



Alfalah Investments

Rated **AM1**  
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# Economic & Capital Market Outlook

**Resilient Macros,  
Compelling Value.**

*Buy the Dip!*

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## From the CIO's Desk

We live in genuinely extraordinary times. The world around us is being reshaped by forces that are simultaneous, interconnected, and moving faster than most institutions and most investors can comfortably keep pace with. The past year has been both eventful and turbulent from a global economic and capital markets perspective.

President Trump's second administration, ongoing geopolitical tensions, fiscal policy developments worldwide, uncertainty around central banks' monetary policy paths, and the artificial intelligence boom have all featured prominently. And as we sit here today, none of these forces have resolved if anything, they have deepened. On the trade front, the world has fundamentally changed. We are now navigating a new global trade order. The knock-on effects of sustained high US tariffs continue to ripple through supply chains, corporate earnings, and emerging market economies. The era of frictionless globalization that defined the last three decades is firmly behind us.

Events in the Middle East have also materially changed the near-term economic and financial outlook, with raised inflation forecasts and lowered growth forecasts across the board. Energy markets remain on edge, and how this evolves will be pivotal for commodity prices, monetary policy, and business planning everywhere.

And then there is AI, which is perhaps the single most transformative force reshaping both economies and markets. The economic gains from AI will be unevenly distributed, with technology's near-term boost to growth centered on the US, driven largely by the surge in capital spending needed to build AI infrastructure. For the rest of the world, including markets like ours, the implications are still unfolding.

Below the surface of all of this, macro risk continues to be a meaningful driver of regional stock and bond returns, creating both dislocations and opportunities for those who can read the signals clearly. In navigating this landscape, the temptation is to wait for clarity, to hold back until the dust settles, until central banks signal a definitive turn, until the geopolitical fog lifts. But a more productive approach is one of disciplined engagement: identifying where dislocations have created genuine value, where the macro noise has caused markets to misprice fundamentals.

For investors in Pakistan, this requires a dual lens one that is globally informed, alive to the cross-currents reshaping the world order, and one that is locally grounded, attuned to the specific opportunities and vulnerabilities that define our market. The road ahead will not be smooth. The road won't be easy. But markets tend to reward those who hold their conviction, stay patient, and move decisively — long before the picture becomes clear to everyone else.





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# 3QFY26 –

# Pakistan Macro Review

## All Eyes on Oil Prices

*Volatility, Value & A Resilient Macro Story*

## Executive Summary

Pakistan's economy is set to enter 4Q FY26, navigating a complex confluence of Middle East geopolitical tensions, higher international oil prices along with extreme volatility, and a fragile but intact macro-stabilization trajectory underpinned by the IMF program. National CPI has reaccelerated to 7.3% in March 2026, with upside risks mounting, if the conflict in the Middle East takes longer to settle. SBP held its policy rate at 10.5% in its March 2026 MPC meeting, signaling a prolonged pause. The last policy rate cut was in December 2025, since then the SBP has adopted a cautious stance, with a wait and see approach.

Equity markets have also depicted increased volatility, and the KSE-100 has shed over 21.4% from its January peak of 189,166 to close near 148,743 on March 31st, 2026. The forward P/E multiple for KSE100 currently stands at 6.2x, signifying a good discount to its historic average of 10x amidst similar periods of economic robustness.

The fixed income space reflects elevated sovereign borrowing needs. Our view is one of selective resilience: position for eventual rate normalization in fixed income and accumulate quality equities on dips in sectors that gain due to energy price shocks like upstream E&P Companies and Banks just in case SBP adopts a more prudent approach and looks for tightening.

3QFY26 presents Pakistan's investment community with a nuanced challenge. The macro stabilization story of the past 18 months, hard earned through painful fiscal and monetary discipline, remains fundamentally intact, but it is being tested by an external shock that the country has limited ability to insulate against. Energy import dependency is both Pakistan's near-term vulnerability and its longest-standing structural reform imperative.

For investors in Alfalah Investments' suite of funds, our message is one of disciplined patience and strategic positioning. The disinflationary tailwind that drove both equity re-ratings and fixed income capital gains in FY25 has paused, not reversed. The SBP's hawkish hold is the appropriate response; and we expect the rate-cut cycle to resume by mid-FY27. On equities, valuations are compelling at current levels, but near-term volatility may persist until there is greater clarity on the oil price trajectory and the US-Iran geopolitical situation.

### Economic Snapshot

Indicator		Mar26	Dec25	SBP / Consensus View
NCPI (YoY)	%	7.3%	6.00%	9 – 10% by Q2 FY26
Core Inflation (YoY)	%	7.4%	7.48%	Elevated; sticky
Policy Rate	%	10.50%	10.50%	On hold; next cut deferred
10Yr PIB Yield	%	12.28%	11.88%	Upward pressure near-term
PKR / USD	PKR	279.30	280.73	Broadly stable
SBP FX Reserves	USD mn	16,375	16,054	USD 18bn target by FY26-end
Trade Deficit (FYTD)	USD mn	27,805	19,310	Widening on oil shock
Brent Crude (Avg)	USD / bbl	103.62	65.36	Risk of spile to USD 120

Source (s): SBP, MOF, PBS, AAML Research

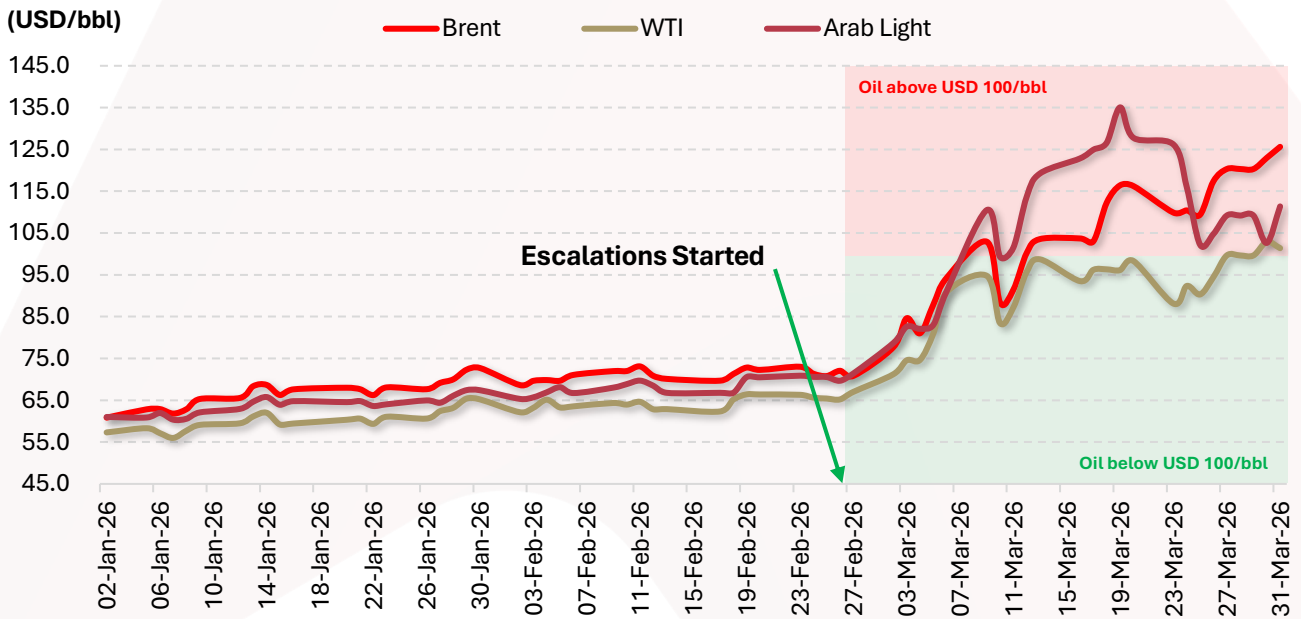


## International Oil Prices, a Structural Headwind

The dominant macro risk for Pakistan originated from the energy markets during 3QFY26. Pakistan's oil and gas production is only 25% of its total requirement. The balance is imported, making the country acutely sensitive to global price movements. Escalating tensions between the United States-Israel and Iran and the resulting disruption to Strait of Hormuz traffic, have driven Brent crude prices sharply higher from our pre-conflict FY27 baseline assumption of approximately USD 60/bbl. We believe energy prices could see a potential spike up to USD 120/bbl under a sustained supply-disruption scenario, echoing the price peaks witnessed during the Russia-Ukraine conflict of 2021-22. The last 4 months of FY26 may see the average monthly import bill rising to USD 5.8bn, compared to 8M FY26 average of USD 5.2bn, an increase of USD 400mn per month.

For Pakistan, 46% of its national electricity generation still depends on oil and RLNG-fed thermal plants constituting a significant portion, compounding the transmission of oil shocks into utility tariffs and, in turn, into CPI. The recent force majeure declaration by Qatar on RLNG cargoes has further tightened the energy supply chain, forced reactivation of domestic Sui gas production. A sustained oil price above USD 100/bbl for two or more quarters could add approx. USD 3–5bn to Pakistan's FY27 annual import bill, reigniting double-digit inflation and placing the IMF program's current account targets under severe stress.

### Oil Prices Trend – Through out the Quater



Oil Price Scenario	Approx. Brent Level	Incremental Annual Import Cost	Estimated Inflation Impact
Base / Pre-shock	USD 80/bbl	Baseline	7% CPI (Q3 FY26)
Moderate shock (Current)	USD 90 – 100/bbl	+ USD 1.5–3.0bn	Elevated- between 9-10%
Severe shock	USD 120/bbl	+ USD 3.0bn to 6bn	Potential return to double digits



## Current Account — Widening Deficit, Manageable for Now

Pakistan's external account continues to remain stable under the IMF Extended Fund Facility. The cumulative trade deficit for 8M FY26 widened 25.3% year-on-year to USD 25.1 billion, with February 2026 recording a trade deficit of USD 3.0 billion (exports: USD 2.3bn, imports: USD 5.3bn). The SBP had projected the current account deficit to remain within 0–1% of GDP for FY26, and we believe the target would be easily met, even if the oil prices remain elevated until June 2026.

Recent geopolitical developments remain a key source of concern, particularly given Pakistan's structural position as a net energy importer. Oil imports account for roughly one-quarter of the country's total import bill, making the economy highly sensitive to fluctuations in global energy prices. Historically, such shocks have translated into a widening current account deficit (CAD), increased dollar demand, and consequent pressure on the exchange rate, inflation, and policy rates—reinforcing a familiar macroeconomic cycle.

That said, the current episode appears somewhat different. Pakistan is entering this phase with relatively stronger external buffers as compared to previous cycles, which may help mitigate the severity of the impact. This view is supported by recently published official data as well as our internal estimates, strengthening our conviction that the macroeconomic fallout, while notable, may remain contained relative to past episodes.

To assess the potential impact of elevated oil prices on FY26, we extrapolate from the first eight months of import data published on PBS (including both crude and petroleum products), assuming similar volumes range for the remaining four months. Applying average prices observed since the onset of the conflict, we estimate the total import bill for FY26 at USD 65.4 billion, reflecting a 10.6%YoY increase. Encouragingly, robust remittance inflows are expected to provide a meaningful offset, with the CAD projected at approximately USD 1.6 billion, or 0.38% of GDP, levels we view as manageable given the current context. Other components of the external account are assumed to follow trends observed during the initial eight-month period.

However, the conflict has now extended beyond a month, shifting the key risk variable from intensity to duration. In our view, a further prolongation of 3–4 weeks could materially alter the outlook, as sustained elevated prices and uncertainty would begin to weigh more heavily on global and domestic economic activity. Under such a scenario, the risk of a broader downturn, both globally and domestically, would rise significantly, potentially overshadowing the relative resilience currently observed.

### Current Account Estimates

USD mn	FY25	FY26E
<b>Current account balance</b>	<b>1,932</b>	<b>(1,773)</b>
Exports of goods FOB	32,340	30,578
Imports of goods FOB	59,111	65,533
Balance on trade in goods	(26,771)	(34,955)
Balance on trade in goods and services	(29,416)	(37,613)
Workers' remittances	38,300	42,000

Source (s): AAML Research

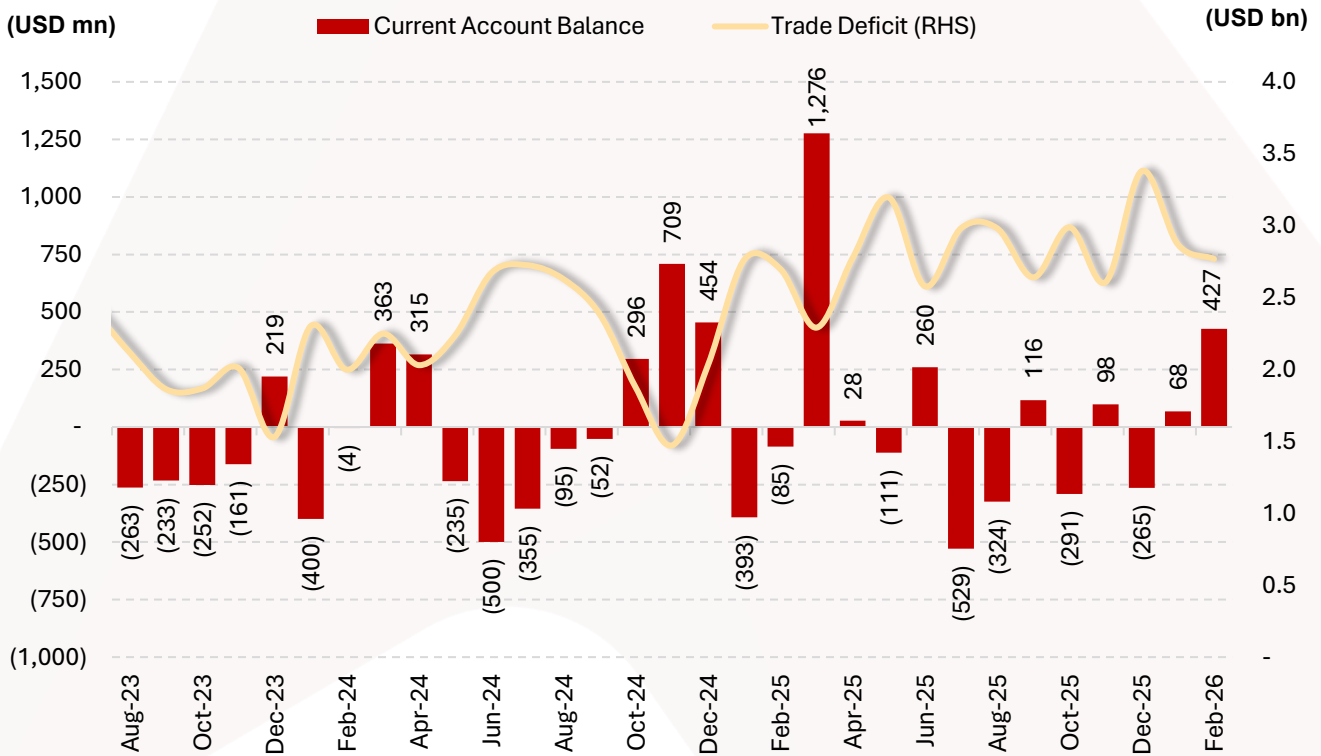


### Potential Risk factors to current account deficit widening

- Petroleum imports projected to rise 13% - 15% YoY as oil prices surge, contributing 26% to total imports in FY26.
- Global shipping and insurance costs can also remain elevated due to heightened regional maritime risk, which can add significantly to the import bill.
- 55% of total remittances originate from GCC economies, face downside risk if oil-dependent GCC growth contracts and demand for expatriate labor declines.
- If the current environment persists over a sustained period, with oil prices remaining elevated at USD 120+, the current account deficit could expand materially from the present estimate of around USD 2 billion to approximately USD 6–7 billion in FY27.

Current account deficit for FY26 will still be manageable at only 0.3-0.5% of GDP, well within the SBP's 0–1% target and within manageable bounds.

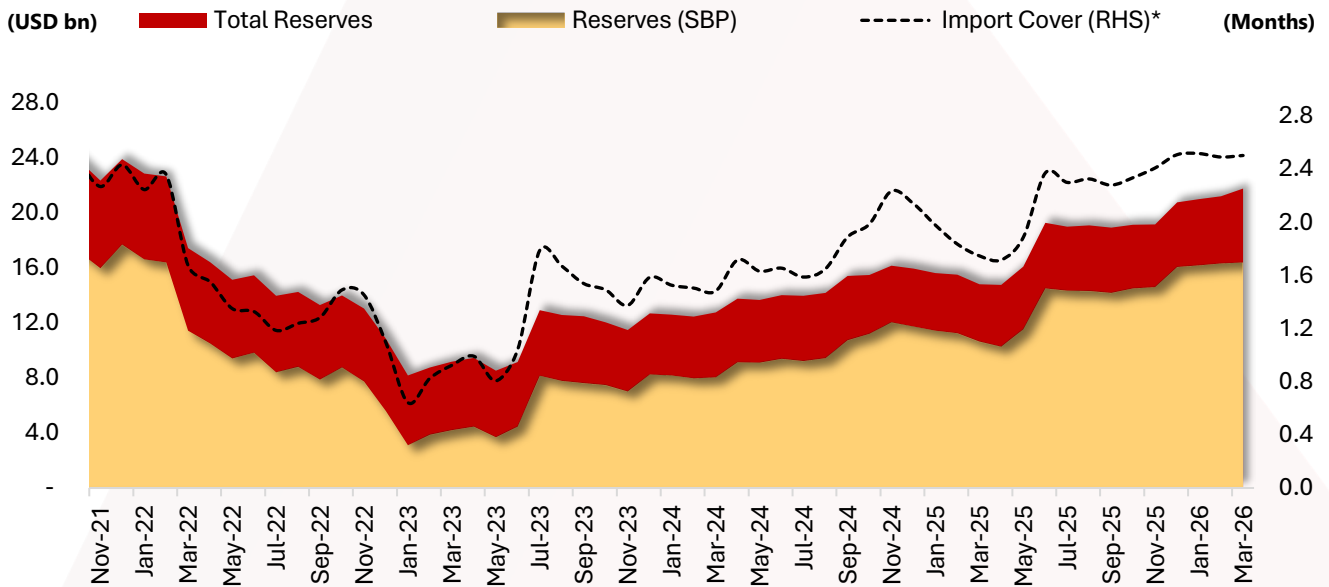
### Current Account Balance & Trade Deficit:



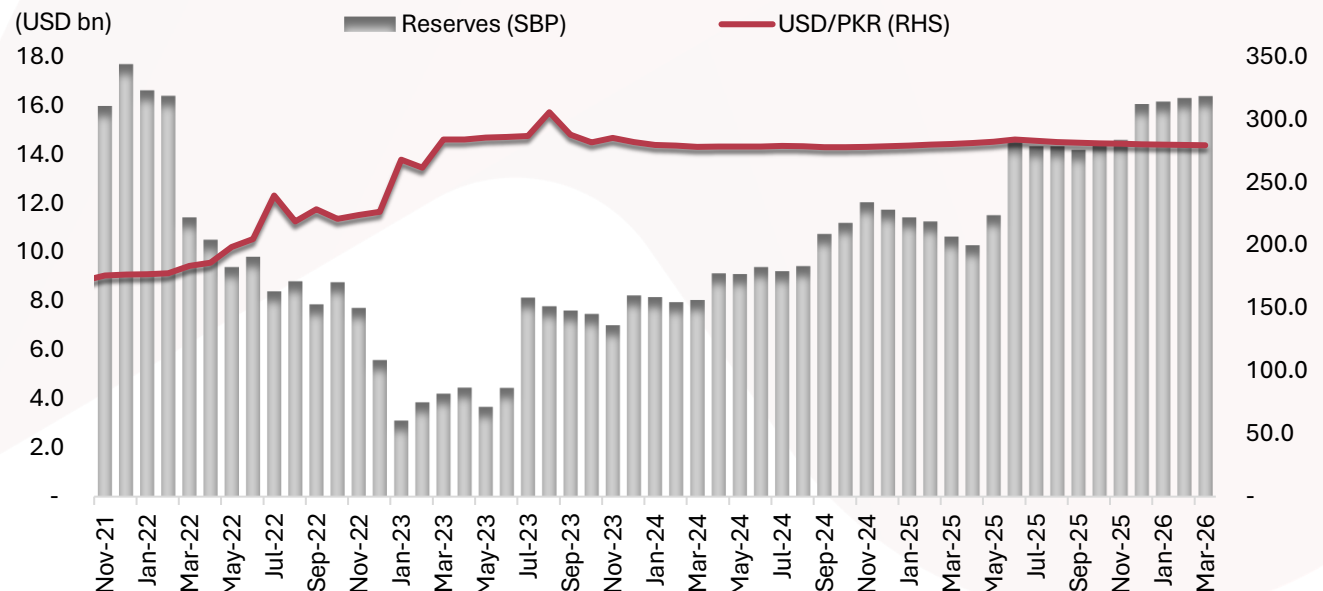
## FX Reserves

FX reserves have improved steadily. SBP-held reserves stood at USD 16.3bn as of March 2026, up from critically low levels of USD 2.9bn, in FY23, providing a meaningful buffer, of about 3x import cover. The pace of reserve accumulation is likely to slow meaningfully however, if the current account deteriorates materially in FY27. The IMF program remains the critical anchor; Pakistan's management of the energy shock will be closely watched by the IMF ahead of the next review, scheduled for December 2026.

### Foreign Exchange Reserves & Import Cover:



### Foreign Exchange Reserves & USD/PKR:



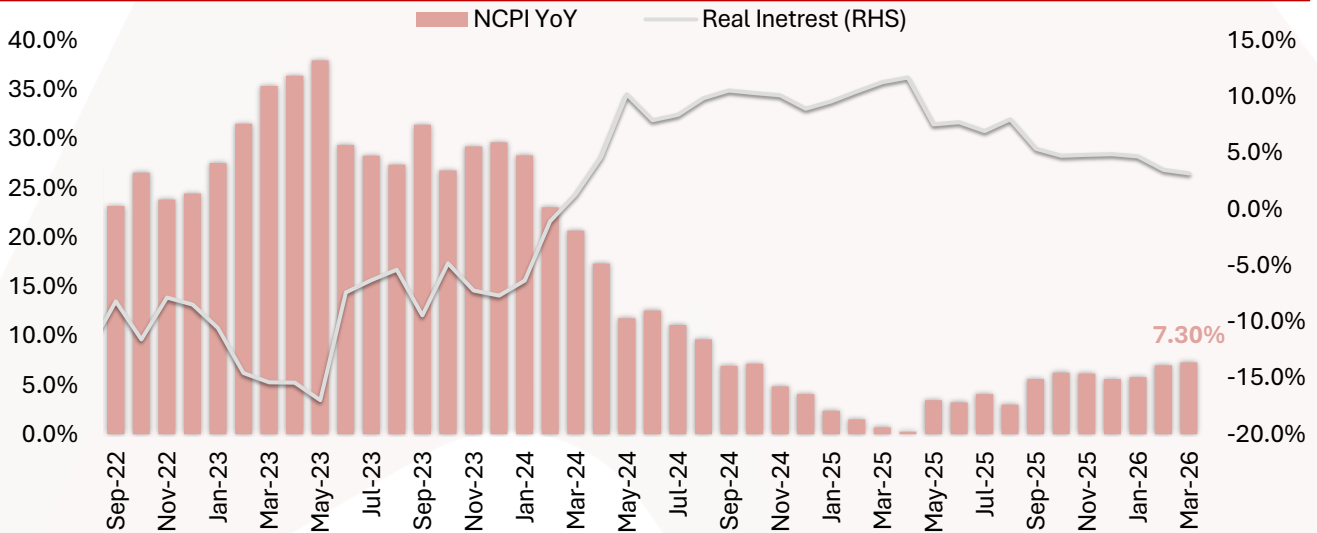
## Inflation — Reversal of the Disinflation Trend

After an impressive disinflationary cycle that saw CPI fall from a near-50-year high of above 30% in mid-2023 to a recent low of 5.6% in December 2025, Pakistan's inflation trajectory has reversed. Headline CPI rose to 7.3% YoY in March 2026, highest reading since October 2024, which was driven primarily by rising transport fuel costs, energy tariff increases, and housing and utilities inflation. Core inflation remained sticky at 7.4% in March 2026, underscoring persistent underlying demand pressures.

### Inflation drivers for 2H FY26

The government implemented a fuel price increase of Rs 55 per liter in March 2026, which was the largest single adjustment in recent history, as it passed through global price increases to domestic consumers. This will feed into the inflation number for March 2026. After this increase, GoP decided to stall fuel price hikes, at least for a month, keeping the spike in inflation under check for March 2026. Should Brent crude approach USD 120/bbl, the return to double digit inflation, last seen during the 2022-23 crisis, cannot be ruled out, though such an outcome represents a tail risk rather than our base case. Average CPI for Q4 FY26 (Apr–Jun 2026) is projected at 10.7%, assuming another round of fuel price hike under current oil price assumptions. We have revised our full-year FY26 average inflation upward to approximately 6.50-7%, against our earlier forecast of 5.4–6.0%, still a comfortable spread of 450bps over policy rate of 10.5%.

### National CPI & Real Interest Rate:



Component	March 2026 YoY	Comment
Headline CPI	7.30%	Highest since Oct-24; oil shock lagging
Core Inflation	7.40%	Demand-side pressures persisting
Housing & Utilities	11.49%	Energy tariff pass-through
Transport	Recovering	Fuel price hike of Rs55/litre in Mar-26
Food (Non-perishable)	5.00%	Input cost pressure via fuel & fertiliser
Food (Perishable)	Declining	Seasonal easing; near-term respite



## Monetary Policy — Rate Cut Cycle on Pause

The State Bank of Pakistan's Monetary Policy Committee (MPC) surprised markets with a hold at 10.5% in its January 2026 meeting (consensus expected a cut to 10.0%), and reiterated the pause at the March 2026 meeting, citing heightened economic uncertainty from the Middle East energy shock. This represents a significant shift in the MPC's stance: earlier in the easing cycle, the SBP had reduced rates from a peak of 22% in June 2024 to 11.0% by end-2025, a cumulative 1,100 basis points of easing.

## Alfalah Investments — Policy Rate Forecast

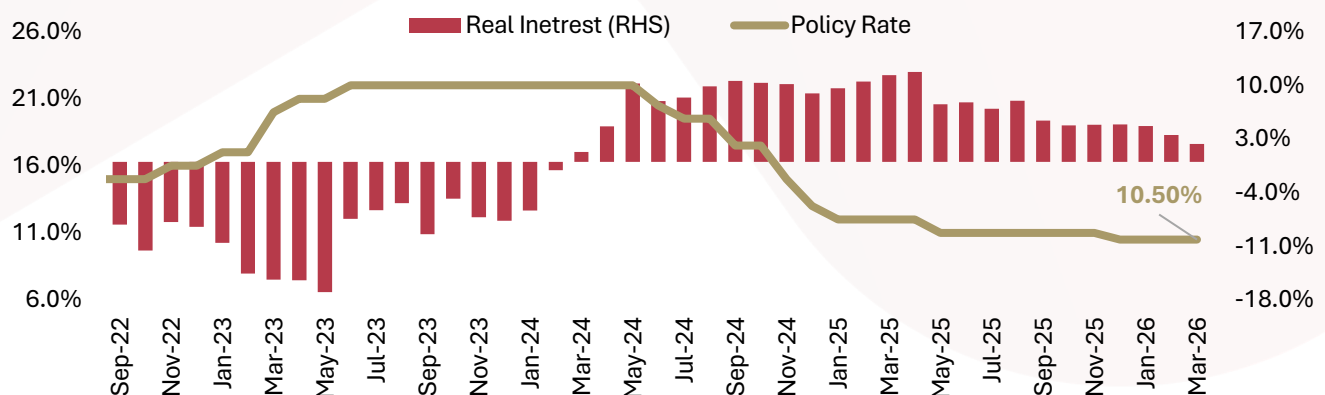
MPC Meeting	Our Forecast	Rationale
March 2026 (actual)	Hold at 10.5%	Oil shock, inflation uptick
April 2026	Hold at 10.5%	Inflation likely to peak
October 2026 (2Q FY27)	Hold at 10.5%	Conditional upon oil price passthrough
December 2026 (3Q FY27)	Gradual cuts to 9.5%	Conditional upon retraction in oil prices

The SBP's policy rate at 10.5%, depicts approximately a 350–400 basis points over headline CPI, and provides some room for a cut, however we believe, the SBP MPC will remain cautious and hold the rates at current level. We believe three conditions must be met before the next rate reduction:

- Inflation must be trending back toward the SBP's target range of 5–7% band;
- Current account must remain within IMF program parameters; and
- PKR must remain broadly stable, avoiding any pass-through from currency depreciation into import prices.

PKR has held steady showing, currently trading near Rs 279/USD as of mid-March 2026, supported by IMF inflows and a measured import management approach. This stability is critical for SBP's anti-inflation narrative. Any deterioration in the external account that forces the SBP into currency defense could delay the rate-cut cycle by two or more quarters, in our view.

## SBP Policy Rate & Real Interest Rate:





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# 3QFY26 –

# Pakistan Capital Market Review

## Fundamentals Intact

*Opportunity to unlock!*

## Capital Market Review:

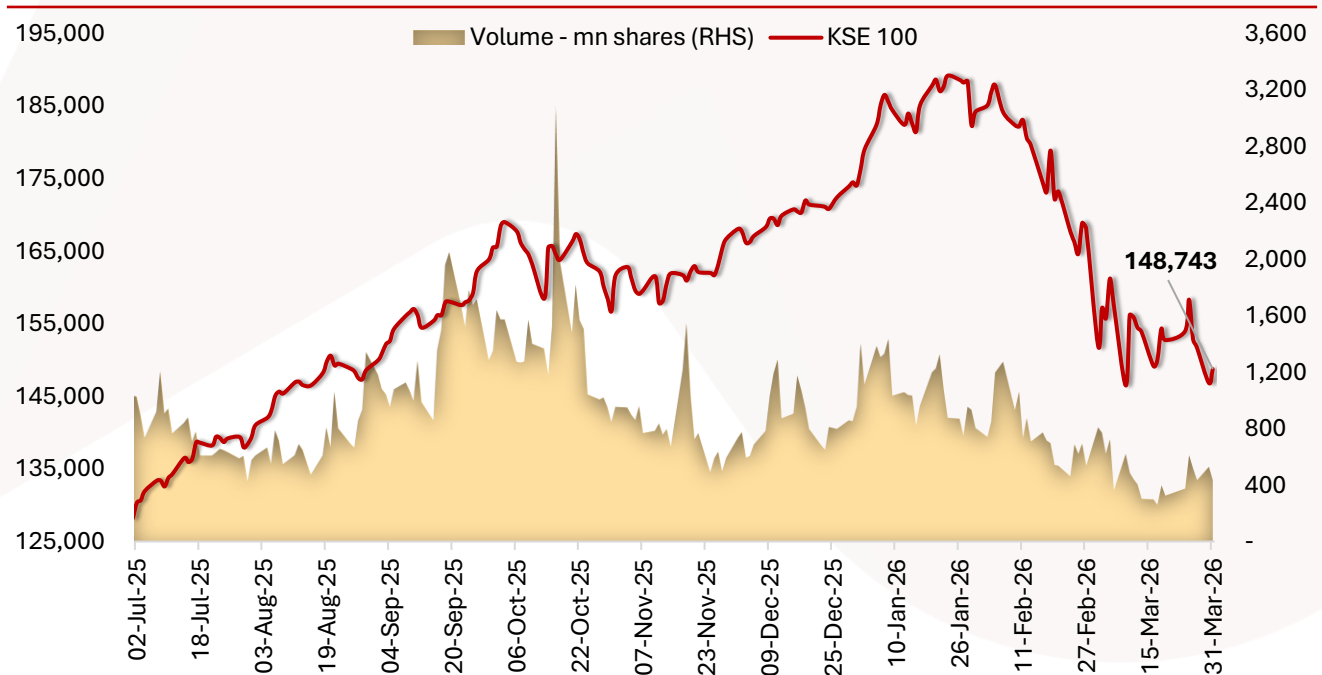
Pakistan equities have remained one of the most compelling global investment stories, with the KSE-100 Index delivering a 51.2% return in CY25, extending a strong multi-year rally. This performance has been driven by macroeconomic stabilization, IMF-backed reforms, easing monetary conditions, and renewed privatization momentum. Over the past three years, the market has generated a cumulative return of 330.61%, positioning it among the top-performing asset classes globally.

The momentum carried into early January 2026, with the index reaching an all-time high of 189,167, before undergoing a sharp correction to 148,743 points, translating into a negative return of -14.54% during 1Q CY26. The pullback was initially triggered by muted corporate earnings and a status quo stance by the SBP, which tempered expectations of aggressive monetary easing. However, the correction deepened as geopolitical risks intensified, particularly rising US-Iran tensions, which led to broader risk-off sentiment across emerging markets.

On the domestic front, trade and logistics disruptions stemming from strained relations with Afghanistan added further pressure, particularly on export-oriented sectors. As a result, key index-heavy sectors, including Banking, Exploration & Production (E&P), and cyclicals, experienced notable selling, amplified by foreign outflows and mutual fund redemptions.

Despite these near-term headwinds, Pakistan’s macroeconomic fundamentals remain significantly stronger compared to previous global shock periods. Improved foreign exchange reserves, a contained current account deficit, moderating inflation, and resilient remittance inflows provide a solid buffer against external volatility. In this context, the recent correction appears largely sentiment-driven rather than fundamentally driven. While elevated oil prices remain a risk for a net energy importer like Pakistan, the impact is expected to be manageable unless sustained over a prolonged period.

### KSE-100 Index Trend:



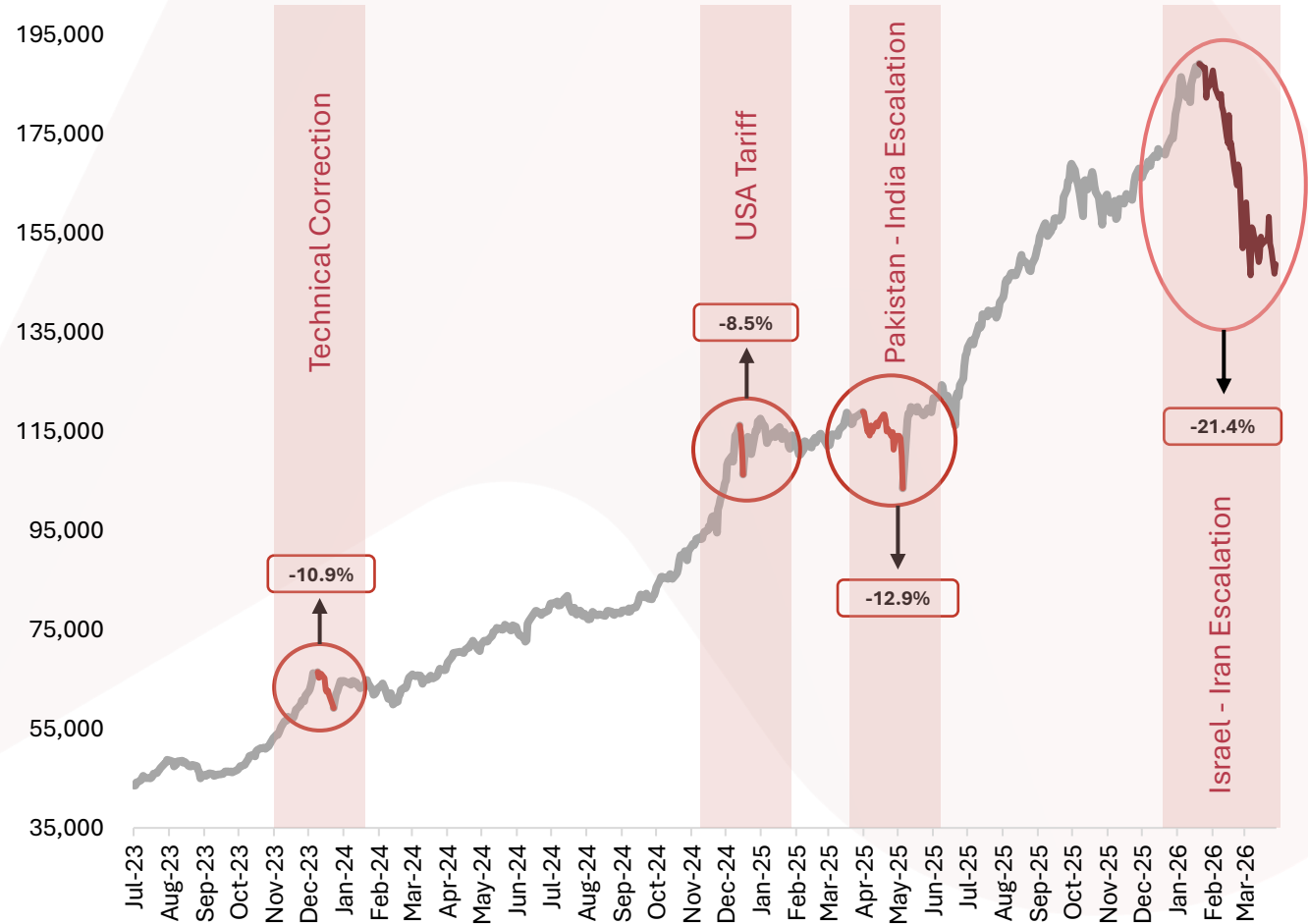
## Investment Strategy – Opportunity in Dislocation

The market has corrected approximately 18% from its January 2026 peak, primarily due to external uncertainties and temporary domestic factors, rather than any structural deterioration. This has led to a meaningful valuation reset, with the KSE-100 now trading at a forward P/E of ~6.2X, representing a significant discount to both historical averages and regional peers. At these levels, equities offer an estimated upside potential of ~40%, compared to 9–10% yields on fixed income instrument, strengthening the relative attractiveness of equities.

Historically, corrections of this nature in the KSE-100 have often been sharp but short-lived, with the market exhibiting a tendency toward V-shaped recoveries once sentiment stabilizes and valuation comfort returns. We believe the current environment reflects a similar phase, where temporary dislocation is creating entry opportunities for long-term investors.

The broader equity story remains intact, supported by improving macro stability, earnings resilience, and attractive dividend yields of around ~6%, which remain compelling in both regional and historical contexts. As such, we view the ongoing consolidation as a strategic accumulation phase, particularly in fundamentally strong and high-quality names across key sectors.

### KSE-100 Index Historic Corrections:

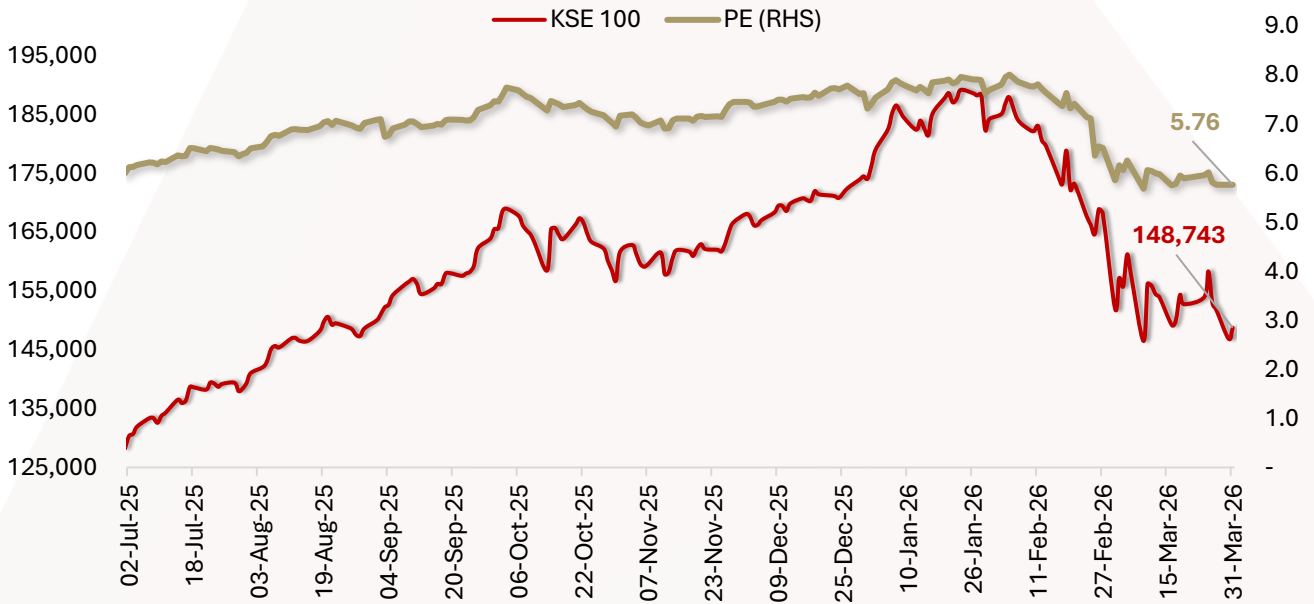


## Equity Market Strategy — Selective Accumulation on Weakness

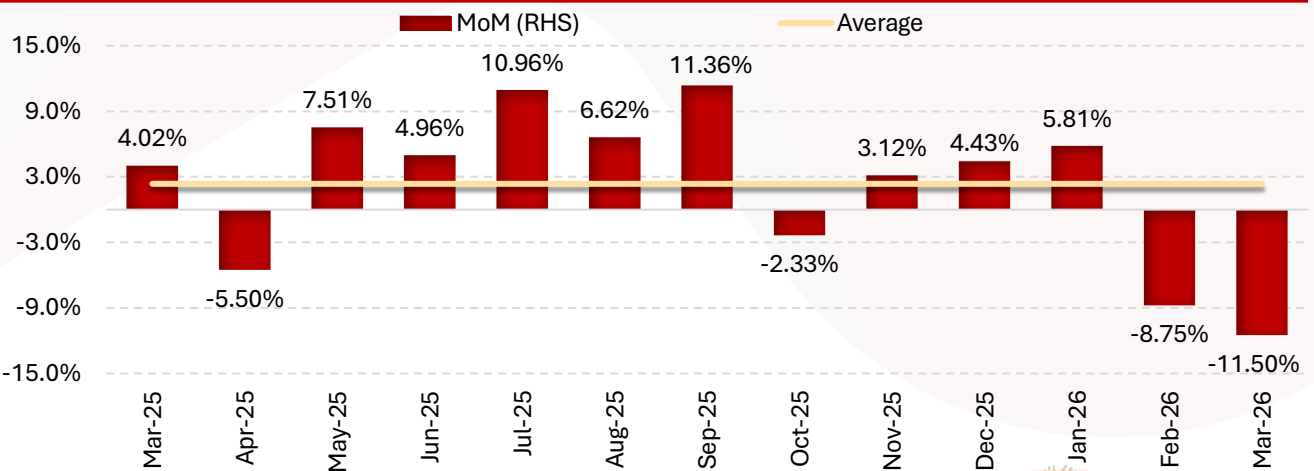
Looking ahead, market direction will be shaped by a combination of macro and external factors. Key catalysts include the IMF program review, where a successful outcome is expected to unlock inflows and reinforce investor confidence; the trajectory of global oil prices, with any easing in geopolitical tensions acting as a major positive trigger; and monetary policy direction, where a potential rate cut could drive a sharp re-rating in equities. Additionally, corporate earnings, particularly in E&P and energy-linked sectors, are likely to depict growth in the current macro backdrop.

While near-term volatility may persist, the combination of strong macro buffers, attractive valuations, and structural growth drivers continue to support the long-term investment case for Pakistan equities. The recent correction, in our view, represents a healthy reset rather than a trend reversal, offering a compelling opportunity for selective and disciplined accumulation as the market positions for its next leg of growth.

### KSE-100 & PE (f):



### KSE-100 Index MoM Returns:





# Alfalah Investments

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