CONSTRUCTION

***Maintain* POSITIVE**

Raw material price poser

KEY INVESTMENT HIGHLIGHTS

- **Average steel bar prices risen for 19 consecutive months to RM3,900 per tonne while average cement prices were up for 15 consecutive months to RM21/50kg in June**
- **Steel bars averaged around RM2,600 to RM2,900 per tonne pre-Covid while cement averaged around RM18 to RM19 per 50kg bag**
- **Channel checks showed that steel bar prices moderated to between RM2,900 and RM3,500 per tonne while cement prices remained firm**
- **Maintain POSITIVE on construction sector with sound margin protection measures in place and on positive developments on project rollouts, led by MRT3**
- **Top BUYS include Gamuda (BUY, TP: RM4.02), IJM Corp (BUY, TP: RM2.18) and Sunway Construction (BUY, TP: 1.87)**

An ongoing concern. The spike in cost of raw materials has been a bane for the construction sector since the gradual relaxation of Covid-19 restrictions across the globe towards 4Q2CY0, about the same time when Pfizer and BioNTech announced their vaccine candidate. It was a combination of two factors, the bottlenecks in the supply chain and the surge in demand amidst the reopening of economies. We take a look at the prices of steel bars and cement, among the two materials that contractors are most reliant upon.

Steel bar prices. According to DOSM's monthly data, our computation showed that the average steel bar price – comprising five types of mild steel bars and four types of high tensile deformed bars – rose for the 19th consecutive month since Dec-20 to RM3,901.81 per tonne as of Jun-22. While the figure last month rose +25.2%yoy, the month-on-month comparison showed a minimal increase of only +0.23%mom as compared to between +0.68% and +9.52% from Dec-20 to May-22. We believe this may suggest that steel bar prices have peaked, which could see prices starting to moderate soon, assuming no further disruptions to the supply chain. Our channel checks support this theory, as latest prices have since moderated to a range of about RM2,900 to RM3,500 per tonne. Back in Dec-20, the average price per tonne was RM2,737.87, meaning that there has been an increase of +42.5% or RM1,163.94 as of Jun-22. Pre-Covid, steel bar prices generally averaged around RM2,600 to RM2,900 per tonne. The only time it went above the RM3,000 mark was four years ago in Apr-18 and May-18 at RM3,018.05 and RM3,013.57 respectively.

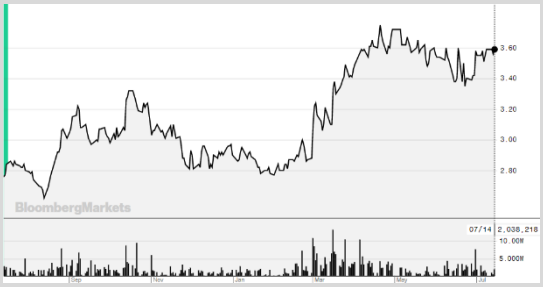
Cement prices. The binding substance averaged out at RM21.05 per 50kg bag in Jun-22 to record a jump of +12.8%yoy, marking its 15th straight month of increase since Apr-21. Like steel bars, the month-on-month increase was marginal at +0.29%mom as compared to previous months, which saw month-on-month increases ranging from +1.1% to +2.4%. The average cement prices per 50kg bag only hit above the RM20 mark in Mar-22. Pre-Covid, it averaged around RM18 to RM19.

COMPANIES IN FOCUS

Gamuda Bhd
Maintain BUY | Unchanged target price: **RM4.02**
Price @ 14th July 2022: RM3.59

- 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

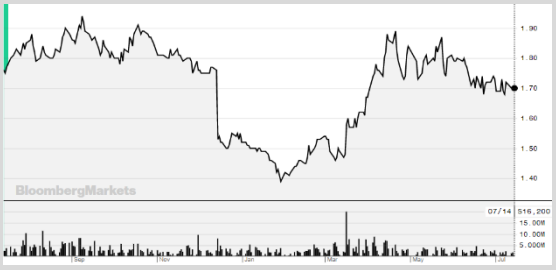
Share price chart



IJM Corp Bhd
Maintain BUY |Unchanged target price: **RM2.18**
Price @ 14th 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



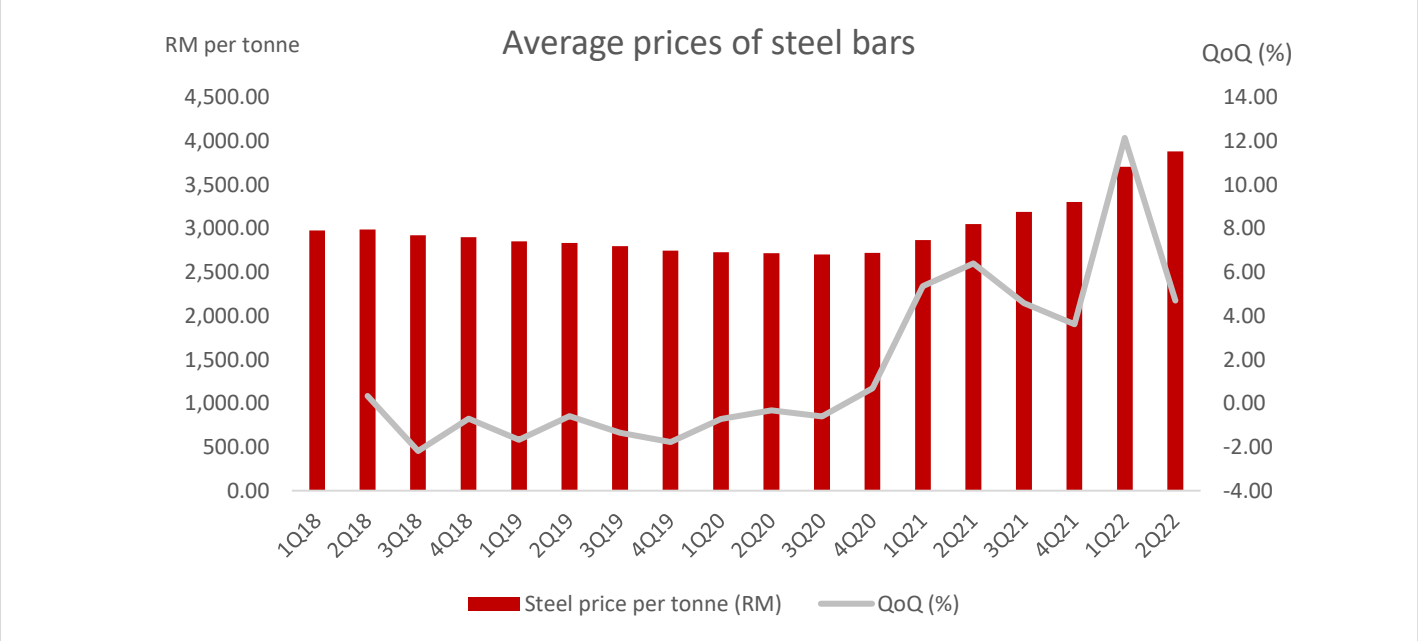
MIDF Research
research@midf.com.my

Our take. We reiterate our view as per our previous reports that we are not overly concerned about the building materials price headwinds being a huge risk to the companies under our coverage as they are still able to mitigate the impacts, on top of margin protection measures such as variation-of-price clauses, which allows part of the additional cost to be passed on to clients. Even if such elements are not available, some contracts would have priced in potential cost inflation or negotiations would have been engaged with clients to put in place huge buffers for possible spike in prices. Unless building material prices continue rising exorbitantly, industry players, albeit the bigger ones, have indicated that the impact is minimal to margins and since our channel checks showed that prices of steel bars have started to ease, in line with the global slump of hard commodities, we believe this would only augur well for companies under our coverage.

Impact on construction players. Gamuda Bhd's management previously guided that impact is rather minimal due to cost escalation clauses in most of its contracts and in projects where such pass through is unavailable, they are confident that their clients would be able to release some of the built-in cost buffers. As for IJM Corp Bhd, the group remains firm that its PBT margin guidance of 6% to 9% is achievable. Checks with Sunway Construction Bhd pointed towards a minimal impact of rising prices, if any, for the projects it secured at the end of 2021. It only purchases steel bars on a need basis, which would allow it to take advantage of the softening prices currently. For its precast segment which is predominantly in Singapore for the Housing Development Board (HDB) projects, there are cost past through clauses for steel bars, in addition to ex-gratia payments for additional support scheme in co-sharing for the rise in steel prices from Jan-21 to Jul-22. Meanwhile, price escalation clauses for Sunway Construction's highway projects in India have also been signed at the onset.

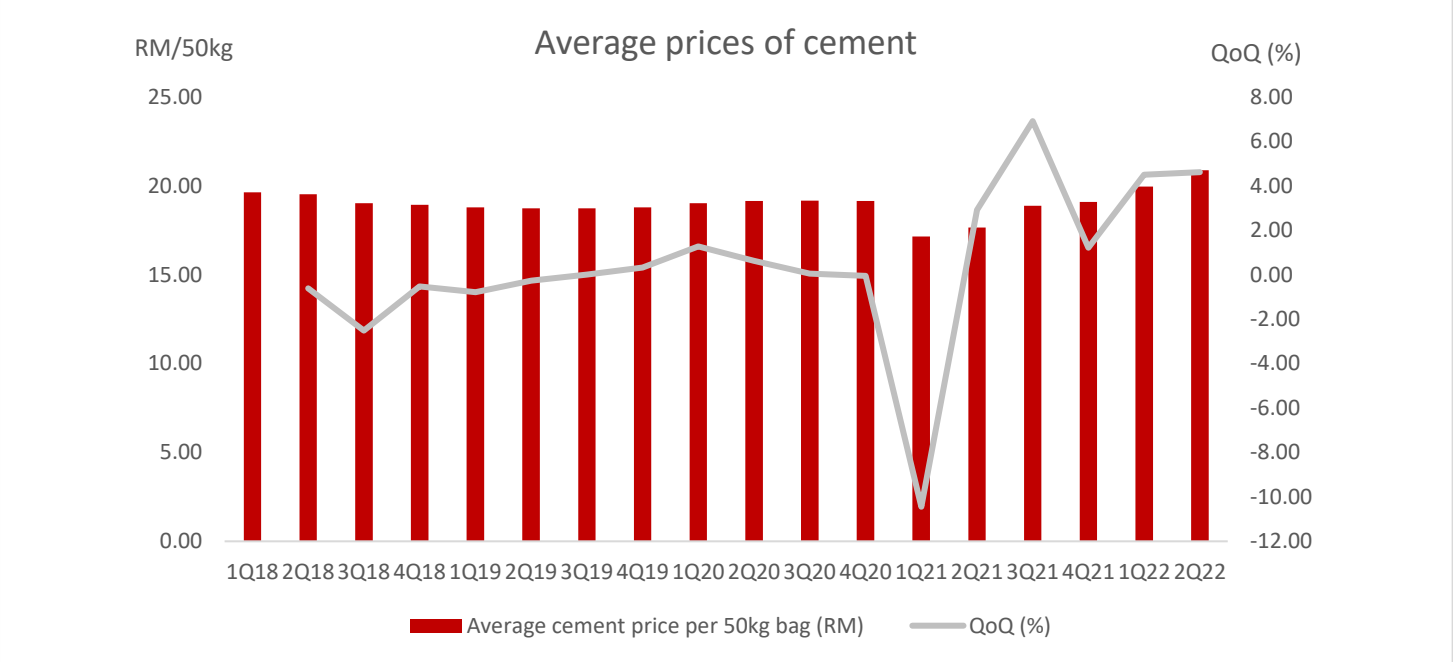
Maintain POSITIVE. We reiterate our **POSITIVE** recommendation on the construction sector in view of the manageable cost headwinds and the potential rollout of infrastructure projects in Malaysia, with positive developments being driven by the upcoming MRT3 tender awards in 4QVY22. We are now inching closer towards the deadline of the tender submissions scheduled next month, Aug 2 for CMC302 (est. contract size RM13.94b) and CMC303 (est. contract size 14.29b) and Aug 30 for CMC301 (est. contract size RM2.79b). Gamuda will be bidding for CMC303 with its partner MMC while we believe IJM and Sunway Construction are targeting CMC302, with CMC301 being the consolation. Also, going by media reports, the Government has given approvals in principle for the construction for the Petaling Jaya Dispersal Elevated Highway (PJD Link), Putrajaya-Bangi Expressway (PBE) and the Kuala Lumpur Northern Dispersal Expressway (KL-NODE). There are also talks of a 64km highway from Gopeng to Kuala Kangsar, which was approved by the Perak Government. Another rail project that is gaining traction is the potential revival of the axed KL-Singapore High Speed Rail (HSR) as Transport Ministries in both countries have begun engagements. Malaysia will also potentially undertake a feasibility study for the line to stretch all the way to Bangkok. At this juncture, 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)**.

Figure 1: Average prices of steel bars (quarterly)



Source: DOSM, MIDF Research

Figure 2: Average prices of cement/50kg (quarterly)



Source: DOSM, MIDF Research

PEER COMPARISON TABLE

Stock	FYE	Rec.	Price @ 14 July 2022 (RM)	Target Price (RM)	Core EPS (sen)		Dividend Yield (%)		Net gearing	Net cash/(debt)
					FY22E	FY23F	FY22E	FY23F		
Gamuda	July	BUY	3.59	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	1.48	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	0.415	0.67	11.1	14.4	2.6	3.7	4.2%	(RM69m)
WCT Holdings	Dec	BUY	0.425	0.86	6.2	6.6	0.6	0.6	73.3%	(RM2.78b)
Gabungan AQRS	Dec	BUY	0.30	0.56	6.8	9.2	1.7	1.7	29.6%	(RM144.8m)
Pintaras Jaya	Dec	BUY	2.33	3.14	33.0	26.1	4.1	6.4	-	RM82.2m
KKB Engineering	June	BUY	1.36	1.50	8.6	9.7	3.3	3.3	-	RM181.6m
Malayan Cement	June	BUY	2.12	3.00	8.7	9.8	-	-	57.9%	(RM3.32b)
Cahya Mata Sarawak	Dec	BUY	0.905	1.37	19.1	17.1	2.6	2.2	-	RM100.6m

Source: Company, MIDF Research

MIDF RESEARCH is part of MIDF Amanah Investment Bank Berhad (197501002077(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 (197501002077 (23878 – X)) for distribution to and use by its clients to the extent permitted by applicable law or regulation.

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 MIDF Investment believes are reliable at the time of publication. All information, opinions and estimates contained in this report are subject to change at any time without notice. Any update to this report will be solely at the discretion of MIDF Investment.

MIDF Investment 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. MIDF Investment and its affiliates and related companies and each of their respective directors, officers, employees, connected parties, associates and agents (collectively, "Representatives") shall not be liable for any direct, indirect or consequential loess, loss of profits and/or damages arising from the use or reliance by anyone upon this report and/or further communications given in relation to this report.

This report is not, and should not at any time be construed as, an offer, invitation or solicitation to buy or sell any securities, investments or financial instruments. The price or value of such securities, investments or financial instruments may rise or fall. Further, the analyses contained herein are based on numerous assumptions. This report does not take into account the specific investment objectives, the financial situation, risk profile and the particular needs of any person who may receive or read this report. You should therefore independently evaluate the information contained in this report and seek financial, legal and other advice regarding the appropriateness of any transaction in securities, investments or financial instruments mentioned or the strategies discussed or recommended in this report.

The Representatives may have interest in any of the securities, investments or financial instruments and may provide services or products to any company and affiliates of such companies mentioned herein and may benefit from the information herein.

This document may not be reproduced, copied, distributed or republished in whole or in part in any form or for any purpose without MIDF Investment's prior written consent. This report is not directed or intended for distribution to or use by any person or entity where such distribution or use would be contrary to any applicable law or regulation in any jurisdiction concerning the person or entity.

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