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Pre-budget buildup

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THE ATTENTION OF THE MARKET early in the month was on the Budget 2004 unveiled on Sept 12. At the time of writing, the mood in the market was already turning bullish ahead of that day. On Sept 5, the benchmark KLSE Composite Index closed at its highest level for the last 15 months at 756.48 points.

But not all stocks are on the rise. The rise of the CI, which has enjoyed a 13-point gain week-on-week, is largely due to large institutional funds buying up index-linked counters such as Maybank, MISC, Genting and Maxis.

On the other hand, lower liners and speculative stocks, which have chalked up significant gains in recent weeks, saw selling pressure in the month of August.

In fact, the Second Board Index has suffered because of substantial declines in prices of some shares, namely that of furniture manufacturer Kimble, engineering-related company Kai Peng and livestock feed manufacturer and duck breeder EMIVEST.

These counters have been the punter's favourite in recent weeks, until they suffered their decline. Still, observers should recall that about a year ago, the same fate befell some other Second Board stocks when investors speculated and chased these stocks to new highs in a short period. Their stock prices declined not too long after.

But the interest in initial public offerings (IPOs) is still strong as seen by the superb opening prices, and this has somewhat overshadowed the broader market performance.

However investors should note that new listings have tended to have low absolute prices and this in turn has exaggerated the percentage gains. Remember that some counters were offered below RM1.

So the focus has turned to laggard blue chips to push the KLSE CI higher, especially those that had reported better than expected results during the recent reporting season.

With the fundamentals of the local and global economy intact, investors believe the market is in its last leg of its second major consolidation since May, with local institutions taking the lead and their interest reverting back to quality stocks at the expense of lower liners.

The US and Japanese stock markets in the last few weeks have broken some key resistance levels, indicating a global economic recovery is underway. Malaysia recently released its second-quarter growth rate of 4.4% that had surpassed most economists' forecasts of below 4%. In addition, the corporate earnings reported by Malaysian-listed companies showed the impact of the Iraq war and the SARS virus was not as bad as earlier envisaged. This puts Malaysia well on track to achieve the 4.5% official growth target for 2003, with some economists expecting it to surpass 5% next year.

A pat on the back for the country's leadership in steering the economy through the difficult period post 1997-Asian financial crisis came from one of the country's most vocal critics, the International Monetary Fund (IMF). Its managing director Dr Horst Kohler, in a recent visit to Malaysia, had said the country was right to take destiny into its own hands by the imposition of capital controls and pegging the ringgit at RM3.80 to the US dollar. With the exception of the peg, the capital controls have been lifted.

Traditionally the market normally stages a 'rally' ahead of Budget as investors take positions - based on speculation of possible measures and their beneficiaries as well as losers - on selected sectors and stocks. It should be noted though that the last few Budgets have turned out to be

relatively neutral with regard to the stock market.

But investors are expecting a different Budget this time around, considering it will be the last for Prime Minister Datuk Seri Dr Mahathir Mohamad before he steps down in October, and also the last before the next General Election.

While some analysts are not expecting the Budget to steer away from the goal of stimulating the economy via fiscal spending, there are indications the government may provide incentives for the private sector to take the lead. Second Finance Minister Datuk Dr Jamaluddin Jarjis recently indicated Budget 2004 would stress on the private sector as the engine of economic growth. Market watchers were betting on a 'people-friendly' Budget.

Going by the 1993 levels, investor interest in the stock market is still relatively mute despite their increased risk appetite and the excess liquidity in hand. Local brokers have started to offer more aggressive financial packages, especially for retail investors. For margin accounts, settlement periods are being extended from T+3 to as high as T+10, to spur 'contra-traders' who were major players in the last bull run.

And the return of more foreign funds to this region, in search of more attractive valuations, could substantially boost the market. In July, KLSE officials said foreigners accounted for 30% of business done on the local bourse in the first half of the year. A bigger participation by these players are needed for the strong rally; and the fact that the Malaysian economy has emerged as the best-performing economy in this region should put the country on the radar of international investors. As it stands at the moment, the KLSE is still trading at a discount to its regional peers.

Given these considerations, the outlook for the stock market appears bright for the rest of the year. The current pre-Budget rally could create momentum for the market to generate another bull run that could possibly extend to the Chinese New Year. The 800-point level earlier predicted may become easily achievable and Malaysia could well catch up with its regional peers and regain the traditional premium valuations it used to enjoy.

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