

# Hong Lai Huat Group Limited

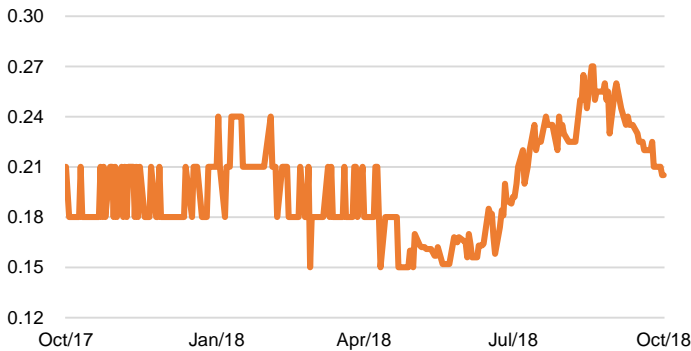
Date: 19 October 2018

**BUY**  
(Maintained)

**Target Price: S\$0.51**  
(+155%)

**HLHG SP**

**Price: S\$0.200** (as at 18 October 2018)



Share price	1M	3M	6M	1Y
Hong Lai Huat	-21.5%	0.0%	5.9%	0.0%
Catalist Index	-5.3%	-9.6%	-14.7%	-17.4%

<b>Market capitalisation</b>	S\$44.4 million		
<b>Current Price</b>	S\$0.200		
<b>Shares outstanding</b>	221.9million		
<b>Free Float</b>	60.5%		
<b>Top shareholders</b>	Dato' Dr. Ong Bee Huat	15.0%	
	Dr. Wong Wen-Young Winston	6.2%	
<b>Recommendation of other brokers</b>	N/A		

Source: Company data, Bloomberg, SAC Advisors

## Analyst

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## Key Financials

Year ended December (S\$m)	FY2015A	FY2016A	FY2017A	FY2018E	FY2019E	FY2020E
<b>Revenue</b>	5.7	10.3	12.6	52.7	105.1	29.9
<b>% Growth</b>	N/A	80.7%	21.8%	318.5%	99.3%	-71.6%
<b>Gross Profit</b>	4.5	7.8	6.4	31.1	59.3	19.6
<b>Gross Profit margin (%)</b>	77.8%	75.9%	50.5%	58.9%	56.4%	65.8%
<b>Profit before tax</b>	7.4	7.0	4.9	18.8	48.5	10.6
<b>Profit after tax</b>	5.5	6.3	2.1	15.0	38.8	8.5
<b>% Growth</b>	516.7%	14.85%	-67.48%	633.02%	158.09%	-78.13%
<b>Profit after tax margin (%)</b>	95.9%	60.9%	16.3%	28.5%	36.9%	28.4%
<b>Basic EPS (S\$ cents)</b>	2.47	2.84	0.92	6.77	17.47	3.82
<b>Diluted EPS (S\$ cents)</b>	2.40	2.76	0.90	6.57	16.97	3.71
<b>P/E (x)</b>	6.59	5.74	17.65	2.41	0.93	4.26
<b>Net Debt/Equity (%)</b>	5.8%	Net cash	2.5%	Net cash	Net cash	Net cash

N/A: Not applicable

## Cambodia Site Visit Notes

**D'Seaview on track for completion by June 2019.** We visited Hong Lai Huat Group Limited's ("Hong Lai Huat", the "Company", or the "Group") signature D'Seaview project development in Sihanoukville, Cambodia as well as the city. We walk away from the visit feeling impressed by the rapid developments currently taking place in the city and see Sihanoukville benefiting from Chinese investments into the city. We also understand that nearly 80% of the project's commercial and residential units have already been sold, while development work is on track for scheduled completion by June 2019.

The Company has also entered into a sales and purchase agreement to sell its 98-room hotel in its D'Seaview project in Sihanoukville, Cambodia for S\$15.7 million. As an early mover in this type of development in the city, they are a price leader in the market, which has translated into good margins for the Company. We understand that land prices in Sihanoukville have skyrocketed since 2015 when the land was acquired, as international developers snapped up landbank over the last 3 years.

**Sihanoukville is a key beneficiary of China's Belt and Road initiative.** Sihanoukville, a rapidly-developing urban area that hosts Cambodia's sole deep-water seaport has seen a building boom in the last three years, driven by Chinese investments in the city. Sihanoukville's deep-water port, part of a vital trade route for Chinese President Xi Jinping's Belt and Road development initiative has driven Chinese investments into the city. In the last three years, projects such as condominium/apartment complexes, hotels, resorts and malls have gone up in different parts of Sihanoukville. By the end of 1H17, a total of 5,700 units within 6 residential-led projects have been announced in the market or are under construction across the town. During our visit to Sihanoukville, Chinese-run construction projects are visible across the city. The city centre is also lined with Chinese businesses and restaurants which have sprouted up in the last few years.

**We maintain BUY.** We are forecasting Hong Lai Huat to post a strong recovery in 2018 and 2019 as it recognises higher sales from D'Seaview. The Group has also signed a MOU with The Royal Group to develop a freehold plot of land at Phnom Penh. The stock is trading at an attractive 0.9x FY19 P/E and 0.28x FY17 P/BV versus sector average of 0.9x. We value Hong Lai Huat at S\$0.51 per share after applying a 40% discount to its RNAV. This translates to an implied FY18 P/BV of 0.8x. We have not factored in any contribution from potential property earnings in Singapore, and cooperation with a third party to expand its cassava business in Cambodia. Despite jumping over 25% since our initiation of coverage on 29 June 2018, we see the Company as deeply undervalued, we maintain BUY.

**Key risks:** Slow response for D'Seaview project

## Company background

Hong Lai Huat was founded by Dato Dr Johnny Ong Bee Huat in 1988 and started as a construction company, named Hong Lai Huat Construction. In 1997, the group was graded by Building and Construction Authority (“**BCA**”) as G8 building contractor after demonstrating a good track record of construction of HDB housing projects, shopping malls, community centres and industrial projects. The G8 grading allows the group to tender for public projects of unlimited values.

In 2000, the Group was listed on the mainboard of SGX under the name of “Hong Lai Huat Group Limited”. The Group launched its maiden project, D’Ecosia at Still Road in 2001 and took pride that the project was completely sold within a year after completion in 2003. Having tasted the success of D’Ecosia, the company went on to develop several projects in Singapore, namely D’Fresco, D’Almira, D’Lithium, D’Centennial, D’Kranji Farm Resort, D’Castilia from year 2003 to 2013.

In 2015, the Group expanded its property development arm to Cambodia after 2 years of careful study.

In Cambodia, it also owns one of the largest cassava plantations in Cambodia with a combined land size of approximately 10,000 hectares and a maximum annual production capacity of 225,500 ton of fresh cassava. The starch factory, which is located within the farm, has a maximum production capacity of 36,000 ton of native tapioca starch per annum.

The group has two core businesses:

### **Property development**

With a vast experience in the property and real estate business in Singapore, it is currently developing its first freehold mixed development in Cambodia known as D’Seaview, a project with 737 residential units and 67 commercial units comprises office buildings, commercial retail shops and a hotel.

### **Agriculture**

The Group cultivates fresh cassava for the production of native tapioca starch for local and the export market. HLH has a 70-year concessional rights to the agriculture land with total land area of approximately 10,000 hectares, located at Aoral District, Kampong Speu Province, Cambodia (“**Aoral farm**”).

## Sihanoukville, Cambodia's Prime Beneficiary of the Belt and Road Initiative

Sihanoukville is a province in southwest Cambodia known for its beaches and tropical islands. More importantly though, it is set around a deep-water port on a peninsula jutting into the Gulf of Thailand. As the home to Cambodia's only deep-water port, which is part of a vital trade route for President Xi Jinping's Belt and Road development initiative, the city has become a focal point for Chinese investment.

The development of the Cambodia Sihanoukville Special Economic Zone ("SSEZ") is also set to transform Sihanoukville into the "Shenzhen" of Cambodia. Cambodia SSEZ is an economic and trade cooperation zone constructed by Chinese and Cambodian enterprises, which is a landmark project on China's Belt and Road initiative, aiming at creating an ideal trading platform for enterprises.



Source: Tourism Cambodia, SAC Advisors



Source: ssez.com



Source: ssez.com



Source: SAC Advisors

SSEZ is located in Sihanoukville, 3km from the Sihanoukville airport and 12km from the Sihanoukville international deepwater port, close to No.4 highway, and 210km from Phnom Penh (the capital of Cambodia).

As an important cooperation project between Cambodia and China, SSEZ attracts high level attention from leaders of both countries. Under the support of the two governments, SSEZ has been developing rapidly. With the total planning area of 11.13km<sup>2</sup>, SSEZ has finished the initial phase of the development area of 5.28km<sup>2</sup>, with textiles and garment, bags and leather products, hardware and machinery, wooden products as the leading industries. In the second phase, they are likely to play to the advantage of the site's vicinity to the port and will mainly bring in industries such as machinery, equipment and construction materials. SSEZ will eventually be built into a well-facilitated, fully-functional, ecological model industrial zone with about 300 enterprises and have around 80,000 to 100,000 industrial workers,

We believe the SSEZ will be an important development for Sihanoukville moving forward. Prime Minister Hun Sen's willingness to embrace Chinese investment, has ensured Cambodia is at the centre of the Belt and Road initiative project in Southeast Asia. The southern coast of Cambodia is now home to US\$4.2 billion worth of power plants and offshore oil operations all owned by Chinese companies. Beyond Sihanoukville, Chinese money is financing a new four-lane highway to Phnom Penh and a bigger airport in the capital.

In the near future, we see an influx of Chinese businessmen arriving in Sihanoukville to take advantage of the new China-Cambodia tax-free economic zone. The majority of the 100-plus factories in the economic zone are now run by Chinese companies, and a further 200 mainly Chinese companies – producing consumer goods and garments – will be part of its ongoing expansion. We believe these create positive effects on the residential property market in Sihanoukville. During our visit there, we observed more than 6 residential apartments under construction by Chinese developers.

## Sihanoukville, Cambodia's Prime Beneficiary of the Belt and Road Initiative

Key Economic Indicators	
GDP growth-Cambodia (2017)	6.9%
Tourist arrivals growth (1H17)	12.8%
Gross Foreign reserves (US\$)	8.0bn

Source: World Bank, SAC Advisors

The developments in Sihanoukville has benefited the real estate market in Cambodia. As investments continue to pour into Sihanoukville, accumulated investment value into the city has reached US\$310 million, according to a report by CBRE Research.

Land prices within Sihanoukville have appreciated rapidly during the past 3 years, driven by rising investment into the coastal city's hospitality and resort sector, as well as residential-led projects and manufacturing industries, particularly focused on the city's SEZs. According to a CBRE survey undertaken in 1H17, land within the vicinity of the beach was offered to the market at between US\$450 and US\$2,500 per square meter.

According to CBRE, for land in the city's downtown area, prices ranged between US\$200 and US\$750 per square meter. Residential land within the town was quoted between US\$120 and US\$300 per square meter.

As compared to Phnom Penh, the Sihanoukville's condominium market is still relatively under-developed. The first high-rise condominium project was launched on Independence Beach in 2015. During 1H17, two residential-led projects comprising a total of 1,324 condominium units were announced and both have already commenced construction. This is consistent with our observation during our visit to Sihanoukville, where we saw numerous developments taking place around the city.

By the end of 1H17, a total of 5,700 units within 6 residential-led projects have been announced in the market or are under construction across the town. The graph on the left shows the supply of condominiums in Sihanoukville during the next three years. Demand within the Sihanoukville condominium sector is expected to be driven primarily by foreign investors, particularly from China.

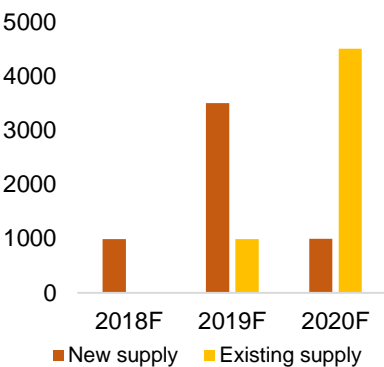
The city's hotel market has also picked up with rising tourism into Sihanoukville. According to Cambodia's Ministry of Tourism, tourism arrivals to Cambodia rose from 3.5 million in 2012 to 5.6 million in 2017, representing a 9.3% compounded annual growth rate. Chinese tourists from the People's Republic of China ("PRC") represented the fastest growing number of visitors into the country, growing at 45.9% from last year. Tourists from PRC also made up the largest share of total tourist arrivals into the country at 21.6%.

To cope with the increased arrivals, a number of 4 – 5 star hotels are planned and completed recently. Xihu International Hotel recently launched a 508-room 5-star hotel. Intercontinental Hotel Group for instance, is on track to complete their 17-storey hotel in Sihanoukville. Marriott Hotel is also in talks to enter the Sihanoukville hospitality market.



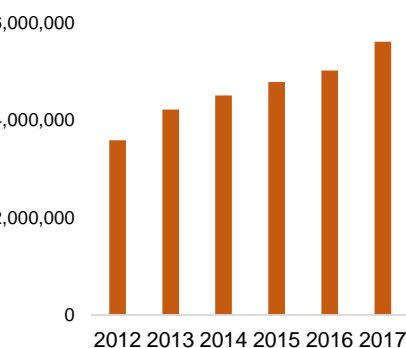
Source: SAC Advisors

Sihanoukville Condominium Supply



Source: CBRE Research, SAC Advisors

Cambodia Tourism Arrival



Source: Ministry of Cambodia

## Cambodia Foreign Ownership Limit

Under Article 44 of the Constitution, foreigners cannot own land in Cambodia. They can however acquire ownership rights in private units of co-owned buildings from the first floor up. This means that they cannot own ground floors or underground floors in co-owned buildings. The rules were set out in the Law on Providing Foreigners with Ownership Rights in Private Units of Co-Owned Buildings, promulgated in May 2010.

According to official documents, the sub-decree states that “legally qualified foreigners can have ownership rights in private units of a co-owned building not exceeding 70% of the total surface-size of all private units of the co-owned building.”

## Sales Update at D'Seaview

D'Seaview is Hong Lai Huat's first freehold mixed-use development venture in Cambodia, comprising 737 residential units and 67 commercial units. The four blocks of commercial segment include a mix of commercial shop space, retail units and a boutique hotel. It is conveniently located, and is just a 3 minutes drive away from Sokha Beach, 12 minutes from the Railway, 26 minutes from the SSEZ and 27 minutes from the Sihanoukville International Airport.

Sales Office of D'Seaview



Source: SAC Advisors



Source: Company data, SAC Advisors



Source: Company data, SAC Advisors



We understand that D'Seaview has already met the minimum 30% ownership criteria by locals, with locals owning about 60% of the units at the moment. All their biggest units – Duplex – have already been sold. Nearly 80% of the project's commercial and residential units have already been sold, while development work is on track for completion by June 2019.

The Company has also entered into a sales and purchase agreement to sell its 98-room hotel in its D'Seaview project in Sihanoukville, Cambodia for S\$15.7 million.

## Payment Terms (Contractual terms)

Hong Lai Huat adopts the progressive payment schedule for their D’Seaview property.

Schedule	Of total purchase price
Upon signing the booking form	5%
Upon signing sales and purchase agreement within 7 days from signing of booking form	15%
Piling works of the unit has been completed	15%
Reinforced concrete framework of the unit has been completed	25%
Brick walls of the unit has been completed	10%
Ceiling, and electrical wiring (without fittings) and the plumbing of the unit has been completed	10%
Door and window frame are in position, and internal plastering and tiling of the unit has been completed	10%
Swimming pool and landscaping work serving the housing project has been completed	5%
Upon handover notice	5%

Source: Company data, SAC Advisors

Based on our conversations with the local sales team, most of the buyers are now at stage 4 and 5 of the schedule. Our conversations with the on-site construction team also suggest that the construction progress is well on-track for completion in June 2019.

## Future Developments

Following the success of its first mixed-use development, D’Seaview in Sihanoukville, the Group signed a memorandum of understanding (“**MOU**”) with Cambodia’s premier investment and development company, The Royal Group of Companies, Ltd. (“**The Royal Group**”), to jointly develop a mixed-use development in Phnom Penh, the capital city of Cambodia.

## **Hong Lai Huat moves into Phnom Penh**

The development will be sited on a freehold plot of land of approximately 8,221 square metres, that is centrally located in the heart of Toul Kuok district, one of Cambodia's most affluent areas, and in close proximity to Cambodia's largest university, the Royal University of Phnom Penh.

Following the MOU, both parties will enter into a joint-venture agreement in the next 30 days where The Royal Group will inject ownership of the land while Hong Lai Huat will fund all development, operation and construction costs for the new development amounting to a sum equivalent to the agreed value of the land. Hong Lai Huat will also be responsible for all operational and personnel matters relating to the design, construction, marketing and sale of the completed development.

## Group Structure



Source: Company data, SAC Advisors



## Recommendation

Hong Lai Huat is trading at attractive FY17 P/BV of 0.28x and forward P/E of 0.9x, based on our earnings forecast for 2019. We value HLH at S\$0.51 per share after applying a 40% discount to its RNAV to factor in the lack of project in the pipeline although D'Seaview is expected to underpin the group's earnings in the next 2-3 years. The target price of S\$0.51 translates into a FY18 P/BV of 0.8x versus sector average of 0.9x. With a substantial potential share price upside of 149%, we maintain our BUY recommendation on Hong Lai Huat

We believe the market is currently undervaluing the stock. We have not factored in any contribution from potential property launch in Singapore, and a possible cooperation with a third party to expand its cassava business in arriving at our valuation.

<b>RNAV breakdown</b>	
Property development surplus (S\$ m)	59.97
NAV - as at end-Dec 2017 (S\$ m)	127.67
RNAV (S\$ m)	187.64
Shares outstanding (m)	221.93
RNAV per share (S\$)	0.85
RNAV discount (%)	40.0%
<b>Discounted RNAV per share (S\$)</b>	<b>0.51</b>
Current share price	0.163
Upside	211.2%
Implied P/BV (x) - FY18	0.79

Source: SAC Advisors

## Income Statement (\$\$ m)

	Fiscal Year Ended				
	FY2016	FY2017	FY2018F	FY2019F	FY2020F
<b>Revenue</b>	<b>10.3</b>	<b>12.6</b>	<b>52.7</b>	<b>105.1</b>	<b>29.9</b>
Cost of goods sold	-2.5	-6.2	-21.7	-45.8	-10.2
<b>Gross Profit</b>	<b>7.8</b>	<b>6.4</b>	<b>31.1</b>	<b>59.3</b>	<b>19.6</b>
Other income	0.5	1.8	0.5	0.5	0.5
Administrative expenses	-4.5	-6.2	-6.0	-6.0	-4.5
Distribution and selling expenses	-1.5	-1.6	-1.7	-1.7	-1.5
Other operating expenses	-0.1	0.0	0.0	0.0	0.0
Depreciation and amortization	-1.7	-3.5	-4.8	-4.9	-4.9
Finance costs	-0.7	-0.5	-0.5	-0.5	-0.5
Interest income	0.0	0.0	0.3	1.8	1.9
JV/associate income	0.0	0.0	0.0	0.0	0.0
Exceptional item	7.0	8.6	0.0	0.0	0.0
<b>Profit before tax</b>	<b>7.0</b>	<b>4.9</b>	<b>18.8</b>	<b>48.5</b>	<b>10.6</b>
Income tax	-0.7	-2.9	-3.8	-9.7	-2.1
Minority Interest	0.0	0.0	0.0	0.0	0.0
<b>Profit for the year/period</b>	<b>6.3</b>	<b>2.1</b>	<b>15.0</b>	<b>38.8</b>	<b>8.5</b>

## Balance Sheet (\$\$ m)

	Fiscal Year Ended				
	FY2016	FY2017	FY2018F	FY2019F	FY2020F
PPE	35.6	94.9	91.1	87.2	83.3
Investment properties	89.4	37.9	37.9	37.9	37.9
Others	0.0	0.1	0.1	0.1	0.1
<b>Total Non-Current Assets</b>	<b>125.1</b>	<b>132.8</b>	<b>129.0</b>	<b>125.1</b>	<b>121.2</b>
Development properties	18.3	15.1	24.8	28.9	0.0
Inventories	0.7	0.5	0.5	0.5	0.5
Trade receivables	7.8	0.6	2.1	4.2	1.2
Cash and short term deposits	6.7	2.0	16.4	74.0	85.8
Others	1.2	11.6	14.6	15.1	15.6
<b>Total current assets</b>	<b>34.8</b>	<b>29.8</b>	<b>58.4</b>	<b>122.7</b>	<b>103.1</b>
Trade payables	1.5	7.3	10.8	22.9	5.1
Loans and borrowings	1.7	3.3	3.3	3.3	3.3
Others	5.8	2.9	9.1	18.8	4.5
<b>Total Current Liabilities</b>	<b>9.0</b>	<b>13.5</b>	<b>23.2</b>	<b>45.0</b>	<b>12.9</b>
Deferred tax liabilities	14.9	16.4	16.4	16.4	16.4
Loans and borrowings	4.5	1.9	1.9	1.9	1.9
Convertible bonds	0.0	2.0	2.0	2.0	2.0
Others	0.7	1.1	1.1	1.1	1.1
<b>Total Non-current Liabilities</b>	<b>20.1</b>	<b>21.5</b>	<b>21.5</b>	<b>21.5</b>	<b>21.5</b>
<b>Shareholder's Equity</b>					
Share capital	94.6	94.6	94.6	94.6	94.6
Reserves	48.0	42.8	42.8	42.8	42.8
Accumulated (losses) profits	-11.8	-9.8	5.3	44.0	52.5
Total equity attributable to shareholders of the company	130.8	127.7	142.7	181.5	190.0
Non-controlling interests	0.0	0.0	0.0	0.0	0.0
<b>Total Equity</b>	<b>130.8</b>	<b>127.7</b>	<b>142.7</b>	<b>181.5</b>	<b>190.0</b>

## Cash Flow Statement (\$\$ m)

	Fiscal Year Ended				
	FY2016	FY2017	FY2018F	FY2019F	FY2020F
<b>Profit before tax</b>	<b>7.0</b>	<b>4.9</b>	<b>18.8</b>	<b>48.5</b>	<b>10.6</b>
Depreciation & amortisation	1.7	3.5	4.8	4.9	4.9
Interest income	0.0	0.0	-0.3	-1.8	-1.9
Interest expense	0.7	0.5	0.5	0.5	0.5
Change in working capital	-7.9	-6.2	-4.5	15.0	-0.6
Others	-7.8	-10.8	-4.0	-8.4	-0.7
<b>Net Cash (used in)/ from operations</b>	<b>-6.3</b>	<b>-8.2</b>	<b>15.4</b>	<b>58.6</b>	<b>12.8</b>
Purchase of PPE	-0.2	-0.3	-1.0	-1.0	-1.0
Others	0.8	2.8	0.0	0.0	0.0
<b>Net Cash (used in)/ from investing</b>	<b>0.6</b>	<b>2.5</b>	<b>-1.0</b>	<b>-1.0</b>	<b>-1.0</b>
Net change in equity	12.9	0.0	0.0	0.0	0.0
Net change in debt	-3.8	-1.7	0.0	0.0	0.0
Others	12.8	0.0	0.0	0.0	0.0
<b>Net Cash (used in)/ from financing</b>	<b>9.0</b>	<b>-1.7</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

## Ratios

	Fiscal Year Ended				
	FY2016	FY2017	FY2018F	FY2019F	FY2020F
<b>Profitability (%)</b>					
Operating profit margin	5.9%	-25.6%	36.1%	44.9%	30.9%
Profit before tax margin	67.5%	38.9%	35.6%	46.1%	35.5%
Profit after tax margin	60.9%	16.3%	28.5%	36.9%	28.4%
<b>Liquidity (x)</b>					
Current ratio	3.88	2.20	2.51	2.73	7.97
Quick ratio	1.76	1.05	1.42	2.08	7.93
Interest coverage ratio	0.90	-6.87	36.39	90.26	17.64
Net Debt to Equity	Net cash	2.5%	Net cash	Net cash	Net cash
<b>Valuation (x)</b>					
P/E	5.74	17.65	2.41	0.93	4.26
Core P/E	-50.67	-5.57	2.41	0.93	4.26
P/B	0.28	0.28	0.25	0.20	0.19
<b>Returns</b>					
Return on equity	5.3%	1.6%	11.1%	23.9%	4.6%
Return on asset	0.4%	-2.0%	10.9%	21.7%	3.9%
Dividend payout ratio	0.0%	0.0%	0.0%	0.0%	0.0%

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