

## PAKISTAN-IMF STAFF LEVEL AGREEMENT

Better late than never

Monday, July 3, 2023

Following long and inordinate delays and a push at the 11th hour, Pakistan has finally been able to reach Staff Level Agreement (SLA) with the IMF on a USD 3Bn Stand-By Arrangement (SBA). The agreement will be subject to approval from the IMF's Executive Board which is expected to meet around mid-July. The long awaited agreement which has been delayed by around 8 months comes right at the tail end of the program tenure which was set to run until Jun 30th, 2023. Amid a combination of sovereign default risk looming large, dwindling forex reserves, weakening PKR, runaway inflation and historic interest rates, the agreement comes as a sigh of relief for the short term but also with a reminder that structural reforms are the need of the hour. We expect KSE-100 to cheer the agreement having been marred by thin participation and weak investor sentiment with improved confidence amid reduced macroeconomic concerns, at least in the short-term.

**What did the IMF statement say?** The IMF highlighted that the immediate focus of the SBA is to bring stability to the economy from external shocks, ensuring macroeconomic stability and arranging foreign financing from multilateral/bilateral partners to create some breathing space on the burgeoning external front. Furthermore, the SBA is aimed at enhanced revenue mobilization and fiscal discipline to ensure social and development spending. While the IMF appreciated recent policy measures taken by the govt. to restore the program, the hint was clear that more needs to be done. On the reforms front, the IMF remained steadfast in sticking to strict policy implementation primarily through prudent fiscal policy, adherence to the FY24 budget, power sector reforms and a tight monetary policy not only to supplement fiscal austerity but also to keep a lid on runaway inflation.

**The road ahead:** Despite breaking the deadlock with the IMF, long term structural reforms are the need of the hour. Though the SBA will prove instrumental in addressing the short term liquidity concerns and paving way for inflows from multilateral/bilateral partners, strict adherence to long term structural reforms and fiscal austerity are imperative. We have repeatedly highlighted the need for a bigger and longer successor IMF program following the conclusion of the current in order to ensure policy implementation and the adoption of long due tough measures.

IMF has repeatedly highlighted at abolishing import restrictions, a free-float based exchange rate, power sector reforms, the need to curb inflation and solution to cash bleeding SOE's as the primary steps to kick-start the reforms process. In the short term, we can expect upward revision in energy tariffs, limited development spending, a tight monetary policy and increased activity on the SOE's front (UAE deal with KPT being a case in point). On the currency front, we can expect greater flows from ex-pats and exporters which will help in settling the PKR/USD parity around the 270 mark.

Given the design of the SBA where USD 3Bn will be disbursed in 3 installments, the program will be completed after the new government assumes office. This, we opine works out for the new govt. as it will have a clear direction on the economic front and could start afresh with the aid of a new IMF program and the sense of having a 5-year mandate to smoothly achieve the same.

**Market vantage point:** The SBA will bring back much needed investor confidence and flows into the market, in our view. There is no doubt about the multi-decade cheap multiples the KSE-100 trades at (FY24E P/E: ~3.0x, D/Y: >10%) and the recent development will provide the investor base much needed impetus to unlock valuations. Increased participation is expected to be spearheaded by individuals and local institutions while PKR stability can also attract foreigner interest. We remain OW in Banks, E&P's, Fertilizers, Cements and IT.

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**BMA Capital Management Ltd.**

IMF - Staff Level Agreements and Board Approvals			Days from SLA to	KSE 100	Index Returns (Before)		Index Returns (After)	
Date	Action	Facility	Board Approval	Index	3Months	6Months	3Months	6Months
29-08-22	Board approval for 7th and 8th reviews	EFF	46	42,504	-4.9%	-4.4%	-0.3%	-4.7%
14-07-22	SLA for 7th and 8th reviews 1.17Bn	EFF		42,349	-5.2%	-7.5%	-0.9%	-4.8%
03-02-22	Board approval for 6th review	EFF	74	45,863	3.0%	-2.3%	-12.5%	-10.5%
21-11-21	SLA for 6th review 1.06Bn	EFF		46,489	4.6%	1.3%	-2.4%	-7.3%
24-03-21	Board approval for 2-5th reviews	EFF	36	45,544	3.1%	8.9%	5.3%	-1.0%
16-02-21	SLA for 2-5th reviews 0.5Bn	EFF		46,868	6.2%	16.3%	-2.3%	0.1%
16-04-20	Board approves 1.386Bn disbursement under RFI	RFI	49	31,329	-28.5%	-8.6%	18.1%	28.2%
27-02-20	SLA of 2nd review	EFF		38,087	-13.0%	24.5%	-11.2%	7.9%
19-12-19	Board approves first review 0.45Bn	EFF	41	40,655	-7.0%	17.3%	-25.9%	-17.8%
08-11-19	SLA reached for first review	EFF		35,978	-17.6%	2.7%	11.6%	-7.5%
03-07-19	Board approves 6Bn 39 month EFF, 1Bn disbursement	EFF	52	34,897	-19.9%	-7.0%	-6.1%	21.3%
12-05-19	SLA reached for EFF	EFF		45,175	3.8%	9.9%	-34.9%	-18.6%
28-09-16	Board approves 12th review, 100Mn	EFF	55	40,355	-5.2%	22.6%	17.5%	20.2%
04-08-16	SLA for 12th Review	EFF		39,447	-7.2%	21.5%	6.1%	25.6%
27-06-16	Board approves 11th review, 0.5Bn	EFF	46	37,040	-12.8%	14.0%	8.8%	26.7%
12-05-16	SLA for 11th review	EFF		36,049	-15.0%	5.2%	10.7%	18.9%
25-03-16	Board completes 10th review, 0.5Bn	EFF	50	32,877	-22.4%	0.2%	13.7%	21.0%
04-02-16	SLA for 10th review	EFF		32,479	-23.2%	-9.6%	8.7%	21.5%
18-12-15	Board approves 9th review, 0.5Bn	EFF	43	32,777	-22.4%	-5.5%	0.9%	18.3%
05-11-15	SLA on 9th review	EFF		34,455	-18.5%	1.3%	-5.7%	4.3%
28-09-15	Board approves 8th review, 0.5Bn	EFF	52	32,690	-22.5%	9.1%	0.0%	0.7%
07-08-15	SLA on 8th review	EFF		36,223	-14.0%	4.5%	-5.0%	-10.3%
26-06-15	Board approves 7th review, 0.5Bn	EFF	46	33,885	-19.5%	5.9%	-3.1%	-4.1%
11-05-15	SLA on 7th review	EFF		32,506	-22.7%	3.9%	11.4%	4.4%
27-03-15	Board approves 6th review, 0.5Bn	EFF	50	29,958	-28.7%	0.8%	13.1%	9.6%
05-02-15	SLA on 6th review	EFF		34,672	-17.3%	16.8%	-3.3%	4.3%

Source: IMF, PSX, BMA Research

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Buy	>15% expected total return
Hold	10%-15% expected total return
Underperform	<10% expected total return
*Total stock return = capital gain + dividend yield	

### Old rating system

Overweight	Total sector return > expected market return
Marketweight	Expected market return
Underweight	Total stock return < expected market return

## Valuation Methodology

To arrive at our period end target prices, BMA Capital uses different valuation methodologies including

- Discounted cash flow (DCF, DDM)
- Relative Valuation (P/E, P/B, P/S etc.)
- Equity & Asset return based methodologies (EVA, Residual Income etc.)