

15 June 2017

Property | Real Estate

Sunway

Buy (Maintained)

Focusing On Value Creation

Yesterday's briefing should boost investors' confidence after executive chairman Tan Sri Dr Jeffrey Cheah shared his strategy for Sunway going forward. Apart from the excitement from the bonus issue and free warrants, we believe investors would gradually re-rate the firm given its healthcare wing's rising earnings base over the medium term. An asset monetisation angle may also be a share price catalyst over the next 1-2 years. **Maintain BUY with a new MYR4.28 TP (from MYR3.95, 15% upside).**

Bonus issue + warrants. Along with its AGM yesterday, Sunway announced a 4-for-3 bonus issue – capitalising on its share premium – and three free warrants for every 10 existing shares. While the bonus issue is already considered a big reward to shareholders, we think the free warrants are also very attractive, given the annual step-down feature for its exercise price over the 7-year tenure. According to management, the exercise price could be 5-7 sen lower pa. This means that the reference price for the warrants could be around 45-50 sen, given the option value and time value for money.

Rationale for recent sector reclassification. We view Sunway's reclassification to the trading/services sector more positively after the briefing. Unlike other pure developers that have to ride through the current cyclical property market slowdown, it is able to take the opportunity to grow its other divisions given its diversified business portfolio. As earnings from the healthcare, trading, and construction segments have been growing steadily, valuations for these divisions should not be ignored. Its earnings profile has, thus, changed over time, with its property development and investment divisions making up only 48% of FY16 earnings (FY12: 75%), while the trading & services segment's contribution increased to 42% last year (FY12: 14%).

Healthcare division could re-rate valuations. Management has allocated a MYR1bn capex to grow its healthcare division. Total number of beds is to increase by 1,090 by end 2020 (618 currently). Therefore, earnings from the division are likely to double in 3-4 years' time from the MYR45-50m forecasted by management for FY17. We believe investors would gradually appreciate the value of Sunway's healthcare division, given the premium valuations attached by the market on some of the healthcare stocks. Management also indicated tentative plans to list this business in the future.

Asset monetisation another re-rating catalyst. While the healthcare division could be a valuation kicker over the next 3-4 years, we think investors should also watch out for Sunway's asset monetisation move over the next 1-2 years. Its pool of investment properties has been growing. Among the assets that are completed and could be injected include Sunway CLIO Hotel, Sunway Pinnacle and Sunway Velocity Mall, which are worth almost MYR2bn. Asset disposal could possibly provide an angle for special dividends.

Maintain BUY. We revise our RNAV estimate as we now attach a separate valuation for Sunway's healthcare division. Our new TP is now MYR4.28 (from MYR3.95), based on a 30% discount to property RNAV and 10% holding company discount. Post bonus issue, our new TP is adjusted to MYR1.84. Weaker-than-expected market conditions are a risk to our call.

Forecasts and Valuations	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Total turnover (MYRm)	4,451	4,726	5,068	5,528	5,993
Reported net profit (MYRm)	620	586	562	606	658
Recurring net profit (MYRm)	597	547	562	606	658
Recurring net profit growth (%)	0.9	(8.3)	2.6	7.8	8.7
Recurring EPS (MYR)	0.33	0.27	0.27	0.29	0.31
DPS (MYR)	0.49	0.12	0.13	0.14	0.15
Recurring P/E (x)	11.2	14.1	13.8	13.0	12.0
P/B (x)	1.02	1.03	1.00	0.97	0.94
Dividend Yield (%)	13.1	3.3	3.5	3.8	4.0
Return on average equity (%)	9.9	8.4	7.4	7.7	8.0
Return on average assets (%)	4.3	3.4	2.9	3.0	3.1
Net debt to equity (%)	45.3	40.9	39.1	39.0	40.2
Our vs consensus EPS (adjusted) (%)			(5.7)	(7.2)	(3.2)

Source: Company data, RHB

Target Price:	MYR4.28
Price:	MYR3.73
Market Cap:	USD1,785m
Bloomberg Ticker:	SWB MK

Share Data

Avg Daily Turnover (MYR/USD)	8.66m/2.00m
52-wk Price low/high (MYR)	2.87 - 3.73
Free Float (%)	39
Shares outstanding (m)	1,724
Estimated Return	15%

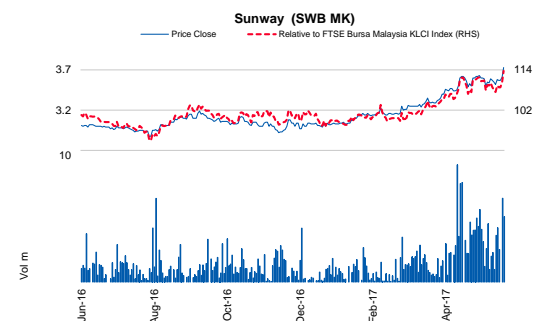
Shareholders (%)

Tan Sri Dato' Jeffrey Cheah	55.4
Employees Provident Fund	5.7

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	23.1	4.8	18.0	22.7	23.9
Relative	13.9	3.9	13.9	13.6	13.7

Source: Bloomberg



Source: Bloomberg

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Financial Exhibits

Financial model updated on: 2017-06-14.

Asia	Financial summary	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Malaysia	Recurring EPS (MYR)	0.33	0.27	0.27	0.29	0.31
Property	EPS (MYR)	0.34	0.28	0.27	0.29	0.31
Sunway	DPS (MYR)	0.49	0.12	0.13	0.14	0.15
Bloomberg	BVPS (MYR)	3.64	3.61	3.72	3.83	3.95
SWB MK	Weighted avg adjusted shares (m)	1,800	2,063	2,084	2,105	2,126
Buy						
Valuation basis	Valuation metrics	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
i. 30% discount to property RNAV;	Recurring P/E (x)	11.2	14.1	13.8	13.0	12.0
ii. 10% holding company discount.	P/E (x)	10.8	13.1	13.8	13.0	12.0
Key drivers	P/B (x)	1.02	1.03	1.00	0.97	0.94
i. New property sales;	FCF Yield (%)	(1.5)	(1.9)	8.7	7.0	5.4
ii. Disposal of investment properties.	Dividend Yield (%)	13.1	3.3	3.5	3.8	4.0
Key risks	EV/EBITDA (x)	15.3	13.3	12.8	12.5	12.5
Weaker-than-expected market conditions.	EV/EBIT (x)	18.5	16.3	15.6	15.0	15.2
Company Profile	Income statement (MYRm)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Sunway is a well-known developer in the Klang Valley. Its flagship project – Bandar Sunway – is a well-established integrated township, where the company successfully transformed mining land into a matured residential and commercial cluster.	Total turnover	4,451	4,726	5,068	5,528	5,993
	Gross profit	1,187	1,355	1,540	1,689	1,809
	EBITDA	693	892	950	1,023	1,076
	Depreciation and amortisation	(119)	(165)	(167)	(171)	(186)
	Operating profit	574	727	783	851	889
	Net interest	(27)	(60)	(49)	(43)	(30)
	Income from associates & JVs	270	192	326	368	383
	Pre-tax profit	816	859	1,060	1,176	1,242
	Taxation	(130)	(140)	(257)	(294)	(311)
	Minority interests	(67)	(133)	(242)	(276)	(273)
	Recurring net profit	597	547	562	606	658
	Cash flow (MYRm)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
	Change in working capital	60	(391)	(161)	(195)	(197)
	Cash flow from operations	864	569	753	760	809
	Capex	(963)	(713)	(75)	(211)	(380)
	Cash flow from investing activities	(2,109)	(971)	(275)	(411)	(580)
	Proceeds from issue of shares	1,067	588	0	0	0
	Dividends paid	(1,082)	(268)	(271)	(295)	(319)
	Cash flow from financing activities	1,987	1,750	(372)	(395)	(418)
	Cash at beginning of period	1,978	2,627	4,060	4,014	3,855
	Net change in cash	741	1,347	106	(45)	(189)
	Ending balance cash	2,719	3,974	4,165	3,968	3,666
	Balance sheet (MYRm)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
	Total cash and equivalents	2,627	4,060	4,014	3,855	3,587
	Tangible fixed assets	8,146	9,051	8,959	8,999	9,192
	Intangible assets	320	343	343	343	343
	Total other assets	463	286	812	1,380	1,962
	Total assets	15,994	18,831	19,588	20,496	21,469
	Short-term debt	3,304	4,831	4,831	4,831	4,831
	Total long-term debt	2,585	2,591	2,607	2,663	2,756
	Other liabilities	416	438	438	438	438
	Total liabilities	8,794	10,612	10,836	11,157	11,517
	Shareholders' equity	6,550	7,456	7,747	8,058	8,397
	Minority interests	651	764	1,005	1,281	1,555
	Total equity	7,200	8,219	8,752	9,339	9,952
	Net debt	3,262	3,361	3,424	3,639	4,000
	Total liabilities & equity	15,994	18,831	19,588	20,496	21,469
	Key metrics	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
	Revenue growth (%)	(8.1)	6.2	7.2	9.1	8.4
	Recurrent EPS growth (%)	(3.3)	(20.0)	1.6	6.7	7.6
	Gross margin (%)	26.7	28.7	30.4	30.6	30.2
	Operating EBITDA margin (%)	15.6	18.9	18.7	18.5	17.9
	Net profit margin (%)	13.9	12.4	11.1	11.0	11.0
	Dividend payout ratio (%)	174.7	45.8	45.8	45.8	45.8
	Capex/sales (%)	21.6	15.1	1.5	3.8	6.3
	Interest cover (x)	4.61	4.33	4.79	5.18	5.62

Source: Company data, RHB

Focusing On Value Creation

Details on bonus issue and warrants

To capitalise on its existing share premium, Sunway has announced a 4-for-3 bonus issue and three free warrants for every 10 existing Sunway shares. The warrants have tenure of seven years, with a special feature of step-down pricing mechanism for its exercise price pa. This feature should encourage long-term holding of the warrants, as it is more attractive to exercise the warrants in the later part of the tenure given the lower exercise price. Hence, immediate dilution can be avoided. In view of this, we, therefore, do not include the dilution impact arising from the warrants into our RNAV estimate.

Expansion on the healthcare segment

While the healthcare division is currently only contributing around 7% to total earnings, we believe this number would grow more substantially in the coming years. About MYR1bn is to be spent to build four new hospitals, including Sunway Medical Centre Velocity, Sunway Medical Centre Seberang Jaya, Sunway Medical Centre Ipoh and Sunway Medical Centre Damansara.

As the total number of beds would be increased by more than 1,000 upon the completion of all these hospitals by end 2020, we believe earnings from this business ought to reach the MYR100m mark in 4-5 years' time. In our view, management's decision to reclassify Sunway under the trading/services sector is to remind investors of the company's value in its other business divisions, which have been largely ignored by the market.

Given the current premium market valuations for most of the healthcare stocks in Malaysia, we think investors would gradually re-rate Sunway. This is because its exposure to the healthcare business is getting more significant. During the briefing, management has also indicated its plan to list the division when the earnings base is more meaningful. Although this may take years to materialise, this plan, nevertheless, would underpin investor interest on the stock over the longer term.

Re-visiting the property segment when the time is right

As for the property development division, management is not too concerned with the current cyclical slowdown in the property market. Local property projects are to be carefully selected before being rolled out. Management may also evaluate the opportunities to undertake property projects overseas, including those in Singapore, China and, possibly, Australia.

Figure 1: Sunway’s changes in earnings contributions by divisions

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%

Note:
* Incorporates the reduction in contribution in the Construction division to 54.4% following its listing in July 2015.

Source: Company data

Figure 2: Sunway’s new medical centres in the pipeline



Source: Company

Figure 3: RNAV estimate

Developments	Remaining		Effective stake	NPV @ 11%
	Landbank (acre)	GDV (MYR m)		
Selangor/KL				
Sunway Damansara	15.36	1,691.28	60%	108.4
Sunway South Quay	40.16	3,086.66	60%	176.5
Sunway Montez	4.40	38.00	60%	2.5
Sunway Semenyih	398.11	728.59	70%	45.6
Sunway Cheras	5.97	16.82	100%	1.4
Sunway Duta	3.16	120.00	60%	6.1
Sunway Montana	1.99	55.51	100%	5.7
Sunway Resort City	14.9	660	100%	61.9
Sunway Velocity	10.00	1,983.98	85%	163.5
Sunway Velocity 2	8.45	2,000.00	50%	52.9
Sunway Tower KL 1	1.00	240.00	100%	19.3
Melawati	2.00	43.00	100%	4.0
Sg Long	111.00	277.00	80%	17.8
Mont Putra, Rawang	163.00	156.00	100%	12.5
Kelana Jaya	21.84	1,900.00	100%	121.6
Subang industrial	6.35	110.00	80%	5.9
Perak				
Sunway City Ipoh	440.5	1,048.38	65%	55.9
Penang				
Sunway Hills	80.70	849.00	100%	66.0
Sunway Wellesley, Bukit Mertajam	52.80	725.47	100%	68.0
Paya Terubong	24.46	1,500.00	100%	117.2
Sunway Tunas, Balik Pulau	9.00	60.00	100%	6.2
Sunway Betong, Balik Pulau	19.87	110.00	100%	11.4
S'pore				
Anchorvale Lane, Sengkang	5.19	1,560.00	30%	38.8
Johor				
Bukit Lenang	64.79	698.40	80%	56.8
Medini	655.73	11,293.00	56%	491.4
Pendas	1,079.07	18,000.00	60%	566.7
China				
Sunway Guanghao	3.73	66.78	65%	3.9
Tianjin Eco City	6.23	575.02	60%	24.4
India				
Sunway OPUS Grand India	23.80	702.36	50%	20.2
Sunway MAK Signature Residence (JV with M.A.K Builders)	14.00	181.22	60%	6.6
Australia				
Wonderland Business Park (Sydney)	12.99	43.80	45%	1.1
Unbilled sales				195.0
TOTAL	3,322.02	55,375.03		2,535.22

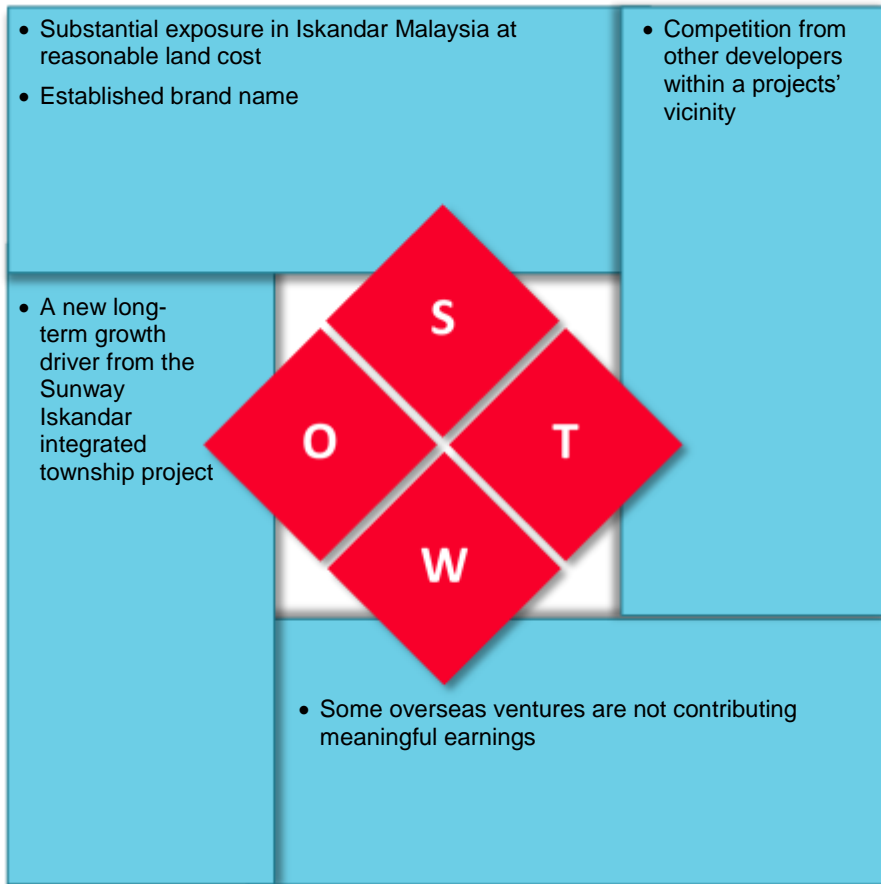
Investment properties	EBITDA (MYR m)	Est. market value (MYR m)	Book value (MYR m)	Equity interest	Net surplus (MYR m)
Monash University Campus	17	299.5	299.5	100%	0
Monash U Residence	15	226.6	226.6	100%	0
Sunway University College	10	255.0	255.0	100%	0
Sunway Hotel Georgetown	4	74.0	37.6	100%	36.4
Sunway Hotel Phnom Penh	2	17.3	17.3	53%	0
Sunway Hotel Hanoi	2	8.8	8.8	100%	0
Sunway Giza	5	55.1	55.1	60%	0
Sunway Pinnacle	N/A	406.0	350.7	100%	47.0
Sunway Velocity Mall	N/A	1,710.0	1,172.3	100%	457.0
Sunway Clio Hotel	N/A	352.9	296.3	100%	48.1

Subtotal	3,123.79
Shareholders' equity (ex cons. & healthcare)	6,905.72
Total	10,029.51
Discount to Property RNAV	30%
Discounted Property RNAV	7,020.66

Other divisions	Market value (MYR m)	Book value (MYR m)	Est. FY17 earnings (MYR m)	PE target (x)	Equity value surplus (MYR m)
34% Sunway REIT	1,654.2	1,479.0			175.16
54.4% Sunway Construction	1,442.0	844.1			597.88
Healthcare			46	25	1,150.00
Others			65	8	520.00
Total					9,463.70
ESOS proceeds					551.52
Warrants conversion @ MYR2.25					651.13
Total RNAV					10,666.35
Holding company discount					10%
Discounted RNAV					9,599.72
Share base (mil)					1,780.00
No. of warrants					289.39
ESOS					172.35
Enlarged share base (mil)					2,241.74
TP (MYR)					4.28

Source: RHB

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2017-05-29	Buy	3.95	3.59
2017-02-28	Buy	3.55	3.23
2016-11-27	Buy	3.40	3.00
2016-08-29	Buy	3.40	3.01
2016-05-29	Buy	3.40	3.03
2016-02-29	Buy	3.40	3.00
2016-02-22	Buy	3.60	2.97
2015-11-27	Buy	3.60	3.07
2015-09-03	Buy	3.86	3.45
2015-08-27	Buy	4.10	3.40

Source: RHB, Bloomberg

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