

# MPS PREVIEW & EQUITY MARKET

Traders' strikes, further monetary tightening and Reko Diq case weighed on equity market

Monday, 15 July, 2019

After the elections of 2018, most of the political instability settled down and it was believed by the market participants that the economic uncertainty would also be over as soon as the government would finalize a bailout package with IMF. However, things didn't go as per the expectations of the investors. IMF imposed strict prerequisite conditions in order to provide financial support which severely hurt the investors' sentiment and caused them to pull out their capital from the equity market and park it in fixed income securities which can be seen in the dried volumes of the market nowadays. Furthermore, the traders' recent strike against the imposition of new taxes and the condition of seeking CNIC on sales of more than Rs50,000 also created uncertainty in the market. Lastly, the penalty of \$5.9bn imposed by world bank group on Pakistan in the Reko Diq case further added fuel to the fire as the country is already facing the deficiency of foreign exchange reserves. However, we expect the upcoming meeting of PM Khan with President Trump as the light at the end of the tunnel as it can be resulted into some waivers from tough conditions of IMF and FATF. Furthermore, the military aid to Pakistan can also be resumed after this meeting which would definitely impact the market in a positive way.

## Deadlock Between Government and Traders Over CNIC and Taxation Issues Could Get Worse If Not Addressed Wisely

A countrywide shutter-down strike was observed by traders on 13<sup>th</sup> July 2019 in all parts of the country in a protest against the "anti-business measures" taken by the federal government in the budget for the current financial year. On the other hand, FBR chairman Shabbar Zaidi said in response to the strike that the government would not compromise on enforcement of its condition regarding the Computerised National Identity Card (CNIC) numbers. Responding to this, the traders have announced that if the government does not agree to their terms, then protest is the only way forward and they would not file their tax returns until demands are met. In our view, documentation of the economy and bringing the traders into the tax net is beneficial as well as necessary for our economy but this should be done gradually and by negotiating and convincing all the stakeholders. Otherwise, the issue will further increase the financial instability into the country.

## 100-125 bps To Be Increased In Upcoming Monetary Policy

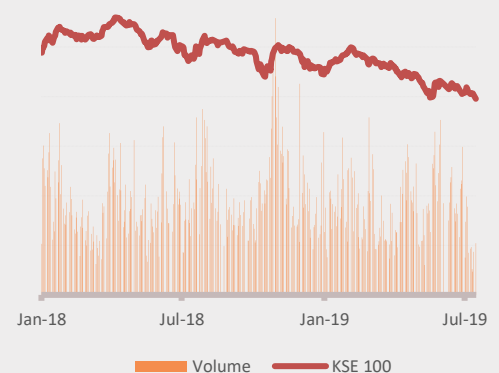
Earlier in May-19, when the SBP raised the interest rate by 150 bps to 12.25%, it was generally assumed that the policy rate has reached its peak as the expected inflation for the year remained under double digits and it was perceived that the IMF condition has also been fulfilled by that raise. However, the recent staff report issued by the IMF further suppressed the investors' sentiment as the fund predicted 13% inflation rate for FY20 and asked to correct the macroeconomic imbalances through appropriate monetary policy. This statement created the sentiment for a further rate hike and to get a healthy response in upcoming MTB and PIB auctions, the SBP has decided to announce the monetary policy for coming two months on Tuesday, 16<sup>th</sup> July 2019 (just one day before the MTB auction). In this regard, we expect the SBP to raise the interest rate by 100-125 bps in tomorrow's monetary policy, the impact of which has already been incorporated in our view.

## Negotiated Settlement Is The Only Way Out in Reko Diq Case

On Friday, 15<sup>th</sup> July 2019, an arbitration tribunal of the World Bank's International Centre for Settlement of Investment Disputes (ICSID) awarded about \$5.9bn in

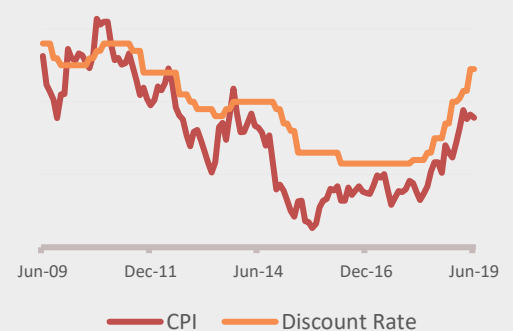
### Key Statistics

KSE 100 Performance



Sources: ACPL Research, PSX

CPI vs Discount Rate



Sources: ACPL Research, PBS, SBP

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## Key Statistics

damages to TCC in arbitration claims it filed against Pakistan following the denial of a mining lease for the Reko Diq project in Pakistan in 2011. After the decision, Tethyan Copper Company (TCC) said on Sunday, 14<sup>th</sup> July 2019 that they remain willing to discuss the potential for a negotiated settlement with Pakistan and will continue to protect their commercial interests and legal rights until the conclusion of this dispute. Prior to the denial of the mining lease application, TCC had completed a feasibility study showing that Reko Diq was one of the world's largest undeveloped copper and gold deposits, and had a potential mine life of over 50 years and an estimated initial capital investment of over \$3bn. In our view, the only way out for Pakistan in the current situation is to negotiate a settlement with the company and as mentioned earlier, the company is also willing to negotiate with Pakistan, we expect the negotiations to remain successful, the Reko Diq project would be resumed with the same company and Pakistan would be able to avoid the penalty after successful negotiations.

### **PM Khan's Upcoming Visit To USA Would Remain Under Limelight In Hope Of Positive Developments**

PM Khan will meet the US president on 22<sup>nd</sup> July 2019 on the invitation of President Trump. During the premier's visit, important matters of the region would be discussed as relations between both countries are the need of the hour for promoting peace in Afghanistan. As we know that the US wants military withdrawal from Afghanistan and for that, it wants Pakistan to play a role of mediator in this process. Therefore, we expect Pakistan to get some benefits in return of offering its services such as waivers from some strict conditions of IMF, Withdrawal of Pakistan's name from FATF's grey list in next meeting scheduled in October 2019 and the resumption of military aid which was suspended in January 2018 as the president Trump accused Islamabad of allowing the Taliban to use its territory for attacks in Afghanistan.

### **Market Strategy And Preferred Sectors**

The market has already incorporated the impact of most of the issues currently prevailing in the country. However, any further hike in interest rate other than tomorrow would further put pressure on the market and cause the investors to leave the equity market for some time in order to enjoy high-risk free returns. On the other hand, if our predictions regarding PM Khan's US visit comes true then we might see a good recovery in the market with improved volumes. We advise our investors to BUY on dips and adopt a long-term investment strategy in order to secure reasonable returns. Our preferred sectors include Oil and Gas Exploration, Banks, Textiles, IT, and Fertilizers. Furthermore, we advise our investors to avoid Cements, Steel, and Autos, until our further recommendation, due to their cyclical nature.

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<b>TP</b>	Target Price	<b>CAGR</b>	Compound Annual Growth Rate	<b>FCF</b>	Free Cash Flows
<b>FCFE</b>	Free Cash Flows to Equity	<b>FCFF</b>	Free Cash Flows to Firm	<b>DCF</b>	Discounted Cash Flows
<b>PE</b>	Price to Earnings Ratio	<b>PB</b>	Price to Book Ratio	<b>BVPS</b>	Book Value Per Share
<b>EPS</b>	Earnings Per Share	<b>DPS</b>	Dividend Per Share	<b>ROE</b>	Return of Equity
<b>ROA</b>	Return on Assets	<b>SOTP</b>	Sum of the Parts	<b>LDCP</b>	Last Day Closing Price

## VALUATION METHODOLOGY

To arrive at our Target Price, Abbasi & Company (Private) Limited uses different valuation methods which include:

- I. Discounted Cash Flow Model
- II. Dividend Discount Model
- III. Relative Valuation Model
- IV. Sum of Parts Valuation

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HOLD	Between -5% to 15%
SELL	Less than and equal to -5%

Sector Rating	Sector Outlook
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Market Weight	Neutral
Underweight	Negative

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