

Sunway Bhd (SWB MK)

1Q17 within expectations; slow start to Property Development

Neutral

Price: M\$3.59

29 May 2017

Price Target: M\$3.90

PT End Date: 30 Dec 2017

Results were within expectations, with core net income up 3% Y/Y to make 19% of JPMe/consensus. We expect seasonal weakness and lumpy contributions to normalize for the Property Development, Construction, and Quarry segments over the rest of the year, while Property Investment should remain strong on the opening of Velocity Mall in Dec-16. We like Sunway Bhd (SWB) in the longer term for its integrated businesses, strong branding, and asset-light model, but believe that at the mean discount to RNAV, the stock is fully valued after its recent 8% outperformance vs the KLCI, **hence our recent downgrade on SWB to Neutral** in our 26 May 2017 sector report entitled *Malaysia Developers: Bottoming, expecting a gradual lift: Still OW on ECW, upgrade SPSB and UEMS to OW, cut SWB to Neutral [here](#)*. Our top picks are **Eco World (OW) and SP Setia (OW, SPSB)**, and we are also **OW on UEM Sunrise (UEMS)**.

- **1Q17 core net income made 19% of JPMe/consensus**, in line with results from peers SPSB and UEMS. Overall, seasonal weakness and lumpy contributions in the Property Development, Construction, and Quarry segments was balanced by stronger Property Investment, lower minorities, and higher finance income.
- **Property Development started the year slow**, with profits down 86% Y/Y on lower progress billings in the seasonally weak first quarter and lumpy contribution from projects approaching completion. However, we expect contributions to improve supported by group unbilled sales of M\$1.4B, or at 1.2x historical revenue. **Group pre-sales made 13% of management's M\$1.1B target**, but this was in line with peers that have reported. While domestic pre-sales were down 59%Y/Y to make only 8% of our forecast, we expect this to improve with M\$2B in planned launches coming mainly in 2H17 (vs M\$650MM for 2016).
- **Prop investment up 21% Y/Y on the opening of Velocity Mall**, adding 880,000 sqft in NLA to SWB's asset portfolio from Dec-16, **compensating for weaker Construction and Quarry**, down 2% Y/Y and 86% Y/Y, respectively, on lumpy contributions.

Table 1: Sunway: 3Q16 results summary

M\$ mn, YE Dec	1Q17	1Q16	Y/Y	4Q16	Q/Q
Revenue	1,091	1,069	2%	1,364	-20%
Core Operating profit	117	150	-22%	252	-54%
Operating margin	10.7%	14.0%		18.4%	
Net finance costs	-7	-16	-58%	-26	-74%
Associates & JVs	43	43	1%	45	-4%
Core PBT	153	178	-14%	230	-33%
Net income	108	102	6%	186	-42%
Core net income	108	105	3%	162	-33%
Core margin	9.9%	9.8%		11.9%	
Core EPS (sen)	5.28	5.59	-6%	7.85	-33%

Source: Company.

Table 2: Sunway: 3Q16 core operating profit breakdown

M\$mn, YE Dec.	1Q17	1Q16	Y/Y	4Q16	Q/Q
Prop development	8	56	-86%	119	-93%
Prop investment	44	36	21%	52	-15%
Construction	35	36	-2%	28	23%
Trading & Manufacturing	13	9	47%	21	-39%
Quarry	1	6	-86%	1	-39%
Others	17	7	135%	30	-45%
Core operating profit	117	150	-22%	252	-54%

Source: Company.

Table 3: Sunway: 3Q16 core operating margins

M\$mn, YE Dec.	4Q16	4Q15	Y/Y	3Q16	Q/Q
Property Development	5.5%	23.8%	-18 ppts	28.8%	-23 ppts
Property Investment	23.6%	21.5%	2 ppts	29.9%	-6 ppts
Construction	11.0%	11.4%	0 ppts	8.5%	2 ppts
Trading & Manufacturing	5.1%	4.4%	1 ppts	9.6%	-5 ppts
Quarry	2.2%	16.5%	-14 ppts	2.7%	0 ppts
Others	10.5%	5.8%	5 ppts	17.4%	-7 ppts
Core operating margin	10.7%	14.0%	-3 ppts	18.4%	-8 ppts

Source: Company.

Table 4: Developer domestic pre-sales

M\$mn	1QCY17	1QCY16	Y/Y	4QCY16	Q/Q
SP Setia	352	264	33%	1,686	-79%
Sunway	75	184	-59%	175	-57%
UEM Sunrise	146	56	160%	567	-74%
TOTAL DEVELOPERS	573	504	14%	2,428	-76%

Source: Companies.

Table 5: Developer peer comparison

As at: 29 May-17	FYE	Mkt cap (US\$m)	Price (M\$)	Rating	Target (M\$)	P/E (x)		EPS growth		Net div yield		P/B (x)	ROE (x)	RNAV (x)	Prem/disc to RNAV
						CY17E	CY18E	CY17E	CY18E	FY17E	FY18E				
Eco World Develop	Oct	1,089	1.58	OW	1.90	27.3	16.3	21.2%	68.1%	0.0%	0.0%	1.1	4.4	2.90	-46%
Mah Sing Group	Dec	880	1.56	N	1.65	11.9	12.8	-6.6%	-7.1%	3.3%	3.1%	1.1	11.3	2.15	-27%
SP Setia	Dec	2,532	3.79	OW	4.40	15.1	17.4	-4.4%	-12.8%	4.7%	3.5%	1.2	7.8	6.10	-38%
Sunway	Dec	1,710	3.59	N	3.90	12.8	12.0	1.6%	6.7%	3.4%	3.7%	1.0	7.5	5.45	-34%
UEM Sunrise	Dec	1,317	1.24	OW	1.60	30.8	28.0	41.1%	10.1%	0.0%	1.0%	0.9	2.8	2.90	-57%
Weighted average		7,527				18.7	17.3	-0.2%	-0.7%	2.8%	2.5%	1.1	6.8		-40%

Source: Bloomberg, J.P. Morgan estimates.

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 what we believe to be 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 Montereiz	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.

Property

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Other Companies Discussed in This Report (all prices in this report as of market close on 29 May 2017)

Eco World Development (ECOW.KL/M\$1.58/Overweight), SP Setia (SETI.KL/M\$3.79/Overweight), UEM Sunrise Bhd (UMSB.KL/M\$1.24/Overweight)

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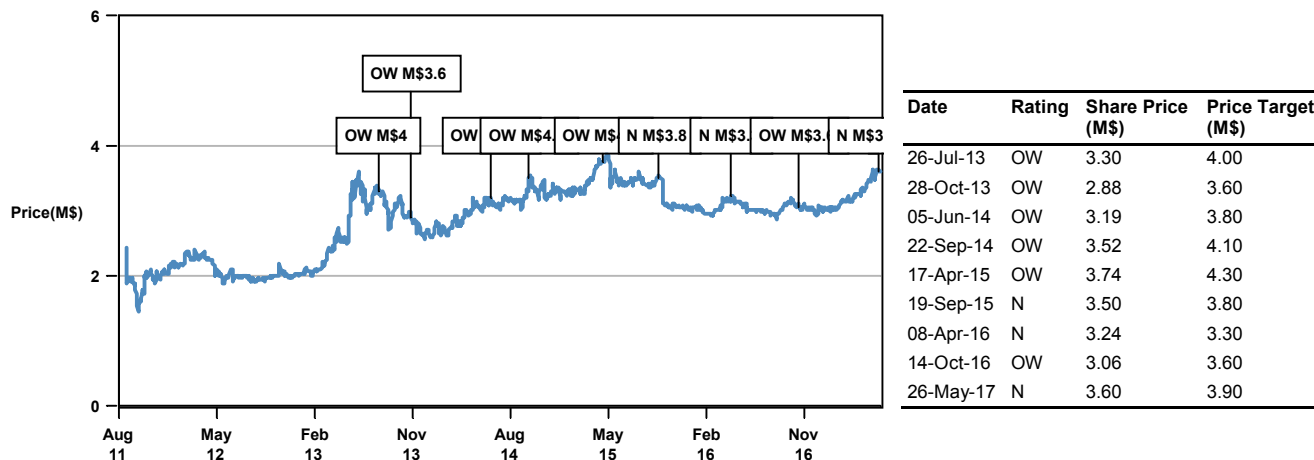
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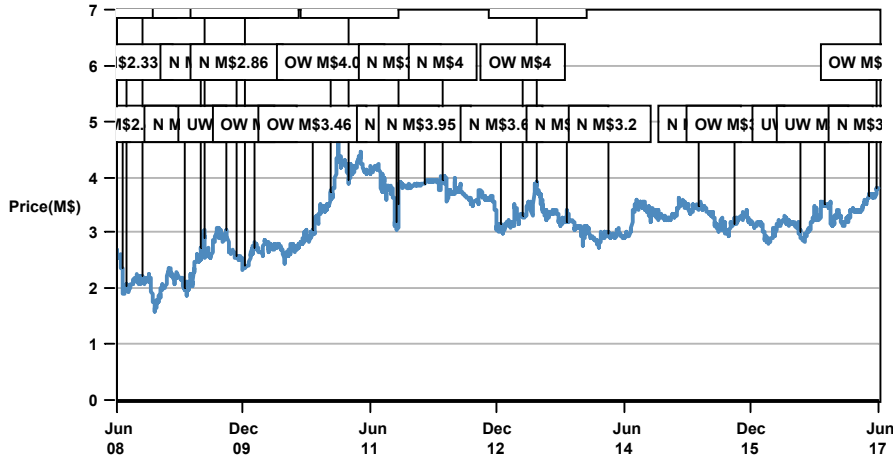
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Sunway Bhd (SWAY.KL, SWB MK) Price Chart



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

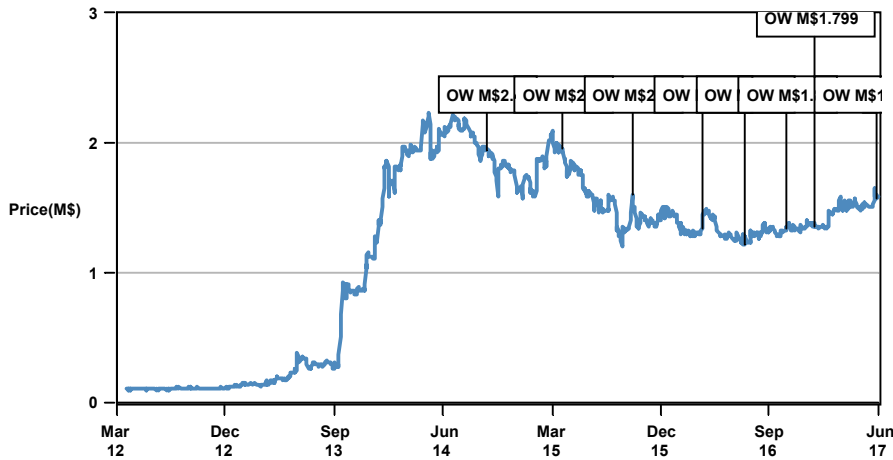
SP Setia (SETI.KL, SPSB MK) Price Chart



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

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	2.72	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	2.40	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	3.94	4.50
22-Sep-11	N	3.19	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	3.30	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	3.01	2.80
14-Oct-16	UW	3.50	3.10
17-Apr-17	N	3.67	3.80
26-May-17	OW	3.79	4.40

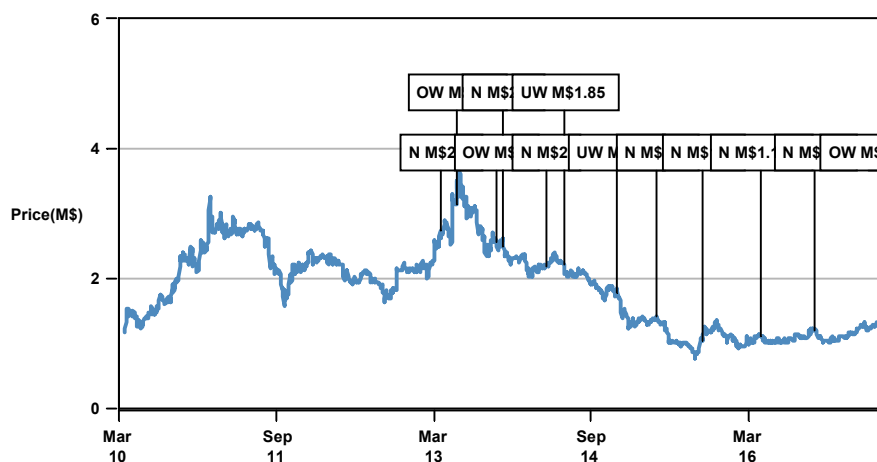
Eco World Development (ECOW.KL, ECW MK) Price Chart



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\$)
16-Sep-14	OW	1.94	2.40
27-Mar-15	OW	1.95	2.60
19-Sep-15	OW	1.60	2.10
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	1.57	1.90

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	3.15	3.60
05-Oct-13	OW	2.56	3.00
28-Oct-13	N	2.50	2.30
26-Mar-14	N	2.18	2.00
27-May-14	UW	2.23	1.85
27-Nov-14	UW	1.79	1.70
17-Apr-15	N	1.41	1.50
19-Sep-15	N	1.06	1.20
08-Apr-16	N	1.11	1.10
14-Oct-16	N	1.21	1.10
26-May-17	OW	1.28	1.60

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

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