

THEMATIC REPORT | Pocket of Opportunities from Revival of Infra-Projects for Logistics Sector

Author:
Adam Mohamed Rahim
adam.mrahim@midf.com.my
03-2772 1686

KEY HIGHLIGHTS

- 2H19 is expected to see a significant rebound in investment activities and continuous upward trajectory for domestic consumption
- The construction sector grew +0.5%yoy in 2Q19 underpinned mainly by the civil engineering subsector which grew by +5.4%yoy in the same quarter
- We believe that there would be spill over effects on the transportation and storage subsector as it recorded the fifth largest growth amongst 17 services subsectors with a +7.0%yoy growth during the same period
- However, this positive impact will be only for a select few
- Tiong Nam, Tasco and MMC Corp's JP Logistics could be a potential beneficiary, as well as Xin Hwa which already has a strong track record in project logistics

Rebound in investment activities expected in 2H19. The Malaysian economy posted a Gross Domestic Product (GDP) growth of +4.9%yoy in 2Q19, marginally above market expectations and our forecast of +4.7%yoy and +4.8%yoy respectively. In fact, this is the highest GDP growth in five quarters. We opine that 2H19 will likely see a significant rebound in investment activities and continuous upward trajectory for domestic consumption. In addition, the positive progression in infrastructure projects such as ECRL and possibly LRT 3 would boost the Government's spending and investment in the medium and long term.

Performance of the construction sector and the transportation sub-sector. The construction sector grew +0.5%yoy in 2Q19 underpinned mainly by the civil engineering subsector which grew by +5.4%yoy in the same quarter. Moving forward, the construction sector is predicted to stay on a healthy pace underpinned by the positive progression of the sector and revival of infrastructure projects. As construction projects are expected to pick up steam in 2H19, we believe that there would be spill over effects on the transportation and storage subsector under the services sector as precast structure would have to be transported to construction sites. The services sector accounted for 57.2% of total GDP and expanded steadily at +6.1%yoy in 2Q19. The transportation and storage subsector followed suit to record the fifth largest growth amongst 17 services subsectors with a +7.0%yoy growth during the same quarter.

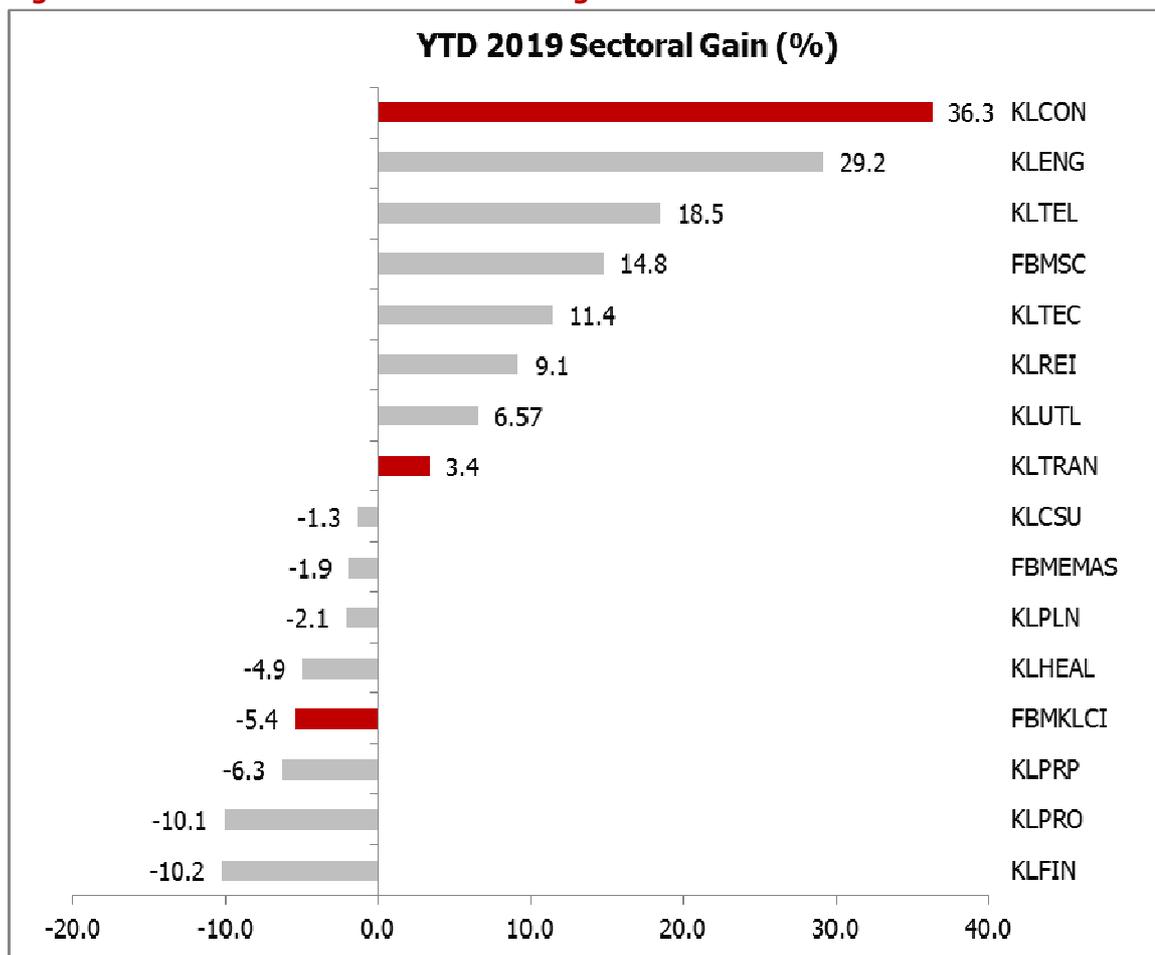
Table 1: Summary of GDP by Supply-Side Approach

	QoQ%			YoY%		
	4Q18	1Q19	2Q19	4Q18	1Q19	2Q19
GDP	3.5	(4.3)	2.1	4.7	4.5	4.9
Construction	(4.6)	1.4	(3.6)	2.6	0.3	0.5
Residential	(1.6)	(0.1)	(9.6)	(9.2)	(7.2)	(1.1)
Non-Residential	14.8	(20.3)	(5.1)	2.8	(4.0)	(9.1)
Civil Engineering	(16.6)	16.2	(2.0)	11.0	7.1	5.4
Special Trades	(7.5)	9.5	2.9	6.4	2.9	4.7
Services	3.8	(4.6)	2.4	6.9	6.4	6.1
Transportation & Storage	4.7	(2.3)	2.0	6.7	6.7	7.0

Source: CEIC, MIDFR

Sectoral indexes have also followed suit. We could observe a parallel in terms of the sectoral indices performance of the FBM KLCI. Amongst the 10 sectors that outperformed, **KL Construction Index** is leading gainers with a 36.3% year-to-date gain. Although the **KL Transportation Index** has only gained +3.4% so far this year, this is an improvement from last year's -17.5% decline in 2018. More importantly both KL Construction and Transportation indexes outperformed the local benchmark.

Figure 1: FBM KLCI Sectoral Year-to-date gains



Source: MIDFR, Bloomberg

Note: As of Friday, 16 August 2019

More encouraging tone from revival of projects. To recall, the projects were either delayed or deferred due to a review in 2Q19 on its contractual agreement. In terms of job outlook, our construction analyst is turning more optimistic in 2H19, based on the historical trend we saw previously. Taking these factors into account, 2H19 is likely to fare better to offset the anticipated slowdown in 1H19. The mood in 2H19 seems to be developing on a more encouraging tone as we believe that the execution of progress works is likely to shift to a higher gear. Meanwhile, we believe notable developments in the sector could also stem from the outcomes of Pan Borneo Highway Sabah and Johor-Singapore RTS projects, with each carrying a value of RM12.8b and RM4.0b respectively.

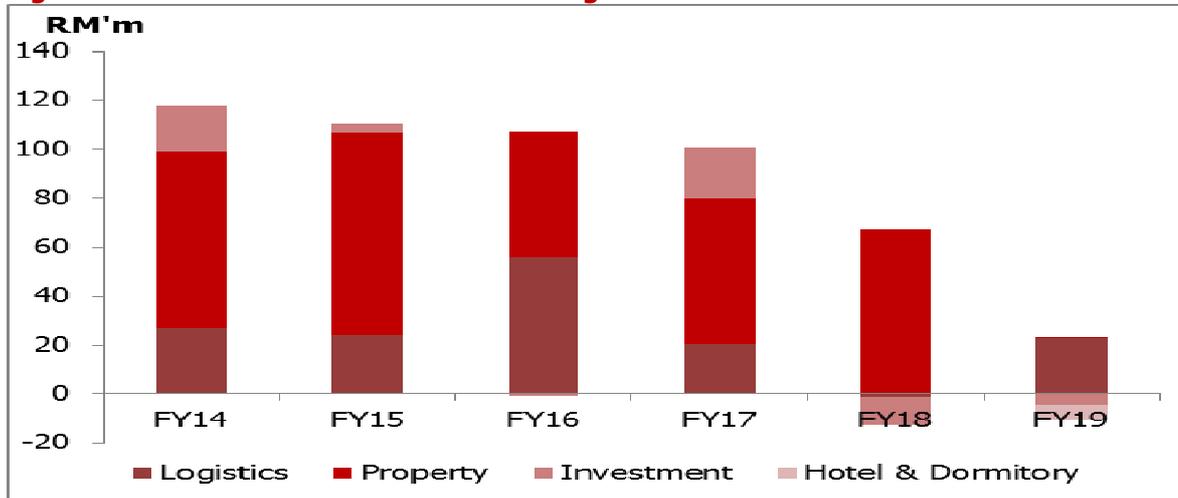
Table 2: List of Projects in Malaysia

Projects	Estimated Value (RM'b)	Remarks
KVMRT2	30.5	Overall progress at 45% as of 1Q19, with completion expected in 2022
KVLRT3	16.6	Progress works to resume in 2HFY19
Gemas-JB Double Tracking	8.9	Sub-contracting works awarded, with expected completion by October 2021
Klang Valley Double Track Upgrade (Phase 2)	4.5	New consultant has been appointed, followed by re-tendering. Upon earlier termination, progress was at 3%. Initially, completion period was scheduled for seven years. Its first phase will be completed in August 2019.
Johor –SG RTS Link	4.0	To be implemented, but no particular timeline was announced. 6-months extension was granted by Singapore. Currently, supplementary agreement is being drafted as Malaysia look for options to reduce costs. Extension was granted until September 2019.
East Coast Rail Link	44.0	The project was relaunched in July 2019. Target completion is December 2026.
KVMRT3	60.0	Shelved until completion of KVMRT2.
KL-SG High Speed Railway	110.0	Deferred to May 2020

Source: MIDFR, Various sources

Possible spillover effects on logistics companies. As mentioned earlier, logistics companies are expected to benefit from the resumption of infrastructure projects as precast structures, machinery and railway equipment will need to be transported. Transportation services for over-dimensional and heavy cargo for large-scale projects, which is commonly known as project cargo will be in demand upon the pickup in construction activities. Amongst the companies under our coverage, we note that **Tiong Nam Logistics Holdings Berhad (Tiong Nam) (SELL; TP: RM0.41)** could potentially be an indirect beneficiary of the pickup in construction as it possesses capabilities for the transportation of heavy-duty equipment required in large-scale projects. Tiong Nam's fleet of low-loaders, lorry cranes and Cometto trailers (40 axle) for transportation of heavy-duty cargo and machinery is supported by a range of integrated crane service systems including lattice-boom, mobile and all-terrain cranes, with between 8 and 330 tonne load capacities. In addition, Tiong Nam processes all applications with the relevant local authorities such as the Road Transport Department and the Malaysia Public Works Department to guarantee smooth passage of goods in compliance with all regulatory requirements. Nevertheless, we believe that this could only provide minimal support as overall profitability is expected to be weighed by the weak performance of its property development segment which is mainly focused in Johor (*refer Figure 2*).

Figure 2: Historical PBT breakdown of Tiong Nam



Source: Tiong Nam

Figure 3: Transportation of Segmental Box Girder



Source: Tiong Nam

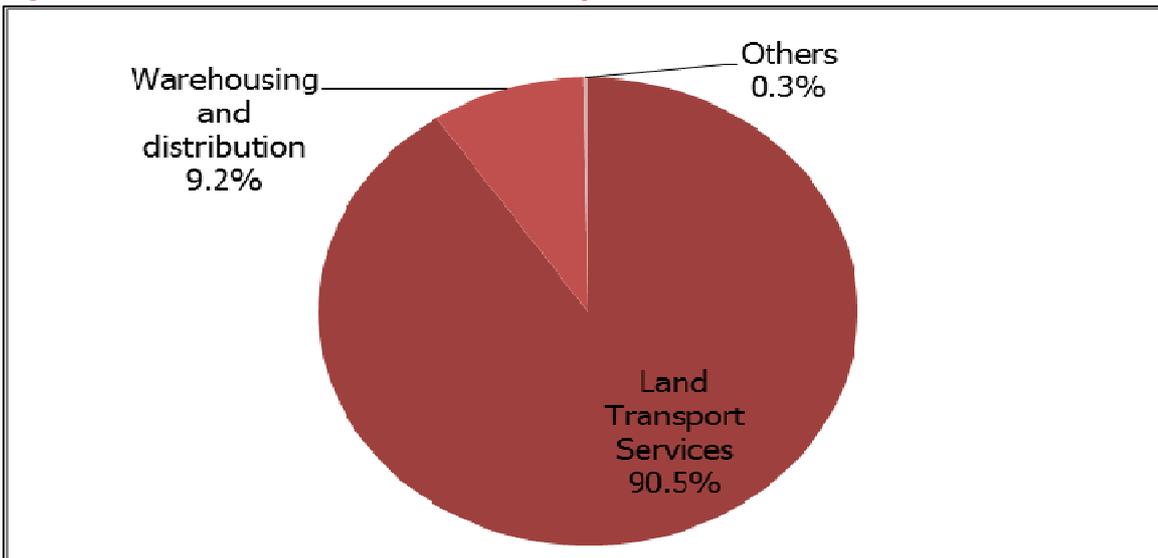
Figure 4: Delivery of Cement Plant Kiln Section



Source: Tiong Nam

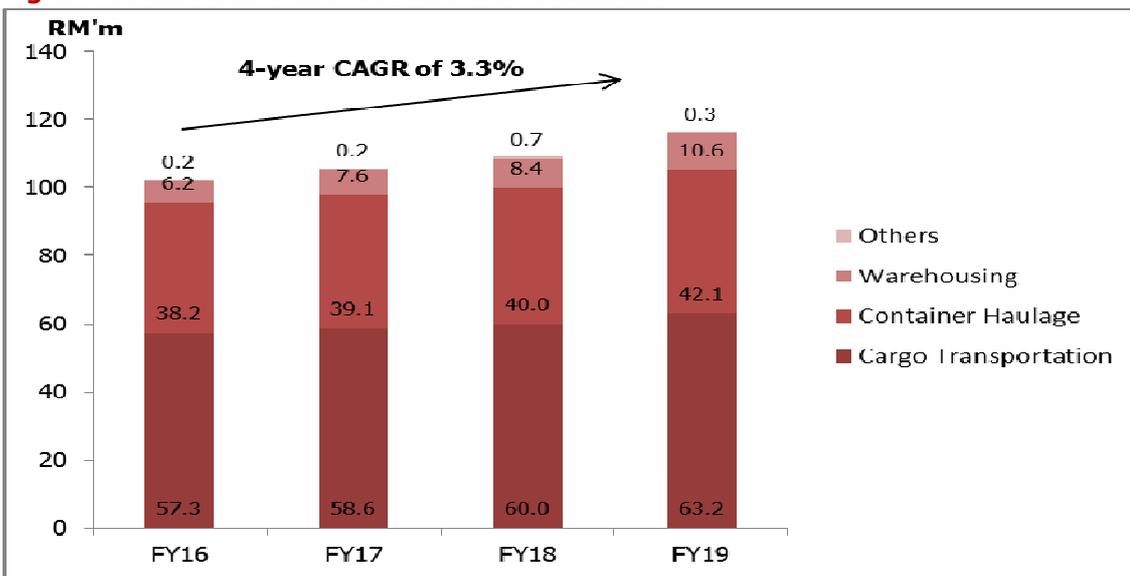
Another public listed company that could be a potential beneficiary is **Xin Hwa Holdings Berhad (Xin Hwa) (NON-RATED)** as it possesses the technical expertise to provide project logistics services for cargo weighing over 50 tonnes. Such expertise is highly specialised and difficult to replicate by its competitors. Xin Hwa operates three major business segments which are: land transportation services which includes cargo transportation services and container haulage services; (ii) warehousing and distribution and (iii) others (manufacturing and fabrication of trailers and freight forwarding). Cargo transportation services which include normal cargo and project cargo makes up around 55% of Xin Hwa's total revenue with solid gross profit margins of above 30.0%.

Figure 5: Xin Hwa's revenue contribution by business activities



Source: Xin Hwa Annual Report 2019

Figure 6: Annual Revenue Breakdown of Xin Hwa



Source: Bursa, Xin Hwa, MIDFR

Note: Revenue for FY16 and FY17 apportioned to reflect periods of quarter ended June' 15 to Mar '16 and June'16 to Mar'17 prior to change in financial year end from December to March

Solid track record from Xin Hwa. Xin Hwa has a track record of providing project logistics services to the construction and oil & gas sectors, having delivered precast concrete tunnel linings for both the KVMRT2 and Singapore MRT projects in the construction industry, and process equipment for oil and gas players. Its strength in the project cargo business will be buttressed by 29 units of multi-axle modular trailers comprising of 156 axle lines (previously 9 units of axle modular trailers comprised of 44 axle lines) making it the company with the biggest capacity in Malaysia.

Table 3: List of contract awards to Xin Hwa in Malaysia for project cargo

Project	Value (RM'm)	Remarks
Pengerang Refinery and Petrochemical Integrated Development Project (RAPID)	5.0	Transportation of equipment
Malaysia Marine Heavy Engineering (MMHE)	1.8	Transportation of spent copper slag from MMHE's yard to the site of its customers
Klang Valley Mass Rapid Transit Line II (KVMRT 2)	13.7	Transportation of precast segmental box girders and crossbeams for the construction and completion of viaduct guideways and other associated works at various project sites of the line.

Source: Bursa, Company

Xin Hwa's contracts which are on hold to resume soon. Previously in December 2017, Xin Hwa was awarded a contract worth up to RM16.8m to deliver precast viaduct and other related products for the Bandar Utama – Klang LRT line (LRT3) for a span of 24 months which was supposed to begin in end 2017. However, the contract has been put on hold when the Government was reviewing the overall costing which led to a revised cost of RM16.6b from the earlier cost of RM31.5b. Notwithstanding this, works for the LRT3 project are expected to resume in 2H19 and will be beneficial for the company's orderbook albeit at a possibly lower amount than what was initially awarded.

Figure 7: Axle-lines deployed by Xin Hwa for MRT2 contract



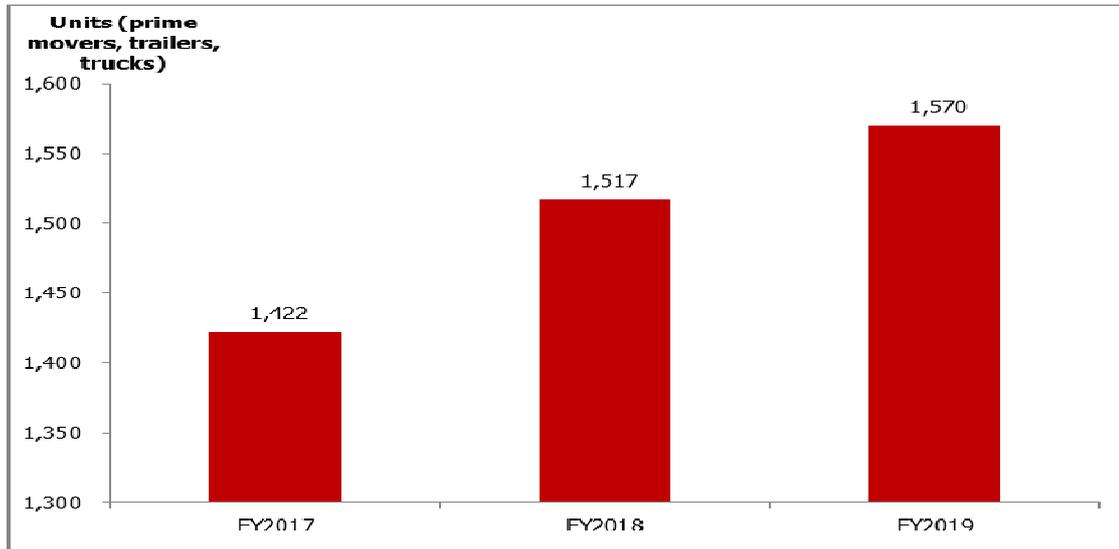
Source: Xin Hwa

Figure 8: Transportation of equipment at RAPID Pengerang



Source: Xin Hwa

Figure 9: Xin Hwa's Fleet Size



Source: Xin Hwa

Container haulage segment could also benefit. Another segment which could potentially benefit is the container haulage segment as some materials, machinery and equipment which are of smaller size are transported via containers from ports to construction sites. **Tasco Berhad (Tasco) (Trading BUY; TP: RM1.68)** is a company under our coverage which has exposure to the container haulage business in addition to Tiong Nam. Tasco's container haulage business is under its contract logistics division which contributes over 40% to the total revenue. The container haulage business itself has registered revenue growth in the past three consecutive years underpinned by the rise in container deliveries especially for electrical and electronics (E&E) and musical instrument customers. As such, the commencement of infrastructure projects by the Government presents an opportunity for Tasco to widen its client base.

We also do not discount the possibility of JP Logistics, a subsidiary of **MMC Corp's (BUY; TP:RM1.31)** Johor Port which also operates container haulage business to leverage from the pickup in construction projects. However, we believe that the potential benefits for container haulage business will not be as much as for transportation cargo due to intense competition (from both listed and non-listed companies) in this segment. Among the players in the non-listed space include Megalift, Nistrans, Avis Pioneer Logistics and Hellmann.

Figure 10: Container haulage by Tasco



Source: Tasco

Figure 11: Container Haulage by JP Logistics



Source: MMC

Conclusion. Overall, we do see a potential spill over from the slew of construction projects for companies under our coverage. However, we opine that the benefits are only for a select few. While we recognize that Tiong Nam may be a beneficiary, it is being dragged by its property development segment. Meanwhile, we do not foresee any gains accruing to companies that focuses mainly on courier delivery and warehousing business such as **GD Express Carriers Berhad (NEUTRAL; TP:RM0.30)**. As mentioned above, Tasco could leverage on the pickup of the construction sector but its main agent of growth driving forward would be its cold supply chain logistics business. Therefore, in our opinion, only Xin Hwa is the only player in the listed space at this juncture which could benefit highly from the Malaysia's infrastructure development. 

Adam Mohamed Rahim
adam.mrahim@midf.com.my
03-2772 1686

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 >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> 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 <i>fall</i> 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.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.