

### COMPANY UPDATE

## Sunway Construction (SCGB MK)

### Strategising For Growth

Despite the COVID-19 outbreak, SunCon has successfully achieved its orderbook replenishment target of RM2b for 2020. The company is upbeat about securing new contracts worth RM2b annually from 2021 in its efforts to achieve an annual burn rate of RM2b. It also plans to grow big internationally and participate in new tenders via the PFI method, like it did with the NHA1 project. Maintain HOLD. Target price: RM1.70. Entry price: RM1.55.

### WHAT'S NEW

- 2020 – Crossed chequered flag!** Sunway Construction (SunCon) has successfully secured new contracts worth RM2b ytd (effective stake: RM1.8b), driven largely by internal contracts from Sunway Bhd. The company has also met its replenishment target of RM2b for 2020. We understand SunCon is eyeing various precast contracts valued at <RM100m for the rest of 2020, with further upside from other projects it has tendered for, like the India highway project.
- Committed to expanding business organically in coming years.** Despite the shrinking pool of domestic infrastructure projects, SunCon is committed to expanding its business organically in the coming years and to achieve a sustainable burn rate of RM2b annually coupled with maintaining an orderbook cover >2.0x. The company will need to replenish new orders of >RM2b annually from 2021 onwards. Jobs targeted by the company in the future include: a) infrastructure related projects – government hospitals and Rapid Transit Systems; b) Sunway Bhd-Sunway Medical hospitals; and c) international projects like the high-speed rail (HSR) project from India as well as highway and civil infrastructure works in Kalimantan, Indonesia. Meanwhile, for projects under Petronas, we understand the contracts that were tendered previously have been put on hold temporarily by the client as most of the contracts are dependent on commercial viability (ie committed tenancy).
- Flexing muscles.** Being one of the few contractors in town in a net cash position allows the company to tender for private finance initiative (PFI) projects, similar to the highway contract it had won recently in India. The company plans to bid for more PFI contracts in India in the future and the US\$19b HSR in India. From our checks, the 463km HSR project in India connecting Mumbai and Ahmedabad has called for technical bids for the project. SunCon might probably team up with a local company to participate and bid for the civil works subcontract. Should the company require more initial funding to fund such PFI projects, SunCon will source financing via external borrowings and/or via corporate exercises like placements (subject to favourable market capitalisation). We anticipate the company will gradually participate in more PFI-related contracts in the future.

### KEY FINANCIALS

Year to 31 Dec (RMm)	2018	2019	2020F	2021F	2022F
Net turnover	2,257	1,769	1,360	2,007	2,198
EBITDA	196	161	130	212	219
Operating profit	155	121	91	172	175
Net profit (rep./act.)	144	129	82	149	154
Net profit (adj.)	142	133	82	149	154
EPS (sen)	11.0	10.3	6.3	11.5	11.9
PE (x)	17.1	18.3	29.6	16.3	15.8
P/B (x)	4.1	3.9	3.7	3.4	3.0
EV/EBITDA (x)	10.7	13.0	16.1	9.9	9.6
Dividend yield (%)	2.1	1.9	2.0	3.4	3.2
Net margin (%)	6.4	7.3	6.0	7.4	7.0
Net debt/(cash) to equity (%)	(46.6)	(49.9)	(50.0)	(52.6)	(55.8)
ROE (%)	25.5	21.3	12.8	21.7	20.2
Consensus net profit	-	-	76	147	152
UOBKH/Consensus (x)	-	-	1.08	1.02	1.01

Source: SunCon, 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):	2,424.0
Market cap (US\$m):	583.7
3-mth avg daily t'over (US\$m):	0.3

### Price Performance (%)

52-week high/low	RM2.10/RM1.29			
<b>1mth</b>	<b>3mth</b>	<b>6mth</b>	<b>1yr</b>	<b>YTD</b>
0.0	0.0	19.0	(4.1)	(1.6)

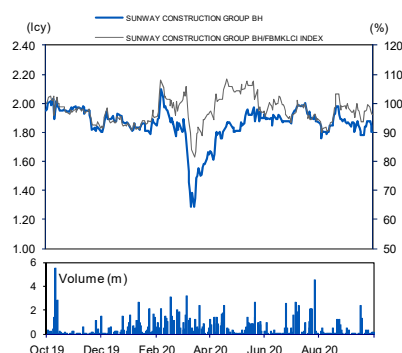
### Major Shareholders

	%
Sunway Berhad	54.4
-	-
-	-

FY20 NAV/Share (RM) 0.51

FY20 Net Cash/Share (RM) 0.25

### PRICE CHART



Source: Bloomberg

### ANALYST(S)

**Farhan Ridzwan**  
 +603 2147 1989  
 farhanridzwan@uobkayhian.com

### STOCK IMPACT

- Strong and diversified outstanding orderbook.** SunCon's outstanding orderbook backlog of RM5.7b provides earnings visibility for its construction arm for the next 3-4 years. Ytd, SunCon has secured new contracts worth RM2.0b. These contracts are: a) India Highway (RM508m, secured in 1Q20) via its 60% JV; b) Sunway International School (RM121m) and MRT2 mechanical and engineering works (RM54m) – both secured in 2Q20; c) Sunway South Quay (RM344m) and Sunway Belfield (RM403m) - both secured in Aug 20; and d) Sunway Velocity Two (RM254m) and Sunway Medical Centre (RM162m) in Oct 20
- 2H20 – Back to normal post-MCO.** From our checks, we understand SunCon's business has been restored to pre-movement control order (MCO) levels. On a positive note, the company hinted that its 3Q20 earnings performance would be similar, or even better, vs 3Q19's. This would have been supported by accelerated billings of its construction orderbook and ongoing cost rationalisation (where it slashed its annual budgeted salary to RM120m in 2020 vs RM150m in 2019). However, this is expected to have been partly dragged by weak performance of its precast arm. The precast division is expected to report weaker earnings due to lower precast deliveries - especially to Singapore amid the border shutdown between Malaysia and Singapore
- Not limiting to “bread and butter” contracts.** Traditionally, construction contracts won by SunCon in the past were ready-financed projects from 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 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. Meanwhile, for future pipeline projects in India, SunCon guided that the contract terms have mitigated the country's historical execution risk
- LRT3 – Concluded and billings to pick up.** The Malaysian Resources Corporation-George Kent JV (LRT3's turnkey contractor) has finalised the contract sum amount with the sum value slashed to RM1.3b (from RM2.2b); the amendments entailed changes in the design and scope of the project. The project is set to be completed in Nov 23. Separately, margins are expected to be slightly positive as the revised contract is on a full-sum contract basis rather than a build-on-quantity contract. This allows SunCon to realise higher profit potential should the company maintain a lean cost structure without compromising on project delivery and safety.
- ICPH to commence operations by mid-22.** The Integrated Construction and Prefabrication Hub (ICPH) in Singapore has an annual capacity of 100,000 cubic metres (cum) and is expected to begin operations by mid-22. It will supply precast products like prefabricated bathroom units and prefabricated volumetric construction products, primarily for Housing Development Board (HDB) flats in Singapore. The 51:49 JV (HL Building Materials: SunCon) is expected to contribute from mid-21 with an estimated bottom line of >S\$5m annually (at the JV level based on 50% utilisation rate). In addition, ICPH's precast products yield better margins (>10%) than Johor's precast products (annual capacity of 150,000 cum).

### EARNINGS REVISION/RISK

- No changes to earnings forecasts while we conservatively maintain our construction orderbook replenishment assumption of RM2.0b for 2020 and RM1.8b for 2021-22.

### 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 (or its 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). Entry price is RM1.55.

### TARGET PRICE

		Value (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 OCT 20

	(RMm)
LRT3	706
Tenaga HQ Campus	666
Petronas Learning Centre	283
India Highway*	508
Others	474
<b>Total External (A)</b>	<b>2,637</b>
Sunway Medical Centre – Phase 4*	513
Sunway Belfield*	403
Sunway Serene	240
Sunway Velocity 2*	253
Others	713
<b>Total Internal (B)</b>	<b>2,731</b>
Precast (C)	320
<b>Total (A+B+C)</b>	<b>5,688</b>

\*New contracts secured in 2020

Source: Sunway Construction, UOB Kay Hian

### ORDERBOOK REPLENISHMENT ASSUMPTIONS

(RMm)	2020F	2021F	2022F
Construction	1,850	1,700	1,700
Precast	150	100	100

Source: UOB Kay Hian

### INDIA HSR ALIGNMENT



Source: National High-Speed Rail Corporation Limited

### PROFIT & LOSS

Year to 31 Dec (RMm)	2019	2020F	2021F	2022F
Net turnover	1,769	1,360	2,007	2,198
EBITDA	161	130	212	219
Deprec. & amort.	40	40	40	44
EBIT	121	91	172	175
Total other non-operating income	20	0	0	0
Associate contributions	4	1	1	1
Net interest income/(expense)	12	11	14	17
<b>Pre-tax profit</b>	<b>157</b>	<b>103</b>	<b>187</b>	<b>193</b>
Tax	(27)	(21)	(37)	(39)
Minorities	(1)	0	0	0
<b>Net profit</b>	<b>129</b>	<b>82</b>	<b>149</b>	<b>154</b>
Net profit (adj.)	133	82	149	154

### CASH FLOW

Year to 31 Dec (RMm)	2019	2020F	2021F	2022F
<b>Operating</b>	<b>188</b>	<b>127</b>	<b>193</b>	<b>200</b>
Pre-tax profit	157	103	187	193
Tax	(45)	(21)	(37)	(39)
Deprec. & amort.	40	40	40	44
Working capital changes	28	17	10	6
Other operating cashflows	7	(12)	(7)	(4)
<b>Investing</b>	<b>(51)</b>	<b>(55)</b>	<b>(55)</b>	<b>(55)</b>
Capex (growth)	(8)	(55)	(55)	(55)
Investments	(47)	0	0	0
Proceeds from sale of assets	0	0	0	0
Others	4	0	0	0
<b>Financing</b>	<b>72</b>	<b>(54)</b>	<b>(85)</b>	<b>(79)</b>
Dividend payments	(90)	(49)	(82)	(77)
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)
<b>Net cash inflow (outflow)</b>	<b>208</b>	<b>17</b>	<b>53</b>	<b>66</b>
Beginning cash & cash equivalent	485	692	710	762
Changes due to forex impact	0	0	0	0
<b>Ending cash &amp; cash equivalent</b>	<b>693</b>	<b>710</b>	<b>762</b>	<b>828</b>

### BALANCE SHEET

Year to 31 Dec (RMm)	2019	2020F	2021F	2022F
Other LT assets	195	211	225	237
Cash/ST investment	693	710	762	828
Other current assets	1,017	1,017	1,017	1,017
<b>Total assets</b>	<b>1,905</b>	<b>1,938</b>	<b>2,005</b>	<b>2,082</b>
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	800
Minority interest	2	2	2	2
<b>Total liabilities &amp; equity</b>	<b>1,905</b>	<b>1,938</b>	<b>2,005</b>	<b>2,082</b>

### KEY METRICS

Year to 31 Dec (%)	2019	2020F	2021F	2022F
<b>Profitability</b>				
EBITDA margin	9.1	9.6	10.6	9.9
Pre-tax margin	8.9	7.5	9.3	8.8
Net margin	7.3	6.0	7.4	7.0
ROA	7.0	4.3	7.6	7.5
ROE	21.3	12.8	21.7	20.2
<b>Growth</b>				
Turnover	(21.6)	(23.1)	47.6	9.5
EBITDA	(17.6)	(19.3)	62.9	3.1
Pre-tax profit	(13.9)	(34.9)	82.0	3.2
Net profit	(10.5)	(36.5)	82.0	3.2
Net profit (adj.)	(6.3)	(38.4)	82.0	3.2
EPS	(6.3)	(38.4)	81.8	3.2
<b>Leverage</b>				
Debt to total capital	37.9	36.7	34.5	32.3
Debt to equity	61.3	58.2	52.8	47.7
Net debt/(cash) to equity	(49.9)	(50.0)	(52.6)	(55.8)