Wealth Management Advisory
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Pakistan Market Outlook

The economic cycle

State Bank has raised rates twice in Q1-2019 and may continue to do so. We maintain our liking for short to medium tenor government bonds.

Pakistan equity market can rebound for the short term based on attractive valuations. However we remain cautiously bullish for the long run.

So far an IMF programme has been difficult to reach. We expect further PKR adjustments.

Macro overview

The economic cycle

- GDP growth likely to soften in FY19, but domestic demand will provide some support.
- To stabilize the economy SBP is expected to remain on course of monetary tightening along with further PKR adjustments and fiscal consolidation.
- PK equities may recover in the near term if economic indicators show signs of stabilization, however delay in IMF bailout and CPEC related projects, political uncertainty and balance of payments issues are key risks that would significantly alter this outlook.

Asset Classes	View	Rates policy	Macro factors
2 Year bond	▲	●	●
10 Year bond	▼	●	●
KSE 100 Index	▲	●	●

Source: Standard Chartered Wealth Management Pakistan Investment Committee

Legend: ● Supportive ● Neutral ● Not Supportive ▲ Preferred ▼ Less Preferred ◆ Core

Macro adjustments slow economic growth

Government is expected to enter into an IMF programme in Q2-2019; conditions are likely to include further macro adjustments and PKR deprecation to address country's twin deficits.

The State Bank of Pakistan has been on course of monetary tightening since Jan 2018. In its recent monetary policy meeting held on Friday 29th March 2019, the SBP raised interest rates by 50basis points, higher than the 25bps increase in previous meeting in Jan 2019. So far SBP has raised 425bps since Jan 2018 & 75bps in Q1-2019 alone. SBP is likely to stick to a tight monetary stance in 2019 to control aggregate demand, inflationary pressures and deteriorating fiscal deficit.

As authorities take corrective measures to stabilize the economy we expect the growth to considerably slow down in FY19 vs. 5.8% in FY18. However we believe firm domestic demand and projects under China Pakistan Economic Corridor will support growth and economic activity in the medium term.

So far the government has not been able to curtail Pakistan's fiscal deficit which rose to 2.7% of GDP in first half of FY19 compared to 2.2% of GDP during the same period of the last fiscal year. Due to domestic and foreign debt servicing along with federal and provincial spending country's fiscal deficit is projected between 6-7% of GDP in FY19, from 6.6% in FY18.

IMPLICATIONS
FOR INVESTORS

GDP growth is expected to slow down in FY19 from 5.8% in FY18 as authorities take measures for macroeconomic adjustments

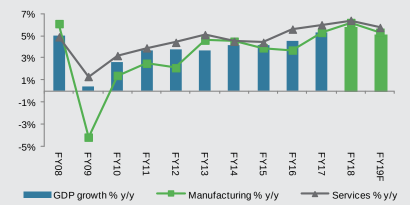
IMF programme likely delayed not derailed

CPEC related projects and domestic demand will continue to positively drive the business sentiment and economic activities

Figure 1

GDP growth likely to slow down in FY19

Pakistan real GDP, manufacturing and services growth and consensus forecasts (Bloomberg consensus)



Source: PBS, SBP, Bloomberg, Standard Chartered

Bond yields increasingly attractive

SBP's tight monetary stance has facilitated PKR bond yields to become increasingly attractive offering a significant risk free return (1yr bond is offering a yield of 11.2%).

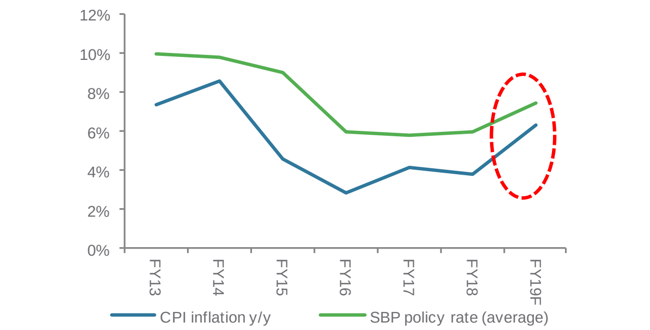
Side by side Inflation has risen considerably in FY19 and may continue to rise in the near term as a result of higher customs and regulatory duty on a range of imported items, rising oil and energy prices following the PKR's depreciation.

The pace of rising inflation and interest rates may gradually slow down in the second half of the year as policy makers engineer a soft landing for the economy. However more than forecasted increase in inflation or oil prices and widening fiscal deficit are key risks to the bond markets.

Figure 2

Inflation likely to rise going forward

Pakistan CPI y/y and SBP discount rate (FY average)



Source: PBS, SBP, Bloomberg, Standard Chartered

PK Equities attractive valuations: near term growth outlook at risk

KSE100 Index posted a return of 4.3% in Q1-2019. The local bourse managed to stay in green after securing support package from UAE & Saudi Arabia. Corporate earnings announcement turned out to be a mixed bag throughout Q1-2019 and added to market volatility.

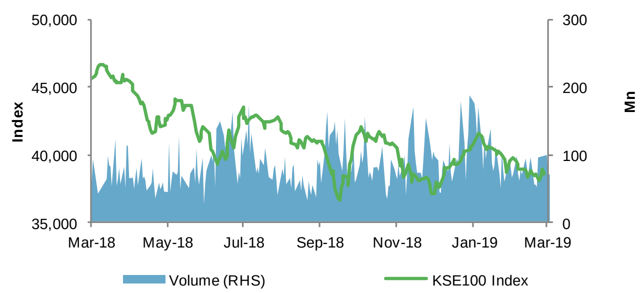
Average traded volume decreased in the first quarter of 2019 as investors shy away from the stock market due to delay in IMF programme, risk of downgrade to frontier markets and vibes of economic slowdown in the country. In line with our expectations foreigners were net buyers in the first quarter of 2019.

PK equities may recover in the near term if economic indicators show signs of stabilization, however delay in IMF bailout and CPEC related projects, political uncertainty and balance of payments issues are key risks that would significantly alter this outlook.

Figure 3

KSE100 Index trading below key resistance level of 40,000pts

KSE100 index and Volume (RHS)



Source: PBS, SBP, Bloomberg, IMF, Standard Chartered

PKR- Stabilization polices likely to include further weakness

Pakistan's current account deficit narrowed 22.5% to US$8.844 billion during the first eight months (Jul-Feb) of the current fiscal year of 2019 owing to decrease in import bill as well as increase in exports and home remittances . Current account deficit shrunk US$2.57 billion from US$11.42 billion during the corresponding period a year earlier.

More over in absence of an IMF programme allies of Pakistan like (China, Saudi Arabia and UAE) have provided external financing that has supported SBP's FX reserves. While these are welcome signs, the balance of payments issue is far from over and Pakistan will likely enter into an IMF programme in Q2-2019. We expect further PKR weakness under an IMF programme.

Disclosure appendix

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