



November 2011

Stock Market Review

The stock market depicted downward trend with lot of volatility during the month of November 2011 on the back of weakening external accounts, fluid local political conditions, renewed concerns on the financial crisis in Eurozone and row over PAK-US diplomatic relations. Heavy sell-off of equities in the emerging markets further reduced the investors' confidence. After depicting downward trend in the first few trading sessions, the market recovered during the first half of the month. However, in the latter half of the month selling by the foreign investors and abysmally low trading volume kept the local investors from taking any fresh position in the market. Overall, during the month KSE-30 Index lost around 3.9% to close at 10800 levels.

State Bank of Pakistan in its recently announced monetary policy statement kept the Policy Rate unchanged at 12% against a cut of 150bps in the previous announcement. Key factors cited by the SBP are downside risk to the external accounts and expected uptick in inflationary trends. Foreign selling continued during the outgoing month as well with outflow of US \$ 4 million against US\$ 82 million during the previous month. Trading activity reduced to considerably lower levels during the month. Average Daily Trading volume for the month was recorded at around 45 million shares versus 92 million shares during the month of October.

The Oil & Gas, Construction & Materials, Banking and Electricity sectors performed better than the market while Chemicals, Non-life Insurance and Financial Services sectors lagged the market. Key companies in the banking sector out-performed the market due to their attractive valuations. Strong expected earnings growth of Oil & Gas Exploration companies resulted in out-performance of Oil and Gas sector. Urea price reduction, news of additional taxes and lower off-take numbers resulted in the lagged performance of the Fertilizer sub-sector. Electricity sector performed better due to attractive dividend yields and sanguine valuations of key companies.

Going forward, in our view, key drivers of the stock market will be: Foreign Portfolio Investment (FPI) activity, US-Pakistan diplomatic relationships, Economic and interest rates outlook, and domestic political situation.

Fixed Income Review

State Bank of Pakistan maintained Policy Rate at 12% in its Monetary Policy announcement on November 30, 2011, after decreasing the Rate by 2% in its first two bi-monthly announcements in FY12. SBP, while acknowledging the increase in macro-economic risks during last two months, maintained its inflation target of 12% for FY12. This indicates that the recent downward path of interest rates has already bottomed. After remaining stable for next few months, the rates may start going up due to vulnerability of Fiscal and Current Accounts. 6-Month KIBOR, the benchmark of lending rates in Pakistan averaged 11.91% for November. In the three T-bills auctions of November, SBP cumulatively accepted Rs. 521 billion against the target of Rs. 425 billion. The cut off yields (p.a.) for the last T-bill auction were noted at 11.65%, 11.67% and 11.80% for the 3 months, 6 months and 12 months maturities respectively. These rates are expected to move up by 10 basis points after the SBP decision, in the auctions scheduled in December.

On the corporate debt sphere, market volumes reported by MUFAP remained thin in November as well. Total traded value reported by MUFAP for November 2011 was Rs 757 mln, as against a value of Rs. 716 mln in October 2011. Banking sector bonds accounted for 87.05% of the traded value.

YoY Inflation (CPI) for October 2011 was 11%, while month-on-month inflation was 1.4%. During the Last four months i.e. (July – October 2011) average monthly increase in CPI is 1.28%. Government borrowing from the scheduled banks is consistently on the rise to finance fiscal deficit. In the first 141 days of the current fiscal year, net Government borrowing from scheduled banks has risen by 46% or Rs 646 billion, including Rs 391 billion conversion of energy sector related circular debt from loans to Government Securities. Current Account Deficit stood at 2% of GDP at the end of the first four months of FY2012 as against 0.8% for the same period last year.

NAFA Government Securities Liquid Fund is the only 'AAA(f)' rated money market fund in Pakistan greater than Rs 10 billion in size. The last three funds in fixed income category launched by NAFA, namely NAFA Savings Plus Fund, NAFA Riba Free Savings Fund and NAFA Financial Sector Income Fund, are also performing well, posting double digit returns. In the current economic environment as mentioned above, the returns of these funds are expected to remain attractive, considering their very low credit risk profile and floating rate linked investments.