

HLIB Research

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FBMKLCI Target: 1,880
Current Level: 1,858

FBMKLCI



Top Picks

Stock	Rating	Price	Target
Tenaga	BUY	16.20	17.50
RHB	BUY	5.29	6.00
MAHB	BUY	8.92	10.00
Genting	BUY	8.80	11.73
Gamuda	BUY	5.17	5.98
Sunway	BUY	1.52	2.30
DRB	BUY	2.40	2.88
GKent	BUY	4.01	5.66
Lay Hong	BUY	0.95	1.24
Rohas	BUY	1.23	1.74

Sector Rating

Sector	Rating
Auto	Neutral
Aviation	Overweight
Banking	Overweight
Brewery	Overweight
Construction	Overweight
Consumer	Neutral
Gaming	Overweight
Healthcare	Neutral
Media	Underweight
Oil & Gas	Neutral
Plantation	Neutral
Power	Overweight
Property	Neutral
REIT	Neutral
Rubber Products	Neutral
Tech	Neutral
Telco	Neutral

Strategy

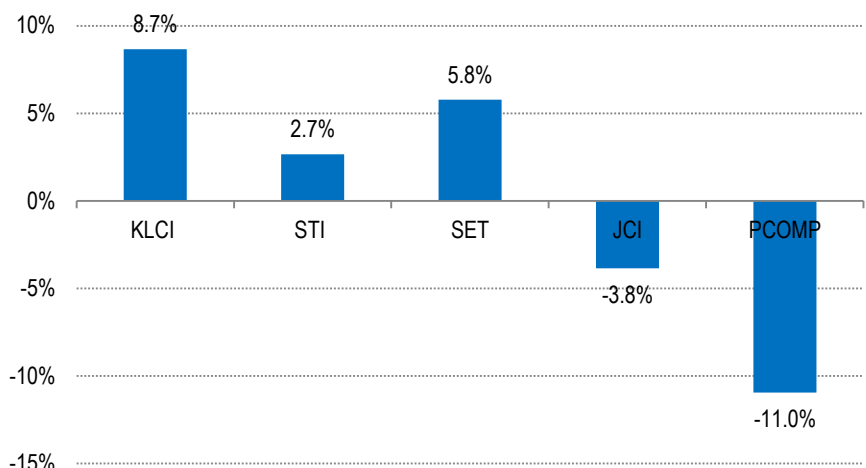
Of tariff tantrums and polls

While FBMKLCI was the top ASEAN-5 performer at 8.7% (currency adjusted), a “risk off” approach was evident with the selloff in small caps, construction and property. For 2Q18, investors are likely to focus on Trump’s tariff tantrums (we see limited and contained impact on Malaysia) and the impending GE14. With BN set to unveil its manifesto this weekend, we envisage the polls towards end-April/ early-May with a status quo outcome (i.e. BN to remain in government). A “risk-on” approach should set in once GE14 is done and dusted. We remain positive on Malaysian equities on a backdrop of domestic consumption pick up, stronger ringgit (1Q18: +4.8% QoQ) and mega construction jobs. Maintain FBMKLCI target of 1,880 premised on 16.5x P/E (0.5SD above mean) tagged to 2018 earnings.

Macro fundamentals intact. Coming into 2Q18, we continue to see strong signs of global economic activity. While some leading economic data (global PMI manufacturing index) has increased at a slower pace, overall 1Q18 average still signals a robust operating environment. In particular, firms are signalling their ability to raise output prices in an environment of stronger demand and higher purchasing power of their clients. The better-than-expected operating environment may lead to positive spillovers to Malaysia’s GDP growth. During its annual report release last week, BNM projected Malaysia’s GDP at 5.5-6% (point estimate: 5.7%). Nonetheless, downside risks have also risen of late following Trump’s trade tariff threats. As the direct impact to Malaysia is limited at this point of time, we maintain Malaysia’s GDP at 5.3% in 2018 and OPR rate at 3.25% for the rest of 2018. However, should global trade war escalate further, it could have further repercussions on global growth and trade with implications on Malaysia.

Top performer within ASEAN-5. Jan was off to a good start with the FBMKLCI gaining 4.8% during the month in what was touted to be an “election rally” coupled with the DJIA hitting an all-time high as well. However, the 1st week of Feb saw a 3% decline in the FBMKLCI due to the selloff spillover from the DJIA amid concerns of faster than expected rate hikes by the Fed. Nonetheless, much of the FBMKLCI’s early Feb losses were eventually recovered in Mar with the index ending 1Q18 up 3.7%. Against its ASEAN-5 peers on a currency adjusted basis, the FBMKLCI was actually the top performer in 1Q18 with returns of 8.7%, thanks to the 4.8% appreciation in the MYR.

Figure #1 Performance of ASEAN-5 equity indices in 1Q18 (currency adjusted)



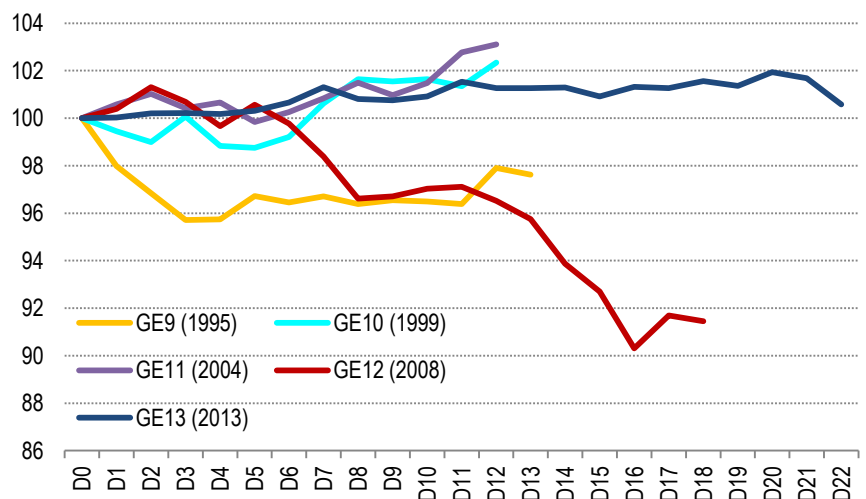
Bloomberg

Temporary “risk off”. Despite the FBMKLCI charting positive territory for 1Q18, we note that the FBM Small Cap Index (FBMSC) was down 12.9% while perceived cyclical sectors such as construction and property saw their respective indices declining 9.1% (KLCON) and 11.6% (KLPROP). We believe that investors will continue to adopt a “risk off” approach until GE14 is over given the perceived political risks. Looking ahead into 2Q18, we reckon that investors will be focused on 2 key developments: (i) Trump’s “tariff tantrum” internationally; and (ii) the impending 14th General Elections (GE14) domestically.

Trump’s tariff tantrum. 1Q18 saw US President Trump announcing import tariffs on (i) solar panels with 30%; (ii) steel with 25% and aluminium with 10%; and (iii) up to USD60bn on Chinese goods. Individually, these items do not constitute a major share of Malaysia’s exports. According to UN Comtrade database, solar exports to US accounts for 1.1% of Malaysia’s total exports to the US. Steel and aluminium account for up to 1.3% of Malaysia’s total exports to the US. With regards to the USD60bn of Chinese goods, should all of Malaysia’s exports of E&E products gets affected through intermediary exports, it will constitute up to 6% of Malaysia’s total exports to the world. In summary, the tariff measures are not anticipated to have a significant impact on Malaysia’s trade performance. Nevertheless, the possible proliferation of further protectionist measures could eventually reverse global economic recovery and dampen Malaysia’s growth prospects. As the affected countries negotiate with each other to achieve their respective objectives, the policy and political uncertainty would lead to equity market volatility in the short term.

A very likely quarter for GE14. Media articles reported that the incumbent Barisan Nasional (BN) government will unveil its manifesto on 7 April. We read this as a strong cue that Parliament will be dissolved very close to that date as well. To recap, during GE13 (2013), BN’s manifesto was revealed 3 days after the Parliament was dissolved (3 April). Assuming that Parliament is dissolved in early April, we reckon that the polls are likely to be held towards month end or early May. In the past 5 GEs, the time gap between Parliament dissolution and polling was 17-32 days. Analysis of the FBMKLCI’s performance between dissolution and polling shows that the index ended higher in 1999, 2004 and 2013 but lower in 1995 and 2008.

Figure #2 FBMKLCI performance from dissolution to polling (rebased at 100)



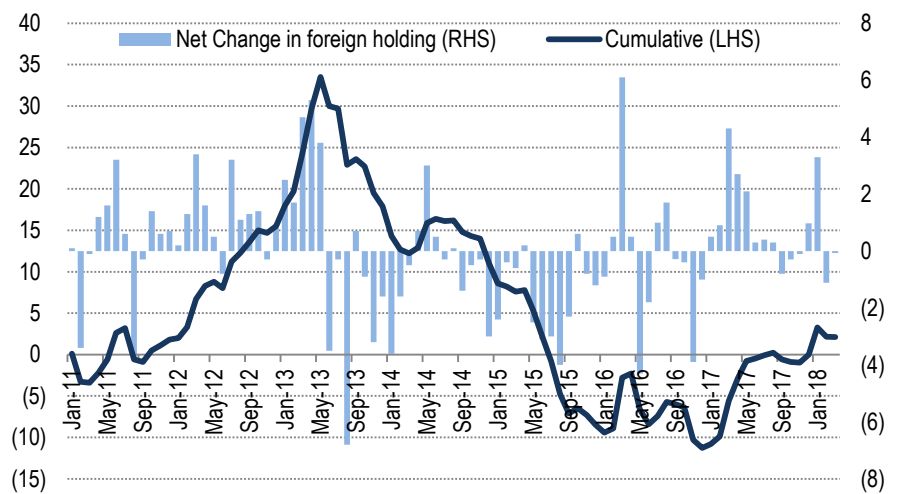
Bloomberg, HLIB estimates

Status quo outcome likely. While it is certainly not our forte to predict on politics, we believe that GE14 will likely result in a status quo outcome, i.e. BN to remain in government. Our view is anchored by the inevitable increase in 3-cornered fights this time around as PAS is no longer with the opposition coalition (now Pakatan Harapan). Media articles reported that PAS will contest in 130 (doubling from GE13) out of the 222 Parliamentary seats. This implies that 59% of the Parliamentary seats will witness 3-cornered fights which typically tilt the balance in favour of BN. To anecdotally justify this, (i) the 2016 Kuala Kangsar and Sg Besar by-elections saw BN winning in 3-cornered fights; and (ii) in the past 5 GEs, BN’s biggest victory occurred when the opposition parties were fragmented in 1995 and 2004.

Still positive on Malaysian equities. We retain our positive view on Malaysian equities for 2018 driven by a confluence of (i) pick up in domestic spending; (ii) stronger ringgit; (iii) rollout of construction jobs; and (iv) the return of investor risk appetite post GE14 as previously elaborated. On domestic consumption, (i) retail sales index grew 9.5% YoY for 2017 (vs 7.1% in 2016 and 5.5% in 2015) with continued positive momentum in Jan (8.5% YoY); and (ii) Consumer Sentiment Index (CSI) ended 2017 at 82.6, improving from 69.8 in 2016 and 63.8 in 2015. Private consumption accelerated to 7% in 2017 (vs 6.1% in 2016 and 6% in 2015) and we expect this to sustain for 2018 (BNM: 7.2%). In Feb, EPF declared its highest dividend in the past 2 decades of 6.9% (conventional account) which we believe should augur well for domestic consumption. The ringgit appreciation theme remains in motion with a 4.8% appreciation against the USD in 1Q18. We expect the USD/MYR exchange rate to average 3.9 in 2018 (2017 average: 4.3), implying a potential 9.5% appreciation YoY on average. Whilst construction job flows were slow in 1Q18 (listed contractors saw a 31% YoY decline in contract awards), we are unfazed as we believe that it was merely due to a timing lag in awarding new mega projects given that GE14 is just around the corner. Key mega projects that we expect to be awarded post GE14 include MRT3 (RM45bn), HSR (RM60bn), Pan Borneo Sabah (RM13bn) and ECRL (RM55bn) subcontracts.

Foreigners were net buyers in 1Q18. Foreigners were net buyers in 1Q18 totalling RM2.1bn. However, the net buying was only in Jan (RM3.3bn) while Feb and Mar saw net selling of RM1.1bn and RM0.1bn. We note that the cumulative net change in foreign holdings (measured since Jan 2011), has moved into positive territory thus far into 2018 after being negative since July 2015. We envisage foreign buying to gain further traction post GE14 once the perception of political risk dissipates. Current foreign shareholding of 23.6% (end Feb) is slightly above mean (23%).

Figure #3 Cumulative and net change in foreign holdings (RM bn)



Bloomberg, HLIB estimates

Maintain FBMKLCI target of 1,880. We maintain our FBMKLCI earnings growth forecast of 7.8% which is pretty much in line with our real GDP (5.3%) + inflation (2.7%) projection of 8%. Our FBMKLCI target of 1,880 is unchanged premised on 16.5x P/E (0.5 SD above mean) tagged to 2018 earnings.

Top picks. For our top picks, we remove Mitra and MB World and replace with GKent (potential MRT3 and HSR contracts coupled with a perceived election play) and Rohas (ASEAN utilities infrastructure growth). All our other top picks, namely Tenaga, MAHB, RHB, Genting, Gamuda, Sunway, DRB and Lay Hong, remain unchanged.

Figure #4 **Top picks**

Stock	Mkt Cap (RM m)	Price (RM)	Target (RM)	Rating	FYE	P/E (x)		P/B (x)		ROE (%)	Yield (%)
						FY18	FY19	FY18	FY19	FY18	FY18
TENAGA	91,789	16.20	17.50	BUY	DEC	10.90	10.60	1.40	1.30	13.90	3.70
RHB	21,213	5.29	6.00	BUY	DEC	11.30	9.40	0.70	0.80	8.80	3.30
MAHB	14,800	8.92	10.00	BUY	DEC	29.90	23.20	1.80	1.70	5.50	1.80
GENTING	33,717	8.80	11.73	BUY	DEC	12.10	11.30	0.80	0.80	7.00	1.80
GAMUDA	12,716	5.17	5.98	BUY	JUL	16.0	14.4	1.6	1.5	10.8	2.5
SUNWAY	7,414	1.52	2.30	BUY	DEC	12.0	10.8	0.9	0.9	6.7	4.2
DRB	4,640	2.40	2.88	BUY	MAR	N.M.	18.7	0.8	0.8	N.M.	0.8
GKENT	2,258	4.01	5.66	BUY	JAN	15.9	14.1	4.3	3.7	28.4	3.2
LAY HONG	598	0.95	1.24	BUY	MAR	15.3	11.5	1.8	1.6	12.0	0.5
ROHAS	581	1.23	1.74	BUY	DEC	11.3	10.3	1.9	1.6	18.4	1.6

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Stock rating definitions

BUY	Expected absolute return of +10% or more over the next 12-months.
HOLD	Expected absolute return of -10% to +15% over the next 12-months.
SELL	Expected absolute return of -10% or less over the next 12-months.
UNDER REVIEW	Rating on the stock is temporarily under review which may or may not result to a change from the previous rating.
NOT RATED	Stock is not or no longer within regular coverage.

Sector rating definitions

OVERWEIGHT	Sector expected to outperform the market over the next -12 months.
NEUTRAL	Sector expected to perform in-line with the market over the next -12 months.
UNDERWEIGHT	Sector expected to underperform the market over the next -12 months.