Capital Market Review

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

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Stock Market Review

Helped by a decent net foreign buying to the tune of USD28 million, highest monthly net inflow since Jun-16, the local bourses (KSE-100 Index) managed to close the month with a gain of 2.9% led by Fertilizer and Oil & Gas Exploration sector after a hefty correction of around 10.4% during the previous month. As we see it, key factors that contributed to the recent subdued performance of the stock market are domestic political fluidity, increasing concerns on the economy driven mainly by deteriorating Balance of Payment (BoP) position, and potential threat of tough stance by the US toward Pakistan such as military conflict or economic sanctions as signaled in the US Afghan policy. Investors were also unnerved by the anti-establishment political rhetoric from the ousted PM and the ruling PML-N government as this may lead to institutional backlash that would fuel political uncertainty and exacerbate policy dysfunction. Uncertain fate of the Finance Minister facing corruption charges in the accountability court has stalled much needed policy measures to address the pressing risks to the economy. Investors also worry that policy inaction may derail the nascent economic recovery and contaminate corporate fundamentals. To dispel these concerns and restore confidence, market participants require not just talks by government officials but concrete policy actions that aim to increase exports & curtail non-essential imports to address the growing trade deficit that is the root cause of deteriorating BoP situation. We believe that current stock market valuations largely reflect this negativity and any positive developments would be cheered by the market. In our base case scenario, we expect political uncertainty to remain contained, some progress on the policy measure to address the BoP situation, and benign near-term inflation and interest rate outlook.

During the month, Oil & Gas Exploration, and Fertilizer sectors performed better than the market while Cement, Oil & Gas Marketing, Engineering, Automobile Assemblers and Textile Composite sectors lagged behind. Recovery in the global crude oil prices, expectation of some currency devaluation, and reasonable valuations led to healthy performance of the Oil & Gas Exploration sector. After sizable under-performance, the Fertilizer sector depicted strong rebound amid sharp recovery in global urea prices from very low levels. Below expected corporate results and continued delay in export package led to lagged performance of the Textile sector. Oil & Gas Marketing sector underperformed led by Gas Distribution companies. Contraction in profit margins due to increase in input costs amid rising coal prices and pressure on cement prices despite healthy volumetric growth weighed on performance of the Cement sector. Sell-offs in the couple of stocks due to one-off events resulted in the subdued performance of the Banking sector.

After the recent correction, the stock market valuations have become quite attractive as captured in P/E ratio of 9.5. In our view, the prevailing investment backdrop characterized by attractive stock market valuations from the historical perspective as well as regional comparison; benign inflation & interest rate environment and supportive monetary conditions; solid corporate fundamentals with strong balance sheet and healthy earnings growth; ameliorating law and order situation and improving power availability helping economic activity are supportive for equities. While domestic political uncertainty may send jitters temporarily, market would take cue from any credible and decisive policy measures to address the deteriorating trade deficit and BoP position. Taken together, we reiterate our view that the market holds potential to deliver a healthy return over the next 12 months.

Money Market Review

After recording 3.41% YoY in August 2017, inflation as measured by the CPI for September 2017 marginally inched up to 3.9%. State Bank of Pakistan (SBP) in its bi-monthly Monetary Policy Statement maintained policy rate at 5.75%. The central bank has expressed optimism over the economic growth amid strong investment activity and improving agriculture sector growth, while cited potential risks to BoP situation due to widening trade deficit and emphasized the need for policy measures in this regard. On inflation, the central bank mentioned pick up in core inflation (Non Food Non Energy) but expects that better supply situation and contained global prices are likely to keep inflation below the target level of 6% for FY18. We see CPI inflation to gradually pick up from the current benign levels driven by partial recovery in global oil prices, measured PKR depreciation, and demand pressures. Accordingly, in our base case scenario, we expect around 100 bps increase in interest rates during CY18.

During the month of September, SBP held two T-Bill auctions with a combined target of Rs. 1,050 billion against a maturity of Rs. 943 billion. In the first T-Bill auction, an amount of Rs. 372 billion was realized against the target of Rs. 500 billion and maturity of Rs. 443 billion at a cut-off yield of 5.99%, 6.01% and 6.04% for 03, 06 and 12 months tenors, respectively. In the second T-Bill auction, Ministry of Finance (MoF) realized Rs. 472 billion against the target of Rs. 550 billion and maturity of Rs. 500 billion wherein cut-off yields for 03 and 06 months tenors were maintained while cut-off yield for 12 months tenor decreased by 1 bps to 6.03%. PIB auction was rejected as bids worth Rs. 5.8 billion were received against the target of Rs. 100 billion and maturity of Rs. 47 billion.

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