AmInvestment Bank

Market report

20 Oct 2020

STRATEGY

US election 2020: A conclusive presidential vote will spark a relief rally

1,530

End-2020 FBM KLCI Target (pts)

(Maintained)

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Rationale for report: Market update

Investment Highlights

We maintain our end-2020 FBM KLCI target of 1,530 pts, pending the outcomes of the US election 2020

- We maintain our end-2020 FBM KLCI target of 1,530 pts based on 16.5x our 2021F earnings projection (+34.2%, after an 18.3% contraction in 2020F) (Exhibit 6). We have moderated our target multiple for the FBM KLCI to 16.5x from 18x (5-year historical average) largely to take the one-off spike in earnings of component stock Top Glove in 2021F into consideration.
- We believe an inconclusive presidential vote in the US election 2020 may lead to a prolonged political turmoil in the US. This could post a significant downside risk to the global financial market, including the FBM KLCI. On the flip side of the coin, a conclusive outcome is likely to unleash a relief rally globally, irrespective of who wins the presidency (Exhibit 1).

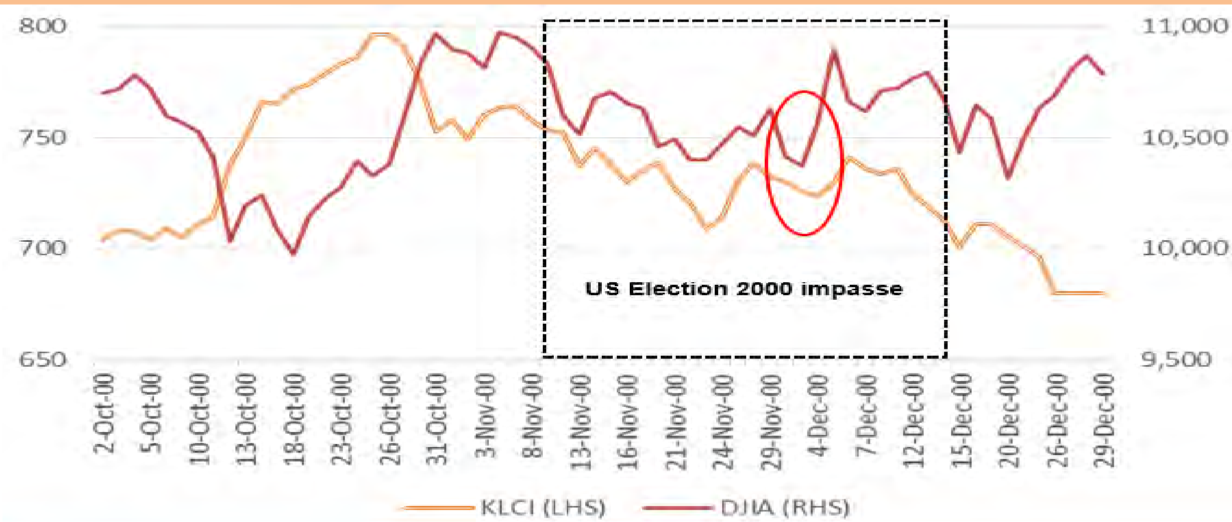
Exhibit 1: Potential Outcomes of the US Election 2020

** One party in total control of White House, House of Representatives and Senate*
^ White House, House of Representatives and Senate in control by different parties
Source: AmInvestment Bank

The market fears for an election impasse, a repeat of US election 2000

- We believe the market's concern over a potential election impasse is valid. With the election being less than two weeks away, incumbent President Donald Trump has not budged from his threat to challenge the legitimacy of postal ballots, and hence the outcomes of the election, in the court.
- Flash back to two decades ago. The winner of the presidential race in the US election 2000 between Democrat Al Gore and Republican George W. Bush, was only decided until 36 days after the 7 Nov 2000 election day. The vote came down to Florida where Bush had won by such a slim margin that state law required a recount. The Florida Supreme Court ordered so but was subsequently blocked by the US Supreme Court on 12 Dec 2000. In the end, Bush was declared the winner for the Florida's electoral votes, and hence the presidency. While Gore's legal advisors believed that he had not exhausted all legal options, Gore decided to "put country before party" and conceded on 13 Dec 2000.
- Amidst the impasse, the Dow Jones Industrial Average (DJIA) lost as much as 5.2% at the lowest point (1 Dec 2000). The FBM KLCI moved in tandem, tumbling about 5% during the same period (Exhibit 2).
- If the outcome of the presidential vote in the coming US election 2020 does come down to a court decision again, we envisage an impasse that could easily top the 36 days recorded during 2000. If that happens, we believe the potential damage to the stock market could exceed the 5.2% recorded then.

Exhibit 2: DJIA and FBM KLCI performance during US Election 2000 impasse

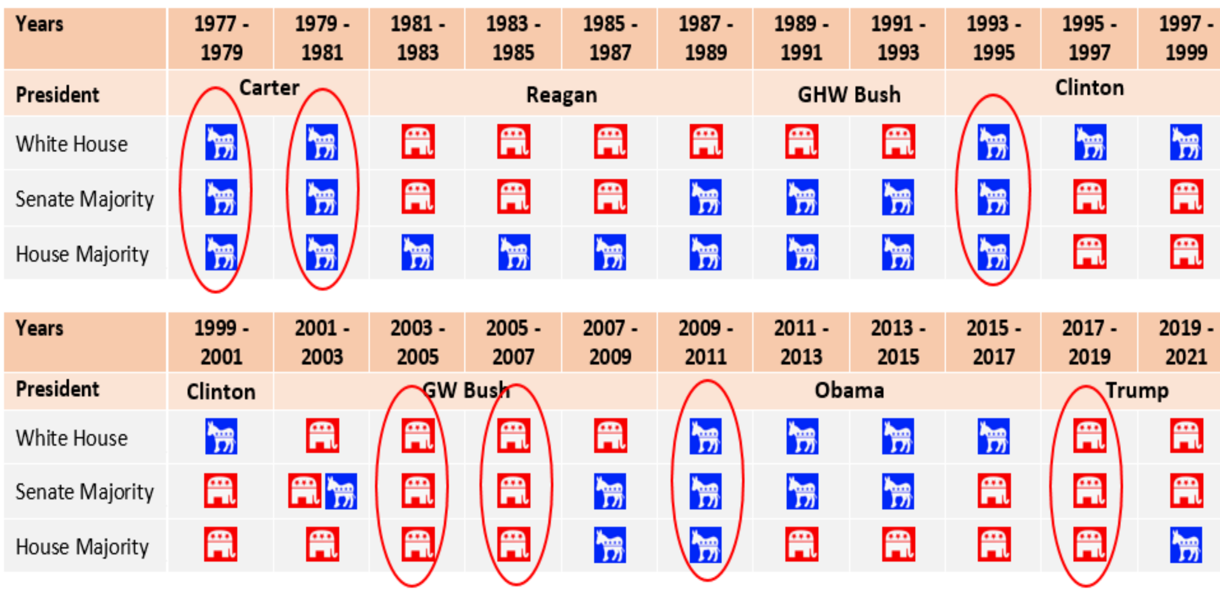


Source: AmInvestment Bank, Bloomberg

A clean sweep is good for the market

- In the event of a conclusive presidential vote, the relief rally could turn out to be even more pronounced, if one party takes control of the White House, Senate and House of Representatives. Under these scenarios – also known as a Blue Wave/Democratic sweep if the Democratic Party is to prevail, or a Red Wave/Republican sweep if otherwise – the US will be in a much better position to strengthen fiscal policy responses to shield the US economy from the fallout of the pandemic, as compared with the much-too-often deadlocks between Senate Republicans and House Democrats at present.
- Having said that, historically, the evidence for a Blue Wave/Red Wave being an ingredient for a bull market during a presidency has been mixed. A Blue Wave over four years in 1977–1981 during Jimmy Carter's presidency did not quite boost stock returns. So was the Red Wave over four years in 2003-2007 during George W. Bush's presidency.
- However, there are stark similarities between the presidencies of Bill Clinton, Barrack Obama and Trump. Their presidencies are synonymous with bull markets, and they enjoyed during their presidencies at least a Blue/Red Wave that had lasted for two years: Clinton in 1993–1995, Obama in 2009–2011 and Trump in 2017–2019 (Exhibit 3).

Exhibit 3: White House, Senate Majority and House Majority by Party



Source: AmInvestment Bank, CQ Researcher

Democrat president ushers in a bear market?

- If Democrat candidate Joe Biden is elected the 46th President of the US (and assuming that there is a peaceful transfer of power), there is still concern that the US and global markets may take a beating.

- Democrats are synonymous with high taxes and increased market regulations which will curb investment, crimp profits and stifle innovation amongst US corporations, especially, Big Tech, Big Pharma, Big Oil and banks. On the flip side of the coin, Democrats are in favour of fiscal expansion and they are advocates of free trade. These could be the potent policies to lift the US and global economies out of the pandemic doldrums.

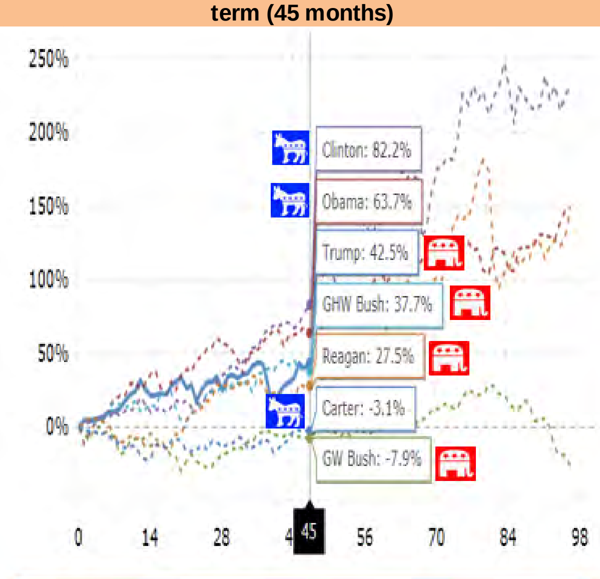
- Based on our analysis, historical data does not point to Democrats presidents ushering in bear markets. By comparing the change in the DJIA during the tenure of the last seven US presidents, namely Carter (D), Reagan (R), George H.W. Bush (R), Clinton (D), George W. Bush (R), Obama (D) and Trump (R), the numbers in fact suggest:

    1. As at the end of the first term, the DJIA recorded the best performances during Democrat presidencies under Clinton (+82.2%) and Obama (+42.5%), followed by Republican President Trump (+42.5%) (Exhibit 4); and

    2. During the full two terms, the DJIA also chalked up the best performances during Democrat presidencies under Clinton (+228.9%) and Obama (+148.3%), with Republican President Reagan (+147.3%) trailing at a close third (Exhibit 5).

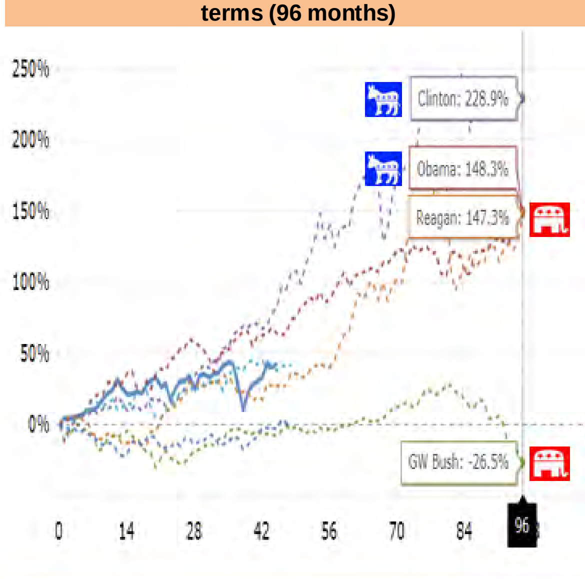
- We acknowledge this analysis could be a tad too simplistic as it does not take into account economic cycles (which arguably are also a product of fiscal, trade and even foreign relation policies of the administration). More importantly, the Federal Reserve's monetary policy has been a major driver of the financial market in recent decades (irrespective of who is or was in the White House) and the Fed is supposed to act independently in accordance with economic data and principles, at least in theory.

Exhibit 4: Change in DJIA during first presidential term (45 months)



Source: macrotrends.net, AmInvestment Bank

Exhibit 5: Change in DJIA over two presidential terms (96 months)



Source: macrotrends.net, AmInvestment Bank

Transitioning from pandemic-themed to recovery focused

- We reiterate our view that 4Q2020 shall mark the market's shift from a predominantly pandemic-themed, to a recovery-focused one. We acknowledged that the daily new Covid-19 infections have been hitting new highs in recent days. However, realising how grave the damage a nationwide lockdown could do to the economy, the government (at least for the time being) has decided against a new nationwide lockdown to protect livelihood. Meanwhile, despite the setback in certain vaccine trials, the world is no doubt getting closer to the availability of a safe and effective Covid-19 vaccine by the day.

- In addition, we believe the market shall hold up based on the following reasons:

  1. We expect the financial system globally to remain awash with liquidity over the short term, underpinned by continuous bond-buying programmes by key central banks in the world and policy rates being anchored at near-zero. With investors having had to stay invested in the market (given the low return from risk-free assets), they are likely to substitute the "pandemic play" with the "recovery play" which shall comprise FBM KLCI component stocks such as major banks, national utility company Tenaga Nasional and even telcos.

     We acknowledge that the switching to banking stocks particularly, may not be a straight-forward exercise given the uncertainty surrounding the extent of the jump in credit cost after the expiry of the 6-month blanket loan moratorium on 30 Sept 2020, and the end of the post-moratorium 3-month case-by-case repayment assistance programme on 31 Dec 2020. Having said that, in a market awash with liquidity, we believe bargain hunting will surface as and when the risk and reward balance tilts in favour of the latter in the event of another selldown in banking stocks. This happened between early June and mid-July 2020.

  2. The market risk premium is likely to remain stable as dominant players in the market, i.e. local investors, seem to have come to terms with a more dynamic political landscape in Malaysia after the 14th general election (while the view and action of foreign investors are less relevant given their low participation in the market).

- Sectors poised to benefit from the recovery in demand/pent-up demand post-pandemic are technology (as the rollout of 5G resumes), healthcare (an increase in semi-elective and elective procedures), power (an increase in electricity demand from the commercial and industrial segments), seaport (higher throughput on a recovery in the global trade), airport (reopening of borders) and auto (tax holiday and recovery in discretionary spending).

- The recovery in airlines is bumpier given the urgent need to recapitalise their balance sheets after months of massive losses amidst a collapse in air travel. Similarly, for the oil and gas industry, while China's demand for oil is recovering as its economy reopens, the fact remains that the world is chronically over-supplied with oil.

Our top buys

- Our top picks reflect names that are likely to benefit from the recovery of the domestic economy, export sector as well as global trade, i.e. **Maybank, Tenaga Nasional, Axiata Group, Dialog Group, RHB Bank, Westports, Malaysia Airports, Allianz Malaysia, MMC Corp** and **MBM Resources** (Exhibit 7).

Exhibit 6: Market Earnings Projection

	Weighting (%)	Earnings growth (%) 2019 A	2020 F	2021 F	PE (x) 2019 A	2020 F	2021 F
ALL SECTORS		(8.2)	8.5	33.8	24.9	25.8	19.4
FBM KLCI @		(7.7)	(18.3)	34.2	17.7	21.7	16.2
Automobile	2.5	(13.4)	(6.4)	27.7	15.6	16.7	13.1
Building Material	2.2	(70.3)	(23.4)	>100.0	111.3	145.4	25.7
Construction	1.7	(12.7)	(37.5)	44.7	12.7	20.2	14.0
Consumer	4.0	(24.0)	4.4	32.2	40.2	38.6	29.2
Financial Services	23.5	2.2	(23.6)	15.1	23.0	30.1	26.2
Glove	13.6	(6.0)	>100.0	>100.0	145.3	36.6	17.1
Healthcare	4.3	(8.6)	(39.6)	70.5	41.6	68.9	40.4
Manufacturing	1.3	14.5	(7.1)	37.0	19.8	21.3	15.5
Media	0.4	14.5	(29.2)	5.2	8.0	11.3	10.7
Oil & Gas	10.5	(20.1)	1.2	24.8	21.2	20.9	16.8
Plantation	8.6	57.6	>100.0	44.2	86.9	38.9	27.0
Power	6.1	(12.1)	(20.4)	29.4	12.2	15.3	11.8
Property	2.9	11.7	(26.6)	26.4	10.6	14.4	11.4
REITs	0.6	0.4	(14.5)	(3.6)	14.7	17.2	17.8
Stock Exchange	0.7	(17.0)	69.1	(15.7)	38.6	22.8	27.1
Technology	2.2	(6.3)	(4.5)	32.8	42.8	44.9	33.8
Telecommunication	10.1	(3.4)	(13.3)	12.2	22.2	25.6	22.8
Transportation & Logistics	5.0	7.4	16.2	7.3	14.7	12.6	11.8

Source: AmInvestment Bank

Exhibit 7: Top Buys

	Recomm.	Price (RM)	FV (RM)	Upside (%)	Mkt Cap (RMmil)	FYE	EPS (sen) FY20F	EPS (sen) FY21F	EPS growth (%) FY20F	EPS growth (%) FY21F	PE (x) FY20F	PE (x) FY21F	PB* (x)	ROE* (%)	NDPS* (sen)	DY* (%)
Malayan Banking	BUY	7.15	8.40	17.5	80,375.7	Dec	58.6	65.2	-20.2	11.3	12.2	11.0	0.9	8.5	50.2	7.0
Tenaga Nasional	BUY	10.00	13.95	39.5	56,436.0	Aug	69.1	89.8	-18.8	29.8	14.5	11.1	0.9	8.3	44.9	4.5
Axiata Group	BUY	2.72	4.50	65.4	24,924.9	Dec	5.7	9.5	-48.6	64.8	47.4	28.8	1.6	5.6	9.5	3.5
Dialog Group	BUY	3.72	4.85	30.4	20,974.5	Jun	10.7	11.7	12.3	9.9	34.9	31.7	4.6	15.2	4.4	1.2
RHB Bank	BUY	4.30	5.70	32.6	17,243.0	Dec	52.7	58.0	-14.9	10.1	8.2	7.4	0.6	8.2	23.2	5.4
Westports Holdings	BUY	3.88	4.45	14.8	13,230.8	Dec	18.2	19.4	-3.9	6.5	21.3	20.0	2.3	12.9	14.5	3.7
Malaysia Airports	BUY	4.05	6.64	64.0	6,719.8	Dec	(12.3)	23.2	nm	nm	nm	17.5	0.8	6.5	11.6	2.9
Allianz Malaysia	BUY	13.62	17.40	27.8	2,407.8	Dec	286.5	309.8	2.8	8.1	4.8	4.4	0.6	13.4	69.0	5.1
MMC Corporation	BUY	0.73	1.56	114.6	2,207.7	Dec	10.0	11.2	22.2	12.5	7.3	6.5	0.2	3.5	6.2	8.5
MBM Resources	BUY	2.90	4.32	48.9	1,133.1	Dec	36.8	48.0	-25.0	30.4	7.9	6.0	0.6	10.2	19.2	6.6

** FY21F*
Source: AmInvestment Bank

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