

Regal International Group

Lack of near term catalysts

SINGAPORE | REAL ESTATE | UPDATE

We did a site visit to Regal International Group's major developments in Kuching in end November, including the already completed Tropics I (almost fully sold out), and several projects under construction - 72 Residences (Tropics II), Orchard Suites/Mall, and Corporate Park. These are some of our post-visit thoughts.

Lack of near term catalysts as major projects are still some way off completion

While it remains to be seen if 72 Residences (Tropics II) and Tropics City (Tropics III) can follow in the successful footsteps of Tropics I in Kuching, the benefits of potential buoyant sales, even if realised, will only be realised towards 2017 as the projects' construction complete. Another major project, Corporate Park, is also slated to complete in 2018. Sales for Corporate Park have yet to fully kick off and demand is uncertain. These three projects make up close to c.55% of our recalculated RNAV.

Long Term outlook and residential property saleability remain strong

Using the price-to-income ratio as a gauge of housing affordability in Sarawak, we make a comparison table of the affordability of housing in Sarawak versus other states in Malaysia. Empirical research by the United Nations Centre for Human Settlement and World Bank found that a median home price to median household income of 3 times was considered to be the global norm and signals a well-functioning housing market.

Sarawak's median multiple stands at close to the acceptable ratio of 3 and according to housing statistics pulled from the Department of Statistics and National Property Information Centre Malaysia, Sarawak's housing ranks as one of the most affordable compared to other states in Malaysia currently. This is despite a CAGR of c.8% for the Sarawak House Price Index since end 2009. Not surprisingly, Kuala Lumpur and Penang ranks as one of the most expensive in the country.

Area	Monthly household median income (RM)	Annual median income (RM)	Median All-House price (RM)	Median Multiple Affordability
Terengganu	3,777	45,324	250,000	5.5
Kuala Lumpur	7,620	91,440	490,000	5.4
P.Pinang	4,702	56,424	295,000	5.2
Sabah	3,745	44,940	230,000	5.1
Pahang	3,389	40,668	200,000	4.9
Kelantan	2,716	32,592	157,740	4.8
MALAYSIA	4,585	55,020	242,000	4.4
Perak	3,451	41,412	180,000	4.3
Perlis	3,500	42,000	181,000	4.3
Johor	5,197	62,364	260,000	4.2
Selangor	6,214	74,568	300,000	4.0
N. Sembilan	4,128	49,536	188,000	3.8
Sarawak	3,778	45,336	164,667	3.6
Kedah	3,451	41,412	140,000	3.4
Malacca	5,029	60,348	180,000	3.0
Singapore 5-room BTO HDB (SGD)	5,800	69,600	384,000	5.5

Source: Department of Statistics Malaysia 2014, National Property Information Centre (NAPIC) Malaysia 2014, HDB Singapore, PSR

29 December 2015

NEUTRAL (Downgraded)

CLOSING PRICE (S\$, 21 Dec 15)	0.165
FORECAST DIV	0.00
TARGET PRICE	0.24
TOTAL RETURN (%)	45.5

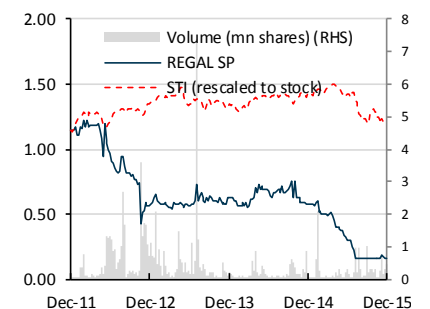
Share Data

Outstanding shares (mn)	200.1
Market cap, mn (S\$ US\$)	33.0 / 23.5
3 mo avg daily volume (000s)	56.6

Top shareholders

	%
Ikram Mahawangsa Sdn	44.5
Stratland Properties	10.2
Chung Jye Su	8.1
Pak Kiong Wong	5.0

Free float (approx.)	29.5		
Change (%)	1 Mo	3 Mo	1 Yr
Company	6.5	(2.9)	(71.6)
STI	(0.3)	1.8	(13.8)



Key Financials (RM m)

FYE Dec	FY13	FY14	FY15F	FY16F
Revenue	125.7	95.3	127.5	140.3
EBITDA	31.7	16.4	(9.6)	(5.2)
NPAT (adj.)	22.3	(17.9)	(16.0)	(5.9)
EPS (sen)	17.2	(12.6)	(8.0)	(3.0)
PER (x)	9.3	N.A.	N.A.	N.A.
P/BV (x)	3.5	0.7	0.9	1.0
ROA (%)	20.7	(6.6)	(5.1)	(2.0)
ROE (%)	75.8	(12.4)	(13.3)	(5.6)

Source: Bloomberg

Valuation Method

RNAV (50% discount)

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For a more meaningful comparison, historically, the median home price/median household income in the U.S. is around 2.6x, according to a study done by Zillow (an online real estate database company) published on Forbes. Using Singapore's 5-room Housing Development Board (HDB) BTO flat as a gauge for the affordability of public housing in Singapore, our median multiple stands at 5.5, according to statistics from HDB.

Change in accounting treatment of revenue to reduce earnings volatility

Currently, Regal's revenue and cost of sales for projects in East Malaysia (the bulk of their projects) are recognised using the complete contract method. This means that bulk of the revenue from a sold unit can only be recognised upon completion of construction and when the ownership of the unit transfers to its new owner. Changes to the accounting rules FRS 115 "Revenue from Contracts with Customers", starting January 2017 mean that developers can switch to recognising revenue progressively, according to the progress of construction works, starting from 2017. This new initiative would be a fairer representation of the profitability of property developers and results in less lumpy earnings.

Current Valuation close to NTA value (net of goodwill). Downgrade to Neutral with lack of near term catalysts.

Regal's last closing price of S\$0.165 trades at close to its NTA value of c.S\$0.175 (excluding RM39m goodwill), assuming an exchange rate of 1SGD:3RM.

With the change of analyst, we downgrade our call from BUY to NEUTRAL with a downwardly revised target price of S\$0.24 from S\$0.43. Our call and target price factor in a steeper 50% discount (original 30%) to Revalued Net Asset Value (RNAV) due to the gestation period for sales to materialize and construction to complete. Uncertain demand for Corporate Park and Airtrollis, as well as the illiquid nature of the shares are also factors for the steeper discount to valuation. Lastly, the challenging outlook for the Group's precision business, coupled with the lack of near term catalysts for the property business arm over the next year, leads us to a Neutral call for the company as we expect FY16 to be similarly loss-making (albeit showing an improvement from FY15) before things turn around thereafter.

Orchard Residences



Regal's Sales Booth at a Shopping Centre



Construction Site for 72 Residences (Tropics II)



Development project	Location	Est. completion	Saleable area (sqft)	Total units	% sold	ASP per sqft (RM)	RNAV Surplus (RM mn)	
Airtrollis	Negri Sembilan	2016 (Phase 1)	897,538	1,104	28%	375.0	84.8	
Corporate Park (80%)	Sarawak	2018 (Phase 1)	12,377,120	384	5%	22.5	74.1	
Tropics III	Sarawak	2018	453,273	604	28%	675.3	69.4	
72 Residences	Sarawak	2017	128,124	72	45%	535.5	13.2	
Orchard City - 50%	Orchard Residences	Sarawak	2014	254,097	120	90%	550.0	2.4
	Orchard Contempo 3	Sarawak	2015	55,039	12	25%	417.0	3.0
	Orchard Mall	Sarawak		93,566	NA	0%	483.5	7.9
	Orchard suites	Sarawak		264,187	NA	0%	483.5	22.4
Tondong Heights	Sarawak	2015 (Phase 1) 2016 (Phase 2) 2018 (Phase 3)	498,537	228	53%	96.1	7.9	
Lundu	Sarawak	2017	68,000	34	0%	298.0	7.1	
Matang	Sarawak	2016	208,302	48	80%	350.0	5.1	
Unitech	Sarawak	2015	46,609	18	83%	306.2	0.8	
Ashraf Avenue 2	Sarawak	2018	67,703	19	90%	254.0	0.6	
Haziiq Ria	Sarawak	2015	33,599	22	95%	432.0	0.3	

Revalued Net Asset Value (RNAV) Surplus	299.0
Less: Financing costs for project duration	(56.2)
Post-tax RNAV	182.1
+ Total Equity as at 3Q15	144.5
- Net of Goodwill (RM mn)	(39.3)
Revalued Net Asset Value, RNAV (RM mn)	287.3
Number of share outstanding (mn)	200.1
RNAV per share (RM)	1.4
RNAV per share (S\$)	0.48
Target discount to RNAV	50%
Target Price (S\$)	0.24

The relevant assumptions for RNAV calculation are as follows:

1. Corporate tax rate at 25% (Malaysia)
2. Financing interest rates at 8% (Mid-range of existing bank overdraft interest rates of 7.6%-8.6%), as disclosed in Annual Report 2014
3. Financing period for 2 years
4. SGD to MYR conversion at 1SGD-3RM

Financials

Income Statement

Y/E Dec, RM mn	2013	2014	2015F	2016F	2017F
Total Revenue	125.7	95.3	127.5	140.3	154.3
Cost of Good Sold	(85.9)	(63.1)	(99.5)	(116.4)	(115.7)
Gross Profit	39.8	32.2	28.1	23.8	38.6
EBITDA	31.7	16.4	(9.6)	(5.2)	7.3
Operating Income	32.0	9.0	(14.4)	(9.5)	2.6
Pretax Profit	30.8	(12.9)	(16.0)	(6.1)	6.2
Net Income after taxes	22.3	(17.9)	(16.0)	(5.9)	5.2

Per share data

Y/E Dec	2013	2014	2015F	2016F	2017F
P/NTA (x)	3.5	1.0	1.3	1.5	1.6
P/BV (x)	3.5	0.7	0.9	1.0	1.0

Cash Flow

Y/E Dec, RM mn	2013	2014	2015F	2016F	2017F
Pretax profit	30.8	(12.9)	(16.0)	(6.1)	6.2
Depreciation	0.8	1.6	4.4	4.9	5.3
Change in Working Capital	(25.1)	(20.0)	(38.1)	3.9	(6.2)
Cash from Op. Activities	5.6	(12.0)	(10.8)	(1.1)	1.2
Cash from Investing Activities	3.2	22.7	(0.6)	(1.0)	(1.0)
Cash from Financing Activities	(6.4)	13.0	5.6	(7.6)	6.9
Net Change in Cash and cash eq.	2.3	23.6	(5.7)	(9.7)	7.1

Source: Company, Phillip Securities Research (Singapore) Estimates

*Forward multiples & yields based on current market price; historical multiples & yields based on historical market price.

Balance Sheet

Y/E Dec, RM mn	2013	2014	2015F	2016F	2017F
ASSETS					
Cash and Short Term Invs	1.3	27.7	22.0	12.2	19.3
Acc Receivable - Trade, Net	56.6	78.9	69.9	77.4	79.0
Total Inventory	19.0	30.3	29.8	23.3	28.9
Development Properties	19.5	50.1	106.7	106.7	106.7
Total Current Assets	97.2	190.9	232.5	223.7	238.0
Property/Plant/Equipment	5.3	26.5	34.0	35.0	36.0
LT Investments - Other	8.1	22.7	19.1	19.1	19.1
Goodwill	0.0	39.3	39.3	39.3	39.3
Total Assets	108.0	270.6	315.2	306.4	320.6
LIABILITIES AND EQUITY					
Total Payable	46.1	55.5	64.6	69.8	69.4
Bank Borrowings and Fin Lease	2.2	16.5	31.9	35.1	38.6
Other Current Liabilities	19.7	24.1	65.6	65.6	65.6
Long Term Debt	2.0	13.7	15.3	15.4	30.9
Total Liabilities	78.5	126.8	193.9	199.0	215.9
Common Stock	0.0	133.1	133.1	133.1	133.1
Total Equity	29.5	143.8	121.2	107.4	104.8

Key Ratios

Y/E Dec	2013	2014	2015F	2016F	2017F
ROE (%)	75.8	(12.4)	(13.3)	(5.6)	4.9
ROA (%)	20.7	(6.6)	(5.1)	(2.0)	1.6
Gross margin (%)	31.7%	33.8%	22.0%	17.0%	25.0%
Net profit margin (%)	17.8%	-18.7%	-12.6%	-4.3%	3.3%
Fully diluted EPS (cts)	17.2	(12.6)	(8.0)	(3.0)	2.5
Fully diluted P/E (x)	9.3	N.A.	N.A.	N.A.	20.3
Gearing	14.3	20.9	38.9	47.0	66.3

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