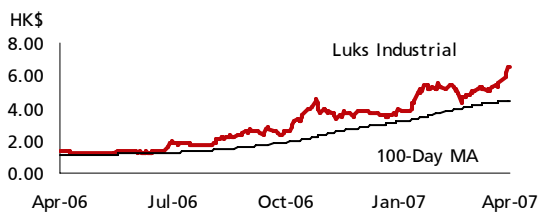


NOT RATED HK\$6.50 HSI: 20,341**Price Target:** 1-year HK\$7.5-8.5**Potential Catalyst:** ASP scale up in cement price and property project acquisition**ANALYST**Oscar Choi · (852) 2863 8877 ·
oscar_choi@hk.dbsvickers.com**EARNINGS VALUATION**

| FY Dec (HK\$m) | 2006F | 2007F | 2008F | 2009F |
|-------------------|-------|-------|-------|-------|
| Turnover | 357 | 590 | 871 | 2,027 |
| Net profit | 81 | 159 | 204 | 429 |
| Basic EPS (HK\$) | 0.16 | 0.31 | 0.40 | 0.84 |
| EPS Gth (%) | 250.3 | 97.5 | 28.0 | 1.1 |
| DPS (HK\$) | 0.05 | 0.06 | 0.08 | 0.17 |
| Div Yield (%) | 0.8 | 1.0 | 1.2 | 0.0 |
| PER (X) | 41.2 | 20.9 | 16.3 | 7.8 |
| Book Value (HK\$) | 2.20 | 2.64 | 3.30 | 4.49 |
| P/Book Value (x) | 3.0 | 2.5 | 2.0 | 1.4 |
| Net Gearing (%) | 1.5% | 10.9% | 17.6% | Cash |
| ROE (%) | 7.4% | 12.9% | 13.4% | 21.5% |

PRICE & VOLUME CHART**AT A GLANCE**

| | |
|---------------------------|-------------|
| Issued Capital (m shrs) | 512 |
| Mkt Cap (HK\$m/US\$m) | 3,331 / 426 |
| Major Shareholders (%) | |
| Luk King Tin | 59.95 |
| Free Float (%) | 40.05 |
| Avg Daily Volume (m shrs) | 2.2 |

Consensus EPS: FY06: n.a. ; FY07: n.a.
Variance vs Cons: FY06: n.a. ; FY07: n.a.

Sector: Property & Cement**Bloomberg/Reuters Code:** 366 HK / 0366.HK**Principal Business:** Vietnam property & cement**Luks Group (Vietnam Hldgs)*****Twin growth engines - cement and property**

➤ **Story:** As an early bird in Vietnam's cement manufacturing and property business, Luks should be a key beneficiary of the newly emerging Asian economy's prosperity.

➤ **Point:** A new cement line will begin operation in 2Q08 and increase the existing production capacity by 85% to 2.8m tonnes (3.0m tonnes in 2009). Moreover, the property development segment should make a significant contribution in 2009.

➤ **Relevance:** As a high growth stock (EPS CAGR of 74% in 2006-2009), Luks deserves to trade at a higher valuation. The stock is trading at 16.3x FY08 PER (7.8x FY09 PER). Its value may reach 10x FY09F PER due to strong EPS growth.

Riding on the wave of Vietnam's expansion. Luks Group (Vietnam Holdings) (366.HK) has successfully transformed into a Vietnam-focused company, engaging in cement manufacturing and property investment/development business. More than 95% of its income is generated from Vietnam. We expect Vietnam to maintain an average GDP growth of 7.5-8.0% per annum from 2006-2010, with the Government investing heavily in infrastructure, thus favouring construction material makers. Moreover, the foreign direct investment and exports undoubtedly will surge along with Vietnam's formal entry into the WTO in January 2007. Vietnam has been replicating the successful story of China, which has proven property and infrastructure as the key winners. With its strong position in southern Vietnam's cement market, Luks should grow with the country's prosperity.

Twin-turbo powered growth. By the end of 2009, Luks will increase its cement production capacity to 3.0m tonnes, double the existing 1.5m tonnes. With the operation of a new production line in 2Q08, Luks should establish a strong position in southern Vietnam's cement market, especially in Vietnam's largest city-Ho Chi Minh City. As for property development, the two newly-acquired residential projects, both located in Ho Chi Minh City, are expected to be on pre-sale in 2Q08 and make fresh contribution in 2009. Luks is targeting to increase the land bank size from the present 188,000sqm to 400,000sqm GFA. Moreover, the investment property - Saigo Trade Centre - can offer a stable recurring income for the company.

Valuation not demanding for a high-growth stock. Thanks to the strong growth in the cement business and fresh contribution from the property development business, Luks is expected to have an explosive bottomline growth in 2006-2009 with a CAGR of 74%. By the end of 2009, the bottomline should increase to HK\$429mn from FY06E's HK\$81mn. The stock is trading at a forward FY08E PER of 16.3x, sharply dropping to 7.8x in FY09 but the valuation is not demanding. In terms of NAV, we believe Luks deserves to trade at a premium of 10-15% over our estimated NAV of HK\$7.4. Its value may reach 10x FY09F PER due to strong EPS growth.

***propose to change name from Luks Industrial (Group) Ltd to Luks Group (Vietnam Holdings) Co Ltd.**

Highlights

- Background.** Luks Group (Vietnam Holdings) Company Ltd (366.HK), previously called Luks Industrial (group) Ltd, started as an industrial company engaging in electronics manufacturing businesses since it was established in 1975 by the Chairman, Mr Luk King Tin. Today, the company has successfully transformed into a holding company with its principal subsidiaries situated in Vietnam, engaging in cement manufacturing and property investment and development business with more than 95% of its income generated from Vietnam. Thanks to the strong economic growth in Vietnam, we believe Luks Group should ride on the wave due to its rich experience in Vietnam's cement and property business.
- In the 2006-2010 Five-Year Planning, the Vietnam Government targets to reach an average GDP growth of 7.5-8.0% per annum from 2006-2010,** up from the average 7.5% p.a. growth achieved from 2001-2005. To boost its economic structure, the Government should focus on the secondary and tertiary industries, especially manufacturing, infrastructure, construction and real estate. In 2006, the country recorded a strong GDP growth of 8.2% and expect to further accelerate to 8.5%-9.0% in 2007 and 2008. The strong economic growth in Vietnam should create an unprecedented golden development opportunity for infrastructure and real estate, as seen in China.

Vietnam- Government's Economic Targets in the 2006-2010 Five Year Plan (FYP)

| Indicators | | 2001-2005 (average) | 2006-2010 (target) |
|-------------------------------------|-------------|------------------------|-----------------------|
| Real GDP Growth | % | 7.5 | 7.5-8.0 |
| Agricultural, forestry, fishery | % | 3.8 | 3.0-3.2 |
| Industry and construction | % | 10.2 | 9.5-10.2 |
| Services | % | 7 | 7.7-8.2 |
| Production Value Composition | | | |
| Agricultural, forestry, fishery | % | 20.9 | 15-16 |
| Industry and construction | % | 41 | 43-44 |
| Services | % | 38.1 | 40-41 |
| GDP Per Capita | US\$ | 640 | 1050-1100 |

Source: Vietnam Five Year Socio Economic Development Planning (2006-2010)

- Foreign Direct Investment surge after the WTO Entry.** With Vietnam's formal entry into the WTO in January 2007, we believe the foreign direct investment (FDI) will significantly increase in the coming several years and the country should enter a period of rapid growth. In 2006, the FDI in Vietnam recorded a strong growth of 94% y-o-y to US\$7.56bn and we believe FDI growth can maintain at a CAGR of 30% in the period of 2006-2010, driving economic growth. A ramp-up in export capacity should become evident over the coming several years. China's experience in the first five years after its WTO accession indicated strong beneficial impact to the country. It resulted in a period of elevated structural export growth, nearly doubled from pre-WTO's 16.5% growth y-o-y to 29.2% growth y-o-y. From 2006-2010, Vietnam should invest up to VND2,677 trillion into the infrastructure. The Government understands the country's constraints in basic infrastructure and utilities, e.g. electricity shortages, lagging-behind toll road, port, railway systems and intends to introduce more foreign investments and Vietnamese private funds into these fields. Thus, we believe the producers of basic construction materials e.g. cement, steel should be one of the major beneficiaries from the development wave.

Vietnam- Infrastructure Investment Targets in the 2006-2010 Five Year Plan (FYP)

| Investment Category | 2001-2005 (average Capacity) | 2006-2010 (targeted Capacity) | Change (%) |
|-----------------------------|---------------------------------|----------------------------------|------------|
| Power Generation- mn watt | 6,383 | 18,400 | 188% |
| Steel Production- 'K tons | 2,390 | 3,800 | 59% |
| Cement Production- 'mn tons | 10.1 | 20.0 | 98% |
| Coal Production- mn tons | 15.4 | 16.5 | 7% |
| Roads- highways- km | 4,575 | 5,800 | 27% |
| Roads- general- km | 65,004 | 100,000 | 54% |
| Railway- upgrade- km | 380 | 950 | 150% |

Source: Vietnam Five Year Socio Economic Development Planning (2006-2010)

- In line with the growth pace of the economy and the group's strategy in investing in property and infrastructure-related business in Vietnam, Luks should further increase its investment in residential property development for sale or leasing purpose in Ho Chi Minh City, which is the largest city in Vietnam – similar to the experience of Shanghai to China.

Prospects

Cement business- the crown jewel

- **The key beneficiary from Vietnam's prosperity.** Having said that, construction material producers have always proven to be the key beneficiaries in the early stage of an emerging country, thanks to the heavy investment in infrastructure and utilities. Along with the growth of Vietnam's economy, the demand for cement has been growing in a faster pace. The domestic production capacity can only satisfy some 50-60% of the country's demand. In 2006, Vietnam's cement production increased to 21m tonnes while demand surged to 33m tonnes. The demand gap had to be fulfilled through imports from countries such as Thailand, China and Indonesia. At present, Vietnam's cement market is still dominated by the state-owned enterprises with a market share of 55%-65%. Luks Group is one of the main foreign cement investors and has a strong position in southern Vietnam.
- **Rapid production capacity expansion plan for cement business.** In December 2006, the Vietnamese Central Government granted approval to Luks to invest in a new cement production line with an annual capacity of 1.3m tonnes, which is scheduled to commence operation in 2Q08. It is anticipated that when the facility is completed, the production output of cement will increase to 2.8m tonnes from the existing capacity of 1.5m tonnes per annum - an increase of approximately 85%. Luks targets to further upgrade the production line and eventually increase the production capacity to 3.0m tonnes.
- **Strong earning growth momentum for cement business- 60% CAGR of EBIT in 2006-2009.** Driven by the production growth and the favourable cement price trend, we believe the earning contribution from the cement business should be one of the key growth drivers for Luks's bottomline. In 2006-2009, the estimated EBIT contribution should record a strong CAGR of 60% and reach HK\$308.5mn by the end of 2009. The group has strong competitive advantage over its peers with its abundant reserves of limestone. Moreover, the new production line should allow the company to enter Vietnam's largest cement-consuming market - HO Chi Minh City, where the average cement price is 10-15% higher than other cities in southern Vietnam.

Luks Group- Vietnam Cement Business

| | 2005 | 2006 | 2007 | 2008 | 2009 |
|---|---------|---------|-----------|-----------|-----------|
| Production Capacity (tons) | 750,000 | 750,000 | 1,500,000 | 2,800,000 | 3,000,000 |
| Utilization (%) | 104% | 117% | 100% | 77% | 93% |
| Cement sales Volume (tons) | 782,000 | 881,020 | 1,500,000 | 2,150,000 | 2,800,000 |
| Growth (%) | 3.0% | 12.7% | 70.3% | 43.3% | 30.2% |
| ASP (USD/ton) | 38 | 40 | 43 | 47 | 50 |
| Growth (%) | 6.1% | 5.0% | 8.5% | 8.0% | 8.0% |
| Vietnam's total cement demand (' mn tons) | 28 | 33 | 45 | 62 | 81 |
| Luks market share (%) | 2.8% | 2.7% | 3.4% | 3.4% | 3.5% |
| EBIT contribution to the Gorup (HK\$'mn) | 61.48 | 75.89 | 141.70 | 211.51 | 308.52 |
| Growth (%) | 5% | 23% | 87% | 49% | 46% |

Source: Company & DBS Vickers

Vietnam property business- the crown prince

- Early bird in Vietnam's property market.** Along with the strong economic growth and the obvious improvement in people's living standards, the property market should enter a rapid growth period. Vietnam has opened its property market to foreign investors only in the past 1-2 years. The market is still very fragmented, with weak involvement by foreign property developers. Luks has been the early bird in the emerging lucrative property market in Vietnam, starting with its first property investment in 1998, the Saigon Trade Centre, one of the landmark buildings in Ho Chi Minh City. Since then, the company has been steadily diversifying into the even higher-return residential market, hoping to build up a strong position in Ho Chi Minh City.
- Lucrative return for residential projects with development margin of 50-60%.** Currently, Luks has two residential projects with a total GFA of 188,000 sqm, both located in the prime location of Ho Chi Minh City. The two projects were procured through setting up a JV with local partner. Due to the cheap land cost and strong demand for high-quality residential houses, the development margin can reach as high as 55-60%. The construction of the two projects is expected to start in 3Q07 and the pre-sale should be conducted as early as 2Q08. We believe the property development business should begin its fresh contribution in 2009 and become one of the key profit contributors for the company. According to the management, the property development business should be one of the prime foci for the company and the land bank size should be targeted to increase to 400,000sqm in the coming 12 months.
- Investment property - a stable recurring income.** Built in 1998, Luks's 100%-owned Saigon Trade Centre is one of the top office buildings in Ho Chi Minh City. The occupancy rate is around 97% and there is still upside room for rent rate due to the increasing demand from foreign enterprises after Vietnam's WTO entry. Key tenants of Saigon Trade Centre include prestigious enterprises such as Intel, Standard Chartered Bank and Colgate. We believe the investment property should continue to offer a stable recurring income for the company.

Vietnam Property Development

| Project | Interest % | Area Sqm GFA | Total cost USD/sqm | ASP USD/sqm | Development Margin % | Construction Commence | Expected Pre-sale |
|--|------------|--------------|--------------------|-------------|----------------------|-----------------------|-------------------|
| Thao Dien Ward, District 2, Ho Chi Minh City | 90% | 73000 | 536 | 1200 | 55% | 3Q07 | 2Q08 |
| An Lac Ward, Binh Chanh District, Ho Chi Minh City | 70% | 115000 | 355 | 800 | 56% | 3Q07 | 2Q08 |

Source: Company, DBS Vickers

Action

- **Estimated EPS CAGR of 74% in 2006-2009.** The beneficiaries of the accelerating pace of the economy and increasing foreign investment in Vietnam, the cement manufacturing and the property development businesses are expected to maintain strong growth momentum in the future. Luks should fully focus on its Vietnam- related businesses and gradually divest its non-core businesses such as Traditional Chinese Medicine business. Having said that, the cement manufacturing business will continue to be the key profit contributor and growth driver from 2006-2008 while property development is expected to make its fresh contribution in 2009 and emerge as another key driver. In our forecast, we expect Luks's earnings to enter an explosive growth period, growing by 97% and 28% in 2007 and 2008, respectively, followed by a stronger growth of 110% in 2009. By the end of 2009, the bottomline should increase to HK\$429mn from FY06E's HK\$81mn.

Earning Forecasts and key figures

| FY Dec (HK\$m) | 2005 | 2006F | 2007F | 2008F | 2009F |
|------------------|--------|-------|-------|-------|-------|
| Net profit | 22 | 81 | 159 | 204 | 429 |
| Basic EPS (HK\$) | 0.05 | 0.16 | 0.31 | 0.40 | 0.84 |
| EPS Gth (%) | (39.2) | 250.3 | 97.5 | 28.0 | 1.1 |
| DPS (HK\$) | 0.08 | 0.05 | 0.06 | 0.08 | 0.17 |
| PER (X) | 144.4 | 41.2 | 20.9 | 16.3 | 7.8 |
| P/Book Value (x) | 3.1 | 3.0 | 2.5 | 2.0 | 1.4 |
| Net Gearing (%) | 0.3% | 1.5% | 10.9% | 17.6% | Cash |
| ROE (%) | 2.1% | 7.4% | 12.9% | 13.4% | 21.5% |

Source: Company, DBS Vickers

- **Valuation still attractive in terms of PE.** Due to the high-growth nature of both Vietnam's cement manufacturing and property development businesses, we believe PE valuation should be a better methodology for assessing Luks Group. Based on our estimation, the stock is trading at forward FY08E PER of 16.3X, not demanding for a high-growth stock. Moreover, the valuation should be further improved in 2009 with the fresh contribution from property development business. The FY09E PER should be as low as 7.8X. NAV methodology can be used as a complementary tool for our valuation of Luks Group. The estimated NAV is HK\$7.4/share. Vietnam cement manufacturing business is the largest contributor, representing 60% of the total NAV. Even though the narrow NAV discount of 12% appears to hinder the stock upside room, we believe the NAV can be significantly improved along with the new property project acquisition. We believe Luks has enough financial muscle to fund the expansion with the net gearing ratio of only 10-15%. Its value may reach 10x FY09F PER due to strong EPS growth.

Luks Group (366.HK)- NAV Valuation

| | USDm | HK\$m | NAV-HK\$/share | % of total NAV |
|---------------------------|--------------|----------------|----------------|----------------|
| Vietnam Cement Business | 270.0 | 2,106.0 | 4.1 | 55.9% |
| Vietnam Investment Proper | 110.3 | 860.1 | 1.7 | 22.8% |
| Vietnam Cement Business | 69.0 | 538.0 | 1.1 | 14.3% |
| Sub-total | 449.2 | 3,504.1 | 6.8 | 93.0% |
| Others | 52.9 | 413.0 | 0.8 | 11.0% |
| Total GAV | 502.2 | 3,917.1 | 7.7 | 103.9% |
| Net debt | (19.0) | (148.0) | -0.3 | -3.9% |
| Total NAV | 483.2 | 3,769.1 | 7.4 | 100.0% |
| Share Price (HK\$) | | | 6.5 | |
| Discount (%) | | | -12% | |

Source: DBS Vickers

ANALYST CERTIFICATION

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