



Party Over But The Hangover Could Last Through 1H2012

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Remain Defensive and Wait to Bottom Fish around 1,100 Levels or Lower

- The fourth quarter is around the corner, rekindling the usual anticipation of a year-end rally after a dreadful August and September that practically drove world stock markets back into a bear territory hardly seen in three years. While the Budget 2012 scheduled for October 7th may ignite interest in selected domestic growth driven cyclical plays, any technical rebound in the FBM KLCI and its component stocks would be short lived in view of the uncertain external climate. Nonetheless, buying interest could resume as we move closer to year-end for window dressing.
- We cut slightly our end-2011 FBM KLCI target to 1,370 from 1,490 after lowering our mid-cycle PER to 13.5x from of 14.5x. Our end-2012 target is also lowered to 1,425 based on a mid-cycle PER of 12.5x from 13.5x previously. We do not discount the possibility of the benchmark index diving to a low of 1,140 by 1H12 based on a minus two standard deviation from its last decade's historical mean of 16.6x, but expect a swift rebound in 2H12 as more concerted efforts are directed towards solving the European debt crisis. As a comparison, if we attach the low PER of 9x during the 2008 down cycle, the floor level in 1H12 could be around 1,025 points.
- To refresh, we have indicated in our Malaysia Strategy Note in August that market volatility will persist and the downside could be capped at 1,340 if conditions in Eurozone do not worsen and pending no double dip in the US and Eurozone economies. We did highlight in the same report that it has the potential to drop below 1,000 points based on historical trends if worries about the US and Europe do materialize. The benchmark index hit a low of 1,310 on September 26th and rebounded sharply to close at 1,387 on 30th September. We anticipate more pullbacks in October to around 1,295 levels before the index rebounds to close the year higher.
- October could provide a good trading opportunity to buy stocks for a short-technical rally and exit by end-January 2012, before the emergence of more negative external data and corporate earnings downgrades. However, to caution, any surprise announcement of a general election in the 4Q11, probably in November, is seen as a bane for the market in current conditions as it would add to the uncertainty. This could shoo away investors to the sideline pending the outcome of the 13th general election. We strongly believe a general election in this current uncertain time is not in the best interest of the nation and should be delayed until 2013. Nonetheless, we believe it could materialize next year before the parliament convenes in March. The fear factor could induce further downside for the index in the 1H12.
- The key highlights in 4Q11 would be Budget 2012, possible award of big ticket items earmarked in the last budget, including the Klang Valley MRT and Expressway projects, award of marginal oil field contracts and the listing of Gas Malaysia Berhad.

- Maintain a Take Profit stance as we view that the FBM KLCI has just entered a major corrective wave that could last through mid-2012 based on historical cycles, but expect a volatile market that would provide pockets of trading opportunities. Traders can take short-term positions in October and exit before next February as we still anticipate year-end and New Year rallies during this period but expect higher downside risks in the 1H12 as the flow of negative economic data and earnings downgrades downplay investor sentiment.
- We still propagate reduced exposure to heavyweight cyclical sectors like **Banks** and **Plantation** that will see further erosion in prices as foreign investors continue to pull the plugs. Although in the same category, selective stocks in the **Construction** and **Oil and Gas** sectors may continue to benefit from domestic pump-priming activities driven by the public and private sectors. Besides that we reiterate that investors should remain defensive and seek exposure in defensive sectors like **Consumer, Gaming, Power, Telco, Healthcare** and **Education**, and selective cyclical plays listed in the following table.

Company	Share Price (RM)	EPS (sen)		PER (x)		GDPS (sen)		Dividend Yield		Target Price (RM)	Capital Gain (%)	Total Gain (%)
		FY11	FY12	FY11	FY12	FY11	FY12	FY11	FY12			
KIANJOO	1.80	26.3	32.2	6.8	5.6	11.0	14.0	6.1%	7.8%	3.22	78.9%	86.7%
SEG	1.70	14.2	21.8	12.0	7.8	8.0	14.5	4.7%	8.5%	2.51	47.6%	56.2%
STAR	3.15	26.0	31.2	12.1	10.1	20.0	20.0	6.3%	6.3%	4.37	38.7%	45.1%
QL	2.64	14.3	19.6	18.5	13.5	9.0	9.0	3.4%	3.4%	3.70	40.2%	43.6%
SAPCRES	3.68	18.1	22.9	20.3	16.1	8.5	10.5	2.3%	2.9%	5.13	39.4%	42.3%
BSTEAD	5.04	49.5	62.7	10.2	8.0	33.0	37.0	6.5%	7.3%	6.56	30.2%	37.5%
CARLSBG	6.45	53.9	57.6	12.0	11.2	37.0	40.0	5.7%	6.2%	8.00	24.0%	30.2%
LITRAK	3.60	19.5	28.9	18.5	12.5	17.0	20.0	4.7%	5.6%	4.40	22.2%	27.8%
BJTOTO	4.25	25.8	29.5	16.5	14.4	21.0	35.0	4.9%	8.2%	4.92	15.8%	24.0%
IJM	5.00	23.4	37.8	21.4	13.2	11.0	11.0	2.2%	2.2%	6.01	20.2%	22.4%

Will Budget 2012 Temporarily Halt the Vicious Down Cycle?

Anticipation of a general election in November this year or by March 2012 is fuelling speculation that Budget 2012 will be business and consumer friendly to firm up the ruling coalition's grip on domestic politics. Nonetheless, the government is not expected to short change its fiscal prudence for popularity to achieve a lower budget deficit of 4.9% in 2012 vs. 5.3% in 2011 but it has the freedom to play around with the allocation for operating and development expenditures.

When the government announced Budget 2011 last year, its commitment went up by 2.8% to RM212bn with 76.8% or RM162.8bn of it going for operational expenditure and the balance 23.3% or RM49.2bn channelled towards development expenditure. With ongoing liberalisation measures and greater private sector participation through measures outlined under the Economic Transformation Programme, expect total allocation for Budget 2012 to be flat at RM211.8bn. Of this, RM170bn (or 80.3% of total allocation) will be channelled towards operational expenditure; while the remaining RM41.8bn (or 19.7%) is allocated for development spending, based on last year's indication of RM90bn development allocation for 2011 and 2012. Considering that as much as RM4bn to RM5bn from 2011 allocation will flow over into 2012 due to the delay in launching LRT and MRT projects, the actual allocation for both years could vary.

The current weak and uncertain external climate but coupled with still high inflationary pressure would induce the Malaysian government to emphasise on three important factors in the upcoming budget. Firstly, it would expedite projects highlighted under the Economic Transformation Programme to buffer downside from slowing external demand. Secondly, it would introduce further liberalisation and incentives to make businesses more competitive as our neighbours like Indonesia emerge as more conducive investment destinations. Finally, it is expected to introduce more structured benefits/subsidies for the hard core poor to compensate for the rising income gap and loss in disposable income caused by inflationary pressures.

Market Strategy

As we believe it is still too early to bottom fish, we continue to advocate investors to **Sell** on any rally and remain defensive. For long-term investors, they can nibble on weakness undervalued stocks with domestic flavour and low foreign shareholdings (see our last August strategy report for stocks with high and low foreign shareholdings). Traders should find ample opportunities to trade as market is expected to remain volatile.

As we anticipate more pullbacks, investors should Sell-on-Strength overvalued high beta plays like Unisem, Media Prima, Hong Leong bank and Top Glove while waiting to accumulate undervalued defensive plays like **QL Resources (TP: RM3.70)**, **Star (TP: RM4.37)**, **BJ Toto (TP: RM4.92)**, **Carlsberg (TP: RM8.00)**, **Kianjoo (TP: RM3.22)** and **Litrak (TP: RM4.40)** to take advantage of their resilient business and ability to sustain acceptable dividend pay outs. We also like selective cyclical plays in the Oil & Gas, Construction and Plantation sectors like **Sapura Crest (TP: RM5.13)**, **IJM Corporation (TP: RM6.01)** and **Boustead Holdings (TP: RM6.56)** respectively due to their niche in the area of business and ability to seize on domestic pump priming measures. We add **SEGI (TP : RM2.51)** to our top ten picks despite its high beta, due to its exposure in the defensive education sector.

Our preference for the top ten picks is premised on the following facts,

- **Kianjoo** - We are positive on Kian Joo as the company has regained pricing power thanks to improved regional economic conditions. Thus, we expect margin to recover substantially going forward. Note that Kian Joo will be expanding its capacity by the year end. Kian Joo plans on adding a 2-piece line by year end and will boost capacity by 50% to 1.4-1.5bn cans. Vietnamese operations are also growing but we believe impact will only be seen in 1-2 years time. Kian Joo also has Indonesia in its pipeline and we are positive on the growth prospect. Maintain Buy at RM3.22 based on FY12 PER of 10x.
- **SEGi** - We expect SEGi to register a strong earnings growth of 54% for FY12 due to higher number of student inflow. With its key role in the ETP, we believe the foreign student flow would play a greater contribution to the group's earnings. On the local front, we believe SEGi would benefit from the population switch moving from public institutions to private institutions due to limited seats in the former. Enrollments in private institutions have outpaced that of public institutions. It also has decent track record of dividend payment. For FY11, the group has declared a special dividend of 14 sen/share. During the recent economic turmoil, its share price has corrected by 18% from its peak of RM2.08 in July 2011 - a good opportunity to accumulate. We value the stock at RM2.51 based on 13x FY12 EPS of 19.3sen.
- **Star** - Although visibility remains uncertain, we like Star as a dividend play stock. With an estimated dividend yield of 5.2%, Star provides good recurring income for shareholders. In addition to that, the impending GE13 would provide an adex booster for Star as political promotional activities is expected to be phenomenal with the expected intense fight between the political parties. We value Star at RM4.37/share using a print segment PER of 14x. Maintain Buy.
- **QL Resources** - We remain positive on QL thanks to its operations in the food-related industry. Growth drivers going forward include, i) fishery plant in Surabaya to be up and running by FY12 which will expand capacity by 20%, ii) Palm biomass pelletizing system to start contributing to topline by FY12. There are huge demands from Europe, China, Korea and Japan, and iii) We expect plantation contribution to quadruple in FY13 coupled with double-egg contribution from Vietnam and Indonesia. Both farms have the capacity to produce 0.5mn eggs per day. Maintain Buy with a target price of RM3.70 based on Sum-of-Parts.

- **SapuraCrest** - With its strong asset base and synergistic acquisitions, SapuraCrest will emerge as a strong contender for lucrative oil and gas contracts in Malaysia and this region. The arrival of two pipe lay vessels in late 2013 will place it in a strong footing to bid for the renewal of Pan Malaysia Integrated T&I Contract that will expire in 2014 under a "3+1+1-years" term. With its 70% market share in the local installation of pipeline and facilities segment and strong orderbook of RM10bn earnings visibility is intact for the next two years. Acquisition of Clough will not only enhance its regional presence but also contribute to stronger exposure in Australia with the start of construction work for the Montana Development Project worth RM482mn. Official announcement on the award for Gorgon natural gas project that could be worth around US\$250mn would be additional booster for the company when it starts in 2013 apart from positive news flows for its bids in Brazil.

Merger with Kencana Petroleum will enhance its competitive landscape as it will be able to provide a complete suite of products and services right from fabrication, installation to inspection, repair and maintenance jobs in the upstream business. This merger allows the group to secure more marginal contracts domestically and larger EPC contracts on a global scale. We value the stock at RM5.13 based on a CY12 target PER of 16x.

- **Boustead Holdings** - It has a CY10/13 earnings CAGR of 14.2% driven by strong order book replenishment, especially in the heavy industry segment. Property could further boost earnings growth as the group is expected to conclude the land swap in Jalan Cochrane and Jalan Ipoh in Kuala Lumpur by end of this year and next year respectively. Its strong plantation assets, prime land banks, earnings quality and near monopoly in navy contracts and government hospitals concession are distinct advantage in current uncertain times. Besides, it is an attractive dividend play with FY12 dividend yield of 7.4% as it has a clear dividend policy that promises a payout ratio of 50%. Quarterly payout is an added attraction. It is also one of the strongest earnings yielding stock from a conglomerate perspective. We value the stock at RM6.56 based on Sum-of-Parts valuation methodology.
- **Carlsberg** - The company is expected to gain from its Singaporean operations. Recall, during the purchase period, there was a profit guarantee of RM44-46mn from Singapore alone. Based on current trends, we believe Singapore operations could easily beat the RM50mn mark. To add, the brewers have enjoyed two rounds of price increase to cushion escalating raw material prices. However, risk for the sector would be an increase in excise duty during the National Budget announcement this week. Maintain Buy with a target price of RM7.90 based on DDM, with a rate of return on 7%.
- **Litrak** - the company is expected to register a strong 48% earnings growth in FY12 due to higher compensation for toll freeze as LDP is scheduled to raise toll rate to RM2.10 from RM1.60. Next hike of RM1 to RM3.10 will be in 2016. Besides that the completion of RM133mn upgrading works at TTDI interchange are expected to be completed by 2012 and will improve traffic flow. The growing population in Puchong (Puchong Intan & Puchong Perdana) and Sri Damansara is expected to boost traffic volume higher as well. It has RM369mn cash and no significant principal repayment until 2021, Thus, being involved a cash business with minimal concerns about revenue collection issues, it has the ability to pay all free cash flows as dividends. We also believe the eventual delisting of PLUS will benefit Litrak as funds switch their holdings. We value the stock at RM4.40 based on DCF model (required rate of return = 9.2%).

- **BJ Toto** - A must have defensive stock amidst uncertain market outlook. Consistent cash flow from strong dominance in the domestic NFO market. Free cash flow amounts to approximately 30 sen - 40 sen/share annually, bulk of which the company typically returns to shareholders as dividends. Previous concerns of declining market share have also diminished as BJToto managed to secure license to operate 4D Jackpot Game in June, 2011. We expect this new game to arrest the shift of market share to Magnum. On a base case scenario, we estimate EPS could grow by 3% - 5% annually. However, if management could deliver on the 4D Jackpot Game, FY12 earnings forecast could easily surpass our expectations, in our view. Maintain Buy with a target price of RM4.92, derived based on DDM model (rate of return = 7.7, long term growth rate = 3.5%).
- **IJM Corporation** - At this juncture, we believe that IJM Corp's share price will be fundamentally supported by its orderbook of over RM3bn. The business is also insulated from global shocks arising from the US and Europe due to the nature of its current jobs (mostly local). The group has hinted that the concession agreement on the West Coast Expressway will be signed by the end of this month. In addition, the original alignment of 286km will be increased to over 300km due to some realignment on Perak's side. We expect the cost to increase close to RM5bn from the initially guided RM4bn. The group is also in the running for one of the MRT lines from Taman Bukit Ria to Plaza Phoenix - tender has been called for. We derive a target price of RM6.01/share on IJM Corp using a construction segment PER of 16x and property segment PER of 10x. Maintain Buy on the stock riding on newsflow and actual award of contracts.

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