

Sunway Construction Group (SCGB MK)

1Q20 profit halved

Balanced risk-reward; D/G to HOLD

SCGB's 1Q20 net profit fell short, at 18%/11% of our/consensus FY20E despite our 41% earnings cut on 13 May [\[link\]](#). As alluded earlier, we expect a loss in 2Q20 due to fixed overheads amid Malaysia's MCO which has disrupted works for almost two months. We cut FY20E earnings by a further 27%, maintain FY21-22E. Our TP is unchanged but with potential total returns having narrowed to 5.4%, the stock is now a HOLD.

Construction down YoY, precast up

SCGB's 1Q20 construction revenue (90% of group revenue) weakened 19% YoY, impacted by two weeks of MCO (from 18 Mar) which also affected margins due to fixed overheads. Construction EBIT fell 54% YoY (margin: -4.1ppts YoY). Precast EBIT was up +3x YoY (small base); it could have been better if not for the MCO which disrupted logistics to clients in Singapore. Balance sheet wise, SCGB remains in a strong net cash position of MYR360m end-Mar 2020 (MYR407m end-2019) which is able to cover 24 months of fixed overheads.

Strong orderbook provides visibility

SCGB announced yet another sizeable win - a MYR121m contract to build the Sunway International School at Bandar Sunway for its sister company. Works are expected to start on 15 Jun 2020, to complete on 30 Jun 2022. This latest win has lifted SCGB's YTD job wins to MYR688m and its outstanding orderbook to MYR5.5b (end-2019: MYR5.2b). Management retains its MYR2b orderbook replenishment target for 2020.

Lowering FY20E; target valuation unchanged

We lower FY20E earnings to incorporate the weak 1Q20 and more conservative project margin assumptions leading to a lower blended EBIT margin estimate of 3.9% vs. 5.4% previously. We continue to peg TP to 16.5x FY21E PER, 10% above our target PER for the market, to reflect our optimism for some big-ticket infrastructure spending by the government to revive the economy, with SCGB to be a beneficiary. Nonetheless, risk-reward is about balanced with the stock now trading at 15.9x FY21E PER.

FYE Dec (MYR m)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	2,257	1,769	1,909	2,818	2,325
EBITDA	215	185	108	230	189
Core net profit	144	129	65	159	121
Core EPS (sen)	11.2	10.0	5.1	12.3	9.4
Core EPS growth (%)	9.2	(10.3)	(49.5)	143.7	(23.9)
Net DPS (sen)	7.0	7.0	3.5	7.0	7.0
Core P/E (x)	11.9	19.1	38.7	15.9	20.9
P/BV (x)	2.9	4.0	3.9	3.6	3.4
Net dividend yield (%)	5.3	3.7	1.8	3.6	3.6
ROAE (%)	25.5	21.3	10.3	23.5	16.7
ROAA (%)	8.1	7.0	3.3	6.9	4.9
EV/EBITDA (x)	6.3	11.1	19.3	8.6	10.7
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Consensus net profit	-	-	146	159	146
MKE vs. Consensus (%)	-	-	(55.2)	0.1	(16.9)

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HOLD

[Prior:BUY]

Share Price MYR 1.96
 12m Price Target MYR 2.03 (+7%)
 Previous Price Target MYR 2.03

Company Description

Sunway Construction Group offers integrated construction services and has precast concrete business in Singapore.

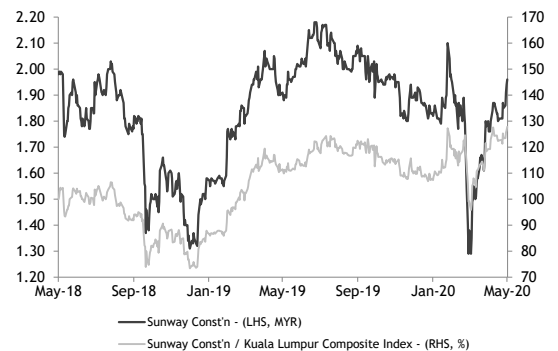
Statistics

52w high/low (MYR) 2.18/1.29
 3m avg turnover (USDm) 0.3
 Free float (%) 25.5
 Issued shares (m) 1,293
 Market capitalisation MYR2.5B
 USD582M

Major shareholders:

Sunway Bhd. 54.4%
 Active Equity Sdn. Bhd. 10.1%
 Employees Provident Fund 8.7%

Price Performance



	-1M	-3M	-12M
Absolute (%)	11	1	3
Relative to index (%)	7	7	15

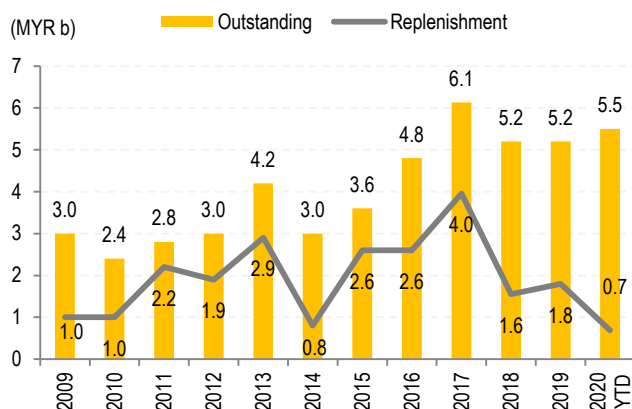
Source: FactSet

Fig 1: Results summary

FY Dec (MYR m)	Quarterly				
	1Q20	1Q19	% YoY	4Q19	% QoQ
Revenue	365.8	440.0	(16.9)	485.9	(24.7)
EBIT	(122.3)	(137.0)	(10.7)	30.8	(496.8)
Net interest	2.5	1.9	31.5	5.3	(51.7)
Assocs, JVs	-	-	NM	4.4	NM
Pre-tax profit	21.2	40.1	(47.1)	40.5	(47.6)
Tax	(4.3)	(8.5)	(49.2)	(7.8)	(44.7)
Minority Interests	(0.6)	(0.6)	(8.6)	(1.1)	(47.1)
Net profit	16.4	31.0	(47.3)	31.6	(48.3)
	1Q20	1Q19	+/- ppt	4Q19	+/- ppt
<i>EBIT margin (%)</i>	(33.4)	(31.1)	(2.3)	6.3	(39.8)
<i>Pretax margin (%)</i>	5.8	9.1	(3.3)	8.3	(2.5)
<i>Tax rate (%)</i>	20.3	21.2	(0.8)	19.3	1.0
Revenue	1Q20	1Q19	% YoY	4Q19	% QoQ
Construction	329.6	407.0	(19.0)	440.5	(25.2)
Precast concrete	36.3	33.0	9.9	45.4	(20.2)
Total	365.8	440.0	(16.9)	485.9	(24.7)
EBIT					
Construction	17.3	37.9	(54.4)	27.0	(35.9)
Precast concrete	1.4	0.3	NM	3.9	(63.5)
Total	18.7	38.2	(51.1)	30.8	(39.4)
EBIT margin (%)	1Q20	1Q19	+/- ppt	4Q19	+/- ppt
Construction	5.2	9.3	(4.1)	6.1	(0.9)
Precast concrete	3.9	1.0	2.9	8.5	(4.6)
Total	5.1	8.7	(3.6)	6.3	(1.2)

Source: Company

Fig 2: Outstanding orderbook vs. replenishment



*Including precast

Source: Company data

Fig 3: 12M forward PER



Source: Company data, Maybank Kim Eng

Fig 4: Outstanding orderbook of MYR5.5b (= MYR5.4b end-Mar 2020 + MYR175m secured in 2Q20)

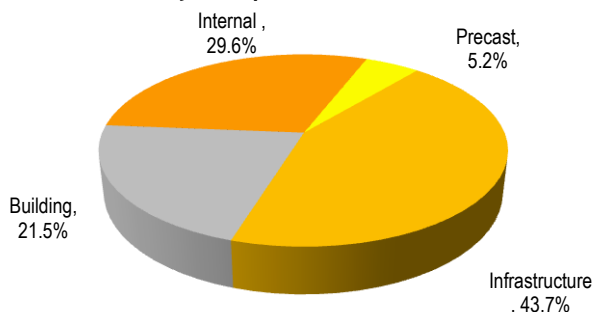
As at end-Mar 2020	Completion	Contract value (MYR m)	Outstanding (MYR m)
Infrastructure			
KVMRT 2, V201 (Sg Buloh-Persiaran Dagang)	2Q21	1,213	142
LRT 3 : Package GS07-08	2Q21	2,178	1,622
Piling Works	-	99	19
Piling Works #	-	60	17
Sentul West Station (MEP) #	1Q21	57	57
Tamil Nadu 4-lane highway construction +	4Q22	508	508
KVMRT 2, Chan Sow Lin underground station (MEP) +	2Q21	54	54
Building			
Putrajaya Parcel F	1Q19	1,610	25
PPA1M Project in Kota Bahru	2Q21	582	68
TNB HQ Campus #	2Q21	781	677
Petronas Learning Centre #	2Q21	310	287
Oxley Tower #	2Q22	68	66
IOI Mall (MEP) #	2Q21	68	67
Internal			
Sunway Medical Centre 4 (2 towers)	4Q21	450	363
Sunway Property - Kelana Jaya Condo	3Q21	413	243
Sunway Carnival 2 Extension - PDP contract	1Q21	286	215
SunGeo Lake 44 storey residential tower	1Q21	223	61
SMC Seberang Jaya	1Q21	180	137
Sunway Velocity Two	4Q21	352	286
Sunway Velocity 3C4	2Q21	100	66
BigBox Hotel #	3Q20	100	63
Parcel CP2 (piling) #	3Q21	119	79
BB Solar #	2Q20	8	0
Sunway Pyramid Solar #	2Q20	3	3
Sunway International School +	2Q22	121	121
New order in 2020 +	2Q20	4	4
Precast			
Secured pre 2019	-	331	285
New order in 2020 #	-	1	1
Total		10,279	5,536

#Secured in 2019; + Secured in 2020; Source: Company

Value Proposition

- SCGB is the construction arm of Sunway Group; it has built a strong brandname having commenced business in 1981 with a cumulative revenue since inception of MYR27b.
- SCGB operates on a fully integrated business model offering building and civil/infrastructure construction, MEP, and foundation & geotechnical engineering services; it also has two precast concrete manufacturing plants in Johor which supply IBS components largely to Singapore.
- Its completed special purpose building projects include KL Convention Centre, Sunway Shopping Mall; while civil projects include SILK, MEX, SKVE, BRT, KVMRT and KVLRT.
- A highly experienced senior management team and continuing support from the Sunway Group add on to its value proposition.

29.6% of MYR5.5b outstanding orderbook at end-Mar 2020 came from Sunway Group

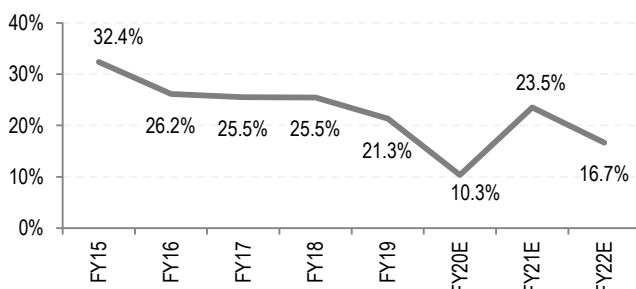


Source: Company

Financial Metrics

- Two main earning growth drivers are rising orderbook and higher margins which may come from value engineering.
- ROEs of >20% since its relisting in 2015 were above peers, but this will see a set-back in FY20E due to work disruption from Malaysia's Movement Control Order; we expect ROE to rebound to >20% in FY21E.
- Balance sheet is strong with a net cash of MYR407m (32sen/shr) as of end-FY19; we expect SCGB to remain in net cash over the medium term.
- DPR is a minimum 35% of PATMI; since its relisting, SCGB has been paying up to 70% (FY19).

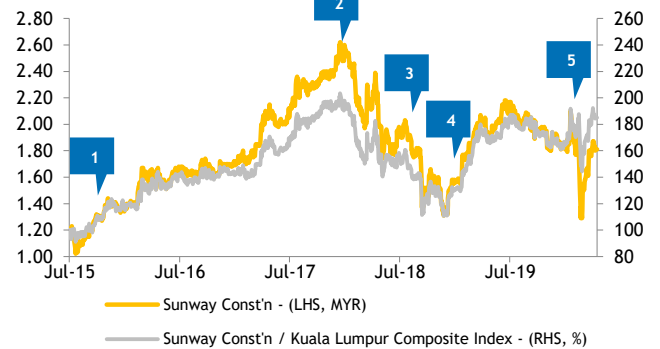
ROEs



Source: Company, Maybank KE

Price Drivers

Historical share price trend



Source: Company, Maybank Kim Eng

- Relisted on Bursa Malaysia on 28 Jul 2015 (earlier listing was from 1997 to 2004).
- Secured work packages under KVMRT 2 and KVLRT 3; outstanding orderbook reached a high of MYR6.1b as of end-2017.
- Post GE14 (9 May 2018) concerns, as the new government sought to review the cost of major infrastructure projects awarded during the previous government.
- Investor sentiment towards the overall construction sector improved.
- Malaysia's Movement Control Order from 18 Mar 2020 led to work disruption at all of SCGB's projects.

Swing Factors

Upside

- Larger-than-expected orderbook replenishment could lift sentiment on the stock although the earnings impact will only be felt in full a year later.
- Significant margin expansion on existing orderbook coming from value engineering breakthrough.
- Government's policy reaffirmation on rising usage of IBS in building construction as a long-term plan to reduce the country's over-reliance on foreign labour; this will be positive for SCGB's precast concrete business.

Downside

- Slower-than-expected work progress at existing major construction projects will affect the timing of earnings recognition.
- The timing of major infrastructure projects roll-out by the government could affect orderbook replenishment.
- At the precast segment, any significant increase in steel prices and stiffer competition could also affect margins.

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FYE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Key Metrics					
P/E (reported) (x)	17.4	19.1	38.7	15.9	20.9
Core P/E (x)	11.9	19.1	38.7	15.9	20.9
P/BV (x)	2.9	4.0	3.9	3.6	3.4
P/NTA (x)	2.9	4.0	4.0	3.6	3.4
Net dividend yield (%)	5.3	3.7	1.8	3.6	3.6
FCF yield (%)	8.0	7.4	2.8	8.6	1.6
EV/EBITDA (x)	6.3	11.1	19.3	8.6	10.7
EV/EBIT (x)	7.7	14.6	28.4	10.4	14.6
INCOME STATEMENT (MYR m)					
Revenue	2,256.8	1,768.7	1,909.1	2,818.3	2,324.8
Gross profit	441.8	391.7	315.0	437.0	395.9
EBITDA	215.1	185.3	108.5	230.5	189.4
Depreciation	(40.0)	(44.2)	(34.7)	(40.3)	(51.4)
EBIT	175.2	141.0	73.8	190.1	138.0
Net interest income / (exp)	6.8	12.0	7.6	8.4	12.2
Associates & JV	0.7	4.4	0.0	0.0	0.0
Exceptionals	0.0	0.0	0.0	0.0	0.0
Pretax profit	182.7	157.4	81.4	198.5	150.2
Income tax	(38.0)	(27.1)	(16.0)	(39.3)	(28.9)
Minorities	(0.3)	(1.0)	0.0	0.0	0.0
Reported net profit	144.4	129.3	65.3	159.3	121.3
Core net profit	144.4	129.3	65.3	159.3	121.3
BALANCE SHEET (MYR m)					
Cash & Short Term Investments	484.9	692.6	719.4	846.8	797.4
Accounts receivable	1,000.2	970.4	1,052.9	1,402.9	1,208.4
Inventory	30.0	25.1	29.1	43.4	35.2
Property, Plant & Equip (net)	177.0	138.7	161.3	205.5	223.9
Intangible assets	3.6	3.6	3.6	3.6	3.6
Investment in Associates & JVs	44.7	48.4	48.4	48.4	48.4
Other assets	27.6	26.2	26.2	26.2	27.2
Total assets	1,768.0	1,905.0	2,040.9	2,576.8	2,344.1
ST interest bearing debt	113.6	233.4	233.4	233.4	233.4
Accounts payable	939.6	885.2	1,000.9	1,467.9	1,203.3
LT interest bearing debt	0.0	52.7	52.7	52.7	52.7
Other liabilities	123.0	109.0	109.0	109.0	110.0
Total Liabilities	1,176.3	1,279.9	1,395.5	1,862.5	1,598.9
Shareholders Equity	590.2	623.0	643.1	712.1	743.0
Minority Interest	1.4	2.2	2.2	2.2	2.2
Total shareholder equity	591.7	625.2	645.3	714.3	745.2
Total liabilities and equity	1,768.0	1,905.0	2,040.9	2,576.8	2,344.1
CASH FLOW (MYR m)					
Pretax profit	182.7	157.4	81.4	198.5	150.2
Depreciation & amortisation	40.0	44.2	34.7	40.3	51.4
Adj net interest (income)/exp	6.8	12.0	7.6	8.4	12.2
Change in working capital	(10.4)	27.9	29.2	102.7	(61.9)
Cash taxes paid	(37.4)	(38.4)	(16.0)	(39.3)	(28.9)
Other operating cash flow	10.9	(15.0)	(7.6)	(8.4)	(12.2)
Cash flow from operations	192.6	188.1	129.2	302.3	110.7
Capex	(54.8)	(4.8)	(57.3)	(84.5)	(69.7)
Free cash flow	137.8	183.3	72.0	217.7	41.0
Dividends paid	(96.9)	(90.4)	(45.2)	(90.3)	(90.3)
Change in Debt	(24.5)	167.9	0.0	0.0	0.0
Other invest/financing cash flow	(18.1)	(43.4)	0.0	0.0	0.0
Net cash flow	(1.7)	217.5	26.8	127.4	(49.4)

FYE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Key Ratios					
Growth ratios (%)					
Revenue growth	8.7	(21.6)	7.9	47.6	(17.5)
EBITDA growth	9.3	(13.9)	(41.4)	112.5	(17.8)
EBIT growth	10.1	(19.5)	(47.7)	157.6	(27.4)
Pretax growth	8.3	(13.9)	(48.3)	143.9	(24.3)
Reported net profit growth	9.2	(10.5)	(49.5)	143.7	(23.9)
Core net profit growth	9.2	(10.5)	(49.5)	143.7	(23.9)
Profitability ratios (%)					
EBITDA margin	9.5	10.5	5.7	8.2	8.1
EBIT margin	7.8	8.0	3.9	6.7	5.9
Pretax profit margin	8.1	8.9	4.3	7.0	6.5
Payout ratio	62.6	69.9	69.1	56.7	74.5
DuPont analysis					
Net profit margin (%)	6.4	7.3	3.4	5.7	5.2
Revenue/Assets (x)	1.3	0.9	0.9	1.1	1.0
Assets/Equity (x)	3.0	3.1	3.2	3.6	3.2
ROAE (%)	25.5	21.3	10.3	23.5	16.7
ROAA (%)	8.1	7.0	3.3	6.9	4.9
Liquidity & Efficiency					
Cash conversion cycle	(29.8)	(30.8)	(16.1)	(24.3)	(39.8)
Days receivable outstanding	169.0	200.5	190.8	156.8	202.2
Days inventory outstanding	5.4	7.2	6.1	5.5	7.3
Days payables outstanding	204.1	238.5	213.0	186.6	249.3
Dividend cover (x)	1.6	1.4	1.4	1.8	1.3
Current ratio (x)	1.4	1.5	1.5	1.4	1.4
Leverage & Expense Analysis					
Asset/Liability (x)	1.5	1.5	1.5	1.4	1.5
Net gearing (%) (incl perps)	net cash	net cash	net cash	net cash	net cash
Net gearing (%) (excl. perps)	net cash	net cash	net cash	net cash	net cash
Net interest cover (x)	na	na	na	na	na
Debt/EBITDA (x)	0.5	1.5	2.6	1.2	1.5
Capex/revenue (%)	2.4	0.3	3.0	3.0	3.0
Net debt/ (net cash)	(371.2)	(406.6)	(433.4)	(560.8)	(511.4)

Source: Company; Maybank

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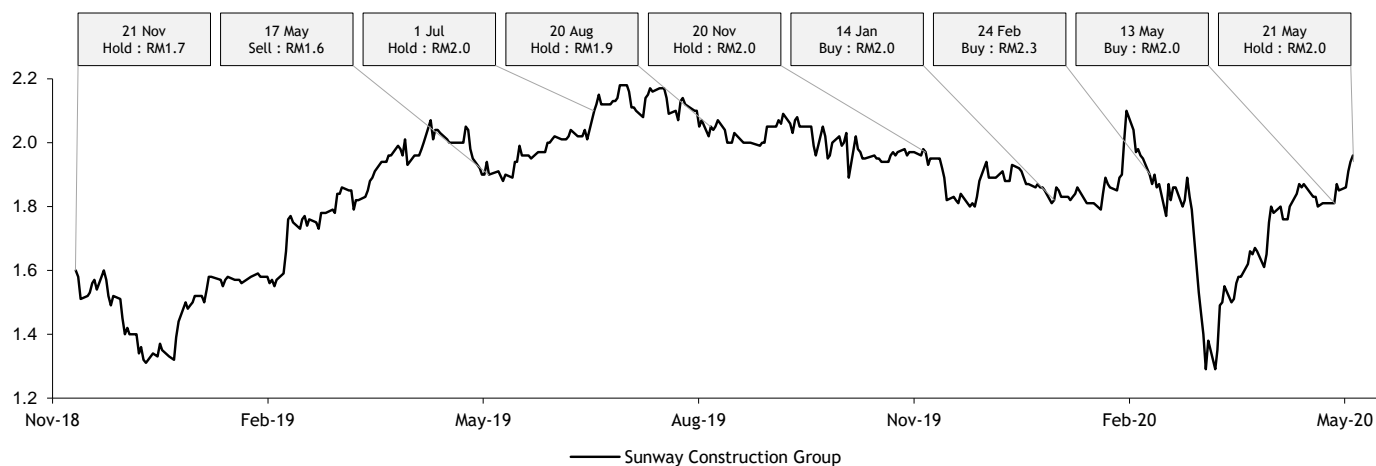
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