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28 August 2015

# DoubleDragon Properties Corp (DD PM)

## Positive | Riding the consumption and retail boom



### Company profile

- Listed on the PSE in April 2014, Double Dragon (DD) is a commercial and residential developer in the Philippines focused on building provincial retail malls (70% of recurring income) and Metro Manila commercial spaces (30%). Recurring income forms 90% of the company's total income and DD only earns 10% of total income from affordable housing segment.

### Reasons for meeting

- DD is targeting for 100 malls in the provincial area of the Philippines over the next five years (from 3 operating malls currently), as well as two major development of Meridian Park (4.8ha integrated development) and Ortigas Tower in Metro Manila (office space). We are interested to know not only how such large-scale projects could be managed and financed, but also the impact on DD's stock valuation, which has risen by 80% YTD.

### Catalysts

- Target leasable area of 1m sqm by 2020 with 70% from provincial malls:** According to Euromonitor, the Philippine retail market is projected to grow at 3.8% CAGR over 2014-19. Under the CityMall brand, DD is well positioned to ride this trend by building 100 malls by 2020. In addition, its focus on building commercial spaces in Metro Manila (30% of targeted leasable area) also provides an opportunity to participate in the growing BPO sector.
- Small-sized, standard convenience malls with two-thirds of space occupied upon completion:** By employing a cookie-cutter mall design, the time to completion of a mall is substantially reduced to 7-8 months and operations can be stabilized in another 4-5 months. This allows DD to manage its high capex by generating cash flows from rentals faster than peers. Furthermore, its partner and shareholder networks and businesses make up at least two-third of net leasable area (NLA) upon completion – ensuring yield on cost of 12% at completion, steadily rising to 14-16% in 3-5years.
- Established and experienced shareholders, business partners:** DD's key shareholders are Mang Inasal (37% – Philippines' second largest fast food brand) and Jollibee (37% – Asia's largest fast food chain). For its CityMall expansion, DD (66% stake) has partnered with SM Prime – bringing in years of experience and network in securing land sites, development, execution, and financial capabilities.

### Conclusion

- Positive outlook; 40% upside:** We estimate an equity value of PHP41.1bn or PHP18.4/sh for DD's 97 new CityMalls, Meridian Park and Ortigas Tower (assume all funded by debt and preference shares). Combined with the current book value of PHP3.7/share, our back-of-the-envelope RNAV for DD is ~PHP22.1/sh. Assuming a discount of 15% applied to its new projects' RNAV, we could conservatively assume fair value of PHP19.3/sh for DD – 40% upside from the current level.

### REPORT AUTHORS

Tata Goeyardi

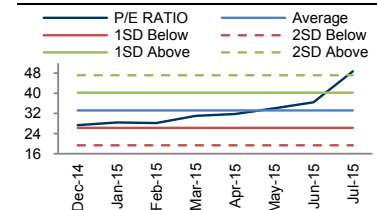
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### Trade statistics

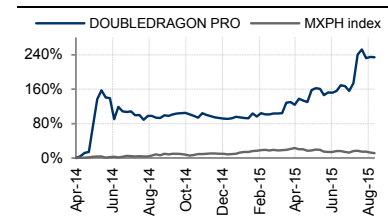
Price (PHP)	13.80
52-week high (PHP)	13.98
52-week low (PHP)	7.20
Market cap (USD mn)	646.49
3m avg daily value (USD mn)	0.54
EPS Best est:	2015 N/A
	2016 N/A
Shares outstanding (mn)	2,229.73
Float (%)	25.64

### DD PM P/E chart



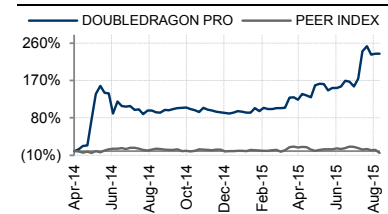
Source: Bloomberg

### DD PM vs. MXP index



Source: Bloomberg

### DD PM vs. peer group



Source: Bloomberg

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### Risks

- **Inability to secure prime lots:** Scarcity of prime lots with an area of 1ha or more coupled with rising land costs could delay land acquisition plans and expansion for CityMall – whether it is in the provincial area or Metro Manila. Land prices could rise faster than expected (currently management assumes costs at US\$200/sqm).
- **Funding concerns:** DD is looking to add additional 97 malls by the end of 2020. Although supported by financially strong shareholders, DD needs to manage its capex and cash flows efficiently, as well as complete its malls on time. We expect the company to use bank loans and possibly preference shares to fund its expansion plans (no equity raising in the near-to-medium term).
- **Construction delay and vacancy rates:** DD is targeting the construction of each CityMall in 7-8 months and stabilization in another 4-5 months (90-100% occupancy in 12 months). Any delay in construction and inability to fill up remaining spaces (excluding 2/3<sup>rd</sup> of anchor tenants from key shareholder network) could delay cash inflow and affect expansion status.
- **Ability to raise rents:** Upon completion, 2/3 of leasable space is taken by Jolibee and SM groups – interested parties. While this presents a huge advantage to DD's expansion plans, it remains to be seen whether DD could continue to raise rents on sustainable basis as guided by management (inflationary 3-5% pa).
- **Economy and consumption slow down:** Philippines economy only grew 5.6% YoY in 2Q (lower than consensus of 5.7%) whilst consumption grew by 6.2% YoY. The economy in the region is vulnerable to the slowdown of China and expected US rate hike. PHP has devalued 2.5% in the past one month time.

Fig 1 - Global peer comparison

Ticker	Name	Market Cap (USD mn)	6m Avg Daily Val. (USD mn)	P/B Trail (x)	P/E Trail (x)	P/E FY16E (x)	ROE (%)	Div Yield (%)	Net D/E (%)
DD PM	DOUBLEDRAGON PRO	646.49	0.55	13.22	48.83	NA	39.34	NA	0.58
PLAT TB	PLATINUM GROUP	400.68	0.98	4.06	23.18	NA	NA	1.18	Net Cash
CPN TB	CENTRAL PATTANA	5,477.93	7.91	4.62	24.65	20.11	19.89	NA	0.29
RLC PM	ROBINSONS LAND	2,537.24	1.70	2.14	22.77	17.53	9.74	NA	0.32
NIRO IJ	NIRVANA DEVELOPM	210.23	0.54	1.54	N.A.	18.35	(3.91)	NA	0.40
3699 HK	WANDA COMM-H	28,039.62	63.65	1.16	6.09	7.88	19.03	2.39	0.60

Source: Bloomberg

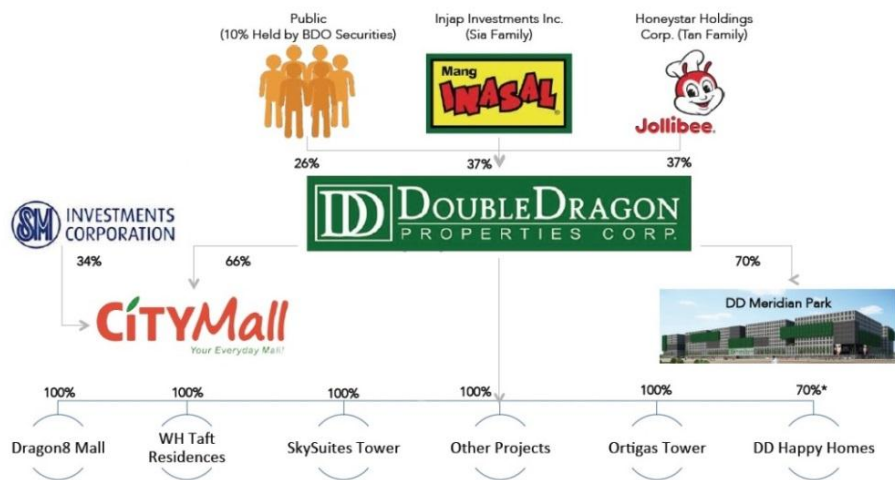
### The Business

- Listed on the PSE in April 2014, Double Dragon (DD) is a commercial and residential developer in the Philippines focused on building provincial retail malls (70% of recurring income) and Metro Manila commercial spaces (30%). Recurring income forms 90% of the company's total income and DD only earns 10% of total income from affordable housing segment
- **Established shareholders:** DD was established in 2009 as a wholly owned real estate arm of Injap Investments Inc. In July 2012, Injap Land Corp was renamed DoubleDragon Properties Corp and structured as a 50/50 Joint Venture between:
  1. Injap Investments Inc, headed by Chairman Edgar 'Injap' Sia II, Founder of Mang Inasal Philippines Inc (the second largest food brand in the Philippines, with 459 branches and a turnover of \$245m), and

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- Honestar Holdings Corp, headed by Chairman Tony Tan Caktiong who is also the Founder and Chairman of Jollibee Foods Corp (Asia’s largest fast food chain, with 3,001 branches and a turnover of \$2bn).
- Listed in 2014:** DD was listed on the Philippine Stock Exchange (PSE) in April 2014, raising PHP1.16bn at an offer price of PHP2/sh, which accounts for 26% of the company’s shares outstanding. The rest 74% was equally shared by Sia Family and Tan Family. In addition, DD went into a 66/34 JV with SM Investments, the well-known mall developer/operator in Philippines, to co-develop provincial malls (under CityMall brand). In the Meridian Park project, DD is also the controlling shareholder with 70% stake (remaining stake held by a local partner).

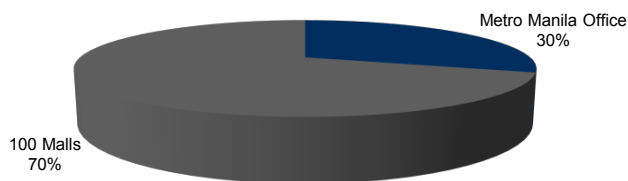
**Fig 2 - DD’s current ownership structure**



Source: company

- 5-year goal of 1m sqm of leasable space (“20/20 Vision”):** the Company’s goal is to develop 1,000,000sqm of leasable space divided mainly into two geographical portions: Metro Manila (30%) and provincial (70%). The provincial projects pertain to its target of 100 CityMalls. Currently, 57% of the land needed for development has been secured and the group has exceeded its target of securing 300,000sqm of leasable space.

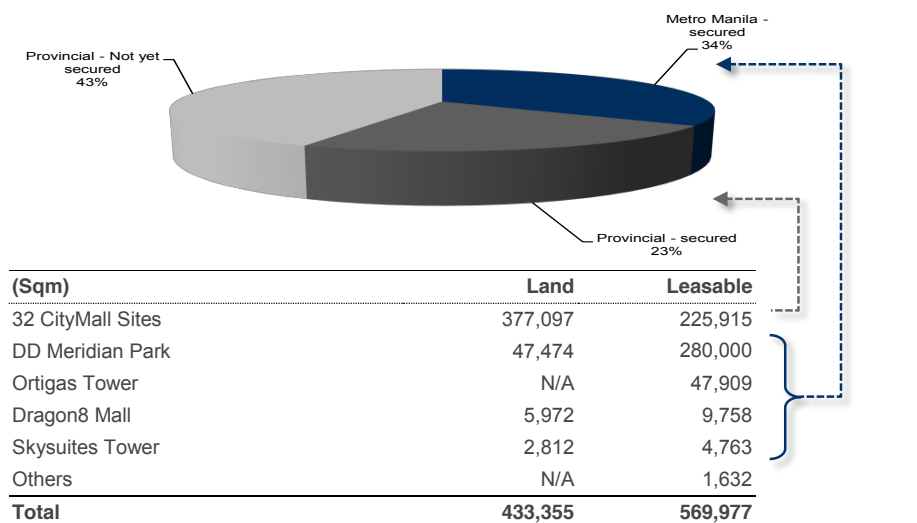
**Fig 3 - 20/20 Vision: 1m sqm of leasable space**



Source: Company

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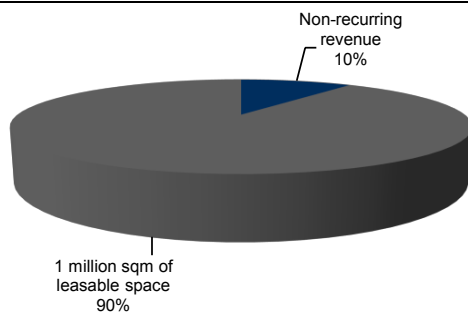
**Fig 4 - 20/20 Vision: Land secured status by area**



Source: Company

- 20/20 Vision a part of DD’s focus on recurring income streams:** DD explains that this plan will put a focus on recurring income, which is estimated to contribute 90% of revenue. DD believes this has three main benefits:
  - Upside potential in property appreciation/escalation,
  - Lower risk profile due to less uncertainty, and
  - A steady future dividend yield.

**Fig 5 - DD’s expected revenue sources**



Source: Company

### CityMall: Capitalizing on an Asian community mall phenomenon

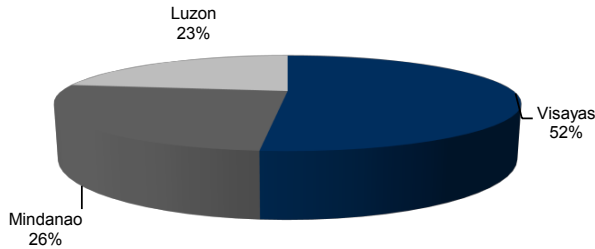
- CityMall positioned as a community mall:** Community malls differ from destination malls, as described below.

Destination Mall: Variety	Community Mall: Convenience
Larger	Much smaller
Located in fringe areas	Located in city centres
Offers a variety of brands/choices	No duplication of tenant mix

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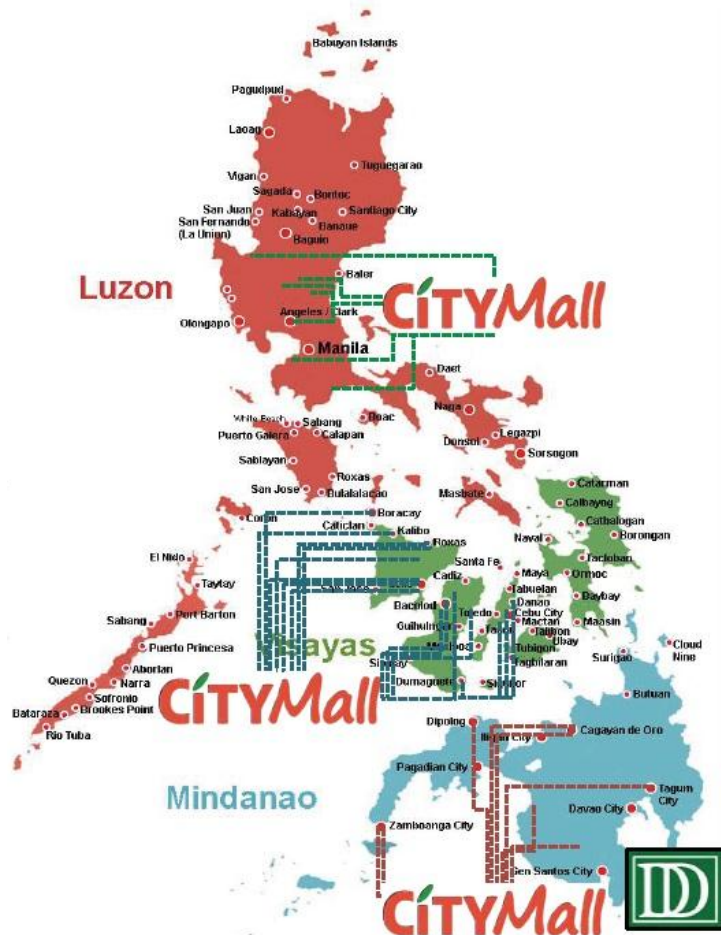
- **Prime location of malls:** CityMall sites secured by DD are located in the prime 'city centers' of second and third tier provincial cities. These sites are within the daily natural movement of the general population and DD expects high daily footfall.

**Fig 6 - Breakdown by location of DD's first 32 secured CityMalls**



Source: Company

**Fig 7 - Map of the secured CityMall sites**



Source: Company

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- Stable and large, well-known core tenants:** Upon completion, two-third of CityMall’s leasable area will be leased to Jollibee (food) and SM (non-food brands), which are related companies of DD. It expects the remaining one-third area to be leased to unrelated parties carrying strong non-competing brands that the company assesses to be a suitable fit for the market of CityMall and which are capable of rolling out nationwide.

**Fig 8 - Tenanted by strongest retail brands in the country**



Source: Company

Notably, the lease term for supermarkets (Savemore) is 15 years and Jollibee’s rental rate is set as a percentage of gross sales, as per standard fast food leases.

- Aggressive expansion plans:** In line with its 20/20 Vision, DD intends to develop 100 provincial CityMalls in total. The company prefers to acquire the land, but where needed, may enter into a 70% JV with current land owners as an incentive to let DD acquire the land. DD may also lease the land where the previous options are not available.

Notably, within 16 months of listing, the company has:

- Secured 32 CityMall sites (leasable area: 225,915sqm)
- Opened 3 CityMalls
- Plans to open 2 CityMalls

DD is targeting completion of 25 CityMalls by Dec 2015 (all opened by 1Q16).

Management is confident of meeting this target. By employing a cookie-cutter mall design, the time to completion of a mall is substantially reduced to 7-8 months and operations can be stabilized in another 4-5 months. **Short completion of malls is the fundamental basis of this business model – leading to a faster revenue cycle and payback period, coupled with rising asset prices.**

- Established and well-known JV partner:** CityMall is a Joint Venture (JV) between CityMall (66%) and SM Prime (34%). The larger SM group has a mall land bank of 2.4m sqm and a total of 67m sqm overall. Evidently, SM group is no stranger to the development of malls and this could benefit DD greatly in terms of expertise.
- High occupancy rates at newly opened CityMalls:** We note that occupancy rates of the first two CityMalls opened are 99% at Arnaldo-Roaxs and 83% at Consolacion-Cebu.

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### Other recurring income sources: Metro Manila

- **DD Meridian Park, a mix of office and retail:** DD Meridian Park is a 4.8ha mixed-use development located in the rising EDSA Extension business district in the Bay Area beside PAGCOR Entertainment City. DD is currently in phase 1 of construction and expects to turnover four BPO towers and a retail strip with a total leasable area of 130,000sqm in 2018. Phase 2 is to be completed in 2020, with a leasable area of 150,000sqm. Management expects the total leasable area of 280,000sqm to yield an annual rental of \$57m, or \$17/sqm per month by 2020.

According to JLL Research, in May 2015, the Bay Area has a 1% vacancy rate with rental rates increasing 10% YoY.

Fig 9 - Master plan of DD Meridian Park



Source: Company

- **Ortigas Tower:** Ortigas Tower is a Metro Manila 40-story Grade-A office with total leasable space of 47,909sqm. With expected completion in 2018, it is projected to deliver rentals at PHP800-850psm by that time.

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**Fig 10 - Ortigas Tower**



Source: Company

**Other properties: a mix of recurring and non-recurring income**

**Fig 11 - Other property details**

The Skysuites Tower	Dragon8 Mall
<ul style="list-style-type: none"> <li>Acquired : September 2014</li> <li>Location : EDSA, Quezon City, MM</li> <li>Status : 45% Completion (June 2015)</li> <li>Total Units : 977 Residential Lofts 69% Sold</li> <li>Leasable (sqm) : 4,673sqm Commercial/ Office</li> <li>Unsold Units : 306 units (14,238sqm)</li> <li>Price/sqm : \$2,900</li> <li>Inventory : \$41m</li> </ul>	<ul style="list-style-type: none"> <li>Acquired: May 2014</li> <li>Opened: June 2015</li> <li>Location: C.M. Recto, Divisoria, Manila</li> </ul> <p><b>Leasehold Rights for Sale (16 years)</b></p> <ul style="list-style-type: none"> <li>Sellable Area: 4,165sqm (412 stalls)</li> <li>Area Sold: 1,492sqm (144 stalls)</li> <li>Ave. Price: \$5k/sqm</li> <li>Add'l Fee: P600 + P250 CUSA per sqm</li> <li>Receivables: \$4m</li> </ul> <p><b>Leasable Space</b></p> <ul style="list-style-type: none"> <li>Leasable Area: 5,148sqm</li> <li>Leased Area: 4,278sqm (83% Leased)</li> <li>Ave. Lease: \$17/sqm</li> </ul>

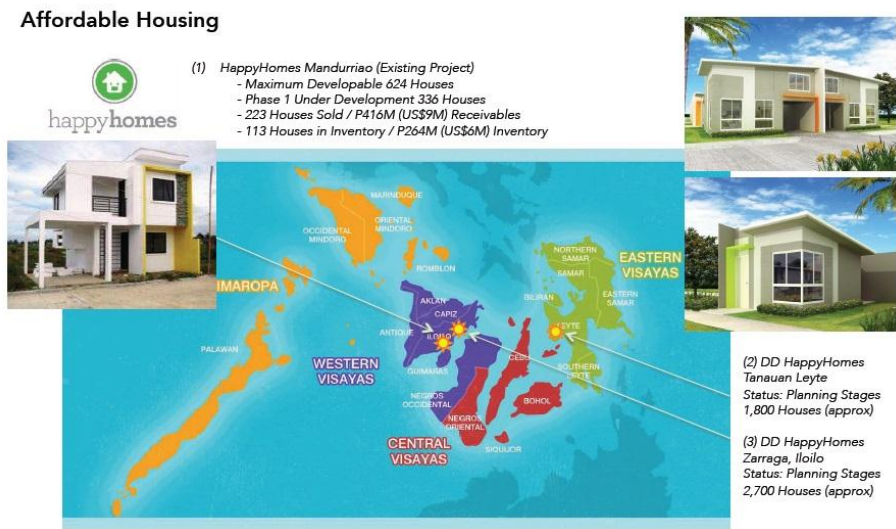
Source: Company

**DD's non-recurring income source: Affordable housing**

- Affordable housing to address shortage:** There is a 5.5m housing backlog in the Philippines. DD will be launching DD HappyHomes through its 70% owned subsidiary that will serve as its horizontal affordable housing arm. These affordable house-and-lot packages will cost from \$10,000 up to \$40,000. The current affordable homes project has been planned mainly in the Visayas region.

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**Fig 12 - Affordable housing**

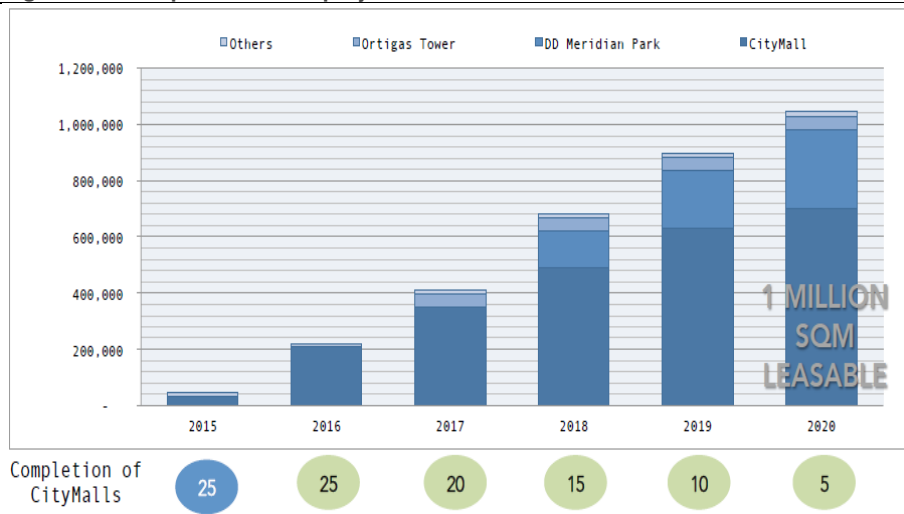


Source: Company

### Capital expenditure and sources of funding

- **Targeting 1m sqm of leasable area in 2020:** DD has opened 3 CityMalls currently and is targeting a total of 25 malls by the end of year. By 2020, all 100 City Malls will be in operation. Together with the completion of DD Meridian Park and Ortigas Tower, DD will have 1m sqm of leasable area in its portfolio.

**Fig 13 - Build-up schedule of projects**



Source: Company, RCML

- **Expected capex for CityMall expansion:** We estimate that a total effective capex of PHP32bn will be needed for the development of all 97 CityMalls, Meridian Park and Ortigas Tower. **Management expects 70% of CityMalls to be wholly owned, while 11% would be developed through JVs with local partners, and another 19% will be on lease terms.** In total, CityMalls will take up 74% of the capex, while Meridian Park and Ortigas Tower will take up the remaining 26%.

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**Fig 14 - Capex of projects (at project level)**

Provincial Retail		Metro Manila Office	
CityMall		Ortigas Tower & DD Meridian Park	
Land cost (\$)	2,400,000	<b>DD Meridian Park - Phase 1</b>	
Building cost (\$)	5,600,000	Est. Capex (\$)	128,888,889
Est. Capex/Mall (\$)	8,000,000	Leasable Space (sqm)	130,000
		Est. Capex per sqm (\$)	991
Est. Wholly owned malls	69	<b>DD Meridian Park - Phase 2</b>	
Est. Capex (\$)	552,000,000	Est. Capex (\$)	148,717,949
Est. JV Malls	16	Leasable Space (sqm)	150,000
Est. Capex (\$)	89,600,000	Est. Capex per sqm (\$)	991
Est. Leased Malls	12	<b>Ortigas Tower</b>	
Est. Capex (\$)	-	Est. Capex (\$)	47,138,305
		Leasable Space (sqm)	47,909
		Est. Capex per sqm	984
Estimated total Capex (\$)	641,600,000	Estimated total Capex (\$)	324,745,143

Source: RCML, Company

- Sources of capital to fund future capex:** DD prefers to raise capital through debt funding at fixed interest rates over a long-term period of seven or more years. At the same time, it aims to maintain a maximum D/E ratio of 2.3x. Thereafter, the company could raise capital through the issuance of preferred shares, when needed. We estimate completed projects could generate PHP22.8bn income, which could be used to fund future projects (rollover). However, there would still be an estimated funding deficit of PHP9.2bn. As at 2Q15, DD had a net gearing ratio of 1.6x; if all PHP9.2bn were to be funded by debt, the D/E ratio could exceed the 2.3x cap. Hence, we could expect some preference shares to be issued to fund development plans over the next five years. Management has mentioned that it favors the use of debt and preferred shares to fund development vis-à-vis normal equity placement.
- Current debt funding:** DD has taken up credit lines/term loans with 12 local banks. About 85% of its outstanding debt is long-term in nature (7-year corporate notes). All corporate notes are unsecured and were issued at fixed interest rates.

**Fig 15 - Previous debt tranches**

October 2014: \$164m Corporate Notes	May 2015: \$111m Corporate Notes
<ul style="list-style-type: none"> <li>Interest Rate: 6.183%, fixed</li> <li>Duration: 7 years</li> <li>Lender: 8 Banks</li> </ul>	<ul style="list-style-type: none"> <li>Interest Rate: 6%, fixed</li> <li>Duration: 7 years</li> <li>Lender: BDO</li> </ul>
July 2015: \$33m Corporate notes	
<ul style="list-style-type: none"> <li>Interest Rate: 5.984%, fixed</li> <li>Duration: 8 years</li> <li>Lender: 1+ Lenders</li> </ul>	

Source: Company



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### Valuations

- High yield on cost to underpin valuations:** Each CityMall costs ~\$8m for land and construction, has a net leasable area of 7,000sqm and a guidance rental of \$13/sqm/month at the beginning. Based on an EBITDA margin of 95% (most costs covered by extra CUSA), CityMall delivers a yield on cost as high as 12%, which climbs further to 14-16% in 3-5 years based on 5% p.a. rental growth. Leasing arrangements are carefully designed to ensure the occupancy and rental levels for all of the malls. As contracted, SM Prime would have the first ROFR to lease space and Robinson Land has the second ROFR for tenancy.

**Fig 16 - CityMall metrics**

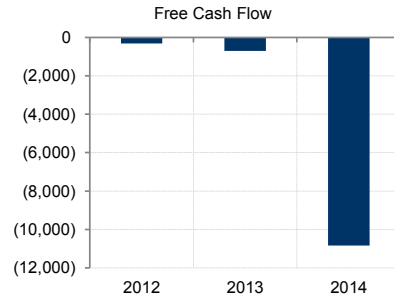
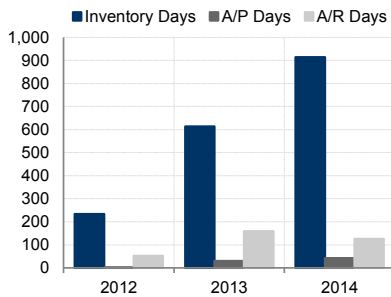
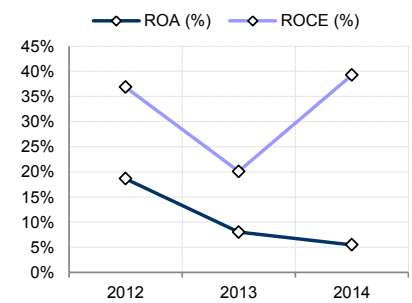
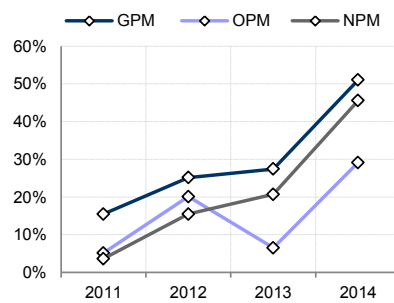
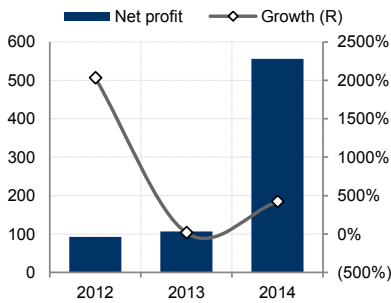
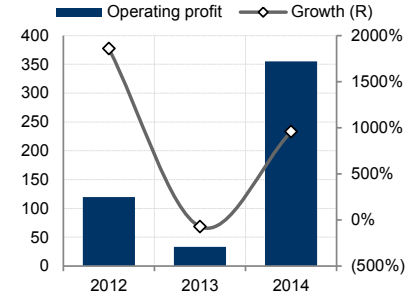
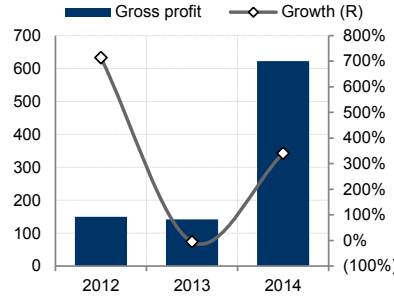
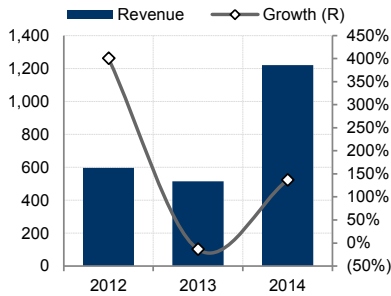
Item	
Number of malls	100
Average Lot size (h.a.)	1.2
Average Gross Leasable Area (sqm)	7,000
Average Land Cost (\$/sqm)	200
Average Construction Cost (\$/mall)	560,000
Average Rental Revenue (\$/mall/month)(excl CUSA)	1,000,000
Average Rental Revenue (\$/sqm/month)	13
Rental Escalation (% p.a.)	5%
Est. yield on cost	12%

Source: Company

- Significant growth in RNAV to boost valuation:** We have used a 9% cap rate for CityMalls and a 7% cap rate for Central Manila offices. We've also made the assumption that all the developments will be funded by debt and internal sources. At 10% discount rate, we derive an equity value of PHP41.1bn or PHP18.4/sh for DD's 97 new CityMalls, Meridian Park and Ortigas Tower (assuming all are funded by debt and preference shares). Combined with the current book value of PHP3.7/share, our back-of-the-envelope RNAV for DD is ~PHP22.1/sh. Assuming a discount of 15% applied to its new projects' RNAV, we could conservatively assume fair value of PHP19.3/sh for DD – ~40% upside from current level.

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### At a Glance



Source: Bloomberg

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