Faysal Asset Management

Research Note - HUBCO

20th November, 2012

In a recent meeting with the management of Hub Power Company Limited (HUBCO) the following points were discussed:

The management is very hopeful that the company will not be liable to pay a turnover tax, as the 1994 power policy does not require it to do so.

HUBCO's old plant is running at an efficiency level of 38% and Narrowal at 46% against tariff specification of 37% and 45% respectively, translating into a load factor of 75%.

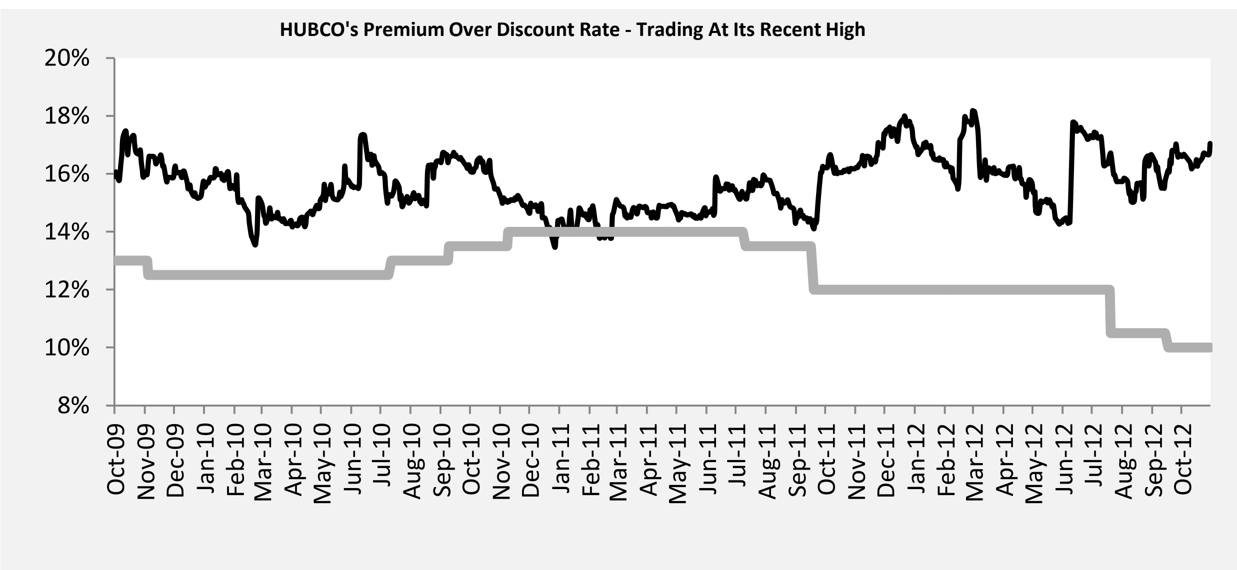
Net receivables in lieu of circular debt have decreased to PKR 17 billion from PKR 22 billion at the end of FY12. Approaching the International Arbitration Court continues to be an option which the company can exercise in case it doesn't get its share of payments from the government. As per the management, the company is in no dire need of funds and chooses to settle the matter amicably with the government.

As per the management, there are no plans of changing the company's dividend payout policy with the change in sponsor of the company.

Work on Laraib Energy is in full swing and is expected to come online much before schedule in December 2012 while it's CoD can be expected by March 2013.

Outlook

News regarding the turnover tax resulted in a downward spiral in the scrip which saw its value decrease by 7% since the start of October 2012. We believe that the FBR sent them a notice to pay turnover tax due to its ambitious tax collection target. No change is expected in the 1994 Power Policy which gives the company's old immunity from paying turnover tax while Narrowal is also exempted as it was commissioned post 2005. Laraib Energy is expected to contribute significantly to the bottom as it too is exempted from turnover tax as per the 2002 Hydel Energy policy. The scrip currently trades at a very attractive dividend yield of 17.05% making it one of the most favored stocks among dividend seeking investors. In lieu of the plants efficiency levels, high dividend yield, its tax exemption and upcoming triggers in the stock we expect HUBCO to perform well.



The graph below shows that in the last one year the premium differential has increased to 4.8% compared to 3% for the entire period, thus showing that in the very short period the differential is expected to settle lower. This provides an ideal buying opportunity in the scrip.