

August 05, 2010

LECICO (LCSW.CA)

12-Month Fair Value: EGP 16.95

Last Close (04 August, 2010): EGP 14.12

Recommendation: BUY - Risk Level: 3

- Lecico's results for 2Q2010 are a true testimony to company's ability to thrive under tough conditions. It might appear to be a subdued financial performance for the quarter but we certainly view the results as positive in the context of the situation. Overall, the results were in line with our forecasts for the quarter.
- Lecico was plagued with multiple problems: 1) the under-utilization of the sanitary ware capacity at the Borg El Arab plant due to shortage of new labour, 2) the recent fire breakout at the export factory at the Borg El Arab plant which destroyed 28% of total sanitary ware stock and 3) the continued weakness of the Euro and Sterling against the Egyptian Pound which negatively impacted export revenues. In spite of the above mentioned problems the company managed to expand its EBITDA margin to 26.3% during 2Q2010 compared to 24.9% in 2Q2009. The EBITDA margin for 2Q2010 is the highest since 1Q2006.
- The company reported total revenue of EGP 255.7 million, down 6.2% year-on-year (YoY) during 2Q2010. This was 3.5% lower than our forecast for 2Q2010. The revenue for the quarter was impacted by an 11.9% YoY drop in sanitary ware revenue. Sanitary ware volumes decreased 8.8% YoY to 1.31 million pieces during 2Q2010 whereas a 3.4% YoY decrease in sanitary ware prices to EGP 107.1 per piece made matters worse.
- Tiles revenue was up 1.8% YoY to EGP 115.8 million during 2Q2010 benefitting from a 3.6% YoY rise in tile prices to EGP 18.9 per sq. m. This increase was mainly due to a price rise in Egypt and a favourable US dollar exchange rate. Though the tile factory continued to operate above nominal capacity during the 2Q2010, sales volumes were down 1.7% YoY to 6.12 million sq. m. The company remains positive on the export tile market in Lebanon and Middle East and plans to counter the expected overcapacity in the domestic tile market by tapping new markets and expanding in their existing markets in the Middle East.
- As mentioned earlier, the company was able to report EBITDA of EGP 67.2 million during 2Q2010 compared to EGP 67.8 million in the same period last year in spite of a decline in revenue. The EBITDA was 2.3% higher than our forecast of EGP 65.7 million. The expansion in EBITDA margin was mainly due a 15% drop in selling and administrative expenses.
- Net profit for the company was negatively impacted due to a 38.5% YoY increase in taxes to EGP 7.2 million during 2Q2010. The rise in effective tax rate to 20.5% in 2Q2010 (we have assumed an effective tax rate of 22% for 2010) compared to 13.6% in 2Q2009 was due to the end of a 10-year tax holiday in one of the sanitary ware plants in Alexandria. Accordingly, net profit was down 15.2% to EGP 25.7 million in 2Q2010 compared to the same period last year.
- The company stays focused on rolling out new products and penetrating new markets for both segments. The company also plans to solve the labour shortage problem with immediate effect thus expecting to increase the overall utilization for the sanitary ware segment. Rebuilding critical stocks for the items lost in the recent fire will also be one of the key focus areas. The company plans to pass on the expected energy price from 01 July, 2010 and hence have successfully negotiated price increases with some its largest customers.
- We continue to stay positive on the company amidst all of the recent difficulties. Given the results were in line, we maintain our 2010 earnings forecast and reiterate our fair value of EGP 16.95 (upside potential of 20%) and hence our 'BUY' recommendation.

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Related Research

- Lecico Analyst Comments - 13 June 2010
- Lecico Initiation of Coverage - 09 June 2010

RISK AND RECOMMENDATION GUIDE

RECOMMENDATION		UPSIDE (DOWNSIDE) POTENTIAL		
BUY		MORE THAN 20%		
ACCUMULATE		BETWEEN 5% AND 20%		
HOLD		BETWEEN -10% AND 5%		
REDUCE		BETWEEN -25% AND -10%		
SELL		LESS THAN -25%		
RISK LEVEL				
LOW RISK			HIGH RISK	
1	2	3	4	5

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