

Sunway Bhd (SWB MK)

Neutral

Price: M\$3.73

14 Jun 2017

Price Target: M\$3.90

PT End Date: 30 Dec 2017

To expand Healthcare unit leveraging on its integrated model; proposes bonus issue & free warrants

SWB has announced its reclassification on Bursa from Properties to Trading/Services with the aim to place equal importance to the other businesses aside from Property, namely Healthcare where there are new plans for M\$1B expansion in the next 5 years. Trading/Services comprise 42% of FY16 core PATAMI, with Healthcare at 7-8%. The announced bonus issue and 7-year free warrants, which will raise-up to M\$965MM, will help improve share liquidity and finance future expansion, limiting risk of future cash calls. Our analysis on valuations below suggests that the estimated accretion of M\$0.60-0.80/share or 10-15% to our base case RNAV of M\$5.45/share by valuing the Healthcare segment in line with peers at 30-40x PE (versus our base case of at book currently), will largely compensate for the estimated dilution from the free warrants. While the ultimate long-term plan is to potentially hive off the Healthcare segment (similar to that for its construction division, which was separately listed back in 2014/15, translating to special dividends), much will still hinge on the execution to expand and build scale for the Healthcare segment longer term. At current levels, hence we **maintain Neutral on SWB** following the stock's strong outperformance in the last 3 months (Figure 1). While SWB's Healthcare/REIT segments provide stability, **we prefer ECW (OW) and SPSB (OW) our top picks in the space**, which we believe are also more leveraged to the expected reflation theme/gradual recovery for the sector from 2018 onwards

- **Three announcements. 1) Reclassification of SWB's sector on Bursa**, from Properties to Trading/Services effective 16 Jun-17. 2) **A proposed bonus issue on a 4 to 3 basis** resulting in the issue of up to 2.80B new bonus shares. 3) **Free warrants on a 3 to 10 basis**, resulting in the concurrent issue of up to 631MM warrants over seven years, and proceeds of up to M\$965MM based on 5 day volume weighted average market price.
- **Rationale for reclassification to the Trading/Services sector.** Management held a briefing to indicate its intention to place equal importance to the other businesses under SWB aside from Property, comprising Trading & manufacturing, Quarry & building materials, Healthcare and Education. Together, these businesses under the Trading & services division (Table 2) grew at a 4-year CAGR of 48% (vs 12% for the group) to make 42% of core PATAMI in FY16 (vs 14% in FY12). Property development and investment/REIT contribution in turn has fallen from 75% to 43% of core PATAMI over the same period, partly due to the softer property market in recent years. In particular, management plans to leverage its integrated model and Education division to scale up its Healthcare business from 365 beds at Sunway Medical Centre (SMC) to 1,700 beds across five hospitals at existing SWB townships/developments over the next five years (Table 3). Overall, Healthcare currently contributes about M\$45MM-M\$50MM pa to core net profit (7%-8% of group).
- **Warrant terms.** The free warrants will be issued on a 3:10 basis, resulting in the issue of up to 631MM warrants over seven years, with an annual step-down built into the exercise price. Proceeds from the exercise of warrants will go towards working capital requirements, including to partly-fund the estimated M\$1B capex to expand the Healthcare division by 1,335 beds next five years. This, plus the portfolio of SWB investment assets that can be unlocked through asset recycling in SREIT, minimizes the risk of future cash calls.
- **Impact on valuations.** Smaller cap Healthcare stocks are currently trading at 2017E PE of 30x-40x as per Table 4 (However, among these smaller stocks, KPJ currently operates with just under 3,000 hospital beds, versus SWB's current only 365 hospital bed capacity). Nevertheless, if we were to optimistically still apply this multiple to SWB's net profit of M\$45-50MM pa from Healthcare and strip out its book value, this will result in an estimated accretion of M\$0.60-0.80/share or 10-15% to our base case RNAV of M\$5.45/share (our base case now values Healthcare at book). This will largely compensate for the estimated dilution of

about 10% from the free warrants (accounting for estimated value of the free warrants). Further upside from here will hinge largely on the execution to expand and build scale for the Healthcare segment longer term.

- **Recent publications.** Our Malaysia Developers note titled “*Bottoming, expecting a gradual lift: Still OW on ECW, upgrade SPSB and UEMS to OW, cut SWB to Neutral*” [here](#).

Table 1: SWB core PATAMI breakdown

RM'000	2012		2013		2014		2015		2016	
Property Development	203,146	58%	243,482	50%	230,819	40%	175,211	31%	192,785	35%
Property Investment & REIT	58,911	17%	62,497	13%	51,018	9%	66,637	12%	70,769	13%
Construction	40,461	12%	59,457	12%	113,817	19%	124,600	22%	58,677*	11%
Trading & Services (Strategic Investments)	48,163	14%	118,585	25%	188,228	32%	197,728	35%	233,665	42%
CORE PATMI	350,680	100%	484,021	100%	583,882	100%	564,175	100%	555,897	100%

Source: Company.

Table 2: Developer peer comparison

As at: 14 Jun-17	FYE	Mkt cap (US\$mn)	Price (M\$)	Rating	Target (M\$)	P/E		EPS growth		Net div yield		P/B	ROE	RNAV (M\$)	Prem/disc to RNAV
						CY17E	CY18E	CY17E	CY18E	FY17E	FY18E				
Eco World Develop	Oct	1,120	1.62	OW	1.90	28.0	16.7	21.2%	68.1%	0.0%	0.0%	1.1	4.4	2.90	-44%
Mah Sing Group	Dec	894	1.58	N	1.65	12.1	13.0	-6.6%	-7.1%	3.3%	3.0%	1.1	11.3	2.15	-27%
SP Setia	Dec	2,561	3.82	OW	4.40	15.3	17.5	-4.4%	-12.8%	4.7%	3.4%	1.2	7.8	6.10	-37%
Sunway	Dec	1,785	3.73	N	3.90	13.3	12.5	1.6%	6.7%	3.3%	3.5%	1.0	7.5	5.45	-32%
UEM Sunrise	Dec	1,353	1.27	OW	1.60	31.5	28.6	41.1%	10.1%	0.0%	1.0%	0.9	2.8	2.90	-56%
Weighted average		7,714				19.1	17.6	-0.2%	-0.5%	2.7%	2.5%	1.1	6.8		-39%

Source: Bloomberg, J.P. Morgan estimates.

Table 3: SWB planned expansion in Healthcare bed capacity

Location	Type	New beds	Completion	Notes
Sunway Medical Centre	Expansion	245	end 2017	Expansion includes 70 consultation suites
Sunway Velocity	New	240	mid 2018	
Sunway Seberang Jaya	New	350	mid 2019	Phase 1: 180 beds, Phase 2: 170 beds
Sunway Ipoh	New	250	end 2019	
Sunway Damansara	New	250	end 2020	
TOTAL		1,335		1,700 beds including existing 365 beds at SMC

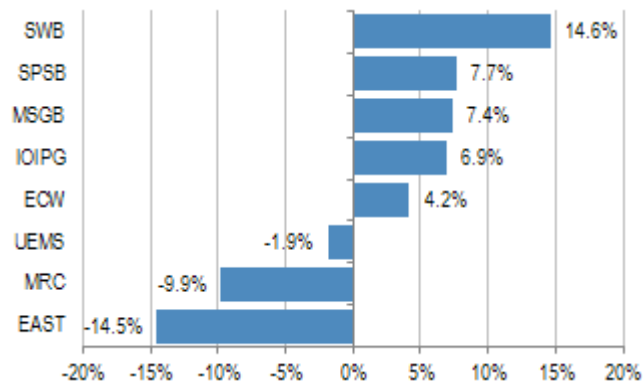
Source: Company.

Table 4: Healthcare peer comparison

As at: 14 Jun-17	Ticker	Ctry	Mkt cap (US\$mn)	Price (LC)	Rating	Target (LC)	2yr EPS CAGR 2017-2018	P/E		EV/Ebitda		ROE	Div Yld	P/B
								CY17E	CY18E	FY17E	FY18E			
HOSPITALS: EM Asia														
IHH Healthcare	IHH MK	MYS	11,618	6.00	N	6.00	19.2%	52.7	40.2	23.0	18.4	4.2	0.6%	2.2
KPJ Healthcare	KPJ MK	MYS	1,037	4.19	OW	4.70	9.4%	29.8	28.4	14.5	12.6	10.3	1.5%	2.8
Harmonicare Medical Hldgs	1509 HK	CHN	378	3.89	NC	-	3.3%	20.4	19.1	7.7	6.8	8.6	1.5%	1.7
Phoenix Healthcare Grp	1515 HK	CHN	1,689	10.32	NC	-	11.3%	29.3	23.7	15.6	12.4	9.7	0.8%	2.3
Apollo Hospitals	APHS IN	IND	2,869	1,326.05	N	1,325.00	49.2%	55.6	36.9	23.3	18.2	9.9	1.1%	4.9
Fortis Healthcare	FORH IN	IND	1,506	187.00	OW	230.00	132.0%	41.5	25.0	18.5	14.6	6.6	0.3%	2.2
Mitra Keluarga Karyasehat	MIKA IJ	IDN	2,366	2,060	NC	-	6.5%	39.7	35.0	30.9	26.8	19.6	1.5%	7.8
Siloam International Hosp	SILO IJ	IDN	1,234	12,650	NC	-	15.4%	121.8	91.5	20.3	16.7	4.2	0.1%	5.1
Raffles Medical Group	RFMD SP	SGP	1,724	1.37	NC	-	2.4%	33.4	31.9	23.2	21.1	10.4	1.5%	3.4
Bangkok Chain Hospital	BCH TB	THA	1,008	13.70	NC	-	7.6%	37.4	32.3	18.8	16.4	17.5	1.4%	6.2
Bangkok Dusit Medical	BDMS TB	THA	8,779	19.20	UW	17.00	-1.2%	40.1	36.8	23.0	21.6	13.4	1.5%	5.1
Bumrungrad Hospital	BH TB	THA	3,721	173.00	OW	200.00	7.9%	39.2	35.5	20.9	18.8	24.7	1.5%	7.7
Chularat Hospital	CHG TB	THA	779	2.40	NC	-	7.8%	38.7	33.3	25.6	21.7	19.5	1.4%	7.7
Weighted average			38,709				17.2%	46.2	37.5	22.3	19.1	11.1	1.1%	4.3
Weighted average (excl. IHH MK)			27,091				16.3%	43.5	36.3	22.0	19.4	14.0	1.3%	5.2

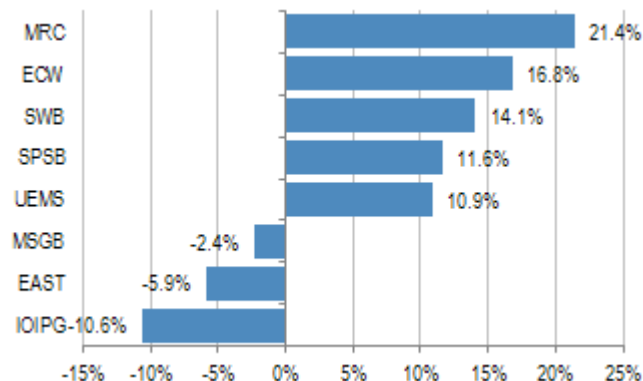
Source: Bloomberg, J.P. Morgan estimates.

Figure 1: 3 moth performance relative to FBMKLCI



Source: Bank Negara.

Figure 2: 12 month performance relative to FBMKLCI



Source: Bank Negara.

Investment Thesis

We continue to like Sunway for its integrated businesses (50-60% earnings from Construction and Property Investment), with strong branding and assets (property development landbank and commercial assets through its 36% stake in Sunway REIT). We also like its asset-light model, with the next asset recycling and potential value-unlocking from recently completed large properties (Pinnacle office tower and Velocity Mall). However, following its share price outperformance and near-fair valuations, we are Neutral on SWB at current levels.

Valuation

Our Dec-17 PT of M\$3.90 is based on a 30% discount to RNAV, in line with the sector's historical 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%	Residential/commercial township	15	1,691	5	127	Discounted at WACC of 10%
Sunway South Quay	60%	Lakeside mixed development	40	3,087	7	277	Discounted at WACC of 10%
Sunway Montez	60%	Residential	4	38	2	2	Discounted at WACC of 10%
Sunway Semenyih	70%	Residential	398	729	10	54	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	12	Discounted at WACC of 10%
Sunway Montana	100%	Residential	2	56	3	6	Discounted at WACC of 10%
Sunway Resort City	100%	Commercial	15	660	6	70	Discounted at WACC of 10%
Sunway Velocity	85%	Mixed development	10	1,984	6	265	Discounted at WACC of 10%
Sunway Tower KL 1	100%	Office	1	240	3	21	Discounted at WACC of 10%
Sunway Velocity Two	50%	Residential	8	2,000	10	199	Discounted at WACC of 10%
Melawati	100%	Residential	2	43	2	5	Discounted at WACC of 10%
Sg Long	80%	Residential	111	277	4	23	Discounted at WACC of 10%
Mont Putra, Rawang	100%	Residential	163	156	6	13	Discounted at WACC of 10%
Kelana Jaya	100%	Mixed development	22	1,900	5	235	Discounted at WACC of 10%
Kampung Subang	80%	Industrial	6	110	2	18	Discounted at WACC of 10%
			808	13,107		1,329	
Northern							
Sunway City Ipoh	65%	Residential	441	1,048	10	85	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%
Paya Terubong	100%	Residential	24	1,500	6	181	Discounted at WACC of 10%
Sungai Ara	100%	Residential	81	849	8	102	Discounted at WACC of 10%
Bukit Mertajam	100%	Residential	53	725	5	87	Discounted at WACC of 10%
			627	4,293		476	
Singapore							
Novena	30%	Medical suites, retail, hotel	0	0	3	5	Discounted at WACC of 10%
Sembawang, Singapore	100%	Residential	5	1,560	4	62	Discounted at WACC of 10%
			5	1,560		67	
Johor							
Bukit Lenang	80%	Residential	65	698	3	67	Discounted at WACC of 10%
Medini	38%	Mixed development	656	11,293	15	584	Discounted at WACC of 10%
Pendas	60%	Mixed development	1,079	18,000	20	671	Discounted at WACC of 10%
			1,800	29,991		1,323	
China							
Sunway Guanghao	65%	Mixed development	4	67	2	5	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%	Condos	24	702	5	10	Discounted at WACC of 10%
Sunway MAK Signature Residence (JV with M.A.K Builders)	60%	Residential	14	181	5	12	Discounted at WACC of 10%
Australia							
Wonderland Business Park (Sydney)	45%	Industrial	13	44	3	2	Discounted at WACC of 10%
			61	1,569		57	
Total			3,301	50,520		3,251	

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

Sunway RNAV

	Value (M\$ M)	Comments
Revaluation surplus	3,251	
Book value as at Dec-16	7,125	
Revaluation gain from investment properties	307	Value 36%-owned Sunway REIT at PT of M\$1.70
Revaluation gain from construction division	1,083	Valued at market price of M\$2.00/share
Outstanding cash obligation for land	(697)	Discounted value for Iskandar land purchase
Total RNAV	11,069	
Number of shares (M)	2,033	
RNAV per share (M\$)	5.45	
PT (M\$)	3.90	30% discount to RNAV

Source: J.P. Morgan estimates.

Risks to Rating and Price Target

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 36%-held

Sunway REIT, resulting in value-unlocking for shareholders; and (3) stronger-than-expected property sales. 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 14 June 2017)

Eco World Development (ECOW.KL/M\$1.62/Overweight), SP Setia (SETI.KL/M\$3.82/Overweight)

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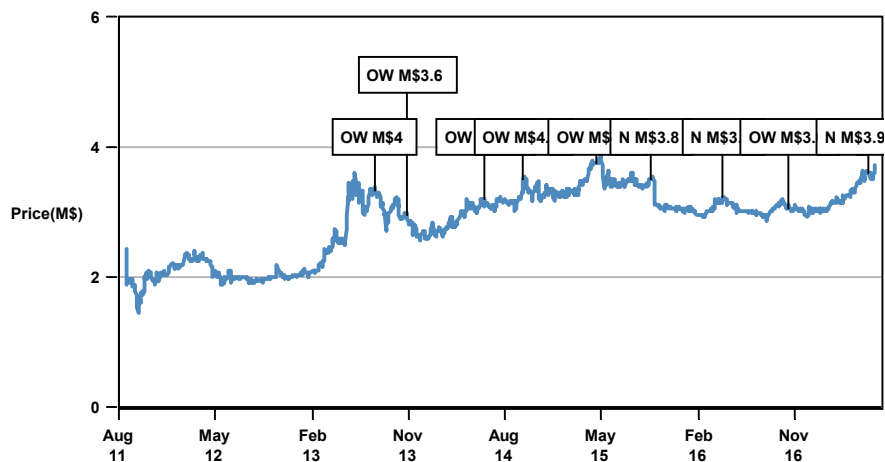
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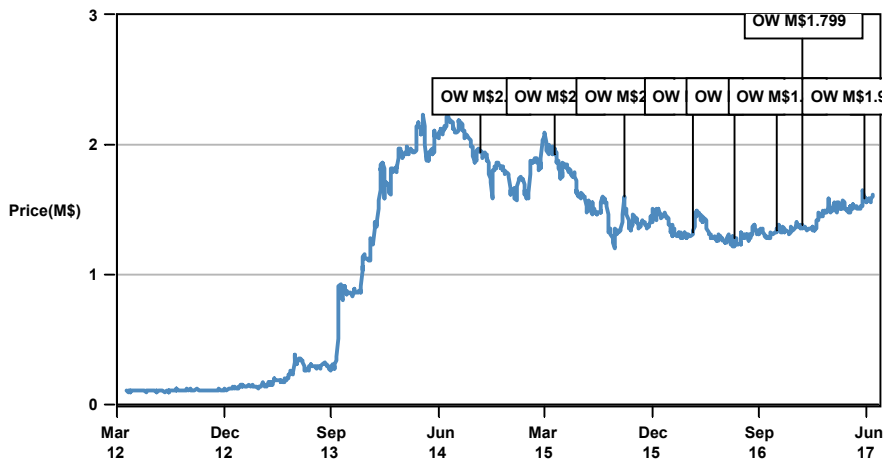
Sunway Bhd (SWAY.KL, SWB MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
26-Jul-13	OW	3.31	4.00
28-Oct-13	OW	2.95	3.60
05-Jun-14	OW	3.19	3.80
22-Sep-14	OW	3.52	4.10
17-Apr-15	OW	3.75	4.30
19-Sep-15	N	3.50	3.80
08-Apr-16	N	3.24	3.30
14-Oct-16	OW	3.06	3.60
26-May-17	N	3.60	3.90

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

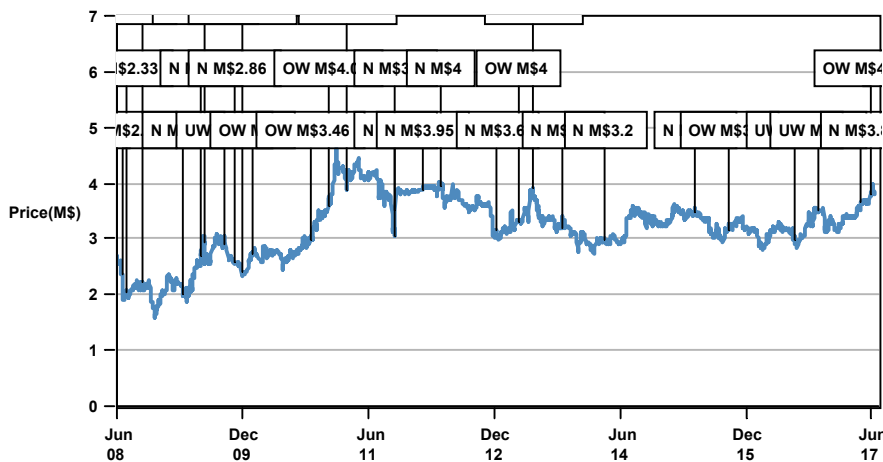
Eco World Development (ECOW.KL, ECW MK) Price Chart



Date	Rating	Share Price (M\$)	Price Target (M\$)
16-Sep-14	OW	1.94	2.40
27-Mar-15	OW	1.93	2.60
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	1.38	1.80
26-May-17	OW	1.59	1.90

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\$)
24-Jun-08	N	2.36	2.46
16-Jul-08	N	2.04	2.33
25-Sep-08	N	2.21	2.00
19-Mar-09	N	2.03	1.80
02-Jun-09	N	2.71	2.40
18-Jun-09	UW	2.96	2.53
17-Sep-09	UW	2.92	2.60
30-Oct-09	N	2.57	2.86
04-Dec-09	OW	2.40	2.86
14-Jan-10	OW	2.73	3.00
23-Sep-10	OW	2.99	3.46
10-Dec-10	OW	3.57	4.06
28-Feb-11	OW	3.89	4.50
22-Sep-11	N	3.06	3.50
28-Sep-11	N	3.50	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	3.91	4.60
23-Sep-13	N	3.20	3.50
26-Mar-14	N	2.98	3.20
17-Apr-15	N	3.47	3.50
19-Sep-15	OW	3.17	3.80
27-Jun-16	UW	2.98	2.80
14-Oct-16	UW	3.50	3.10
17-Apr-17	N	3.67	3.80
26-May-17	OW	3.79	4.40

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

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IB clients*	66%	63%	47%

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