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Weekly Stock Market Commentary

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During the holiday shortened outgoing week, amid large intraday swings, led by the Oil & Gas Exploration sector, the benchmark KSE 100 Index gained by 520 points (an increase of 1.1%) on a week-on-week basis. During FYTD through February 4th 2021, the market has delivered a robust return of 36% and it has surged by a massive 72% from its bottom hit on March 25th 2020.

Looking at the participant-wise activity during the week, Individual Investors and Companies stood as major buyers in the market, accumulating fresh positions to the tune of USD 9 million and USD 7 million, respectively. On the contrary, Other Organization, Insurance Companies, and Foreign Investors emerged as main sellers in the market, offloading their positions by USD 6 million, USD 4 million, and USD 3 million, respectively.

Many investors are still skeptical of this ongoing rally at the local bourse as they think that the market is disconnected from the real economy. Actually, the market is forward looking and is driven by future economic prospects and not by the present economic conditions. Based on the same cardinal principle, we have witnessed a spectacular rally at the local bourse off the March 2020 low when the Coronavirus mandated lockdown brought the economic activity to a standstill. The improving economic activity as manifested by the frequently released economic data such as cement dispatches, automobile sales volumes, and sales of the retail fuel has started catching up with investors' optimism. In turn, the robust corporate earnings growth in 1QFY2021 and strong showing in the ongoing results season has validated this remarkable market rally and would power the next leg up, in our view.

Another concern of some investors is that the market has gone too far too fast and therefore has run its course. As we understand, new bull markets that coincide with new economic cycles last for years, not months. In short, the market has a long way to run. As we see it, investors are underestimating the constructive investment backdrop for equities shaped by improving economic outlook, attractive market valuations, promising corporate earnings prospects, and easier financial conditions.

On the economic front, economic activity has picked up steam as reflected by a robust 7.41% y-o-y growth in the Large-Scale Manufacturing Industries (LSMI) as per the latest available data of 5MFY21. During 1HFY2021, a current account surplus of USD 1.1 billion was recorded compared to a deficit of USD 2 billion during the corresponding period last year. The SBP has signaled the continuation of the accommodative monetary policy in the coming months and we anticipate a modest 1%-1.5% hike in the Policy Rate during CY21. From the valuation standpoint, the market is trading at an attractive forward Price-to-Earnings (P/E) multiple of 7.4x, versus 10-year average of 8.5x. The market also offers a healthy dividend yield of 5%. Corporate earnings are expected to grow at a double-digit rate over the next two to three years.

The bottom Line: There is a strong investment case for equities for investors with medium to long-term investment horizon. Our sanguine view on the stock market is underpinned by attractive market valuations, robust expected corporate earnings growth, and supportive financial conditions.