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Resumption of market rally seen next week

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LAST week, we called for a market bottom and a better fourth quarter. The reasons supporting our call, both fundamental and technical, were detailed in last week's issue and we were right!

Technically, we spotted a change in market sentiment as early as last Thursday when the market bounced off its 675 support to register a "black hammer" bullish reversal pattern. And the unprecedented "gap" of 35 points on the KLCI on Friday was another powerful signal that the market is taking off.

Fundamental news supporting this change in sentiments was also highlighted in last week's issue. Our Prime Minister Datuk Seri Dr Mahathir Mohamad had announced the lifting of trading restrictions and a deferment of mega projects in a bid to reduce our burgeoning trade deficit.

The combination of fundamental and chart signals were as clear as daylight for us to call a market bottom and a buy.

This Monday, the KLCI continued to propel itself upwards by another 58.12 points or 7.06 per cent from 821.59 to 879.71. Tuesday saw a first attempt at breaking the 900 psychological resistance since August 12, but buying interest was insufficient to stem the tide of profit-takers who had taken positions last Thursday and Friday. That led to another two down days on Wednesday and Thursday, which brought the KLCI back down to 821.02 and even to 814.16 yesterday before strong institutional buyers re-surfaced to prop the KLCI back up to close 17.91 points or 2.15 per cent, at 852.08.

Those in the market will agree that the pullback from 900.99 on Tuesday to 821.02, representing an 86.83-point or 9.6 per cent drop, by Thursday was depressing enough to question whether last Friday was another "flash-in-the-pan" rally.

Typifying the efficiencies with which rumours are disseminated via the stock market, stories abound that foreign funds are still net sellers over their lack of confidence with Malaysia's frequent change in policies. Some succumbed to these rumours and sold down, either to cut losses or take quick profits, if they had bought last Friday.

But I think it is a big mistake if they have done so because, firstly, the volumes were relatively small on Tuesday and Wednesday even if the KLCI had corrected 86.83 points from its high of 900.99 to 821.02.

Put things in perspective. One must not forget that the KLCI had rallied a total of 22.5 points or 33.3 per cent from 675 to 900 in just four sessions. Given the phenomenal rally, a correction is expected and in the present case, it merely corrected one-third of its prior move. Yesterday's rebound from the one-third support of 814 was very technical indeed!

With yesterday's bounce to close at its high of 852.08, readers who understand charting need not be told where the market will be heading next week, at least not on Monday morning. Yes, the market is going to go "up". The first chart pattern supporting this bullish forecast is the Japanese "piercing line" pattern established on the KLCI and bullish "harami" pattern on the second board index.

The second chart pattern pointing to a possible resumption of uptrend is the Western "flag" etched out by these three days of correction. A "flag" is a short-term consolidation pattern which should give way to a breakout in the volume above 400 million shares for the main boards to confirm the

return of the bulls.

There is a strong chance of another powerful rally next week. Thirdly, the V-type pattern we spoke of many weeks ago is now taking shape. It will not be an ideal "V" but one with a right extension. We believe that the correction these three days was very healthy and yesterday's rebound shows that whatever profit-taking was well absorbed and we now have a strong platform to launch another rally. Next targets are 1,051 to 1,080. The 938 resistance should not pose much problem.

Incidentally, this week's V-type pattern bears some uncanny resemblance to the V pattern of 1995 (see chart). And the reasons for the selldown in 1995 also stemmed from foreign fears of Malaysia's economy "overheating" and its worsening trade deficit pegged by foreign analysts at RM16.8 billion.

The selldown commenced on August 3 1995 at 1,077 and by November 14 1995, the KLCI was down to 880 before stern measures, similar to the ones announced by Finance Minister and Deputy Prime Minister Anwar Ibrahim on Wednesday, triggered an about-turn.

Note that the strong rally that followed after November 14 1995 had a brief consolidation of three sessions (labelled as a "flag" in the lower chart). Note also the "flag breakout" afterwards in the 1995 scenario. The interesting question is, will history repeat itself?

If so, and there is a high probability of it happening, we expect a sharp rally to complete this V-type pattern, just like in the 1995 chart.

Fundamental news are aplenty to back this resumption of a rally next week. This weekend, Dr Mahathir and Anwar are expected to meet with 30 to 50 foreign fund managers in Hong Kong. Back home in Malaysia, the Government is already acting to reduce our trade deficit by reviewing or even freezing projects approved by the country's 13 state governments. Government spending is expected to be reduced by 2 per cent.

And to underscore that foreign investors are market chameleons who bear no permanent grudges and are adept at "gostan" or turning around if conditions change, Rothshild Asset Management Singapore's chairman has this to say about Asian markets: "The funds will be back within a year. Investors will have little choice but to come back. Where else can they go? ... Where else will they see the growth that we see in Asia? Very soon we will see a spectacular turnaround in Asian stocks." And I totally agree with him!

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