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Consolation of consolidation

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SHOULD CAUTION AND SCEPTICISM be the order of the day? This question is being increasingly asked by stock market investors these days. One school of thought says a little scepticism is healthy, especially in these volatile times.

The problem however is that if you have been sceptical, then chances are that you would have missed out on the recent rally experienced by the Kuala Lumpur Stock Exchange (KLSE).

Still, most investment advisors suggest a moderate level of scepticism in light of recent events. Case in point: the recent bomb blast at JW Marriott Hotel in Jakarta, as this confirms terrorism is still very much alive today. Hence the sceptical investor is one who will maintain a diversified portfolio and is able to discipline himself to avoid being taken in by small rallies in the stock market.

But that's not to say the stock market should be avoided. The recent bomb blast in Jakarta is believed to have only a short-term impact on markets. True, the long-term effects take the form of acting as a stumbling block to efforts by regional governments to woo back foreign funds, but as far as the stock market goes, the impact is minimal for now.

Economists say this is because the severity of the latest terrorist attack did not come close to that of the Bali bombing in October 2002. The Bali blast was a much more direct attack on regional tourism and had greater repercussions compared to what happened in Jakarta, say economists.

Markets are sentiment-driven

But it is only natural that equity markets in the region fell in a knee-jerk reaction to the incident. Japan, South Korea and Hong Kong experienced the sharpest slides. Similarly, the KLSE Composite Index (CI) shed one point to close 722 on Aug 8, from the 723 closing on Aug 1.

It should be noted however that at the time of the incident, the local stock market was already in a consolidating phase. Thus the news of the blast only served to enhance this.

Analysts reckon that based on prevailing market sentiments, the KLSE is likely to move sideways with a possible downward bias. For the short term, the CI is likely to find support at the 720 level and encounter resistance at around the 735 point.

After surging past the psychological 700-point level on July 2 and peaking at 730 on July 7 the local bourse has been consolidating.

For the past two weeks, the CI has been trading below the 720 mark with many investors taking profits, given the strong gains that have been chalked up over the last two months.

In terms of trading volume, the numbers show a healthy trend. In the last two weeks of July, trading volume averaged 559 million units per day. While this is less than the daily trading volume of 851 million units in the first two weeks of July, it is still an improvement over the average daily volume of 225 million units in the first five months of the year.

Investor interest seems to have shifted to smaller capitalised stocks, namely those of the Second Board and MESDAQ Market.

Initial public offerings (IPOs) are also the flavour of the market, judging by the attractive premiums achieved by recent debutantes.

The few companies that went public in July saw their shares registering premiums of not less than 24% over their initial public offer (IPO) prices at the close of their first day of trading. In comparison, the KLSE CI only rose about 4% month-on-month in July.

Theme plays

One theme that caught investor interest in July was oil and gas,

following the discovery of new oil reserves in Kikeh, off the coast of east Malaysia. Most stocks in this sector surged on expectations of greater potential in exploration and production (E&P) activities in view of this latest discovery.

But a comment by Petroliam Nasional Bhd (Petronas) president and CEO Tan Sri Mohd Hassan Marican in late July put the brakes on this conceptual play. He said the national oil company did not plan to increase its spending on E&P activities. He also denied the company had dished out contracts worth between RM2 billion and RM3 billion to local oil and gas companies.

Going forward the next investment theme is said to that of water-related stocks given that government allocations for this sector have been growing by 8% per annum. Despite the amount spent over the years, sufficient and clean water supply remains a major issue and to address this, a RM52 billion National Water Policy is on the drawing board.

Covering a period up to 2050, the annual allocation under this policy works out to about RM5 billion per year and involves large capital expenditure works to raise national water supply to meet demand from the growing population. The Federal government's decision to take over state water matters is also aimed at bringing about more efficient management of water resources in the country.

Theme plays aside, analysts say small-capitalised stocks will remain in the limelight for the immediate term, but they point some of these stocks could be in an oversold position and investors are advised to exercise caution when investing in them.

Good news are a boost

Be that as it may, the underlying tone of the market is firm, supported by more positive economic data coming out from the US and locally. The US economy grew at 2.4% in the second quarter, which far exceeded economists' forecasts of 1.5%.

Locally there are indications of economic resilience. With the Industrial Production Index (IPI) having been on the upside in recent months, we could potentially see a further upgrade in economic growth in coming months. Malaysia is expected to post GDP growth of at least 4% for the second quarter of this year after exports rose 6% year-on-year in June.

The corporate results season in August and September could potentially see some positive surprises as well. So far companies have not done badly, sparking optimism that earnings may exceed analysts' expectations.

The announcement of other investor-friendly measures in the last couple of months, the latest being the relaxation of the 30% bumiputra shareholding quota for listed companies, are seen as positive for the equity market.

And for the immediate term, investors would be looking at the unveiling of the 2004 Budget on September 12 for some excitement. Analysts are expecting a people-friendly budget given that elections are expected by next year. Bearing in mind that this will be Datuk Seri Dr Mahathir Mohamad's last Budget, we could see the introduction of more measures to stimulate domestic spending in the country, say analysts.

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