Vector Analysis

June 2011

Sources: SBP; SECP; NCCL; KSE; MUFAP; FBS; AMC; Newspapers & TV Channels.

Suggested Investment Approach

Suggested Investment Strategy
Managing Investments In A Volatile Market

Rising Interest Rates

Good Investment
Floating Rate Bonds
Money/Income Funds
Short term Investments

Bad Investments
Fixed Rate Bonds

Topped Interest Rates

Good Investment
Fixed Coupon Bonds
Income/Bond Funds
Long term Investments

Bad Investments
Floating Rate Bonds

Falling Interest Rates

Good Investment
Equities
Bond Funds
Long term Investments

Bad Investments
Floating Rate Bonds

contact@vector.com.pk
www.vector.com.pk

ASSUMPTIONS

* Pakistan continues to tread on a difficult economic path. Devastation of floods at the start of the outgoing fiscal year, energy shortages and resultant social unrest, inflation and deteriorating security in the wake of war on terror which further aggravated in the post May 2 event has severely affected investments and business productivity in the country. Add to this fiscal pressures in the wake of weak internal and external sources of funds, the situation becomes more challenging to achieve sustainable economic growth.
* Revenue targets for the new fiscal year seem ambitious given that not only was the revenue target for the outgoing fiscal year revised downward thrice, even the final target of Rs.1,588bn seemed difficult to achieve since the FBR faced a shortfall of Rs.121bn till June 26, 2011.
* The suspension of IMF Standby Arrangement continues to put strain on external sources of funds. Moreover, efforts to raise USD500mn through sale of OGDC exchangeable bonds have not been fruitful. Accordingly, government's reliance on domestic borrowing, to finance estimated budget deficit of Rs.1.08trillion for FY11, is likely to maintain its current upward trend atleast in the near term.
  Government borrowing from scheduled banks during July 1 to June 18 FY11 stood at Rs.530bn as against Rs.260bn during corresponding period of FY10. This unabated government borrowing is resulting in 'crowding out' private sector credit which is vital for economic growth.
* Robust exports and high remittances contributed to current account surplus during July-May FY11. The sustainability of the improvement in external account position is questionable given the global slide in prices of exportable items of Pakistan particularly cotton.
* In view of the back drop, there are growing concerns regarding 'roll over risk' given heavy borrowing by the government through short term t-bills (outstanding stock of Rs.1.8trillion as on May 2011) and weakness on the revenue generation front. Interest rates are therefore expected to stay stable in the near term with an upward bias.
* Possibility of SBP changing its tight monetary stance in its upcoming monetary policy announcement is very bleak given the current economic dynamics.

CRITICAL TO WATCH

* Revenue generation measures and their results. Also the fate of the proposed OGDC exchangeable bond transaction as it success is critical for inducing some level of confidence amongst investors in the local capital markets as well as raising valuable funds for the cash starved government.
* Pakistan's current international image and domestic political events as they have a significant bearing on the country's economics and investment climate.

INVESTMENT APPROACH

* We maintain our stance on following a conservative approach in the wake of current political and economic climate. Investment in short duration instruments, cash/money market funds is recommended given competitive risk/returns offered.
* The equity market is likely to stay volatile. Upcoming result season may attract interest in the market. Profit taking at high levels and buying at dips in selective scrips in oil and gas, fertilizer, cement, textile and power sectors is recommended.

Economic Snapshot

Economic numbers for the first eleven months of fiscal year FY11 (July 2010-May 2011).

CURRENT ACCOUNT

After having recorded surplus on current account during March and April 2011, the country posted current account deficit of USD457mn during May 2011 mainly on account of higher imports and lower exports during the month of May. Trade deficit during May stood at USD1bn as against a deficit of USD316mn during previous month. During the review period, current account recorded surplus of USD205mn as against deficit of USD3.4bn during corresponding period of FY10.

EXPORTS

Export of goods registered YoY increase of 27.4% rising to USD22.7bn during the period under review. Textile group which accounted for 51% of total exports registered YoY increase in export receipts of 27%. Food group which accounted for 16% of total exports registered YoY growth of 21%. On monthly basis however, exports registered MoM decline of 13% primarily due to decline in export receipts of food items.

IMPORTS

Import of goods grew by 14.5% YoY during July-May FY11. Food group which accounted for 13% of total imports registered YoY increase of 53% largely driven by substantial increase in import bill of palm oil and sugar. Import bill of petroleum group, constituting highest share in import bill at 34%, registered YoY increase of 17%. On monthly basis, import bill increased by 12.7% primarily on account of 25% MoM increase in oil import bill.

HOME REMITTANCES

Home remittances continued to exhibit an upward trajectory crossing USD1bn mark for the second consecutive month and increasing by 1.8% MoM in May 2011. On cumulative basis, remittances increased by 25.2% YoY during the first eleven months of FY11.

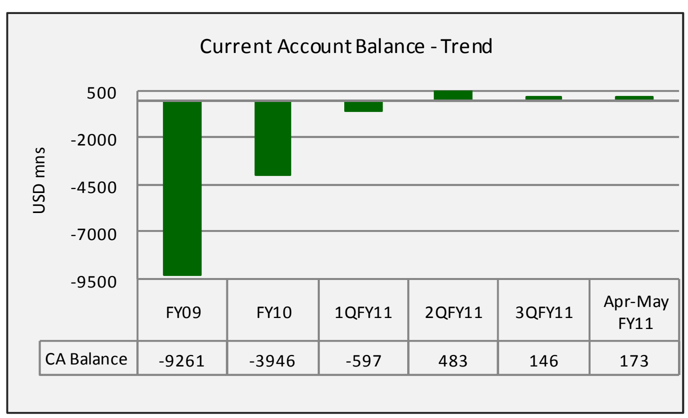
FOREIGN INVESTMENT

Foreign Direct Investment (FDI) continued to falter falling to USD1.4bn during July-May FY11 as against USD1.9bn during corresponding period of FY10 registering YoY decline of 29.7%. Portfolio investment, however, turned positive with an inflow of USD347mn against and outflow of USD133mn during July-May FY10.

INFLATION

CPI for May 2011 increased by 13.2% YoY and by 0.2% MoM. The marginal 'easing' in CPI for the month of May over April was primarily due to marginal decline in prices of perishables.

Selective Indicators	FY11 Jul-May	FY10
GDP	-	4.1%
Import of goods	32.1	31.2
Export of goods	22.7	19.6
Trade Deficit	9.4	11.6
Current account balance	0.2	(3.9)
CPI*	14.0%	11.7%
Food	18.2%	12.5%
Non-Food	10.5%	11.1%
Net Foreign Investment	1.7	2.1
FDI	1.4	2.2
Portfolio	0.3	-0.1
Remittances	10.4	8.9
Reserves	**17.4	16.7
Pvt Sector Disbursement (Rs. bn)	***103	3,019
Govt Borr from SBP (Rs. bn)	***185	1,142
Govt Borr from scheduled banks	***530	803
Net Govt Sector Borrow (Rs.bn)	***670	2,441
All figures in USD bn unless specified in PKR		
**Period Average*		
***As on June 25, 2011*		
****Position July 1 to June 18 FY11 (govt borr represents federal govt)*		



Source: SBP & Federal Bureau of Statistics

Snapshot — Interbank Market

Market Highlights

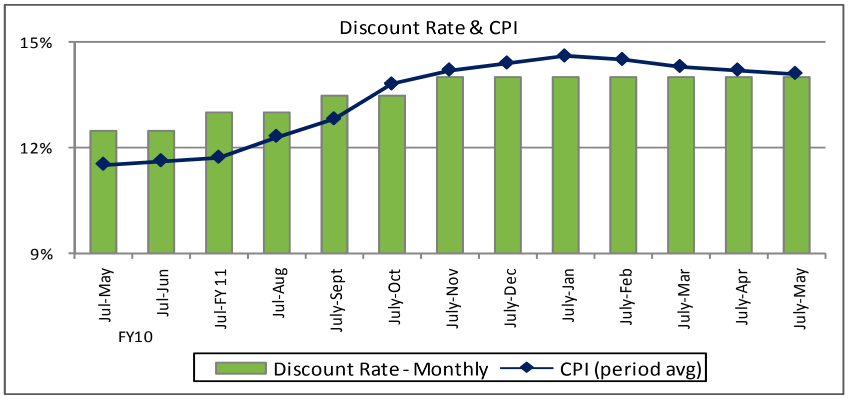
Treasury Bill Auctions Held			
	Cut-off (%)	Chg bps	Amt Accepted (Rs. In bn)
Jun 1			
3M	13.53	32 ▲	16.32
6M	13.76	16 ▲	77.20
12M	13.91	7 ▲	41.95
Jun 15			
3M	13.48	5 ▼	28.43
6M	13.73	3 ▼	82.91
12M	13.90	1 ▼	69.00
Jun 29			
3M	13.48	-	6.97
6M	13.73	-	42.84
12M	13.90	-	23.00

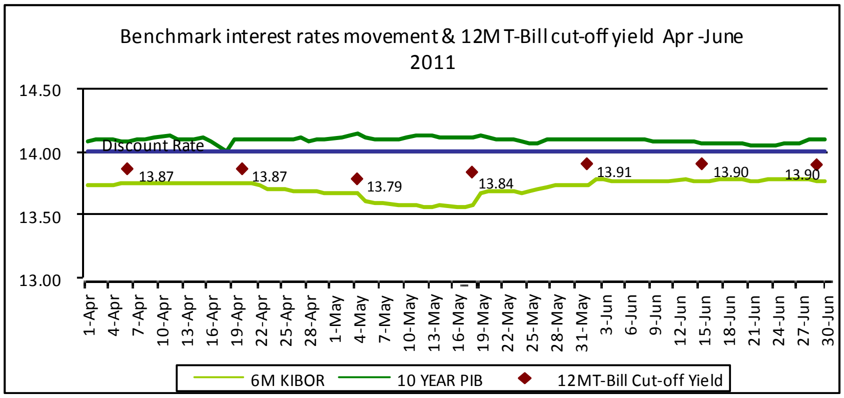
PIB Auction Held			
Jun 22	Cut-off (%)	Chg bps	Amt Accepted (Rs. In bn)
3 yr	14.00	-	10.96
5 yr	14.05	-	2.86
7 yr	-	-	Rej
10 yr	14.09	-	14.76
15 yr	14.10	-	0.2
20 yr	14.14	-	0.2
30 yr	14.19	*64 ▲	0.2

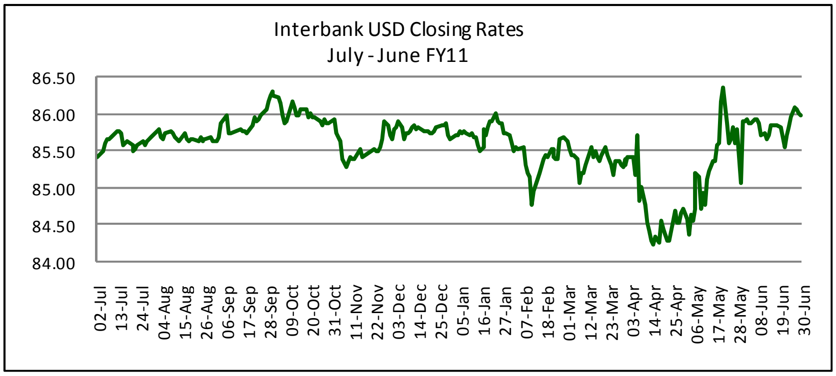
Last cut-off 13.55% auction held on Feb 2010

Selective Indicator	June 30, 2010	June 30, 2011
PKR vs Dollar	85.51	85.99
6 M KIBOR	12.37%	13.78%
3 M T-Bill*	12.13%	13.46%
6 M T-Bill*	12.26%	13.68%
1 year T-Bill*	12.38%	13.85%
10 year PIB*	12.84%	14.09%

**revaluation rates*







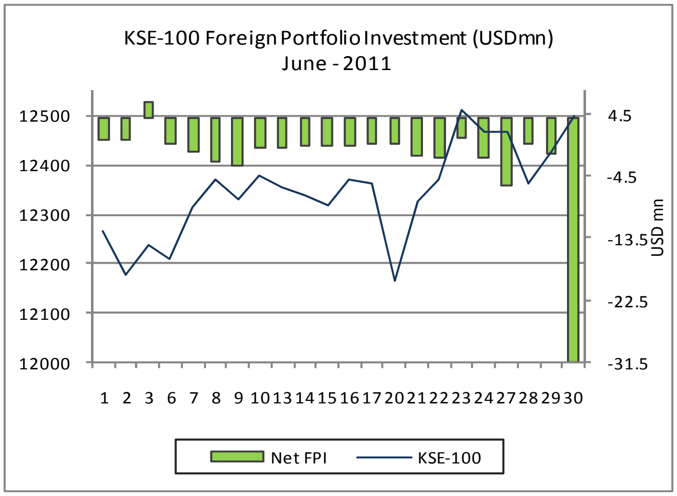
COMMENTARY

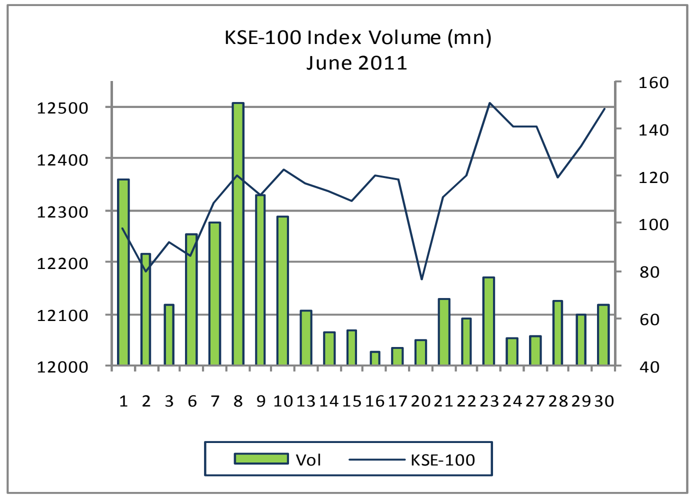
The outgoing fiscal year closed with interbank rates on the high side on YoY basis given the government's growing appetite for funds and dependence on domestic sources of funding.

Benchmark rates stayed largely stable during the month. T-Bill auctions witnessed continued interest in the 6month paper which accounted for 51% of the total participation signalling stability in near term rates.

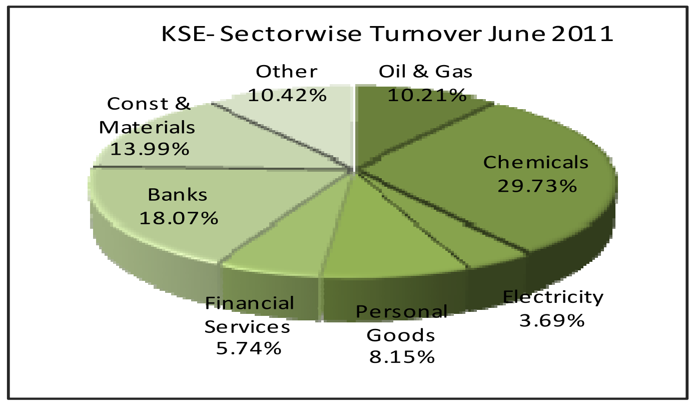
On the forex side, flow of home remittances and realization of export proceeds helped support foreign exchange reserves and PKR stability against the USD in the wake of end quarter external debt payments and oil import bill. The PKR closed FY11 at Rs.85.99.

Snapshot — Equities Market





Equity Market Highlights	May 31	June 30	% Change
KSE-100 Index	12123	12496	3.0 ▲
KSE-30 Index	11762	11586	-1.5 ▼
KMI-30 Index	20628	20936	1.4 ▲
Mkt Capitalization Rs. Mn*	3,185	3,265	2.5 ▲
Monthly Turnover (T+2) mn*	71	75	5.2 ▲
*Average daily			



Corporate News

Pakistan Petroleum Ltd (PPL) announced second interim dividend of Rs.5/share (50%) for the year ending June 2011. The government is expected to earn Rs.4.2bn through the dividend announcement. First interim dividend announced by the company was also 50%.

Furthermore, according to the company, the Cabinet Committee on Privatization has approved secondary public offering of 2.5% (21.1mn shares) of GoP holding in PPL .

The proposed issue of OGDC exchangeable bonds worth USD500mn failed to attract desired foreign interest. The issue was expected to generate funds before the outgoing fiscal year end.

Engro Corporation Ltd to list Engro Foods Ltd via offer of 27mn shares at Rs.25/share (including premium of Rs.15). The offer represents 3.6% of total paid up share capital of Engro Foods. The proceeds would be utilized to invest in Al-Safa acquisition in North America.

COMMENTARY

Last month of the outgoing fiscal year 2011 witnessed low volumes and volatility at the KSE. The benchmark index touched a low of 12130 during intraday trading as uncertainty prevailed over the future direction of the market given economic concerns and in particular on going energy crisis and its impact on industrial production.

Post budget session induced selling as status quo was maintained on CGT. However, budget proposals regarding the discontinuation of flood surcharge, lack of asset tax, reduction of FED on cement and no change in corporate tax on banks coupled with hydrocarbon discovery proved to be positive as the KSE-100 index, largely under the lead of index heavy scrips in the oil and gas and fertilizer sectors, crossed the 12500 psychological barrier. Political issues coupled with negative news regarding the OGDC exchangeable bonds and EU tariff concessions and year end portfolio adjustments induced selling towards month end. Support, in index heavy scrips notably OGDC in the last trading session of June helped the KSE-100 close FY11 above 12500.

Foreign investment declined by 51% YoY in FY11. As per NCCPL records, against a net inflow of USD567mn in FY10, FY11 registered net inflow of USD280mn.

Snapshot — Mutual Funds Industry

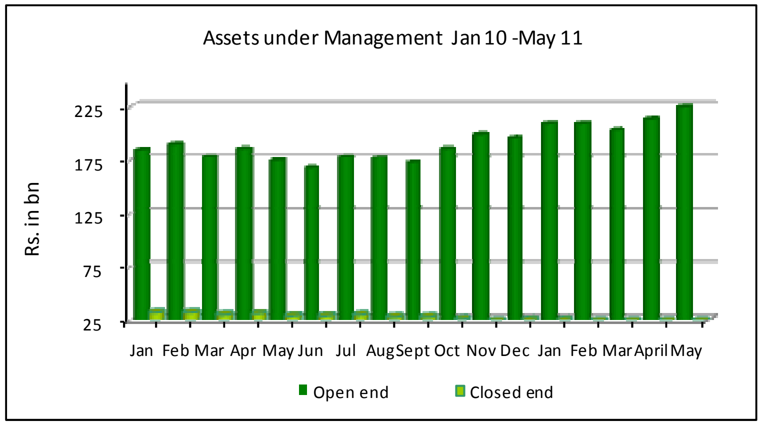
Top five funds based on returns

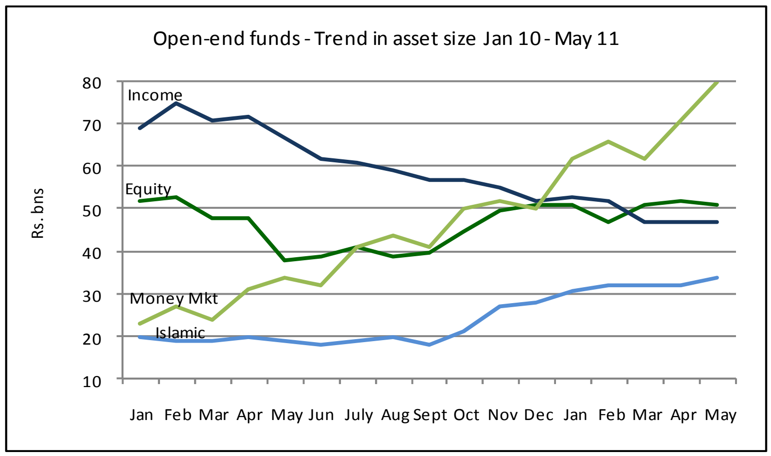
Money Market	YTD %	MTD %	AUM (Rs. mns) April	AUM (Rs. mns) May
Askari Sovereign	12.26	12.03	5,314	6,435
PICIC Cash	11.74	11.99	1,088	1,086
IGI Money	11.88	11.86	2,251	2,437
Atlas Money	11.65	11.71	2,843	3,312
JS Cash	12.06	11.70	1,330	1,435

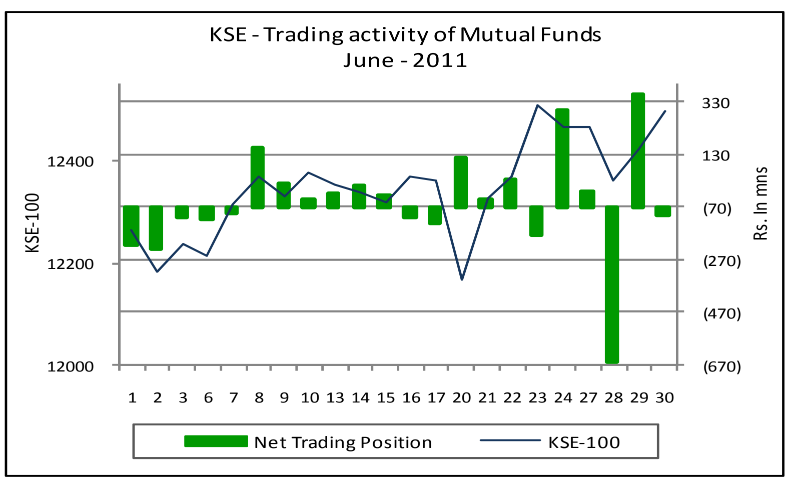
Income Funds	YTD %	MTD %	AUM (Rs. mns) April	AUM (Rs. mns) May
Dawood Money	24.31	-3.84	437	460
HBL Income	13.41	21.51	1,479	1,494
Crosby Phoenix	13.05	11.82	193	170
Pakistan Income	12.57	5.94	1,878	1,813
Pak Inc Enhance	12.51	14.38	1,687	1,626

Equity Funds	YTD %	MTD %	AUM (Rs. mns) April	AUM (Rs. mns) May
Atlas Islamic	45.17	0.45	290	326
JS Islamic	40.57	-0.18	243	244
Atlas Stock	40.47	-2.10	686	672
Meezan Islamic	39.01	0.68	4,378	4,444
JS Large Cap	38.08	-0.41	1,637	1,685

Market Indices	YTD %	MTD %
KSE-100	28.53	3.08
KSE-30	21.24	-1.50
KMI-30	43.34	1.49







COMMENTARY

Cash funds continued to attract interest given the current environment of weak economics, fiscal constraints and expectations of an 'uppish' trend in interest rates. Asset base (including Islamic cash funds) grew by 11% MoM as investors opted for low risk invest options.

On the equity market, mutual funds were net sellers at Rs.983mn in June compared to net buying of Rs.72.2mn in May, largely due to profit booking and fiscal year end considerations.

**Money Market funds are ranked based on monthly performance while income and equity are ranked based on YTD.*