# Capital Markets Review

November 2012

## Stock Market Review

During the month of November the stock market extended the gains of the undergoing fiscal year and the index reached an all-time high levels lead by Food Producers, Construction and Materials, Textile and Banking sectors. Expectations of monetary easing in the upcoming monetary policy announcements by the SBP; better-than-expected earnings reports of the selected sectors; and positive developments on the upcoming national elections cheered-up investors. On the other hand, deteriorating external and fiscal accounts stoke up concerns of the local and foreign investors. The month started with KSE-100 Index at 15,910 levels and closed the month at 16,574 levels. Overall, the stock market surged by 4.2% during the month, taking the fiscal year increase to 20%. Trading activity improved markedly with average daily traded volume at 216 million shares against 124 million shares in the previous month. Foreign investors' activity remained healthy with net inflows of US$ 35 million.

Despite significant decline in the interest rates amid fall in the inflation the economy is facing headwinds emanating from fragility of the external accounts, slippages on the fiscal accounts, and deep-seated structural weaknesses. Depleting foreign exchange reserves due to large loan payments to IMF and paucity of fiscal and capital inflows are exerting pressures on the exchange rate. The latent risks of currency depreciation and large government borrowings are building upside risks to the inflation expectations. Lack of any decisive efforts on the part of policy makers to resolve the structural issues facing economy, economic growth is expected to remain subdued. In its upcoming monetary policy decision in the first half of December, SBP will strike balance between these complicated economic indicators.

Oil and Gas, Chemicals, and Electricity sectors were among the laggards. On the other hand, Banking, Constructions and Material, Food Producers sectors were among the out-performers. Subdued off-take of the fertilizer and chronic gas curtailment kept investors from fertilizer sub-sector. Electricity sector is facing mounting circular debt issues impacting its attractiveness as a dividend play. Attractive valuations and expectations of healthy payouts drew investors' interest in the Banking sector. Construction and Materials sector remained in the lime light amid optimistic earnings outlook.

In our view, the market will take direction from upcoming elections announcement, inflation and interest rates outlook and foreign investors' activity.

## Fixed Income Review

The YoY headline inflation as measured by CPI stood at 6.9% for the month of November 2012 as compared to 7.7% in October 2012, which created room for SBP to consider further easing in the upcoming monetary policy announcement. The expectation of 50 bps rate cut was reflected in Treasury yields in the secondary market as well as in the last auction. In the T-Bill auctions during the month, MoF accepted Rs 317 billion (realized amount) against the target of Rs 300 billion and maturity of Rs 244 billion. During the month of November, T-Bills auctions bid pattern continued to depict major participation in 6-month tenor, while considerably small interest was observed in 3 months.

Yields of AA rated banking sector TFCs in the secondary market have declined due to limited primary issues and aversion for low credit quality TFCs. The prevailing yields (KIBOR + 50 to 70bps) on such TFCs does not justify the inherent risks – interest rate, credit and liquidity. Trading activity of TFCs in the secondary market remained healthy during the month, with total traded value reported by MUFAP at Rs 547 mln. Banking sector bonds contribution in the total traded value of private sector bonds was around 85% during November, while remaining volume was in Chemicals and Telecom sector bonds. Due to lower yields on eligible universe of TFCs and upside risk to the interest rates, we have not built further position in TFCs. We are monitoring the market situation and will rebalance the Portfolio proactively.