

EQUITY: ENGINEERING & CONSTRUCTION

Catch your breath

Downgrade to Neutral as some future awards likely priced-in

Share price jumps on optimism about future awards

Sunway Construction's (SunCon) share price has jumped 36% YTD, vs the KLCI's 4%. Being the first Malaysian contractor to benefit from large data center (DC) project awards in late 2022, we believe the recent share price movement seems to suggest optimism that SunCon is likely to win one, or possibly more such projects in the near future. We have received investor questions asking how much higher its orderbook can go in such a scenario, and what to make of current valuations.

What jobs is SunCon in the running for?

At this juncture, there is no actual newsflow or company announcement on any job wins. Our 1-10-20 formula for DC construction capex (details inside) suggests orderbook opportunity ranging from MYR1.5bn+ for hyperscale DC (~200MW capacity) to <MYR500mn for non-hyperscale Klang Valley DCs. Our understanding is that SunCon is bidding for both smaller DCs in the Klang Valley, and hyperscale DCs in Johor. This is in addition to other large job opportunities such as the Song Hau 2 thermal power plant in Vietnam, and the CMC02 package for MRT Line 3.

Downgrade to Neutral, some future awards likely priced in

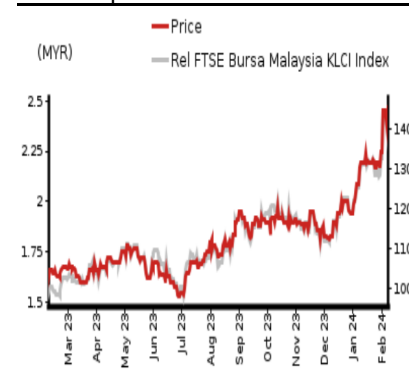
It is hard to assess how many of the above opportunities SunCon will be able to convert to firm awards. To build in this optimism, we revise estimates upwards. Our new orderbook replenishment assumptions are MYR3.5/2.5bn in FY24F/25F (previously MYR2/2bn). Our new FY24F/25F earnings is up 33%/46%. In our view, these revisions capture some upside from new DC opportunities. Note: we are currently not assuming the award of the Song Hau 2 power plant (where financial closure has been delayed several times) and MRT3 CMC02 package (where tenders have been delayed, and SunCon faces tough competition). SunCon's market cap-to-orderbook ratio as well as forward P/E are stretched, suggesting some future opportunities and earnings accretion are now priced in. We downgrade the stock to Neutral, on weaker risk-reward at current price levels. Our revised TP of MYR2.70 is based on 17x revised FY24F earnings, which is +1SD to its LT average (down from 18x previously to factor in the new +1SD level). This represents implied upside of 3%. We prefer Gamuda (GAM MK, Buy) in the sector. Upside risks to our view are: 1) SunCon winning multiple large hyperscale DC projects, 2) SunCon winning the MRT3 CMC02 package or the Song Hau 2 power plant achieving financial close. Downside risks to our view are: 1) delays / cancellations of projects or 2) weaker margins.

Year-end 31 Dec	FY22	FY23F		FY24F		FY25F	
Currency (MYR)	Actual	Old	New	Old	New	Old	New
Revenue (mn)	2,155	2,967	2,746	3,026	3,750	2,753	3,860
Reported net profit (mn)	135	147	137	157	208	163	238
Normalised net profit (mn)	135	147	137	157	208	163	238
FD normalised EPS	10.48c	11.34c	10.56c	12.14c	16.09c	12.58c	18.41c
FD norm. EPS growth (%)	20.1	8.2	0.8	7.0	52.3	3.6	14.4
FD normalised P/E (x)	25.1	-	24.9	-	16.3	-	14.3
EV/EBITDA (x)	16.4	-	16.4	-	11.2	-	9.9
Price/book (x)	4.6	-	4.2	-	3.7	-	3.3
Dividend yield (%)	2.1	-	2.2	-	3.4	-	3.8
ROE (%)	18.8	18.9	17.7	18.5	24.2	17.6	24.4
Net debt/equity (%)	net cash	46.4	47.1	34.8	35.5	23.1	21.6

Source: Company data, Nomura estimates

Rating	Neutral
Down from Buy	
Target price	MYR 2.70
Increased from MYR 2.00	
Closing price	MYR 2.63
8 February 2024	
Implied upside	+2.7%
Market Cap (USD mn)	713.5
ADT (USD mn)	0.6

Relative performance chart



Source: LSEG, Nomura

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Key data on Sunway Construction

Performance

(%)	1M	3M	12M		
Absolute (MYR)	21.2	39.2	59.4	M cap (USDmn)	713.5
Absolute (USD)	18.2	36.6	43.7	Free float (%)	35.4
Rel to FTSE Bursa Malaysia KLCI Index	20.0	35.3	56.5	3-mth ADT (USDmn)	0.6

Income statement (MYRmn)

Year-end 31 Dec	FY21	FY22	FY23F	FY24F	FY25F
Revenue	1,729	2,155	2,746	3,750	3,860
Cost of goods sold	-1,590	-1,969	-2,536	-3,435	-3,516
Gross profit	139	187	210	315	344
SG&A					
Employee share expense					
Operating profit	139	187	210	315	344
EBITDA	167	210	234	340	371
Depreciation	-27	-24	-24	-25	-27
Amortisation					
EBIT	139	187	210	315	344
Net interest expense	0	-4	-29	-39	-30
Associates & JCEs	13	2	2	2	2
Other income					
Earnings before tax	152	184	183	278	316
Income tax	-41	-45	-45	-69	-78
Net profit after tax	111	139	138	209	238
Minority interests	2	-4	-1	-1	0
Other items					
Preferred dividends					
Normalised NPAT	113	135	137	208	238
Extraordinary items	-17	0	0	0	0
Reported NPAT	95	135	137	208	238
Dividends	-68	-71	-75	-114	-131
Transfer to reserves	28	64	61	94	107

Valuations and ratios

Reported P/E (x)	35.6	25.1	24.9	16.3	14.3
Normalised P/E (x)	30.1	25.1	24.9	16.3	14.3
FD normalised P/E (x)	30.1	25.1	24.9	16.3	14.3
Dividend yield (%)	2.0	2.1	2.2	3.4	3.8
Price/cashflow (x)	14.2	-	-	19.6	13.6
Price/book (x)	4.9	4.6	4.2	3.7	3.3
EV/EBITDA (x)	19.8	16.4	16.4	11.2	9.9
EV/EBIT (x)	23.3	18.5	18.3	12.0	10.7
Gross margin (%)	8.1	8.7	7.6	8.4	8.9
EBITDA margin (%)	9.6	9.8	8.5	9.1	9.6
EBIT margin (%)	8.1	8.7	7.6	8.4	8.9
Net margin (%)	5.5	6.3	5.0	5.5	6.2
Effective tax rate (%)	27.3	24.6	24.6	24.7	24.7
Dividend payout (%)	71.0	52.5	55.0	55.0	55.0
ROE (%)	14.3	18.8	17.7	24.2	24.4
ROA (pretax %)	8.8	10.7	10.5	12.8	12.8

Growth (%)

Revenue	11.4	24.6	27.4	36.6	2.9
EBITDA	34.6	26.0	11.2	45.5	9.1
Normalised EPS	54.7	20.1	0.8	52.3	14.4
Normalised FDEPS	54.7	20.1	0.8	52.3	14.4

Source: Company data, Nomura estimates

Cashflow statement (MYRmn)

Year-end 31 Dec	FY21	FY22	FY23F	FY24F	FY25F
EBITDA	167	210	234	340	371
Change in working capital	125	-198	-155	-60	-13
Other operating cashflow	-54	-227	-374	-107	-108
Cashflow from operations	239	-215	-295	173	250
Capital expenditure	-35	-27	-25	-25	-25
Free cashflow	204	-242	-320	148	225
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	-320	148	225
Cash dividends	-52	-90	-70	-95	-123
Equity issue					
Debt issue	-65	239	300	0	0
Convertible debt issue					
Others	-6	-6	0	0	0
CF from financial acts	-122	143	230	-95	-123
Net cashflow	-101	393	-90	53	103
Beginning cash	200	99	492	402	455
Ending cash	99	492	402	455	558
Ending net debt	139	-11	379	326	223

Balance sheet (MYRmn)

As at 31 Dec	FY21	FY22	FY23F	FY24F	FY25F
Cash & equivalents	99	492	402	455	558
Marketable securities					
Accounts receivable	661	813	1,036	1,415	1,457
Inventories	46	53	58	78	80
Other current assets	209	279	279	279	279
Total current assets	1,015	1,637	1,775	2,228	2,374
LT investments	724	223	225	227	228
Fixed assets	125	108	109	108	107
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	2,676	3,131	3,276
Short-term debt	93	172	172	172	172
Accounts payable	891	886	958	1,298	1,328
Other current liabilities	8	45	45	45	45
Total current liabilities	992	1,103	1,175	1,515	1,546
Long-term debt	145	309	609	609	609
Convertible debt					
Other LT liabilities	10	3	3	3	3
Total liabilities	1,147	1,415	1,787	2,127	2,158
Minority interest	18	84	85	86	86
Preferred stock					
Common stock	259	259	259	259	259
Retained earnings	471	516	583	696	811
Proposed dividends					
Other equity and reserves	-30	-37	-37	-37	-37
Total shareholders' equity	699	737	804	917	1,033
Total equity & liabilities	1,864	2,236	2,676	3,131	3,276

Liquidity (x)

Current ratio	1.02	1.48	1.51	1.47	1.54
Interest cover	324.2	44.9	7.3	8.1	11.5

Leverage

Net debt/EBITDA (x)	0.83	net cash	1.62	0.96	0.60
Net debt/equity (%)	19.9	net cash	47.1	35.5	21.6

Per share

Reported EPS (MYR)	7.39c	10.48c	10.56c	16.09c	18.41c
Norm EPS (MYR)	8.73c	10.48c	10.56c	16.09c	18.41c
FD norm EPS (MYR)	8.73c	10.48c	10.56c	16.09c	18.41c
BVPS (MYR)	0.54	0.57	0.62	0.71	0.80
DPS (MYR)	0.05	0.05	0.06	0.09	0.10

Activity (days)

Days receivable	165.3	124.8	122.9	119.6	135.8
Days inventory	9.2	9.2	8.0	7.2	8.2
Days payable	210.2	164.8	132.7	120.2	136.3
Cash cycle	-35.8	-30.7	-1.8	6.7	7.7

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 17x on FY24F earnings estimate of MYR208mn for FY24F. We arrive at our TP of MYR2.70. The benchmark index for the stock is FTSE Bursa Malaysia KLCI Index.

Risks that may impede the achievement of the target price

Upside risks to our view are: 1) SunCon winning multiple large hyperscale DC projects, 2) SunCon winning the MRT3 CMC02 package or the Song Hau 2 power plant achieving financial close, and translating to SunCon's orderbook. Downside risk to our view are: 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.

Catch your breath

Share price jump backed by past successes in data center / warehouse theme

Sunway Construction's (SunCon) share price has jumped a significant 36% YTD, bringing the last 12-month returns to 59%. This comfortably exceeds KLCON/KLCI's 34%/3% returns over the past year. Investor optimism on this name is somewhat justified – 1) SunCon was the first Malaysian contractor to clinch a breakthrough in the lucrative hyperscale data center (DC) growth story, when they *won a MYR1.7bn contract* to build the JHB1X0 DC project in the Sedenak Tech Park (STeP) from Yellowwood Properties in December 2022, 2) the company also won a much smaller *MYR190mn DC contract* for the Kuok Group owned K2 Data Center, also planned in STeP, and 3) they won a *~MYR300mn warehouse contract* for the Japanese brand Daiso in Selangor. Overall, the company so far has been a frontline beneficiary of the “tectonic supply chain shift” theme in Asia, which has resulted in FDI flows in data centers and factories in Malaysia.

In the absence of newsflow, reasonable to assume that some future jobs are being priced in

While tenders and negotiations with more prospective clients are ongoing, there has been no major project announcement by the company in 2024. In that context, when looking at the 36% share price rise YTD, we think that current valuations are already pricing in one or more major contract wins for SunCon possibly coming soon. During previous investor meetings, the company mentioned that they are bidding for DC jobs, with awards expected by end-2023 / early-2024. After the share price rally, we have received investor questions asking how much higher its orderbook can go in case SunCon wins more data center jobs, and what to make of current valuations.

Data center capex primer – remember the 1 – 10 – 20 formula

Our analysis of the data center construction opportunity (see our Oct-2023 report *Multi-year, multi-billion data-center capex cycle*) suggests that the potential job sizes from DC range widely, depending on the capacity, and whether the DC is hyperscale or not. At the upper end, we have hyperscale DCs, where a ballpark estimate for capex is USD10mn per 1MW of capacity. However, construction orderbook opportunities to build the DC *shell*, which is within the scope of works contractors like SunCon can do, range up to just 20% of the capex, with the remaining 80% investment required going towards expensive equipment like servers. Using this 1MW – USD10mn – 20% formula (or, 1 – 10 – 20 formula), and assuming a hyperscale DC with 200MW capacity plans, the total investment required will therefore be USD2bn, with potential construction orderbook for SunCon of up to USD400mn (or ~MYR1.9bn). This is similar to the 200MW Yellowwood DC contract for SunCon in Dec-2022 which was worth MYR1.7bn. At the other end of the spectrum, non-hyperscale DC projects, such as those in the Klang Valley are smaller in size, ranging from a few MW to 50MW, and the orderbook potential is also smaller correspondingly.

What jobs is SunCon bidding for?

Our understanding is that SunCon is bidding for both smaller DCs in the Klang Valley, and hyperscale DCs in Johor. This is in addition to other large job opportunities, such as the Song Hau 2 thermal power plant in Vietnam, and the CMC02 package for MRT Line 3. The *Song Hau 2 power plant* can be worth an additional ~MYR6bn to SunCon, which holds a 60% stake in the project's EPC contractor, but the project is yet to achieve financial close. The *MRT3 CMC02 package* is also large, worth ~MYR10bn, and SunCon is likely to have a material stake in one of the consortia who have submitted tenders for it. SunCon also previously bid for semiconductor factory capex in Malaysia.

Downgrade to Neutral, some future opportunities priced in

It is hard to assess how many of the above opportunities SunCon will be able to convert to firm awards. We make some upward revisions to our estimates. In our revised base case, we raise new orderbook assumptions materially to MYR3.5/2.5bn in FY24F/25F from MYR2/2bn. In our view, this captures some upside from new DC opportunities. We are currently not assuming the award of the Song Hau 2 power plant (where financial close has been delayed several times) and MRT3 CMC02 package (where tenders have been delayed, and SunCon faces tough competition). Along with upward revision to margins due to a recovery of the precast segment, our FY24F/25F earnings are up 33%/46%. Our FY23F earnings, however, are cut 7% due to slow progress in the already won data center contract due to delay in receiving specifications from the end-client.

SunCon’s market cap-to-orderbook ratio as well as forward P/E are stretched, suggesting some future opportunities and earnings accretion is now priced in. We downgrade the stock to Neutral, on weaker risk-reward at current price levels. Our raised TP of MYR2.70 is based on 17x revised FY24F earnings, which is +1SD to its LT average (down from 18x previously to factor in new +1SD level). This represents upside of 3%.

Upside risks to our view are: 1) SunCon winning multiple large hyperscale DC projects, 2) SunCon winning the MRT3 CMC02 package or the Song Hau 2 power plant achieving financial close, and translating into SunCon’s orderbook. Downside risks to our view are: 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 cancellations or arbitration.

Fig. 1: SunCon: Changes to our estimates

MYR mn	Old			New			% change		
	FY23F	FY24F	FY25F	FY23F	FY24F	FY25F	FY23F	FY24F	FY25F
Orderbook replenishment	2,000	2,000	2,000	2,470	3,500	2,500	24%	75%	25%
External	1,000	1,000	1,000	1,320	2,500	1,500	32%	150%	50%
Internal	700	700	700	950	700	700	36%	0%	0%
Precast	300	300	300	200	300	300	(33%)	0%	0%
Revenue	2,967	3,026	2,753	2,746	3,750	3,860	(7%)	24%	40%
Adj PBT	196	210	216	183	278	316	(7%)	32%	46%
PBT margins	6.6%	6.9%	7.8%	6.7%	7.4%	8.2%	0.0 ppt	0.5 ppt	0.3 ppt
Adj NPAT	147	157	163	137	208	238	(7%)	33%	46%

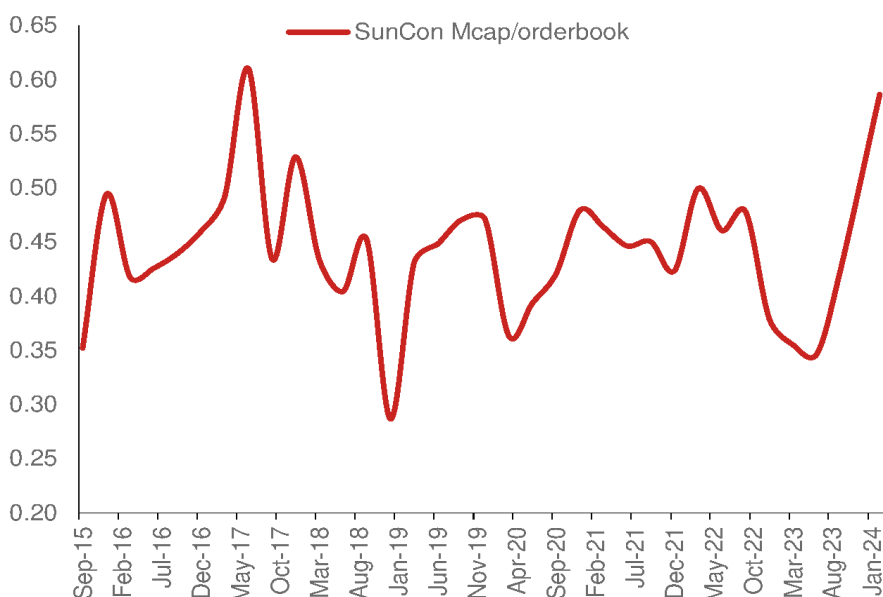
Source: Nomura estimates

Fig. 2: SunCon – Target price valuation methodology

	Dec-24 FY24F
Normalised net profit (MYR mn)	208
FD number of shares outstanding (mn)	1,293
FD EPS (MYR/ sh)	0.16
Target FY24F P/E	17.0 x
Price target (MYR/ sh)	2.70

Source: Nomura estimates

Fig. 3: SunCon: Market cap to orderbook



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

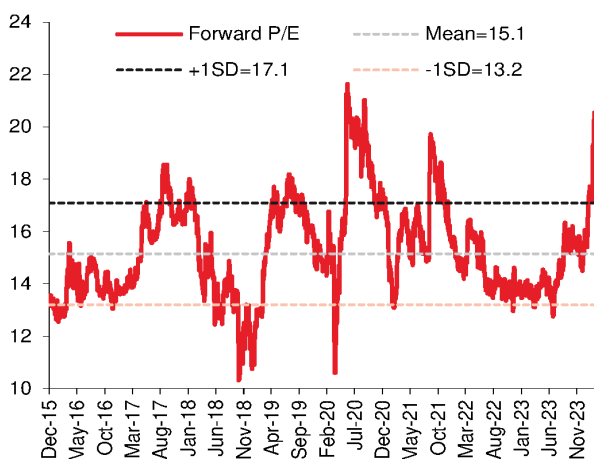
Fig. 4: SunCon’s outstanding orderbook

As of end-3Q23

MYR mn	Contract Sum		Outstanding order book	
Infrastructure/Piling				
LRT3: Package GS07-08	2,178	1,295	1,589	14
RTS Link Package 1B and 5		605		551
LRT3: GS06		191		35
Building				
Oxley Tower + VO		77		40
JHB1X0 - Data Centre		1,700		1,500
K2 Datacentre		190		190
Daiso		298		298
India				
Thorapalli Agraharam - Jittandahalli		508		255
Meensurutti - Chidambarm 32km		315		63
Renewable energy				
Solar - External		35		8
Solar - Internal		12		4
Lss4 Gopeng		200		88
Lss4 Sharp Ventures		185		88
South Quay Square Dcs		35		29
Cgpp - Green*		46		46
New Order 2023 - External		45		38
Internal				
SMC 4 + VO		612		62
Sunway Belfield		412		162
Sunway Velocity 2		352		7
South Quay Square - Superstructure		756		357
South Quay Square - Superstructure (VO)		607		607
Sw Carnival Mall - Refurbishment		253		239
Sunway Velocity 2B		253		91
Smc Damansara		240		126
Smc Ipoh + VO		217		141
SW International School (SIS)		140		6
Sunway Velocity 3C4		100		5
Big Box Office		51		5
SW Flora		278		250
Singapore				
Precast		613		310
External - New order 2023		180		177
Total		10,798		5,789
Orderbook burn rate (FY22, including internal)				3,011
Implied earnings visibility (years)				1.9

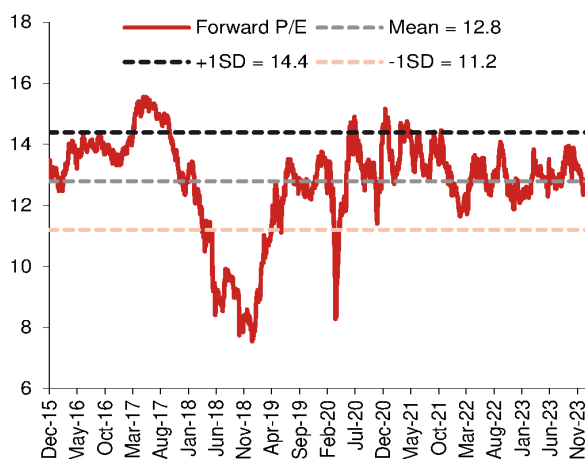
Source: Company data, Nomura research

Fig. 5: SunCon forward P/E (consensus)



Source: Bloomberg Finance L.P., Nomura research

Fig. 6: 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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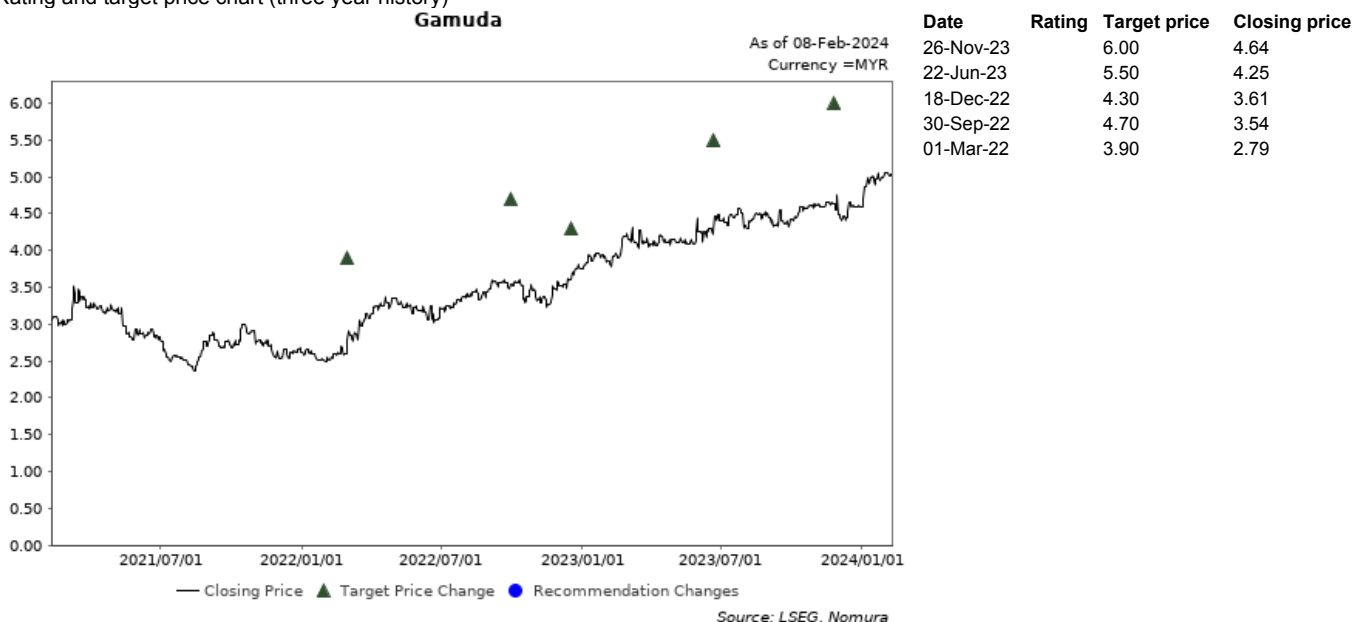
Materially mentioned issuers

Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
Gamuda	GAM MK	MYR 5.04	08-Feb-2024	Buy	N/A	
Sunway Construction	SCGB MK	MYR 2.63	08-Feb-2024	Neutral	N/A	

Gamuda (GAM MK)

MYR 5.04 (08-Feb-2024) 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)

Valuation Methodology We value Gamuda on a target P/E of 15x, and arrive at our target price of MYR 6.00 using our fully diluted EPS forecast of 40sen for CY24F. The benchmark index for the stock is the KLCI index.

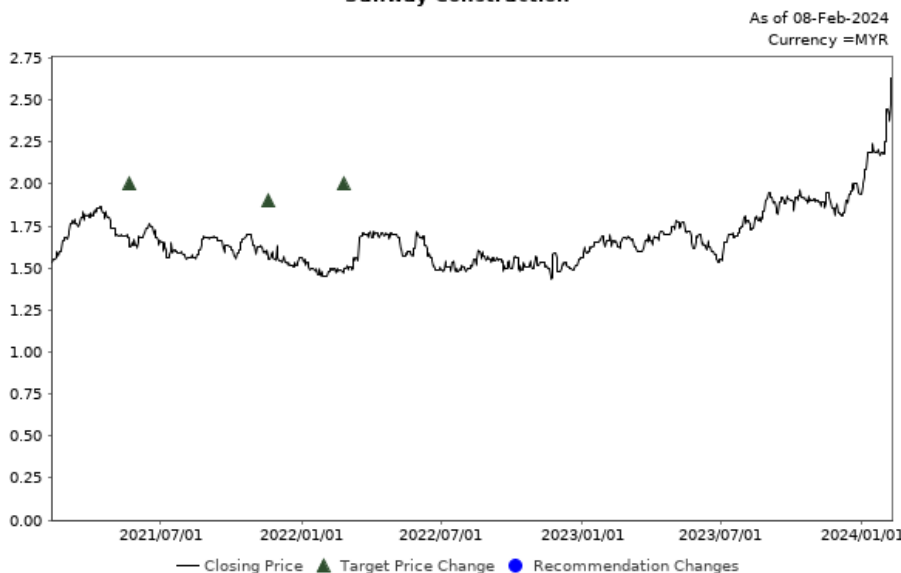
Risks that may impede the achievement of the target price Downside risks include: 1) unexpected project cancellations or scope reductions; 2) slowdown in the property market in Malaysia, Vietnam, UK or Singapore; 3) balance sheet risks due to high receivables and cash intensive property business; 4) prolonged period of slow project awards; 5) execution and margin risk in projects.

Sunway Construction (SCGB MK)

MYR 2.63 (08-Feb-2024) Neutral (Sector rating: N/A)

Rating and target price chart (three year history)

Sunway Construction



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

Valuation Methodology We value SunCon at a target P/E of 17x on FY24F earnings estimate of MYR208mn for FY24F. We arrive at our TP of MYR2.70. The benchmark index for the stock is FTSE Bursa Malaysia KLCI Index.

Risks that may impede the achievement of the target price Upside risks to our view are: 1) SunCon winning multiple large hyperscale DC projects, 2) SunCon winning the MRT3 CMC02 package or the Song Hau 2 power plant achieving financial close, and translating to SunCon’s orderbook. Downside risk to our view are: 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.

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 As at 31 December 2023.

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STOCKS

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