

## Strategy

### Strong bull market losing steam

#### Key message

1. We believe the bullishness in the Taiex market will lose steam after hitting the 20,000-point mark.
2. Upswings brought by the AI frenzy have just reached the midpoint of the bull term during the dotcom bubble, thus we believe a long-term Taiex bull run is probable.
3. Our preferences are stocks with high yield and a low base as the Taiex consolidates.

#### **The bullishness in the Taiex market will fade after hitting the 20,000-point mark**

The Taiex surged 2,000 points, hitting the 20,000-point mark, over the past month, reflecting fears of missing out (FOMO) on the AI frenzy. Although 2024-25F profitability of the Taiex will soar rapidly, driven by the AI trend, we expect the 'fast' bull will turn into a 'slow' bull, as skyrocketing share prices have diverged too far from fundamentals in the near term, indicating the Taiex rally will convert into consolidation at high levels while fundamentals recover. Results revealed over the past month were largely in line with expectations, and the consensus profitability forecast for Taiex-listed companies thus remains intact. However, on the back of the share price surge, the forward 12-month PE of the Taiex soared rapidly to 19x from 16x, exceeding the long-term average of 15x by 1-2 standard deviations (SD), approaching the levels of two historical peaks. The forward 12-month PE peaked during the China-US trade war, at 20x, and the COVID-19 pandemic, at 19x. Moreover, over two thirds of the sectors or counters posted less-than-stellar sales achievements in accumulated January-February sales, relative to 1Q24 forecasts. 1Q24F results, which will determine the Taiex trend in April and May, may be disappointing unless sales in March register a significant jump.

#### **The AI frenzy has reached the midpoint of the equivalent bull term of the dotcom bubble & we believe a long-term Taiex bull run is sustainable**

The bull run for the tech sector, which was the leading sector in US stocks during the dotcom bubble, continued to 1Q00 from its start in 1998. The bull run lasted for over two years, while share prices doubled. The forward PE also peaked at 75x from 24x. The AI frenzy that started in 2023 has only lasted for one year to date, with share prices increased by 50%, and seen forward PE trend up to 37x from 22x. Compared to the dotcom bubble, we believe the current AI frenzy has just reached the midpoint of its bull run. Additionally, corporate earnings growth driven by the AI trend is more significant compared to that seen during the dotcom bubble. As Taiwan firms are key suppliers to the AI arms race, we expect 2024-25F Taiex overall earnings growth to be above 20%. We will revisit our prediction of a 20,000-point peak when 1Q24 results are revealed.

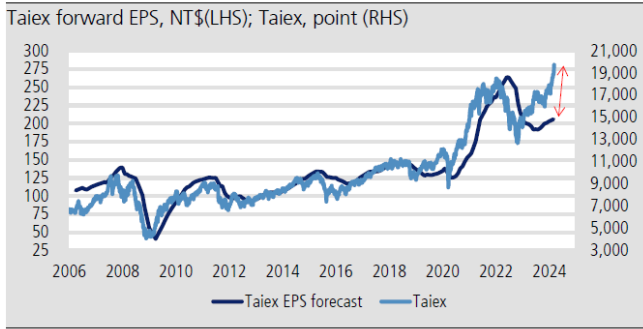
#### **We recommend investors engage high-yield stocks and sub-sectors with low bases and valuations as the Taiex consolidates**

We recommend investors engage high-yield stocks and sub-sectors with low bases and valuations as the Taiex consolidates at high levels. Historically, high yield stocks easily attract funds during the second and third quarters. Additionally, valuations will be bolstered by high-dividend ETF passive funds this year. Sub-sectors with low bases and valuations include bicycles, industrial automation, smartphones, PC, automotive components and aerospace.

#### **Valuation & Action**

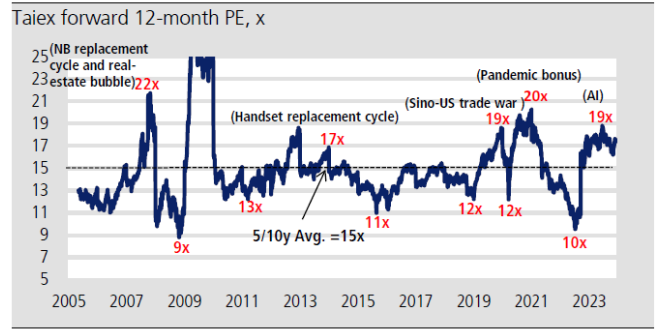
Compared to the dotcom bubble, the AI frenzy has just reached the mid-point of its bull run. Hence, we believe a long-term bull run for the Taiex is sustainable. However, as the Taiex rally has diverged away from fundamentals, we think the strength of the bullishness in the market will fade, implying the index may shift to consolidation at high levels from a strong rally. We recommend investors start to engage high-yield stocks and sub-sectors with low bases and valuations.

Figure 1: The Taieix, which saw a rapid jump recently, has diverged too far from fundamentals



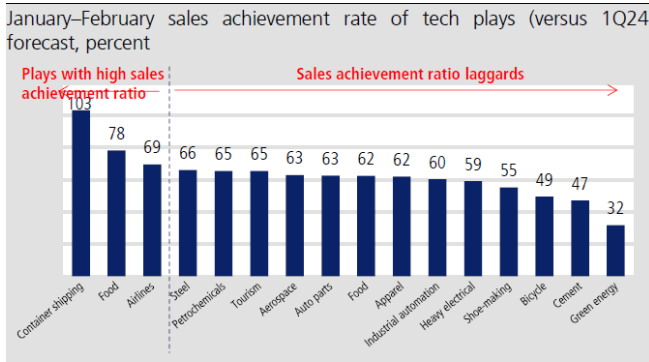
Source: Bloomberg; KGI Research

Figure 2: Forward PE of the Taieix soared to 19x from 16x



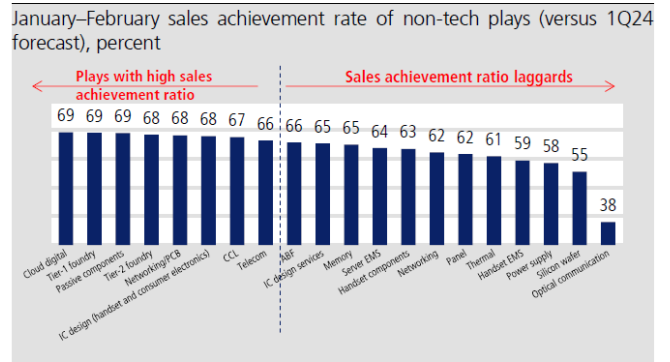
Source: TEJ; KGI Research and KGI estimates

Figure 3: Only 30% of tech plays achieve the 1Q24 forecast



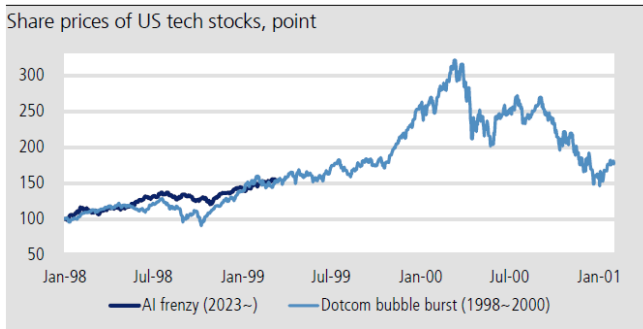
Source: TEJ; KGI Research and KGI estimates

Figure 4: Only 20% of non-tech plays achieve the 1Q24 forecast



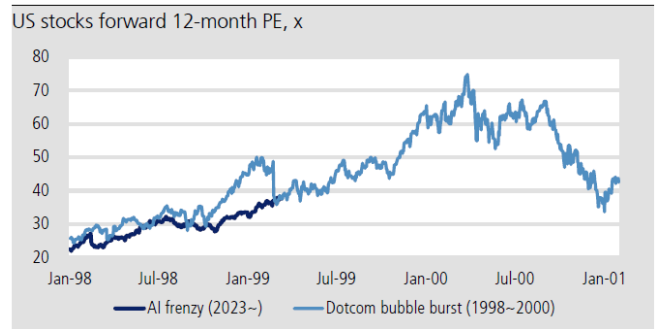
Source: TEJ; KGI Research and KGI estimates

Figure 5: The stock price performance affected by the AI frenzy have just arrived at the mid-point of the dotcom bubble bull run



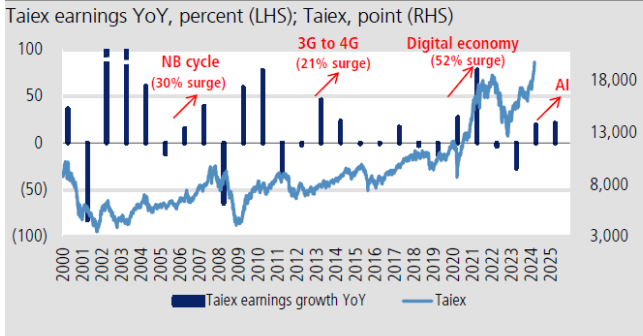
Source: Bloomberg; KGI Research

Figure 6: The valuations affected by the AI frenzy have just arrived at the mid-point of the dotcom bubble bull run



Source: Bloomberg; KGI Research

**Figure 7: 2024-25F earnings growth of the Taiex will be over 20%, bolstered by the AI frenzy**



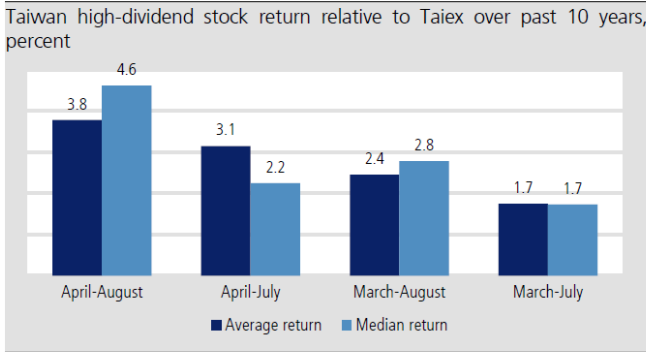
Source: TEJ; KGI Research and KGI estimates

**Figure 8: The Taiex 2H24F peak hinges on PE valuations from consensus for 2025F earnings**

Forecasted Taiex matrix (points)	Target PE(X)						
	15	16	17	18	19	20	21
0	15,568	16,606	17,643	18,681	19,719	20,757	21,795
10	17,125	18,266	19,408	20,549	21,691	22,833	23,974
15	17,903	19,096	20,290	21,484	22,677	23,871	25,064
20	18,681	19,927	21,172	22,418	23,663	24,908	26,154
25	19,460	20,757	22,054	23,352	24,649	25,946	27,244
30	20,238	21,587	22,937	24,286	25,635	26,984	28,333
35	21,016	22,418	23,819	25,220	26,621	28,022	29,423

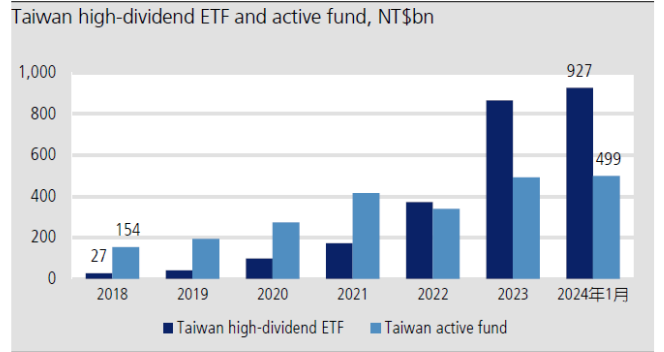
Source: KGI Research and KGI estimates

**Figure 9: High-dividend stocks outperform in April-August, with +4-5% returns relative to Taiex**



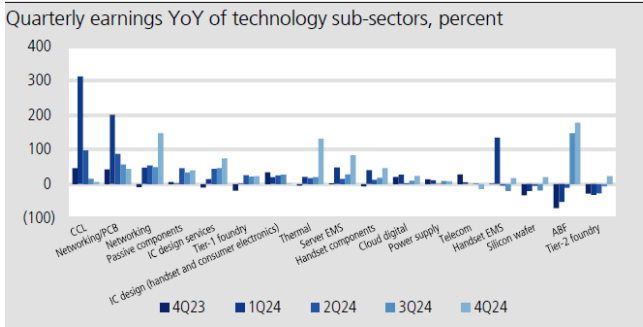
Source: TEJ; KGI Research

**Figure 10: Taiwan's high-dividend ETF market nears NT\$1.0tn**



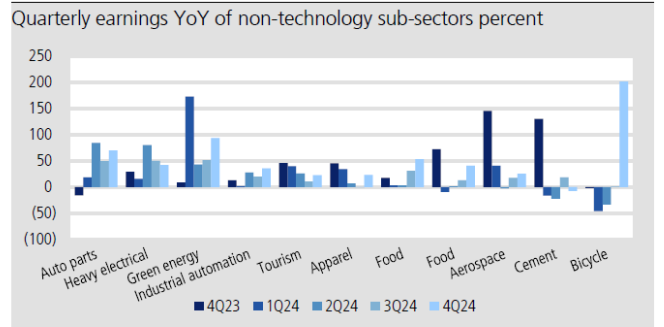
Source: TEJ; KGI Research

**Figure 11: Earnings momentum of the AI supply chain is relatively strong, while smartphone & consumer electronics are recovering from a bottom**



Source: TEJ; KGI Research and KGI estimates

**Figure 12: For non-tech plays, earnings momentum of auto components, industrial automation & bicycles is improving**



Source: TEJ; KGI Research and KGI estimates

**Figure 13: Taixex sub-sectors - Valuations**

	2022	KGI forecast		Consensus		Forecast PE(x)	
		2023F	2024F	2023F	2024F	2023F	2024F
Tech							
Optical communication	-	88.9	201.6	-	-	42.5	14.1
Networking PCB	56.1	(17.6)	75.5	(18.5)	73.5	21.8	18.5
Networking	239.5	47.0	75.1	58.7	75.7	21.5	16.9
CCL	(7.7)	8.2	52.6	9.0	50.0	31.1	20.4
ABF	102.5	(68.1)	47.5	(69.5)	52.8	327.5	17.6
IC design and service	94.8	5.3	45.3	7.2	44.7	67.2	47.5
Server EMS	(9.3)	9.1	42.9	9.6	42.6	34.8	22.5
Thermal	50.6	9.1	39.3	19.1	23.8	35.7	25.3
Passive components	(0.8)	(24.7)	30.2	(22.5)	27.8	14.0	10.8
Handset components	28.4	(36.5)	29.4	(34.9)	23.8	16.9	12.5
First-line foundry	70.4	(17.5)	18.0	(19.0)	20.0	23.7	20.1
IC design (handset/consumer electronics)	(2.9)	(32.6)	17.1	(35.5)	23.9	24.8	20.6
Cloud digital	16.3	19.9	15.5	17.8	18.2	31.7	25.4
Handset EMS	(2.1)	(7.2)	12.1	(5.0)	14.4	12.8	11.3
Power supply	15.1	4.3	6.7	5.1	15.7	20.6	19.1
Telecom	2.6	13.7	(2.4)	6.9	10.3	26.9	27.1
Silicon wafer	29.5	25.1	(7.9)	25.2	(9.6)	13.8	15.0
Second-tier foundries	51.6	(33.3)	(11.6)	(36.1)	(13.0)	13.5	16.2
Non-tech							
Steel	(75.4)	(89.0)	368.2	(91.0)	667.3	213.0	38.2
Green energy	56.9	69.7	76.0	91.7	54.0	32.1	14.4
Auto parts	52.8	(24.7)	54.1	(19.4)	42.8	20.7	13.3
Petrochemicals	(63.1)	(50.6)	52.6	(39.5)	41.3	48.0	26.5
Heavy electrical	(1.9)	39.4	45.1	42.7	39.5	40.5	26.7
Tourism	(46.5)	175.9	25.0	165.2	15.4	19.2	14.8
Industrial automation	5.2	(14.2)	21.5	(12.3)	23.8	36.2	28.5
Food	(2.9)	99.9	20.1	106.1	15.7	17.8	14.7
Aerospace	135.4	35.6	17.9	29.0	14.9	3.0	20.9
Apparel	32.1	(11.3)	14.1	(10.4)	17.0	26.1	22.9
Food	(13.6)	23.4	10.1	23.9	5.1	20.5	18.7
Bicycle	(12.7)	(39.1)	(3.7)	(36.1)	18.0	27.1	27.7
Cement	(50.7)	31.4	(9.3)	20.0	10.9	17.1	18.4
Airlines	(37.8)	201.9	(17.3)	209.8	(32.8)	12.4	15.9
Container shipping	19.7	(92.9)	(92.4)	(93.3)	(46.8)	N.M.	N.M.
Technology	17.8	(20.9)	23.2	(19.6)	24.0		
Non-tech	(12.0)	(68.2)	7.0	(67.4)	13.2		
Taixex	(3.7)	(28.7)	18.9	(34.4)	22.3		

Source: KGI Research and KGI estimates

**Figure 11: Taixex - Valuations**

	Forward PB(X)								Forward PE(X)							
	Forward 1-year	2024	2025	5-year average	10-year average	20-year average	2007 peak	2008 bottom	Forward 1-year	2024	2025	5-year average	10-year average	20-year average	2007 peak	2008 bottom
Taixex	1.98	1.98	1.83	1.71	1.61	1.61	2.28	0.95	19.01	19.01	15.70	15.00	14.89	17.11	21.73	8.80
Taixex excl. TSMC	1.52	1.52	1.41	1.39	1.38	1.46	2.22	0.89	18.54	18.54	15.04	14.69	14.88	16.01	22.71	8.06

Source: KGI Research and KGI estimates

Figure 15: Our top picks

	Company	Code	Investment rating	Target price (NT\$)	Mkt cap (US\$m)	Share price (NT\$)	Change +/- (%)	EPS (NT\$)		PE (x)		P/B (x)		ROE (%)		Cash yield (%)	
								2023F	2024F	2023F	2024F	2023F	2024F	2023F	2024F	2023F	2024F
High yield stocks	MTK	2454 TT	Neutral	986.0	61,857	1215.0	(18.8)	48.51	57.98	25.0	21.0	4.7	4.6	17.9	21.9	4.5	5.2
	UMC	2303 TT	Outperform	56.0	20,935	52.5	6.7	4.93	4.39	10.6	12.0	1.8	1.7	17.5	14.6	4.8	4.7
	Chicony	2385 TT	Outperform	152.0	5,479	226.5	(32.9)	10.35	11.69	21.9	19.4	4.3	4.0	20.1	21.1	3.2	3.6
	Catcher	2474 TT	Neutral	190.0	4,461	206.0	(7.8)	17.81	12.69	11.6	16.2	0.8	0.6	6.8	4.1	4.9	4.9
Low valuations with fundamentals troughing	Hon Hai	2317 TT	Outperform	126.0	52,505	119.0	5.9	8.55	10.40	13.9	11.4	1.1	1.0	8.0	9.3	3.7	4.5
	Largan	3008 TT	Outperform	3120.0	10,705	2520.0	23.8	134.17	155.78	18.8	16.2	2.0	1.8	11.1	11.8	2.7	3.1
	Airtac	1590 TT	Outperform	1230.0	6,715	1055.0	16.6	34.83	41.00	30.3	25.7	4.9	4.5	17.1	18.2	1.5	1.7
	Giant	9921 TT	Outperform	270.0	2,689	215.5	25.3	8.61	7.03	25.0	30.6	2.4	2.4	9.9	7.8	2.4	2.0
	Hu Lane	6279 TT	Outperform	185.0	530	167.0	10.8	9.21	11.98	18.1	13.9	2.8	2.6	16.0	19.4	3.3	4.2
DPI	4572 TT	Outperform	230.0	203	163.5	40.7	7.10	7.66	23.0	21.3	3.0	2.7	13.9	13.3	2.2	2.3	

Source: KGI Research and KGI estimates

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