AHAM CAPITAL ASSET MANAGEMENT

30 November 2022

FUNDAMENTAL FLASH

Clarity Emerging For Malaysia

Prepared by AHAM Asset Management

Resolution as Impasse Ends

Datuk Seri Anwar Ibrahim was sworn in as Malaysia's 10th Prime Minister (PM) last week ending a nail-biting political impasse after the 15th General Election (GE15) which resulted in a hung Parliament as no coalition was able to attain a simple majority.

Anwar will now lead a unity government comprising the main coalitions of Pakatan Harapan (PH), Barisan Nasional (BN), Gabungan Parti Sarawak (GPS), Gabungan Rakyat Sabah (GRS) as well as support of member of parliaments from Muda, Warisan and other independents.

After years of political instability, will the promise of Malaysia Baru now have its day? In our latest Fundamental Flash, we unpack what lies ahead for Malaysia with greater clarity emerging on the political-front and investment opportunities.

Once Bitten, Twice Shy

When Pakatan Harapan came into power in 2018 under the 7th Prime Minister Tun Dr. Mahathir, markets drifted lower as the government then embarked on a swathe of policy reforms that also grounded the wheels of commerce and eroded market confidence.

Backward-looking policy including cancellation of infrastructure projects like MRT3 as well as wholesale changes of CEOs heading corporates or government-linked companies (GLC) impeded decision-making and stalled growth.

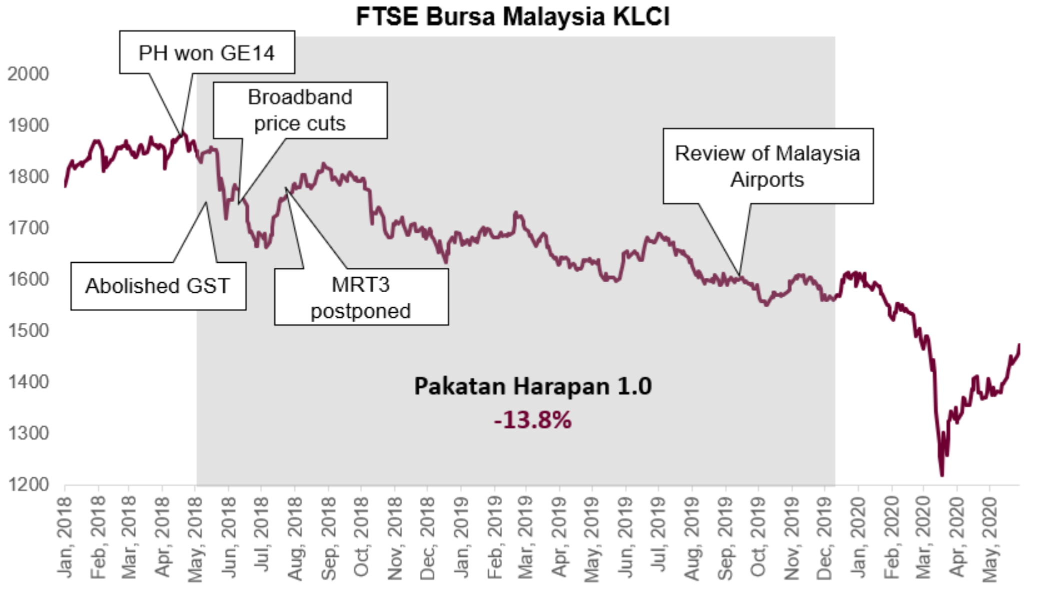
Flashpoints

- The political impasse ended last week as Datuk Seri Anwar Ibrahim was sworn in as the 10th Prime Minister of Malaysia.
- He leads a unity government comprising the main coalitions of PH, BN and the Borneo bloc.
- With a second shot at power, PH is unlikely to repeat the same mistakes and policy flip-flops that plagued its first tenure. Channel checks reveal an acknowledgement of the need to be more practical in setting policy direction.
- All eyes will be on the line-up of the Cabinet which is expected to be leaner and comprise a mix of technocrats and politicians to drive economic policies.
- With low foreign positioning and domestic funds highly cashed-up, any incremental positives will drive market performance as more clarity emerges.

Other populist moves to abolish the goods and services tax (GST) which resulted in a RM40 billion revenue shortfall as well as broadband price cuts also decimated markets as investors grew concerned of other socialist policies.

With a second shot at power, PH is unlikely to repeat the same mistakes and policy flip-flops that plagued its first tenure especially with Anwar now firmly holding the reins. Channel checks with party officials also reveal an acknowledgement of the need to be more practical and nuanced in setting policy direction as well as communicating them.

Graph 1: Market Performance under Pakatan Harapan Government



Source: Bloomberg, as at May 2020

All Eyes on Cabinet

Strange bedfellows currently make up the unity government with BN and PH component parties which were once at odds with each other now finding themselves seating on the same side of Dewan Rakyat.

It is hoped that the new unity government which effectively commands a two-third majority in Parliament would be able to close ranks and restore political stability in order to carry out much needed fiscal and institutional reforms to attract foreign interest and invigorate the economy.

These include broadening the country's revenue tax base and rationalising a ballooning subsidy bill that is projected to hit RM80 billion this year. If these reforms can be effectively carried out, we could see a reversal of foreign fund flows and help revitalise the local equity market.

At the time of writing, the unity government has yet to be unveiled. Though, expectations are that we would see a much a leaner Cabinet comprising a mix of technocrats and politicians that would help drive economic policies. It will be important to monitor key Cabinet roles such as Finance which could set the policy tone for other ministries.

Technicals are Favourable

Mired by political instability, the local market has been stuck in the doldrums for the past few years. Since 2014 to date, when 1MDB issues started hitting the market, the local equity market fell by over 18% in Ringgit terms or 40% in USD terms, as USD$15.9 billion worth of portfolio monies flowed out.

Foreign shareholding reached a 10-year low as political uncertainty dissuaded foreign investors from ploughing money. Domestic institutional funds have been also highly cashed-up as they sit on the side-lines.

Crucially, if there is a return of political stability and a growth story, foreign inflow could drive our markets higher. In every year between 2010 to 2021, whenever there is net foreign buying, our market has been driven positively higher.

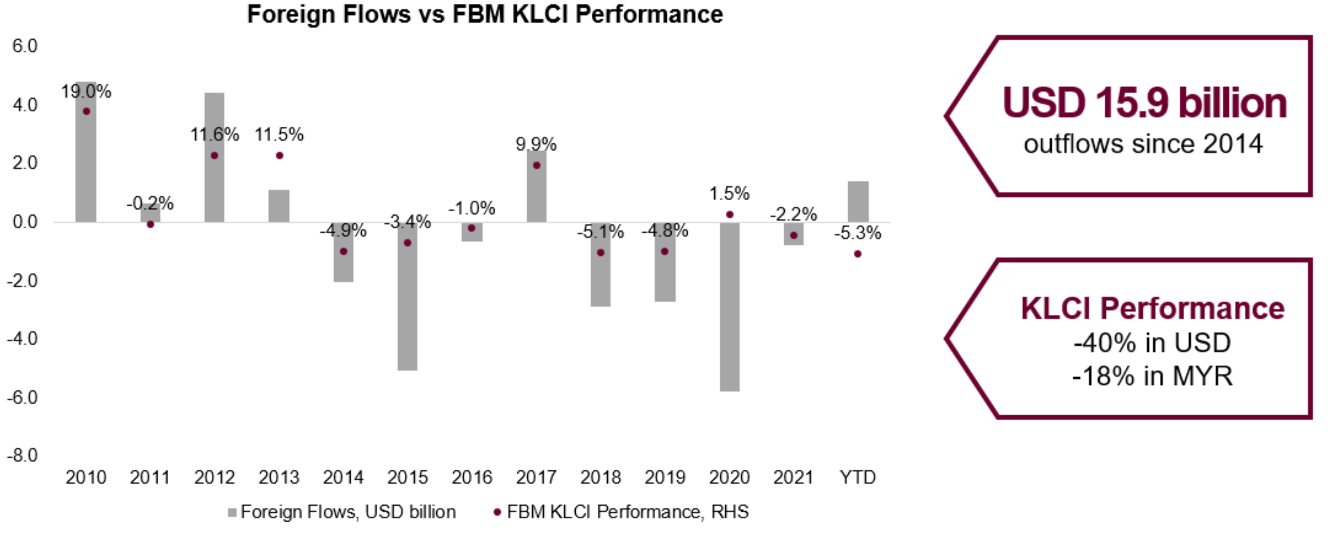
With emerging clarity and successful execution of policies, we expect the local market to gradual ascend higher as it climbs over walls of worry in the political sphere. The first obstacle is when Prime Minister Datuk Seri Anwar Ibrahim tests his parliamentary majority through a vote of confidence on the 19th December when Parliament convenes.

With low positioning and foreign funds underweight Malaysia, we could see as much as RM10 billion in terms of foreign inflows, should foreign investors neutralise their benchmark-weights in Malaysia as confidence grows with greater clarity.

It is still early-stage but Malaysia could emerge as a prime growth destination for reinvestment and political stability in the region after being out of the radar for so long.

We've seen strong appetite for Malaysia as evidenced by the sharp gains seen in the local market when Datuk Seri Anwar Ibrahim was appointed as Prime Minister which ended the political impasse. The rally was broad-based across sectors and driven by both domestic and foreign inflows suggesting that investors are willing to relook at Malaysia again for opportunities.

Graph 2: Foreign Flows Vs. FBM KLCI Performance



Source: Bloomberg, J.P. Morgan, Bursa Malaysia, as at October 2022

Portfolio Positioning

Incremental positives domestically as well as in the macro environment with tentative signs showing US inflation peaking could signal an inflection point for Malaysian equities as the Fed tones down its hawkish rhetoric.

A renewed zeal to carry out reforms and to avoid repeating the same mistakes also augurs well for the unity government as it finds its footing.

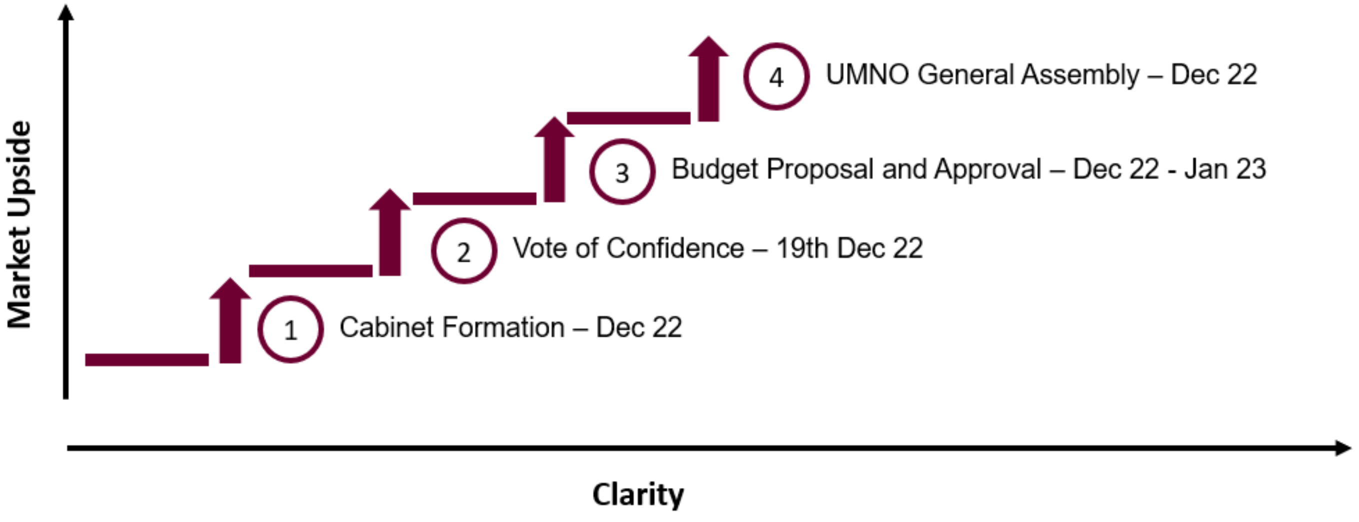
While recognising that there is a timing trade-off between waiting for more clarity but also potentially missing out on gains, we find the balance of risks tilted towards the upside.

We are taking a selective approach towards building exposure through large caps in particular:-

- Banks which continue to offer attractive dividend yields;
- Property stocks as a potential investment cycle play;
- Healthcare names given potential doubling of budget spending here;
- Beneficiaries of labour shortage restructuring;
- Beneficiaries of Ringgit strength and subsidy restructuring and;
- Reopening-plays as more cross-border restrictions are lifted.

Graph 3: Overcoming Walls of Worry

Successful execution of policies and reforms will bring upside to markets



Source: AHAM Capital, as at November 2022

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