



AmInvestment Bank

Sector report

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CONSTRUCTION

MRT3 news to buoy trading sentiment

NEUTRAL

(Upgraded)

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Rationale for report: Sector update

Investment Highlights

- We upgrade our weighting for the construction sector to **NEUTRAL** from UNDERWEIGHT following news reports over the weekend, quoting Transport Minister Datuk Seri Dr Wee Ka Siong that the government, in a recent cabinet meeting, decided to go ahead with the MRT3 project. The implementing agency Mass Rapid Transit Corporation has been given three months to update the studies on the project, including its cost and the construction will begin in 2H2021.
- Given a news flow-driven, liquidity-fuelled and risk-on stock market, we believe investors are likely to react positively to the minister's statement. We nonetheless have reservations as follows:
 - The local political landscape remains dynamic, with a strong likelihood of the 15th general election being called immediately after the lifting of the nationwide state of emergency on 1 Aug 2021;
 - Given the government's fiscal constraints, the implementation model of the project may gravitate towards a public-private partnership of which the main contractor may be required to take on certain operating/commercial risk and/or participate in the funding of the project (East Coast Rail Link and Island A of the Penang Transport Master Plan are good examples); and
 - The construction period may be prolonged to lighten the stress on the government's cash flow that means the earnings impact of the MRT3 project on construction companies may not be as significant as compared with the MRT1 and MRT2 (that were fast tracked).
- To reflect the improved trading sentiment towards construction stocks on the back of the latest news, we raise our benchmark forward target PE for large- and mid-cap contractors to 14x from 12x (except for Gamuda to 13x from 11x to reflect its riskier order book with self-funded reclamation works for Island A of the Penang Transport Master Plan) and for small-cap contractors to 9x from 8x.
- As a result, we raise the fair values (FV) of construction stocks under our coverage by 6–17% (Exhibit 1). We upgrade **Sunway Construction** to **HOLD** from UNDERWEIGHT, while maintaining **HOLD** for **Gamuda**, **Hock Seng Lee** and **Kimlun Corp** and **UNDERWEIGHT** for **IJM Corp** and **Econpile**.
- The minister's statement on the MRT3 project aside, the fact remains that the government will have very limited room for fiscal manoeuvre given the elevated national debt, weighed down further by the economic impact of the pandemic (including reduced tax and petroleum revenues), as well as the massive relief spending to cushion the economic impact of the pandemic.
- Operationally, construction players are subject to higher operating cost and lower efficiency (due to restrictions on working hours and worker density on the site, and the additional expenses incurred in upgrading the dormitory for foreign workers in compliance with the Worker' Minimum Standards of Housing and Amenities Act 1990, also known as Act 446) and higher operating risk (due to the potential stop-work order or enhanced movement control order on the dormitory in the event of Covid-19 infection and, shortage of foreign workers as borders remain largely closed).
- Amidst the uncertainty in the rollout of public infrastructure projects locally, a number of players have ventured into or returned to overseas markets. For instance, Sunway Construction in 2020 bagged two highway projects worth more than RM800mil in India on a hybrid annuity model, while Econpile secured a US\$85.7mil (RM347.6mil) piling and substructure works in Phnom Penh, Cambodia. Meanwhile, Gamuda has been shortlisted for three motorway/metro line projects (that require extensive tunnelling works) in Australia.
- We do not have any top pick for the sector. However, for the purpose of anchoring a portfolio, we recommend **Gamuda (HOLD; FV RM3.49)** and **Sunway Construction (HOLD; FV RM1.80)**.

EXHIBIT 1: FV AND VALUATION BASIS CHANGES

	FV (RM)			PE* (x)		
	After	Before	Chg (%)	After	Before	Chg
Gamuda	3.49	3.25	7	13	11	+2
IJM Corp#	1.19	1.12	6	14	12	+2
SunCon	1.80	1.54	17	14	12	+2
Econpile	0.20	0.18	11	9	8	+1
HSL	0.96	0.90	7	9	8	+1
Kimlun	0.91	0.79	15	9	8	+1

*Forward target for construction business

Source: AmlInvestment Bank

EXHIBIT 2: VALUATION MATRIX

	Recomm.	Price (RM)	FV (RM)	Upside (%)	Mkt Cap (RMmil)	FYE	EPS (sen)		EPS growth (%)		P/E (x)		P/B* (x)	ROE* (%)	NDPS* (sen)	Div Yield* (%)
							FY21F	FY22F	FY21F	FY22F	FY21F	FY22F				
Gamuda	HOLD	3.58	3.49	↑ -2.5	8,853.3	Jul	23.0	23.3	9.0	1.3	15.6	15.4	1.0	6.4	0.0	0.0
IJM Corp#	UNDERWEIGHT	1.70	1.19	↑ -30.0	6,163.7	Mar	10.7	11.2	69.8	4.7	15.9	15.2	0.6	3.9	6.0	3.5
SunCon	HOLD ↑	1.81	1.80	↑ -0.6	2,340.1	Dec	10.2	12.5	82.1	22.5	17.7	14.5	3.5	20.1	7.0	3.9
Econpile	UNDERWEIGHT	0.50	0.20	↑ -59.6	662.1	Jun	1.4	2.2	133.3	57.1	35.4	22.5	1.6	4.1	0.5	1.0
HSL	HOLD	0.96	0.96	↑ 0.0	559.4	Dec	11.2	10.7	100.0	-4.5	8.6	9.0	0.6	7.5	1.4	1.5
Kimlun	HOLD	0.85	0.91	↑ 7.7	270.9	Dec	9.9	10.1	135.7	2.0	8.5	8.4	0.4	4.8	3.3	3.9
Weighted Average									46.9	6.8	16.3	15.2	1.2			

*FY21 #FY20F and FY21F refer to FY21F and FY22F

Source: AmlInvestment Bank

EXHIBIT 3: MEGA PROJECTS

Project	Value (RM bil)	Status	
		On-going	Pending
Penang Transport Master Plan	46.0	√	
East Coast Rail Link	44.0	√	
MRT2	30.5	√	
MRT3	22.5		√
LRT3	16.6	√	
Pan Borneo Highway, Sarawak	16.5	√	
Pan Borneo Highway, Sabah	12.8	√	
Coastal Road, Second Trunk Road and 11 mega bridges in Sarawak	11.0	√	
Central Spine Road	10.7	√	
Sarawak-Sabah Link Road	5.2		√
Klang Valley Double Track (Phase 2)	4.5	√	
Rasau water treatment plant	4.5		√
Johor Bahru-Singapore Rapid Transit System (JB-Singapore RTS)	3.2	√	

Source: AmlInvestment Bank, various news reports

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