



# Sunpower Group

(SPWG SP/SUNP.SI)

## New chapter unfolding

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- 1Q21 revenue grew by 31% YoY and PATMI rose by 17% YoY, in line with our expectations mainly due to the contribution from Shantou Phase 1 project.
- Sunpower's valuation will be wholly derived from GI projects moving forward as the company continues its transformation to pursue sustainability.
- We maintain an **OUTPERFORM** rating with an upgraded target price of \$\$1.53 (ex-dividend \$\$1.29) based on individual project's discounted cash flows and the special dividend declared of RMB1.1627 (equivalent of S\$0.2359) per share.

Financials & Key Operating Statistics					
YE Dec (RMB m)	FY17	FY18	FY19	FY20	FY21F
Revenue	1,965	3,263	3,605	4,059	4,540
Gross Profit	408	694	889	981	1,201
PATMI	117	254	352	377	480
Basic EPS	16	34	45	48	61
Fully Diluted EPS	9	19	27	33	42
Basic EPS grth (%)	-18%	117%	31%	6%	27%
Basic P/E (x)	29.9	13.8	10.5	9.9	7.8
Fully diluted P/E (x)	52.5	24.9	17.8	14.4	11.3
Basic P/B (x)	3.0	2.5	2.0	1.7	1.4
Fully Diluted P/B (x)	5.1	4.2	3.4	2.8	2.4
Gross Margin (%)	21%	21%	25%	24%	26%
Net Margin (%)	6%	8%	10%	9%	11%
Net Gearing (%)	8%	36%	80%	81%	88%
Interest Coverage (x)	5.4	6.3	5.1	5.7	5.7
ROE (%)	10%	17%	19%	17%	18%

Financials and ratios are not reflective of M&S divestment

Source: Company Data, KGI Research

**1Q21 performance review.** It was a good start for Sunpower in FY21. The improvement in profitability was mainly due to the contribution of Shantou Phase 1 project which commenced in 4Q20. The overall performance met our expectation as China's economic recovery continues. During the period, developing countries in South and Southeast Asia still suffered from rising COVID infections. China's export of goods and services surged as it was one of the few countries which maintained normalised production activities. We believe tailwinds will continue at least until 3Q21.

Figure 1: Key financial highlights

(RMB mn)	1Q21	1Q20	YoY change
<b>Revenue</b>	<b>882.8</b>	<b>672.7</b>	<b>31%</b>
M&S revenue	465.2	413.5	13%
GI revenue	417.6	259.1	61%
<b>Gross profit</b>	<b>187.4</b>	<b>154.4</b>	<b>21%</b>
EBITDA	168.9	131.3	29%
<b>PATMI</b>	<b>59.7</b>	<b>51.1</b>	<b>17%</b>

Source: Company

### Outperform - Maintain

Price as of 28 May 21 (SGD)	0.95	<b>Performance (Absolute)</b>	
12M TP (\$) (cum-dividend)	1.53	1 Month (%)	2.7%
Previous TP (\$)	1.45	3 Month (%)	18.1%
Upside (%)	61.9	12 Month (%)	113.6%
<b>Trading data</b>		<b>Perf. vs STI Index (Red)</b>	
Mkt Cap (\$mn)	750		
Issued Shares (mn)	792		
Vol - 3M Daily avg (mn)	3.4		
Val - 3M Daily avg (\$mn)	3.0		
Free Float (%)	39.3%		
<b>Major Shareholders</b>		<b>Previous Recommendations</b>	
Guo Hongxin	19.4%	14-Aug-20	OP \$0.91
Ma Ming	17.4%	17-Nov-20	OP \$0.91
Lin Yucheng	12.6%	12-Jan-21	OP \$1.45

Figure 2: Project updates as of 1Q21

Project	Designed capacity of steam (no. of boilers * tonnes/hour)	Designed capacity of power (no. of generators * MW/hour)
<b>In operation</b>		
Changrun	2*220	2*25
Yongxing	2*100 + 1*150	2*18
Xinyuan	3*75 + 1*220	2*6 + 1*25
Suyuan	1*90 + 2*75	1*7
Lianshui	2*40	NA
Qianjiao	1*40	NA
Xintai Zhengda (old)	NA	NA
Jining	NA	NA
Shantou P1	3*150	2*20
<b>Under construction</b>		
Tongshan P1	1*130	1*35
Shanxi Xinjiang	1*130	1*15
Xintai Zhengda (new)	3*130	1*35 + 1*18
Shantou P2	2*260	2*30
Changrun Project - Connection to Sanli	NA	NA

Source: Company

**Valuation & Action:** We maintain an OUTPERFORM rating with an upgraded target price of \$\$1.53 (ex-dividend \$\$1.29) based on each project's discounted cash flows and the special dividend declared of S\$0.2359 per share.

**Risks:** The surge in coal prices could lead to a short-term margin compression. Although Sunpower can pass the mark-up in costs to customers in the long run, the performance volatility will increase for certain months. Meanwhile, rising interest rates and financing costs due to inflation expectation could lower project rate of returns.

**Road to transformation.** The good news for both the company and shareholders this year was the restructuring of the business by divesting the manufacturing and services segment (refer to our previous [report](#) for detailed analysis).

At this juncture, shareholders should see the bigger picture of the company as it undergoes its transformation process. Before 2014, the company's main business was equipment manufacturing, engineering, procurement, and construction, which was integrated in M&S in 2018. In 2015, the group stepped into green investment (GI) which engaged in utilities projects. Over the past 5 years, revenue contribution from GI has been increasing, and as of FY20, GI revenue accounted for 32.9% of total revenue (FY16: Nil, FY17: 7.7%). As a result, Sunpower had two engines of growth to drive the overall business.

To understand why management decided to switch back to one (better) engine business model, investors need to understand the core features of and differences between the two. M&S is an order book-driven business. Although the segment secured a record high order book of RMB2.8bn before the divestment was announced, it suffered from low growth during 2014 and 2015 when oil market crashed. During the years of oil recovery, the segment consistently secured large-size contracts. Hence, the segment performance is cyclical in line with market capital expenditure conditions due to its heavy exposure to the petrochemical sector.

However, the era of clean energy has come, squeezing the growth of the petrochemical industry as talent and capital will gradually shift out. In terms of profitability, M&S is not comparable to high-end manufacturing like semiconductor, precise engineering, and robotics. The net margin of M&S is mid- to high-single digit.

On the other hand, GI provides better growth and visibility. The projects under GI own quality assets, with the average internal rate of return of more than 15%, and payback period of around eight years (concession period: 30 years). More importantly, these assets are profit-making and generating consistent positive operating cash flows. Not only does GI have organic growth by expanding and upgrading of existing plants owing to the increase in demand from new customers, but it also has inorganic growth by acquiring new projects. Instead of exposure to a single sector, GI serves multiple sector clients in the industrial park. Diversity buffers cyclical impact. Meanwhile, GI's net profit margin is more than 10%.

**Moat guarantees sustainability.** GI has an economic moat as policies promote a centralised boiler where the supply of heat and steam are integrated into a single provider. This helps to sustain supply and demand dynamics on a regional level. It is along this lines that the transformation of Sunpower over the last 5 years is on the path to sustainability and stability.

**GI valuation.** Investors should understand GI's value is the overall group's value after the divestment of M&S is completed. We upgrade our ex-dividend TP to S\$1.29 from the previous S\$1.22 as some plants' utilization rates are expected to increase due to accelerating economic recovery in 2H21.

Figure 4: Pro forma income statement of GI segment ONLY

Y/E Dec (RMB mn)	FY21F	FY22F
<b>Revenue</b>	<b>1741.2</b>	<b>2209.6</b>
Cost of sales and servicing	(1,265.5)	(1,599.1)
<b>Gross revenue</b>	<b>475.7</b>	<b>610.5</b>
Operating income	398.9	524.1
Profit for the period	258.1	350.5
Profit attributable to:		
<b>Owners of the Company</b>	<b>240.7</b>	<b>326.7</b>
Non-controlling interests	17.5	23.7

Source: KGI Research

Figure 3: Updated GI segment valuation

	GI											
	Changrun (Phase 1)	Xinyuan	Lianshui	Quanjiao	Yongxing	Suyan	Xintai Zhengda (New facility)	Shantou (Phase 1)	Shantou (Phase 2)	Tongshan	Shanxi Xinjiang	
<b>FCF p.a.</b>												
Year 1	83	133	6	9	103	51	78	102	124	56	66	
Year 2	80	132	6	9	101	50	75	101	123	55	65	
Year 3	77	131	6	9	98	49	73	99	122	53	64	
Year 4	74	130	5	8	95	48	71	98	120	51	63	
Year 5	71	129	5	8	92	47	68	96	119	49	62	
Year 6	68	129	4	8	89	46	65	94	118	47	60	
Year 7	64	128	4	8	85	44	62	92	116	45	59	
Year 8	60	2413	4	8	2,441	1,131	59	90	115	43	1399	
Year 9 to the end of the concession	135	-	12	12	-	-	118	128	144	87	-	
<b>NPV</b>	445	1,825	16	55	2,338	1,142	340	671	973	287	573	
Ownership	100%	85%	95%	100%	100%	90%	87%	51%	51%	100%	100%	
NPV owned by Sunpower	445	1551	15	55	2,338	1027	294	342	496	287	573	
Capital structure	Debt: 60%, Equity: 40%											
Cost of equity	9.0%											
Cost of debt	5.5%											
Tax rate	16.0%											
WACC	6.4%											
Total NPV	7,424											
Total number of shares if fully diluted	1,152											
TP (RMB)	6.44											
FX	5.00											
<b>TP (SGD)</b>	<b>1.29</b>											

Source: KGI Research

YE 31 Dec

INCOME STATEMENT (RMB m)	FY17	FY18	FY19	FY20	*FY21F
<b>Revenue</b>	<b>1,965</b>	<b>3,263</b>	<b>3,605</b>	<b>4,059</b>	<b>4,540</b>
Cost of sales	-1,558	-2,569	-2,716	-3,077	-3,339
<b>Gross Profit</b>	<b>408</b>	<b>694</b>	<b>889</b>	<b>981</b>	<b>1,201</b>
Other operating income/(expenses)	47	38	-2	-17	36
SG&A	-242	-329	-323	-341	-459
Othes	-31	-12	-0	-1	0
<b>Profit from Operations</b>	<b>182</b>	<b>391</b>	<b>563</b>	<b>623</b>	<b>779</b>
Finance income/(expenses)	-34	-62	-110	-109	-136
Share of JV results	0	-1	1	2	0
<b>Profit before Tax</b>	<b>149</b>	<b>328</b>	<b>454</b>	<b>516</b>	<b>643</b>
Income tax	-27	-62	-91	-112	-129
Non-controlling interests	5	12	11	27	35
<b>PATMI</b>	<b>117</b>	<b>254</b>	<b>352</b>	<b>377</b>	<b>480</b>

BALANCE SHEET (RMB m)	FY17	FY18	FY19	FY20	*FY21F
Cash and cash equivalents	903	685	690	534	424
Pledged deposit	88	112	107	209	144
Trade and other receivables	1,264	1,289	1,352	1,452	1,510
Inventory	343	500	545	541	574
Others	368	396	540	627	871
<b>Current Assets</b>	<b>2,966</b>	<b>2,982</b>	<b>3,234</b>	<b>3,363</b>	<b>3,523</b>
Property, plant and equipment	474	870	1,013	999	1,341
Intangible assets	1,284	2,074	2,527	3,007	3,334
Others	276	697	846	915	947
<b>Non-current Assets</b>	<b>2,034</b>	<b>3,641</b>	<b>4,386</b>	<b>4,922</b>	<b>5,621</b>
<b>Total assets</b>	<b>5,000</b>	<b>6,623</b>	<b>7,620</b>	<b>8,285</b>	<b>9,145</b>
Trade and other payables	1,740	2,499	2,094	2,131	2,169
Borrowings (current)	517	493	1,010	766	1,277
Others	33	73	85	49	49
<b>Current Liabilities</b>	<b>2,291</b>	<b>3,065</b>	<b>3,188</b>	<b>2,946</b>	<b>3,495</b>
Borrowings (non-current)	568	839	1,272	1,783	1,609
Convertible bonds	732	837	817	794	753
Others	36	148	221	222	219
<b>Non-current liabilities</b>	<b>1,336</b>	<b>1,824</b>	<b>2,310</b>	<b>2,800</b>	<b>2,581</b>
<b>Total liabilities</b>	<b>3,626</b>	<b>4,889</b>	<b>5,499</b>	<b>5,746</b>	<b>6,076</b>
Shareholders equity	1,224	1,494	1,851	2,222	2,621
Non-controlling interests	150	240	273	313	448
<b>Total Equity</b>	<b>1,374</b>	<b>1,734</b>	<b>2,125</b>	<b>2,535</b>	<b>3,069</b>
<b>Total Liabilities and Equity</b>	<b>5,000</b>	<b>6,623</b>	<b>7,623</b>	<b>8,281</b>	<b>9,145</b>

CASH FLOW STATEMENT (RMB m)	FY17	FY18	FY19	FY20	*FY21F
Net income before tax	178	395	454	516	643
Depreciation & non cash adjustments	50	106	145	174	225
Others	-19	0	152	143	179
Change in Working Capital	-80	-174	-168	-123	-207
Income Tax Paid	-22	-47	-83	-129	-129
Interest Paid	-21	-51	-65	-68	-127
<b>CF from operating activities</b>	<b>86</b>	<b>229</b>	<b>434</b>	<b>513</b>	<b>585</b>
Purchase/Disposal of PPE	-52	-71	-105	-79	-100
Purchase/Disposal of intangible assets	-522	-228	-519	-434	-300
Others	-119	-467	-620	-268	-695
<b>CF from investing activities</b>	<b>-693</b>	<b>-767</b>	<b>-1,244</b>	<b>-781</b>	<b>-1,095</b>
Dividends Paid	-8	-8	-12	-15	-2
Debt Raised / (Repaid)	461	171	877	264	337
Equity Raised / (Bought Back)	0	16	12	0	0
Issuance of convertible bonds	732	123	0	0	0
Others	43	18	-55	-80	64
<b>CF from financing activities</b>	<b>1,228</b>	<b>320</b>	<b>823</b>	<b>169</b>	<b>400</b>
Net increase in cash & cash equiv.	621	-217	14	-99	-111
FX effects	-0	0	0	-0	0
Beginning Cash	281	903	685	690	534
<b>Ending Cash</b>	<b>903</b>	<b>685</b>	<b>699</b>	<b>591</b>	<b>424</b>

KEY RATIOS	FY17	FY18	FY19	FY20	*FY21F
<b>Profitability</b>					
Basic EPS (RMB Cents)	16	34	45	48	61
Fullu diluted EPS (RMB Cents)	9	19	27	33	42
Basic EPS Growth (%)	-18%	117%	31%	6%	27%
DPS (SGD Cents)	0.12	0.19	0.25	0.30	0.19
Dividend Yield (%)	0.2%	0.3%	0.5%	0.5%	0.3%
<b>Profitability</b>					
Gross margin	21%	21%	25%	24%	26%
EBITDA margin	12%	15%	20%	20%	22%
Net margin	6%	8%	10%	9%	11%
ROE	10%	17%	19%	17%	18%
ROA	2%	4%	5%	5%	5%
<b>Financial Structure (x)</b>					
Interest coverage	5.4	6.3	5.1	5.7	5.7
Total Debt/Equity	0.9	0.9	1.2	1.1	1.1
Net Gearing	0.1	0.4	0.8	0.8	0.9

\*FY21 forecasts do not factor in the divestment of M&S segment, and all the estimates are subject to revision when the full financial details are disclosed.

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<b>Outperform (OP)</b>	We take a positive view on the stock. The stock is expected to outperform the expected total return of the KGI coverage universe in the related market over a 12-month investment horizon.
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