

Strategy

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MSCI reclassifies Pakistan to Frontier Market from Emerging Market; Implies Limited Market Impact

- MSCI in its latest press release has downgraded Pakistan from Emerging Market Index to Frontier Market Index, coinciding with November 2021 Semi Annual Index Review
- For MSCI Frontier market index, only 4 securities namely LUCK, MCB, HBL and OGDC meet the classification standard. These will have a cumulative weight of 1.9% (2.3% as of April 2021).
- Moreover, MSCI further seeks consultation to reclassify Pakistan in the list of eligible markets for MSCI Frontier Market 100 index and MSCI Frontier Markets 15% Country Capped Index.
- In our view, barring the outgoing securities from MSCI Emerging Market LUCK, MCB and HBL, we see neutral impact on overall market.

MSCI reclassifies Pakistan to Frontier Market Index...

Morgan Stanley Capital International (MSCI) earlier today, based on consultation on its Market Reclassification Proposal, has downgraded Pakistan from Emerging Market Index to Frontier Market Index, coinciding with November 2021 Semi Annual Index Review (SAIR).

... Amid lack of market Size and Liquidity

According to MSCI, Pakistan meets requirements for Market Accessibility under Emerging Market Classification, but no longer meets the standards for Size and Liquidity. To recall, concerns on lack of Size and Liquidity have been identified since November 2018, but Pakistan remained in Emerging Market Classification under the Index Continuity rule which pertains to achieving basic level of diversification.

4 securities to be added from Pakistan in MSCI Frontier Market Index

As of May-21 consultation documents Pakistan has 3 securities in MSCI Emerging Market, LUCK, MCB and HBL with total size of USD 1.6bn constituting to a cumulative weight of 0.02%. For MSCI Frontier market index, only 4 securities namely LUCK, MCB, HBL and OGDC meet the classification standard. These will have a cumulative weight of 1.9% (2.3% as of April 2021).

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Consultation to classify Pakistan in MSCI Frontier Market 100 Index

Moreover, MSCI further seeks consultation to reclassify Pakistan in the list of eligible markets for MSCI Frontier Market 100 index and MSCI Frontier Markets 15% Country Capped Index in its quarterly review later in by February, 2022. Under these two indices, stimulated market size of Pakistan is estimated at 5.8%.

Exhibit: Stimulated constituents of MSCI Frontier Market Index

Symbol	Name	Current Price	Shares (in mn)		Market Capitalisation (in USDbn)		Weights (%)	
			Outstanding	Free float	Outstanding	Free float	Outstanding	Free float
LUCK	Lucky Cement Limited	805.4	323.4	113.2	1.6	0.5	1.7%	0.6%
MCB	MCB Bank Limited	163.1	1,185.1	414.8	1.2	0.4	1.3%	0.4%
HBL	Habib Bank Limited	119.1	1,466.9	733.4	1.0	0.5	1.1%	0.6%
OGDC	Oil & Gas Development Company Limited	90.5	4,300.9	645.1	2.3	0.3	2.5%	0.4%
Total					6.1	1.8	6.6%	2.0%

Source: MSCI Frontier Market Index (Aug-2021), Prices as of 7/09/2021

Outlook

In our view, barring the outgoing securities from MSCI Emerging Market LUCK, MCB and HBL, we see neutral impact on overall market. Arguably the size of MSCI Emerging Market is much larger than MSCI Frontier, but Pakistan constitutes a smaller weight in Emerging Market. Hence in broader aspect, we believe domestic market will most likely be able to absorb much of the liquidity drain. As for MSCI Frontier Market, Pakistan trades at a significant discount, with respect to market multiples whereby Pakistan has a current P/E of 5.5x versus 16.5x, dividend yield of 6.7% versus 2.62% and P/B of 0.9x versus 2.2x. These discounts could potentially attract a larger share of frontier market interest.

Exhibit: Foreign Investment flows since Jun, 2017 suggest almost USD 1.4bn has been divested in Pakistan Equity market

In USDmn	Total	Corporates	Individuals
Cement	(142)	(161)	20
Fertilizer	(21)	(19)	(2)
Food	(20)	(17)	(3)
E&Ps	(432)	(450)	18
OMCs	(32)	(35)	3
Power	(66)	(63)	(2)
Banks	(459)	(482)	22
Tech	9	4	5
Textile	(45)	(45)	0
Other	(158)	(144)	(14)
Total	(1,366)	(1,412)	46

Source: NCCPL, IGI Research

Exhibit: Simulated constituents of MSCI Pakistan Frontier Market Index

Symbol	Market Capitalisation (in USDbn)		Weights (%)		Size-Segment
	Outstanding	Free float	Outstanding	Free float	
OGDC	2.3	0.3	2.53%	0.38%	Standard
LUCK	1.6	0.5	1.69%	0.59%	Standard
PPL	1.3	0.3	1.41%	0.35%	Small Cap
MARI	1.2	0.2	1.36%	0.27%	Small Cap
MCB	1.2	0.4	1.26%	0.44%	Standard
HBL	1.0	0.5	1.13%	0.57%	Standard
ENGRO	1.0	0.5	1.08%	0.60%	Small Cap
UBL	0.8	0.3	0.92%	0.37%	Small Cap
FFC	0.8	0.4	0.87%	0.48%	Small Cap
POL	0.6	0.3	0.70%	0.32%	Small Cap
HUBC	0.6	0.5	0.68%	0.51%	Small Cap
PSO	0.6	0.3	0.65%	0.29%	Small Cap
INDU	0.6	0.1	0.65%	0.11%	Small Cap
EFERT	0.6	0.3	0.67%	0.30%	Small Cap
TRG	0.5	0.4	0.57%	0.48%	Small Cap
BAHL	0.5	0.3	0.49%	0.32%	Small Cap
ABOT	0.4	0.1	0.49%	0.10%	Small Cap
NBP	0.4	0.1	0.46%	0.11%	Small Cap
SYS	0.6	0.4	0.69%	0.41%	Small Cap
MTL	0.4	0.2	0.39%	0.19%	Small Cap
SEARL	0.3	0.1	0.34%	0.15%	Small Cap
BAFL	0.3	0.1	0.38%	0.15%	Small Cap
PKGS	0.3	0.1	0.30%	0.08%	Small Cap

Source: MSCI, IGI Research, Prices as of 07/09/2021

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