Pakistan


- Pakistan, a CRT-5 country, has a high level of economic risk and very high levels of political and financial system risk. A.M. Best considers the five countries evaluated in South Central Asia to be either a CRT-4 country (India and Sri Lanka) or a CRT-5 country (Bhutan, Nepal and Pakistan).

- Pakistan is a net importer of oil and has benefited from the lower commodity prices in recent years. Weaker growth in the EU region and China, however, will be a headwind near-term. Gross domestic product (GDP) growth is projected at 4.5% for 2016, with growth ranging between 4.5% and 5.5% over the medium term.

- Inflation has moderated from a recent high of 19.6% in 2009. In 2016, inflation is forecasted at 3.3% and is expected to increase slightly over the next few years to approximately 5.0%.
Regional Summary: South Central Asia

- The region of South Central Asia comprises the countries south of the Himalayans.

- Economic activity in the region is expected to increase led by India, the region’s largest economy. Lower oil prices and foreign direct investment were the main catalysts for past growth. Future growth in the region will increasingly depend on export performance and strong investment.

- Risks facing the region include vulnerabilities relating to global economic conditions, including the effects of monetary policy tightening in the U.S. and the potential for stagnation in Europe. Domestic developments, such as political turmoil and non-sustainable fiscal policies, could undermine stability and investor confidence.

- As labor costs increase in other Asian markets, South Central Asia has the opportunity to increase its manufacturing activity. However, the region will need to boost competitiveness by improving infrastructure, reducing bureaucracy and limiting corruption.

Economic Risk: High

- Pakistan's economy is dominated by the services industry, which represents 60% of the country’s GDP. Recently, agricultural output has been adversely affected by extreme weather conditions.

- Energy and water shortages remain a key bottleneck for improving economic growth, particularly in the manufacturing sector. Many businesses and households are without power for up to twelve hours each day.

- As U.S. aid to Pakistan has fallen, China has emerged as an important source of funding for the country. China has agreed to fund rail and energy infrastructure projects, such as the China-Pakistan economic corridor.

- The operating environment keeps Pakistan’s economic growth below its potential.
Political Risk: Very High

- Political instability has been somewhat reduced as a result of improving relations between the military chiefs and the civil government. However, there are points of contention that remain between the two groups that could prove to be volatile.

- The government has been criticized for power shortages. The ruling party’s political future could be heavily dependent upon its ability to reduce the shortages before the next election in 2018.

- Terrorism, domestic conflicts and the potential for social unrest continue to be significant security risks. Security risks limit institutional and governance effectiveness.

- Massive tax avoidance is one of the main challenges for increasing fiscal revenue and reducing Pakistan's reliance upon foreign aid. According to the OECD, approximately 1.0% of Pakistan's population pays income tax.

- Politics in the country is marked by high levels of corruption and charges of nepotism.

Financial System Risk: Very High

- The insurance industry is regulated by the Insurance Division of the Securities and Exchange Commission of Pakistan.

- While improving over the last few years, foreign exchange reserves continue to be at a low level. The country still depends on support from the International Monetary Fund (IMF). The current 3-year IMF program is set to expire in September 2016.

- Enhanced central bank independence remains an important goal toward achieving an improved monetary framework. Initiatives to combat money laundering and terrorism financing could be further improved.

- Due to low inflation rates, the central bank was able to reduce its policy interest rate to its lowest level in over forty years.
# Guide to Best's Country Risk Tiers

A.M. Best defines country risk as the risk that country-specific factors could adversely affect the claims-paying ability of an insurer. Country risk is evaluated and factored into all Best's Credit Ratings. Countries are placed into one of five tiers, ranging from “CRT-1” (Country Risk Tier 1), denoting a stable environment with the least amount of risk, to “CRT-5” (Country Risk Tier 5) for countries that pose the most risk and, therefore, the greatest challenge to an insurer’s financial stability, strength and performance.

A.M. Best’s Country Risk Tiers are not credit ratings and are not directly comparable to a sovereign debt rating, which evaluates the ability and willingness of a government to service its debt obligations.

## Country Risk Tiers

<table>
<thead>
<tr>
<th>Country Risk Tier</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>CRT-1</td>
<td>Predictable and transparent legal environment, legal system and business infrastructure; sophisticated financial system regulation with deep capital markets; mature insurance industry framework.</td>
</tr>
<tr>
<td>CRT-2</td>
<td>Predictable and transparent legal environment, legal system and business infrastructure; sufficient financial system regulation; mature insurance industry framework.</td>
</tr>
<tr>
<td>CRT-3</td>
<td>Developing legal environment, legal system and business environment with developing capital markets; developing insurance regulatory structure.</td>
</tr>
<tr>
<td>CRT-4</td>
<td>Relatively unpredictable and nontransparent political, legal and business environment with underdeveloped capital markets; partially inadequate regulatory structure.</td>
</tr>
<tr>
<td>CRT-5</td>
<td>Unpredictable and opaque political, legal and business environment with limited or nonexistent capital markets; low human development and social instability; nascent insurance industry.</td>
</tr>
</tbody>
</table>

## Country Risk Reports

A.M. Best Country Risk Reports are designed to provide a brief, high-level explanation of some of the key factors that determine a country’s Country Risk Tier assignment. It is not intended to summarize A.M. Best’s opinion on any particular insurance market or the prospects for that market.

## Categories of Risk

Country Risk Reports provide scores for three categories of risk for each country. These scores are (1) Very Low; (2) Low; (3) Moderate; (4) High and (5) Very High.

### Category of Risk | Definition
--- | ---
Economic Risk | The likelihood that fundamental weaknesses in a country's economy will cause adverse developments for an insurer. A.M. Best's assessment of economic risk evaluates the state of the domestic economy, government finances and international transactions, as well as prospects for growth and stability.
Political Risk | The likelihood that government or bureaucratic inefficiencies, societal tensions, inadequate legal system or international tensions will cause adverse developments for an insurer. Political risk comprises the stability of the government and society, the effectiveness of international diplomatic relationships, the reliability and integrity of the legal system and of the business infrastructure, the efficiency of the government bureaucracy, and the appropriateness and effectiveness of the government’s economic policies.
Financial System Risk | Financial system risk (which includes both insurance and non-insurance financial system risk) is the risk that financial volatility may erupt due to inadequate reporting standards, weak banking system or asset markets, and/or poor regulatory structure. In addition, it includes an evaluation of whether the insurance industry’s level of development and public awareness, transparent and effective regulation and reporting standards, and sophisticated regulatory body will contribute to a volatile financial system and compromise the ability of an insurer to pay claims.

## Political Risk Summary

To provide additional detail on the political risk in a given domicile the Country Risk Reports include the Political Risk Summary. The Political Risk Summary is a radar chart that displays scores for nine different aspects of political risk scored on a scale of one to five with one being the least amount of risk and five being the highest amount of risk.

### Category | Definition
--- | ---
International Transactions Policy | Measures the effectiveness of the exchange rate regime and currency management.
Monetary Policy | Measures the ability of a country to effectively implement monetary policy.
Fiscal Policy | Measures the ability of a country to effectively implement fiscal policy.
Business Environment | Measures the overall quality of the business environment and ease of doing business.
Labor Flexibility | Measures the flexibility of the labor market, including the company’s ability to hire and fire employees.
Government Stability | Measures the degree of stability in a government.
Social Stability | Measures the degree of social stability, including human development and political rights.
Regional Stability | Measures the degree of stability in the region.
Legal System | Measures the transparency and level of corruption in the legal system.

## Country Risk Tier Disclosure

A Country Risk Tier (CRT) is not a credit rating, rather it represents a component of A.M. Best’s Credit Rating Methodology that is applied to all insurers. A CRT is not a recommendation to purchase, hold or terminate any security, insurance policy, contract or any other financial obligation issued by a government, an insurer or other rated issuer, nor does it address the suitability of any particular policy, contract or other financial obligation for a specific purpose or purchaser.

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