January 1, 2021
REP-019

PAKISTAN
STRATEGY

MARKET
VISTA

2020—A study in perseverance

- In a year of many firsts, persistent and pervasive headline risks making for, at times, a noisy macro environment, the KSE-100 index exhibited immunity (~61% recovery from March'20 lows), posting +7.4% return for the year, continuing its annual run-up to a second consecutive year supporting the long term upward momentum of domestic equity markets (5/10 yr cumulative return of ~32%/3.6x, avg. annual ~6/53%)
- Average volumes solidified significantly, with KSE100/All volumes rising 92/108%YoY where average traded value in the ready counter climbed to an annual avg of US$75.2mn (up 93%YoY, highest point in three years), while investors branched out to small and mid-cap stocks in search of returns (KSE-100 share of ready volume averaged 63% vs. 68% in CY19)
- Individual participation dominated flows during the year (US$232.3mn) followed by Insurance (US$229.9mn) and Companies (US$110.6mn), where the latter participants doubled down on their positions late in the year, while FPI outflows picked pace (US$571.2mn), taking cumulative outflows over the last five years to US$1.9bn, with Banks also clocking net outflows (US$33.4mn)
- Sectors driving the index higher during the year were Edible oils (+3.4x), Technology (+2.2x), Engineering/Steel (+97%), Paper (+74.2%) and Refineries (+66.8%), with index heavy weights remaining laggards E&Ps (-23.6%), Power (-13.5%), Commercial Banks (-4.8%) and Fertz (-2.6%), mostly from idiosyncratic dampeners (liquidity crunch, policy uncertainty, choppy crude price environment).
- Return to normalcy, particularly in the wake of vaccine launches, would bring back IMF and sustained reform agenda as key determinants driving market performance in the medium run. Our conviction on CY21 market outlooks stems directly from profitability expectations of the broader market where ex-Banks, we foresee earnings growth of 23% while D/Y stands at an impressive 7.5%.

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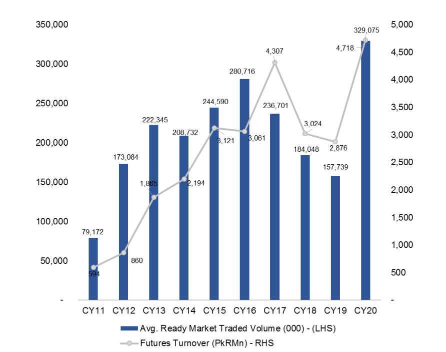
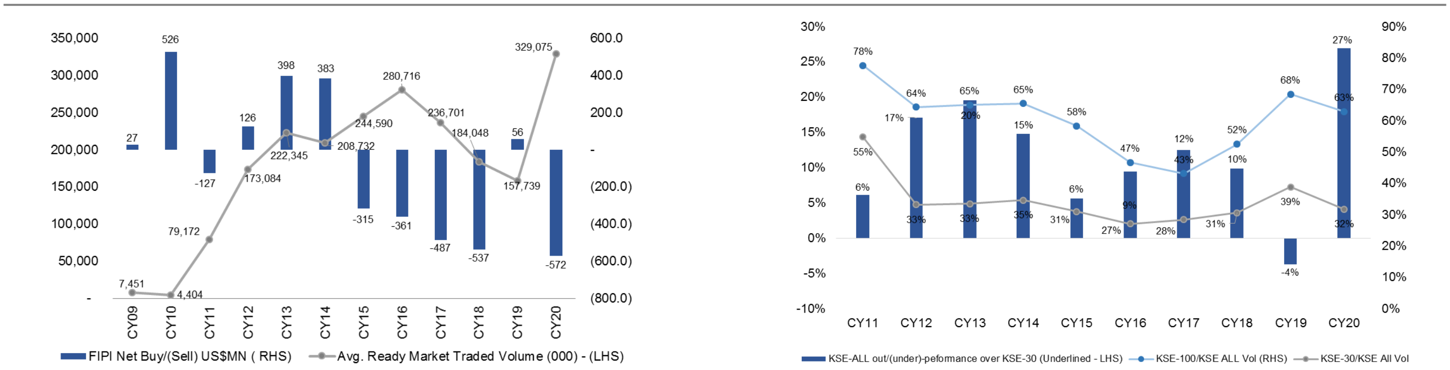
Futures and Ready market turnover climb



Source: PSX & AKD Research

Despite foreign selling, ready market traded volume climbed to highs as investors shunned large cap sectors



Source: PSX & AKD Research

A study in perseverance: Starting the year on a rough note and contending with the spread of a global pandemic, raising the trade-offs between human costs and economic spillovers to levels not seen during this century, domestic equity markets confounded bearish sentiments. In a year of many firsts (social distancing, lockdowns, work from home) persistent and pervasive headline risks making for at times, noisy external macro environment (crude price volatility, commodity swings), the KSE-100 index exhibited immunity (~61% recovery from March'20 lows), posting +7.4% return for the year, continuing its annual run-up to a second consecutive year supporting

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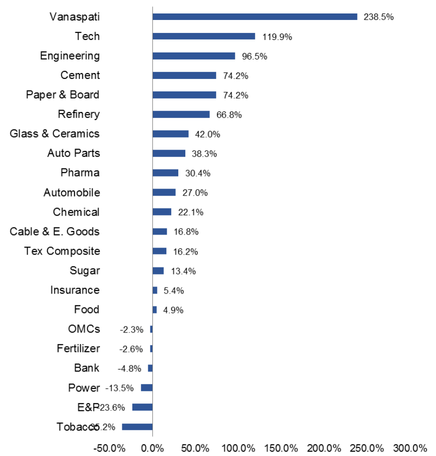
the long term upward momentum of domestic equity markets (5/10 yr cumulative return of ~32%/3.6x, avg. annual ~6/53%).

Small and mid cap sectors excite: Sectors driving the index higher during the year were Edible oils (+3.4x, as demand for staples remained robust), Technology (+2.2x, work from home/ new economy effects), Engineering/Steel (+97%, pricing power on the back of construction package), Paper (+74.2%) and Refineries (+66.8%, expected reforms), with index heavy weights remaining laggards E&Ps (-23.6%), Power (-13.5%), Commercial Banks (-4.8%) and Fertz (-2.6%), mostly from idiosyncratic dampeners (liquidity crunch, policy uncertainty, choppy crude price environment). Sectors contributing to index strength included Cements (74.2% on the back of construction sector incentives, debt relief), Autos (27.0%, from new model launches) and Textile (16.2% from strong export order books).

Flows remain prominent: Individual participation dominated flows during the year (US$232.3mn) followed by Insurance (US$229.9mn) and Companies (US$110.6mn), where the latter participants doubled down on their positions late in the year, while FPI outflows picked pace (US$571.2mn), taking cumulative outflows over the last five years to US$1.9bn, with Banks also clocking net outflows (US$33.4mn). Within FPI flows, selling was concentrated in Banks (US$168.3mn), E&P (US$119.6mn), Cements (US$100.9mn) with the three accounting for 68% of total outflows during the year.

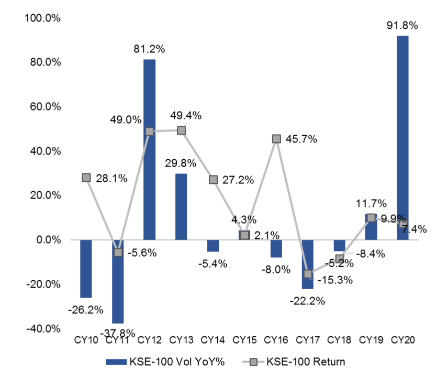
Investment Perspective: With the Govt. prioritizing to build economic gains earned during CY20 (continuation of construction-related amnesty), market is likely to sustain its bull run in the immediate run with liquidity flush providing additional support. Senate elections and political climate would be the factors to keep an eye on in the short run whereas FATF Review would take backstage, in our view. However in the return to normalcy, particularly in the wake of vaccine launches (despite efficacy, supply chain/logistics remain uncertain), would bring back IMF and sustained reform agenda as a key determinant driving market performance in the medium run. Our conviction on CY21 market outlooks stems directly from profitability expectations of the broader market where ex-Banks, we foresee earnings growth of 23% while D/Y stands at an impressive 7.5%. While across the board bullish on Pakistan equities, preferred plays include Banks (interest rate tightening, multiple re-rating – HBL, MCB, MEBL), Oil & Gas (valuations – OGDC), Cements (demand growth – LUCK, MLCF), OMCs (new policy, circular debt clearance – PSO), Textiles (valuations, export outlook – NML), Power (circular debt clearance – HUBC), Technology (valuations – TRG, SYS) and Autos (numbers outlook – INDU). We also like FFBL in Fertilizers (earnings outlook), THALL and GTYR in Auto & Allied and PSX on valuations.

Sector performance CY20



Source: NCCPL & AKD Research

KSE-100 volume and returns



Source: PSX & AKD Research

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- Discounted Cash Flow (DCF, DDM)
- Relative Valuation (P/E, P/B, P/S etc.)
- Equity & Asset return based methodologies (EVA, Residual Income etc.)

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Neutral	**＞ 8.5% to ＜ 14.5% expected total return**
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