

Sunway Construction SCOG.KL SCGB MK

EQUITY: ENGINEERING & CONSTRUCTION

A temporary blip in 1Q23

Ramp-up of projects and receivables monetisation should be positive catalysts

1Q23 in numbers: SunCon reported adjusted 1Q23 net income of MYR28mn, down 19% y-y and down 39% q-q. The q-q decline was driven by lower margins from both the construction and precast segments. 1Q23 net income formed 19%/18% of our old/Bloomberg consensus' FY23F estimates. SunCon's net gearing ratio is now at 0.06x vs a net cash position of MYR55mn as at end-2022, due to receivables from India projects.

Cashflow and orderbook: The company reported negative operating cash flows (OCF) of MYR61mn vs MYR107mn negative OCF in 4Q22. SunCon is targeting MYR2bn orderbook replenishment (Nomura: MYR2bn) in FY23E and it has already secured MYR1.28bn worth of projects in 1Q23.

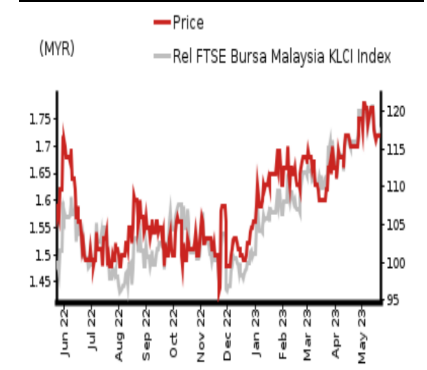
Earnings revisions: We adjust FY23F/24F earnings by +2%/+17% due to the higher orderbook replenishment and faster progress on new projects, which is partially offset by lower PBT margins from India projects due to higher finance costs.

Outlook: Potential pipeline for SunCon includes the further packages for JB-Singapore RTS (two more packages are to be awarded), data-center projects, semiconductor factory and warehouse projects; a shopping mall in Ipoh (to be awarded by end of the year), Extension of Sunway Carnival Mall in Penang mainland (~MYR100-200mn project), Sunway Medical Centre extension (~MYR50-80mn) and precast.

Reiterate Buy with an unchanged TP of MYR2.00: We reiterate our Buy rating on SunCon as: 1) we think a visible pipeline of projects from the parentco and Malaysia/India jobs should help with orderbook replenishment and provide better earnings visibility; 2) catalysts such as ramp-up of projects should lead to better upcoming quarters, and potential monetisation of receivables should help its balance sheet, 3) we believe SunCon is the best pure-play exposure within our construction sector coverage universe in Malaysia, with strong earnings to cash flow conversion, a liquid balance sheet, and high ROEs (FY23F/24F: 19%/ 18.5%); and 4) we expect its precast orderbook to grow again due to the opening of its new precast plant in Singapore. We value SunCon at a FY23F P/E of 18x (+1SD to its long-term average valuation, justified for an asset light cash generative business) to arrive at our TP of MYR2.00, implying ~18% upside. The stock is currently trading at 14.9x FY23F EPS of 11sen.

Rating Remains	Buy
Target price Remains	MYR 2.00
Closing price 23 May 2023	MYR 1.69
Implied upside	+18.3%
Market Cap (USD mn)	479.4
ADT (USD mn)	0.1

Relative performance chart



Source: Thomson Reuters, Nomura

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Year-end 31 Dec	FY22	FY23F		FY24F		FY25F	
Currency (MYR)	Actual	Old	New	Old	New	Old	New
Revenue (mn)	2,155	2,597	2,967	2,313	3,026		2,753
Reported net profit (mn)	135	144	147	134	157		163
Normalised net profit (mn)	135	144	147	134	157		163
FD normalised EPS	10.48c	11.14c	11.34c	10.36c	12.14c		12.58c
FD norm. EPS growth (%)	20.1	21.9	8.2	-7.0	7.0		3.6
FD normalised P/E (x)	16.1	-	14.9	-	13.9	-	13.4
EV/EBITDA (x)	10.7	-	10.6	-	9.4	-	9.2
Price/book (x)	3.0	-	2.7	-	2.5	-	2.3
Dividend yield (%)	3.2	-	3.7	-	3.9	-	4.1
ROE (%)	18.8	18.9	18.9	16.3	18.5		17.6
Net debt/equity (%)	net cash	net cash	46.4	net cash	34.8		23.1

Source: Company data, Nomura estimates

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Key data on Sunway Construction

Performance

(%)	1M	3M	12M		
Absolute (MYR)	-0.6	1.2	6.3	M cap (USDmn)	479.4
Absolute (USD)	-3.3	-1.6	2.3	Free float (%)	35.4
Rel to FTSE Bursa Malaysia KLCI Index	-0.4	3.8	14.3	3-mth ADT (USDmn)	0.1

Income statement (MYRmn)

Year-end 31 Dec	FY21	FY22	FY23F	FY24F	FY25F
Revenue	1,729	2,155	2,967	3,026	2,753
Cost of goods sold	-1,590	-1,969	-2,744	-2,780	-2,510
Gross profit	139	187	223	247	244
SG&A					
Employee share expense					
Operating profit	139	187	223	247	244
EBITDA	167	210	247	272	270
Depreciation	-27	-24	-24	-25	-26
Amortisation					
EBIT	139	187	223	247	244
Net interest expense	0	-4	-29	-39	-30
Associates & JCEs	13	2	2	2	2
Other income					
Earnings before tax	152	184	196	210	216
Income tax	-41	-45	-48	-52	-53
Net profit after tax	111	139	148	158	163
Minority interests	2	-4	-1	-1	0
Other items					
Preferred dividends					
Normalised NPAT	113	135	147	157	163
Extraordinary items	-17	0	0	0	0
Reported NPAT	95	135	147	157	163
Dividends	-68	-71	-81	-86	-89
Transfer to reserves	28	64	66	71	73

Valuations and ratios

Reported P/E (x)	22.9	16.1	14.9	13.9	13.4
Normalised P/E (x)	19.4	16.1	14.9	13.9	13.4
FD normalised P/E (x)	19.4	16.1	14.9	13.9	13.4
Dividend yield (%)	3.1	3.2	3.7	3.9	4.1
Price/cashflow (x)	9.1	-	-	12.7	11.2
Price/book (x)	3.1	3.0	2.7	2.5	2.3
EV/EBITDA (x)	13.0	10.7	10.6	9.4	9.2
EV/EBIT (x)	15.3	12.0	11.8	10.4	10.2
Gross margin (%)	8.1	8.7	7.5	8.2	8.9
EBITDA margin (%)	9.6	9.8	8.3	9.0	9.8
EBIT margin (%)	8.1	8.7	7.5	8.2	8.9
Net margin (%)	5.5	6.3	4.9	5.2	5.9
Effective tax rate (%)	27.3	24.6	24.6	24.6	24.7
Dividend payout (%)	71.0	52.5	55.0	55.0	55.0
ROE (%)	14.3	18.8	18.9	18.5	17.6
ROA (pretax %)	8.8	10.7	11.0	10.5	10.6

Growth (%)

Revenue	11.4	24.6	37.7	2.0	-9.0
EBITDA	34.6	26.0	17.5	10.0	-0.7
Normalised EPS	54.7	20.1	8.2	7.0	3.6
Normalised FDEPS	54.7	20.1	8.2	7.0	3.6

Source: Company data, Nomura estimates

Cashflow statement (MYRmn)

Year-end 31 Dec	FY21	FY22	FY23F	FY24F	FY25F
EBITDA	167	210	247	272	270
Change in working capital	125	-198	-165	-10	7
Other operating cashflow	-54	-227	-377	-90	-83
Cashflow from operations	238	-215	-295	172	194
Capital expenditure	-35	-27	-20	-20	-20
Free cashflow	204	-242	-315	152	174
Reduction in investments	-235	500	-2	-2	-2
Net acquisitions					
Dec in other LT assets	6	-267	-300	0	0
Inc in other LT liabilities	4	-7	0	0	0
Adjustments	42	265	302	2	2
CF after investing acts	21	250	-315	152	174
Cash dividends	-52	-90	-73	-83	-88
Equity issue					
Debt issue	-70	233	300	0	0
Convertible debt issue					
Others	-1	0	0	0	0
CF from financial acts	-122	143	227	-83	-88
Net cashflow	-101	393	-87	68	86
Beginning cash	200	99	492	404	473
Ending cash	99	492	404	473	559
Ending net debt	139	-11	376	308	222

Balance sheet (MYRmn)

As at 31 Dec	FY21	FY22	FY23F	FY24F	FY25F
Cash & equivalents	99	492	404	473	559
Marketable securities					
Accounts receivable	661	813	1,120	1,142	1,039
Inventories	46	53	62	63	57
Other current assets	209	279	279	279	279
Total current assets	1,015	1,637	1,866	1,957	1,934
LT investments	724	223	225	227	228
Fixed assets	125	108	104	99	92
Goodwill	0	0	0	0	0
Other intangible assets	0	0	0	0	0
Other LT assets	1	268	568	568	568
Total assets	1,864	2,236	2,762	2,850	2,823
Short-term debt	93	172	172	172	172
Accounts payable	891	886	1,037	1,050	948
Other current liabilities	8	45	45	45	45
Total current liabilities	992	1,103	1,254	1,267	1,165
Long-term debt	145	309	609	609	609
Convertible debt					
Other LT liabilities	10	3	3	3	3
Total liabilities	1,147	1,415	1,866	1,879	1,777
Minority interest	18	84	85	86	86
Preferred stock					
Common stock	259	259	259	259	259
Retained earnings	471	516	590	663	738
Proposed dividends					
Other equity and reserves	-30	-37	-37	-37	-37
Total shareholders' equity	699	737	811	885	959
Total equity & liabilities	1,864	2,236	2,762	2,850	2,823

Liquidity (x)

Current ratio	1.02	1.48	1.49	1.54	1.66
Interest cover	324.2	44.9	7.8	6.4	8.2

Leverage

Net debt/EBITDA (x)	0.83	net cash	1.52	1.13	0.82
Net debt/equity (%)	19.9	net cash	46.4	34.8	23.1

Per share

Reported EPS (MYR)	7.39c	10.48c	11.34c	12.14c	12.58c
Norm EPS (MYR)	8.73c	10.48c	11.34c	12.14c	12.58c
FD norm EPS (MYR)	8.73c	10.48c	11.34c	12.14c	12.58c
BVPS (MYR)	0.54	0.57	0.63	0.68	0.74
DPS (MYR)	0.05	0.05	0.06	0.07	0.07

Activity (days)

Days receivable	165.3	124.8	118.9	136.8	144.6
Days inventory	9.2	9.2	7.7	8.3	8.8
Days payable	210.2	164.8	127.9	137.4	145.3
Cash cycle	-35.8	-30.7	-1.3	7.7	8.0

Source: Company data, Nomura estimates

Company profile

Sunway Construction (SunCon) a pure-play construction company that provides a full range of integrated design and construction services including building, infrastructure, foundation and geotechnical engineering, mechanical, electrical and plumbing (MEP) services, manufacturing and sale of precast concrete products as well as sustainable energy services. It has presence in seven countries – Malaysia, Singapore, Philippines, UAE, Trinidad & Tobago and Myanmar. It has 2 precast plants in Malaysia and its Integrated Construction and Prefabrication Hub (ICPH) precast plant in Singapore will complete in 2022. SunCon's orderbook is also supported by its parentco Sunway Bhd (SWB MK, not rated).

Valuation Methodology

We value SunCon at a target P/E of 18x on FY23F earnings estimate of MYR147mn for FY23F. We arrive at our TP of MYR2.00. The benchmark index for the stock is FTSE Bursa Malaysia KLCI Index.

Risks that may impede the achievement of the target price

Downside risks include: 1) delays in construction project awards; 2) lower-than-expected margins; 3) lower pre-cast earnings persisting; 4) a lack of new projects; 5) risk of project cancellation or arbitration.

ESG

We ascribe a score of 3.5 (out of 5.0) for SunCon's Environment-related (E) achievements and risks due to the nature of construction business which leads to some environmental impact. That said, the company is moving towards adding renewal energy projects as part of its orderbook. We ascribe a score of 4.0 (out of 5.0) for SunCon's Social-related (S) achievements and risks. We ascribe a score of 3.5 (out of 5.0) for SunCon's Governance-related (G) achievements and risks. The company is well managed with good shareholder return policy and asset-light business model which enhances return on capital and has a high dividend payout ratio. It has good long-standing customer relationships with key Malaysian project owners in both the public and private sector, which is testament to its execution capabilities.

1Q23 results review

Results snapshot: SunCon reported adjusted 1Q23 net income of MYR28mn, down 19% y-y and down 39% q-q. The q-q decline was driven by lower margins from both the construction and precast segments. 1Q23 net income formed 19%/18% of our old/Bloomberg consensus' FY23F estimates. SunCon's net gearing ratio is now at 0.06x vs a net cash position of MYR55mn as at end-2022, due to receivables from Indian highways which have deferred payment terms.

Construction segment review: Construction revenue for 1Q23 was MYR469mn, up 6% q-q. However, PBT was down 29% q-q due to lower margins. PBT margins were down 4pp q-q to 7.7% vs 11.5% in 4Q22, as a number of projects were completed last year and new ongoing projects are in the initial stages. Management noted that the existing active projects are in the initial stages and therefore work progress was slower in 1Q23. New orderbook replenishment for 1Q23 was at MYR1.28bn. The company's outstanding orderbook currently stands at MYR6bn, while the active tender-book stands at MYR22.7bn. The company reported negative operating cash flows (OCF) of MYR61mn vs MYR107mn negative OCF in 4Q22. Note that SunCon currently has a long term receivables balance of MYR330mn on its balance sheet. This relates to two India projects, which have deferred payment terms for 60% of project value, and therefore need SunCon to draw down debt to finance it. The receivables balance is likely to go up by another ~MYR230mn as these projects near completion by end of the year. Management is also looking to monetise and sell these receivables to interested parties, which will be positive in our view.

Precast segment review: Precast revenue/PBT for 1Q23 came in at MYR53mn/ MYR1mn (-11%/ -76% q-q). The extent of PBT decline was higher vs the revenue decline due to higher depreciation after the opening of its precast plant (ICPH) in Singapore in Jan'23. Note that, on a group level, depreciation was down q-q due to lower depreciation from the construction segment as a lot of machinery was fully depreciated in the past. There should be higher contribution from the precast segment to SunCon's earnings in the near future, according to management, with the new capacity at the Singapore plant operational.

Outlook: SunCon is targeting MYR2bn orderbook replenishment (Nomura: MYR2bn) in FY23E, and it has already secured MYR1.28bn worth of projects in 1Q23. On MRT3, should SunCon not win the main contractor role, it is open to be a subcontractor in the civil work packages. The tender evaluation for MRT3 and pre-qualification for Bayan Lepas LRT are still ongoing, with MRT3 tender evaluation extended to Jun'23 and the pre-qualification validity for Bayan Lepas LRT extended to Jul'23. Management foresees some delays in MRT3 award due to alignment changes. Potential pipeline for SunCon also includes the further packages for JB-Singapore RTS (2 more packages are to be awarded), data-center projects, semiconductor factory and warehouse projects; shopping mall in Ipoh (to be awarded by end of the year), extension of Sunway Carnival Mall in Penang mainland (~MYR100-200mn project), Sunway Medical Centre extension (~MYR50-80mn) and precast. On margins, management is guiding for a normalised PBT margin of 5-8% from the construction segment as a number of projects are in the initial stages. SunCon has also entered into a definitive EPC agreement for Song Hau 2 thermal power plant in *Vietnam* in Mar'23. It is still awaiting financial closure on this project which is expected in Sep'23, as per management. As mentioned above, with the opening of its precast plant in Singapore, earnings contribution from the precast division will also increase. Capex for SunCon will remain low as ICPH development is almost complete.

Fig. 1: SunCon – 1Q23 results snapshot

MYR mn	1Q23	NMR FY23F new	as % of NMR new	Cons FY23F	as % of cons
Revenue	522	2,967	18%	2,777	19%
Adj PBT	38	196	19%	199	19%
Adj NPATAMI	28	147	19%	153	18%
Reported NPATAMI	28	147	19%	153	18%

Source: Company data, Bloomberg Finance L.P., Nomura estimates

Fig. 2: SunCon – 1Q23 results review

MYR mn	1Q23	1Q22	% chg y-y	4Q22	% chg q-q	FY23F new	as % of FY23F new
Revenues	522	625	(16%)	503	4%	2,967	18%
Construction	469	588	(20%)	444	6%	2,792	17%
Precast concrete	53	37	44%	59	(11%)	175	30%
Operating profit	42	43	(3%)	64	(35%)	223	19%
Construction	38	42	(9%)	54	(30%)		
Precast concrete	4	1	187%	10	(61%)		
Adjusted Pretax profit	38	47	(20%)	56	(33%)	196	19%
Construction	36	46	(22%)	51	(29%)	192	19%
Precast concrete	1	1	28%	5	(76%)	4	30%
Core PAT	29	36	(20%)	46	(37%)	148	19%
Core PAT - equityholders	28	35	(19%)	46	(39%)	147	19%
Other one-off charges	0	0	NM	0	NM	0	NM
Headline NPAT - equityholders	28	35	(19%)	46	(39%)	147	19%
Adj Pretax margins	7.2%	7.6%	0 ppt	11.2%	-4 ppt	6.6%	
Construction	7.7%	7.9%	0 ppt	11.5%	-4 ppt	6.9%	
Precast concrete	2.4%	2.7%	0 ppt	8.9%	-6 ppt	2.5%	

Source: Company data, Nomura estimates

Fig. 3: SunCon's outstanding orderbook

end-1Q23

MYR mn	Contract Sum		Outstanding order book	
Infrastructure/Piling				
LRT3: Package GS07-08	2,178	1,295	1,589	29
Jalan Tambun		14		4
RTS Link Package P2A		10		3
RTS Link Package 1B and 5		605		605
LRT3: GS06		191		73
Building				
Oxley Tower + VO		77		51
JHB1X0 - Data Centre		1,700		1,656
Renewable energy		499		416
India				
Thorapalli Agraharam - Jittandahalli		508		363
Meensurutti - Chidambarm 32km		315		144
Internal				
Sunway Medical Centre Phase 4 + VO		612		102
Velo 2		352		11
3C4		100		14
SMC IPOH + VO		217		181
SIS + VO		140		19
South Quay Square		557		472
South Quay Square - VO		607		607
Belfield residential condo		403		236
Sunway Velocity TWO		253		146
Big Box Office		51		5
SMC Damansara		240		174
SW Flora		278		273
Renewable energy		12		5
Singapore				
Precast		693		430
External - New order 2023		13		13
Total		9,740		6,030
Orderbook burn rate (FY22, including internal)				3,011
Implied earnings visibility (years)				2.0

Source: Company data, Nomura research

Fig. 4: YTD 2023 orderbook replenishment

Project	Duration	Contract Sum (MYR mn)
Bidadari C17 - LPS	Dec-23	4
Precast - Watertanks	Various	9
Heliosel Solar PV System - Package L3	Dec-23	34
Heliosel Solar PV System - Package L2	Oct-23	11
Oxley Tower VO	Feb-24	9
RTS Link Package 1B and 5	Jun-25	605
South Quay Square mix development	Oct-25	607
Total		1,278

Source: Company data, Nomura research

Fig. 5: SunCon – changes to our estimates

MYR mn	Old		New		% change	
	FY23F	FY24F	FY23F	FY24F	FY23F	FY24F
Orderbook replenishment	1,800	1,800	2,000	2,000	11%	11%
External	800	800	1,000	1,000	25%	25%
Internal	700	700	700	700	0%	0%
Precast	300	300	300	300	0%	0%
Revenue	2,597	2,313	2,967	3,026	14%	31%
Adj PBT	192	176	196	210	2%	19%
PBT margins	7.4%	7.6%	6.6%	6.9%	(0.8 ppt)	(0.7 ppt)
Adj NPAT	144	134	147	157	2%	17%

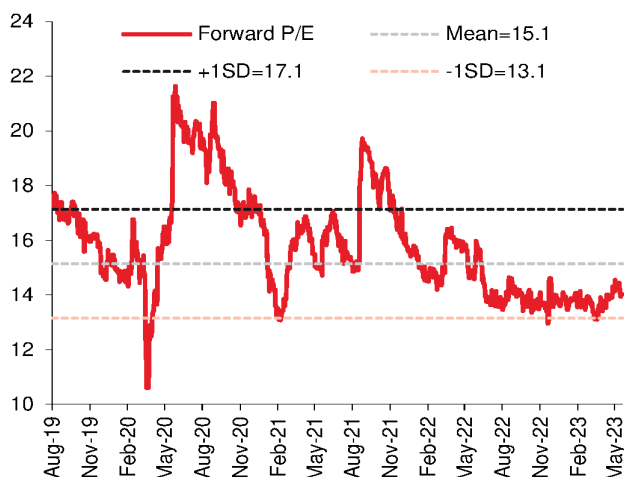
Source: Nomura estimates

Fig. 6: SunCon – Target price valuation methodology

	Dec-23
	FY23F
Normalised net profit (MYR mn)	147
FD number of shares outstanding (mn)	1,293
FD EPS (MYR/ sh)	0.11
Target FY23F P/E	18.0 x
Price target (MYR/ sh)	2.00

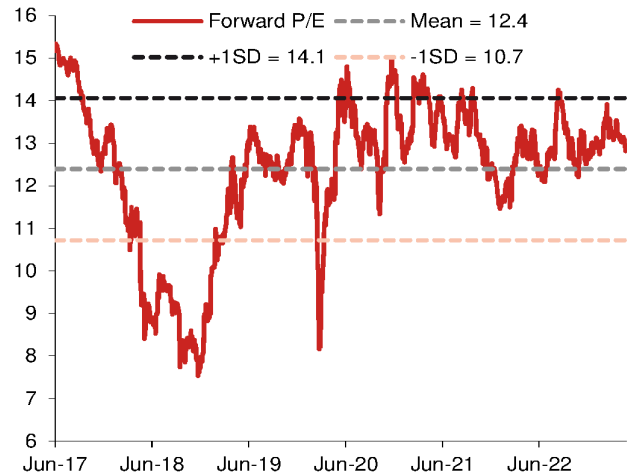
Source: Nomura estimates

Fig. 7: SunCon forward P/E (consensus)



Source: Bloomberg Finance L.P., Nomura research

Fig. 8: KLCON 12M forward P/E - consensus



Source: Bloomberg Finance L.P., Nomura research

Appendix A-1

Analyst Certification

I, Tushar Mohata, hereby certify (1) that the views expressed in this Research report accurately reflect my personal views about any or all of the subject securities or issuers referred to in this Research report, (2) no part of my compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this Research report and (3) no part of my compensation is tied to any specific investment banking transactions performed by Nomura Securities International, Inc., Nomura International plc or any other Nomura Group company.

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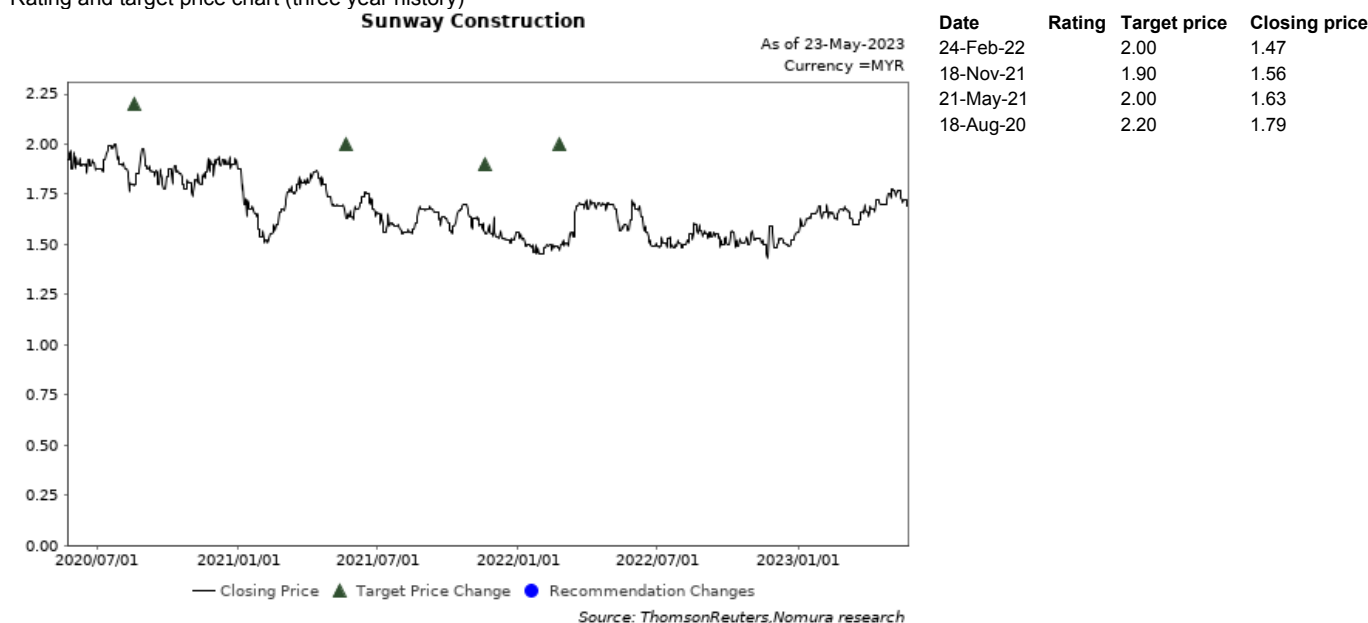
Materially mentioned issuers

Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
Sunway Construction	SCGB MK	MYR 1.69	23-May-2023	Buy	N/A	

Sunway Construction (SCGB MK)

MYR 1.69 (23-May-2023) Buy (Sector rating: N/A)

Rating and target price chart (three year history)



For explanation of ratings refer to the stock rating keys located after chart(s)

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 As at 31 March 2023.

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STOCKS

A rating of '**Buy**', indicates that the analyst expects the stock to outperform the Benchmark over the next 12 months. A rating of '**Neutral**', indicates that the analyst expects the stock to perform in line with the Benchmark over the next 12 months. A rating of '**Reduce**', indicates that the analyst expects the stock to underperform the Benchmark over the next 12 months. A rating of '**Suspended**', indicates that the rating, target price and estimates have been suspended temporarily to comply with applicable regulations and/or firm policies. Securities and/or companies that are labelled as '**Not rated**' or shown as '**No rating**' are not in regular research coverage. Investors should not expect continuing or additional information from Nomura relating to such securities and/or companies. Benchmarks are as follows: **United States/Europe/Asia ex-Japan**: please see valuation methodologies for explanations of relevant benchmarks for stocks, which can be accessed at: <http://go.nomuranow.com/research/globalresearchportal/pages/disclosures/disclosures.aspx>; **Global Emerging Markets (ex-Asia)**: MSCI Emerging Markets ex-Asia, unless otherwise stated in the valuation methodology; **Japan**: Russell/Nomura Large Cap.

SECTORS

A '**Bullish**' stance, indicates that the analyst expects the sector to outperform the Benchmark during the next 12 months. A '**Neutral**' stance, indicates that the analyst expects the sector to perform in line with the Benchmark during the next 12 months. A '**Bearish**' stance, indicates that the analyst expects the sector to underperform the Benchmark during the next 12 months. Sectors that are labelled as '**Not rated**' or shown as '**N/A**' are not assigned ratings. Benchmarks are as follows: **United States**: S&P 500; **Europe**: Dow Jones STOXX 600; **Global Emerging Markets (ex-Asia)**: MSCI Emerging Markets ex-Asia. **Japan/Asia ex-Japan**: Sector ratings are not assigned.

Target Price

A Target Price, if discussed, indicates the analyst's forecast for the share price with a 12-month time horizon, reflecting in part the analyst's estimates for the company's earnings. The achievement of any target price may be impeded by general market and macroeconomic trends, and by other risks related to the company or the market, and may not occur if the company's earnings differ from estimates.

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