

3 April 2018

Construction & Engineering | Engineering & Construction

Sunway Construction Group

Buy (Maintained)

Time To Get Back In The Sun

Target Price:	MYR2.50
Price:	MYR2.06
Market Cap:	USD689m
Bloomberg Ticker:	SCGB MK

We believe the recent sell-down in Sunway Construction presents investors with an opportunity to accumulate shares in the company. Having secured MYR0.5bn worth of jobs in 3M18, the company remains on track to hit its internal target of MYR1.5-2bn worth of new jobs in 2018. We are slightly more optimistic, forecasting a MYR2.2bn orderbook replenishment rate for FY18, as we see good scope for new job wins in all three key segments – buildings, projects from its parent and infrastructure projects. The company remains one of the frontrunners to clinch the PDP role for the HSR, along with its partners. Maintain BUY with a lower TP of MYR2.50 (from MYR2.70, 21% upside).

Share Data

Avg Daily Turnover (MYR/USD)	3.83m/0.98m
52-wk Price low/high (MYR)	1.76 - 2.624
Free Float (%)	35
Shares outstanding (m)	1,293
Estimated Return	21%

Shareholders (%)

Sunway	55.4
Employees Provident Fund	5.6
Norges	2.1

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(17.9)	(11.6)	(16.3)	(10.1)	17.0
Relative	(21.6)	(12.0)	(20.8)	(16.3)	9.9

Source: Bloomberg

Correction overdone. After closing 2017 on a high note – at an all-time high of MYR2.51, Sunway Construction succumbed to profit-taking, bringing its share price down to the MYR2.05-level, a decline of 22%. We opine that the sell-off could be overdone, with no negative developments made known to us during a recent meeting with management. Quite the opposite, we believe it is a good opportunity for investors to accumulate at a more palatable level – 13.4x rolling 12-month forward earnings, 1SD below its 5-year mean.

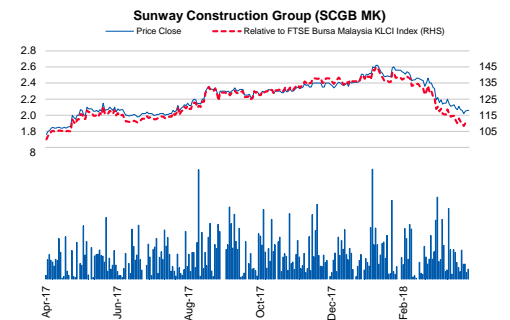
Won MYR0.5bn worth of jobs in 3M18. The management of Sunway Construction guided for a FY18 orderbook replenishment target of MYR1.5-2bn. So far, it has already secured MYR456m worth of new jobs from its parent, Sunway – which replenishes its internal job orderbook, of which projects are mostly at advanced stages.

Plenty of job opportunities remain. Sunway Construction has tendered for several jobs within the buildings segment, specifically for the mid- to high-end office and mixed property developments, located within the Klang Valley, which could add MYR600-900m worth of new jobs. Its parent, Sunway, on the other hand, plans to launch MYR1.4bn worth of new projects in 2018, up from MYR1bn in 2017, which provides Sunway Construction with further opportunities. In particular, it is eyeing residential projects in the mid- to high-end segment and medical centre projects. For the infrastructure space, Sunway Construction has pre-qualified for the East Coast Rail Link (ECRL) project.

Key downside risks include fewer-than-anticipated job wins, weaker-than-expected margins and possible cost overruns.

Maintain BUY. We adjust our FY18 earnings forecast down by 10%, factoring in lower progress billings for certain key projects. Maintain BUY, with a lower TP of MYR2.50. The appointment of the high-speed rail (HSR) project delivery partner (PDP) is imminent, with Sunway Construction as one of the frontrunners, in our view.

In our estimate, winning the PDP would boost the company's fair value by MYR0.30 to MYR2.80. Sunway Construction's current outstanding orderbook stands at MYR6.6bn, equivalent to 3.4x its FY17 construction revenue. It receives strong backing from its parent company, and maintains a high forecasted 3-year average ROE of 33%.



Source: Bloomberg

Forecasts and Valuations	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
Total turnover (MYRm)	1,917	1,789	2,076	2,625	3,083
Reported net profit (MYRm)	127	124	138	181	221
Recurring net profit (MYRm)	127	124	138	181	221
Recurring net profit growth (%)	11.4	(2.9)	11.7	30.9	22.1
Recurring EPS (MYR)	0.10	0.10	0.11	0.14	0.17
DPS (MYR)	0.04	0.05	0.07	0.08	0.09
Recurring P/E (x)	20.9	21.6	19.3	14.7	12.1
P/B (x)	5.90	5.40	5.18	4.54	3.95
P/CF (x)	33.5	na	17.8	8.0	9.4
Dividend Yield (%)	1.9	2.4	3.4	3.9	4.1
EV/EBITDA (x)	13.6	12.4	11.4	7.6	6.1
Return on average equity (%)	32.4	26.2	27.4	32.8	35.0
Net debt to equity	net cash	net cash	net cash	net cash	net cash
Our vs consensus EPS (adjusted) (%)				6.6	

Source: Company data, RHB

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Financial Exhibits

Financial model updated on : 2018-03-29

Asia	Financial summary	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
Malaysia	Recurring EPS (MYR)	0.10	0.10	0.11	0.14	0.17
Construction & Engineering	EPS (MYR)	0.10	0.10	0.11	0.14	0.17
Sunway Construction Group	DPS (MYR)	0.04	0.05	0.07	0.08	0.09
Bloomberg SCGB MK	BVPS (MYR)	0.35	0.38	0.40	0.45	0.52
Buy	Weighted avg adjusted shares (m)	1,293	1,293	1,293	1,293	1,293
Valuation basis	Valuation metrics	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
We value the company based on FY18F ex-cash P/E of 16x, the higher end of our benchmark upcycle 1-year forward target P/E for mid-cap construction stocks. Sunway Construction's net cash position allows it to gear up for more jobs moving forward.	Recurring P/E (x)	20.9	21.6	19.3	14.7	12.1
	P/E (x)	20.9	21.6	19.3	14.7	12.1
	P/B (x)	5.90	5.40	5.18	4.54	3.95
	FCF Yield (%)	1.5	(7.4)	3.6	11.3	9.8
	Dividend Yield (%)	1.9	2.4	3.4	3.9	4.1
	EV/EBITDA (x)	13.6	12.4	11.4	7.6	6.1
	EV/EBIT (x)	17.7	15.7	14.0	9.3	7.2
Key drivers	Income statement (MYRm)	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
Sunway Construction's earnings are strongly backed by:	Total turnover	1,917	1,789	2,076	2,625	3,083
i. An outstanding order backlog of MYR6.8bn, of which >90% is from construction that may keep the firm busy for next three years;	Gross profit	400	401	435	612	726
ii. Recurring orders from its parent company and key GLC clients;	EBITDA	177	188	202	276	321
iii. A highly profitable precast operation in Singapore.	Depreciation and amortisation	(41)	(39)	(38)	(49)	(48)
	Operating profit	136	149	165	226	273
	Net interest	5	4	7	1	2
	Income from associates & JVs	(0)	1	2	0	0
	Pre-tax profit	141	154	174	227	276
	Taxation	(13)	(30)	(36)	(47)	(56)
	Minority interests	(1)	(0)	0	0	1
	Recurring net profit	127	124	138	181	221
Key risks	Cash flow (MYRm)	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
Upside risks include better-than-expected margins at the construction segment and new job wins coming in ahead of our estimates while downside risks include possible cost overruns and higher material cost.	Change in working capital	28	(72)	(25)	102	16
	Cash flow from operations	79	(177)	150	331	282
	Capex	(39)	(19)	(55)	(30)	(20)
	Cash flow from investing activities	(65)	79	35	(30)	(20)
	Proceeds from issue of shares	0	0	0	0	0
	Dividends paid	(70)	(84)	(71)	(108)	(131)
	Cash flow from financing activities	(68)	(84)	(74)	(128)	(149)
	Cash at beginning of period	292	390	466	487	676
	Net change in cash	(53)	(183)	110	173	114
	Ending balance cash	234	208	575	661	790
Company Profile	Balance sheet (MYRm)	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
Sunway Construction is one of the largest construction companies in Malaysia. Apart from civil & infrastructure construction services, the company also provides the more specialised: i) foundation & geotechnical engineering services, and ii) mechanical, electrical & plumbing (MEP) services. In addition, it runs a highly profitable precast concrete products manufacturing operation in Malaysia and Singapore. Aside from fulfilling local requirement, hose concrete products are supplying largely to Housing & Development Board (HDB) projects in the island republic.	Total cash and equivalents	390	466	487	676	788
	Tangible fixed assets	163	134	97	77	49
	Intangible assets	4	4	4	4	4
	Total investments	0	0	0	0	0
	Total other assets	14	12	2	2	2
	Total assets	1,515	1,567	1,831	2,059	2,365
	Short-term debt	137	137	135	115	95
	Other liabilities	0	0	(16)	0	0
	Total liabilities	1,063	1,073	1,316	1,471	1,690
	Shareholders' equity	451	493	515	587	674
	Minority interests	1	1	1	1	1
	Total equity	452	494	516	588	675
	Net debt	(254)	(329)	(353)	(562)	(693)
	Total liabilities & equity	1,515	1,567	1,831	2,059	2,365
	Key metrics	Dec-15	Dec-16	Dec-17	Dec-18F	Dec-19F
	Revenue growth (%)	1.9	(6.7)	16.1	26.4	17.4
	Recurrent EPS growth (%)	11.4	(2.9)	11.7	30.9	22.1
	Gross margin (%)	20.9	22.4	21.0	23.3	23.5
	Operating EBITDA margin (%)	9.2	10.5	9.7	10.5	10.4
	Net profit margin (%)	6.6	6.9	6.6	6.9	7.2
	Dividend payout ratio (%)	40.7	52.3	65.6	60.0	59.5
	Capex/sales (%)	2.0	1.1	2.6	1.1	0.6
	Interest cover (x)	38.9	24.5	27.1	60.5	87.0

Source: Company data, RHB

Peaks and valleys

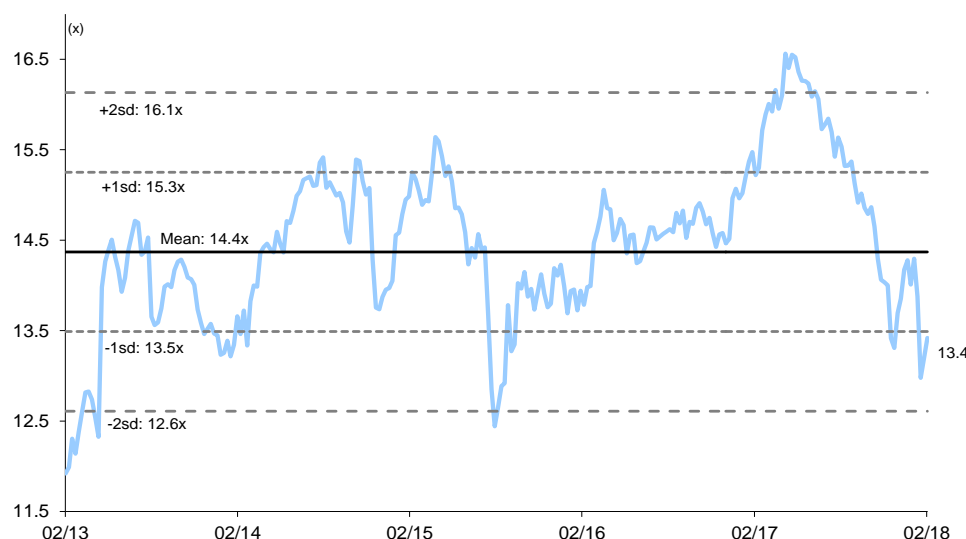
Sunway Construction concluded 2017 on a high note, closing at an all-time high of MYR2.51 – capping a good run in its share price, which rose 48% from the start of 2017. Its stellar share price performance continued briefly into 2018, reaching an intraday peak of MYR2.64 in January – just 2% shy of our MYR2.70 TP. Shortly thereafter, profit-taking ensued, bringing its share price down to the MYR2.05-level, a decline of 22%.

In our opinion, the sell-off could have emanated in part due to its FY17 results released in late-February that missed estimates, and market participants adopting a more risk-off stance favouring more defensive stocks.

We opine that the sell-off could be overdone, with no negative developments made known to us during a recent meeting with management. In fact, prospective investors are now presented with an opportunity to participate in Sunway Construction's robust growth prospects, with a 3-year CAGR estimated at 19% and valuations at a more palatable level – 13.4x rolling 12-month forward earnings, 1SD below its 5-year mean.

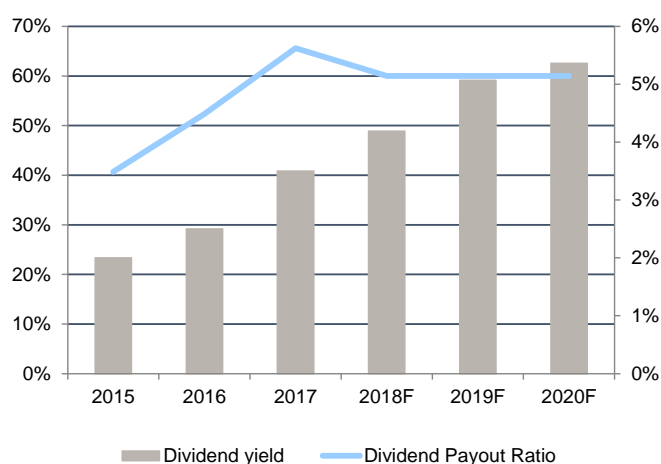
Downside risk, meanwhile, could be limited in our view, with an estimated dividend yield for FY18 at 3.9% based on a 60% payout ratio (the average payout ratio between FY16 and FY17). Share buybacks, on the other hand, were initiated by the company at MYR1.98 in mid-2017 – to the tune of 1.3m shares, which could serve as a support level.

Figure 1: Sunway Construction's 5-year average rolling 12-month forward earnings



Source: Bloomberg, RHB

Figure 2: Dividend payout ratio and yields



Source: Company data, RHB

Figure 3: Share repurchases in mid-2017 (MYRm)

Announcement date	Shares repurchased	Average Price	Total consideration
20/6/2017	280,000	1.98	554,417
21/6/2017	374,000	1.98	740,800
29/6/2017	654,000	1.98	1,295,217
Total	1,308,000		2,590,435

Source: Company data, RHB

MYR1.5-2bn orderbook replenishment target achievable

Sunway Construction's management guided for a FY18 orderbook replenishment target of MYR1.5-2bn, having secured MYR456m worth of new jobs thus far in 2018. Its recent job wins (Sunway Carnival 2 and Sunway Bayou) comprise of awards by its parent company, Sunway (SWB MK, NEUTRAL, TP: MYR4.33), which we view positively, as the majority of projects on hand awarded by its parent are reaching their tail-end, with the exception of only two projects – Sunway Medical Centre 4 and Sunway Serene Service Residences.

Figure 4: Sunway Construction's outstanding orderbook as of Dec 2017

Infrastructure:	Outstanding	Progress
MRT V201 + S201 (Sg Buloh - Persiaran Dagang)	871.0	28%
MRT V201 - Advance Works	19.0	98%
SUKE + DASH (Bore Piling)	21.0	98%
BBCC (Bore Piling)	78.0	94%
Mega Capital	0.0	100%
LRT3: Package GS07-08	2,150.0	1%
Infrastructure sub-total	3,139.0	
Building:		
Putrajaya Parcel F	707.0	56%
KLCC (NEC + Package 2 & 2a)	98.0	92%
HUKM (MEP Works)	45.0	96%
International School of Kuala Lumpur	133.0	89%
Gas District Cooling (Plant 1)	102.0	92%
PPA1M project in Kota Bharu	540.0	55%
Warehouse in Shah Alam	70.0	94%
Others	6.0	100%
Building sub-total	1,701.0	
Internal:		
Sunway Velocity Hotel + Office	3.0	100%
Sunway Velocity Medical Centre	128.0	89%
Sunway Medical Centre 4 (2 towers)	383.0	68%
Sunway Iskandar - Citrine Service Apartments	12.0	99%
Sunway Geo Retail Shops & Flexi Suites Phase 2	19.0	98%
Sunway Iskandar - Emerald Residences	32.0	97%
Sunway Iskandar - 88 units shoplots	13.0	99%
Sunway Iskandar - Retail Complex/Big Box	70.0	94%
Sunway Serene - Serviced Residences	426.0	65%
Others	3.0	
Internal sub-total	1,089.0	
Grand Total	5,929.0	
Precast	207	

Source: Company data, RHB

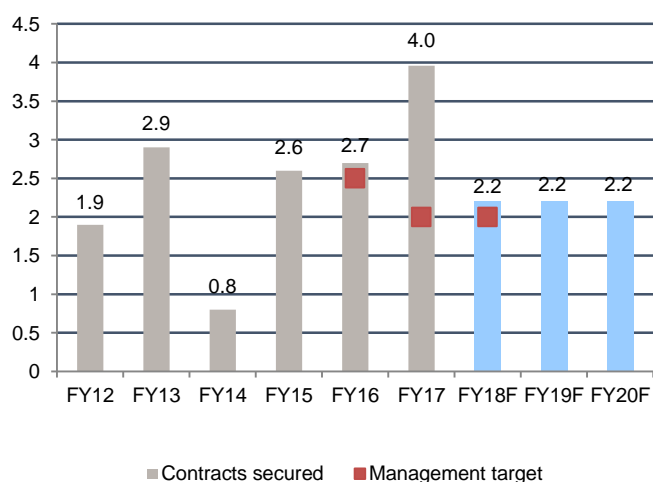
We understand that Sunway Construction has tendered for several jobs within the buildings segment, specifically for the mid- to high-end office and mixed property developments located within the Klang Valley. This segment of projects, if successful, could add between MYR600-900m worth of new jobs to Sunway Construction's orderbook, in our view.

Meanwhile, we observe that parent company, Sunway, has planned for a higher value of new property launches in 2018 with a total GDV of MYR1.4bn – compared to MYR1bn in 2017. We opine that Sunway Construction stands to benefit from the mid- to high-end property projects such as the MYR320m GDV Sunway Velocity 2. In addition, Sunway acquired a 4.53-acre piece of land at Jalan Belfield in Kuala Lumpur in 2017, with a planned GDV of MYR1.1bn. In its announcement on Bursa Malaysia, Sunway stated that it could begin launching the project in 2H18, likely to be in phases, in our view. The healthcare space, meanwhile, could see Sunway opening tenders for one or two of its pipeline of five planned medical centres. In total, we estimate that MYR600-700m worth of job opportunities could emerge from its parent.

Within the infrastructure space, we understand that Sunway Construction was among the contractors that have pre-qualified for the MYR55bn ECRL project. According to the project owner, Malaysia Rail Link (MRL), the tender for up to 30% of infrastructure work packages could commence in April. We believe that Sunway Construction could compete for piling related works with its in-house piling specialist (Sunway Geotechnics), especially for underground portions, which have higher substructure work requirements. The ECRL project has tunnels comprising of 39.1km of the alignment, with the 16.3km Bentong to Gombak tunnel being the longest.

We assess that there is a reasonable chance for Sunway Construction of exceeding its MYR1.5-MYR2bn target. Hence, we are forecasting a FY18 orderbook replenishment of MYR2.2bn – 10% higher than the upper bound of management's target. Overall tenderbook, meanwhile, stood at MYR2-3bn as of Dec 2017.

Figure 5: Annual orderbook wins (MYRbn)



Source: Company data, RHB

Figure 6: Sunway's 2018 new launches

Klang Valley	GDV
Sunway Bayou @ South Quay Condominiums	550
Sunway Velocity 2 Service Apartments	320
Sunway Wangsa Maju Service Apartments	220
Total Klang Valley	1,090
Outside Klang Valley	
Sunway Iskandar Citrine Lakehomes Phase 2	80
Sunway Onsen Suites @ Lost World Tambun	135
Sunway City Ipoh Townhouses	90
Sunway Wellesley @ Bukit Mertajam Shophouses	25
Total Non-Klang Valley	330
Total Malaysia	1,420

Source: Company data, RHB

Figure 7: Sunway's pipeline of medical centres

No	Planned Medical Centres	Beds	Estimated Completion
1	Sunway Medical Centre Seberang Jaya, Penang	180	2020
2	Sunway Medical Centre Damansara, Selangor	250	2022
3	Sunway Medical Centre Ipoh, Perak	200	2023
4	Sunway Medical Centre Iskandar, Johor	N/A	N/A
5	Sunway Medical Centre Penang Island	N/A	N/A

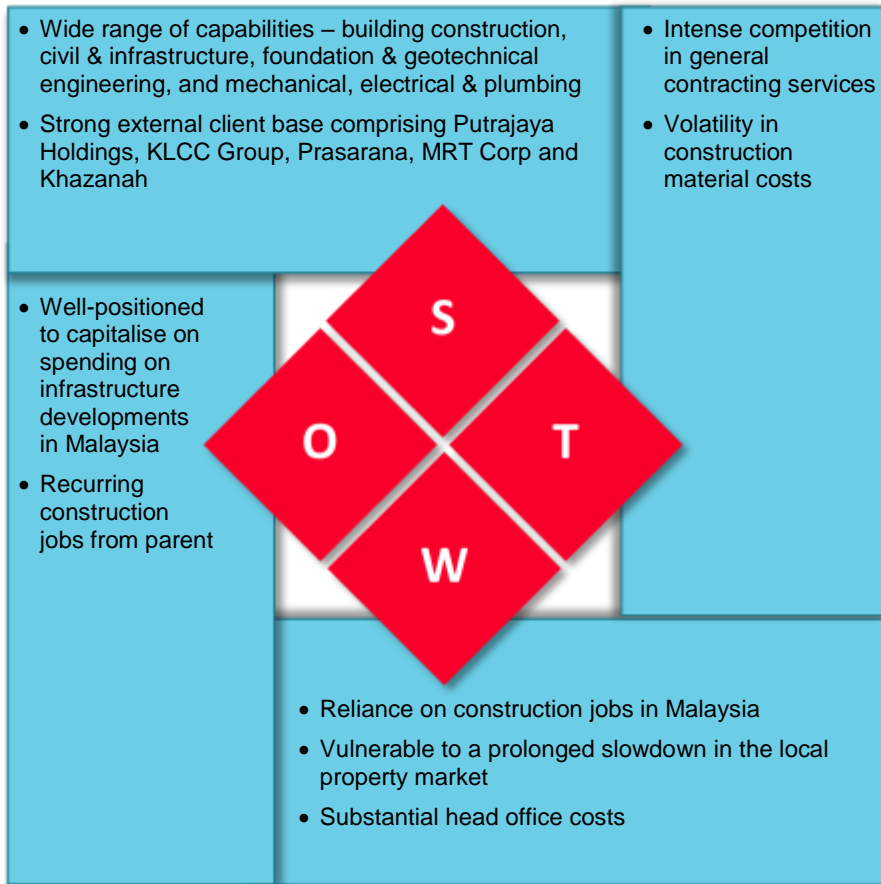
Source: Bloomberg, RHB

Maintain BUY

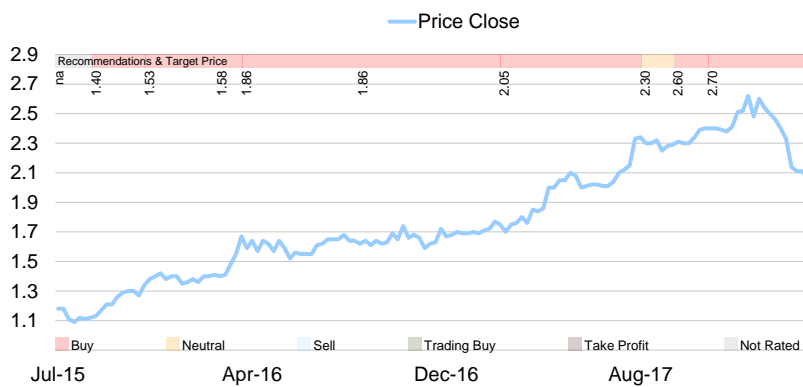
We are lower our FY18 earnings estimate by 10% to account for slower progress billings for two of Sunway Construction's larger outstanding projects – namely the LRT3 Package GS07-08 and Putrajaya Parcel F. This is due to delays in site handover for the former and changes in project design for the latter. Correspondingly, our ex-cash target price based on FY18F P/E multiple of 16x is lowered by 7.5% to MYR2.50.

Despite the earnings cut, we remain upbeat on the company's prospects, as it secured almost MYR0.5bn worth of jobs in 3M18. Meanwhile, the appointment of the HSR PDP is imminent – which, in our estimate, would boost the company's fair value by MYR0.30 to MYR2.80. In addition, Sunway Construction's current outstanding orderbook stands at MYR6.6bn, equivalent to 3.4x its FY17 construction revenue. It receives strong backing from its parent company, and maintains a high forecasted 3-year average ROE of 33%. Maintain BUY, with a TP of MYR2.50.

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2018-02-27	Buy	2.70	2.40
2017-12-29	Buy	2.70	2.51
2017-11-20	Buy	2.70	2.40
2017-10-06	Buy	2.60	2.29
2017-08-25	Neutral	2.30	2.34
2017-02-24	Buy	2.05	1.75
2016-08-26	Buy	1.86	1.62
2016-07-24	Buy	1.86	1.65
2016-03-29	Buy	1.86	1.67
2016-02-26	Buy	1.58	1.40

Source: RHB, Bloomberg

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Neutral: Share price may fall within the range of +/- 10% over the next 12 months

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