

24 June 2024

Construction

The Best is Yet to Come

By Teh Kian Yeong | tehy@kenanga.com.my

OVERWEIGHT



We maintain our OVERWEIGHT rating on the construction sector on the back of the roll-out of mega public infrastructure projects led by the MRT3. We believe the government now has more fiscal space to do so, having got the ball rolling on fuel subsidy rationalisation with the removal of diesel fuel subsidy from 10 Jun 2024. Meanwhile, the private-sector construction market will stay vibrant underpinned by massive investment in new data centres and semiconductor foundries. Our top sector pick is GAMUDA (OP; TP: RM7.29).

More public projects to get off the ground following fuel subsidy rationalisation. Despite the YTD outperformance (driven largely by the award of the RM10b Mutiara Line of the Penang LRT and various data centre building jobs), we remain upbeat as we believe the best is yet to come, i.e. the roll-out of mega public infrastructure projects led by the MRT3 (RM45b). We believe the government now has more fiscal space to do so, having got the ball rolling on fuel subsidy rationalisation with the removal of diesel fuel subsidy from 10 Jun 2024.

A galore of data centre building jobs. The sector has enjoyed a strong flow of private-sector jobs, especially data centre building jobs. **GAMUDA** secured RM1.74b data centre job in Elmina Business Park, Selangor in May 2024, while **SUNCON (OP; TP: RM4.28)** clinched a RM748m data centre job in Cyberjaya in Mar 2024 and an extra RM1.5b data centre job for Yellowwood in Johor in Jun 2024. We believe there will be more with Microsoft embarking on its data centre project in Johor, having committed to USD2.2b (RM10.3b) investment in cloud computing & AI services in Malaysia. Similarly, Google has committed to invest USD2b in developing its first data centre and cloud region in Malaysia. Meanwhile, **TM (OP; TP: RM7.53)** has teamed up with SingTel to build a 64MW data centre in Johor with the first phase expected to be operational by CY26. On the other hand, **TENAGA (OP; TP: RM14.50)** has inked Electricity Supply Agreements (ESA) with ten data centre developers with a total electricity requirement of 2,000MW. Two of them with a total electricity demand of 535MW were completed in 1QFY24. Over the longer term, the national utility company guided for a total electricity demand of 5,000MW from new data centres by CY35.

Plenty of road jobs in East Malaysia. Meanwhile, in East Malaysia, Pan Borneo Highway Sarawak Phase 2 and the Phase 1B of the Pan Borneo Highway Sabah are ready to get off the ground while Sabah-Sarawak Link Road is under construction. **KIMLUN (OP; TP: RM1.76)** has expressed interest to bid for work packages from Pan Borneo Highway Sarawak Phase 2 given that it is already in the market with its involvement in Sarawak-Sabah Link Road. We understand **IJM (MP; TP: RM3.00)** has also shown interest in the market.

Margin recovery. Meanwhile, the industry is poised for margin recovery as newly-secured contracts reflected cost inflation. In addition, post the pandemic, it has become increasingly common for contracts to carry price escalation clauses to safeguard the margins of contactors. As such, we expect industry margins to improve further from here as older contracts with low margins tail off and new contracts with normalised and higher margins start to contribute.

We now value large-cap builders at 20x forward PER. The expansion in our benchmark multiple is premised upon the improved prospects for the roll-out of mega public infrastructure projects following the fuel subsidy rationalisation. We now value large-cap contractors, i.e. **GAMUDA**, **IJM** and **SUNCON** at 20x (from 18x) forward PER, and mid-cap and small-cap players **KERJAYA (OP; TP: RM2.16)** at 16x (from 14x), **WCT (OP; TP: RM0.88)** and **KIMLUN** at 12x (from 10x). Hence, we raise our TP for **GAMUDA** to RM7.29 from RM6.70; **IJM** to RM3.00 from RM2.77; **SUNCON** to RM4.28 from RM3.85; **KERJAYA** to RM2.16 from RM1.90; and **KIMLUN** to RM1.76 from RM1.47. We have already upgraded **WCT's** TP to RM0.88 on 21 Jun 2024. Consequently, we upgrade **KERJAYA** and **KIMLUN** to **OUTPERFORM** from **MARKET PERFORM** and downgrade **IJM** to **MARKET PERFORM** and **OUTPERFORM**, while maintaining our **OUTPERFORM** calls for **GAMUDA**, **SUNCON** and **WCT**.

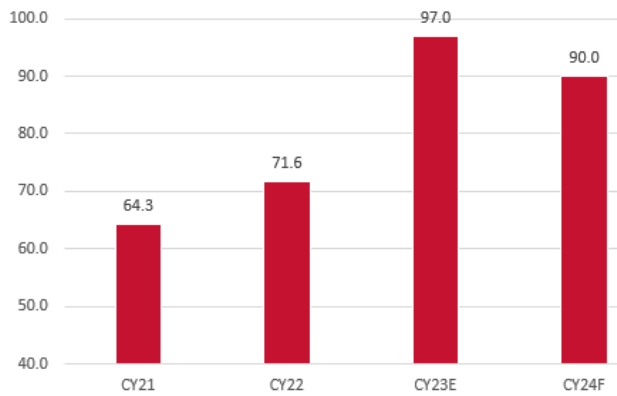
We maintain our sector rating at **OVERWEIGHT** and our sector top pick is **GAMUDA** for: (i) being in the driver's seat for the Mutiara Line of the Penang LRT and front-runner for the tunnelling job for the MRT3, (ii) its ability to secure new jobs in overseas markets, (iii) its strong war chest after the disposal of its toll highways, (iv) its strong earnings visibility underpinned by a record outstanding order book of RM25.8b, and (v) its inroads into the renewable energy space.

Changes to Valuation Basis, TPs and Ratings

	PER* (x)			TP (RM)			Rating		
	Before	After	Chg	Old	New	Chg	Old	New	Chg
GAMUDA	18	20	↑	6.70	7.29	↑	OP	OP	↔
IJM	18	20	↑	2.77	3.00	↑	OP	MP	↓
KERJAYA	14	16	↑	1.90	2.16	↑	MP	OP	↑
KIMLUN	10	12	↑	1.47	1.76	↑	MP	OP	↑
SUNCON	18	20	↑	3.85	4.28	↑	OP	OP	↔
WCT	10	12	↑	0.66	0.88	↑	OP	OP	↔

* for construction business
Source: Kenanga Research

Gross Development Expenditure (RM b)



Source: Budget 2024, Kenanga Research

Penang Bayan Lepas LRT

Station	Nearby Landmark
1	Komtar
2	Modallium
3	Bandar Sri Pinang
4	Sky Club
5	East Jelutong
6	The Light
7	Gelugor
8	USM
9	Batu Uban
10	Pesta
11	Sungai Nibang
12	Bukit Jambul
13	SPICE
14	Jalan Tengah
15	FR North
16	FR South
17	Sungai Tiram
18	Penang Airport
19	Pematang Damar Laut
20	Stn A1
21	Stn A2
22	Stn A3
23	Stn A4

Petunjuk / Legend

- Stesen / Station
- Stesen Pertukaran / Interchange Station
- Depot / Depot
- P Kemudahan Park & Ride / Park & Ride Facility

Jarak (km) / Length (km) 26.8

Bilangan Stesen / Number of Stations 23



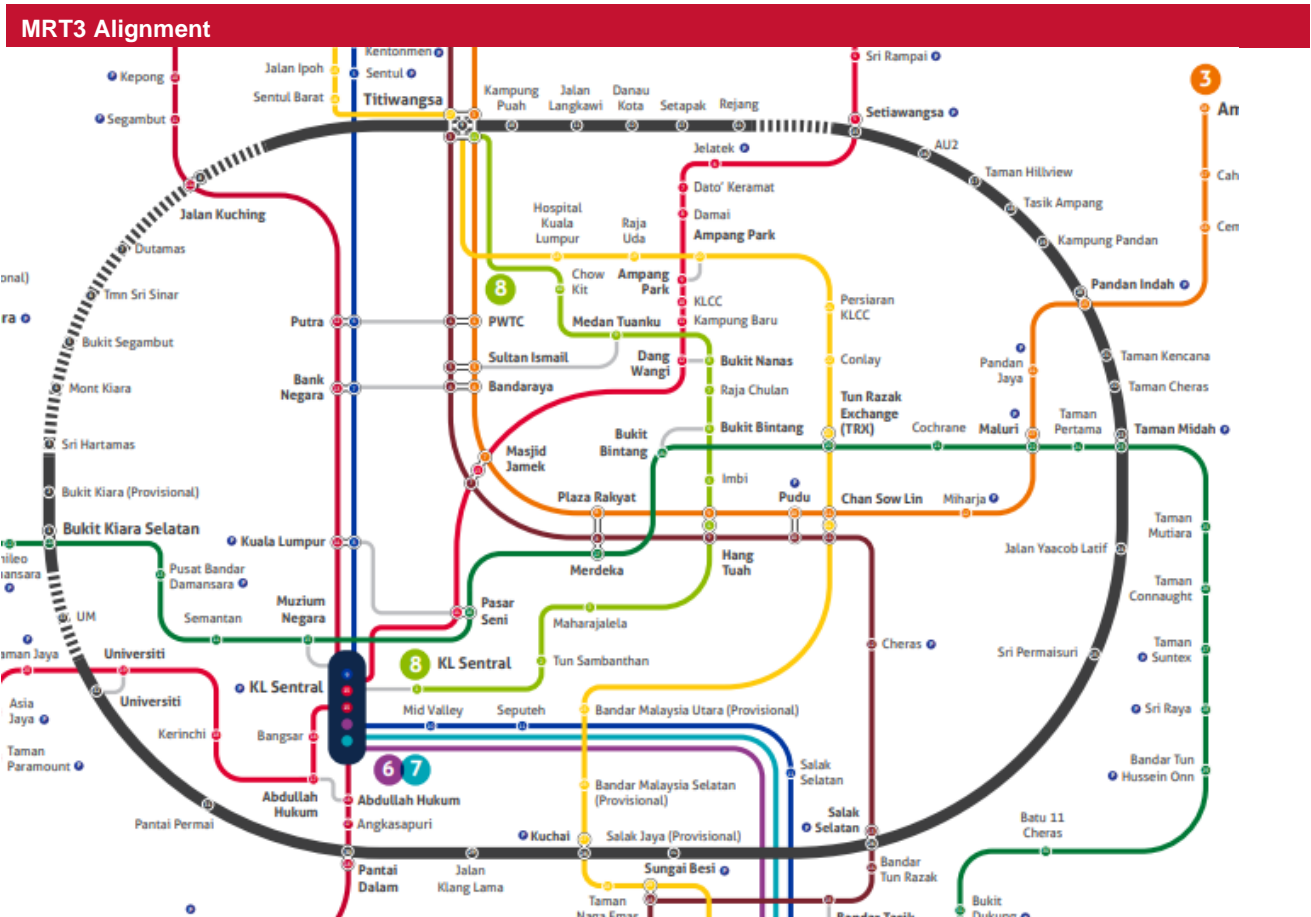
Source: Penang Infrastructure Corporation

KL-Singapore HRS



Source: MyHSR Corp

24 June 2024



Source: MRT Corp

Projects	Value (RM b)	Status	
		Ongoing	Pending
Penang Transport Masterplan	46.0		✓
MRT3	45.0		✓
Mutiara Line, Penang LRT	10.0		✓
Penang Airport Expansion	1.5		✓
Subang Airport Redevelopment Plan	3.7		✓
KL-SG HSR	N/A		✓
Johor Bahru-Singapore RTS	4.3	✓	
Central Spine Road	10.7	✓	
Pan Borneo Sarawak Phase 1	16.0	✓	
Pan Borneo Sarawak Phase 2	4.6		✓
Pan Borneo Sabah Phase 1	15.3	✓	
Pan Borneo Sabah Phase 1B	15.7		✓
Sabah Sarawak Link Road Phase 1	5.2	✓	
Sabah Sarawak Link Road Phase 2	7.2		✓
Large-scale flood mitigation projects	13.0		✓
Rasau Water Treatment Plant	4.5	✓	
Johor Bahru ART	NA		✓
Kuching Autonomous Rail Transit	6.0	✓	
Large-scale Flood Mitigation Projects	13.0		✓

Source: Kenanga Research, Media reports

24 June 2024

Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside	Market Cap (RM m)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE	Net Div. (sen)	Net Div Yld
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
Stocks Under Coverage																	
GAMUDA	OP	6.38	7.29	14.3%	17,677.0	Y	07/2024	40.2	50.6	29.7%	25.8%	17.5	14.1	1.5	10.0%	12.0	1.9%
IJM	MP	3.00	3.00	0.0%	10,518.5	Y	03/2025	13.0	14.4	-8.3%	11.2%	32.9	35.2	1.1	4.8%	8.0	2.7%
KERJAYA	OP	1.84	2.16	17.4%	2,320.3	Y	12/2024	14.2	15.8	33.3%	11.3%	15.1	13.2	1.6	13.0%	10.0	5.4%
KIMLUN	OP	1.28	1.76	37.5%	452.3	Y	12/2024	11.9	14.7	493.0%	23.0%	12.9	11.0	0.6	5.5%	1.0	0.8%
SUNCON	OP	3.80	4.28	12.6%	4,899.6	Y	12/2024	14.0	20.4	19.4%	45.7%	29.9	28.6	4.9	19.1%	6.0	1.6%
WCT	OP	0.825	0.880	6.7%	1,169.2	Y	12/2024	2.9	4.4	-83.8%	50.0%	32.7	22.4	0.4	1.4%	0.5	0.6%
Sector Aggregate					37,036.9					43.6%	23.3%	18.3	14.8	1.3	7.3%		2.2%

Source: Kenanga Research

This section is intentionally left blank

24 June 2024

Stock Ratings are defined as follows:**Stock Recommendations**

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

This document has been prepared for general circulation based on information obtained from sources believed to be reliable but we do not make any representations as to its accuracy or completeness. Any recommendation contained in this document does not have regard to the specific investment objectives, financial situation and the particular needs of any specific person who may read this document. This document is for the information of addressees only and is not to be taken in substitution for the exercise of judgement by addressees. Kenanga Investment Bank Berhad accepts no liability whatsoever for any direct or consequential loss arising from any use of this document or any solicitations of an offer to buy or sell any securities. Kenanga Investment Bank Berhad and its associates, their directors, and/or employees may have positions in, and may effect transactions in securities mentioned herein from time to time in the open market or otherwise, and may receive brokerage fees or act as principal or agent in dealings with respect to these companies. Kenanga Investment Bank Berhad being a full-service investment bank offers investment banking products and services and acts as issuer and liquidity provider with respect to a security that may also fall under its research coverage.

Published by:

KENANGA INVESTMENT BANK BERHAD (15678-H)

Level 17, Kenanga Tower, 237, Jalan Tun Razak, 50400 Kuala Lumpur, Malaysia
Telephone: (603) 2172 0880 Website: www.kenanga.com.my E-mail: research@kenanga.com.my