Capital Management Sdn Bhd
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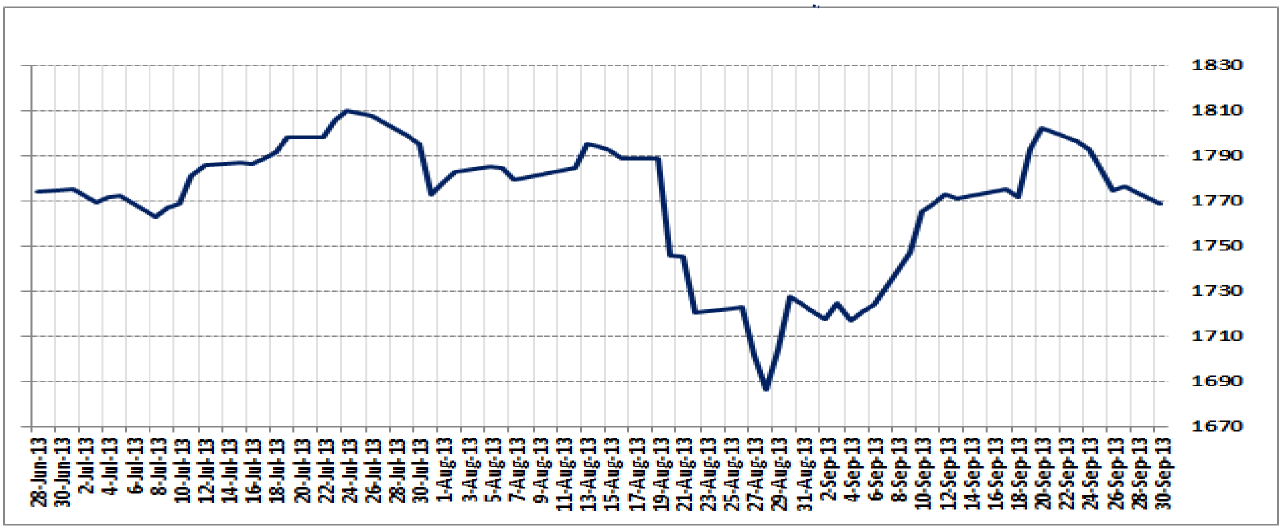
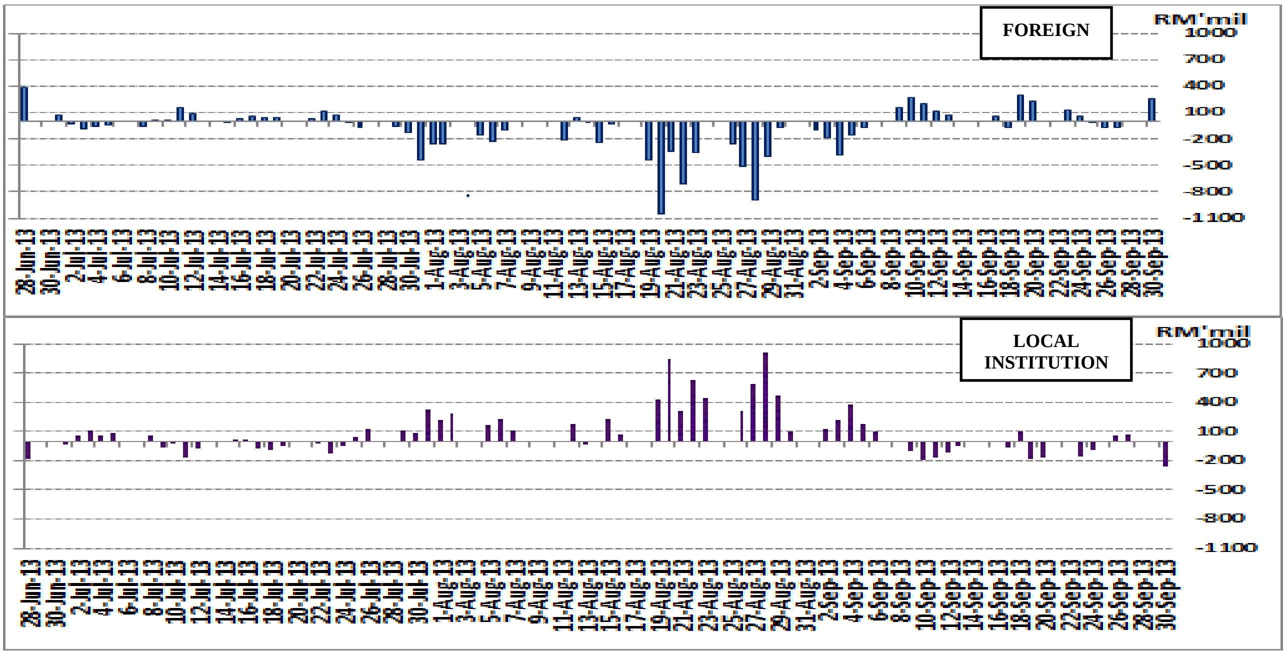
SEP 2013

# QUARTERLY REPORT

## FBM KLCI
## (Jul – Sep'13)




BURSA MALAYSIA: DAILY TRADING PARTICIPATION



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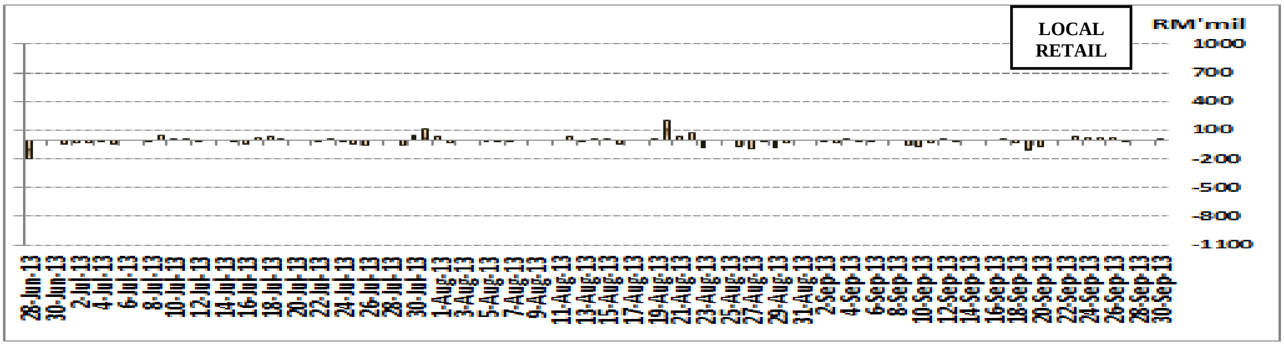


## OVERVIEW

Global markets plummeted after the Fed (Federal Reserve or Central Bank) declared its intention to taper the monthly US$85 bn bond purchases. Prices fell across all asset classes as there were reversal of money back to the US either due to repayment related to US$ carry trades or by long investors which saw the US$ rebounded.

Indonesia and India were the two biggest casualties as both equities and currencies plunged under heavy selling pressure. Other Asean markets also went down together albeit on smaller scale.

***INDEX PERFORMANCE***

| | 31-Dec-12 | 28-Jun-13 | 30-Sep-13 | 3Q13 | YTD |
|---|---|---|---|---|---|
| **Malaysia** | | | | | |
| KLCI | 1,688.95 | 1,773.54 | 1,768.62 | -0.3% | 4.7% |
| KL Construction | 236.20 | 278.35 | 279.89 | 0.6% | 18.5% |
| KL Finance | 15,357.24 | 16,884.92 | 16,426.13 | -2.7% | 7.0% |
| KL Plantation | 8,314.11 | 8,363.46 | 8,283.11 | -1.0% | -0.4% |
| KL Property | 1,053.71 | 1,374.54 | 1,331.97 | -3.1% | 26.4% |
| FBM Emas | 11,438.14 | 12,304.91 | 12,289.65 | -0.1% | 7.4% |
| FBM ACE | 4,214.15 | 4,684.50 | 5,537.17 | 18.2% | 31.4% |
| | | | | | |
| Malaysia (KLCI) | 1,688.95 | 1,773.54 | 1,768.62 | -0.3% | 4.7% |
| Singapore (ST Index) | 3,167.08 | 3,150.44 | 3,167.87 | 0.6% | 0.0% |
| Hong Kong (HS Index) | 22,656.92 | 20,803.29 | 22,859.86 | 9.9% | 0.9% |
| China (SSE) | 2,269.13 | 1,979.21 | 2,174.67 | 9.9% | -4.2% |
| S.Korea (SC) | 1,997.05 | 1,863.32 | 1,996.96 | 7.2% | 0.0% |
| Japan (Nikkei225) | 10,395.18 | 13,677.32 | 14,455.80 | 5.7% | 39.1% |
| US (DJIA) | 13,104.14 | 14,909.60 | 15,129.67 | 1.5% | 15.5% |

*Source: PCM*

Foreigners who have invested heavily in our bonds liquidated some positions that caused our ringgit to weaken and the currency declines spark the equity sell-off by foreign investors. Blue chip big-cap stocks led the fall and lower liners subsequently followed the decline. The support by local institutional investors helped our market to hold up relatively well.

The sudden change in the Fed decision to continue with its bond buying program after mid-September gave investors the relief to re-enter the market again. Equity, bond and currency markets rebounded sharply before selling pressure set in and pulled down the markets towards end of September.

## WHAT WE DID (applicable to a typical account)

We were nibbling in July and continued to accumulate more shares when market came down in August and started to trim on selected stocks when the market recovered in September.

We participated in two share private placements during the quarter. The first was in property-cum-developer Crest Builder and the second was in waste management company-turned-solar power producer **Cypark**. We took some profit on **Crest Builder** during the quarter. We also re-purchased **CIMB** at market bottom but completely sold off the stock upon market recovery. We further added some small quantity in oil & gas stocks **Daya Materials** and Dayang as well as telco service provider OCK. We also increased our holdings in **Axiata, AirAsia** and **CanOne**. We have also added a new stock during the quarter in **Supermax** which is the second largest rubber glove producer in Malaysia.

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During the quarter, we were allocated shares in **Sona** IPO which we have sold off with some profit immediately after its listing. Our investments in **MPHB** (subsequently changed name to Magnum) together with its spin-off company MPHB Capital were completely sold off after the capital repayment by MPHB. We took advantage of market recovery in September to reduce our investments in **Axiata** and **Genting** from 3% to 2%.

## HOW THE STOCKS PERFORMED (applicable to a typical account)

Our best performing stock during the quarter was **Datasonic** which surged by another 113% in price after its 1 : 2 bonus issue as well as on back of its strong earnings growth arising from the high acceptance of its better quality national identity cards. Among our oil & gas stocks, only **Daya Materials** surged by 33.5%. Other oil & gas stocks consolidated in 3Q2013 after their strong performance in the previous quarter. **OCK** which we bought since IPO also surged by 24.5%. The price of insurance stock**, Sykt Takaful** also surged to new high after its consolidation between May and July, gaining 23.6% in Q3 2013.

Several other stocks that gained more than 10% include food-based company **QL Resources** (+15.7%), new property developer **Matrix Concepts** (+14.2%) and travel insurer **TuneIns** (+10.3%).

**AirAsia** led the losers with 19.7% plunge in price as weaker ringgit will raise its fuel cost and increase its US$ debt burden. Our heavyweights did not do well in this quarter as **MBSB** fell 6.8% and Maybank was still 3% lower after adjusted for its dividend payment. A few stocks fell marginally such as Dayang (-3%), Telekom (-3%) and TRC (-5.0%).

As a whole, our fund performed better than FBM KLCI which slipped 0.3% during 3Q 2013 while the cumulative performance of our fund of about 23% this year is also way ahead of KLCI's 5% gain.

## GOING FORWARD

### The Bad News

Everyone treat US tapering of its bond purchases as bad news. Markets have been conditioned to the continuous flow of cheap money from US and have at the same time presumed such supply of money will continue forever. Whenever the reversal of a trend comes, the market will panic initially and may worsen subsequently when speculative hedge funds take advantage of the weak market sentiments to short sell both the equity market and currency. In the recent reversal of funds back to US, the "attacks" on Indonesia and India by speculative funds resemble the initial assault of Thailand back in 1997. Although fundamentals of Asian nations are now much better, Indonesia and India which both have certain forms of twin deficits - current account deficit and budget deficit gave speculators the excuse to sell their currencies and stock markets. Indonesian governments were forced to raise its reference interest rate by 1.25% to 7.25% during the quarter under review to defence its currency.

**Asian Financial Crisis Comparison**

**Asian economies are much stronger now to withstand the "attack"**

| | Asian Financial Crisis | Current Reversal of Foreign Funds |
|---|---|---|
| Hot Money | Overheated economy attracted much foreign funds | Low interest rates attracted hot money |
| US$ Peg | Currency pegged to US$ | Managed float |
| US$ Loan | Corporates borrowed in US$ | More domestic borrowing & bonds |
| The Trigger | Sold down on Thai baht | Sold Indonesian rupiah and Indian rupee (twin deficit) |
| Forex Reserve | Low foreign exchange reserve | High foreign exchange reserve |
| Current A/c | Current account deficit (high import) | Only Indonesia, India & Vietnam having current account deficits (lower export) |

*Source: PCM*

**The Good News**

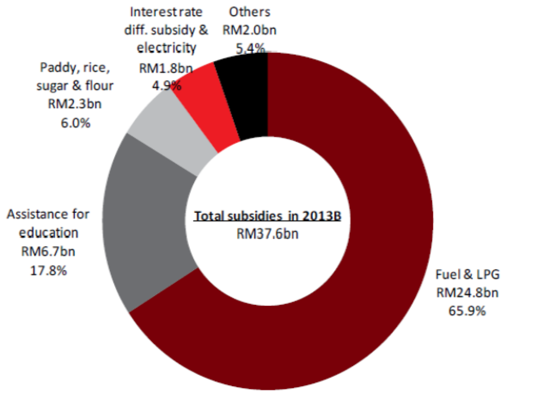
The sudden decision by the Fed (US Federal Reserve) to continue with its bond purchases in September was seen as a relief by the market. We, on the other hand, view it as a deferment as eventually the Fed will still need to stop its money printing program. Although the Fed is unlikely to change its view in the next October meeting, its December meeting is crucial as it is the last meeting for the Fed's Chairman, Ben Bernanke before his departure. Bernanke may want to do something on the quantitative easing (QE) which he initiated during his tenure as chairman of the Fed. Bernanke once said that he will drop money from the helicopter and flood the market with cheap money in order to save the US economy during the infamous Lehman Brothers Crisis.

The Fed is waiting for confirmation of US economic data before commencing its tightening program. During its September meeting, the Fed also lowered its estimates of US economy this year from 2.3-2.6% to 2.0-2.3% even though US unemployment rate has fallen to 7.3% in August 2013. So, when US economy improves further in the coming few months, the fear of bond purchase tapering will re-surface.

**Negative Outlook by Fitch**

On the local front, Fitch Rating's revision of Malaysia rating outlook from "stable" to "negative" could be viewed as a wake-up call for Malaysian government to rectify some of the country's economic weaknesses. Fitch was obviously dissatisfied with the inaction of Najib administration in tackling the escalating government debts (near the self-imposed 55% of GDP and more than 70% if all the government guarantees are included), the high household debts/GDP ratio and its failure to cut subsidies and raise revenue through GST (goods and service tax) in order to reduce the budget deficits.

**Malaysian Federal Government Subsidy Breakdown**



SOURCES: MOF, CIMB RESEARCH

The first response by the government came in early September when petrol RON95 and diesel prices were raised by RM0.20 each. The subsidy cut will save the government RM3.3 billion a year. Although this is a good start, the amount is small compared with the total subsidy of RM37 bn a year.

**More Tightening in Budget**

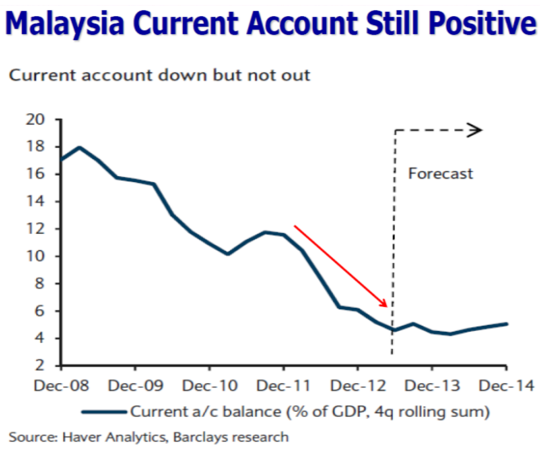
We believe more measures will be disclosed in the coming budget on 25 October 2013. Some of the possible measures to address the pertinent issues include the timeline to roll out GST, fuel cost-pass-through to reduce electricity subsidy, higher sin taxes (on liquor, tobacco and perhaps gaming) and deferment of some less crucial mega projects especially those with high import contents such as high speed rail to Singapore.

The government is still adamant to be able to keep the budget deficit on tract, i.e. 4.0% this year, 3.5% next year and 3.0% by 2015. With the promise of more handouts during the last general election, it is yet to be seen how the government can achieve this without more tax revenues.

**Stable Economy**

Despite the weaker external demand, Malaysian 2nd quarter GDP growth improved slightly to 4.3% from 1Q's 4.1%. The fairly stable economic growth again confirmed that the diversified Malaysian economic structure can withstand the global volatility much better than our neighbouring countries where recent weaker demand from China has affected the exports of this region. The fall in exports is also reflected in the sharp fall in Malaysian current account surplus.

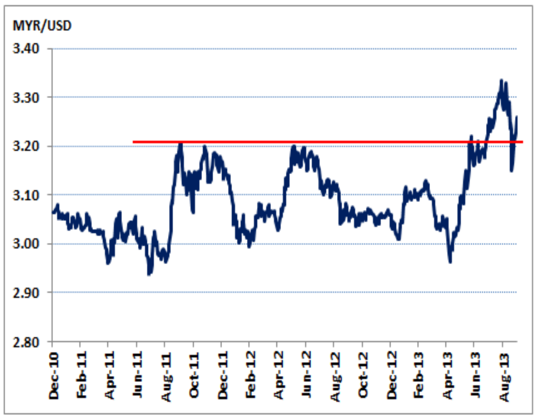
Going forward, Malaysian economy will continue its mild growth. Dr Marc Faber, the renowned contrarian investor, described our economy as one which is stable but not exciting.




**Immediate Outlook & Strategies**

With the ringgit back to its resistance of 3.2 per US$, the worse is over, at least for the time being. The normally weak Aug-Oct period may or may not recur this year after the Fed threw in the lifeline to defer the tapering of its QE program. However, US cannot continue with its QE program forever and it will have to unwind this monetary policy at some point in time. The tapering of bond purchase is just the beginning of tightening and the raising of US benchmark interest rate will eventually happen (most expect this to occur in 2015, depending on the speed of US economic recovery). We believe when the actual bond purchase tapering materialises, the impact on the market will be much milder as investors would have expected it and become immune to the taper-talk by then.

**Ringgit Back to RM3.2/USD Support**



Source: Bloomberg

In the mean time, we will continue with our strategy of investing in strong fundamental stocks with reasonable valuation which is normally found among the mid-cap stocks. Following the call by our Prime Minister for government linked investment institutions to invest more in mid-cap stocks, these stocks have performed well. As our fund typically has about 2/3 in mid-cap stocks, we will continue to benefit from this new trend.

**Ang Kok Heng**
**Chief Investment Officer**
**Phillip Capital Management Sdn. Bhd.**