

24 August 2023

Sunway Construction Group

A Soft Patch, Better Prospects Ahead

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SUNCON's 1HFY23 results disappointed due to a slower-than-expected pickup in its construction work progress and weaker margins. We remain optimistic on SUNCON given the imminent roll-out of key public infrastructure projects post the recent state elections. We cut FY23-24F earnings forecasts by 11-5%, trim our TP slightly to RM2.12 (from RM2.13) but maintain our OUTPERFORM call.

SUNCON's 1HFY23 core profit of RM58.2m missed expectations at only 36% and 39% of our full-year forecast and the full-year consensus estimate, respectively. The variance against our forecast came largely from a slower-than-expected pickup in its construction work progress and weaker margins.

It declared an 1st interim NDPS of 3.0 sen (ex-date: 11 Sept; payment date: 27 Sept) in 2QFY23, which matched the 3.0 sen NDPS paid in 2QFY22.

YoY, its 1HFY23 revenue fell 5% to RM1.13b while core profit contracted 20% to RM58.2m as key new projects were still at their initial stages of construction. Meanwhile, high interest cost which jumped from RM4.3m to RM19.7m also impacted earnings negatively. The higher borrowing was to fund its India projects at higher progress stages.

QoQ, its 2QFY23 revenue rose 16% to RM604.1m while core profit grew 25% to RM32.3m. This was due to higher progress billings from sustainable energy projects as well as the acceleration in work progress of newer projects.

Outlook. We expect a significant revitalisation of the construction sector in 2HCY23 backed by: (i) the roll-out of the RM45b MRT3 project and six flood mitigation projects reportedly to be worth RM13b, and (ii) an accelerated disbursement of the massive RM97b gross development expenditure budgeted under Budget 2023 (+35% YoY over RM71.6b a year ago). Similarly, the private sector construction market is vibrant underpinned by massive investment in new semiconductor foundries and data centres. Meanwhile, SUNCON's current outstanding order book stands at RM5.8b (of which RM1.5b was secured during the year) while its active tender book stands at RM27.0b comprising data centre building jobs, MRT3 work packages and contracts from parent and sister companies.

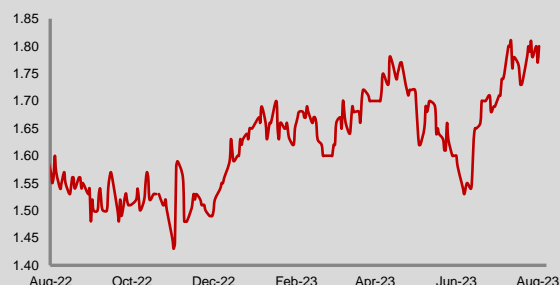
Forecasts. We cut our FY23-24F net profit forecasts by 11-5% to account for lower revenue and margin assumptions as key new projects are still at initial construction stages as mentioned above.

As we also roll forward our valuation base year to FY24F (from FY23F), the downgrade in TP is negligible by only 0.5% to RM2.12 (from RM2.13). We value SUNCON at 16x FY24F PER, at the upper range of our target forward PER for mid-sized and large contractors given SUNCON's large market capitalisation and strong track record in mega infrastructure projects. Our TP carries a 5% premium by virtue of its 4-star ESG rating as appraised by us (see Page 4).

OUTPERFORM ↔

Price: RM1.80
Target Price: RM2.12 ↓

Share Price Performance



KLCI	1,440.11
YTD KLCI chg	-3.7%
YTD stock price chg	15.4%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	SCGB MK Equity
Market Cap (RM m)	2,320.9
Shares Outstanding	1,289.4
52-week range (H)	1.84
52-week range (L)	1.41
3-mth avg daily vol:	450,811
Free Float	13%
Beta	0.8

Major Shareholders

Sunway Holdings Sdn Bhd	54.6%
Sungei Way Corp Sdn Bhd	10.1%
Employees Provident Fund Board	9.8%

Summary Earnings Table

FY Dec (RM m)	2022A	2023F	2024F
Turnover	2155.2	2587.0	2854.4
EBIT	188.2	196.0	224.6
PBT	184.1	190.5	214.6
Net Profit (NP)	135.2	146.1	163.3
Core net profit	144.0	146.1	163.3
Consensus (NP)	-	149.1	161.1
Earnings Revision	-	-10.7	-4.8
Core EPS (sen)	11.2	11.3	12.7
Core EPS growth (%)	28.7	1.5	11.8
NDPS (sen)	5.5	5.0	5.0
NTA per Share (RM)	0.59	0.66	0.73
Price to NTA (x)	3.0	2.7	2.5
PER (x)	16.1	15.9	14.2
Net Gearing (x)	N Cash	0.06	N Cash
ROE (%)	18.9	17.3	17.3
Net Div. Yield (%)	3.1	2.8	2.8

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We like SUNCON for: (i) its strong replenishment pipeline from parent SUNWAY, (ii) its dominant position in the local construction space with extensive capabilities in building, infrastructure, solar, mechanical, electrical and plumbing works, and (iii) its strong balance sheet that allows it to participate in deferred payment model projects. Maintain **OUTPERFORM**.

Risks to our call include: (i) sustained weak flows of construction jobs from public and private sectors, (ii) project cost overrun and liabilities arising from liquidated ascertained damages (LAD), and (iii) rising cost of building materials.

Income Statement								
FYE Dec (RM m)	2Q	1Q	QoQ	2Q	YoY	1H	1H	YoY
	FY23	FY23	Chg	FY22	Chg	FY23	FY22	Chg
Revenue	604.1	522.1	16%	557.9	8%	1,126.2	1,182.5	-5%
Operating Expenses	-562.5	-484.3	16%	-517.6	9%	-1,046.8	-1,100.7	-5%
Other Operating Income	5.0	3.9	30%	2.1	144%	8.9	3.4	159%
Operating Profit	46.7	41.7	12%	42.4	10%	88.4	85.3	4%
Finance Income	6.7	4.1	64%	3.2	112%	10.8	5.4	101%
Finance costs	-11.5	-8.3	39%	-3.2	260%	-19.7	-4.3	355%
Associates	0.3	0.0	N/A	0.6	-50%	0.3	3.8	-92%
JV	0.0	0.0	N/A	0.0	N/A	0.0	0.0	N/A
PBT	42.3	37.5	13%	43.0	-2%	79.8	90.1	-12%
Tax	-9.0	-8.9	1%	-9.3	-4%	-17.9	-20.9	-14%
PAT	33.3	28.6	16%	33.6	-1%	61.9	69.3	-11%
MI	0.3	0.8	-67%	1.3	-80%	1.1	2.5	-56%
Net Profit	33.0	27.8	19%	32.3	2%	60.8	66.8	-9%
Exceptionals	0.7	1.9	-64%	-5.3	N/A	2.6	-6.3	N/A
CNP	32.3	25.9	25%	37.6	-14%	58.2	73.1	-20%
DPS	3.0	0.0	N/A	3.0	0%	3.0	3.0	0%
EBIT margin	7.7%	8.0%		7.6%		7.8%	7.2%	
Pretax margin	7.0%	7.2%		7.7%		7.1%	7.6%	
NP margin	5.5%	5.5%		6.0%		5.5%	5.9%	
CNP margin	5.3%	5.0%		6.7%		5.2%	6.2%	
Net gearing (x)	0.12	0.07		-0.46		0.12	-0.46	
Effective tax	21.3%	23.7%		21.7%		22.4%	23.2%	

Source: Company, Kenanga Research

Segmental Breakdown								
FYE Dec (RM m)	2Q	1Q	QoQ	2Q	YoY	1H	1H	YoY
	FY23	FY23	Chg	FY22	Chg	FY23	FY22	Chg
Revenue								
Construction	535.6	469.1	14%	523.0	2%	1,004.7	1,110.7	-10%
Precast Concrete	68.5	53.0	29%	34.9	96%	121.5	71.8	69%
Total Revenue	604.1	522.1	16%	557.9	8%	1,126.2	1,182.5	-5%
Pre-tax Segmentation								
Construction	39.0	36.2	8%	41.1	-5%	75.3	87.3	-14%
Precast Concrete	3.2	1.3	149%	1.9	71%	4.5	2.9	56%
Total PBT	42.3	37.5	13%	43.0	-2%	79.8	90.1	-12%
PAT Segmentation								
Construction	30.0	28.3	6%	32.2	-7%	58.3	67.1	-13%
Precast Concrete	3.2	0.4	808%	1.4	124%	3.6	2.2	63%
Total PAT	33.3	28.6	16%	33.6	-1%	61.9	69.3	-11%
Net Profit Segmentation								
Construction	29.8	27.5	8%	30.9	-4%	57.2	64.6	-11%
Precast Concrete	3.2	0.4	808%	1.4	124%	3.6	2.2	63%
Total Net Profit	33.0	27.8	19%	32.3	2%	60.8	66.8	-9%
PBT margins								
Construction	7.3%	7.7%		7.9%		7.5%	7.9%	
Precast Concrete	4.7%	2.4%		5.4%		3.7%	4.0%	
Total	7.0%	7.2%		7.7%		7.1%	7.6%	

Source: Company, Kenanga Research

Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside (%)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE (%)	Net Div. (sen)	Net Div Yld (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.				
Stocks Under Coverage																	
GAMUDA	OP	4.43	5.15	16.3%	11,799.0	Y	07/2023	35.0	43.6	7.4%	24.7%	12.2	9.8	1.3	10.4%	50.0	11.3%
IJM	MP	1.65	1.67	1.2%	6,018.0	Y	03/2024	9.2	8.6	-2.1%	-6.3%	18.1	19.3	0.6	4.0%	6.0	3.6%
KERJAYA	OP	1.19	1.53	28.6%	1,508.0	Y	12/2023	12.2	14.0	31.0%	14.6%	9.8	8.5	1.4	14.6%	6.0	5.0%
KIMLUN	OP	0.805	0.900	11.8%	284.5	Y	12/2023	10.3	14.1	-5.4%	37.1%	8.1	6.9	0.4	5.2%	1.0	1.2%
SUNCON	OP	1.80	2.12	17.8%	2,327.0	Y	12/2023	11.3	12.6	1.5%	11.7%	14.2	13.5	2.7	17.7%	5.0	2.8%
WCT	OP	0.460	0.600	30.4%	652.3	Y	12/2023	2.5	3.7	-28.6%	48.6%	18.3	12.5	0.2	2.7%	0.5	1.1%
Sector Aggregate					22,588.8					5.0%	16.9%	14.2	12.1	0.9	6.5%		4.2%

Source: Kenanga Research

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Stock ESG Ratings:

	Criterion	Rating				
GENERAL	Earnings Sustainability & Quality	★	★	★	☆	
	Corporate Social Responsibility	★	★	★	★	
	Management/Workforce Diversity	★	★	★	★	
	Accessibility & Transparency	★	★	★	★	☆
	Corruption-Free Pledge	★	★	★	★	
	Carbon-Neutral Initiatives	★	★	★	★	☆
SPECIFIC	Migrant Worker Welfare	★	★	★	★	
	Waste Disposal/Pollution Control	★	★	★	★	
	Work Site Safety	★	★	★	★	
	Environmentally Friendly Construction Technology	★	★	★	★	
	Supply Chain Auditing	★	★	★	★	
	Energy Efficiency	★	★	★	★	
OVERALL		★	★	★	★	

☆ denotes half-star
 ★ -10% discount to TP
 ★★ -5% discount to TP
 ★★★ TP unchanged
 ★★★★ +5% premium to TP
 ★★★★★ +10% premium to TP

Stock Ratings are defined as follows:

Stock Recommendations

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
 MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
 UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
 NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
 UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

***Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.

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