NBP Fullerton Asset Management Ltd.
A Subsidiary of National Bank of Pakistan

Dr. Amjad Waheed, CFA
Chief Executive Officer

Investment Outlook under the Newly Elected Government

The stock market has responded positively to the election of the new government led by Pakistan Muslim League (N). Investors consider the PML(N) government to be more “pro-business” relative to the previous one. The stock market has risen sharply by 9.6 % since the date of the elections. However, even the 31.7% rise in the stock market over the six months preceding the elections can be mostly attributed to the expectations of a change of government, as almost all polls results were predicting that PML(N) will win the elections.

The honey moon period will be short for the newly elected government. The SBP foreign exchange reserves have dropped to an alarming level of US$6.6 billion, with huge payments outstanding to IMF in the coming months. The Coalition Support Fund is expected to release around US$ 1.5 billion shortly, but this will not be sufficient. Some are expecting the Saudis to bail us out with a package of US$ 15 billion. However, this does not seem realistic. The safer and faster course of action for the government is to sign a new package with the IMF, which will give it breathing room, and eliminate the threat of any default by the country. In the medium term there is no other solution than to increase revenues and reduce spending, especially subsidies to state-owned enterprises, which presently exceed Rs 500 billion per annum.

The new government is expected to announce its budget for FY13-14 by mid-June. We expect the budget to include some tough measures like a double-digit increase in electricity prices, elimination of subsidies, and some tax measures to increase government revenues. Inflation is expected to pick up as a result of these measures. The Government is planning to issue Rs.500 billion worth Treasury bills to clear the circular debt. Although, necessary to reduce power shortage, this is expected to have an adverse impact on inflation and interest rates. These measures, though good for the country in the long-run, may dampen investment sentiments and we may see a stock market correction around budget time.

The general perception and hope is that the newly elected government will be better able to cope with the issues of governance, corruption, power shortages, and law & order situation, versus the previous one. This government is also expected to provide better facilitation and comfort to foreign investors to come and invest in Pakistan’s energy and other sectors. The benefits of these improvements will incur gradually over a 5-year period. We expect the economic growth rate to average 5% per annum over the next five years. Stock market is trading at an attractive price-to-earnings ratio of 8.3 times, corporate earnings growth is estimated at 19% for FY 13-14, and is expected to remain healthy thereafter as well. Consequently, we expect the stock market to continue to perform well in the coming years, delivering double-digit returns to investors.