

27 February 2018

Construction & Engineering | Engineering & Construction

## Sunway Construction Group

**Buy** (Maintained)

### Secures About MYR0.5bn Worth Of Jobs In 2M18

Target Price: MYR2.70  
 Price: MYR2.46  
 Market Cap: USD814m  
 Bloomberg Ticker: SCGB MK

Sunway Construction's FY17 earnings missed our and consensus estimates. While quarterly revenue rose to record levels, EBIT margins fell as a result of higher building and internal works being billed, as opposed to infrastructure-related works that deliver 2-3ppt higher margins. Still, we remain upbeat on the company's prospects, as it secured almost MYR0.5bn worth of jobs in 2M18 and the appointment of the HSR PDP is imminent – which, in our estimate, would boost the company's fair value by MYR0.30 to MYR3.00. Maintain BUY, with a TP of MYR2.70 (10% upside).

**Earnings are just off the mark.** Sunway Construction's FY17 core net profit of MYR137.3m, which was a tad shy of our and consensus FY17 forecasts, comprised 90-91.5% of the respective full-year numbers. The slight earnings miss was due to lower-than-anticipated EBIT margins in 4Q17. Along with the results, the company announced a second interim DPS of MYR0.04, bringing FY17 dividends to MYR0.07 – implying a payout of 66% of net profit.

**Higher recognition of lower-margin jobs.** In 4Q17, its quarterly revenue increased 35.3% YoY to MYR721.7m – a record for the company. However, EBIT margins unexpectedly fell to 5.3% in the quarter, compared with 9.5% in 9M17. This, in our view, could be due to a higher proportion of work billings for the building and internal divisions – which we estimate made up 80% of overall construction billings, compared to 20% from infrastructure-related jobs. We assess that infrastructure-related jobs typically carry 2-3ppt higher margins, compared to building or internal jobs.

**Almost MYR0.5bn worth of contracts secured in FY18.** Although projects consist of internal jobs from its parent company, Sunway, we were pleasantly surprised to learn that Sunway Construction secured MYR456m worth of new jobs between January and February. This places the company firmly on track to achieve its internal MYR1.5-2bn job replenishment target, having secured 23% of its stretch-MYR2bn target. We remain slightly more optimistic, forecasting a job replenishment rate of MYR2.2bn for FY18, based on its MYR10-15bn in outstanding tenders.

**High-speed rail (HSR) project delivery partner (PDP) announcement drawing near.** According to the company, the tender bidding related to the PDP for the civil works portion of the Kuala Lumpur-Singapore HSR closed in mid-Feb 2018. In the event Sunway Construction's consortium is appointed, it would be a game changer for the company, in our view. According to our estimates, a PDP win would see an MYR0.30 lift in our valuation for Sunway Construction to MYR3.00 (from MYR2.70), representing an upside of 22% from current levels.

**Maintain BUY.** Our TP of MYR2.70 is unchanged for now, pending the announcement of the HSR PDP. Our TP is pegged to a 2018F ex-cash P/E of 16x, in line with its large-cap peers, Gamuda (GAM MK, BUY, TP: MYR5.70) and IJM Corp (IJM MK, BUY, TP: MYR3.65). This is predicated on its current outstanding orderbook of MYR6.6bn, equivalent to 3.4x its FY17 construction revenue, strong backing from its parent company, and high forecasted 3-year average ROE of 31%.

#### Share Data

Avg Daily Turnover (MYR/USD) 3.49m/0.87m  
 52-wk Price low/high (MYR) 1.70 - 2.62  
 Free Float (%) 35  
 Shares outstanding (m) 1,293  
 Estimated Return 10%

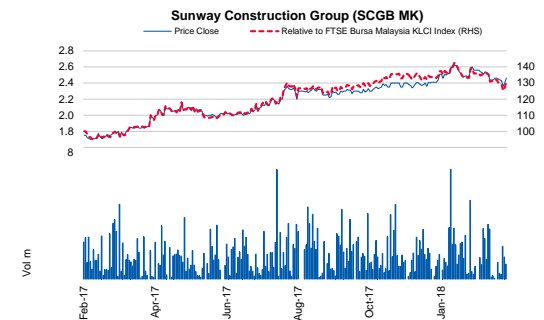
#### Shareholders (%)

Sunway 55.4  
 Employees Provident Fund 3.6  
 Norges 2.1

#### Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(2.0)	(5.4)	2.5	5.1	40.6
Relative	(5.5)	(5.7)	(5.8)	0.0	31.1

Source: Bloomberg



Source: Bloomberg

Forecasts and Valuations	Dec-16	Dec-17	Dec-18F	Dec-19F	Dec-20F
Total turnover (MYRm)	1,789	2,076	2,970	3,164	3,251
Reported net profit (MYRm)	124	138	200	221	227
Recurring net profit (MYRm)	124	138	200	221	227
Recurring net profit growth (%)	(2.9)	11.7	45.2	10.1	3.0
Recurring EPS (MYR)	0.10	0.11	0.15	0.17	0.18
DPS (MYR)	0.05	0.07	0.08	0.09	0.09
Recurring P/E (x)	25.8	23.1	15.9	14.4	14.0
P/B (x)	6.45	6.18	4.93	4.04	3.41
P/CF (x)	na	21.2	8.7	11.6	11.5
Dividend Yield (%)	2.0	2.8	3.3	3.5	3.7
EV/EBITDA (x)	15.2	14.0	8.5	7.4	6.6
Return on average equity (%)	26.2	27.4	34.5	30.8	26.4
Net debt to equity	net cash	net cash	net cash	net cash	net cash
Our vs consensus EPS (adjusted) (%)			18.2	0.0	0.0

Source: Company data, RHB

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## Financial Exhibits

Financial model updated on : 2018-02-26.

Asia	<b>Financial summary</b>	<b>Dec-16</b>	<b>Dec-17</b>	<b>Dec-18F</b>	<b>Dec-19F</b>	<b>Dec-20F</b>
Malaysia	Recurring EPS (MYR)	0.10	0.11	0.15	0.17	0.18
Construction & Engineering	EPS (MYR)	0.10	0.11	0.15	0.17	0.18
<b>Sunway Construction Group</b>	DPS (MYR)	0.05	0.07	0.08	0.09	0.09
Bloomberg SCGB MK	BVPS (MYR)	0.38	0.40	0.50	0.61	0.72
<b>Buy</b>	Weighted avg adjusted shares (m)	1,293	1,293	1,293	1,293	1,293
<b>Valuation basis</b>	<b>Valuation metrics</b>	<b>Dec-16</b>	<b>Dec-17</b>	<b>Dec-18F</b>	<b>Dec-19F</b>	<b>Dec-20F</b>
We value the company based on 16x FY18F EPS, which is at the higher end of our benchmark upcycle 1-year forward target P/E for mid-cap construction stocks. Sunway Construction's net cash position allows the company to gear up for more jobs moving forward.	Recurring P/E (x)	25.8	23.1	15.9	14.4	14.0
	P/E (x)	25.8	23.1	15.9	14.4	14.0
	P/B (x)	6.45	6.18	4.93	4.04	3.41
	FCF Yield (%)	(6.2)	3.0	10.6	8.0	8.0
	Dividend Yield (%)	2.0	2.8	3.3	3.5	3.7
	EV/EBITDA (x)	15.2	14.0	8.5	7.4	6.6
	EV/EBIT (x)	19.2	17.2	10.1	8.7	7.8
<b>Key drivers</b>	<b>Income statement (MYRm)</b>	<b>Dec-16</b>	<b>Dec-17</b>	<b>Dec-18F</b>	<b>Dec-19F</b>	<b>Dec-20F</b>
Sunway Construction's earnings is strongly backed by:	Total turnover	1,789	2,076	2,970	3,164	3,251
i. An outstanding order backlog of MYR6.8bn, of which over 90% is from construction jobs that may keep the firm busy for the next three years;	Gross profit	401	435	688	738	758
ii. Recurring orders from its parent company and key government-linked company clients;	EBITDA	188	202	300	321	331
iii. Its highly profitable precast operation in Singapore.	Depreciation and amortisation	(39)	(38)	(49)	(48)	(50)
	Operating profit	149	165	251	273	281
	Net interest	4	7	1	2	2
	Income from associates & JVs	1	2	0	0	0
	Pre-tax profit	154	174	252	276	284
	Taxation	(30)	(36)	(52)	(56)	(58)
	Minority interests	(0)	0	0	1	1
	Recurring net profit	124	138	200	221	227
<b>Key risks</b>	<b>Cash flow (MYRm)</b>	<b>Dec-16</b>	<b>Dec-17</b>	<b>Dec-18F</b>	<b>Dec-19F</b>	<b>Dec-20F</b>
Downside risks include possible cost overruns and higher material costs.	Change in working capital	(72)	(25)	118	7	2
	Cash flow from operations	(177)	150	367	273	276
	Capex	(19)	(55)	(30)	(20)	(20)
	Cash flow from investing activities	79	35	(30)	(20)	(20)
	Proceeds from issue of shares	0	0	0	0	0
	Dividends paid	(84)	(71)	(70)	(76)	(79)
	Cash flow from financing activities	(84)	(74)	(89)	(94)	(95)
	Cash at beginning of period	390	466	487	751	908
	Net change in cash	(183)	110	248	159	160
	Ending balance cash	208	575	735	910	1,068
<b>Company Profile</b>	<b>Balance sheet (MYRm)</b>	<b>Dec-16</b>	<b>Dec-17</b>	<b>Dec-18F</b>	<b>Dec-19F</b>	<b>Dec-20F</b>
Sunway Construction is one of the largest construction companies in Malaysia. Apart from civil & infrastructure construction services, the company also provides the more specialised:	Total cash and equivalents	466	487	751	908	1,066
i. Foundation & geotechnical engineering services;	Tangible fixed assets	134	97	77	49	19
ii. Mechanical, electrical & plumbing (MEP) services.	Intangible assets	4	4	4	4	4
	Total investments	0	0	0	0	0
	Total other assets	12	2	2	2	2
	Total assets	1,567	1,831	2,302	2,525	2,696
	Short-term debt	137	135	115	95	75
	Other liabilities	0	(16)	0	0	0
	Total liabilities	1,073	1,316	1,656	1,737	1,762
	Shareholders' equity	493	515	645	787	933
	Minority interests	1	1	1	1	1
	Total equity	494	516	646	788	934
	Net debt	(329)	(353)	(636)	(813)	(992)
	Total liabilities & equity	1,567	1,831	2,302	2,525	2,696
	<b>Key metrics</b>	<b>Dec-16</b>	<b>Dec-17</b>	<b>Dec-18F</b>	<b>Dec-19F</b>	<b>Dec-20F</b>
	Revenue growth (%)	(6.7)	16.1	43.0	6.5	2.8
	Recurrent EPS growth (%)	(2.9)	11.7	45.2	10.1	3.0
	Gross margin (%)	22.4	21.0	23.2	23.3	23.3
	Operating EBITDA margin (%)	10.5	9.7	10.1	10.2	10.2
	Net profit margin (%)	6.9	6.6	6.7	7.0	7.0
	Dividend payout ratio (%)	52.3	35.0	35.0	34.7	34.7
	Capex/sales (%)	1.1	2.6	1.0	0.6	0.6
	Interest cover (x)	24.5	27.1	67.1	87.0	110.6

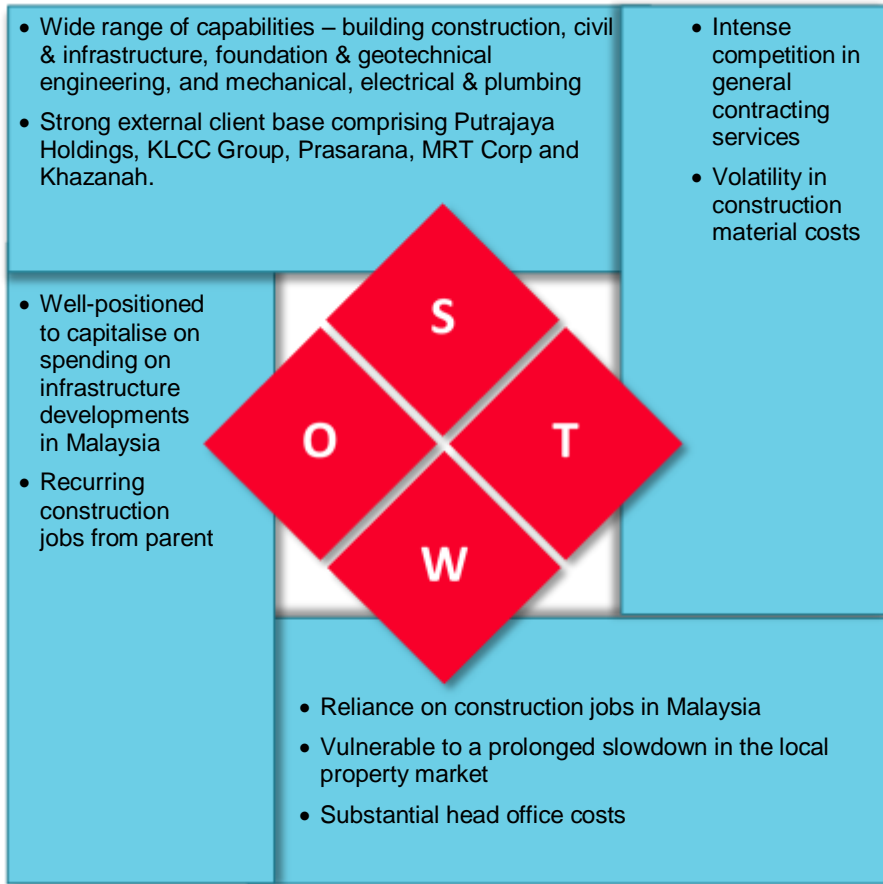
Source: Company data, RHB

Figure 1: Sunway Construction's results review

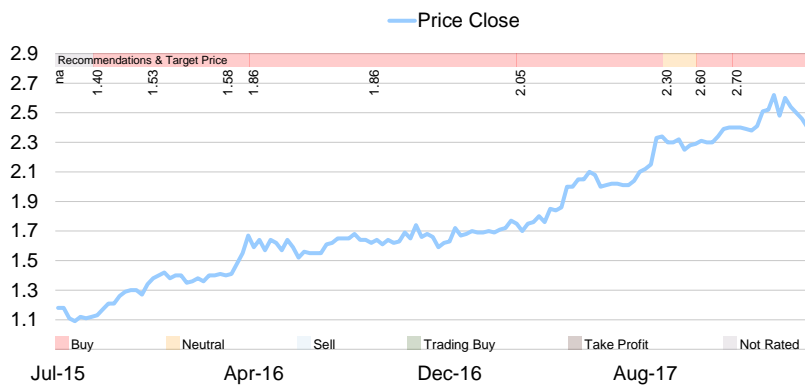
FYE Dec (MYRm)	4Q16	3Q17	4Q17	QoQ (%)	YoY (%)	FY16	FY17	YoY (%)	Comments
<b>Revenue</b>	<b>553.1</b>	<b>491.4</b>	<b>748.2</b>	<b>52.3</b>	<b>35.3</b>	<b>1,788.8</b>	<b>2,076.3</b>	<b>16.1</b>	Higher contribution from the construction segment, which compensated for the reduction in revenue from the precast segment
<b>EBIT</b>	<b>37.0</b>	<b>42.4</b>	<b>39.9</b>	<b>(5.9)</b>	<b>7.7</b>	<b>149.6</b>	<b>166.1</b>	<b>11.0</b>	
<i>EBIT Margin (%)</i>	6.7	8.6	5.3			8.4	8.0		
Interest expense	(1.5)	(2.0)	(1.8)	(9.3)	15.4	(6.1)	(6.1)	0.5	
Interest income	2.1	2.6	5.4	104.6	150.3	10.1	13.5	32.9	
Associates	0.0	0.0	0.0	nm	nm	0.0	0.0	nm	
EI/Others	0.0	0.0	0.7	nm	nm	0.0	0.7	nm	
<b>Pretax profit</b>	<b>37.6</b>	<b>43.1</b>	<b>44.2</b>	<b>2.6</b>	<b>17.4</b>	<b>153.7</b>	<b>174.2</b>	<b>13.3</b>	
<i>Pretax Margin (%)</i>	6.8	8.8	5.9			8.6	8.4		
Tax	(5.7)	(8.6)	(12.0)	40.2	113.1	(30.0)	(36.2)	20.6	
<i>Effective tax rate (%)</i>	(15.0)	(20.0)	(27.3)			(19.5)	(20.8)		
Minority Interest	0.1	0.1	(0.2)	0.0	0.0	0.0	0.0	0.0	
<b>Net Profit</b>	<b>32.1</b>	<b>34.6</b>	<b>31.9</b>	<b>(7.6)</b>	<b>(0.3)</b>	<b>123.5</b>	<b>138.0</b>	<b>11.7</b>	Missed expectations
<b>Core Profit</b>	<b>32.1</b>	<b>34.6</b>	<b>31.2</b>	<b>(9.7)</b>	<b>(2.5)</b>	<b>123.5</b>	<b>137.3</b>	<b>11.1</b>	
<i>Core Net Margin (%)</i>	5.8	7.0	4.2			6.9	6.6		Slightly lower margins due to job mix

Source: RHB

## SWOT Analysis



## Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2017-12-29	Buy	2.70	2.51
2017-11-20	Buy	2.70	2.40
2017-10-06	Buy	2.60	2.29
2017-08-25	Neutral	2.30	2.34
2017-02-24	Buy	2.05	1.75
2016-08-26	Buy	1.86	1.62
2016-07-24	Buy	1.86	1.65
2016-03-29	Buy	1.86	1.67
2016-02-26	Buy	1.58	1.40
2015-11-25	Buy	1.53	1.37

Source: RHB, Bloomberg

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**Neutral:** Share price may fall within the range of +/- 10% over the next 12 months

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