

Sunway Bhd (SWB MK)

3Q18 slightly below consensus; pre-sales pick-up comes from a low base

Neutral

Price: M\$1.45

21 Nov 2018

Price Target: M\$1.50

PT End Date: 30 Jun 2019

Results were slightly below consensus with 3Q18 core net profit flat Y/Y to leave cumulative earnings at 76%/70% of JPM/consensus. At the operating level, growth of 4%Y/Y in 3Q18 came mainly from stronger domestic billings in the Prop Development and Construction segments. Pre-sales for the cumulative 9M18 period jumped at both the domestic (up 7x) and group (up 1.5x including international) levels, but coming from a low base with few launches over 2016/17. **We are Neutral on SWB**, and at current valuations (P/BV at 0.9x, RNAV discount of 40%) see better value in its peers. **Our top picks are ECW (OW) and SPSB (OW), and we are also OW on UEMS.**

- **Core net profit flat Y/Y in 3Q18**, leaving cumulative 9M18 earnings at 76%/70% of JPM/consensus full-year, with lower JV contribution and higher minority interest erasing operating profit growth of 4%Y/Y. Overall, operating level results were driven by stronger domestic billings in the Prop development and Construction segments, which offset lower building material margins in the Others segment.
- **Segment performance updates:**
 - **Prop Development.** 3Q18 operating profit was up 63%Y/Y on higher domestic progress billings, but partly offset at the EBIT level by lower contribution from JVs after two years of slow launches. Group pre-sales of M\$1.6B made 94%/95% of JPM/management's full-year target of M\$1.7B on high take-up for large international projects such as Rivercove Residences in Singapore (GDV M\$0.6B, 99% take-up) and Sunway Gardens in Tianjin (GDV M\$0.6B, 85% take-up including bookings). Excluding these, underlying domestic pre-sales of M\$554MM made 78% of our M\$712MM domestic forecast on both Klang Valley and Johor projects. Unbilled sales of M\$2.1B is 53% domestic, representing 2.1x historical segment revenue (1.1x for domestic projects only).
 - **Construction.** 3Q18 operating profit was up 26%Y/Y on higher domestic progress billings, with pre-cast slightly weaker. The outstanding order book of M\$5.2B is 68% external, representing 3.2x historical segment revenue.
 - **Prop Investment.** 3Q18 operating profit was flattish (down 1%Y/Y), but was up 5%Y/Y at the revenue level on new or rising contribution from new assets such as Velocity Mall (0.9MM sqft), Velocity Hotel (350 rooms) and Geo Tower (0.24MM sqft) in the Klang Valley. This left overall cumulative segment operating profit for 9M18 up 17%Y/Y.
- **Recent publications.** Please also see our 8 Nov-18 Malaysia Developers note titled "*Clearing clouds; Upgrade UEMS to OW; Top picks remain ECW (OW) and SPSB (OW)*" [here](#).

Table 1: SWB 3Q18 results summary

M\$ mn, YE Dec	3Q18	3Q17*	Y/Y	2Q18	Q/Q	9M18	9M17*	Y/Y
Revenue	1,445	1,283	13%	1,287	12%	4,040	3,612	12%
Core Operating profit	160	154	4%	166	-4%	456	464	-2%
Operating margin	11.1%	12.0%		12.9%		11.3%	12.9%	
Net finance costs	-3	-6	-45%	-13	-73%	-24	-32	-25%
Associates & JVs	38	49	-24%	89	-58%	165	188	-12%
Core PBT	194	189	3%	183	6%	538	554	-3%
Net income	145	145	0%	199	-27%	467	448	4%
Core net income	145	145	0%	140	4%	407	391	4%
Core margin	10.1%	11.3%		10.9%		10.1%	10.8%	
Core EPS (sen)	2.99	6.98	-57%	2.88	4%	8.36	15.91	-47%

Source: Company. * Restated.

Table 2: SWB 3Q18 core operating profit breakdown (excluding JVs/associates)

M\$ mn, YE Dec	3Q18	3Q17*	Y/Y	2Q18	Q/Q	9M18	9M17*	Y/Y
Prop development	34	21	63%	44	-23%	96	94	1%
Prop investment	60	61	-1%	54	11%	174	148	17%
Construction	48	38	26%	46	3%	133	113	17%
Trading & Manufacturing	18	17	1%	16	7%	48	44	9%
Quarry	2	3	-23%	4	-34%	8	8	0%
Others	(2)	14	-114%	2	-213%	(2)	57	-104%
Core operating profit	160	154	4%	166	-4%	456	464	-2%

Source: Company. * Restated.

Table 3: SWB 3Q18 core operating margins

	3Q18	3Q17*	Y/Y	2Q18	Q/Q	9M18	9M17*	Y/Y
Prop development	17.4%	12.8%	4.6 ppts	49.6%	-32.2 ppts	23.0%	16.4%	6.6 ppts
Prop investment	25.3%	26.9%	-1.6 ppts	25.0%	0.3 ppts	25.7%	23.9%	1.9 ppts
Construction	10.2%	9.1%	1.2 ppts	10.3%	0.0 ppts	9.8%	10.8%	-1.1 ppts
Trading & Manufacturing	5.9%	6.0%	0.0 ppts	5.7%	0.2 ppts	5.6%	5.7%	-0.2 ppts
Quarry	4.2%	6.1%	-1.9 ppts	6.1%	-2.0 ppts	5.0%	5.4%	-0.5 ppts
Others	-1.0%	8.0%	-9.0 ppts	0.9%	-1.9 ppts	-0.4%	11.4%	-11.7 ppts
Core operating margin	11.1%	11.6%	-0.6 ppts	12.9%	-1.8 ppts	11.3%	12.7%	-1.4 ppts

Source: Company. * Restated.

Table 4: JPM Developer universe domestic pre-sales

M\$mn, YE Dec	3QCY18	3QCY17	Y/Y	2QCY18	Q/Q	9MCY18	9MCY17	Y/Y
Mah Sing Group	278	436	-36%	472	-41%	1,220	1,255	-3%
SP Setia	913	585	56%	769	19%	2,318	1,661	40%
Sunway	380	48	692%	73	421%	554	230	141%
TOTAL DEVELOPERS	1,571	1,069	47%	1,315	20%	4,092	3,146	30%

Source: Companies.

Table 5: Developer peer valuation comparison

As at: 21 Nov-18	FYE	Mkt cap (US\$m)	Price (M\$)	Rating	Target (M\$)	P/E		EPS growth		Net div yield		P/B	ROE	RNAV (M\$)	Prem/disc to RNAV
						CY18E	CY19E	CY18E	CY19E	FY18E	FY19E				
Eco World Develop	Oct	716	1.02	OW	1.60	16.9	10.4	36.6%	63.3%	0.0%	2.0%	0.7	4.4	2.80	-64%
Mah Sing Group	Dec	585	1.01	N	1.20	8.8	8.8	-24.9%	-0.5%	4.7%	4.7%	0.7	8.6	2.10	-52%
SP Setia	Dec	1,991	2.12	OW	3.60	23.9	15.9	-52.3%	50.9%	3.1%	4.7%	0.7	3.0	6.30	-66%
Sunway	Dec	1,666	1.45	N	1.50	12.9	11.5	-6.1%	12.0%	3.9%	4.4%	0.9	6.9	2.40	-40%
UEM Sunrise	Dec	849	0.78	OW	1.00	16.8	12.2	-25.0%	37.7%	1.5%	2.0%	0.5	2.9	2.90	-73%
Weighted average		5,807				17.3	12.7	-30.9%	30.0%	2.9%	3.9%	0.7	4.8		-58%

Source: Bloomberg, J.P. Morgan estimates.

Investment Thesis

We continue to like Sunway for its integrated businesses (with about 60% of earnings from the Prop investment and Construction segments), strong branding, and good assets (landbank and commercial assets, including through its 40% stake in Sunway REIT). We also like its asset-light model, with the next round of asset recycling and potential value-unlocking likely coming from maturing large properties (i.e. Pinnacle office tower or Velocity Mall).

However, on valuations we are Neutral on SWB at current levels, and see better value in its peers. Within the sector, we prefer ECW (OW) and SPSB (OW).

Valuation

Our Jun-19 PT of M\$1.50 is based on a 40% discount to RNAV, or between -1SD and the historical sector mean.

Developer RNAV band



Source: Bloomberg, J.P. Morgan.

Sunway RNAV

Projects	% stake	Description	Undeveloped land (acres)	Remaining GDV (M\$ M)	Years to develop	Revaluation surplus (M\$ M)	Comments
Klang Valley							
Sunway Damansara	60%	Mixed township	15	1,691	5	141	Discounted at WACC of 10%
Sunway South Quay	100%	Mixed development	40	3,087	7	425	Discounted at WACC of 10%
Sunway Montereiz	60%	Residential	4	38	2	3	Discounted at WACC of 10%
Sunway Semenyih	70%	Residential	398	729	10	51	Discounted at WACC of 10%
Sunway Cheras	100%	Residential	6	17	2	2	Discounted at WACC of 10%
Sunway Duta	60%	Residential	3	120	3	9	Discounted at WACC of 10%
Sunway Montana	100%	Residential	2	56	3	8	Discounted at WACC of 10%
Sunway Resort City	100%	Commercial	15	660	6	89	Discounted at WACC of 10%
Sunway Velocity	85%	Mixed development	10	1,984	6	243	Discounted at WACC of 10%
Sunway Tower KL 1	100%	Office	1	240	3	33	Discounted at WACC of 10%
Sunway Velocity Two	50%	Mixed development	8	2,000	10	142	Discounted at WACC of 10%
Melawati	100%	Residential	2	43	2	6	Discounted at WACC of 10%
Sg Long	80%	Residential	111	277	4	27	Discounted at WACC of 10%
Mont Putra, Rawang	100%	Residential	163	156	6	19	Discounted at WACC of 10%
Sunway Serene Kelana Jaya	100%	Mixed development	18	1,450	5	219	Discounted at WACC of 10%
Sunway Industrial Park Subang	80%	Industrial	0	109	3	12	Discounted at WACC of 10%
Jalan Belfield-Kampung Attap-Istana	100%	Residential	5	1,100	6	158	Discounted at WACC of 10%
Lot One Kajang	100%	Residential	5	460	5	72	Discounted at WACC of 10%
USJ1 Subang Jaya	100%	Mixed development	15	1,400	5	235	Discounted at WACC of 10%
Sunway Wangsa Maju	55%	Residential	4	500	5	42	Discounted at WACC of 10%
			826	16,116		1,953	
Northern							
Sunway City Ipoh	65%	Residential	441	1,048	10	84	Discounted at WACC of 10%
Sunway Paya Terubong	100%	Residential	24	1,500	6	181	Discounted at WACC of 10%
Sunway Hills	100%	Residential	81	849	8	107	Discounted at WACC of 10%
Sunway Wellesley Bukit Mertajam	100%	Residential	51	710	5	91	Discounted at WACC of 10%
Sunway Tunas Balik Pulau	100%	Residential	9	60	2	7	Discounted at WACC of 10%
Sunway Betong Balik Pulau	100%	Residential	20	110	2	13	Discounted at WACC of 10%
			626	4,278		484	
Johor							
Bukit Lenang	80%	Residential	65	698	3	65	Discounted at WACC of 10%
Medini	60%	Mixed township	643	10,833	15	692	Discounted at WACC of 10%
Pendas	60%	Mixed township	1,079	18,000	20	815	Discounted at WACC of 10%
			1,787	29,531		1,571	
Singapore							
Rivercove Residences Sengkang	30%	Residential	5	1,967	4	24	Discounted at WACC of 10%
Brookvale Park Clementi	30%	Residential	9	3,000	4	36	Discounted at WACC of 10%
Canberra Link Sembawang	30%	Residential	4	1,500	4	16	Discounted at WACC of 10%
			18	6,467		77	
China							
Sunway Guanghao	65%	Mixed development	4	67	2	4	Discounted at WACC of 10%
Tianjin Eco City	60%	Mixed development	6	575	6	36	Discounted at WACC of 10%
India							
Sunway OPUS Grand India	50%	Condominiums	24	702	5	33	Discounted at WACC of 10%
Sunway MAK Signature Residence (JV with M.A.K Builders)	60%	Residential	14	181	5	8	Discounted at WACC of 10%
Australia							
Wonderland Business Park Sydney	45%	Industrial	13	44	3	2	Discounted at WACC of 10%
			61	1,569		82	
Total			3,318	57,961		4,167	

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

Sunway RNAV

	Value (M\$mn)	Comments
Revaluation surplus	4,167	
Book value as at Dec-18E	7,810	
Revaluation gain from investment properties	249	Valuing 40%-owned Sunway REIT at PT of M\$1.80
Revaluation gain from construction division	278	Valuing 54%-owned Sunway Construction Group at market price of M\$1.78/share
Outstanding cash obligation for land	(697)	
Total RNAV	11,807	
Number of shares (M)	4,874	
RNAV per share (M\$)	2.42	
PT (M\$) – rounded off	1.50	40% discount to RNAV

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

Risks to Rating and Price Target

Key upside risks include:

1. Reasonably-priced and accretive landbank acquisitions, especially in the more resilient Klang Valley, where pre-sales have held up better amid the slower consumer environment;
2. Asset recycling into 40%-owned Sunway REIT, resulting in value-unlocking for shareholders;
3. Stronger than expected property pre-sales or construction new orderbook

Key downside risks include: Slower than expected property pre-sales, and keen competition in the Iskandar region in Johor.

Real Estate

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Other Companies Discussed in This Report (all prices in this report as of market close on 21 November 2018)

Eco World Development (ECOW.KL/M\$1.02/Overweight), SP Setia (SETI.KL/M\$2.12/Overweight), UEM Sunrise Bhd (UMSB.KL/M\$0.78/Overweight)

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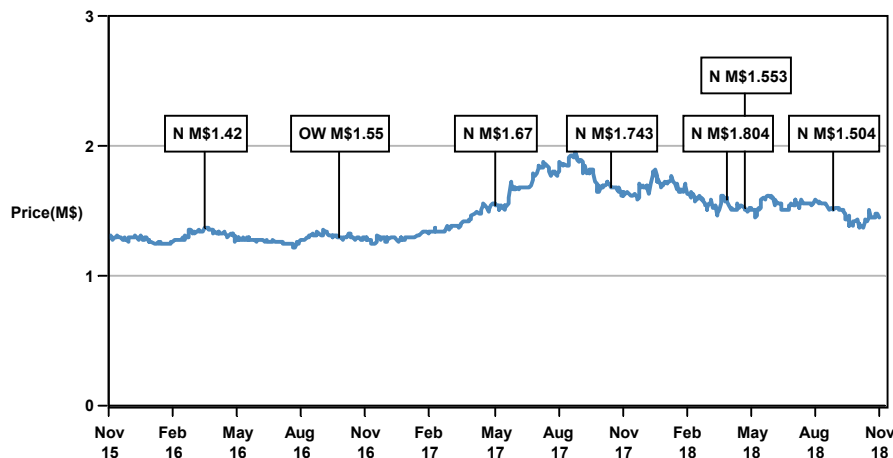
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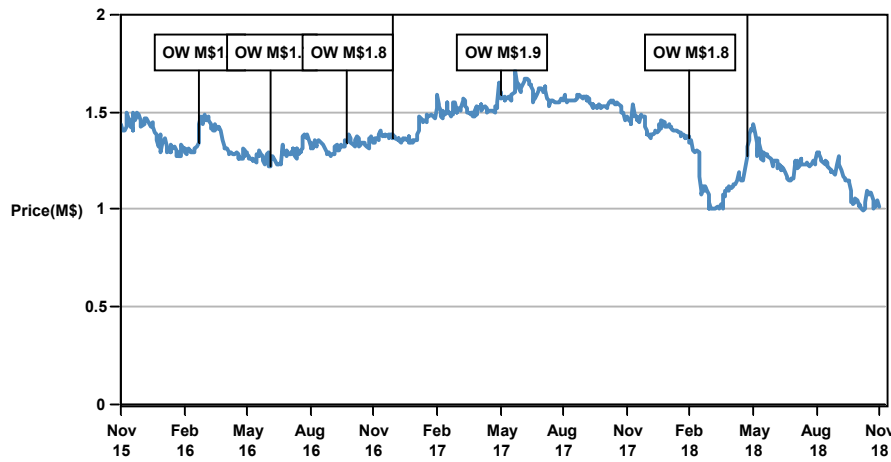
Sunway Bhd (SWAY.KL, SWB MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
08-Apr-16	N	1.38	1.42
14-Oct-16	OW	1.30	1.55
26-May-17	N	1.54	1.67
06-Nov-17	N	1.67	1.74
18-Apr-18	N	1.59	1.80
14-May-18	N	1.52	1.55
18-Sep-18	N	1.51	1.50

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

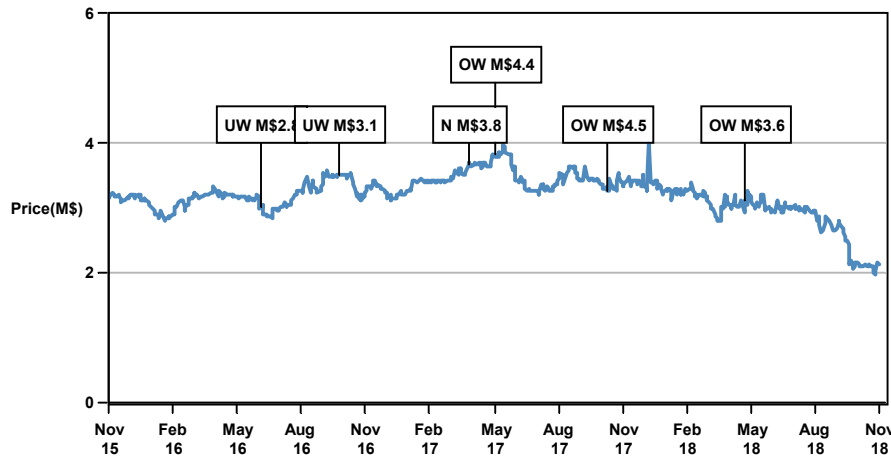
Eco World Development (ECOW.KL, ECW MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
14-Mar-16	OW	1.34	1.90
28-Jun-16	OW	1.22	1.70
14-Oct-16	OW	1.34	1.80
20-Dec-16	OW	1.36	1.80
26-May-17	OW	1.59	1.90
20-Feb-18	OW	1.36	1.80
14-May-18	OW	1.27	1.60

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

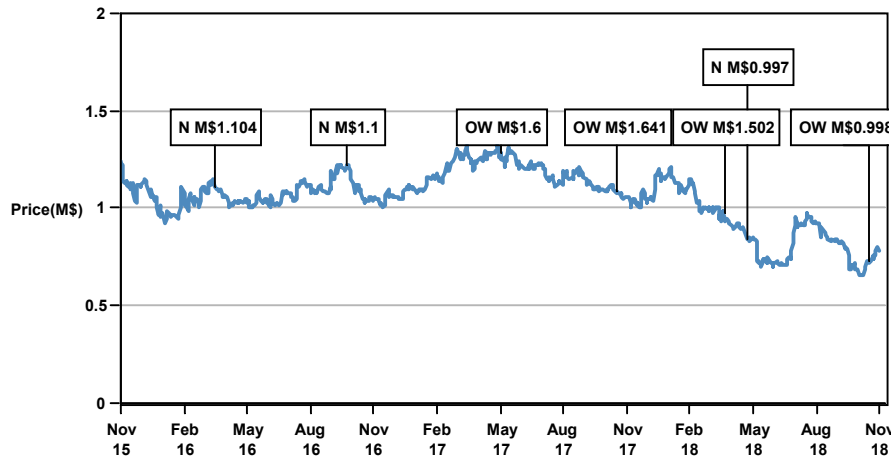
SP Setia (SETI.KL, SPSB MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
27-Jun-16	UW	3.01	2.80
14-Oct-16	UW	3.50	3.10
17-Apr-17	N	3.67	3.80
26-May-17	OW	3.80	4.40
01-Nov-17	OW	3.27	4.50
14-May-18	OW	3.11	3.60

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Aug 12, 2003.

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



Date	Rating	Share Price (M\$)	Price Target (M\$)
08-Apr-16	N	1.11	1.10
14-Oct-16	N	1.22	1.10
26-May-17	OW	1.28	1.60
07-Nov-17	OW	1.09	1.64
12-Apr-18	OW	0.97	1.50
14-May-18	N	0.84	1.00
08-Nov-18	OW	0.73	1.00

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

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