Weekly Stock Market Commentary

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During the outgoing week ending 26th May, the stock market posted losses on a week-on-week basis, as the benchmark KSE-100 fell by 635 points (down by 1.5%).

Negative sentiments prevailed in the stock market primarily attributable to the persistent political uncertainty and delays in the IMF program. The Finance Minister Ishaq Dar, while speaking to a delegation of businessmen, also hinted that the IMF program may expire on June 30th without revival due to restricted time. Investors also exercised caution due to rumors about potential new taxes in the upcoming budget. Proposed tax reforms include, but are not limited to, capital gains tax on movable and immovable property, taxing exporters who hold back foreign exchange in anticipation of rupee devaluation and make gains on their foreign exchange, imposing higher tax rates on non-filers to broaden the tax base, and taxing the accumulated reserves of all companies. Although exact mechanism of slapping additional taxes on corporates on accumulated profits is still unclear, it will have serious consequences on the cashflows of many companies and market also penalized few of those low dividend paying stocks during the week under review. Economic data for the country's output was also released during the week. The provisional growth rate of GDP for the fiscal year 2022-23 is estimated at 0.29%, with the agricultural sector growing at 1.55%, the industrial sector experiencing a negative growth of 2.94%, and the services sector growing at 0.86%. The IMF program remains deadlocked, and the PM has hinted at expected support from China till the time IMF program is not revived. The FX reserves held by the State Bank of Pakistan (SBP) decreased by USD 119 mn to USD 4.19 bn during the week, providing a one-month import cover.

Going forward, we acknowledge that the country is facing serious macro-economic challenges in the form of record high inflation, woefully inadequate foreign exchange reserves held by SBP, and large revenue collection shortfall. With near end to the ongoing IMF program, meeting the near-term debt obligations will further erode the reserves, although the government has underlined that bulk of these loans will be rolled over, there will be further drawn down in reserves, which are already abysmally low. It will also put further pressure on the currency, which in recent days has again seen its gap widening in the open market due to elevated seasonal demand. This growing disparity between the open and interbank markets suggests the likelihood of heightened imported inflation in the months ahead. Investors will also be been keenly following the upcoming budget, which many fears will be an election budget and may further erode investors confidence, since it will further imperil the macro-economic stability. The ongoing political unrest within the country, coupled with the persistent conflict between the government and opposition, is exacerbating economic uncertainty and adversely affecting both economic metrics and stock market returns.

Having said this, we also find it pertinent to highlight that despite challenges facing the economy, corporate profitability has so far remained resilient. During the 1QCY23, the listed corporate sector has posted a cumulative profit growth of around 15-18%. However, the burgeoning macro-economic challenges and the new budgetary measures pose a risk to growth. That said, the ongoing wave of buybacks and stock purchases by leading corporates and sponsors in their respective industries also remain key catalyst which have strengthened investors' confidence in select companies and sectors. At the same time, it has been a source of much needed liquidity for the market.

Looking at fundamentals, Price-to-Earnings Ratio (P/E) of market is at multi-year low of around 3.8 times (earnings yield of around 26.3% as against 10-yr PIB yield of 15.1%). Therefore, we advise investors with medium to long-term investment horizon to build position in stock market through our NBP stock funds.