Sunway Construction (SCGB MK)

BUY (maintain)
Up/Downside: +41.0%

Price Target: RM2.20
Previous Target (Rating): RM2.06 (BUY)

Strong recovery

- **Sunway Construction's (SunCon) core earnings rebounded 213% qoq to RM24.7m in 3Q21 on a higher construction profit margin despite lower revenue**
- **But core earnings eased 2% yoy to RM52.9m in 9M21 due to the impact of the pandemic lockdowns up to mid-August. Although new contract wins were only RM796m in 9M21, SunCon maintained its RM2bn target for 2021**
- **We lift core EPS by 11% in 2021E to reflect better construction profit margin but cut 2022E core EPS by 3% for the prosperity tax impact. SunCon remains a top sector BUY with a higher 12-month RNAV-based TP of RM2.20**

Within our expectation

SunCon's core net profit of RM52.9m (-2% yoy) in 9M21 comprised 68% of the consensus full-year forecast of RM77.7m and 62% of our previous estimate of RM85.5m. But we expect a better 4Q21 performance as progress billings accelerate for ongoing projects and the high 3Q21 construction profit margin to be sustainable.

Better profit margin for some projects near completion

Revenue grew 19% yoy to RM1.1bn in 9M21 with both construction (+18% yoy) and pre-cast concrete (+38% yoy) divisions reporting higher revenue. Group PBT increased 3% yoy to RM61.2m in 9M21 on the back of the higher revenue. But group PBT margin narrowed to 5.6% in 9M21 from 6.4% in 9M20 due to higher operating costs. Construction PBT declined 2% yoy in 9M21 as its profit margin was squeezed during the pandemic lockdowns. Construction PBT margin was marginally lower at 5.9% in 9M21 compared to 7.0% in 9M20. But margin recovered to 10.5% in 3Q21 due to the re-calibration of profit margins for some projects near completion. Precast concrete PBT was RM1.2m in 9M21 compared to a RM1.6m loss in 9M20, driven by a rebound in revenue (+38% yoy).

Good prospects to replenish order book

SunCon's high remaining order book of RM4.7bn will support earnings growth in 2021-23E, and it has good prospects of replenishing its order book with RM8bn of tenders submitted for new projects (20% overseas). Potential hospital and commercial property projects worth RM0.7bn could be secured from its parent Sunway this year.

Remains a sector top BUY with a higher TP of RM2.20

We believe SunCon is more resilient relative to peers in the current downturn due to its strong balance and we expect a strong earnings recovery in 4Q21. We maintain our BUY call and raise our RNAV-based TP to RM2.20 from RM2.06 to reflect the higher net cash of RM0.30/share at end-3Q21 with payment regularised for its LRT3 project (80% complete). Key risks: a slow roll-out of infrastructure projects and higher costs.

Earnings & Valuation Summary

FYE 31 Dec	2019	2020	2021E	2022E	2023E
Revenue (RMm)	1,768.7	1,552.7	1,772.8	2,842.0	3,177.4
EBITDA (RMm)	185.2	143.1	152.8	192.4	216.0
Pretax profit (RMm)	157.4	101.1	122.3	164.1	187.1
Net profit (RMm)	129.3	72.8	90.0	120.9	141.7
EPS (sen)	10.0	5.6	7.0	9.4	11.0
PER (x)	15.6	27.7	22.4	16.7	14.2
Core net profit (RMm)	133.2	92.0	95.0	120.9	141.7
Core EPS (sen)	10.3	7.1	7.4	9.4	11.0
Core EPS growth (%)	(11.3)	(31.0)	3.3	27.2	17.2
Core PER (x)	15.1	21.9	21.2	16.7	14.2
Net DPS (sen)	7.0	4.0	7.0	7.0	7.0
Dividend Yield (%)	4.5	2.6	4.5	4.5	4.5
EV/EBITDA	8.7	11.7	11.8	9.7	8.5
Chg in EPS (%)			11.1	-2.6	0.0
Affin/Consensus (x)			1.2	0.9	1.0

Source: Company, Affin Hwang forecasts

> *"3Q21 core earnings rebounded 213% qoq"*

Share price performance

	1M	3M	12M
Absolute (%)	-7.1	-1.3	-15.2
Rel KLCI (%)	-2.1	-1.2	-10.7

	BUY	HOLD	SELL
Consensus	8	6	-

Stock Data

Sector	Construction
Issued shares (m)	1,289.4
Mkt cap (RMm)/(US$m)	2,011.4/481.4
Avg daily vol - 6mth (m)	0.2
52-wk range (RM)	1.50-2.00
Est free float	18.3%
Stock Beta	0.82
Net cash/(debt) (RMm)	389.5
ROE (2021E)	14.1%
Derivatives	No
Shariah Compliant	Yes
FTSE4Good Constituent	No
FBM EMAS (Top 200)	No
ESG Rank	
ESG Risk Rating	26.3 (-3.2 yoy)

Key Shareholders

Sunway Holdings	54.6%
Sungei Way Corp	10.1%
EPF	9.2%
ASN	5.5%

Source: Bloomberg, Affin Hwang, ESG Risk Rating Powered by Sustainalytics, Bursa Malaysia

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Fig 1: Results comparison

FYE 31 Dec (RMm)	3Q20	2Q21	3Q21	QoQ % chg	YoY % chg	9M20	9M21	YoY % chg	Comment
Revenue	**419.4**	**375.3**	**272.1**	***(27.5)***	***(35.1)***	**925.4**	**1,102.5**	***19.1***	Higher construction (+18% yoy) and pre-cast concrete (+38% yoy) revenue.
Op costs	(370.6)	(363.5)	(237.8)	*(34.6)*	*(35.8)*	(836.6)	(1,022.2)	*22.2*	Higher steel and other construction costs.
EBITDA	**48.9**	**11.7**	**34.3**	***192.6***	***(29.8)***	**88.8**	**80.3**	***(9.5)***	
EBITDA margin (%)	*11.6*	*3.1*	*12.6*	*9.5ppt*	*1.0ppt*	*9.6*	*7.3*	*(2.3ppt)*	Lower profit margin for new construction contracts secured in 2020 due to the competitive landscape and higher steel costs.
Depn and amort	(8.1)	(5.8)	(6.9)	*18.8*	*(14.7)*	(25.6)	(20.8)	*(18.8)*	
EBIT	**40.8**	**5.9**	**27.4**	***362.3***	***(32.8)***	**63.2**	**59.6**	***(5.8)***	
Interest income	4.6	1.4	1.0	*(28.8)*	*(78.7)*	14.3	3.1	*(78.3)*	Lower cash returns following cuts in deposit rates.
Interest expense	(1.6)	(1.0)	(0.9)	*(7.2)*	*(41.4)*	(6.6)	(3.5)	*(46.8)*	
Associates	0.0	2.8	2.4	*(14.2)*	*#DIV/0!*	0.1	7.1	*10,978.1*	
Forex gain (losses)	(0.2)	(0.0)	(0.2)	*435.9*	*9.4*	(0.1)	(0.3)	*197.8*	
Exceptional items	(7.7)	0.5	(5.2)	*NA*	*(32.6)*	(11.4)	(4.7)	*(58.4)*	
Pretax profit	**36.0**	**9.5**	**24.5**	***157.3***	***(31.9)***	**59.5**	**61.2**	***2.9***	Lower construction PBT (-2% yoy) due to lower profit margin. Pre-cast concrete operation turned around in 9M21.
Core pretax	**43.8**	**9.1**	**29.8**	***229.2***	***(31.9)***	**71.0**	**66.3**	***(6.7)***	
Tax	(11.7)	(3.6)	(5.0)	*38.2*	*(57.7)*	(16.3)	(15.5)	*(4.8)*	
Tax rate (%)	*32.6*	*53.1*	*22.4*	*(30.6ppt)*	*(10.2ppt)*	*27.3*	*28.6*	*1.2ppt*	
Minority interests	(0.2)	2.4	(0.2)	*NA*	*19.3*	(0.7)	2.1	*NA*	
Net profit	**24.0**	**8.3**	**19.3**	***131.8***	***(19.7)***	**42.6**	**47.9**	***12.4***	Within expectations.
Core net profit	**31.9**	**7.9**	**24.7**	***213.2***	***(22.7)***	**54.1**	**52.9**	***(2.2)***	Within expectations. Exclude one-off items.
EPS (sen)	1.9	0.7	1.5	*130.8*	*(19.4)*	3.3	3.7	*12.4*	

Source: Affin Hwang, Company

Fig 2: Segmental revenue breakdown

Segment	3Q20	2Q21	3Q21	QoQ % chg	YoY % chg	9M20	9M21	YoY % chg
Construction	403.4	349.2	255.8	*(26.7)*	*(36.6)*	870.2	1,026.3	*17.9*
Precast concrete	16.0	26.1	16.3	*(37.6)*	*1.8*	55.2	76.2	*38.0*
Total	**419.4**	**375.3**	**272.1**	***(27.5)***	***(35.1)***	**925.4**	**1,102.5**	***19.1***

Source: Affin Hwang, Company

Fig 3: Segmental PBT breakdown

Segment	3Q20	2Q21	3Q21	QoQ % chg	YoY % chg	9M20	9M21	YoY % chg
Construction	34.8	9.5	26.9	*182.0*	*(22.6)*	61.1	60.1	*(1.7)*
Precast concrete	1.2	(0.0)	(2.4)	*8,582.1*	*(302.6)*	(1.6)	1.2	*(176.1)*
Total	**36.0**	**9.5**	**24.5**	***157.3***	***(31.9)***	**59.5**	**61.2**	***2.9***

Source: Affin Hwang, Company

Fig 4: Segmental PBT margin

FYE 31 Dec (%)	3Q20	2Q21	3Q21	QoQ ppt chg	YoY ppt chg	9M20	9M21	YoY ppt chg
Construction	8.6	2.7	10.5	*7.8*	*1.9*	7.0	5.9	*(1.2ppt)*
Precast concrete	7.5	(0.1)	(14.9)	*(14.8)*	*(22.5)*	(2.8)	1.6	*4.4ppt*
Total	**8.6**	**2.5**	**9.0**	***6.5***	***0.4***	**6.4**	**5.6**	*(0.9ppt)*

Source: Affin Hwang, Company

Fig 5: RNAV and target price

Segments	Stake (%)	New RNAV (RMm)	Old RNAV (RMm)	Change (%)
Construction @ PER 16x sustainable earnings of RM130m	100	2,080	2,080	0
Pre-cast concrete @ PER 16x sustainable earnings of RM20m	100	320	315	2
Investment in Singapore IPPH JV @ book value	50	44	44	0
Net cash/(debt)		389	217	79
RNAV		**2,834**	**2,657**	**7**
No. of shares (m)		1,291	1,291	0
RNAV/share (RM)		**2.20**	**2.06**	**7**
Target price at RNAV/share		**2.20**	**2.06**	**7**

Source: Affin Hwang, Company

Important Disclosures and Disclaimer

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +10% over a 12-month period
HOLD	Total return is expected to be between -5% and +10% over a 12-month period
SELL	Total return is expected to be below -5% over a 12-month period
NOT RATED	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.

OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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