

Faysal Asset Management

PSX reaction to PM disqualification..... “Political Skeptism & market volatility, what now?”

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Dear investors,

In a historic judgment, the five member bench of the Supreme Court (SC) disqualified Prime Minister, Mr. Nawaz Sharif (NS), and asked him to vacate the prime minister's position with immediate effect. The SC announced the decision on the Panama Leak, or alleged ownership of foreign assets by NS' family.

The decision is clearly a big development for the market though not completely surprising, in our view as we believe that ever since the report released by Joint Investigation Team (JIT) on 10th July, 2017, the market had already formed a consensus that PM will be ousted. With speculation hitting its peak ahead of the verdict, investors adopted a cautious approach in anticipation of the verdict announcement, and selling drove as the market opened down before posting a slight recovery.

We believe that the equity market reaction will largely be hinged upon the official reaction from the sitting government, whereby if they opt to choose the unlikely path of agitation then the continuation of uncertainty will keep Pakistan equities under pressure in the near term.

In case the PM concedes, and there is a smooth transition of power to another member of PML-N, then the receding uncertainty is likely to translate into a sharp rally in Pakistan equities.

The political uncertainty has opened up market valuations from current P/E of 9.7x (CY17E) to 8-8.5x, implying the index to trade in the range of 45,000-49,000 till Dec 2017.

In the meanwhile, growing concerns on PKR stability should tilt sector allocation towards industries that stand to benefit from PKR depreciation. We also expect depreciation of PKR over FY18, where we project the currency to close at PKR 111-114 against USD.

Local equity market seems to be gradually realizing the macro-economic headwinds. Our Research Head has been highlighting these risks for quite some time; even before the broader market correction set in. Interestingly, on the street we have just now started to see downgrade to the index targets for the year end as well.

Remember! Polarity or variance in fundamentals is usually much higher in Emerging markets as compared to developed markets which remain a challenge for Fund Managers looking for undervalued businesses in these select individual markets. It is quite true that each particular sector/ sub-sector or a company sometimes offer a unique blend of risk and return profile. ***Political noise, be that domestic or international, seems likely to stay for the next whole twelve months. So you've to bear with that. But, what is notable to realize is, it that could offer good trading opportunities though.***

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