01 March 2018

BUY
TP: PHP 1.40
▲ 40.0%

Sta. Lucia Land, Inc.

SLI.PH

Unleashing Balance Sheet Potential

Sta. Lucia Land (SLI) is one of the largest horizontal property developers in the Philippines with over 90 ongoing projects nationwide. SLI is embarking on a capex-driven expansion (~PHP11bn) over the next 4 years, which could add PHP18bn value uplift into current portfolio. We forecast a 23% EPS CAGR from FY18-20E; initiate coverage with a TP PHP 1.40/share, BUY.

- **A seasoned property developer with a 45 year track record:** Sta. Lucia Group, represented by SLI, has two principal businesses: 1) Horizontal & Vertical property developments (57% of revenue); and 2) Commercial/Retail Leasing (29%). SLI core expertise is in Horizontal land developments, which command ~20% higher margins than Vertical ones. SLI was incorporated via a back-door listing on the PSE in 2007.
- **Philippines property tailwind:** 1) Rising disposal income, and the 2) Young and growing population, is driving the fundamental and aspirational demand for quality housing for average Filipinos. Land prices in Metro Manila have risen by 9.6% CAGR for 2015-17 and we expect continued growth of 11% pa in 2018-19E.
- **Capex-driven expansion:** SLI is embarking on a capex-driven expansion approach by acquiring land banks that surround Metro Manilla and cradle ongoing PHP9.0tn worth of government infrastructural development. It plans to spend ~PHP11bn of capex over next 4 years, which could add PHP18bn value uplift to SLI's current portfolio. We project SLI to utilize both debt and equity funding to achieve this objective, while maintaining gearing below 1.0x.
- **Initiating coverage with BUY:** SLI is attractively valued at 0.7x P/B vis-à-vis average Phils Developers of 1.7x. In addition, we project EPS to grow by a robust 23% CAGR from FY18-21E. SLI currently trades at a 50% discount to our estimated end-2018 RNAV, applying a discount rate of 7.3%.

Financial highlights

Y/E 31 Dec (PHP M)	FY17E	FY18E	FY19E	FY20E	FY21E
Revenue	3,316	4,997	6,200	7,604	8,413
Net profit	835	1,030	1,445	1,860	2,226
Outstanding shares (M)	8,946	8,946	10,796	10,796	10,796
EPS (PHP)	0.093	0.115	0.134	0.172	0.206
EPS growth (%)	14.3%	23.4%	16.2%	28.8%	19.7%
NPM (%)	25.2%	20.6%	23.3%	24.5%	26.5%
ROE (%)	5.4%	5.8%	6.7%	7.4%	8.8%
BV per share	1.60	1.70	1.78	1.93	2.10
P/B (x)	0.65	0.61	0.58	0.53	0.49

Source: Company, SCCM Research; Prices as of closing 28 Feb 2018

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PRICE CLOSE (01 Mar 2018)
PHP1.00

MARKET CAP
PHP 8.9 Bln
USD 0.2 Bln

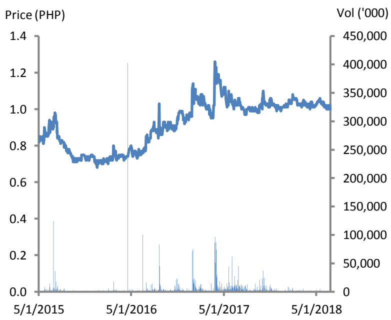
SHARES O/S
8,946 mln

FREE FLOAT
17%

3M AVG DAILY VOLUME/VALUE
PHP 0.697 mln / USD 0.01 mln

52 WK HIGH	52 WK LOW
PHP1.23	PHP0.96

Target Price PHP1.40



Sta. Lucia Land, Inc.

SLI.PH

Investment Thesis

Catalysts

- **Unlocking balance sheet potential:** As compared to its peers, SLI's balance sheet is under-levered at 0.7x vs. the industry average of 0.8x. Even so, SLI is able to deliver consistently strong 50% gross margins and ~35% EPS growth from FY14-17. The company plans to spend PHP10.8bn over the next 4 years to acquire and develop land banks surrounding Metro Manilla. We project SLI to utilize both debt and equity funding to achieve this objective, while maintaining gearing below 1.0x.

Under-levered balance sheet; SLI looks to spend ~PHP11bn over the next 5 years to drive EPS growth

- **Strategic location enhances current project portfolio value:** With PHP9.0tn of government infrastructure rollout (highways and public transportations systems) over the next 5 years cradling SLI's land parcels, we expect a 20% value premium over SLI's current property valuation, which we have not priced-in into our model.

- **Focused on Profitability:** SLI specializes on horizontal land development which has traditionally commanded a 20 percentage points higher margin than vertical development (Gross Margins on horizontal and vertical developments are roughly 65% and 45%, respectively) due to lower overhead and higher turnover value. Horizontal development represents 75.3% of real estate sales and we expect this to grow to 84.3% in FY20E.

Land is still an abundant commodity in the Philippines. We expect SLI's business model to remain sustainable in the long-run

- **Visible bottom-line growth over the next 3 years:** SLI's capex-driven expansion strategy has been in the works for the past 4 years. By taking on a larger quantum of order books in key growth-centric cities, we expect top-line revenue and EPS to grow by 32% and 23% CAGR, respectively, from FY18-21E. SLI currently trades at 0.7x P/B vs. the industry average of 1.7x.

- **Understated asset values:** SLI has conservatively kept its investment properties and strategic land bank at book value. We estimate that the company currently trades at 50% discount to its end-2018 RNAV based on our conservative model. Note that we have yet to price-in the potential value uplift of projects proximate to ongoing government infrastructure (20% potential uplift) and its investment properties (50% value uplift).

Taking its flagship Sta Lucia Mall as an example, its stated book value is PHP5.1bn vs estimated appraised value of PHP7.9bn.

Risks

- **Regulatory risk:** Surrounding government projects is a double-edged sword. While beneficial in the long term, delays and conflicts of interest may impair the development trajectory that SLI has so carefully planned-out.

- **Execution risk:** As with any property developers, SLI is vulnerable to project delays and or delays in collection of accounts receivables, which may adversely afflict the reputation and liquidity of the company's operations.

- **Collection risk:** Given that SLI also acts as a mortgage lender to majority of its clientele that rely on remittance. Currently, loan defaults are still less than 5%. But the figure could increase as the company takes on more projects and clients, or if screening becomes more lax to push the sales of its units

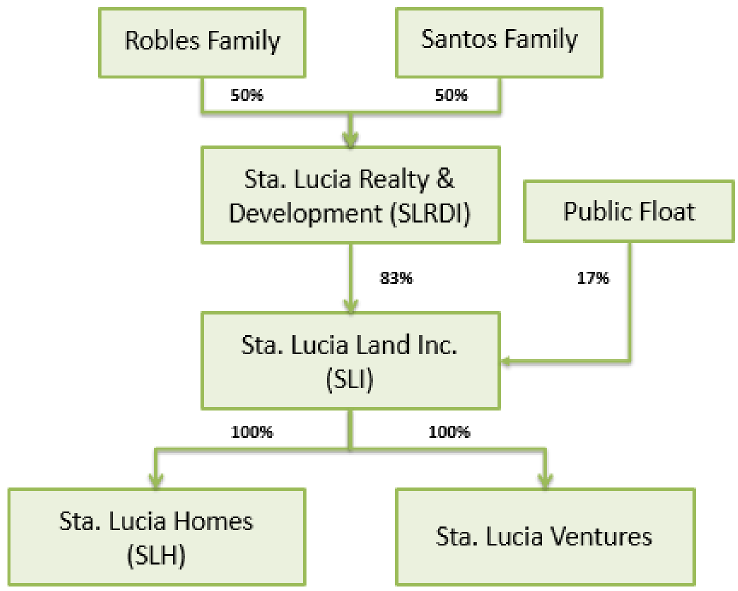
- **Market risk:** SLI is vulnerable to the changes in the global economy given that OFW remittances significantly contribute to the disposable income of ordinary Filipinos. Additionally, Philippines could be vulnerable to another round of political upheaval should incumbent President Duterte lose power in the near term.

Sta. Lucia Group Profile

Group Structure & History

- Sta. Lucia Land (SLI) is 83% owned by Sta. Lucia Realty and Development (SLRDI), which is equally owned by the Robles and Santos family. Over the last 45 years, the group has developed 220 projects covering over 10,100 hectares and 14 golf courses all over Philippines.

Fig 1 - SLI's current shareholding structure



Source: Company

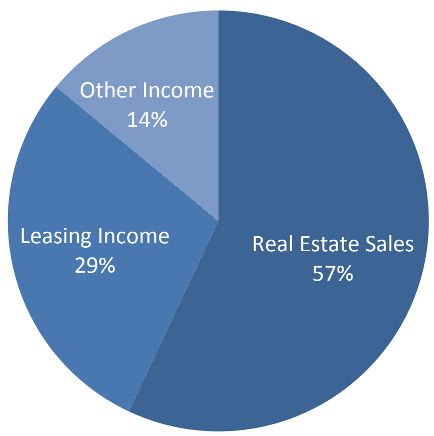
- In 2008, SLRDI was contemplating to go public. Instead, SLRDI acquired a listed company called Zipporah Mining and changed the name to Sta. Lucia Land (SLI). Post-listing, SLRDI swapped over ~PHP10bn worth of assets with ~PHP10bn worth of shares issued by SLI, making SLRDI the majority shareholder of SLI. The amount of debt transferred was approximately PHP300m.
- Since 2008, SLI became the flagship company of the group and all projects are now being undertaken at the SLI level.
- Historically, the Robles & Santos Family tends to be more cautious when expanding the business. While this has allowed SLI to maintain a fairly under-levered balance sheet and maintain relatively low business risk, it has kept a ceiling to SLI's growth.
- In the advent of improving macro conditions and stronger demographic support, the two families brought their new EVP/CFO David Dela Cruz on board 5 years ago to facilitate the transition towards a more aggressive expansion model while still ensuring certain degree of prudence in gearing.

Company Overview (Sta. Lucia Land)

Bulk of SLI's revenue came from selling developed land lots

- SLI's main business comes from sale of developed land lots. In addition, SLI owns a portfolio of retail properties and Condotels, which contribute as recurring income. SLI is currently developing over 40 projects nationwide with gross development value (GDV) of over PHP24.2bn.
- Revenue contribution is broken down as follows: Real Estate Sales (57%), Leasing Income (29%) and Other Income, including Interest Income (14%) based on 3Q17.

Fig 2 - Revenue Contribution (3Q17)



Source: Company

Overseas Foreign Workers (OFWs) represent 10% of the population and their remittance contributes ~10% of the country's GDP.

- SLI mainly operates in South Luzon region and most of its projects are located outside of Metro Manila. The company taps on OFW's desire to build a house in their home provinces. SLI mainly targets the price segment between PHP1.5- 5.0m, which is the largest housing market segment in the Philippines (29% market share).
- SLI's revenue is largely derived from land lot sales with Philippines' increasingly affluent middle class as its key demographic. The middle class is mainly made-up of OFWs & their families (70%), SME owners (15%), and Middle Class Employees (15%). 95% of SLI's operating revenue is generated domestically.
- They have a 120,000 strong local and international sales force. Out of the 7 major marketing companies, 5 of them work exclusively with SLI.

Fig 3 - SLI's relationship with the 7 major real estate agents in Philippines

Source: Company

Business Overview

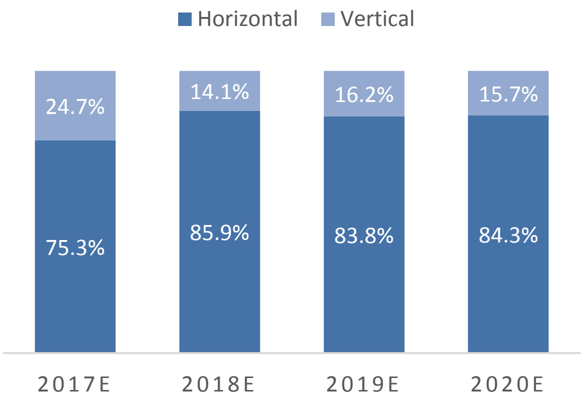
Horizontal Development – Low Overhead, Shared Risk, High Margin

- Their main business follows an Asset-Light Business model wherein the company acquires the land by entering Joint Venture (JV) with landowners to develop the land and sell the land plot.

Philippines still has abundant land bank in areas surrounding Metro Manilla that are under-developed

- **Two-phase approach:** Phase 1) "Lots-Only" enables the buyers to have the opportunity to build their own house at their own desired pace, size and location without having to bear a large financial obligation. Phase 2) SLI's fully owned house construction subsidiary Sta. Lucia Homes will offer Sta. Lucia Lot owners a competitive package for the construction of their house. With relationship previous built with the lot owners, agents are able to better market the construction package. SL Homes undertake the construction on a turn-key basis and offer services such as securing permits and construction financing.

Fig 4 - Real Estate Sales Segment Breakdown Projection



Source: Company, SCCM Research

- Most of their direct clients are relatives/spouses of OFWs who do not file an income tax return and are hence not eligible for a bank loan. As such, SLI extends the necessary financing at a 14% interest rate, which contributes to Other Income.

It is a common practice for developers to offer direct financing at prevailing interest rates range 14-16%

- The JV model allows SLI to reduce upfront capex and share the risk with landowners. Sale price of the developed lots typically ranges 5-6x the development and land acquisition cost combined. As such, horizontal projects are typically 1.5x more profitable than vertical projects.

Fig 5 - Illustration of difference between Horizontal & Vertical Projects

(per sqm)	Horizontal Projects	Vertical Projects
Land Acquisition Costs	P 500-1000	P 1,000-10,000
Raw Materials/ Labour Costs	P 800-1000	P 25,000-35,000
Selling Price	P 5,000-10,000	P 65,000-100,000
Administrative & Marketing Costs	15% of Selling Price	15% of Selling Price
Margins	~65%	~45%

Source: Company, SCCM Research

Vertical Development – Strategic Location, Better Uptake

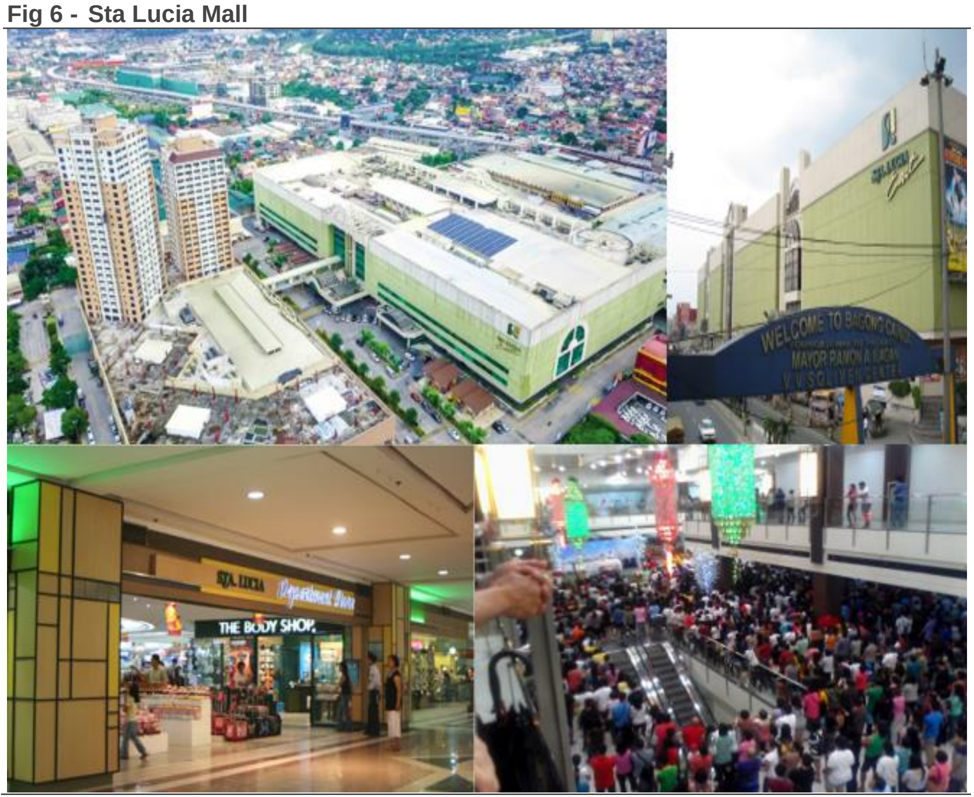
- Condominiums target a younger segment of the middle class. Younger Filipinos tend to seek out housing options that are closer to city centers and amenities.
- As condominiums are more capital intensive, SLI is extremely selective of the location and typically only greenlights projects where there is high certainty of demand. Vertical developments tend to command a lower margin than horizontal ones due to higher overhead and marketing costs.
- Condotel concept is condominium units being sold to buyers but are managed as hotels. Experienced hotel managers and staff will operate and manage the condotel and take care of maintenance. Unit owners get 30 complimentary room nights per year, transferrable across all Sta. Lucia Group affiliated hotels and condotels in the Philippines. Condotel units will be placed under the management's hassle-free rental program for an initial period of 15 years.

Condotels are popular with foreign buyers as a vacation home/ mini investment option given SLI's commitment to choose locations that are close to popular tourists' destinations

Investment Properties – Stable Recurring Income

- SLI owns Sta. Lucia East Grand Mall ("SL Mall") which serves nearby cities of Marikina, Antipolo, Pasig and the neighboring Rizal province. The mall currently has 115,492sqm of leasable space; of which 95.4% is leased by 453 tenants.
- Additionally, SLI has completed a two-storey wing with GFA of 40,000sqm and GLA of 12,600sqm. It provides 20,000sqm of parking for residential and retail clients.
- Sta. Lucia Mall acts as an one-stop destination for family and groups of friends. It has amenities from clinics, clothing stores, gyms, playgrounds and food outlets.

Fig 6 - Sta Lucia Mall



Source: Company

- SLI is currently constructing the Sta. Lucia Business Center in Pasig City, which is slated to be a 6-storeys BPO/Office and Retail Building. It is connected to LRT 2 expansion and SL Mall. We expect this development to add PHP100-120m per annum to the top line in earliest 2019.

Fig 7 - Business Center (U/C)

Source: Company

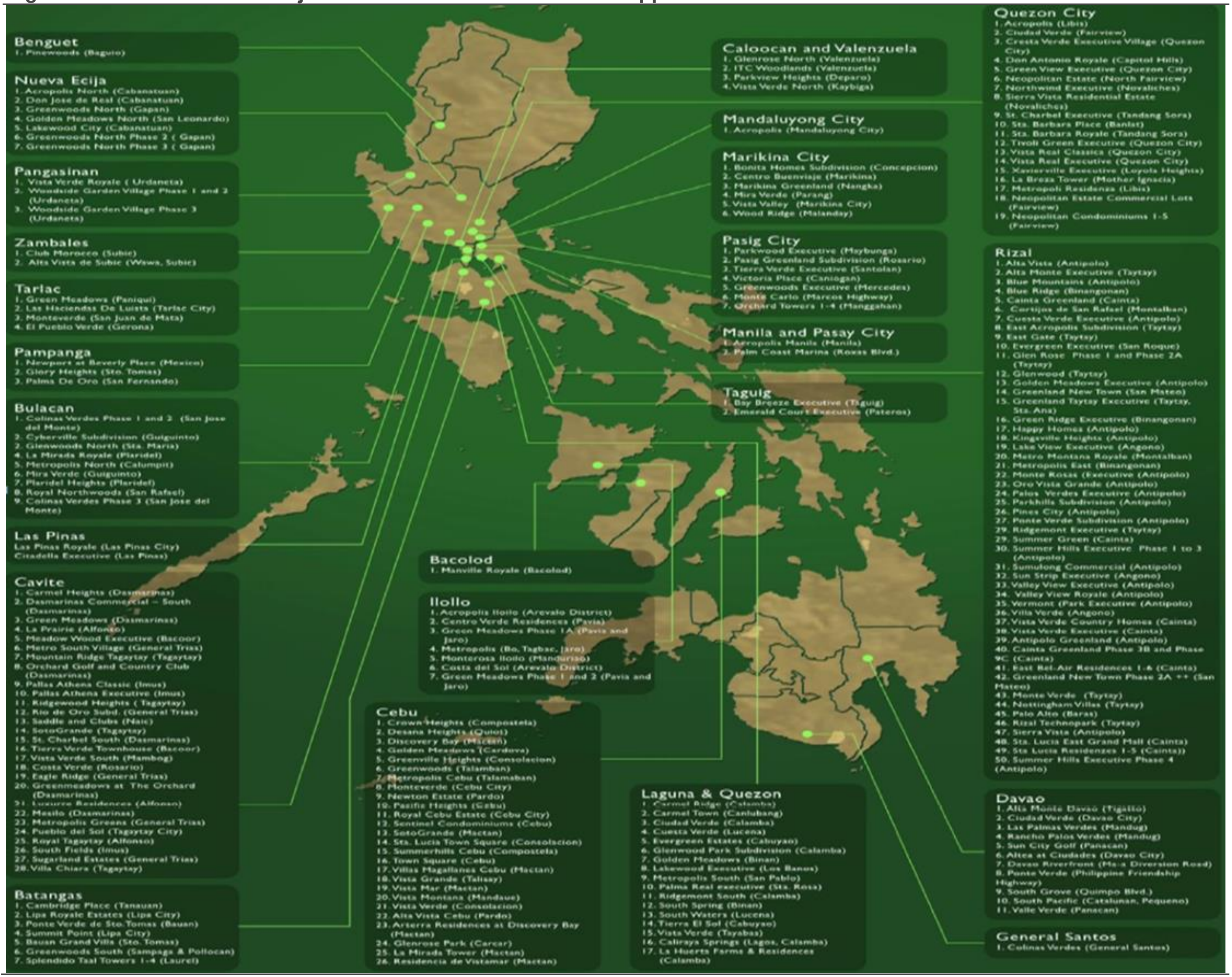
- Leasing Income currently contributes 29% of 3Q17 Revenues. We expect leasing revenues from the mall to grow at a nominal 3% per annum. This segment will continue to contribute stable recurring income but will constitute a smaller contribution as SLI's real estate order books grow.

- The company has kept its investment properties (Business Center and the Mall) valued at book. We also conservatively used book value of SLI's investment properties in our RNAV calculation. We estimate the market value of its mall today stands at PHP7.9bn vs PHP5.1bn at book.

Property Portfolio: Ongoing Projects

- SLI plans to progressively lever its balance sheet and broaden capital base to accumulate land bank in Quezon City, Rizal Laguna, Batangas, Iloilo, and Davo (see full map of development in Fig. 8) and accelerate land lot development within a board-approved level of capital expenditure. We estimated GDV of current project portfolio at approximately PHP24.2bn, applying a discount rate of 7.3%.

Fig 8 - SLI's Nationwide Project Foot Print – See Exhibit 1 in Appendix for details



Source: Company

- Majority of its residential assets mushrooms around Metro Manilla to provide quality housing to the workers in the business center. While majority of its luxury properties sprouts in popular holiday destinations such as Cebu, management is very careful in its land selection and prefers locations with relative certainty of uptake and proximity to amenities. Below are some of the highlights on SLI's current projects.

Green Meadows Iloilo

- Green Meadows is Iloilo's first lake community. Located within the outskirt towns of Pavia and Jaro, Green Meadows is designed around Lake Victoria and it boasts unique features and amenities such as the 5-hectare man-made lake, ideal for boating, fishing, kayaking and jet ski. SLI started selling this project in 2011 at ASP PHP3,900/sqm and today, the project has been 86% sold with latest ASP of PHP7,500/sqm (~10% CAGR in price appreciation).

Fig 9 - Flagship Project – Green Meadows Iloilo

Type: Mega Horizontal Estate

Location: Green Meadows Ave, Jaro, Iloilo City

GFA: 810,000sqm

Estimated average selling price: ₱7,500/sqm

Source: SCCM Research, Company

Neopolitan Estate

- The Neopolitan Condominium, 9 towers of 9-storey buildings nestled at the centre of the Business Park. Soon to rise along Mindanao and Regalado Avenues, Neopolitan Condominium offers residential living option right in the centre of a growing, fast-paced and easily accessible suburban location. The first Tower has a clubhouse, showroom, swimming pool & other essential modern amenities. SLI started selling this project in 2011 at ASP PHP68,000/sqm and today, the project has been 41% sold with latest ASP of PHP83,500/sqm (~3.5% CAGR in price appreciation).

Fig 10 - Flagship Project – Neopolitan Estate (Condominium Estate)

Type: Mega Condominium Estate

Location: Belfast, Novaliches, Quezon City

GFA: 8,856sqm

Estimated average selling price: ₱50,000/sqm

Source: SCCM Research, Company

Nasacosta Cove Batangas

- Nasacosta Resort & Residences is a resort community. The amenities include a swimming pool area and cocktail lounge. The development is designed to be a vacation home with a sea view that offers a more luxurious option to retirees and wealthier individuals. SLI started selling this project in 2016 at ASP PHP8,500/sqm and today has been 97% sold with latest ASP of PHP12,500/sqm (~20% CAGR in price appreciation).

Fig 11 - Flagship Project – Nasacosta Cove Batangas

Type: Resort Residence

Location: Nasugbu, Batangas

GFA: 216,787sqm

Estimated average selling price: ₱12,500/sqm

Source: SCCM Research, Company

Harmonizing with Government Projects

- The Philippines government has budgeted to pour in approximately PHP9.0tn over the next 5 year to develop and connect areas around the capital to accommodate the proliferation of activities around the city center. SLI has acquired land pieces that strategically located near important government-led infrastructural developments.

- SLI is actively mushrooming around the Government infrastructural projects in tandem with the pace of development in key areas such as Luzon, Laguna, Rizal and Davao City.

- Condominium project sites are close to subways to improve its accessibility and hence its attractiveness to young Filipinos working in the city center. It would improve the desirability of the project as a home or investment and consequently the selling price.

- Taking reference to a case study of Green Meadows Iloilo, the completion of a major government infrastructure – Circumferential Road 1, has lifted the lot prices from the day it was launched in 2011. **The road was completed in 2013, and improved the projects accessibility to the city center, which brought an approximate 92% uplift to ASP from PHP3,900/sqm in 2011 to PHP7,500/sqm at present (~14% CAGR in price appreciation).**

President Duterte initiated 'Build, Build, Build!', which aims to invest ~9.0tn pesos in 2017-2022 to upgrade Philippines's public infrastructure to facilitate growth and create jobs.

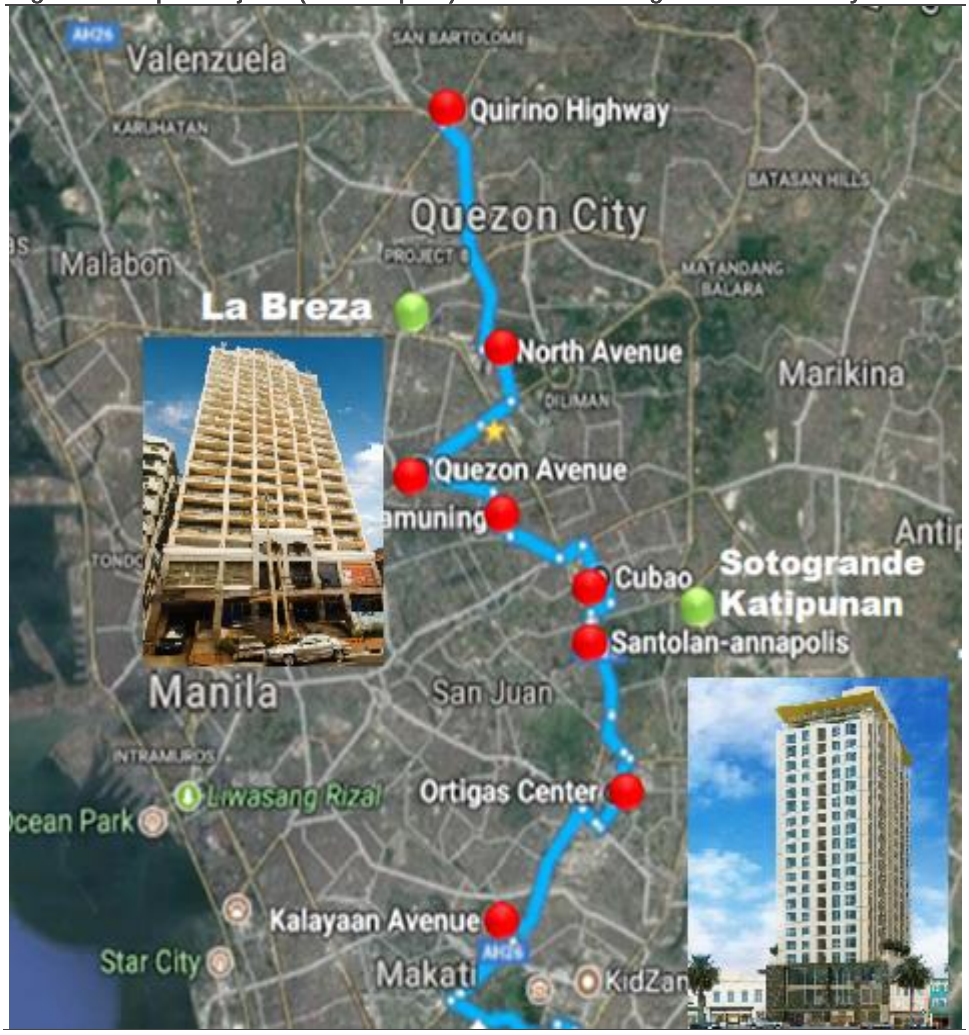
Fig 12 - Circumferential Road 1 in relation to Green Meadows Iloilo

Source: SCCM Research

- We can expect to see similar bump to projects that are built close to government infrastructure rollout. Below are examples of two future projects: La Breza and Sotogrande Katipunan and their proximity in relation to the Mega Manilla Subway, due to complete in 2020. Conservatively, we have not priced-in this potential uplift into our model though a conservative 20% uplift in ASP is likely granted given historical track-record of such projects.

We expect La Breza and Sotogrande to have a ~20% value uplift with the completion of the Mega Manilla Subway

Fig 13 - Sample Projects (Green Spots) Proximate to Mega Manilla Subway



Source: Company, SCCM Research

- SLI has long-term interest in developing projects in areas surrounding the Metro Manilla Expressway (MME). We expect Metro Manilla alone will not be able to accommodate the growth in inhabitants and will likely spill to the peripheral areas surrounding the capital.

- Below are examples of three future projects: East Bel-Air Residences Tower 2, Greenland Executive Village and Greenwood Executive village, which will benefit from the completion of the Metro Manilla Expressway. Likewise, we have not priced-in the potential uplift into our model. We think conservatively these projects should command a 20% value uplift upon completion of this expressway.

We expect East Bel-Air; Greenland Executive Village and Greenwood Executive Village to have a ~20% uplift with the completion of the Metro Manilla Expressway.

Fig 14 - Sample Projects (Green Spots) Proximate to Metro Manila Expressway

Source: Company, SCCM Research

- Below are some of the identified projects in SLI's portfolio of land banks that could benefit from certain government infrastructure projects in future. We roughly estimate ~PHP3.5bn of total value of these projects (priced-in into our end-2018 RNAV) based on their future cash flow potential, but not their valuation uplift yet. **Assuming a 20% further uplift from our current assumptions, this could add PHP0.08/share into end-2018 RNAV.**

Fig 15 - Schedule of Ongoing SLI Projects in Relation to Government Projects

Government Project	Station/Exit	Proximity	SLI Project Name	Type	Current RNAV (PHP'm)
Mega Manilla Subway	North Avenue Station	1.5km	La Breza	Condotel	54
	Katipunan Station	1.9km	Soto Grande Katipunan	Condotel	14
Pasig Marikina River Channel			Metropoli Residezia	Horizontal	80
	Along Marcos Highway	4.0km	Vermont Park	Horizontal	14
			Monte Carlo Residence	Condominium	26
			Santorini	Condotel	174
	Emerald Station	1.0km	East Bel-Air	Condominium	56
Metro Manilla Expressway	Ortigas Exit	2.0km	Greenwood Executive Vill	Horizontal	354
	Ortigas Exit	2.0km	Greenland Cainta	Horizontal	77
	Ortigas Exit	4.0km	Rizal Technopark	Commercial	44
	Ortigas Exit	6.0km	Monte Verde Royale	Horizontal	44
	Ortigas Exit	1.0km	Glenrose East Subdivision	Horizontal	3
	Marcos Highway	9.0km	Summerhills Executive Village	Horizontal	28
	Marcos Highway	9.0km	Greenland Antipolo	Horizontal	4
	Batasang Pambansa	6.0km	Greenland Newtown	Horizontal	8
Central Luzon MRT 7	SJDM Bulacan Station		Colina Verdas Bulacan	Horizontal	39
	Regalado Ave. Station		Neopolitan Business Park	Commercial	430
	Regalado Ave. Station		Neopolitan Condominium	Condominium	65
	Regalado Ave. Station		Sotogrande Neopolitan	Condotel	3
Ilocos/Pangasinan Expressway	Urdaneta Exit	5.0km	Woodside Park	Horizontal	69
	Pura Exit	5.0km	El Pueblo Verde, Tarlac	Horizontal	49
Central Luzon Link Expressway	Cabanatuan Interchange	2.5km	Lakewood City Country Club	Luxury	114
Cavite-Laguna Expressway	Open Canal Interchange	9.0km	Greenmeadows at the Orchard	Horizontal	46
	Governors Drive	10.0km	Eagle Ridge Country Club	Luxury	175
	Governors Drive	6.0km	Metropolis Greens	Horizontal	25
	Kawit Interchange	10.0km	Costa Verde Subdivision	Horizontal	15
	Open Canal Interchange	4.0km	South Fields	Horizontal	20
	Governors Drive		Mesilo Neuva Vida	Horizontal	62
	Governors Drive	8.0km	Sugarland Estate	Horizontal	64

PNR South Commuter	Binan Station	4.0km	Golden Meadows	Horizontal	20
	San Pedro Station	5.0km	South Spring	Horizontal	20
Bacolod Economic Highway	Silay Exit	3.0km	Manville Royale	Horizontal	35
Metro Cebu Expressway	Mandaue Exit	4.0km	Alta Vista	Horizontal	153
	Mandaue Exit	13.0km	Vista Mar Country Club	Luxury	122
	Mandaue Exit	15.0km	Arterra Residences	Condotel	108
	Mandaue Exit	12.0km	La Mirada Tower	Condominium	116
	Nega, Cebu Exit	14.0km	Glenrose Park	Horizontal	3
Mindanao Railway	Davao City		South Pacific	Horizontal	249
	Davao City		South Groove	Horizontal	95
	Davao City		Soto Grande	Condotel	7
	Davao City		Davao Riverfront	Horizontal	209
	Davao City		Althea Ciudades	Horizontal	16
	Davao City		Ponte Verde	Horizontal	187
Total (RNAV End-2018)					3,496

Source: Company, SCCM Research

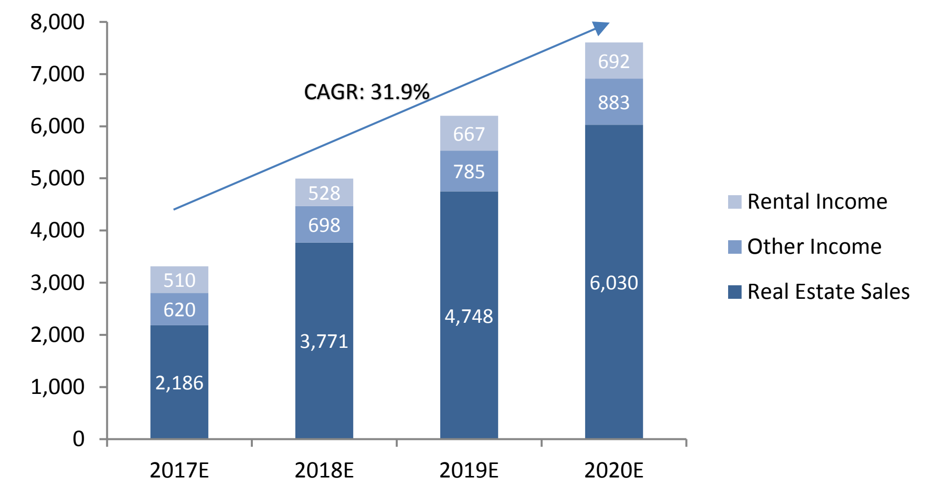
What we can expect in the next 3 years

We project Real Estate Sales to grow by 40.2% CAGR over FY17E-20E.

- The company is actively accumulating land surrounding the increasingly populated Metro Manilla while completing about 40 developments in the pipeline. We expect a ramp-up in Capex peaking in 2019, post completion of the Sta. Lucia Biz Centre, which we expect to contribute PHP100-120m of recurring income.

- We project total revenue to grow by 32% CAGR from FY17-20E, driven primarily by Real Estate sales (Horizontal developments represent 70-85% of Real Estate sales), which we expect to grow by 40% CAGR for the same period.

Fig 16 - Total Revenue Growth



Source: Company, SCCM Research

Note: Other Income includes interest payments from mortgages SLI grants to its clients. We project that the Sta. Lucia Biz Center will contribute PHP100-150M of recurring revenue from 2019 onwards.

- We expect SLI's balance sheet to become more levered and their capital efficiency ratios to improve as their under-utilized capacity achieves economic of scale. We expect ROA to improve from 3.0% to 5.3% in FY20E and ROE to improve from 5.8% to 8.8% in FY20E, while Net profit to grow by 31% CAGR from FY17-20E.

Fig 17 - SLI's Balance Sheet & Capital Efficiency in the next 3 years

(in PHP'M)	FY16	FY17	FY18E	FY19E	FY20E
Actual Capex	587	2,432			
Budgeted Capex	1,200	2,700	2,700	2,700	2,700
Net profit	730	835	1,030	1,445	1,860
Net profit growth		14.3%	23.4%	40.3%	28.8%
Net Profit Margin		25.4%	20.6%	23.3%	24.5%
Long Term debt	3,935	5,100	**10,100**	10,038	9,571
Total Debt	10,659	12,324	14,824	14,762	14,295
Total Equity	13,466	14,287	15,317	**19,437**	21,192
Debt to Equity	0.8x	0.9x	1.0x	0.8x	0.7x
ROE	5.4%	5.8%	6.7%	7.4%	8.8%
ROA	3.0%	3.1%	3.4%	4.2%	5.2%

Source: Company, SCCM Research

Note: In 2017, SLI Issued a 10 year note of PHP3.1Bn. In 2018, SLI intends to further issue a 7 year note of PHP5.0Bn. In 2019, SLI plans to raise PHP2.775Bn through equity issuance.

What makes SLI attractive?

- **Plenty of Gearing Headroom:** While most of its direct competitors have a 1.0x debt-to-equity ratio, SLI's leaner book (0.7x) offers more capex headroom to acquire land bank and ramp up developments. We expect PHP2.7bn pa capex over the next four years, while keeping its net gearing below 1.0x.

SLI is looking to spend a budgeted PHP2.7bn capex annual for the next 4 years without excess burden on its balance sheet.

- **Capital Efficiency Improvements:** Due to efficient capital management and a streamlined business model, SLI has been able to maintain approximately 65% gross margins over the years. SLI's gross margins remains the highest vis-à-vis its peers such as Filinvest and Vista Land. As the company becomes more levered, **we expect ROA to improve from 3.1% to 5.3% in FY20E and ROE to improve from 5.8% to 8.8% in FY20E.**

Fig 18 - Snapshot of SLI's Key Metrics

	FY13	FY14	FY15	FY16	FY17E	FY18E	FY19E	FY20E
Gross Margin	64.2%	60.5%	69.9%	65.2%	67.0%	62.3%	61.7%	60.4%
Net Profit Margin	25.5%	27.7%	25.3%	26.4%	24.3%	20.6%*	23.3%	24.5%
ROA	1.7%	3.1%	3.2%	3.0%	3.1%	3.4%	4.2%	5.2%
ROE	2.5%	4.7%	5.3%	5.4%	5.8%	6.7%	7.4%	8.8%

Source: SCCM Research

**The fall in net profit margin is due to higher interest expense surrounding new 7-year note of PHP5.0Bn issued*

Fig 19 - SLI Comparable

Name	Ticker	Mkt Cap (USD'bn)	P/B	P/E	ROA (%)	ROE (%)	Debt/ Equity	Gross Margin (%)	3Y EPS CAGR (%)
Sta. Lucia land	SLI.PM	0.2	0.65x	10.2x	3.4%	6.5%	0.68x	68.2%	22.7%
Ayala Land	ALI.PM	12.5	4.15x	26.2x	4.4%	16.0%	0.91x	36.3%	16.8%
Century Property Group	CPG.PM	0.1	0.34x	8.1x	1.5%	4.0%	0.97x	32.0%	N.A.
SM Prime Holdings	SMPH.PM	20.8	4.13x	38.1x	5.4%	11.2%	0.75x	84.1%	13.2%
Robinson Land	RLC.PM	1.8	1.32x	14.2x	4.6%	9.3%	0.71x	53.3%	8.8%
Vista Land & Lifescapes	VLL.PM	1.4	1.04x	8.7x	4.7%	11.3%	1.07x	51.3%	13.3%
Megaworld Corp	MEG.PM	3.3	1.17x	12.4x	4.4%	9.4%	0.46x	65.9%	9.1%
Filinvest	FLI.PM	0.9	0.71x	7.3x	4.4%	9.8%	0.95x	49.3%	12.8%
Industry Average			**1.70x**	**15.7x**	**4.1%**	**9.7%**	**0.81x**	**54.5%**	**10.6%**

Source: Bloomberg, SCCM Research; Prices as of closing 28 Feb 2018

- **Attractively-valued:** SLI's reinvention has been 5 years in the making. Despite its order book visibility and quality portfolio, it still trades at a 50% discount to our end-2018 RNAV (7.3% discount applied). In addition, the company trades at 0.7x, below the industry average of 1.7x, which lends further comfort to our recommendation.

- **Understated asset values:** SLI has conservatively kept its investment properties and strategic land bank at book value. **Note that we have yet to price-in the potential value uplift of projects proximate to ongoing government infrastructure (PHP0.08/share) and its investment properties (PHP0.25/share).**

Forecasts & assumptions

- The core assumptions for the P&L are as follows:
  - Our revenue assumption is based on management's projections on product launches, completions, as well as a 3% pa ASP increase. Horizontal developments remain the bulk and driver of revenue. We expect overall revenue to grow by a robust 32% CAGR over FY17-20E.
  - The Sta Lucia Business Center is slated to operate in FY19E and contribute approximately PHP120m to the annual recurring income in the first year of operation. We have assumed a 5% pa rental increase for both the mall and the business center in our model.
  - We estimate Income generated from mortgages to grow by 12.5% annually, using the growth from FY16-17E as a benchmark. This will contribute steadily to Interest Income of SLI's topline.
  - We expect Gross Margin to remain steady at above the 60% level, despite continued expansion phase over next few years. In addition, we expect EBIT margins to remain stable at above 40% level though likely will be affected slightly by the step-up in marketing efforts of new projects.
  - Net profit margins would likely dip to 19.2% in 2018 due to increased interest expense arising from the issuance of new 7-year note of PHP5.0bn. However, it should recover and stabilize at 22% by FY20E. We project Net profit to grow by 31% CAGR over FY17-20E.

We project total revenue contribution from Horizontal Developments to rise from 48.7% in FY17E to 58.1% in FY20E

Fig 20 - Consolidated P&L

Y/E 31 Dec (PHP M)	FY17E	FY18E	FY19E	FY20E	FY21E
Operating Revenue					
Horizontal Developments	1,646	3,146	3,753	4,171	3,457
Vertical Developments	539	517	725	779	544
New Order book	-	108	270	1,080	2,700
Other Revenues					
Mall Lease	510	528	547	567	588
Biz Center Lease	-	-	120	125	130
Interest Income	157	177	199	223	251
Other Income	463	521	586	659	742
Total Revenue	**3,316**	**4,997**	**6,200**	**7,604**	**8,413**
Revenue Growth Rate		*50.7%*	*24.1%*	*22.7%*	*10.6%*
Operating Expenses					
COGS	(1,093)	(1,885)	(2,374)	(3,015)	(3,351)
Gross Profit	**2,223**	**3,111**	**3,862**	**4,590**	**5,062**
GPM Margins	*67.0%*	*62.3%*	*61.7%*	*60.4%*	*60.2%*
Other Operating expenses					
Overhead and Marketing Costs	(492)	(848)	(1,068)	(1,357)	(1,508)

Depreciation	(170)	(170)	(190)	(190)	(190)
EBIT	**1,561**	**2,093**	**2,567**	**3,043**	**3,364**
EBIT Margins	*47.1%*	*41.9%*	*41.4%*	*40.0%*	*40.0%*
Interest Expense	(411)	(723)	(718)	(686)	(512)
Income taxes	(345)	(411)	(525)	(676)	(822)
Net Profit	**805**	**959**	**1,324**	**1,681**	**2,029**
Net Profit Margins	*24.3%*	*19.2%*	*21.4%*	*22.1%*	*24.1%*
Net Profit Growth		*19.1%*	*38.1%*	*27.0%*	*20.7%*
Add: Income from SLHomes	30	71	120	179	197
Consolidated Income	**835**	**1,030**	**1,445**	**1,860**	**2,226**
Consolidated Net Profit Margin	*25.2%*	*20.6%*	*23.3%*	*24.5%*	*26.5%*
No. of Shares Outstanding	8,946	8,946	10,796	10,796	10,796
EPS	**0.093**	**0.115**	**0.134**	**0.172**	**0.206**
EPS Growth	*14.3%*	*25.0%*	*16.2%*	*28.8%*	*19.7%*

Source: Company, SCCM Research

- The core assumptions for the balance sheet are as follows:
  - We expect Accounts Receivable to grow by 44.1% pa over FY17-20E to reflect the growing working capital of the company.
  - We estimate Capex of total PHP10.8bn over the next 4 years, which will support PHP8.0bn of gain in asset value for the same period.
  - In 2018, SLI intends to issue a 7-year note of PHP3.0bn with over-subscription of PHP2.0bn in effort to finance capex. In our projection, we expect the full PHP5.0bn to be fully-subscribed.
  - In 2019, SLI plans to raise PHP2.775bn through equity issuance in effort to keep gearing manageable below 1.0x. We have priced this into our model.

Cash Collection is likely to lag the percentage completion of projects as buyers usually pay in instalments

Fig 21 - Consolidated Balance Sheet

Y/E 31 Dec (PHP bn)	**FY17E**	**FY18E**	**FY19E**	**FY20E**	**FY21E**
Cash	819	2,132	4,162	3,651	2,460
Accounts Receivable	2,885	4,458	6,351	8,656	10,671
Inventory	13,160	13,574	13,900	13,586	12,935
Other Current Assets	2,473	2,473	2,453	2,433	2,413
Non-Current AR	934	934	934	934	934
Commercial Assets	5,403	5,653	5,482	5,312	5,142
Investment in List Co.	844	844	844	844	844
Other Non-Current Assets	94	73	72	71	70
Total Assets	**26,612**	**30,142**	**34,199**	**35,488**	**35,469**
Accounts Payable	2,800	2,800	2,800	2,800	2,800
Customer Deposit	909	909	909	909	909

Short term Debt	2,896	396	396	396	1,196
Long term Debt	5,100	10,100	10,038	9,571	6,636
Others	620	620	620	620	620
Total Liabilities	**12,325**	**14,824**	**14,762**	**14,295**	**12,160**
Equity	10,386	10,386	13,161	13,161	13,161
Retained Earnings	3,460	4,489	5,834	7,590	9,706
Other Equity Accounts	441	441	441	441	441
Total Equity	**14,287**	**15,331**	**19,437**	**21,292**	**23,308**
Total Liabilities & Equity	**26,612**	**30,142**	**34,199**	**35,488**	**35,469**

Source: Company, SCCM research

Valuation – Initiating with a BUY; TP PHP1.40

RNAV valuation implies substantial upside

- As of end-2018, SLI's RNAV per share is PHP1.96. To be conservative, we have 1) applied a modest 3% pa increment to selling price on completed percentages of projects; while 2) assigned a 30% discount on the RNAV to arrive at our TP of PHP1.40, representing a 40% upside. Historically, SLI has been trading at an average of 30-35% discount to its book value.

We think that a 3% step-up in ASP is a modest assumption given historically, land price in Manila has been growing by ~10% pa in the past few years

- We believe SLI is undervalued given not only it currently trades at a 50% discount to our end-2018 RNAV (applying a discount of 7.3%), but also its robust 22.7% CAGR EPS growth from FY18-20E (vs peers of 12.3%). We initiate with a BUY rating.

Fig 22 - RNAV of current project portfolio

In PHP'm	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E	2027E
EBITDA from Horizontal Projects	1,981	2,290	1,816	1,363	996	1,095	848	916	501
EBITDA from Vertical Projects	722	774	687	558	519	553	1,377	58	0
Combined EBITDA	2,704	3,064	2,504	1,921	1,515	1,648	2,225	974	501
BV of Sta Lucia Biz Center and Mall	5,653								
Annual increment rate to selling price	3.0%								
Discount Rate Applied	7.3%								
RNAV (End-2018)	**17,526**								
RNAV per share	**1.96**								
Current Discount to RNAV	**50.0%**								
Target Price	**1.40**								
Upside From Target Price	**40.0 %**								

Source: SCCM Research

- Based on a simple sensitivity analysis, we think that we are fairly conservative with our estimate. We think that the strong macro-economic conditions and government infrastructure roll-out could support a potentially higher land ASP growth, which can drive our RNAV higher as well.

Fig 23 - RNAV Sensitivity Analysis – Annual ASP increment against Discount Rate

Data Table	0.0%	1.0%	2.0%	3.0%	4.0%	5.0%	6.0%	7.0%	8.0%
5.0%	1.88	1.94	2.00	2.07	2.14	2.21	2.28	2.36	2.44
6.0%	1.84	1.90	1.96	2.02	2.08	2.15	2.22	2.29	2.37
7.3%	1.79	1.85	1.90	**1.96**	2.02	2.08	2.15	2.22	2.29
8.0%	1.77	1.82	1.87	1.93	1.99	2.05	2.11	2.18	2.25
9.0%	1.73	1.78	1.83	1.89	1.94	2.00	2.06	2.13	2.19
10.0%	1.70	1.75	1.80	1.85	1.90	1.96	2.02	2.08	2.14
11.0%	1.67	1.71	1.76	1.81	1.86	1.92	1.97	2.03	2.09

Source: Company, SCCM Research

- We think that this discount is set to widen further as the company invests PHP10.8bn over the next 5 years to acquire land banks and extend its order books. In addition, in line with the government's push to improve the nation's infrastructure, we expect a further conservative uplift of ~20% to its RNAV (PHP0.08/share). We have also conservatively valued its investment properties at book value despite its current market value of its malls is now ~50% higher (PHP0.25/share).

Sta Lucia Mall's stated book value is PHP5.1bn vs estimated appraised value of PHP7.9bn.

Fig 24 - RNAV Contribution breakdown by project type

	RNAV Contribution in PHP'M	GD Contribution in %
Horizontal projects	8,302	47.4
Condo & Condotel	995	5.7
Commercial	2,539	14.5
Investment Properties	5,653	32.3
Others	36	0.2
Total	17,526	100.0

Source: SCCM Research

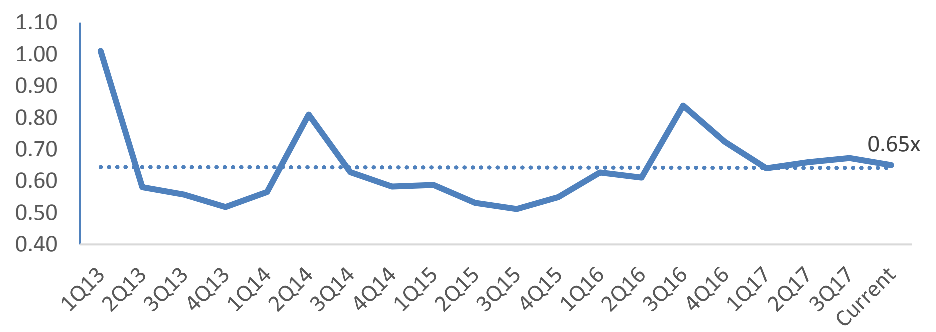
- Investors should focus on SLI's earnings trajectory, robust margin profile, and gearing headroom. We note that SLI's growth profile started at a lower base because of management's initial reluctance to take on more debt, impairing growth potential the past few years. However, this is set to change as the company utilizes its balance sheet to grow over next few years.

Current P/B provides valuation support

- SLI currently trades at 0.65x P/B, which we think is undervalued given that the company has kept its reported land banks and projects valued at cost. We think with project completions ramping up and consequent stronger earnings performance, the company should trade closer to its book value.

We think that there is a tangible growth story to support a higher P/B valuation given its 23% EPS CAGR growth over FY17E-20E

Fig 25 - SLI Historical Price to Book – Average 0.65x



Source: Bloomberg

- Therefore, taking a conservative stance on a 12mo forward book value, we think that the company should trade at 0.80-0.85x as it gravitates towards the industry average of 1.7x. Using a simple sensitivity analysis (plotting book value growth against P/B) as shown in Fig. 26, we think that there is a comfortable valuation support to our target price. Our end-2018 TP implies SLI trading at 0.89x current P/B or 0.82x 12mo forward P/B.

Fig 26 - Forward P/B Sensitivity Analysis – Book value growth against P/B

Current Price		1.00							
3Q17 Book Value (PHP'M)		14,145							
Number of Shares ('M)		8,946							
Current BV/Share		1.58							
Expected P/B		0.8x							
Book Value Growth Assumption		7.7%							
Base Assumption		**1.36**							
Data Table	5.0%	5.5%	6.0%	6.5%	7.0%	7.5%	8.0%	8.5%	9.0%
0.60x	1.00	1.00	1.01	1.01	1.02	1.02	1.02	1.03	1.03
0.65x	1.08	1.08	1.09	1.09	1.10	1.10	1.11	1.12	1.12
0.70x	1.16	1.17	1.17	1.18	1.18	1.19	1.20	1.20	1.21
0.75x	1.25	1.25	1.26	1.26	1.27	1.27	1.28	1.29	1.29
0.80x	1.33	1.33	1.34	1.35	1.35	**1.36**	1.37	1.37	1.38
0.85x	1.41	1.42	1.42	1.43	1.44	1.44	1.45	1.46	1.46
0.90x	1.49	1.50	1.51	1.52	1.52	1.53	1.54	1.54	1.55

Source: Company, SCCM Research

Comparables with Valuation

- In the universe of Philippine developers, SLI is considered small in terms of market cap and is very much under-appreciated. Its profitability or growth potential does not pale in comparison to larger players such as Megaworld or Vista Land.

We expect EPS CAGR of 23% for FY17-20E, which is much stronger than the industry average of 14%

Fig 27 - SLI Comparable

Name	Ticker	Mkt Cap (USD'bn)	P/B	P/E	ROA (%)	ROE (%)	Debt/ Equity	Gross Margin (%)	3Y EPS CAGR (%)
Sta. Lucia land	SLI.PM	0.2	0.65x	10.2x	3.4%	6.5%	0.68x	68.2%	22.7%
Ayala Land	ALI.PM	12.5	4.15x	26.2x	4.4%	16.0%	0.91x	36.3%	16.8%
Century Property Group	CPG.PM	0.1	0.34x	8.1x	1.5%	4.0%	0.97x	32.0%	N.A.
SM Prime Holdings	SMPH.PM	20.8	4.13x	38.1x	5.4%	11.2%	0.75x	84.1%	13.2%
Robinson Land	RLC.PM	1.8	1.32x	14.2x	4.6%	9.3%	0.71x	53.3%	8.8%
Vista Land & Lifescapes	VLL.PM	1.4	1.04x	8.7x	4.7%	11.3%	1.07x	51.3%	13.3%
Megaworld Corp	MEG.PM	3.3	1.17x	12.4x	4.4%	9.4%	0.46x	65.9%	9.1%
Filinvest	FLI.PM	0.9	0.71x	7.3x	4.4%	9.8%	0.95x	49.3%	12.8%
Industry Average			**1.70x**	**15.7x**	**4.1%**	**9.7%**	**0.81x**	**54.5%**	**10.6%**

Source: Bloomberg, SCCM Research; Prices closing as of 28 Feb 2018

- According to SLI, their main competitors in terms of bidding for land bank are Vista Land (VLL) and Filinvest (FLI). They are frequently compared with each other due to their relative similarity in size and business scope (horizontal developments). In terms of their numbers, we project SLI's EPS CAGR of 23% from FY17-20E to outpace VLL's 13% and FLI's 13% based on Bloomberg estimates.

- SLI's current P/B and P/E is one of the more depressed of its peers at 0.7x and 10.2x (vis-à-vis 1.7x and 15.7x, respectively) despite its strong growth potential. We think that the company is deeply undervalued considering that we expect EPS to grow by 23% CAGR for FY17-20E vis-a-vis 14% for its peers.

- In terms of gross margins, SLI is also more profitable than the bigger players. In fact, their Gross Margins of 68.2% outperforms the industry average of 55% and bigger players such as Ayala Land, Vista Land, and Filinvest, thanks to its less risky, higher margin, land-plot focus.

- Currently, SLI's ROE is relatively lower at 6.5%, but we think that as its projects ramp up and its books become more levered, ROE could progressively improve to 8.8% in FY20E, roughly in line with industry average.

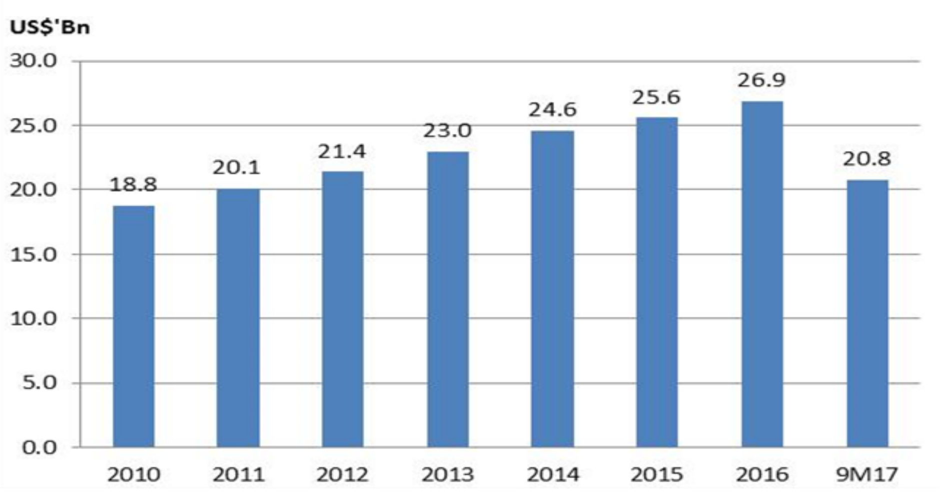
Industry Tailwind

2017 GDP growth beats forecasts

The Philippines government is committed to support the long-term growth of the country that would require improved infrastructure in place.

- For financial year 2017, Philippines' economic growth stood at a respectable 6.7% YoY – one of the fastest growing economies in the region. This paves the way for the new President to attract more investments and step up infrastructure spending ahead.
- Remittances from overseas Filipino workers (OFWs) reached US$28.1bn (+4.3% YoY) in 2017. OFWs are a steady source of remittance for their families back home. With favourable tax exemption treatment of remittance by the government, OFW remittances are going to continue to enable greater economic migration to the middle class and foster home ownership.

Fig 28 - OFW remittance continue to stay robust and support home purchases



Source: *Bangko Sentral ng Pilipinas.*

- Looking ahead, as macroeconomic fundamentals remain strong with manufacturing and investments contributing significantly to the country's GDP growth, and BPO revenues and OFW remittances expected to sustain household consumption, GDP is expected to continue to grow by 6.7-6.8% in 2018.

Strong land prices to sustain

- In 4Q17, Capital values for Makati CBD/Fort Bonifacio/Rockwell condominium increased by 1.9%/2.3%/0.3% QoQ. Given the high pre-sale volumes and a prolonged low interest rate environment, Colliers expects Makati CBD, Fort Bonifacio and Rockwell condo prices to grow by 14%, 8% and 11% over the next 12 months, respectively.

Fig 29 - Comparative Luxury 3BR Residential Capital Values (PHP/sqm)

LOCATION	3Q 2017	4Q 2017	%CHANGE (QoQ)	4Q 2018F	%CHANGE (YoY)
Fort Bonifacio	111,600 - 238,600	112,000 - 239,400	0.3%	121,200 - 259,200	8.3%
Makati CBD	110,300 - 277,900	111,700 - 286,400	2.5%	127,000 - 325,200	13.8%
Rockwell Center	197,200 - 236,600	198,000 - 244,300	1.9%	220,500 - 270,000	11.4%

Source: Colliers International Philippines Research

- In 4Q17, condo rental rates continued to soften across major business districts, with rates in Makati CBD sliding 0.8% QoQ (vs.-1.6% in 4Q16). Similarly, rents in Fort Bonifacio (-1.4% QoQ) and Rockwell (+0.1% QoQ) remained soft. Gentle recovery of 1-3% is expected for the near to midterm given strong demand from domestic and foreign workers.

Fig 30 - Comparative Luxury 3BR Residential Rental Values (PHP/sqm)

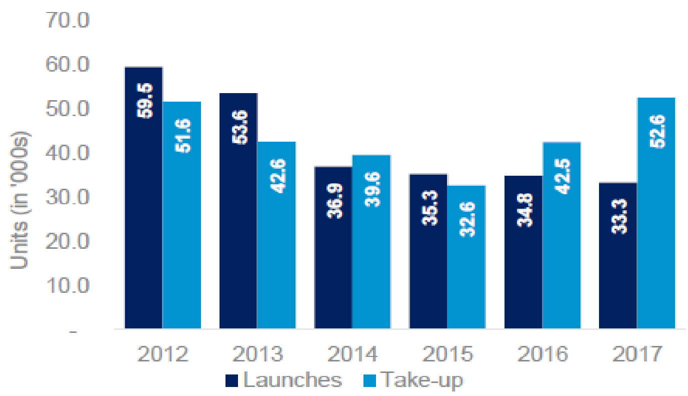
LOCATION	3Q 2017	4Q 2017	%CHANGE (QoQ)	4Q 2018F	%CHANGE (YoY)
Fort Bonifacio	620 - 1,000	620 - 1,000	0.1%	610 - 1,000	-1.0%
Makati CBD	530 - 1,080	530 - 1,070	-0.8%	520 - 1,060	-1.6%
Rockwell Center	730 - 1,040	730 - 1,020	-1.4%	720 - 1,000	-1.3%

Source: Colliers International Philippines Research

- Looking ahead, amid shortage of available land, growing investor interest and robust demand support, we believe prices of land, particularly in major business districts, would continue to firm up. According to Colliers, land prices at Makati CBD, Fort Bonifacio and Ortigas Center could potentially increase by an average 13.8% over the next 12 months.

The strong demand is likely to spill to Manila's peripheral cities as Manilla become increasingly over—populated.

Fig 31 - Metro Manilla Condominium Launches and Take-up



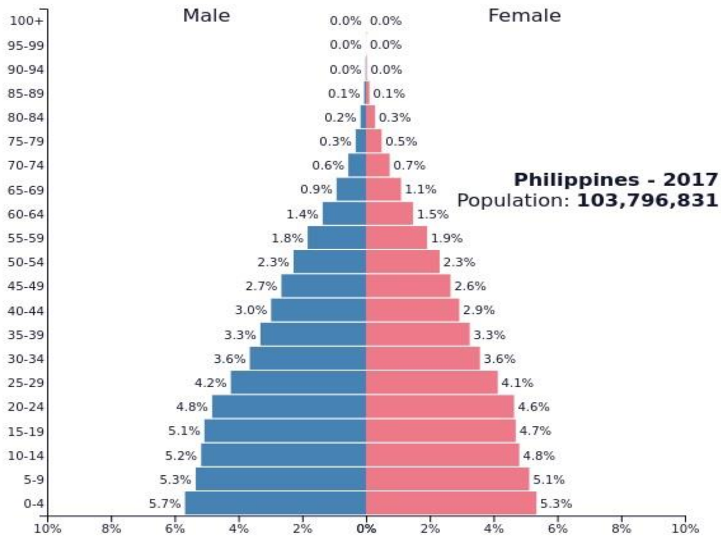
Source: Colliers International Philippines Research

The Demographic Advantage – Supporting Organic Growth

- **Young and Growing Population:** Philippines, like several of its ASEAN counterparts, have a growing and sophisticating workforce with fertility rate of 2.9. The financial and career burden of birthing and raising children has yet to become a significant impediment to young mothers. IMF forecasts a 1.52% population growth in 2018.

Younger Filipinos would require quality housing to support their aspirational demand. Proper housing options support robust economic activities.

Fig 32 - Philippines 'population pyramid



Source: Population Pyramid

- **Healthy Rate of Household Formation:** Based on the latest data from Euromonitor, there were 529,000 new households annually from 2011-2016. With President Duterte's steady hand ushering in a new era of economy-centric politics, the younger workforce is migrating towards Metro Manilla and its peripheral cities for career opportunities, demand for modern housing options rises in tandem.

- **Emerging Middle Class:** The World Bank projects that Philippines GDP will grow by 6.9% while GDP per Capita will grow by 9.27% in 2018. The higher disposable income of the average Filipino has supported capital appreciation trends

There is still no socio-economic issues that would impair the growth of household as yet. We think this trend is sustainable in the short to mid term.

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Recommendation Interpretation

Recommendation	Expected absolute returns (%) over 12 months
Buy	More than 15%
Hold	Between 15% and –5%
Sell	Less than –5%

Expected absolute returns are based on the share price at market close unless otherwise stated. Stock recommendations are based on absolute upside (downside) and have a 12-month horizon. Our target price represents the fair value of the stock based upon the analyst's discretion. We note that future price fluctuations could lead to a temporary mismatch between upside/downside for a stock and our recommendation.

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