HLIB Research
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Sunway Construction Group

Important execution year

SunCon is targeting a base case replenishment target of RM2.0bn in FY23. This could rise to RM8.0bn on a bull case scenario, augmented by the Vietnam power plant job. There is further upside should the company prove successful in its Tier 1 MRT3 bids. FY23 will be an important year execution wise as this could unlock further data centre jobs with opportunities on an uptrend. Improving labour supply conditions should be helpful to this end. Increase FY23 earnings forecasts by +10.0% but cut FY24 earnings by -7.3% post adjusting burn rate for data centre project. Maintain BUY with lower TP of RM1.94 after removing NCPS assumption. SunCon presents a safer exposure to future infrastructure project rollouts, backed by strong support from parent-co.

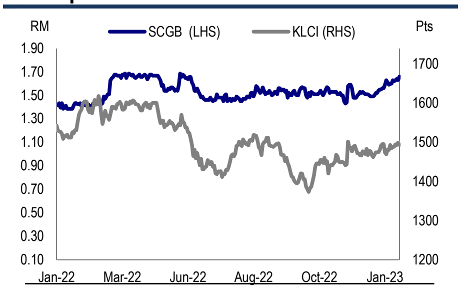
BUY (Maintain)

Target Price:	**RM1.94**
Previously:	**RM2.06**
Current Price:	**RM1.67**

Capital upside	16.2%
Dividend yield	3.1%
Expected total return	19.3%

Sector coverage: Construction
Company description: SunCon is involved in construction and precast products.

Share price



Historical return (%)	1M	3M	12M
Absolute	10.7	9.2	11.4
Relative	9.6	2.4	15.1

Stock information

Bloomberg ticker	SCGB MK
Bursa code	5263
Issued shares (m)	1,289
Market capitalisation (RM m)	2,159
3-mth average volume ('000)	892
SC Shariah compliant	Yes
F4GBM Index member	No
ESG rating	NA

Major shareholders

Tan Sri Dato' Seri Dr Jefferey Cheah	64.7%
EPF	9.4%

Earnings summary

FYE (Dec)	FY21	FY22f	FY23f
PATMI - core (RM m)	145.3	130.4	167.2
EPS - core (sen)	11.2	10.1	12.9
P/E (x)	14.9	16.6	12.9

We caught up with SunCon's management recently with the following key takeaways:

FY23: RM2bn target. SunCon's base case replenishment target for 2023 stands at RM2.0bn with a bull case target of RM8.0bn. The latter scenario is double of its record high wins achieved in FY17. Making up its RM2.0bn base case target are: (i) Tier 2 MRT 3 works at RM1.0-1.2bn, (ii) CP2 at RM300m, (iii) Ipoh mall at RM200m, and (iv) precast jobs at ~RM300m (SGD100m). There are also several other tenders ongoing such as Tier 1 MRT3 packages and mixed development – podium, warehouses and data centres. We believe SunCon's upside scenario has incorporated the RM5.8bn Vietnam power plant project (interim EPC signed) but no Tier 1 MRT 3 packages. We believe developments in 1H23 would be critical as to where SunCon's replenishment pathway will look like in FY23.

Data centre. Its RM1.7bn data centre project in Sedenak Tech Park, Johor is scheduled to achieve 80% burn within the first 14 months with the remaining 20% in the last 5 months. If it materialises in accordance with SunCon's expectations this would present upside risk to our revised FY23 earnings forecasts. The project is a low rise building covering a wide area of land; more foundation works and precast usage. Management is expecting to deploy up to 30 piling rigs for the project. Given that its SunCon's first data centre project, execution is its utmost priority in FY23. We believe smooth execution would place SunCon in a strong position for more data centre wins where construction opportunities are on an uptrend.

Vietnam. SunCon recently signed an interim EPC contract with Toyo Ink for the construction of the 2x1,060 MW Song Hau 2 thermal power plant (RM5.8bn based on 60% stake). The company is undertaking a further due diligence process and project developments could come in 1H23. For some background, Toyo Ink finalised its BOT agreement with the Vietnamese government in Dec-20, more than a decade since the initial approval. The total development cost of the project is estimated at USD3.23bn (USD2.2bn for EPC). We gather that the BOT agreement carries government guarantees such as: (i) PPA offtake, (ii) default protection against all Vietnamese counterparties, (iii) changes in law & government event risks as well as (iv) USD convertibility. Nevertheless, financial close has been tough, made worse by China, Japan and South Korea's pledge to cease financing of new coal-fired plants. We reckon Malaysia's EXIM Bank would have to source from coal friendly ASEAN countries. Due to reasons above we have left this project unaccounted for.

Labour intake to improve. The company has received 390 out of 400 approved workers from its first batch of applications submitted early last year. The second batch of 300 workers could come in by either 1Q23 or 1H23. Recent modifications to the labour intake process have been well received by the company. We see the government's decision to do away with the need of advertising on MyFutureJobs alone could trim 30 days from the entire process. According to SunCon, this, alongside concurrent running of several other processes could cut the intake process by half from its peak of 9-10 months. We gather that as a result of fresh arrivals, there is some respite on wage rates.

Precast kicker not so soon. Contrary to our initial expectations, management has adopted a more conservative guidance thus delaying earnings kicker from the ICPH plant to late FY23. In our revised forecasts, we have factored in an earnings drag from the new plant for a majority of FY23. The precast demand should remain healthy in SG on the back of HDB's 2023 launch target amounting to 23k units (flattish vs 2022; +35% higher than 2021).

Could turn net gearing. SunCon could slip into net gearing position mainly due to cash flow mismatch for its two Indian highway projects**.** Mode of delivery for both projects is based on the hybrid annuity model (HAM). Under this model, 40% of the contract value will be paid during the construction period while the remaining 60% is paid over 15 years as fixed annuity amount plus interest (benchmarked to RBI rate +3% pa; RBI rate is currently 6.25%). Compared to a traditional BOT model, SunCon is not exposed to traffic volume risks. We think SunCon has the option to factorise receivables to restore net cash position if need be.

Forecasts. Increase FY23 earnings forecasts by +10.0% but cut FY24 earnings by -7.3% post adjusting burn rate for data centre project and lower contribution from new precast plant.

Maintain BUY, TP: RM1.94. Maintain BUY with lower TP of RM1.94 (from RM2.06) post to earnings. Despite the earnings uplift in FY23, our TP is reduced as we remove NCPS of RM0.30 from our calculations due to reasons mentioned above. TP is derived by pegging FY23 EPS to 15x P/E. SunCon presents a safer exposure to future infrastructure project rollouts, backed by strong support from parent-co. Nevertheless, our call is premised on no disruptive infrastructure policies going forward. Risks: MRT3 cancellation, prolonged political deadlock, elevated materials prices and labour shortage.

Financial Forecast

All items in (RM m) unless otherwise stated

Balance Sheet

FYE Dec (RM m)	FY20	FY21	FY22f	FY23f	FY24f
Cash	200.1	98.8	114.8	331.3	447.8
Receivables	904.9	660.8	949.8	1,252.8	1,301.3
Inventories	34.3	46.2	24.1	31.6	33.0
PPE	107.3	124.7	105.4	88.3	69.3
Others	659.6	933.7	940.3	940.9	962.7
Assets	**1,906.1**	**1,864.2**	**2,134.5**	**2,644.9**	**2,814.2**
Debts	300.9	237.9	352.4	461.8	482.3
Payables	947.4	873.2	965.5	1,265.1	1,321.5
Others	19.1	36.3	36.4	36.4	36.4
Liabilities	**1,267.5**	**1,147.4**	**1,354.3**	**1,763.2**	**1,840.1**
Shareholder's equity	636.9	699.1	762.6	864.0	956.4
Minority interest	1.7	17.6	17.7	17.7	17.8
Equity	**638.6**	**716.8**	**780.2**	**881.7**	**974.2**

Cash Flow Statement

FYE Dec (RM m)	FY20	FY21	FY22f	FY23f	FY24f
Profit before taxation	120.3	185.0	179.2	215.7	214.9
Depreciation & amortisation	33.4	27.4	39.3	37.1	38.9
Changes in working capital	0.9	157.9	(174.6)	(10.9)	6.4
Share of JV profits	(0.1)	(13.3)	(6.6)	(0.5)	(21.9)
Taxation	(28.8)	(41.5)	(48.0)	(47.3)	(42.5)
Others	(37.9)	(76.8)	-	-	-
Operating cash flow	**87.8**	**238.7**	**(10.7)**	**194.1**	**195.9**
Net capex	(1.9)	(40.6)	(20.0)	(20.0)	(20.0)
Others	(171.3)	(133.4)	-	-	-
Investing cash flow	**(173.2)**	**(174.0)**	**(20.0)**	**(20.0)**	**(20.0)**
Changes in borrowings	14.7	(63.0)	114.5	109.3	20.6
Issuance of shares	-	-	-	-	-
Dividends paid	(62.3)	(77.0)	(67.8)	(66.9)	(80.1)
Others	(99.7)	17.7	-	-	-
Financing cash flow	**(147.3)**	**(122.4)**	**46.7**	**42.5**	**(59.5)**
Net cash flow	**(232.7)**	**(57.7)**	**16.0**	**216.5**	**116.4**
Forex	-	-	-	-	-
Others	(259.9)	(43.5)	-	-	-
Beginning cash	692.6	200.1	98.8	114.8	331.3
Ending cash	200.1	98.8	114.8	331.3	447.8

Income Statement

FYE Dec (RM m)	FY20	FY21	FY22f	FY23f	FY24f
Revenue	**1,552.7**	**1,729.2**	**2,166.8**	**2,857.9**	**2,968.7**
EBITDA	143.2	199.6	213.6	260.3	242.0
EBIT	109.7	172.2	174.4	223.2	203.0
Net finance income/ (cost)	10.5	(0.4)	(1.8)	(8.1)	(10.0)
Associates & JV	0.1	13.3	6.6	0.5	21.9
Profit before tax	**120.3**	**185.0**	**179.2**	**215.7**	**214.9**
Tax	(27.8)	(41.5)	(48.0)	(47.3)	(42.5)
Net profit	**92.5**	**143.5**	**131.3**	**168.3**	**172.4**
Minority interest	(0.7)	1.8	(0.9)	(1.2)	(1.1)
Core PATAMI	**91.9**	**145.3**	**130.4**	**167.2**	**171.4**
Exceptional items	(19.2)	(32.8)	-	-	-
Reported earnings	72.7	112.6	130.4	167.2	171.4

Valuation & Ratios

FYE Dec (RM m)	FY20	FY21	FY22f	FY23f	FY24f
Core EPS (sen)	7.1	11.2	10.1	12.9	13.3
P/E (x)	23.5	14.9	16.6	12.9	12.6
EV/EBITDA (x)	15.8	11.3	10.6	8.7	9.3
DPS (sen)	4.0	6.0	5.2	5.2	6.2
Dividend yield	2.4%	3.6%	3.1%	3.1%	3.7%
BVPS (RM)	0.5	0.5	0.6	0.7	0.7
P/B (x)	3.4	3.1	2.8	2.5	2.3
EBITDA margin	9.2%	11.5%	9.9%	9.1%	8.2%
EBIT margin	7.1%	10.0%	8.0%	7.8%	6.8%
PBT margin	7.7%	10.7%	8.3%	7.5%	7.2%
Net margin	6.0%	8.3%	6.1%	5.9%	5.8%
ROE	14.6%	21.8%	17.8%	20.6%	18.8%
ROA	4.6%	7.1%	6.2%	6.4%	5.5%
Net gearing	15.8%	19.9%	31.2%	15.1%	3.6%

Assumptions

FYE Dec (RM m)	FY20	FY21	FY22f	FY23f	FY24f
Construction	2,281	1,149	2,414	2,000	2,000
Precast	38	296	168	400	200
Total new job wins	**2,319**	**1,445**	**2,582**	**2,400**	**2,200**

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BUY	Expected absolute return of +10% or more over the next 12 months.
HOLD	Expected absolute return of -10% to +10% over the next 12 months.
SELL	Expected absolute return of -10% or less over the next 12 months.
UNDER REVIEW	Rating on the stock is temporarily under review which may or may not result in a change from the previous rating.
NOT RATED	Stock is not or no longer within regular coverage.

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OVERWEIGHT	Sector expected to outperform the market over the next 12 months.
NEUTRAL	Sector expected to perform in-line with the market over the next 12 months.
UNDERWEIGHT	Sector expected to underperform the market over the next 12 months.

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