SOLIDERE

BLOMINVEST BANK S.A.L.

Equity Research

Sector:	Real Estate	Share Price (USD):	22.86
Country:	Lebanon	Fair Value (USD):	31.00
Date:	May 17, 2010	Upside:	36%
		Recommendation:	BUY

Initiating coverage with a BUY Recommendation and a Fair Value of USD 31 per share based on the 4 channels of analysis below

Business Model

Solidere holds a monopolistic position in a very attractive and highly appreciating real estate market located in Beirut Central District (BCD). Its revenue is mainly driven by land and real estate sales in BCD but is evolving to a recurring revenue through an expansion in rental properties. Solidere is aiming to leverage its strong brand and expertise in real estate development and master planning through its associate, Solidere International, which operates regionally.

Financials

Profit Margins are considerably high at Solidere when compared to its regional peers. This is due to having booked its entire land bank in 1994 which allows it to hold its costs steady as real estate prices continue to rise. Solidere enjoys high liquidity and low leverage on its balance sheet as part of its strategy to withstand economic and political threats in the country. Its interest coverage ratio has never declined below 8 which allows us to treat Solidere as a safe equity investment.

Valuation

We estimate the fair value of Solidere's share at USD 31.00 with a 36% upside potential. Most of the value relies on Solidere's land bank which still contains 1.9 million sqm of unsold or undeveloped area. We valued Solidere International at Book due to the challenges its projects are experiencing outside of Lebanon. When comparing Solidere to its peers, we find that the valuation multiples are slightly higher. This is expected due to the fact that it enjoys a monopoly position in Beirut and much less exposure to the financial crisis.

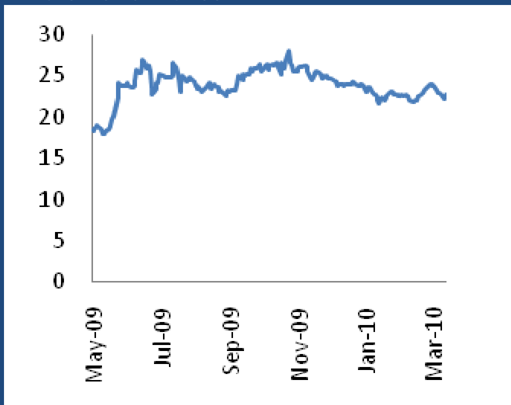
Economic

In 2009, Lebanon boasted an 8 % GDP growth accompanied by a moderate inflation and a flourishing economic activity. Housing demand remains strong and emanates from end-users not speculators due to regulations set by monetary authorities to immunize the sector against the regional turbulence. Construction activity has been vigorous echoing efforts deployed by developers to match the expansion of demand.

Share Data

Bloomberg Symbol	SOLDA.LB
Reuters Symbol	SOLA.BY
Market Cap	3,468,640,000
Number of Shares	152,000,000
Free Float	92.1%
Price-to-Earnings 09e	18.62
Price-to-Book 09e	2.01

Share Performance



1 Month Return	-1.96%
3 Month Return	1.16%
6 Month Return	-7.03%
12 Month Return	24.59%
52 Week Range	27.91 – 15.96

Performance and Forecasts

Year	2008	2009e	2010e	2011f	2012f	2013f
Revenues (USD millions)	286	340	368	412	451	509
Net Income (USD millions)	183	196	224	251	272	307
EPS (USD)	1.18	1.29	1.47	1.65	1.79	2.02
BVPS (USD)	11.97	11.90	11.82	11.65	11.36	11.11
ROA	6%	7%	8%	9%	10%	11%
ROE	10%	11%	12%	14%	16%	18%

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FINANCIALS & VALUATION

Year	2008	2009e	2010e	2011f	2012f	2013f
Profit & Loss Summary						
Revenue (USDm)	286	340	368	412	451	509
Revenue Growth (%)	-8.3	18.9	8.1	11.9	9.6	12.8
Gross Profit (USDm)	207	243	280	312	338	380
Gross Margin (%)	72.4	71.5	76.1	75.7	75.0	74.7
Net Profit (USDm)	183	196	224	251	272	307
Profit Margin (%)	64.0	57.6	60.9	61.0	60.3	60.3
Net Profit Growth (%)	-18.3	7.0	14.4	12.2	8.4	12.7
Earnings Per Share (USD)	1.18	1.29	1.47	1.65	1.79	2.02
Price-to-Earnings (Forward P/E)	19.37	17.72	15.49	13.81	12.74	11.31
Balance Sheet Summary (USDm)						
Cash & Cash Balances	292	170	252	265	271	285
Accounts & Notes Receivables	296	370	331	350	361	382
Inventory of Land & Real Estate	1,274	1,114	1,048	972	822	664
Investment Properties	217	366	366	366	429	491
Other Assets	374	389	398	409	419	430
Total Assets	2,453	2,409	2,395	2,361	2,302	2,252
Total Liabilities	594	600	599	590	575	563
Book Value Per Share (USD)	11.97	11.90	11.82	11.65	11.36	11.11
Profitability						
ROA (%)	6.2	6.8	7.9	9.0	9.9	11.5
ROE (%)	9.9	10.7	12.4	14.1	15.6	18.0
Liquidity						
Cash / Current Liabilities	0.49	0.28	0.42	0.45	0.47	0.51
Current Assets / Current Liabilities	1.06	0.97	1.05	1.13	1.19	1.30
Net Working Capital / Current Assets	0.06	(0.03)	0.05	0.11	0.16	0.23

Comparables

	Valuation			Margin Analysis (%)			Profitability (%)	
	P/E	P/Rev	P/BV	Gross	Operat.	Net	ROE	ROA
Solidere	18.6	10.7	2.0	71.5	63.6	57.6	10.8	8.1
Average of Peers	15.5	6.6	1.5	55.6	42.5	41.1	11.7	4.3

Valuation

	USDm	USD/shr	FV %
Value from Sales of Traditional Land	842	5.4	17
Value from Sales of Reclaimed Land	4,146	26.7	86
Value from Rentals	552	3.6	12
Book Value of Solidere International	310	2.0	6
Book Value of Non-Operating Assets	616	4.0	13
Total Liabilities	(600)	(3.9)	-12
Value Loss from General & Admin.	(475)	(3.1)	-9
Tax Effect	(677)	(4.4)	-14
Fair Value	4,714	31.00	100%

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INVESTMENT SUMMARY

We are initiating a BUY recommendation on Solidere shares after carefully analyzing the essential factors that would classify an equity as investment grade.

Macroeconomic Environment

While the global economy shrank by 0.8 %, we estimate that Lebanon registered an 8 % growth of its gross domestic product (GDP) in 2009. The two main factors that contributed to this growth are the return to political stability and the growing capital inflows by investors seeking to diversify their portfolio away from markets impacted by the financial crisis. The real estate sector mirrored the economic performance in the country driven by demand from locals, expatriates, and Gulf Arabs. Demand remains strong and emanates from end-users with real housing needs. Speculation is limited due to regulations set by monetary authorities to immunize the sector against the regional turbulence. To match the expansion of demand, construction activity has been vigorous echoing efforts deployed by developers.

Business Model

Solidere enjoys a monopoly position in the Beirut city center where its mission is to rebuild and develop the Beirut city center after it had been torn during the Lebanese civil war. It is the master planner for all real estate and infrastructure development in the 4.7 million squared meter (sqm) area that constitutes the Beirut Central District (BCD). Most of Solidere's revenues are generated through land and real estate sales and are expected to remain so in the near future. Out of its 4.0 million sqm of land, 1.9 million sqm are still either unsold or undeveloped and have an estimated depletion period of 10 to 15 years depending on demand and the company's strategy.

Rental Income is growing considerably as Solidere focuses on generating recurring revenues from its properties. Instead of selling to developers, it is leasing retail, office, and residential units to the end-consumer and has set a target of USD 100 million to be reached by 2015.

Type of Land	Size (million sqm)	Remaining (million sqm)	Estimated Price/sqm in USD
Traditional	2.3	0.4	3,500
Reclaimed	1.7	1.5	5,000
Total	4.0	1.9	

Source: Solidere

Profitability

Solidere enjoys a very unique situation in BCD where its real estate acquisition costs cannot grow since it booked most of the property at inception (Estimated at USD 505/sqm). This has caused its gross margins from land and real estate sales to continuously increase as land and real estate prices naturally rise with time and inflation. Solidere has never had an earnings deficit during the past 9 years. Its profit margins are among the highest in the industry and will continue to rise as it begins recognizing sales from the 1.5 million sqm reclaimed area. Earnings-Per-Share (EPS) have grown almost 70% from USD 0.69 in 2005 to USD 1.18 in 2008 with a Compounded Annual Growth Rate (CAGR) of 19.74%. This EPS growth is not only a result of growing profits but also of Solidere's stock buyback strategy where the company has continuously increased its ownership and currently holds almost 8% of all shares.

Return-on-Equity (ROE), another key indicator for profitability, has enjoyed double digit returns (12% in 2007 and 10% 2008) and we expect this to continue in 2009.

Growth

Solidere's top line performance has experienced a CAGR of 3.76% between 2005 and 2008 growing to USD 257 million. Revenue growth was affected by a 10% drop in 2008 from its 2007 levels caused by delays in sales recognition during that year. We are expecting a considerable increase in 2009 due to a rise in recognizable land sales. On the other hand, Solidere's profits have grown significantly over the years at an estimated CAGR of 18% between 2005 and 2008. This is expected to continue as revenue recognition of the highly valuable reclaimed land begins in 2010. Solidere's long term future growth lies in its associate, Solidere International, which is expected to start paying dividends soon. Even though the present economic climate in the region is not very positive, this is a move that should be welcomed by investors as a long term growth and sustainability strategy.

Financial Position

Solidere has continuously enjoyed a strong financial position to shield itself from the political instability in Lebanon. It has maintained high liquidity and low debt levels on its balance sheet and continues to hold a large cash account. We estimate cash in 2009 to decrease after reaching extremely high levels in 2007 and 2008. This is partly due to utilizing its cash in new and existing projects with issuing little or no debt. Solidere's Debt-to-Equity ratio in 2008 was 0.33 which is significantly lower than comparable real estate companies. Its Interest Coverage Ratio (Operating Income / Interest Expense) has never dropped below 8 indicating a sufficient financial standing.

Cash flows are normally positive with the exception of 2008 due to Solidere exercising a call option on treasury shares.

Valuation

We estimate the fair value of Solidere's share at USD 31.00 through a hybrid methodology valuing the operating assets at market value using a discounted cash flow (DCF) model and the non-operating assets at Book Value. Operating assets consist of the 1.9 million sqm of unsold land along with its rental developments. We assumed a 9% discount rate, a 3% YOY price hike for sales over a 10 year depletion period, and a 3% terminal growth rate for rentals beyond our 10-year forecasts.

Solidere International was valued at Book Value due to an ongoing challenging real estate market in the region. In addition, its flagship project in Ajman, UAE is encountering some difficulties and expected to continue doing so in the near term.

When comparing Solidere to its regional peers, we find that with a P/E ratio of 18.62, it may be slightly overpriced against an average P/E of 15.53. However, when considering its monopoly position, its higher margins and a significantly less leveraged balance sheet, we can understand why investors may be overpaying in comparison to its peers.

Dividends

As long as it enjoys a strong financial position, Solidere is committed to distributing dividends to its shareholders. Previously, a dividend yield of 4 - 5% has been distributed and we expect a similar yield in 2009 resulting in a dividend of approximately USD 1.15 per share.

Risks

We have four major concerns related to investing in Solidere with the most significant being the political stability in Lebanon. As long as security risks are mitigated and the political factions remain in harmony, we find little reason to treat this as a severe threat. The exploding real estate price growth over the last 3 years is also a concern. However, after analyzing the historic prices and comparing them to regional real estate markets, our rationale shifts to that of an undervalued real estate market going through a correction to reach its fair value. Another visible risk that is affecting Solidere's expansion strategy is the sluggish real estate market outside Lebanon. Through its associate, Solidere International, the company is experiencing difficulties in its flagship project in Ajman, UAE and we expect this to continue in the short term. Finally, legal scuffles between Solidere and other parties (the jewelers in particular) may have an impact on profits in the short term if they end against the company. A delay in receiving the titles of land in the reclaimed area is also something we are closely following.

ECONOMIC OVERVIEW

A Strong Macroeconomic Performance

In a deteriorating global and regional environment, the Lebanese economy admirably avoided the recession that afflicted the rest of the world in 2009. While the global economy shrank by 0.8 %, we estimate that Lebanon registered an 8 % growth of its gross domestic product (GDP), accompanied by a moderate inflation and a flourishing economic activity in nearly all sectors.

Two complementary factors backed growth in 2009:

- The return to politico-security stability after several years of unrest restored general confidence in the country and its economy. After the election of a president and a new Parliament, consumers were encouraged to revert to spending while investors resumed projects that were put on hold for years. With tourists flocking to the country like never before, demand expanded significantly, propping up GDP growth.
- To a large extent, Lebanon weathered the financial crisis as its banks did not invest in derivatives and structured products that were proscribed by the regulatory authorities. Coupled with a high interest rate differential between Lebanon and the rest of the world, this led Lebanese expatriates and Arab investors that were looking for a safe financial haven to massively transfer their holdings to local banks. Colossal capital inflows, strong conversions to Lebanese pound and stable remittances that reached USD 7 billion provided the economy with a generous cushion of liquidity, stimulating growth by triggering an ease in interest rates and thus encouraging lending.

A Resilient Sector

The construction sector, traditionally a main driver of the local economy, mirrored the solid economic growth and delivered an outstanding performance in 2009. Not only did it weather the global crisis, but it also benefited from the woes of peer regional markets. The global financial and economic turmoil was a real sinecure for the local real estate sector that was offered a priceless growth opportunity at a time when all regional and international markets plummeted.

As a matter of fact, many Lebanese expatriates and Gulf investors seeking alternative high-yielding investments to diversify their portfolio away from markets impacted by the crisis converted their holdings into property in Lebanon. The resilience of the local market towards adverse conditions as well as the global decline in interest rates made it quite attractive for both resident and non-resident investors. Consequently, real estate purchases by foreigners surged by 17.6 % in 2009 and some 40 % of loans granted by Banque de l'Habitat (Housing Bank) were distributed to non-residents. An appreciable fraction (68 % in 2008) of foreign direct investments (FDI) inflows to Lebanon is usually channeled to the real estate sector.

The resilience of the real estate sector resulted not only from the strength of the financial system but also from a rock-hard demand. We attribute the vigor of the latter to the following:

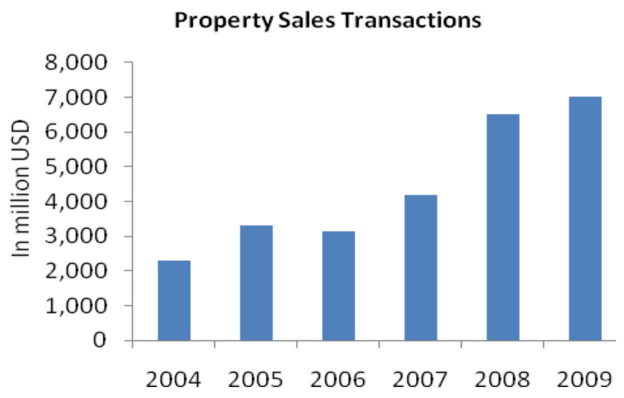
- There is a robust and genuine housing need emanating from end-users. Indeed, the urban population has been growing during the last five years at an average annual rate of 1.15 %. In addition, acquiring a residence is a sign of success and a goal for numerous local and expatriate workers.
- Speculation remains limited as monetary authorities capped banking loans funding construction projects at 60 % of the value of the project. In other words, short term speculative investments in the real estate sector are limited by the obligation for developers to self-finance 40 % of their projects' value.
- Funding of property purchase by the banking sector is abundant. Commercial banks provide their customers with a wide and growing range of housing loan products with growing maturities that reach 30 years and improving conditions for both residents and

expatriates. They currently hold some 60,000 housing loans in their portfolios with a total value of $ 3.2 billion.

- The government is subsidizing housing loans through the National Housing Institute (NHI) in partnership with commercial banks. NHI has currently some 32,450 outstanding credits. Moreover, Banque du Liban is encouraging housing loans by granting banks a 60% reduction in reserve requirements on deposits equivalent to the amounts of housing loans.

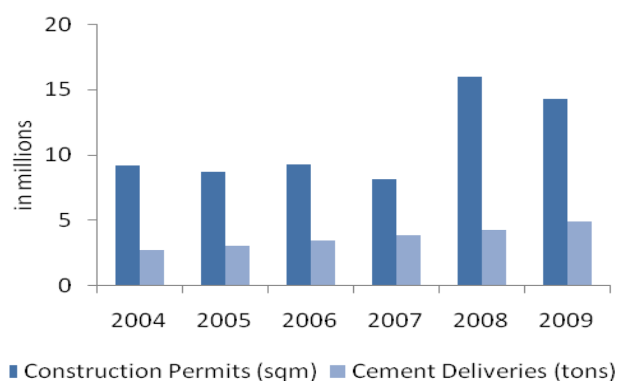
A Growth in all Indicators

The combination of local and non-resident demand led to a 2.3 % increase in the number of real estate transactions that reached 83,622. In parallel, the total value of transactions rose by 8.3 % to USD 7.01 billion.



Source: Directorate of Real Estate

On the supply side, construction activity was vigorous throughout the year, echoing efforts deployed by developers to match the expansion of demand. The number of construction permits climbed by 11 % to 15,136, while the total weight of cement deliveries jumped by 16.07 % to 4.9 million tons.



Source: Order of Engineers

Buoyant Prices

Property prices soared again in 2009, as the average value of real estate transactions jumped by 5.8 % to USD 83,910 due to the fact that the value of sales augmented at a higher pace than their volume. Driven by a steady demand, we estimate that prices surged by 5 to 10 % following several months of stability during 2008 and Q1 2009.

Consequently, average apartment prices per square meter (sqm) currently range between USD 4,000 and USD 5,000 in Beirut (excluding Beirut's central district), depending on the neighborhood. In the capital's central district where the demand mainly emanates from Gulf investors, wealthy Lebanese expatriates and major corporations, the average price fluctuates between USD 6,000 and USD 9,000 per sqm as per the estimates of Ramco Real Estate Advisers.

This upsurge was also mirrored by the rental prices of commercial real estate. Four Lebanese locations appeared among the top ten regional areas in terms of rental prices, according to a report released by Cushman & Wakefield. Beirut's downtown, ABC mall Achrafieh, Verdun and Kaslik came respectively in the second, fourth, fifth and seventh position on a regional level. Moreover, five Lebanese areas were among the top-ten regional locations in terms of rents' increase. Beirut's downtown ranked first in the Middle East with a growth rate of 80 %. Kaslik came second with 20 %, followed by Hamra (+13.3 %, 4th), ABC mall Achrafieh (+12 %, 5th) and Verdun (8.35 %, 6th). Globally, Lebanon registered a 26 % increase in rents, surpassing by far the 0.8 % growth of rental prices on a regional level.

Although the skyrocketing real estate prices seem as a bubble that is going to burst at some point in time, we think that the upswing in property prices relies on solid foundations:

- We believe that prices went through a correction movement in the past 2-3 years being undervalued for several years due to politico-security risks. Between 2000 and 2007, prices increased at low rates before gaining momentum again.
- The lag between the increase in demand and the expected adjustment in supply generated inflationary pressures on the real estate market.

The rapid increase in land prices translated into an upsurge in apartment prices, even if construction costs did not rise much. This is mainly due to the fact that land is becoming scarce in Beirut where available land for new building represents less than 10 % of the city's area. Reflecting the general upswing in the cost of land in the capital, prices more than tripled between 2003 and 2009 in the traditional area of BCD, with a CAGR) of 20 %.

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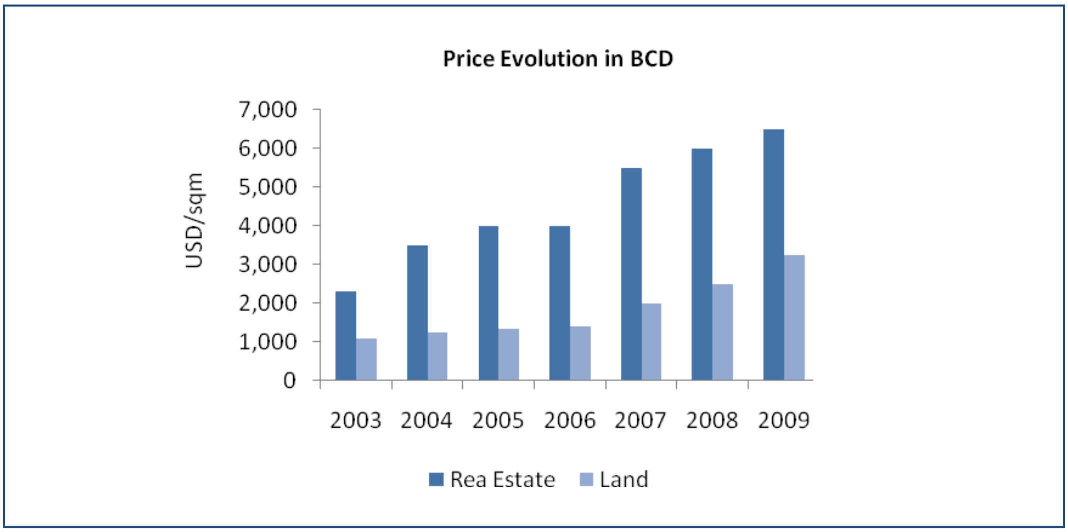
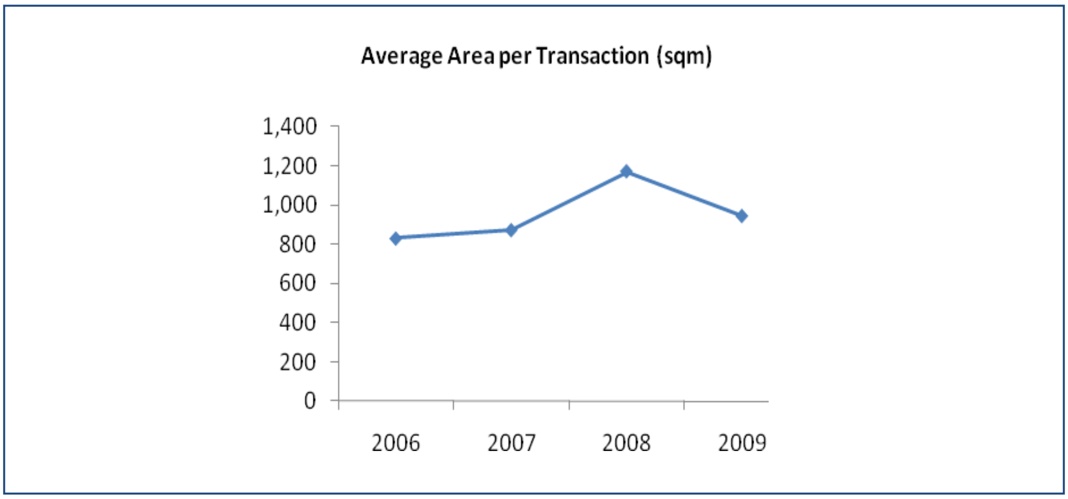


Source: InfoPro Research, Lebanon Opportunities, Solidere

Facing the exponential growth of land prices in Beirut, developers shifted to Mount-Lebanon which captured 80 % of loans granted by the National Housing Institute as well as a 47 % stake of total construction space followed by the North region with 19.9 %.

A Shift towards Suburbs and Smaller Lots

The tremendous increase in land prices has compelled property developers to reduce the surface of their projects as the cost of land now accounts for 50 % of the price of an apartment compared to 2.5 % for cement. Consequently, while the number of construction permits rose by 11 %, construction area fell by 11 % to 14.33 million sqm entailing a 19 % drop in the average area per transaction to 947 sqm. This highlights a shifting focus towards smaller lots that match the financial capacity of middle-class clients.



Source: Order of Engineers

Banks are trying to accompany this trend by offering more sophisticated housing loan products with more flexible conditions and longer maturities. The latter averaged between 15 and 20 years during previous years and now reach up to 30 years.

A Continuous Growth at Medium Term

The real estate sector will probably continue to expand during 2010 before the market starts to get saturated and the prices level off. No burst is expected as demand is generated by real housing needs and will remain solid, especially that numerous bank funding solutions are available. Both demand and supply will probably soar furthermore, following the anticipated decline in interest rates that will lower the cost of borrowing and encourage households to invest in real-estate due to the decline in deposit yields.

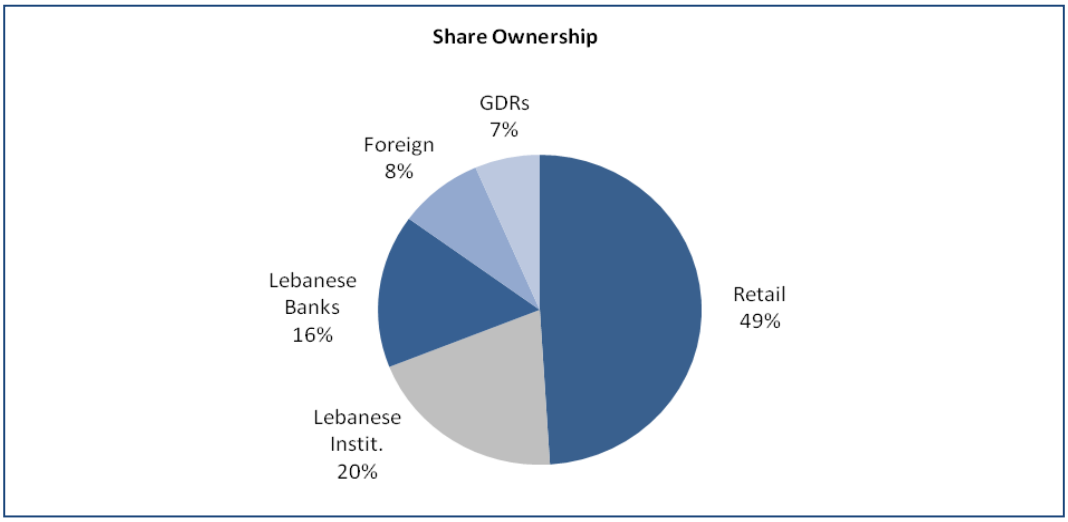
In spite of the great number of projects under construction and the multiplication of actors, the local property market still offers many development opportunities. Even if the upscale and luxurious residential segment comes to saturation, developers could easily shift to middle-class housing projects and to tourism related projects such as hotels. These market segments are still under-exploited and have a great potential of growth to meet the steady increase in tourist inflows.

COMPANY PROFILE

Solidere was founded in May 1994 with the objective of rebuilding and developing the Beirut city center after it had been torn during the Lebanese civil war. It continues to be the master planner for all real estate and infrastructure development in the 4.7 million sqm of Built-Up Area (BUA) that constitutes the Beirut Central District. Initially, its business was made strictly through selling land and real estate to builders but has evolved into additionally leasing residential and commercial units.

Ownership

Solidere's stock is publicly traded on the Beirut Stock Exchange through two share classes, A and B. 10 million A shares were originally granted to property holders in the Beirut city center where Solidere will be operating, while 6.5 million B shares were issued through the initial public offering. Both share types were issued at a par value of USD 100 but then went through a 10-to-1 split in 1996 setting a par value of USD 10. In addition, 15 million shares are traded on the London Stock Exchange as Global Depository Receipts (GDRs).



Source: Solidere

Management

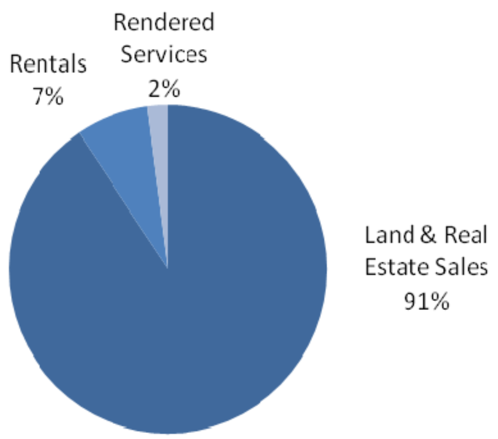
Name	Position	Start Date
Nasser Chammaa	Chairman, General Manager	05/94
Mounir Douaidy	General Manager, CFO	05/94
Maher Beydoun	Vice Chairman of the Board	05/94
Sami Nahas	Board Member, Legal Counsel	05/94
Raphael Sabbagha	Board Member, Secretary General	05/94
Fouad Al Khazen	Board Member	05/94
Joseph Asseily	Board Member	05/94
Fadi Boustani	Board Member	06/09
Abdul Hafiz Mansour	Board Member	06/00
Maher Daouk	Board Member	05/94
Sarkis Demerjian	Board Member	05/94
Mosbah Kanafani	Board Member	06/00
Basile Yared	Board Member	05/94

Solidere International

In 2007, Solidere International (SI) was founded in Dubai through a private placement offering priced at USD 700 million. Initially, Solidere owned 37.6% of SI through a USD 219 million investment and later expanded its ownership share to 38.2%. It is an active investor utilizing SI as its geographic expansion strategy. This complements Solidere's core business in Beirut allowing it to leverage its strong brand and expertise in real estate development and master planning.

BUSINESS MODEL

Solidere's business model has evolved from having land and real estate sales as the sole revenue source into having three different sources represented below with their respective revenue share for 2009.



Source: Blominvest

Revenue Mix

i. Land and Real Estate Sales continue to form the core of Solidere's revenues and are expected to remain so in the near future. Of its 4.0 million sqm of land, 1.9 million sqm are still either unsold or undeveloped and have an estimated depletion period of 10 to 15 years depending on demand and the company's strategy.
Its customers consist of local and regional builders and partners that have been in business with Solidere since its inception.

ii. Rental Income is growing considerably as Solidere focuses on generating recurring revenues from its properties. Instead of selling real estate, it is leasing retail, office, and residential units to the end-consumer and has set a target of USD 100 million to be reached by 2015. Major drivers for this target are the Beirut Souks along with future developments which include residential projects, an office block, and a boutique hotel.

Project	Status	Net BUA in sqm	Expected Opening Year	Revenue at Full Capacity
South Souks	Operational	71,903	2009	22,000,000
North Souks - Cineplex	Under Construction	19,000	2012	10,000,000
North Souks - Dept Store	Under Construction	27,000	2013	10,000,000
Saifi Residential Project	Under Planning	12,500	2013	6,000,000
Office Block in Zkak Blatt	Under Planning	24,000	2014	11,700,000
Furnished Apartments in Mina	Under Planning	18,700	2014	9,000,000
Mixed Use Development	Under Planning	15,000	2014	7,300,000
Existing Rentals	Operational	76,124	Various	22,000,000
Total		264,227		98,000,000

Source: Solidere, Blominvest

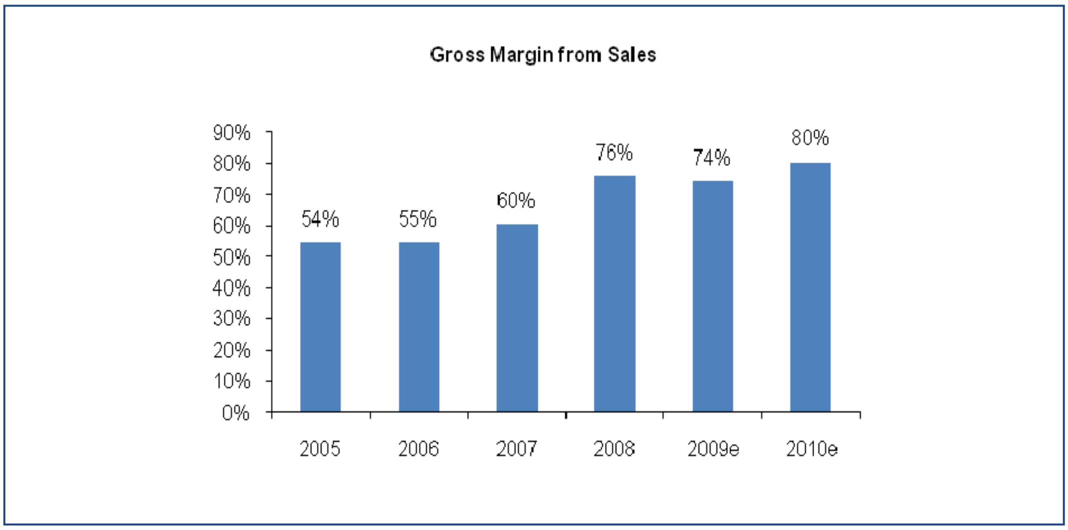
iii. Revenues from Rendered Services are also increasing with more businesses seeking Solidere's expertise in real estate development and master planning. Services consist of two types:

a. Local services for existing developments in the form of property management and administration. These can also be proceeds from the Broadband Network as well as project management fees in new developments. Growth is driven by an increase of inhabitants in the area and third party projects coming online.

b. Consulting services for projects that involve town planning, urban design & management, infrastructure and land reclamation etc… Growth is driven by new projects undertaken by Solidere International.

Ever-growing Margins

Solidere enjoys a very unique situation in Beirut Central District where its real estate acquisition costs cannot grow since it booked the land at inception (Estimated at USD 505/sqm). This has caused its gross margins from land and real estate sales to continuously increase as land and real estate prices naturally rise with time and inflation. Margins from developments built for rental purposes will also improve since there wouldn't be any substantial land costs in comparison to other real estate developers.



Source: Blominvest

STRATEGY

Solidere's strategy to shield itself from the political turbulence in Lebanon through high liquidity and low leverage has been successful. It has been able to continuously operate and grow amidst a hostile political environment such as the Israeli war in July 2006 and the political sit-in in downtown Beirut. Furthermore, Solidere's strategy has evolved to reduce reliance on its core land bank in Beirut by growing internationally through its associate and increasing revenue share from rental properties. When analyzing Solidere's strategy, we find that it revolves around the following 4 pillars:

High Liquidity and Low Leverage

Solidere has shielded itself from the political instability in Lebanon by maintaining high liquidity and low debt levels on its balance sheet. It has always carried a large cash account with current assets always exceeding current liabilities. This high liquidity made it possible for Solidere to invest in Solidere International.

Revenue Diversification

Solidere's investment portfolio is shifting from one that is dominated by land and real estate sales to a portfolio of recurring rental income. This is a logical move that should be welcomed by investors considering the limited supply of land designated to Solidere in Beirut. Its revenue diversification strategy is beginning to have a noticeable impact on both its revenues and its profits where rent is considerably increasing with the opening of new projects such as the Souks.

Value Enhancement

Solidere has added a new revenue source through hospitality management where it plans to operate a number of restaurants, cafes and hotels. The purpose is to enhance the value of land and real estate by increasing pedestrian traffic through new commercial offerings.

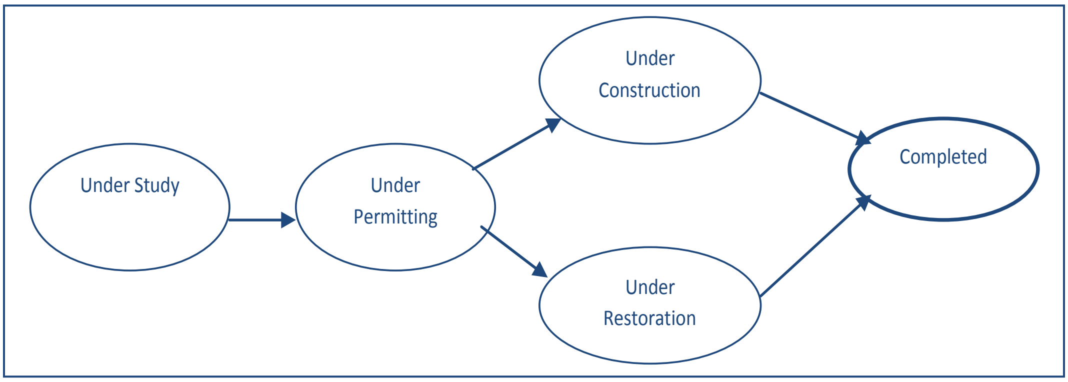
Growth and Sustainability

Solidere's long term future growth lies in its associate, Solidere International, which would utilize the extensive experience gained by its management team. This represents a geographic diversification strategy where Solidere's business would not be dominated by the fluctuations of one market as it currently is. Even though the present economic climate in the region is not very positive, this is a move that should be welcomed by investors as a long term growth and sustainability strategy. It is important to note that Solidere, through its associate, will be operating in a different competitive environment outside of Beirut where it enjoys a monopoly position. It would have to consistently build strategic partnerships, scout for new engagements, and learn the dynamics of local markets.

PROJECTS OVERVIEW

Real estate projects at Solidere normally follow the flow chart below beginning with a status of "Under Study" and reaching a status of "Completed" upon finalization of the project. During any phase, a project can be labeled "On Hold" for various reasons that may delay the project.

Project Flow Chart



Source: Solidere, Blominvest

Status	December 2008		December 2009	
	Projects	BUA sq m	Projects	BUA sq m
Completed	238	1,023,354	256	1,160,161
Under Construction	35	495,324	38	406,893
Under Restoration	12	20,900	11	31,875
Under Permitting	38	344,147	23	233,277
Under Study	19	425,452	40	648,229
On Hold	9	23,994	11	67,520
Total	373	2,838,735	390	2,967,533

Source: Solidere, Blominvest

When comparing the status of Solidere's projects between the end of 2008 and 2009, we can draw several conclusions.

- Solidere initiated 17 new projects with a BUA of 128,198 sqm bringing the total to 390 projects
- 18 projects have been completed in 2009 leading to a total of 256 projects completed since the inception of Solidere.
- Projects under construction grew from 35 to 38 but BUA declined by 88,431 sqm. This indicates project lot sizes are shrinking.
- A significant reduction has been made in projects under permitting which means projects are moving to the construction or restoration phase.
- Projects under study more than doubled indicating a growing number of prospects.

MAJOR DEVELOPMENTS

Developments in Beirut

Solidere's land bank consists of 4.0 million sqm in Beirut of which 1.9 million sqm are still unsold or undeveloped. While land sales continue to dominate Solidere's revenues, the company plans to maintain ownership of some land to develop rental properties. This is evident in its flagship project, the Beirut Souks and especially true in the newly reclaimed area that consists of 1.5 million sqm.

Beirut Souks

Background

Located in the Beirut City Center, the eagerly awaited Beirut Souks have been launched in 2009. Considered to be a major regional shopping and entertainment center, the Souks follow a pre-Roman ancient street grid integrating archeological features and gardens in the commercial center. South Souks, the section currently operational, includes a variety of stores, cafes, restaurants, and office space. North Souks, which represents the remaining section of the Souks project, involves a Cineplex and a Department Store and is expected to open in 2012.

Investment Rationale

The Souks project is a major push for Solidere to drive its revenue away from one-time sales transactions into annually recurring revenues. The entire Souks project consists of approximately 90,000 leasable sqm of commercial real estate and is expected to generate USD 45 million annually once fully operational. The property is bound to experience a large volume of shoppers due to its geographic location in the heart of the capital surrounded by offices and residential areas with easy car and pedestrian access.

Expectations

According to Solidere, 95% of space in South Souks has been already leased and is expected to operate at full capacity in 2011. As an incentive to ensure most space is leased, Solidere offered highly competitive rates with 6-year lease agreements. It will also be able to raise prices 5% annually during years 4, 5 and 6 of the contract. As for North Souks, Solidere is already experiencing high demand for its space and expects to offer longer term contracts than its South Souks agreements.

Developments outside Beirut

Solidere International (SI) has been founded as part of Solidere's geographic expansion strategy outside of Beirut. It is currently involved with two major projects, one in Ajman UAE and the other in Egypt. The latter consists of two separate developments in Cairo.

Al Zorah Project

Background

Located in Ajman UAE, Al Zorah is the first project SI was engaged in. Initially, SI made a USD 510 million investment to own 50% of the project but later sold 11% to investors maintaining 39% ownership. The other 50% of the project is owned by the Ajman government. This helps align incentives for the project that requires significant infrastructure investments since it is located in a fairly underdeveloped emirate.

Investment Rationale

The project consists of 22 million sqm of BUA located in a coastal and sea reclaimed area 35 km north of Dubai. The investment rationale is to create a housing alternative in a resort environment for those working in Dubai and are willing to commute. This previously happened with Sharjah (located 15 km north of Dubai), which used to be the bedroom community of Dubai and has developed into a fully fledged city on its own.

Expectations

We believe the project is expected to have several challenges in the short term among which are the falling real estate prices all over UAE and especially Dubai. This makes it more affordable to live closer to work and challenges the investment rationale for the Al Zorah project. Even though 30% of the project is committed in presales, this happened in 2008 before the financial crisis began forcing some investors to request amendments to their contracts. Currently, SI is focused on the core of the project, which is about 1 million sqm of surface land and constitutes the city center. Infrastructure and delivery of plots for third party developers in this section is expected to take approximately four years.

Eastown and Westown

Background

Located in Cairo, Egypt, both Eastown and Westown projects are in partnership with SODIC, an Egyptian real estate developer. The projects are structured so that SODIC is responsible for the financing and construction of the properties while SI performs master planning and urban design along with sales and marketing.

Eastown:

- Situated 22 km east of downtown Cairo, Eastown consists of 1.125 million sqm of BUA located near the New Cairo District, which houses the American University of Cairo and is home to Egypt's upper class.
- SI is paid in the form of a fee amounting to 7% of gross margin for each sqm sold by SODIC. It has no equity stake in the project but holds the option to purchase 50,000 sqm at the cost of EGP 1,100/sqm (USD 197/sqm) which it expects to exercise.

Westown:

- Situated 23 km west of downtown Cairo, Westown consists of 1.9 million sqm of BUA located near SODIC's Allegria residential project which mainly caters to upper class.
- SI is paid in the form of a fee amounting to 10% of gross margin for each sqm sold by SODIC. It recently exercised the option to buy 250,000 sqm at the cost of EGP 900/sqm (USD 170/sqm) which it intends to pay over a period of 6 years.

Investment Rationale

With global demand for high-end real estate booming during the last few years, it made sense to invest in new developments to create alternatives for the Egyptian upper class that wish to move out of the busy and polluted city center. These developments would also be attractive for those seeking a second home or as real estate investments. However, after the financial crisis, real estate as an asset class is no longer as attractive as before and supply for high-end properties considerably outgrew demand.

Expectations

Developments in Westown have already started and Eastown is to be launched by the second half of 2010. The projects are expected to be completed on a partial basis every few years due to lack of available funds to fully finance the projects. On a short term basis, the real estate environment will be challenging due to slowing demand and a weakening appetite by the banks to offer credit and financing for real estate projects. On a long term basis, new developments will be needed considering a young and growing population in Egypt along with urbanization.

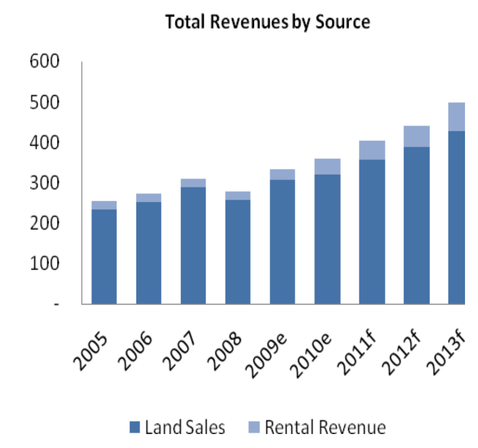
Other Solidere International Projects

- The Hazmieh project is SI's first venture in Lebanon where it has a strong presence through its parent company Solidere. The project consists of 227,000 sqm of BUA and 127,000 sqm of land for sale and construction. SI has a 20% equity stake in the project plus an option for an additional 15%. Sales are expected to begin in the last quarter of 2010. The project is of small size when compared to its ventures outside Lebanon, however we believe it is an important indicator of how well Solidere and SI can operate in the same market.
- SI also has a Memorandum of Understanding (MOU) for the Bodrum Project in Turkey consisting of around 8 million sqm of land.

FINANCIAL ANALYSIS

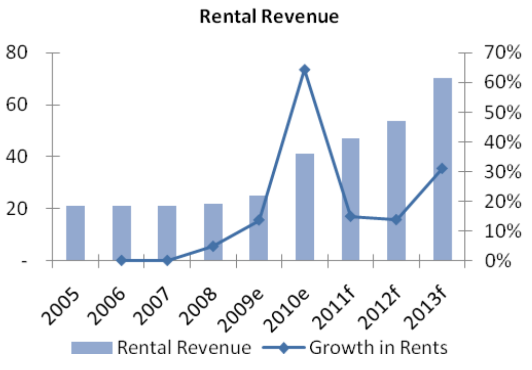
Revenues

Solidere's performance has been resilient to the financial crisis and its resulting shocks in the global real estate markets. When most real estate companies have experienced declining revenue, Solidere has continued to grow its revenues through land sales in the Beirut Central District. We expect this growth to continue as recognizable sales of the highly valuable reclaimed land (1.5 million sqm) begin in 2010 - 2011. It is important to note that sales are recognized on the basis of the full accrual method once several conditions such as the transfer of ownership are complete.



Source: Blominvest

Land Sales are expected to continue dominating the majority of Solidere's revenue; however, rental income is expected to significantly increase in 2010 after a full year of operation for South Souks project that was inaugurated in Q4 of 2009. Rental from South Souks is expected to enhance Solidere's revenue by an estimated USD 22 million annually. Furthermore, the opening of the North Souks (Cineplex in 2012 and a Department Store in 2013) is also expected to enhance revenue by another USD 20 million annually.

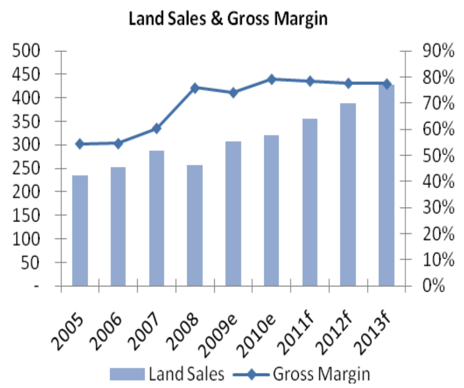


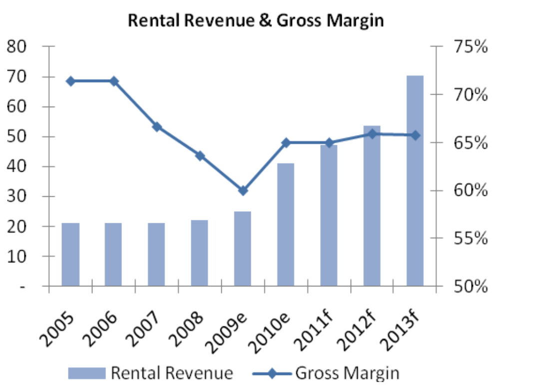
Source: Blominvest

As for Rendered Services as a revenue source, it is still small in comparison to overall revenues and estimated at 7 million in 2009. However, revenues from services are expected to grow as Solidere International takes on new projects, and businesses seek Solidere's expertise in real estate development and master planning.

Gross Margins

In comparison to its peers, Solidere enjoys much higher Gross Margins due to booking its land at low costs (Estimated at USD 505 per sqm) in 1994. Margins continue to improve with rising market prices and steady costs; this is especially true once sales of land in the reclaimed area start to be recognized. With an estimated market value of USD 5,000 per sqm instead of the current USD 3,500 per sqm for the traditional land, Gross Margins are expected to hover around 80% instead of its current 75%. Up until 2009, 100% of recognized sales are attributed to land and real estate projects in the traditional BCD area.



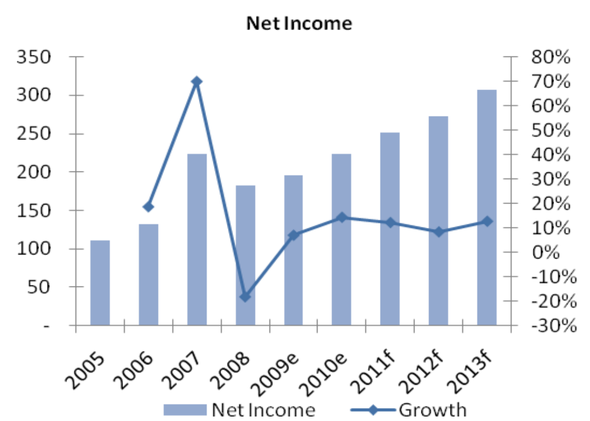


Source: Blominvest

As for the rental gross margin, it has historically fluctuated between 64% and 71% and is expected to remain between these levels. Such costs represent depreciation on the rental properties, property taxes, maintenance etc… Note that the rental margin may be slightly affected during the inauguration year of new properties. For example, in 2009, the gross margin might be around the lower end of this range due to the opening of the Souks. We took this into consideration in our forecasts below.

Earnings

We estimate Solidere's 2009 Net Income to reach USD 196 million resulting in a 7% annual growth from its USD 183 million reported in 2008. This increase is mostly due to larger revenues from land sales.



Source: Blominvest

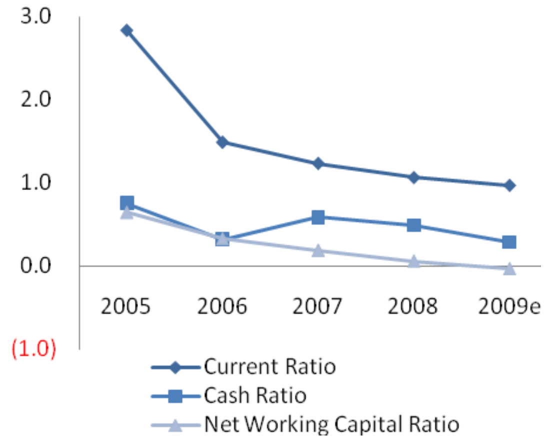
Liquidity

Solidere has consistently maintained high Cash Balances in its assets. Its Cash-to-Current Liabilities has always been at least 30%. In 2009, Solidere's balance sheet witnessed a significant decline in its cash mostly due to self-funding new projects and maintaining low debt levels.

Solidere's current assets have always been at least as much as its current liabilities. This is partly due to carrying a much larger balance of Accounts Receivables in comparison to Accounts Payable. Hence, Net Working Capital, that is the difference between Solidere's current assets and current liabilities, has always been positive. However in 2009, it might be negative for the first time due to the large drop in cash used for self-financing new projects.

While Solidere has maintained strong cash balances and a positive net working capital, we find that its liquidity levels have been constantly declining since 2005. This is shown in the chart below and again is partly due to Solidere relying on its cash instead of taking on new debt. Note that this may be a positive evolution for Solidere since excessive liquidity does harm profitability.

Current Ratio = Current Assets / Current Liabilities
Cash Ratio = Cash / Current Liabilities
Net Working Capital Ratio = (Current Assets – Current Liabilities) / Current Assets

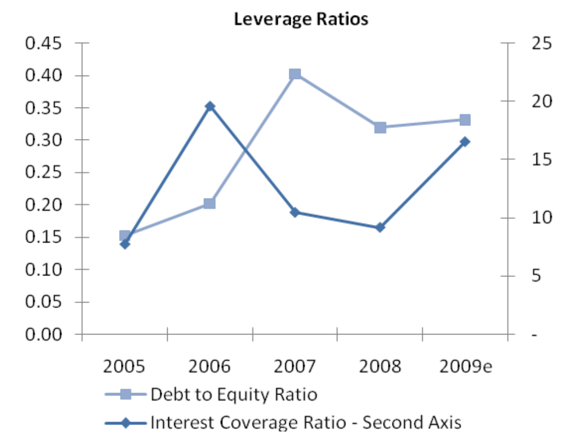


Source: Blominvest

Leverage

As part of Solidere's strategy to withstand the threats of a turbulent Lebanese economy, it has maintained low debt levels since its inception. Its Debt-to-Equity peaked in 2007 at 40% due to a temporary balance of USD 170 million in Deferred Credits as Solidere was executing option contracts on its treasury shares. We expect its Debt-to-Equity to hover around 33% in 2009 and the following years.

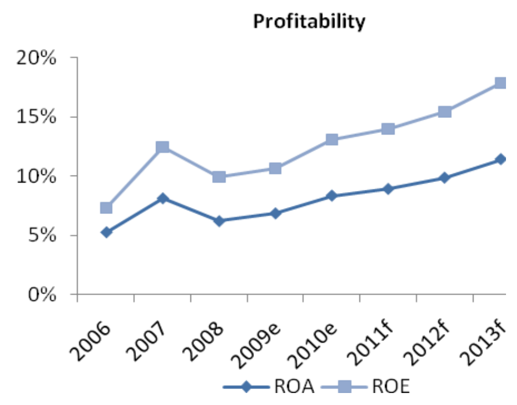
Another important indicator we looked at was the Interest Coverage Ratio which shows by how many times Solidere's Operating Income covers its interest expense. We treat this as a leading indicator to expose any financial troubles that may be looming in the horizon. Historically, this ratio has never declined to less than 8 times and occasionally reached as much as 20, which allows us to treat Solidere as a safe equity investment.



Source: Blominvest

Profitability

As for the profitability indicators, both Return on Assets (ROA) and Return on Equity (ROE) have been growing steadily and are expected to reach their 2007 levels of 8% and 13% respectively in 2009.



Source: Blominvest

Dividends

As long as it enjoys a strong financial position, Solidere is committed to distributing dividends to its shareholders. Previously, a dividend yield of 4 - 5% has been distributed and we expect a similar yield in 2009 resulting in a dividend of approximately USD 1.15 per share.

COMPARABLE ANALYSIS

When studying a company, we find it necessary to see how it compares to its peers from three standpoints:

1. Relative Valuation: Shows how the market perceives the company (overvalued, undervalued, or fairly valued)
2. Profitability Comparison: Shows how well the company is managing its expenses through different margin analysis (Gross Margin, Operating Margin, Net Income)
3. Management Effectiveness: Shows how efficient management is at using its assets and equity to generate earnings.

Comparable Firms

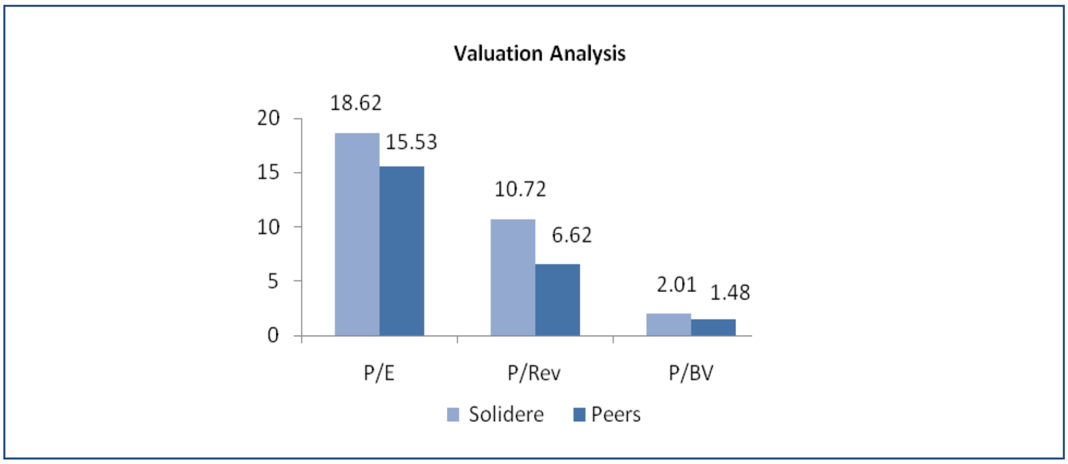
No matter how carefully we construct our list of comparable firms, we will end up with firms that are different from the company we are analyzing. However, taking the average of those that operate in the same region and industry does provide insight into the strengths and weaknesses of our target company.

The list we compiled consists of 13 Real Estate companies that operate in the Middle East. The largest has a market cap of USD 6.8 billion while the smallest has USD 819 million and the average is USD 2.4 billion. On the other hand, Solidere's market cap is approximately USD 3.6 billion.

Relative Valuation

We considered three ratios to get a sense of how Solidere is valued by the market against its peers. We compared price against earnings, revenues, and Book Value to mitigate differences that can result from accounting standards or financial reporting procedures since these companies operate in different countries.

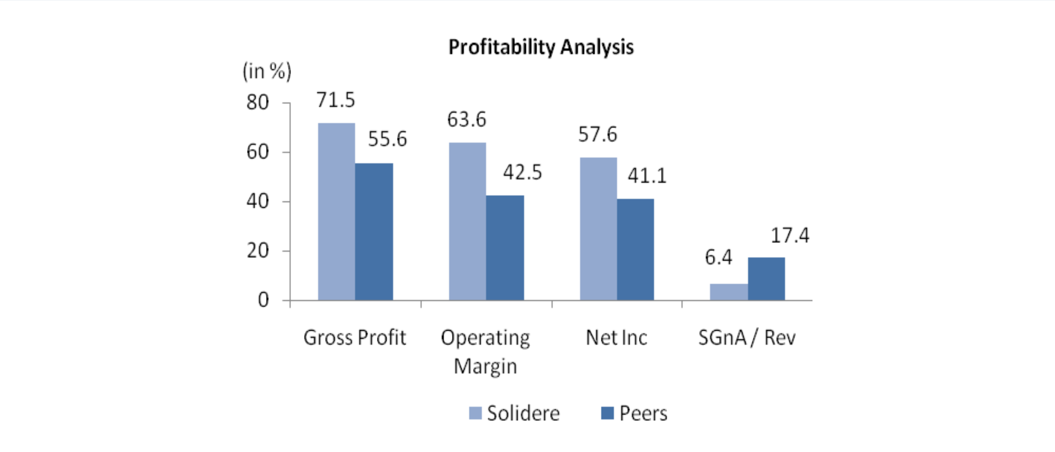
All three ratios show that Solidere may be overvalued in comparison to its peers.



Source: Blominvest

Profitability Comparison

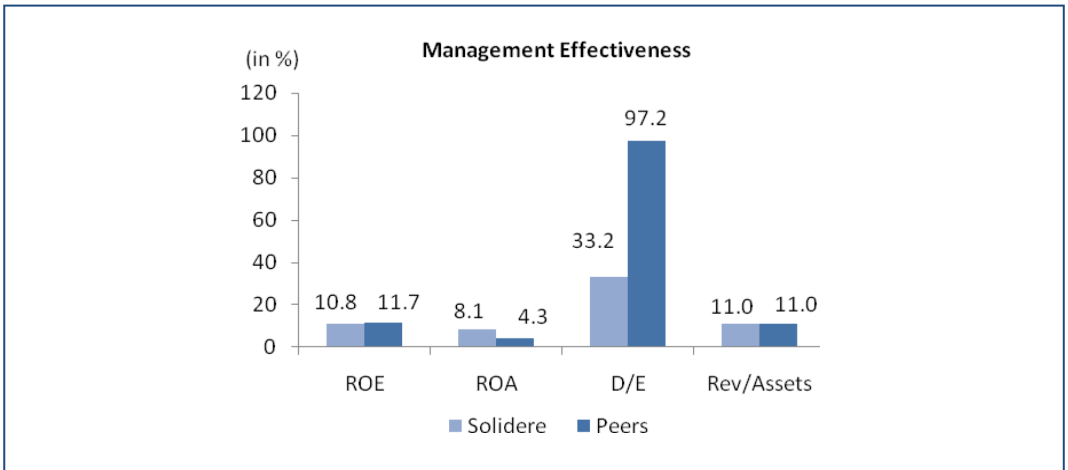
We compared the Gross Margin, Operating Margin, and Net Income as a percentage of revenues to better understand how Solidere is managing its expenses in comparison to its peers. All three ratios show that Solidere has considerably higher margins than its peers. We believe this is a result of its monopoly position in the very attractive Beirut Central District where real estate prices have been continuously increasing. In addition, the low costs with which it booked the land it operates in contributes significantly to these higher margins. We also added a ratio that represents Selling, General, & Administrative as a percentage of revenue and again, expenses are much lower at Solidere.



Source: Blominvest

Management Effectiveness

To measure management's efficiency at generating returns from its assets and equity, we compared Return on Equity (ROE) and Return on Assets (ROA) at Solidere to the average of its peers. We can see that the Lebanese company significantly out-performs its peers in generating earnings from its assets but slightly under-performs in providing returns to equity investors. The Debt-to-Equity percentage shows that Solidere has a stronger financial position than the average of its peers carrying much less debt on its balance sheet. Finally, the Revenue-to-Assets ratio shows that Solidere is on par with its peers in its ability to generate revenues from its assets.



Source: Blominvest

Putting It Together

Solidere appears to be overpriced at first glance with relation to its price multiples. However, when considering its higher margins and significantly less leveraged balance sheet we can understand why investors may be overpaying in comparison to its peers. Higher margins are a result of Solidere's monopoly position in a very attractive real estate market while less leverage has been part of Solidere's strategy to withstand political and economic disturbances in both Lebanon and the region.

Additionally, in contrast to the 13 firms we used to compile the list of peer companies, Solidere had minimal impact due to the financial crisis that struck most real estate markets. Investors are then inclined to pay a premium for gaining exposure to Lebanon's growing market.

VALUATION

We estimate the fair value of Solidere's share at USD 31.00 through a hybrid methodology valuing the operating assets at market value using a discounted cash flow (DCF) model and the non-operating assets at Book Value.

Component	USD million	USD per share
Market Value of Operating Assets in Beirut		
Value from Sales of Traditional Land	842	5.4
Value from Sales of Reclaimed Land	4,146	26.7
Value from Rental	552	3.6
Book Value of Solidere International		
Investment in Associates	310	2.0
Book Value of Non Operating Assets		
Cash & Cash Balances	170	1.1
Prepayments & Other Debit Balances	32	0.2
Accounts & Notes Receivables	370	2.4
Investments In Securities	7	0.0
Fixed Assets	37	0.2
Total Liabilities	(600)	(3.9)
General & Administrative Value Loss	(475)	(3.1)
Tax Effect	(677)	(4.4)
Fair Value	4,714	31.00

Source: Blominvest

Market Value of Operating Assets in Beirut

A Discount Rate of 9% was used in valuing all Operating Assets which consist of Solidere's land bank and its rental properties in Beirut. It was derived as follows:

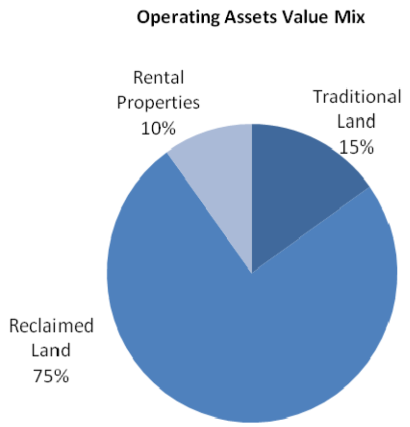
Solidere Discount Rate = Risk-Free Rate + (Beta * Market Risk Premium)
= 5.0% + (1.513 * 2.54%)
= 8.84% rounded up to 9%

We used a Risk-Free Rate of 5.0% represented by the 5 year Eurobond yield issued by the Lebanese government. Compared to the 5 year U.S. Treasury Risk-Free Bonds yielding 2.0%, we felt the Eurobond captures the additional risk of investing in a smaller and higher risk country.

Solidere's weekly Beta over the past 4 years is estimated at 1.513. This is a measure of Solidere share volatility against the BLOM Stock Index (BSI) which represents the Beirut Stock Exchange.

A Market Risk Premium of 2.54% is the result of the difference between the average 4 year return of the BSI estimated at 7.54% and the Risk-Free Rate of 5.0%. This represents the premium investors expect to gain for realizing the additional risk of investing in securities.

The result of Solidere's Discount Rate is 8.84% that we rounded up to 9%.



Source: Blominvest

Sales of Reclaimed & Traditional Land

We estimated the market value of Solidere's land bank at USD 31.10 per share with 26.7 of this value resulting from its reclaimed land and 5.4 from its traditional land.

The land bank consists of:

- 1.5 million sqm of reclaimed land in the Beirut Central District currently priced at USD 4,750 per sqm. To value this land, we assumed a depletion period of 10 years using an accelerated method starting with 5% of land sold in the first year and 15% of land sold in year 10.
- 0.4 million sqm of traditional land in the Beirut Central District currently priced at USD 3,500 per sqm. To value this land, we assumed a depletion period of 10 years using a straight line method with 10% of the land being sold each year.

A 3% annual growth rate was used in our price forecasts over the 10-year period and a constant cost of USD 505 per sqm across the entire land bank

Rental Portfolio

The rental portfolio consists of several projects which we valued separately based on the potential cash flows each project generates. Since rental properties generate a recurring and perpetual income, we used a terminal growth rate of 3% to capture the value beyond our 10-year forecast.

We assumed an improving Gross Margin between 65% and 70% in all rental income which is aligned with Solidere's previous performance and our cost breakdown estimates.

The current rental portfolio generates USD 22 million annually and is valued at USD 183 million. We used a 3% annual growth rate to forecast revenues and a steady 65% Gross Margin based on estimates from Solidere's previous years.

The South Souks is valued at USD 203 million and consists of total leasable BUA of 45,400 sqm of mixed-use space with a weighted average rental rate of USD 600 per sqm annually. Our price forecasts are based on the 6 year lease agreements for the majority of the tenants in South Souks which holds the price constant for 3 years then escalates the price at 5% annually for the following 3. We expect South Souks to be fully operational by the end of 2010 and therefore estimate 60% of capacity for the entire year and 95% capacity for 2011 and onwards.

The North Souks is valued at USD 166 million and consists of a total leasable BUA of 41,000 sqm split evenly across 2 segments: The Cineplex and Department Stores. The Cineplex is expected to go online around the summer of 2012 while Department Stores are expected in the first quarter of 2013. Due to still being in the early stages of structuring the lease contracts, we assumed similar rental price forecasts to those of South Souks.

Other developments are under planning and consideration and are expected to come online around 2014. The total BUA of these developments is around 80,000 sqm and consists of the following projects:

- Saifi Residential Project
- Office Block in Zkak Blatt
- Furnished Apartments in Mina
- Grand Theatre Boutique Hotel in Bashoura
- A mixed use development property that includes a wellness center, retail shops…

We did not account for these developments in our valuation as a conservative measure due to the projects still being at a very early stage.

Book Value of Solidere International

We chose to value Solidere's share of Solidere International (SI) at its Net Equity Value of USD 310 million due to the following:

- Its flagship project in Ajman is expected to experience some challenges and we doubt it will generate any considerable cash flows in the near term.
- The Hazmieh project is expected to start generating revenues by the end of 2010. However due to the small size of the project and SI's 20% equity stake, we feel it will not have a considerable impact on SI's valuation.
- Eventually, SI needs to start paying dividends to its parent company. We chose not to consider this in our valuation until the first dividend distribution occurs.

Book Value of Non-Operating Assets

The Book Value of non-operating assets is simply the sum of all assets that do not contribute to the operating income of the company. In Solidere's case, the sum of non-operating assets amounts to USD 619 million and consists of Cash, Accounts Receivable, Prepayments, Fixed Assets, and Investments In Securities.

Total Liabilities

At the end of 2009, liabilities are estimated at 600 million and are treated as a negative contributor to the valuation.

General and Administrative Value Loss

In our forecasts, we assumed 9% of Net Revenues to represent General and Administrative (G&A) expenses resulting in a USD 475 million of total value loss. General and Administrative (G&A) expenses have historically fluctuated between 6% and 10% of Solidere's Net Revenues. The assumptions made are the same as those in the valuation of Operating Assets such as a 9% discount rate and a 3% terminal growth rate beyond the 10 year forecasts.

Tax Effect

A 15% tax rate is applied to the annual earnings resulting in a total Present Value of USD 677 million of taxes.

PROJECTED INCOME STATEMENT

In USD million	2006	2007	2008	2009e	2010e	2011f	2012f	2013f
Revenues from Land & Real Estate Sales	253	288	257	308	320	356	388	429
Revenues from Rented Properties	21	21	22	25	41	47	54	70
Revenues from Rendered Services	2	3	7	7	7	8	9	10
Cost of Land & Real Estate Sales	(115)	(114)	(62)	(80)	(66)	(76)	(87)	(97)
Charges on Rented Properties	(6)	(7)	(8)	(10)	(14)	(17)	(18)	(24)
Cost of Rendered Services	(2)	(4)	(7)	(7)	(7)	(7)	(8)	(8)
Gain/(Loss) on Sale of Investment Properties	-	(1)	(2)	-	-	-	-	-
Net Revenues from Operations	153	186	207	243	280	312	338	380
Share Result from an Associate	-	68	(2)	-	-	-	-	-
General & Admin. Expenses	(14)	(18)	(19)	(22)	(25)	(28)	(30)	(34)
Depreciation of Fixed Assets	(2)	(1)	(5)	(5)	(5)	(5)	(6)	(6)
Write-Back of Provision against Land & Real Estate Development Cost	(3)	(8)	10	-	-	-	-	-
Write-Off of Land & Real Estate Development Cost	-	-	(8)	-	-	-	-	-
Other Taxes	(1)	(1)	(4)	-	-	-	-	-
Provision for Doubtful Receivables	-	-	-	-	-	-	-	-
Other Income	-	-	1	-	-	-	-	-
Interest Income	27	40	55	27	29	31	32	33
Interest Expense	(7)	(16)	(20)	(13)	(16)	(14)	(14)	(13)
Profit Before Tax	153	250	215	230	263	296	320	361
Income Tax Expense	(21)	(26)	(32)	(35)	(40)	(44)	(48)	(54)
Profit for the Year	132	224	183	196	224	251	272	307

PROJECTED BALANCE SHEET

In USD million	2006	2007	2008	2009e	2010e	2011f	2012f	2013f
Assets								
Cash & Cash Balances	106	328	292	170	252	265	271	285
Prepayments & Other Debit	28	34	35	32	35	40	45	51
Accounts & Notes Receivables	349	319	296	370	331	350	361	382
Investments in Securities	9	10	6	7	8	8	8	9
Inventory of Land & Projects	1,458	1,405	1,274	1,114	1,048	972	822	664
Investment Properties	151	150	217	366	366	366	429	491
Investments in Associates		287	296	310	310	310	310	310
Fixed Assets	26	36	37	40	45	51	56	60
Total Assets	2,127	2,569	2,453	2,409	2,395	2,361	2,302	2,252
Liabilities								
Bank Overdraft & Short Term	48	181	177	169	160	115	74	26
Accounts Payable	83	100	95	91	105	110	119	129
Dividends Payable	31	46	63	77	92	104	115	126
Deferred Revenue & Other Credit Balances	168	233	257	261	239	259	266	280
Deferred Credits Under Structured Contracts	-	170	-	-	-	-	-	-
Loans From Banks	27	7	2	2	2	2	2	2
Total Liabilities	357	737	594	600	599	590	575	563
Total Equity	1,769	1,832	1,859	1,809	1,796	1,771	1,726	1,689
Total Liabilities & Equity	2,126	2,569	2,453	2,409	2,395	2,361	2,302	2,252

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