

Resilience at a discount

Discounted valuations, stronger foundations

Pakistan equities offer scope for a gradual re-rating, supported by stronger external buffers, discounted valuations and attractive dividend carry. At c.7.0x forward earnings, the KSE-100 trades below its 8.1x long-term average, following a correction from c.8.3x at the 2026 peak. Higher reserves, improved import cover and resilient remittance inflows provide a more favourable starting point than during previous periods of external stress.

Our base case is for external stability to hold, inflation to moderate and monetary easing to become more visible into FY28. Under this scenario, valuations could recover toward 7.5–8.5x. Reported FY27 EPS growth for our universe is c.3%, compared with c.15% on a normalized FY26 earnings base (E&Ps), while a c.6.5% dividend yield provides carry during the normalization phase. The timing of any re-rating remains uncertain, and further downside is possible if external conditions come under pressure.

Macro buffers are stronger; valuations remain below average

	SBP reserves (US\$bn)	Total liquid reserves (US\$bn)	Import cover (m)	Current a/c (%GDP)	Policy rate (%)	CPI (%)	Fwd P/E (x)	D/Y (%)
Current	21.4	26.8	3.8	-0.7	11.5	10.3	7.0	6.5
LT avg.	11.3	16.9	2.8	-1.6	11.0	10.5	8.1	7.2

Source: PBS, SBP, Bloomberg, IMS Research

Investment outlook: Resilience amid external risks

- **Valuation reset:** The correction has created a more attractive entry point, with the KSE-100 trading below its long-term average forward P/E. A durable recovery, however, will require macroeconomic confirmation.
- **Stronger shock absorbers:** Higher FX reserves, improved import cover and robust remittances leave Pakistan better placed to absorb external shocks than during previous stress episodes.
- **Oil remains the key swing factor:** Sustained Arab Light prices above US\$115/bbl would meaningfully widen external pressures, raise inflation risks and test reserve adequacy.
- **Position for carry, retain upside:** Favor dividend-paying, cash-generative stocks for portfolio resilience, complemented by selective domestic recovery plays and company-specific re-rating opportunities.

Oil sensitivity: Where macro pressure builds

The oil-price path remains critical to the outlook. Against an US\$85/bbl baseline, sustained Arab Light prices of US\$115/bbl could add an estimated US\$5.3bn to the annual oil import bill, lift FY27 average CPI to 10.4% and widen the current account deficit to 1.8% of GDP. At US\$130/bbl, the incremental bill rises to US\$7.9bn, with import cover falling below 2.5 months. These are sustained-price stress scenarios, not forecasts; the duration of the oil shock will be as important as the peak price.

Oil Shock: Pakistan's Macro Stress Test

Arab Light (US\$/bbl)	85	100	115	130
FY27 CPI (avg)	7.7%	9.1%	10.4%	12.0%
Current account (% GDP)	-0.7%	-1.2%	-1.8%	-2.4%
Import cover (months)	>3.5	>3.0	2.5-3.0	<2.5
Policy bias	Hold	Hold	Tightening	Tightening
Macro read-through	Contained	Manageable	Stress	Severe stress

Source: Bloomberg, SBP, PBS, IMS Research

Portfolio stance: Carry first, re-rating second

We favour a barbell approach, anchored in cash-generative, dividend-paying names (**OGDC, MARI, PSO, APL, FFC, HBL, BAFL** and **MCB**), complemented by selective domestic recovery plays (**MLCF, DGKC**), **ATRL**'s transformation upside, and quality compounders **SYS** and **AGP**. The strategy prioritizes income and resilience, while retaining upside from a gradual market re-rating as macro conditions normalize.

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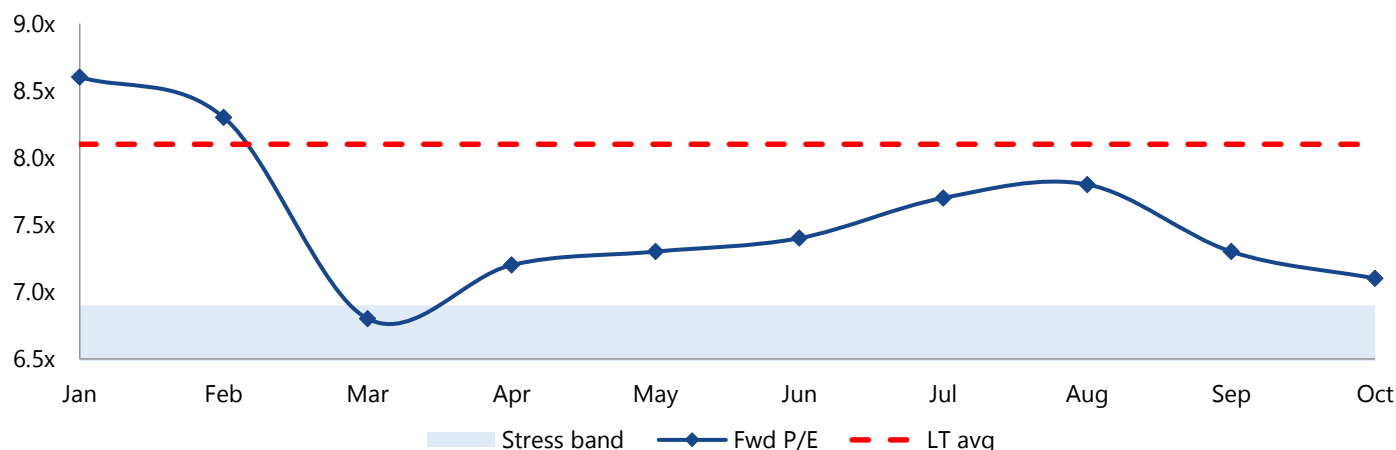
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Valuations have reset; recovery needs confirmation

The KSE-100's forward P/E multiple has compressed from c.8.5x at its 2026 peak to below 7.0x currently, having touched 6.4x intraday and averaged 6.8x in March. After entering FY27 at 7.3x, the market has remained above the March trough. With valuations below the 8.1x long-term average, the correction has improved the entry point for investors willing to look through near-term volatility. However, the adjustment may not be complete, with further downside possible if external conditions deteriorate. Conversely, continued macroeconomic stability would support a gradual recovery in multiples.

KSE100 has already repriced to stress, not crisis



Source: PBS, SBP, IMS Research

Stronger buffers, lower external vulnerability

Previous periods of severe equity stress coincided with deteriorating external balances, falling reserves, weaker import cover, currency depreciation and sharply higher inflation and interest rates. Financing constraints amplified the pressure on the economy and financial markets. The current position is more favorable across several key indicators. Reserve adequacy and import cover have improved substantially, while the current-account deficit is forecast to remain relatively contained. This provides greater capacity to absorb external pressure, although the durability of these improvements remains central to the investment case.

Pakistan's External Buffers: Stronger Than in Past Crises

Indicator	FY08-09	FY18-19	FY22-23	FY27f	Trend
Current account (% GDP)	-6.0%	-4.8%	-2.9%	-0.7%	Contained
SBP reserves (US\$bn)	9.4	10.5	10.5	21.7	Rebuilt
Import cover (months)	3.1	2.2	1.8	3.8	Restored
Policy rate	12.1%	7.7%	13.3%	11.3%	Lower
Inflation	16.5%	5.4%	20.6%	7.7%	Lower
USD/PKR (avg.)	70.6	123.0	212.6	282.4	Stable
External financing	Deteriorating	Deteriorating	Constrained	Access restored	Credible

Source: SBP, PBS, IMS Research

The improvement is most evident in reserve adequacy, import cover and access to external financing. Relative to previous stress episodes, Pakistan has more room to absorb external shocks before they translate into acute financing constraints. The stronger starting point supports our constructive medium-term view, though renewed pressure could still erode these buffers.

From external pressure to equity return

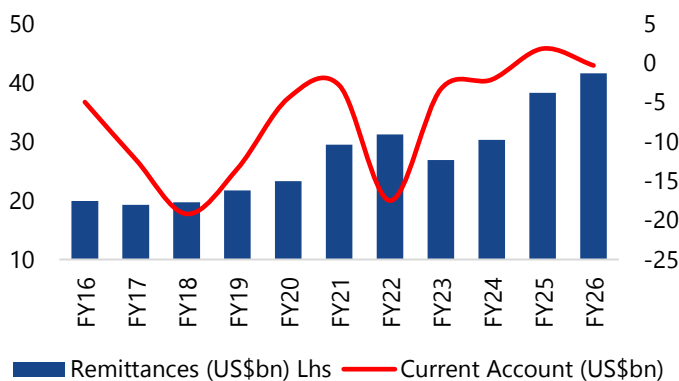
The current account: remittances provide a cushion

The current account remained in surplus in February and March following the onset of the Gulf supply shock, before moving into intermittent deficits as the higher import bill fed through. FY26 nevertheless closed broadly around balance, with a deficit of US\$139mn, compared with a US\$1.8bn surplus in FY25.

Remittances and services exports helped offset the wider goods trade deficit. Goods exports declined to US\$30.8bn in FY26 from US\$32.3bn, while remittances reached a record US\$41.6bn and services exports totalled US\$10.0bn.

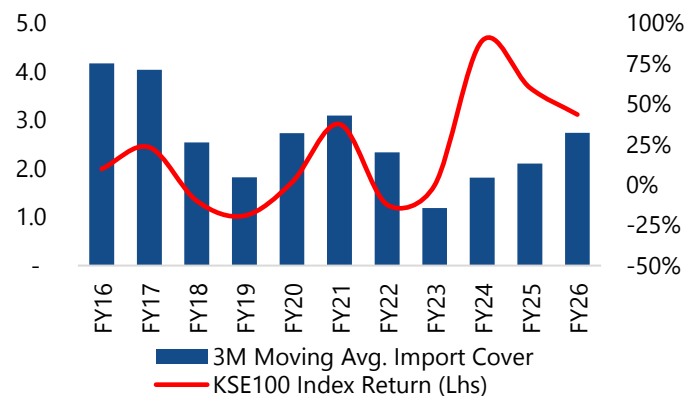
Support has carried into FY27. August remittances reached c.US\$3.7bn, up 16.5% YoY, while the monthly current-account deficit narrowed to US\$98mn. The Jul–Aug deficit of US\$543mn was 36% below the comparable period last year. These inflows provide an important cushion, although their ability to offset sustained import-cost pressure depends on the trajectory of imports and other FX flows.

Record remittances cushion the CAD



Source: SBP, IMS Research

Import cover vs. KSE-100 return



Source: SBP, PBS, IMS Research

US\$41.6bn

FY26 remittances (record)

US\$10.0bn

FY26 services exports

-US\$0.14bn

FY26 current account (~balanced)

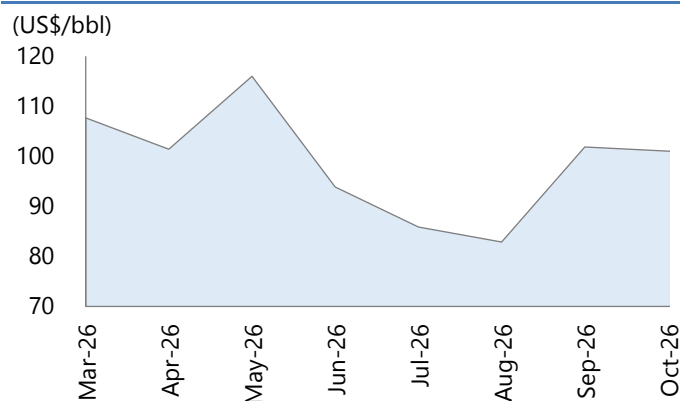
Oil prices and import volumes: the cost of the shock

Arab Light rose to c.US\$116/bbl in May following the Gulf supply shock, eased toward the mid-US\$80s by mid-summer and subsequently rebounded to c.US\$102/bbl in September. It stood at US\$105.20/bbl on 8 October.

Physical import volumes have also been volatile. Pakistan imported c.0.8mn tons of crude in July and c.2mn tonnes in August, a 62% MoM increase, taking Jul–Aug imports to c.2.0mn tons. Industry reporting attributed the increase partly to refinery inventory-building amid uncertainty over future supplies and international market conditions. The increase should not be interpreted as an equivalent rise in underlying consumption.

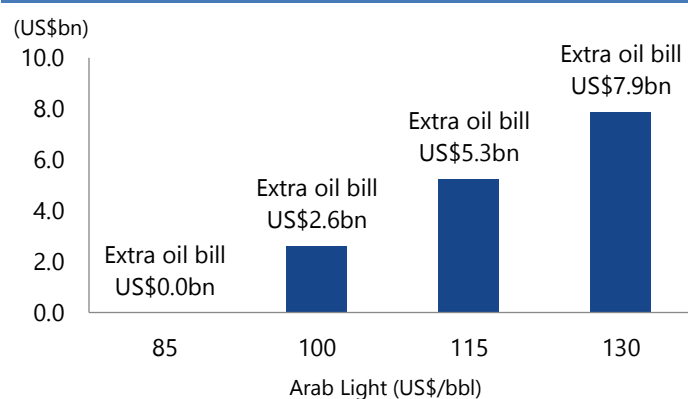
Lower crude prices would reduce the import bill even if volumes remained unchanged. An unwinding of inventory-building could provide an additional volume offset, although the extent of any normalization will depend on domestic demand, refinery runs and inventory requirements. Each US\$10/bbl increase in crude adds an estimated US\$1.5–2.0bn to Pakistan's annual oil import bill. The ultimate impact will depend on how long prices remain elevated and on the response of physical import volumes.

Arab Light rebounds after easing through summer



Source: SBP, IMS Research

Sustained high oil would test external buffers



Source: SBP, IMS Research

Historical stress episodes and subsequent equity returns

Historical episodes show that oil prices alone are a poor guide to equity performance. The condition of the external account and the policy response have been more important in determining subsequent market returns.

In September–October 2018, oil averaged US\$83/bbl, but import cover stood at only 1.7 months. The KSE-100 subsequently fell 29% over the following 12 months. Oil averaged a similar US\$83/bbl in October–November 2021, when import cover was higher at 2.5 months. The market declined 8% over the next 12 months but delivered an 81% return over 36 months.

The 2022–23 episodes also demonstrate the potential for strong returns as macro conditions stabilize. The January–February 2023 episode delivered returns of 55%, 185% and 331% over the following 12, 24 and 36 months, respectively. The July–December 2023 episode recorded corresponding returns of 89%, 203% and 335%.

These recoveries followed acute macroeconomic stress, with inflation at 28–29%, policy rates at 16.5–22.0% and import cover as low as 0.7 months. The historical record supports the potential for recovery as adjustment progresses but does not establish that the current cycle will follow the same path.

Oil shocks, external vulnerability and subsequent KSE-100 returns

Episode	Oil (US\$/bbl)	CPI	Policy rate	Import cover (x)	Return during the period	12M Return	24M Return	36M Return
Jul-Oct-08*	105	16.9%	11.1%	2.9	-25%	-42%	-21%	2%
Sep-Oct-18	83	6.2%	8.3%	1.7	0%	-29%	-2%	14%
Oct-Nov-21	83	10.2%	7.3%	2.5	1%	-8%	3%	81%
Jan-Dec-22	105	19.5%	13.0%	1.7	-9%	-9%	40%	158%
Jan-Feb-23	85	28.3%	16.5%	0.7	0%	55%	185%	331%
Jul-Dec-23	90	28.6%	22.0%	1.8	51%	89%	203%	335%

Source: SBP, PBS, Bloomberg

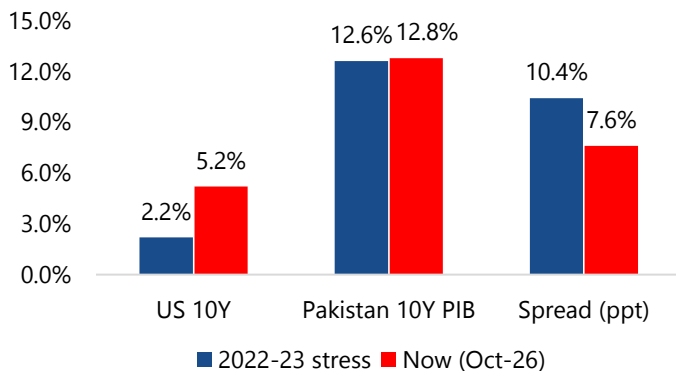
Global rates are a headwind, but Pakistan's risk premium remains contained

The US 10Y Treasury yield was c.5.25% on 9 October, compared with c.2.2% during the 2022–23 stress period. In contrast, Pakistan's 10Y PIB yield remained broadly stable at 12.8% versus 12.6%, narrowing the Pakistan–US yield differential from 10.4ppt to c.7.5ppt. This resilience is consistent with improved macroeconomic credibility and lower external vulnerability, although domestic inflation expectations and monetary policy also influence the differential.

Pakistan's return to international capital markets provides a further signal of improved financing access. The US\$3bn dual-tranche Eurobond issuance attracted nearly US\$6bn in orders, including a 10Y tranche carrying a 7.9% coupon.

For equities, higher global yields are not a standalone valuation shock; their impact depends on domestic rates, liquidity and external conditions. We do not make further tightening our base case, although another 50–100bps remains possible if inflationary pressures persist. September CPI eased to 10.3% YoY from 11.1% in August, while a higher base in 4QFY27 should support moderation. However, sustained oil-price pressures or currency weakness could delay monetary easing.

Higher US yields, narrower Pakistan yield differential



Source: Bloomberg, IMS Research

Pakistan's 5Y CDS Spread Chart



Source: SBP, IMS Research

A recovery in multiples requires macro normalization

At c.7.0x forward earnings, the KSE-100 trades below its 8.1x long-term average. A gradual recovery toward 7.5–8.5x appears plausible if external stability holds and inflation moderates. A move toward 8.5–9.5x would require greater confidence in a sustained easing cycle and normalized double-digit earnings growth.

These are scenario ranges rather than point targets. Our base case is gradual normalization, not an immediate return to peak-cycle multiples.

Current stress	Normalization	Easing + earnings recovery
6.5–7.0x	7.5–8.5x	8.5–9.5x

Source: IMS Research

The barbell approach

Defensive carry	Domestic recovery	Structural re-rating	Preferred names
<i>Cushion while visibility is limited</i> • E&Ps • Fertilizers • Selected Banks • Selected OMCs	<i>Build ahead of the first cuts</i> • Cements • Autos • Pharmaceuticals	<i>Returns independent of the cycle</i> • Refineries • ATRL • Strong balance sheet • Favorable near-term dynamics (GRMs) • Sustainable earnings	<i>Quality, yield, recovery</i> • Banks: HBL, MCB, BAFL • E&Ps / OMCs: OGDC, MARI, PSO, APL • Cements: MLCF, DGKC • Fertilizer: FFC • Refineries: ATRL • Pharma: AGP • Tech: SYS

Source: IMS Research

Investment view: attractive valuations; recovery remains conditional

At c.7.0x forward earnings, the KSE-100 trades below its long-term average and offers a c.6.5% dividend yield. Stronger reserves, improved import cover and resilient remittance inflows provide a more favourable starting point than during previous periods of external stress.

Our base case is for external stability to hold, inflation to moderate and monetary easing to become more visible into FY28. Under this scenario, valuations could recover toward 7.5–8.5x, with further upside contingent on a clearer easing cycle and sustained earnings growth.

The risks remain two-sided. A prolonged deterioration in external conditions or slower-than-expected disinflation could delay the recovery and trigger further de-rating. Conversely, continued stability would allow the market to focus increasingly on earnings normalization and lower rates.

We remain constructive on medium-term returns, supported by discounted valuations, dividend carry and the prospect of macro normalization. The timing and extent of any recovery will depend on the resilience of external conditions and the path of monetary policy.

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Ratings Guide*	Criteria
Buy	Total return expectation of $\geq$ 15% or expected to outperform the KSE-100 index
Neutral	Total return expectation of $>$ -5% or expected to match the return of KSE-100 index
Sell	Expected downside of more than 5% or expected to underperform the KSE-100 index

*Based on 12 month horizon unless stated otherwise in the report.

Valuation Methodology: We use multiple valuation methodologies in arriving at a Target Price including, but not limited to, Discounted Cash Flow (DCF), Dividend Discount Model (DDM) and relative multiples based valuations.

Risks: Not applicable

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