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Weekly Stock Market Commentary

December 10, 2021

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During the week ending December 10th, 2021, the stock market performance remained muted, and the benchmark KSE-100 index rose by 163 points (up by 0.4% on a week on week basis). Except for Oil and Gas exploration sector, where investors are eyeing for some resolution of circular debt emanating from short term liquidity injection, almost all other major sectors remained under pressure.

Several factors can be attributed to the recent lackluster performance of the equity market. Firstly, the CPI numbers released last week, which clocked in at 11.53% for Nov-21, beat the market consensus by a wide margin and rattled the confidence of the investors. It has fueled the expectations of further and steeper hike in the policy rate, as reflected by uptrend in the yield curve across all maturities. Secondly, the trade deficit numbers stood at an alarming level for the month of November-21. Driven by the highest ever imports, which clocked in at USD 7.85 billion, the trade deficit surged by around USD 1 billion on a MoM basis, to stand at USD 4.96 billion which further unnerved the market participants. Thirdly, investors also remained wary of government's commitment of supplementary money bill as part of an agreement with the IMF for a net fiscal adjustment of almost PKR 550 billion during the remaining part of the current fiscal year through cut in development spending, withdrawal of sales tax exemptions, and hike in Petroleum Development Levey (PDL). There is also growing possibility that the government may step up tax rates for commercial banks which dented the sector prospects, despite promising earnings growth going forward. Likewise, the untoward event in Sialkot brought bad publicity for the Textiles, as investors weighed its impact on the outlook of the sector.

Regarding participant-wise activity during the week, Mutual Funds emerged as the largest sellers in the market, that offloaded stocks worth USD 4 million amid redemptions. Alongside, Broker Prop. Trading sold stocks to the tune of USD 2 million. On the contrary, Other Organizations, and Companies were the largest buyers, adding equities amounting to USD 4 million, and USD 2 million, respectively.

Looking ahead, though there are some economic challenges in the form of burgeoning current account deficit (CAD) & inflationary pressures, we believe that the monetary and fiscal authorities have demonstrated their intent to bring stability and preserve growth using various policy tools. The current monetary tightening, coupled with the higher Cash Reserve Requirement (CRR) of banks attempt to cool down domestic demand that will help arrest CAD and ease off inflationary pressures going forward. In addition to the steep currency devaluation, enhanced scope of cash margin on imports, the government is looking to further enhance the duties and restrict import of non-essential items. More importantly, the commodity cycle also appears to have waned somewhat (iron ore, coal, crude oil, palm oil prices have moderated), that will help soften the trade deficit going forward. And as and when the impact of TERF led machinery and vaccines imports wane off, the external numbers will improve thenceforth. Lastly the revival of EFF facility with the IMF will allow for resumption of multilateral flows of IFIs and Eurobond issuance, which will ease pressure on the BoP and market yields, and bring discipline on part of the government towards macroprudential measures.

From the fundamental perspective, the market is trading at an attractive forward Price-to-Earnings (P/E) multiple of 5.5x versus 10-year average of 8.3x. The market also offers a healthy 6% dividend yield. As we see it, the recent sell-off has sent the market valuations to the equivalent of the crisis eras. Therefore, given a strong investment case for equities, we advise investors with medium to long-term investment horizon to build position in the stock market through our NBP stock funds.