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Weekly Stock Market Commentary

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During the outgoing week ending 5th Aug, stock market rebounded sharply as KSE-100 index shot up by around 1,946 points, translating into a healthy weekly gain of 4.8%. The rally was broad based as all sectors contributed to the index gain, however, Banks & Cement sectors were major driving force in propelling the index. In terms of sectoral return, Engineering, Cements, Autos and OMCs outperformed the market.

Though start of the week was pretty lukewarm, as the index further receded by 0.2% on Monday. However, as the week progressed, there was a major shift in investors' sentiments and the stock market displayed swift bounce back in subsequent days, surging by 2,020 points. There were few positive developments that have led to this change. Firstly, the trade deficit for July-22 depicted a marked improvement on a monthly basis, declining from around USD 5 billion in June-22 to USD 2.6 billion, raising hope that the runaway CAD has finally been arrested. Though it is too soon to think that this trend would sustain, but it points towards relative benign CAD for FY23, below the market expectations. Its impact was also visible on the currency market as pressure on payments mellowed and importers rushed to bring in their proceeds. As a result, Pak Rupee also reversed the ongoing weakening trend and strengthened by PKR 15.3 per USD (around 6.4%), closing at PKR 224 at the end of the week, which also comforted investors. IMF representative also said that Pakistan had met last prior action required for combined 7th and 8th review by raising the petroleum development levy (PDL). The development paves the way for the disbursement of the USD 1.17 billion tranche. In another positive news, SBP acting governor informed that Pakistan is set to get assurances of USD 4 billion additional financing from friendly countries shortly that is now the only stumbling block for revival of the IMF program. International debt instrument yields also responded to these developments and came off considerably during the week. International commodity prices, especially crude oil further trended downwards, owing to demand slackening and rising fears of global slowdown/recession. Inflation for the month of July-22 was also reported during the week, that clocked in at 24.9%, highest in the last 14 years.

In terms of trading activity during the week, Brokers & Mutual Funds were the largest buyers with net inflows to the tune of USD 2 million each. On the contrary, Banks/DFIs & Foreigners remained the largest sellers with net outflows of USD 1 million each.

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

In terms of corporate earnings, we acknowledge that backdrop remains challenging due to recent budgetary measures (10% one-off tax) and the economic measures (utilities and fuel price rationalization). Furthermore, due to mounting inflationary pressures amidst steep devaluation seen in the last few months, demand and as well as margins of cyclical corporates may also come under pressure. However, for other sectors that remain insulated from demand pressures, and are beneficiary of PKR devaluation and Interest rate upcycle like Oil & Gas, Power Generation, Fertilizers, Technology, and Commercial Banks, we expect robust earnings growth going ahead, offsetting the decline in cyclical sector profitability. Therefore, we expect that overall corporate profitability would continue to grow, albeit at a modest pace. The recent corporate result announcements also strengthen this view, where companies have posted record pre-tax earnings. We again re-iterate that current stock market valuations compensate for the risks highlighted and any tangible improvement on economic front will trigger a strong relief rally.

Looking at the fundamentals, where Price-to-Earnings Ratio (P/E) of the market is at multi-year low of around 4.4 times (earnings yield of around 23%). Therefore, we advise investors with medium to long-term investment horizon to build position in the stock market through our NBP stock funds.