

Housing and construction sectors

Q4 preview: Our order of preference is homebuilders, followed by housing equipment and then construction

■ Industry Overview

Shusuke Terada

+81-3-6270-4815

shusuke.terada@citi.com

- **Conclusion** — Faced with a challenging demand environment, homebuilding and housing equipment companies have strengthened their earnings bases by growing non-homebuilding and overseas businesses and cutting costs. With the exception of Toto, we expect these companies to guide for record-high profits in FY3/14 on sustained growth in the domestic new build market. In particular, we think that for homebuilders able to maintain prices due to introduction of more sophisticated products, the impact of higher raw materials via yen weakness will be limited. Meanwhile, we think guidance at construction companies could come in below market expectations, which could in turn trigger a downward correction to lofty valuations. In order of preference, we rank the homebuilding companies ahead of housing equipment companies, followed by construction companies.
- **Positives** — With its unit construction method helping limit the impact of higher labor costs, we expect Sekisui Chemical to forecast a larger rise in mainstay housing segment margins than at peers and issue FY3/14 guidance above market expectations. With low margins on completed construction squeezing earnings, we think any recovery at Haseko is likely to be muted, but the announcement of a redemption of preferred shares could prove a positive catalyst.
- **Negatives** — We expect FY3/13 OP at Lixil to miss guidance on yen weakness and low interest rates. Market participants are likely to take a dim view of any continuation of the earnings shortfalls that began in FY3/12. Also, we believe general contractors will issue low building project margin forecasts for FY3/14. We think bullish order projections are also unlikely, given the lack of clarity on FY3/13 supplementary budget-related orders.

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Figure 1. Housing and Construction sector: Results preview

Code	Company name	Results announced	Investment rating	Share price (April 3 close) (¥)	Share price performance			FY12 OP (¥bn)	
					One-month	Three-month	Six-month	CE	Citi E
1801	Taisei	05/13	3	253	-8.7%	-11.5%	11.9%	41.0	41.4
1802	Obayashi	05/14	2	463	-3.9%	-4.3%	30.1%	34.0	34.8
1803	Shimizu	05/14	3	302	2.0%	-6.5%	15.7%	14.5	12.5
1808	Haseko	05/09	2	90	2.3%	32.4%	80.0%	24.0	24.6
1812	Kajima	05/14	2	253	-7.7%	-10.9%	17.1%	15.0	15.2
1878	Daito Trust	04/30	1	7,530	-11.9%	-7.6%	-4.0%	84.0	84.0
1925	Daiwa House	05/10	2	1,788	3.5%	20.9%	57.7%	125.0	126.9
4204	Sekisui Chemical	04/26	1	1,010	10.1%	34.8%	67.5%	62.0	61.5
5332	TOTO	04/26	2	793	-5.1%	22.8%	41.1%	23.0	23.0
5938	LIXIL Group	05/07	1	1,755	-8.5%	-8.5%	-3.7%	54.0	46.0
5947	Rinnai	05/10	1	6,360	-5.4%	8.7%	14.4%	28.0	27.5

Code	Company name	Citi E	Average	FY13 OP (¥bn)		Guidance forecast	Surprise possibility	FY12 PER Citi E (x)	FY13 PER Citi E (x)
				Consensus	Upper limit				
1801	Taisei	41.8	43.9	49.0	36.2	42.0	↓	17.6	15.7
1802	Obayashi	35.3	36.8	42.0	28.6	35.0	↓	27.5	15.2
1803	Shimizu	17.1	17.1	22.0	10.2	17.0	↓	38.8	21.0
1808	Haseko	27.3	26.8	27.0	26.5	27.0	↑	11.7	10.3
1812	Kajima	29.4	28.9	34.0	25.0	28.0	--	13.8	16.8
1878	Daito Trust	92.0	91.2	95.9	87.0	92.0	--	11.9	10.9
1925	Daiwa House	137.0	137.5	145.0	127.0	140.0	--	16.4	14.2
4204	Sekisui Chemical	75.1	72.7	78.0	68.7	75.0	↑	18.1	12.5
5332	TOTO	27.2	26.4	28.0	24.4	27.0	--	17.0	15.5
5938	LIXIL Group	76.1	71.3	74.0	68.6	70.0	↓	30.7	11.9
5947	Rinnai	32.4	30.3	32.4	29.0	30.0	↓	16.5	14.1

Code	Company name	Comment
1801	Taisei	Even with profit growth at subsidiaries like Taisei-Yuraku, we think parent construction revenue and margins will decline in FY3/14, so little growth is likely for consolidated OP.
1802	Obayashi	In FY3/13 we think an undershoot for parent OP will be offset by a subsidiary overshoot. In FY3/14 we model a small OP increase as profit growth at development-related subs exceeds the decline in parent profits.
1803	Shimizu	We think FY3/13 OP will fall below plan on a lower-than-expected building profit margin. Little recovery is likely at either the parent or subsidiaries in FY3/14.
1808	Haseko	Earnings recovery is likely to be muted due to a low margin on completed construction, but the announcement of preferred share redemption could be a positive catalyst.
1812	Kajima	We look for the OP in the construction segment to rise sharply in FY3/14 as losses on the Algeria East-West Highway drop out and real estate earnings increase.
1878	Daito Trust	FY3/13 OP could fall below plan on a labor shortage in construction, but we think FY3/14 forecasts will be the same as current medium-term plan targets.
1925	Daiwa House	We think rental housing will remain strong in FY3/14. The commercial facility and business facility segments could contribute little to profit growth due to higher labor costs. Fujita profitability is unclear.
4204	Sekisui Chemical	We look for a small undershoot in UIEP in FY3/13 but for FY3/14 we think RoE will rise above 10% for the first time in 23 years driven by the housing segment.
5332	TOTO	Overseas earnings should increase in FY3/14 on yen weakness, and this, plus domestic cost cutting, should mean another large profit increase. However, China ops are weak, excluding the forex impact.
5938	LIXIL Group	OP looks set to undershoot in FY3/13 on yen weakness and low interest rates. We think the sales targets in the upcoming medium-term plan (including FY3/14) could be somewhat optimistic.
5947	Rinnai	OP could undershoot in FY3/13 on domestic inspection costs. We think FY3/14 guidance will be conservative, as usual, which could impact the shares short term.

Note: An arrow pointing up suggests the possibility of a positive surprise, while an arrow pointing down suggests the possibility of a negative surprise.

Source: Company data, IFIS, Citi Research.

Appendix A-1

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