

COMPANY RESULTS

Sunway Construction (SCGB MK)

1H20: In Line. Wins Big Contracts From Sunway

SunCon's 1H20 core net profit came in at 27% of our full-year estimates. We deem the results is in line as we anticipate gradual recovery from 3Q20 onwards and the construction activities likely to restore to pre-MCO level from mid 3Q20. Positively, the company secured two additional new contracts worth RM747m from Sunway Berhad, bringing its ytd job wins of RM1.5b while keeping our earnings forecasts unchanged. Maintain HOLD and target price of RM1.70. Entry price: RM1.55.

2Q20 RESULTS

Year to 31 Dec (RMm)	2020	1Q20	qoq % chg	yoy % chg	1H20	yoy % chg
Revenue	140.2	365.8	(61.7)	(68.2)	506.0	(42.5)
Construction	137.2	329.6	(58.4)	(66.2)	466.8	(42.6)
Precast Concrete	3.0	36.3	(91.8)	(91.2)	39.3	(41.3)
EBIT	0.1	18.7	(99.6)	(99.8)	18.8	(75.3)
Construction	3.4	17.3	(80.2)	(90.7)	20.7	(72.3)
Precast Concrete	(3.3)	1.4	(337.8)	(534.5)	(1.9)	(276.8)
Pre-tax Profit	2.3	21.2	(89.0)	(94.3)	23.6	(71.0)
PATMI	2.2	16.4	(86.6)	(93.4)	18.5	(71.1)
Core PATMI	4.6	17.6	(73.8)	(85.9)	22.1	(63.3)
Margins	%	%	+/-ppt	+/-ppt	%	+/-ppt
Construction	2.5	5.2	(2.8)	(6.6)	4.4	(4.8)
Precast Concrete	-111.9	3.9	(115.8)	(114.2)	-4.9	(6.6)
PBT	1.7	5.8	(4.1)	(7.7)	4.7	(4.6)
PATMI	1.6	4.5	(2.9)	(6.0)	3.7	(3.6)

Source: SunCon, UOB Kay Hian

RESULTS

• **1H20: Within expectations.** Sunway Construction (SunCon) reported 2Q20 core net profit of RM5m (-74% qoq, -86% yoy) on revenue of RM140m (-62% qoq, -68% yoy). Despite 1H20 core net profit coming in at 27% of our full-year forecasts, we deem the results in line as we expect a gradual recovery from 3Q20 driven by construction billings and precast deliveries. We expect construction work activities to restore to pre-MCO levels in mid-3Q20 which will drive construction billings with the delivery of precast products into Singapore and yield better margins. Meanwhile, 1H20 core net profit dropped 63% yoy on lower billings from its construction orderbook backlog and margin contraction as a result of two months of MCO from mid-Mar 20. Positively, SunCon has clinched two new contracts worth RM747m.

KEY FINANCIALS

Year to 31 Dec (RMm)	2018	2019	2020F	2021F	2022F
Net turnover	2,257	1,769	1,311	2,064	2,213
EBITDA	196	161	132	212	216
Operating profit	155	121	92	171	172
Net profit (rep./act.)	144	129	83	149	152
Net profit (adj.)	142	133	83	149	152
EPS (sen)	11.0	10.3	6.4	11.5	11.7
PE (x)	16.4	17.5	27.9	15.6	15.4
P/B (x)	3.9	3.7	3.5	3.2	2.9
EV/EBITDA (x)	10.2	12.4	15.2	9.4	9.2
Dividend yield (%)	2.2	1.9	2.1	3.5	3.3
Net margin (%)	6.4	7.3	6.4	7.2	6.9
Net debt/(cash) to equity (%)	(46.6)	(49.9)	(50.1)	(52.7)	(55.7)
ROE (%)	25.5	21.3	13.0	21.6	19.9
Consensus net profit	-	-	88	148	151
UOBKH/Consensus (x)	-	-	0.95	1.01	1.01

Source: Sunway Construction, Bloomberg, UOB Kay Hian

HOLD

(Maintained)

Share Price	RM1.80
Target Price	RM1.70
Upside	-5.5%

COMPANY DESCRIPTION

A leading construction company in Malaysia

STOCK DATA

GICS sector	Industrials
Bloomberg ticker:	SCGB MK
Shares issued (m):	1,289.4
Market cap (RMm):	2,320.8
Market cap (US\$m):	553.8
3-mth avg daily t'over (US\$m):	0.3

Price Performance (%)

52-week high/low RM2.10/RM1.29

1mth	3mth	6mth	1yr	YTD
(9.5)	(2.7)	(11.8)	(13.0)	(5.8)

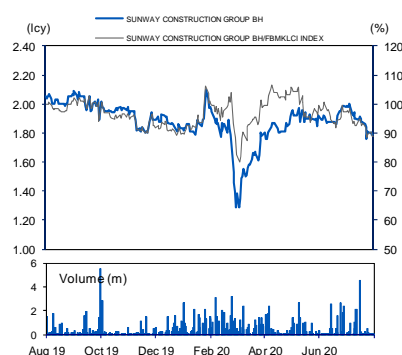
Major Shareholders

	%
Sunway Berhad	54.4
-	-
-	-

FY20 NAV/Share (RM) 0.51

FY20 Net Cash/Share (RM) 0.25

PRICE CHART



Source: Bloomberg

ANALYST(S)

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- Construction: Billings and margins to pick up in 2H20.** Despite reporting weak 1H20 earnings, we expect billings to gradually pick up from 3Q20 onwards and are likely to return to pre-MCO levels from mid-3Q20 onwards with the company complying with standard operating procedures (SOP) at sites (ie ensuring all workers are screened and practice social distancing). However, 2020 construction margins are expected to be affected due to the slower billings in 1H20 - compounded by overhead expenses during the period (which we have conservatively factored into our forecasts). On a positive note, the company has secured two additional sizable contracts from Sunway Bhd worth RM743m, bringing its ytd job wins to RM1.5b. The two new contracts won involve the construction of: a) mixed development project in Sunway South Quay worth RM344m; and b) Sunway Belfield high-rise residential project worth RM403m.

STOCK IMPACT

- Strong and diversified outstanding orderbook.** SunCon's outstanding orderbook backlog of RM5.4b provides earnings visibility for its construction arm for the next 3-4 years. Ytd, SunCon secured new contracts worth RM1.5b. Contracts secured were: a) India Highway (RM508m, secured in 1Q20) via its 60% JV, b) Sunway International School (RM121m) and MRT2 M&E works (RM54m) – both secured in 2Q20, and c) Sunway South Quay (RM344m) and Sunway Belfield (RM403m) - both were secured in Aug 20.
- Not limiting to “bread and butter” contracts.** Traditionally, construction contracts won by SunCon in the past were ready-financed projects from the clients (ie SunCon to bill revenue based on progress billings and to be paid by the client(s) accordingly). Realising the shrinking pool of new contracts locally, the company has embarked on geographical diversification into the ASEAN region and India to win new contracts (both ready-financed projects and private finance initiative projects). For instance, the highway contract won through its JV in India is a private funded initiative (PFI) project. The JV acts as the contractor (and does not bear any traffic risks) for the highway project, and the project's progress payment will be paid by the National Highways Authority of India (NHAI). NHAI will pay the first 40% of the project's value during the construction duration (24 months, with construction works to commence in Oct 20) and the 60% will be paid in annuity during the 15-year concession period. The interest on the deferred payment is based on the Reserve Bank of India's cash reserve ratio of +3%. As such, we believe SunCon will carefully look into all aspects, including the profitability of the projects as well as its ability to manage its cashflow.
- MCO dragged 1H20 performance.** Due to the movement control order (MCO), SunCon's construction activities have been halted for more than two months beginning mid-Mar 20. While SunCon has received approval to restart its construction works from May 20, the costs of adhering to the SOP might erode its margins, with social distancing (meaning less manpower on site) and other costs like thermal screenings. However, we understand that most of SunCon's workers have been tested for COVID-19, while the subcontractors are currently undergoing screening. As such, we expect construction activities would attain its optimum level by mid-3Q20 onwards as most of its workers would have been tested by then with mobilisation works having taken place.

- LRT3 progress to-date.** The MRCB-GKENT JV (LRT3's turnkey contractor) has concluded the design and specification negotiations for the six stations and the bridge design under the SunCon package. Post-design and specification revisions (less facade works, lower number of escalators, removal of subcontractor fees), SunCon expects the JV to be able to reduce station construction costs by at least 30% to below RM40m per station. Conservatively, we had already revised down our projection on SunCon's LRT3 contract value by 35% in our previous note (to RM1.1b, from RM1.7b) factoring in the revised scheme, but with margins unchanged. SunCon is hopeful of finalising the formal review by 1H20, but has already commenced construction works in 1Q20 and should complete the project before the deadline of 2024.

EARNINGS REVISION/RISK

- No changes to earnings forecasts while we conservatively maintain our construction orderbook replenishment assumption of RM1.7b for 2020-22F.

VALUATION/RECOMMENDATION

- Maintain HOLD and target price of RM1.70.** Our target price is based on 13x 2021F PE and net cash position as of 2020F, implying 14.7x PE (trading at 5-year average). We ascribe a higher-than-peers' PE multiple in view of SunCon's solid fundamentals and earnings visibility, underpinned by new contracts secured, its ability to clinch a balanced mix of external and internal construction projects and a strong balance sheet (net cash). Should SunCon hit its orderbook replenishment target of RM2b in 2020, our target price will be RM1.74, based on 13x 2021F PE. Entry price is RM1.55.

TARGET PRICE

		(RMm)	Value (RMm)	Remarks
2021F net profit	A	149		
Net interest (income)/expense after tax	B	-11		
Net profit less net interest income	C=A-B	138	1,792	13x PE
Net cash (as of 2020F)	D	405	405	
Total SOTP value	E=C+D		2,197	
Share base (m)	F		1,292	
				Implied PE (x)
TP (RM)	E/F		1.70	14.7
TP (RM) (ex-cash)	C/F		1.49	13.0

Source: UOB Kay Hian

OUTSTANDING ORDERBOOK AS OF JUN 20

	(RMm)
LRT3**	1,589
Tenaga HQ Campus	666
Petronas Learning Centre	283
India Highway*	508
Others	474
Total External (A)	3,520
Sunway Medical Centre – Phase 4	351
Sunway Serene	240
Sunway Velocity 2	265
Others	713
Total Internal (B)	1,569
Precast (C)	320
Total (A+B+C)	5,414

*New contracts secured in 2020

**Subject to revision. However, based on our estimates, we revised the outstanding contract down by 35% to RM1.1b

Source: Sunway Construction, UOB Kay Hian

ORDERBOOK REPLENISHMENT ASSUMPTIONS

(RMm)	2020F	2021F	2022F
Construction	1,700	1,700	1,700
Precast	100	100	100

Source: UOB Kay Hian

ORDERBOOK REPLENISHMENT FOR YEAR 2020

	RMm
Internal (A)	1,000
Mixed Development	500
Residential	300
Medical Centre	200
External (B)	1,200
Building Works (to secure at least one of the three contracts. Each contract worth RM500m each)	500
Renewable Energy (EPCC) – 60 MW	200
Piling	300
Precast	200
Annual target replenishment for 2020	-2,200
Building works (2 contracts valued RM500m/each)	1,000
Mixed development - Myanmar	250
Toll Highways (RM500m/package), tendered 2 packages	1,000
Other potential job wins	-2,250

Source: Sunway Construction, UOB Kay Hian

PROFIT & LOSS

Year to 31 Dec (RMm)	2019	2020F	2021F	2022F
Net turnover	1,769	1,311	2,064	2,213
EBITDA	161	132	212	216
Deprec. & amort.	40	40	40	44
EBIT	121	92	171	172
Total other non-operating income	20	0	0	0
Associate contributions	4	1	1	1
Net interest income/(expense)	12	11	14	17
Pre-tax profit	157	104	186	190
Tax	(27)	(21)	(37)	(38)
Minorities	(1)	0	0	0
Net profit	129	83	149	152
Net profit (adj.)	133	83	149	152

CASH FLOW

Year to 31 Dec (RMm)	2019	2020F	2021F	2022F
Operating	188	128	192	197
Pre-tax profit	157	104	186	190
Tax	(45)	(21)	(37)	(38)
Deprec. & amort.	40	40	40	44
Working capital changes	28	17	10	6
Other operating cashflows	7	(12)	(7)	(4)
Investing	(51)	(40)	(40)	(40)
Capex (growth)	(8)	(40)	(40)	(40)
Investments	(47)	0	0	0
Proceeds from sale of assets	0	0	0	0
Others	4	0	0	0
Financing	72	(55)	(85)	(78)
Dividend payments	(90)	(50)	(82)	(76)
Issue of shares	0	0	0	0
Proceeds from borrowings	168	0	0	0
Loan repayment	0	0	0	0
Others/interest paid	(6)	(5)	(3)	(2)
Net cash inflow (outflow)	208	31	63	73
Beginning cash & cash equivalent	485	692	724	787
Changes due to forex impact	0	0	0	0
Ending cash & cash equivalent	693	724	787	859

BALANCE SHEET

Year to 31 Dec (RMm)	2019	2020F	2021F	2022F
Other LT assets	195	211	225	237
Cash/ST investment	693	710	763	827
Other current assets	1,017	1,017	1,017	1,017
Total assets	1,905	1,938	2,005	2,081
ST debt	233	233	233	233
Other current liabilities	887	887	887	887
LT debt	148	148	148	148
Other LT liabilities	11	11	11	11
Shareholders' equity	623	656	723	799
Minority interest	2	2	2	2
Total liabilities & equity	1,905	1,938	2,005	2,081

KEY METRICS

Year to 31 Dec (%)	2019	2020F	2021F	2022F
Profitability				
EBITDA margin	9.1	10.0	10.3	9.7
Pre-tax margin	8.9	7.9	9.0	8.6
Net margin	7.3	6.4	7.2	6.9
ROA	7.0	4.3	7.6	7.4
ROE	21.3	13.0	21.6	19.9
Growth				
Turnover	(21.6)	(25.9)	57.4	7.2
EBITDA	(17.6)	(18.3)	60.8	1.9
Pre-tax profit	(13.9)	(33.8)	79.0	1.8
Net profit	(10.5)	(35.6)	79.0	1.8
Net profit (adj.)	(6.3)	(37.4)	79.0	1.8
EPS	(6.3)	(37.4)	78.8	1.8
Leverage				
Debt to total capital	37.9	36.7	34.5	32.3
Debt to equity	61.3	58.2	52.8	47.8
Net debt/(cash) to equity	(49.9)	(50.1)	(52.7)	(55.7)