



**NBP Fullerton
Asset Management Limited**
(Formerly National Fullerton Asset Management Limited)

Capital Market Review

October 2010

Stock Market Review

During October 2010, the stock market demonstrated decent performance led by strong corporate results. The month began with weak investors sentiments due to hike in the Policy rate, fluctuating political situation and persistent inflationary pressures. The month started with the KSE-30 Index at 9700 level and touched a high of 10297 on October 25, 2010. Later on, investors brushed aside political noise and economic worries and took positions in the market mainly focusing on healthy earnings announcements and improved Foreign Portfolio Investment. Overall, the KSE-30 Index gained around 4.97% during the month.

The inflationary pressures are showing persistence driven by food inflation due to supply side shocks. For the month of September 2010, the inflation as measured by CPI was recorded at 15.7% on a YoY basis. Net Foreign Portfolio Investment (FPI) activity slightly improved during the month. Net FPI during October 2010 was recorded at around US \$ 31.82 million, as against US \$ 22.35 million during September 2010. Trading activity improved substantially and Average Daily Traded Volume during October 2010 was recorded at 106.95 million shares, compared to 60.77 million shares in September 2010.

The Oil & Gas Exploration sub-sector out-performed the market due to healthy earnings growth. The Refineries sub-sector performed better than the market as a result of higher earnings than expectations. The Oil and Gas Marketing sub-sector demonstrated sluggish performance on the back of lower than expected corporate earnings due to the turnover tax. Banking sector out-performed the market driven by better than expected earnings announcements. Lower offtake of urea weakened investors sentiments in key companies in the Fertilizer sub-sector that resulted in their under-performance versus the market. Expectations of higher dispatches post-flood enabled the cement sub-sector to perform better than the market. Some of the key companies in the Power sub-sector under-performed the market due to lower than expected earnings.

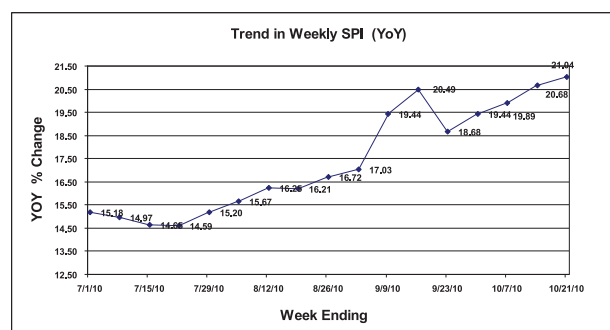
Going forward, we believe that key drivers of the stock market are: (i) launch of financing product; (ii) Foreign Portfolio Investment activity; (iii) foreign assistance and aid in the flood related areas; (iv) inflationary trends; and (v) SBP monetary stance.

Fixed Income Review

Headline inflation (Year on Year Consumer Price Index, CPI) reached 15.7% in September 2010, from 13.2% a month earlier. The below chart of the weekly YoY change in the Sensitive Price Indicator (SPI) also suggests the same trend.

In addition, Pakistan's domestic debt has swelled to Rs 4.86 trillion in August 2010 from Rs 4.05 trillion a year ago, an increase of 20.1%. These two challenges of inflation and fiscal deficit on the one hand, slow economic and private sector growth on the other hand, need to be addressed by the Government and the SBP.

Current account surplus for the month of September was USD 447 million in contrast to the average monthly deficit of USD 496 million during the first two months of the current fiscal year. This has resulted in improvement in the Current Account deficit by 7.7% in Q1, FY 2011 over Q1, FY2010. Imports declined and Workers' remittances increased to USD 2,646 million in Q1, FY2011 from USD 2,331 million in Q1, FY2010, an improvement of 13.5%.



TFC pricing volatility continued during the month and most of the income funds faced volatility. A few selected TFCs are trading at significantly lower prices. Restructuring agreements of a few remaining non-performing TFCs are expected to be finalized during November 2010. We advise that income funds' investors should take a longer term view in order to take advantage of the attractive yields on current prices of the debt securities. With increase in the Discount Rate in the previous month, the new coupons resets are occurring at higher Base rates (KIBOR). The monthly average of 6-Months KIBOR was 13.21% in October 2010 as compared to 12.92% in September 2010. This has further improved the attractiveness of the TFCs. For investors with a shorter investment horizon, NAFA Government Securities Liquid Fund, NAFA Savings Plus Fund and NAFA Riba Free Savings Fund continue to post competitive returns in line with the market. As of September 2010, the banking system deposits of over Rs 4.6 trillion are placed at a weighted average rate of 5.77%, roughly half the return of what the above mentioned short-term Funds are currently yielding.

The money market remained fairly liquid during most of October. In the two T-bills auctions of October, SBP cumulatively accepted about Rs. 228 billion against the target of Rs. 175 billion. The cut off yields for the last auction of the month were noted at 12.79%, 13.11% and 13.24% for the 3 months, 6 months and 12 months T-bills respectively. Going forward, interest rates are not expected to ease as Government borrowing is expected to remain excessive.

Disclaimer: This publication is for informational purpose only and nothing herein should be construed as a solicitation, recommendation or an offer to buy or sell the fund. All investments in mutual funds are subject to market risks. The price of units may go up as well as down. Past Performance is not necessarily indicative of future results.