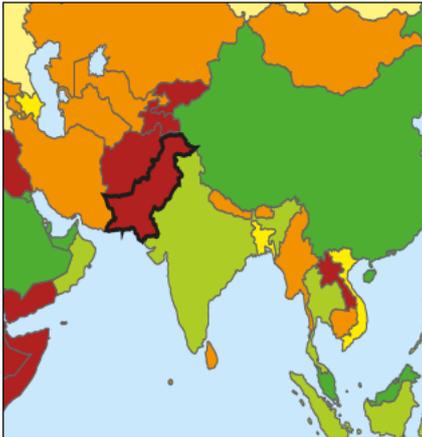




The country risk categories are arranged on a scale from 0 to 7. The lower the figure, the better the country's creditworthiness.



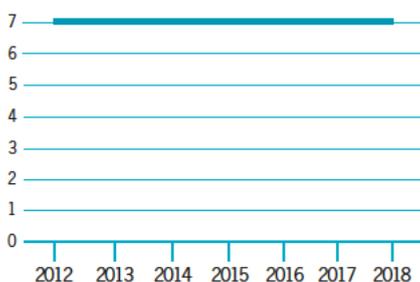
CONTACT

Country analyst: Johan Dahl
Tel. +46 (0)8 -788 00 45
email: johan.dahl@ekn.se

BASIC FACTS

Population	194 million (2016)
Nominal GDP	USD 279 billion (2016)
GDP/capita	USD 1 441 (2016)

COUNTRY CLASSIFICATION HISTORY



Source: EKN

High growth but rising current account deficit

Pakistan is characterised by political instability, a difficult security situation, a cyclical economy and weak rule of law. The country has experienced an economic upswing in recent years thanks to both progress under the completed IMF programme and China's extensive investments in the country. At the same time, the high level of growth has resulted in increasing imports and the country now once more facing a growing current account deficit and falling international reserve.

Parliamentary elections will be held in summer 2018, which means that no major, wide-ranging decisions or reforms will be enacted until the autumn at the earliest. The challenge facing Pakistan at present is to reduce the deficit while at the same time maintaining high growth in GDP. The most likely scenario is that the new government, regardless of majority, will initiate discussions with the IMF on a new economic programme in order to balance the economy.

THE COUNTRY'S STRENGTHS AND WEAKNESSES

STRENGTHS

- + Pakistan has a relatively stable banking system.
- + A steady inflow of remittances and good relations with bilateral donors and multilateral development banks.

WEAKNESSES

- Political instability, security problems and extensive military influence in both the economy and politics.
- Weak public finances and a chronic trading deficit create a fragile economy.
- Challenging business environment with weak rule of law and a high level of corruption.

SWEDISH EXPORTS TO PAKISTAN, MSEK

	MSEK
2017	2 128
2016	2 036
2015	1 966
2014	2 285
2013	1 535

Source: SCB

EKN'S EXPOSURE

	MSEK
Guarantees	8 037
Offers	1 585

EKN'S POLICY

EKN has placed Pakistan in country risk category 7, for both short-term and long-term guarantees – an assessment made in collaboration with the other OECD countries. If the counterpart is a public buyer, such as a ministry or a federal state, EKN requires a guarantee from the state. State, bank or company risks are subject to the normal risk assessment, which means that there are no predetermined restrictions on the granting of a guarantee.

EKN'S EXPOSURE AND EXPERIENCE

EKN has guaranteed 219 transactions to Pakistan with just over thirty different exporters in the last five years. Of those 219 transactions, 65 were class A or class B. The amount guaranteed over the five-year period is equivalent to SEK 2.7 billion. Most of the guarantees relate to letter of credit guarantees, and the trend is on the increase. Guarantees issued as of the end of February 2018 totalled SEK 8.0 billion and offers SEK 1.6 billion. The guarantees relate primarily to export transactions to the Pakistani state and to the telecoms sector. Outstanding late payments are modest at SEK 2.1 million, and no claims have been paid since 2014. EKN's experience of guaranteeing export transactions to Pakistan is generally good.

EKN's outstanding claims total SEK 570 million and originate from transactions in the 1990s. The claims are mainly settled in Paris Club agreements. Payments are being made according to plan and the final due date is 2024.

The difficult security situation and internal conflicts are having a negative impact on the local population. It is not clear how people's rights to housing and adequate compensation for land are being handled in major infrastructure projects.

WHAT MIGHT CAUSE A CHANGE IN THE COUNTRY POLICY

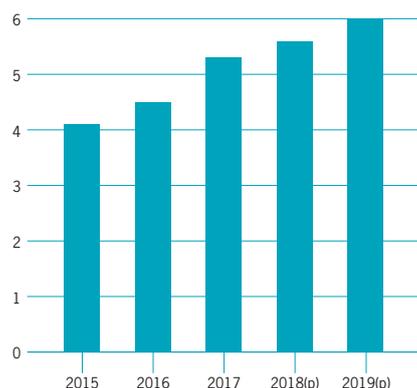
LESS RESTRICTIVE

- Sustainable, responsible and long-term economic policy that reduces deficits and the country's vulnerability.
- A more stable security situation, increased political stability and predictability contributing to international confidence, increased investments and a continued high rate of growth in the longer term.
- Intensification of the reform work within the energy sector, infrastructure and business environment, which will ultimately increase competitiveness.

MORE RESTRICTIVE

- An economic policy leading to a continuation of increased deficits, increased indebtedness or a significantly reduced international reserve.
- Deterioration of the security situation in the country.

GDP GROWTH (% PER ANNUM)



Source: IMF WEO

CURRENT ACCOUNT (% OF GDP)



Source: IMF WEO

INTERNATIONAL RESERVE (MONTHS OF IMPORT)



Source: IMF

COUNTRY ANALYSIS

BACKGROUND

Pakistan is characterised by political instability, a difficult security situation, a cyclical economy and weak rule of law. The civilian government's ability to achieve political influence is limited by military forces, the special interests of the country's elite and a confrontational political tradition. The fragile nature of the democracy is apparent from how the most recent change of power in 2013 was the first time that an outgoing government had served its full term. There will be parliamentary elections once more in summer 2018.

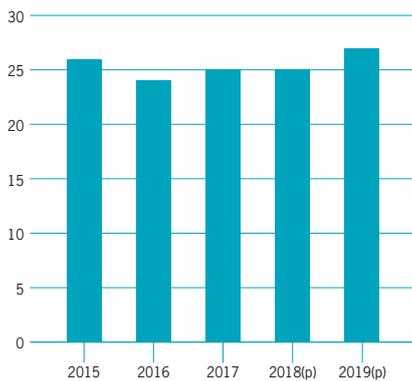
RECENT DEVELOPMENTS

The relationship between China and Pakistan is longstanding, but Chinese influence has increased considerably in recent years. Part of the enormous One Belt One Road (OBOR) initiative from China consists of investments under the heading of the China Pakistan Economic Corridor. China has announced investments in Pakistan of between USD 40 and 60 billion by the year 2030, aimed primarily at the energy and infrastructure sectors. These investments are expected to have a positive effect on economic activity and may consequently also increase the country's competitiveness. At the same time there are also new challenges such as increased indebtedness and increased dependence on China.

In contrast to the multilateral banks, China offers favourable financing opportunities without interfering in domestic policy and without requirements like those which Pakistan in many cases found it difficult to fulfil in relation to the IMF. In the area of defence, Pakistan has an established cooperation with China and a shared rival in India. Transport and energy are other sectors in which extensive cooperation is developing. The port in Gwardar in Pakistan suits China's strategy to have access to a port that does not rely on crossing the South China Sea. There are thus reasons on both sides to promote increased cooperation.

Pakistan has experienced both ups and downs since the last change of power. In the years 2013-2016 Pakistan completed a successful IMF programme, which involved increased budget discipline, progress in economic reforms and a stronger international reserve. Growth in GDP has been above four per cent for many years and is expected to approach six per cent in 2018-2019. Prime Minister Sharif was forced to step down in 2017 because of accusations of corruption in the wake of the so-called Panama Papers. Political turbulence since then has prevented important reforms. At the same time, increasing investments have brought improving growth, which has in turn resulted in a strong rise in imports. With few exceptions, Pakistan has experienced a deficit in its current account for decades, but when the economy is performing too well the deficit increases. Instead of allowing the Pakistani currency to fall in value, and thus strengthen the international reserve and increase the competitiveness of exports, the central bank has maintained a narrow target rate against the US dollar. This has made the international reserve fall quickly once more in a very short time.

EXTERNAL DEBT (% OF GDP)



Source: Pakistan Central Bank

LONG-TERM TREND

Cooperation between China and Pakistan will be the single most important factor in the economic trend for Pakistan for many years. Sustainable and productive investments on the scale being discussed represent an enormous opportunity for Pakistan. Increasing indebtedness increases the risk, but Pakistan's external debt is not alarming. The biggest proportion of the national debt is domestic and a relatively small proportion, 27 per cent in relation to GDP, is external debt. Additional improvements to the economy may be achieved by completing ongoing reforms such as, for example, increased production for export and a more cohesive tax system. While the security situation has improved, fundamental structures such as the power balance between the military and the civilian regime have not changed.

The challenge facing Pakistan at present is to extract itself from the negative spiral of an increasing deficit and a falling international reserve. Parliamentary elections are scheduled for summer 2018, which means that no major, wide-ranging decisions or reforms will be enacted until the autumn at the earliest. The most likely scenario is that the new government, regardless of majority, will blame the previous government's lack of action to justify the wide-ranging measures that are needed to get the economy back on the right track. The IMF will make tough demands for a new programme, but it is still likely that discussions about a new agreement will be initiated towards the end of the year.

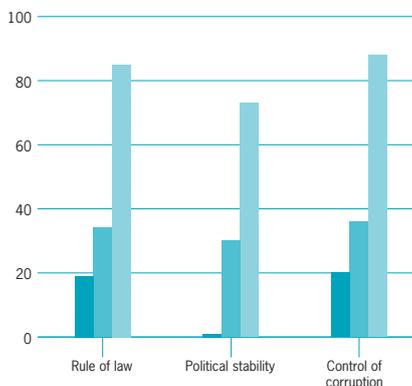
BUSINESS ENVIRONMENT

At an early stage, Pakistan undertook to use IFRS, the international financial reporting standards. During 2015, the use of IFRS, which previously solely concerned banks and large companies, was extended to also include small companies. There is relatively good insight into companies' financial situation and ownership.

Public institutions are generally very weak, do not function satisfactorily and are deficient in their implementation of regulations. The World Bank ranks Pakistan very low in terms of both corruption and rule of law, and very low in terms of political stability.

Pakistan's ranking in the World Economic Forum's competitiveness index is low, at 115 out of 137 countries, and the country ranks at about the same level in the World Bank's Doing Business Index, at 147 out of 190 countries. EKN has little experience of recovering claims in Pakistan. But according to the World Bank, the average recovery rate in Pakistan is 43 per cent, compared with 32 per cent for South Asia overall. On the other hand, the regulatory framework is in some respects modern and relatively well-developed compared with other developing countries. This is true of the banking sector, among others.

BUSINESS ENVIRONMENT



■ Pakistan
 ■ South Asia
 ■ High-income OECD

Ranking between 0 (worst) and 100 (best)

Source: World Bank

Pakistani authorities and organisations have realised that the weak ranking, among other things in the Doing Business Index, represents an obstacle to investments in the country. Against the background of the lack of any indication of more extensive structural improvements in, for example, the corruption situation, the politicisation of institutions and the legal system, the assessment is, however, that the business environment will not improve to any great extent in the coming years.