

PAKISTAN STRATEGY

Political capital paves runway for reforms

- A recent IRI poll highlights strong approval rating for the newly elected PTI gov't, with 57%/56% of the respondents rating performance of the PM Imran Khan and his gov't as satisfactory.
- Interestingly, the performance of provincial governments led by PTI (i.e. Punjab & KPK) was also rated as satisfactory, with a strong approval rating of 58%.
- Notably, 74% of the respondents consider economic challenges as the most important problem, with inflation being top most (39%), followed by poverty (18%) and unemployment (15%).
- We see the aforementioned survey results as a macro-positive, signifying that the gov't has enough political capital to initiate the reform process, including key macro and energy sector challenges.
- However, potential ramifications of tough reform process could take its toll on valuations and consequently on the overall market performance. In this backdrop, any weakness should be taken as an opportunity to accumulate, taking a longer term investment horizon.
- We have a preference for macro-hedged sectors encompassing Banks, E&Ps, selected Power and Textiles. Our top picks include, MCB, MEBL, OGDC, HUBC and NML.

PTI riding the popularity wave: A recent IRI poll highlights strong approval rating for the newly elected PTI gov't, with 57%/56% of the respondents rating performance of the PM Imran Khan and his gov't as satisfactory. Interestingly, despite the economic challenges, the PTI has gained ground, with the party popularity inching up to 34% (vs. 32% during election times), as per survey results. Also, the performance of provincial governments led by PTI (i.e. Punjab & KPK) was rated as satisfactory, with a strong approval rating of 58%. Notably, 74% of the respondents consider economic challenges as the most important problem, with inflation being top most (39%), followed by poverty (18%) and unemployment (15%).

Political capital can allow Government to initiate significant reforms: We see the aforementioned survey results as a macro-positive, signifying enough political capital to initiate the reform process. We believe the GoP's policy to protect the marginalized/lower income population from the price hikes (i.e. gas & electricity) so far has played a key role in maintaining its popularity. This is also evident from lower income group inflation (avg. quintile 1 & 2 inflation since PTI gov't came into power: 4.2/4.7% vs. avg. headline inflation of 6.5%). Recent survey results give us confidence that the gov't can comfortably kick start the reform process to address key macro and energy sector challenges. From policy perspective, concrete action to tame fiscal woes remains missing, with rate hike adjustments in energy chain also falling short. With fiscal side of the equation remaining largely unaddressed, we expect the next policy thrust to be on the same front. Forthcoming FY20 budget would be key checkpoint in this regard.

Outlook: Political capital allows the gov't to jump start reforms and set the tone for much needed policy direction that could invigorate investor interest. Investor participation has remained weak so far, with avg. volumes since the new gov't came into the power standing at 164.8mn (Aug'18-Feb'19) vs. 216.0mn (Jun'13-Dec'13) in the early tenure of the PML-N gov't. That said, in the short run the negative impact of reforms could take its toll on valuations and consequently on the overall market performance. In this backdrop, any weakness should be taken as an opportunity to accumulate, taking a longer term investment horizon. To highlight, KSE-100 index has cumulatively de-rated by ~12% in the past one year (exc. dividends) to trade at a CY19F P/E of 8.2x where in era of weak macros (CY10-12) market had actually re-rated by an avg. 4.0%. We have a preference for macro-hedged sectors encompassing Banks, E&Ps, selected Power and Textiles. Our top picks include, MCB, MEBL, OGDC, HUBC and NML.

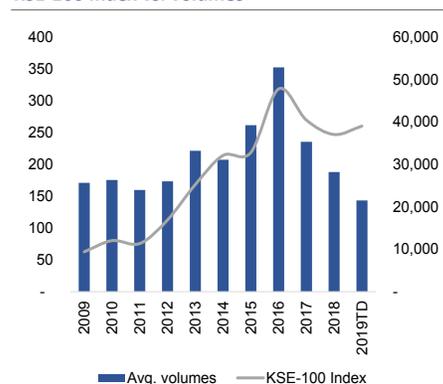
Umer Farooq
 umer.farooq@akdsecurities.net
 111-253-111 Ext: 602

Key highlights

Benchmark	% of respondents in favor
PTI / PMLN Popularity	34/21%
% of population viewing last elections free and fair	83%
PM Khan approval rating	57%
PTI Federal Government approval rating	56%
Time willing to give to Govt. to deliver on promises	1-2y: 40% >2y: 44%
Things heading in the right direction	
Elimination of corruption	34%
Change	26%
Law and Order improvement	12%
Things heading in the wrong direction	
Inflation	52%
Unemployment	19%
Poverty	10%
Approval rating	
Law enforcement agencies	53-96%
Courts	70%
National Assembly	57%
Civil Service	55%
Opposition	47%

Source: Int. Republican Institute & AKD Research

KSE-100 Index vs. volumes



Source: PSX & AKD Research



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Buy	> 19% expected total return (Rf: 13% + Rp: 6%)
Neutral	> 13% to < 19% expected total return
Sell	< 13% expected total return (Rf: 13%)

Old Rating Definitions (Discontinued)

Buy	> 20% upside potential
Accumulate	> 5% to < 20% upside potential
Neutral	< 5% to > -5% potential
Reduce	< -5% to > -20% downside potential
Sell	< -20% downside potential
Not Rated	No investment opinion or recommendation

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To arrive at our period end target prices, AKDS uses different valuation techniques including:

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

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