

Stock Market Review

Local equities rebounded modestly during December with the benchmark KSE 100 index rising by around 1.7%. Defying improving macroeconomic prospects, the stock market closed CY15 with lackluster gains of 2.1% amid heightened volatility. On the positive side, inflation hit a multiyear low primarily due to collapsing commodity prices, allowing the central bank to cut discount rate by 300 bps during CY15; and FX reserves reached comfortable level of 4 months imports cover. Fiscal deficit is expected to come in at 5.5% amid some new taxation measures and cut in energy subsidies; and GDP growth is likely to touch 4.5% helped by lower input cost and some improvement in energy availability. We attribute the dismal performance of the stock market during CY15 to foreign selling and subdued corporate earnings growth led by Oil & Gas and Banking sectors. Concerns on the global economic growth, uncertainty linked to divergent monetary policy actions in the advanced economies, rout in the emerging market currencies, and collapsing commodity prices were also a drag on the performance of the local bourse. Similarly, growing geopolitical risks from turmoil in Middle East linked to war in Yemen and Syria; tragic terrorist attacks in Paris; China's military assertiveness in the South China Sea created bouts of volatility in the global equities, commodities, currencies and bond markets. We believe that for local equities, unabated foreign selling of US Dollar 315 million remains the swing factor for this anemic performance during CY15.

During CY15, Automobiles Assemblers, Cement, Engineering, Fertilizer, Pharmaceuticals, Power Generation & Distribution sectors performed better than the market while, Oil & Gas Exploration, Banking, Paper & Board, and Textile Composite sectors lagged behind. Automobile sector depicted strong performance on earnings growth amid healthy volumetric growth and robust profit margin. Healthy domestic dispatches and steady profit margins contributed to the robust performance of the Cement sector. Collapsing global oil prices amid supply glut triggered sell-off in Oil & Gas Exploration sector. Paltry yield on the alternative fixed income avenues resulted in the superior performance of Power Generation & Distribution sector. Strong run continued in the pharmaceutical sector on the back of robust earnings announcements amid healthy top-line growth. Banking stocks remained under pressure amid series of discount rates cuts and some other policy measures from the SBP, as well as some adverse taxation measures announced in the budget, that acted as a drag on the profitability.

Going forward, we hold a sanguine outlook on the stock market driven by relatively attractive valuations; benign near-term inflation and interest rates outlook; comfortable external account position; scarcity of yield on the alternative fixed income avenues; and improving macroeconomic prospects. We have repositioned the portfolios of our equity related funds and advisory portfolios based on our capital market expectations and macroeconomic outlook.

We also acknowledge that volatility may remain elevated in the coming months amid divergent monetary policy and economic environment with spillover on the emerging and low income economies. Moreover, any escalation of geopolitical risks from war ravaged Middle East may create bouts of volatility. To navigate this challenging investment landscape, we recommend investors to keep long-term perspective and resist the urge to head for exit amid heightened volatility. We expect the market to deliver a healthy double digit returns in CY16 driven by around 6% dividend yield; probable rerating of the market amid improving macro economy; and some capital gains.

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SBP pursued aggressively accommodative monetary policy during CY15, slashing Discount Rate by 300 bps to 6.5% from 9.5%. Accordingly, the yield on T-bills decline by around 300 bps whereas, yield on PIBs saw a decline of 130-270 bps. Key underpinning of this monetary policy action was falling inflation; improving FX reserves position; largely contained fiscal position helped by new taxation measures and reduction in subsidy burden. Inflation as measured by the CPI clocked in 3.2% for December compared to 4.3% for the corresponding period last year. During December 2015, government took new tax measures of Rs 40 billion to buttress the revenue collection. SBP OMO injection closed the month at Rs.1.3 trillion after hitting Rs 1.4 trillion during the month. We expect inflation to gradually pick-up to 6% during CY16 due to reversal of base effect, new tax measures, and partial recovery in global commodities. Resultantly, we see around 100 bps increase in the sovereign yields during CY16.

In the two T-Bills auctions during the month, MoF accepted Rs. 123 billion (realized amount) against the target of Rs.275 billion and maturity of Rs.250 billion at cut-off annualized yields of 6.34%, 6.36% and 6.39% for 3, 6 and 12 months tenors respectively. Last T-Bills auctions bid pattern skewed towards the 3 and 6 months as compared to 12 months. In PIB auction held on 16th December 2015, an amount of Rs.36 billion was accepted against the target of Rs.50 billion and participation of Rs.144 billion. The cut-off yield remained at 6.99%, 7.99% and 9.1% for 3 year, 5 year and 10 year respectively. The bid pattern witnessed a major shift towards 3 year tenor followed by 5 and 10 year tenors respectively. On 15th December MoF also announced GOP Ijara Sukuk Auction and accepted Rs.118 billion against the target of Rs.100 billion at a profit rate of 6-Month T-bill minus 50bps.

We have adjusted the portfolio of our money market and income funds based on our capital market expectations. We are closely monitoring the developments in the capital markets and will rebalance the portfolio accordingly.

Our Contacts

Contact our Investment Consultant for free Investment advice

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