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Stock market expected to be volatile till year-end

Analysts take a look at key risks to the local bourse

ANALYSIS - MARKET

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>
> *CGS-CIMB*

PETALING JAYA: The sustainability of the current stock market rally is dependent on the pace of economic and earnings recovery from the Covid-19 fallout against expectations.

According to CGS-CIMB Research, key risks to the local equity market for the remaining part of the year are when glove makers hit peak quarterly earnings, retail interest wanes and/or projected corporate earnings recovery disappoints.

The brokerage, in its report yesterday, said Malaysian equities would remain volatile till the end of the year given the uncertain environment.

"We expect the market to remain volatile in the second half (2H) of 2020 due to uncertainties on the pace of the global economic recovery as social distancing, and intermittent periods of mandated lockdowns are set to be the norm in 2H20 and 2021 until effective, mass market treatments and vaccines are available or until the infectiousness and fatality of the Covid-19 virus reduce to an acceptable level," analysts at CGS-CIMB led by head of research Ivy Ng said.

"Our key concerns going into the 2H20 lie in the ability of corporate earnings to recover to pre-Covid-19 levels, when stimulus measures progressively end in the fourth quarter of 2020, as the market appears to have already priced in this potential," they wrote.

The second and third quarter earnings season in August and November as well as political developments are likely determinants of the market direction, while among the key positives to watch in 2H20 are the roll-out of medium to long-term policy measures by the Government in October and the Budget 2021 that will be unveiled on Nov 6.

Despite the uncertainties, CGS-CIMB raised its earnings estimates for the benchmark FBM KLCI, premised on higher earnings forecasts for glove makers.

The brokerage now expects the FBM KLCI earnings for 2020 to contract 10.2%, compared with its earlier forecast of an 11.2% decline.

For 2021, it now expects the FBM KLCI earnings to rise 20.8%, compared with its previous forecast of an 18.3% growth.

Consequently, it raised its end-2020 FBM KLCI target to 1,550 points based on an unchanged price-earnings (PE) multiple target of 16 times. It had earlier projected the FBM KLCI to close at 1,496 by year end.

The FBM KLCI gained 1.48 points to close at 1,611.42 yesterday.

"We advise investors to stay defensive and venture into selective cyclicals that offer deep value for those with higher risk appetites," Ng said.

Her team noted the five investment themes for the second half of 2020 were the 15th general election play; mergers and acquisitions and deep value; dividend yield play; Covid-19 beneficiaries and Covid-19 recovery play.

They maintain their top three stock picks as Tenaga Nasional Bhd, Top Glove Corp Bhd and Yinson Holdings Bhd, while their preferred sectors were gaming, oil and gas, electronics manufacturing services, gloves and healthcare.

Meanwhile, UOB Kay Hian Research expects the FBM KLCI to end the year at 1,520, based on 16.2 times forward PE.

It said its year-end target is highly dependent on glove manufacturers' valuations.

The brokerage pegged the market support at 1,400, and blue-sky scenario at 1,630.

Kenanga Research last week raised its end-2020 FBM KLCI target to 1,618 points from its earlier target of 1,531 points.

The brokerage said its new end-2020 FBM KLCI target was based on 17.4 times estimated earnings per share of 93.2, compared with 87.8 sen previously.

This followed its upward revision in the earning estimates and target prices for the shares of Top Glove and Hartalega Holdings Bhd.

"We estimate that each 10% movement in the price of Top Glove would move the FBM KLCI by 12 points, and by eight points in the case of Hartalega," it said, noting its target price for Top Glove was RM32, and RM22.30 for Hartalega.

Overall, Kenanga concurred the market would remain volatile in 2H20.

"Our view that volatility will remain high going into 2H20 necessitates the pricing of a higher equity risk premium. It is going to be volatile because there are the uncertainties of known risks that the market will need to discount and digest as information unfold," the brokerage explained in its strategy report early this month.