%	-1.7%
PSO	2%	2%	-0.2%	2%	8%	-5.6%
HBL	5%	4%	0.5%	2%	4%	-2.2%
ABL	2%	2%	0.0%	0%	0%	0.3%
NESTLE	4%	4%	0.3%	9%	26%	-17.4%
POL	3%	2%	0.8%	2%	2%	-0.1%
ULEVER	3%	2%	0.7%	4%	21%	-17.5%
Total	69%	70%	-0.5%	-	-	-

PKR/USD PARITY TREND



Sector Strategies

Exploration & Production

The heavyweights shape up

Exploration & Production

Positive

- Favorable oil price movements and expected rise in production has been keeping the E&P sector in the limelight. So far during FY12, oil prices have remained higher (37% YoY and 1% HoH during 1HFY12). Meanwhile, ongoing shortage of gas with a flat production growth (2%YoY during 1HFY12) has been creating a bundle of problems for Pakistan's energy and manufacturing sectors that in turn has been hampering growth.

- Drilling activity failed to pick up during 1HFY12, as only 20% of the total targeted wells were drilled compared to last year's progress of 25% completion. Meanwhile, a discovery is yet to be struck at any exploratory fields whereas two discoveries (including Makori East) were struck in the same period last year, and focus continues to remain tilted towards developmental wells.

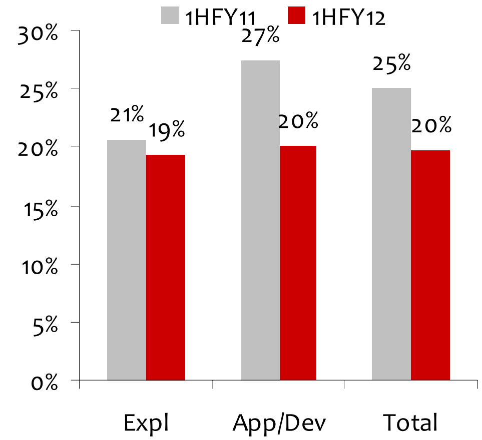
- Existing wells have remained in the limelight with incremental production coming from Nashpa and Tal blocks while further flows are expected from the respective blocks as additional development wells are still under progress.

- Introduction of new petroleum policies are directed to cater to the rising demand-supply gap under natural gas. The policies not only aim to offer higher gas prices, but also provide impetus for exploration of low BTU and Tight gas.

Outlook

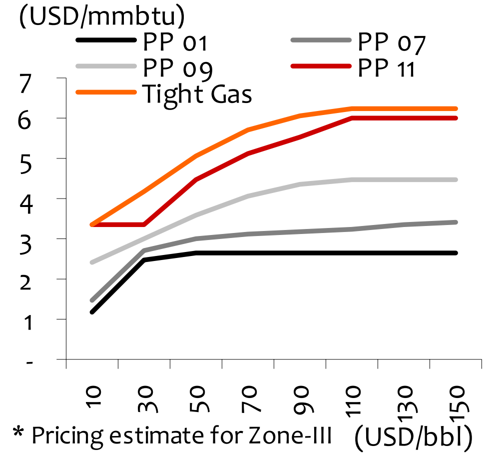
- The sector is going to benefit from higher oil prices expected to be realized during FY12, as well as production enhancements coming from various fields. Existing fields under development would continue to remain in the limelight, which is foreseen to primarily scale up the profitability of the E&P companies.

Drilling Activity*



*Wells drilled % of target

Gas pricing comparisons*



* Pricing estimate for Zone-III

Oil & Gas Development Company (OGDC)

Bloomberg Code	OGDC PK	Shr. 52W High, Low	Rs181 Rs120
Reuters Code	OGDC KA	Last Closing	Rs151.62
No. of Shares	4300.93mn	Target Price	Rs174.00
Avg. Daily Vol. (1-Y)	0.71mn Sh.	Upside Potential	14.70%

Hold

Strengths

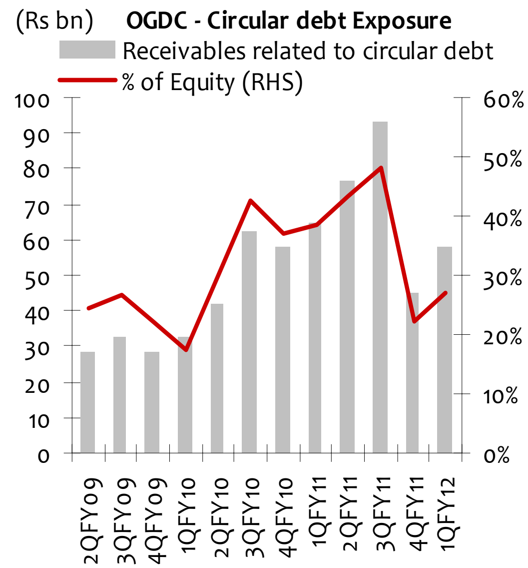
- OGDC remains the largest E&P company in the country, with balanced revenue mix coming from oil (49% in total) and gas (48% in total).
- After charging one-offs in FY11, earnings of the company are expected to see revival in FY12. Incremental production from developmental projects including KPD, Sinjhoro, Dakhni, Jhal Magsi and Qadirpur development, is expected to be materialized by end FY12. The projects are anticipated to enhance ~2300bpd of oil and ~240mmcfd of gas production.

Weaknesses

- Company remains exposed to the circular debt issue, with receivables from refineries reaching Rs57bn by Sep-11 end (massively up 28% QoQ).
- Timeline for completion of key development projects has often been pushed forward, adding uncertainty to timing of additional flows.

Potential Drivers

- With improved results materializing from the Nashpa field, additional wells in the block are expected to enhance production further.
- While Zin block might yield a discovery in the near term, the possible low BTU content of the field could delay its commerciality compared to an average gas discovery.



Company Financial Highlights

Rs mn	FY11A	FY12E	FY13F
Net Sales	155,631	197,176	228,662
Gross Profit	102,728	133,339	156,035
Other Income	3,304	6,148	6,233
Profit After Tax	63,527	86,780	99,557
EPS (Rs) @ 4,301 mn sh.	14.77	20.18	23.15
DPS (Rs) @ 4,301 mn sh	5.50	6.50	7.00
P/E	10.37	7.59	6.62
P/BV	3.34	2.57	2.02
Dividend Yield	3.6%	4.2%	4.6%
Return on Equity	32.2%	33.9%	30.6%
Return on Assets	24.7%	26.7%	24.4%

InvestCap.

Pakistan Petroleum Limited (PPL)

Bloomberg Code	PPL PK	Shr. 52W High, Low	Rs228 Rs168
Reuters Code	PPL KA	Last Closing	Rs168.32
No. of Shares	1,314.48mn	Target Price	Rs262.48
Avg. Daily Vol. (1-Y)	0.75mn Sh.	Upside Potential	55.90%

Buy

Strengths

- The company has been showing very strong recovery in earnings compared to peers' owing to rising oil production.

- Rising contribution of oil to its revenue mix is anticipated to balance revenue mix of the company and reduce dependency on few gas fields. Meanwhile, the company also benefits from oil price rise owing to major gas fields being price-uncapped.

Weaknesses

- Dwindling reserves from the Sui field remains the biggest challenge for the company. At current levels, Sui field contributes ~53% to total gas production of the company while still contributing 35% to the overall revenue mix.

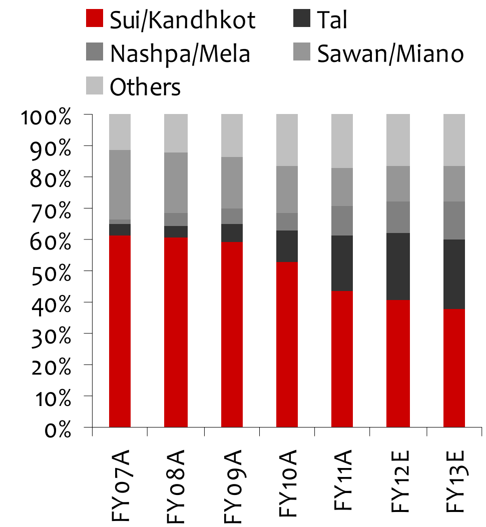
- Company's own exploratory program is still dormant in nature compared to peers'. The company has been overly dependent on flows from fields operated by joint venture partners (especially Tal and Nashpa blocks), thereby enhancing exposure to operating risks of the partners.

Potential Drivers

- The company would benefit from incremental flows from Nashpa in the near term, as it holds 26% stake in the block.

- Considering the diminishing production from own fields, PPL is focusing on revival of its exploration program. Meanwhile, Sui field has shown recovery in recent weeks, depicting additional production bonus for PPL.

Field wise contribution to revenues



Company Financial Highlights

Rs mn	FY11A	FY12E	FY13F
Net Sales	78,252	108,875	115,173
Gross Profit	52,187	71,193	74,389
Other Income	4,451	4,101	4,392
Profit After Tax	31,446	41,425	45,761
EPS (Rs) @ 1,314 mn sh.	23.92	31.51	34.81
DPS (Rs) @ 1,314 mn sh	10.91	15.00	15.00
P/E	7.04	5.34	4.84
P/BV	2.34	1.77	1.51
Dividend Yield	6.5%	8.9%	8.9%
Return on Equity	33.3%	33.1%	31.1%
Return on Assets	25.3%	25.0%	24.2%

Pakistan Oilfields Limited (POL)

Bloomberg Code	POL PK	Shr. 52W High, Low	Rs390 Rs282
Reuters Code	POL KA	Last Closing	Rs346.45
No. of Shares	236.55mn	Target Price	Rs486.00
Avg. Daily Vol. (1-Y)	1.341mn Sh.	Upside Potential	32.20%

Buy

Strengths

- Owing to low production base of the company, a massive jump in production of both oil and gas is visible in company portfolio, which expected to be enhanced as further development takes place.
- The company has relatively lower exposure to the circular debt owing to its association with Attock Group and excess to the entire oil supply chain via the Group companies.
- Apart from production enhancement from the joint-venture fields from Tal block, the company-operated Domial field also showed encouraging results, reducing its exposure to partner's operational risks.

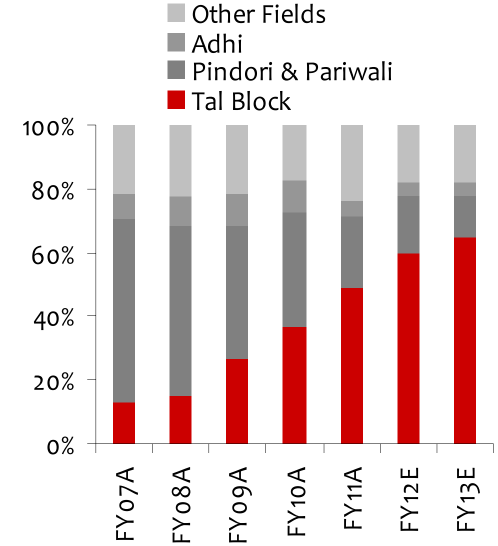
Weaknesses

- Company's revenue mix is still largely skewed towards oil production, thereby making it most sensitive to oil price movements and adding volatility to the revenue stream.

Potential Drivers

- The company remains the biggest beneficiary of incremental production from the Tal block among the listed sector companies. The prospects of the block remain promising with development underway on the mega oil-producing fields.
- Domial-2 has reached targeted depth and well's testing is expected to commence soon.

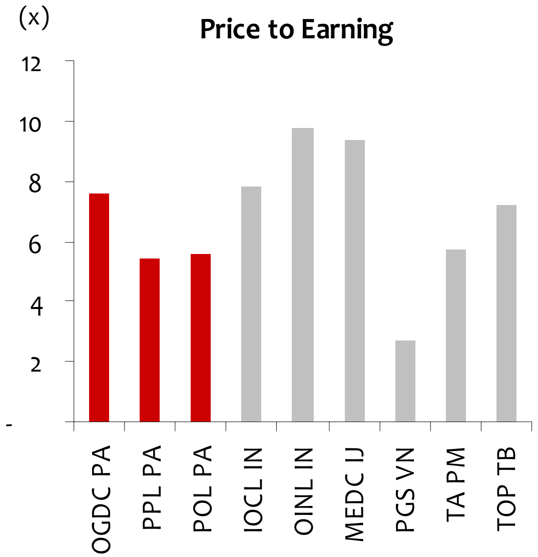
Field wise contribution to revenues

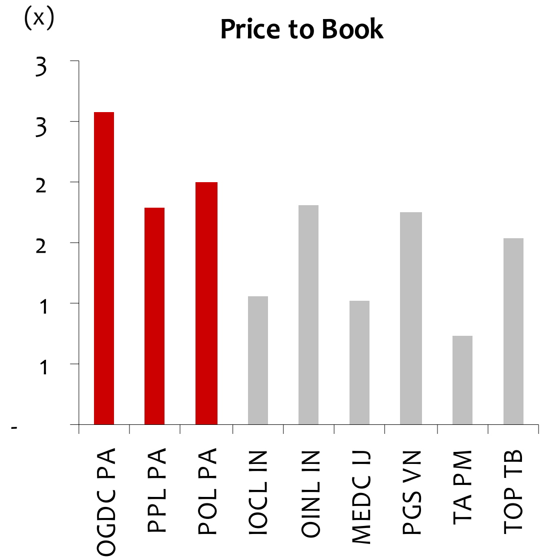


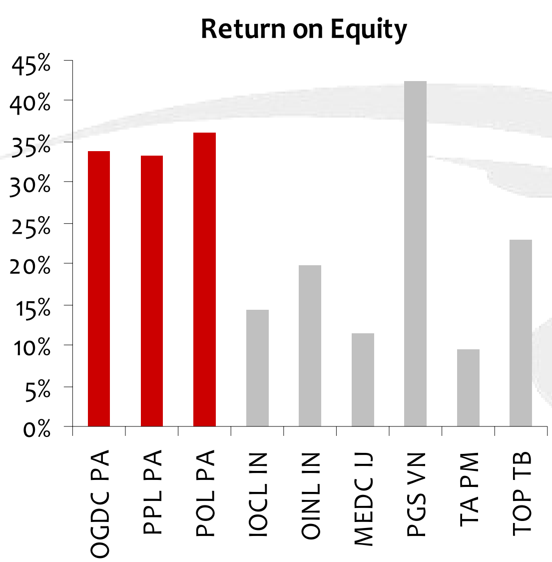
Company Financial Highlights

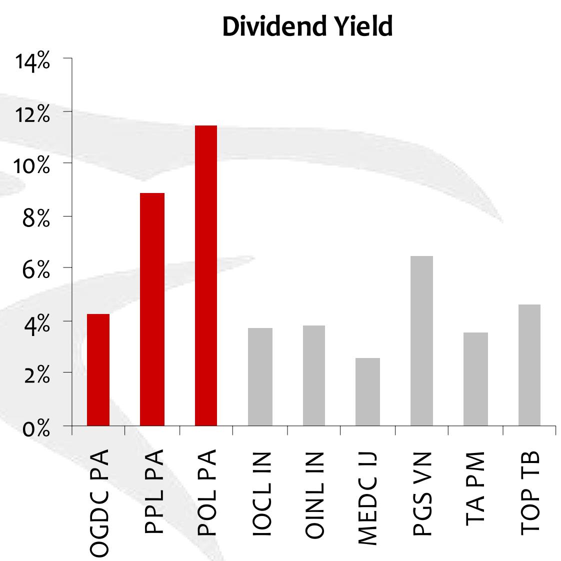
Rs mn	FY11A	FY12E	FY13F
Net Sales	24,951	32,529	35,455
Gross Profit	15,628	22,124	23,206
Other Income	1,809	1,653	2,029
Profit After Tax	10,815	14,823	15,667
EPS (Rs) @ 237 mn sh.	45.72	62.67	66.23
DPS (Rs) @ 237 mn sh.	35.00	40.00	40.00
P/E	7.58	5.53	5.23
P/BV	2.45	1.99	1.71
Dividend Yield	10.1%	11.5%	11.5%
Return on Equity	32.4%	36.0%	32.6%
Return on Assets	23.0%	27.0%	25.4%

Regional Attractiveness









Refineries

All about proportions

Refineries

Neutral

- Circular debt has gripped Refinery sector sales as well, where ongoing power crisis, higher oil prices, reduced hydal dependency and increasing power demand have all resulted in widening of the gap.

- Refinery profitability is amongst the most volatile in our sample universe, as factors including international gross refinery spreads, domestic product mix and inventory gains and losses contribute to this volatility. Although GRMs jumped further by 29% YoY during 1HFY12, the issue of inventory pileup owing to circular debt and low throughput by certain refineries has affected earnings negatively.

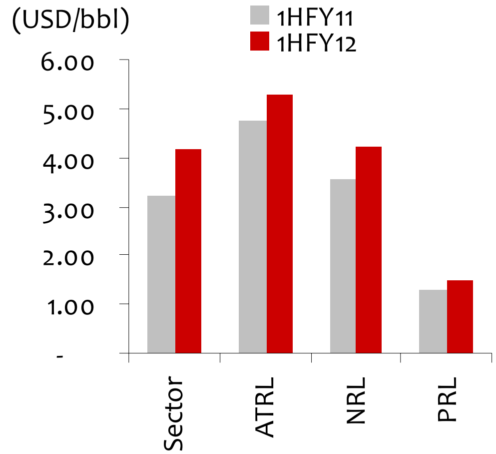
- Refinery sector principally agreed to expand and upgrade capacities to meet Euro standards. In this manner, a plan was submitted aiming to enhance capacity to 19.34mn tons with a huge investment of USD9.9bn.

- Although refinery prices were partly deregulated more recently, the element of Deemed Duty and incidentals remain part of the refinery pricing formula. While incidentals play a limited role, Deemed Duty on HSD is still a critical factor in determining refinery sector profitability. The risk of sequential removal or reduction still remains at large, though with refineries laying out their plans to invest in order to meet domestic demand as well as international standards, the Deemed Duty issue could stay muted till such investments are materialized.

Outlook

- Numerous factors affecting refinery sector performance are expected to continue to impact future profitability of the sector. While projects targeting to reduce sulphur content may not yield additional financial returns, we deem refineries targeting to install isomerization units will be key beneficiaries of improved product yields in the future. Nearly all the local refineries are targeting to enhance Mogas yield through such projects.

Gross Refinery Margins



Investment Outlook (USD mn)	
Short term	**1,590**
BOPL	660
ATRL	250
BPPL	90
PRL	250
NRL	305
PARCO	35
Medium/Long term	**8,310**
BOPL - Chemical	275
BOPL - DBN	135
Trans-Asia	600
Khalifa	5,000
ATRL-II	2,000
MMTJPP	300
Total	**9,900**

Attock Refinery Limited (ATRL)

Bloomberg Code	ATRL PK	Shr. 52W High, Low	R146 Rs99
Reuters Code	ATRL KA	Last Closing	Rs107.65
No. of Shares	85.29mn	Target Price	Rs150.00
Avg. Daily Vol. (1-Y)	1.26mn Sh.	Upside Potential	39.00%

Buy

Strengths

- Having better yields of high-margin products, such as Mogas and HSD, the refinery is a key beneficiary of favorable movements in the GRMs.
- Relatively less exposed to the circular debt crisis, owing to dedicated supplies to the Group's downstream company.
- Group synergies further play a vital role owing to dividend income from associates (including NRL and APL) increasingly contributing towards ATRL's bottomline.

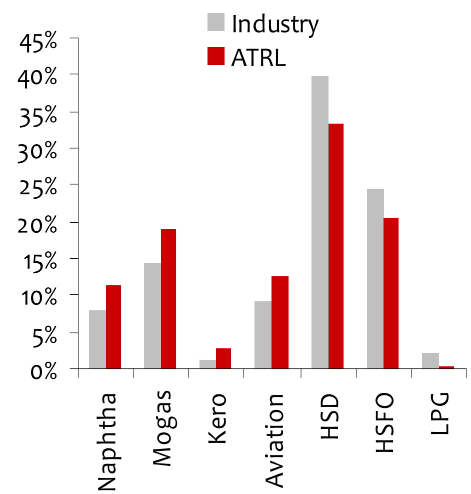
Weaknesses

- Being in the business of oil refining, the company is still prone to unfavorable movements in the refinery spreads and inventory losses. The company's earnings have also historically remained most volatile in our sample universe owing to this inherent risk.

Potential Drivers

- The refinery remains dedicated to enhance productivity and improve standards through near-term projects worth USD250mn, including installation of a isomerization complex and Diesel Hydro Desulphurization (DHDS) plant. Long term plans include expansion of 2.3mn tons worth USD2.0bn.
- Holding the highest white oil yield amongst the listed peers, ATRL would remain the prime beneficiary of better refinery spreads.

Refinery Yields



Company Financial Highlights

Rs mn	FY11A	FY12E	FY13F
Net Sales	116,397	123,757	122,470
Gross Profit	1,558	1,773	1,437
Other Income	1,566	463	1,097
Profit After Tax	2,186	2,178	2,434
EPS (Rs) @ 85 mn sh.	25.62	25.54	28.54
DPS (Rs) @ 85 mn sh.	2.00	2.00	2.00
P/E	4.20	4.22	3.77
P/BV	0.43	0.40	0.36
Dividend Yield	1.9%	1.9%	1.9%
Return on Equity	10.3%	9.4%	9.6%
Return on Assets	3.4%	2.5%	2.7%

National Refinery Limited (NRL)

Bloomberg Code	NRL PK	Shr. 52W High, Low	R383 Rs231
Reuters Code	NRL KA	Last Closing	Rs242.69
No. of Shares	79.97mn	Target Price	Rs323.00
Avg. Daily Vol. (1-Y)	0.25mn Sh.	Upside Potential	33.00%

Buy

Strengths

- The only Lube-based refinery in the country where Lube business continues to remain a prominent contributor to company's bottomline. Earnings remain relatively less volatile historically owing to this diversity that the company holds.

- NRL's refinery yields are relatively balanced compared to other high FO-yielding refineries in the country. This enables the company to reap benefit of rising refinery spreads.

Weaknesses

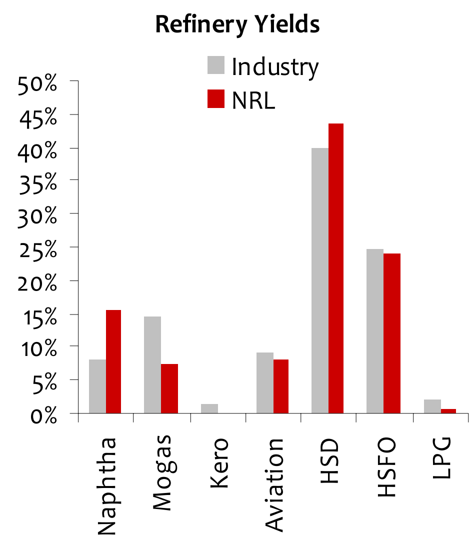
- Circular debt issue has recently caused furnace oil inventory pileup pushing refinery business into losses.

- Weakness in Lube industry dynamics could turn unfavorable for the company owing to high dependency on the business segment.

Potential Drivers

- Better diversity offered by the company operations makes it relatively a safer bet in the refinery sector.

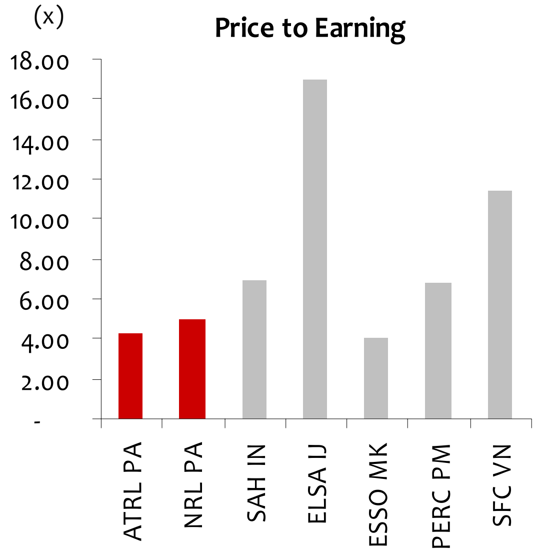
- Like peers, NRL also plans to install isomerization and DHDS complex worth USD305mn, which would partially improve Mogas yields.

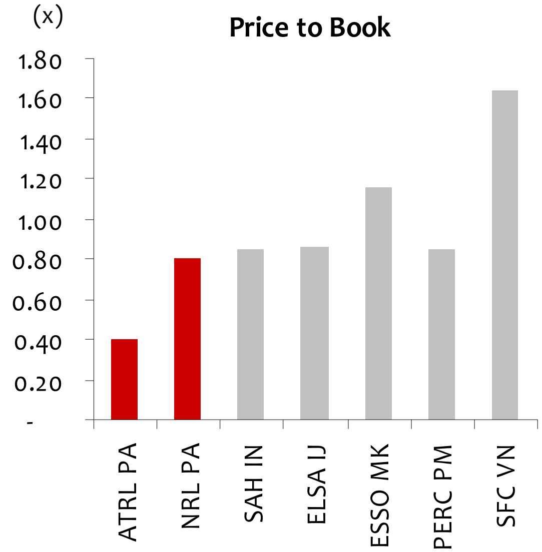


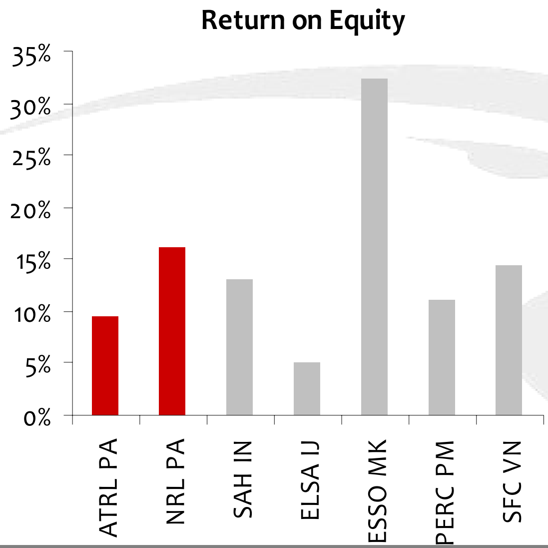
Company Financial Highlights

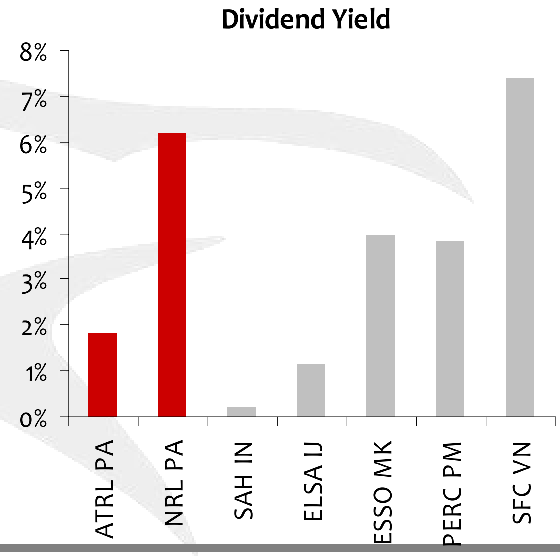
Rs mn	FY11A	FY12E	FY13F
Net Sales	148,558	166,566	177,864
Gross Profit	10,007	4,593	7,831
Other Income	2,498	2,602	2,792
Profit After Tax	6,569	3,938	5,646
EPS (Rs) @ 80 mn sh.	82.14	49.24	70.60
DPS (Rs) @ 80 mn sh.	25.00	15.00	20.00
P/E	2.95	4.93	3.44
P/BV	0.90	0.80	0.69
Dividend Yield	10.3%	6.2%	8.2%
Return on Equity	30.5%	16.2%	19.9%
Return on Assets	11.1%	5.9%	7.5%

Regional Attractiveness









Oil Marketing Companies

Queues at pump keep getting longer

Oil Marketing Companies

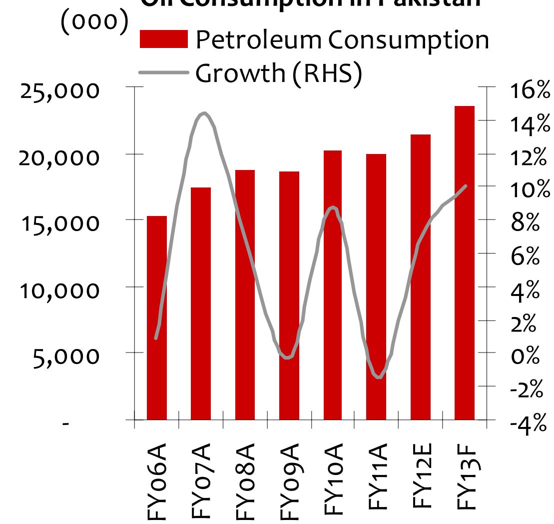
Neutral

- Oil consumption in Pakistan has been growing at a CAGR of 5.5% (FY06-FY11). After a temporary slowdown observed during FY11 due to series of floods faced by the country, growth has resumed from Jul-11 onwards (9.0% next 3 years).
- Acute electricity (5,000-7,000MW, with an 8-10% annual demand growth) as well as gas shortages in the country coupled with few energy sources (low hydel and gas availability with tiny reliance on coal) will increase oil consumption (primarily furnace oil) while erratic supply of CNG will improve Petrol consumption ahead.
- The upcoming lot of the power plants (both IPPs and few RPPs) is mainly thermal-based (FO based), thus, we expect furnace oil 3-year volume CAGR at 7%.
- OGRA has allowed gradual increase in OMC margins for MS, HSD and LDO in PKR terms with 27% jump from last figures. This increase is expected to have positive impact on OMCs in 2HFY12 onwards (provided oil prices stay at current levels) as the cumulative contribution of these products ranges between 37% (PSO 37%) and 46% (SHEL 46%, APL 38%) along with rising FO margins (unregulated).
- Besides core earnings growth, we believe, the inventory gains/losses are expected to stay in the limelight given rising oil prices (WTI already up 4.4% YoY) due to colder Winter, however, declining PKR/USD parity may offset these gains.
- Major risk mounting is the circular debt across energy chain. It is expected to take time to resolve as slow-thinning of subsidies on electricity and gas this year (last year of the gov't term), may continue to impact liquidity, earnings and payouts.

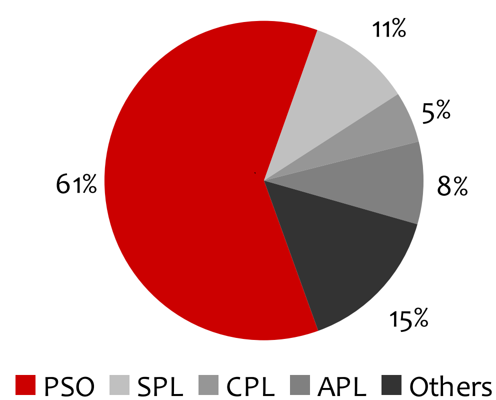
Outlook

- OMC sector will benefit from higher oil consumption and prices expected to be realized in FY12 while the only drag on earnings and payouts will be circular debt.

Oil Consumption in Pakistan



OMCs Market Share 5MFY12



Pakistan State Oil (PSO)

Bloomberg Code	PSO PK	Shr. 52W High, Low	Rs314 Rs206
Reuters Code	PSO KA	Last Closing	Rs227.21
No. of Shares	171.52mn	Target Price	Rs277
Avg. Daily Vol. (1-Y)	0.53mn Sh.	Upside Potential	22.00%

Buy

Strengths

- Market leader in almost all the POL products (~61% market share in 5MFY12), PSO maintains largest network of over 3,800 (CNG integrated) outlets across the country.
- PSO is expected to benefit the most from FO (amid power and gas crises) and Petrol and Diesel (interrupted supplies of CNG) sales growth.
- PSO derives most of its recurring profits from high-volume deregulated petroleum products (FO and HSD). The company was also the first to introduce Ethanol-mixed fuel in Pakistan.

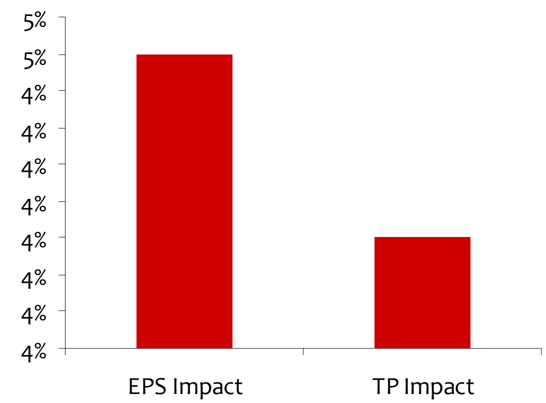
Weaknesses

- PSO's bottomline is most vulnerable to int'l oil price changes in terms of inventory gains/losses as it has largest petroleum storage capacity (~1mn tons).
- PSO stands as the central victim of the circular debt crisis in the country with ~Rs180bn of receivables resulting in towering financial charges and frequent liquidity issues.

Potential Drivers

- PSO is expected to benefit from rising oil prices in terms of inventory gains.
- Any resolution on the circular debt front would amply unlock cash flows and payouts. New RPPs and IPPs contracts would also escalate FO demand ahead and boost company's FO volumes and therefore strengthening PSO's earnings

USD10/bbl Change Impact on PSO



Company Financial Highlights

Rs mn	FY11A	FY12E	FY13F
Net Sales	148,558	166,566	177,864
Gross Profit	10,007	4,593	7,831
Other Income	2,498	2,602	2,792
Profit After Tax	6,569	3,938	5,646
EPS (Rs) @ 80 mn sh.	82.14	49.24	70.60
DPS (Rs) @ 80 mn sh.	25.00	15.00	20.00
P/E	2.95	4.92	3.43
P/BV	0.90	0.80	0.68
Dividend Yield	10.3%	6.2%	8.3%
Return on Equity	30.5%	16.2%	19.9%
Return on Assets	11.1%	5.9%	7.5%

Attock Petroleum Limited (APL)

Bloomberg Code	APL PK	Shr. 52W High, Low	Rs434 Rs321
Reuters Code	APL KA	Last Closing	Rs412.50
No. of Shares	69.12mn	Target Price	Rs484.00
Avg. Daily Vol. (1-Y)	0.14mn Sh.	Upside Potential	17.00%

Buy

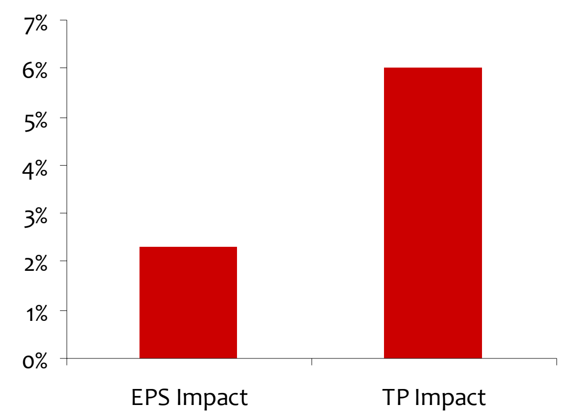
Strengths

- Market leader in non-regulated POL products (100% market share in Asphalt, Naphtha exports etc). Meanwhile, APL is the second largest FO distributor after PSO with over 4% market share, with total market share of the company (~7%) being consistently on the rise.

- APL derives most of its recurring profits from deregulated petroleum products (HSD, Asphalt, and FO). The company is also penetrating into Central Asian economies by exporting its products through its own distribution network in Afghanistan.

- Lower capacity (~3-4 days inventory) leads to smaller inventory gains/losses. APL does not import any of POL products, which saves potential FX losses. APL is also least affected by the circular debt and thus has no exposure to debt.

USD10/bbl Change Impact on APL



Weaknesses

- Small sized capacity with limited penetration in major cities of the country.

- Limited exposure in high-margin non-regulated products, such as Lubes, with no alternate fuel in the product-mix i.e. CNG, LPG.

Potential Drivers

- Consistent core margins with earnings growth, insignificant financial cost and better cash flows will lead to improved cash payouts. New IPP contracts with number of thermal power plants coming online in FY12, will help improve FO offtake and thus company earnings.

Company Financial Highlights

Rs mn	FY11A	FY12E	FY13F
Net Sales	148,558	166,566	177,864
Gross Profit	10,007	4,593	7,831
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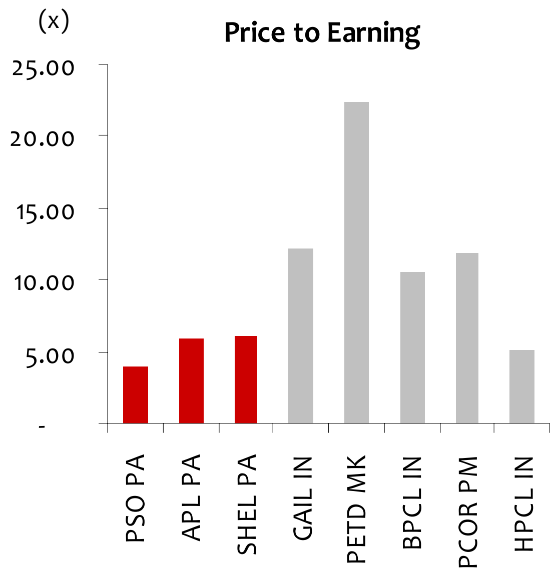
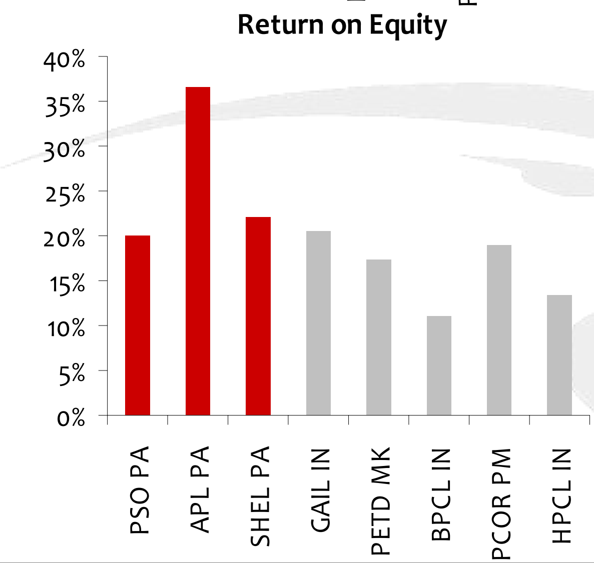
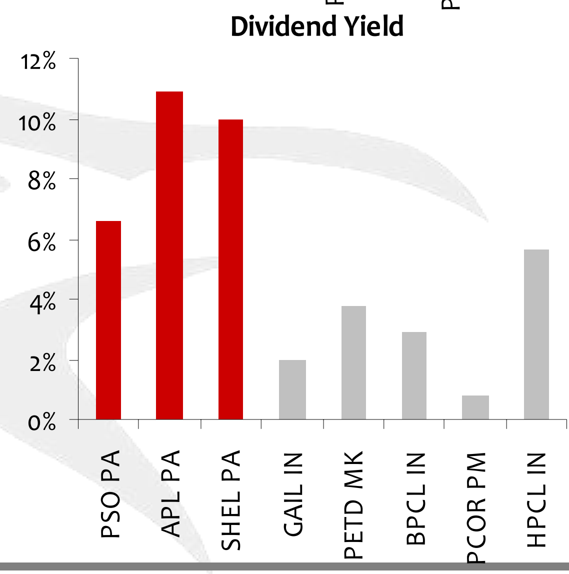
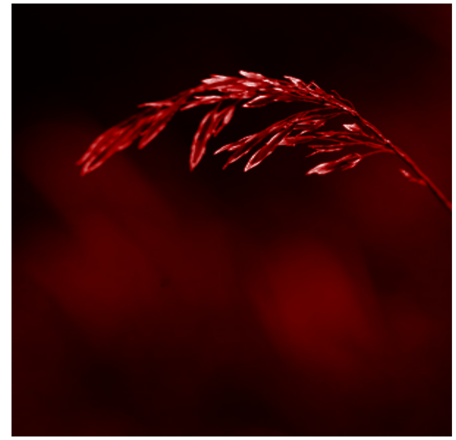
Regional Attractiveness









Fertilizer

Yield is the name of the game

InvestCap.

Fertilizer

Positive

- Production of Urea during 11MCY11 has been recorded at 4.5mn tons down 4% YoY. Despite capacity enhancement of 1.15mn tons (EnVen and Fatima plants) acute shortage of gas to the fertilizer sector has brought down operating capacity utilization to 82%, down 15pps. Offtake of the sector has remained passive during 11MCY11 as well and was recorded at 5.2mn tons (down 5% YoY).

- There has been unprecedented increase in the price of Urea throughout the year 2011, owing to the above mentioned gas curtailment especially to EnVen. The main reason behind price increase of Urea on such a massive scale, has been failure of SNGP network to supply uninterrupted gas to ENGRO's USD1.1bn plant.

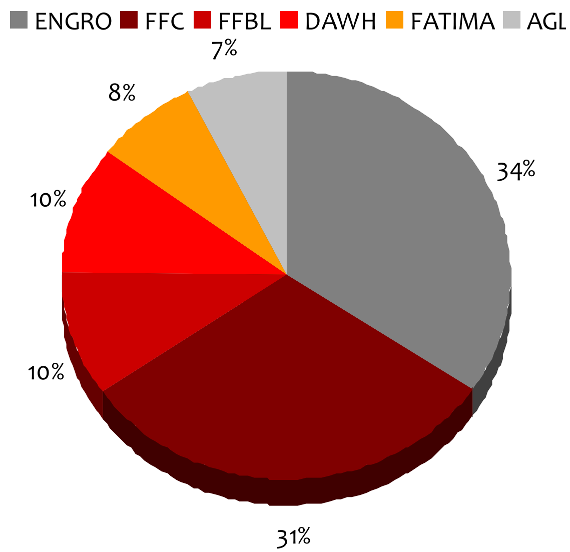
- Lack of production has forced the gov't to import Urea in extensive quantities, and then to subsidize them so that the price of imported Urea could be brought down to the level of prevailing local prices. In 11MCY11, the gov't imported 715k tons of Urea, and paid Rs15.4bn on them in the form on subsidy, against the budgeted amount of Rs14bn for this year.

- Gas development surcharge is to be imposed on feed gas for the fertilizer sector. Post implementation of the said surcharge, feed price is expected to be around USD3.3 per mmbtu (closer to price of feed gas in the international market). However, the said surcharge is expected to be passed on to end consumers.

Outlook

- Pakistan being an agrarian economy always enjoys extensive demand of fertilizers, with local manufacturers equipped with stern pricing power. Stupendous level of profitability of the fertilizer sector is expected to remain intact with expectation of minor revisions going forward.

Industry Capacity Share



Impact of GDS and price increase

	Engro	FFC	FFBL
	Price increase/bag	EPS impact	EPS impact
EnVen Prod	GDS on both plants		
450k tons	288	3.40	(0.17)
600k tons	283	3.11	(0.22)
900k tons	276	2.69	(0.30)
	GDS on old plant		
450k tons	213	(0.85)	(0.97)
600k tons	194	(1.96)	(1.18)
900k tons	164	(3.62)	(1.50)

Fauji Fertilizer Company Limited (FFC)

Bloomberg Code	FFC PK	Shr. 52W High, Low	Rs198 Rs110
Reuters Code	FFC KA	Last Closing	Rs149.54
No. of Shares	848.16mn	Target Price	Rs251
Avg. Daily Vol. (1-Y)	2.23mn Sh.	Upside Potential	68.00%

Buy

Strengths

- Being on Mari network, the company faces mere 12% gas curtailment as compared to its peers on the Sui network.
- FFC enjoys massive price expansion brought in by Engro as the latter fights the menace of gas curtailment on much extensive scale as compared to the former.
- The company has recently ventured into Wind Power business, diversifying FFC's focus from Urea manufacturing to power generation.

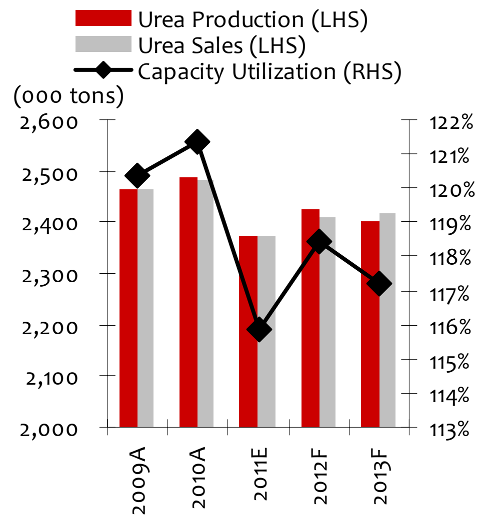
Weaknesses

- Earnings retention rate might be higher going forward, as the company aims to make its mark on the Wind power generation business, which is expected to turn its exuberant cash payout policy in to a relatively normal one.
- Profitability is expected to be truncated if GDS is not imposed on new plants (EnVen and Fatima) as indicated by the government approvals.

Potential Drivers

- Any rise in the price of Urea amid additional gas curtailment on SNGP network would further strengthen the profitability of the company.
- Company's venturing into Wind power business (where attractive returns are being offered by the gov't) would yield additional returns and enhanced cash payouts in future.

FFC production and sales snapshot



Company Financial Highlights

Rs mn	CY10A	CY11E	CY12F
Net Sales	44,874	54,528	65,320
Gross Profit	19,564	32,453	41,403
Other Income	3,153	6,251	4,477
Profit After Tax	11,029	20,454	24,207
EPS (Rs) @ 848 mn sh.	13.00	24.12	28.54
DPS (Rs) @ 848 mn sh.	16.00	22.25	26.50
P/E	11.50	6.23	5.24
P/BV	8.21	5.42	5.05
Dividend Yield	14.9%	17.7%	17.7%
Return on Equity	71.4%	109.2%	118.3%
Return on Assets	25.6%	40.9%	45.3%

Fauji Fertilizer Bin Qasim Limited (FFBL)

Bloomberg Code	FFBL PK	Shr. 52W High, Low	Rs64 Rs35
Reuters Code	FFBL KA	Last Closing	Rs42.43
No. of Shares	934.11mn	Target Price	Rs76.00
Avg. Daily Vol. (1-Y)	4.44mn Sh.	Upside Potential	79.00%

Buy

Strengths

- FFBL enjoys competitive advantage against all its peers for being the sole manufacturer of DAP and granular Urea in the country.
- The company enjoys committed supply of Phos-acid (raw material) due to its effective backward integration with Pak-Morocco Phosphate.
- FFBL has a well-balanced fertilizer business, where any impact of DAP volatility is minimized by the Urea business.
- Like FFC, FFBL is also venturing into the Wind power generation business.

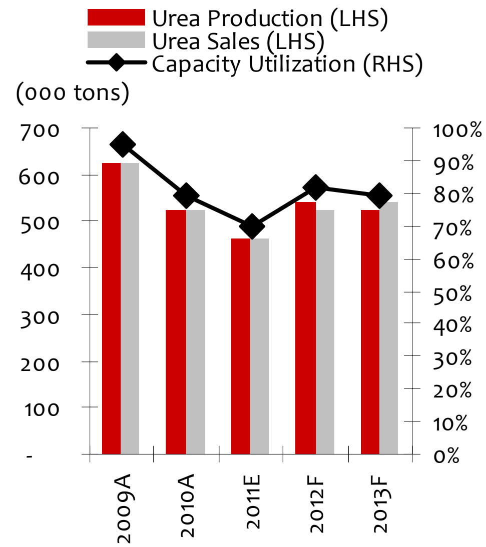
Weaknesses

- DAP prices are determined through imported supplies where the company is a price-taker. Thus, FFBL is more prone to follow the prices that prevail in the international market.
- Rupee depreciation impacts FFBL negatively as the company's raw material purchase is primarily denominated in the USD.

Potential Drivers

- Decline in the prices of Phos-acid is expected to enable the company to maintain its primary margins at current levels going forward.

FFBL urea production and sales snapshot



Company Financial Highlights

Rs mn	CY10A	CY11E	CY12F
Net Sales	43,257	56,170	59,130
Gross Profit	13,463	20,012	16,860
Other Income	1,033	1,323	887
Profit After Tax	6,514	10,159	7,755
EPS (Rs) @ 934 mn sh.	6.97	10.88	8.30
DPS (Rs) @ 934 mn sh.	6.55	9.75	7.25
P/E	6.08	3.90	5.11
P/BV	3.25	2.29	2.68
Dividend Yield	23.0%	17.1%	17.1%
Return on Equity	53.4%	63.9%	43.4%
Return on Assets	18.4%	28.7%	21.4%

Engro Corporation Limited (ENGRO)

Bloomberg Code	ENGRO PK	Shr. 52W High, Low	Rs237 Rs92
Reuters Code	ENGRO KA	Last Closing	Rs92.70
No. of Shares	393.28mn	Target Price	Rs210.00
Avg. Daily Vol. (1-Y)	2.40mn Sh.	Upside Potential	127.00%

Buy

Strengths

- Participation in different businesses makes Engro Corp. the most diverse group.
- The company enjoys the status of price-maker in the Urea industry.
- Food business has come into its own with further growth prospects in the pipeline. The subsidiary successfully acquired Al Safa Halal Foods, setting its footing in the North American halal foods market.
- Decline in interest rates is also proving to be most favorable for ENGRO as it reduces the company's financial cost.

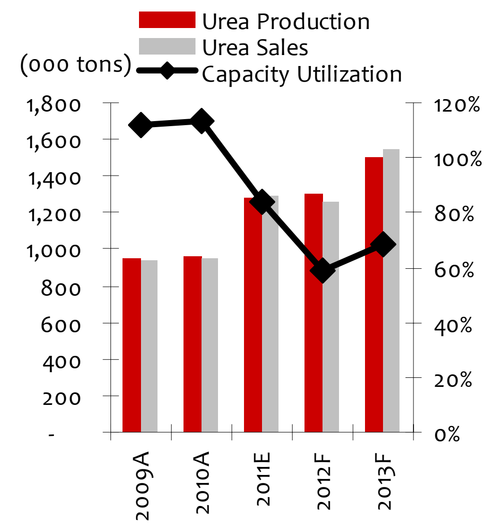
Weaknesses

- Unannounced gas outages have plagued the company's 1.3mn tons Urea production capability.
- Numerous startups of EnVen are expected to have its toll on the life of the plant in the long run and would significantly increase the maintenance cost for the company, going forward.

Potential Drivers

- As per our understanding GDS would not be applied on new plants, suggesting that cumulatively, ENGRO is expected to face lower fixed cost as compared to its peers'. Thus, it would be relatively easier for ENGRO to pass that increased fixed cost on to the end consumer.

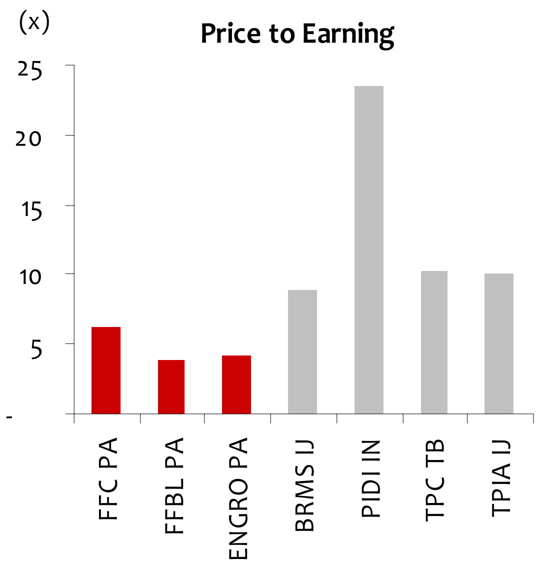
Engro production and sales snapshot

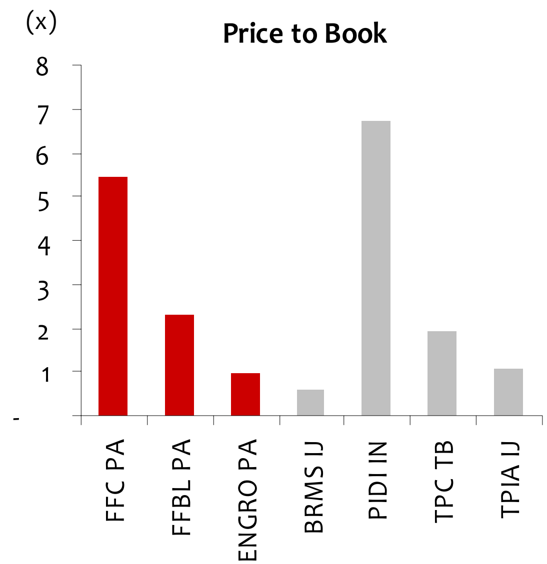


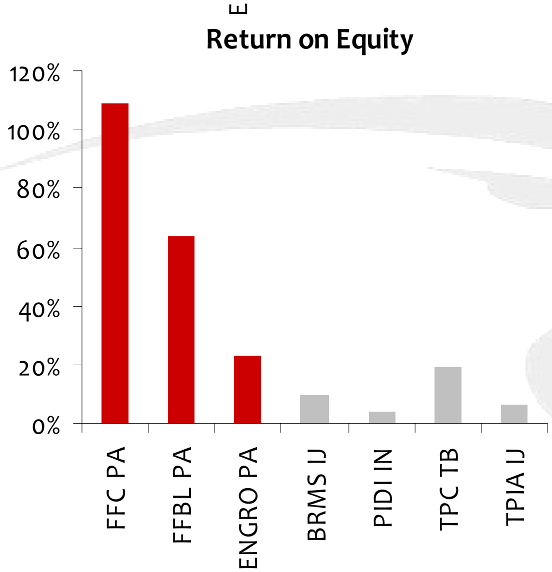
Company Financial Highlights

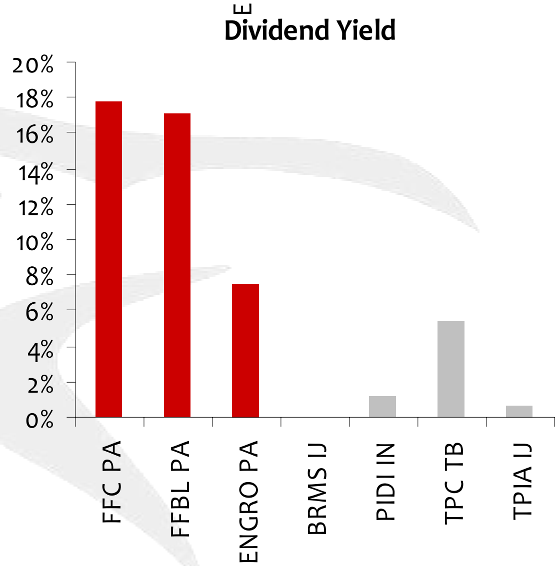
Rs mn	CY10A	CY11E	CY12F
Net Sales	79,976	95,631	108,651
Gross Profit	20,274	30,520	34,067
Finance Cost	4,201	10,011	9,298
Profit After Tax	6,441	8,716	12,352
EPS (Rs) @ 393 mn sh.	17.26	22.21	31.52
DPS (Rs) @ 393 mn sh.	6.00	6.00	7.00
P/E	5.66	4.18	2.95
P/BV	1.07	0.97	0.77
Dividend Yield	6.5%	7.6%	7.6%
Return on Equity	18.9%	23.2%	26.2%
Return on Assets	3.9%	5.0%	6.5%

Regional Attractiveness









Power (IPPs)

Much hype, less availability

Power (IPPs)

Neutral

- The circular debt crisis remains a major issue in the energy sector. The government attempted to reduce it through borrowing from banks in the shape of swap with gov't securities. However, circular debt has started swelling again owing to restricted progress towards a long term solution. The increase in circular debt is causing the expansion of receivables in the sector, hurting generation on the back of dried liquidity of the power companies.

- The recent increase in furnace oil prices coupled with gas load-shedding in the power sector is causing the increase in cost of power generation. Although the cost increase is partially passed on to the consumer on account of fuel adjustment, it is still creating hurdles for power generation in the country.

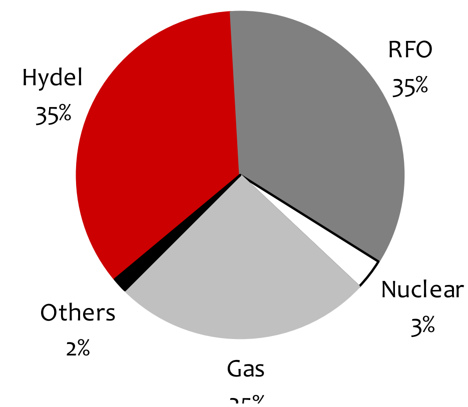
- As far as profitability is concerned, the InvestCap power sector universe companies remained safe from the circular debt and increase in furnace oil prices as the sector enjoys liberty under the Power Policy 1994 to pass on such costs.

- Currently, the country is facing short fall in the electricity as the sector is unable to provide sufficient level of electricity to the consumers. Going forward, we anticipate continued short fall in generation during 2012, as only 1,023MW capacity was added to the total capacity so far.

Outlook

- With the increasing demand of electricity in the country power sector would remain in the lime light. However, increasing fuel prices coupled with shortage of gas in the country would continue to hurt the generation of the sector in the medium term.

Source Wise Generation



Projected Supply and Demand

(MW)	Generation	Demand	Gap
FY12	21,746	25,284	(3,538)
FY13	24,212	27,092	(2,880)
FY14	25,081	29,032	(3,951)
FY15	34,223	31,299	2,924

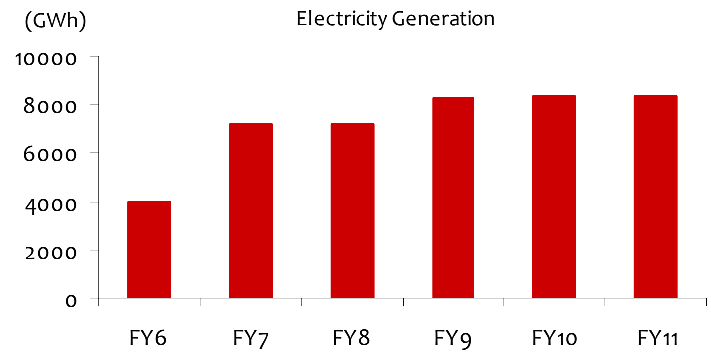
Hub Power Company Limited (HUBC)

Bloomberg Code	HUBC PK	Shr. 52W High, Low	Rs43 Rs34
Reuters Code	HUBC KA	Last Closing	Rs34.20
No. of Shares	1,157mn	Target Price	Rs52
Avg. Daily Vol. (1-Y)	1.4mn Sh.	Upside Potential	52.00%

Buy

Strengths

- Due to USD and US CPI-based tariff payments, the company's returns are hedged.
- Initiation (COD) of the much-awaited Narowal plant has finally taken place, which was one of the primary expansion projects of the company.
- The company provides dividend yield of 15.1% (assuming 100% payout), offering a premium of 240bps compared to current 10-year PIB yield.
- Amount payable to PSO stands at Rs82.6bn while receivables from WAPDA at Rs97.4bn till Sep-11. Higher receivables provide a spread to HUBC as the interest rate remains same on both receivables and payables. However, to fill the gap HUBC relies on the short-term borrowing for continuity of fuel supply.



Weaknesses

- The fuel supply agreement with Bakri Trading Company is a little concerning because, if HUBC is unable to pay the billed amount to the company with any delay, the supplier could refuse to supply FO to the Narowal Plant.
- Rising circular debt could escalate the liquidity problems for the company.
- Increase in the interest rates could further squeeze overall liquidity.

Potential Drivers

- Materialization of agreed tariff instead of reference tariff of the Narowal plant would add significant amount to the company's bottomline.

Company Financial Highlights

Rs mn	FY11A	FY12E	FY13F
Net Sales	123,310	165,024	166,788
Gross Profit	9,217	9,311	9,038
Other Income	27	66	76
Profit After Tax	5,425	6,063	6,044
EPS (Rs) @ 1157 mn sh.	4.69	5.24	5.22
DPS (Rs) @ 1157 mn sh.	5.50	5.24	5.22
P/E	7.30	6.53	6.55
P/BV	1.39	1.34	1.34
Dividend Yield	16.1%	15.3%	15.3%
Return on Equity	19.1%	20.5%	20.5%
Return on Assets	4.8%	4.9%	4.6%

InvestCap.

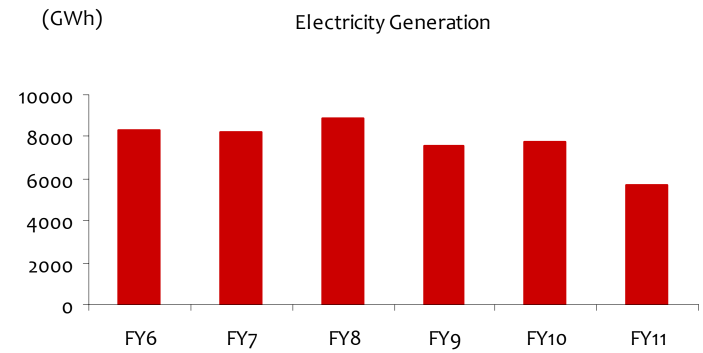
Kot Addu Power Company Limited (KAPCO)

Bloomberg Code	KAPCO PK	Shr. 52W High, Low	R47 Rs40
Reuters Code	KAPCO KA	Last Closing	Rs41.32
No. of Shares	880.25mn	Target Price	Rs60
Avg. Daily Vol. (1-Y)	0.36mn Sh.	Upside Potential	45.00%

Buy

Strengths

- Due the indexation of USD at Rs34/USD for the tariff the company takes benefit of any depreciation in the PKR against the USD.
- Consistent dividend payout policy keeps the company scrip at attractive levels.
- KAPCO is one of the largest power plants in the country with a total capacity of 1600MW.



Weaknesses

- Increase in the amount of payables to PSO compared to receivable amount from WAPDA could hurt the company's bottomline as the interest rate on payables is higher than that on company's receivables.
- Circular debt could create liquidity problems for the company as KAPCO's leverage position has increased up to considerable levels against its overall equity.

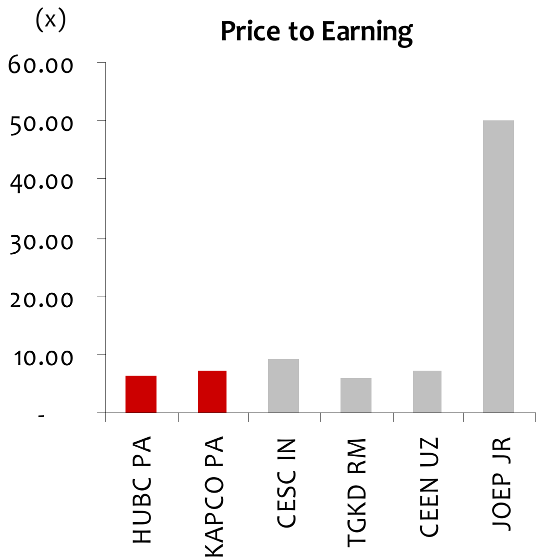
Potential Drivers

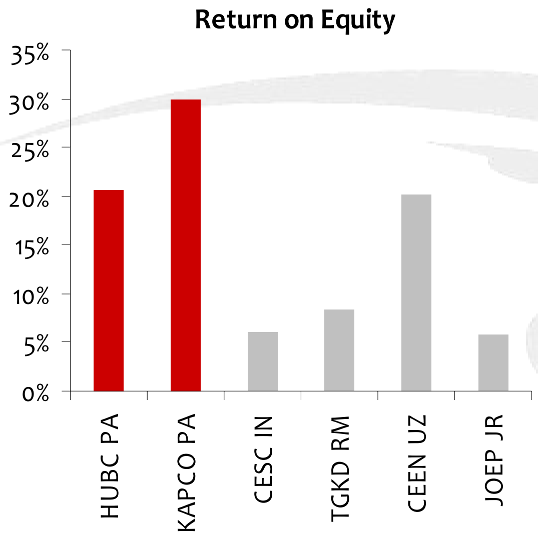
- Any potential resolution of the circular debt would unlock liquidity for the company that has been denting bottmline for quite some time. This would also enable the company to assume higher leverage given the level amount of equity on company's balance sheet..

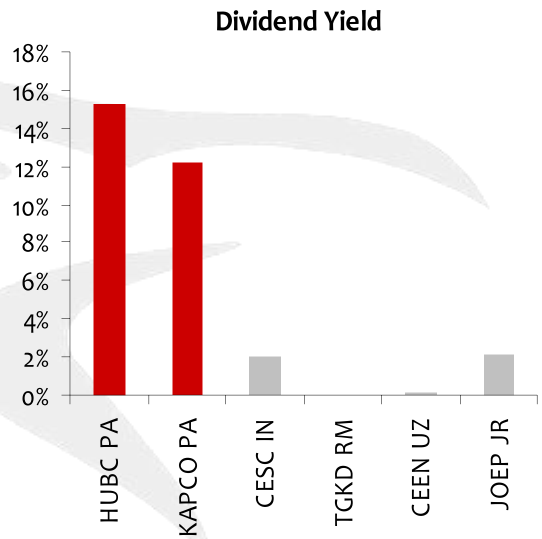
Company Financial Highlights

Rs mn	FY11A	FY12E	FY13F
Net Sales	74,351	109,889	112,574
Gross Profit	10,698	12,124	12,798
Other Income	8,381	8,140	8,373
Profit After Tax	6,527	5,200	4,643
EPS (Rs) @ 880 mn sh.	7.41	5.91	5.27
DPS (Rs) @ 880 mn sh.	6.50	5.02	4.48
P/E	5.57	6.99	7.83
P/BV	1.52	1.38	1.35
Dividend Yield	15.7%	12.2%	10.9%
Return on Equity	30.0%	30.0%	30.0%
Return on Assets	7.1%	4.5%	3.8%

Regional Attractiveness







Textiles

Hedge against currency

Textiles

Neutral

- With the depreciation in the PKR against the USD and Euro, the local Textiles sector is to benefit from exports of their products as the InvestCap universe textile companies export as much as ~75% of the products they manufacture.

- Decline in cotton prices provides cheap production cost therefore enabling the Textiles sector to compete with its regional competitors i.e. China, India and Bangladesh.

- Low interest rates scenario coupled with decline in cotton prices trims down the financial charges as the sector has to borrow funds for purchase of cotton.

- Currency pact between Japan and China is expected to appreciate the Chinese Yuan against USD, which would make the Pakistani Textiles more competitive.

- The sectors gross margins could get a hit owing to pass-on of the cost of cotton to the buyers with a time lag.

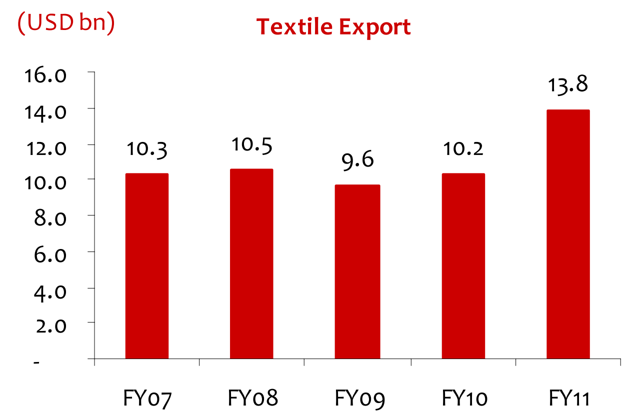
- Rise in interest rates could increase the financial charges of the sector as the sector is highly leveraged. Electricity and gas crisis in the country could further hurt productivity of the Textiles sector, going forward.

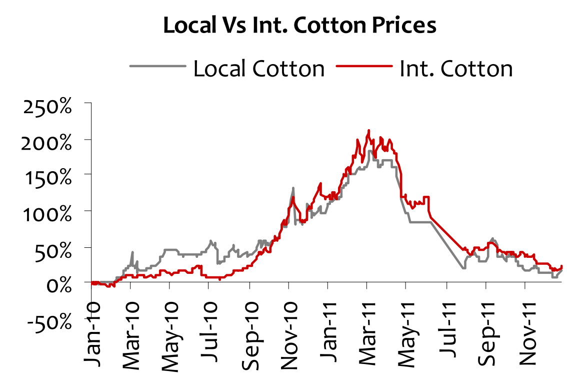
Outlook

- Low cotton prices and weak PKR against USD are in favor of Textiles. However, shortage of gas and electricity is the main hurdle for the sector, with limited improvement expected in supply of gas and electricity in the near term.

Contribution of Textile Sector in Pakistan's Economy

GDP	7.4%
LSM	32.6%
Employement	38.0%
Exports	55.6%
Mkt. Capitalization	3.2%
FDI	1.6%
Private Loans	20.2%





InvestCap.

Nishat Mills Limited (NML)

Bloomberg Code	NML PK	Shr. 52W High, Low	Rs71 Rs38
Reuters Code	NML KA	Last Closing	Rs40.45
No. of Shares	351.6mn	Target Price	Rs62
Avg. Daily Vol. (1-Y)	1.75mn	Upside Potential	53.00%

Buy

Strengths

- Investments in MCB, DGKC, Nishat Power, AES Lal Pir and AES Pak Gen provide diverse exposure to various businesses in the country.
- Continued dividend income from investment in Group companies nullifies the impact of any downward fluctuation in the core business profitability.
- Weakness in the PKR against the major currencies provides cushion of bargaining in the international markets.

Weaknesses

- Appreciation in PKR against USD and Euro reduces company's margins.
- Any hike in the interest rates could increase the borrowing cost thus affecting the bottomline of the company.
- Increase in power and gas tariffs could increase the cost of production of the company.

Potential Drivers

- Low cost inventory improves margins with price increase in the international markets.
- Continued PKR depreciation against USD and Euro is expected to improve net margins going forward.
- Profitability of the company would be enhanced by reversal in cotton prices.

Cotton Prices Impact in FY12 (Rs/sh)

Cotton (per maund)	5,000	6,003	7,000
TP	57.65	59.43	61.22
EPS FY11	5.32	9.50	13.69

Cotton Prices Impact in FY13 (Rs/sh)

Cotton (per maund)	5,000	5,702	7,000
TP	58.24	59.43	60.62
EPS FY12	4.94	8.81	10.22

Company Financial Highlights

Rs mn	FY11A	FY12E	FY13F
Net Sales	48,565	34,326	33,032
Gross Profit	7,846	4,983	4,342
Other Income	2,445	2,193	2,447
Profit After Tax	4,844	3,340	3,096
EPS (Rs) @ 352 mn sh.	13.78	9.50	8.81
DPS (Rs) @ 352 mn sh.	3.30	2.28	2.11
P/E	2.94	4.26	4.59
P/BV	0.40	0.37	0.35
Dividend Yield	8.1%	5.6%	5.2%
Return on Equity	14.5%	9.1%	7.9%
Return on Assets	9.7%	6.3%	6.0%

Nishat Chunian Limited (NCL)

Bloomberg Code	NCL PK	Shr. 52W High, Low	Rs29Rs16
Reuters Code	NCL KA	Last Closing	Rs17.86
No. of Shares	162.09mn	Target Price	Rs31
Avg. Daily Vol. (1-Y)	1.20mn	Upside Potential	73.90%

Buy

Strengths

- One of the major exporters of bed sheets to the US and European markets among the Textiles sector peers in Pakistan.
- Improving other income on the back of dividends from NCPL provides cushion to company's bottomline against any unusual decline in core business.
- Continuing depreciation in PKR against USD and Euro helps improve primary margins of the company, as it makes company product more competitive.
- Local availability of raw material saves the company from any international price influence impacting the cost side.

Weaknesses

- Appreciation in PKR against USD and Euro reduces core margins of the company. Company's bottomline is highly sensitive to changes in interest rates due to heavy leverage on its books, thus affecting company's bottomline significantly.
- Increase in power and gas tariff could increase the cost of production of the company.

Potential Drivers

- Low-cost inventory improves margins with price increase in the international market.
- Reversal in the cotton prices would improve profitability of the company.

Cotton Prices Impact in FY12 (Rs/sh)

Cotton (per maund)	5,000	6,003	7,000
TP	30.12	31.05	32.60
EPS FY11	3.82	6.82	9.82

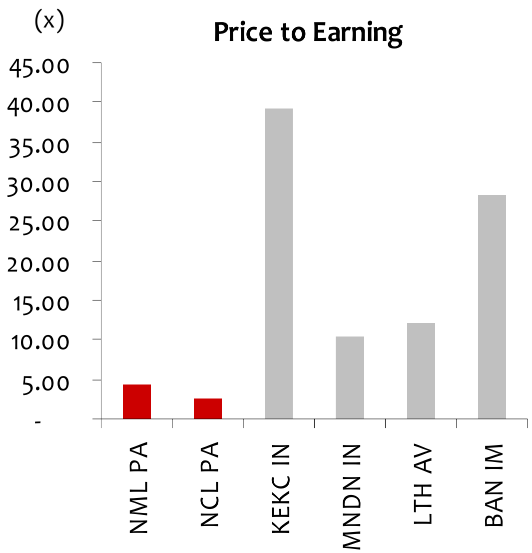
Cotton Prices Impact in FY13 (Rs/sh)

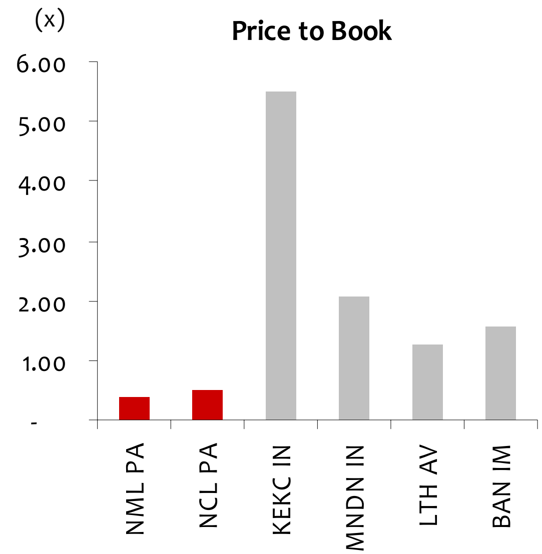
Cotton (per maund)	5,000	5,702	7,000
TP	30.43	31.05	32.91
EPS FY12	3.52	6.28	9.42

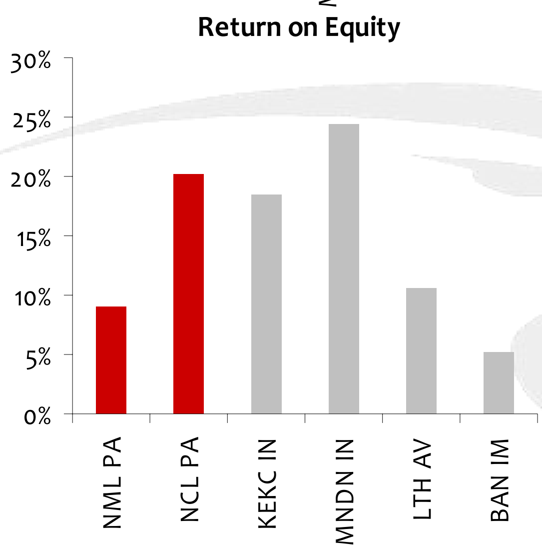
Company Financial Highlights

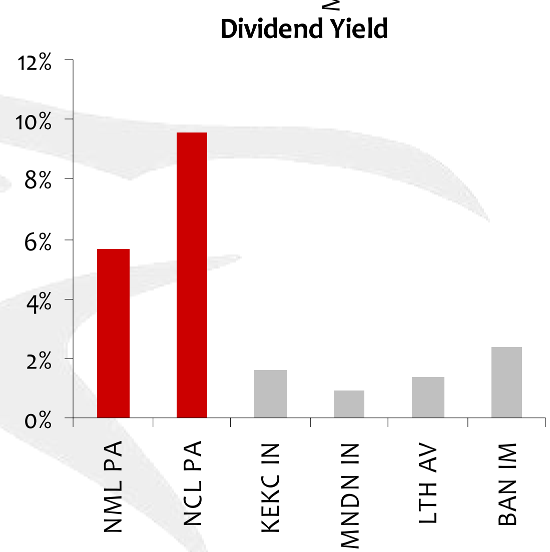
Rs mn	FY11A	FY12E	FY13F
Net Sales	20,322	17,325	16,955
Gross Profit	3,409	2,746	2,562
Other Income	604	563	536
Profit After Tax	1,459	1,129	1,039
EPS (Rs) @ 165 mn sh.	8.82	6.82	6.28
DPS (Rs) @ 165 mn sh.	2.00	1.71	1.57
P/E	2.03	2.62	2.84
P/BV	0.55	0.48	0.43
Dividend Yield	11.2%	9.6%	8.8%
Return on Equity	30.2%	20.1%	16.3%
Return on Assets	9.2%	6.7%	6.5%

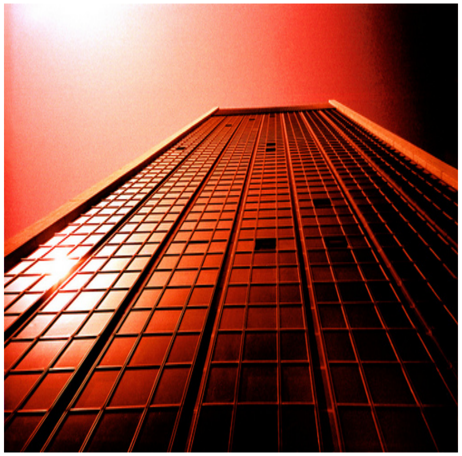
Regional Attractiveness











Cement

Infrastructural development the way forward

Cement

Positive

- Cement sector is largely linked with the economic growth of the country. However, due to economic slowdown, infrastructural activities remain stagnant. At the same time proper utilization of the Public Sector Development Program (PSDP) should be considered as a trigger for the sector. Out of total Rs730bn budgeted under the PSDP head for FY12, around 60% remains unutilized by far.

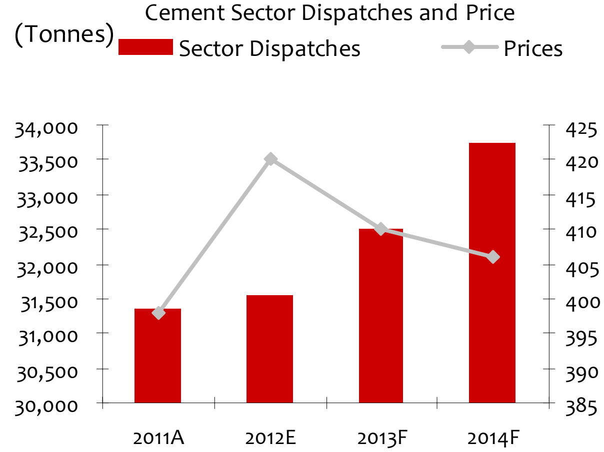
- Complete reduction of import duty on shredded tyres is expected to aid the cement sector in bringing down its cost of production. The import duty currently stands at 20%.

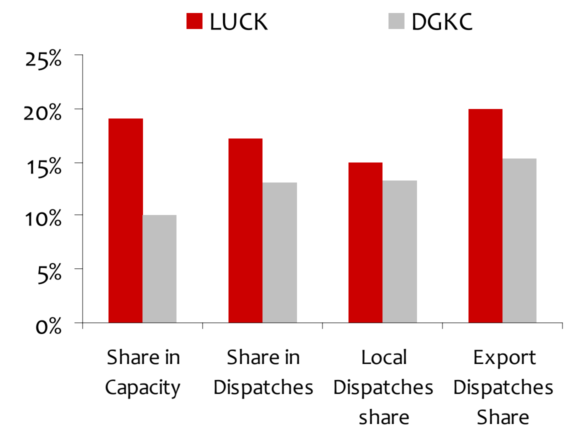
- Demand from Afghanistan and India are on the positive track. Meanwhile, due to price attractiveness of Pakistani cement (cement prices in Pakistan are at 16% discount to those prevailing in India), the demand from both the countries are expected to improve onwards.

- Prices at the local front are hovering around Rs420/bag in northern and Rs405/bag in south region in the country (up 24% YTD), while int’l coal prices eased up to USD108/tons (down 11% YTD). At the same time, the sector giants are implementing cost efficiency measures (TDF, RDF, WHR). This phenomenon is expected to bode well for manufacturers’ core margins in the upcoming months and years.

Outlook

- In the upcoming year, we expect 1) better PSDP utilization 2) MFN provided status to India to yield material results 3) higher domestic cement prices 4) lowering int’l coal prices and construction of mega dams to be the triggers for the sector.





Impact Of Coal Prices On Earnings*

Coal USD/TON	95	100	110	115
FY12 EPS				
LUCK	2.56	1.28	-1.28	-2.56
DGKC	1.53	0.75	-0.75	-1.53
FCCL	0.15	0.07	-0.07	-0.15

*Base case is USD105/ton

Lucky Cement Limited (LUCK)

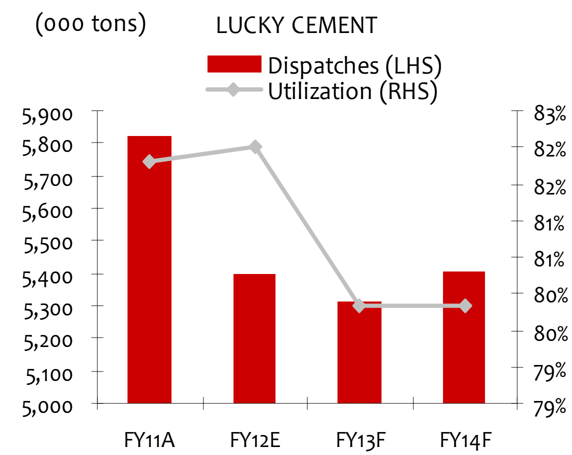
Bloomberg Code	LUCK PK	Shr. 52W High, Low	Rs84 Rs60
Reuters Code	LUCK KA	Last Closing	Rs75.04
No. of Shares	323.38mn	Target Price	Rs101
Avg. Daily Vol. (1-Y)	1.1mn Sh.	Upside Potential	35.00%

Buy

Strengths

- The company holds 14% share in total local dispatches while 25% share in export dispatches. Thus, LUCK can be regarded as the market leader of the cement industry of Pakistan. The company holds 19% of the total industry capacity while it has a strong ability to capture both local and export demand.

- Company has implemented WHR plan as well as TDF (Tire Derived Fuel) successfully, which is expected to be operational by end Jan-12. These initiatives are expected to turn company's reliance away from fluctuating int'l coal prices, simultaneously improving company's overall margins going forward.



Weaknesses

- Depressed local demand, along with faltering export dispatches is expected to be a major concern for the company as it holds big chunk of the industry dispatches.

- Excess cement supply in the country along with lower demand on export front can result in price depreciation in the country thereby affecting company margins.

Potential Drivers

- Prices in the local market showed stickiness at the peak winter season, despite lowering demand, it would derive cement manufacturers' margins upward when demand restores in the 2H of the year.

- Decrease in int'l coal prices and increased cost efficiency measure could be seen as a healthy trigger for LUCK.

Company Financial Highlights

Rs mn	FY11A	FY12E	FY13F
Net Sales	26,018	25,300	26,283
Gross Profit	8,711	8,843	9,224
Other Income	2	163	126
Profit After Tax	3,970	5,393	6,439
EPS (Rs) @ 323 mn sh.	12.28	16.68	19.91
DPS (Rs) @ 323 mn sh.	4.00	4.00	4.50
P/E	6.11	4.50	3.77
P/BV	0.87	0.76	0.66
Dividend Yield	5.3%	5.3%	5.3%
Return on Equity	14.3%	16.9%	17.5%
Return on Assets	10.0%	12.5%	14.4%

DG Khan Cement (DGKC)

Bloomberg Code	DGKC PK	Shr. 52W High, Low	RS23 Rs18
Reuters Code	DGKC KA	Last Closing	Rs19.03
No. of Shares	438.12mn	Target Price	Rs27.00
Avg. Daily Vol. (1-Y)	2.5mn Sh.	Upside Potential	42.00%

Buy

Strengths

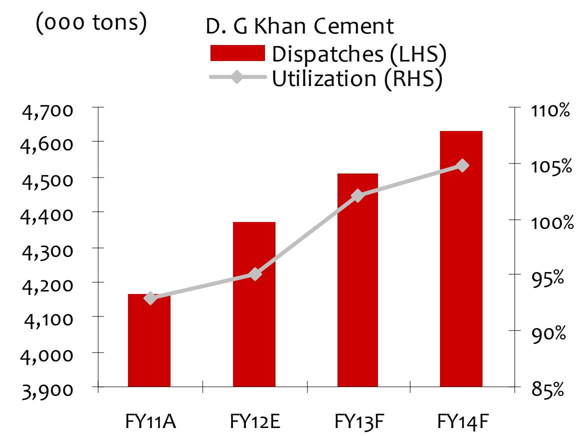
- DGKC is associated with one of the biggest and opulent groups in the country, Nishat Group. The major portion of the company income comes from its investment in different Group companies, such as MCB, AICL and NML.
- More probably, MFN status given to India would help in removing NTBs (Non Tariff Barriers) and the country will be allowed to export cement through roads. This would help DGKC offload its excess cement supply on to Indian territory.

Weaknesses

- The company is still facing a huge financial burden in prevailing interest rate scenario. Any increase in interest rates severely impacts company bottomline.
- Company's bottomline is more dependent on investment income. Therefore any threat to portfolio of investments would be a dampener for DGKC's profitability.

Potential Drivers

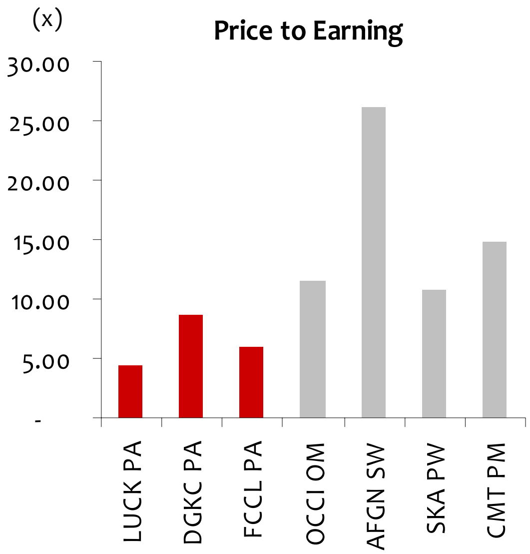
- Prices in the northern region are hovering around Rs420/bag despite chilling winter season. This phenomenon would help the company sustain and even increase its core business margins from 2HFY12 onwards.
- Cost efficiency measures including WHR,RDF along with construction of Dams in the north and lowering int'l coal prices would potentially driver bottomline.

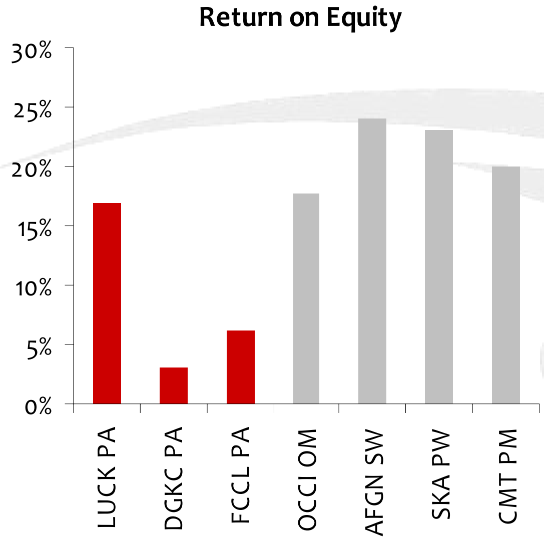


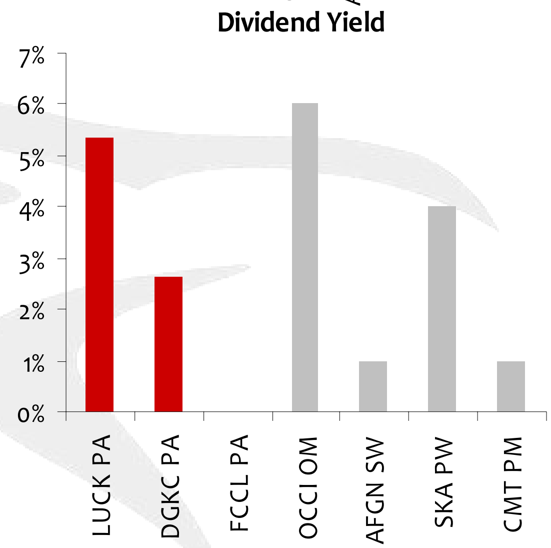
Company Financial Highlights

Rs mn	FY11A	FY12E	FY13F
Net Sales	18,577	20,092	21,446
Gross Profit	4,385	5,191	4,877
Other Income	1,107	1,127	1,074
Profit After Tax	171	960	712
EPS (Rs) @ 438 mn sh.	0.39	2.19	1.63
DPS (Rs) @ 438 mn sh.	-	0.50	-
P/E	48.77	8.68	11.71
P/BV	0.28	0.27	0.26
Dividend Yield	0.0%	2.6%	2.6%
Return on Equity	0.6%	3.1%	2.2%
Return on Assets	0.4%	2.0%	0.0%

Regional Attractiveness







Chemicals

Attracting the reaction

Chemicals

Positive

- Favorable oil price movements are expected to help in pulling the much subdued primary margins of many different chemicals on individual basis.

- Free fall in cotton prices due to bumper crop in China and India, has squeezed the Polyester Staple Fiber (PSF) margins globally, while any upward reversal in the price of cotton is expected to be the major trigger for PSF margins revival.

- Increase in the import duty of Purified Terephthalic Acid (PTA) from 4% to 8% would provide Lotte PTA Pakistan with enough security the Group requires to invest in the country in order to double its production capacity.

Outlook

- Most Favored Nation (MFN) status given to India is expected to resume trades between the two counties. We foresee this to have considerably positive impact on the country’s Chemical sector as excess supplies can then be easily exported to India.

ICI Pakistan Limited (ICI)

Bloomberg Code	ICI PK	Shr. 52W High, Low	Rs170 Rs112
Reuters Code	ICI KA	Last Closing	Rs120.27
No. of Shares	138.8mn	Target Price	Rs153
Avg. Daily Vol. (1-Y)	0.21mn Sh.	Upside Potential	27.00%

Buy

Strengths

- The company has a diversified product line that enables it to cater to the demand of different consumer segments.
- The company's global brand name and its affiliation with AkzoNobel Group enables ICI to maintain larger penetration in the local market.
- ICI remains the market leader in paints and soda ash business.

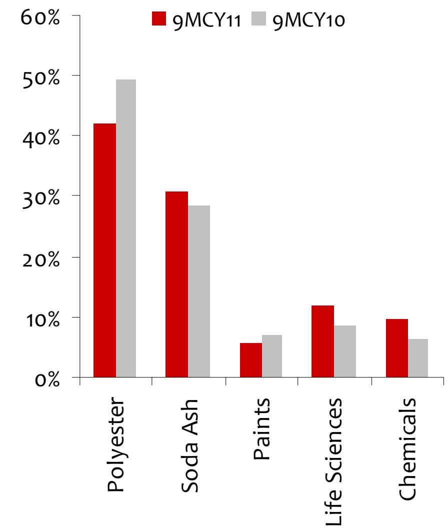
Weaknesses

- Low cotton prices have forced a fall in the demand of PSF
- Gas curtailment has continuously haunting company's soda ash business.

Potential Drivers

- Increase in the margins of PSF to PTA and MEG.
- Escalation in the price of cotton to pull the boost the sales of PSF business.

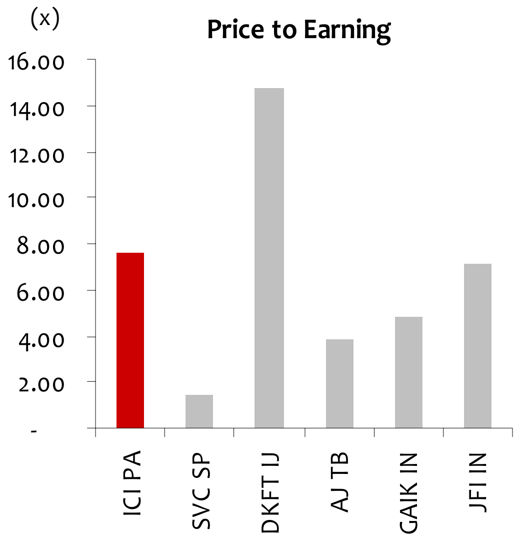
Segment wise Income Contribution

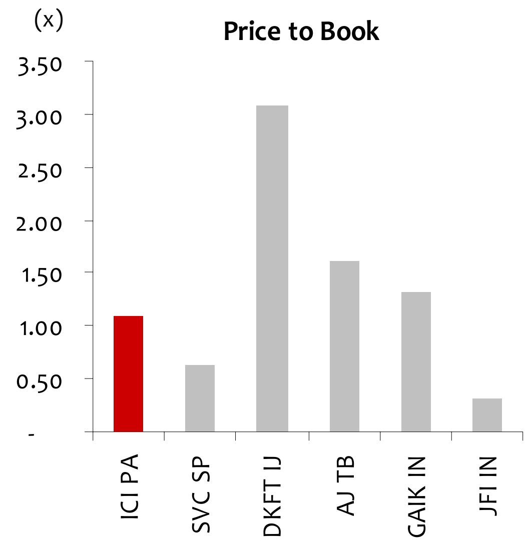


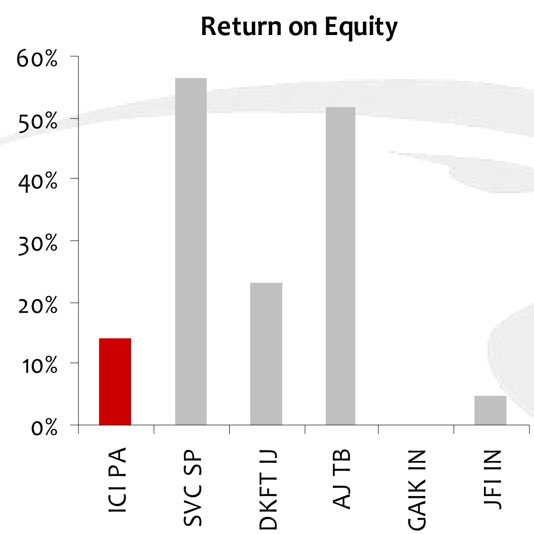
Company Financial Highlights

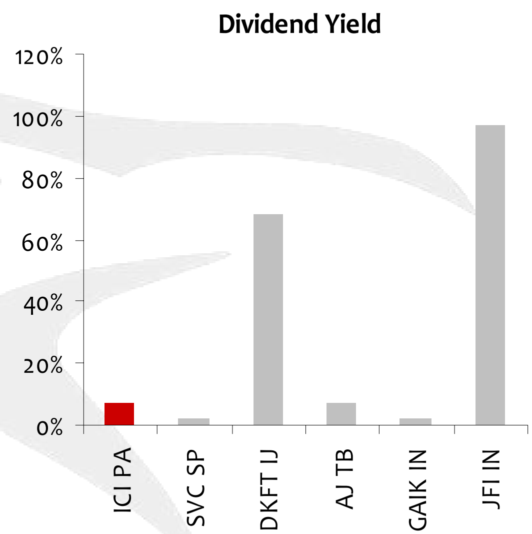
Rs mn	CY10A	CY11E	CY12F
Net Sales	35,130	41,022	43,074
Gross Profit	6,686	6,266	5,867
Operating Income	3,713	3,394	2,851
Profit After Tax	2,429	2,180	1,818
EPS (Rs) @ 139 mn sh.	17.50	15.70	13.10
DPS (Rs) @ 139 mn sh.	12.00	9.00	8.00
P/E	6.87	7.66	9.18
P/BV	1.15	1.09	1.05
Dividend Yield	10.0%	7.5%	6.7%
Return on Equity	16.7%	14.2%	11.4%
Return on Assets	11.9%	10.3%	8.2%

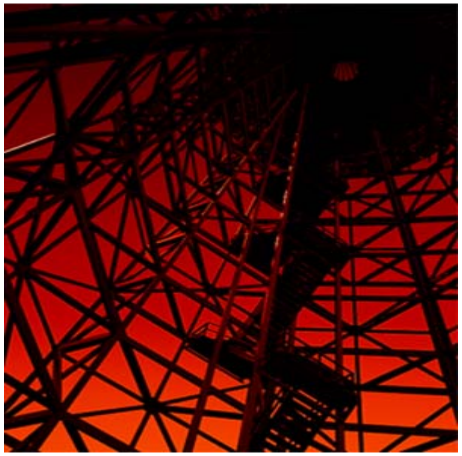
Regional Attractiveness











Telecom

Rise of the next generation

Telecom

Neutral

- Despite economic slump, teledensity levels in the country continued to rise during FY11, reaching 69% by Jun-11 end. Meanwhile, telecom revenues also recovered more sharply in FY11 (6.7% YoY) after dip witnessed in growth a year earlier (1.5% YoY). Despite revenue growth, competition remains stiff, straining bottomline growth of the sector. Cost reduction and introduction of value-added services stay as the ideal strategy for survival and growth.

- Cellular segment continues to lead the sector in terms of penetration, revenues and overall contribution in growth. The latest in the offing is the auction of frequency spectrum (expected by Mar-12) for introduction of technologies under 3G, 4G or related LTE regime. The gov't plans to raise ~USD1.0bn through the auction of 3 licenses. However, given past record and tricky nature of 3G technology, the auction could get further delayed despite gov't efforts, as 3G is not only costly but also turns difficult to sustain as many of the services under 3G are still infant and could face difficulty in finding suitable markets.

- The issue of dues from Etisalat against PTC acquisition remains unresolved. The remaining amount of USD800mn, if realized during FY12, could provide much needed support to external account of the country during the period.

Outlook

- Apart from the potential of valuable foreign exchange, 3G auction could redefine the use of broadband and related data services in Pakistan. The shift could also alter the state of competition among the cellular operators in the country, which could potentially result in mergers or acquisitions. However, the same could take time to materialize depending upon the magnitude of investment deployed, the kind of technologies launched and success of the same.

Global 3G auctions

Country	Avg amount per license (USD mn)
UK	7,082
Germany	7,721
Italy	2,017
Hong Kong	168
Taiwan	279
India	1,839
Global Average	1,309
Pakistan (est.)	300

Outstanding dues from Etisalat

Installment	Amount (USD mn)	Status
Jun-05	260	Paid
Apr-05	1140	Paid
Sep-06	133	Paid
Mar-07	133	Paid
Sep-07	133	Paid
Mar-08	133	Deferred
Sep-08	133	Deferred
Mar-09	133	Deferred
Sep-09	133	Deferred
Mar-10	133	Deferred
Sep-10	133	Deferred

Pakistan Telecom Company (PTC)

Bloomberg Code	PTC PK	Shr. 52W High, Low	Rs20 Rs10
Reuters Code	PTC KA	Last Closing	Rs10.39
No. of Shares	3.77bn	Target Price	Rs23.00
Avg. Daily Vol. (1-Y)	2.02mn Shr.	Upside Potential	125.00%

Buy

Strengths

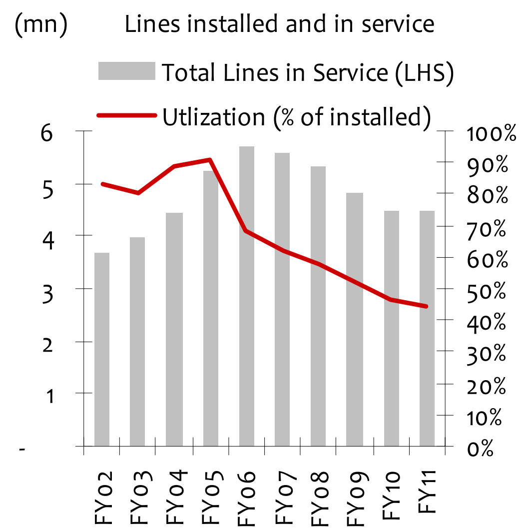
- Being the sole carrier service provider in the country, PTC enjoys a unique position with leadership in voice and data services.
- Through its wholly owned subsidiary, PTC benefits hugely from Ufone dividends, which contributed ~Rs0.6/share in FY11 to PTC bottomline.

Weaknesses

- Fixed line dependency still remains at large, although the company has been taking measures to slowdown the pace of decline.
- High operating leverage in the form of admin cost and rise in salary expense often thin down bottomline amid limited topline growth.

Potential Drivers

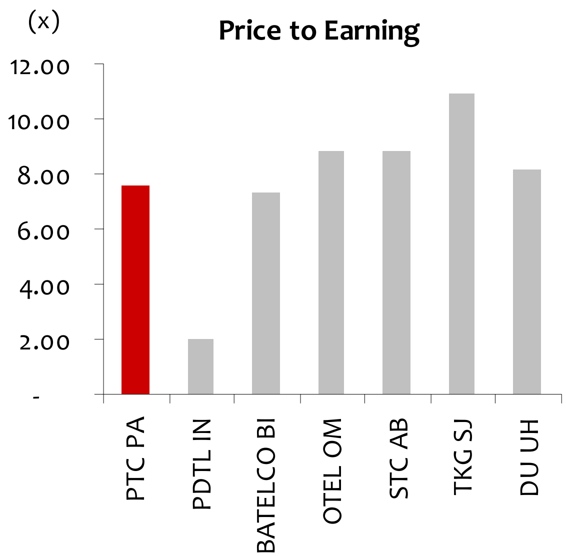
- PTC continues to maintain highest share in the broadband segment, while also maintain leadership in the WLL segment.
- With cellular segment dynamics staying sharp, introduction of 3G technology would further shift the sector, while PTC can continue to take benefit of technological advancement and up gradation in the cellular segment through its subsidiary Ufone.

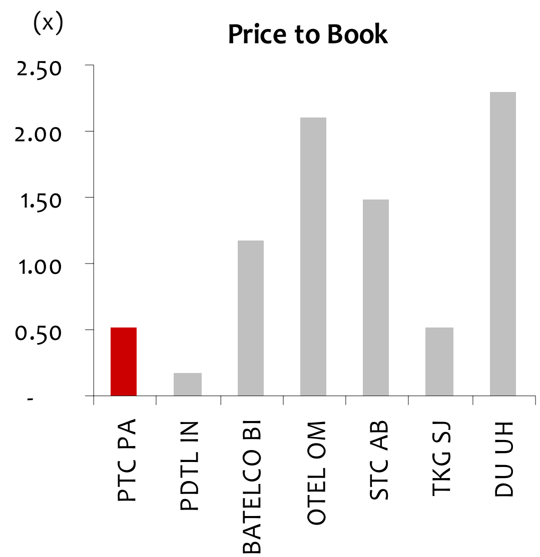


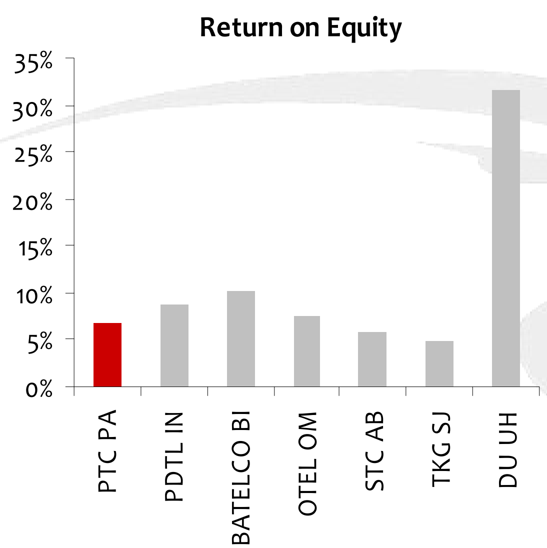
Company Financial Highlights

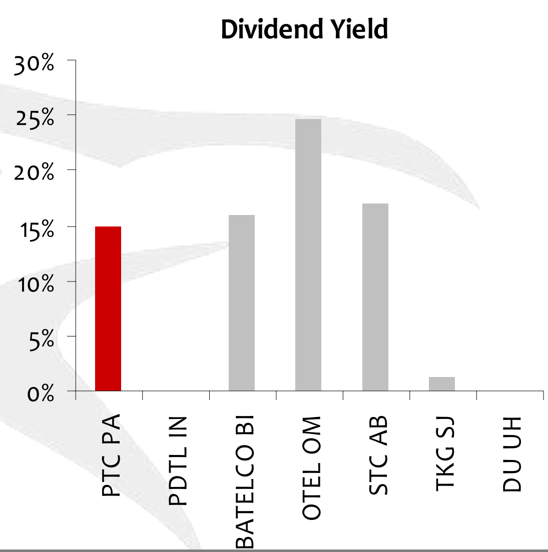
Rs mn	FY11A	FY12E	FY13F
Revenue	55,254	57,641	60,540
Gross Profit	13,439	14,825	15,433
Other Income	7,840	6,119	6,095
Profit After Tax	7,428	6,716	6,822
EPS (Rs) @ 5,100 mn sh.	1.46	1.32	1.34
DPS (Rs) @ 5,100 mn sh	1.75	1.50	1.50
P/E	7.13	7.89	7.77
P/BV	0.54	0.54	0.55
Dividend Yield	16.8%	14.4%	14.4%
Return on Equity	7.6%	6.9%	7.1%
Return on Assets	4.9%	4.5%	4.5%

Regional Attractiveness









Banks

This left feels 'right'

Banks

Positive

- Banking sector deposits have experienced expansion of 6% CY11TD, highlighting the ability of the domestic banking sector to pioneer new products that have been successful in attracting deposits.

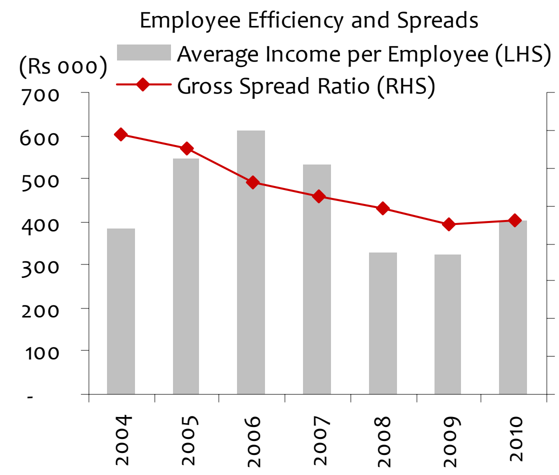
- Due to prevailing law & order situation coupled with energy crisis, demand of credit from the private sector has virtually dried up. As a result, a shift in the revenue means of the sector has been experienced, which is further clarified by unprecedented increase of 32% CY11TD in the investments made by the banking sector. Conversely, advances have shrunk by 2% CY11TD.

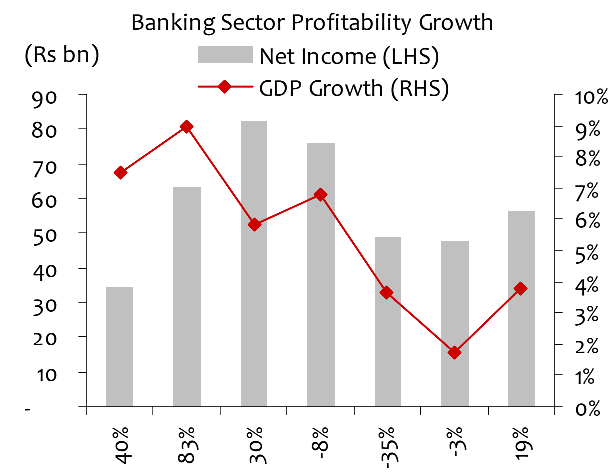
- Despite the decrease in the asset size (advances) of the banking sector, rate of infected advances has grown rapidly during 3QCY11, where the gross infection ratio of the sector was recorded at 18%. This signifies how additional markup on the already infected loans is further inflating the infection of the banking sector advances.

- With SBP's MCR imposition of Rs8bn by end of CY11, we expect a series of mergers and acquisitions to resume in the banking sector this year. This is expected to lessen the risk of the overall sector.

Outlook

- Average spreads of the sector during 9MCY11 have been witnessed at 7.36%, 23bps lower as compared to same period last year, and since then, the policy rate has been slashed by 200bps to 12%. However, latest surge in the private sector credit offtake indicates that going forward, the banks are expected to strengthen their falling ADRs. The sector is expected to enjoy profitability with more focus on advances than investments, going forward.





United Bank Limited (UBL)

Bloomberg Code	UBL PK	Shr. 52W High, Low	Rs70 Rs51
Reuters Code	UBL KA	Last Closing	Rs52.39
No. of Shares	1,114mn	Target Price	Rs67.00
Avg. Daily Vol. (1-Y)	0.44mn Sh.	Upside Potential	28.00%

Buy

Strengths

- UBL is the second largest private sector bank in the country in terms of asset size. with one of the most active corporate and investment banking businesses.

- Widely spread network of 1,167 branches signifies UBL's presence throughout the country. In addition, UBL's branchless banking services, UBL Omni, has broadened the banks presence in over 600 cities and towns. Across the country. This has enabled UBL to maintain its strong leadership in Government to Person (G2p) payments.

Weaknesses

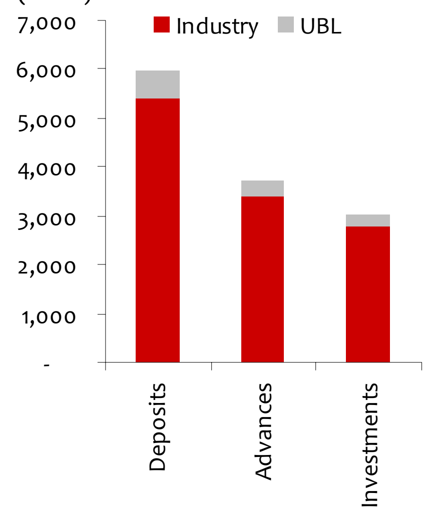
- UBL has not been able to actively attract fresh funds from customers in the form of deposits, which can be witnessed by banks deposit base that grew by mere 1.2% during 9MCY11 as compared to industry deposit growth of 6% during the same period.

- Presently, the bank has 15% of its gross advances infected, which is the highest amongst the other top-tier banks, with nearly 50% of the infection taking place in consumer and textile segment advances.

Potential Drivers

- With gov't proposal of conversion of energy sector's debt into gov't securities, ~11% of UBL's gross advances are expected to be converted into more secure revenue stream, thus positively impacting bank's profitability, going forward.

UBL comparison with Industry



Company Financial Highlights

Rs mn	CY10A	CY11E	CY12F
Net Interest Income	34,109	40,942	41,632
Provisions	8,005	9,958	10,015
Other Opt Income	10,121	11,681	12,227
Profit After Tax	11,160	14,338	13,846
EPS (Rs) @ 1,224 mn sh.	9.12	11.71	11.31
DPS (Rs) @ 1,224 mn sh	5.00	5.50	6.00
P/E	5.75	4.47	4.63
P/BV	0.94	0.80	0.71
Dividend Yield	4.3%	5.7%	7.6%
Return on Equity	17.3%	19.1%	16.2%
Return on Assets	1.7%	2.0%	1.7%

Allied Bank Limited (ABL)

Bloomberg Code	ABL PK	Shr. 52W High, Low	Rs72 Rs54
Reuters Code	ABL KA	Last Closing	Rs53.87
No. of Shares	860.31mn	Target Price	Rs73
Avg. Daily Vol. (1-Y)	0.11mn Sh.	Upside Potential	36.00%

Buy

Strengths

- The bank's IDR has risen by a massive 21.3pps, suggesting that bank is now targeting safer means to achieve its revenue targets.
- The bank has extensive presence in the Punjab province, primarily in areas that are indulged in agriculture. This has enabled the bank to venture into the untapped areas.
- The bank enjoys the least infected advances among top private banks of the sector. This signifies the high quality of advances portfolio that the bank successfully maintains.

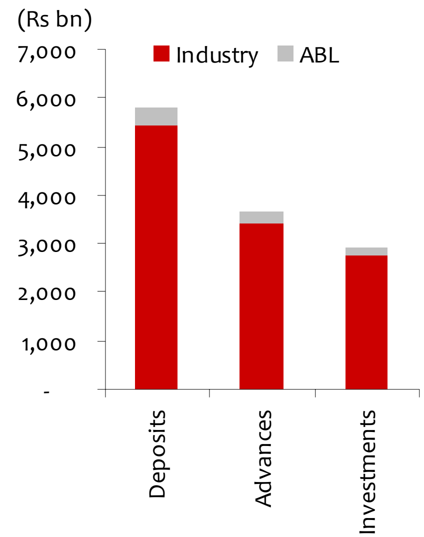
Weaknesses

- ADR of the bank has fallen to ~54% during 9MCY11 from the level of ~62% witnessed during CY10, showcasing that bank is straying away from its core banking activities.
- Bank's deposits witnessed growth of 9% during 1HCY11. However, during 3QCY11 deposit base of the base shrank by 5% QoQ. This suggests that bank has not been successful in maintaining its deposit base.

Potential Drivers

- With a number of relatively smaller banks failing to meet the MCR of the SBP, it provides ABL with an opportunity to expand by acquiring such banks and as a result, increasing its asset base and branch network amongst many other areas.

ABL comparison with Industry



Company Financial Highlights

Rs mn	CY10A	CY11E	CY12F
Net Interest Income	22,565	26,957	30,171
Provisions	4,083	3,940	4,668
Other Opt Income	5,672	5,513	6,954
Profit After Tax	8,225	10,599	12,113
EPS (Rs) @ 860 mn sh.	9.56	12.32	14.08
DPS (Rs) @ 860 mn sh.	4.00	5.00	5.50
P/E	5.63	4.37	3.83
P/BV	1.29	1.05	0.89
Dividend Yield	6.8%	9.3%	11.2%
Return on Equity	24.7%	25.7%	24.4%
Return on Assets	1.9%	2.2%	2.3%

Bloomberg Code	MCB PK	Shr. 52W High, Low	Rs248 Rs135
Reuters Code	MCB KA	Last Closing	Rs134.60
No. of Shares	836.24mn	Target Price	Rs185.00
Avg. Daily Vol. (1-Y)	0.68mn Sh.	Downside Risk	37.00%

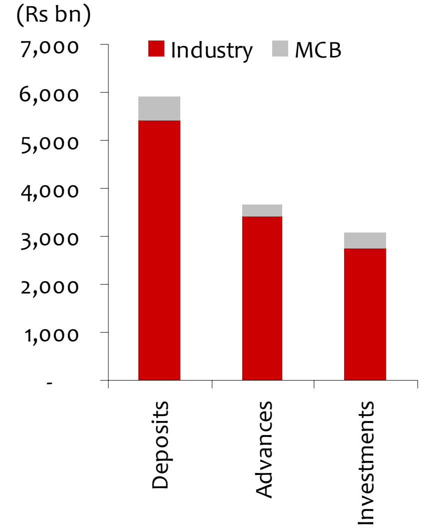
MCB Bank Limited (MCB)

Buy

Strengths

- MCB is the leading performer of the Pakistani banking industry having 33% share in the total profitability amongst the top-4 local private banks. During the year, the bank has been awarded with The Most Stable Bank title by CFA Association of Pakistan along with Best Bank in Pakistan award given by the EUROMONEY.
- The bank is highly successful in attracting fresh deposits, which has been highlighted by the sheer pace of bank's deposit growth, as in 9MCY11 MCB's deposit base grew by twice the velocity of the industry's, growing at 12%.

MCB comparison with Industry



Weaknesses

- Amongst the top-tier private banks of the country, MCB has the weakest Retail and Consumer banking business. During previous year, the income from the said business division decreased by 16% YoY, while cost of the doing business rose by ~3% during the same period.
- The bank is very susceptible to falling interest rates as it has a huge low-cost deposit base (CASA mix).

Potential Drivers

- Extensive foreign selling has exerted undue pressure on the bank's scrip however, fundamentally the bank has experienced no negativity as such. Any revival in private sector credit offtake is expected to provide MCB with an opportunity to enhance its ADR base, thus offsetting the susceptibility of interest rate decline the bank has due to low-cost deposits.

Company Financial Highlights

Rs mn	CY10A	CY11E	CY12F
Net Interest Income	36,834	45,341	44,884
Provisions	3,597	4,359	3,922
Other Opt Income	6,265	6,310	6,641
Profit After Tax	16,873	22,321	21,802
EPS (Rs) @ 836 mn sh.	20.18	26.69	26.07
DPS (Rs) @ 836 mn sh.	11.00	12.00	14.00
P/E	6.67	5.04	5.16
P/BV	1.42	1.25	1.12
Dividend Yield	7.8%	8.9%	11.6%
Return on Equity	22.9%	26.6%	22.9%
Return on Assets	3.1%	3.7%	3.2%

National Bank of Pakistan (NBP)

Bloomberg Code	NBP PK	Shr. 52W High, Low	Rs81 Rs36
Reuters Code	NBP KA	Last Closing	Rs41.05
No. of Shares	1,682mn	Target Price	Rs50
Avg. Daily Vol. (1-Y)	2.8mn Sh.	Upside Potential	22.00%

Buy

Strengths

- National Bank of Pakistan is the largest bank in the country as far as asset size is concerned. It is the only top-tier bank in the country that is a public sector entity.

- The bank has wide range of products that bodes well with its different business segments. The bank's core strength lies in its excellent commercial banking business segment and with the help of this wide portfolio of products, the bank pays close attention to its core business segments.

Weaknesses

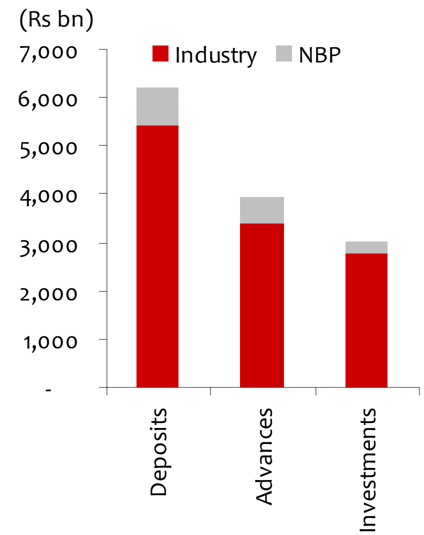
- National Bank's deposits faltered by 4% CYTD against the growth of 6% YoY witnessed in the deposits of the whole industry. In addition to that, the bank has the lowest employee efficiency amongst the big-5 banks.

- The bank's asset infection has increased significantly by ~36% during 9MCY11, highlighting the flaws in the advances' portfolio selection of the bank with nearly 45% of NPLs concentrated in the textile and energy sectors.

Potential Drivers

- When the industry advances' growth is moving reverse, 7% increase in the advances of the bank shows that NBP is one of the most aggressive banks in the sector at the moment. Going forward, the bank is better equipped for further decline in discount rates as compared to its peers in the sector.

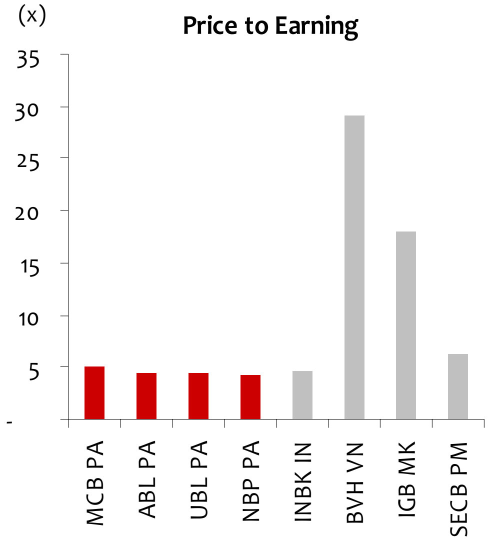
NBP comparison with Industry

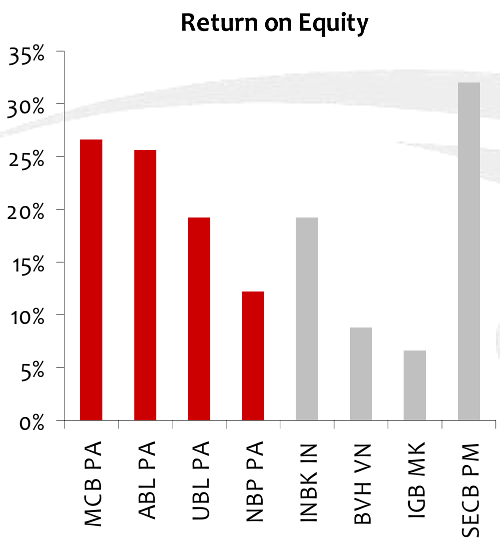


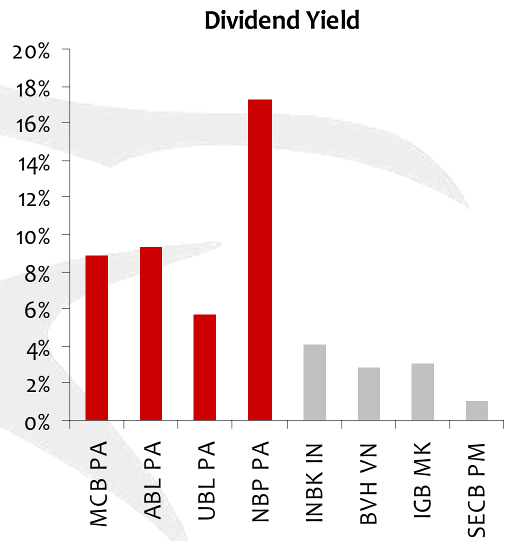
Company Financial Highlights

Rs mn	CY10A	CY11E	CY12F
Net Interest Income	43,222	45,508	53,713
Provisions	9,970	9,729	11,234
Other Opt Income	17,633	17,192	17,720
Profit After Tax	24,415	23,938	28,985
EPS (Rs) @ 1,682 mn sh.	10.44	9.47	11.41
DPS (Rs) @ 1,682 mn sh	8.00	7.00	9.00
P/E	3.93	4.33	3.60
P/BV	0.54	0.54	0.52
Dividend Yield	14.6%	17.3%	20.8%
Return on Equity	14.2%	12.2%	14.0%
Return on Assets	1.8%	1.6%	1.9%

Regional Attractiveness







Earnings Guide

Ticker	Price*	Mkt. Cap.	Target Price*		EPS*			DPS*			PE			Dividend Yield		
	30-Dec-11	USD mn	Dec-12	Recom.	2011	2012	2013	2011	2012	2013	2011	2012	2013	2011	2012	2013
ABL	53.87	49,768	73.0	Buy	12.32	14.08	12.75	5.00	6.05	6.66	4.37	3.83	4.23	9.3%	11.2%	12.4%
ATRL	107.65	9,333	149.9	Buy	25.62	25.54	28.54	2.00	2.00	2.00	1.82	1.82	1.63	1.9%	1.9%	1.9%
AICL	87.24	6,811	68.0	Buy	4.83	10.28	15.42	2.36	2.88	3.62	9.64	4.52	3.02	2.7%	3.3%	4.2%
APL	412.50	25,575	484.0	Buy	61.58	70.10	78.29	41.50	45.00	50.00	6.70	5.88	5.27	10.1%	10.9%	12.1%
BAFL	11.25	14,728	14.0	Buy	2.89	3.18	3.50	0.44	0.87	0.95	3.89	3.54	3.22	4.0%	7.7%	8.5%
DGKC	19.03	8,967	27.0	Buy	0.39	2.19	1.63	0.00	0.50	0.00	48.77	8.68	11.71	0.0%	2.6%	0.0%
ENGRO	92.70	49,663	210.0	Buy	22.16	31.41	39.95	6.00	7.00	8.00	4.18	2.95	2.32	6.5%	7.6%	8.6%
FABL	8.13	7,300	13.4	Buy	2.21	3.57	3.66	0.22	0.71	0.73	3.69	2.28	2.22	2.7%	8.8%	9.0%
FCCL	3.30	3,824	3.5	Hold	0.32	0.56	0.54	0.00	0.00	0.00	10.30	5.91	6.13	0.0%	0.0%	0.0%
FFC	149.54	125,837	251.0	Buy	24.01	28.54	28.33	22.25	26.50	27.00	6.23	5.24	5.28	14.9%	17.7%	18.1%
FFBL	42.43	41,626	76.0	Buy	10.88	8.30	8.86	9.75	7.25	7.75	3.90	5.11	4.79	23.0%	17.1%	18.3%
HBL	106.08	122,437	131.9	Buy	19.92	20.32	20.72	6.65	9.64	10.82	5.33	5.22	5.12	6.3%	9.1%	10.2%
HCAR	8.64	1,500	14.0	Buy	(1.85)	0.52	2.65	0.00	0.00	0.00	N/M	16.60	3.27	0.0%	0.0%	0.0%
HUBC	34.20	40,872	52.0	Buy	4.69	5.24	5.22	5.50	5.24	5.22	7.30	6.53	6.55	16.1%	15.3%	15.3%
ICI	120.27	18,525	153.0	Buy	15.70	13.10	11.16	12.00	9.00	8.00	7.66	9.18	10.78	10.0%	7.5%	6.7%
INDU	205.03	17,567	268.0	Buy	34.90	31.44	33.84	15.00	13.51	14.54	5.87	6.52	6.06	7.3%	6.6%	7.1%
KAPCO	41.32	36,613	60.0	Buy	7.43	6.23	5.27	6.50	5.03	4.49	5.56	6.63	7.84	15.7%	12.2%	10.9%
LUCK	75.04	23,530	101.0	Buy	12.28	16.68	19.91	4.00	4.00	4.50	6.11	4.50	3.77	5.3%	5.3%	6.0%
MCB	134.60	134,513	185.0	Buy	26.69	26.07	22.88	12.00	14.00	13.73	5.04	5.16	5.88	8.9%	10.4%	10.2%
NBP	41.05	76,334	50.0	Buy	9.47	11.41	12.04	7.10	8.55	7.23	4.33	3.60	3.41	17.3%	20.8%	17.6%
NCL	17.86	3,271	31.0	Buy	8.82	6.82	6.28	1.96	1.71	1.57	2.03	2.62	2.84	11.0%	9.6%	8.8%
NML	40.45	17,070	62.0	Buy	13.78	9.50	8.81	3.30	2.28	2.11	2.94	4.26	4.59	8.2%	5.6%	5.2%
NRL	242.69	20,467	322.7	Buy	82.14	49.49	70.60	25.00	15.00	20.00	2.95	4.90	3.44	10.3%	6.2%	8.2%
OGDC	151.62	654,196	173.9	Hold	14.77	20.18	23.15	5.50	6.50	7.00	10.26	7.51	6.55	3.6%	4.3%	4.6%
PKGS	82.72	8,008	132.0	Buy	(13.30)	(17.35)	(0.36)	0.00	0.00	0.00	N/M	N/M	N/M	0.0%	0.0%	0.0%
POL	346.45	74,834	485.6	Buy	45.72	62.67	66.23	35.00	40.00	40.00	7.58	5.53	5.23	10.1%	11.5%	11.5%
PPL	168.32	228,400	262.5	Buy	23.92	31.51	34.81	10.91	15.00	15.00	7.04	5.34	4.83	6.5%	8.9%	8.9%
PSMC	59.03	5,167	66.0	Hold	8.99	6.69	6.36	0.50	0.50	0.50	6.57	8.82	9.28	0.8%	0.8%	0.8%
PSO	227.21	43,224	277.0	Buy	86.17	57.73	57.05	10.00	15.00	20.00	2.64	3.94	3.98	4.4%	6.6%	8.8%
PTC	10.39	72,851	23.4	Buy	1.46	1.32	1.34	1.75	1.50	1.50	7.13	7.89	7.77	16.8%	14.4%	14.4%
SHEL	190.28	13,686	180.0	Sell	27.96	31.23	34.20	13.98	18.95	23.13	6.81	6.09	5.56	7.3%	10.0%	12.2%
SNGP	15.71	11,493	21.0	Buy	1.95	1.98	1.41	0.95	0.95	0.95	8.05	7.92	11.16	6.1%	6.1%	6.1%
SSGC	19.29	17,316	23.1	Buy	5.36	5.46	5.20	2.38	2.62	4.40	3.60	3.53	3.71	12.3%	13.6%	22.8%
UBL	52.39	69,407	67.0	Buy	11.71	11.31	12.42	3.00	4.00	6.00	4.47	4.63	4.22	5.7%	7.6%	11.5%
ULEVER	5565.80	71,673	4,546.0	Sell	271.18	309.22	324.70	180.00	230.00	260.00	20.52	18.00	17.14	3.2%	4.1%	4.7%

Note: Number of shares are updated according to book closures; Companies valuations are based on their respective year ends, * In PKR per share

List of Abbreviation

3G	3rd Generation
4G	4th Generation
ADR	Advance to Deposit Ratio
AL	Arab Light
BN	Billion
BOP	Balance of Payments
BPD	Barrel per day
BPS	Basis Points
BTU	British Thermal Unit
BV	Book Value
CAD	Current Account Deficit
CAGR	Compound Average Growth Rate
CAR	Capital Adequacy Ratio
CFY	Cashflow Yield
CNG	Compressed Natural Gas
CPI	Consumer Price Index
CRR	Cash Reserve Requirement
CY	Calendar Year
CY11TD	Caldendar Year 11 till date
DAP	Diammonium Phosphate
DEP	Depreciation
DPS	Dividend per share
DSC	Defence Savings Certificates
DY	Dividend Yield
DHDS	Diesel Hydro Desulphurization
E&P	Exploration & Production
EBIT	Earning before interests & taxes
EBITDA	Earning before interest, taxes, depreciation & amortization
EM	Emerging Market
EPS	Earning per share
EY	Earning Yield
FDI	Foreign Direct Investment
FIPI	Foreign Investor Portfolio Investment
FM	Frontier Market
FO	Furnace Oil
FMCG	Fast Moving Consumer Goods
FSV	Forced Sale Value
FX/Forex	Foreign Exchange
FY	Fiscal Year
GDC	Gas Distribution Companies
G2P	Government to Person
GDP	Gross Domestic Product
GDS	Gas Development Surcharge
GENCO	Generation Companies
GM	Gross Margin
GoP	Government of Pakistan
GRM	Gross Refinery Margin
HOBC	High Octane Blended Component
HoH	Half on Half
HSD	High Speed Diesel
IDR	Investment to Deposit Ratio
IFEM	Inland Freight Equalization Margin
IFI	International Financial Institutions
IMF	International Monetary Fund
IPI	Iran-Pakistan-India
IPP	Independent Power Producer
IPS	Investor Portfolio Securities
JUI	Jamiat Ulema Islam
Kero	Kerosene Oil
KIBOR	Karachi Interbank Offered Rate
KPD	Kunnar Pasaki Deep
KSE	Karachi Stock Exchange
LDO	Light Diesel Oil
LIBOR	London Interbank Offered Rate
LIPI	Local Investor Portfolio Investment
LPG	Liquified Petroleum Gas
LSM	Large Scale Manufacturing
LTE	Long Term Evolution
M&A	Merger & Acquisition
MCR	Minimum Capital Requirement
MEG	Ethylene Glycole
MFN	Most Favoured Nation
MMCFD	Millions of cubic feet per day
MN	Million
MOGAS	Motor Gasoline
MoU	Memorandum of Understanding
MPS	Monetary Policy Statement
MQM	Muttahida Quami Movement
MSCI	Morgan Stanley Composite Index
MT	Metric Ton
MTS	Margin Trading System
MS	Motor Spirit
MW	Mega Watt
NDA	Net Domestic Assets
NFA	Net Foreign Assets
NFC	National Finance Commission
NII	Net Interest Income
NPL	Non Performing Loan
NSS	National Saving Scheme
NTB	Non-Tarriff Barriers
OCAC	Oil Companies Advisory Committee
OGRA	Oil and Gas Regulatory Authority
OMC	Oil Marketing Company
PAT	Profit After Tax
PB	Price to Book
PCF	Price to Cash Flow
PEG	Price Earning to Growth
PEPCO	Pakistan Electric Power Company
PER	Price to Earning Ratio
PIB	Pakistan Investment Bond
PKR	Pakistan Rupees
PL	Petrroleum Levy
PML	Pakistan Muslim League
POL	Petroleum Oil Lubricants
PP	Petroleum Policy
PPIB	Private Power Infrastructure Board
PPIS	Pakistan Petroleum Information Service
PPP	Pakistan People Party
PPS	Percentage Points
PSDP	Public Sector Development Program
PSF	Polyester Staple Fibre
PTA	Purified Terephtalic Acid
QoQ	Quarter on Quarter
RGST	Reformed General Sales Tax
ROA	Return on Assets
RDF	Refused Derive Fuel
ROE	Return on Equity
RPPs	Rental Power Projects
SBA	Standby Agreement
SBP	State Bank of Pakistan
SCRA	Special Convertible Rupee Account
SECP	Securities Exchange Commission of Pakistan
SLR	Statuary Liquidity Requirement
SME	Small Medium Enterprises
SR	Sharpe Ratio
STA	Single Treasury Account
TBILL	Treasury Bill
TDF	Tyre Derived Fuel
TI	Transparency International
USD	United States Dollar
WAPDA	Water and Power Development Authority
WHR	Waste Heat Recovery
WTI	West Texas Intermediaries
YoY	Year on Year
YTD	Year to date

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NOTE: All data have been extracted from sources including Company Reports, Bloomberg, MoF, SBP, FBR, KSE, Bloomberg, FBS, OGRA, PPIS, OCAC, ICT, NFDC, APCMA, APTMA, PEPCO, NEPRA and InvestCap Research Estimates