8 Capital Markets

Pakistan's capital markets have seen substantial improvement over the last four years (see **Table 8.1**). In the Karachi Stock Exchange (the leading equity market) despite a reduction in the number of listed companies, the listed capital has risen by one third and, the market capitalization of the KSE has risen by an impressive 59.8 percent, while the average daily turnover volume surged by over 82.4 percent, during the last two years. Similarly, the corporate debt market had also seen significant improvement with the value of outstanding listed issues increasing by 99.0 percent during the same period.

Table 8.1: Overview of Capital Market

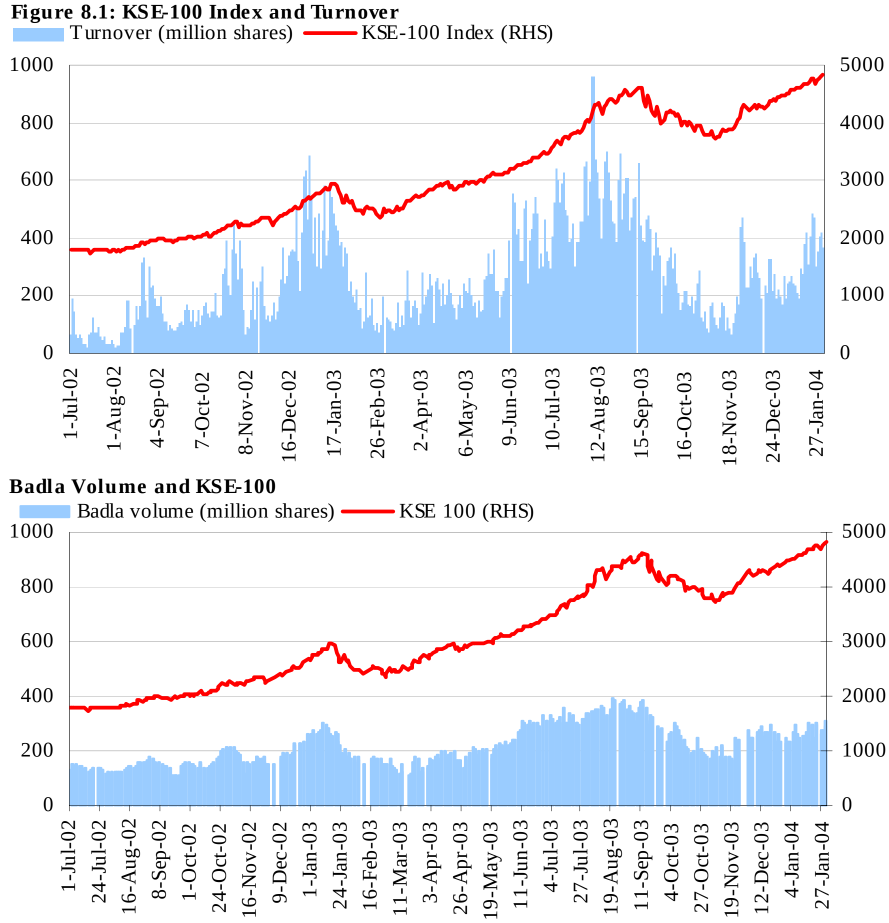
Equities (KSE)		**CY00**	**CY01**	**CY02**	**CY03**
Listed Companies	numbers	741	747	711	701
Listed Capital	billion Rs	237	236	291	313
Market Capitalization	billion Rs	383	296	595	951
New Companies Listed	numbers	3	3	4	6
New Listed Capital	billion Rs	2	2.9	6.3	4.6
Debt Instruments (all listed)					
New Debts Instruments Listed	numbers	6	17	18	15
Amount	billion Rs	1.2	12	9.7	6.2
KSE–100 Index (Nov 1, 1991=100)					
High		2054.4	1550.4	2701.4	4606.0
Low		1276.1	1075.2	1322.1	2356.5
Turnover (KSE)					
Average Volume per Day (shares)	billion	0.19	0.10	0.17	0.31
Total Value	billion Rs	1750	746	1483	3841

This exceptional performance of the capital markets in Pakistan is not surprising given the huge growth in rupee liquidity and the consequent availability of cheap credit that: (1) inflated the assets prices and offered lucrative capital gains to the investors in equity markets, and (2) reduced financial charges and increased profitability for corporates. In addition, the last four years witnessed a recovery in the economy, which helped improve corporate profitability and investor confidence. These factors have continued to drive the equity market, in particular, during Q2-FY04 as well.

8.1 KSE Performance during Q2-FY04

Q2-FY04 witnessed an equity market rebound in November 2003 (see **Figure 8.1**) after a large and extended correction (that had started in mid-September 2003) on the back of: (1) positive developments on the political front (the ceasefire proposal and resumption of air and road links with India; and the resolution of LFO issue)

Figure 8.1: KSE-100 Index and Turnover



as well as (2) on the economic front (the S&P upgrade of Pakistan's credit rating, and expectations of very good corporate results).[1,2]

[1] Besides highly leveraged holdings, the delay in PSO privatization, change in COT regulations, SBP regulation to limit the banks investments in the equity market, PTCL decision to cut the line rent and installation charges, and SBP proposal of replacing badla financing with margin financing were the major factors in keeping the bears in the market during October-November 2003. Specifically, the KSE-100 index fell to 3732.3 on November 6, 2003 from its peak at 4606.0 on September 12, 2003.

[2] In January-February 2004, the market rally gained further momentum and the KSE-100 index almost touched the 5000 mark.

8.2 Market Movers

The share of top ten scrips in total market turnover increased significantly from 67.2 percent in October 2003 to 71.1 percent in December 2003, primarily reflecting a strong co-movement of trading in these scrips with the total market turnover that increased from 4934.3 million shares to 6088.0 million shares in the respective months (see **Table 8.2**).

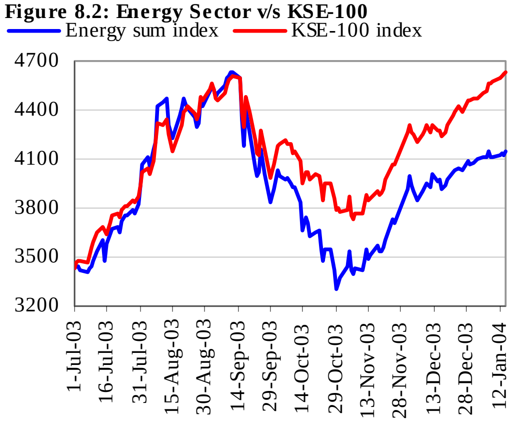
Table 8.2: Top 10 Symbols during Q2-FY04*
million shares

December 2003		November 2003		October 2003	
Symbol	**Turnover**	**Symbol**	**Turnover**	**Symbol**	**Turnover**
DGKC	576.7	FFBQ	327.5	PSOC	612.7
HUBC	552.7	DGKC	220.1	PTC	530.1
PTC	530.4	PSOC	191.2	HUBC	426.3
FFBL	525.6	PTC	178.9	DGKC	408.9
PSOC	424.6	HUBC	170.5	FFCJ	278.1
MPLC	423.5	BOSI	79.0	FCCL	249.6
NBPL	336.2	TRG	67.0	DSFL	245.5
FCCL	331.4	FCCL	66.8	PPTA	212.3
PAKO	326.7	MPLC	65.7	NBPL	199.6
PIAC	302.9	DEML	65.3	MPLC	150.2
Share in Total	71.1		67.0		67.2

* Source: KSE website (www.kse.net.pk)

As shown in **Figure 8.2**, interest in the energy sector stocks was an important factor in the movements of the KSE-100 index during Q2-FY04 e.g. reports of a delay in the privatization process for PSO (apart from other factors) contributed to the decline of the KSE-100 during initial part of Q2-FY04. Similarly, the market rally in mid-November 2003 onwards was led by investor interest in energy sector scrips such as Pakistan Oil Fields and Hubco (amid expectations of an exceptional result

Figure 8.2: Energy Sector v/s KSE-100



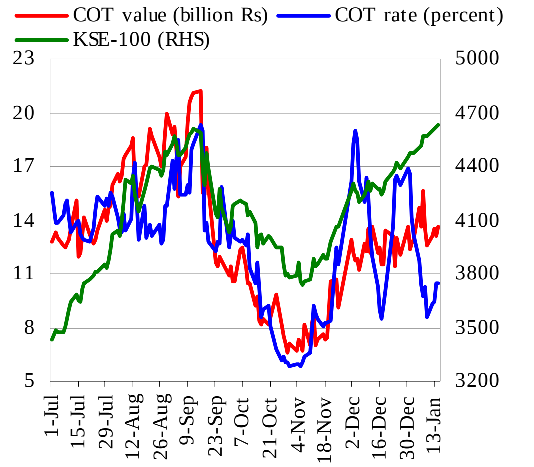
*The Energy Index is calculated by taking market capitalization of energy sector for July 1, 2003 as base (3432), and tracking the relative changes in the market capitalization of energy stocks afterwards.

announcement) and PSO (in anticipation of early privatization).

8.3 COT (Badla) Financing

Figure 8.3 clearly depicts the pivotal role of the badla financing in the KSE movements. As discussed in preceding SBP quarterly report, the large weak holdings and the very high badla rates were probably important contributors to the extended market correction that began in September 2003. Not surprisingly, the continued decline of the market gradually forced a decline in the outstanding badla volume as well as the financing rate, until the reversal of the downtrend, early in November 2003.

Figure 8.3: COT (Badla Market)



The badla values then bounced back quickly as the market surged in November 2003, but the pace of the rise then moderated during December 2003, as the Ramadan reduced market activity. Nevertheless, average badla volume, value and rate fell during Q2-FY04 compared with the preceding quarter; this is consistent with the overall decline in the trading volumes in the KSE (see **Table 8.3**).

Table 8.3: COT Market Summary

	Volume (million shares)	**Value** (billion Rupees)	**Rate** (percent)
		Q1-FY04	
Average	333.1	15.7	14.6
Max	391.2	21.2	19.3
Total	19,986.8	942.4	-
		Q2-FY04	
Average	230.8	10.1	11.0
Max	306.4	13.6	19.0
Total	13,387.9	584.4	-

8.4 Corporate Earnings[3]

Corporate results have shown a tremendous improvement during 2003 compared with the preceding year. As reported in **Table 8.4**, the earnings data for the top 30 companies on the basis of profit after tax (PAT), earnings per share (EPS),

[3] Based on results announced till February 19, 2004 (530 companies).

dividends, yield, and market value reflects a marked improvement in corporate performance compared with the preceding year. In fact, PAT, EPS and Cash dividends have posted a healthy improvement in all analysis.

Table 8.4: Earning Performance of Top 30 Companies*

	PAT *(million Rs)*	EPS *(Rupees)*	Cash div. *(percent)*	Bonus div. *(percent)*
on PAT basis				
2003	65843.5	6.1	40.6	1.5
2002	55760.6	5.1	33.8	1.7
Growth	*18.1*	*18.1*	*20.1*	*-15.6*
on EPS basis				
2003	21313.0	25.3	128.3	6.4
2002	14108.3	16.8	80.6	3.3
Growth	*51.1*	*51.1*	*59.1*	*91.9*
on dividend basis				
2003	23813.9	19.7	126.7	5.5
2002	18094.7	15.0	88.0	4.2
Growth	*31.6*	*31.6*	*44.0*	*30.0*
on yield basis				
2003	8211.0	4.3	39.5	1.5
2002	8142.5	4.2	51.6	0.0
Growth	*0.8*	*0.9*	*-23.4*	-
on market value basis				
2003	54061.8	5.6	29.7	0.9
2002	37575.8	1.8	24.9	1.1
Growth	*43.9*	*206.5*	*19.2*	*-22.7*

A sectoral 2003 earnings performance based on 530 KSE listed companies shown in **Table 8.5.** The top-performing sector is the oil *and gas exploration* sector with a massive EPS of Rs 19.4. The weak performance of *textile spinning* is a puzzling given the significantly improved export performance (see **Section** on **Trade Account**).

The performance of *cement* and *power generation & distribution* sectors was however relatively poor. This was despite the fact that DG cement and Hub Co performed very well within their respective sectors.[4] In fact, both DG cement and Hub Co were amongst the top performing stocks in the KSE.

Table 8.5 Comparative Performance of Selected Sectors

Sector	No. of Results	EPS (Rs)	PER (x)	DPS (Rs)	Yield (%)
Banks	6	6.1	6.8	1.8	4.3
Textile spinning	105	1.5	11.4	0.4	2.3
Oil and gas market	6	6.4	13.2	4.6	5.5
Oil and gas exp.	2	19.4	9.9	14.3	7.5
Cement	21	-	-	0.3	1.6
Auto assembler	8	11.1	6.7	4.0	5.4
Tech. and comm.	6	4.3	9.0	3.3	8.5
Power gen. and dist.	12	-0.1	-	0.7	5.7
All sectors	**530**	**2.5**	**12.2**	**1.8**	**5.7**

8.5 New Floatation, Mergers and De-listings

As expected given the robust equity market, new floatation has also shown some

[4] Heavy losses to KESC (Rs 8.3 billion) accounted for the bulk of losses in the *power generation and distribution* sector. In fact, only 2 other companies incurred losses and the rest earned higher profits compared with 2002.

improvement. Specifically, against floatation of 4 companies last year, 2003 witnessed floatation of 9 companies. However, out of these 9 companies 2 floatations were a result of mergers and 2 floatations were disinvestments of government stocks of the respective organizations (see **Table 8.6**).

Table 8.6: New Floatation (2003) - KSE

million Rupees

Company	Present issue	Subscribed	Premium	Total
Ittehad Chemicals Limited *Direct*	62.5	39.9	48.4	88.3
TRG Pakistan Limited ***(A - Class)***	200.0	1,121.9	-	1,121.9
Mashreq Bank Pakistan Limited *				-
Pakistan International Container Terminal Ltd.	160.0	1,340.7	-	1,340.7
National Bank Of Pakistan Limited	131.3	1,222.3	956.7	2,179.0
First National Bank Modaraba	100.0	121.1	-	121.1
NDLC - IFIC Bank Limited **				-
Oil & Gas Development Company Limited	2,150.5	8,787.7	19,330.6	28,118.4
World CALL Broadband Limited***	300.0	-	-	-
Total	**3,104.3**	**12,633.7**	**20,335.8**	**32,969.4**

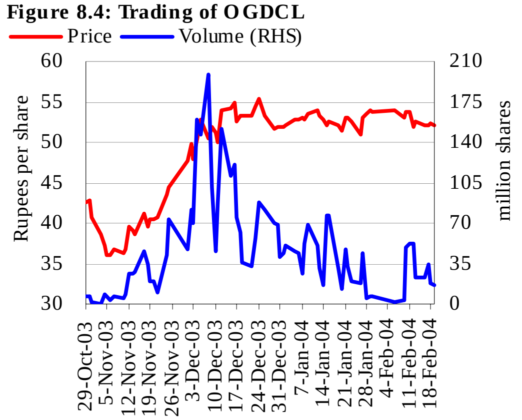
* The Bank was listed without public offering due to merger of Crescent Investment Bank and Pakistan branches of Mashreq Bank

** The Bank was listed without public offering due to merger of National Development Leasing Corporation Limited

*** Prospectus released in December 2003 while formal subscription on 07-08 January 2004

Encouragingly, most issues were heavily subscribed. The biggest flotation of the year was of OGDCL in October 2003 that resulted in total proceeds of Rs 28.1 billion against an issue of Rs 2.2 billion, reflecting huge public interest despite a bearish spell in equity market at that time. Specifically, the level of over-subscription was almost 7 times.

Figure 8.4: Trading of OGDCL



As shown in **Figure 8.4**, the share price of OGDCL reflects a steep hike during November-December 2003, showing the exceptional capital gain accrued by the successful subscribers. The success of new floatation during 2003 would encourage other companies to get listed in near future. Moreover, the privatization of some other public sector corporation is likely to get similar response to that of OGDCL.

Table 8.7 Mergers during 2003

	Name of company	New name of the company merged with	Date	Ratio
1	Orient Insurance Company Ltd.	Business & Industrial Insurance Co. Ltd.	22-Jan	1.08: 1.0
2	Nafees Cotton Mills Limited	Legler - Nafees Denim Mills Limited	29-Jan	1.0: 4.1
3	KASB & Company Limited	KASB Bank Limited	04-June	1.0: 2.3
4	Crescent Investment Bank Limited	Mashreq Bank Pakistan Limited	09-July	1.0: 2.4
5	First Crescent Modaraba	First Standard Investment Bank Ltd.	31-July	1.0: 3.0
6	First Professional Modaraba	Al-Zamin Leasing Modaraba	01-Aug	1.0: 1.0
7	PEL Appliances Limited	Pak Electron Limited	30-Aug	1.0: 0.14
8	NDLC (Rs. 5 per share)	IFIC Bank Limited (Rs. 10 per share)	17-Oct	1.0: 1.18

Source: KSE website (www.kse.net.pk)

The **Table 8.7** shows that 8 mergers took place during 2003 compared with 12 mergers in 2002. The biggest merger of 2003 (paid up capital Rs 500.3 million) was between CIBL and MBLP in July 2003.

The number of companies de-listed fell sharply from 24 in 2002 to 8 in 2003 (see **Table 8.8**). Similarly, average paid-up capital of de-listed companies in 2003 was only Rs 33.0 million against Rs 89 million for the preceding year.

Table 8.8 De-listings during 2003

	Company	Date
1	Burma Oil Mills Limited *	10-Feb
2	National Tanneries of Pak Ltd.*	24-Mar
3	Hilal Flour & General Mills Ltd.*	24-Mar
4	Latif Cotton Mills Ltd.*	30-Apr
5	Asia Board Industries Ltd.*	30-Apr
6	Universal Leather & Footwear Ind. Ltd.*	12-May
7	Souvenir Tobacco Co. Ltd.*	17-Jun
8	Elite Publishers Limited*	9-Dec

* De-listed after completing formalities of buy back of shares.

Source: KSE website (www.kse.net.pk)

8.6 Corporate Bond Market

The total stock of outstanding listed corporate debt increased to Rs 30.9 billion at end-December 2003 (comparable figure for FY03 was Rs 25.0 billion). Despite an increase of 24 percent, the size of the listed corporate debt market remained less than one percent of GDP.

Table 8.9 Corporate Debt Profile

amount in billion Rupees

	No. of new issues	Amount
FY02	17	10.1
FY03	22	10.7
Q1-FY04	2	1.3
Q2-FY04	3	1.3
H1-FY04	*5*	*2.6*
*Total Outstanding**	*57*	*30.9*

*end-December 2003

As visible in **Table 8.9**, few debt issues are evident in H1-

FY04 compared to the corresponding period last year. A possible reason for this is the aggressive marketing by banks to fund corporate long-term borrowing needs.

8.7 Mutual Funds

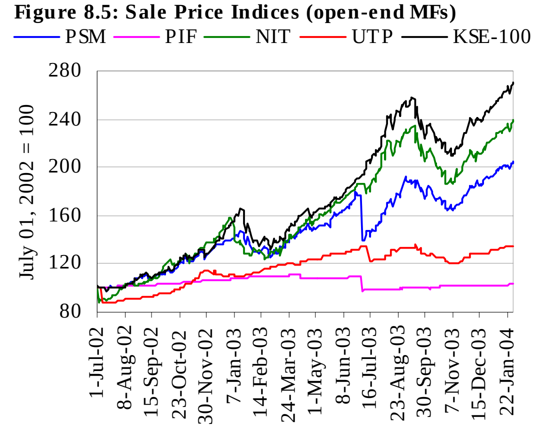
As reported in **Table 8.10**, there are 23 mutual funds operating in Pakistan, 9 open-end and rest closed-end. Only one fund (NIT) is under public sector management and rest are under private sector fund management companies.

Open-end

As in Q1-FY04, the NAVs of open-end mutual funds continue to follow the KSE-100 trends during Q2-FY04.

As shown in **Figure 8.5**, the sale price indices of major open-end funds fell between September 2003 and early-November 2003 before rebounding and getting to new respective peaks. The relative change of stock market fund seems be less than the relative change in KSE-100 index, indicating an under-performance by these funds compared with the overall market KSE-100 performance since July 2002. Also, not surprisingly, the funds with large fixed income investments are less correlated with the KSE-100.

Figure 8.5: Sale Price Indices (open-end MFs)



Closed-end[5]

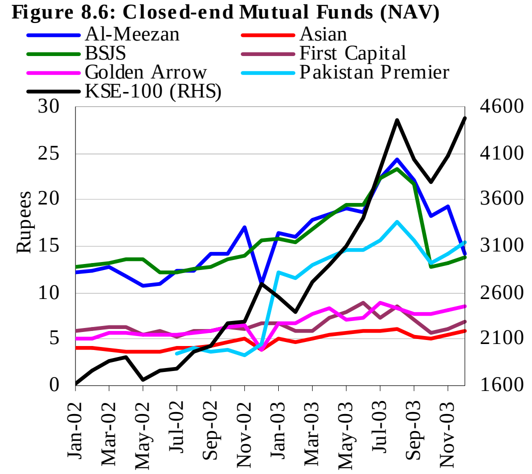
The closed-end mutual funds performed exceptionally well during 2003 with a growth of 155.6 percent in the PAT.[6] The earning per share also increased from

[5] Closed-end mutual funds are those where the shares are initially offered to the public and are then traded in the secondary market. The trading usually occurs at a slight discount to the NAV. The history of closed-end mutual funds dates back to 1966, when Investment Corporation of Pakistan (ICP) offered a series of closed-end mutual funds. There are two set of rules governing mutual funds in Pakistan, which are: (1) Investment Companies and Investment Advisors' Rules, 1971, governing closed-end mutual funds, and (2) Asset Management Companies Rules, 1995, governing open-ended mutual funds

Rs 2.4 in 2002 to Rs 6.1 in 2003. Moreover, against *zero* dividends last year, 2003 witnessed dividend pay outs as well as a rise in NAVs (see **Figure 8.6**).

This is not surprising given the substantial expansion in the equity market in Pakistan during the last two years. The NAVs of selected closed-end mutual funds[7] clearly follow the KSE-100 movements.[8] However, the intensity of co-movement with KSE-100 index varies from fund to fund due to: (1) the type of fund (e.g. balanced, equity), and (2) portfolio of stocks and bonds in the fund.

Figure 8.6: Closed-end Mutual Funds (NAV)



[6] Based on corporate results announced since February 19, 2003.
[7] Source: Mutual Funds Association of Pakistan (www.mufap.com)
[8] Al-Meezan fund and BSJS balanced deviated from the market trend in September and October 2003 respectively, due to announcement of right issues. The issuance of right shares results in an increase in number of outstanding shares and decreases the NAV.