

PAKISTAN



Pakistan Economy

June CPI to be 10.1% YoY

MoM inflation to be 0.1%

National CPI is expected to clock in at 10.1% YoY in June'21 (vs 10.9% YoY last month). In MoM comparison, inflation is estimated to be a modest 0.1% as uptick in electricity prices given fuel charges adjustment would be offset by decline in food prices. This would result in average inflation of 8.9% during FY21.

We foresee average inflation of 8.1% in FY22 given higher forecasted YoY International oil prices in our base case of no increase in electricity tariff. In case electricity tariff is increased as per IMF requirements, it would take up average inflation to ~9.3% YoY in FY22.

Modest uptick in inflation expected

We expect June'21 CPI YoY reading to be around 10.1% vs 10.9%/8.6% in May'21/June'20. CPI on MoM basis is expected to be mere 0.1% during June as fall in food prices (~34.6% weight in CPI) would be balanced by a corresponding uptick in electricity prices (4.1% weight in CPI) given higher fuel charges adjustment in electricity prices during the month. In the food head, prices of chicken and bananas were substantially lower during June'21.

Inflation has been 8.8% YoY in 11MFY21 (vs 10.9% YoY in 11MFY20) mostly due to high food inflation (12.6/13.5% YoY in Urban/Rural in 11MFY21 – see Fig 1) as core inflation (non-food, non-energy) has been relatively stable (5.9/7.6% YoY in Urban/Rural in 11MFY21 vs 7.6/8.7% in 10MFY20), in line with moderate underlying demand in the economy. High food inflation stems from supply disruptions caused by non-availability of quality seeds, weak commodity management, tighter border control, untimely/torrential rains and higher international food prices.

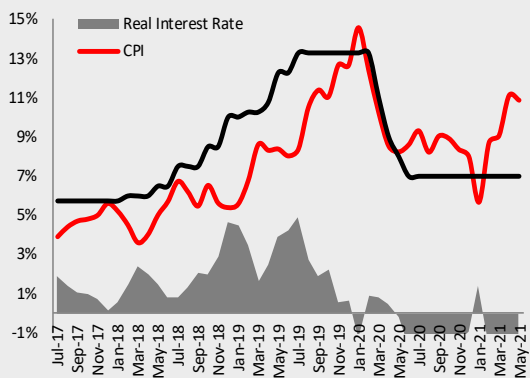
Deadlock with IMF to be resolved soon

The 6th review of the IMF program was supposed to be concluded in early June following which 4th tranche of US\$1.1bn was to be disbursed. However, IMF staff and Gov't have been unable to reach an agreement with major stumbling points of (1) energy tariff hike and (2) budgetary tax measures. This has not only delayed disbursement of the US\$1.1bn IMF tranche but also postponed US\$1.0bn loans from World Bank and Asian Development Bank. We feel that Gov't plan (1) to resolve circular debt and (2) implement structural reforms would result in resolution of deadlock with IMF within 3-6 months.

During 11MFY21, current account recorded a surplus of US\$153mn which has been underpinned by record remittances (up by US\$6.1bn or 29% YoY in 11MFY21). However, we note with consternation that goods imports have touched levels last seen during FY18 balance of payments crisis (see Fig 5). This presents a risk to CAD outlook if (1) import volumes increase (given higher Gov't economic growth target) or (2) commodity prices rise further or (3) remittances normalize. To highlight, currency has depreciated against the greenback by 2.4/2.4/1.8% during last 1/2/3 months but reserves have remained stable.

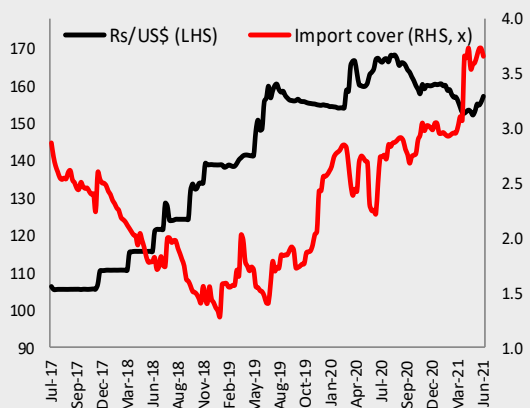
It is worth mentioning that as economic growth continues accelerating, any policy measures to curtail runaway domestic demand (and hence imports) would take time to work their way through the economy and we expect a lag of 6-12 months before such actions start bearing fruit. Thus, barring any immediate policy actions, we expect imports would remain elevated during much of FY22.

CPI vs policy rate



Source: SBP, Foundation Research, June 2021

Rupee against greenback



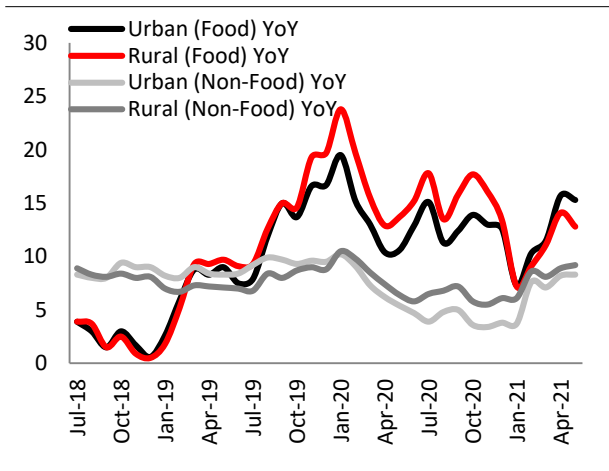
Source: SBP, Foundation Research, June 2021

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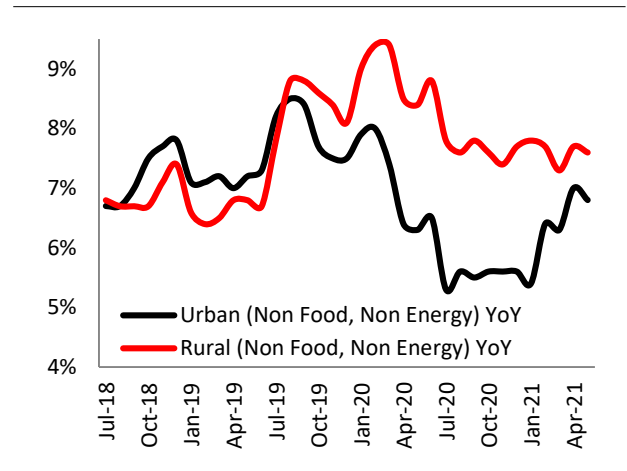
Foundation Securities (Pvt) Ltd
Wednesday, June 30, 2021

Fig 1: Inflation has recently shown resurgence...



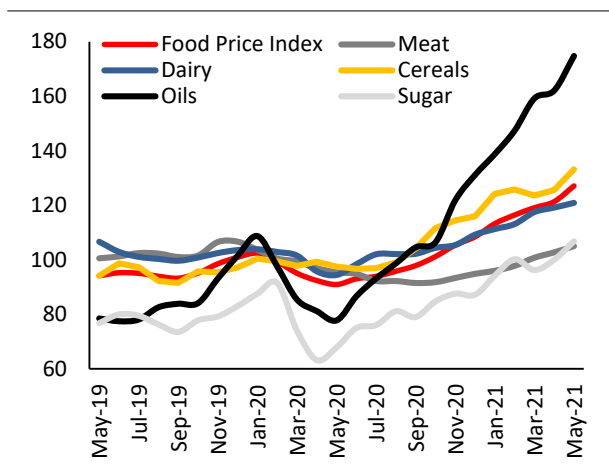
Source: PBS, FSL Research, June 2021

Fig 2: Urban core inflation also showing upsurge...



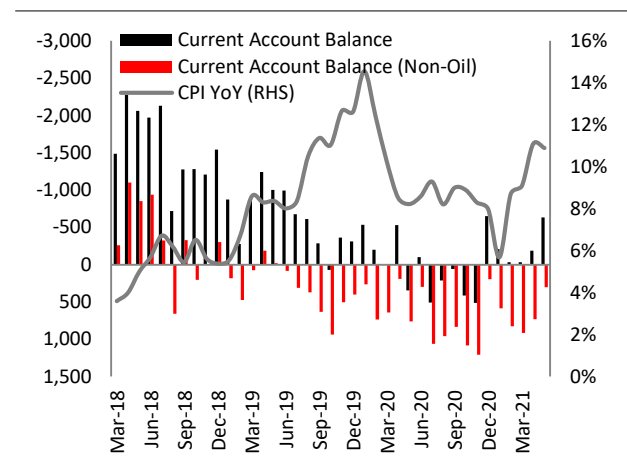
Source: PBS, FSL Research, June 2021

Fig 3: Int'l food prices keep marching upwards...



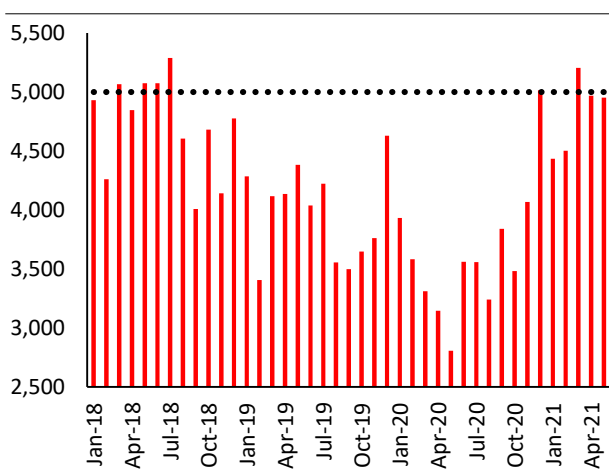
Source: FAO, SBP, FSL Research, June 2021

Fig 4: Current account and CPI...



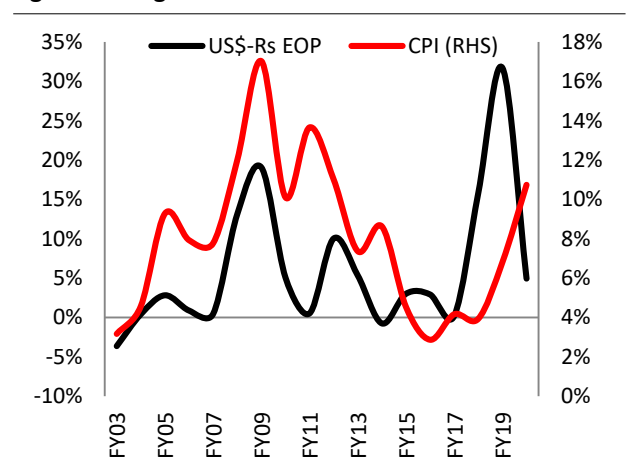
Source: SBP, PBS, FSL Research, June 2021

Fig 5: Goods import rise to FY18 levels (US\$ bn)



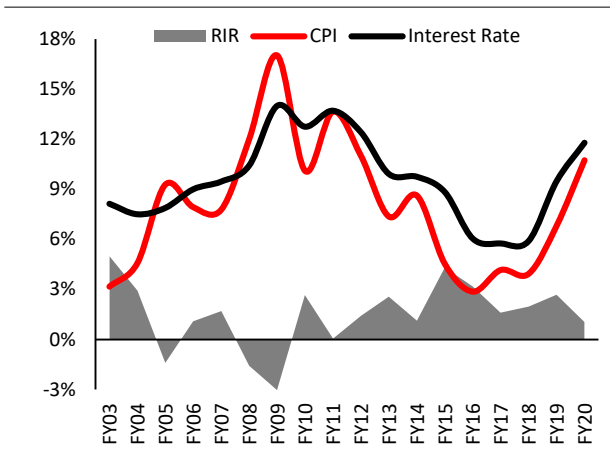
Source: SBP, FSL Research, June 2021

Fig 6: Exchange rate and inflation move in tandem



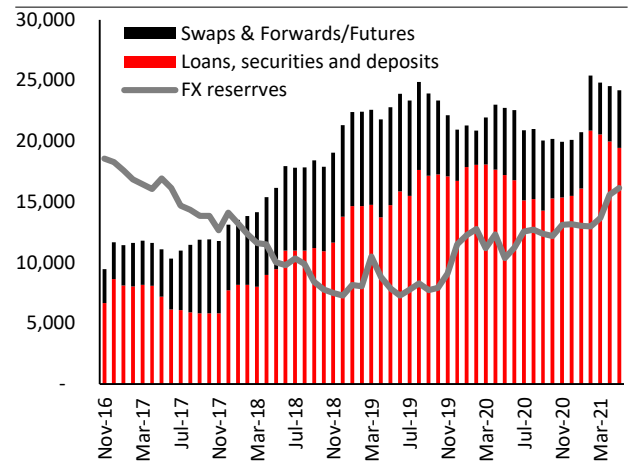
Source: Bloomberg, SBP, FSL Research, June 2021

Fig 7: Inflation and interest rate over the long run



Source: PBS, SBP, FSL Research, June 2021

Fig 8: SBP FX reserves lower than o/s 1yr liabilities



Source: SBP, FSL Research, June 2021

Abbreviations

- FX Foreign Exchange
- MoM Month on Month
- YoY Year on Year

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Recommendations definitions

- If Expected return >+10% Outperform.
- Expected return from -10% to +10% Neutral.
- Expected return <-10% Underperform.