



## Alert on Q2 2013 Earnings

Sector: Basic Materials &amp; Industrial Products

Country: Egypt

Date: January 15, 2014

Share Price (EGP): 16.54

Target Price (EGP): 18.38

Upside: 11.1%

Recommendation: ACCUMULATE

Risk: High

## Raising our target price on Ezz to EGP 18.38 with an ACCUMULATE recommendation to account for revised forecast

## Top-Line supported by robust local demand

Ezz Steel recorded an 8% y-o-y increase in H1 revenues to EGP 11.1 billion, as a result of higher sales volumes and selling prices for both long and flat products. Sales from long steel used in construction constituted 78% of the top-line, primarily targeting the growing Egyptian market which captured 92% of total long product sales at Ezz. As well, Egypt accounted for 54% of total flat sales which were mainly directed before toward satisfying foreign demand, mainly due to the reduced activity in the global flat steel market. Ezz sold almost 1.94 million tons of long products, a rise of 1% compared to a year earlier. Similarly, flat sales volumes, which are concentrated at EZDK, edged up by 9% to 522 thousand tons despite the suspension of flat production at EFS facility.

## Earnings lifted by higher revenues and lower production costs

Ezz was able to enhance operating efficiency in H1 2013 with production costs dropping to 87% of sales compared to 90% a year earlier. Hence, gross profit grew by 42% to EGP 1.4 billion, sending gross margin up to 13%. Net income followed suit, registering a considerable surge to reach EGP 302 million as opposed to EGP 82 million a year before, further supported by higher non-operating revenues, forex gains, and interest income despite the rise in SG&A expenses. We expect the company's earnings to grow at a CAGR of 19.5% in the coming three years with an estimated net income of EGP 382 million for 2013.

## DRI to further boost Ezz's profitability

Ezz liquidity position improved during H1 following an EGP 550 million top-up syndicated loan facilities signed in 2013 with a group of local banks to fund the construction of the Direct Reduced Iron (DRI) project. This translated on the balance sheet with an increase of 33% in the cash balance and a 2% rise in total debt. Net debt-to-equity ratio declined to 124% from 137% in H1 2012, contributing to lower risk on the steel maker's balance sheet. However, Ezz continues to have a highly leveraged balance sheet noting that the recent borrowings were directed to finance the progress of the DRI project with an estimated cost of EGP 3.7 billion. Once successfully completed, the latter project will increase vertical integration and operational efficiency, lifting margins and profitability.

## Upgrading to ACCUMULATE on recovering operational performance

We raise our target price on Ezz to EGP 18.38 per share, upgrading our recommendation to ACCUMULATE on the back of recovering operations along with easing macroeconomic and political tensions in Egypt. We incorporate in our model the improving profitability with the start of the DRI operation at the end of 2014 in addition to the resilient domestic demand supported by the country's strong demographic features. Ezz shares followed the upward trend in the Egyptian market, rallying by more than 60% in the past six months to hit a 3-year high with investors reacting positively to easing political tensions especially after army chief General, Al-Sisi, showed interest in becoming a president. However, we continue to perceive additional specific risks from the lawsuits filed against Ahmad Ezz and the company's most profitable subsidiary, EZDK.

## Share Data

Bloomberg Symbol	ESRS EY
Reuters Symbol	ESRS.CA
Market Cap (EGP)	8,985,603,547
Number of Shares	543,265,027
Free Float	35%
Price-to-Earnings 2013e	23.50
Price-to-Book 2013e	1.32

## Share Performance



Source: Reuters

1 Month Return	9.3%
3 Month Return	33.5%
6 Month Return	60.7%
12 Month Return	65.4%
52 Week Range	7.72 - 16.90

Source: Reuters

## Contact Information:

Equity Analyst: Malak Hawa  
malak.hawa@blominvestbank.com

Head of Equities: Maya Mantach, CFA  
maya.mantach@blominvestbank.com

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

## Performance and Forecasts

In EGP millions	2010	2011	2012	2013f
Revenues	16,621	18,611	19,799	21,521
Gross Profit	1,923	2,207	1,690	2,540
Gross Profit Margin %	12%	12%	9%	12%
Net Income	251	202	8	382
Profit Margin %	2%	1%	0%	2%

Source: Ezz Steel, Blominvest

## PROJECTED INCOME STATEMENT

<i>In EGP million</i>	2010	2011	2012	2013e
Net sales	16,621	18,611	19,799	21,521
Cost of goods sold	(14,698)	(16,404)	(18,109)	(18,982)
<b>Gross Profit</b>	<b>1,923</b>	<b>2,207</b>	<b>1,690</b>	<b>2,540</b>
Selling & marketing Exp.	(154)	(113)	(102)	(129)
General & Admin. Expenses	(235)	(297)	(373)	(355)
Impairment Loss on Assets	(2)	(17)	(4)	-
Provisions	(95)	(81)	(2)	(15)
<b>Total expenses</b>	<b>(486)</b>	<b>(509)</b>	<b>(480)</b>	<b>(499)</b>
Finance expenses	(754)	(764)	(880)	(997)
Interest income	67	64	42	62
Other income	22	30	148	175
<b>Total other expenses</b>	<b>(665)</b>	<b>(670)</b>	<b>(690)</b>	<b>(760)</b>
<b>Net profit before tax &amp; non-controlling interest</b>	<b>772</b>	<b>1,028</b>	<b>520</b>	<b>1,280</b>
Income tax expense	(171)	(359)	(275)	(320)
Deferred tax expense	(37)	(133)	5	20
<b>Net profit before minority interests</b>	<b>564</b>	<b>536</b>	<b>250</b>	<b>980</b>
Minority interest	(313)	(334)	(242)	(598)
<b>Net profit after minority interests</b>	<b>251</b>	<b>202</b>	<b>8</b>	<b>382</b>

Source: Ezz Steel, Blominvest

## BALANCE SHEET

<i>In EGP million</i>	2010	2011	2012	Q2 2013
<b>Non-current Assets</b>				
Property, plant & equipment	9,567	9,937	11,127	11,493
Projects under construction	3,319	3,558	2,755	2,891
Goodwill	315	315	315	315
Other non-current assets	244	281	304	313
<b>Total non-current assets</b>	<b>13,445</b>	<b>14,090</b>	<b>14,500</b>	<b>15,012</b>
<b>Current Assets</b>				
Inventories	3,734	3,629	3,620	3,649
Trade & notes receivable	185	122	52	175
Debtors & other debit balances	586	628	924	1,067
Advances to suppliers	48	135	59	37
Investments in treasury bills	57	63	47	43
Cash & cash equivalents	1,415	1,171	1,290	1,714
<b>Total current assets</b>	<b>6,025</b>	<b>5,747</b>	<b>5,991</b>	<b>6,684</b>
<b>Total Assets</b>	<b>19,470</b>	<b>19,837</b>	<b>20,492</b>	<b>21,696</b>
<b>Non-current Liabilities</b>				
Loans	4,466	3,937	3,377	3,312
Other non-current liabilities	205	667	779	842
Bonds loan	651	433	216	217
Deferred tax liabilities	658	790	789	783
<b>Total Non - current liabilities</b>	<b>5,980</b>	<b>5,828</b>	<b>5,161</b>	<b>5,154</b>
<b>Current Liabilities</b>				
Banks credit accts & Overdrafts	1,136	1,003	2,061	2,211
ST Loans & Borrowings	3,292	3,573	4,203	4,359
Bonds loan	220	220	220	220
Trade & notes payable	1,145	1,364	1,413	1,650
Advances from customers	410	236	287	302
Creditors & other credit balances	677	389	359	404
Income Tax	-	359	275	243
Liability of the supplementary pension scheme	-	-	-	10
Provisions	123	204	205	202
<b>Total Current Liabilities</b>	<b>7,003</b>	<b>7,349</b>	<b>9,023</b>	<b>9,602</b>
<b>Total Liabilities</b>	<b>12,983</b>	<b>13,177</b>	<b>14,184</b>	<b>14,756</b>
<b>Shareholders' Equity</b>	<b>6,487</b>	<b>6,661</b>	<b>6,307</b>	<b>6,940</b>
<b>Total Liabilities &amp; Equity</b>	<b>19,470</b>	<b>19,837</b>	<b>20,492</b>	<b>21,696</b>

Source: Ezz Steel

**BLOMINVEST BANK s.a.l.**

Research Department  
 Verdun, Rachid Karamah Street  
 POBOX 11-1540 Riad El Soloh  
 Beirut 1107 2080 Lebanon

Tel: +961 1 747 802

[research@blominvestbank.com](mailto:research@blominvestbank.com)

**For your Queries:**

Marwan Mikhael, Head of Research  
[marwan.mikhael@blominvestbank.com](mailto:marwan.mikhael@blominvestbank.com)  
 +961 1 747 802 Ext: 1234

Maya Mantach, Head of Equities  
[maya.mantach@blominvestbank.com](mailto:maya.mantach@blominvestbank.com)  
 +961 1 1 747 802 Ext: 1240

Malak Hawa, Equity Analyst  
[malak.hawa@blominvestbank.com](mailto:malak.hawa@blominvestbank.com)  
 +961 1 1 747 802 Ext: 1260

**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

**IMPORTANT DISCLAIMER**

This research is based on current public information that we consider reliable, but we do not represent it is accurate or complete, and it should not be relied on as such.

Blom Bank SAL or Blom Invest SAL can have investment banking and other business relationships with the companies covered by our research. We may seek investment banking or other business from the covered companies referred to in this research.

Our salespeople, traders, and other professionals may provide oral or written market commentary or trading strategies to our clients and our proprietary trading desks that reflect opinions that are contrary to the opinions expressed in this research. Our asset management area, our trading desks and investing businesses may make investment decisions that are inconsistent with the recommendations or views expressed in this research.

We and our affiliates, officers, directors, and employees, excluding equity analysts, will from time to time have long or short positions in, act as principal in, and buy or sell, the securities or derivatives (including options and warrants) thereof of covered companies referred to in this research.

This research is not an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients.

Clients should consider whether any advice or recommendation in this research is suitable for their particular circumstances and, if appropriate, seek professional advice. The price and value of the investments referred to in this research and the income from them may fluctuate.

Past performance is not a guide to future performance, future returns are not guaranteed, and a loss of original capital may occur. Certain transactions, including those involving futures, options, and other derivatives, give rise to substantial risk and are not suitable for all investors. Fluctuations in exchange rates could have adverse effects on the value or price of, or income derived from, certain investments.

Copyright 2014 BLOM Invest SAL.

No part of this material may be copied, photocopied or duplicated in any form by any means or redistributed without the prior written consent of Blom Invest SAL.