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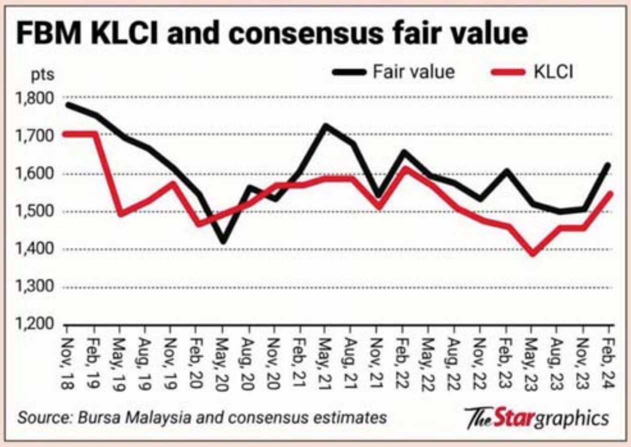
Inside insights

Rising expectations for market and reforms



Source: Bursa Malaysia and consensus estimates

ALTHOUGH the underlying strength of the recently concluded quarterly results was much better than the preceding three quarters in terms of more companies reporting earnings surprises, the core earnings momentum was marginally slower.

Still, most brokers remain optimistic with most broking firms maintaining their 2024 year-end targets while a few turned bolder with an uptick in their FBM KLCI forecast level.

Selective sectors continued to be weighed down by sector issues. This included the poor earnings from the plantation sector, except for United Plantations Bhd, which also announced a huge bumper dividend.

Glove stocks remain under pressure due to thin margins while the technology sector is still not out of the woods. Construction was a mixed bag, with IJM Corp Bhd and Sunway Construction Group Bhd posting better than expected results, while Gamuda Bhd's quarterly results top estimates.

Shining star

Property stocks, the likes of Sime Darby Property Bhd and S P Setia Bhd, also provided positive surprises, while in the aviation sector, both AirAsia X Bhd and Capital A Bhd reported core losses despite higher topline growth, while Malaysia Airports Holdings Bhd saw the second strongest quarterly results since its first quarter (1Q) of 2018.

The utility sector was a mixed bag with poor performance from Tenaga Nasional Bhd and Malakoff Bhd but YTL Power International Bhd, and to a large extent, YTL Corp Bhd, continue to deliver exceptional performance.

As for telcos, except for a decent performance from Axiata Group Bhd and CelcomDigi Bhd, others were generally in line with estimates.

Within the consumer sector, the automotive sector delivered a strong performance, led by Sime Darby Bhd, while gaming companies too showed promising results during the quarter.

The banking sector was again the shining star with strong performances by CIMB Group Holdings Bhd and Hong Leong Bank Bhd.

Malaysia's economy showed a marked slowdown in real terms, expanding just 3% year-on-year (y-o-y) in the 4Q23 period versus the preceding quarter's growth of 3.3% y-o-y.

On a seasonal-adjusted basis, Malaysia recorded a 2.1% quarter-on-quarter (q-o-q) contraction against the preceding quarter's growth of 2.6%.

The 4Q23 seasonally adjusted quarterly contraction was also larger than the quarterly contraction of 1.7% witnessed in the previous 4Q period in 2022.

However, in nominal terms, the economy expanded 2.9% q-o-q and 1.9% y-o-y to RM476.4bil in 4Q23 while for the whole of 2023, it expanded 1.7% y-o-y to RM1.82 trillion.

Surprisingly, the positive economic momentum compared with the preceding quarter was not matched by corporate Malaysia as core net earnings contracted 3.4% q-o-q but firmer by 3.5% y-o-y. Overall, last year's core earnings were disappointing as they fell 1.8% y-o-y.

Improved performance

As analyst expectations were expected to be more accurate in the 4Q period than the preceding three quarters as they have the benefit of actual results for the first half of the year, it was not surprising to see a much-improved set of results.

The ratio of companies' earnings that surprised the market against those that were below expectations improved, as 24.1% of companies reported earnings that were above expectations against 28.9% that were below consensus estimates.

This was slightly firmer than the 3Q and 2Q reporting seasons when 22.5% and 14.2% of companies reported results that were above expectations and 32.1% and 34.5% were below expectations, respectively.

Hence, the earnings disappointment ratio improved to 1.20 times from 1.43 times and 2.43 times in 2Q and 1Q period, respectively.

Following the 4Q23 results, there have been some adjustments to earnings estimates for 2024 as well as an introduction to the 2025 earnings forecast.

For 2024, from the earlier forecast earnings growth of 13.8% at the end of 3Q23 quarterly reporting period, the revised estimate now shows earnings growth of 14.1% for this year, a 0.3 percentage point increase.

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Positive inflows of RM2bil for first two months of the year

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However, earnings momentum is expected to be slower in 2025 based on forecasts made by several broking firms, which stood at a modest 8.1% y-o-y growth.

Only two broking firms have raised their fair FBM KLCI fair value for 2024 and that has now bumped up the market's forecast to 1,618 from 1,608 points previously.

Interestingly, if one were to plot the consensus estimate of the index target and the index level at the end of each reporting quarterly season as seen in the accompanying chart, it is rather telling that the market has been stuck with the average fair value of the FBM KLCI at approximately 1,600 points for the longest time, that is, for more than five years now.

The trend of change in the FBM KLCI's fair value also seems to suggest that analysts are market followers and are quick to cut estimates when the market is falling but the opposite is true when the market is rising.

While the upside between the index's current level and the fair value is now at just over 5% and earnings growth for this year has also been left largely unchanged from the preceding quarter, the question is what will it take for the index to rise above 1,600 points within the next three quarters?

Foreign inflows

With political stability well entrenched and as the government is ready to carry out reform measures, what matters to the market in the short to medium term is the foreign portfolio flows, the ringgit level as well as interest rates.

As for portfolio flows, while we ended the first two months with a positive inflow of RM2bil from foreign purchases, the first five days of trading this month itself saw an outflow of some RM1.63bil.

The sale of a 16.5% stake in AMMB Holdings Bhd by ANZ, which will see the latter repatriating some RM2.1bil, is also expected to add pressure on strategic foreign shareholding of companies listed on Bursa Malaysia by approximately 0.1 percentage point and cause some weakness on the ringgit, although some of this may be offset by foreign institutional funds picking up some 15%-20% of the block sale.

Nevertheless, recent comment by US Federal Reserve (Fed) chair Jerome Powell that the Fed would cut rates this year, but unsure of the timing of it just yet, suggests the US dollar may turn weaker this year.

As it is, from this year's high, the Dollar Index (DXY) is already down by approximately 2.1% at the time of writing. The yield on the 10-year US Treasuries too has dropped by approximately 24 basis points (bps), while the yield spread with the local 10-year Malaysian Government Securities has more than halved from a high of 49 bps to just 23 bps.

For the longer term and sustainability of the market's momentum, the government needs to deliver on the promised reform agenda – not only those related to the various blueprints that were presented last year but also political and social reforms that would lift the lives of all Malaysians.

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