

# Pakistan Business Forecast Report Q3 2014

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## Abstracts

### Core Views

Pakistan's economy is picking up strongly, with the IMF's reform initiatives having a positive impact on the manufacturing sector. We believe that the Fund will release the third loan tranche of the Extended Fund Facility over the coming months, given the progress so far, and see upside risks to our already-above consensus real GDP growth forecast for FY2013/14 of 3.4%. We continue to forecast an acceleration in growth to 4.0% in FY2014/15.

The appreciation of the Pakistani rupee since December 2013 has been nothing short of spectacular. The currency has strengthened by over 10% from the December trough, and while there have been some genuinely positive signs on the macroeconomic front, the unprecedented move may also have stemmed from the State Bank of Pakistan's desire to send a message that the rupee is not a one-way losing bet. However, we expect the recent strength to subside over the coming months, and forecast the unit to weaken back to PKR 100.00/USD over the coming months.

We believe that headline consumer price inflation (CPI) will continue on its broadly declining trend over the coming months and quarters as money supply growth continues to cool, the impact of the stronger rupee keeps imported price inflation muted, and supply-side developments continue to gather momentum. We are forecasting CPI to end FY2013/14 and FY2014/15 at 7.5% and 6.5% respectively.

Pakistan's recent USD1.5bn 'gift' from Saudi Arabia has raised a number of questions regarding the implications for the former's stance on Syria, and the Iran-Pakistan (IP) gas pipeline project. With the Pakistani economy in a fragile state, and in great need of external financing, the grant was difficult to refuse, but is likely to lead to a further deterioration of relations with neighbouring Iran.

## Major Forecast Changes

We have upgraded our FY2013/14 real and FY2014/15 exchange rate forecasts for the rupee, owing to the intense strength seen at the start of 2013. While we still expect the unit gradually depreciate, we now expect it to average PKR99.8/USD in FY2013/14 and PKR100.5/USD in FY2014/15.

We have also rolled back our expectations for further interest rate hikes by the State Bank of Pakistan, due to the disinflationary pressure provided by recent currency strength. We expect the reverse repo rate to remain at 10.00% in FY2013/14 and FY2014/15.

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Pakistan's recent USD1.5bn 'gift' from Saudi Arabia has raised a number of questions regarding the implications for the former's stance on Syria, and the Iran-Pakistan (IP) gas pipeline project. With the Pakistani economy in a fragile state, and in great need of external financing, the grant was difficult to refuse, but is likely to lead to a further deterioration of relations with neighbouring Iran.

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Instability To Prevail, But Outright Collapse Unlikely

Pakistan is at risk of experiencing years of instability and militant activity, but an outright collapse of the state is unlikely unless the core province of Punjab becomes ungovernable. Under such circumstances, we would not preclude a military coup. Meanwhile, due to its strategic importance, Pakistan's foreign allies will do everything they can to ensure its stability.

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We believe that headline consumer price inflation (CPI) will continue on its broadly declining trend over the coming months and quarters as money supply growth continues to cool, the impact of the stronger rupee keeps imported price inflation muted, and supply-side developments continue to gather momentum. We are forecasting CPI to end FY2013/14 and FY2014/15 at 7.5% and 6.5% respectively.

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