

Sunway Bhd (SWB MK)

Neutral

Price: M\$1.51

21 May 2018

Price Target: M\$1.55

PT End Date: 31 Dec 2018

1Q18 - property investment the star performer while pre-sales slow; Prefer ECW & SPSB

SWB's 14% Y/Y core earnings rise in 1Q18 was driven mainly by the property investment division. Including JV/associate contributions, profits from construction and property development were flat. Pre-sales was also slow in 1Q18 at just M\$166MM (13% of full year forecast) but this is seasonal and expected due also to the cautiousness ahead of the just concluded general elections. Despite short term uncertainty from the surprise outcome of the elections with a new government and review of policies, we remain positive on the longer term prospects for the property sector which had already started to show signs of bottoming ahead of the elections.

Our Top Picks in the property space remain ECW (OW) and SPSB (OW), while we maintain Neutral on SWB. For details, please see our 14 May-18 Malaysia Developers note titled "PTs cut post surprise election outcome; Maintain OW on ECW (top pick) and SPSB; Downgrade UEMS to Neutral" [here](#).

- **SWB's 1Q18 core net income (+14% Y/Y)** came in at 21%/20% of JPM/consensus full year forecast. 1Q is seasonally a weaker period and we maintain our forecast.
- **Property investment – the star performer.** Including associates and JV profits, growth was driven mainly by the property investment division, while profits from property development and construction were flattish. Property investment profits rose 29% Y/Y at the operating level (+21% including JVs/associates) driven by higher contribution from Sunway Pyramid Hotel following completion of its refurbishment exercise, new contribution from Sunway Velocity hotel which started operations in Sept-17, as well as improvement in performance from the new Sunway Velocity Mall and the group's theme parks.
- **A slow start in pre-sales which is seasonal and partly due to cautiousness ahead of elections.** Overall group pre-sales of M\$166MM in 1Q18 (vs M\$142MM in 1Q17) made 13% of JPM/management's full-year target of M\$1.3B, with domestic pre-sales of M\$101MM in 1Q18 (vs M\$75MM in 1Q17) accounting for 11% of our full year forecast. No change in the group's full year target.
- **Earnings visibility and financials.** Unbilled property sales of M\$947MM stood at 0.96x of historical revenue, while construction order-book of M\$6.1B as at end-1Q18 (of which M\$542MM was secured in 1Q18) stood at 3.8x its historical revenue. Net gearing improved to 38% in 1Q18 (from 45% in FY17).

Table 1: SWB 1Q18 results summary

M\$ mn; year-end Dec	1Q18	1Q17*	Y/Y	4Q17	Q/Q
Revenue	1,308	1,089	20%	1,730	-24%
Core Operating profit	130	125	4%	222	-42%
Operating margin	9.9%	11.5%		12.9%	
Net finance costs	-8	-7	13%	9	-183%
Associates & JVs	38	43	-11%	29	34%
Core PBT	161	152	6%	245	-34%
Net income	122	107	14%	183	-34%
Core net income	122	107	14%	167	-27%
Core margin	9.3%	9.8%		9.7%	
Core EPS (sen)	2.48	2.22	12%	3.40	-27%

Source: Company. * Restated.

Table 2: SWB 1Q18 core operating profit breakdown (excluding JVs/associates)

M\$ mn; year-end Dec	1Q18	1Q17*	Y/Y	4Q17	Q/Q
Prop development	18	11	68%	105	-83%
Prop investment	59	46	29%	61	-2%
Construction	39	38	2%	53	-26%
Trading & Manufacturing	14	13	11%	14	-2%
Quarry	2	1	149%	(1)	-443%
Others	(2)	17	-111%	(9)	-80%
Core operating profit	130	125	4%	222	-42%

Source: Company. * Restated.

Table 3: SWB 1Q18 core operating margins

	1Q18	1Q17*	Y/Y	4Q17	Q/Q
Prop development	13.3%	7.5%	6 ppts	25.4%	-12 ppts
Prop investment	26.9%	24.6%	2 ppts	24.7%	2 ppts
Construction	8.8%	12.1%	-3 ppts	9.0%	0 ppts
Trading & Manufacturing	5.0%	5.1%	0 ppts	6.1%	-1 ppts
Quarry	4.4%	2.2%	2 ppts	-1.2%	6 ppts
Others	-1.0%	10.5%	-11 ppts	-4.8%	4 ppts
Core operating margin	9.9%	11.5%	-2 ppts	12.9%	-3 ppts

Source: Company. * Restated.

Table 4: Developer domestic pre-sales

M\$mn; year-end Dec	1QCY18	1QCY17	Y/Y	4QCY17	Q/Q
SP Setia	636	352	81%	890	-29%
Sunway	101	75	35%	472	-79%
TOTAL DEVELOPERS	737	427	73%	1,362	-46%

Source: Companies.

Table 5: Developer peer comparison

As at: 21 May-18	FYE	Mkt cap (US\$m)	Price (M\$)	Rating	Target (M\$)	P/E		EPS growth		Net div yield		P/B	ROE	RNAV (M\$)	Prem/disc to RNAV
						CY18E	CY19E	CY18E	CY19E	FY18E	FY19E				
Eco World Develop	Oct	1,050	1.42	OW	1.60	20.5	14.0	51.8%	46.2%	0.0%	1.6%	0.9	5.1	2.80	-49%
Mah Sing Group	Dec	677	1.11	N	1.10	8.9	9.5	-14.1%	-6.2%	4.6%	4.3%	0.8	9.3	2.10	-47%
SP Setia	Dec	3,108	3.18	OW	3.60	22.5	18.4	-24.1%	22.8%	3.3%	4.1%	1.1	4.9	6.40	-50%
Sunway	Dec	1,849	1.51	N	1.55	12.2	10.8	5.4%	12.2%	4.2%	4.8%	0.9	7.6	2.50	-40%
UEM Sunrise	Dec	958	0.84	N	1.00	18.1	13.2	-25.0%	37.7%	1.4%	1.9%	0.6	2.9	2.70	-69%
Weighted average		7,641				18.0	14.5	-13.1%	19.9%	3.0%	3.7%	0.9	5.7		-50%

Source: Bloomberg, J.P. Morgan estimates.

Investment Thesis

We continue to like Sunway for its integrated businesses (50%-60% earnings from Construction and Prop Investment), with strong branding and assets (Prop Development landbank and commercial assets through its 37% stake in Sunway REIT). We also like its asset-light model, with the next asset recycling and potential value-unlocking coming from recently completed large properties (Pinnacle office tower and Velocity Mall). However, on valuations, we are Neutral on SWB at current levels, and see better value in its peers. We prefer SPSB (OW) and ECW (OW).

Valuation

Our Dec-18 PT of M\$1.55 is based on a 40% discount to RNAV (from 30% discount previously), or close to -1SD to historical mean for the sector.

Developer RNAV band



Source: Bloomberg, J.P. Morgan.

Sunway RNAV

Projects	% stake	Description	Undeveloped land (acres)	Remaining GDV (M\$ M)	Years to develop	Revaluation surplus (M\$ M)	Comments
Klang Valley							
Sunway Damansara	60%	Mixed township	15	1,691	5	136	Discounted at WACC of 10%
Sunway South Quay	100%	Mixed development	40	3,087	7	423	Discounted at WACC of 10%
Sunway Montereiz	60%	Residential	4	38	2	3	Discounted at WACC of 10%
Sunway Semenyih	70%	Residential	398	729	10	51	Discounted at WACC of 10%
Sunway Cheras	100%	Residential	6	17	2	2	Discounted at WACC of 10%
Sunway Duta	60%	Residential	3	120	3	9	Discounted at WACC of 10%
Sunway Montana	100%	Residential	2	56	3	8	Discounted at WACC of 10%
Sunway Resort City	100%	Commercial	15	660	6	88	Discounted at WACC of 10%
Sunway Velocity	85%	Mixed development	10	1,984	6	235	Discounted at WACC of 10%
Sunway Tower KL 1	100%	Office	1	240	3	32	Discounted at WACC of 10%
Sunway Velocity Two	50%	Mixed development	8	2,000	10	141	Discounted at WACC of 10%
Melawati	100%	Residential	2	43	2	6	Discounted at WACC of 10%
Sg Long	80%	Residential	111	277	4	27	Discounted at WACC of 10%
Mont Putra, Rawang	100%	Residential	163	156	6	19	Discounted at WACC of 10%
Sunway Serene Kelana Jaya	100%	Mixed development	18	1,450	5	218	Discounted at WACC of 10%
Sunway Industrial Park Subang	80%	Industrial	0	109	3	10	Discounted at WACC of 10%
Jalan Belfield-Kampung Attap-Istana	100%	Residential	5	1,100	6	148	Discounted at WACC of 10%
Lot One Kajang	100%	Residential	5	460	5	69	Discounted at WACC of 10%
USJ1 Subang Jaya	100%	Mixed development	15	1,400	5	241	Discounted at WACC of 10%
Sunway Wangsa Maju	55%	Residential	4	500	5	39	Discounted at WACC of 10%
			826	16,116		1,919	
Northern							
Sunway City Ipoh	65%	Residential	441	1,048	10	75	Discounted at WACC of 10%
Sunway Paya Terubong	100%	Residential	24	1,500	6	191	Discounted at WACC of 10%
Sunway Hills	100%	Residential	81	849	8	106	Discounted at WACC of 10%
Sunway Wellesley Bukit Mertajam	100%	Residential	51	710	5	91	Discounted at WACC of 10%
Sunway Tunas Balik Pulau	100%	Residential	9	60	2	7	Discounted at WACC of 10%
Sunway Betong Balik Pulau	100%	Residential	20	110	2	13	Discounted at WACC of 10%
			626	4,278		483	
Johor							
Bukit Lenang	80%	Residential	65	698	3	68	Discounted at WACC of 10%
Medini	60%	Mixed township	643	10,833	15	705	Discounted at WACC of 10%
Pendas	60%	Mixed township	1,079	18,000	20	871	Discounted at WACC of 10%
			1,787	29,531		1,644	
Singapore							
Rivercove Residences Sengkang	30%	Residential	5	1,560	4	52	Discounted at WACC of 10%
Brookvale Park	30%	Residential	9	3,000	3	103	Discounted at WACC of 10%
			14	4,560		155	
China							
Sunway Guanghao	65%	Mixed development	4	67	2	3	Discounted at WACC of 10%
Tianjin Eco City	60%	Mixed development	6	575	6	28	Discounted at WACC of 10%
India							
Sunway OPUS Grand India	50%	Condominiums	24	702	5	31	Discounted at WACC of 10%
Sunway MAK Signature Residence (JV with M.A.K Builders)	60%	Residential	14	181	5	8	Discounted at WACC of 10%
Australia							
Wonderland Business Park Sydney	45%	Industrial	13	44	3	2	Discounted at WACC of 10%
			61	1,569		72	
Total			3,314	56,054		4,273	

Source: Company data, J.P. Morgan estimates.

Sunway RNAV

	Value (M\$mn)	Comments
Revaluation surplus	4,273	
Book value as at Dec-17E	7,811	
Revaluation gain from investment properties	249	Value 37%-owned Sunway REIT at PT of M\$1.77
Revaluation gain from construction division	577	Valued at market price of M\$2.20/share
Outstanding cash obligation for land	(697)	Discounted value for Iskandar land purchase
Total RNAV	12,213	
Number of shares (M)	4,874	
RNAV per share (M\$)	2.51	
PT (M\$) – rounded off	1.55	40% discount to RNAV

Source: J.P. Morgan estimates.

Risks to Rating and Price Target

Key upside risks include:

1. Reasonably-priced, accretive landbank acquisitions, especially in the more resilient Klang Valley, where pre-sales have held up better amid the slower consumer environment
2. Asset recycling into 37%-held Sunway REIT, resulting in value-unlocking for shareholders
3. Stronger-than-expected property pre-sales

Key downside risks include: Slower-than-expected property pre-sales and keen competition in the Iskandar region in Johor.

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Other Companies Discussed in This Report (all prices in this report as of market close on 21 May 2018)

Eco World Development (ECOW.KL/M\$1.42/Overweight), SP Setia (SETI.KL/M\$3.18/Overweight)

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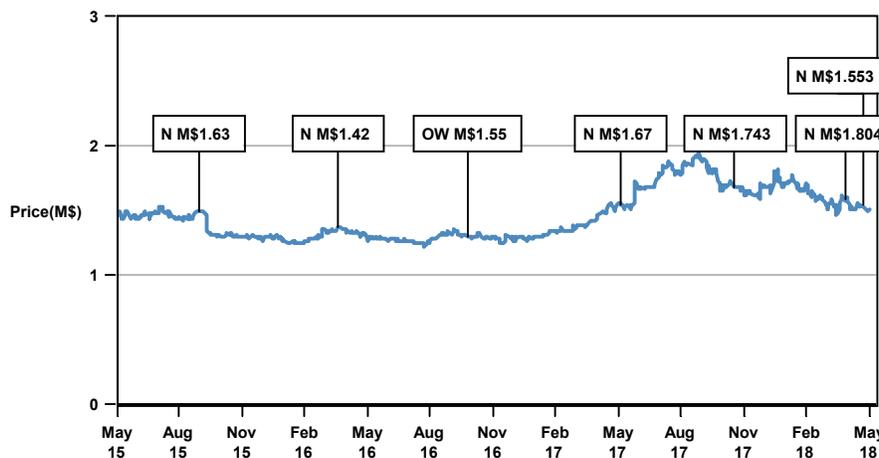
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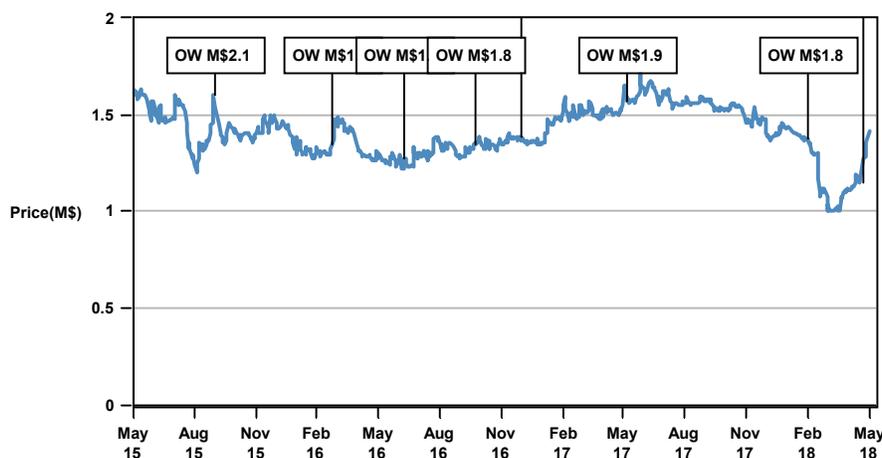
Sunway Bhd (SWAY.KL, SWB MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
19-Sep-15	N	1.48	1.63
08-Apr-16	N	1.38	1.42
14-Oct-16	OW	1.30	1.55
26-May-17	N	1.54	1.67
06-Nov-17	N	1.67	1.74
18-Apr-18	N	1.59	1.80
14-May-18	N	1.54	1.55

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Jul 26, 2013.

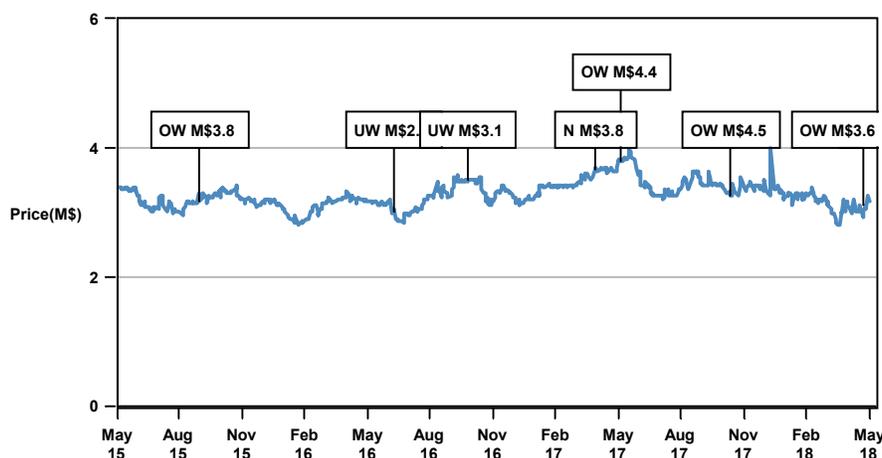
Eco World Development (ECOW.KL, ECW MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
19-Sep-15	OW	1.60	2.10
14-Mar-16	OW	1.34	1.90
28-Jun-16	OW	1.27	1.70
14-Oct-16	OW	1.34	1.80
20-Dec-16	OW	1.38	1.80
26-May-17	OW	1.57	1.90
20-Feb-18	OW	1.37	1.80
14-May-18	OW	1.15	1.60

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Sep 16, 2014.

SP Setia (SETI.KL, SPSB MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
19-Sep-15	OW	3.17	3.80
27-Jun-16	UW	3.01	2.80
14-Oct-16	UW	3.50	3.10
17-Apr-17	N	3.67	3.80
26-May-17	OW	3.79	4.40
01-Nov-17	OW	3.27	4.50
14-May-18	OW	3.11	3.60

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Aug 12, 2003.

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