NBP Fullerton Asset Management Ltd.
A Subsidiary of National Bank of Pakistan

Dr. Amjad Waheed, CFA
Chief Executive Officer

Economic Outlook For FY15

Following Pakistan's entry into a fresh IMF Program and associated stabilization measures and policies adopted by the government, Pakistan's macroeconomic performance considerably improved during the last fiscal year. GDP growth accelerated to a six year high of 4.1%, CPI inflation remained fairly contained at 8.6% and fiscal deficit significantly narrowed to 5.5% of GDP from 8.2% in FY13. Current account deficit remained manageable at 1.2% of GDP (US $ 2.9 billion), while overall balance of payments position substantially strengthened, recording a surplus of USD3.8bn compared to a deficit of USD2.0bn posted in FY13. SBP foreign exchange reserves increased to USD9.0bn, import cover improved to 3.5 months and Pak rupee ended at 98.8 against US dollar. Private sector credit off-take also picked up sharply after a long pause.

We foresee decent macroeconomic performance in FY15, driven by positive business /consumer sentiments. We expect FY15 GDP growth to remain at 4.1% on the back of a recovery in agriculture production (minor crops and livestock), continued momentum in the services (finance, communication and trade) and industrial sectors (manufacturing, construction, electricity and mining). We anticipate headline inflation to clock at 8.5% as inflationary pressures are likely to remain subdued due to lower commodity prices and restricted money supply growth. SBP is likely to keep its policy rate unchanged due to government commitment to further retire SBP borrowing which would squeeze liquidity in the system.

We forecast fiscal deficit at 6% of GDP due to decent revenue growth (new taxes, abolition of some exemptions) and measured expenditure growth (lower development expenditure, off balance sheet financing of circular debt). We expect current account deficit to remain manageable at 1.2% of GDP as higher remittances should neutralize a wider trade deficit (US $ 17 billion). We project overall balance of payments to record a surplus of USD2.9bn due to higher inflows under financial and capital account on account of higher FDI and portfolio inflows and multilateral / bilateral loans. Thus, under our base case, SBP reserves would increase to nearly USD12bn by fiscal year-end. We expect Pak rupee to depreciate by 5.3% against US dollar to Rs104 by June 2015.

The last few weeks have remained particularly tumultuous for the local bourses, with the benchmark KSE-100 Index exhibiting extreme volatility and falling by 6% during August. As stated earlier, country's economic outlook for the ongoing fiscal year looks favorable so far. However, simmering political tensions and continued stand-off between the government and opposition groups (PTI/PAT) have dented investors' confidence leading to a correction in the market. Nonetheless, after the recent correction, forward Price to Earnings (PE) of the stock market has declined to 8.2x offering attractive expected dividend yield of 6%. While the current political impasse is having a short-term negative impact on the equity markets, given cheap market valuations, positive macroeconomic indicators and 15% expected corporate earnings growth in FY15, we expect the stock market to post a healthy double digit return during the current fiscal year.

Fig 1 Pakistan-economic indicators and forecasts

Fiscal year runs from July to June	2010-11	2011-12	2012-13	2013-14	2014-15F
Nominal GDP (Rsbn)	18,276	20,047	22,489	25,402	28,704
Nominal GDP (US$bn)	214	225	233	247	286
Per capita GDP (US$)	1,207	1,243	1,261	1,313	1,490
Real GDP Growth (%YoY)	3.60%	3.80%	3.70%	4.10%	4.10%
CPI (average)	13.70%	11.00%	7.40%	8.60%	8.50%
Money supply-M 2	15.90%	14.10%	15.90%	12.50%	13.00%
SBP discount rate	14.00%	12.00%	9.00%	10.00%	10.00%
Consolidated fiscal deficit (% GDP)	6.50%	8.80%	8.20%	5.50%	6.00%
Trade balance (US$bn)	-10.5	-15.8	-15.4	-16.6	-17.3
Current account balance (US$bn)	0.2	-4.7	-2.5	-2.9	-3.3
as % GDP	0.10%	-2.10%	-1.10%	-1.20%	-1.20%
Overall balance (US$bn)	2.5	-3.3	-2	3.8	2.9
SBP reserves (US$bn)	14.7	10.8	6.0	9.1	12
Exchange rate PKR/USD (end period)	85.9	94.4	99.7	98.8	104
% YoY	0.7%	9.9%	5.6%	-0.9%	5.3%

Source: SBP, MOF and NAFA estimates