

Sunway Bhd (SWB MK)

Neutral

Price: M\$1.56

21 Aug 2018

Price Target: M\$1.55

PT End Date: 31 Dec 2018

Results dragged by weaker Prop development, but Prop investment and Construction segments stonger

- **SWB 2Q18 core net profit was flat Y/Y**, leaving the cumulative 1H18 up 7%Y/Y to make 44%/43% of JPM/consensus full-year. Overall, 2Q18 core operating profit was dragged by the Prop development segment (down 30%Y/Y), but compensated by higher Prop investment and Construction, and lower net interest and tax expenses. Management declared a dividend of 3.5 sen.
- **2Q18 segment operating performance updates:**
 - **Prop Development.** Results were dragged by lower domestic progress billings and the impact of adopting MFRS 15 at a project in Singapore, which resulted in SWB only recognising contribution on project completion. This was partly offset by realised forex gains from other overseas projects. For 1H18, group pre-sales of M\$840MM made 65% of JPM/management's full-year forecast/target of M\$1.3B, driven mainly by international projects (79% contribution), and in particular the Rivercove Residences in Singapore. While YTD pre-sales to Aug-18 has since met our M\$1.3B forecast on launches in Jul-18, domestic pre-sales of M\$367MM lags our M\$925MM forecast on consumer cautiousness and lack of launches around the General Elections. Unbilled sales of M\$1.5B is 61% domestic, representing 1.5x historical segment revenue (0.9x for domestic projects only).
 - **Prop Investment.** Core operating profit up 32%Y/Y on contribution from new and newly opened assets like Velocity Mall, Velocity Hotel and Geo in the Klang Valley.
 - **Construction.** Core operating profit up 24%Y/Y on higher domestic progress billings, partly offset by lower pre-cast. Outstanding orderbook of M\$5.8B is 67% external, representing 3.6x historical segment revenue.
- **Maintain Neutral, our top picks in the Property space are ECW (OW) and SPSB (OW).**

Table 1: SWB 2Q18 results summary

M\$ mn; year-end Dec	2Q18	2Q17*	Y/Y	1Q18	Q/Q	1H18	1H17*	Y/Y
Revenue	1,287	1,241	4%	1,308	-2%	2,596	2,329	11%
Core Operating profit	166	186	-11%	130	28%	296	311	-5%
Operating margin	12.9%	15.0%		9.9%		11.4%	13.3%	
Net finance costs	-13	-19	-32%	-8	68%	-20	-25	-20%
Associates & JVs	89	96	-7%	38	131%	127	139	-8%
Core PBT	183	213	-14%	161	14%	344	365	-6%
Net income	199	196	2%	122	64%	321	303	6%
Core net income	140	139	1%	122	15%	262	246	7%
Core margin	10.9%	11.2%		9.3%		10.1%	10.6%	
Core EPS (sen)	2.88	6.71	-57%	2.49	16%	5.37	8.93	-40%

Source: Company. * Restated.

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

M\$ mn; year-end Dec	2Q18	2Q17*	Y/Y	1Q18	Q/Q	1H18	1H17*	Y/Y
Prop development	44	63	-30%	18	150%	62	74	-16%
Prop investment	54	41	32%	59	-9%	113	87	30%
Construction	46	37	24%	39	19%	85	76	13%
Trading & Manufacturing	16	14	18%	14	18%	30	26	15%
Quarry	4	4	-15%	2	60%	6	5	14%
Others	2	26	-94%	(2)	-189%	(0)	43	-100%
Core operating profit	166	186	-11%	130	28%	296	311	-5%

Source: Company. * Restated.

Table 3: SWB 2Q18 core operating margins

	2Q18	2Q17*	Y/Y	1Q18	Q/Q	1H18	1H17*	Y/Y
Prop development	49.6%	23.1%	26.5 ppts	13.3%	36.3 ppts	27.9%	17.8%	10.1 ppts
Prop investment	25.0%	19.8%	5.2 ppts	26.9%	-2.0 ppts	26.0%	22.1%	3.9 ppts
Construction	10.3%	12.0%	-1.7 ppts	8.8%	1.5 ppts	9.5%	12.0%	-2.5 ppts
Trading & Manufacturing	5.7%	6.2%	-0.4 ppts	5.0%	0.7 ppts	5.4%	5.6%	-0.2 ppts
Quarry	6.1%	7.1%	-1.0 ppts	4.4%	1.7 ppts	5.4%	5.1%	0.2 ppts
Others	0.9%	15.7%	-14.8 ppts	-1.0%	1.9 ppts	-0.1%	13.1%	-13.2 ppts
Core operating margin	12.9%	15.0%	-2.1 ppts	9.9%	3.0 ppts	11.4%	13.3%	-1.9 ppts

Source: Company. * Restated.

Table 4: Developer domestic pre-sales

M\$mn; year-end Dec	2QCY18	2QCY17	Y/Y	1QCY18	Q/Q	1HCY18	1HCY17	Y/Y
Sunway	73	107	-32%	101	-28%	174	182	-4%

Source: Companies.

Table 5: Developer peer comparison

As at: 21 Aug-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	898	1.25	OW	1.60	18.0	12.3	51.8%	46.2%	0.0%	1.8%	0.8	5.1	2.80	-55%
Mah Sing Group	Dec	723	1.22	N	1.10	9.8	10.5	-14.1%	-6.2%	4.2%	3.9%	0.8	9.3	2.10	-42%
SP Setia	Dec	2,800	2.94	OW	3.60	20.8	17.0	-24.1%	22.8%	3.6%	4.4%	1.0	4.9	6.40	-54%
Sunway	Dec	1,852	1.56	N	1.55	12.6	11.2	5.4%	12.2%	4.1%	4.7%	1.0	7.6	2.50	-38%
UEM Sunrise	Dec	1,024	0.93	N	1.00	20.0	14.5	-25.0%	37.7%	1.3%	1.7%	0.6	2.9	2.70	-66%
Weighted average		7,297				17.2	13.9	-13.0%	19.3%	3.0%	3.7%	0.9	5.8		-50%

Source: Bloomberg, J.P. Morgan estimates.

Investment Thesis

We continue to like Sunway for its integrated businesses (50-60% earnings from Construction and Prop Investment), with strong branding and assets (Prop Development landbank and commercial assets through its 37% stake in Sunway REIT). We also like its asset-light model, with the next asset recycling and potential value-unlocking coming from recently completed large properties (Pinnacle office tower and Velocity Mall). However, on valuations, we are Neutral on SWB at current levels, and see better value in its peers. We prefer SPSB (OW) and ECW (OW).

Valuation

Our Dec-18 PT of M\$1.55 is based on a 40% discount to RNAV (from 30% discount previously), or close to -1SD to historical mean for the sector.

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	136	Discounted at WACC of 10%
Sunway South Quay	100%	Mixed development	40	3,087	7	423	Discounted at WACC of 10%
Sunway Monterez	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	88	Discounted at WACC of 10%
Sunway Velocity	85%	Mixed development	10	1,984	6	235	Discounted at WACC of 10%
Sunway Tower KL 1	100%	Office	1	240	3	32	Discounted at WACC of 10%
Sunway Velocity Two	50%	Mixed development	8	2,000	10	141	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	218	Discounted at WACC of 10%
Sunway Industrial Park Subang	80%	Industrial	0	109	3	10	Discounted at WACC of 10%
Jalan Belfield-Kampung Attap-Istana	100%	Residential	5	1,100	6	148	Discounted at WACC of 10%
Lot One Kajang	100%	Residential	5	460	5	69	Discounted at WACC of 10%
USJ1 Subang Jaya	100%	Mixed development	15	1,400	5	241	Discounted at WACC of 10%
Sunway Wangsa Maju	55%	Residential	4	500	5	39	Discounted at WACC of 10%
			826	16,116		1,919	
Northern							
Sunway City Ipoh	65%	Residential	441	1,048	10	75	Discounted at WACC of 10%
Sunway Paya Terubong	100%	Residential	24	1,500	6	191	Discounted at WACC of 10%
Sunway Hills	100%	Residential	81	849	8	106	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		483	
Johor							
Bukit Lenang	80%	Residential	65	698	3	68	Discounted at WACC of 10%
Medini	60%	Mixed township	643	10,833	15	705	Discounted at WACC of 10%
Pendas	60%	Mixed township	1,079	18,000	20	871	Discounted at WACC of 10%
			1,787	29,531		1,644	
Singapore							
Rivercove Residences Sengkang	30%	Residential	5	1,560	4	52	Discounted at WACC of 10%
Brookvale Park	30%	Residential	9	3,000	3	103	Discounted at WACC of 10%
			14	4,560		155	
China							
Sunway Guanghao	65%	Mixed development	4	67	2	3	Discounted at WACC of 10%
Tianjin Eco City	60%	Mixed development	6	575	6	28	Discounted at WACC of 10%
India							
Sunway OPUS Grand India	50%	Condominiums	24	702	5	31	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		72	
Total			3,314	56,054		4,273	

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

Sunway RNAV

	Value (M\$mn)	Comments
Revaluation surplus	4,273	
Book value as at Dec-17E	7,811	
Revaluation gain from investment properties	249	Value 37%-owned Sunway REIT at PT of M\$1.77
Revaluation gain from construction division	577	Valued at market price of M\$2.20/share
Outstanding cash obligation for land	(697)	Discounted value for Iskandar land purchase
Total RNAV	12,213	
Number of shares (M)	4,874	
RNAV per share (M\$)	2.51	
PT (M\$) – rounded off	1.55	40% discount to RNAV

Source: J.P. Morgan estimates.

Risks to Rating and Price Target

Key upside risks include:

1. Reasonably-priced, 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 37%-held Sunway REIT, resulting in value-unlocking for shareholders
3. Stronger-than-expected property pre-sales

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

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

Eco World Development (ECOW.KL/M\$1.25/Overweight), SP Setia (SETI.KL/M\$2.94/Overweight)

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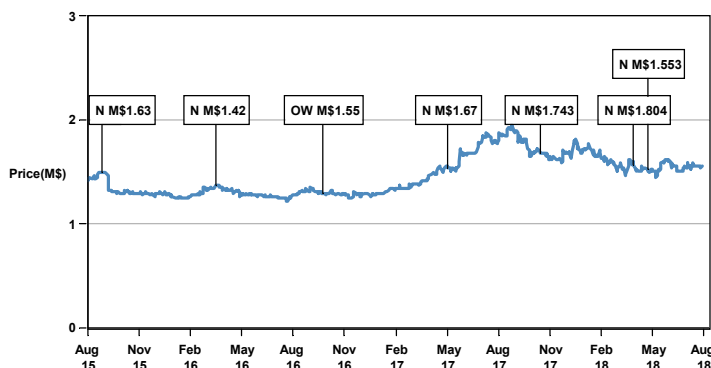
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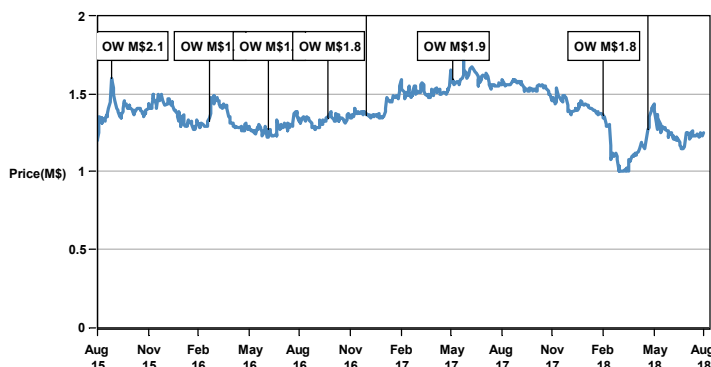
Sunway Bhd (SWAY.KL, SWB MK) Price Chart



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

Date	Rating	Share Price (M\$)	Price Target (M\$)
19-Sep-15	N	1.48	1.63
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	1.57	1.80
14-May-18	N	1.52	1.55

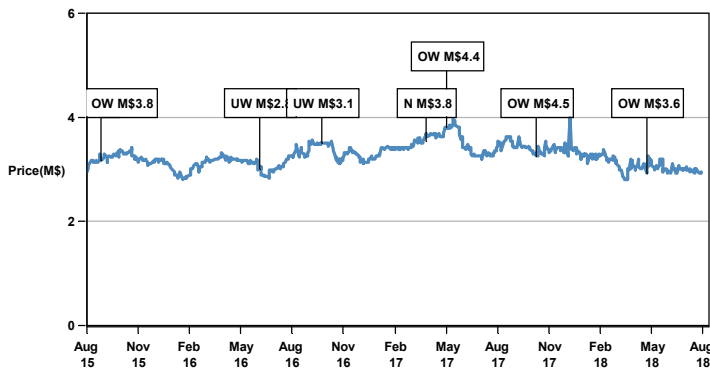
Eco World Development (ECOW.KL, ECW MK) Price Chart



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

Date	Rating	Share Price (M\$)	Price Target (M\$)
19-Sep-15	OW	1.60	2.10
14-Mar-16	OW	1.32	1.90
28-Jun-16	OW	1.27	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

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



Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends; initiated coverage Aug 12, 2005.

Date	Rating	Share Price (M\$)	Price Target (M\$)
19-Sep-15	OW	3.17	3.80
27-Jun-16	UW	3.01	2.80
14-Oct-16	UW	3.50	3.10
17-Apr-17	N	3.55	3.80
26-May-17	OW	3.80	4.40
01-Nov-17	OW	3.27	4.50
14-May-18	OW	2.93	3.60

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