Building Materials

Outlook Remains Lacklustre

UNDERWEIGHT

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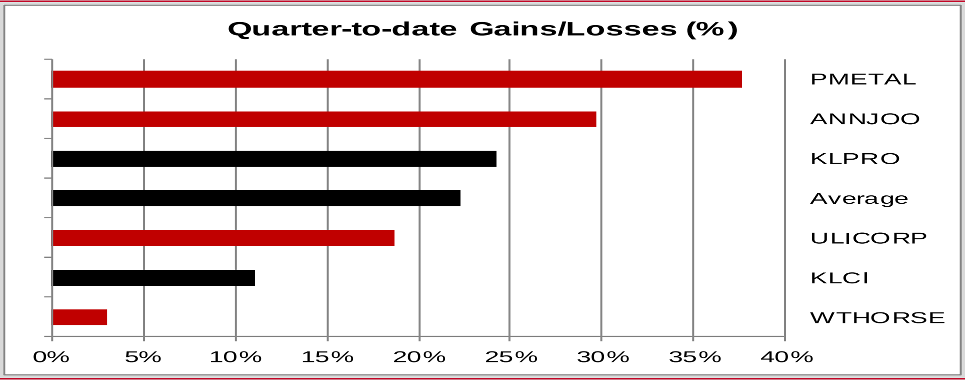
In view of continued softer demand, higher raw material and production cost and depressed margin on intensified competition, we remain UNDERWEIGHT on the Building Materials sector. In addition, the expected COVID19-led economic slowdown and sluggish business confidence are piling more pressures on the sector, especially for the long and flat steels as well as ceramic tiles sub-sectors. However, we believe aluminium prices have already bottomed out and a V-shape recovery is possible once COVID19 subsides, based on the 2008 financial crisis scenario. As such, PMETAL should enjoy better earnings prospects next year on aluminium price recovery. In addition, new +42% new capacity next Jan and potential logistic cost savings should propel its earnings to new heights.

Below expectation. Overall, for 1QFY20, only PMETAL performed broadly within our expectations, with the remaining 3 counters coming in below our expectations. The deviations were mainly as follow:- (i) ANNJOO - lower-than-expected sales tonnage and manufacturing margin, (ii) ULICORP – lower-than-expected margin achieved, and (iii)WTHORSE- lower-than-expected sales and profit margin.

Quarter-to-date share price performance review. During 2QCY20, as at our report cut-off date of 30/6/2020, the Industrials Product Index had rebounded 24%, outperforming FBM KLCI return of +11%. The improved market sentiment was buoyed by: (i) hopes on business recovery post economic re-opening, (ii) potential revival of mega infrastructure projects, and (iii) market technically rebounding from oversold position due to political change and outbreak of Covid-19.

2QCY20 Gains/ Losses (%)



Source: Bloomberg

Gradual recovery expected but outlook remains lacklustre. Post economic re-opening, following the resumption of construction activities, property development projects and raw material's supply chain, we expect the industry to recover gradually from 3QCY20 onwards. However, (i) weak selling price, (ii) oversupply and intense competition situation, (iii) softer market demand resulting from slower construction and property development activities, (iv) higher raw material and production cost, and (v) economic slowdown remain the downside risk to the industry. Hence, we opine that CY2020 remains a tough year for the building material sector until we see increased investment on infrastructure project, revival of mega project, or recovery in property development activities.

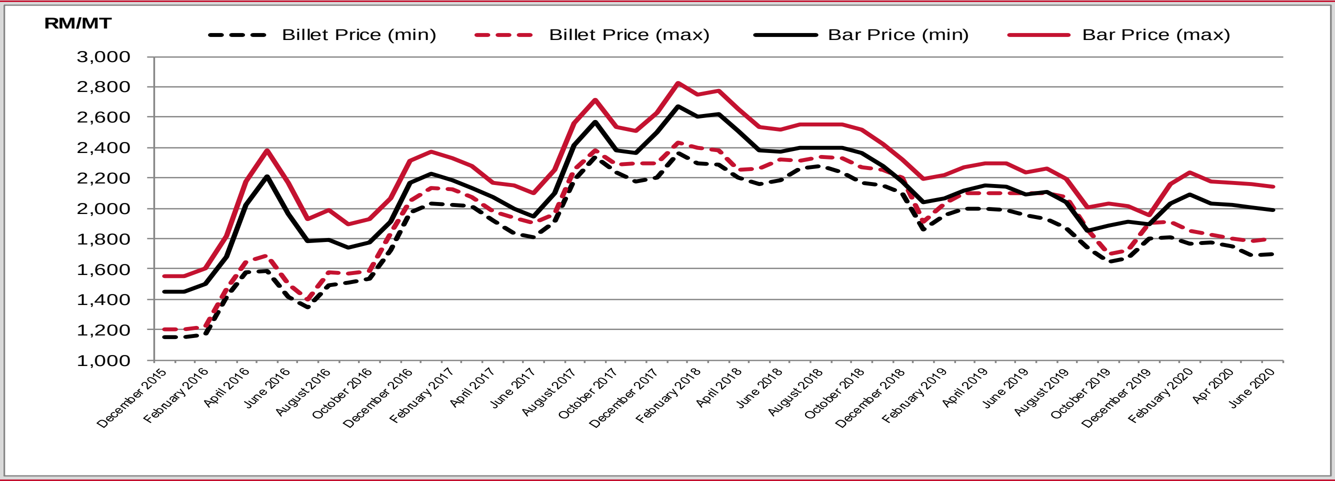
Long Steel

China steel vs. Malaysia steel. As of the report cut-off date, China domestic steel rebar traded at c.RM2,200/MT (excluding import duties, safeguard measure and transportation costs) compared to the domestic average steel price of c.RM2,000/MT. The China steel price has been rebounding recently following the resumption of the construction activities across the country. Moving forward, we think the price trend remains strong, boosted by government economic stimulus packages and huge investment in supporting infrastructure development. With the current price gap, we believe the risk from imported steel to Malaysian players remain low as the domestic price is more attractive and the steel demand in China is stronger than our domestic market demand.

Challenging outlook ahead. Although the steel industry was picking up its momentum in early CY2020, unexpected changes in political environment and outbreak of Covid-19 disrupted the steel demand and ANNJOO's business operation. We expected to see a sharp decline in steel demand for 2QFY20, but gradual recovery after the business resumed its operation in May 2020. Future outlook remains uncertain in view of (i) slower construction and property development activities, (ii) oversupply of steel in domestic market, (iii) increase in iron ore prices (from USD80/DMTU to USD100/DMTU) affected by the disruption in global supply chain due to ongoing Covid-19 cases in Brazil and Australia as well as high demand from China. However, slight recovery in average selling price (from RM1,900/MT to above RM2,000/MT) will help to ease the margin pressure. Besides, we are encouraged by ANNJOO's strategy to increase steel export to oversea market in boosting sales tonnage and gaining tax incentive from increasing export.

All in, we maintain **UNDERPERFORM** call on ANNJOO with unchanged TP of **RM0.550** based on P/BV of 0.26x (at minus 2SD) pegged to FY20E BV/share of RM2.11, which we believe is justified due to: (i) depressed ASP of rebar steel, (ii) weaker domestic and international demand, and (iii) higher raw material cost.

Long Steel Prices



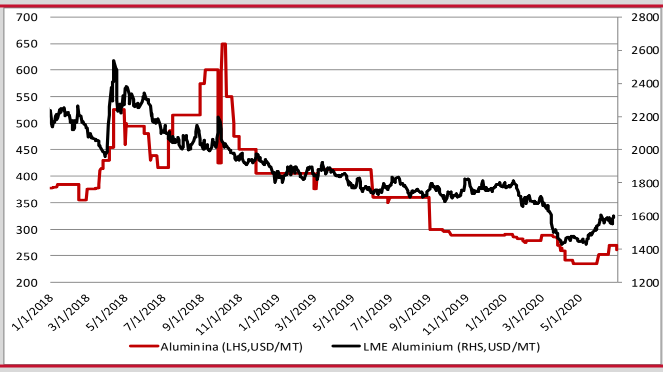
Source: MITI,Kenanga Research

Aluminium

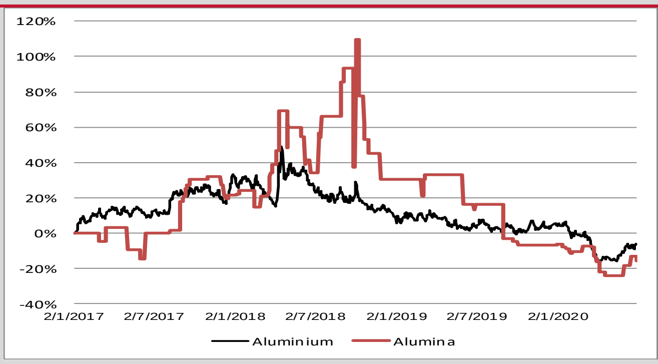
Aluminium prices have bottomed out. The LME aluminium price fell 9% to a 3-year low of USD1,658/MT within 10 days from above USD1,800/MT after the Covid-19 spread turned pandemic in end-Feb but it recovered to above the USD1,700/MT-level briefly before diving back to below USD1,600/MT-level currently (-10% YTD). In this depressed business environment, prices are expected to remain volatile but we believe prices should have bottomed out. Based on the last financial crisis in 2008-2009, aluminium price plunged sharply by 62% from a peak of USD3,271/MT on 11 Jul 2008 to USD1,252/MT on 23 Feb 2009 but it formed a V-shape recovery to end the year of 2009 at USD2,197/MT. As such, the fall in aluminium price of late is not alarming as when the pandemic subsides, price is likey to recover swiftly, in our opinion.

Alumina cost remains moderated. Alumina prices also fell 10% YTD to RM261.5/MT from USD289/MT while the percentage of aluminia cost to aluminium price is also within the usual range of 16%-17% from 16.2% at the beginning of the year. YTD, the alumina price as a percentage to aluminium price is averaging at 16.6% which is still within the normal range, against average of 19.9% in FY19 and 22.0% in FY18. Should it maintain at current level, profit margin is likely to improve further from the past two years. Meanwhile, the upstream acquisition of two supply chain refineries will ensure raw material supply certainty while the acquisition of PT Bintan has enabled transportation cost savings.

Aluminum vs. Alumina Prices

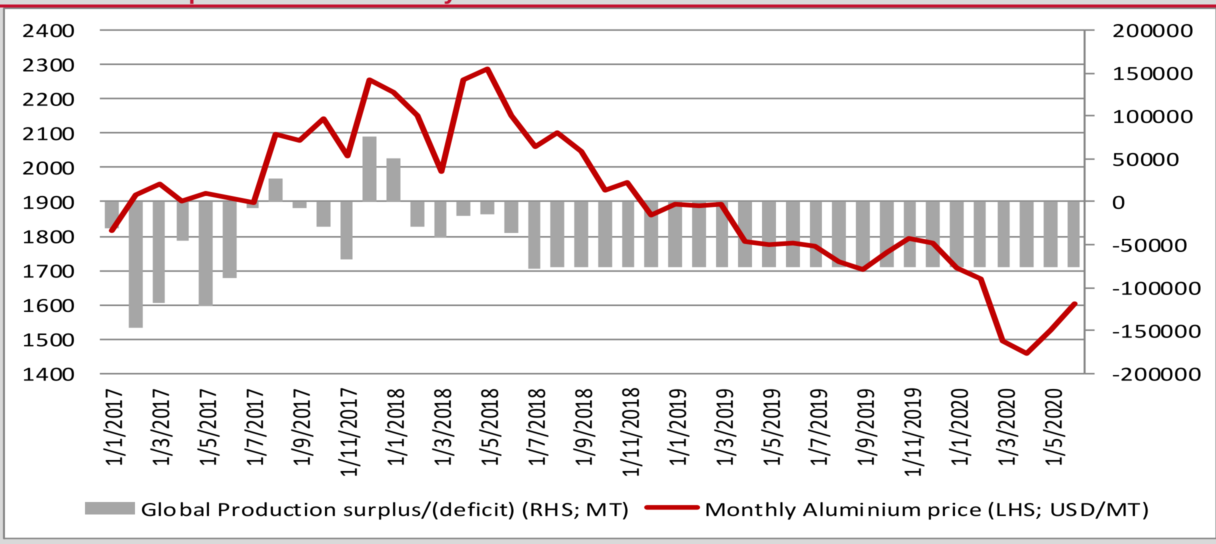


Aluminum vs. Alumina Prices – % Movement



Source: Bloomberg, Kenanga Research

Global Production Surplus/Deficit vs. Monthly Aluminium Price



Source: Bloomberg, Kenanga Research

Keep MARKET PERFORM on PMETAL. From the 52-week low of RM2.85 during the peak of market meltdown in mid-March, share price of PMETAL has recovered sharply by 59% on the back of robust market sentiment together with the recovery of aluminium prices. With the view that aluminum prices should have bottomed out, and coupled with economic activities resumption, we should see a seasonally strong 2HFY20. Nonetheless, we believe its recent strong share price performance has already priced in near-term positives. Going forward, we remain upbeat on its FY21 prospects on the back of the recovery of aluminium prices, potential logistic cost savings as well as the additional smelthing capacity of 42% to come on-stream next Jan which will propel its earnings to new heights. We keep MP rating on PMETAL with unchanged TP of RM4.45 which is based on 3-year PBV mean of 1.37x.

Flat steel

Uninspiring outlook. Moving forward, the outlook remain challenging in view of: (i) weak prospects in construction industry, dragged by less construction projects and slower work progress, (ii) stiff competition from other players, (iii) higher operational cost such as labor and administrative expenses, and (iv) slower economic growth continuing to drag performance.

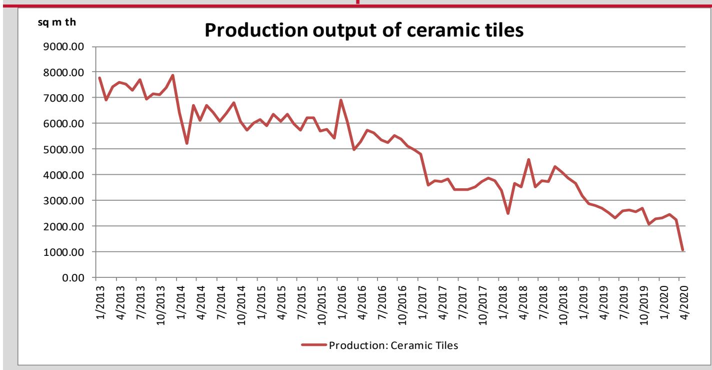
Hence, we reiterate **UNDERPERFORM** on ULICORP with unchanged TP of **RM0.250** based on Fwd. P/BV of 0.19x applied to FY20E BV/share of RM1.30, which is at 1SD below mean, in line with the lacklustre sentiment on the sector and challenging operating environment.

Tiles

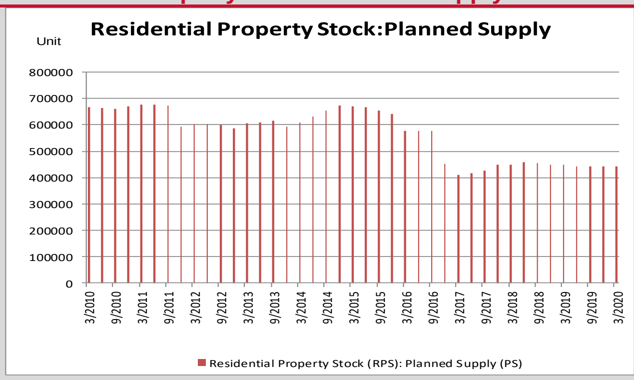
Sluggish demand. YoY, ceramic tiles production volume has continued to drop, by 30%, compared to a year ago, mainly impacted by: (i) the slowdown in the construction and property industry, and (ii) business disruption due to MCO implementation. Moving forward, property developers remain cautious with their new launches in view of the glut in the domestic market and uncertain economic environment. Overall, we expect the tiles industry to remain unexciting until there is a visible recovery in the property market.

Maintain **MARKET PERFORM** on WTHORSE with unchanged Target Price of **RM0.740** based on unchanged 0.31x Fwd. PBV (which is at the current trough level) pegged to FY21E BV/share of RM2.39. We believe this is justified due to the followings; (i) the company has been in loss-making position since 2QFY18, and (ii) slower pace in the construction and property development sectors.

Ceramic Tiles Production Output



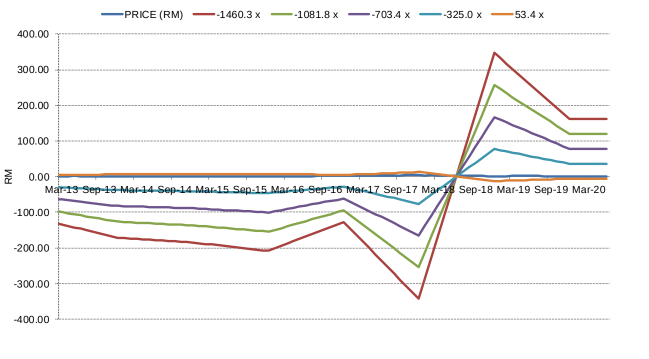
Residential Property Stock: Planned Supply



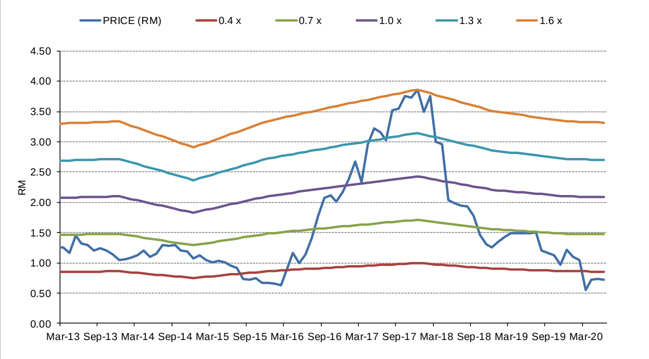
Source: CEIC, Kenanga Research

APPENDIX

ANNJOO – Fwd PER Band

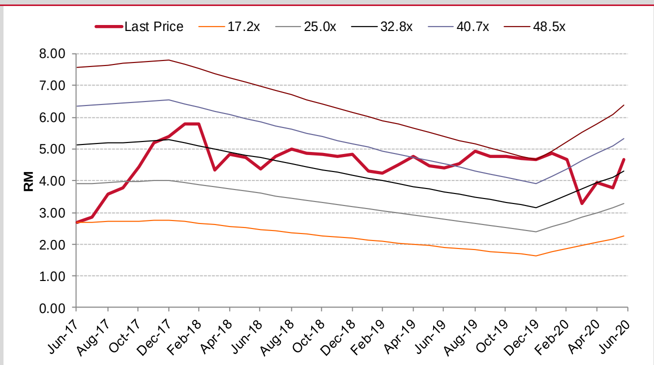


ANNJOO - Fwd PBV Band

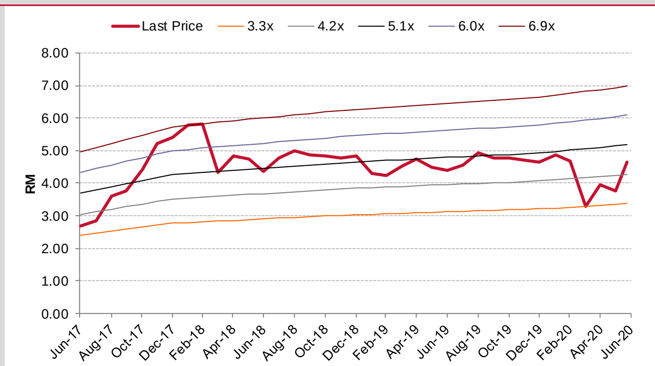


Source: Company, Kenanga Research

PMETAL – Fwd Core PER Band

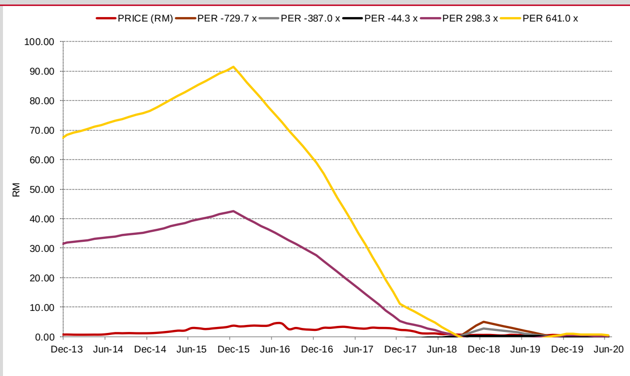


PMETAL - Fwd PBV Band

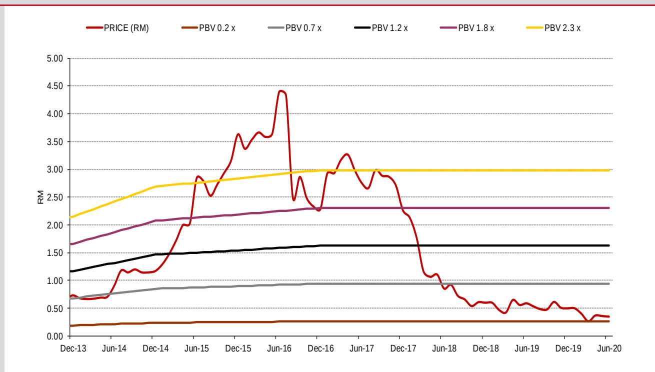


Source: Company, Kenanga Research

ULICORP – Fwd Core PER Band

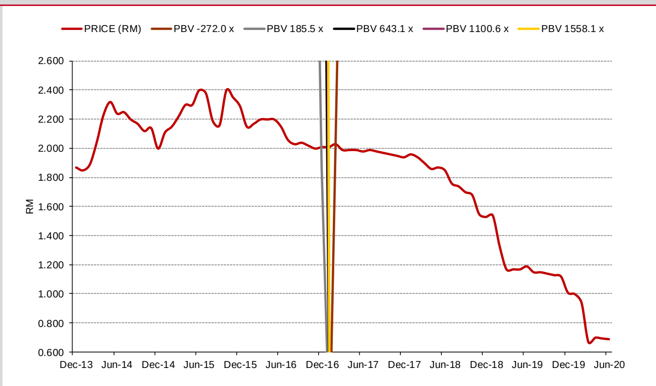


ULICORP - Fwd PBV Band

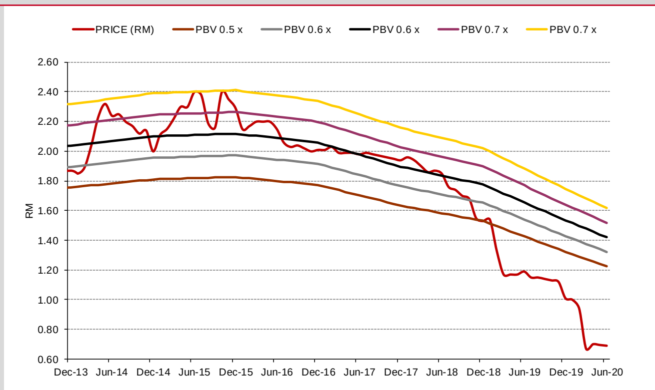


Source: Company, Kenanga Research

WTHORSE – Fwd Core PER Band



WTHORSE - Fwd PBV Band



Source: Company, Kenanga Research

Peer Comparison

Name	Last Price @ 30 June 2020 (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth 1-Yr. Fwd.	Revenue Growth 2-Yr. Fwd.	Core Earnings Growth 1-Yr. Fwd.	Core Earnings Growth 2-Yr. Fwd.	PER (x) - Core Earnings Hist.	PER (x) - Core Earnings 1-Yr. Fwd.	PER (x) - Core Earnings 2-Yr. Fwd.	PBV (x) Hist.	PBV (x) 1-Yr. Fwd.	ROE (%) 1-Yr. Fwd.	Net Div.Yld. (%) 1-Yr. Fwd.	Target Price (RM)	Rating
BUILDING MATERIALS UNDER COVERAGE																	
ANN JOO RESOURCES BHD	0.720	388.5	Y	12/2020	-10.4%	12.4%	-146.9%	-121.7%	N.A.	N.A.	N.A.	0.3	0.3	-5.1%	0.0%	0.550	UP
PRESS METAL ALUMINIUM	4.53	18,292.6	Y	12/2020	-17.1%	28.5%	-24.4%	74.0%	26.9	32.2	19.9	5.0	4.7	10.3%	0.8%	4.45	MP
UNITED U-LI CORP BHD	0.350	76.2	Y	12/2020	-5.3%	3.0%	-80.0%	66.7%	N.A.	175.0	175.0	0.3	0.3	0.1%	0.0%	0.250	UP
WHITE HORSE BHD	0.690	157.1	Y	12/2020	-5.4%	3.9%	-182.8%	-177.4%	N.A.	N.A.	N.A.	0.2	0.3	-8.6%	0.0%	0.740	MP
Simple Average					**-9.5%**	**11.9%**	**-108.5%**	**-39.6%**	**26.9**	**103.6**	**97.5**	**1.5**	**1.4**	**-0.8%**	**0.2%**		

Source: Bloomberg, Kenanga Research

Stock Ratings are defined as follows:

Stock Recommendations

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

*******Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.***

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