

June 2011

## Stock Market Review

During the month of June, the stock market depicted a dull behavior. Government's political row with a major coalition partner, chronic power and gas shortages, mounting energy related circular debt issues, and subdued Foreign Portfolio Investment (FPI) activity grappled the market. Federal Budget for FY 2011-12 brought no surprise for the majority of the sectors of the economy. Investors remained cautious about the development on the Pak-US relations. Lack of any headway on the stalled IMF tranche under the SBA weakened the investors' confidence in the market. Against the expectations of the market, no relief measures regarding the Capital Gains Tax (CGT) on stocks were announced in the Federal Budget for FY 2011-12. Among other factors, this resulted in abysmally low trading activity in the market. The month started with KSE-30 Index at around 11,762 levels and after touching a low of 11,528 levels on June 20, closed the month at 11,586 levels. Overall, during the month KSE-30 Index decreased by around 1.50%.

Inflation as measured by CPI for the first 11 months of FY 2011 was recorded at 14% compared with 11.6% during the same period last year. The surge in prices of food and energy, notably oil, significantly contributed to this high CPI. However, on the back of the substantial growth in exports and record workers' remittances external accounts showed significant improvements. Foreign Portfolio Investment (FPI) remained sluggish during the month and net foreign portfolio outflow was recorded at US\$ 41.2 million. Trading activity remained thin and Average Daily Traded Volume during the month was recorded at around 75 million shares.

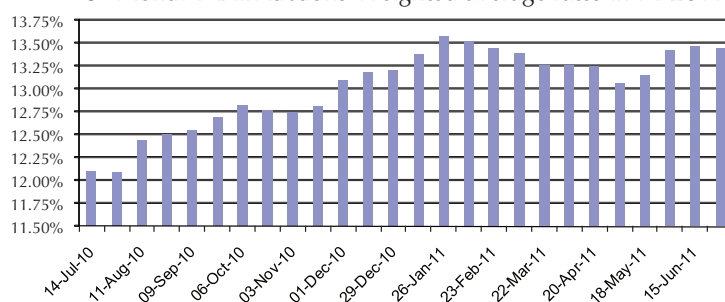
During the month, Oil & Gas, Financial Services, and Industrial Engineering sectors performed better than the market. Whereas, Banking, Chemicals, and Electricity sectors under-performed the market. Announcement of discovery by a key energy exploration company contributed to the out-performance of Oil and Gas Exploration sub-sector. Delay in announcement of Commercial Operation Date (COD) of its expansion plant by a selected fertilizer company due to gas curtailment resulted in the lagged performance of the Chemical sector. Risk of further increase in Non Performing Loans (NPLs) and associated high provisioning kept the investors away from taking positions in the Banking sector. Investors avoided taking positions in the Cement sub-sector due to weak dispatches' numbers despite decrease in the FED on cement in the Federal Budget of FY 2011-12.

Going forward, key drivers of the stock market will be: (i) Foreign Portfolio Investment activity; (ii) earnings announcements; (iii) Pak-US relations; (iv) law and order conditions and (v) Bilateral and Multilateral financial inflows.

## Fixed Income Review

FY-2011 ended with three increases of 0.5% each in the first half of the year taking the Discount rate to 14% from 12.5%. The T-Bills auctions bid pattern of June 2011, similar to the trend observed in the earlier two months, suggests that the market continues to prefer six months and one year T-Bills over three month papers. In the three T-Bills auctions of June, SBP cumulatively accepted Rs. 385.12 billion against the target of Rs. 375 billion. The cut off yields for the last auction of the month were noted at 13.49%, 13.74% and 13.91% for the 3 months, 6 months and 12 months T-Bills respectively.

3- Month T-Bill Auctions Weighted average rates in FY 2011



On the corporate debt sphere, there continues to be a marginal improvement in the market's demand for debt securities of high rated issuers. Total traded value reported by MUFAP for FY 2011 was Rs 16.23 bln. Banking sector TFCs contributed 62% of the total traded value during the year, followed by 16% and 14% in Telecom and Chemical sectors.

Inflation, as measured by CPI, averaged 14% for the first eleven months of FY-11 against 11.6% for the same period a year ago. Government borrowing from the scheduled banks is on the rise, which can only be matched with market appetite by offering high yields on Government Securities. As per SBP data, Banks are holding Rs 1,730 billion in liquid securities mainly T-Bills, which are Rs 958 billion more than the statutory requirement of Rs 772 billion. This excess holdings over required liquid assets by banks show their risk aversion. This factor is also crowding out the more productive private sector credit.

NAFA's money market fund i.e. NAFA Government Securities Liquid Fund (NGSLF) and income funds with short maturities and no TFCs, i.e. NAFA Savings Plus Fund (NSPF) and NAFA Riba Free Savings Fund (NRFSF), all posted competitive double digit returns this year. In the current interest rate environment as mentioned above, the returns of these funds are expected to remain attractive. For investors with long investment horizon of three or more years, our other income funds offer very attractive yields, although with some credit risk.

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