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Stocks likely to stage further recovery

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THE downtrend which started on February 28 at 1,270 looks like it is over. This is because of the market's failed attempt to breach its 880 support.

As I anticipated in last week's Market Trek, the KLSE Composite Index (KLCI) came sharply down on Monday by 30.22 points to close at 903.22. By Tuesday, the KLCI was poised to test my 880 support. The KLCI came sharply down once again on follow-through selling by foreign funds in early morning trade on Tuesday but this was abruptly reversed in afternoon trade as bulls staged counter-attacks after hitting major supports and bouncing off them, resulting in many etching out bullish reversal patterns such as engulfing bullishes, hammers, piercing lines, haramis or inverted hammer patterns.

A small black hammer was formed as a result, indicating a possible reversal signal. Tuesday's price action is significant and worth deliberating further. Readers may like to know that Tuesday's rebound was not coincidental and it is not that analysts got lucky by quoting the 880 level as the market's major support in their reports.

The 880 support level was in fact the low established on November 14 1995 and it is significant because it represented the day when the Malaysian Government announced a deferment of mega projects. The move was in response to the trade deficit of RM16.8 billion arising from the mega projects due to be undertaken.

"Overheating" of the Malaysian economy was the excuse used by foreign funds to justify the sell-down of Malaysian stocks that started on August 3 1995. In this 1995 downtrend, the KLCI slumped from 1,072 to 880 for a 192-point loss or 17.9 per cent.

Note that last Tuesday's rebound was a result of news similar to that which caused a rebound on November 14 1995. On Tuesday, Deputy Prime Minister Datuk Seri Anwar Ibrahim announced that Malaysia may defer some big import items and less important infrastructure projects to cushion the impact of the ringgit on the trade account.

But there is another supporting factor which should be viewed as bullish for the ringgit. This came from the International Monetary Fund and Asian countries' pledge to contribute to a US\$16 billion (US\$1 = RM2.79) package to rescue Thailand's economy.

Those two important factors were responsible for the sentiment change on Tuesday. The subsequent two-day rally posted a 21.29-point rise on the index, something not seen since July 18. This week's recovery would have been ideal if not for yesterday's correction of 8.36 points, reportedly coming from the ringgit's renewed weakness when it broke through the 2.800 barrier to 2.8250, its weakest post-flotation level.

I would view Tuesday's test of the 880 as a major bottom. I do not expect the KLCI to test 836 as I had forecast last week. This change in my view is because, technically, the 836 low recorded on January 24 1995 was an "aberration". It was a two-day false breakdown which was redressed in the next four days by a recovery to above 880.

By and large, 880 is our major support. Also, the 880 support that held on Tuesday is significant because it was backed by fresh fundamentals.

The announcement by Anwar, for example, should be a strong enough hint that the ringgit's decline is coming to an end. Fund managers should take the cue from Anwar and start purchasing ringgit before it strengthens once more. Buying stocks now would be most favourable for foreign funds which

had cashed out of the Malaysian market when the ringgit was around 2.52-2.60 and the KLCI at the 1,100-1,200 level.

Factors to consider which are going to change investors' perception about the ringgit and Malaysian stocks are:

- * The Thai bailout of US\$16 billion by IMF/Asian countries;
- * Anwar's announcement of deferment of mega projects;
- * Overnight rates softening to 5.5 per cent;
- * Rumours of an SRR cut of 1-2 per cent which could pump RM6 billion-RM7 billion into the banking system;
- * The Dow's continuing correction;
- * Prime Minister Datuk Seri Dr Mahathir Mohamad's confidence that Malaysia will register a budget surplus for 1997.

My position is that fears of a further currency destabilisation have already been discounted by the stock market. I think that foreign funds have started to turn BUYERS. This can be implied by the lack of selling pressure since Monday (except yesterday) and instead the presence of support every time prices fell.

It is impossible for local funds to prop up the market for four days without foreign support.

I see yesterday's correction as merely "profit-taking", and prices should recover once again next week to continue a V-bottom type of formation which typifies the Malaysian market. Funds should start to accumulate as it is possible that we may not be seeing these prices for quite a while.

From September onwards we should see a much better market.

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