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Weekly Stock Market Commentary

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During the outgoing week, positivity was witnessed at the local bourse as the benchmark KSE 100 Index surged by 1,102 points (2.7%) on a week-on-week basis. As we see it, investors looked past the rising noise in the domestic politics and shifted their attention to the ongoing corporate results season where majority of the companies posted above expected earnings and, in some cases, announced hefty payouts. Adding to the investors' optimism was improving macroeconomic indicators as the country again posted current account surplus of USD 73 million in the month of September 2020, taking 1QFY21 current account surplus to USD 792 million versus a deficit of USD 1,492 million during the same period last year. However, market sentiments were muted by the news surrounding the upcoming meeting of the Financial Action Task Force (FATF) plenary scheduled for Oct 21-23 to decide whether Pakistan should be excluded from its grey list, based on the review of Islamabad's performance to meet global commitments and standards on fight against Money Laundering and Terrorist Financing (ML&TF).

Looking at the participant-wise activity during the week, Mutual Funds emerged as the largest buyers in the market, accumulating fresh positions to the tune of USD 8 million. Alongside, Companies and Broker Proprietary Trading were other major buyers, adding equities amounting to USD 5 million and USD 3 million, respectively. On the other hand, Banks/DFIs stood as the largest sellers in the market, trimming their holdings to the tune of USD 8 million. Similarly, Foreign Investors and Individuals were other major sellers in the market, liquidating shares worth USD 7 million and USD 4 million, respectively.

What lies ahead for the market? We believe that the investment landscape is constructive for equities. Our sanguine view on the stock market is driven by improving economic prospects and attractive market fundamentals. Despite some recent increase in the active cases of Covid-19 in the country, we do not expect any significant disruption to the economic activity due to shutdown of businesses. On the vaccine development front, researchers are testing 48 vaccines in clinical trials on humans worldwide, with twelve vaccines under large-scale efficacy test and six approved for early / limited use.

The three-day FATF plenary meetings to review Pakistan's progress on 27 action plans concluded that the country has made progress across all action plan items and has now largely addressed 21 of the 27 action items however, the FATF strongly urged Islamabad to swiftly complete its full action plan by February 2021. We see this outcome as an acknowledgement of Pakistan's efforts in strengthening AML/CFT framework. This, along with the requisite actions would go a long way in making monetary transactions more transparent that in turn would help in curbing terrorist financing and support the drive for documentation of economy.

On the economic front, business activity has gained momentum as reflected by the frequently released economic data such as automobile sales, retail fuel sales, and cement dispatches. Similarly, Large Scale Manufacturing (LSM) data also confirm increasing industrial activity. We see recent elevated CPI readings as transitory and anticipate inflation to moderate to 8% in FY21 compared with 10.7% in FY20. The SBP is likely to maintain the prevailing accommodative monetary policy regime in the near-term to support nascent economic recovery in the backdrop of challenging global economic outlook. External account, the Achille's heel of Pakistan's economy has improved significantly, thanks to a hefty 31% increase in the workers' remittances during 1QFY21. We anticipate the Current Account Deficit (CAD) to widen to a still manageable level of USD 4.4 billion (1.7% of the GDP) in FY21.

From the fundamental perspective, the stock market is attractive as captured by the forward Price-to-Earnings (P/E) multiple of 7.6, versus 10-year average of 8.5x. On a relative basis, the Earnings Yield of 13.2% offered by the market also looks appealing compared with the 10-year PIB yield of 10.02%. The market also offers a healthy dividend yield of 5.5%. Corporate earnings are expected to grow at a healthy rate over the next two to three years.

Taken it all together, we believe that market is well poised to deliver healthy double-digit returns over the medium to long-term. Therefore, we advise investors with the medium to long-term investment horizon to build positions in equities through our NBP stock funds.