

### SECTOR UPDATE

## Construction – Malaysia

Mixed 1H23 Results; All Eyes On Budget 2024

The sector delivered mixed 1H23 results with sector earnings moderating by 1.0% qoq despite higher revenue. We anticipate stronger 2H23 earnings on higher progress billing amid an easing of the labour shortage and lower building material prices. Companies are expected to ride on the fresh rollout of mega projects (such as MRT3) and a more vibrant Johor property market. Maintain MARKET WEIGHT. Our top picks are Gamuda, Gabungan AQRS and Kerjaya Prospek Group.

### WHAT'S NEW

- Mixed bag of 2Q23 results.** 2Q23 earnings were mixed as three companies' results came in within expectations vs three that came in below, and one that exceeded expectations. Sector earnings moderated by 1.0% qoq to RM382.0m despite a 10.0% increase in revenue to RM5.3b, weighed down by elevated building materials prices. Notably, Gamuda posted an exceptional 3QFY23 (FYE 31 July) earnings on higher contributions from Australia projects which partially made up for the weaker performances by IJM and WCT.

### 2023 RESULTS SUMMARY

Company	Revenue (RMm)	CNP (RMm)	vs. UOBKH	vs. consensus	Earnings Revision		
					+1YR Fwd	+2YR Fwd	+3YR Fwd
Gabungan AQRS	71.0	7.2	In line	In line	-	-	-
Gamuda*	2,067.1	223.4	In line	In line	-	-	-
IJM Corp**	1,225.8	66.4	Below	Below	-2%	-3%	-2%
Kerjaya Prospek Group	309.3	29.9	Below	Below	-4%	-10%	-2%
Malaysian Resources Corp	599.3	10.9	In line	Above	-	-	-
Sunway Construction Group	604.1	32.3	In line	In line	-	+18%	+6%
WCT Holdings	424.5	11.9	Below	Below	-7%	-3%	-3%

FYE July, based on 3QFY23 results; \*\*FYE Mar, based on 1QFY24 results; Source: Companies, UOB Kay Hian

- Anticipate better 2H23 earnings; to ride on the rollout of mega projects and a more vibrant Johor property market.** We continue to anticipate stronger 2H23 earnings on the back of higher progress billing amid an easing of the labour shortage and decline in building material prices. In addition, the upcoming rollout of mega projects such as MRT3 and Penang LRT may further catalyse near-term earnings. For companies with exposure in property development operations, progressive new project launches would also help spur earnings momentum. We also think IJM Corp, WCT, and Gabungan AQRS may ride on the more vibrant property market in Johor given their existing landbanks in the state's prime areas such as Iskandar Puteri and Johor Bahru.

### ACTION

- Maintain MARKET WEIGHT on the sector.** Our neutral sector rating is premised on a lack of visibility on the details regarding the rollout of mega projects amid fiscal constraints, despite a more stable domestic political landscape. Our top pick for the sector remains Gamuda, backed by its robust orderbook with pronounced overseas jobs secured which help to mitigate the muted local contract flows. We derive a higher target price of RM5.14/share for Gamuda, upon rolling forward our valuation base year to FY24 and revising upward FY23-25 earnings to reflect a stronger orderbook. We also like Gabungan AQRS and Kerjaya Prospek Group for their superior orderbook cover ratio and stronger property development earnings from upcoming project launches.

### PEER COMPARISON

Company	Ticker	Rec	Price @ 11 Sep 23 (RM)	Target Price (RM)	Market Cap (RMm)	P/E 2024F (x)	P/B 2024F (x)	Yield 2024F (%)
Gabungan AQRS	AQRS MK	BUY	0.37	0.48	199	3.3	0.4	n/a
Gamuda	GAM MK	BUY	4.34	5.14	11,701	13.1	1.1	2.8
IJM Corporation	IJM MK	HOLD	1.78	1.62	6,493	19.3	0.7	3.1
Kerjaya Prospek Group	KPG MK	BUY	1.20	1.54	1,521	10.9	1.2	4.6
Malaysian Resources Corp	MRC MK	HOLD	0.44	0.41	1,966	17.6	0.4	2.3
Sunway Construction Group	SCGB MK	HOLD	1.86	1.69	2,405	15.8	2.8	3.8
WCT Holdings	WCTHG MK	BUY	0.51	0.69	723	7.7	0.2	3.3

Source: UOB Kay Hian

## MARKET WEIGHT

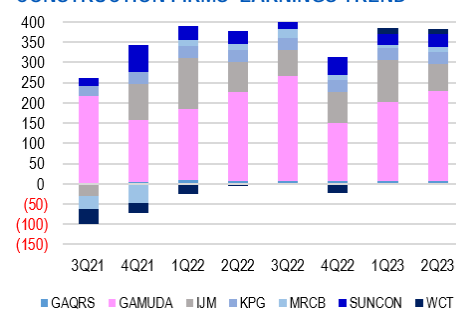
(Maintained)

### SECTOR BUYS

Company	TP(RM)	Upside(%)
Gabungan AQRS	0.48	31.5
Gamuda	5.14	18.4
Kerjaya Prospek Group	1.54	28.3
WCT Holdings	0.69	35.3

Source: UOB Kay Hian

### CONSTRUCTION FIRMS' EARNINGS TREND



Source: Companies, UOB Kay Hian

### OUTSTANDING ORDERBOOK AS OF AUG 23

Company	Value (RMb)	Orderbook cover (x)
Gabungan AQRS	0.9	2.7
Gamuda	21.5	4.2
IJM Corporation	4.9	1.1
Kerjaya Prospek Group	4.5	4.0
Sunway Construction Group	5.8	2.7
WCT Holdings	3.1	1.5

Source: UOB Kay Hian

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ESSENTIALS

• **Most companies met orderbook replenishment targets.** In 2Q23, most companies remained on track to meet their projected orderbook replenishment. In particular, Gamuda maintained its lead with RM10.5b (including the immediate addition of RM4.5b orderbook from the acquisition of DT Infrastructure) worth of new jobs secured as of end-3QFY23. This means the company will be able to comfortably meet its guided average annual orderbook replenishment target of RM12b-13b for FY23-FY24, while a subsequent pick-up in domestic job flows would further strengthen its already-sturdy position.

Meanwhile, Sunway Construction Group and Kerjaya Prospek Group also recorded commendable replenishment of RM1.6b and RM1.1b respectively as of end-Aug 23, underpinned by a resilient mix of external and internal job flows. While other companies had secured fewer new projects in 2023, we understand that they still hold a rather upbeat outlook on the back of a potentially strong influx of infrastructure jobs such as MRT3 and ECRL. This is despite a lukewarm outlook from the private sector owing to the long-lasting property overhang environment.

• **Budget 2024 to provide further clarity on the rollout of mega projects.** We also believe that the upcoming Budget 2024 (which is tentatively scheduled to be on 13 October) may inject fresh stimulus to the construction sector. While the budget may likely entail higher development expenditure (DE) to pump prime the domestic economy, we reckon that a large portion of the DE is earmarked for small-to-medium projects which could hardly benefit listed contractors. That said, we think Budget 2024 may provide further execution details (project costs and implementation timelines) for mega projects such as MRT3.

• **MRT3 to be concluded soon.** Recall that there are three packages under MRT3: a) Civil Main Contractor 301 (CMC301) for the elevated portion with estimated costs of RM2b, b) CMC302 for other elevated portions coupled with additional tunnelling jobs with estimated costs of RM12b, and c) CMC303 - tunnelling jobs worth around RM11b. For CMC301, MRCB is said to have put the lowest bid, while YTL and Gamuda are the lowest bidders for CMC302 and CMC303 respectively. Besides proposed project costs, MRT Corp is also assessing tenders based on technical, commercial and track record aspects. The tender outcome is expected to be concluded later this month, following the three-month extension of tender validity to end-Sep 23.

In addition, we note that there is a confluence of other sizeable infrastructure projects being highlighted in the mid-term review of 12<sup>th</sup> Malaysia Plan including: a) Penang LRT (estimated project costs of RM9.5b), b) remaining packages of Pan Borneo Highway Sabah and Sarawak-Sabah Link Road II, c) expansion of airports in Penang and Subang, d) upgrades and expansions of highways, as well as e) multiple flood mitigation projects worth RM22b. We believe this suggests a high likelihood of these projects being carried out eventually albeit with limited visibility on project timelines.

• **Stabilising building materials prices.** Meanwhile, the continued easing of building materials prices should bode well for construction companies and lead to margin improvements in the upcoming quarters. We note that steel bar prices eased by 7.8% qoq to RM2,765/tonne in 2Q23 and have further declined by 2.8% to RM2,640/tonne as of end-Aug 23. Meanwhile, prices for bulk cement also declined by 4.6% qoq to RM372/tonne in 2Q23 despite rising by 2.2% to RM380/tonne as of end-Aug 23 (still lower than RM390/tonne in 1Q23). This bolsters our anticipations of better 2H23 earnings for construction firms on profit margin improvements, not to mention a ramp-up of construction progress amid gradual easing of labour shortage issues.

MEGA PROJECTS PIPELINE

Project	Value (RMB)	Remarks
ECRL	50	Status: Around 49% completion in 1Q23 with expected completion in Dec 26. Potential beneficiaries: IJM Corp (for vertical package: Econpile, Suncon (for horizontal package).
MRT3	30	Status: Approved in Budget 2023; jobs to be awarded in 2023. Potential beneficiaries: Contractors with rail expertise; Gamuda and MMC (underground section); Suncon, IJM, WCT, GAQRS, MRCB, YTL, HSSE
Pan Borneo Highway Sabah	4	Status: Cabinet approval in 2022 to proceed with the remaining 19 work packages (five years) under Phase 1B. Phase 1 was 82% done as of Aug 23. Potential beneficiaries: Suria Capital (JV with GAQRS), WCT
Rapid Transit System (RTS)	4	Status: 41% completion as of Jul 23; Aims to hit 70% by end-23; Expected completion: Dec 2026 Ekovest won RM2b EPC contract. Potential beneficiaries: Subcontractor works for rail-related contractors such as Suncon, IJM Corp
High Speed Rail (HSR)	TBC	Status: In preliminary stages with MyHSR recently hosted RFI exercise in Jul 23 and may submit proposal to Singapore government in coming months. Potential beneficiaries: Contractors with rail expertise; Gamuda and MMC (underground section); Suncon, IJM, WCT, GAQRS, MRCB, YTL, HSSE

Source: Media reports, UOB Kay Hian

MRT3 PROJECT DETAILS

Project owner	MRT Corp
Project period	2023-30 (8 years)
Project structure	a) 2 contractors for elevated works b) 1 contractor for underground works c) 1 contractor for integrated rail system d) 1 project management consultant
Estimated cost	RM30-50b
Funding structure	Sukuk issuances and other hybrid funds; every work package will have its own PFI
Length of alignment	51km: 40km of elevated tracks & 11km of underground tunnels
No. of stations	31 including 10 interchange stations

Source: Media reports, UOB Kay Hian

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