ARIF HABIB LIMITED

REP-300

Nov 11, 2020

Pakistan Economy

Symptomatic! But likely to Test Negative

Balance of Payment- Symptomatic!

But likely to test negative

- **Pakistan expected to record a Current Account Deficit of USD 2.5bn in FY21**
- **Imports to grow at 2% YoY while Exports to register a 3% YoY jump**
- **Remittances to clock in at USD 24bn in FY21E, growth of 3% YoY**
- **PKR Dollar Parity expected to be PKR 165/USD by Jun’21**
- **Reserves (SBP) expected to be around USD 13.7bn as at Jun’21, marking an increment of USD 1.5bn from Jun’20 closing.**

In the run up to the recent Global Health Crisis

In the run up to the recent global health crisis, Pakistan’s Balance of Payments had embarked on the path of recovery owing to different economic measures taken by the government/SBP such as import restrictions, export packages, Pakistan Remittance Initiatives (PRI), monetary tightening and a number of other measures. Came in the COVID-19, and world socio-economic dynamics changed drastically, becoming a worldwide threat to economic progress and sustainability. The economic situation in Pakistan too, therefore, became implicitly challenging with time. During 2HFY20, PKR fell almost 8% against greenback, IMF program got temporarily halted, and overall world lockdown added further pressure to the already weak international trade of Pakistan. Despite all these impediments, Pakistan was able to post a 78% lower Current Account Deficit (CAD) of USD 3bn in FY20, on account of 30% decline in Balance of Trade (BoT) during the year, well-supported by 6% higher remittances. An 88% jump in Foreign Direct Investment was witnessed while more support came from program loans from multilateral agencies, amounting to USD 2.5bn. The country received USD 13bn external inflows from multiple financing sources during the period. This held the overall reserves at a level of USD 17.9bn by Jun’20 end.

Recovery interrupted amid COVID-19 waves

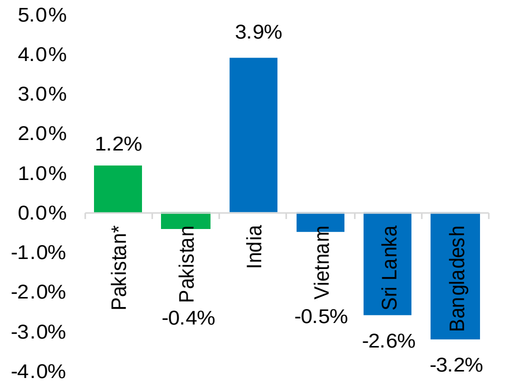
With the onset of new Fiscal Year 2021, demand and supply side disruption remained a peril to the growth of external sector of Pakistan. The global economy continues facing turmoil in 2020, but we remain largely optimistic in our outlook for Pakistan’s external account, given the continued attempts to find a resolution to dwindling trade position and continuous inflows of remittances. Despite these challenges, Pakistan was able to record a Current Account Surplus of USD 792mn in 1QFY21. After a gap of more than five years (3QFY15: USD 514mn), Pakistan posted this quarterly Current Account Surplus against a deficit of USD 1,492mn recorded in the same period last year. This is the highest surplus after 1QFY04 (USD 1.1bn) - almost 17 years.

Pakistan Balance of Payments

USD bn	FY19	FY20	YoY	1QFY21
Exports of Goods	24.3	22.5	-7%	5.4
Imports of Goods	51.9	42.4	-18%	10.6
Goods Balance	(27.6)	(19.9)	-28%	(5.3)
Services Balance	(5.0)	(2.8)	-43%	(0.5)
Balance on Trade	(32.6)	(22.7)	-30%	(5.8)
Primary Inc. Bal.	(5.6)	(5.7)	1%	(1.5)
Secondary Inc. Bal.	24.8	25.4	3%	8.1
CAB	(13.4)	(3.0)	-78%	0.8
CAB % of GDP	***-4.8%***	***-1.1%***		***1.2%***
Capital Acc. Bal.	0.2	0.3	27%	0.1
Financial Acc.	(1.2)	(7.7)	554%	0.7
Overall Balance	1.5	(5.3)	nm	0.2

Source (s): SBP, AHL Research

Regional CAB as % of GDP (Apr'20-Jun'20)



Source (s): World Bank, SBP, *Jul'20-Sep'20

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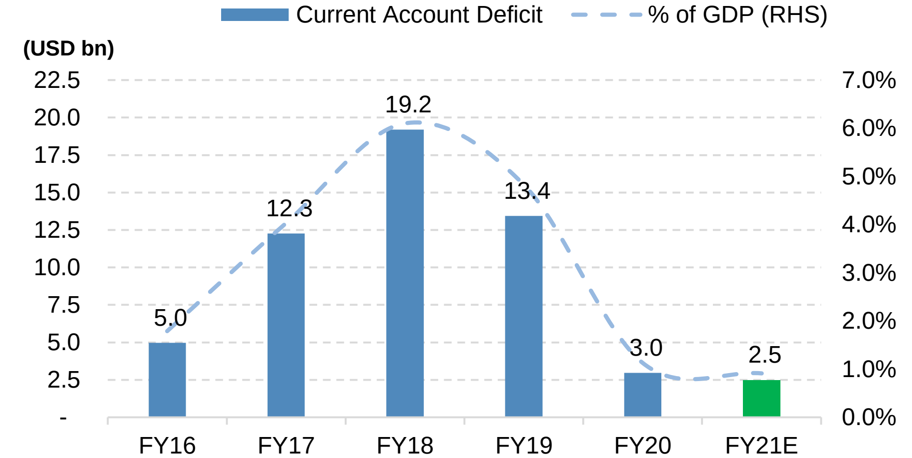
Fig 01: Current Account Deficit



Source (s): SBP, AHL Research

Going forward, however, the current account is expected to turn red and post a deficit of USD 2.5bn in FY21, with 2% increase in quantum of imports, 3% increase in exports and remittances, both. Moreover, financial account is expected to show improvement on account of hot money flowing into the debt markets. Debt moratorium by G20 countries till Dec-20 (recently extended up to June-21 for which Pakistan is yet to officially apply) has provided a relief to the reserves of the country. We expect Pakistan to be able to maintain the reserves level at USD 21bn by FY21 year end. However, pressure on PKR is expected as the overall external account remains in a state of jeopardy. We anticipate PKR to depreciate to 165/USD by the end of FY21.

The severity of 'second wave' blocking the recovery between the 2QFY21 and 3QFY21 cannot be ignored

Table 01: Current Account Balance- At a Glance

USD mn	FY16	FY17	FY18	FY19	FY20	FY21E
Current Account Balance	(4,961)	(12,270)	(19,195)	(13,434)	(2,970)	(2,493)
% of GDP	*-1.8%*	*-4.0%*	*-6.1%*	*-4.8%*	*-1.1%*	*-0.9%*
Exports of Goods	21,972	22,003	24,768	24,257	22,507	23,289
Imports of Goods	41,118	48,001	55,671	51,869	42,417	43,924
Balance on Trade in Goods	(19,146)	(25,998)	(30,903)	(27,612)	(19,910)	(20,636)
Exports of Services	5,456	5,915	5,851	5,966	5,440	5,577
Imports of Services	9,002	10,576	12,277	10,936	8,267	7,873
Balance on Trade in Services	(3,546)	(4,661)	(6,426)	(4,970)	(2,827)	(2,296)
Balance on Trade in Goods and Services	(22,692)	(30,659)	(37,329)	(32,582)	(22,737)	(22,932)
Balance on Primary Income	(5,345)	(5,014)	(5,437)	(5,610)	(5,682)	(5,867)
Balance on Secondary Income	23,076	23,403	23,571	24,758	25,449	26,306
Workers' Remittances	19,917	19,351	19,914	21,740	23,131	23,799

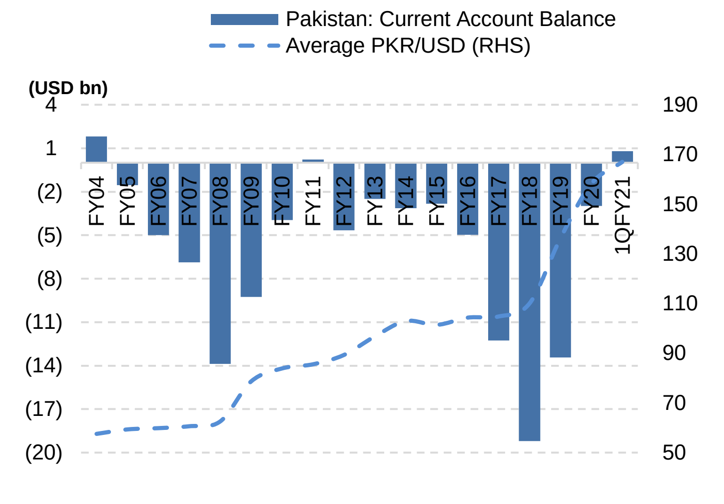
Source (s): SBP, AHL Research

CA: 1Q- Recovery! Remaining year, uncertainty?

Amidst global headwinds, the Current Account Balance remained impressive over the first three months of FY21, although exports were slower relative to 2020. For a shred of evidence, Pakistan posted a quarterly Current Account Surplus of USD 792mn during 1QFY21 against a deficit of USD 1,492mn recorded in the same period last year. This quarterly surplus comes after a gap of more than five years (3QFY15: USD 514mn). Based on the historical data, we saw that this is the highest surplus after 1QFY04 (USD 1.1bn) - almost 17 years. In the month of Sep'20 alone, Current Account Balance (CAB) arrived at USD 73mn compared to a deficit of USD 278mn during Sep'19. Aug'20 CAB has also been revised to USD 211mn from a surplus of USD 297mn. The primary factors leading to the monthly surplus in Sep'20 were: a 31% YoY (USD 544mn) rise in remittances along with a 5.4% YoY uptick in total exports mainly led by export of services (+30% MoM). However, total imports also went up by 11.6% YoY (USD 452mn) during the same period.

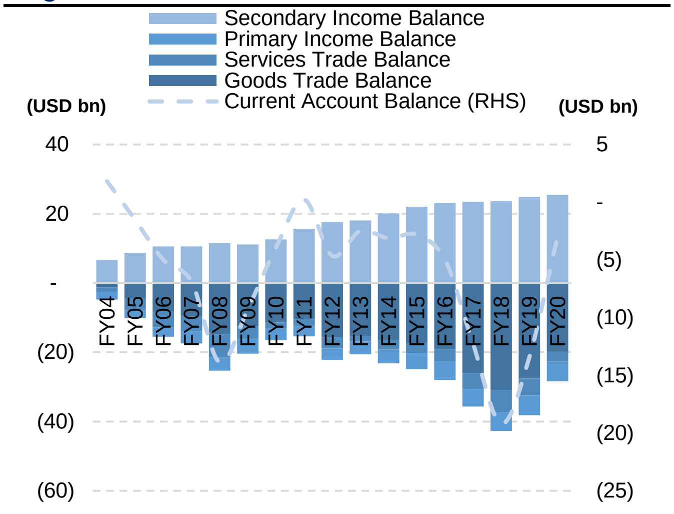
... trade balance is still on a shaky ground as global uncertainty escalates

Fig 02: Current Account Surplus in 1QFY21 (1.2% of GDP)



Source (s): SBP, AHL Research

Fig 03: Current Account Balance of USD 3bn in FY20

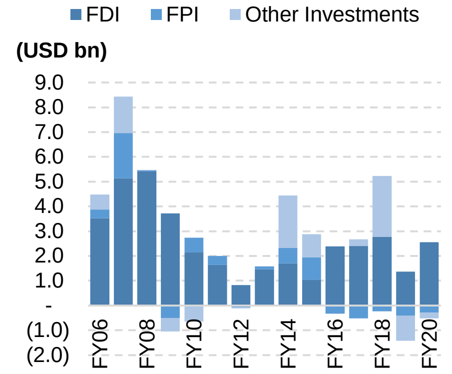


Source (s): SBP, AHL Research

For the remaining period of the current Fiscal Year 2021, we are of the view that the trade balance is still on a shaky ground as global uncertainty escalates. Thus, we foresee trade balance swinging to deficit, in 2HFY21 particularly, as domestic seasonality increases and global uncertainty prevails. The current account will post a deficit of USD 2.5bn (0.9% of GDP) in FY21, we expect. With economic activity expected to pick further pace, import growth is expected to outpace export growth, hence dragging the current account balance. Despite government following a policy of limiting the import of certain products, rationing imports and increasing reliance on local production, we still expect a 2% likely jump in the total imports - goods & services (USD 52bn) in FY21. Furthermore, the SBP introduced new measures to strengthen our exports in these challenging times. However, we believe, primarily due to sluggish global demand, total export- goods & services will remain under pressure in FY21 growing only 3% to USD 29bn.

All told, one bright spot on the Balance of Payment Statement we expect, would be Worker's Remittances (+3% YoY) in FY21 as workers sending money to their families more than usual in this situation of uncertainty will continue its momentum till situation across the globe improves. In addition to this, government is also putting in efforts to attract more foreign investment by offering products like Roshan Digit Account, lucrative rates on government securities, to name a few. Moreover crackdown on unofficial channels such as "Hundi" and "Hawala" have stimulated inflows through official banking channels. Therefore, we expect that Pakistan will be able to attract around USD 24bn (9% of GDP) given global recovery remains uninterrupted.

Fig 04: Share of Capital Importation



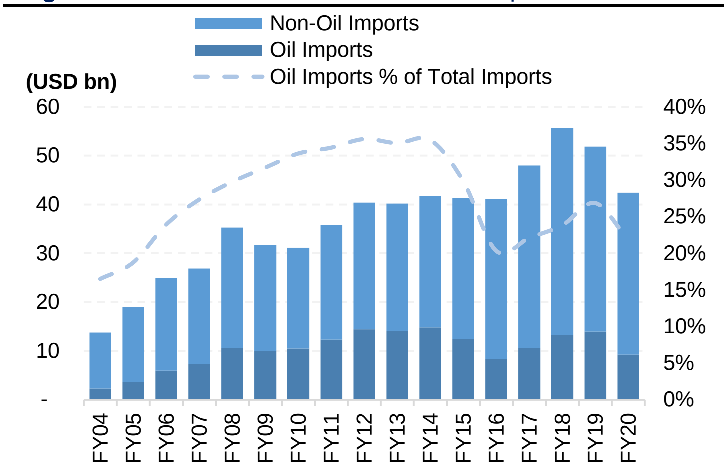
Source (s): SBP, AHL Research

Import Resurgence as Aggregate Demand Inflects

A growth phase of the economy in Pakistan is usually seen to be complemented with deteriorating health of the external account. Imports have contributed an average of 17% to the GDP over the last five years whereas exports have contributed a mere 8% during the said period. We have already witnessed imports ticking up in Sep'20 where it recorded an increase of 18% MoM to USD 4,358mn compared to USD 3,696mn recorded in Aug'20. On a yearly basis, jump was 12% in Sep'20 from USD 3,906mn recorded in Sep'19. The import of goods was up by 15% YoY | 18% MoM during Sep'20. However, the import of services was down by 6% YoY | up 18% MoM during Sep'20. Albeit, FY21 initially saw decline in imports due to depressed aggregate demand in the economy, however resurgence was witnessed post ease in lockdown. With this, 1QFY21 total imports recorded a decline of 8% YoY to USD 12,374mn.

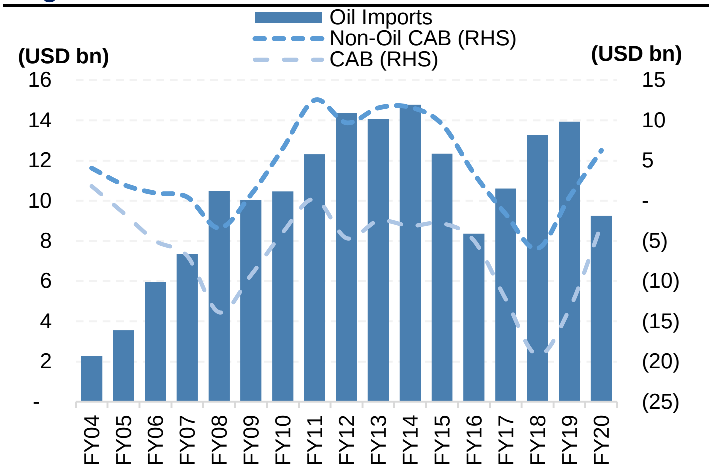
... recovery in consumption to pick up growth in import

Fig 05: Historical Trend of Oil and Non-Oil Imports



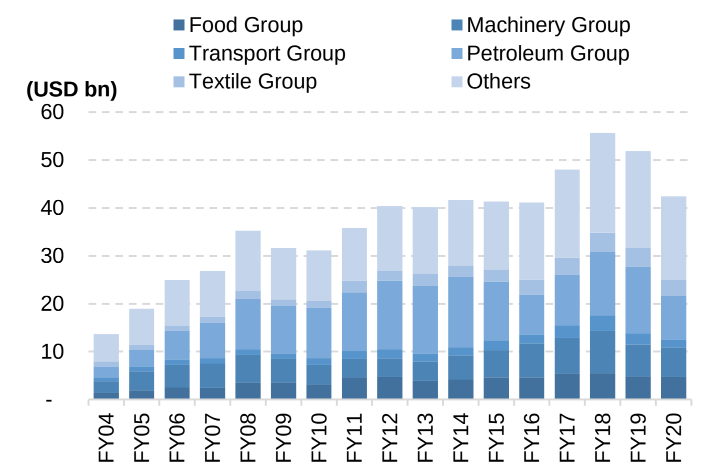
Source (s): SBP, AHL Research

Fig 06: Oil and Non-Oil Current Account Balance



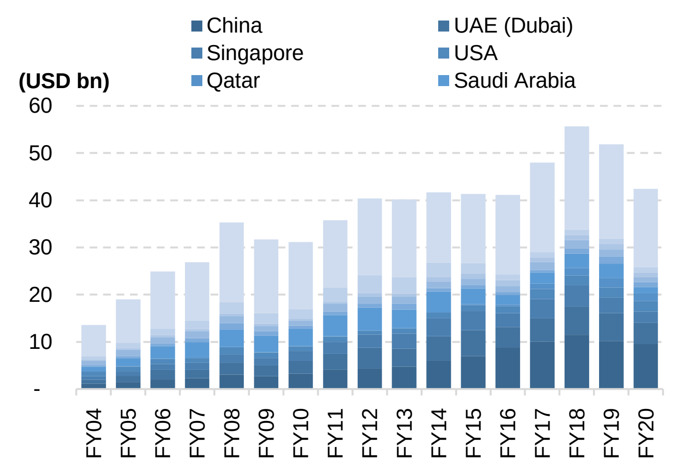
Source (s): SBP, AHL Research

Fig 07: Commodity wise Imports Break-up



Source (s): SBP, AHL Research

Fig 08: Country wise Imports Break-up



Source (s): SBP, AHL Research

As the government is considering a variety of measures to propel demand through an expansionary fiscal policy, we expect goods' imports in upcoming year to expand 4% YoY to settle at USD 44bn. Going forward, we expect the textile category may witness a jump in imports (+26% YoY) as the cotton crop is expected to suffer from locust attacks and monsoon rains. For the same reason, we expect food imports to go up too (+13% YoY) as country has already started importing essentials food items such as wheat and sugar. Moreover, we also anticipate the imports of transport to record a yearly growth of 22%. The machinery group, we expect, may also increase 9% in FY21 as major expansionary cycles of the cement, steel and related sectors are expected to resume once economy starts recovering. By sector, the main drags on overall imports will be primarily led by lower petroleum imports on account of noticeably lower crude oil prices (FY21 average prices assumed at USD 45/bbl vis-à-vis USD 54/bbl in FY20) following the outbreak of COVID-19 which resulted in a drastic slump in global oil demand. We forecast savings of ~USD 2bn p.a. assuming constant volumes. However, as aggregate demand is likely to inflect next year, we believe volumetric growth in petroleum products shall partially offset the savings impact. Petroleum imports contributed 22% to the total import bill in FY20 and are expected to contribute 19% to the bill in FY21.

Table 02: Goods Imports Breakup

USD mn	FY16	FY17	FY18	FY19	FY20	FY21E
Petroleum Group	8,360	10,607	13,263	13,929	9,249	8,463
Agri. & Other Chemicals	6,715	7,123	8,315	8,394	7,043	7,554
Machinery Group	7,097	7,410	8,785	6,768	6,193	6,778
Food Group	4,600	5,417	5,502	4,751	4,711	5,335
Textile Group	3,155	3,589	4,091	3,854	3,305	4,157
Metal Group	3,663	3,674	4,762	3,907	3,229	3,559
Transport Group	1,861	2,643	3,207	2,315	1,513	1,850
Miscellaneous Group	999	1,196	1,256	1,030	789	921
Others	4,668	6,342	6,491	6,919	6,386	5,307
Total	**41,118**	**48,001**	**55,671**	**51,869**	**42,417**	**43,924**

Source (s): SBP, AHL Research

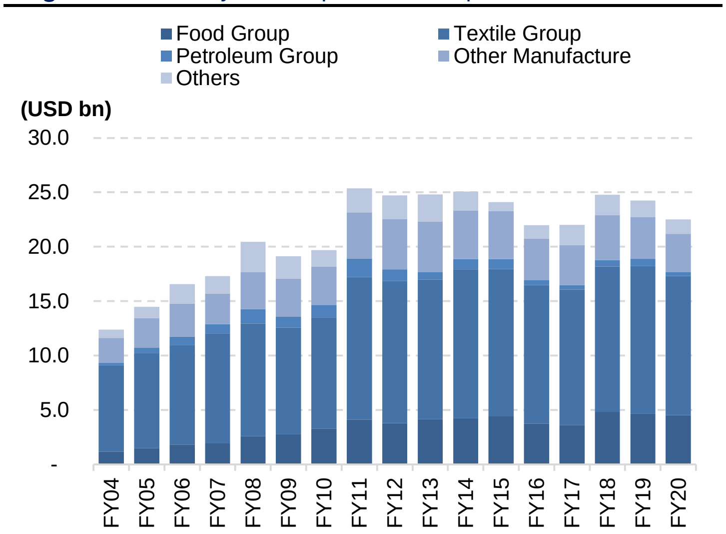
Export: Resilient, despite widening CA Deficit

In order to help prevent export industry to fall into deep trouble with the onset of COVID-19, SBP announced some proactive measures in March'20 which included: reducing performance requirement for availing cheaper credit under Export Financing Scheme (EFS) from 2 to 1.5 times, extension till Dec 20 to perform under EFS, relaxation in conditions for Long Term Financing Facility, etc. These measures along with revival of economic activities have started reaping results recently. We saw total exports (goods and services) increasing by 29% MoM during Sep'20 to USD 2,414mn compared with USD 1,867mn recorded in the previous month. On a yearly basis also, total exports registered an increase of 5% in Sep'20 which stood at USD 2,290mn in Sep'19. The export of goods was up 4% YoY | 29% MoM during Sep'20. Interestingly, the export of services recorded a significant jump of 30% | 13% MoM | YoY during Sep'20. With this, total exports during 1QFY21 stood at USD 6,583mn, which fell 9% short of previous year's same period actual export figures. Nonetheless, we have so far limited the long-term damage and facilitated the recovery, backed by SBP's monetary stimuli and liquidity support.

Going forward, we expect exports of goods to improve by 3% YoY to USD 23bn in FY21. This would hugely depend on trading partners starting their rehabilitation phase more robustly. With the current pandemic situation, Pakistani exporters should focus more on catering demand for medical instruments, health clothing, pharmaceutical products, bed linen, towels, and simple garments and clothing. Exporters can also benefit from rules relaxation and rising prices in EU of food items, vegetables and fruits once supply disruptions and logistic issues are resolved globally.

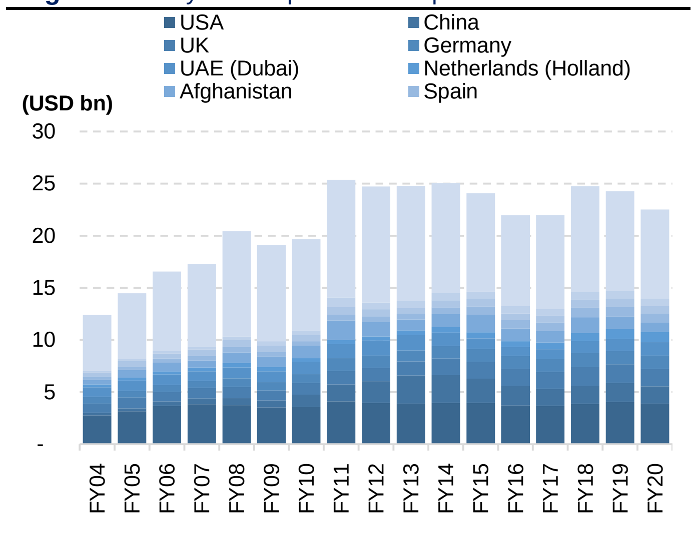
Exports will end the year well, despite initial signs of interruption in recovery - to close Fiscal Year 2021 at USD 23bn

Fig 09: Commodity wise Exports Break-up



Source (s): SBP, AHL Research

Fig 10: Country wise Exports Break-up



Source (s): SBP, AHL Research

We expect a dip of 11% in food category with locust attack affecting crops and clearance of cargoes backlog. In the backdrop of muted global demand, our concerns double when it comes to textile exports of our country. Pakistan's textile sector, which accounts for 55% of total exports, was recently adversely affected by slowdown in manufacturing in China in particular, as the country imports majority of the raw material –dyes & chemicals from this part of the world. However, recent numbers show that textile exports have gone up 13% YoY (USD 3.4bn) in 1QFY21. This is an encouraging sign for the export sector, however downside risks associated with this progress are: cotton crop shortage owing to supply constraints post locust attack and Monsoon for the current season and any uptick in cost of production especially if interest rates go up and also, further energy tariff hikes (if any). Another important factor for textile exports would be PKR/USD parity which we are expecting to reach 161/ USD by Dec-20 end. However, any appreciation of the Rupee from here would put further pressure on textile exports. Our expectation is that the textile segment will post a 6% YoY higher export growth during FY21.

Table 03: Goods Exports Breakup

USD mn	FY16	FY17	FY18	FY19	FY20	FY21E
Textile Group	12,756	12,457	13,377	13,581	12,783	13,566
Food Group	3,722	3,618	4,818	4,648	4,534	4,023
Other Manufacture	3,805	3,659	4,134	3,822	3,502	3,814
Petroleum Group	450	411	575	676	369	449
Others	3,914	5,620	5,269	5,344	4,962	5,108
Total	**21,972**	**22,003**	**24,768**	**24,257**	**22,507**	**23,289**

Source (s): SBP, AHL Research

Remittances: More than Just Money, a Lifeline!

Remittances inflow to Pakistan mounted erratically upward in 1QFY21 clocking in at USD 7,147mn, an increase of 31% YoY. In the month of Sep'20 alone, Pakistan received USD 2,284mn marking a jump of 9% MoM | 31% YoY compared to USD 1,740mn during Sep'19. This was the fourth consecutive month Pakistan reported over USD 2bn remittance inflow. The country wise data reveals that the inflow from KSA, UAE, USA and UK amounted to USD 666mn (+29% YoY, +12% MoM), USD 473mn (+12% YoY, +15% MoM), USD 180mn (+54% YoY, -11% MoM) and USD 289mn (+64% YoY, -4% MoM), respectively. Some of the possible reasons for this uptick are: suspension of international travelling, crackdown on illegal channels of remitting and workers sending money to their families more than usual during the pandemic.

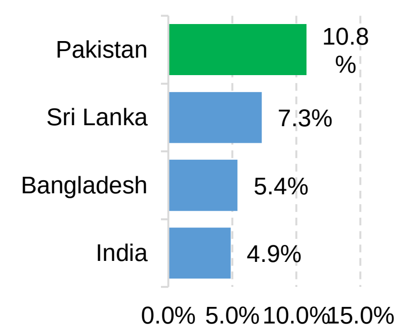
Factors like efforts under the Pakistan Remittances Initiative (PRI), gradual re-opening of major host destinations, Pakistan's crackdown on illegal channels, and curbing illegal financial transactions contributed to higher remittances.

The inflows so far have panned out stronger than expected. In the short term, we can expect the momentum of c.USD 2bn to continue till Dec'20. As the year unfolds, we expect remittances flow to weaken with international economies returning to normalcy. However, seasonal uptick such as in Ramadanis likely to support the inflows. In our opinion, the declining trend in remittances will have adverse repercussions on the economy, not to forget that our Current Account stability is heavily reliant on it. A dent on the remittances level means government will have to borrow more externally to keep foreign exchange reserves intact. Also, remittances sent back home serves as a source of income for families of the migrant workers. As per ADB, around 4% in Pakistan receive remittance income. Hence, a decline would put further pressure on domestic consumption vis-a-vis the overall economic growth of Pakistan.

Regional Comparison

Regional markets too have portrayed high resilience in the recent months, despite the challenging backdrop in terms of the current global health crisis. Initially remittance flows in Asia Pacific region depicted a mixed trend, particularly in the second quarter of CY20. However, the rebound in flows was robust particularly robust in countries like Pakistan and Bangladesh. As seen in Fig 11, most countries in the region like Sri Lanka, Bangladesh and India were well supported by unusual strength in remittances | CAGR 7.3%, 5.4% and 4.9% respectively, over a decade.

Fig 11: Remittances (10-Y CAGR)



Source (s): World Bank, SBP, AHL Research

Table 04: Country Wise Remittances

USD mn	FY16	FY17	FY18	FY19	FY20	FY21E
Saudi Arabia	5,968	5,470	4,859	5,003	6,613	6,838
UAE	4,365	4,328	4,333	4,617	5,612	5,485
Other GCC Country	2,423	2,325	2,158	2,119	2,910	2,848
UK	2,580	2,342	2,763	3,412	2,569	2,846
USA	2,525	2,453	2,714	3,309	1,743	1,913
EU Countries	418	483	656	609	1,778	1,848
Others Countries	1,638	1,951	2,139	2,670	1,907	2,021
Total	**19,917**	**19,351**	**19,622**	**21,739**	**23,132**	**23,799**

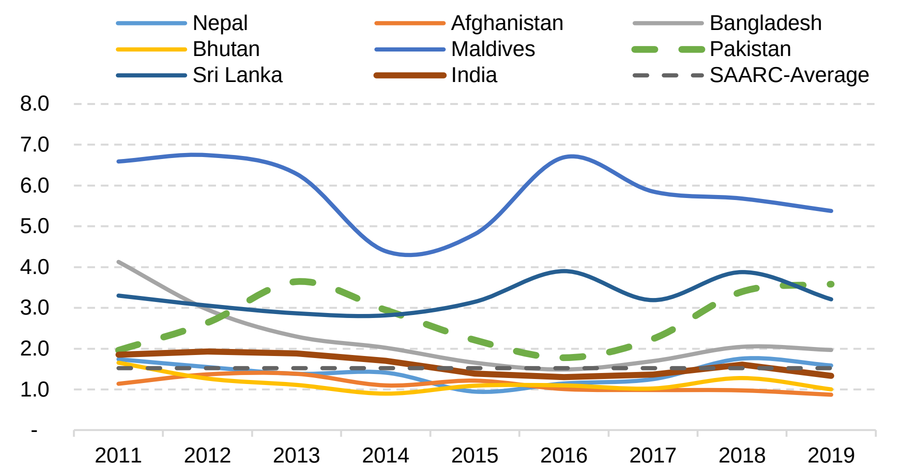
Source (s): SBP, AHL Research

Adequate Reserves to Buffer Depreciation Pressures

Pakistan's international forex reserves rose to USD 19.4bn in Oct-20 from USD 17.9bn at the end of Dec-19. At almost 2.9 months of imports coverage, Pakistan's foreign reserves are slightly below the IMF's minimum 3 months threshold. Compared to regional players, Pakistan stands well above the average Import Cover of the countries graphically illustrated in Figure 12. Moreover, an increase of PKR 248bn in Net Foreign Assets (NFA) of Pakistan's banking system in 1QFY21 is also reflected in Foreign Exchange Reserves. Causes of this increase in Net Foreign Assets was a Current Account Surplus along with deferment of some repayments of foreign loans which helped ease off pressure from foreign exchange reserves of the country. Another important external account related indicator i.e. Net Domestic Assets (NDA) to NFA ratio, turned negative as NDAs of the banking system went into negative. The Net Foreign Assets of the banking system witnessed an inflow of PKR 992bn during the past FY20.

What does NDA/NFA ratio depict? It speaks a lot about the strength of the currency and the stability of the financial system. If there is a continuous outflow of foreign exchange from the country and the currency continues to depreciate, inflationary pressure will surface and confidence in the domestic financial system will decrease significantly as prices of goods and services would spiral.

Fig 12: Import Cover



Source (s): SBP, World Bank, AHL Research

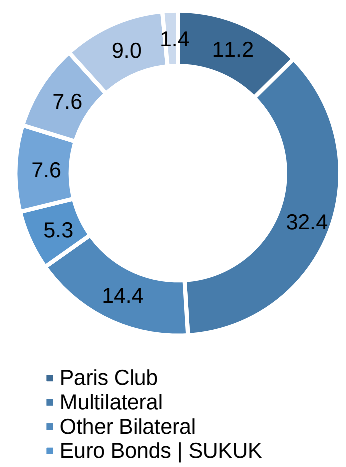
The total external debt repayment of USD 10.3bn comprises of USD 8.5bn as principle payment of loans and USD 1.8bn as interest repayment.

With the current level of reserves, Pakistan faces increasing external debt servicing pressures as the amount due in FY21 is USD 10.3bn. As per Economic Affairs Division's Monthly Bulletin (Sept 2020), Pakistan received USD 2.7bn in 2MFY21 from multiple sources, break-up of which is as follows:

- USD 1.3bn as program/budgetary support assistance to restructure the economy,
- Commercial Borrowing to repay maturing Sukuk and foreign commercial loans USD 149mn
- Assistance for development of the economy USD 317mn
- Safe deposits USD 1bn

On the other hand, so far USD 798mn has been repaid in the first two months of FY21 and the remaining amount (over USD 9.5bn) is to be paid in the next 10 months.

Fig 13: Public Debt



Source (s): SBP, AHL Research

Table 05: External Position (Inflows vs. Outflows) - FY21E

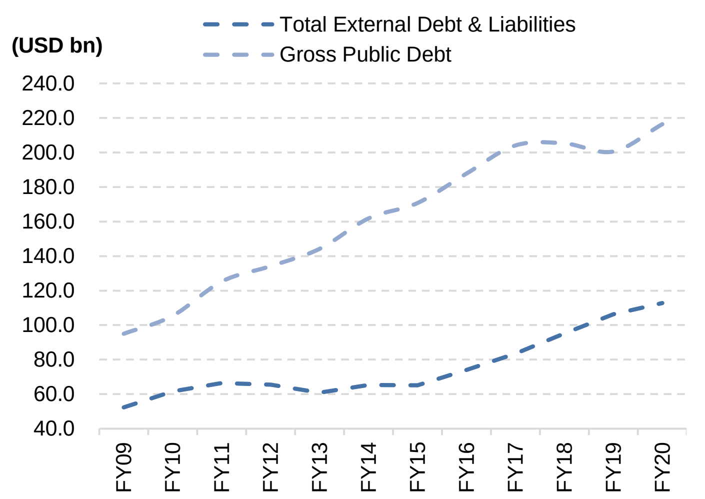
Outflows (USD mn)			(12,057)	Inflows (USD mn)	13,604
External Public Debt Servicing				IMF	904
	Estimates	**Actual**		Multilateral-ADB/WB	2,100
Bilateral	(2,142)	(102)	(2,040)	Commercial	4,000
Multilateral	(2,114)	(493)	(1,621)	Received from Multiple Sources in 2MFY21	2,700
Commercial	(4,353)	(204)	(4,149)	Net FDI	1,600
Eurobond | SUKUK	(440)	-	(440)	Eurobond | SUKUK	1,500
IDB (Short-term)	(1,194)	-	(1,194)	Others*	800
IMF	(120)	-	(120)	**Expected Increase in FX reserves- as at Jun'21**	**1,547**
Total			**(9,564)**	**Actual Reserves- SBP (As at Jun'20)**	**12,132**
Current Account Balance			**(2,493)**	**Expected Reserves- SBP (As at Jun'21)**	**13,679**

Source (s): SBP, AHL Research, *RDA, Hot Money and SBP Purchases

Pakistan will be relying on financing from IMF and other bilateral partners to meet its external debt requirements in FY21. We have assumed that the net increase in FX reserves during FY21 would amount to USD 1.5bn.

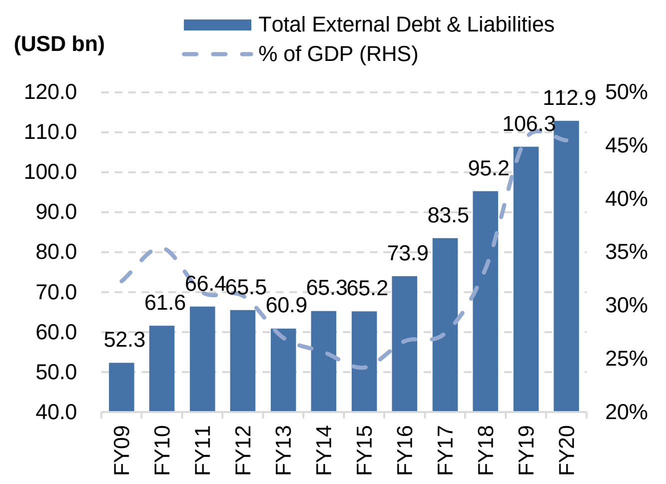
- The Government is likely to raise USD 1.5bn from Euro bonds and Sukuk; USD 200-300mn Panda Bonds inclusive.
- Continuation of the IMF EFF (Extended Financing Facility): USD 904mn expected.
- Other multilateral inflows including ADB and World Bank worth USD 3-3.5bn.
- Others including, Roshan Digital Accounts/Naya Pakistan Certificates, Hot money and SBP purchase: expected amount USD 800mn.
- Commercial Borrowings expected around USD 4-5bn (USD 2.5bn rolled over amount- China)

Fig 14: External and Public Debt



Source (s): SBP, AHL Research

Fig 15: Historical Trend of External Debt



Source (s): SBP, AHL Research

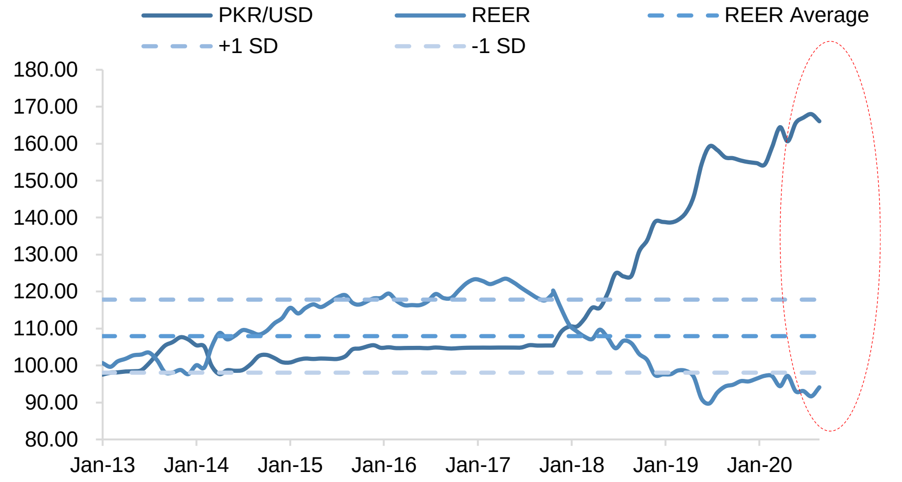
‘Push and Pull factors’ to keep the Parity Volatile

State Bank adopted Market Determined Exchange rate along with stringent targets to rebuild foreign exchange reserves (Net International Reserves). We saw PKR appreciating 4.9% against greenback during 4MFY21. This recent jump was attributable to: uptick in remittance inflows (around USD 2bn per month since the beginning of FY21), current account surplus of USD 792mn in 1QFY21 after more than five years (last time a surplus was recorded was in 3QFY15), dollar weakening against all major currencies (the dollar index is down 10% since March), deferment of USD 1.8bn loan repayment to G20 till December 2020 – with a further relaxation anticipated till June 2021 and expected improvement in inflows with the launch of Roshan Digital Account. If we look at the parity few years back, the Pak Rupee remained significantly overvalued in terms of REER (Real Effective Exchange Rate) from 2016 till 2018 (between 107-117). Following the onset of the depreciation era that initiated in Dec’17, the REER began its downwards journey, coming down to 101.5 in Nov’18. However the PKR/USD parity continued to slide further touching a high of PKR 169/USD in Aug’20. The REER fell further, going down to 91.8 in Aug’20. This shows, REER has been continuously declining since Nov’18. Recently, as the currency experienced significant adjustment (4.9% appreciation in 1QFY21) resulting in increase of REER to 94.1199 (as at Sep’20). Therefore, majority of the overvaluation of PKR before 2018 has been corrected thereby instilling confidence in Foreign Investors. Considering the Real Effective Exchange Rate (REER) for the Pakistan over this fiscal year, the local unit has appreciated to its highest level of PKR 158.49 (on 11-Nov-20). The REER is currently below the lower standard deviation band (implying that it is undervalued).

The real effective exchange rate (REER) is the weighted average of country’s currency in relation to an index or basket of other major currencies, adjusted for the effects of inflation.

We expect PKR/USD to clock-in at 161 by Dec’20.

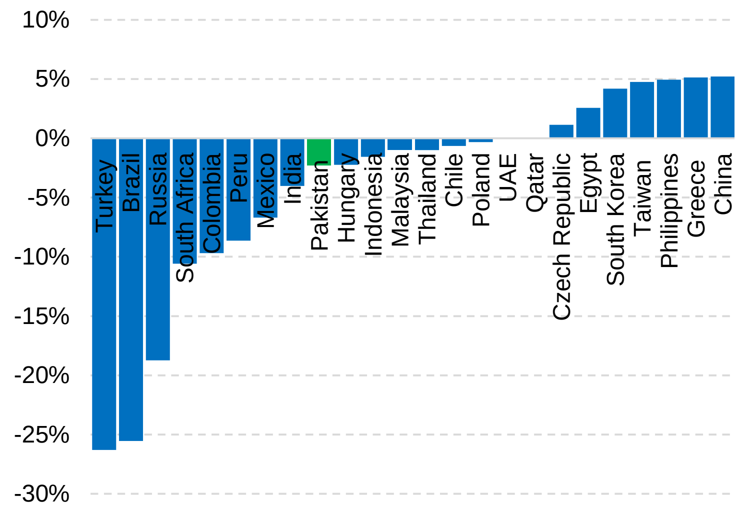
Fig 16: Real Effective Exchange Rate



Source (s): SBP, AHL Research

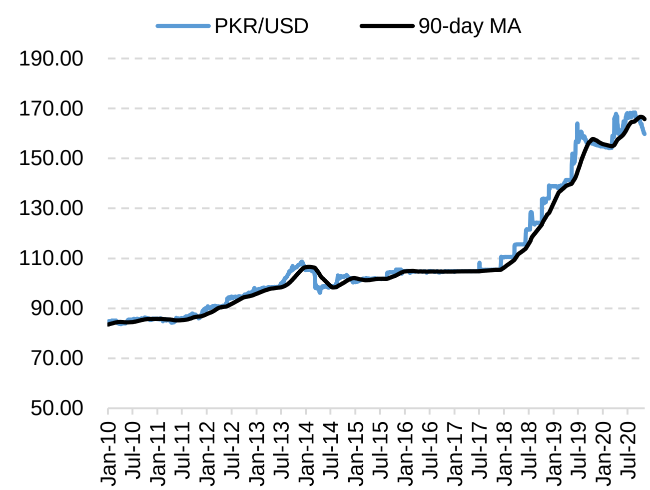
We expect PKR to be 161/ USD by Dec’20 with REER inching up. We expect SBP to adopt greater flexibility in the short term, allowing PKR to appreciate, but still accumulate more reserves. While in the short-term SBP may sterilize excess liquidity by selling government securities to ward-off a further flaring up of the headline CPI inflation, an enduring solution could be to use the inflow of capital for real investments and capacity creation, thereby managing growth, inflation and financial conditions consistently and positively. In the longer term, there are a few key considerations such as i) addressing the speculations on heavy external borrowing by GoP, ii) the repayments scheduled from 2HFY21 onwards, and iii) widening CA deficit will put pressure on the PKR/USD parity which is expected to reach 165 per USD by Jun'21. Though currency depreciation is a concern for the economy, it should largely be taken as positive since it benefits key market-driving sectors as far as their short-term profitability is concerned. Such as IPPs (USD-based ROE), Textiles (for improved exports), E&Ps (product pricing in USD), while the situation stands neutral to negative for Cements (raw material imports), neutral to positive for Fertilizer (FFBL's USD based DAP primary margins) and negative for OMCs (FX losses), Autos, Pharmaceuticals and Consumer sectors.

Fig 17: EM Currency Change vs. US dollar (CY20TD)



Source (s): SBP, AHL Research

Fig 18: PKR/USD Spot Performance



Source (s): SBP, AHL Research

Glossary

1H	First Half
1Q	First Quarter
2H	Second Half
2Q	Second Quarter
3Q	Third Quarter
4Q	Fourth Quarter
ADB	Asian Development Bank
bn	Billion
BOP	Balance of Payment
c	Approximately
CA/CAB	Current Account Balance
CAGR	Compounded Annual Growth Rate
CPI	Consumer Price Index
CY	Calendar Year
E	Expected
EM	Emerging Markets
EU	European Union
F	Forecasted
FY	Fiscal Year
GCC	Gulf Cooperation Council
GDP	Gross Domestic Product
GIS	Govt. Ijarah Sukuk
GoP	Government of Pakistan
IMF	International Monetary Fund
Mio/ Mn	Million
MoM	Month on Month
NDA	Net Domestic Assets
NFA	Net Foreign Assets
PKR	Pakistani Rupee
QoQ	Quarter on Quarter
RDA	Roshan Digital Accounts
REER	Real Effective Exchange Rate
RoE	Return on Equity
SBP	State Bank of Pakistan
SPLY	Same Period Last Year
Trn	Trillion
UK	United Kingdom
USD	United States Dollar
YoY	Year on Year

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Rating	Description
BUY	Upside* of subject security(ies) is more than +10% from last closing of market price(s)
HOLD	Upside* of subject security(ies) is between -10% and +10% from last closing of market price(s)
SELL	Upside* of subject security(ies) is less than -10% from last closing of market price(s)

* Upside for Power Generation Companies is upside plus dividend yield.

Equity Valuation Methodology

AHL Research uses the following valuation technique(s) to arrive at the period end target prices;

- **Discounted Cash Flow (DCF)**
- **Dividend Discounted Model (DDM)**
- **Sum of the Parts (SoTP)**
- **Justified Price to Book (JPTB)**
- **Reserve Base Valuation (RBV)**

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The following risks may potentially impact our valuations of subject security (ies);

- **Market risk**
- **Interest Rate Risk**
- **Exchange Rate (Currency) Risk**

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