

Stock Market Review

Amid heightened volatility, rally at the local bourse extended during December as the benchmark KSE 100 Index increased by 1,447 points (3.7%) on a month-on-month basis, taking CY2019 return to 9.9%. The market started off the outgoing month on a strong note with the KSE 100 Index reaching a high of 41,769 points on December 17th, a hefty 6.3% rise from the last month closing level. However, the market lost momentum as heightened uncertainty surrounding the special court's verdict in a high treason case against ex-president Musharraf weighed on investors' sentiments amid fear of stand-off between the state institutions. Provocative statements by the Indian Army Chief against Pakistan and buildup of military installations along the Line of Control (LoC) also unnerved investors. However, the downside was short lived due to positive developments on the economic front.

The current account deficit (CAD) plunged by 73% to USD 319 million in November, as compared to USD 1,166 million in the same period last year. The SBP received concessionary loan of USD 1.3 billion from the Asian Development Bank for budgetary support and power sector reforms that lent support to the FX reserves in the wake of foreign loan payments. The SBP also received USD 452 million as a second tranche of the USD 6 billion IMF loan after successful review where it mentioned that Pakistan's economic reform program is on track and decisive policy implementation is helping to preserve economic stability. In our view, this endorsement by the IMF would boost the confidence of foreign investors that would pave the way for fetching Foreign Investment (FDI & FPI), facilitate access to the international capital markets, and accelerate flows from the multilateral agencies. However, determination by the OGRA for significant increase in gas prices, that awaits government's approval, weighed on the investors' sentiments as it would stoke inflation and hurt the corporate profitability.

What lies ahead for the market in CY2020? In our view, the market holds potential to exhibit strong performance in CY2020. Despite robust rally from its lows, the market is trading at an attractive forward P/E multiple of 7.0, as per our estimates. Corporate earnings are expected to grow at double digit rates for 2020 and 2021. We expect economic growth to recover in FY2021 as economic stabilization takes hold in FY2020. There is ample local liquidity that is likely to enter the market amid declining appeal of alternative fixed income and real estate avenues. During CY2020, the odds of substantial foreign portfolio inflows have increased as economy is well on the path of stabilization.

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The SBP raised interest rates by 325bps in CY19 to counter inflation and contain demand pressures. However, after achieving stability on the external front, the Discount Rate was left unchanged in the last two policy meetings. During CY20, we project inflation to remain elevated in mainly in the first half of the year; however, we estimate it to fall sharply in second half of the year. Resultantly, we expect interest rates to fall by around 200bps in CY20.

During the outgoing month, SBP held three T-Bill auctions with a combined target of Rs. 1,000 billion against the maturity of Rs. 546 billion. In the first T-Bill auction, an amount of Rs. 370 billion was accepted at a cut-off yield of 13.54%, 13.29% and 13.14% for 3-month, 6-month and 12-month tenures, respectively. In the second T-Bill auction, an amount of Rs. 449 billion was accepted at a cut-off yield of 13.49%, 13.29% and 13.13% for 3-month, 6-month and 12-month tenures, respectively. In the third T-Bill auction, an amount of Rs. 469 billion was accepted at a cut-off yield of 13.49%, 13.29% and 13.13% for 3-month, 6-month and 12-month tenures respectively. Besides this, in the PIB auction, bids worth Rs. 151 billion were realized for 3-year, 5-year and 10-year at a cut-off yield of 11.75%, 11.19% and 10.99% respectively; while bids for 20-year tenure were rejected. Furthermore, SBP in the recent floating rate PIB auction held on December 11th attracted bids worth Rs. 142 billion. Out of the total bids, only Rs. 77 billion was accepted at a cut-off margin of 39.5 basis points over the benchmark (i.e. weighted average yield of the 06-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.