

Eastern Province Cement Company (EPCC)

SELL
Target Price
SAR42.8

Market Data

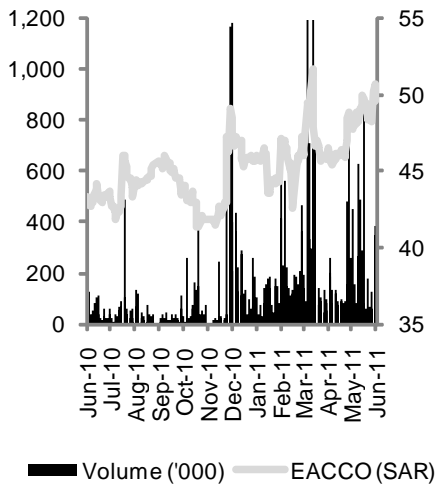
Bloomberg Code:	EACCO AB
Reuters Code:	3080.SE
CMP (15 June 2011):	SAR 49.6
O/S (mn)	86.0
Market Cap (SAR mn):	4,266
Market Cap (USD mn):	1,137
P/E 2011e (x):	12.5
P/Bv 2011e (x):	2.3

Price Performance 1-Yr

High (SAR):	51.8
Low (SAR):	41.3
Average Volume: (000)	145.3

	1m	3m	12m
Absolute (%)	3.5	15.7	22.9
Relative (%)	5.7	5.6	16.1

Price Volume Performance



Source: Zawya

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- **Net profit decrease by 10.5%YoY in 1Q11**
- **Increase in operating costs eroding margins**
- **Capacity constraints restraining growth**
- **Fair value upgraded; Recommendation unchanged**

Net profit below our forecasts

Eastern Province Cement Company 1Q11 net profit was 9.4% below our forecast and 10.5% lower than 1Q10. The net profit suffered due to 7.5%YoY increase in cost of sales on the back of higher labor and power costs. The company has the highest cost of sales per ton of SAR117.3 per ton in 1Q11 compared to our Saudi cement sector universe. The company has seen a surge in cost of sales due to operation of old lines.

The net profits also suffered due to increase in SG&A costs by 11.9%YoY in 1Q11. The SG&A costs have increased as the company is apparently being forced to sell in other areas of the Kingdom due to lower demand in the Eastern region and ban on exports.

Sales remain flat

Sales remained flat with a slight increase of 0.12% to SAR210.5mn. The decline in volumes by 2.1% to 893,000 tons was offset by increase in realization prices by 2.3% to SAR235.7 per ton. Meanwhile, the gross margins declined to 46.7% in 1Q11 compared to 50.4% in 1Q10 largely due to increase in costs despite the improvement in average realization prices.

Revision in estimates

We have increased our sales revenue forecast by 2.9% to SAR827mn for 2011 in light of improvement in average realization prices in 4Q10. However, we expect volumes to remain restricted due to capacity constraints. We have also increased our 2011 estimate of cost of sales by 2.2% due to increase in costs. Going forward, the theme of Eastern Province Cement will revolve around possible lifting of export ban. Though, the company faces capacity limitations, the lifting of export ban will help support cement realization prices and thus profitability. We have not incorporated this scenario in the model which can lead to further upward revision in fair value.

Eastern Province Cement Company 2011e

SAR mn	Earlier Estimates	Revised estimates	Change %
Revenues	803	827	2.9%
Cost of sales	(428)	(437)	2.2%
Operating Profit	337	349	3.4%
Net Profit	338	341	1.0%

Source: Global Research

Valuation update

We have upgraded our fair value by 3.4% to SAR42.8/share due to improvement in cement demand outlook. The stock has risen by 17.5% since Qatar won the 2022 World Cup bid in December 2010, which we believe is unwarranted considering the limited ability of the company to take advantage of any possible increase in exports due to capacity constraints.

Despite the upgrade in fair value, we maintain our **SELL** recommendation on the stock as our fair value is at a 13.7% discount to the current price of SAR49.6/share. The stock is also expensive on earnings multiple with its 2011e P/E of 12.5x at a premium of 6.8% to our Saudi cement sector universe 2011e P/E of 11.7x

Financial Statements

(SAR mn)	2008	2009	2010	2011e	2012e	2013e	2014e
Income Statement							
Revenue	799	779	819	827	810	798	786
Revenue growth	-13.5%	-2.5%	5.3%	0.9%	-2.0%	-1.5%	-1.5%
Cost of sales	(336)	(376)	(432)	(437)	(432)	(432)	(430)
Gross Profit	463	402	388	389	378	366	356
SG&A	(41)	(34)	(37)	(41)	(40)	(39)	(39)
Operating profit	422	368	351	349	338	327	317
Financial charges	(4)	(3)	(4)	(4)	(3)	(3)	(3)
Other income/losses	32	(1)	11	9	13	18	18
Profit Before Taxation	451	364	357	354	347	342	333
Zakat and minority interest	(17)	(14)	(14)	(13)	(12)	(12)	(12)
Net Profit	434	351	343	341	335	330	321
Net profit growth	-19.8%	-19.2%	-2.2%	-0.5%	-2.0%	-1.3%	-2.8%
Balance Sheet							
Cash and Bank Balance	253	341	401	283	234	190	140
Receivables	105	145	173	181	189	197	205
Inventories	358	337	306	351	355	361	366
Other current assets	88	32	30	32	33	35	37
Total current assets	804	855	910	847	811	782	748
Investments	471	395	386	424	467	514	565
Deferred charges	23	19	12	13	13	14	14
Net fixed assets	903	1,048	1,052	1,083	1,109	1,122	1,131
Total Fixed assets	1,397	1,461	1,450	1,520	1,589	1,649	1,710
Total Assets	2,201	2,316	2,360	2,367	2,400	2,432	2,458
Accounts payables	74	79	79	89	86	84	86
Zakat provision	17	14	14	15	16	16	17
Other current liabilities	85	85	91	48	53	57	62
Long-term debt	115	73	25	23	20	18	16
Employee end-of-service benefits	35	38	40	42	44	46	48
Share capital	860	860	860	860	860	860	860
Retained Earnings	194	-	40	79	111	138	156
Other reserves	562	910	910	910	910	910	910
Total Shareholders Equity	1,874	2,028	2,111	2,150	2,182	2,209	2,228
Total Equity & Liability	2,201	2,316	2,360	2,367	2,400	2,432	2,458
Cash Flow							
Cash Flow from Operating Activities	353	461	452	392	417	417	415
Cash Flow from Investing Activities	(171)	(70)	(91)	(159)	(163)	(157)	(162)
Cash Flow from Financing Activities	(557)	(302)	(302)	(350)	(304)	(303)	(303)
Change in Cash	(375)	88	60	(118)	(49)	(44)	(50)
Net Cash at End	253	341	401	283	234	190	140
Ratio Analysis							
Gross margin	58.0%	51.6%	47.3%	47.1%	46.6%	45.9%	45.2%
Operating profit margin	52.8%	47.3%	42.8%	42.2%	41.7%	41.0%	40.3%
Net Profit Margin	54.4%	45.0%	41.9%	41.3%	41.3%	41.4%	40.8%
Return on Average Assets	18.5%	15.5%	14.7%	14.4%	14.0%	13.7%	13.1%
Return on Average Equity	21.8%	18.0%	16.6%	16.0%	15.5%	15.0%	14.5%
EV/ton (USD)	254.7	309.1	272.0	305.4	309.0	312.1	315.8
Quick ratio (x)	2.5	2.9	3.3	3.3	3.0	2.7	2.3
Debt / Equity (x)	0.08	0.06	0.04	0.01	0.01	0.01	0.01
EV/EBITDA (x)	7.9	11.0	10.1	11.4	11.9	12.5	13.0
EV/Revenues (x)	4.2	5.2	4.4	4.8	5.0	5.1	5.3
FCF Yield	8.0%	5.9%	9.5%	6.4%	7.0%	7.2%	7.2%
EPS (SAR)	5.0	4.1	4.0	4.0	3.9	3.8	3.7
Book Value Per Share (SAR)	18.8	20.6	21.1	21.5	21.9	22.2	22.4
Market Price (SAR) *	40.0	49.8	45.3	49.6	49.6	49.6	49.6
Market Capitalization (SAR mn)	3,440	4,283	3,896	4,266	4,266	4,266	4,266
Dividend Yield	7.5%	6.0%	7.7%	7.1%	7.1%	7.1%	7.1%
P/E Ratio (x)	7.9	12.2	11.4	12.5	12.7	12.9	13.3
P/BV Ratio (x)	2.1	2.4	2.2	2.3	2.3	2.2	2.2

Source: Company Reports & Global Research

* Market price for 2011 and subsequent years as per closing prices on June 15, 2011

Disclosure

The following is a comprehensive list of disclosures which may or may not apply to all our researches. Only the relevant disclosures which apply to this particular research has been mentioned in the table below under the heading of disclosure.

Disclosure Checklist

Company	Recommendation	Bloomberg Ticker	Reuters Ticker	Price	Disclosure
Eastern Province Cement Company	SELL	EACCO AB	3080.SE	SAR 49.6	1,10

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SELL	Fair value of the stock is < -10% from the current market price

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