Positive Momentum Amid Uncertainties

Underlined by Less Hawkish Rate Outlook & Local Resilience

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Strategy Report

KEY INVESTMENT HIGHLIGHTS

- FBM KLCI has experienced mixed quarterly results this year.
- 1QCY26 rally was interrupted by war and 2QCY26 performance beset by foreign outflows on prospect of US monetary tightening while 3QCY26 exhibits positive momentum on favourable tailwinds.
- Lower crude oil prices below post-war support level contributed to tame inflation data.
- Tame inflation data supports the case for either no or mild policy rate hike by the Fed.
- Interest rate futures market implies only a 53% chance of one rate hike later this year.
- Local economic resilience evident by above expected Malaysia's 2QCY26 GDP growth.
- Local equity investors maintain a tacit bullish posture, buying heavily on pullbacks and selling lightly on rallies.
- The outcome of the Middle East conflict and its impact on energy prices and monetary policy remain the key wild card.
- We are keeping our eyes on the various potential outcomes while still maintain our FBM KLCI end-2026 price target of 1,770 points (or PER26 of 15.6x).

2026 THUS FAR:

Mixed quarters

FBM KLCI has experienced mixed quarterly results this year. It added +0.6% in 1QCY26, corrected -1.6% in 2QCY26, and rebounded +4.2% thus far in 3QCY26.

1QCY26 rally interrupted by war while 2QCY26 beset by foreign outflows on rate hike worries

The index started the year with robust upward momentum, supported by a strengthening Ringgit, foreign fund inflows, and macroeconomic optimism. However, this positive sentiment was interrupted by the outbreak of the US-Israel-Iran war and its negative impact on global energy prices. In the second quarter, market performance was weighed down by elevated inflation concerns and the prospect of US monetary tightening, which triggered foreign fund outflows.

3QCY26 exhibits positive momentum

In the current quarter, the FBM KLCI has rebounded, exhibiting a cautious recovery. Some key factors engendering the positive momentum are (1) tame US inflation, (2) lower crude oil prices, (3) less hawkish Fed rate outlook, (4) macroeconomic outperformance, and (5) tacit bullish local investors.

Tame US inflation

The headline and core July PPI came in at 0%mom (exp: +0.2%mom) and +0.2%mom (exp: +0.3%mom), respectively. Moreover, the headline and core July CPI came in at +0.1%mom (exp: +0.1%mom) and +0.2%mom (exp: +0.2%mom), respectively. The latest inflation data supports the case for either no or mild policy rate hike by the Fed, distinct from the aggressive tightening cycle of 2022/3.

Lower crude oil prices

The tame July inflation data may stem partly from lower energy prices. Brent crude oil prices dropped below their post-war support level of USD94pb in mid-June and have remained mostly below that threshold throughout the third quarter.



BRENT CRUDE OIL

Less hawkish Fed rate outlook

Investors are becoming less hawkish on the Fed rate outlook after (1) the latest FOMC meeting, (2) weak July jobs data, and (3) tame July inflation figures. Evidently, the interest rate futures market implies only a 53% chance of a +25bp rate hike in October 2026 (as measured by CME FedWatch aggregated probabilities).

Macro outperformance

Malaysia's GDP growth accelerated to +6.0%yoy in 2QCY26 (1QCY25: +5.4%yoy), higher than the advance estimate and our expectation. We upgrade our projection for Malaysia's 2026 GDP growth (from +4.5%) to +5.1% (2025: +5.2%).

Tacit bullish local investors

From 13 May to 1 July, the FBM KLCI fell from 1,751 to 1,657 (-94 points) as foreign investors net sold -RM6.3 billion. From 2 July to 5 August, the FBM KLCI rebounded from 1,657 to 1,748 (+91 points), even though the foreign investors net bought only +RM0.4 billion. From 6 August to 17 August, the FBM KLCI fell to 1,726 (-22 points) despite -RM1.2 billion foreign net selling. In essence, local investors maintain a tacit bullish posture, buying heavily on pullbacks and selling lightly on rallies.

MARKET OUTLOOK:

Favourable macro, earnings & valuation support up trending market

Underpinned by expectations of continued robust GDP growth (+5.1%) and a recovery in earnings growth (+8.8%) in 2026, as well as an inexpensive valuation below the 10-year average PER of 16.0x, the FBM KLCI should be able to retain its mid-term positive trend trajectory, i.e. the upward price trend (higher-lows and higher-highs), established since the June 2025 trough of 1,490 points.

Earlier rate hike worries exert pressure on market

However, since mid-May this year, the prospect of US rate hikes has negatively impacted local currency performance, fund flows, and equity valuations, thereby exerting pressure on the FBM KLCI trend trajectory.



FBM KLCI

But more recently, several favourable tailwinds, particularly a fading likelihood of multiple US rate hikes and Malaysia's continued robust economic performance, have helped to generate positive market momentum. Moreover, local investors are seen maintaining a tacit bullish stance by buying heavily during market pullbacks and selling sparingly on rallies. It is anticipated that these dynamics will persist under current circumstances.

Recent tailwinds generate positive market momentum

Having said that, the conflict in the Middle East remains unsettling. An extended closure/blockade (lasting months rather than weeks) of the Strait of Hormuz and Bab El-Mandeb could further deplete the world's crude oil inventories, potentially leading to substantially higher energy prices and tighter monetary conditions.

Middle East impact on energy prices the main wild card

We are keeping our eyes on the various potential outcomes. At this juncture, we still maintain our marginally positive view on the equity market with FBM KLCI end-2026 price target of 1,770 points (or PER26 of 15.6x).

Maintain target while keeping eyes open

Meanwhile, the 2QCY26 corporate earnings season will begin in earnest this week and next. In view of the strong GDP growth performance during the quarter (which was driven by higher growth in the services and manufacturing sectors, in addition to the rebound in mining output, and stronger domestic spending), we expect corporate earnings to not disappoint. We shall discuss the verdict in our 2QCY26 Earnings Wrap to be published on 2 September 2026. Our reiterate our top picks for 2HCY26 as below:

	Rec.	Price (RM) @ 18/8/26	Target Price (RM)	E. Price Return	E. Dividend Yield	Expected Total Returns	FBM ESG Rating	FTSE4Good?
Petronas Chemicals	BUY	4.53	6.60	45.7%	3.0%	48.7%	4	Y
Mr D.I.Y.	BUY	1.50	2.13	42.0%	3.6%	45.6%	3	Y
Hong Leong Bank	BUY	22.60	30.50	35.0%	4.5%	39.5%	4	Y
Gamuda	BUY	4.49	5.60	24.7%	2.2%	26.9%	4	Y
Inari Amertron	BUY	2.37	2.95	24.5%	2.1%	26.5%	4	Y
CelcomDigi	BUY	2.92	3.54	21.2%	4.9%	26.1%	4	Y
99 Speed Mart	BUY	3.54	4.37	23.4%	1.2%	24.6%	2	N
CIMB Group	BUY	7.87	9.29	18.0%	5.9%	24.0%	4	Y
Tenaga Nasional	BUY	14.48	16.40	13.3%	3.8%	17.1%	4	Y
YTL Power	BUY	4.90	5.65	15.3%	1.6%	16.9%	3	Y

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STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	The stock price is expected to rise by >10% within 3 months after a Trading Buy rating has been assigned due to positive news flow.
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	The stock price is expected to fall by >10% within 3 months after a Trading Sell rating has been assigned due to negative news flow.

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.

ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell

☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
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* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology