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Sunway Construction's midway mark earnings intact

▶ **Recommendation: Hold**
TARGET Price: RM2.33
by Hong Leong Investment Bank Bhd (Aug 25)

Results at a Glance

SUNWAY Construction Group Bhd (SunCon) reported 2QFY17 results with revenue of RM417m (-1% QoQ, -3% YoY) and earnings of RM37m (+6% QoQ, +18% YoY). This brings cumulative 1H revenue to RM837m (-2% YoY) and earnings at RM71m (+18% YoY).

Deviation. Its 1H earnings were within expectations at 51% of our full-year forecast, but slightly below consensus at 46%.

Dividends. Interim dividend of three sen was declared versus 2.5 sen last year.

▶ **SUNWAY CONSTRUCTION GROUP BHD**

FYE DEC	FY16	FY17E	FY18F	FY19F
REVENUE (RM mil)	1,789	2,010	2,382	2,665
CORE PATAMI (RM mil)	105	141	151	169
CORE EPS (sen)	8.1	10.9	11.7	13.1
PE (x)	28.7	21.3	19.9	17.8

Highlights

Higher construction margin. Although 1H construction revenue was flat YoY, PBT rose by 37% given margin expansion from 6.4% to 8.8%. This was attributed to: i) Better margins recorded for its newer jobs; and ii) an arbitration gain from India.

Contract flows remain healthy. SunCon's YTD job wins stand at RM991m (including RM212m stations job which is part of its main Mass Rapid Transit Line 2 [MRT2] viaduct package).

Management is gunning for RM2b in job wins for FY17 (FY16: RM2.7b) which could potentially see some sizeable job flows for the remainder of the year.

We gather that SunCon is one of the top contenders to secure a package of the soon-to-be awarded Light Rail Transit Line 3 (LRT3) (RM9b) given its track record on jobs such as the LRT extension, MRT1 and the bus rapid transit.

Lower for precast. Both the company's 1H revenue and PBT for the precast division fell 18% and 22% YoY. This was due to slow construction progress by the main contractor (ie SunCon's client). PBT margin, nonetheless remained relatively stable at 22.4% in 1H versus 23.6% last year.

Risks. Orderbook replenishment coming below its burn rate.

Forecasts. As the results were in line, we maintain our earnings forecast.

Rating 'Hold'

We acknowledge that SunCon is a well-managed contractor with commendable execution capability, putting it in a prime spot as a pure construction play.

However, given its strong YTD share price performance of 36%, we feel that the stock is now priced to perfection, and hence, we downgrade our rating from 'Buy' to 'Hold'.

It currently trades at FY17-FY18 P/E of 21.3x and 19.9x respectively.

We advocate its parent, Sunway Bhd, ('Buy', TP: RM5.14), which trades at FY17-FY18 P/E of 15.2x and 14.1x, as a cheaper exposure to SunCon.

Valuation

While our earnings forecasts are unchanged, we roll over our valuation horizon from mid-FY18 to end-FY18, raising our target price (TP) from RM2.25 to RM2.33 at an unchanged 20x P/E target.

We reckon that our premium valuation yardstick for SunCon is justified given the following:

i) Its superior ROE of 27%, which is more than double of its peer's average; and

ii) healthy balance with net cash position of RM364m (RM0.28/ share).