

Stock Market Review

Equity market performance remained listless during June-20 as the benchmark KSE-100 Index rose by 491 points (1.4%) on a MoM basis. The month started off on a positive note as investors looked forward to the Federal Budget, which was being termed as Corona relief budget and the Index was up by around 1,200 points in the first 9 trading days, but the market was somewhat disappointed by the budget, paring the earlier gains. Though the government did not take any new taxation measures, it envisaged around PKR 5 trillion FBR revenues target, compared to the expected revenue collection of PKR 3.9 trillion in FY20 (translating into a mammoth growth of 27%), which puzzled the market. The participants expected some rationalization in CGT which did not materialize. On the positive side, Super-corona tax was not levied and corporate tax rate was maintained. Other than FED hike across non essential/luxury products such as cigarettes, and double cabin vehicles, some relief has been offered to numerous other sectors in the form of reduction in custom duties, regulatory duties to lower the input material costs and enhance the ease of doing business. FED on cement has been reduced, WHT on steel melters has been withdrawn, and remittances have been exempted from WHT too. Textiles will also benefit from reduction in duties on raw materials and Sales Tax on POS linked retailers has also been brought down to 12% to enhance tax compliance in the sector. In our view, this budget is neutral to positive for the market. Also, in another surprise meeting during the month, the central bank further cut the Policy Rate by 1%, which also augurs well for stock market.

During the month, Automobile Parts & Accessories, Banks, Fertilizers, Paper & Board, and Pharma sectors performed better than the market. On the contrary, Chemicals, Engineering, Food & Personal Care, Glass, Insurance, Oil & Gas Exploration, Power Generation, Technology and Textile sectors lagged behind. On participant-wise activity, Foreign Investors remained major sellers in the market, liquidating stocks worth USD 46 million, and cumulative net outflows amounting to USD 285 million in FY2020. Local investors were net buyers in the month, with large sizeable inflows of USD 18 million, USD 10 million, and USD 10 million from Individuals, Mutual Funds and Insurance, respectively.

We advise investors to look beyond short-term economic turmoil as we believe that rapid pace of development on an effective vaccine and treatment would gradually restore economic activity. The recent drop in number of cases and flattening of active cases in the country also seem encouraging. The unprecedented monetary easing and historic fiscal relief would assuage the economic damage and we expect economic activity to start returning to some normalcy from 1st quarter of FY21. From the valuation standpoint, the market is trading at an undemanding Price-to-Earnings multiple of 7x and offers a healthy 6% dividend yield. We contend that the case for flow of funds towards equities from alternate fixed income avenues has strengthened given the large 6.25% reduction in Policy Rate by the SBP. Empirical analysis also suggests that equities perform well in a low inflation and interest rates environment. Taken it all together, we advise investors to stay the course, ignore the short-term market volatility and consolidate position in equities, focusing on their long-term investment objectives.

Money Market Review

In an unscheduled meeting held on June 23rd, the State Bank of Pakistan (SBP) decided to further reduce the policy rate by 100 basis points to 7%, a cumulative reduction of 6.25% during this monetary easing cycle. The SBP cited continuing economic slowdown, rising downward risk to economic growth, rising unemployment, and improving inflation outlook. SBP has seen a decline in its foreign exchange reserve largely due to foreign debt payments. However, since then, SBP has received fresh inflows of \$1.75 Billion from the World Bank, Asian Development Bank, and Asian Infrastructure Investment Bank. Inflation as measured by the CPI clocked-in at 8.6% due to hike in food prices owing to supply side disruption. We expect inflation to moderate to 7% in FY21. In our view, interest rates have bottomed out.

During the outgoing month, T-Bill auctions were held with a combined target of Rs.475 Billion against the maturity of Rs. 238 billion. In the first T-Bill auction, an amount of Rs. 164 billion was accepted at a cut-off yield of 8.13%, 7.98% and 7.71% for 3-month, 6-month and 12-month tenures, respectively. In the second T-Bill auction, an amount of Rs. 75 billion was accepted at a cut-off yield of 7.8%, 7.48% and 7.36% for 3-month, 6-month and 12-month tenures, respectively. In the PIB auction, bids worth Rs. 115 billion were realized for 3-year, 5-year, 10-year, 15-year & 20 years at a cut-off yield of 7.97%, 8.44%, 8.99%, 9.90% and 10.51%, respectively. Furthermore, SBP in the recent floating rate of PIB auction dated 17th June, attracted bids worth around Rs. 164 billion. Out of the total bids, only Rs. 124 billion was accepted at a cut-off margin of 70 basis points over the benchmark.