

Alert on FY 2011 Earnings

Sector: Power
Country: Egypt
Date: April 5, 2012

Share Price (EGP): 22.34
Fair Value (EGP): 24.00
Upside: 7.43%
Recommendation: HOLD
Risk: Medium

Strong operations but sacrificed margins amidst regional political instability

Revenues at SE jumped by 18% y-o-y in 2011 to EGP 15,169M in line with our expectations, on improved operations across all business lines. The turnkey segment was a special achiever owing to the emergent African market. Net revenues from the segment grew more than expected, by 49% y-o-y to EGP 2,525M, contributing to almost 17% of the company's revenue mix for the year, versus 13% in 2010. SE was able to also improve sales of its cables segment by 15% y-o-y to EGP 11,305M, on a 5% increase in sales volume despite challenging events in primary markets like Egypt, Syria, Libya and Yemen, pressuring the company to seek haven in the GCC and European markets. The gross margin from the cables segment fell to 9% in 2011 from 12.7% previously, on higher competition from local players in the GCC, feeble demand in Europe and the hike in copper prices in 2011 relative to 2010. Following, the total gross margin dropped to 13%, as we expected, down from 15% in 2010.

Earnings pressured by higher borrowing costs and forex losses

EBIT fell only by 3% y-o-y to EGP 1,054M, as the company made every effort to reduce operating costs last year and improve its collection cycle to compensate for the forewent gross profit. The biggest hit to earnings which fell by 34% y-o-y to EGP 536M, came from net interest expense which witnessed a twofold hike last year to EGP 310M. This was due to the conversion of a US\$-denominated debt to Egyptian Pound in Q4 and the large interest rates spread. Foreign exchange losses of EGP 111M also contributed to the drop in SE's 2011 net profit margin to 3.5% from 6.3% a year earlier.

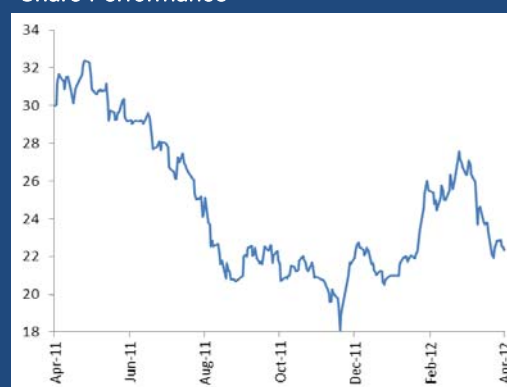
Lowering our fair value on high uncertainty surrounding cables operations

We expect demand in Egypt to remain weak in 2012, further dropping by 20% according to SE's management, on limited public spending as the country struggles to establish a sound political frame. Operations in Yemen continue to be jeopardized and divesting operations in the market might be SE's next strategy, while the ongoing turmoil in Syria limits expectations of a major contribution from the Syrian market for the short term. Following, we believe SE will continue to compensate weak primary markets operations by less profitable export markets, notably in the GCC and Europe. However, the growing turnkey segment will continue to profit from a strong African market and slightly offset lost profitability in the cables business, as it increases its stake in the revenue pool. We thus lower our target price to EGP 24 per share and maintain a HOLD recommendation on the high uncertainty surrounding operations in core markets, which remains the major impediment to SE's profitability.

Share Data

Bloomberg Symbol	SWDY EY
Reuters Symbol	SWDY.CA
Market Cap (EGP)	4,991,158,120
Number of Shares	223,418,000
Free Float	25%
Price to 2011 Earnings	9.80
Price to 2011 Book Value	0.90

Share Performance



Source: Reuters

1 Month Return	15.1%
3 Month Return	-12.4%
6 Month Return	6.8%
12 Month Return	-25.5%
52 Week Range	18.10 – 32.41

Source: Reuters

Contact information

Equity Analyst: Cathy Hobeika
cathy.hobeika@blominvestbank.com

Research Analyst: Nader Ali Khedr
nakhedr@blomsecurities.com

Head of Research: Marwan Mikhael
marwan.mikhael@blominvestbank.com

Performance and Forecasts

In EGP million	FY 11	FY 10	% YoY	Q4 11	Q4 10	% YoY
Revenues	15,169	12,902	18%	3,799	3,690	3%
EBIT	1,054	1,084	-3%	78	167	-53%
EBIT Margin %	6.9%	8.14%		2.1%	4.5%	
Net Income (Loss)	536	817	-34%	-23	90	-126%
Profit Margin %	6.3%	3.5%		-0.6%	2.4%	

Source: El Sewedy Electric

VALUATION

<i>In EGP million</i>	2012e	2013f	2014f	2015f	2016f
Net revenues from Cables & Wires	11,995	12,175	12,310	13,213	14,850
<i>Contribution to revenue pool (%)</i>	72.4%	68.7%	65.3%	63.9%	62.7%
Net revenues from Turnkey	3,261	4,108	4,951	5,704	6,870
<i>Contribution to revenue pool (%)</i>	19.7%	23.2%	26.3%	27.6%	29.0%
Net revenues from Electrical Products	1,307	1,439	1,582	1,768	1,961
<i>Contribution to revenue pool (%)</i>	7.9%	8.1%	8.4%	8.5%	8.3%
Net Revenue	16,563	17,722	18,843	20,685	23,682
Net Income	560	776	860	927	1,162
Discount rate (WACC %)	16.5%				
Terminal growth rate	3.0%				
El Sewedy Value (EGP M)	5,372				
Number of shares (million)	223.4				
Target Price (EGP)	24.00				

Source: Blominvest Bank

A discount rate of 16.5% was deemed appropriate in our valuation model, despite SE operating in a challenging environment based on the following:

- Turnkey, the most profitable segment among SE's business lines, is holding an increasing share of the cable maker's revenue mix. We expect the contribution to increase from 16.6% in 2011 to 29% by 2016. As of 31 December 2011, backlog for the turnkey and contracting business stood at EGP 4.7 billion and included projects in the Middle Eastern and African region. The fast-growing African market holds the biggest bulk of the backlog and provides a shelter for SE's operations from the unrest in the Middle Eastern markets.
- SE can turn to export markets that are untouched by political tumult, like the GCC and Europe, to exhaust its cables production, despite the slight profitability trade-off. Also, the cables and wires segment's contribution to SE's revenues has been declining over the past few years and is expected to fall to 62.7% by 2016 from 74.5% in 2011 to give place to more profitable revenue contributors like turnkey and transformers lines.

PROJECTED INCOME STATEMENT

<i>In EGP million</i>	2010	2011	2012e	2013f	2014f	2015f
Operational revenues	12,902	15,169	16,563	17,722	18,843	20,685
Operational costs	(10,914)	(13,258)	(14,396)	(15,167)	(16,013)	(17,541)
Gross Profit	1,988	1,911	2,166	2,555	2,830	3,144
Other operating income	148	94	83	89	94	103
Selling & distribution expenses	(341)	(345)	(359)	(371)	(396)	(428)
Admin. Expenses	(51)	(556)	(580)	(638)	(716)	(827)
Other OPEX	(201)	(50)	(166)	(177)	(188)	(207)
Operating income	1,084	1,054	1,144	1,457	1,624	1,785
Finance Income	57	61	46	50	53	58
Finance costs	(234)	(482)	(524)	(582)	(655)	(741)
Net financing costs	(176)	(421)	(477)	(532)	(602)	(684)
Net profit before tax	908	633	667	925	1,022	1,102
Income tax						
Current income tax	(86)	(94)	(100)	(139)	(153)	(165)
Deferred income tax	(5)	(3)	(7)	(10)	(9)	(9)
Net profit for the year after tax	817	536	560	776	860	927

Source: El Sewedy Electric, Blominvest

PROJECTED BALANCE SHEET

In EGP million	2010	2011	2012e	2013f	2014f	2015f
Assets						
Long term assets						
Fixed assets	3,544	3,480	3,410	3,513	3,688	3,873
Projects under construction	270	256	230	242	261	287
Investments AFS	14	15	15	15	15	15
Investments in associates	10	13	10	10	10	10
Paid on account of investments	1	-	-	-	-	-
Debit balances	239	203	248	266	283	310
Non-tangible assets	166	227	227	227	227	227
Deferred tax assets	32	37	35	35	35	35
Total long term assets	4,278	4,231	4,177	4,308	4,520	4,758
Current assets						
Inventories	3,700	3,554	4,528	4,693	4,852	5,486
Trade, notes & other receivables	4,115	4,391	4,937	5,355	5,588	6,184
Due from affiliates	283	156	342	312	305	375
Investment fund/ T Bills / CDs	569	401	574	622	604	702
Cash & cash equivalents	1,000	1,242	1,325	1,418	1,507	1,655
Total current assets	9,667	9,744	11,706	12,400	12,857	14,402
Total Assets	13,944	13,975	15,883	16,707	17,377	19,160
Current liabilities						
Banks facilities & overdrafts	4,164	4,061	4,141	4,608	5,276	5,999
ST loans and installments of LTD	601	922	950	1,030	1,050	1,199
Certificates of deposit payable to bank	-	175	-	-	-	-
Trade, notes & other payables	2,316	1,930	2,739	2,789	2,827	3,260
Due to affiliates	156	240	187	232	252	260
Provisions	72	49	105	89	92	112
Total current liabilities	7,310	7,377	8,122	8,747	9,496	10,830
Long term liabilities						
Loans	1,073	825	728	826	948	1,040
Deferred tax liabilities	109	120	100	100	100	100
Other liabilities	111	78	72	80	93	101
Total long term liabilities	1,293	1,023	900	1,006	1,141	1,241
Total liabilities	8,603	8,400	9,022	9,753	10,637	12,072
Shareholders' equity						
Issued and paid capital	1,719	2,234	2,234	2,234	2,234	2,234
Own stock	(2)	(1)	-	-	-	-
Legal reserve	37	122	67	116	142	134
Increase in subsidiary value	579	579	579	579	579	579
Retained earnings	1,858	1,798	3,002	2,824	2,478	2,737
Net profit for the year	796	509	534	737	815	876
Forex from foreign entities translation	(59)	(80)	(62)	(67)	(70)	(66)
Total shareholders' equity	4,927	5,161	6,354	6,424	6,179	6,495
Minority interests	414	414	507	530	560	593
Total Equity	5,341	5,575	6,861	6,954	6,739	7,088

Source: El Sewedy Electric, Blominvest

El Sewedy Electric

BLOMINVEST BANK s.a.l.

Research Department
Verdun, Rashid Karamah Str.
POBOX 11-1540 Riad El Soloh
Beirut 1107 2080 Lebanon

Tel: +961 1 991 784

Fax: +961 1 991 732

research@blominvestbank.com

For your Queries:

Marwan Mikhael, Head of Research

marwan.mikhael@blominvestbank.com

+961 1 991 784 Ext: 360

Cathy Hobeika, Equity Analyst

cathy.hobeika@blominvestbank.com

+961 1 991 784 Ext: 362

Nader Ali Khedr, Research Analyst

nakhedr@blomsecurities.com

+202 3761 7682

Equity Rating Key

Recommendations are based on the upside (downside) between our 12-month Fair Value estimate and the current Market Price.

Buy: Fair Value higher than Market Price by at least 20%

Accumulate: Fair Value higher than Market Price by 10% to 20%

Hold: Fair Value ranges between -5% to +10% in relation to Market Price

Reduce: Fair Value lower than Market Price by 5% to 15%

Sell: Fair Value lower than Market Price by at least 15%

Risks are based on share price volatility along with qualitative factors such as the nature of the business, the country risk and sensitivity to a single event, single product or single buyer. We've arranged the risk factor into 5 trenches:

- High Risk
- Medium-to-High Risk
- Medium Risk (similar to Market Risk)
- Medium-to-Low Risk
- Low Risk

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