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## Why is a new index needed?

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**FACT FILE**

## Why is a new index needed?

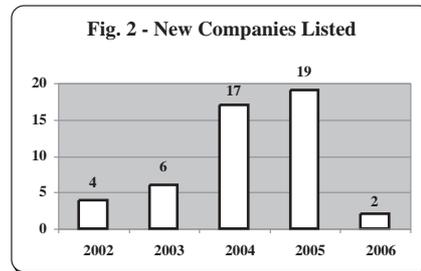
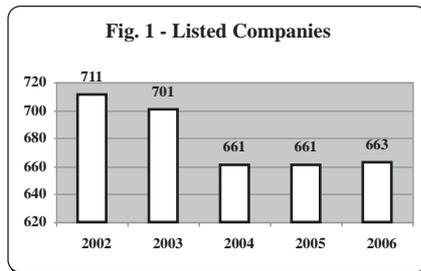
Shama Ahmed

The **Karachi Stock Exchange** is the largest of three stock exchanges in Pakistan. Generally the price trends in the stock markets are shown by an index which is also taken as a measure of the performance of the market. Initially to judge the performance of Karachi Stock Exchange, 50 shares index was introduced but it became non-representative with the increase in the market size. On November 1, 1991, KSE-100 was introduced which is the most generally accepted measure of the Exchange.

The KSE-100 is a capital weighted index and consists of 100 companies representing about 86 percent of market capitalization of the Exchange.

In 1995 to support the KSE-100 Index, the KSE-All Share Index was launched but KSE-100 remains the most acceptable measure of the market activity.

### Dynamics of KSE:



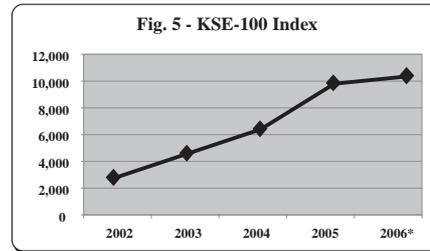
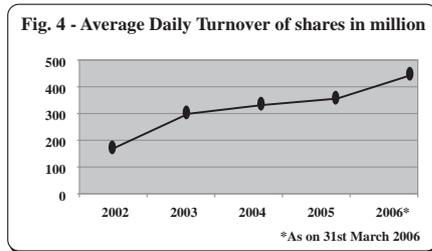
Source: <http://www.kse.com.pk>

As of May 2006, the number of listed companies is 663, which has been quite consistent over the years as shown in Fig. 1, with the addition of only 2 companies in 2006 depicted by Fig. 2.



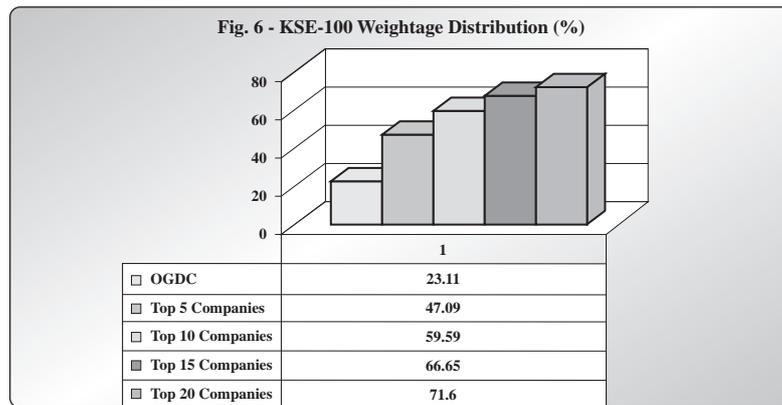
As depicted by Fig. 3, the market capitalization has increased phenomenally over the years which cannot be attributed to increase in the number of companies. The average daily turnover has also increased over the period.

**Why is the KSE-100 Index distorted?**



The KSE-100 Share Index has shown a marked improvement in terms of activity which is shown by the rising trend in the index points. The index weightage in the market is nearly 86%. As the index is based on market capitalization so the companies enjoying high market capitalization capture the index. The distribution of the companies' weightage in the index is given in Fig. 6 which clearly shows the distortions caused by the index calculation.

It can be seen from Fig. 6 that OGDC<sup>1</sup>, has the highest market capitalization and enjoys 23.11% of the total KSE-100 Index capitalization. This is too high a weightage given to one scrip and causes distortions in terms of market movements<sup>2</sup>. Top 5 companies, OGDC, PTCL, NBP, PPL and MCB, are representing almost 49% of total index weightage. KSE-100 index has been a target of criticism for its asymmetry. Even a trivial change in prices of a few of heavyweight stocks changes the direction of the market.



KSE-All Shares Index is not generally an acceptable measure of the market movement and hardly used to track market changes.

<sup>1</sup>Oil and Gas Development Company

<sup>2</sup>The data is for May 24, 2006 taken from KSE Website.

It can be concluded from the above cursory look at the indices dynamics that a new index is urgently needed which should be a representative of the market. A meeting of the board of directors of the Karachi Stock Exchange on Thursday, May 11, 2006 was conducted and decision was taken to implement the KSE-30 index from July 1.

The proposed index – KSE-30 Share Index is based on the following factors: as is seen from Fig. 6, that a few scrips draw investors' interest so an index with a smaller number of shares will be more representative of the market. An example of such an index is the Sensex – Bombay Exchange Sensitive Index – the benchmark index of the Bombay Stock Exchange. It is composed of 30 of the largest and most actively-traded stocks on the BSE. Secondly the market capitalization should be calculated on free-float. This is a variation of the market capitalization method, which instead of using a company's outstanding shares, uses its float, or shares that are readily available for trading. The free-float method, therefore, does not include restricted stocks, such as those held by company insiders that cannot be readily sold. The decision regarding running of the two indices parallel is still to be taken.

As on May 24, 2006

Symbol	Volume	Current Rate	Price Change	% Change	Index Weight-age (%)	Index Points	Outstanding Shares (million)	Market Capt. (million)
<b>Oil and Gas Development</b>	19,751,300	150.4	1.75	1.18	<b>23.11</b>	29.67	4,300.93	646,859.63
P.T.C.L.A	2,836,700	51.3	0.25	0.49	6.92	3.72	3,774.00	193,606.20
National Bank	17,953,700	253.15	4.6	1.85	6.41	12.86	709.07	179,501.38
Pak Petroleum	12,318,800	253.85	6.1	2.46	6.22	16.49	685.82	174,095.76
MCB Bank	5,287,600	242.2	2.7	1.13	4.43	5.45	511.84	123,967.46
<b>Top 5 Companies</b>					<b>47.09</b>			
United Bank Ltd.	797,300	148.25	4.25	2.95	3.43	10.85	647.5	95,991.88
Pak Oilfields	5,161,800	408.75	4.45	1.1	2.88	3.46	197.12	80,573.45
Fauji Fertilizer	132,500	127	0.3	0.24	2.24	0.58	493.47	62,671.22
P.S.O.	1,238,800	343.3	2.8	0.82	2.1	1.89	171.52	58,882.68
Sui Northern Gas	268,400	103.85	0.35	0.34	1.85	0.69	499.19	51,840.53
<b>Top 10 Companies</b>					<b>59.59</b>			
Allied Bank Limited	408,500	111	3.95	3.69	1.75	6.86	440.46	48,891.52
Nestle Pakistan	2,400	1046	-54.4	-4.94	1.69	-9.72	45.35	47,435.63
Kot Addu Power	102,000	42.6	0.1	0.24	1.34	0.35	880.25	37,498.79
Fauji Fert. Bin Qasim	2,882,000	35.55	0.2	0.57	1.19	0.74	934.11	33,207.61
Lucky Cement	3,568,500	116.15	-0.1	-0.09	1.09	-0.1	263.38	30,591.01
<b>Top 15 Companies</b>					<b>66.65</b>			
Engro Chemical	440,300	198.4	1.9	0.97	1.08	1.15	152.94	30,343.30
Faysal Bank	678,000	70.95	0.3	0.42	1.07	0.5	423.72	30,062.62
Union Bank	1,333,500	78.4	0.4	0.51	0.95	0.53	338.75	26,558.04
Dawood Hercules	14,200	319	6	1.92	0.94	1.96	82.87	26,434.33
P.I.A.C. (A)	363,500	14.15	-0.1	-0.7	0.91	-0.71	1,797.32	25,432.02
<b>Top 20 Companies</b>					<b>71.6</b>			

Source: <http://www.kse.com.pk>