

21 May 2021

Construction & Engineering | Construction

Sunway Construction (SCGB MK)

Buy (Maintained)

Resilient Despite Lingering Challenges; Keep BUY

Target Price (Return): MYR2.03 (20.8%)
 Price: MYR1.68
 Market Cap: USD522m
 Avg Daily Turnover (MYR/USD): 1.29m/0.31m

- **BUY, new MYR2.03 TP from MYR2.18, 21% upside with c.4% FY21F yield.** 1Q21 earnings missed expectations at 13%/14% of our/Street's full-year estimates. Despite this, we believe the incremental pick-up in billings is encouraging. Revenue has improved YOY on higher output levels and productivity. Activities are expected to continue as usual, throughout MCO 3.0, as the sector is recognised as an essential service. Valuations remain attractive with the stock trading at a 17% discount from its 5-year mean.
- **Incremental growth expected, albeit gradually.** After excluding exceptional items, ie the disposal of an asset and one-off accretion of financial assets, Sunway Construction reported 1Q21 core earnings of MYR20.3m (+24% YoY, -30% QoQ.). At the operating level, we noticed a significant improvement in the margins of the precast business.
- **Construction wing saw higher revenue of MYR421m (+28% YoY, -28% QoQ)** in 1Q21, supported by higher progress billings from the TNB campus project in Bangsar and Petronas National Leadership Centre in Bangi. Progress billings will likely stay robust as it catches up with the completion schedule. In the precast division, SunCon has started recognising better margins, owing to higher-yield projects in Singapore. Management expects earnings from the segment to stay healthy in the coming quarters.
- **Short-term catalysts could surface in 2H21,** from the rollout of MRT3 packages. Management is confident in competing for the elevated portion, given its prior experience in MRT1 and MRT2, and capability to implement building information modelling and industrialised building system models into the construction process. A further boost to income looks supported by lumpy new orders bagged last year, which should sustain earnings into FY23F. SunCon's orderbook stands at MYR5.0bn.
- **Our TP is lowered after rolling over valuations to FY22F.** While we kept our revenue expectations, assumptions on operating cost levels were revised. In particular, we factored in the downside risk of steel price increases, which – according to management – could drive its overall costs up. Consequently, our net profits were reduced by 10%/8%/8% for FY21F-23F. At this juncture, we reduce our P/E from 18x to 16.5x (5-year mean). We stay conservative at this juncture as COVID-19 risks remain.
- **Downside risks:** Failure to secure new contracts, a prolonged downturn in the retail and property markets, and a longer-than-expected delay in the rollout of mega infrastructure projects. Increased restrictions on activities – possibly due to tighter lockdown measures, if implemented – may present further downside risks.

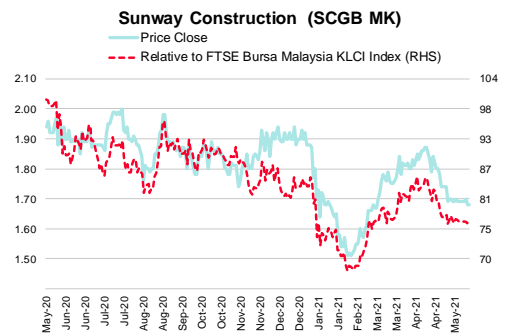
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(10.6)	(8.7)	5.0	(9.7)	(13.4)
Relative	(7.4)	(6.7)	5.6	(8.5)	(23.2)
52-wk Price low/high (MYR)	1.51 – 2.00				



Source: Bloomberg

Overall ESG Score: 3.0 (out of 4)

E: Good

Efforts are being made to reduce its environmental footprint. This includes improving energy efficiency, using resources responsibly, and reducing waste. Through the recycling and reuse of hydraulic oil, SunCon recycled a total of 12,787 litres of hydraulic oil in 2019. A plan is being made to increase the usage of green energy, through the installation of solar panels at its new workshop to generate electricity for its own consumption.

S: Good

The group ensures the safety and health of all its employees and at public areas surrounding the construction sites, via various training and safety programmes. Apart from up-to-standard health & safety policies, we see active community engagement and efforts in uplifting employee relations.

G: Excellent

57% of SunCon's board members are independent, with full disclosure on director remuneration including salaries and bonuses. It has an in-house investor relations team. Accessibility to investor relations is excellent, and the team mostly helps to deal with investors' queries.

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD1bn.

Forecasts and Valuation	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Total turnover (MYRm)	1,769	1,553	2,065	2,404	2,370
Recurring net profit (MYRm)	124	92	140	159	160
Recurring net profit growth (%)	(15.5)	(25.9)	51.8	13.6	0.8
Recurring P/E (x)	17.50	23.61	15.55	13.69	13.57
P/B (x)	3.5	3.4	3.1	2.8	2.5
P/CF (x)	8.82	na	22.60	12.07	9.64
Dividend Yield (%)	3.7	2.4	3.2	3.7	3.7
EV/EBITDA (x)	9.43	12.81	8.79	7.47	6.95
Return on average equity (%)	21.3	11.6	20.8	21.3	19.4
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, RHB

21 May 2021

Construction & Engineering | Construction

Financial Exhibits

Asia	Financial summary (MYR)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Malaysia	Recurring EPS	0.10	0.07	0.11	0.12	0.12
Construction & Engineering	DPS	0.06	0.04	0.05	0.06	0.06
Sunway Construction	BVPS	0.48	0.49	0.55	0.61	0.67
SCGB MK	Return on average equity (%)	21.3	11.6	20.8	21.3	19.4
Buy						
	Valuation metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Recurring P/E (x)	17.50	23.61	15.55	13.69	13.57
	P/B (x)	3.5	3.4	3.1	2.8	2.5
	FCF Yield (%)	11.0	(1.0)	0.5	5.8	7.8
	Dividend Yield (%)	3.7	2.4	3.2	3.7	3.7
	EV/EBITDA (x)	9.43	12.81	8.79	7.47	6.95
	EV/EBIT (x)	12.25	19.72	11.36	9.65	9.19
	Income statement (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Total turnover	1,769	1,553	2,065	2,404	2,370
	Gross profit	378	68	393	448	439
	EBITDA	183	139	210	241	246
	Depreciation and amortisation	(42)	(49)	(47)	(54)	(60)
	Operating profit	141	91	162	186	186
	Net interest	12	10	5	5	7
	Pre-tax profit	157	101	176	200	201
	Taxation	(27)	(28)	(36)	(41)	(41)
	Reported net profit	129	73	140	159	160
	Recurring net profit	124	92	140	159	160
	Cash flow (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Change in working capital	86	(140)	(101)	(33)	5
	Cash flow from operations	246	(18)	96	180	225
	Capex	(8)	(3)	(85)	(55)	(55)
	Cash flow from investing activities	(51)	181	(75)	(55)	(55)
	Dividends paid	(91)	(61)	(70)	(79)	(80)
	Cash flow from financing activities	72	(147)	(70)	(79)	(80)
	Cash at beginning of period	485	693	640	591	637
	Net change in cash	267	16	(49)	46	90
	Ending balance cash	751	708	591	637	727
	Balance sheet (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Total cash and equivalents	693	640	591	637	727
	Tangible fixed assets	139	107	145	145	140
	Total investments	49	49	39	39	39
	Total assets	1,905	1,906	1,828	2,044	2,112
	Short-term debt	233	234	234	234	234
	Total long-term debt	62	67	67	67	67
	Total liabilities	1,280	1,267	1,119	1,256	1,245
	Total equity	625	639	708	788	868
	Total liabilities & equity	1,905	1,906	1,828	2,044	2,112
	Key metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Revenue growth (%)	(21.6)	(12.2)	33.0	16.4	(1.4)
	Recurrent EPS growth (%)	(15.5)	(25.9)	51.8	13.6	0.8
	Gross margin (%)	21.4	4.4	19.0	18.7	18.5
	Operating EBITDA margin (%)	10.4	9.0	10.2	10.0	10.4
	Net profit margin (%)	7.3	4.7	6.8	6.6	6.8
	Dividend payout ratio (%)	61.6	70.9	50.0	50.0	50.0
	Capex/sales (%)	0.5	0.2	4.1	2.3	2.3
	Interest cover (x)	10.7	13.1	12.0	13.8	13.7

Source: Company data, RHB

21 May 2021

Construction & Engineering | Construction

Results At a Glance

Figure 1: SunCon's results review

FYE Dec (MYRm)	1Q20	4Q20	1Q21	QoQ (%)	YoY (%)	Comments
Revenue	365.8	627.2	455.2	(27.4)	24.4	Driver of growth is the construction segment.
EBIT	18.7	37.6	26.2	(30.3)	40.3	
<i>EBIT margin (%)</i>	5.1	6.0	5.8			
Interest expense	(2.7)	(0.3)	(1.6)	373.1	(41.4)	
Interest income	5.2	3.0	0.8	(75.2)	(85.6)	
JV/Associates	0.0	0.0	2.0	4,195.7	nm	
El/Others	0.0	1.2	(0.1)	(108.6)	nm	
Pretax profit	21.2	41.6	27.2	(34.5)	28.4	
<i>Pretax margin (%)</i>	5.8	6.6	6.0			
Tax	(4.3)	(11.5)	(6.9)	(39.8)	60.8	
<i>Effective tax rate (%)</i>	(20.3)	(27.7)	(27.4)			
Minority Interest	(0.6)	0.1	(0.1)	(151.4)	(87.0)	
Net profit	16.4	30.2	20.2	(33.0)	23.8	
Core profit	16.4	29.0	20.3	(29.8)	24.4	Below estimates
<i>Core net margin (%)</i>	4.5	4.6	4.5			

Source: Company data, RHB

Figure 2: SunCon's segmental results

FYE Dec (MYRm)	1Q20	4Q20	1Q21	QoQ (%)	YoY (%)	Comments
Revenue:						
Construction	329.6	585.0	421.3	(28.0)	27.8	Higher turnover was mainly due to higher progress billings from TNB campus project in Bangsar and Petronas National Leadership Centre in Bangi
Precast Concrete	36.2	42.2	33.9	(19.7)	(6.4)	
EBIT:						
Construction	17.3	34.8	22.3	(35.8)	29.3	
Precast Concrete	1.4	4.0	3.8	(5.9)	167.3	
EBIT Margin %:						
Construction	5.2%	6.0%	5.3%			Margin was low due to slower-than-expected construction activities
Precast Concrete	3.9%	9.5%	11.1%			

Source: Company data, RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2021-02-24	Buy	2.18	1.66
2020-08-20	Buy	2.09	1.80
2020-08-13	Buy	2.14	1.81
2020-07-23	Neutral	2.14	1.99
2020-05-22	Neutral	1.86	1.92
2020-04-23	Neutral	1.72	1.76
2020-04-09	Neutral	1.51	1.67
2020-02-18	Neutral	1.95	1.97

Source: RHB, Bloomberg

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