24 September 2021

Regulatory Tightening

SBP revises Prudential Regulations for auto and consumer financing

The State Bank of Pakistan (SBP) has revised Prudential Regulations (PRs) for consumer financing to moderate imports and demand growth. This follows recent measures undertaken to curb import-led demand which include allowing the c.7% CY21td PKR devaluation, a 25bps hike in interest rates in the September Monetary Policy and an increase in cash margins on imports of luxury goods (to 100% of value). These targeted steps will help to moderate demand and consequently reduce the burden on balance-of-payments. We understand that the government may levy further measures to curb imports.

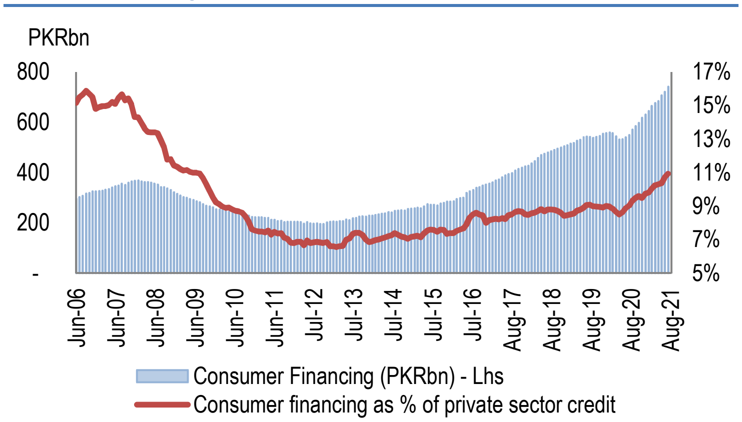
Changes to the Prudential Regulations	Potential impact
Personal loans & credit cards	
Maximum tenure of personal loan has been reduced from five to four years Maximum debt-burden ratio, allowed to a borrower, has been decreased from 50% to 40%	This will help moderate public spending and reduce risks associated with personal loans and default risk.
Auto Financing	
Maximum tenure of auto finance has been reduced from seven to five years Overall auto financing limits availed by one person will not exceed PKR3mn at any point in time Minimum down payment for auto financing has been increased from 15% to 30%	This may reduce demand at the margin for financing of domestically manufactured/ assembled vehicles of >1000 cc engine capacity.
Restrictions on loans given for new and used imported vehicles	This may improve sales of locally assembled vehicles.

Source: SBP Circular and IMS Research

We do not anticipate a widespread impact

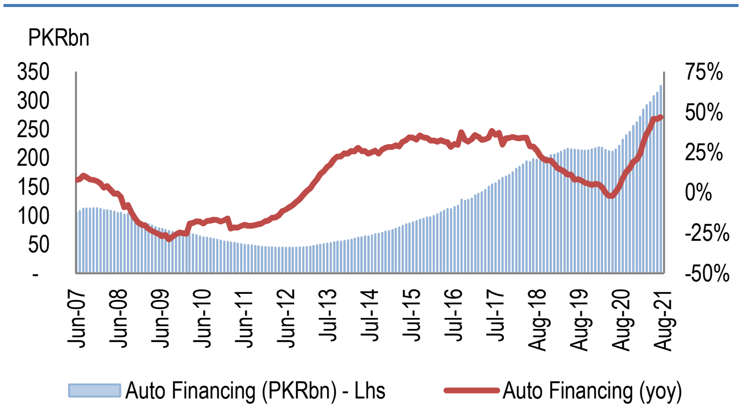
Consumer financing accounts for c.11% of total private sector credit in Pakistan, with Auto financing forming a large portion (over 40%) of all consumer loans. Growth in auto loans has surpassed 40% yoy in the past few months rising to 4.8% of private sector credit vs. 3.5% pre-Covid, while personal loans are also growing sharply, up over 20% yoy. While changes in Prudential Regulations may moderate import-led demand at the margin, a greater push is likely to occur from further monetary tightening, in our view. Moreover, SBP continues to protect the lower to middle income category purchases, as these new regulations are not applicable to locally manufactured or assembled vehicles of up to 1,000cc engine capacity.

Consumer financing as a portion of private sector credit



Source: SBP

Growth in Auto financing at historically high levels



Source: SBP

Continued on the next page…

Abdul Ghani Mianoor
abdul.ghani@imsecurities.com.pk
+92-111-467-000 Ext: 101

Yusra B. Farhan
yusra.beg@imsecurities.com.pk
+92-111-467-000 Ext: 305

PSMC is a key beneficiary

We highlight that despite the greater cost of used imported vehicles amid sharp PKR depreciation, FY22td CBU imports have risen a staggering 2.3x yoy. PSMC stands as the main beneficiary from the revised PRs due to the exclusion of assembled vehicles up to 1,000cc, in our view (PSMC is presently producing cars below 1,000cc following the discontinuation of the Swift model). The restriction on financing of used vehicles (lower share in overall auto finance loans), may potentially result in greater local sales (import substitution). However, the impact is unlikely to be very significant, in our view.

The impact on INDU and HCAR, however, is likely to be negative, in our view, where according to our back-of-the-envelope estimates, financing may be provided for cars up to c.PKR4.2mn (maximum finance allowed to be raised is PKR3.0mn; 70% debt finance). Sales of cars above 1,800cc such as the Fortuner, Revo, Sportage, Tucson and Sorento, among others, are likely to slow down, in our view.

The revised PRs are aimed at reducing auto financing, which is likely to impact HCAR due to the high share of auto financing contribution to overall sales (c.40%), while INDU's auto-finance-led sales are c.30%, due to the greater share of sales in the rural centers. PSMC in this case remains unscathed, in order to protect the interest of the lower to middle income groups.

We, Abdul Ghani Mianoor and Yusra B. Farhan, certify that the views expressed in the report reflect our personal views about the subject securities. We also certify that no part of our compensation was, is, or will be, directly or indirectly, related to the specific recommendations made in this report. We further certify that we do not have any beneficial holding of the specific securities that we have recommendations on in this report.

Ratings Guide*	Criteria
Buy	Total return expectation of ≥ 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: (i) PKR depreciation against Yen and US$, (ii) adverse regulatory measures, and (iii) decline in sales due to delta variant.

RESEARCH DISCLOSURES

Third Party Research

This is third party research. It was prepared by Intermarket Securities Limited (IMS), with headquarters in Karachi, Pakistan. Intermarket Securities Limited (IMS) is authorized to engage in securities activities according to its domestic legislation. Intermarket Securities Limited (IMS) has sole control over the contents of this research report.

Intermarket Securities Limited (IMS) is the employer of the research analyst(s) responsible for the content of this report and research analysts preparing this report are resident outside the U.S. and are not associated persons of any U.S. regulated broker-dealer. The analyst whose name appears in this research report is not registered or qualified as a research analyst with the Financial Industry Regulatory Authority ("FINRA") and, therefore, may not be subject to applicable restrictions under FINRA Rules on communications with a subject company, public appearances and trading securities held by a research analyst account.

None of the materials provided in this report may be used, reproduced, or transmitted, in any form or by any means, electronic or mechanical, including recording or the use of any information storage and retrieval system, without written permission.

Disclaimers

Investing in any non-U.S. securities or related financial instruments (including ADRs) discussed in this report may present certain risks. The securities of non-U.S. issuers may not be registered with, or be subject to the regulations of, the U.S. Securities and Exchange Commission. Information on such non-U.S. securities or related financial instruments may be limited. Foreign companies may not be subject to audit and reporting standards and regulatory requirements comparable to those in effect within the United States. The value of any investment or income from any securities or related financial instruments discussed in this report denominated in a currency other than U.S. dollars is subject to exchange rate fluctuations that may have a positive or adverse effect on the value of or income from such securities or related financial instruments.

Frontier and Emerging Market laws and regulations governing investments in securities markets may not be sufficiently developed or may be subject to inconsistent or arbitrary interpretation or application. Frontier and Emerging Market securities are often not issued in physical form and registration of ownership may not be subject to a centralized system. Registration of ownership of certain types of securities may not be subject to standardized procedures and may even be effected on an ad hoc basis. The value of investments in Frontier and Emerging Market securities may also be affected by fluctuations in available currency rates and exchange control regulations. Not all of these or other risks associated with the relevant company, market or instrument which are the subject matter of the report are necessarily considered.

US Distribution

This Report is considered independent third-party research and was prepared by **Intermarket Securities Limited (FBD)**, with headquarters in **Pakistan**. The distribution of this Research is provided pursuant to the exemption under Rule 15a-6(a)(2) and is only intended for an audience of Major U.S. Institutional Investors (MUSIIs) as defined by Rule 15a-6(b)(4). This research is not a product of **StoneX Financial Inc.**. **Intermarket Securities Limited** has sole control over the contents of this research report. **StoneX Financial Inc.** does not exercise any control over the contents of, or the views expressed in, any research reports prepared by **Intermarket Securities Limited** and under Rule 15a-6(a)(3), any U.S. recipient of this research report wishing to effect any transaction to buy or sell securities or related financial instruments based on the information provided in this research report should do so only through **StoneX Financial Inc.** For any information, please contact Gene Turok. Under no circumstances should any U.S. recipient of this research report effect any transaction to buy or sell securities or related financial instruments through **Intermarket Securities Limited.**

Intermarket Securities Limited (IMS) is not registered as a broker-dealer in the United States and, therefore, is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. This research report is provided for distribution to "major U.S. institutional investors" and other "U.S. institutional investors" in reliance on the exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act").

Distribution outside US

This report is not intended for distribution to the public and may not be reproduced, redistributed or published, in whole or in part, for any purpose without the written permission of Tellimer. Tellimer shall accept no liability whatsoever for the actions of third parties in this respect. This report is for distribution only under such circumstances as may be permitted by applicable law.

This report may not be used to create any financial instruments or products or any indices. Neither Tellimer, nor its members, directors, representatives, or employees accept any liability for any direct or consequential loss or damage arising out of the use of all or any part of the information herein.

United Kingdom: Distributed by Exotix Partners LLP only to Eligible Counterparties or Professional Clients (as defined in the FCA Handbook). The information herein does not apply to, and should not be relied upon by, Retail Clients (as defined in the FCA Handbook); neither the FCA's protection rules nor compensation scheme may be applied.

UAE: Distributed in the Dubai International Financial Centre by Exotix Partners LLP (Dubai) which is regulated by the Dubai Financial Services Authority ("DFSA"). Material is intended only for persons who meet the criteria for Professional Clients under the Rules of the DFSA and no other person should act upon it.

Other distribution: The distribution of this report in other jurisdictions may be restricted by law and persons into whose possession this document comes should inform themselves about, and observe, any such restriction