

Sunway Construction SCOG.KL SCGB MK

EQUITY: ENGINEERING & CONSTRUCTION

Construction works back to normalized levels

Precast remains weak, maintain Buy with TP of MYR2.20

2Q20 results review; adjust earnings, but maintain Buy

- SunCon reported 3Q20 adjusted net income of MYR24mn, which was down 28% y-y. However, sequentially net income was up strongly (from just MYR2mn in 2Q20, which was impacted by the lockdown in Malaysia and Singapore). Cumulatively, 9M20 adjusted net income of MYR43mn (-56% y-y) formed 54%/ 56% of our revised/consensus estimates for the full-year.
- As per management, construction activity has now resumed to pre-COVID levels in Malaysia and in Singapore, and all jobs have been given a green light to start work as of 30 Sept 2020. Recall that by the end of Jun-20, only ~20% works had begun in Singapore. Therefore, we expect further improvement in earnings q-q in 4Q20.
- SunCon reported negative operating cash flows (OCF) of MYR55mn in 3Q20 vs positive OCF of MYR105mn in 2Q20 and MYR3mn in 3Q19. The group has net cash position of MYR318mn as of end-3Q20. YTD orderbook replenishment stands at ~MYR2.3bn (excluding the reduction of MYR883mn in LRT3 contract sum). Note that the effective YTD orderbook replenishment (taking into account the effective share of SunCon in JVs) is MYR2bn. Current tenderbook stands at MYR5.3bn, of which >50% is overseas including India, Singapore and the Philippines.
- We raise our FY20F/21F earnings by 8%/ 1% due to higher project billings but lower margins. Orderbook replenishment targets for FY20F/ 21F are at MYR2bn/ 1.9bn (vs MYR2bn each earlier).

Maintain Buy and TP unchanged at MYR2.20, implying 20% upside

We reiterate our Buy rating on SunCon as: 1) it is likely to be a beneficiary of positive news flows from project awards in Malaysia on the revival of infra jobs and projects from parentco, and also overseas job wins from India; 2) we believe SunCon is the best pure-play exposure within our coverage to the construction sector in Malaysia with strong earnings to cash flow conversion, net cash balance sheet, and high ROE (FY21F: 22%); and 3) we expect its precast business to grow again with the opening of a new precast plant in Singapore. We value SunCon at a FY21F P/E of 20x (premium valuation for strong orderbook momentum) (unchanged; current: 16.4x; FY21F EPS of 11sen), to arrive at our TP of MYR2.20 (unchanged).

Year-end 31 Dec	FY19	FY20F		FY21F		FY22F	
Currency (MYR)	Actual	Old	New	Old	New	Old	New
Revenue (mn)	1,769	1,169	1,383	1,834	2,034	2,263	1,934
Reported net profit (mn)	129	72	78	143	144	161	141
Normalised net profit (mn)	129	72	78	143	144	161	141
FD normalised EPS	10.02c	5.58c	6.05c	11.08c	11.16c	12.42c	10.92c
FD norm. EPS growth (%)	-13.8	-44.3	-39.6	98.7	84.4	12.0	-2.1
FD normalised P/E (x)	18.3	-	30.2	-	16.4	-	16.8
EV/EBITDA (x)	10.6	-	16.0	-	9.7	-	9.3
Price/book (x)	3.8	-	3.8	-	3.4	-	3.2
Dividend yield (%)	3.8	-	2.3	-	4.3	-	4.2
ROE (%)	21.3	11.6	12.5	21.8	21.8	22.3	19.7
Net debt/equity (%)	net cash	net cash	net cash	net cash	net cash	net cash	net cash

Source: Company data, Nomura estimates

Rating Remains	Buy
Target price Remains	MYR 2.20
Closing price 19 November 2020	MYR 1.83
Implied upside	+20.2%
Market Cap (USD mn)	577.6
ADT (USD mn)	0.1

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3Q20 results review

- Continued orderbook replenishment due to the support from the parentco remains one of the bright spots for SunCon. In 3Q20, MYR 1.26bn worth new contracts were bagged by SunCon. Also in 4Q20 so far, SunCon has won MYR333mn worth contracts mainly from overseas (India) (*see our note*). This implies total orderbook replenishment for YTD 2020 stands at ~MYR2.3bn (this excludes the reduction of MYR883mn in the LRT3 contract sum, also announced this year, *see our note*). Note that the effective YTD orderbook replenishment (taking into account the effective share of SunCon) is MYR2bn (*Fig. 4*).
- Current tenderbook stands at MYR5.3bn, of which >50% is overseas including India, Singapore and the Philippines. In Budget 2021, MYR15bn will be allocated to fund the Pan Borneo Highway, Gemas-Johor Bahru Electrified Double-Tracking Electrified Project and Klang Valley Double Tracking Project Phase One. In addition, several key projects will also be continued, such as Rapid Transit System Link from Johor Bahru to Woodlands, Singapore; and MRT3 in Klang Valley (*see our note*). However, we believe that given the fiscal constraints the Malaysian government faces, relying only on Malaysian mega-projects for orderbook replenishment is a risky strategy. As a result, we find contractors are likely to be even more committed to international diversification going forward as flagged in our multi-sector report (*The four 'R's*).
- SunCon reported negative operating cash flows (OCF) of MYR 55mn in 3Q20 vs positive OCF of MYR105mn in 2Q20 and MYR3mn in 3Q19. The group has net cash position of MYR318mn as of end-3Q20.
- Construction:** Construction revenue for 3Q20 was MYR403mn, up 11% y-y. However, PBT was marginally down 2% y-y.
- Precast:** Precast revenue for 3Q20 was MYR16mn (-57% y-y) and the division reported PBT of MYR1mn.

Fig. 1: SunCon – 9M20 results snapshot

MYR mn	9M20	NMR FY20F new	as % of NMR new	Cons FY20F	as % of cons
Revenue	925	1,383	67%	1,515	61%
Adj PBT	60	97	61%	97	61%
Adj NPATAMI	43	78	54%	76	56%
Reported NPATAMI	43	78	54%	76	56%

Source: Company data, Bloomberg consensus, Nomura estimates

Fig. 2: SunCon – 3Q20 results review

MYR mn	3Q20	3Q19	% chg y-y	2Q20	% chg q-q	9M20	9M19	% chg y-y	FY20F new	as % of FY20F new
Revenues	419	403	4%	140	>100%	925	1,283	(28%)	1,383	67%
Construction	403	365	11%	137	>100%	870	1,178	(26%)	1,297	67%
Precast concrete	16	37	(57%)	3	>100%	55	104	(47%)	87	64%
Operating profit	33	34	(4%)	0	>100%	52	110	(53%)	89	58%
Construction	32	34	(6%)	3	>100%	52	108	(52%)		
Precast concrete	1	1	59%	(3)	NM	(1)	2	NM		
Adjusted Pretax profit	36	36	1%	2	>100%	60	117	(49%)	97	61%
Construction	35	35	(2%)	6	>100%	61	117	(48%)	98	62%
Precast concrete	1	0	>100%	(4)	NM	(2)	0	NM	(1)	179%
Core PAT	24	33	(27%)	2	>100%	43	98	(56%)	79	55%
Core PAT - equityholders	24	33	(28%)	2	>100%	43	98	(56%)	78	54%
Other one-off charges	0	0	NM	0	NM	0	0	NM	0	NM
Headline NPAT - equityholders	24	33	(28%)	2	>100%	43	98	(56%)	78	54%
Adj Pretax margins	9%	9%	0 ppt	2%	7 ppt	6%	9%		7%	
Construction	9%	10%	-1 ppt	4%	4 ppt	7%	10%		8%	
Precast concrete	8%	1%	7 ppt	(118%)	126 ppt	(3%)	0%		(1%)	

Source: Company data, Nomura estimates

Fig. 3: SunCon's outstanding orderbook

Including projects won in 4Q20 so far

MYR mn	Contract Sum	Outstanding order book
Infrastructure/Piling		
MRT V201 + S201 (Sg Buloh-Persiaran Dagang)	1,213	36
LRT3: Package GS07-08	2,178 1,295	1,589 655
Piling Works	99	7
Sentual West Station	57	50
Chan Sow Lin KVMRT UG St (MEP)	54	52
Building		
Putrajaya Parcel F	1,610	20
PPA1M project in Kota Bharu	582	58
TNB HQ Campus	781	614
Petronas Leadership Center	310	248
Oxley Tower	68	63
IOI Mall	68	45
India		
Thorapalli Agraharam - Jittandahalli	508	508
Meensurutti - Chidambarm 32km	315	315
Internal		
Sunway Medical Centre Phase 4	450	327
Sunway Serene - Serviced Residences	413	218
Velo 2	352	231
3C4	100	58
Sunway GEOLake	223	36
Carnival Mall Ext	286	196
SMC Seberang Jaya	180	129
Big Box Hotel	100	42
Parcel CP2	119	49
SIS	121	117
CP2	344	344
Belfield residential condo	403	403
Sunway Velocity TWO	253	253
Sunway resort hotel & Spa renovation	81	78
Sunway Intl School (add VO)	15	15
Sunway Medical Phase 4 (add VO)	162	162
Renewable energy	7	7
Rooftop solar	18	18
Singapore		
Precast	331	247
Precast - New order 2020	37	38
Total	11,014	5,639
Orderbook burn rate (FY19, including internal)		2,668
Implied earnings visibility (years)		2.1

Source: Company data, Nomura research

Fig. 4: SunCon: YTD contract wins

Project	Duration	Contract Sum (MYR mn)	Effective Contract Sum (MYR mn)
Thorapalli Agraharam - Jittandahalli	24 months	508	305
Bukit Batok Primary School	various	1	1
Rooftop solar projects	<6months	7	7
Chan Sow Lin KVMRT UG St (MEP)	12 months	54	54
Sunway Intl School	30 months	121	121
Ang Mo Kio N6C34	24 months	37	37
CP2	40 months	344	344
Belfield residential condo	45 months	403	403
Sunway Intl School (add VO)	30 months	15	15
Sunway resort hotel & Spa renovation	13 months	81	81
Sunway Medical Phase 4 (add VO)	22 months	162	162
Sunway Velocity TWO	34 months	253	253
Meensurutti - Chidambarm 32km	24 months	315	189
Rooftop solar	12 months	18	18
Total		2,319	1,990

Source: Company data, Nomura research

Fig. 5: SunCon – changes to estimates

MYR mn	Old			New			% change		
	FY20F	FY21F	FY22F	FY20F	FY21F	FY22F	FY20F	FY21F	FY22F
Orderbook replenishment	2,000	2,000	2,000	2,027	1,900	2,000	1%	(5%)	0%
External	700	1,200	1,200	611	1,200	1,200	(13%)	0%	0%
Internal	1,200	500	500	1,379	500	500	15%	0%	0%
Precast	100	300	300	37	200	300	(63%)	(33%)	0%
Revenue	1,169	1,834	2,263	1,383	2,034	1,934	18%	11%	(15%)
Adj PBT	90	179	201	97	181	177	9%	1%	(12%)
PBT margins	7.7%	9.8%	8.9%	7.0%	8.9%	9.1%	(0.6 ppt)	(0.9 ppt)	0.3 ppt
Adj NPAT	72	143	161	78	144	141	8%	1%	(12%)

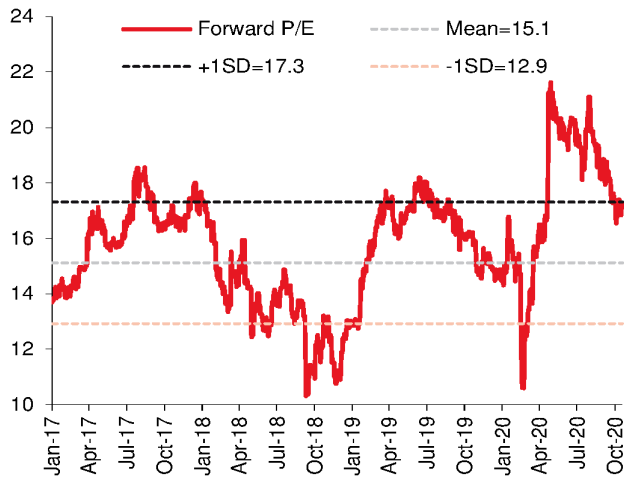
Source: Nomura estimates

Fig. 6: SunCon – Target price valuation methodology

	FY21F
Normalised net profit (MYR mn)	144
FD number of shares outstanding (mn)	1,291
FD EPS (MYR/ sh)	0.11
Target FY21F P/E	20.0 x
Price target (MYR/ sh)	2.20

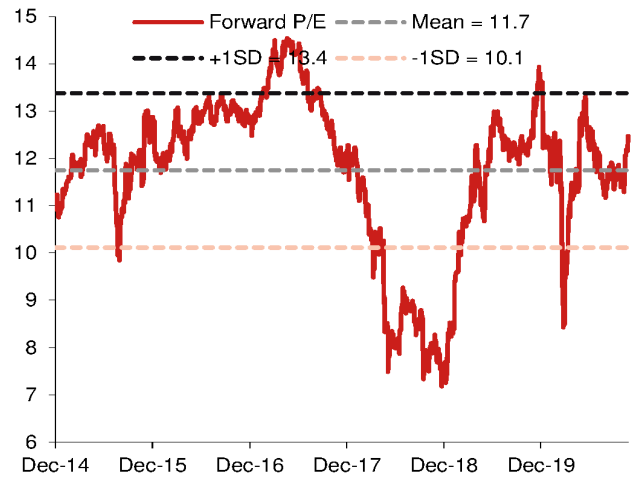
Source: Nomura estimates

Fig. 7: SunCon forward P/E (consensus)



Source: Bloomberg consensus, Nomura research

Fig. 8: KLCON forward P/E (FY21) - consensus



Source: Bloomberg consensus, Nomura research

Appendix A-1

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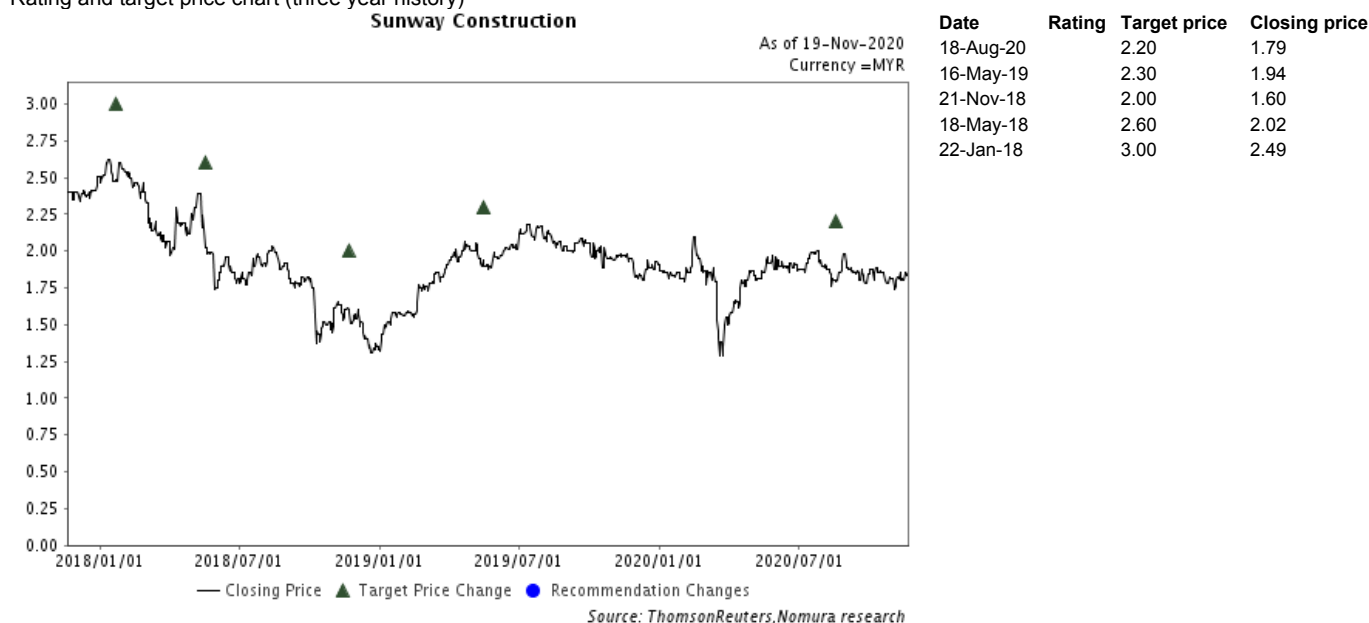
Materially mentioned issuers

Issuer	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
Sunway Construction	SCGB MK	MYR 1.83	19-Nov-2020	Buy	N/A	

Sunway Construction (SCGB MK)

MYR 1.83 (19-Nov-2020) Buy (Sector rating: N/A)

Rating and target price chart (three year history)



For explanation of ratings refer to the stock rating keys located after chart(s)

Valuation Methodology We value SunCon at a target P/E of 20x on FY21F earnings. Using net income of MYR144mn for FY21F and a target P/E of 20x, we arrive at our TP of MYR2.20. The benchmark index for the stock is FTSE Bursa Malaysia KLCI Index.

Risks that may impede the achievement of the target price Downside risks include: 1) delays in construction project awards; 2) lower-than-expected margins; 3) lower pre-cast earnings persisting; 4) a lack of new projects; 5) risk of project cancellation or arbitration.

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As at 30 September 2020.

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