Malaysia Strategy

Budget 2024: Reform in progress

MALAYSIA | STRATEGY

- The expansionary Budget 2024 saw a record high RM394bn allocation
- Higher development expenditure with the reinstatement of five LRT stations was a pleasant surprise. Bigger cash assistance was extended to cushion the higher cost of living
- Overweight on the Construction, EMS and O&G sectors. Top picks include Gamuda, Kerjaya Prospek, NationGate and Dayang

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Focus on fiscal discipline and sustainability

Budget 2024 is unlikely to excite the market due to the absence of significant goodies for the Rakyat. The T20 group may feel the negative impact on some new taxes, while the savings are expected to channelled to support the B40 group. However, Budget 2024 outlined some important strategies aimed at addressing the structural issues in Malaysia's economy, particularly in strengthening fiscal discipline and sustainability. In line with its vision under the Madani Framework, the Budget 2024 highlighted the adoption of targeted fuel subsidies from next year onwards that would enable a more effective fiscal spending in providing social safety net. On the other hand, the introduction of new taxes and the raising of current taxes to widen the tax base may further enhance fiscal sustainability. Despite the waning of political risks in the recent months providing some confidence to the Government in executing the structural reforms, Budget 2024 is relatively conservative in its new policies, such as exclusion of RON95 from the targeted fuel subsidy regime and the absence of an announcement on GST reintroduction. Overall, we believe the Budget 2024 would mark a positive step for the Government in setting the right direction to drive the economy and strengthen the country's economic foundation.

Revival of LRT 3; possible Penang LRT and MRT 3 contract delays

The 8% net increase in development expenditure for 2024 is positive for the construction sector, reaffirming our Overweight view. The reinstatement of five LRT3 stations was a pleasant surprise. The Penang LRT under Public-Private Partnership (PPP) model may delay contract rollouts to the later part of 2024. The property sector should benefit from the relaxation of Malaysia My Second Home (MM2H) application conditions with the announced measures also auguring well with the affordable housing segment.

Bigger cash assistance handed out

The increased sugar tax, introduction of 5–10% luxury goods tax and elimination of price controls for poultry and eggs were among the key highlights in the consumer sector. The stricter curbs on cigarette and liquor smuggling activities is beneficial. The food & beverage and telecommunication services were both spared from the hike in services tax rate (from 6% to 8%). Also, the absence of new gaming and sin taxes should provide a sense of relief.

Maintain Neutral on market – O/W: Construction, EMS and O&G

The 10% capital gains tax for the disposal of unlisted shares can be waived by way of IPOs, which could help stimulate the capital market. While KLCI has been trading at -1SD below its historical mean, we see limited catalysts for the market. The recent conclusion of state elections has partly relieved some market concerns, but focus will remain on potential risks associated with a global economic slowdown, looming US recession, and higher-for-longer US interest rate environment. We are Overweight on sectors such as **Construction** (**Gamuda**, **Kerjaya Prospek**– higher allocation spillover), **EMS** (**NationGate**– trade diversion beneficiary backed by structural growth themes) and **O&G** (**Dayang**– Petronas lower dividend commitment supportive of higher capex spending and activities).

Current KLCI: 1,444.14

Market valuation and growth

	FBMKLCI		FBMSC	
	'23E	'24E	'22	'23E
P/E (x)	14.4	13.0	11.9	12.8
EPS Growth (%)	7.5	10.4	NA	14.1

Source: Bloomberg
**No available 2024E data on FBMSC*

Coverage BUY calls

Name	Price (RM)	TP (RM)	Upside (%)
NationGate	1.23	1.80	46.3
Dayang	1.87	2.30	23.0
Sky World	0.58	0.89	53.4
Kerjaya	1.40	1.72	22.9
Lagenda	1.26	1.55	23.0
Gamuda	4.60	5.01	8.9

Source: Bloomberg, Phillip Research
**Share prices as of 13 Oct 2023*

Table 1: Summary of sector implications

Sector	Implication	Comments
Automotive	Neutral	No new measure to drive TIV sales. Ongoing efforts in building more charging stations
Consumer	Neutral	Higher cost of living as a result of price ceiling removal on poultry and eggs, revised higher sugar tax negate the effect of bigger cash assistance. No new sin tax being introduced
Construction	Neutral	Revival of 5 LRT 3 stations. MRT 3 not mentioned (off balance sheet). Penang LRT to be funded under the PPP model
EMS	Positive	The EMS sector may benefit from tiered reinvestment tax incentive
Financial	Neutral	Potential increase in capital market listing interest to bypass the capital gains tax
Gaming	Positive	No changes in existing gaming tax. Gradual return of international tourists likely to boost visitations
Healthcare	Positive	MOH budget (largest allocation) increasing by 14% yoy in 2024 is expected to benefit public healthcare sector. Acquisition of medical equipment might benefit listed companies
Oil and Gas	Positive	Reduced Petronas dividend commitment supportive of higher capex spending leading to increased activities within the sector
Plantation	Neutral	The higher emphasis on automation will lower foreign labours dependency and leading to reduced operating costs and increased efficiency
Property	Neutral	The negative from introduction of 4% flat stamp duty might be offset by relaxation of MM2H application process
Solar	Positive	Numerous incentives provided to achieve goal outlined in NETR
Technology	Positive	Continued tax allowance and loans spur investments within the sector

Source: Phillip Research

Budget 2024 impact on sectors

Automotive: Building more EV charging stations

Measures

- RM170m investments from Tenaga, Gentari and Tesla Malaysia to install 180 EV charging stations
- Introduction of Electric Motorcycle Usage Incentive Scheme with rebates up to RM2,400 for individuals with annual income of RM120,000 or below
- 4-years extension of income tax relief up to RM2,500 on EV charging equipment
- 2-years extension of tax deductions for EV rental costs

Sector implications

The continued EV incentives introduced is in line with government's ambition to build 10,000 charging stations by 2050 and solidifies its commitment in developing the nation's EV charging infrastructure. While this is long-term positive, we believe this would have a minimal impact on overall TIV sales on heighten competitive landscape. Possible beneficiaries from EV initiative include **Tenaga** and **Yinson** (non-rated).

Consumer: Removal of poultry/egg price ceiling, raising sugar tax and introduction of luxury good tax

Measures

- Proposed tighter import control for cigarettes; to be carried out on a full container load
- Transshipment activities for liquor will be limited to certain ports
- Imposing 5–10% tax on high-value items such as jewelry and watches based on item price threshold value
- Increasing cash assistance by 25% to RM10bn (from RM8bn) through Rahmah Cash Donation, benefiting 10m recipients
- Imposing excise duty on chewing tobacco products at 5% and RM27/kg
- Increasing excise duty for sugary drinks from RM0.40/litre to RM0.50/litre
- Proposed removal of subsidy and price ceiling on poultry and eggs

Sector implications

The higher cash assistance will lighten the burden of the B40 income group. However, the announced removal of the price ceiling on poultry and eggs and sugar tax hike may increase near-term cost of living. Companies such as **Nestle**, **Power Root** and **F&N** (non-rated) may end up passing on the higher costs to consumers, or alternatively, tweaking the formula by reducing its sugar content. Meanwhile, the 5–10% luxury goods tax may impact **Bonia** (non-rated). The tighter control curb on cigarette and liquor smuggling activities is viewed positive for companies such as **BAT**, **Carlsberg** and **Heineken** (non-rated).

Construction and Infrastructure (Overweight): Revival of five LRT stations

Measures

- Development expenditure allocation is 8% higher yoy at RM90bn in 2024 (excluding RM13.3bn of 1MDB bond redemption in 2023 DE)
- Allocation of RM11.8bn for 33 high-priority flood mitigation projects
- Allocation of RM2.8bn for federal roads and bridges repairs
- Tender process for 19 work packages with a total contract value of RM15.7bn from Pan Borneo Sabah Phase 1b is expected to be finalized by November 2023
- Sabah-Sarawak Link Road (SSLR) Phase 2 with an estimated cost of RM7.4bn is expected to commence by the end of this year
- RM2.4bn for the construction and maintenance of government quarters
- The construction of five LRT3 stations is expected to resume with an estimated cost of RM4.7bn
- Penang LRT is expected to cost RM10bn under a public-private partnership (PPP) approach

Sector implications

The higher RM90bn infrastructure spending (excluding debt repayment) in 2024 aligns with our expectations and is positive for the construction sector. Notable projects including the Pan Borneo Highway, SSLR, Penang LRT and LRT3 have received substantial allocations in the Budget 2024. There was a lack of mention on MRT 3 due to off balance sheet funding by Danainfra Nasional.

The revival of the LRT3 stations (estimated RM4.7bn value) that were previously shelved came as a positive surprise and could see turnkey contractor, **MRCB** (non-rated) benefiting. We believe subcontractors such as **SunCon** **(SCGB MK, HOLD; TP: RM2.06)** may likely be appointed to undertake additional works due to its previous track record in the LRT 3 Package GS07&08.

The Penang LRT under the PPP model instead of being fully funded by the federal government came as a surprise as this may lead to an longer funding timeframe and contract rollout delays, in our view. Potential key beneficiaries are **Gamuda** and **SunCon**. For the Pan Borneo project, **Gamuda's** strong track record in executing the WPC-04 work package makes it a formidable contender.

The flood mitigation, road maintenance and the repair and upgrading of government buildings and schools are likely to benefit relatively smaller-sized contractors, primarily due to lower project margins.

Recommendations

We have an **OVERWEIGHT** call on the construction sector with our top pick being **Gamuda** **(GAM MK, BUY; TP: RM5.01)** and **Kerjaya Prospek** **(KPG MK, BUY; TP: RM1.72)** due to their robust balance sheet strength and consistency in securing orderbook replenishments from respective construction subsectors of infrastructure and building construction.

Electronic Manufacturing Services (Overweight): Further incentives to grow

Measures

- Plan to provide tiered reinvestment tax incentive in the form of tax allowance ranging between 70–100%

Sector implications

The proposed tax allowance could entice global MNCs to invest in Malaysia, partly encouraged by the US–China trade tension. We reaffirm our positive view that the EMS sector will continue to benefit from the supply chain relocation as more MNCs choose to shift their manufacturing hubs out from China into Malaysia, benefiting contract manufacturers within the region.

Recommendations

We have an **OVERWEIGHT** call on the EMS sector. Our top pick is **NationGate** **(NATGATE MK, BUY; TP: RM1.80)** being a prime beneficiary of ongoing trade diversification and as it is strategically positioned into the secular growth trends such as artificial intelligence, data centres, and EV.

Financials: Potential higher listing interest to bypass Capital Gains Tax

Measures

- Imposing 10% Capital Gains Tax for the disposal of unlisted shares effective 1 March 2024; but exemptions will be considered for activities including IPOs, internal restructuring and venture capitals
- Income tax exemption on income arising from Islamic Securities Selling and Buying (ISSB) and shariah-based securities borrowing and lending (SBL)
- Full income tax exemption to Labuan entity carrying out Islamic financing trading activities for 5 years

Sector implications

The exemption of Capital Gains Tax through IPOs, rather than the sale of unlisted shares may attract greater capital market listing interest and in turn stimulate the sluggish capital market. The income tax exemption on ISSB and SBL aims to boost the securities trading volume and liquidity.

Healthcare: Higher budget allocation to benefit the sector

Measures

- The Malaysian Ministry of Health allocated higher RM41.2bn allocation, from RM36.3bn in 2023, of which RM5.5bn is designated for the acquisition of medicines, material consumables, reagents and vaccines
- Allocation of RM1.3bn for new projects including construction of hospitals and clinics
- Allocation of RM1.2bn for clinics renovation, medical apparatus procurement, digital medical records dissemination across clinics
- Allocation of RM130m to enhance efforts in disease prevention
- Allocation of RM100m for broadening MADANI Medical Scheme and extension of mySalam scheme for an additional 2 years

Sector implications

Companies involved in the supply of medical equipment, pharmaceuticals, and digital healthcare solutions may potentially see an increase in business engagements with public healthcare institutions. The focus on digitalisation and modernisation of healthcare services might open up avenues for collaborations or partnerships between the government and private healthcare companies. Measures are mostly centered around public healthcare, as such little impact to private healthcare service provider. Potential beneficiaries may include medical equipment providers such as **UMedic** and **LKL** (non-rated).

Oil and Gas (Overweight): More room for capex spending on lower Petronas dividend payout

Measures

- Diesel subsidy will be introduced in phases
- Special tax rate or investment tax allowance to be provided for the development of Pengerang Integrated Petroleum Complex (PIPC)
- Lower Petronas dividend payout of RM32bn in 2024 (2023: RM40bn)

Sector implications

Budget 2024 highlighted the gradual phasing out of the diesel subsidy, although no details have been outlined in terms of actual implementation. Additional tax incentives are being introduced to support developments within PIPC and to attract FDI. We see this as a positive move to attract more investments into PIPC as a chemical and petrochemical hub. Prime Minister Anwar Ibrahim in March 2023 secured RM80bn investments from Rongsheng Petrochemical, China's largest petrochemical company.

Recommendations

Petronas' reduced dividend payout to the Government may lead to increased capital spending and spur activities within the sector. We have an **OVERWEIGHT** call on the O&G sector with our top pick being **Dayang** **(DEHB MK, BUY; TP: RM2.30)** for its prominent position as a market leader in the offshore upstream maintenance segment and solid RM1.2bn orderbook providing earnings visibility until end-24.

Plantation: More assistance for smallholders

Measures

- Allocation of RM2.4bn to FELDA, FELCRA, and RISDA to boost agri-commodity activities and increase socio-economic of smallholders
- Allocation of RM100m as part of the palm replanting program incentives, being extended to 7,000 small private oil palm farmers
- Allocation of RM70m for increasing sustainability of oil palm industry and intensifying anti palm old campaign
- Allocation of RM90m to RISDA and FELCRA to optimize use of farmland
- Automation tax incentives will be enhanced to elevate productivity and scale down the dependency on foreign labour
- Allocation of RM400m to further raise the activation price level of Rubber Production Incentive (IPG) from RM2.70/kg to RM3.0/kg

Sector implications

The aid allocated benefits the FELDA, FELCRA, RISDA and smallholders. The tax incentives provided for automation are expected to have a positive impact by reducing dependence on foreign labour, resulting in lower operating costs and better efficiency. The replanting incentives may not directly benefit the listed Plantation companies but broadly the sector should see increased productivity from the gradual implementation of automation.

Property (Neutral): Higher stamp duty but MM2H requirement relaxed

Measures

- Increasing Housing Credit Guarantee Scheme (SJKP) to RM10bn (Budget 2023: RM5bn)
- Imposing 4% flat rate stamp duty on property transfer documents by non-citizens and foreign firms
- Relaxing requirements for Malaysia My Second Home (MM2H) applications
- Threshold residents' consent to en-bloc sales will be reduced from 100% to a level consistent with international practice such as Singapore (c.80-90%)

Sector implications

The relaxation of eligibility criteria for MM2H programme is expected to attracts foreign investors looking to relocate to Malaysia. However, the introduction of flat 4% stamp duty may increase cost from RM24,000 to RM40,000, assuming RM1m property value which is the minimum threshold value for foreigner.

Recommendations

We remain NEUTRAL as we believe announced measures have minimal impact on the sector. Further details on MM2H conditions need to be outlined. We believe affordable house developer like Lagenda Properties **(LAGENDA MK; BUY; TP: RM1.55)** is likely to benefit.

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Solar: More investments to spur the sector

Measures

- Established the National Energy Transition Easy Fund with a total value of RM2bn to support the implementation of NETR
- Developing a solar buy-back program for rooftop installations with minimal impact on system costs
- Urges companies to offer a 'Zero Capital Cost' subscription model for solar panels installation on residential homes
- Encouraging more companies to participate in voluntary carbon markets. The government proposes additional tax deductions of up to RM300,000 for companies making expenditures on Measurement, Reporting, and Verification (MRV) related to carbon projects
- Exploring avenues to implement the Third-Party Access model to drive investments in renewable energy (ie: Corporate Green Power Program)
- Financial institutions to provide financing of RM200bn to support industries to reduce carbon emission

Sector implications

The announced tax incentives are positive for the renewable energy (RE) sector. This is also part of the NETR roadmap and to achieve the 70% renewable energy target by 2050. We expect the rollout of more RE projects to benefit solar engineering, procurement, construction and commissioning (EPCC) players such as **Solarvest**, **Sunview** and **Samaiden** (non-rated).

Technology: Boosting R&D and innovation

Measures

- Plan to provide tiered reinvestment tax incentive in the form of tax allowance ranging between 70–100%
- Development of high-tech industrial area in Kerian, North Perak to broaden the E&E cluster
- Allocation for technology development in various sectors, including RM10m for E&E, aerospace, drone and robotics technology
- Allocation of RM900m to encourage SMEs to enhance productivity via automation and digitalization
- Acceleration of capital allowance claims for ICT equipment and software from 4 years to 3 years

Sector implications

Various tax incentives continue to be provided to promote R&D and innovation, which is positive. Allocation to promote TVET education were also seen to address the shortage of skilled workers. The relaxation of capital allowance and provision of loans helps companies, especially SMEs to embrace technological advancement. This comprehensive approach aims to strengthen the sector's global competitiveness while facilitating both foreign and domestic investments. Potential beneficiaries include **Vitrox**, **Pentamaster**, **UWC**, **Greatec** (non-rated).

Table 2: Coverage List

Ticker	Stock	Rating	Price (RM)	TP (RM)	Mkt Cap (RM m)	Core PE (x) 2023E	Core PE (x) 2024E	Core EPS Growth (%) 2023E	Core EPS Growth (%) 2024E	P/BV 2023E	P/BV 2024E	Div. Yield (%) 2023E	Div. Yield (%) 2024E	ROE (%) 2023E	ROE (%) 2024E
NATGATE MK EQUITY	NATIONGATE	BUY	1.23	1.80	2,550.9	40.5	18.5	(26.6)	119.3	4.5	3.8	0.6	1.4	19.8	28.3
DEHB MK EQUITY	DAYANG ENTERPRISE	BUY	1.87	2.30	2,165.0	13.0	10.6	46.9	23.2	1.4	1.3	2.4	2.9	11.1	12.6
SKYWLD MK EQUITY	SKYWORLD DEVELOPMENT	BUY	0.58	0.89	580.0	4.5	5.4	(5.9)	(16.6)	0.9	0.7	5.2	4.2	29.9	19.2
KPG MK EQUITY	KERJAYA PROSPEK	BUY	1.40	1.72	1,765.5	11.6	9.3	31.0	25.4	1.5	1.3	4.3	4.3	13.1	15.2
LAGENDA MK EQUITY	LAGENDA PROPERTIES	BUY	1.26	1.55	1,055.0	5.7	4.6	3.7	22.9	0.9	0.8	4.4	5.4	16.9	18.1
GAM MK EQUITY	GAMUDA	BUY	4.60	5.01	12,405.3	13.6	11.1	4.9	22.2	1.2	1.1	10.9	2.6	8.7	10.4
SCGB MK EQUITY	SUNWAY CONSTRUCTION	HOLD	1.92	2.06	2,475.6	18.2	14.9	(5.2)	21.8	3.1	2.8	2.9	2.9	17.7	19.5
					22,997.4										

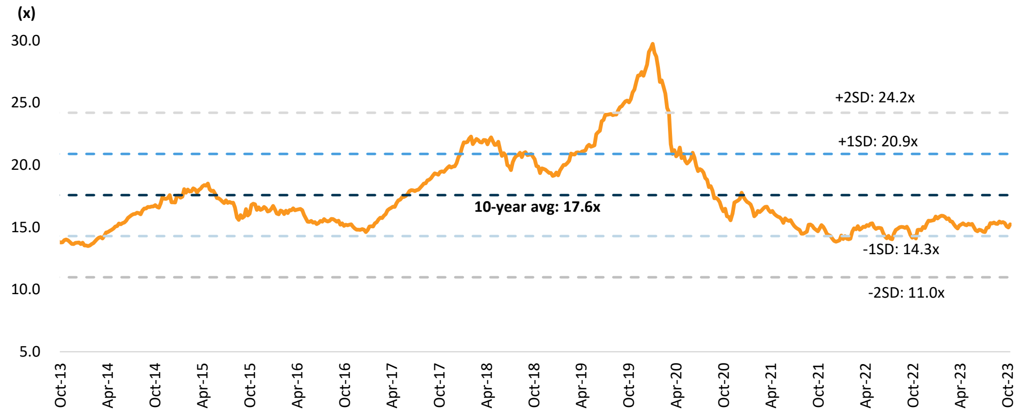
Source: Bloomberg, Phillip Research forecasts

Table 3: Top Picks Commentaries

Company	Comments
NationGate (BUY; TP: RM1.80)	NationGate, an industrial Electronic Manufacturing Service (EMS) service provider based in Penang, is expected to benefit from the ongoing US-China trade diversion as more MNCs shift out their manufacturing operations out from China. Inquiries from potential new customers, in particular the data centre space have been rising. NationGate is aggressively expanding floorspace (+53% by end23 and estimate another +30% by end24) to cater for high incoming customer demand.
Dayang Enterprise (BUY; TP: RM2.30)	We like Dayang for its prominent position as a market leader in the offshore upstream maintenance segment and solid orderbook of RM1.2bn, providing earnings visibility until end-24. Dayang stands to benefit greatly from the increase in domestic offshore activities, hastened by Petronas as it seeks to capitalize on high global oil prices. Key re-rating catalyst for potential greater upside includes securing Petronas' 5-year contract renewal for iHUC, MCM and ABC packages.
Gamuda (BUY; TP: RM5.01)	Gamuda is well-positioned to secure several new wins in Malaysia's upcoming infrastructure rollouts such as MRT3 (RM45bn) and Penang LRT (RM10bn). The group has also recently acquired a new construction arm (Downer's Transport Projects), which would allow Gamuda to tender for several upcoming mega projects in Australia with an estimated RM46bn package size. Gamuda is our sector top pick as we believe prospects will remain bright in the long term, driven by its strong regional presence in both the construction and property segment.
Kerjaya Prospek (BUY; TP: RM1.72)	Kerjaya Prospek is one of the leading contractors for high-rise buildings in Malaysia. We like it for its consistency in securing high-rise construction contracts from strong clientele and related parties such as Gamuda, UEM Sunrise and Eastern & Oriental. The group has also been consistent in delivering above average PAT margin of 10-13%.

Source: Phillip Research

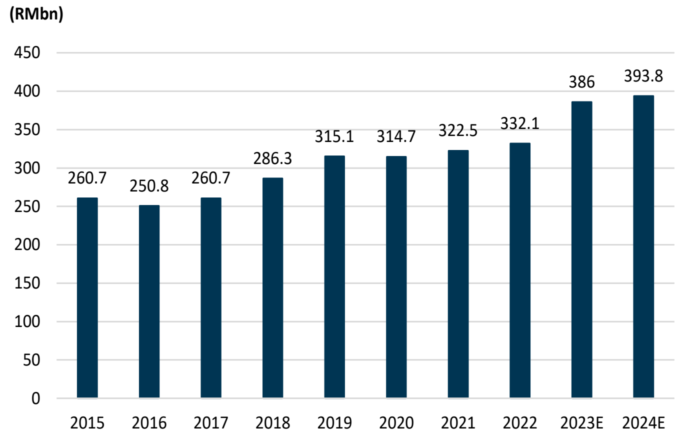
Table 4: KLCI forward PE



Source: Bloomberg, Phillip Research

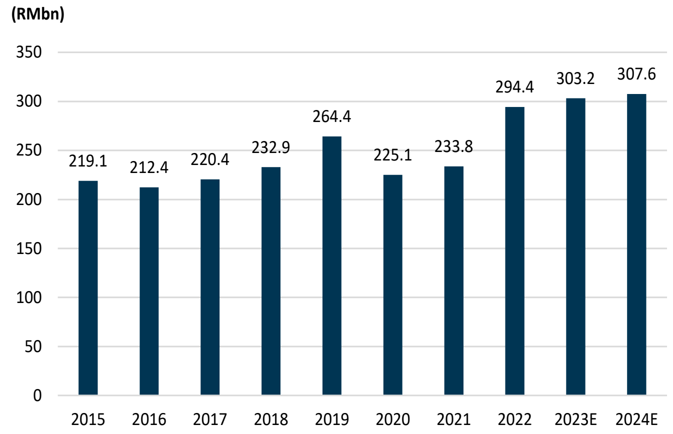
Appendix

Table 5: Budget allocation



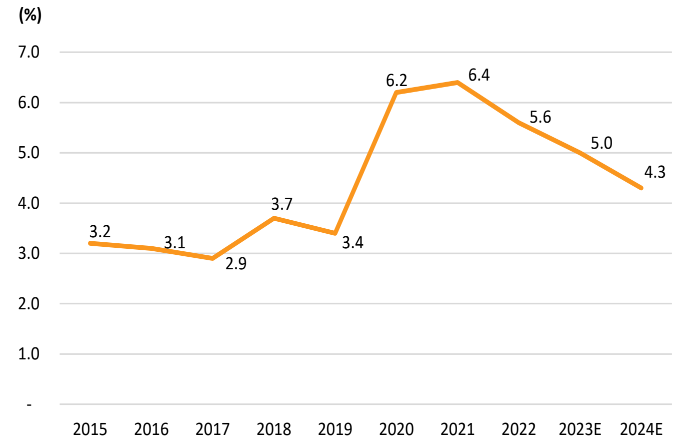
Source: MOF

Table 6: Government revenue



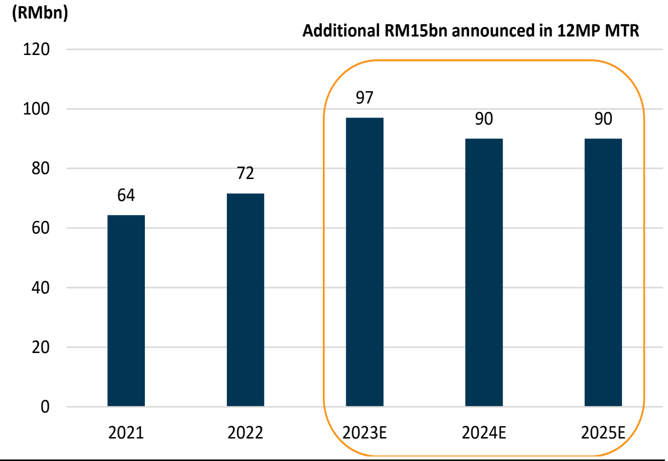
Source: MOF

Table 7: Fiscal deficit position (% of GDP)



Source: MOF

Table 8: Development expenditure



Source: MOF

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