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Sunway Construction seen to hit target margins

CONSTRUCTION

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PETALING JAYA: Despite the high inflationary environment coupled with a labour shortage, Sunway Construction Group Bhd  (SunCon) is likely to achieve its management's 5% to 8% earnings before interest and taxes or Ebit margin guidance for 2022, as prudent recognition from jobs reaching completion should see upward revision upon account finalisation, says Kenanga Research.

"The margin compression from high building material costs and labour shortages will be supplemented by upward margin adjustments for contracts completing this year upon account finalisation, given that SunCon has been prudent with margin recognition for ongoing projects all this while," said the research unit.


Kenanga Research also noted that SunCon was suffering from a severe labour shortage, with only 260 direct workers compared with 800 at the peak and 500 during the pandemic stage.


Although execution progress for the group is not affected, it will require additional costs for additional subcontractors – translating to margin erosion.

SunCon intends to secure another 700 direct workers, but noted that it would be tough to secure the quota.

Also, the current high steel prices of RM3,400 per tonne and cement prices of RM350 per tonne will erode margins from ongoing construction projects, and more so for its precast division.

High solar panel costs have halted the progress of SunCon's two existing solar contracts worth RM300mil.

The concessionaires, which awarded SunCon the contracts, are trying to renegotiate with [Tenaga Nasional Bhd](#)  for an extension of the concession period to ride out this high price period and wait for panel prices to drop - so that the initial internal rate of return or IRR can be maintained.

Meanwhile, year-to-date, SunCon's replenishment of RM266mil is trailing behind SunCon management's RM2bil jobs' target, which is divided evenly among precast, buildings and in-house works such as from [Sunway Bhd](#) , and infrastructure projects in India.

Current key tenders include the Johor Baru-Singapore rapid transit system Customs, immigration and quarantine or CIQ superstructure at a RM400mil value.

"Nonetheless, management has revealed that tenders are extremely competitive for this package," said Kenanga Research.

The group is also keen to secure the mass rapid transit 3 (MRT3) circle line project's elevated portions.

This includes the civil package one (six km elevated section and main depot) and civil package two (27km elevated and 1.2km on ground tunnel).

Kenanga Research has estimated that the civil packages one and two are worth RM2.5bil and RM12bil, respectively, based on contract costs extrapolated from MRT2.

However, in order to participate, the tendering consortium must have 60% bumiputra shareholding, and hence, SunCon will require a joint-venture partner for these jobs.

SunCon's Singapore precast plant or ICPH is on track to commence operations in August 2022 with a 75,000 cubic metre capacity (currently at 125,000 cubic metres).

SunCon's management has said that the plant would require RM300mil to RM500mil per annum revenue for full utilisation.

Its two India projects cumulatively worth RM818mil have commenced construction.

Upon completion of these two contracts, Kenanga Research expects SunCon's net cash position to swing to a net gearing of 0.05 times.

SunCon is internally comfortable with a net gearing of 0.5 times.

Kenanga Research has maintained its "market perform" call on SunCon's stock, with a target price of RM1.52.