


Pakistan Equity | Economy

July 13, 2023

REP-057

IMF Board Approves US\$3bn SBA, as expected Inflation of 26% higher than Govt estimates



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Pakistan
Best Local Brokerage
House 2015-16, FY2020

ASIAMONEY
Best Local Brokerage House
Brokers Poll 2011-14, 2016-21



FinanceAsia
Best Brokerage
House 2018,19-20



2019
INTERNATIONAL
FINANCE
BROKERAGE AWARDS
Best Research
House 2019-20



ASSET ASIAN AWARDS 2019
★ TRIPLE A ★
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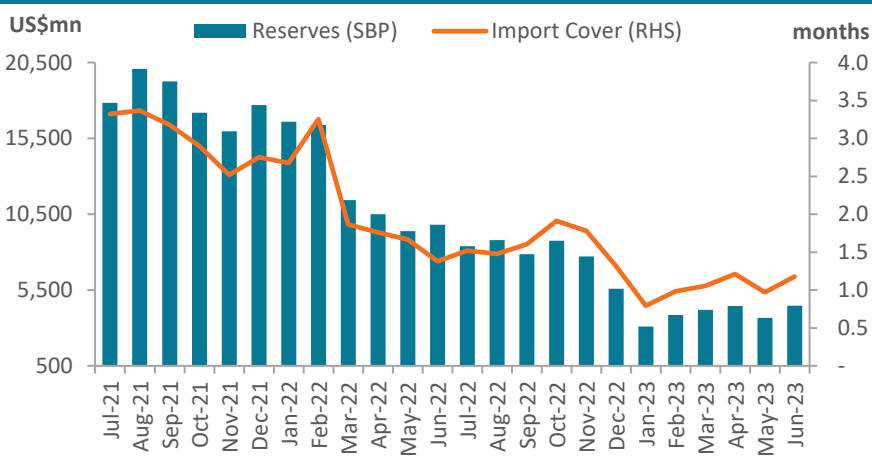
IMF program to pave way for other flows, no immediate default/restructuring risk

IMF Macro Estimates

	FY22	FY23P	FY24P
GDP Growth	6.1%	-0.5%	2.5%
CPI (Average)	12.1%	29.6%	25.9%
CPI (Period end)	21.3%	34.0%	16.2%
CAB (% of GDP)	-4.6%	-1.2%	-1.8%
FDI (% of GDP)	0.5%	0.4%	0.2%
Gross Reserves (US\$m)	9,821	4,056	8,982
Total External Debt (% GDP)	32.1%	36.4%	37.3%
Revenue and Grants (% of GDP)	12.1%	11.4%	12.3%
Expenditure (% of GDP)	20.0%	18.9%	19.8%
Primary balance, Ex Grants (% of GDP)	-3.1%	-1.0%	0.4%
Budget balance, Ex Grants (% of GDP)	-7.9%	-7.6%	-7.5%

Source: IMF Press Release

Pakistan Foreign Exchange Reserves & Import Cover



Source: SBP, Topline Research

- As anticipated the Executive Board of International Monetary Fund (IMF) have approved a 9-month Stand By Agreement (SBA) for Pakistan amounting to US\$3bn (SDR 2,250mn).
- The approval allows for an immediate disbursement of US\$1.2bn. The remaining amount will be phased over the program's duration, subject to two quarterly reviews.
- To recall IMF staff agreed to provide new short term loan SBA to Pakistan on June 30, 2023 after Pakistan failed to complete the previous EFF.
- Since than Pakistan short duration EuroBonds (2024 and 2025) has rallied 13%, local equities are up 10% while PKR has appreciated by 3% against USD.
- Though some confusion was there regarding IMF Board approval as IMF team preferred to meet the key political parties before the final approval.
- With IMF money along with US\$2bn from Saudi and US\$1bn from UAE along with other bilateral and multilateral inflows, Pakistan liquid FX reserves with SBP is likely to reach US\$8-9bn. This is in addition to US\$5.3bn of public money with banks and US\$4bn worth of Gold lying with the government.
- This will improve Pakistan liquidity position as import Cover will rise from 1.2 to 2.2. This is still below the long term 10 year average of 2.8.
- Interesting most of the estimates provided by IMF in their release are in line with government targets for FY24, but inflation estimate is different.
- Pakistan government is estimating average CPI inflation of 21% which is in line with street forecast. Our estimate is 20-22% for FY24 considering last year high base, relatively stable currency and falling global commodity prices. However IMF is estimating inflation of 26%.
- In a Tbill auction yesterday, that happened before IMF board approval, many investors participated in long term 1 year paper also signaling market expectations of falling inflation and policy rate.
- We believe this better than expected loan by IMF will provide the much needed economic stability to Pakistan at a time when Pakistan will see a transfer of power from one government to caretakers and then to New government.
- In the past we have seen government not complying with IMF conditions due to political reasons. But now considering that ruling PDM government term will end in next few weeks, chances of non compliance by the caretaker and new government seems less as election by that time will be over.

Key takeaways from IMF press release

- Pakistan's economic reform program aims to support immediate efforts to stabilize the economy and guard against shocks while creating the space for social and development spending to help the people of Pakistan. We agree with that as we think this loan will provide some stability and will help restore confidence.
- Steadfast policy implementation will be critical for Pakistan and the success of the program. This will require greater fiscal discipline, a market-determined exchange rate to absorb external pressures, and further progress on reforms related to the energy sector, climate resilience, and the business climate. In this regard all 3 governments need to strictly follow IMF guidelines. As mentioned earlier chances of major non compliance are less as Elections will be over by Oct/Nov.
- **Following the Executive Board discussion, Kristalina Georgieva, Managing Director and Chair, made the following statement:**
- *"Pakistan's economy was hit hard by significant shocks last year, notably the spillovers from the severe impacts of floods, the large volatility in commodity prices, and the tightening of external and domestic financing conditions. These factors together with uneven policy implementation under the EFF combined to halt the post-pandemic recovery, sharply increase inflation, and significantly depleted internal and external buffers. The authorities' new Stand-By Arrangement, implemented faithfully, offers Pakistan an opportunity to regain macroeconomic stability and address these imbalances through consistent policy implementation."*
- *"The authorities' FY24 budget, which targets a modest primary surplus, is a welcome step toward fiscal stabilization. The anticipated improvement in tax revenues is critical to strengthen public finances, and to eventually create the fiscal space needed to bolster social and development spending. Maintaining discipline over non-critical primary expenditure will be essential to support budget execution within the envisaged envelope. In parallel, the authorities urgently need to strengthen energy sector viability by aligning tariffs with costs, reforming the sectors cost base, and better-targeting power subsidies. Looking beyond this fiscal year, enhanced efforts to expand the tax base and improve public financial management, including in the delivery of quality infrastructure, are needed and increase progressivity and efficiency."*
- *"The recent increase in the policy rate by the SBP is appropriate given the very high inflationary pressures, which disproportionately impact the most vulnerable. A continued tight, proactive, and data-driven monetary policy is warranted going forward. A market-determined exchange rate is also critical to absorbing external shocks, reducing external imbalances, and restoring growth, competitiveness, and buffers. Close oversight of the banking system and decisive action to address undercapitalized financial institutions would support financial stability."*
- *"Accelerating structural reforms to build climate resilience, enhance safety nets, strengthen governance, including of state-owned enterprises, and improve the business environment by creating a level-playing-field for investment and trade are necessary for job creation and raising inclusive growth."*

Background of the current & last IMF program

History of IMF Lending Commitments to Pakistan (amount in mn SDR)				
Program Name	Date of Arrangement	Expiration Date	Amount Agreed	Amount Drawn
Standby Arrangement	Jun 30, 2023	Mar 30, 2024	2,250	-
Extended Fund Facility	Jul 03, 2019	Jun 30, 2023	4,988	2,144
Rapid Financing	Apr 16, 2020	Apr 20, 2020	1,016	1,016
Extended Fund Facility	Sep 04, 2013	Sep 30, 2016	4,393	4,393
Standby Arrangement	Nov 24, 2008	Sep 30, 2011	7,236	4,936
Extended Credit Facility	Dec 06, 2001	Dec 05, 2004	1,034	861
Standby Arrangement	Nov 29, 2000	Sep 30, 2001	465	465
Extended Fund Facility	Oct 20, 1997	Oct 19, 2000	455	114
Extended Credit Facility	Oct 20, 1997	Oct 19, 2000	682	265
Standby Arrangement	Dec 13, 1995	Sep 30, 1997	563	295
Extended Credit Facility	Feb 22, 1994	Dec 13, 1995	607	172
Extended Fund Facility	Feb 22, 1994	Dec 04, 1995	379	123
Standby Arrangement	Sep 16, 1993	Feb 22, 1994	265	88
Structural Adjustment	Dec 28, 1988	Dec 27, 1991	382	382
Standby Arrangement	Dec 28, 1988	Nov 30, 1990	273	194
Extended Fund Facility	Dec 02, 1981	Nov 23, 1983	919	730
Extended Fund Facility	Nov 24, 1980	Dec 01, 1981	1,268	349
Standby Arrangement	Mar 09, 1977	Mar 08, 1978	80	80
Standby Arrangement	Nov 11, 1974	Nov 10, 1975	75	75
Standby Arrangement	Aug 11, 1973	Aug 10, 1974	75	75
Standby Arrangement	May 18, 1972	May 17, 1973	100	84
Standby Arrangement	Oct 17, 1968	Oct 16, 1969	75	75
Standby Arrangement	Mar 16, 1965	Mar 15, 1966	38	38
Standby Arrangement	Dec 08, 1958	Sep 22, 1959	25	-

Source: IMF, Topline Research

- To recall, IMF executive board had signed a US\$6bn EFF program with Pakistan in Jul-2019. In Nov-2019, Pakistan successfully completed its first review and in Feb-2020 reached Staff Level Agreement (SLA) on second review. However, the release of the tranche under second review was delayed due to COVID-19 outbreak.
- In order to combat challenges pertaining to COVID-19, IMF had also disbursed US\$1.4bn in April 2020 under the Rapid financing agreement.
- Later on after prolonged discussion with Abdul Hafeez Shaikh (Former Finance Minister), IMF board successfully approved the Second, Third, Fourth and Fifth Tranche in Mar-2021.
- Abdul Hafeez Shaikh was replaced by Shaukat Tarin in April-2021 who then carried out talks with IMF and reached a SLA in Nov-2021 for the sixth review after a delay due to differences and lack of implementation on few of the proposed policy actions.
- Seventh and Eighth reviews of Pakistan EFF program was initially scheduled in March 2022 and June 2022 but Pakistan was not able to reach SLA with IMF due to delay in proposed policy actions like removal of petroleum subsidies, imposition of Petroleum Levy (PDL), energy tariff rationalization & increased tax measures. Later on after prolonged discussion with Miftah Ismail (Former Finance Minister) IMF board successfully approved Seventh and Eighth in August-2022.
- Miftah Ismail was replaced by Ishaq Dar in Sep 2022 who then carried out talks with IMF for 9th review but unable to reach SLA in Nov-2022 due to lack of implementation of the proposed policy actions and meeting external funding requirement.
- On the last day of EFF program i.e. Jun 30, 2023, Pakistan achieved a significant breakthrough by signing a new and better than expected nine month Stand By Arrangement (SBA) with the IIMF worth US\$3bn (SDR 2.25bn).
- This is Pakistan's 24th IMF program which will expire in 2024.

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