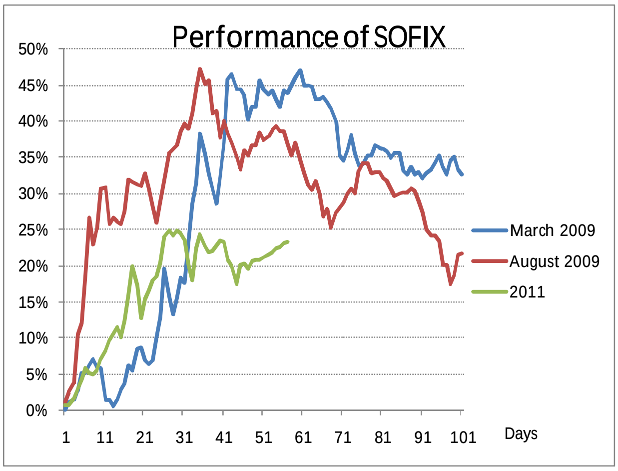
Back to normal

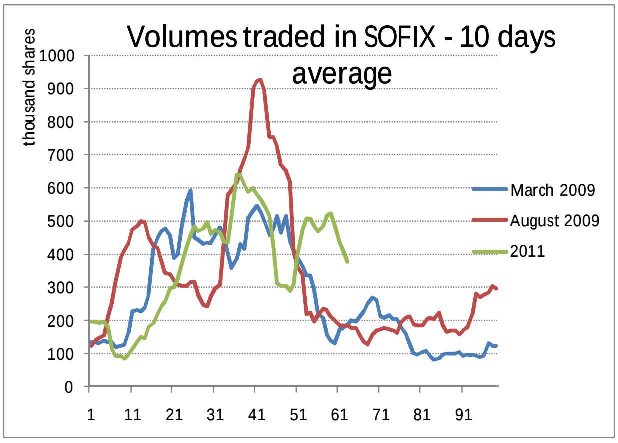
After two months of hefty gains Bulgarian stocks made a brief pause. The market is consolidating as individual investors (the primary driving force for the price increase) gradually stepped aside. However, neither individuals nor institutional investors have expressed concerns of the temporal character of the rally. Is this time different than the two periods of gains in 2009?



Let's first dissect the causes and consequences of the last rally. It started in early January due to modest buying from speculators that put some money into attractive stocks. Supply was very limited and gains were easy to achieve even with the limited financial resources of individuals. Some institutional investors, mainly domestic pension funds, also joined carefully. They accumulated some shares or used the appearance of foreign players to make portfolio adjustments. Foreign investors traded more actively in February following the bulk of the gains. They were attracted by the positive performance of stocks and became buyers of companies with attractive multiples like banks and the holding Chimimport.

Individual investors are the driving force behind the rally as they buy stocks on market. Large players are looking for blocks in the spread and will not push prices on the upside. That is why we first witness a spike in prices than volumes when foreign players join in. It happened in 2009 twice and the pattern repeated again this year.

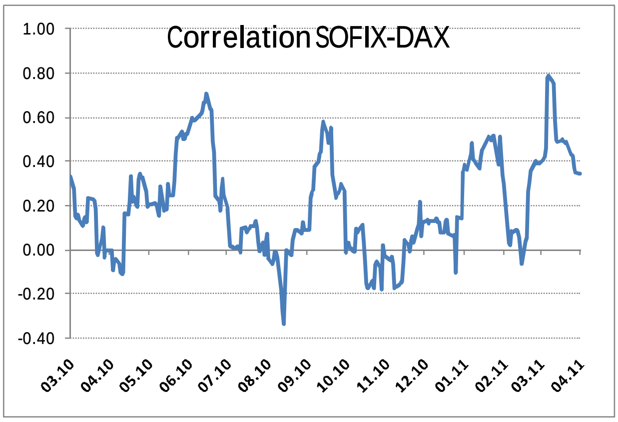
The main difference between 2011 and the both rallies in 2009 is in the level of gains. As it can be seen in the graph, SOFIX jumped 45% in 2009, whereas it added only 25% during the first two months of 2011. The rally was needed to continue for another 10 trading days to repeat the performance but investors were reluctant to chase further gains. This could be sign of more limited capitals after the severe recession in Bulgaria.



This graphic explains the difference between the recent rally and the market gains in 2009. Volumes provided by the stock-exchange are for shares traded but the data could give us correct perception for the rising participation of investors. The initial increase of SOFIX in early 2011 was accompanied by lower volumes but they quickly jumped to half million shares per session in February. This is due to the post-holiday's activity. However, the main difference could be the more prolonged period of elevated volumes between 50 and 60 days after the beginning of the rally. Maybe this time is different and could be seen in the higher volumes. Stocks are well bid, thus limiting the decline after the peak but SOFIX needs to jump above the last high to change the pattern of strong gains for two months, followed by consolidation and then deeper correction. For now we are looking for proofs that confirm or deny our expectations for small correction before the next movement on the upside.

Correlation to world markets

Bulgarian investors tend to ignore the movement in foreign markets for short period of time. However, the recent increase of the short-term correlation is showing risks for higher volatility as speculators will react to news from abroad.



The graph is showing the one-month correlation between SOFIX and German index DAX. The low correlation is usually a sign for small volumes and lack of price volatility of major stocks. We expect that correlation will gradually decrease to very low levels. In this case the main risks will come from supply and demand and not from fundamentals or the global economic picture.

At the end of March trading volumes were substantially above the usual supply from individual shareholders. The demand managed to support the stock prices and the only shallow pullback of SOFIX is actually very good news for the market as it unveil the positive expectations of investors.

The new SOFIX

The half-year changes in SOFIX took place in March. Corporate Commercial Bank (6C9) and Real Estate Fund Bulgaria (5BU) replaced Bulgarian American Credit Bank (5BN) and Zarneni Hrani (T43) due to their better liquidity. This had visible effect on the prices of all four positions. The new components of the index jumped the session prior to the change. The most notable gainer was Corporate Commercial Bank that quickly returned to its recent highs. The other two stocks fell.

Stocks in focus

Not all stocks jumped during the rally. Two banks and two diversified holdings outperformed the broad market. Central Cooperative bank (4CF) and First Investment bank (5F4) soared. This was not a surprise as both positions are actively traded by domestic speculators. Shares of Chimimport (6C4) also gained significantly due to the same reason. Stara Planina Hold is usually less actively traded but also grabbed the attention of individual players. All four stocks had low multiples that attracted buyers.

	2010	06.4.2011	Change
6A6	1.20	1.42	18.43%
6AB	48.10	60.50	25.78%
4EH	0.89	1.00	12.43%
4ID	0.99	1.13	14.13%
6K1	4.90	5.20	6.12%
5MB	6.30	7.17	13.87%
E4A	7.10	7.00	-1.41%
3JR	3.91	4.47	14.14%
5BU	0.53	0.80	52.19%
6C9	64.00	82.87	29.48%
5DOV	3.45	3.23	-6.40%
4CF	0.99	1.66	67.00%
5SR	2.78	4.04	45.32%
6C4	2.32	3.57	53.81%
5F4	2.15	3.37	56.88%

We consider that the best performing positions would continue to shine through the course of the year. However, a pullback in low volumes is possible as some investors will take profit. Stocks that added less than 20% for the period are less exposed to risk of price decline but their multiples are higher, most notably price-to-earnings ratios. Investors would like to see further improvement of both revenues and profits in those positions.

Industrial Holding Bulgaria (4ID) and Eurohold Bulgaria (4EH) increased their capitals, which had negative effect on the price per share. A short-term bounce in both positions is possible.

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BUY	More than 5% higher as compared to SOFIX and BG40 performance
HOLD	Market performance, +/-5% as compared to SOFIX and BG40
SELL	More than 5% lower as compared to SOFIX and BG40 performance

Frequency of Recommendations: No schedule of recommendations is available. The frequency of recommendations depends on specific factors to individual companies and the opinion of the analyst(s) for the necessity of minor or major changes.

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