

22 May 2020

Construction & Engineering | Construction

Sunway Construction (SCGB MK)

Neutral (Maintained)

Looking Ripe for Mean Reversion

Target Price (Return): MYR1.86 (-5.1%)
 Price: MYR1.96
 Market Cap: USD582m
 Avg Daily Turnover (MYR/USD): 1.42m/0.33m

- **Maintain NEUTRAL with new TP of MYR1.86 from MYR1.72, 5% downside and 2% yield.** We remain optimistic on Sunway Construction's earnings growth recovery. This is supported by its strength in work execution and aggressive ongoing tenders. While we favour its resilience, the stock looks fairly valued now. It already trades at 16.4x P/E to FY21F EPS, close to its 5-year mean average.
- **Impact from Movement Control Order (MCO).** 1Q20 revenue registered at MYR366m (-25% QoQ, -17% YoY). Core net profit came in at MYR18m, a significant decline of 43% QoQ and 39% YoY. The earnings account for 12% of our and 13% of Street forecasts. The decline in revenue was mainly due to the impact from two weeks of Movement Control Order (MCO) during the quarter. Works were not able to progress during this period, which affected billings. We expect a more pronounced impact in the subsequent quarter, as works were seen at a standstill for more than a month.
- **Precast division booked better results.** Revenue was higher 10% YoY, but declined 20% QoQ. On a yearly basis, 1Q20 EBIT of MYR1.4m was >100% higher due to recovery in margin and the low base effect in 1Q19. However, note that the margin has not fully recovered to 4Q19's level of 8.5%. SunCon looks to strengthen the precast division's earnings base through sales of its supplies in Singapore. The demand is to be buoyed by the sizeable launches of Housing & Development Board flats in the country.
- **Earnings adjusted down in FY20F-21F.** 1Q20 earnings came in well below our expectation. This suggests that our estimates on COVID-19's impact previously were likely understated. Following 1Q20 results, we fine-tune our forecasts for FY20-22 by adjusting earnings by -42%, -6% and +7% respectively. We believe SunCon will only see its annual earnings normalise in FY21.
- **Maintain NEUTRAL.** SunCon looks well prepared to properly restart works following the shutdown period, and could potentially recover faster than its peers. Positively, the company was awarded a second big job (>MYR100m) this year, which entails construction-related works for Sunway International School, Subang Jaya. The contract is valued at MYR121m, bringing FY20's new job value to MYR688m. On that note, the company continues to stand out and prove its prowess, despite facing multiple constraints in the sector. Accordingly, we believe SunCon's fundamentals look ripe for a mean-reversion valuation. Hence, our new TP of MYR1.86 is arrived at after pegging its FY21 EPS to P/E of 15.6x (5-year mean of forward P/E).
- **Key risks.** Downside risks include failure to secure new contracts, and prolonged downturns in the retail and property markets. Upside risk could stem from the Government taking a more aggressive tack to pump prime the economy via the resumption of large-scale public infrastructure projects.

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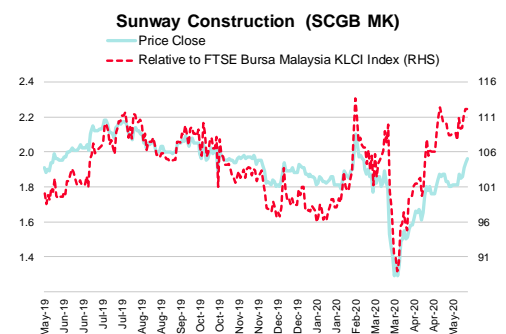


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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	2.6	11.4	0.5	1.6	2.6
Relative	11.2	6.3	5.7	10.4	12.1
52-wk Price low/high (MYR)				1.29	2.18



Source: Bloomberg

Forecasts and Valuation	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Total turnover (MYRm)	2,257	1,769	1,266	2,166	2,216
Recurring net profit (MYRm)	147	116	86	154	154
Recurring net profit growth (%)	11.6	(20.9)	(25.7)	78.1	0.6
Recurring P/E (x)	17.25	21.82	29.38	16.50	16.40
P/B (x)	4.3	4.1	3.8	3.4	3.1
P/CF (x)	13.16	10.71	na	16.16	12.07
Dividend Yield (%)	3.6	3.1	1.7	3.0	3.0
EV/EBITDA (x)	9.88	12.30	15.06	9.44	8.86
Return on average equity (%)	25.5	19.7	13.4	21.8	19.8
Net debt to equity (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, RHB

Financial Exhibits

Asia	Financial summary (MYR)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
Malaysia	Recurring EPS	0.11	0.09	0.07	0.12	0.12
Construction & Engineering	DPS	0.07	0.06	0.03	0.06	0.06
Sunway Construction	BVPS	0.46	0.48	0.52	0.57	0.63
SCGB MK	Return on average equity (%)	25.5	19.7	13.4	21.8	19.8
Neutral						
	Valuation metrics	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Recurring P/E (x)	17.25	21.82	29.38	16.50	16.40
	P/B (x)	4.3	4.1	3.8	3.4	3.1
	FCF Yield (%)	5.4	9.0	(5.3)	4.0	6.1
	Dividend Yield (%)	3.6	3.1	1.7	3.0	3.0
	EV/EBITDA (x)	9.88	12.30	15.06	9.44	8.86
	EV/EBIT (x)	11.99	16.35	21.61	12.06	11.61
	Income statement (MYRm)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Total turnover	2,257	1,769	1,266	2,166	2,216
	Gross profit	447	121	364	423	422
	EBITDA	215	170	148	232	236
	Depreciation and amortisation	(38)	(42)	(45)	(50)	(56)
	Operating profit	177	128	103	181	180
	Net interest	8	12	5	4	6
	Pre-tax profit	183	148	109	193	194
	Taxation	(38)	(27)	(22)	(40)	(40)
	Reported net profit	145	120	86	154	154
	Recurring net profit	147	116	86	154	154
	Cash flow (MYRm)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Change in working capital	(10)	86	(210)	(47)	(0)
	Cash flow from operations	193	237	(79)	157	210
	Capex	(56)	(8)	(55)	(55)	(55)
	Cash flow from investing activities	(74)	(51)	(55)	(55)	(55)
	Dividends paid	(97)	(91)	(43)	(77)	(77)
	Cash flow from financing activities	(118)	72	(5)	(69)	(69)
	Cash at beginning of period	487	485	693	553	586
	Net change in cash	0	257	(139)	33	85
	Ending balance cash	489	741	553	586	671
	Balance sheet (MYRm)	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Total cash and equivalents	485	693	574	606	692
	Tangible fixed assets	163	139	149	154	153
	Total investments	45	49	49	49	49
	Total assets	1,754	1,905	1,556	2,047	2,157
	Short-term debt	114	233	253	243	233
	Total long-term debt	0	62	62	62	62
	Total liabilities	1,162	1,280	888	1,302	1,334
	Total equity	593	625	668	745	822
	Total liabilities & equity	1,754	1,905	1,556	2,047	2,157
	Key metrics	Dec-18	Dec-19	Dec-20F	Dec-21F	Dec-22F
	Revenue growth (%)	8.7	(21.6)	(42.7)	113.5	2.3
	Recurrent EPS growth (%)	11.6	(20.9)	(25.7)	78.1	0.6
	Gross margin (%)	19.8	6.8	28.8	19.5	19.0
	Operating EBITDA margin (%)	9.5	9.6	11.7	10.7	10.7
	Net profit margin (%)	6.4	6.8	6.8	7.1	7.0
	Capex/sales (%)	2.5	0.5	4.3	2.5	2.5
	Interest cover (x)	21.3	9.7	7.7	13.4	13.8

Source: Company data, RHB

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Figure 1: SunCon's results review

FYE Dec (MYRm)	1Q19	4Q19	1Q20	QoQ (%)	YoY (%)	1Q19	1Q20	YoY (%)	Comments
Revenue	440.0	485.9	365.8	(24.7)	(16.9)	440.0	365.8	(16.9)	Impacted by two weeks of MCO
EBIT	35.8	34.4	18.7	(45.6)	(47.8)	35.8	18.7	(47.8)	Lower due to higher admin expenses
<i>EBIT Margin (%)</i>	8.1	7.1	5.1			8.1	5.1		
Interest expense	(2.3)	(3.4)	(2.7)	(20.4)	17.8	(2.3)	(2.7)	17.8	
Interest income	4.2	8.7	5.2	(39.4)	24.1	4.2	5.2	24.1	
JV/Associates	0.0	4.4	0.0	(100.0)	nm	0.0	0.0	nm	
EI/Others	2.4	2.6	(1.2)	(146.9)	(149.9)	2.4	0.0	(100.0)	
Pretax profit	40.1	35.6	21.2	(40.3)	(47.1)	40.1	21.2	(47.1)	Contraction in margin
<i>Pretax Margin (%)</i>	9.1	7.3	5.8			9.1	5.8		
Tax	(8.5)	(2.5)	(4.3)	69.9	(49.2)	(8.5)	(4.3)	(49.2)	
<i>Effective tax rate (%)</i>	(21.2)	(8.1)	(20.3)			(21.2)	(20.3)		
Minority Interest	(0.6)	0.5	(0.6)	0.0	0.0	(0.6)	(0.6)	(8.6)	
Net Profit	31.0	33.5	16.4	(51.2)	(47.3)	31.0	16.4	(47.3)	
Core Profit	28.6	30.9	17.6	(43.2)	(38.7)	28.6	17.6	(38.5)	
<i>Core Net Margin (%)</i>	6.5	6.4	4.8			6.5	4.8		

Source: Company data, RHB

Figure 2: SunCon's segmental results

FYE Dec (MYRm)	1Q19	4Q19	1Q20	QoQ (%)	YoY (%)	1Q19	1Q20	YoY (%)	Comments
Revenue:									
Construction	407.0	440.5	329.6	(25.2)	(19.0)	407.0	329.6	(19.0)	Impacted by MCO
Precast Concrete	33.0	45.4	36.2	(20.3)	9.7	33.0	36.2	9.7	Lower utilisation rate
EBIT:									
Construction	37.9	27.0	17.3	(35.9)	(54.4)	37.9	17.3	(54.4)	
Precast Concrete	0.3	3.9	1.4	(63.5)	330.3	0.3	1.4	330.3	
EBIT Margin %:									
Construction	9.3%	6.1%	5.2%			9.3%	5.2%		
Precast Concrete	1.0%	8.5%	3.9%			1.0%	3.9%		

Source: Company data, RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-04-23	Neutral	1.72	1.76
2020-04-09	Neutral	1.51	1.67
2020-02-21	Neutral	1.95	1.95
2020-02-18	Neutral	1.95	1.97
2020-02-18	Neutral	1.95	1.97
2019-11-20	Neutral	1.95	1.97
2019-10-09	Neutral	2.03	1.95
2019-08-20	Neutral	2.09	2.05
2019-05-17	Neutral	2.12	1.90

Source: RHB, Bloomberg

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