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Weekly Stock Market Commentary

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During the week ending October 15th, 2021, amid heightened volatility, the benchmark KSE 100 Index managed to increase by 344 points (a gain of 0.8%) on a week-on-week basis. The market started off the outgoing week on a faltering note as the Index slumped by 1,255 points during the first three trading days of the week. However, amid value buying during the last two trading days, the market reversed all the earlier losses of the week to close the Index with a decent gain. For the context, despite attractive valuations, the market has delivered a meagre 2.4% return during CY21 through October 15th, 2021. In our view, this lackluster market performance is attributable to investors' concern on the corporate profitability outlook; worries over the Balance of Payment (BoP) position; anxiety over shifting Pak-US relations; and sell-off by the leveraged retail investors, who received margin calls after continuous decline in the Index. So-called stalemate over the appointment of DG ISI also sent jitters in the market during the outgoing week.

Regarding participant-wise activity during the week, Foreigners emerged as the largest sellers in the market, liquidating their equity holdings to the tune of USD 13 million. Alongside, Companies and Individuals were other main sellers, as each trimmed their positions by USD 3 million. On the other hand, Insurance Companies stood as the largest buyers in the market, accumulating shares worth USD 12 million. Likewise, Mutual Funds and Other Organization were other major buyers, as each bought shares worth USD 3 million.

Regarding the much-needed International Monetary Fund (IMF) Programme, in a bid to revive the programme, the government has sought the federal cabinet's approval to increase electricity tariff by Rs. 1.39 per unit. According to sources, against the IMF's demand to levy Rs. 525 billion additional taxes, the government has shown inclination to immediately withdraw over Rs. 300 billion sales tax exemptions. The large currency devaluation, beginning of monetary tightening cycle with a token 25 bps hike in the Policy Rate, hike in electricity prices, and willingness to levy additional taxes show commitment of the government for resumption of the stalled IMF programme. The successful completion of 6th review would pave the way for the release of USD 1 billion from the IMF under the Extended Fund Facility (EFF) and facilitate flows from other multilateral agencies such as the Asian Development Bank, World Bank, and Islamic Development Bank.

Looking ahead, we reiterate our positive view on the stock market given: extremely attractive market valuations; strong economic activity; easier financial conditions; and plentiful market liquidity. We expect healthy corporate profitability as companies are gradually passing on the increasing input costs to maintain profit margins due to resilient consumer demand. To curtail import-based consumption demand, the SBP has let the currency devalue by over 10% since May-21 and has broadened the scope of 100% cash margin requirement on imports. Similarly, the government has levied regulatory duties on non-essential imported items. In the same vein, the benchmark Policy Rate was increased by 25 bps to 7.25%. In our view, the SBP would gradually dial back the prevailing ultra-loose monetary accommodation that is unlikely to lead to disruptive financial tightening. We believe that these demand compression policies would prevent overheating of the economy (as envisaged by the poliymakers), but unlikely to derail the ongoing growth momentum.

The market is currently valued at an attractive forward Price-to-Earnings (P/E) multiple of 5.8x, versus 10-year average of 8.3x. The market also offers a healthy 5.8% dividend yield. In our view, the market is well poised to deliver a healthy double-digit return in FY22, and beyond. Therefore, we advise investors with medium to long-term investment horizon to build position in the market through our NBP stock funds.