

COMPANY RESULTS

Sunway Construction (SCGB MK)

1Q20: Misses Expectations, Pulled Down By MCO

SunCon's 1Q20 net profit came in below expectations, pulled down by lower billings and a delay in precast delivery, while margins contracted due to MCO. We expect construction billings to pick up from mid-20 as SunCon is expected to adhere and fulfil the necessary SOP by then. This prompts us to revise down our earnings for 2020. Positively, SunCon has clinched new contracts worth RM688m ytd and is upbeat on meeting its RM2b target for 2020. Maintain HOLD with a higher target price of RM1.70. Entry price: RM1.45.

1Q20 RESULTS

Year to 31 Dec	1Q20 (RMm)	4Q19 (RMm)	qoq % chg	yoy % chg
Revenue	365.8	485.9	(24.7)	(16.9)
Construction	329.6	440.5	(25.2)	(19.0)
Precast Concrete	36.3	45.4	(20.1)	9.9
EBIT	18.7	30.8	(39.3)	(51.1)
Construction	17.3	27.0	(35.9)	(54.4)
Precast Concrete	1.4	3.9	(63.5)	330.3
Pre-tax Profit	21.2	40.5	(47.6)	(47.1)
PATMI	16.4	31.6	(48.3)	(47.3)
Core PATMI	17.6	36.3	(51.7)	(37.1)
Margins	%	%	+/-ppt	+/-ppt
Construction	5.2	6.1	(0.9)	(2.9)
Precast Concrete	3.9	8.5	(4.6)	13.4
PBT	5.8	8.3	(2.5)	(1.7)
PATMI	4.5	6.5	(2.0)	(1.4)

Source: SunCon, UOB Kay Hian

RESULTS

• **1Q20: Misses expectation.** Sunway Construction (SunCon) reported 1Q20 core net profit of RM18m (-52% qoq, -37% yoy) on revenue of RM366m (-25% qoq, -17% yoy). 1Q20 core net profit came in below our and consensus expectations, at 13% of our and consensus full-year estimates respectively. 1Q20 core net profit declined 37% yoy on lower billings from its construction orderbook backlog and margins contraction as a result of two weeks of Movement Control Order (MCO) from mid-Mar 20. Precast earnings contribution improved yoy due to higher-yield precast products. We expect a sluggish 2Q20 as minimal to zero billings would be recognised with fixed overheads. We expect construction orderbook billings to gradually pick up from mid-20.

KEY FINANCIALS

Year to 31 Dec (RMm)	2018	2019	2020F	2021F	2022F
Net turnover	2,257	1,769	1,311	2,064	2,213
EBITDA	196	161	129	212	216
Operating profit	155	121	92	171	172
Net profit (rep./act.)	144	129	83	149	152
Net profit (adj.)	142	133	83	149	152
EPS (sen)	11.0	10.3	6.4	11.5	11.7
PE (x)	17.8	19.0	30.5	17.0	16.7
P/B (x)	4.3	4.1	3.9	3.5	3.2
EV/EBITDA (x)	11.3	13.7	17.1	10.4	10.2
Dividend yield (%)	2.0	1.8	2.0	3.2	3.0
Net margin (%)	6.4	7.3	6.4	7.2	6.9
Net debt/(cash) to equity (%)	(46.6)	(49.9)	(49.7)	(52.4)	(55.5)
ROE (%)	25.5	21.3	13.0	21.6	19.9
Consensus net profit	-	-	137	156	153
UOBKH/Consensus (x)	-	-	0.61	0.96	0.99

Source: SunCon, Bloomberg, UOB Kay Hian

HOLD

(Maintained)

Share Price	RM1.96
Target Price	RM1.70
Upside	-13.2%
(Previous TP)	RM1.57

COMPANY DESCRIPTION

A leading construction company in Malaysia

STOCK DATA

GICS sector	Industrials
Bloomberg ticker	SCGB MK
Shares issued (m)	1,289.4
Market cap (RMm)	2,527.1
Market cap (US\$m)	581.5
3-mth avg daily t'over (US\$m)	0.3

Price Performance (%)

52-week high/low	RM2.18/RM1.29			
1mth	3mth	6mth	1yr	YTD
11.4	0.5	1.6	2.6	2.6

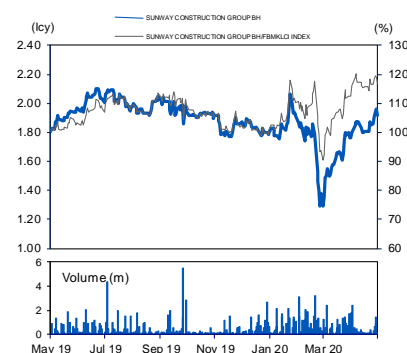
Major Shareholders

	%
Sunway Berhad	54.4
-	-
-	-

FY20 NAV/Share (RM) 0.51

FY20 Net Cash/Share (RM) 0.25

PRICE CHART



Source: Bloomberg

ANALYST(S)

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• **Construction: Billings to gradually pick up in 2H20.** Due to MCO, lower billings and fixed overhead costs, 1Q20 PBT margin eased 2.5ppt qoq and 1.7ppt yoy. The trend should continue into 2Q20 as minimal to no billings would be recognised and may potentially result in low profits (or losses). From our checks, we understand SunCon has started reducing overhead costs. From mid-20, we expect progress billings of its outstanding orderbook to gradually pick up, while to comply with the standard operating procedures (SOP) at sites, including ensuring all workers are screened and to practice social distancing. On a positive note, the company has secured new contracts worth RM688m ytd.

• **Higher-yield products delivered in 1Q20.** During the quarter, the division saw improved yoy earnings, thanks to delivering higher-yield precast products (high-ASP precast products). PBT margin rose 1.9ppt yoy but fell 2.4ppt qoq due to MCO. During the MCO period, production was halted and delivery of completed precast was restricted. We expect precast contribution to gradually improve from mid-20 as precast delivery to Singapore could begin from mid-20 and SunCon is not bounded to the local SOP (if any) as it merely delivers the products to customers.

STOCK IMPACT

• **Strong and diversified outstanding orderbook** of RM5.4b provides earnings visibility for the construction arm for the next 3-4 years. Ytd, SunCon has secured new contracts worth RM688m and is upbeat on meeting its 2020 replenishment target of RM2b. The new contracts include India Highway (RM508m, secured in 1Q20) via its 60% JV, Sunway International School (RM121m) and MRT2 M&E works (RM54m). In relation to the India Highway contract, the JV will not bear any traffic risk from this construction as it only acts as the contractor for the projects, and project progress payment will be paid by the National Highways Authority of India (NHAI). NHAI will pay the first 40% of the project during construction duration (24 months, with construction works to commence in Oct 20) and 60% will be paid via annuity form over the 15-year concession period. The interest on the deferred payment is based on Reserve Bank of India's cash reserve ratio + 3%.

• **MCO dragged 1H20 performance.** Due to the MCO, SunCon's construction activities have been halted for more than two months beginning mid-Mar 20. While SunCon has received approval to restart its construction works from May 20, the costs of adhering the SOP might erode its margins, with social distancing (meaning less manpower on site) and other costs like thermal screenings. However, we understand that most of SunCon's workers have been tested for Covid-19, while the subcontractors are currently undergoing screening. As such, we expect construction activities would only restart from mid-20 as we expect most of the workers would have been tested by then.

• **LRT3 progress to-date.** The MRCB-GKENT JV (LRT3's turnkey contractor) has concluded the design and specification negotiations for the six stations and the bridge design under the SunCon package. Post design and specification revision (less facade works, lower number of escalators, removal of subcontractor fees), SunCon expects the JV to be able to reduce station construction costs by at least 30% to below RM40m per station. Conservatively, we had already revised down SunCon's LRT3 contract by 35% in our previous note (to RM1.1b, from RM1.7b) factoring in the revised scheme but margins remain unchanged.

EARNINGS REVISION/RISK

• We revise our 2020-22 net profit forecasts by -38%, -2% and +8% respectively to factor in: a) the impact of MCO which will delay its billings and backload from 2021; and b) lower margins for 2020 but normalise from 2021. Our earnings forecasts are adjusted for revision in progress billings recognition.

VALUATION/RECOMMENDATION

• **Maintain HOLD with a higher target price of RM1.70** as we roll valuation to 2021. Our target price is based on 13x 2021F PE (-1SD below its 3-year average of 15.4x) and net cash position as of Mar 19. We ascribe a higher-than-peers' PE multiple in view of SunCon's solid fundamentals and earnings visibility, underpinned by new contracts secured, its ability to clinch a balanced mix of external and internal construction projects and a strong balance sheet (net cash). Should SunCon hit its orderbook replenishment target of RM2b in 2020, our target price will be RM1.74, based on 13x 2021F PE. Entry price is RM1.45.

TARGET PRICE

		(RMm)	Value (RMm)	Remarks
2021F net profit	A	149		
Net interest (income)/expense after tax	B	-11		
Net profit less net interest income	C=A-B	138	1,792	13x PE
Net cash (as of Mar 19)	D	405	405	
Total SOTP value	E=C+D		2,197	
Share base (m)	F		1,292	
				Implied PE (x)
TP (RM)	E/F		1.70	14.7
TP (RM) (ex-cash)	C/F		1.49	13.0

Source: UOB Kay Hian

OUTSTANDING ORDERBOOK AS OF MAR 20

	(RMm)
LRT3**	1,622
Tenaga HQ Campus	677
Petronas Learning Centre	287
India Highway*	508
Others	463
Total External (A)	3,557
Sunway Medical Centre – Phase 4	363
Sunway Serene	243
Sunway Velocity 2	286
Others	620
Total Internal (B)	1,512
Precast (C)	286
Total (A+B+C)	5,359

*New contracts secured in 2020

**Subject to revision. However, based on our estimates, we revised the outstanding contract down by 35% to RM1.1b

Source: Sunway Construction, UOB Kay Hian

ORDERBOOK REPLENISHMENT ASSUMPTIONS

(RMm)	2020F	2021F	2022F
Construction	1,700	1,700	1,700
Precast	100	100	100

Source: UOB Kay Hian

TENTATIVE ORDERBOOK REPLENISHMENT FOR YEAR 2020

	RMm
Internal (A)	1,100
Medical Centre	200
International school	100
Residential	500
Mixed Development	300
External (B)	1,200
Piling	300
Building Works (to secure at least one of the three contracts. Each contract worth RM500m each)	500
Renewable Energy (EPCC) – 60 MW	200
Precast	200
Annual target replenishment for 2020	-2,300
Building works (2 contracts valued RM500m/each)	1,000
Mixed development - Myanmar	250
Toll Highways (RM500m/package), tendered 2 packages	1,000
Other potential job wins	-2,250

*SunCon will potentially to achieve its target from item (A) and (B). Source: Sunway Construction, UOB Kay Hian

PROFIT & LOSS

Year to 31 Dec (RMm)	2019	2020F	2021F	2022F
Net turnover	1,769	1,311	2,064	2,213
EBITDA	161	129	212	216
Deprec. & amort.	40	37	41	44
EBIT	121	92	171	172
Total other non-operating income	20	0	0	0
Associate contributions	4	1	1	1
Net interest income/(expense)	12	11	14	17
Pre-tax profit	157	104	186	190
Tax	(27)	(21)	(37)	(38)
Minorities	(1)	0	0	0
Net profit	129	83	149	152
Net profit (adj.)	133	83	149	152

BALANCE SHEET

Year to 31 Dec (RMm)	2019	2020F	2021F	2022F
Other LT assets	195	213	227	238
Cash/ST investment	693	708	761	826
Other current assets	1,017	1,017	1,017	1,017
Total assets	1,905	1,938	2,005	2,081
ST debt	233	233	233	233
Other current liabilities	887	887	887	887
LT debt	148	148	148	148
Other LT liabilities	11	11	11	11
Shareholders' equity	623	656	723	799
Minority interest	2	2	2	2
Total liabilities & equity	1,905	1,938	2,005	2,081

CASH FLOW

Year to 31 Dec (RMm)	2019	2020F	2021F	2022F
Operating	188	120	190	196
Pre-tax profit	157	104	186	190
Tax	(45)	(21)	(37)	(38)
Deprec. & amort.	40	37	41	44
Working capital changes	0	0	0	0
Other operating cashflows	35	0	0	0
Investing	(51)	(55)	(55)	(55)
Capex (growth)	(8)	(55)	(55)	(55)
Investments	(47)	0	0	0
Proceeds from sale of assets	0	0	0	0
Others	4	0	0	0
Financing	72	(50)	(82)	(76)
Dividend payments	(90)	(50)	(82)	(76)
Issue of shares	0	0	0	0
Proceeds from borrowings	168	0	0	0
Loan repayment	0	0	0	0
Others/interest paid	(6)	0	0	0
Net cash inflow (outflow)	208	15	53	65
Beginning cash & cash equivalent	485	692	708	761
Changes due to forex impact	0	0	0	0
Ending cash & cash equivalent	693	708	761	826

KEY METRICS

Year to 31 Dec (%)	2019	2020F	2021F	2022F
Profitability				
EBITDA margin	9.1	9.8	10.3	9.8
Pre-tax margin	8.9	7.9	9.0	8.6
Net margin	7.3	6.4	7.2	6.9
ROA	7.0	4.3	7.6	7.4
ROE	21.3	13.0	21.6	19.9
Growth				
Turnover	(21.6)	(25.9)	57.4	7.2
EBITDA	(17.6)	(19.9)	64.5	1.8
Pre-tax profit	(13.9)	(33.9)	79.1	1.8
Net profit	(10.5)	(35.6)	79.0	1.8
Net profit (adj.)	(6.3)	(37.5)	79.0	1.8
EPS	(6.3)	(37.5)	78.9	1.8
Leverage				
Debt to total capital	37.9	36.7	34.5	32.3
Debt to equity	61.3	58.2	52.8	47.8
Net debt/(cash) to equity	(49.9)	(49.7)	(52.4)	(55.5)