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FIRST SPONSOR GROUP LIMITED

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SINGAPORE | REAL ESTATE | INITIATION

21 September 2020

- Unrecognised property development revenue of S$586mn with another S$1.95bn worth of gross development value (GDV) to be unlocked, equivalent to 5 years of sales.
- Property financing loan book grew at 19% CAGR in the past 5 years. These securitised loans offer recurring income at low to mid-teens returns. We are estimating loan book growth of around 8% for FY20e and FY21e.
- Initiate coverage with BUY and target price of S$1.65.

Company Background

Listed on the mainboard of the SGX on 22 July 2014, First Sponsor Group (FSG) is a property developer (FY19 revenue: 50%), owner (22.5%) and financier (27.5%). It operates in China (FY19 assets: 58%), Europe (40%) and Australia (2%). Hong Leong Group Singapore (35.8%) and Tai Tak Estates (44.1%) are its two controlling shareholders.

Investment Merits

1. **1H20 unrecognised revenue equates to 1-2 years of sales; GDV to unlock is equivalent to 5 years of sales; demand for Dongguan's residential properties exceeds expectations.** Unrecognised revenue as of 1H20 from development properties amounted to S$586mn. FSG holds GDV of S$1.95bn that has yet to be unlocked. Buying sentiment in Dongguan exceeded FSG's expectations after business resumed in late February 2020. Residential units at most of its projects that were launched in April have been almost fully sold. Another residential block in The Pinnacle was launched for pre-sales on 14 July and has sold more than 85%.
2. **Humen TOD to become one of FSG's largest development projects.** FSG won the bid for a mixed-use development on 29 June at RMB6.6bn (c.S$1.3bn) in a joint venture with China Poly Group (CPOLYZ CH, Not Rated) and China State Railway Group (390 HK, Not Rated). The land will be developed into a transit-oriented development with more than 1mn sqm Gross Floor Area (GFA). FSG has a c.17% effective equity interest in the JV.
3. **High recurring income for its Chinese property financing business plus double-digit growth in securitised loan book.** FSG charges interest rates of low to mid-teens p.a. for its property financing business. LTV of its loan book is 40-60%. PRC loan book grew at a CAGR of 19% from 2015 to 2019. 1H20 loan book grew 12% YoY to RMB2,295mn (S$459mn). To date, FSG has not incurred any bad-debt losses in property financing. We are estimating loan book growth of around 8% for FY20e and FY21e.

Key risks

1. **Worst may not be over for the hotel portfolio; stunted recovery is expected.** As of 30 June 2020, all temporarily closed hotels except Bilderberg Garden Amsterdam had re-opened. FSG's well-diversified portfolio is situated in areas where most hotels saw a greater recovery in August (Netherlands portfolio ex-Amsterdam/Rotterdam and Germany). However, the Netherlands has seen a resurgence of Covid-19 cases lately as new cases in September exceeded its peak in April. We are expecting a stunted recovery for the hotel portfolio.

We initiate coverage with a BUY rating. Our target price is S$1.65, based on its historical 30% average discount to RNAV. This implies a potential total return of 33.6% and dividend yield of 1.75%.

The report is produced by Phillip Securities Research under the 'Research Talent Development Grant Scheme' (administered by SGX).

BUY (Initiation)

LAST CLOSE PRICE	SGD 1.250
FORECAST DIV	SGD 0.021
TARGET PRICE	SGD 1.650
TOTAL RETURN	33.6%

COMPANY DATA

BLOOMBERG CODE:	FSG SP
O/S SHARES (MN) :	912
MARKET CAP (USD mn / SGD mn) :	840 / 1141
52 - WK HI/LO (SGD) :	1.39 / 1
3M Average Daily T/O (mn) :	0.02

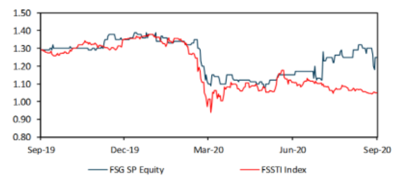
MAJOR SHAREHOLDERS (%)

REPUBLIC HOT & RES LTD	31.8%
FIRST SPONSOR CAPITAL LTD	31.4%
TAI TAK ASIA PROPERTIES LTD	12.7%

PRICE PERFORMANCE (%)

	1MTH	3MTH	1YR
COMPANY	0.9	9.7	(0.8)
STI RETURN	(2.0)	(5.1)	(17.8)

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Dec (S$'	FY18	FY19	FY20e	FY21e
Gross Rev	277,361	319,164	354,939	447,449
Gross Profit	161,500	189,035	195,732	231,312
EBITDA	133,707	201,719	165,741	186,046
PATMI	108,467	163,610	125,821	144,781
P/NAV (x)	0.63	0.69	0.55	0.51
P/E (x)	7.66	6.28	7.51	6.53
ROE (%)	8.20	10.23	7.35	7.87

Source: Company, PSR

VALUATION METHOD

RNAV (30% discount)

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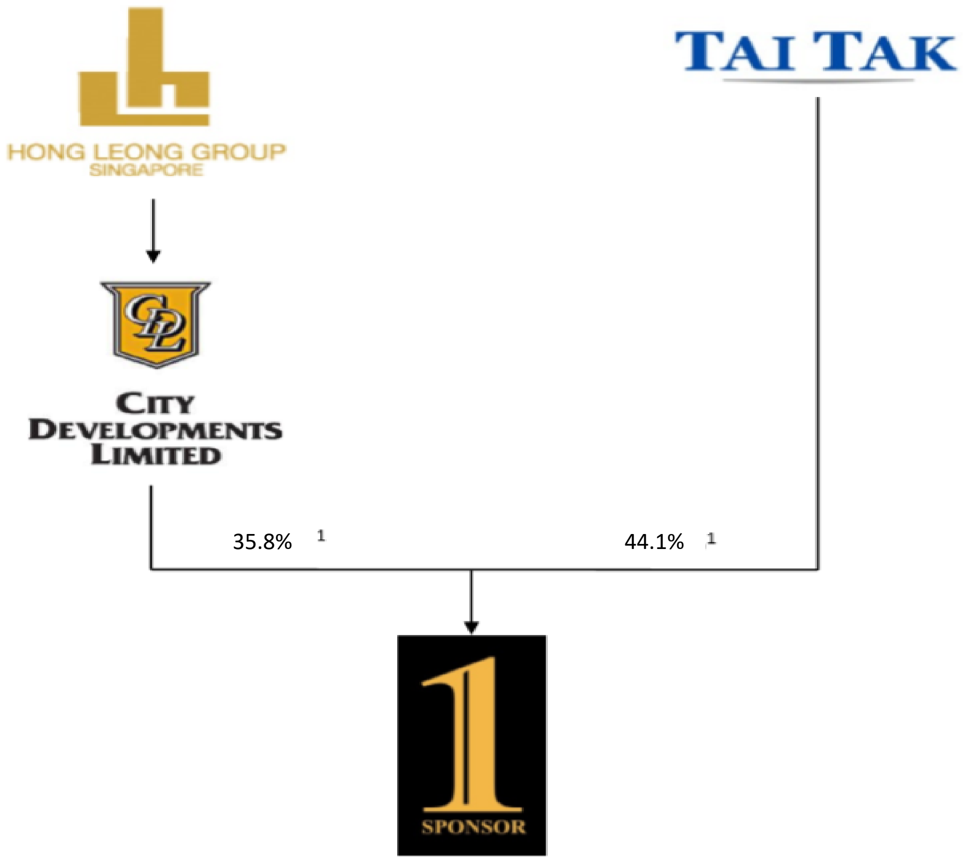
About First Sponsor Group Limited

FSG has been listed on the mainboard of the SGX since 22 July 2014. The group is supported by controlling shareholders, the Hong Leong group of companies, through its shareholding interest in City Developments Limited (CIT SP, Current: S$8.09,TP: S$11.68), and Tai Tak Estates Sendirian Berhad, both recognised property-holding companies in Asia.

Figure 1: Its two key stakeholders - Hong Leong Group and Tai Tak - own 80% of FSG



[1] As of closing on 18 August 2020

Source: Company

Hong Leong Group is a globally diversified company with gross assets of over S$40bn, owned by the Kwek family. It employs some 30,000 people around the world. The Group's four core businesses are property development, hotels, financial services, and trade & industry.

Tai Tak is a family-owned (Ho family) private company incorporated in Singapore in 1954. It invests in a wide range of businesses, including plantations, listed and private equities, property holding and development. The Tai Tak family is one of the largest shareholders of United Overseas Bank (UOB SP, ACCUMULATE, TP: S$20.40). The family was a co-founder of the bank with the Wee family and was the second largest shareholder until the merger of UOB and Overseas Union Bank.

Revenue

FSG has three operating segments: **Property Development, Property Holding and Property Financing**.

Property Development:
- 6 mixed (residential and commercial) developments in China (Chengdu and Dongguan);
- 1 residential and 2 commercial developments in The Netherlands (Rotterdam) and
- 1 hotel and residential development in Australia (Sydney)

Property Holding:
- 18 hotel operations and 6 office investments in China, Netherlands, Germany and Italy

Property Financing:
- Property financing services in China, The Netherlands, Germany and Australia

Property Development is historically its largest revenue contributor. In FY19, it contributed 50%, followed by Property Financing's 27% and Property Holding's 22%. The bulk of FSG's income is derived from its operations and assets in the PRC (FY19: 58%) and Europe (40%). In 2015-2019, profit after tax and net asset value grew at CAGRs of 19% and 10% respectively. Property Financing has the highest gross profit margin (Fig. 20).

Figure 2: Revenue contributions by segment (S$mn, 2015-1H20)

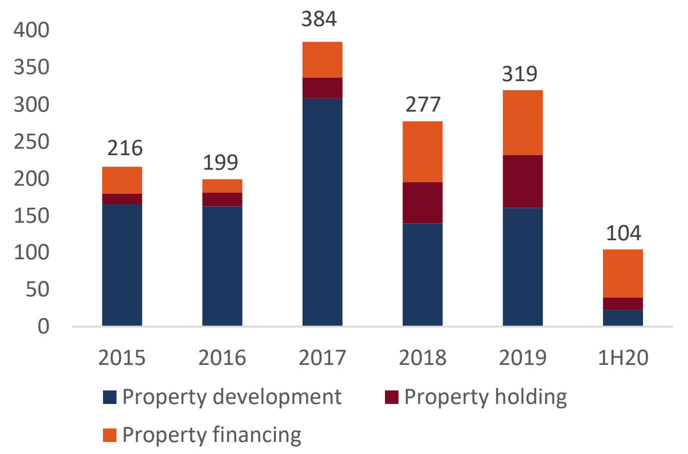


Figure 3: Total assets by geography

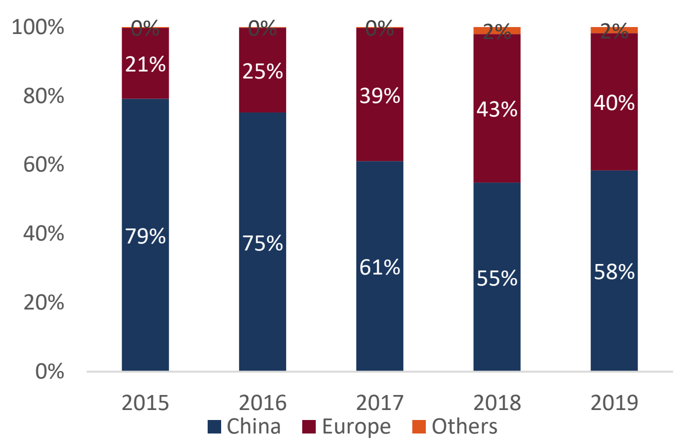


Figure 4: Profit After Tax (S$mn, 2015-1H20)

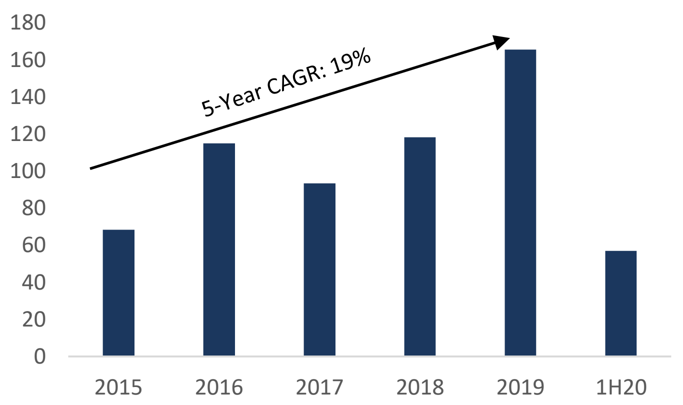
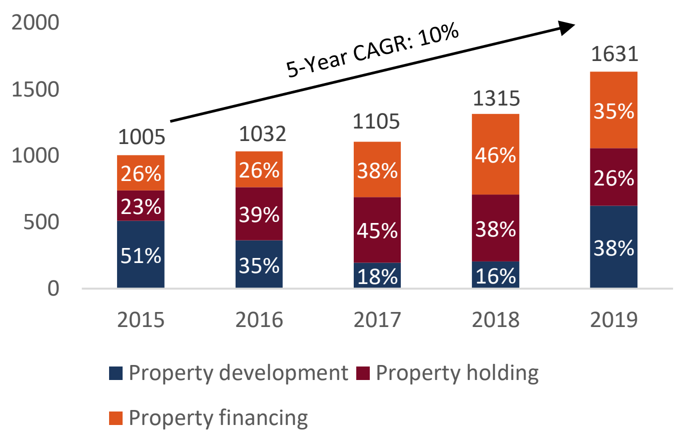


Figure 5: Net asset value by segment (S$mn, 2015-2019)



Source: Company

I. Property Development

Presently, FSG is working on the Millennium Waterfront, Dongguan portfolio and The Terraced Tower in The Netherlands**.** Its Dongguan portfolio consists of Star of East River (SoER), Emerald of the Orient (EoO), The Pinnacle, Skyline Garden and the Humen Transit Oriented Development (TOD) Project.

Figure 6: Properties under Property Development

Development properties	City	Effective Interest	Land Use Rights Expiry	Site area (sqm)	GFA (sqm)*	Total GDV (S$mn)
China						
Millennium Waterfront (Plots E & F) (Figure 7)	Chengdu	100%	2051	48,237	470,450	756
The Pinnacle (Figure 8)	Dongguan	60%	2058 (commercial) 2088 (residential)	36,404	75,400	273
Star of East River** (Figure 9)	Dongguan	30%	2054 (commercial) 2084 (residential)	49,136	177,000	256
Emerald of the Orient	Dongguan	20%	2058 (commercial) 2088 (residential)	67,477	144,371	173
Skyline Garden (Figure 10)	Dongguan	27%	2059 (commercial) 2089 (residential)	42,343	209,700	284
Humen TOD Project (Figure 11)	Dongguan	17%	2060 (commercial) 2090 (residential)	200,000	1,034,159	808
The Netherlands						
Meerparc	Amsterdam	100%	Freehold	9,744	-	-
Dreeftoren	Amsterdam	100%	2039***	5,740	-	-
The Terraced Tower	Rotterdam	33%	Freehold	1,220	39,539	48
Total				460,301	2,150,619	2,597

*: Excludes underground GFA and/or carpark
**: Excludes 31,000sqm LFA of retail mall
***: Perpetual leasehold interest with ground rents paid until Year 2039
-: Yet to be ascertained as the development plan for the project is at a preliminary stage
Source: Company

Investment Merits

1. **Unrecognised revenue from development properties amounts to S$586mn, or 1-2 years of sales.** Revenue is only recognised upon handover for its Chinese properties and by percentage of completion for The Terraced Tower. As most of its projects are due for handover either in late 2020 or 2021, we expect the bulk of the revenue to be reflected this and next year.

Development properties	Revenue to be recognised from handover/ % of completion	Revenue (S$mn)
China	Revenue is recognised upon handover	
Millennium Waterfront (Plots E & F)	FSG has recognised profit from all 7,302 residential units in Plots A to D. For Plot F, 84.2% of the SOHO loft units has been sold. It is expected to be handed over in phases from early 2021.	67
The Pinnacle	It launched five residential blocks for sale in phases since April 2020 which were almost fully sold soon after their respective launches. It is expected to be handed over in phases from 2021.	158
Star of East River*	One SOHO block was handed over in March 2020, another is expected to be handed over in 2021. Office block that is 89.7% sold is expected to be handed over in late 2020/early 2021	218
Emerald of the Orient	All sold units (852 residential units and 137 villas) are expected to be handed over from late 2020 to early 2021.	138
The Netherlands	Revenue is recognised based on % completion	
The Terraced Tower*	The Terraced Tower comprises 340 residential units, retail spaces and 212 car park lots. It is expected to be completed by 2021. The property is estimated to be c.80% completed	6
Total		586

*: Assuming S$64.4mn has been recognized from The Terraced Tower and the handover from one block of Star of East River.
Source: Company, PSR

Figure 7: Plot F, Chengdu Millennium Waterfront

Figure 8: The Pinnacle

Figure 9: Star of East River

Figure 10: Skyline Garden

Figure 11: Humen TOD Project

Source: Company

2. **GDV of S$1.95bn for unlocking, equivalent to 5-6 years of sales.** The largest projects in its pipeline are Plot E Millennium Waterfront and its recently secured Humen TOD project.

Development properties	Development/ Selling/ Leasing potential yet to be unlocked	GDV (S$mn)
China		
Millennium Waterfront (Plots E & F)	For Plot F, there are 15.8% of the SOHO loft units left to be sold. Plot E will be the last development plot for the project.	689
The Pinnacle	There are 2 more residential blocks in the next phase to be launched. The SOHO cluster is expected to be launched for presale in 4Q20.	115
Star of East River	One unit in the SOHO blocks left to be sold. As at 2Q20, 89.7% of the office tower block (778units) were sold, while 86.2% of the 27,335sqm retail lettable floor area of the commercial podium has been leased.	15
Emerald of the Orient	2 saleable residential units left to be sold. 222 residential units (24,605 sqm) and 31 villas (4,452 sqm) to be kept for a minimum holding period of 5 years	35
Skyline Garden	Comprises development of 5 residential blocks, 7 SOHO blocks as well as 4,400 sqm of commercial space. The development of the project is on track and the pre-sale of the residential component is expected to commence in 4Q20.	284
Humen TOD Project	A transit-oriented development in excess of 1 million sqm GFA	808
Total		1,947

Source: Company, PSR

3. **Humen TOD to become one of FSG's largest development projects to date (Figs. 11-12).** FSG successfully won the bid for a mixed-use development on 29 June at RMB6.6bn (c.S$1.3bn) in a JV with China Poly Group and China State Railway Group. The land will be developed into a transit-oriented development with more than 1mn sqm in GFA, encompassing the different interchanges along Guangzhou, Hongkong, Shenzhen, Humen and Dongguan. FSG has a c.17% effective equity interest in the JV.

4. **Unrelenting demand in Dongguan residential market.** Dongguan, a city in China's Greater Bay Area, is located between Shenzhen and Guangzhou. It is a manufacturing hub that is receiving an influx of talent, as more companies move to the city. As Shenzhen remains a highly-sought-after market due to its proximity to Hong Kong, Dongguan is benefitting from spillover demand for properties in the Greater Bay Area.

   Buying sentiment in the Dongguan property market has exceeded FSG's expectations after normal business activities resumed in late February. As of 30 June, almost all the SOHO units in its SoER project and saleable residential units in its EoO project had been sold. The Pinnacle project launched five residential blocks for sale in phases from April. These were also almost fully sold soon after their launches. Another residential block in The Pinnacle was launched for pre-sales on 14 July and has since sold more than 85%. The current resurgence of demand has triggered price-control measures from the Dongguan municipal, though the measures appear to have failed to slow down sales. The Group will pace the launch of its remaining two residential blocks in The Pinnacle and five residential blocks in its Skyline Garden project appropriately.

Key Risks

1. **Rental abatements provided to retail tenants during Covid-19.** Due to the impact of Covid-19, several retail tenants in the Star of East River retail mall requested for concessions to their rental obligations. The amount of rental abatements provided as of 1H20 was about three months of rent. We are expecting an additional waiver of three months to help the tenants tide over the crisis. Total amount of arrears is estimated to be S$2mn.

2. **Reassessment of development pipeline to slow down growth plans.** FSG obtained an irrevocable building permit to redevelop and increase the net lettable floor area of its Dreeftoren Amsterdam office property (acquired for €11.7mn) by 74% in 2019. In light of prevailing market conditions, it is re-assessing the feasibility of this new residential and office project. If it does not materialise and assuming a net yield of 3%, we are expecting S$0.98mn worth of delay in recurring profits.

Figure 12: Location of the new Humen TOD project

Figure 13: Real-estate investments in China rebounded to pre-COVID levels from late February (RMB trn)

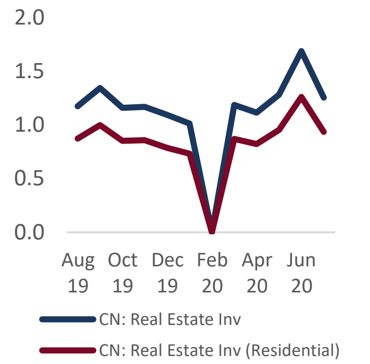
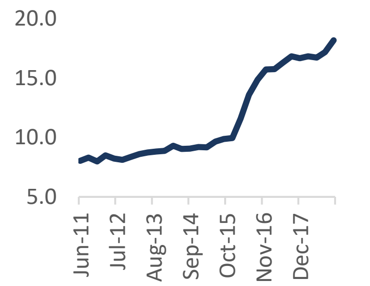


Figure 14: Dongguan's residential property prices (RMB '000/sqm) grew at a CAGR of 12.4% from 2011 to 2018



Source: Company, CEIC

II. Property Holding

FSG owns a portfolio of hotels and investment properties in Europe (FY19: 13.6% of total assets) and China (7.8%).

Figure 15: Investment Properties

Investment properties	Effective interest	Land Use Rights - Expiry	NLA (sqm)
The Netherlands			
Arena Towers #	100%	2053*	17,396
Berg & Bosch	33%	Freehold	34,024
Herengracht 21	33%	Freehold	473
Mondriaan Tower	33%	Freehold	24,936
Munthof	33%	Freehold	3,515
Oliphant	33%	2048*	21,136
Zuiderhof I	33%	2050*	12,538
Germany			
Le Méridien Frankfurt	50%	Freehold	15,602
Total			129,620

Figure 16: Hotel properties

Hotel properties	Effective interest	Land Use Rights - Expiry	GFA (sqm)	Number of rooms
China				
Crowne Plaza Chengdu Wenjiang Hotel & Holiday Inn Express Chengdu Wenjiang Hotspring Hotel (Fig. 17)	100%	2051	81,041	608
The Netherlands				
Hampton by Hilton Utrecht Centraal Station & Crowne Plaza Utrecht Centraal Station	100%	2069	13,822	193 (Hampton) 144 (Crowne Plaza)
Hilton Rotterdam (Fig. 18)	33%	Freehold	20,800	254
Bilderberg Garden Hotel Amsterdam	31%	2020*^	6,920	124
Bilderberg Parkhotel Rotterdam	31%	Freehold	12,875	194
Bilderberg Europa Hotel Scheveningen	31%	2026*	9,950	174
Bilderberg Kasteel Vaalsbroek	31%	Freehold	16,270	130
Hotel de Bilderberg	31%	Freehold	12,685	146
Bilderberg Hotel De Keizerskroon	31%	Freehold	7,588	93
Bilderberg Hotel 't Speulderbos	31%	Freehold	10,150	102
Bilderberg Résidence Groot Heideborgh	31%	Freehold	7,530	84
Bilderberg Grand Hotel Wientjes	31%	Freehold	4,087	57
Bilderberg Hotel De Bovenste Molen	31%	Freehold	6,575	82
Bilderberg Château Holtmühle	31%	Freehold	5,600	66
Germany				
Bilderberg Bellevue Hotel Dresden (Fig. 19)	95%	Freehold	40,678	340
Italy				
Bare shell hotel formerly known as Grand Hotel Puccini	100%	Freehold	2,980	To be refurnished into a hostel
Total			259,551	2,791

#: (Holiday Inn Amsterdam and Holiday Inn Express Amsterdam hotels)

*: Perpetual leasehold interest with ground rents paid until Year (indicated in Fig.15)

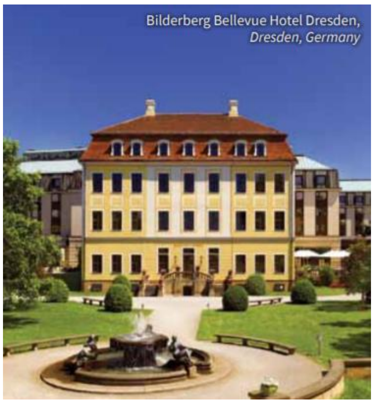
^: A one-off payment will be made in 2021 to prepay the ground rents until Year 2070

Source: Company

Figure 17: Crowne Plaza Chengdu Wenjiang

Figure 18: Hilton Rotterdam

Figure 19: Bilderberg Bellevue Hotel Dresden



Source: Company

Investment Merits

1. **Arena Towers provide recurring income at yields of more than 6%.** Arena Tower comprise two hotels in Amsterdam and their adjoining car parks that have been leased to external tenants. Each lease contains annual rents indexed to consumer prices and an initial non-cancellable period of 25 years. Despite Covid-19, tenant is still paying rent. In case of default, FSG holds three months of bankers' guarantees. With regards to the other investment properties, most are paying rent except for a few small tenants.

2. **Strong financial standing opens FSG to new opportunities.** With cash of S$474.9mn and a low net debt-equity ratio of 0.16x, balance sheet remained robust as at end-1H20. Additionally, undrawn committed long-term debt facilities of S$520.1mn and potential equity infusions from the exercise of outstanding warrants of S$460mn should equip FSG financially to take advantage of acquisition opportunities.

Key Risks

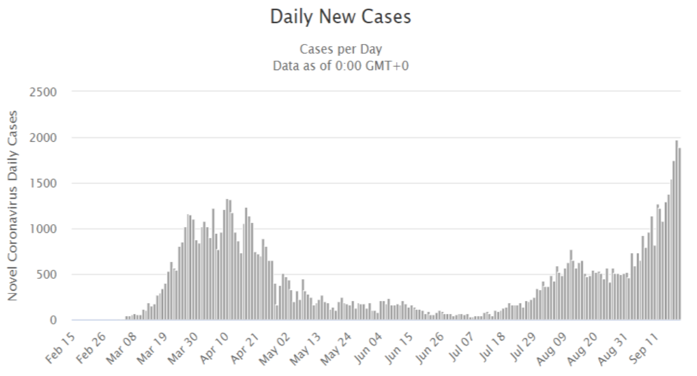
1. **Worst may not be over; stunted recovery is expected.** FSG's hotels are located in the parts of Europe where hotels saw a greater recovery in August (Netherlands portfolio ex-Amsterdam/ Rotterdam and Germany), boosted by demand for staycations. However, The Netherlands has seen a resurgence of Covid-19 cases lately, with new cases in September exceeding their peak in April. We are thus expecting a stunted recovery for its hotel portfolio till the end of 2020.

Figure 20: Hotel portfolio's occupancy YTD versus the month of August

	YTD occ. (%)	August occ. (%)
China		
Chengdu Hotels	20	28
The Netherlands		
Utrecht Centraal Station Hotels	30	40
Hilton Rotterdam	32	32
Bilderberg Portfolio	28	64
Germany		
Bilderberg Bellevue Hotel Dresden	18	60
Average	26	45

Source: Company

Figure 21: Daily new Covid-19 cases in the Netherlands



Source: Worldometers

2. **Rental arrears at Le Méridien Frankfurt.** Le Méridien Frankfurt's lessee, MHP, closed the hotel in March 2020 without the permission of the landlord and did not pay rent for April 2020. The Group has sought legal advice from its German lawyers on the non-payment of rents for May and June and half the rent for July. As at 21 July 2020, rental arrears amounted to €1.0mn, excluding VAT. The tenant re-opened the hotel on 15 May 2020. FSG holds a one-year banker's guarantee for this lease. Results of the court hearing will be announced in 3Q20.

3. **Reassessment of development pipeline to slow down growth plans.** FSG is reconsidering its plan to convert its bare-shell hotel in Milan acquired for €10.7mn in January 2019 into a high-density youth hostel in light of current market conditions. If this development does not materialise and assuming a 5% net yield, we are expecting S$0.86mn worth of delay in recurring profits

III. Property Financing

According to the World Economic Forum, China has one of the largest shadow-banking industries, with about 40% of its outstanding loans tied up in shadow banking. Shadow banking is mainly driven by the need for funding by small and medium-sized private companies (SMEs). These companies are unable to obtain loans from banks, which often prefer to lend to state firms and the larger listed private companies. FSG operates its property-financing business primarily in China via entrusted loans, The Netherlands, Germany, and Australia. In China, FSG only lends in first-tier and second-tier cities where it has a presence in. (Refer to Appendix I – Entrusted Loans).

Investment Merits

1. **High recurring income coupled with double-digit growth in loan book.** Of all its business lines, property financing has the highest gross profit margin (Fig. 22). This is because funding for this business in China is derived from its Chinese operations, which allows the business to grow at minimal to no costs. The business gives FSG high recurring income underpinned by interest rates of low to mid-teens p.a. Its China loan book grew at a CAGR of 19% from 2015 to 2019, largely attributable to high demand for credit among the SMEs. We are estimating loan book growth of around 8% for FY20e and FY21e. Average tenure for its China loan book is 3 years.

Figure 22: Property financing has the highest GPM out of its three businesses segments

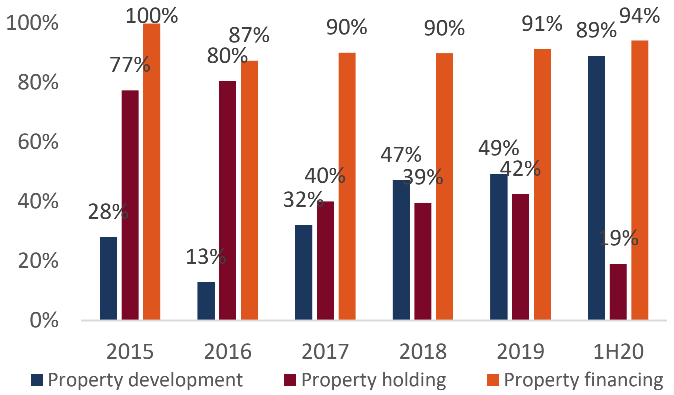
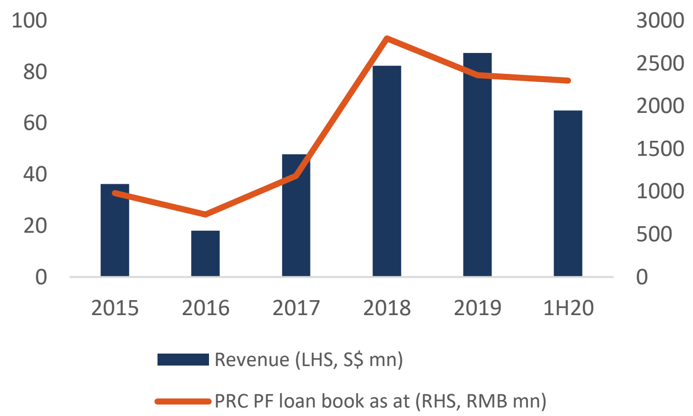


Figure 23: 1H20 property financing loan book increased by 12% YoY



Source: Company, PSR

As of 1H20, two defaulted loans had been fully repaid. The YoY increase in revenue in 1H20 (Fig. 21) was mainly due to one-off loan restructuring income of S$15.5mn and establishment fees from its new development venture in Australia.

2. **Zero bad-debt losses in eight years of operations; conservative LTV range of 40-60%.** FSG started its property-financing business in 2012. To date, it has not incurred any bad-debt losses. Although there were two cases of default in 2015 and 2016, FSG has managed to recover both its principal and interest. A 30.4% annual return was registered for one of these defaulted loans. Average loan to value (LTV) ratio for its portfolio ranges from low 40% to 60%.

3. **Maiden venture in Australia to redevelop City Tattersalls Club.** FSG holds an equity stake of 39.9% in ICD SB Pitt Street Trust, which is renovating Sydney's City Tattersalls Club's premises and developing the airspace above into a hotel and residential apartments. Apart from development fees payable to the trust, FSG will also charge a single-digit interest rate p.a. on a A$370mn (S$368mn) construction loan financing facility to fund the project. The project has received approval for its Stage 1 concept development and construction is expected to start in 2022.

Figure 24: City Tattersalls Club

Source: Company

Key Risks

1. **Subject to interest-rate cuts for penalty interest.** China's Supreme Court announced a plan in July to cut interest rates that shadow banks can charge for default penalties. The default penalty rate is now limited to 4x the Loan Prime Rate (4.35%) + a court-judged default rate (6%). This means FSG's return on default loans is now capped at 23.4%, versus no limits previously. The Group had ever recovered defaulted loans at 30.4% p.a. penalty rates in the past.

2. **Short-term deferral for interest payments provided for 40% of its China loan book.** Amid Covid-19, FSG has given consent to two borrowers of a RMB580mn loan and RMB330mn loan respectively for the short-term deferral of their interest payments.
    a. The RMB580mn loan is secured on a Guangzhou city hotel with a 44% LTV. The borrower could defer 50% of its monthly interest payments for a few months from 2Q2020, on condition that it contributes additional equity to a bank account jointly controlled by the borrower and FSG.
    b. The RMB330m loan is secured on a residential villa (RMB50m @ 46% LTV) and a 5-floor retail mall (RMB280m @ 55% LTV) in Shanghai. The related borrower group has been given consent to defer interest payments for one month.

Others

East Sun and Wanli portfolios. Through a 90% stake in Dongguan East Sun Limited, which has a 49% stake in Dongguan Wan Li Group Limited (Wanli), FSG owns a portfolio of commercial and industrial properties in Dongguan. The East Sun and Wanli portfolios are tenanted with positive running yields.

Update on sale of certain parts of Chengdu Cityspring. In February 2020, the buyer of certain parts of FSG's Chengdu Cityspring project wrote to the Group to terminate their sale and purchase agreement. In June 2020, the buyer entered into a supplemental agreement with the Group to obtain a discount of RMB3.5m on the purchase consideration for 292 car-park spaces and to acquire another 268 car-park spaces. The total purchase consideration was increased by RMB5.9m to RMB470.9m. The buyer has also withdrawn its termination letter. To date, 89% of the total purchase consideration has been collected, or RMB421.3mn. The outstanding RMB49.6mn will be repaid via monthly instalments of at least RMB10mn.

Disposal of Villa Nuova Office, Zeist, The Netherlands. FSMC completed the sale of Villa Nuova, a 1,428 sqm office property in Zeist, The Netherlands, on 31 Jan 2020. The property was 100% leased with lease expiry on 1 Jun 2022. The sale was completed before the Covid-19 pandemic hit The Netherlands, at a premium of about 8% over its allocated cost. FSMC had enjoyed an annual net rental yield of more than 10% since its purchase in November 2015.

Market Outlook

Property development in China. Hong Kong and mainland China are closely connected. With well-developed cross-boundary transportation networks and cross-boundary facilities, cross-boundary passenger traffic has been on the rise in recent years. In 2018, over 235mn passenger trips were made across the border via land crossings, bringing the daily average to over 640,000 passenger trips.

Initiated in July 2017, the Greater Bay Area (Fig. 25) covers the four core cities of Hong Kong, Macao, Guangzhou and Shenzhen as engines for regional development, while supporting Zhuhai, Foshan, Huizhou, Dongguan, Zhongshan, Jiangmen and Zhaoqing to become key node cities with distinct characteristics. The ultimate aim is to raise the development quality of this cluster of cities. The Dongguan property market is expected to continue to benefit from the development of the Greater Bay Area. Additionally, Shenzhen's continuing dominance as a tech hub could drive demand from mainland and Hong Kong tenants. In March 2020, 288 apartments in a new Shenzhen property development were sold out online in less than eight minutes. Dongguan's proximity to Shenzhen is expected to position FSG well for capturing spillover demand for residential properties.

Figure 25: Cities in the Greater Bay Area

Source: PSR, CEIC, https://www.bayarea.gov.hk/en/home/index.html

Property financing in China. After 2.5 years of regulatory clampdown, shadow banking has returned as China pledges faster credit growth to rescue its coronavirus-hit economy. According to Moody's, shadow-banking assets in the world's second-largest economy grew RMB100bn (US$14bn) to RMB59.1trn (US$8.4trn) in the first quarter of 2020, compared with a RMB1.2trn decline to RMB60.2trn during the same period in 2019. A survey in February 2020 of 2,069 small businesses by Zhenghe Island Research Institute found that more than a fifth of the respondents took private loans after Covid-19 broke out. The borrowing binge came with high interest rates. Private lenders in four provinces said they charged annual interest of 18-40%, compared with the benchmark one-year bank lending rate of 3.85%, to offset credit risks among subprime borrowers.

China's Supreme Court announced a plan in July 2020 to cut the penalty interest rate that shadow banks can charge. The figure could fall as low as 15% a year from 24%, affecting nearly RMB7trn (US$1trn) of outstanding loans. As a result, multiple shadow-banking lenders may stop servicing medium to high-risk borrowers. FSG is selective about the loans it makes, with several criteria to be met by its borrowers (Appendix I – Entrusted Loans). It is also not in the 'high risk' business, as evident from the interest rates it charges on its loans relative to the other lenders. Given current economic conditions, it has received overwhelming requests for loans. However, FSG intends to remain discerning and selective.

Figure 26: Real-estate investments in China grew at a CAGR of 14.3% over 2009-2019

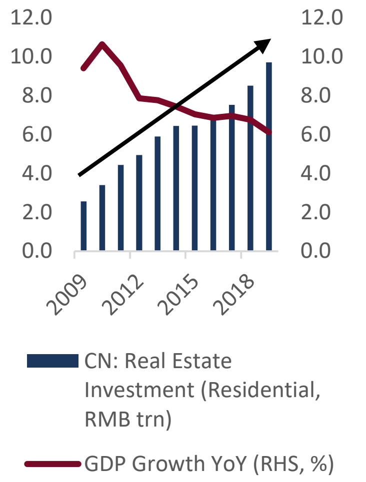
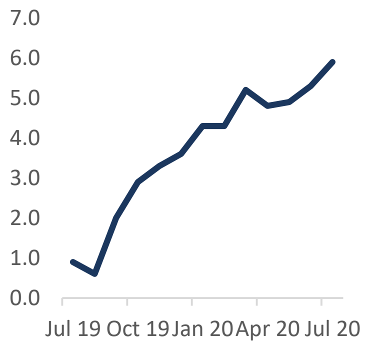


Figure 27: Shenzhen's property price index increased more than 3% YoY (%) even amid Covid-19.



Source: PSR, CEIC

Property holding in The Netherlands. Amsterdam remains the most attractive city for hotel investments in 2020 for the fourth year in a row due to its positive demand fundamentals and yield profile. Overall arrivals at Amsterdam grew at a CAGR of almost 7% annually over the past 10 years with continuous national y-o-y arrival growth since 2008. In 2019, international inbound tourists (19.5mn) largely comprised EU residents (79%), according to NBTC Holland Marketing. Residents from the US and Asia constituted 11% and 7% respectively. This highlights that inbound tourism is highly reliant on EU travellers.

Member states of the EU were provided with guidelines and recommendations to lift travel restrictions gradually on 13 May. In July, ticket numbers for cross-border air travel within Europe stood at 28% of 2019 levels, as Europeans began to travel again after months of lockdown, according to the travel analysis group, ForwardKeys. However, in recent months, countries across Europe are seeing a resurgence of Covid-19 cases, after successfully slowing down outbreaks earlier. France, Poland, The Netherlands and Spain could be dealing with a much-feared second wave.

The Dutch government has announced specific measures to control the spread of coronavirus. The measures apply to the six safety regions that are currently seeing the sharpest spikes in coronavirus infections. These are Amsterdam-Amstelland, Rotterdam-Rijnmond, Haaglanden, Utrecht, Kennemerland and Hollands Midden. Restrictions include a ban on gatherings of more than 50 people and closing of catering establishments by midnight. The six regions are also adopting specific local measures. We are expecting these restrictions to undo the August recovery for FSG's hotels in July and August and for hotel occupancy to fall back to YTD levels till the end of the year, before a potential recovery in 2021 should the situation improve.

Property Development in Australia. According to CBRE, residential prices in Sydney grew 8% in 2019, though vacancies climbed higher to 3.3% (2018: 2.5%), amid lower apartment completions. We are expecting residential price growth to moderate in 2020 due to existing inventories before the decline in new supply comes through in 2020 and 2021.

Figure 28: Development cycle is quickly returning to undersupply again

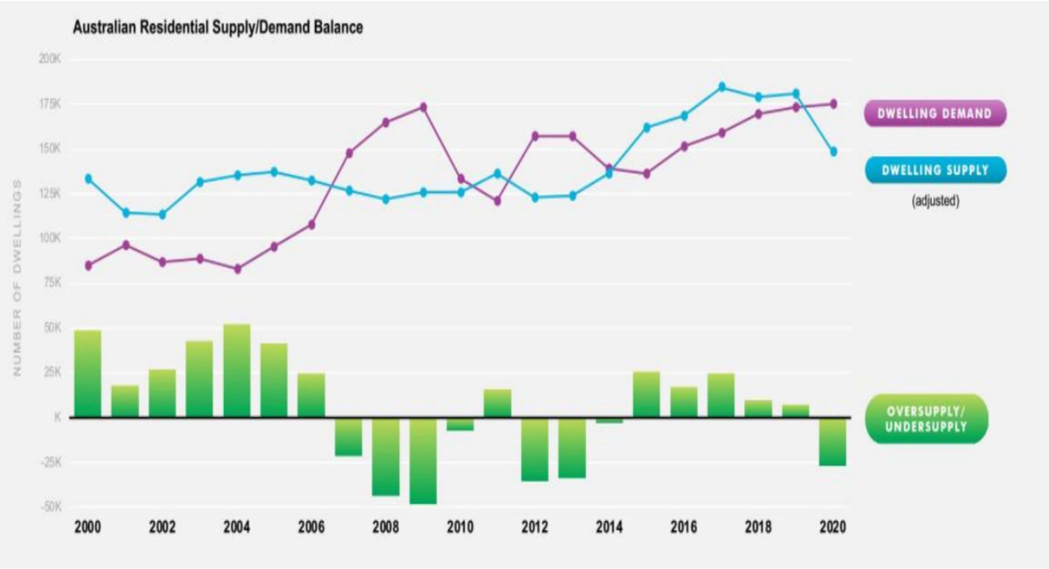


Figure 30: Sydney's apartment completions (bar chart) and vacancy (line chart)

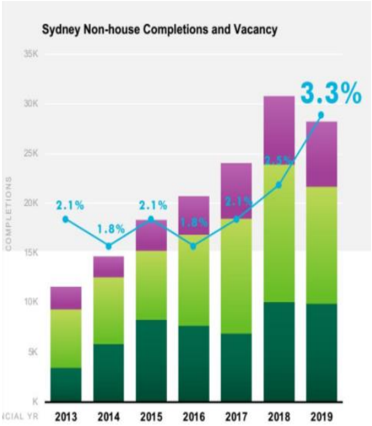


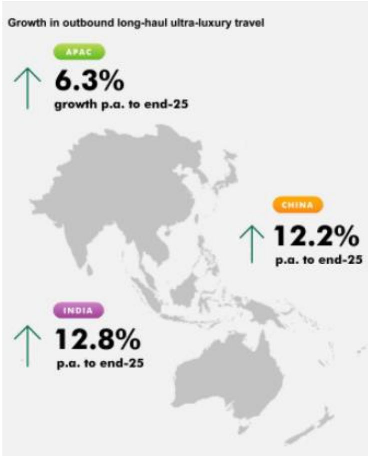
Figure 29: Australian residential price growth, historical and forecasts

Australian residential price growth, historic and forecast

MARKET	10 YEAR P.A.		2019 (EST.)		2020 (FORECAST)	
	HOUSES	UNITS	HOUSES	UNITS	HOUSES	UNITS
Sydney	6.7%	5.7%	8.0%	1.0%	7%-12%	5%-10%
Melbourne	5.5%	3.8%	9.0%	7.0%	7%-12%	5%-10%
Brisbane	1.7%	0.7%	0.0%	0.0%	5%-10%	2%-7%
Perth	-0.2%	-1.1%	-6.0%	-3.0%	0%-2%	0%-2%
Adelaide	2.2%	2.2%	1.0%	4.0%	0%-5%	0%-5%
Canberra	3.0%	1.6%	-4.0%	0.0%	0%-5%	0%-2%
National	4.2%	3.8%	5.0%	2.0%	5%-10%	3%-6%

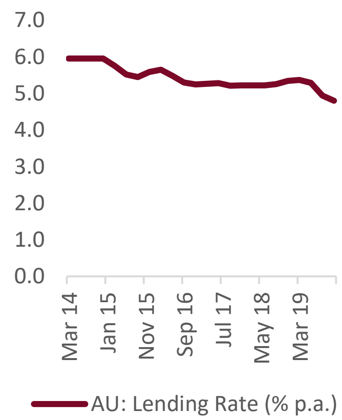
Source: CBRE

Figure 31: Growth in outbound long-haul ultra-luxury travel



For hotels, softer trading conditions in 2020 will be driven by a combination of supply additions and subdued demand growth. New CBD retail luxury brands are expected to attract international visitors after the relaxation of travel restrictions (Fig. 31).

Figure 32: Australia's lending rate (% p.a.)



Source: CEIC, PSR, CBRE

Property financing in Australia. Non-bank lending in the Australian property market is forecast to expand further in 2020, driven by increased interest from both developers and investors. The Australian non-bank loan market has been an essential source of funding for Australian property developers and investors for decades. Domestic banks currently hold around 70% of the corporate lending market, according to Metrics.

Due to the large balance-sheet capacity and capital required to operate in the market, barriers to entry are high. In recent times, banks have come under regulatory pressure to reign in their loan portfolios to meet stricter capital requirements. This has opened up opportunities for non-bank lenders to claim a greater share of the >US$900bn market. For this reason, we expect non-bank lenders to register modest growth in the coming year.

Valuation

We initiate coverage of FSG with a BUY rating and RNAV-derived target price of S$1.65. Our target price implies a total potential return of 33.6% and dividend yield of 1.75%. It is based on a 30% discount to FSG's fully-diluted RNAVPS (@1,102mn shares after adding outstanding warrants). Based on its current number of shares (912mn), we derive a target price of S$1.99. FSG trades at 0.6x FY20e P/B versus its historical 5-year average of 0.7x.

Figure 33: RNAV estimation

		Valuation ($mn)
A)	**Hotel properties**	**851**
B)	**Investment Properties**	**789**
C)	**Development Properties**	**449**
D)	**Property Financing**	**310**
E)	**Other Investments**	**393**
	Interests in associates and joint ventures	308
	East Sun Portfolio	34
	Other equity investments	11
	Other debt investments	40
Total		**2793**
-	**Net Debt**	**204**
FSG VALUATION		**2588**
No of shares (mn, fully diluted basis)		**1,102**
Discount		**30%**
TP (S$)		**$1.65**

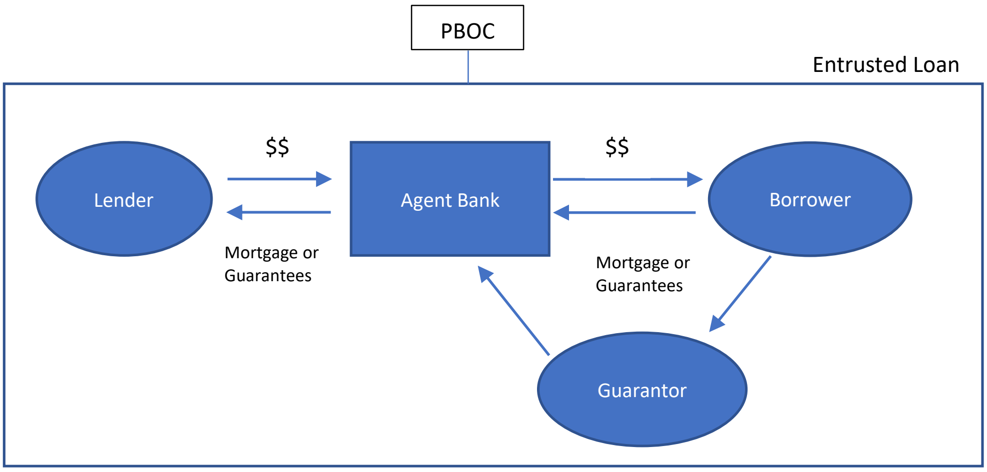
Peer Comparison

Companies	Mkt. Cap. (S$mn)	Price (S$)	P/NAV	Gearing (%)	ROE	EV/EBITDA	P/EBITDA	P/SALES	P/E
First Sponsor Group	1,141	1.25	0.6	25	12.0	N.A.	24.1	4.9	7.4
Capitaland	14,125	2.72	0.6	38	5.9	25	4.5	2.2	10.1
Hong Kong Land	8,682	3.72	0.2	11	-5.5	14	N.A.	3.7	N.A.
City Developments	7,337	8.09	0.7	43	1.8	27	12.7	2.5	39.4
Frasers Property	3,482	1.19	0.5	46	5.9	26	3.1	0.9	8.1
Guocoland	1,739	1.47	0.4	47	7.9	27	3.6	1.4	6.0
OUE	1,036	1.15	0.3	37	-0.4	N.A.	5.3	1.3	N.A.
Bukit Sembawang	948	3.66	0.7	18	5.8	N.A.	8.0	2.6	12.4
Oxley Holdings	907	0.22	0.9	59	N.A.	9	3.3	1.3	6.3
GuocoLeisure	739	0.54	0.5	49	4.4	N.A.	5.5	2.0	N.A.

Source: PSR, Company

Appendix I – Entrusted Loans

Entrusted loans (委托贷款) involve lending between two parties where an agent bank serves as an intermediary for the provision of funds to a borrowing company designated by the lending company (in this context, FSG). FSG leverages the entrusted loan system governed by PBOC. The agent bank is responsible for the collection of principal and any interest, for which it charges a handling fee of 1%, but does not assume any loan risk. All loans are booked with PBOC, which provides a level of protection for FSG as it takes on borrower and/or guarantor risks.



Source: PSR, Company

<u>Process Flow</u>

Step 1: FSG will receive loan proposals from various brokers and select based on its criteria. Some of its key criteria are coupon rate, loan tenure, type of collateral and Know Your Client (KYC). Collateral must be assets that FSG does not mind owning and are found in any of the four Tier-1 cities or Dongguan and Chengdu where FSG operates in.

Step 2: FSG will view the property, assess borrower creditworthiness and approve the loan. Entrusted loans are generally secured by a mortgage of land use rights and/or property as well as personal and/or corporate guarantees in favour of the entrusted bank. The loan disbursed is capped at a pre-set LTV ratio of a low 40-60% of the property collateral.

Step 3: Commercial bank will register the loan as entrusted loan in the PBOC system. When the property collateral is pledged under a loan, the computerised entrusted loan system will not allow for the same collateral to be pledged under another loan. Loans are disbursed typically with tenures of 1-3 years.

Step 4: In the event of default, FSG can initiate a court case to trigger a cross-default on all of the borrower's debt facilities. The lender can initiate a court case to enforce the borrower's obligation to repay the loan. Should the court rule in the lender's favour, the loan will be marked as a default loan which triggers a cross-default on all of the borrower's debt facilities registered with the PBOC. Subsequently, the borrower is subject to penalty interest of up to 23.4% for a certain duration till the principal and interest have been repaid. Otherwise, the asset in the collateral will be put up for public auction for the repayment of its debt obligation.

Financials

Statement of Total Return and Distribution Statement

Y/E Dec, (S$'000)	FY17	FY18	FY19	FY20e	FY21e
Revenue	**384,392**	**277,361**	**319,164**	**354,939**	**447,449**
Cost of sales	(231,360)	(115,861)	(130,129)	(159,207)	(216,137)
Gross Profit	**153,032**	**161,500**	**189,035**	**195,732**	**231,312**
Net finance income	8,072	7,230	870	(3,841)	(3,494)
Administrative expenses	(24,146)	(27,997)	(38,206)	(42,607)	(57,843)
Share of profits from JVs and associa	3,648	5,502	71,222	3,905	20,490
Other items	(19,373)	(1,687)	(28,722)	666	(15,239)
Profit Before Tax	**121,233**	**144,548**	**194,199**	**153,854**	**175,227**
Taxation	(27,940)	(26,298)	(28,623)	(25,334)	(27,340)
PATMI	**88,283**	**108,467**	**163,610**	**125,821**	**144,781**
EBIT	**108,151**	**127,535**	**191,363**	**154,996**	**175,614**
EBITDA	**113,661**	**133,707**	**201,719**	**165,741**	**186,046**

Per unit data

Y/E Dec	FY17	FY18	FY19	FY20e	FY21e
NAVPS (S$)	1.83	2.02	1.97	2.14	2.30
NAVPS (S$, diluted)	1.83	1.65	1.65	1.82	1.94
EPS (S$ cents)	13.61	16.72	21.64	15.71	18.07
EPS (S$ cents, diluted)	13.61	15.02	17.12	12.40	14.17
DPU (S$ cents)	2.20	2.30	2.70	2.06	2.37
DPU (S$ cents)	2.20	2.07	2.14	1.63	1.86

Cash Flow

Y/E Dec, (S$'000)	FY17	FY18	FY19	FY20e	FY21e
CFO					
Profit for the year	**93,293**	**118,250**	**165,576**	**128,520**	**147,887**
Adjustments	42,872	(15,948)	(55,097)	34,030	20,776
WC changes	(122,542)	(444,608)	27,838	75,852	(289,101)
Cash generated from ops	**13,623**	**(342,306)**	**138,317**	**238,403**	**(120,439)**
Others	23,529	45,577	20,005	(25,334)	(27,340)
Cashflow from ops	**37,152**	**(296,729)**	**158,322**	**213,069**	**(147,779)**
CFI					
Acquisition of subsidiaries	-	-	(156,770)	-	-
Advances to associates (net)	-	-	(86,867)	(46,042)	-
Payment for acquisition of other inve	-	(3,395)	(357)	(15,998)	-
Payment for additions to PPE	(6,423)	(421)	(37,482)	(14,706)	-
Payment for investments in associat	(6,187)	(36,778)	(81,242)	(17,971)	-
Others	48,488	61,602	154,632	31,818	24,304
Cashflow from investments	**35,878**	**21,008**	**(208,086)**	**(62,899)**	**24,304**
CFF					
Advances from associates (net)	13,484	3,009	120,261	18,196	-
Dividends paid to the owners of the	(11,796)	(14,271)	(19,078)	(16,385)	(18,854)
Proceeds from issuance of medium t	-	-	-	100,000	-
Repayment of bank borrowings	(744,192)	(345,950)	(632,633)	(407,517)	-
Proceeds from bank borrowings	766,308	293,551	611,205	436,318	-
Others	(55,260)	148,795	164,773	(48,988)	(27,798)
Cashflow from financing	**(31,456)**	**85,134**	**244,528**	**81,624**	**(46,652)**
Net change in cash	**41,574**	**(190,587)**	**194,764**	**231,794**	**(170,126)**
Cash at the start of the period	280,304	319,298	125,711	313,389	545,183
Currency translation	(2,580)	(3,000)	(7,086)	-	-
Ending cash	**319,298**	**125,711**	**313,389**	**545,183**	**375,056**

Balance Sheet

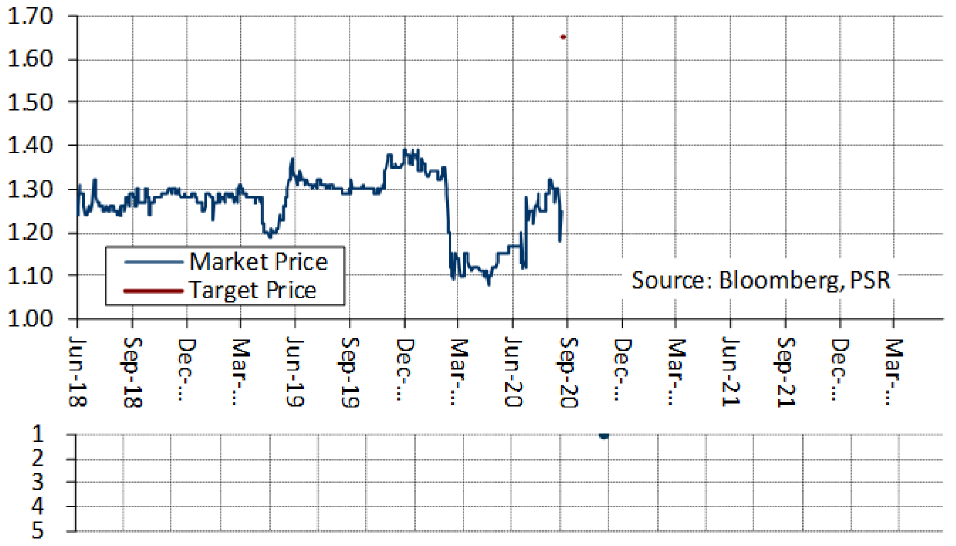
Y/E Dec, (S$'000)	FY17	FY18	FY19	FY20e	FY21e
ASSETS					
Investment properties	282,634	259,135	94,827	98,947	98,947
Property, plant and equipment	230,844	170,435	345,847	358,071	347,639
Interests in associates and joint	64,361	80,817	298,062	307,984	328,474
Trade and other receivables	284,455	660,948	824,848	824,848	824,848
Others	49,635	130,903	146,842	153,420	153,420
Total non-current assets	**911,929**	**1,302,238**	**1,710,426**	**1,743,270**	**1,753,328**
Development properties	390,704	356,890	390,046	449,253	449,253
Trade receivables	445,534	505,887	315,255	346,247	804,946
CCE	319,298	125,711	313,389	545,183	375,056
Inventories	175	215	550	404	635
Others	38,863	90,872	30,830	33,135	33,135
Total current assets	**1,194,574**	**1,079,575**	**1,050,070**	**1,374,222**	**1,663,025**
Total Assets	**2,106,503**	**2,381,813**	**2,760,496**	**3,117,491**	**3,416,353**
LIABILITIES					
Trade payables	166,093	138,381	307,085	266,662	362,016
ST borrowings	-	45,338	251,220	300,767	408,317
Contract liabilities	177,726	161,279	39,288	196,069	162,994
Others	36,012	45,202	65,663	65,663	65,663
Total current liabilities	**379,831**	**390,200**	**663,256**	**829,161**	**998,990**
LT borrowings	609,988	641,390	369,943	448,898	448,898
Others	29,803	26,729	128,708	128,708	128,708
Total non-current liabilities	**639,791**	**668,119**	**498,651**	**577,606**	**577,606**
Total liabilities	**1,019,622**	**1,058,319**	**1,161,907**	**1,406,767**	**1,576,596**
Net assets	**1,086,881**	**1,323,494**	**1,598,589**	**1,710,724**	**1,839,757**
Represented by:					
Share Capital	73,640	81,405	101,251	101,251	101,251
Reserves	1,006,514	1,069,091	1,320,670	1,432,805	1,561,838
Others	6,727	172,998	176,668	176,668	176,668
Total equity	**1,086,881**	**1,323,494**	**1,598,589**	**1,710,724**	**1,839,757**

Valuation Ratios

Y/E Dec	FY17	FY18	FY19	FY20e	FY21e
P/NAV (x)	0.6	0.6	0.7	0.6	0.5
P/E (x)	7.6	7.7	6.3	7.5	6.5
EV/EBITDA (x)	2.6	23.7	15.2	18.2	17.7
Growth & Margins (%)					
Growth					
Revenue		-27.8%	15.1%	11.2%	26.1%
Gross profit		5.5%	17.0%	3.5%	18.2%
EBITDA		17.6%	50.9%	-17.8%	12.3%
EBIT		17.9%	50.0%	-19.0%	13.3%
Margins					
Gross profit margin	39.8%	58.2%	59.2%	55.1%	51.7%
EBITDA margin	29.6%	48.2%	63.2%	46.7%	41.6%
EBIT margin	28.1%	46.0%	60.0%	43.7%	39.2%
Key Ratios					
ROE	8.1%	8.2%	10.2%	7.4%	7.9%
ROA	4.2%	4.6%	5.9%	4.0%	4.2%
Gearing (%)	48.4%	44.4%	42.1%	45.1%	46.1%

Source: Company, Phillip Securities Research (Singapore) Estimates

Ratings History



PSR Rating System

Total Returns	Recommendation	Rating
> +20%	Buy	1
+5% to +20%	Accumulate	2
-5% to +5%	Neutral	3
-5% to -20%	Reduce	4
< -20%	Sell	5

Remarks

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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