Regina Capital Development Corporation
Member: Philippine Stock Exchange

STOCK REPORT

January 25, 2017

Recommendation

2016 was a transformational year for Sta. Lucia, at least in terms of finding another life line to support the company in the mid-term.

Thanks largely to its replenished land bank (close to a thousand ha. by end-2016), restructured business segments (increased contributions of commercial retail in the mix), as well as the gradual pay-off from positioning in next-wave cities (increased portfolio outside MM), it appears SLI is gearing for the long haul.

And RCDC has no problem commending these developments, seeing one positive news after another. SLI has shown no indication of being unable following up on these pipelines.

However, while the company wants us to wait for them at the end of the 5-year mark, RCDC still cautions over the near-term prospects of the firm - the interim segment between now and the full utilization of the acquired properties.

As SLI continues to hold on to large chunk of land on a slow roll out of projects, the efficiency and leverage of the company continues to suffer - and eventually, spilling into weakened profitability.

As of its last coverage, RCDC already raised impending operational issues faced by the firm. But it seems the market is now hinged on its long-term promise of improvement, as indicated by changes found in 9M16 results. Therefore, RCDC is maintaining its BUY recommendation and fair valuation of P1.40/share on SLI. The stock now poses a 32% potential upside from its last closing.

BUY

Target Price
PHP 1.40/sh.

+	Additional 937ha of land bank for future developments; Increasing contribution of retail segment; Roll-out of tourism projects; Prime properties outside of MM; Strong cash position from restructured tenant payment; Highly-liquid; Well-rounded business segments;
-	Slower take-up for residential segment; Increased competition across all segments: lower brand recall on residential, lower human traffic on malls; Limited price action, low trading volume;

Updates, Disclosures & News

+	As of end-December, SLI acquired a total of 937ha of land bank, via the combination of acquisitions and JV partnership. This is to lay the ground work for its long-term plans of increasing geographic nationwide depth and breadth, in its residential, commercial and tourism portfolio. Majority of these developments are adjacent to existing projects.
-	SLI generated a profit of P534.1mn for the first nine months of 2016, a minimal 4% increase from the comparable period last year. This is coming from also a modest revenue growth of 5% to close at P2.4bn for 9M16. The stable growth is attributed to the increase in both real estate and rental businesses of the company.
+	Also, SLI reported the launch of its tourism expansion plans, under the brand SotoGrande Hotels, via new developments in area such as Katipunan QC (23 storey); Fairview, QC (8-storey); Iloilo (6-storey); and Davao (20-storey). The SLI group already owns and operates existing hotel projects such as La Breza, Splendido Tower 1, Sta. Lucia Residenzes Monte Carlo, among others.
+	Further, SLI wants to penetrate, or expand presence in next-wave cities in the country for the mid-term. For Iloilo, SLI already launched several projects, including Greenmeadows (172ha), Metropolis Executive Village (51ha), Nottingham Villas (3ha) and SotoGrande Iloilo. This sums up to 262 ha of past and future developments in the province.
+	In September, SLI created a commercial business unit in order to spearhead its pipeline of commercial properties and expansion plans. These will include office spaces, retail and mall developments, industrial, institutions and tourism/leisure assets. SLI initially identified the following projects for construction: Sta. Lucia Business Center (Pasig); Neopolitan Business Park (Fairview); Greenmeadows (Iloilo); Ponte Verde (Davao); and Davao Riverfront Business Park (Davao). And further, the board approved a total of 4.18mn sq m of JV and 3.65mn sq m of land for the allocation of commercial development.

Company Description

STA. LUCIA LAND INC.

Sta. Lucia Land Inc (SLI) *has already established a track record in horizontal development, since listing in 1987, and began diversifying into vertical developments, housing construction, and marketing services. SLI also begun expanding its mall operations as a strategy to increase recurring income, as well as convert some of its commercial lots for sale into leasable spaces.*

As of December 2015, SLI is 83.28% owned by Sta. Lucia Realty and Development, Inc (SLRDI).

Stock Data

Last Price		PHP1.06
Performance (YTD)		-2.75%
52-week range		P0.73 – P1.30
Beta		0.57
Outstanding Shares		10,796.45mn
Market Capitalization		P9,125.4mn
Free Float Level		16.69%
Par Value		1.0
Sector		Property
Subsector		Property
Major stakeholders	Sta. Lucia Realty & Dev't Corp.	83.28%
Fiscal Year		31-Dec
Previous Rating	May 30,2016	BUY P1.40/sh

Board of Directors

Chairman	Vicente R. Santos
Director	Exequiel D. Robles Antonio D. Robles Aurora D. Robles Mariza Santos-Tan Orestes R. Santos Santiago Cua
Independent Directors	Jose Ferdinand R. Guiang Osmund C. De Guzman, Jr.

RCDC Research

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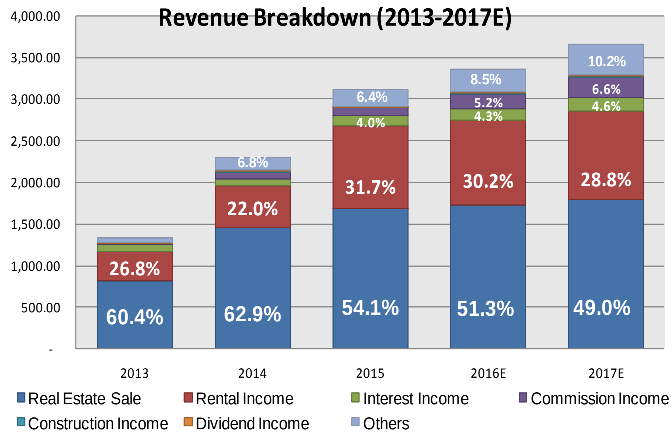
Revenue breakdown

- Sta. Lucia Land (SLI) is one of the pioneers in developing the townhouse & gated community subdivisions in the country, explaining the sheer number of simultaneous projects under the company. Land banking at cost was substantially cheaper before, and the company's previous strategy was to acquire huge amount of land and develop it by phases depending on the location's demand.
- The continuous rise in the number of property players in recent years divided market shares and stiffened competition. Plus, the introduction of mix-type developments (e.g. integrated townships) caused public preferences to blur, with a point against SLI on its failure to offer similar products.
- Remaining mostly a gated subdivision developer, SLI became a laggard in comparison to more aggressive companies within the industry.



- However, in terms of performance, SLI still registered positive year-on-year improvements. And in reaction to the changes in the industry, SLI took a more pro-active decision to boost its recurring income base, as well as engage in the tourism estate development.

Developments outside Metro Manila

- The breakdown of managed projects outside the capital includes:

  -84 projects amounting 1,924.6ha in Region 4A (Cavite, Laguna, Batangas, & Rizal);

  8 project worth 788.7ha in Region 3 (Bulacan, Nueva Ecija, Tarlac, Pampanga, Dagupan, Cabanatuan, & Zambales);

  8 projects for 428.2ha in Region 7 (Cebu);

  6 projects for 315.0ha in Region 6 (Iloilo and Bacolod);

  8 projects totaling 299.2ha in Region 11 (Davao);

  200ha project in CAR (Baguio);

  7.3ha project in Region 1 (Pangasinan);

  And, 2 projects totaling 6.1ha in Region 4B (Palawan);
- Total projects outside Metro Manila numbered 233, covering 9,127.2ha.

Residential segment on high inventory

- Growth in RE sales came via horizontal and vertical (condominium, condotels) projects in both Metro Manila and outside regions.
- RE Sales is the bread & butter of the firm, with as high as 60.4% of the revenue mix in 2012. But despite growing at a +9% CAGR from 2012 to 2015, percentage of RE Sales dropped to 54.3% in 2015 to give way to a boosted retail and commercial segments. On a yearly basis, RE receipt captured a +16% growth in 2015, even if the contribution to the mix is gradually being reduced.
- For 2017E, RCDC estimates RE Sales percentage in the top line mix to further reduce to 49.0% at P1.9bn. A lower share in contribution does not imply slower growth, as RCDC sees at least another +4% growth in the business for 2017E.

- Further, the board of SLI approved its entry into several JVs that aims to develop 14 new projects on an area of 162,054 sq m.
- The same board acquired rights to 22,212 sq m additional land bank, in areas like Palawan, Laguna, and Cavite.
- As a whole, SLI has a total of 35 on-going projects (including Mesilo Nueva Vida, Greenwoods Phase 2, & Sta. Lucia Residences – Santorini, among others) and 29 new projects in the pipeline (such as Cebu Com Tower 1 & 2, Sta Lucia Residenze Tower 3-5, among others).

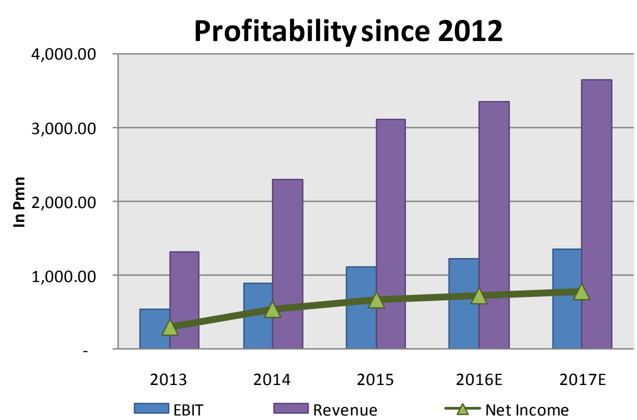
Boosted Recurring Segment

- SLI's main business strategy & growth plan is to increase Rental earnings contributions, and expand its leasable, commercial portfolio.
- And one of the most significant decisions in 2014 was to cut the middle man in the transaction between SLI and its mall occupants. The middle man, Sta. Lucia East Comm'l Corp (SLECC), will instead manage the properties.
- The decision boosted cash by +1,808% in 2015, and +281% in the first 2 months of the accord implementation in October 2014. RCDC estimates cash reserves to normalize entering 2016, with organic growth coming from rent adjustments & occupancy rate increase.
- Another decision was to replace classification for 35 remaining commercial lots-for-sale into commercial lots-for-lease, which chains down cash flow into the company for a longer period of time without any material changes in assets.
- Lastly, mall expansion is one of the strategies included in its medium to long-term plans, with particular focus on Sta. Lucia East Malls. SLI has also introduced retail components to newer developments.
- In term of top line contribution, Rental Income from mall tenants has increased significance, from the 26.8% contribution in 2013 to 31.7% in 2015, with P984mn. RCDC expects this to reach as high as 36.0% by 2016E. Rental receipt also registered one of the strongest growth, with a 36% CAGR since 2012 and a 95.2% annual growth.

Other Income sources

- Other sources of income turned significant by the end of 2015, starting with commissions coming from marketing efforts of SLI units. Commissions registered a 128.3% CAGR since 2012 and a 35.5% year-to-year improvement. While Construction and Dividend Income both showed 26% growth, respectively. As per share in the top line, not one of the other sources provided more than 5% of the total mix.

Profitability



- Despite laggard performance in comparison to aggressive growth of peers, SLI still held its own. There have been no extraordinary gains registered between 2013 and 2015 to offset earnings figure. EBIT and EBITDA are surprisingly stable over the course of the period, with 23.5% and 24.3% y-o-y growth, respectively. And this is coupled by the same level with 25.4% and 25.6% CAGR since 2012. Profit, likewise, was kept stable on a 23.2% annual increase and 30% CAGR since 2012. However, profit estimates for 2016E was kept at a conservative +7.7% to account for its transition phase into a significant retail player, as well as to consider the slowdown in the property industry itself.

Ratios	2013	2014	2015	2016E	2017E
Return on Equity	2.48%	4.68%	5.32%	5.50%	5.30%
Earnings per share	0.03	0.06	0.08	0.08	0.09
Profit Margin	22.61%	23.90%	21.78%	21.70%	21.27%
Asset Turnover	0.08	0.13	0.15	0.13	0.13
Return on Assets	1.75%	3.08%	3.16%	2.82%	2.77%
Assets to Equity	1.42	1.52	1.68	1.92	1.98
Altman's Z-Score	1.08	1.48	1.58	1.38	1.29
Price to Earnings	20.87	12.46	10.32	11.18	10.47
Price to Book Value	0.52	0.58	0.55	0.61	0.55
Graham Multiplier	10.82	7.26	5.67	6.87	5.81
Book Value per share	1.12	1.37	1.42	1.50	1.59
Dividend Yield	-	-	-	-	-

- Despite the acquisition of close to a thousand hectares of land bank by end-December, performance-based indicators for RCDC are still pegged to improve at a slightly modest rate, as RCDC sees a slower conversion of these properties into income generating projects – true to SLI's type of development.
- By end-December, SLI was able to secure 937ha of both acquired properties and JV's for land, in order to replenishing its (own land bank for its long-term prospects. Location include NCR (1.95ha), Davao (228.24ha), Region 4A (325.34ha), and Iloilo (153.57ha), among others.
- Using price-based indicators, valuation over the last 3 years saw a significant improvement, cutting P/E from 20.9x in 2013 to 10.32x as of end-2015. Though SLI is likely to go up a bit to 11.18x P/E by the full year 2016, RCDC sees this improvement to be sustained moving forward.
- In 2015, SLI sold 400mn shares, increasing O/S shares to 8.9bn.
- In 2014, 2.2bn shares, covering P900mn advances, were issued back by parent-firm SLDRI to the firm, forming SLI's new treasury shares. This decreased O/S shares for SLI from 10.8bn in 2013 to 8.5bn in 2014. Currently, SLI is now 83.28% owned by SLDRI.
- The increase in O/S shares from the infusion caused equity returns to almost double within the year (2014), and has been sustained ever since, with 5.5% in 2016E.

Sales to Inventories of Diversified Property Firms

Ratios	2011	2012	2013	2014	2015
ALI	1.74	1.34	3.17	2.04	2.09
CPG	2.33	5.53	2.35	1.54	0.96
DD	-	-	-	1.44	0.29
ELI	0.14	0.15	0.15	0.27	0.24
FLI	0.25	0.46	0.44	0.54	0.58
GERI			0.09	0.19	0.38
HOUSE	-	2.87	3.18	3.36	3.00
MEG	2.53	0.93	0.74	0.70	0.48
RLC	0.70	0.48	0.48	0.47	0.42
SMPH	-	-	7.04[1]	3.63	2.93
SLI	**-**	**-**	**-**	**0.18**	**0.21**
VLL	1.08	1.10	1.36	1.41	1.37

[1]SMPH used to be an independent property arm of the SM group, but was folded into SMDC beginning 2014.

- The sheer number of units & sq m of leasable land folded under the company capped Sales-to-Inventory ratio into lower levels, as compared to those with one or two project roll-outs per year.

Key Financial Data in PhP billions	2015
Ave. Total Assets	19,605
Ave. Total Debt	2,973
Ave. Total Equity	12,216
Net Income After Tax[1]	676
Interest Expense	137
Asset Income[2]	813
Debt/Equity Ratio	0.24
Cost of Debt	4.60%

[1] Does not include Comprehensive Income
[2] Asset Income = NIAT + Interest Expensed

Limlingan Financial Model©

ROE = ROA + D/E * (ROA - Cost of Debt)

LFM Inputs	2015
Return on Assets[3]	4.15%
Debt/Equity Ratio	0.24
Cost of Debt	4.60%
ROA - CD	-0.45%
Return on Equity	**4.04%**

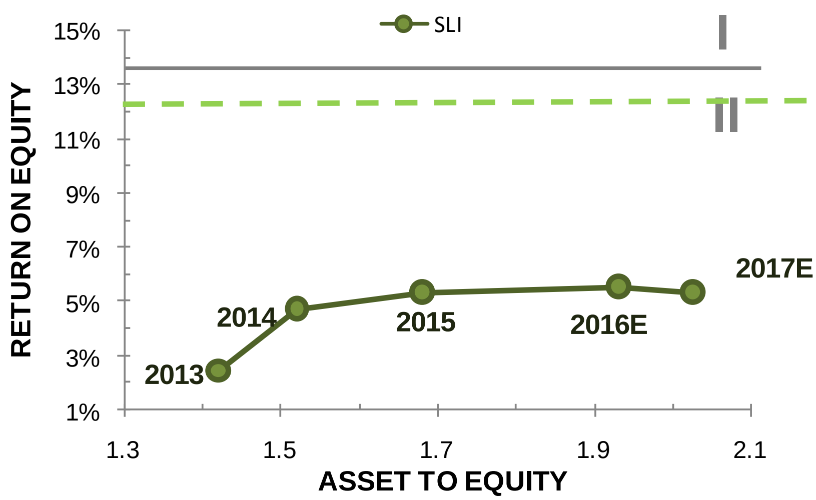
Case 1: Improve Efficiency by 20%	
Return on Assets[3]	4.98%
Debt/Equity Ratio	0.24
Cost of Debt	4.60%
ROA - CD	0.38%
Return on Equity	**5.07%**

Case 2: Increase Leverage by 20%	
Return on Assets[3]	4.15%
Debt/Equity Ratio	0.29
Cost of Debt	4.60
ROA - CD	-0.45%
Return on Equity	**4.01%**

Case 3: Cut Debt Cost by 20%	
Return on Assets[3]	4.15%
Debt/Equity	0.24
Cost of Debt	3.68%
ROA - CD	0.47%
Return on Equity	**4.26%**

Highlighted items denote changed inputs
[3] In this model, ROA is computed as:
ROA = Asset Income / Ave. Total Assets

FINANCIAL PERFORMANCE



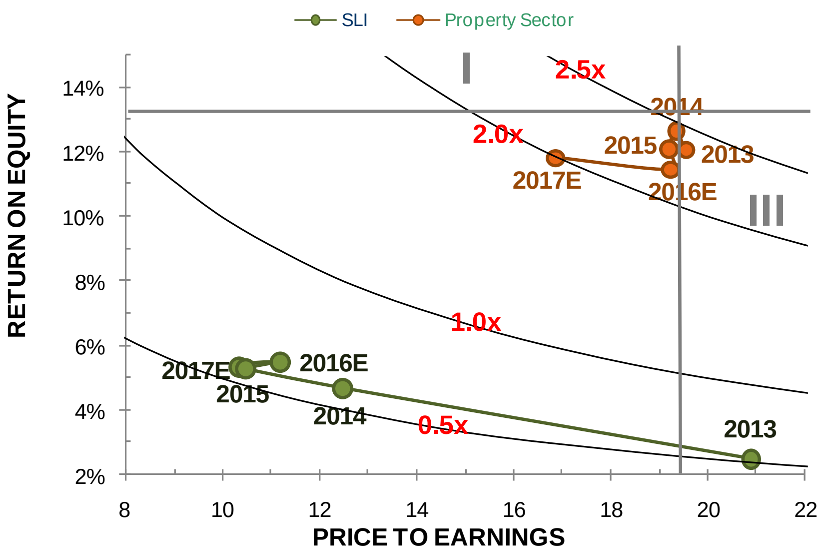
Leverage vs. Profitability

- Sta. Lucia Land (SLI) remains a laggard in profitability within the industry, with equity returns trailing behind peers at single-digit levels.
- Moving forward, profitability still seen to remain largely stagnant, as most acquired land bank and signed JV's won't completely materialize until the mid-term. 2016E and 2017E ROE's are placed within 5.5% and 5.3%, respectively. And anticipated surge likely to show by 2018.
- Leverage for SLI is not far from the industry-average, but still placed on the lower end of the spectrum, at about 1.3x to 2.0x A/E. (against the industry's 2.3x). 2016E and 2017E A/E to expand from acquisitions and land banking activities done in the year.
- The historical low profitability on modestly growing leverage of SLI makes it into a stable – albeit verging on stagnant – firm, with low financial risk, but at the same time, low financial returns.
- The solid gridlines represent the 3-year Asset to Equity and ROE averages of companies in the Exchange, while the dotted lines represent the aggregate property industry. Due to the outlier nature of the firm, quadrants 1 and 2 are the only one shown.

Legend:

I - Higher Returns, Lower Financial Risk	*IV - Higher Returns, Higher Financial Risk*
II - Lower Returns, Lower Financial Risk	*III - Lower Returns, Higher Financial Risk*

VALUATION ISOQUANTS



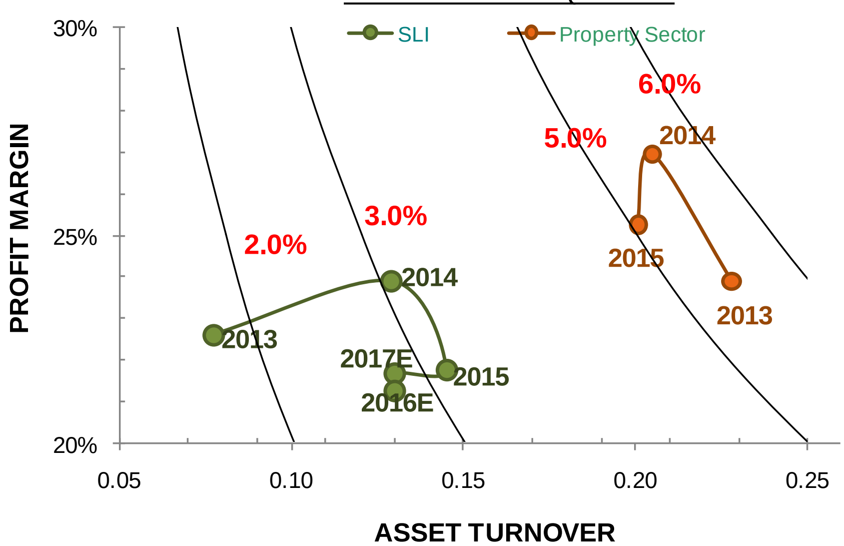
Perception vs. Profitability

- Consistent with its relatively improving financial performance, participants have also improved valuation for SLI over the years, with decreasing P/E from an expensive 20.9x in 2013 to a forecasted 11.8x by 2016E.
- However, the low profitability of SLI makes its supposedly cheap valuation into an underperforming stock against the Exchange.
- Further, SLI is also an outlier to the industry, settled at less than its book value, while peers are trading within the range of 2x to 2.5x respective book values.
- Isoquant lines (0.5x, 1.0x, 2.0x and 2.5x) represent Price to Book values, while gridlines represent the average P/E and ROE of companies in the PSEi in the last 3 years.

Legend:

I – Undervalued (Bargain)	*IV – Fairly valued*
II – Fairly valued (Underperforming)	*III – Overpriced*

OPERATING ISOQUANTS



Efficiency vs. Profitability

- SLI was one of the earlier property firms in the country, with reliance to the older version of land development involving homogenized housing units on gated communities, before the idea of township eventually caught up.
- The recurring income is derived from stand alone projects such as the Sta Lucia mall.
- This translated to a historically stable but low margin between 20% and 30%. SLI has not entered into an integrated township concept that includes a retail component to the residential segment inside an inclusive property space. This placed a cap on margins as the integrated approach exhibited boosted income for other peers in the industry.
- Asset T/O is still below industry average, at a slower asset return of 3% from the 5% average.

Daily chart as of January 24, 2017

- On a 3-month chart, SLI entered a downward channel after losing steam, following a break out in early December. The stock has tried breaking channel resistance since.
- Indicators also showed bearish signals, since MACD crossed the signal line in late December, and continued to show selling pressure. Likewise, RSI remains flat and nearing oversold signals.
- A strong support is spotted on the 200-d MA (0.99), and incidentally its channel support. If breached, this could send SLI into its year-long support range of 0.946 to 0.912.
- SLI likely to tread the channel (currently at 1.096 to 0.99) within the near-term, or unless an external catalyst puts an upward/downward pressure on the stock.
- **Trade the range.**

SLI v PSEi v VLL
Source: www.bloomberg.com

Recommendation Guide

Recommendation Guide		Expected Performance in 6-12 months
BUY	The stock is a bargain relative to the PSEi or its peers; the stock has significant long-term upside	Projected Gain > 10%
HOLD	Neutral; the company's fundamentals are good, but interested buyers should wait and consider buying other stocks with better upside.	+/- 10%
SELL	Take profits or cut losses; the stock does not have much upside so investors should close their position and look for bargains.	Projected Loss > 10%

Financial Ratios

Return on Equity	Shows how much profit a company generates with the money its shareholders have invested.
Earnings per share	The portion of a company's profits allocated to each outstanding share of common stock.
Profit Margin	Measures how much earnings a company actually keeps after expenses.
Asset Turnover	The amount of sales generated for every peso of assets
Return on Assets	Reflects a company's efficiency at using its assets to generate earnings.
Asset to Equity	Shows the company's financial leverage. It is an indicator of the overall financial stability of a company.
Altman's Z-Score	An indicator of a firm's financial stability; It calculates the odds that a company will become bankrupt. If: Z > 3.0, Safe Zone; 1.80 < Z < 3.0, "Grey" Zone; Z < 1.80, Distress Zone (high likelihood of bankruptcy)
Price to Earnings	Reflects how much investors are willing to pay per dollar of earnings.
Price to Book	Reflects how many times book value investors are willing to pay for a share of the company.
Graham Multiplier	P/E Ratio x P/B Ratio; Benjamin Graham prefers companies that have a Graham Multiplier below 22.5
Book Value per share	A per share estimation of the minimum value of a company's equity.
Dividend Yield	Shows how much a company pays out in dividends relative to its share price.

Technical Analysis Term/s

Fibonacci Retracement	Potential retracement of a security's original move in price. It uses horizontal lines to indicate key areas of support or resistance (23.6%, 38.2%, 50%, 61.8% and 100%).

Limlingan Model: ROE = ROA + D/E * (ROA – CD)

Basic Assumptions:

ROE = Return on Equity
ROA = Return on Assets*
D/E = Debt to Equity
CD = Cost of Debt

If ROA > CD, then ROE > ROA
If ROA < CD, then ROE < ROA

**using Asset Income*

Can be used to undertake the following financial analyses:

- Pinpoint areas of weak and strong financial management
- Answers 'what if' in terms of the impact of the ROE
- Prepare financial plans which start with the ROE targets and end with specific, financial targets such as maintaining operating expenses and leverage
- Better assign areas of responsibilities to financial officers
- Create 'equity centers' where general managers have both asset and debt management responsibilities

CEO
Maximize ROE for its shareholders

COO
Improve ROE through operational efficiency or ROA

CFO
Improve ROE by maximizing debt (reduce leverage or cost of debt)

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