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

Capital Markets Review

May 2016

Stock Market Review

Defying the upcoming budget related uncertainties; during May the local equities continued with their positive momentum on the back of Pakistan's probable entry into the widely tracked MSCI Emerging Market Index. Moreover, global concerns emanating from fears of hard landing in China & associated abrupt currency devaluation; plunging global commodity prices and associated disruptive devaluation of Emerging Market currencies; divergent monetary policy by the systematically important central banks and risks of competitive currency devaluations, eased off substantially. The foreign selling which we believe is the swing factor for the lackluster performance of the market since beginning of 2015 has petered out during the month with net foreign buying of around US $ 4 million recorded in May 2016. We see large foreign inflows into the local equities post their reclassification into MSCI Emerging Market Index on the back of improving macroeconomic prospects, reasonable valuations and improving security situation. Federal budget FY2016-17 was unveiled by the government with a focus on exports and agriculture. From an overall stock market perspective, the budget is neutral to positive, offering significant relief to the struggling Fertilizer and Textile sectors. The benchmark KSE 100 index increased by 3.9% during the month in review, taking the FY16 gains to 4.8%.

Turning to the Sector-wise performance, Oil & Gas Exploration, Chemicals, Engineering, Oil & Gas Marketing, and Power Generation & Distribution sectors out-performed the market while, Cement, Automobile Assemblers, Commercial Banks, and Paper & Board sectors were laggard. Oil & Gas Exploration sector exhibited solid performance amid strong rebound in the global oil prices due to supply side adjustments. The high yielding Power sector drew investors' interest following a 25 bps cut in the policy rate by the SBP in its recently announced monetary policy announcement. The news of increase in the FED in the Federal Budget FY17 resulted in the lagged performance of the Cement sector. Banking stocks remained out of favour on the back of increasing pressure on the already shrinking Net Interest Margins (NIMs). Strengthening Japanese yen with negative impact on the profit margins kept investors from the Automobile & Assembler sector.

Going forward, we maintain our sanguine outlook for equities driven by attractive valuations as captured in 8.6 times forward Price to Earnings ratio (PE); benign near-term inflation and interest rate outlook; a comfortable external account position; improving macroeconomic prospects; and expectation of large portfolio inflows post PSX's likely entry into MSCI EM Index. However, we acknowledge that volatility may increase from the current levels amid global policy mistake and escalation of domestic political tension linked to investigations on Panama Leaks.

Money Market Review

Inflation as measured by CPI for May 2016 clocked in at 3.2% on a year on year basis helped by lower readings for the food component, as compared to 4.2% the previous month. Against the market expectation, State Bank of Pakistan (SBP) reduced policy rate by 25 basis points from 6% to 5.75% in its bi-monthly monetary policy review meeting in May 2016. SBP in its statement highlighted improvement in the macroeconomic conditions, better law and order situation, and positive future prospects of Foreign Direct Investment under China Pakistan Economic Corridor. However, SBP expressed concerns on the inflation due to expectation of increase in commodity prices. The central bank also highlighted the downside risks to the external account due to declining exports receipts. During the month, PKRV yields remained stable prior to monetary policy announcement, however, yields responded accordingly post policy rate decline of 25 bps. As we see it, the yield curve may remain under pressure due to a huge Rs. 1.35 trillion maturity of PIBs in July. Foreign exchange reserves increased above USD21 billion during the month.

During the month SBP held two T-Bill auctions with a combined target of Rs. 300 billion and a maturity of Rs. 243 billion. In the first T-Bill auction, Ministry of Finance (MoF) accepted Rs. 246 billion against the target of Rs. 200 billion and maturity of Rs. 176 billion at a cut-off yield of 6.26%, 6.27% and 6.28% for the 3 month, 6 month and 12 month tenors respectively. Bid pattern remained skewed towards 3 month as compared to 6 and 12 month. Moreover, in the second T-Bill auction, Ministry of Finance (MoF) accepted Rs. 278 billion against the target of Rs. 100 billion and maturity of Rs. 67 billion. The cut off yields responded to the policy rate cut and were noted at 5.99%, 6.01% and 6.03% for the 3 month, 6 month and 12 month tenors respectively. Bid pattern shifted towards 6 months as compared to 3 and 12 months. PIB auction on 18-May-2016 with a target of Rs. 50 billion and maturity of Rs. 37 billion was scrapped.

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 portfolios accordingly.

Our Contacts

Contact our Investment Consultant for free Investment advice

Call 0800-20002 | UAN 111-111-632 | sms NAFA INVEST to 8080 | www.nafafunds.com | info@nafafunds.com