Apex INVESTMENT SERVICES BERHAD (420390-M)
20 years and beyond

Portfolio Manager’s View

17 August 2021

Fund Management Department

Regional

1. After China's weaker than expected July Caixin Manufacturing Index, subsequent economic releases were just going to point in one downward direction. Therefore, this week's poor July retail sales, industrial output, and fixed asset investment numbers were no longer surprises to the market. And the continued closure of Ningbo Port since last weekend, the third busiest port in the world due to Covid-19 outbreak, will negatively impact even the more resilient export sector. China's GDP third quarter of 2021 may look ugly. And it is this very reason we believe that June's 50bp cut in reserve ratio requirement is only the beginning of China's shift to an easier monetary policy.

2. This week, it was revealed that the Chinese Government has taken a 1% stake in ByteDance which gets a board representation as well. This must go down in history as the smallest shareholding stake that has gotten any shareholder almost absolute control over a company. The Chinese internet sector will continue to be brought to heel. The message is also clear that the avenue to future public listings, especially those now with a Chinese Government shareholding can only be in China's domestic stock exchanges. Nasdaq and most other foreign stock exchanges are no longer viable options for companies such as ByteDance anymore. Any investor hoping to participate in China's

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future growth can only be through the growing and more influential domestic capital markets under the more watchful eyes of the Chinese Government.

3. The US Federal Reserve's Annual Policy Retreat at Jackson Hole will be held at the end of August. Investors are already looking towards this event for any signs of a definitive change in the US Fed's monetary policy. Meanwhile, there remains quite diverse opinion among the US Fed members on when is the right time to start asset purchase tapering. Whatever and whenever this decision is made, it is expected to create some volatility to markets. We are of the view that it is not the beginning of this change in monetary policy that matters but what is the end game? We are also of the view that, as with the US Fed's ill-timed Quantitative Tightening experiment in 2018, that the size of the US Fed's balance sheet will remain larger than what most market watchers will believe it should be, and that REAL interest rate (not the absolute level or the quantum of the increase) will be sustainably lower than the past. The implication and impact on markets over the longer-term will be very different from the short-term knee-jerk reaction.....something to think about.....

Malaysia

1. The KLCI closed at 1,523 @ 17.08.21, a decline of -1.2% M-o-M. Last week, Industrial & Metals (+2.1%) & Healthcare (+1.5%) were the best performing sectors. In contrast, Technology (-2.1%) and Construction (-1.6%) were the worst performing sectors. Year-to-date @ 13.8.2021, the KLCI has retreated by -7.7%.

2. The process has begun for Yang di-Pertuan Agung to appoint the country's 9th Prime Minister. This follows the resignation of Tan Sri Mahiaddin Yassin as Malaysia's Prime Minister on 16 August 2021. We expect the market to take the news in its stride. While <u>we continue to see downward pressure on the KLCI</u>, **we do not expect the market to correct sharply**. The reasons are as follows:

    - **Political uncertainty factored in**. When Tun Mahathir abruptly resigned as the 8th Prime Minister on 24 February 2020, the market was caught completely off-guard. The market had little warning it was coming. In the case of Tan Sri Mahiaddin, his tenuous grip on power was obvious from the onset as PM. When UMNO withdrew support for Tan Sri Mahiaddin on 8 July 2021, a leadership change looked imminent. The market had ample notice.

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- **Covid-19 pandemic sparked a sell-down last year**. A number of factors laid siege on the market last year. The leadership transition in 2020 occurred during the early stages of the Covid-19 pandemic. The market was gripped by fear and uncertainty due to the pandemic. This was compounded when the economy went into lockdown on 18 March 2020 (MCO 1.0). However, the current transition takes place at a time when vaccination rates have soared. Healthcare experts also are more knowledgeable about the virus. Inspite of the country recording circa 20,000 Covid-19 cases a day, it is reasonable to expect infections to plateau soon. The target of 80% vaccination rate (two doses) by end of Oct-21 appears achievable. Sentiment will improve when there are signs that Covid-19 is brought under control – allowing the economy to open again.

- **Earnings are recovering in 2021 & 2022**. In Q1 2020, the KLCI was staring at an abyss as far as corporate earnings were concerned. Analysts had just begun to ratchet down their earnings. In 2020, KLCI's net profit fell by an estimated 30%. However, net profit in 2021 is expected to rebound by 77% (with gloves)/54% (excluding gloves). In 2022, KLCI's net earnings are expected to grow by a further 5% (with gloves)/14% (excluding gloves) - see Exhibit 1.

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- **Foreign selling is dissipating**. Foreign shareholding on Bursa was around 22.7% in February last year vs 20.2% currently. This is an all time low. YTD foreign selling @ 13.8.2021 totalled RM6.0 bil vs RM 24.6 bil for the whole of 2020. Foreign outflows is gradually subsiding. We expect further selling to be well contained.

- **Valuation is a silver lining**. PE multiples rose sharply to 21x in 2020 (more than +2 standard deviation above mean) as earnings were slashed due to the Covid-19 pandemic. At KLCI's close of 1,503 on 16.8.2021, the KLCI is trading at 13.4x/13.8x in 2021/2022 respectively. This is -2 standard deviation below the mean of 16x (see Exhibit 2). Finally, Malaysia traded at between 10% to 40% premium to Asia ex-Japan until 1H 2020. Currently, the KLCI is at an 18% discount to Asia ex-Japan. This is one of the widest discounts seen in the last 5 years (see Exhibit 3).

- **Other indicators are supportive**. KLCI's prospective dividend yield of 4.5% (range 3.0% to 4.5% since 2011) and price to book of 1.53x (-1SD below mean of 1.74x) are also supportive of the market's fundamentals (see Exhibit 4).

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- **We see justification for the KLCI to be supported at around 1,680** based on our bottoms-up fair valuation which assumes a 15% decline in the glove companies (see Exhibit 1). This implies a 2022 PER of 15.4x which is still below the mean of 16x.

- On balance, we believe the **risk to reward ratio for the KLCI is reasonable**. The leadership transition offers the country an opportunity to reset. The market is in need of a catalyst to reverse its downward trajectory. Meaningful and enduring reforms hold the key to a potential market reversal. We have a healthy level of cash and look for opportunities to Buy. Our positive stance on technology since 2019 have played out well. We continue to be exposed to stocks which may benefit when the economy starts to reopen.

3. Greatech, a factory automation solution provider, announced revenue and profit growth of 142% YoY and 117% YoY respectively for 2QFY21 (vs 2QFY20). Its management was optimistic over their Solar and Electric Vehicle Battery segments. They expect demand to experience an upswing on the back of government policies which are gravitating towards innovation and adoption of sustainable technology.

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In the light of its aggressive capacity expansion 1mil sq ft of plant space (currently 140k sq ft) and good order visibility for FY2021 and FY2021, we expect to see Greatech gain a greater foothold and exposure in the global sustainable technology landscape.

4. World Semiconductor Trade Statistics (WSTS) announced June 2021 sales increased by 26.1% YoY (vs 25.9% YoY for May-21) and 6.7% MoM (vs 6.7% for May-21). Exhibit 5 shows that growth in global semiconductor sales are still trending upwards. We remain positive for the next few quarters. There has been 7 cycles since 1997. The average duration of an upcycle is 31 months. We are in the 16 month of the current upcycle. The monthly sale value has increased by 28% in the *current* cycle vs a historical average increase of 23% from start to peak (see Exhibit 5).

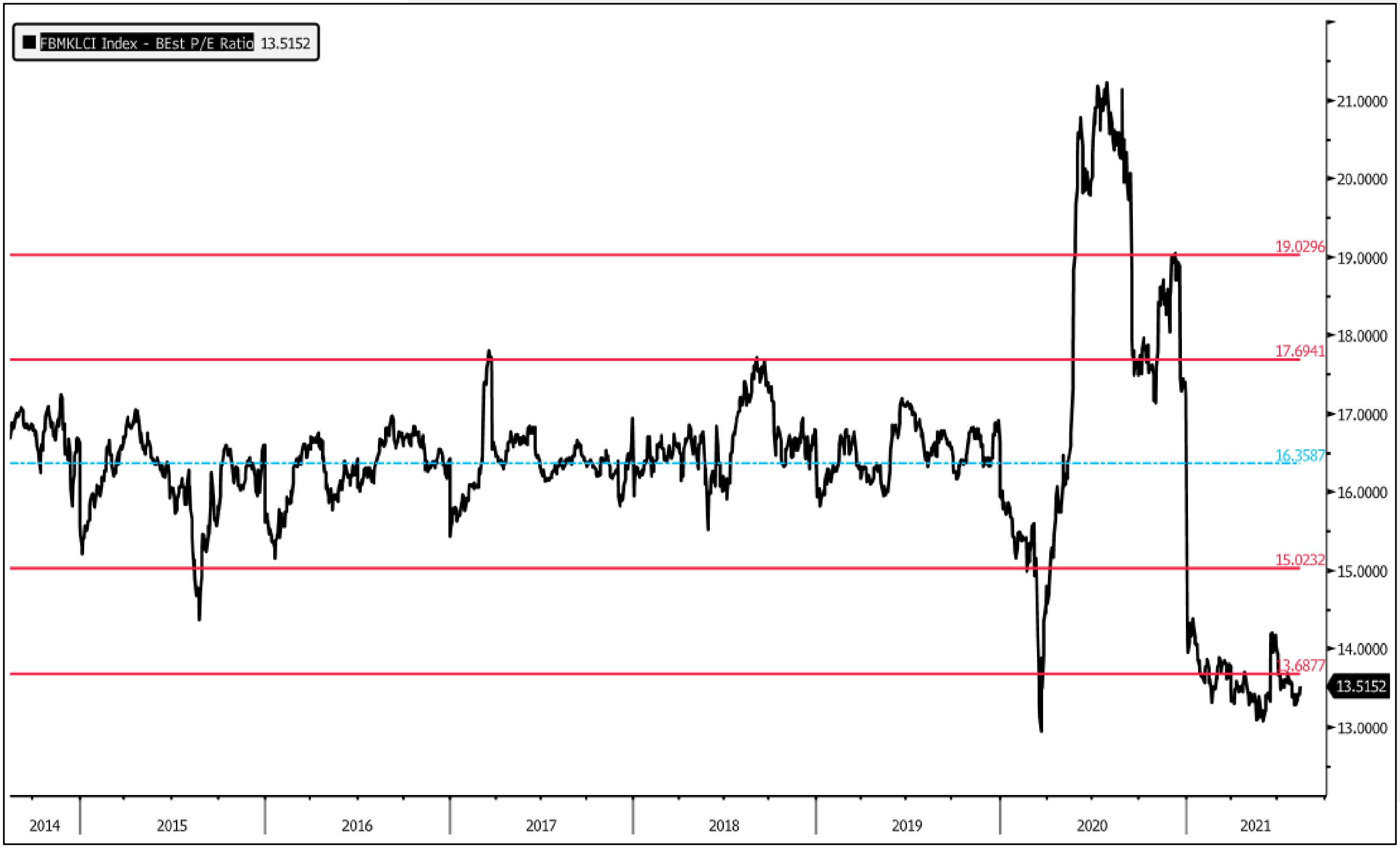
Exhibit 1 : KLCI's Fair Value

FAIR VALUE ANALYSIS		2019	2020	2021	2022
Total earnings (RM bil)		53.1	37.1	65.7	68.9
Gloves earnings (RM bil)		1.4	2.2	11.9	7.6
Total earnings ex gloves (RM bil)		51.8	34.9	53.8	61.3
Mkt PER		18.8	26.9	15.2	14.5
Gloves PER		40.3	24.6	4.6	7.1
Mkt PER ex Gloves		18.3	27.0	17.6	15.4
Net profit growth			-30%	77%	5%
Net profit growth - ex glove			-33%	54%	14%
2022 Earnings - ex gloves (RM bil)					61.3
Target 2022 PER ex gloaves					**17.5**
Market cap - ex gloves (RM bil)					1,073.4
Add : Market cap gloves (RM bil)	assume		15% decline		46.2
Total market cap (RM bil)					1,119.6
KLCI market cap - current					998.9
Upside					12.1%
KLCI current					1,500
Target - KLCI					1,681

Source : Bloomberg & AISB

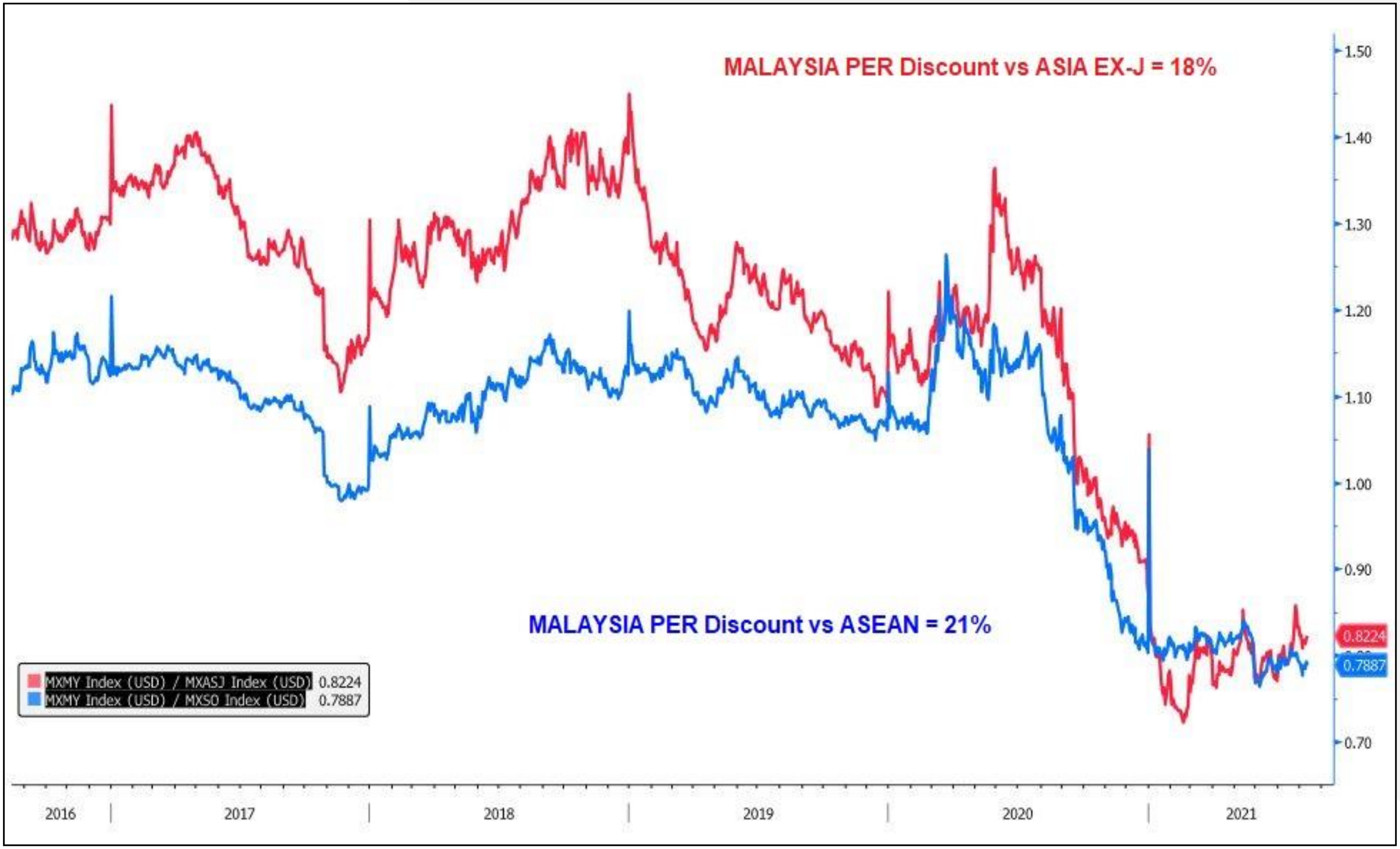
(Source: Bloomberg & AISB)

Exhibit 2 : 7 Year KLCI Per Chart



(Source: Bloomberg)

Exhibit 3 : Malaysia Discount vs Asia Ex Japan @ 13.08.21

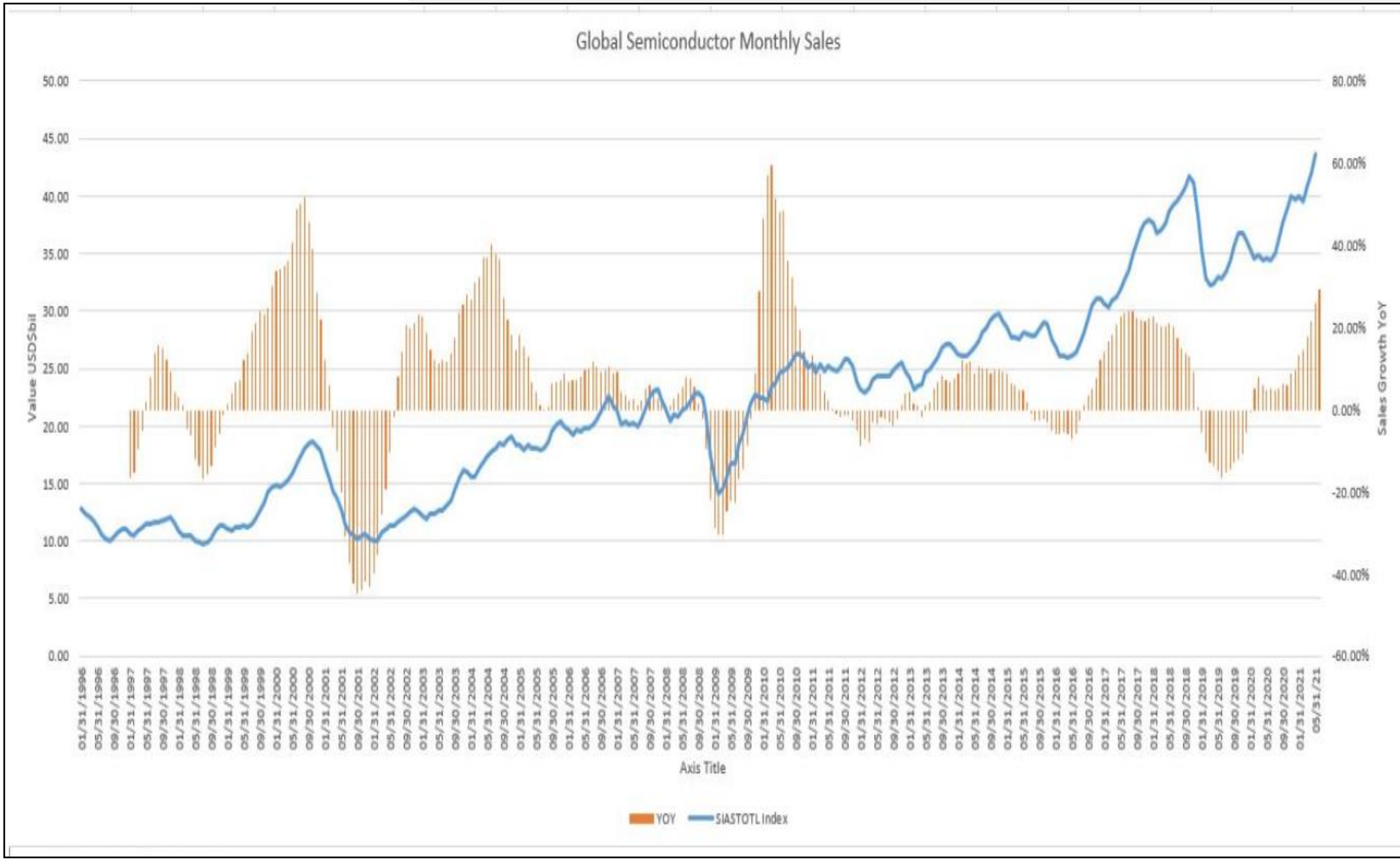


(Source: Bloomberg)

Exhibit 4 : 7 year KLCI PBR Chart

(Source: Bloomberg)

Exhibit 5 : Global Semiconductor Monthly Sales



(Source: Bloomberg & AISB)

Exhibit 6 : Semiconductor Sales Cycles

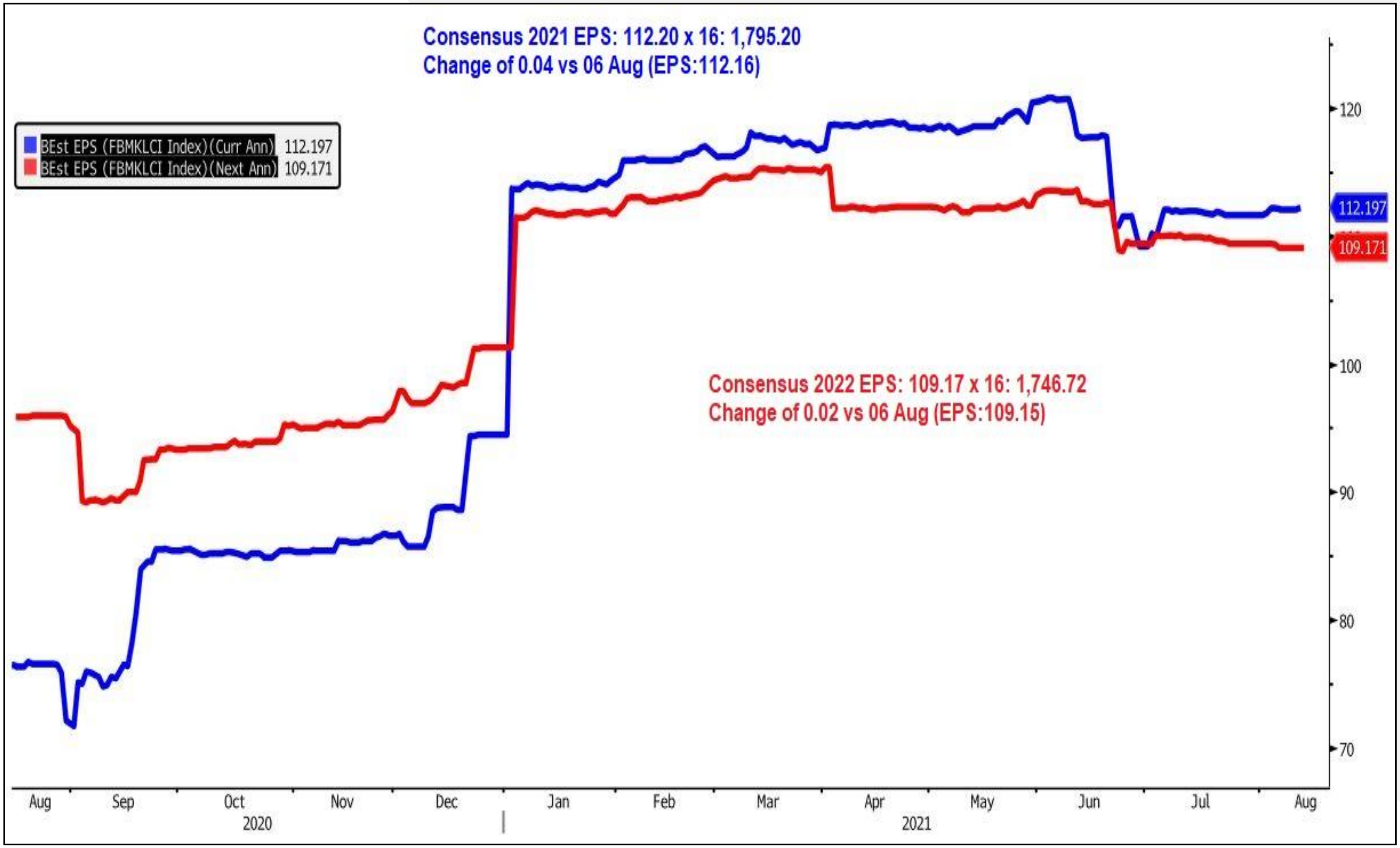
Semiconductor Sales Cycles

	Dates			Duration (Months)			Monthly Orders
	Start	Peak	End	Start to end	Start to peak		% Increase to Peak
1	06/30/1997	08/31/1997	02/28/1998	9	3		2%
2	02/28/1999	08/31/2000	02/28/2001	25	19		66%
3	08/31/2002	06/30/2004	09/30/2008	74	23		49%
4	12/31/2009	03/31/2010	06/30/2011	19	4		4%
5	12/31/2012	02/28/2014	06/30/2015	31	15		5%
6	09/30/2016	06/30/2017	12/31/2018	28	10		11%
7	*03/31/2020*	*01/31/2021*	*02/28/2021*	*16*	*16*	*	28%
	Average -excluding current cycle			31	12		23%

* *Current cycle*

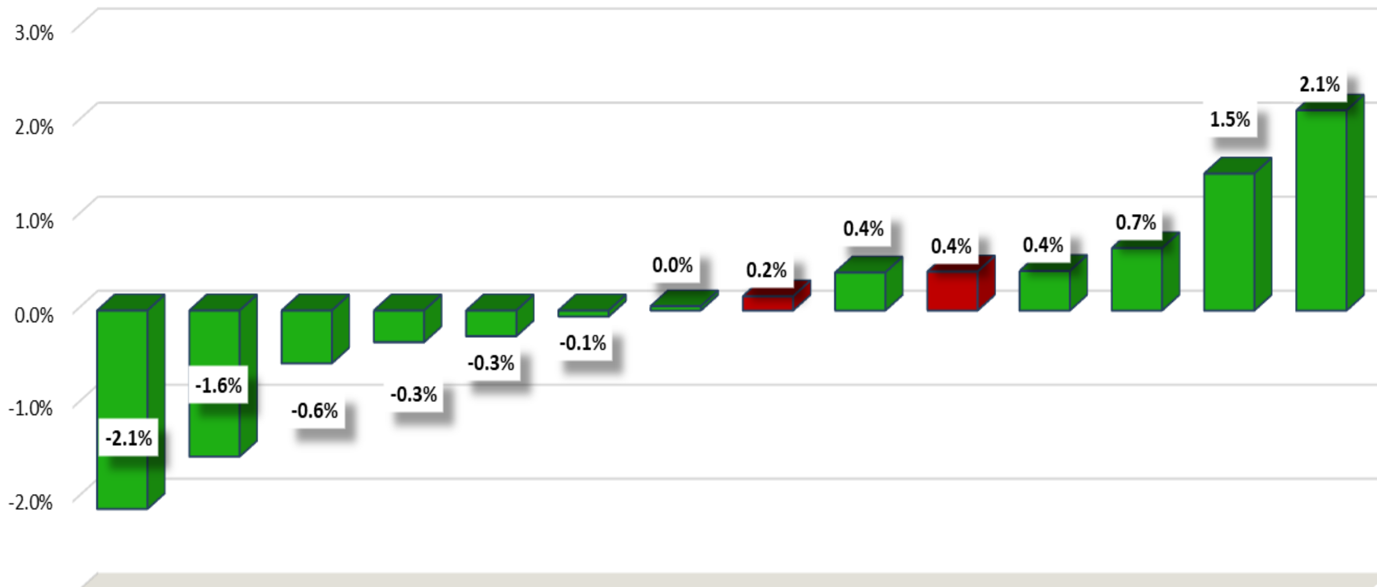
(Source: Bloomberg & AISB)

Exhibit 7 : FBMKLCI Consensus Earnings Per Share (EPS) @ 13.08.21



(Source: Bloomberg)

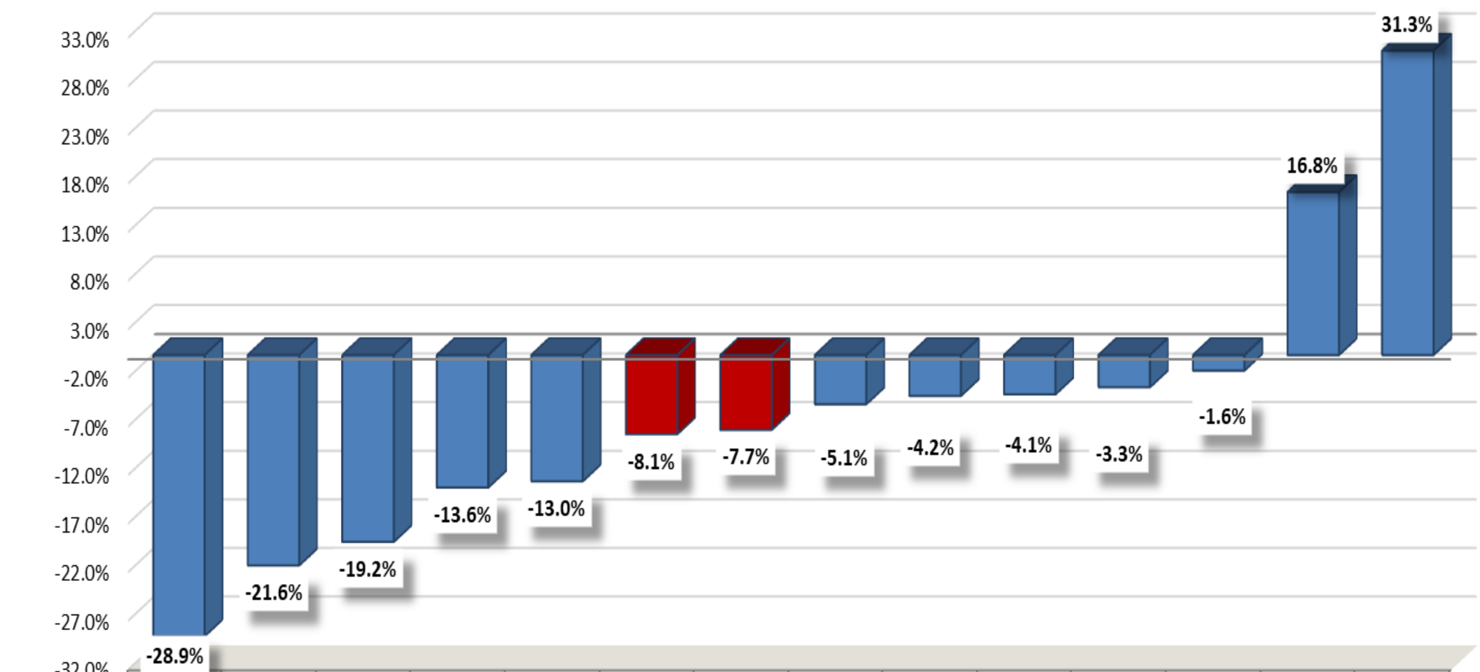
Exhibit 8 : Sector Performances (Week-on-Week) @ 13.08.21



	FTSE B/M EMAS Technology Index	FTSE B/M EMAS Construction & Materials Index	FTSE B/M EMAS Industrials Index	FTSE B/M EMAS Oil & Gas Index	FTSE B/M EMAS Utilities Index	FTSE Bursa Mal Small Cap Index	FTSE B/M EMAS Banks Index	FTSE MALAYSIA EMASSHARI	FTSE B/M EMAS Consumer Goods Index	FTSE Bursa Malaysia KLCI	FTSE B/M EMAS Food & Beverage Index	FTSE B/M EMAS Real Estate REITs Index	FTSE B/M EMAS HealthCare Index	FTSE B/M EMAS Industrial Metals & Mining Index
Change WoW	-2.1%	-1.6%	-0.6%	-0.3%	-0.3%	-0.1%	0.0%	0.2%	0.4%	0.4%	0.4%	0.7%	1.5%	2.1%

(Source: Bloomberg)

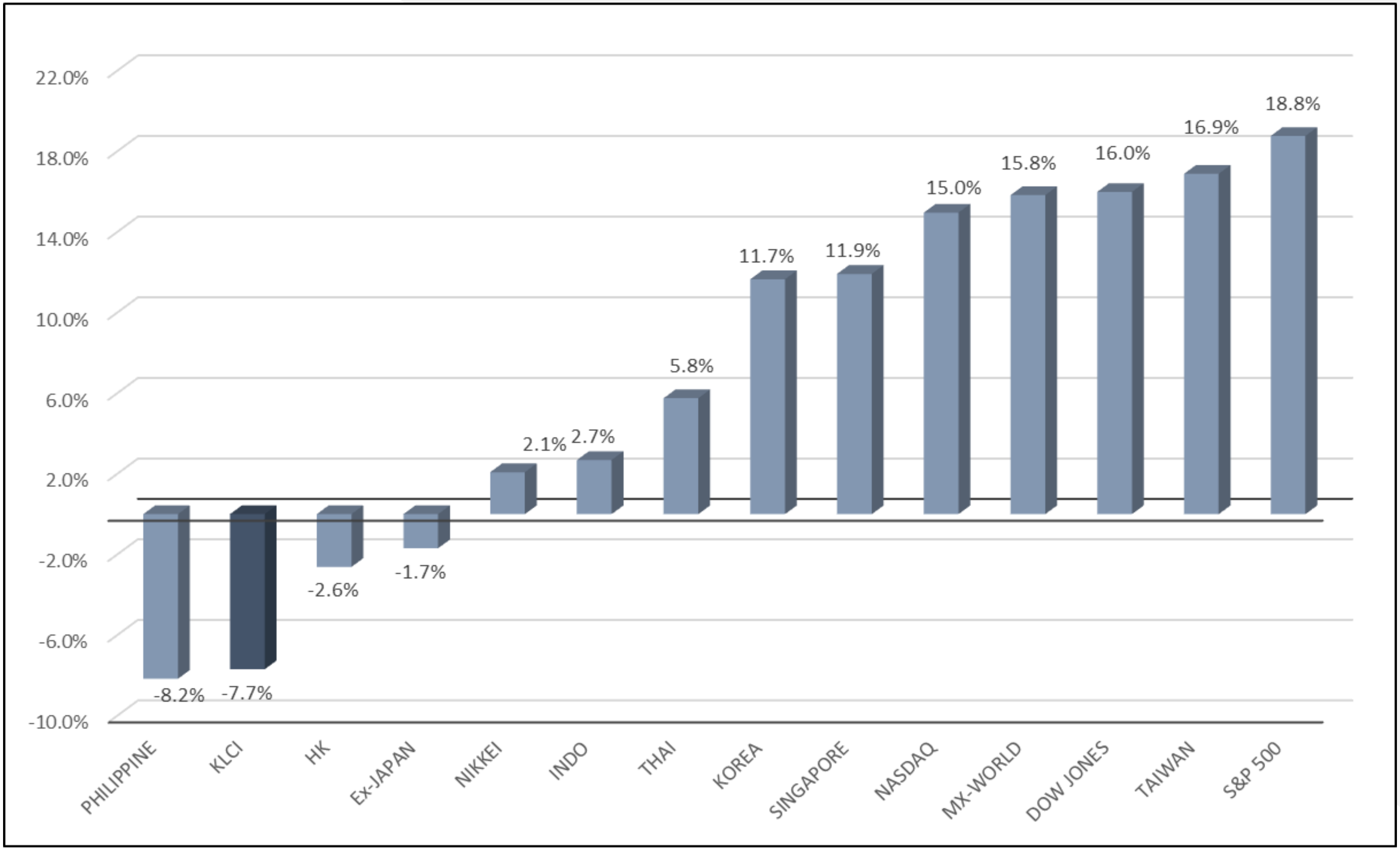
Exhibit 9 : Sector Performances (Year-to-Date) @ 13.08.21



	FTSE B/M EMAS HealthCare Index	FTSE B/M EMAS Oil & Gas Index	FTSE B/M EMAS Construction & Materials Index	FTSE B/M EMAS Food & Beverage Index	FTSE B/M EMAS Consumer Goods Index	FTSE MALAYSIA EMASSHARI	FTSE Bursa Malaysia KLCI	FTSE B/M EMAS Real Estate REITs Index	FTSE B/M EMAS Utilities Index	FTSE B/M EMAS Industrials Index	FTSE B/M EMAS Banks Index	FTSE Bursa Mal Small Cap Index	FTSE B/M EMAS Industrial Metals & Mining Index	FTSE B/M EMAS Technology Index
Change YTD	-28.9%	-21.6%	-19.2%	-13.6%	-13.0%	-8.1%	-7.7%	-5.1%	-4.2%	-4.1%	-3.3%	-1.6%	16.8%	31.3%

(Source: Bloomberg)

Exhibit 10 : Performance of Indices (Year-to-Date) @ 13.08.21



(Source: Bloomberg)

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