Sector note

Egypt real estate

Real estate | Egypt

MENA research

A safe haven

- **Political turmoil did not end by 2H12 as expected; developers still face litigation risk and lack of clear regulatory framework**
- **Nevertheless, the factors at play ended up benefitting the real estate sector; pent-up real demand and fear of devaluation and inflation are the main demand drivers**
- **We stick to our stock selection criteria but change our top picks to TMG Holding and Madinet Nasr Housing**

Shaky political and economic conditions in Egypt continue to affect the real estate sector… The general consensus was that Egypt's political and economic environment would stabilize by 2H12 after a new president and parliament were elected, the cabinet was changed, and a new constitution was approved. However, the People's Assembly was dissolved, the constitution was approved by a slim majority of 64%, and the cabinet faced challenging economic and political conditions that undermined its popularity and prolonged the uncertainty. For the real estate sector, this led to a prolonged litigation overhang for most of our coverage universe (TMG, SODIC, and PHD), though promising signs of the government's desire to settle disputes between developers and the New Urban Communities Authority (NUCA) began to emerge in 1Q13 with the positive announcement regarding SODIC's Eastown land. However, the sector still faces delays in the issuance of new permits and approval of master plans.

…but benefit the sector in some respects. Due to the improved sentiment that prevailed from 4Q11 until the resurgence of political uncertainty in October 2012, the companies under our coverage experienced strong demand, backed by pent-up real demand. After October 2012, demand was driven mainly by devaluation and inflation fears, as investors view real estate as a safe haven, as well as by pent-up real demand, in our view.

We keep our stock selection criteria but switch our top picks to TMG and Madinet Nasr Housing. Despite the significant litigation overhang on TMG, we believe the stock is oversold at current price levels. Madinet Nasr Housing is not involved in any litigation and we believe it offers an attractive turnaround story and enjoys strong fundamentals. We resume coverage of Palm Hills Developments (PHD) with a Neutral rating versus our previous recommendation of Overweight from before we placed the stock under review as it is no longer oversold and is becoming increasingly risky due to its deteriorating credit profile. For over a year, rumors have been circulating that the company is an acquisition target. We downgrade our recommendation on SODIC to Neutral on decreased guidance on certain projects' margins and limited upside (17%) as the stock has rallied 32% since our last note and maintain our Neutral recommendation on Heliopolis Housing as its growth prospects remain inhibited.

TMG	Overweight
Target price (EGP)	6.4
Current price (EGP)	4.1
Potential return	57%

MNHD	Overweight
Target price (EGP)	31.3
Current price (EGP)	21.2
Potential return	47%

SODIC	Neutral
Target price (EGP)	24.6
Current price (EGP)	21.1
Potential return	17%

PHD	Neutral
Target price (EGP)	2.6
Current price (EGP)	2.3
Potential return	14%

HELI	Neutral
Target price (EGP)	24.3
Current price (EGP)	20.4
Potential return	19%

Note: All prices as of 3 March 2013

10 March 2013

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Investment case

- **We remain bullish on the real estate sector and believe it stands to benefit from current fear of devaluation and inflation; pent-up real demand still drives demand**
- **We stick to our stock selection criteria but change our top picks to TMG and Madinet Nasr Housing; TMG is oversold at current price levels, in our view, despite its strong fundamentals; Madinet Nasr Housing offers an attractive growth story, enjoys sound fundamentals, and is free of litigation**
- **We now include how efficiently companies use their land banks among our stock selection criteria, which confirms our view of the companies under our coverage**

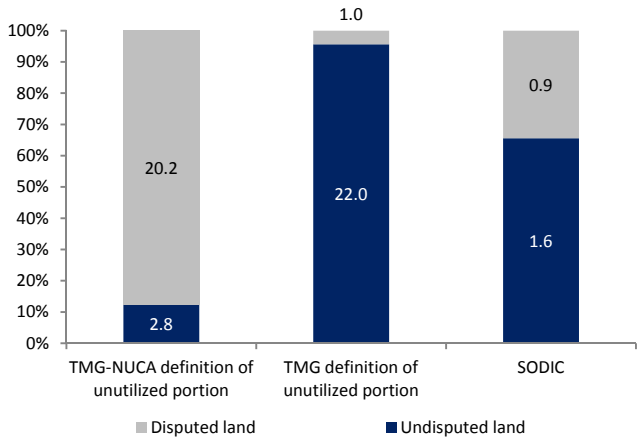
We remain bullish on the real estate sector as (1) heightening political and economic uncertainty has led to devaluation and inflation fears, which increased demand for real estate units and resulted in increased prices as investors consider real estate a safe haven, and (2) pent-up real demand continues to drive demand, especially for mid-income housing due to a supply shortage in this segment (see our exercise on real estate demand on page 15). This is why developers like SODIC have been focusing more on this segment and downsizing units recently.

We continue to favor companies with (1) exposure to the mid-income housing and primary home markets, (2) an undervalued Cairo land bank in prime locations, (3) a strong balance sheet with no funding gap expected for 2013e, (4) low or nonexistent litigation risk, (5) minimal delay in project execution and deliveries, and (6) the ability to generate new sales. We also add a new selection criterion: the efficiency with which companies use their land banks (see exercise on page 6). Our land model is summarized in the pyramid chart on the next page. We divide land into 6 categories, with developed urban land (generally based in Cairo), which is the most prime, in our view, at the top of the pyramid and raw land allocated for second home use at the bottom. Between these 2 extremes, we place land in the remaining categories based on master plan status and location, as well as other qualitative factors such as the developer's track record.

HC land model

Source: HC

Disputed land banks in our coverage universe (m sqm)



Source: HC

We update our top picks to TMG and Madinet Nasr Housing, downgrade SODIC to Neutral, resume coverage of PHD with a Neutral rating, and maintain our rating on Heliopolis Housing

Despite factoring in TMG's litigation overhang by maintaining our 80% discount to the valuation of the company's undeveloped Madinaty land, the stock offers upside of 57%, the highest in our coverage universe. We believe that the stock is oversold at current price levels, trading at a cheap 2013e multiple (P/B of 0.3x versus historical average trading multiple of 0.6x), and that the market is not assigning any value to the company's land bank. TMG enjoys strong fundamentals and offers the most exposure to Egypt's real estate story. The sector has outperformed the EGX30 from 2012 to date, with the exception of TMG, another reason to believe that the stock is oversold and likely to rebound. We believe Madinet Nasr Housing offers an attractive turnaround story. Its fundamentals are strong, with no land litigation, a sizeable attractive Cairo land bank, full exposure to mid-income housing demand, and a solid unleveraged balance sheet (net debt/equity of 0.3%).

We resume coverage of PHD with a Neutral rating versus our previous recommendation of Overweight from before we placed the stock under review as we believe it is no longer oversold and is becoming increasingly risky due to the company's deteriorating credit profile. We downgrade SODIC to Neutral from Overweight in light of decreased guidance on the margins of certain projects and as the stock shows limited upside after rallying 32% since our last note. We believe SODIC might need to take additional debt following the announcement of a possible settlement with the NUCA on its Eastown land as (1) the terms stipulate that the company will have to develop Eastown within 3 years of the date that the NUCA extends infrastructure to the land and (2) in March 2012 SODIC made a commitment to the NUCA to develop Westown over a 3-year time frame as well, which is expected to pressure its cash flows. We maintain our Neutral recommendation on Heliopolis Housing despite increasing our TP 31% (on an upward revision of land prices) as its growth prospects remain inhibited by its inefficient management style and as the stock has rallied 27% since our last note.

Overview of recommendations

	Recommendation	Action	New TP	Old TP	Action	Change in TP
TMG	Overweight	↑	EGP6.4	EGP5.2	↑	23%
SODIC	Neutral	↓	EGP24.6	EGP25.8	↓	-5%
PHD[1]	Neutral	↓	EGP2.6	EGP2.5	↑	5%
Madinet Nasr Housing	Overweight	↔	EGP31.3	EGP31.3	↔	0%
Heliopolis Housing	Neutral	↔	EGP24.3	EGP19.0	↑	28%

Source: HC
Note: (1) Old TP, actions, and change in TP reflect our numbers for PHD before we placed it under review

Summary of our valuations and market implied land valuations for the companies under our coverage (EGP)

	TMG	MNHD	SODIC	PHD	HELI
Recommendation	**OW**	**OW**	**N**	**N**	**N**
Target price	**6.4**	**31.3**	**24.6**	**2.6**	**24.3**
Potential return	*57%*	*47%*	*17%*	*14%*	*19%*
Current stock price (A)	4.1	21.2	21.1	2.3	20.4
Less: Backlog and hotel valuation/share (as per DCF) (B)	5.1	6.9	14.1	2.4	1.5
Market implied land valuation/share (A–B)	**(1.1)**	**14.3**	**6.9**	**(0.1)**	**18.9**
HC land valuation/share (C)	1.3	24.4	7.3	0.2	23.5
Market premium (discount) to HC	*N/M*	*(41%)*	*(5%)*	*N/M*	*(20%)*
Land bank as a percentage of market cap	**-27%**	**67%**	**33%**	**-4%**	**93%**
Outstanding shares (m) (D)	2,064	115	91	1,048	111
Total HC land value (EGPm) (C×D)	2,600	2,801	660	238	2,610
Undeveloped land area (m sqm) (E)	23.0	8.9	2.5	8.6	29.7
Market implied land valuation/sqm ((A–B)×D/E)	(97)	185	250	(11)	71
HC land valuation/sqm (C×D/E)	113	314	263	28	88
Market premium (discount) to HC	*N/M*	*(41%)*	*(5%)*	*N/M*	*(20%)*
2013e NAV/share	**14**	**84**	**34**	**8**	**159**
Market implied premium (discount) to NAV	*(70%)*	*(75%)*	*(38%)*	*(71%)*	*(87%)*
TP implied premium (discount) to NAV	(53%)	(63%)	(28%)	(67%)	(85%)

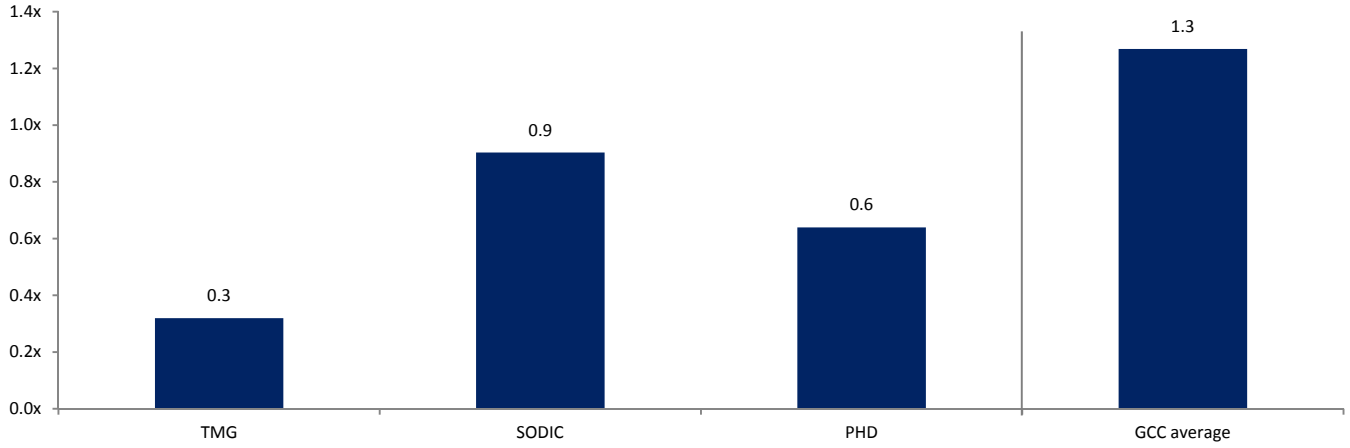
Source: HC, Bloomberg

Land valuation update

	Project	Land area (m sqm)	New value/sqm (EGP)	Old value/sqm (EGP)	Total value (EGPm)	New discount factor	Old discount factor	Value after discount (EGPm)	Value/share (EGP)
SODIC	Westown	0.39	2,000	1,500	783	60%	60%	313	3.5
	Cairo-Alex Road	1.26	250	230	315	60%	60%	126	1.4
PHD[1]	Ellamy	0.02	1,000	500	18	85%	85%	3	0.00
	Downtown VGO	0.1	1,500	500	181	85%	85%	27	0.03
MNHD[2]	KM45	5.5	500	375	2,757	80%	90%	565	4.9
	Teegan	3.2	2,000	1,500	6,408	65%	75%	2,243	19.5
HELI	New Heliopolis City	20	500	250	9,978	85%	85%	1,457	13.1
	Helio Park	7.1	500	250	3,560	85%	85%	520	4.7
	Heliopolis area	2.5	1,500	750	3,813	85%	65%	557	5.0
	Obour City	0.1	500	500	47	85%	65%	7	0.1

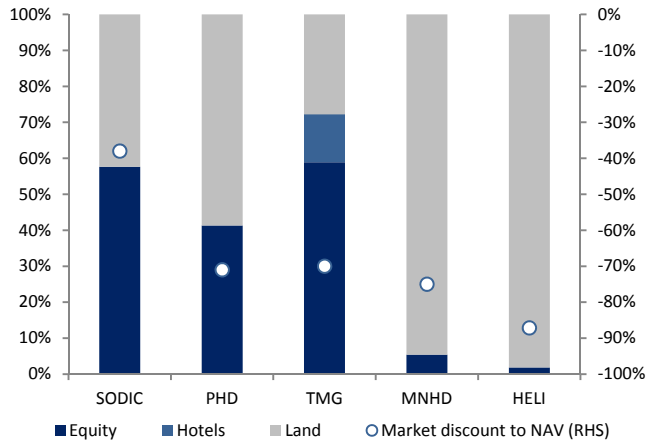
Source: HC
Note: (1) Old value/sqm and old discount factor reflect our numbers for PHD before we placed it under review (2) Reflects latest update as of 11 November 2012, Overweight, TP EGP31.3

Egypt real estate players trade at lower current P/B multiples than GCC names



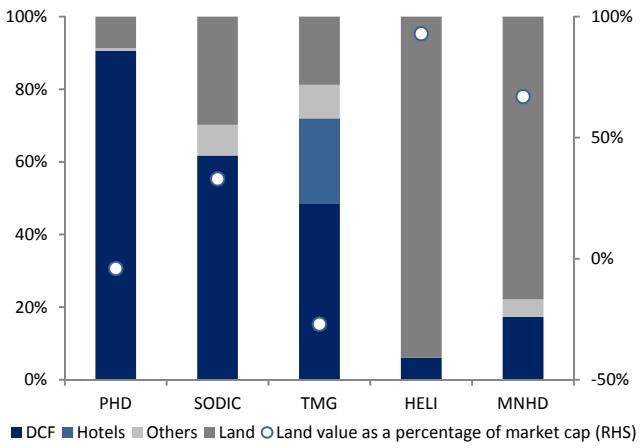
Source: Bloomberg , HC

Egyptian real estate stocks trading at deep discounts to NAV



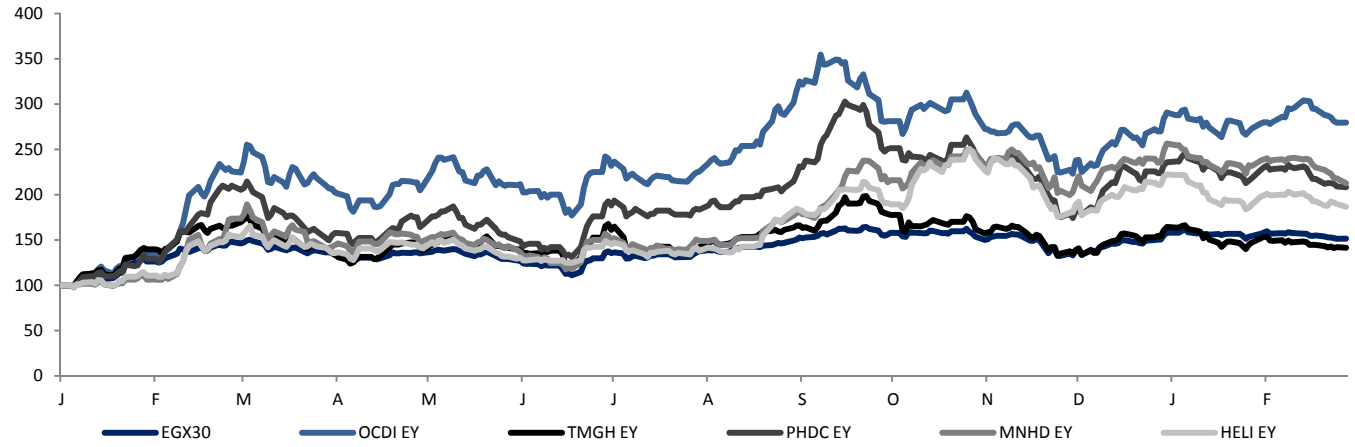
Source: HC

Valuation breakdowns for companies under our coverage



Source: HC

The real estate sector has continued to outperform the EGX30 in 2013, with the exception of TMG, another reason we believe the stock is oversold and likely to rebound

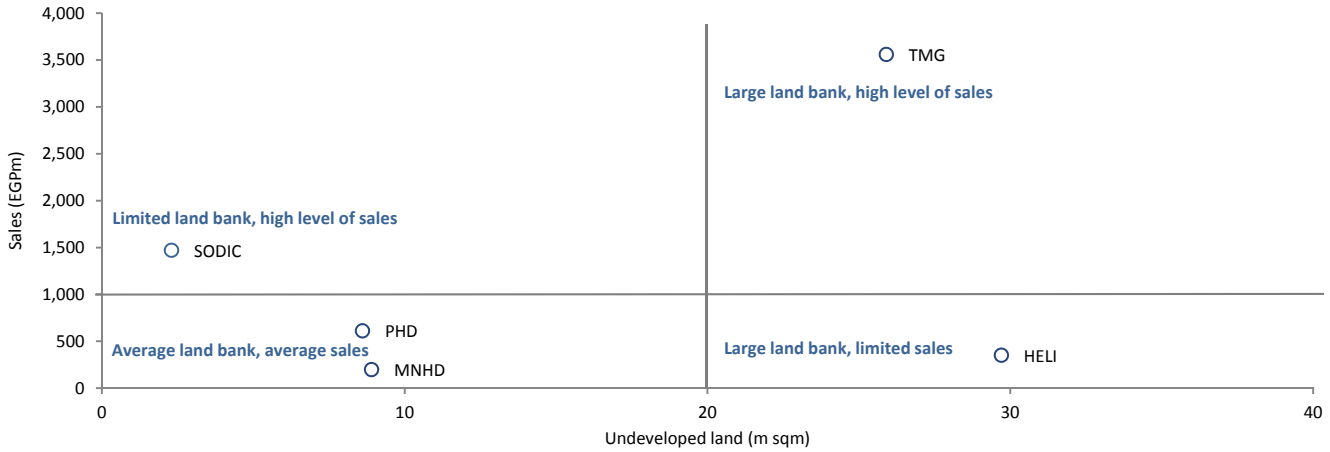


Source: HC

Our new stock selection criterion – efficiency of land bank usage – supports our view on our coverage universe

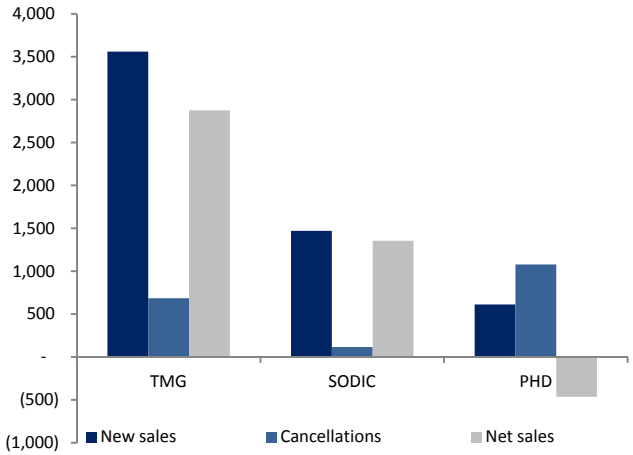
Based on an exercise in which we evaluate how efficiently companies use their land banks to generate sizeable sales, we conclude that TMG is the most efficient developer under our coverage as it generates sales in line with the size of its land bank, while the most inefficient player is Heliopolis Housing, which has the biggest land bank of our coverage universe but is unable to monetize it. Despite its limited land bank, but due to its efficient management, SODIC generates decent sales. We expect Madinet Nasr Housing to become more efficient in unlocking the value of its land bank due to its expected turnaround as the launch of Tag Sultan should bring it unprecedented levels of off-plan sales, which we expect to rise to EGP700m–EGP830m by 2013e from EGP130m in 2011, putting it in the same league as the industry's biggest players such as SODIC and PHD though still leaving it far behind TMG. PHD is unable to generate sizeable new sales that match the size of its land bank due to its operational and financial problems.

As of 9M12,TMG is the most efficient developer in our coverage universe, while Heliopolis Housing is the most inefficient



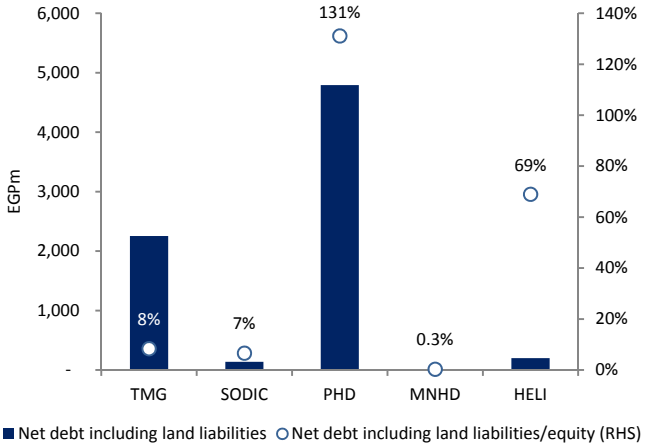
Source: HC

As of 9M12, TMG generated the highest level of sales… (EGPm)



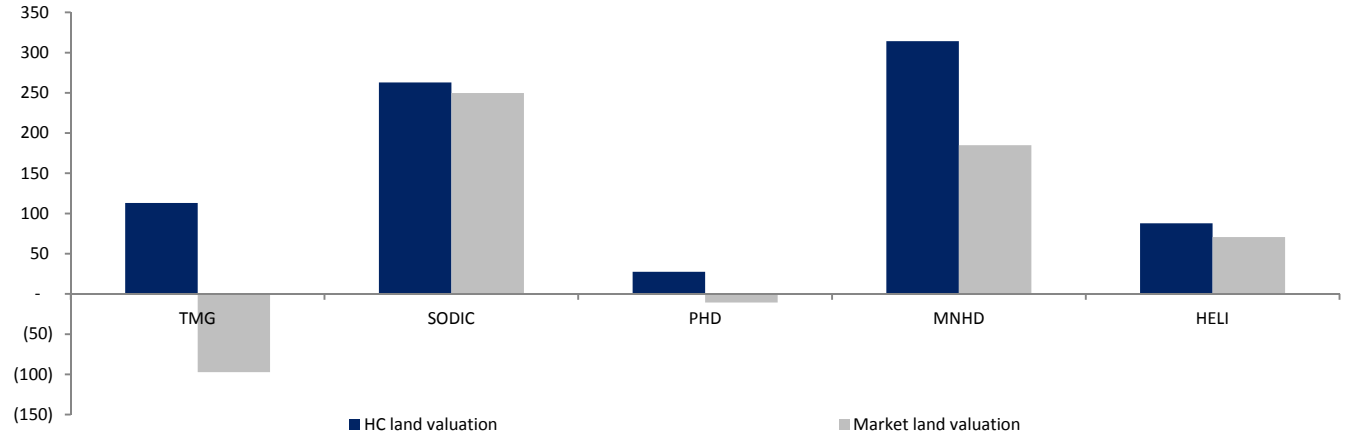
Source: HC

…and fared best in terms of balance sheet strength, along with Madinet Nast Housing and SODIC[(1)]



Source: HC
Note: (1) Net debt includes land liabilities, except for TMG, which has an in-kind land liability

Market not assigning any value to TMG's land and not much to PHD's (EGP/sqm)



Source: HC

Against all odds, recovery is in the making

- **The sector is still subject to political instability, the economic slowdown, and litigation risk as the political turmoil did not end by 2H12 as expected…**
- **…however, despite these challenges, demand for small units remains resilient, backed by pent-up real demand and fear of devaluation and inflation**
- **In light of EGP devaluation and increased energy prices, the risk of rising raw material costs is becoming real; we expect budget housing to be affected most**

Regulatory framework remains hazy despite positive signs on possible settlements between the government and developers

Despite recent attempts to set a clear framework in order to eliminate potential land litigation and attract investments into the country, regulations in the real estate market remain unclear. The NUCA recently approved a memorandum to amend some clauses of Egypt's real estate law that provide incentives to investors. The NUCA requested that the cabinet speed up the process of replacing law 89 of the year 98 (the bidding and auctioning law) with law 59 of the year 79, which stipulates that the NUCA can directly allocate land without infrastructure in 8 new cities and that, in return for investors' provision of infrastructure and development in the new cities, they will not be obliged to pay for the land until a specific period of time has passed. We see this as positive for the sector as it should clear the way for investments that were put on hold until a well-defined framework is in place. There are some discrepancies in the current land auctioning system, such as the pricing of the land being offered, which led to the cancellation of some auctions. Due to pricing disputes, the NUCA recently cancelled the auction of 326 land plots it had offered to the high-income segment earlier, and it cancelled the rest of an auction in which it sold 5 plots in Sheikh Zayed with areas of 480–900 sqm at prices of EGP3,500–EGP4,350 per sqm. The NUCA is currently studying a new law for auctioning land. We believe a reasonable option would be to offer plots at predetermined prices and to allocate the land to the bidder willing to make the highest advance payment, similar to Heliopolis Housing's land auctioning system. This would set a clear pricing strategy and would provide the government with cash inflows, which it urgently needs to fund the budget gap.

On a more positive note, the announcement of a possible settlement of the Eastown land dispute between the NUCA and SODIC sent positive signals to the market that the government is serious about resolving disputes with developers. The proposed settlement terms include a time frame for SODIC to develop the land once the NUCA provides infrastructure and the payment of a settlement equal in value to only a percentage of the difference between price at which the land was acquired and prevailing market prices, while taking into account all of the expenses the company has incurred on the plot. We see this as something new and positive for the sector that could reduce the financial burden on developers with price settlement cases, such as TMG.

Land litigations in a nutshell

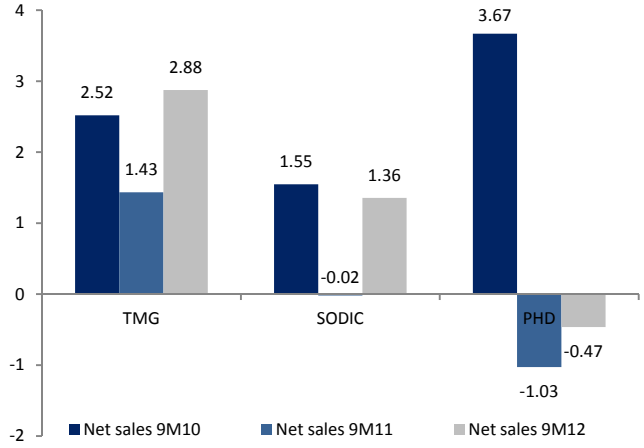
	Legal situation	Best-case scenario	Worst-case scenarios	Impact on cash flows	Impact on valuation
TMG (OW, TP EGP6.4)	In a hearing on 16 January, an Egyptian court technically accepted both TMG's appeal regarding the revaluation of the unutilized portion of its Madinaty land and Hamdy El Fakharany's appeal concerning the validity of the new Madinaty land contract. The cases will now be referred to another circuit court, with the first hearing scheduled for 16 April. The definition of 'utilized' is a point of conflict, with TMG considering the term to apply to all land to which utilities have been extended (which represents 97% of the Madinaty land), while the NUCA believes the term refers to built-up area (currently c40% of Madinaty land). Expected closure: 2H13	The court issues a ruling in favor of TMG regarding the unutilized portion of the Madinaty land while issuing another ruling against Hamdy El Fakharany.	The valuation floor for the government's 7% share of Madinaty's built-up area is raised, according to TMG's legal advisor, or a cash settlement is made by revaluing the unutilized portion of the land.	We estimate a cash outflow that represents a percentage fee applied to an amount of EGP6.1bn, based on the NUCA's definition of 'utilized,' while factoring in TMG's investments to date in the extension of utilities.	The unutilized portion of the Madinaty land contributes 19% of our valuation (EGP1.2/share). If the Madinaty dispute is resolved in TMG's favor, we will lower our land valuation discount to at least 70% from 80%, which would increase our valuation to EGP7.0/share.
SODIC (N, TP EGP24.6)	Eastown: The Conflict Resolution Committee (CRC) cancelled the NUCA's decision to revoke SODIC's Eastown land and granted the company a 3-year time frame to develop the project. The company will be required to pay a percentage of the difference between the price of the land at the time it was acquired and its current price, while taking into account all the expenses the company has incurred on the plot. SODIC's appeal of the NUCA's decision to revoke the land in the first place is still in court, with the next hearing scheduled for 6 April. SODIC has the right to appeal the fee set by the CRC in front of the State Council. Expected closure: 2013–14	Eastown: The court accepts SODIC's appeal and rules in its favor, which allows it to retain its Eastown land without paying cash settlements.	Eastown: The court rejects SODIC's appeal leaving it no option but to resort to cash settlement. A favorable agreement on the fee to be paid cannot be reached with the NUCA.	Eastown: There could be an outflow in case of a cash settlement. We estimate that the percentage fee would be applied to an amount of EGP828m–EGP1,086m.	Eastown: We value Eastown at EGP2.8/share after applying a discount of 60%. This is based on a total value of EGP634m, which includes the book value, land acquisition premium, and investments.
	Solidere International (SI): SODIC and SI filed for arbitration regarding the annulment of a contract under which SI was to develop 250,000 sqm of land in Westown after SI exercised an option to own the land. SI is requesting that SODIC pay EGP237m plus 9% interest, which represents the current value of exercising the option. Expected closure: 2014–15	SI: SODIC wins the arbitration and becomes legally entitled to the 250,000 sqm without any monetary outflow.	SI: SODIC loses the arbitration, the land is returned to the government, and SODIC pays EGP160m–EGP237m to SI.	SI: If SODIC loses the arbitration, the outflow would amount to EGP160m–EGP237m. If SODIC wins the arbitration, there will be no financial liability.	SI: This piece of land is not included in our valuation, but, in a best-case scenario, it would add EGP2.2/share, bringing our valuation to EGP26.8/share.
PHD (N, TP EGP2.6)	The withdrawal of 220 feddans in Golf Extension Phase C was resolved following reconsideration of the progress PHD had made on the land. However, its appeal of the annulment of its Katameya land contract is still in progress. Expected closure: Early 2013	PHD's appeal is accepted.	PHD's appeal is not accepted and it has to pay for the portion of the project without infrastructure, which constitutes c28,000 sqm out of a total c1m sqm, as per management's estimate.	PHD could pay a cash settlement limited to the remaining area of the land, 3% of the total area.	The impact will depend on the cash settlement, which is still unknown, with the possibility of settlement terms similar to SODIC's.

Source: HC, company data

Increased sales and successful launches confirm strong real estate demand

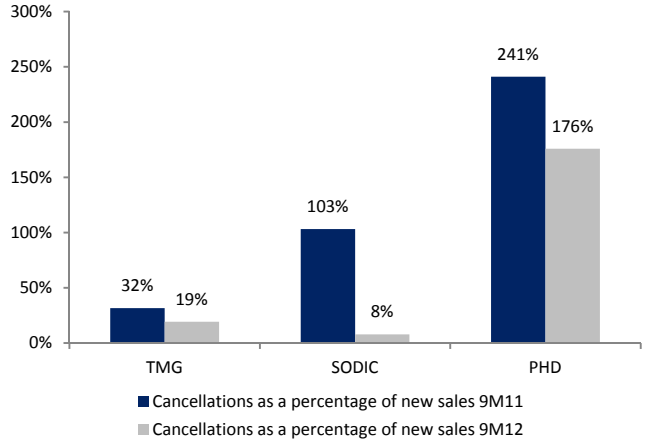
Backed up by rising real demand and decreased cancellations, net presales increased significantly y-o-y for the companies under our coverage, except for PHD as it is facing serious operating and financial problems that are hindering new sales generation. Despite TMG's litigation issues, its net presales almost doubled y-o-y in 9M12 to EGP2.8bn from EGP1.4bn, also exceeding 9M10 sales as well as 2011's net sales of EGP2bn. During the same period, SODIC achieved a positive net presales figure of EGP1.4bn versus negative net sales the year before, supported by its Westown Residences launches and missing 9M10 sales by only 12%. The 4Q12 launches of phases 1 and 2 of Tag Sultan were another success story; Madinet Nasr Housing sold 285 units with a total value of EGP200m, exceeding its 2012 sales target for the project of EGP150m. With off-plan sales of EGP0.7bn–EGP0.8bn versus a total of just EGP0.1bn in 2011, we expect Tag Sultan to put the company on the radar with big real estate developers like SODIC and PHD by 2013. These successful launches suggest that demand is rebounding to pre-revolution levels. A pickup in demand is also indicated by the fact that (1) some companies, such as SODIC, are looking to increase their land banks and (2) production volumes of construction materials, namely steel and cement, rose significantly in 1H12, though they began to decline in 3Q12 due to the heightened political uncertainty; however, we believe this dip will be short-lived.

Net presales increased significantly in 9M12, nearing pre-revolution levels (except for PHD)… (EGPbn)



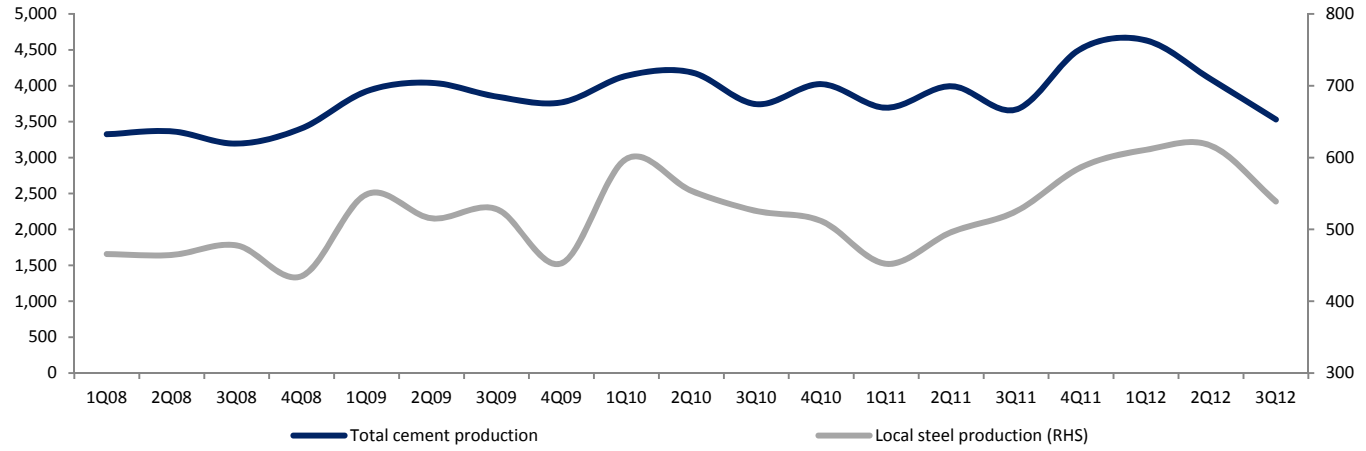
Source: HC, company data

…backed by a pickup in demand and decreased cancellation rates



Source: HC, company data

Steel and cement production peaked in 1H12, signaling strong demand; we believe the dip witnessed in 3Q12 will be short-lived (tons)



Source: Egypt's Information Portal (EIP), HC

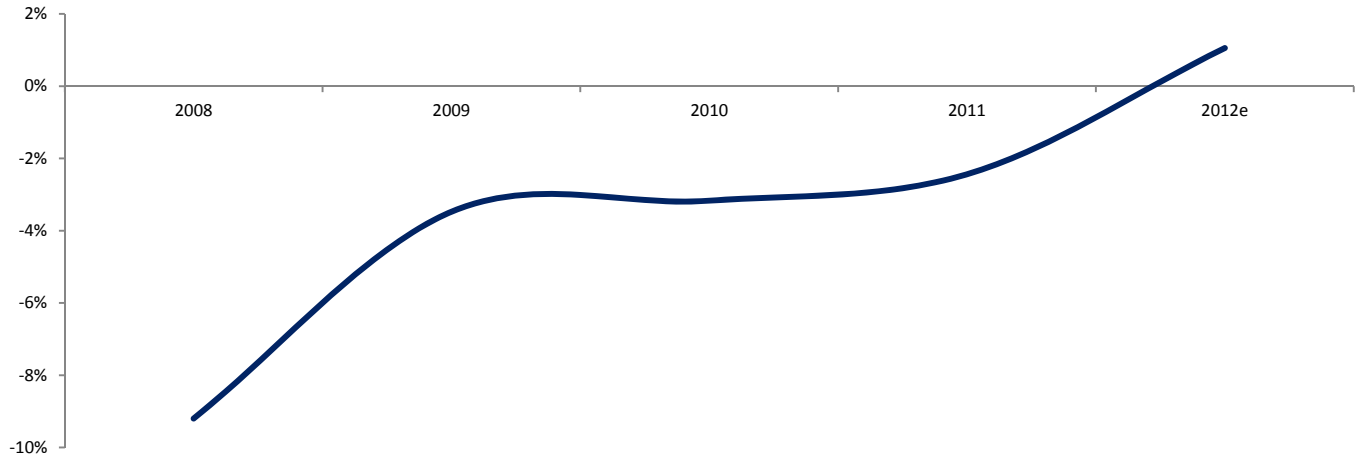
Building permits impacted by political uncertainty and litigation

Source: EIP, HC

Devaluation and inflation fears to spur further activity in the sector

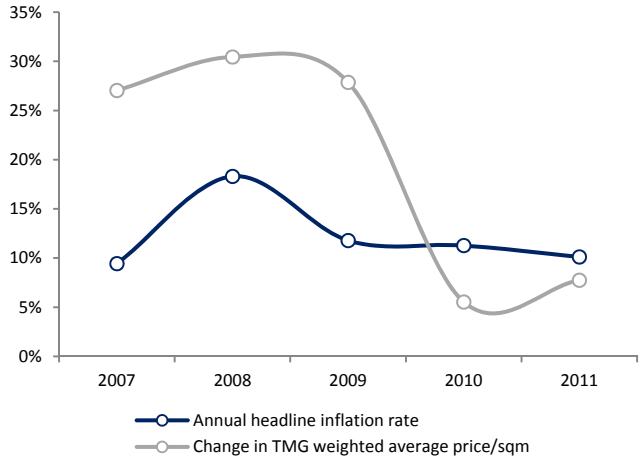
Since the revolution, real estate sales have been driven mainly by real pent-up demand. However, in light of current economic conditions including mounting fear of EGP devaluation and inflation, we expect investment in real estate to spur further activity in the sector. We believe real estate investment will be considered a safe haven for funds as that has historically proven to be the case in Egypt.

With the recent ease in inflation, the real interest rate has turned positive but is unlikely to remain that way, making investment in real estate attractive



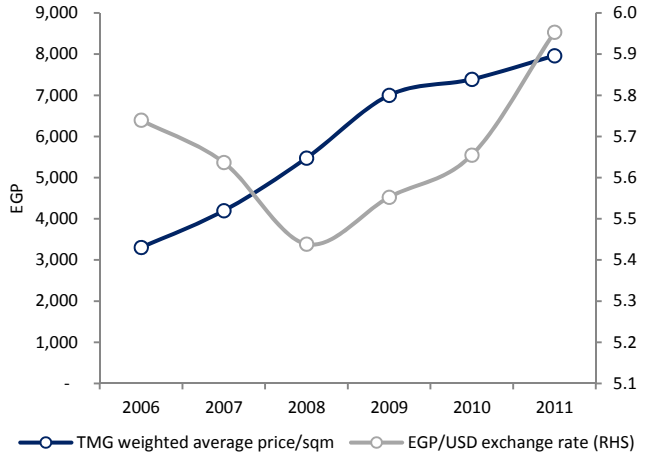
Source: Central Bank of Egypt (CBE), Colliers, Jones Lang LaSalle (JLL), HC

Real estate prices are moving in line with inflation…



Source: Bloomberg, company data, HC

…and EGP devaluation

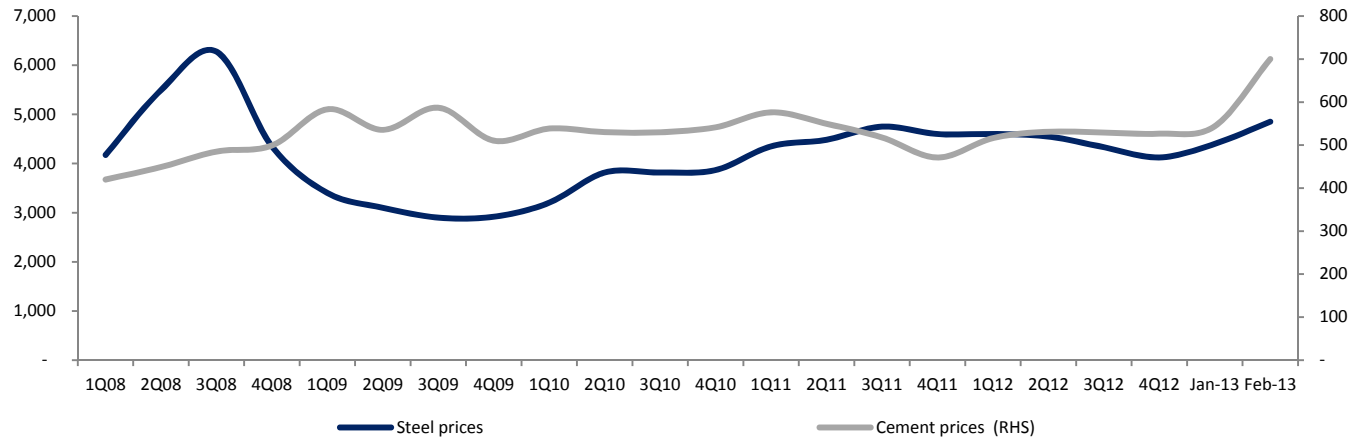


Source: Bloomberg, company data, HC

Rising raw material costs to be passed on to end customers and to affect budget housing the most

The recent hike in steel and cement prices was due mainly to (1) devaluation of the EGP and (2) an increase to USD6/mmbtu from USD4/mmbtu in the price of natural gas and heavy fuel oil for cement companies. Steel and cement make up 12%–23% of total construction costs, depending on the income segment – the proportion is higher for budget housing than for mid- and high-income housing. We believe the impact of increased raw material costs on developers' profitability will be limited as they usually pass rising costs on to consumers and as some are even hedging against the rise in steel and cement prices by including clauses in their contracts to preserve their margins by passing price hikes on to end customers. For example, Madinet Nasr Housing factors an 8% increase into its contractual agreements with customers in order to hedge against possible rises in raw material costs. It also includes a 6% price increase in its sales model as a precaution against inflation. Of the companies under our coverage, only Madinet Nasr Housing offers budget housing, but we value it conservatively at inventory value.

Prices up 10% m-o-m for steel and 29% for cement in February 2013 on EGP devaluation and rise in energy costs (EGP/ton)



Source: Central Agency for Public Mobilization and Statistics, Ezz Steel, HC

Developers financed part of their 2012 construction works through bank loans, which is unlikely to continue if rates increase further

We believe operational improvements across the sector, manifested by strong presales levels, helped banks to regain trust in developers in 2012. This was also helped by declining T-bill yields, though rates have been increasing again recently with the delays in the signing of an IMF loan agreement. In light of tight liquidity in the sector (if an IMF loan is further delayed), we believe some developers might partner with others to fund their expansions as this would allow them to minimize cash injections and capitalize on their management expertise, though it would come at a cost – we believe such a move would result in decreased margins.

Loans obtained by real estate developers in 2012 (EGPm)

	Period	Loan amount	Use of proceeds
TMG	1Q12	300	To partly finance commercial component of Madinaty
SODIC	3Q12	170	To finance Kattameya Plaza and Forty West
PHD	2Q12	240	To finance the construction of the Palm Club and a golf course
Madinet Nasr Housing	2012	100	A total of 3 facilities to finance construction works
Heliopolis Housing	2Q12	50	To finance working capital needs

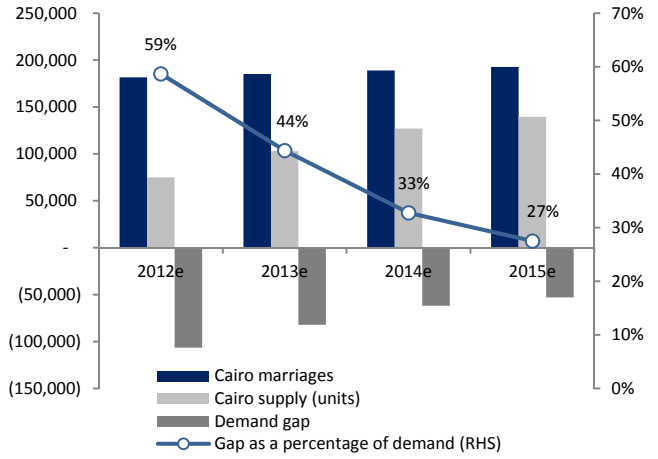
Source: Company data, HC

Demand-supply gap persisting

In line with construction delays and given the political circumstances, we expect the demand-supply gap to widen to 60% by the end of 2012e, to drop to 27% by 2015e, and to average c40% over our forecast period. We use the number of marriages in Cairo, Giza, and Sixth of October City as an indicator for demand in Greater Cairo, assuming that each marriage indicates demand for 1 unit, and increase this number 2% per year, in line with the population growth rate for those between 20 and 40 years of age, who account for 38% of Egypt's population. For Greater Cairo supply, we use Jones Lang LaSalle's 3Q12 estimates up until 2014e and forecast an annual growth rate of 10%, incorporating yearly deliveries from our coverage universe, which we expect to peak in 2014 and 2015 and to account for an average of 7% of supply. We expect the demand gap to narrow due to (1) the pickup in construction activity reflected in timely deliveries, (2) developers' shift in focus toward mid-income housing, where the majority of demand lies, and (3) government efforts to auction land for mid-income housing projects and to stimulate the National Housing Project. The price of apartments in New Cairo and Sixth of October City increased in 3Q12, accompanied by a slight decline in villa prices, which reflects a gradual shift in demand towards apartments. Apartment prices increased 8% q-o-q to EGP6,082/sqm in Sixth of October City and 15% to EGP7,360/sqm in New Cairo. Villa prices reversed their upward trend and declined in both cities, recording a 4% decline in blended price to EGP7,311/sqm in Sixth of October City and a 10% drop to EGP9,885/sqm in New Cairo. This suggests that mid-income housing will provide the biggest growth opportunity for developers over the coming years. Developers' moves to capitalize on mid-income housing demand include (1) the construction of more apartments than villas (Madinet Nasr Housing's Tag Sultan master plan is 90% apartments and 10% villas), (2) decreased unit sizes, and (3) more affordable payment schemes.

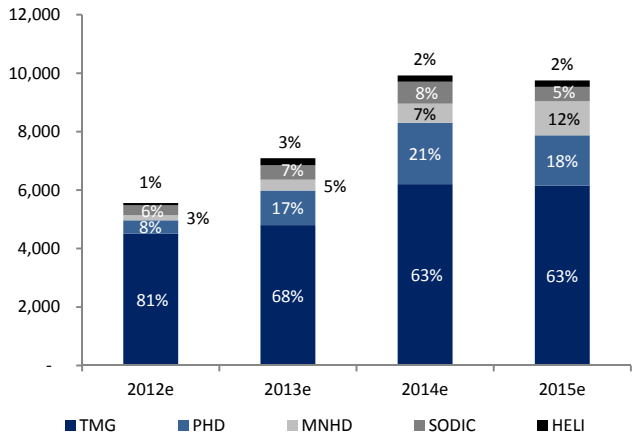
We have prepared an exercise that defines various income levels, the concentration of demand, and the supply that the companies under our coverage provide to each bracket. The results suggest that the supply provided by the developers in our coverage universe is concentrated in the upper mid- and high-income segments, while demand is mostly concentrated in the low- and mid-income brackets, which pushed the companies to shift some of their supply to cater to mid-income demand.

Cairo demand-supply gap to narrow when construction activity picks up…



Source: HC

…with deliveries expected to increase in our coverage universe, peaking in 2014e and 2015e supported by 2012 launches (units)



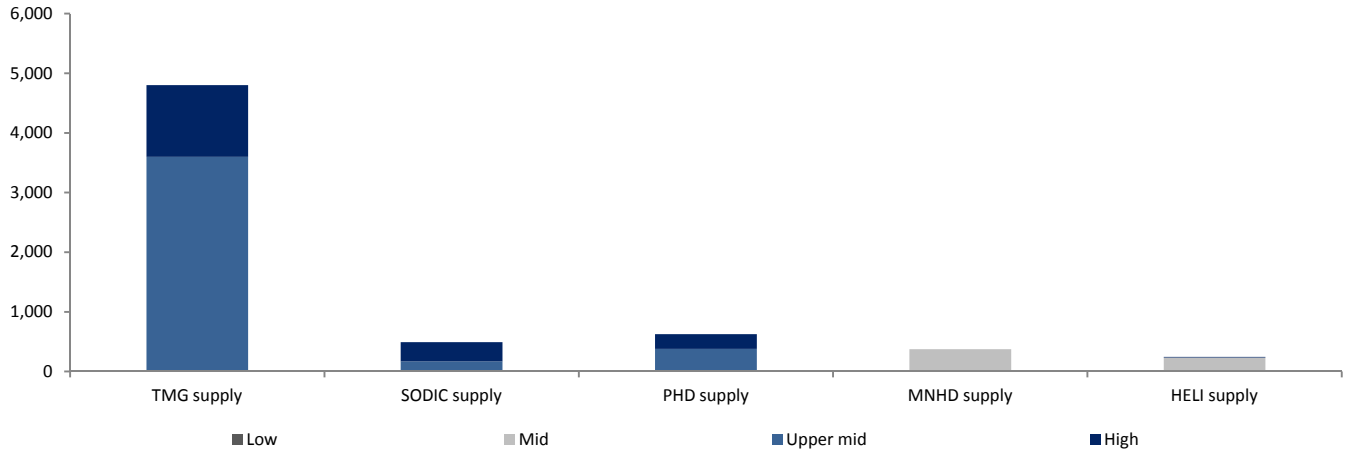
Source: HC

Definition of income levels and demand concentration (EGP)

	Low (C and D)	Mid (B and B-)	Upper mid (A and B+)	High (A+)
Annual income	Less than 50,000	50,000–150,000	150,000–350,000	More than 300,000
Monthly income	Less than 4,000	4,000–13,000	13,000–30,000	More than 30,000
Unit price	Less than 250,000	250,000–600,000	600,000–1,500,000	More than 1,500,000
% of total population	65%	23%	10%	2%
2013e supply from our coverage universe	0%	9%	63%	27%
Percentage of demand covered by 2013e supply from our coverage universe	0%	1%	22%	48%

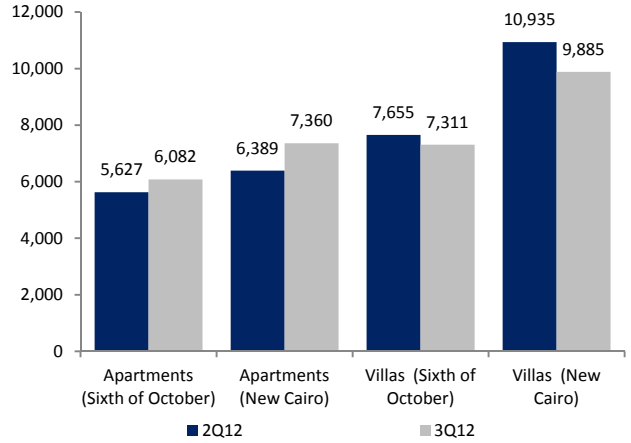
Source: IMF, Mobinil, HC

Our coverage universe's exposure to various income levels based on 2013e deliveries (units)



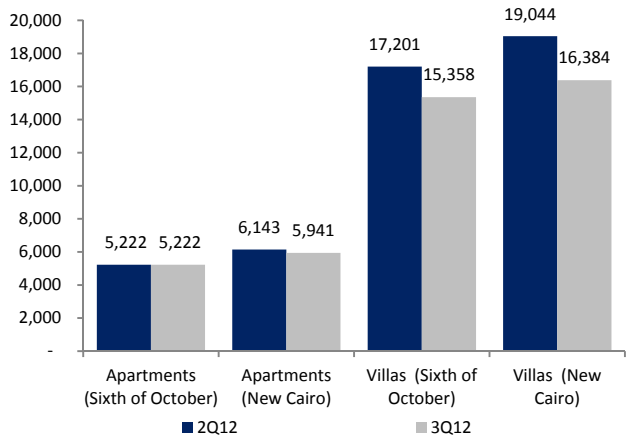
Source: Company data, HC

Shift in demand toward apartments reflected in q-o-q apartment price increases and villa price drops… (EGP/sqm)



Source: HC, JLL

…with rental rates almost stable for apartments but decreasing for villas (EGP/month)



Source: HC, JLL

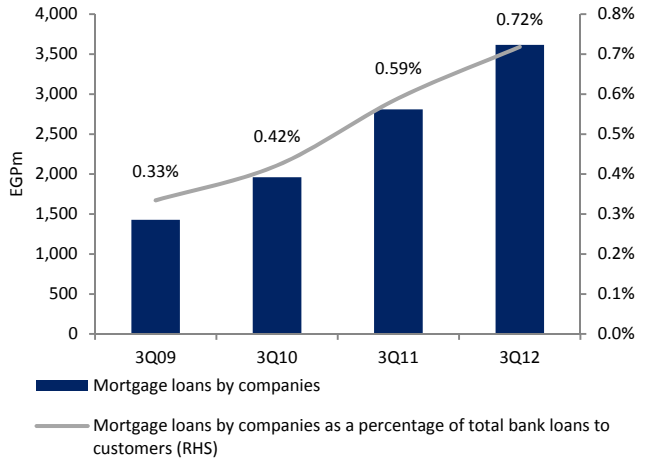
Mortgage market largely untapped; reforms expected to trigger demand in the long term

The mortgage market continues to lag significantly behind the real estate market's growth. This is demonstrated by the fact that (1) mortgage loans by companies represent only 0.72% of total bank loans to customers, (2) mortgage loans amount to less than 1% of GDP versus an average of 11%–14% in the MENA region, which leaves huge growth potential, and (3) mortgage companies had lent EGP3.7bn as of 4Q12, which represents only 31% of their full capacity of cEGP12bn (9x their paid-in capital). Adding the value of mortgage loans by banks brings the total size of the mortgage market to EGP5.7bn as of 4Q12. The government aims to increase mortgage loans by EGP1bn per year to EGP7bn in 2013e.

We believe that the main factors limiting the growth of the mortgage market include (1) the high borrowing rate of 12%–16%, which results in monthly installments that are unaffordably large. In 2012, the average monthly installment reached EGP3,096, and it is therefore difficult for those most in need of mortgages to afford the payments. Interest rates are usually 4%–6% higher than the corridor lending rate of 10.25%, including a risk premium of 1%–2%. Other major obstacles include **(2) the property registration process**, which limits the use of mortgage financing and is among the issues to be tackled in the proposed mortgage reforms that are pending parliamentary approval, **(3) the lack of strict regulations regarding default**, which makes mortgage lending more risky and further increases interest rates – this has discouraged banks from extending mortgage loans and explains why mortgage loans are the smallest component of Egyptian banks' loan portfolios as opposed to constituting the bulk of loans, as is the case in developed countries – and **(4) the fact that mortgage companies and banks cannot finance units sold off plan**. The government plans to embark on a set of reforms aimed at increasing mortgage loans/GDP to 4%–5% and reducing the interest rate on mortgages to a maximum of 10.5%. If inflation decreases, we expect mortgage rates to follow suit and believe that demand for mortgage loans should be boosted significantly if their rates fall to the single digits.

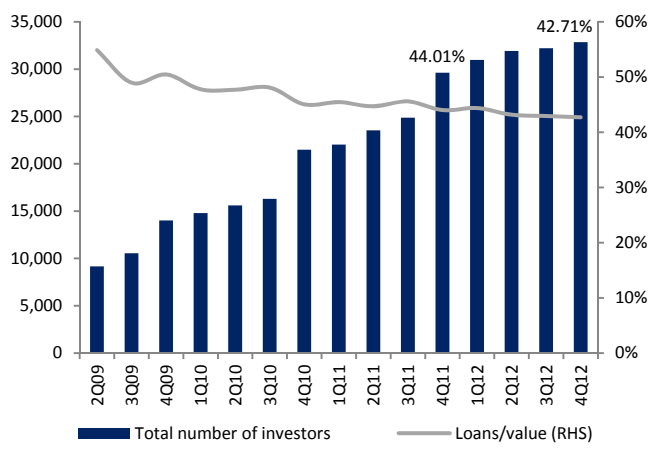
We view mortgage market development as an important but long-term catalyst for the sector (especially the low- and mid-income segments) as we expect it to take time for reforms to yield results.

Mortgage loans by companies account for a small 0.72% of total bank loans



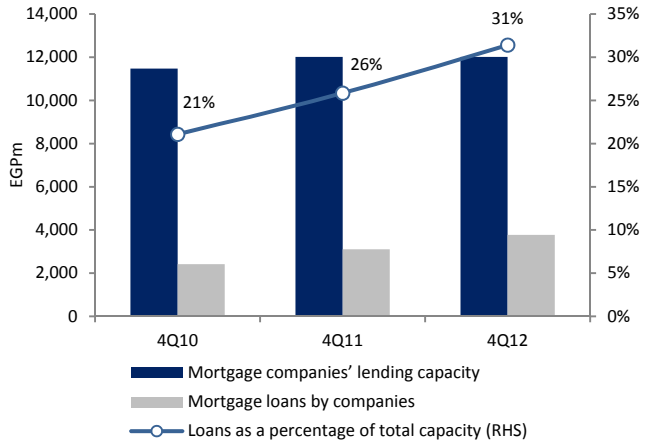
Source: Egyptian Financial Supervisory Authority (EFSA), CBE, HC

Despite an 11% y-o-y increase in mortgage lending by companies, the number of customers is still minimal at 32,863 and loans/value fell to 43% in 2012 from 44% a year earlier



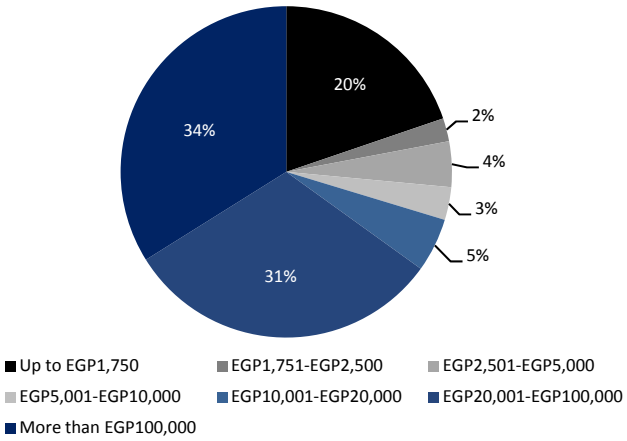
Source: EFSA, HC

Huge potential for growth as mortgage companies are lending at only 31% capacity



Source: EFSA, HC

65% of mortgage funding is going to those in the upper mid- and high-income segments, who earn more than EGP20,000 per month



Source: EFSA, HC

Property taxes have minimal effect on developers

In line with the government's recent moves to raise taxes in order to reduce the budget deficit, property taxes will go into effect starting in July following several delays but will apply only to residential units worth EGP2m or more, namely the high-income segment. The companies under our coverage universe that cater to this segment are TMG, PHD, and SODIC. However, we believe the taxes will have a minimal effect on the companies' sales levels as the effective annual tax rate amounts to less than 0.15% of a unit's market value. The tax is fixed at 10% of the tax pool, and the effective rate increases with property value.

Property taxes (EGP)

Market value	Effective value (60% of market value)	Annual rental value	Tax pool	Annual taxes paid (10% of tax pool)	Effective tax rate (annual taxes paid/market value)
2,000,000	1,200,000	36,000	1,200	120	0.01%
3,000,000	1,800,000	54,000	13,800	1,380	0.05%
4,000,000	2,400,000	72,000	26,400	2,640	0.07%
5,000,000	3,000,000	90,000	39,000	3,900	0.08%
7,000,000	4,200,000	126,000	64,200	6,420	0.09%
9,000,000	5,400,000	162,000	89,400	8,940	0.10%
11,000,000	6,600,000	198,000	114,600	11,460	0.10%
13,000,000	7,800,000	234,000	139,800	13,980	0.11%
15,000,000	9,000,000	270,000	165,000	16,500	0.11%

Source: HC

TMG: Oversold at current levels

- **Madinaty overhang continues to affect TMG, but SODIC's Eastown news is a promising sign that disputes with the NUCA could be settled at reasonable terms**
- **TMG's fundamentals remain strong; the stock is oversold at current price levels and is trading at cheap multiples, in our view**
- **We upgrade our recommendation to Overweight from Neutral and increase our TP 23% to EGP6.4/share as we decrease our risk-free rate**

Negative sentiment continues to affect TMG, with the next hearing postponed to 16 April. The court accepted Hamdy El Fakharany's appeal regarding the new Madinaty land contract and TMG's appeal on the revaluation of the unutilized portion of its Madinaty land (EGP1.2/share of our TP), prolonging the litigation overhang to 2H13. On a more positive note, following SODIC's news, we believe TMG stands a chance of reaching a reasonable cash settlement agreement with the NUCA if it loses its appeal. The amount of SODIC's cash settlement is to be calculated as a percentage of the difference between prevailing market prices and the acquisition price, factoring in its investments to date.

We like TMG's strong fundamentals and believe the stock is oversold at current price levels and that the market is not assigning any value to the company's land bank. TMG fares the best of the companies under our coverage in terms of generating sizeable off-plan sales while incurring minimal cancellations. We believe the market is penalizing TMG too much for the Madinaty litigation overhang by not assigning any value to the plot. The stock trades at a low 2013e P/B of 0.3x versus its historical average of 0.6x.

We upgrade the stock to Overweight and increase our TP 23% to EGP6.4/share (57% upside) as we lower our risk-free rate. Due to decreased T-bill rates, we reduce our WACC to 16.8% from 17.5%; this is the main factor behind our TP increase. We maintain our discount rate on the undeveloped Madinaty land bank (74% of TMG's total undeveloped land area and 96% of its undeveloped Egyptian land) at 80% to reflect the continued uncertainty surrounding the plot. We value TMG's launched projects using a DCF methodology, while projects that have yet to be launched are valued as land. We derive EGP4.6/share from existing projects and hotels, EGP1.3/share (of which Madinaty contributes 92%) from land, and EGP0.6/share from investments, including the Saudi JV. Our TP represents a discount of 52% to our 2013e NAV of EGP13.3/share.

Key multiples	2011	2012e	2013e
P/B	0.3x	0.3x	0.3x
P/NAV	0.3x	0.3x	0.3x

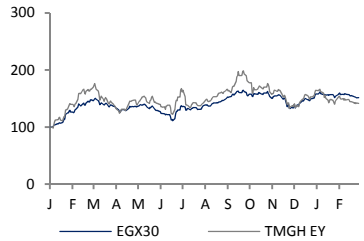
Source: HC

Overweight

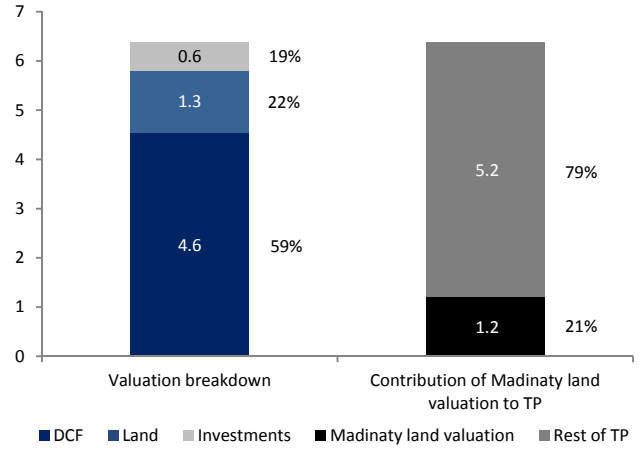
Target price (EGP)	**6.4**
Current price (EGP)	4.1
Potential return	57%
Bloomberg	TMGH EY
Reuters	TMGH.CA
Mcap (EGPm)	8,378
Mcap (USDm)	1,250
Free float	24%
Daily volume (USDm)	3.0

Note: All prices as of 3 March 2013

Price performance

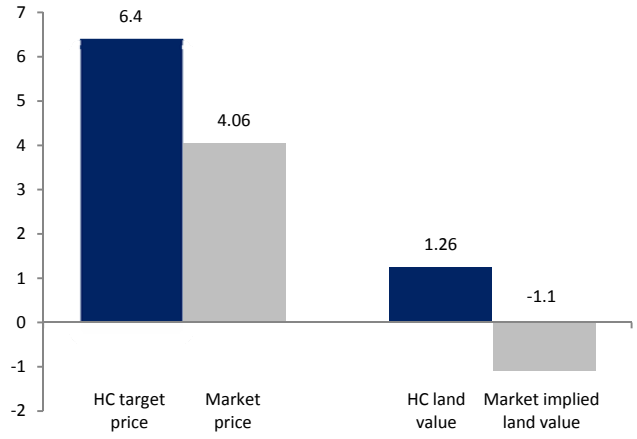


TMG valuation breakdown (EGP/share)



Source: HC

The market is not assigning any value to TMG's land (EGP/share)

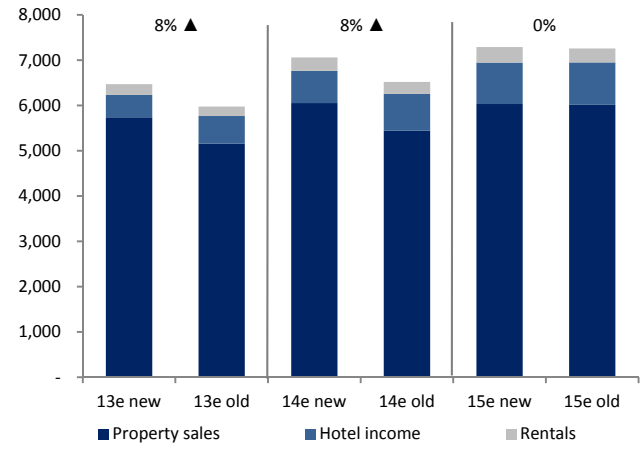


Source: HC

Deliveries pushed back, increasing 2013e and 2014e revenue estimates

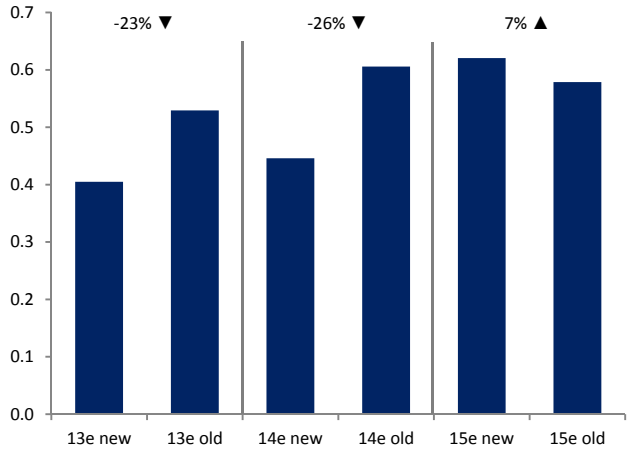
As 2012 numbers fell short of our estimates, we push deliveries back, which leads to a rise in our 2013e and 2014e revenue forecasts. However, the positive effect this has on our EPS projections is outweighed by the negative effect of decreased gross profit margins, increased net interest expenses as we add debt and account for a higher effective tax rate as the company's tax exemption for unit deliveries ended last year.

Revenue estimate revisions (EGPm)



Source: HC

EPS estimate revisions (EGP)



Source: HC

Development of the Madinaty land case

Aug 2005
- TMG's first Madinaty land contract was signed by the NUCA and Arab Company for Projects and Urban Development.

Jun 2010
- In April 2010, Hamdy El Fakharany (the original claimant) filed a lawsuit to invalidate the contract as the land was not publically auctioned. In June 2010, a court issued a ruling annulling the contract, which both the NUCA and TMG appealed.

Sep 2010
- The Supreme Administrative Court supported the lower court's ruling, officially annulled the Madinaty contract, and rejected both appeals.

Nov 2010
- A new contract was signed according to the public interest law as per a clause in the bidding and auctioning law.

Jan 2011
- The state judicial council issued a report recommending that a case filed to scrap the new Madinaty contract be rejected.

Nov 2011
- A court ruled in favor of TMG, validating the contract but demanding that the unutilized land be revalued. Hamdy El Fakharany appealed the verdict, challenging the validation of the contract, while TMG filed an appeal regarding the revaluation of the unutilized portion of the Madinaty land (3% of the land according to TMG versus c60% according to the NUCA).

Jul 2012
- The State Commissioner's Authority (SCA) released a nonbinding report invalidating the new Madinaty contract.

Nov 2012
- A hearing of the 2 appeals was held, with both sides presenting documents in response to the SCA's report. The case was postponed to 16 January.

Jan 2013
- The 2 appeals were technically accepted and referred to another circuit court, with the first hearing scheduled for 16 April.

Source: Company data, HC

Risks

Key downside risks to our forecasts and valuation include (1) a negative ruling on Madinaty, (2) higher than expected sales returns, (3) political uncertainty putting further pressure on tourism, and (4) additional construction delays.

TMG Holding financial statements and ratios (EGPm)

Year to December	2008	2009	2010	2011	2012	2013e	2014e	2015e
Income statement								
Revenue	**3,977**	**4,822**	**5,339**	**5,098**	**4,636**	**6,471**	**7,060**	**7,289**
Total costs	**(2,728)**	**(3,138)**	**(3,817)**	**(3,912)**	**(3,408)**	**(4,622)**	**(5,062)**	**(5,154)**
Gross profit	**1,249**	**1,685**	**1,522**	**1,187**	**1,228**	**1,849**	**1,998**	**2,135**
Margin	*31%*	*35%*	*29%*	*23%*	*26%*	*29%*	*28%*	*29%*
EBIT	**1,082**	**1,402**	**1,234**	**715**	**763**	**1,332**	**1,418**	**1,521**
Margin	*27%*	*29%*	*23%*	*14%*	*16%*	*21%*	*20%*	*21%*
Profit before taxes	**516**	**1,312**	**1,203**	**605**	**691**	**1,198**	**1,333**	**1,825**
Income taxes	(151)	(113)	(199)	(74)	(181)	(300)	(333)	(456)
Minority shareholder interest	(182)	(93)	64	(47)	(35)	63	79	88
Net profit (loss)	**547**	**1,106**	**940**	**578**	**546**	**836**	**920**	**1,281**
Margin	*14%*	*23%*	*18%*	*11%*	*12%*	*13%*	*13%*	*18%*
Basic EPS (EGP)	**0.3**	**0.5**	**0.5**	**0.3**	**0.3**	**0.4**	**0.4**	**0.6**
EBITDA	**1,082**	**1,402**	**1,234**	**715**	**763**	**1,460**	**1,574**	**1,697**
Margin	*27%*	*29%*	*23%*	*14%*	*16%*	*23%*	*22%*	*23%*
DPS (EGP)	**-**	**-**	**-**	**-**	**-**	**-**	**0.4**	**0.4**
Balance sheet								
Cash and cash equivalents	1,425	399	577	225	332	261	3,166	8,350
Long-term receivables	14,856	16,851	15,353	14,064	12,944	12,241	8,201	3,106
Development properties	10,306	11,718	13,800	15,183	17,221	16,678	14,740	12,051
Current assets	**34,320**	**34,053**	**33,977**	**32,948**	**33,854**	**31,917**	**28,470**	**25,375**
Noncurrent assets	**19,480**	**19,835**	**20,885**	**20,941**	**21,110**	**21,793**	**22,313**	**22,531**
Total assets	**53,800**	**53,889**	**54,863**	**53,889**	**54,964**	**53,710**	**50,783**	**47,906**
Current liabilities	**24,333**	**23,621**	**22,952**	**21,352**	**22,454**	**20,400**	**17,869**	**15,097**
Noncurrent liabilities	**5,518**	**5,439**	**6,225**	**6,236**	**6,163**	**6,063**	**5,463**	**4,863**
Minority interest in subsidiaries	1,994	1,685	1,328	1,350	958	1,021	1,100	1,188
Shareholder equity	**23,949**	**24,829**	**25,685**	**26,302**	**26,347**	**27,246**	**27,452**	**27,946**
Total liabilities and equity	**53,800**	**53,889**	**54,863**	**53,889**	**54,964**	**53,710**	**50,783**	**47,906**
Cash flow statement								
Cash flows from operating activities	**(743)**	**(485)**	**725**	**(682)**	**(97)**	**320**	**5,929**	**7,448**
Cash flows from investing activities	**(6,449)**	**(528)**	**(1,316)**	**(165)**	**(382)**	**(811)**	**(676)**	**(394)**
Cash flows from financing activities	**8,506**	**45**	**795**	**498**	**621**	**420**	**(2,348)**	**(1,869)**
Net addition (deduction) in cash	1,314	(968)	205	(349)	142	(71)	2,905	5,184
Cash at beginning of fiscal year	-	1,314	350	546	180	332	261	3,166
Net forex difference/others	-	4	(9)	(17)	(56)	-	-	-
Cash at end of fiscal year	**1,425**	**399**	**577**	**225**	**332**	**261**	**3,166**	**8,350**
Key ratios								
Revenue growth	112%	21%	11%	(5%)	(9%)	40%	9%	3%
Net profit growth	(59%)	102%	(15%)	(39%)	(6%)	53%	10%	39%
Debt/equity	8%	8%	11%	12%	14%	15%	9%	4%
Net debt	495	1,708	2,227	3,001	3,303	3,774	(731)	(7,244)
Net debt/equity	2%	7%	9%	11%	13%	14%	(3%)	(26%)
Current ratio	1.4	1.4	1.5	1.5	1.5	1.6	1.6	1.7
Average ROE		5%	4%	2%	2%	3%	3%	5%
Average ROIC		4%	3%	2%	2%	3%	3%	4%
P/B		0.4x	0.3x	0.3x	0.3x	0.3x	0.3x	0.3x
P/NAV		0.3x	0.3x	0.3x	0.3x	0.3x		
P/E		7.5x	8.7x	14.5x	15.4x	10.0x	9.1x	6.5x

Source: Company data, HC

Madinet Nasr Housing: Tag Sultan a game changer as value unlocking begins…

- **Market concerns on stalled land development relieved with launch of Tag Sultan, which puts Madinet Nasr Housing on the radar with big property developers**
- **Fundamentals are strong with no land litigation, a sizeable attractive Cairo land bank, full exposure to mid-income housing demand, and a solid unleveraged balance sheet (net debt/equity of 1%)**
- **We maintain our TP at EGP31.3/share and our Overweight rating**

In October 2012, the company launched Tag Sultan, a 0.3m sqm development targeting the upper mid-income segment, which we believe is a major breakthrough versus previous projects. In terms of target market and product offering, we see the project as comparable to SODIC's Westown Residences, which proved to be a success. Madinet Nasr Housing managed to exceed its 4Q12 off-plan Tag Sultan sales target of EGP150m, generating EGP200m of sales from the project compared with EGP130m in the whole of 2011 from all of its projects. This suggests strong client interest and paves the way for the company to achieve its 2013 off-plan sales target of EGP700m–EGP830m. We forecast a 2012–16e revenue CAGR of c38% and EPS CAGR of c41%.

Despite its small size relative to Madinet Nasr Housing's total land bank, we believe Tag Sultan's successful launch (1) alleviates investor concerns following the cancellation of the company's agreement with Orascom Development and Management, (2) proves the company's ability to develop its land bank, and (3) puts it on the radar with big real estate players. We therefore believe a high land valuation discount is no longer justified. We apply a 65%–80% discount to the company's land to arrive at a TP of EGP31.3/share.

Our TP is at a c63% discount to Madinet Nasr Housing's 2013e NAV of EGP84/share (P/NAV of 0.3x) and implies a potential return of 47%; we therefore maintain our Overweight rating. In our view, the company's c9m sqm of prime, undisputed Cairo land, coupled with its full exposure to mid-income demand and its strong unleveraged balance sheet (net debt/equity of 0.3%), makes it an attractive buy. Key downside risks include delays in the approval of Teegan's and KM45's master plans, higher than forecast land bank value erosion, changes in the regulatory framework affecting the company's land bank, and prolonged political and economic uncertainty.

Key indicators	2012e	2013e	2014e	2015e
Revenue growth	-7%	32%	86%	118%
EPS growth	30%	5%	48%	142%

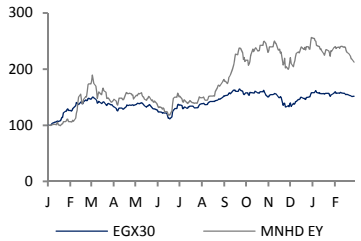
Source: Company data, HC

Overweight

Target price (EGP)	**31.3**
Current price (EGP)	21.2
Potential return	47%
Bloomberg	MNHD EY
Reuters	MNHD.CA
Mcap (EGPm)	2,443
Mcap (USDm)	365
Free float	42%
Daily volume (USDm)	0.3

Note: All prices as of 3 March 2013

Price performance



Madinet Nasr Housing stand-alone financials (EGPm)

Year to December	2009	2010	2011	2012e	2013e	2014e	2015e	2016e
Income statement								
Revenue	**139**	**125**	**186**	**173**	**228**	**424**	**924**	**926**
Total costs	**(5)**	**(9)**	**(62)**	**(40)**	**(72)**	**(180)**	**(439)**	**(431)**
Gross profit	**135**	**116**	**124**	**132**	**155**	**244**	**485**	**494**
Margin	*97%*	*93%*	*67%*	*77%*	*68%*	*58%*	*52%*	*53%*
EBIT (including revaluation gain)	**119**	**92**	**83**	**89**	**113**	**173**	**388**	**398**
Margin	*86%*	*74%*	*45%*	*52%*	*50%*	*41%*	*42%*	*43%*
Profit before taxes	**128**	**98**	**83**	**108**	**112**	**166**	**401**	**454**
Income taxes	(25)	(19)	(20)	(27)	(26)	(39)	(94)	(107)
Minority shareholder interest	-	-	-	-	-	-	-	-
Net profit (loss)	**103**	**79**	**63**	**81**	**86**	**127**	**307**	**347**
Margin	*74%*	*63%*	*34%*	*47%*	*38%*	*30%*	*33%*	*38%*
Basic EPS (EGP)	**0.9**	**0.7**	**0.6**	**0.7**	**0.7**	**1.1**	**2.7**	**3.0**
DPS (EGP)	0.9	0.9	-	-	-	-	1.1	1.4
EBITDA	**120**	**93**	**75**	**90**	**114**	**175**	**390**	**399**
Margin	*86%*	*74%*	*40%*	*52%*	*50%*	*41%*	*42%*	*43%*
Balance sheet								
Cash and cash equivalents	63	36	11	16	38	181	631	816
Receivables	453	454	530	484	359	247	148	207
Development properties	69	56	81	86	69	51	32	12
Development work in progress	65	74	67	167	355	447	171	7
Current assets	**754**	**729**	**859**	**904**	**926**	**988**	**1,020**	**1,065**
Noncurrent assets	**111**	**116**	**122**	**125**	**127**	**130**	**132**	**133**
Total assets	**865**	**845**	**981**	**1,029**	**1,053**	**1,118**	**1,152**	**1,198**
Current liabilities	**560**	**543**	**602**	**515**	**418**	**322**	**225**	**129**
Noncurrent liabilities	**33**	**11**	**9**	**84**	**108**	**143**	**97**	**52**
Minority interest in subsidiaries	-	-	-	-	-	-	-	-
Shareholder equity	**272**	**291**	**370**	**431**	**526**	**653**	**829**	**1,017**
Total liabilities and equity	**865**	**845**	**981**	**1,029**	**1,053**	**1,118**	**1,152**	**1,198**
Cash flow								
Cash flows from operating activities	**71**	**20**	**19**	**(97)**	**(14)**	**106**	**623**	**385**
Cash flows from investing activities	**(3)**	**(1)**	**(3)**	**(0)**	**2**	**2**	**3**	**6**
Cash flows from financing activities	**(126)**	**(90)**	**(8)**	**67**	**35**	**35**	**(176)**	**(205)**
Net addition (deduction) in cash	(58)	(70)	8	(30)	23	143	450	185
Cash at beginning of fiscal year	175	117	32	11	16	38	181	631
Cash at end of fiscal year	**63**	**36**	**11**	**16**	**38**	**181**	**631**	**816**
Key ratios								
Revenue growth	0%	(11%)	49%	(7%)	32%	86%	118%	0%
Net profit growth	7%	(24%)	(21%)	30%	5%	48%	142%	13%
Debt/equity	2%	1%	1%	24%	24%	25%	14%	7%
Net debt	(59)	(32)	(7)	87	89	(20)	(515)	(745)
Net debt/equity	(22%)	(11%)	(2%)	20%	17%	(3%)	(62%)	(73%)
Current ratio	1.3	1.3	1.4	1.8	2.2	3.1	4.5	8.3
Average ROE	36%	28%	19%	20%	18%	22%	41%	38%
Average ROIC	36%	28%	19%	18%	15%	18%	36%	35%
P/B	10.1x	9.4x	7.4x	6.4x	5.2x	4.2x	3.3x	2.7x
P/NAV				0.3x	0.3x	0.3x		
P/E	25.4x	34.8x	40.1x	33.8x	32.1x	21.7x	9.0x	7.9x
Dividend yield	4%	4%	0%	0%	0%	0%	5%	6%

Source: Company data, HC

SODIC: Land is key

- **The CRC cancelled the NUCA's decision to revoke SODIC's Eastown land and granted the company 3 years to develop the project, while asking it to pay a cash settlement**
- **Strong sales, project execution, and fundamentals already factored into current market price; land replenishment remains a concern**
- **We downgrade SODIC to Neutral and lower our TP 5% to EGP24.6/share as we exclude bulk land sales and decrease margins on guidance**

The CRC's decision significantly alleviates the litigation overhang, relieves concerns on land replenishment, and further secures backlog for the coming 3–5 years, pressuring cash flows, however. SODIC has been asked to pay a percentage of the difference between the price of the land at the time of it was allocated and its current price, while taking into account all the expenses the company has incurred on the plot; we see this as something new and positive for the company and the sector. We estimate the amount to which the percentage fee will be applied at EGP828m–EGP1,086m. **We now use the full value of investments incurred on Eastown, including the land acquisition premium, rather than just the book value. This adds EGP2.0/share and brings Eastown's contribution to our valuation to EGP2.8/share (after a 60% discount), which represents 11% of our TP**.

We believe the current market price factors in SODIC's resilient operational performance and robust fundamentals, with the stock outperforming the whole sector and EGX30 from the beginning of 2012 to date. SODIC recorded hefty net off-plan sales of EGP1.6bn in 2012, supported by the Westown Residences launches, and construction is progressing on track, with the first deliveries at Forty West starting ahead of schedule in December versus mid-2013.

We downgrade SODIC to Neutral and decrease our TP 5% to EGP24.6/share, mainly on the back of decreased margins as per company guidance. We also exclude bulk land sales as SODIC focuses on land replenishment. Though we reduce our after-tax risk-free rate to 11.2% on decreased 1-year T-bill rates, we raise our beta to 1.4, which yields a WACC of 19.7% (up from 18.2%) and a DCF value of EGP15.2/share. We derive EGP7.3/share from land as we adjust our numbers to match prevailing prices but maintain our land valuation discount at 60%. We value SODIC's investments in Syria at cost, which amounts to EGP2.1/share. Our TP is at a 28% discount to SODIC's 2013e NAV of EGP34/share. We see SI's plot as a potential catalyst that could add EGP2.2/share but do not include it in our TP.

Key multiples	2011	2012e	2013e
P/B	1.0x	0.9x	0.8x
P/NAV	0.7x	0.7x	0.6x

Source: Company data, HC

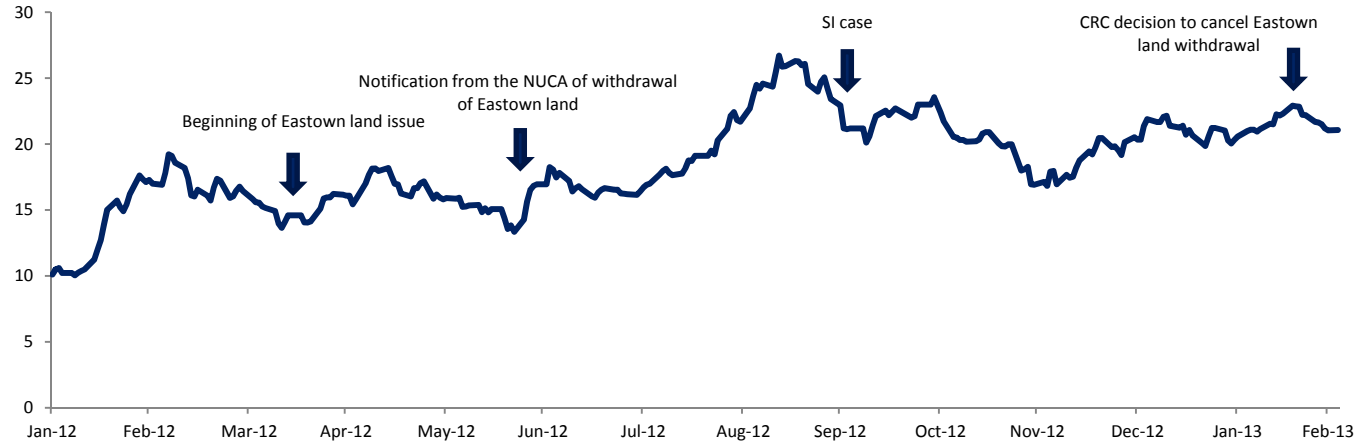
Neutral

Target price (EGP)	**24.6**
Current price (EGP)	21.1
Potential return	17%
Bloomberg	OCDI EY
Reuters	OCDI.CA
Mcap (EGPm)	1,910
Mcap (USDm)	285
Free float	57%
Daily volume (USDm)	1.1

Note: All prices as of 3 March 2013

Price performance

SODIC's share price performance has been impacted mainly by Eastown developments, yet the stock has outperformed the whole sector and EGX30, which is unlikely to be the case over the coming period



Source: HC

Positive development on Eastown could pressure cash flows

The CRC's cancellation of the NUCA's decision to revoke SODIC's Eastown land contract is more or less in line with the government's recent announcements that it seeks to settle disputes with developers that fell behind schedule by offering them the option of either returning the land or revaluing it at prevailing market prices and paying the difference. However, SODIC has been asked to pay only a percentage of the difference, while taking into account all expenses it incurred on the plot – we see this as something new and positive that could reduce the financial burden on all developers with price settlement cases. It is important to highlight that SODIC is nevertheless proceeding with its appeal, which was postponed to 6 April. This development is positive for SODIC as (1) it significantly alleviates the litigation overhang on the stock (though this will not disappear completely until such time as the company reaches a favorable agreement with the NUCA regarding the value and payment terms of the financial settlement), (2) it eases concerns related to land replenishment since Eastown's total area of c860,000 sqm represents 34% of SODIC's undeveloped land bank, and (3) it secures future backlog for the company over the coming 3–5 years.

On the other hand, we believe that, along with the financial settlement, developing Eastown over 3 years will pressure the company's cash flows as it already agreed with the NUCA in March 2012 to develop Westown on a 3-year schedule. To ease this pressure, SODIC announced that it plans to fund payments through Eastown project sales. We also believe that, in light of recent government announcements, developers' delays will be calculated starting from the date the NUCA provides infrastructure to the land; this could give SODIC some additional time before it needs to start developing Eastown. Also, SODIC has room for leverage to partly finance these obligations in light of its low 2012 net debt/equity ratio of 0.05x. We performed an exercise to find a rough estimate of the amount to which the percentage fee will be applied and arrived at a value of EGP828m–EGP1,086m.

Eastown acquisition details

Book value of land excluding premium (EGPm)	**170**
Book value/sqm excluding premium (EGP)	198
Premium paid (EGPm)	**350**
Investments incurred (EGPm)	**114**
Total acquisition cost + investments (EGPm)	**634**
All-inclusive value/sqm (EGP)	737
Estimated market price/sqm (EGP)	1,700–2,000
Estimated amount to which a percentage fee will be applied (EGPm)	**828–1,086**

Source: Company data, HC

Eastown adds EGP2.0/share to land valuation; SI could add another EGP2.2/share but is not included in our TP

In terms of valuation, we had previously included only Eastown's EGP170m book value (excluding the land acquisition premium and investments) as part of our land valuation at a 60% discount. We now include the acquisition premium and investments incurred to date and maintain our land valuation discount, which adds EGP2.0/share and brings Eastown's total contribution to our valuation to EGP2.8/share (11% of our TP of EGP24.6/share).

Positive outcome to land litigations to ease land replenishment concerns; SI could add an estimated EGP2.2/share

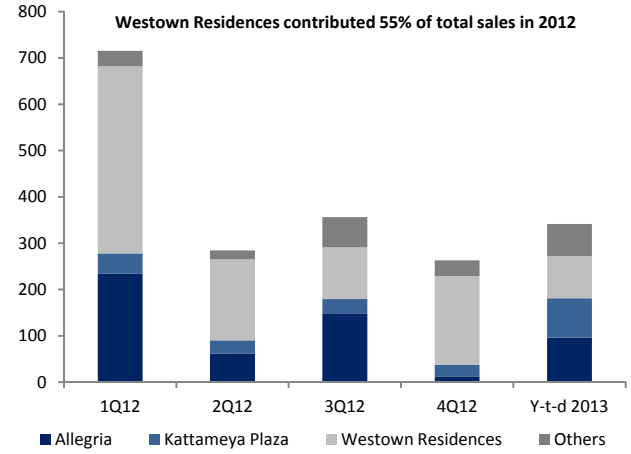
Legal situation	Best-case scenario	Worst-case scenario	Impact on cash flows	Impact on valuation
(1) Eastown				
The CRC cancelled the NUCA's decision to revoke the land contract and requested that SODIC pay a percentage of the difference between prevailing prices and the acquisition price, factoring in investment costs. SODIC is still proceeding with its appeal against the NUCA's cancellation of the land contract. SODIC has the right to appeal the fee set by the CRC in front of the State Council. Appeal hearing: 6 April Expected closure: 2013–14	SODIC wins the appeal and does not pay any settlements.	SODIC loses the appeal and pays a higher than expected settlement value.	SODIC pays a percentage of an estimated amount of EGP828m–EGP1.1bn, which represents the difference between prevailing prices and the acquisition price of the Eastown land, factoring in investments.	We value Eastown at EGP2.8/share, which includes the land acquisition premium and investments, and apply a discount of 60%.
(2) SI				
SODIC and SI filed for arbitration regarding the annulment of a contract under which SI was to develop 250,000 sqm of land in Westown. SI is requesting that SODIC pay EGP237m plus 9% interest. Expected closure: 2014–15	SODIC wins the arbitration and becomes legally entitled to the 250,000 sqm without any monetary outflow.	SODIC loses the arbitration, the land is returned to the government, and SODIC pays EGP160m–EGP237m to SI.	If SODIC loses the arbitration, the outflow would amount to EGP160m–EGP237m. If SODIC wins the arbitration, there will be no financial liability.	This piece of land is not included in our valuation, but, in a best-case scenario, it would add EGP2.2/share, bringing our valuation to EGP26.8/share.

Source: Company data, HC

Launch of Westown Residences supports sales; execution is on track to meet the 3-year deadline…

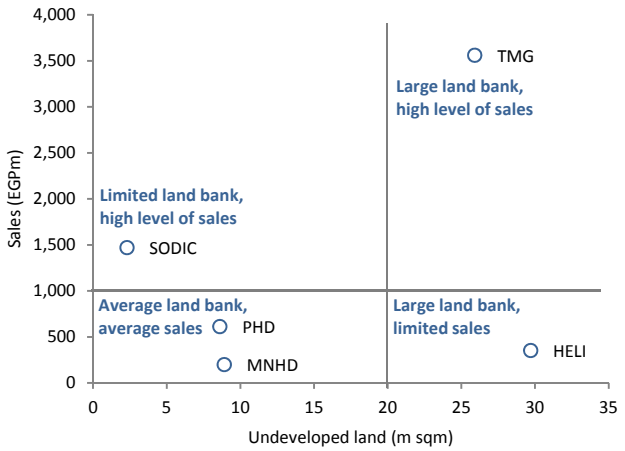
Competitively priced at EGP600,000–EGP1.2m per unit, phase 6 of Westown Residences has helped diversify SODIC's project portfolio away from the high-income segment. Westown Residences' product differentiation has helped keep sales strong, with the project contributing 51% of 2012's total net off-plan sales of EGP1.6bn. SODIC managed to sell a customer 7,000 sqm in its high-end project The Polygon for EGP79m. On the execution front, the company is expediting construction of Westown (55% developed) to meet the 3-year deadline. Also, SODIC launched Westown Hub, a retail project, with operations expected to kick in starting in 3Q13.

Strong y-t-d sales supported by Westown Residences… (EGPm)



Source: HC

…yet land replenishment remains biggest challenge



Source: HC

…but replenishing its land bank will be SODIC's main challenge, in our view

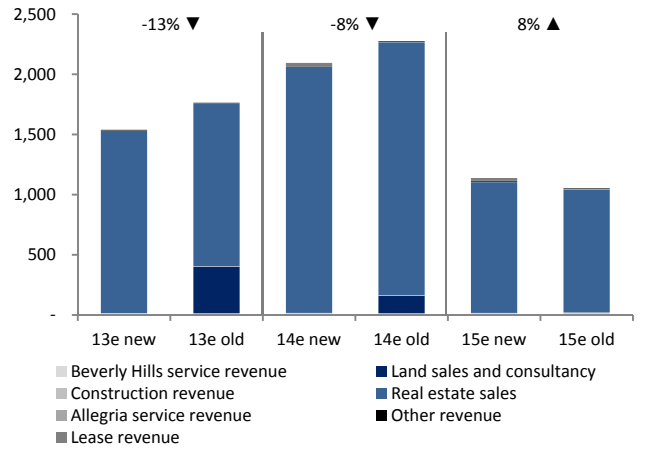
While SODIC ranks high in our coverage universe in terms of sales (gross sales of EGP1.5bn as of 9M12, the second highest following TMG), it has the smallest amount of undeveloped land with 2.5m sqm. SODIC's options for land acquisition revolve around (1) a favorable final outcome in the Eastown and SI cases, (2) the possibility of forming JVs on favorable terms with other developers that have sizable land banks, and (3) the possibility of acquiring land from private owners or through government auctions. SODIC's management is targeting presales of cEGP2bn–EGP3bn per year, which we believe could be achievable given its competent management and good track record, pending land bank expansion, however.

We lower our estimates as we exclude bulk land sales and revisit gross margins based on company guidance

We lower our 2013–14e revenue as we exclude bulk land sales given the company's need for land replenishment. We include phases 4–6 of Westown Residences, which increases 2015e revenue on expected deliveries. We also include lease revenue from Westown Hub starting in 2014e.

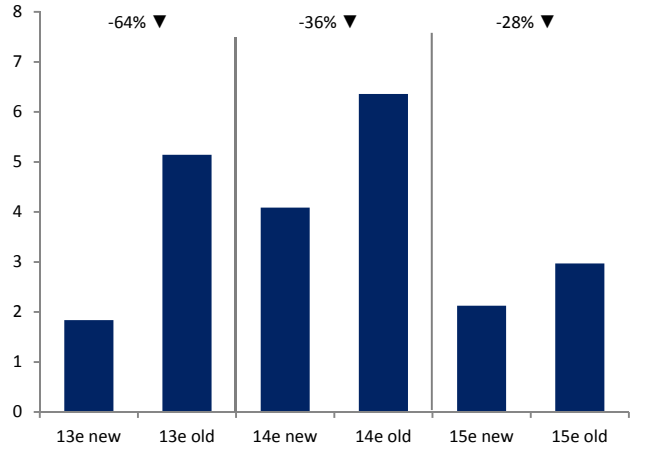
As per company guidance, we adjust the gross margins of certain projects. We decrease margins across SODIC's project portfolio with the exception of Allegria and Westown Residences. For 2013–15e, we lower our EPS forecasts on the back of decreased revenue and/or margins. Also, while we increase revenue 8% in 2015e and increase the margin on Westown Residences to 45%, reduced margins on Forty West and The Polygon impact earnings in that year.

Revenue estimate revisions (EGPm)



Source: HC

EPS estimate revisions (EGP)



Source: HC

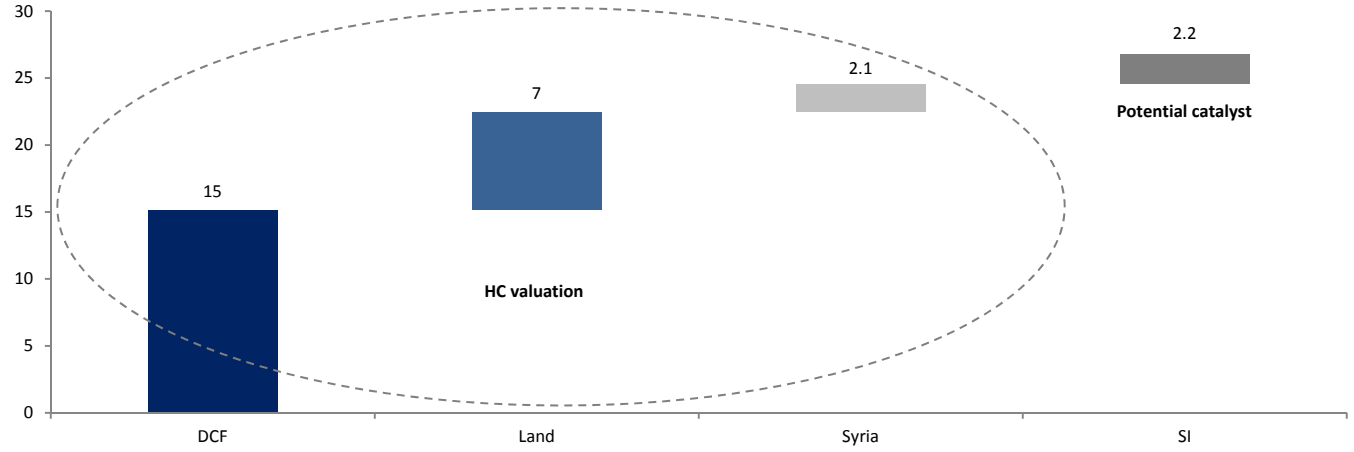
We lower our TP to EGP24.6/share and downgrade SODIC to Neutral on an increased WACC and decreased margins despite raising our land valuation

We maintain our land valuation discount at 60% as SODIC progresses with land monetization and continue to conservatively value Eastown at a 60% discount to its book value (including the land acquisition premium and investments incurred to date). We increase our land valuation 85% to EGP7.3/share as we (1) now use the full value of the company's investments in Eastown, including the land acquisition premium, rather than just the book value – this adds EGP2.0/share and brings Eastown's contribution to our valuation to EGP2.8/share, which represents 11% of our TP – and (2) revise land prices upward. We update our estimate for Westown to reflect prevailing prices (valued at EGP2,000/sqm versus EGP1,500/sqm previously). Having said that, we reduce our overall valuation to EGP24.6/share on the downward margins adjustment, the exclusion of bulk land sales, and an increased WACC of 19.6% (versus the previous 18.2%). We derive a DCF value of EGP15.18/share, down 21% as we increase our WACC after raising our beta to 1.4, despite decreasing our after-tax risk-free rate to 11.2% from 12.4% on decreased 1-year T-bill rates. We value the company's investments in Syria at their book value of EGP2.1/share. Our TP is at a 28% discount to SODIC's 2013e NAV of EGP34/share.

Risks

Key upside risks to our forecasts and valuation include (1) a favorable final outcome to the Eastown and SI land cases, (2) land replenishment, and (3) political and economic stability. Key downside risks include (1) an adverse outcome to the land litigations and (2) increased sales cancellations.

SI land is considered a catalyst that would add EGP2.2/share to current valuation of EGP24.6/share (EGP/share)



Source: HC

SODIC financial statements and ratios (EGPm)

Year to December	2008	2009	2010	2011	2012	2013e	2014e	2015e
Income statement								
Revenue	**232**	**31**	**520**	**542**	**1,426**	**1,539**	**2,094**	**1,139**
Total costs	**(109)**	**(33)**	**(266)**	**(561)**	**(929)**	**(1,015)**	**(1,345)**	**(708)**
Gross profit	**123**	**(2)**	**253**	**(19)**	**497**	**524**	**735**	**414**
Margin	*53%*	*-7%*	*49%*	*-4%*	*35%*	*34%*	*35%*	*36%*
Operating expenses	**(98)**	**(135)**	**(121)**	**(170)**	**(209)**	**(232)**	**(234)**	**(236)**
EBIT	**25**	**(137)**	**132**	**(189)**	**288**	**292**	**501**	**178**
Margin	*11%*	*-447%*	*25%*	*-35%*	*20%*	*19%*	*24%*	*16%*
Profit before taxes	**37**	**(138)**	**190**	**(186)**	**268**	**256**	**536**	**305**
Income taxes	(10)	25	(55)	(7)	(11)	(64)	(134)	(76)
Minority shareholder interest	0	2	1	(4)	7	25	31	36
Net profit (loss)	**27**	**(114)**	**135**	**(189)**	**250**	**167**	**371**	**193**
Margin	*12%*	*-373%*	*26%*	*-35%*	*18%*	*11%*	*18%*	*17%*
Basic EPS (EGP)	**1.0**	**(4.0)**	**3.7**	**(2.1)**	**2.8**	**1.8**	**4.1**	**2.1**
DPS (EGP)	-	-	4	-	-	-	-	2
EBITDA	**25**	**(137)**	**132**	**(166)**	**309**	**307**	**516**	**192**
Margin	*11%*	*-447%*	*25%*	*-31%*	*22%*	*20%*	*25%*	*17%*
Balance sheet								
Cash and cash equivalents	238	482	853	506	320	890	1,867	2,410
Trade and other receivables (current and noncurrent)	-	1,549	1,822	1,659	2,407	3,314	1,810	621
Development properties (Allegria)	0	920	1,306	1,245	855	473	-	-
Development work in progress (Eastown and Westown land)	1,310	795	1,093	1,390	1,801	1,537	1,051	446
Current assets	**3,863**	**4,568**	**6,330**	**5,695**	**6,287**	**7,004**	**5,404**	**4,039**
Noncurrent assets	**79**	**48**	**72**	**70**	**629**	**648**	**685**	**679**
Total assets	**4,242**	**5,016**	**6,902**	**6,365**	**6,916**	**7,652**	**6,089**	**4,717**
Current liabilities	**2,277**	**3,112**	**4,308**	**3,959**	**4,419**	**4,890**	**3,051**	**1,526**
Noncurrent liabilities	**183**	**146**	**186**	**450**	**332**	**405**	**279**	**204**
Minority interest in subsidiaries	25	26	96	43	52	77	108	144
Shareholder equity	**1,782**	**1,758**	**2,408**	**1,956**	**2,165**	**2,357**	**2,759**	**2,987**
Total liabilities and equity	**4,242**	**5,016**	**6,902**	**6,365**	**6,916**	**7,652**	**6,089**	**4,717**
Cash flow statement								
Cash flows from operating activities	**29**	**160**	**279**	**(405)**	**(183)**	**632**	**1,155**	**628**
Cash flows from investing activities	**(229)**	**(164)**	**(360)**	**(4)**	**11**	**(34)**	**(53)**	**(10)**
Cash flows from financing activities	**(17)**	**178**	**545**	**48**	**62**	**(27)**	**(125)**	**(75)**
Net addition (deduction) in cash	(217)	174	464	(361)	(110)	570	977	543
Cash at beginning of fiscal year	425	238	482	853	506	320	890	1,467
Cash at end of fiscal year	**238**	**482**	**853**	**506**	**320**	**890**	**1,867**	**2,410**
Key ratios								
Revenue growth		(87%)	N/M	4%	163%	8%	36%	(46%)
Net profit growth		N/A	N/A	(240%)	(232%)	(33%)	122%	(48%)
Debt/equity	0%	6%	6%	20%	20%	18%	12%	9%
Net debt	(237)	(385)	(720)	(114)	115	(455)	(1,537)	(2,134)
Net debt/equity	(13%)	(22%)	(30%)	(6%)	5%	(19%)	(56%)	(71%)
Current ratio	1.7	1.5	1.5	1.4	1.4	1.4	1.8	2.6
Average ROE		(6%)	6%	(9%)	12%	7%	14%	7%
Average ROIC		(6%)	6%	(8%)	11%	6%	13%	6%
P/B		1.1x	0.8x	1.0x	0.9x	0.9x	0.7x	0.7x
P/NAV					0.7x	0.6x		
P/E		(5.3x)	5.8x	(10.3x)	7.8x	11.6x	5.2x	10.1x

Source: Company data, HC

PHD: When the going gets tougher

- **Despite receiving financial support from its main shareholders, the company faces insolvency risk on insufficient funding, limited cash collection, and significant financial obligations**
- **Vulnerable to challenging economic environment due to business model**
- **The stock has rallied 28% since our last note; we resume coverage with a Neutral rating and a TP of EGP2.6/share**

PHD's liquidity problem has worsened as (1) its limited cash collection led to further construction and delivery delays, (2) it keeps rescheduling debt and land obligations, and (3) it has in**sufficient funding sources as banks are reluctant to extend it new loans in light of its worsening liquidity situation**. This had led the company to (1) almost halve its 2012e CAPEX to cEGP600m and (2) reschedule its 2012e land liabilities and debt to 2013e. We expect 2013e's funding gap to be wider than the EGP0.5bn announced for 2012e and believe it will be bridged through a combination of (1) further injections by El Mansour & El Maghraby Investment and Development in 2013–14e and (2) bank loans (though this could be challenging). We believe it will be difficult for PHD to fully close the 2013e gap and expect it to shift part of its CAPEX and land liabilities to future years. We expect its operational and financial problems to continue until sufficient cash is injected. The market is speculating that PHD is an acquisition target, which has supported the share price over the past year.

PHD's large exposure to the high-income and second home markets makes it more vulnerable than peers to the challenging economic environment. Its sales levels have dropped significantly since the revolution (gross sales down c81% between 2010 and 2011), while cancellations have surged (up 167%). Given that c55% of PHD's land was for second home projects, generating new sales became more challenging after the revolution (the segment experienced the most cancellations in 2011, 55% versus 45% in the primary home market). To ease its financial obligations, PHD returned c17m sqm (adjusted for its stake) of second home land along the North Coast and Red Sea to the government, but this might impact its competitive edge as a leader in the segment**.**

We raise our TP 5% from before we placed the stock under review to EGP2.6/share (67% discount to 2013e NAV of EGP8/share) but resume coverage with a Neutral rating as the stock has rallied 28% since our last note, in which we issued an Overweight recommendation (as the stock was oversold at that time). We value PHD using a combination of DCF and land valuation methods, deriving EGP2.4/share from projects and EGP0.2/share from land and investments. We increase our WACC to 18.1% as we raise our beta to 1.4 from 1.1. We hold our land discount at 85%.

Key multiples	2011	2012e	2013e
P/B	0.6x	0.6x	0.5x
P/NAV	0.3x	0.3x	0.3x

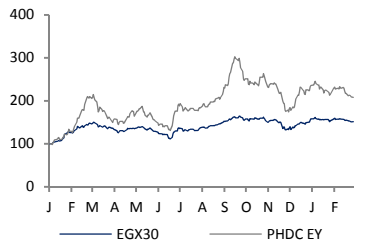
Source: HC

Neutral

Target price (EGP)	**2.6**
Current price (EGP)	2.3
Potential return	14%
Bloomberg	PHDC EY
Reuters	PHDC.CA
Mcap (EGPm)	2,380
Mcap (USDm)	355
Free float	36%
Daily volume (USDm)	5.8

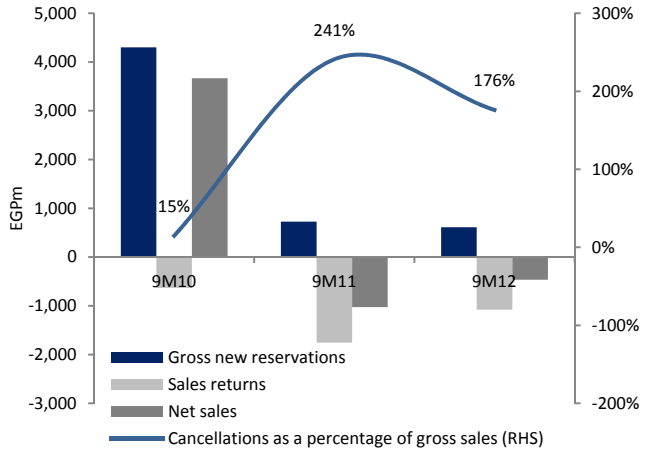
Note: All prices as of 3 March 2013

Price performance



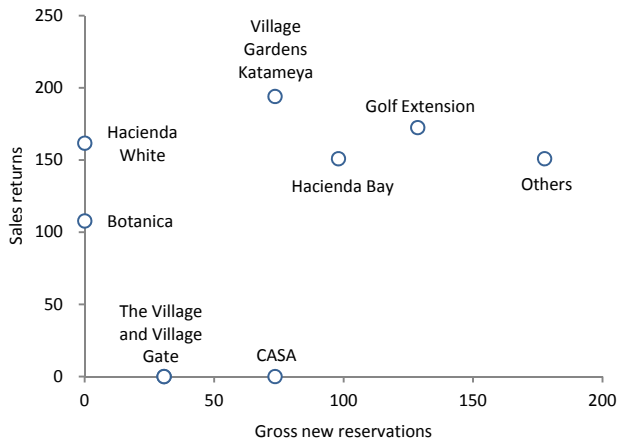
Regaining pre-revolution sales levels remains a challenge for PHD due to lack of customer confidence on the back of (1) its construction and delivery delays, (2) high cancellation rates in most of its projects, and (3) its funding problems, all of which have affected the company's image. Only 3 projects are generating positive net sales with no cancellations, namely CASA, The Village, and Village Gate, as they are in an advanced stage of construction. Some projects such as Botanica and Hacienda White have not generated any new sales since the start of 2012.

PHD is far from achieving pre-revolution sales levels; cancellations declined in 9M12 but still exceed gross sales



Source: Company data, HC

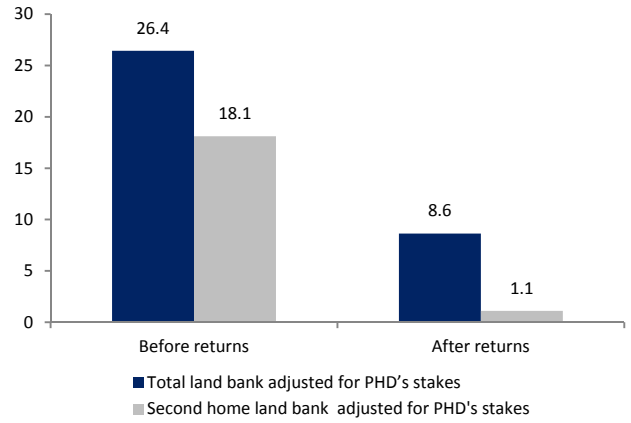
Village Gate, The Village, and CASA are the only projects achieving positive net sales as of 9M12 (EGPm)



Source: Company data, HC

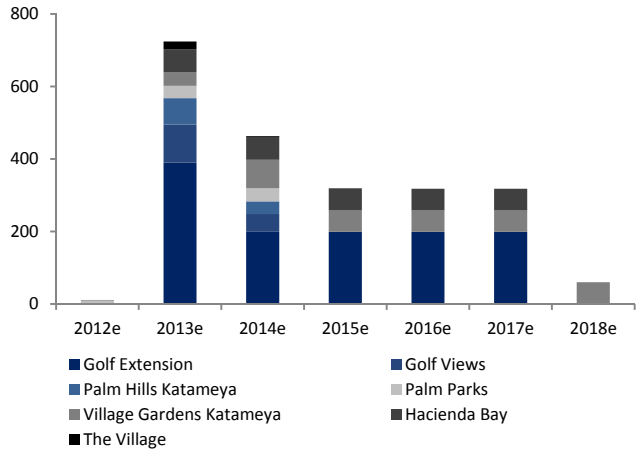
The North Coast and Red Sea land returns depleted the company's diversified second home land bank. On a more positive note, we believe the land returns will lower PHD's exposure to the second home market, which is extremely volatile, especially during slowdowns. The returns also reduced land liabilities 31%, easing the financial burden on the company, with cEGP2.2bn left to be paid in 2013–18. We believe it is unlikely that the government will return any of the funds PHD invested in the returned plots. We see the government reducing the company's remaining land liabilities by an equivalent amount as the more likely scenario. Although the land return may seem strategically correct under current circumstances, it might impact PHD's competitive edge as a leader in the second home segment when things pick up as it shrunk the company's second home land bank c94% (specifically, the returned Hacienda Bay Zone 3, Ain Sukhna, and Gamsha land accounted for 81% of the company's second home land portfolio). PHD's ability to develop new projects (both primary and secondary) will also be restricted to a decreased land bank of only c9m sqm versus c26m sqm before the land returns.

The 94% cut to PHD's second home land bank minimized its exposure to the segment but could hurt its competitive edge when things pick up (m sqm)



Source: Company data, HC

Remaining land liabilities, mostly on the Golf Extension project, to peak in 2013e and 2014e (EGPm)

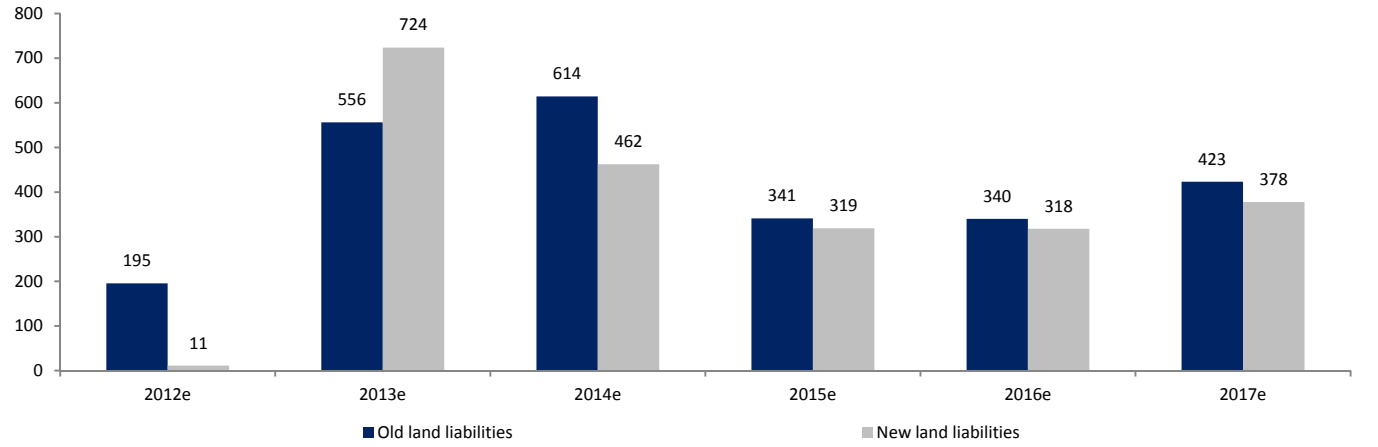


Source: Company data, HC

The company made some operational improvements during 2H12, such as (1) recording the lowest level of cancellations y-t-d in 3Q12, (2) achieving a narrower net loss, and (3) reducing SG&A expenses, which comprise the bulk of expenses. At EGP280m, 3Q12's cancellations were the lowest y-t-d, narrowing the company's negative net presales figure to EGP48m (versus a negative EGP238m in 2Q12 and negative EGP179m in 1Q12). As of 9M12, net presales had also improved, recording a negative figure of EGP465m compared with 9M11's negative EGP1,027m. In 3Q12, PHD's net loss also narrowed to EGP3m, the smallest since 2011. SG&A expenses fell 24% to cEGP120m in 9M12, though the company missed its target of lowering yearly SG&A to EGP120m through decreased advertising, layoffs, and salary cuts.

We expect PHD's funding gap to widen in this year as (1) 2013e CAPEX increased to an estimated cEGP700m after the 2012e figure was cut, (2) land liabilities were shifted to 2013e from 2012e, bringing 2013e repayments to cEGP754m, and (3) debt repayments were rescheduled. We expect El Mansour & El Maghraby Investment and Development to make further injections of cEGP400m in 2013–14e to partially bridge the funding gap, bringing its total accumulated injections from an expected EGP594m as of the end of 2012e to EGP994m by 2014e. Nevertheless, we believe PHD will have to take on more debt to close its funding gap, but this remains extremely challenging given the company's distressed financial position, as reflected by its (1) worsened liquidity profile, with a net debt/equity ratio (including land liabilities) of 1.3x as of 9M12 versus 0.9x as of 1H12 (the highest among peers), (2) distressed cash flows, with cancellations exceeding new sales in most projects and receivables collection of c60% (though this is an improvement from a previous rate of c30%, it is still low compared to peers' average of c90%), and (3) minimal cash levels versus project size (EGP71m as of 9M12).

Shifting land liabilities to further pressure PHD's financial position in 2013e, resulting in an increased funding gap (EGPm)



Source: Company data, HC

Valuation

We resume coverage of the stock with a Neutral recommendation versus our previous rating of Overweight (as the stock was oversold at that time) from before we placed the stock under review. We raise our TP to EGP2.6/share on the back of increased margins. We value PHD using a combination of DCF and land valuation methods, deriving EGP2.4/share from projects and EGP0.2/share from land and investments. Despite the fact that 1-year T-bill rates have fallen to 14.0% from 15.7%, we increase our WACC to 18% as we raise our beta to 1.4 from 1.1. Our TP represents a discount of 67% to our 2013e NAV of EGP8/share.

We take a conservative approach in valuing PHD, accounting for neither (1) proceeds from its return of c17m sqm of land to the government nor (2) sales from Botanica, given the high level of returns due to the delay in the adjustment of the project's master plan. We maintain our land valuation discount at 85% due to the uncertainty surrounding PHD's land bank, but we increase our land valuation 1% to EGP0.23/share to reflect increased land prices in New Cairo and Sixth of October City. We account for PHD's investments in Saudi Arabia at book value, deriving EGP0.02/share after applying an 85% discount.

Risks

Key upside risks to our forecasts and valuation include (1) the return of Yaseen Mansour, which we believe could improve client confidence, (2) approval of the master plan of Botanica (PHD's largest project), and (3) the sale of the Saudi land at a favorable valuation. Downside risks include (1) an inability to close funding gaps due to tight liquidity, (2) further delays in construction and deliveries, (3) increased cancellations, (4) difficulty generating new sales, and (5) an adverse outcome to land disputes, leading to settlements for which the company has not provisioned.

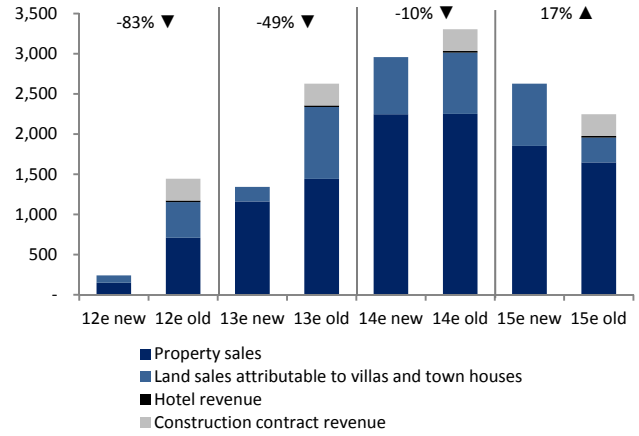
A snapshot of PHD's current land bank (m sqm)	
Total undeveloped land bank	31.2
Land bank adjusted for ownership stakes	26.4
Land filed for return adjusted for ownership stakes	-17.8
Raw undeveloped land (HC estimate)	**8.6**
Built-up area of launched project phases	2.8

Source: HC

Revenue estimates for 2012–14e decreased and pushed back on construction and delivery delays

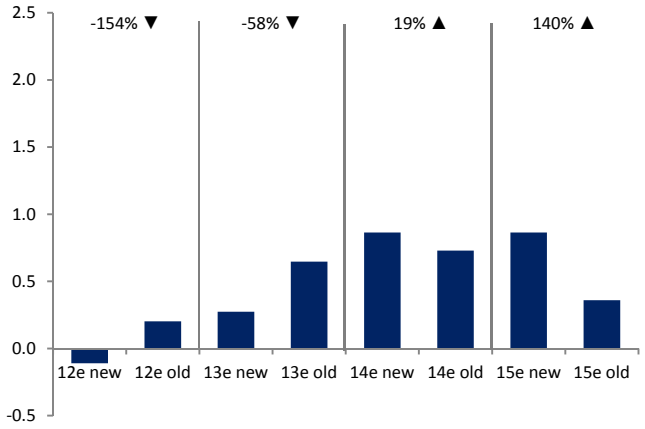
We lower our revenue estimates 83% for 2012e, 49% for 2013e, and 11% for 2014e due to construction and delivery delays. We therefore push deliveries back, increasing our 2015e revenue estimate 17%. Our EPS forecasts for 2012–13e are down on the back of the decreased revenue projections but up for 2014e on increased margins.

Revenue estimate revisions (EGPm)



Source: Company data, HC

EPS estimate revisions (EGP)



Source: Company data, HC

Palm Hills Developments financial statements and ratios (EGPm)

Year to December	2008	2009	2010	2011	2012e	2013e	2014e	2015e
Income statement								
Revenue	**1,235**	**1,146**	**1,831**	**572**	**243**	**1,346**	**2,954**	**2,628**
Total costs	**(293)**	**(455)**	**(838)**	**(619)**	**(220)**	**(755)**	**(1,617)**	**(1,351)**
Gross profit	**941**	**691**	**993**	**(47)**	**23**	**592**	**1,337**	**1,277**
Margin	*76%*	*60%*	*54%*	*-8%*	*10%*	*44%*	*45%*	*49%*
EBIT	**755**	**503**	**606**	**(298)**	**(196)**	**368**	**1,109**	**1,045**
Margin	*61%*	*44%*	*33%*	*-52%*	*-81%*	*27%*	*38%*	*40%*
Profit before taxes	**719**	**560**	**636**	**(347)**	**(113)**	**337**	**1,066**	**1,065**
Income taxes	(59)	(40)	(91)	(1)	(0)	(51)	(160)	(160)
Minority shareholder interest	**2**	**45**	**19**	**(17)**	**2**	**-**	**-**	**-**
Net profit (loss)	**658**	**476**	**526**	**(331)**	**(115)**	**287**	**906**	**905**
Margin	*53%*	*42%*	*29%*	*-58%*	*-47%*	*21%*	*31%*	*34%*
Basic EPS (EGP)	**1.5**	**0.7**	**0.5**	**(0.3)**	**(0.1)**	**0.3**	**0.9**	**0.9**
DPS (EGP)	-	-	-	-	-	-	0.2	0.8
EBITDA	**755**	**503**	**606**	**(298)**	**(196)**	**368**	**1,109**	**1,045**
Margin	*61%*	*44%*	*33%*	*-52%*	*-81%*	*27%*	*38%*	*40%*
Balance sheet								
Cash and cash equivalents	280	135	144	72	171	12	603	906
Notes receivable (postdated checks)	683	967	1,585	1,362	1,077	722	570	443
Development properties	4,940	5,474	5,354	3,514	3,391	3,197	2,561	2,143
Current assets	**6,425**	**7,250**	**8,446**	**6,588**	**6,840**	**6,662**	**5,836**	**4,388**
Noncurrent assets	**2,720**	**3,281**	**4,638**	**5,326**	**4,440**	**4,723**	**5,013**	**5,193**
Total assets	**9,145**	**10,531**	**13,084**	**11,914**	**11,280**	**11,384**	**10,849**	**9,581**
Current liabilities	**2,681**	**3,692**	**5,056**	**4,039**	**3,875**	**3,248**	**2,679**	**2,454**
Noncurrent liabilities	**3,633**	**3,429**	**3,219**	**3,584**	**3,148**	**3,394**	**2,478**	**1,768**
Minority interest in subsidiaries	145	248	421	288	274	274	274	274
Shareholder equity	**2,832**	**3,410**	**4,809**	**4,291**	**4,257**	**4,743**	**5,692**	**5,358**
Total liabilities and equity	**9,145**	**10,531**	**13,084**	**11,914**	**11,280**	**11,384**	**10,849**	**9,581**
Cash flow statement								
Cash flows from operating activities	**(572)**	**(30)**	**(584)**	**(193)**	**(87)**	**(662)**	**1,755**	**2,251**
Cash flows from investing activities	**(518)**	**(250)**	**(353)**	**238**	**(30)**	**(754)**	**(492)**	**(349)**
Cash flows from financing activities	**1,359**	**99**	**950**	**(94)**	**193**	**1,257**	**(672)**	**(1,598)**
Net addition (deduction) in cash	268	(181)	13	(49)	77	(159)	590	303
Cash at beginning of fiscal year	-	168	(11)	144	171	171	12	603
Cash at end of fiscal year	**280**	**135**	**144**	**72**	**248**	**12**	**603**	**906**
Key ratios								
Revenue growth	131%	(7%)	60%	(69%)	(58%)	454%	119%	(11%)
Net profit growth	234%	(28%)	11%	(163%)	(65%)	(349%)	216%	0%
Debt/equity	22%	22%	21%	21%	21%	41%	22%	17%
Net debt	144	473	531	764	586	1,802	497	(166)
Net debt/equity	5%	14%	11%	18%	14%	38%	9%	(3%)
Current ratio	2.4	2.0	1.7	1.6	1.8	2.1	2.2	1.8
Average ROE		15%	13%	(7%)	(3%)	6%	17%	16%
Average ROIC		14%	12%	(7%)	(2%)	5%	14%	14%
P/B		0.8x	0.5x	0.6x	0.6x	0.5x	0.4x	0.5x
P/NAV			0.4x	0.3x	0.3x	0.3x		
P/E		3.3x	4.5x	N/M	N/M	8.3x	2.6x	2.6x

Source: Company data, HC

Heliopolis Housing: Long road to monetization

- **Inefficient capital structure continues to inhibit the company's growth despite its attractive land bank**
- **Funding options (long-term financing or partnerships) are key for the stock to re-rate; limited sales capacity adds to the problem**
- **We maintain our Neutral rating but increase our TP 28% to EGP24.3/share on an upward revision of land prices**

Despite its strong fundamentals (c30m sqm Cairo land bank with almost no litigation risk and good exposure to mid-income demand), the company's growth remains inhibited by inefficient cash flow management. This is due to the company's (1) lack of off-plan sales even though it makes payment facilities of up to 20 years, (2) persistence in using short-term borrowing to finance its long-term projects as it is unwilling to use its land bank as debt collateral, capping gearing at a level that inhibits growth, and (3) maintenance of a high dividend payout policy (historical payout ratio of 75%–105%). **These factors have led to an ineffective cash cycle and have drained the company's liquidity, capping its growth potential.**

Any announcement of bulk sales in New Heliopolis City (possible sale of 211 feddans in the commercial area) or Sheraton (possible sale of 8 buildings) could provide short-term liquidity relief, but taking long-term debt to finance construction works or entering into partnerships on the project level would accelerate value unlocking and act as catalysts.

We increase our TP 28% to EGP24.3/share while maintaining our Neutral rating, mainly because we adjust our land prices to match prevailing market prices. That said, despite the company's litigation-free land bank, we standardize our discount factor to 85% across the company's land bank from 65%–85% previously given slow monetization. We increase our land valuation, which now accounts for EGP23/share, and derive a reduced EGP1.5/share from DCF. Our TP represents a deep discount of 84%to our 2013e NAV of EGP159/share, which reflects the company's weak monetization efforts and maturity profile, with most of its value coming from land.

Key multiples	2011/12	2012/13e	2013/14e
P/B	6.5x	6.9x	6.1x
P/NAV	0.1x	0.1x	0.1x

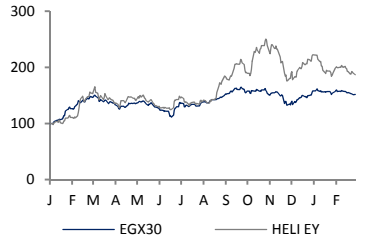
Source: Company data, HC

Neutral

Target price (EGP)	**24.3**
Current price (EGP)	20.4
Potential return	19%
Bloomberg	HELI EY
Reuters	HELI.CA
Mcap (EGPm)	2,265
Mcap (USDm)	338
Free float	28%
Daily volume (USDm)	0.5

Note: All prices as of 3 March 2013

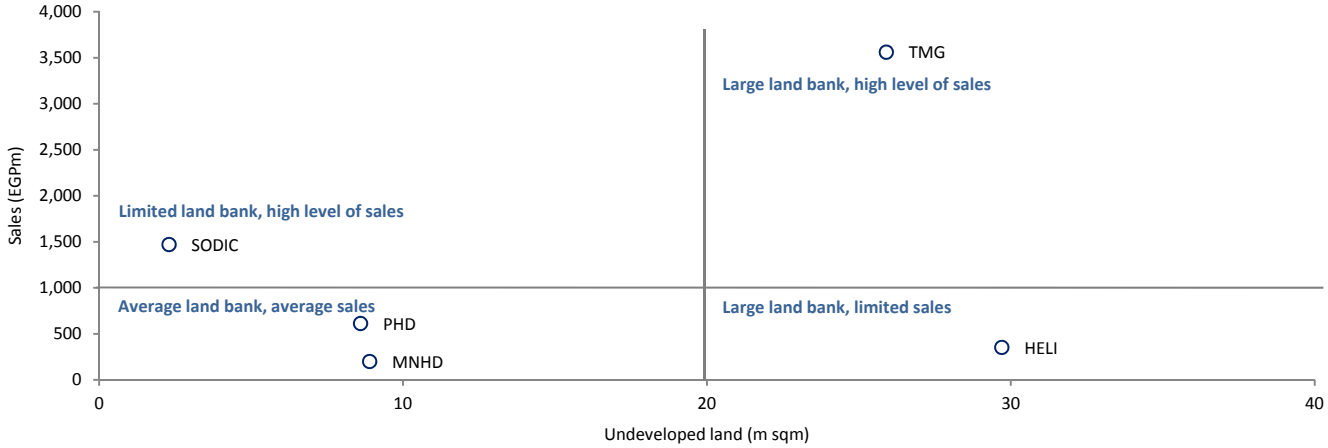
Price performance



Heliopolis Housing's contracted sales do not reflect the size of its land bank

Although Heliopolis Housing's undeveloped land bank of c30m sqm is the largest in our coverage universe, its contracted sales were the second lowest in 2011 and we expect them to be the lowest starting this year as we believe Tag Sultan will increase Madinet Nasr Housing's contracted sales to EGP700m–EGP830m by 2013e.

Heliopolis Housing has the biggest undeveloped land bank in our coverage universe but had the second lowest contracted sales in 2011

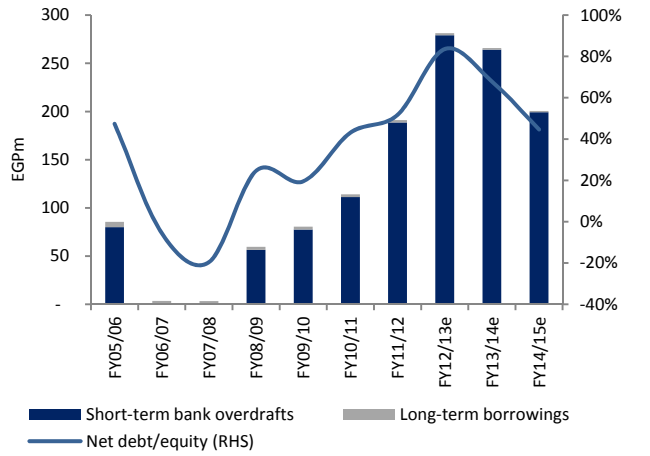


Source: HC

Dividend distribution policy continues to inhibit growth

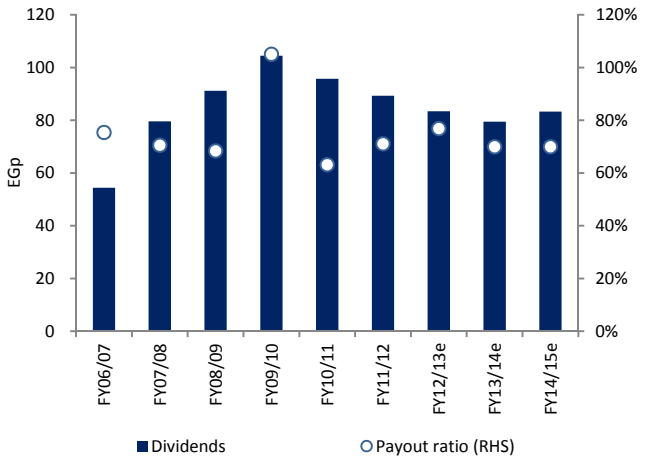
Despite Heliopolis Housing's efforts to conserve cash, the government, which holds a 72% stake in the company, is keen on extracting dividends from it, which we believe compromises the company's long-term growth strategy. Its payout ratio has been as high as 105% of earnings (see the chart on the next page). We see this as a concern as the company seeks short-term bank financing (76% net debt/equity as of 1H12/13) to finance its long-term projects and to implicitly finance its dividend distribution. That said, the company's cash fell to an all-time low of EGP0.8m in 1Q12/13.

Increased leverage (net debt/equity c76% as of 1H12/13)…



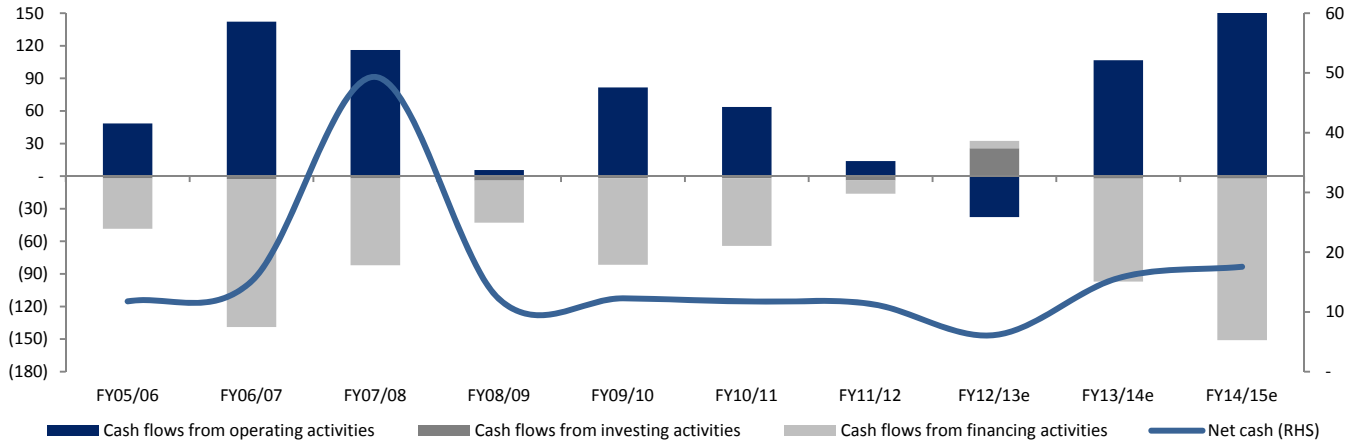
Source: HC

…to finance construction works in light of high dividend payout policy



Source: HC

Net cash flows impacted by high dividend payout (EGPm)



Source: HC

Bulk sales of land and buildings could provide liquidity relief

We understand that Heliopolis Housing intends to offer for sale 211 feddans (886,200 sqm) of land in the commercial area of New Heliopolis City as well as 8 buildings in Sheraton. We see such sales as short-term catalysts as they could provide the company with liquidity relief. If the sale of the 211 feddans goes through, we expect it to generate proceeds of cEGP0.9bn–EGP1bn over the coming 10 years (EGP1,000–EGP1,200 per sqm). We conservatively exclude the buildings and the 211 feddans from our DCF valuation and include them as part of our land valuation at a decreased price of EGP500/sqm, especially as the land was offered at a previous auction but received no interest. As per the company's auction regulations, at least 3 buyers must compete for the land, with the buyer offering the highest advance payment winning the auction. If only 1–2 buyers show interest, the auction is cancelled.

Maintain rating at Neutral but increase TP 28% to EGP24.3/share

We maintain our Neutral recommendation on Heliopolis Housing but raise our TP 28% to EGP24.3/share. We value the company using a combination of land valuation and DCF (for launched projects). The main change to our valuation is an upward revision of our land valuation to match prevailing prices. Land contributes c94% to our valuation at EGP23/share (up 49% from our previous valuation of EGP15/share). We now value the company's Heliopolis plot at EGP1,500/sqm versus EGP750/sqm previously. We also increase the value of New Heliopolis City and Helio Park land to EGP500/sqm. Despite the company's attractive land bank location, we see minimal progress on land bank monetization; as such, we standardize our land bank discount at 85% from 65%–85% previously.

For our DCF valuation, we lower our WACC to 18.7% from 20.0% as we adjust our after-tax risk-free rate to 11.3% to reflect decreased yields on 1-year T-bills (14.07% as of February). Having said that, we derive a decreased DCF value of EGP1.5/share (60% lower than our previous estimate of EGP3.74/share) as we reduce margins going forward based on company guidance. We value Heliopolis Housing at an 85% discount to its FY12/13e NAV of EGP159/share. The increased discount to NAV reflects the company's slow land monetization and maturity profile, with a large portion of its value coming from land.

Risks

Key downside risks to our forecasts and valuation include (1) inhibition of land monetization due to the company's conservative business approach and (2) high leverage on property prices as 94% of its valuation comes from land. Possible catalysts include (1) the sale of 211 feddans in New Heliopolis City and 8 buildings in Sheraton and (2) a different approach to business through the assumption of long-term debt or the establishment of partnerships on the project level.

Land valuation details

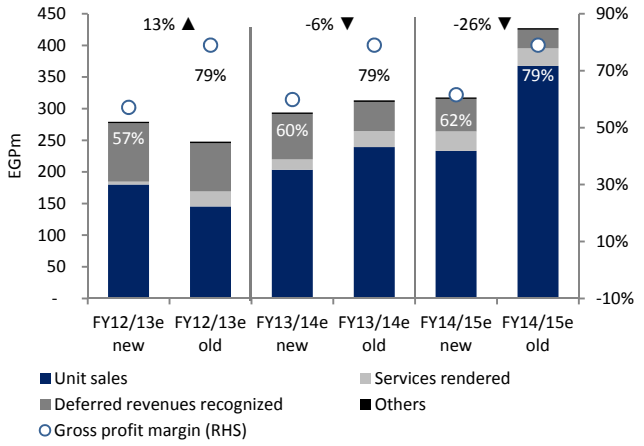
Project	Land area (m sqm)	Value/sqm (EGP)	Total value (EGPm)	Discount factor	Value after discount (EGPm)	Value/share (EGP)
Heliopolis	2.5	1,500	3,813	85%	557	5.0
New Heliopolis City	20.0	500	9,978	85%	1,457	13.1
Obour City	0.1	500	47	85%	7	0.1
Helio Park	7.1	500	3,560	85%	520	4.7
Total	**29.7**		**17,397**		**2,540**	**22.8**

Source: HC, company data

We reduce our EPS estimates going forward, mainly on decreased margins

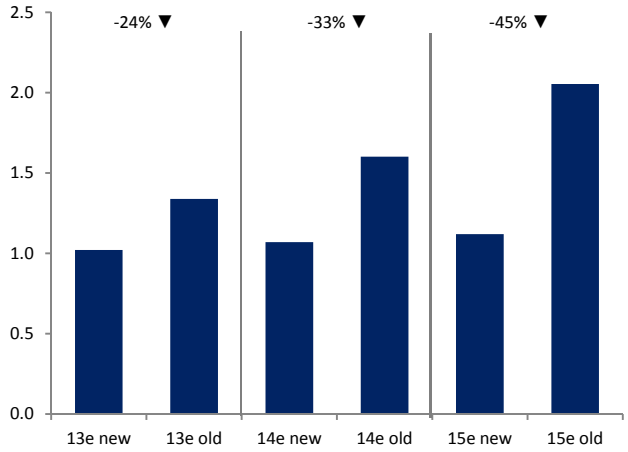
We increase our FY12/13e revenue forecast 13% as the company beat our estimate in FY11/12; however, our new projection is still 13% lower than company guidance of EGP322m as management is known to budget liberally (revenue came in 17% lower than guidance while net income missed by 33% in FY11/12). We also lower our revenue estimates for FY13/14e and FY14/15e as we smooth sales and deliveries more towards FY15/16e and FY16/17e. We decrease our gross profit margin forecasts to 57%–62%, in line with that of FY11/12 and management guidance. We therefore lower our bottom line expectations as well.

Revenue and margin estimate revisions



Source: HC

EPS estimate revisions (EGP)



Source: HC

Heliopolis Housing financial statements and ratios (EGPm)

Year to June	FY10/11	FY11/12	FY12/13e	FY13/14e	FY14/15e
Income statement					
Revenue	**209**	**248**	**279**	**294**	**318**
Total costs	**(61)**	**(104)**	**(120)**	**(118)**	**(122)**
Gross profit	**148**	**143**	**160**	**176**	**196**
Margin	*71%*	*58%*	*57%*	*60%*	*62%*
EBIT	**116**	**108**	**118**	**132**	**148**
Margin	*56%*	*43%*	*42%*	*45%*	*47%*
Profit before taxes	**159**	**146**	**151**	**159**	**166**
Income taxes	(33)	(38)	(38)	(40)	(42)
Minority shareholder interest	-	-	-	-	-
Net profit (loss)	**126**	**108**	**113**	**119**	**125**
Margin	*60%*	*44%*	*41%*	*40%*	*39%*
Basic EPS (EGP)	**1.1**	**1.0**	**1.0**	**1.1**	**1.1**
DPS (EGP)	0.9	0.8	0.7	0.7	0.7
EBITDA	**117**	**108**	**118**	**132**	**149**
Margin	*56%*	*43%*	*42%*	*45%*	*47%*
Balance sheet					
Cash and cash equivalents	12	11	6	16	18
Customer receivables	1,132	1,379	1,472	1,317	1,121
Current assets	**1,561**	**1,814**	**1,834**	**1,609**	**1,336**
Noncurrent assets	**23**	**23**	**24**	**25**	**26**
Total assets	**1,584**	**1,838**	**1,857**	**1,634**	**1,362**
Current liabilities	**1,235**	**1,386**	**1,457**	**1,210**	**913**
Noncurrent liabilities	**112**	**104**	**72**	**56**	**40**
Minority interest in subsidiaries	-	-	-	-	-
Shareholder equity	**237**	**347**	**329**	**369**	**410**
Total liabilities and equity	**1,584**	**1,838**	**1,857**	**1,634**	**1,363**
Cash flow statement					
Cash flows from operating activities	**64**	**14**	**(38)**	**107**	**153**
Cash flows from investing activities	**(2)**	**(4)**	**26**	**(2)**	**(2)**
Cash flows from financing activities	**(62)**	**(12)**	**7**	**(95)**	**(149)**
Net addition (deduction) in cash	(1)	(2)	(5)	10	2
Cash at beginning of fiscal year	12	16	11	6	16
Cash at end of fiscal year	**12**	**11**	**6**	**16**	**18**
Key ratios					
Revenue growth	-35%	18%	13%	5%	8%
Net profit growth	-17%	-14%	5%	5%	5%
Debt/equity	48%	55%	85%	72%	49%
Net debt	102	180	275	250	183
Net debt/equity	43%	52%	84%	68%	45%
Current ratio	1.3	1.3	1.3	1.3	1.5
Average ROE	43%	37%	34%	34%	32%
Average ROIC	42%	37%	33%	34%	32%
P/B	9.5x	6.5x	6.9x	6.1x	5.5x
P/NAV		0.1x	0.1x	0.1x	
P/E	18.0x	20.9x	20.0x	19.0x	18.2x
Dividend yield	4%	4%	4%	4%	4%

Source: Company data, HC

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Company name: Talaat Mostafa Group Holding Company	**Disclosure:** None
Company name: Madinet Nasr Housing	**Disclosure:** None
Company name: Sixth of October for Development and Investment Company	**Disclosure:** 8
Company name: Palm Hills Developments	**Disclosure:** None
Company name: Heliopolis Housing and Development Company	**Disclosure:** None

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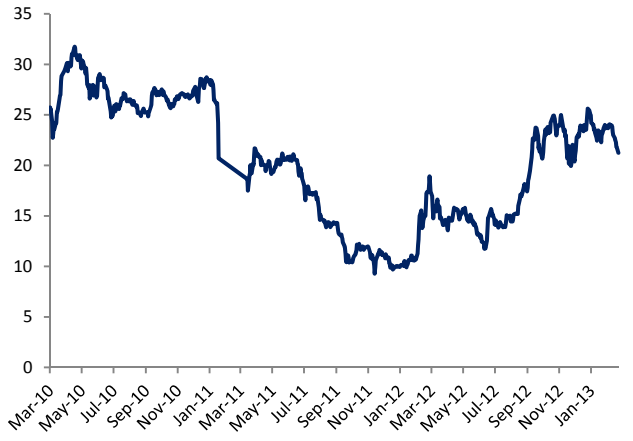
Rating	Count	Percent	Percent provided investment banking services in past 12 months
Overweight (OW)	10	62.50	0.00
Neutral (N)	5	31.25	0.00
Underweight (UW)	1	6.25	0.00

Talaat Mostafa Group Holding Company as of 3 March 2013

Date	Recommendation	Target price[1]
7 Dec 2009	Overweight	EGP8.8
4 May 2010	Overweight	EGP11.2
16 Sep 2010	Underweight	EGP5.6
28 Sep 2010	Overweight	EGP11.2
22 Nov 2010	Overweight	EGP9.8
28 Feb 2011	Underweight	EGP6.1
18 Aug 2011	Overweight	EGP5.1
26 Apr 2012[2]	Overweight	EGP5.8
9 Jul 2012	Neutral	EGP5.2
10 Mar 2013	Overweight	EGP6.4

Note: (1) Adjusted for stock dividend (2) Change of analyst

Madinet Nasr Housing as of 3 March 2013



Date	Recommendation	Target price[1]
4 May 2010	Overweight	EGP48.0
22 Nov 2010	Overweight	EGP37.0
28 Feb 2011	Neutral	EGP25.0
18 Aug 2011	Overweight	EGP19.0
26 Apr 2012[2]	Neutral	EGP20.5
11 Nov 2012	Overweight	EGP31.3

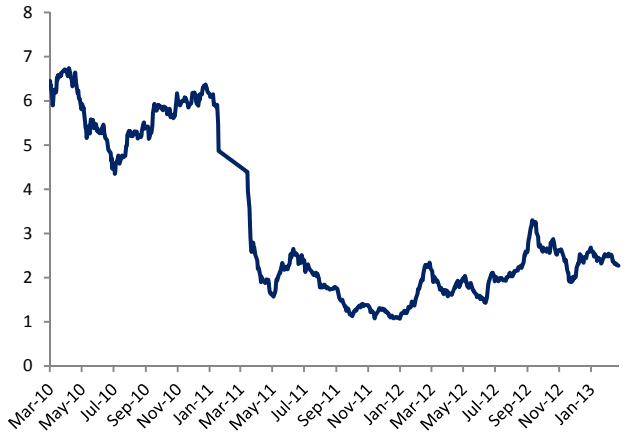
Note: (1) Adjusted for stock dividend (2) Change of analyst

Sixth of October for Development and Investment Company as of 3 March 2013

Date	Recommendation	Target price[1]
7 Dec 2009	Overweight	EGP42.0
4 May 2010	Overweight	EGP50.0
22 Nov 2010	Overweight	EGP52.0
28 Feb 2011	Neutral	EGP38.0
18 Aug 2011	Overweight	EGP29.0
26 Apr 2012[2]	Overweight	EGP27.4
20 Jun 2012	Overweight	EGP25.8
10 Mar 2013	Neutral	EGP24.6

Note: (1) Adjusted for stock dividend (2) Change of analyst

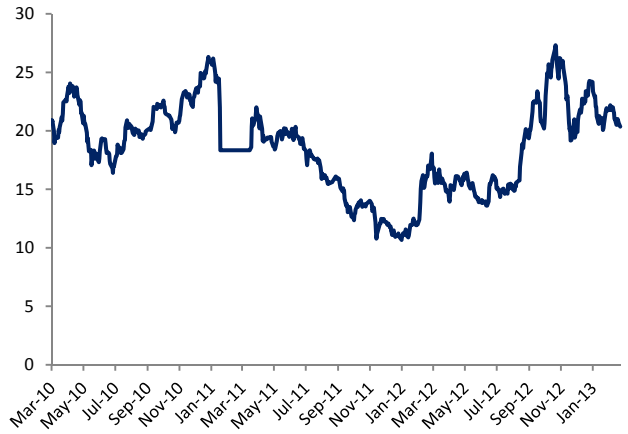
Palm Hills Developments as of 3 March 2013



Date	Recommendation	Target price
7 Dec 2009	Neutral	EGP9.5
4 May 2010	Neutral	EGP7.5
22 Nov 2010	Overweight	EGP7.5
28 Feb 2011	Underweight	EGP4.6
18 Aug 2011	Neutral	EGP2.1
26 Apr 2012[1]	Overweight	EGP2.5
13 Nov 2012	Under Review	N/A
10 Mar 2013	Neutral	EGP2.6

Note: (1) Change of analyst

Heliopolis Housing and Development Company as of 3 March 2013



Date	Recommendation	Target price[1]
22 Nov 2010	Neutral	EGP27.3
28 Feb 2011	Neutral	EGP18.3
24 Mar 2011	Neutral	EGP21.4
18 Aug 2011	Neutral	EGP17.9
26 Apr 2012[2]	Neutral	EGP19.0
10 Mar 2013	Neutral	EGP24.3

Note: (1) Adjusted for stock dividend (2) Change of analyst

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