July 2013

Stock Market Review

Paring back the losses of the last month, the stock market depicted robust performance during July. The benchmark KSE-100 Index surged by around 11% led by the Banking, Fixed Line Communication and Construction and Material sectors amid expectations of healthy corporate earnings announcements in the ongoing results season, mitigation of downside risk to the external account post Pak - IMF negotiations for fresh IMF package and improvement of liquidity with the resolution of energy related circular debt. However, at the end of the month, a sell-off was witnessed in the market as it started paying attention to negative signals from the bond and forex markets. Trading activity remained healthy with average daily trading volume recorded at 253 million shares. Foreign Portfolio Inflows were recorded at US $ 26.5 million (adjusted for outflows related to KAPCO shares). KSE 100 Index started the month at 21,006 levels and after touching a high of 23,776 levels on July 24, closed July at 23,313.

Banking, Fixed Line Communication and Construction and Material sectors performed better than the market. On the other hand, Oil & Gas, Electricity and Industrial Engineering sectors lagged the market. Outlook of the banking sector improved on expectations of improvement in Net Interest Margins (NIMs) on the back of uptick in interest rates and relaxation in Minimum Deposit Rate (MDR). Investors took fresh positions in the selected telecom giant on the expectations of transfer of real estate properties. Hopes of robust earnings announcement and healthy payouts drove upbeat performance of Construction and Material sector. Electricity sector took a breather following robust performance during the last couple of months.

As per our estimates, the stock market is currently trading at an 8.9 times forward earnings. Going forward, developments on the fresh IMF package, foreign portfolio inflows, announcement/implementation of energy policy and upcoming financial results will be the key drivers of the stock market.

Fixed Income Review

As compared to 5.9% in June 2013, the YoY headline inflation as measured by Consumer Price Index (CPI) increased to 8.3% in July 2013 led by the food component. Expected hike in energy tariffs, rupee weakness, upward adjustment in fuel prices, reversal of base effect and strong broad money growth are likely to further stoke up inflation going forward.

The market witnessed a major shift in the SBP Open Market Operation from injection to mop up due to the large maturities of Treasury Bills as compared to the targets in the month of July and significant increase in direct government borrowing from SBP to resolve the energy sector circular debt. Longer tenor yields surged during the month to the level seen before the last policy rate cut by the central bank. For instance, Yield of 10 year PIB increased to 11.76% at the end of the month compared to 10.93% at the beginning of the month.

In the two T-Bills auctions during the month, MoF accepted Rs 516 billion (realized amount) against the target of Rs 600 billion and maturity of Rs 803 billion. The cut- off annualized yields for the last T- Bill auction were noted at around 8.96%, 8.99% and 8.98% for 3, 6 and 12-month tenors, respectively. T-Bills auction bid pattern depicted major participation in 3 & 6-month tenor, while considerably smaller interest was observed in 12-month tenor. In PIB auction during the month an amount of Rs. 18 billion was accepted against the target of Rs. 50 billion at a cut-off yield of 10.44%, 10.90% and 11.65% in the 3 year, 5 year and 10 year tenors respectively, whereas no bid was 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.