

Stock Market Review

Amid amplified volatility, the stock market remained in the grip of bears, albeit a hefty rebound in the third week of the month, with the benchmark KSE-100 Index declining sharply by 7.1% on a month-on-month basis. August 2019 was the seventh consecutive month of losses at the local bourse. The market shrugged off the significantly improved Current Account Deficit (CAD) number for July 2019 that clocked in at USD 579 million versus USD 2,130 million for the same period last year. Conversely, the focus of the market participants shifted squarely to the deteriorating relationship between the nuclear-armed India-Pakistan after the repeal of article 370 and imposition of curfew/lockdown by the former in Indian occupied Kashmir. The news flow regarding the shortfall in budgetary revenue collection for the ongoing fiscal year also sent jitters in the market. Towards the end of the month, the announcement of government's intention to partially sell its stakes in the Index heavy OGDCL & PPL also weighed on the performance of the stock market. Consequently, despite dirt cheap valuations in the broader part of the market, investors resorted to indiscriminate selling or opted to stay on the side line.

During the month, Automobile Assemblers, Chemicals, Oil & Gas Exploration, Oil & Gas Marketing Companies, Power Generation & Distribution lagged the market. On the other hand, Cement, Commercial Banks, Engineering, Fertilizer, and Textile Composite sectors performed better than the market. Looking at the participant-wise activity during the month, Mutual Funds and Insurance Companies remained the major sellers in the market, offloading equities worth USD 34 million and USD 10 million, respectively. Alongside, Foreign Investors turned sellers, liquidating positions worth USD 4 million. On the contrary, Individual Investors and Banks/DFIs, continued to be the main buyers in the market, accumulating fresh positions to the tune of USD 28 million and USD 8 million, respectively. Similarly, Companies added net equity positions amounting to USD 6 million.

What lies ahead? On the economic front, stabilization policies including monetary policy tightening, PKR devaluation, and expanding the tax base/increasing the tax rates have started yielding positive results as the CAD for July 2019 has shrunk significantly. We also expect inflation to start moderating in the 2nd half of FY2020 after peaking at around 13% in February 2020. From the valuation perspective, after a hefty 44% decline in the benchmark KSE-100 Index from all-time high level of 52,876 points hit in May 2017 to 29,672 points, the market is trading at a compelling forward Price-to-Earnings (P/E) multiple of 5.4 and offers around 7% dividend yield. On a relative basis, this indiscriminate sell-off has made PSX the cheapest market in the region. Corporate earnings growth, the overarching determinant of the stock market performance, remains resilient despite slowing economic growth and is expected to grow at double-digit rate for 2020 and 2021, helped by the Index heavy Oil & Gas Exploration, Banking, Power, and Fertilizer sectors. Contrary to the foreign portfolio outflows during the last three years, there are increasing odds of continuation of foreign portfolio inflows this year and beyond.

Taken it all together, we advise investors to look past the dismal performance of the stock market over the last two years or so and consider adding their positions in equities gradually, keeping long-term investment objectives in mind as the market holds potential to deliver robust returns.

Money Market Review

After recording 10.3% YoY in July 2019, inflation as measured by CPI is expected to go up in the next few months. The inflation outlook is driven by upside inflationary pressures from the second-round impact of the recent PKR depreciation, higher government borrowing from the banking system, recent adjustments in utility prices and rising food prices. However, the inflation going forward in FY21 is expected to fall. We expect inflation to peak at around 13% in February and start falling by the end of FY2020. We expect that interest is nearing its peak however, a further 50 bps increase can not be ruled out.

During the outgoing month, SBP held two T-Bill auctions with a combined target of Rs. 2,600 billion against the maturity of Rs. 3,341 billion. In the first T-Bill auction, an amount of Rs. 1,229 billion was accepted at a cut-off yield of 13.75%, 13.95% and 14.25% for 3-month, 6-month and 12-month tenors, respectively. In the second T-Bill auction, an amount of Rs. 701 billion was accepted where the cut-off yield was maintained at 13.75% for the 3-month tenor while yields for 6-month and 12-month tenures were noted at 13.94% and 14.24%, respectively. In the PIB auction, bids worth Rs. 514 billion were realized for 3-year, 5-year and 10-year at a cut-off yield of 14.25%, 13.55% and 13.15%, respectively; while bids for 20-years were rejected. Furthermore, SBP in the recent floating rate PIB auction dated 21-August-19, attracted bids worth Rs. 47.5 billion. Out of the total bids, only Rs. 41.5 billion was accepted at a cut-off margin of 75 basis points over the benchmark (i.e. weighted average yield of the 6-month Market Treasury Bills).

We have calibrated the portfolio of our money market and income funds based on our interest rate outlook and will remain alert to any developments that may influence our investment strategy.