

# STRATEGY

*Malaysia: Returning to EM roots*

**1,300**

End-2020 FBM KLCI Target (pts)

(Downgraded)

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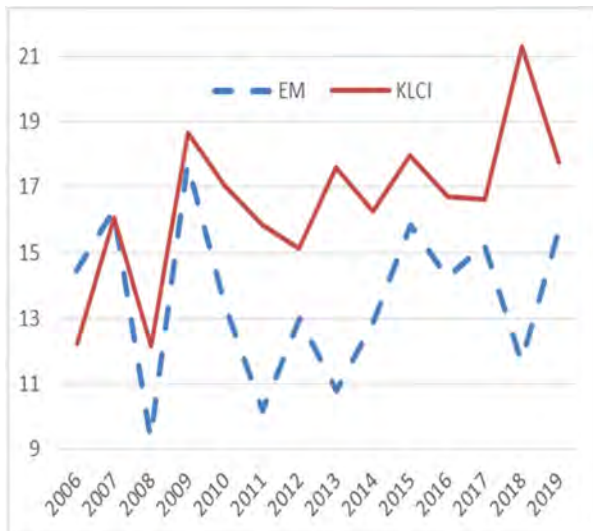
*Rationale for report: Market update*

**Investment Highlights**

**Malaysia going back to its EM roots**

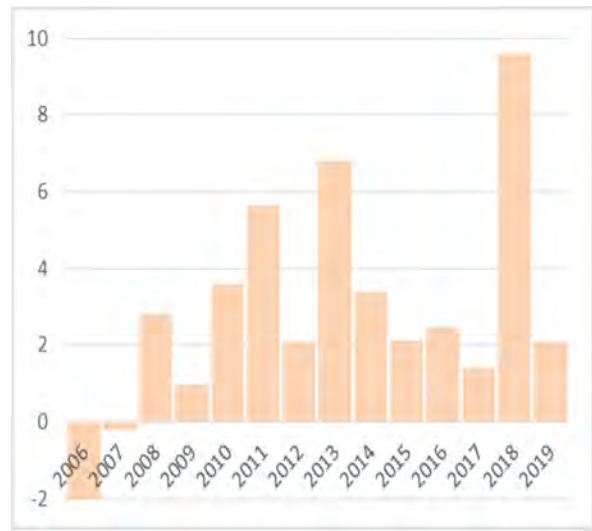
- Since 2019 or over the last 15 months, the FBM KLCI has lost 26% from 1,691pts to 1,257pts (of which 6% loss occurred in 2019 and 20% loss in 1Q2020). This compares with only a 14% loss in the MSCI Emerging Markets (EM) Index from 966pts to 827pts during the same period. This translates to an underperformance by the FBM KLCI against the MSCI EM Index of 12 percentage points.
- **We see a silver lining in the seemingly unabated fall in the FBM KLCI.** Assuming the FBM KLCI is to fall by about another 100pts from the current level to 1,150pts, this will bring the FBM KLCI in line with the MSCI EM Index's 10-year (2010–2019) average P/E of 13.3x. This will put Malaysia back onto the radar of international EM fund managers, who currently generally feel less excited about Malaysia due to its high valuations.
- The unique “Malaysian premium” over its EM peers came about more prominently after the global financial crisis in 2008. Prior to that, the FBM KLCI was indeed traded at a 2x multiple discount to the MSCI EM Index in 2006, and at par with it in 2007 (Exhibit 2). The build-up of the premium was a result of too much savings trapped locally, chasing after too few fundamentally strong large-cap Bursa Malaysia-listed stocks. The premium had been sustained despite major market de-rating catalysts such as the unfolding of the 1MDB scandal and the collapse of oil prices in 2014–2015, as well as the fall of the Barisan Nasional government during the 14th general election in 2018. We believe this was due to the availability of local liquidity during extreme market conditions in those times.

**Exhibit 1: P/E Convergence: FBM KLCI vs. MSCI EM (x)**



Source: AmInvestment Bank, Bloomberg

**Exhibit 2: FBM KLCI's P/E Premium over MSCI EM (x)**



Source: AmInvestment Bank, Bloomberg

### Nonetheless, we downgrade our end-2020 FBM KLCI target to 1,300pts

- We downgrade our end-2020 FBM KLCI target to 1,300pts based on 15x our 2020F earnings (growth of +1.8%), from 1,480pts based on 16.5x previously. We believe it is defensible to price the FBM KLCI at a slight premium to the MSCI EM Index in terms of P/E valuation given the significant presence of highly defensive (and hence high P/E) sectors, i.e. plantation and glove, in the FBM KLCI with a combined weighting of 14%.
- We remain cautious on the outlook of the FBM KLCI amidst the Covid-19 pandemic (that is disrupting global supply chains and sending private sector/consumer spending plunging), the oil price crash (that is severely hurting the government's petroleum revenues) and the delicate political situation locally (that gives rise to a higher policy risk, and hence an increased market risk premium).

### Our top buys

- As we are navigating the Covid-19 outbreak, oil price crash and delicate political situation locally, we pick defensive names such as **Tenaga Nasional, Digi.Com and Kossan Rubber**. To position ourselves beyond these air pockets, we pick a mixed bag of fundamentally strong large- and mid-cap stocks that have been sold down indiscriminately amidst the market meltdown such as **Maybank, RHB Bank, Sime Darby, Sunway, IOI Properties, Guan Chong & YTL Hospitality REIT** (Exhibit 3).

### Exhibit 3: Top Buys

	Recomm.	Price	FV	Upside	Mkt Cap	FYE	EPS (sen)		EPS growth (%)		P/E (x)		P/B*	ROE*	NDPS*	DY*
		(RM)	(RM)	(%)	(RMmil)		FY20F	FY21F	FY20F	FY21F	FY20F	FY21F	(x)	(%)	(sen)	(%)
Malayan Banking	BUY	7.36	9.50	29.1	82,145.0	Dec	74.2	76.7	1.0	3.4	9.9	9.6	1.0	10.0	57.1	7.8
Tenaga Nasional	BUY	11.24	14.60	29.9	63,434.1	Aug	88.8	94.3	4.3	6.2	12.7	11.9	1.0	8.5	44.4	4.0
DiGi.Com	BUY	3.92	4.70	19.9	30,478.0	Dec	18.8	19.4	1.8	3.3	20.9	20.2	55.1	240.4	18.8	4.8
RHB Bank	BUY	4.69	6.30	34.3	18,806.9	Dec	62.9	67.3	1.6	7.0	7.5	7.0	0.7	9.4	31.4	6.7
Sime Darby	BUY	1.71	2.64	54.2	11,629.7	June	14.1	15.8	0.7	12.4	12.2	10.8	0.8	6.4	9.1	5.3
Sunway	BUY	1.42	2.07	46.1	6,963.3	Dec	13.3	13.9	1.9	5.0	10.7	10.2	0.8	8.3	6.6	4.6
Kossan Rubber	BUY	4.89	6.07	24.2	6,254.0	Dec	23.6	22.5	32.7	-4.7	20.7	21.7	3.8	19.9	9.4	1.9
IOI Properties	BUY	0.87	1.54	78.0	4,762.8	Dec	10.3	10.8	-7.7	4.2	8.4	8.0	0.2	3.0	5.0	5.8
Guan Chong	BUY	1.77	3.53	99.6	1,784.0	Dec	24.7	27.2	19.2	9.9	7.2	6.5	1.6	24.2	5.0	2.8
YTL REIT	BUY	0.94	1.63	73.8	1,593.6	Dec	7.8	8.4	-0.4	6.9	11.9	11.2	0.6	4.9	7.8	8.4

Source: AmInvestment Bank

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