

INVESTMENT PROCESS IN PAKISTANI CAPITAL MARKETS

By

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Positive Side of
Capital Formation through
Secondary Markets Listed
Equities

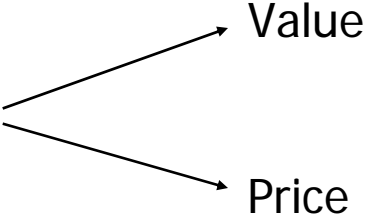
Investment Process

- Objective
- Asset Allocation
- Security Selection
- Risk Tolerance

Why Have a plan?

To be aware of the variables...

Effects of Secondary Market Listings

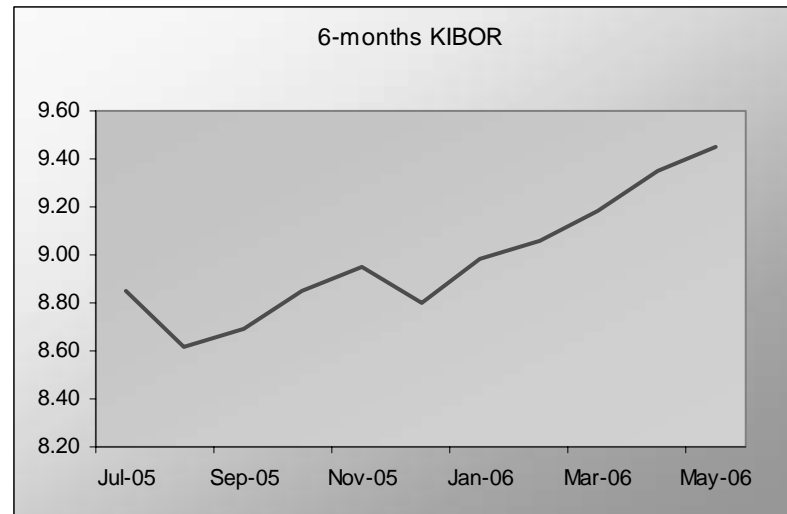
- Actual vs. Perceived
 - Risk Sharing
 - RoI vis-à-vis RoE
 - Better Governance
 - Easy access to Capital : Lower Cost
- 
- ```
graph LR; A[Actual vs. Perceived] --> B[Value]; A --> C[Price]
```
- The diagram shows a central point from which two arrows branch out to the right. The top arrow points to the word 'Value' and the bottom arrow points to the word 'Price'. This indicates that the concept of 'Actual vs. Perceived' is related to both 'Value' and 'Price'.

# Prices vs. Values

- Prices are driven by liquidity
- How do you price liquidity in the system?

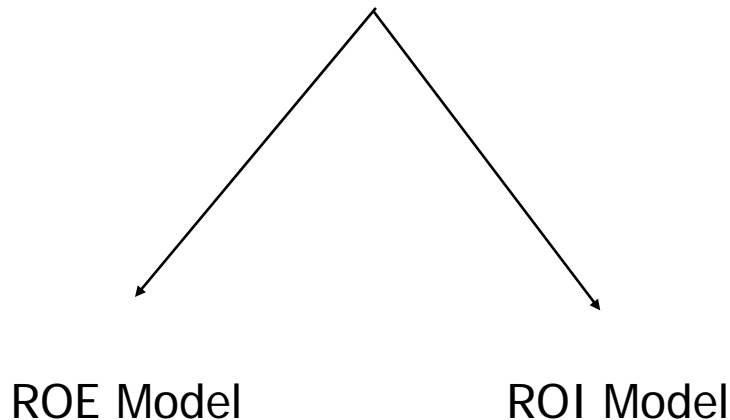
# Liquidity is determined by

- Size of the liquid funds vis-à-vis the free float of the market
- Price of the liquid funds with short-term interest rates



# Value

- Value is in the eyes of the beholder
- How to manage a portfolio of equities in an active market where prices fluctuate



# Trading Activity creates Prices through

- Noise
- Information



They create volatility



Leads to Risk in the market



# Structure of a Transaction

- To Identify and Manage risk
- Basic Risk Equation:

$$E(r_i) = r_f + \beta_{im} \{ (E(r_m) - r_f) \}$$

$E(r_i)$  = Return on the Capital Asset

$r_f$  = Risk-free rate of return

$\beta_{im}$  = The Relevant Risk of the asset

$(E(r_m) - r_f)$  = Market Risk Premium

# The Relative Risk

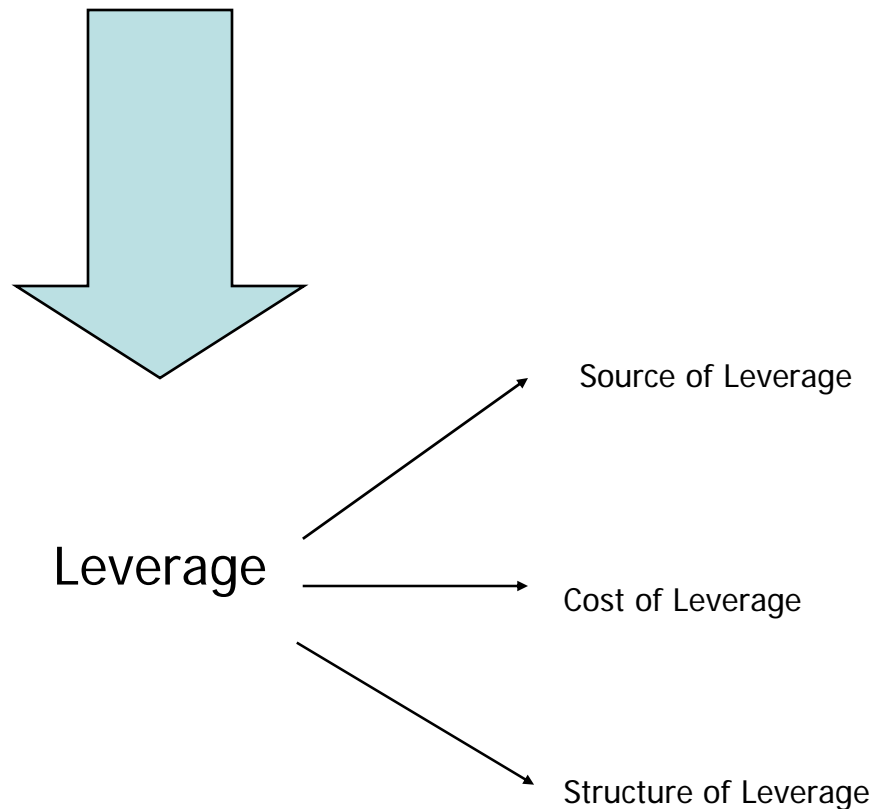
- Beta is the sensitivity of the asset returns to the market returns
- What is market risk?

$$\beta_{im} = \text{Cov}(r_i, r_m) / \text{Var}(r_m)$$

Drawback of the model: Risk tolerance of all investors is assumed to be uniform

# Market Risk

- How do you identify risk in the market?



# Capital Structure of a Corporate Entity

- The Capital Structure of an entity identifies the risk vis-à-vis the business model.
- How resilient is the structure to withstand the unexpected pressures exerted by the external and internal (economic) forces.

# The Market at 11,500...

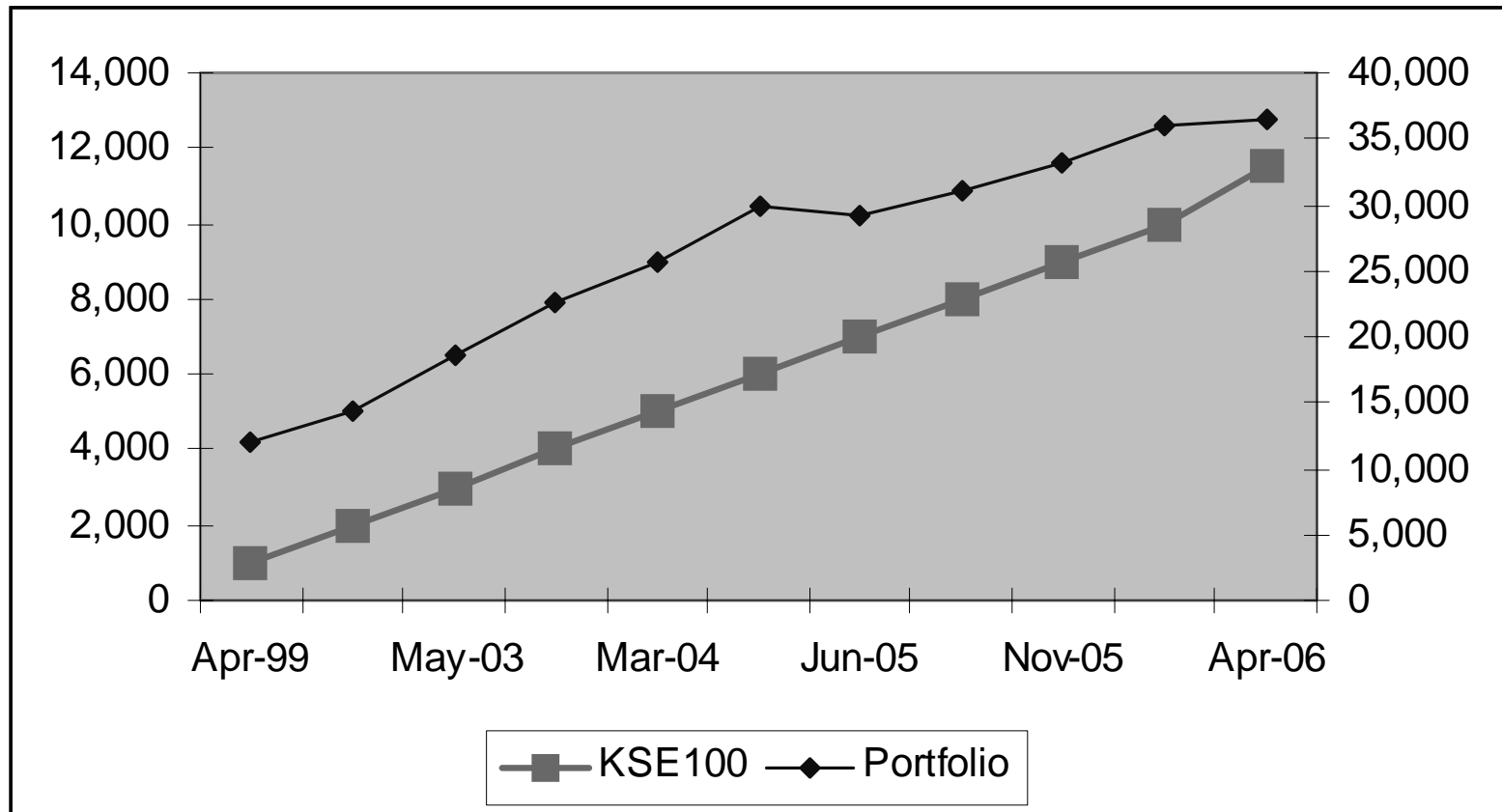
- Listed Companies: 666
- Market Capitalization: \$53.98 billion
- Average Volume: 325.35 million shares

Par value of most of the shares is Rs.10.

# Value at 11,500 Index

- Rs.36,361
  - 666 Companies
  - Food & Personal Care = 15.17%
- 
- With 100 shares/Company: Rs.3,636,100
  - With 500 shares/Company: Rs.18,180,500

# Value of Portfolio & KSE100



# Value and KSE100 cont'd...

| <b>KSE100</b> | <b>Portfolio</b> |
|---------------|------------------|
| <b>1,000</b>  | <b>Rs.11,937</b> |
| <b>2,000</b>  | <b>Rs.14,280</b> |
| <b>3,000</b>  | <b>Rs.18,693</b> |
| <b>4,000</b>  | <b>Rs.22,700</b> |
| <b>5,000</b>  | <b>Rs.25,764</b> |
| <b>6,000</b>  | <b>Rs.29,799</b> |
| <b>7,000</b>  | <b>Rs.29,110</b> |
| <b>8,000</b>  | <b>Rs.30,963</b> |
| <b>9,000</b>  | <b>Rs.33,144</b> |
| <b>10,000</b> | <b>Rs.36,117</b> |
| <b>11,500</b> | <b>Rs.36,361</b> |



# Summary of Value & KSE100

91.30 % drop in KSE100 (11,500 to 1,000)  
makes the value of our portfolio fall by  
67.17%

# Par vs Capitalization Matrix

KSE100: 11,500

|                  | Number | Par-Value (In Rs) | Value (In Rs.) |
|------------------|--------|-------------------|----------------|
| Less than par    | 232    | 2,300             | 1,086          |
| Greater than par | 434    | 4,009             | 35,276         |
| Total            | 666    | 6,309             | <b>36,361</b>  |

# Par vs Capitalization Matrix

KSE100: 10,000

|                  | Number | Par-Value (In Rs) | Value (In Rs.) |
|------------------|--------|-------------------|----------------|
| Less than par    | 227    | 2,250             | 1,121          |
| Greater than par | 399    | 4,029             | 34,996         |
| Total            | 626    | 6,279             | <b>36,117</b>  |

# Par vs Capitalization Matrix

KSE100: 9,000

|                  | Number | Par-Value (In Rs) | Value (In Rs.) |
|------------------|--------|-------------------|----------------|
| Less than par    | 238    | 2,355             | 1,107          |
| Greater than par | 383    | 3,874             | 32,037         |
| Total            | 621    | 6,229             | <b>33,144</b>  |

# Par vs Capitalization Matrix

KSE100: 8,000

|                  | Number | Par-Value (In Rs) | Value (In Rs.) |
|------------------|--------|-------------------|----------------|
| Less than par    | 248    | 2,455             | 1,139          |
| Greater than par | 373    | 3,774             | 29,825         |
| Total            | 621    | 6,229             | <b>30,963</b>  |

# Par vs Capitalization Matrix

KSE100: 7,000

|                  | Number | Par-Value (In Rs) | Value (In Rs.) |
|------------------|--------|-------------------|----------------|
| Less than par    | 249    | 2,465             | 1,155          |
| Greater than par | 376    | 3,804             | 27,955         |
| Total            | 625    | 6,269             | <b>29,110</b>  |

# Par vs Capitalization Matrix

KSE100: 6,000

|                  | Number | Par-Value (In Rs) | Value (In Rs.) |
|------------------|--------|-------------------|----------------|
| Less than par    | 208    | 2,060             | 1,116          |
| Greater than par | 407    | 4,109             | 28,683         |
| Total            | 615    | 6,169             | <b>29,799</b>  |

# Par vs Capitalization Matrix

KSE100: 5,000

|                  | Number | Par-Value (In Rs) | Value (In Rs.) |
|------------------|--------|-------------------|----------------|
| Less than par    | 252    | 2,490             | 1,281          |
| Greater than par | 368    | 3,739             | 24,483         |
| Total            | 620    | 6,229             | <b>25,764</b>  |



# Par vs Capitalization Matrix

KSE100: 4,000

|                  | Number | Par-Value (In Rs) | Value (In Rs.) |
|------------------|--------|-------------------|----------------|
| Less than par    | 284    | 2,805             | 1,215          |
| Greater than par | 363    | 3,694             | 21,485         |
| Total            | 647    | 6,499             | <b>22,700</b>  |

# Par vs Capitalization Matrix

KSE100: 3,000

|                  | Number | Par-Value (In Rs) | Value (In Rs.) |
|------------------|--------|-------------------|----------------|
| Less than par    | 297    | 2,955             | 1,289          |
| Greater than par | 331    | 3,364             | 17,404         |
| Total            | 628    | 6,319             | <b>18,693</b>  |

# Par vs Capitalization Matrix

KSE100: 2,000

|                  | Number | Par-Value (In Rs) | Value (In Rs.) |
|------------------|--------|-------------------|----------------|
| Less than par    | 387    | 3,835             | 1,537          |
| Greater than par | 275    | 2,809             | 12,742         |
| Total            | 662    | 6,644             | <b>14,280</b>  |

# Par vs Capitalization Matrix

KSE100: 1,000

|                  | Number | Par-Value (In Rs) | Value (In Rs.) |
|------------------|--------|-------------------|----------------|
| Less than par    | 488    | 4,825             | 1,908          |
| Greater than par | 264    | 2,629             | 10,029         |
| Total            | 752    | 7,454             | <b>11,937</b>  |

# Conclusion

- Believe in an asset class: “Equities in the long-term beat other investments”
- Spread your buying over a period of time, say 10 years
- Invest on a regular basis with a solid plan
- Invest small
- Disinvest once you achieve your target zone
- “No Illusion of control”
- The Market is always right.