midf RESEARCH

SPECIAL REPORT | Strategy

13 March 2019

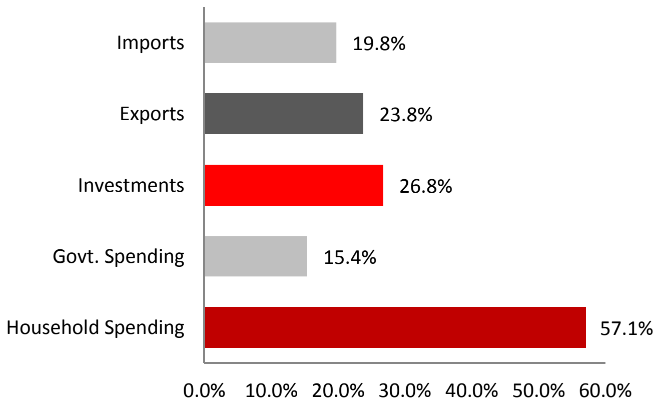
Assessing Turkey's Recession Impact on Malaysia

- **Turkey slides into recession as Lira remains is bad shape**
- **Overall minimal yet cautious impact to the Malaysia economy**
- **Expect MAHB and IHH to be unscathed back by strong operational numbers**
- **TNB to see minimal risk after having fully impaired its carrying value in Gama**

Macroeconomic Analysis

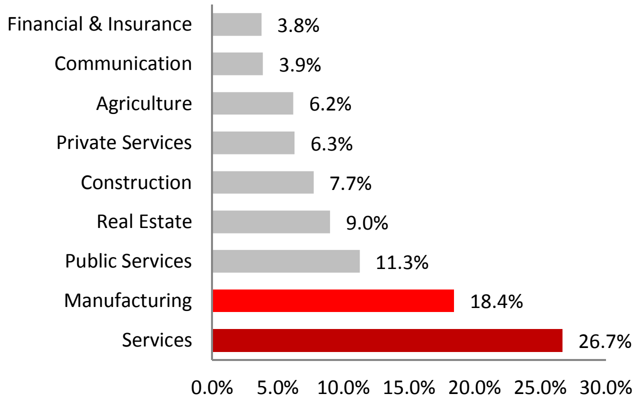
Turkey slides into recession. On annual basis, Turkey's GDP shrank -3%yoy, lowest in 9-quarter. The economy contracted twice in 3Q18 and 4Q18, confirming the technical recession condition. The main dragging factors were household spending and investments, -8.9%yoy and -12.9%yoy respectively in 4Q18. Both components constitute about 57.1% and 26.8% of the economic activities. The contractions among others due to depreciation of Lira, decline optimism among business & consumer and increase in jobless rate. Turkey's unemployment rate touched 12.3% in Nov-18, highest since Feb-17. Moving forward, we view the economy will slowly improve especially with support from external demand as trade war tension recedes, modest pick-up in commodity prices and steady recovery in Lira.

Chart 1: GDP Share by Expenditure (%)



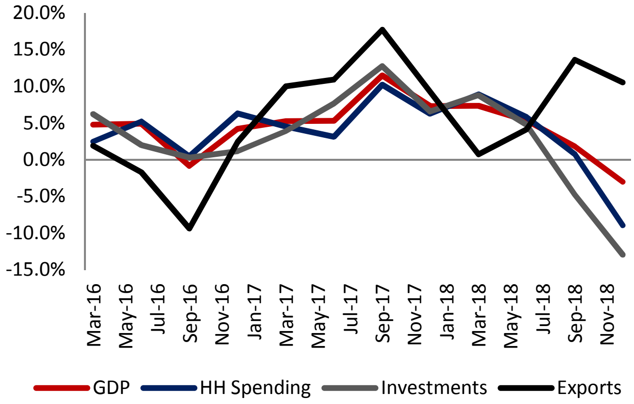
Source: Bloomberg, MIDFR

Chart 2: GDP Share by Supply-Side (%)



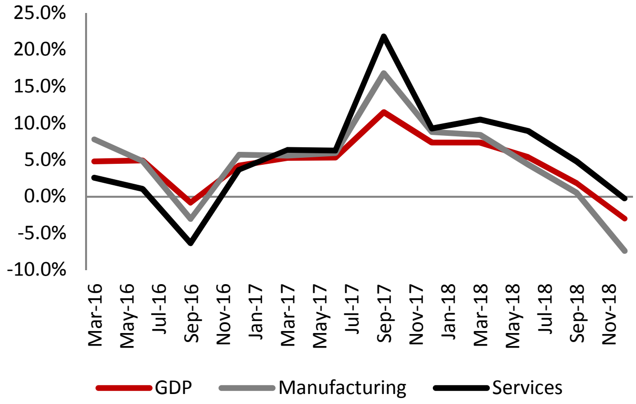
Source: Bloomberg, MIDFR

Chart 3: GDP Share by Expenditure (YoY%)



Source: Bloomberg, MIDFR

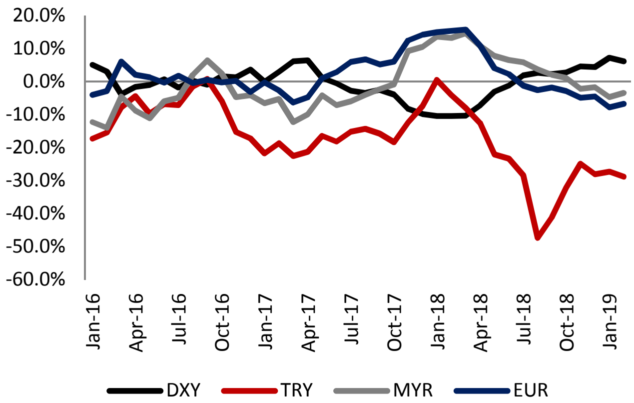
Chart 4: GDP Share by Supply-Side (YoY%)



Source: Bloomberg, MIDFR

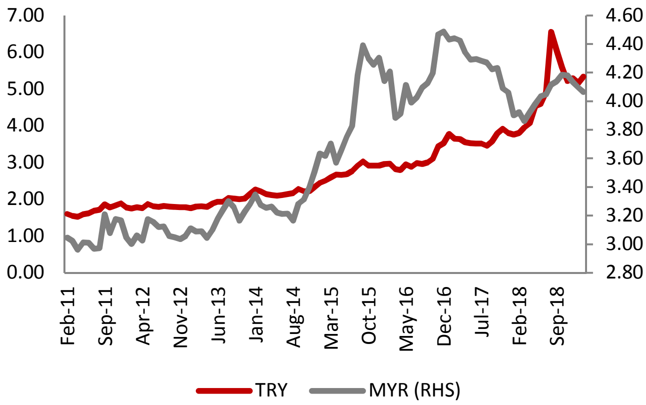
Lira remains in a bad shape. Deteriorating ties between the US and Turkey among others affected Lira to continue depreciating. The nosedived fall was due to the announcement higher tariffs on metal imports from Turkey in Aug-18. Lira plunged -47.3%yoy during the month. In fact, the currency has been on depreciating trend since Feb-18. Trade war tension, political uncertainty in EU and geopolitical risks in Middle East are among significant factors causing the Lira to slide. Moving forward, we foresee a steady rebound in currencies of emerging economies including Turkey and Malaysia especially when the US and China agree to sign a trade deal. In addition, slower pace of interest rate normalisation by the Fed provides rooms for the currencies to improve.

Chart 5: Lira vs Other Currencies (YoY%)



Source: Bloomberg, MIDFR

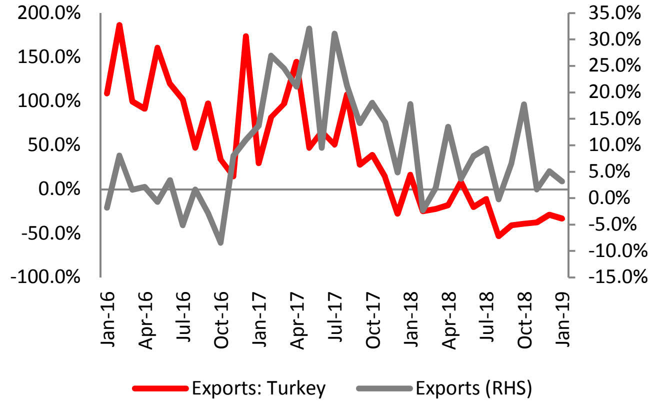
Chart 6: Lira vs Ringgit (Currency Value)



Source: Bloomberg, MIDFR

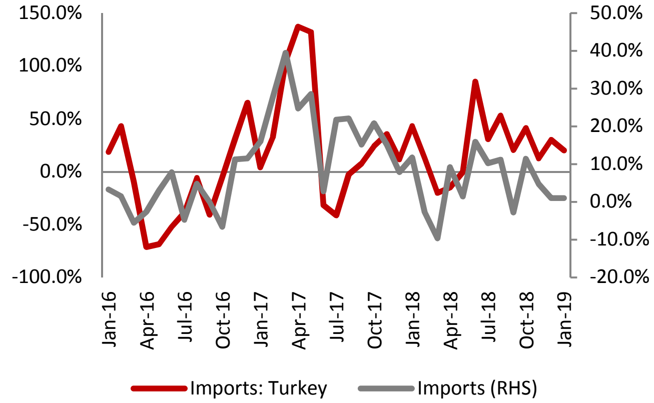
Minimal yet cautious impact to Malaysia. Tracking back the data, share of Turkey exports to Malaysia's total exports is relatively low hovering below 1% even after the implementation of Malaysia-Turkey Free Trade Agreement (MTFTA) in Aug-15. Turkey is ranked fourth for Malaysia's palm oil exports destination, constituting 5.2% of the commodity outbound shipments in Jan-19. As Lira plunged in Aug-18, we saw weakening exports to Turkey but on the other hand strong imports of Turkish products by Malaysia. With the less significant position, we expect the ongoing crisis in Turkey to have a minimal impact on Malaysia.

Chart 7: Total Exports vs Exports to Turkey (YoY%)



Source: CEIC, MIDFR

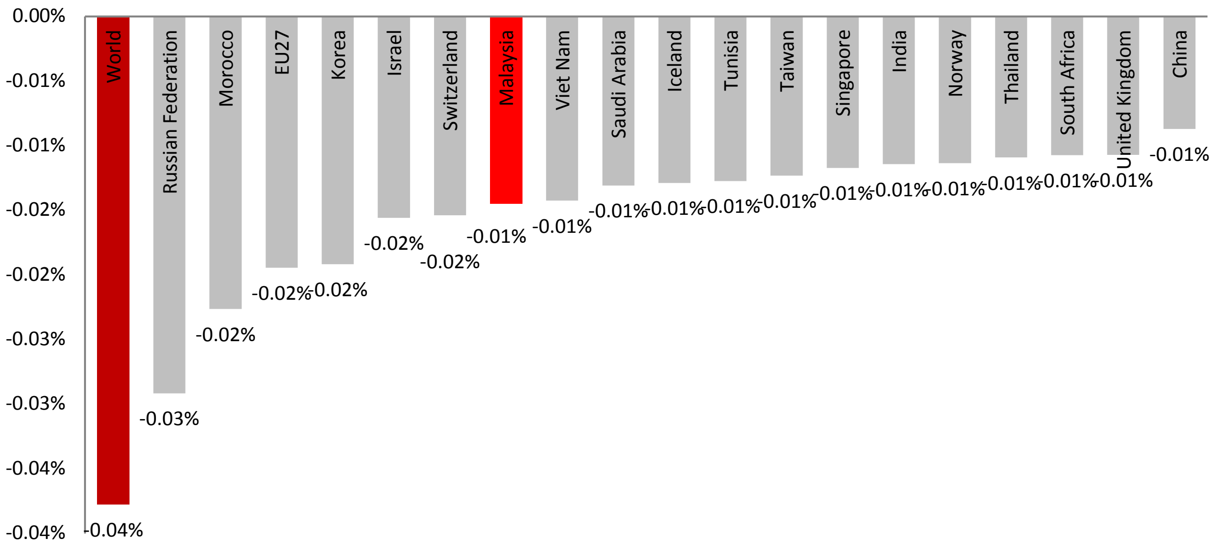
Chart 8: Total Imports vs Imports to Turkey (YoY%)



Source: CEIC, MIDFR

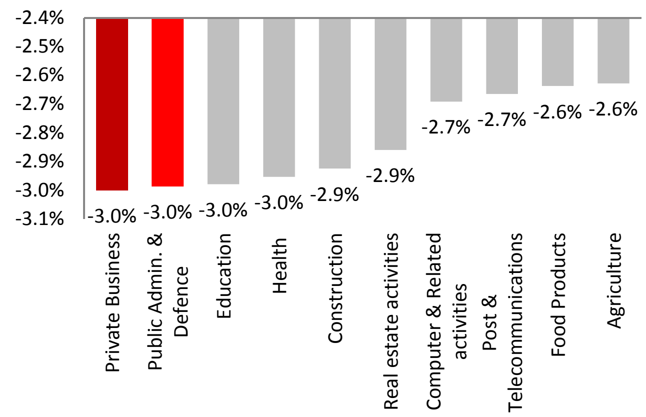
Trivial impacts to global economy. Based on our estimate, global economy is predicted to contract by -0.04% in the event of Turkey slowdown by -3%. Several economies from EU, Middle East and Africa would be impacted the most. As for Malaysia, slowdown in Turkey would affect marginal contractions in industries such as textiles, chemicals, food and agriculture. Overall, recession in Turkey has minimal impacts towards global growth as well as Malaysia's economic development.

Chart 9: Global Impacts as Turkey's Economy Contracted -3%



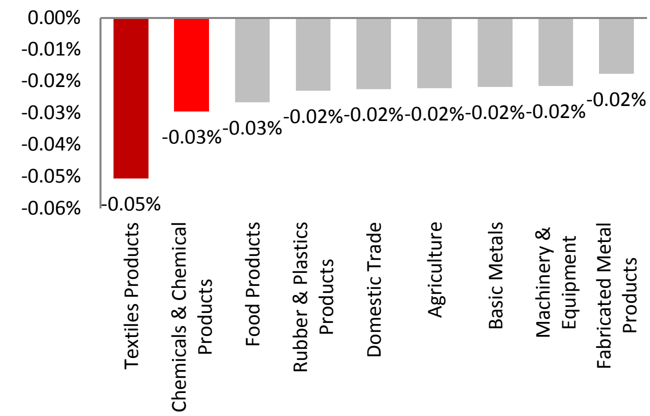
Source: CEIC, MIDFR

Chart 10: Sectoral Impacts on Turkey (%)



Source: OECD, MIDFR

Chart 11: Sectoral Impacts on Malaysia (%)



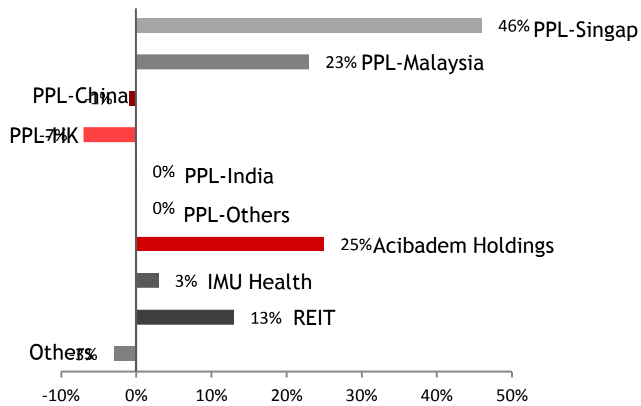
Source: OECD, MIDFR

Impact to key companies under our coverage which are operating in Turkey:

IHH Healthcare Berhad (IHH)

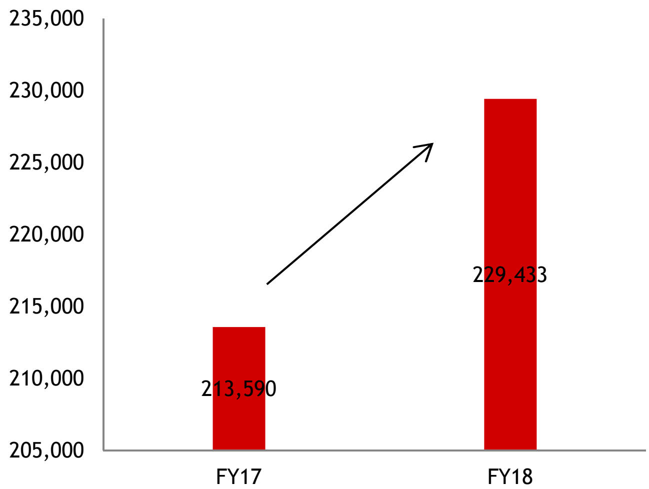
Neutral on the news. Turkey's leading private healthcare provider, Achibadem Holdings (90.0% owned subsidiary of IHH) contributed about 32.0% and 25.0% to IHH group's revenue and EBITDA respectively for the full year FY18. Despite the depreciation in Turkish Lira, FY18 revenue has only dropped by -3.0%yoy to RM1,813.7m while FY18 EBITDA was up by +2.0%yoy to RM297.1m. Looking at inpatient admissions, it grew by +7.4%yoy to 229,433 driven by the contribution from Acibadem Altunizade Hospital which was opened in March 2017. In addition to the increase inpatient admission, revenue intensity per patient has also improved driven by the: (i) price adjustments for patients on private insurance and paying out-of-pocket, (ii) taking on more complex cases and; (iii) increase in foreign patients.

Chart 12: FY18 EBITDA contribution by operating segment (%)



Source: Company, MIDFR

Chart 13: Achibadem Holidngs's inpatient admission (FY17 vs FY18)



Source: Company, MIDFR

Accelerating restructuring plans to reduce foreign currency debt. Nonetheless, IHH's FY18 earnings was dragged downed by the unrealised foreign exchange loss which had nearly doubled to RM644.1 in FY18 (from RM379.2m in FY17) driven by its sizeable non-Turkish Lira denominated borrowings (primarily in USD). According to the management, they are targeting to pare down its USD$250.0m subordinated loans by 1QFY19. This accounts for about 27.2% of Achibadem Holdings' total debt. Over the medium term, IHH will look to divest Acibadem's non-core assets to further reduce its foreign debt obligations and deleverage its balance sheet. On the bright side, Turkish Lira has recovered by more than +20.0% since September 2019. As such, we believe this has partially alleviate investors' concern.

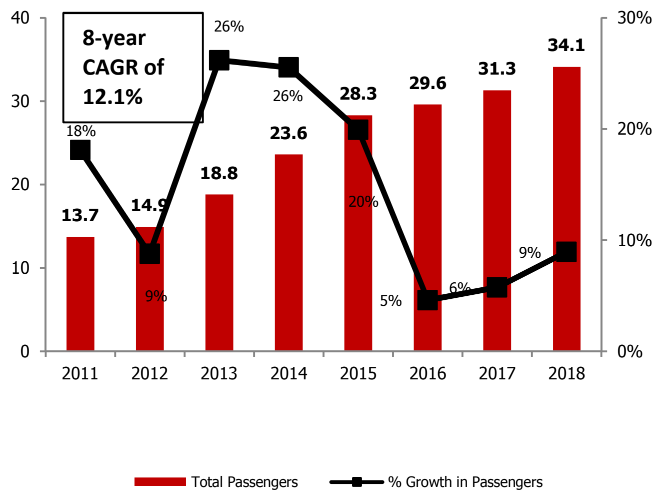
Maintain BUY, TP: RM6.57. All things considered, we maintain our **BUY** call on IHH with a target price of RM6.57 as we take comfort on management active efforts to reduce the Lira foreign exchange impact coupled with the healthy operating statistics recorded by Achibadem Holdings. Geographically, IHH has increasing exposure to India and Greater China with the recent acquisition of Fortis Healthcare Limited and ramped-up of Gleneagles Hong Kong. We believe these could power the group into its next phase of growth. In addition, we like IHH due to its adoption of multi-country portfolio strategy to diversify source of earnings as it is vital to eliminate country specific risk in the current global economic climate.

Malaysia Airports Holdings Berhad (MAHB)

Neutral on the news. MAHB generates around 20.0% of its total revenue from Turkey's International Sabiha Gokcen Airport (ISG). However, the revenues from Turkey operations are primarily generated in Euros (around 80.0-85.0%), while the operating expenses are denominated in the local currency, Turkish Lira. In relation to this, we opine that any depreciation of the Turkish Lira may help ISG to sustain their profitability and could possibly expand margins. Excluding the purchase price allocation for the fair valuation exercise on the Turkey operations, Turkey operations recorded a PBT of RM7.8m or approximately EUR1.7m, leading to a PBT margin of 0.2%.

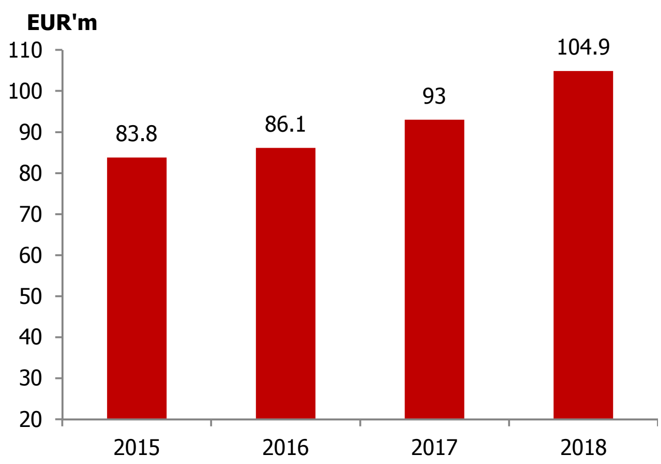
Operationally robust. ISG has managed to attract a strong flow of passengers over the past few years, leading to annual growth in both domestic and international sector with an 8-year CAGR of more than 10.0%. As such, aeronautical revenue in the form of passenger service charge has also been growing in tandem with the passenger growth of ISG. It was also notable that international passengers grew by 12.9%yoy in FY18 which outpaced the 6.7%yoy growth for domestic passengers. Latest figures as of February 2019 also indicate that international passengers have recorded five consecutive months of y-o-y growth. Therefore, we opine that any depreciation in the Turkish Lira could spur further demand in the international sectors which could offset uncertainties to the domestic traffic flow in the immediate term. This can be seen in the passenger traffic growth in ISGA for August 2018 remained resilient at +5.1%mom which offset the -2.8%mom drop in domestic growth despite the plunge in the Turkish Lira.

Chart 14: Annual passenger growth of ISG



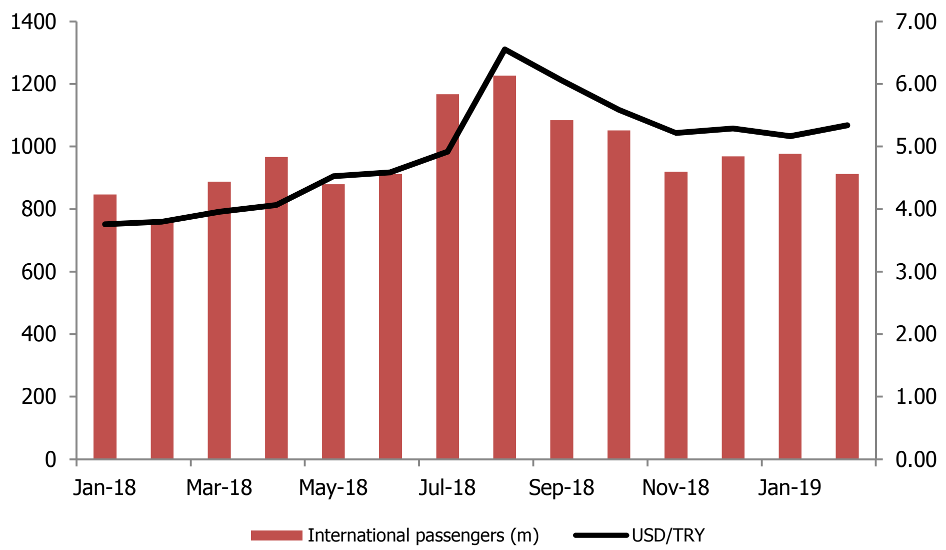
Source: Company, MIDFR

Chart 15: PSC Revenue of ISG



Source: Company, MIDFR

Chart 16: Relation between Turkish Lira and ISG international passenger growth



Source: Company, MIDFR

Moving forward, we opine that growth is likely to continue driven by increased airport capacity and future opening of ISG's second runway by 2019. This should provide a solid structural base for ISG to maintain its momentum, catering to the growing passengers' traffic. We noted that ISG was recognized as Europe's fastest growing airports in terms of number of passengers for seven consecutive years.

Figure 1: Overview of ISG's Runways

Source: Company

MAHB still a BUY, TP: RM9.44. While we are **NEUTRAL** on the news, we maintain our POSITIVE view on the group's overall operation. We believe the strong momentum of traffic flow primarily international to continue, underpinned by the robust air travel demand. This will be supported by supportive visa policies in Malaysia and increased direct flight connectivity to other airports beside KLIA Main Terminal and klia2. Accordingly, we maintain our BUY call on the stock with an unchanged TP of RM9.44 per share.

Tenaga Nasional Berhad (Tenaga)

Tenaga (BUY, TP: RM14.40) has exposure to the Turkey power sector via 30.0%-owned GAMA Enerji (Gama). Operationally, Gama registered positive EBITDA of USD110.9m in FY18 (RM455m), but was loss making at the bottomline. Tenaga's share of Gama's FY18 net loss is estimated at around RM140.0m, with the bulk contributed by forex losses in 2Q18-3Q18. However, Gama's losses accounts for just 2.0% of Tenaga's core net earnings of RM5.9b in FY18. Given that the Turkish Lira saw sharp depreciation last year, Tenaga had already fully impaired its carrying value in Gama of RM496.0m in FY18 (in 2Q18 and 3Q18). Additionally, Tenaga took a RM207.0m impairment for financial guarantees to Gama's lenders in 4Q18. We see minimal risk of any further impairments going forward.

DISCLOSURES AND DISCLAIMER

MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS	
STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <-10% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >10% 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.