Pakistan Equity Outlook 2020

Thursday, 16 January 2020

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Market to Cherish Economic Recovery

Starting 2019, we saw a material slowdown in Pakistan economy. Much of this weakness reflected hard-hitting contractionary and reform measures that the government attempted to fix past governments' growth blend and rein in systemic risks in the economy.

We expect economy to stabilize in 2020

While the effects of these contractionary measures will continue to show-up till 2020, we expect Pakistan economy to stabilize in 2021. This should be underpinned by a combination of easing monetary conditions, supportive fiscal policy through the government's tax and spending policies and bottoming out of industrial activity. In fact, a number of economic indicators we point highlight a shift towards stabilization.

Additionally, the present government is putting a greater emphasis on overseeing longer-term risks in the economy by bringing in series of stimulus reforms particularly targeting fiscal and energy sector. Progress on these reforms will be crucial, which alongside improved law & order situation and continuation of investment cycle with the start of CPEC phase II will frame a key setting for a sustainable growth trend.

What will drive economic growth?

However, we opine some additional easing will be needed to support economic growth over the next 12-months given the challenging domestic economy and external environment. Hence, we view starting 2hFy20, SBP and the government's combined pro-active efforts in absence of inflationary pressure will allow for lower interest rates which will stimulate overall credit growth.

Fiscal side has been a weak point and resultantly economy will have to deal with reduced development budget this year around. However, disbursement on development budget has been strong so far and with the government opting for a pro-growth approach in 2hFy20 along with international funding, we may see some pick-up in infrastructure spending. Similarly, with IMF backing fiscal discipline is likely to come in play, therefore we think government can fund more infrastructure investments in 2020-onwards. However, this outcome can become less certain, as major drags could appear from Pakistan's precarious geopolitical situation with its neighboring country India and delicate relations with the US.

Valuations are below average and earnings look set to pick up

For year 2020, we estimate earnings growth of our coverage companies (~65% of the KSE 100 market capitalization) to post a +11% y/y growth to EPS of PKR 13.6 compared to PKR 12.2 & 10.9 in 2019 and 2018 respectively. In terms of 3-yrs forward outlook, we expect a ~8.1% cagr which is relatively in-line with trailing 3-yrs cagr of ~8.9%.

Market P/E multiple has already re-rated nearly ~49% since Aug-19 to stand at 7.6x and trades at forward 2020 P/E of 6.8x, which is still below its historic mean of 8.6x. With valuations for the overall market slightly below their long term average and economy exhibiting signs of stabilization, we may continue to see liquidity support from local and foreign institutions.

Targeting index level of 50,000

By December 2020, we eye index target of 50,000, generating a total return of ~23% from its current index level of 42.5k. We have taken a market P/E multiple approach as our basis for index estimation. Based on our index target of 50,000, market would trade at a forward P/E of 8.6x which is in-line with its historic average.

Where are the opportunities in equity market?

Against this backdrop, we are adopting a balanced approach, with 'growth at a reasonable price' and 'high dividend yielders' as our investment theme. We remain focused on banks, energy, materials and industrials which we believe will benefit from Pakistan's medium term growth story.

Accordingly, our top picks sector wise are:

Exhibit: Preferred picks

Sym	Current Price	Target Price	Upside	P/E	D/Y	P/B	3yr - EPS CAGR	3yr - Fwd. ROE
KOHC	76	154	102%	16.5	1.3%	0.8	9%	9%
HUBC	103	139	35%	5.4	5.8%	1.9	50%	40%
INDU	1,050	1,403	34%	12.3	5.4%	1.8	-10%	18%
PPL	149	197	32%	6.6	2.7%	1.1	2%	17%
FCCL	17	22	30%	14.6	5.8%	1.2	-2%	9%
MARI	1,370	1,775	30%	5.8	0.5%	1.9	10%	31%
EPCL	35	45	28%	7.4	4.2%	1.4	2%	18%
ISL	57	72	26%	15.8	2.6%	1.9	18%	20%
OGDC	154	191	24%	5.6	7.1%	1.0	-3%	16%
HBL	169	205	21%	6.9	8.1%	1.1	55%	18%
PSO	215	257	20%	7.7	4.7%	0.8	18%	11%
EFERT	75	80	7%	5.4	17.3%	2.1	7%	39%
FFC	103	110	7%	7.5	10.7%	3.5	1%	45%

Contents

2019: Starting On a Weak Macro Footing

A Weak Growth Mix

For over a decade Pakistan's economy has been trapped in a growth mix which can aptly be termed as 'weak growth' mix, driven by high domestic demand with a declining private investment as a percentage of GDP.

Higher domestic demand has been supported by lax fiscal policies with less emphasis on broadening tax net and limited focus on curbing non-productive expenditures. Given less resources at hand, governments' historically have resorted to borrowing, both internally and externally, which led to a high debt pile-up. The impacts of such growth mix have repeatedly surfaced in the form of a) high inflation which in turn led to elevated cost of capital and tighter interbank liquidity, b) discouraged domestic investments and c) high current account deficit. This created what seemed like an almost repetitive loop at the time, where debt continued to pile up and started to weigh on economic growth.

Hence there were no economic surprises, with growth hitting a five-year low in Fy19 and expected to further dip to 2.7% in Fy20. This was followed by a string of disappointing macroeconomic data led by high debt levels, widening C/a deficit, low reserves and rising inflation.

Exhibit: Pakistan aggregate demand and fiscal record

For over a decade Pakistan's economy has been trapped in a growth mix which can aptly be termed as a 'weak growth' mix.

%age of GDP	2019	2018	2017	2016	2015	2014	2013	2012	2011	2010	2009
Private Cons.	77.1%	78.3%	77.7%	75.4%	75.2%	76.7%	76.8%	78.4%	77.7%	76.8%	77.2%
Consumption	89.0%	89.4%	88.4%	86.1%	85.5%	86.9%	87.3%	88.4%	87.0%	86.7%	87.4%
Private Invest.	9.2%	9.8%	9.5%	9.7%	9.8%	9.3%	9.4%	9.3%	8.9%	10.1%	11.4%
Investment	13.0%	14.4%	13.8%	13.3%	13.3%	12.3%	12.7%	12.8%	12.0%	13.7%	15.5%
Govt. Spending	7.6%	6.6%	6.7%	7.3%	7.3%	6.9%	6.5%	6.4%	5.8%	5.2%	4.1%
Net Imports	-9.6%	-10.4%	-8.9%	-6.6%	-6.1%	-6.1%	-6.4%	-7.6%	-4.8%	-5.6%	-7.1%
Aggregate Demand	13%	8%	9%	6%	9%	13%	12%	10%	24%	14%	25%
Direct Tax Revenue	3.7%	4.5%	4.2%	4.0%	3.8%	3.5%	3.2%	3.5%	3.3%	3.6%	3.4%
Current Expenditure (ex. Int.)	13.0%	12.7%	12.1%	11.6%	11.4%	11.2%	11.7%	10.8%	12.2%	11.9%	10.7%
Development	3.2%	4.7%	5.3%	4.4%	4.2%	4.9%	5.0%	3.6%	2.8%	4.5%	3.5%
Fiscal Deficit	8.9%	6.6%	5.8%	4.6%	5.3%	5.5%	8.0%	6.6%	6.6%	7.3%	5.2%
Primary Deficit	3.5%	2.2%	1.6%	0.3%	0.6%	0.9%	3.7%	2.3%	2.7%	2.9%	0.3%
Public Debt	84.8%	72.5%	67.2%	66.5%	63.5%	63.0%	62.4%	61.5%	59.6%	61.4%	59.0%
Interest Payment	5.4%	4.4%	4.2%	4.3%	4.8%	4.5%	4.3%	4.3%	3.9%	4.4%	4.9%
Domestic Borrowing	7.9%	4.3%	4.2%	3.3%	4.6%	3.5%	8.0%	6.0%	6.0%	5.0%	4.0%

Fixing the Growth Mix

Breaking free from this growth mix is challenging, given complicated and unwelcoming political and economic consequences. However, the current government's economic team has promised to break the decades old persistent weak growth mix which has so far kept macro stability risks alive. Since taking the office, the government of Pakistan Tehreek-e-Insaaf (PTI), led by Prime Minister Imran Khan has undertaken a set of refined and stringent structural reforms, albeit backed by International Monetary Fund (IMF).

Pessimism plenty: fixation measures had a hard-landing on overall economy

The earliest of these fixation measures include adopting a macroeconomic policy framework that is slew towards contracting both fiscal and monetary policy, with a foremost objective to a) curb overall aggregate demand, b) anchor down inflationary pressure and c) build-up FX reserves enough to buffer out potential external balances emergency.

By pulling these levers, the economy moved into a contractionary phase. Interest rates have been tightened-up close to a decade high level (+675bps increase since Jun-2018), development budget along with non-development expenditure has been cut-down, while tax revenue targets have been pumped up and currency has been let loose to be determined by market demand-supply mechanism (PKR depreciated by nearly ~30% from PKR/USD 120).

Exhibit: Pakistan currency against major currencies

2018 stands out amongst the rest, in terms of the worst year for PKR. (PKR against an equal basket of USD, GBP, EUR, CNY, JPY)

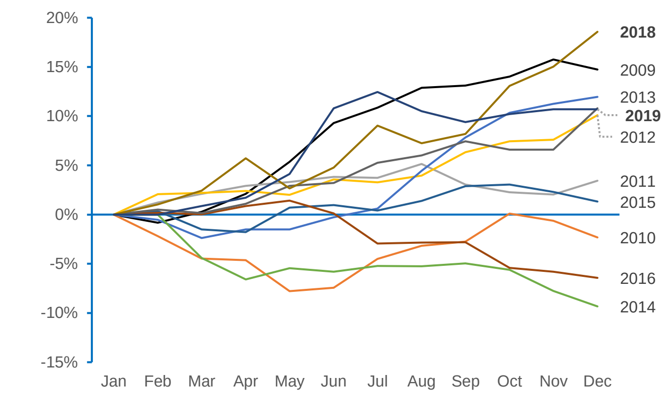
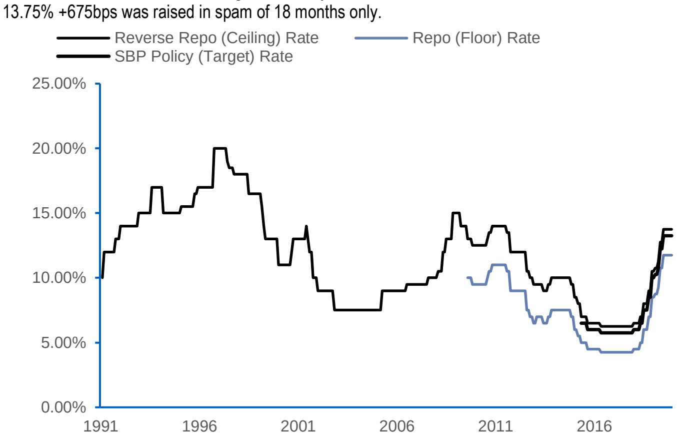


Exhibit: Pakistan Interest History

Interest rates reached a decade high 13.75% by Dec-19 a level last seen in 2011. Out of this 13.75% +675bps was raised in spam of 18 months only.



This was followed by a series of administrative energy price hikes which combined with weaker exchange rate led to one of the worst forms of cost-push inflation and a drastic reduction in overall demand. Consequently, the effects of which have started to surface with both agricultural and manufacturing output expected to register negative growth in Fy20. GDP growth is now expected to slow down and is projected to further dip to 2.4% (as per IMF) in Fy20, slowest growth in almost a decade.

Exhibit: Pakistan Food and Core Inflation

Wholesale Price Index (WPI - a proxy index for imported inflation), touched a high of +21.7% in Fy19 on average. This year however, it was more about Food Prices depicted by SPI index (proxy index for food inflation).

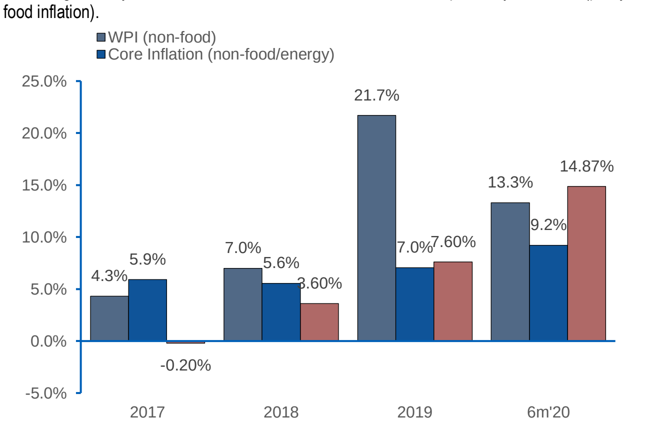
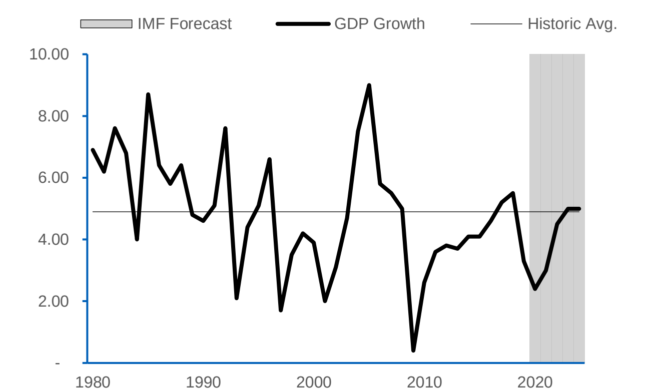


Exhibit: GDP Growth

IMF Projects Pakistan GDP growth to reach ~5% by 2024 close to its historic average; for 2020 IMF see 2.4% growth



2020: Economy showing signs of Early-cycle

Early Signs of Stabilization: While the economy is still adjusting to reforms and industrial / business activity still remain anemic, we view the economy has started to witness a shift towards stabilization with early signs showing up at the end of the year.

Generally, this form of recovery from a contractionary phase is marked by an inflection from negative to positive growth in economic activity and then eventually begins to gather steam. Monetary policy becomes less stringent, credit growth picks up speed, leading to higher sales growth and thus improve business margins and profitability.

We think starting 2020, SBP and the government's combined pro-active efforts in absence of inflationary pressure will allow for,

- ✓ **Lower interest rates –** Inflation will ease-off after a gradual uptick in 1q 2020 later allowing for easing monetary policy, implying real and nominal yields will continue to drop, stimulating overall liquidity and credit growth
- ✓ **Reforms –** A broad basket of reforms undertaken albeit under the watchful eye of IMF will ensure, growth output trend stays on-track.

10 Economic Indicators hinting to a Growth Up-cycle

1 #	External Balance	Risk of external balance considerably reduced
2 #	Exchange rate	Adjustments in exchange rate has been key in supporting exports
3 #	Large Scale Manufacturing	Large-scale manufacturing growth trend has bottomed-out
4 #	Inflation	CPI to trend lower from Mar-20 onwards
5 #	Monetary Policy	Subsiding inflation and external account risks should prompt rate cuts
6 #	IMF	Ensuring reforms stays on track
7 #	Fiscal	Consolidation finally shaping up
8 #	Liquidity	Fiscal prudence should help private sector crowding-in
9 #	Bond Yield	Drop in yield advocates subsiding economic headwinds
10 #	Consumer Confidence Index	Consumer more confident of economy than ever before

1# C/a Balance: Risk of external balance considerably reduced

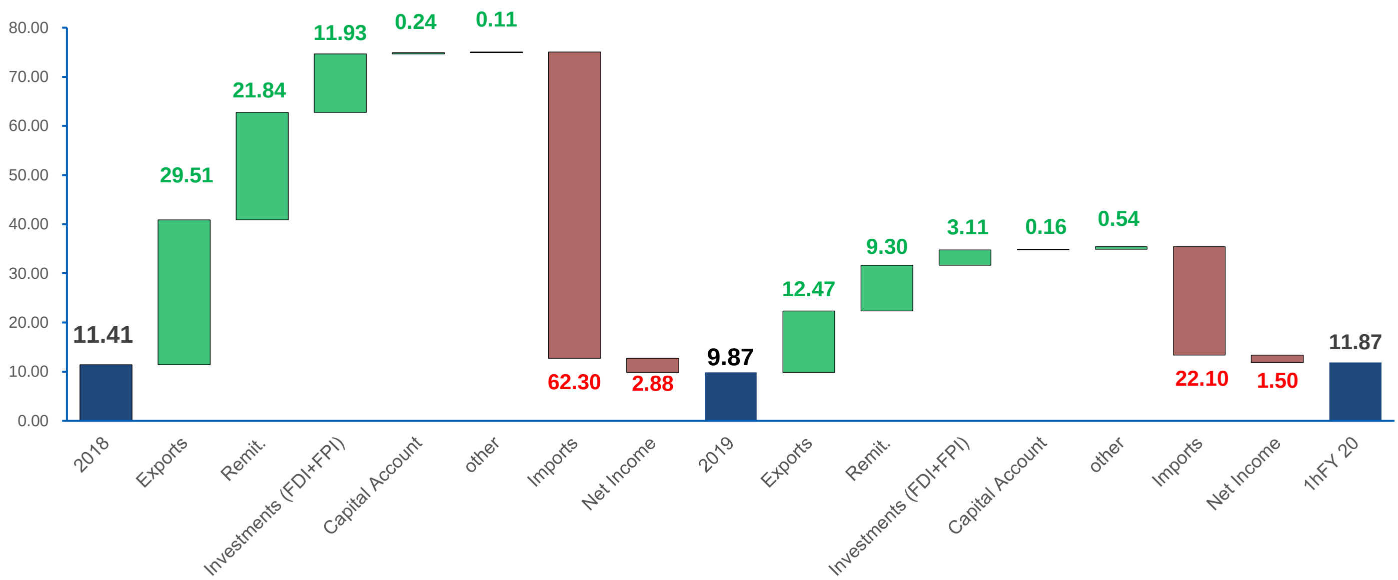
Starting off with C/a deficit which rose to USD ~20bn (6.0% of GDP) in 2018 and in 2019 came down to USD ~14bn (4.6% of the GDP). However, given the FX reserve size of USD 14bn problems became eminent. To cut the menace, the policymakers put up stringent policies (focusing more on curtailing non-essential import items) during Fy19 which to an extent helped eased trade deficit by ~10%y/y to USD 28.5bn.

Exhibit: Key highlights of C/a Balance and external balance for the month of Nov-19

USDbn	Nov/2019	5m/20	5m/19	2019	4q/19	3q/19	2q/19	1q/19	2018	2017	2016
Export	2.1	10.3	9.9	24.3	6.2	6.2	6.0	5.9	24.8	22.0	22.0
Import	3.6	18.3	23.2	52.8	12.7	12.0	13.8	14.3	56.6	48.7	41.3
Import Cover (mths)	4.4	4.4	3.0	3.6	3.5	2.8	4.0	3.8	3.5	2.3	1.8
Import / Export Ratio	1.7	1.8	2.4	2.2	2.0	1.9	2.3	2.4	2.3	2.2	1.9
Trade Balance	**(1.5)**	**(8.0)**	**(13.4)**	**(28.5)**	**(6.5)**	**(5.9)**	**(7.8)**	**(8.4)**	**(31.8)**	**(26.7)**	**(19.3)**
Trade Cover (mths)	10.4	10.0	5.2	6.1	6.7	8.9	5.3	5.3	6.2	9.6	14.4
Services Balance	**(0.3)**	**(1.6)**	**(1.7)**	**(4.3)**	**(1.4)**	**(0.7)**	**(1.1)**	**(1.1)**	**(6.1)**	**(4.3)**	**(3.4)**
Income Balance	**1.5**	**7.8**	**8.4**	**19.0**	**4.7**	**4.5**	**4.6**	**5.2**	**18.0**	**18.4**	**17.8**
Remittances	1.9	10.3	10.5	24.7	6.5	5.7	6.1	6.3	23.5	23.4	23.2
C/a Bal.	**(0.3)**	**(1.8)**	**(6.7)**	**(13.8)**	**(3.2)**	**(2.1)**	**(4.3)**	**(4.3)**	**(19.9)**	**(12.6)**	**(4.9)**
%age of GDP	-1.4%	-1.6%	-5.7%	-4.6%	-4.5%	-2.9%	-6.1%	-6.0%	-6.0%	-3.9%	-1.6%
Cap. /a Bal.	**0.01**	**0.16**	**0.13**	**0.24**	**0.07**	**0.02**	**0.05**	**0.11**	**0.38**	**0.38**	**0.27**
Fin. /a Bal.	**(0.98)**	**(1.38)**	**(0.20)**	**(0.20)**	**(0.20)**	**(0.20)**	**(0.20)**	**(0.20)**	**(0.20)**	**(0.20)**	**(0.20)**
FDI	0.20	0.80	0.50	1.70	0.50	0.40	0.20	0.60	3.50	2.70	2.30
PI	0.70	1.20	(0.30)	(1.40)	(1.00)	-	(0.20)	(0.20)	2.20	(0.30)	(0.30)
Inflow	5.70	26.50	27.20	67.00	14.60	19.20	16.70	16.40	69.40	63.70	58.60
Outflow	5.00	25.10	29.10	68.70	17.40	15.90	17.70	17.70	74.60	65.80	56.40
Net Flow	0.70	1.50	(1.90)	(1.70)	(2.80)	3.40	(1.00)	(1.30)	(5.20)	(2.00)	2.20
Balance of Payment	**0.68**	**2.08**	**(1.90)**	**(1.54)**	**(2.88)**	**3.36**	**(1.20)**	**(0.82)**	**(6.14)**	**(1.95)**	**2.65**
Fx Reserve	16.00	16.00	14.00	14.50	14.50	17.40	13.80	14.90	16.40	21.40	23.10

Exhibit: Pakistan Current Account Balance and SBP FX reserve positon

Marked improvement in 1h Fy20 as exports picked up and imports growth remained relatively shallow. As a result, SBP FX reserves in 1h Fy20 reached USD 11.9bn from USD 9.9bn in 2019



Entering Fy20, in continuation of 2019 policies the C/a deficit showed a sharp deceleration with 5mFy20 total deficit recorded USD 1.8bn compared to USD 6.7bn (~73%y/y decline). Trade cover improved to 10-months as imports contracted by ~21% y/y along with a modest +5%y/y increase in exports (led by textiles and food).

Moreover, improvement in C/a balance along with foreign direct and portfolio investments inflows of USD 2.0bn (USD 0.15bn previous year same period) started to reflect on country's improving balance of payment (BOP) terms, which by Nov-20 turned positive to USD 2.0bn. Moreover, with disbursement from IMF and other bilateral agencies country's gross FX reserve reached USD 16.0bn, improving trade and import cover to just over 10 and 4 months.

Exhibit: Pakistan Trade Balance

Trade balance of Pakistan of Textile, POL and Food constituted nearly ~45% of the total imports and ~75% of total exports, turned positive in 5m'20, last time it was 2016

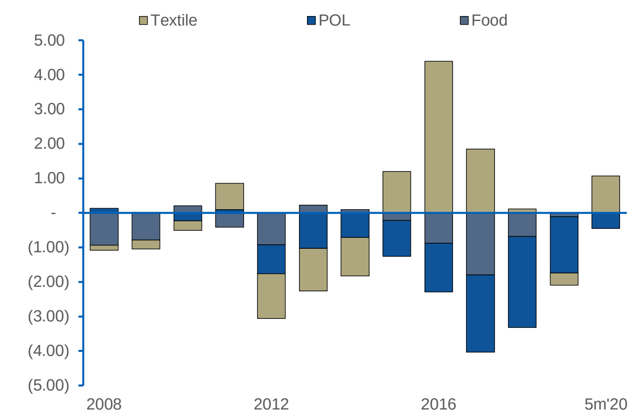
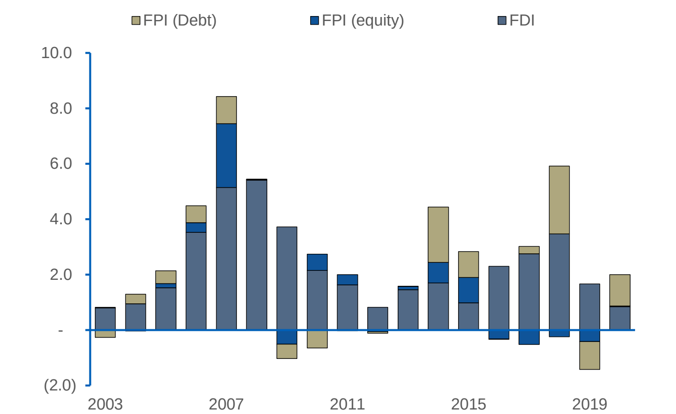


Exhibit: FDI and FPI Inflows

In 2020, Pakistan received FDI =USD 0.8bn and FPI=USD 1.2bn till Nov-2019. FDI includes one-off payment from telecom company



While Pakistan has successfully managed to avert an immediate risk of external balances, going forward we see;

Saving and investment gap to widen: Firstly, with expected rate cycle reversal in 2020 which should see real rates narrowing (Saving rates have come off by 200bps to average 11.27% in Nov-19 from 13.4% in Jul-19), we expect savings will eventually calm down and investment cycle will revive in the latter half of 2020 where we should start seeing growing current account deficit.

Imports risks: General outcome on petroleum oil price increase remains subdued as of now as weak global growth weigh, hence eliminating major risks on import bill. Moreover, Pakistan secured a USD 3.6bn deferred oil facility from Saudi which should be able to cover 1/3 of total monthly oil import fluctuations. We estimate for USD 10/bbl change in oil prices will increase country's current deficit to GDP by 0.65%.

Current Account Deficit to remain manageable under 2% of the GDP by 2020: Going forward we expect C/a deficit to narrow in Fy20 to USD 5.9bn or 2.0% of the GDP. We expect a +6% y/y growth in country's export while imports are expected to post a 3% y/y reduction. This should restrict overall trade deficit to USD 25.5bn compared to USD 28.5bn last year. Similarly, supportive remittances (remittances and exports cumulatively now accounts for ~17% of the GDP in 2020, compared to 10% last year) will also play a crucial part in keeping overall deficit restricted.

Exhibit: C/a balance forecast

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USDbn	2015	2016	2017	2018	2019	2020E	2021F	2022F
C/a Deficit	(2.8)	(4.9)	(12.6)	(19.9)	(13.8)	(5.9)	(5.4)	(5.2)
Exports	24.1	22.0	22.0	24.8	24.3	25.8	26.6	27.5
Imports	41.4	41.3	48.7	56.6	52.8	51.4	52.5	54.0
Trade Balance	(17.3)	(19.3)	(26.7)	(31.8)	(28.5)	(25.5)	(25.8)	(26.5)
C/a Balance (%age GDP)	-1.0%	-1.6%	-3.9%	-6.0%	-4.6%	-2.0%	-1.7%	-1.5%

2# Exchange rate: Adjustments in exchange rate has been key in supporting exports sector growth

Improvement in country's balance of payment has reduced foreign payment pressure in the interbank, causing PKR to appreciate against USD in by ~7% from its high of 165 in Jul-19 to current 155.

So far in 2020 exchange rate policy has been supportive of exports growth, effectively pumping up exports to reach USD ~10bn (up by +5% y/y in 5mFy20). Quantity wise major exports items witnessed significant growth. However, low commodity prices internationally have meant reduced export receipts, such as in textile and POL exports. In 2hFy20, government of Pakistan is off the view to further incentivize export sectors, including concessionary financing rates, rebates, subsidized power and energy tariff, which combined with competitive exchange rate policy should see exports volume staying afloat.

Exhibit: Textile Sector Export

	Non-value added Textile Goods							Value added Textile Goods								
	Raw	Yarn	Cloth	Combed	Other	USD/unit	qty	Knitwear	Bed	Towels	Canvas	Readymade	Synthetic	USD/Unit	qty	USD/unit
2013	1.66	3.05	1.24	1.40	3.29	**1.71**	251	20.9	6.8	4.5	3.6	66.5	1.2	**7.46**	77	**3.06**
2014	1.79	3.00	1.18	1.27	3.37	**1.59**	262	19.4	6.8	4.5	2.9	66.0	1.3	**7.91**	80	**3.07**
2015	1.56	2.88	1.18	1.14	3.03	**1.59**	236	23.2	6.5	4.6	2.8	67.8	1.2	**8.33**	79	**3.27**
2016	1.55	2.82	1.05	1.07	2.65	**1.37**	218	19.8	6.2	4.5	2.8	68.5	1.2	**8.26**	78	**3.19**
2017	1.71	2.73	1.04	1.05	2.70	**1.36**	212	22.7	6.0	4.1	2.9	66.0	1.2	**8.83**	75	**3.31**
2018	1.65	2.63	0.93	0.38	2.89	**1.25**	245	25.7	6.0	3.9	3.0	64.4	1.0	**8.22**	89	**3.10**
2019	1.61	2.60	0.76	0.88	2.81	**1.02**	268	23.8	5.5	4.2	2.8	50.0	0.8	**7.67**	98	**2.79**
5m'2020	1.33	2.48	0.79	0.73	2.52	**1.06**	258	25.8	4.9	4.2	2.4	44.2	0.7	**7.05**	113	**2.88**

Exhibit: Pakistan Exports

Off to a weak start

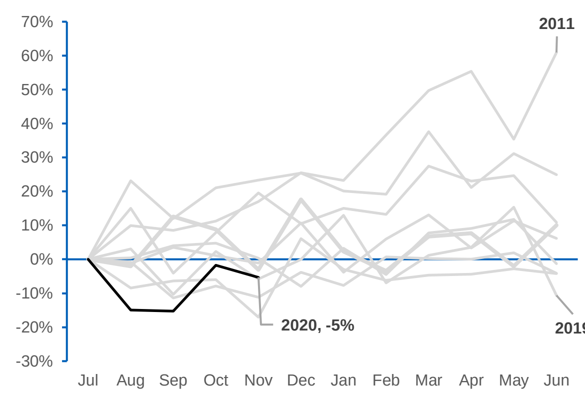
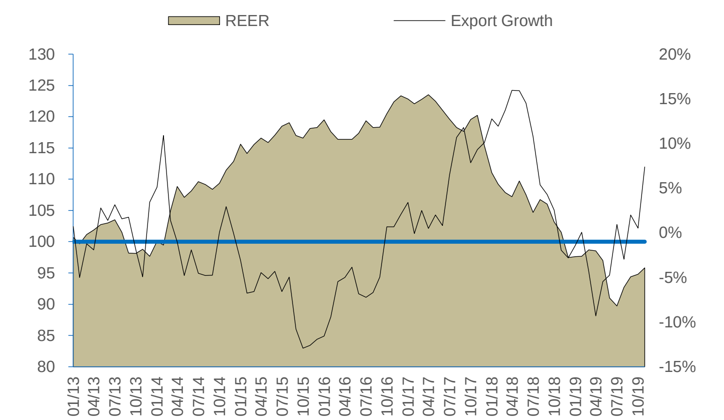


Exhibit: Pakistan REER and Exports

By Nov-20, Pakistan REER adjusted to 95.8 from a high of 120 back in Nov-17, which have been supportive of exports competitiveness. Looking ahead, we view changes in REER weightages (changes in China and US weights), will allow for even a lower REER index by about ~25%.



Expecting a stable USD/PKR Parity in 2020: Since Pakistan has moved into a market-driven exchange rate regime, PKR has exhibited stability. We target 3-4% of further depreciation in 2020 to 164 (Dec20) against USD. However, we could see PKR could come under pressure once SBP starts to cut rate, but this will be more than offset by;

- ✓ Higher available funding of USD 29bn – As per IMF accounts, Pakistan will have a higher funds availability in 2020, including FDI of 2.2bn, disbursements of USD 26bn and other. Moreover, total financing requirement in 2020 comes at 27bn with only USD 20bn of loan repayment. This comes out of net financing surplus of Pakistan at USD 1.6bn, including IMF EFF funding which will reach close to USD 4.0bn.

Exhibit: Pakistan total disbursement and repayments (IMF)

In USDbn	2018A	2019A	2020E	2021F	2022F	2023F	2024F
Official (non-IMF)	9.0	16.5	18.8	18.5	15.0	11.8	10.0
Project Loans	3.5	2.7	2.6	3.0	2.9	2.8	2.9
China	1.8	2.0	1.1	1.1	1.1	1.1	1.1
Programs Loan	0.3	0.0	2.9	2.0	2.4	1.8	0.0
World Bank	0.2	-	0.8	0.9	1.5	0.7	-
ADB	0.1	-	2.1	1.0	0.9	1.1	-
Private	12.1	4.3	7.1	7.2	10.9	15.1	17.0
Disbursements	**21.1**	**20.8**	**25.9**	**25.6**	**25.8**	**26.9**	**27.1**
Public debt	5.7	7.0	16.2	16.0	16.1	12.4	12.7
LT (non-IMF)	4.2	4.4	12.2	9.7	5.7	4.1	7.7
Bonds	0.1	1.0	1.0	-	1.0	1.0	1.0
Private debt	4.7	4.2	3.8	3.7	5.1	7.2	9.2
Repayments	**10.4**	**11.2**	**20.0**	**19.7**	**21.2**	**19.6**	**21.9**

- ✓ Saudi Oil facility of USD 3.6bn
- ✓ Recently signed FTA with China substituting CNY as trade currency as against USD previously
- ✓ Euro and Panda bond – GoP introduced a medium-term note (MTN) program to float Eurobonds and international Sukuk for a period of one year with an estimated size of USD3.0bn and USD 1.0bn issuance of Panda-Bond in 1q/Fy20
- ✓ FDI and FPI - Pakistan has been able to attract foreign inflows both in the form of portfolio and direct, which along with reduced forward FX liabilities have helped build-up FX reserves, causing some stability to PKR. Steady PKR has also induced de-dollarization in the economy depicted by reduced foreign currency deposits.
- ✓ Changes in REER basket – Changes in REER basket weightages to potentially ward-off a sharp 'overvaluation' situation and keep Pakistan currency competitive.

Exhibit: Pakistan Gross Reserve Additions (IMF)

In USDbn	2018A	2019A	2020E	2021F	2022F	2023F	2024F
External Financing Req.	30.4	25.4	27.3	26.7	28.1	26.7	29.7
- Of which C/a Deficit	19.9	13.8	6.6	5.9	5.9	6.0	6.8
- Of which Loan Repayments	10.4	11.2	20.0	19.7	21.2	19.6	21.9
- Of IMF	0.1	0.4	0.8	1.0	1.0	1.1	1.0
Available Financing	24.0	22.8	28.9	29.1	30.2	32.3	33.2
- Of which FDI	3.5	1.7	2.2	3.0	3.9	4.9	5.6
- Of which Disbursement	21.1	20.8	25.9	25.6	25.8	26.9	27.1
- Of which Other	(0.5)	0.4	0.8	0.5	0.5	0.5	0.5
Net Financing Requirement	6.4	2.5	(1.6)	(2.4)	(2.1)	(5.6)	(3.5)
IMF Borrowing	-	-	2.4	1.3	1.6	0.8	-
FX Reserve Addition	(6.4)	(2.5)	4.0	3.6	3.7	6.4	3.5
Gross Reserve	9.8	7.3	11.2	14.9	20.7	27.1	30.6

3# LSM: Large-scale manufacturing growth trend has bottomed-out

On growth side, large-scale manufacturing (LSM) continues to show a declining trend with 4m Fy20, LSM index down by 6.3%y/y. This downtrend in LSM is a factor of a) high interest rates, b) realignment of the exchange rate during 2019 causing higher import input costs, and c) slowdown in demand. However, much of the aforementioned factors are expected to be addressed in 2020, which along with certain regulatory and tax relief measures suggests LSM growth trend has now bottom-out. Production of key industrial items including POL, Cements, Glass, Billets, HRC and Paper & Board, have started to show a change in trend. Similarly, recent credit data fortifies a pick-up in fixed investment credit growth.

Exhibit: Pakistan Industrial Product changing growth trend

Quantity production of main industrials products (POL, Cements, Glass, Billets, HRC Sheet, Paper & Board) started to show a change in trend from Sep-19

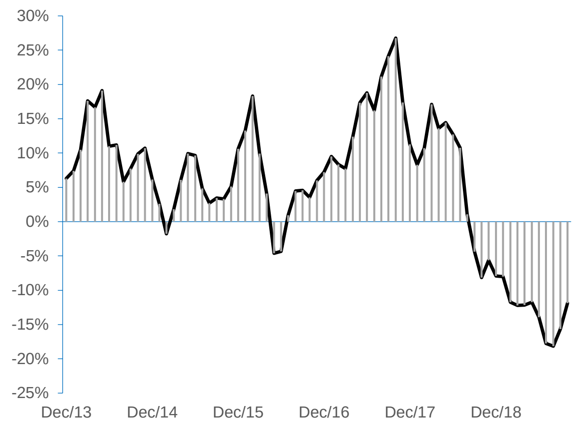
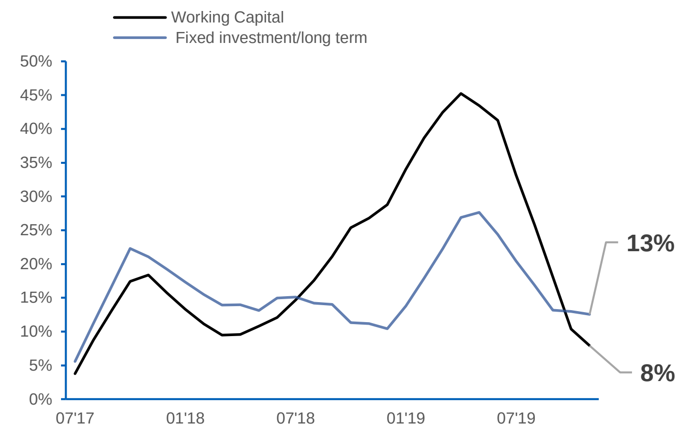


Exhibit: Credit by Type of Finance

Fixed-investment credit have increased by +13% y/y compared to 8% y/y increase in Nov-19



4# Inflation: CPI to trend lower from Mar-20 onwards

Based on new calculation methodology and re-basing index from 2008-09 to 2015-16; 1h Fy20, inflation printed a growth of +11.1% y/y (avg. monthly increase of +1.2% m/m) compared to +6.0% y/y in 2019 same period. Factors responsible for high inflation growth so far have been a) high perishable food items prices, b) administrative price hike of gas and power tariff, and c) lagged impact of high cost-push inflation due to PKR depreciation.

Inflation dynamics should be under heavy scrutiny in 2020: High m/m changes in headline inflation was largely fueled by 'temporary factors' led by food supply disruption and then partly due to second round effects of administrative price increases. We are of the view that these food prices in particularly perishable food items prices are likely to revert back going forward, as depicted by Dec-19 CPI growth (perishable food prices down 9.3% y/y). Hence, looking into 2h Fy20, we think inflationary pressure to remain rather controlled.

However, we estimate CPI inflation will continue to stay in double-digit from Jan-to-Mar 2020, but eventually ease-off and rest in single digit territory post 3q Fy20. On inflation outlook we expect headline CPI to average 10-11% compared to SBP target of 11-12% and IMF revised target of 11%. However, risks remain plentiful, such as administrative price hikes and volatility in international oil prices.

Budgetary borrowing from SBP has played a pivotal role in anchoring down inflation expectation: The government's appetite for SBP financing remained subdued compared to last year due to government committed on achieving zero quarterly borrowings from SBP to finance its deficit under the EFF program. As a result, borrowings from commercial bank increased which amid seeing monetary cycle reversal had developed a strong appetite of LT tenure sovereign paper, helping government's debt to re-profile from ST to LT.

Exhibit: Domestic Consumer Gas Prices hike

Since taking Sep-18, government has raised domestic gas prices significantly. In Jan 2020 it is expected that GoP would further hike gas prices. Break-up wise, consumption of 100m3 or below roughly accounts for 66% of the population, but so far has experienced a +28% growth in gas bill

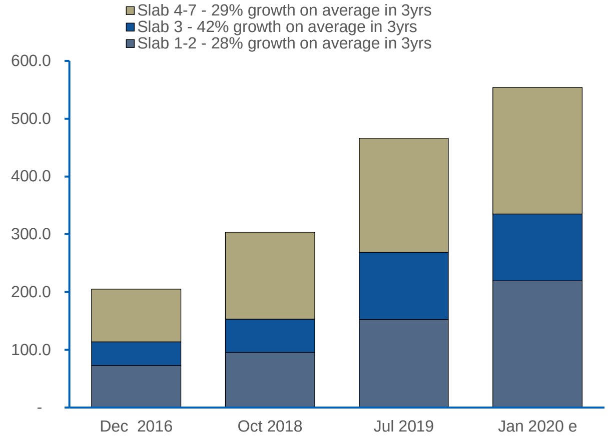
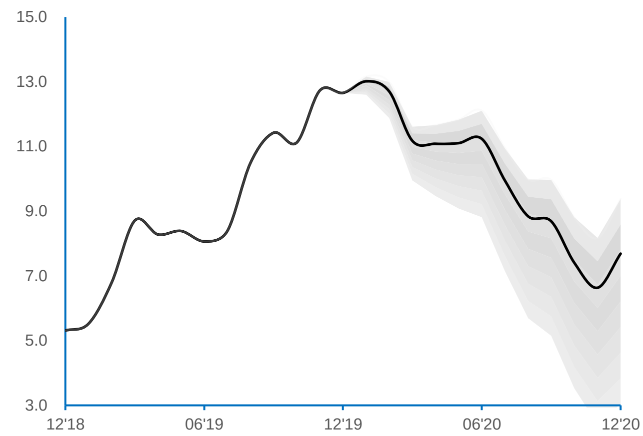


Exhibit: Pakistan headline CPI Forecast

For Fy20, average inflation is expected to remain close to SBP target of ~11%. Going forward by 2020 end, inflation is expected to float between 7-9%.



5# Monetary Policy: Subsiding inflation and external account risks should prompt rate cuts

Given improvement in external account and inflation we expect a policy rate cut by 200bps in 2020 to 11.25% from current 13.25%.

When can we see monetary rate cycle reversal? Our inflation forecast for 10-11% in Fy20 (SBP 11-12% and IMF 11%), puts our 3m forward real interest rates over >3% compared to historical average of ~2.0%. Although, SBP does not follow a stated real interest rate target regime, we see real rate will further increase in Mar-20 onwards as we expect inflation to drop close to single digit, leaving sufficient room for authorities to cut key policy rate.

GOP and SBP see pro-growth policies in 2h/Fy20: However, keeping in mind, SBP in its last monetary policy report issued in Nov-19 highlighted a closely monitoring area, the real sector. SBP expects no change in its growth outlook; 3.5% in Fy20 regardless of contracting LSM growth and views 2h Fy20 with the help of higher PSDP disbursement should allow for LSM growth to normalize. Nonetheless, this is one area of concern where we think a faster contraction in aggregate demand could potentially trigger an earlier rate cut response by SBP.

Exhibit: Interest rate Outlook
Period End=December

Year	2017A	2018A	2019A	2020F	2021F
1Q	5.75%	6.00%	10.25%	13.25%	10.75%
2Q	5.75%	6.50%	12.25%	12.75%	10.75%
3Q	5.75%	7.50%	13.25%	11.25%	10.75%
4Q	5.75%	10.00%	13.25%	11.25%	10.75%
Average	**5.75%**	**7.50%**	**12.25%**	**12.13%**	**10.75%**

Exhibit: Pakistan Real Rates

Based on our inflation forecast, 3m fwd. real rates will start to trend upward from Mar-20 onwards breaking its historic 2.0% benchmark

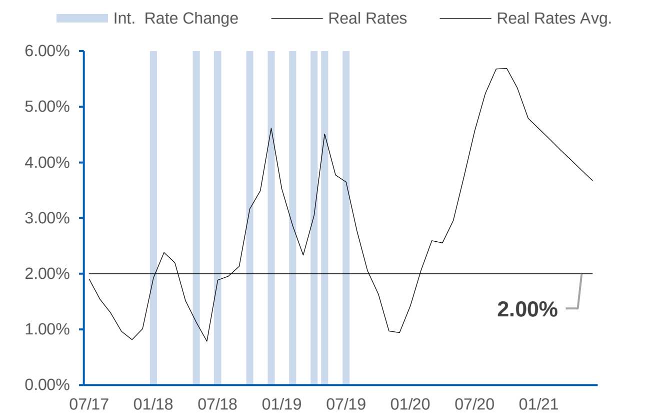
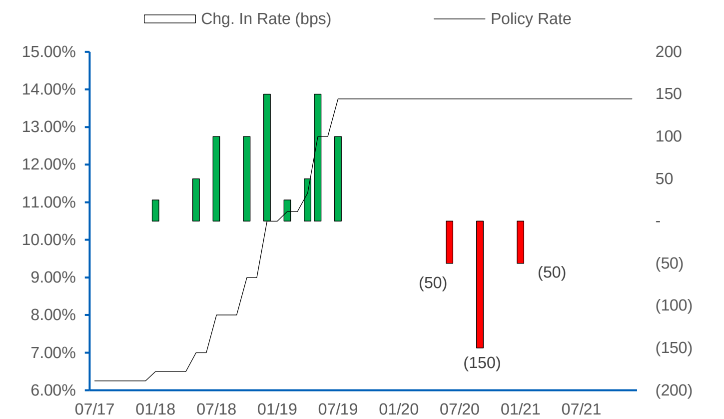


Exhibit: Policy Rate

We expect a cumulative cut of 200bps in 2020 and 50bps in 2021



6# IMF: Ensuring Growth stays on track

A key highlight during 2019 was Pakistan entering International Monetary Fund (IMF) program in July with a bailout package seeking USD 6.0bn under its Extended Fund Facility (EFF) for a period just over 3-yrs. The program aimed at restoring macro stability and reducing external/ internal imbalances. The focus was on key areas such as fiscal deficit, monetary policy, exchange rate and growth.

Exhibit: IMF program policy action

Subject	Policy Action	Comments
Fiscal Policy	A decisive fiscal consolidation to reduce public debt and build resilience	✓ Country's primary balance will be brought down to 0.6% meaning roughly equivalent to PKR 650-700bn (GDP size USD 290bn in 2020) will be needed either in the form of additional taxes (removal of tax exemption) or reduction in non-growth targeted expenditure.
Exchange rate and monetary policy	A flexible, market-determined exchange rate to restore competitiveness. & Tighter Monetary Policy	✓ The objective aims at strengthening SBP's operational independence, reduce inflation and implement market determined exchange rate. Increase in interest rates, strict Anti-Money Laundering (AML) policy and reduce borrowing from SBP along with other measures to curb external shock were suggested by IMF. ✓ To note, prior to entry in the program exchange rate was already adjusted with REER hovering close to equilibrium.
Structural Reforms	Structural reforms through strengthening institutions & Enhancing the Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT)	✓ Key amongst the structural reforms include energy sector. As per the press release by IMF, electricity and gas price tariffs will be gradually increased to bring the sector to cost-recovery. ✓ To cater better cost recovery, government has also initiated the Anti-Theft Drive to recover full cost and targets to bring down circular debt to PKR 225bn by Dec-2019. Moreover, to remove cost burden on Government's part, IMF has recommended depoliticising power and gas tariffs ✓ Structural reforms will allow for strengthening institutions and remove growth impediments, for that matter IMF has also recommended focusing on enhancing AML/CFT framework, which will later be critical for Pakistan FATF review.

Source: IMF Press Release (https://www.imf.org/en/News/Articles/2019/07/03/pr19264-pakistan-imf-executive-board-approves-39-month-eff-arrangement), IGI Research

How has been the success so far? The IMF mission to Pakistan during its first review (Oct-Nov-19), praised government efforts on program implementation while achieving major economic stability measures. The press release cited, all of end-September 2019 criteria were met with comfortable margins and progress continues towards meeting all structural benchmarks. The successful completion of the review allowed for disbursement of second tranche of USD 450mn.

From September 2019, IMF Review Report:

All end-September 2019 and continuous performance criteria (PCs) were observed. The floor on net international reserves (NIR), ceiling on net domestic assets (NDA), ceiling on SBP's stock of net foreign currency swaps/forwards, ceiling on net government budgetary borrowing from the SBP, and ceiling on the general government primary budget deficit were met by wide margins. The ceiling on government guarantees was also observed and no external public payment arrears were incurred.

Exhibit: Pakistan Schedule of reviews and disbursement

Date	Amt. USDmn (est.)	Amt. SDRmn	Conditions	Status
3-Jul-19	982	716	Approval July 2019	Received
6-Dec-19	450	328	First Review September - End	Received
6-Mar-20	450	328	Second Review December - End	
5-Jun-20	450	328	Third Review March - End	
4-Sep-20	450	328	Fourth Review June - End	
5-Mar-21	768	560	Fifth Review December - End	
3-Sep-21	768	560	Sixth Review June - End	
4-Mar-22	768	560	Seventh Review December - End	
2-Sep-22	768	560	Eighth Review June - End	
Total	**5855**	**4268**		

Exhibit: Pakistan and IMF history

SDRmn	EFF	SBA	ECF	Other	Amount Agreed	Amount Drawn	Drawn / Agreed ratio
1958-63	-	25	-	-	25	-	0%
1964-69	-	113	-	-	113	113	100%
1970-75	-	250	-	-	250	234	94%
1976-81	2,187	80	-	-	2,267	1,159	51%
1982-87	-	-	-	-	-	-	
1988-93	-	538	-	382	920	664	72%
1994-99	834	563	1,289	-	2,686	969	36%
2000-05	-	465	1,034	-	1,499	1,326	88%
2006-11	-	7,236	-	-	7,236	4,936	68%
2012-17	4,393	-	-	-	4,393	4,393	100%
2018-23	4,268	-	-	-	4,268	716	17%
Total*	11,682	9,270	2,323	382	19,389	13,794	71%

**Drawn/Agreed Ratio excludes 2019*

Exhibit: IMF Forecast on Key Macroeconomic Indicators

%age of GDP	2018A	2019A	2020E	2021F	2022F	2023F	2024F
GDP (%age)	5.5	3.3	2.4	3.0	4.5	5.0	5.0
GDP Deflator (%age)	2.4	7.5	11.8	8.3	6.0	5.0	5.0
CPI (%age average)	3.9	7.3	11.8	8.3	6.0	5.0	5.0
C/a Balance	(6.3)	(4.9)	(2.4)	(2.0)	(1.8)	(1.7)	(1.8)
C/a Balance (ex. Oil imports)	(2.1)	0.4	3.3	3.6	3.7	4.0	4.0
Gross Reserves	9.8	7.3	11.2	14.8	20.7	27.1	30.5
External Debt	30.3	37.6	41.2	40.9	40.1	38.9	36.8
Tax Revenue	12.9	11.6	13.7	15.6	16.7	17.3	17.2
Development Expenditure	4.2	2.6	3.3	3.5	3.8	3.8	3.8
Primary Fiscal Balance	(2.2)	(3.5)	(0.6)	0.9	1.9	2.6	2.6
Fiscal Deficit	(6.5)	(8.9)	(7.6)	(5.5)	(4.0)	(2.8)	(2.6)
Net General Govt. Debt	66.1	75.2	73.7	71.2	68.1	64.6	61.3

Key measures taken to boost tax in 2020

I - Increase in sales tax rates
II - Reinstatement of taxes on telecom services
III - Upward revision of tax rates on various salary slabs
IV - Increase in interest rates and higher tax on profit on debt
V- Upward revision in the federal excise duty (FED) rates
VI- Abolishment of the zero rating regime on five export-oriented

7# Fiscal: Consolidation finally shaping up

Ever since taking charge, the incumbent PTI government has focused its policies towards achievement of a sustainable economic growth. As such, the government has undertaken some stringent measures mainly achieving fiscal discipline and reforming energy and power sector.

Fiscal consolidation underway: A multiple approach for enhancing tax revenues has been adopted, with tax revenue target set at PKR 5.5trn (12.5% of the GDP, compared to historic average of 12%) this seemed rather necessary.

So far in 1q/20 fiscal details appears to have marginally achieved these targets, revenue collection has remained strong printing a +17%y/y growth to PKR 1.1trn, and tax filers have jumped up by +57%y/y (till Oct-19). Similarly, on expenditure side most of the current expenditures as of 1q/20 appears to come in-line with the budget target and more importantly country's primary deficit turned positive at 0.6% of the GDP which is one of targets set by IMF under EFF program. On the development side, although the government has reduced overall development expenditure in Fy20 (PSDP at 3.7% of GDP compared average of ~4.5% in previous years) but a consistent and improved PSDP releases are in line with the governments objective which hasn't been the case historically will eventually spur economic activity.

Exhibit: 1q/Fy20 Fiscal account snapshot
Importantly, the government did not resort to the usual practice of cutting development expenditures to achieve fiscal consolidation

%age of GDP	1q/16	1q/17	1q/18	1q/19	1q/20	Growth y/y
Total Revenue	12.2%	10.3%	11.4%	11.5%	13.5%	35%
Tax	9.4%	9.0%	10.1%	10.2%	10.4%	17%
Non-tax	2.8%	1.3%	1.3%	1.3%	3.1%	173%
Total Expenditure	**16.5%**	**15.5%**	**16.3%**	**17.1%**	**16.1%**	**8%**
Current	14.2%	12.8%	13.8%	15.4%	14.4%	7%
Interest Payments	5.4%	4.9%	5.0%	5.3%	5.2%	13%
Development	**2.2%**	**2.3%**	**2.5%**	**1.1%**	**1.3%**	**35%**
Fiscal bal.	-4.3%	-5.2%	-4.9%	-5.6%	-2.6%	-47%
Primary bal.	**1.1%**	**-0.3%**	**0.1%**	**-0.4%**	**2.6%**	**n.a.**

Key Fiscal Reforms underway:

Expediting tax refunds: Expedite clearance of the present backlog of tax refund arrears mainly includes textile Sector

Strengthening budgeting and public financial management: Fortifying treasury single account (TSA)

SOEs: Reforming state-owned enterprises & Privatization

Expenditure targets likely to be met without much compromise on development budget: Much of the expenditure contraction in 1q/20 is due to cut downs in social, defense and other public safety expenditure. However, eyeing an a) interest rate reversal, b) stable exchange rate, and c) reduced government borrowing, we think would help keep interest payment tepid in 2020. A 100bps decline in sovereign yields could shave of 0.5% of the fiscal deficit ceteris-paribus. Hence we think expenditure ex-development will likely come in line with government projections.

Meeting revenue targets would be challenging: However, this cannot be said for the revenue.1q/Fy20 revenue collection had some one-off tax inflows and reversals of concessions in previous year. Slowdown in imports has already led to a downward revision in tax revenue by PKR 317bn (0.7% of the GDP) while government continues to provide concessions and waivers to certain sectors which will make tax target achievement rather challenging.

8# Liquidity: Fiscal prudence should help private sector crowding-in

The improve fiscal position has let the SBP exercise more monetary accommodation, reflected in form of reduced government borrowing from banking sources which dropped significantly during 2019. This improvement however, was less visible in form of private sector credit 'crowding-in'. As banks deposits growth suffered due to rise in currency in circulation, hence banks opted to park their excess liquidity in government securities and in particularly longer-term paper. Going forward we expect system liquidity will remain positive, which will be impetus for credit growth. Mainly we say this on back drop of a) increase in bank deposit owing to slowdown in currency in circulation amid government increase focus on documenting economy (such as liquidation of prize bonds, reforms in real sector etc.), and b) recued government bond yields will create an appetite for private sector credit.

Exhibit: Government borrowing
Government borrowing for budgetary requirement recued significantly from commercial banks

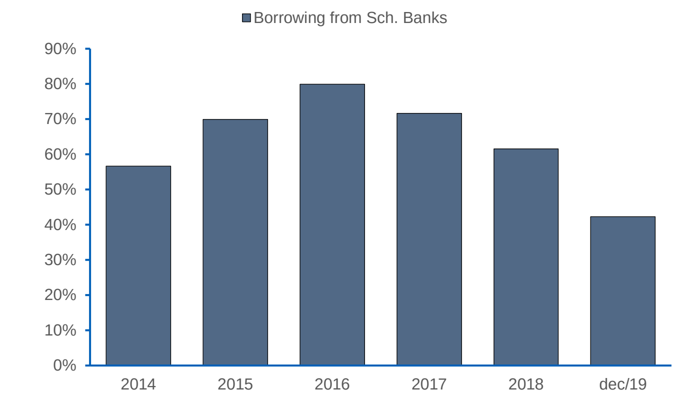
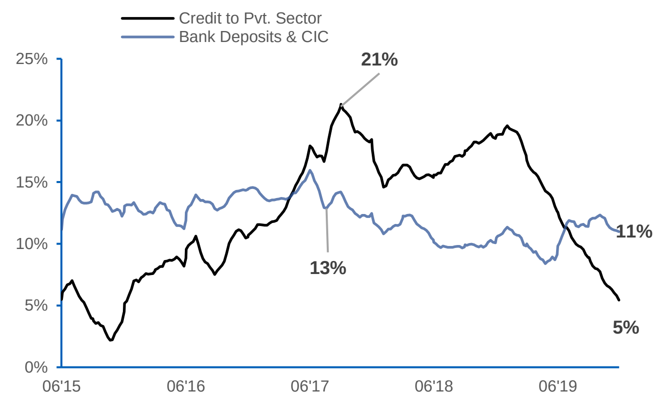


Exhibit: Bank deposits and CIC versus credit to private sector
Private credit declined owing to increase in Banks deposit and currency in circulation



9# Bond Yield: Drop in yield advocates subsiding economic headwinds

By Aug-19, bond yields fell significantly leading to sovereign bond yield curve inversion. Although curve inversion largely incorporates a forward-looking approach of low inflation, building-up expectation of future rate cuts, however this yield inversion in our view had more to do with demand and supply imbalances which led to excess liquidity with commercial banks, insurance, mutual funds and pension funds. Nevertheless, this decline in sovereign bond yields has provided support to equity valuations which was later reflected by market rally. Either case, be it improved liquidity or expectations of future interest rate cuts, drop in yield advocates easing credit conditions going forward.

Exhibit: Banks and Non-banks participation in PIB and Treasury Bills
Banks and other Corporates demand for Sovereign bond investment increased starting 2019, amid major liquidity

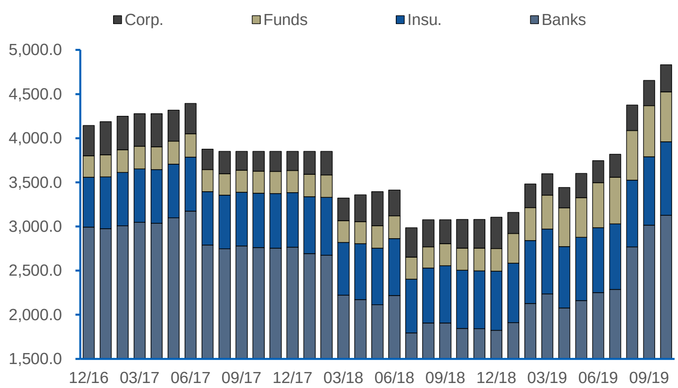
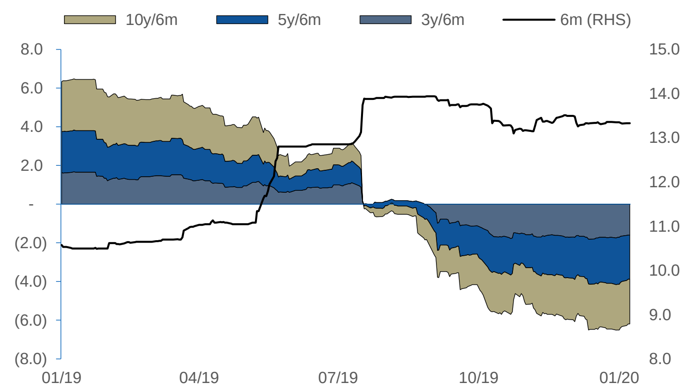


Exhibit: Bond Yield Spread
By the end of Jul-20, post IMF approval of EFF bond yield spread between 6m PKRV and longer-tenure PKRV turned negative with an average discount of ~1.5% rising to ~2.2% by Dec-19



10# Consumer Confidence Index: Consumer more confident of economic growth

SBP-IBA Consumer Confidence Survey conducted in Nov-19 have shown a significant improvement, whereby 27% respondents agree with improving economic conditions in the next 6-months, up by 23% and 20% in 2018 and 2017 survey respectively. Moreover, starting Fy20, the number of household durable purchase in the next 6-months grew stronger compared to household durable purchase that is of today.

Exhibit: Pakistan Business survey

As per Nov-19 business survey by SBP, 'General Economic conditions over next six months compared to today' 28% respondents agree to improving general economic conditions compared to a low of 8% back in 2012

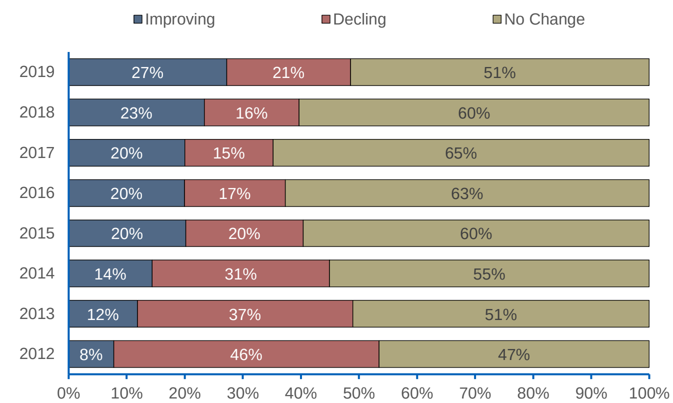
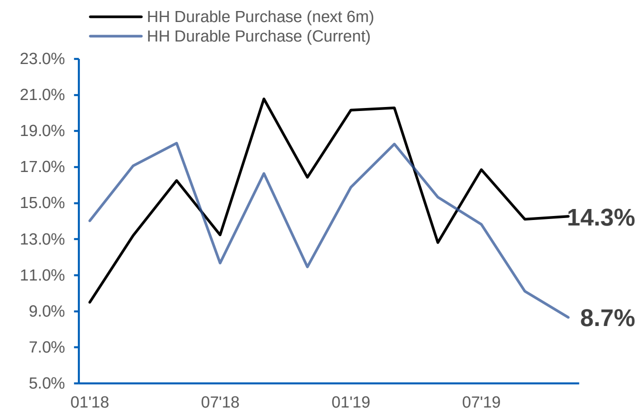


Exhibit: Household Purchase

HH durable purchase in the next 6-months is much strong than it is today.



Growth to trough in 2020

Pakistan's GDP printed a +3.3% growth in 2019 and we expect further slowdown in 2020 to +2.7%. This is lower than the estimate of State Bank of Pakistan (SBP) of 3.5% and slightly higher by IMF of 2.4%.

While major drag is expected to stem from Industrial sector, led predominantly by the large scale manufacturing (LSM), this will be further corroborated with slowdown in agricultural sector output. Major cash crops are expected to present negative growth as compared to the comparative period.

However, post 2020 we expect growth to pick-up, where lower interest rates amid reduced inflationary pressure will stimulate overall aggregate demand. Consumption has done much of the heavy lifting in terms of supporting growth this year, and we expect this trend to continue in 2021 onwards. Savings rates have come down by about 200bps during the year, but still remain at elevated levels. In terms of private investment, we could see manufacturing investment gather pace in the early phases of economic cycle, as credit conditions starts to ease for corporates and profit expectations improve. In addition, fiscal policy will remain supportive of this growth.

Moreover, out of the way facilitation of the export sectors by the incumbent government and improving business confidence of Pakistan will keep external balance situation rather stable in 2020.

Exhibit: Pakistan GDP Growth
Growth to rebound in 2021

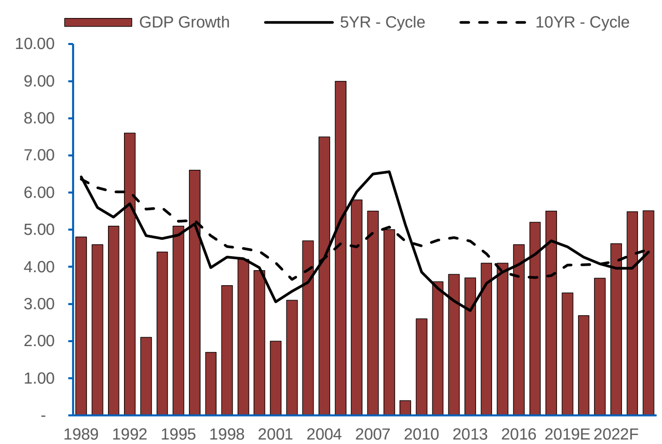


Exhibit: GDP Contribution
Service Sector will continue to dominate overall GDP

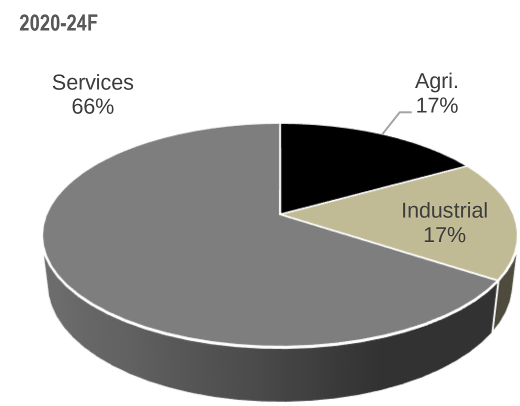


Exhibit: Key GDP growth sector wise forecast
As per IGI team estimates

		2015A	2016A	2017A	2018A	2019A	2020E	2021F	2022F
GDP Growth	%	4.1	4.6	5.2	5.5	3.3	2.7	3.7	4.6
Agricultural Sector	%	2.1	0.2	2.2	3.9	0.8	(0.5)	0.8	1.3
Industrial Sector	%	5.2	5.7	4.6	4.9	1.4	(5.0)	(3.0)	1.0
Service Sector	%	3.0	0.1	9.0	10.1	13.1	6.2	6.5	6.5
Investment to GDP	%	15.7	15.7	16.2	16.7	15.4	17.4	19.9	23.0
GDP	(PKRtrn)	27.4	29.1	31.9	34.6	38.6	42.6	47.6	53.7
GDP	(USDbn)	287.5	296.0	321.6	331.2	301.8	287.8	310.4	342.7
GDP per capita	(USD)	1,514.0	1,529.5	1,630.1	1,648.3	1,474.7	1,290.0	1,358.5	1,464.9

Market Review: A 'V-shaped' recovery in 2019

2019 was an exciting period for market. The benchmark KSE 100 index after exhibiting a lull period till Aug-19, finally gathered ground and ended on a positive note return +9%. However, regionally, KSE 100 failed to impress, which barring a few EM countries, MSCI Pakistan (+3.31% in 2019) underperformed MSCI Emerging Market (+15.42% in 2019) by 12%.

Breaking down the year in two halves, the first 8-months market tanked to a nearly 5yr low with index settling at 29k level posting a negative return of ~22% starting 2019. A string of disappointing macroeconomic data, high debt levels, widening c/a deficit, low reserves, expectations of tough budgetary tax measures and rising inflation began with interest rates hike, started to weigh on country's growth and thus corporate earnings outlook. Moreover, to top it up government prolonging IMF funding program and given edgy domestic political and cross-border situation investor activity at bay. Volumes dried up to average 133mn and market index touched a low of 5.9x P/E.

However, the pessimism was rather short-lived. Post Aug-2019, market reflected sharply to incoming positive macroeconomic data, starting with drop in long-term bond yields, reduced c/a deficit, rising exports, curbed import bills and IMF review expressing satisfaction over Pakistan's economic growth progress. As an outcome, market rallied to touch 42k index level by Dec-2019 (~44% return) along with improved market volumes averaging 259mn.

Exhibit: Market during 2019
Muddled by political and weak macro stats (Index=LHS, Volume in Mn=RHS)

Exhibit: KSE 100 annual returns

After a consecutive 2-years of negative returns 2019 finally ended on a positive note

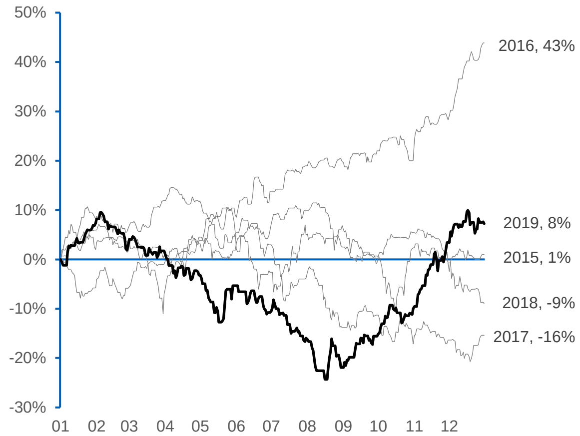


Exhibit: KSE 100 versus Regional Market Returns

KSE 100 witnessed a sharp recovery in Aug-19 compared to regional market

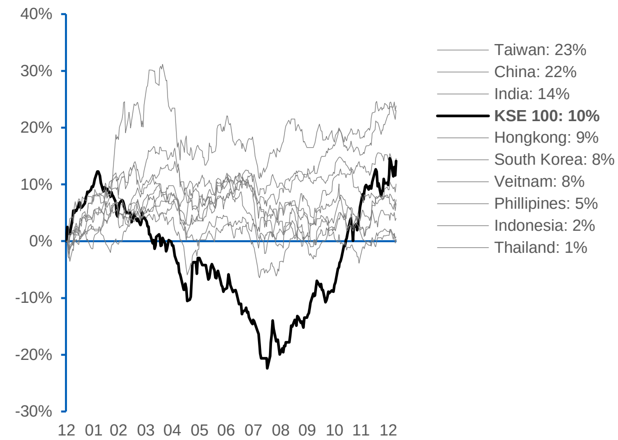


Exhibit: KSE 100 market Volumes in million

Market volumes in 2019 touch a low averaging 133mn, however in last quarter of 2019 volume recovered to a multi-year high

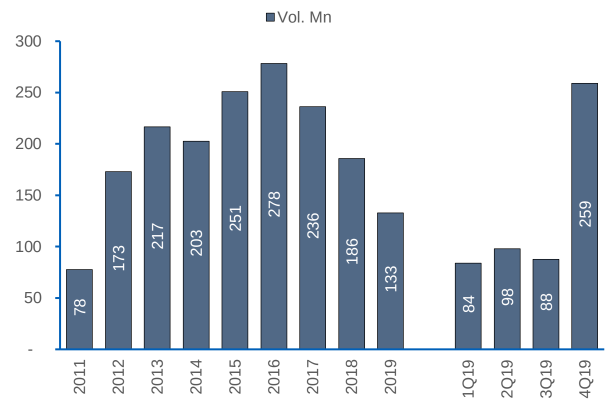
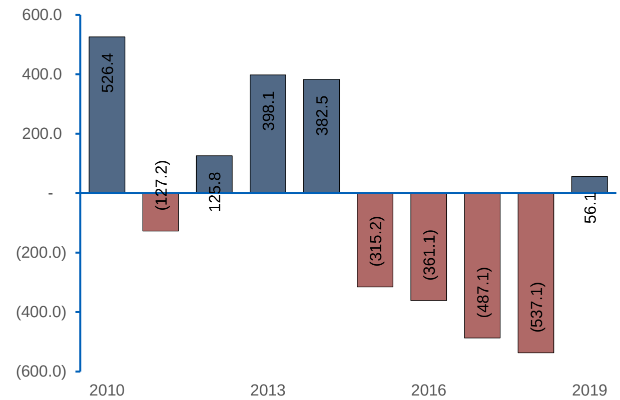


Exhibit: Foreign Investor Portfolio Investments

Foreign investments turned positive after a series of divestment experienced in past 4 years, however 2019 overall FIPI stood at net buy of USD 56.1mn



Market Outlook: Valuations are below historic average and earnings look set to pick up

We base our market outlook on stable earnings growth and P/E multiple recovery to its historic mean.

Earnings growth tapered-off 2019: Despite a host of weak macroeconomic data, corporate earnings for companies under IGI coverage (taken as a proxy for market earnings) registered a growth of +11% in 2019, to PKR 495bn or EPS of 12.2 however, slightly tapering off form last year growth of +14%.

Exhibit: 2019e Sector earnings performance

%age y/y	2019	3yr trailing Cagr
Oil & Gas Exploration Companies	46%	35%
Textile Composite	42%	12%
Commercial Banks	19%	-2%
Power Generation & Distribution	11%	5%
Fertilizer	4%	14%
Chemical	-14%	80%
Engineering	-30%	19%
Automobile Assembler	-39%	-7%
Cement	-40%	-18%
Oil & Gas Marketing Companies	-90%	-49%

Earnings contributions were limited to E&Ps, Textile and Banks: For market heavy sector, E&Ps, 2019 was yet another positive year with profitability up by +46% owing to exchange gains and high wellhead gas prices on account of PKR depreciation. With adjusting PKR, export driven textiles sector earnings showed a +42% y/y growth. For banks NIMs expansion amid favorable interest rate environment, one-off losses and earnings adjustments kept overall profitability growth limited at +19%.

Manufacturing sector earnings started to wane following compressing margins and slowing demand: Under industrial sectors fertilizer and chemicals posted positive earnings growth albeit meager, Cements and automobile assemblers registered a negative earnings growth. This was much to do with reduce demand, rising interest rates and a rapid increase in product prices.

2020 Earnings to print decent growth of +12%y/y

Market earnings to remain robust in 2020: For year 2020, we estimate earnings growth of our coverage companies (~65% of the KSE 100 market capitalization) to post a +12% y/y growth to EPS of PKR 13.6 compared to PKR 12.2 & 10.9 in 2019 and 2018 respectively. In terms of 3yr forward outlook, we expect a ~8.1% cagr which is relatively in-line with trailing 3yr cagr of ~8.9%.

Exhibit: KSE 100 Earnings outlook (based on IGI team coverage)

We expect market earnings to post a 3-yr forward ~8.3% cagr which is relatively close to what the market has achieved in past 3-yrs. (~8.8% in 2017-2019)

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Earnings Growth	26%	-5%	-10%	2%	14%	11%	12%	7%	6%	5%	6%
EPS	11.1	10.5	9.4	9.6	10.9	12.2	13.6	14.6	15.4	16.2	17.2
DPS	5.9	6.1	5.7	5.6	5.5	5.0	5.8	7.6	8.1	8.8	9.9
Payout Ratio	54%	58%	60%	59%	50%	41%	43%	52%	53%	54%	57%
P/E	8.4	8.8	9.8	9.7	8.5	7.6	6.8	6.4	6.0	5.7	5.4
D/Y	6.4%	6.5%	6.1%	6.1%	5.9%	5.4%	6.3%	8.1%	8.8%	9.5%	10.6%
P/B	1.8	1.7	1.6	1.5	1.3	1.2	1.1	1.0	0.9	0.9	0.8
P/S	1.1	1.2	1.5	1.2	1.0	1.0	0.9	1.0	0.9	0.9	0.8
ROA	13.6%	3.4%	2.7%	2.4%	2.5%	2.7%	2.7%	2.6%	2.5%	2.4%	2.3%
Lev	4.7	5.7	5.9	6.4	6.4	5.8	5.8	6.0	6.2	6.3	6.5
ROE	63.9%	19.1%	15.9%	15.0%	15.7%	15.8%	15.9%	15.8%	15.6%	15.2%	15.1%

Exhibit: Year 2020 Waterfall Chart of KSE 100 earnings contribution sector-wise
From Year 2019 to Year 2020

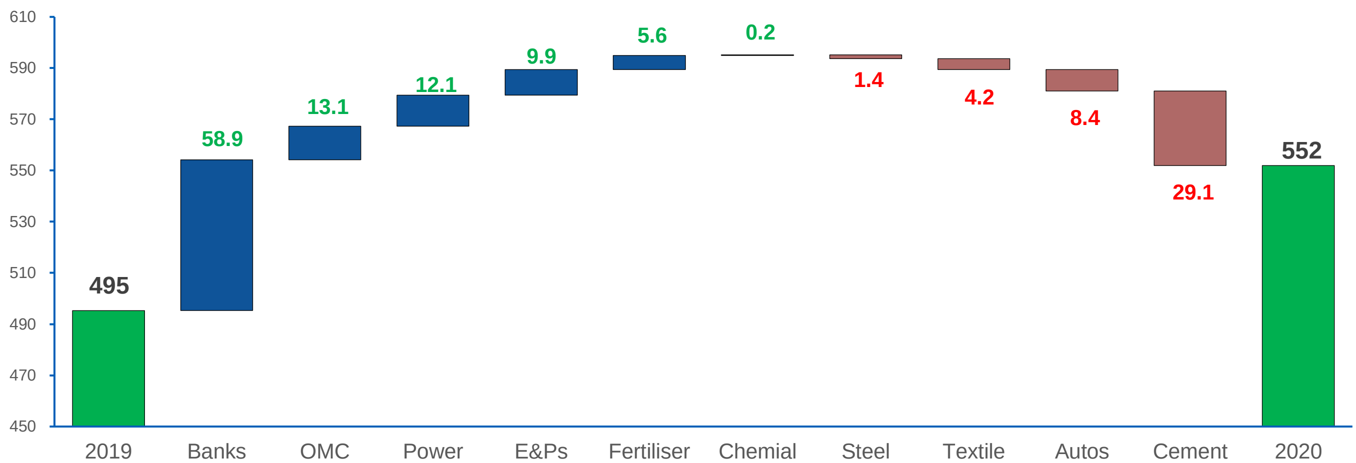


Exhibit: Year 2020 Waterfall Chart of KSE 100 earnings contribution Company-wise
From 2019 to 2020

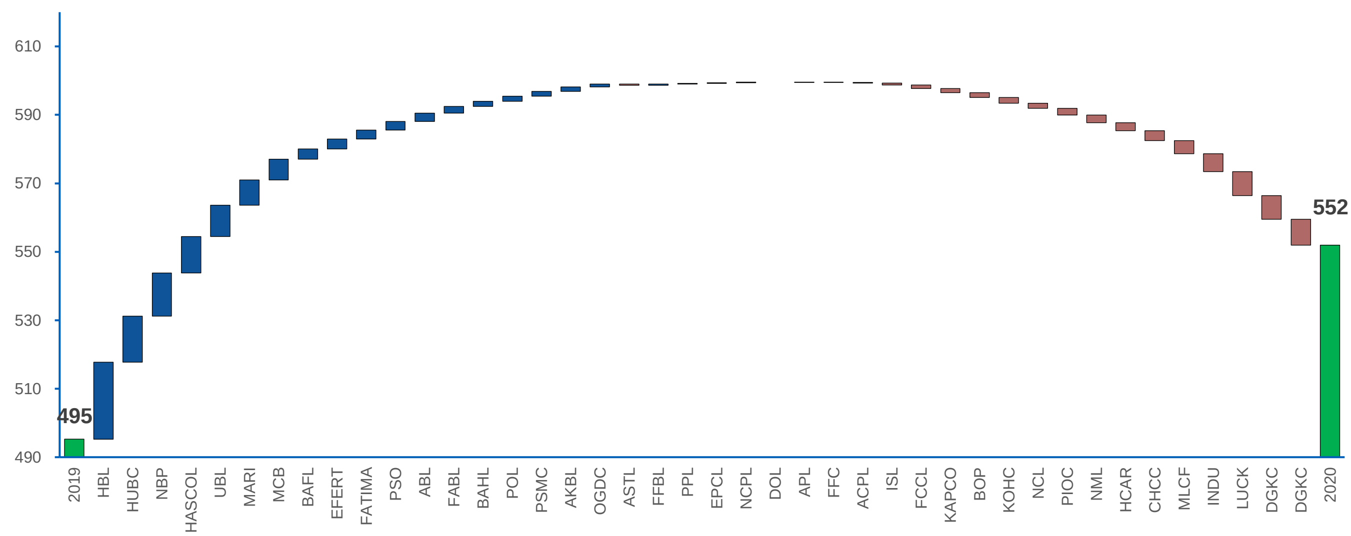


Exhibit: KSE 100 Earnings Growth Contribution (based on IGI team coverage)
Market Sector-wise contribution in percentage points

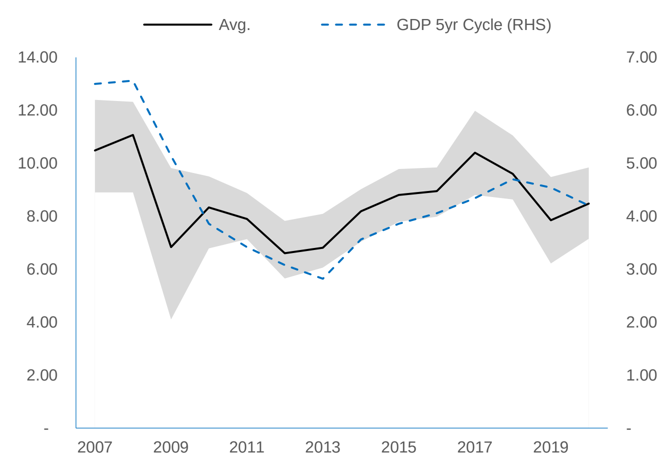
	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Market	**-4.9%**	**-10.2%**	**1.8%**	**13.5%**	**11.4%**	**11.6%**	**7.4%**	**5.9%**	**4.8%**	**6.4%**
Commercial Banks	4.6%	1.4%	-7.1%	0.8%	5.3%	15.2%	3.9%	4.3%	4.7%	6.7%
Oil & Gas Exploration Companies	-8.9%	-8.3%	9.3%	9.5%	20.7%	1.9%	-0.6%	-1.0%	-2.9%	-2.2%
Fertilizer	1.5%	-2.4%	0.4%	4.0%	0.2%	1.3%	0.4%	-0.6%	-0.5%	0.1%
Power Generation & Distribution	1.8%	-0.1%	-0.1%	0.5%	0.6%	3.2%	0.1%	-0.3%	0.6%	0.6%
Cement	1.6%	1.9%	-0.6%	-0.1%	-1.9%	1.0%	-1.6%	9.5%	3.3%	1.7%
Oil & Gas Marketing Companies	-1.5%	1.4%	4.0%	-0.7%	-0.4%	17.6%	0.8%	0.7%	1.0%	0.0%
Automobile Assembler	8.2%	-0.1%	1.7%	0.1%	-1.1%	-0.6%	1.2%	0.3%	0.3%	0.3%
Engineering	0.0%	0.8%	0.7%	0.6%	-0.3%	-0.1%	1.1%	0.7%	0.6%	0.4%
Chemical	0.0%	-1.0%	1.1%	1.6%	-0.1%	0.0%	0.0%	0.0%	0.1%	0.1%
Textile Composite	-0.3%	0.6%	-0.1%	0.1%	0.8%	-0.4%	0.2%	0.1%	0.0%	0.1%

Market to re-rate on improving business cycle pick-ups

Market P/E multiple has re-rated nearly ~49% since Aug-19 to stand at 7.6x and trades at forward 2020 P/E of 6.8x, which is still below its historic mean of 8.6x. Periods of sustained low P/E are rare. A look back suggests periods of high interest rates are generally followed by low market multiples as credit growth squeezes, growth slows-down and corporate profitability starts to suffer, typical of economies under contractionary phase. In Pakistan, it happened over multiple times with most recent memory in 2012-13 whereby interest rates peaked at 14% and started to weigh on growth, hence market P/E tanked to a low of 5.6x falling from a high of 8.8x in prior year.

Months leading up to Aug-19 can also be categorized under similar fashion. Following a slew of rate hikes market P/E multiple touched a low of 5.1x a level last seen back in 2008-2009. However, market was soon to correct itself taking early indication from drop in bond yields. Responding to inverted yield curve consensus started to shift, pricing in future rate cuts supported by a string of positive macroeconomic data flow and a general perception of coming through contractionary economic phase.

Exhibit: Pakistan GDP Growth (5yr) and P/E
Recovering growth cycle to uplift P/E



Market multiple to recover to 8.6x in 2020 as business cycle picks up: As business cycle picks up and expected to gain traction by late 2020, taking the next 5-years average GDP growth cycle to ~5% (2024F) from its current 2.4% (2020E IMF), we expect market multiple to also recover to its historical average of 8.6x. Historically in periods of high growth market multiple has averaged 9.0x in Pakistan. Recent example of which is 2013-18, whereby market multiple averaged 9.2x compared to 7.4x during weak growth cycle of 2008-13. Based on our earnings estimates for 2020, market P/E comes at 6.8x, which takes it near to a ~5-year low level and below to its historic average of 8.6x.

Exhibit: Implied P/E based on 5yr growth cycle

Based on 5yr average growth assumption, implied market P/E comes at 8.5x, which is close to its historic average.

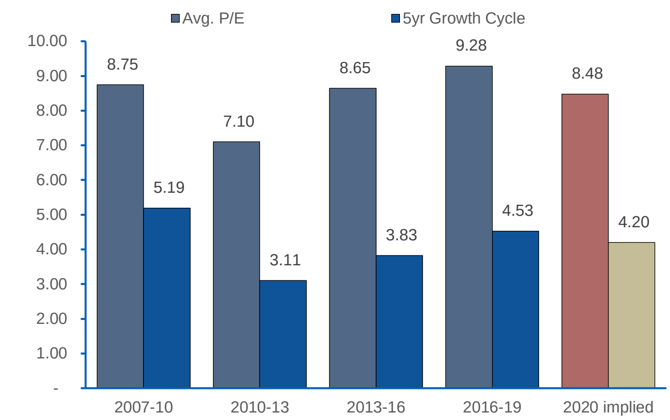
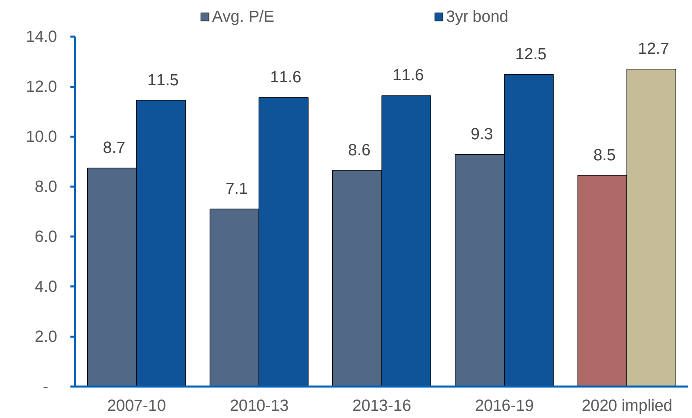


Exhibit: implied P/E based on 3yr Bond Yld

Similarly, taking 3yr. bond yield implied market P/E comes at 8.5x.



Market regional discount justifies weak growth outlook to its peers: Our implied market multiple of 8.6x is relatively in-line with its historic regional discount of ~40% and MSCI emerging market discount of ~35% (MSCI EM 2020fwd P/E of 12.8x). We believe market discounts to region will hold given country's slower growth compared to region.

Exhibit: Key Regional economies Growth

	2018	2019	2020	2021	Avg.	fwd. P/E
Pakistan	3.40	3.40	2.70	4.00	3.37	6.6
China	6.60	6.20	6.10	6.00	6.10	11.2
India	7.20	7.50	7.50	7.50	7.50	23.3
Vietnam	7.10	6.60	6.50	6.50	6.53	13.5
Philippines	6.20	6.40	6.50	6.50	6.47	15.2
Indonesia	5.20	5.20	5.30	5.30	5.27	14.4
Thailand	4.10	3.50	3.60	3.70	3.60	15.5
EM	4.30	4.00	4.60	4.60	4.40	12.8

Valuations

Exhibit: KSE 100 annual returns

After a consecutive 2-years of negative returns 2019 finally ended on a positive note

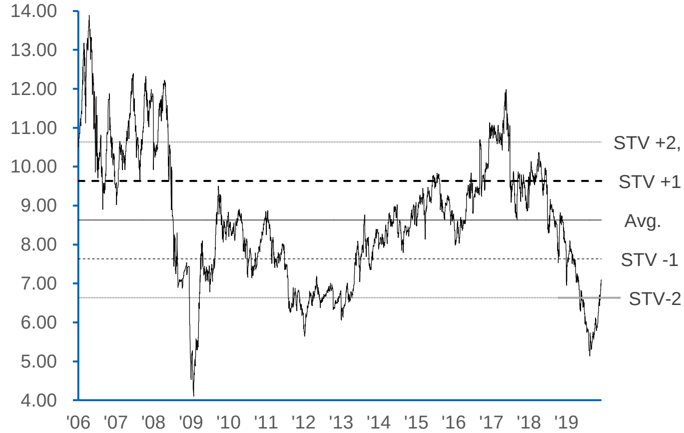


Exhibit: KSE 100 versus Regional Market Returns

Against KSE 100 witnessed a sharp recovery in Aug-19

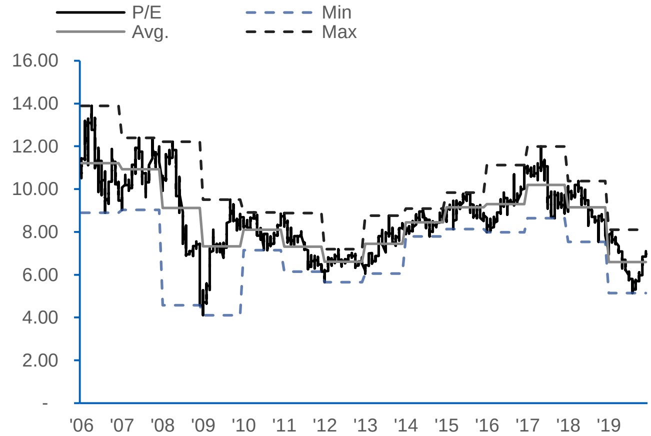


Exhibit: Earnings yield versus 3yr Bond yield

Earnings yields (1/pE) in tandem to 3yr bond yields

Exhibit: Market Cap to GDP

As of current market capitalisation stands at ~17% of the GDP, given a historic average of ~21%, it represents a +23% upside

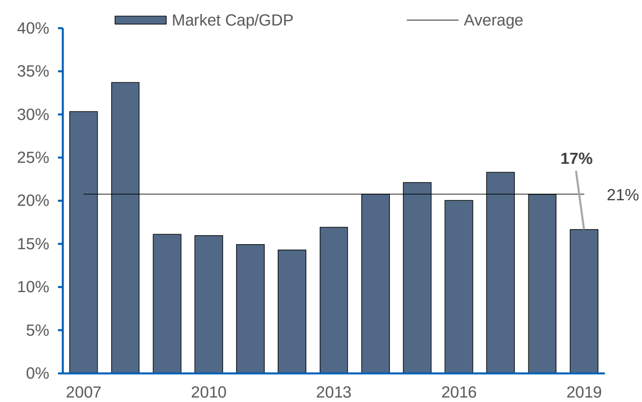
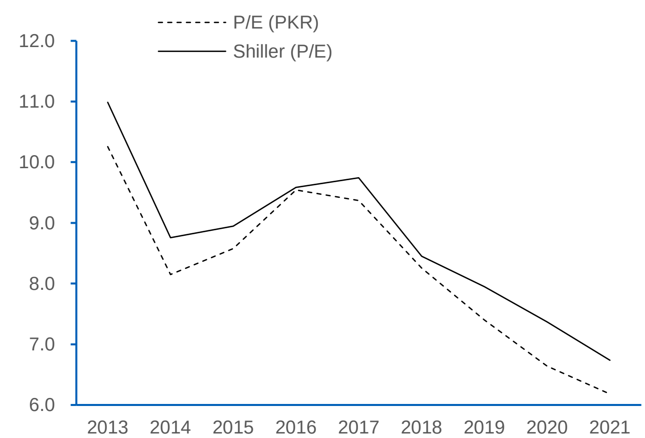


Exhibit: Shiller P/E

Market P/E adjusted for domestic inflation



Regional Comparison

Exhibit: KSE 100 DY and P/E

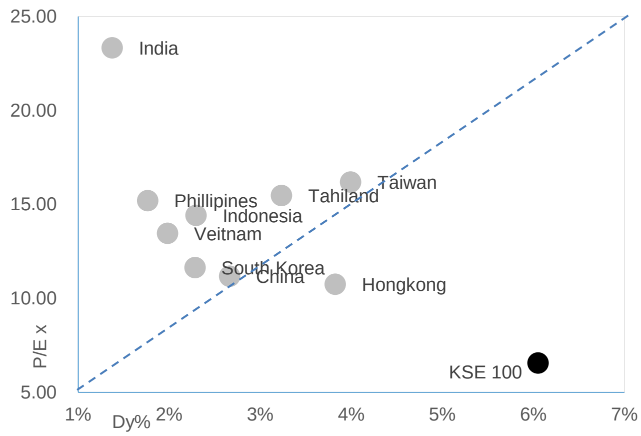


Exhibit: KSE 100 P/B and ROE

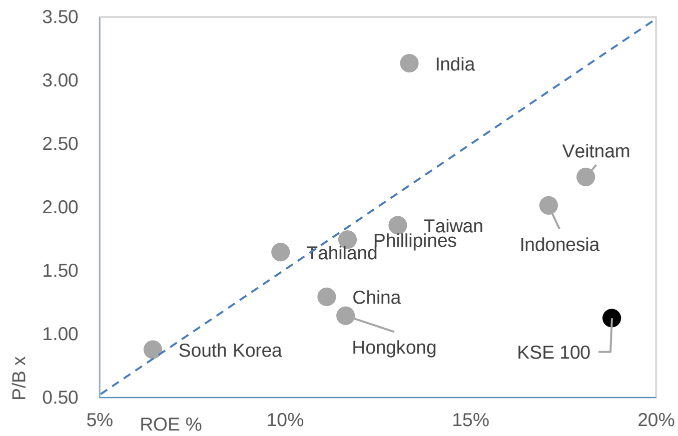


Exhibit: KSE 100 Discount to Regional Markets

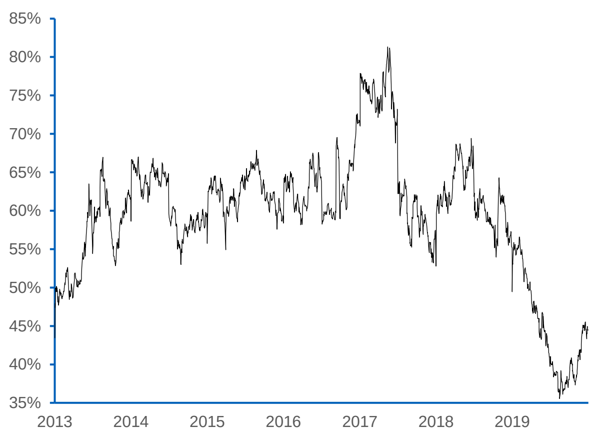


Exhibit: Regional GDP in 2020 and Market 2020 f P/E

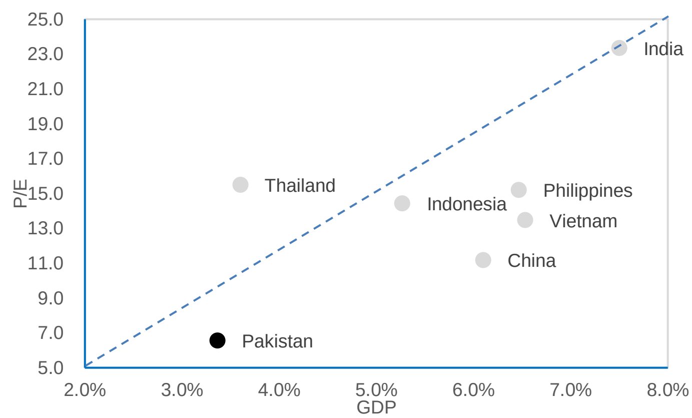


Exhibit: KSE 100 Regional Comparison

		P/E	P/B	D/Y	ROE
Pakistan	KSE100 Index	6.6	1.1	6.1	18.8
Average		**14.6**	**1.8**	**2.6**	**12.5**
India	SENSEX Index	23.3	3.1	1.4	13.4
China	SHCOMP Index	11.2	1.3	2.7	11.1
Hong Kong	HSI Index	10.8	1.1	3.8	11.6
Philippines	PCOMP Index	15.2	1.7	1.8	11.7
Taiwan	TWSE Index	16.2	1.9	4.0	13.0
Vietnam	VNINDEX Index	13.5	2.2	2.0	18.1
Thailand	SET Index	15.5	1.6	3.2	9.9
Indonesia	JCI Index	14.4	2.0	2.3	17.1
South Korea	KOSPI Index	11.6	0.9	2.3	6.4

Liquidity

Exhibit: Mutual Funds AUM (PKRbn)

Mutual fund AUM increased substantially as we close to 2019

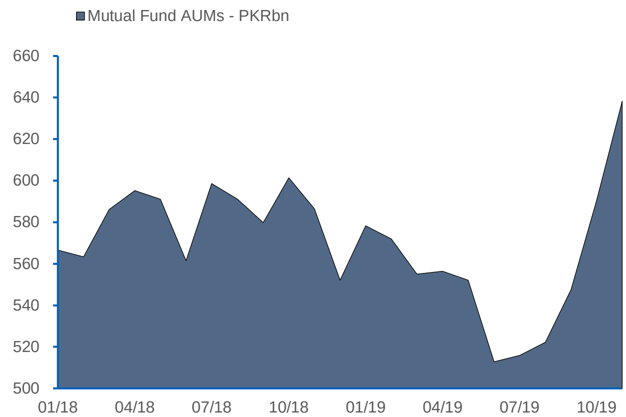


Exhibit: Individual versus Institutions liquidity

Despite higher liquidity at institutions, Individuals were the man liquidity provider (USDmn)

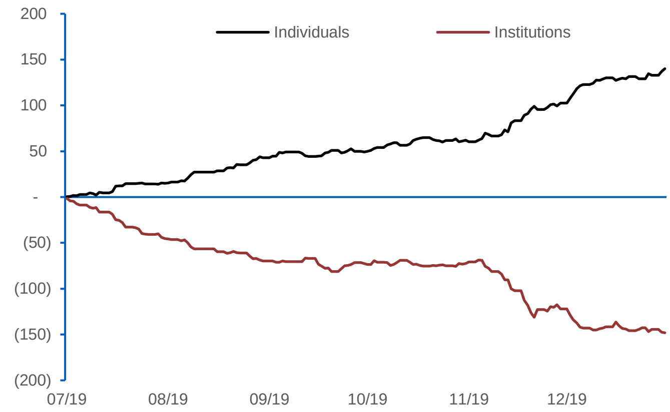


Exhibit: Sector-wise Local investment

E&Ps attracted the most liquidity by locals

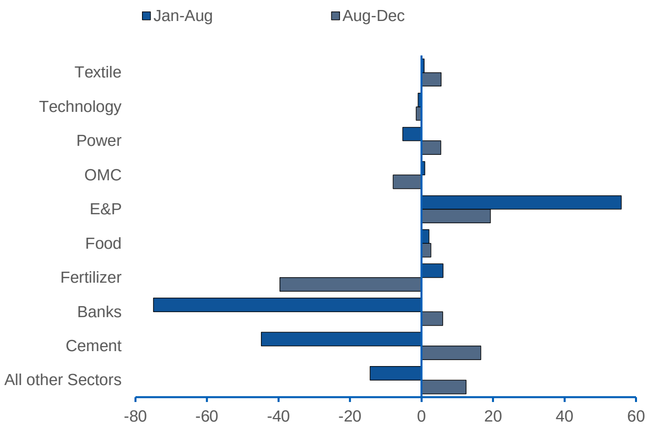


Exhibit: FIPI Sector Wise

Banks remained favourite for foreigners in 2019

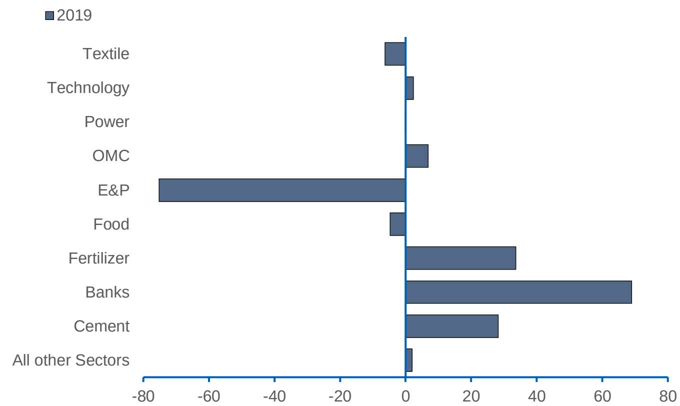


Exhibit: Large Cap volumes

Large cap (OGDC, PPL, MARI, HBL, UBL, MCB, LUCK) volumes averaged nearly 6% of the total market volumes

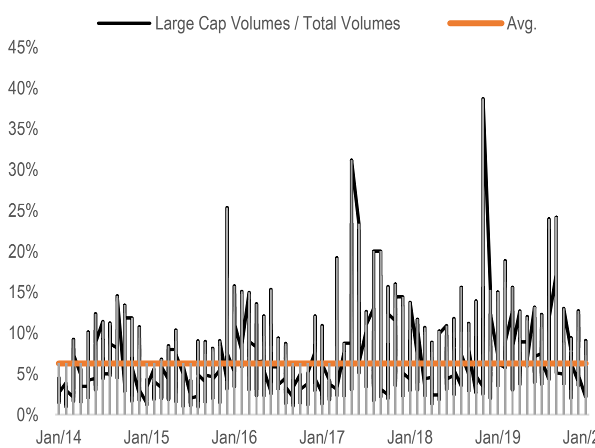
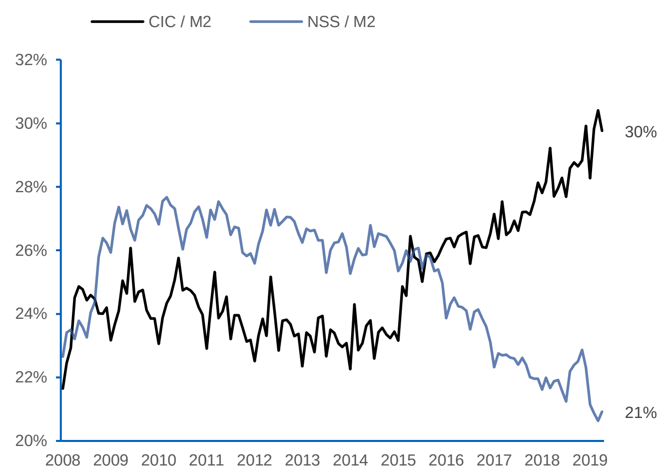


Exhibit: Broad Money

Cash in hand increased reaching 30% of total broad money (M2) while saving (NSS) deposits saw a decline overall



KSE 100 index target	Market Forward P/E	Dividend Yield	Total Return 2020
50,000	**8.6x**	**6.3%**	**~23%**

Eyeing an Index target of 50,000

Base case: Index target of 50,000; offering a total return of +23%

By December 2020, we eye index target of 50,000, generating a total return of ~23% from its current index level of 42.5k. We have taken market P/E multiple approach as our basis for index estimation. Based on our index target of 50,000 market would trade at a forward P/E of 8.6x which is in-line with its historic average.

Market P/E and Index Target

Case	P/E	Index Target
Bear	8.0	48,000
Base	**8.6**	**50,000**
Bull	9.6	55,000

Exhibit: Market Historic average, high and low P/E
Based on our index target of 50,000 market would trade at a forward P/E of 8.6x which is in-line with its historic average

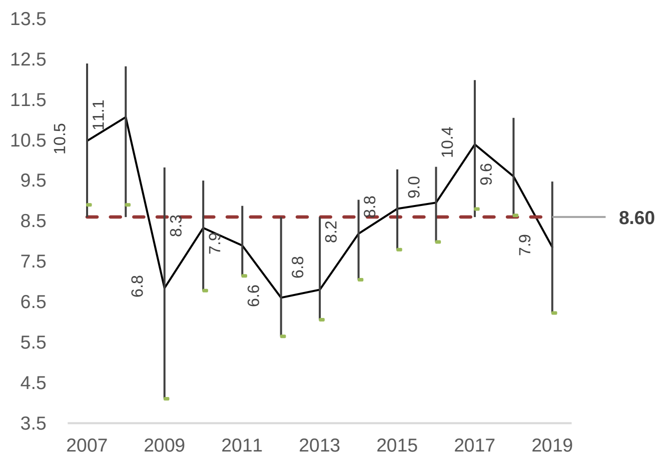


Exhibit: Index Target for 2020
Base=50,000, Bear=48,000, Bull=55,000

Bull Case: 55,000

For our bull case we have factored in aggressive rate cut (300bps in 2020) amid sharp decline in inflation. For that, we highlight declining oil price could act as a catalyst, which could drive stronger economic (GDP growth of 3.0%) and corporate earnings growth than our baseline forecast. Moreover, continued capital inflows in form of FPI and uni/bi-lateral funding will continue to support external accounts and thus FX reserve build-up, which will instill confidence in both local and foreign investors. If materialized, this could stretch equity valuations to its long-term average of 9.6x, implying a target index of 55,000.

Bear Case: 48,000

For our bear case, we factored in slow GDP growth, delays in monetary easing and delays in reform leading to further fiscal constraints. We see less probability of this happening. Based on this our implied market multiple comes at 8.0x giving an index target of 48,000.

Interest Rates	GDP Growth: 2.0%	2.3%	2.4%	3.0%	3.5%
10.5%	10.6	11.3	11.7	13.8	16.2
11.0%	9.6	10.1	10.4	12.1	13.9
11.5%	8.7	9.1	9.4	10.7	12.1
12.0%	8.0	8.3	**8.6**	9.7	10.8
12.5%	7.4	7.7	7.9	8.8	9.7
13.0%	6.8	7.1	7.3	8.1	8.8
13.5%	6.4	6.6	6.8	7.4	8.1

P/E (x)	EPS Growth: -20%	-10%	13.6	10%	20%
7.2	39,000	42,000	45,000	48,000	51,000
7.7	41,000	44,000	47,000	50,000	53,000
8.1	42,000	45,000	48,000	52,000	55,000
8.6	43,000	47,000	**50,000**	54,000	58,000
9.1	45,000	49,000	53,000	56,000	60,000
9.6	47,000	51,000	55,000	59,000	63,000
10.2	49,000	53,000	57,000	62,000	66,000

Strategy

Market Performance during Early Phase

In terms of asset classes stocks outperform other asset classes such as bonds during an early-cycle. Generally, an end of contractionary cycles is marked by easing interest rates, hence sectors and companies that are more sensitive to interest rates perform best at the end of contractionary cycle. These lower interest rates later help stimulate aggregate demand which is marked as the start of early-cycle causing credit demand to expand followed by pick-up in commercial activity as business confidence improves.

Exhibit: Business cycle and economic conditions

	Contractionary	Early	Mid	Late
GDP Growth	**Decline**	**Pick-up**	**Strong**	**Moderate**
Monetary Policy	Start easing	Easing	Neutral	Contract
Credit Growth	Fall	Pick-up	Strong	Tighten
Business Confidence	Low	Improve	Strong	Low
Corporate Profitability	**Fall**	**Recover**	**Expand**	**Moderate**
Inventories	Build-up	Reduce	High	Low
Sales	Slow	Recover	Expand	Moderate
Profit Margins	Decline or Bottom	Recover	Expand	Moderate
Cash	Rebuilding	Build-up	Build-up	Decline
Capex	Declines	Rebuilding	Stabilizes	Accelerate
Market	**Fall**	**Trend Up**	**Peak**	**Trend Down**
Cons. Disc.		++	-	--
Cons. Staples	++			++
Energy				++
Financials		+		
Health Care	++	--		++
Industrials	--	++		
Tech&Comm.	-		+	
Materials		+	--	++
Real Estate	--	++		
Utilities	++	--	-	+

Pakistan had its own set of these early-cycle hits, with latest episode being in 2011-13. As representative of this period consumer discretionary and materials sector performed well, followed by financials and energy (mainly due to less sensitivity to economic cycle and more with oil prices).

Exhibit: Sector Wise Return during economic growth Cycle

	2019	2018	2017	2016	2015	2014	2013	2012	2011	2010	2009
GDP Growth	3.3%	5.5%	5.2%	4.6%	4.1%	4.1%	3.7%	3.8%	3.6%	2.6%	0.4%
Consumer Discretionary	-6%	-24%	-15%	65%	2%	56%	56%	54%	-26%	4%	15%
Consumer Staples	-10%	5%	8%	16%	5%	42%	54%	21%	9%	31%	42%
Energy	-7%	-25%	-9%	58%	-21%	-14%	30%	18%	-14%	26%	98%
Financials	8%	-9%	-19%	31%	-13%	24%	36%	36%	-34%	-2%	35%
Health Care	-2%	-10%	-36%	39%	15%	76%	102%	36%	-21%	-12%	28%
Industrials	0%	-28%	-55%	18%	13%	32%					
Information Technology	3%	-17%	-25%	12%	-6%	-15%	64%	79%	-49%	11%	5%
Materials	-7%	-18%	-30%	68%	6%	49%	45%	103%	-25%	21%	8%
Real Estate	4%	9%	1%	1%							
Utilities	-13%	-10%	-26%	23%	-4%	52%	12%	91%	-22%	10%	44%

In terms of corporate performance matrix, early-cycles generally see a recovery in profitability along with sales and thus profit margins. Sectors such as Materials including Cements, Steel, Chemical and Consumer Discretionary including Autos, Textile, and Consumer Goods perform best in early cycle but their profitability performance matrix varies during the transition from contractionary to early-cycle.

Interest rate sensitive: Companies that have had a high capex in late-cycle were also the ones with high debt level, including cements, chemicals and steel. Hence companies under these sectors will be the early beneficiary of interest rates cuts.

Credit cycle: Autos and Oil & Marketing companies' in general show better profitability performance during the latter part of early-cycle as and when credit growth picks-ups which in our case is likely to come by 1h of Fy21. Similarly, given the credit expansion, banks tend to perform best during these times.

Exhibit: Sector key performance matrix
Sectors include, Cements, Chemicals, OMC, Autos, Textile, Steel

	2014	2015	2016	2017	2018	2019	2020f	2021f	2022f	2023f	2024f
EPS Growth	1.7	1.8	2.1	2.5	2.5	1.4	0.7	1.2	1.8	2.3	2.7
EPS Growth	19%	2%	19%	17%	2%	-44%	-52%	76%	49%	32%	15%
Sales Growth	13%	-13%	-15%	27%	22%	3%	0%	-9%	7%	8%	9%
EBIT Margin	6%	7%	10%	9%	7%	5%	3%	5%	5%	6%	6%
EBIT Growth	22%	2%	17%	15%	-3%	-23%	-33%	22%	29%	23%	11%
Net Margin	4%	4%	6%	6%	5%	3%	1%	2%	3%	4%	4%
P/E	9.7	9.5	7.9	6.8	6.6	11.9	24.9	14.2	9.5	7.2	6.3
P/B	1.6	1.4	1.3	1.1	1.0	1.0	0.9	0.9	0.9	0.8	0.7
EV	784	762	736	775	813	971	948	867	823	753	686
EBITDA	127	132	152	174	172	143	112	132	158	185	200
EV /Ebitda	6.2	5.8	4.9	4.5	4.7	6.8	8.4	6.6	5.2	4.1	3.4

Preferred Picks

Growth at a Reasonable Price

From a market strategy standpoint, we like "growth at a reasonable price" stocks among banks, energy, materials and industrials – both large and mid-caps. Our preferred picks are as follows:

Exhibit: Preferred picks

Sym	Current Price	Target Price	Upside	P/E	D/Y	P/B	3yr - EPS CAGR	3yr - fwd. ROE
KOHC	76	154	102%	16.5	1.3%	0.8	9%	9%
HUBC	103	139	35%	5.4	5.8%	1.9	50%	40%
INDU	1,050	1,403	34%	12.3	5.4%	1.8	-10%	18%
PPL	149	197	32%	6.6	2.7%	1.1	2%	17%
FCCL	17	22	30%	14.6	5.8%	1.2	-2%	9%
MARI	1,370	1,775	30%	5.8	0.5%	1.9	10%	31%
EPCL	35	45	28%	7.4	4.2%	1.4	2%	18%
ISL	57	72	26%	15.8	2.6%	1.9	18%	20%
OGDC	154	191	24%	5.6	7.1%	1.0	-3%	16%
HBL	169	205	21%	6.9	8.1%	1.1	55%	18%
PSO	215	257	20%	7.7	4.7%	0.8	18%	11%
EFERT	75	80	7%	5.4	17.3%	2.1	7%	39%
FFC	103	110	7%	7.5	10.7%	3.5	1%	45%

For high dividend yield stocks, we recommend,

Exhibit: Dividend Yield Stocks

Sym	Current Price	D/Y	DPS 2020	DPS 2021	DPS 2022	3yr - DPS CAGR
EFERT	75	17.3%	13.0	13.0	13.0	6%
FATIMA	27	15.0%	4.1	4.2	3.0	-8%
POL	468	11.2%	52.5	55.0	54.0	3%
FFC	103	10.7%	11.0	11.2	11.2	1%
MCB	222	9.9%	22.0	25.8	28.3	15%
APL	383	9.1%	35.0	40.0	45.0	31%
FABL	22	8.1%	1.8	2.3	2.8	30%
HBL	169	8.1%	13.8	16.5	19.3	50%
ABL	101	7.9%	8.0	9.0	11.0	16%
AKBL	20	7.5%	1.5	1.8	2.3	31%

Based on low P/E we have a preference for,

Exhibit: Low P/E stocks

Sym	Current Price	P/E	EPS 2020	EPS 2021	EPS 2022	3yr - EPS CAGR
FATIMA	27	3.4	8.1	8.4	6.0	-7%
AKBL	20	3.7	5.4	5.7	6.2	12%
FABL	22	4.2	5.2	5.6	6.0	15%
EFERT	75	5.4	14.0	14.5	14.8	7%
BAFL	51	5.4	9.6	9.4	10.8	11%
HUBC	103	5.4	19.0	21.1	29.0	50%
OGDC	154	5.6	27.7	27.1	25.2	-3%
MARI	1,370	5.8	237.8	244.7	244.3	10%
PPL	149	6.6	22.7	22.0	23.7	2%
HBL	169	6.9	24.3	28.8	33.5	55%

Sector Summary

Sector	Stance	Comments	Top pick
Banks	Overweight	Favorable macro tail winds to drive sector profitability in 2020. With monetary easing expected from 1q2020 this may deem positive for NIMs expansion due to reduced cost of funding and laggard impact of asset re-pricing. Moreover, we see risk of NPL formation remains limited as industry coverage and infection ratio mix is placed ideally to its historic trend	HBL, UBL, BAF & AKBL
E&Ps	Overweight	Fy19 recorded a healthy earnings growth for E&P sector on account of PKR depreciation in form of higher well head prices and exchange gains. However, Fy20 earnings growth would be driven by full year impact of PKR depreciation and rise in oil prices due to geopolitical tensions along with easing trade wars. On production front, new discoveries are likely to sustain flows for next 2-3 years whereas new blocks auction would be value accretive for the sector as existing blocks have reached a saturation point with no sizeable discovery in last few years. Foreign ventures with oil companies abroad are almost being explored to enhance production base.	PPL & MARI
Power	Overweight	Resolution of outstanding dues through Sukuk-II bond and structural power sector reforms to improve cash position for IPPs leading to better cash payout. Furthermore, expansion in new projects may allow HUBC to have better earnings growth. Moreover, substantial decline in FO prices post IMO-2020 would lift FO based IPPs position in merit order list.	HUBC
OMCs	Overweight	OMC's (in particular PSO) is likely to benefit from circular debt resolution where outstanding dues on FO and LNG have piled up substantially and are expected to come down post structural reforms to arrest circular debt pile up. This would allow for better cash position for PSO and APL. Moreover, Fy20 is likely to witness growth due to low base in retail segment where MS and HSD are likely to lead volumetric growth. Higher inflation will also pull up notable increase in OMC margin for Fy21.	PSO
Cement	Underweight	Economic contraction and excess supply due to commencement of new plants, especially in North region, is to keep pricing power limited and competition to be intense. These are anticipated to keep gross margins on the lower side. Moreover, record high debt levels to fund expansions in a peaked interest rate scenario is to further dent net margins.	FCCL & KOHC
Engineering	Underweight	With primary raw material highly susceptible to forex exchange movements, the previous 24 months (~50%) PKR depreciation has made the already capital intensive final product pretty costly, hurting margins severely in an already economically tight situation. A heavily geared sector, further injury is expected to incur on account of hefty finance costs in a peaked interest rate scenario where PKR depreciation has only piled up short term debt requirements	ISL
Autos	Underweight	We believe subdued demand may keep volumetric growth restricted. Although, interest rate reversal seems a likely scenario in the next six months or so, we think the worst in terms of sales volume is still looming, a sustainable growth recovery still seems some time away as ongoing macro weakness subsides.	INDU
Fertilizers	Market weight	We see host of factors such as proposed gas price hike, GIDC verdict, and ongoing inventory concern to govern sector dynamics. The sector offers safe investment amid stable demand and manufacturer's strong pricing power. The sector's valuation offers limited upside but consistent pay-outs with high yield and limited risks on horizon warrants a safe bet.	EFERT
Chemical	Market weight	Our coverage companies have monopoly over the products they produce, namely and therefore have the capacity to charge at premium pricing. On the other hand, government stance on limiting imports through increase in duties, may deem beneficial for the sector. More so, currency devaluation impacts favorably to bottom-line owing to imported parity principle. With local prices determined by international prices, the companies in this regard can easily pass on the impact of devaluation, thereby reaping additional margin	EPCL

Exhibit: IGI Coverage Companies Recommendation and key Financial Highlights

SYM	Cur. Price	Target Price	Recom.	EPS			DPS			BVPS			Earnings Gr%		
				'19	'20	'21	'19	'20	'21	'19	'20	'21	'19	'20	'21
INDU	1050.0	1403.0	Buy	174.5	85.6	109.3	108.0	56.4	72.1	509	583	620	-13	-51	28
HCAR	212.2	196.0	Neutral	27.0	7.1	11.1	12.2	3.2	5.1	123	127	133	-41	-74	57
PSMC	226.1	180.8	Sell	-37.4	-19.9	2.2				395	414	430	-337	-47	-111
Autos				**14.5**	**6.1**	**10.4**	**10.2**	**4.9**	**6.4**	**90**	**98**	**103**	**-39**	**-58**	**70**
ACPL	103.1	160.4	Buy	15.1	11.2	14.9	4.0	4.0	7.5	117	124	135	-53	-26	33
CHCC	52.3	56.2	Buy	9.1	-10.9	-8.2	1.0			61	50	41	-11	-220	-25
DGKC	76.7	74.5	Neutral	3.7	-13.5	-6.1	1.0			162	147	141	-82	-467	-54
FCCL	17.2	22.4	Buy	2.0	1.2	1.2	1.5	1.0	1.0	15	15	15	-19	-42	3
KOHC	76.2	153.9	Buy	12.3	4.6	9.7	2.5	1.0	2.0	98	100	109	-17	-62	109
MLCF	22.8	31.6	Buy	4.1	-4.6	-0.5	0.5			51	54	51	-46	-212	-89
PIOC	30.0	72.4	Buy	3.5	-6.5	-4.6				59	52	48	-52	-286	-30
LUCK	493.7	462.3	Neutral	32.4	10.9	14.5	6.5	2.5	3.0	292	296	308	-14	-66	33
Cement				**24.5**	**-4.6**	**4.7**	**6.2**	**2.9**	**3.8**	**278**	**272**	**272**	**-39**	**-119**	**-202**
HBL	169.1	205.0	Buy	9.0	24.3	28.8	5.8	13.8	16.5	145	156	168	6	170	18
NBP	44.6	55.0	Buy	10.3	16.3	14.3			9.5	101	117	123	10	58	-12
UBL	182.0	215.0	Buy	16.4	23.8	28.4	11.3	12.8	16.5	137	148	161	32	45	19
MCB	222.2	245.0	Buy	22.5	27.7	30.3	18.5	22.0	25.8	133	139	144	25	23	10
ABL	100.9	125.0	Buy	11.8	14.0	16.9	7.0	8.0	9.0	94	101	109	4	18	21
BAHL	81.7	95.0	Buy	9.4	10.7	14.4	2.5	3.3	5.3	53	60	70	17	14	34
BAFL	51.5	65.0	Buy	7.9	9.6	9.4	3.5	3.8	4.3	47	53	58	32	21	-2
BOP	13.3	19.0	Buy	3.5	2.9	3.6	1.0	1.0	1.3	14	16	19	23	-17	22
AKBL	19.9	25.0	Buy	4.4	5.4	5.7	1.0	1.5	1.8	33	37	41	24	24	5
FABL	21.7	25.0	Buy	3.9	5.2	5.6	1.3	1.8	2.3	32	35	38	24	32	7
Banks				**140.7**	**199.7**	**220.5**	**66.9**	**88.5**	**127.7**	**1129**	**1244**	**1342**	**19**	**42**	**10**
EFERT	74.9	80.3	Neutral	12.3	14.0	14.5	11.0	13.0	13.0	35	36	38	-6	14	3
FFC	103.1	110.3	Neutral	13.6	13.7	14.0	10.9	11.0	11.2	27	30	32	20	1	2
FFBL	20.8	24.7	Buy	-1.8	0.7	1.3		0.6	0.9	13	13	14	-219	-140	72
FATIMA	27.4	38.8	Buy	7.4	8.1	8.4	3.8	4.1	4.2	33	37	41	17	9	4
Fertilizer				**47.6**	**53.7**	**55.9**	**36.5**	**40.5**	**41.3**	**163**	**177**	**191**	**2**	**13**	**4**
OGDC	154.2	191.1	Buy	27.5	27.7	27.1	11.0	11.0	10.5	145	162	178	50	1	-2
PPL	149.1	197.0	Buy	22.7	22.7	22.0	2.0	4.0	8.5	110	131	144	35	0	-3
POL	468.4	518.7	Buy	59.4	64.7	65.3	50.0	52.5	55.0	134	146	157	48	9	1
MARI	1370.4	1774.9	Buy	182.4	237.8	244.7	6.0	6.5	6.6	477	719	957	58	30	3
E&Ps				**221.2**	**231.1**	**227.7**	**67.7**	**74.0**	**84.8**	**1026**	**1188**	**1330**	**46**	**4**	**-1**
PSO	214.7	257.1	Buy	22.5	28.0	32.8	10.0	10.0	12.0	254	273	294	-32	24	17
HASCOL	26.9	30.8	Buy	-12.6	-1.9	-0.8				1	7	6	-6138	-85	-60
APL	382.6	419.5	Neutral	39.8	39.1	41.6	20.0	35.0	40.0	190	194	196	-30	-2	6
OMC				**2.0**	**15.2**	**18.8**	**6.7**	**8.2**	**9.6**	**139**	**154**	**164**	**-90**	**643**	**24**
KAPCO	29.7	44.8	Buy	14.9	13.3	13.8	4.5	5.5	9.0	47	55	59	23	-11	4
HUBC	103.2	139.0	Buy	8.7	19.0	21.1		6.0	15.0	39	53	60	2	119	11
NCPL	19.0	23.7	Buy	9.3	9.7	2.6	2.0	3.5	4.5	39	46	45	0	4	-73
Power				**27.8**	**39.9**	**40.5**	**4.7**	**13.9**	**29.0**	**107**	**134**	**147**	**11**	**44**	**2**
EPCL	35.3	45.3	Buy	4.7	4.8	5.3	1.0	1.5	0.5	30	33	36	0	1	11
DOL	23.8	29.4	Buy	4.3	5.2	6.1		1.3	1.5	26	28	31	20	20	18
Chemical				**4.7**	**4.9**	**5.5**	**0.9**	**1.5**	**0.6**	**29**	**33**	**36**	**1**	**3**	**12**
ISL	57.4	72.1	Buy	7.2	10.1	13.5	3.0	1.5	2.8	36	43	53	97	41	34
ASTL	37.2	40.1	Neutral	1.7	6.4	10.4			0.8	41	45	51	-252	288	61
Steel				**3.6**	**6.3**	**8.9**	**1.3**	**0.7**	**1.4**	**28**	**32**	**38**	**186**	**74**	**42**

Exhibit: IGI Coverage Companies Valuation Highlights and price performance

SYM	P/E			DY			P/B			ROE			ROA			52 Week		PERFORMANCE		
	'19	'20	'21	'19	'20	'21	'19	'20	'21	'19	'20	'21	'19	'20	'21	HI	LO	03M	06M	12M
INDU	4.6	3.7	3.5	5.0	7.5	8.8	0.6	0.5	0.5	15	15	14	0.7	0.8	0.8	1391	924	5%	-11%	-13%
HCAR	5.5	4.2	3.9	5.8	8.1	10.4	0.7	0.6	0.6	13	16	15	1.0	1.2	1.2	272	116	48%	50%	20%
PSMC	**8.7**	**6.1**	**5.5**	**5.5**	**7.3**	**10.5**	**1.1**	**1.0**	**0.9**	**13**	**17**	**17**	**1.0**	**1.3**	**1.3**	340	149	36%	12%	24%
Autos	6.1	5.4	5.2	14.7	17.3	17.3	2.1	2.1	2.0	35	39	39	13.6	15.6	17.1			**16%**	**2%**	**-2%**
ACPL	7.6	7.5	7.4	10.6	10.7	10.9	3.8	3.5	3.2	51	49	45	12.0	12.0	12.0	137	66	30%	41%	-5%
CHCC	-11.4	28.5	16.5		2.9	4.3	1.6	1.6	1.5	-13	6	9	-2.2	0.9	1.6	91	25	60%	60%	-28%
DGKC	3.7	3.4	3.3	13.9	15.0	15.3	0.8	0.7	0.7	24	23	21	14.2	15.3	15.3	111	42	32%	53%	-10%
FCCL	**6.5**	**5.7**	**5.5**	**11.9**	**13.2**	**13.4**	**1.9**	**1.7**	**1.6**	**30**	**32**	**30**	**10.5**	**12.0**	**12.5**	25	12	16%	14%	-20%
KOHC	5.6	5.6	5.7	7.1	7.1	6.8	1.1	1.0	0.9	20	18	16	16.5	15.3	14.1	103	41	37%	47%	-12%
MLCF	6.6	6.6	6.8	1.3	2.7	5.7	1.4	1.1	1.0	23	19	16	14.9	13.2	12.0	52	14	30%	3%	-49%
PIOC	7.9	7.2	7.2	10.7	11.2	11.7	3.5	3.2	3.0	48	46	43	22.2	22.0	21.6	55	17	25%	39%	-34%
LUCK	7.5	5.8	5.6	0.4	0.5	0.5	2.9	1.9	1.4	47	40	29	13.4	13.3	12.7	532	329	31%	30%	7%
Cement	**6.3**	**6.0**	**6.1**	**4.9**	**5.3**	**6.1**	**1.4**	**1.2**	**1.0**	**23**	**21**	**18**	**15.9**	**14.7**	**13.6**			**30%**	**32%**	**-8%**
HBL	9.5	7.7	6.5	4.7	4.7	5.6	0.8	0.8	0.7	9	11	12	2.6	3.2	4.0	151	106	29%	42%	28%
NBP	-2.1	-14.4	-35.5				38.3	3.9	4.4	-190	-50	-12	-18.2	-2.7	-1.1	50	29	29%	22%	1%
UBL	9.6	9.8	9.2	5.2	9.1	10.5	2.0	2.0	2.0	21	20	21	8.6	8.5	9.0	159	120	25%	22%	32%
MCB	**88.2**	**11.9**	**9.6**	**3.7**	**4.5**	**5.3**	**1.3**	**1.2**	**1.1**	**1**	**10**	**12**	**0.4**	**2.9**	**3.7**	213	154	29%	27%	14%
ABL	2.0	2.2	2.2	15.1	18.5	30.3	0.6	0.5	0.5	34	26	24	9.4	8.6	9.5	113	83	15%	0%	-8%
BAHL	11.9	5.4	4.9		5.8	14.5	2.6	1.9	1.7	26	41	37	5.5	10.0	9.4	87	64	18%	6%	4%
BAFL	2.0	2.0	7.2	10.5	18.4	23.7	0.5	0.4	0.4	26	23	6	12.2	11.8	3.5	51	37	18%	20%	10%
BOP	**6.0**	**4.2**	**4.1**	**2.8**	**8.3**	**17.4**	**1.6**	**1.2**	**1.1**	**29**	**33**	**29**	**7.5**	**9.7**	**9.1**	14	7	36%	52%	5%
AKBL	7.5	7.4	6.6	2.8	4.2	1.4	1.2	1.1	1.0	17	15	15	9.7	9.1	9.5	26	16	6%	5%	-17%
FABL	5.6	4.6	3.9		5.2	6.3	0.9	0.8	0.8	17	19	21	16.8	18.8	20.5	26	15	22%	5%	-10%
Banks	**7.3**	**7.1**	**6.3**	**2.6**	**4.3**	**1.8**	**1.2**	**1.0**	**1.0**	**17**	**16**	**16**	**10.1**	**9.7**	**10.1**			**25%**	**22%**	**12%**
EFERT	8.0	5.7	4.3	5.2	2.6	4.8	1.6	1.3	1.1	22	25	28	7.6	10.5	13.6	79	61	9%	12%	0%
FFC	22.4	5.8	3.6			2.0	0.9	0.8	0.7	4	15	22	1.6	6.1	9.5	109	85	7%	6%	7%
FFBL	**10.0**	**5.7**	**4.0**	**3.6**	**1.8**	**3.9**	**1.3**	**1.1**	**0.9**	**14**	**21**	**25**	**5.1**	**8.6**	**11.9**	44	14	17%	9%	-45%
FATIMA	4.6	3.7	3.5	5.0	7.5	8.8	0.6	0.5	0.5	15	15	14	0.7	0.8	0.8	37	24	6%	-2%	-20%
Fertilizer	5.5	4.2	3.9	5.8	8.1	10.4	0.7	0.6	0.6	13	16	15	1.0	1.2	1.2			**8%**	**7%**	**-7%**
OGDC	**8.7**	**6.1**	**5.5**	**5.5**	**7.3**	**10.5**	**1.1**	**1.0**	**0.9**	**13**	**17**	**17**	**1.0**	**1.3**	**1.3**	154	105	22%	18%	8%
PPL	6.1	5.4	5.2	14.7	17.3	17.3	2.1	2.1	2.0	35	39	39	13.6	15.6	17.1	194	103	9%	3%	-13%
POL	7.6	7.5	7.4	10.6	10.7	10.9	3.8	3.5	3.2	51	49	45	12.0	12.0	12.0	523	349	20%	18%	-2%
MARI	-11.4	28.5	16.5		2.9	4.3	1.6	1.6	1.5	-13	6	9	-2.2	0.9	1.6	1405	830	23%	40%	-1%
E&Ps	3.7	3.4	3.3	13.9	15.0	15.3	0.8	0.7	0.7	24	23	21	14.2	15.3	15.3			**18%**	**15%**	**-1%**
PSO	**6.5**	**5.7**	**5.5**	**11.9**	**13.2**	**13.4**	**1.9**	**1.7**	**1.6**	**30**	**32**	**30**	**10.5**	**12.0**	**12.5**	281	125	24%	36%	-9%
HASCOL	5.6	5.6	5.7	7.1	7.1	6.8	1.1	1.0	0.9	20	18	16	16.5	15.3	14.1	222	12	8%	-55%	-82%
APL	6.6	6.6	6.8	1.3	2.7	5.7	1.4	1.1	1.0	23	19	16	14.9	13.2	12.0	510	233	25%	27%	-14%
OMC	7.9	7.2	7.2	10.7	11.2	11.7	3.5	3.2	3.0	48	46	43	22.2	22.0	21.6			**32%**	**10%**	**-41%**
KAPCO	7.5	5.8	5.6	0.4	0.5	0.5	2.9	1.9	1.4	47	40	29	13.4	13.3	12.7	53	28	-13%	-14%	-39%
HUBC	**6.3**	**6.0**	**6.1**	**4.9**	**5.3**	**6.1**	**1.4**	**1.2**	**1.0**	**23**	**21**	**18**	**15.9**	**14.7**	**13.6**	96	61	37%	33%	15%
NCPL	9.5	7.7	6.5	4.7	4.7	5.6	0.8	0.8	0.7	9	11	12	2.6	3.2	4.0	26	15	5%	11%	-17%
Power	-2.1	-14.4	-35.5				38.3	3.9	4.4	-190	-50	-12	-18.2	-2.7	-1.1			**24%**	**22%**	**-1%**
EPCL	9.6	9.8	9.2	5.2	9.1	10.5	2.0	2.0	2.0	21	20	21	8.6	8.5	9.0	42	21	27%	28%	-11%
DOL	**88.2**	**11.9**	**9.6**	**3.7**	**4.5**	**5.3**	**1.3**	**1.2**	**1.1**	**1**	**10**	**12**	**0.4**	**2.9**	**3.7**	37	13	46%	52%	-21%
Chemical	2.0	2.2	2.2	15.1	18.5	30.3	0.6	0.5	0.5	34	26	24	9.4	8.6	9.5			**29%**	**29%**	**-12%**
ISL	11.9	5.4	4.9		5.8	14.5	2.6	1.9	1.7	26	41	37	5.5	10.0	9.4	89	29	31%	67%	-17%
ASTL	2.0	2.0	7.2	10.5	18.4	23.7	0.5	0.4	0.4	26	23	6	12.2	11.8	3.5	0	0	41%	64%	-23%
Steel	**6.0**	**4.2**	**4.1**	**2.8**	**8.3**	**17.4**	**1.6**	**1.2**	**1.1**	**29**	**33**	**29**	**7.5**	**9.7**	**9.1**			**34%**	**66%**	**-19%**

Exhibit: IGI Coverage Companies Valuation metrics

SYM	EBITDA / Margin			Net Margin			Ebit Margin			Debt/ Equity			EV / Ebitda			Sales Growth		
	'19	'20	'21	'19	'20	'21	'19	'20	'21	'19	'20	'21	'19	'20	'21	'19	'20	'21
INDU	13.4	12.8	13.2	8.7	6.4	6.8	12.1	9.0	9.6				2.6	5.2	3.9	13.1	(33.2)	18.9
HCAR	6.8	6.0	4.9	4.0	1.9	2.5	5.9	4.3	3.6				3.7	8.5	8.2	3.9	(45.3)	21.2
PSMC	2.6	3.6	3.7	(3.7)	(2.1)	0.2	(1.3)	(0.4)	0.3	0.1	0.0		9.8	6.3	5.0	(31.3)	(7.3)	5.4
Autos	**8.9**	**8.3**	**8.4**	**4.3**	**2.6**	**3.9**	**7.0**	**4.9**	**5.4**	**0.0**	**0.0**		**3.4**	**5.9**	**4.6**	**(4.5)**	**(30.3)**	**15.0**
ACPL	18.5	17.1	17.0	10.0	7.5	9.6	14.7	13.3	13.4	0.4	0.2	0.1	5.4	4.7	3.8	23.1	(0.9)	3.9
CHCC	22.6	9.5	9.2	11.1	(11.2)	(8.5)	13.8	(0.3)	(0.2)	1.8	1.9	2.2	8.6	16.3	16.3	11.4	18.9	(0.9)
DGKC	21.8	4.6	13.4	4.0	(15.5)	(6.6)	13.1	(5.2)	4.0	0.6	0.7	0.7	8.4	43.6	14.2	32.1	(6.3)	6.6
FCCL	29.0	21.3	21.4	13.6	8.9	9.4	21.7	12.7	13.0	0.1	0.0	0.0	4.1	5.5	5.6	(1.7)	(12.3)	(2.1)
KOHC	27.5	18.8	25.1	15.8	6.4	10.7	23.8	11.5	16.8	0.3	0.2	0.1	4.3	6.9	3.4	16.4	(7.9)	25.5
MLCF	25.1	8.1	16.8	9.5	(11.2)	(1.2)	15.0	(6.8)	3.8	0.7	0.5	0.6	5.4	15.3	7.0	1.3	(5.8)	9.3
PIOC	21.6	6.7	17.3	8.1	(13.6)	(6.3)	16.4	(3.5)	6.9	1.6	1.8	2.1	13.0	38.6	10.4	(3.8)	11.6	51.9
LUCK	32.3	19.8	20.5	21.8	8.1	8.9	25.4	9.8	11.0	0.0	0.0	0.0	9.4	14.9	11.5	1.0	(9.9)	21.3
Cement	**25.7**	**13.2**	**17.5**	**12.4**	**(2.5)**	**2.2**	**18.5**	**3.6**	**8.4**	**0.4**	**0.4**	**0.4**	**7.5**	**14.0**	**9.1**	**9.8**	**(4.4)**	**12.5**
EFERT	32.0	30.5	29.1	15.2	16.8	16.9	27.4	26.2	25.0	0.6	0.4	0.2	3.3	3.2	3.2	(1.7)	3.7	2.9
FFC	27.9	25.1	24.5	16.0	15.3	15.1	26.0	23.3	22.7	0.7	0.6	0.5	3.2	3.3	3.4	2.3	5.2	3.6
FFBL	7.2	9.3	9.1	(3.0)	1.1	1.9	4.5	7.1	7.0	2.6	2.3	2.2	8.9	5.5	5.9	(6.0)	9.2	0.5
FATIMA	50.2	49.5	49.3	29.7	32.5	33.6	47.0	46.2	46.1	0.1	0.1		2.1	1.7	1.4	14.0	(0.6)	0.4
Fertilizer	**29.2**	**27.7**	**26.9**	**14.6**	**15.8**	**16.0**	**26.0**	**24.7**	**24.1**	**0.6**	**0.4**	**0.3**	**3.2**	**3.0**	**2.9**	**1.0**	**4.5**	**2.3**
OGDC	79.1	74.7	73.4	45.3	43.5	42.4	68.2	63.6	61.8				2.7	2.6	2.3	27.3	4.9	0.3
PPL	60.9	58.7	58.9	37.6	35.1	33.7	49.2	47.9	48.0	0.0	0.0	0.0	3.9	3.4	2.7	29.9	7.5	0.9
POL	76.1	67.9	68.0	38.4	37.7	38.6	65.1	57.1	57.0				2.9	2.7	2.5	38.0	10.8	(1.3)
MARI	61.9	64.1	63.5	40.9	44.7	43.1	56.8	58.0	57.6				4.2	3.0	2.5	46.1	19.5	6.7
E&Ps	**71.3**	**67.9**	**67.2**	**41.8**	**40.5**	**39.5**	**60.8**	**57.5**	**56.6**	**0.0**	**0.0**	**0.0**	**3.2**	**2.9**	**2.4**	**30.9**	**7.8**	**1.1**
PSO	2.4	2.6	3.3	0.9	1.1	1.7	2.3	2.5	3.2	0.9	0.7	0.5	7.4	5.5	4.9	9.2	6.5	(25.7)
HASCOL	(0.6)	2.5	2.6	(10.4)	(1.2)	(0.4)	(1.6)	1.6	1.8	60.4	5.8	6.0	(90.4)	14.9	13.2	(48.5)	32.3	9.6
APL	2.8	3.0	3.1	1.8	1.9	2.0	2.6	2.6	2.6				5.4	5.3	4.7	25.8	(9.8)	3.6
OMC	**2.2**	**2.6**	**3.2**	**0.1**	**1.0**	**1.4**	**2.0**	**2.4**	**2.9**	**1.1**	**0.8**	**0.6**	**9.5**	**6.4**	**5.8**	**2.0**	**6.1**	**(18.5)**
KAPCO	34.9	37.5	33.6	15.5	16.3	16.2	32.1	34.2	30.5	1.3	1.0	0.7	2.7	2.7	2.5	(7.7)	(15.4)	4.7
HUBC	42.9	46.8	44.7	19.3	39.4	43.9	34.9	39.0	36.9	1.9	1.7	1.8	8.8	7.5	8.2	(41.9)	7.7	(0.2)
NCPL	38.9	32.4	25.3	22.7	18.6	9.2	31.7	26.8	15.2	1.0	0.8	0.4	3.7	3.2	5.1	(9.5)	27.6	(45.2)
Power	**38.2**	**40.6**	**37.7**	**17.6**	**26.0**	**27.4**	**33.1**	**35.2**	**32.1**	**1.6**	**1.3**	**1.3**	**5.3**	**5.0**	**5.5**	**(24.2)**	**(2.8)**	**(3.6)**
EPCL	23.2	21.5	20.1	11.9	11.2	11.8	20.5	17.9	16.3	0.3	0.2	0.2	4.7	4.6	4.8	2.0	8.3	5.6
DOL	30.7	25.0	25.9	16.2	17.9	19.4	24.3	19.7	21.1	0.4	0.3	0.2	4.1	3.6	2.8	29.5	8.7	8.2
Chemical	**23.8**	**21.8**	**20.5**	**12.2**	**11.6**	**12.3**	**20.7**	**18.0**	**16.6**	**0.3**	**0.2**	**0.2**	**4.6**	**4.5**	**4.6**	**3.5**	**8.3**	**5.8**
ISL	11.0	10.2	12.2	5.7	8.0	9.3	9.0	7.9	10.1	1.1	0.9	0.7	7.0	7.8	5.3	15.6	(0.5)	15.6
ASTL	4.2	5.8	8.1	1.7	5.8	8.5	4.2	3.8	6.2	1.0	1.0	0.9	19.2	12.6	8.4	84.5	14.6	10.2
Steel	**8.7**	**8.5**	**10.7**	**4.3**	**7.2**	**9.0**	**7.4**	**6.4**	**8.7**	**1.1**	**1.0**	**0.8**	**9.0**	**9.0**	**6.1**	**32.5**	**4.7**	**13.5**

Exhibit: Commercial banks key financial metrics

Sym	NIM			Non-II / Rev.			Cost / Income			Prov. / ROA			ROA			Asset / Equity			ROE		
	19	20	21	19	20	21	19	20	21	19	20	21	19	20	21	19	20	21	19	20	21
HBL	3.9	4.8	4.6	16.5	18.0	17.4	78.2	61.4	59.5	0.0	0.1	0.1	0.5	1.2	1.1	14.2	14.1	15.6	6.4	16.2	17.8
NBP	4.2	5.1	4.5	25.0	23.0	25.2	49.2	45.0	49.9	0.3	0.2	0.2	1.2	1.6	1.4	13.2	12.4	12.3	16.3	20.2	16.7
UBL	4.1	4.9	5.0	24.2	21.3	20.8	50.7	46.8	45.6	0.4	0.4	0.2	1.1	1.5	1.6	11.7	11.0	11.1	12.6	16.7	18.3
MCB	4.4	4.7	5.3	21.4	20.5	18.3	44.8	42.4	36.9	(0.0)	(0.1)	(0.1)	1.6	1.8	2.2	9.7	9.9	10.8	15.3	18.3	23.2
ABL	3.4	3.7	3.8	20.3	20.6	19.6	52.4	52.1	49.3	(0.1)	(0.1)	(0.1)	1.1	1.2	1.3	11.9	11.6	12.1	12.6	14.3	16.1
BAHL	4.2	4.3	4.6	14.4	14.3	12.6	59.4	59.5	54.6	(0.0)	(0.0)	(0.0)	1.0	1.1	1.3	19.3	17.6	17.5	19.3	19.0	22.2
BAFL	5.1	5.2	4.6	16.6	16.6	17.4	52.3	50.9	53.6	0.2	0.2	0.1	1.3	1.5	1.3	13.2	13.0	13.2	17.6	19.1	16.9
BOP	4.2	3.3	3.3	12.6	16.6	15.7	44.7	51.1	48.3	0.2	0.1	0.1	1.3	0.9	1.0	19.4	20.5	20.9	24.7	19.1	20.4
AKBL	3.4	3.6	3.5	22.5	20.8	21.1	64.4	62.7	64.1	0.1	0.1	0.1	0.7	0.8	0.8	19.5	18.2	18.1	14.5	15.3	14.4
FABL	3.9	4.2	4.1	26.7	24.9	24.8	58.9	58.0	59.3	0.0	0.3	0.1	1.1	1.1	1.2	13.3	12.8	13.0	14.3	13.6	15.0
Banks	4.1	4.4	4.3	20.0	19.7	19.3	55.5	53.0	52.1	0.1	0.1	0.1	1.1	1.3	1.3	14.5	14.1	14.5	15.4	17.2	18.1

Over-weight

Commercial Banks

Macro Tailwinds to up Sector Earnings

We remain **'Over-weight'** on Pakistan Banks in 2020 and favour large-to-small tier. Sector earnings performance mainly dependent on favorable macro tailwinds with limited risk on horizon.

- ✓ **Net interest Margins** - Starting 2019, the SBP (State Bank of Pakistan) has hiked discount rate by cumulative +325bps taking the key policy rate to 13.25% (reverse repo 13.75%), owing to rise in inflation and weak external account balances. While this has helped lift yield on earning assets, but overall NIMs remained relatively stable ~4.0-**4**.5% in 2019 as cost of funding also tagged along. Stepping into 2020, monetary easing is expected to start from 1q 2020 onwards, which should allow for decline in cost of funding (due to cut in deposit rates and a reduction in bank borrowing discouraged by inverted yield curve) along with laggard impact of asset re-pricing. Hence in terms of NIMs guidance, we expect 35-45bps additions from its current. Here large banks in our view have an upper hand over small, due to better a) deposit mix and growth, b) better loan risks, and c) diversified revenue stream (fee income).
- ✓ **Asset growth** – So far in 2019, asset growth has been robust tilted toward government securities offering higher asset yields funded by growth in deposit and bank borrowing. Contrary to historical trends, investments in government securities this time around in our view is likely to show a slowdown primarily as a) government reduce bank borrowing, b) government debt duration tilted to LT than ST, and c) lower yield on LT maturity bonds. We think credit growth will pick-up albeit moderately (xx% in next 3-yrs., compared to xx% in past 5-yrs.). Risk of NPL formation on income remain limited as industry coverage and infection ratio mix is placed ideally to its historic trend.

Earnings and Valuation: Earnings for Large-5 banks during 2019 was held back by higher non-recurring operating expenses (PPOP growth for large-5 2019: +17% vs 38% in mid-small-tier), however provision charge remained less of drag on profitability. 3yr forward EPS growth is expected to post a ~>25% compared to mid-small-tier ~+11%. Banks ROE are estimated to >~17% and P/B values are below their historic trend.

Top picks and recommendation: For large banks, we prefer HBL and UBL, as our top pick, while BAFL fall under our growth pick and AKBL as value picks.

Key Risks: a) Implementation of IFRS9 from 2021, b) FATF blacklisting, c) Implementation of Treasury single account, d) Major asset deterioration on domestic and international book.

			3yr	EPS			DPS			P/E			D/Y			P/B			ROE		
Sym	Recomm.	TP (PKR)	EPS CAGR	19	20	21	19	20	21	19	20	21	19	20	21	19	20	21	19	20	21
HBL	BUY	205	55%	9.0	24.3	28.8	5.8	13.8	16.5	18.8	6.9	5.9	3.4	8.1	9.8	1.2	1.1	1.0	6.4	16.2	17.8
NBP	BUY	55	12%	10.3	16.3	14.3	-	-	9.5	4.3	2.7	3.1			21.3	0.4	0.4	0.4	10.4	14.9	11.9
MCB	BUY	245	14%	22.5	27.7	30.3	18.5	22.0	25.8	9.9	8.0	7.3	8.3	9.9	11.6	1.2	1.2	1.1	17.4	20.4	21.5
UBL	BUY	215	27%	16.4	23.8	28.4	11.3	12.8	16.5	11.1	7.6	6.4	6.2	7.0	9.1	1.1	1.0	0.9	12.6	16.7	18.3
ABL	BUY	125	16%	11.8	14.0	16.9	7.0	8.0	9.0	8.5	7.2	6.0	6.9	7.9	8.9	0.5	0.5	0.5	12.6	14.3	16.1
BAFL	BUY	65	11%	7.9	9.6	9.4	3.5	3.8	4.3	6.5	5.4	5.5	6.8	7.3	8.3	0.4	0.4	0.4	17.6	19.1	16.9
BAHL	BUY	95	16%	9.4	10.7	14.4	2.5	3.3	5.3	8.7	7.6	5.7	3.1	4.0	6.4	0.4	0.4	0.4	19.3	19.0	22.2
FABL	BUY	25	15%	3.9	5.2	5.6	1.3	1.8	2.3	5.5	4.2	3.9	5.8	8.1	10.4	0.2	0.1	0.1	13.1	15.6	15.1
AKBL	BUY	25	12%	4.4	5.4	5.7	1.0	1.5	1.8	4.6	3.7	3.5	5.0	7.5	8.8	0.1	0.1	0.1	14.5	15.3	14.4
BOP	BUY	19	5%	3.5	2.9	3.6	1.0	1.0	1.3	3.8	4.5	3.7	7.5	7.5	9.4	0.2	0.2	0.1	24.7	19.1	20.4
Commercial Banks			**20%**							**8.7**	**6.1**	**5.5**	**5.5**	**7.3**	**10.5**	**1.1**	**1.0**	**0.9**	**12.9**	**16.8**	**17.1**

Habib Bank Limited (HBL)

Habib Bank Limited (HBL) earnings has been under stress, with its EPS stuck under PKR 10/share since 2017, and 2019 seems no different with EPS estimated at PKR 9.0/share with a slightest nip of improvement from last year. Higher operating costs and slowdown in non-interest income mainly on account of a) NY branch wrap-up, b) regulatory initiatives, c) exchange losses, and d) upgradation of its alternative delivery channel (ADC) 'Konnect/FMFB'. However, post 2019, we estimate bank's EPS to display a +~55% cagr over the next 3-yrs., which should be able to pull its current ROE of ~6% on average to >~17% by 2022.

Investment thesis

- ✓ **High earning asset yields -** Earning asset yields of bank have shown a consistent improvement and have accelerated later in 9m 2019e to ~11%, an increase of +350bps from last year, benefiting from 1h 2019 rate hikes and rolling over of matured high-yield sovereign bonds at higher rates. In 2020 we expect trend to continue and asset yield of the bank to remain upbeat as full impact of rate hike will follow through at the least till 1h 2020.
- ✓ **Cost-of-funding improving but more grounds to catch -** Moreover, cost of funding growth will remain limited due to build-up in favourable deposit mix (CASA: 86% with 37% of current deposits) and reduction in bank borrowing owing to yield curve inversion. The combine impact of this should help the bank post a double digit growth to its net interest income in 2020, pulling up net interest margins (NIM) in the range of 4.8% which is in-line with its historic performance.
- ✓ **Absences of one-offs, non-interest income to support total revenue base -** Similarly, non-interest income excluding capital gains during 2020 is expected to normalize, in absence of major fluctuations in FX income and a stable and a growing fee income trend will further cushion total revenue growth in 2020.
- ✓ **Cost-to-income should begin normalizing in 2020-**But more importantly, following +20% and 21% y/y growth in 2018/19e respectively in operating expenses (Opex), in 2020 opex is expected to show some normalization. Bank management expects US remediation costs will eventually evaporate by 1h 2020, while business transformation will remain but won't be that substantial, hence a cost-to-income should start to descend from current ~78% to 60% in 2020 and beyond.
- ✓ **Limited worry on NPL provisioning charge-** Bank's asset quality is well favorable, high coverage ratio (~87% in Sep-19) with a falling infection ratio (7% in Sep-19 from 12% in 2014) which despite an above industry loan growth (~18% on average 2017-2019) has reduced major provisioning drag on income. In-line with industry recovery rate (5-7%) and low net NPLs means risks of high NPL provisioning charge remain limited

Recommendation: We value HBL stock on a Gordon growth model assuming cost of equity at 17.8%, normalized ROE 20% and a growth rate 9%, giving a Dec-20 fair value of PKR 205/share. We apply exit multiple of 1.25x, derived using above assumptions, to the CY20e equity base of HBL which is PKR 156bn. The stock is currently trading at Cy 20e P/E of 6.7, P/B of 1.03 and a DY of 8.6%.

Key Risks: a) Capital buffer remains thin amid bank has been designated as DSIB (domestic systematically important bank), b) Additional provisioning on domestic assets under IFRS9 still needs to reflect, which as per bank's management is likely to come-by in 2021, c) Government pushing for a treasury single account (TSA) although formalities are yet to be disclosed, HBL has about ~10% of its deposits from government, d) Business transformation and NY branch remediation costs expand in to 2020 and beyond.

Habib Bank Limited (HBL)

Current Price: (PKR) 169.11 | Target Price: (PKR) 205 | Upside: 21% | BUY

Period end (DEC) - PKRbn	2018A	2019E	2020F	2021F	2022F
Income Items					
Net Interest Income	81,677	96,772	128,547	146,865	161,569
Fee Income	18,024	18,925	21,764	23,941	25,856
Non Interest Income	19,894	19,174	28,304	30,968	33,206
Total Op. Revenues	101,571	115,945	156,851	177,833	194,775
Operating Exp.	74,978	90,698	96,229	105,856	116,532
Pre-Prov. Profits	26,593	25,247	60,621	71,977	78,243
Provisions	5,009	746	2,521	3,206	3,333
Pre-tax Profits	21,585	24,502	58,101	68,771	74,910
Tax	9,144	11,286	22,384	26,454	25,804
Post-tax Profits	12,441	13,216	35,717	42,317	49,106
Balance Sheet Items					
Gross Advances	1,152,434	1,325,299	1,457,829	1,574,455	1,700,411
NPLs	80,831	90,831	99,831	109,831	119,831
Net Advances	1,080,440	1,234,468	1,357,998	1,464,624	1,580,580
Investments	1,390,052	1,078,277	1,464,327	1,946,889	2,199,985
IEA	2,564,412	2,402,295	2,921,825	3,523,451	3,907,055
Non-IEA	2,703,073	2,485,611	3,031,658	3,666,916	4,089,653
Total Assets	3,025,853	2,821,156	3,382,177	4,034,993	4,478,066
Deposits	2,137,293	2,396,171	2,662,413	2,995,214	3,384,592
CASA%	83%	82%	82%	82%	82%
IBL	2,703,073	2,485,611	3,031,658	3,666,916	4,089,653
Total Liabilities	2,826,601	2,609,140	3,153,937	3,787,944	4,209,431
Share Capital	14,669	14,669	14,669	14,669	14,669
Total Equity	199,252	212,017	228,240	247,049	268,635
Per Share Data					
EPS (diluted)	8.5	9.0	24.3	28.8	33.48
EPS Growth%	46%	6%	170%	18%	16%
DPS	4.00	5.75	13.75	16.50	19.25
BVPS	136	145	156	168	183.1
Capital					
CAR %	16.2%	15.3%	15.0%	14.9%	14.9%
RORWA	1.1%	1.0%	2.5%	2.7%	2.9%

Period end (DEC)	2018A	2019E	2020F	2021F	2022F
Valuation					
P/E (X)	19.9	18.8	6.9	5.9	5.1
P/B (X)	1.24	1.17	1.09	1.00	0.92
Div. Yld (%)	2.4%	3.4%	8.1%	9.8%	11.4%
Payout	47%	64%	56%	57%	58%
Bonus (%)	0%	0%	0%	0%	0%
ROA	0.4%	0.5%	1.2%	1.1%	1.2%
ROE	6.4%	6.4%	16.2%	17.8%	19.0%
NIMs	3.4%	3.9%	4.8%	4.6%	4.3%
Asset Quality					
IEA Yld%	6.8%	9.4%	12.0%	10.6%	9.3%
IBL Yld%	3.3%	5.2%	6.9%	5.8%	4.8%
Cost of Deposit	3.0%	4.9%	6.5%	6.0%	5.0%
IDR	65.0%	45.0%	55.0%	65.0%	65.0%
ADR	50.6%	51.5%	51.0%	48.9%	46.7%
Infection Ratio	7.0%	6.9%	6.8%	7.0%	7.0%
NPL/Assets	2.7%	3.2%	3.0%	2.7%	2.7%
Coverage Ratio	84.7%	84.7%	84.7%	84.7%	84.7%
Growth Rates					
Advances	25.1%	15.0%	10.0%	8.0%	8.0%
NPL	6.6%	12.4%	9.9%	10.0%	9.1%
IEA	11.4%	-6.3%	21.6%	20.6%	10.9%
Deposits	6.9%	12.1%	11.1%	12.5%	13.0%
NII	-0.2%	18.5%	32.8%	14.2%	10.0%
Fee income	-7.7%	5.0%	15.0%	10.0%	8.0%
Operating Exp.	20.2%	21.0%	6.1%	10.0%	10.1%
PPOP	-50.4%	-5.1%	140.1%	18.7%	8.7%
EPS	46.4%	6.2%	170.3%	18.5%	16.0%
Non-Financial					
Branches	1,743	1,758	1,768	1,778	1,788

Source: IGI Research, Company Financials — *Updated as of : 10-Jan-20*

Over-weight

Oil & Gas Exploration Companies

New blocks and energy reforms key to sustainability on reserves

We maintain our '**Over-weight**' stance on the E&P sector. We base our investment thesis on the back of full year impact of PKR depreciation in Fy20 and likely improvement in cash position post structural reforms to recover cost. Furthermore, auction of new blocks in pipeline would also allow E&P to expand their acreage in to untapped areas which remain as high potential zones. Recovery of over dues from SNGP /SSGC post gas tariff hikes and Sukuk issue would allow better cash position to expand production base outside of Pakistan and also allow for increase in cash payout.

- ✓ **Recovery of over dues to improve cash position for OGDC and PPL** - Recent hikes in gas tariff and likely Sukuk-II issue would improve recoveries of over dues from SNGP and SSGC for PPL and OGDC which would in turn lead to better cash position and payout. This would also allow better cash position for investment abroad with international oil giants in our view.
- ✓ **New blocks key to arrest natural depletion and sustainability of reserves** - GoP has planned to auction new blocks for exploration which remain highly lucrative in terms of sizeable discovery potential as existing blocks have already reached saturation point lacking any notable discovery in recent years. The first round of auction started last year in Nov-18 which 10 blocks being auctioned.
- ✓ **Development projects and new discoveries to boost production in next 3yrs** - Development projects such as Nashpa, Adhi, Mela and Dhok Hussain are likely to enhance flows from these wells whereas new discoveries coming online would further sustain and grow oil and gas flow for the next 3 years. Success at Makori Deep-2 development well along with drilling in Jhandial-2 and Nashpa-10 wells remain imperative to sustain production flows.
- ✓ **With oil showing signs of recovery, E&P sector remains highly undervalued** - Oil prices have started to show signs of recovery amid deeper production cuts by OPEC and non-OPEC members, easing trade tensions and geopolitical tensions, where Arab light prices have crossed USD 68/bbl while E&P sector trading at implied oil price of below USD 40/bbl.

Earnings and Valuation: We estimate sector to post a modest +4%y/y growth in Fy20, owing to hefty exchange gains booked in Fy19, primarily led by MARI. However, in the absence of exchange gains, sector is likely to post +4%y/y EPS growth on account of full year impact of PKR depreciation and sustainable gas production.

Top picks and recommendation: We maintain PPL and MARI as our top picks and OGDC value stock. Considering recovery of over dues and development projects coming online along with new discoveries to commence production in next few years.

Key Risks: a) Substantial drop in oil prices, b) Higher dry well costs amid lack of new blocks on offer c) Delays in bidding and allocation of new blocks for exploration, d) Lower demand from refineries effecting fields production for prolonged periods, e) Divestment of GoP stake to keep supply concerns at forefront.

Sym	Recomm.	TP (PKR)	3yr EPS CAGR	EPS			DPS			P/E			D/Y			P/B			ROE		
				19	20	21	19	20	21	19	20	21	19	20	21	19	20	21	19	20	21
OGDC	BUY	191	-3%	27.5	27.7	27.1	11.0	11.0	10.5	5.6	5.6	5.7	7.1	7.1	6.8	1.1	1.0	0.9	20.1	18.1	15.9
PPL	BUY	197	2%	22.7	22.7	22.0	2.0	4.0	8.5	6.6	6.6	6.8	1.3	2.7	5.7	1.4	1.1	1.0	22.9	18.9	16.1
POL	BUY	519	-1%	59.4	64.7	65.3	50.0	52.5	55.0	7.9	7.2	7.2	10.7	11.2	11.7	3.5	3.2	3.0	47.6	46.1	43.1
MARI	BUY	1775	10%	182.4	237.8	244.7	6.0	6.5	6.6	7.5	5.8	5.6	0.4	0.5	0.5	2.9	1.9	1.4	46.9	39.8	29.2
Oil & Gas Exploration			**0%**							**6.3**	**6.0**	**6.1**	**4.9**	**5.3**	**6.1**	**2.7**	**2.3**	**2.1**	**23.4**	**20.9**	**18.1**

Pakistan Petroleum Limited (PPL)

We base our investment case on 3yr profitability CAGR of +2% over Fy20-22 while earnings are expected to remain stagnant in Fy20 on account of hefty exchange gains in Fy19 (+19%y/y EPS growth in Fy20 excluding exchange gains in Fy19). PPL is also likely to benefit from gas sector reforms and Sukuk issue which would ease cash constraints leading to improved cash pay-out and investment in new exploration asset locally and abroad.

Investment thesis

- ✓ **Gambat south to start production post completion of GPF IV**: With completion of Gambat South Gas Processing Facility (GPF)-IV, we expect discoveries to commence production bringing total production to nearly 133mmcfd. Production from Gambat south remains lucrative for PPL as it would be priced under PP12 and would constitute nearly 15% of total gas production of PPL.
- ✓ **Resolution of circular debt to allow for normalized cash pay-outs:** PPL's receivables have soared to PKR 259bn as at Sep-19 from PKR 142bn in Fy18 out of which PKR 202bn is outstanding from SNGP and SSGC alone. Total overdue amount from SOE's stand at PKR 217bn (GENCO-II, SNGP, SSGC and OGDC). As result PPL's cash pay-out ratio has dropped from 69% in Fy17 to 9% in Fy19. The GoP has planned to issue 2nd Tranche of PKR 200bn Sukuk to clear overdue amount with gas and electricity tariff hike of 124% and PKR 2.6/unit for improved cost recovery of gas utility companies. As a result of settlement of dues from these SOE's, PPL is likely to increase its cash pay-out and enhance its exploration activities.
- ✓ **Dhok sultan, Adhi and drilling in Iraq block to further expand production base:** The Company's management expects Dhok Sultan to be game changer for PPL where the well tested for 4000bopd of oil whereas Adhi oil production is expected to sustain at 10,000bopd for next few years. Furthermore, PPL plans to drill a number of wells in Iraq block with first well Madain-1 planned for drilling.
- ✓ **Oil production to grow by +13% in next 3 years:** PPL's oil production is expected to grow by +13% in next 3 years on account of new discoveries coming online including addition in Gambat South. Nashpa and Dhok Sultan. Nashpa production is expected to increase by 1,120bopd post completion of compression unit. Dhok Sultan production is estimated to be ramped up to 4000bopd. Depletion of Sui gas field has also been contained to nearly 400mmcfd.

Recommendation: We value PPL stock on a reserve based-discounted model, giving a Dec-20 target price of PKR 197.0/share (32% upside). The company is currently trading at Fy20E P/E of 6.6x.

Key Risks: Key risks to our rating on PPL are a) Delay in production commencement from Gambat South, b) unfavorable decision regarding Tal Block verdict, c) aggressive drilling with little success could lead to higher exploration expense and, d) further pile up of receivables from SSGC and SNGP.

Pakistan Petroleum Limited (PPL)

Current Price (PKR):	149		Target Price (PKR):	197		Upside	32%		Recommendation		BUY
Jun-end	FY18A	FY19A	FY20E	FY21F	FY22F	Jun-end	FY18A	FY19A	FY20E	FY21F	FY22F
Income Statement Items (PKRmn)						**Valuation Ratios**					
Net Sales	126,210	163,890	176,160	177,781	191,509	EPS (PKR)	16.79	22.65	22.73	22.04	23.69
Field Expenditure	47,206	67,251	61,293	65,250	68,860	DPS (PKR)	5.50	2.00	4.00	8.50	9.00
Royalty	18,512	24,329	26,392	26,225	27,536	BVPS (PKR)	121.92	151.45	180.10	198.35	217.96
Gross Profit	60,491	72,310	88,474	86,306	95,113	P/E (x)	11.73	6.58	6.56	6.77	6.30
Other Income	9,319	16,528	6,533	6,485	6,534	P/EBITDA (x)	6.83	5.37	5.19	5.12	4.69
Other Exp.	5,931	8,166	10,606	7,503	7,393	D/Y (%)	2.79	1.02	2.03	4.47	4.82
Finance Costs	444	741	816	823	832	P/B (x)	1.62	1.30	1.09	0.99	0.90
Pre-tax Profits	63,436	79,931	83,586	84,464	93,422	Earnings Growth (%)	28.05	34.90	0.36	(3.05)	7.49
Post- Tax Profits	45,688	61,632	61,853	59,970	64,461	ROE (%)	19.01	20.64	17.42	15.33	15.00
Balance Sheet Items (PKRmn)						ROA (%)	12.44	13.45	12.93	11.53	11.54
PPE	154,703	159,842	168,549	176,425	184,726	Cash / Share	3.91	4.07	7.47	19.54	18.32
D/P Asset	37,691	45,285	51,164	57,924	65,699	**Margins**					
Expl & Eval Assets	16	34	16	16	16	Gross Margins (%)	47.93	44.12	50.22	48.55	49.66
Non-Current Assets	192,913	205,734	220,676	235,397	251,665	EBIT Margin (%)	50.61	49.22	47.91	47.97	49.22
Trade Debts	142,636	227,382	220,199	222,226	245,132	Net Profit Margins (%)	36.20	37.61	35.11	33.73	33.66
Cash	7,715	8,022	14,723	38,530	36,128	**Macro- Assumption**					
Current Assets	174,408	252,557	257,588	284,556	306,915	Oil (USD/bbl)	62.4	69.4	65.0	60.0	55.0
Total Assets	367,321	458,291	478,264	519,953	558,580	PKR/USD	110.0	135.7	156.0	158.4	161.2
Payables	61,883	88,389	78,955	81,681	83,005	**Production (boe) '000**					
Current Liabilities	64,094	94,938	81,123	88,195	85,155	Total Production	62,122	61,106	58,158	58,823	63,312
Non-current liabilities	62,835	64,744	42,037	40,672	43,662	Oil (bbl)	5,801	5,754	5,881	6,409	6,497
Total Equity	367,321	458,291	478,264	519,953	558,580	Gas (boe)	56,320	55,353	52,277	52,414	56,815
Cash Flow Items (PKRmn)											
Operating CF	33,672	23,115	76,381	79,940	62,410						
Investing CF	(14,489)	(25,640)	(37,234)	(35,127)	(37,654)						
Financing CF	(9,533)	3,763	(33,377)	(21,006)	(27,159)						

Source: IGI Research, Company Financials

Updated as of : 10-Jan-20

Mari Petroleum Company Limited (MARI)

We base our investment case on 3yr profitability CAGR of +10% over Fy20-22 while earnings are expected to post healthy earnings growth in FY20 of +30%YoY. Our liking for the scrip emanates from higher wellhead gas price which has reached 100% of the wellhead gas price and full year impact will be visible in FY20. Furthermore, higher production from HRL field fetches PP12 wellhead gas price which is likely to remain key earnings driver in next 3 years.

Investment thesis

- ✓ **Mari wellhead gas price reached 100%**: Under the revised mechanism, Mari field wellhead gas price reached 100% of the gas price in Jan-19 for which full year impact will be visible in FY20. Resultantly this is likely to have annualized earnings impact of PKR 9.4/share in FY20.
- ✓ **Development well to sustain production plateau at 650mmcfd:** As per management, Phase-I of the plan to drill 19 development well in Mari gas field to arrest and sustain the production plateau from Mari HRL at 650mmcfd was successfully completed by Jun-19. Out of these 19 wells, 12 wells have already been put on production. Once these wells are connected then the production could be further enhanced to 630-650mmcfd. Phase-II has been kicked off where major pipeline hydraulic constraints were determined by 3rd party and debottlenecking and revamping of Central Manifolds is underway to ensure sustainable production from HRL field.
- ✓ **Lower benchmark during customer plant closure days:** MARI is also expected to benefit from lower benchmark rate of production during ATA of customers plant at 477.5mmcfd which allows MARI to better avail PP12 pricing on incremental production during lower demand. As a result MARI achieved availability of 98% days out of 92 days in 1QFY20.
- ✓ **Aggressive on exploration, 9 wells planned for drilling in FY20:** MARI remains aggressive on exploration front while 9 wells have been planned for drilling in FY20. Recently MARI announced substantial oil discovery in Ghauri Block while seismic data acquisition in Bannu West, Block-28, Sukkur and Kalchas. Our of these wells include 2 exploratory well in Mari field to be spud in Mar-Apr'20, Sughar (Karak) by May-20 and Bannu West (Jun-20). Non-Operated include 3 wells in Bela West, Kohat and Hala Block.
- ✓ **Plan to assure uninterrupted supply from Mari field:** To assure uninterrupted supply from Mari field, the Company plans to negotiate take-or-pay basis agreement with customers and utilization of unutilized gas to swing customers. This would allow to ensure sustainable gas flows from Mari field and better availability of incremental revenue under PP12 pricing.
- ✓ **Enhancing production base in short-medium term…:** The company further expects to enhance its exploration portfolio by acquiring new block in the upcoming bidding of new blocks to allow for drilling in untapped areas specially in frontier areas. Furthermore, MARI plans to acquire exploration assets outside of Pakistan to further expand its assets and reserve size.
- ✓ **…while long term plan to diversify:** However, in the long term the management of the company is primarily focused on diversifying its operations in to oil pipeline, refinery, power project, renewable and alternate energy.

Recommendation

We maintain MARI as one of our top picks with Dec-20 target price of PKR 1,774.9/share (30% upside). The company is currently trading at Fy20E P/E of 5.8x.

Key Risks

Key risks to our rating on MARI are a) substantial drop in production from Mari HRL field resulting in loss of additional revenue on PP12 pricing and, b) lack of substantial addition of reserves to arrest natural decline in Mari gas field.

Mari Petroleum Company Limited (MARI)

Current Price (PKR):	1,370		Target Price (PKR):		1,775	Upside	30%			Recommendation	BUY
Jun-end	FY18A	FY19A	FY20E	FY21F	FY22F	Jun-end	FY18A	FY19A	FY20E	FY21F	FY22F
Income Statement Items (PKRmn)						**Valuation Ratios**					
Net Sales	40,676	59,448	71,016	75,743	75,055	EPS (PKR)	115.25	182.36	237.78	244.70	244.28
Royalty	5,181	7,575	9,048	9,651	9,563	DPS (PKR)	6.00	6.00	6.50	6.60	6.70
Operating Costs	9,985	11,713	13,854	14,958	15,242	BVPS (PKR)	364.55	576.93	869.54	1,158.19	1,446.32
Exploration Costs	3,690	4,308	5,165	5,380	5,606	P/E (x)	11.89	7.51	5.76	5.60	5.61
Gross Profit	20,372	33,417	40,038	42,651	41,569	P/EBITDA (x)	7.86	5.03	4.14	3.90	3.91
Other Income	(207)	326	1,121	969	1,569	D/Y (%)	0.44	0.44	0.47	0.48	0.49
Finance Costs	640	802	957	442	475	P/B (x)	3.76	2.38	1.58	1.18	0.95
Pre-tax Profits	20,292	34,708	44,008	45,546	45,468	EPS Growth (%)	68.28	58.23	30.39	2.91	(0.17)
Post- Tax Profits	15,374	24,327	31,720	32,643	32,587	ROE (%)	72.13	74.46	78.19	67.89	50.90
Balance Sheet Items (PKRmn)						ROA (%)	21.10	20.96	22.89	21.23	17.58
PPE	13,266	16,176	19,101	21,391	24,092	Cash / Share	65.93	60.19	116.04	169.97	193.47
D/P Asset	11,887	12,756	13,481	14,361	14,837	**Margins**					
Expl & Eval Assets	2,690	6,554	8,857	11,475	14,257	Gross Margin (%)	50.08	56.21	56.38	56.31	55.38
Non-Current Assets	29,760	36,407	41,737	47,408	53,471	EBIT Margin (%)	49.58	56.76	57.96	57.59	57.47
Trade Debts	95,295	148,940	158,550	142,695	128,425	Net Profit Margins (%)	37.80	40.92	44.67	43.10	43.42
Cash	7,269	6,636	12,793	18,739	21,330	**Macro- Assumption**					
Current Assets	114,406	183,655	213,551	210,708	205,528	Oil (USD/bbl)	62.4	69.4	65.0	60.0	55.0
Total Assets	144,166	220,062	255,289	258,117	258,999	PKR/USD	110.0	136.3	156.0	158.4	161.2
Trade Payables	93,805	140,372	153,054	122,444	90,058	**Production (boe) '000**					
Current Liabilities	96,022	146,398	153,547	122,836	90,352	Total	45,355	45,241	45,945	48,002	48,165
Non-current Liabilities	103,974	156,455	159,422	130,426	99,543	Oil (bbl)	543.8	405.1	453.9	618.4	634.7
Total Equity	40,192	63,607	95,867	127,691	159,457	Gas (boe)	44,811.3	44,835.7	45,491.0	47,383.2	47,530.5
Cash Flow Items (PKRmn)											
Operating CF	18,171	20,120	31,942	20,145	16,488						
Investing CF	(9,801)	(21,947)	(22,142)	(15,094)	(14,677)						
Financing CF	(3,388)	2,405	(4,854)	895	780						

Source: IGI Research, Company Financials *Updated as of : 10-Jan-20*

Oil & Gas Development Company Limited (OGDC)

We base our investment case on healthy balance sheet with consistent cash pay-out and cheaper valuation multiples. OGDC likely to post +1%y/y EPS growth in Fy20 whereas excluding exchange gains EPS likely to post +11%y/y growth. Furthermore, receipt of over dues from Sui companies is likely to improve cash position easing way for acquisition of new exploration assets to sustain and enhance production base. Development projects in pipeline are also expected arrest production decline concerns.

Investment thesis

- ✓ **New discoveries along with development projects to help sustain production flows**: Recent discoveries along with development project including Mela, Nashpa, Bitrism and Dhok Hussain are likely to help sustain production flows. New exploratory discoveries are expected to add ~91mmcfd of gas and ~1,700bopd of oil in next 3 years. Development project at Nashpa would allow to sustain oil flows and increase LPG flows to ~370mtpd while Mela and Dhok Hussain would increase oil and gas flows. Nashpa project is expected to be completed by Jun-20 while Mela in Jan-20.
- ✓ **Receivables to come down post reforms and energy Sukuk** – OGDC's receivables have spiked to PKR 264bn as at Sep-19 from PKR 164bn in Fy18 out of which PKR 218bn is overdue from oil refineries and gas companies. We expect the receivables amount to come down post issuance of Sukuk-II and increase in tariff for gas companies. This would allow OGDC to expedite and ramp up its drilling activity along with investment in foreign blocks with international oil giants.
- ✓ **Aggressive exploration to continue in Fy20:** OGDC has planned to spud 17 exploratory and 8 development/appraisal wells in Fy20 along with 1 shale well. This along with auction of new blocks by GoP would allow the company to arrest the issue of low reserve replacement ratio due to its high production base.
- ✓ **Cheaper multiple along with healthy pay out:** OGDC remains cheap in terms of implied oil price (USD 30/bbl) whereas it offers healthy pay out (40% in Fy19) despite substantial rise in receivables. OGDC also has the second highest reserve life of 16.5yrs after MARI. Recent revision in gas reserves of 72% and 5% in Uch and Qadirpur which contribute combined 53% to total gas production, would allow to sustain flows from these wells post development.

Recommendation

We value OGDC stock on a reserve based-discounted model, giving a Dec-20 Target price of PKR 191.2/share, offering 24% upside from last close. OGDC is currently trading at Fy20 P/E of 5.6x compared to market and E&P sector P/E of 8.0x and 6.0x respectively.

Key Risks

Key risks to our rating on OGDC are a) delay in production commencement from old and new discoveries, b) no resolution in circular debt leading to pile up of receivables restricting growth potential and c) further depletion in aging wells such as Qadirpur, Uch and Nashpa.

Oil & Gas Development Company Limited (OGDC)

Current Price (PKR):	154		Target Price (PKR):		191
Jun-end	**FY18A**	**FY19A**	**FY20E**	**FY21F**	**FY22F**
Income Statement Items (PKRmn)					
Net Sales	205,335	261,481	274,281	275,068	261,927
Royalty	21,971	29,336	30,772	31,076	29,489
Operating Costs	60,213	63,456	65,977	68,358	69,908
Gross Profit	121,480	167,062	175,824	173,921	160,900
Exploration Costs	16,190	12,499	13,301	13,164	12,675
Other Income	16,008	32,288	19,360	16,613	16,244
Finance Costs	1,730	1,693	1,721	1,150	1,003
Pre-tax Profits	112,627	176,599	172,745	168,928	157,044
Post- Tax Profits	78,736	118,386	119,194	116,560	108,298
Balance Sheet Items (PKRmn)					
PPE	124,064	117,787	121,844	134,293	147,285
D/P Asset	94,404	91,959	102,606	99,538	94,803
Expl & Eval Assets	6,526	15,217	18,478	26,152	33,436
Non-Current Assets	35,627	31,849	113,058	114,238	113,808
Trade Debts	163,692	242,732	227,653	261,314	256,688
Cash	3,670	20,570	19,988	21,545	63,436
Current Assets	405,858	509,786	436,533	487,395	533,965
Total Assets	666,477	766,597	792,517	861,615	923,297
Trade Payables	55,195	72,643	48,968	49,215	48,074
Current Liabilities	55,195	72,643	48,968	49,215	48,074
Non-current Liabilities	60,726	68,588	48,263	45,928	42,404
Total Equity	550,556	625,365	695,287	766,472	832,818
Cash Flow Items (PKRmn)					
Operating CF	60,993	84,421	141,468	114,010	143,754
Investing CF	(19,077)	(30,559)	(71,605)	(63,537)	(55,061)
Financing CF	(42,977)	(39,448)	(67,959)	(48,916)	(46,802)

Upside	24%		Recommendation		BUY
Jun-end	**FY18A**	**FY19A**	**FY20E**	**FY21F**	**FY22F**
Valuation Ratios					
EPS (PKR)	18.31	27.53	27.71	27.10	25.18
DPS (PKR)	10.00	11.00	11.08	10.83	10.06
BVPS (PKR)	128.01	145.40	161.66	178.21	193.64
P/E (x)	8.42	5.60	5.56	5.69	6.12
P/EBITDA (x)	4.72	3.20	3.24	3.29	3.49
D/Y (%)	6.48	7.13	7.20	7.00	6.55
P/B (x)	1.20	1.06	0.95	0.87	0.80
EPS (%)	23.40	50.36	0.68	(2.21)	(7.09)
ROE (%)	14.30	18.93	17.14	15.21	13.00
ROA (%)	11.81	15.44	15.04	13.53	11.73
Cash / Share	0.85	4.78	4.65	5.01	14.75
Margins					
Gross Margins (%)	59.16	63.89	64.10	63.23	61.43
EBIT Margin (%)	55.69	68.19	63.61	61.83	60.34
Net Margins (%)	38.35	45.28	43.46	42.38	41.35
Macro- Assumption					
Oil (USD/bbl)	62.4	72.0	65.0	60.0	55.0
PKR/USD	110.0	136.3	156.0	158.4	161.2
Production (boe) '000					
Total Production	80,109	79,429	90,296	90,675	87,750
Oil (bbl)	15,066	14,896	14,285	14,122	13,558
Gas (boe)	65,043	64,533	76,011	76,553	74,192

Source: IGI Research, Company Financials *Updated as of : 10-Jan-20*

Market-weight

Fertiliser

Stable demand to keep sector dynamics afloat

We maintain **'Market-weight'** stance on the sector and see host of factors such as proposed gas price hike, GIDC verdict, and ongoing inventory concern to govern sector dynamics. Although as valuation offers limited upside but consistent pay-outs with high yield and limited risks on horizon warrants a safe bet.

- ✓ **Oversupply situation, short time concern** - Urea sales so far in 2019 have posted a +16%y/y growth, outstripping demand causing higher inventory levels (~1mnT, +4.0x y/y). Looking ahead, in 2020 gas supply to RLNG plants may suspend causing inventories to deplete. The prospects of exports of existing inventories remain probable in our view.
- ✓ **GIDC issue as yet remains inconclusive** - The year 2019 started off on GIDC front wherein proposal was put forth for 50% waiver on GIDC outstanding dues (PKR~70bn) and 50% reduction in cess rate on feed/fuel. The issue ended in deadlock and was passed over to the court. On a positive note if enacted, would lead to a one-off gain on sector earnings, with FFC being the prime beneficiary. The recurring impact on earnings will be positive for FFC/FFBL while negative for EFERT/FATIMA. On the flip side, if the decision goes against the manufacturers, that is fertilizers have to pay outstanding dues, it would result in excessive cash outflow from the balance sheet, and company's might have to compromise their short term investments.
- ✓ **Gas price hike and GIDC verdict to determine pricing -** We view two key areas to determine urea price levels proposed gas price hike and GIDC verdict. Fertilizer players have so far increased urea prices by PKR 500/bag to over PKR 2,000/bag. On the other end talks for another gas price increase (both for feed/fuel), would raise input costs by PKR ~600/bag, which will raise Urea bag price to PKR 2,600/bag (close to current imported prices). Although manufacturers have been successful in passing the price to farmers, this time around a govt. pro-farmer approach will make it rather difficult, hence we think GDIC resolution will come in-hand via reduction in cess-rate to reduce overall input cost.

Earnings and Valuation: We estimate sector to post +12%y/y growth in CY20, owing to sustainable fertilizer offtake and high prices. Moreover, drop in finance cost (owing to reversal in interest rates) and stable income stream from different businesses may sustain earnings, in our view.

Top picks and recommendation: We maintain EFERT as our top pick based on strong dividend yield and trading at low P/E compared to forward market P/E of 8.75x

Key Risks: a) Increase in gas prices, b) Decrease in fertilizer prices, c) Increase in finance costs and d) High inventory levels from continuous operation of RLNG-based fertilizer plants.

Sym	Recomm.	TP (PKR)	3yr EPS CAGR	EPS			DPS			P/E			D/Y			P/B			ROE		
				19	20	21	19	20	21	19	20	21	19	20	21	19	20	21	19	20	21
EFERT	NEUTRAL	80	7%	12.3	14.0	14.5	11.0	13.0	13.0	6.1	5.4	5.2	14.7	17.3	17.3	2.1	2.1	2.0	35.3	39.0	39.0
FFC	NEUTRAL	110	1%	13.6	13.7	14.0	10.9	11.0	11.2	7.6	7.5	7.4	10.6	10.7	10.9	3.8	3.5	3.2	51.4	48.6	45.2
FFBL	BUY	25	-191%	(1.8)	0.7	1.3	-	0.6	0.9	(11.4)	28.5	16.5		2.9	4.3	1.6	1.6	1.5	(13.1)	5.6	9.4
FATIMA	BUY	39	-7%	7.4	8.1	8.4	3.8	4.1	4.2	3.7	3.4	3.3	13.9	15.0	15.3	0.8	0.7	0.7	23.6	22.9	21.3
Fertiliser			**3%**							**6.5**	**5.7**	**5.5**	**11.9**	**13.2**	**13.4**	**3.5**	**3.2**	**3.0**	**29.9**	**31.6**	**30.4**

Engro Fertilizer Limited (EFERT)

We are overweight on EFERT currently trading at P/E of 5.4x. Offering at a discount of 35% with respect to market P/E of 8.8x the company also offers decent dividend yield. The company's low cost structure and high payout with an attractive dividend yield (18%) are the key factors underlining our case.

Investment thesis

- ✓ **Benefit of concessionary feed gas rate-** The Company has low cost structure owing to concessionary feed gas rate for its enVen plant as per Fertiliser Policy 2001. While, other players in the industry increase their product prices to offset incremental gas costs, EFERT in this regard has margin to charge at increased prices (impact of gas price increase stands low compared to industry average), thereby reaping additional margins. However, post CY22 the standard feed gas rate may apply and we see margins to narrow down (~25% drop in earning)
- ✓ **Diverse product portfolio-** having maintained 35% share in urea market EFERT is also expanding its product category in blended phosphate segment (NP/NPK/SSP). Comprising 5% (NP/NPK) in sales mix this perhaps bodes well, with less seasonal variation experienced in this segment
- ✓ **GIDC issue-** The GIDC matter presents mixed impact on company's earnings. On one end, we see earnings to have one-offs of PKR1.33/share, while from the other perspective the recurring impact is negative PKR ~2/share with 50% reduction in cess rate.
- ✓ **Highest payout-** EFERT has the highest payout ratio backed by ample free cash flow generation (PKR ~15/share). This is reflective during the CY19 performance so far, wherein the company's payout exceeded 1.4x from its 9mcy19 earnings. While we don't expect any dividends in the last quarter, we see company maintaining its payout going forward.

Recommendation

We maintain EFERT as one of our top picks with our Dec-20 Target price of PKR 80/share, offering +7% upside from last close. The company is currently trading at CY20E P/E of 5.2 x at a dividend yield of 18%

Key Risks

a) Increase in gas prices, b) Decrease in fertilizer prices, c) Increase in finance costs, d) High inventory levels from continuous operation of RLNG-based fertilizer plants, e) Reduction in cess rate and f) PKR depreciation against USD.

Engro Fertilizers Limited (EFERT)

Current Price (PKR):	75		Target Price (PKR):		80
Period end (DEC) – PKRmn	CY18A	CY19E	CY20P	CY21P	CY22P
Income Statement					
Net Sales	109,197	107,352	111,273	114,516	119,068
Gross Profit	35,316	37,153	36,185	36,702	37,466
Selling / Dist.	8,008	7,920	7,952	8,360	8,783
Operating Profits	25,723	27,676	26,619	26,681	26,957
Other Op. Income	2,062	3,981	4,347	3,728	3,313
Ebit	26,353	29,440	29,108	28,585	28,453
Finance Cost	2,071	4,137	2,807	1,383	579
Pre-Tax Profits	24,282	25,304	26,301	27,202	27,874
Taxation	6,869	8,938	7,627	7,888	8,084
Post-Tax Profits	17,414	16,366	18,674	19,313	19,791
Balance Sheet Items					
Non-Current Assets	72,834	71,624	70,435	69,268	68,121
Stores And Spares	5,325	7,349	7,617	7,839	8,151
Interest And Mark-Up Accrued	426	426	426	426	426
Current Assets	44,887	52,212	45,062	41,239	42,446
Total Assets	117,721	123,836	115,498	110,507	110,567
Non-Current Liabilities	33,069	29,192	15,521	10,275	7,512
Payables	16,496	19,662	19,013	21,066	20,965
Total Liabilities	72,198	76,626	66,961	60,005	57,621
Total Equity	45,523	47,210	48,537	50,502	52,946
Cashflow Items					
Operating Cash Flow	21,174	21,843	22,279	24,746	23,149
Investing Cash Flow	(5,230)	(7,538)	4,085	1,610	(3,520)
Financing Cash Flow	(14,751)	(20,282)	(26,364)	(26,357)	(19,629)
Closing Cash	730	1,735	1,735	1,735	1,735
Per share Data					
Eps	13.0	12.3	14.0	14.5	14.8
Dps	11.0	11.0	13.0	13.0	13.0
Bvps	34.1	35.4	36.4	37.8	39.7

Upside	7%		Recommendation		HOLD
Period end (DEC) - PKRbn	CY18A	CY19E	CY20P	CY21P	CY22P
Valuation					
P/E	5.579	5.94	5.20	5.03	4.91
P/B	2.1	2.06	2.00	1.92	1.83
Div. Yld %	15%	15.1%	17.9%	17.9%	17.9%
Payout Ratio	84%	90%	90%	90%	90%
Roe	39.6%	35.3%	39.0%	39.0%	38.3%
Roa	15.2%	13.6%	15.6%	17.1%	17.9%
Margins					
Gross Profit Margins	32.3%	34.6%	32.5%	32.0%	31.5%
Operating Profits Margins	23.6%	25.8%	23.9%	23.3%	22.6%
Ebit Margins	24.1%	27.4%	26.2%	25.0%	23.9%
Growth Rates					
Revenue	41.6%	-1.7%	3.7%	2.9%	4.0%
Ebitda	29%	32%	31%	29%	28%
Earning	56.1%	-6.0%	14.1%	3.4%	2.5%
Financial Ratios					
Debt/Equity	0.56	0.46	0.17	0.06	0.00
Interest Coverage	12.73	7.12	10.37	20.67	49.15
Current Ratio	1.15	1.10	0.88	0.83	0.85
Quick Ratio	1.01	0.95	0.73	0.67	0.68
Du-Pont Analysis					
Op. Profit Margin	24.1	27.4	26.2	25.0	23.9
Asset Turnover	1.0	0.9	0.9	1.0	1.1
Interest Expense Rate	1.80	3.42	2.35	1.22	0.52
Tax Retention	71.7	64.7	71.0	71.0	71.0
ROA	15.2	13.6	15.6	17.1	17.9
Equity Multiplier	2.61	2.60	2.50	2.28	2.14
ROE	39.6	35.3	39.0	39.0	38.3

SOURCE: IGI Research, Company accounts

Updated as of: 10-Jan-20

Fauji Fertilizer Company Limited (FFC)

We have a liking for FFC currently trading at forward P/E of 7.5x, offering at a discount of 12% from market P/E of 8.8x. The company is well placed in our fertilizer universe in terms of, strong pricing power, having largest share and diversification. Led by stable sector dynamics FFC has seen +14% (3yr CAGR) growth in earnings, which we expect to sustain (+5%) going forward in the next three years or so.

Investment thesis

- ✓ **Dominant market share-**FFC enjoys largest market share in the fertilizer sector, capturing 44% of the urea market. With 2.5mn tons of urea sales the company has maintained its dominance in the industry and is able to exercise its pricing power well (gradual price increases up to PKR~600/bag courtesy gas hikes and supply shortfall in 1HCY18). As such, the company's flagship product "Sona urea" is sold at relatively premium price. Amid stable urea demand to continue (~6mntons) we foresee FFC to sustain its share given supply from LNG- based fertilizer player's ceases.
- ✓ **GIDC matter-** With over PKR 42bn GIDC dues lined up the company is well poised to benefit (one off PKR 12/share) if the decision goes in favor. Alongside, the recurring impact from the reduction in the cess rate will be positive, PKR 5/share. However, we think this will be offset by a corresponding reduction in urea prices amidst another gas price hike and ongoing increase in inventory levels
- ✓ **Increased short term investments-**While the FFC's balance sheet is highly leveraged (1.3x D/E) the company has parked its accruals in short term investments, taking advantage of rising interest rates and partially absorbing its finance costs. Going forward with monetary easing around the corner, this may bode well in bringing down finance costs.
- ✓ **Diverse business portfolio-**FFC has heavily invested (PKR 27bn) in various sectors (banks, cements, energy and food), enjoying steady income stream, with the recent investment (PKR~ 2.0bn) made in Thar energy limited (30% stake). We expect stable income (+6% -3yr CAGR) from these portfolio to continue, contributing 14% to the earnings.

Recommendation

We have a liking for FFC based on our Dec-20 Target price of PKR 110/share, offering +8% upside from last close The company is currently trading at CY20E P/E of 7.3x at a dividend yield of 11%.

Key Risks

a) Increase in gas prices, b) Decrease in fertilizer prices, c) Increase in finance costs and d) high inventory levels from continuous operation of RLNG-based fertilizer plants

Fauji Fertilizer Company Limited (FFC)

Current Price (PKR):	103		Target Price (PKR):	110

Period end (DEC) - PKRmn	CY18A	CY19E	CY20P	CY21P	CY22P
Income Statement					
Net Sales	105,964	108,394	114,072	118,131	119,464
Gross Profit	27,979	32,692	31,655	32,259	32,492
Selling / Dist.	8,833	7,994	8,177	8,475	8,606
Operating Profits	19,145	24,698	23,478	23,784	23,886
Other Op. Income	6,283	6,222	5,729	5,739	5,458
EBIT	23,320	28,137	26,578	26,866	26,703
Finance Cost	1,637	4,149	2,574	2,364	2,103
Pre-Tax Profits	21,683	23,988	24,004	24,502	24,600
Taxation	7,244	6,642	6,555	6,697	6,724
Post-Tax Profits	14,439	17,347	17,449	17,805	17,876
Balance Sheet Items					
Non-Current Assets	51,135	51,650	51,641	51,633	51,624
Stores And Spares	3,474	4,344	4,554	4,716	4,769
Interest And Mark-Up Accrued	301	301	301	301	301
Current Assets	95,355	91,462	95,009	98,553	101,720
Total Assets	146,490	143,112	146,651	150,186	153,344
Non-Current Liabilities	12,872	8,703	6,803	5,666	5,853
Payables	18,516	15,690	15,806	16,469	16,680
Total Liabilities	113,107	108,939	109,034	109,040	108,597
Total Equity	33,383	34,172	37,617	41,146	44,747
Cashflow Items					
Operating Cash Flow	22,866	39,506	15,968	16,857	16,854
Investing Cash Flow	(21,108)	(1,544)	(2,079)	(2,078)	(2,077)
Financing Cash Flow	16,495	(35,272)	(13,888)	(14,778)	(14,776)
Closing Cash	3,818	3,818	3,818	3,818	3,818
Per share Data					
EPS	11.35	13.63	13.72	13.99	14.05
DPS	8.85	10.90	11.00	11.20	11.20
BVPS	26.2	26.86	29.58	32.37	35.22

Upside	8%		Recommendation	HOLD

Period end (DEC) - PKRbn	CY18A	CY19E	CY20P	CY21P	CY22P
Valuation					
P/E	8.797	7.27	7.34	7.20	7.17
P/B	3.8	3.72	3.38	3.09	2.84
Div. Yld %	9%	11.0%	10.9%	11.1%	11.1%
Payout Ratio	78%	80%	80%	80%	80%
ROE	46.0%	51.7%	48.2%	44.8%	41.3%
ROA	11.3%	12.1%	11.9%	11.9%	11.7%
Margins					
Gross Profit Margins	26.4%	30.3%	27.6%	27.2%	27.1%
Operating Profits Margins	18.1%	22.9%	20.4%	20.0%	19.8%
Ebitda Margins	24.0%	28.0%	25.0%	24.4%	24.0%
Growth Rates					
Revenue	16.8%	2.5%	4.9%	3.5%	1.1%
Ebitda	25%	20%	-6%	1%	-1%
Earning	34.8%	21.0%	-0.9%	2.0%	0.4%
Financial Ratios					
Debt/Equity	0.25	0.12	0.06	0.03	0.03
Interest Coverage	14.25	6.82	10.24	11.28	12.59
Current Ratio	0.95	0.91	0.93	0.95	0.99
Quick Ratio	0.92	0.87	0.88	0.91	0.94
Du-Pont Analysis					
Op. Profit Margin	22.0	26.1	23.2	22.6	22.2
Asset Turnover	0.8	0.7	0.8	0.8	0.8
Interest Expense Rate	1.28	2.87	1.78	1.59	1.39
Tax Retention	66.6	72.3	72.7	72.7	72.7
ROA	11.3	12.1	11.9	11.9	11.7
Equity Multiplier	4.07	4.29	4.04	3.77	3.53
ROE	46.0	51.7	48.2	44.8	41.3

SOURCE: IGI Research, Company accounts

Updated as of: 10-Jan-20

Market-weight

Oil & Gas Marketing Companies

Gradual recovery in volumes while reforms to act as a catalyst

We have a **'Market-weight'** stance on OMC sector on the back of pile up of receivables (we have not incorporated substantial recovery), rising competition, high prices and existence of grey-market will keep volumetric growth sub-par. Though earnings are expected to rise in Fy20 due to gradual rise in volumes (low base in Fy19) and absence of exchange losses, we highlight weak fundamentals and increased competition to keep sector earnings growth limited.

- ✓ **OMC margins to rise substantially as CPI jacks up** - CPI inflation for Fy20 is estimated to average 11-13% all risks incorporated. As a result, OMC margins are likely to witness an increase to PKR 3.06/ltr for MS and HSD each from current PKR 2.81/ltr. This will have an incremental EPS impact of PKR 4.3/3.5/0.6 on PSO/APL/HASCOL earnings.
- ✓ **Major contraction in volumes witnessed in Fy19, we expect recovery from Fy20 and onwards -** Volumes witnessed major contraction in Fy19 with total volumes down by 25%y/y (FO/HSD down 58%/20%) due to slowdown in aggregate demand, along with higher prices and existence of grey-market. However, from Fy20 and onwards we foresee a gradual recovery in volumes with supportive base of Fy19 and upturn in economy. We also see retail segment to drive volumes with MS leading the way while HSD volumes are likely to remain stable. However, for FO we expect volumes to further decline on account of lower FO generation in Fy20 but post that we estimate stability in volumes owing to drop in cost of generation on FO. As a result, we forecast +1%y/y growth in volumes in Fy20 with MS posting +7%y/y growth while FO dropping by 11%y/y.
- ✓ **Measures underway to address circular debt issue -** With another tranche of Sukuk-II in the pipeline we highlight PSO to remain prime beneficiary of another PKR 200bn payment injection. PSO received PKR 60bn from first tranche and another PKR 45-50bn are expected to be received from second tranche. As a result, PSO's receivable from power sector are likely to go down to PKR 50-55bn from PKR 101bn as at Oct-19. Thus PSO's ST borrowings are also likely to come down. However, we foresee limited increase in cash payout as PSO is likely to utilize the cash for investment in PRL. Furthermore, pile up in LNG receivable have also been a concern reaching nearly PKR 60bn while circular debt although at slow pace is still accumulating. Thus, effectiveness of reform measures remains key in addressing circular debt issue.

Earnings and Valuation: We estimate IGI OMC sector to post healthy growth in earnings in Fy20 owing to absence of hefty exchange losses and recovery in volumes. PSO is likely to lead earnings growth with +24%y/y growth in EPS in Fy20 with 3yr CAGR of +18%. HASCOL's earnings are likely to recover in 2020 due to hefty exchange losses booked in 2019, however still likely to remain in losses.

Top picks and recommendation: We maintain our preference for PSO considering recovery of over dues through Sukuk and power sector reforms, stability in margins post drop in FO quantum and increase in MS storage through conversion of existing FO.

Key Risks: a) Delays in notification of margin increase, b) GoP failure to arrest grey market, c) Exchange rate and oil prices volatility, d) Rise in circular debt.

Sym	Recomm.	TP (PKR)	3yr EPS CAGR	EPS			DPS			P/E			D/Y			P/B			ROE		
				19	20	21	19	20	21	19	20	21	19	20	21	19	20	21	19	20	21
PSO	BUY	257	18%	22.5	28.0	32.8	10.0	10.0	12.0	9.5	7.7	6.5	4.7	4.7	5.6	0.8	0.8	0.7	9.2	10.6	11.6
APL	NEUTRAL	420	2%	39.8	39.1	41.6	20.0	35.0	40.0	9.6	9.8	9.2	5.2	9.1	10.5	2.0	2.0	2.0	21.2	20.3	21.3
HASCOL	BUY	31	-136%	(12.6)	(1.9)	(0.8)	-	-	-	(2.1)	(14.4)	(35.5)				38.3	3.9	4.4	(189.7)	(49.6)	(11.7)
Oi & Gas Marketing			**122%**							**81.2**	**10.9**	**8.8**	**2.2**	**3.5**	**4.0**	**0.3**	**0.3**	**0.3**	**1.5**	**10.3**	**11.8**

Pakistan State Oil Company Limited (PSO)

We base our investment case on a 3yr profitability CAGR of +18% over Fy20-22. Furthermore, with reforms in power sector and Sukuk issue we highlight PSO to benefit the most.

Investment thesis

- ✓ **Earnings to accrete at 3yr CAGR of 18%-** We foresee PSO to post a 3yr CAGR of +18% in earnings from Fy20-22F on the back of a) expansion in retail outlets and storage facility to keep retail segment growth healthy, b) recovery in HSD sales, c) Sukuk-II issue likely to further ease cash constraints for PSO and, d) lower exchange losses amid stable PKR.
- ✓ **Energy Sukuk-II to further ease cash constraints**- As another tranche of PKR 200bn Sukuk is in the pipeline we highlight PSO to benefit most as it would further improve cash position for PSO. PSO receivables are down to PKR 101bn from power sector in Oct-19 compared to PKR 200bn as at Jun-18. A lower working capital requirement would allow for capex in PRL and lower short term borrowings thus making a case for re-rating of the stock.
- ✓ **Total volumes to grow by +7%y/y in Fy20-** We expect recovery in volumes for PSO which is already visible in 1HFy20 numbers posting +9%y/y growth already. PSO is expected to post +11%/5%y/y growth in MS and HSD volumes in Fy20 thus regaining market share at 39%/43%.
- ✓ **Higher inflation to support retail margins-** CPI is expected to clock in at 11%/9% for Fy20/21F which would allow for a healthy increase in OMC margins for MS and HSD. This would likely offset any substantial decline in FO margins due to IMO-2020 restrictions hurting FO demand and local discounts by refineries. MS and HSD gross profit contribution is expected to increase to 63% in Fy21 from 53% in Fy19.
- ✓ **LNG business continues to be earnings driver-** We expect LNG business to continue till Fy23 where LNG income is expected to contribute nearly 15-17% to gross profit. However, with recent pile up of LNG receivables to PKR 58bn, we expect LNG over dues to come down post gas tariff hike for gas companies.

Recommendation: We value PSO stock on discounted cash flow model, giving a Dec-20 target price of PKR 257.14/share (20% upside). The company is currently trading at Fy20E P/E of 7.7x and offers a dividend yield of 4.7%.

Key Risks: a) Increased competition leading to further decline in market share, b) Power sector reforms yielding less than expected return and delay in Sukuk issue to further deteriorate cash position, c) Delays in margin revision and d) Substantial pile up in LNG receivables.

Pakistan State Oil Company Limited (PSO)

Current Price (PKR):	215	Target Price (PKR):	257	Upside	20%	Recommendation:	BUY

Period end (Jun) - PKRbn	FY18A	FY19A	FY20F	FY21F	FY22F
Income Statement Items					
Net Sales	1,056.9	1,154.3	1,229.1	913.1	971.9
Gross Profit	39.6	36.0	39.1	40.4	45.0
Selling & Distr. Expense	9.2	9.9	10.1	10.6	11.3
Admin Expense	2.8	2.5	2.6	2.8	3.0
Other Income	7.5	7.3	7.6	5.9	6.1
EBIT	31.9	26.2	30.2	28.9	32.6
Finance Costs	5.1	8.9	8.6	6.3	6.2
Pre-tax Profits	27.2	17.5	21.9	22.8	26.7
Post- Tax Profits	15.5	10.6	13.1	15.4	17.6
Balance Sheet Items					
PPE	7.3	8.2	11.1	15.8	19.2
LT Invest.	4.8	11.4	12.0	15.6	12.5
Non Current Assets	24.5	32.9	36.7	48.9	42.6
Inventory	81.6	89.7	81.5	57.4	60.9
Trade debts	245.6	219.6	206.0	171.9	180.8
Total Assets	402.6	417.1	405.8	371.0	381.1
Payables	195.8	181.9	177.2	154.1	149.1
Current Liab.	286.9	290.4	269.2	224.4	222.9
LT Debt	-	-	-	-	-
Non Current Liab.	5.2	7.5	8.3	8.7	9.1
Total Liab.	292.1	297.9	277.5	233.1	232.0
Share Capital	3.3	3.9	4.7	4.7	4.7
Total Equity	110.5	119.2	128.2	137.9	149.0
Cash Flow Items (PKRbn)					
Operating CF	10.1	(8.4)	27.8	43.9	(7.2)
Investing CF	41.9	(9.3)	(5.1)	(13.5)	4.7
Financing CF	(47.9)	16.2	(19.6)	(27.2)	(2.5)
Cash	4.6	4.6	7.7	11.0	5.9
Per Share					
EPS	32.9	22.5	28.0	32.8	37.5
DPS	15.0	10.0	10.3	12.1	13.9
BV	338.8	304.6	273.2	293.8	317.5
Cash	14.2	11.7	16.3	23.4	12.5

Period end (Jun) - PKRbn	FY18A	FY19A	FY20F	FY21F	FY22F
Valuation					
P/E (x)	6.5	9.5	7.7	6.5	5.7
P/EBITDA (x)	0.3	0.4	0.3	0.3	0.3
D/Y (%)	7.0	4.7	4.8	5.6	6.5
P/B (x)	0.6	0.7	0.8	0.7	0.7
ROE (%)	14.50	9.22	10.61	11.57	12.26
ROA (%)	3.89	2.58	3.19	3.96	4.68
Margins					
Gross Margins (%)	3.8	3.1	3.2	4.4	4.6
EBIT Margin (%)	3.0	2.3	2.5	3.2	3.4
Net Profit Margins (%)	1.5	0.9	1.1	1.7	1.8
Financial Gearing					
Total Debt / Equity (%)	-	-	-	-	-
Interest Coverage	6.2	2.9	3.5	4.6	5.3
Efficiency Ratios					
Current Ratio	1.3	1.3	1.4	1.4	1.5
Quick Ratio	1.0	1.0	1.1	1.2	1.2
Cash Cycle					
Cash Cycle	43.8	39.9	35.0	29.0	34.0
Inventory Days	26.5	28.0	25.0	24.0	24.0
Receivable Days	79.1	73.5	90.0	70.0	70.0
Payable Days	61.9	61.6	80.0	65.0	60.0
Volumes (mn'tons)					
Total Sales	12.44	.75	8.35	8.75	9.25
MS	2.90	2.76	3.08	3.38	3.82
HSD	3.85	2.86	3.00	3.13	3.22
FO	4.85	1.49	1.49	1.41	1.38
Market Share (%)					
Total	51%	42%	45%	45%	45%
MS	40%	37%	39%	39%	40%
HSD	43%	40%	43%	43%	43%
FO	68%	49%	55%	55%	55%

Source: IGI Research, Company Financials

Updated as of: 10-Jan-20

Under-weight

Automobile Assemblers

Demand recovery looks slightly slow; near-term outlook remains muted

We maintain **'Under-weight'** stance on Automobile assemblers, as we believe subdued demand may keep volumetric growth restricted. Although, interest rate reversal seems a likely scenario in the next six months or so, we believe the worst in terms of sales volume is still looming. A sustainable growth recovery still seems some time away as ongoing macro weakness subsides.

- ✓ **Depressed sales environment to continue in the medium term** - We eye a modest upturn in sales for our auto universe during the latter half of Fy21 (+6%) onwards as impact of economic upturn may slightly trigger demand. In parallel with previous episodes of slowdown witnessed in the years 2008 and 2013 wherein contractionary phase lasted for ~2yrs we base our expectations for the year 2020 (14% decline) in-line with this trend. With that said, we think consumer's shift in demand for 1000cc segment seems a possibility (36% share FY20TD in passenger car category as against 26% same period last year).
- ✓ **Earnings to come under margin pressure, low volumes and other income** - Slowdown in sales may weigh on earnings, depicting a cyclical downturn (~60%y/y) during 2020. Although, volatility in exchange rate has subsided, a positive sign indeed, we believe margins may remain subdued (~200bps drop) as under unutilized capacity (raising fixed cost/unit) and declining volumes may erode gross profits. More so, for cash rich companies (INDU and HCAR) support to other income may also restrain with ~60% drop in short term investments.
- ✓ **Competition sinks in diverse segments; 1000cc segment a key focus** - The current year has seen new launches by foreign entrants, with LCVs, SUVs and passenger car (1000cc) segment being the prime market. By far the focus of new entrants have moved away from sedan segment (1300<x<1800cc), where HCAR and INDU dominates. We therefore don't expect any major impact on their sales volumes. On the flip side, for PSMC sales volumes would rather be critical in the 1000cc range as on-going launches grabs this market (e.g. KIA launching Picanto at roughly the same price points) gradually.

Earnings and Valuation: We estimate sector to witness ~60%y/y drop in earnings in Fy20, owing to volumetric decline stemming from subdued demand. On individual basis, we expect 70% decline in HCAR earnings and 60% drop in INDUs. While for PSMC we see losses to continue in CY20 as well.

Top picks and recommendation: We maintain INDU as our top pick based on high upside and rapid earnings recovery following contractionary phase. The company's relatively strong cash generation, premium pricing power and flagship product warrants a bullish stance

Key Risks: a) PKR depreciation against USD and JPY, b) Increase in international CRC prices, c) Increase in FED and custom duties, and d) Foreign competition

Sym	Recomm.	TP (PKR)	3yr EPS CAGR	EPS			DPS			P/E			D/Y			P/B			ROE		
				19	20	21	19	20	21	19	20	21	19	20	21	19	20	21	19	20	21
INDU	BUY	1403	-10%	174.5	85.6	109.3	108.0	56.4	72.1	6.0	12.3	9.6	10.3	5.4	6.9	2.1	1.8	1.7	35.7	15.7	18.2
HCAR	NEUTRAL	196	-23%	27.0	7.1	11.1	12.2	3.2	5.1	7.9	30.0	19.1	5.7	1.5	2.4	1.7	1.7	1.6	22.2	5.6	8.5
PSMC	SELL	181	-146%	(37.4)	(19.9)	2.2	-	-	-	(6.1)	(11.4)	105.0				0.6	0.5	0.5	(10.0)	(4.9)	0.5
Automobile & Assembler			**-6%**							**9.1**	**21.6**	**12.7**	**7.8**	**3.7**	**4.9**	**4.7**	**4.3**	**4.1**	**16.7**	**6.5**	**10.3**

Indus Motor Company Limited (INDU)

Amongst our coverage companies we have liking for INDU. The company's relatively strong cash generation, premium pricing power and flagship product warrants a bullish stance. We are of the view that a decline in earnings trajectory in the medium term may keep stock in check. The stock is currently trading at P/E 12.2x, offering +35% upside.

Investment thesis

- ✓ **Possible launch underway-** Talks are in the air for a new launch (either Vios/Yaris) in the market, a replacement for 1,300cc Corolla (expected to discontinue). While demand is weak and uncertainty looms, we think company is eyeing a feasible time to come up with the launch once the dust settles.
- ✓ **Strong market share in sedan segment-**In terms of market share, INDU has maintained its share at 27% (avg.), compared to its closest peer HCAR (19%). Although Fy18 saw a dip, Fy19 ended with company regaining back its share, thanks to healthy sales of Corolla. Looking at the sales number, we see consumer preference for Corolla remained tied despite 30 %y/y (avg.) increase in prices (price-passover from PKR depreciation), signifying pricing power.
- ✓ **Excess liquidity relative to its peers-**With respect to liquidity INDU is better placed, having excessive cash tied up in investments (PKR ~300/share), taking advantage of rising interest rates helping in lifting profitability. However, for the sector itself, liquidity has to turned to a be a concern with OEMs availing short term financing, INDU in this regard is relatively safe, despite drop in advances and short term investments.
- ✓ **Decline in earnings to continues in Fy20-** The start of the quarter Fy20, has been bleak (~60% drop in earnings) as the impact of declining volumes (60%y/y) translated. The Fy20 may rather be challenging for INDU compared to Fy19 as we expect earning erosion and faltering demand to persist. However, post Fy21 recovery in sales, albeit slow (+10%), may drive earnings (est. ~30%).

Recommendation: We maintain INDU as our top pick with our Dec-20 Target price of PKR 1403/share, offering +34% upside from last close. The company is currently trading at Fy20E P/E of 13.2x at a dividend yield of 5.0%

Key Risks: a) PKR depreciation against USD and JPY, b) Increase in international CRC prices, c) Increase in duties (FED and custom) and d) Foreign competition in sedan segment

Indus Motor Company Limited (INDU)

Current Price (PKR):		**1,050**	Target Price (PKR):	**1,403**
Period end (JUN) - PKRmn	FY18A	FY19A	FY20E	FY21F	FY22F

Period end (JUN) - PKRmn	FY18A	FY19A	FY20E	FY21F	FY22F
Income Items					
Net Sales	139,715	157,996	105,592	125,505	136,297
Gross Profit	23,885	19,192	10,011	13,577	15,626
Admin.	1,524	1,410	1,159	1,300	1,419
Dist. & Admin.	2,808	2,814	2,348	2,685	2,915
Other Income	3,901	4,307	2,677	2,330	2,736
EBITDA	24,971	21,134	13,524	16,540	18,638
EBIT	23,079	19,043	9,529	12,103	14,154
Profit Before Tax	22,999	18,976	9,471	12,103	14,154
Tax	7,227	5,261	2,747	3,510	4,105
Profit After Tax	15,772	13,715	6,725	8,593	10,049
Balance Sheet Items					
Fixed Assets	7,225	13,805	15,331	15,493	14,108
Stock In Trade	11,151	13,560	10,475	12,266	9,918
Trade Debts / Accrued Returns	1,574	2,583	1,402	1,666	1,809
Current Assets	74,543	50,858	42,817	51,109	62,470
Total Assets	81,928	64,783	58,263	66,716	76,692
Trade And Payables	15,731	15,950	8,820	10,360	12,585
Total Liabilities	45,183	24,738	12,433	17,957	24,508
Paid Up Capital	786	786	786	786	786
Total Equity	36,744	40,045	45,830	48,759	52,185
Cashflow Items					
Operating Cashflow	25,487	(12,090)	2,978	16,426	23,249
Investing Cashflow	(16,382)	23,003	(1,258)	(10,762)	(16,625)
Financing Cashflow	(11,004)	(8,503)	(4,567)	(5,664)	(6,624)
Closing Cash	2,201	3,282	3,930	3,930	3,930
Per Share Data					
EPS (diluted)	200.7	174.5	85.6	109.3	127.9
DPS	140.0	108.0	56.4	72.1	84.3
BVPS	467.5	509.5	583.1	620.3	663.9

Upside	**34%**		Recommendation	**BUY**	
Period end (JUN)	FY18A	FY19A	FY20E	FY21F	FY22F
Valuation					
P/E (X)	5.6	6.5	13.2	10.3	8.8
P/B (X)	2.4	2.2	1.9	1.8	1.7
Div. Yld (%)	12.4	9.6	5.0	6.4	7.5
ROE	44.3	44.2	46.4	35.7	15.7
ROA	21.2	21.4	21.6	18.7	10.9
EV/EBITDA (x)	1.7	2.9	2.6	2.8	3.4
Margins					
Gross Profit	17.1	12.1	9.5	10.8	11.5
EBITDA	17.9	13.4	12.8	13.2	13.7
EBIT	16.5	12.1	9.0	9.6	10.4
Net Profit	11.3	8.7	6.4	6.8	7.4
Growth Rates					
Revenue	12.7%	3.2%	24.4%	13.1%	-33.2%
EBIT	23.2%	11.8%	18.1%	-17.5%	-50.0%
Earnings	25.7%	13.6%	21.3%	-13.0%	-51.0%
Financial Ratios					
Current Ratio	1.7	2.1	3.6	2.9	2.6
Quick Ratio	1.4	1.4	2.6	2.1	2.1
Du-Pont Analysis					
Op. Profit Margin	16.5	12.1	9.0	9.6	10.4
Asset Turnover	1.9	2.2	1.7	2.0	1.9
Interest Expense Rate	0.1	0.1	0.1	-	-
Tax Retention	68.6	72.3	71.0	71.0	71.0
ROA	21.6	18.7	10.9	13.8	14.0
Equity Multiplier	2.1	1.9	1.4	1.3	1.4
ROE	46.4	35.7	15.7	18.2	19.9

SOURCE: IGI Research, Company accounts

Updated as of: *10-Jan-20*

Under-weight

Cements

Economic contraction to present net losses for sector; strong recovery expected post FY21

We continue our underweight stance on cement sector despite the recent rally witnessed. We draw our stance on the back of anticipated poor earnings display for FY20 followed with shallow performance in FY21. The government's efforts of placing structural reforms has infect brought the economy in a pullback phase making overall atmosphere for the construction sector quite negative. While reforms have gradually started to bear fruits with deficits coming under control, the economy is expected to remain in a contractionary phase for the coming year.

- ✓ **Demand to remain steady, albeit excess supply to pose threat on prices, especially in North**-Though, enhanced earmarking of PSDP funds is anticipated to keep local dispatches steady, the recently available unutilized expansion capacities (LUCK, PIOC and KOHC also awaited) will keep prices on the lower side and dealer discounts on the higher side, thus severely hurting sector gross margins. Accordingly, average gross margins of the sector are expected to decline to 7% in Fy20 as against 22% recorded in Fy19.
- ✓ **Export to generate better proceeds than local**-Substantially weakened currency and intense competition in the domestic market are expected to exhibit superior retentions in the export market for CY20. This is against the historic norm, where despite a healthy duty and tax structure on domestic offtakes, local retentions have always been dominant. With this in mind, South players stand at a relative advantage given North region has limited export avenues.
- ✓ **Finance costs to present net losses in Fy20 and erode profitability in Fy21**-Highly leveraged on account of the recent expansion spree coupled with double digit benchmark interest rates, finance costs are to hit a heavy blow to earnings in the next couple of years. With gross margins already benign in Fy20, impact of heavy finance cost is expected to present net losses for Fy20 and also eat away substantial profitability in Fy21.

Earnings and Valuation: Worst financial performance is expected to be witnessed in FY20, wherein we expect IGI cement coverage to present heavy losses, followed up with sublime profits in FY21 driven largely by economic contraction, heavy finance costs and intense competition. However with macro outlook improving gradually, we expect sector performance to rebound strongly post FY21 owing to jacked up demand, improved margins and lowered finance costs.

Top picks and recommendation: While traditional blue chips such as LUCK and DGKC remain out of favor, our focus remains on FCCL and KOHC due to availability of upside opportunity whereas ACPL, PIOC and MLCF stand as our growth pullers.

Key Risks: Substantial decline in cement sales prices, b) PKR depreciation and c) Volatility in global coal prices

Sym	Recomm.	TP (PKR)	3yr EPS CAGR	EPS			DPS			P/E			D/Y			P/B			ROE		
				19	20	21	19	20	21	19	20	21	19	20	21	19	20	21	19	20	21
ACPL	BUY	160	8%	15.1	11.2	14.9	4.0	4.0	7.5	6.8	9.2	6.9	3.9	3.9	7.3	0.9	0.8	0.8	13.4	9.3	11.5
CHCC	NEUTRAL	56	-51%	9.1	(10.9)	(8.2)	1.0	-	-	5.8	(4.8)	(6.4)	1.9			0.9	1.1	1.3	15.4	(19.8)	(18.0)
DGKC	NEUTRAL	75	-5%	3.7	(13.5)	(6.1)	1.0	-	-	20.9	(5.7)	(12.5)	1.3			0.5	0.5	0.5	2.2	(8.7)	(4.2)
FCCL	BUY	22	-2%	2.0	1.2	1.2	1.5	1.0	1.0	8.4	14.6	14.1	8.7	5.8	5.8	1.1	1.2	1.1	13.6	7.9	8.2
KOHC	BUY	154	9%	12.3	4.6	9.7	2.5	1.0	2.0	6.2	16.5	7.9	3.3	1.3	2.6	0.8	0.8	0.7	13.1	4.7	9.2
MLCF	BUY	32	-13%	4.1	(4.6)	(0.5)	0.5	-	-	5.5	(4.9)	(43.0)	2.2			0.4	0.4	0.4	8.1	(8.8)	(1.0)
PIOC	BUY	72	-13%	3.5	(6.5)	(4.6)	-	-	-	8.6	(4.6)	(6.6)				0.5	0.6	0.6	5.9	(11.7)	(9.2)
LUCK	NEUTRAL	462	-12%	32.4	10.9	14.5	6.5	2.5	3.0	15.2	45.4	34.1	1.3	0.5	0.6	1.7	1.7	1.6	11.6	3.7	4.8
Cements			**-8%**							**11.3**	**(59.6)**	**58.7**	**0.0**	**0.0**	**0.0**	**0.3**	**0.3**	**0.3**	**8.9**	**(1.7)**	**1.7**

Fauji Cement Company Limited (FCCL)

Our investment case on the scrip is premised on healthy balance sheet with consistent cash pay-out and cheaper valuation multiples. Though decline in FCCL's FY20 profitability is clearly evident, due to the current unfavorable cement atmosphere where in major players are expected to present losses, it ranks the second best with respect to percentage drop in earnings thanks to its debt free balance sheet in such challenging times. However, post FY20, the scrip is expected to present a strong recovery with a 3Yr earnings CAGR of 32%. The scrip also pays consistent heavy payouts (70-80%) and the possibility of coming up with an expansion lately further corroborates our liking.

Investment thesis

- ✓ **Debt free balance sheet to protect against tough economic headwinds:** While not coming up with an expansion may reduce FCCL's domestic foot print, this has also kept the Company's books almost debt free, making it an economically viable company in the current fiercely competitive cement market, especially in the North region, where domestic retention prices have gone down to new lows. Where our average companies hold an average finance cost of PKR 24/bag (including LUCK), FCCL's cost comes to less than PKR 2/bag, providing it with better profitability prospects in a situation where major producers are expected to display losses or minimal profits.
- ✓ **FCCL always brings expansion at the end of the cycle; will recover its lost market share-** FCCL has always been a laid back in entering the expansion cycle, waiting cautiously for intense competition post expansion to settle out before coming up with its own plans in a pro-business environment. Similarly, by not entering the current cycle as of now, FCCL's market share is expected to decline to ~7.2% as against 8.7% achieved in FY19. However, we believe this won't hurt FCCL much as explained above. Albeit, while we have not yet incorporated any expansion plans for FCCL in our estimates, we strongly believe based on the Company's past practice that it will come up with an expansion lately to recover it lost share, thus making it more attractive for our investors.
- ✓ **Consistent dividend pay-out history of ~80% an eye candy for investors-**FCCL has a history of paying high cash dividends of around 70 - 80% (pay-out) to its equity holders. This practice was even held in FY19 wherein majority of cement players shied away from paying out taking advantage of relaxed income tax ordinance rules. Accordingly, we believe FCCL is to continue its high pay-out policy going forward providing its investors further candy.

Recommendation: We present a Buy call on FCCL with a Dec-20 target price of PKR 22/share, offering a 30% upside from last close, which is in addition to 5.8% dividend yield for FY20, taking total return to around 36%.

Key Risks: a) Decrease in cement sales prices, b) Administrative increase in energy prices and c) Substantial rise in coal prices

Fauji Cement Company Limited (FCCL)

Current Price (PKR):	17	Target Price (PKR):		22		Upside	30%		Recommendation		BUY
Period end (JUN) - PKRbn	FY18A	FY19E	FY20F	FY21F	FY22F	Period end (JUN)	FY18A	FY19E	FY20F	FY21F	FY22F
Income Statement Items						**Per Share Data**					
Net Sales	21,161	20,798	18,244	17,860	19,904	EPS	2.5	2.0	1.2	1.2	1.9
Gross Profit	5,115	5,323	2,995	3,018	4,346	BV	14.8	15.1	14.8	15.0	16.0
Sell. / Dist. & Admin	583	626	655	710	769	DPS	2.0	1.5	1.0	1.0	1.5
Operating Profit	4,531	4,697	2,340	2,308	3,577	Cash & Equivalents	0.4	0.3	0.7	1.6	3.0
EBIT	4,324	4,519	2,315	2,321	3,607	**Valuation**					
Dep. & Amt.	1,417	1,520	1,564	1,493	1,429	P/E (X)	6.8	8.4	14.6	14.1	9.0
EBITDA	5,741	6,039	3,879	3,815	5,036	P/B (X)	1.2	1.1	1.2	1.1	1.1
Financial Charges	148	107	96	35	16	Div. Yld (%)	11.7	8.7	5.8	5.8	8.7
Pre-tax Profits	4,176	4,412	2,219	2,286	3,592	Earnings growth (%)	34.2	(19.5)	(42.4)	3.3	57.0
Taxation	669	1,588	593	606	955	EBITDA growth (%)	6.3	5.2	(35.8)	(1.7)	32.0
Post-tax Profits	3,508	2,824	1,626	1,680	2,636	ROE (%)	17.1	13.5	7.9	8.1	12.0
Balance Sheet Items						**Margins**					
PPE	22,624	23,203	21,852	20,905	19,998	Gross Margins (%)	24.2	25.6	16.4	16.9	21.8
LT Invest.	-	-	-	-	-	EBITDA Margin (%)	27.1	29.0	21.3	21.4	25.3
Inventory	1,245	944	1,012	985	1,033	Net Profit Margins (%)	16.6	13.6	8.9	9.4	13.2
Receivables	1,168	947	798	782	871	**Financial Gearing**					
ST-invest.	-	-	277	1,462	3,453	Debt / Equity (%)	13	8	2	1	-
Current Assets	6,338	5,676	5,421	6,389	8,563	Interest Coverage	29	42	24	66	233
Total Assets	29,049	28,965	27,359	27,380	28,648	**Efficiency Ratios**					
ST-Borrowings & CP of LT Loans	2,065	1,309	212	106	-	Current Ratio	1.5	1.5	1.9	2.4	3.2
Other Current Liab.	2,194	2,443	2,590	2,523	2,640	Quick Ratio	0.5	0.4	0.7	1.2	2.0
LT Loans	637	318	106	-	-	**Volumes (mn tons)**					
Other Non-Current Liab.	3,665	3,997	3,997	3,997	3,997	Local	3.1	2.8	2.7	2.5	2.6
Share Capital	13,798	13,798	13,798	13,798	13,798	Exports	0.3	0.2	0.3	0.3	0.3
Total Equity	20,489	20,899	20,455	20,754	22,011	Total Capacity	3.6	3.6	3.6	3.6	3.6
Cash flow Items						Capacity Utilization	96	85	84	79	82
Operating	4,526	5,128	4,155	3,323	3,999	**Macro - Assumption**					
Investing	(2,038)	(2,099)	(489)	(1,732)	(2,514)	Cement Price/bag	553	549	592	600	618
Financing	(1,016)	(3,502)	(3,379)	(1,592)	(1,486)	Coal	93	88	68	70	70
Cash	532	403	690	690	690	PKR/USD	110	136	153	158	161

SOURCE: IGI Research, Company Accounts

Kohat Cement Company Limited (KOHC)

We build our investment case on healthy balance sheet and strong earnings growth outlook. Though decline in KOHC's FY20 profitability is certain (down by 62%YoY), due to the current unfavorable cement atmosphere where in major players are expected to present losses, however post FY20 we expect the stock to display 3Yr earnings CAGR of around 67%. Earnings growth stems from enhanced market share post expansion and marginal finance costs as compared to peers in an all-time high interest rate environment.

Investment thesis

- ✓ **KOHC to increase market share post commencement of expansion plant:** With the new expansion plant expected to commence in 3QFY20, KOHC is all set to enhance its domestic market share in North to 8.7% as against 6.9% recorded in FY19. With economic recovery bound to pick up cement sector, enhanced market share will translate into substantial earnings growth. Accordingly, we expect KOHC earnings to display 3 Yrs earnings CAGR of 67% post FY20.
- ✓ **Debt free balance sheet to protect against tough economic headwinds:** With minimum debt financing obtained to come up with the new expansion plant, KOHC's balance sheet is less leveraged as compared to other competitors making it an economically viable company also in the current fiercely competitive cement market, especially in the North region, where domestic retention prices have gone down to new lows. Where our average companies hold an average finance cost of PKR 24/bag (including LUCK), KOHC's cost comes to less than PKR 7/bag, providing it better profitability prospects in a situation where major producers are expected to display losses or minimal profits.

Recommendation: We present a Buy call on KOHC with a Dec-20 target price of PKR 154/share, offering a 102% upside from last close.

Key Risks: a) Decrease in cement sales prices, b) Administrative increase in energy prices, c) substantial rise in coal prices and d) Significant PKR depreciation against USD

Kohat Cement Company Limited (KOHC)

Current Price (PKR):	76		Target Price (PKR):	154	Upside	102%		Recommendation		BUY

Period end (JUN) - PKRbn	FY18A	FY19E	FY20F	FY21F	FY22F
Income Statement Items					
Net Sales	13,439	15,646	14,411	18,082	20,514
Gross Profit	4,325	4,206	1,928	3,687	5,259
Sell. / Dist. & Admin	300	372	440	494	541
Operating Profit	4,025	3,834	1,489	3,193	4,718
EBIT	4,077	3,722	1,654	3,044	4,517
Dep. & Amt.	522	585	1,049	1,498	1,471
EBITDA	4,599	4,307	2,703	4,542	5,988
Financial Charges	107	46	362	335	105
Pre-tax Profits	3,970	3,676	1,292	2,709	4,412
Taxation	990	1,207	366	770	1,256
Post-tax Profits	2,980	2,469	926	1,938	3,156
Balance Sheet Items					
PPE	9,113	21,874	22,029	20,862	19,703
LT Invest.	3,656	3,692	3,692	3,692	3,692
Inventory	659	709	977	1,065	1,045
Receivables	646	714	586	594	562
ST-invest.	5,160	1,947	170	1,013	2,532
Current Assets	10,407	5,606	4,347	5,700	7,441
Total Assets	23,316	31,315	30,211	30,396	30,979
ST-Borrowings & CP of LT Loans	284	1,247	708	407	-
Other Current Liab.	3,395	4,277	4,751	5,011	4,672
LT Loans	142	4,400	2,937	1,425	-
Other Non-Current Liab.	1,518	1,718	1,718	1,718	1,718
Share Capital	1,545	2,009	2,009	2,009	2,009
Total Equity	17,977	19,673	20,096	21,834	24,588
Cashflow Items					
Operating	3,389	5,034	2,100	3,188	4,067
Investing	(2,109)	(10,172)	573	(1,173)	(1,833)
Financing	(2,805)	4,648	(2,504)	(2,014)	(2,234)
Cash	824	434	603	603	603

Period end (JUN)	FY18A	FY19E	FY20F	FY21F	FY22F
Per Share Data					
EPS	14.8	12.3	4.6	9.7	15.7
BV	89.5	97.9	100.1	108.7	122.4
DPS	5.0	2.5	1.0	2.0	4.0
Cash & Equivalents	29.8	11.9	3.8	8.0	15.6
Valuation					
P/E (X)	5.1	6.2	16.5	7.9	4.9
P/B (X)	0.9	0.8	0.8	0.7	0.6
Div. Yld (%)	6.6	3.3	1.3	2.6	5.2
Earnings growth (%)	(15.9)	(17.2)	(62.5)	109.4	62.8
EBITDA growth (%)	(23.6)	(6.3)	(37.2)	68.0	31.8
ROE (%)	16.6	12.5	4.6	8.9	12.8
Margins					
Gross Margins (%)	32.2	26.9	13.4	20.4	25.6
EBITDA Margin (%)	34.2	27.5	18.8	25.1	29.2
Net Profit Margins (%)	22.2	15.8	6.4	10.7	15.4
Financial Gearing					
Debt / Equity (%)	2	29	18	8	-
Interest Coverage	38	81	5	9	43
Efficiency Ratios					
Current Ratio	2.8	1.0	0.8	1.1	1.6
Quick Ratio	2.1	0.6	0.3	0.5	0.9
Volumes (mn tons)					
Local	2.1	2.2	2.5	3.0	3.1
Exports	0.1	0.1	0.1	0.1	0.1
Total Capacity	3.0	3.0	4.1	5.3	5.3
Capacity Utilization	76	80	64	59	60
Macro - Assumption					
Cement Price/bag	553	549	592	600	618
Coal	93	88	68	70	70
PKR/USD	110	136	153	158	161

SOURCE: IGI Research, Company Accounts

Under-weight

Steel

Economic pressure to heavily weigh down sector

We remain **'Under-weight'** on Pakistan Steels in 2020. Sector earnings performance are expected to decline on the back of receding gross margins and incurrence of high-end finance costs.

- ✓ **Poor economic factors to hamper demand and pricing power till 1HFy21**- With the country currently undergoing economic contraction, we expect overall demand of steel products to remain rather sluggish in Fy20, with pickup expected by second half of Fy21. Though, tightening the noose of undocumented sectors through introduction of heavy taxation would lead to closure of many small unregistered steel players, thus providing room for big players to capture the share of grey market. However, pricing power would be limited given high-end rise in input prices and poor purchasing power of consumers, thereby expecting decent margins as compared to highs of previous years.
- ✓ **Administrative hike in energy prices to further depress margins**- While substantial depreciation of PKR has caused much damage to margins and price pass over ability of steel producers, significant devaluation of similar quantum is least expected to occur going forward. However, with the steel sector being an energy intensive sector, the recent OGRA approved 31% (third of similar quantum in the last 1 year) hike in domestic gas prices may add further worries to gross margins, if it gets the nod from the federal government.
- ✓ **Reversal of Monetary cycle to support net margins –** With interest rates having already peaked out at 13.25%, reversal in interest rate cycle is very much anticipated. Expected to begin from Mar this year, it appears the SBP might pull off a cumulative decline of 200bps in benchmark rates by CY20, providing much needed earnings breather to an already heavily leveraged sector.

Earnings and Valuation: Earnings for IGI steel coverage dropped by a massive 55%y/y in Fy19 led by substantial rise in input costs driven majorly by heavily depreciated PKR and incurrence of hefty finance cost post expansion capex. Poor financial performance is expected to follow in Fy20, wherein we expect our coverage companies earnings to decline further by 54%y/y, however post Fy20 we expect earnings to recover strongly with a 3Yr earnings CAGR of 34% led by higher demand, gross margins recovery and decline in finance costs due to repayments and down trending interest rates.

Top picks and recommendation: The recent rally in our coverage companies have exhausted upside opportunities, with the exception of ISL only.

Key Risks: Global steel prices and b) PKR depreciation against USD

Sym	Recomm.	TP (PKR)	3yr EPS CAGR	EPS			DPS			P/E			D/Y			P/B			ROE		
				19	20	21	19	20	21	19	20	21	19	20	21	19	20	21	19	20	21
ISL	BUY	72	18%	6.1	3.6	7.2	3.0	1.5	2.8	9.4	15.8	8.0	5.2	2.6	4.8	1.9	1.9	1.6	21.6	12.2	21.7
ASTL	NEUTRAL	40	288%	0.1	(1.1)	1.7	-	-	0.8	336.5	(34.1)	22.4			2.0	0.9	0.9	0.9	0.3	(2.7)	4.1
Steel			**33%**							**13.4**	**28.6**	**10.0**				**0.2**	**0.2**	**0.1**	**10.8**	**5.0**	**13.7**

International Steels Limited (ISL)

Our investment case is backed by 3Yr profitability CAGR of +18%, whereas earnings in FY20 are expected to recede by almost 41%YoY, owing to unconducive business environment for the sector in the current year. Playing in a cyclical space, the country's economic recovery down the line, sector protection from international dumping and substantial reduction in finance costs in a monetary reversal scenario form the building blocks of our investment case.

Investment thesis

- ✓ **High protectionary duties to help enhance market share:** Local flat steel producers have been very much vigilant about imported flat steel products entering Pakistan at dumped prices. While they earlier sought anti-dumping duties within the range of 13-19% from products dumped from China and Ukraine, they have now been successful in gaining preliminary antidumping duty of around 14% from Russia and Canada. With these protectionary measures in place and given ISL's enhanced capacity much benefit is expected to follow going forward.
- ✓ **Reversal of Monetary cycle to support net margins:** Ever since the PKR had been let loose, short term borrowing requirements of steel sector have sky rocketed resulting in greater finance costs. Adding further injury were the rising benchmark interest rates which now appear to have peaked out at 13.25%. With interest rates expected to recede post 3QFy20, much needed earnings breather is expected to arrive.
- ✓ **Earnings to grow by a 3Yr CAGR of 18% post Fy20**: While economic contraction is to keep earnings performance in Fy20 quite dismal to PKR 3.58/share, depicting a 42%y/y decline as compared to the previous year, we expect them to recover rather strongly post Fy20 with a 3Yr earnings CAGR of 18%.

Recommendation: We present a Buy call on ISL with a Dec-20 target price of PKR 72/share, offering a 25% upside from last close, which is in addition to 3% dividend yield for FY20, taking total return to around 29%.

Key Risks: a) Decrease in CRC/HDGC sales prices, b) Administrative increase in energy prices and c) Substantial depreciation of PKR

International Steels Limited

Current Price (PKR):	58		Target Price (PKR):		72
Period end (JUN) - PKRmn	**FY18A**	**FY19A**	**FY20E**	**FY21F**	**FY22F**
Income Statement Items					
Net Sales	47,621	55,062	54,803	63,333	70,751
Gross Profit	7,631	6,449	5,825	8,224	9,709
Sell. / Dist. & Admin	720	986	1,264	1,435	1,597
Operating Profit	6,911	5,463	4,561	6,789	8,112
EBIT	6,342	4,968	4,324	6,403	7,602
Dep. & Amt.	857	1,077	1,241	1,299	1,352
EBITDA	7,199	6,045	5,566	7,702	8,954
Financial Charges	539	1,289	2,177	2,177	1,658
Pre-tax Profits	5,803	3,679	2,147	4,226	5,943
Taxation	1,438	1,015	563	1,107	1,557
Post-tax Profits	4,365	2,664	1,584	3,118	4,386
Balance Sheet Items					
PPE	18,263	19,862	19,372	19,109	18,830
LT Invest.	-	-	-	-	-
Inventory	14,133	14,648	16,102	18,118	18,396
Receivables	645	868	927	1,071	1,196
Current Assets	17,327	19,897	20,468	22,710	23,193
Total Assets	35,593	39,762	39,843	41,822	42,025
Trade Payables	4,504	5,612	6,709	8,304	10,034
ST-Borrowings & CP of LT Loans	9,664	11,101	13,428	12,836	9,877
Other Current Liab.	1,123	1,573	805	805	805
LT Loans	6,768	6,367	4,405	3,183	1,960
Other Non-Current Liab.	1,708	2,231	1,338	1,071	535
Share Capital	4,350	4,350	4,350	4,350	4,350
Total Equity	11,825	12,878	13,158	15,624	18,814

Upside	25%		Recommendation		BUY
Period end (JUN)	**FY18A**	**FY19A**	**FY20E**	**FY21F**	**FY22F**
Per Share Data					
EPS	10.03	6.12	3.64	7.17	10.08
BV	27.18	29.61	30.25	35.92	43.25
DPS	4.50	3.00	1.50	2.75	4.00
Cash & Equivalents	0.23	0.93	0.50	0.50	0.50
Valuation					
P/E (X)	5.7	9.4	15.8	8.0	5.7
P/B (X)	2.1	1.9	1.9	1.6	1.3
Div. Yld (%)	7.8	5.2	2.6	4.8	7.0
Earnings growth (%)	43	(39)	(41)	97	41
EBITDA growth (%)	23	(16)	(8)	38	16
ROE (%)	36.9	20.7	12.0	20.0	23.3
Margins					
Gross Margins (%)	16.0	11.7	10.6	13.0	13.7
EBITDA Margin (%)	15.1	11.0	10.2	12.2	12.7
Net Profit Margins (%)	9.2	4.8	2.9	4.9	6.2
Financial Gearing					
Debt / Equity (%)	139	136	136	103	63
Interest Coverage	12	4	2	3	5
Efficiency Ratios					
Current Ratio	1.0	1.1	1.1	1.0	1.0
Quick Ratio	0.3	0.2	0.3	0.2	0.2
Volumes (mn tons)					
CRC Prices	585.1	718.9	663.3	623.0	628.0
HRC Prices	478.9	632.9	588.5	550.0	550.0
Spread	106.2	86.1	74.7	73.0	78.0

SOURCE: IGI Research, Company Accounts

Market-weight

Power Generation & Distribution Companies

Making inroads in reducing circular debt

We are **"Market-weight"** on Pakistan IPPs on the back of (i) expected improvement in circular debt build-up where pace of accumulation has stalled to PKR10bn/month, (ii) removal of subsidies/tariff adjustments to recover costs, and (iii) anti-theft drives leading to higher recoveries. Furthermore, substantial drop in FO prices may lift FO plants up in merit order list.

- ✓ **Generation mix-**The power sector landscape in Pakistan has altered dramatically with 8,500 MW added to the national grid in the last few years to ~30,500 MW in Fy19, with the aim of providing cost efficient electricity to the national grid. The share of expensive RFO based generation within the mix nosedived to 7% in Fy19 vs. 53% in Fy14 replaced by LNG/Gas based generation largely led by Bhikki, Baloki and Haveli (66% guaranteed fuel supply of the LNG import). This has also resultantly led to plant shut down at most RFO based plants. That said, the regulator remains contractually obligated to pay capacity payments irrespective of dispatch. Over the next few years several IPPs formed before the 2002 Power Policy are likely to be weaned of the fixed capacity charge due to imminent expiry of PPAs. PPA extensions are unlikely, in our view, instead there may be a gradual shift towards take-and-pay structure.
- ✓ **Circular debt**-The incumbent Government has made inroads in reducing circular debt under IMF program, where prior actions required tackling of rising arrears (PKR 1.69bn, 4% of GDP as at Sep-19). This has been primarily led by cost recovery via tariff hikes where accumulation of new arrears has stalled to PKR10bn/month in 3MFy20 (PKR 38bn/month in Fy19). While IMF's target for circular debt reduction is ambitious (PKR75bn/annum by Fy23), tariff adjustments, coupled with intermittent liquidity injection (Sukuk II of PKR 200bn) should further ease on cash flows. Sukuk-II is expected to address overdue CPP payments to IPPs which may open up room for payouts.
- ✓ **Temporary disruptions in winter season adding to woes-**On the flip side, running parallel to tariff adjustments, the cost gap (PKR/kwh) between RFO and LNG has capsized with LNG costs outstripping RFO (Sep-19: PKR 10.16/kwh, vs. PKR 7.71 RFO). This has forced GoP to subsidize expensive LNG for domestic consumers (in winter months), thus adding to the overall debt burden. To add fuel to the fire, RFO based plants are being pushed further down the merit order list (due to relatively lower efficiency and high costs vs. LNG/coal plants), while capacity payments (CPP) are contractually guaranteed (irrespective of energy dispatch). The culmination of these factors has led to a rise in fixed costs (CPP charge to the overall tariff). This is however, a temporary phenomenon and should normalize with peak demand during summer season.

Earnings and Valuation: With several expansion projects to come online over the next few years, we expect IGI IPPs universe to post +44%y/y growth in earnings in Fy20 with a 3Yr forward CAGR of +11%.

Top picks and recommendation: We hold a preference for HUBC due to an unparalleled yield from Fy21 (15%) onwards, multiple expansion projects adding to Cashflow life which makes HUBC a growth company.

Key Risks: a) Circular debt build up, b) Reforms insufficient to address circular debt, c) revision in PPA's of existing IPP's, d) prolonged dividend amid cash constraints and e) delays in project COD.

Sym	Recomm.	TP (PKR)	3yr EPS CAGR	EPS			DPS			P/E			D/Y			P/B			ROE		
				19	20	21	19	20	21	19	20	21	19	20	21	19	20	21	19	20	21
HUBC	BUY	139	50%	8.7	19.0	21.1	-	6.0	15.0	11.9	5.4	4.9		5.8	14.5	2.6	1.9	1.7	26.0	41.2	37.4
KAPCO	BUY	45	-100%	14.9	13.3	13.8	4.5	5.5	9.0	2.0	2.2	2.2	15.1	18.5	30.3	0.6	0.5	0.5	34.4	26.2	24.2
NCPL	BUY	24	-41%	9.3	9.7	2.6	2.0	3.5	4.5	2.0	2.0	7.2	10.5	18.4	23.7	0.5	0.4	0.4	25.7	22.9	5.8
Power Generation			**11%**							**6.0**	**4.2**	**4.1**	**0.5**	**0.9**	**1.7**	**0.9**	**0.7**	**0.7**	**29.3**	**33.2**	**28.9**

The Hub Power Company Limited (HUBC)

We base our investment case on +119%y/y earnings growth in Fy20 with a 3yr profitability CAGR of 50% over Fy20-23. We base our call on earnings growth for HUBC. Though we expect no cash payout in Fy20 owing to equity requirement for new project, we highlight possibility of modest cash dividend post issuance of Sukuk-II.

Investment thesis

- ✓ **Multiple expansion projects in the pipeline-**From a defensive play to aggressively expanding into high IRR projects (17-20%), HUBC's story has changed over the last five years. HUBC's 1320MW coal fired power plant (CPHGCL) achieved COD in Aug-19, Thar Energy (TEL) has received a 1yr extension for financial close deadline to Feb-20 (COD Mar-21), while ThalNova is expected to achieve COD by Dec-21. Meanwhile SECMC's Phase-I has achieved COD and is catering to Engro's coal plants, whereas Phase-II (commenced in Dec-19) will supply to TEL and Thal Nova. While the base plant will contribute ~50% to HUBC's earnings until its PPA expiry in Fy27, the new projects will contribute ~70% Fy28f onwards.
- ✓ **…which have required debt financing-**Equity financing for expansions has necessitated raising debt and retaining earnings (HUBC skipped dividends in Fy19). HUBC obtained the first round of funding (USD 258mn, of which PKR 26.5bn are loans and PKR 7bn rights) in Fy18-19. The second round of funding (Fy20f: USD 144mn) has mostly been raised (through issuance of commercial paper, TFC and internal cash-flows in Fy20f).
- ✓ **The wish list is increasing…-**HUBC is also looking to convert two of the four RFO based units of its base plant (1,200MW) to imported coal. This may entail a moderate capex, as per management, at about USD 200mn per unit, where HUBC has received approval from the government to undertake this project. The project will help in reducing the overall cost and push the base plant up the merit order (enhancing its relevance), which is still liable to pay capacity payments (CPP) to the base plant. HUBC's management is also actively pursuing three reverse-osmosis water desalination projects worth USD 105mn cumulatively. (i) DHA project providing 5mn gallons/day, (ii) waste water treatment of 470kgallons released into the sea by Sindh Govt and (iii) reverse-osmosis for a smaller project.
- ✓ **…at the cost of delayed dividends**-HUBC is likely to retain dividends over the next 1-1.5 years particularly as the sponsor plans to expand into water desalination and coal conversion of the base plant. However, cash-flows will improve significantly as the ongoing projects come online. This should in turn lead to the resumption of large dividends from late-Fy21f as the new projects begin to generate returns.
- ✓ **…but the dividend yield is worth the wait**-We expect HUBC to revert to type i.e. steady dividend stream from end-Fy21, with high likelihood of one-time bumper payout (dividends worth of two years Fy20-21). This thesis may be derailed if HUBC continues to deploy high capital into new expansion projects (water desalination, coal conversion of base plant)
- ✓ **Circular debt has adopted a more modest pace**-Second Sukuk issue remain in the pipeline where we expect HUBC to benefit through likely receipt of overdue capacity payments which stand at PKR 30bn which may allow for a PKR 4-6/share dividend payout in Fy20. HUBC received energy payment in the first Sukuk in 2019 amounting to PKR 17bn out of which PKR 12.5bn was paid to PSO.

Recommendation: HUBC trades at Fy20 P/E of 5.4x and offers a Fy20/21 D/Y of 6%/15% respectively. We maintain HUBC as our top pick with our Dec-20 Target price of PKR 139/share, offering +35% upside from last close.

The Hub Power Company Limited (HUBC)

Current Price (PKR):	103	Target Price (PKR):		**139**	
Period end (Jun) - PKRbn	FY18A	FY19A	FY20E	FY21F	FY22F
Income Statement Items					
Net Sales	99,999	58,129	62,583	62,427	89,504
Gross Profit	18,279	21,489	25,424	24,251	39,683
Selling & Distr. Expense	1,525	1,606	1,283	1,531	1,583
Other Income	219	527	341	380	402
Other expenses	110	128	70	67	76
EBIT	16,863	20,282	24,412	23,033	38,425
Finance Costs	4,432	7,401	12,181	9,346	13,887
Net Profit	11,665	11,930	25,615	28,437	41,385
Profit attributable to owners	11,057	11,241	24,659	27,433	37,012
Balance Sheet Items					
PPE	53,818	68,487	104,157	123,532	116,542
LT Invest.	8,824	36,303	53,105	58,895	71,159
Non-Current Assets	64,156	106,332	158,740	183,905	189,178
Inventory	6,347	5,845	1,697	1,733	1,887
Trade debts	98,856	85,647	77,556	85,312	68,249
Total Assets	186,006	225,268	267,079	316,860	307,699
Payables	83,261	70,807	72,814	79,794	64,437
Current Liab.	119,449	131,913	120,562	131,786	112,180
LT Debt	25,288	33,399	68,575	89,942	78,156
Non-Current Liab.	27,522	35,932	70,607	91,573	79,466
Total Liab.	146,972	167,845	191,169	223,359	191,647
Share Capital	11,572	12,972	12,972	12,972	12,972
Total Equity	35,450	50,999	68,831	77,811	98,441
Cash Flow Items (PKRbn)					
Operating CF	10,453	17,333	47,400	30,959	51,422
Investing CF	(12,109)	(46,845)	(57,260)	(30,054)	(14,112)
Financing CF	(1,761)	42,371	14,190	14,364	(35,190)
Cash	2,654	12,132	16,461	31,730	33,851

Upside	35%	Recommendation:		**BUY**	
Period end (Jun) - PKRbn	FY18A	FY19A	FY20E	FY21F	FY22F
Valuation					
EPS	8.5	9.0	19.0	21.1	28.5
DPS	6.6	-	6.0	15.0	16.0
BV	27.3	39.3	53.1	60.0	75.9
P/E (x)	12.1	11.5	5.4	4.9	3.6
P/EBITDA (x)	9.3	7.6	7.6	8.3	4.6
D/Y (%)	6.4	-	5.8	14.5	15.5
ROE (%)	32.9	23.4	37.2	36.5	42.0
ROA (%)	6.3	5.3	9.6	9.0	13.4
Margins					
Gross Margins (%)	18.3	37.0	40.6	38.8	44.3
EBIT Margin (%)	16.9	34.9	39.0	36.9	42.9
Net Profit Margins (%)	11.06	19.34	39.40	43.94	41.35
Financial Gearing					
Total Debt / Equity (%)	4.1	3.3	2.8	2.9	1.9
Interest Coverage	3.8	2.7	2.0	2.5	2.8
Efficiency Ratios					
Current Ratio	1.0	0.9	0.9	1.0	1.1
Quick Ratio	1.0	0.9	0.9	1.0	1.0

Source: IGI Research, Company Financials *Updated as of : 10-Jan-20*

Engro Polymer & Chemical Limited (EPCL)

We are overweight on EPCL currently trading at P/E of 7.3x, offering at a discount of 12% with respect to market P/E of 8.7x. We base our investment case on key attributes, monopoly in PVC market, ongoing investments in different businesses and focus on increasing cost efficiencies.

Investment thesis

- ✓ **Monopoly in PVC market-**EPCL enjoys the monopoly of being the sole producer of PVC in Pakistan having a competitive advantage to charge at premium pricing. Demand for the product has remained robust (4Yr-CAGR of 9%) spurred by strong activities in the downstream sectors (pipe and fittings, construction activities). The company is operating at full capacity and has maintained its market share of 70%.
- ✓ **Projects in pipeline-**The Company has undertaken various projects related to process improvements and cost efficiency. As such EPCL will make use of oxygen based VCM technology, reducing its raw material consumption by 2% (annual impact PKR ~0.5/share). In addition, company also plans to decrease its gas requirement for PVC manufacturing by 10%, reducing costs by PKR 0.3/share.
- ✓ **Addition of caustic flake-**EPCL has recently introduced caustic flake in its product portfolio, a variant of caustic soda. With this new product addition, the company can also tap in to export markets, in addition to the local industry, thereby enhancing its market share. The new variant is expected to be offered at a price of 10-15% above that of caustic soda
- ✓ **Potential entry in hydrogen peroxide and LABSA business-** To expand its product portfolio the company eyes to enter in hydrogen peroxide (HP) business (20-25k tons of expected capacity) where DOL and SPL have dominated the market. More so, the company has recently planned for another product line, Linear Alkyl Benzene Sulphonic Acid (LABSA) with an annual capacity of 24Mtons.
- ✓ **Margins soared during CY19-** PVC-core delta depicted healthy trend during CY19 marking a +30%y/y increase to 440 USD/ton. A declining trend was seen during the year in PVC and Ethylene prices as US-China trade war and economic slowdown acted as a drag. We see core delta to normalize once capacities come online and demand shifts as global economy revives. Looking at the past trend of margins, we project USD 310/ton core delta, going forward.

Recommendation: Our Dec-20 target price of PKR 45.3/share is derived by using DCF based methodology, using risk free rate of 11.75%. The company is currently trading at CY20E P/E of 6.7x at a dividend yield of 4.7%.

Key Risks: a) Increase in gas prices, b) Decrease in PVC-core delta and c) Increase in finance costs.

Engro Polymer Company Limited (EPCL)

Current Price (PKR):	35		Target Price (PKR):	45	Upside	28%		Recommendation		BUY

Period end (DEC) - PKRbn	CY18A	CY19E	CY20F	CY21F	CY22F
Income Statement Items					
Net Sales	35,272	35,976	38,959	41,150	43,481
Gross Profit	8,736	8,876	9,772	9,521	9,483
Sell. / Dist. & Admin	2,044	1,375	2,677	2,828	2,988
Other Op. Income/Expense	377	(143)	(124)	(181)	(204)
EBIT	7,069	7,358	6,971	6,709	6,595
Dep. & Amt.	959	999	1,408	1,720	1,797
Financial Charges	606	1,672	974	851	754
Pre-tax Profits	6,463	5,686	5,996	5,858	5,841
Taxation	1,533	1,555	1,679	1,560	1,485
Post-tax Profits	4,930	4,131	4,317	4,298	4,356
Balance Sheet Items					
PPE	19,398	20,704	32,947	36,461	37,375
LT Invest.	84	84	84	84	84
Inventory	5,144	5,346	5,757	6,239	6,706
Receivables	430	493	534	564	596
ST-invest.	7,798	-	-	288	2,294
Current Assets	16,434	7,556	8,350	9,060	11,698
Total Assets	36,023	39,298	42,536	45,861	49,417
Payables	6,436	5,569	5,997	6,499	6,986
Other Non-Current Liab.	390	390	390	390	390
Share Capital	9,089	9,089	9,089	9,089	9,089
Total Equity	16,796	20,018	22,972	26,816	30,035
Cashflow Items					
Operating	3,865	5,841	6,061	5,939	6,283
Investing	(9,986)	2,444	(13,708)	(5,415)	(4,610)
Financing	205	(909)	(1,454)	(621)	(1,303)
Cash	1,362	454	454	454	454

Period end (DEC)	CY18A	CY19E	CY20F	CY21F	CY22F
Per Share Data					
EPS	5.4	4.5	4.7	4.7	4.79
BV	18.5	22.0	25.3	29.5	33.05
DPS	1.1	1.0	1.5	0.5	-
Cash & Equivalents	10.1	0.5	0.5	0.8	3.02
Valuation					
P/E (X)	5.9	7.0	6.7	6.8	6.72
P/B (X)	1.7	1.5	1.3	1.1	0.98
Div. Yld (%)	3.4%	3.1%	4.7%	1.6%	0%
Earnings growth (%)	140%	-16%	5%	0%	1%
EBIT growth (%)	80%	4%	-5%	-4%	-2%
ROE (%)	40.2	22.4	20.1	17.3	15.32
Margins					
Gross Margins (%)	24.8%	24.7%	25.1%	23.1%	21.8%
EBIT Margin (%)	20.0%	20.5%	17.9%	16.3%	15.2%
Net Profit Margins (%)	14.0%	11.5%	11.1%	10.4%	10.0%
EBITDA Margins (%)	22.8%	23.2%	21.5%	20.5%	19.3%
Financial Ratios					
Debt / Equity	2.24	2.70	3.17	3.79	4.35
Interest Coverage	11.66	4.40	7.15	7.88	8.75
Current Ratio	1.45	0.72	0.75	0.78	0.97
Quick Ratio	1.00	0.21	0.23	0.24	0.41
Financial Leverage	2.14	1.96	1.85	1.71	1.65
Defensive Interval	3.97	0.18	0.07	0.25	1.29

SOURCE: IGI Research, Company Accounts

Updated as of: *10-Jan-20*

Key risks to our call

Geopolitical tensions: Multi-geopolitical tension forms a precarious situation

FATF: Prospects of Pakistan falling under 'blacklist' remain limited

Out of the total set of **40** recommendations formulated by FATF, Pakistan has;

Fully Complaint=1
Largely Compliant=9
Partially Compliant=27
Not compliant=4

As part of the country's on-going compliance with Anti-Money Laundering (AML)/ Combating the Financing of Terrorism (CFT), the FATF (Financial Action Task Force) in its last evaluation report has maintained Pakistan's status under the grey list category, with technical deficiencies still left unaddressed and for that an extended deadline to Feb-20 has been recommended. In case of not meeting the above compliance by stated dates, FATF will take action, which could include the "FATF calling on its members and urging all jurisdictions to advise their FIs to give special attention to business relations and transactions with Pakistan". We think a relatively, short timeline by Feb-20 to fully complete implementation of AML/CFT could be challenging and remains by far one of the crucial risk. However, prospects of Pakistan falling in blacklist remain limited in our view.

Pakistan/India cross border tension: Starting 2019, Pakistan – India relation have been at a standstill with a series of close to conflict situations, starting from early 'Pulwama attack' to 'surgical strikes', Pakistan air-response and later revoke of Kashmir special status by India. While tension between Pakistan and India remain precarious we rule out possibility of military conflict forming up.

US/China Trade: Uncertainty over US/China Trade relations have had a hard hitting on global markets in 2018-2019 across. A slowdown in global growth can potentially open up external balance vulnerabilities mainly on account of slowdown in country's already ailing export sector, remittances and financial inflows both FDI and portfolio investments, which could deter country's growth trend output. However recent news of 15% tariff rollback on USD 100bn worth of imports from China may provide much breather to the existing situation.

Pakistan/US relation: China rising influence in Pakistan and the region via CPEC has kept US and Pakistan relation rather edgy in past. However, Pakistan authorities have opted to act as main negotiator for a safe exit of US military from Afghanistan, which has somewhat amended Pakistan/US relations.

US/Iran: The US and Iran relations have been on shaky grounds since May-2019, with latest rounds of escalation starting 2020. Key outcome of if situation deteriorates, could be a) sustained high oil prices - since Strait of Hormuz (which is a pathway to nearly 20% of oil supply shipments) could be blocked again, and b) deterioration of US/Pak relation if Pakistan authorities choose to tag out.

Commodities: Oil price hike risk stands looming

We see oil prices to average in the region of between USD 60-65/bbl for Fy20

Oil prices: Crude oil prices remained volatile range bound between USD 50-75/bbl during 2019. Characterized by multiple of events including a) Iran waiver expiring in May-19, b) continuation of production cuts by OPEC and OPEC plus members, c) supply disruption in OPEC member countries, and d) drop in US crude oil inventories caused Oil to touch north of USD 75/bbl. However, during the second half of 2019, oil price retreated back in the range of USD 60-65/bbl amid a) escalation in US/China trade war, b) rise in US inventories, and c) expectation of global economy slowdown further strengthens.

We see oil prices to average between USD 60-65/bbl for Fy20. However, upside risk such as geopolitical tension, escalated by recent attack on Iran, easing trade tensions between US and China and lower than expected slowdown in economy could drive up oil prices beyond USD 70/bbl. Furthermore, exit of Russia from OPEC plus agreement and cessation of Saudi Aramco's IPO following which Saudi Arabia might loosen its production output cuts may lead to lower oil prices, in our view.

Given Pakistan's heavy reliance on oil imports, we see USD 10/bbl increase in oil prices could potentially push a) c/a deficit by +0.15% of the GDP, b) 3-5% of inflation basket is directly impacted while, indirectly subsequently we may see monthly inflation picking by additional 0.05% m/m, c) delaying monetary easing and d) increase fiscal borrowing.

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