FOREIGN PORTFOLIO INVESTMENT IN PAKISTAN DURING THE COVID-19 OUTBREAK

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Hot money was recently the talk of town in the investment community. Its inflow warded pressures off the nominal exchange rate during the last six months. Foreign investors were lured by high interest rates on Pakistan's T-Bills and PIBs in an environment when globally more than 15 trillion dollars of debt had negative yields. Governments of some European countries, e.g. Germany, raised huge sums in negative yielding debt. In this environment, double-digit nominal returns on Pakistan's government securities were nothing short of a golden goose to chase after for fixed income investors. The State Bank's policy of keeping discount rate relatively stable by cutting it by only 75 basis points in the recent monetary policy intervention has also criticized in business circles as it favors hot money over local businesses financing concerns. However, the black swan event of the COVID 19 pandemic has put a strain on that strategy. Pakistan reported its first case of COVID 19 on 26 of February. Prior to that date, foreign investors were pouring in money in fixed income securities, raising their market value from Rs 276 billion on January 10th to Rs 527 billion on 21st February. The market values of those securities plunged to Rs 500 billion on February 28h and continued that trend to reach at Rs 337 billion on 13 March. Equity securities held by foreigners have also consistently lost market value on the back of slump in their share prices as shown in the graph below.

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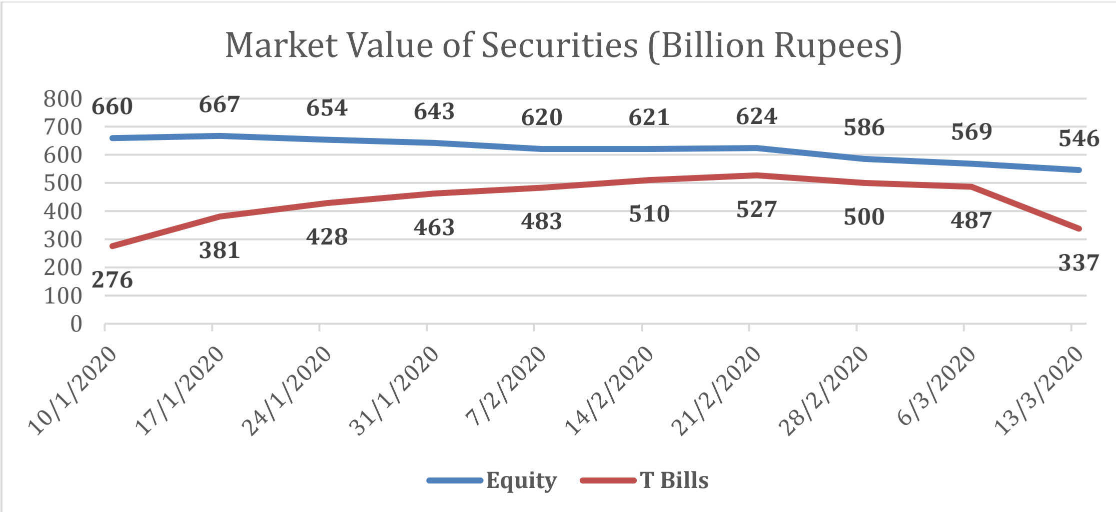

Figure 1

Source: State Bank of Pakistan: Special Convertible Rupee Account Dataset

Apart from the decline in the market value due to plunging prices, foreigners have also reduced their stakes in Pakistan's securities, as they have in many other countries. Sell off pressure was observed during the past three weeks (28th Feb to 13th March 2020) as cautious foreigners offloaded more than Rs 200 billion of securities. The trend exacerbated during March and is expected to continue in a couple of weeks post March 13h as well, specifically for equity securities as KSE-100 index has been in a free fall for a couple of days after March 13. This decline is in sharp contrast to the increase in foreign stakes observed before February 26. Thus, outbreak of COVID 19 in Pakistan can be characterized as an inflection point in this analysis. In addition to this entire sell off pressure, foreign investors have also increased their remittances from those sale proceeds to their respective countries. However, going forward, it is expected that dividend repatriation will ease off, as oil and gas exploration companies are expected to post lower profits on the back of lower international oil prices. Lower dividend repatriation will imply lower outward remittances. Weekly details are given in figures below.

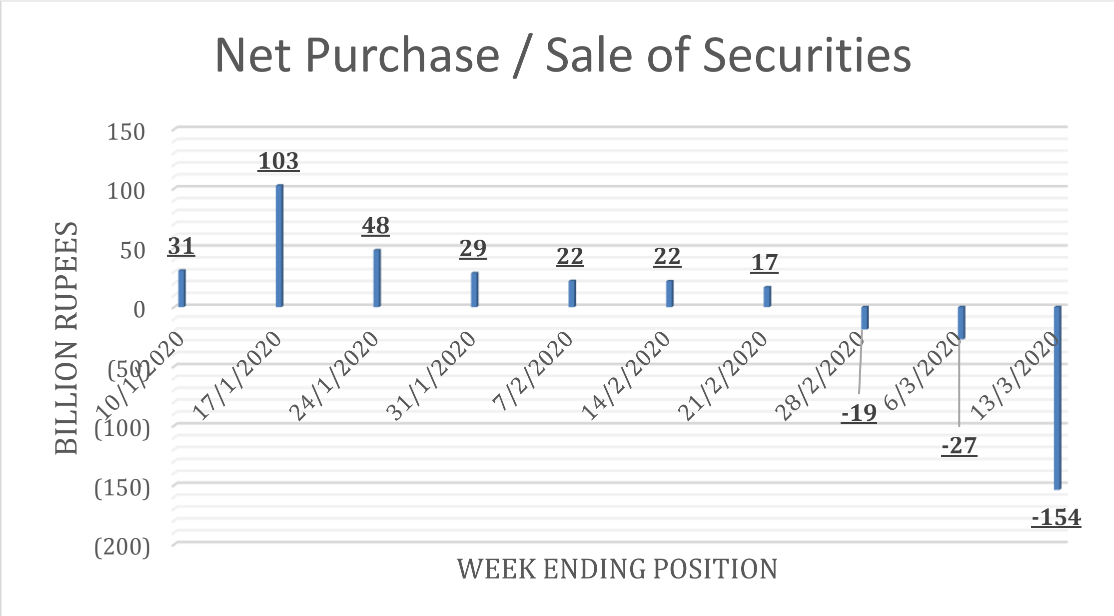

Figure 2

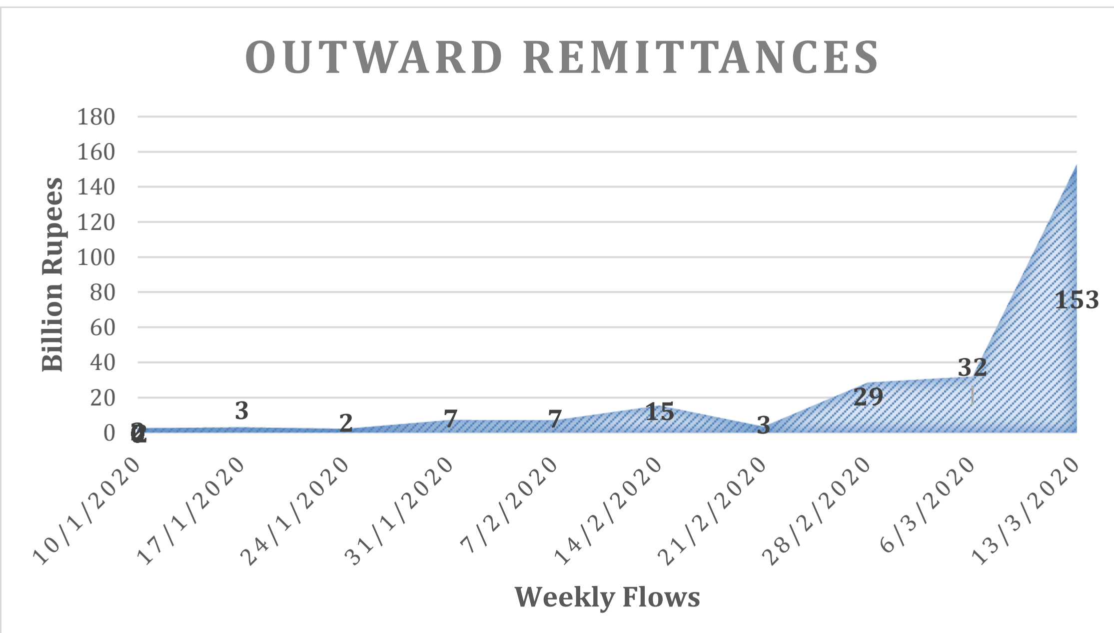

Figure 3

Source: State Bank of Pakistan: Special Convertible Rupee Account Dataset

In my opinion, this entire slump in market values and continuous offloading by foreign investors will not persist longer and we will be back to normal after few months. This sentiment is slightly captured by the following excerpt from Principles of Political Economy (1848) by John Stuart Mill.

"*What has so often excited wonder, is the great rapidity with which countries recover from a state of devastation, the disappearance in a short time, of all traces of mischief done by earthquakes, floods, hurricanes, and the ravages of war. An enemy lays waste a country by fire and sword, and destroys or carries away nearly all the movable wealth existing in it: all the inhabitants are ruined, and yet in a few years after, everything is much as it was before*."