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Weekly Stock Market Commentary

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During the week ending August 7th, amid high average daily trading volumes and large intraday swings, the benchmark KSE 100 Index increased by 772 points (2%) on a week-on-week basis. Carrying forward the positive momentum, the market started off the week on a strong note, rising by a massive 614 points on Monday, 3rd August. However, during the subsequent trading days of the week, some investors opted for profit taking as the Index reached near the psychological level of 40,000. It merits highlighting that the market has delivered a massive return of 47% from its bottom it hit on March 25th, 2020. This robust performance of the market is attributable to positive developments on the public health front; bold & timely policy actions by the policymakers; and encouraging economic data.

Looking at the participant-wise activity during the week, Individual Investors emerged as the sole major buyers in market, accumulating fresh positions worth USD 41 million. Alongside, Foreign Investors turned buyers, adding equities for an amount of USD 4 million. On the contrary, Insurance Companies turned major sellers in the market, off-loading shares to the tune of USD 29 million. Likewise, Mutual Funds and Other Organizations sold shares worth USD 12 million and USD 3 million, respectively.

What lies ahead for the stock market? In our view, the market would take cue from path of the pandemic, progress on the development of an effective & widely available vaccine, and associated global & local economic recovery. Encouraged by a substantial drop in the Covid-19 new infections, the federal government has announced that restrictions on the hospitality and recreational sectors, put in place nearly five months ago to curb the spread of the coronavirus, would be lifted from August 10th. On the vaccine development front, there are more than 165 vaccines in the different stages of development, 28 are in human trials, and six are at stage-III of large-scale efficacy test.

On the economic front, average inflation for FY21 is expected to moderate to 7% after clocking-in at 10.8% in FY20. The Policy Rate after peaking at 13.25% has come down to 7%. The Current Account Deficit (CAD) has narrowed to USD 3 bn (1.3% of the GDP) in FY20 that is expected to widen to a still manageable level of USD 4.4 bn (1.6% of the GDP) in FY21.

From the valuation perspective, despite a robust rally, the stock market is trading at an undemanding forward Price-to-Earnings (P/E) multiple of 8x and Price-to-Book value of 1.0x. The market also offers a healthy dividend yield of 5.2% that looks appealing compared with a paltry 7% yield on T-Bills. While Coronavirus induced slowdown in the economic activity would impact corporate profitability in the short-term, we expect strong corporate earnings growth over the next two to three years.

Bottom Line: While the market may depict large swings, we hold a positive view on the stock market over the medium to long-term given: undemanding valuations; benign near-term inflation outlook & loose monetary conditions; plentiful local liquidity; a manageable Current Account Deficit (CAD); and a healthy corporate earnings growth over the next two to three years.