

CONSTRUCTION

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PETALING JAYA: The construction sector, which is off to a strong start this year, has been buoyed primarily by domestic project flows.

However, analysts warned that sector stocks might be exposed to some profit taking and rotational play.

The FTSE Construction Index is up nearly 37% year-on-year at 222 points and is at its highest since July 2019, despite corporate results in the final quarter of 2023 (4Q23) being mixed.

RHB Research noted that out of the 11 companies under its coverage that reported results between February and March (mostly for the financial year ending December), four were in line, two exceeded expectations and five missed.

However, that did not seem to matter to investors as 1Q24 domestic contract awards rose 45% quarter-on-quarter to RM6.96bil.

The contracts were predominantly led by the private sector, which experienced robust flows primarily driven by commercial and residential projects.

"The private-sector construction market is expected to remain vibrant, supported by substantial investments in new semiconductor foundries and data centres," said Nixon Wong, chief investment officer at Tradeview Capital.

More big awards are on the way for the industry.

The noteworthy contracts to be awarded include major infrastructure projects such as the Penang LRT (valued at over RM10bil), Pan Borneo Sabah Phase 1B (RM15.7bil), flood mitigation packages worth RM11.8bil, Sabah-Sarawak Link Road (RM7.4bil), LRT3 reinstatement (RM4.7bil), KUTS-Green Line developments, and various water scheme projects.

RHB Research noted the much awaited multi-billion-ringgit Mass Rapid Transit (MRT) 3 project is envisaged to roll out after 4Q24 as MRT Corp is expected to finalise the land to be acquired in 3Q24.

Builders to benefit from domestic project rollouts

Robust launches of commercial and residential jobs

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Nixon Wong

With a multiplier effect of two times in the economy, Wong said these initiatives are anticipated to drive job creation and activity levels higher throughout this year.

"Increased property and construction activities will primarily drive demand for building materials like cement and steel, resulting in heightened production and sales for manufacturers, distributors and retailers in the building materials sector.

"Additionally, this growth positively influences the financial sector by increasing lending for property and construction projects, leading to higher loan volumes and interest income for banks and financial institutions," he said.

Wong, however, warned the strong performance of the sector has resulted in stretched valuations now at an average price earnings multiple of 14 times (10-year mean of 12.7 times).

This situation may prompt some investors to take profit and lead to a correction in the near term, especially if there's a rotation of investments across sectors, according to Wong.

"The sector's robust performance was primarily driven by domestic project flows and this characteristic makes it less likely to be significantly impacted by external factors such as the US Federal Reserve's move on interest rates.

"Domestic project flows tend to have their own momentum and are often influenced by factors such as government policies, economic conditions and local demand dynamics," Wong added.

Kevin Khaw, senior research analyst at iFAST Capital said the risk-on sentiment for infrastructure across the southern region has boosted the property and construction sector in 2024.

"Apart from that, we witnessed heightened foreign interest in emerging coun-

tries like Malaysia, as they are switching their focus to growth-oriented plays.

"The higher participation rate from domestic institutional and retail players has supported the rally in the sector as well," he said.

Like Wong, Khaw has turned cautious as sector valuation has hit above plus one standard deviation, a level not seen in the past decade.

"We maintain a positive view towards the infrastructure play to boost its earnings soon, yet we think the current price has reflected the forward earnings," he pointed out.

With catalysts in store for the sector, RHB Research, however, viewed the current valuation of the index as still having some room to exhibit an uptrend.

"The presence of sizable industrial jobs such as data centres and flood mitigation projects, which were absent back in 2017, may possibly even push the index higher than before," the research firm noted in its strategy report.

It noted that while major infrastructure projects signalled by the government have yet to be rolled out, the rise in value of construction work done for civil engineering could likely be underpinned by the ramping-up of works by contractors on existing projects amid better labour supply and operating conditions.

The research house remained "overweight" on the sector with top picks being Gamuda Bhd, Sunway Construction Group Bhd and Kerjaya Prospek Group Bhd due to their healthy order books and financial positions.