

Political Euphoria – Light at the End of the Tunnel – II

In October 2007 I wrote: “Political Euphoria-Light at the End of the Tunnel” highlighting that the political uncertainty has overshadowed the positive economic stimuli prevalent in the market. Today we have witnessed the positive impacts of the results of the recent elections held in the country. The new government has taken charge and the political euphoria has peaked out. The tables have turned and the lack of good economic data is now overshadowed by better political outlook.

National Front: The State Bank of Pakistan has lowered its GDP growth forecast by approximately 0.5% in its latest economic report. This is due to the decelerated growth in the manufacturing segment of the economy. The services sector is still showing robust growth along with the agriculture sector. The increasing inflationary pressure has negatively impacted consumer spending and purchasing power. The imbalance in the current account deficit and the widening of the trade gap are alarming signs of further weakness. The impact of the rising prices of global commodities including oil prices has impacted our trade data negatively. We have witnessed a decrease in the foreign direct investment, FDI, as well as the foreign portfolio investment, FPI, as compared with previous year. All these economic numbers are indicating towards further tightening in the monetary policy by the central bank in the future leading to deeper deceleration in the growth of the manufacturing segment of the economy. Despite all these negative economic factors, KSE-100 index is currently at an all-time high level indicating investor exuberance due to the lack of political uncertainty.

International Front: Asian markets remained in focus due to the trickle-down impact of the sub-prime credit crisis of the U.S. economy. The weakening dollar and higher oil prices further added to the problems of Asian markets. The MSCI's measure of Asian stocks outside Japan dropped over 13 percent this quarter marking its worst performance since the quarter ended in September 2002. These losses have contrasted sharply with the double digit gains in the index in each of the previous five years. The rise in the international commodity prices along with food inflation will remain high in the near future due to supply-side constraints. The launch of new funds targeting commodities and the need to hedge has also led to higher commodity prices. International emerging market managers have reduced their equity exposure from the Asian markets due to the impact of the slow-down of the U.S. economy and the impact of the current financial crisis.

In the light of the recent national and international economic developments we advise our clients to remain focused on maintaining a constructive long-term portfolio with the right mix of equities and fixed income funds to outperform inflation in the long run.