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`Flag' pattern may give way to an upside trend

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THE benchmark Kuala Lumpur Stock Exchange Composite Index (KLCI) ended the week lower by 12.79 points or 1.4 per cent at 912.66 as investors remained sidelined ahead of the US FOMC meeting next Tuesday.

Fears of an interest rate raise could trigger sharp declines on the Dow which would likely rub off onto Asian bourses including Malaysia.

Already reacting ahead of these fears, jittery investors dumped stocks across Asia this week. Thai stocks were the worst hit, suffering a loss of 8.9 per cent to close at 345. Fears of further weakening of the Thai baht and an implementation of some form of capital controls to stop its slide had unnerved investors in Thai stocks.

The next biggest loser this week was Japan. The Nikkei 225 issues lost 5.8 per cent to close at 17,357, its lowest close since October 1999. Singapore stocks, apparently the "safe haven in Asia" whenever there is a crisis, was not spared either, as investors sold ahead of impending weakness of the Dow. Week-on-week, it lost 91 points to close at 2,026 after testing a major support of 1,980.

Hong Kong stocks could have been a major fatality if not for yesterday's strong rebound of 619 points. As at Thursday's close, the Hang Seng Index was down by 776 points to 14,492 before a 619-point rally yesterday brought it back to close above the 15,000 level, at 15,111. Week-on-week, the Hang Seng Index lost only 1 per cent.

This week, Malaysia's Second Board Index (SBI) reacted in tandem with Asian bourses, primarily influenced by tech stocks' sharp plunges across Asia, all of which emanated from Nasdaq's 8.3 per cent plunge. The SBI lost a "hefty" 11.3 points or 4.2 per cent to close the week at 259.98.

With the much dreaded FOMC meeting next Tuesday where the Fed is expected to raise interest rates by at least 50 basis points, it is not too surprising that players are opting out of the market in anticipation of further weakness next week.

This accounts for the negative close on all Asian bourses this week! Come next Monday, some players may even be tempted to unload stocks further for fears of a plunge on Wall Street. There were even soothsayers predicting a "crash" come May 16.

Our views are as follows:

- \* Given the negative sentiments surrounding the world's largest market - the US - where investors of lesser markets look to for market direction, it is only normal that they sell and stay out of their own bourse given the uncertainties of the Dow and, especially, the Nasdaq.

- \* Malaysian players are not different when it comes to herd instinct. As they see regional bourses falling like ten pins, it is only natural that they unload their Malaysian stocks ahead of the "financial typhoon" that they see blowing this way.

- \* But much as we agree that Malaysian stocks were affected to a certain extent by this psychological typhoon, we observed that falls of our stocks were one of the least severe among Asian bourses.

- \* Note from our research of selected market performances this month (see chart) that month-to-date (May 1 to 12) Malaysian second board stocks were the best performers among Asian bourses (this despite this week's falls). Our SBI is still higher by 6.5 points or 2.5 per cent to close at 259.98. Next best performer in our selected list is South Korean stocks which is higher by 14 points or 1.9 per cent to 740 month-to-date. Third was our

KLCI, which despite yesterday's rout of 8.5 points and a weekly loss of 12.79 points, still managed to close higher by 14.3 points or 1.6 per cent on a month-to-date basis.

\* The rest of the Asian bourses still in negative territory (in order of severity) on a month-to-date basis are Thailand (-11.3 per cent), Singapore (-6.3 per cent), the Philippines (-3.7 per cent), Japan (-3.4 per cent), Hong Kong (-2.6 per cent) and Taiwan (-2.5 per cent).

Why is it that Malaysian stocks are still the favourite among fund managers and investors? Why are they still supported inspite of falls in the bourse which was once considered a "safe haven".

Our views:

\* Fundamentally speaking: From the fundamental view point, Malaysian stocks are attractive for the following reasons: Its interest rates are coming down while others are rising; the Malaysian ringgit is considered by many to be under-valued. This should continue to attract an inflow of foreign funds; Malaysia's fixed currency rate is a safe haven for hot monies fleeing from weakening Asian currencies like the Thai baht and Aussie dollar; and not to mention the almost forgotten news Malaysian stocks' reinstatement into MSCI by the end of May. And politically, the smooth Umno elections so far will also have removed some uncertainty over the future of Malay leadership.

\* Technically speaking: Technically, note that although the KLCI, at 912.66, is now below its moving average support, it is still above its May 5 low (908). Yesterday's 8.05-point loss is acceptable as it is a result of force-selling from the high volume day of May 5. Of course the rumour in town that triggered some selling yesterday was talk of a rift between Prime Minister Datuk Seri Dr Mahathir Mohamad and Finance Minister Tun Daim Zainuddin and failed talks in the telecommunications sector. But judging from the low volumes clocked and most stocks' inability to close below their May 5 low, the market's reaction to these news is not severe enough to trigger a sell signal, even if there is some truth to the rumours.

Come next week, selling pressure should be well over. The next critical support to look out for is 904 to 908 levels. They should provide the support in the event of further falls. And lastly, for those who still believe that a head-and-shoulders pattern is still possible, then it has to break its neckline which is the 890 level.

We view this week's pattern as a "flag" within a bigger consolidation pattern called a "wedge". This sideways pattern should give way to a trend which is likely to be resolved on the upside. Players should look for higher volumes to confirm a resumption of play.

And with Asian countries now being exposed to the currency volatility and high interest rates, Malaysia should be the safe haven that foreign funds will find attractive. Here is where they will likely place their money. With that being our view, investors should continue to hold on to their stocks and not sell just because of fears of an interest rate raise in the US next Tuesday or because of weakness in Asian bourses. There are times when Malaysian stocks trend in a different direction from them because of differing fundamentals. This could be one of these times where we may have decoupled ourselves from others.

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