NBP Fullerton Asset Management Ltd.
A Subsidiary of National Bank of Pakistan

Capital Markets Review

May 2015

Stock Market Review

The stock market depicted lackluster performance during May ahead of the federal budget 2015-16 with the benchmark KSE 100 index declining by around 2%, taking the CY15 gains to just 3%. The investment landscape for equities was marked by competing factors. On the positive side, accommodative monetary policy stance being pursued by the SBP with the 100 bps reduction in discount rate in the last monetary policy announcement; attractive stock market valuations as captured in 9 times P/E multiples based on forward earnings; and improving macroeconomic outlook as reflected by anchored inflation, largely contained fiscal deficit, rising external reserves position, and uptick in growth rate are supportive of equities. Another underpinning for the stock market rally is falling yields on sovereign securities with 3,5, and 10 years PIBs yielding 7.5%, 8.1% and 9.2% respectively, making the yield plays specially attractive. On the contrary, uncertainty related to the upcoming federal budget and news flows related to judicial inquiry into alleged irregularities/rigging in the 2013 national election weighed on the investors' sentiments in the market. Foreigners were net buyers during the month with net inflows of US 15$ million versus US 34 $ million recorded during the previous month.

Among the out-performers were Automobile Assemblers, Engineering, Oil & Gas Marketing, Paper & Board and Pharmaceuticals sectors while Cement, Chemicals, Commercial banks and Fertilizer sectors lagged the market. Expectations of strong earnings driven by healthy volumetric growth coupled with robust margins supported the strong rally in automobile assembler sector. Cement stocks took a breather after strong run during the last few months. Uncertainty triggered by the imposition of Gas Infrastructure Development Cess (GIDC) on fertilizer plants kept the investors on the sidelines. Above expected reduction in policy rate coupled with reduction of interest rate corridor by 50 bps and news of increase in taxes on capital gains and dividend income weighed on the earnings outlook of the banks.

We reiterate our sanguine view on the stock market based on a combination of easy monetary conditions led by benign inflation, attractive market valuations, decent corporate earnings growth, ultra low yields on alternative fixed income avenues and stabilizing political situation. However, we think that after a long period of calm with solid gains, stock market returns will now be accompanied by bouts of volatility driven by external developments such as exit from an accommodative monetary policy in the US, evolving geo-politcial situation in the Middle-East and commodity price movements. As per our estimates, currently the market is trading at around 9 times estimated earnings and is offering around 6% dividend yield.

We are closely monitoring the developments in the capital markets and will rebalance the portfolios of our equity related funds and SMAs accordingly.

Money Market Review

The State Bank of Pakistan (SBP) in its recent Monetary Policy Review Meeting in May reduced discount rate by 100 bps bringing it to a 42 years low of 7%. SBP also introduced a target rate set 50 basis points below the ceiling rate. SBP will ensure that the overnight rate remains close to this target rate. Furthermore, width of the interest rate corridor has been reduced by 50 basis points from 250 to 200 basis points. Consequently, the floor rate is set at 5%. According to SBP i) improving external account position; ii) benign inflation reading and anchored inflation outlook; and iii) continued increase in foreign exchange were key drivers for the expansionary monetary policy decision.

Turning to the fixed income market, the treasury bills yields further declined by around 25-30 bps following the monetary policy announcement by the SBP. In the two T-Bills auctions during the month, MoF accepted Rs. 211 billion (realized amount) against the target of Rs.175 billion and maturity of Rs.459 billion. The cut-off annualized yields for the last T-Bill auction were noted at 6.62%, 6.65% and 6.75% for 3, 6 and 12 month tenors respectively. Last T-Bills auction bid pattern skewed towards 3 months as compared to 6 and 12 months. In the PIB auction during the month, an amount of Rs.64 billion was accepted at a cut-off yield of 7.55%, 8.1% and 9.25% in 3 year, 5 year and 10 year respectively (realized amount) against the target of Rs.50 billion and total participation of Rs.118 billion. No bids were received in 20 year tenors. The bid pattern witnessed a major shift towards 5 year tenor followed by 3 and 10 year tenors respectively.

We have adjusted the portfolio of our money market and income funds based on capital market expectations and 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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