AKD Securities Limited
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Equity Research / Pakistan

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Wednesday, Jun 07, 2017

Today's Daily

Limited implications of Gulf tensions

Imposition of a complete and abrupt embargo by Saudi Arabia led bloc of Middle Eastern nations (Egypt, UAE, Bahrain and Yemen) on the State of Qatar. While the situation remains very fluid, with developments coming by the hour, Pakistan has been neutral so far with the foreign office stressing that Pakistan has no plans to cut diplomatic ties with Qatar. In terms of implications from an adverse event, import reliance on Qatar has been low for Pakistan, however this has seen a shift recently with RLNG agreements signed with the country (import share at 2.3% in 10MFY17 vs. 0.5% 5yr average). Moreover, Qatar ranks a distant 7th place with inbound remittances making up only ~2% of total remittances over the last 5yrs. With regards to RLNG, imports (up 1.7xYoY in 10MFY17) have been rising at a major clip bolstered by long term RLNG supply agreement inked with Qatar. While the agreement is based on a Take or Pay structure, we believe the contractual grounding for the agreement insulates Pakistan from any untoward developments on the RLNG front. Besides, the Qatari government and related entities have assured its largest customers that shipments will not face disruptions (the same is expected in our case). We believe, political developments and geopolitics closer to home are expected to outweigh GCC-related developments for local investors.

KSE100 - Index

Current	50,144.63
Previous	50,120.92
Chg.	0.05%

Mkt Cap. (PkRbn/US$bn)

Current	9,939 / 94.78
Previous	9,965 / 95.03
Chg.	-0.26%

Daily Turnover (mn)

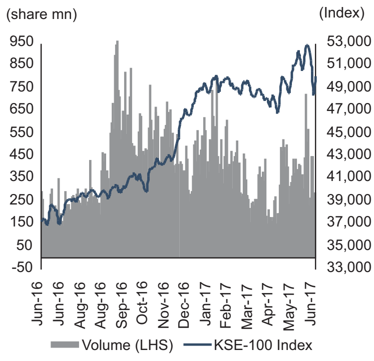
Current	231.74
Previous	255.14
Chg.	-9.2%

Value Traded (PkRmn/US$mn)

Current	13,543 / 129.16
Previous	13,858 / 132.16
Chg.	-2.3%

News and Views

- Moody's Investor Service has estimated Pakistan's GDP growth for both FY17/FY18 at 5%.While highlighting the GoP's commitment to moderate fiscal deficits in FY18 budget, international credit rating agency cautioned against ambitious revenue and GDP growth targets set in FY18 budget.
- PM Nawaz Sharif - in a CCE meeting held yesterday (Tuesday) - has granted approval to set up new LNG based 1200MW power plant, the location of which is yet to be decided. Agenda items related to the circular debt and load management plan were deferred for the next meeting.
- The GoP is set to increase property valuation rates by 30% for major cities of the country from July'17, it also plans to include new cities (Larkana, Khairpur, and Shaheed Benazirabad) under the ambit of new property valuation regime.



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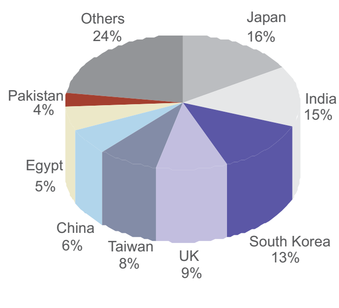
The six member Gulf Cooperation Council bloc of nations have been considered to be at odds, where UAE and KSA have publicly severed diplomatic ties with Qatar before (most recently in March'14), citing policies supported by Qatar to be negative for regional stability. The country is a relatively modest exporter of Oil and condensate (production capacity of 600,00bpd, making up 1.9% of OPEC exports). Qatar remains the world's single largest exporter of RLNG (8.77bcm, 23.2% of total shipments) and the embargo has sent RLNG markets on edge.

RLNG supply looks to continue: Imports have been rising at a major clip bolstered by long term RLNG supply agreement inked between Qatar Liqueified Gas Company and PSO on Feb'16 for fifteen years (till CY31). Annual contract quantities covered by the agreement extend to 3.75mtpa (195,000,000 MMBTU), which were instrumental in pushing LNG imports to US$965mn (up 1.7xYoY) for 10MFY17, expected to cross US$1bn by FY17 end. While the agreement is based on a Take or Pay structure, we believe the contractual grounding for the agreement insulates Pakistan from any untoward developments on the RLNG front. Besides, the Qatari government and related entities have assured its largest customers that shipments will not face disruptions (the same is expected in our case). In terms of news flows regarding an additional RLNG supply agreement with Doha, developments may be delayed on this front, giving room for procuring spot or short term RLNG shipments to meet demand (largely from 1,120MW Bhikki with an expected COD by 4QCY17). When including future expected RLNG shipments, ~US$3.4bn are expected to be added to the annual import bill (at oil price assumption of US$55/bbl, 1,200mmcfd of imports, load factor of 80%, thermal efficiency at 50%) where every 150mmcfd (RLNG required for one net 1,100MW) adds ~US$400mn.

% of LNG exports from Qatar by destination for 2016

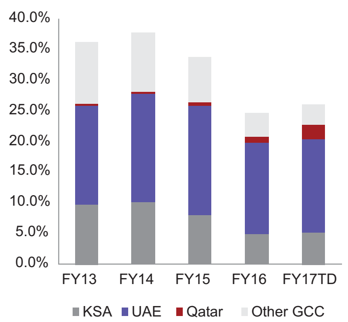


Source: Wood Mackenzie & AKD Research

Remittances at the fore: Pakistan's external economics intersect more closely with the Arab bloc. While remittances from the region have been on a dip (-4.8%YoY), they continue to form a key support to Pakistan's BoP stability with KSA (~30% share of total remittances in past 5yrs) and UAE (5yr average share at 21.2%) are first and second largest sources of remittances. On the other hand, Qatar ranks a distant 7th place with inbound remittances making up only ~2% of total remittances over the last 5yrs (down 1.6%YoY to US$304.8mn in 10MFY17). This limits the direct impact on remittance flows of the recent turmoil and its potential spillover effects on Pakistani labor in Qatar. However, impact may be aggravated if expected pick up in remittances from the upcoming FIFA World Cup 2022 (Qatar) fails to materialize.

Trade relationships: As for trading relationships, the GCC bloc is a key import partner for the country (5yr average import share at 34.3%) with petroleum imports making 23% of Pakistan's total import bill. KSA and the UAE command the largest share of trade from Pakistan with imports at US$1.9bn and US$5.8bn in 10MFY17 (15.4% and 5.1% share respectively). Historically, import reliance on Qatar has been low for Pakistan, however this has seen a shift recently with RLNG agreements signed with the country (import share at 2.3% in 10MFY17 vs. 0.5% 5yr average).

Import Share of GCC countries



Source: SBP & AKD Research

What to look for in the near term: Developments likely to guide regional markets include: 1) efforts by the non-aligned bloc within the GCC (Kuwait and Oman) to resolve tensions (where they have succeeded in the past), 2) additional diplomacy and state action by regional organizations (Arab League, Organization of Islamic Conferences, OPEC, Iran), and 3) US government and any actions (or inaction) regarding its forward Al-Ubeid airbase (10,000 troops stationed). Additionally, many regional countries either directly or indirectly (through agreements or tenders with third party suppliers or traders) source RLNG from Qatar. That said, only 10% of the country's exported RLNG lands in the Middle East with the UAE being its largest importer. The UAE government has banned all Qatar bound vessels from Fujairah, an essential fueling port for shipments headed to Asia.

Outlook: By and large we believe Pakistan is relatively insulated from developments regarding the Qatar embargo. RLNG makes up less than 5% of our power mix, with no major plants contributing to the national grid currently. Looking at the PSX, foreign activity is likely to guide market sentiments in the short term with the market seeing increased volatility until complete re-balancing of portfolios. Additionally, the ongoing proceeding by the JIT tasked with probing the Sharif family's offshore properties (2nd out of 4 progress reports to be submitted to the SC shortly) can heighten political noise in the near term. That said, the recent correction has opened up valuations, including MSCI EM basket stocks. In this backdrop, we prefer UBL (TP: PkR270.3/sh), HBL (TP: PkR296.1/sh) and LUCK (TP:

PkR1,180/sh). We also like FCCL (TP: PkR56/sh) and INDU (TP: PkR2,214/sh) at current price levels.

Regional Countries & Organizations

Countries	Arab league	Council of Arab economic unity	Gulf Co-operation council	Organization of petroleum exporting countries
Algeria	✓	✓		✓
Bahrain	✓	✓	✓	
Egypt	✓	✓		
Iraq	✓	✓		✓
Jordan	✓	✓		
Kuwait	✓	✓	✓	✓
Libya	✓	✓		✓
Oman	✓	✓	✓	
Qatar	✓	✓	✓	✓
Saudi Arabia	✓	✓	✓	✓
UAE	✓	✓	✓	✓
Yemen	✓	✓		

Source: AKD Research

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Neutral	≤ 5% to ≥ -5% potential
Reduce	< -5% to > -20% downside potential
Sell	≤ -20% downside potential

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