

PAKISTAN STRATEGY

MARKET VISTA

REP-019

MSCI: Pakistan set to be reclassified into FM from EM

- Pakistan is set to be classified under Frontier Markets from Emerging Markets on Nov 11'21 with the change coming in affect by Nov-end. This should draw curtains on country's 4.5yr long ride in EM index — the second in Pakistan's market history — during which the market witnessed net foreign outflows of US\$1.4bn and performed 1.4% during this period vs. 26.2% of MSCI EM index.
- Together with the current review, MSCI shall open consultation for classifying Pakistan in MSCI FM 100 index and MSCI Frontier Markets 15% Country Capped Index, with possible announcement in Feb'22.
- Pakistan is expected to fetch an indicative weight of 1.9% in FM as per MSCI release, which is significantly lower than ~9% when the country exited FM back in 2017. While Argentina is downgraded from MSCI EM as a standalone index, potential reclassification to FM could further compress Pakistan's weight in the index.
- The transition is unlikely to materially alter market's participation dynamics, and macro factors would continue to dominate market direction where possible resumption of IMF program with Govt. addressing structural issues, ease-off in commodity prices (Brent at its one month low, coal prices coming off 39% from peak), and relative calm on political front to stretch current rally at the bourse (market +9.25% from recent low).

Pakistan set to be reclassified to FM from EM: Pakistan is set to be classified under Frontier Markets from Emerging Markets on Nov 11'21 with the change coming in affect by Nov-end. This should draw curtains on country's 4.5yr long ride in EM index — the second in Pakistan's market history — during which the market witnessed net foreign outflows of US\$1.4bn and performed 1.4% during this period vs. 26.2% of MSCI EM index. The weak performance was mostly attributable to idiosyncratic country risks and classification of other better positioned markets such as that of KSA, compressed weight to 0.02% (latest) from 0.1% when Pakistan was initially classified. Pakistan has been hanging in Emerging Markets since Nov'18 courtesy buffering rules while none of the Pakistani companies in the MSCI Pakistan equity universe meet the EM Size and Liquidity criterion under the MSCI Market Classification Framework since Nov'19. Foreign corporates' net sell during this period stood at US\$1.5bn with value sectors falling out of favor as Banks and E&Ps witnessed a net sell of US\$1.02bn while tech space recorded an inflow; though a meagre one of US\$9.5mn. Together with the current review, MSCI shall open consultation for classifying Pakistan in MSCI FM 100 index and MSCI Frontier Markets 15% Country Capped Index, with possible announcement in Feb'22.

Pakistan to fetch a meagre weight in FM as well: Pakistan seemingly fetch an indicative weight of 1.9% in FM as per MSCI release, which is significantly lower than ~9% when the country exited FM back in 2017. While Argentina is downgraded from MSCI EM as a standalone index, potential reclassification to FM could further compress Pakistan's weight in the index. EM Pakistan's standard index participants namely, LUCK, MCB, and HBL together with OGDC are likely to meet frontier's quantitative criteria for standard index while total constituents would reach to 23 from 16 currently in EM. Consequently, MSCI FM would incorporate 59.1% of total KSE FF vs. 47.0% in MSCI EM. As per market grapevine, total AUMs of EM funds currently stands close to US\$1.8trn compared to AUMs of FM funds of US\$15bn which should result in net outflow settling close to US\$70-80mn. However, potential fresh allocation to FM space from major funds going forward can result in reduced outflow or net inflow.

Locals to dominate participation, focus on macro holds the key: The transition is unlikely to materially alter market's participation dynamics in our view, where foreigners occupy 15.3% of total market capitalization (including strategic holdings) compared to companies and individuals engrossing cumulative share of 55.6% in capitalization. Hence, macro factors would continue to dominate market direction where possible resumption of IMF program with Govt. addressing structural issues, ease-off in commodity prices (Brent at its one month low, coal prices coming off 39% from peak), and relative calm on political front to stretch current rally at the bourse (market +9.25% from recent low). We continue to advocate from thematic plays which includes Banks (on monetary tightening), Construction-driven sectors (Cements, Steel), and Textiles (on devaluations and strong export prospects).

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Simulated MSCI Frontier Markets100 Index

Security	Country	Simulated Index Weight
LUCK	Pakistan	0.81%
ENGRO	Pakistan	0.62%
HUBC	Pakistan	0.58%
HBL	Pakistan	0.53%
MCB	Pakistan	0.48%
TRG	Pakistan	0.48%
UBL	Pakistan	0.43%
FFC	Pakistan	0.39%
PSO	Pakistan	0.33%
PPL	Pakistan	0.32%
MARI	Pakistan	0.29%
EFERT	Pakistan	0.26%
MTL	Pakistan	0.26%

Source: MSCI Document and AKD Research

Proposed stocks in MSCI FM

Symbol	Full Mcap (USDmn)	FIF Mcap (USDmn)	FIF	Size-Segment
OGDC*	2189	328	0.14	Standard
LUCK	1446	506	0.4	Standard
PPL	887	300	0.2	Small caps
MARI	1099	266	0.2	Small caps
MCB	1059	395	0.35	Standard
HBL	1073	536	0.4	Standard
ENGRO	873	528	0.5	Small caps
UBL	985	394	0.4	Small caps
FFC	787	433	0.4	Small caps
POL	524	288	0.35	Small caps
PSO	308	239	0.45	Small caps
HUBC	517	434	0.8	Small caps
INDU*	566	97	0.2	Small caps
EFERT	578	261	0.4	Small caps
TRG	444	377	0.75	Small caps
BAHL*	468	304	0.7	Small caps
ABOT*	434	93	0.2	Small caps
NBP*	451	107	0.2	Small caps
SYS*	527	394	0.5	Small caps
MTL	232	176	0.6	Small caps
SEARL	148	149	0.4	Small caps
BAFL	343	134	0.4	Small caps
PKGS*	273	68	0.35	Small caps

Source: MSCI Document and AKD Research

*Not part of MSCI EM Index



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Buy	> 14.5% expected total return (Rf: 8.5% + Rp: 6%)
Neutral	> 8.5% to < 14.5% expected total return
Sell	< 8.5% expected total return (Rf: 8.5%)



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