Strategy

Taiex volatility in 2H24F, with rebound at year-end

Key message

1. Taiex to see drastic swings in 2H24F due to mixed market forces.
2. Taiex to consolidate in 3Q24F, before rebounding at year-end; US presidential election is a major risk factor.
3. Investors should look for stocks with bottoming industry momentum, low valuations, high dividends, or government policy support in 3Q24, before focusing on the AI supply chain in 4Q24.

Taiex to see drastic swings in 2H24F due to mixed market forces

While we remain upbeat about the long-term outlook for the Taiex, in light of the AI frenzy, we expect some noticeable market swings in 2H24, because: (1) although expectation of US Fed rate cuts keeps pumping liquidity into the Taiex, we note that sell-off pressure could emerge if rate cuts are postponed again, in the wake of sticky or rising inflation; (2) manufacturers have been rebuilding inventories since late-2023, but end-market demand has been muted, with the exception of AI servers, indicating structural weakness in the ongoing recovery; (3) while the AI frenzy will drive structural earnings growth for AI server suppliers in 2024-25F, we note that stock valuations have risen well above their long-term averages, with PEG ratios of many Taiex AI stocks now at 1.0-1.2x; and (4) the US presidential election will be held in 2H24, and while the ruling party tends to announce favorable policies before voting day, uncertainty of trade policies of the next US president could impact market sentiment.

**Taiex to consolidate in 3Q24F & rebound at year-end; US presidential election is a major risk factor**

We predict that the Taiex will consolidate in 3Q24, before rebounding at year-end, as: (1) PEG ratios of leading Taiex AI suppliers are now 1.0-1.2x, which mean they are overvalued. More investors will choose to engage when PEG is below 1.0x; (2) the Fed's tight monetary policy is taking a toll on the economy, evidenced by lackluster restocking in the manufacturing sector. Meanwhile, the Taiex index has kept hitting record highs, suggesting it has deviated from economic fundamentals; (3) anemic end-market demand and a high base in 2023 will result in much slower earnings growth for Taiex stocks in 2Q-3Q24F, creating downside pressure on the index; and (4) the upcoming US presidential election will determine the direction for the US' long-term trade policy, and we expect many investors to remain on the sidelines before the election result is determined. We estimate the Taiex will peak at 23,000 (20x 2024-25F average EPS) and trough at 20,000 (18x 2024-25F average EPS) in 2H24F. Average PE of the Taiex over the past five years is 15x.

Top picks for 3Q24 are plays that have troughed and have low valuations, as well as high dividends & policy support; engage AI supply chain in 4Q24

The Taiex will consolidate in 3Q24F. We thus suggest investors focus on plays that have troughed and boast low valuations, high dividends, and policy support. Additionally, we recommend investors engage the AI supply chain as 4Q24 approaches, when we expect PEG ratios to retreat to below 1.0x. Generally speaking, PC and smartphone plays troughed then rebounded from end-2023 to early-2024. On the other hand, subsectors, such as networking, traditional servers, e-paper, consumer electronics, automobiles, and bicycles, will begin to trough or rebound in 2Q-3Q24F. Our top picks are stocks under the aforementioned industries with low valuations, high dividends, and policy support.

Our top picks

Our top picks in 3Q24 are Zilltek Technology (6679 TT), Parade Technologies (4966 TT), Silergy (6415 TT), Wistron NeWeb (6285 TT), Merida Industry (9914 TT), Evergreen Aviation Technologies (2645 TT), Bizlink Holding (3665 TT), Langan Precision (3008 TT), E.Sun FHC (2884 TT), CTBC FHC (2891 TT), and Bora Pharmaceuticals (6472 TT). In 4Q24, they are Elite Material (2383 TT), Accton Technology (2345 TT), Delta Electronics (2308 TT), Hon Hai Precision (2317 TT), Asustek (2357 TT), Kaori Heat Treatment (8996 TT), Gold Circuit Electronics (2368 TT), Asia Vital Components (3017 TT), Alchip (3661 TT), Chenbro Micom (8210 TT), and Shinfox Energy (6806 TT), Kuo Toong (8936 TT).

Figure 1: Taiex has largely priced in earnings growth driven by AI frenzy

Source: TEJ; KGI Research
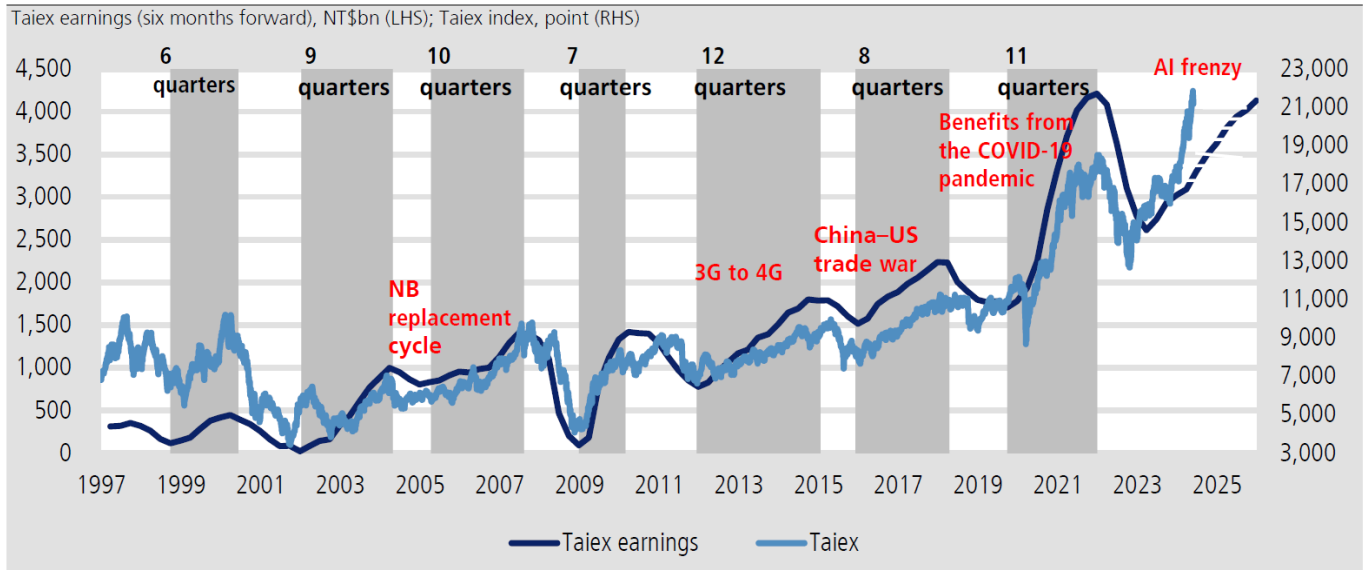
Figure 2: Our top picks

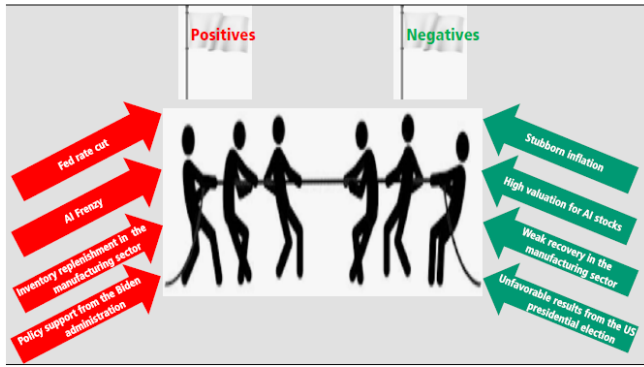|	Company	Code	Investment rating	Target price (NT$)	Mkt cap (US$mn)	Share price (NT$)	Change +/- (%)	EPS (NT$) 2024F	EPS (NT$) 2025F	PE (x) 2024F	PE (x) 2025F	P/B (x) 2024F	P/B (x) 2025F	ROE (%) 2024F	ROE (%) 2025F	Cash yield (%) 2023	Cash yield (%) 2024F	Cash yield (%) 2025F
3Q24 Top picks (low valuations, high dividends & policy support)	Zilltek	6679 TT	Outperform	560.0	701	413.0	35.6	12.16	16.06	34.0	25.7	4.0	3.8	12.2	14.8	1.3	2.5	3.4
	Parade	4966 TT	Outperform	970.0	2,161	862.0	12.5	34.62	44.08	24.9	19.6	3.3	2.9	13.5	15.6	1.5	2.0	2.6
	Silergy	6415 TT	Outperform	480.0	6,030	507.0	(5.3)	5.48	13.61	92.5	37.3	1.5	1.3	6.7	15.1	0.4	0.5	1.2
	WNC	6285 TT	Outperform	158.0	2,475	165.5	(4.5)	10.52	N.A.	15.7	N.A.	2.5	N.A.	16.1	N.A.	3.6	3.9	N.A.
	MIC	9914 TT	Outperform	280.0	2,041	221.0	26.7	8.80	12.71	25.1	17.4	3.1	2.9	12.5	17.0	2.7	2.4	3.5
	EGAT	2645 TT	Outperform	157.0	1,308	113.0	38.9	5.23	5.83	21.6	19.4	3.2	3.2	15.0	16.5	4.0	4.2	4.6
	BHI (Bizlink)	3665 TT	Outperform	402.0	1,672	330.0	21.8	20.82	29.49	15.9	11.2	2.1	1.9	13.6	18.0	2.7	3.8	5.3
	Largan	3008 TT	Outperform	3370.0	10,741	2605.0	29.4	168.55	164.06	15.5	15.9	1.9	1.8	13.0	11.6	2.6	3.2	3.1
	E.S.F.H	2884 TT	Outperform	32.0	14,033	29.0	10.3	1.52	1.64	19.1	17.7	1.7	1.6	9.5	9.2	4.1	3.8	4.1
	CTBC Holding	2891 TT	Outperform	39.0	23,185	38.3	2.0	3.29	3.39	11.6	11.3	1.5	1.3	14.3	12.6	5.0	5.0	5.2
	Bora	6472 TT	Outperform	860.0	2,400	765.0	12.4	43.11	60.23	17.7	12.7	6.7	4.8	58.2	58.5	1.2	1.2	1.2
4Q24 Top picks (AI、Green energy)	EMC	2383 TT	Outperform	590.0	4,866	457.5	29.0	27.41	31.55	16.7	14.5	5.2	4.6	33.0	33.6	3.7	3.7	4.3
	Accton	2345 TT	Outperform	620.0	9,300	537.0	15.5	19.28	22.05	27.9	24.3	10.5	9.1	39.9	40.0	2.4	2.4	2.7
	DELTA	2308 TT	Outperform	490.0	30,212	376.5	30.1	14.21	18.13	26.5	20.8	4.3	3.8	17.4	19.6	1.9	1.9	2.4
	Hon Hai	2317 TT	Outperform	205.0	88,223	206.0	(0.5)	11.38	14.19	18.1	14.5	1.8	1.7	10.3	12.2	2.9	2.9	3.6
	Asustek	2357 TT	Outperform	540.0	11,771	513.0	5.3	31.53	35.91	16.3	14.3	1.5	1.5	9.6	10.6	4.6	4.6	5.3
	Kaori	8996 TT	Outperform	570.0	1,287	464.0	22.8	7.97	16.95	58.2	27.4	14.9	10.5	26.0	45.1	0.9	0.9	1.8
	GCE	2368 TT	Outperform	270.0	3,107	204.5	32.0	12.79	17.21	16.0	11.9	5.5	4.3	37.5	40.6	2.9	2.9	3.9
	AVC	3017 TT	Outperform	800.0	8,455	714.0	12.0	18.91	26.66	37.8	26.8	10.7	8.9	30.4	36.2	1.3	1.3	1.9
	Alchip	3661 TT	Outperform	4600.0	6,360	2600.0	76.9	84.39	99.44	30.8	26.1	8.9	7.5	32.1	30.8	1.6	1.6	1.9
	Chenbro	8210 TT	Outperform	340.0	1,088	292.0	16.4	14.52	18.90	20.1	15.5	5.5	4.7	29.4	32.9	2.6	2.6	3.4
	Shinfox Energy	6806 TT	Outperform	161.0	976	143.0	12.6	6.86	8.96	20.8	16.0	2.0	1.9	11.3	12.3	2.4	2.4	3.1
	KTI	8936 TT	Outperform	114.0	571	74.5	53.0	3.37	5.69	22.1	13.1	3.0	2.7	14.3	22.1	2.4	2.4	4.0

Source: KGI Research

While we remain upbeat about the long-term outlook for the Taiex, in light of the AI frenzy, we expect some noticeable market swings in 2H24.

Mixed forces will lead to drastic swings for Taiex in 2H24F

The Taiex has outperformed most global peers by advancing more than 30% since late-2023. The rally has been driven in part by the ongoing AI frenzy, which we believe will prompt 20-30% YoY earnings growth for Taiex tech stocks in 2024-25F, and by growing risk appetite on the expectation of US Fed rate cuts. Notably, financial stocks have also benefitted from the Taiex rally, with 1Q24 earnings doubling YoY, and we estimate their 2024F earnings will grow by more than 20% from last year.

Looking ahead, while we remain upbeat about the long-term outlook for the Taiex, in light of the AI frenzy, we expect some noticeable market swings in 2H24F, because: (1) although the expectation of US Fed rate cuts keep pumping liquidity into the Taiex, we note that sell-off pressure could erupt if rate cuts are postponed again, in the wake of sticky, or even rising inflation; (2) manufacturers have been rebuilding inventory since late-2023, but end-market demand has been rather muted, with the exception of AI servers, indicating structural weakness in the ongoing recovery; (3) while the AI frenzy will drive structural earnings growth for AI server suppliers in 2024-25F, we note that stock valuations have risen well above their long-term averages, with the PEG ratios of many Taiex AI stocks now standing at 1.0-1.2x; and (4) the US presidential election will be held in 2H24, and while the ruling party tends to announce favorable policies before voting day, uncertainties surrounding the trade policies of the next US president could impact market sentiment.

Stock and bond markets move in the same direction in an environment of high inflation and high interest rates, contrary to the see-saw effect we have seen over the past two decades of low inflation, from 2000-20. Although US inflation has come down from the 2022 peak of 9% to the current 3-4%, it remains above the long-term target level of 2%. As such, we expect stocks and bonds to continue moving in tandem in 2H24F. Since 2022, we have seen stock investors capitulate when US Treasury yields skyrocketed time and time again, and we noticed that overvalued tech and semiconductor stocks were particularly vulnerable to volatility in Treasury yields. Moving forward, while potential Fed rate cuts bode well for market risk appetite, investors shouldn't overlook the risk of stubborn inflation, which could lead to further rate cut delays hurting stock and bond prices.

The long awaited restocking cycle for the global manufacturing sector finally arrived in end-2023, after a strict period of destocking in 2022-23. However, readings of the latest US manufacturing PMI suggest the recovery has been anemic, with the PMI standing above the 50-point watershed in March, before falling below the prosperity line again in April. Our industry surveys show that pull-in demand from non-AI server sectors, namely smartphone, PC, consumer electronics and general server sectors, has been lukewarm, while in the non-tech space, restocking by petrochemicals, steel, cement and industrial automation firms has been extremely limited across the board, as the Chinese economy has been mired in deep difficulties.
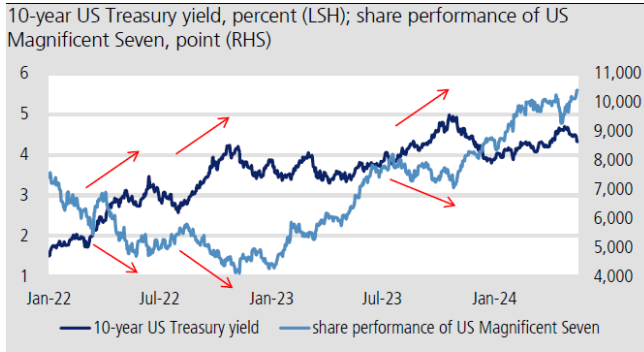
Global tech giants have been aggressive in growing capex, in light of the continued proliferation of generative AI. We estimate AI server shipments will increase nearly by two fold in 2024F, and grow almost 100% YoY in 2025F. While the penetration rate of AI servers will be only 6-10% in 2024-25F, we note that underlying component spec upgrades will create enormous business opportunities for suppliers, who will most likely enjoy substantial earnings growth in 2024-25F. The AI frenzy has prompted global large cloud service providers to not only purchase Nvidia's GPUs, but also invest in chip R&D, consequently benefitting IC design service houses in Taiwan, which are specialized in providing customized ASIC designs. That being said, we note that stocks of Taiwanese IC design service houses are valued at over 40x PE, down slightly from the high of more than 50x earlier this year, but far above their long-term average of 26x. Nvidia's GB200 servers will switch to liquid cooling thermal solutions, likely boosting the content value of thermal components by more than 10x compared to air cooling solutions. Thermal solution suppliers for GB200 servers are set to register 40% earnings growth in 2024F, followed by 40% profit growth in 2025F. In the meantime, these suppliers are valued at 30-40x PE, well above their long-term average of 12x.

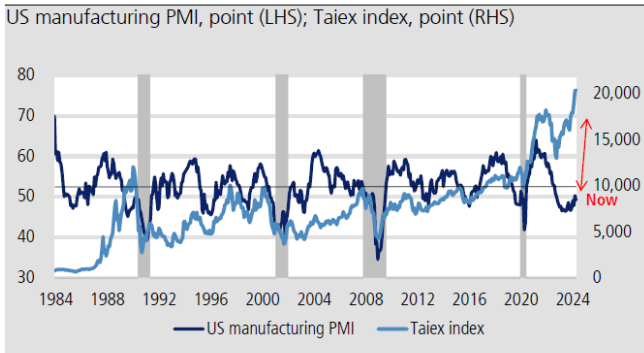**Figure 3: Mixed forces will lead to drastic swings for the Taiex in 2H24F**

Source: KGI Research

Figure 4: Stock & bond markets tend to move in the same direction when inflation is high

Correlation in monthly returns on stocks and bonds, point (LHS); US CPI YoY, percent (RHS)

Source: Bloomberg; KGI Research

Figure 5: Stock performances of the US Magnificent Seven (Apple, Google, Amazon, Microsoft, Meta, Nvidia & Tesla) are sensitive to Treasury yields during high inflation
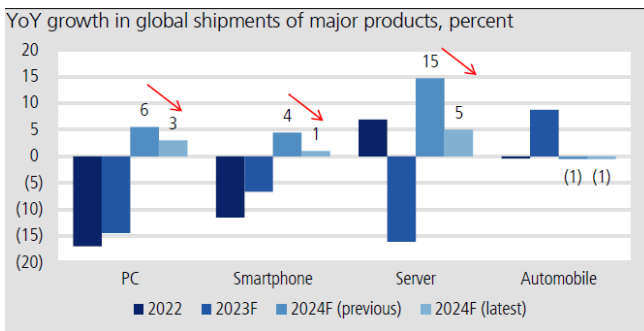
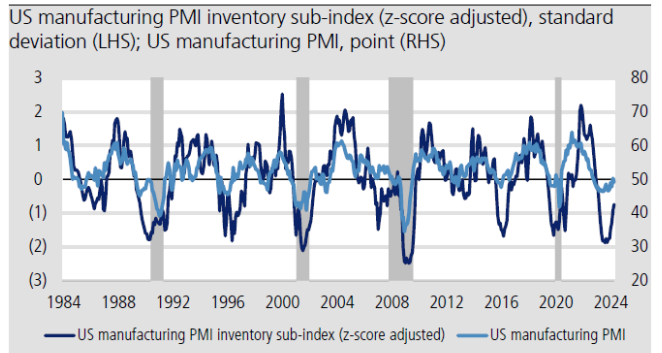10-year US Treasury yield, percent (LSH); share performance of US Magnificent Seven, point (RHS)

Source: Bloomberg; KGI Research

Figure 6: US Treasury yields have been a major swing factor for the Taiex amid high inflation

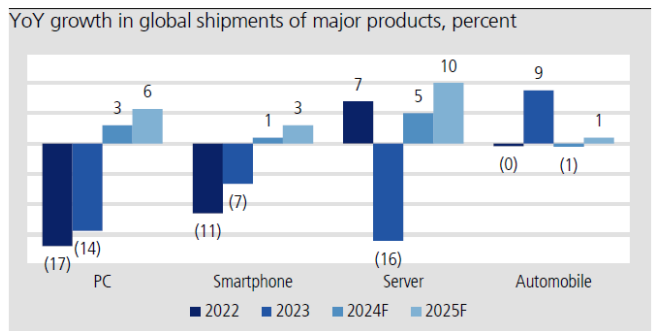10-year US Treasury yield, percent (LSH); Taiex index, point (RHS)

Source: Bloomberg; KGI Research

Figure 7: Recent Taiex rally is much stronger than the ongoing manufacturing recovery

US manufacturing PMI, point (LHS); Taiex index, point (RHS)
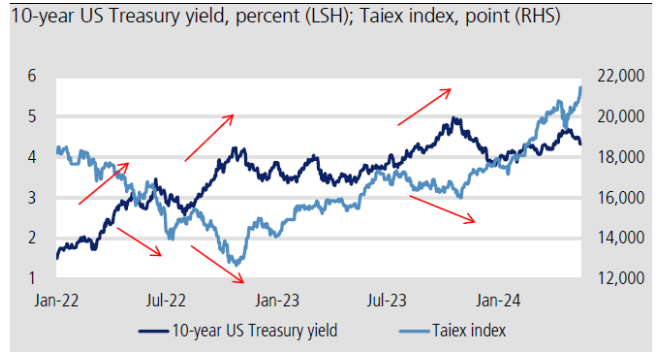
Note: Shaded areas indicate periods of US economic recession
Source: Bloomberg; KGI Research

Figure 8: Current manufacturing recovery has been weak

US manufacturing PMI inventory sub-index (z-score adjusted), standard deviation (LHS); US manufacturing PMI, point (RHS)

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

Figure 9: Demand recovery for PCs, handsets and general servers has been weaker than expected so far in 2024

YoY growth in global shipments of major products, percent

Source: KGI Research

Figure 10: End-market demand recovery to be weak throughout 2024F

YoY growth in global shipments of major products, percent

Source: Bloomberg; KGI Research

Figure 11: AI stock valuations well above their long-term average & broader market

Taiex and tech subsector projected PE (highest, lowest, five-year average, 2024-25 average), x

✕ 5yAvg ■ 2024-25F
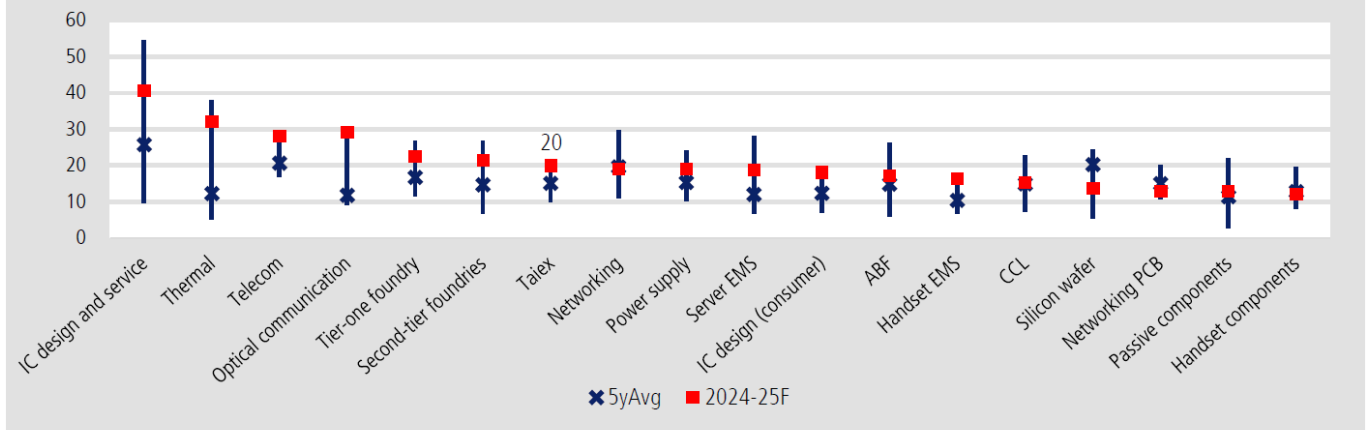
Note: Subsectors are ranked based on their forward looking 2024-25F PE
Source: TEJ; KGI Research

Figure 12: Overview of Taiex & subsector earnings growth

Tech	Earnings growth YoY (%)				Forecast PE (x)		Non-tech	Earnings growth YoY (%)				Forecast PE (x)	
	2022	2023	2024F	2025F	2024F	2025F		2022	2023	2024F	2025F	2024F	2025F
Server EMS	(9.3)	10.2	50.3	26.8	20.8	16.8	Cement	(50.7)	31.4	(9.3)	11.9	19.4	17.3
Thermal	34.5	20.5	38.7	43.8	38.3	26.0	Food	(13.6)	6.8	19.4	11.7	21.2	19.0
Power supply	15.1	4.3	6.2	16.5	20.5	17.6	Petrochemicals	(63.1)	(50.6)	19.6	53.9	44.9	21.5
ABF	102.5	(68.1)	17.1	81.3	22.6	11.9	Apparel	32.1	(11.3)	11.1	12.7	23.2	20.6
Optical communication	-	63.4	34.7	30.1	33.0	25.3	Footwear makers	100.0	(45.2)	26.3	21.6	25.5	20.9
IC design and service	94.8	5.3	41.1	27.0	46.8	34.5	Auto parts	52.8	(24.7)	50.9	(1.1)	14.5	-
Memory	(36.0)	-	-	658.8	106.1	14.0	Industrial automation	5.2	(14.2)	21.2	22.8	26.7	20.5
Networking PCB	56.1	(22.8)	78.3	34.5	14.8	11.0	Bicycle	(12.7)	(44.8)	9.9	42.8	27.8	19.4
Networking	77.3	15.2	18.2	-	18.6	-	Container shipping	19.7	(94.4)	203.6	(68.6)	9.5	58.9
CCL	(7.7)	8.2	71.9	15.1	16.4	14.3	Steel	(75.4)	(89.0)	368.2	169.4	37.4	15.5
Tier-one foundry	70.4	(17.5)	20.5	25.4	23.6	18.9	Tourism	(46.5)	176.4	9.4	11.0	17.0	15.0
Second-tier foundries	51.6	(33.3)	(11.6)	9.6	21.9	20.9	Food	(2.7)	92.7	8.2	17.0	16.2	14.0
Handset components	28.4	(36.7)	29.0	15.0	12.8	12.2	Aerospace	135.4	21.3	24.5	16.4	21.6	16.0
Silicon wafer	29.5	25.1	(18.5)	19.3	16.2	13.6	Airlines	(37.8)	185.5	(2.2)	(38.2)	12.3	21.2
Passive components	(0.8)	(24.7)	18.5	18.5	14.7	12.4	Heavy electrical	(1.9)	42.9	46.6	30.2	35.1	26.6
Telecom	2.6	13.7	(2.4)	9.4	29.1	27.1	Green energy	56.9	80.8	58.5	33.6	17.4	13.7
IC design (handset/consumer electronics)	(2.9)	(32.6)	18.2	12.1	20.2	18.4							
Handset EMS	(2.1)	0.8	10.5	24.1	18.1	14.9							
Cloud digital	16.3	17.1	13.5	19.7	26.1	21.7							

Note: Based on KGI forecasts & consensus
Source: KGI Research

We estimate the Taiex will consolidate in 3Q24, before rebounding at year-end, with peak of 21,500 and trough of 20,000 in 2H24.

Taiex to consolidate in 3Q24F & rebound at year-end; US presidential election is a major risk factor

We predict that the Taiex will consolidate in 3Q24, before rebounding at year-end, as: (1) the PEG ratios of leading Taiex AI suppliers now range between 1.0-1.2x, which means their stocks are overvalued. More investors will choose to engage when PEG is below 1.0x; (2) the Fed's tight monetary policy is taking a toll on the economy, evidenced by lackluster restocking in the manufacturing sector. In the meantime, the Taiex index has kept hitting new highs, suggesting that it has deviated from economic fundamentals; (3) anemic end-market demand and a high base in 2023 will result in much slower earnings growth for Taiex stocks in 2Q-3Q24F, creating downside pressure on the index; and (4) the upcoming US presidential election will determine the direction for the US' long-term trade policy, and we expect many investors will stand on the sidelines before the election result is determined. We estimate the Taiex will peak at 23,000 (20x 2024-25F average EPS) and trough at 20,000 (18x 2024-25F average EPS) in 2H24F. The average PE ratio on the Taiex over the past five years was 15x.

The AI frenzy has boosted supply chain stocks to tremendous highs, and has underpinned excessive surges in earnings. However, according to data from the AI supply chain under our coverage, we see the PEG ratios of most plays is over 1.0x. In general, we consider the share price reasonable when the PEG ratio of a counter is at 1.0x. When PEG is lower than 1.0x, it implies the share price is undervalued. A PEG above 1.0x indicates means the share price has exceeded a fair range. According to our estimate, for plays in the AI-related supply chains, besides server assemblies, the PEG ratios of thermal suppliers, IC design services and chip foundries are at 1.0-1.2x. In addition, the AI supply chain accounts for over 40% of the overall market. Therefore, the Taiex will be weighed on as share prices of the AI supply chain decline towards fair valuations.

Although the US economy is currently heading towards a healthy scenario of a "soft landing" or a "non-landing", with structurally higher interest rates and inflation, a slowdown in growth is an inevitable fact, evidenced by the PMI of the manufacturing and service sectors falling below 50 simultaneously, indicating that the Fed's tightening of monetary policy has begun to weigh on the economy. According to market consensus, the US GDP growth rate (SAAR) will fall below 1.7% in 2H24F, lower than the long-term trend growth rate of 1.8-2.0%. Although the current inventory replacement cycle has started in 4Q23, pull-in demand has not been significant, as year-end inventory digestion was not thorough enough, and most importantly, end-demand has been weak. Our latest assessment points out that the 2024F PC shipment volume will be revised down from the 6% YoY growth forecasted in early-2024 to 3% YoY growth; smartphone shipments cut from 4% YoY growth to 1% YoY growth; and server shipments revised down from 15% YoY growth to 5% YoY growth.

In addition to AI servers, the highlight of technology products in 2H24F will be AI PCs. The market is eagerly anticipating that AI PC launches will initiate a replacement cycle. However, we think that instead of a sudden break out at a certain period, followed by rapid proliferation, AI PCs will proliferate step-by-step, coupled with back-and-forth confirmation. AI PC adoption depends on consumer experience sand technological maturity after launches in 2H24F. Therefore, we think that it will be difficult for AI PC sales to immediately push up the earnings of the supply chain in 2H24F. Based on the fact that only AI servers will see guaranteed end-demand in 2H24F, with related products subject to seasonality, and coupled with a high base in 2023, we predict that the earnings growth of Taiex-listed firms will slow down significantly from 2Q24F to 3Q24F, before speeding up again in 4Q24F.

The US presidential election will be held on November 5. The elected president and vice president will take office on January 20, 2025. Looking back at the long-term data since the 1970s, although the market is bullish throughout the fourth year of a presidential term, the market tends to fluctuate violently two to three months before, and rebound after, presidential elections. The results of this year's presidential election will significantly affect long-term US trade policy, which will affect the stock market.

Figure 13: Current PEG ratios of tech stocks are above 1.0x, implying share prices have exceeded fair valuations
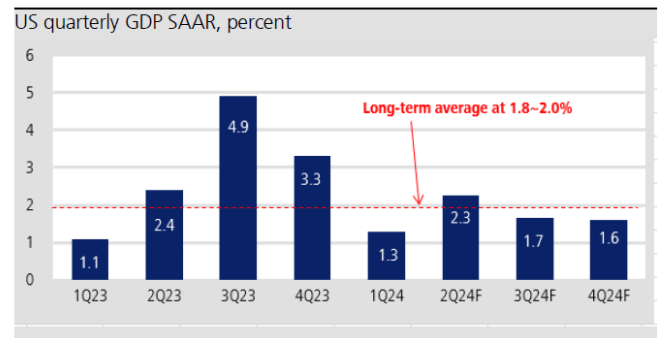
Tech stocks 2021-25 earnings CAGR, percent (X-axis); 2024-25 average forward PE, x (Y-axis)
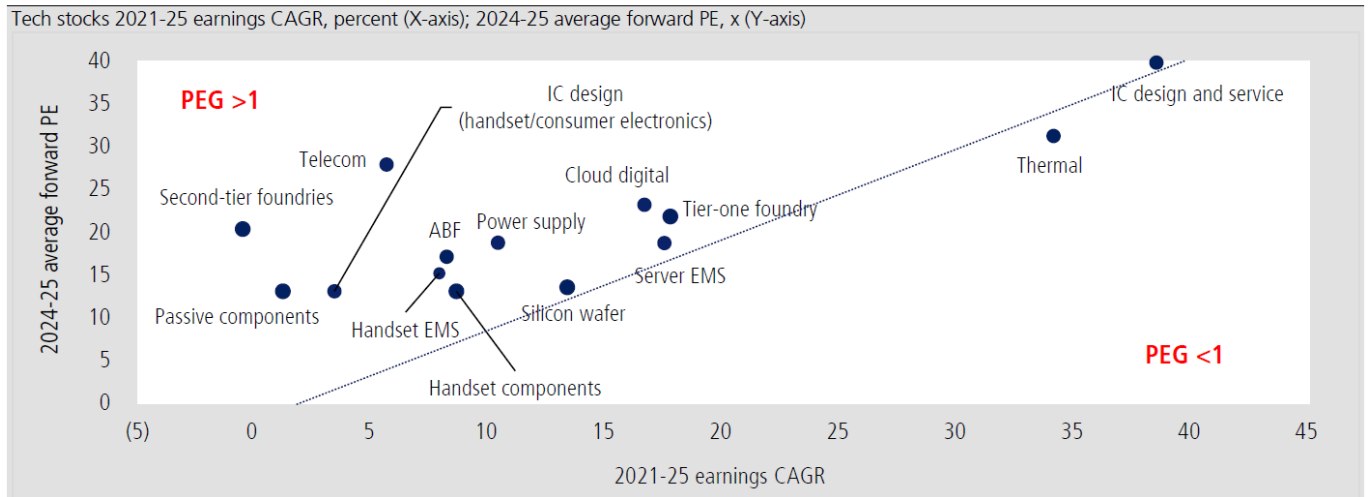
Source: TEJ; KGI Research and KGI estimates

**Figure 14: US manufacturing & service sector PMI both fell below 50 in April**

US manufacturing and service sector PMI index, point
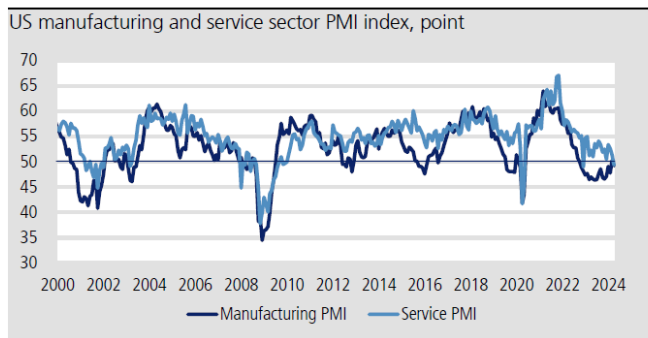
Source: Bloomberg; KGI Research
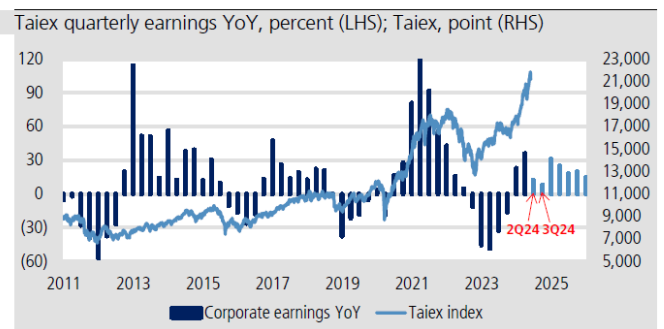
Figure 15: US economic growth to slow in 2H24F

US quarterly GDP SAAR, percent

Source: Bloomberg; KGI Research

Figure 16: Earnings growth of Taiex-listed firms to slow in 2Q-3Q24F

Taiex quarterly earnings YoY, percent
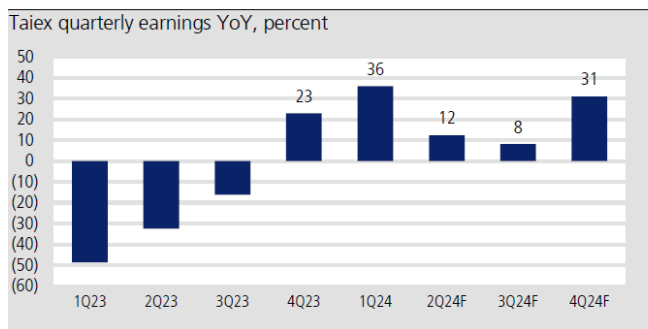
Source: TEJ; KGI Research estimates

Figure 17: Earnings slowdown in 2Q-3Q24F to weigh on Taiex

Taiex quarterly earnings YoY, percent (LHS); Taiex, point (RHS)

Source: TEJ; KGI Research estimates

## Figure 18: Historically, US stocks tend to consolidate two to three months before presidential election

Average rate of return of S&P 500 in first half of year before and after the US presidential election, percent
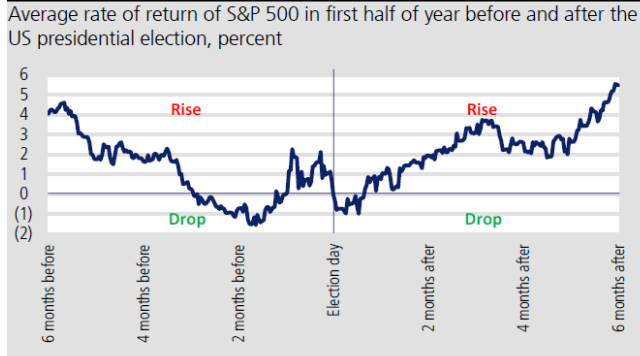
Source: Bloomberg; KGI Research

Figure 19: Scenario analysis of 2024 US presidential election

Possible scenarios	Possible influence	Taiex trend	
Scenerio 1: Donald Trump wins	Promoting tariff war may impact global trade	Slight slump	
Scenario 2: Donald Trump loses but doesn't concede defeat	May cause political unrest or civil war	Excessive plummet	
Scenario 3: Joe Biden wins presidency for a second term	Continue existing trade and military policies	Rally	

Source: Bloomberg; KGI Research

Figure 20: Current Taiex valuation at record high

Taiex forward PE (12-months), x
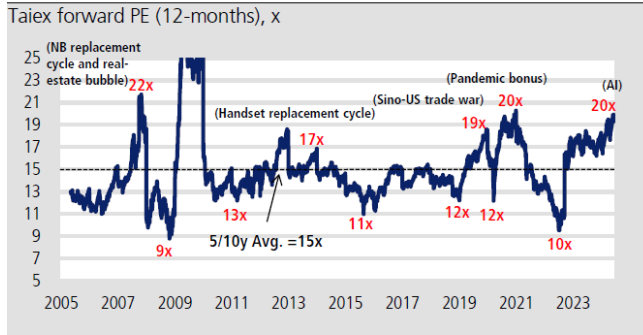
Source: TEJ; KGI Research estimates

Figure 21: Comparison of Taiwan stock valuations & Taiex

2024-25F PE	Equivalent index level (point)	2025F PE	Equivalent index level (point)
15x	17,102	15x	18,611
16X	18,242	16X	19,851
17x	19,382	17x	21,092
18X	20,522	18X	22,333
19X	21,663	19X	23,574
20X	22,803	20X	24,815

Source: TEJ; KGI Research estimates

Figure 22: Comparison of Taiex 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
Taiex	2.17	2.24	2.07	1.72	1.61	1.62	2.28	0.95	20.48	21.65	18.14	15.16	14.98	17.13	21.73	8.80
Taiex excl. TSMC	1.63	1.69	1.56	1.40	1.38	1.46	2.22	0.89	19.36	20.57	17.02	14.83	14.95	16.04	22.71	8.06

Source: TEJ; KGI Research estimates

Figure 23: Taiex to consolidate in 3Q24F, then rebound at end-2024F

2H24 Taiex forecast and positive & negative factors

	1Q24	2Q24	3Q24	4Q24
Index movement	↗	↗ ↘	↗ ↘ ↗ ↘	↘ ↗
Positives	(1) PC and handset demand recovery (2) Manufacturing inventory replenishment since 4Q23 (3) The January Effect and policies supporting a bull run before the presidential election (4) Apple launching new products (5) Dividend payout announcement	(1) Nvidia introduces a new server chip (2) China launches new Android handsets (3) European and US central banks commence interest rate cuts	(1) AI PC production in small quantities (2) The iPhone 16 series drives new product stocking (3) Massive cash dividend payouts (4) Intel introduces the Birch Stream server platform	(1) Market expectations for PC/handset replacement cycle in 2025 (2) AI frenzy likely to drive 20% YoY Taiex earnings growth in 2025 (3) Valuations of the AI supply chain returning to reasonable levels (4) Window-dressing effect
Negatives	(1) Results from the Taiwan presidential election affects cross-strait relations (2) 2023 annual results (3) BOJ ending its negative interest rate policy	(1) Weaker-than-expected PC and handset demand recovery (2) Market delays projected rate cuts on stubborn inflation (3) Moody's updates credit rating for US debt (4) 1Q24 results on May 15	(1) Stretched valuations for the AI supply chain (2) Lackluster sell-through of AI PC due to high prices (3) Monetary tightening policies weigh on economy (4) Taiex earnings decelerate markedly in 2Q-3Q24 (5) Investors stay on sidelines before US presidential election	(1) Market sentiment driven by conclusion of US presidential election (2) 3Q24 corporate results on November 14

Source: KGI Research

The Taiex will consolidate in 3Q24F. We thus suggest investors focus on plays that have troughed, have low valuations, high dividends, and policy support. We recommend engaging the AI supply chain at any pullback.

Our top picks for 3Q24 are plays that have troughed, have low valuations, high dividends, & policy support; engage AI supply chain in 4Q24

The Taiex will consolidate in 3Q24F. We thus suggest investors focus on plays that have troughed, boast low valuations, high dividends, and policy support. Additionally, we recommend investors to engage the AI supply chain as 4Q24 approaches, when we expect PEG ratios will retreat to below 1.0x.
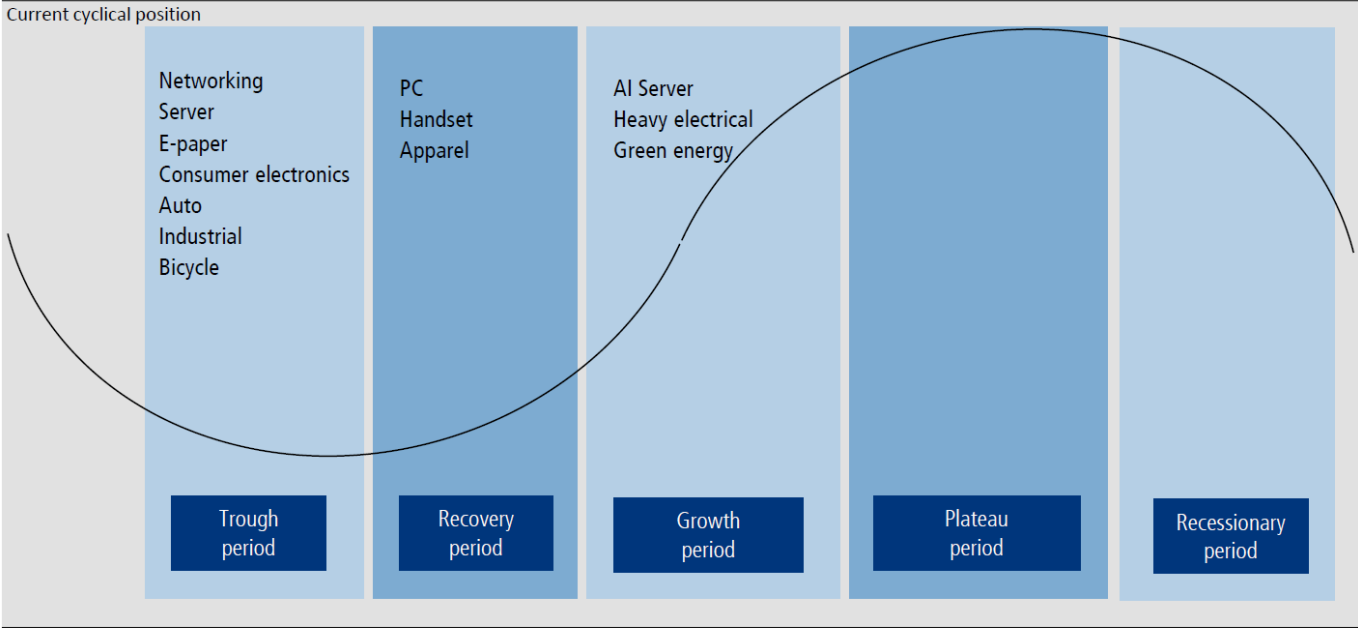
Although a replacement cycle kicked off after a wave of inventory adjustments for the manufacturing sector ended in 4Q23, the period when each subsector troughed and the magnitude of the subsequent recovery have differed. Generally speaking, PCs and smartphones troughed, then rebounded from end-2023 to early-2024. On the other hand, subsectors, such as networking, traditional servers, e-paper, consumer electronics, automobiles, and bicycles will begin to trough or rebound in 2Q-3Q24F. Our top picks are stocks under the aforementioned industries with low valuations, high dividends, and policy support.

In his May 20 inauguration speech, President Lai Ching-te set out his target of developing "Five Trusted Industry Sectors", namely semiconductors, AI, military, security and surveillance, and next-generation communications. He emphasized his intention to build a Taiwan where the "economic sun never sets." He plans to invest aggressively in fields such as quantum computing, robots, the metaverse, precision medicine, and other advanced technologies. In the future, we will continue to keep an eye on favorable policies for related industries being rolled out.

Our top picks

Our top picks in 3Q24 are Zilltek Technology (6679 TT), Parade Technologies (4966 TT), Silergy (6415 TT), Wistron NeWeb (6285 TT), Merida Industry (9914 TT), Evergreen Aviation Technologies (2645 TT), Bizlink Holding (3665 TT), Langan Precision (3008 TT), E.Sun FHC (2884 TT), CTBC FHC (2891 TT), and Bora Pharmaceuticals (6472 TT). In 4Q24, they are Elite Material (2383 TT), Accton Technology (2345 TT), Delta Electronics (2308 TT), Hon Hai Precision (2317 TT), Asustek (2357 TT), Kaori Heat Treatment (8996 TT), Gold Circuit Electronics (2368 TT), Asia Vital Components (3017 TT), Alchip (3661 TT), Chenbro Micom (8210 TT), and Shinfox Energy (6806 TT), Kuo Toong (8936 TT).

Figure 24: Subsectors to rebound from trough in 3Q24F

Current cyclical position

Networking Server E-paper Consumer electronics Auto Industrial Bicycle	PC Handset Apparel	AI Server Heavy electrical Green energy		
Trough period	Recovery period	Growth period	Plateau period	Recessionary period

Source: KGI Research

Figure 25: Potential policy beneficiaries under Lai Ching-te's administration

Economic policy approaches	Key development industries
Five Trusted Industry sectors	Semiconductors, AI, military, security and surveillance, and next-generation communication
Vision of building Taiwan as a country where the "economic sun never sets."	Quantum computing, robotics, the metaverse, precision medicine

Source: KGI Research

Figure 26: Our top picks

	Company	Code	Investment rating	Target price (NT$)	Mkt cap (US$mn)	Share price (NT$)	Change +/- (%)	EPS (NT$) 2024F	EPS (NT$) 2025F	PE (x) 2024F	PE (x) 2025F	P/B (x) 2024F	P/B (x) 2025F	ROE (%) 2024F	ROE (%) 2025F	Cash yield (%) 2023	Cash yield (%) 2024F	Cash yield (%) 2025F
3Q24 Top picks (low valuations, high dividends & policy support)	Zilltek	6679 TT	Outperform	560.0	701	413.0	35.6	12.16	16.06	34.0	25.7	4.0	3.8	12.2	14.8	1.3	2.5	3.4
	Parade	4966 TT	Outperform	970.0	2,161	862.0	12.5	34.62	44.08	24.9	19.6	3.3	2.9	13.5	15.6	1.5	2.0	2.6
	Silergy	6415 TT	Outperform	480.0	6,030	507.0	(5.3)	5.48	13.61	92.5	37.3	1.5	1.3	6.7	15.1	0.4	0.5	1.2
	WNC	6285 TT	Outperform	158.0	2,475	165.5	(4.5)	10.52	N.A.	15.7	N.A.	2.5	N.A.	16.1	N.A.	3.6	3.9	N.A.
	MIC	9914 TT	Outperform	280.0	2,041	221.0	26.7	8.80	12.71	25.1	17.4	3.1	2.9	12.5	17.0	2.7	2.4	3.5
	EGAT	2645 TT	Outperform	157.0	1,308	113.0	38.9	5.23	5.83	21.6	19.4	3.2	3.2	15.0	16.5	4.0	4.2	4.6
	BHI (Bizlink)	3665 TT	Outperform	402.0	1,672	330.0	21.8	20.82	29.49	15.9	11.2	2.1	1.9	13.6	18.0	2.7	3.8	5.3
	Largan	3008 TT	Outperform	3370.0	10,741	2605.0	29.4	168.55	164.06	15.5	15.9	1.9	1.8	13.0	11.6	2.6	3.2	3.1
	E.S.F.H	2884 TT	Outperform	32.0	14,033	29.0	10.3	1.52	1.64	19.1	17.7	1.7	1.6	9.5	9.2	4.1	3.8	4.1
	CTBC Holding	2891 TT	Outperform	39.0	23,185	38.3	2.0	3.29	3.39	11.6	11.3	1.5	1.3	14.3	12.6	5.0	5.0	5.2
	Bora	6472 TT	Outperform	860.0	2,400	765.0	12.4	43.11	60.23	17.7	12.7	6.7	4.8	58.2	58.5	1.2	1.2	1.2
4Q24 Top picks (AI、Green energy)	EMC	2383 TT	Outperform	590.0	4,866	457.5	29.0	27.41	31.55	16.7	14.5	5.2	4.6	33.0	33.6	3.7	3.7	4.3
	Accton	2345 TT	Outperform	620.0	9,300	537.0	15.5	19.28	22.05	27.9	24.3	10.5	9.1	39.9	40.0	2.4	2.4	2.7
	DELTA	2308 TT	Outperform	490.0	30,212	376.5	30.1	14.21	18.13	26.5	20.8	4.3	3.8	17.4	19.6	1.9	1.9	2.4
	Hon Hai	2317 TT	Outperform	205.0	88,223	206.0	(0.5)	11.38	14.19	18.1	14.5	1.8	1.7	10.3	12.2	2.9	2.9	3.6
	Asustek	2357 TT	Outperform	540.0	11,771	513.0	5.3	31.53	35.91	16.3	14.3	1.5	1.5	9.6	10.6	4.6	4.6	5.3
	Kaori	8996 TT	Outperform	570.0	1,287	464.0	22.8	7.97	16.95	58.2	27.4	14.9	10.5	26.0	45.1	0.9	0.9	1.8
	GCE	2368 TT	Outperform	270.0	3,107	204.5	32.0	12.79	17.21	16.0	11.9	5.5	4.3	37.5	40.6	2.9	2.9	3.9
	AVC	3017 TT	Outperform	800.0	8,455	714.0	12.0	18.91	26.66	37.8	26.8	10.7	8.9	30.4	36.2	1.3	1.3	1.9
	Alchip	3661 TT	Outperform	4600.0	6,360	2600.0	76.9	84.39	99.44	30.8	26.1	8.9	7.5	32.1	30.8	1.6	1.6	1.9
	Chenbro	8210 TT	Outperform	340.0	1,088	292.0	16.4	14.52	18.90	20.1	15.5	5.5	4.7	29.4	32.9	2.6	2.6	3.4
	Shinfox Energy	6806 TT	Outperform	161.0	976	143.0	12.6	6.86	8.96	20.8	16.0	2.0	1.9	11.3	12.3	2.4	2.4	3.1
	KTI	8936 TT	Outperform	114.0	571	74.5	53.0	3.37	5.69	22.1	13.1	3.0	2.7	14.3	22.1	2.4	2.4	4.0

Source: KGI Research

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