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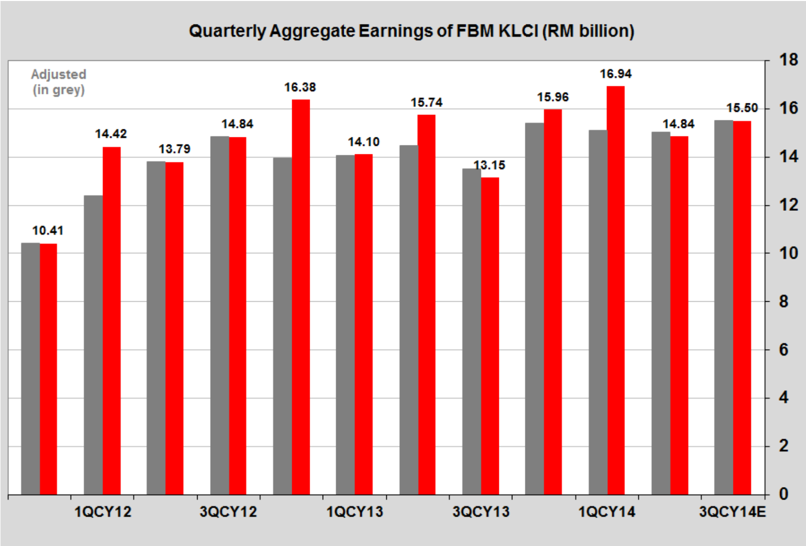
3QCY14: Expect double-digit on-year growth

KLCI: 1,818.38

Price pullback helps earnings to catch up with expectation

(2014 Year-end Target: 1,850-1,800 points)

Aggregate earnings of FBM KLCI stocks may increase +3.2%qoq and +14.8%yoy. For the quarter ended September 2014, the aggregate earnings of FBM KLCI current constituents is estimated at RM15.50b. Against the combined RM15.02b adjusted earnings recorded in preceding quarter, the 3QCY14 aggregate earnings is expected to record a sequential growth of +3.2%qoq. Furthermore, the on-year growth number in 3QCY14 is estimated to rise by +14.8%yoy hence broadly outdoing the prior quarter's 3.7%yoy adjusted growth performance.



Source: Bloomberg, MIDFR

3QCY14 aggregate earnings is estimated at RM15.50b

Expect better on-year reported earnings among all index sub-sectors. All of FBM KLCI sub-sectors are expected to show positive on-year growth in 3QCY14. The best on-year earnings performance may come from the Plantation sub-sector. We also expect positive on-quarter growth in all index sub-sectors excepting Plantation and Oil & Gas. The highest sequential earnings growth number in 3QCY14 may come from the variety of companies classified as Others within the benchmark.

FBM KLCI: Quarterly adjusted earnings (RM million) and growth estimates

	3QCY14E*	2QCY14	QoQ	3QCY13	YoY
Banking	5,704.12	5,663.02	0.7%	5,565.34	2.5%
Telecommunication	1,941.77	1,788.83	8.5%	1,876.65	3.5%
Plantation	1,945.20	2,132.30	-8.8%	1,357.76	43.3%
Oil & Gas	1,685.83	1,685.33	0.0%	1,651.47	2.1%
Others	4,221.17	3,753.87	12.4%	3,051.36	38.3%
OVERALL	15,498.09	15,023.35	3.2%	13,502.59	14.8%

Source: Bloomberg, MIDFR; E* - estimate

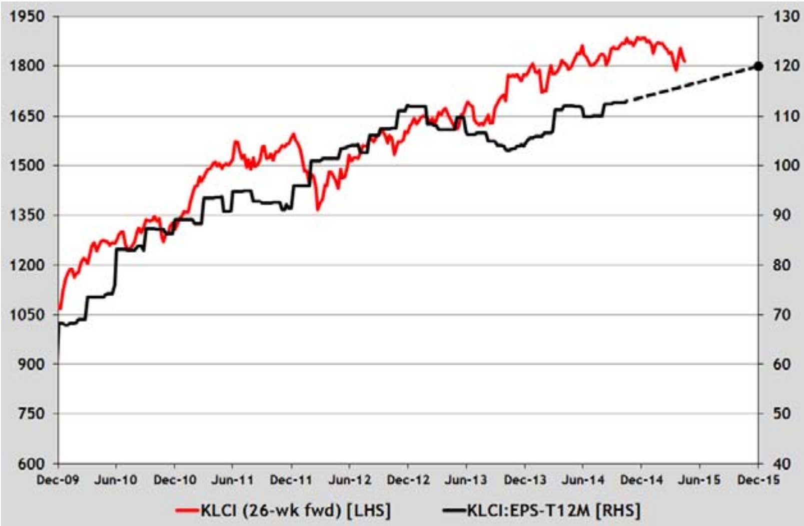
Banking. The Banking sector is anticipated to continue on chalking rather unassuming albeit steady sequential and on-year earnings trajectory with low single-digit growth in 3QCY14. This prognosis is in line with the continued moderation in the momentum of loan growth coupled with pressure on NIM as well as weaker NOII.

Telecommunication. The expected modest on-year growth performance among telecommunication players is reflective of the maturing and competitive industry landscape. We do not think this situation will change drastically for the better anytime soon.

Plantation. Average CPO price declined almost -14% to circa RM2,209pmt in 3QCY14 from 2,565pmt in the preceding quarter. Year-on-year, the decline in CPO price was more modest at less than -6% from RM2,349pmt in 3QCY13. Hence plantation companies may show negative sequential earnings growth in 3QCY14 but however, the decline may be moderated by higher FFB output in the third vis-à-vis preceding quarter. On the other hand, the aggregate plantation earnings of FBM KLCI constituents may show a large year-on-year rise. This is due to (i) generally higher CPO output (average +5%yoy) in the third quarter this year against the same quarter last year, and (ii) a low base effect owing to Sime Darby's poor performance in the corresponding quarter last year attributable to lower earnings contribution from all of its business divisions.

Oil & Gas. The rather tepid expected earnings performance by the oil & gas companies may be blamed on the challenging operating environment among the major downstream players which result in (i) low plant utilisation rate and weak product prices, as well as (ii) lower profit margin and higher cost of sales.

Empirically, the movement of FBM KLCI is a good leading indicator to its upcoming earnings result performance. Our 'best-fit' historical chart of the FBM KLCI against its 12-month trailing earnings (KLCI:EPS-T12M) shows the former led the latter by about 26 weeks . The approximately half-year lead time provides rather reliable guidance on earnings performances of the recent/prevailing quarter as well as the subsequent one.



Recent FBM KLCI price pullback helps its earnings to catch-up

Source: Bloomberg, MIDFR

Recent price pullback helps earnings to catch up with expectation. By looking at the performance of FBM KLCI during the past 26 weeks (see Chart above), we can expect its earnings to continue on an upward trajectory in the third quarter of this year. Subsequently, its earnings trajectory is anticipated to remain on an upbeat pace in the quarter ending December 2014. In essence, earnings are expected to steadily catch-up with the price-led expectation. It is even more reachable with the recent price pullback.

Expect FBM KLCI to remain on secular upward trend on favourable macro outlook. We continue to be rather sanguine on the likelihood of FBM KLCI forward earnings to eventually catch-up with the price-led expectation, supported by prospects of (i) gentler yet still robust domestic growth momentum, and (ii) supportive external economic conditions. Hence our view that the FBM KLCI to remain on its secular upward trend at least in the medium-term.

But the trend trajectory may be moderated by valuation, monetary and liquidity headwinds. At the same time, we wish to reiterate the potential headwinds to the market trend trajectory going forward, namely (i) the prevailing above mean market valuation, (ii) worries over interest rate hikes both domestic and foreign, and (iii) the intermittent volatility in foreign liquidity flow.

FBM KLCI year-end 2014 at 1,850 points. Thus we reaffirm our rather modest FBM KLCI year-end 2014 range target of 1,850-1,800 points and year-end 2015 target of 1,970 points.

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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.