Kenanga Investors

Date: 19 May 2015

Top Fund sees Bargains in Small Stocks at 39% Discount

The Edge Financial Daily (19 May 2015)

KUALA LUMPUR: The country's top performing fund manager is adding to holdings of small cap stocks, betting that a bull market rally will continue as earnings improve and valuations trail larger peers. Kenanga Investors Bhd. favours exporters and builders as the US economy recovers and Malaysia boosts spending on infrastructure, chief investment officer Lee Sook Yee said in an interview.

The FBM Small Cap Index is valued at 10.2 times estimated earnings, a 39% discount to the FBM KLCI.

Smaller companies are involved in more diverse industries with better prospects than larger peers, which are dominated by banks and commodity producers, Lee said. Profits of companies in the small cap measure will increase 21% in the next 12 months, compared with a 3.5% gain for the KLCI, analyst estimates compiled by *Bloomberg* show.

"Small caps will continue to outperform the narrower KLCI and lead the recovery," said Lee, who helps oversee RM5.6 billion. "Even after the outperformance, we continue to see value within this space."

The small cap index rose 0.3% to a three-week high at the close in Kuala Lumpur. It has surged 11 % this year, more than triple the KLCI's 3.5% gain.

Lee said exporters are benefiting from the weaker ringgit as well as being "indirect proxies" to the recovery in both the technology industry and US consumer confidence.

Inari Amertron Bhd, the semiconductor packager whose main client is US-based Avago Technologies Ltd, is among the best performers on the small cap gauge this year, with a 41% advance. Malaysian Pacific Industries Bhd, a semiconductor company which gets 29% of its revenue from the US, has jumped 48%.

The ringgit has fallen 6.1% against the US dollar in the past six months, the second biggest drop after the rupiah, helping to boost overseas earnings for exporters. The US labour market has continued to strengthen, with data last week showing the fewest jobless claims in 15 years, while the Nasdaq Composite in April topped its 2000 dot-com-era high.

The Kenanga Growth Fund, set up for long-term capital growth and to outperform the KLCI, has returned 21% annually in the past five years to beat 87 peers with assets of more than US$100 million (RM357 million), according to data compiled by *Bloomberg*. Kenanga's top holdings include builders HM Corp and Gamuda Bhd.

IJM, whose net income doubled in 2014 from a year earlier, has risen 8.4% this year. Gamuda, which is helping to develop the Klang Valley Mass Rail Transit system, posted a 33% increase in 2014 net income.

The government plans to spend RM48.5 billion on development this year, including the Pan-Borneo Highway and other transport links. Malaysia cut its 2015 economic growth target in January to 4.5% to 5.5% from an earlier projection of as much as 6%, citing the dampening effect of an oil price slide. Oil-related contributions make up almost 30% of annual state revenue.

"The larger cap stocks within the KLCI consist mainly of banks, plantation and oil and gas names, and the current macro environment doesn't favour those few sectors aforementioned," Lee said. "On the other hand, the small cap universe consists of companies with very diversified business sectors and some of them offer superior earnings growth profiles."

Malayan Banking Bhd and Tenaga Nasional Bhd, the nation's two biggest listed companies by market value, have gained less than 2% this year. Oil palm planter IOI Corp has fallen 11% in the period after reporting a 75% slump in second-quarter net income.

The gauge of smaller companies entered a bull market last month after rebounding more than 20% from its December low. The measure has since dropped 2.6% from its April 21 high.

"The small cap index has had a good run year-to-date," Lee said."As long as macro conditions remain intact, any corrections are more likely to represent a mid-cycle consolidation rather than a trend reversal." — *Bloomberg*

Source: ***The Edge Financial Daily (19 May 2015)***

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