

Strategy

Wait for the bottom

Key message

1. We are watching major events in September including economic data, industry guidance, monetary policy and the US presidential debate.
2. While the market is retreating, investors are advised to keep a weighting of stocks at 50% in their portfolios to create space for both aggressive and defensive trading strategies.
3. We recommend sectors like the iPhone supply chain, gaming, e-paper, foldable handset, financials and high-yield stocks.

More uncertainty ahead in September

The Taiex has pulled back once again after making a v-shaped turnaround on August 6. Such drastic consolidation came as debates continue among investors, about: (1) whether the US economy will make a hard or soft landing in the coming six months; (2) whether the Fed will cut interest rates by 25bps or 50bps in September; (3) when the Bank of Japan (BOJ) will raise interest rates again; (4) who will prevail in the US presidential election; and (5) whether the new iPhone 16 series can drive enough replacement demand. Uncertainties will linger for a while, but some upcoming major events will shape market views, consequently affecting the direction of the Taiex index. These events include: (1) the announcement of August US labor market results on September 6; (2) the debut of iPhone 16 models on September 10; (3) the US presidential debate on September 10; (4) the FOMC meeting on September 18; and (5) the Bank of Japan's (BOJ) monetary policy meeting on September 20.

Non-farm payrolls & the unemployment rate are key factors to watch for in the August labor market data to be released on September 6

The US will announce August labor market data on September 6, and we believe all eyes will be on non-farm payrolls and the unemployment rate. If the increase to non-farm payrolls falls below its three-month average of 160k jobs added, the market will assume a much higher probability of an economic hard landing, and vice versa. If unemployment stays flat MoM at 4.3% or rises, the odds of the US economy making a hard landing will rise substantially. The July labor market results took investors aback, as only 110k jobs were added to non-farm payrolls, and unemployment surged to 4.3%, adding to concerns about an economic hard landing. The current consensus on August results is for 170k jobs to be added to non-farm payrolls, and for unemployment to dip to 4.2%.

Market will be most curious about iPhone16 pricing and whether additional fees are required to access AI services

Hardware upgrades in the upcoming iPhone 16 series are not as significant as for previous series, and we believe the market will focus more on the pricing for the new models, as well as the user experience and fees for Apple Intelligence, which we see as the primary swing factors for replacement demand. If Apple transfers additional costs to consumers, it will undermine replacement demand, and if prices are kept unchanged from the previous iPhone 15 series, replacement demand will most likely be flat. Consensus argues that AI features to be launched along with the iPhone 16 series will be the primary driver of replacement demand, but we note it all comes down to the actual user experience and whether additional fees are required to access AI services. The pricing for Apple Intelligence has yet to be unveiled, but many predict that Apple will launch the service in a subscription business model similar to iCloud. Monthly subscription fees could range between US\$10-20 and services could be provided in a tiered system.

Swing state polling after the US presidential debate on September 10 will show who has the upper hand

The incumbent Vice President Kamala Harris was officially nominated for President by the Democratic Party on August 5. By mid-August, she had surpassed her competitor, Donald Trump in swing state polling, thus significantly reducing the risk of a second term for the former president, which many investors fret about. However, the latest polling in seven critical swing states suggest that Harris is leading by an average of only 0.2ppts (47.7% versus 47.5%), within the margin of error, and thus it is too early to tell who will be victorious. We believe the upcoming presidential debate on September 10 will help US voters acquire a better understanding of Harris' economic and trade policies, and swing state polling after the debate will tell us whether the risk of a Trump comeback will materialize.

Rate cut of 25bps or 50bps at September FOMC meeting is the focus of the market

It is now a consensus belief that the Fed will announce an interest rate cut at the September FOMC meeting. The question is the size – will there be a cut of 25bps or 50bps? The pace of rate cuts matters, as it will determine whether the market should anticipate a hard or soft landing ahead for the US economy. Since the 1990s, whenever the Fed cuts interest rates by 50bps or more in one go, the US economy has been in, or on the brink of, a recession. As such, if the rate cut announcement in September is a cut of 50bps, or the Fed provides forward guidance indicating a 50bp cut is around the corner, it will be negative for stock markets, including the Taiex.

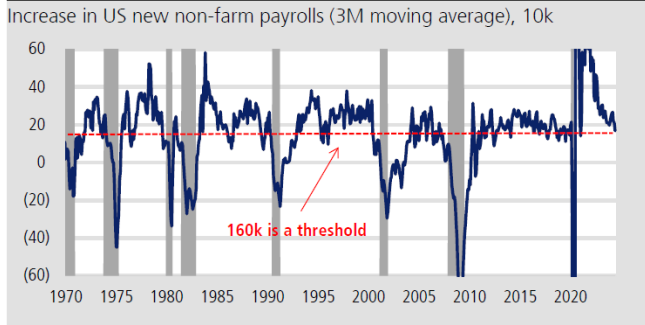
Will the BOJ provide guidance on next rate hike at the September 20 meeting?

The BOJ surprised the market by announcing a rate hike of 15bps on July 31, triggering a sharp appreciation of the Japanese yen and forcing investors to unwind their carry trade positions, leading to pullbacks in global stock markets. The next BOJ monetary policy meeting will take place on September 20, and we believe investors will be keen to know the BOJ's rate hike pathway. We recall four occasions where the US-Japan interest spread narrowed substantially since the 1990s, and the Japanese yen appreciated against the greenback by over 50%, 24%, 38% and 11%, respectively. The magnitude of yen appreciation is determined by the degree of interest spread narrowing. Specifically, we estimate that every 1ppt, or 100bp, narrowing of US-Japan interest spread will lead to 5-10% appreciation of the Japanese yen.

Valuation & Action

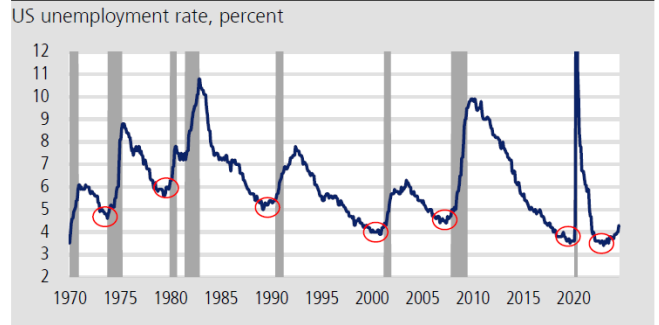
After some drastic swings in July, we believe volatility will continue as a result of multiple major events in September. Looking ahead, we expect the Taiex to rebound when uncertainties are gone and negatives have been priced in. While the market is still retreating, investors are advised to keep a weighting of stocks at 50% in their portfolios, to create space for both aggressive and defensive trading strategies. We recommend sectors like the iPhone supply chain, gaming, e-paper, foldable handset, financials and high-yield stocks.

Figure 1: The US economy will most likely make a hard landing if non-farm payrolls sink below 160k jobs added



Note: Shaded areas indicate US economic recessions
Source: Bloomberg; KGI Research

Figure 2: Sharp upticks in the US unemployment rate following a rebound from a trough often entail a significant economic downturn



Note: Shaded areas indicate US economic recessions
Source: Bloomberg; KGI Research

Figure 3: All eyes are on prices for the upcoming iPhone 16 series

Retail prices for iPhone 15 models in the US upon debut (September 2023)

iPhone 15 series	Retail price in the US
iPhone 15	US\$799 up
iPhone 15 Plus	US\$899 up
iPhone 15 Pro	US\$1,099 up
iPhone 15 Pro Max	US\$1,299 up

Source: Apple; KGI Research

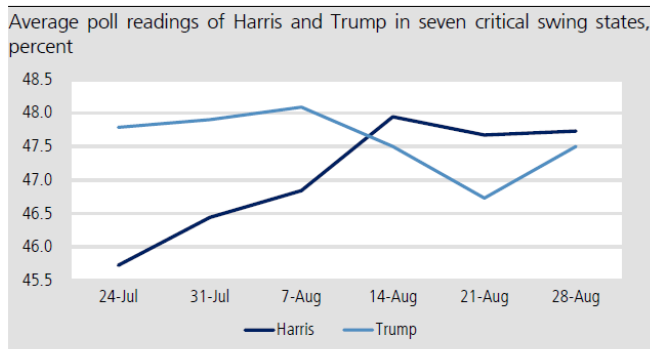
Figure 4: Pull-in from assemblers of iPhone 16 to increase by 6-12% compared to iPhone 15

iPhone new model stocking-up at assembly, mn units

Year	iPhone Model	Stocking-up at assembly plants
2014	iPhone 6	100
2015	iPhone 6S	80-85
2016	iPhone 7	70-80
2017	iPhone X/8	75-80
2018	iPhoneXS/XR	85-90
2019	iPhone 11	75-80
2020	iPhone 12	80
2021	iPhone 13	85
2022	iPhone 14	85
2023	iPhone 15	80
2024	iPhone 16	85-90

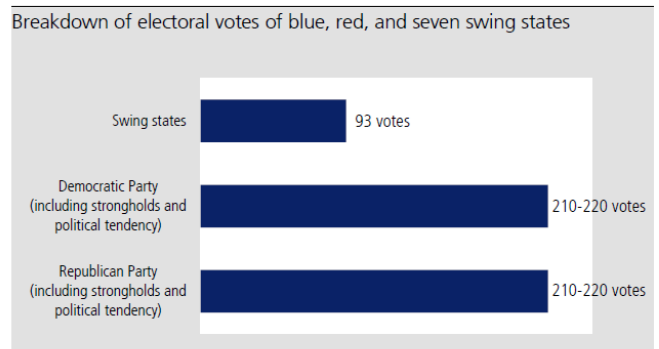
Source: KGI Research

Figure 5: Harris is leading in swing state polling, but the lead is within the margin of error



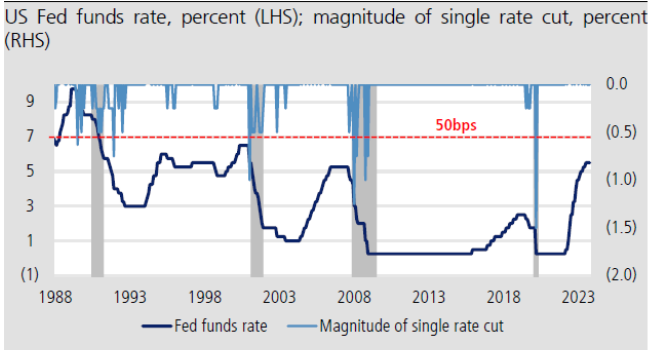
Source: RealClearPolitics; KGI Research

Figure 6: Swing states will determine which party prevails in the US presidential election



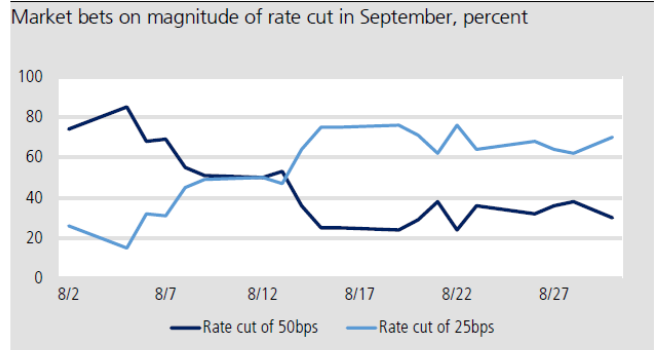
Source: KGI Research

Figure 7: US economy is typically in or on the brink of a recession when the Fed cuts interest rates by at least 50bps



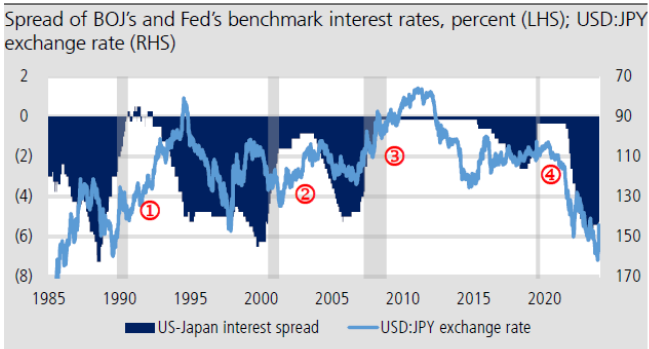
Note: Shaded areas indicate US economic recession
Source: Bloomberg; KGI Research

Figure 8: Odds of a 25bp & 50bp rate cut in September stand at 70% and 30%, respectively



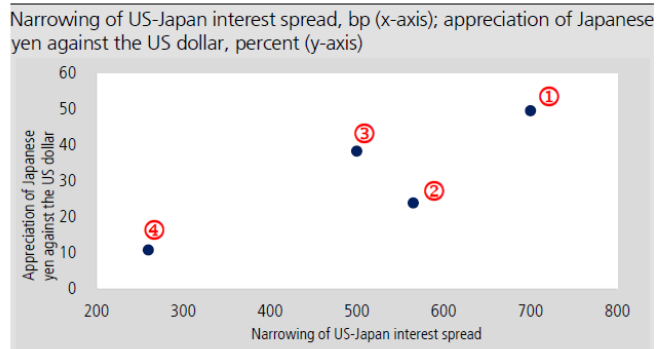
Source: CME; KGI Research

Figure 9: Since the 1980s, the Japanese yen has appreciated markedly on four occasions when the US-Japan interest spread narrowed substantially



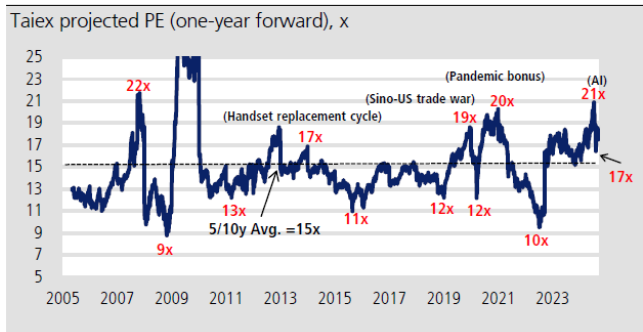
Note: Shaded areas indicate US economic recession
Source: Bloomberg; KGI Research

Figure 10: For every 1ppt, or 100bp, narrowing of the US-Japan interest rate spread, the Japanese yen will appreciate 5-10% against the greenback



Source: Bloomberg; KGI Research

Figure 11: Taix is now valued at 17-18x PE versus long-term average of 15x



Source: TEJ; KGI Research

Figure 12: Taix valuations & corresponding index level

2024-25F average PE (x)	Equivalent index level (point)	25F PE (x)	Equivalent index level (point)
15x	17,779	15x	19,200
16x	18,964	16x	20,480
17x	20,149	17x	21,760
18x	21,334	18x	23,040
19x	22,520	19x	24,320
20x	23,705	20x	25,600
21x	24,890	21x	26,880

Source: TEJ; KGI Research

Figure 13: Valuation comparison

	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
Taix	1.96	2.07	1.92	1.73	1.62	1.62	2.28	0.95	17.50	19.34	16.48	15.15	14.98	17.11	21.73	8.80
Taix excl. TSMC	1.46	1.55	1.43	1.40	1.38	1.46	2.22	0.89	16.65	18.44	16.11	14.81	14.94	16.02	22.71	8.06

Source: KGI Research

Figure 14: 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 (%)		
							2024F	2025F	2024F	2025F	2024F	2025F	2024F	2025F	2023	2024F	2025F
TSMC	2330 TT	Outperform	1290.0	714,416	889.0	45.1	41.67	51.73	21.3	17.2	5.4	4.5	28.1	28.6	1.5	1.8	2.0
Hon Hai	2317 TT	Outperform	265.0	77,218	179.5	47.6	11.25	15.26	16.0	11.8	1.6	1.5	10.2	13.1	3.0	3.3	4.5
Largan	3008 TT	Outperform	3880.0	12,098	2925.0	32.6	185.77	194.02	15.7	15.1	2.1	1.9	14.2	13.5	2.3	3.2	3.3
Compeq Manufact	2313 TT	Outperform	97.0	2,700	73.1	32.7	5.47	6.98	13.4	10.5	2.0	1.8	15.8	18.3	2.1	3.0	3.8
VPEC	2455 TT	Outperform	220.0	779	136.0	61.8	4.15	5.80	32.8	23.4	7.3	6.5	23.6	29.5	1.6	2.6	3.6
MSI	2377 TT	Outperform	212.0	4,516	172.5	22.9	12.46	15.80	13.8	10.9	2.7	2.4	20.2	23.5	3.1	4.4	5.6
Asustek	2357 TT	Outperform	665.0	12,153	528.0	25.9	41.48	41.58	12.7	12.7	1.6	1.5	12.6	12.2	3.2	5.9	5.9
EIH	8069 TT	Outperform	335.0	10,361	292.0	14.7	7.97	11.94	36.6	24.5	6.5	5.9	18.1	25.2	1.5	1.8	2.7
Fositek	6805 TT	Outperform	1000.0	1,504	708.0	41.2	18.96	35.60	37.3	19.9	9.3	7.7	26.6	42.4	0.8	1.4	2.7
E.S.F.H	2884 TT	Outperform	30.0	13,507	27.3	10.1	1.55	1.66	17.6	16.4	1.7	1.6	10.1	10.0	4.0	4.0	4.4
SMP	6121 TT	Outperform	460.0	2,078	362.5	26.9	28.77	32.61	12.6	11.1	1.9	1.8	15.2	16.5	5.6	5.6	6.4
Chicony	2385 TT	Outperform	202.0	3,698	157.0	28.7	13.16	13.79	11.9	11.4	2.7	2.5	23.4	22.5	5.9	5.9	6.2

Source: KGI Research

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