

30 May 2014

Buy

Price
RM3.19

Target price
RM4.20

Bloomberg code
SWB MK

Sunway

A good start

Sunway delivered a commendable 1Q14 with normalized earnings improving 22% yoy on the back of better profits from property development and construction. The stock remains one of our top picks in the property sector. For a diversified conglomerate with good earnings visibility, we believe valuations are compelling at 13.5x FY14F PE and 1x PB versus sector 13.7x FY14F and 1.1x PB.

- On a yoy basis, 1Q14 revenue was flat while operating profit increased 35%, driven mainly by the property development and construction divisions. Normalized net profit (upon stripping out RM6.3m in fair value expense for ESOS option) increased 22% yoy, buoyed by lower interest costs as part of the rights proceeds raised in August 2013 were used to pare down borrowings.
- On a qoq basis, 1Q14 revenue was down 24% while operating profit declined 31%, which was largely due to lower performance in property development as a result of lower progress billings and property investment division from seasonal factors. Normalized net profit declined 30% qoq off the higher base in 4Q13, which is typically the strongest quarter.
- Property development revenue was up 10% while EBIT improved 104% yoy attributable to higher profit recognition from local development projects, although contribution from Singapore property projects was lower yoy.
- The group has achieved effective property sales of RM242m as at 1Q14 or 19% of its target of RM1.3bn for FY14. Half of the sales comprised the Singapore project and Sunway Geo Residences (Bandar Sunway). Total launches as at 1Q14 amounted to RM205m, comprising Sunway Wellesley (townhouses and semi-D) and Sunway Eastwood Park villa (superlink homes).
- Property investment revenue improved 2% while EBIT declined 7% yoy. While the hospitality and leisure divisions performed better, this was offset by lower REIT management fees as a result of reclassification to jointly-controlled entity upon the disposal of 20% equity interest in Sunway REIT management last year.
- While construction revenue was down 16% yoy, EBIT picked up strongly by 13% due to stronger profit recognition from contracts that have reached advanced construction stages, enabling higher profits to be recognized.
- The outstanding construction order book stands at RM3.7bn, of which 77% are external jobs and 23% internal jobs. The group has replenished RM178m in order book as at 1Q14, i.e., for the construction of Sunway Medical Center Phase 3, which is trailing behind its target of RM2.5bn for FY14.
- Overall, 1Q14 normalized earnings made up 25% of our full-year forecast, which is a good start given that the first quarter is typically the slowest.

Analyst

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Table 1 : Quarterly performance trends

| (RM m) | Quarter | | | | | | | | | Change | | KAF | |
|--------------------------|-------------|--------------|--------------|--------------|--------------|--------------|--------------|----------------|--------------|-------------|-----------|--------------|-----------|
| | FYE 31 Dec | Mar-12 | Jun-12 | Sep-12 | Dec-12 | Mar-13 | Jun-13 | Sep-13 | Dec-13 | Mar-14 | % qoq | % yoy | FY14F |
| Turnover | 814.8 | 996.1 | 867.0 | 1,241.8 | 1,021.0 | 1,118.0 | 1,066.1 | 1,342.2 | 1,025.7 | (24) | 0 | 4,038.3 | 25 |
| EBIT | 60.5 | 95.7 | 106.1 | 149.1 | 86.0 | 116.6 | 116.2 | 167.8 | 115.9 | (31) | 35 | 534.3 | 22 |
| EBIT margin (%) | 7.4% | 9.6% | 12.2% | 12.0% | 8.4% | 10.4% | 10.9% | 12.5% | 11.3% | | | 13% | |
| Net interest expense | (18.6) | (22.8) | (19.5) | (33.6) | (11.7) | (12.6) | (6.3) | (24.5) | (7.8) | (68) | (33) | (65.5) | 12 |
| Associates and JVs | 42.9 | 35.1 | 56.1 | 73.5 | 47.9 | 48.9 | 49.4 | 83.4 | 40.4 | (51) | (16) | 156.5 | 26 |
| Exceptional items | 0.2 | 85.2 | (0.3) | 23.1 | 0.3 | 59.6 | (41.2) | 1,021.4 | (6.3) | nm | nm | - | nm |
| Profit before tax | 84.9 | 193.1 | 142.4 | 212.1 | 122.5 | 212.5 | 118.2 | 1,248.1 | 142.2 | (89) | 16 | 625.3 | 23 |
| Normalized PBT | 84.7 | 107.9 | 142.7 | 189.0 | 122.2 | 152.9 | 159.4 | 226.7 | 148.5 | (35) | 22 | 625.3 | 24 |
| Tax | (18.5) | (30.3) | (32.4) | (44.1) | (26.3) | (32.5) | (16.6) | (45.5) | (30.4) | (33) | 16 | (126.6) | 24 |
| Minority interest | (2.0) | (8.5) | (15.7) | (21.4) | (5.6) | (9.7) | (8.5) | (63.9) | (7.8) | (88) | 38 | (49.4) | 16 |
| Net profit | 64.4 | 154.3 | 94.3 | 146.6 | 90.6 | 170.3 | 93.1 | 1,138.8 | 104.0 | (91) | 15 | 449.3 | 23 |
| Norm. net profit | 64.2 | 77.6 | 94.6 | 114.2 | 90.3 | 110.7 | 124.4 | 157.5 | 110.3 | (30) | 22 | 449.3 | 25 |

Source: Company, KAF

Income statement

| FYE December (RMm) | 2011A | 2012A | 2013E | 2014F | 2015F |
|------------------------------|--------------|--------------|----------------|--------------|--------------|
| Turnover | 3,691.7 | 4,128.8 | 4,733.7 | 4,038.3 | 5,047.7 |
| EBITDA | 396.6 | 824.7 | 921.1 | 609.5 | 823.1 |
| Depreciation & Amortisation | (90.7) | (89.9) | (136.9) | (75.2) | (112.4) |
| EBIT | 305.9 | 734.8 | 784.2 | 534.3 | 710.8 |
| Net interest | (53.4) | (147.9) | (102.4) | (65.5) | (77.2) |
| Associates | 185.6 | 144.6 | 172.5 | 156.5 | 132.2 |
| Exceptional items | 60.4 | 108.2 | 1,040.1 | - | - |
| Pretax profit | 498.5 | 839.7 | 1,894.3 | 625.3 | 765.8 |
| Taxation | (69.6) | (115.4) | (120.9) | (126.6) | (166.0) |
| Profit after tax | 429.0 | 724.3 | 1,773.4 | 498.7 | 599.8 |
| Minority interest | (41.4) | (285.5) | (273.0) | (49.4) | (76.5) |
| Net profit | 387.6 | 438.8 | 1,500.5 | 449.3 | 523.3 |
| Normalised net profit | 327.1 | 350.7 | 482.9 | 449.3 | 523.3 |

Source: Company, KAF

Balance sheet

| FYE December (RMm) | 2011A | 2012A | 2013E | 2014F | 2015F |
|--|----------------|-----------------|-----------------|-----------------|-----------------|
| Non-current assets | | | | | |
| Property, plant and equipment | 960.6 | 1,562.8 | 857.9 | 1,282.8 | 1,670.4 |
| Investment properties | 888.9 | 4,779.1 | 1,804.3 | 1,804.3 | 1,804.3 |
| Land held for development | 1,017.3 | 598.9 | 877.9 | 877.9 | 877.9 |
| Investment in associates & jointly controlled entity | 1,332.5 | 586.9 | 2,331.1 | 2,487.5 | 2,619.8 |
| Goodwill | 326.5 | 318.1 | 319.9 | 319.9 | 319.9 |
| Deferred tax assets | 33.3 | 33.7 | 37.7 | 37.7 | 37.7 |
| Total non-current assets | 4,559.0 | 7,879.5 | 6,228.8 | 6,810.1 | 7,330.0 |
| Current assets | | | | | |
| Properties under development | 669.3 | 991.5 | 1,276.1 | 1,560.6 | 1,845.2 |
| Inventories | 451.8 | 650.3 | 622.9 | 531.4 | 664.2 |
| Total receivables | 1,319.1 | 1,584.9 | 1,402.6 | 1,196.6 | 1,495.7 |
| Tax recoverable | 67.6 | 47.8 | 55.3 | 55.3 | 55.3 |
| Deposits, cash and bank balances | 776.7 | 1,197.5 | 1,519.1 | 1,033.7 | 740.8 |
| Assets held for sale | - | 12.2 | 7.5 | 7.5 | 7.5 |
| Total current assets | 3,284.6 | 4,484.2 | 4,883.4 | 4,385.0 | 4,808.6 |
| Total assets | 7,843.6 | 12,363.7 | 11,112.3 | 11,195.2 | 12,138.6 |
| Current liabilities | | | | | |
| Total payables | 2,005.6 | 1,844.8 | 2,154.0 | 1,837.6 | 2,296.9 |
| Bank borrowings | 319.2 | 2,955.0 | 1,804.9 | 1,804.9 | 1,804.9 |
| Other liabilities | 1.6 | 0.2 | 0.1 | 0.1 | 0.1 |
| Taxation | 27.1 | 21.0 | 24.0 | 24.0 | 24.0 |
| Total current liabilities | 2,353.4 | 4,821.0 | 3,983.0 | 3,666.6 | 4,126.0 |
| Financed by: | | | | | |
| Share capital | 1,292.5 | 1,292.5 | 1,723.5 | 1,723.5 | 1,723.5 |
| Share premium & Reserves | 1,724.4 | 1,922.3 | 3,611.3 | 3,961.3 | 4,368.9 |
| Shareholders' funds | 3,016.9 | 3,214.8 | 5,334.9 | 5,684.8 | 6,092.4 |
| Minority interest | 327.3 | 2,136.5 | 317.3 | 366.7 | 443.2 |
| Long-term bank borrowings | 1,934.5 | 1,688.4 | 990.6 | 990.6 | 990.6 |
| Other liabilities | 154.9 | 449.7 | 431.1 | 431.1 | 431.1 |
| Deferred tax liabilities | 56.6 | 53.2 | 55.3 | 55.3 | 55.3 |
| Total liabilities & shareholders' funds | 7,843.6 | 12,363.7 | 11,112.3 | 11,195.2 | 12,138.6 |

Source: Company, KAF

Cash flow statement

| FYE December (RMm) | 2011A | 2012A | 2013E | 2014F | 2015F |
|---|----------------|----------------|----------------|----------------|----------------|
| Cashflow from operations (CFO) | | | | | |
| Pretax profit | 498.5 | 839.7 | 1,894.3 | 625.3 | 765.8 |
| Tax paid | (117.0) | (105.3) | (127.3) | (126.6) | (166.0) |
| Others | (124.9) | 778.8 | (943.0) | (15.8) | 57.3 |
| Net change in working capital | 122.9 | (947.1) | 234.3 | (303.4) | (257.1) |
| CFO | 399.0 | 591.8 | 1,093.6 | 179.4 | 400.0 |
| Cashflow from investing (CFI) | | | | | |
| Purchase of property, plant and equipment (Capex) | (337.2) | (414.3) | (612.6) | (500.0) | (500.0) |
| Investments | (54.2) | (227.9) | (163.3) | - | - |
| Others | 98.5 | (60.4) | (129.2) | - | - |
| CFI | (293.0) | (702.6) | (905.1) | (500.0) | (500.0) |
| Cashflow from financing (CFF) | | | | | |
| Interest paid | (66.4) | (180.4) | (117.5) | (103.8) | (103.8) |
| Interest received | 27.5 | 24.2 | 35.6 | 38.3 | 26.6 |
| Repayment of term loans | (44.9) | - | - | - | - |
| Dividends paid | (39.5) | (181.7) | (344.3) | (99.4) | (115.7) |
| Others | (73.0) | 716.5 | 561.6 | - | - |
| CFF | (196.3) | 378.6 | 135.4 | (164.8) | (192.9) |
| Net change in cash and cash equivalents | (90.2) | 267.8 | 323.9 | (485.4) | (292.9) |

Source: Company, KAF

Disclosure Appendix

Recommendation structure

Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price and only reflects capital appreciation. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%.

Performance parameters and horizon: Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Market or sector view: This view is the responsibility of the strategy team and a relative call on the performance of the market/sector relative to the region. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.

Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

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