CONSTRUCTION

***Maintain* POSITIVE**

A sigh of relief

KEY INVESTMENT HIGHLIGHTS

- **Construction is among the 3 sectors allowed to hire workers from all 15 permitted source countries**
- **Government had also approved proposal by CLAB to fully manage entry of foreign construction workers involving more than 100 people. These are positive for the sector, which requires about 600,000 foreign workers**
- **Malaysia will be engaging Indonesia on the issue of hiring freeze, which we believe will be resolved amicably**
- **Maintain POSITIVE on construction sector. Top BUYS include Gamuda (BUY, TP: RM4.02), IJM Corp (BUY, TP: RM2.18) and Sunway Construction (BUY, TP: 1.87)**

A much-needed relief. The Government has given the green light for three crucial sectors – construction, manufacturing and services – to hire foreign workers from all the 15 permitted source countries as stipulated by the Home Affairs Ministry. This is on top of the approval given to a proposal by the Construction Labour Exchange Centre Bhd (CLAB), an organisation under the Construction Industry Development Board (CIDB), to fully manage the entry of foreign construction workers involving more than 100 people. These will provide much relief for the construction sector, which has been plagued with the issue of labour shortage, triggered by the MCOs in 2020 and 2021 that saw many foreign workers returning to their originating countries, including those that caught their employers off guard by fleeing illegally.

Alternative sources. The Government's latest decision opens up the avenue for construction companies to hire workers from other countries such as Thailand, Cambodia, Nepal, Myanmar, Laos, Vietnam, the Philippines, Pakistan, Sri Lanka, Turkmenistan, Uzbekistan and Kazakhstan. This is a vital move at a time when Indonesia has put in place a hiring freeze stemming from what seems to be a misunderstanding on the online systems to be used for hiring domestic helpers from Indonesia. We gather from the industry that Indonesian construction workers are generally preferred as they are higher skilled. Since that option is off the table now with the temporary hiring freeze by Indonesia, we believe that the next in line in terms of preference will be workers from Bangladesh, apart from all the other countries that construction firms can now hire from.

About 600,000 needed. The construction industry currently needs about 600,000 foreign workers as industry players ramp up their operations with the reopening of the economy and as they gear up for upcoming infrastructure contract rollouts, starting with the MRT3 in 4QCY22. Pre-Covid, the construction sector's number of filled jobs peaked at 1.31 million people in 4QCY19. This dwindled to 1.22 million people as of 1QCY22, a reduction of -6.8% or 88,600 people, according to DOSM's quarterly employment statistics. A shortage of labour causes delay in work progress, which may lead to penalties or Liquidated Ascertained Damages (LAD) claims. Contractors have no recourse in these situations.

COMPANIES IN FOCUS

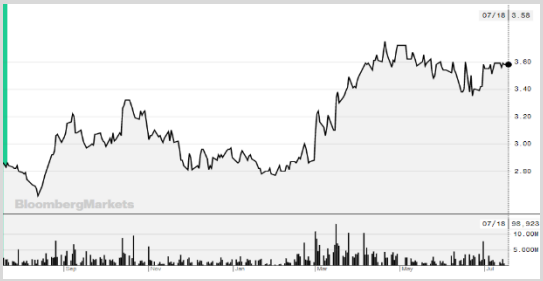
Gamuda Bhd

Maintain BUY | Unchanged target price: **RM4.02**

Price @ 18th July 2022: RM3.64

- Vast experience in MRT1 and MRT2, making it the frontrunner of MRT3's largest contract
- Record high order book of RM14.37b with strong overseas job wins, earnings visibility up to FY26
- Effective margin protection measures

Share price chart



IJM Corp Bhd

Maintain BUY | Unchanged target price: **RM2.18**

Price @ 18th July 2022: RM1.70

- Potential winner of MRT3's second largest contract
- Solid outstanding order book of about RM4.26b which translates into earnings visibility up to FY24
- Solid margin protection measures

Share price chart



MIDF Research
research@midf.com.my

Amicable resolution soon? As we expected, the Malaysian Government will be engaging its Indonesian counterparts, represented by the Immigration Department and the Human Resources Ministry to look into the issue of the hiring freeze. We believe an amicable resolution can be expected soon, at least before the rollout of mega projects locally. The ongoing tiff between Malaysia and Indonesia, while uncalled for, may be happening at the right time in our view, before we start to see inflows of infrastructure projects. A lull period is expected prior to the rollout of MRT3 in 4QCY22 and both governments are expected to resolve the matter by then. In the meantime, depending on the size of projects at hand, we are not too concerned about the shortage of workers affecting the companies under our coverage. Even if the issue prolongs, construction companies are still able to rely on hiring workers from Bangladesh, their next top choice after Indonesia and from other source countries. Despite the lack of foreign workers in the industry, some companies are comfortable with their current workforce levels as their ongoing projects do not require a huge number of labour while other companies have immediate need for workers. Sunway Construction for example, had earlier obtained necessary approvals from the authorities and have paid all the levies and agency fees for about 400 workers, mainly from Indonesia. This in our view, would not be a problem even with the current freeze in place.

Maintain POSITIVE. We reiterate our **POSITIVE** recommendation on the construction sector as we do not view the issue of foreign labour shortage to be a massive headwind for the sector, especially with the Government's commitments to assist industry players with the relaxation for hiring from other source countries. We are also optimistic that the issue of hiring freeze from Indonesia can be resolved amicably between both Governments. Among other factors are the manageable cost headwinds and the potential rollout of infrastructure projects in Malaysia, with positive developments being driven by the upcoming MRT3 tender awards in 4QCY22. As mentioned previously, we continue to favour companies with robust balance sheets, which will give them the headroom for upfront financing requirements such as in MRT3 and for future highway projects where the Government will no longer provide financial assistance. Thus, our top picks for the construction sector are **Gamuda (BUY, TP: RM4.02)**, **IJM Corp (BUY, TP: RM2.18)** and **Sunway Construction (BUY, TP: 1.87)**. On a side note, we want to put forth a view that it is timely for the construction to seriously adopt labour-saving technologies including automation with a long-term view of reducing the reliance on low-skilled foreign labour. As cliché as it may sound, the industry should not let a moment of crisis like this, no matter how insignificant the impact, go to waste.

PEER COMPARISON TABLE

Stock	FYE	Rec.	Price @ 18 July 2022 (RM)	Target Price (RM)	Core EPS (sen)		Dividend Yield (%)		Net gearing	Net cash/(debt)
					FY22E	FY23F	FY22E	FY23F		
Gamuda	July	BUY	3.64	4.02	25.9	27.7	3.5	12.4	10.9%	(RM1.1b)
IJM Corp	Mar	BUY	1.70	2.18	10.5	13.8	2.8	2.8	-	RM557.6m
Sunway Construction	Dec	BUY	1.54	1.87	9.6	10.7	2.7	2.7	17.0%	(RM129.8m)
MRCB	Dec	BUY	0.34	0.44	1.7	1.5	2.3	4.5	28.6%	(RM1.3b)
Muhibbah Engineering	June	BUY	0.42	0.67	11.1	14.4	2.6	3.7	4.2%	(RM69m)
WCT Holdings	Dec	BUY	0.44	0.86	6.2	6.6	0.6	0.6	73.3%	(RM2.78b)
Gabungan AQRS	Dec	BUY	0.295	0.56	6.8	9.2	1.7	1.7	29.6%	(RM144.8m)
Pintaras Jaya	Dec	BUY	2.22	3.14	33.0	26.1	4.1	6.4	-	RM82.2m
KKB Engineering	June	BUY	1.35	1.50	8.6	9.7	3.3	3.3	-	RM181.6m
Malayan Cement	June	BUY	2.10	3.00	8.7	9.8	-	-	57.9%	(RM3.32b)
Cahya Mata Sarawak	Dec	BUY	0.895	1.37	19.1	17.1	2.6	2.2	-	RM100.6m

Source: Company, MIDF Research

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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.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.
ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell	
☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology