

Outthink. Outperform.

Policy risks

Tan Sri Muhyiddin Yassin was appointed as the new Prime Minister yesterday and is expected to form a new government under a new ruling coalition Perikatan Nasional with allies such as Gabungan Parti Sarawak (GPS). The sector is susceptible to changes in government policies and delays in public-sector project awards. The previous change in government saw the KLCON Index underperforming the FBM KLCI by 37% over a 1-month period. Maintain our **UNDERWEIGHT** call on the Construction Sector. Top **BUYs** are SunCon, AME and Taliworks. Top **SELLs** are Gamuda and MRCB.

Risk of change in government policies

The elevated political uncertainties arising from the change in government and Prime Minister will continue to dampen sentiment on the Construction Sector. It is uncertain at this point if the open tender system to award public-sector projects practiced by the previous government will continue under the new government. The change in the Minister of Works could further delay the roll out of public-sector projects depending on the level of experience of the new Minister in this area and could lead to possible review of projects. But some construction companies with political links could benefit from the change in government, eg, Gabungan AQRS (BUY) and MRCB (SELL).

More public-sector projects in Johor possibly

As a former Chief Minister of Johor and Member of Parliament for Pagoh, we believe new Prime Minister Tan Sri Muhyiddin Yassin could favour the implementation of projects in Johor to strengthen his voter base. Implementation of some infrastructure projects, such as the Johor Bus Rapid Transit and Johor Bahru-Singapore Rapid Transit System, could accelerate. Potential construction and concession company beneficiaries with operations in Johor include AME Elite Consortium (BUY), YTL Corp (HOLD), Kimlun Corporation (N-R) and Ranhill Utilities (N-R).

Delays in infrastructure projects in Penang possibly

The implementation of the Penang Transport Master Plan (PTMP) could be adversely impacted by the change in government. Some components of the project, such as the Bayan Lepas LRT, relies on federal government-guaranteed bonds to fund the construction. The Penang state government has become an opposition state and infrastructure spending for the state could be cut under the new government. Negative for Gamuda, which leads the SRS Consortium (PTMP Project Delivery Partner), if the project implementation is delayed due to lack of government support funds.

More federal government funding for Sarawak projects possibly

The implementation of Sarawak-based projects could accelerate as Gabungan Parti Sarawak (GPS), which leads the state government, provided crucial support to Muhyiddin to become the new Prime Minister. Hence, there could be additional federal funding support for the development of infrastructure projects in Sarawak ahead of the next state election, which is due to be held by 7 September 2021. Potential beneficiaries are construction and building material suppliers such as Cahya Mata Sarawak (N-R), Sarawak Consolidated Industries (N-R), NAIM Holdings (N-R), Hock Seng Lee (N-R) and KKB Engineering (N-R).

Maintain our **UNDERWEIGHT** sector call

We reiterate our **UNDERWEIGHT** call on the Construction Sector. SunCon remains our top sector BUY given its ability to secure in-house and private-sector projects and its being relatively less reliant on government jobs. Our

Sector Update

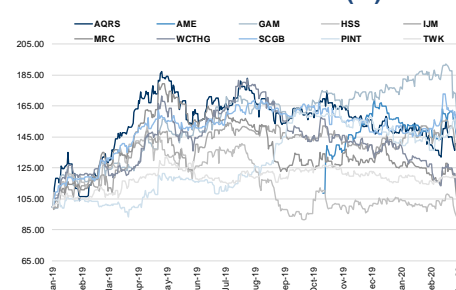
Construction

UNDERWEIGHT (maintain)

Absolute Performance (%)

	1M	3M	12M
AME	-6.8	-13.6	NA
AQRS	-4.7	-13.7	-8.0
Gamuda	-14.2	-10.1	13.4
HSS Eng	-10.8	-11.9	-34.7
IJM Corp	-8.5	-5.8	6.0
MRCB	-14.9	-23.5	-27.4
Pintaras	-15.0	-22.6	-18.7
SunCon	3.3	2.2	6.3
WCT	5.5	-9.1	28.3
Taliworks	-0.6	-6.7	-3.5

Relative Performance to KLCI (%)



Source: Affin Hwang, Bloomberg

Loong Chee Wei, CFA
 (603) 2146 7548
 cheewei.loong@affinhwang.com

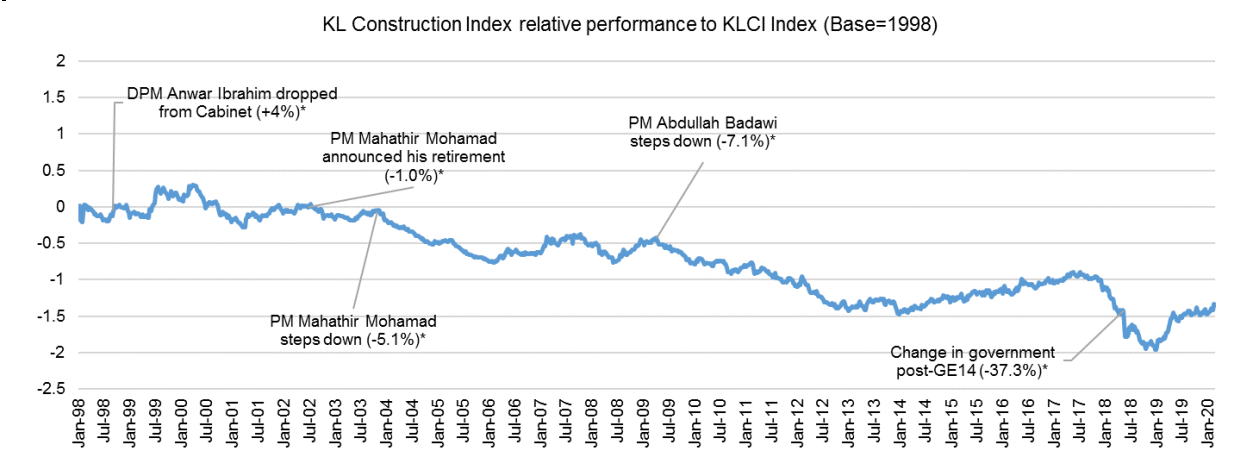
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small-cap top BUYs are AME (industrial properties continue to see good demand) and Taliworks (high dividend yield) among our small-cap top BUYs. Top SELLs are Gamuda and MRCB given uncertainties in winning new contracts.

Construction stocks underperformed previously

We observe that the KL Construction Index (KLCON) typically underperformed the KLCI during previous periods of political uncertainty caused by changes in the Prime Minister or government. The KLCON underperformed the KLCI by 5-7% over a 1-month period after the change in Prime Minister in 2003 and 2009. However, the KLCON underperformed the KLCI more severely, by 37%, following the change in government in 2008. Hence, the degree of underperformance for the KLCON could be as severe as 37% with the change in Prime Minister and the government.

Fig 1: Relative performance of KLCON vs KLCI during previous periods of political uncertainty



* 1-month relative performance of the KLCON vs KLCI post-event in brackets
Source: Affin Hwang, Bloomberg

Risk of further delays in rolling out infrastructure projects

The potential change in leadership or government could lead to further delays in rolling out infrastructure projects. Given the uncertainties, we downgrade the sector to an UNDERWEIGHT from Overweight previously.

Construction peer comparison

Company Name	Stock Code	Rating	Share Pr (RM)	TP (RM)	Mkt Cap (RMb)	Core PE (x)	Core EPS growth (%)	EV/EBI TDA (x)	P/BV (x)	ROE (%)	Div Yield (%)	RNAV/share	Sh Pr discount to RNAV	TP Discount to RNAV				
						CY20E	CY21E	CY20E	CY21E	CY20E	CY20E	CY20E						
LIM CORP	LIM MK	HOLD	1.94	2.02	7.0	21.6	18.6	4.9	16.4	9.8	0.6	3.0	3.1	2.75	29.5	0		
GAMJDA	GAM MK	SELL	3.31	3.00	8.3	13.1	13.6	(7.6)	(3.6)	9.9	1.1	7.4	3.6	4.34	23.7	0		
MRCB	MRC MK	SELL	0.57	0.53	2.5	79.9	81.9	(191.9)	(2.5)	32.8	0.5	0.7	3.1	0.97	41.2	40		
WCT	WCTHG MK	HOLD	0.65	0.71	0.9	9.9	7.8	(24.6)	24.8	11.8	0.3	2.7	2.6	1.92	66.1	50		
SUNWAY CONSTRUCTION	SCGB MK	BUY	1.87	2.20	2.4	16.2	15.3	12.0	5.9	8.9	3.6	22.3	4.3	4.8	2.45	23.7	10	
AME ELITE	AME MK	BUY	1.65	2.28	0.7	11.1	10.0	20.8	10.8	6.7	1.1	9.6	1.8	3.24	49.1	30		
GABUNGAN AQRS	AQRS MK	BUY	1.01	1.16	0.5	10.0	8.6	46.4	16.9	9.2	1.5	9.4	4.0	2.02	50.0	30		
PINTARAS	PINT MK	BUY	2.90	4.04	0.5	8.3	8.1	18.9	1.6	4.3	1.4	16.3	6.9	NA	NA	NA		
TALMWORKS	TWK MK	BUY	0.83	1.18	1.7	18.6	24.2	81.1	(23.2)	13.0	1.7	9.1	8.0	1.30	36.2	10		
HSS ENGINEERING	HSS MK	HOLD	0.71	0.73	0.3	20.6	18.8	>100	9.6	10.2	1.5	7.4	0.0	NA	NA	NA		
Average						24.9	16.5	15.8	7.5	3.9	10.7	1.3	5.0	3.7	3.8	2.37	39.9	21

Source: Bloomberg, Affin Hwang forecasts

Note: Pricing as of close on 28 February 2020

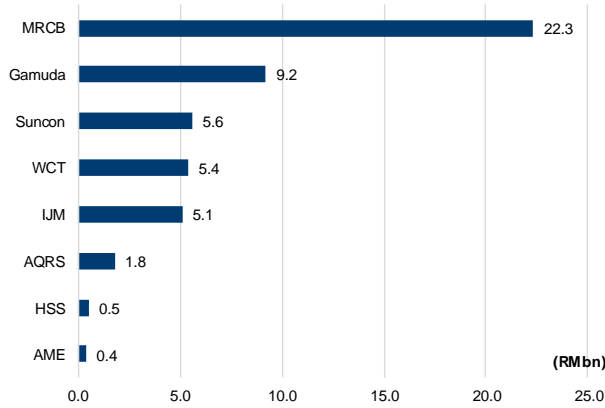
Key risks

Key upside risks to our negative view on the sector are (1) no change in government and leadership, easing political uncertainties; (2) acceleration in the award of government projects; and (3) major infrastructure projects are revived.

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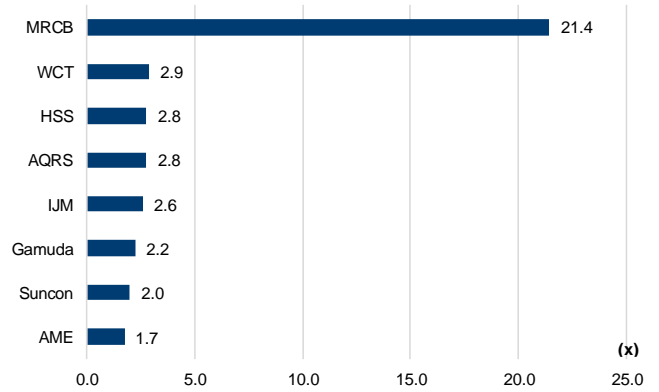
Key focus charts

Fig 2: Construction order book at end-3Q19



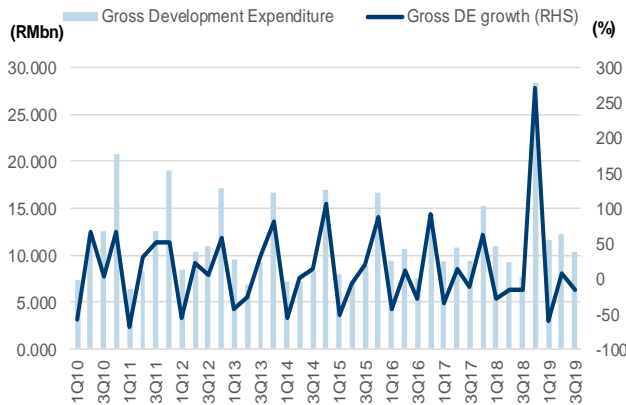
Source: Company, Affin Hwang estimates

Fig 3: Order book/revenue at end-3Q19



Source: Company, Affin Hwang estimates

Fig 4: Government gross development expenditure



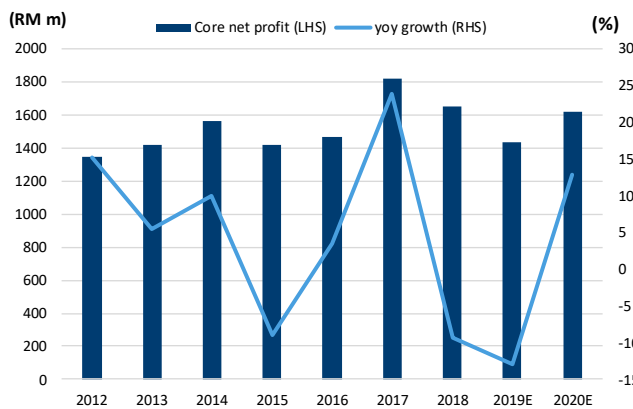
Source: Ministry of Finance

Fig 5: Infrastructure works to be awarded in 2019 onwards

Project	Estimated cost (RMbn)
Penang Transport Master Plan (PTMP)	32
Bandar Malaysia infrastructure	21
Klang Valley MRT Line 3 - Circle Line (MRT3)	21
KL-Singapore High Speed Rail - Fast Train	20
Pan Borneo Highway Sabah (PBH)	13
East Coast Rail Link subcontracts	8
Sarawak Water Grid Phase 1	8
Sarawak Coastal Highway	5
Sarawak Second Trunk Road	6
Labuan Bridge	4
Johor Bahru-Singapore Rapid Transit System	3
Others	10
Total	146

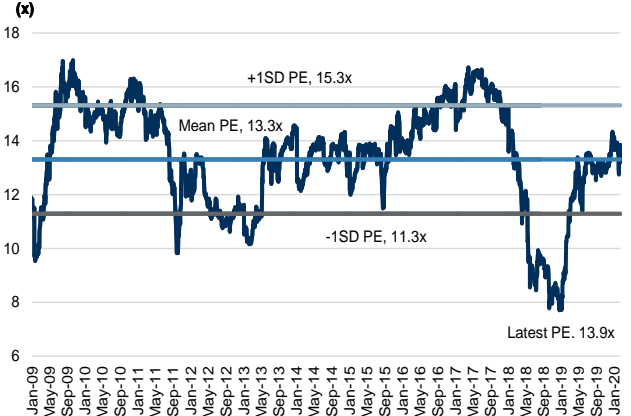
Source: Affin Hwang estimates, various media, eg, The Star and The Edge Financial Daily

Fig 6: Aggregate construction core net profit and yoy change



Source: Companies, Affin Hwang forecasts

Fig 7: KL Construction Index 12-month forward PER



Source: Bloomberg, Affin Hwang forecasts

Important Disclosures and Disclaimer

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +10% over a 12-month period
HOLD	Total return is expected to be between -5% and +10% over a 12-month period
SELL	Total return is expected to be below -5% over a 12-month period
NOT RATED	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.

OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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Affin Hwang Investment Bank Berhad (14389-U)
A Participating Organisation of Bursa Malaysia Securities Berhad

22nd Floor, Menara Boustead,
69, Jalan Raja Chulan,
50200 Kuala Lumpur, Malaysia.

T : + 603 2146 7544/7481/7487
F : + 603 2146 7630
research@affinhwang.com

www.affinhwang.com