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SET PROVES RESILIENT IN FACE OF NEGATIVE NEWS; DOWNSIDE RISK TO GROWTH RISING

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Market sentiment has improved over the past week, despite the constant flow of negative news. The SET Index rebounded 6.1 per cent from the low of 1,364.09 points in the past two weeks to close at 1,446.45 on Thursday, beating the MSCI AC ex-Japan Index's rebound of 3.7 per cent from its low last week.

The market was still pressured by foreign fund outflows with cumulative foreign net sales of Bt28 billion in the last two weeks, but this has improved slightly from net sales of Bt32 billion in the first two weeks of June. Local institutions, brokerages and retail investors were net buyers with aggregate value of Bt28 billion.

At the macro level, the downside risk to growth is rising. The major economic agencies have slashed their GDP growth targets for this year. The National Economic and Social Development Board is now expecting growth this year at the low end of its 4.2-5.2-per-cent range, while the Fiscal Policy Office cut its growth estimate to 4.5 per cent from 4.8 per cent, citing weak global demand and baht volatility, which has pressured export growth, as well as frail domestic consumption.

That said, we also see downside risk to our present GDP forecast of 5 per cent and may look to revise our growth target to 4.6 per cent should infrastructure projects fail to roll out this year.

On the interest rate trend, we expect the policy rate to be maintained at 2.5 per cent until 2Q14 when we expect the Bank of Thailand to shift to a hawkish stance with a 25bp hike, possibly due to higher inflation.

We have recently cut our year-end SET Index target to 1,500 points, as our study suggests QE tapering should push the US Term Spread and VIX up and consequently drive the Thai equity risk premium (ERP) higher. This should result in the SET's P/E contraction. Assuming ERP at 4.06 per cent, bond yield at 2.82 per cent and EPS growth of 20 per cent, the fair SET Index level would be around 1,500.

With the weaker baht, we see exporters that derive their revenue in foreign currencies as major beneficiaries. Clear winners are DELTA and HANA. AOT managed to convert yen-denominated loans into baht in May at the time when the yen was very weak and therefore could see some forex gain in 3Q13 (April-June). The losers are importers and those with net foreign currency loans, such as TVO and THAI.

Also, if interest rates rise next year, companies with high net gearing and high floating-rate debts could be more vulnerable. These include TRUE, ROJNA, ITD and SPCG.

TISCO SECURITIES

Thai equities face further turbulence this month after a rollercoaster ride last month that saw the SET fall to six-month lows before rallying in the final days of the month. The sharp rise in US bond yields amid a rebalancing in the portfolios of global investors has triggered heavy outflows from emerging markets including Thailand.

However, foreign investors were strong buyers of Bt5.9 billion of Thai equities last Thursday, although some of this was likely due to window dressing and short covering.

In the very near term, the Thai market looks set to claw back more of its recent losses due to an improvement in global sentiment caused by the improving liquidity situation in China's interbank market and the downward revision to US 1Q13 GDP to 1.8 per cent QoQ annualised from 2.4 per cent. The disappointing GDP data have raised hopes among investors that the Fed may delay its plans to taper QE3.

On the domestic front, the SET could get a boost from the Cabinet reshuffle, aimed at shoring up the government's popularity. However, the upside may be limited by a new series of GDP downgrades by Thai government agencies as well as the Central Administrative Court's decision to put the Bt350 billion water management project on hold until public hearings are conducted.

The 2H13 outlook for the Thai market also remains clouded by the slowdown in China's economy and the potential for further baht downside following the weaker-than-expected Thai import-export data for May and another large trade deficit.

We continue to favour selective telecom stocks, notably ADVANC and INTUCH, due to their multiyear earnings growth outlook and their attraction as dividend yield plays. Given that operators are already seeing lower regulatory costs from the first wave of 3G migration, we believe the downside to the share prices of major telecoms is limited. Other stocks we like at current levels include AOT, SIRI, BGH and STEC.

The recent sell-off in bank stocks makes the sector's valuations more attractive, and presents good bargain-shopping opportunities, particularly for SCB, KK and BAY. Note that BAY's share price climbed 7 per cent last week following Japanese media reports that Mitsubishi UFJ Financial Group plans to acquire up to 51 per cent of the Thai bank in a deal valued at US$4.1 billion, or two times 2013F BVPS.

In the current volatile environment, we expect BAY to outperform the sector on M&A speculation. We consider the M&A pricing of 1.8-2 times PBV (15 per cent + upside from the current price) as reasonable in light of BAY's mid-teen ROE, cleaned-up balance sheet and strong retail banking franchise.

RESEARCH DEPARTMENT

Trinity Securities

Waiting for a clear sign of fund flows

The SET Index rebounded following other stock markets across the world last week after the United States reported first-quarter GDP growth of 1.8 per cent, lower than analysts' expectations, in its final round. With this, investors expect the Fed to extend its QE. The SET Index also gained benefits from the close of window dressing for the second quarter.

We are keeping an eye on fund flows, particularly foreigners' net purchases of Thai stocks in the past few days. However, we have not seen a certain flow of funds into the bond market and that will not likely happen soon, given the nearly smallest difference between the returns on Thai bonds and US bonds in one year. This factor is expected to pressure the baht to weaken further.

We see the SET Index's recent rebounds as an opportunity to sell stocks for cash, given its temporary rebound period until the flow of funds returns. Thai stocks will become attractive again if the SET Index's earnings yield gap moves to its average of 1,320 points.

Selective buys include stocks that are referred to the global recovery theme with low downside risk or very low valuation compared to the past. Stock picks: PTT, communications group with high dividend yields, ADVANC and INTUCH, underweight stocks related to domestic consumption, particularly those in the retail group, and the property sector and commercial banking group due to signs of a slowdown in domestic demand in the light of the higher household debt burden.

Investors should take more precautions with firms with a high proportion of exports to China, given the downside risk to China's consumption on lower credit.