

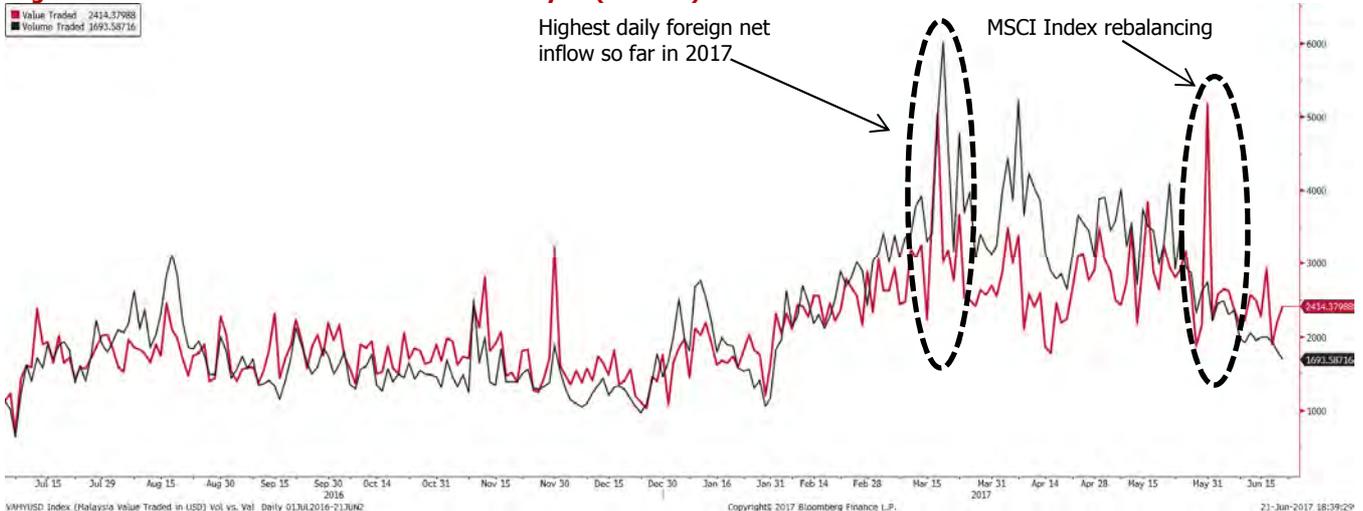
22 June 2017 | Strategy

Small cap stocks has legs to run

Potential for growth is present

- Value traded has been relatively higher this year.** The year 2017 so far has seen a significant increase in trading activities in the local bourse compared to year 2016. On the year to date basis, average daily trading volume has reached 2.5 billion shares a day, up 39% from the 2016 average (1.8 billion shares/day) and average daily traded value has rose a staggering 73% to RM2.8 billion a day (2016 : RM1.6 billion/ day).

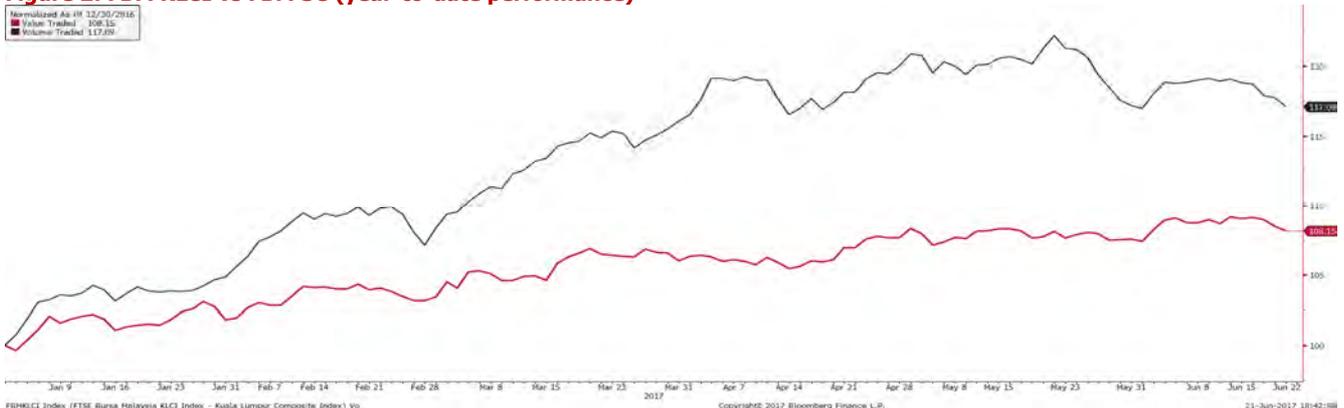
Figure 1: Value Traded vs. Volume Traded in Malaysia (USD mn)



Source: Bloomberg

- Increase in value traded coincided with foreign funds inflow.** The cumulative foreign net inflow into Malaysia this year is approximately RM10b, offsetting 30% of the total net outflow in the last three years. So far, Malaysia has experienced foreign buying in 21 out of 24 weeks this year. There was two spikes on high value trading days, the first spike in mid-March was accompanied by an influx of foreign net inflow to Malaysia equities especially into blue chips, whereby the daily net inflow recorded was the highest so far in 2017, which amounted to RM816m net. Meanwhile, the second spike which occurred at the end of May was partly attributable to the increase in trading activity following the rebalancing of the MSCI index.

Figure 2: FBM KLCI vs FBM SC (year-to-date performance)



Source: Bloomberg

- KLCI's performance reaching intraday high of 1,796.75 pts.** Year-to-date, as of 21 June 2017, the benchmark index has gained 8.2% on the back of the strong foreign inflows. Furthermore, earnings of FBM KLCI is expected to grow in FY2017 and FY2018 as per the (Bloomberg consensus) FBM KLCI 2017 estimate of 106.6 points, the earnings integer is expected to increase further, albeit slightly. Nonetheless, the FBM Small Cap Index (FBM SC) even gained more with a year-to-date gain of 17.1% indicating a high potential for small cap stocks to grow.

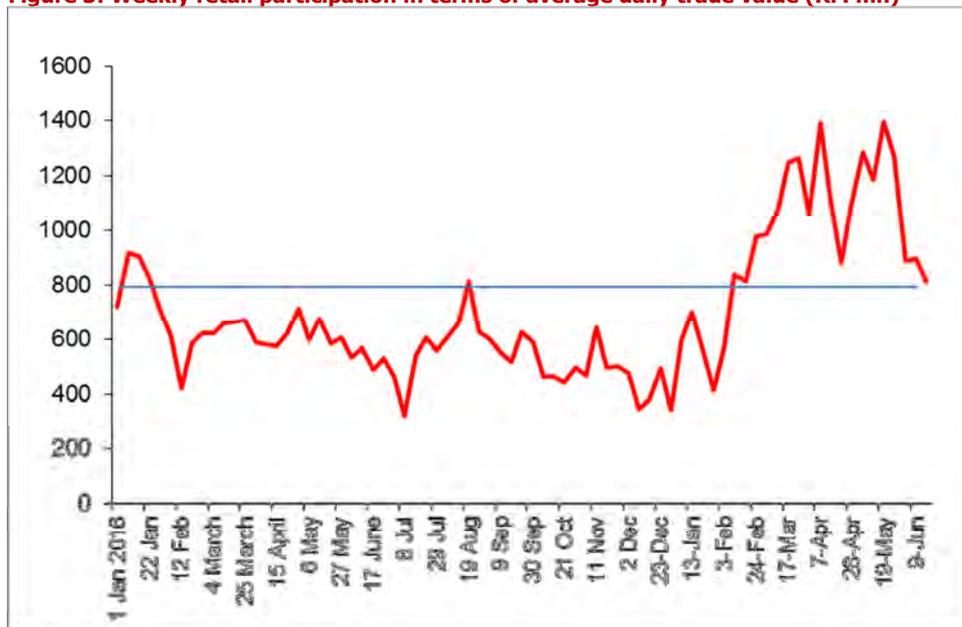
Table 1: Earnings estimate for FBM KLCI

	EARNINGS (RM mn)		EARNINGS (Annual % Chg)	
	FY2017	FY2018	FY2017	FY2018
TOTAL (FBM KLCI)	55,770.6	57,621.9	9.4	3.3

Source: Bloomberg

- Room for small cap stocks to grow.** Despite FBM SC's high performance against the FBM KLCI, we opine that small and mid-cap stocks are poised to continue its growth trajectory in the near future in line with more active retail participation. So far, the retail participation on Bursa in terms of foreign average daily trade on a weekly basis value remains moderate above the RM800m, more than 33% higher that levels seen in 2016. In our recent visit note to Bursa Malaysia, the bourse noted that more younger investors aged 25 years and below are participating in the market, as evident by the +36%yoy jump of the number of Central Depository System (CDS) account holders, to circa 30,000 in 2016. Moreover, Bursa's recently launched Mid and Small-cap Research Scheme (MidS) has the potential to attract retailer participants and in turn boost traction, both in terms of volume traded and value traded, for small and mid-cap stocks.

Figure 3: Weekly retail participation in terms of average daily trade value (RM mn)



Source: Bursa Malaysia

- **Top 10 picks for mid and small cap stocks.** Henceforth, we would like to bring forward our top 10 picks for small cap stocks contained in the following sectors outlined below:
 - Construction

Under the construction sector, our mid and small cap stock picks are **Muhibbah (Buy,TP:RM3.24)**, **Hock Seng Lee (Buy,TP:RM2.00)** and **Gabungan AQRS (Buy,TP:1.49)**. Viewing the spread between 5-Y MGS and earnings yield as barometer for earnings attractiveness, these three companies have a commendable spread while being the most persistent against the tide of market volatility.
 - REITs

AmanahRaya REIT (Buy,TP: RM1.15) is our only mid and small cap stock under the REITs. The company's asset portfolio exposure to education property and attractive dividend yield of 5.8% are factors. Apart from that, the entry Kenedix, a Japanese real estate asset management company) which should bode well for the asset management prospect for AmanahRaya REIT while also allowing the company to secure high quality tenants by tapping into network of Kenedix. All in, the declining MGS yield is positive to REITs as spread between yield of REITs and MGS yield widened, making REITs more appealing.
 - Plantation

For plantation, **Ta Ann Holdings (Buy,TP:RM4.30)** is our mid and small cap stock pick. The reason being is that its plantation division earnings growth should remain strong due to high FFB volume expected at 10%, and timber division is expected to remain profitable due to the support from high export logs price.
 - Industrials

Superlon (Buy,TP:RM2.26) and **Daibochi (Buy,TP:3.02)** are our mid and small cap stocks under industrials. For Daibochi, the 20% profit growth in FY18 is expected to be driven by Indonesia and Myanmar which are high-growth markets that the group was previously absent from. Besides that, we believe that the cost pressure encountered last year should be easing as management resolves its labour resources issue. Going forward, management will continue its operational efficiency enhancement efforts. Meanwhile, we continue to favour Superlon for its growth potential in volume with its new warehouse. Apart from that, Superlon's net cash position and strong operating cashflow can ensure that funding for the new plant will not have an issue, allowing room for some leverage.
 - Transport

Tasco (Buy,TP:RM2.91) is one of our small-mid cap stocks that we favour under transportation. Tasco's purchase of cold chain logistics assets provides an impetus in FY18, evolving from having nil cold chain assets to a market leader in the segment. Apart from that, a nascent recovery in international trade growth and an improving manufacturing sector would augur well for the company, in our view. Another small-mid cap pick is **Tiong Nam (Buy,TP:RM2.08)** for its market leading position in the integrated logistics industry. Meanwhile, an IPO of its logistics assets into a REIT could provide immediate rerating catalyst for the stock, giving rise to the potential of special dividends.
 - Consumer

Spritzer (Buy,TP:RM2.83) is our pick under the consumer sector. The company has been charting undisrupted growth in the last five years. Its 2012 to 2016 net profit CAGR was 30%. We expect the company to continue its upward climb in FY18 as it solidifies its existing market share while it expands into new markets.

Table 2: Investment Statistics of Mid and Small Cap Stocks

	Price Close (RM) 21 June	Target Price (RM)	Expected Price Return (%)	P/E (x)		Dividend Yield	
				FY17	FY18F	FY16	FY18F
Muhibbah	2.73	3.24	18.7	8.5	7.0	1.8	1.8
Hock Seng Lee	1.63	2	22.7	11.5	10.7	1.5	1.6
Gabungan AQRS	1.4	1.49	6.4	17.5	15.6	n/a	n/a
Amanah Raya REIT	0.96	1.15	19.8	15.3	14.3	5.7	6.1
Ta Ann	3.54	4.3	21.5	13.7	12.5	3.8	4.1
Superlon	2.03	2.26	11.3	13.6	11.7	2.7	3.0
Daibochi	2.26	3.02	33.6	21.9	18.2	2.9	3.1
Tasco	2.36	2.91	23.3	17.1	9.8	1.9	2.1
Tiong Nam	1.72	2.08	20.9	12.1	12.2	2.8	3.3
Spritzer	2.47	2.83	14.6	19.9	14.8	1.9	2.2

Source: MIDFR, Bloomberg

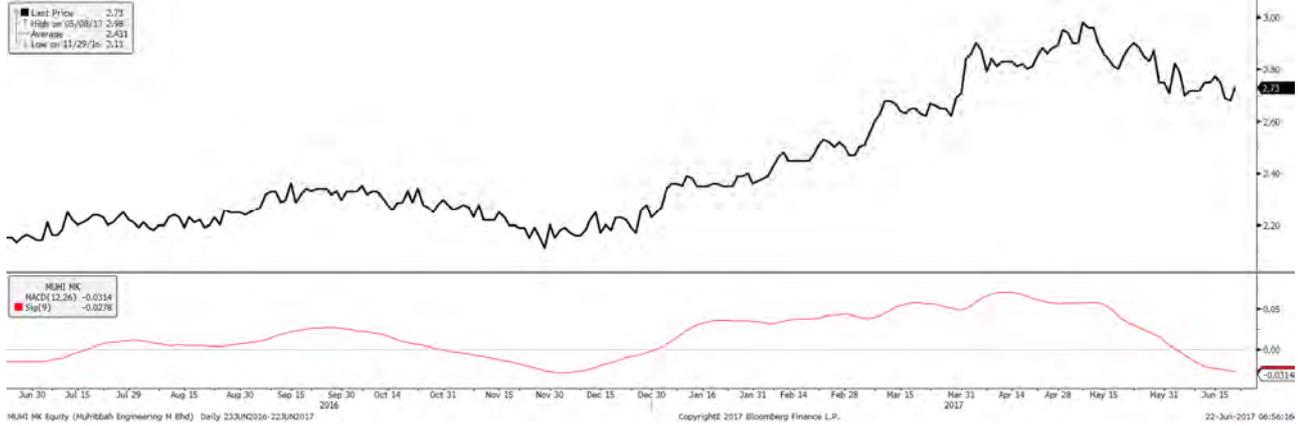
- Conclusion.** 2017 has seen an increase in market activities that saw the benchmark FBMKLCI almost breaching the 1,800 mark. The year so far also seen significant net inflow of foreign funds of approximately RM10 billion. Mid and small cap stocks, meanwhile have outperform the benchmark index, doubling the latter's return at 17%. Despite concerns over the future of the bull run, we think that there is still room for growth for the mid and small cap stocks, particularly selected ones with strong potential upside, owing from the positive corporate developments, presence of strong strategic foreign shareholder, and favourable commodity prices.

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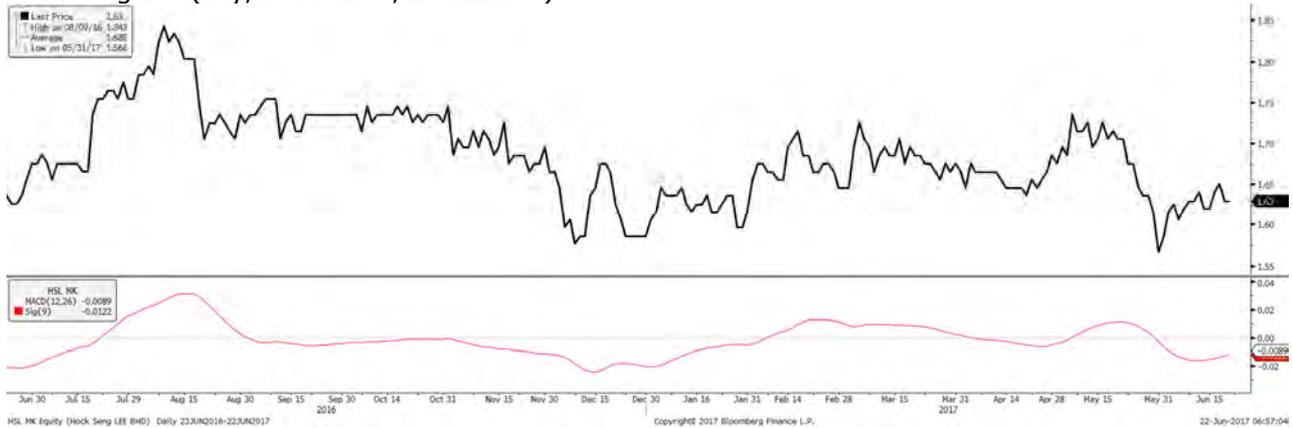
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APPENDIX

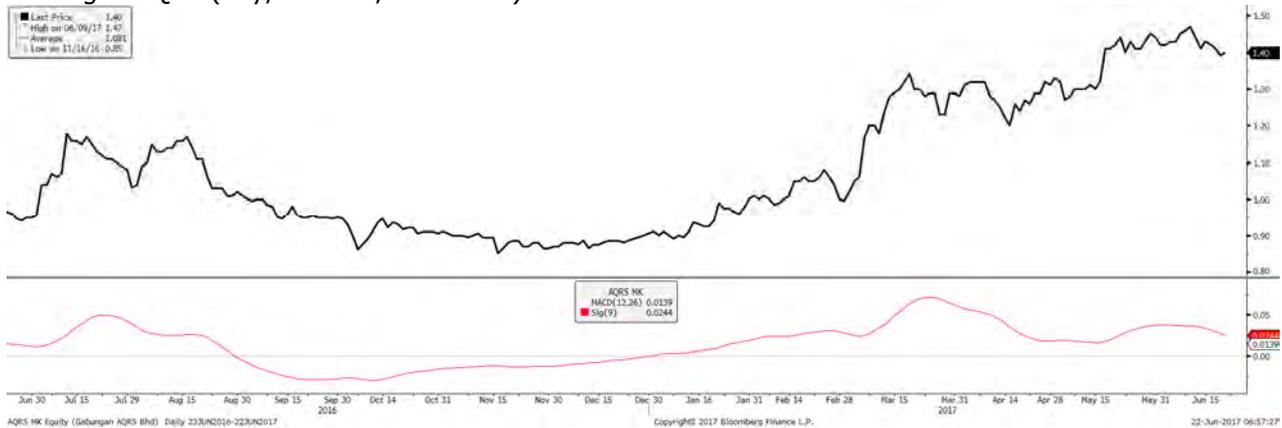
Muhibbah (Buy; TP:RM3.24; EPR:18.7%)



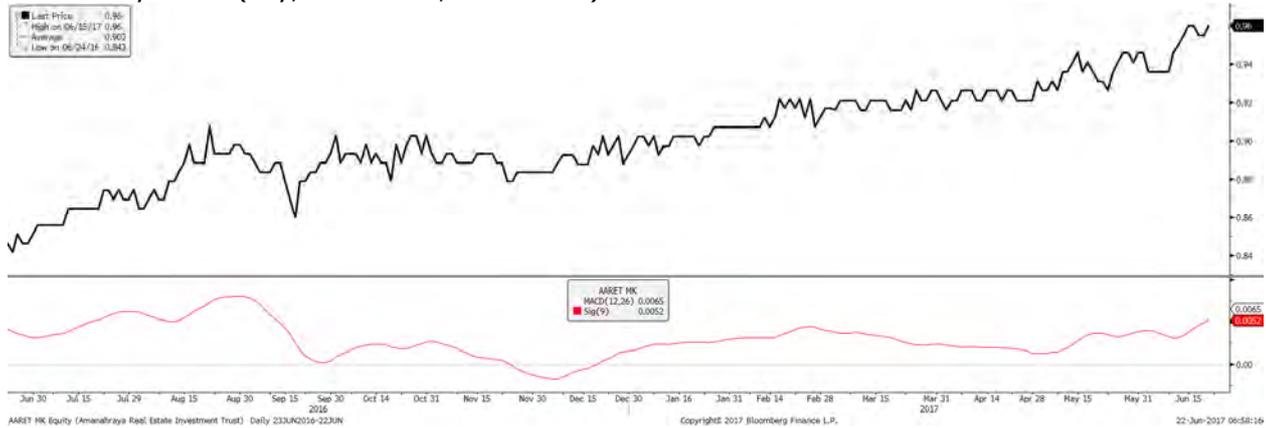
Hock Seng Lee (Buy; TP:RM2.00; EPR:22.7%)



Gabungan AQRs (Buy; TP:1.49; EPR:6.4%)

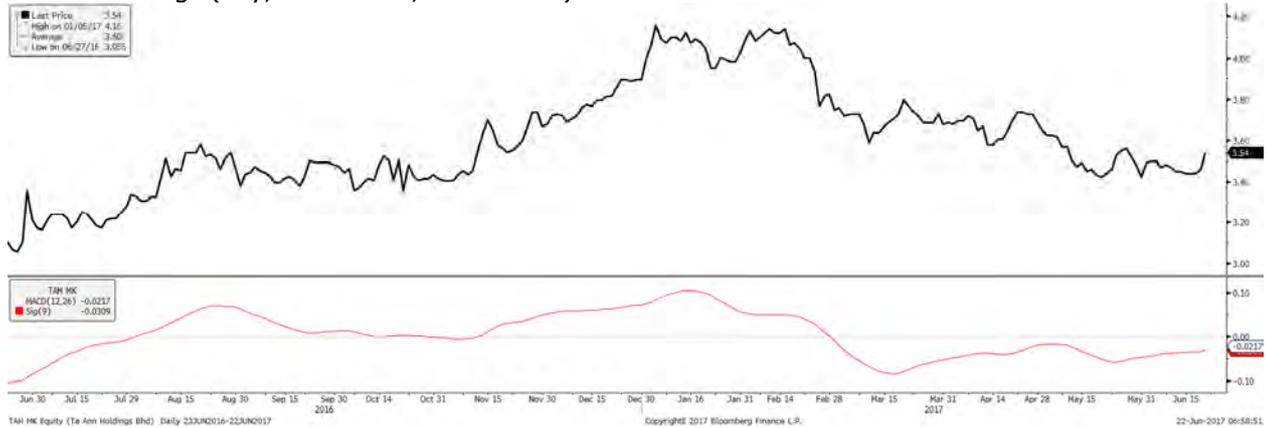


AmanahRaya REIT (Buy; TP:RM1.15; EPR:19.8%)



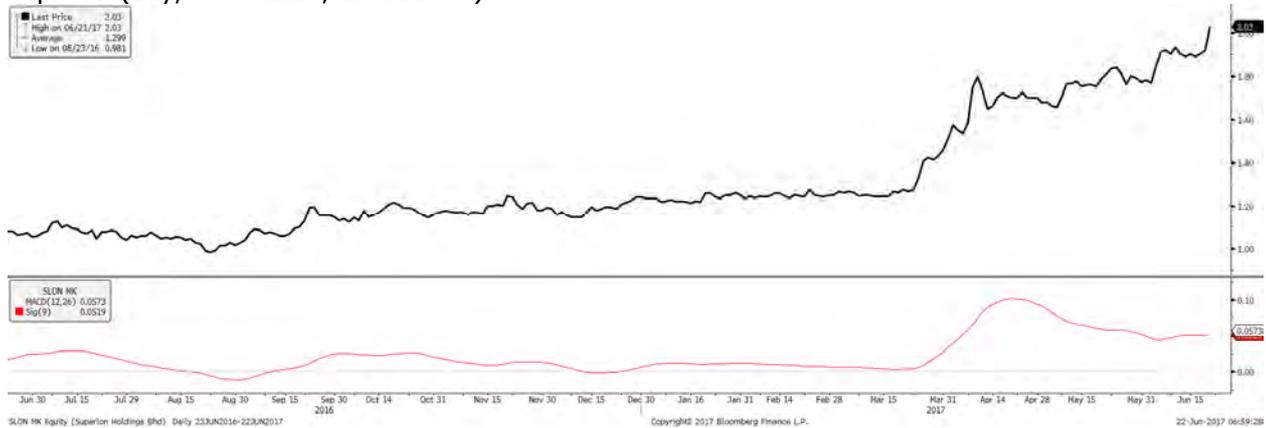
Source: Bloomberg

Ta Ann Holdings (Buy; TP:RM4.30; EPR:21.5%)



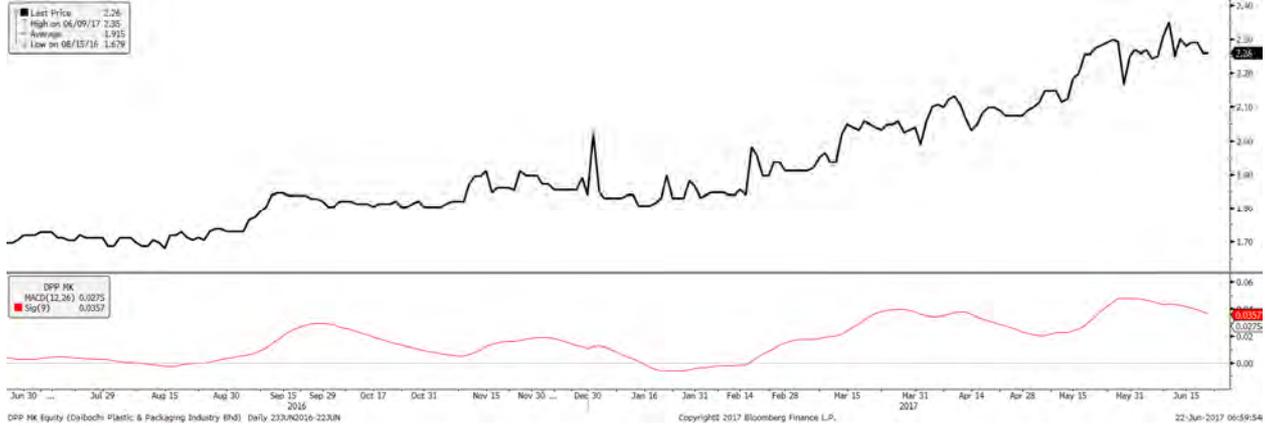
Source: Bloomberg

Superlon (Buy; TP:RM2.26; EPR:11.3%)



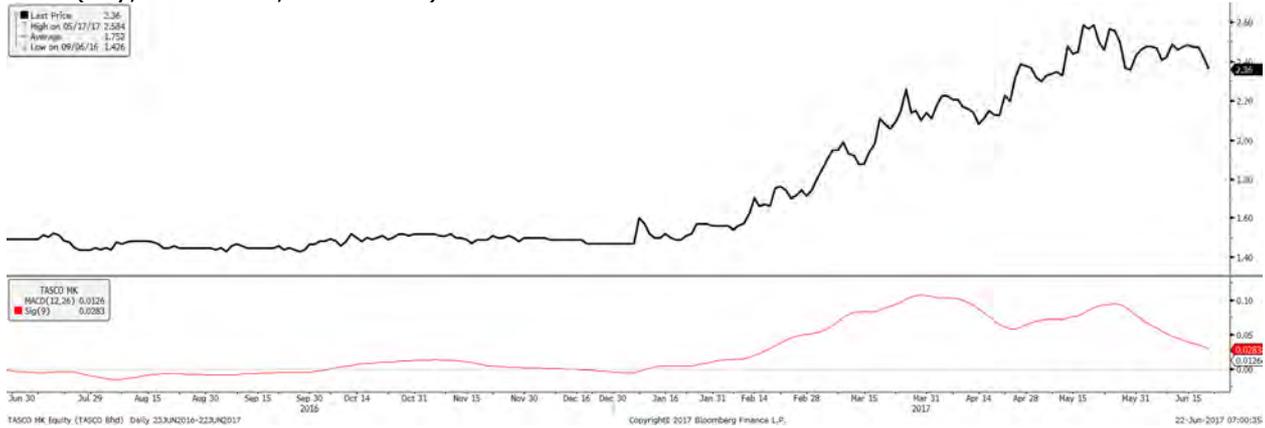
Source: Bloomberg

Daibochi (Buy; TP:RM3.02; EPR:33.6%)



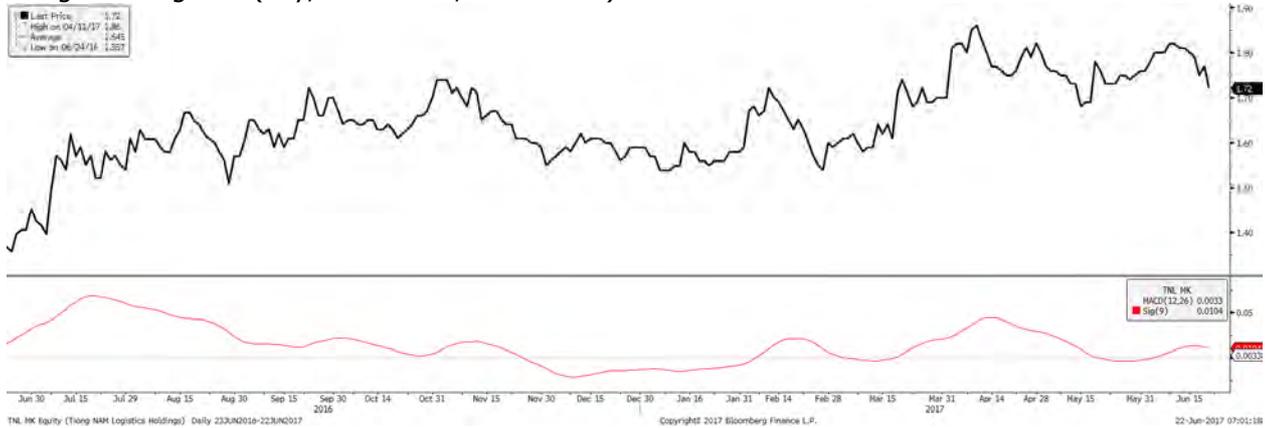
Source: Bloomberg

Tasco (Buy; TP:RM2.91; EPR:23.3%)



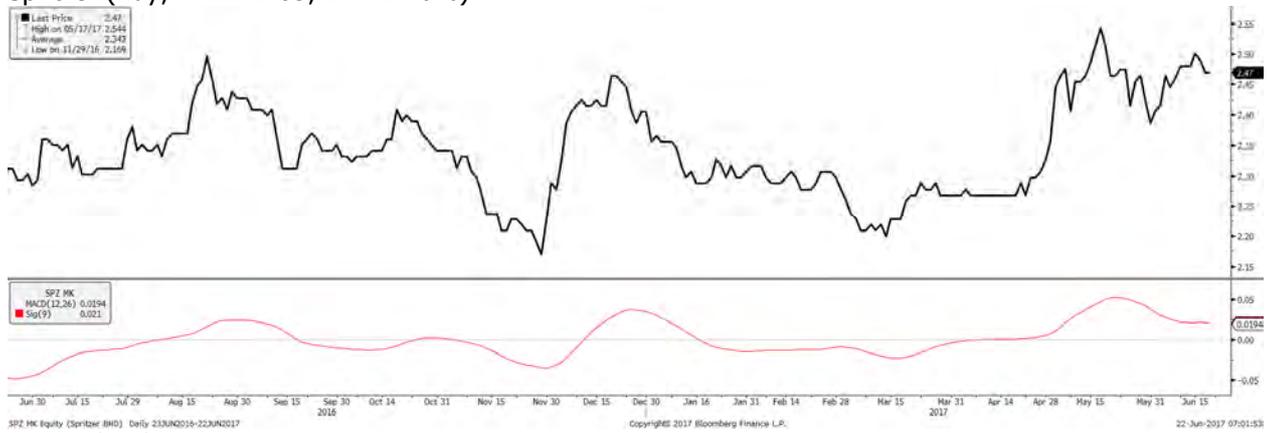
Source: Bloomberg

Tiong Nam Logistics (Buy; TP:RM2.08; EPR:20.9%)



Source: Bloomberg

Spritzer (Buy; TP:RM2.83; EPR:14.6%)



Source: Bloomberg

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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 <i>rise</i> 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 <i>fall</i> 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.