

11 August 2021

Construction & Engineering | Construction

Sunway Construction (SCGB MK)

Buy (Maintained)

Weaker 2Q May Not Come As a Surprise; BUY

Target Price (Return): MYR1.81 (+16%)
 Price: MYR1.56
 Market Cap: USD476m
 Avg Daily Turnover (MYR/USD): 0.28m/0.07m

- **Maintain BUY, new MYR1.81 TP from MYR1.94, 16% upside and c.2% yield.** The outcome of Sunway Construction's tenders will likely be known later this year, as signalled by management's confidence about hitting the MYR2bn target. With the combined new contracts worth MYR462m already secured, potential new awards will serve as a positive catalyst in 2H21F. Very few local contractors enjoy this positive outlook, as they are burdened by COVID-19 restrictions. We believe SCGB's current valuation – at a 13% discount to its 5-year mean – is attractive.
- **Owing to Phase 1 of the National Recovery Plan (NRP),** we believe SCGB will report a weaker QoQ performance in 2Q21. This is following a period of low productivity during the quarter, as the group was only allowed to run its operations at 60% maximum capacity. On that note, we believe it will likely report a 2Q21F net profit of MYR22-25m, implying a 26% decline QoQ, but >100% YoY growth. The slowdown was evidenced by data from the Department of Statistics Malaysia this week. We understand that the total value of construction work done (in Malaysia) in 2Q21 was recorded at only MYR28bn – a 10% QoQ drop from 1Q21's MYR31bn. Noting that most construction projects remain under Phase 1 of the NRP until today, the slowdown seen in 2Q21 will likely extend into 3Q21 (Jul-Sep 2021).
- **Full reopening of construction sector still possible.** Our base case scenario suggests that it can happen as early as 4Q21. Consequently, an early recovery would be likely during the period, allowing SCGB to meaningfully ramp up productivity from a low base. However, this should only come after two quarters of sluggish activities, as a result of Phase 1 of the NRP restrictions that have been extended until today (in Kuala Lumpur and Selangor). With vaccination rates reaching higher levels daily, we believe this will gradually present the possibility of easing restrictions on construction activities in the near term.
- **Our TP is lowered after adjusting FY21F-23F earnings by -12%, -7% and -1%.** The adjustments are mainly on the prolonged operational constraints of Phase 1 of the NRP. SCGB's activities were negatively impacted when EMCO was imposed for two weeks in Selangor and several areas in Kuala Lumpur. This is in addition to the pending approvals for certain construction projects, which hinder it from further improving its progress billings. At this juncture, we maintain our 16.5x FY22F P/E (5-year mean). Despite our medium-term optimism, we stay conservative at this point as we recognise the lingering COVID-19 risks.
- **Downside risks:** Failure to secure new contracts, a prolonged downturn in the retail and property markets, and longer-than-expected delays in the rollout of mega infrastructure projects.

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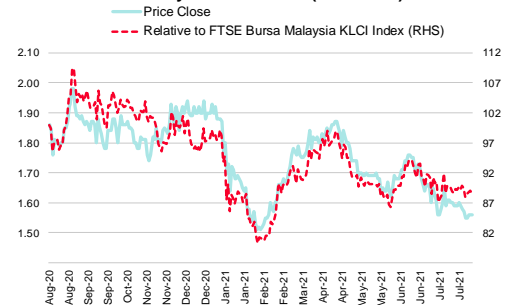
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(17.0)	0.0	(7.7)	2.6	(17.0)
Relative	(9.0)	1.6	(2.0)	8.2	(11.8)
52-wk Price low/high (MYR)				1.51	1.98

Sunway Construction (SCGB MK)



Source: Bloomberg

Overall ESG Score: 3.0 (out of 4) E: Good

Efforts are under way to reduce its environmental footprint. This includes improving energy efficiency, using resources responsibly, and reducing waste. Through the recycling and reuse of hydraulic oil, SCGB recycled a total of 12,787 litres of hydraulic oil in 2019. The group also plans 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 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 to uplift employee relations.

G: Excellent

57% of its board members are independent, with full disclosure on director remuneration including salaries and bonuses. The group has an in-house investor relations team. Accessibility to investor relations is excellent, and the team mostly helps to deal with investor 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	1,716	2,250	2,348
Recurring net profit (MYRm)	124	92	92	141	152
Recurring net profit growth (%)	(15.5)	(25.9)	0.0	53.1	8.2
Recurring P/E (x)	16.25	21.92	21.92	14.31	13.23
P/B (x)	3.2	3.2	3.0	2.7	2.4
P/CF (x)	10.39	9.57	50.50	14.68	9.50
Dividend Yield (%)	4.0	2.6	2.3	3.5	3.8
EV/EBITDA (x)	8.69	13.15	10.79	7.15	6.28
Return on average equity (%)	21.3	11.6	14.0	19.6	19.3
Net debt to equity (%)	net cash	15.8	22.9	19.2	7.7

Source: Company data, RHB

Financial Exhibits

Asia	Financial summary (MYR)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
Malaysia	Recurring EPS	0.10	0.07	0.07	0.11	0.12
Construction & Engineering	DPS	0.06	0.04	0.04	0.05	0.06
Sunway Construction	BVPS	0.48	0.49	0.53	0.58	0.64
SCGB MK	Return on average equity (%)	21.3	11.6	14.0	19.6	19.3
Buy						
	Valuation metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Recurring P/E (x)	16.25	21.92	21.92	14.31	13.23
	P/B (x)	3.2	3.2	3.0	2.7	2.4
	FCF Yield (%)	9.2	10.3	(0.5)	4.1	7.8
	Dividend Yield (%)	4.0	2.6	2.3	3.5	3.8
	EV/EBITDA (x)	8.69	13.15	10.79	7.15	6.28
	EV/EBIT (x)	11.17	18.01	13.99	9.34	8.27
	Income statement (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Total turnover	1,769	1,553	1,716	2,250	2,348
	Gross profit	378	270	320	406	425
	EBITDA	181	124	156	234	254
	Depreciation and amortisation	(40)	(33)	(36)	(55)	(61)
	Operating profit	141	91	121	179	193
	Net interest	11	1	(9)	(8)	(7)
	Pre-tax profit	158	102	116	177	192
	Taxation	(27)	(28)	(24)	(36)	(39)
	Reported net profit	129	73	92	141	152
	Recurring net profit	124	92	92	141	152
	Cash flow (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Change in working capital	33	104	(88)	(58)	(1)
	Cash flow from operations	194	211	40	137	212
	Capex	(8)	(3)	(50)	(55)	(55)
	Cash flow from investing activities	(356)	(173)	(50)	(55)	(55)
	Dividends paid	(91)	(62)	(46)	(70)	(76)
	Cash flow from financing activities	19	(147)	96	(10)	(16)
	Cash at beginning of period	485	615	200	204	276
	Net change in cash	(142)	(110)	86	72	141
	Ending balance cash	351	505	286	276	417
	Balance sheet (MYRm)	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Total cash and equivalents	787	200	204	276	417
	Tangible fixed assets	139	107	122	122	116
	Total investments	49	489	489	489	489
	Total assets	2,002	1,906	1,794	2,106	2,255
	Short-term debt	233	234	284	334	384
	Total long-term debt	62	67	77	87	97
	Total liabilities	1,280	1,267	1,110	1,351	1,424
	Total equity	722	639	685	755	831
	Total liabilities & equity	2,002	1,906	1,794	2,106	2,255
	Key metrics	Dec-19	Dec-20	Dec-21F	Dec-22F	Dec-23F
	Revenue growth (%)	(21.6)	(12.2)	10.5	31.1	4.4
	Recurrent EPS growth (%)	(15.5)	(25.9)	0.0	53.1	8.2
	Gross margin (%)	21.4	17.4	18.6	18.0	18.1
	Operating EBITDA margin (%)	10.2	8.0	9.1	10.4	10.8
	Net profit margin (%)	7.3	4.7	5.4	6.3	6.5
	Dividend payout ratio (%)	61.6	70.9	50.0	50.0	50.0
	Capex/sales (%)	0.5	0.2	2.9	2.4	2.3
	Interest cover (x)	10.7	13.0	8.1	11.5	10.7

Source: Company data, RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2021-06-29	Buy	1.94	1.64
2021-05-21	Buy	2.03	1.63
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

Source: RHB, Bloomberg

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