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Weekly Stock Market Commentary

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The equity market experienced a modest uptick during the week ending on January 26th, as the benchmark KSE-100 index gained 531 points, translating into a week-on-week return of 0.8%. The primary contributors to these index gains were the Oil & Gas Exploration, Banking, and Fertilizer sectors.

The week began on a strong note following the release of the first review report by the IMF over the previous weekend. In the report, the Fund expressed overall satisfaction with Pakistan's economic progress and structural benchmarks. The IMF made significant downward revisions to Pakistan's gross external financing requirements, lowering them by around USD 15.5 billion over the FY24-FY26 period. Additionally, GDP growth for FY24 was revised down from 2.5% to 2%, and inflation estimates were slightly trimmed. A crucial structural benchmark set by the IMF was the implementation of gas tariff adjustments by February 15th, as determined by Ogra. The IMF also emphasized the need for a formalized plan to reduce circular debt in the gas sector. The inclusion of gas price revisions in the IMF's structural benchmarks is expected to mitigate the flow of gas sector circular debt and boost investor confidence.

The KSE 100 index rallied in the first three days of the week, led by strong price performances in heavyweight Oil & Gas sector stocks. The Ministry of Energy was reportedly working on proposals to settle the approximately PKR 1250 billion stock of gas sector circular debt. As a result of this settlement, benchmark index heavyweights OGDC and PPL were expected to receive PKR 552 billion and PKR 126 billion, respectively. Subsequent media reports indicated differences in the Ministry of Finance, which were eventually resolved before the plan was sent to the IMF for approval. While there may be better ways to execute the circular debt management plan in our opinion, the plan should not pose issues for the IMF, provided it remains fiscally neutral for the government.

In terms of other major news, cut-off yields in the latest T-Bill auction dropped by 62 basis points for the 12-month paper, recording at 20.23%. Similarly, 3-month and 6-month papers also witnessed a drop in yields by 50 and 56 basis points, respectively, signaling market expectations of a likely cut in the policy rate. In this auction, the government raised PKR 184 billion against overwhelming participation of PKR 1,121 billion. On the external front, SBP's reserves reached a six-month high after a net increase of USD 243 million during the week. Domestic commodity prices showed some relief as weekly inflation declined slightly by 0.14% WoW, following four consecutive weeks of an uptick. Pak-Iran relations also appear to have normalized after a brief period of tension escalation last week, contributing to a calming effect on investors' nerves.

Looking ahead, we reckon that equities may remained sideways in the near term, ahead of the general elections, scheduled on 8^{th} February. The political environment will remain charged and the prevailing uncertainty surrounding elections may result in pre-election nervousness amongst investors. The investors will also be keenly following Monetary Policy Committee meeting scheduled for Monday, whereby majority of the market participants expects status quo in the rates, but any surprise rate cut can not be ruled out. However, in the medium to long term, we expect strong price performance in equities to continue given the favorable conditions in the back drop of 1) steep decline in Policy Rate expected in CY24 on the back of easing inflationary pressures, 2) sizeable inflow of foreign and as well as institutional liquidity in equities, and 3) strong earnings momentum of listed companies.

Despite blistering stock market performance since July-23, our universe's Price-to-Earnings Ratio (P/E) stands at a modest 4.2x (Bloomberg PE 3.6x), translating into an earning yield of approximately 23.8%, surpassing the 10-year PIB yield of 14.2%. Additionally, the market boasts a healthy dividend yield of 9-10%.

For investors eyeing a medium to long-term horizon, we recommend establishing a position in the stock market through our NBP stock funds. Our funds have demonstrated a track record of delivering superior returns. Notably, our flagship Nafa Stock Fund (NSF) exhibited outstanding performance in the outgoing CY23, yielding an impressive 60.1% return compared to the benchmark KSE-100 Index return of 54.5%. This resulted in a substantial outperformance of 5.6% (net of all expenses) for our valued investors, reaffirming the fund's commitment to generating significant returns beyond market benchmarks.