Equity Beat
midf RESEARCH

21 January 2015

Budget 2015 (Revision)

"We are not in a crisis"

BROAD MEASURES

The Government is taking pre-emptive measures following the changes in the external global economic landscape particularly in relation to (i) the slumping crude oil prices, as well as (ii) the relative weakness of the Ringgit against US Dollar. This is imperative in order to ensure that the nation's economy attains a reasonable growth within the revised target range of 4.5-5.5% this year. Some of the key broad measures announced by Prime Minister Najib Razak are as follow:

Trade. Frontload implementation of Logistics & Trade Facilitation by improving last-mile connectivity to Port Klang and establish a hub and spoke system for air transport. To boost exports of goods and services by actively promoting import-substitution services such as shipping, port, education and professional services.

Utilities. No increase in both electricity tariff and in the scheduled gas price hike for the industrial sector this year.

Construction. Local contractors [registered with the Construction Industry Development Board (CIDB) - Class G1 (Class F), G2 (Class E) and G3 (Class D)] will be given priority in project tenders and will be given the task of carrying out repair works on flood-hit areas.

Retail. Extend the period and increase the frequency of mega sales nationwide.

Tourism. Intensify domestic tourism promotions by offering competitive airfares. Grant waiver of visa fee for inbound tourists from, among others, China to help boost tourism industry.

Domestic Investment. Encourage GLCs and GLICs to invest domestically.

Financing. Bank Negara Malaysia will establish a RM500 million Special Relief Facility for SME loan financing at a concessionary rate of 2.25% with a grace period of up to 6 months through banking and development financial institutions.

SECTORAL IMPACTS

We do not expect wide ranging sectorial boosts to emanate from the above key broad measures. Nonetheless, as we had earlier on expecting a sizable cut to the Development Expenditure, hence the decision to maintain and spend the budgeted amount of RM48.5 billion for 2015 is in itself positive news, particularly to the construction sector.

Construction

We are rather surprised that the Government retains the RM48.5b allocation for Development Expenditure. Having said that, we are positive on the Government's stance to continue to commit with the initial measures tabled in October last year. The measures proposed are better targeted on priority infrastructure projects, specifically the mega rail-lines and highways projects. As these projects have big multiplier effect, it does make sense that the Government should carry on with these projects in order to reinvigorate economic growth. Besides the urban public transport infrastructure projects, the Government also reaffirm its commitment on the implementation of RM40.0b Kuala Lumpur-Singapore High-Speed Rail and RM60.0b RAPID Pengerang projects as well as people-centric projects such as public housing, flood mitigation, water supply and electricity.

With that, we believe the selling panic on the construction stocks should be over after having seen their share prices plummeted in the not too distant past. This is in view that the Government's decision to go ahead with its plans should remove the significant risk of deferment in the implementation of mega projects. As a result, public listed construction companies' orderbook replenishment may remain intact and thus, propel earnings visibility for the next few years.

Budget 2015 infrastructure projects	Estimated Value
Rail-lines	
1. KVMRT Line 2	RM23.0b
2. LRT 3	RM9.0b
3. Upgrading the East Coast railway line	RM150.0m
Roads and Highways	
1. 1,663-km Pan-Borneo Highway	RM27.0b
2. 276-km West Coast Expressway	RM5.0b
3. 59-km Sungai Besi-Ulu Klang Expressway	RM5.3b
4. 47-km Damansara-Shah Alam Expressway	RM4.2b
5. 36-km Eastern Klang Valley Expressway	RM1.6b
6. 635-km of rural roads	RM943.0m

Even though there is still a timing issue related to the roll-out of several pending mega projects, we advocate investors to look at this as a strategic opportunity to accumulate construction stocks at current levels before the contracts are awarded. Some of these construction stocks have yet to reflect their earnings prospect. Among the major potential beneficiaries, we particularly like Gamuda (TP: RM5.28), IJM Corp (TP: RM7.33), Muhibbah Engineering (RM2.74), Hock Seng Lee (TP: RM2.14), MRCB (TP: RM2.59), relisting of Sunway Construction (non-rated), Cahya Mata Sarawak (non-rated), Mitrajaya (non-rated), Gadang (non-rated), TRC Synergy (non-rated) and AZRB (non-rated).

We understand that the latest estimate of damage to infrastructure by the recent East Coast floods came in at approximately RM2.9b. Pursuant to this, the Government will undertake proactive measures to redevelop infrastructure of affected states, including Kelantan, Terengganu, Pahang, Kedah and Perak. Nonetheless, we believe the reconstruction works would benefit small local contractors as the Government has given priority to local class G1, G2 and G3 contractors registered with CIDB to undertake that works in their respective flood affected areas. These categories of contractors are able bid for the contracts worth between RM200k and RM1.0m.

Among the measures that have been taken and will be implemented to assist flood victims include:

Measures	Estimated Value
1. Rehabilitation works and welfare programmes	RM500.0m
2. Repair and reconstruction of basic infrastructure such as schools, hospitals, roads and bridges	RM800.0m
3. Flood mitigation projects	RM893.0m
4. Build 8-ft stilt houses	N.A.

Overall, we remain POSITIVE on the construction sector on the back of aforesaid mega projects. Apart from projects abovementioned, we believe the sector will continue to excite investors with timely progress update on other large-scale projects such as the RM26b Tun Razak Exchange, RM5b PNB Warisan Merdeka Tower, RM6b Penang Third link projects and Penang Integrated Transport. Our top pick for the sector is Gamuda (TP: RM5.28) while in the small-cap space, Protasco (TP: RM2.45).

Cement

In line with our POSITIVE view on the construction sector, we expect the demand for cement to continue to be supported by on-going projects in the last two years and potential lock-in of cement sales for forthcoming projects. Thus, we do not see any setback from the budget revision announced yesterday.

Moreover, postponement of the scheduled electricity tariff hike this year should be a positive to the cement players. Recall that Lafarge Malaysia' 9MFY14 performance dropped -20%yoy to RM206.1m following the hike in electricity tariff by an average of about 14.89% in January 2014. The decision to postpone the tariff hike would at least provide a cushion to cement players this year to offset volatile cement sale. As competition has been intense, sale of cement by companies will continue to be flattish.

For the flood recovery effort, we opine it would only benefit cement players who can offer lower cement selling price for the low-cost housing programme. Hence, the earnings prospect of cement players is expected to continue to register modest growth. We reiterate our NEUTRAL recommendation for both the sector and Lafarge Malaysia with an unchanged TP of RM9.82.

Consumer

Among the initiatives to enhance private consumption are:

1. Intensification of promotions for "Buy Malaysia" products,
2. Higher frequency and longer shopping hours of nationwide mega sales,
3. Promotion of domestic tourism through competitive domestic air fares,
4. Leverage benefits from ASEAN Economic Community, and
5. Waving of visa for tourists, particularly from China.

Potential beneficiaries include Parkson, Padini and AEON. There will be a boost in discretionary spending due potentially higher concentration of tourist arrivals and relatively higher propensity to consume. This will help to mitigate the expected slowdown in consumer consumption in the build up to GST implementation.

Oil & Gas

Making reference to Prime Minister Najib Razak's speech on the revision of Budget 2015, the government has used a baseline average Dated Brent crude oil price for 2015 of USD55pb. In our previous strategy reports, we were initially estimating crude oil to average at around USD75-80pb. However, in light of recent events that have caused further downside weakness to the global crude oil market, we are revising our 2015 average Dated Brent crude oil estimates to USD60-70pb. Our estimation is guided by both the asset breakeven price of global supply and also the fiscal breakeven price of major OPEC producers.

Our estimation is not based on any particular trend line because at this juncture, trend lines are not reflective and meaningful due to the erratic price movements of the past few months. Even if the trend line were to fit our model, the line will still be upwards sloping as oil price had stayed at levels above USD100pb for over the past three years. As such, our new estimation of USD60-70pb could possibly the new equilibrium level at which oil price could hover in due course.

Utility (Power)

Government is set to postpone the scheduled electricity tariff hike in 2015. In our view, this is a continuity of the earlier announcement in November 2014 that the Government had decided that the current electricity tariff is set to stay until June 2015. We are not surprise with the Government decision to let the current tariff structure to stay. In addition, we are of a NEUTRAL view on the impact of this announcement on the power sector as the input cost has gone down in line with the fall of crude oil prices. We believe that the current input cost imputed in the current tariff structure would be sufficient to cover the operation of the power sector over the next six months. We also believe that any potential downside risk arises from the increment in the input cost would be supported by utilising the savings generated from PPA savings which has a balance of approximately RM170m.

Aviation

We view the government's decision to waive visa entry fees for inbound tourists, particularly those from China, as positive for the aviation sector as it may help to revive the interest of Chinese travellers towards Malaysia. This would primarily benefit airport operator, MAHB, which could see higher spending at its retail outlets as well as increase in PSCs contribution. We also believe this could help AAX and AirAsia, through the FlyThru program, as about 40% of AAX's passenger volumes flow to the latter.

Furthermore, the reduction in fuel pump prices which is expected to boost disposable income by RM7.5b is also positive for the aviation sector. This should be able to help mitigate the impact from the GST imposition effective from Apr 2015, and possibly negating any potential weakness in travel demand.

We are NEUTRAL on MAHB (TP: RM7.53) and AAX (TP: RM0.69). We have a BUY call on AirAsia (TP: RM3.70) which is also our top pick for the sector.

Automotive

There was no announcement on the implementation of the ELV program during the PM's Budget review speech and thus our outlook for the automotive sector remains largely unchanged. However, the government's lower GDP forecast range for 2015 of 4.5-5.5% may potentially imply downside risk to our 2015 TIV target of 670k units. As a result, we may consider trimming our TIV target for 2015.

MARKET OUTLOOK

The Budget review speech clearly state the revised key budget assumptions and parameters with regard to (i) crude oil prices with average Dated Brent of USD55 per barrel, (ii) GDP output growth range of between 4.5-5.5% (from 5.0-6.0%), and (iii) fiscal deficit target at 3.2% (from 3.0%) of GDP for 2015. The announcements are positive as the key budget assumptions and parameters are now more realistic and attainable. Furthermore, the decision to "reprioritising [operating] expenditure" to the tune of RM 5.5 billion, in lieu of taking an easier way by axing the development budget, with the aim of helping to reduce the fiscal deficit is commendable. In addition, assurances on the status of the country's external position this year will help to allay market's lingering fears against the possibility of it turning into a twin deficit situation. We maintain our FBM KLCI baseline 2015 year-end target at 1,900 points, with the upper and lower bounds at 1,950 points and 1,850 points respectively. The year-end target equates to PER of circa 16.4x or +¾ standard deviation (SD) over its long-term mean (since 2006 to present).

MIDF RESEARCH is part of MIDF Amanah Investment Bank Berhad (23878 - X).
(Bank Pelaburan)
(A Participating Organisation of Bursa Malaysia Securities Berhad)

DISCLOSURES AND DISCLAIMER

This report has been prepared by MIDF AMANAH INVESTMENT BANK BERHAD (23878-X). It is for distribution only under such circumstances as may be permitted by applicable law.

Readers should be fully aware that this report is for information purposes only. The opinions contained in this report are based on information obtained or derived from sources that we believe are reliable. MIDF AMANAH INVESTMENT BANK BERHAD makes no representation or warranty, expressed or implied, as to the accuracy, completeness or reliability of the information contained therein and it should not be relied upon as such.

This report is not, and should not be construed as, an offer to buy or sell any securities or other financial instruments. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. All opinions and estimates are subject to change without notice. The research analysts will initiate, update and cease coverage solely at the discretion of MIDF AMANAH INVESTMENT BANK BERHAD.

The directors, employees and representatives of MIDF AMANAH INVESTMENT BANK BERHAD may have interest in any of the securities mentioned and may benefit from the information herein. Members of the MIDF Group and their affiliates may provide services to any company and affiliates of such companies whose securities are mentioned herein This document may not be reproduced, distributed or published in any form or for any purpose.

MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS	
STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >15% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >15% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -15% and +15% over the next 12 months.
SELL	Total return is expected to be <-15% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >15% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.
SECTOR RECOMMENDATIONS	
POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.