

October 7<sup>th</sup>, 2016

## Solidere Profits for H1 2016 reach \$72.10M and fair value revised to \$11.68

Bloomberg / Reuters Symbol:	SOLA.LB/ SOLA.BY
Share Price on 07/10/2016:	USD 9.56
Target Price:	USD 11.68
Recommendation:	BUY

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### Delivery of Plots Boosts Income Statement

Solidere released its consolidated financial statements for the first 6 months of 2016, revealing an improvement in its bottom line from a net loss of \$28.71M by H1 2015 to a net profit of \$72.10M over the same period this year. During the first half of 2016, Solidere sold 40,000 sqm of Built Up Area (BUA), 5,500 of which were in the traditional area, with the remaining portion sold in the Waterfront. The average price per BUA was \$3000-\$3500.

### Financial Performance Summary

\$M	2016	2015	Y-t-D change
Net Income	72.1	(28.71)	351.13%*
Total Assets	2,924.37	2,917.50	0.24%
Total Liabilities	912.49	960.01	-4.95%
Total Equities	2,011.88	1,957.49	2.78%

\*Net Income is reflective of the yearly change between H1 2016 and H1 2015

Total revenues registered \$160.67M for the first six months of 2016, compared to \$57.84M in H1 2015. The total cost of revenue expanded at a slower pace, ending the period at \$41.72M compared to \$21.83M. As such, Solidere's net operating margin improved from 64.35% by June 2015 to a higher 74.45% margin by H1 2016. Solidere is expected to recognize the sale of an additional 30,000 sqm currently held in backlog before the end of the fiscal year. Therefore, Solidere's sales are expected to surpass the \$200M mark for the first time since 2011. Recently, Solidere has been hampered by liquidity issues and lack of investment appetite due to the troublesome local and regional political scene.

### Revenue Breakdown by Segment

Revenues from land sales reached \$128.90M by June 2016, compared to \$26.40M over the same period in 2015. The operating profit margin improved from 74.38% in H1 2015 to 80.04% in H1 2016. Solidere's Investor Relations (IR) affirmed that all buyers were Lebanese, as foreign demand remains subdued, and that the Waterfront plots sold were to be developed both for office and residential purposes. Solidere has increasingly loosened its sales terms in the past 2 years to stimulate demand on its plots and accommodate the market changes.

Revenues from rented properties slightly dipped in value, decreasing 0.89% y-o-y to \$27.94M despite occupancy rates remaining stable at 90%, as per Solidere's IR. A similar dip in rental income operating profit margins from 58.11% by June 2015 to 51.92% over the same period this year is likely linked to retail rents being waived during H1 2016 and Solidere offering more flexible terms.

# SOLIDERE

Revenues from services rendered by Solidere to its clients, such as the broadband network (BBN), improved 24.24% y-o-y to \$3.62M by H1 2016.

## Solidere's Focus Is Entirely on Existing Projects

Solidere's current expenditures are divided among the completion of the Waterfront's infrastructure and the department store, which is scheduled to be finalized by early 2018. All other projects are currently put on hold, and will resume among completion of the former two.

## Solidere International Succumbs to GCC Stresses

Solidere International Limited, an associate company which Solidere Group owns 39.05% of and which operates mainly in Saudi Arabia and the United Arab Emirates, recognized a loss of \$6.95M over the first 6 months of 2016. Solidere SAL's share of these results is a \$2.58M loss.

## Balance Sheet Indicates Improved Cash Flow Management

On the balance sheet, Solidere's total assets remained relatively stagnant, increasing 0.24% y-t-d to \$2.92B. It is worth mentioning that net accounts and notes receivables increased by 9.58% y-t-d to \$510.89M, as a result of lower provisions taken out for problematic receivables. Also, Solidere's accounts receivable turnover significantly improved from 2,036 days at end-2015 to 742 days by June 2016, a 5-year low.

On the liabilities side, Solidere managed to decrease its accounts payable from \$111.62M by end-December 2015 to \$105M by H1 2016. The decrease in liabilities contributed to the decrease of Solidere's accounts payable turnover to 953 days from a previous 1,249 days at end-2015.

## Debt Levels Remain High

Solidere's bank overdrafts and short term facilities remained high but displayed a downward trend, decreasing by 5.32% y-t-d to \$526.47M, while the longer term bank loans displayed less of a change, dipping 1.17% to \$130.82M over the same period. As such, the company's annualized implied average interest rate across its short and long term debt is 5.44%. Solidere paid \$18.23M in interest expense during H1.

The company owns a land bank of 1.72M sqm, valued by FFA at roughly \$6.68B last year, with income generating projects valued at another \$1.4B. FFA was commissioned by Solidere to perform the valuation.

## Dividend Distribution for FY 2015

The latest shareholder general assembly on June 27th was concluded with the decision to distribute a dividend share for every 80 shares held, in addition to a cash dividend of 10 cents per share, equivalent to a distribution of approximately 2 million shares, and \$16.5M in cash. These dividends were distributed on July 18th, 2016, and represented a dividend yield of 2.28% at that time.

## Recommendation

We estimate the fair value of Solidere's share at \$11.68, in light of a stagnant economy and a waning demand in real estate, using a combination of the DCF method and the PB multiple, and based on sales forecasts that align with the current company's performance.

Current share price, 07/10/2016,	\$9.56
Target Price	\$11.68
Upside potential	22.18%
Weighted Average Cost of Capital (WACC)	20.01%

Source: Bloomberg, Solidere financials

Blominvest estimated the target price by forecasting Solidere's revenues for the coming 5 years. We used Solidere land sales and rental revenues as the key drivers of net income to arrive to our findings.

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We assumed a base-line scenario that aligns with the forecasts for Lebanon's economic situation and its real estate sector, in which the economic stagnation is expected to continue in the near to medium term. The outlook remains bleak due to the persistence of the Syrian crisis, threatening the country's stability, growth prospects, and fiscal deficit. Moreover, the pressure on the fiscal budgets of GCC members resulting from the slash in oil prices, led them to curb their investments in the region and apply radical spending cuts. Lower Foreign Direct Investments and the expected decline in remittances from the GCC are especially affecting the real estate demand.

As such, we forecast Solidere to sell an average of 40,000 sqm BUA over the following 2 years, with prices to be maintained at current levels of \$3,000-\$3,500 per sqm, as we don't see a nearing revival of real estate prices.

Starting 2019, we forecast BUA sold and unit prices to grow at modest respective annual rates of 10% and 5%, in line with a slight recovery and impact from the growing consumption. As for this year, Solidere's pipeline has around 30,000 sqm of BUA waiting to be recognized before the end of 2016 at price levels similar to those witnessed in H1 2016.

Also in light of the current economic and political situation, we forecast rental occupancy rates to maintain their current levels of 90% in the near future, and assumed a price increase of 5% starting 2019.

<b>Valuation</b>		
	<b>USDm</b>	<b>USD/shr</b>
Value from Land Sales (DCF)	2,097	12.66
Value from Rentals and Services	122	0.74
Book Value of Solidere International	402	2.4
Book Value of Non-Operating Assets	812	4.9
Total Liabilities	(912)	(5.5)
Value Loss from General & Admin.	(67)	(0.4)
Tax Effect	(45)	(0.3)
<b>Fair Value</b>	<b>2,409</b>	<b>14.60</b>
<b>Current Price-to-Book Ratio</b>		<b>0.80</b>
<b>Target Price</b>		<b>11.68</b>

Source: Blominvest, Solidere financials H1 2016

*We therefore issue a BUY recommendation on Solidere shares, with a target price of USD11.71 and an upside potential of 22.49%, based on estimated sales for 2016 of \$290million and estimated profits of \$131million. Barring any cancellations during the course of the final quarter of 2016, and if the transactions lying in the pipeline materialize, Solidere may be set to achieve in 2016 the best results since 2011.*

# SOLIDERE

## Performance of Solidere Class "A" Share on Beirut Stock Exchange

Solidere "A" Close on 07/10/2016	\$9.56
QTD Return	1.72%
6-Month Return	-4.73%
YTD Return	-14.47%
52-Week Range	\$8.20-\$11.47

Source: Beirut Stock Exchange, Blominvest

## 1Y Performance of Solidere Class "A" Share on Beirut Stock Exchange



Source: Beirut Stock Exchange, Blominvest

# SOLIDERE

## Projected Income Statement

<i>In USD million</i>	2011	2012	2013	2014	2015	2016e
Revenues from Land & Real Estate Sales	242	50	95	169	27	226
Revenues from Rented Properties	50	54	52	62	57	56
Revenues from Rendered Services	5	7	8	8	8	8
Cost of Land & Real Estate Sales	(39)	(7)	(19)	(28)	(7)	(45)
Charges on Rented Properties	(22)	(25)	(21)	(25)	(26)	(27)
Cost of Rendered Services	(6)	(8)	(7)	(9)	(6)	(5)
Gain/(Loss) on Sale of Invest. Properties	1	4	4	4	3	-
<b>Net Revenues from Operations</b>	<b>231</b>	<b>71</b>	<b>109</b>	<b>181</b>	<b>55</b>	<b>212</b>
General & Admin. Expenses	(35)	(34)	(31)	(34)	(34)	(32)
Depreciation of Fixed Assets	(5)	(5)	(7)	(6)	(4)	(6)
Other Income (Expense)	(7)	(3)	(3)	0	4	
Interest Income	24	29	19	20	19	20
Interest Expense	(21)	(26)	(32)	(34)	(35)	(36)
Profit Before Tax	187	18	48	130	(88)	154
Income Tax Expense	(25)	(2)	(6)	(17)	1	(23)
<b>Profit for the Year</b>	<b>162</b>	<b>16</b>	<b>42</b>	<b>113</b>	<b>(87)</b>	<b>131</b>

Source: Solidere Financials, Blominvest Estimates

## Balance Sheet Summary

<i>In USD million</i>	2012	2013	2014	2015	H1 2016
Cash & Cash Balances	149	165	148	136	132
Accounts & Notes Receivables	546	435	438	466	511
Inventory of Land & Real Estate	1,208	1,143	1,153	1,134	1,095
Investment Properties	437	565	563	593	614
Other Assets	405	476	468	589	572
<b>Total Assets</b>	<b>2,745</b>	<b>2,784</b>	<b>2,770</b>	<b>2,918</b>	<b>2,924</b>
<b>Total Liabilities</b>	<b>908</b>	<b>905</b>	<b>893</b>	<b>960</b>	<b>912</b>
<b>Total equity</b>	<b>1,908</b>	<b>1,952</b>	<b>2,065</b>	<b>1,957</b>	<b>2,076</b>
<b>Book Value Per Share (USD)</b>	<b>11.48</b>	<b>11.74</b>	<b>11.73</b>	<b>11.86</b>	<b>12.19</b>
<b>Price-to-Book Value</b>	<b>1.11</b>	<b>1.09</b>	<b>1.02</b>	<b>0.90</b>	<b>0.80</b>

Source: Solidere Financials

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## 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