Sidi Kerir Petrochemicals Co.

بلوم مصر لتداول الأوراق المالية
BLOM EGYPT SECURITIES

BLOMINVEST BANK

Equity Research – Initiation of Coverage		Share Price (EGP):	11.45
Sector:	Petrochemicals	Fair Value (EGP):	13.75
Country:	Egypt	Upside:	20%
Date:	November 28, 2011	Recommendation:	HOLD

Initiating with a HOLD Recommendation and a Fair Value of EGP 13.75 per share

Slow demand in Egypt to be counterbalanced by exports

The slow economic growth and political uncertainty in Egypt is expected to cause local demand for petrochemicals to decline. The IIF estimates real GDP in the country to grow by 1.2% for 2011 and 1.8% for 2012. However, we expect Egyptian exports to increase as the Egyptian Pound has been trading near a seven year low of EGP 6.02 / USD, positioning Egyptian products as attractive in markets abroad. Even though forecasts for economic growth in both Europe and the US remain fairly disappointing, ethylene inventories have been reduced considerably as most producers are operating at low utilization rates.

Revenues grow impressively but reenacting tax reduces profitability

We estimate 2011's revenues around EGP 2.35 billion, almost 24% higher than 2010. Prices for Sidpec's core products are currently being traded at an average of USD 1,380 / ton, 25% higher than 2010 and 8% higher than 2008 which is the company's record sales year. Even though we expect revenues to grow considerably during 2011, Sidpec's net income is expected to grow more modestly due to the expiration of its tax exemption. We estimate a 2011 net income of EGP 891 million, 9% higher than 2010 with profit margin shrinking from 43.5% in 2010 to 38% in 2011.

A cash rich operation with little or no leverage

Sidpec reported EGP 650 million in cash for its first half in 2011, almost 8x its current liabilities. Its strong liquidity position is also indicated by its current assets, which are 21x its current liabilities. We expect this strong position to persist over the coming few years as no major capital expenditures are planned besides its 20% equity stake in the expansion plans with GASCO. Leverage at Sidpec is almost non-existent with a debt to equity ratio consistently between 0% and 1%.

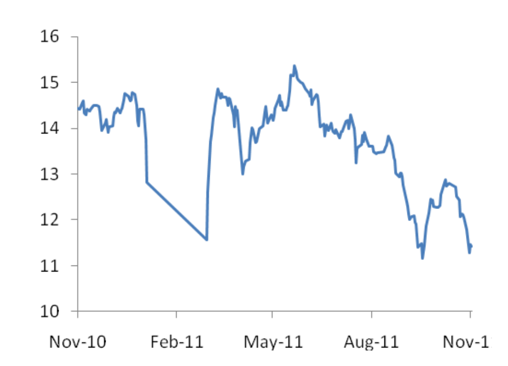
Stock trades at a significant discount due to unrest in Egypt

We value Sidpec at EGP 13.75 using a DCF method with a WACC of 15% and a terminal growth rate of 2%. Forecasts were extended over a five year period assuming no additions in production capacity. With a P/E of 7.8, the stock is undervalued compared to global and regional peers offering the potential to appreciate at least another 30% to be on par with the average. We attribute this valuation discount to the situation in Egypt where Sidpec generates 60% of its revenues. Challenges on structuring Egypt's democracy continue forcing us to recommend a wait-and-see approach unless an investor is willing to take considerable risk.

Share Data

Bloomberg Symbol	SKPC EY
Reuters Symbol	SKPC.CA
Market Cap (EGP)	6,037,500,000
Number of Shares	525,000,000
Free Float	23%
Price-to-Earnings	7.80
Price-to-Book	2.80

Share Performance



Source: Reuters

1 Month Return	-6.93%
3 Month Return	-16.09%
6 Month Return	-19.41%
12 Month Return	-20.86%
52 Week Range	15.36 – 11.16

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Performance and Forecasts

Year	2010	2011e	2012f	2013f	2014f
Revenues (EGP millions)	1,891	2,328	2,209	2,278	2,171
Net Income (EGP millions)	821	888	809	823	767
EPS (EGP)	1.56	1.69	1.54	1.57	1.46
BVPS (EGP)	4.92	4.70	4.35	4.24	4.24
ROA (%)	31.1	34.0	32.8	35.0	33.0
ROE (%)	34.5	37.6	36.9	40.1	38.2

Source: Company Historicals and Blominvest Estimates

FINANCIALS & VALUATION

Year	2010	2011e	2012f	2013f	2014f
Profit & Loss Summary					
Revenue (EGPm)	1,891	2,328	2,209	2,278	2,171
Revenue Growth (%)		23.1	-5.1	3.1	-4.7
EBITDA (EGPm)	895	1,218	1,114	1,111	1,080
EBITDA Margin (%)	47.3	52.3	50.4	48.8	49.8
Net Profit (EGPm)	821	888	809	823	767
Profit Margin (%)	43.4	38.1	36.6	36.1	35.3
Net Profit Growth (%)		8.2	-8.9	1.7	-6.8
Earnings Per Share (EGP)	1.56	1.69	1.54	1.57	1.46
Price-to-Earnings (Forward P/E)	7.36	6.80	7.46	7.34	7.87
Balance Sheet Summary (EGPm)					
Cash & Cash Balances	830	978	906	880	934
Current Receivales	187	210	221	198	239
Total Inventory	231	244	210	242	261
Fixed Assets	844	726	632	546	474
Other Assets	561	405	408	411	415
Total Assets	2,653	2,563	2,376	2,278	2,321
Total Liabilities	72	95	95	96	94
Book Value Per Share (EGP)	4.92	4.70	4.35	4.16	4.24
Profitability					
ROA (%)	31.1	34.0	32.8	34.0	33.3
ROE (%)	34.5	37.6	36.9	38.9	38.6
Liquidity					
Cash / Current Liabilities	11.5	11.6	10.8	10.3	11.2
Current Assets / Current Liabilities	24.2	21.0	20.0	19.5	21.2
Net Working Capital / Current Assets	1.0	1.0	0.9	0.9	1.0

Comparables

	Valuation			Margin Analysis (%)			Profitability (%)	
	P/E	P/Rev	P/BV	Gross	Operat.	Net	ROE	ROA
Sidi Kerir	7.8	3.6	2.8	50.2	38.9	43.4	34.5	31.1
Global Average	14.2	1.7	2.5	28.3	12.4	9.8	16.6	9.0

Valuation

In EGP million	2011e	2012f	2013f	2014f	2015f
Revenues	2,328	2,209	2,278	2,171	2,180
Net Income	888	809	823	767	817
Free Cash Flow	804	1,025	910	824	959
Terminal Value					7,527
Discounted Cash-flows	804	892	688	542	4,291
Sidi Kerir Total Value					7,216
Number of shares (in millions)					525
Share Value (EGP)					13.75

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INVESTMENT SUMMARY

We issue a HOLD recommendation on Sidi Kerir after carefully analyzing the following:

Macroeconomic Environment

Demand and pricing of petrochemicals is favorable during an economic expansion as its prices have historically exhibited a direct correlation to GDP growth. The cracking of oil is the primary process for the production of ethylene and propylene. It therefore isn't a surprise that prices of petrochemicals also follow the price of oil which has been currently experiencing downward pressure due to a slowdown in the global economy. European demand for petrochemicals has been mildly slowing during the second half of 2011, but the likelihood of a crash or a significant decline in pricing seems remote. Even though forecasts for economic growth in both Europe and the US remain fairly disappointing, inventories have been reduced considerably as most petrochemical producers are operating at low utilization rates. China's overheating economy is another key driver that we will monitor closely as it is the world's largest buyer of petrochemicals. In Egypt, the slow economic growth and political uncertainty is expected to cause local demand for petrochemicals to decline. The Institute of International Finance estimates real GDP in the country to grow by 1.2% for 2011 and 1.8% for 2012. On a positive note however, Egyptian exports are expected to increase as the Egyptian Pound has been trading near a seven year low of EGP 6.02 / USD positioning Egyptian products as attractive in markets abroad.

Business Model

Sidi Kerir, also known as Sidpec, is Egypt's only producer of ethylene and polyethylene established in 1997 in sponsorship by the Egyptian government. The company focuses on producing two main products, ethylene with a capacity 300,000 tons and polyethylene with a capacity of 225,000 tons. The Egyptian Natural Gas Company (GASCO) supplies Sidpec with its feedstock needs at a subsidized price set according to a formula that management does not disclose. Prior to 2008, Sidpec's gas price was around USD 1.25/mmbtu but was raised to USD 3.00/mmbtu that year leading to a considerable hike in its production costs. We expect the company to continue operating near its full capacity as it is the only Egyptian producer serving the local market. Historically, Sidpec's local sales have constituted around 60% of its revenues with the exception of 2009, where local sales captured almost 64% due to a slowdown in regional markets. We expect the current mix to remain around 60/40 for local/export sales unless an interruption occurs on the local or regional scene.

Growth

We expect 2011's revenues to break Sidpec's 2008 record as prices for ethylene and polypropylene, which constitute more than 95% of revenues, continue to trade at considerable highs during 2011. Prices for Sidpec's core products are currently being traded at an average of USD 1,380 / ton, 25% higher than 2010 and 8% higher than 2008 which is the company's record sales year. Prices for its products move in tandem with oil prices for which we do not expect further price appreciation and therefore anticipate revenues to hover between EGP 2 billion and 2.3 billion in the near future. We estimate 2011's revenues around EGP 2.35 billion, almost 24% higher than 2010. Another key factor in the revenue equation is Sidpec's production capacity in which we expect no expansion to come online before 2015. Sidpec has signed an agreement with GASCO, its feedstock supplier, to build a new ethylene production facility with an annual capacity of 460,000 tons of ethylene, 400,000 of polyethylene and 20,000 tons of butadiene. The company has already leased 60 acres of its unused land and raised USD 100 million as paid-in-capital to begin funding the project. Sidpec's share in the project is estimated at 20% and will therefore be treated as an equity investment.

Profitability

Even though we expect revenues and EBITDA to grow considerably during 2011, Sidpec's net income is expected to grow more modestly due to the expiration of its corporate tax exemption. We estimate a 2011 net income of EGP 891 million, only 9% higher than 2010 with profit margin shrinking from 43.5% in 2010 to 38% in 2011. We estimate both ROA and ROE to rise in 2011 to reach 34% and 37%, respectively. Of course, the company's profitability relies on movements in oil prices which we assume to slightly decline during 2012. With no anticipated change in Sidpec's financial structure, we expect ROA and ROE to remain steady in the near future.

Financial Position

Sidpec enjoys an extremely strong liquidity position with its current assets estimated at around 21x its current liabilities for 2011. The company reported EGP 650 million in cash for its first half in 2011, almost 8x its current liabilities. We expect this strong position to persist over the coming few years as no major capital expenditures are planned besides its 20% equity stake in the expansion plans with GASCO. Leverage at Sidpec is almost non-existent with a debt to equity ratio consistently between 0% and 1%. The company has had a stable operation since its inception with strong backing from government entities and little need for any debt. Sidpec doesn't have any noticeable interest expenditures and therefore its interest coverage ratio is extremely high reaching a low of 39 in 2008. We consider companies that have a coverage ratio over 8 to be relatively safe investments.

Valuation

We valued Sidpec at EGP 13.75 using a DCF method with a WACC of 15% and a terminal growth rate of 2%. Revenue forecasts were extended over a five year period assuming no additions in production capacity with utilization rates of 92% for ethylene and 100% for polyethylene. We assumed fluctuating petrochemical pricing with a sideway pattern as a conservative and realistic measure. Production costs have been estimated between 45% and 49% of revenues while Selling, General and Administrative have been estimated to be around 2.7% of revenues in line with the historic average.

Sidpec's relative valuation appears to be attractive compared to both regional and global peers. With a price-to-earnings (P/E) of 7.8, the stock has the potential for appreciating at least another 30% – 40% to be on par with the average. We attribute the discount it currently trades at to the political situation in Egypt where the company generates around 60% of its revenues. Challenges on structuring Egypt's democracy persist and with the long-awaited elections closing in, we would recommend a wait and see approach unless an investor is willing to take considerable risk.

Market Risks

We have three major concerns related to investing in Sidpec, two of which, oil shocks and the global economy, are linked. As previously mentioned, petrochemical pricing is directly correlated to the price of oil. Any substantial decline in oil pricing may impact profitability at Sidpec and any other petrochemical company. Likewise, demand for petrochemicals, which also affects pricing, relies on economic expansion as most products are used in cyclical industries such as housing and automotive. In our forecasts, we assumed a soft and gradual economic recovery over the next three years reflected in the overall demand and pricing of petrochemicals. Any further delay in the economic recovery of leading economies may have a negative effect on our recommendation. Finally, any sudden increase in feedstock pricing at which Sidpec receives from GASCO will also have an effect on the company's profit margins. The parameters in the pricing formula through which Sidpec sources its feedstock are reviewed every three years with the latest review completed in 2010. No adjustments were made and we do not attribute any significant risk to changes in the formula until 2013.

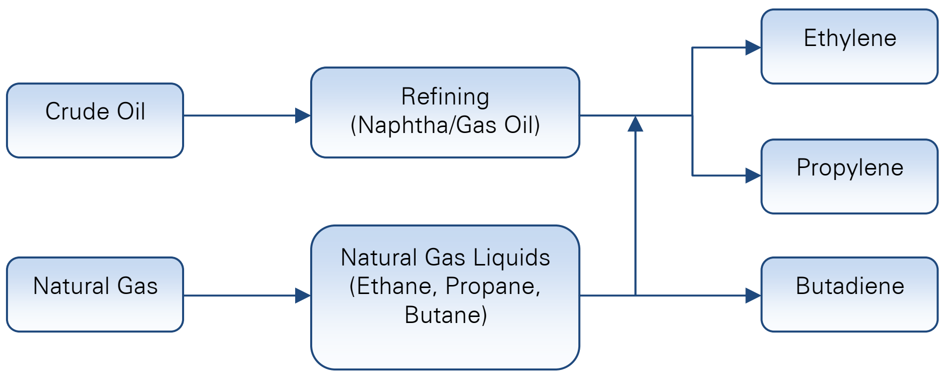
ECONOMIC OVERVIEW

Petrochemicals are produced from crude oil or natural gas

The petrochemical industry is among the most vital industries in the modern world economy, converting raw materials like oil and natural gas into more than 70,000 different products.

Crude oil and natural gas are considered to be the primary feedstock for the industry.

Naphtha, which is produced from crude oil, offers a more extensive selection of end products while natural gas-based production involves lower production costs.



The basic petrochemicals that result from feedstock are ethylene and propylene which in turn produce various intermediates and end-products.

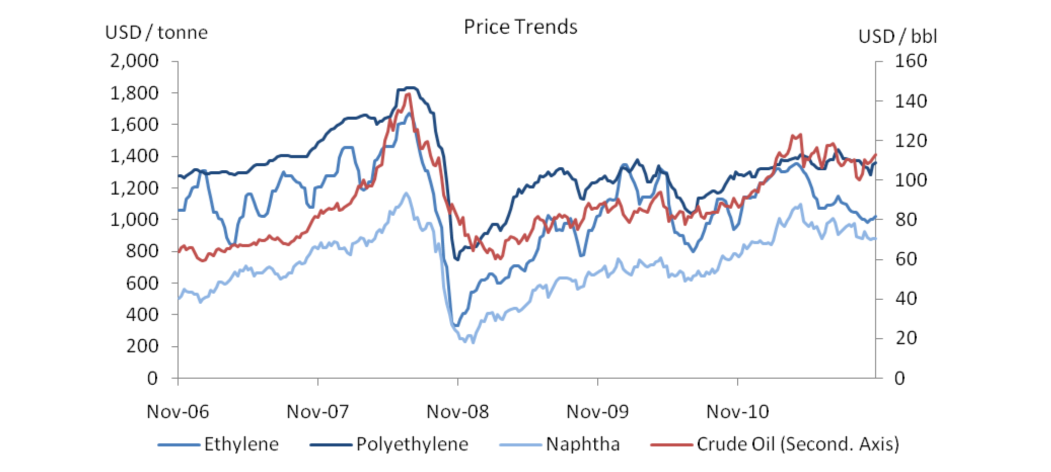
Examples of the Value Chain of Basic Petrochemicals

Basic	Intermediates	Applications
Ethylene	Low-Density Poly-Ethylene (LDPE) High Density Poly-Ethylene (HDPE)	Bottles
	Ethylene Dicloride	Pipes
	Ethylene Oxide Ethylene Glycol	Automotive
	Ethyl Benzene	Tires, Footwear
Propylene	PolyPropylene	Pipes
	Propylene Oxide	Fibers, Foam
	Isopropyl Alcohol	Plastics, Paints
Butadiene	Polybutadiene Rubber	Tires, Golf Balls

Source: Blominvest

Pricing of petrochemicals exhibit a positive correlation with oil prices and GDP growth

With the exception of petrochemicals produced in the Middle East through natural gas, naphtha cracking is the primary process used for the production of ethylene and propylene. As a result, prices of these basic petrochemicals follow those of naphtha, which in turn is obtained by the cracking of oil. This illustrates why petrochemical prices follow that of oil.



Historically, the prices of petrochemical products have also exhibited a direct correlation to GDP growth. During the second half of 2008, prices of end products fell sharply due to the global financial crisis and the fall in oil prices. However, prices have bounced back following the recovery in oil prices and the economic growth registered in leading emerging economies such as China and India.

This leads us to take a closer look at the global economy and the challenges it faces that will impact economic growth, oil prices and demand for petrochemical products. The European crisis is a major concern as government spending to boost the European economies is being reduced in response to the fiscal challenges in many of the EU members. European demand for petrochemicals has been mildly slowing during the second half of 2011, but the likelihood of a crash or a significant decline in pricing seems remote. Even though forecasts for economic growth in both Europe and the US remain fairly disappointing, inventories have been reduced considerably as most petrochemical producers are operating at a low utilization rate. This cautious approach has been repeatedly used to mitigate downside risks during an expected slowdown and will probably serve its purpose in the current economic environment.

Low inventories counterbalance the effects of slow economic growth

China's overheating economy is another key driver that we will monitor closely as it is the world's largest buyer of petrochemicals, mostly from the Middle East. A property crash would have severe repercussions similar to those we witnessed following the US sub-prime crisis. Several markets will be affected, among which are petrochemicals. If China reduces its demand for petrochemicals, Middle Eastern producers would target other global markets as they have access to cheap feedstock and can compete in any market regardless of the business cycle. This will prompt producers in more developed countries with higher ethylene production costs to shift their focus to more sophisticated production and maybe even reduce their capacity or, in an extreme case, shut down completely.

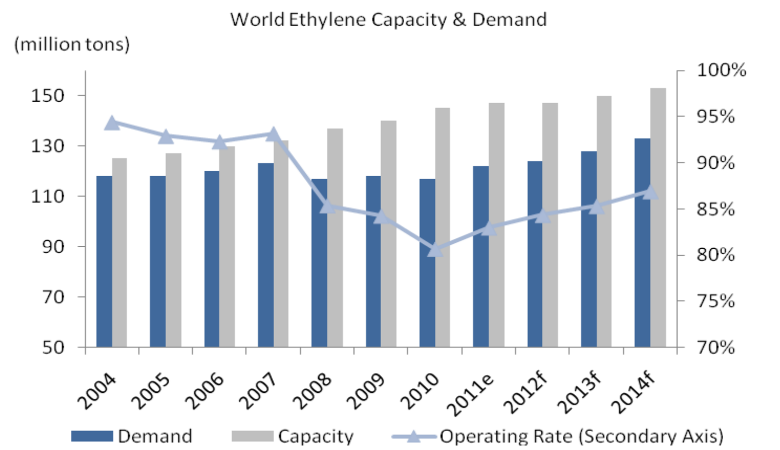
Finally, the effects of the earthquake that struck Japan during this year will probably continue well on into 2012 as Japanese petrochemical plants are forced to operate below capacity due to electricity shortages. The logistical infrastructure and electricity supply will need time to be fully repaired leading to shortage of petrochemicals in the region.

Ethylene demand has been estimated to annually grow at a rate of 1.5 times the global GDP growth rate

Global demand for Ethylene expected to grow faster than capacity expansion

Discrepancy between demand and supply of Ethylene and Propylene may also affect the pricing of petrochemicals. A key indicator that is normally monitored is the "operating rate", which is the percentage of available capacity that is being produced/supplied. When there is high demand, companies normally produce near-full capacity pushing the operating rate to near 100% and applying upward pressure on prices.

The operating rate has considerably declined during the past few years due to the economic slowdown which reduced demand for the primary products. Ethylene demand has been estimated to grow annually at a rate of 1.5 times the global GDP growth since 1990, which explains the recent decline in Ethylene's operating rate. However, higher operating rates are expected during the next few years as demand is estimated to grow at a faster rate than capacity expansion. Even with this growth however, we do not believe that the operating rate will exceed 85% any time before 2013.

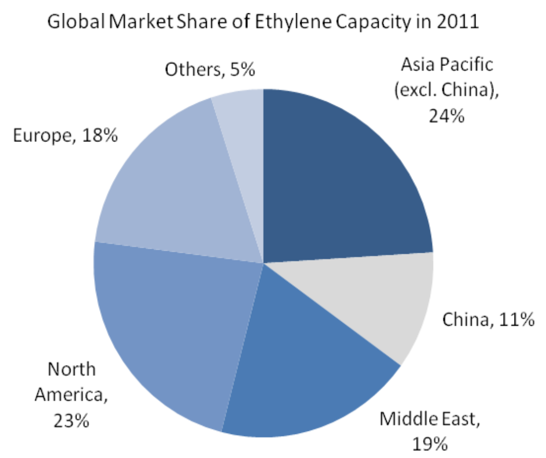


Source: Business Monitor International

Plant closure of high-cost producers in developed countries seems likely

Capacity expansion in the Middle East likely to disrupt balance in global ethylene production

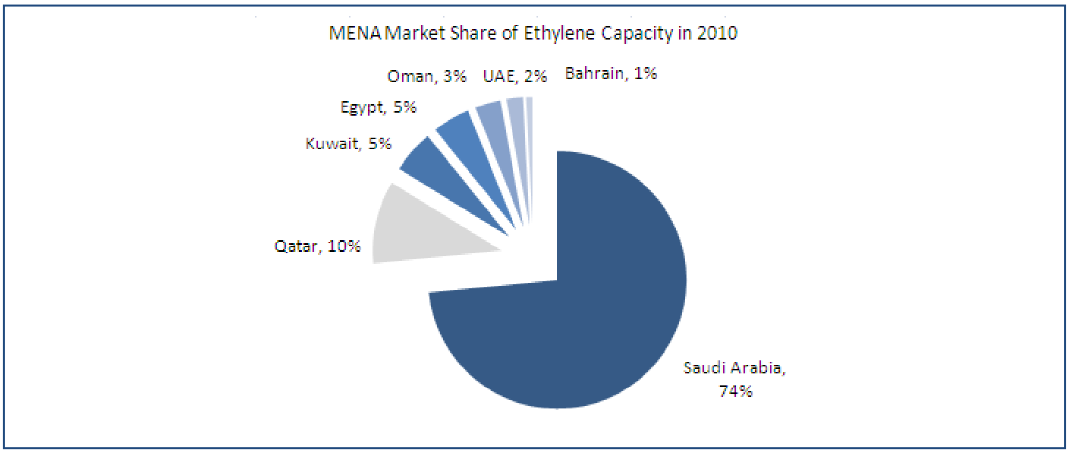
Most of the capacity expansion is expected to be from China and Saudi Arabia with the capabilities of each growing at around 20% since 2009. The Middle East exports more than 75% of its ethylene production, with Asia Pacific and China representing a major destination. Asian markets however are unlikely to absorb the additional capacity that Middle Eastern companies are planning, forcing them to diversify their exports to European and American markets in the coming years. This is likely to result in plant closures of high-cost producers in developed countries as they cannot compete with their low-cost counterparts that benefit from huge subsidies.



Source: Business Monitor International

Egypt captures 5% of ethylene production capacity in MENA

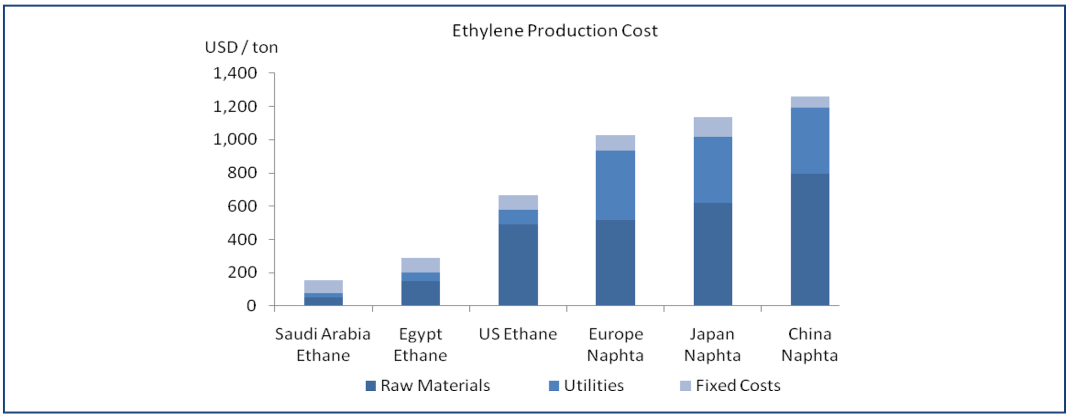
As the only ethylene producer in Egypt, Sidpec accounts for almost 5% of ethylene capacity in the region, preceded only by Saudi Arabia and Qatar. Most of the ethylene produced is transformed into polyethylene which is then either exported or used in the Egyptian market. Sidpec's priority is to serve its local market with around 60% of its polyethylene production in 2010 used to satisfy half of the local market. Imports capture the remaining half mostly from Saudi Arabia which enjoys the most competitive feedstock pricing in the world. A 5% custom tariff on imports applies which improves the competitiveness of the Egyptian producer.



Source: *Global Research*

Subsidized feedstock enables Sidpec to produce ethylene at a significant cost advantage

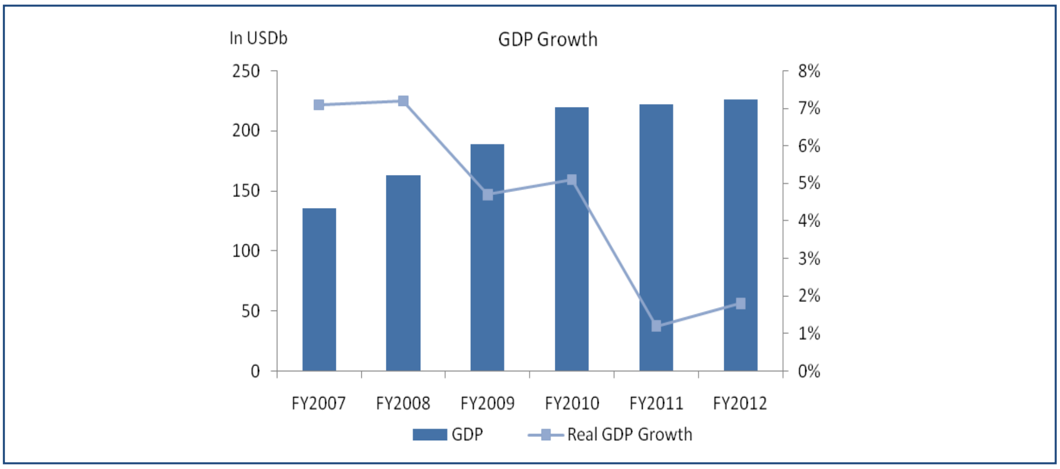
Sidpec enjoys a strong global cost advantage as it receives its feedstock at a subsidized price from the Egyptian Natural Gas Company (GASCO). The price is set according to a nondisclosed formula linking the gas cost to global ethylene and polyethylene prices. Prior to 2008, Sidpec's gas price was estimated around USD 1.25/mmbtu but was raised to around USD 3.00/mmbtu that year leading to a considerable hike in its production costs. Even with this hike however, the Egyptian producer still enjoys a significant competitive advantage over global producers with the exception of Saudi producers. We estimate its ethylene production costs at around USD 300/ton compared to USD 150/ton for Saudi producers and USD 750/ton for those in the U.S.



Source: *Bloomberg, Blominvest*

Economic growth needed to boost local demand of petrochemical products

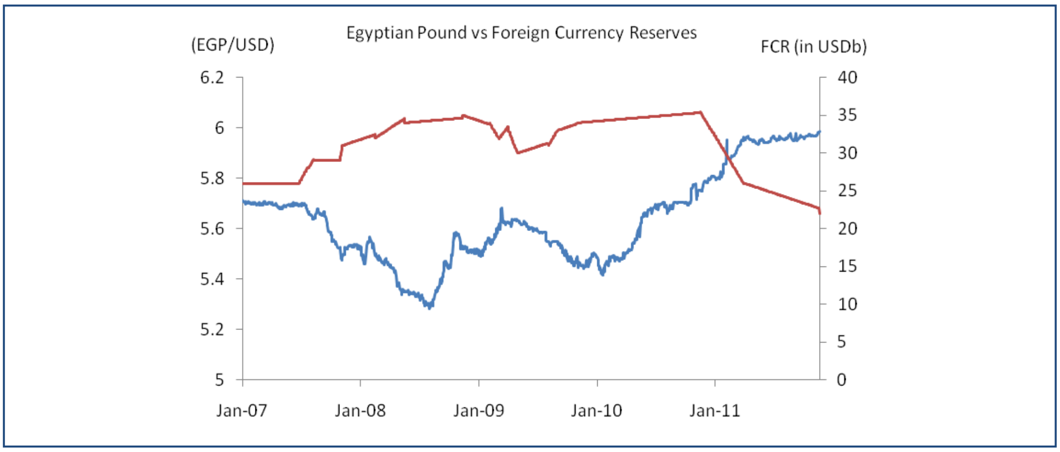
With slow economic growth and political uncertainty in the medium term, demand for petrochemicals in Egypt is expected to slow in tandem with growth in the country's GDP. The Institute of International Finance estimates real GDP to grow by 1.2% for 2011 and 1.8% for 2012. While this will not have a tangible impact on demand, however it may cause a stagnant market to remain in such a phase for quite some time.



Source: Institute of International Finance

A weak Egyptian currency induces appetite for exports

Since the beginning of the year as the situation in Egypt unfolded, the Egyptian Pound has been trading near a seven year low of EGP 6.02 / USD. This has resulted in positioning Egyptian products as attractive in markets abroad due to the depreciating currency. During 2010, Sidpec sold almost 40% of its production outside of Egypt. We estimate exports will reach a higher level during 2011 due to a considerably depreciated currency and a weak local market. We do not foresee any appreciation in the near term for the Egyptian Pound as the economy's balance of payments continues to deteriorate with ongoing depletion in the central bank's stock of foreign currency reserves.



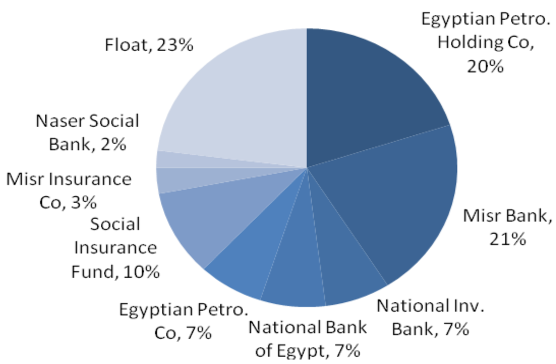
Source: Bloomberg, Central Bank of Egypt

COMPANY PROFILE

Sidi Kerir, also known as Sidpec, is Egypt's only producer of ethylene and polyethylene established in 1997 in sponsorship by the Egyptian government and under the Egyptian Investment Law. The company's production facilities are located in Alexandria with its mission to develop oil and gas-based petrochemical products to satisfy the local demand. It began its commercial operation in 2001 with a total capacity of 300,000 tons of ethylene and 225,000 tons of polyethylene. Sidpec's end-products are mainly high density polyethylene (HDPE) and low density polyethylene (LDPE) along with other secondary products that are extracted during the production of ethylene.

Ownership

Through state-owned institutions, the government indirectly owns around 77% of the company while the remaining 23% are in free float.



Source: Sidpec

Board of Directors

Ashraf Al Baqli	Chairman, Managing Director
Ahmad Abdul Mohsen	Chief Financial Officer
Nasr Abdul Halim	Member of the Board
Thuraya Abdul Hamid	Member of the Board
Mohammed Abdul Moumen	Member of the Board
Sharif Al Afandi	Member of the Board
Mahmoud Al Baroudi	Member of the Board
Khalid Al Ghazali	Member of the Board
Subhi Al Sahrawi	Member of the Board
Leyla Azzam	Member of the Board
Nahed Bassyouni	Member of the Board
Mahmoud Hamed	Member of the Board
Mustafa Hilal	Member of the Board
Mohammed Ismail	Member of the Board
Ahmad Khalil	Member of the Board
Asfour Rajab	Member of the Board

Source: Reuters

Capacity Breakdown

Product Name	Plant Capacity (kilo tons per annum)	Feedstock
Ethylene	300	Ethane/Propane
Polyethylene	225	Ethylene
Liquefied Petroleum Gas (LPG)	50	Ethylene
Butene-I	10	Gas from Ethylene Cracker

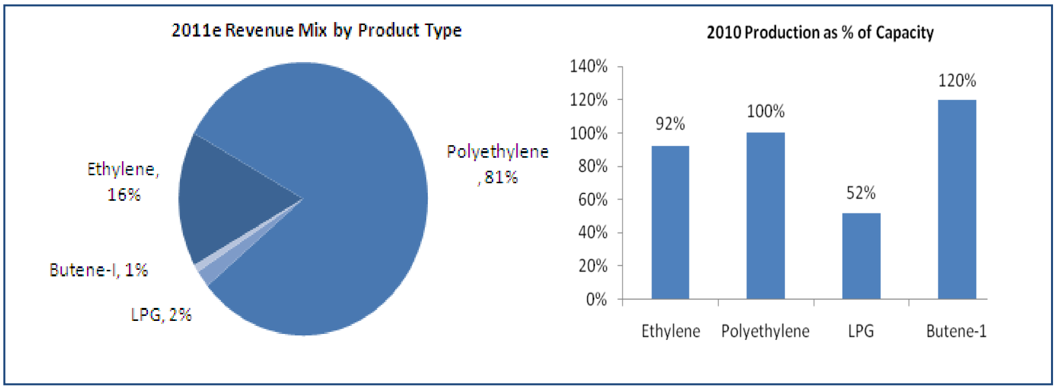
Source: Sidpec

BUSINESS MODEL

Product and Revenue Mix

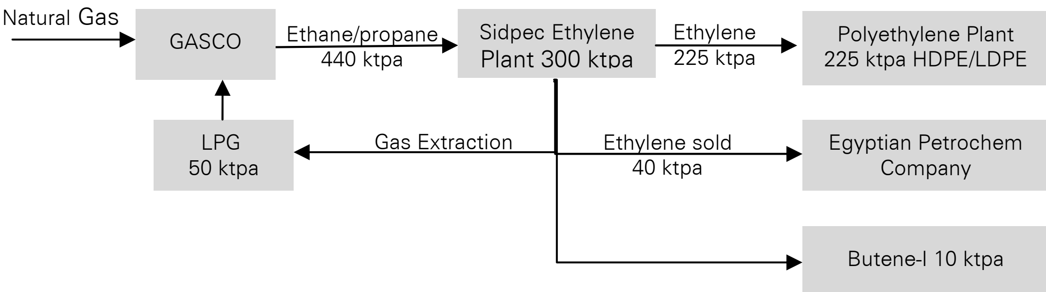
Sidpec focuses on producing two main products, ethylene and polyethylene, which constitute the majority of Sidpec's revenues. Most of the ethylene (85% in 2010) is used in the production of polyethylene while the remaining balance is sold to the Egyptian Petrochemicals Company (EPC). Sidpec specializes in creating two forms of polyethylene: High Density polyethylene (HDPE) and Linear Low Density polyethylene (LDPE). Both forms are used in the production of shopping and grocery bags while HDPE is also practically used in the production of plastic containers and boxes.

Additionally, Sidpec produces and sells two secondary products, Liquefied Petroleum Gas (LPG) and Butene-I. Most of the LPG produced is sold to GASCO, Sidpec's feedstock supplier, while Butene-I is partially sold and partially used in the production of polyethylene.



Source: BlomInvest

Production Process



Source: Sidpec

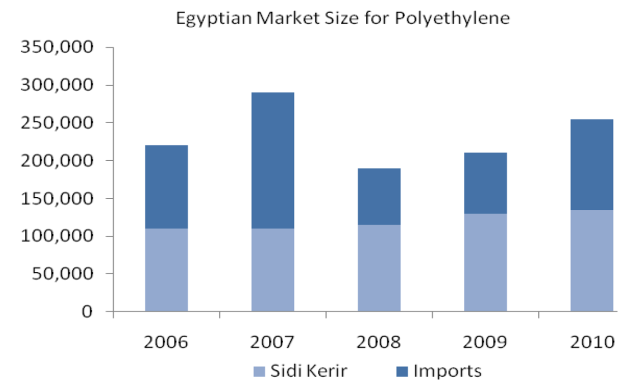
Feedstock Mix and Costs

The Egyptian Natural Gas Company (GASCO) supplies Sidpec with its feedstock needs to produce ethylene using an ethylene steam cracker. Its feedstock mix has been composed of 85% ethane and 15% propane which it receives at a subsidized price. Sidpec's feedstock price is set according to a formula that management does not disclose, linking the gas cost to global ethylene and polyethylene prices. The parameters in the pricing formula are reviewed every three years with the latest completed in 2010. We therefore do not expect any significant change in the feedstock price at least until 2013.

Prior to 2008, Sidpec's gas price was around USD 1.25/mmbtu but was raised to USD 3.00/mmbtu that year leading to a considerable hike in its production costs. Since 2008, its feedstock cost has been around 20% of polyethylene prices whereas without the subsidy, we estimate they should be around 30%. This puts Sidpec at a considerable cost advantage against global peers but at a disadvantage against Middle Eastern producers, especially Saudi companies, which enjoy an even larger subsidy.

Capacity Utilization and Expansion

Sidpec has operated at its full polyethylene capacity since 2004 producing around 225,000 ktpa. We expect the company to continue operating near its full capacity as it is the only Egyptian producer serving the local market. Egypt's polyethylene market size has somewhat fluctuated over the past few years. In 2010, it was estimated at 250,000 tons, with imports from the GCC satisfying demand over Sidpec's local sales. The Egyptian petrochemical market is unregulated and therefore prices of ethylene and polyethylene fluctuate with global prices. However, there is a 5% custom tariff on polyethylene imports which improves Sidpec's competitiveness in the Egyptian market.

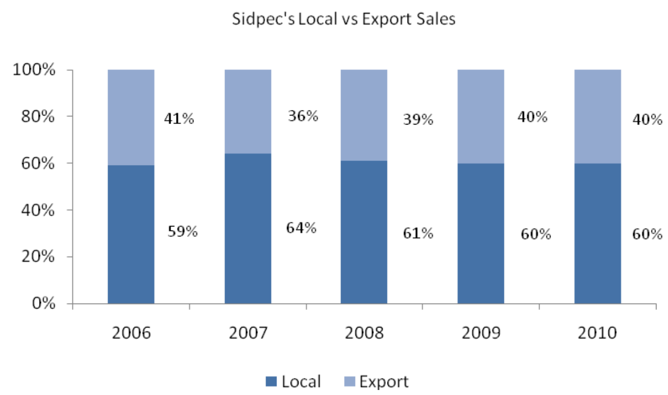


Source: CAPMAS

As for its capacity expansion plans, Sidpec has signed an agreement with GASCO, its feedstock supplier, to build a new ethylene production facility with an annual capacity of 460,000 tons of ethylene, 400,000 of polyethylene and 20,000 tons of butadiene. The company has already leased 60 acres of its unused land and raised USD 100 million as paid-in-capital to begin funding the project. Sidpec's share in the project is estimated at 20% and will therefore be treated as an equity investment.

Local Sales vs Export Sales

Historically, Sidpec's local sales have constituted around 60% of its revenues with the exception of 2009, where local sales captured almost 64% due to a slowdown in regional markets. The company's main objective continues to be satisfying polyethylene demand in Egypt, however it has been targeting external markets as a means for diversification and reducing risks attached to relying on a single market. We expect the current mix to remain around 60/40 for local/export sales unless an interruption occurs on the local or regional scene.



Source: Sidpec

RISKS

Oil shocks

With petrochemical pricing being directly linked to the price of oil, a major decline in oil prices would pose a downside to Sidpec's profitability. In our forecasts, we assumed fluctuating prices for petrochemicals with a base price of USD 90 per barrel for oil during 2011. Hence, any sudden or sharp declines in pricing will create a downside to our valuation.

Additionally, any decline in oil prices will apply pressure on Sidpec's gross margin since the feedstock pricing formula allows this margin to expand when prices increase and contract when prices decrease

Stagnant global economic recovery

In general, demand for petrochemical products relies on economic expansion as most products are used in cyclical industries such as housing and automotive. In our forecasts, we assumed a soft and gradual economic recovery over the next three years reflected in the overall demand and pricing of petrochemicals. Any further stagnation in the economic recovery of leading economies such as the United States and Europe may have a negative effect on our petrochemical pricing assumptions and our financial forecasts.

Adjustment in Sidpec's feedstock formula

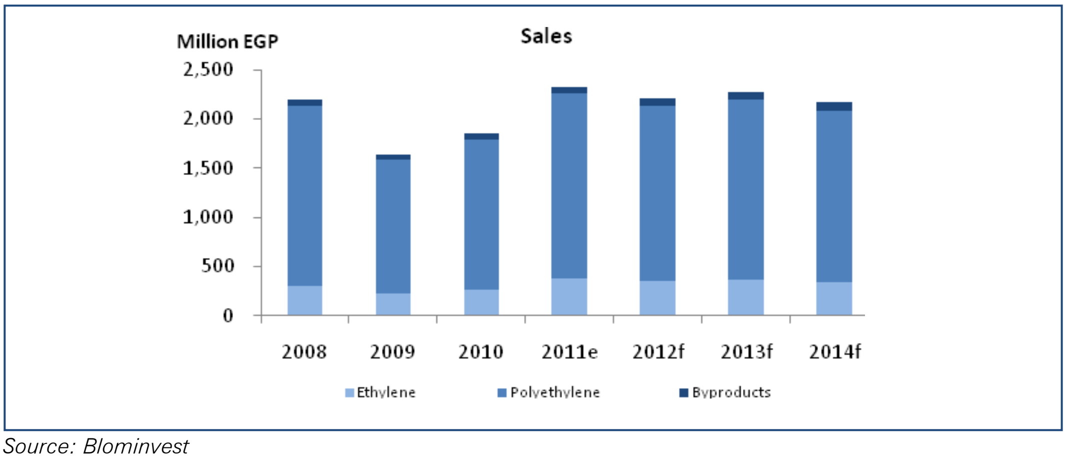
The parameters in the pricing formula through which Sidpec sources its feedstock are reviewed every three years with the latest review completed in 2010. No adjustments were made and we do not attribute any significant risk to changes in the formula until 2013. As the economic and political climate evolves in Egypt, we find that there may be likelihood that the formula will be adjusted in a way that would increase Sidpec's feedstock price yielding higher revenues for state-owned GASCO. The government has recently increased natural gas prices for energy intensive industries such as steel and fertilizers but no mention has been made in reference to the petrochemical industry.

FINANCIAL ANALYSIS

Revenues

We expect 2011's revenues to break Sidpec's 2008 record as prices for ethylene and polypropylene, which constitute more than 95% of revenues, continue to trade at considerable highs during 2011. Prices for Sidpec's core products are currently being traded at an average of USD 1,380 / ton, 25% higher than 2010 and 8% higher than 2008 which is the company's record sales year. Prices for its products move in tandem with oil prices for which we do not expect further price appreciation and therefore anticipate revenues to hover between EGP 2 billion and 2.3 billion in the near future. We estimate 2011's revenues around EGP 2.35 billion, almost 24% higher than 2010.

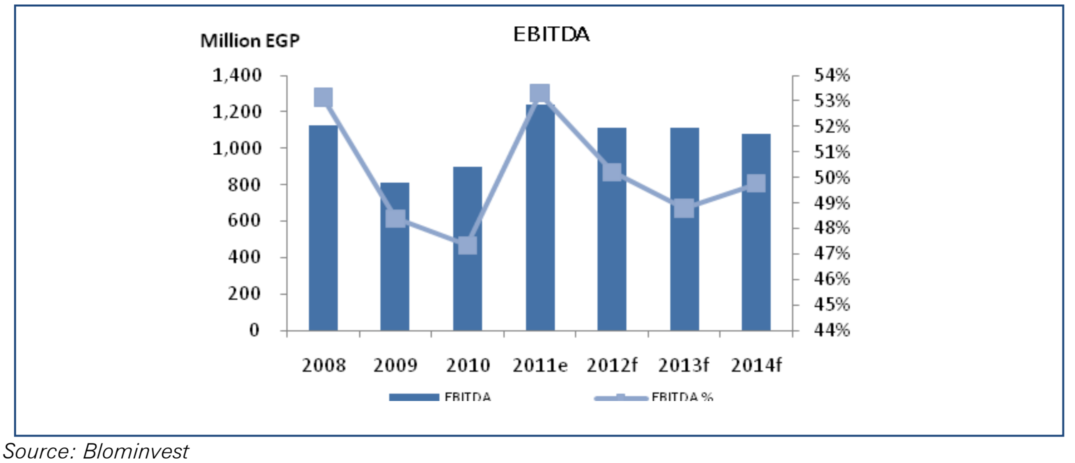
Another key factor in the revenue equation is Sidpec's production capacity in which we expect no expansion to come online before 2015. Sidpec has operated near full capacity since inception and we expect it to continue doing so due to its dominant market position as the only ethylene/polyethylene producer in Egypt.



Source: Blominvest

EBITDA

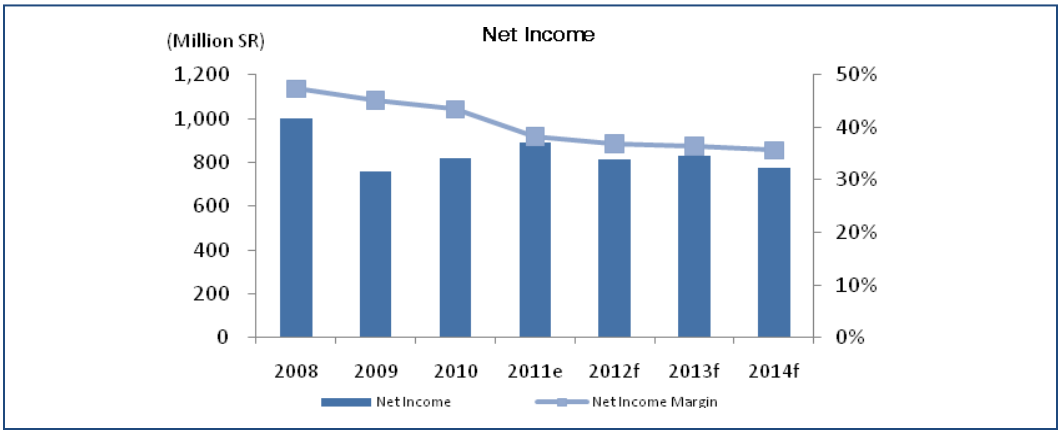
Sidpec's production costs come in two forms, feedstock that it purchases from GASCO at a subsidized price using a formula benchmarked to global ethylene prices, and other production costs which include direct labor and services associated with production. Historically, Sidpec has sourced around 440 ktpa of ethane and propane from GASCO used in the production of 275 ktpa of ethylene. As apparent in the graph below, the feedstock formula is set in a way that allows Sidpec gross margin to expand when global prices are elevated and shrink when in decline. Its EBITDA margin has reached a high of 53% in 2008 which we anticipate will be repeated in 2011. As oil prices settle or decline, we expect this margin to follow suit in the next few years.



Source: Blominvest

Earnings

Even though we expect revenues and EBITDA to grow considerably during 2011, Sidpec's net income is expected to grow more modestly due to the expiration of its corporate tax exemption. We estimate a 2011 net income of EGP 891 million, only 9% higher than 2010 with profit margin shrinking from 43.5% in 2010 to 38% in 2011. The profit margin is expected to further shrink as oil prices and EBITDA margins decline pushing it to hover around 36% in the near future. We expect profitability to remain stagnant or perhaps decline from 2011 onwards unless oil prices maintain their current levels or increase.

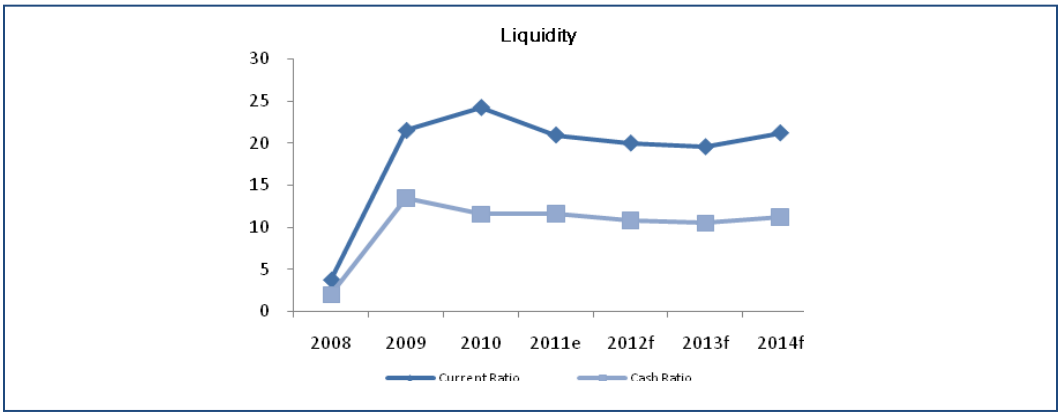


Source: Blominvest

Liquidity

Sidpec enjoys an extremely strong liquidity position with its current assets estimated at around 21x its current liabilities for 2011. The company reported EGP 650 million in cash for its first half in 2011, almost 8x its current liabilities. We expect this strong position to persist over the coming few years as no major capital expenditures are planned besides its 20% equity stake in the expansion plans with GASCO. This venture only requires another USD 14 million in the next few years which would not make a tangible dent in its liquidity position.

Current Ratio = Current Assets / Current Liabilities
Cash Ratio = Cash / Current Liabilities



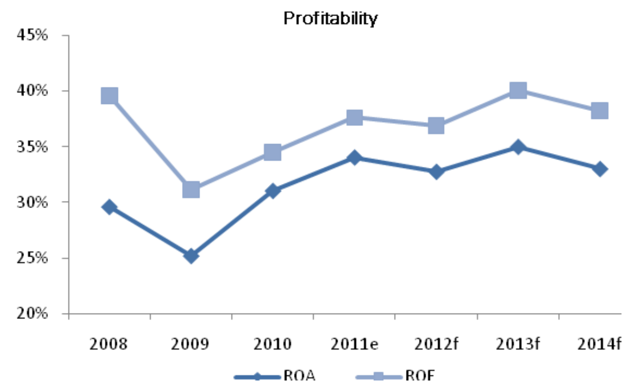
Source: Blominvest

Leverage

Leverage at Sidpec is almost non-existent with a debt to equity ratio consistently between 0% and 1%. The company has had a stable operation since its inception with strong backing from government entities and little need for any debt. Sidpec doesn't have any noticeable interest expenditures and therefore its interest coverage ratio is extremely high reaching a low of 39 in 2008. We consider companies that have a coverage ratio over 8 to be relatively safe investments.

Profitability

With no anticipated change in Sidpec's financial structure, we expect ROA and ROE to remain steady in the near future. Growth in the company's business will be neutralized by the expiration of its 10-year tax holiday where a tax rate of 25% now applies. We estimate both ROA and ROE to rise in 2011 to reach 34% and 37%, respectively. Of course, the company's profitability relies on movements in oil prices which we assume to slightly decline during 2012.



Source: Blominvest

Dividends

Since 2007, Sidpec has paid out around 90% of its earnings in the form of dividends distributed to shareholders. The company expects to continue paying dividends but we anticipate it may slightly reduce the payout ratio as it funds its 20% equity share of the capacity expansion in collaboration with GASCO.

	2007	2008	2009	2010	2011
Dividend Paid (EGP)	1.70	2.00	1.70	1.25	1.40
Average Share Price During Year	19.40	18.10	10.50	12.80	13.60
Dividend Yield (%)	8.8	11.0	16.2	9.8	10.3
EPS of previous year	1.91	2.22	1.91	1.45	1.56
Dividend Payout Ratio	89.0%	90.1%	89.0%	86.4%	89.5%

Source: Sidpec, Blominvest

COMPARABLE ANALYSIS

In order to assess the performance of Sidpec in comparison to peers, we compare it on four different fronts:

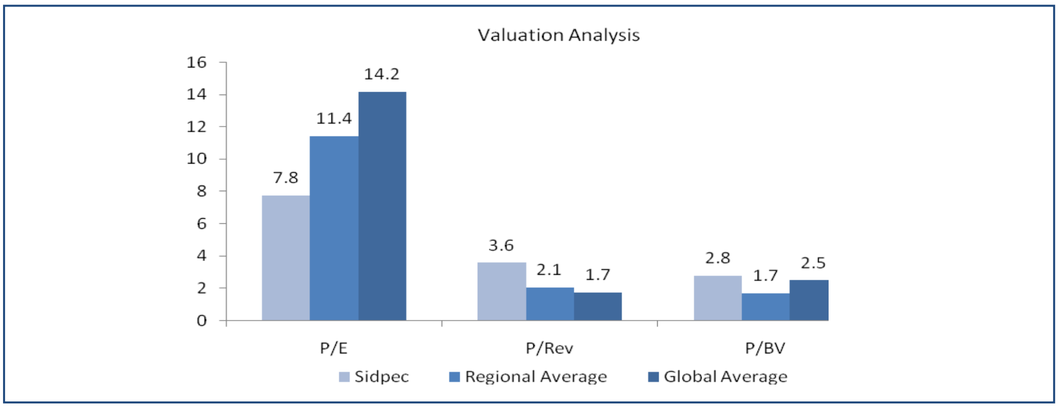
1. Relative Valuation: Shows how the market perceives the company (overvalued, undervalued, or fairly valued)
2. Profitability: Shows how well the company is managing its expenses through different margin analysis (Gross Margin, Operating Margin, Profit Margin)
3. Management Effectiveness: Shows how efficient management is at using its assets and equity to generate earnings.
4. Liquidity: Offers a glance at the company's liquidity position in comparison to peers.

Comparable Firms

We compiled a list of 15 petrochemical producers split into two groups, 11 producers represent global peers while the remaining four represent the regional average for petrochemical companies of similar size to Sidpec. The companies we selected have a market cap ranging between USD 2.4 billion and USD 600 million with an average of USD 1 billion for global peers and USD 1.7 billion for the region versus USD 1.1 billion for Sidpec.
The complete list of comparables is available in the appendix.

Relative Valuation

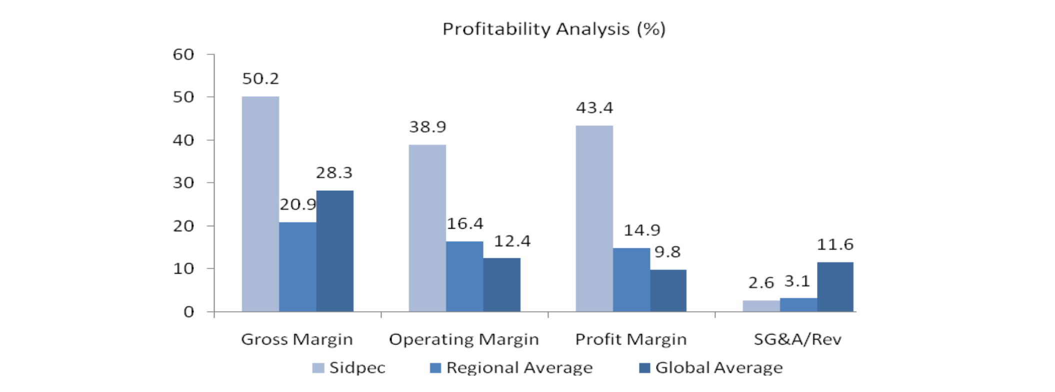
We find Sidpec's relative valuation to be attractive compared to both regional and global peers. With a price-to-earnings (P/E) of 7.8, it has the potential for appreciating at least another 30% – 40% to be on par with the average. We attribute this discount it currently trades at to the political situation in Egypt where the company generates around 60% of its revenues. Challenges on structuring Egypt's democracy persist and with the long-awaited elections closing in, we would recommend a wait and see approach unless an investor is willing to take considerable risk. When looking at the price-to-revenue ratio (P/Rev), Sidpec appears to be significantly overvalued. However, this is explained through the company's profit margin which is almost 3x more the regional average and 4x more the global average. We can therefore conclude that it makes sense for investors to be willing to pay more for every dollar of revenue that Sidpec generates as they get to keep more of it. Finally, when looking at the price-to-book value ratio (P/BV), again the company seems to be overvalued compared to the regional average however we attribute this difference to the low leverage that Sidpec operates with. The company's debt-to-equity is close to zero compared to a 100% debt-to-equity for the average in the region. Its entire liabilities form only 10% of assets which is extremely low producing a high BV/Assets ratio and therefore a higher P/BV. If were to assume liabilities to be around 50% of assets, Sidpec's P/BV ratio would drop to around 1.4 which is 20% lower than the regional average.



Source: Blominvest

Profitability Analysis

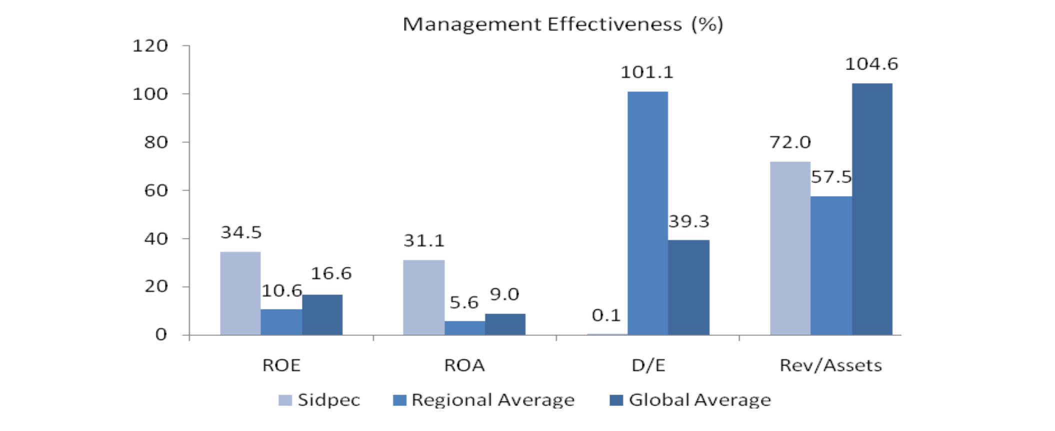
When looking at Sidpec's gross margin, it is clearly visible that it outperforms both regional and global peers. The company does enjoy competitive feedstock pricing compared to the global average however its subsidies are less than Saudi producers which have been included in our regional average. We note that in our sample of companies, leading Saudi petrochemical producers that enjoy high margins were excluded from the list due to their extremely large size, which therefore wouldn't make sense to compare with Sidpec. As for the selected companies, they produce an array of petrochemical products whereas Sidpec focuses on polyethylene, which has a higher gross margin. Of course, both operating margin and profit margin follow suit.
Selling, general and administrative (SG&A) at global producers is significantly more than the region at 11.6% of revenues. This is due to the nature of the industry where it is more capital intensive in the region along with higher labor costs in more developed countries. The profit margin at Sidpec is actually an improvement on its operating margin due to its large cash balance which earns a relatively high interest income.



Source: Blominvest

Management Effectiveness

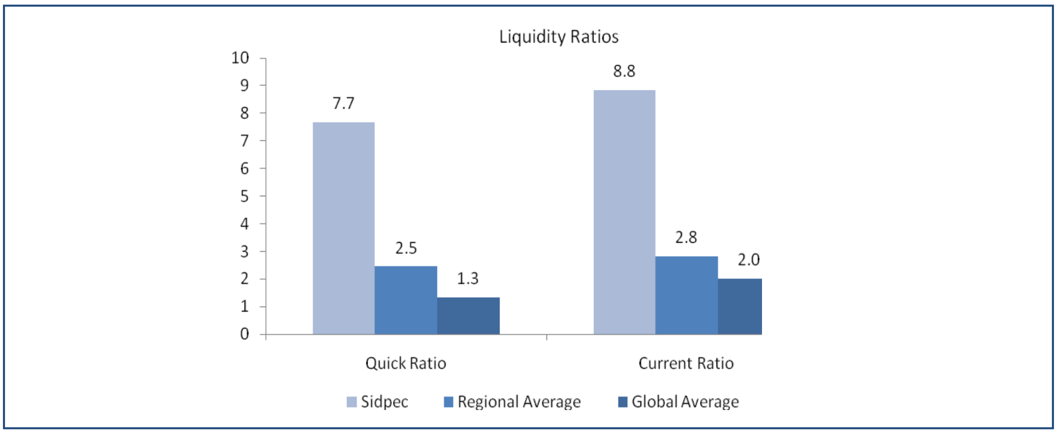
Sidpec's ROE and ROA stand at 34.5% and 31.1%, significantly higher than both the regional and global averages mostly due to a higher profit margin. The company practically has no leverage with zero debt compared to 100% for region and 40% for global competitors. Global peers outperform both Sidpec and the region when it comes to their efficiency in generating revenues from their assets. This is mostly due to the petrochemical industry in the region being more capital intensive in nature which requires a larger investment in assets.



Source: Blominvest

Liquidity

Sidpec's quick and current ratios surpass both the regional and the global averages due to its strong financial position where cash makes up almost half of all the company's current assets. We expect this to continue being the case as no significant capital expenditures or investments are anticipated.



Source: Blominvest

VALUATION

We valued Sidpec's share at EGP 13.75 using a Discounted Cash Flow (DCF) method based on a 5-year forecast with the following assumptions:

Discount Rate

We used a WACC of 15% for the purpose of valuing Sidpec's equity derived as follows:

WACC = (Weight of Equity * Cost of Equity) + (Weight of Debt * Cost of Debt) * (1 – Tax Rate)
= (0.98 * 15.17%) + (0.02 * 7.14%) * (1 – 25 %) = 14.98% rounded up to 15.00%

Sidpec Cost of Equity = Risk-Free Rate + (Beta * Market Risk Premium)
= 13.50% + (0.67 * 2.50%) = 15.17%

- We used a Risk-Free Rate of 13.50% represented by the 5-year Treasury bond recently issued by the Egyptian government. This captures the additional risk of investing in a relatively undeveloped country such as Egypt when comparing it to the U.S. Treasury, along with the risk associated with its currency.
- Sidpec's Beta over the past 5 years is estimated at 0.67. This is a measure of the share volatility against the EGX-30 Index that represents the 30 largest shares on the Egyptian Stock Exchange.
- A Market Risk Premium of 2.50% is the result of the difference between the expected return of investing in the EGX-30 estimated at 16.00% and the Risk-Free Rate of 13.50%. This represents the premium investors expect to gain for realizing the additional risk of investing in securities.

Revenue Growth

We forecasted revenues using the following assumptions:

- No additions in production capacity
- Capacity utilization rate for Ethylene at 92%. While listed capacity is 300 ktpa, actual production has been around 276 ktpa over the past few years. The company has never been able to exceed this rate due to technical bottlenecks in production.
- Capacity utilization rate for Polyethylene at 100%.
- Fluctuating petrochemical pricing as illustrated in the table below

Average Prices in USD	2011e	2012f	2013f	2014f
Ethylene price/ton	1,430	1,335	1,335	1,300
Polyethylene price/ton	1,460	1,370	1,370	1,350
LPG price/ton	300	320	320	340
Butene-I price/ton	300	320	340	340

Source: Blominvest

This resulted in revenues growing at a CAGR of 3.51% during the next 4 years.

In million USD	2011e	2012f	2013f	2014f
Revenues from Ethylene (only 37 ktpa sold)	64	60	62	59
Revenues from Polyethylene	325	308	316	301
Revenues from LPG	8	9	10	11
Revenues from Butene-I	4	4	4	4
Total Revenues	401	381	393	374
Total Revenues *(in million EGP)*	2,328	2,209	2,278	2,171
Total Revenue Growth	23.1%	-5.1%	3.1%	-4.7%

Source: Blominvest

Production and Operating Costs

Production costs have been estimated between 45% and 49% of revenues. Over the past 3 years, Sidpec's margins fluctuated between 44% and 50%. When revenues and prices increased, Sidpec's gross margin expanded; when revenues and prices decreased, the company's margin contracted. This is due to an undisclosed formula at which Sidpec's feedstock cost is calculated.

As for Selling, General and Administrative (SG&A), we have estimated them to be around 2.7% of revenues in line with the historic average. This resulted in an EBITDA margin with a high of 52% for 2011 and a low of 49% for 2013 while the rest of the years are estimated around 50%.

Determining Free Cash Flow and Share Value

From Net Income, we deduce Free Cash Flow (FCF) through the following:

In EGP Million	2011e	2012f	2013f	2014f	2015f	Terminal Year
Net Income	2,328	2,209	2,278	2,171	2,171	
Add: Depreciation	167	167	167	167	167	
Subtract: Capital Expenditures	(50)	(50)	(50)	(50)	(50)	
Subtract: Change in WC	(204)	96	(33)	(63)	22	
Add: Interest Expense	3	3	3	3	3	
FCF	804	1,025	910	824	959	
FCF Terminal						7,527
FCF Discounted	804	892	688	542	548	3,742
Fair Value	7,216					
Number of Shares (in millions)	525					
Fair Value per Share (EGP)	**13.75**					

Source: Blominvest

As for the Terminal Growth Rate, we assumed a 2% growth rate for FCF beyond 2015.

Note that we did not account for Sidpec's 20% stake in the capacity expansion project with GASCO as it is still in the early stages of implementation and the company would not be able to claim any cash flows from it in the next five years.

Sensitivity Analysis

Terminal Growth Rate	Discount Rate: 11%	13%	**15%**	17%	19%
1.0%	14.9	14.0	13.2	12.4	11.8
1.5%	15.2	14.3	13.5	12.7	12.0
2.0%	15.6	14.6	**13.8**	13.0	12.2
2.5%	15.9	15.0	14.1	13.3	12.5
3.0%	16.4	15.3	14.4	13.6	12.8

Source: Blominvest

PROJECTED INCOME STATEMENT

In EGP million	2008	2009	2010	2011e	2012f	2013f	2014f
Revenue	2,119	1,683	1,891	2,328	2,209	2,278	2,171
COGS	(939)	(820)	(950)	(1,048)	(1,038)	(1,105)	(1,031)
Selling, General & Administrative	(54)	(49)	(46)	(63)	(57)	(61)	(59)
EBITDA	1,126	814	895	1,218	1,114	1,111	1,080
Depreciation	(167)	(167)	(166)	(167)	(167)	(167)	(167)
EBIT	959	648	735	1,051	947	944	913
Interest Expense	(24)	(0.1)	(0.6)	(3)	(3)	(3)	(3)
Interest Income	67	65	44	49	43	38	49
Other Income / (Expense)	1	39	43	0	0	0	0
Net Income Before Taxes	1,003	752	821	1,096	987	979	959
Tax / Zakat	(0.3)	7	0	(208)	(178)	(157)	(192)
Net Income	1,003	759	821	888	809	823	767

Source: Sidpec, Blominvest

PROJECTED BALANCE SHEET

In EGP million	2008	2009	2010	2011e	2012f	2013f	2014f
Cash & Cash Equivalents	1,166	985	830	978	906	911	934
Current Receivables	117	227	187	210	221	205	239
Inventories	241	222	231	244	210	251	261
Due from Associates	604	113	325	300	300	300	300
Other Current Assets	47	24	168	35	35	35	35
Total Current Assets	2,175	1,572	1,742	1,767	1,672	1,702	1,768
Fixed Assets	1,145	994	844	726	632	546	474
Total Long Term Investments	57	57	61	64	67	70	74
Other Non-Current Assets	7	9	7	6	6	6	6
Total Non-Current Assets	1,209	1,061	912	796	705	623	554
Total Assets	3,385	2,633	2,653	2,563	2,376	2,324	2,321
Current Portion of Long Term Debt	5	5	2	6	5	6	5
Accounts Payable	502	40	17	33	33	35	33
Accruals Expenses	9	11	13	14	14	15	14
Due to Sister Companies & Other	72	17	39	31	31	31	31
Total Current Liabilities	588	73	72	84	84	87	83
Long Term Debt	9	4	0	11	11	12	11
Total Non-Current Liabilities	9	4	0	11	11	12	11
Total Provisions	254	218	157	170	190	210	230
Total Equity	2,534	2,338	2,424	2,297	2,092	2,016	1,997
Total Liabilities & Equity	3,385	2,633	2,653	2,563	2,376	2,324	2,321

Source: Sidpec, Blominvest

APPENDIX

I - List of Comparable Peers

Company	Country	Mkt Cap USD (m)	Relative Valuation: P/E	P/Rev	P/BV	Profitability Analysis: Gross Margin (%)	Operating Margin (%)	Profit Margin (%)	SG&A / Rev	Management Effectiveness: ROE	ROA	Rev/ Assets	D/E	Liquidity: Quick Ratio	Current Ratio
Global Peers															
Sao Martinho SA	Brazil	1,342	14.3	1.8	1.2	30.8	18.2	11.0	12.3	7.4	3.5	0.3	36.4	1.0	1.4
Enaex S.A.	Chile	1,344	17.2	3.3	3.3	30.2	22.5	18.9	7.6	20.1	11.8	0.6	49.9	1.1	1.5
Chandra Asri Petrochemical Tbk PT	Indonesia	1,021	9.1	1.8	0.3	11.8	9.0	6.7	2.8	7.2	4.0	0.6	27.8	1.4	2.1
Berger Paints India Limited	India	713	22.4	1.5	5.0	29.8	9.1	6.3	19.3	23.3	11.0	1.7	50.2	1.0	2.0
ADEKA CORPORATION	Japan	1,054	13.5	0.5	0.7	23.8	6.4	4.0	13.1	5.7	3.5	0.9	19.0	1.5	2.0
Oriental Union Chemical Corp	Taiwan	1,061	10.4	2.6	2.2	18.3	12.3	17.3	4.9	14.9	12.5	0.7	9.2	1.3	1.5
Befar Group Co.,Ltd	China	1,566	15.9	2.8	3.2	21.2	12.9	10.3	7.6	17.2	9.4	0.9	19.4	1.3	1.5
Arch Chemicals, Inc.	USA	1,200	19.0	0.9	2.7	30.9	6.8	4.7	21.4	15.2	5.3	1.1	82.7	1.6	2.2
Tikkurila Oyj	Finland	861	17.2	1.1	3.3	50.9	10.3	6.2	19.1	21.9	8.4	1.4	77.9	1.5	2.2
Neo Material Technologies Inc.	Canada	903	8.3	2.7	3.5	38.7	21.5	17.6	12.8	24.5	18.8	1.1	4.1	2.0	3.2
H&R AG	Germany	656	8.7	0.4	2.1	25.0	7.6	4.8	6.9	25.5	10.5	2.2	55.6	1.0	2.5
Global Average		**1,066**	**14.2**	**1.7**	**2.5**	**28.3**	**12.4**	**9.8**	**11.6**	**16.6**	**9.0**	**104.6**	**39.3**	**1.3**	**2.0**
Regional Peers															
Saudi Industrial Investment Group	Saudi Arabia	2,322	12.2	1.8	1.5	13.0	10.1	7.9	2.9	7.2	1.8	0.2	227.8	5.0	5.3
Saudi International Petrochemichal	Saudi Arabia	1,960	11.9	3.7	1.5	43.2	33.1	30.9	4.6	7.7	5.2	0.2	100.9	2.6	2.8
Advanced Petrochemical Co Ltd	Saudi Arabia	1,040	7.6	1.9	2.2	19.5	17.8	16.2	1.8	18.9	9.7	0.6	69.8	1.2	1.5
Petkim Petrokimya Holding A.S.	Turkey	1,388	14.0	0.8	1.5	7.9	4.7	4.5	3.2	8.5	5.8	1.3	6.0	1.0	1.6
Regional Average		**1,678**	**11.4**	**2.1**	**1.7**	**20.9**	**16.4**	**14.9**	**3.1**	**10.6**	**5.6**	**57.5**	**101.1**	**2.5**	**2.8**
Sidi Kerir Petrochemicals Co.	**Egypt**	**1,133**	**7.8**	**3.6**	**2.8**	**50.2**	**38.9**	**43.4**	**2.6**	**34.5**	**31.1**	**72.0**	**0.1**	**7.7**	**8.8**

Source: Thomson Reuters, Blominvest

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Equity Rating Key

Buy: A recommendation with a potential return greater than 10% based on our current 12-month view of total shareholder return*.

Hold: A recommendation with a potential return between -10% and 10% based on our current 12-month view of total shareholder return.

Sell: A recommendation with a potential return of less than -10% based on our current 12-month view of total shareholder return.

* Total Shareholder Return is calculated by the potential price growth over a 12-month period along with the expected dividend yield.

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