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Value emerging in small, mid caps?

Investors also turn positive on wood exporters after heavy selldown

BY ALEX CHONG

KUALA LUMPUR: After taking a nose-dive and falling more than 20% last year, the ringgit has been strengthening since late January. The accommodative monetary stance by the world's major central banks and the increased risk appetite by investors saw foreign funds coming back to Malaysia, lifting up the local bond and equity markets.

Thanks to foreign investors who mainly centre on large-cap, blue-chip stocks, the FBM KLCI was up 1.5% in the first quarter of 2016 (1Q16), outpacing mid caps' 1.2% gain and a negative return of 1.4% by small caps. With large caps now more richly valued, investors seem to turn their attention to the small-cap space; aggregate market capitalisation for small caps increased 1% in the first three weeks of April, beating a meagre 0.1% to 0.2% by large and mid caps.

The outperforming sectors so far include conglomerates, banks, property and real estate investment trus, utilities, construction, plantation and particularly airlines. AirAsia Bhd's share price has soared 65.9% year to date to RM2.14, while AirAsia X Bhd shares have surged 111.1% to 38 sen. Upon a closer look, many of these outperforming stocks this year so far are high-yield stocks and/or beneficiaries of the stronger ringgit through either significant input costs being denominated in US dollars or having sizeable foreign currency-denominated loans.

Shares in AirAsia, AirAsia X and Genting Bhd, which have substantial portions of their borrowings denominated in foreign currencies, reversed their negative returns in 2015 and have surged over 30% year to date (see table 1). Similarly, utility

firm Tenaga Nasional Bhd, which has 19% of its loans denominated in foreign currencies, rose 8.3% this year. Although YTL Power International Bhd has large foreign debts, its foreign exchange impact is somewhat mitigated as a large portion of its revenue is in British pound and Singapore dollars.

TV broadcasters Astro Malaysia Holdings Bhd and Media Prima Bhd, which would benefit from lower content costs for foreign programmes, saw their share prices up 4.7% and 13.4% year to date respectively. Meanwhile, publishers Media Chinese International Ltd and Star Media Group Bhd enjoyed all-time low US dollar-denominated newsprint prices with their share prices up 17.4% and 4.3% respectively.

Consumer companies are another beneficiary of the ringgit's recovery as a stronger currency lowers their import costs and boosts consumers' real purchasing power. Apparel retailer Padini Holdings Bhd and healthcare products distributor Hai-O Enterprise Bhd, which source a lion's share of their products from China, rose 16.1% and 9.1% respectively. The strengthening of the ringgit could also provide some cushion to earnings of auto distributors amid a challenging operating environment, as component imports are mainly priced in US dollars or Japanese yen.

On the other hand, export-oriented sectors like gloves, condoms, electrical & electronics (E&E), furniture, wood boards, timbers are the worst performers in 1Q16. Case in point, board maker Heveaboard Bhd plunged 24.5% in 1Q — a big contrast to its almost 300% surge in share price last year (see table 2).

That said, investors appear to have

turned positive on wood-related exporters since the beginning of April, judging by their share price performance. As companies have yet to release their 1Q results, so what have changed investors' perception of these counters? The answer could lie in trade data released early this month, which basically point to two things: timber and the United States.

According to data prepared by the Statistics Department, exports in February reported a year-on-year growth of 6.7%, beating economists' estimate of 3.1% growth and reversing a contraction of 2.8% in January.

furniture maker Lii Hen Industries Bhd, which exports roughly 80% of its products to the US, rebounded by a sharp 17.9% this month, while Sabah-based lumber supplier Focus Lumber Bhd, which exports 65% of its goods to the US, gained 8.3% in just three weeks.

Other wood-related exporters that have large US exposure include Latitude Tree Holdings Bhd, SHH Resources Holdings Bhd and Poh Huat Resources Holdings Bhd. The positive sentiments also seem to have spilled over to exporters in other sectors with SAM Engineering & Equipment Bhd and Comfort Gloves Bhd up 1% to 2% this month.

As to what drives the stellar growth of these wood-related companies, analysts believe that the rising worldwide furniture shipments are the key driver. The US housing market, fuelled by the Federal Reserve's (Fed) ultra-low interest rate policy, has been recovering steadily from the subprime crisis in 2008.

However, the latest US housing data surprised economists with new starts of homes dropping 8.8% in

March to 1.089 million units, the lowest level since October. Accordingly, the greenback also declined to a 10-month low last Tuesday on the dismal housing data.

As the Fed board prepares to meet in the upcoming Federal Open Market Committee meeting this week, market observers opined that disappointing economic data have reduced the likelihood of rate action to virtually nil. At best, Fed members will use the April meeting statement to try to preserve the possibility of an interest-rate increase in June or July by emphasising the need for evidence of the economy's 2Q performance.

For January and February, timber and timber-based products posted a 14.1% jump from a year ago, followed by E&E products' 5.5% and palm oil products' 8%, which helped to offset a continued fall in oil-related shipments.

While exports to Japan in January and February slumped 23.4% to RM11.1 billion, this was mitigated by a strong 13.9% growth to RM12.3 billion in exports to the US, followed by a 6.2% increase to RM13 billion in exports to China. Perhaps, now it is not hard to see why wood

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Table 1: Beneficiaries of stronger ringgit

	2015	1Q16	April	% Foreign debt
1 AirAsia X	-65.3%	61.0%	31.0%	100%
2 AirAsia	-51.9%	41.9%	16.4%	90%
3 Genting	-16.9%	33.5%	-3.4%	100%
4 Tenaga	-1.3%	4.7%	3.4%	19%
5 YTL Power	6.6%	0.0%	2.0%	73%
6 Astro	-4.9%	8.3%	-3.3%	43%
7 Media Prima	-22.3%	14.9%	-1.4%	Net cash
8 Padini	36.9%	10.7%	4.8%	Net cash
9 Hai-O	12.9%	7.8%	1.2%	Net cash
10 Berjaya Auto	-4.3%	1.7%	3.7%	Net cash

Table 2: Beneficiaries of weaker ringgit

	2015	1Q16	April	% Foreign sales
1 Lii Hen	200%	-22.2%	17.9%	92%
2 Sam Engineering	191%	-13.7%	1.9%	95%
3 Comfort Gloves	42%	-16.8%	1.3%	89%
4 Latitude Tree	106%	-27.0%	3.9%	83%
5 Focus Lumber	200%	-28.4%	8.3%	98%
6 Heveaboard	299%	-24.5%	3.8%	92%
7 Inari Amerton	96%	-11.0%	-7.7%	88%
8 MPI	112%	-20.0%	-4.4%	85%
9 Careplus	106%	-18.1%	-7.9%	99%
10 SLP Resources	232%	15.8%	-4.1%	59%