AmResearch

Company report

PROPERTY DEVELOPMENT

SUNWAY BHD

(SWB MK, SWAY.KL)

5 June 2014

All set for Sunway Iskandar maiden launch

HOLD

(maintained)

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Rationale for report: Company Update

Price	**RM3.21**
Fair Value	**RM3.08**
52-week High/Low	RM3.96/RM2.55

Key Changes

Fair value	unchanged
EPS	unchanged

YE to Dec	FY13	FY14F	FY15F	FY16F
Revenue (RMmil)	4,721.4	4,458.0	4,961.6	4,551.9
Core net profit (RMmil)	484.0	452.2	511.0	566.5
EPS (Sen)	30.7	26.2	29.6	32.9
EPS growth (%)	28.4	n/a	13.0	10.9
Consensus EPS (Sen)	n/a	n/a	n/a	n/a
DPS (Sen)	10.0	10.0	11.0	0.0
PE (x)	10.5	12.2	10.8	9.8
EV/EBITDA (x)	8.3	6.8	6.3	6.0
Div yield (%)	3.1	3.1	3.4	0.0
ROE (%)	34.9	8.3	8.8	9.2
Net Gearing (%)	19.3	20.8	19.8	22.3

Stock and Financial Data

Shares Outstanding (million)	1,723.5
Market Cap (RMmil)	5,532.5
Book value (RM/share)	3.09
P/BV (x)	1.0
ROE (%)	34.9
Net Gearing (%)	19.3
Major Shareholders	Tan Sri Jeffrey Cheah (47.7%) GIC (12.2%)
Free Float (%)	30.0
Avg Daily Value (RMmil)	3.3

Price performance	3mth	6mth	12mth
Absolute (%)	6.2	21.2	(25.7)
Relative (%)	4.6	18.6	(31.1)

Investment Highlights

- **We maintain HOLD on Sunway, with an unchanged fair value of RM3.08/share, based on a 5% discount to an SOP value of RM3.23/share.**

- **Sunway yesterday brought a group of analysts and fund managers for a site visit at Sunway Iskandar, in conjunction with the unveiling of the masterplan for the >RM30bil development, for which it has dubbed "Nature's Capital City".**

- **At the newly-unveiled show gallery, a briefing was conducted by Sunway property development division (Malaysia/Singapore) joint managing director Sarena Cheah, CFO Chong Chang Choong, and Sunway group executive director, property & construction (southern region & Singapore) Tan Wee Bee. The key takeaways are:-**

- **(1) The group is poised to execute the masterplan, with the maiden launch – the Citrine, at the Lakeview Precinct (one of six precincts) – slated within the next two months.**

- **(2) Sunway could potentially launch up to RM1bil worth of properties annually in the initial years. Management says it has the capacity to go beyond RM1bil annually, if it is required. Sunway welcomes JV partners with the capital to back up their commitment. It is difficult to say when revenue and earnings from Sunway Iskandar could peak during the 15-20 year development period.**

- **(3) The group is confident of its ability to differentiate itself from other developers in the economic corridor; it has pledged to retain 40% of the land at Sunway Iskandar (Medini and Pendas) for green spaces. It owns the biggest plot of land in Medini (the zone with special government incentives), with Sunway Iskandar making up 31% (691 acres) of land there.**

- **(4) Other than unique features for each of the six planned precincts, competitively-priced products, easy accessibility and proximity to Singapore, the group is banking on its proven track record and development philosophy to attract potential investors and buyers alike.**

- **(5) Sunway will allocate 60% and 40% of the development for the residential and commercial portions, respectively. We understand that possibly 20% or more of the total value (comprising mainly commercial properties such as a mall) could have their ownership retained for recurring income and strategic purposes (such as tenancy management, or for injection to SUNREIT).**

- **As the group braces for its new phase of growth, execution would be key. Notwithstanding the current cautious property market, Sunway Iskandar is set to be a long-term growth anchor for the group. We maintain our Hold call for now.**

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SUNWAY ISKANDAR – NATURE'S CAPITAL CITY

"A journey of a thousand miles begins with a single step," as the popular saying goes.

For Sunway, that upcoming journey is the >RM30bil Sunway Iskandar township – a key driver of its next phase of growth – which will replicate its earlier successes at Sunway City Resort (Bandar Sunway) and Sunway City Ipoh, save on a bigger scale.

Dubbed "Nature's Capital City" and spanning 720ha within Iskandar Malaysia, the massive 15-20 year development will comprise six precincts – The Capital, The Parkview, The Lakeview, The Riverside, The Seafront, and The Marketplace.

Within the next one or two months, Sunway Iskandar is slated to undertake its maiden launch, at the Lakeview in Medini.

Ahead of that first launch, Sunway yesterday brought a group of analysts and fund managers for a site visit at Sunway Iskandar, in conjunction with the unveiling of the masterplan.

At the newly-built RM3mil show gallery, a briefing was conducted by Sunway property development division (Malaysia/Singapore) joint managing director Sarena Cheah, CFO Chong Chang Choong, and executive director, property & construction (southern region & Singapore) Tan Wee Bee.

❑ *Poised for maiden launch at RM350mil Citrine*

The group is ready to execute and implement the masterplan, with the first launch – the RM350mil Citrine, at the Lakeview Precinct – within the next two months.

Spanning 100 acres, the RM2bil Lakeview development will include serviced apartments, boutique offices, retail units, a Sunway International School, and an eco-water theme park along the 7km-long Pendas river bank.

The earthworks are now being carried out for the first phase of residential and commercial buildings at the Citrine, which offers 328 serviced apartments, 197 office suites and 51 retail units.

Sunway will retain ownership of the retail units, to manage tenancy quality and for recurring income.

The residential units, with a built-up of between 618 and 1,571 square feet each, have an indicative pricing of ~RM700/sq ft.

For the office suites, the indicative pricing is at between RM550 and RM650/sq ft for each unit with a built-up of 746 square feet to 1,671 square feet.

About 46% of the designer office suites are corner units.

Maintenance charges could amount to 30 sen/sq ft and 22 sen/sq ft for the residential and office units, respectively. Indicative yield for the office space is at ~5%.

Out of the RM350mil GDV for the Citrine, the office suites would account for RM80mil-RM90mil, while the residential units make up the rest.

We understand that operating margins could be in the low teens for the initial launches at Medini.

It has been reported that the Citrine will take about three years to complete, while the overall Lakeview precinct development will take about five years.

Sunway says it would be the first township in Iskandar to launch five important components — retail, office units, serviced apartments, a theme park and an international school — in the first year of its first phase.

Other components include a theme park mall, a hotel, a medical park, and a petrol station.

The Sunway International School is the only school in the country to offer the Canadian (Ontario) curriculum; it will have an initial student capacity of 600 in the first intake.

Other prominent features of the Lakeview are the fronting of a scenic 8-acre lake with recreational facilities and a 360-degree view of the lake, park, mangrove, river and the Straits of Singapore.

Over the past few months, potential buyers have registered their interest for the Citrine properties.

Managements said 60% of the interested buyers are Malaysians, 30% Singaporeans, and the remaining 10% are of other nationalities.

The company expects the first buyers to comprise mainly investors, as opposed to owner occupiers.

Notably, the Lakeview will set the tone for Sunway's strategic launches ahead.

The group intends to launch clusters of properties, with (a) component/s to be unveiled at short intervals of one another – with the primary aim of creating a sustainable "living community" within each cluster.

Management believes this would not only be more cost-efficient, but be more effective marketing-wise.

From our conversations with management, we believe the group could potentially launch up to RM1bil worth of properties in Sunway Iskandar annually in the initial years.

Nonetheless, management said it has the capacity to go beyond RM1bil annually, if and when market conditions permit. While the pipeline of projects has been identified, it remains flexible to adapt to changes in market conditions.

At this point, however, it is difficult to tell when revenue and earnings from Sunway Iskandar could peak.

The company said it does not at the moment cater to request for purpose-built offices, but will instead focus on building satellite offices.

Management also said Sunway welcome JV partners, but they must come to the table with capital to back up their commitment.

Differentiation strategy

The group is confident of its ability to differentiate itself from other developers in the economic corridor.

Notably, it has pledged to retain 40% of the land at Sunway Iskandar (Medini and Pendas) for green spaces.

We believe this alone will garner substantial premium for future launches.

Sunway's "development philosophy of integrating and enhancing the natural surroundings" will resonate with many, particularly for foreign buyers looking for unique propositions.

It owns the biggest plot of land in Medini (the zone with special government incentives), with Sunway Iskandar making up 31% (691 acres) of land there.

Overall, Sunway Iskandar would have a low-density population of ~120,000.

Other than unique features for each of the six planned low-density precincts (plot ratio of one), competitively-priced products, easy accessibility and proximity to Singapore, the group is banking on its proven track record to attract potential investors and buyers alike.

Apart from intent on developing communities from the outset and the commune with nature, the group is also banking on its one other prong in its development philosophy, i.e., one that focuses on accessibility, connectivity and security.

At the micro level, it means whenever viable, connectivity could be provided between components of each cluster of development via underground passages or car parks.

60% residential, 40% commercial

Sunway will allocate 60% and 40% of the development for the residential and commercial portions, respectively.

We further understand that possibly 20% or more of the total value (comprising mainly commercial properties such as a mall) could be retained for its own, for recurring income and strategic purposes (such as tenancy management, or for injection to SUNREIT).

SUNWAY ISKANDAR BACKGROUND

To recap, the 1,800-acre Sunway Iskandar is now a 15 minute-drive away from the Second Link between Malaysia and Singapore. With a proposed southern access, that would be cut to a mere five minutes to the Second Link.

This would be Sunway's third integrated townships after the iconic Sunway Resort City in Bandar Sunway and Sunway City Ipoh.

One of the main elements that would set Sunway Iskandar apart from the other two earlier developments is the existing major attractions at Iskandar Malaysia – such as Legoland Malaysia, Pinewood Iskandar Malaysia Studios, the Premium Outlet, and EduCity.

Additionally, unlike Bandar Sunway when it was first developed, Sunway Iskandar's basic public infrastructure such as roads and main drainage has already been built – providing it with cost advantages.

The current RM30bil price tag translates into ~RM400/sq ft.

Furthermore, for the Medini portion of Sunway Iskandar, comes with incentives tailored for developers. They include:- (1) Exemption from corporate tax up to 2020 and RPGT; (2) Exemption from Bumiputra quota; (3) Exemption from low cost housing requirement; and (4) Exemption from the minimum threshold of RM1mil in respect of foreign purchasers.

Sunway owns a total of 691 acre-leased land in Medini, via a JV vehicle with government investment arm Khazanah.

Sunway currently holds a 51% stake in the JV (up from 38% initially). Pursuant to the lease purchase agreement, it would increase that to 60% by June next year.

It owns an additional 1,079.7 acres in Pendas, within Iskandar Malaysia, via another JV with Khazanah. Sunway's effective interest in the Pendas land is also 60%, with Khazanah holding the balance.

All in, Sunway acquired the Pendas land for an average of RM12.69/sq ft vs. RM24.73/sq ft for the Medini land.

Sunway has full control of the river front development on both sides of the river bank along Sungai Pendas.

Note that in the accounting treatment, Sunway's JV with Khazanah in the Iskandar Malaysia development is deemed to be jointly-controlled entities that would be equity accounted, instead of being consolidated.

LONG-TERM GROWTH STORY

As the group braces for its new phase of growth, execution would be key.

Notwithstanding the current cautious property market, Sunway Iskandar is set to be a long-term growth driver for the group. We maintain our numbers and our HOLD call for now.

CHART 1 : PB BAND CHART

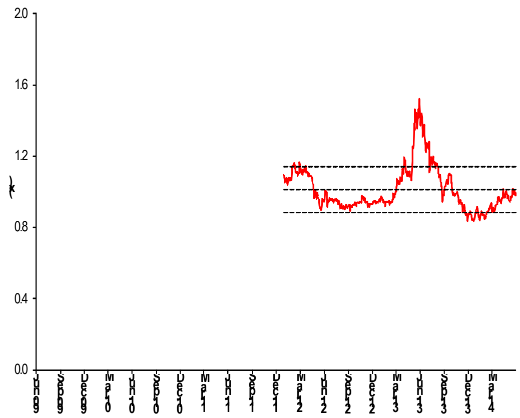

CHART 2 : PE BAND CHART

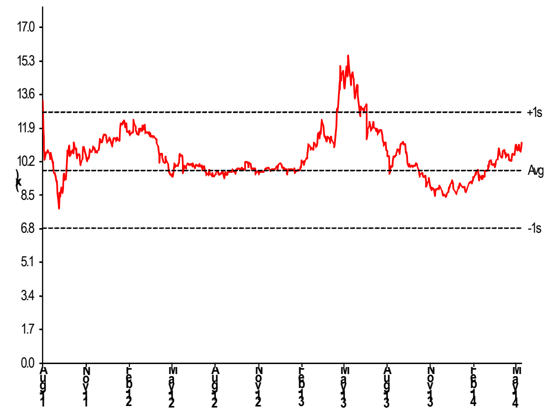

TABLE 1 : FINANCIAL DATA

Income Statement (RMmil, YE 31 Dec)	2012	2013	2014F	2015F	2016F
Revenue	4,128.8	4,721.4	4,458.0	4,961.6	4,551.9
EBITDA	519.5	589.5	727.7	778.0	888.1
Depreciation	(138.0)	(137.0)	(139.0)	(141.0)	(159.0)
Operating income (EBIT)	381.5	452.5	588.7	637	729.1
Other income & associates	219.8	255.9	225.9	258.0	265.7
Net interest	(76.8)	(46.1)	(80.5)	(94.3)	(132.9)
Exceptional items	315.2	1,238.1	0.0	0.0	0.0
Pretax profit	**839.6**	**1,900.4**	**734.1**	**800.7**	**862.0**
Taxation	(115.4)	(137.0)	(183.5)	(200.2)	(215.5)
Minorities/pref dividends	(285.5)	(273.0)	(98.4)	(89.6)	(80.0)
Net profit	**438.8**	**1,490.4**	**452.2**	**511.0**	**566.5**
Core net profit	350.7	484.0	452.2	511.0	566.5

Balance Sheet (RMmil, YE 31 Dec)	2012	2013	2014F	2015F	2016F
Fixed assets	6,948.8	3,564.1	3,978.4	4,242.7	5,197.2
Intangible assets	318.1	319.4	319.4	319.4	319.4
Other long-term assets	612.6	2,369.7	2,520.3	2,531.3	2,549.8
Total non-current assets	**7,879.5**	**6,253.3**	**6,818.2**	**7,093.5**	**8,066.4**
Cash & equivalent	1,197.5	1,448.8	1,436.5	1,995.5	2,720.9
Stock	650.3	615.8	834.2	884.2	937.3
Trade debtors	1,584.9	1,525.5	1,456.7	1,596.9	1,482.9
Other current assets	1,051.6	1,258.1	1,284.6	1,320.9	1,358.3
Total current assets	**4,484.2**	**4,848.3**	**5,012.1**	**5,797.6**	**6,499.4**
Trade creditors	1,844.8	2,051.8	2,366.5	2,508.5	2,659.0
Short-term borrowings	2,955.0	2,000.7	935.9	1,285.9	1,585.9
Other current liabilities	21.2	86.3	21.5	21.5	21.5
Total current liabilities	**4,821.0**	**4,138.9**	**3,323.9**	**3,815.9**	**4,266.4**
Long-term borrowings	1,688.4	794.7	2,059.6	2,259.6	3,059.6
Other long-term liabilities	503.0	522.8	522.8	522.8	522.8
Total long-term liabilities	**2,191.4**	**1,317.5**	**2,582.3**	**2,782.3**	**3,582.3**
Shareholders' funds	**3,214.8**	**5,328.3**	**5,607.2**	**5,975.9**	**6,400.2**
Minority interests	2,136.5	316.9	316.9	316.9	316.9
BV/share (RM)	2.49	3.09	3.25	3.47	3.71

Cash Flow (RMmil, YE 31 Dec)	2012	2013	2014F	2015F	2016F
Pretax profit	839.6	1,900.4	734.1	800.7	862.0
Depreciation	138.0	137.0	139.0	141.0	159.0
Net change in working capital	(379.0)	93.0	(65.6)	(84.5)	174.1
Others	(31.6)	(1,037.1)	(288.1)	(104.4)	(316.3)
Cash flow from operations	**567.0**	**1,093.4**	**519.4**	**752.8**	**878.7**
Capital expenditure	(399.4)	(85.4)	(332.9)	(83.0)	(133.9)
Net investments & sale of fixed assets	56.5	11.3	11.2	11.2	11.2
Others	(334.9)	(815.9)	(467.4)	(260.0)	(47.9)
Cash flow from investing	**(677.8)**	**(889.9)**	**(789.1)**	**(331.7)**	**(170.5)**
Debt raised/(repaid)	434.5	498.3	298.3	249.3	249.3
Equity raised/(repaid)	0.0	0.0	0.0	0.0	0.0
Dividends paid	0.0	(163.7)	(150.8)	(142.2)	(142.2)
Others	(56.0)	(292.2)	110.0	30.7	(89.8)
Cash flow from financing	**378.6**	**42.4**	**257.4**	**137.8**	**17.3**
Net cash flow	**267.8**	**245.8**	**(12.3)**	**558.9**	**725.4**
Net cash/(debt) b/f	**838.0**	**1,102.3**	**1,359.1**	**1,346.8**	**1,905.8**
Net cash/(debt) c/f	**1,102.3**	**1,359.1**	**1,346.8**	**1,905.8**	**2,631.2**

Key Ratios (YE 31 Dec)	2012	2013	2014F	2015F	2016F
Revenue growth (%)	11.8	14.4	n/a	11.3	n/a
EBITDA growth (%)	19.3	13.5	23.4	6.9	14.2
Pretax margins (%)	20.3	40.2	16.5	16.1	18.9
Net profit margins (%)	10.6	31.6	10.1	10.3	12.4
Interest cover (x)	3.8	5.5	4.4	4.1	3.7
Effective tax rate (%)	13.7	7.2	25.0	25.0	25.0
Net dividend payout (%)	13.3	8.7	28.6	27.8	0.0
Debtors turnover (days)	128	120	122	112	123
Stock turnover (days)	49	49	59	63	73
Creditors turnover (days)	155	151	181	179	207

Source: Company, AmResearch estimates

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