07 April 2016 | Market Review

Performance Review 1Q16

KLCI: 1,717.01 points

2016 Year-end Target: 1,800 points

THE MARKET

Entering 2016, the FBM KLCI index was under selling pressure due to continued slump in crude oil prices coupled with softening Ringgit as well as negative spillovers from China's market collapse. The local benchmark retreated to a year-low of 1,600.92 points on 21 January.

However, aided by the oil price recovery due to a potential production freeze agreement among world major oil producers, the FBM KLCI started to reclaim its lost grounds. The rally was further buttressed by the strengthening of Ringgit and returning of foreign funds pursuant to the US FOMC's decision to hold its benchmark rate unchanged and scale back its rate increase projection this year to two hikes from the earlier four.

Fed chair Yellen's words of "proceed cautiously" in US rate normalization provided the final boost to FBM KLCI which closed the quarter at 1,717.58 points, registering a 1.5% advance in 1Q16.

Based on market capitalization-weighted performance of all stocks under our coverage, the sectoral winners and losers for the first quarter are:

Sector	1Q16 Performance
Media	+8.36
REIT	+6.07
Consumer	+5.67
Construction	+5.49
Transportation	+5.06
Banking	+4.88
Utility	+4.13
Building Material	+3.51
Plantation	+3.00
Finance	+2.30
FBM KLCI	**+1.48**
Property	+0.67
Healthcare	+0.30
Insurance	-0.46
Tobacco	-3.64
Oil & Gas	-5.44
Telecommunication	-6.93
Automotive	-9.36
Technology	-11.55
Glove	-24.28

Source: Bloomberg, MIDFR

MAIN SECTORAL OUTPERFORMERS

Media: +8.36%

The media industry emerged as the best performing sector in the market. Although media companies encountered significant challenges in the digital age with rampant pirated TV shows online and the emergence of social network sites as the medium for news transmission, their effort to diversify revenue streams from the conventional advertisement and subscription businesses seemed to re-elicit investors' confidence in their prospects.

Companies such as Astro Malaysia Holdings Berhad and Media Prima Berhad have tapped into the realm of home-shopping business. Though the venture was in its nascent form, investors seemed to hold faith in the move in the medium to long term when the digital-leaned millennials replace their older generation as the main purchasing force in the economy.

Astro in its recent earnings release reported an increase in merchandise sales of RM37.7m from its home-shopping business. Though its contribution to the overall earnings might appear marginal, the growing home-shopping business carried a symbolic meaning marking the evolution of domestic media industry to counteract the digital current.

REIT: +6.07%

REIT was one of the second best performers in the market. One of the primary drivers for the advance was the downward-adjusting 10-year MGS yield. With the US FOMC's dovish-leaned policy decision on their benchmark interest rate in January and March, global investors appeared to have directed their money back to Malaysia's bond market.

The yield for 10-year MGS, dated 31 March, has declined by 38 basis points. This has widened the spread between the REIT and MGS yields. The relative attractiveness of REIT investment to the low-risk 10-year MSG was in turn enhanced.

Apart from that, the 3% reduction in EPF contribution and income tax relief announced during the January budget recalibration were perceived to be able to boost the faltering consumer spending. These measures appeared to have provided support to the share price with investors arguably perceived the imminence of a more encouraging occupancy rate and rental fee growth in the retail segment of the industry.

Consumer: +5.67%

The consumer industry emerged as one of the best performers amid the record low consumer sentiment index in the previous quarter.

The primary booster to the industry was arguably the stimulus measures laid out in the January budget recalibration. The 3% reduction in EPF contribution and income tax relief effectively increased households' disposable income, potentially increasing their spending on discretionary items.

In addition, households' purchasing power was further enhanced with the declining petrol prices throughout the first quarter. For instance, the widely used RON95 dropped by a total of 35 cents in the first three month of 2016. The windfall from a cheaper petrol price arguably heightened households' spending spirit, boosting the sales revenue of consumer-oriented companies. Investors thereby were attracted by the industry's encouraging earnings prospects.

Construction: +5.49%

The construction industry was one of the best performing sectors in the market. The industry was one of the main beneficiaries from the government 2016 budget which has allocated considerable amount of funds for infrastructure spending.

Among the projects proposed included long-term mega projects such as the KLIA Aeropolis and Malaysian Vision Valley, road construction such as West Coast Expressway and Pan Borneo Highway, and public transport system construction such as KVMRT2 and LRT3. The proposed budget was set to provide a boost to construction companies' order book.

However, the plunge of crude oil price into the USD30-40pb territory threatened the budget's feasibility, with the government subsequently announced an imminent budget recalibration. Market uncertainties heightened, fearing cancellation or postponement of the proposed infrastructure projects.

Nevertheless, market tensions eased as the allocated funds for the respective projects mostly remained intact in the revision. Investors re-recognized the industry's earnings potential, supporting the share price of the related companies.

MAIN SECTORAL UNDERPERFORMERS

Glove: -24.28%

The glove sector was the worst performing industry in the market. This was arguably driven by the weakening US dollar in recent months. As an export-oriented industry with a considerable portion of its sales denominated in the dollar, glove producers' earnings are directly impacted by the strength of the dollar.

Without sufficient currency hedging, glove producers' overseas sales earnings in the Ringgit tend to exhibit a strong positive correlation with the dollar value. As at 31 March, the dollar has depreciated year-to-date by 9.0% against the Ringgit. This imposed a significant punch on the glove sector's Ringgit earnings prospects, thereby dragging down the share prices of glove manufacturers.

Nonetheless, the adjustment to foreign workers levy, introduced by the Prime Minister in his January budget recalibration, was finalized on mid-March to be a 48% increase for the manufacturing industry, much smaller than the initially proposed 100%.

Although the glove manufacturers were believed to be able to pass on the additional cost to the buyers with minimal impact on their sales volume, market might have priced in a risk premium in their share prices due to the increasing uncertainties in terms of the labor cost fluctuation subjected to government discretionary policy revision.

Technology: -11.55%

The technology industry emerged as the second worst hit sector in the market. The technology industry, similar to the glove industry, is export-oriented and thus holds relatively high exposure to currency risks.

The Ringgit has appreciated by 9.0% against the US dollar in the first quarter. Without sufficient foreign exchange hedging, the technology companies' Ringgit earnings potentially deteriorated, dampening their shares' attractiveness to the investors.

Moreover, according to the Semiconductor Industry Association (SIA), the global sales of semiconductors in January was 2.7% lower than the previous month and was 5.8% lower than the corresponding month a year ago. As technology companies' sales rely considerably on international buyers, a sluggish global demand would have certainly hurt their potential earnings, driving investors away from holding their shares.

Automotive: -9.36%

The automotive industry was one of the worst performers in the market. This was driven primarily on the weakening demand side partly due to the price hikes pursuant to the elevated US dollar value with respect to Ringgit.

According to the survey by MIER, the consumer sentiment index dipped to a record low of 63.8 for 4Q15. The dampened purchasing spirits, possibly due to the intensifying global uncertainty and the GST implementation, were reflected in the automotive TVI, which registered a -12%yoy and -25%yoy drop for January and February this year, respectively.

Apart from the weakening macro-economic setting and the lingering impact of GST, the decline could be attributed to the price hikes across the industry early this year. The price increase was administered to compensate for the elevated import costs due to a weaker Ringgit. Car sellers, however, seemed to be unable to avoid a substantial loss in their sales volume due to the price adjustment. Overall earnings projections appeared to be less favorable, weakening investors' interest in the industry.

On the flip side, the Ringgit has strengthened against the US dollar by 9.0% in the first quarter. However, car sellers were unlikely to fully benefit from the weaker dollar in the immediate term, as a portion of their inventories might have been purchased back then when the dollar was stronger.

Telecommunication: -6.93%

The telecommunication sector was one of the worst performing industry. With the market becoming saturated, telcos, in their search for further growth, were forced to compete among themselves to expand their market share. They have tried to beat their peers by introducing new packages at more competitive prices. Their profit margins, as a result, were squeezed.

The degree of competition seemed to heighten with the announcement of spectrum reallocation by the MCMC. Smaller market players like Digi and U-mobile were expected to be able to compete on an equal footing to Maxis and Axiata by having access to a greater share of capex-efficient spectrum.

The price competition was expected to intensify as a result, further dampening the industry's earnings prospects. Investors therefore appeared cautious with the industry.

In addition, market uncertainty escalated with the fees on the spectrum yet to be revealed. Market was expecting the government to try to extract the maximum fees from this reallocation to alleviate the tight federal budget due to slumping crude oil price.

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DISCLOSURES AND DISCLAIMER

MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS	
STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	Total return is expected to be <-15% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >15% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.
SECTOR RECOMMENDATIONS	
POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.