STRATEGY

FBM KLCI 2020 Target: 1,320 pts

Manoeuvring Covid-19-induced Market Volatility

KEY INVESTMENT HIGHLIGHTS

- **The underlying (tacit) recommendation of our FBM KLCI 2020 target since the onset of Covid-19 pandemic in March has shifted from Buy, then Hold and now Sell**
- **Our FBM KLCI 2020 target was cut to 1,480 points in mid-March, then 1,400 points in mid-April and now 1,320 points since early June**
- **Meanwhile, the FBM KLCI was trading circa 1,200 levels in mid-March, then 1,400 levels in mid-April and now at more than 1,500 levels since early June**
- **At current levels, the market seems to impute blue-sky scenario in regard to the post-lockdown economic recovery**
- **But recent statements by the US Fed as well as cue from China (already in post-lockdown) suggest that post-lockdown economic recovery may not be plain sailing**
- **We reckon the second downward thrust (fallout phase) may later emerge, possibly in the third quarter, as the fuller extent of economic and corporate earnings impacts of Covid-19 become manifest**

BUY LOW, SELL HIGH

Source: TradingView.Com, MIDFR

We revised our FBM KLCI 2020 target three times since early March due to heightened market volatility in reaction to the fluidity in the macro environment as a direct result of the Covid-19 pandemic.

Nonetheless, as in previous market upheavals, there is always an underlying order amid the chaos as highlighted in our strategy report titled The Bear Market Waves dated 24 March. In gist, a bear market empirically follows a 3-wave (down-up-down) pattern. Fundamentally, they can be classified as (i) trigger-(down), (ii) reaction-(up), and (iii) fallout-(down) phases.

BUY SIGNAL GROWS LOUDER AS SELLING INTENSIFIES DURING TRIGGER PHASE

The FBM KLCI slumped to circa 1,200 points level during the trigger phase while we cut our 2020 target to 1,480 points in mid-March (vide Hope in the Shadow of Fear dated 16 March). We tacitly recommended a Buy on the market as we were anticipating an impeding emergence of the reaction (rebound) phase.

The world's equity market duly rebounded off its 23 March low as investors were encouraged by the announcements of massive monetary easing as well as fiscal stimulus by the US authorities in particular. Later on, beginning in April, equity prices were also buoyed by flattening Covid-19 curve in numerous countries worldwide. Intermittently, claims of progress made on the development of Covid-19 vaccine also helped to excite the equity market.

HOLD SIGNAL AS REACTION (REBOUND) PHASE UNDERWAY

We were expecting the upside to the FBM KLCI during the reaction phase to be capped at an upper consolidation target of 1,400 points (with a lower consolidation target at 1,250 points). With that in mind, while premised on a downward revision to our GDP target for this year, we cut our FBM KLCI 2020 target to 1,400 points in mid-April (vide FBM KLCI Cut On GDP Revision dated 14 April).

Until mid-May, the FBM KLCI was on a holding pattern at around 1,400 points levels. During that period, we were tacitly recommending a Hold on the market.

SELL SIGNAL AS REBOUND GOES OVERDRIVE WHILE FALLOUT PHASE REMAINS A LURKING FEAR

The world's equity market rebound went into overdrive since mid-May on the prospect of post-lockdown economic recovery but arguably driven by burgeoning financial liquidity worldwide. It must also be highlighted that the start of the recent price rally coincided with the commencement of the USD0.5t SMCCF on May 12 by the US Fed. In this regard, the correlative impact (of the US Fed providing backstop on credit risk premium) towards equity pricing cannot be underestimated.

During the past three weeks, international equity market indices rebounded impressively. On Wall Street, the Dow Jones Industrial Average (DJIA) recouped the early March levels as it regained the 27,000 points mark. Meanwhile, the tech-laden Nasdaq Composite (with some constituents seen as beneficiary of the lockdowns) even managed to register a new all-time high level.

Likewise, the local benchmark also had a good run since mid-May. In spite of profit taking, the FBM KLCI ended yesterday at 1,557.25 points which was still more than erased (i) all of the losses incurred after the 11 March Covid-19 pandemic declaration by the World Health Organisation (WHO), as well as (ii) all of the losses in reaction to the 9 March crash in crude oil prices due to production cut spat between Saudi Arabia and Russia.

It is implicit in the prevailing buoyant world's equity market performance that (i) there will be no second (and subsequent) wave of Covid-19 infections, (ii) the Covid-19 vaccine shall be found (sooner than normally expected) hence rescinding the need for social distancing and its attendant adverse impacts on economic activities, and (iii) the economy is slated for a V-shape recovery after the lockdown is over with very limited fallouts on both the corporate and consumer fronts while social norms would quickly reverting back to the old normal.

On above score, fundamentally, we believe the unfolding reality may differ from what the liquidity-driven market is currently implying.

Firstly, the WHO says that the Covid-19 could become endemic (i.e. the virus would never go away) thus the risk of subsequent waves of infections remain present until the society develops herd immunity. In fact, the director of the US Centers for Disease Control and Prevention (CDC) warns of a second Covid-19 wave to coincide with flu outbreak in the fall season.

Secondly, according to many health experts, the likely scenario is for a Covid-19 vaccine to be found and ready only by the middle of next year at the earliest. Hence the social distancing rules would likely remain in effect at least for the next 13 months. Another point to note is that none of the vaccine of the earlier types of coronavirus (e.g. SARS and MERS) was ever found.

Thirdly, a V-shape economic recovery could be achieved and sustained only if the virtuous economic circle of employment-consumption-revenue-investment-employment can be revived and safeguarded. However, without the Covid-19 vaccine, the economic consequence of social distancing rules on consumption and investment would remain a drag to output revival and growth in the foreseeable future.

Moreover, as alluded by the US Fed Chair Jerome Powell, a slower than desirable pace of economic recovery could turn what initially deem as liquidity problems into solvency problems among both the households and businesses.

A telltale sign that the post-lockdown recovery period is not expected to be plain sailing for the world economy can be glanced from the recent decision by China's authority to abandon (for the first time since 1994) an economic growth target for 2020. "This is because our country will face some factors that are difficult to predict in its development, due to the great uncertainty regarding the Covid-19 pandemic and the world economic and trade environment," said Premier Li Keqiang.

Moving forward, possibly in the third quarter, we expect the equity market to encounter another wave of selling pressure, i.e. second downward thrust (fallout phase) as the real extent of economic/corporate earnings impacts of Covid-19 become manifest.

In regard above, during both the current and ensuing quarters, the economic/corporate earnings data (i) may continue to deteriorate based on year-on-year basis, while (ii) the post-lockdown monthly sequential (month-on-month) jump may quickly fizzle out as pent-up demand in the aftermath of the economic reopening is duly satisfied. During this period, we may see the next wave of selling in the equity market.

As the fallout phase remains a lurking fear (and premised on the diminution in consensus EPS20 estimate for the FBM KLCI to 77.4 points as of end-May as well as the downward revision in our GDP target to -2.1% for this year), we cut our FBM KLCI 2020 target to 1,320 points in early June (vide Fallout Phase Remains A Lurking Fear dated 2 June). Thus, at this juncture, we are tacitly recommending a Sell on the market.

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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS	
STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <10% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >10% 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.