

Stock Market Review

After three consecutive months of positive return, some mild correction was witnessed at the stock market during February 2021, as the benchmark KSE-100 Index dropped marginally by 521 points (modest decline of 1.1%) on a month-on-month basis. We reckon that this muted market performance is due to some profit taking in the market, since the market has risen by a robust 33% during FY21 to date through February, and has surged by a whopping 68% from its recent bottom hit in March 2020. Thus, we view this brief pause as a healthy consolidation to an otherwise strong trendy market. Our conviction on the market is underpinned by strong showing in the ongoing corporate result season during which most of the companies surpassed street estimates both in terms of superior revenue growth and as well as margin expansion, driven by robust demand across all sectors. This is again indicative of our oft iterated viewpoint of sharp rebound in economic activity. Other notable developments during the month included the cabinet approval of government and IPPs deal, which is win-win for both parties. Other major highlight of the month was long awaited resumption of the IMF program, as the country and the Fund reached staff level agreement over reforms that will lead to release of USD 500 million. The IMF also acknowledged that the policies and reforms implemented by the authorities reduced economic imbalances and set the conditions for improving economic performance prior to Covid-19 and most of the targets under the EFF-supported program were on track to be met. Another key event of the month was the scheduled plenary meeting of FATEF, that decided to keep Pakistan in its 'grey list', though it acknowledged significant progress made on the entire action plan, as the country has made progress across all action plan items and has now largely addressed 24 of the 27 action items.

During the month, Cements, Automobile Assemblers, Chemical, Oil & Gas Exploration, Pharmaceutical, Refinery, Technology and Textile Composite sectors performed better than the market. On the contrary, Commercial Banks, Engineering, Food & Personal Care, Glass & Ceramics, Oil & Gas Marketing, Paper & Board, and Power Generation & Distribution sectors lagged behind. On participant-wise activity, Individuals and Companies stood as major buyers in the market, adding equities worth USD 34 million and USD 23 million, respectively. Insurance Companies, Banks/DFIs, and Broker Proprietary Trading were major sellers, offloading their positions by USD 18 million, USD 12 million, and USD 11 million, respectively.

Going forward, we reiterate our positive view on the stock market underpinned by the improving economic outlook, supportive financial conditions, attractive market valuations, and promising corporate earnings prospects. Economic activity has gathered pace as reflected by the output of the Large Scale Manufacturing Industry (LSMI) that rose sharply by 11.4% for December 2020, taking half year growth to an impressive 8.2%. Moreover, the recently concluded corporate result season also substantiates the economic recovery narrative. Current Account Deficit (CAD) for January clocked-in at USD 229 million, taking seven months' cumulative Current Account surplus to USD 912 million, vis-à-vis a CAD of USD 2.54 billion during the same period last year. From the valuation stand point, the market is trading at an attractive forward Price-to-Earnings (P/E) multiple of 6.8x, versus 10-year average of 8.5x. The market also offers a healthy dividend yield of 5%. We expect corporate earnings to grow at a double-digit rate over the next two to three years. We anticipate continuation of accommodative monetary policy regime in the coming months with a modest 1%-1.5% hike in the Policy Rate during CY21. Therefore, we believe that there is a strong investment case for equities and we advise investors with medium to long-term investment horizon to build positions in stock market through our NBP stock funds.

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Inflation as measured by the CPI increased to 8.7% for February 2021 versus 5.7% in January 2021 mainly due to spike in electricity tariff. We expect inflation to keep upward trajectory due to expected rise in retail fuel prices, base effect, and some further rise in power tariff. We expect the SBP to maintain accommodative monetary policy regime in the near term with a modest 1% to 1.5% increase in the Policy Rate in CY21.

During the outgoing month, SBP held two T-Bill auctions with a combined target of Rs. 1,400 billion against the maturity of Rs. 1,314 billion. In the first T-Bill auction, an amount of Rs. 669 billion was accepted at a cut-off yield of 7.18%, 7.49% and 7.80% for 3-month, 6-month, and 12-month tenures, respectively. In the second T-Bill auction, an amount of Rs. 768 billion was accepted at a cut-off yield of 7.25% and 7.55%, for 3-month, 6-month, tenures, respectively whereas bids for 12-month were rejected. In the PIB auction, bids worth Rs. 62 billion were realized for 3-year, 5-year, 10-year & 20-year tenures at a cut-off yield of 8.99%, 9.59%, 10.05% and 10.58%, respectively.

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.