



## AKD Securities Limited

TREC Holder & Registered Broker  
Pakistan Stock Exchange

Equity Research / Pakistan



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### Today's Daily

#### ■ Economy: Turkish tensions rile the shores of emerging markets

Recent episodes of volatility in emerging market currencies, headlined by the Lira (38.6% depreciation in CY18TD), Indian Rupee (8.9%), Argentine Peso (37.7%) and South Africa Rand (15.0%) have elevated fears of a global financial contagion. This has partly been fueled by strengthening of the dollar index (up 7.6% since Apr'18) due to rising US interest rate profile accompanied by fiscal stimulus (tax relief). Additionally, global factors including concurrent global monetary tightening, higher oil prices, possible trade disputes on top of heightened geopolitical tensions have raised serious concerns over the stability of emerging economies, with economies reliant on dollar borrowing are in the crosshairs. Closer to home, Pakistan's ability to absorb external shocks in the event of a financial contagion remains very low considering depleting reserves and external sector woes. Within this view, strengthening of dollar index and rising volatility of emerging market currencies reinforce our case of another ~6.4% depreciation from current levels (parity at PkR133/US\$ by Jun'19).

#### KSE100 - Index

Current 42,446.56  
Previous 42,637.59  
Chg. -0.45%

#### Mkt Cap. (PkRbn/US\$bn)

Current 8,704 / 70.36  
Previous 8,729 / 70.56  
Chg. -0.28%

#### Daily Turnover (mn)

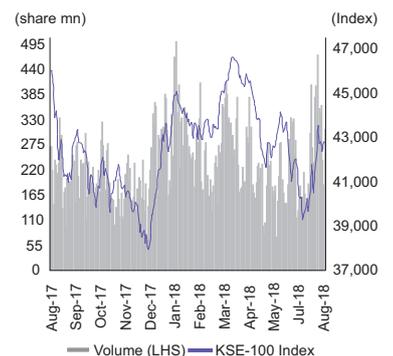
Current 145.25  
Previous 163.22  
Chg. -11.0%

#### Value Traded (PkRmn/US\$m)

Current 8,480 / 68.55  
Previous 8,051 / 65.08  
Chg. 5.3%

#### News and Views

- The Islamabad High Court (IHC) has constituted a division bench to hear a petition seeking Pakistan Tehreek-i-Insaf chairman Imran Khan's disqualification under Article 62 of the Constitution. The bench will be headed by Justice Shaukat Aziz Siddiqui and will also comprise Justice Athar Minallah.
- As per latest SBP statistics, Pakistan's foreign debt and liabilities soared around 14%YoY to US\$95.097bn in FY18. Recent data shows that the country's public external debt amounted to US\$75.357bn in June-end compared to US\$66.103bn a year earlier.
- The Ministry of Energy (MoE) has been asked to finalize its evaluation of the impact of US sanctions on Pakistan's options for growth of economic relations with Iran, particularly in the energy sector. The MoE's recommendation would form part of the incoming government's economic and trade relations abroad amid realignment of regional and international relationships among major global powers, particularly in the aftermath of US pulling out of nuclear deal with Iran.



Haris Imtiaz

haris.imtiaz@akdsecurities.net

111-253-111 Ext:685

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## Economy: Turkish tensions rile the shores of emerging markets

Recent episodes of volatility in emerging market currencies, headlined by the Lira (38.6% depreciation in CY18TD), Indian Rupee (8.9%), Argentine Peso (37.7%) and South Africa Rand (15.0%) have elevated fears of a global financial contagion. This has partly been fueled by strengthening of the dollar index (up 7.6% since Apr'18) due to rising US interest rate profile accompanied by fiscal stimulus (tax relief). Additionally, global factors including concurrent global monetary tightening, higher oil prices, possible trade disputes on top of heightened geopolitical tensions have raised serious concerns over the stability of emerging economies, with economies reliant on dollar borrowing are in the crosshairs. Closer to home, Pakistan's ability to absorb external shocks in the event of a financial contagion remains very low considering depleting reserves and external sector woes. Within this view, strengthening of dollar index and rising volatility of emerging market currencies reinforce our case of another ~6.4% depreciation from current levels (parity at PkR133/US\$ by Jun'19).

**Turkish Lira:** Recent escalation of the standoff between Turkey and US with possible imposition of tariffs on Turkish steel and aluminum triggered the fall of lira, plunging 13.7% in a single day. Although, the quantum of effect of tariff remains relatively minimal (exports to US stands at ~5.5% of total export receipts), the recent move in lira represents a fundamentally weakened currency due to ongoing economic crisis along with administration's inability to adopt corrective actions timely. The growth at all cost agenda led to widening deficit (12 month rolling CAD estimated to be over 6.5% of GDP) and rise in domestic inflation (standing at 15.85%YoY in Jul'18). Despite raising benchmark interest rates by 975bps since Apr'18, it remained insufficient to counter escalating inflationary pressures. Adding to its economic woes, growth remained primarily financed through external debt standing US\$467bn (55% of GDP) in 1QCY18. Concurrently, private sector turns out to be most vulnerable as it bears 82.6% of total maturing short-term external debt stock of US\$180.6bn with likely spillover effects on entire European union.

**Risk of Financial Contagion:** The fall in lira (38.6% in CY18TD), Indian rupee (8.9%), Argentine Peso (37.7%) and South Africa Rand (15.0%) raises serious concern of financial contagion. Although each case is subject to idiosyncratic factors yet flight to safe yields propelling the dollar index (up 7.6% since Apr'18) remains common to all. In this background, global risk factors including a strong dollar, global monetary tightening, higher oil prices, concern over possible trade war between the US and China and heightened geopolitical tension could likely test stability of emerging economies, with economies reliant on dollar borrowing being most vulnerable. In this regard, as per World Bank, external debt stock of emerging economies stood at US\$6.88trn in 2016 (up 92.2% since last financial crisis of 2008).

Lira plunges as tension escalates



Source: Bloomberg & AKD Research

Strengthening dollar index



Source: Bloomberg & AKD Research



**Pakistan faces its own challenges:** In Pakistan's case, Rupee movements have largely been reliant on the extent of central bank intervention, where presently Pakistan's ability to absorb external shocks is very low considering depleting reserves and external sector woes. In this backdrop, recent bouts of currency volatility in other economies along with strengthening of Dollar Index reinforce our case of another ~6.4% depreciation from current levels in FY19F. Other catalyst for weakening parity includes elevated CAD (5.4% of GDP in FY19F) along with sizable debt repayments likely to push gross external financing to ~US\$22bn. In this regard, we estimate SBP FX reserves to shrink to <1 month of import cover by FY19-end (excluding IMF financing facility). As such, any delay in materializing sizable financial inflows (IMF financing facility) to stabilize depleting FX reserves could possibly trigger currency depreciation beyond our estimates of PKR133/US\$.

**Pakistan's External Flows  
Projection (US\$bn)**

	FY17A	9MFY18A	FY19F
Debt Repayments	(6.26)	(3.53)	(7.53)
Interest Payments	(1.62)	(1.44)	(2.36)
Current Account	(12.62)	(12.08)	(17.59)
Foreign Investment	2.22	2.01	2.70
Capital Account	0.38	0.29	0.30
<b>External Financing</b>	<b>(16.29)</b>	<b>(13.31)</b>	<b>(22.12)</b>
Eurobond/Sukuk	1.00	2.50	2.50
Paris Club	0.19	0.07	0.25
Multilateral/Bilateral	2.97	2.02	3.50
IMF	0.10	-	-
Commercial loans	4.37	1.72	4.00
Private sector external	4.14	1.00	2.00
China	1.59	1.22	1.50
<b>Debt Inflows</b>	<b>14.36</b>	<b>8.53</b>	<b>13.75</b>

Source: EAD, SBP, AKD Research



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Reduce	< -5% to > -20% downside potential
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