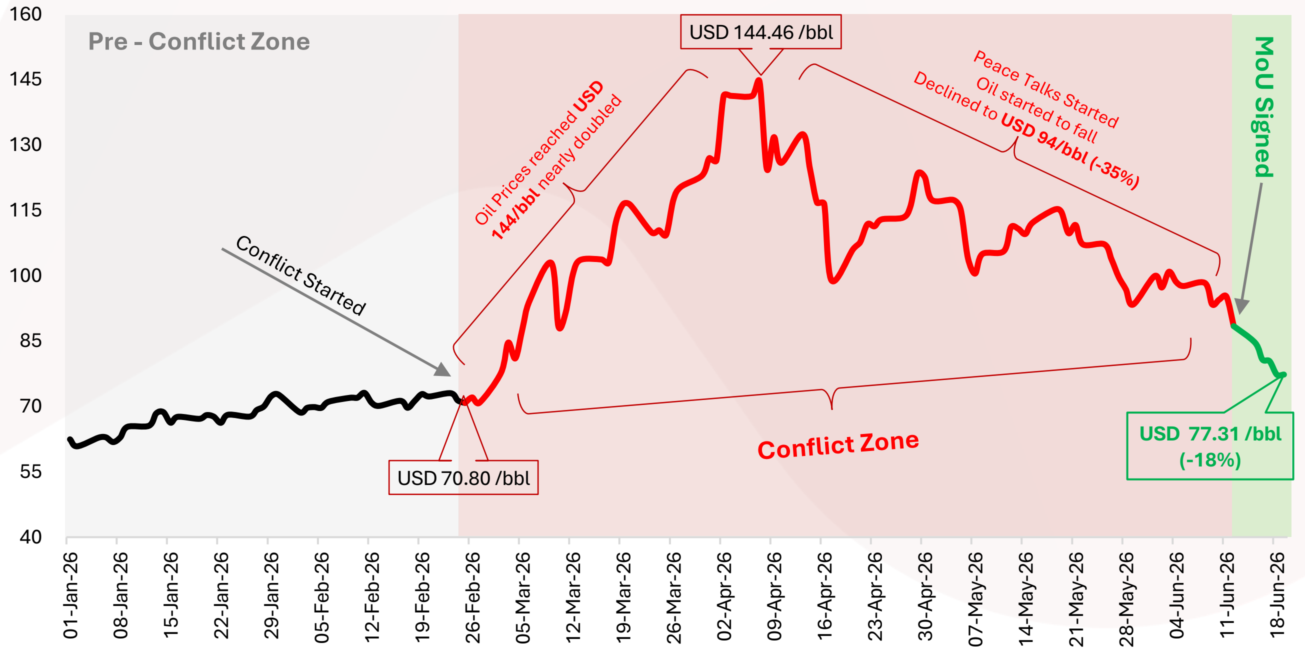
The Oil Dividend: Pakistan's Second Catalyst Arrives

When we wrote of a Peace Premium six weeks ago, we argued that Pakistan's diplomatic breakthrough would generate economic dividends whose full magnitude markets had not yet begun to price. The first of those dividends has now arrived, as a major milestone is achieved. Acting as a credible and neutral intermediary, Pakistan successfully convened foundational negotiations that led to the signing of a Memorandum of Understanding (MoU) between the US and Iran this week. Substantive negotiations are advancing in Switzerland, the next 60 days are crucial, and the delegations are working through the technical architecture of normalization. While geopolitical volatility typically accompanies such transitions, and near-term oil price swings are to be expected, the MoU has fundamentally altered the trajectory. With both parties now formally committed to a structured dialogue framework, we do not expect any further military interventions. Reacting to this, the global oil markets repriced with speed, and Brent Crude fell more than 30% as a knee jerk reaction, shedding over USD 22/bbl in five trading sessions. Markets are pricing in the full normalization of Iranian supply to a world that was already adequately served. For Pakistan, this is not a commodity development. It is the direct, measurable economic payoff of the peace deal it helped mediate.

The linkage is structural. Pakistan imports approximately 85% of its petroleum requirements. Its energy import bill, running at approximately USD 14–15 billion annually, has been the single most persistent constraint on the current account, the fiscal position, the exchange rate, and by extension, the entire trajectory of monetary policy. Prior to the conflict, oil had averaged approximately USD 60-70/bbl, manageable within Pakistan's current account framework. Escalation drove prices to settle at USD 92/bbl, adding an estimated USD 3–4 billion per annum of additional import pressure to an already strained balance of payments estimates for FY27 estimates. A 20% decline from the conflict period average levels of USD 90/bbl in global oil prices does not improve one of these ledgers. It improves all of them, simultaneously. We estimate the annual saving on Pakistan's petroleum import bill at USD 3.0–4.0 billion from where it could have peaked, assuming oil reverts back to its pre-conflict levels, a figure equivalent to approximately 1.0–1.3% of GDP.

Brent Crude Oil Price Trend (USD/bbl):



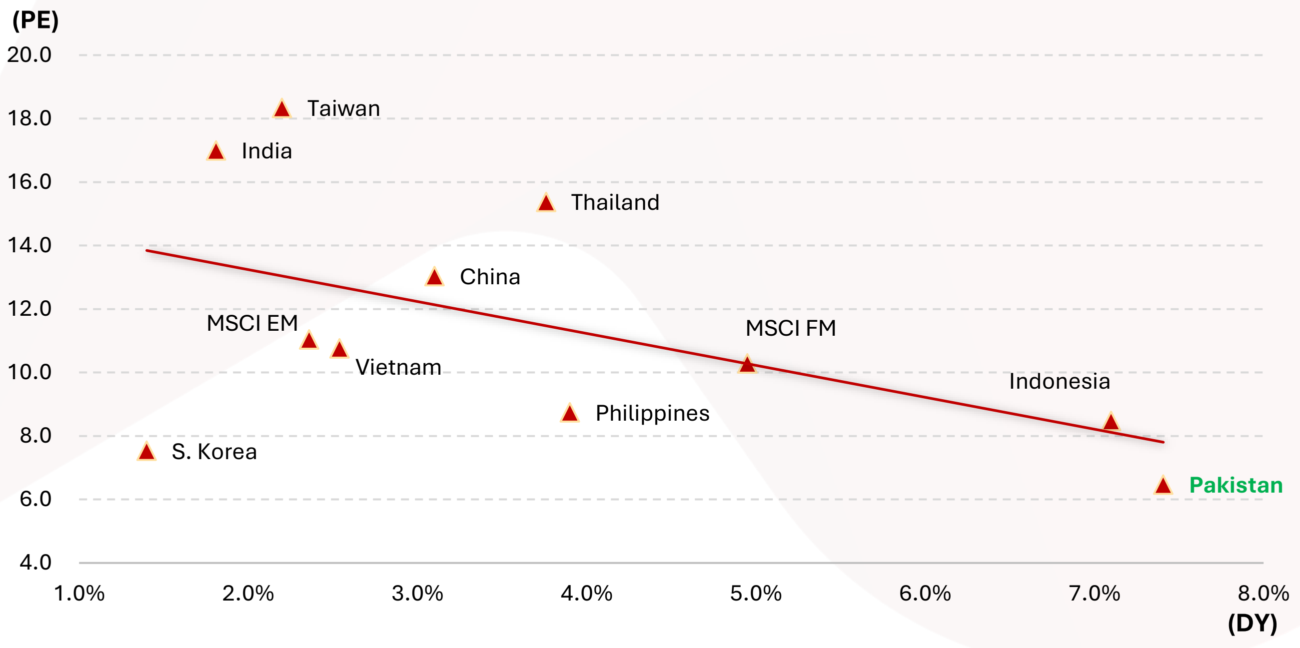
Capital Markets have noted this with characteristic efficiency. The KSE-100, which surged 9.58% on the ceasefire announcement in April, now confronts a second and structurally distinct catalyst, one that operates not through the removal of risk premium, but through the direct improvement of underlying fundamentals. Both forces, taken together, represent the most compelling risk-reward configuration Pakistan's equity market has offered in at least a decade. The investment case, already compelling in April, has just been materially strengthened.

The Arithmetic of the Dividend

We have already seen HSD and Motor Gasoline prices in Pakistan decline by 40% and 34% respectively from their peaks. For Pakistan, the transmission from lower oil to improved fundamentals is rapid and multi-layered. On inflation: Pakistan's headline CPI, highly sensitive to fuel price movements through transport, utilities, and industrial input costs, is expected to ease by 200–350 basis points over the next two to three months, assuming the government passes through the benefit of lower petroleum prices. This creates conditions for the SBP to materially accelerate its rate easing cycle, potentially delivering 100–200 basis points of additional policy rate reduction in 2H CY2026 beyond what was previously anticipated.

On the fiscal front: lower energy costs directly reduce the accumulation of the power sector's chronic circular debt, ease the subsidy burden on the exchequer, and improve the primary fiscal balance, at precisely the moment when the IMF program demands visible consolidation. PKR already more insulated from depreciation pressure following the ceasefire-induced current account improvement, gains additional structural support as petroleum import payments shrink. In aggregate, these forces create a self-reinforcing cycle: lower oil, lower inflation, lower policy rate, higher equity valuations, stronger investment confidence and greater economic activity. However, this transmission fully materializes only if the US-Iran ceasefire deal and associated MOU remain intact; any reversal in geopolitical tensions or breakdown in negotiations are likely to quickly reverse the oil price decline and eliminate these tailwinds.

Regional Markets PE and DY:



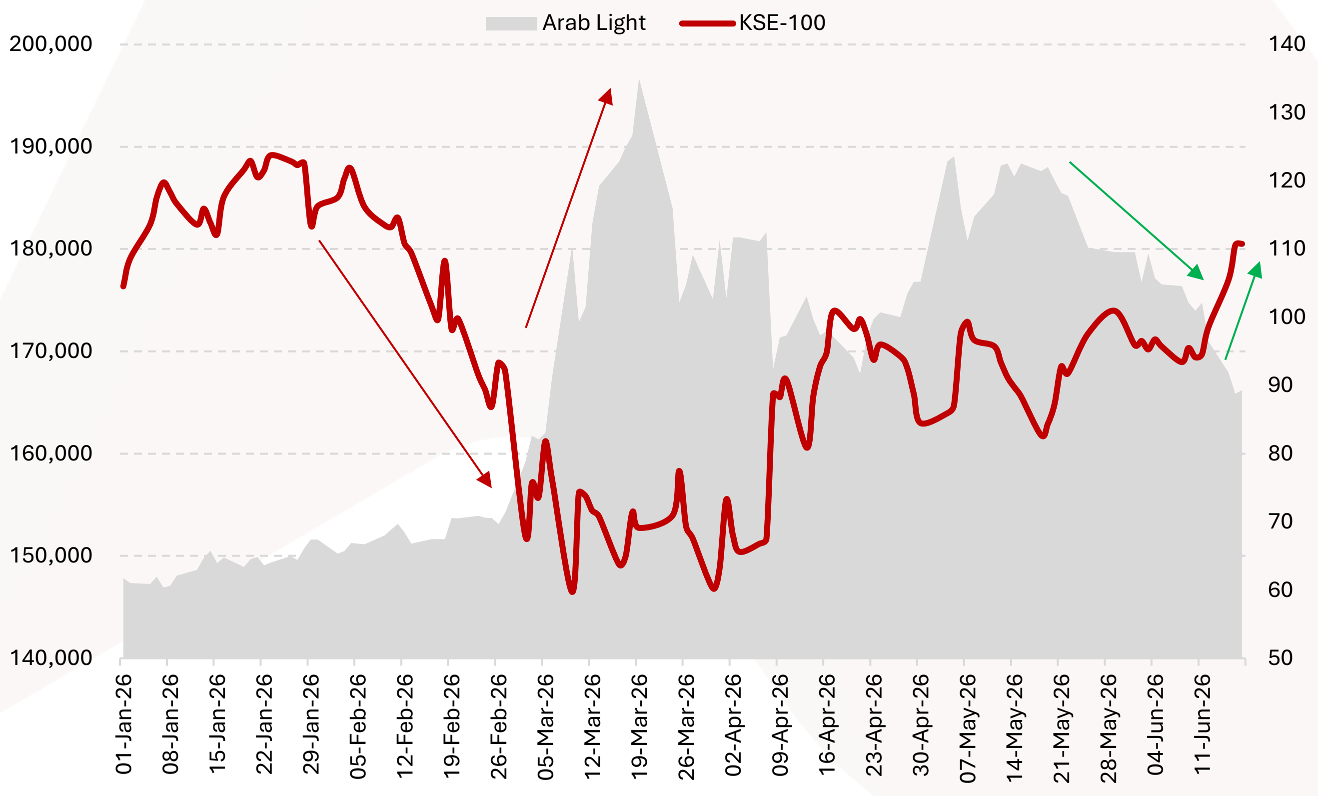
The Second Leg: From Inflection to Acceleration

Pakistan's equity market, still trading at a forward P/E of 6.5x, a 40% discount to the MSCI EM Index, now benefits from a compounding re-rating dynamic. The earnings base grows as input costs fall across the industrial, consumer, and financial economy and the discount rate falls simultaneously as monetary easing accelerates. When both the numerator and denominator of equity valuation move in the right direction at the same time, the outcome is not incremental. It is transformational.

For equity allocations, the sectoral implications are clear and actionable. Banks benefit from accelerating credit demand, lower provisioning requirements, and the steepening rate-easing cycle that lower inflation enables. Textiles, Pakistan's largest export earner, see energy input costs compress the cost of production and improve export competitiveness simultaneously. Cement, fertilizers, and consumer-facing businesses see margin expansion as energy-intensive production costs decline. The oil and gas exploration sector will face wellhead price headwinds.

KSE100 had lost 23% to a low of 146,480 points by March 2026 since January 2026, which has since then recovered meaningfully to 180,511 with a gain of 23.2% from its trough. The oil dividend, if sustained, as current US-Iran framework terms suggests it will be, sets the stage for the second and more fundamental leg of that recovery: one driven not only by sentiment reversal but by improving earnings, lower rates, and a macro backdrop that is for the first time in years, genuinely supportive of sustained economic growth.

KSE-100 Index Trend:



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