CLSA ASIA-PACIFIC MARKETS

Luks

HK$10.20 - BUY

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31 October 2007

Hong Kong
Property/Cement

Reuters	0366.HK
Bloomberg	366 HK

Priced on 25 October 2007
HK HSI @ 28,373.6

12M hi/lo HK$16.50/3.20

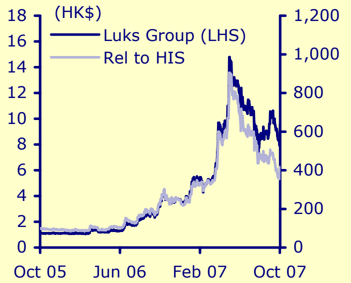
12M price target	HK$13.00
±% potential	+27%
Target set on	23 Oct 07
Shares in issue	573.2m
Free float (est.)	45.0%
Market cap	US$754m

3M average daily volume
HK$23.05m (US$2.96m)

Major shareholders
Management 55.0%

Stock performance (%)

	1M	3M	12M
Absolute	1.4	(5.7)	220.8
Relative	(10.2)	(26.2)	95.1
Abs (US$)	1.6	(4.8)	222.0



Source: Bloomberg

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Free option on Vietnam growth

Hong Kong-listed Luks offers rare and high-quality exposure to Vietnam's rapidly growing economy, where the company owns the Saigon Trade Centre and the sixth-largest cement plant. After recent weakness, the shares appear mispriced, offering a compelling investment opportunity. Investors effectively have a free call option on Vietnam property on top of an established and cash-generating property and cement business. We recently initiated coverage with a BUY rating to our HK$13.00 target.

Tower of strength

Luks' assets include the Saigon Trade Centre, the tallest building in Vietnam, which enjoys 100% occupancy. We believe strong upside exists, with rents of US$27/m² well below comparable-grade rents of US$35-40/m² in Ho Chi Minh City. Luks' cement operations are the nation's sixth largest, after doubling capacity last year. The government recently approved plans to double its potential output again next year.

More projects on the way

Luks is well entrenched in Vietnam. Having first entered the country in the early 1990s and having launched five local JVs this year. The company plans to form two joint-stock companies in Vietnam and to list both on the Vietnamese Stock Exchange by 2010.

Lagging Vietnam play

Following a strong surge in early 2007 owing to Vietnam's ascension into the WTO, Luks' share price has been left behind despite a revitalised Vietnam stock market (up 23% versus just 3% for the stock) since bottoming on 6 August. We attribute this underperformance to three factors. First, Hong Kong small-cap sentiment has been poor versus large caps. Second, we believe the market was overly optimistic on the delivery of a number of future projects in Vietnam. Third, and related to the second point, Luks is still an under-researched small company.

Cheap on existing assets plus free option

Our sum-of-parts target price of HK$13.00 implies 27% upside. Those more cautious about its pipeline should take comfort that Luks is trading slightly below the value of its established business, which we value at HK$10.90 (conservatively valuing cement at US$138/tonne - cheap regionally). We estimate the pipeline value, on a probability adjusted basis, at HK$2.10, which is essentially a free call option on future developments in Vietnam.

Financials

Year to 31 Dec	05A	06A	07CL	08CL	09CL
Revenue (HK$m)	313	374	519	637	775
Net profit (HK$m)	60	59	153	258	555
EPS (HK¢)	12.3	12.0	28.5	45.0	96.9
CL/consensus(EPS%)	-	-	110	78	94
EPS (% YoY)	62.5	(2.6)	138.1	58.1	115.1
PEx (@HK$10.20)	83.0	85.3	35.8	22.7	10.5
Dividend yield (%)	0.3	1.1	1.0	1.2	1.4
FCF yield (%)	2.7	0.6	3.0	(5.0)	10.7
ROAE (%)	5.70	5.20	9.20	11.80	21.90
Price/book (x)	4.8	4.2	2.8	2.6	2.1
Net gearing (%)	(1.14)	(0.88)	(37.43)	(4.74)	(11.59)

Source: CLSA Asia-Pacific Markets

Luks - HK$10.20 - BUY

The business

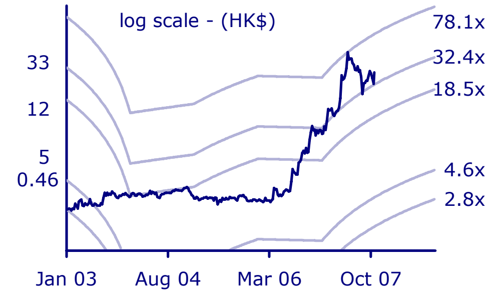
Luks is a cement manufacturer and property manager/developer in Vietnam. The company owns the sixth-largest cement plant in Vietnam and is seeking to double capacity next year (after doubling last year). Luks wholly owns the Saigon Trade Centre, currently the tallest building in Vietnam and has entered into five local JVs to further develop its property portfolio. The company was founded in 1975. It was formerly known as Luks Industrial (Group) and changed its name to Luks Group (Vietnam Holdings) Company in June 2007. The company has been listed on the HKSE since 1987.

Competition & market franchise

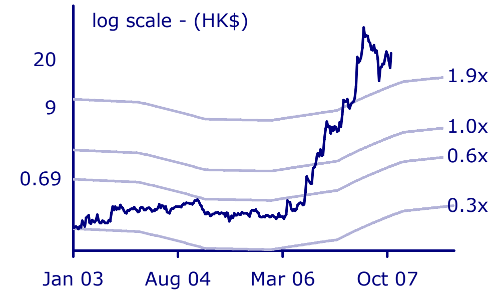
Luks competes in a number of segments: office and residential property and in cement production. In the office market, it owns the Saigon Trade Centre in a market where supply is limited for now. Luks' venture into residential property in Vietnam is new and it is regarded as a small player in a highly fragmented market. In cement, Luks is the sixth-largest player and has a dominant position in central Vietnam. The company also owns its own limestone reserve and clinker production lines, which is uncommon in Vietnam.

Valuation history

PE bands



PB bands



Comment

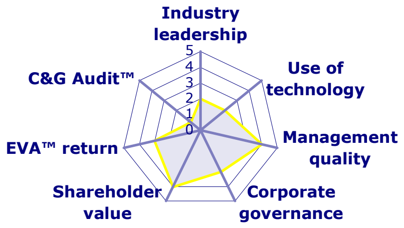
Luks has rerated significantly on a PE basis after Vietnam entered the WTO in January.

The company has since been active in securing JVs and alliances in property development in Vietnam.

We believe investors should focus on the NAV of the parts of the company rather than PE.

Bands (from the top): max, +1sd, avg, -1std, min.

Jet Stream® radar



Corporate governance at Luks

Criteria	Score	Country avg (%)	Country rank	Asia-xJ avg (%)	Sector rank
Discipline	55	64	61	63	35
Transparency	55	75	71	69	34
Independence	62	52	23	44	8
Accountability	50	50	30	44	11
Responsibility	38	63	69	53	35
Fairness	78	64	21	57	3
Social resp	83	85	36	77	15
Wtd CG score	**59**	**64**	**60/84**	**57**	**22/49**

Clean & Green Audit™

Criteria	Score
Leadership	0.00
Recognition	3.00
Disclosure	1.00
Looking to the future	0.00
C&G score/20	**3.14**

For details on methodology and scoring ranges across Asia, see our annual Clean & Green Audit report, which debuted in September 2006.

Outlook	1 year	Comment
***Jet Stream®* criteria**		
Industry leadership	×	Luks is well established in Vietnam in cement, but is not the leader.
EVA™ return	✓	Luks strong returns have only started gaining traction in recent years.
Shareholder value	✓	ROE has steadily increased but more upside is possible following a period of investment.
Corporate governance	✓	High standards set, allowing good corporate access.
Management quality	✓	Focused and experienced.
Use of technology	×	Some technological improvements made in cement production.
CLSA Clean & Green Audit™	×	Aware of implications and quality certified in cement production; has not disclosed C&G targets.
Valuations		
Earnings momentum	✓	We are expecting 134% earnings growth in 2007 and 61% in 2008.
Price/earnings	✓	Trading at 35.8x 07CL EPS. We believe Luks should be valued on an NAV basis.
Price/book value	✓	Trading at 2.8x 07CL BPS. Downside protected by Grade A property and net cash.
Macro factors		
Country risk	×	Vietnam is an emerging economy; regulatory and legislative inefficiencies still to be ironed out.
Strategy	×	We slightly underweight small-caps versus large caps, but we are positive on Vietnam.
Liquidity	✓	Luks liquidity is improving, now at approximately US$3m/day.
Technical analysis		The odds are good that the stock is resuming its long-term uptrend to re-test the May highs. Key support to this view is HK$7.80.
Conclusion	**BUY**	

Existing operations in Vietnam to realise 26% Cagr over next 5 years

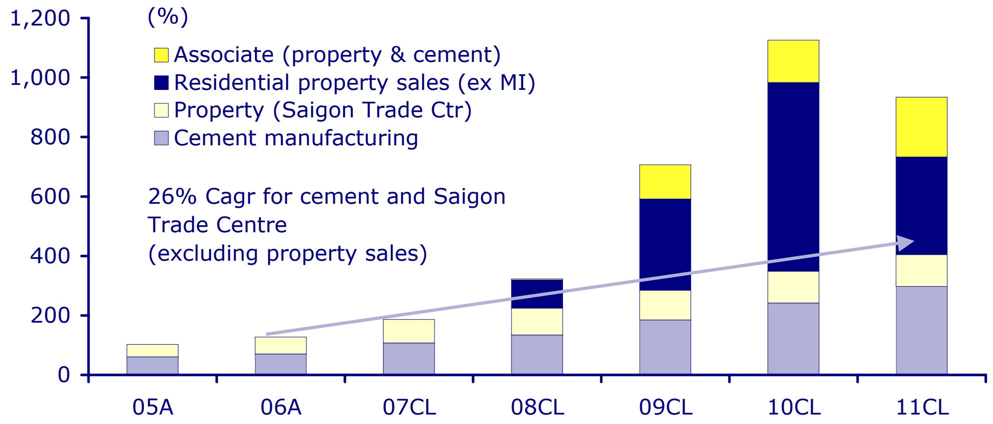
Tower of strength

Luks' assets include the Saigon Trade Centre, the tallest building in Vietnam, which enjoys 100% occupancy. We project strong upside, with rents of US$27/m² well below comparable-grade rents of US$35-40/m² in Ho Chi Minh City, according to property consultants CB Richard Ellis Research (Jul-07). Luks' cement operations are the nation's sixth largest, after doubling capacity last year, and the government recently approved plans to double capacity again next year. The company is leveraged to Vietnam domestic growth. We project a 26% Cagr in existing operations in the country over the next five years.

Cement capacity sets to double again

Figure 1

Existing businesses Cagr of 26% over next five years



Source: CLSA Asia-Pacific Markets

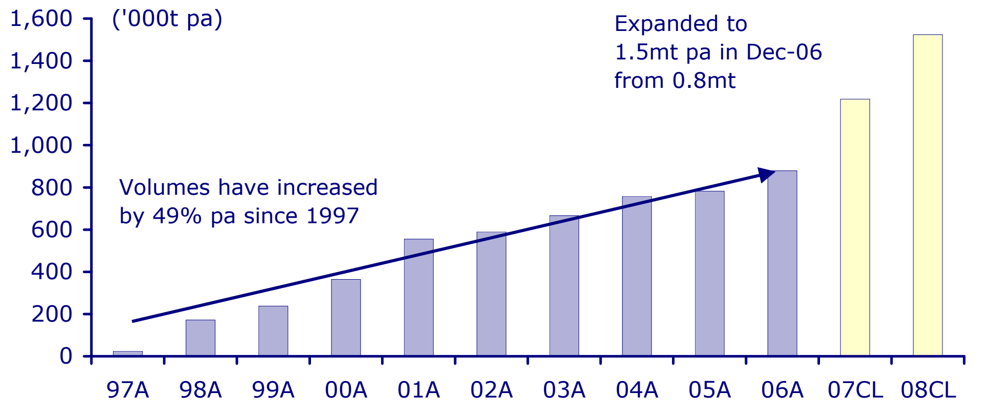
Cementing growth in Vietnam

The key development in Luks' cement-manufacturing business is the recently completed capacity expansion in December 2006, which takes its total annual production capacity to 1.5mt, up from 800,000t. Luks owns 100% of its cement plant, a business the company acquired in full from its JV partner in 2002. We understand this is the sixth-largest cement plant in Vietnam and the largest in the central part of the country. The company also owns a limestone quarry with estimated reserves sufficient for 50 years; ie, a capacity of 3mt a year.

Steady increase since day one, more to come

Figure 2

Cement-production volumes



Source: CLSA Asia-Pacific Markets, Company

Vietnam's cement industry

In 2007, industry demand estimates of 36mt; set to grow 20-25%

Management believes that the cement-manufacturing business in Vietnam is healthy, citing cement shortages in the country of roughly 5mt in 2005 and in 2006. This is based on demand estimates of approximately 32mt annually (was 28mt in 2005, up 14% YoY), with local supply only capable of supplying 27mt. The remaining 5mt (mainly clinker) is imported, with Thailand a key exporter. For 2007, industry observers estimate demand at around 36mt, set to grow 20-25% pa after the country's entry into the WTO this year. We have seen a 49% volume Cagr from Luks' cement plant in Hue since 1997.

Figure 3

Luks cement plant in Hue, central Vietnam

Figure 4

Luks owns this limestone quarry

Source: CLSA Asia-Pacific Markets

Most of Luks' competitors are indirectly state-owned

In Vietnam since early 90s; close ties with provincial governments

While most of Luks' competitors are indirectly state-owned (the Vietnam National Cement Corporation (VNCC) owns up to 70% of the market if one counts its numerous JVs), we do not see this as a risk to Luks for two reasons. Firstly, the company has been established in Vietnam for a long time (since the early 1990s) and secondly, it has close relationships with the provincial governments, especially in Hue, where the company is a key contributor to the local industry. Recent events also confirm our view that Luks is allowed to operate and grow in line with its state-owned peers. For example, approval to expand capacity at the company was fast-tracked by the VNCC and Luks has also entered into a number of strategic JVs with state-owned enterprises to develop cement and property projects.

Barriers to entry in Vietnam's cement industry are high

The industry is also set up in such a way that new entrants require approval from the six ministries and the prime minister, which could prove difficult. To deal with the shortage in cement, the government is encouraging existing manufacturers to expand capacity instead of inviting new players. We understand there are no subsidies or similar support offered by the government other than supportive administrative processes for expansion. We also understand that the pricing environment has been stable and slightly higher (3% in 2006 and 5–7% in 2007), as the government controls the prices of the VNCC given the interest of the government to ensure healthy construction levels. Any price increase requires government approval, and the implementation can be difficult from what we gather.

Luks has two key distribution channels. First, approximately 70% of sales are to dealers (which number in the hundreds) for domestic use. This reflects the company's physical location in central Vietnam. The second channel is direct sales to construction sites, such as for the construction of tunnels, oil refineries, buildings, highways and so forth, which are mostly in southern Vietnam. This does provide a wider gross profit margin of roughly 50% (cement overall is 40%). Luks is looking to increase its sales to the faster-growing southern region by building up a cement-grinding plant at Long An.

Luks cement plant produces all grades of cement

Luks' cement plant produces all grades of cement including PCB30, PC40 and high density cement (eg, tunnel construction). Major projects have included the Hai Van Pass Tunnel, Dung Quat Oil Refineries Plant and numerous highways and hydro-electric power stations in Vietnam. Luks' key cement brand is *Kim Dinh,* which is especially well known in central Vietnam.

Cement performance

In 1H07, Luks' cement volumes increased by 32%, accelerating from 12.5% growth recorded in 2006. The strong expansion in volumes reflects the increased capacity put in place at the end of 2006, up from 0.8mt pa to 1.5mt pa (production was constrained for most of 2006). Luks saw some price increases in the half, which also helped drive Ebitda growth of 43%. Management is not seeing any pressure on the cost side. We note that around 41% of total cost of sales is represented by electricity and coal, with cement gross profit margins around the 42% mark. Ebitda margin widened from 34.7% to 36.4% in 1H07. In the longer term Luks is seeking to build its own power plant, which should result in material cost savings (not factored into our forecast). Stronger volume growth is likely in 2H07 as the new capacity stabilises.

Luks' new capacity of 1.3mt to come on stream from 08CL

Figure 5

Luks cement performance and forecast

(HK$m)	04A	05A	06A	07CL	08CL	09CL
Sales	212	232	275	395	502	628
Sales growth (%)	8.9	9.3	18.5	43.7	27.3	25.0
Ebitda	75	78	93	143	188	236
Ebitda margin (%)	35.4	33.6	33.8	36.3	37.5	37.5
Capex pa	6	112	114	120	341	31
Volume sold (t)	757,000	782,000	880,000	1,218,700	1,523,375	1,904,219
Capacity (t)	700,000	750,000	1,500,000	1,500,000	2,800,000	2,800,000

Source: CLSA Asia-Pacific Markets

STC is the only property exposure in Vietnam generating revenue now

Saigon Trade Centre

The Saigon Trade Centre (STC) is currently the company's only property exposure in Vietnam that is generating a revenue stream. Luks owns 100% of this property after acquiring its JV partner's (Ministry of Defence) 25% stake in 2001.

Luks has 100% ownership of the tallest building in Vietnam

Figure 6

Luks owns the tallest building in Vietnam

Figure 7

View of HCM from the rooftop

Source: CLSA Asia-Pacific Markets

The property is located on 37 Ton Duc Thang Street, right in the heart of the city near two major roads. The building, at 33 storeys, is currently the tallest in Vietnam, has 40,000m² in saleable area and possesses a high-quality tenant mix including Prudential, Thai Military Bank, Chase Manhattan Bank, Standard Chartered Bank, Colgate-Palmolive and Vietnam Airlines, Qantas etc. The building offers office space on the 6^{th} to 30^{th} floors; ground floor and 2^{nd} to 5^{th} floor retail (bank branch on ground floor), roof-top bar and restaurant, and basement car parking.

Figure 8

Saigon Trade Centre performance and forecast

(HK$m)	04A	05A	06A	07CL	08CL	09CL
Sales	47	64	82	109	123	134
Sales growth (%)	26.3	34.6	28.0	33.3	13.0	9.4
Ebitda	22	39	52	71	84	93
Ebitda margin (%)	47.2	60.8	63.8	65.4	68.0	69.0
Occupancy (%)	71	86	95	100	100	100
Rental (US$/m²/mth)	17	20	22	28	32	35
Rental growth (%)	3.2	14.0	12.9	26.6	13.0	9.4

Source: CLSA Asia-Pacific Markets

Valuation of Saigon Trade Centre

There are few if any comparable valuations on office property in HCMC

There are few if any comparable valuations on office property in Ho Chi Minh City (HCMC) in recent times. We take into account three key considerations in arriving at our valuation for the property at US$240m (US$6,000/m²) or HK$3.24 per share to Luks Group:

Reasonable rental yield of 6.5%, cap rate of 6.5%

- We base our valuation on a reasonable expected rental yield of 6.5%, or a capitalisation rate of 6.5%.
- As a cross check, we found a somewhat comparable base-case transaction recently. China Motion Tel (989 HK – NR) acquired a prime commercial site in District 1, HCMC for US$328m, based on the planned development of Time Square, which is to consist of a hotel, apartment and commercial project at a 5-6-star standard. The land-site area is 4,573m², with the project to be 45 storeys high with a GFA of 88,183m². The entire development is likely to be completed in early 2010. The implied price paid per square metre is US$3,720, which in our view is comparable to our US$6,000/m² value, as the project is three to four years away from completion (furthermore, only the piling and foundation work has been completed so far).

Property consultants expect Grade-A rentals to push through US$50/m²

- Strong fundamentals. The STC is currently enjoying an occupancy rate of 100%, up from 95% last year. We found that the average rental per square metre achieved in 1H07 was US$27/month, up from US$20-22/month last year. We believe there is room for significant upside to rentals after our discussion with Luks' management in Vietnam and based on research by CB Richard Ellis (July 2007). The latter source suggests Grade-A rentals in Ho Chi Minh City could push through the US$50/m² mark in 2007 from the average US$39/m² level seen in 1Q07, before stabilising to the upper US$40/m² range. CB Richard Ellis also highlights that estimates of pent-up demand are in the 150,000-200,000m² range and are increasing.

More projects on the way

Entrenched in Vietnam, having first entered the country in the early 90s

Luks is well entrenched in Vietnam, having first entered the country in the early 90s and having launched five local JVs this year. Luks plans to form two joint-stock companies in Vietnam, with the intention to list both on the Vietnamese Stock Exchange in three years (ie, by 2010).

Figure 9

Luks' JVs with local partners

Local partner	Project	Luks interest (%)	GFA (m²)
Thanh Phat	Residential property development	70	115,000
Hong Phuc	Residential property development	90	73,000
CNS	Residential property development	30	146,400
CNS	Cement	45	na
Indochine	Residential property development	95	167,787

Source: CLSA Asia-Pacific Markets

A less well known fact is that Luks does have property-development experience dating back to 1991 in China. Some projects developed by Luks include Shenzhen Lo Wu Commercial City and Shenzhen Jinfeng City and several residential estates in Chengdu.

JV with Thanh Phat and Hong Phuc

Partnering with local firms to grow property, cement businesses

Luks announced in January 2007 the formation of two JVs with local partners to develop two residential properties for sale located in An Lac Ward, Binh Chanh District (115,000m² GFA) and Thao Dien Ward, District 2 (73,000m² GFA). We value the two JVs on a DCF basis, taking into account land cost, construction cost and eventual sale price, discounted back to a present value basis. Our valuation of both projects for Luks is HK$418m (HK$0.73/share).

We estimate Thanh Phat and Hong Phuc JVs to be worth HK$0.43 per share

Figure 10

Project valuation – Thanh Phat and Hong Phuc JVs

An Lac Ward, Binh Chanh District, HCMC (HK$m)				
Luks' interest (%)	70			
Gross floor area (m²)	115,000			
Key assumptions				
Land/construction costs (US$/m²)	350			
Sale price	800			
Profit & loss impact	**07CL**	**08CL**	**09CL**	**10CL**
Revenue (other income)		135	135	135
Minority interest		(40)	(40)	(40)
Capex		(63)	233	233
NPV @ 10% + 20% discount	244			
Luks' interest	171			
Value per share (HK$)	**0.30**			
Thao Dien Ward, District 2, HCMC (HK$m)				
Luks interest (%)	90			
Gross floor area (m²)	73,000			
Key assumptions				
Land/construction costs (US$/m²)	370			
Sale price	1,200			
Profit & loss impact	**07CL**	**08CL**	**09CL**	**10CL**
Revenue (other income)	0	0	236	236
Minority interest	0	0	(24)	(24)
Capex	0	0	(95)	(95)
NPV @ 10% + 20% discount	274			
Luks' interest	247			
Value per share (HK$)	**0.43**			

Source: CLSA Asia-Pacific Markets

JV with CNS

Luks entered into an MOU with CNS, a Vietnam-incorporated company which belongs to the Industry Department of Ho Chi Minh City on 18 May 2007. CNS is engaged in a number of industries such as mechanics, electronics, food-processing, investment and infrastructure projects in Vietnam. We value the CNS JV on the announced property and cement projects to be worth HK$623m, or HK$1.08 per share.

Intention to list on the Vietnamese stock exchange in three years

The CNS agreement essentially involves setting up a cement and property business: Luks and CNS will form two joint-stock companies to invest in cement and property projects in Vietnam. In addition, both parties will manage the joint-stock companies with a view to listing both on the Vietnamese stock exchange in three years time. Importantly for Luks, the agreement sets out a rough plan to cooperate on other projects including: investment in a thermal power plant; construction of industrial zones; and investment in an ecological resort.

CNS cement project

To form a joint-stock company to invest in cement in Vietnam

Luks and CNS will form a joint-stock company to invest in cement projects in Vietnam, with Luks owning 45% of the business. The first project will involve the construction of a cement-grinding factory with a 3mt pa capacity, a new clinker production line with a 1.25mt annual capacity, and limestone mining rights. We forecast that this project will come on stream only in June 2008, achieving 250,000t in 2008, with full completion in two years, or by mid-2009.

We estimate CNS Cement JV to be worth HK$1.00 per share

Figure 11

Project valuation - CNS cement

(HK$m)	08CL	09CL	10CL	16CL
Profit& loss contribution				
Sales	98	234	304	1,170
Ebitda	34	82	106	409
Depreciation	24	25	25	57
Ebit	10	57	81	352
Tax	(1)	(9)	(12)	(53)
NPAT	8	49	69	299
NPAT to Luks (associate profit)	4	22	31	135
Capex pa	483	15	15	30
Volume sold (t)	250,000	600,000	780,000	2,999,737
Capacity (t)	1,500,000	1,500,000	1,500,000	3,000,000
Valuation				
Free cashflow	(454)	55	75	318
Discount rate (%)	10.0			
Terminal growth rate (%)	4.0			
Enterprise value	2,561			
Implied EV/t (US$)	109			
Luks' interest (%)	45.0			
Probability factor (%)	50.0			
Luks' interest - 45%	576			

Source: CLSA Asia-Pacific Markets

Our valuation for the entire project is HK$2.6bn, of which Luks' 45% interest equates to HK$1.15bn. To be conservative, given the relatively long-dated completion of the project, we have assigned a probability factor of 50% to our valuation, giving us a valuation of HK$576m (HK$1.00/share). The implied EV/t is US$109. In terms of P&L impact, this is likely to be reflected as a share of profit from associate companies.

Second joint-stock company to invest in and develop property

CNS property project

Luks and CNS will form another joint-stock company to invest in and develop property in Vietnam, starting with an existing land plot, with more to come from CNS. Our discounted NAV valuation for the announced landbank of 18,300m² is HK$311m, of which Luks' 30% interest equates to HK$93m. To be conservative, given the relatively long-dated completion of the project, we have assigned a probability factor of 50% to our valuation, giving us a valuation of HK$46.5m (HK$0.08/share).

We estimate CNS Property JV to be worth HK$0.08 per share

Figure 12

Project valuation - CNS property

Group interest (%)	**30**				
Sites (m²)					
1. 11/121 Le Duc Tho St, Ward No 17, Go Vap District, HCMC	10,000				
2. 242 Tran Phu St, District 5, HCMC	2,300				
3. 52 Thanh Thai, District 10, HCMC	6,000				
Total land area	18,300				
Plot ratio	8				
Gross floor area	146,400				
(US$m)		**08CL**	**09CL**	**10CL**	**11CL**
Estimated construction cost @ US$300/m²		(11.0)	(32.9)		
Other costs @ US$22/m²			(1.1)	(1.1)	(1.1)
Sale on completion @ US$900/m²			43.9	43.9	43.9
Cashflow after tax		(9.3)	8.4	36.4	36.4
PV of cashflow @ 10% discount rate		(8.3)	6.8	26.9	24.4
Profit & loss contribution					
(US$m)		**08CL**	**09CL**	**10CL**	**11CL**
Revenue			44	44	44
Construction/land costs			(16)	(16)	(16)
NPAT			24	24	24
(HK$m)					
Capex		25.7	79.6	2.5	2.5
NPAT			187.0	187.0	187.0
NPAT to Luks (associate profit)			93.3	56.1	56.1
NPV	388.6				
Post-20% discount to NPV	310.9				
Valuation	93.3				
Probability factor (%)	50				
Luks' interest, 30%	46.6				

Source: CLSA Asia-Pacific Markets

JV with Indochine, a Vietnamese company

JV with Indochine

On 29 August 2007, Luks' wholly owned subsidiary Luks Land has entered into a JV with Indochine, a Vietnamese-incorporated company, to develop residential and commercial property in Vietnam.

The land, injected into the JV by Indochine, is located at Truong Thanh Ward, District 9, Ho Chi Minh City, Vietnam, measuring 159,737m². The land relates to three sites of 38,983m², 68,796m² and 51,958m², which includes a 19,851m² watercourse area. The estimated plot ratio is 1.05x, which suggests a GFA of 167,787m². Management has also indicated that the plot ratio could change (ie, rise).

In terms of the JV agreement, Indochine contributes the land, while Luks pays (to Indochine directly) the cost of gaining the approval from all relevant authorities for the investment to proceed (including permits, etc) and compensation for the removal of existing residents and structures on the land to get it ready for piling (estimated compensation rate is US$93.89/m²).

Construction to begin from late 2009

In its circular released by Luks on the announcement of the JV on 29 August 2007, the company stated that Indochine had obtained approval from the People's Committee of District 9 of Ho Chi Minh City, Vietnam to implement the project, and had also obtained approval for construction from the Department of Planning and Architecture. The application to set up the JV will only be made once compensation for the land had been completed. We are expecting construction to only begin from late 2009 as we believe the land approval/permit process is still a challenging and tedious task. In addition, we understand the land sites still require the basic infrastructure to be built including road, sewerage and electricity.

Figure 13

Indochine JV – capital required

(US$m)	Luks	Indochine	JV	Comment
Share of JV (%)	95	5	100	
Land contribution	No	Yes		Indochine contributes the land into the JV
Charter capital	4.8	0.3	5.0	Luks will advance US$3m as initial compensation to land owners
Shareholder loans to JV	10.2	0.5	10.7	Contribution to be made in stages to land users, within two years
Total consideration	**15.0**	**0.8**	**15.7**	
Planned investment[1]	13.5	0.7	14.3	Including construction costs
Total investment	**28.5**	**1.5**	**30.0**	

[1] Preliminary estimates. Source: CLSA Asia-Pacific Markets, Company

Total investment capex of US$60m, double management's US$30m

On arriving at our valuation we have incorporated a 20% discount to NAV. Our NAV is based on a DCF valuation of the project, for which we assume project construction from 2008 and completion by 2011. We have also forecast a land and construction cost of US$372/m², or a total investment capex of US$60m, double the US$30m estimate given by the company. Our projected sale price of the property is US$900/m².

We estimate the Indochine JV to be worth HK$0.43 per share

We are valuing the entire JV at HK$370m, of which Luk's 95% interest equates to HK$351m. We also assign a probability factor of 70% to account for some uncertainty, which brings our valuation down to HK$246m, representing (HK$0.43/share).

Figure 14

Project valuation - Indochine JV

Truong Thanh Ward, District 9, HCMC					
Luks interest (%)	95				
Gross floor area (m²)	167,787				
Key assumptions (HK$m)					
Land / construction costs (US$/m²)	372				
Sale price	900				
Profit & loss impact (HK$m)	**07CL**	**08CL**	**09CL**	**10CL**	**11CL**
Revenue (other income)	0	0	0	346	346
Minority interest	0	0	0	(17)	(17)
Capex	0	0	0	(231)	(231)
NPV @ 10% + 20% discount	370				
Luks' interest	352				
Probability factor (%)	70				
Adjusted valuation	246				
Value per share (HK$)	0.43				

Source: CLSA Asia-Pacific Markets

Lagging Vietnam play

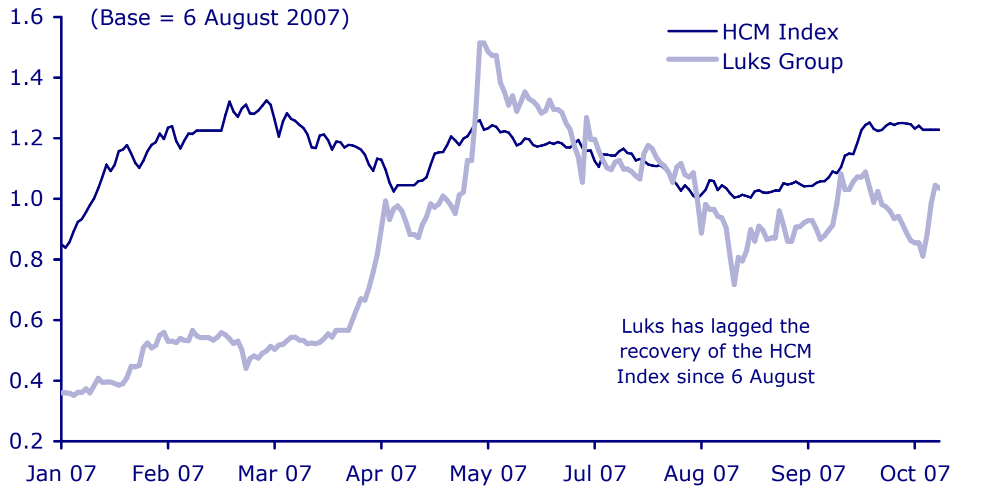
Share price left behind despite a revitalised Vietnam stock market

Luks' share price has been left behind despite a revitalised Vietnam stock market (up 23% vs just 3% for the stock) since bottoming on 6 August. We attribute Luks' underperformance to three factors. Firstly, HK small-cap sentiment has been poor vs large caps. Secondly, we believe the market was overly optimistic on the delivery of a number of future projects in Vietnam. Thirdly, and related to the second point, Luks is still an under-researched small company.

Up significantly in early 2007 following Vietnam's ascension into the WTO

Figure 15

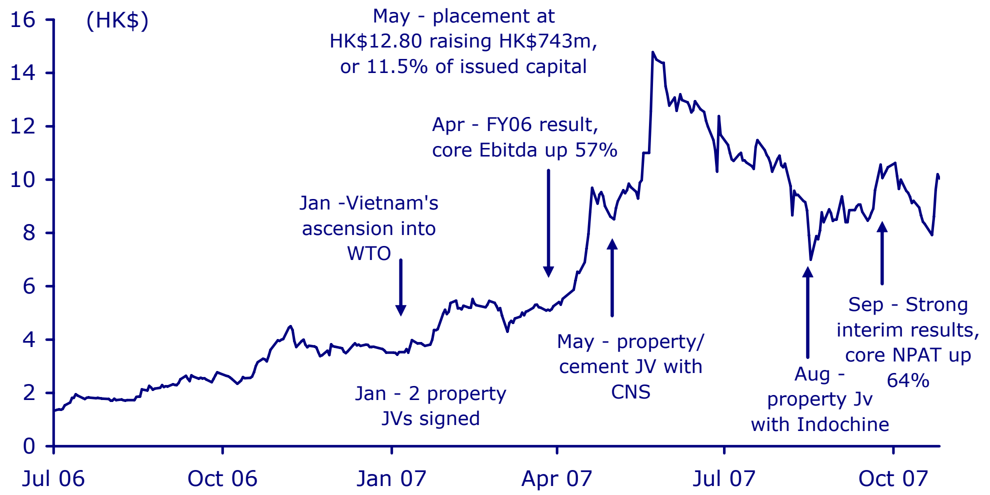
Lagging Vietnam play – Relative price performance



Recent weakness due to poor small-cap sentiment and lack of research

Figure 16

Share-price performance and key events



Source: CLSA Asia-Pacific Markets

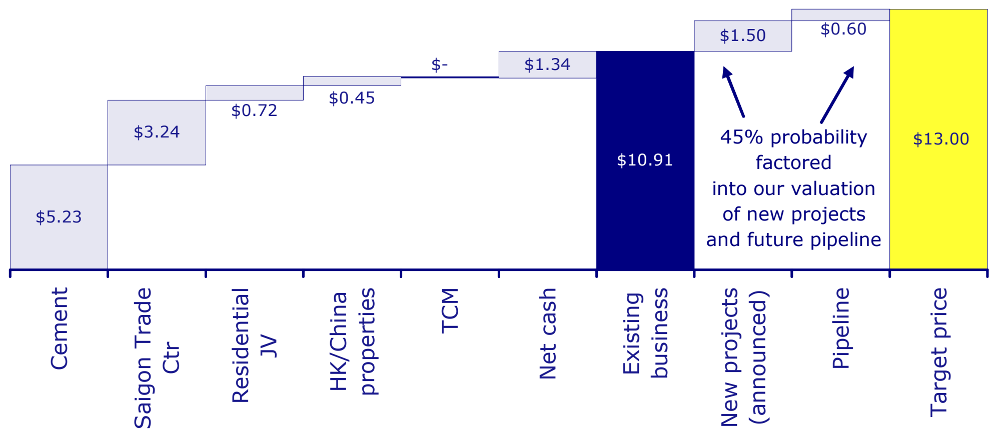
Cheap on existing assets plus free option

Current share price presents a free call option on Vietnam property and infrastructure growth

Our fair value and price target for Luks is HK$13.00, based on a sum-of-parts valuation, including HK$10.90 for existing businesses and HK$2.10 for the future project pipeline. We believe the current share price presents an attractive investment opportunity. Essentially, investors can buy Luks at a 7% discount to the valuation of the existing business, which is cash-generative and contains HK$1.34 in net cash. In addition, investors are granted a free call option on future developments in Vietnam that have already been announced by the company, mainly in property and cement. We estimate this option to be worth HK$2.10 per share, probability adjusted.

Figure 17

Sum-of-parts valuation



Note: Our valuation captures both existing business and future value of new projects (probability adjusted). Source: CLSA Asia-Pacific Markets

Figure 18

We employ a sum-of-parts valuation methodology

Sum-of-parts valuation assumptions

	Valuation approach	(HK$m)	(HK$/shr)
Existing business:			
Cement	DCF @10% DR, implied EV/t US$138 based on 2.8mt capacity	3,024	5.23
Saigon Trade Centre	NAV at 6.5% cap rate (rental US$32/m²) implies NAV/m² of US$6,000	1,872	3.24
Residential property JV	20% disc to DCF	418	0.72
Other properties	Reported book value	260	0.45
Chinese Medicine	DCF	(42)	(0.07)
Add: Net cash	07CL	775	1.34
Sub-total (existing business)		6,307	10.90
Announced projects:			
CNS JV Cement, 45% interest	DCF, EV/t of US$109 based on 3mt capacity, 50% probability	576	1.00
CNS JV Property, 30% interest	20% disc to DCF, 50% probability	47	0.08
Indochine JV Property, 95% interest	20% disc to DCF, 70% probability	246	0.43
Sub-total (existing business + announced projects)		7,183	12.40
Projects in the pipeline:			
Commercial/residential projects	20% disc to DCF, 30% probability	347	0.60
Total equity value		7,522	
No of shares & options (m)			579
Valuation per share			13.00
Current share price			10.20
Upside to valuation (%)			27.5

Source: CLSA Asia-Pacific Markets

Valuation scenarios

We find that Luks is currently trading on par with our bear-case valuation scenario and at a 38% discount to our bull-case valuation.

Luks is trading at a 38% discount to our bull-case valuation scenario

Figure 19

Valuation scenarios

HK$ per share	Base-case	Bull-case (no NAV discount and no probability weighting)	Bear-case (zero value on new projects)
Existing business:			
Cement	5.23	5.23	5.23
Saigon Trade Centre	3.24	3.24	3.24
Residential property development	0.72	**0.89**	**0.00**
Other properties	0.45	0.45	0.45
Chinese Medicine	(0.07)	(0.07)	(0.07)
Announced projects:			
CNS JV Cement	1.00	**1.99**	**0.00**
CNS JV Property	0.08	**0.20**	**0.00**
Indochine JV Property	0.43	**0.80**	**0.00**
Future pipeline:			
Commercial/residential projects	0.60	**2.49**	**0.00**
Net cash	**1.34**	**1.34**	**1.34**
Value per share	**13.00**	**16.56**	**10.18**
Discount to valuation (%)	**(22)**	**(38)**	**0**

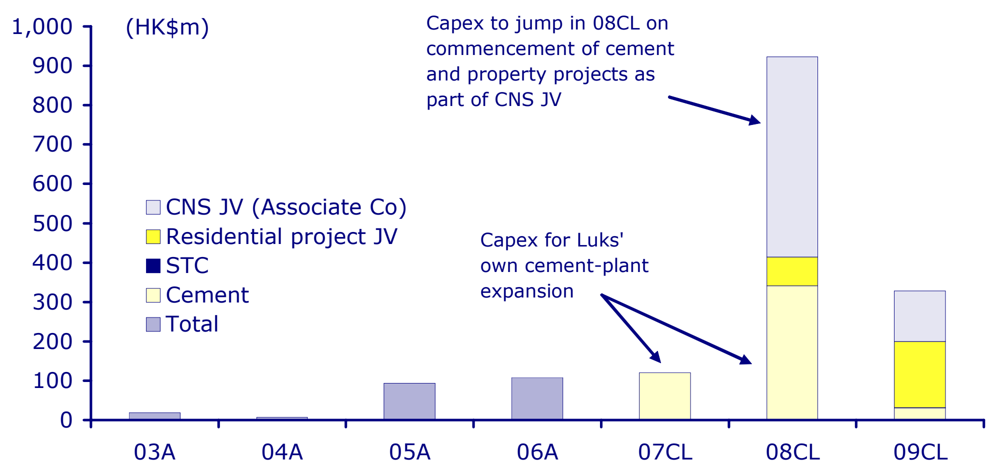
Source: CLSA Asia-Pacific Markets

Return on capital to accelerate

Preparing to deploy capital into property, cement in Vietnam

Figure 20

Large capex from 2008

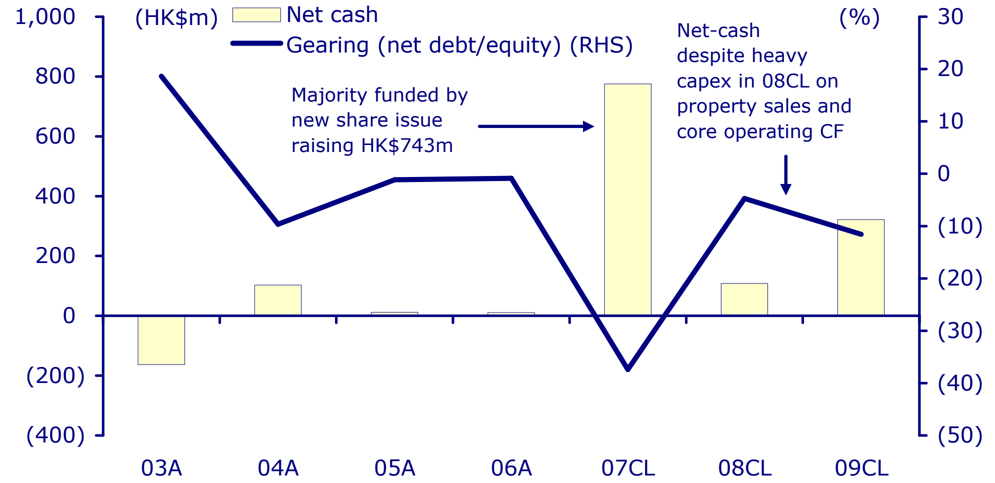


Source: CLSA Asia-Pacific Markets

Well funded from internal cashflow thanks to capital raising earlier this year

Figure 21

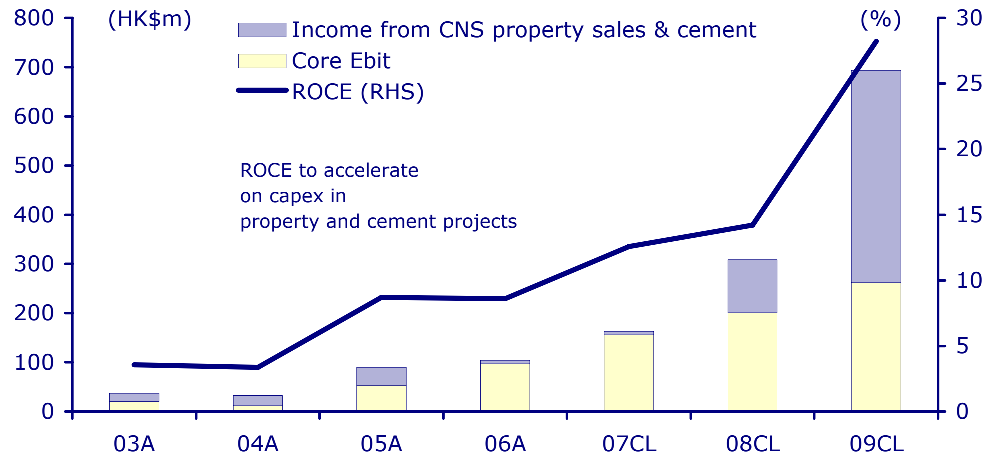
Healthy balance sheet from internal funds and operating cashflow



Strong ROCE increase on the deployment of capital in next 2-3 years

Figure 22

ROCE is set to increase to more than 25% from less than 10% currently



Source: CLSA Asia-Pacific Markets

Luks Group Vietnam Holdings has enjoyed a near vertical accent since clearing overhead resistance at HK$1.40 in July 2006. The stock peaked at HK$16.50 in May and has worked through a corrective phase which has recently bounced off long-term trendline support. The odds are good that the stock is resuming its long-term uptrend to re-test the May highs. Key support to this view is HK$7.80. A break below this level would suggest a move down to HK$5.77

Appendix 1: What the charts say

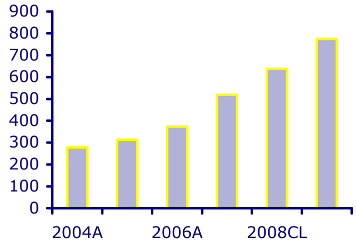
Luks Group weekly with 40-week WMA

Source: CLSA Asia-Pacific Markets

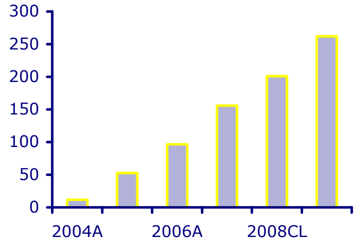
These views are based on technical analysis and may or may not be in agreement with the 'fundamental' view.
For further information please contact
Laurence Balanco, Analyst, Asian Technical Research
Tel: (852) 26008576 e-mail: laurence.balanco @clsa.com

Appendix 2: Risks & drivers

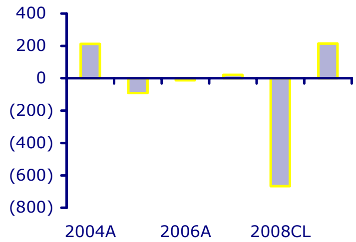
Sales (HK$m)



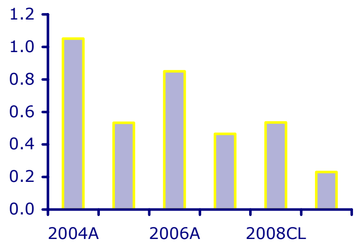
Op profit (HK$m)



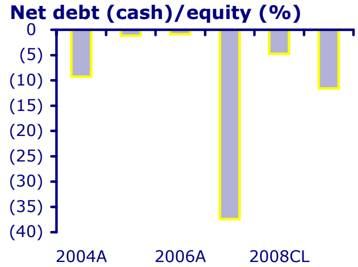
Net cashflow (HK$m)



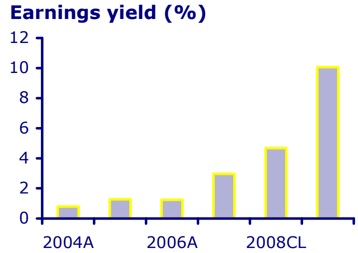
Debt coverage (years)



Net debt (cash)/equity (%)



Earnings yield (%)



Investment by numbers

We are a forecasting revenue Cagr of 27.5% for the next three years, driven mainly by the expansion of Luks' cement business (capacity doubling again) and Saigon Trade Centre (rentals growing 16% pa). We are also expecting residential property sales to begin feeding through from 2008 (HK$134m), which we recognise as 'other revenue' in our forecast. In addition, we also forecast the contribution from a number of JVs to be recognised under associate profit.

We expect operating profit to be driven by cement (three-year Cagr of 38%), Saigon Trade Centre (21%) and the first-time property sales contribution from 08CL. We project residential property sales proceeds after deducting minority interests to account for 14% of earnings in 08CL and 50% in 09CL.

In terms of returns, we forecast ROAE to increase from 5.2% in 2006 to 21.9% by 09CL. While Luks has a large capex program ahead, particularly in 08CL, the company has sufficient net cash on its balance sheet (HK$700m) that will also be supported by ongoing cashflow from existing operations (cement and Saigon Trade Centre).

Risks to our view

Luks has entered into five JVs with local parties this year to develop property and build another cement production line. We acknowledge there is some uncertainty as to when the projects will be completed (all expected by 2010), which is why we have incorporated a probability weighted discount in our valuation for each of the projects. Our aggregate discount to the valuation of the pipeline projects is 45%, resulting in the total pipeline valued at HK$2.10, contributing to our total fair value of HK$13.00.

Most of Luks' competitors in cement are indirectly state-owned. However we do not see this as a risk to Luks for two reasons. Firstly, Luks has been established in Vietnam for a long time (since mid-90s) and secondly, it has close relationships with the provincial governments, especially in Hue, where the company is a key contributor to the local industry. Recent events also confirm our view that the company is allowed to operate and grow in line with its state-owned peers.

Vietnam is an emerging economy, and while there have been major reforms (ie, shift to free market), regulatory and legislative inefficiencies still need to be ironed out.

Key earnings drivers

Year to 31 December	2005A	2006A	2007CL	2008CL	2009CL
Cement capacity (mt)	750,000	1,500,000	1,500,000	2,800,000	2,800,000
Utilisaton (mt)	782,000	880,000	1,218,700	1,218,700	1,218,700
Sale price (US$/t)	38.0	40.0	41.5	42.3	42.3
Saigon Trade Ctr					
Rental (US$/m²)	19.8	22.4	28.3	28.3	28.3
Occupancy (%)	86	95	100	100	100
Capex (HK$m)	93.0	107.9	120.4	923.3	328.6

Appendix 3: Summary financials

Summary P&L forecast (HK$m)

Year to 31 December	2005A	2006A	2007CL	2008CL	2009CL
Revenue	**313**	**374**	**519**	**637**	**775**
Operating Ebitda	73	115	194	257	315
Operating Ebit	53	97	156	201	262
Interest income	3	5	16	27	20
Interest expense	(6)	(11)	(9)	(16)	(20)
Other items	37	3	5	146	493
Profit before tax	**87**	**94**	**168**	**357**	**755**
Taxation	(23)	(37)	(15)	(59)	(136)
Minorities and other	(3)	2	0	(40)	(64)
Profit	**60**	**59**	**153**	**258**	**555**
Summary cashflow forecast (HK$m)					
Operating Ebit	**53**	**97**	**156**	**201**	**262**
Depreciation/amort	20	19	38	56	53
Working capital - trade	14	58	(6)	(7)	(9)
Other operating items	146	5	105	429	785
Operating cashflow	**233**	**178**	**293**	**680**	**1,091**
Net interest/taxes/other	(6)	(42)	(8)	(48)	(136)
Cashflow	**227**	**136**	**285**	**632**	**955**
Capital expenditure	(93)	(108)	(120)	(923)	(329)
Acq/inv/disposals	(47)	1	0	0	0
Free Cashflow	**87**	**30**	**165**	**(292)**	**627**
Ord div paid/Other items	(178)	(31)	600	(376)	(413)
Decrease in net debt	(91)	(1)	765	(667)	214
Summary balance sheet forecast (HK$m)					
Cash & equivalents	133	127	908	446	542
Debtors - trade	20	25	50	61	74
Inventories - trade	13	19	13	16	20
Other current assets	0	0	0	0	0
Fixed assets	400	482	565	1,432	1,707
Intangible assets	94	16	16	16	16
Other term assets	691	925	925	925	925
Total assets	**1,351**	**1,594**	**2,477**	**2,896**	**3,285**
Short-term debt	58	77	89	226	147
Creditors - trade	25	20	33	40	49
Other current liabs	85	112	112	112	112
Long-term debt/CBs	63	38	44	112	73
Other long-term liabs	73	127	127	127	127
Minorities/other equity	0	(2)	(2)	(2)	(2)
Shareholder funds	1,046	1,221	2,074	2,280	2,778
Total liabs & equity	**1,351**	**1,594**	**2,477**	**2,896**	**3,285**
Ratio analysis					
Revenue growth (%)	12.6	19.4	38.9	22.8	21.6
Op Ebitda growth (%)	11.6	57.2	68.2	32.7	22.4
Op Ebit growth (%)	347.3	82.5	61.1	29.0	30.3
Op Ebitda margin (%)	23.4	30.9	37.4	40.4	40.6
Op Ebit margin (%)	16.9	25.9	30.0	31.5	33.8
Net profit margin (%)	19.3	15.9	29.4	40.5	71.7
Dividend payout (%)	24.4	91.1	36.8	27.8	14.5
Tax rate (%)	26.8	39.0	9.0	16.5	18.0
Ebitda/net int exp (x)	25.2	20.7	(28.4)	(24.2)	390.1
Net debt/equity (%)	(1.1)	(0.9)	(37.4)	(4.7)	(11.6)
Gross debt/equity (%)	11.6	9.5	6.4	14.8	7.9
Net debt/op Ebitda (x)	(0.2)	(0.1)	(4.0)	(0.4)	(1.0)
Gross debt/op Ebitda (x)	1.7	1.0	0.7	1.3	0.7
Return on equity (%)	5.7	5.2	9.3	11.9	22.0
ROCE (%)	8.8	8.9	12.9	20.0	32.7
Return on assets (%)	4.5	4.0	7.5	9.6	18.0

Other items include property sales. Investors should also note the associated minority interest distribution as Luks has entered into five local JVs in Vietnam.

We expect Luks' capex program to begin mostly from 08CL, with a focus on property development and expansion of its cement-production capacity.

Strong operating Ebitda growth in 07CL supported by 58% growth in 1H07.

Our cashflow projection does not suggest Luks needs to raise more capital in the near term, aside from any acquisitions.

Appendix 4: Recommendation history

Luks Group (Vietnam Holdings) 366 HK

Date	Rec level	Closing price	Target
23 October 2007	BUY	7.92	13.00

Source: CLSA Asia-Pacific Markets

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