

Alert on 2011 Earnings Report

Sector: Basic Materials & Industrial Products

Country: Lebanon

Date: June 5, 2012

Share Price (USD): 16.50

Fair Value (USD): 15.24

Downside: -7.64%

Recommendation: Hold

Maintaining a HOLD recommendation with a target share price of USD 15.24 as earnings meet our expectations

Sales grow as local demand exhausts Holcim Liban's capacity

Revenues at Holcim Liban (HL) reached USD 196 million in 2011, growing by 5.7% y-o-y, led by rising prices and slight growth in local demand. The size of the Lebanese grey cement market grew to 5.5 million tons in 2011, of which HL was able to satisfy 2.2 million tons. Grey cement export sales however remained negligible in 2011 due to local demand exhausting the company's total capacity and prices in Syria remaining highly unattractive to local producers. White cement sales volume increased by 51% y-o-y to 97,000 tons, as the surge in the local demand offset the near halt in exports that resulted from serious border issues arising from the unfolding instability in Syria.

High energy prices reduce profit margins and net earnings

HL's gross income declined by 4.5% to \$65.9 million in 2011, as a rise in energy prices during the second half of the year negatively impacted profitability. This translated into gross margins tightening from 37.3% in 2010 to 33.7% in 2011. Similarly, net income also contracted by nearly 16% y-o-y falling to \$28.3 million, mainly due to higher production costs. Net profit margin for 2011 also dropped to 14.5% from 18.2% for the previous year.

Solid balance sheet leads to debt reduction

During 2011, HL continued experiencing high levels of liquidity which permitted paying down its debt. In addition, the company is still going forward with the projected 50% capital reduction on the nominal value of HL's stock, amounting to \$64.7 million or the equivalent of \$3.3 per share expected to be completed near year-end. Despite significant debt repayment and the distribution of \$30.8 million in dividends on 2010 profits, HL maintained current and cash ratios at 1.7 and 0.4, respectively. The cement producer further agreed to pay out \$26.5 million in dividends during the year on 2011 profits.

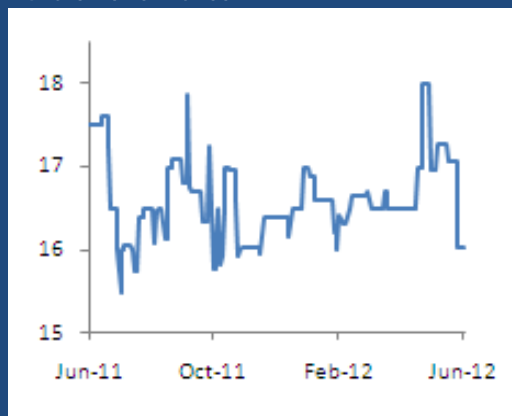
Target price lowered on signs of lower activity in the real estate market

With the real estate market in Lebanon exhibiting signs of slowness since the beginning of the year, we lower our target price to \$15.24 from \$16.16 previously and maintain a HOLD recommendation with a discount rate of 15% and a 3.0% terminal growth, revised down from 3.5% previously. We note that if the company completes the anticipated capital reduction, the share price would decline by an amount close to the reduction to hover near \$13.

Share Data

Bloomberg Symbol	HOLC LB
Reuters Symbol	HOLC.BY
Market Cap	341,530,700
Number of Shares	19,516,040
Free Float	17.8%
Price-to-Earnings 11	11.03
Price-to-Book 11	2.16

Share Performance



Source: Bloomberg

1 Month Return	-5.60%
3 Month Return	-2.91%
6 Month Return	-2.32%
12 Month Return	-8.56%
52 Week Range	15.49 – 18.00

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Performance and Forecasts

Year	2010	2011	2012e	2013f	2014f	2015f
Revenues (USD millions)	185.0	195.6	201.1	207.0	213.0	225.0
Net Income (USD millions)	33.7	28.3	30.7	30.9	31.4	33.1
EPS (USD)	1.73	1.45	1.57	1.58	1.61	1.70
BVPS (USD)	9.07	8.18	9.08	9.06	8.98	9.17
ROA	11.5%	9.6%	10.3%	10.3%	10.3%	10.7%
ROE	15.8%	13.1%	14.1%	13.9%	13.9%	14.6%

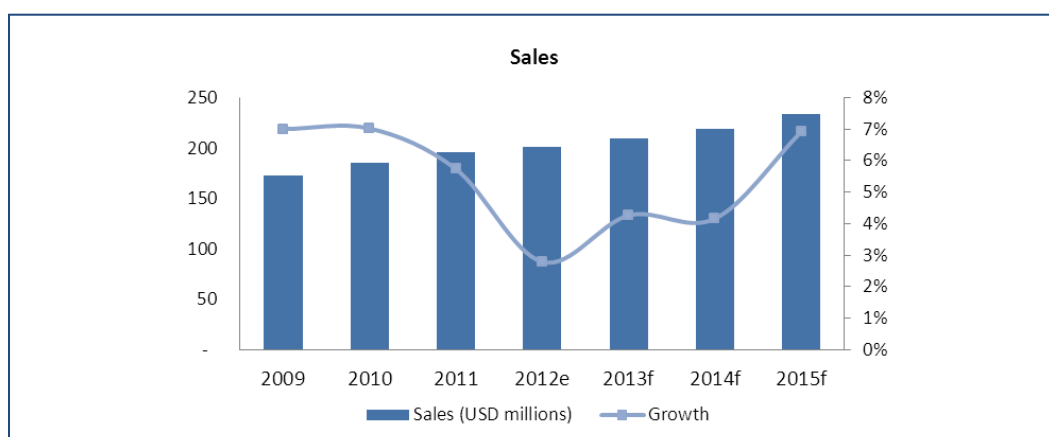
Source: Company Financials, Blominvest Estimates

INCOME STATEMENT HIGHLIGHTS

Revenues

Holcim Liban's (HL) revenues recorded a 5.7% y-o-y increase in 2011 reaching \$196 million, expanding at a slightly slower pace than the 7.0% growth a year earlier. This expansion was caused by rising local prices, along with slim growth in demand despite fears of a construction and real estate slow down.

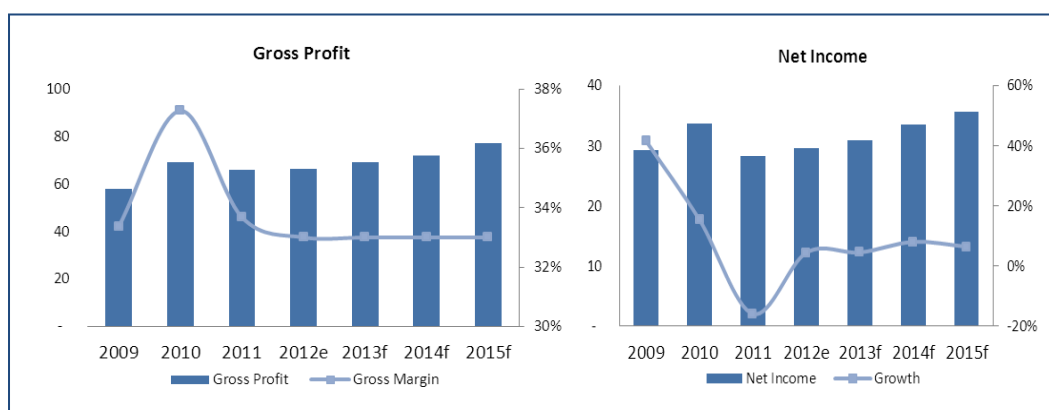
Local demand for grey cement reached 5.5 million tons for the year, out of which HL was able to satisfy 2.22 million tons, or a nearly 2.0% y-o-y increase in sales volume for the product. White cement sales volume witnessed a spike in growth, increasing by 51% y-o-y to nearly 97,000 tons in 2011, near its full capacity which is estimated around 100,000 tons.



Source: Blominvest

Grey cement export sales remained negligible in 2011 with local demand exhausting the company's total capacity. This trend is expected to continue, as higher local cement prices present Holcim with more profitable opportunities.

White cement export sales, however, witnessed a large decline from 38,100 tons a year earlier to negligible levels in 2011 due to serious border issues arising from the unfolding instability in Syria.



Source: Blominvest

Earnings and margins

Despite improvement in overall sales, HL's gross income in 2011 declined by 4.5% y-o-y to \$65.9 million, as a rise in energy prices during the second half of the year negatively impacted profitability. This translated in gross margins tightening from 37.3% in 2010, to 33.7% in 2011. Following, HL's operating margin dropped from a six year high of 23% in 2010, to 18.9% in 2011, with distribution, selling and administrative expenses accounting for 12.7% of sales versus 11.7% a year earlier.

Net income contracted in 2011 by nearly 16% y-o-y to \$28.3 million from \$33.7 million. This was mainly due to the increased production costs, as financing expenses declined by \$700,000 with HL continuing to reduce the amount of outstanding debt it carries on its balance sheet. As a result, net profit margin in 2011 stood at 14.5%, versus 18.2% a year earlier.

BALANCE SHEET HIGHLIGHTS

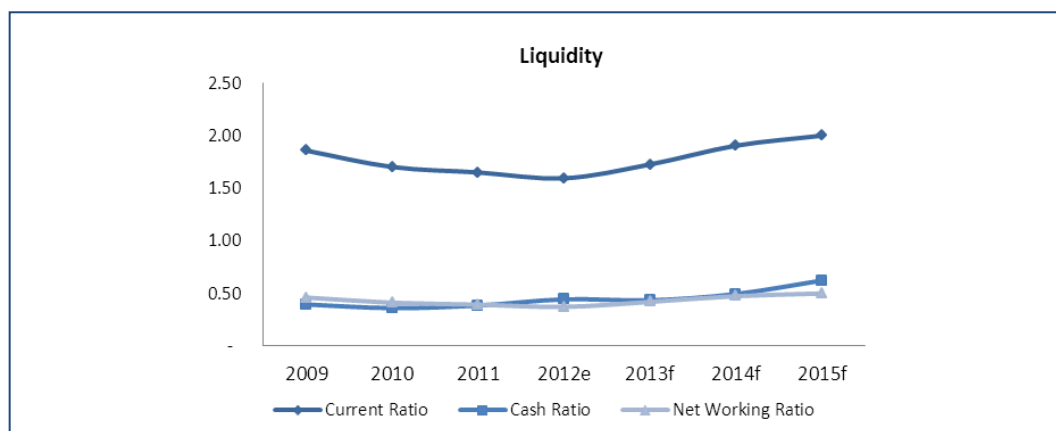
Liquidity

In 2011, HL's balance sheet witnessed a \$22.5 million increase in its cash and inventories against a \$15 million rise in current liabilities, leading to current and cash ratios remaining relatively unchanged at 1.65 and 0.38, respectively, while the net working capital ratio slightly decreased to 0.39 from 0.41 in 2010. The current portion of loans and borrowings declined by around \$6 million last year as the company continues to reduce its dependence on debt, but this gain was largely offset by a \$22 million growth in the payables and accruals account.

Current Ratio = Current Assets / Current Liabilities

Cash Ratio = Cash / Current Liabilities

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



Source: Blominvest

Dividend payment

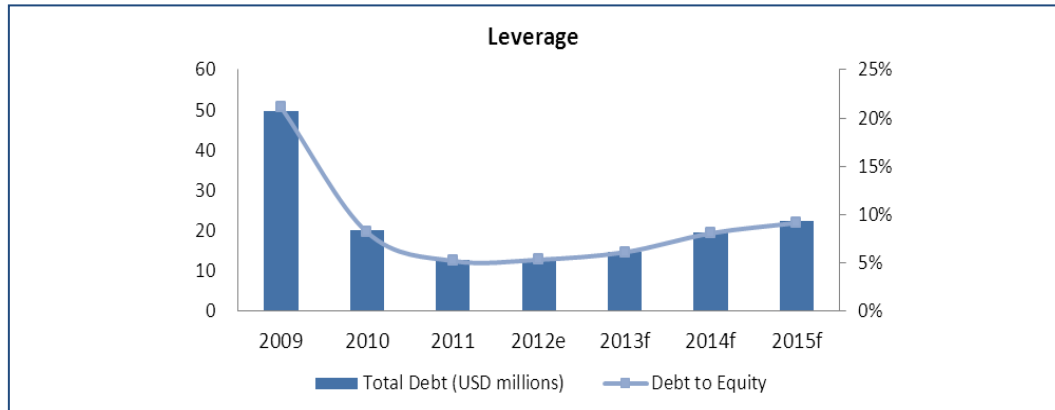
HL distributed \$30.25 million in dividends on the profits of 2010 for a dividend yield of around 9.1% on the year-end 2010 closing share price of \$17.00 per share. The company will further distribute \$26.57 million, or \$1.36 per share, in dividends on 2011 earnings for a gross dividend yield of 8.0% on the year-end 2011 closing share price of \$16.98.

Capital reduction

The extraordinary General Assembly held on December 14, 2010 voted for a capital reduction of \$64.7 million, to be paid upon the completion of some legal proceedings estimated to persist at least until the end of 2012. The company expects to repay around 50% of the nominal value of its stock, or an equivalent of LL 5,000 (\$ 3.3) per share on the 19,516,040 shares which constitute HL's share capital. Were the company to complete the capital reduction as expected, we believe that the share price of HL would decline by an amount close to the reduction to hover near \$13.

Financial Leverage

During 2011, HL repaid another \$2 million of its non-current portion of debt which fell to \$10 million sending the gearing ratio – which measures a company's long-term debt to equity – down to 4.84% in 2011 from 19% only two years earlier. Repayment of debt has been mostly enabled by the high levels of liquidity during the year, especially since no new major capital expenditures have been planned for the near future.



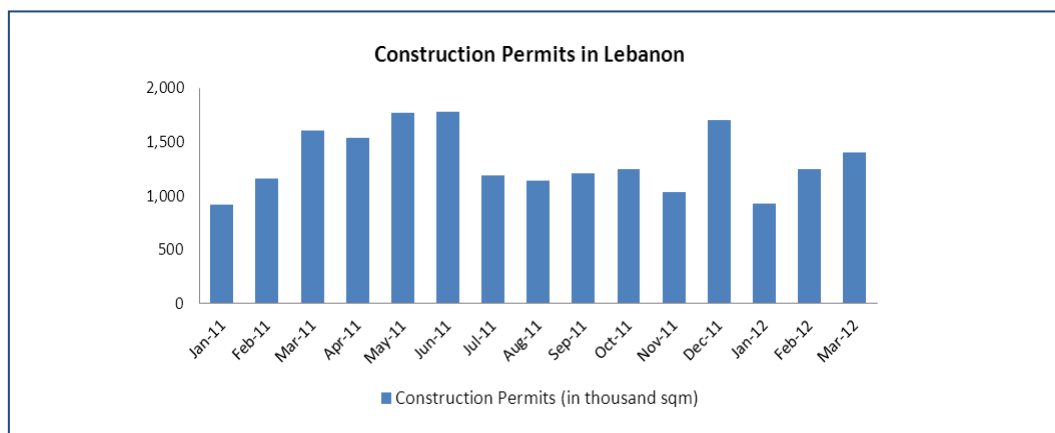
Source: Blominvest

OUTLOOK

The Lebanese real estate market faces a challenging year

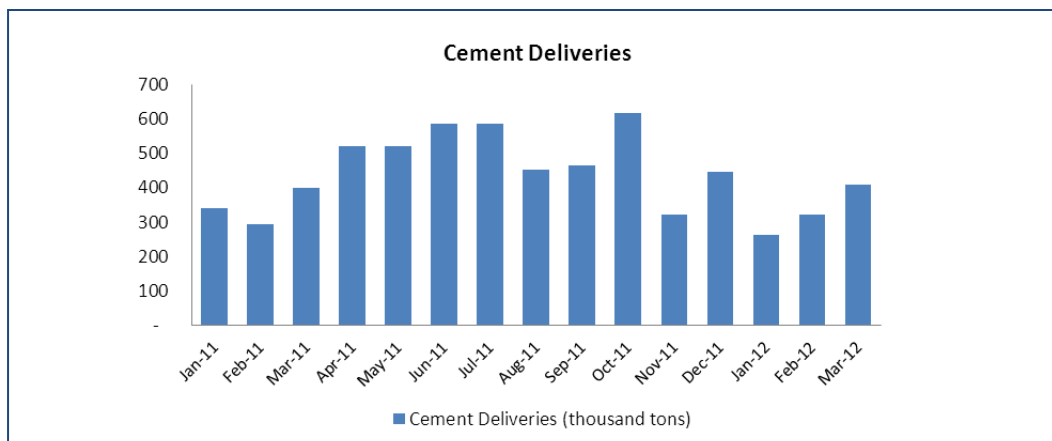
The real estate sector in Lebanon seems to have started the year on a decline compared to the same period in 2011, as the number of construction permits in terms of square meters has posted a 2.50% y-o-y decrease. On the demand side, the number of real estate sales transactions during the first four months of the year fell by 6% y-o-y to 22,141 as the regional political instability and the unfolding crisis in Syria is impacting the Lebanese market.

It is also important to note that a newly proposed tax on capital gains made through real estate is part of the revised 2012 budget draft as announced by Finance Minister Mohammad Safadi. The tax would amount to 15% of capital gains on properties bought after 2009. As for properties that were acquired before 2009, a 4% tax applies on the total sale value. The law is mostly applicable to individuals excluding the sale of their primary residences. Of course this draft would have to be approved by both the council of ministers and parliament in order to go into effect



Source: BDL, Blominvest

In comparison, the value of real estate transactions increased by 4% y-o-y, giving evidence that prices remain relatively sticky as developers keep prices high in the face of the slowing demand, reflective of the cost of land that seems to be withstanding the demand's downward trend. On the supply side, cement deliveries declined by 4.2% y-o-y over the first quarter of 2012 to 992 thousand tons further enforcing our anticipation for a slowing real estate market.



Source: BDL, Blominvest

Anticipating a decline in Holcim's top line for 2012

Holcim's 2011 results were resilient given the headwinds of higher energy costs and the ongoing political instability plaguing the region. Going forward, we anticipate a continued slowdown in the Lebanese real estate market which will slightly lower demand for cement from 5.5 million tons in 2011 to 5.3 million tons, but will stabilize thereafter slightly increasing through 2015.

In our financial model, we increase the price of grey cement to \$100 per ton from \$90 per ton used previously, supported by rising oil prices. On the other hand, we believe the price of white cement will remain near \$181 per ton. Gross margin is expected to stabilize near 33% for 2012 supported by sustained production efficiency. HL's bottom line going forward will be affected by the company's ability to counteract a slower growth pattern against continually increasing cement prices.

Finally, we lowered our terminal growth rate to 3.0% from 3.5%, in line with our expectations for sluggish revenue as no long-term capacity expansion plans have been planned or announced according to HL's management. We maintain a discount rate of 15% as the risk associated with the current turmoil in Syria impacting the Lebanese market is already reflected in our forecasts with Holcim operating below its full capacity in 2012.

PROJECTED INCOME STATEMENT

<i>In USD million</i>	2009	2010	2011	2012e	2013f	2014f	2015f
Sales of Goods	173	185	196	201	207	213	225
Production Cost of Goods Sold	(115)	(116)	(130)	(134)	(138)	(142)	(150)
Gross Profit	58	69	66	67	69	71	75
Distribution & Selling expenses	(15)	(17)	(19)	(19)	(21)	(21)	(22)
Administrative Expenses	(4)	(5)	(6)	(6)	(7)	(7)	(7)
Other Income	2	2	2	1	1	1	1
Other Expenses	(4)	(6)	(6)	(5)	(5)	(5)	(5)
Interest Income	0	0	0	0	1	1	1
Finance Costs	(3)	(2)	(1)	(2)	(2)	(2)	(3)
Profit Before Tax	35	40	36	37	37	37	39
Income Tax Expense	(6)	(7)	(7)	(6)	(6)	(6)	(6)
Profit for the Year	29	34	28	31	31	31	33

Source: Blominvest

PROJECTED BALANCE SHEET

<i>In USD million</i>	2009	2010	2011	2012e	2013f	2014f	2015f
Current Assets							
Cash & Cash Balances	16	17	24	34	43	50	60
Inventories	36	40	56	44	48	51	49
Accts Receivables & Prepayments	23	23	24	24	25	26	27
Total Current Assets	75	80	103	102	116	126	137
Non-Current Assets							
Property, plant & equipment	155	143	137	131	126	121	116
Investment Properties	11	11	11	13	13	15	15
Goodwill	18	18	18	18	18	18	18
Intangible assets	35	32	27	25	23	21	19
Other Financial Assets	4	4	4	6	7	7	8
Total Non-Current Assets	224	207	197	193	187	182	176
Total Assets	299	288	301	296	303	308	313
Current Liabilities							
Loans & Borrowings	10	8	2	7	7	10	13
Accounts Payable & Accruals	25	33	55	44	48	45	43
Taxes Payable	5	7	5	5	5	5	5
Provision for Risks & Charges	0	0	0	1	1	1	1
Total Current Liabilities	41	47	63	57	61	61	63
Non-Current Liabilities							
Loans & Borrowings	40	12	10	11	11	14	15
Provision for employee benefits	4	4	4	5	5	5	5
Provision for risks & Charges	4	6	8	1	1	1	1
Deferred Tax Liability	1	1	0	0	0	0	0
Total Non-Current Liabilities	49	24	23	17	17	21	21
Shareholders' Equity							
Share Capital	129	129	129	129	129	129	129
Statutory Reserve	17	19	23	25	27	29	31
Revaluation Reserve	34	34	34	34	34	34	34
Retained earnings	26	30	30	27	30	31	33
Total Equity	210	217	215	222	224	226	228
Total Liabilities & Equity	299	288	301	296	303	308	313

Source: Blominvest

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