

15 August 2017

NAGA Warrants 2017 Eighth Issuance

Selective Picks to Navigate an Uncertain Market

By Lawrence Yeo Eng Chien | lawrenceyeo@kenanga.com.my

Last Friday, the FBMKLCI suffered its worst drop in three months as global markets sold off amid a war of words between US president Donald Trump and North Korean leader Kim Jong Un that stoked concerns over a nuclear threat. Although the North Korea rhetoric had somewhat settled down this week, Friday's sharp pull-back underscores the market's fragility after a period of relative calm. As it is, the FBMKLCI's overall technical picture is signalling some risk given the "Dead Cross" between the 20-day and 50-day SMAs while foreign investors turned net sellers last week after four consecutive weeks of net buying.

Of note, the FBMKLCI's 14-day volatility jumped from the lowest level in eleven years (2.1%) last week and currently stands at 4.6%. Even so, market volatility remains uncharacteristic low and we do not rule out the possibility of a spike ahead – potentially creating fertile grounds for traders who wish to benefit from the widening premiums.

In today's batch of Naga Warrants issuances, Equity Derivatives will be issuing 12 Structured Warrants comprising AXIATA-C21 (strike: RM5.35), CIMB-C27 (strike: RM7.70), HENGYUAN-CD (strike: RM7.00), HENGYUAN-CE (strike: RM8.80), KOSSAN-CV (strike: RM7.70), MALAKOF-C3 (strike: RM1.00), MAYBANKC33 (strike: RM10.00), MRCB-C23 (strike: RM1.30), MISC-C13 (strike: RM8.00), PMETAL-CU (strike: RM3.00), SPSETIA-C1 (strike: RM3.50), SIME-C15 (RM10.00).

Structured Warrants Commentary

Most of the new Naga Warrants are being issued to replace expiring structured warrants from previous listings, with an additional few being provided as added tools for investors who wish to trade on the more active news-driven counters. Although, we have just two underlying counters with an OUTPERFORM call from this batch (**PMETAL-CU** and **SPSETIA-C1**), we see potential for **HENGYUAN-CD**, **HENGYUAN-CE**, **KOSSAN-CV** and **MAYBANKC33** to attract some trade from a charting perspective.

For **PMETAL (OP; TP: RM4.05)**, we recently upgraded our target price from RM3.15 after Bloomberg reported that China is clamping down on c.10% of its aluminium production. According to the report, China has called for the closure of 3.21m MT of illegal aluminium capacity in China's key aluminium production hub, Shandong - resulting in aluminium prices spiking beyond the USD2,000/MT mark for the first time since end-2014. Fundamentally, we believe that **PMETAL** stands to benefit given aluminium price's recent jump to a 3-year high and have conservatively increased our FY18 aluminium price assumptions to USD1,900/MT. At the same time, we have also rolled over our valuation base year and applied a higher PER valuation of 18x (from 17x earlier).

Meanwhile for **SPSETIA (OP; Ex/Cum -TP: RM4.08/ RM4.24)**, recent corporate exercise includes plans to acquire I&P for RM3.65b which necessitated a target price upgrade from RM3.86 previously. Post-acquisition, **SPSETIA** will become the third largest land owner with 9,417ac just behind **SIME** and **UEMS** in terms of land bank size. Overall, we are long-term positive on the deal as the synergies from both companies will take time to materialize. However, investors will need to give **SPSETIA** 1-2 years before I&P's land banks can be realized more aggressively. In the meantime, we expect FY18E core PER to expand by 31% to 21.7x and have raised our FY18E CNP by 5% after accounting for I&P's potential contributions and iRCPS costs.

Worthy of mention, **HENGYUAN** experienced active trading in its shares and has been the subject of wire-news highlights in recent weeks. Of the twin **HENGYUAN-CD** and **HENGYUAN-CE** listings, we favour **HENGYUAN-CD (strike: RM7.00)** for trading shorter term movements given its high effective gearing of 5.0x. This structured warrant is in-the-money, making the price more sensitive to changes in the underlying share price and facilitating a smoother entry and exit.

Conversely, **HENGYUAN-CE (strike: RM8.80)** is more suited for longer-term traders who expect high upside potential in the underlying share price. Although **HENGYUAN-CE** is out-of-the-money, effective gearing is still decent at 3.1x while the main advantage lies in its comparatively low delta of 0.53 (vs 0.77 for **HENGYUAN-CD**)

These 12 structured warrants are priced with a range of +/-17% moneyness. All the warrants issued are European Styled Non-Collateralised Cash Settled Warrants with a tenure of 7 months. The gearing ranges from as low as 3.4x to as high as 16.1x and the conversion premium ranges from 5.1% to 36.8%. Call-warrants are leveraged instruments.

For instance, by participating in **PMETAL-CU**, an investor is exposed to a gearing of 4.8x. To be more precise, this call warrant offers up to 2.8x effective gearing for traders. Given our fundamental target price of RM4.05 (implying a potential upside objective of 41.6% based on the EOD price of RM2.86). Theoretically speaking, a 41.6% increase in the underlying price should translate to ~117% gain in **PMETAL-CU**. This general estimate is applicable to other Naga Warrants as well.

15 August 2017

Table 1: Warrant Parameters

Name	Time to Expiry	Spot Price (RM)	% of Spot Price	Exercise Price (RM)	Exercise Ratio	Warrant Price (RM)	Gearing (x)	Effective Gearing (x)	Conversion Premium
AXIATA-C21	7 months	4.69	114.1%	5.35	4.0	0.15	7.81	3.79	26.9%
CIMB-C27	7 months	6.56	117.4%	7.70	4.0	0.15	10.93	4.61	26.5%
HENGYUAN-CD	7 months	7.80	89.7%	7.00	8.0	0.15	6.50	5.00	5.1%
HENGYUAN-CE	7 months	7.80	112.8%	8.80	9.0	0.15	5.78	3.08	30.1%
KOSSAN-CV	7 months	7.30	105.5%	7.70	7.0	0.15	6.95	3.81	19.9%
MALAKOF-C3	7 months	1.03	97.1%	1.00	2.0	0.15	3.43	2.28	26.2%
MAYBANKC33	7 months	9.65	103.6%	10.00	4.0	0.15	16.08	8.11	9.8%
MRCB-C23	7 months	1.17	111.1%	1.30	2.0	0.15	3.90	2.34	36.8%
MISC-C13	7 months	7.60	105.3%	8.00	4.0	0.15	12.66	6.29	13.2%
PMETAL-CU	7 months	2.86	104.9%	3.00	4.0	0.15	4.77	2.82	25.9%
SPSETIA-C1	7 months	3.28	106.7%	3.50	2.0	0.15	10.93	5.40	15.9%
SIME-C15	7 months	9.39	106.5%	10.00	5.0	0.15	12.52	6.05	14.5%

* Note that the share prices are on a closing basis. Data is as at EOD.

Daily Charting – Hengyuan Refining Co Berhad (HENGYUAN)



Source: Bloomberg, Kenanga Research

Technical Ratings

Name : Hengyuan Refining Co Berhad
Bursa Code : HENGYUAN

Key Resistance and Support Levels

R2 : RM 10.00 (123.6% FP/ Psych. level)
R1 : RM 8.50 (August high)
Closing : RM 7.50
S1 : RM 6.96 (23.6% FR level/ 20-day SMA)
S2 : RM 6.00 (May-June resistance-turned-support)

Theoretical Warrants Price (HENGYUAN-CE)

TWR 2 : RM0.28
TWR 1 : RM0.19
- : -
TWS 1 : RM0.10
TWS 2 : RM0.04

HENGYUAN has been on a strong uptrend since December last year, having quadrupled from a low of RM2.00 to as high as RM8.50 recently. Although the share price has pulled back over the past week, its medium-to-longer term technical picture remains positive while the momentum indicators reflect a healthy pause in an overall uptrend. From here, any share price weakness is likely to be shallow and temporary, with an eventual retest expected of this month's high of RM8.50 (R1) before a further climb towards RM10.00 (R2) further up. Support levels likely to see buying interest are RM6.96 (S1) and RM6.00 (S2).

This section is intentionally left blank

15 August 2017

Daily Charting – Kossan Rubber Industries Berhad (KOSSAN)



Source: Bloomberg, Kenanga Research

Technical Ratings

Name : Kossan Rubber Industries Berhad
 Bursa Code : KOSSAN

Key Resistance and Support Levels
 R2 : RM 8.00 (61.8% FR level)
 R1 : RM 7.56 (Channel resistance)
 Closing : RM 7.15
 S1 : RM 7.00 (Channel support)
 S2 : RM 6.50 (23.6% FR level)

Theoretical Warrants Price (KOSSAN-CV)

TWR 2 : RM0.22
 TWR 1 : RM0.18
 - : -
 TWS 1 : RM0.14
 TWS 2 : RM0.10

KOSSAN has been trading within an uptrend channel since its RM5.62 low in May. Since then, the share price has risen to an 18-month intraday high of RM7.36. Although the share price is currently taking a breather from overbought levels, its uptrend channel remains intact while the key SMAs (20-, 50- and 100-day) are in a positive crossover. From here, look to enter on any dips towards RM6.90/7.00 (S1) where the channel support line is located. Failing which, the next major support level is RM6.50 (S2). Overhead resistance levels include RM7.56 (R1) and RM8.00 (R2).

Daily Charting – Malayan Banking Berhad (MAYBANK)



Source: Bloomberg, Kenanga Research

Technical Ratings

Name : Malayan Banking Berhad
 Bursa Code : MAYBANK

Key Resistance and Support Levels
 R2 : RM 10.50 (138.4% FP level)
 R1 : RM 10.18 (123.6% FP level)
 Closing : RM 9.69
 S1 : RM 9.67 (Resistance-turned-support)
 S2 : RM 9.25 (May lows)

Theoretical Warrants Price (MAYBANKC33)

TWR 2 : RM0.255
 TWR 1 : RM0.215
 - : -
 TWS 1 : RM0.15
 TWS 2 : RM0.10

Last September, MAYBANK kicked off an uptrend, and has since climbed from RM7.50 to as high as RM9.84 earlier this month. Notably, the share price had recently punched through its crucial RM9.67 horizontal resistance to signal a continuation of its prior uptrend after a three-month long sideways hover. As a result, the MACD has also crossed above its Signal line to reflect this shift in sentiment. With the share price now at a three-year high, we envisage a clear path towards resistance levels of RM10.18 (R1) and RM10.50 (R2) next. Downside support levels include the aforementioned RM9.67 (S1) resistance-turned-support. Failing which, the next support is located at RM9.66 (S2) below.

15 August 2017

Daily Charting – Press Metal Aluminium Holdings Berhad (PMETAL)



Source: Bloomberg, Kenanga Research

Technical Ratings

Name : Press Metal Aluminium Holdings Berhad
 Bursa Code : PMETAL

Key Resistance and Support Levels

R2 : RM 3.55 (138.2% FP level)
 R1 : RM 3.39 (123.6% FP level)
 Closing : RM 3.26
 S1: : RM 3.00 (Resistance-turned-support)
 S2: : RM 2.84 (Congestion zone/ 20-day SMA)

Theoretical Warrants Price (PMETAL-CU)

TWR 2 : RM0.25
 TWR 1 : RM0.23
 - : -
 TWS 1 : RM0.17
 TWS 2 : RM0.15

After a strong run-up from January-April period, PMETAL subsequently entered into a period of sideways trading in the following months. Nevertheless, the share price has now taken out its May's high of RM3.00 into fresh record high. Trading volume was explosive during the breakout. Although the RSI and Stochastic indicators have become overbought, PMETAL's overall technical picture is now in a bullish state. Any weakness back towards RM3.00 (S1) and RM2.84 (S2) support levels can be viewed as a buying opportunity while overhead resistance levels to look out for are RM3.39 (R1) and RM3.55 (R2) further up.

This section is intentionally left blank

15 August 2017

Glossary

Gearing

The additional exposure gained on the underlying by purchasing warrants.

Formula:

$$\text{Gearing} = \frac{\text{Underlying price}}{\text{Warrant price} \times \text{Exercise ratio}}$$

Example, gearing of a warrant is 10x, it means using the same amount of capital, you will have 10 times more exposure than if you purchased the underlying.

To estimate the increase / decrease in the warrant price relative to the underlying price, we should look at effective gearing.

Implied Volatility

The most important indicator when assessing a warrant. It refers to the estimate of future price volatility of a specified underlying asset and is used by the market as an indicator to decide whether a warrant is cheap or expensive.

All things being equal, the higher the expected volatility, the higher the warrant price.

Effective Gearing

Effective gearing reflects the relationship between changes in the warrant price and in the underlying price.

Formula:

$$\text{Effective Gearing} = \text{Gearing} \times \text{Delta}$$

Effective gearing of 10 times, other things being equal, means for every 1% change in underlying price, the warrant price moves by 10%.

Delta

Measures the theoretical movement in warrant price when the price of the underlying asset changes. Delta for Call Warrant lies between 0 and 1.

Formula:

$$\text{Delta} = \frac{\text{Change in warrant price} \times \text{Exercise ratio}}{\text{Change in the underlying price}}$$

Example, a call warrant with an exercise ratio of 1,

A delta of 0.50 implies that if the value of the underlying changes by 20 sen, then the value of the call warrant should change by 10 sen.

Premium

Price difference between buying and exercising the warrant, compared to a direct purchase of the underlying asset.

Formula:

$$\text{Premium for Call warrant} = \frac{[(\text{Warrant price} \times \text{Exercise ratio}) + \text{Exercise price}] - \text{Underlying price}}{\text{Underlying price}}$$

Volatility

The uncertainty in the movement of prices which will affect the return of an underlying.

This document has been prepared for general circulation based on information obtained from sources believed to be reliable but we do not make any representations as to its accuracy or completeness. Any recommendation contained in this document does not have regard to the specific investment objectives, financial situation and the particular needs of any specific person who may read this document. This document is for the information of addressees only and is not to be taken in substitution for the exercise of judgement by addressees. Kenanga Investment Bank Berhad accepts no liability whatsoever for any direct or consequential loss arising from any use of this document or any solicitations of an offer to buy or sell any securities. Kenanga Investment Bank Berhad and its associates, their directors, and/or employees may have positions in, and may effect transactions in securities mentioned herein from time to time in the open market or otherwise, and may receive brokerage fees or act as principal or agent in dealings with respect to these companies.

Published and printed by:

KENANGA INVESTMENT BANK BERHAD (15678-H)

Level 12, Kenanga Tower, 237, Jalan Tun Razak, 50400 Kuala Lumpur, Malaysia
Telephone: (603) 2172 0880 Website: www.kenanga.com.my E-mail: research@kenanga.com.my



Chan Ken Yew
Head of Research