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Weekly Stock Market Commentary

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During the holiday shortened outgoing week, despite large future rollover positions, the market continued positive momentum with the benchmark KSE 100 Index rising by a decent 620 points (1.4%) on a week-on-week basis. From its recent low level of 42,780 hit on March 11th, the market has recovered by 6.4% and it is merely 3% off from the February 3rd peak level of 46,934. It may also be recalled that during FYTD through March 26th, the market has delivered robust returns of 32% and it has surged by a hefty 67% from its bottom hit during the Coronavirus crash in March 2020.

Looking at the participant-wise activity during the week, Broker Proprietary Trading and Mutual Funds emerged as major buyers in the market, accumulating fresh positions to the tune of USD 4 million and USD 2 million, respectively. On the contrary, Banks/DFIs and Companies remained main sellers in the market, offloading their equity holdings by USD 3 million and USD 2 million, respectively.

What to expect from the market going forward? We reiterate our sanguine view on the market over medium to long-term given improving economic outlook, a supportive financial condition, attractive market valuations, and promising corporate earnings prospects. Economic activity has gained momentum as reflected by the output of the Large Scale Manufacturing Industry (LSMI) that rose sharply by 9.13% in January 2021, taking 7MFY21 growth to an impressive 7.85%. Similarly, persistent upswing is observed in the business sentiment as SBP-IBA Business Confidence Survey shows the overall business confidence index increasing further to 60 in February 2021 from 56 in December 2020. This pick-up in economic activity coupled with the easier financial conditions bode well for the corporate profitability and we expect a double-digit corporate earnings growth over the next two to three years.

External account, the key determinant of our stock market performance has improved significantly, thanks to a large 24% year-on-year growth in the workers' remittances during 8MFY21. Moreover, during 8MFY21, a cumulative Current Account surplus of USD 881 million was recorded, vis-à-vis a Current Account Deficit (CAD) of USD 2.74 billion during the same period last year.

From the valuation standpoint, the market is trading at a forward Price-to-Earnings (P/E) multiple of 6.6x, versus 10-year average of 8.5x. The Earnings Yield of 15.15% offered by the market also looks appealing compared with 10-year PIB Yield of 10.45%. The stock market also offers a healthy dividend yield of 5%. We anticipate continuation of the prevailing easier financial conditions with a modest 1%-1.5% hike in the Policy Rate during CY21.

The Bottom Line: Taken together, there is a strong investment case for equities driven by: (i) attractive valuations as captured by the forward P/E multiple of 6.6x; (ii) double digit corporate earnings growth expected over the next two to three years; (iii) easier financial conditions; and (iv) paltry yields on the alternative fixed income avenues. Therefore, we advise investors with medium to long-term investment horizon to build positions in equities through our NBP stock funds.