Capital Markets Review

August 2013

Stock Market Review

The stock market swung between gains and losses during the first half of the month and retreated during the latter half driven by concerns regarding possible hike in interest rates in the upcoming monetary policy and liquidity tightening under the upcoming IMF program. Sell-off in the global and regional markets amid signals of Quantitative Easing (QE) tapering off by the US Fed and debate on military actions in Syria by the US lead coalition also weighed in on the investors' sentiments. Furthermore, investors' mood dampened due to below expected earnings announcements and payouts by the majority of companies. Trading activity dropped with average daily trading volume recorded at 201 million shares versus 253 million shares during the previous month. Foreign investors were net buyers in the market during the month with net Foreign Portfolio Inflows (FPI) at US $ 26.5 million. Overall, KSE 100 Index declined by 4.9% during August 2013.

Banking, Electricity and Oil & Gas sectors out-performed the market whereas, Construction & Materials, Fixed Line Communication, and Personal Goods sectors under-performed the market. Investors took fresh positions in the Banking sector on the expectations of improvement in the earnings outlook driven by the interest rates hike. Sanguine valuations and healthy payouts resulted in the upbeat performance of the Electricity sector. Talks of rift in cement cartel and lower than expected earnings and payouts resulted in subdued performance of Construction & Material sector.

Stock market is currently trading at an 8.6 times forward earnings as per our estimates. Going forward, announcement of the fresh IMF package, foreign portfolio inflows, developments in Syria, and inflation and interest rates outlook will be the key drivers of the stock market.

Fixed Income Review

As expected, inflationary pressures have stoke up recently with YoY headline inflation as measured by Consumer Price Index (CPI) jumping to 8.55% in August 2013 as compared to 5.9% in June 2013. We expect further pick up in inflation in the coming months led by spike in food prices due to recent floods along with rupee depreciation, upward adjustment in utility prices, and unabated government borrowing to finance fiscal deficit.

SBP is scheduled to announce Monetary Policy on 13 September 2013 wherein market expects increase in the policy rate. Bid pattern of the Treasury Bills in the last auction and increase in cut off yields in last PIB auction corroborates the market view of increase in the Discount Rate.

In the two T-Bills auctions during the month, MoF accepted Rs 229 billion (realized amount) against the target of Rs 500 billion and maturity of Rs 367 billion. The cut- off annualized yields for the last T- Bill auction were noted at around 8.96% and 8.99% for 3 and 6 month tenors, respectively while bids were rejected in 12 month tenor. In PIB auction during the month an amount of Rs. 30 billion was accepted against the target of Rs. 50 billion at a cut-off yield of 11.15%, 11.65% and 11.99% in the 3 year, 5 year and 10 year tenors respectively, whereas no bids were received in the 20-year tenor.

We are keeping short maturities for our money market funds on the expectation of upside risk to the inflation and interest rates. Therefore, increase in the interest rate bodes well for the performance of our money market funds.