

Singapore Company Guide

Sunpower Group Ltd

Version 1 | Bloomberg: SPWG SP | Reuters: SUNP.SI

Refer to important disclosures at the end of this report

DBS Group Research . Equity

2 Mar 2020

This coverage is under the MAS GEMS scheme

BUY

Last Traded Price (28 Feb 2020): S\$0.525 (STI : 3,011.08)

Price Target 12-mth: S\$0.84 (61% upside) (Prev S\$0.81)

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What's New

- FY19 underlying profit rose 31.5% y-o-y led by ramp up in GI projects
- M&S orderbook maintained at RMB2.5bn
- Gearing increased to 1.25x
- Maintain BUY, lift TP to S\$0.84 as we revise FY20F net profit up by 10%

Price Relative



Forecasts and Valuation

FY Dec (RMBm)	2019A	2020F	2021F	2022F
Revenue	3,605	4,322	4,954	5,029
EBITDA	696	762	949	1,008
Pre-tax Profit	240	337	491	627
Net Profit	138	224	314	429
Net Pft (Pre Ex.)	352	379	484	467
Net Pft Gth (Pre-ex) (%)	38.9	7.5	27.8	(3.5)
EPS (S cts)	3.48	5.65	7.92	10.8
EPS Pre Ex. (S cts)	8.87	9.54	12.2	11.8
EPS Gth Pre Ex (%)	34	8	28	(4)
Diluted EPS (S cts)	2.25	3.65	5.12	6.98
Net DPS (S cts)	0.20	0.32	0.45	0.62
BV Per Share (S cts)	43.5	48.8	56.3	89.0
PE (X)	14.9	9.2	6.6	4.8
PE Pre Ex. (X)	5.9	5.4	4.3	4.4
P/Cash Flow (X)	4.6	4.1	3.9	3.1
EV/EBITDA (X)	6.7	6.3	5.0	3.5
Net Div Yield (%)	0.4	0.6	0.9	1.2
P/Book Value (X)	1.2	1.1	0.9	0.6
Net Debt/Equity (X)	1.2	1.1	0.9	0.3
ROAE (%)	8.3	12.3	15.1	14.9
Earnings Rev (%):		0	0	0
Other Broker Recs:		B: 3	S: 0	H: 0

Source of all data on this page: Company, DBS Bank, Bloomberg Finance L.P

Racing for green

Green investment (GI) plant ramp up to drive growth.

Sunpower's GI plants have ramped up successfully, with GI operating cash flow rising by c.19% y-o-y to RMB252m. GI operating margin also improved by 1.6ppt. With the Shantou and Xintai Zhengda projects starting to ramp up in FY20F and FY21F, a further 1,080t/h of active steam capacity, representing c.50% of FY21F total active steam capacity, is expected to come online soon. This combined with the steady closure of small boilers and shifting of businesses to industrial parks will drive a 27.2% growth in GI operating profit for FY20F.

In line with its target of having RMB2.5bn in GI equity investments by FY21, Sunpower recently announced its plans to invest in the Tongshan Project in Xuzhou City. We estimate that Phase 1 of the project will start operating within two years with the cost of Phase 2 set to be cheaper than Phase 1.

Margin improvement in traditional manufacturing and services (M&S) driven by operational improvements.

Sunpower's M&S factory is operating at close to full utilisation on an order book of RMB2.5bn. The group is in a good position to cherry pick higher margin projects while keeping its orderbook steady.

Where we differ: We have assumed lower impact of COVID-19 on Yongxing and Xinyuan plant as a significant portion of their capacity is used for heating purposes and less linked to industrial activity.

Potential catalyst: Resolution of COVID-19 situation in China, new GI plant development or acquisition.

Valuation:

Maintain BUY with DCF-based TP of S\$0.84. Our TP is raised to S\$0.84 as we revised our earnings higher to reflect faster ramp up of GI projects. Our valuation excludes a potential RMB2.0bn in GI projects that Sunpower is expected to invest in by FY21F.

Key Risks to Our View:

Unfavourable changes in the regulatory environment; steep rise in coal prices; worsening of COVID-19 outbreak

At A Glance

Issued Capital (m shrs)	811
Mkt. Cap (S\$m/US\$m)	422 / 303
Major Shareholders (%)	
Gua Hong Xin	19.0
Ma Ming	17.0
Lin Yucheng	12.3
Free Float (%)	51.7
3m Avg. Daily Val (US\$m)	0.75

GIC Industry : Industrials / Capital Goods



Live more, Bank less

Sunpower Group Ltd

WHAT'S NEW

Racing for green

Sunpower's FY19 net profit above expectations.

- Revenue rose 10.5% y-o-y to RMB3,604.6m driven by a ramp-up in GI projects and new GI plant acquisitions.
- Underlying net profit leapt 31.5% y-o-y to RMB352.2m. The improved performance was similarly due to increasing capacity utilisation of GI plants, portfolio expansion and enhancement initiatives. We note that with the latest results, Sunpower appears to be on track to hit its convertible bond underlying profit targets of RMB370m and RMB460m in FY20 and FY21 respectively.
- A dividend of S\$0.0025 per share was declared, which while low in absolute terms still represents an increase of 31.6% y-o-y.

M&S margin improved; Orderbook stable

- M&S revenue declined to RMB2.4bn due to timing differences in contracts. Notably, M&S operating margin improved to 10.8% from 9.3% a year ago while orderbook remained at a healthy RMB2.5bn. The improvement in M&S margin came on the back of efforts to drive operational improvements.

Upcoming GI plants on track for completion.

Shantou Phase 1 currently in trial production while works for Shantou Phase 2 are undergoing. Xintai Zhengda project is nearing completion and expected to begin trial production in 1H20.

Tongshan Project to deliver long-term recurring cashflows.

Sunpower recently announced a planned investment of RMB420m into Phase 1 of the Tongshan Project in an estimated 75:25 debt-equity proportion. The plant, to be built in the Tongshan District of Xuzhou City, will comprise of 2x 130t/h steam boilers and 2x 35MW electricity generators and will supply civil heating to homes as well as electricity to the State Grid. Judging from past projects, we believe that Phase 1 may become operational within 2 years. While no plans for Phase 2 has been announced, we note that Phase 2 of Sunpower's greenfield developments have typically been cheaper and took a shorter time to complete.

COVID-19 virus outbreak.

The COVID-19 outbreak in China led to Lunar New Year holiday extensions that lasted till as late as 24 Feb. This had no doubt impacted many Chinese businesses with Sunpower

not being an exception. While meeting the convertible bond targets remains important, the health and safety of Sunpower's workers is paramount. Management has confirmed that none of Sunpower's staff have been infected with COVID-19 and has put in place measures to defend against the virus. With no end to the virus outbreak in sight, any impact on Sunpower's FY20 results remains uncertain. That said, due to the holiday extensions, Sunpower's GI plants saw lower capacity utilisation. As business in China returns to normalcy, we expect topline growth to slow by c.3% attributed to COVID-19.

FY20F and FY21F net profit revised up by 10% and 29% respectively to account for faster ramp up in GI projects.

We had previously assumed later completions and ramp up of GI plants in Shantou and Xintai Zhengda. Together, these projects have an active steam capacity of 1,080t/h representing c.50% of FY21F active steam capacity.

As a result of this assumption, our previous GI operating margins were more conservative at 25.5% for FY21F. With the Shantou and Xintai Zhengda projects looking to ramp up soon and the achievement of a 28.2% GI operating margin for FY19, we believe these projects will see higher capacity utilisation than previously forecasted with GI operating margins to maintain at 28.2% for FY20F and FY21F.

Additionally, we have factored in the new development of the Tongshan Project with the assumption of it beginning operations towards the end of FY21F.

Overall, these changes led to our revision in net profit by 10% and 29% for FY20F and FY21F. Following Sunpower's beat in FY19 underlying profit guidance of c.RMB300m by c.17%, we believe that Sunpower is on track to meet its convertible bond targets and raise our TP to S\$0.84 (previously S\$0.81).

As a side note, our FY22F underlying net profit (i.e. net profit pre ex) was down 3.5% from the previous year. This is attributed to forecasted lower revenue from service concession arrangements for M&S due to lower plant construction activity. FY22F net profit was however up from the previous year as we expect the convertible bonds to mature, resulting in lower finance expenses.

Sunpower Group Ltd
Quarterly / Interim Income Statement (RMBm)

FY Dec	4Q2018	3Q2019	4Q2019	% chg yoy	% chg qoq
Revenue	1,280	778	1,356	6.0	74.4
Cost of Goods Sold	(993)	(580)	(1,008)	1.5	73.7
Gross Profit	286	197	348	21.6	76.4
Other Oper. (Exp)/Inc	(69.7)	(88.5)	(88.6)	27.2	0.1
Operating Profit	217	109	259	19.8	138.5
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	-	-
Associates & JV Inc	(0.2)	0.31	0.26	nm	(15.5)
Net Interest (Exp)/Inc	44.5	(57.1)	49.7	11.7	nm
Exceptional Gain/(Loss)	68.0	78.8	(190)	nm	nm
Pre-tax Profit	329	131	119	(63.7)	(8.8)
Tax	(34.8)	(22.0)	(37.3)	6.9	69.1
Minority Interest	(9.1)	1.57	(7.4)	18.4	nm
Net Profit	285	110	74.5	(73.8)	(32.4)
Net profit bef Except.	217	31.5	265	22.1	740.1
EBITDA	249	144	295	18.3	104.4
Margins (%)					
Gross Margins	22.4	25.4	25.7		
Opg Profit Margins	16.9	14.0	19.1		
Net Profit Margins	22.3	14.2	5.5		

Source of all data: Company, DBS Bank

Sunpower Group Ltd

CRITICAL DATA POINTS TO WATCH

Critical Factors

GI asset acquisitions or new greenfield developments

Sunpower recently announced the planned investment in the Tongshan Project that will add 260t/h in steam production and 70MW of electricity generation capacity to the GI portfolio. As a result, Sunpower's total GI active steam capacity may rise to an estimated c.2,450t/h upon completion of the Tongshan Project. Taking into account the RMB420m cost for Tongshan Phase 1, we estimate that Sunpower still has a remaining c.RMB2.0bn of GI investments to be made in order to hit its FY21 target. A portion of this may go to Phase 2 of the Tongshan Project which we believe could cost between RMB300m – RMB400m.

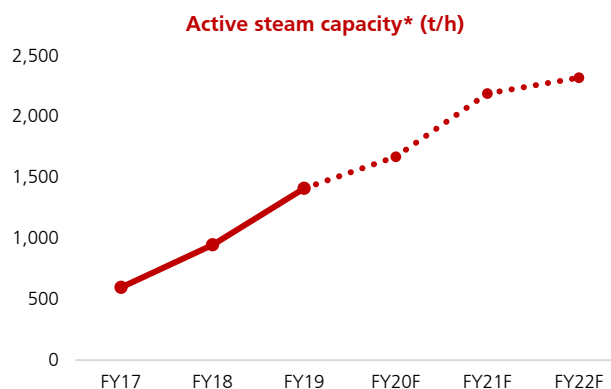
M&S order book size and margins. M&S order book has remained robust, maintaining at RMB2.5bn. Operating margins for the segment has also improved rising to 10.8% from 9.3%. This was largely driven by operational improvements and the ability to cherry pick orders due to the high factory utilisation. Going forward, while the COVID-19 has introduced more uncertainty into Sunpower's business, we believe there is a chance for a further improvement in margins or a rise in order book as smaller players face operational disruptions, resulting in customers gravitating to Sunpower. That said, lower contributions from revenue from service concession arrangements due to lower plant construction activity may weigh on margins.

Chinese government regulations and plans

Changes to regulations surrounding environmental standards may affect Sunpower's share price due to the potential impact on demand for environment protection products and steam plants. Amidst the COVID-19 outbreak, the government has extended the holiday period in China which has caused disruptions to factory operations. Looking at environmental regulations, we will be monitoring news surrounding the 14th Five-Year Plan set to be endorsed in March 2021. The 13th Five-Year Plan provided the framework for environmental regulations enacted from 2016 – 2020, as such we believe that the new plan play a similar role.

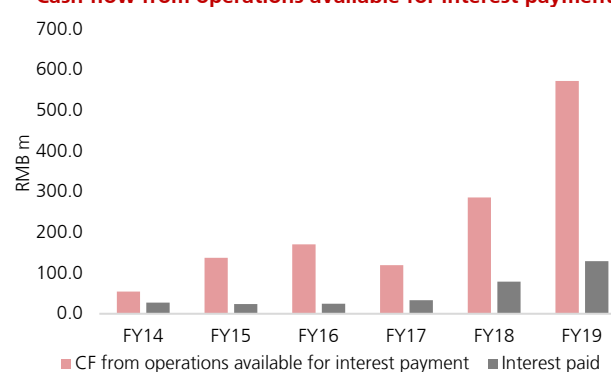
Outlook on China's thermal coal price

Sunpower's GI plants are mostly reliant on coal as a source of energy in the production of steam. Burning coal has largely been thought of to be harmful for the environment. That said, a key innovation has enabled Sunpower's GI plants to harness coal as a source of energy and operate in a less pollutive and greener manner as compared to other sources of energy such as natural gas.

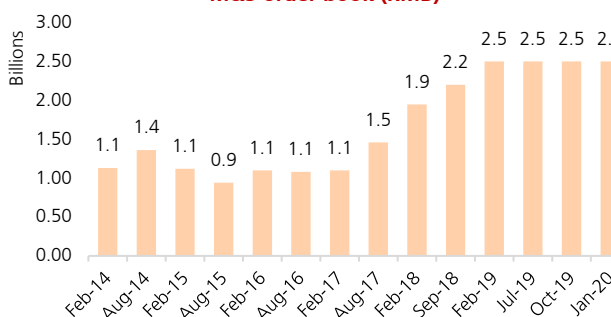


*assuming Phase 1 Tongshan completed in FY22

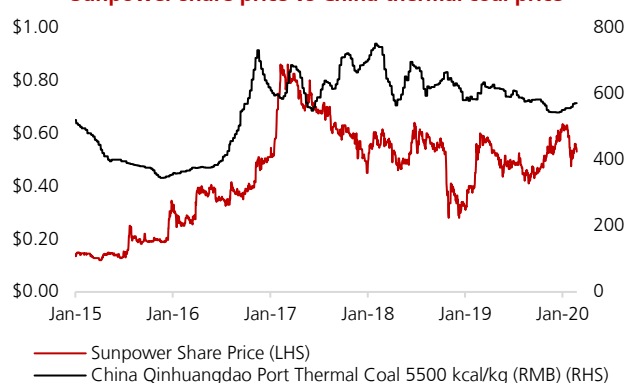
Cash flow from operations available for interest payment



M&S order book (RMB)



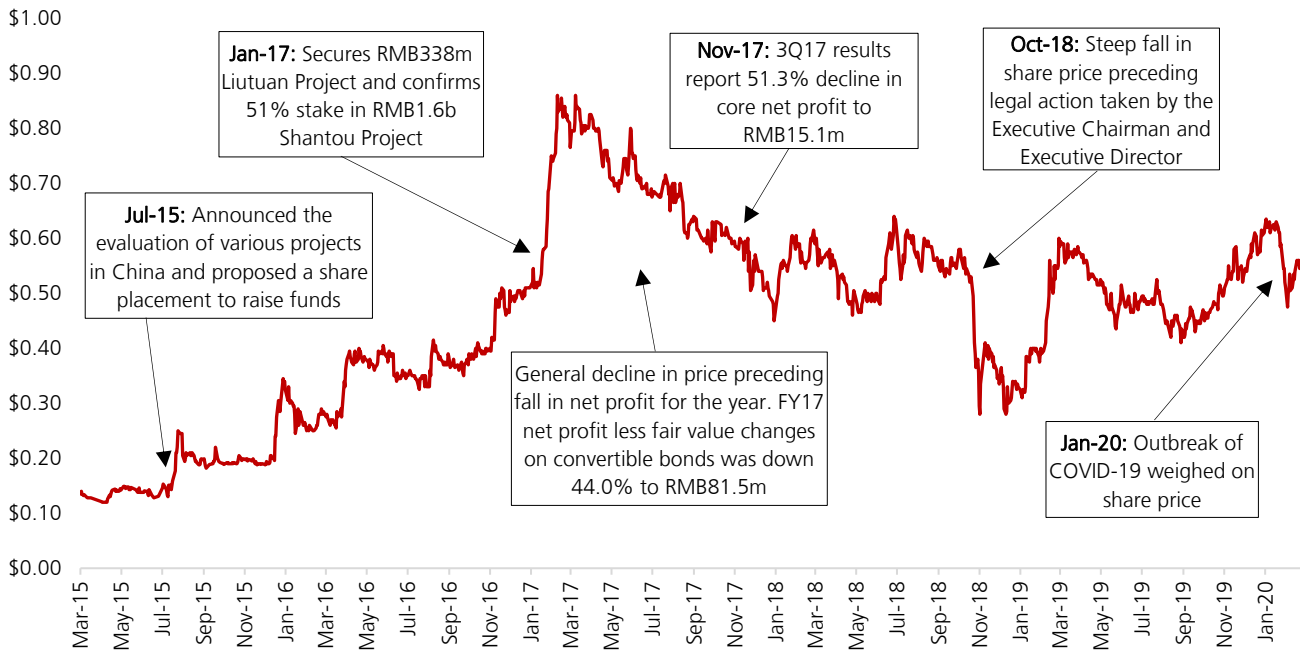
Sunpower share price vs China thermal coal price



Source: Company, DBS Bank

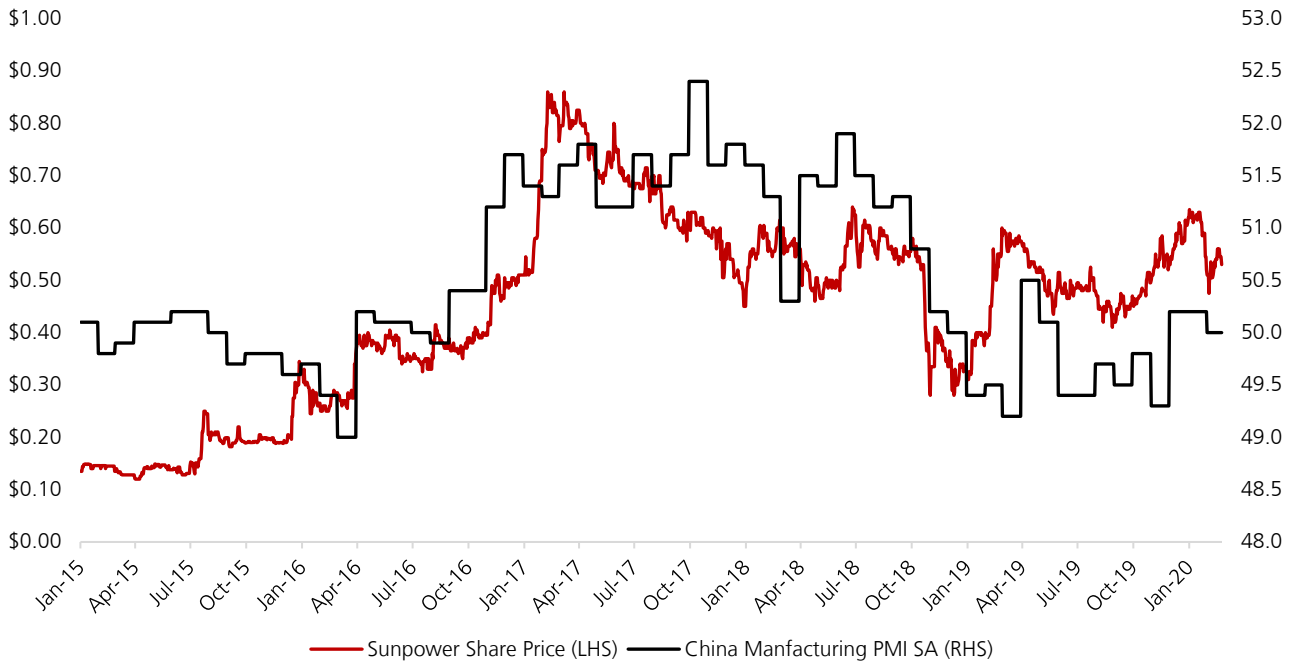
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Appendix 1: A look at Company's listed history – what drives its share price?



Source: Bloomberg Finance L.P., DBS Bank

Sunpower's share price vs China Manufacturing PMI SA



Source: Bloomberg Finance L.P., DBS Bank

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Balance Sheet:

Gearing (net debt-equity) rose to 1.25x. Going forward, we believe that gearing will trend higher as Sunpower aims to meet its investment target of RMB2.5bn in equity for GI projects in a 40:60 equity-debt proportion. Taking into account Sunpower's recent planned investment in Tongshan, gearing may rise to c.1.3x by end-FY20 from 1.25x as at end-Dec 2019.

Share Price Drivers:

Rise in M&S segment margins or orderbook. With orderbook remaining stable at RMB2.5bn, a rise in orderbook could signify Sunpower's success in securing higher margin projects given that current factory utilisation is at peak level.

New GI asset acquisitions or developments. Sunpower's share price is partly driven by steam production capacity which in turn is dependent on the number of plants and boilers it operates. Following the announcement of the Tongshan Project, we think new plant acquisitions may be on the horizon with a further RMB2.1bn to deploy given the group's GI investment target.

Key Risks:

Regulatory risk. Sunpower's GI plants are subject to negotiable caps on the steam tariffs charged. This may lead to hurdles when raising prices in future. That said, coal prices have largely been capped, resulting in no need for prices to be raised beyond the caps.

Miss in convertible bond performance targets. Sunpower is required to hit an adjusted PATMI target of RMB370m and RMB460m for FY20 and FY21 respectively under its convertible bond deals. Missing these targets would entitle the convertible bond owners to a lower conversion price that would be dilutive to other shareholders.

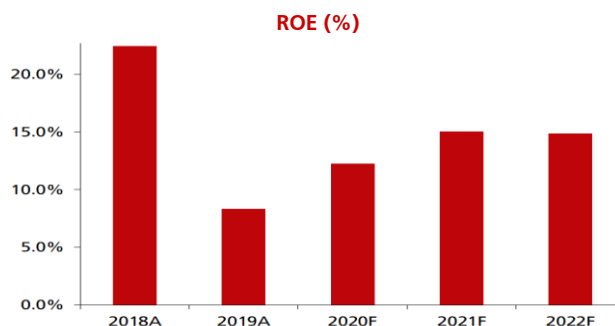
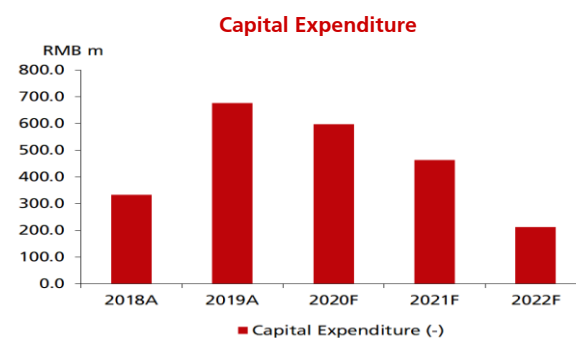
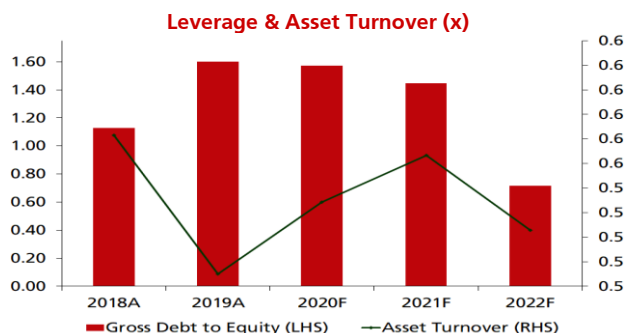
COVID-19 outbreak. A worsening of the COVID-19 outbreak or an infection of Sunpower's employees could cause the group's operations to be disrupted.

Environment, Social, Governance:

For 2018, Sunpower improved both water and electricity intensity. Sunpower saw water intensity decline by 9.2% y-o-y to 1.58t per RMB10,000 of turnover. Electricity intensity also dipped by 12% y-o-y to 81.2kWh per RMB10,000 of turnover.

Company Background

Sunpower Group is a China-focused steam, electricity and heat solutions provider that manufactures energy saving and environment protection products. The group has two main business segments, Green Investments which deals mainly with steam production and distribution and Manufacturing & Services which revolves around petrochemical equipment.



Source: Company, DBS Bank

Sunpower Group Ltd

Segmental Breakdown

FY Dec	2018A	2019A	2020F	2021F	2022F
Revenues (RMBm)					
Manufacturing & services	2,526	2,449	2,852	2,765	2,513
Green investments	737	1,155	1,469	2,189	2,516
Total	3,263	3,605	4,322	4,954	5,029
Operating Profit (RMBm)					
Manufacturing & services	234	265	248	226	184
Green investments	196	326	415	618	711
Total	430	591	663	844	895
Operating Profit Margins					
Manufacturing & services	9.3	10.8	8.7	8.2	7.3
Green investments	26.6	28.2	28.2	28.2	28.2
Total	13.2	16.4	15.3	17.0	17.8

Lower M&S revenue due to lower plant construction activity assumed

Income Statement (RMBm)

FY Dec	2018A	2019A	2020F	2021F	2022F
Revenue	3,263	3,605	4,322	4,954	5,029
Cost of Goods Sold	(2,569)	(2,716)	(3,220)	(3,666)	(3,697)
Gross Profit	694	889	1,102	1,288	1,333
Other Opng (Exp)/Inc	(309)	(329)	(502)	(516)	(511)
Operating Profit	384	559	600	772	822
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	(1.0)	1.20	1.20	1.20	1.20
Net Interest (Exp)/Inc	(55.7)	(106)	(110)	(113)	(158)
Exceptional Gain/(Loss)	67.0	(214)	(154)	(170)	(38.0)
Pre-tax Profit	395	240	337	491	627
Tax	(62.1)	(90.7)	(98.1)	(139)	(146)
Minority Interest	(12.0)	(11.3)	(14.6)	(37.7)	(51.5)
Preference Dividend	0.0	0.0	0.0	0.0	0.0
Net Profit	321	138	224	314	429
Net Profit before Except.	254	352	379	484	467
EBITDA	490	696	762	949	1,008
Growth					
Revenue Gth (%)	66.0	10.5	19.9	14.6	1.5
EBITDA Gth (%)	122.8	41.9	9.6	24.4	6.3
Opg Profit Gth (%)	126.2	45.4	7.3	28.7	6.4
Net Profit Gth (Pre-ex) (%)	117.5	38.9	7.5	27.8	(3.5)
Margins & Ratio					
Gross Margins (%)	21.3	24.7	25.5	26.0	26.5
Opg Profit Margin (%)	11.8	15.5	13.9	15.6	16.3
Net Profit Margin (%)	9.8	3.8	5.2	6.3	8.5
ROAE (%)	22.5	8.3	12.3	15.1	14.9
ROA (%)	5.5	1.9	2.8	3.5	4.5
ROCE (%)	5.5	5.2	4.7	6.0	4.6
Div Payout Ratio (%)	1.4	5.7	5.7	5.7	5.7
Net Interest Cover (x)	6.9	5.3	5.5	6.8	5.2

Estimated finance costs attributed to CB and warrants

Underlying net profit was S\$352.2m, this figure includes differences in foreign exchange and admin expenses caused by CB and warrants

Source: Company, DBS Bank

Sunpower Group Ltd

Quarterly / Interim Income Statement (RMBm)

FY Dec	4Q2018	1Q2019	2Q2019	3Q2019	4Q2019
Revenue	1,280	812	659	778	1,356
Cost of Goods Sold	(993)	(640)	(487)	(580)	(1,008)
Gross Profit	286	171	172	197	348
Other Oper. (Exp)/Inc	(69.7)	(63.6)	(88.7)	(88.5)	(88.6)
Operating Profit	217	108	83.1	109	259
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	0.0	0.0
Associates & JV Inc	(0.2)	0.28	0.35	0.31	0.26
Net Interest (Exp)/Inc	44.5	(42.1)	(56.5)	(57.1)	49.7
Exceptional Gain/(Loss)	68.0	(86.4)	(16.4)	78.8	(190)
Pre-tax Profit	329	(20.4)	10.5	131	119
Tax	(34.8)	(18.3)	(13.1)	(22.0)	(37.3)
Minority Interest	(9.1)	(2.8)	(2.6)	1.57	(7.4)
Net Profit	285	(41.5)	(5.2)	110	74.5
Net profit bef Except.	217	44.8	11.2	31.5	265
EBITDA	249	142	125	144	295

Seasonal rise in revenue q-o-q due to higher heating needs during the cold season

Growth

Revenue Gth (%)	67.5	(36.6)	(18.8)	18.0	74.4
EBITDA Gth (%)	136.7	(43.0)	(12.2)	15.7	104.4
Opg Profit Gth (%)	171.4	(50.2)	(23.0)	30.9	138.5
Net Profit Gth (Pre-ex) (%)	995.7	(79.3)	(75.1)	181.9	740.1

Margins

Gross Margins (%)	22.4	21.1	26.1	25.4	25.7
Opg Profit Margins (%)	16.9	13.3	12.6	14.0	19.1
Net Profit Margins (%)	22.3	(5.1)	(0.8)	14.2	5.5

Balance Sheet (RMBm)

FY Dec	2018A	2019A	2020F	2021F	2022F
Net Fixed Assets	1,155	1,307	1,385	1,481	1,571
Invts in Associates & JVs	9.26	10.5	11.7	12.9	14.1
Other LT Assets	2,476	3,030	3,389	3,579	3,516
Cash & ST Invts	783	863	1,052	1,305	1,727
Inventory	500	559	627	714	720
Debtors	1,192	1,321	1,506	1,727	1,753
Other Current Assets	508	559	559	559	559
Total Assets	6,623	7,650	8,530	9,378	9,861
ST Debt	493	1,010	1,010	1,010	1,010
Creditor	1,717	1,619	1,977	2,251	2,270
Other Current Liab	866	603	598	639	646
LT Debt	1,569	2,194	2,494	2,694	1,797
Other LT Liabilities	148	225	225	225	225
Shareholder's Equity	1,590	1,726	1,938	2,234	3,535
Minority Interests	240	273	288	326	377
Total Cap. & Liab.	6,623	7,650	8,530	9,378	9,861
Non-Cash Wkg. Capital	(383)	217	117	110	116
Net Cash/(Debt)	(1,279)	(2,340)	(2,451)	(2,398)	(1,080)
Debtors Turn (avg days)	137.4	127.2	119.4	119.1	126.3
Creditors Turn (avg days)	229.3	235.9	214.6	221.1	235.0
Inventory Turn (avg days)	62.5	74.9	70.8	70.2	74.6
Asset Turnover (x)	0.6	0.5	0.5	0.6	0.5
Current Ratio (x)	1.0	1.0	1.0	1.1	1.2
Quick Ratio (x)	0.6	0.7	0.7	0.8	0.9
Net Debt/Equity (X)	0.7	1.2	1.1	0.9	0.3
Net Debt/Equity ex MI (X)	0.8	1.4	1.3	1.1	0.3
Capex to Debt (%)	16.2	21.1	17.0	12.5	7.6
Z-Score (X)	NA	NA	NA	NA	NA

Rise attributed to increase in service concession arrangements from new plants

Source: Company, DBS Bank

Sunpower Group Ltd

Cash Flow Statement (RMBm)

FY Dec	2018A	2019A	2020F	2021F	2022F
Pre-Tax Profit	395	240	337	491	627
Dep. & Amort.	107	136	161	175	186
Tax Paid	(45.7)	(88.2)	(70.8)	(98.1)	(139)
Assoc. & JV Inc/(loss)	1.03	(1.2)	(1.2)	(1.2)	(1.2)
Chg in Wkg.Cap.	(175)	(151)	72.2	(33.3)	(13.4)
Other Operating CF	(52.4)	309	0.0	0.0	0.0
Net Operating CF	229	443	499	533	659
Capital Exp.(net)	(333)	(676)	(597)	(462)	(212)
Other Invt.(net)	0.0	0.0	0.0	0.0	0.0
Invt in Assoc. & JV	0.0	0.0	0.0	0.0	0.0
Div from Assoc & JV	0.0	0.0	0.0	0.0	0.0
Other Investing CF	(433)	(570)	0.0	0.0	0.0
Net Investing CF	(767)	(1,246)	(597)	(462)	(212)
Div Paid	(7.8)	(11.8)	(12.9)	(18.0)	(24.6)
Chg in Gross Debt	294	877	300	200	(896)
Capital Issues	0.0	0.0	0.0	0.0	896
Other Financing CF	34.0	(57.5)	0.0	0.0	0.0
Net Financing CF	320	808	287	182	(24.6)
Currency Adjustments	0.12	0.04	0.0	0.0	0.0
Chg in Cash	(217)	5.18	189	253	422
Opg CFPS (S cts)	10.5	15.0	10.7	14.3	16.9
Free CFPS (S cts)	(2.7)	(5.9)	(2.5)	1.79	11.2

Source: Company, DBS Bank

Target Price & Ratings History



Note: Share price and Target price are adjusted for corporate actions.

S.No.	Date of Report	Closing Price	12-mth Target Price	Rating
1:	16 Dec 19	0.61	0.81	BUY
2:	02 Mar 20	0.53	0.84	BUY

Source: DBS Bank

Analyst: Singapore Research Team

Lee Keng LING

DBS Bank recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return, i.e., > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable share price catalysts within this time frame)

*Share price appreciation + dividends

Completed Date: 2 Mar 2020 19:14:08 (SGT)

Dissemination Date: 2 Mar 2020 19:38:45 (SGT)

Sources for all charts and tables are DBS Bank unless otherwise specified.

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