Capital Markets –

Local view with International Perspective

Political cloud overshadowed the equity markets during the month of November. The announcement of state of emergency and then a series of events impacted the KSE-100 index negatively. The political scene witnessed signs of recovery with positive news from Islamabad as well as the stock market in Karachi. The market reacted positively on the clarity of Presidential elections and then the announcement of general elections in the country. The market also reacted positively to the news regarding the end of state of emergency in the country on December 16th 2007. We witnessed large outflows from the special convertible rupee account (SCRA) during the month indicating foreign portfolio investors exiting from the Pakistani capital markets amid the state of emergency. SCRA account declined from a level of almost $300 million to $80 million level, a decline of 73% on foreign portfolio investments for the fiscal year. With the improvement in the political conditions in the country, SCRA account also improved towards the end of the month indicating positivity in the foreign investor sentiment.

International markets also witnessed volatility after a long bullish run. The U.S. markets consolidated during the initial part of the month after large financial organizations reported heavy write-offs due to their sub-prime exposure. Oil prices peaked close to $100 per bbl before retreating below $90 on the back of large U.S. inventories. Recent comments by U.S. Federal Reserve Chairman Ben Bernanke indicated another quarter point cut in the U.S. interest rate leading to the extension of the Bull Run on Wall Street. Fed chairman Ben Bernanke said that resurgence in financial strains in recent weeks had dimmed the outlook for the U.S. economy and that the Fed would have to remain "exceptionally alert and flexible". The labor market was also witnessing a slow down following the housing market slump in the U.S.

European and Asian equity markets also witnessed Bull Run during the month. The pan-European FTSEurofirst 300 index reached a level of 1,522.42 points, after rising to 1,523.7, it's highest in two weeks with the financial stocks being the top gainers. Earlier in Asia, Tokyo's Nikkei average touched a three-week high while the MSCI's measure of other Asian stocks climbed to two-week highs towards the end of the month.

Typically, lower interest rates would make the dollar less attractive against other currencies but investors are now seeing rate cuts as a positive sign for the strength of dollar as a currency. The yen fell broadly towards the end of the month amid the extended recovery in equities. Gulf countries are also meeting to decide the future pegging of their currencies to the U.S. dollar. Keeping the decline in the U.S. currency in perspective, one must remember that the world's GDP is about $55 trillion in size, and the U.S. makes up 25% of it. U.S. buys and sells some $4 trillion in goods and services with the rest of the world each year and other countries will have to keep large amounts of dollar-based reserves.

Finally, we have to understand that higher international Oil prices and a weaker dollar will have an incremental impact on the inflationary pressure. It will also have a negative impact on our future economic growth. We should also take a look at the positives of our economy and can expect over 6% GDP growth during this fiscal year. Rising Oil prices and weaker dollar can be positive for the E&P sector along with the fertilizer and the banking sector. Based on 08 P/E our equity market is trading at over 25% discount to other Asian equity markets. All these factors should be taken into account in order to make a wise long-term investment decision through mutual funds.

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