August 2020

Stock Market Review

During Aug-20, the stock market carried forward the positive momentum from the previous month as the benchmark KSE-100 Index surged by around 1,853 points (4.7%) on a month-on-month basis. The market derived its optimism from improving business environment as Covid-19 related restrictions were further lifted from the remaining sectors, and the entire economy was re-opened, backed by major decline in new Covid-19 cases as well as total active cases. Moreover, the high frequency economic data released during August also points to normalization of economic and trade activities, e.g. cement sales grew by 33%, FBR collection mounted by 15%, POL product sale exhibited growth of around 10% YoY, and fertilizer sales surged by 20-30% on a YoY basis. The improving trend was also observed in the external trade numbers, as exports rebounded to USD 2 billion, from USD 1.9 billion, a year ago, showing a YoY growth of 6%. The key highlight was the record workers' remittances, which clocked in at USD 2.77 billion during July leading to a large current account surplus of USD 424 million. Notably, the market remained impervious to the negative news related to the GIDC decision by the SC, MoUs signed by IPPs agreeing to reduce their returns, and rumours of strains in Pak-Saudi relations after the agreement between UAE and Israel for normalization of relations between two countries.

During the month, Automobile Parts & Accessories, Cements, Engineering, Oil & Gas Marketing Companies, Paper & Board, Power Generation & Distribution, Refineries, Technology & Communication, Textile and Transport sectors performed better than the market. On the contrary, Auto Assembler, Commercial Banks, Fertilizers, Food & Personal Care, and Oil & Gas Exploration sectors lagged behind. On participant-wise activity, Insurance Companies and Banks/DFIs remained major sellers in the market, liquidating stocks worth USD 37 million and USD 28 million, respectively. Foreign selling abated a bit to USD 7 million during the month. On the contrary, Individuals and Mutual Funds were the largest buyers with net inflows to the tune of USD 59 million and USD 12 million, respectively.

It has been an impressive start of the year FY2021, as the market has surged by a significant 19% during 2MFY21. Looking ahead, we maintain our positive outlook for the market over the medium to long-term. Our liking for the stock market is underpinned by growing optimism on health as well as economic fronts. Economic activity is gathering pace as corroborated by high frequency economic data. We expect continuation of monetary easing going forward given benign near-term inflation outlook. Though one cannot rule out second wave of the Coronavirus pandemic that might again impede the economic activity; the repair/policy response market phase is likely to be followed by the recovery phase where the economic fundamentals would improve and catch-up investors' optimism. External account is also likely to remain manageable given decent export growth and continuation of multilateral inflows. From the valuation standpoint, the market is trading at an undemanding Price-to-Earnings multiple of 7.8x and offers a healthy 5% dividend yield. Taken it all together, we advise investors to ignore the short term market volatility and consolidate position in equities, focusing on their long-term investment objectives.

Money Market Review

After clocking in at 9.3% in July 2020, driven by upward adjustment in retail fuel prices and spike in prices of some food items; CPI inflation for August stood at 8.2%. We expect to inflation to moderate to 7%-8% in FY21 after clocking-in at 10.7% in FY20. After an aggressive 6.25% reduction in the Policy Rate by the SBP in this easing cycle, interest rates have bottomed out, in our view. We expect the central bank to continue with the accommodative monetary policy stance in the near term to stimulate the economy that is hit hard by the Covid-19 induced economic disruption.

During the outgoing month, SBP held two T-Bill auctions with a combined target of Rs. 600 billion against the maturity of Rs. 832 billion. In the first T-Bill auction, an amount of Rs. 111 billion was accepted at a cut-off yield of 6.99%, 7.18% and 7.15% for 3-month, 6-month and 12-month tenures, respectively. In the second T-Bill auction, an amount of Rs. 532 billion was accepted at a cut-off yield of 7.15%, 7.18% and 7.30% for 3-month, 6-month and 12-month tenures, respectively. In the PIB auction, bids worth Rs. 45 billion were realized for 3-year, 5-year, 10-year, 15-year & 20-year at a cut-off yield of 8.20%, 8.45%, 8.99%, 9.98% and 10.55%, respectively. Furthermore, SBP in the recent floating rate PIB auction dated 27th August, attracted bids worth around Rs. 218 billion. Out of the total bids, only Rs. 88 billion was accepted at a cut-off margin of 30 basis points for 3 year tenure, 37 basis points for 5 year, and 54 basis points for 10 year over the benchmark.

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.

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