Thematic Report | Thursday, 06 April 2023

THEMATIC REPORT

Assessing the Impacts of Malaysia's Borders Reopening

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KEY HIGHLIGHTS

- **Services exports surged following borders reopening in Apr-22. It sustained a strong double-digit growth of +81.4%yoy (3QCY22: +77%yoy), gaining from the continued recovery in tourism sector with the increased number of foreign tourists' arrivals.**
- **As of Feb-23, passenger movements from China were up by +61.0%mom, with 49 inbound weekly flights (13% of 2019 levels).**
- **The increase in out-of-home and tourism activities creates opportunities for food and beverage producers with well-known household brand names that provide a variety of ready-to-drink beverages and snack-sized biscuits.**
- **The higher shopper footfall would increase tenant sales as tourist spend at malls which will underpin the positive rental reversion outlook at shopping malls and bodes well for earnings growth of retail REITs.**
- **The higher tourist arrival in 2023 will be slight positive to property sector as foreign buyers typically make up around 10%-15% of buyers account pre-pandemic.**
- **The full reopening of Malaysia's economy and borders has allowed contractors to ramp up their operations to higher capacity to catch up on work progress that was lost during the periods of movement control orders (MCOs).**
- **The recovery in plantation sector continues with the recent announcement that the labour shortage in oil palm plantations is about 80% sorted and approvals have been given to fully resolve the situation.**

ECONOMICS & POLICY

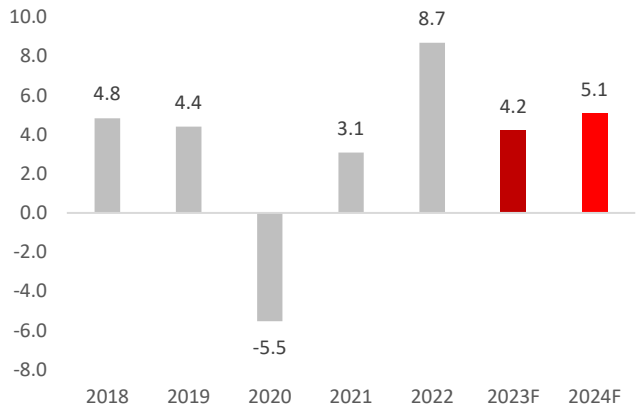
Services exports surged following borders reopening in Apr-22. Services exports sustained a strong double-digit growth of +81.4%yoy (3QCY22: +77%yoy), gaining from the continued recovery in tourism sector with the increased number of foreign tourists' arrivals. On a quarter-on-quarter basis, the services exports growth hit the peak point of +32.4%qoq in 2QCY22 and maintained a double-digit rate for 2HCY22. Moving forward, we foresee real exports of services to expand by +6.6% in 2023 (2022: +57.9%) and +12.5% in 2024. Global economic slowdown, elevated inflationary pressure and higher interest rate levels in many countries may limit the potential output of tourism activities across the globe. Nevertheless, reopening of China and removal of Covid-19 measures in many countries will uplift further tourism activities particularly in Malaysia.

Travel account returned to surplus in 3QCY22. Travel account has been contributing positively to Malaysia's current account prior to the pandemic crisis. The account has been on deficit since 2QCY20 until 2QCY22. With the reopening of Malaysia's international borders in Apr-22, the travel account returned to surplus value of +RM0.8b in 3QCY22 and improved further to +RM1.9b in the last quarter of last year. As a result, Malaysia's current account remained in surplus and increased to nine-quarter high at RM25.7b in 4QCY22. In terms of percentage to GDP, the current account rose to +5.5% (3QCY22: +3.1%). The steady improvement was due to smaller deficit ratio of services trade -1.8% of GDP (3QCY22: -2.1%), again thanks to improving tourism activities. We foresee services trade to gain further especially driven by the reopening of Japan's borders in Oct-22 and China in Jan-23. As global demand and elevated commodity prices maintained, goods trade to GDP ratio rose to +11.1% (3QCY22: +9.4%) while primary and secondary income ratio stayed in deficit. As for 2022, the current account ratio stood at +2.6%, the lowest since 2019. We forecast the current account ratio to rise to 3.00% for 2023. The

downward pressure is mainly on further deficit in primary income and stronger goods import growth. Moving forward, we view Malaysia's current account surplus shall rebound firmly, to be driven by steady exports revenue derived from elevated global commodity prices, firm regional demand and steady recovery in services trade primarily tourism activities.

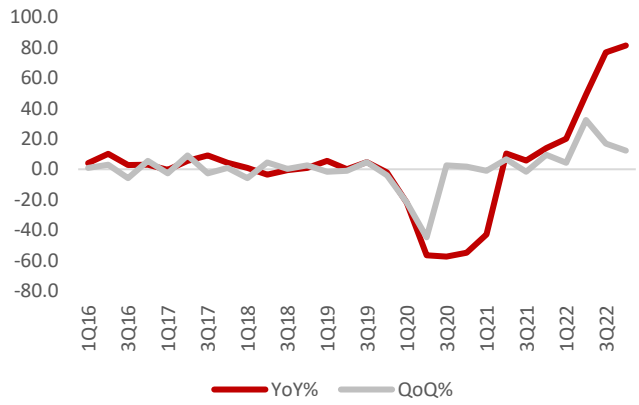
Malaysia's economy to expand by +4.2%, driven by firming domestic demand. Considering the external headwinds, global financial market uncertainties and tightening monetary policy in many economies, Malaysia's GDP growth is predicted to moderate to +4.2% in 2023. The softening growth is mainly due to a deceleration in external trade performances as global demand is anticipated to be slower than the previous year. The global economy is expected to slow down rather than recession in 2023. On the back of higher interest rates, banking turmoil and elevated inflationary pressure, domestic demand in the US and EU will likely to dampen in 2023. Consequently, Malaysia's real exports is projected to grow at +3% (2022: +12.5%), partially supported by improving services exports via recovering tourism activity. On a flip side, China's sooner-than-expected reopening provide a silver lining to global economy. The reopening would boost Malaysia's services exports as well as tourism activity. In addition, Malaysia's external trade is believed to continue benefiting from increased external demand for commodities especially palm oil, crude petroleum and LNG as the prices of CPO and Brent crude oil are projected to stay elevated at RM3,500 per tonne and USD85pb for 2023. With demand expected to continue growing, agriculture and mining sectors will record an expansion rate of +1% each, while manufacturing output to grow modestly by +2.7% for 2023.

Chart 1: GDP Growth Forecast (YoY%)



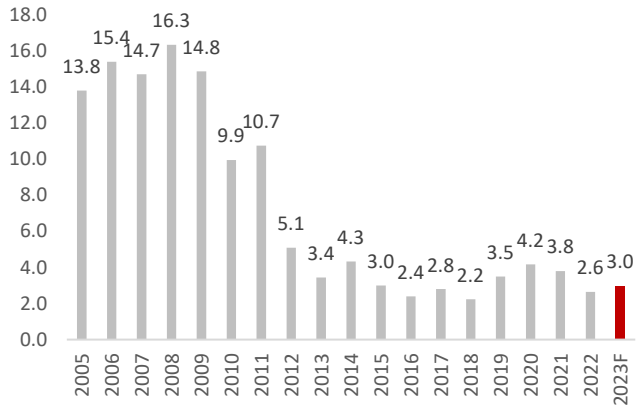
Source: Macrobond, MIDFR

Chart 2: Services Exports (YoY%)



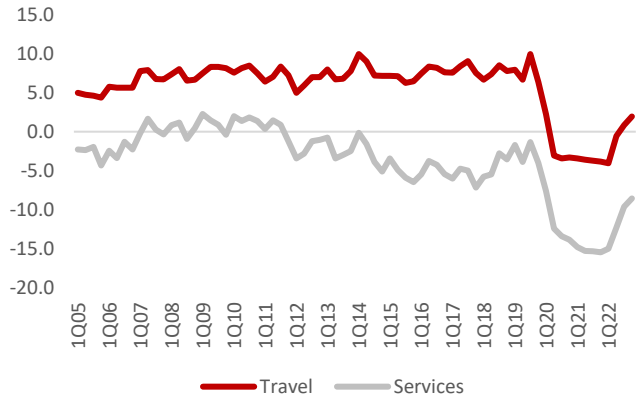
Source: Macrobond, MIDFR

Chart 3: Current Account Surplus (% of GDP)



Source: Macrobond, MIDFR

Chart 4: Services vs. Travel (RMb)



Source: Macrobond, MIDFR

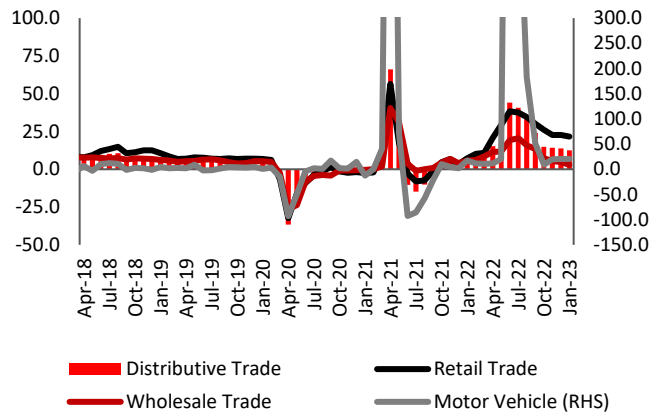
Consumer spending surged robustly. Despite concerns on inflation and therefore weaker purchasing power, retail spending looks strong. The latest data shows retail sales growing at +21.7%yoy in Jan-23, sustaining double-digit growth

for the 12th consecutive month. Even if we deflated the growth with consumer price inflation, the real growth in retail spending still recorded a double-digit surge since Apr-22 in line with the reopening of the economy (i.e. moving towards endemicity). Consumers increased their mobility and outdoor activities, increasing their spending even more after the uplifting of strict movement controls as the country transitioned into the endemic phase. In terms of value, the monthly retail sales in Jan-23 remained on upward trend and close to RM60b, having surpassed the pre-pandemic peak (of RM47.8b in Dec-19).

Supported by pent-up demand and policy support. Apart from the pent-up demand from revenge spending, the increase in spending last year was also boosted by policy measures such as EPF withdrawals, cash assistance from the government and savings accumulated from loan repayment moratorium given during the Covid-19 lockdowns. With the EPF withdrawals credited in Apr-22 the same month when the economy was reopened, this has also led to the surge in consumer spending from Apr-22 (+20.9%yoy; Mar-22: +10.8%yoy). The strength in retail spending, growing at the double-digit pace, has been sustained even until the recent month in Jan-23. Given the strong recovery especially after the economic reopening, real private consumption surged +11.3% in 2022 (2021: +1.9%).

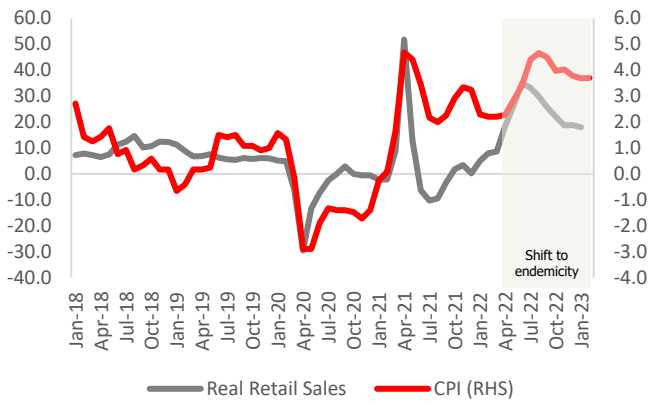
Inflation to ease. Inflation in Malaysia is projected to ease in 2023. We forecast for the price increase to slow to +2.5% (2022: +3.4%), considering better supply chain activity and relatively lower commodity prices (vis-à-vis the highs recorded to last year) will bring down supply-side pressures. This has been reflected in the easing PPI inflation, which turned to negative (-0.8%yoy) in Feb-23 as the decline in crude materials led to declines in cost pressures for the agriculture and primary industries as well as slower rise in PPI for manufacturing sector. Moreover, imported inflation would be more manageable on the back of stronger ringgit this year (average 2023f: RM4.20 vs. 2022: RM4.40).

Chart 5: Distributive Trade (YoY %)



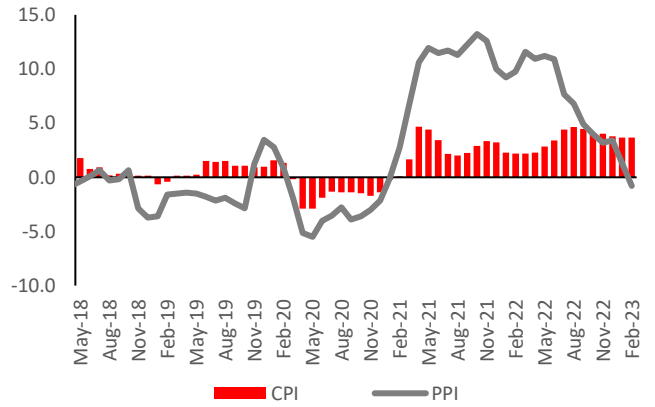
Source: Macrobond, MIDFR

Chart 6: Real Retail Spending vs. CPI (YoY%)



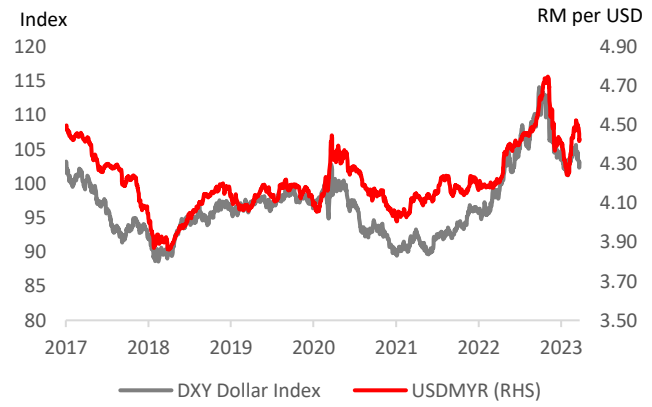
Source: Macrobond, MIDFR

Chart 7: CPI vs. PPI Inflation (YoY%)



Source: Macrobond, MIDFR

Chart 8: USDMYR vs. DXY Dollar Index



Source: Bloomberg, MIDFR

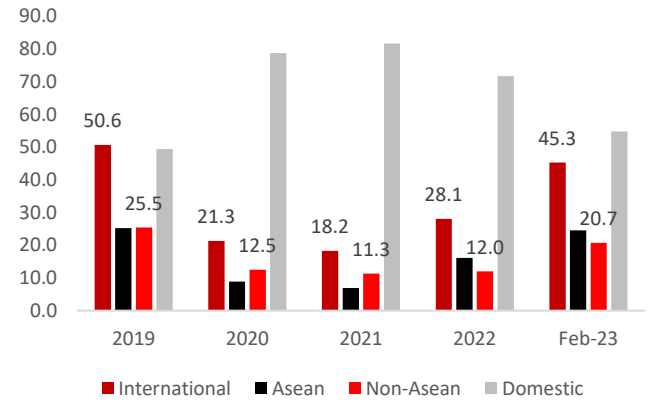
Airports passenger movement firm on recovery path. The second month of 2023 saw the international passenger movements registered at 2.6 million, approximately reaching 62.4% of Feb-19 levels. Due to seasonal factor, the end of year-end holidays also caused contractionary growth in the first two months. The passenger traffic declined by -6.1%mom, ASEAN tourists were down by -6.4%mom and non-ASEAN tourists declined by -5.7%mom. During the pre-pandemic, 50.7% of Malaysia's airports passenger traffic was contributed by international travels, 25.0% by ASEAN and 25.7% by non-ASEAN destinations. As of Feb-23, travellers for domestic destinations accounted for 54.7% (2022: 71.7%) vis-à-vis international destinations at 45.3% (2022: 28.1%), whereby 20.7% were non-ASEAN and 24.5% ASEAN. Moving forward, we expect airport passenger movements to improve in 2023 underpinned by borders reopening by China & Japan. The recovery towards 2019 level is still a long journey despite the reopening of Malaysia's international borders since last year. Our house view is that the earliest for passenger traffic to reach 2019 level will only be by 2024.

Table 1: Malaysia Airports: Passenger Traffic (Million)

Monthly International Passenger Movements, Million												
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
International												
2019	4.4	4.2	4.5	4.4	4.0	4.4	4.7	4.6	4.1	4.3	4.4	5.1
2022	0.3	0.3	0.4	0.6	1.0	1.3	1.6	1.8	1.9	2.1	2.2	2.9
2023	2.8	2.2										
CY22 % of CY19	6.1	6.4	9.1	13.2	25.6	29.4	35.0	37.9	46.5	48.9	50.9	55.6
CY23 % of CY19	62.5	62.4										
ASEAN												
2019	2.1	2.0	2.3	2.2	2.0	2.3	2.3	2.3	2.1	2.2	2.2	2.5
2022	0.1	0.1	0.2	0.3	0.6	0.8	1.0	1.1	1.2	1.3	1.3	1.7
2023	1.5	1.4										
CY22 % of CY19	5.2	5.3	6.9	12.4	30.0	35.1	43.7	47.7	55.0	60.6	58.7	66.4
CY23 % of CY19	70.6	69.6										
Non-ASEAN												
2019	2.3	2.2	2.2	2.2	2.0	2.1	2.4	2.4	2.0	2.2	2.2	2.6
2022	0.2	0.2	0.3	0.3	0.4	0.5	0.6	0.7	0.8	0.8	0.9	1.2
2023	1.3	1.2										
CY22 % of CY19	6.9	7.5	11.3	13.9	21.0	23.3	26.4	28.5	37.7	37.2	43.1	45.3
CY23 % of CY19	55.0	55.5										

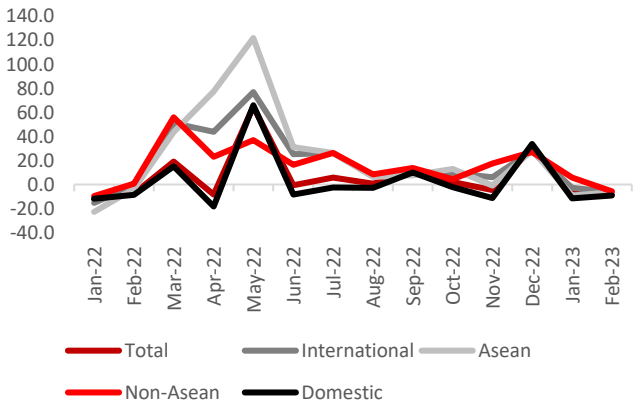
Source: MAHB, MIDFR

Chart 9: Passenger Movements by Citizens (Share %)



Source: MAHB, MIDFR

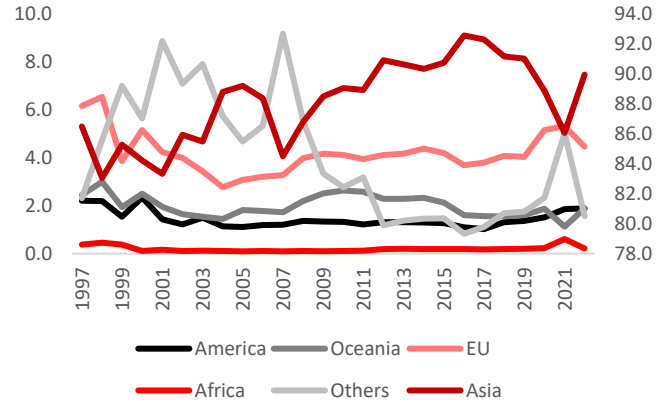
Chart 10: Airports Passenger Movements (MoM%)



Source: MAHB, MIDFR

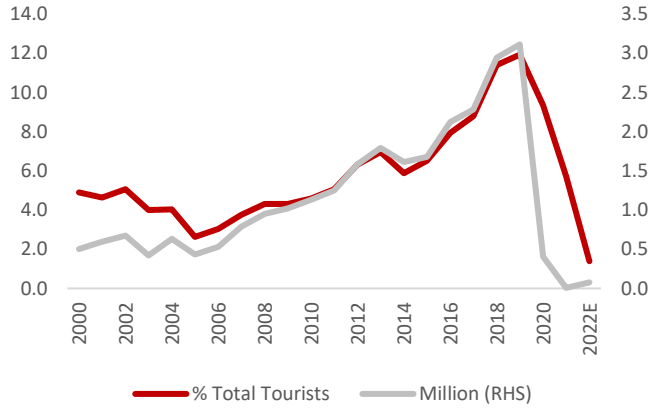
Chinese tourists to rally again. Prior to pandemic crisis, approximately 90% of the Malaysia's foreign tourists is from Asia. Close to 70% is ASEAN and another 20% non-ASEAN. Continents such as America, Oceania and Europe contribute less than 5%. In 2019, Chinese tourists' ratio to total foreign tourists hit its peak point at 11.9%, equivalent to 3.1 million persons. Long-term average growth rate of tourist's arrival to Malaysia from 2001~2019 is +5.9% per annum. Comparatively, the speed rate for Chinese tourists is 12.4% per annum. With the reopening of China's borders and removal of Covid-19 restrictive measures, we are optimistic the Chinese tourists will make a comeback and contribute positively to Malaysia's tourism sector. In fact, we are confident the Chinese tourists will breach the 3 million mark by 2024 especially with its population size and income growth potentials.

Chart 11: Tourist Arrivals by Region (% Share)



Source: TOURISM MALAYSIA, MIDFR

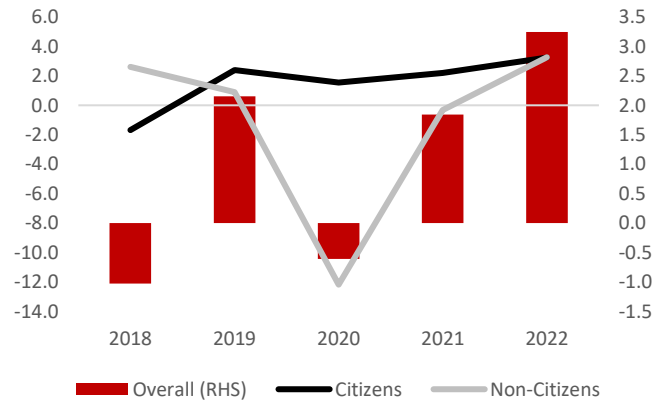
Chart 12: China Tourist Arrivals to Malaysia



Source: TOURISM MALAYSIA, MIDFR

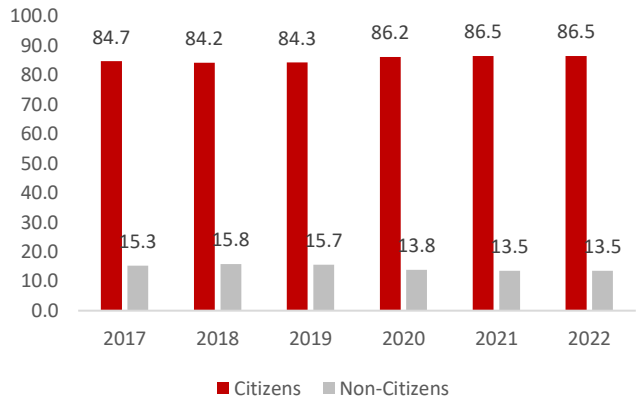
Non-citizens employment about 10% lower than pre-pandemic level. Throughout the pandemic years, we saw significant contractions of non-citizens, -12.3% in 2020 and -0.3% in 2021. In absolute value, almost 300K left the workforce. As Malaysia reopened its international borders in Apr-22, employment of non-citizens increased by +3.3% and 68.2K only. Employment of non-citizens is still -9.6% lower than its 2019 level while citizens employment registered +7.1% higher. We believe the move made by the government to ease the hiring process of non-citizens will spur higher employment growth and reduce overall jobless rate in 2023. The return of non-citizens is very likely positive for labor-intensive sectors, namely plantation, manufacturing and construction as mentioned in our thematic report Improving Labour Market Yet Structural Issues Remained.

Chart 13: Citizens vs. Non-Citizens Employment (YoY%)



Source: DOSM, MIDFR

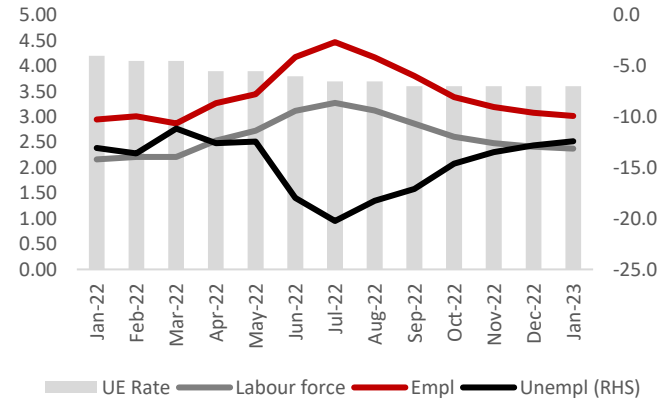
Chart 14: Citizens vs. Non-Citizens (% Total Employment)



Source: DOSM, MIDFR

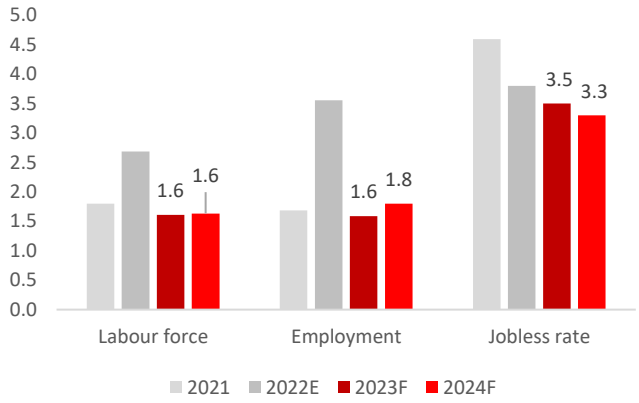
Jobless rate to descend further. Labour market in Malaysia is expected to strengthen further in 2023 and 2024 underpinned by continous upbeat momentum in domestic economy and modest expansion in external sector. We foresee Malaysia's unemployment rate to decline further to 3.5% in 2023 and return to pre-pandemic levels at 3.3% in 2024. In particular, the return of non-citizens workers is expected to boost overall employment and reduce jobless rate. As of 4QCY22, non-citizens employment is almost 10% lower than pre-pandemic levels. Steady expansion in primary sectors as well as construction and services will prop up more employment opportunities next year. Labour force and employment are predicted to expand at the range of +1.6~1.8%. As mentioned in our thematic report Positive Real Wage Growth to Continue Fueling Strong Consumer Spending, further improvement in labour market would strengthen consumer spending as wage receipients to employment ratio has reached a new peak at 64.5% in 2021, among others thanks to the higher minimum wage policy.

Chart 15: Labour Market Performances (%)



Source: DOSM, MIDFR

Chart 16: Labour Market Forecasts (YoY%)



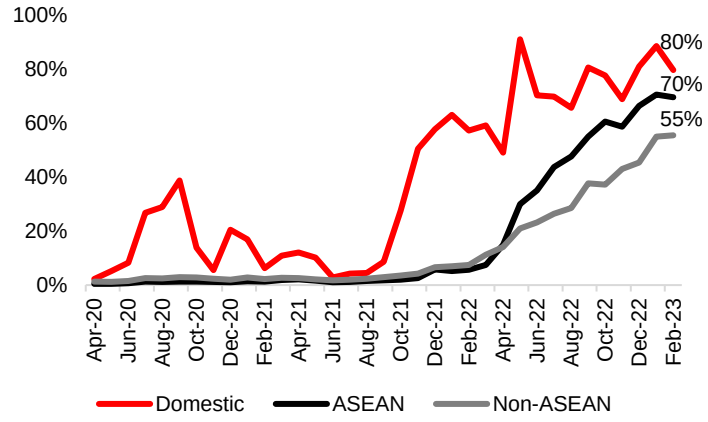
Source: DOSM, MIDFR

Spending outlook remains positive. Given the economy has been fully reopened, we foresee the outlook for domestic spending remains positive. As the economy is expected to continue to grow, a further rise in employment (and income) will support spending this year. Furthermore, easing inflation will pose less of a drag on consumer purchasing power. Government support such as cash assistance for the B40, income tax reduction for M40, continued spending on subsidies will also help the rakyat to face the challenge from rising cost of living. Moreover, the revival in tourist arrivals such as from China, Taiwan, and Japan will also support domestic trade, benefiting from the recovery in tourist spending.

SECTOR OUTLOOK

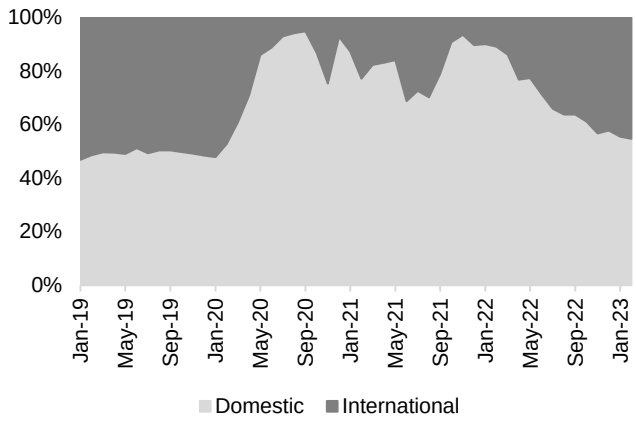
AVIATION .....Maintain NEUTRAL

Chart 17: Recovery of Passenger Traffic



Source: MAHB, MIDFR

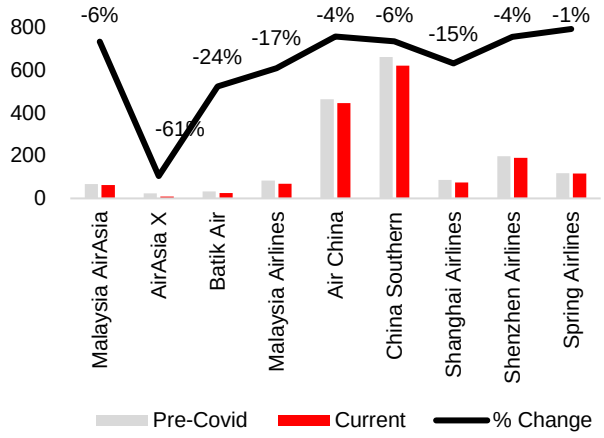
Chart 18: Passenger Mix



Source: MAHB, MIDFR

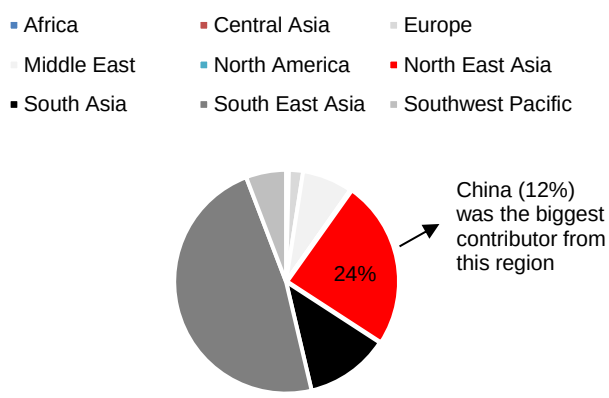
Recap of the past year. Since the interstate travel ban was lifted in Oct-21, domestic passenger traffic across the Malaysian airport network has been steadily recovering. Since Dec-22, it has been consistently at a healthy level 80% or above in comparison to the 2019 levels - corresponding to the recovery of weekly domestic seat capacity which had reached 79% in Feb-23. On the other hand, international passenger traffic started to record double-digit recovery since Apr-22, when Malaysia reopened its borders around the same time as neighbouring countries. It has been on an uptrend month by month, with a pandemic peak of 62% in Feb-23 (ASEAN: 70%, non-ASEAN: 55%). The recovery of weekly international seat capacity stood at 67% in Feb-23, with the non-ASEAN sector lagging behind due to the delayed reopening of key Northeast Asia markets such as China, Hong Kong, Taiwan, and Japan. These markets historically contributed approximately 20% to the international passenger traffic at KLIA. Nonetheless, the passenger mix between domestic and international sectors has been approaching the pre-pandemic level of a 50:50 breakdown, which is good news for the aviation players as it helps them rebuild their profitability. This is illustrated in Chart 18.

Chart 19: Operational Aircraft by Airlines



Source: Companies, planespotters.net, MIDFR

Chart 20: Int. Traffic 2019 by Sectors at KLIA



Source: MAHB, MIDFR

China's reopening's is undoubtedly a positive development for the aviation sector in Malaysia for two reasons: (i) the Chinese market used to account for approximately 12% of KLIA's international passenger traffic and (ii) Chinese tourists are known for their free-spending habits. We believe that the recovery of this sector is still in its early stages, as airlines are gradually increasing their flight offerings. As of Feb-23, passenger movements from China were up by +61.0%mom, with 49 inbound weekly flights (13% of 2019 levels). MAHB had previously set a target of increasing this to 64% of 2019 levels by end-1QCY23. We anticipate that the traffic recovery from this sector will become more significant in 2HCY23 as airlines reinstate capacities. There have been some challenges with short notice of reopening, as airlines serving the top 5 high-density routes, namely Beijing, Shanghai, Chengdu, Guangzhou, and Shenzhen, have downsized their number of operational aircraft as a result of the pandemic (refer to Chart 19). Only 5,907 additional seat capacity (+16.2%mom) was added for the China market in Jan-23 and +5.0%mom in Feb-23.

Outlook. The return of Malaysia AirAsia's (MAA) inactive aircraft in the upcoming months is anticipated to play a significant role in the recovery of passenger traffic, as the airline transported the majority of passengers (40%) prior to the pandemic. The recently launched MYAirline, which aims to increase its fleet size from 5 to 20 aircraft by end-CY23, will also help to some extent boost the domestic traffic through its network expansion. Meanwhile, the international traffic should improve as more foreign airlines restart or introduce their services across MAHB's network including the entry of Indonesia's TransNusa Airlines from Apr-23 onwards. There are currently 53 foreign airlines and 8 local airlines operating in Malaysia in 1QCY23, totaling to 61 airlines (84% of 2019 level) with the addition of Ethiopian Airlines and Air Arabia earlier this year. MAHB expects the total destination served within its network to recover to 79% of 2019 level by end-CY23 (end-CY22: 64%). Some positive factors supporting the local airlines include: (i) narrowing jet fuel crack spread, (ii) the expectation of a stronger MYR against USD and (iii) reasonable pricing of airfares. We expect passenger traffic to recover to 85% (domestic: 90%, international: 80%) this year. **Capital A (BUY, TP: RM0.91)** looks set to benefit from the improved fundamentals of the airline business as it targets to reach full utilisation of its fleet in 3QCY23. With the likelihood of turning profitable in FY24F, the market awaits its PN17 regularisation plan in 2QCY23.

CONSUMER..... Maintain POSITIVE

Riding the wave of out-of-home consumption. The reopening of international borders, particularly China and the lifting of Covid-19 measures in many countries is expected to boost tourism industry in Malaysia. With higher tourist arrival, out-of-home spending is expected to be higher. The uptick in tourism can significantly benefit retailers of general merchandise, and convenience store goods, as well as food and beverage producers. The growth in both domestic and foreign tourists to Malaysia will lead to higher traveller spending, which will be good news for local food manufacturers who provide packaged foods and snacks that are ready to eat and can be carried on buses, trains, or planes. As more people travel, particularly in countries with warm and humid climates like Malaysia, the demand for bottled water and isotonic drinks will likely rise which will benefit local beverage makers with well-known brands to achieve higher sales. Besides, retailers of general merchandise and convenience store would benefit from selling tourist-friendly merchandise like snacks, packaged foods, and ready-to-drink drinks to boost sales. Moreover, the surge in tourism is projected to increase demand for locally produced food and beverage items with unique, and authentic tastes that are attractive to tourists. Overall, the increase in out-of-home and tourism activities creates opportunities for food and beverage producers with well-known household brand names that provide a variety of ready-to-drink beverages and snack-sized biscuits, including **Nestle Malaysia (NEUTRAL, TP: RM139.50), F&N (BUY, TP: RM33.50), Hup Seng Industries (BUY, TP: RM0.88)** and **Spritzer (BUY, TP: RM2.80).** The increase in tourism could also be advantageous for general retailers like **Aeon Co (BUY, TP: RM1.90)** and convenience

store retailers like family mart under **QL Resources (BUY, TP: RM6.80),** as travellers could purchase beverages or snacks from the store.

Benefit from supplying products to hotels and restaurants. The influx of local and international tourists will increase demand for restaurants and hotels that cater for tourists. This will benefit well-known F&B producers as well as poultry producers who provide tourist-focused restaurants and hotels with large quantities of fresh chicken, isotonic drinks, bottled water, and cereal products. Additionally, the rise may increase demand for sourcing F&B manufacturers to create private-label names that could boost customer loyalty for the restaurant and hotel. Overall, we believe that well-known F&B producers with high production capacity such as **Nestle Malaysia (NEUTRAL, TP: RM139.50), F&N (BUY, TP: RM33.50)**, and **Spritzer (BUY, TP: RM2.80)** could benefit from the supplying products to tourist-oriented restaurants and hotels. **Leong Hup International (BUY, TP: RM0.90)** and **QL Resources (BUY, TP: RM6.80),** both of Malaysia's biggest poultry producers with economies of scale, could benefit from selling the restaurant and hotel a substantial quantity of fresh chicken at a competitive price.

Maintain POSITIVE. Overall, we are confident that the increase in tourists will support the consumer sector's top line. We continue to be optimistic about the consumer sector, underpinned by: (1) a stable labour market which could boost domestic consumption, (2) high tourist movement, which supports out-of-home consumption, and (3) better margins for F&B producers supported by the lower commodity prices and a stronger MYR. Given the inelastic demand for essential items, we continue to prefer consumer staple-related companies such as **QL Resources (BUY, TP: RM6.80), F&N (BUY, TP: RM33.50),** and **AEON (BUY, TP: RM1.90).** We prefer QL Resources on the back of the steady demand for marine and livestock products. We also like F&N because the company is likely to benefit from the rising demand for ready-to-drink beverages, which is being fuelled by an increase in tourist traffic. As for AEON, we believe that general merchandise stores (GMS) and supermarkets will continue to see solid sales in the near term, supported by strong domestic demand and an increase in tourist arrivals.

REIT.....Maintain POSITIVE

Higher tourist arrival supports earnings growth of retail REIT. The increased tourist arrival is expected to boost shopper footfall at malls which are tourist hotspots namely Suria KLCC, Pavilion KL, Mid Valley Megamall, The Gardens Mall and Sunway Pyramid. Note that tourist typically made up about 20%-30% to shopper footfall at malls in KL city centre pre-pandemic. Hence, with countries border reopened and tourist arrival expected to improve significantly to close to pre-pandemic level in 2023, we see that shopper footfall at malls would improve further. The higher shopper footfall would increase tenant sales as tourist spend at malls. That will underpin the positive rental reversion outlook at shopping malls and bodes well for earnings growth of retail REITs namely Pavilion REIT, IGB REIT, Sunway REIT and KLCCP Stapled Group.

Turnaround of hotel industry. As tourist arrival improving and expected to increase further in 2023, the hotel industry is anticipated to see further recovery. Hotel industry has been seeing improvement in occupancy rate and average room rate (ARR) since reopening of country border. With tourist arrival is anticipated to increase further in 2023, that will increase demand for hotel rooms and increase spending for F&B at hotels. As such, overall hotel industry is expected to see earnings recovery in 2023 due to higher ARR and higher income from F&B as well as event. In that context, REIT with exposure to hotel industry namely KLCCP Stapled Group and Sunway REIT should benefit from turnaround of hotel industry due to improving performance of Mandarin Oriental and Sunway hotels.

Maintain POSITIVE on REIT. The increasing tourist arrival is positive to REIT as it will support growth of retail and hotel industry in Malaysia. Overall, we are positive on earnings outlook for REIT in CY23 which offer decent average yield of 5.3%. Hence, we maintain **POSITIVE** on REIT with top picks are **IGB REIT (BUY, TP: RM1.86) and Sunway REIT (BUY, TP: RM1.73)**. We like IGB REIT due to high occupancy rates of Mid Valley Megamall and The Gardens Mall. We also like Sunway REIT as earnings from retail and hotel divisions is expected to remain solid in FY23 which will support earnings growth of Sunway REIT.

PROPERTY.....Maintain NEUTRAL

Higher tourist arrival a slight positive to property sector. The higher tourist arrival in 2023 will be slight positive to property sector as foreign buyers typically make up around 10%-15% of buyers account pre-pandemic. Hence, the return of tourist could support buying interest on property slightly particularly properties in Johor and KL which may see buying interest from tourist from Singapore and China. Note that property sales at Southern region of Malaysia improved following reopening of Malaysia's border. Nevertheless, we think that buying interest may still largely depend on the attractiveness of incentive for foreigners to purchase properties in Malaysia such as Malaysia My Second Home (MM2H).

Better outlook for property overhang in Malaysia. With marginally higher buying interest from foreigners, we think that could help improve property overhang in Malaysia slightly. According to data released by National Property Information Centre (NAPIC), residential overhang in Malaysia stood at 27,746 units in 2022, declining from 36,863 units in 2021. Johor has the highest residential overhang units of 6,089 followed by Selangor (6,095 units) and Penang (5,493 units). We think that buying interest from foreigner could further improve the residential overhang in Malaysia particularly states with higher overhang units namely Johor, Selangor and Penang.

Maintain NEUTRAL on property sector. Despite higher tourist arrival could help increase buying interest on property slightly, we see limited catalyst to property sector in the near-term. Hence, we maintain our **NEUTRAL** stance on property sector. We see that properties in the mid-market and affordable segment will continue to see resilient buying interest from property buyers as buyers look for properties that they could afford amid normalizing interest rate environment. Hence, we continue to favour companies which focus on affordable price range properties namely **Mah Sing Group (BUY, TP: RM0.75)** and **Glomac Berhad (BUY, TP: RM0.43)** due to their high exposure to mid-market and affordable homes segments.

CONSTRUCTION.....Maintain POSITIVE

Return of foreign labour. The full reopening of Malaysia's economy and borders has allowed contractors to ramp up their operations to higher capacity to catch up on work progress that was lost during the periods of movement control orders (MCOs). Contractors have previously been suffering from a labour shortage due to the repatriation of foreign workers during the peak of the pandemic in 2020 and 2021. The reopening has also allowed the gradual return of foreign workers that the industry is reliant upon and this is a diminishing problem for companies under our coverage. **Sunway Construction (BUY, TP: RM2.00)** for example, received 394 foreign workers in 2022 and has received the approval from the Human Resource Ministry for 300 more in Jan-23.

Higher value of work done. The ramping up of operations has translated into higher value of work done, which concurs with the figures published by the Department of Statistics Malaysia (DOSM). In 4Q22, the value of work done grew +15.7%yoy (3Q22: +%23.2%yoy) to RM32.0b (3Q22: RM30.5b), driven by civil engineering (37.9%), non-residential

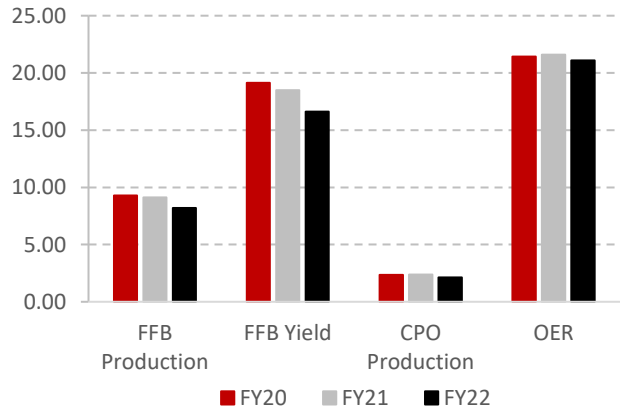
buildings (30.1%), residential buildings (21.8%) and special trade activities (10.2%). Overall in 2022, the construction sector rebounded 8.8% with a value of work done of RM121.9b, after two years of decline. It is notable that the value is still lower than what was achieved during the pre-pandemic period, which was RM146.4b in 2019, which can be attributable to the lower value and volume of jobs awarded in recent years. This should improve moving forward with the slew of infrastructure works and public utilities jobs that were announced during the revised Budget 2023 in Feb-23.

MRT3 to generate excitement. We bank on the upcoming MRT3 to be the mega project that will give the construction sector a boost this year. We expect the main packages of the rail project to be awarded by 2H23, considering the current review on the project to reduce its cost by 10% to RM45b. Coupled with the gradual return of foreign workers to Malaysia, there should be no issues in terms of manpower when the MRT3 project kick starts. Industry players may be affected the rise in steel bar prices alongside the rise in prices of iron ore but we expect it to only be a short-term problem as the authorities from China has committed to curb the speculation in prices and also to cut down on the country's crude steel production, which should ease the tight demand of iron ore. Our top picks for the construction sector are **Gamuda (BUY, TP RM5.04), Sunway Construction (BUY, TP: RM2.00)** and **IJM Corp (BUY, TP: RM1.90),** due to the robustness of their balance sheets and their strong overseas presence.

PLANTATION.....Maintain NEUTRAL

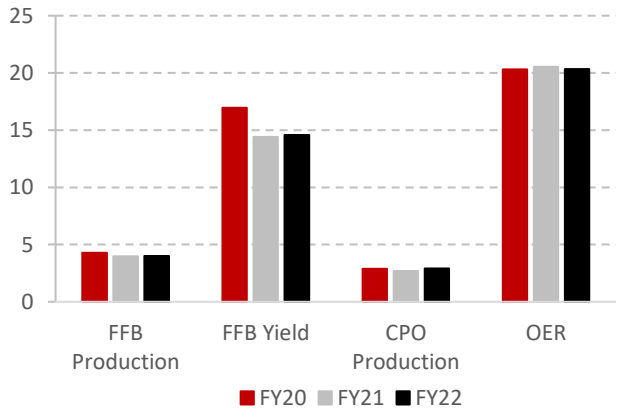
Return of the foreign labour. It seems the recovery in plantation sector continues with the recent announcement that the labour shortage in oil palm plantations is about 80% sorted and approvals have been given to fully resolve the situation. In summary, plantation yield dropped and Malaysia has lost out on an estimated RM20b in revenue in CY22, according to the Ministry of Plantation & Commodities. On the ground, the planted area, FFB and Oil Yield declined by -1.1%yoy, -1.6%yoy, and -1.5%yoy, respectively, to 5.6m ha, 3.05 tonne/ha, and 19.70 tonne/ha due to the scarcity of 63,000 foreign labours. Nonetheless, the PO contribution to Malaysia's KDNK remained high to RM46.0m grew by +2.3%yoy this was well supported by an increase of average CPO price which traded at RM5,125.6/tonne (+16.0%yoy) amid higher export value and volume of RM137.b (+27.1%yoy) and 26.5m tonne (+4.3%yoy).

Chart 21: Sime. Plant Operational Performances



Source: MIDFR

Chart 22: FGVH Operational Performances



Source: MIDFR

Beneficiary for huge landbank players. Narrowing down to the company level, this will positively benefit those with a huge landbank players i.e. Sime. Plant & FGVH, since they are top 2 companies that possessed high oil palm planted areas. Comparatively, Sime. Plant has the biggest landbank and planted area accounted for 744,630 ha and 579,708 ha (78% planted area) while FGVH had 453,885 ha landbank with approximate of 336,315 ha planted area (74% planted area). Both

companies equipped with 80,041 and 26,973 plantation workers, where foreign workers stood out around 59.7% and 82.3% of total workers.

Based on 4QCY22 result, we've seen the arrival of foreign workers lift the operational CY23 outlook, where Sime. Plant was only shortage of 2,468 workers while FGV managed to reduce the labour shortage to 13% (FY21; 32%). Nonetheless, on the full year basis, the setbacks in upstream activities last year remain, resulted productivity in FFB & CPO production, FFB yield, oil extraction rate for Sime. Plant fell by -10% &-10%, -10% and -2% respectively. In contrast, FGV operational has marginally stable as FFB & CPO production, FFB yield and OER improved to 3.99m Mt (+0.3%yoy) & 2.90 Mt/ha (+8.0%yoy), FFB yield 14.57 Mt/ha (+1.0%yoy) and 20.35% (-1.0%yoy).

Outlook. Based on MPOB data, we have seen Malaysia production recovery is on track, as February data showed that production improved to 1.25m tonne (-9.4%mom; +10.0%yoy; +10.1%Ytd) versus 1.14m tonne in prior year supported by contribution from most of the states except for Negeri Sembilan (-1.0%yoy), impacted by uneven weather events of the month. In addition, the average FFB yield continued to rise by +8.7% year-on-year to 1.07 t/ha, while OER inched lower to 19.24% following subdued mills operational on low cycle months, but performance was relatively stable backed by improving foreign labour inflow. We maintain that for 2QCY23, performance will continue to improve since palm trees pollination cycle is now at a tail end and there will be fewer wet days, aided by return of foreign labour shortage (which is now 80% resolved). As a result, an increase +23%qoq to 4.82m tonne is imminent based on our assumption. We maintain **NEUTRAL** call on the sector with average CPO target price of RM3,500 for CY23.

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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