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Consolidation phase for market likely this week

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STOCKS on Bursa Malaysia Bhd succumbed to selling pressure last week as investors locked in profits from the recent rebound.

New evidence of weakness in the US economy and concerns over negative impact from the renewed increase in oil prices also weighed on the equity markets, both domestically and globally.

As expected, trading began on a weak note last Monday as profit-taking on overbought stocks and contra-selling from the high trading volume generated in the previous week dampened prices. Selling pressure persisted into the mid-week on lack of stimulating leads and weakness in global equity markets.

During the week, there were growing signs that the US economy might be headed for a slowdown. Corporate earnings, especially that from technology stocks, spooked optimistic investors. Economic data were also below expectations. Industrial production for June posted a surprise decline after strong showing in April and May. The 0.3 per cent decline from the prior month was the largest since April last year.

Meanwhile, retail sales and consumer sentiment index also showed poorer-than-expected figures. Taken together with a lower-than-expected increase in consumer prices, which in itself is a mixed blessing, the latest data point to a possible slowdown in the US economy. Hence, we expected the market to pay close attention to Federal Reserve chairman Alan Greenspan this week when he testifies before the Congress.

The slowdown in the external front would have great impact on the local economy. Apart from the US, our largest trading partner that is showing signs of slowdown, the latest economic numbers from China also suggest that the economy is cooling down. and possibly achieving the soft-landing scenario that it wished.

Setting against this backdrop, however, is the recent Malaysian Government's announcement that it is allocating an additional RM10 billion for economic development under the Eighth Malaysia Plan and the commitment to dish out more infrastructure spending in the second half. Putting the two and two together, this would show that the Ggovernment has a great foresight in economic management.

Indeed former Prime Minister Tun Dr Mahathir Mohamad pointed to possibility of Malaysia raising its current gross domestic product forecast of 6 to 6.5 per cent when he alluded to a strong growth in the second quarter and in the second half. Such signs of strength in the domestic economy may underpin market upside, but in the meantime, the market is looking at earnings reports from the local corporate sector that are due over the next few weeks.

#### Technical Outlook

The Kuala Lumpur Composite Index (KLCI) slid 11.41 points, or 1.3 per cent, to close at 842.65 points for last week, the first weekly decline in four weeks. The average daily trading volume shrunk to 290.1 million shares from a three-month high of 409.5 million shares the previous week, as lack of follow-through buying interest dampened trading activity. The KLCI July futures closed at 846.5 point for a near four-point premium to the cash index, shored up by a technical rebound last Friday.

The KLCI fell from an early high of 854.79 last Monday as profit-taking on overbought stocks and weak follow-through buying caused the index to slide to 837.65 low last Thursday. However, a technical rebound last

Friday lifted the index and the broader market off their lows for the week.

The daily slow stochastics indicator on the KLCI has fully neutralised its previous overbought momentum and fell down to the neutral zone with reading of 40. However, the weekly stochastics continued to ascend and has just entered into an overbought territory with reading of 84, which could restrict medium-term upside momentum.

Meanwhile, the 14-day and 14-week Relative Strength Index (RSI) are hovering at the neutral region with readings of 56 and 54 respectively, indicating consolidation process on neutral technical momentum.

On trend indicators, the daily Moving Average Convergence/ Divergence (MACD) has developed a hinge and could potentially trigger a near-term sell signal. Meanwhile, the hook-up on weekly MACD has levelled off below the trigger line and will delay a potential medium-term buy signal.

The daily ADX on the Directional Movement Indicator (DMI) has topped out and turned south to reverse last week's bullish hook-up to cross above the -DI line, thereby erasing potential for strong uptrend in the near-term. The weekly ADX has levelled off on expanding +DI and -DI lines, which is positive, but needs further confirmation of bullish momentum to sustain uptrend.

#### Conclusion

The weaker momentum and mixed trend indicators for the KLCI suggest that a consolidation phase is in order. With short-term overbought momentum fully neutralised, range- bound trading for base building process may follow to reinforce stronger support. The KLCI will need to hold above its 30-day Simple Moving Average (SMA), currently at 830 and rising, to sustain the current upward momentum with 200-day SMA at 822 acting as strong support platform.

The return of active daily trading volumes of above 500 million shares will be crucial to spark strong rebound and promote further upside potential to challenge the resistance from the recent high of 858.

Selective lower-liners and second board stocks with positive news flows might attract active rotational plays.

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