

Sector Note

I Malaysia

Overweight (no change)

Highlighted companies

Gamuda

ADD, TP RM5.88, RM4.59 close

Gamuda provides the biggest exposure to MRT and Penang TMP and, therefore, is not a pure water infra play. The potential conclusion of the sale of 40%-owned Splash is its only angle in Selangor.

Puncak Niaga Holdings

ADD, TP RM3.40, RM2.88 close

Puncak Niaga is also a water infra contractor but its focus appears to be more in East Malaysia and less in Klang Valley at this juncture. Its estimated outstanding order book is less than RM400m.

Salcon

ADD, TP RM0.95, RM0.63 close

Salcon's diverse tender book of RM1bn-2bn covers water, sewerage and desalination plant jobs and non-revenue water (NRW) contracts. We also expect it to be in the running for Langat 2 WTP phase 2 (worth over RM800m).

Summary valuation metrics

P/E (x)	Dec-15F	Dec-16F	Dec-17F
Gamuda	16.34	15.93	14.48
Puncak Niaga Holdings	4.64	4.48	4.30
Salcon	82.76	21.58	18.54
P/BV (x)	Dec-15F	Dec-16F	Dec-17F
Gamuda	1.74	1.72	1.69
Puncak Niaga Holdings	0.56	0.56	0.56
Salcon	0.98	0.87	0.76
Dividend Yield	Dec-15F	Dec-16F	Dec-17F
Gamuda	2.52%	2.52%	2.52%
Puncak Niaga Holdings	0.00%	0.00%	0.00%
Salcon	4.76%	4.76%	5.56%

Analyst



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Construction

A monsoon of water jobs in the pipeline?

- Based on recent data points, the momentum of government and private sector-funded water projects should play catch-up with non-water contracts.
- 5% of total RM49bn development expenditure for 2016 earmarked for water infra jobs. We project a wave of recovery for this segment.
- Bigger names in the sector are unlikely to be promising contenders but we expect smaller-cap integrated water players to benefit strongly.
- Salcon offers the biggest exposure to new domestic water infrastructure contracts in addition to wastewater/sewage tenders. We retain Add on Salcon.

RM12bn for water jobs under 11MP

There is a high chance that water contracts could be revived. Based on recent data points, the momentum of government and private sector-funded water projects should play catch-up with non-water contracts. The government's large budget substantiates this, with RM12bn in total under 11MP (over five years from 2016), based on our compilation. We believe the bulk of the budget allocation excludes pipe replacement given the focus on treatment plants, implying that eventual spending could be higher.

Budget 2016 allocation higher than the 7-year average

One of the key catalysts for a comeback in water projects is Budget 2016. 25% of the total RM2.2bn is specifically for the upgrading and building of new water treatment plants (WTPs) nationwide. This is slightly higher than the average allocation p.a. in the past seven years, which is positive for the backlog of water capex in Klang Valley and, more importantly, in Selangor. This also means that there could be several tenders for WTP upgrades in other states. The other catalyst is Selangor's industry consolidation.

Over RM2bn worth of awards to address backlog of water capex

We expect over RM2bn worth of water-type contracts to be awarded largely in 2016. This does not include potential jobs from the private sector side. Overall, this is good news for pure water infra contractors, where the average order book based on our checks is currently running at below RM1bn. Salcon, which is the only pure water infra contractor under our coverage, could emerge with a bigger share of wins. Its tender book (jobs in tender) stands at RM1bn-2bn.

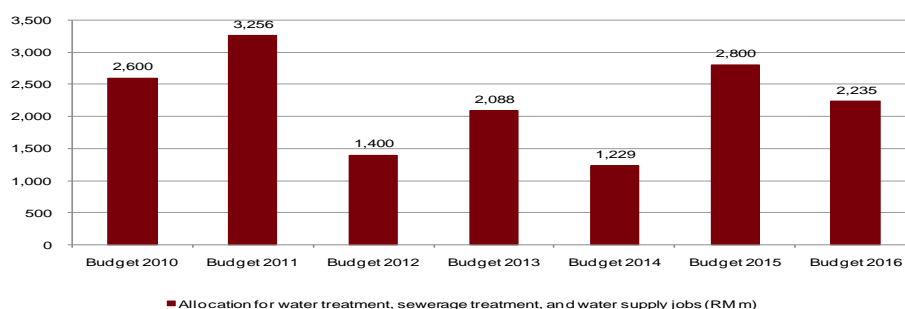
Salcon more attractive than Puncak Niaga for water infra

With the exit of Puncak Niaga from the water business in Selangor, Salcon now looks more attractive given its position among the contractors that could benefit from new tenders post the water consolidation in the state. The critical water reserve margin of below 5% in the state implies that new alternative water supply jobs will be expedited before the implementation of Langat 2 WTP phase 2 (RM800m to RM1bn in value). Salcon is also in the running for this job given its advantage in phase 1.

Maintain Overweight

Smaller-cap integrated water contractors offer good order book growth prospects. Within our coverage, Salcon provides the only exposure as its larger peers are focused on other segments. We maintain our Overweight call on the construction sector. Gamuda remains our top big-cap pick while Muhibbah is our preferred small/mid-cap stock.

Figure 1: Allocation for water jobs in Budget 2010-16 (RM m)

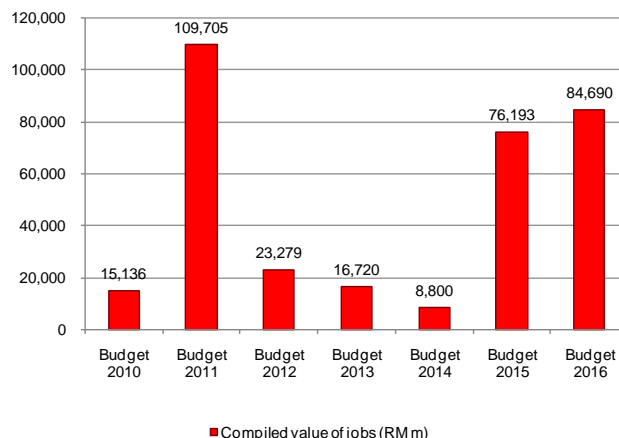


SOURCES: CIMB RESEARCH, COMPANY

KEY CHARTS

Total value of jobs in focus across seven Budgets since 2010

The RM85bn total value of jobs compiled under Budget 2016 is 11% higher than in Budget 2015. This kicks off the 11th Malaysia Plan's (MPs) first year of implementation, of which 91% of the total value of jobs planned are deemed high value/high impact, including RM12bn for rural water supply, sewerage treatment plants (STPs) and sewerage pipe networks.



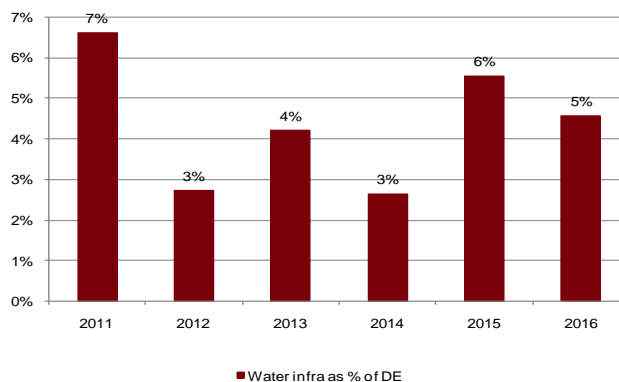
Water jobs still retain a meaningful share

Water-related projects still account for a meaningful allocation in 2016. 3% of the compiled value of total jobs of RM85bn, or RM2.2bn, will be used to implement water, drainage and water treatment plant (WTP) contracts. This value does not include private sector tenders and is likely to exclude potential major pipe replacement works in the Klang Valley.

Categories	RM m	% of total
Non-tolled roads	31,200	36.8%
Rail	38,000	44.9%
Highways	9,480	11.2%
BRT	2,500	3.0%
Airports	42	0.0%
Water/WTPs/drainage	2,235	2.6%
Rural electrification	878	1.0%

Water jobs as % of total DE

Over the past seven Budgets, water infra allocation made up 5-7% of total development expenditure (DE) p.a. The reducing proportion is due to the inclusion of higher-value non-water infra contracts, such as MRT 2, LRT 3 and the Pan-Borneo Highway, in 2016's budget. Nevertheless, the absolute value remains sizeable if set against the average water contractors' outstanding order book of less than RM1bn.



Salcon's order book growth prospects

Salcon's diverse tender book of RM1bn-2bn covers water, sewerage and desalination plant jobs and non-revenue water (NRW) contracts. We also expect it to be in the running for Langkat 2 WTP phase 2, which is worth over RM800m.

Type of local jobs in tender/tender book	RM m	% of total tender book	Success rate %	Potential win	
				(RM m)	Time line
Sewerage treatment plants (STP)	1,158	53%	30%	347.4	12-18 months
Desalination plant	900	41%	20%	180	12-18 months
Water treatment plants (WTP)	110	5%	20%	22	12-18 months
Non-revenue water (NRW) related	36	2%	20%	7.2	12-18 months
Total	2,204			556.6	
Current outstanding order book (Oct 2015)				652.0	
Potential enhancement to order book				85%	

SOURCE: CIMB, COMPANY REPORTS

Figure 2: Sector comparison

Company	Bloomberg Ticker	Recom.	Price (local curr)	Target Price (local curr)	Market Cap (US\$ m)	Core P/E (x)		3-year EPS CAGR (%)	P/BV (x)		Recurring ROE (%)			EV/EBITDA (x)		Dividend Yield (%)		
						CY2015	CY2016		CY2015	CY2016	CY2015	CY2016	CY2017	CY2015	CY2016	CY2015	CY2016	
Benalec Holdings	BHB MK	HOLD	0.61	0.56	110	61.7	12.9	19.5%	0.73	1.22	1.2%	7.6%	22.5%	17.6	10.6	0.0%	1.6%	
Gamuda	GAM MK	ADD	4.59	5.88	2,520	15.0	16.3	1.4%	1.88	1.74	12.7%	11.1%	10.9%	16.5	13.5	2.5%	2.5%	
Malaysian Resources Corp	MRC MK	ADD	1.45	1.40	591	43.9	26.9	na	1.63	1.40	3.9%	6.1%	7.3%	43.2	18.9	1.7%	2.1%	
Malaysian Resources Corp	MRC MK	ADD	1.45	1.40	591	43.9	26.9	na	1.63	1.40	3.9%	6.1%	7.3%	43.2	18.9	1.7%	2.1%	
Muhibbah Engineering	MUHI MK	ADD	2.20	2.89	235	10.8	9.4	2.9%	na	na	13.7%	14.6%	15.2%	7.5	5.4	1.8%	2.0%	
Mudajaya Group	MDJ MK	HOLD	1.16	1.13	143	na	42.5	-48.7%	0.58	0.58	-6.6%	1.5%	2.7%	na	15.9	5.2%	3.4%	
Salcon	SALC MK	ADD	0.63	0.95	97	na	82.8	na	0.77	0.98	-7.3%	1.0%	4.3%	na	18.4	4.8%	4.8%	
Sunway Bhd	SWB MK	ADD	3.06	3.95	1,249	8.9	8.6	-1.5%	0.89	0.92	11.2%	11.5%	11.0%	8.5	11.5	3.6%	12.1%	
WCT Holdings	WCTHG MK	ADD	1.34	1.63	365	14.8	13.6	-23.6%	0.74	0.68	5.4%	5.7%	5.8%	26.5	12.0	2.9%	2.9%	
YTL Corporation	YTL MK	ADD	1.52	1.90	3,614	12.2	13.3	-1.1%	1.11	1.08	9.3%	8.2%	9.2%	9.0	9.5	7.2%	6.6%	
Malaysia average							14.5	14.1	2.5%	1.24	1.22	8.7%	8.8%	9.4%	11.3	10.7	4.4%	5.1%
Adhi Karya	ADHI IJ	ADD	2,225	3,000	582	15.8	13.0	11.6%	2.30	0.97	16.1%	11.5%	11.5%	6.8	2.1	1.1%	0.7%	
Nusa Raya Cipta	NRCA IJ	ADD	660.0	950.0	121	5.9	7.7	-11.7%	1.65	1.44	32.6%	21.1%	14.4%	7.5	9.2	2.9%	4.2%	
Pembangunan Perumahan	PTPP IJ	ADD	3,675	4,500	1,307	33.4	26.1	20.4%	7.45	6.02	25.4%	27.1%	29.7%	10.3	9.8	0.5%	0.7%	
Total Bangun Persada	TOTL IJ	ADD	700.0	1,180	175	14.8	12.5	-3.7%	2.99	2.68	21.8%	23.8%	23.9%	7.6	8.1	4.2%	4.1%	
Wijaya Karya	WIKA IJ	HOLD	2,755	2,900	1,244	27.5	29.2	2.2%	4.24	3.86	18.5%	14.8%	17.5%	10.2	13.2	1.0%	1.1%	
Waskita Karya	WSKT IJ	ADD	1,685	2,300	1,679	32.4	22.4	32.3%	5.71	2.54	20.3%	15.6%	12.1%	15.9	7.1	0.7%	0.7%	
Indonesia average							25.2	21.7	12.6%	0.13	0.07	21.2%	17.1%	15.9%	10.5	8.7	34.2%	40.2%
CH. Kamchang	CK TB	HOLD	27.75	25.00	1,308	20.2	25.0	27.1%	2.46	2.15	13.0%	9.5%	9.9%	19.8	18.5	2.0%	1.8%	
Italian-Thai Development	ITD TB	REDUCE	7.70	5.10	1,132	85.4	54.6	6.3%	2.89	2.88	3.6%	5.3%	6.6%	18.7	17.2	0.6%	0.6%	
Sino-Thai Eng & Construction	STEC TB	ADD	24.70	30.00	1,049	24.8	27.0	-5.2%	4.51	4.16	19.3%	16.7%	15.6%	14.7	16.0	1.6%	1.9%	
Thailand average							28.8	31.3	8.9%	3.02	2.78	11.2%	9.5%	10.0%	18.0	17.3	1.4%	1.4%
Hindustan Construction	HCC IN	ADD	23.00	44.80	270	na	na	na	1.32	1.02	-14.7%	-1.3%	3.7%	12.3	8.9	0.3%	1.0%	
NCC Limited	NJCC IN	ADD	75.40	91.30	632	37.4	17.3	143.6%	1.36	1.22	4.1%	7.5%	10.5%	7.4	5.6	0.7%	1.2%	
India average							na	26.9	na	1.35	1.15	-1.9%	4.7%	8.2%	9.6	7.0	0.6%	1.1%
Average (all)							18.8	17.4	7.3%	1.68	1.56	9.3%	9.4%	10.2%	11.7	10.7	3.0%	3.4%

SOURCE: CIMB RESEARCH, COMPANY

RELEASING THE WATER INFRA BACKLOG

Water accounts for 5-7% of total DE annually

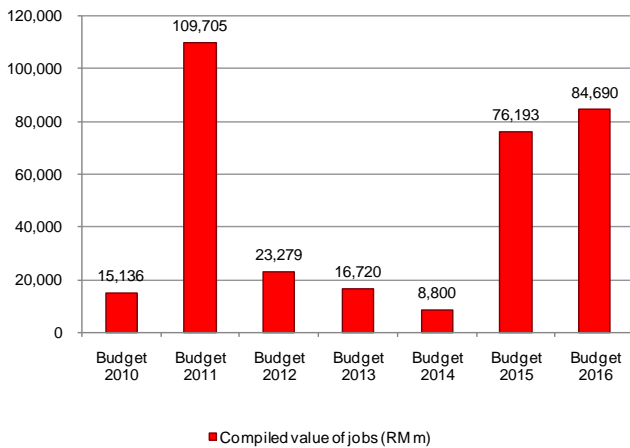
Water contracts have typically accounted for an average of 4% (RM2.2bn-3.3bn) of the government's total annual budgeted expenditure since 2011. Most water capex is federal government-driven while the private sector is usually involved in selected sewerage treatment plants for specific industrial growth areas or major residential townships that require smaller processing capacities. Separately, the 11MP has allocated a more longer-term budget of RM12bn for rural water projects and water treatment plants (WTPs) over the next five years. This underpins sizeable annual water budgets in 2016-2020 that could be progressively higher.

Figure 3: Breakdown of water infra allocation as % of total development expenditure (DE)

Budget	Opex (RM bn)	DE (RM bn)	DE as % of total	Water infra (RM m)	Water infra as % of DE
2011	162.8	49.2	23%	3,256	7%
2012	181.6	51.2	22%	1,400	3%
2013	201.9	49.7	20%	2,088	4%
2014	217.7	46.5	18%	1,229	3%
2015	223.4	50.5	18%	2,800	6%
2016	215.0	49.0	19%	2,235	5%

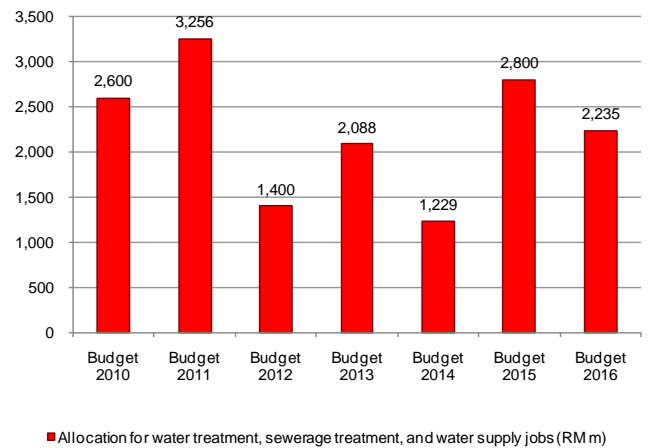
SOURCES: CIMB, BUDGET ANNOUNCEMENTS

Figure 4: Compiled value of projects under Budget 2010-2016



SOURCE: CIMB RESEARCH, BUDGET ANNOUNCEMENTS

Figure 5: Water projects' allocation for Budget 2010-2015



SOURCE: CIMB RESEARCH, BUDGET ANNOUNCEMENTS

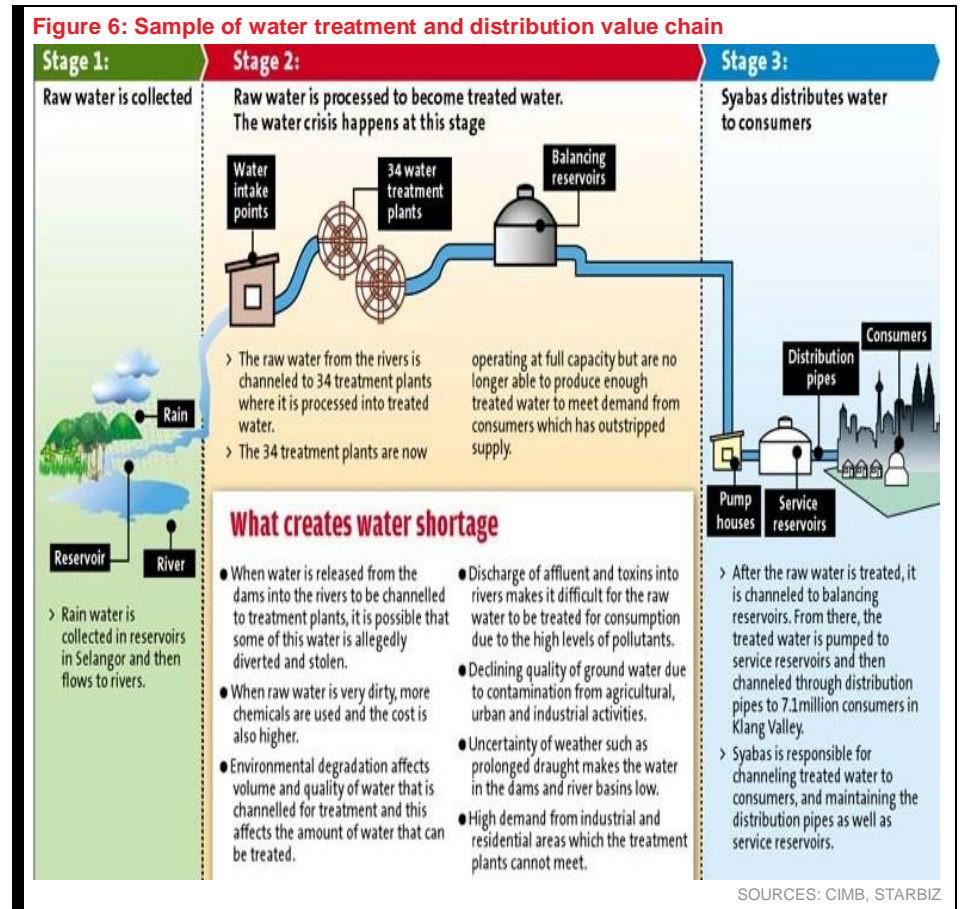
COVERS THE ENTIRE VALUE CHAIN

More needed to build and upgrade WTPs and pipes

The entire value chain of any large-scale water project includes the construction of dams, pumping stations and large-diameter feeding pipes for the upstream portion while the downstream involves the building of water treatment plants (WTPs) and distribution pipes. There could be sizeable new facility construction and upgrade projects due to the rising population and demand from industrial areas. This is especially so for the Klang Valley given the water shortage issues, especially in the state of Selangor, where the water reserve margin has fallen below 5%.

Focus in Selangor for big contracts ▶

A study conducted by Syabas estimated that a total capex of RM4.3bn would be required to improve the water supply services in Klang Valley over the next 4-5 years. A major undertaking is the construction of phase 1 of the Langat 2 WTP, which is already at c.20% physical progress and costs RM994m. The next phase is even larger, worth c.RM1bn, given the total WTP capacity of 2,500 MLD. The stalled progress of the RM8bn Pahang-Selangor interstate water transfer scheme (IWTS) could regain some traction with larger-diameter pipe supply contracts awarded to complete the network between the water transfer tunnel and Langat WTP. This will directly benefit pure larger-diameter pipe players, such as Engtex (NR) and YLI (NR). The total value of pipe orders was earlier estimated to be between RM300m and RM500m.



WATER INFRA THEME FAVOURS SMALLER PLAYERS

Comparing Gamuda, Puncak Niaga and Salcon ▶

With the exit of Puncak Niaga from the water business in Selangor, Salcon offers greater appeal in terms of its position among the contractors that could benefit from new tenders post the water consolidation in the state. Though Puncak Niaga is also a water infra contractor, its focus appears to be more in East Malaysia and less in Klang Valley at this juncture, with an estimated outstanding order book of less than RM400m. Gamuda on the other hand, is not a pure water infra play. The potential conclusion of the sale of 40%-owned Splash is its only angle in Selangor. Nevertheless, Gamuda continues to be our top big cap pick as it provides the biggest exposure to MRT and Penang TMP.

Upside from water infra wins is bigger for Salcon ▶

For Salcon, we remain positive about its prospects for securing more contracts in the medium term. Tender opportunities are also anchored by 1) state-driven sewerage treatment plants (STP) outside of Selangor, 2) private sector desalination plant contracts, 3) water treatment plants (WTP), and 4) non-

revenue water- (NRW) related jobs. The total tender book (jobs in tender) of RM1bn-2bn provides a good indication of the backlog of water capex, which should roll out beginning in 2016.

Our calculation shows that based on the historical success rate of 20-30%, Salcon could secure over RM500m worth of jobs against its current outstanding order book of RM652m, which is now good for up to three years. The order book could be bumped up by 85%.

Figure 7: Breakdown of Salcon's tender book

Type of local jobs in tender/tender book	RM m	% of total tender book	Success rate %	Potential	
				win (RM m)	Time line
Sewerage treatment plants (STP)	1,158	53%	30%	347.4	12-18 months
Desalination plant	900	41%	20%	180	12-18 months
Water treatment plants (WTP)	110	5%	20%	22	12-18 months
Non-revenue water (NRW) related	36	2%	20%	7.2	12-18 months
Total	2,204			556.6	
Current outstanding order book (Oct 2015)				652.0	
Potential enhancement to order book				85%	

SOURCES: CIMB, COMPANY REPORTS

Figure 8: Salcon's RNAV

	FY17	P/E	Stake	Value
	RM m	(x)	(%)	(RM m)
Construction net profit	16.9	15	100%	253.0
	DCF value	WACC	Stake	
	(RM m)	(%)	(%)	
10-year contract (VBT, RM4-5m revenue per telco)	91.3	7%	50.1%	45.8
Water concession in Vietnam (110 MLD) at BV	75.0		36%	27.0
Land bank	Acres	m sq ft	RM psf	Stake
Eco Mid Town - Johor	12.5	0.54	210	50%
Belfield Crest	5.35	0.23	800	70%
Cash (2Q15)				263.3
Remaining proceeds from China water assets monetisation				40.0
Borrowings (2Q15)				(97.9)
Property investments				8.4
Investment in associate & JVs				58.1
Net current asset less property dev. cost				279.1
RNAV				1,064.5
No. of shares (m)				672.6
RNAV/share (RM)				1.58
RNAV discount (%)				40%
Target price (RM)				0.95

SOURCES: CIMB, COMPANY REPORTS

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1528 companies under coverage for quarter ended on 30 September 2015		
	Rating Distribution (%)	Investment Banking clients (%)
Add	58.1%	6.0%
Hold	30.4%	3.5%
Reduce	10.9%	1.0%

Corporate Governance Report of Thai Listed Companies (CGR). CG Rating by the Thai Institute of Directors Association (Thai IOD) in 2015.

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The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

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- Neutral** A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
- Underweight** An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

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Definition:

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