

8 January 2014 | Strategy

## FBM KLCI

The likely path in 2014

FBM KLCI: 1,825.11

(2013 Year-end Target: 1,900 points)

The FBM KLCI shall continue on its upward trajectory on favourable macro conditions. The FBM KLCI is expected to remain in the upper half of its secular upward trajectory during the next 12 months, supported by expectations of (i) gentler yet still robust domestic growth momentum, and (ii) brightening external economic conditions.

### FBM KLCI: Secular Trend Channel



Source: Bloomberg, MIDFR

**Potential downside would be limited to 1,750-1,700 points range...** The largely favourable macro scenario shall limit the downside on the FBM KLCI to between 1,750-1,700 points range, beneath which resides the lower half of its secular trend channel. The lower half domain was last visited, albeit briefly, in 2H11 pursuant to the downgrade of US sovereign rating to AA+ by S&P as well as worsening sovereign debt situation in Europe.

...as major event risk is presently deemed as not imminent. Presently, we see no fundamental triggers for a revisit to the lower half of FBM KLCI secular trend channel. But then again, like in the past, the timing of the actual trigger can evade the scrutiny of the most seasoned market watchers. Furthermore, the list of the potential triggers can never be exhaustive, but some of the plausible suspects include (i) the breakdown of China's shadow banking system (with attendant consequences on property prices and overall output growth), and (ii) massive currency (capital) flight particularly from countries suffering the twin (external and fiscal) deficits. However, at this juncture, we deem their probability of occurrence as low.

**Nonetheless market upside may be capped by liquidity, earnings, monetary and valuation factors.** Despite the generally positive macro underpinnings, the local benchmark is expected to travel mostly within the lower-upper half (as opposed to upper-upper half) of its secular trajectory. We opine so on the premise that (i) incessant albeit measured withdrawal of foreign liquidity pursuant to the commencement of QE3 taper, (ii) relatively muted FBM KLCI earnings growth of circa 10% in 2014, (iii) expectation of a hike in the OPR, as well as (iv) Malaysia's relatively weak albeit improving current account situation, may put a cap to the prevailing above-mean market valuation going forward.

## Major Indices: Standard Deviation (SD) of PER (as at 3 Jan 2014)

EURO STOXX 50	+1.04
UK FTSE 100	+0.96
S&P500	+0.71
FBM KLCI	+0.68
PHIL. COMP	+0.65
MSCI WORLD	+0.64
GERMAN DAX	+0.53
DJIA	+0.35
NIKKEI	-0.02
TAIWAN TAIEX	-0.06
S'PORE STI	-0.23
SET THAI	-0.36
JAKARTA JCI	-0.49
KOREA KOSPI	-0.70
MSCI APxJ	-0.89
CHINA CSI300	-1.13
HANG SENG	-1.26

Source: Bloomberg, MIDFR; Note: data from 2006 to present

**The comparative valuation of FBM KLCI surpassed most other markets.** As at 3 January 2014, the standard deviation (SD) of price-earnings ratio (PER) of FBM KLCI stood at +0.68. At this level, the comparative valuation of the local benchmark surpassed arguably all its regional peers and lagged only few equity benchmarks of the recovering economies in US and Europe. It is noteworthy that most other major Asian equity benchmarks were trading at levels even below their secular mean PER, i.e. SD of less than zero. Thus the glaring disconnect between the valuation of the local benchmark vis-à-vis its regional counterparts leads us to believe that, going forward, there is a greater tendency for the FBM KLCI to revert back towards its mean PER, rather than otherwise.

**We reiterate our FBM KLCI 2014 year-end target of 1,900 points.** Hence, our rather modest FBM KLCI baseline 2014 year-end target of 1,900 points, with the upper and lower bounds at 1,980 points and 1,840 points respectively. 

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#### 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.