

Sunway Bhd (SWB MK)

Overweight

Price: M\$3.37

19 Sep 2014

Price Target: M\$3.80

PT End Date: 30 Jun 2015

Value unlocking from proposed listing of construction arm; to translate to FY15E net div yield of 10-11%

Sunway's shares hit a high for the year on Friday last week. The group has announced a listing of its construction unit by 2Q15 (subject to various authority approvals). This is positive for Sunway, in our view, as shareholders will receive special cash dividends from proceeds of the IPO and dividend-in-specie via free shares in the new listed vehicle translating to a total estimated net dividend yield of 10-11% for FY15E (including ordinary dividends). The unlocking of value here could see the stock's discount to RNAV narrow. **Sunway (OW) remains our top developer pick and we also like Eco World (OW).** For details please refer to our recent Sunway update of 22 Aug-14 titled, '*So far, so good*' as attached [here](#).

- **Proposes listing of construction arm.** This will see the construction unit listed under a new vehicle, Sunway Construction Group (SWG) by 2Q15. Sunway will sell down its stake to 51-55.7% (from 100%) via an offer for sale of 31-35.7% equity interests to the public and distribution of 13.3% in SWG shares to Sunway shareholders on the basis of 1 share for every 10 shares held.
- **Valuations for construction division based on our existing estimates already built in our RNAV assumptions.** The construction arm to be held by SCG contributes an estimated 11-13% to Sunway's group profits for FY14E/15E and does in-house jobs as well as external work with an existing order-book of M\$3.4B (or over 2x historical revenue) and a tender order-book of M\$3B. SCG recorded a net profit of M\$75MM for FY13 (against a revenue of M\$1.8B), and is estimated to record a net profit of over M\$90MM for FY14E. In our RNAV for Sunway, we have already valued the construction unit at M\$1.15B (book value plus revaluation gain) or M\$0.54 per Sunway share on a fully diluted basis based on 12.5x FY14E PE, a slight discount to sector average of 14x, given its smaller size relative to the bigger listed construction plays (see table for construction peers below). Hence, based on our existing estimated value for the construction unit already built in our RNAV, a sell down of a 31-35.7% stake would raise proceeds of about M\$356-411MM for Sunway.
- **Positive for Sunway.** Loss of earnings with the sell down in its stake in SCG will reduce Sunway's earnings by an estimated 6% for FY15E assuming full impact. However, management guided that a substantial part of the proceeds from the offer for sale will be distributed to shareholders as cash dividends aside from the dividend-in-specie on the basis of 1 SCG share for every 10 Sunway shares held. Assuming 80% of proceeds raised are paid out as special cash dividends, we estimate each shareholder of Sunway will receive M\$0.25-0.29 in dividends (including annual ordinary dividends), or translating to a net dividend yield of 7.3-8.5% for FY15E at current levels. If we include also the dividend-in-specie, total FY15E net yield will rise to an estimated 9.7-11.2%. **To reiterate, the estimates here are all based on the valuations for the construction division of M\$1.15B already built in our RNAV estimates for Sunway (Table 3 and 4).**
- **Remains our top property pick.** Unlocking of value for the construction arm under this exercise could see Sunway's discount to RNAV narrow. The stock is currently trading at 37% discount to RNAV versus the sector's historical mean of 28.5%. We maintain our view that Sunway will likely emerge as one of the preferred sector proxies given lack of quality alternatives with the privatization of IJM Land (OW, our previous Top pick), the departure of key management at SP Setia (Neutral), and the challenges faced by UEM Sunrise (UW, Top Avoid) in Iskandar, Johor due to rising competition. We also like Eco World (OW)

which we just initiated on as per our report of 16th Sept-14 titled, 'New world vintage; initiate with OW' as attached [here](#).

Table 2: Developer peer comparison

As at: 19 Sep-14	FYE	Mkt cap (M\$mn)	Price (M\$)	Rating	Target (M\$)	P/E		EPS growth		Net div yield		P/B FY15E	ROE FY15E	RNAV (M\$)	Prem/disc to RNAV
						CY14E	CY15E	CY14E	CY15E	FY14E	FY15E				
Eco World Develop#	Oct	1,201	1.69 ex 4.75 (cum)	OW	2.40 ex (6.00 cum)	45.3	30.6	-54.4%	47.9%	0.0%	0.0%	1.2	6.1	3.00	-44%
IJB Corporation	Dec	3,845	2.88	UW	2.40	16.3	15.6	13.2%	4.7%	2.2%	2.2%	0.8	5.4	5.02	-43%
IJM Land*	Mar	5,035	3.23	OW	4.00	13.4	12.5	9.7%	7.2%	2.1%	2.5%	1.3	11.0	4.95	-35%
Mah Sing Group	Dec	3,571	2.42	N	2.10	11.9	10.0	18.9%	18.3%	4.0%	4.7%	1.4	18.5	2.58	-6%
SP Setia	Oct	8,300	3.27	N	3.20	15.7	12.5	19.3%	25.0%	3.7%	4.6%	1.3	10.6	5.11	-36%
Sunway	Dec	5,790	3.36	OW	3.80	13.9	12.5	-2.6%	11.5%	2.5%	2.8%	1.0	9.4	5.33	-37%
UEM Sunrise	Dec	8,485	1.87	UW	1.85	14.6	18.8	0.7%	-22.5%	2.1%	2.4%	1.4	6.9	3.20	-42%
Weighted average		36,229				15.5	14.7	7.0%	7.2%	2.6%	3.1%	1.3	9.7		-35%

Source: Bloomberg, J.P. Morgan estimates. * FY15E/16E for IJM Land. # Based on an ex-all price of M\$1.69/share post-restructuring (M\$4.74/share cum-all); RNAV discount is also ex-all.

Table 3: Construction sector peer comparison

As at: 19 Sep-14	Ticker	Mkt cap (US\$mn)	Price (LC)	Rating	Target (LC)	P/E		2yr EPS CAGR 2013-2015	ROE		Div Yld		Net gearing FY14E
						CY14E	CY15E		FY14E	FY15E	FY14E	FY15E	
Gamuda	GAM MK	3,456	4.81	OW	5.50	13.3	11.0	21.3%	14.9	17.2	2.3%	2.9%	16.4%
Hock Seng Lee	HSL MK	313	1.84	NC	-	11.0	9.8	10.2%	15.9	15.3	2.0%	2.3%	-44.3%
IJM Corp	IJM MK	2,935	6.45	OW	7.90	15.5	12.1	21.2%	9.1	10.2	3.9%	2.0%	27.8%
WCT	WCTHG MK	712	2.11	N	2.30	12.1	10.6	6.7%	9.8	9.5	1.4%	1.5%	2.8%
Weighted average		7,417				14.0	11.4	19.4%	12.2	13.6	2.8%	2.4%	17.1%

Source: Bloomberg, J.P. Morgan estimates.

Investment Thesis

We are cautious on the outlook for property developers in 2014 following Budget cooling measures that are expected to impact Iskandar-focused stocks most. While Sunway Bhd (SWB) has some exposure to Iskandar, we believe it commands an edge in terms of location, product concept (landed township) and execution in Iskandar, and that its diversified earnings base will also provide support. We continue to like its long-term fundamentals in view of the following:

1. **Strong commercial asset backing:** Via 34%-owned Sunway REIT, the group owns prime investment properties, with prospects for unlocking value and raising cash here in the next phase of asset injection into its REIT vehicle, which we believe is likely from FY15/16.
2. **Diversified earnings base:** Unlike purer developers, property development accounts for a smaller 50% of SWB's earnings. In Iskandar, SWB is starting from a zero base (with a recent maiden launch in Jul-14), so we believe it has more to gain than to lose, as opposed to the existing Iskandar dominant player, UEM. For now, we have more conservatively forecast that the Medini, Iskandar projects will account for no more than 12%/18% of new property sales over FY14E/15E.
3. **Construction sector growth:** Existing construction order-book of M\$3.7B accounts for 2.3x historical revenue with the group tendering for an additional over M\$2B worth of domestic projects. Higher proportion of domestic construction projects going forward will also contribute to stronger operating margins forecast at 5-6% over FY14E/16E (versus 3-5% over last 3 years).

Valuation

Our Jun-15E PT of M\$3.80 is based on a c.30% discount to RNAV, in line with the sector's historical mean. In a worst-case scenario, stripping out value accretion from Iskandar projects and valuing the assets here at just book or its land cost of M\$20psf (versus recent transactions at M\$35-147psf), our PT would fall to M\$2.50 at a 37% discount to RNAV (-1SD from the historical sector mean).

Table 4: Sunway RNAV

Projects	% stake	Description	Undeveloped land (acres)	Remaining GDV (M\$ M)	Years to develop	Revaluation surplus (M\$ M)	Comments
Selangor/KL							
Sunway Damansara	60%	Residential/commercial township	15	1,691	5	141	Discounted at WACC of 10%
Sunway South Quay	60%	Lakeside mixed development	52	3,990	7	335	Discounted at WACC of 10%
Sunway Monterez	60%	Residential	5	44	3	4	Discounted at WACC of 10%
Sunway Semenyih	70%	Residential	398	729	10	71	Discounted at WACC of 10%
Sunway Cheras	100%	Residential	6	17	3	2	Discounted at WACC of 10%
Sunway Duta	60%	Residential	3	120	3	2	Discounted at WACC of 10%
Sunway Montana	100%	Residential	2	56	3	4	Discounted at WACC of 10%
Sunway Alam Suria	100%	Residential	1	12	2	5	Discounted at WACC of 10%
Sunway Resort City	100%	Commercial	15	660	6	81	Discounted at WACC of 10%
Casa Kiara III	80%	Residential	3	210	3	21	Discounted at WACC of 10%
Sunway Velocity	85%	Mixed development	18	2,859	6	343	Discounted at WACC of 10%
Sunway Tower KL 1	100%	Office	1	240	3	24	Discounted at WACC of 10%
Bangi	100%	Residential	3	59	2	6	Discounted at WACC of 10%
Melawati	100%	Residential	2	43	2	9	Discounted at WACC of 10%
Sg Long	80%	Residential	111	277	4	29	Discounted at WACC of 10%
Mont Putra, Rawang	100%		163	156	6	17	Discounted at WACC of 10%
Perak							
Sunway City Ipoh	65%	Residential	895	1,048	10	97	Discounted at WACC of 10%
Penang							
Sunway City Penang	100%	Residential	16	172	2	20	Discounted at WACC of 10%
Sunway Grand	100%	Residential	12	186	2	22	Discounted at WACC of 10%
Sungai Ara	100%	Residential	56	849	3	101	Discounted at WACC of 10%
Bukit Mertajam	100%	Residential	42	694	2	82	Discounted at WACC of 10%
S'pore							
Novena	30%	Medical suites, retail, hotel	2	2,242	3	177	Discounted at WACC of 10%
Sembawang, Singapore	100%		1	75	2	-	Discounted at WACC of 10%
Johor							
Bukit Lenang	80%	Residential	88	932	5	106	Discounted at WACC of 10%
Medini	38%	Mixed development	691	12,000	10	890	Discounted at WACC of 10%
Pendas	60%	Mixed development	1,079	18,000	15	1,411	Discounted at WACC of 10%
China							
Sunway Guanghao	65%	Mixed development	4	67	2	5	Discounted at WACC of 10%
Tianjin Eco City	60%	Mixed development	91	5,344	6	438	Discounted at WACC of 10%
India							
Sunway OPUS Grand India	50%	Condos	24	702	5	39	Discounted at WACC of 10%
Sunway MAK Signature Residence (JV with M.A.K Builders)	60%		14	181	5	14	Discounted at WACC of 10%
Australia							
Wonderland Business Park (Sydney)	45%		48	378	6	16	Discounted at WACC of 10%
Total			3,861	54,032		4,513.3	

Source: Company data, J.P. Morgan estimates.

Table 5: Sunway RNAV

	Value (M\$ M)	Comments
Revaluation surplus	4,513.3	
Book value as at Dec-14	5,273.7	
Revaluation gain from investment properties	358.5	Valuing 34%-owned Sunway REIT at PT of M\$1.60
Revaluation gain from construction division	734.7	Valued at 12.5x P/E on FY14E
Outstanding cash obligation for land	(515.8)	Discounted value for Iskandar land purchase
Total RNAV	10,364.3	
Number of shares (millions)	1,723.5	
RNAV per share	6.01	
FD RNAV		
<u>Warrants & ESOS</u>		
Add proceeds from warrants & ESOS	1,084.7	258.5mn outstanding warrants at M\$2.50/share and 133.6MM ESOS
Adjusted RNAV	11,449.0	
Fully diluted number of shares	2,146.7	With warrants and ESOS
RNAV per share	5.33	
RNAV per share (rounded off)	3.84	
Price target (30% discount to RNAV)	3.80	

Source: Company data, J.P. Morgan estimates.

Figure 1: Property sector RNAV band



Source: Bloomberg, J.P. Morgan estimates.

Risks to Rating and Price Target

Key downside risks include:

- 1) Slower-than-expected property sales versus our forecast following the Budget 2014 property cooling measures.
- 2) Rising competition in Iskandar. Medini projects, which have yet to be launched and currently have no earnings contribution, account for an estimated 23% of our base-case RNAV.

Real Estate

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Other Companies Discussed in This Report (all prices in this report as of market close on 19 September 2014)
 Eco World Development (ECOW.KL/M\$4.75/Overweight), IJM Land (IJML.KL/M\$3.23/Overweight), SP Setia (SETI.KL/M\$3.26/Neutral), UEM Sunrise Bhd (UMSB.KL/M\$1.85/Underweight)

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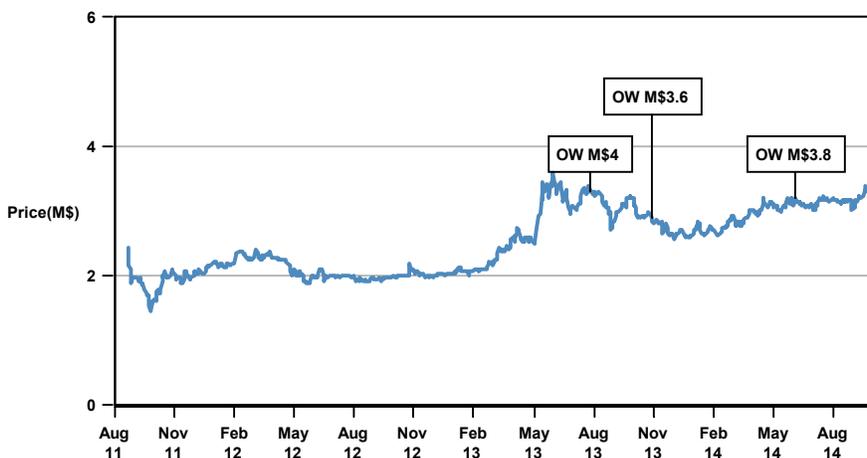
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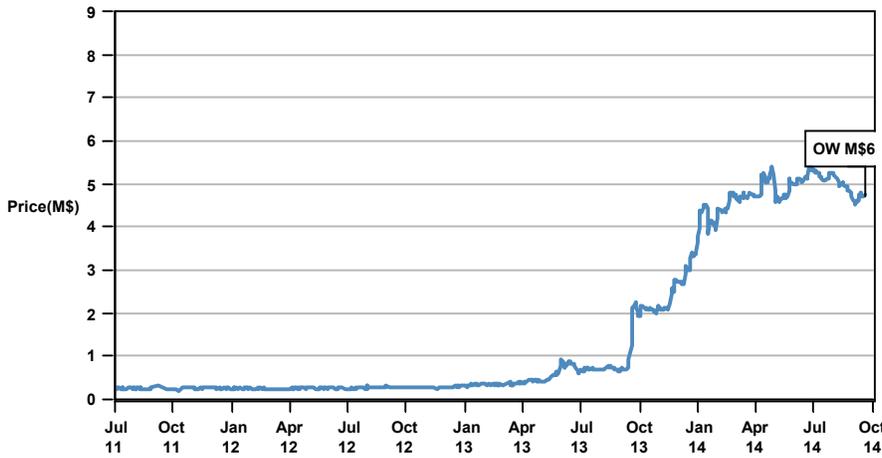
Sunway Bhd (SWAY.KL, SWB MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
26-Jul-13	OW	3.30	4.00
28-Oct-13	OW	2.88	3.60
05-Jun-14	OW	3.21	3.80

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends.
 Initiated coverage Jul 26, 2013.

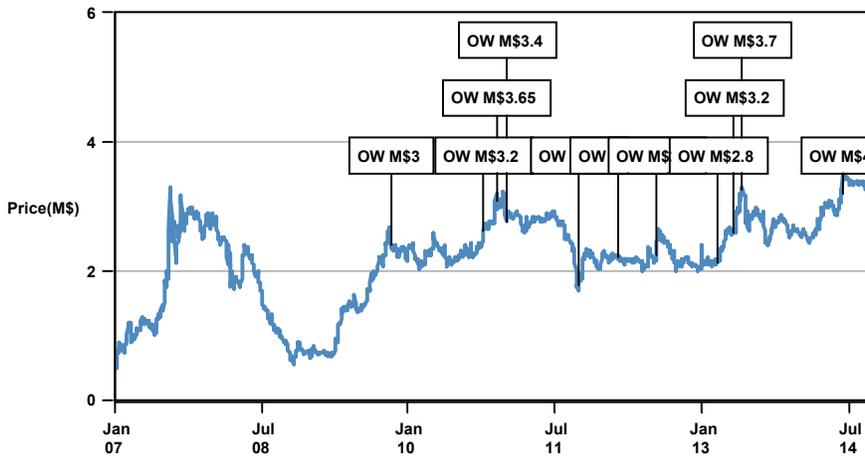
Eco World Development (ECOW.KL, ECW MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
16-Sep-14	OW	4.70	6.00

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Sep 16, 2014.

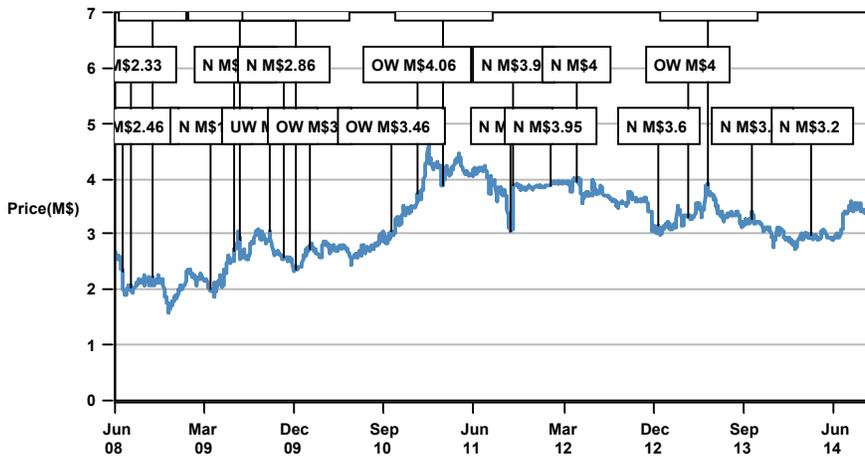
IJM Land (IJML.KL, IJMLD MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
29-Oct-09	OW	2.39	3.00
08-Oct-10	OW	2.61	3.20
24-Nov-10	OW	3.08	3.65
03-Jan-11	OW	2.77	3.40
26-Sep-11	OW	1.79	2.40
22-Feb-12	OW	2.20	2.60
12-Jul-12	OW	2.26	2.90
26-Feb-13	OW	2.13	2.80
28-Apr-13	OW	2.59	3.20
28-May-13	OW	3.25	3.70
10-Jun-14	OW	3.20	4.00

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Oct 29, 2009.

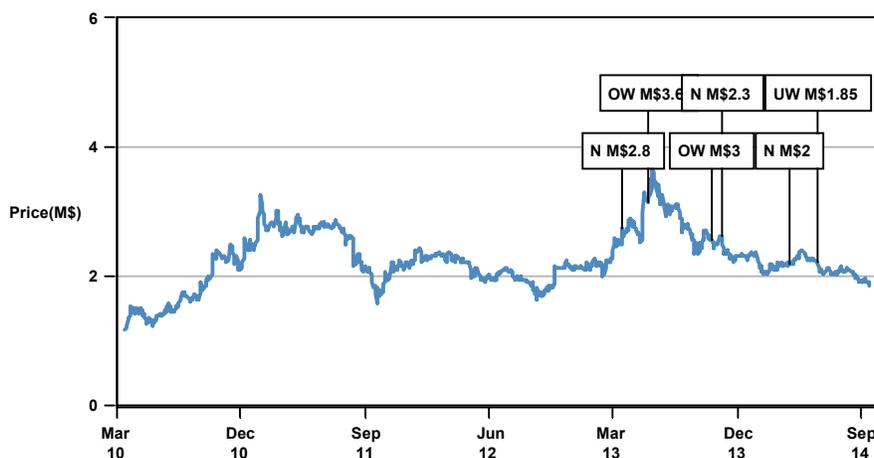
SP Setia (SETI.KL, SPSB MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
24-Jun-08	N	2.33	2.46
16-Jul-08	N	2.04	2.33
25-Sep-08	N	2.21	2.00
19-Mar-09	N	2.01	1.80
02-Jun-09	N	2.71	2.40
18-Jun-09	UW	2.92	2.53
17-Sep-09	UW	3.07	2.60
30-Oct-09	N	2.58	2.86
04-Dec-09	OW	2.39	2.86
14-Jan-10	OW	2.73	3.00
23-Sep-10	OW	3.04	3.46
10-Dec-10	OW	3.72	4.06
28-Feb-11	OW	3.89	4.50
22-Sep-11	N	3.06	3.50
28-Sep-11	N	3.87	3.90
20-Jan-12	N	3.88	3.95
10-Apr-12	N	3.96	4.00
13-Dec-12	N	3.15	3.60
14-Mar-13	OW	3.29	4.00
15-May-13	OW	3.87	4.60
23-Sep-13	N	3.28	3.50
26-Mar-14	N	2.98	3.20

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Jun 24, 2008.

UEM Sunrise Bhd (UMSB.KL, UEMS MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
21-Mar-13	N	2.74	2.80
16-May-13	OW	3.13	3.60
05-Oct-13	OW	2.56	3.00
28-Oct-13	N	2.60	2.30
26-Mar-14	N	2.18	2.00
27-May-14	UW	2.23	1.85

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Mar 21, 2013.

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