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Weekly Stock Market Commentary

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During the outgoing week ending 22nd July, the KSE-100 index declined by around 1,998 points, translating into a weekly drop of 4.7%. Trading activity also slowed down on a week on week basis, and almost all the major sectors closed in red, with Banking, Fertilizer & Cement sectors responsible for more than half of index decline.

Right from the start of the week, the stock market remained in bear grip. The stocks fell for four straight days during the week, before slight bounce back on the last trading day. Political uncertainty triggered by the relatively unexpected result of the by-elections on 20 seats held in Punjab on Sunday, initiated the market decline. Contrary to expectations of most political analysts, PTI trumped PML-N, that had the unequivocal support of the PDM, by bagging around 15 seats and as a result became the leading party in the Punjab provincial assembly. The surprise result once again spooked investors as it again casted uncertainty over the continuity of the present government set-up that was formed just a couple of months back, after PTI was ousted from the federal and Punjab governments. This political uncertainty has again brought forth economic uncertainty, as investors appeared frightened about the ongoing precarious economic situation. Though IMF has accorded its nod & Staff Level Agreement has been reached, but the usual delay in Board approval before realization of inflows remained a cause of concern as reserves remain abysmally thin and under pressure, which unnerved investors. Rising yields on some of Pakistan's international Sukuks and Eurobonds that reached alarming level of around 50% further unhinged confidence as it also fueled the solvency concerns of the country. It also led to steep and unprecedented PKR devaluation against USD during the week, that was agonizing for investors and further eroded the sentiment of the market. The Rupee lost its value by around 8.3% (around PKR 17.4 per USD) during the outgoing week. SBP reserves further fell by around USD 389 million to stand at USD 9.3 billion. During the week, ratings agency Fitch has revised Pakistan's outlook to negative from stable while affirming its long-term foreign-currency (LTFC) issuer default rating (IDR) at "B-". It highlighted that renewed political volatility cannot be excluded and could undermine the authorities' fiscal and external adjustment, as happened in early 2022 and 2018, particularly in the current environment of slowing growth and high inflation.

In terms of trading activity during the week, Individual & Foreigners were the largest buyers with net inflows to the tune of USD 5 million and USD 3 million, respectively. On the contrary, Mutual Funds & Insurance remained the largest sellers with net outflows of USD 8 million and USD 2 million respectively.

Looking ahead, inflation is likely to remain elevated throughout the rest of the year with an accompanying tight monetary setting during the year. While economic growth will moderate, it will be more sustainable and durable. The key challenge has been on the external front and with signing of IMF staff level agreement and with global commodity super cycle waning gradually, we remain cautiously optimistic on the ability of the country to steer through the ongoing challenges. With IMF deal, flows from friendly countries are also likely to follow through and the resumption of multi-lateral funding will also materialize that will help shore up FX reserves.

In terms of corporate earnings outlook, the recent budgetary measure (10% one-off tax) and the economic measures (Utilities and fuel price rationalization) will squeeze the near-term earnings profile of listed corporate sector. Furthermore, due to mounting inflationary pressures amidst steep devaluation seen in the last few months, demand and as well as margins of the corporates may also come under pressure. Having said this, we again re-iterate that current stock market valuations compensate for the risks highlighted. Any tangible improvement on economic front will trigger a strong relief rally.

Looking at the fundamentals, the valuations of stock market remain inexpensive. Corporate profitability growth is expected at around 15% in FY22, despite imposition of 10% super tax. For FY23, we expect the growth to moderate to 9.1%. Due to lackluster market performance, Price-to-Earnings Ratio (P/E) has come down to a multi-year low of around 4.2 times (earnings yield of around 24%).

Therefore, we advise investors with medium to long-term investment horizon to build position in the stock market through our NBP stock funds. Short-term risk-averse investors can benefit from double digit interest rates by investing in our NBP savings and money market funds.