



September 2013

## Stock Market Review

The stock market after depicting a lot of volatility during the month retreated during the latter half with a correction of 7.6% in the last five trading sessions. The stock market rallied during the first half of the month on the erroneous perception of a benign IMF program. However, pursuant to an unexpected increase in discount rate, emerging clarity on tough quantitative targets set by the IMF, subsequent fall in PKR/USD parity and, lastly, increase in minimum deposit rate (MDR) on savings deposits of banks, the index went into a significant correction mode. Hawkish SBP tone and likely increase in inflation indicate further monetary policy tightening going forward. Resultantly, investors started taking position in index heavy banking sector, the key beneficiary of higher interest rates, which provided some support to the market post monetary policy announcement. However, steep fall in PKR/USD exchange rate and increase in MDR further soured the market sentiment causing KSE-100 Index to plunge by a massive 7.6% from 24 Sept to date. Average daily trading volume recorded at 215mn shares compared with 201mn shares during the previous month. Due to increasing concerns on currency depreciation and fiscal woes, Foreign Portfolio flows turned negative recording an outflow of \$7mn during Sept-13.

Our estimates suggest that currently market is trading at 8.0 times forward earnings. Expected increase in inflation to double digits indicates further tightening in the upcoming monetary policy. Furthermore, likely squeeze in liquidity amid increasingly stringent ceiling on government borrowing from SBP shall prove further drag on the market in the coming months. In anticipation of correction in the market we reduced our allocation in equities below the market weight that benefitted our funds. We are closely monitoring the capital market developments and will reposition our asset allocation accordingly.

## Fixed Income Review

In an unexpected move, State Bank of Pakistan (SBP) hiked Discount Rate by 50bps to 9.50% in its monetary policy decision of September 13, 2013, ending the monetary easing cycle which started in August 2011 and delivered its last rate cut in June 2013. SBP cited inflationary impact of GST increase, phasing out of subsidies, potential instability in oil price and continued government reliance on banks to finance its fiscal deficit as the key factors for the higher inflation expectations. Due to above mentioned reasons SBP expects inflation in the range of 11-12% for FY14.

In the two T-Bills auctions during the month, MoF accepted Rs 604 billion (realized amount) against the target of Rs 500 billion and maturity of Rs 425 billion. The cut-off annualized yields for the last T-Bill auction were noted at around 9.41% and 9.45% for 3 and 6 months respectively, while no bid was received in 12-month tenor. T-Bills auction bid pattern depicted major participation in 3-month as compared to 6-month tenor, while market participants showed no interest in 12-month tenor due to expectations of further hike in the policy rate. In PIB auction during the month an amount of Rs. 16 billion was accepted against the target of Rs. 50 billion at a cut-off yield of 11.69%, 12.15% and 12.60% in the 3 year, 5 year and 10 year tenors respectively, whereas no bid was received in the 20-year tenor. As mentioned in our last monthly report, in anticipation of monetary tightening we kept short maturities of our money market funds which benefitted our investors. We will continue to follow this strategy on the expectation of further uptick in the interest rates in the coming months.