HLIB Research
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Economics & Strategy

The second wave

While Malaysia is experiencing a second Covid wave, this seems less widespread (86% of cases from Kedah and Sabah). Consequently, a nationwide MCO is unlikely, but a targeted approach instead. Hotspot states Kedah and Sabah account for 9% of Malaysia's GDP. Cases in KV seem under control but a spike would be dire as it makes up 41% of GDP. Rising domestic cases are negative for those related to the consumer's basket (aviation, retail, F&B, gaming, hospitals, malls and hotels) but positive for telco and courier. The second wave could be a key market headwind in 4Q, but shouldn't see the same panic selling experienced during the first wave. Maintain KLCI target at 1,580.

Economic snapshot – Malaysia

	2018	2019	2020F
Real GDP (% YoY)	4.7	4.3	-5.0
CPI (% YoY)	1.0	0.7	-0.5
CA (RM bn)	33.5	49.7	30.0
OPR (% year-end)	3.25	3.00	1.75
MYR/USD (average)	4.04	4.14	4.23-4.28

FBMKLCI Target:	**1,580**
Current Level:	**1,519**

FBMKLCI

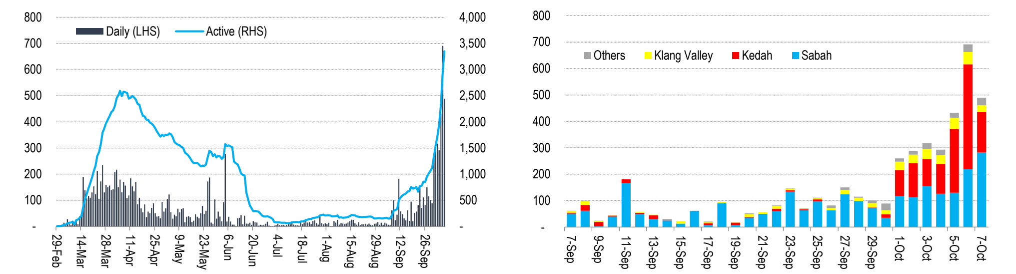
Top Picks

Stock	Rating	Price	Target
TOPGLOVE	BUY	8.80	13.00
TENAGA	BUY	10.26	12.50
TM	BUY	4.13	5.22
BURSA	BUY	8.37	11.85
SUNWAY	BUY	1.40	1.95
IJM	BUY	1.40	1.66
ARMADA	BUY	0.25	0.60
MBM	BUY	3.01	5.00
MQREIT	BUY	0.80	0.92
LIIHEN	BUY	3.28	4.08
PECCA	BUY	1.47	1.75
FOCUSP	BUY	0.49	0.88

Resurgence but… While Malaysia successfully flattened the first wave of Covid since June, an unfortunate resurgence occurred from early Sept. New daily Covid cases have consecutively chalked in triple digits since Oct (highest on 6 Oct: 691). Consequently, the number of active cases has surged to 3.35k (7 Oct), surpassing the previous high during the first wave (5 Apr: 2.6k).

…less widespread. Despite new daily cases in this second wave being higher, they seem less widespread vs the first. Of the 4.6k cases recorded from the second wave (i.e. 7 Sept to 7 Oct), the majority were from Sabah (56%; started from illegal foreigners and exacerbated by the state elections) and Kedah (30%; prison cluster). While numbers in the Klang Valley (i.e. Selangor + KL) still seem under control (9% of total second wave cases), cracks are starting to show with cases slowly creeping up from mid-teens in end-Sept to 30-40s in Oct.

Figure #1 LHS: Daily new Covid cases in M'sia, RHS: Breakdown by state



MOH *MOH*

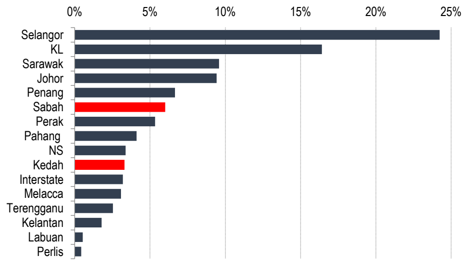
Nationwide lockdown the last resort. As mentioned in our 4Q20 Outlook report (2 Oct), we believe that another nationwide lockdown will only be an act of last resort. This was reaffirmed during the PM's recent 6 Oct address, who reassured that lockdowns will only be targeted to high risk areas. We believe the opportunity cost of a 2nd nationwide MCO will be greater as: (i) the economy is still recovering from the wounds of first lockdown and (ii) current cumulative death rate is stable at 1.3%, much lower than the peak of 9.7% in late Mar (see Appendix). Furthermore, as elaborated above, 85.9% of the second wave cases are from Sabah and Kedah, rather than widespread throughout the nation. With much better contact tracing now (>60% adoption rate of MySejahtera app) compared to the first wave, this allows for a less economically disruptive way to control the pandemic's spread vs a lockdown.

Economic implications from targeted lockdowns. The targeted lockdowns that have been enacted thus far were mostly in the hotspots of Kedah and Sabah (Figure #2). These states had a respective contribution of 3.3% and 6% towards Malaysia's GDP in 2019. We estimate that the affected districts in Kedah account for 43% of the state's population, while for Sabah it stands at 66%. Of greater concern would be if Klang Valley's cases spike and prompt more targeted lockdowns there; the region is the largest contributor to Malaysia's GDP at 40.6% (Selangor: 24.2%, KL: 16.4%).

Effective today, several areas in the Klang district have been placed under CMCO; the district is estimated to make up 12.4% of Klang Valley's population. On a broader basis, the targeted lockdowns will also have indirect ramifications to non-impacted areas as people spend more time at home to reduce contagion risk and business may have to operate at sub-optimal capacity to ensure social distancing SOPs are adhered to. While 2H20 GDP is expected to stage a recovery, we project it will still remain in negative territory YoY (2H20f: -1.7% vs 1H20: -8.2%); maintain 2020f GDP at -5.0%.

Figure #2 LHS: Lockdown areas announced (as of 7 Oct); RHS: GDP contribution by state

Area	State	Lockdown	Start	End
Kenanga	Kedah	TEMCO	28-Aug	13-Sep
Mawar	Kedah	TEMCO	28-Aug	13-Sep
Melur	Kedah	TEMCO	28-Aug	27-Sep
Kota Setar	Kedah	EMCO	11-Sep	25-Sep
Lahad Datu	Sabah	TEMCO	29-Sep	12-Oct
Tawau	Sabah	TEMCO	29-Sep	12-Oct
Kunak	Sabah	TEMCO	29-Sep	12-Oct
Semporna	Sabah	TEMCO	29-Sep	12-Oct
Alor Setar Prison	Kedah	TEMCO	6-Oct	20-Oct
Kota Kinabalu	Sabah	CMCO	7-Oct	tbd
Penampang	Sabah	CMCO	7-Oct	tbd
Putatan	Sabah	CMCO	7-Oct	tbd
Sandakan	Sabah	CMCO	9-Oct	tbd
Papar	Sabah	CMCO	9-Oct	tbd
Tuaran	Sabah	CMCO	9-Oct	tbd
Klang	Selangor	CMCO	9-Oct	tbd



Various news articles *DOSM*

Sectorial impact. Needless to say, the sectorial impact from rising Covid cases in Malaysia is mostly negative (see Appendix). Key negatives largely stem from those sectors that are affiliated to the consumer's basket: aviation (travel aversion), consumer retail (lower footfall to outlets), breweries (less drinking out), gaming (less visitors to RWG; NFOs may see slight dip in ticket sales), healthcare (non-critical treatments deferred) and REITs (lower footfall for malls and check-ins for hotels). We reckon there will be some positives for telco (higher data demand as more stay at home) and logistics (more courier services as online shopping increases). While rising domestic cases may seem positive for gloves too, we reckon the global count is more relevant as Malaysia accounts for <5% of their sales.

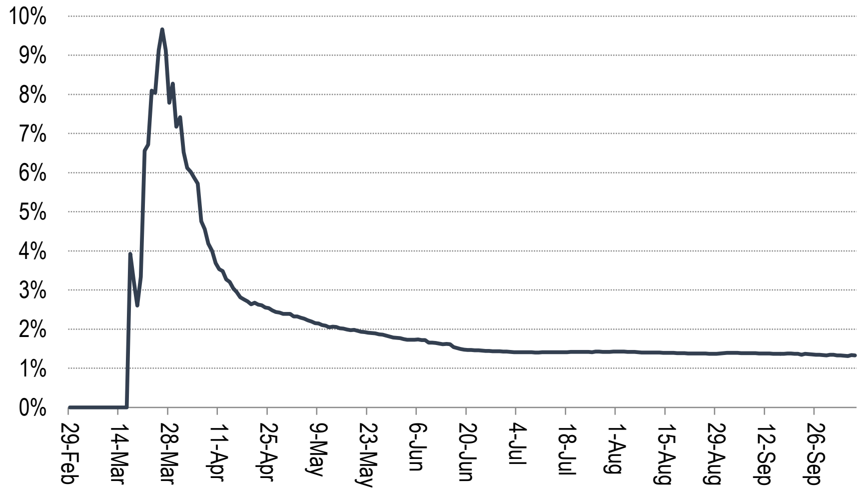
Those with Kedah, Sabah and Klang exposure include:

- **MAHB (SELL, TP: RM4.15):** Kedah and Sabah accounted for 21.2% of domestic passengers in FY19.
- **WCT (HOLD, TP: RM0.44):** Its Première Hotel is in BBT Klang.
- **BToto (HOLD, TP: RM2.20):** From their website, it has 31 outlets in Klang (affected outlets tbd). In Sabah, 6 of its outlets are in the TEMCO districts and 9 in CMCO districts. It has a total of 680 NFO outlets in Malaysia.
- **Top Glove (BUY, TP: RM13.00)** and **Kossan (BUY, TP: RM18.30):** Their main plants in Klang should not be affected as gloves are deemed "essentials".
- **KPJ (BUY, TP: RM1.00):** Kedah Medical Centre had to close for 3 days as some of its staff tested positive. KPJ Klang to continue operations as an "essential".
- **Westports (BUY, TP: RM3.98):** BAU for its port ops as deemed "essentials".
- **Construction:** Possible delays for WTP jobs in Kedah and Pan Borneo Sabah.
- **Plantation:** CPO output from Sabah makes up 24% of Malaysia's total output YTD; minimal impact as deemed "essential".

Maintain KLCI target at 1,580. The rising domestic Covid count may pose as a key market headwind in 4Q. However (barring another nationwide MCO), the same magnitude of panic selling seen in Feb-Mar during the first wave is unlikely as (i) cases are less widespread now, (ii) short selling is banned, (iii) asymmetric upper and lower limits for KLCI constituents and (iv) temporary relief measures relating to margin financing has been extended to 31 Dec 2020. Maintain 12M KLCI target at 1,580 based on 17.7x P/E (5Y mean) tagged to CY21 EPS.

Appendix

Figure #3 Cumulative Covid mortality rate in Malaysia



Worldometers, HLIB estimates

Figure #4 Sectorial impact from rising Covid-19 cases in Malaysia

Stock	Impact	Comments
Aviation	Negative	As it is, the aviation sector is already facing a significant shrinkage to mostly domestic travel only (as international boarders remain closed). What's left of this smaller pie will be negatively impacted too with the rising domestic cases causing travel aversion.
Banks	Negative	Slower economic activities would affect repayment capability of borrowers, which consequently, poses further asset quality risks. As such, the sector may need more provisioning buffers and cause earnings recovery to turn U- or W-shape (from current V-shape projection)
Construction	Negative	Potential earnings downside if stricter SOPs are adopted and positive cases are found at work sites. Jobs flow would suffer given the uncertainty and redirection of resources. Current TEMCO in Sabah and Kedah will slow down progress for Pan Borneo Sabah and WTPs in Kedah. Edgenta's consultancy segment would also be affected due the slow progress for Pan Borneo Sabah.
Consumer	Negative	Retail players will be impacted from reduced foot traffic in shopping centres. Breweries may suffer from volume decline as consumers avoid drinking venues. For consumer staples, reduced purchases by F&B outlets could be offset by higher household buying (i.e. stocking up).
Gaming	Negative	Resorts World Genting will be impacted from reduced footfall in its casino. NFOs may see a slight decline in ticket purchases as gamblers opt to stay at home.
Gloves	Neutral	Sales are predominately for the export market with little contribution from Malaysia (<5%). May have some +ve sentiment effect, perhaps from retail investors.
Healthcare	Slight Negative	Hospitals: Operational as usual, however KPJ Healthcare's Kedah Medical Centre had to close for 3 days hence small impact to the group. Healthcare support: For Edgenta, we expect higher operating costs on their concession business especially for their Kedah hospitals (9 hospitals).
REITs	Negative	Footfall to malls will be impacted, especially if a confirmed case has been determined there, which would then impact their tenant sales. If malls are impacted by targeted lockdowns, REIT managers may be inclined to help their tenants out via rental rebates, putting a dent to REIT's earnings. Hotels will too be negatively hit as the short-lived pent up demand for domestic tourism takes a backseat.
Plantation	Neutral	CPO output from Sabah makes up 24% of Malaysia's total output YTD; minimal impact as deemed "essential".
Telco	Positive	Demand for data will surge as a result of more WFH, entertainment and education purposes. We expect fixed players (TM and TdC) to benefit the most.
Logistics	Positive	People are spending less time shopping outside and opt for online shopping instead which will increase the demand for courier service. In this regard, PosM is a beneficiary given their high capacity to handle and extensive network.

HLIB estimates

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Stock rating guide

BUY	Expected absolute return of +10% or more over the next 12 months.
HOLD	Expected absolute return of -10% to +10% over the next 12 months.
SELL	Expected absolute return of -10% or less over the next 12 months.
UNDER REVIEW	Rating on the stock is temporarily under review which may or may not result in a change from the previous rating.
NOT RATED	Stock is not or no longer within regular coverage.

Sector rating guide

OVERWEIGHT	Sector expected to outperform the market over the next 12 months.
NEUTRAL	Sector expected to perform in-line with the market over the next 12 months.
UNDERWEIGHT	Sector expected to underperform the market over the next 12 months.

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