3QCY22 Investment Strategy

Inflation Posing Challenges, But Opportunities Beckon

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FBMKLCI	
Current	Target
1,456.74	1,610 ↓

Summary

- **We reduce our end-2022 FBM KLCI target to 1,610 pts (from 1,670 pts) based on 16x our 2022F earnings projection (-4.7%) against a backdrop of a considerably more aggressive monetary tightening by major policy makers globally in recent months.**
- **With inflation seemingly spinning out of control, policy makers have no choice but to make reining in inflation their top priority by raising rates and embarking on quantitative tightening, inevitably at the expense of growth (or even driving the global economy into a recession) and asset prices.**
- **While EM assets generally do not do well during a rate hike cycle in the US, we see an exception this time around as the current US rate hike cycle coincides with a super boom in commodity prices, which augurs well for the generally commodity export dependent EM. Also, EM now appears a safer bet vs. Europe given the Russia-Ukraine war situation.**
- **Within the EM space, there has been a shift in focus away from China (on the heels of regulatory crackdowns, a tech selloff, an ineffective zero Covid-19 policy and an ambiguous stance in the Russia-Ukraine war) while Russia has been completely removed from MSCI EM Index in the wake of the war. These have resulted in a corresponding rise in weighting for other countries in the index, including Malaysia.**
- **Under the current sustained high inflation scenario, we believe investors should seek refuge in stocks of companies with strong pricing power. We acknowledge that these are rare in our market, but we believe there are no lack of "near-proxies" for pricing power, which we define as "companies that are able to maintain their margins despite the rising cost pressures".**
- **We see them in: (1) Service-based industries that have kept wage pressures at bay, i.e. Banks and Telecommunications players; (2) Suppliers to multinational companies with pricing power, predominantly in the tech/consumer electronics space (which means there are less cost pressures to be passed on along the supply chain), i.e. local players in the fields of Outsourced Semiconductor Assembly and Test (OSAT), Automated Test Equipment (ATE) and Electronics Manufacturing Services (EMS); and (3) Providers of goods/services with a low "price elasticity of demand" such as Private Healthcare.**
- **We also like commodity producers, i.e. strong names in the Plantation and Oil & Gas space as we expect CPO and crude oil prices to stay elevated in 2H 2022. We hold the view that the time is about right for investors to position themselves in Construction stocks ahead of the 15th General Election (GE15).**
- **Our Overall Top Picks are MAYBANK, PCHEM, IHH, KLK, RHBBANK, DIGI, INARI, GAMUDA, ABMB and PIE.**
- **Our Top Shariah Picks are PCHEM, IHH, KLK, DIGI, TM, INARI, GAMUDA, TAKAFUL, BPLANT and PIE.**

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End-2022 FBM KLCI Target of 1,610 pts

We reduce our end-2022 FBM KLCI target to 1,610 pts (from 1,670 pts) based on 16x our 2022F earnings projection (-4.7%). This is at a discount to its 5-year historical average of 18x to reflect:

1. The inevitable deflation in asset prices across the board against a backdrop of a considerably more aggressive monetary tightening by major policy makers globally in recent months;
2. The heightened risk of the global economy slipping into a recession/stagflation if major policy makers globally fail to tame the inflation with their existing measures and have to prescribe stronger medicine which will inflict even greater collateral damage to global growth; and
3. FBM KLCI earnings in 2022 being weighed down by the windfall/prosperity tax dubbed *Cukai Makmur*.

Monetary Tightening Amidst Sustained Elevated Inflation

Living and investing with inflation. We hold the view that inflation is here to stay globally in 2H 2022. While it appears that the Covid-19 pandemic is coming to a close in most parts of the world (other than China), global supply chain disruptions—a key factor that has stoked the inflation—are still far from over. Adding fuel to the inflation fire, are the now seemingly prolonged war in Ukraine and hence the corresponding sanctions on Russia (both countries are key exporters of oil & gas, metals and grains to the rest of the world), and the intermittent Covid-19 outbreaks in China and the resulting lockdowns driven by its Covid-zero policy.

With inflation seemingly spinning out of control, policy makers have no choice but to make reining in inflation their top priority by raising rates and embarking on quantitative tightening, inevitably at the expense of growth (or even driving the global economy into a recession). Asset prices (particularly for bonds, equities and alternative assets such as crypto-currencies), which were buoyed by an ultra-loose monetary policy in recent years, are now experiencing a major reversal. These make the investing environment extremely challenging for the remainder of 2022 (probably well into 2023 as well).

Already, equity markets globally took a severe beating in 1H 2022 as the Fed embarked on a new rate hike cycle in March 2022, ended its quantitative easing (QE) programme in the following month, and initiated quantitative tightening (QT) in June 2022. During 1H 2022 (at the close on 17 June 2022), US Dow Jones, S&P 500 and Nasdaq 100 indices fell 17.8%, 22.9% and 31.0% respectively, while MSCI EM index contracted 18.5%. Amidst all the gloom and doom, the local equity market turned out to be surprisingly resilient with the bellwether FBM KLCI Index only easing 7.1% (thanks to strong performance coming largely from the banking and plantation sectors, partly also underpinned by the return of foreign investors on favourable EM index weighting rebalancing).

A steep rate hike cycle. In the current new rate hike cycle, the Fed has thus far raised the target range for the Fed Funds Rate by 150 bps to 1.50%-1.75% from 0.00%-0.25%, comprising a 25-bp hike, a 50-bp hike and a 75-bp hike in March, May and June 2022, respectively. The latest Fed Funds futures indicates that the market expects the Fed to hike another 75 bps during the Federal Open Market Committee (FOMC) meeting in July 2022, with two more 50-bps hikes in September and November 2022, respectively, followed by two 25-bps hikes in December 2022 and February 2023, before pausing at 3.75%-4.00% (see Exhibit 1).

In other words, the market, taking the cue from the latest narrative of Fed Chair Powell, is projecting a 375-bps rise in Fed Funds Rate, from 0.00%-0.25% to 3.75%-4.00%, within a short span of 12 months. This compares with an actual 225-bps hike, from 0.00%-0.25% to 2.25%-2.50% over 37 months during the previous rate hike cycle in 2016-2019.

Across the Atlantic, similarly, European Central Bank (ECB) is poised to raise its deposit rate—for the first time in more than a decade—by 25bps from -0.5% to -0.25% in July 2022, and has signaled potentially a bigger move in September 2022 "if the medium-term inflation outlook persists or deteriorates". It will also put an end to its long-standing bond-buying programme from 1 July 2022.

Exhibit 1: Fed Funds Rate Probabilities#

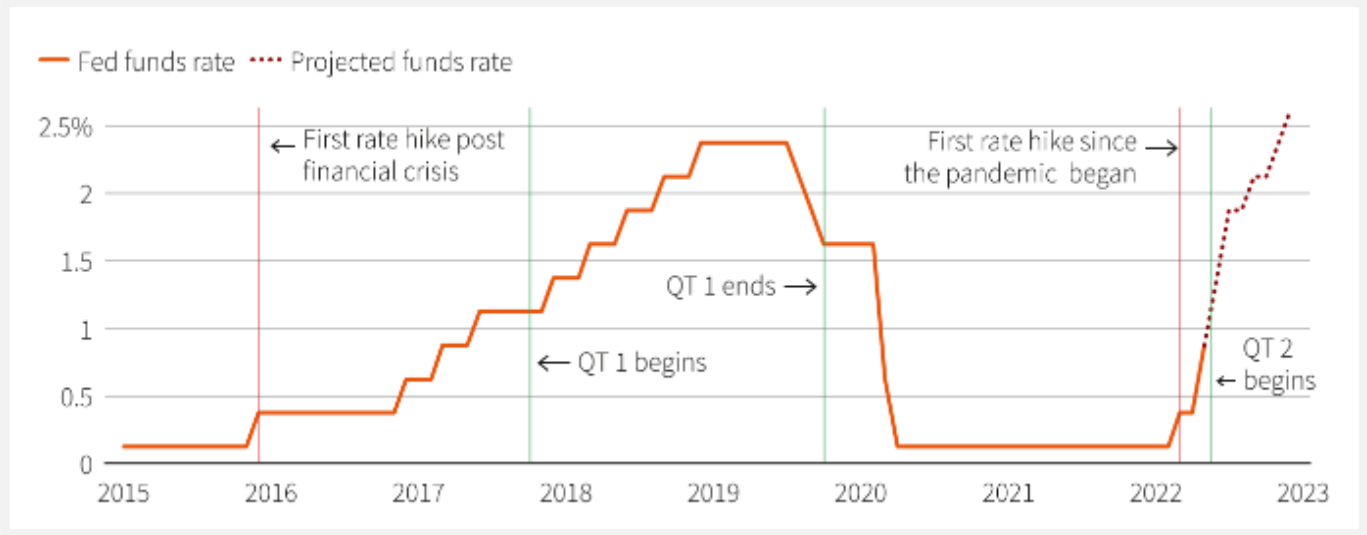
	2.00-2.25	2.25-2.50	2.50-2.75	2.75-3.00	3.00-3.25	3.25-3.50	3.50-3.75	3.75-4.00	4.00-4.25	4.25-4.50	4.50-4.75
27-Jul-22	13.8%	86.2%	0.0%	0.0%	-	-	-	-	-	-	-
21-Sep-22	0.0%	0.0%	8.0%	55.8%	36.2%	0.0%	0.0%	0.0%	0.0%	-	-
2-Nov-22	0.0%	0.0%	0.0%	2.8%	24.9%	48.9%	23.4%	0.0%	0.0%	0.0%	0.0%
14-Dec-22	0.0%	0.0%	0.0%	0.0%	2.3%	20.6%	44.3%	28.3%	4.5%	0.0%	0.0%
1-Feb-23	0.0%	0.0%	0.0%	0.0%	1.0%	10.5%	31.3%	37.1%	17.6%	2.5%	0.0%
15-Mar-23	0.0%	0.0%	0.0%	0.0%	0.7%	7.6%	24.8%	35.3%	23.6%	7.2%	0.8%
3-May-23	0.0%	0.0%	0.0%	0.0%	1.0%	8.4%	25.3%	34.7%	22.9%	6.9%	0.7%
14-Jun-23	0.0%	0.0%	0.0%	0.2%	2.5%	11.8%	27.2%	32.4%	19.7%	5.6%	0.6%
26-Jul-23	0.0%	0.0%	0.1%	0.9%	5.0%	16.0%	28.6%	28.9%	15.8%	4.3%	0.4%

 # at the close on 17 June 2022
Source: CME Group, Kenanga Research

An equally aggressive QT exercise. Meanwhile, in terms of the "breathing space" after the first rate hike in the cycle, size, pace and acceleration, the current QT cycle (dubbed the QT2) makes its predecessor in 2017-2019 (dubbed the QT1) feel like a breeze.

There was only a space of two-and-a-half months between the first rate hike in the last cycle (16 March 2022) and the start of the QT2 (1 June 2022). This compares with a"breathing space" of 22 months between the first rate hike in the cycle (December 2015) and the start of the QT1 (October 2017) (see Exhibit 2).

Exhibit 2: QT vs. Rate Hike Cycle



Source: Reuters

Exhibit 3: QT1 vs. QT2

	QT1 (2017-2019)	QT2 (2022-2025#)
"Breathing Space" after First Rate Hike (months)	22	2.5
Balance Sheet at Start of QT (USDtril)	4.5	9.0
Balance Sheet at End of QT (USDtril)	3.8	6.0#
Balance Sheet Reduction (USDtril)	-0.65	-3.0#
Balance Sheet Reduction (%)	-14	-33
Initial Pace (USDbil/month)	10	47.5
Maximum Pace (USDbil/month)	50	95
Time to Maximum Pace (months)	12	3

 # Consensus
Source: Reuters, Kenanga Research

Also, in the QT2, the Fed will shrink its balance sheet by a whopping USD47.5b/month during the first three months of the exercise, before ramping it up to the maximum USD95b/month subsequently. This is very aggressive as compared with a start of only USD10b/month during the QT1, followed by an increase of USD10b every quarter until it hit the maximum pace of USD50b/month 12 months later.

In terms of the total reduction in the Fed's balance sheet during the QT2, consensus views are currently pointing to USD3t or 33% from USD9t to USD6t. Again, this is massive both in absolute and percentage terms, as compared with a shrinkage during the QT1 of merely USD650b or 14% from USD4.5t to USD3.8t.

Emerging Markets Not Spared the Meltdown, But There Are Sweet Spots

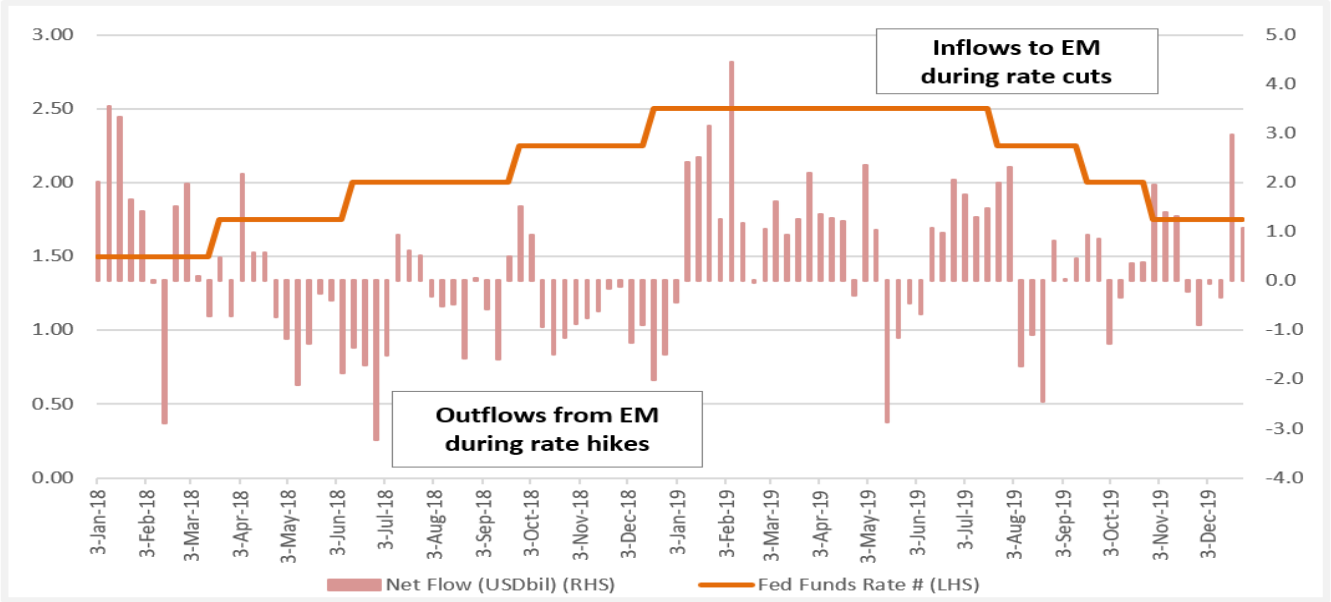
USD's strength hurts EM. EM assets are highly sensitive to the rate cycle in the US and they generally do not do well during a rate hike cycle as rising US Treasury yields: (1) dampen risk-taking in EM assets; (2) crimp the return on the EM carry trade (i.e. to borrow in USD and park the money in high-yielding EM assets); and (3) fuel USD's strength against EM currencies, posting increased risk of translation loss for holding EM assets.

In 2018 during which the Fed raised its target rate by 100 bps from 1.25%-1.50% to 2.25%-2.50%, investors pulled money from EM equities for the large part of the year (see Exhibit 4). However, they jumped back into EM equities at the start of 2019 when they felt that the rate had peaked and raised their bets further as the Fed started to ease policy in mid-2019 (also see Exhibit 4).

But strong commodity prices and outflow from Europe help. However, the current US rate hike cycle coincides with a super boom in commodity prices (as the production of many types of commodities has yet to return to the pre-pandemic levels due to various lingering pandemic-induced disruptions, exacerbated by the untimely war in the Ukraine), which augurs well for the generally commodity export-dependent EM. Malaysia is a clear winner in this situation given that it is one of the few privileged net energy exporters in the region and the second largest exporter of palm oil in the world. Also, on a relative basis, EM now appear a safer bet vs. Europe given the Ukraine war situation and the ban on Russian oil and gas imports, giving rise to a looming energy crisis and recession in Europe.

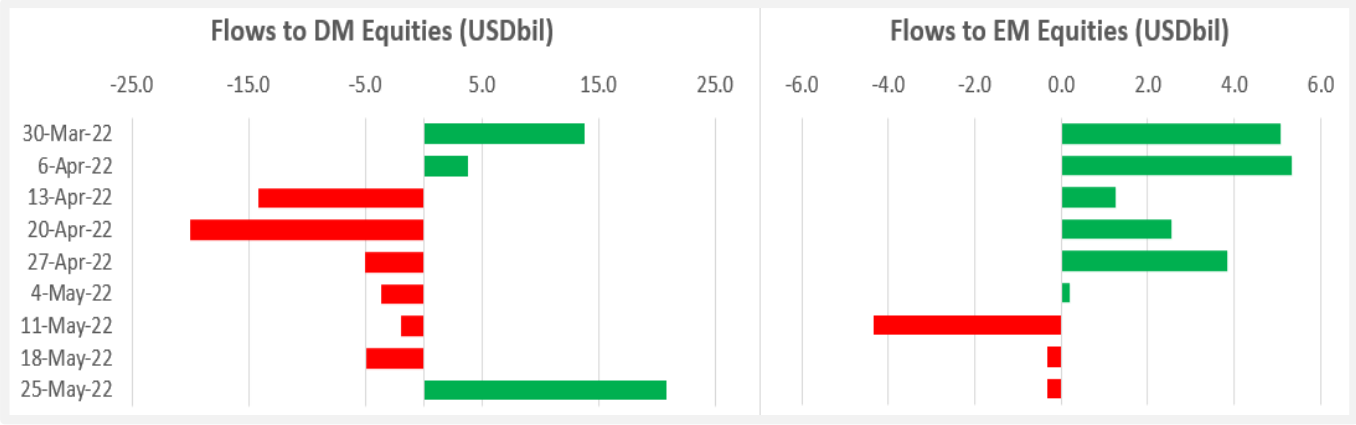
EM equities have shown resilience in the current global selloff. While its bigger cousin, i.e. developed markets (DM) equities, suffered massive outflows during the month of April, EM equities actually reported inflows throughout the same period and have only caught up with the outflows from DM equities from the second week of the month of May onwards (see Exhibit 5).

Exhibit 4: Flows to EM during Transition from Rate Hikes to Rate Cuts in 2018-2019



 # The upper end of the target range for the Fed Funds Rate
Source: FOMC, EPFR & Kenanga Research

Exhibit 5: Outflows during Recent Global Selloff: DM vs. EM



Source: EPFR & Kenanga Research

China's predicament and Russia's exit are gains to other EM countries. There has been a tectonic shift in weighting by country in the MSCI EM Index over the last 6-12 months. Once seemingly unstoppable, China has seen its weighting in the index—that serves as a benchmark for over USD1.8tril in assets globally—easing from the high thirties to the low thirties on the heels of a combination of regulatory crackdowns, a tech selloff, an ineffective zero Covid-19 policy and an ambiguous stance in the Russia-Ukraine war. Meanwhile, Russia has dropped out altogether from the index in the wake of the war. These have resulted in a corresponding rise in weighting for other countries in the index, including Malaysia (see Exhibit 6).

Exhibit 6: Indicative Weigthing in MSCI EM Index by Country

%	July 2021	June 2022	Chg
China	37.52	33.18	-4.34
Taiwan	13.78	15.42	+1.64
South Korea	13.10	11.82	-1.28
India	9.87	12.44	+2.57
Brazil	5.28	5.18	-0.10
South Africa	3.52	3.59	+0.07
Russia	3.30	0.00	-3.30
Saudi Arabia	2.87	4.34	+1.47
Mexico	1.75	2.04	+0.29
Thailand	1.59	1.86	+0.27
Malaysia	1.24	1.47	+0.23
Indonesia	1.09	1.86	+0.77

Source: ishares.com & Kenanga Research

Key Investment Themes: Pricing Power Near-Proxies, Commodity Producers and The GE15

Pricing power near-proxies. Under the current sustained high inflation scenario, it does not take a genius to figure out that investors should seek refuge in stocks of companies with strong pricing power. Typically, pricing power is derived from a global market leadership, a strong brand name (and the corresponding customer loyalty), unrivaled product quality (at least in the customer's perception), continuous product innovation backed by heavy investment in R&D, etc.

We acknowledge that it is difficult to find one that substantially fits the bill in the local market. However, we believe there are no lack of "near-proxies" for pricing power in the local bourse, which we define as companies that are able to maintain their margins despite the rising cost pressures. These include:

1. Service-based industries that have kept wage pressures at bay, i.e. **Banks and Telecommunications** players;
2. Suppliers to multinational companies with pricing power, predominantly in the tech/consumer electronics space (which means there are less cost pressures to be passed on along the supply chain), i.e. local players in the fields of **Outsourced Semiconductor Assembly and Test (OSAT), Automated Test Equipment (ATE)** and **Electronics Manufacturing Services (EMS)**; and
3. Providers of goods/services with a low **"**price elasticity of demand" such as **Private Healthcare**.

Commodity producers. The CPO futures contracts for July-December 2022 were last traded at between RM5,080/tonne and RM5,340/tones on Bursa Malaysia Derivatives while crude oil futures contracts for the same period last changed hands at between USD100/bbl and USD110/bbl on New York Mercantile Exchange.This will translate to super profits and free cash flows to players—especially to those in the upstream segment—in both the **Plantation** and **Oil & Gas** industries. There are concerns that CPO and crude oil prices may adjust down sharply as supply disruptions dissipate and/or high prices lead to demand destruction. Until that happens, commodity producers will continue to generate super free cash flows that strengthen their balance sheets, war chests and dividend-paying ability, resulting in a *permanent* improvement in their fundamentals.

The GE15. We hold the view that the time is about right for investors to position themselves ahead of the 15th General Election (GE15) due at the latest by September 2023. If not dissolved earlier, the parliament will head towards an automatic dissolution in July 2023, paving the way for the GE15 within the next 60 days. With the nation seemingly having already come out the other end of the Covid-19 pandemic, we foresee a shift in the focus of the government's fiscal spending plan from pandemic relief and vaccination back to infrastructure development. We expect more announcements on civil projects led by the RM31b Mass Rapid Transit 3 (MRT3) Circle Line project over the near term. This should revive investors' interest in **Construction** stocks.

Our **Sector Recommendations**, **Overall Top Picks** and **Top Shariah Picks** and their rationales and key investment statistics are reflected in Exhibits 7 to 11.

Exhibit 7: Sector Recommendations, Rationales and Picks

	Sector	Rationale	Top Picks
OVERWEIGHT	Automobile	Brisk sales as consumers frontload purchases (booking by June 2022 and registration by end-Mar 2023) to avoid the Sales and Services Tax.	BAUTO, MBMR
	Aviation	Re-opening of international borders.	AIRPORT
	Building Material	A proxy to renewable energy-based aluminium smelting (PMETAL).	PMETAL
	Construction	Award of infrastructure projects ahead of the GE15, a change in fiscal spending focus from pandemic relief and vaccination back to development.	GAMUDA, KERJAYA
	Financial	A proxy to economic recovery, resilience amidst inflation as wage pressures are kept at bay, favourable loan/deposit rate repricing amidst a rate hike cycle.	MAYBANK, RHBBANK, CIMB, ABMB
	Gaming	Re-opening of the tourism industry, partially offset by lingering ESG concerns.	GENTING, GENM
	Oil & Gas	Sustained elevated crude oil prices.	PCHEM, DAYANG, UZMA
	Plantation	Sustained elevated crude palm oil prices.	KLK, HSPLANT, BPLANT
	Private Healthcare	Pent-up demand for elective surgeries, resilience amidst inflation due to low "price elasticity of demand" for healthcare services.	IHH
	Technology/EMS	Robust tech demand and capex, significant pricing power. Local EMS providers benefit from multi-national companies' diversification away from China.	MPI, INARI, SKPRES, PIE, KGB
	Tele-communications	Resilience amidst inflation as wage pressures are kept at bay, the selloff triggered by challenges in 5G rollout is overdone.	DIGI, TM
	Utility	Recovery in electricity demand from the commercial and industrial segments.	TENAGA
NEUTRAL	Consumer	Inability to pass on higher input costs as excessive selling price hikes hurt demand.	MRDIY, AEON, PADINI
	Media	Recovery in adex and digital transformation, offset by higher content cost (ASTRO).	MEDIA
	Plastics & Packaging	Inability to pass on entirely the higher resin/operating cost to end-customers.	TGUAN
	Property	Higher effective mortgage rates and rising construction cost to weigh down on affordability.	IOIPG, ECOWLD
	REIT	Losing appeal to yield seekers on rising interest rates.	none
	Seaport & Logistics	A bumpy recovery in the global supply chain, rising operating cost, particularly fuel.	none
	Tobacco & Brewery	Price hikes to hurt demand, losing appeal to yield seekers on rising interest rates, ESG concerns.	none
UNDERWEIGHT	Gloves	ASP is suppressed as massive new capacity comes online while demand eases significantly as more countries come out the other end of the pandemic.	none

Source: Kenanga Research

Exhibit 8: Overall Top Picks and Rationales

Top Picks	Comments
MAYBANK (OP; TP: RM11.05)	MAYBANK continues to be the champion for dividend prospects (7-8%) which we believe is highly sought after amidst market uncertainties. Relative to its ROE of c.9%, we believe it provides investors the most favourable mix amongst its other high-ROE peers. Further, despite commanding the leading market share for loans (28% of listed peer total), MAYBANK still commands a better-than-industry GIL ratio of 1.9% (vs average 2.0%), which is testament to its asset quality controls. Investors may also be keenly monitoring the strategies of its new management which may lead to a leaner operating environment.
PCHEM (OP; TP: RM11.00)	PCHEM is a beneficiary of the elevated crude oil and petrochemical prices. Given its arrangement with Petronas, PCHEM benefits from a favourable feed-cost structure against peers – i.e. most of PCHEM's gas feed stock are procured from Petronas at a fixed pre-agreed price, while others may be hampered by the volatile input cost environment. PCHEM also enjoys dominant market share regionally, which will be further cemented by the start-up of its Pengerang complex in 2H2022 - increasing its capacity by ~15%. TP is pegged to 16x PER – in-line with other regional petrochemical giants (e.g. Formosa Chemicals, LG Chem).
IHH (OP; TP: RM7.20)	Given the low "price elasticity of demand" of private healthcare services, IHH has been able to pass on cost inflation to customers, as reflected in its rising revenue per inpatient over the past several quarters. IHH's investment appeal lies in: (i) its pricing power, as the inelastic demand of healthcare needs provides it with the ability to pass cost through amidst rising inflation; (ii) strong pent-up demand from domestic and international patients of which the group have started seeing in end Mar 2022; and (iii) commanding market position in countries it operates in.
KLK (OP; TP: RM30.00)	KLK ranks among the top integrated player in the palm oil sector. It runs some of the most profitable oil palm estates and is a prime beneficiary of firm edible oil and biofuel prices. Balance sheet is solidly backed with nearly 350,000 Ha of land while its 53% net gearing as at 2QFY22 is not high and is set to fall. ESG is a priority and KLK aims to certify IJM Plantations, which it bought recently, within three years. Our RM30.00 TP or 16x FY23 PER is not demanding considering strong FY22 growth, defensive balance sheet and proven management.
RHBBANK (OP; TP: RM6.95)	RHBBANK demonstrated the highest loans growth ability (+7% YoY vs 5.4% large cap average) which was mainly fuelled by strong penetration into SMEs. The stock's leading capital ratios (CET-1: 17%) could allow to group to deliver dividend surprises. Otherwise, it provides strong buffers against unexpected worsening of movement restrictions. Additionally, the group's recent digital banking licence win could serve as a sentiment booster to the group as it nears the launch of its new entity and digital offerings. Its 3-year plan to elevate ROE to 11.5% would put them close to the top of the industry, if successful.
Digi.Com (OP; TP: RM3.70)	The merger with Celcom will give birth to a market leader in the mobile segment in Malaysia with a lion's market share of 44% and niche strengths in providing mobile services to the public sector and migrant workers. The reopening of the economy and the return of migrant workers will drive DIGI's growth in the prepaid space. In the absence of significant wage pressures, we expect DIGI to take inflation in stride. Our TP is based on DCF (WACC: 6.6%, TG: 1%) with an implied FY23E EV/EBITDA of 10x. Its dividend yield of c.4% is among the highest in the industry.
INARI (OP; TP: RM3.30)	We like INARI given its proxy to the US customer's smartphone supply chain which is expected to remain resilient owing to the end customer's ability to command pricing and market share. Despite weak global smartphone shipment numbers in 1Q22 which fell 8.9% YoY, the US smartphone was the only brand to eke out a 2.2% YoY growth. In addition, the US company is expected to keep its smartphone production flat YoY for an upcoming new model that is slated to launch in September 2022 which we deem to be an encouraging sign.
GAMUDA (OP; TP: RM4.00)	We like GAMUDA's: (i) ability to pivot into highly regulated construction regions (such as Singapore & Australia) and relinquishing its dependence on the lacklustre domestic space caused by the current fiscal constraints, (ii) improving balance sheet post disposal of tolls which allows for PFI initiatives and a special dividend, (iii) high probability of success for the MRT3 tunneling tenders, (iv) strong orderbook of RM12.5b providing revenue cover of 3x, and (v) its appealing PER of 13.3x which we anticipate would rerate running up towards GE15 to be held within the next 15 months.
ABMB (OP; TP: RM3.95)	ABMB's high SME mix (>30%) and revivification from past asset quality concerns makes the stock an attractive pick for economic recovery angles. The group also has the highest CASA-to-deposits mix amongst its peers, making it defensible against NIM pressures from rate hikes as we believe current levels still do not warrant an industry-wide migration to fixed deposits on low base returns. A ROE standing of c.10% puts them in the lead amongst its similar-sized conventional banking peers with dividend yield of >6% which is commendable.
PIE (OP; TP: RM3.70)	We like PIE owing to its unique clientele base as well as its ability to grow its margins amid various macro challenges during Covid-19. Having been able to avoid the intensive competition surrounding household cleaning products, PIE was able to secure a big customer (34% of group revenue) for a home entertainment product last year which grew the group's revenue above the RM1b mark. Also, the group recently secured another major Chinese customer (relating to ASIC computer hardware) which intends to relocate its production to Malaysia.

Source: Kenanga Research

Exhibit 9: Overall Top Picks and Key Investment Statistics

Stock	Stock Call	Last Price	Target Price	Upside	Market Cap	FYE	EPS (sen)		EPS Growth (%)		PER (x)		PBV*	ROE*	NDPS*	Div. Yield*
		(RM)	(RM)	(%)	(RMmil)		FY22F	FY23F	FY22F	FY23F	FY22F	FY23F	(x)	(%)	(sen)	(%)
MAYBANK	OP	8.88	11.05	24.4	106,294	Dec	73.1	89.5	4.9	22.4	12.5	10.2	1.2	9.8	60.0	6.8
PCHEM	OP	9.52	11.00	15.5	76,160	Dec	87.2	68.8	-5.0	-21.1	10.9	13.8	2.0	19.0	43.6	4.6
IHH	OP	6.28	7.20	14.6	55,281	Dec	18.6	20.5	-12.5	10.6	33.9	30.7	2.3	7.1	6.0	1.0
KLK	OP	23.40	30.00	28.2	25,229	Sep	192.2	185.8	-3.1	-8.4	11.5	12.6	1.9	17.3	55.0	2.4
RHBBANK	OP	5.88	6.95	18.2	24,767	Dec	65.1	75.3	0.7	15.7	9.4	8.1	0.8	9.2	32.0	5.4
DIGI	OP	3.18	3.70	19.5	24,725	Dec	13.3	16.8	-11.1	26.3	23.9	18.9	38.4	162.0	13.2	4.2
INARI	OP	2.63	3.30	25.5	9,750	Jun	10.8	11.5	7.6	7.1	24.4	22.8	6.5	27.8	8.4	3.2
GAMUDA	OP	3.60	4.00	11.1	9,194	Jul	27.5	20.7	15.3	-24.7	13.6	18.0	1.1	7.9	12.0	3.3
ABMB #	OP	3.40	3.95	16.2	5,264	Mar	43.7	48.9	18.1	12.0	7.8	6.9	0.8	10.3	22.0	6.5
PIE	OP	3.07	3.70	20.5	1,179	Dec	20.3	22.6	28.2	11.7	15.2	13.6	2.0	14.2	5.0	1.6

 # FY22F and FY23F refers to FY23F and FY24F
** FY22F*
Source: Kenanga Research

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Exhibit 10: Top Shariah Picks and Rationales

Top Picks	Comments
PCHEM (OP; TP: RM11.00)	PCHEM is a beneficiary of the elevated crude oil and petrochemical prices. Given its arrangement with Petronas, PCHEM benefits from a favourable feed-cost structure against peers – i.e. most of PCHEM's gas feed stock are procured from Petronas at a fixed pre-agreed price, while others may be hampered by the volatile input cost environment. PCHEM also enjoys dominant market share regionally, which will be further cemented by the start-up of its Pengerang complex in 2HCY22 - increasing its capacity by ~15%. TP is pegged to 16x PER – in-line with other regional petrochemical giants (e.g. Formosa Chemicals, LG Chem).
IHH (OP; TP: RM7.20)	Given the low "price elasticity of demand" of private healthcare services, IHH has been able to pass on cost inflation to customers, as reflected in its rising revenue per inpatient over the past several quarters. IHH's investment appeal lies in: (i) its pricing power, as the inelastic demand of healthcare needs provides it with the ability to pass cost through amidst rising inflation; (ii) strong pent-up demand from domestic and international patients of which the group have started seeing in end Mar 2022; and (iii) commanding market position in countries it operates in.
KLK (OP; TP: RM30.00)	KLK ranks among the top integrated player in the palm oil sector. It runs some of the most profitable oil palm estates and is a prime beneficiary of firm edible oil and biofuel prices. Balance sheet is solidly backed with nearly 350,000 Ha of land while its 53% net gearing as at 2QFY22 is not high and is set to fall. ESG is a priority and KLK aims to certify IJM Plantations, which it bought recently, within three years. Our RM30.00 TP or 16x FY23 PER is not demanding considering strong FY22 growth, defensive balance sheet and proven management.
Digi.Com (OP; TP: RM3.70)	The merger with Celcom will give birth to a market leader in the mobile segment in Malaysia with a lion's market share of 44% and niche strengths in providing mobile services to the public sector and migrant workers. The reopening of the economy and the return of migrant workers will drive DIGI's growth in the prepaid space. In the absence of significant wage pressures, we expect DIGI to take inflation in stride. Our TP is based on DCF (WACC: 6.6%, TG: 1%) with an implied FY23E EV/EBITDA of 10x. Its dividend yield of c.4% is among the highest in the industry.
TM (OP; TP: RM6.70)	TM's earnings will be driven by: (i) improving subscription for its UNIFI service given its highly competitive offering and 5G availability (TM being one of the pioneers in Malaysia); and (ii) TM ONE as enterprise spending increases in line with the reopening of the economy. TM's home broadband market share is poised to climb back to pre-pandemic levels of >80%, from 70% at present. Meanwhile, it is on track to complete its nationwide fibre network expansion covering six million premises under the Jendela Initiative.
INARI (OP; TP: RM3.30)	We like INARI given its proxy to the US customer's smartphone supply chain which is expected to remain resilient owing to the end-customer's ability to command pricing and market share. Despite weak global smartphone shipment numbers in 1QCY22 which fell 8.9% YoY, the US smartphone was the only brand to eke out a 2.2% YoY growth. In addition, the US company is expected to keep its smartphone production flat YoY for an upcoming new model that is slated to launch in September 2022 which we deem to be an encouraging sign.
GAMUDA (OP; TP: RM4.00)	We like GAMUDA's: (i) ability to pivot into highly regulated construction regions (such as Singapore & Australia) and relinquishing its dependence on the lacklustre domestic space caused by the current fiscal constraints, (ii) improving balance sheet post disposal of tolls which allows for PFI initiatives and a special dividend, (iii) high probability of success for the MRT3 tunneling tenders, (iv) strong orderbook of RM12.5b providing revenue cover of 3x, and (v) appealing PER of 13.3x which we anticipate would rerate running up towards GE15 to be held within the next 15 months.
TAKAFUL (OP; TP: RM3.90)	We see TAKAFUL as a strong Shariah pick as its selldown amidst MFRS17 uncertainties appears unwarranted, which does not leave any implications to the group's operations. Having incorporated the tail-end range impact per the group's guidance, the stock still commands strong earnings potential from its solid foothold in the bancassurance space. Additionally, ongoing digitalisation would assist the group in penetrating an underserved retail market of RM13b in premiums. The reducing reliance on an agency workforce also positions the group firmly against disruptions in physical distribution.
BPLANT (OP; TP: RM1.00)	BPLANT is a Shariah compliant upstream plantation player with good dividends payouts. The Group has already declared and paid half of our estimated FY22 dividends within 1Q after strong operating profit was uplifted by disposal gain. Robust 2Q operating profit looks likely. Operationally, weak yields from older palms is mitigated by good selling prices (purely upstream) and yield improvement measures - from replanting with better seedlings to ensuring sufficient labour pool (engaging retired army personnel) to mechanisation. Our RM1.00 TP translates to 13x PER (20% below sector) and 14% full-year dividend yield.
PIE (OP; TP: RM3.70)	We like PIE owing to its unique clientele base as well as its ability to grow its margins amid various macro challenges during Covid-19. Having been able to avoid the intensive competition surrounding household cleaning products, PIE was able to secure a big customer (34% of group revenue) for a home entertainment product last year which grew the group's revenue above the RM1b mark. Also, the group recently has secured another major Chinese customer (relating to ASIC computer hardware) which intends to relocate its production to Malaysia.

Source: Kenanga Research

Exhibit 11:Top Shariah Picks and Key Investment Statistics

Stock	Stock Call	Last Price	Target Price	Upside	Market Cap	FYE	EPS (sen)		EPS Growth (%)		PER (x)		PBV *	ROE*	NDPS *	Div. Yield*
		(RM)	(RM)	(%)	(RMmil)		FY22F	FY23F	FY22F	FY23F	FY22F	FY23F	(x)	(%)	(sen)	(%)
PCHEM	OP	9.52	11.00	15.5	76,160	Dec	87.2	68.8	-5.0	-21.1	10.9	13.8	2.0	19.0	43.6	4.6
IHH	OP	6.28	7.20	14.6	55,281	Dec	18.6	20.5	-12.5	10.6	33.9	30.7	2.3	7.1	6.0	1.0
KLK	OP	23.40	30.00	28.2	25,229	Sep	192.2	185.8	-3.1	-8.4	11.5	12.6	1.9	17.3	55.0	2.4
DIGI	OP	3.18	3.70	19.5	24,725	Dec	13.3	16.8	-11.1	26.3	23.9	18.9	38.4	162.0	13.2	4.2
TM	OP	5.06	7.00	38.30	19,095	Dec	30.9	35.1	30.1	13.8	16.4	14.4	2.5	15.6	17.0	3.4
INARI	OP	2.63	3.30	25.5	9,750	Jun	10.8	11.5	7.6	7.1	24.4	22.8	6.5	27.8	8.4	3.2
GAMUDA	OP	3.60	4.00	11.1	9,194	Jul	27.5	20.7	15.3	-24.7	13.6	18.0	1.1	7.9	12.0	3.3
TAKAFUL	OP	3.37	3.90	15.70	2,822	Dec	41.3	43.5	-16.0	5.2	8.2	7.8	1.4	18.0	14.0	4.2
BPLANT	OP	0.84	1.00	19.00	1,882	Dec	14.6	7.6	169.1	-74.0	2.9	11.1	0.7	24.4	14.0	16.7
PIE	OP	3.07	3.70	20.5	1,179	Dec	20.3	22.6	28.2	11.7	15.2	13.6	2.0	14.2	5.0	1.6

** FY22F*
Source: Kenanga Research

Automotive

Stronger Recovery Drive Ahead

OVERWEIGHT

↔

By Wan Mustaqim Bin Wan Ab Aziz I wanmustaqim@kenanga.com.my

We maintain OVERWEIGHT on the sector driven by the re-opening of economic activities, and further driven by buoyant recovery in car sales as evident from the growing number of back-logged bookings for popular models (up to 6 months), with stream of new higher-margin models launched in 2022 (including models that were postponed from 2021). Positively, we expect sustainable car sales post-SST exemption period as we believe order cancellations would be minimal as the demand would still outweigh the supply given the massive back-logged orders accumulated since last year coupled with the government commitment to absorb the SST for orders before 30th June 2022, with JPJ registration before 31st March 2023. Our 2022 TIV target at 600k units (+18%) is in line with MAA's 2022 TIV target.

The sector is currently trading at trailing 12x PER which is at a 25% discount to pre-pandemic mean of 16x PER. We expect profits in subsequent quarters to gradually normalise to pre-pandemic levels on the back of sector earnings growth of 22% in FY23 which should justify sector PER to gradually reverting closer to the mean.

We prefer players with industry leading market position, and sustainable high-margin profit models. We like MBMR (OP; TP: RM4.10) given their market leading position in the national marques space. We believe the player that benefits most from high-margin new launches is BAUTO (OP; TP: RM2.30) given that it's just added two new marques under its stable (Kia and Peugeot) with 18 new models including Mazda starting 4QCY21 until 2023.

Maintain OVERWEIGHT with 2022 TIV target of 600k units (+18%). Our call on the sector is driven by the re-opening of economic activities, and further boosted by buoyant recovery in car sales as evident from the growing number of back-logged bookings for popular models (up to 6 months), with stream of new higher-margin models launched in 2022 (including models that were postponed from 2021). Positively, we expect sustainable car sales post-SST exemption period as we believe order cancellations would be minimal as the demand would still outweigh the supply given the massive back-logged orders accumulated since last year coupled with the government commitment to absorb the SST for orders before 30th June 2022, with JPJ registration before 31st March 2023. Additionally, Battery Electric Vehicles (BEVs) new launches are expected to be boosted by full exemption on import & excise duties, sales tax, road tax, and individual tax relief of up to RM2,500 for the costs of purchase and installation as well as rental and subscription fees of EV charging facilities up to 31 December 2025 (for CKD and CBU up to 2023) to support development of the local EV industry. Automakers have prioritized their usage of shortage parts, diverting to their most profitable vehicles such as full-size trucks and SUVs, as well as luxury vehicles. Our 2022 TIV target at 600k units (+18%) is in line with MAA's 2022 TIV target.

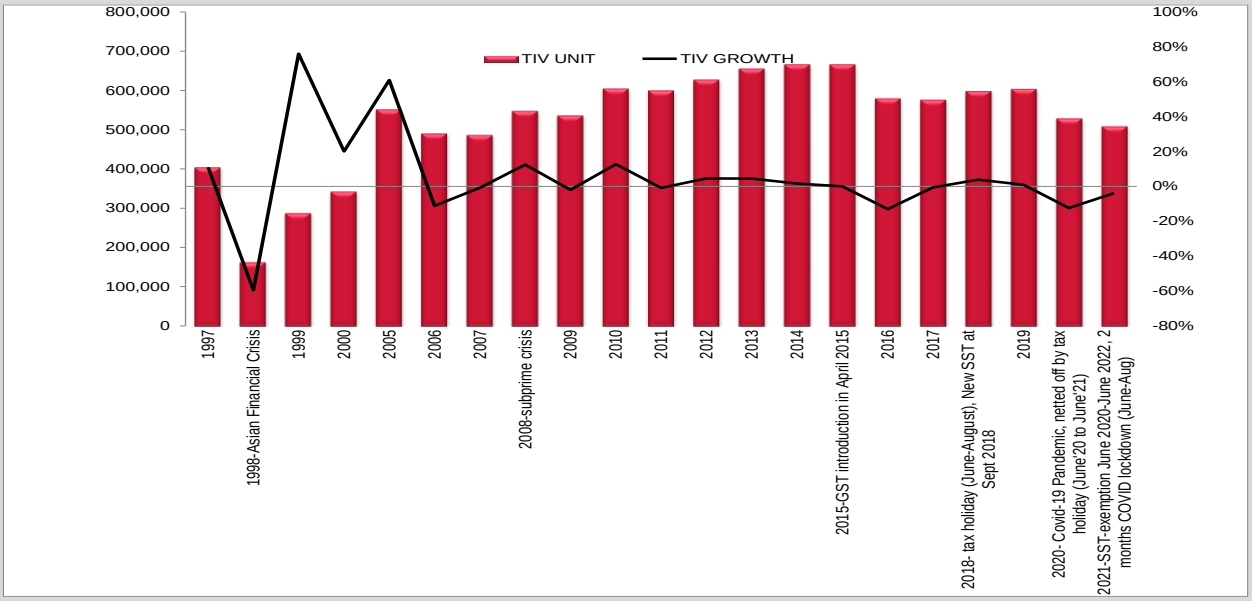
Discount to mean valuation is unjustified. The sector is currently trading at trailing 12x PER which is at a 25% discount to pre-pandemic mean of 16x PER. We expect profits in subsequent quarters to gradually normalise to pre-pandemic levels on the back of sector earnings growth of 22% in FY23 which should justify sector PER to gradually reverting closer to the mean.

Sustainable car sales despite the ending of SST-exempted period. We expect sustainable car sales post-SST exemption period as we believe order cancellations would be minimal as the demand would still outweigh the supply given the massive back-logged orders accumulated since last year coupled with the government commitment to absorb the SST for orders before 30th June 2022, with JPJ registration before 31st March 2023. Current backlog as shared by the Ministry of Finance (MoF) is at 264,000 units which translated into 4 to 5 months delivery queue from the supply chain disruption (based on our target of 600,000 units) which could as well to drive the back-log orders up to 9 months. This also provides assurances to the automakers to fast-track their production level and safeguard their margin if there is a need to increase the car prices given the increase in auto parts procurement costs (final car prices is reflected in the final invoice, not during the booking).

Our sector top picks are MBMR and BAUTO. We like MBMR (OP; TP: RM4.10) for its: (i) deep value stake in 22.58%-owned Perodua, and (ii) dual-income streams as the largest Perodua dealer and spare parts supplier for most of the popular marques. We like BAUTO (OP; TP: RM2.30) as it offers: (i) one of the highest dividend yields in our auto universe coverage, and (ii) the highest PATAMI margin which is head and shoulders compared to peers.

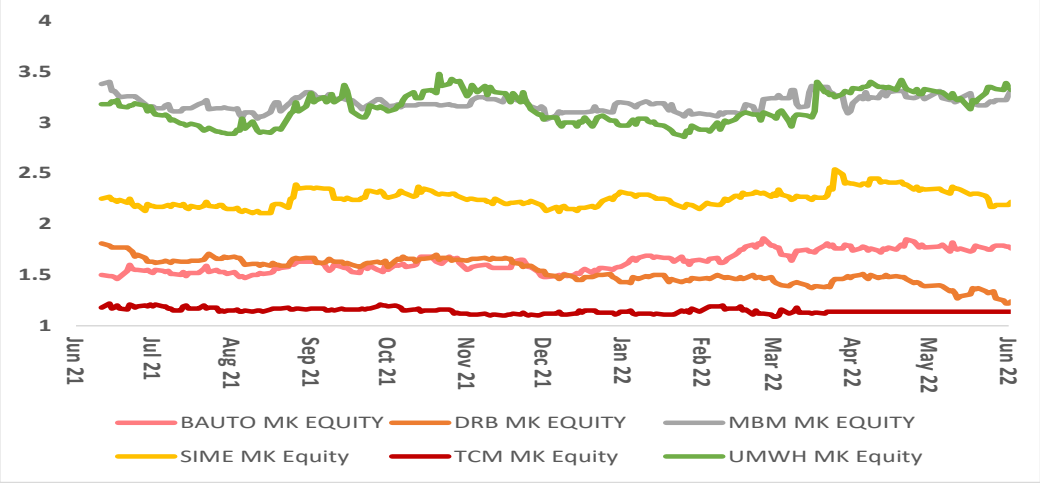
Risks to our sector rating are: (i) slower-than-expected recovery in production volume from the supply-chain disruption, (ii) lower-than-expected margin for companies under our coverage, and (iii) stricter government regulation on the automotive industry especially on excise duties calculation which could trigger pushing vehicles already selling at higher prices out of the affordable range.

Total Industry Volume from1997 to 2021



Source: MAA, Kenanga Research

Share Price Movement June 2021-June 2022



Source: MAA, Kenanga Research

TIV Market Share Movement

Position	Marques	4M22	4M21	Market Share	Sales	Comment
1st	Perodua	40%	39%	▲	11%	Driven by the all-new Axia, Myvi, and Ativa, shifting toward SUV.
2nd	Proton	16%	24%	▼	-28%	Driven by Proton X70 and further all-new X50, and PIES line-ups.
3rd	Toyota	14%	13%	▲	12%	The all-new Toyota Vios, all-new Toyota Yaris, and Toyota Hilux received overwhelming responses.
4th	Honda	12%	10%	▲	31%	Driven by all-new Honda City and HR-V 2021.
5th	Nissan	2%	2%	◄►	24%	Lack of new volume-driven model launches.
6th	Mazda	3%	2%	▲	35%	Driven by CX-5 and all-new CX-8.
National Marques		56%	63%	▼		Shift toward lower volume SUV for Perodua and boosted by Proton.
Non-national Marques		44%	37%	▲		Increasing new launches of updated volume driven models.

Source: MAA, Kenanga Research

Peer Comparison

Name	Price as at 17th June 2022 (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net DivYld(%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
STOCKS UNDER COVERAGE																	
BERMAZ AUTO BHD	1.78	2,066.6	Y	04/2022	1.1%	10.1%	5.1%	14.4%	13.3	12.6	11.0	3.2	2.9	24.4%	4.8%	2.30	OP
DRB-HICOM BHD	1.16	2,242.3	Y	12/2022	29.5%	11.7%	-7.5%	35.4%	N.A.	11.5	8.5	0.2	0.2	2.1%	1.7%	1.80	OP
MBM RESOURCES BERHAD	3.13	1,223.5	Y	12/2022	33.7%	11.4%	16.5%	16.6%	7.3	6.3	5.4	0.6	0.5	8.7%	6.4%	4.10	OP
SIME DARBY BERHAD	2.13	14,486.1	Y	06/2022	5.0%	5.0%	3.9%	3.9%	12.7	12.2	11.8	0.9	0.9	7.2%	5.2%	2.60	OP
TAN CHONG MOTOR HOLDINGS BHD	1.14	766.1	N	12/2022	32.9%	10.2%	-31.3%	54.4%	N.A.	61.3	39.7	0.3	0.3	0.5%	2.6%	1.00	UP
UMW HOLDINGS BHD	3.15	3,680.1	Y	12/2022	7.1%	7.9%	60.5%	9.9%	16.5	10.3	9.3	0.5	0.5	4.9%	1.9%	4.40	OP
Simple Average					**18.2%**	**9.4%**	**7.9%**	**22.4%**	**12.4**	**19.0**	**14.3**	**1.0**	**0.9**	**8.0%**	**3.8%**		

Source: Bloomberg, Kenanga Research

Aviation

Heading to Airport

OVERWEIGHT
↑

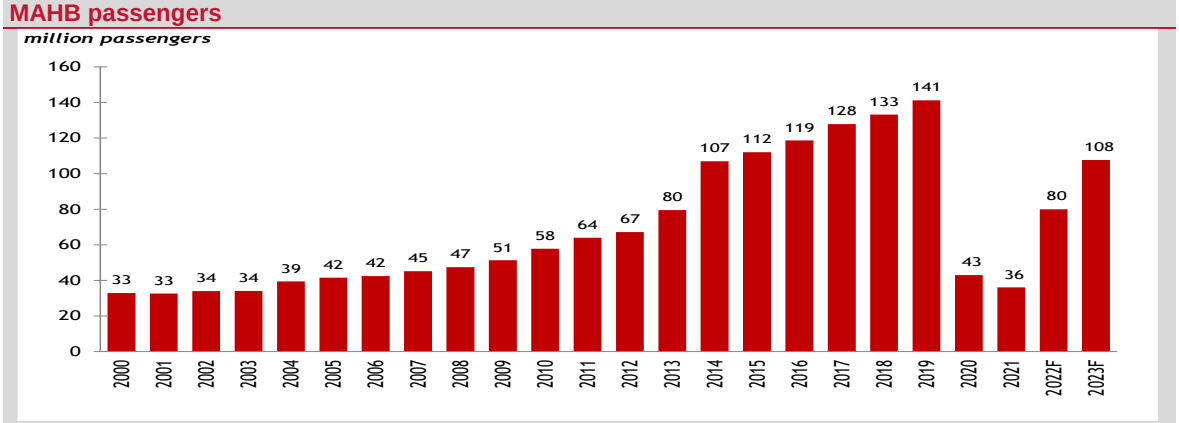
By Raymond Choo Ping Khoon I pkchoo@kenanga.com.my

Upgrade to Overweight from Neutral. We expect a gradual recovery in air travel beginning 2H 2022 following the reopening of our international borders starting 1 Apr 2022 to quarantine-free travel for fully-vaccinated travelers. While we expect a gradual recovery in air travel beginning 2H 2022, we expect losses at CAPITALA to persist over the next two quarters while the PN17 status of the company will remain an overhang despite on-going restructuring efforts. For the sector, we prefer Malaysia Airport Holdings Berhad (MAHB), being the dominant airport operator in the country. The yet-to-be signed Operating Agreement (OA) could be a re-rating impetus for MAHB which we reiterate as an Outperform. MAHB is a beneficiary of border reopening, leveraging on the anticipated strong recovery for air travel. We maintain Market Perform on CAPITALA (MP; TP: RM0.65). For stock picks, we like MAHB (OP; TP: RM7.65) being a dominant airport operator in the country premised on gradual air travel recovery.

MAHB - International travel to pick up pace in 2H 2022. We expect passenger improvement to gain momentum as we enter 2H 2022. Total MAHB's network of airports passenger traffic continued to gain traction in May 2022, recording 7.1m (+47% M-o-M) bringing 5MYTD number to 26.8m (+182%) which came in inline at 34% of our full-year forecast of 80m (vs. 36m in 2021). We expect traffic trajectory to grow exponentially from low base in subsequent months driven by domestic seat capacity nearing 90% of pre-COVID from July and international seat capacity expected to recover to at least 50% during the same period before any further upward slot revisions for the Northern winter season. The further relaxation of movement restriction from 1st May 2022 is expected to ease international travellers' journey and would further facilitate the resumption of international traffic gradually over the coming quarters. AirAsia and Scoot Airlines are the first international flights to resume services to Kota Kinabalu International Airport on 16th and 29th April, respectively, after two years of lull. Among the airlines that have resumed services in April at Penang International Airport and KLIA are Thai AirAsia, AirAsia X, Vietjet Air and AirAsia to Bangkok, Incheon, Hanoi and Hat Yai. Royal Brunei Airlines has resumed services to Kota Kinabalu from Bandar Seri Begawan from 6th May 2022, utilising Airbus 320neo with two-time weekly frequencies. Recall that on 12 Apr 2019, MAHB announced that the Government had approved the extension of MAHB's concession to operate 39 airports in Malaysia, from year 2034 to 2069. The new OA with the government following the extension of the concession (yet to be signed) will pave the way for the stock to be re-rated. We believe the new OA will be investor-friendly, and create a sustainable long-term development path for MAHB.

CAPITALA's PN17 status remains an overhang but gradual recovery in air travel seen. While we expect a gradual recovery in air travel beginning 2H 2022, we expect losses to narrow but persist over the next two quarters while the PN17 status of the company remains an overhang despite its on-going restructuring efforts. Its digital segment is expected to remain loss-making. Airasia Super App is expected to grow, underpinned by the continued resurgence of travel demand from borders reopening and tactical campaigns, alongside expected growth from airasia Food, airasia Ride and airasia Xpress. Additionally, Teleport is expected to continue growing throughout 2022 as it adds new international lanes and delivery hubs. In March 2022, BigPay fully launched its digital lending platform to provide new loan products.

MAHB passengers



Source: Kenanga Research, MAHB

Peer Comparison – Airlines

Name	Last Price @ 17/6/2022 (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
AVIATION UNDER COVERAGE																	
AIRASIA GROUP BHD	0.580	2,414		12/2022	347%	32%	-125%	-73%	N.A.	N.A.	12.6	(0.8)	(0.7)	21.4%	0.0%	0.650	MP
MALAYSIA AIRPORTS HLDGS BHD	6.35	10,536		12/2022	78%	21%	-65%	89%	N.A.	39.3	20.8	1.5	1.4	3.7%	102.4%	7.65	OP

Source: Bloomberg, Kenanga Research

Banking

Finding Defensive Ground

OVERWEIGHT

↔

By Clement Chua I clement.chua@kenanga.com.my

We maintain our OVERWEIGHT call on the sector. Against greater concerns and uncertainties in global macros, we continue to see banking stocks as a safe haven for being especially shielded from inflationary pressures. Rising costs are also not to be an expected concern for the banks as CIRs are typically under high surveillance while a rising OPR environment would support NIMs expansion. Our in-house expectations are for another three 25 bps hikes in 2HCY22, as BNM might follow the US Fed's hawkish footsteps to curb inflation. At this juncture, we do not foresee the need for full-fledged repayment assistance programs to return unless nationwide movement restrictions are again reinforced. Hence, we see provisioning needs to be adequate post-front loading from previous periods and remaining troubled accounts from existing programs to be inconsequential to the respective banks. Writebacks are mostly anticipated to occur in CY23, which would be a boon to earnings then. Our sector Top Pick for 3QCY22 is MAYBANK (OP; TP: RM11.05) for dividend safety (7-8% yield) providing a solid shelter amidst the aforesaid inflationary concerns. Despite being the market share leader, they continue to command decent asset quality which we believe will remain undeterred against unforeseen headwinds. For the smaller cap banks, we like AFFIN (OP; TP: RM2.40). We believe AFFIN's monetisation of its business units (AHAM and AXA Affin) could lead to possible surprises to its existing dividend yield prospects of 5-6%. Also, the streamlining of business units could affirm the stocks identity as a traditional bank to bring it to a level more comparable to its peers.

OPR excitement could draw further interest. After the surprise 25 bps hike in May 2022, we reckon that BNM may opt for further monetary tightening to curb inflation. This could be taking notes from the US Fed which recently on 15 June drew a 75 bps increase (150 bps YTD) to the Fed Funds Rate. While it is expected for inflationary pressures to pick up from a less restrictive economy and reopening of borders, fluctuations in commodities that stemmed from the still ongoing Russia-Ukraine conflict seek to exacerbate it. As such, our house-view leans towards a 25 bps OPR increase each from BNM's July, September and November monetary policy meetings. To recap, every 25 bps rate hike would translate to a 1-3% increase in net earnings to the banking stocks from NIM expansion. No doubt this may be less retail-friendly, but we do not anticipate a meaningful worsening of asset quality as previous cash flow concerns that were mainly stirred by restricted economic movement has evaporated.

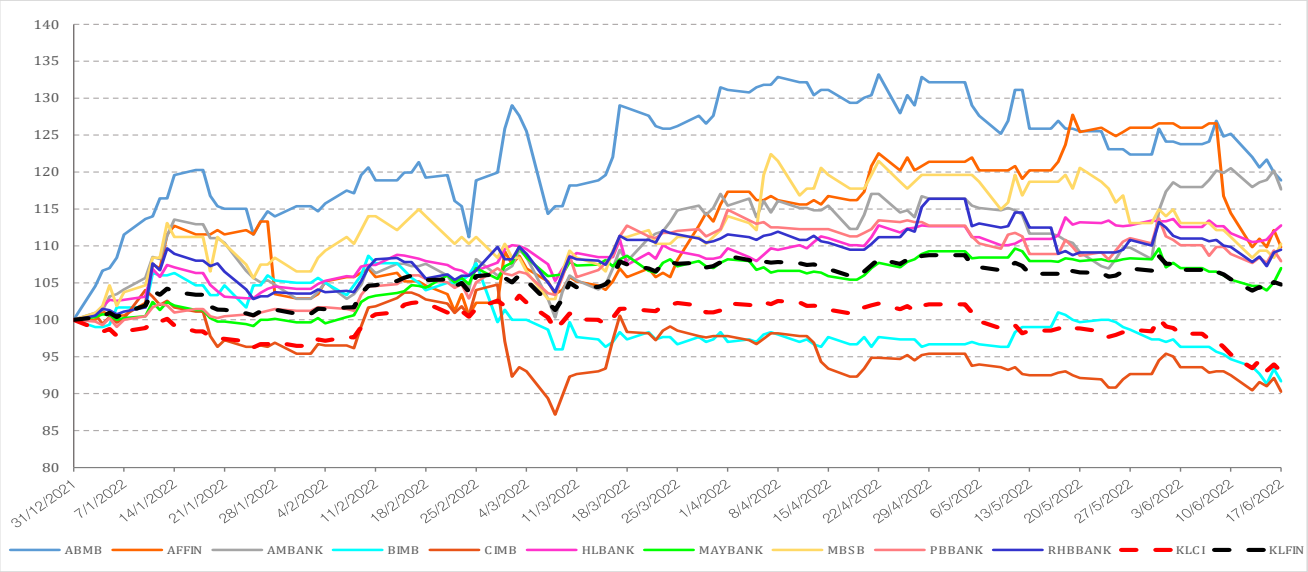
Adding to this, **residual repayment assistance accounts should be a paltry mix in 2HCY22.** Across the banks, April 2022 saw their respective **active repayment assistance mix coming in at 5-14% (vs Dec 2021: 8-31%)** of total domestic loan books. With applications for URUS already closed, we can only expect these proportions to only narrow, of which the banks do not expect situational extensions to be common. That said, even with the graduation of its entire repayment assistance books, BNM cautioned banks against premature writebacks of its provisions before establishing the full recoverability and sustainability of an account's health, with an indicative 3-6 months of undisrupted loan repayment to serve as reference. From 1QCY22 results, the banks have an average of 60 bps in pre-emptive buffers against their loan books.

Non-interest income may experience near-term hurdles. On the flipside to higher net interest gains from eventual OPR hikes, the translated rise in bond yields may in turn lead to adverse adjustments to its fair values. Corporates have guided lower allocation towards debt securities in anticipation of such predicament, albeit not at an exhaustive level. Subsequently, an overall softer landscape of the investment market may dampen trading performance as compared to the heydays in the past two years. However, an increased effort in promoting wealth management products looks to cushion the downfall from weakness here. Meanwhile, higher credit card transactions could further support income here as consumer spending is revitalised.

Maintain OVERWEIGHT on the Banking Sector. We continue to view the banking space favourably as they are well positioned against an inflationary environment, particularly being anchored by their mostly cost-stable operating structure. Broadly, they are beneficiaries of: (i) higher loans growth from economic reopening/recovery; (ii) higher NIMs with eventual OPR hike; (iii) progressive write-backs of Covid-19 loan provisions; and (iv) investing post-CY22 which will witness an earnings surge ex-prosperity tax in CY23. For 3QCY22, we are cognizant that there may be a higher interest for safety, hence we align our picks with dividend yielders. With that, we feature **MAYBANK (OP; TP: RM11.05)** which remains the champion for dividend prospects (7-8%) which we believe is highly sought after amidst market uncertainties. Relative to its ROE of c.9%, we believe it provides investors the most favourable mix amongst its other high-ROE peers. Further, despite commanding the leading market share for loans (28% of listed peer total), MAYBANK still commands a better-than-industry GIL ratio of 1.9% (vs average of 2.0%). We also like **AFFIN (OP; TP: RM2.40)** which has reaped commendable PBT growth from management's operating strategies. Present dividend yields stand at 5-6% but we see possibility for surprises with the pending completion of AHAM and AXA Affin's disposal during this 2HCY22 period. We surmise that with these disposals, the group may be viewed more favourably with peers which may trigger a revaluation later on.

Banking sector outperforming benchmark indices. While ongoing macro concerns persist to cloud sentiment, the banking sector appears mostly unaffected by foreign sell-downs and recessionary fears. Gains from the banks were mainly drawn by heavy anticipation for loans growth with the relaxation of movement restrictions and sustained by May 2022's OPR hike as the markets eased off. Outliers are BIMB and CIMB which were bogged down by: (i) earnings disappointments amidst untimely defaults from large corporate accounts and subsequent misses, and (ii) double-crediting issue which was raised in Feb 2022 from operating mismanagement, respectively.

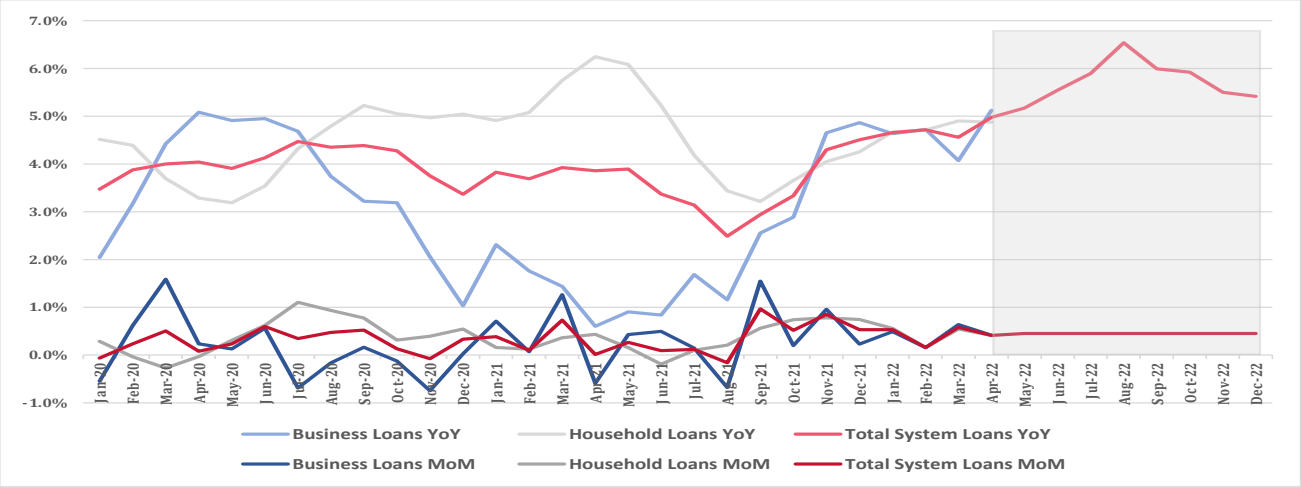
Table 1: YTD Performance of Banking Stocks against the KLCI and Bursa Finance Index (KLFIN)



Source: Companies, Kenanga Research

5.0-5.5% industry loans growth target for CY22 intact. Now at the halfway mark of the year, we reaffirm that our 5.0-5.5% industry loans growth target is achievable (YTD-April: +1.7%). The momentum for loans demand has been mainly spurred by household loans as private individuals seek to capitalise on a low interest rate environment. Subsequent to the May 2022 hike and with more possible to come, we suspect that this mix will be skewed towards business loans as working capital needs are even more demanding in an expansionary business landscape. Our estimates are in-line with our in-house GDP target of 5.0-5.5% which translate to higher compounded economic activity in 2HCY22 yielded from the progressive pick-up. Troubled sectors in the past years (i.e. hospitality, retail) are expected to make a come-back by then.

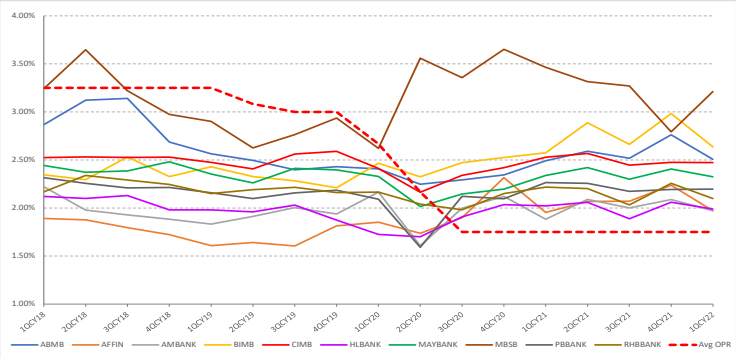
Table 2: YoY and MoM Loans Growth and Projection



Source: BNM, Kenanga Research

Margin prospects to revitalise. Following the recent quarters, we begin to see NIMs plateauing as most banks have exhausted repricing opportunities and are instead competing to capture a larger share of CASA deposits. Although some banks have opted to not compete in pricing with some resorting to only targeted marketing, the net impact was the numbing of NIM expansion across the industry. With the rise in OPR, corporates are at least confident to sustain existing levels which without, could lead to further compression. This is in line with the expectations that only a 1-3 bps impact could be seen with every rate hike. Hence, multiple increases are required to result into a more meaningful NIMs growth.

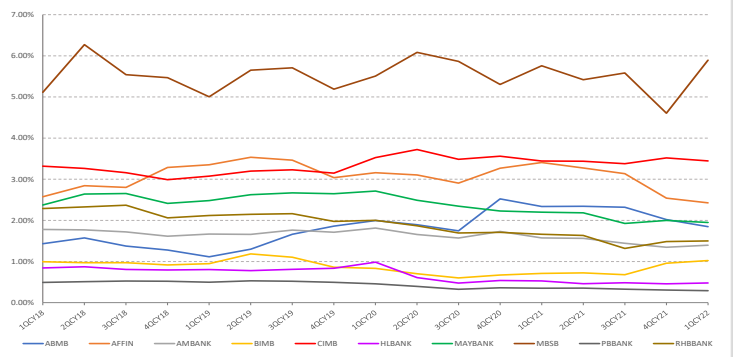
Table 3: Est. Annualised NIM trends (1QCY18-1QCY22)



Source: Companies, Kenanga Research

Asset quality remains amenable. The GIL ratio was under high scrutiny during the introduction of repayment assistance programs on grounds that it would only delay the degradation of non-salvageable accounts. With the expiry of PEMULIH and URUS applications in 1QCY22, there has been little signal to show that there will be prevailing risks in the coming quarters. Further, it appears reapplications were mostly from a small proportion of B40 accounts; hence, defaults from their own would be mostly inconsequential to the financial system going forward.

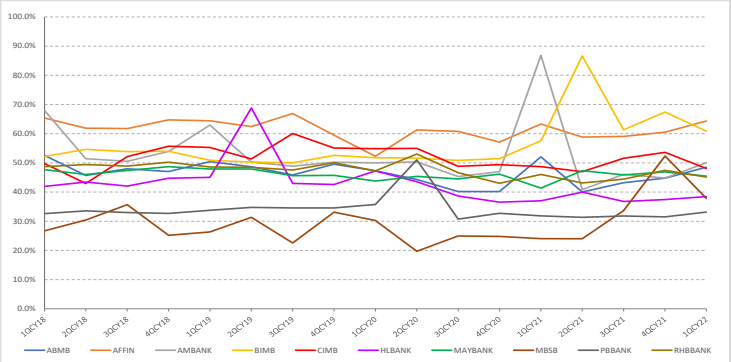
Table 4: Est. GIL trends (1QCY18-1QCY22)



Source: Companies, Kenanga Research

Cost management much in control. During periods of movement control, certain banks implemented right-sizing measures with marketing activities capped by physical limitations. As we move towards a more liberal environment, these expenses are likely to pick up to align with the group's aspired income growth. That said, we do not believe the banks would be overly aggressive as cost elements are usually budgeted tightly. Additionally, with the corporate guidance to keep CIR flattish at best, the likely negative deviation would arise from failure to expand topline, which we believe in unlikely in the current climate of higher loans and higher margins later on.

Table 5: Cost-to-Income Ratio (1QCY18-1QCY22)



Source: Companies, Kenanga Research

Table 5 : Updated corporate guidances post-1QCY22 results

Company	FYE	Loan growth	Deposit growth	Net interest margin	Cost-to-income ratio	Credit cost	Return on equity	Gross impaired loan	CASA Mix
ABMB	Mar-23	6-8% *(FY22: 4.6%)*		~2.50% *(FY22: 2.53%)*	<45% *(FY22: 44.1%)*	40-45 bps) *(FY22: 48 bps)*	>10.0% *(FY22: 9.0%)*		
AFFIN	Dec-22	12.0%) *(FY21: 11.1%)*		2.04% *(FY21: 1.97%)*	55% *(FY21: 60.7%)*	30 bps) *(FY21: 41 bps)*	7.0% *(FY21: 5.4%)*	2.20% *(FY21: 2.54%)*	
AMBANK	Mar-23	7% *(FY22: 4.6%)*		2.05-2.10% *(FY22: 2.02%)*		35-40 bps *(FY22: 66 bps)*	9.3-10% *(FY22: 9.6%)*		
BIMB	Dec-22	8.0% *(FY21: 6.5%)*		2.40% *(FY21: 2.38%)*		25-30 bps *(FY21: 34 bps)*	10% *(FY21: 8.4%)*		
CIMB	Dec-22	5-6% *(FY21: 3.2%)*		-10 bps *(FY21: 2.51%)*	<49% *(FY21:48.5%)*	60-70 bps) *(FY21: 73 bps)*	8.5-9.0% *(FY21: 8.1%)*		
HLBANK	Jun-22	6-7% *(FY21: 6.8%)*		2.10% *(FY21: 2.14%)*	<40% *(FY21: 38.0%)*	~10 bps *(FY21: 43 bps)*	>10.5% *(FY21: 10.1%)*	<0.8% *(FY21: 0.48%)*	>30% *(FY21: 32.3%)*
MAYBANK	Dec-22			stable *(FY21: 2.32%)*	45-46% *(FY21: 45.3%)*	40-50 bps *(FY21: 49 bps)*	9.5-10% *(FY21: 9.5%)*		
MBSB	Dec-22	10-11% *(FY21: 1.3%)*			~30% *(FY21: 40.4%)*	45bps *(FY21: 24 bps)*		<3% *(FY21: 4.6%)*	
PBBANK	Dec-22	4-5% *(FY21: 3.6%)*	4-5% *(FY21: 4.0%)*	Stable (from single digit compression) *(FY21: 2.22%)*		<20 bps *(FY21: 34 bps)*	11-12% *(FY21: 11.9%)*		
RHBBANK	Dec-22	4-5% *(FY21: 6.7%)*		2.14% (from 2.11%) *(FY21: 2.14%)*		30 bps *(FY21: 30 bps)*	8.5% *(FY21: 9.6%)*	<1.70% *(FY21: 1.49%)*	30.0% *(FY21: 30.0%)*

Source: Companies, Kenanga Research

Peer Table Comparison

Name	Last Price as of 17 Jun 2022 (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net DivYld (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
Stocks Under Coverage																	
AFFIN BANK BHD	1.90	4,035.7	N	12/2022	12.6%	4.1%	9.4%	23.2%	7.6	7.0	5.6	0.4	0.4	5.7%	5.8%	2.40	OP
ALLIANCE BANK MALAYSIA BHD	3.40	5,263.6	N	03/2023	4.8%	4.5%	18.1%	12.0%	9.2	7.8	6.9	0.8	0.8	10.3%	6.5%	3.95	OP
AMMB HOLDINGS BHD	3.73	12,355.3	N	03/2023	6.4%	4.0%	5.7%	7.7%	8.2	7.8	7.2	0.7	0.7	9.2%	4.3%	4.35	OP
BANK ISLAM MALAYSIA BHD	2.75	5,927.0	Y	12/2022	-7.1%	0.6%	-2.6%	14.8%	12.8	13.2	11.3	1.1	1.0	7.9%	3.8%	2.85	MP
CIMB GROUP HOLDINGS BHD	4.92	51,533.3	N	12/2022	4.4%	6.4%	1.3%	30.5%	10.6	10.5	8.0	0.8	0.8	7.8%	4.7%	5.70	OP
HONG LEONG BANK BHD	21.00	45,522.1	N	06/2022	4.0%	8.6%	5.8%	22.8%	15.0	14.2	11.6	1.5	1.4	10.0%	2.7%	22.85	OP
MALAYAN BANKING BHD	8.88	106,293.7	N	12/2022	4.3%	7.0%	4.9%	22.4%	12.7	12.1	9.9	1.2	1.2	9.8%	6.8%	11.05	OP
MALAYSIA BUILDING SOCIETY BHD	0.590	4,231.2	N	12/2022	67.0%	6.5%	16.7%	42.9%	9.6	8.3	5.8	0.5	0.5	5.8%	5.9%	0.520	UP
PUBLIC BANK BHD	4.49	87,154.0	N	12/2022	6.9%	6.5%	-0.1%	25.4%	15.4	15.4	12.3	1.8	1.7	11.4%	3.5%	4.40	MP
RHB BANK BHD	5.88	24,767.0	N	12/2022	3.6%	3.7%	-6.0%	15.7%	8.5	9.0	7.8	0.9	0.8	9.2%	5.4%	6.95	OP
Simple Average					**10.7%**	**5.2%**	**5.3%**	**21.7%**	**11.0**	**10.5**	**8.6**	**1.0**	**0.9**	**8.7%**	**4.9%**		

Source: Kenanga Research

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Building Materials

Opportunities in Aluminium and Flat Steel

OVERWEIGHT
↔

By Lum Joe Shen I lumjs@kenanga.com.my; Teh Kian Yeong I tehky@kenanga.com.my

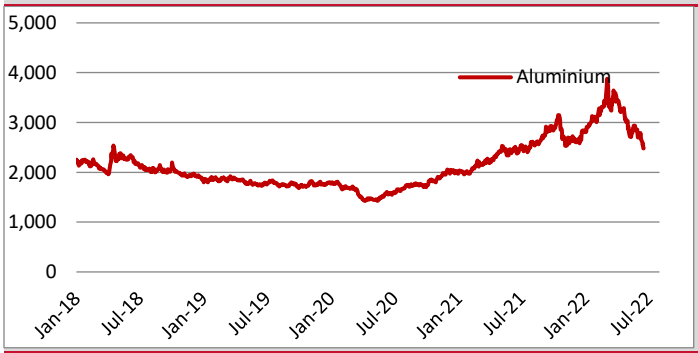
OVERWEIGHT maintained on the Building Material Sector as we are positive on aluminium and flat steel manufacturers. While aluminium price has come off peak, at above USD2,500/MT at present, it is still well above its 10-year average of USD1,950/MT. Given the lingering supply constraints, we expect aluminium prices to stay elevated over the short term. Maintain OP on PMETAL with a revised TP of RM5.95. Meanwhile, the playing field for flat steel producers has become less crowded in the wake of weak players exiting at the height of the pandemic. Coupled with the strong recovery in demand on the heels of economy re-opening in Malaysia and Singapore, the survivors, ULICORP included, now enjoy superb margins. Reiterate OP for ULICORP with an unchanged TP of RM1.85. Conversely, long steel producers now find themselves in a double whammy of weakening ASP while input cost takes off due to some price adjustment time lag, coupled with lockdown-induced volatility in their key export market, i.e. China. We therefore maintain UP on ANNJOO with a lower TP of RM0.85.

Aluminium: Prices supported by supply constraints. In line with other metals, aluminium price has retraced from its recent peak of USD3,876/MT in March 2022 to about USD2,500/MT at present. We hold the view that aluminium prices will at least hold at the current levels as global aluminium supply remains tight while demand is rapidly recovering as more economies reopen, coming out the other end of the pandemic. **PMETAL (OP; TP: RM5.95)** is poised to realise a stronger ASP given that aluminium spot prices have averaged at USD3,112/MT YTD, +26% yoy vs. an average of USD2,463/MT in 2021. Meanwhile, in terms of input cost, the alumina price to aluminium price ratio has remained relatively stable at 13.6% YTD vs. 13.7% in 2021. In addition to high aluminium prices, an additional earnings kicker for PMETAL will come from the first full-year contribution from its new P3 plant commissioned in Oct 2021. We rationalise our TP for PMETAL to RM5.95 based on DCF (a WACC of 7.5% and a terminal growth rate of 5%) from RM6.68 that was previously based on PER.

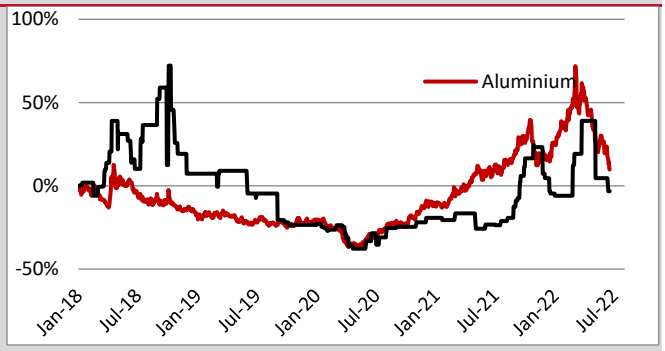
Flat steel: Better prices amidst reduced competition. Flat steel producers enjoy better margins as: (i) the playing field has become less crowded in the wake of weak players exiting at the height of the pandemic; and (ii) strong recovery seen in demand on the heels of the re-opening of the economy in Malaysia and Singapore. For **ULICORP (OP; TP: RM1.85),** its margins are further boosted by its niche cable tray products (vs. commoditised offering from competitors). Maintain OP for ULICORP with an unchanged TP of RM1.85 based on 8x FY22E PER, in line with the sector's historical average during earnings upcycles.

Long steel: Falling ASP and rising input cost, lockdowns in China. The intermittent lockdowns in some Chinese cities due to China's zero Covid-19 policy have stymied the demand for rebars and billets in China, which in turn have hurt the brisk long steel exports from Malaysia to China. **ANNJOO (UP; TP: RM0.85)**, for instance**,** has to channel its exports to South East Asian countries such as the Philippines (at reduced margins vs. China) as the demand from China wanes. Meanwhile, the cost of coking coal (raw material for coke) has skyrocketed due to a supply halt from Russia. Adding salt to the wound, are rising labour and transport costs. We downgrade ANNJOO's TP to RM0.85 (from RM1.25) based on FY22E PBV of 0.41x (from 0.6x), which is the sector's historical average PBV during downcycles.

Aluminum Prices

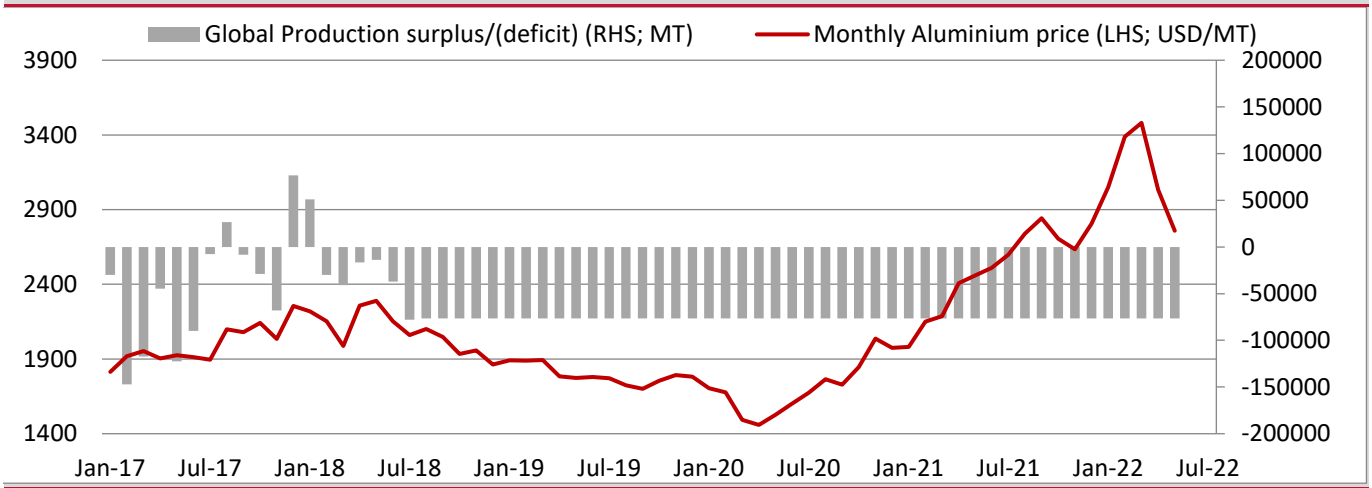


Aluminum vs. Alumina Prices – % Movement



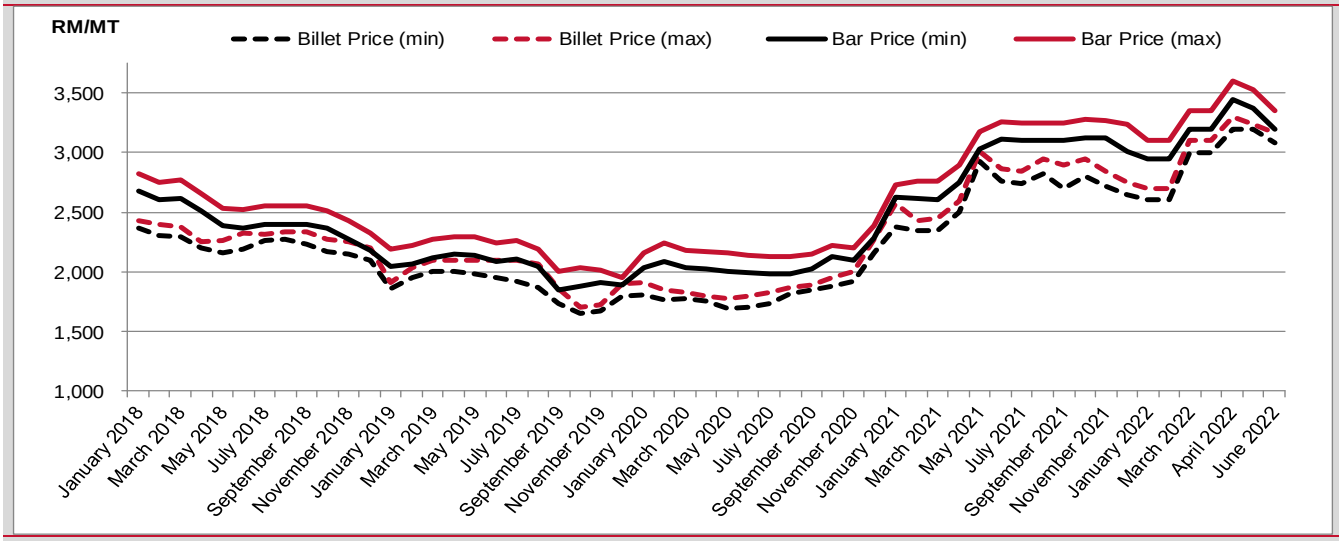
Source: Bloomberg, Kenanga Research

Global Production Surplus/Deficit vs. Monthly Aluminium Price



Source: Bloomberg, Kenanga Research

Local Long Steel Prices



Source: MITI,Kenanga Research

Peer Comparison

Name	Last Price (RM)	Market Cap	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
ANN JOO RESOURCES BHD	1.10	614.1	Y	12/2022	4.3%	-1.2%	-78.6%	-15.4%	2.8	13.3	15.5	0.5	0.5	4.5%	1.9%	1.25	UP
PRESS METAL ALUMINUM HOLDINGS BHD	4.70	38,726.2	Y	12/2022	24.1%	3.7%	90.9%	6.8%	27.9	33.4	20.7	9.9	6.4	39.7%	0.8%	5.95	OP
UNITED U-LI CORPORATION BHD	1.00	217.8	Y	12/2022	19.6%	4.5%	13.4%	7.4%	5.0	4.3	4.1	0.8	0.7	17.3%	7.0%	0.85	OP
Simple Average					**16.0%**	**2.3%**	**8.6%**	**-0.4%**	**11.9**	**17.0**	**13.4**	**3.7**	**2.6**	**20.5%**	**3.2%**		

Source: Bloomberg, Kenanga Research

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Construction

A GE15 Play

OVERWEIGHT ↑

By Lum Joe Shen I lumjs@kenanga.com.my

Upgrade to OVERWEIGHT ahead of the 15th General Election (GE15). We expect the rollout of pubic infrastructure projects to pick up ahead of the GE15 to bring about the feel-good factor, and we believe the government of the day is in the position to do so, thanks to the fiscal room freed up from the more moderate pandemic relief and vaccination spending. Post GE15, on the assumption of the emergence of a government with a stronger mandate, we expect accelerated project implementation to shield the domestic economy from the slowdown in external demand in a rising interest environment globally. Meanwhile, we are mindful of the sector's headwinds at present, i.e. labour shortage and elevated input cost, while job replenishment has been mixed with some players having successfully lifted their outstanding order-book to above the pre-pandemic levels namely GAMUDA, KERJAYA and KIMLUN, while IJM, WCT and SUNCON still having much room for improvement. Our Top Pick for the sector is GAMUDA.

A better job flow ahead of the GE15. We expect the rollout of public infrastructure projects to pick up ahead of the GE15. These could potentially include MRT3, Pan Borneo Sarawak Phase 2, Pan Borneo Sabah, flood mitigation projects and more. The government have provided their commitment to roll out these crucial jobs which we find timely as most of the ongoing infrastructure jobs are reaching tail-end i.e. MRT2, LRT3, Pan Borneo Phase 1. The tenders for the three civil packages under MRT3 will close in August 2022 and we anticipate the awards to be announced latest by early-CY23.

Gamuda has shown green shoots of recovery. Putting aside the GE factor, certain contractors under our coverage have announced significant job wins in recent months, such as Gamuda's new overseas jobs in Australia and Singapore worth RM9.5b, as well as KERJAYA's YTD wins worth RM1.1b comprising three high rise developments at Ampang, Bangsar and Penang (in STP2).

PPP/PFI projects to alleviate fiscal constraints. We acknowledge that fiscal spending is constrained by a high public debt. However, this could be alleviated by implementing public projects on PPP/PFI (public-private partnership/public finance initiative) model. For instance, (i) MRT3 will require contractors upfront funding for the first 2 years (month 1-24) of the project before being able to recoup these costs for the subsequent 2 years in equal instalments (month 25-48), (ii) flood mitigation project in the Western Klang Valley proposed by private companies i.e. SMART 2 by Gamuda, and (iii) three new proposed highways by private companies to address congestion in the Klang Valley i.e. PJD Link, Bangi Putrajaya Highway, and KL NODE.

We are mindful of sector headwinds. The two main headwinds in the current climate include shortage of labour and elevated material costs (which is unlikely to abate this year). We believe steel ASPs will remain elevated due to the higher costs of raw material needed for steelmaking i.e. iron ore, coke, and scrap amidst the geopolitical tensions and supply disruptions. As for cement, we opine that prices will no longer be as volatile but will be sticky upwards given that MCEMENT now has over 60% market share in the local market.

Prices of other key construction materials such as copper, aluminium and others have also risen in tandem driven by inflation and the tight supply-demand dynamics globally (partially due to logistical issues). While contractors would price in the overall price increases of these materials into their newly tendered contracts, we note that there will be imminently higher working capital needs which would weigh onto balance sheet and lead to higher financing requirements. Moving forward, while we expect margins to be stronger than pandemic years (upon more efficient operations given the absence of lockdowns), we do not expect margins to revert back to pre-Covid times *(refer to Table 4 in Appendix).*

Upgrade to OVERWEIGHT (from NEUTRAL). We believe a sector re-rating is in the making ahead of GE15 on anticipation of better political stability and increased project implementations. If not dissolved earlier, the parliament will head towards an automatic dissolution in July 2023, paving the way for the GE15 within the next 60 days.

Our top pick for the sector is GAMUDA given: (i) its ability to pivot into highly regulated construction regions (Singapore/Australia) and relinquishing its dependence on the lacklustre domestic space due to the current fiscal constraints, (ii) improving balance sheet post disposal of tolled highway which allows for PFI initiatives and a special dividend, and (iii) high probability of success for the MRT3 tunnelling tenders.

Table 1: Ongoing/Future projects

Ongoing/Future Projects	Value	Status	
	RM b	Ongoing	Pending
Federal Government Projects			
MRT3	31	√	
Pan Borneo Sarawak Ph2	n.a.		√
Pan Borneo Sabah	15.3	√	
JB-SG RTS	4.3	√	
Central Spine Road	10.7	√	
Sabah Sarawak Link Road	5.2	√	
Flood Mitigation Projects	n.a.	√	
Duke Phase 2A	6.3 (PFI)		√
Waste To Energy (Kepong)	n.a. (PFI)		√
PJD Link	n.a. (PFI)		√
Bangi Putrajaya Highway	n.a. (PFI)		√
KL NODE highway	n.a. (PFI)		√
State Government Projects			
Penang Transport Masterplan	46		√
Rasau Water Treatment Plant	4.5		√
Iskandar BRT	2.56	√	
Kuching Autonomous Rail Transit	6	√	

Source: Bursa, Kenanga Research

Table 2: Historical and Forward Replenishment Targets

Replenishment (RM b)	FY18A	FY19A	FY20A	FY21A	FY22 Target	FY23 Target
Gamuda	0.37	1.24	0.20	0.0	10.0	10.0
IJM	0.51	0.53	1.50	1.34	1.68 (actual)	1.90
Kerjaya	0.99	1.22	1.47	0.91	1.50	1.50
Kimlun	0.77	0.56	0.69	1.16	0.80	0.95
Suncon	1.60	1.80	2.30	1.47	1.50	2.20
Wct	2.67	0.12	1.20	1.12	1.00	1.00
Total	**6.9**	**5.5**	**7.4**	**6.0**	**16.5**	**17.6**
Total (without Gamuda)	**6.5**	**4.2**	**7.2**	**6.0**	**6.5**	**7.6**
YoY	**n.a.**	**-21%**	**35%**	**-19%**	**175%**	**6%**
YoY (Without Gamuda)	**n.a.**	**-35%**	**69%**	**-16%**	**8%**	**17%**

Source: Bursa, Kenanga Research

Table 3: Contractors Outstanding order-book

Outstanding orderbook (RM b)	FY19A	FY20A	FY21A	FY22 YTD
GAMUDA	9.2	6.9	4.5	12.4
IJM	9.4	7.8	4.5	4.2
KERJAYA	3.0	2.9	3.5	4.4
KIMLUN	2.2	1.5	1.4	2.0
SUNCON	5.2	5.2	5.1	4.4
WCT	6.4	5.0	4.7	4.4
Total	**35.4**	**29.4**	**23.7**	**31.8**
YoY	**n.a.**	**-17%**	**-19%**	**34%**

Source: Bursa, Kenanga Research

Table 4: Operating Margins (Before JVA for fair comparison)

OP Margins (before JVA)	FY18A	FY19A	FY20A	FY21A	FY22E	FY23E
GAMUDA	9.0%	7.8%	5.0%	10.4%	10.0%	12.1%
IJM (only PBT segment available)	9.6%	8.8%	8.4%	7.1%	8.0%	9.0%
KERJAYA	17.8%	18.4%	14.6%	13.8%	15.0%	14.7%
KIMLUN	9.2%	7.4%	4.4%	2.4%	6.1%	7.1%
MUHIBAH	9.1%	1.9%	3.5%	1.7%	2.4%	3.6%
SUNCON	8.2%	8.4%	6.0%	8.4%	7.8%	7.7%
WCT	7.5%	9.2%	3.4%	0.0%	7.5%	7.5%
Average	**10.1%**	**8.8%**	**6.5%**	**6.2%**	**8.1%**	**8.8%**

Source: Bursa, Kenanga Research

Table 5: Valuation levels for stocks under our coverage vs Pre GE 14

Valuations	Current Share price	# of shares	Mkt Cap	Current Fwd PER	Peak PER pre GE14 elections
Gamuda	3.60	2514	9048.6	13.3	19.0
IJM	1.74	3646	6343.2	20.5	16.5
Kerjaya	1.13	1242	1403.4	8.8	16.0
Kimlun	0.705	353	249.1	5.4	10.0
Muhibah	0.505	485	245.0	4.9	20.0
Suncon	1.56	1293	2016.9	15.9	20.0
Wct	0.440	1418	624.0	9.0	20.9

Source: Kenanga Research

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Peer Comparison

Name	Last Price (RM) 17/6/2022	Market Cap (RM'm)	Shariah Compliant	Current FYE	PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div Yld (%)	Target Price	Rating
					Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
STOCKS UNDER COVERAGE													
GAMUDA BHD	3.60	9,194.2	Y	07/2022	15.1	13.0	17.3	1.0	1.0	7.9%	3.3%	4.00	OP
IJM CORP BHD	1.74	6,146.7	Y	03/2023	25.8	20.4	19.1	0.6	0.6	3.8%	3.4%	1.90	MP
KERJAYA PROSPEK GROUP BHD	1.13	1,425.0	Y	12/2022	14.9	8.8	8.6	1.4	1.3	15.3%	4.0%	1.42	OP
KIMLUN CORP BHD	0.705	249.1	Y	12/2022	N.A.	9.2	5.7	0.4	0.3	4.0%	2.1%	1.10	OP
MUHIBBAH ENGINEERING (M) BHD	0.505	367.1	Y	12/2022	N.A.	126.3	9.7	0.2	0.3	0.2%	0.0%	0.535	MP
SUNWAY CONSTRUCTION GROUP BHD	1.56	2,011.4	Y	12/2022	15.9	15.8	15.9	3.2	3.0	19.4%	3.2%	1.52	MP
WCT HOLDINGS BHD	0.440	623.6	Y	12/2022	N.A.	7.0	8.9	0.2	0.2	4.4%	0.0%	0.620	OP
Simple Average					**17.9**	**28.6**	**12.2**	**1.0**	**1.0**	**7.9%**	**2.3%**		

Source: Bloomberg, Kenanga Research

Consumer

NEUTRAL

Undermined by Input Costs

↔

By Ahmad Ramzani Ramli I ahmadramzani@kenanga.com.my ; Tan Jia Hui / jhtan@kenanga.com.my

We stay NEUTRAL for the sector given the risks of still elevated input prices ahead. We remain positive on toplines for 2HCY22 driven by the endemic phase and easing movement restrictions for both domestic and international travelling. We remain vigilant on the somewhat slow pace of recovery amidst supply disruption, inflationary pressures and geo-political tensions. Although toplines are expected to be robust in tandem with demand, margins will likely face pressure from both elevated input costs and volatile freight charges. Given these risks, we reiterate our NEUTRAL rating for the sector but we like some undervalued large cap stocks in our universe such as AEON (OP; TP: RM1.85), F&N (OP; TP: RM26.30), PADINI (OP; TP: RM3.80), PWROOT (OP; TP: RM1.70) and MR DIY (OP; TP: RM2.65). Our top picks for this round are: (i) MR DIY, (ii) AEON, and (iii) PADINI – all benefiting from: (i) full reopening of the economy, (ii) margins looking solid unaffected by volatile raw materials prices, and (iii) solid financial muscle to absorb rising costs.

Leading indicators suggest improved sentiment. The MIER Consumer sentiment index saw an improvement in index hitting around 100 index points since the partial reopening of the economy in Sep 21 which has continued to trek northwards with the full reopening of the economy. That said, the "revenge spending" effect was strong, and we may expect a sustained growth in the 2HCY22, boosted by festivities and year-end demand in the final quarter of the year. Based on our in-house distributive trade sales forecast, we are expecting a higher rate of 15% compared to 4.0% in 2021 on higher tourism spending. Thus, we expect expansion in private consumption growth on the back of: (i) higher sales value due to higher tourist spending as borders reopened, and (ii) increase in minimum wages. We are expecting a lower unemployment rate of 3.9% compared to 4.6% in 2021, reflecting a recovery in the labour market on the back of full resumption of economic activities. Thus, we expect sustained recovery in private consumption.

Sustained growth. On endemic phase transition and minimum wage increase, we expect consumer spending to sustain in subsequent quarters. Channel checks on footfall in malls and shops are mostly favourable. Most of the stocks in our consumer universe are: (i) essential dietary items, (ii) offering goods tailored for the masses, (iii) benefitting from the reopened borders, and (iv) unfavourable Ringgit – the last two benefitting the tourism sector (and Horeca channels) and retailers in southern Malaysia. We do not expect significant inflation risk on our Consumer stocks premised on the two reasons mentioned above which would keep prices muted. However, we are cautious on margins on the back of supply chain disruptions, still-elevated commodity prices and unfavourable Ringgit.

Margins risk. Although overall EBITDA margins slide was seen in the latest financial quarter, a number of stocks either from the F&B and Retails were able to defend their margins on a combination of better product mix and operational efficiency which mitigated the elevated input costs. Global and domestic economic momentum which has been building up since last year faces renewed rising economic challenges - elevated input and logistics costs as supply tries to cope with rising demand. New geo-political tensions stoked further the inflationary pressures as energy prices surged amid volatile supply. Global economic indicators showed that input prices are likely to remain elevated posing risks to earnings, indicating that pre-pandemic level margins is still a long way off especially for the F&B producers. Our economics team expects potential improvement in supply chain conditions only in 4QCY22 on the expectation of China's gradual opening.

We maintain our NEUTRAL stance on the Consumer sector premised on uncertainties of inputs costs. The unfavorable Ringgit is compounding the challenge as most of the stocks in our consumer stocks universe are domestic players relying on imported supply of raw materials and commodities. Given such risks, we reiterate **NEUTRAL** for the sector but there are some undervalued large cap stocks in our stock coverage universe such as: **AEON (OP; TP: RM1.85), F&N (OP; TP: RM26.30), PADINI (OP; TP: RM3.80), PWROOT (OP; TP: RM1.70) and MR DIY (OP; TP: RM2.65)**. Our top picks for this round are: (i) **MR DIY**, (ii) **AEON** and (iii) **PADINI** – all benefiting from: (i) full reopening of the economy, (ii) margins looking solid unaffected by volatile raw materials prices, and (iii) financial muscle to absorb rising costs.

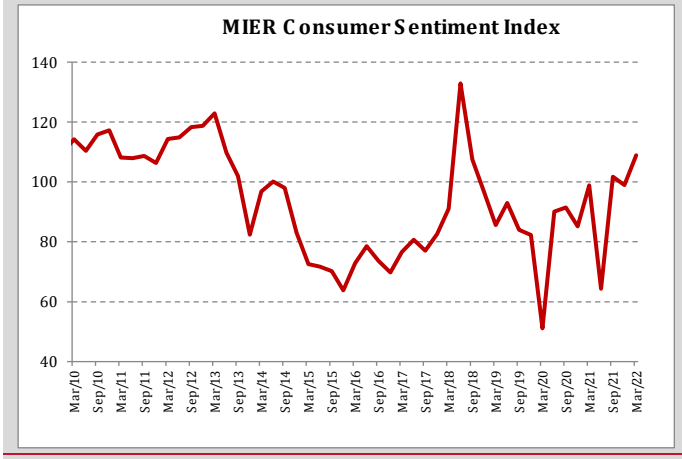
Top Picks

MR DIY (OP; TP; RM2.65). We do not see further risk from lower shopper footfall as the economy enters deeper into the endemic phase. ASP look likely to increase as its 'Price Lock' campaign has ended; we are confident that demand would be sustained as historically like in 2018, when the Group increased prices, demand was sustained. Given the inflationary pressure ahead, the Group's "low prices and quality" products will remain an attractive proposition. We take note that 54% of its outlets are located in the Central and South region – a favourable positioning given the reopened economy and consumers looking for competitively-priced goods. Despite elevated inputs costs, management guided for 40%-41% GP margin for FY22 boosted by the passing of rising costs to consumers. TP is anchored on FY23E PER of 34x (vs. regional peers of 29x). The high PER is justified based on: (i) robust growth potential, driven by sustainable market demand for its products, and stores expansion, (ii) its unchallenged position in the domestic space, (iii) strong GP margins (c.40% vs peers of 32%) with the absence of near- and long- term margin volatility thanks to its supply source China's massive economies of scale, (iv) robust balance sheet providing ample cash for expansion, and (v) net cash position ahead, allowing MR D.I.Y. to deliver sustainable dividends.

PADINI (OP; TP: RM3.80). We expect consumer spending to persist in 2HCY22. We believe that the increased minimum wages may benefit PADINI by improving its topline growth through higher consumer buying power but remain cautious on margins due to supply chain disruption and inflationary pressure. However, we expect a slight improvement in the inventory level with the easing of lockdowns in China – supported by a strong net cash position to front-load its inventory level, shielding PADINI from volatile supply issues. We understand that the company will continue to with its stores expansion in CY22/CY23. 3QCY22 margins suffered a dip due to higher administrative costs and lower footfall after the festive season. Reiterate OP with TP of RM3.80 at FY23E PER of 21.2x, which is at a slight premium to our sector average forward PER of 20x, to account for: (i) recovering footfall traffic, (ii) favourable product mix, and (iii) its net cash position.

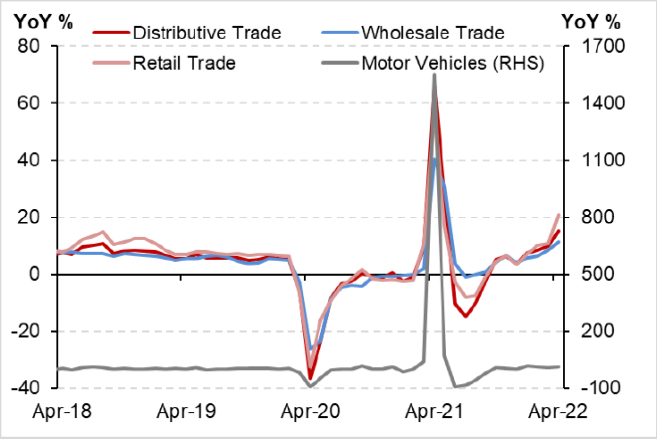
AEON (OP; TP: RM1.85). With the increase in mall footfall, we understand that the company will see pent-up demand for its the store occupancy improving further its property management segment. We see a higher occupancy rate than pre-pandemic in 1QCY22. We expect flattish growth in the retail business with consumers still in a "retaliatory consumption" mood. That said, we expect sales contribution in softline and hardline will continue to improve, with foodline remaining sustained. 1QFY22 EBIT margin fell by 4.7% due to year-end annual rebate recognition. Maintain OP with TP of RM1.85 based on FY23E PER of 21x (vs. sector average forward PER of 20x), on: (i) new occupancy streamlining revenue, (ii) retail business remaining sustained, and (iii) store expansion and rejuvenation plans.

Chart 1: MIER Consumer Sentiment Index – improved sentiments since Sep 21



Source: MIER, Kenanga Research

Chart 2: Sales Value on the Uptrend



Source: Dept. of Statistics, CEIC, Kenanga Research

Table 1: Revenue (RMm)

	1QCY21	2QCY21	3QCY21	4QCY21	1QCY22
F&B					
DLADY	258.6	284.0	290.7	300.4	299.9
F_N	1,091.8	1,059.6	896.3	1,106.6	1107.7
Nestle	1,448.8	1,379.8	1,438.7	1,466.5	1693.8
PWROOT	65.0	74.7	80.8	95.5	96.9
QL	1,213.8	1,225.4	1,248.1	1,400.8	1373.1
	4,078.1	**4,023.6**	**3,954.5**	**4,369.9**	**4,571.4**
QoQ (%)	***4%***	***-1%***	***-2%***	***11%***	***5%***
YoY (%)		***16%***	***4%***	***11%***	***12%***
Retail					
AEON	1,013.5	874.2	750.6	992.1	1001.8
AMWAY	353.7	355.9	383.9	392.4	391.2
MyNews	69.6	62.9	69.7	93.4	N.a
MR DIY	870.2	759.8	768.0	975.4	905.2
PADINI	262.9	209.8	81.4	427.2	329.3
SEM	657.1	676.7	680.2	795.1	840
	3,227.0	**2,939.3**	**2,733.9**	**3,582.1**	**3,467.5**
QoQ (%)	***11%***	***-9%***	***-7%***	***31%***	***-3%***
YoY (%)		***11%***	***-12%***	***23%***	***7%***
SIN					
BAT	566.6	595.8	613.0	861.9	521.6
C'Berg	532.0	349.2	349.3	542.3	653.9
HEIM	547.7	349.4	389.8	692.3	698.3
	1,646.3	**1,294.4**	**1,352.2**	**2,096.5**	**1,873.7**
QoQ (%)	***0%***	***-21%***	***4%***	***55%***	***-11%***
YoY (%)		***19%***	***-12%***	***27%***	***14%***
Overall QoQ %	***5%***	***-8%***	***-3%***	***25%***	***-1%***
Overall YoY %		***15%***	***-5%***	***18%***	***11%***

Table 2 : EBITDA (RM m)

	1QCY21	2QCY21	3QCY21	4QCY21	1QCY22
F&B					
DLADY	32.0	44.9	39.4	207.2	36.4
F_N	207.2	152.8	94.9	139.7	143.5
Nestle	275.5	232.1	266.2	206.5	346
PWROOT	2.1	4.5	8.0	9.0	15.1
QL	214.3	131.4	140.3	166.4	156.7
	731.0	**565.6**	**548.7**	**728.8**	**697.7**
QoQ (%)	***17.4%***	***-22.6%***	***-3.0%***	***32.8%***	***-4.3%***
YoY (%)		***6%***	***1%***	***17%***	***-5%***
Industry Margins	17.9%	14.1%	13.9%	16.7%	15.3%
Retail					
AEON	193.1	176.6	113.9	241.8	194.1
AMWAY	31.1	19.1	14.7	6.2	31.2
MyNews	3.2	19.2	(0.3)	5.4	N.a
MR DIY	237.1	182.9	194.0	259.3	212.1
PADINI	49.6	48.4	11.6	113.3	79.8
SEM	83.7	73.6	80.7	114.1	106.9
	597.8	**519.8**	**414.7**	**740.1**	**624.1**
QoQ (%)	***9.1%***	***-13.0%***	***-20.2%***	***78.5%***	***-15.7%***
YoY (%)		***21.1%***	***-30.7%***	***35.1%***	***4.4%***
Industry Margins	18.5%	17.7%	15.2%	20.7%	18.0%
SIN					
BAT	90.2	109.9	111.2	112.9	85.1
C'Berg	93.8	57.1	42.9	87.2	125.1
HEIM	115.3	51.2	84.5	146.3	172.5
	299.3	**218.1**	**238.6**	**346.4**	**382.7**
QoQ (%)	***18%***	***-27%***	***9%***	***45%***	***10%***
YoY (%)		***105%***	***-4%***	***36%***	***28%***
Industry Margins	**18%**	**17%**	**18%**	**17%**	**20%**
Overall QoQ %	*14%*	*-20%*	*-8%*	*51%*	*-6%*
Overall YoY %		*22%*	*-14%*	*27%*	*5%*

Source: Bloomberg, Kenanga Research

Table 3: EBIT (RM m)

	1QCY21	2QCY21	3QCY21	4QCY21	1QCY22
F&B					
DLADY	23.0	35.9	29.4	198.2	27.8
F_N	139.1	118.6	61.2	108.3	111.9
Nestle	228.0	185.3	215.5	157.3	297.8
PWROOT	0.3	2.7	6.2	7.2	13.3
QL	158.7	68.8	82.6	109.1	103.9
	549.1	**411.3**	**395.0**	**580.1**	**554.7**
QoQ (%)	***13%***	***-25%***	***-4%***	***47%***	***-4%***
YoY (%)		***2%***	***-6%***	***20%***	***1%***
Industry Margins	**13%**	**10%**	**10%**	**13%**	**12%**
Retail					
AEON	72.7	60.7	(1.2)	128.7	83.4
AMWAY	26.9	10.8	10.7	1.9	26.8
MyNews	(6.2)	(9.5)	(9.6)	(4.8)	**N.a**
MR DIY	185.2	127.3	138.4	194.0	149.5
PADINI	21.7	18.3	(16.3)	86.1	47.2
SEM	35.1	24.0	30.5	64.8	61.9
	335.4	**231.7**	**152.5**	**470.7**	**368.8**
QoQ (%)	***18%***	***-31%***	***-34%***	***209%***	***-22%***
YoY (%)		***40%***	***-55%***	***65%***	***10%***
Industry Margins	10%	8%	6%	13%	11%
SIN					
BAT	86.8	106.6	108.0	109.8	82.1
C'Berg	83.0	46.2	30.4	87.1	113.8
HEIM	97.6	33.4	67.6	125.4	155.7
	267.3	**186.1**	**206.0**	**322.3**	**351.5**
QoQ (%)	***22%***	***-30%***	***11%***	***56%***	***9%***
YoY (%)		***152%***	***-6%***	***47%***	*32%*
Industry Margins	**16%**	**14%**	**15%**	**15%**	**19%**
Overall QoQ %	*17%*	*-28%*	*-9%*	*82%*	*-7%*
Overall YoY %		*29%*	*-23%*	*39%*	*11%*

Table 4 : Net Profit (RM m)

	1QCY21	2QCY21	3QCY21	4QCY21	1QCY22
F&B					
DLADY	20.16	16.88	27.29	20.38	183.47
F_N	136.80	103.51	96.14	58.68	92.95
Nestle	132.49	175.16	134.53	148.02	112.10
PWROOT	7.17	1.70	2.04	5.64	6.02
QL	80.51	117.97	45.24	50.73	68.74
	377.12	**415.22**	**305.23**	**283.46**	**463.27**
QoQ (%)	***23.9%***	***10.1%***	***-26.5%***	***-7.1%***	***63.4%***
YoY (%)			***7.0%***	***-6.9%***	***22.8%***
Industry Margins	9.6%	10.2%	7.6%	7.2%	10.6%
Retail					
AEON	22.0	10.9	(18.7)	71.0	28.1
AMWAY	20.1	7.9	8.0	0.9	20.2
MyNews	(8.0)	(11.2)	(7.1)	0.0	**N.a**
MR DIY	124.8	82.1	90.4	134.6	100.5
PADINI	12.2	10.5	(16.9)	60.9	32.6
SEM	13.5	3.6	8.9	32.8	31.2
	184.7	**103.8**	**64.6**	**300.1**	**212.6**
QoQ (%)	***20%***	***-44%***	***-38%***	***365%***	***-29%***
YoY (%)		***97%***	***-65%***	***95%***	***15%***
Industry Margins	6%	4%	2%	8%	6%
SIN					
BAT	63.1	71.6	78.7	71.5	52.3
C'Berg	67.8	37.4	27.0	67.2	92.8
HEIM	73.5	25.3	51.0	95.8	113.4
	204.5	**135.3**	**156.1**	**235.5**	**258.4**
QoQ (%)	***23%***	***-34%***	***15%***	***51%***	***10%***
YoY (%)		***189%***	***-6%***	***41%***	***26%***
Industry Margins	***12%***	***10%***	***12%***	***11%***	***14%***
Overall QoQ %	*15%*	*-32%*	*-7%*	*98%*	*-12%*
Overall YoY %		*41%*	*-23%*	*43%*	*9%*

Source: Bloomberg, Kenanga Research

Peer Comparison

Name	Last Price (RM) (As of 17 Jun 2022)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div Yld (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
F&B AND RETAIL																	
7-ELEVEN MALAYSIA HOLDINGS BHD	1.42	1,599.4	N	12/2022	10.2%	-2.6%	79.2%	-5.8%	36.1	20.2	21.4	12.9	11.6	60.6%	3.5%	1.70	OP
AEON CO (M) BHD	1.43	2,007.7	Y	12/2022	20.2%	4.4%	32.5%	8.8%	23.5	17.8	16.3	1.2	1.1	6.5%	2.9%	1.85	OP
AMWAY MALAYSIA HOLDINGS BHD	5.02	825.2	Y	12/2022	-10.0%	-5.0%	62.6%	-4.8%	22.4	13.8	14.5	3.7	3.5	26.1%	5.4%	5.30	MP
DUTCH LADY MILK INDUSTRIES BHD	32.78	2,097.9	Y	12/2022	1.0%	1.0%	-67.3%	5.2%	8.5	25.8	24.6	5.5	4.9	19.9%	1.5%	35.60	MP
FRASER & NEAVE HOLDINGS BHD	19.70	7,225.5	Y	09/2022	4.8%	6.4%	-16.5%	3.5%	18.3	21.9	21.2	2.6	2.4	11.4%	2.5%	26.30	OP
MR. D.I.Y	2.89	18,161.7	Y	12/2022	27.6%	16.1%	39.3%	23.5%	42.0	30.2	24.5	15.8	12.3	45.8%	1.6%	4.00	OP
MYNEWS HOLDINGS BHD	0.570	388.8	N	10/2022	61.2%	13.1%	-138.8%	5.7%	N.A.	23.2	22.0	2.7	2.5	11.1%	1.8%	0.850	OP
NESTLE (MALAYSIA) BHD	131.20	30,766.4	Y	12/2022	7.4%	4.6%	23.3%	-9.2%	54.0	43.8	48.2	52.8	50.8	118.3%	2.2%	136.50	MP
PADINI HOLDINGS BHD	3.37	2,217.2	Y	06/2022	23.3%	32.2%	123.6%	-4.1%	41.1	18.4	19.1	2.8	2.7	14.8%	3.6%	3.80	OP
POWER ROOT BHD	1.67	659.6	Y	03/2023	8.2%	7.9%	7.3%	-6.8%	26.7	24.9	26.7	2.4	2.3	13.4%	5.4%	1.70	OP
QL RESOURCES BHD	5.00	12,168.3	Y	03/2023	17.5%	9.3%	23.9%	26.7%	56.0	45.2	35.7	4.1	4.0	9.5%	1.2%	5.45	MP
Simple Average					**15.6%**	**8.0%**	**15.4%**	**3.9%**	**32.9**	**25.9**	**24.9**	**9.7**	**8.9**	**30.7%**	**2.9%**		
SIN																	
BRITISH AMERICAN TOBACCO (M) BHD	11.50	3,283.6	N	12/2022	-2.4%	-1.0%	-10.2%	5.5%	11.5	12.8	12.2	8.6	8.3	65.8%	7.4%	13.40	OP
CARLSBERG BREWERY MALAYSIA BHD	21.84	6,677.5	N	12/2022	31.3%	6.0%	38.0%	15.1%	32.4	23.5	20.4	31.2	31.2	130.8%	4.3%	28.05	OP
HEINEKEN MALAYSIA BHD	23.80	7,189.9	N	12/2022	30.8%	11.1%	32.8%	16.9%	29.3	22.0	18.9	18.2	18.2	82.5%	4.5%	27.40	OP
Simple Average					**19.9%**	**5.4%**	**20.2%**	**12.5%**	**24.4**	**19.5**	**17.1**	**19.3**	**19.2**	**93.0%**	**5.4%**		

Source: Bloomberg, Kenanga Research

Gaming

Better Days Ahead

OVERWEIGHT
↔

By Teh Kian Yeong I tehky@kenanga.com.my

We remain optimistic of the earnings recovery story for the Gaming Sector with borders reopened from 1st of April for both Malaysia and Singapore which likely means the worst could be over for casino operators as tourists return. The casino operators have geared up to roll out capacity in preparation for the reopening, which led to higher opex in 1QFY22 and this high opex position will persist in the coming quarters but the expected higher tourists flow should be sufficient to offset this. On the other hand, we expect a quicker recovery for the NFO players as opposed to the casino operators given the former's domestic-driven consumption while the latter have foreign clienteles. As such, NFO players are likely to see ticket sales recovering fully to pre-COVID-19 levels as early as end-2022 while the casino operators are likely to see business volume recover fully by 2HCY23. In all, we maintain our OVERWEIGHT rating for the sector.

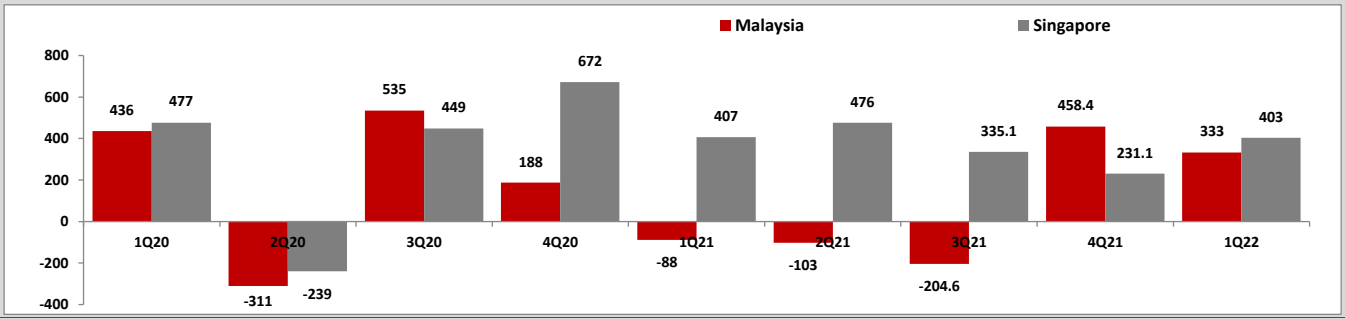
Earnings recovery is on the way; OVERWEIGHT reiterated. With COVID-19 now deeper into the endemic phase, more countries are opening up their international borders. We believe the worst is over for the gaming sector, one of the hardest pandemic-hit sectors in the past two years, especially the casino operators which would be a major beneficiary of earnings recovery theme this year. We still prefer **GENTING (OP; TP: RM5.86**) over **GENM (OP; TP: RM3.87)** for multi-recovery plays in GENM, and **GENS (NOT RATED)** as well for the new wholly-owned casino *Resorts World Las Vegas (RWLV)*. For income seekers, NFOs are the best yielding stocks for sustainable attractive dividend yield of >7% and **SPTOTO (OP; TP: RM2.33)** is our preferred pick over **MAGNUM (MP; TP: RM1.93)** for better NFO recovery and consistency of earnings. Overall, we maintain OVERWEIGHT on the Gaming Sector.

Casino: borders reopened; earnings prospects to improve further. Malaysia and Singapore have already reopened its borders from April 1, which allow international tourists in without having to quarantine. This is expected to have positive impact on GENM's *Resorts World Genting (RWG)* and GENP's *Resorts World Sentosa (RWS).* In May, *RWG* opened only 5,000 hotel rooms (88% occupancy) out of its 10,500 available rooms at the hilltop resort. Therefore, there are ample rooms for *RWG* to accept bigger crowds. In addition, the newly opened theme park *Genting SkyWorlds* (in early Feb), should be able to broaden GENM's non-gaming revenues. Meanwhile, GENM's UK and USA operations have produced commendable results in the past one year after the reopening/relaxation of operating restriction. Nonetheless, GENM's operating costs would stay elevated in the coming quarters given the start-up costs arising from the ramp-up of operation in preparation for the economy reopening. Similarly, GENS is also investing SGD400m in 2022 for RWS2.0 and related refurbishment works for the theme park and three of its hotels in preparation for the reopening. All these should eventually benefit parent-company GENTING as well as the fairly new wholly-owned *RWLV*.

NFO: ticket sales recovery on the right path. We still expect NFO ticket sales to recover fully to pre-COVID-19 levels in 2HCY22 from c.80%-85% currently as new lockdowns are unlikely given that the country has entered the endemic phase. In fact, SPTOTO's 3QFY22 ticket sales hit 96% of pre-COVID-19 levels thanks largely to Toto 6/58 jackpot run while MAGNUM's 1QFY22 ticket sales only posted 72% recovery rate against pre-COVID-19 levels which we believe could have been cannibalised by SPTOTO's jackpot run. Going forth, enforcement on illegal operators remain the key to ticket sales growth where the licensed NFO players saw their ticket sales growing substantially in 2HCY19 with strong enforcement on the illegal operators back then. This led us to believe that 2023 will be the full recovery year in earnings and makes its attractive dividend yield of >7% sustainable. Overall, we prefer SPTOTO over MAGNUM for its earnings consistency and quicker ticket sales recovery.

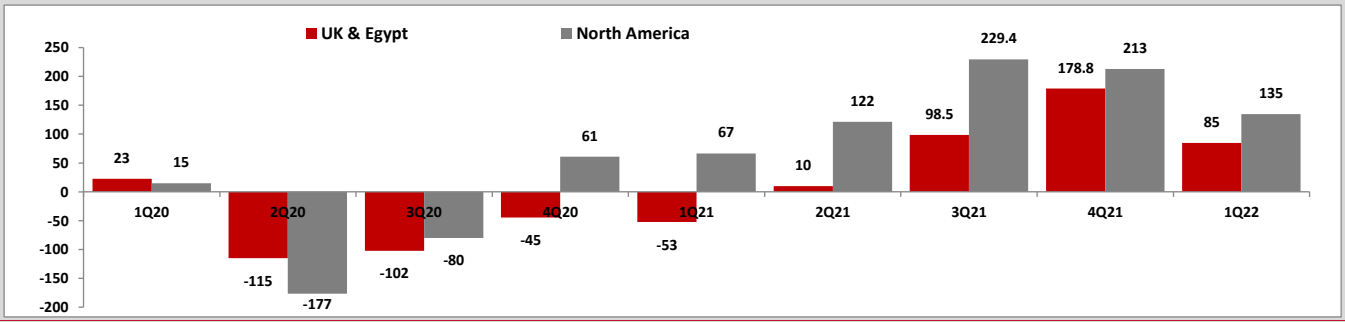
Better earnings from 2QCY22 onward. After a disappointing 1QCY22 owing to higher operating expenses in preparation of reopening for casinos operators and slower-than-expected ticket sales (MAGNUM), we expect earnings rebound in the coming 2QCY22 as border reopened, which could mean GENM and GENS are likely to experience growing volume from 2QCY22 onwards while MAGNUM is also likely to see improving ticket sales as the jackpot run at SPTOTO had ended. As such, we believe casino business volume is likely to recover to pre-COVID-19 levels only in 2HCY23 while SPTOTO could see normalising ticket sales in its upcoming 4QFY22 results after the exceptionally strong ticket sales in 3QFY22 owing to the abovementioned jackpot run. On the other hand, we expect a quicker recovery in ticket sales as early as end-2022 as compared to casino volume business by 2HCY23 as the former is mainly driven by domestic consumption. Overall, as we enter deeper into the endemic phase of COVID-19, we expect a meaningful recovery for the industry players in 2022 and a full recovery from 2023 onwards.

GENTING: EBITDA - Malaysia vs. Singapore (RM m)



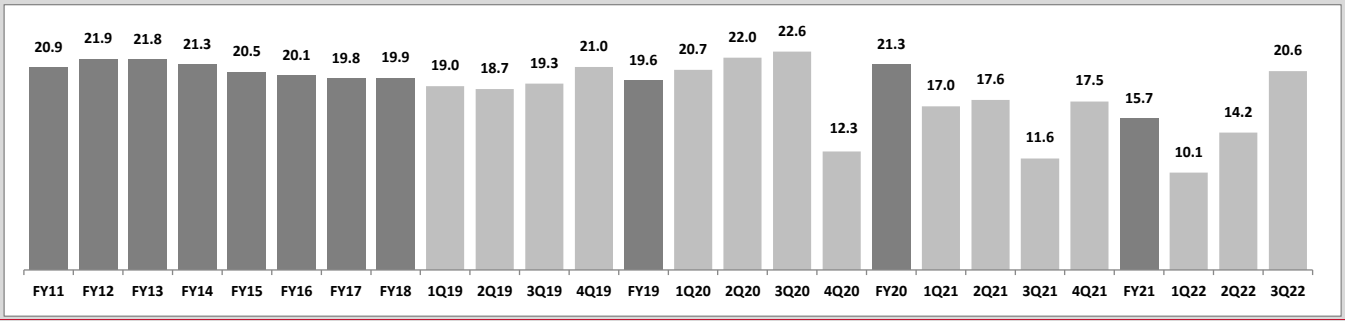
Source: Company

GENTING: EBITDA – UK & Egypt vs. North America (RM m)



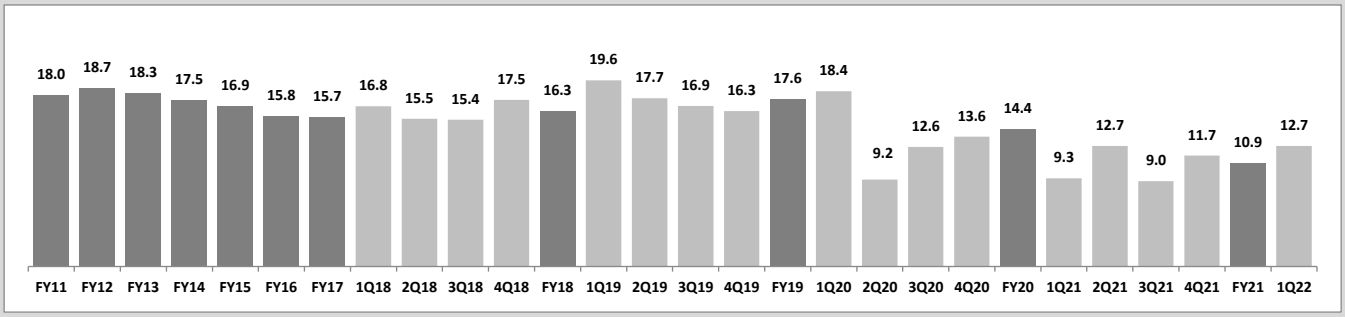
Source: Company

SPTOTO: Average Ticket Sales Per Draw (RM m)



Source: Company

MAGNUM: Average Ticket Sales Per Draw (RM m)



Source: Company

Peer Comparison

Name	Price @ 17 Jun 2022	Market	Shariah	Current	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div.Yld. (%)	Target	Rating
	(RM)	Cap (RM'm)	Compliant	FYE	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	Price (RM)	
SPORTS TOTO BHD	1.91	2,558.2	N	06/2022	4.4%	27.2%	-0.5%	58.5%	14.2	14.2	9.0	3.2	3.1	22.0%	5.6%	2.33	OP
GENTING BHD	4.56	17,558.6	N	12/2022	75.6%	1.9%	118.8%	39.8%	N.A.	13.4	9.6	0.5	0.5	4.0%	3.3%	5.86	OP
GENTING MALAYSIA BHD	2.81	15,919.2	N	12/2022	137.7%	2.5%	3.5%	61.6%	N.A.	22.4	13.9	1.2	1.2	5.4%	4.3%	3.71	OP
MAGNUM BHD	1.64	2,357.0	N	12/2022	75.3%	9.0%	79105.6%	38.1%	13,094.5	16.5	12.0	1.0	1.0	6.0%	4.8%	1.93	MP
Simple Average					**73.3%**	**10.1%**	**19806.8%**	**49.5%**	**6554.3**	**16.6**	**11.1**	**1.5**	**1.4**	**9.3%**	**4.5%**		

Source: Bloomberg, Kenanga Research

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Gloves

UNDERWEIGHT

↓

Oversupply to Persist

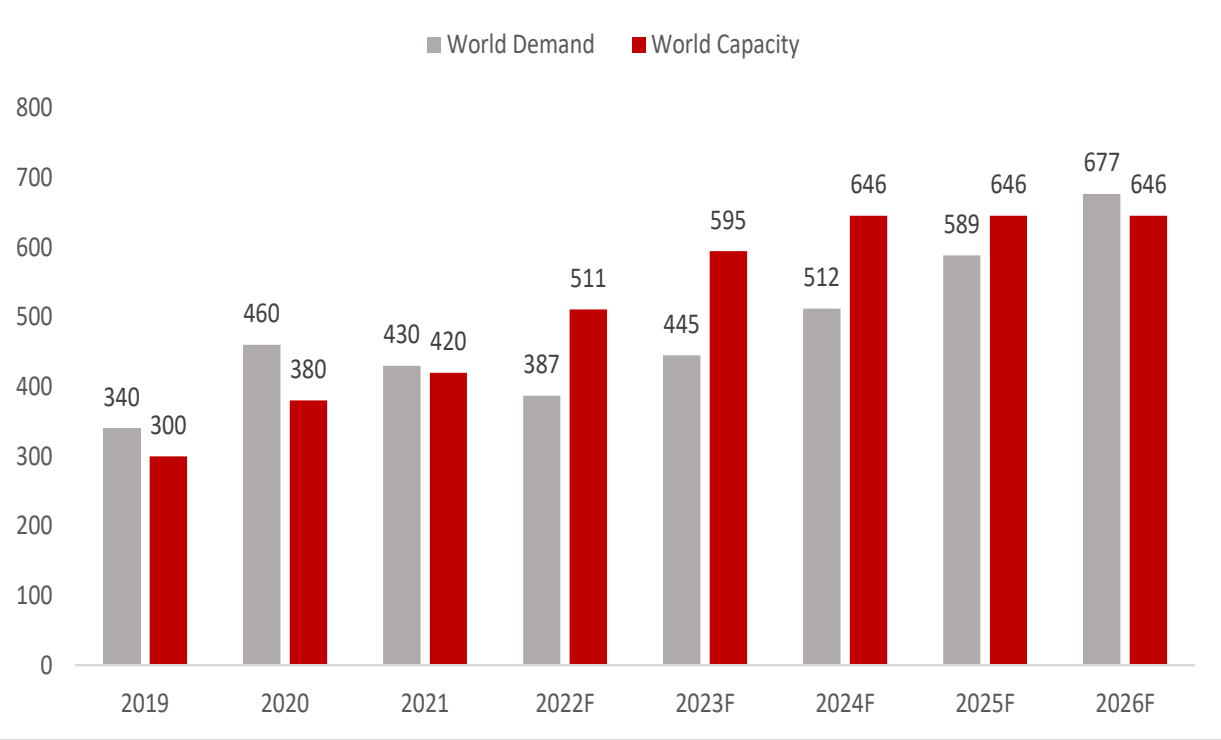
By Raymond Choo Ping Khoon I pkchoo@kenanga.com.my

Downgrade to Underweight from Neutral. Indications from our supply-demand analysis are pointing towards excess capacity in the sector spanning the next two years. Hence, we expect the weak operating environment to continue to weigh down glove makers over the medium term to long-term. Specifically, industry leader TOPGLOV's recently released results are already indicating weaker earnings ahead for glove makers suggesting that earnings have yet to bottom out. This is due to crimped margins arising from the mismatch between ASP and inability to fully past cost through, further exacerbated by low industry plant utilization averaging 50-60% which appears to likely persist over the medium term. The situation is further aggravated by the softening demand as evident from the low utilization rate of glove players leading to oversupply putting pressure on ASP coupled with customers' reluctance to commit to sizeable orders as they expect selling prices to ease further. Our ratings are as follows: HART (MP; TP: RM2.90), TOPGLOV (UP; TP: RM0.80), KOSSAN (UP; TP: RM1.20) and SUPERMX (UP; TP: RM0.65).

Excess supply and low utilization to weigh down on earnings. We expect ASP to remain in the doldrums in 2H 2022. As a result of massive capacity expansion by incumbent players as well as new players during the pandemic years — enticed by the super fat margins that had eventually evaporated — we estimate that the global glove manufacturing capacity has jumped by 22% to 511b pieces in 2022 (see chart on the following page). On the other hand, as more countries come out the other end of the pandemic, we project the global demand for gloves to ease by 10% in 2022 to 387b pieces (partly also due to the destocking activities along the distribution network). This will result in an excess supply of 124b pieces (assuming, hypothetically, capacity utilisation is maximised). In 2023, we estimate that the global glove manufacturing capacity to surge by another 16% to 595b pieces (as more capacity planned during the pandemic years finally comes on-line) while the global demand for gloves shall resume its organic growth of 15% annually (taking our cue from MARGMA's projection of 10-15% growth in global glove demand yearly), resulting in the excess supply rising further to 150 b pieces. Based on our estimates, the demand-supply situation will only start to head towards equilibrium in 2025 when there is virtually no more new capacity coming onstream while the global demand for gloves continues to rise by 15% per annum underpinned by rising hygiene awareness.

All in, the industry excess supply could well mean that glove players have less pricing power to pass costs through and the situation is further aggravated by low industry utilization rate putting pressure on margins. The recent round of results reported by glove makers suggested that glove makers' earnings have yet to bottom with ASP expected to continue declining with the low plant utilization averaging 50-60% likely to persist over the medium term amidst intense competition. The situation is further aggravated by the softening demand as evident by the low utilization rate of glove players leading to oversupply putting further pressure on ASP coupled with customers' reluctance to commit to sizeable orders as they expect selling prices to ease further. Based on the results announced by glove players, the followings are our observations:- (i) players are unable to fully pass on the cost increase due to the current oversupply situation which is expected to remain challenging; (ii) apart from reduced economies of scale arising from volume that is less than optimum on the back of the soft demand evident from the low utilisation rate, glove players are experiencing margins erosion as raw materials costs are not adjusting down as fast as ASP; (iii) ASP over the short to medium term could be lower than pre-pandemic level due to the current supply-demand imbalance as evident in historically low utilization of 50-60% but some players see margins bottoming; (iv) current industry utilisation rate of 50-60% is expected to put brakes on excessive new capacity of which in our view is expected to put some near-term pressure on ASP; and (v) in terms of M&A – the players under our coverage have been approached by potential sellers but lack urgency given the excess industry capacity.

Estimated Global demand/supply - excess supply over CY22-CY24



Source: Kenanga Research

Estimated production capacity from Malaysia, China, Thailand and Others

Billion pieces	CY22F	CY23F	CY24F
Malaysia	328	379	405
China	80	105	125
Thailand	68	76	81
Others	35	35	35
Total	511	595	646
Chg (%)	+22	+16	+9

Source: Kenanga Research

Peer Comparison

Name	Price(RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net DivYld (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
GLOVES																	
HARTALEGA HOLDINGS BHD	2.71	9,214	Y	03/2023	-55%	-3%	-89%	8%	2.8	25.1	23.2	1.8	1.7	7.1%	2.2%	2.90	MP
KOSSAN RUBBER INDUSTRIES	1.33	3,402	Y	12/2022	-59%	-5%	-92%	2%	1.2	14.5	14.3	0.8	0.8	5.8%	4.5%	1.20	UP
SUPERMX CORP BHD	0.850	2,313	Y	06/2022	-55%	-40%	-84%	-78%	0.6	3.7	16.6	0.5	0.4	12.6%	9.4%	0.650	UP
TOP GLOVE CORP BHD	1.01	8,282	Y	08/2022	-60%	-7%	-96%	-1%	1.1	27.3	27.6	1.4	1.5	5.2%	1.9%	0.800	UP

Source: Bloomberg, Kenanga Research

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Healthcare

Resilient in Facing Sustained Elevated Inflation

OVERWEIGHT ↑

By Raymond Choo Ping Khoon I pkchoo@kenanga.com.my

Upgrade to Overweight from Neutral. In the face of sustained elevated inflation, we like private hospitals given the inelastic demand of healthcare; hence, their ability to pass higher cost through. We believe that the healthcare industry will continue to enjoy growth, supported by growing healthcare expenditure, rising medical insurance coverage, and an ageing population demographic. In terms of stock exposure, we like IHH for: (i) its pricing power, as the inelastic demand of healthcare provides it the ability to pass cost through amidst rising inflation, (ii) strong pent-up demand from domestic and international patients of which the group have started seeing from end-Mar 2022, and (iii) commanding material market position in countries it operates in. KPJ suffered from lack of re-rating catalysts while its new hospitals under gestation period could continue to be a drag on earnings; hence, we reiterate our Market Perform call. Our calls are as follows: IHH (OP; TP: RM7.20), KPJ (MP; TP: RM0.87) and Pharmaniaga (MP; TP: RM0.64).

IHH taking inflation in its stride. Given the low "price elasticity of demand" of private healthcare services, IHH has been able to pass on cost inflation to customers, as reflected in its rising revenue per inpatient over the past several quarters. We highlight that its list prices have been adjusted for inflation in 1QFY22. There have been strong returns of domestic patients as well as growth in foreign patients in Malaysia and Singapore. Specifically, the group in April 2022 saw a strong return of local and foreign patients. In Turkey (80% bed occupancy rate) and Europe, IHH foresees the high bed occupancy rates to continue. While in India, it expect gradual improvement of non-Covid patients starting from 2QFY22 since 1QFY22 saw depression in low elective surgeries due to the omicron wave. IHH's investment appeal lies in: (i) its pricing power, as the inelastic demand of healthcare needs provides it with the ability to pass cost through amidst rising inflation, (ii) strong pent-up demand from domestic and international patients of which the group have started seeing from end-Mar 2022, and (iii) commanding market position in countries it operates in.

Pedestrian earnings growth for Pharmaniaga. Despite recording bumper profits in FY21, we do not expect FY22 to chalk up positive net profit growth since most of the vaccines delivery has been completed. Leveraging on the experience and expertise in manufacturing fill and finish of the Sinovac COVID-19 vaccine, the Group intends to export the vaccine to countries such as Indonesia, Philippines, Cambodia, Thailand and several African nations that are facing vaccine supply shortages. Pharmaniaga is actively negotiating with Sinovac Biotech Ltd to secure a deal to allow the Group to speed up the supply of vaccines to these countries. The Group is in the midst of finalising the logistics and distribution contract extension agreement with the Ministry of Health Malaysia, slated to be completed by 3Q 2022. Going forward, the Group is strengthening its business footprint in Indonesia as it has huge untapped potential. In Indonesia, the division has successfully staged a swift turnaround, highlighting the effectiveness of the reorganisation of the Indonesian business to enhance its operational efficiency through an ongoing stock optimisation exercise and aggressive payment collection. However, due to the negative earnings growth forecast and a high net gearing at 2x, we conservatively **lowered our TP from RM0.71 to RM0.64** based on 11x FY23E EPS (previously 12x), at a 25% discount to peers' average of 14x due to its smaller market capitalisation. The saving grace is a 6% dividend yield.

KPJ lacking re-rating catalysts, Reiterate MP. KPJ suffered from lack of re-rating catalyst while its new hospitals under gestation period could continue to be a drag on earnings. The Group will continue to take advantage of government's incentives in order to mitigate the adverse effects of the pandemic. However, its new hospitals such as KPJ Bandar Dato' Onn, KPJ Batu Pahat, KPJ Perlis and KPJ Miri which are currently under gestation period could continue to drag overall earnings. Although we like KPJ for the following reasons:- (i) inelastic demand of healthcare needs hence ability to pass cost through amidst rising inflation, and (ii) having the largest hospitals network locally, catalysts are lacking despite its share price falling to seemingly attractive levels at mean PER. **Hence, our TP is nudged down from RM0.97 to RM0.87 based on 25x FY23E EPS, at a 20% discount to regional peers' average due to its smaller market capitalisation.**

Peer Comparison

Name	Price @ 17/6/22 (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div Yld (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
HEALTHCARE																	
IHH HEALTHCARE BHD	6.28	55,281	Y	12/2022	6%	6%	2%	11%	34.6	33.8	30.6	2.5	2.3	7.1%	1.0%	7.20	OP
KPJ HEALTHCARE BERHAD	0.850	3,692	Y	12/2022	9%	7%	140%	18%	70.0	29.2	24.7	1.7	1.6	5.6%	1.4%	0.870	MP
PHARMANIAGA BERHAD	0.605	793	Y	12/2022	-20%	-10%	-45%	-18%	4.6	8.4	10.2	1.8	1.6	20.1%	6.6%	0.640	MP

Source: Bloomberg, Kenanga Research

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Media

Difficult Transition to the Endemic Phase

NEUTRAL

↓

By Ahmad Ramzani Ramlil *ahmadramzani@kenanga.com.my*

Downgrade to NEUTRAL from OVERWEIGHT. Despite improved adex numbers, we have yet to see a full recovery of the segment as media players continue to suffer from lingering effects of the pandemic. Even as we enter the endemic stage, meaningful recovery of the cinema and in-store media segments has yet to be seen. Digital avenues continue to grow but TV remains the largest segment. ASTRO (MP; TP: RM1.00), the major satellite TV player, saw a fall in both their top and bottom lines as rising costs, a stagnating subscriber base and limited deployment of their ISP venture continued to dent margins. MEDIA (OP; TP: RM0.74), on the other hand, continued to display resilient growth as their Omnia segment is up 33% YoY. Overall, we downgrade the media sector to NEUTRAL.

CY22 looks like a mixed bag. Despite projected increase in adex for CY22, the outlook for the year seems neutral overall. Given the estimated increase in licensing fees for TV players and persistently lagging print and in-person mediums, the growth in top-line looks to be offset by operating costs. Based on our most recent round of results, we surmise the following: (i) TV numbers continue to stagnate as ASTRO, the major satellite TV player, continued to display marginal falls in viewership. Despite the growth in TV adex, projected decreased subscription numbers and household penetration are primed to offset the renewed interest in advertising campaigns, (ii) digital media continued to lead the way in terms of growth but printed media are still lagging behind, and (iii) digital adex has continued up-trending as the medium offers improved ad targeting and a wider audience. However, the growth in the medium is being counteracted by tightening margins surrounding newspaper and other printed media, meaning those benefiting from the growth of their online publications continued to struggle with the recovery of their traditional printed channels. We have yet to see any meaningful recovery of in-person channels. We anticipate both STAR and MEDIAC to continue to reel from the after-effects of COVID-19 as their in-person events and travel segments, respectively, are showing little signs of life. While the transition to the endemic phase is beneficial, the combination of lingering cautious sentiments surrounding the pandemic and Omicron variant fear overlapping with major periods of celebration spell trouble for these segments. Overall, even considering seasonal upticks in adex later in the year, we expect CY22 to continue to be a period of gradual recovery for the sector.

Contracting margins. CY22 is expected to be a difficult year for the sector as growth in adex could be offset by rising cost of operations. The television segment is anticipated to incur high content costs as concurrent major sporting events such as the World Cup and the Commonwealth Games erode bottom line. The digital segment is anticipated to continue to grow but margins will continue to be pulled down by printed media and its associated costs. Additionally, despite easing movement restrictions, we have yet to see meaningful recovery in the travel or events segments to pre-pandemic levels. Combined with easier access to in-person shopping nibbling into home-shopping numbers, we are still seeing some adjustments. We expect increases in adex, both seasonal and yearly, to be offset by increased costs and lingering effects from the pandemic. Channels such as digital advertising and cinemas will continue to show growth, cinemas especially with the transition to the endemic phase. However,TV continues to make up the largest segment but is currently on a downtrend. Combined with rising inflationary pressure, we may see reduced consumer spending in general, impacting both subscription numbers, even as advertisers are willing to spend on a consumer base providing diminishing returns. Hence, we remain neutral on our outlook for the rest of CY22. We believe more integrated media players such as MEDIA will be in a better position to capitalise on the easing restrictions but others are expected to see some erosion in the bottom line.

Sector's call is downgraded to NEUTRAL. The sector has struggled to capitalise on improved adex as recovery from pandemic movement restrictions are dragging overall performance. Meaningful recovery to pre-pandemic levels seems to be a long road ahead, stretching out to the end of CY22 and maybe even into CY23. All in all, we like **MEDIA (OP; TP: RM0.74)** for its position as an integrated media platform and its consistent growth in the Omnia segment.

Appendix

Statistics in this report are correct at time of printing. Nielsen measures advertising spending based on published rate cards for traditional media. Digital ad spend is based on industry agreed "cost-per-mille" (CPM) rates.

Figure 1: Quarterly gross adex by medium

Media Type	1Q22 (RM'm)	1Q21 (RM'm)	YoY Chg	4Q21 (RM'm)	QoQ Chg
FTA Television	862.3	772.3	11.6%	978.9	-11.9%
Newspapers	206.7	219.2	-5.7%	280.7	-26.4%
Magazines	5.7	4.9	16.8%	8.3	-31.4%
Radio	105.0	77.1	36.3%	120.8	-13.1%
Cinema	36.1	1.7	2058.2%	23.6	53.1%
In-Store Media	6.5	31.0	-79.2%	16.9	-61.9%
Digital*	308.2	239.3	28.8%	332.1	-7.2%
Total	**1,530.4**	**1,345.4**	**13.7%**	**1,761.2**	**-13.1%**
Total (ex-Digital)	**1,222.2**	**1,106.1**	**10.5%**	**1,429.2**	**-14.5%**

Notes:
** Digital media does not account for adex from mobile in-app spend, social media, and search engines*

Source: Nielsen, Kenanga Research

Figure 2: YTD adex change

Media Type	3M22 (RM'm)	3M21 (RM'm)	YoY Chg
FTA Television	862.3	772.3	11.6%
Newspapers	206.7	219.2	-5.7%
Magazines	5.7	4.9	16.8%
Radio	105.0	77.1	36.3%
Cinema	36.1	1.7	2058.2%
In-Store Media	6.5	31.0	-79.2%
Digital*	308.2	239.3	28.8%
Total	**1,530.4**	**1,345.4**	**13.7%**
Total (ex-Digital)	**1,222.2**	**1,106.1**	**10.5%**

Figure 3: Quarterly key newspaper languages gross adex

Language	1Q22 (RM'm)	1Q21 (RM'm)	YoY Chg	4Q21 (RM'm)	QoQ Chg
West Msia					
-BM	45.6	41.2	10.6%	75.6	-39.7%
-Chinese	43.2	65.4	-33.9%	77.9	-44.6%
-English	79.1	75.0	5.3%	111.4	-29.0%
Others*	38.9	37.6	3.5%	15.7	146.7%
Total	**206.7**	**219.2**	**-5.7%**	**280.7**	**-26.4%**

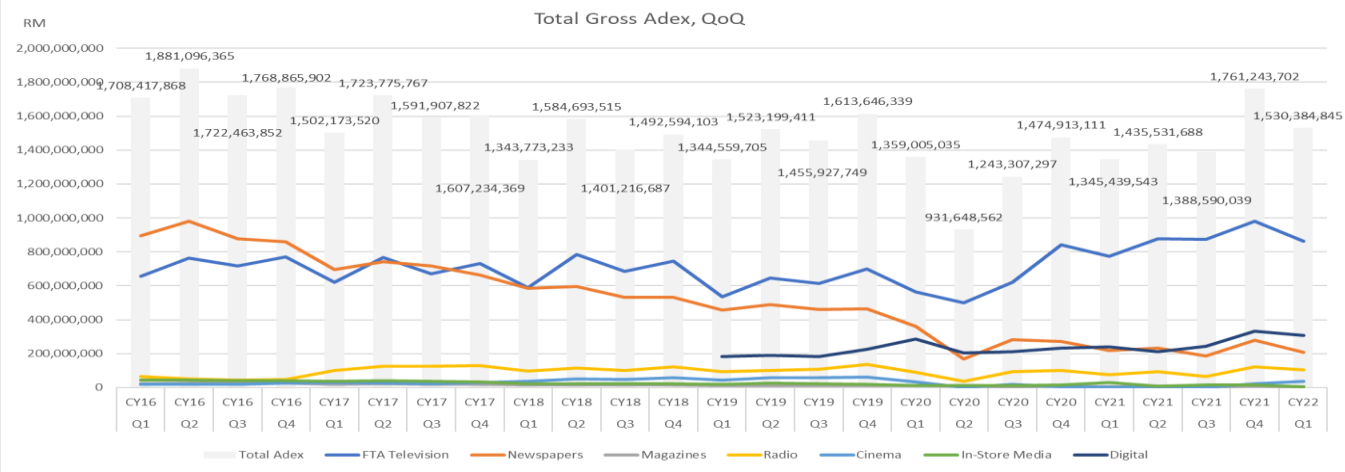
Notes:
** Others includes East Malaysian and tamil language papers*

Source: Nielsen, Kenanga Research

Figure 4: YTD Key newspaper languages gross adex

Language	3M22 (RM'm)	3M21 (RM'm)	YoY Chg
West Msia			
-BM	45.6	41.2	10.6%
-Chinese	43.2	65.4	-33.9%
-English	79.1	75.0	5.3%
Others*	38.9	37.6	3.5%
Total	**206.7**	**219.2**	**-5.7%**

Figure 5: Quarterly gross adex (%)



Source: Nielsen, Kenanga Research

Peer Comparison – Media

Name	Last Price @ 17-Jun-2022 (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net DivYld (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
Stocks Under Coverage																	
ASTRO MALAYSIA HOLDINGS BHD	0.940	4,901.6	N	01/2023	6.2%	2.1%	-8.9%	36.2%	10.3	11.3	8.3	4.1	3.8	34.6%	6.9%	1.00	MP
MEDIA CHINESE INTERNATIONAL	0.175	295.3	Y	03/2023	15.2%	7.0%	3525.0%	64.1%	738.2	20.4	12.4	0.4	0.4	2.1%	3.4%	0.190	MP
MEDIA PRIMA BHD	0.435	482.5	N	12/2022	15.6%	8.3%	27.9%	25.8%	8.7	6.8	5.4	0.8	0.7	10.9%	4.6%	0.740	OP
STAR MEDIA GROUP BHD	0.295	213.8	Y	12/2022	10.2%	7.1%	165.8%	25.0%	N.A.	41.1	32.9	0.3	0.3	0.8%	0.0%	0.335	MP
Simple Average					**11.8%**	**6.1%**	**927.5%**	**37.8%**	**252.4**	**19.9**	**14.8**	**1.4**	**1.3**	**12.1%**	**3.7%**		

Source: Bloomberg, Kenanga Research

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MREITs

Threatened by Rising Bond Yields

NEUTRAL ↓

By Marie Vaz / msvaz@kenanga.com.my

Downgrade to NEUTRAL. FY22 will be a recovery year as business operations and earnings are expected to normalize closer to pre-Covid levels. The retail segment's earnings are improving steadily in recent quarters, in line with the reopening of the economy, with prime malls expected to do better than suburban malls post the country entering the endemic phase. The Industrial segment remains fundamentally stable on low single-digit reversions, while the Office segment may see flattish reversions for now and we remain cautious of its long-term outlook. Despite earnings improving, we are cautious of a rising 10-year MGS yield which has put a dampener on MREITs' valuations. All in, we increase our 10-year MGS target to 4.5% and lower our sector call to NEUTRAL from OVERWEIGHT.

FY22 a year of recovery for MREITs business. Going forward, we believe business disruption for malls will be minimal compared to FY20 and FY21 as the country has entered the endemic phase, while most malls are reporting increased shopper traffic but more importantly tenant sales returning closer to or on par with pre-Covid levels. As such, earnings are expected to normalize in FY22 and improve in FY23. We are currently expecting YoY earnings growth of 25% in FY22 and 10% in FY23 which is on track to meeting expectations thus far.

Prime malls to benefit the most. As shopping and spending habits change, it appears that prime malls would fare better due to two reasons; (i) their shopper demographic is less affected by the impact of Covid as demand for luxury goods has been increasing post-pandemic, and (ii) they attract tourist – which would also be keen to spend in prime malls with the reopening of international borders this year. As such, earnings for these malls have been normalising closer to pre-Covid levels as the economic situation continues to return to the old normal. That said, we do not completely discount the possibility of further economic disruptions from potentially new Covid variants, but believe the probability of this happening is low for now.

The industrial segment will continue to remain stable. This segment is known for its minimal organic growth (of 2-3% p.a.) but during the pandemic, it has been fortress of stability within the MREITs space. On top of stable organic growth, AXREIT, the only industrial REIT is also actively acquiring more industrial assets, targeting an additional RM120m worth of industrial asset acquisitions, focusing on Grade A logistics located in Selangor, Penang and Johor and a net yield of c.6.5-7.0%.

Not overly optimistic about the office segment, save for KLCC. Over the medium to long run, we believe the office segment may see a decline in demand vs. the pre-Covid era, either from shorter lease terms or tenants requiring less office space. This is because most companies were able to function seamlessly through work-from-home arrangements during the pandemic. This may also further exacerbate the pre-existing oversupply of offices in the Klang Valley. That said, our pessimism for the office segment does not apply to KLCC even though it is primarily office space driven as it is well protected by its secured long-term leases (>10 years vs. retail of 2-3 years) and with an easy to manage triple-net-lease (TNL) structure.

The rising 10-year MGS a downside risk to valuations. Despite expected earnings improvements this year, it is unfortunate that MREITs are now bogged down by a rising 10-year MGS yield. To date, the MGS has climbed from 3.5% at the beginning of the year, rising to a peak of 4.4% in April, and is currently at 4.28%. This is in line with recent surge in US Treasury yields and expectations of the US Feds sizeable rate hikes going forward. As such, we have increased our internal 10-year MGS target during the results seasons, and we are pegging MREITs under our coverage to a 4.50% 10-year MGS target (from 4.15%-4.4% previously).

Downgrade to NEUTRAL (from OVERWEIGHT) as earnings improvements are not enough to outweigh rising bond yields. We are comfortable with our 10-year MGS target of 4.50% for now, in line with our in-house risk-free rate, and as the 10-year MGS appears to be trending sideways in the near term. Our valuations have been rolled forward previously to FY23E to better encapsulate a new normal to earnings as 2022 is poised to be a recovery year, especially for the ailing retail and hospitality segments. We are more optimistic on MREIT's earnings potential going forward, and thus have pegged MREITs to marginally lower spreads to the 10-year MGS target.

Industrial based AXREIT has the thinnest spread (+0.8ppt) under our coverage due to: (i) extremely stable earnings profile and the ability to weather the pandemic, (ii) positive single-digit rental reversions which is better than the retail and office segments, (iii) an active acquisition trail allowing for strong YoY growth of 10% p.a. vs. organic growth of 2-3% p.a., and (iv) its high yielding acquisitions of 6.5-8% (higher than retail and office of 4-6%). Additionally, we like AXREIT and one of two Shariah compliant MREITs under our coverage.

Retail MREITs applied spreads are between +1ppt to +2ppt, slightly higher than the industrial segment and lower than office segment. This is because; (i) the retail segment is more susceptible than the industrial segment to negative earnings impact from the pandemic, (ii) it has lower rental reversions than industrial (flattish vs. low single-digit positive reversions), and (iii) minimal acquisitions due to the low yielding nature of retail asset acquisitions (c.4-6%). The only outlier for the retail segment is CMMT at +4.2ppt spread due to its challenging asset profile which commands negative reversions and struggles with fluctuating occupancy, while FY22 is expected to be challenging due to the high amount of leases up for expiry of 40%.

The office segment is spilt between KLCC and SENTRAL. KLCC warrants a low spread of +1.0ppt, closer to AXREIT due to: (i) its stable earnings from its office segment (55% of earnings), and long term lease expiry profile (>10 years), which is also Covid-proof (ii) positive low single-digit rental reversions on stable occupancy for the office segment, although the retail and hospitality segment are still susceptible to earnings risk from the pandemic on flattish reversions and high occupancy cost, and (iii) its Shariah-compliant status. SENTRAL on the other hand warrants a higher spread of +3.6ppt as it operates like a typical office asset which has; (i) earnings variability from tenant movements due to an oversupply of office spaces in the Klang Valley, (ii) shorter lease expiry terms of 4-7 years (vs. KLCC >10 years), and (iii) flattish to mildly negative rental reversions due to the competitive nature of this segment which we are long-term negative.

MREITs Valuations

MREIT	Last Price as at 17/06/22	GDPS (RM)	FY	Gross Yield based on last price	Target Gross Yield	Gross yield spread to 10-yr MGS	10-yr MGS target	New Call	New TP (RM)	Old Call	Old TP (RM)	Share price upside/ downside (%)	Total Returns (%)
KLCC	6.49	0.36	FYDec23E	5.5%	5.5%	1.0%	4.50%	MP	6.45	MP	6.55	-1%	4%
SUNREIT	1.54	0.09	FYDec23E	5.8%	5.9%	1.4%	4.50%	MP	1.50	MP	1.40	-3%	3%
CMMT	0.56	0.05	FYDec23E	8.6%	8.7%	4.2%	4.50%	MP	0.56	OP	0.56	-1%	7%
AXREIT	1.93	0.10	FYDec23E	5.3%	5.3%	0.8%	4.50%	MP	1.95	OP	2.10	1%	6%
PAVREIT	1.36	0.08	FYDec23E	6.2%	6.5%	2.0%	4.50%	MP	1.30	MP	1.45	-4%	1%
IGBREIT	1.63	0.08	FYDec23E	5.1%	5.60%	1.1%	4.50%	MP	1.50	OP	1.55	-8%	-3%
SENTRAL	0.96	0.07	FYDec23E	7.5%	8.1%	3.6%	4.50%	MP	0.890	MP	0.87	-7%	-1%

Source: Bloomberg, Kenanga Research

Risks to our NEUTRAL sector call include: (i) stronger/weaker-than-expected consumer spending, (ii) stronger/weaker-than-expected rental reversions, (iii) U.S. Fed increasing interest rates aggressively, and (iv) stronger/weaker-than-expected occupancy rates.

Peer Comparison

Name	Last Price (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
AXIS REIT	1.93	3,167.2	Y	12/2022	8.7%	9.1%	10.4%	9.9%	24.1	21.4	19.3	1.2	1.2	6.2%	4.3%	1.95	MP
CAPITALAND MALAYSIA MALL TRUST	0.560	1,206.9	N	12/2022	46.1%	2.5%	150.3%	3.3%	28.0	11.2	11.2	0.5	0.5	2.6%	7.5%	0.560	MP
IGB REIT	1.63	5,834.5	N	12/2022	33.5%	2.0%	46.6%	2.0%	27.2	20.4	20.4	1.5	1.5	6.2%	4.6%	1.50	MP
KLCCP STAPLED GROUP	6.49	11,716.6	Y	12/2022	-4.4%	17.4%	-1.0%	20.6%	18.5	18.0	17.5	0.9	0.9	5.4%	5.0%	6.45	MP
SENTRAL REIT	0.960	1,028.9	N	12/2022	9.0%	1.8%	-2.5%	0.7%	12.7	12.7	12.7	0.8	0.8	5.3%	6.8%	0.890	MP
PAVILION REIT	1.32	4,029.7	N	12/2022	25.0%	2.0%	91.4%	2.2%	33.0	16.5	16.5	1.1	1.0	6.0%	5.6%	1.30	MP
SUNWAY REIT	1.54	5,274.2	N	12/2022	7.6%	5.0%	-21.3%	21.7%	23.1	18.0	16.5	1.0	1.0	5.4%	4.8%	1.50	MP
Simple Average					**17.9%**	**5.7%**	**39.1%**	**8.6%**	**23.8**	**16.9**	**16.3**	**1.0**	**1.0**	**5.3%**	**5.5%**		

Source: Bloomberg, Kenanga Research

Oil & Gas

Stronger Earnings in Pipeline

OVERWEIGHT

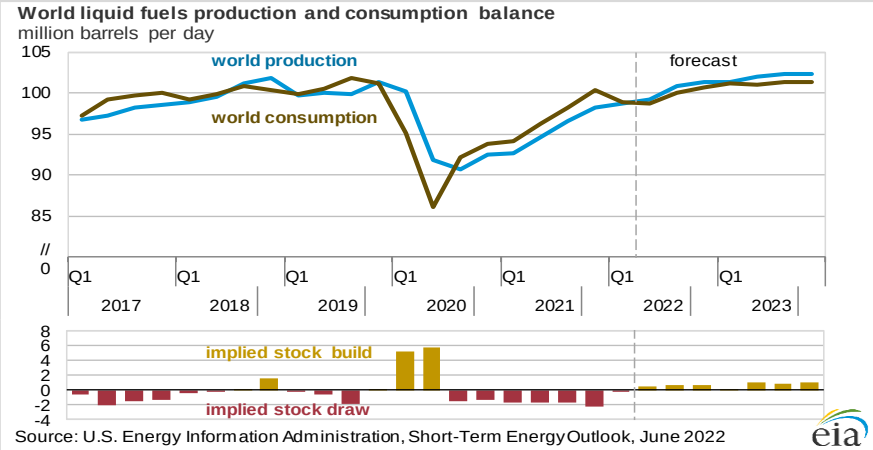
↔

By Steven Chan / steven.chan@kenanga.com.my

We believe oil prices are likely to stay elevated throughout 2022-2023, underpinned by the resurgence of China's demand to drive global demand, while increased Russian sanctions coupled with OPEC+'s capacity constraints may lead to supply being insufficient to keep pace. Overall, we are raising our 2022-2023 average Brent crude oil price assumption to USD110/barrel (from USD90/barrel previously). Petronas had recently revised its annual capex guidance upwards to RM60b (from RM40-50b previously) – almost doubled YoY from RM30.5b in 2021, in preparation for the resumption of activities. With 1QCY22 capex still largely underwhelming, we are convinced that capex spending will be backloaded into the coming quarters – hence translating to a resurgence of local activity levels. Petronas' net-cash position is currently at a 3-year high of RM90.6b, with dividend commitments remaining flat at RM25b despite the better earnings outlook. Hence, we see little obstacles in Petronas meeting its own capex guidance. Globally, offshore E&P capex is also expected to pick up in the coming years as an aftermath of under-investments over the past several years and may even surpass pre-Covid levels. Given the largely laggard earnings effect of the locally listed oil and gas players (which is mostly dominated by local-centric equipment and service providers), we have yet to see any meaningful or sustainable rallies within the sector, except for those with high earnings correlation to oil prices (e.g. PCHEM, HIBISCS). The KL Energy Index is still trading at a forward PER valuation close to its trough seen during the peak lockdowns in 1HCY20. We believe this signals some selective laggard opportunities within the sector. Maintain OVERWEIGHT on the sector, with stock picks to include: (i) PCHEM – as a prime beneficiary of the continued elevated oil prices, and (ii) DAYANG – a play on the recovery of local activity levels.

Oil prices expected to stay elevated. We believe oil prices are likely to stay elevated throughout 2022-2023. While a weaker economic outlook may look to moderate consumption, this is expected to be more than offset by the resurgence of China's demand to drive global oil demand. Meanwhile, global oil supply may continue to struggle to keep pace with the higher demand as tighter sanctions forced Russia to shut in more wells. The EU countries have agreed to ban 90% of the bloc's imports of Russian crude and oil products, to be phased out over the next 6-8 months. Note that prior to this, Russia accounts for ~10% of global oil supply, and ~40% of Europe's gas supply. Additionally, while the modest upward adjustment in OPEC+'s planned production numbers may provide a near-term relief, these are still likely insufficient to offset the growth in demand and supply constraints going into the next couple of months. Overall, **we are raising our 2022-2023 average Brent crude oil price assumption to USD110/barrel** (from USD90/barrel previously).

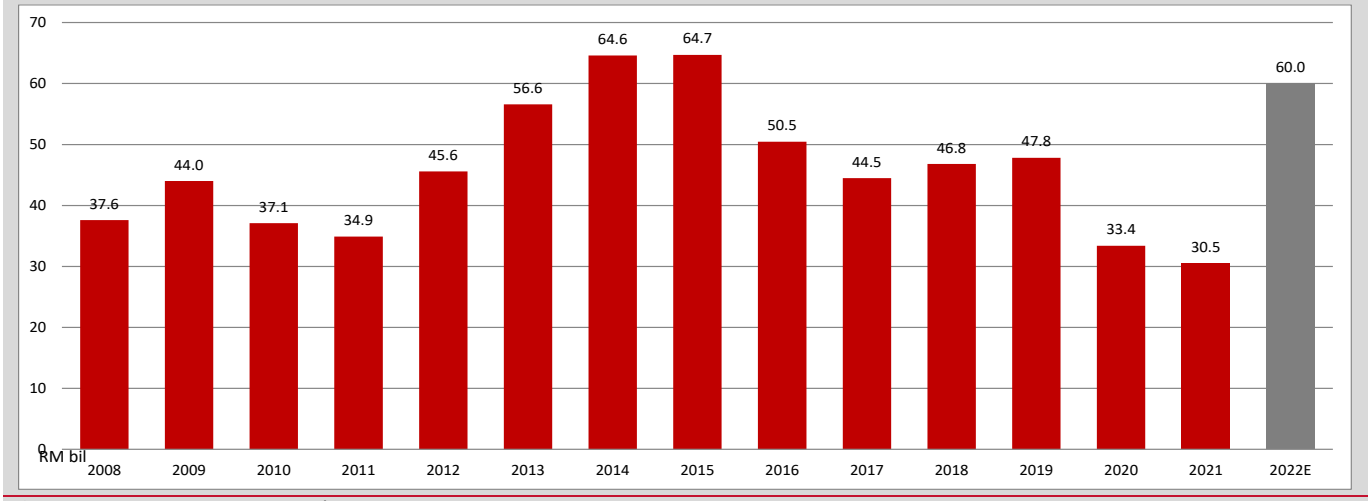
World Oil Production vs Consumption



Source: EIA

Steep recovery in spending and activity levels. In recent weeks, Petronas had increased its annual capex guidance to RM60b, from RM40-50b previously, in preparation for the resumption of business activities in a post-Covid environment. This is almost doubled YoY from 2021 capex of RM30.5b - the highest capex spend the group has incurred since 2015. And while there is increased commitment towards clean energy, most of the capex spend will still be earmarked for oil and gas. Petronas' 1QCY22 capex is still largely underwhelming at only RM7.4b (-48% QoQ), and hence, we firmly believe that these capex investments will be backloaded in the coming quarters. The group's net-cash position is at a near 3-year high at RM90.6b, while dividend commitments are expected to stay flattish YoY at RM25b despite the stronger profits – hence we see little difficulty for Petronas to meet the aforementioned capex guidance. In a readthrough of Petronas' latest Activity Outlook report, we had previously highlighted the offshore maintenance, construction and modification (MCM), and hook-up and commissioning (HUC) spaces as potential key winners – which may stand to benefit DAYANG especially given its position as a market leader within these specialities. Meanwhile globally, 2022-2023 is also expected to see an aggressive ramp-up in offshore exploration and production (E&P) capex, surpassing even pre-Covid levels, as an aftermath of under-investments in the industry over the past several years. All three of our Bursa-listed FPSO players (i.e. YINSON, MISC, ARMADA) are seen to have been in active participation in international job bids, with opportunities emerging from Latin America, Asia Pacific and Africa. The FPSO space is starting to see a supply squeeze – i.e. many global FPSO players are already pre-occupied with jobs developing at hand, and hence, more recent bids have started to see very limited bidders, making it very much an operator market.

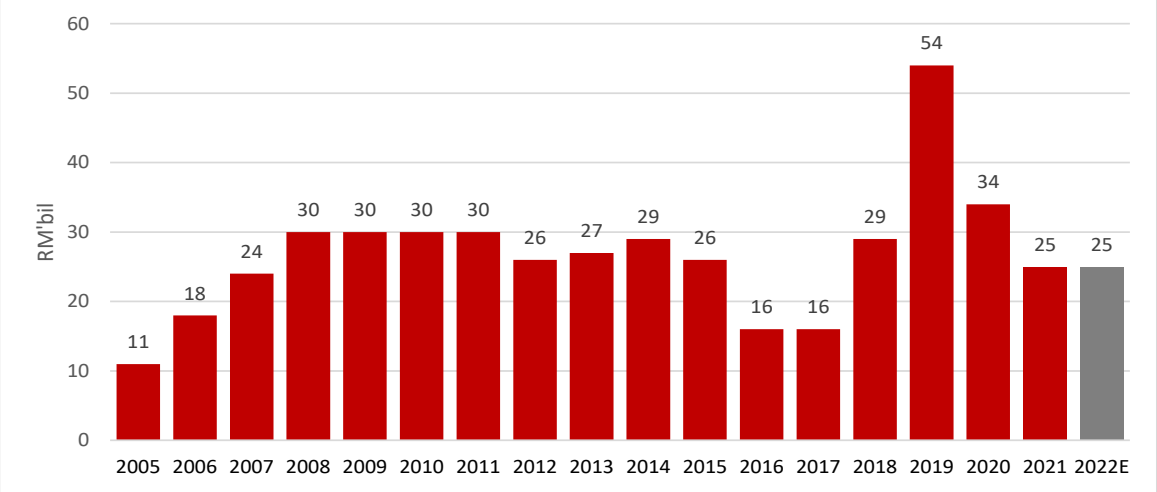
Petronas Yearly Capex (RM bil)



Source: Petronas, Kenanga Research

Commentary: Petronas is guiding RM60b capex in 2022 – almost doubled YoY from 2021 levels.

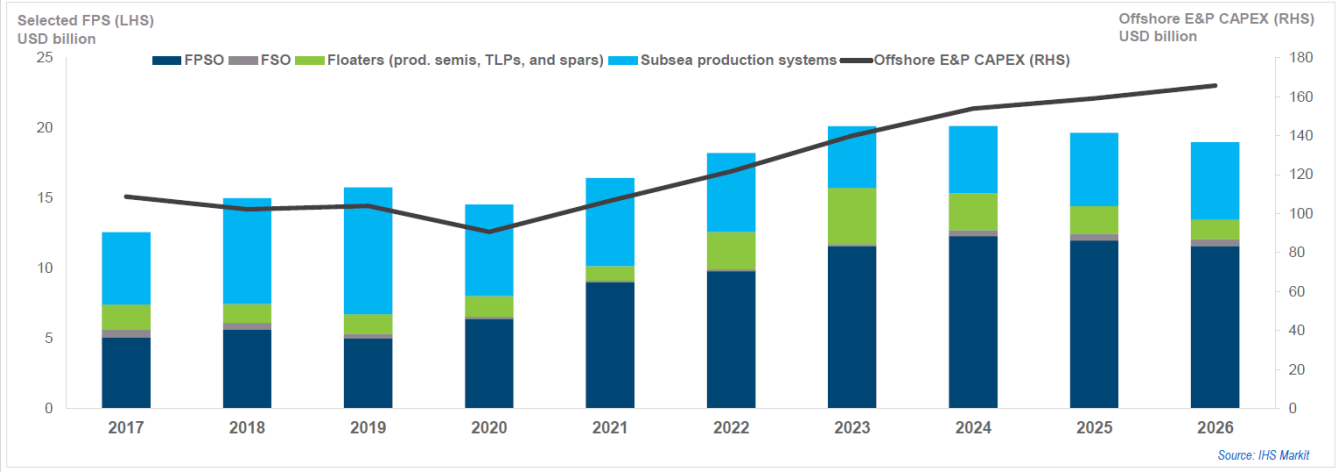
Petronas Yearly Dividends (RM bil)



Source: Petronas, Kenanga Research

Commentary: Petronas dividend commitment for 2022 is expected to stay flat at RM25b, despite the better earnings outlook.

Global Offshore E&P Capex Spending / Global Floater Project Awards

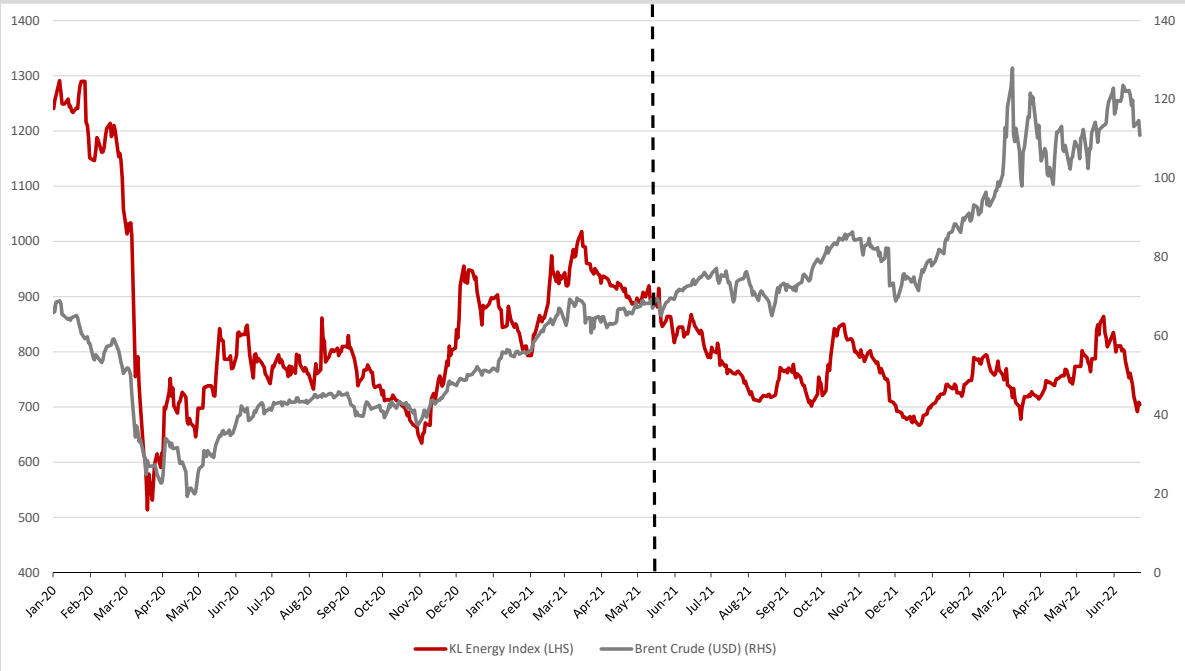


Source: MISC, IMF Markit

Commentary: Offshore E&P capex, as well as global bidding opportunities for floater projects are expected to rise in the coming years, even surpassing pre-Covid levels.

Sector still largely trading at a divergence from fundamental recovery. Since mid-last year, the KL Energy Index is still trading at a divergence against the strength in crude oil *(refer chart below)*. While this could be partially explained by the downfall of some notable names (e.g. Sapura Energy, Serba Dinamik), we have noticed that only stocks with high direct earnings correlation to oil prices (e.g. PCHEM, Hibiscus) had enjoyed any sustainable rallies. In fact, most in the underlying sector (which are mostly dominated by local-centric service contractors and equipment providers) have yet to see any meaningful gains. While this could be attributable to the laggard earnings nature of the space (i.e. sustained high oil prices may require some time to translate to actual work orders for these contractor names), we believe the gradually improving underlying fundamentals of the sector will translate to significantly improved earnings trends and job tendering opportunities in the coming quarters. Valuation-wise, the KL Energy Index's forward PER is still trading at trough levels similar to the peak pandemic lockdowns in 1HCY20 *(see chart below)*, suggesting that some laggard plays opportunities are present.

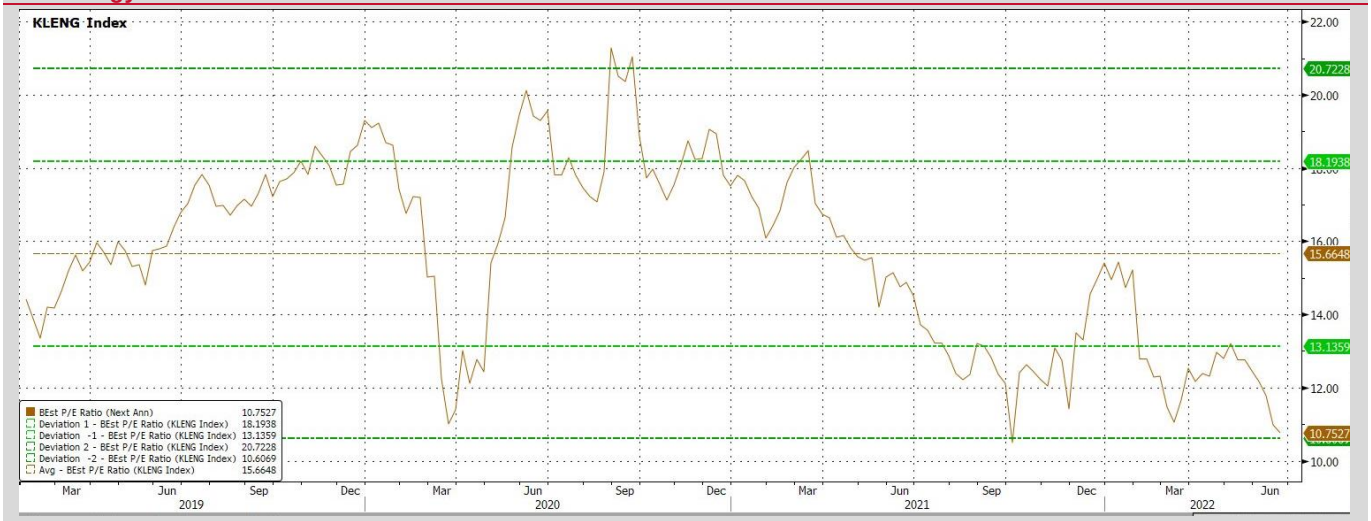
KL Energy Index vs Brent Crude Oil Price



Source: Bloomberg, Kenanga Research

Commentary: The KL Energy Index has been mostly trading at a divergence from the rally in Brent crude oil price throughout 2021-2022.

KL Energy Index Forward PER Valuation



Source: Bloomberg, Kenanga Research

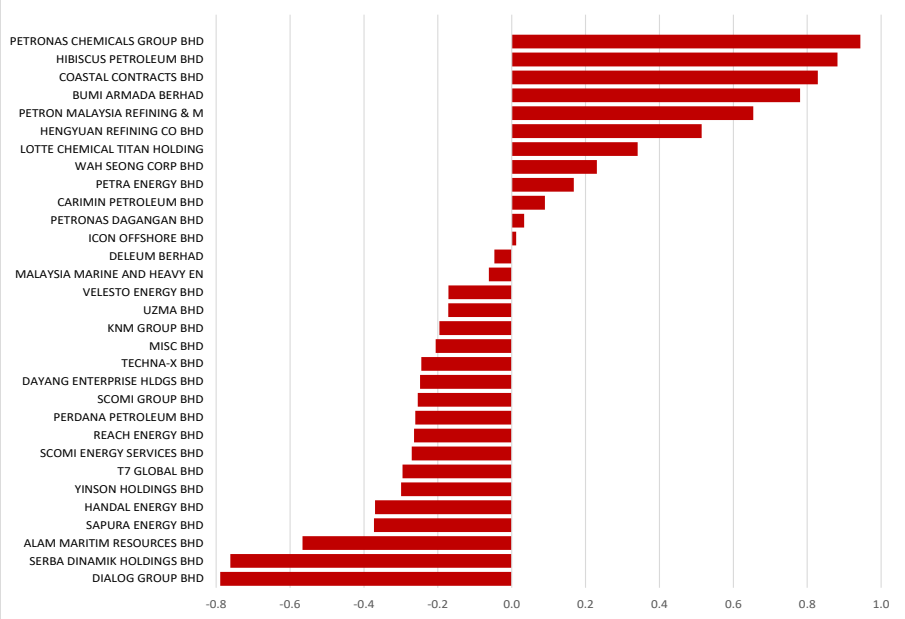
Commentary: The KL Energy Index is still at a forward PER close to the lows seen in 1H2020 during peak lockdowns.

Maintain OVERWEIGHT on the sector, premised on promising recovery prospects of activity levels as well as current elevated oil prices sustaining. For stock picks, we highlight:

PCHEM (OP; TP: RM11.00): Being the best play on oil and petrochemical product prices, with our correlation study highlighting this as the highest correlated stock to the movements of oil prices. Against peers, PCHEM is able to enjoy better and more stable margins thanks to its more favourable feed costs arrangements with Petronas.

DAYANG (OP; TP: RM1.25): Being the best play on the recovery of local activities. DAYANG is the market leader within the MCM and HUC space, which is expected to see jump in demand in the coming 2-3 years, in accordance to Petronas' latest activity outlook.

Stock Price Correlation to Brent Crude Oil Price



Source: Bloomberg, Kenanga Research

Commentary: Based on our study, PCHEM and Hibiscus are the two most correlated stocks to oil prices. Note that study period is from 2020 – present.

Peer Comparison

Name	Price	Market	Shariah	Current	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div.Yld. (%)	Target	Rating
	(RM)	Cap (RM'm)	Compliant	FYE	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	Price (RM)	
BUMI ARMADA BHD	0.375	2,219.3	N	12/2022	12.8%	0.0%	-10.7%	3.4%	3.3	3.7	3.5	0.6	0.5	14.1%	0.0%	0.630	OP
DAYANG ENTERPRISE HLDGS BHD	0.945	1,094.1	Y	12/2022	10.8%	12.0%	46.6%	50.2%	25.0	17.0	11.3	0.8	0.8	4.8%	0.0%	1.25	OP
DIALOG GROUP BHD	2.13	12,018.7	Y	06/2022	13.5%	49.2%	1.7%	13.2%	22.6	22.3	19.7	2.6	2.4	11.3%	1.4%	3.30	OP
MISC BHD	7.06	31,514.0	Y	12/2022	-0.8%	4.2%	-15.2%	1.1%	16.7	19.7	19.5	0.9	0.9	4.7%	4.7%	7.70	MP
PETRONAS CHEMICALS GROUP BHD	9.20	73,600.0	Y	12/2022	16.4%	-10.0%	-3.9%	-21.1%	10.1	10.6	13.4	2.1	1.9	19.0%	4.7%	11.00	OP
PETRONAS DAGANGAN BHD	21.06	20,922.1	Y	12/2022	30.0%	5.0%	-1.8%	26.6%	38.2	38.9	30.7	3.7	3.7	9.6%	2.6%	17.85	UP
SAPURA ENERGY BHD	0.045	719.1	Y	01/2023	-7.0%	0.0%	-115.1%	-174.3%	N.A.	N.A.	N.A.	2.9	(3.2)	N.M.	0.0%	0.005	UP
UZMA BHD	0.380	133.8	Y	06/2022	-2.7%	10.0%	-60.4%	72.1%	5.6	14.1	8.2	0.3	0.3	1.9%	0.0%	0.540	OP
VELESTO ENERGY BHD	0.105	862.6	Y	12/2022	-6.8%	9.6%	-136.7%	-168.7%	N.A.	N.A.	N.A.	0.4	0.4	-2.8%	0.0%	0.100	UP
WAH SEONG CORP BHD	0.630	487.8	Y	12/2022	44.1%	26.2%	51.9%	56.4%	N.A.	13.6	8.7	0.8	0.8	5.9%	0.0%	0.790	MP
YINSON HOLDINGS BHD	1.98	6,584.7	N	01/2023	6.1%	-16.6%	1.2%	20.7%	10.5	10.4	8.6	1.8	1.6	16.1%	3.0%	2.50	OP
Simple Average					**10.6%**	**8.1%**	**-22.0%**	**-11.0%**	**16.5**	**16.7**	**13.7**	**1.5**	**0.9**	**8.5%**	**1.5%**		

Source: Bloomberg, Kenanga Research

Plantation

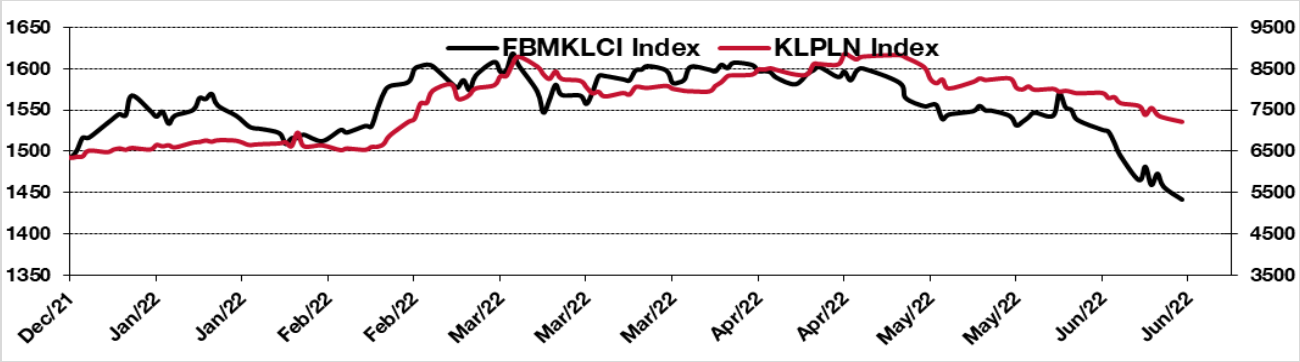
Resilient & Defensive

OVERWEIGHT
↑

By Teh Kian Yeong I tehky@kenanga.com.my

The investment case for the plantation sector is no longer earnings recovery but earning resilience especially when concerns over high inflation and weakening economy are clouding the market. After outpacing the broader market in 1Q 2022, the KL Plantation Index consolidated for much of 2Q 2022 before dipping this month on broad equity weakness led by the US. CPO prices then fell as Indonesia re-opens for exports coupled with seasonally rising palm oil output as well as pending US soyabean harvest in 3Q/4Q. Peak palm oil prices may be behind us but plantation earnings look set to stay healthy on resilient demand for palm oil. Robust margins are also expected on firm price outlook despite rising cost. The sector's defensive asset-rich NTA is another attraction and valuations are not excessive either, trading at or even below the broad market ratings with some offering good yields. For investors benchmarked against the Shariah Index, the sector is also unavoidable as the plantation sector accounts for 9.6% by weight in the FBM Shariah Index (and 9.4% in the FBMKLCI). Upgrade from NEUTRAL to OVERWEIGHT.

KLCI vs KLPLN Index



Peering into 2Q 2022 earnings seasons, another good set of plantation earnings can be expected before earnings moderate after 2H on softer CPO price outlook. Nevertheless, we expect CPO prices to stay firm, averaging at RM4,500 per MT in 2022 and RM4,000 per MT in 2023 against production cost of between RM2,000 to 2,500 per MT; hence, margins are attractive. Our expectation of firm CPO prices for 2022 and 2023 hinges on the following:

(a) Supply is likely to be stay fragile until 2023. Any seasonal uptick in 2H of 2022 will provide a welcome relief but unlikely to reverse the overall tightness. An above average season in 2023 could just about reverse the tightness.
(b) Sticky demand is also likely. Edible oils and fats are part of our daily diet. As such, cutting consumption can be done, especially temporarily but deeper more prolonged cuts are less easy.
(c) Elevated fossil fuel prices are supportive of demand for biofuel; thus, demand for edible oils.

Responsible agriculture is important and palm oil - the most widely used edible oil – has drawn more than its rightful share of media and NGO's attention. However, the Russia–Ukraine conflict highlights just how ill prepared the world is in facing a supply shock to the global food chain. This may reset towards a more rounded perspective on food security and ESG going forward. Importantly, the palm oil industry has progressively addressed various ESG issues. Certified palm oil supply is on the rise and they meet some of the highest agriculture standards worldwide.

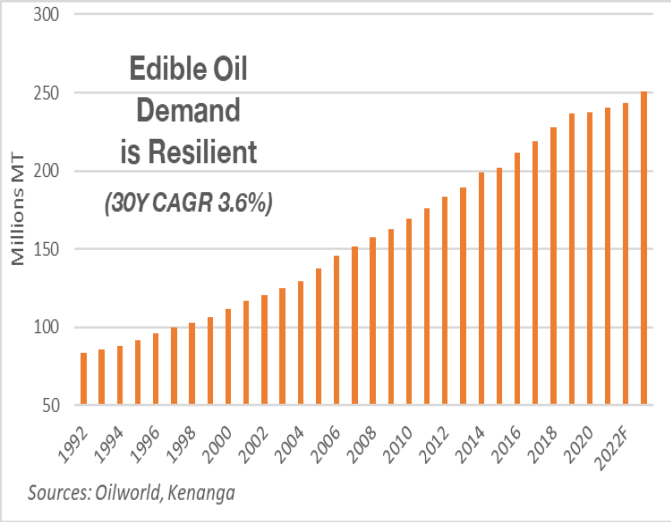
Importantly, recent market sell-down has rendered the sector even more attractive considering the sector's defensive business and solid asset base. We are upgrading the sector from **NEUTRAL to OVERWEIGHT**. Our top integrated pick is **KLK (OP, TP: RM30.00)** which offers strong YoY earnings growth in FY22, a beneficiary of firm prices of edible oils and biofuels with strong balance sheet and track record. We also like mid-cap such as **BPLANT (OP, TP RM1.00)** and **HAPLNT (OP, TP RM3.30)** for generous dividends and **TSH (OP, TP RM1.90)** for long-term growth as it seeks to expands its planted area from under 40k Ha to 60-65K Ha over the next 6-8 years.

Outlook for 2022 and 2023

The edible oils market is dominated by palm oil (c.35% market share) and soyabean oil (c.25% share). Both are expected to enjoy seasonal uptrend in production in the latter half of this year. However, this pending 2H supply uptick is unlikely to resolve the overstretched supply situation. However, it should prevent the current tightness from getting worse. Therefore, relatively firm CPO prices is likely for the rest of 2022 and, increasingly, into 2023 as well due to the following reasons:

a) **Supply needs more time to recover.** Current global edible oils tightness began when production dipped and failed to meet demand in 2020. Inventory slipped and continued doing so in 2021. If the pending 2H season does go well, 2022 inventory should edge up YoY but unlikely to exceed 2019 levels. An above average 2023 season is needed for inventory to surpass 2019 levels but even so the inventory-to-usage ratio will likely stay under the 10-year average. A favourable 2023 scenario is possible given that prices are still good but helpful weather is also needed and Malaysia's labour shortage does not curtail palm oil output substantially.

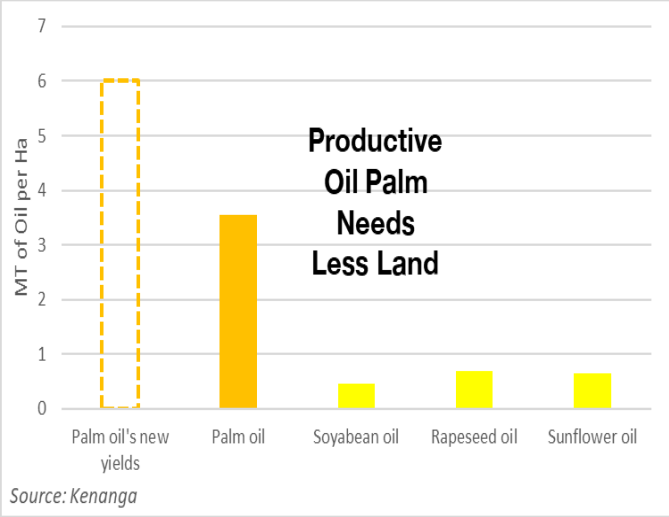
b) **Historically, demand has been rather resilient.** Underpinned by rising population and affluence, annual consumption grew 3% on average for the past 10 years (30-year average is 3.6% p.a.). However, growth during the Covid-19 years of 2020-21 moderated to around 1% and we suspect 2022 growth is still hovering around 1-2%, dampened by high prices. However, a reversion back to 3% growth as the world adapts to a new post-Covid norm is likely. It is noteworthy that China has yet to fully emerge out of its zero-Covid policy and edible oil demand thus far has been subdued. Also, in the event of a global economic slowdown, demand contraction cannot be ruled out but it will probably be a long and severe downturn to produce such a negative outcome.



c) Supportive biofuel demand. About 70% of edible oils is consumed as food, hence the demand resilience but just over 20% ended up as biofuel last year. Due to elevated fossil fuel prices, especially after the Russia-Ukraine conflict, demand for biofuel has been good and is likely to stay supportive.

Environment, Social & Governance

Kenanga believes in responsible investing but we also believe that palm oil is here to stay despite some ESG overhangs. Palm oil is, first and foremost, food and it is the most widely used edible oil in the world. Replacing palm oil will be a challenge. Palm oil is very cost competitive despite being taxed and enjoy no subsidy. It is also flexible enough to meet the demands of high temperature frying, bread making, cocoa butter substitute to being a salad oil. Yielding 3.5 MT of oil per Ha, it is also the most productive oil crop in the world thus leaving a much smaller environmental footprint compared to other oil crops. Yet 3.5 MT per ha is considered low among better managed groups which averaged 4-5 MT of palm oil per Ha a year. Increasingly, the target is for 6 MT of palm oil per Ha or approximately 10x more land-efficient than other oil crops.



Importantly, the plantation sector has responded positively and improved on the ESG front. Today, about 16m MT of palm oil is certified, an amount not too far from Malaysia's entire annual production. It is also worth noting that certified palm oil meets some of the highest ESG standards for agriculture products internationally. Therefore, the issue is not about survival but more about adapting and many planters have successfully done so despite the lack of recognition.

Our thoughts on the sector

Monthly palm oil production typically bottoms around February and peaks in September or October. Therefore, during 2Q, CPO prices often come under downward pressures. However, for 2Q 2022, CPO prices stayed at near record levels until June on the back of tight edible oils supply, as the Russia-Ukraine conflict (Ukraine exports almost half the world's sunflower oil of 6-7m MT) and subsequent economic sanctions on Russia which disrupted global supply of fossil fuels and fertillser caused the prices of such commodities to rise. Hari Raya Aidilfitri also fell on 1 May, which supported palm oil demand for a good portion of 2Q 2022.

Altogether, 2Q 2022 plantation earnings should enjoy stronger prices and output compared to 1Q 2022. **Nevertheless, CPO prices have probably peaked and earnings should ease after 2Q 2022. However,** we are still expecting firm CPO price of RM4,500 per MT for 2022 and RM4,000 per MT for 2023. Margins are thus expected to stay robust with **production cost hovering between RM2,000 to 2,500 per MT after taking into consideration higher labour, fertiliser as well as fuel costs.**

Overall, the appeal of the plantation sector is no longer about earnings recovery but earning resilience especially when **concerns over high inflation and weakening economy are clouding the market. Firstly, plantation earnings look set to stay healthy on resilient demand for palm oil. Robust margins are also expected on firm price outlook despite rising cost. The sector's defensive asset-rich NTA is another attraction and valuations are not excessive either. For investors benchmarked against the Shariah Index, the sector is also unavoidable as the plantation sector accounts for 9.6% by weight in the FBM Shariah Index (and 9.4% in the FBMKLCI).**

More importantly, we are upgrading the sector from NEUTRAL to OVERWEIGHT following recent market sell-down which has made the sector even more attractive considering the sector's defensive business and asset base. PERs are at or even below broad market ratings with good dividends expected for 2022 and 2023. Our top integrated pick is still KLK (OP, TP: RM30.00) which offers strong YoY earnings growth in FY22, a beneficiary of firm prices in edible oils and biofuels with strong balance sheet and track record. We also like mid-cap such as BPLANT (OP, TP: RM1.00) and HAPLNT (OP, TP: RM3.30) for good dividends and TSH (OP, TP: RM1.90) for long-term growth as it is expanding its planted area from under 40k Ha to 60-65K Ha over the next 6-8 years.

Peer Comparison

Name	Last Price @ 17/6/2022 (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div. Yld. (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
STOCKS UNDER COVERAGE																	
BOUSTEAD PLANTATIONS BHD	0.87	1,948.8	Y	12/2022	30.7%	-27.7%	35.1%	-48.2%	8.1	6.0	11.4	0.8	0.7	24.4%	16.1%	1.00	OP
FGV HOLDINGS BHD	1.60	5,837.0	Y	12/2022	10.9%	-6.1%	-2.2%	-20.9%	23.6	11.3	16.4	1.4	1.3	19.5%	5.3%	2.30	MP
GENTING PLANTATIONS BHD	6.70	6,011.2	Y	12/2022	23.0%	-5.4%	32.1%	-6.2%	25.2	14.5	16.5	1.2	1.2	10.4%	4.3%	9.50	OP
HAP SENG PLANTATIONS HOLDINGS	2.50	1,999.2	Y	12/2022	32.0%	-14.7%	15.0%	-17.2%	28.9	10.5	16.5	1.2	1.1	13.1%	5.6%	3.30	OP
IOI CORP BHD	4.04	25,100.4	Y	06/2022	46.7%	-15.7%	64.6%	-17.5%	30.1	19.5	22.7	2.5	2.3	15.8%	2.4%	4.65	MP
KUALA LUMPUR KEPONG BHD	23.40	25,228.9	Y	09/2022	26.1%	-2.8%	23.4%	-3.3%	15.0	17.7	19.1	2.1	2.0	17.3%	2.4%	30.00	OP
PPB GROUP BHD	15.32	21,794.2	Y	12/2022	12.0%	5.2%	-7.7%	7.9%	16.7	16.1	15.3	1.0	0.9	5.7%	2.6%	15.00	UP
SIME DARBY PLANTATION BHD	4.46	30,844.1	Y	12/2022	19.9%	-13.2%	39.1%	-23.0%	37.0	12.6	19.7	2.3	2.1	17.4%	4.7%	5.25	MP
TA ANN HOLDINGS BHD	4.38	1,929.2	Y	12/2022	17.7%	-6.5%	-7.4%	-3.7%	30.5	7.5	13.1	1.4	1.3	16.3%	6.8%	6.00	MP
TSH RESOURCES BHD	1.11	1,532.0	Y	12/2022	38.4%	-8.9%	9.9%	1.0%	21.3	8.1	15.1	1.0	0.9	13.7%	3.6%	1.90	OP
UNITED MALACCA BHD	5.48	1,149.5	Y	04/2022	20.4%	-5.6%	297.5%	-4.9%	40.5	18.2	24.5	0.9	0.8	8.5%	2.7%	5.90	MP
Simple Average					24.7%	-7.4%	46.4%	-8.8%	26.9	13.6	17.9	1.5	1.4	13.8%	4.0%		

Source: Bloomberg, Kenanga Research

Plastics & Packaging

Higher Sales Dented by Margin Erosion

NEUTRAL

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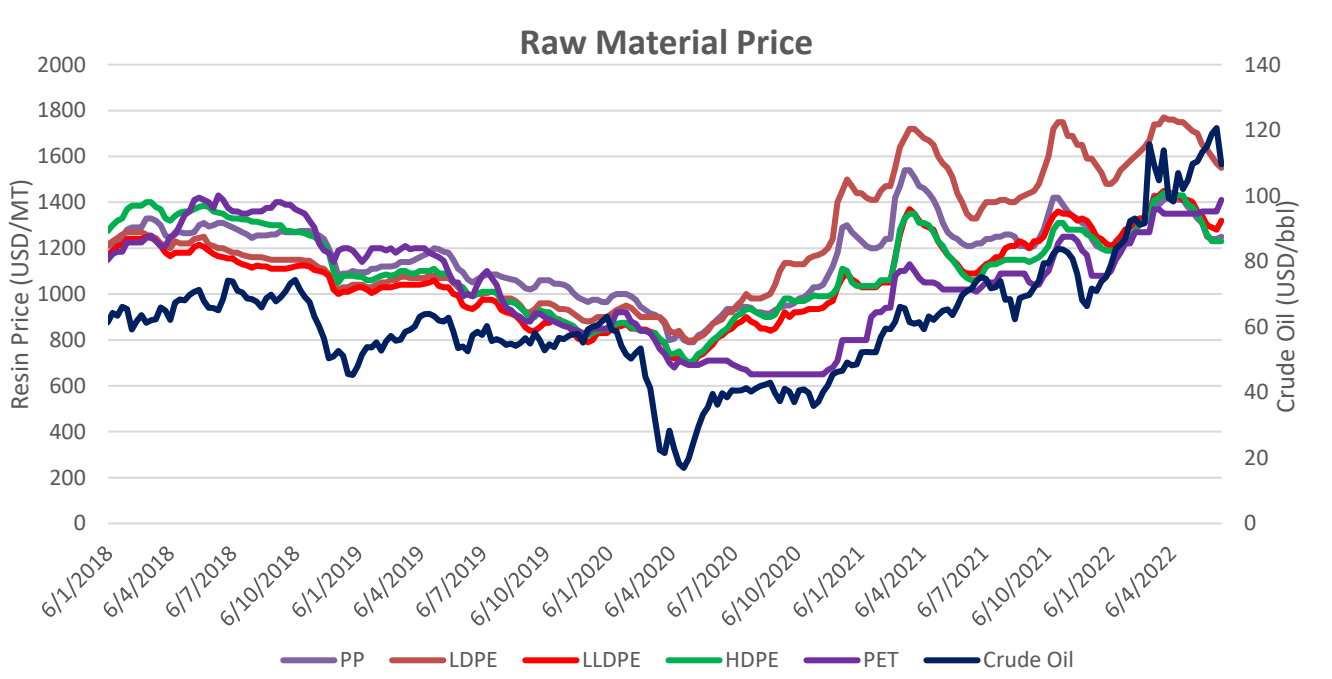
ByTan Jia Hui I jhtan@kenanga.com.my

We reiterate our NEUTRAL sector view with TGUAN (OP, TP RM3.90) being our top pick given its more favourable product mix and sustained earnings growth. While we expect resin prices and freight costs to soften further in 2HCY22, overall production cost will likely remain high due to hikes in wages and electricity tariffs. Hence, even as plastic packaging companies under our coverage will show stronger revenue growth amid elevated ASPs and growing sales volume, weaker operating margins could drag bottomline.

Signs of softening in resin prices. Despite crude oil prices staying around USD110/barrel level due to the unresolved Russia-Ukraine war and other supply chain disruptions, resin prices have shown signs of softening recently. Resin prices have dropped c.10% to approximately USD1,350/MT currently from the recent peak in April (which was previously triggerred by the geopolitical tension). Based on our channel checks, we expect resin prices to soften further in 3QCY22 on the back of: (i) new resin capacity coming onstream in the market, and (ii) softer resins demand from China.

The falling price for resins (a major raw material cost) will benefit plastic players after they have run down their existing resin inventory to fulfill running orders, translating to lower overall production cost gradually. For CY22, we maintain our average resin price assumption at USD1,200/MT to USD1,300/MT, marginally below the YTD average of USD1,300/MT to USD1,400/MT but still higher than CY2021's average of RM1,100/MT to USD1,200/MT.

Resin and Crude Oil Prices



Source: Bloomberg, Kenanga Research

Separately, freight/shipment cost has been on the decline *(YTD, down c.17% based on data from the Baltic Exchange and Statista)*. Nevertheless, in spite of the expectations for lower resin and transporation expenses, overall operating cost is expected to remain high on account of increased staff cost (due to labour shortage and the implementation of minimum wage policy starting in May 2022) and electricity tariff hike (up 17%% for industrial / commercial rates since Feb 2022).

Higher topline but weaker margins. Based on our channel checks, we expect ASPs to stay elevated due to lag effect (despite the falling resin prices). For the whole of 2022, we are assuming ASPs to be 10%-15% higher YoY. Together with stronger sales volume projections on the back of resilient demand, this will boost the topline of packaging companies under our coverage by 5%-19% in the current financial year. However, the higher revenue growth will be negated by weaker margins, which we have assumed at 8%-10% for CY2022 (down from 10%-12% last year).

Maintain NEUTRAL on the sector in view of the mixed fortunes for the individual plastic packaging companies under our coverage.

We still like **TGUAN (OP; TP: RM3.90)** for: (i) its better product mix amid resilient demand especially for nano stretch film, food wrap and others, (ii) its capacity expansion plan (completed in 1QCY22, raising capacity by c.30%), mainly catering to premium products (such as stretch films and courier bags) to fuel medium-term growth, and (iii) positive currency effects arising from a stronger USD/RM exchange rate, which may help to boost its price competitiveness.Within our coverage, TGUAN is currently trading at the lowest PERs with the highest earnings growth prospect in the next two financial years.

Meanwhile, we maintain MP call for BPPLAS with revised TP of RM1.45 based on unchanged FY22E EPS of 14.5 sen as we apply a lower PER of 10x (from 11x previously) which is at a 15% discount to the1-year forward sector average PER of 11.7x (to reflect its negative earnings growth expectation in FY22).

In addition, we maintain OP for SLP with revised TP of RM0.99 based on unchanged FY22E EPS of 7.1 sen with an ascribed PER of 14x (from 16.6x previously), which is at 20% premium to the 1-year forward sector average PER of 11.7x as we recalibrate its PER valuation vis-à-vis its sector peers to reflect its slower earnings growth in FY23 and lower trading liquidity.

Risks to our call include: (i) lower-than-expected demand for plastic products, (ii) higher-than-expected resin prices, (iii) labour shortage, (iv) higher-than-expected operating cost, and (vi) foreign currency risk.

Valuations

Company	Last Price @ 17th June 2022	Valuation Method	Valuation Basis (vs sector avg forward PER of 11.7x)	Key investment points	Current TP	Current Call	Previous TP	Previous Call
Consumer								
SLP	0.88	PER	14x PER (~20% premium to sector average) on FY22E EPS of 7.1sen	(i) net cash position (ii) niche products which fetch superior margins (iii) attractive dividend yield (iv) low trading liquidity	0.99	OP	1.18	OP
SCGM	2.27	PER	14x PER (~20% premium to sector average)on FY23E EPS of 18.0sen	(i)niche market segment focussing on growing demand for consumer packaging (ii) resilient demand (iii) In the midst of disposing of its entire packaging business, which has been valued at RM544.4m at an implied historical PER of 16.0x.	2.53	MP	2.34	OP
Industrial								
SCIENTX	3.59	PER/PBV	SOP comprising: (i) 14x PER on manufacturing segment, (ii) 0.7x PBV on property segment	(i) largest market cap status (ii) better economies of scale	3.33	MP	4.15	MP
TGUAN	2.33	PER	13x PER (~10% premium to sector average) on FY22E EPS of 30.0sen.	(i) better product mix amid sustainable demand (ii) capacity expansion plan for its premium products (iii) highest forward earnings growth over the two FYs (iv) net cash position	3.90	OP	3.90	OP
BPPLAS	1.36	PER	10x PER (15% discount to sector average) on FY22E EPS of 14.5sen	(i) facing more acute margin squeeze than its peers due tohigher production costs (ii) steadydividend yield	1.45	MP	1.59	MP

Source: Bloomberg, Kenanga Research

Peer Comparison

Name	Last Price@ 17/3/2022 (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
STOCKS UNDER COVERAGE																	
BP PLASTIC HOLDING BHD	1.36	382.8	Y	12/2022	13.8%	7.8%	-12.1%	25.2%	8.3	9.4	7.5	1.7	1.5	16.8%	4.4%	1.45	MP
SCGM BHD	2.27	437.1	Y	04/2022	15.1%	16.0%	-10.3%	13.4%	12.8	14.3	12.6	2.3	2.1	15.1%	2.8%	2.53	MP
SCIENTEX BHD	3.59	5,568.1	Y	07/2022	5.4%	18.1%	-13.4%	44.0%	12.5	14.5	10.1	1.9	1.7	12.5%	2.1%	3.33	MP
SLP RESOURCES BHD	0.880	278.9	Y	12/2022	9.7%	5.5%	28.6%	9.3%	15.9	12.4	11.3	1.5	1.5	12.0%	6.3%	0.99	OP
THONG GUAN INDUSTRIES BHD	2.33	897.4	Y	12/2022	19.7%	20.4%	22.2%	21.2%	9.5	7.8	6.4	1.2	1.0	14.3%	2.4%	3.90	OP
Simple Average					**12.7%**	**13.6%**	**3.0%**	**22.7%**	**11.8**	**11.7**	**9.6**	**1.7**	**1.6**	**14.1%**	**3.57%**		

Source: Bloomberg, Kenanga Research

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Ports & Logistics

A Mixed Bag

NEUTRAL

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By Wan Mustaqim Bin Wan Ab Aziz I wanmustaqim@kenanga.com.my

We keep our NEUTRAL call on the sector premised on moderation in trade volume and macroeconomic trends (IMF projects global growth to moderate from 6.1% in 2021 to 3.6% each in 2022 and 2023) amidst prolonged global supply chain disruptions brought about by China's zero-Covid policy and the ongoing Russia-Ukraine war. On the other hand, e-commerce boom has boosted demand for warehousing and land-based logistics. Meanwhile, the operating environment for both the conventional mail and courier segments remains challenging. The conventional mail segment is struggling to stay relevant in the digital age, while the cut-throat competition in the over-crowded courier segment will not be resolved without a massive sector consolidation. Our top pick for the sector is SWIFT (OP; TP: RM1.01).

Seaport segment: Trade volume to moderate. Global trade, the lifeline of the seaport segment, is projected by United Nations Conference on Trade and Development (UNCTAD) to moderate in 2022, after a record year at USD28.5trn in 2021. This is not surprising given the weakened outlook of the global economy, as reflected in the International Monetary Fund (IMF) cutting its global growth forecast for 2022 further in July 2022, after reducing it to 3.6% from 4.2% in April 2022 (vs. 6.1% estimated for 2021). On expectations of a lower throughput volume, we trim Westports' FY22E and FY23E core profit forecasts by 3.5% each, lower our DCF-derived TP to RM3.80 (from RM4.00) based on a discount rate equivalent to a WACC of 6.4% and a terminal growth rate of 2%), and maintain our MARKET PERFORM call.

Logistics segment: A mixed picture. The value of ASEAN's e-commerce expanded almost 6x in just four years' time, rising from US$9.5b in 2016 to US$54.2b in 2020. Based on a projected annualised growth rate of 22%, it should top US$146b by 2025. Zooming in on Malaysia, the picture is equally rosy. According to the Department of Statistics, e-commerce's share of gross domestic product (GDP) leaped from 8.5% in 2019 to 11.5% in 2020, and there is no sign that the number will be slowing down in the foreseeable future. The e-commerce boom has boosted demand for warehousing (to be used as distribution hubs) and land-based logistics. We expect a CAGR of 22% between 2012 and 2019 in terms of the supply of logistics warehouses in Greater Kuala Lumpur as estimated by JLL Malaysia to sustain over the immediate term. From our observation, global brands such as Ikea, Daiso, Nestlé and Continental Tyres have invested in distribution hubs in Malaysia to expand their footprint in the region. International logistics players such as Nippon Express, CJ Century Logistics and DHL are also actively expanding within Greater Kuala Lumpur. Moving forward, J&T Express looks to build an integrated logistics centre (for US$136m) for express distribution, logistics transportation, and warehousing, while JLL Malaysia expect to see 6.7m sq ft of warehouse/logistics facilities being completed in the next three years. As for SWIFT, the group will continue to focus on expanding its customer base domestically and regionally with the concurrent warehouse expansion to 1.3m sq. ft (+46%) in FY22. We like SWIFT for its: (i) robust growth potential, driven by both higher market demand for its container haulage, land transportation and expanding warehouse space, and (ii) pre-tax profit margin of 10% which is head and shoulders above the industry average of about 4%. SWIFT's valuation is based on 14x FY23E EPS, in-line with peers' average.

Conventional mail and courier segments: Different challenges. The conventional mail business of POSM continues to struggle to stay relevant in the digital age (the digital economy in Malaysia expanded by 10% in 2020 and is projected to grow at CAGR of 24% up to 2025. While the conventional mail volume of POSM declined by an average of 13% annually between FY14 to FY21, we doubt that we have seen the bottom. Taking our cue from its YTD performance, we now project the conventional mail volume to decline by 20% (-10% previously) and 10% (-5% previously) in FY22 and FY23, respectively. Meanwhile, industry experts project the courier, express and parcel (CEP) market in Malaysia to expand by a CAGR of 9% between 2017 and 2027. Incumbent POS has to face tremendous competition from new players such as J&T Express and Ninja Van that undercut aggressively on rates to expand their market shares. Players may be able to breathe a sigh of relief following a halt in the issuance of new courier licenses (Sept 14, 2020 to Sept 15, 2022) and the introduction of a new courier licensing framework that may set in motion industry consolidation. In the meantime, we revised FY22E earnings from a core loss of RM50.9m to core loss of RM66.3m, and FY23E's from core profit at RM56.4m to core loss of RM30.6m. We downgrade POSM to MP from OP, with DCF-derived TP to RM0.550 from RM0.720. Our valuation is based on a discount rate equivalent to a WACC of 6.8% and a terminal growth rate of 0%.

Peer Comparison

Name	Last Price as at 17th June 2022 (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) (RM)	ROE (%) Cap (RM'm)	Net Div.Yld. (%)	Target FYE	Rating 1-Yr. Fwd.
TRANSPORT & LOGISTICS																	
POS MALAYSIA BHD	0.565	442.3	Y	12/2022	-15.0%	-12.4%	-134.0%	-146.2%	N.A.	N.A.	N.A.	0.5	0.6	-8.3%	-	0.550	MP
SWIFT HAULAGE BHD	0.470	418.2	Y	12/2022	11.7%	12.1%	29.7%	12.4%	9.5	7.3	6.5	0.5	0.5	7.2%	4.3%	1.01	OP
WESTPORTS HOLDINGS BHD	3.59	12,241.9	Y	12/2022	-0.9%	5.9%	-8.9%	11.3%	16.7	18.3	16.4	3.9	3.7	20.9%	4.1%	3.80	MP
Simple Average					**-1.4%**	**1.9%**	**-37.7%**	**-40.8%**	**13.1**	**12.8**	**11.5**	**1.7**	**1.6**	**6.6%**	**2.8%**		

Source: Bloomberg, Kenanga Research

Property Developers

An Uphill Battle

NEUTRAL

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By Lum Joe Shen I lumjs@kenanga.com.my

Maintain NEUTRAL as the sector remains plagued with affordability, policy and oversupply issues. We feel the sector still lacks sustainable earnings visibility and growth to justify a re-rating in valuations. We believe it would be increasingly hard for players to drive sales in CY22 given: (i) absence of HOC discounts, (ii) blanket government subsidy removals, (iii) expected interest rate hikes, and (iv) a persistent oversupply situation. In our opinion, developers' margins would have to be sacrificed to push sales. In this climate, we advocate to only pick developers which can generate sustainable cash flows and are committed to dishing it out as dividends to avoid a value trap. Two such picks that we have identified under our coverage are ECOWLD (OP; TP: RM0.83) and IOIPG (OP; TP: RM1.65).

FY22 will get tougher. For the rest of the year, we foresee sales risks from (i) rising OPR, (ii) electricity & petrol subsidy removals and, (iii) potential reimplementation of GST. All these would erode the affordability of buyers. From a developers' cost perspective, the elevated construction material prices, labour shortages and higher interest rates would weigh onto developer's margins. These mounting challenges come amidst a current oversupply backdrop. According to National Property Information Centre (NAPIC)'s data (refer table below), residential units in circulation* as of 2021 stood at an all-time high of 173.4k units (+8% YoY; highlighted in orange in table). **In view of these headwinds, we expect FY22 sales from developers under our coverage to contract 16% YoY while margins will also be compressed (refer appendix for our respective targets).**

Figure: Total overhangs and unsold under construction units (aka units in circulation)

UNITS	Residential Overhang	Service apartment Overhang	Total overhang (A)	Residential Unsold under construction	Service apartment Unsold under construction	Total Unsold under construction (B)	Total units overhang + Unsold Under construction (A+B) ie units under circulation
2015	10285	906	11191	49568	18530	68098	79289
2016	14792	3912	18704	64077	31278	95355	114059
2017	24738	6364	31102	61882	45955	107837	138939
2018	32313	11371	43684	80984	37285	118269	161953
2019	30664	17142	47806	72692	33827	106519	154325
2020	29565	23606	53171	71735	35258	106993	160164
2021	36863	24295	61158	70231	42094	112325	**173483 (all time high)**

Source: NAPIC, Kenanga Research

Developers' four key metrics in 1QCY22 showed no anomalies. Sales, unbilled sales, margins and net gearing observed in developers' recent earnings announcements did not show much anomalies against historical levels (refer appendix for tables).

1. 1QCY22 total sales for developers under our coverage shrank slightly by 4% attributable to the absence of HOC.
2. Total unbilled sales stood relatively healthy at RM25.94b.
3. YTD core operating margins (adjusted for one-offs) were strong with some even registering higher than pre-pandemic levels. This is due to more effective sales and marketing initiatives (i.e. digital marketing) adopted by developers during the pandemic which reset their cost base lower.
4. Meanwhile, net debt for developers continued to gradually trend upwards – with exception to ECOWLD and UOADEV.

Bashed down share prices could go lower amidst uncertainties. Developer's valuations (PBV/discount to RNAV) have continued to get cheaper despite already hitting depressed levels. We believe there are opportunities amidst such a severe sell-down. However, we must be selective and suggest to only **picking developers which can generate sustainable cash flows AND are committed to dish it out as dividends to avoid a value trap.** Two such picks we have identified under our coverage are IOIPG and ECOWLD.

ECOWLD's dividend yield stands high at 5.8% against our coverages' average of 3.5%. Despite the headwinds ahead, we believe the company's reputable branding coupled with its nimble management team would sail through this period and continue generating strong cash flows. Case in point, ECOWLD has continued to reduce its net gearing/net debt even during the challenging pandemic times. We deem its share prices a bargain should forward dividend yields hit a range of 7-8%. Such yields would be appealing against other asset class i.e. MGS (currently at 4.4% yield), MREITS (average yield of c.7%). **Reiterate OP with unchanged TP of RM0.83 (60% discount to RNAV implying 0.5x PBV).**

IOIPG's current PBV 0.26x is almost trading close to its pandemic bottom of 0.24x – a bargain in our view. While IOIPG's headline debt levels seem high (at net gearing of 0.75x), we are less concerned as these borrowings are mostly attached to its Singapore assets (Central Boulevard Tower, Marina View land). The potential profit/cash from these Singaporean assets which are located in the CBD should be able to self-service its respective debts once construction completes. Our investment thesis for the group remains – we think that investors are under appreciating IOIPG despite IOIPG having prime investment properties located throughout Klang Valley, Singapore and China. These properties could potentially be injected into a REIT for value unlocking and monetisation. The group has been conservative with dividends (<25% payout currently) as they channel profits generated from their ongoing operations to service interests from the construction of 2 major investment assets – IOI City Mall Ph2 and Central Boulevard. We believe dividend payout levels can be raised once these assets are completed in 2022 and 2023, respectively. **Reiterate OP with unchanged TP of RM1.65 (0.45x PBV target).**

For counters with share price that have fell and deviated against out rating, we evaluate these counters to see if an upgrade/downgrade is required.

SPSETIA's sharp fall of over 42% since late-April has plummeted below our TP of RM0.90 (PBV target of 0.3x). Nonetheless, the risk attached to SPSETIA is still high especially in a rising rate environment with such high debt burdens. With turnaround chances being slim, we choose to lower our valuations for SPSETIA to its pandemic low of 0.18x PBV to reflect the elevated uncertainties attached to the group. **Thereafter, we reduce SPSETIA's TP to RM0.54 (from RM0.90) and reiterate UNDERPERFORM.**

MAHSING has continued to fall despite showcasing strong sales and earnings during the recent reporting quarter. The group's property division continue to showcase resiliency and deliver earnings thanks to excellent cost management by the company. Cashflows from the property division is also expected to be strong in anticipation of the multiple handovers this year – improving its net debt. Nonetheless, its recently established glove division continued to record losses. For now, we choose to be conservative and **maintain Market Perform with lower TP of RM0.60 on reduced PBV of 0.40x (from 0.45x). We would turn positive on the group once we have ascertained that its glove division would not see its losses widened.**

SIMEPROP has sunk below its pandemic lows and currently stands at RM0.435 (yield of 4.6%; PBV of 0.32x). We believe the fall in share price is attributable to the foreign funds' outflow from the counter as the ringgit weakens. Fundamental-wise, the group's net gearing remains healthy and sales are likely to be well received from its township residential developments and industrial properties. Hence, we remain positive on SIMEPROP's outlook. Nonetheless, we revalue Simeprop's PBV lower to 0.40x (from 0.53x) against peers' average of 0.45x to commensurate its ROEs which are lower than average (2.6% vs 2.8% average). **Consequently, TP is reduced to RM0.55 (from RM0.725). Reiterate OUTPERFORM.**

Figure: Table for changes in Call and TP

Stock	Before		After	
	Rating	TP (RM)	Rating	TP (RM)
Ecowld	OP	0.83	OP	0.83
Ioipg	OP	1.65	OP	1.65
Mahsing	MP	0.65	MP	0.60 (↓)
Mrcb	MP	0.375	MP	0.375
Simeprop	OP	0.55	OP	0.55 (↓)
Spsetia	UP	0.56	UP	0.54 (↓)
Sunway	OP	2.05	OP	2.05
Uems	OP	0.40	OP	0.40
Uoadev	MP	1.76	MP	1.76

Source: Kenanga Research

Maintain NEUTRAL. Overall, the sector's fundamentals from an affordability and oversupply standpoint will remain challenging. Despite the low valuations (in PBV terms), the entire sector still lacks sustainable earnings visibility and growth to justify a re-rating. Certain developers' growing net debt is also a concern as this could insinuate higher completed inventories in the near future. Hence, we remain selective within the space and only pick branded developers with high cashflow generation capabilities.

Appendix

Figure: Sales, Sales Targets (RM m)

Sales Stock	FY18 Actual	FY19 Actual	FY20 Actual	FY21A Actual	FY22E Our target	FY22E Company Target
Ecowld	3110	2700	2300	3522	3300	3500
Ioipg	1877	1930	1840	2300	1900	2100
Mahsing	1500	1500	1100	1600	1700	2000
Mrcb	470	537	187	310	300	500
Simeprop	1340	3140	1980	2950	2500	2600
Spsetia	5120	4560	3820	4260	3500	4000
Sunway	1900	1550	1300	2610	1600	2200
Uems	1430	1130	1100	1450	800	1500
Uoadev	1480	787	384	341	650	n.a.
Total	**18227**	**17834**	**14011**	**19343**	**16250**	

Sales Stock	YTD sales reported (FY22) Actual		% of sales target achieved YTD	YTD sales reported (FY21) Actual	
Ecowld	2170	7M22	66%	2530	7M21
Ioipg	1314	9M22	69%	1558	9M21
Mahsing	450	1Q22	26%	400	1Q21
Mrcb	23	1Q22	8%	52	1Q21
Simeprop	890	1Q22	36%	630	1Q21
Spsetia	670	1Q22	19%	1190	1Q21
Sunway	447	1Q22	28%	1160	1Q21
Uems	110	1Q22	14%	272	1Q21
Uoadev	103	1Q22	16%	81	1Q21
Total	**7557**	**-4% YoY**		**7873**	

Source: Kenanga Research

Figure: Unbilled Sales

Unbilled sales (RM b)	FY18	FY19	FY20	FY21	YTD (FY22)
Ecowld	4.65	4.70	3.70	3.51	3.88
Ioipg	0.65	0.61	0.61	0.81	0.79
Mahsing	2.38	1.73	1.64	1.90	1.90
Mrcb	1.56	1.64	1.10	0.92	0.92
Simeprop	2.18	1.55	1.58	2.40	2.40
Spsetia	12.32	10.67	10.05	10.20	10.20
Sunway	2.10	2.10	2.40	3.40	3.40
Uems	4.36	1.80	1.95	2.34	2.34
Uoadev	1.50	0.99	0.31	0.09	0.09
Total	**31.70**	**25.78**	**23.34**	**25.58**	**25.92**

Source: Kenanga Research

Figure: OP margins

OP margins (Before interest, tax and JVA)	FY18	FY19	FY20	FY21	FY22 (YTD)	Comments
Ecowld	10%	9%	12%	13%	16%	Improve in SMA (Sell, Marketing, Admin)
Ioipg	26%	38%	46%	37%	38%	
Mahsing	18%	18%	12%	19%	23%	Improve in SMA (Sell, Marketing, Admin)
Mrcb	9%	4%	8%	4%	11%	-
Simeprop	4%	16%	11%	13%	16%	Improve in admin costs
Spsetia	34%	21%	17%	19%	20%	Improve in admin costs
Sunway	19%	30%	17%	19%	3%	-
Uems	23%	18%	9%	0%	8%	-
Uoadev	39%	42%	44%	47%	60%	Higher other income from Rentals
Average	**20%**	**22%**	**20%**	**19%**		

*Ewint, ECOWLD and IOIPG are actual numbers registered for FY21

Source: Kenanga Research

Figure: Net gearing/Net Debt

Net Gearing (x)	FY18	FY19	FY20	FY21	Latest YTD
Ecowld	0.77	0.70	0.62	0.45	0.36
Ioipg	0.52	0.52	0.50	0.48	0.76
Mahsing	0.19	0.24	0.25	0.37	0.33
Mrcb	0.20	0.27	0.24	0.28	0.30
Simeprop	0.28	0.25	0.28	0.32	0.31
Spsetia	0.81	0.84	0.95	0.96	0.99
Sunway	0.52	0.58	0.73	0.62	0.64
Uems	0.51	0.32	0.40	0.50	0.50
Uoadev	-0.11	-0.18	-0.34	-0.34	-0.32

Net Debt (RM m)	FY18	FY19	FY20	FY21	Latest YTD	Comments
Ecowld	3321	3179	2860	2095	1703	
Ioipg	9568	9750	9504	9426	15166	Surged because bought Marina View land in SG
Mahsing	132	293	850	1134	1171	
Mrcb	948	1311	1090	1251	1368	
Simeprop	2624	2461	2528	2922	2938	
Spsetia	7581	8109	9022	9482	9784	
Sunway	4137	4832	6247	6879	7223	
Uems	3605	2329	2790	3359	3398	
Uoadev	-504	-821	-1849	-1887	-1796	
Total	**31412**	**31443**	**33042**	**34662**	**40955**	

Source: Kenanga Research

Peer Comparison

Name	Last Price (RM) 17/6/2022	Market Cap (RM'm)	Shariah Compliant	Current FYE	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	Rating
STOCKS UNDER COVERAGE													
ECO WORLD DEVELOPMENT GROUP	0.690	2,031.6	Y	10/2022	8.6	8.6	7.7	0.4	0.4	4.9%	5.8%	0.830	OP
IOI PROPERTIES GROUP BHD	0.955	5,258.4	Y	06/2022	8.4	8.2	7.4	0.3	0.3	3.4%	2.9%	1.65	OP
MAH SING GROUP BHD	0.575	1,395.9	Y	12/2022	13.2	9.3	9.9	0.4	0.4	4.9%	5.2%	0.60	MP
MALAYSIAN RESOURCES CORP BHD	0.350	1,563.6	Y	12/2022	N.A.	29.2	70.0	0.3	0.3	1.1%	2.9%	0.375	MP
SIME DARBY PROPERTY BHD	0.435	2,958.4	Y	12/2022	21.1	12.5	11.8	0.3	0.3	2.5%	3.0%	0.55	OP
SP SETIA BHD	0.705	2,868.0	Y	12/2022	17.6	10.7	12.6	0.2	0.2	2.9%	5.4%	0.54	UP
SUNWAY BHD	1.72	8,409.2	Y	12/2022	27.8	21.5	12.8	0.9	0.9	4.4%	1.7%	2.05	OP
UEM SUNRISE BHD	0.315	1,593.4	Y	12/2022	N.A.	N.A.	N.A.	0.2	0.2	-0.6%	0.0%	0.400	OP
UOA DEVELOPMENT BHD	1.85	4,304.0	Y	12/2022	12.3	13.2	12.3	0.7	0.7	3.9%	7.0%	1.76	MP
Simple Average					**15.6**	**14.2**	**18.1**	**0.4**	**0.4**	**3.0%**	**3.8%**		

Source: Bloomberg, Kenanga Research

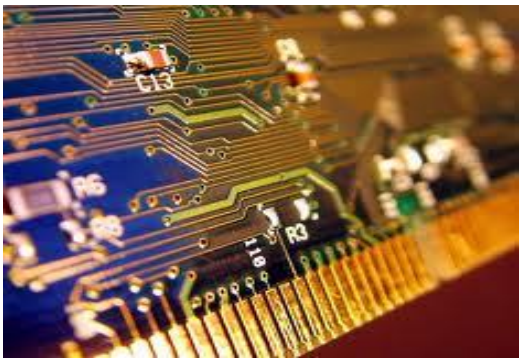
Technology

Value Emerges After Recent Pullback

OVERWEIGHT
↔

By Samuel Tan I samueltan@kenanga.com.my

We maintain our OVERWEIGHT stance on the technology sector moving into 3QCY22, premised on resilient chip demand as the Semiconductor Industry Association (SIA) reported 23% YoY increase in semiconductor sales for 1QCY22. Meanwhile, shipment numbers for car sales and consumer end-devices did not reflect the same optimism. We attribute this to the sporadic lockdowns in China, causing backlogs to pile up. We remain selectively positive on the sector, favouring companies that were unjustifiably bashed down but still holds strong fundamentals to weather through this high inflationary and rising interest rate environment. Despite weakening shipment numbers for global smartphones (1QCY22: -8.9% YoY), the US smartphone manufacturer was the only brand to record a slight growth of 2.2% YoY and is expected to keep its production unchanged for its upcoming new model. As such, we like INARI (OP; TP: RM3.30) for being in the US smartphone supply chain with a brand that is able to continue growing its loyal user base. With the Chinese government easing back on lockdowns, car sales in the EU and China posted encouraging numbers (May 2022: +68% MoM and +15.6% MoM respectively), resuming the recovery trend. This bodes for MPI (OP; TP: RM38.10) given its strong automotive exposure and more importantly having a head start in next-generation packages that is gradually being adopted in electric vehicles. Shifting away from the intensive competition surrounding household cleaning products, we believe PIE (OP; TP: RM3.70) offers an exciting investment case given its exposure to unique clients with stable order visibility. The new Chinese customer (relating to ASIC computer hardware) secured as a result of trade diversion is expected to contribute meaningfully to the group's earnings in FY22.



Favouring resilient fundamentals. We maintain our **OVERWEIGHT** stance on the technology sector moving into 3QCY22 premised on resilient chip demand, particularly in the automotive space. For 1QCY22, the Semiconductor Industry Association (SIA) reported a 23% YoY increase in semiconductor sales with April continuing the trend at 21% YoY. The growth came from all geographical regions while the Americas led the pack with a 40.9% YoY jump. Meanwhile, car sales data and shipment numbers of consumer electronics (smartphone and laptop) seems to lag behind SIA's reported growth. We believe this is likely due to macro challenges such as the lockdown in China causing massive logistical problems, resulting in backlogs which will be delivered with the easing of lockdown restrictions. That said, we remain selectively bullish on the sector, favouring companies that were unjustifiably bashed down but still holds strong fundamentals to weather through this high inflationary and rising interest rate environment.

US smartphone manufacturer keeps production forecast. Despite waning demand for consumer devices (e.g. smartphone and laptop), as evident by the latest 1QCY22 global smartphone shipment numbers which fell 8.9% YoY, the US smartphone manufacturer was the only one to eke out a 2.2% YoY shipment growth. In addition, it is expected to keep its smartphone production flat YoY for its upcoming model that is slated to launch in September 2022. We see this as an encouraging sign against the backdrop of supply chain challenges from the sporadic lockdowns in China as well as the cautious inflation data that could potentially dampen consumer spending. On this front, we continue to like **INARI (OP; TP: RM3.30)** as a proxy to the US smartphone manufacturer's supply chain which is expected to remain resilient owing to its ability to command pricing and market share.

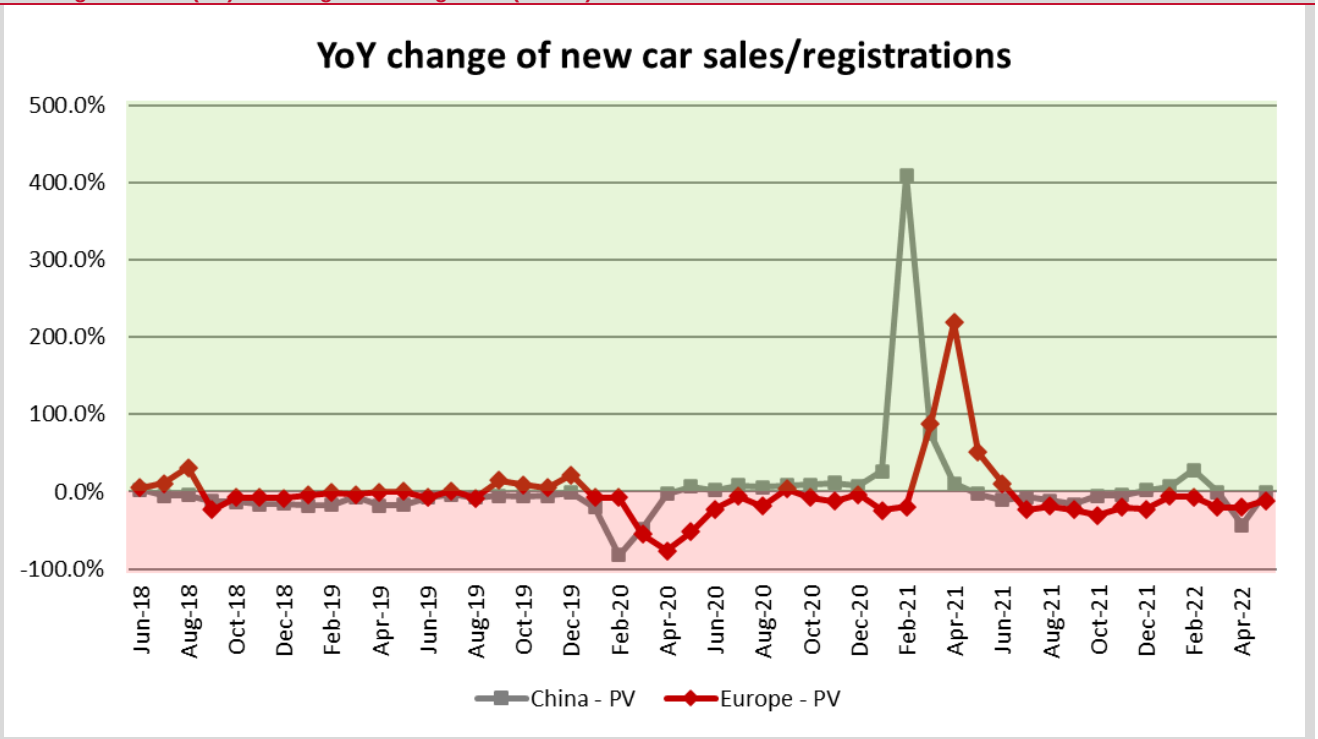
Worldwide Smartphone Sales to End Users by Vendor (m of units)

	Shipments (units)			Growth		Market Share		
Company	**1Q22**	**4Q21**	**1Q21**	**QoQ**	**YoY**	**1Q22**	**4Q21**	**1Q21**
Samsung	73.6	68.9	74.5	6.8%	-1.2%	23%	19%	22%
Apple	56.5	84.9	55.3	-33.5%	2.2%	18%	23%	16%
Xiaomi	39.9	45.0	48.6	-11.3%	-17.9%	13%	12%	14%
Oppo	27.4	30.1	37.5	-9.0%	-26.9%	9%	8%	11%
Vivo	25.3	28.3	35.0	-10.6%	-27.7%	8%	8%	10%
Others	91.4	105.2	93.9	-13.1%	-2.7%	29%	29%	27%
Total	**314.1**	**362.4**	**344.8**	**-13.3%**	**-8.9%**	**100%**	**100%**	**100%**

Source: IDC

Stabilising of automotive chips supply is expected to drag beyond 2022 mainly due to the punishing zero-Covid policy in China which has resulted in logistical challenges. Thankfully, the Chinese government has begun easing back on the restrictions which led to early improvements in May after a slump in the previous months. China car sales rose 68% MoM in May 2022 to 1.62m units while Europe car sales recorded 15.6% MoM increase to 791,546 units during the same period. While these numbers are still a YoY decline (China -1.4% and Europe -11.2%), we look forward to a resumption of the recovery phase as production gradually returns to normalcy. This bodes well for **MPI (OP; TP: RM32.90)** which has 38% revenue exposure to automotive and a unique advantage being the only local outsourced semiconductor assembly and test (OSAT) that is capable of packaging next-generation chips that uses materials such as silicon carbide (SiC) and gallium nitride (GaN). MPI has also proven itself as one of the most resilient tech companies as evident by its eight consecutive quarters of revenue growth throughout the pandemic. We maintain our earnings forecasts and OP call for MPI but lower our TP to RM32.90 (from RM38.10) to reflect the broad-based re-pricing of tech valuations amidst the higher terminal rate. We now value MPI at a lower PER of 19x FY23F (from 22x) which is at a 20% discount to peer's average forward PER to reflect its low share liquidity.

Passenger vehicle (PV) sales/registrations growth (% YoY)



Source: CAAM, ACEA

In line with automotive recovery trend, we believe that **D&O (OP; TP: RM4.50)** will continue to benefit from robust demand for its automotive LEDs as we observed car manufacturers are increasing the usage of LEDs as one of the key differentiation factors in the new vehicle launches, especially for electric vehicles (EV). This trend is observed in upcoming models such as the SAIC IM L7 which consists of >6,000 LEDs compared to an average internal combustion engine vehicle with c.500-700 LEDs. We raised FY23F earnings forecast by 6.5% to RM182m and maintain our OP recommendation for D&O. Similarly, we lower our TP to RM4.50 (from RM5.40) to reflect the broad-based re-pricing of tech valuations amidst the higher terminal rate. Our revised TP is based on a 25x FY24F PER (from 45x FY22F PER), in line with the average forward PER of original brand manufacturers (OBM) with design capabilities. We roll forward our valuation base year to FY24 as believe our FY24F earnings of RM222.5m better capture D&O's earnings potential as an OBM and a top five players in the global automotive LED space. While **JHM (MP; TP: RM1.40)** is also involved in automotive LEDs, the group is mainly focused on module assembly of headlamps and taillamps (falling short of designing LEDs). Again, we lower our TP for JHM to RM1.40 (from RM1.50) to reflect the broad-based re-pricing of tech valuations amidst the higher terminal rate. While keeping our earnings forecasts, we roll forward our valuation base year. Our revised TP is based on a 17.5x FY23F PER (from 22x FY22F PER), in line with the average forward PER of general suppliers along the LED value chain.

Refreshing catalyst. We have identified **PIE (OP; TP: RM3.70)** as one of our top picks in the sector owing to its unique clientele base as well as the ability to continue growing its margins amid various macro challenges such as labour shortages and rising component cost. Having been able to avoid the intensive competition surrounding household cleaning products, PIE has been presented with opportunities to take on reputable customers that provides strong order visibility, such as the big customer win (34% of group revenue) for a home entertainment product last year which grew the group's revenue above the RM1b mark. Building upon its achievement, the group had earlier this year secured another major Chinese customer (relating to application-specific integrated circuit or ASIC computer hardware) due to regulatory challenges in China which has forced the customer to relocate its production to Malaysia and PIE has been selected as their preferred vendor. The Chinese customer has decided to consign all the production materials, shielding PIE from rising component cost. Having only to bear the labour cost, this arrangement is expected to translate into better margins for PIE.

Maintain OVERWEIGHT stance on the technology sector. Our top picks are:

(i) **PIE (OP; TP: RM3.70).** We like PIE for its unique clientele exposure, providing a refreshing catalyst other than the highly competitive household cleaning products in the EMS segment. Riding on the big customer win back in FY21 which grew the group's revenue above the RM1b mark, PIE has secured another major Chinese customer that is relocating its production of application-specific integrated circuit (ASIC) computer hardware to Malaysia due to regulatory challenges in China. We believe this customer will be the main earnings driver for FY22 as PIE has dedicated an upcoming 120k sq ft factory and has received approval from the local government to bring in more foreign workers for this Chinese customer.

(ii) **INARI (OP; TP: RM3.30).** Being in the US smartphone supply chain, particularly in 5G radio frequency (RF) components, continues to be beneficial for INARI as the US smartphone brand was the only one to eke out YoY shipment gain of 2.2% in 1QCY22 while global shipment numbers were down 8.9% during the same period. The US smartphone manufacturer is expected to keep its smartphone production flat YoY for its upcoming model, an encouraging sign. Meanwhile, INARI is also working to grow other revenue streams from the data centre, automotive and memory space which could potentially morph into future earnings drivers.

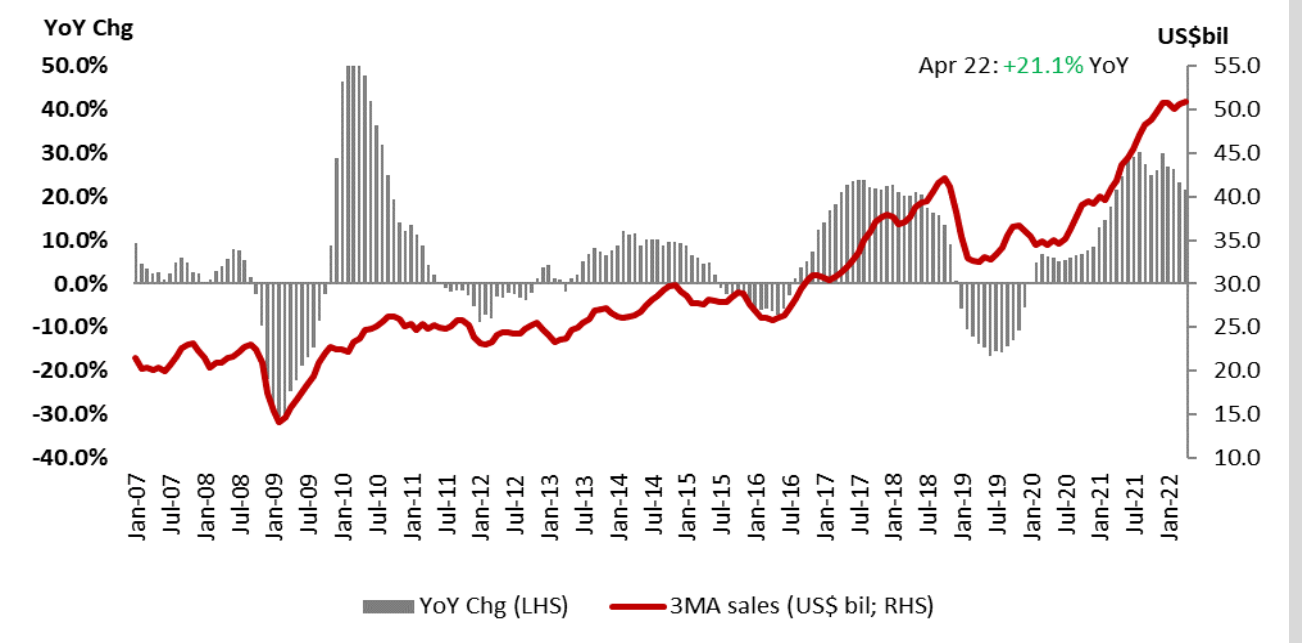
(iii) **MPI (OP; TP: RM32.90).** Having a healthy revenue exposure with 38% from automotive and 32% from data centre puts MPI is a comfortable spot to continue benefiting from the recovery in automotive as well as growing demand for digitalisation which in turn translates into data centre expansions. The group also has 22% revenue exposure in the communication segment where it is mainly involved in 5G infrastructure which will continue to be in good demand as development of 5G infrastructure still lags behind the vast 5G consumer devices that have been sold for the past 2-3 years. More importantly, MPI has future proofed their prospects by being the only OSAT in Malaysia capable of packaging wide bandgap (e.g. GaN and SiC) chips that have superior properties compared to the common silicon.

Worldwide PC Sales to End Users by Vendor (m of units)

	Shipments (units)			Growth		Market Share		
Company	1Q22	4Q21	1Q21	QoQ	YoY	1Q22	4Q21	1Q21
Lenovo	18.6	21.7	20.9	-14.5%	-11.1%	24%	25%	25%
HP	15.9	18.6	19.3	-14.9%	-17.8%	20%	21%	23%
Dell	13.8	17.2	13.0	-19.7%	6.1%	18%	19%	16%
Apple	7.0	6.8	6.4	2.3%	8.6%	9%	8%	8%
Asus	5.6	6.2	4.6	-9.6%	20.6%	7%	7%	6%
Acer	5.5	6.1	5.9	-9.4%	-5.5%	7%	7%	7%
Others	11.5	11.7	13.4	-1.8%	-14.1%	15%	13%	16%
Total	**77.9**	**88.4**	**83.5**	**-11.9%**	**-6.8%**	**100%**	**100%**	**100%**

Source: Gartner

Global Semiconductor Sales and YoY growth



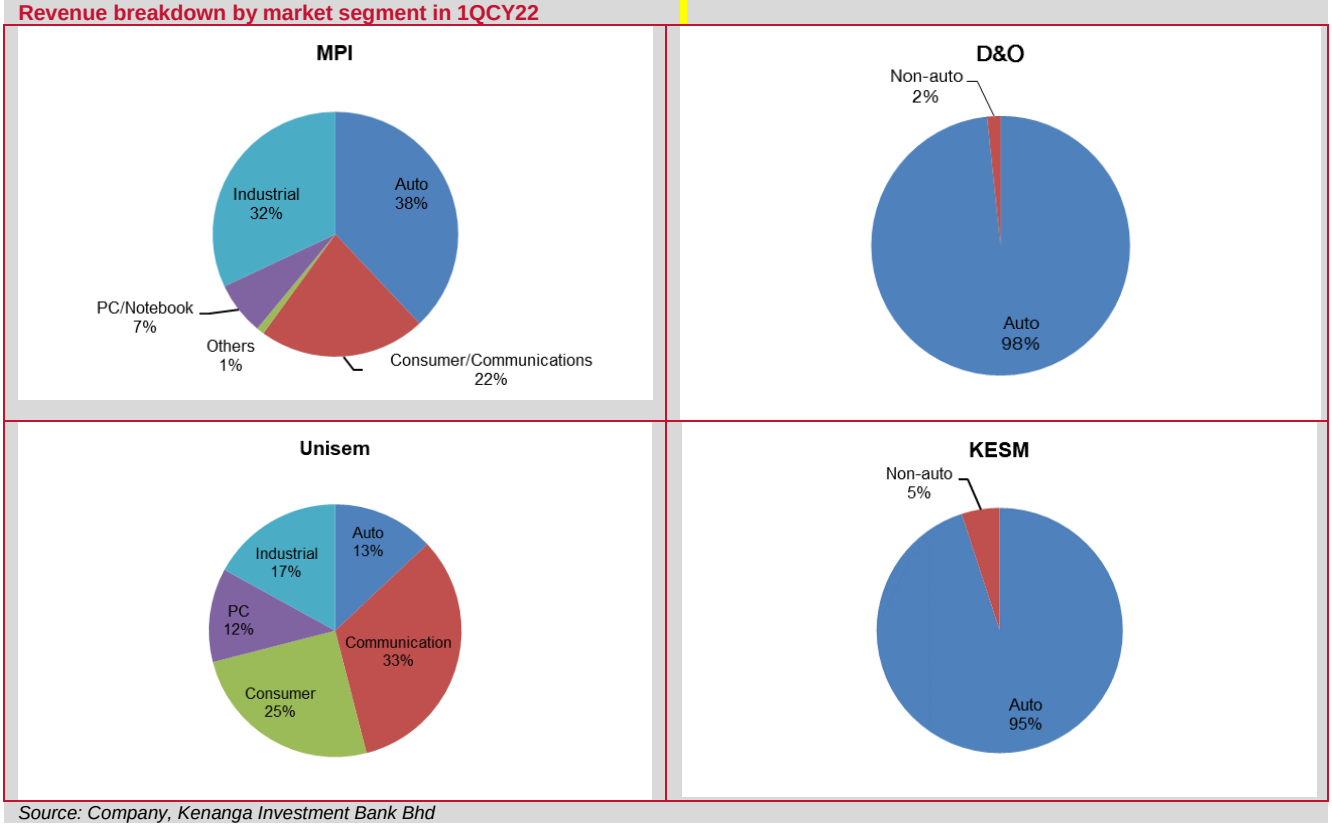
Source: SIA

WSTS Semiconductor Sales Forecasts by Product Type (Fall 2021 Q4 Update)

	US$ bil				YoY %			
	2020	2021	2022F	2023F	2020	2021	2022	2023F
Discrete Semiconductors	**23.8**	**30.3**	**33.4**	**34.7**	*-0.3*	*27.4*	*10.2*	*3.8*
Optoelectronics	**40.4**	**43.4**	**43.5**	**45.2**	*-2.8*	*7.4*	*0.3*	*3.7*
Sensors	**15.0**	**19.1**	**22.2**	**23.0**	*10.7*	*28.0*	*15.7*	*3.6*
Integrated Circuits	**361.2**	**463.0**	**547.3**	**576.8**	*8.4*	*28.2*	*18.2*	*5.4*
Analog	55.7	74.1	88.3	93.3	*3.2*	*33.1*	*19.2*	*5.7*
Micro	69.7	80.2	89.4	94.1	*4.9*	*15.1*	*11.4*	*5.3*
Logic	118.4	154.8	187.0	200.5	*11.1*	*30.8*	*20.8*	*7.3*
Memory	117.5	153.8	182.7	188.9	*10.4*	*30.9*	*18.7*	*3.4*
Total	**440.4**	**555.9**	**646.5**	**679.7**	***6.8***	***26.2***	***16.3***	***5.1***

Source: WSTS

Revenue breakdown by market segment in 1QCY22



Source: Company, Kenanga Investment Bank Bhd

Malaysian Technology Peers Comparison

Name	Last Price @ 17/06/22 (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net Div Yld (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
D&O GREEN TECHNOLOGIES BHD	4.04	4,998.1	Y	12/2022	28.0%	15.3%	34.0%	15.5%	41.4	30.9	26.8	6.0	5.1	17.1%	0.5%	4.50	OP
GHL SYSTEMS BHD	1.35	1,541.0	Y	12/2022	22.7%	7.0%	22.1%	13.9%	61.7	50.5	44.4	3.4	3.2	6.3%	0.0%	1.40	MP
INARI AMERTRON BHD	2.63	9,750.2	Y	06/2022	22.5%	7.0%	20.7%	7.1%	25.6	23.8	22.2	6.2	6.7	28.2%	3.8%	3.30	OP
JHM CONSOLIDATION BHD	1.19	663.5	Y	12/2022	10.7%	15.2%	38.6%	15.8%	25.9	18.7	16.1	2.8	2.4	12.6%	0.4%	1.40	MP
KELINGTON GROUP BHD	1.14	733.0	Y	12/2022	59.6%	1.7%	38.9%	1.8%	22.8	16.7	16.4	3.8	3.2	19.4%	1.5%	1.90	OP
KESM INDUSTRIES BHD	6.6	283.9	Y	07/2022	-0.2%	4.6%	-54.3%	294%	84.6	185.0	46.9	0.9	1.0	1.1%	0.7%	7.50	MP
MALAYSIAN PACIFIC INDUSTRIES BHD	29.5	5,867.4	Y	06/2022	18.0%	6.0%	19.4%	5.5%	22.6	19.0	18.0	4.4	3.8	16.6%	1.1%	32.90	OP
P.I.E. INDUSTRIAL BHD	3.07	1,179.0	Y	12/2022	18.3%	11.9%	28.2%	11.7%	17.5	13.7	12.2	22.1	1.8	13.5%	1.8%	3.70	OP
SKP RESOURCES BHD	1.61	2,515.4	Y	03/2023	17.3%	7.7%	27.5%	6.3%	13.6	12.8	11.9	2.9	2.6	20.0%	3.9%	2.10	OP
UNISEM (M) BHD	2.58	4,161.7	Y	12/2022	14.0%	10.0%	22.1%	11.3%	23.9	19.6	176	2.2	2.0	10.4%	2.0%	3.75	OP

Source: Kenanga Research

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Telecommunications

Warming up to Single Wholesale Network

OVERWEIGHT ↑

By Ahmad Ramzani Ramli I ahmadramzani@kenanga.com.my

We raise our call for the sector to OVERWEIGHT from NEUTRAL. We believe telcos and investors alike are warming up to the Single Wholesale Network (SWN) model, which they had resisted previously. We believe the steep de-rating of the sector in recent months has adequately reflected the market's reservation on the model, which means a reversal in share prices, may be on the cards once the dust finally settles. We also see telcos as a service-based industry that is able to maintain their profit margins amidst high inflation by keeping wage pressures at bay. Our top picks within the sector are DIGI (OP; TP: RM3.70) and TM (OP; TP: RM6.70).

Single Wholesale Network is inevitable. The deadline of the Telco's equity participation in DNB's is fast approaching and we take the view that the telcos will accept it as they cannot afford to sit out the next big evolution in the digital-based economy driven by the 5G technology and Industrial Revolution 4.0. The remaining question to be answered is the quantum of the equity participation of large MNOs (Celcom, Digi, Maxis and Umobile) in DNB, the holding company for the SWN. We do not rule of the possibility of the large MNOs being granted a greater equity participation in DNB in exchange for their unwavering support for the SWN model.

A win-win situation. While concerns have been raised on DNB's wholesale fixed capacity charges to support its bond-raising requirements, we do not expect a material increment in the telcos total outlay to DNB thus cost, funding structure and timeline would probably be revised by the new investors (the MNOs) which could influence DNB's pricing mechanism, procurement strategies and cost management, benefitting the MNOs in the long run. Furthermore, we believe the commitment by the MNOs to DNB's equity participation could likely boost DNB's credit rating in its bond-raising exercise. This is also a win for national interest as it accelerates Malaysia's IR 4.0 progress, boosted by efficient mobile speeds at affordable tariffs.

OVERWEIGHT. We feel the uncertainties surrounding the 5G rollout have been priced in by the market; thus there will be potential rerating on the sector once the dust finally settles. Our **NEUTRAL** rating is raised to **OVERWEIGHT** for the sector. While there are no changes to our FY22E/FY23E earnings, TP are revised down for all to reflect higher cost of debt (on a higher risk-free rate). **AXIATA (OP; TP: RM3.45**), **DIGI (OP; TP: RM3.70), MAXIS (OP; TP: RM3.90), OCK (OP; TP: RM0.45) and TM (OP; TP: RM6.70)** are all rated **OUTPERFORM** with **DIGI also raised to OUTPERFORM**. The implied FY23 EV/EBITDA multiples of for the TPs are reflected in the table on the next page. Our top picks for the sector are **DIGI and TM.** We like **DIG**I for the following reasons: (i) impending merger with Celcom AXIATA, (ii) returning foreign workers will boost its prepaid subscription segment, and (iii) superior EBITDA margins among the telcos. We like TM for its foray into the mass market and it being one of the pioneers in 5G service in Malaysia which should drive its broadband subscriptions.

Top Picks

DIGI (OP, TP: RM3.70). We view it as an exciting proposition due to its impending merger with CELCOM AXIATA. The new entity will have the biggest market share in the mobile market at 44% (based on MCMC's Dec 2021 figures) dwarfing other MNO's and outpacing its nearest competitor's market share by 21%. In the recent 1QCY21, mobile subscribers for the combined entity saw a 3% YoY uptick vs its nearest rival's flattish growth. In the postpaid arena, its nearest rival which has a 30% market share (4QCY21) will be dwarfed by the combined entity's 46%. The nearest rival is well known for its elites' demographics but will be eclipsed by the new entity which is well entrenched in the public sector and migrant workers space. The reopening of the economy and influx of foreign workers will support DIGI's growth in the prepaid arena in the coming months. DIGI's margin has always been solid, the best in our Telco Universe at 49% outpacing the industry's average of 41%. Its quantum of debt is among the lowest among the Big 4 which will keep its interest expense the lowest among the Big 4. Our new TP is at RM3.70 based on a DCF (WACC: 6.6%, TG: 1%) implying a FY23E EV/EBITDA of 10x. We feel this is justifiable given its historical multiple of 13x – the lower multiples to reflect rising funding costs and spectrum lease. Its dividend payout is among the highest and with dividend yield of c.4%, we raised it to **OUTPERFORM.**

TELEKOM (OP, TP: RM6.70). Our revised TP implies a FY23E EV/EBITDA of 6.0x (vs its historical 6.5x). It is among the first to adopt 5G and its home broadband market share is at c.70%. We believe the adoption to 5G has helped to contribute to Unifi's subscription continued resilience (+5% QoQ, +35% YoY) on top of the limited availability of 5G at the market - as we had expected it to slow down as the work-from-home trend starts to fade. ARPU has continued to slide down which we had expected given the aggressive promotion of its UNIFI broadband. The reopening of the economy should see gradual recovery in enterprise spending, hence TM ONE could start to see growth after 5 consecutive years of declining revenue.TM has almost completed its nationwide fibre network expansion of 6m premises (under the Jendela Initiative) which would accelerate its 5G services.

Appendix

Table 1: Valuations

Companies	Target Price (RM)	Rating	Valuation Method	TP Implied FY23 EV/EBITDA (x)
AXIATA GROUP BHD	**3.45**	**OP**	Sum-of-parts (refer below)	
DIGI.COM BHD	**3.70**	**OP**	Discounted cash flow (WACC: 6.6%, TG: 1.0%)	**10.0**
MAXIS BHD	**3.90**	**OP**	Discounted cash flow (WACC: 7.4%, TG: 1.0%)	**9.0**
OCK GROUP BHD	**0.45**	**OP**	Discounted cash flow (WACC: 6.5%, TG: 1.0%)	**6.5**
TELEKOM MALAYSIA BHD	**6.70**	**OP**	Discounted cash flow (WACC: 8.4%, TG: 1.0%)	**6.0**

Source: Kenanga Research

Table 2: AXIATA Sum-of-Parts Valuation

Companies	Valuation Method	Earnings Multiple	Enterprise Value (RM' m)	Axiata's Stake (%)	Value to Axiata (RM' m)
XL (Indonesia)	DCF	WACC: 9.5%, TG: 2.0%	19,410	61.5%	11,937
Robi (Bangladesh)	EV / EBITDA	7.7x	12,924	61.9%	8,229
Dialog (Sri Lanka)	EV / EBITDA	3.0x	3,798	83.3%	3,258
Ncell (Nepal)	EV / EBITDA	5.0x	4,825	80.0%	3,921
Smart (Cambodia)	EV / EBITDA	6.0x	5,219	72.5%	4,096
Axiata Digital Services	EV / Sales	20.0x	3,960	100.0%	-
edotco	EV / EBITDA	9.0x	14,058	63.0%	9,162
			Total Enterprise Value		**40,602**
			(-) FY22E Net Debt and Minority Interest		25,477
			(+) Celcom Digi 33% Value to AXIATA		**16,537***
			Total Equity Value		**31,662**
			Fair Value/Share (RM)		**3.45**

** After NewCo discount of 80%*
Source: Kenanga Research

Table: CELCOM DIGI Valuation (RM'm)

CDB EBITDA	6,308
Asc. EV/EBITDA (x)	10
CDB Target EV	62,445
- Debt	12,315
- Additional Debt	1,700
+ Cash	1,944
- Cash to AXIATA	2400
CDB Target MC	**47,974**
NOSO (m)	11,732
CDB TP (RM)	**4.09**

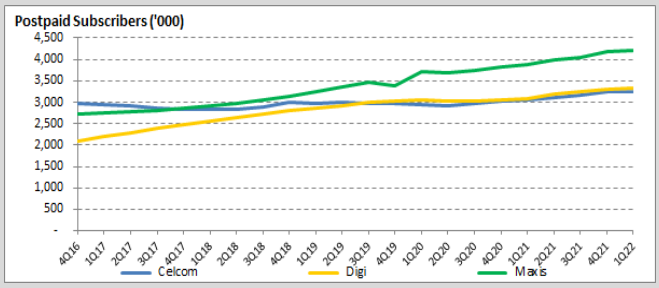
Source: Kenanga Research

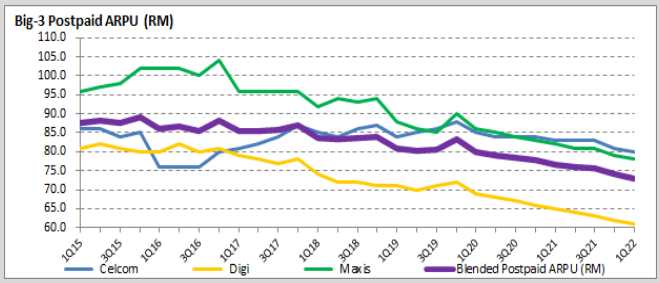
Table 3: Malaysia's 5G rollout timeline

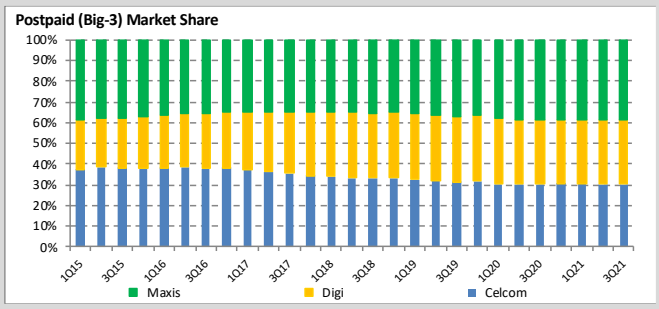
Time	Goals
End-2021	Launched 5G in Putrajaya, Cyberjaya and selected areas in Kuala Lumpur.
2022	Deploy 5G in 5 major cities and districts in Selangor, Penang, Johor, Sabah and Sarawak.
2023	Expansion to 17 cities and rural areas.
2024	Achieve 80% 5G population coverage.
2025-2030	>90% coverage in populated areas (by 2027).

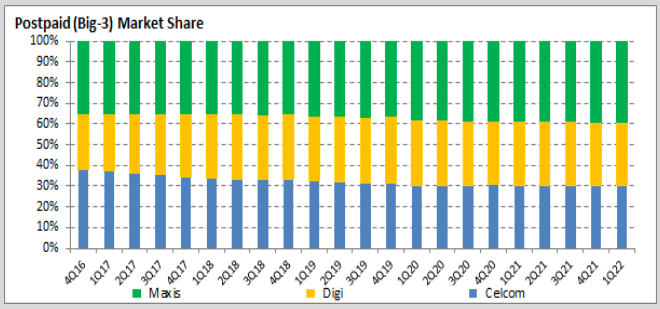
Source: Digital Nasional Berhad, Kenanga Research

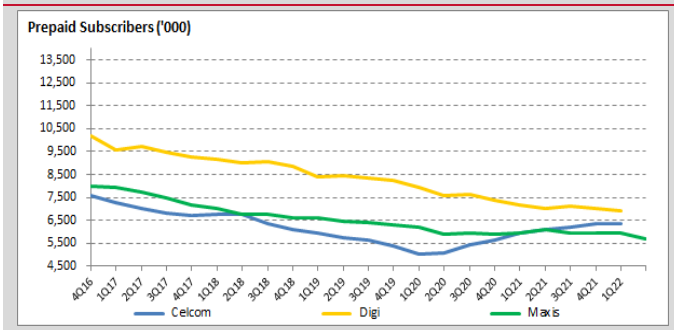
Mobile Market Share and ARPU (Average Revenue Per User)

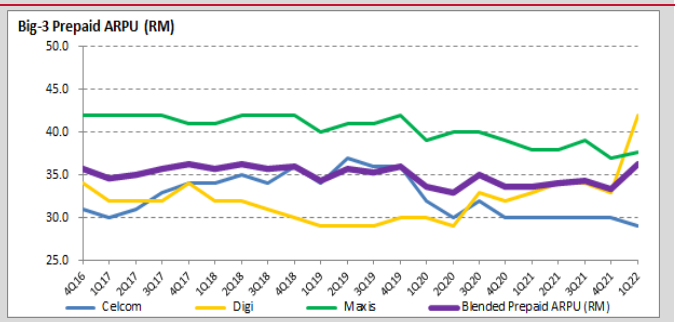


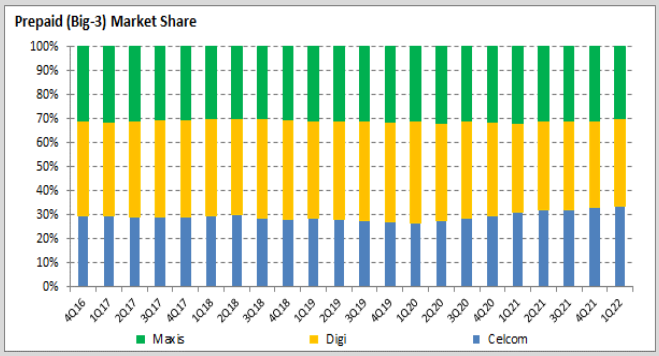


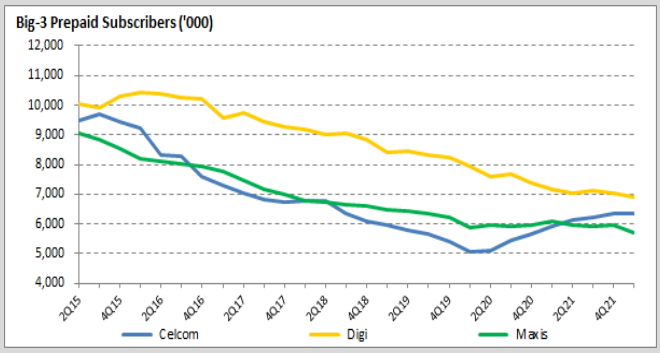












Source: MCMC, Companies, Kenanga Research

Peer Table Comparison

Name	Last Price @ 17/6/2022 (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)	Net DivYld (%)	Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.		
Stocks Under Coverage																	
AXIATA GROUP BHD	2.75	25,236.2	Y	12/2022	5.0%	2.5%	-3.1%	7.0%	19.0	19.6	18.4	1.4	1.4	7.2%	4.4%	3.45	OP
DIGI.COM BHD	3.18	24,724.5	Y	12/2022	1.1%	4.5%	-8.9%	26.3%	21.8	23.9	18.9	39.1	38.4	162.0%	4.2%	3.70	MP
MAXIS BHD	3.22	25,200.6	Y	12/2022	3.0%	2.5%	-6.0%	20.4%	18.8	20.0	16.6	3.7	3.8	18.7%	5.0%	3.90	OP
OCK GROUP BHD	0.390	411.3	Y	12/2022	6.8%	6.0%	36.6%	12.6%	17.7	13.0	11.5	0.6	0.6	4.6%	0.0%	0.45	OP
TELEKOM MALAYSIA BHD	5.06	19,094.9	Y	12/2022	5.3%	3.6%	-1.4%	13.8%	16.2	16.4	14.4	2.6	2.5	15.6%	3.4%	6.70	OP
Simple Average					**4.2%**	**3.8%**	**3.5%**	**16.0%**	**18.7**	**18.6**	**16.0**	**9.5**	**9.3**	**41.6%**	**3.4%**		

Source: Kenanga Research

Utilities

Defensive Power

OVERWEIGHT

↔

By Teh Kian Yeong I tehky@kenanga.com.my

The Utilities Sector is maintained at OVERWEIGHT for their defensive earnings profile which also supports above average dividend yields. This has been proven during the pandemic era with earnings staying resilient thanks to the industry's regulated/concessionary mechanism. Fuel prices, especially coal price has skyrocketed and jumped more than triple from the base price. However, this should be earnings-neutral to TENAGA as the higher fuel cost would eventually be passed to end-user or partially funded by KWIE fund under the IBR mechanism. Meanwhile, gas utilities PETGAS and GASMSIA are in their final year of RP1 and we still expect resilient earnings even in the coming RP2. On the other hand, with the completion of the acquisition of Tuaspring, earnings prospect for YTLPOWR gets brighter. MALAKOF should also see the normalisation of IPP earnings with planned outages fully completed.

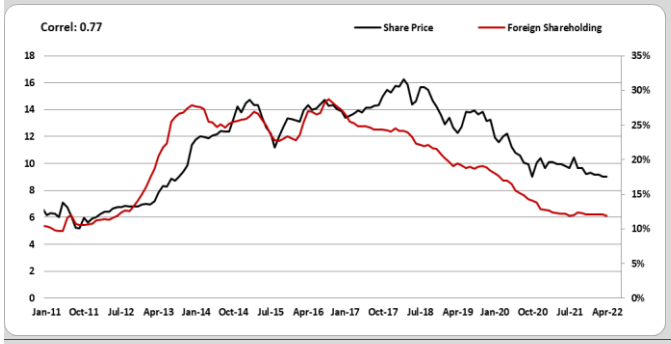
Power utilities: to see higher surcharge in 2HCY22, given the skyrocketing fuel prices globally where the Indonesia coal benchmark price jumped 54% to USD282.02/MT on average for Apr and May as opposed to the average of USD183.52MT in 1QCY22. This is against the coal base price of USD79/MT @ 4.123/MYR under the RP3 parameter. Assuming coal price stays at an average of USD282.02/MT in 2QCY22 with unchanged coal generation mix as 1QCY22 at **TENAGA (OP; TP: RM10.81)**, total coal cost would increase c.RM3.28b QoQ in 2QFY22. As such, its 1HFY22 total coal cost would be c.RM8.6b or 24.9 sen/kWh higher based on the coal base price of USD79/MT. Nonetheless, under the IBR mechanism, the increased cost will eventually pass through to consumers or partly offset by KWIE fund with a 6-month lag. Therefore, TENAGA may take a hit in the near term for the lag effect and this may have been reflected in the recent heavy sell-down. In rationalising our valuation method, we decided to switch to DCF from PER methodology to value TENAGA to derive a new TP of RM10.81 based on WACC of 7.1% with a terminal growth of 2%.

Gas Utilities: high earnings certainty. With RP1 to end this year, **PETGAS (MP; TP: RM17.51)** is expected to see a step-down tariff rate in RP2 over 2023-2025 which possesses earnings downside risk. However, this should be mitigated by new earnings kickers from two major projects, namely a RM541m gas pipeline project to cater for an IPP in Pulau Indah by 1QFY23 and the RM460m gas compressor station project in Kluang by 1QFY24 which should add new value to its already ageing book value to improve profitability as these assets are mostly 20-30 years old assets with low carried value. Thus, these two new assets should add value to its regulated asset base and hence higher returns. On the other hand, despite market liberalisation which started from Jan 2022, **GASMSIA (OP; TP: RM3.10)** is expected to see strong earnings going forth of which it had shown in its recent 1QFY22 results as it was able to expand its margin spread from GMES, arising from better deal in contract renegotiation coupled with higher retail margin as gas prices spiked. With its shortest contract tenure of three years, this means GASMSIA could be able to maintain its superb retail margin for a minimum of three years. In all, GASMSIA's total margin spreads are likely to stay high at RM2.40/mmbtu for FY23 and FY24.

IPPs earnings to recover further. After a disappointing last quarter, we expect upcoming **MALAKOF's (OP; TP: RM0.98)** 2QFY22 and **YTLPOWR's (OP; TP: RM1.11)** 4QFY22 results to improve on the back of the completion of repairing work for forced outage at TBE on 14 Feb for the former while the latter had completed the acquisition of Tuaspring on 1 Jun which should add value to PowerSeraya. In addition, Alam Flora has been posting improving results consistently since early 2020, which should ensure MALAKOF's earnings certainty making its dividend payout more sustainable. On the other hand, with c.RM3b cash proceed from the disposal of ElectraNet, we believe YTLPOWR will continue to look out for new investment, in addition to its recent new ventures, such as building YTL Green Data Center Park, and it intends to develop LSS both in Johor, as well as winning a digital banking license along with Sea Ltd's Shopee. Meanwhile, **PESETCH (OP; TP: RM0.66)** expects to see soft earnings till FY23 given the challenging market conditions such as slowdown in activities and award of new jobs while the rising building material costs would erode profit margin for existing contracts. However, we continue to like this niche utility infrastructure play which could potentially benefit from the revival of mega rail projects domestically, new rail projects with the ASEAN market and the fast-growing energy infrastructure development market in Indonesia.

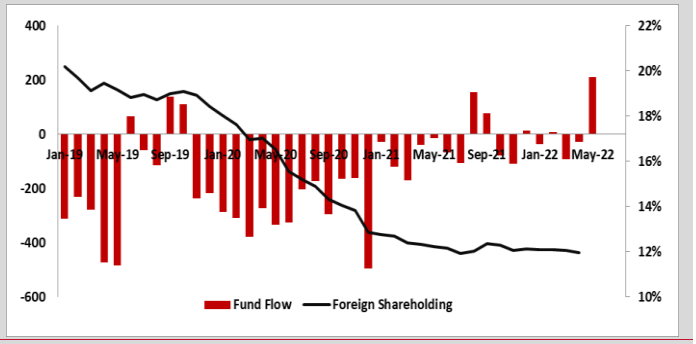
Defensive earnings; OVERWEIGHT retained. While its less-exciting GDP-growth-like earnings growth may not appealing, the regulated business environment has had helped the Utilities players sailing through previous economy downturns and the COVID-19 pandemic period has indeed demonstrated such earnings defensiveness for the sector players. The regulated environment has also helped to sustain their above average dividend yield of 5%-7%. Earnings of TENAGA, PETGAS and GASMSIA are fairly resilient, being regulated under the IBR framework while IPPs MALAKOF and YTLPOWR's earnings are backed by PPA with new assets helping to bridge earnings gap as certain old IPP assets are expiring. Meanwhile, niche utility infrastructure play PESTECH offers an exciting growth story in Cambodia coupled with promising rail electrification contract flows in the region. Thus, we reiterate our OVERWEIGHT rating on the sector.

TENAGA: Share Price vs. Foreign Shareholding



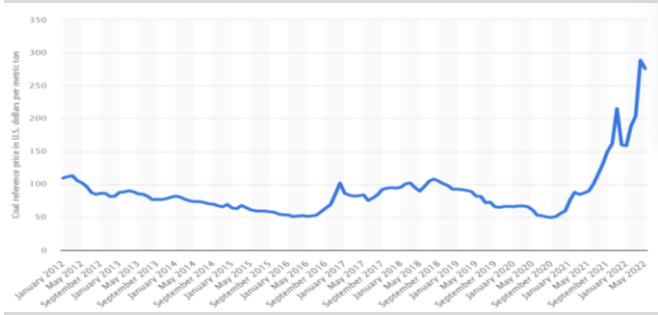
Source: Company/Bloomberg

TENAGA: Foreign Fund Flow vs. Foreign Shareholding



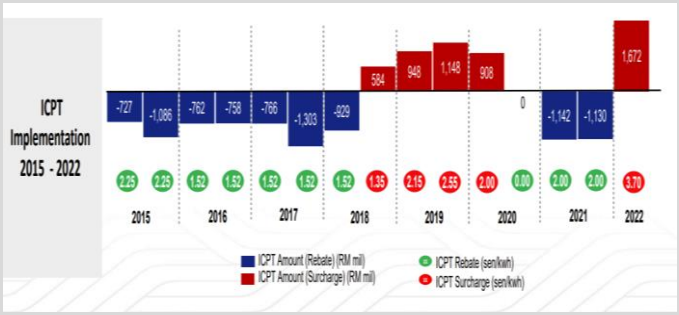
Source: Company/DIBots

Indonesia Coal Benchmark Price



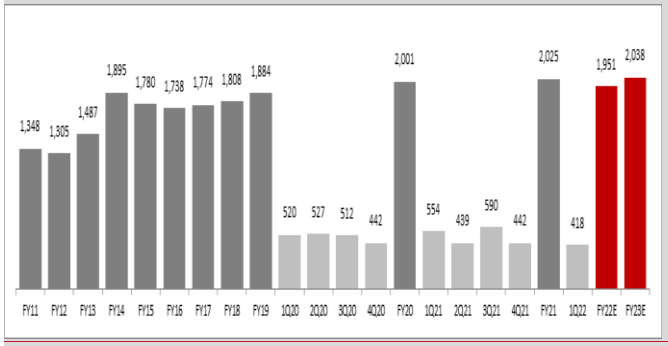
Source: Stastita

TENAGA: ICPT Adjustment



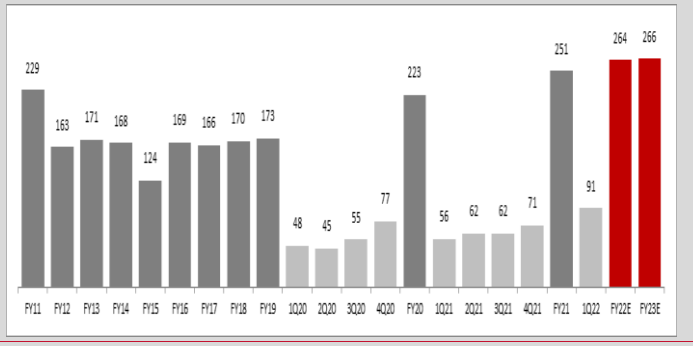
Source: Company

PETGAS: Profitability



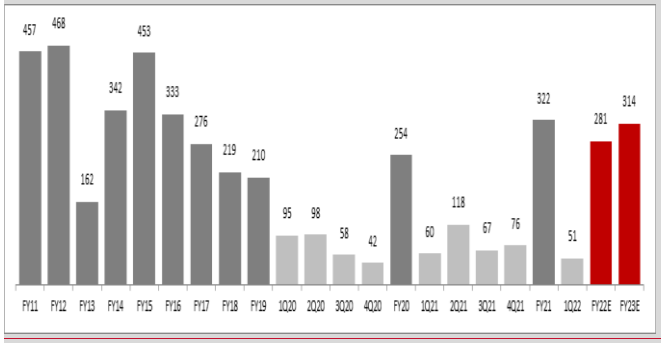
Source: Company

GASMSIA: Profitability



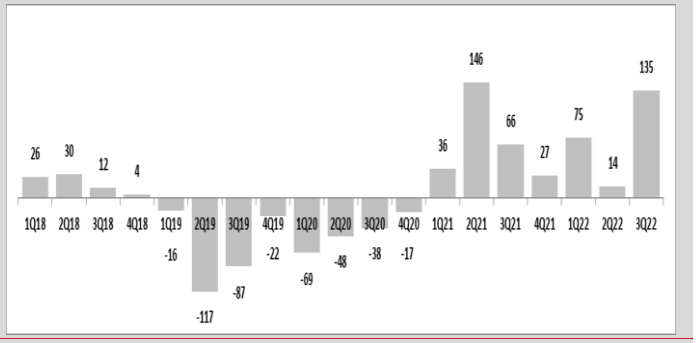
Source: Company/DIBots

MALAKOF: Profitability



Source: Company

YTLPOWR: PowerSeraya Quarterly PBT



Source: Company

Peer Comparison

Name	Price @ 17 Jun 2022 (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
GAS MALAYSIA BHD	3.01	3,864.8	Y	12/2022	9.3%	8.3%	5.1%	0.6%	15.4	14.6	14.5	3.4	3.3	23.1%	6.1%	3.10	OP
MALAKOFF CORP BHD	0.585	2,858.9	Y	12/2022	22.8%	-5.8%	-12.6%	11.8%	9.1	10.4	9.3	0.5	0.5	5.2%	7.7%	0.980	OP
PESTECH INTERNATIONAL BHD	0.415	408.6	Y	06/2022	-10.1%	-6.3%	-30.1%	3.8%	5.5	7.8	7.6	0.7	0.6	8.2%	0.0%	0.660	OP
PETRONAS GAS BHD	16.04	31,738.9	Y	12/2022	1.0%	-0.8%	-3.7%	4.5%	15.7	16.3	15.6	2.4	2.4	14.8%	5.2%	17.51	MP
TENAGA NASIONAL BHD	8.30	47,526.6	Y	12/2022	-3.3%	1.8%	-0.8%	13.1%	9.9	10.0	8.8	0.8	0.8	8.3%	5.0%	10.81	OP
YTL POWER INTERNATIONAL BHD	0.680	5,509.5	N	06/2022	31.8%	1.5%	-61.4%	104.7%	12.0	31.1	15.2	0.4	0.4	1.4%	7.4%	1.11	OP
Simple Average					**8.6%**	**-0.2%**	**-17.2%**	**23.1%**	**11.2**	**15.0**	**11.8**	**1.4**	**1.4**	**10.2%**	**5.2%**		

Source: Bloomberg, Kenanga Research

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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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