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Weekly Stock Market Commentary

July 29, 2022

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During the outgoing week ending 29th July, the stock market performance remained muted as KSE-100 index crept up by around 72 points, translating into a weekly gain of 0.2%. In terms of index contribution, Commercial Banks and Oil & Gas Exploration sectors positively contributed to the index, while Fertilizer sector remained a major drag on the index.

The market started off the week on a negative note and index fell by 0.6% on Monday, as political wrangling continued in the country. The newly elect Chief Minister (CM) Punjab was first directed to work as a trustee by the Supreme Court (SC), while later on in its decision, the SC struck down Punjab Assembly deputy speaker's ruling in CM favor. The continuing political brinksmanship amidst ongoing economic turmoil has beleaguered the investors and the market. During the week, current account deficit (CAD) numbers were released, which clocked in at USD 2.3 billion, up massively by USD 845 million, on a month on month basis, taking FY22 CAD to USD 17.4 billion (highest CAD in last 4 years), up from USD 2.8 billion in the previous year. Record fuel imports during the month led to massive CAD increase during the month. Foreign exchange reserves held by the central bank continued their descent, dropping by around USD 754 million, to stand at USD 8.6 billion on July 22nd. In the same vein, PKR continued to depreciate against USD at a brisk pace, losing its value by around 4.8%, further rattling the confidence of the market participants. After Moody's and Fitch, the S&P Global Ratings on Thursday revised the outlook on Pakistan's long-term ratings to negative from stable previously.

In terms of trading activity during the week, Banks/DFIs & Companies were the largest buyers with net inflows to the tune of USD 3 million and USD 2 million, respectively. On the contrary, Individuals & Insurance remained the largest sellers with net outflows of USD 2 million each.

Looking ahead, we are of the view that economic backdrop is set to improve in the coming month. 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 will also follow through and the resumption of multi-lateral funding will also materialize that will help shore up FX reserves. Inflation is likely to remain elevated throughout the rest of the year with an accompanying tight monetary setting during the year. Though it will moderate economic growth, it will be more sustainable and durable.

Looking ahead at corporate earnings, we acknowledge that environment remains challenging for the corporate listed space due to the 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 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 announcement in the outgoing week also strengthen this view, where fertilizers and banks have posted record pre-tax earnings. We again re-iterate that current stock market valuations compensate for the risks highlighted earlier and 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 is expected to grow by around 15% in FY22, despite imposition of 10% super tax. For FY23, we expect the growth to moderate to 7-9%. 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, 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. Investors who seek safety can benefit from the double digit interest rates via our NBP money market and savings funds.