

August 2011

Stock Market Review

The stock market plunged during the month of August on very thin volumes. Key factors responsible for this downfall are US rating downgrade and associated global equity sell-off, severe energy crisis, mounting energy related circular debt; and worsening law and order situation. Local investors were net sellers in anticipation of heavy foreign selling. Lower than expected results announcements by the key companies belonging to different sectors also weakened the investors' confidence in the market. Currently stock market is trading at a forward PE multiple of 6.6 times. Corporate earnings are expected to grow at around 20% in the next four quarters. The month started with KSE-30 Index at 11,560 levels and lost around 10.5% to touch a low of 10,351 levels on August 19. Overall, during the month the KSE-30 Index lost around 9%.

State Bank of Pakistan unexpectedly decreased Policy rate by 50 basis points to 13.5% from 14% in its Monetary Policy announcement on July 30, 2011. Key factors cited were improvement in external accounts position and inflation outlook; and to arrest decline in Private sector investment. Foreign investors were net sellers in the market during the month with total outflow recorded at around US\$ 11.6 million. Trading volume remained stubbornly low during the month. Average Daily Trading volume was recorded at 49 million shares versus 58 million shares during the previous month.

During the month, Construction and Materials; and Electricity sectors out-performed the market while, Oil and Gas, Banking, Chemicals, and Personal Goods sectors lagged the market. Below expectations results announcements by the key oil exploration companies resulted in the under-performance of the Oil and Gas Exploration subsector. Approval of increase in the Oil Marketing Companies margin restored confidence in OMC sub-sector. Selected companies in the Fertilizer sub-sector under-performed the market due to chronic Gas curtailment while, other companies with healthy results announcements and payouts performed better than the market. Better than expected corporate results announcements and healthy profit margins attracted investors to take positions in key companies of Cement sub-sector. Investors' preference for high dividend payouts resulted in the out-performance of the Power sub-sector.

Going forward, key drivers of the stock market will be: Foreign Portfolio Investment (FPI) activity; development on domestic political situation; Bilateral and multilateral financial inflows; and inflation and interest rates outlook.

Fixed Income Review

The money market remained very tight during the month with overnight repo rates hovering just below the revised Discount Rate of 13.5%. This was because of banks preference for holding longer maturity Government Securities and usual Eid related outflows from banking system. The last T-Bills auctions' bid pattern of August 2011 showed almost entire participation in one year T-Bill, while negligible amounts in six months and three months. The 10-year PIB traded as low as 13.10% p.a. In the two T-bills auctions of August, SBP cumulatively accepted Rs. 300 billion against the target of Rs. 260 billion. The cut off yields (p.a.) for both T-Bills auctions were noted at 13.07%, 13.28% and 13.38% for the 3 months, 6 months and 12 months maturities respectively.

On the corporate debt sphere, market volumes reported by MUFAP remained thin in August as well. Total traded value reported by MUFAP for August 2011 was Rs 562 mln, as against a value of Rs. 687 mln in July 2011. Banking and Chemical sectors bonds accounted for 70.8% and 28.5% of the traded value respectively.

For July 2011 YoY Inflation (CPI) was 13.8%, while month-on-month inflation in July 2011 was 1.8%. Government borrowing from the scheduled banks is consistently increasing to finance fiscal deficit. In first fifty days of the current fiscal year, net Government borrowing from scheduled banks has risen by 9% or Rs 126 billion. Rising workers' remittances continue to provide a breather. However, there are concerns on the sustainability of this trend.

Continued market risk aversion has led NAFA Government Securities

Liquid Fund maintain Rs. 12 bln mark, which makes it the only 'AAA(f)' rated fund greater than Rs 10 billion in size. The last two funds in fixed income category launched by NAFA namely NAFA Riba Free Savings Fund and NAFA Savings Plus Fund, are also performing well posting double digit returns. In the current interest rate environment as mentioned above, the returns of these funds are expected to remain attractive, considering their very low credit risk profile. NAFA's management has started monthly distributions (dividends) in these three funds. For investors with long investment horizon of three or more years, our other income funds offer very attractive yields as TFC prices are at significant discount.

Month-on-Month Consumer Price Index (CPI inflation)

