The Monthly Chronicles August 2019

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A Month in Brief – A Well-Received Rate Cut

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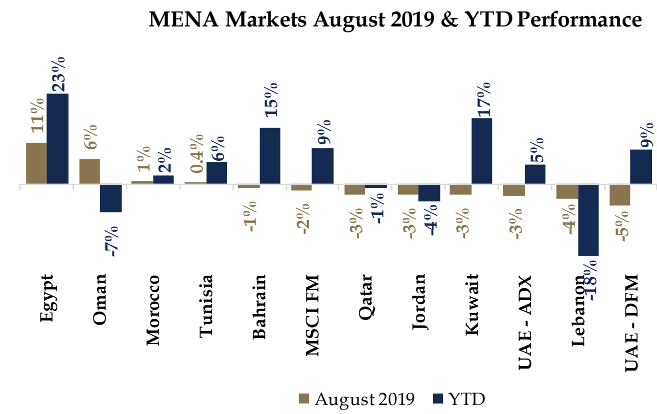
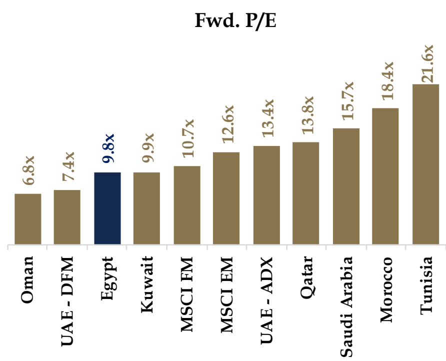
In *The Daily Beam* dated 19 August 2019, we came to a conclusion that the US equity market's oft-cited phenomenon "Sell in May and Go Away" is translated to "Buy in August and Sell in February" in Egypt. Judging from the performance of the Egyptian equities so far, that interpretation clearly holds true with the EGX 30 gaining 11% in August (+23% ytd). Also, traded value totaled EGP15bn in August, the fourth-highest month so far in 2019, with the last session in the month recording more than EGP1.3bn. We can largely attribute this outstanding performance to the CBE's decision to cut interest rates by 150bps in late August, a much-anticipated move that encouraged investors to dive deeper into the market. Foreigners turned buyers to a large measure in August from being heavy net sellers in July, but we note that a considerable part of their inflows was induced by the execution of Global Telecom Holding's (GTHE) deal. Egyptians were mostly the sellers in GTHE's deal, and Arabs also turned net sellers on a ytd basis. Egypt is still the third cheapest market, trading at a discount to MSCI EM and MSCI FM. Below, we analyze the market performance during August.

- **Egypt**'s equity market was the best performer compared to its MENA peers in August after it was the second worst market in July. **EGX 30** gained 11% in USD terms in August, outperforming **MSCI FM** (-2%) and **MSCI EM** (-7%). Accordingly, Egypt returned to top MENA markets on a ytd basis after being fifth in July, with the EGX 30 index adding 23% ytd in USD terms. On the valuation side, Egypt is still the third cheapest among the MENA markets behind **Oman** and **Dubai**. By the end of August, EGX 30 was traded at a 22% discount to MSCI EM and at a 8% discount to MSCI FM.

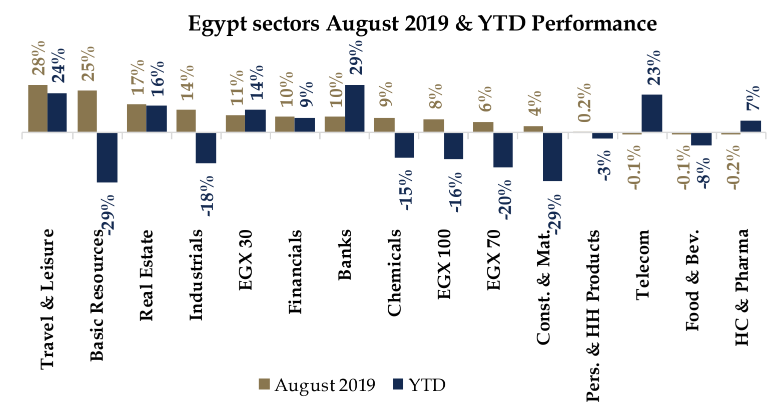


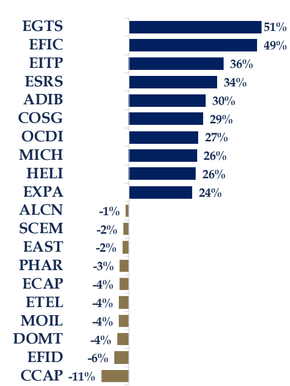


Note: Performance measured in USD terms. Source: Bloomberg.

- After the bloody month of July, most of **EGX** sectors returned to the green zone in August. **Travel & leisure** and **basic resources** were the top risers, while **health care & pharmaceuticals**, **food & beverage**, and **telecom** were the only decliners during August 2019. Judging from the market's generally good performance in August, it seems that investors opted for cyclicals as opposed to non-cyclicals (i.e. **health care** and **F&B**). Indeed, **basic resources** was lifted by a remarkable performance by **Ezz Steel** (ESRS), after its 55%-owned subsidiary **Al-Ezz Dekheila Steel**'s (IRAX) BoD agreed

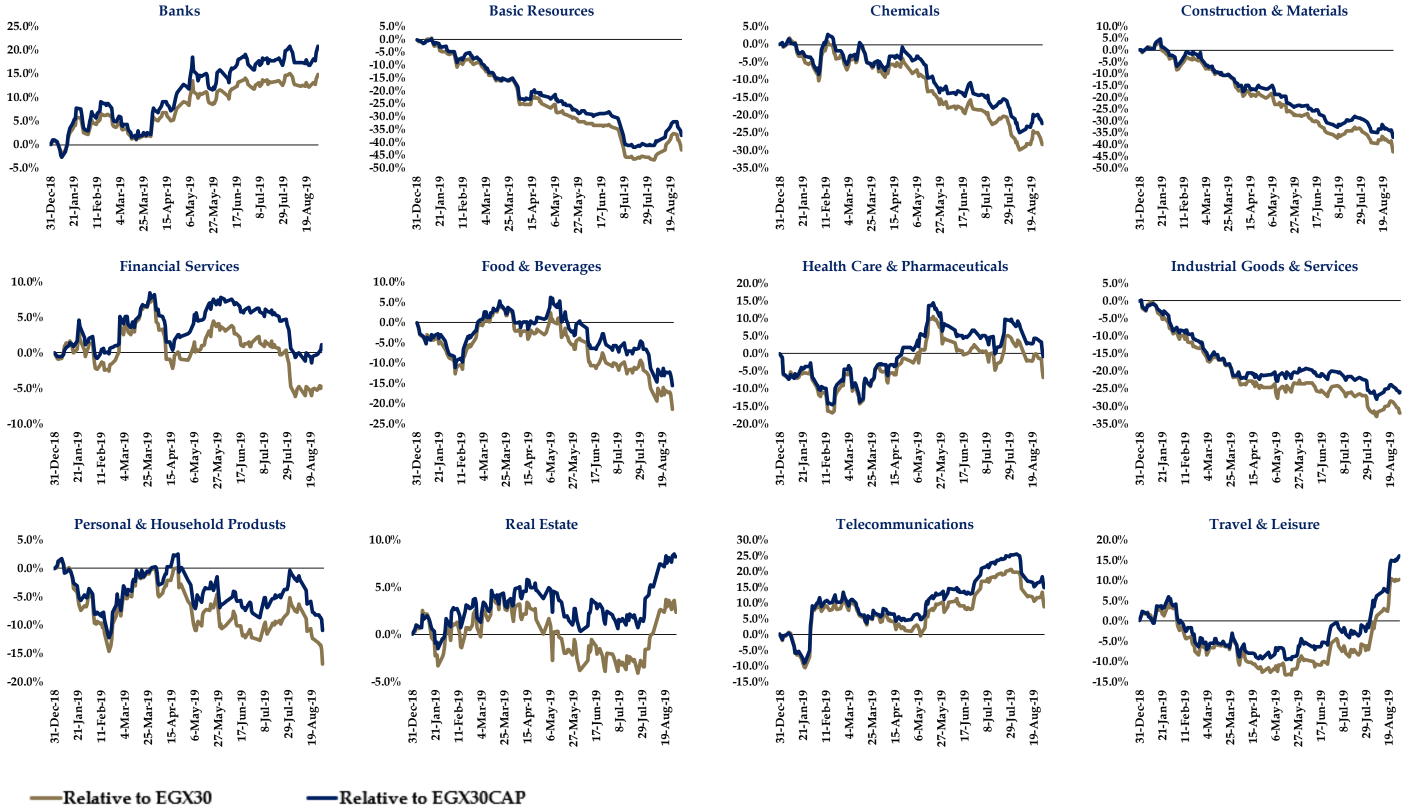
On a ytd basis, **banks**, **telecom**, and **travel & leisure** were the top winners, while **basic resources** and **construction & materials** lost the most. The below chart to the right depicts ten of the the best- and worst-performing stocks in the EGX 100 based on an analysis of total return in August.





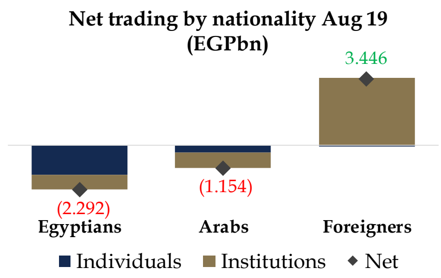
Note: Performance measured in EGP terms. Source: Bloomberg.

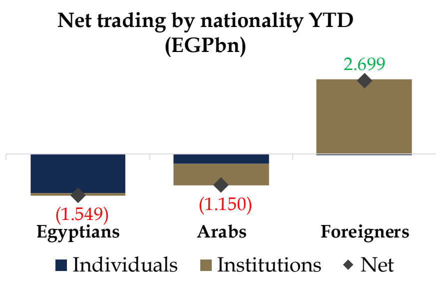
The daily performance of the market's 12 sectors relative to EGX 30 and EGX 30 CAP on a ytd basis



Source: Bloomberg, SHUAA Securities Egypt.

Investors by type





Source: EGX.

- **Egyptians** were <u>net sellers</u> with EGP2.29bn of net outflows in August (net outflows of EGP1.55bn ytd), driven by individuals.
- **Arabs** were <u>net sellers</u> with EGP1.15bn of net outflows (net outflows of EGP1.15bn ytd), led by institutions.
- **Foreigners** were <u>net buyers</u> with EGP3.45bn of net inflows (net inflows of EGP2.70bn ytd), dominated by institutions.

We note that the turnover figures in August account for the execution of GTHE's deals which amounted to EGP9.72bn.

Thursday, 1 August 2019

FWRY - Growth Potential When Under-penetration Meets Competition

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On Wednesday, we published a pre-IPO note on Fawry, setting our fair value for the stock at EGP4.86 (25% less than the IPO price). In *Today's Story*, we highlight the main points of our pre-IPO note. For more details about our valuation and the company's business model, please revert to our report.

- **The offering:** Fawry, the first fintech company in Egypt, is going public, probably setting the benchmark for other IPOs to come. This EGP1.6bn offering will mark a secondary sale of up to c.36% of Fawry's total shares, which will be sold by the current shareholders in proportion to their holdings. The IPO will take place in two tranches: 31% for institutions and 5% for retailers. With Fawry's shares count totaling c.707mn, the sale is priced at EGP6.46/share. As it stands today, Fawry is 99.9% owned by PSI Netherlands Holding which is a fully-owned subsidiary of Payment Solutions International (PSI). Meanwhile, PSI is owned by four strategic investors and other minority investors, including the management. Please see the pre- and post-IPO shareholder structure on the left. Of the institutional tranche, 21% of Fawry's total shares will be evenly offered to three strategic investors, namely National Bank of Egypt, Banque Misr, and Actis Direct investments. Meanwhile, another 10% will be offered in a private placement (which ends today), and the remaining 5% will be put up for public subscription (the retail tranche). After the IPO, the shareholding structure of the company is expected to turn from indirect into direct ownership.

- **We valued Fawry using two models as depicted in the right tables: (1) a transaction-based method (30% weight), (2) DCF (70% weight) in order to capture different narratives from the company's growth story. Using the weighted output of the aforementioned two valuation methods, we arrived at a fair value of EGP4.86 per a Fawry stock (25% below the IPO price). Considering the overall growth potential of the company, we think the IPO offers a relatively high premium when considered by long-term investors, something that also depends on how the company can capture its growth potential amid existing and emerging competition. Nonetheless, in view of the one-month stabilization fund allocated for the 5% retail tranche, we recommend subscribing thereto as subscribers can capture any upside following the flotation while limiting their downside to the IPO price.**

Summary of valuation

Method	FV	Weight	EGP/Share
Transaction based	6.20	30%	1.86
DCF	4.29	70%	3.01
		Weighted FV (EGP/share)	**4.86**
		Upside / (downside) vs. IPO price	(25%)

Source: SHUAA Securities Egypt.

Transaction-based method	
ResponsiAbility transaction valuation for 10% stake (USDmn)	19.5
ResponsiAbility transaction implied valuation for Fawry (USDmn)	195
FX rate	17.77
ResponsiAbility transaction implied valuation for Fawry (EGPmn)	**3,465**
2017's Earnings	51
Implied P/Ex	**68x**
Implied Price to POS	**46,819**
Equity valuation (P/Ex) @ 2018a earnings	3,848
Equity valuation (Price to POS) & 2018 POS count	4,916
Average equity valuation	**4,382**
NOS	707
FV/ share	**6.20**

DCF		2019	2020	2021	2022	2023	TV
	1.00	**0.81**	**0.67**	**0.56**	**0.47**	**0.40**	**0.40**
COE		**23.1%**	**21.7%**	**20.3%**	**18.9%**	**17.5%**	**15.6%**
Operating profit		77	105	135	168	209	
Net interest income		75	90	95	104	123	
Tax rate		-22.5%	-22.5%	-22.5%	-22.5%	-22.5%	
NOPAT		**118**	**151**	**178**	**210**	**257**	**278**
Allocations		(20)	(25)	(30)	(35)	(43)	
D&A		78	155	173	199	192	
Capex		(245)	(258)	(311)	(300)	(348)	
Change in working capital		269	195	200	198	245	
FCF		**200**	**218**	**211**	**272**	**303**	**4,331**
PV of FCF		162	146	117	127	121	1,721
Sum of PVs		**2,393**					
Cash (Q1 2019)		**643**					
Equity valuation		**3,037**					
NOS		707					
FV / share		**4.29**					

Monday, 5 August 2019

BoP Performance: Are Chronic Imbalances Resurfacing Already?

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The **Central Bank of Egypt (CBE)** has earlier released the results of the Balance of Payments (BoP) for the 9-month period July-March FY2018/19. The overall balance has reverted back to the negative territory, registering at a deficit of USD351mn, as a net result of a 39% surge in Current Account deficit (CAD) simultaneously with shrinking Financial Account (FA) inflows. We find figures disappointing to say the least, but not surprising. This reflects the "typical" imbalances that we had referred to in our note back in January 2019.

Please read the detailed report from this link, where we summarize our key observations on Egypt's external sector performance.

Tuesday, 6 August 2019

What IRAX's Acquisition of ESRS Facilities Mean for the Group

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The board of directors of Al-Ezz Dekheila Steel (IRAX), a 55%-owned subsidiary of Ezz Steel (ESRS), agreed to acquire 56% of Ezz Flat Steel (EFS) and 100% of Ezz Rolling Mills (ERM)—two moves that should leave IRAX a full owner of both companies and simplify ESRS's corporate structure. This takeover will be financed through a capital increase by IRAX of 13mn shares at EGP1,176.85 each (EGP100 par value + EGP1,076.85 capital surplus) or the fair value set by the independent financial advisor (IFA). IRAX's existing shareholders will be able to subscribe to 12.17mn of the 13mn-share rights issue, proportional to their respective holdings in IRAX.

- **What are the values set by the IFA for EFS and ERM, and what does it say about ESRS?** The IFA valued EFS at USD757mn or EGP12.47bn (based on the spot exchange rate of EGP16.48/USD and the IFA's fair value of USD10.09/share). Meanwhile, the IFA valued ERM at EGP2.07bn (EGP23.07/share). ESRS's direct ownerships in EFS and ERM are is c.47% and 99%, respectively. Using the IFA's fair values of IRAX, EFS and ERM, we calculate that the implied value of ESRS—based on its current ownership in each of the three subsidiaries, excluding **Ezz Steel Rebars (ESR)**—comes out as EGP30.38/share.
- **What is the impact of this corporate restructure on the companies' operational performance?** This acquisition should provide synergy, improve operational efficiency, and reflect better market sentiment for ESRS, as follows:
  1. EFS and ERM already reached their maturity phase and the acquisition cost is presently much lower than replacement cost. Thus, this would present a good opportunity for IRAX to expand.
  2. The consolidation of IRAX, EFS, and ERM will allow EFS and ERM to satisfy their working capital requirements through new debt facilities and will shield them against financial distress.
  3. This consolidation will also resolve many operational issues and allow ESRS to be more focused on its plans and strategies. It should improve the company's image since the operational KPIs will be enhanced.
- **How will the pre- and post-capital increase be structured?** The total values of the EFS and ERM equity stakes subject to the acquisition by IRAX is EGP9.06bn. If the acquisition is approved by IRAX's EGM, the value of the deal will show on IRAX's liabilities as payable until the capital increase takes place, after which the equity values will shift to the equity part of the balance sheet. The capital increase can take place under two scenarios – in our view:
  1. Under the **first scenario**, the full EGP15.3bn capital increase (13mn shares at an FV of EGP1,176.85/IRAX share) would be subscribed to by both IRAX's existing shareholders and the minority shareholders of EFS and ERM, proportionally. As ESRS owns c.55% of IRAX, it will subscribe proportionally through an effective share swap amounting to 6.65mn IRAX shares in return for its stakes in EFS and ERM. Meanwhile, the remaining shareholders of IRAX will be able to subscribe to 5.53mn shares of the rights issue, while the minorities of EFS and ERM will cover 0.82mn shares of the capital increase through an effective share swap. We calculate that this scenario would partially dilute ESRS's ownership in IRAX from 54.6% to 52.9%.
  2. Under the **second scenario**, ESRS and minority shareholders of EFS and ERM would participate in the subscription through am effective share swap as well, while the remaining IRAX shareholders would face a dilution risk if they do not participate in the capital increase. We calculate that this scenario would raise ESRS's ownership in IRAX to 66.9%.

We Note that the capital increase and the acquisition are still subject to IRAX's EGM approval. In this vein, we expect that the FRA will not allow ESRS to vote on this decision due to conflict of interest. We believe that while this proposed corporate restructuring would be more positive for ESRS as opposed to IRAX, the current conditions in the steel industry (as mentioned in our notes dated 9 July 2019 and before that date) would still be an overhang on the performance of ESRS.

Wednesday, 7 August 2019

CI Capital Q2 2019 Conference Call Highlights

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CI Capital Holding's (CICH) management held its Q2 2019 conference call last Wednesday, where they discussed the group results. Below, we highlight our main takeaways from the call.

- **Corplease impacted by a shift to EAS No. 49 on an FX hit: Corplease**, CICH's 87%-owned subsidiary, witnessed a change in accounting standards from No. 20 to a new No. 49 which is an equivalent application of IFRS 16. Under the new standard, Corplease will have to mark its portfolio by its end-of-period FX rate. With an appreciation in EGP witnessed during the first six months of the year, CICH took an EGP13mn hit in the form of FX losses in H1 2019, EGP10mn of which was recorded solely in Q2 2019. Also, EGP3mn of the aforementioned EGP13mn FX losses was related to holding company operations. The new accounting standard will remove depreciation on fixed leased assets as both revenue and cost items. Also, under the new standard, Corplease will not record fixed leased assets on its balance sheet. Instead, they will record debit balances related to lessees' account.
- **Reefy may be subject to a product offering revamp:** The microfinance vehicle, **Reefy**, CICH's 80%-owned subsidiary, witnessed a sequential drop of 6% in its bottom line, whereas its loan book grew 7% ytd. Slow loan book growth in H1 2019 was partially attributed to system maintenance which took place in Q4 2018 and Q1 2019. However, loan book growth came at 5% in Q2 2019 (still considered slow in our view) due to a delay in opening some six branches during the quarter. Management said they will revisit their growth projection for Reefy, which was previously targeted at 30% annually. Management thinks that rising competition is another reason for subpar growth, hence the need to revamp Reefy's product offerings.
- **Investment bank remained sluggish on weak market activities:** Investment bank revenues fell to EGP93mn (-30% y/y). Brokerage as well as investment banking operations happened to be mostly responsible for the slump. Only asset management figures showed signs of improving. Management attributed the drift in its IB segment to weak market activities, particularly trading volume. Also, some of the deals to be executed by the investment banking division saw some delays and are expected to be finalized by Q3 2019.
- **2019 targets maintained by management:** Q2 2019 annualized ROAE fell below 20%, recording 17%. Management believes that a target ROE in the low 20s% is still valid and that the slippage is due to a significant one-off (i.e. FX) during the quarter. Meanwhile, management targets a bottom line after minority in c.EGP550mn, implying an annual growth rate of 29%.
- **Valuation:** In respect with management guidance, CICH trades at a forward P/E of 7.7x, while trades at current P/B of 1.75x. In our view, CICH's current multiples could signal cheap valuation levels in the event of: (1) maintaining a leading position within the leasing market, (2) successful navigation to Reefy's growth prospects, and (3) a flourishing local equity market for potential fruitful spillover on IB operations.

Thursday, 8 August 2019

Egypt's Water Conservation Plan Reinforces the Potential for ORAS and SWDY

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- In *The Daily Beam* issue published on 18 June 2019, we have highlighted the potential opportunity for both **Orascom Construction** (ORAS) and **Elsewedy Electric** (SWDY) to benefit from the **Egyptian** governmnet's focus on water treatment and desalination in the near future in a story titled *"The Shape of Water" in Egypt – An Opportunity for ORAS and SWDY?"* On 5 August 2019, the **Ministry of Housing** unveiled fresh details of its water conservation plan which includes the following:

Egypt's water conservation plan

Segment	No.	Details	Capacity	Notes	Cost
Water desalination	23	Matrouh, Red Sea, North Sinai, South Sinai, Port Said and Dakahlia	734k cbm/day	Under construction	EGP15.968bn
	16	Matrouh, Red Sea, North Sinai, South Sinai and Kafr El Sheikh	671k cbm/day	Planned	EGP13.327bn
	58	North Sinai, South Sinai, Red Sea. Matrouh and Ismailia	440k cbm/day	Constructed	
Water treatment	26	Upper Egypt		Constructed	
	26	Upper Egypt		Under construction - done by end of 2019	
	5	Upper Egypt		To be upgraded by December 2019	
	3	Upper Egypt		To be upgraded	
District Metering Areas	105	16 different governrates		Done	
	2,878k cbm/day			To be saved by reducing water waste from 30% to 20%	
Water meters	30%			remaiang targeted subscribers	
	1.4mn	Water meters		Supplied by end of 2019	
	245k	Prepaid-water meters		Supplied by end of 2019	
	40k	Bulk water meters		Supplied by end of 2019	
Irrigation using waste water	3,000 feddans	New Beni Sueif city		In-cooperation with Egypt kuwait Holding	
	3,000 feddans	El Sadat city			
	6,000 feddans	New El minya			
	1,000 feddans	Samalout			

Source: Youm7.

- **The need and potential for wastewater treatment is real:** A step closer to finalizing the water conservation plan offers some comfort at a time where several reports about water stress in Egypt are seeping out. The **World Resource Institute (WRI)** ranked Egypt 43rd out of 164 countries in terms of water stress, classifying it as a "high base line water stress" country. In July, the **Ministry of Irrigation & Water Resources** announced a nationwide "state of emergency" due to a 5bn cbm fall in Egypt's share of Nile water in 2019 as the rainfall on upstream countries of the Nile river basin declined. This is besides the **United Nations**' classification of **Egypt** among the 22 most water-stressed countries in **Africa** and the **Middle East**, as alluded to in the aforementioned June story. That said, according to the WRI, 82% of waste water in MENA is left unused. On the other hand, 84% of wastewater is treated in the GCC countries, with 44% reused. This points to the potential in MENA for further expansion into water treatment, with both Egyptian and foreign companies eyeing the sector in Egypt.

- **Government moves that fed into Egypt's water conservation plan as it stands today:**

1) In March, the **Minister of Irrigation & Water Resources** presented a USD50bn plan to combat water scarcity during 2017-2037.
2) In June, the **Arab Organization for Industrialization (AOI)** signed an MOU with **South Korea**-based membrane manufacturer **SepraTek** to help enhance **Egypt**'s national production in the field of water desalination. The two sides discussed establishing a factory for manufacturing membranes for water desalination by January 2020.
3) In July, **UAE**-based wastewater manager **Metito** said it will establish an EGP1.6bn water desalination plant in **El-Arish** with a capacity of 100,000 cbm/day. The project will be constructed in cooperation with ORAS and is slated for completion in 2021, according to Metito's CEO Karim Medour.
4) In July, the Egyptian government said it was planning to begin negotiations in August with several companies to construct desalination plants to treat 150,000 cbm/day under a PPP framework. The companies include **Spain**'s **Aqualia**, **France**'s **Schneider Electric**, **Switzerland**'s **Aqua Swiss**, and **Metito**.

- **The broader and longer project frameworks open the window of opportunity for ORAS and SWDY even wider:** We reaffirm that the Egyptian government's focus on water projects (e.g. water desalination, treatement, reducing water waste, and network upgrades) bodes well for **Orascom Construction** (ORAS) and, potentially, **Elsewedy Electric** (SWDY) if it taps into the segment as part of its turnkey porjects. A good clue supporting our view is the USD739mn water treatment plant that ORAS recently added to its backlog in May 2019 which represented 79% and 53% of its new awards in Q2 2019 (USD935mn) and H1 2019 (USD1.4bn). In addition to being involved in water desalination and treatment plants, ORAS can benefit from selling pipelines to upgrade/expand Egypt's water network. **We note that both ORAS and SWDY, already part of our EGX Model Portfolio, are considered cheap, trading at forward P/E of 4x and 6x, respectively.**

Wednesday, 14 August 2019

ETEL – Still Cheap Despite Its One-Off Q2 2019

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Telecom Egypt (ETEL) reported a mixed set of results for Q2 2019, where reported earnings plunged 60% y/y, hit by a one-off item related to the company's early retirement program (ERP). Total revenues grew substantially by 24% y/y, while adjusted EBITDA edged down 3% y/y. ETEL is currently trading at a cheap 7x TTM earnings, even after the drop in earnings.

- **Earnings dropped on ERP expenses:** ETEL's earnings fell 60% y/y to EGP515.6mn, pressured by expenses of EGP1bn arisen by the company's ERP during Q2 2019. Investment income from VFE decreased 19% y/y to EGP477.8mn, bending the earnings curve downwards even tighter. Investment income from VFE shrank over loans taken by the company to finance part of its EGP12.2bn cash dividends, which left it with more interest expense and less earnings. On the other hand, ETEL's FX gains of EGP416.3mn still offset the ERP expenses and the decline in investment income from VFE, albeit slightly. Adjusted earnings (i.e. ERP expenses and FX gains) would have shown a less intense drop of c.15% y/y to EGP1.1bn.

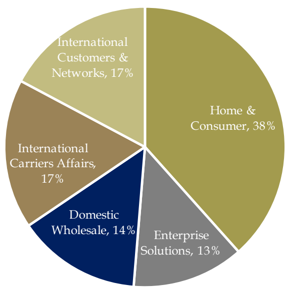
Results summary

EGPmn	Q2 2019	Q2 2018	y/y	Q1 2019	q/q
Home & Consumer	2,539	1,935	31%	2,401	6%
Enterprise Solutions	851	629	35%	750	13%
Domestic Wholesale	941	1,085	-13%	1,309	-28%
International Carriers Affairs	1,141	1,140	0%	1,128	1%
International Customers & Networks	1,137	554	105%	498	128%
Total Revenues	**6,609**	**5,343**	24%	**6,087**	9%
EBITDA	**735**	**1,787**	-59%	**1,903**	-61%
Net Income	**516**	**1,284**	-60%	**1,615**	-68%
EBITDA Margin	11%	33%	-22 ppts	31%	-20 ppts
Net Margin	8%	24%	-16 ppts	27%	-19 ppts

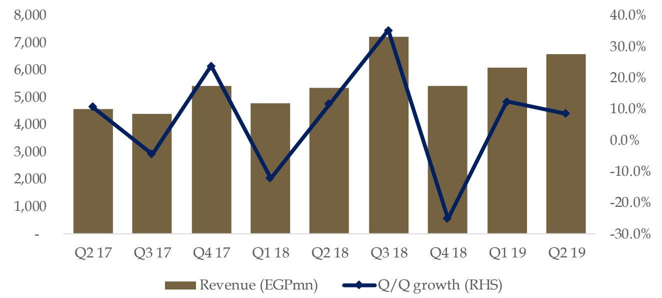
Source: Company reports.

- **Revenues were boosted by home & consumer and IC&N segments:** ETEL achieved revenue growth of 24% y/y to EGP6.6bn in Q2 2019. This growth in revenue is owed to (1) the home & consumer segment which yielded 31% larger revenues to EGP2.5bn in Q2 2019 (contributing 38% to total revenues), bolstered by data; and (2) the international customers & networks (IC&N) segment which produced 105% more revenues y/y to EGP1.1bn in Q2 2019 (contributing 17% to total revenues), propelled up by two cable projects, one of which is the PEACE cable contract that ETEL has signed in April. Domestic wholesale revenues fell 13% y/y to EGP0.9bn. Meanwhile, the number of mobile subscribers in ETEL grew 29% y/y to 4.3mn but remained flat sequentially as ETEL excluded inactive subscribers in calculating its mobile subscribers.
- **Adjusted EBITDA edged slightly down during Q2 2019:** Adjusted EBITDA (i.e. excluding ERP expenses) declined slightly by 3% y/y to EGP1.7bn, reflecting an EBITDA margin of 26%. The company attributed this slide to absent IRU sales domestically as well as lower revenue margin of one of the two cable projects.
- **Our take:** We like the decent revenue growth that ETEL has generated during Q2 2019. The drop in adjusted EBITDA was not severe—in our view—and could be taken care of in subsequent quarters. Moreover, ERP should bode well for ETEL in the future. On the flip side, our main concerns are (1) the drop in investment income from VFE, but ETEL's management said, in this respect, it expects a recovery by next year; and (2) possible FX losses if the EGP depreciates against the USD. Lastly, we remind our readers that ETEL has been part of our ***EGX Model Portfolio*** from the start. Our latest valuation for the stock was EGP18.6/share (+29% upside).

Revenue contribution by segment in Q2 2019



Revenue quarterly growth



Note: Home & Consumer and Enterprise Solutions are classified as Retail. Domestic Wholesale, Int. Carriers Affairs and Int. Customers & Networks are classified as Wholesale.
Source: Company reports.

Thursday, 15 August 2019

Berth-55 Project: What's in It for ALCN?

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The Holding Company for Maritime & Land Transport's (HCMLT) BoD recently approved transferring 13% of its 33% stake in the Egyptian Group for Multipurpose Terminals (EGMT) which is to own/develop eight berths (55-62) in Alexandria's port, to Alexandria Containers & Cargo Handling Company (ALCN), noting that EGMT's authorized capital is EGP500mn. Post this move, Alexandria Port Authority, Suez Canal Authority, and HCMLT will hold respective stakes of 34%, 33%, and 20% in EGMT, in addition to ALCN's 13% stake. We note that HCMLT and APA own stakes of c.55% and c.40% in ALCN, respectively.

- **Berth-55 Project – How did it all start?** Back in 2004, HCMLT had prepared a study suggesting **Alexandria Port Authority (APA)** will reach full utilization by the end of FY2015/16. Accordingly, two terminal expansion projects were proposed: *Berth 100* in **El-Dehkeila**'s port and *Berth 55* in **Alexandria**'s port. Discussions between the different stakeholders about the two projects had been taking place intermittently over the years. Execution of the Berth-100 project was recently ruled out indefinitely as **Alexandria International Containers Terminal (AICT)**, one of the two companies operating in APA, was found entitled to file an international claim against APA for breaching their initial agreement, which gives AICT the right to develop Berth 100. In 2015, the Berth-55 project was discussed at the *Egypt Economic Development Conference (EEDC),* despite the fact that APA's utilization was merely 65% in FY2016/17 (with the Alexandria and El-Dekheila's ports reaching respective utilization rates of 72% and 60%). Furthermore, our rough calculations show that APA could not reach full utilization even by FY2022/23. However, the Berth-55 project could increase the attractiveness of Alexandria's port for transit containers, given its proposed 17m depth, especially if port and handling fees were alluring enough compared to other regional ports, such as those of **Malta**, **Cyprus**, **Ashdod**, and **Istanbul**.

- **How big is EGMT?** According to the publicly-available data, EGMT's terminals are almost the same size as ALCN's Alexandria and El-Dekheila terminals combined. According to the **Minister of Transport** Kamel El-Wazeer, Berth 55 should be developed in two years starting 2019. However, in longer scenarios, it could take up to 5-8 years. In this vein, it had taken AICT four years to develop its berths which are even smaller than the proposed Berth-55 project.

Specifications of Berth 55 vs. ALCN's Alexandria and El-Dekheila terminals

	Berth 55	ALCN		
		Alexandria	El-Dekheila	Total ALCN
Area (sqm)	**560,000**	163,000	406,000	**569,000**
Length (m)	**2,480**	531	1,040	**1,571**
Depth (m)	**17**	12	12 to 14	**12 to 14**
Storage capacity (TEU)	**N/A**	15,500	27,000	**42,500**
Handling (mn tons/year)	**15-18**			
Containers	**1,250,000**			**1,500,000**
Serves …	**Up to 6 vessels at a time**	Up to 3 vessels at a time	Up to 3 vessels at a time	**Up to 6 vessels at a time**
Cost (USDmn)	**550**	N/A	N/A	**N/A**

Source: Media reports, ALCN.

- **EGMT – a competitor or a partner; which is better for ALCN?** Before ALCN's 13% takeover was approved by the seller, we had viewed the overall impact of the Berth-55 project on ALCN as neutral to negative. On one hand, given that Berth 55 mainly targets transit containers, the project would have little to no effect on ALCN's Alexandria terminal, save for that import-export containerships may abandon EGMT due to the crowdedness of Alexandria port terminals. On the other hand, the project threatens ALCN's El-Dekheila terminal and the company's ongoing efforts (i.e. deepening Berth 96 to 16m) to attract transit containerships. Nonetheless, this threat is a bit deterred by Alexandria Port being already more crowded than El-Dekheila Port. Although it is too early to judge whether a 13% stake in EGMT would be enough to offset any possible market share cannibalization for ALCN, it would probably minimize the negative impact, if any. Anecdotally, there was a similar case with **East** and **West Port Said** ports; West Port Said was mainly serving import-export containers in addition to transit containers. Later on, the East Port Said port was established with deeper berths. Ultimately, the West Port Said port ended up specializing in import-export containers, while East Port Said specialized in transit containers (ALCN presumably being in West Port Said's shoes and EGMT in East Port Said's in these scenarios). **We note that ALCN is currently trading at a forward P/E of 8.6x, a discount to its historical levels of 10.2x in 2018 and 11.7x in 2017.**

Sunday, 18 August 2019

Cheaper Materials Can Improve Metal Makers' H2 2019 Price Spread

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Prices of alumina and iron ore, the main raw materials used by metal producers, began to decline in August, weaving a pattern that will favor aluminum and fully-integrated steel producers in H2 2019.

When it comes to aluminum producers:

- **Australian** alumina benchmark sunk to a year-low of USD299/ton early in August. We had expected this dive in alumina prices in our initiation of coverage for **Egypt Aluminum** (EGAL) published on 17 March 2019. The return of offline capacities to the market (**UC Rusal** and **Alunorte-Brazil**) triggered the price drag for the most part.
- The current spot prices reflect aluminum-alumina cash spread of USD1,198/aluminum ton, higher than our estimates (SSEe) of USD1,184/aluminum ton in FY2019/20 and an average cash spread of USD1,086/aluminum ton in FY2018/19. Also, the ratio of alumina vs. aluminum on a price-per-ton basis stands at 16.9% based on the current prices compared to 18.6% in SSEe in FY2019/20 and 22.4% in FY2018/19 on average. (Note: EGAL's future contract allows them to secure alumina at 20.86% of aluminum price.) ***If the current (alumina/aluminum) price ratio persists, EGAL will enjoy higher-than-expected margins during Q1 FY2019/20, and operating cash flows will be enhanced due to lower working capital requirements.***
- A key risk for EGAL's performance is further EGP appreciation weighing on its operating margins and hence value. In Q4 FY2018/19, EGAL margins have been pressured—as expected—due to low aluminum base prices and a stronger EGP. As for now, we await the release of full financials and data breakdown to update our financial model. **We note that our latest rating of EGAL is Neutral / High Risk with a 12M PT of EGP15.8/share.**

When it comes to steel producers:

- The iron ore–62% benchmark slumped 22% to USD91.3/ton in the last couple of weeks which is positive for integrated steel producers, such as **Ezz Steel** (ESRS) and its 55%-owned subsidiary **Ezz Al-Dekheila Steel** (IRAX). Meanwhile, local steel prices stabilized at EGP10,430/ton (USD631/ton) but upside risk remains if the **Administrative Judiciary** decides to reinstate the safeguard measures imposed by the **Ministry of Trade & Industry** on steel billets. Furthermore, a decision by the **Central Bank of Egypt**'s **Monetary Policy Committee** to cut interest rates this coming Thursday would be another catalyst for the performance of ESRS and IRAX.
- As for ESRS, we look forward to IRAX's EGM decision concerning its capital increase and its acquisition of **Ezz Flat Steel (EFS)** and **Ezz Rolling Mills (ERM)**. We believe a favorable decision by IRAX's EGM approving this corporate restructure would be more beneficial for ESRS as opposed to IRAX.

Monday, 19 August 2019

Does 'Sell in May and Go Away' Translate to 'Buy in August' in Egypt?

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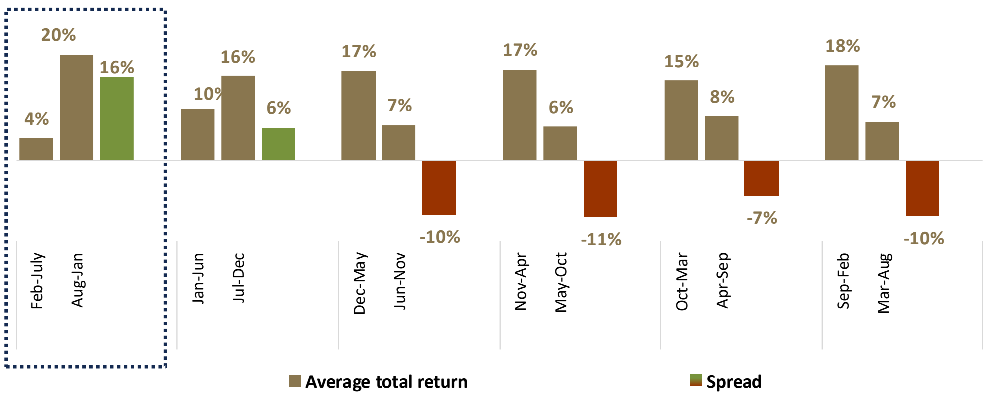
In *Today's Story*, we are re-examining the US equity market's oft-cited adage "sell in May and go away" — sometimes dubbed the Halloween indicator. It presumes that investors are better off selling their positions in May and holding the proceeds in cash before turning buyers in the fall, capitalizing on the high returns of the winter months. We tested this phenomenon against the Egyptian equity market using the average total return of the EGX 30 index in the trailing half of each of the past 21 years compared to the other half of each year (e.g. August-January vs. February-July or July-December vs. January-June).

- **Egypt would say "sell in February and buy in August":** The US equity market's well-worn adage "sell in May and go away" is seen taking effect in different months in Egypt. If translated in local practice, the investing principle would be more like "sell in February then buy in August." The below chart illustrates that the EGX 30 index in the past 21 years tended to produce the highest average returns (+20%) in the August-January period and the lowest returns (+4%) in the February-July period, marking the widest spread between investors who may have employed the subject strategy to their local timing and the rest of their peers. Meanwhile, when we compare the returns of the other trailing halves, we noticed a lower spread (in the half that starts in July vs. the other half that starts in January) or even a negative spread (in the halves that start in March, April, May, and June vs. the other halves that start in September, October, November, and December) to the returns achieved in the other half of the year.

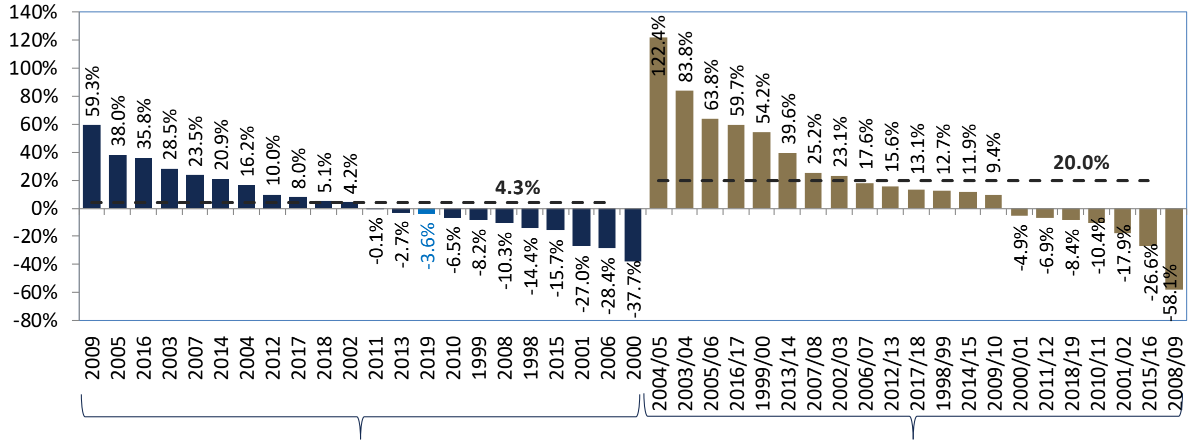
The two halves' EGX 30 performance of the last 21 years



Source: Bloomberg, SHUAA Securities Egypt.

- **EGX 30 saw a hike in returns in the August-January period:** As the below chart shows, the EGX 30's total return in each August-January period has so far averaged +20.0% versus +4.3% in each February-July period during the past 21 years. In the August-January period, the EGX 30 generated positive returns 66.7% of the time vs. only 50.0% in the February-July period. In 2016, when the EGP was floated, we encountered the same phenomenon, where the August-January period was more lucrative than the February-July period. Excluding 2016, we find that a "buy in August" strategy still emerges in Egypt as the axiom that mirrors that Halloween effect. Meanwhile, this phenomenon did not hold good in 2018 when the market peaked in the first half of the year (February-July) with the EGX 30 hitting an all-time high of 18,414.11 on 29 April, while the second half of the year (August 2018-January 2019) trended dramatically down. Again, if we exclude 2018, the phenomenon, in its "buy in August" translation, would be observable. August 2019 is the latest example, where EGX 30 hit the green zone so far in seven sessions out of nine, which can be traced to the subject translation of the phenomenon, suggesting it may have started to take its effect in Egypt in the first half of August. Historically, perusing a "buy in August" strategy has been somewhat proven to be a shrewd advice when comparing to the returns of the other half of the year (i.e. February-July).

EGX 30 total return in EGP terms



	February to July	August to January
Average	4.3%	20.0%
Median	2.1%	13.1%
% Positive	50.0%	66.7%

Source: Bloomberg, SHUAA Securities Egypt.

- **Now that it is interpreted for Egypt, what to buy to leverage this phenomenon?** One of the decisions that usually revives the market is an interest rate cut by the **Central Bank of Egypt**. With high expectations of a 100bps cut by economists in the coming meeting scheduled for 22 August on the back of favorable inflation readings, we see a high probability that highly-leveraged names may outperform the rest of the market. In this vein, we can name **PHDC**, **ESRS**, **HELI**, **ORHD**, **AUTO**, **DOMT**, **MCQE**, and **SCEM** as the top beneficiaries from any rate cut. These names are part of a longer list, including **OIH**, **HRHO**, **SRWA**, **ISPH**, **CICH**, and **ATLC**, that should benefit from any rate cut due to the dynamics of their business model.

Tuesday, 20 August 2019

How Will the EGX 30 Fare If the CBE Cut Rates This Thursday?

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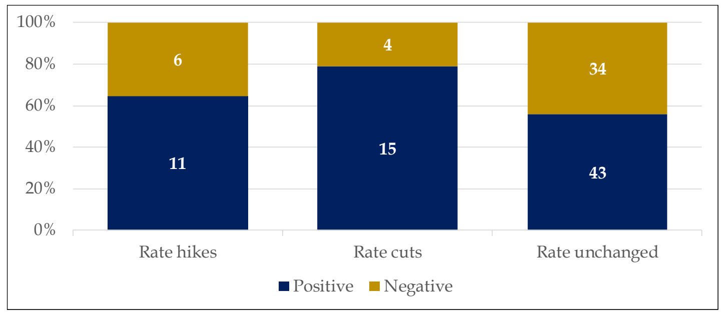
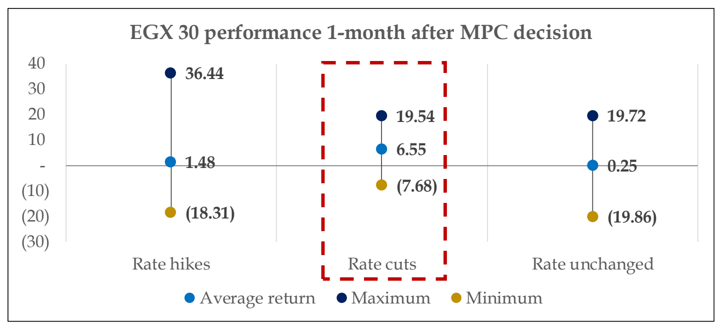
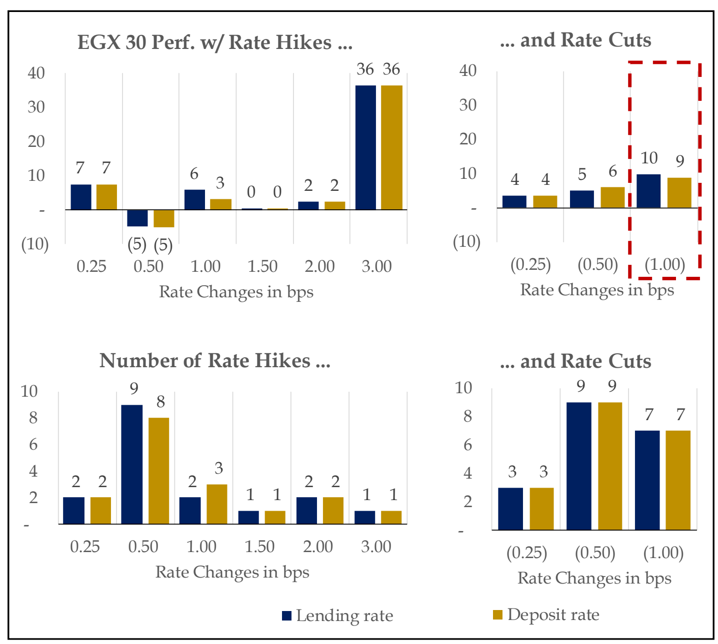
- **Revisiting our one-year-old analysis:** Once again, we look at the historical performance of EGX 30 one month after each interest rate decision, be it a hike, a rate cut, or no change. We had looked at this analysis almost a year ago (30 September 2018) after the **Central Bank of Egypt (CBE)** had kickstarted its easing cycle in February 2018. Market participants usually keep a close eye on interest rate decisions because conventional wisdom says that higher interest rates are bad for stocks and lower interest rates are good for stocks. But as we found out, this is not always the case because interest rate alone is not the only factor impacting stock market performance. Higher interest rates mean higher required rates of return and a lower present value of companies' cash flows and hence valuation. Therefore, higher interest rates are generally negative for the stock market. Below and to the right, we analyze the EGX 30 index performance over the years to gauge how it fared one month after each interest rate decision by the CBE.
- **Our findings:** Over the last 14 years and one month, 113 rate decisions have been made by the CBE. Rates have changed 36 times with 17 hikes, 19 cuts, and 77 "no change" decisions. On average, EGX 30 performance has always been positive one month after the decision to differing degrees:
  - In the **17 times (65% of the time) rates were hiked up**, EGX 30 averaged **a positive return of 1.48%.**
  - In the **19 times (79% of the time) rates were cut**, EGX 30 averaged **a positive return of 6.55%** (first dotted box to the right).
  - In the **77 times (56% of the time) rates were left unchanged**, EGX 30 averaged **a positive return of 0.25%.**
- **Conclusion:** With the MPC highly expected by economists to cut interest rates by 100bps in its coming meeting scheduled for Thursday, 22 August 2019 on the back of favorable inflation readings, and based on history, **there is a 79% chance that the EGX 30 will be positive one month from that meeting.** If history is any guide, after a 100bps rate cut, EGX 30 performance **averaged a positive return of 9-10% one month later** (second dotted box to the right).

EGX 30 1-month performance post each interest rate decision







Source: SHUAA Securities Egypt.

Wednesday, 21 August 2019

Insights into Cairo's Office Property Market

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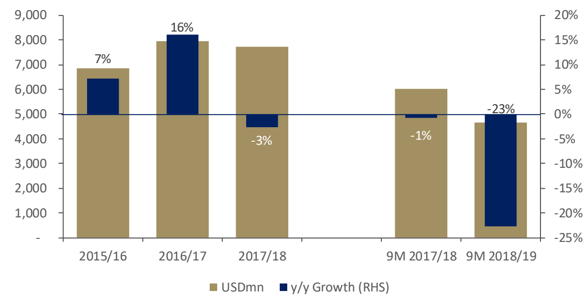
- **A wave of launches breaking on the office market:** Cairo's commercial office segment has been publicized as the money spinner of the real estate sector, due to the segment's big sales values and tendency to remain stable during market swirls. Hence, many property developers resorted to launching business parks that include grade A offices. According to a recent report by real estate services provider *Savills*, demand for offices is driven by needs for relocation and expansion.
- **Are there external incentives for buying a commercial property?** an office market is usually promising when foreign investments expand, as the bulk of demand for quality office spaces is dominated by multinationals. The current macro-economic environment in Egypt, as positive as it may seem, has not been enough to attract large new foreign direct investments (FDIs). While lower headline inflation, solid PMI figures, and an announcement of a flexible investment framework should enhance Egypt's investment appeal, current competition from state-owned players in various industries is likely a source of concern to any foreign investor. This is in addition to already-declining FDIs globally over economic uncertainty arising from trade tensions.

FDIs



Source: CBE.

- **Where is interest detected?** Consumer interest is easily detected in the eastern region of Cairo where grade A stock can be found, and where vacancies are declining. The additional airport capacity is expected to spur further demand as the government plans to introduce the new Katameya/Capital International Airport that will serve the New Administrative Capital. Meanwhile, at the other end of Cairo, vacancies are high, but more activity is expected as the new Sphinx International Airport should be fully operational by 2020. Also, the Grand Egyptian Museum will be completed around the same time. In the same vein, several heavily-branded launches in the area are taking place, namely those of *Golf Central* in Palm Hills October, *Capital Business Park* and *Zed* in Sheikh Zayed.

- **The occupiers' profile:** Demand, for relocation or expansion purposes, was initially generated by sectors such as banking, technology, FMCG, and online services. A *Savills* research indicates that most of the transactions are closed by existing occupiers, while demand from new market entrants is still limited. This pattern is expected to continue under the current uncertainty prevailing the local and global markets.

- **So, which companies are making the noise in the office market right now? Talaat Moustafa Group Holding** (TMGH) does not currently have any exposure to the office market, but their latest strategy is focused on recurring income activities. **Orascom Development Egypt**'s (ORHD) exposure to the office market is also minimal – all concentrated in El-Gouna, but the company plans to launch *O West*'s commercial component by September. **Palm Hills Developments** (PHDC) and **Madinet Nasr Housing & Development** (MNHD) recently made their first moves in the office market, with the release of *Golf Central* and *Cobalt Business District*. **Sixth of October Development & Investment Co. "SODIC"** (OCDI) carries a good reputation as an office property developer with *The Polygon* in Sheikh Zayed and another project in EDNC in east Cairo.

Thursday, 22 August 2019

No Need to Hit the Snooze Button; 6 Reasons to Expect a Rate Cut Today

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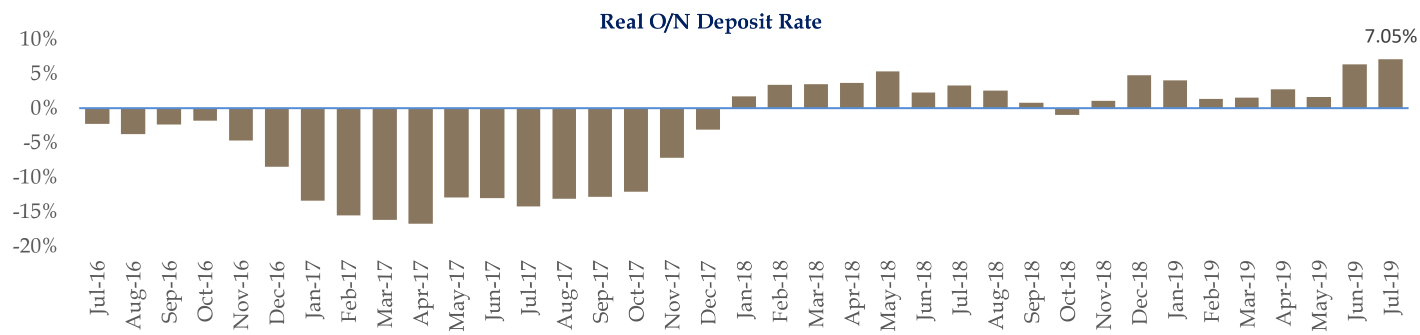
Once again, all eyes are on the CBE's Monetary Policy Committee meeting scheduled for today. First things first, we believe the scene is exceptionally suitable for resuming the easing cycle with a 100bps cut. Our case for this forecast is set out in *Today's Story*.

1. **Headline and core inflation rates are at four-year lows:** Despite the implementation of fiscal reform measures early July, urban headline and core inflation rates retreated to 8.7% and 5.9%, respectively. Furthermore, we see no need to wait for another inflation reading, because even if inflation in August goes up, it would be for seasonal reasons, i.e. Eid al-Adha which might produce an increase in the price of meat (a core food item). In the same context, the impact of the recent increase in cigarette prices on the overall index will be marginal, due to the trivial weight assigned to the item (2% of the whole index).
2. **All this leaves a vast room for cutting rates without hurting the objective, a tight real interest rate:** Again, even if August inflation readings were higher than those recorded in July, we think the real positive deposit rate, being at around 7%, is enough for a reasonable cut of 100bps with no worries.
3. **Global monetary easing in advanced and emerging countries:** We believe that recent global developments pave the way for CBE to resume the easing cycle such as the **Fed**'s cut, a signaled potential cut by the **ECB**, **New Zealand**'s cut, and other cuts by emerging markets (EMs), including **Turkey** and **India** just to name a few. Rate cuts already taking place in EMs in specific shield the competitiveness of Treasuries in Egypt should it cut rates itself.
4. **Let's not forget oil prices:** Speaking of global factors, global easing, along with current oil prices hovering around early USD60's a barrel, risks to domestic prices are tamed.
5. **Time to spur private sector-led growth:** The ugly side of recent global developments (i.e. trade tensions and slowing growth) stresses the need for promoting private investments to maintain a much-needed high growth rate. In other words, at the current global stance, Egypt's economy cannot count much on FDIs, as global protective measures have hit capital flows hard. Therefore, continuous normalization of interest rates is imperative.
6. **We definitely do not overlook Suez Canal investment certificates:** Some EGP60bn is expected to be paid back to holders of the Suez Canal investment certificates early September, which may make the CBE reluctant to cut rates soon in fear of high inflation. However, we do not think this poses a high risk to inflation as we believe the greatest portion of the withdrawn funds will be reinvested in bank deposits at the highest rates possible. Let us recall here that in 2014, when inflation rate averaged around 10%, the certificates were issued with a 12% interest rate which was quite appealing to a wide range of the household sector. Therefore, we believe a 100bps rate cut will not curb this sector's propensity to save and reinvest their maturing certificates at the then-market rates.

In view of the above factors, we see the overall picture conducive to a rate cut. Confirming the easing trend is essential to spur private investment, which we believe is the main and most important way to weather the global turmoil. Global and domestic factors suggest no need to hit the snooze button again today on interest rate normalization—a situation that serves the overall economy.



Source: CBE.

Sunday, 25 August 2019

What Does the Recent Interest Rate Cut Mean for the Market?

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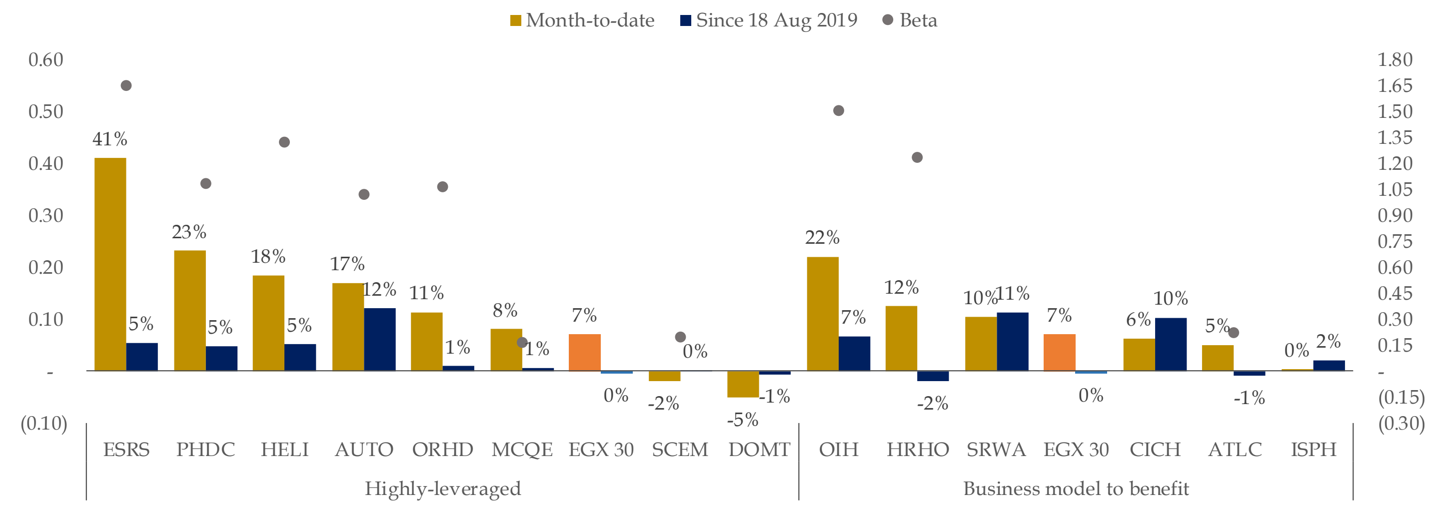
- **A rate cut is now a fact, albeit higher than expected:** It is now confirmed; that the CBE has resumed its easing cycle in line with our expectations. We had expected that the CBE will likely cut interest rates in 2019 by a cumulative 300bps, of which 100bps took place in February 2019 and another 150bps last Thursday. This means we could potentially see another 50-100bps move by end of year, depending on inflation readings and expectations as clearly spelled out in the MPC statement.

- **Short term positive but could be muted:** The latest 150bps rate cut was above our expectation of a 100bps cut which also coincided with market consensus. The question now is what this means for the market in general and for the stocks in specific. As for the market, the EGX 30 has recently been pricing in the 100bps rate cut more than in any prior CBE decisions. Thus, the fact that the rate cut was larger than expected may help push the market higher over the coming couple of days. However, with global markets tumbling last Friday, the upward move in the EGX 30 could be muted.

- **Long term positive:** While the larger-than-expected rate cut bodes well for the market overall, it is not yet large enough to trigger a full-blown investment/capex cycle. In other words, it is a move in the right direction, but companies will not necessarily press the "invest" or "borrow" buttons immediately. But don't get it wrong; the rate cut is much needed for signaling purposes. The CBE is basically sending the market a message that it is now less concerned with tamed inflation rates and more focused on growth.

- **Who's to benefit?** As we mentioned before in *The Daily Beam* published on 19 August 2019, we believe highly leveraged companies and those with business models benefitting from a low-interest rate environment will likely outperform the rest of the market. For the former group, we had picked **PHDC**, **ESRS**, **HELI**, **ORHD**, **AUTO**, **DOMT**, **MCQE**, and **SCEM**. For the latter group, we had picked **OIH**, **HRHO**, **SRWA**, **ISPH**, **CICH**, and **ATLC**. We note that both groups have outperformed the EGX 30 since the beginning of August and since our published note mentioned above.

Stock performance vs. beta for stocks set to benefit off lower interest rates



Average performance	Month-to-date	Since 18 Aug 2019
EGX 30	7.0%	(0.5%)
Highly-leveraged	13.9%	3.5%
Business model to benefit	9.4%	4.5%

Source: Investing.com.

Monday, 26 August 2019

Key Themes Dominating Banks' Financials in H1 2019

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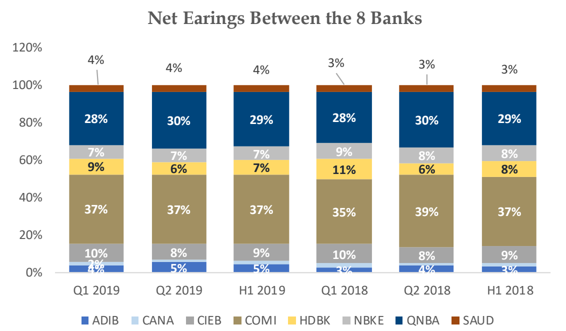
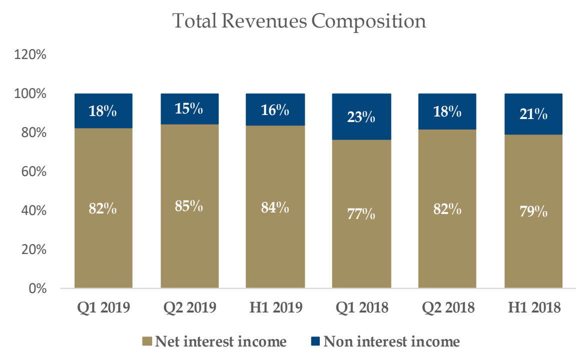
With Q2 2019 earnings season approaching its end, many EGX-listed banks have already reported their H1 2019 results. In *Today's Story*, we highlight the dominant themes that ran through the income statements of eight EGX-listed banks, namely ADIB, CANA, CIEB, COMI, HDBK, NBKE, QNBA, and SAUD. Combined, these eight banks generated EGP14.43bn in earnings in H1 2019 (+21% y/y), with net interest income (NII) hitting EGP24.31bn (+24% y/y) and revenues totaling EGP29.07bn (+18% y/y).

- **Solid annual growth in net interest income:** The eight EGX-listed banks grew their combined NII to EGP24.31bn in H1 2019 (+24% y/y). Higher income was fostered by a set of factors, including some price leaps and volume-induced growth on a ytd basis. Although H1 2018 has counted 200bps in rate cuts vs. 100bps in H1 2019, we have seen funding costs for the respective banks growing by some 13% y/y, whereas interest income growth hit 18%—on average. This is primarily a product of the retroactive application of the new tax treatment, which pushed banks to rack up Treasury investments within H2 2018 at high yields. The effect of such Treasury acquisitions on interest income reflected on H1 2019 interest income. On the other hand, the rate cut last February helped contain growth of funding costs.



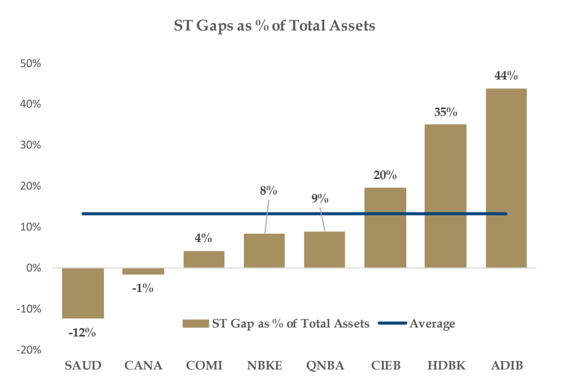
Source: Company reports.

- **Non-interest income lagged:** Contrary to interest income, the non-interest portion of revenues lagged notably for the eight banks, with fees and commissions income retreating 4.5% y/y to EGP3.28bn in H1 2019. Meanwhile, total non-interest income fell 7% y/y to EGP4.76bn, representing only 16% of revenues. Weaker demand, coupled with thinner margins on credit fees products, caused the revenue drag.



Source: Company reports.

- **Poor sequential growth with deterioration in efficiency:** Despite strong annual growth in profitability, quarterly growth was rather flattish. H1 2019 earnings hit EGP14.43bn (+21% y/y), whereas Q2 2019 earnings stood at EGP7.28bn (+18% y/y, +2% q/q). Sequential growth was weakened by (1) slow growth in interest income, (2) smaller non-interest income, and (3) higher opex which led to a higher cost-to-income ratio. In H1 2019, the eight banks' cost-to-income ratios rose to 29.8% from 26.8% a year ago. Efficiency was impaired by weaker non-interest income as well, coupled with higher G&A expenses. The increase in opex is to a larger extent the work of COMI, as the bank accrued expenses in some accounts as was the case in Q1 2019.



Source: Company reports.

- **Lower credit losses on IFRS9 application and a lower effective tax rate:** Provision for credit losses in H1 2019 declined by as much as 49% y/y to EGP997mn, coinciding with the application of IFRS9, due to massive provisions reversal by some banks. It seems like the readiness efforts for IFRS9 have kicked off early (before and through 2018), creating a high base for 2019. On a different note, while 2019 was projected to see a hike in banks' effective tax rate on the back of the new tax regime application, the effective tax rate actually decreased by 21bps in H1 2019. However, it was not really a surprise since the application took place retroactively, with banks slowing down their Treasury purchases notably during H1 2019, amid relatively higher lending activities.

- **What's next after the recent rate cut?** With last Thursday's 150bps cut, rates have so far been cut by 250bps ytd. This is surely to affect banks' NIMs in H2 2019. The above chart to the right summarizes the short-term repricing gaps (up to one year) for the eight EGX-listed banks as of Q2 2019, representing them in percentages of the banks' total assets. A higher positive repricing gap coinciding with rate cuts indicates higher vulnerability to NIM shocks, led by ADIB, HDBK, and CIEB.

Tuesday, 27 August 2019

GB Auto's Stock: A Dud or a Stud?

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In *Today's Story*, we draw a picture about investing in GB Auto's stock (AUTO), after the recent interest rate cut and the company's performance during H1 2019. We also pinpoint the major catalysts for the company that investors should keep an eye on.

- **The recent interest rate cut helps AUTO:** As one of the highly-leveraged companies on the EGX, AUTO is clearly set to benefit from the recent 150bps cut in interest rates. The company's hefty financing expenses were a major reason behind its losses in the past quarters. With the resumption of the easing cycle by the CBE, we can expect a positive impact on AUTO, resting on:
    - **Less intense financing expenses**, which could narrow AUTO's losses or even widen its profits.
    - **A pick-up in car loans**, which could result in a better performance from the auto business.
    - **An expansion in lending volume** by the company's NBFS arm, **GB Capital**.
- **The auto business has seen all the negatives in H1 2019—in our view:** In H1 2019, the company's auto business has witnessed many unfavorable events, from competition that imports zero-tariff European cars to the "let it rust" car boycott campaign. This scene has led AUTO to lose ground in the local passenger cars market. For example, AUTO's market share decreased to 20% during H1 2019 from 28% a year ago, and margins also contracted after a reduction in its car prices. Moreover, the new government regulations placing a monthly limit on issuing the three-wheelers licenses have constrained supply, despite strong demand in the market. That said, AUTO's regional operations performed well in H1 2019, which have partially offset the weak performance given by the company's local passenger cars and two- and three-wheelers segment.
- **Value resides in GB Capital:** Our back-of-the-envelope valuation for AUTO resulted in a total equity value of EGP3.8bn or EGP3.6/share, 15% below market price. We valued AUTO using the sum-of-the-parts (SOTP) methodology, where we used the DCF approach to value the company's auto business, which pointed to a negative equity value due to the pressing needs of working capital plus a large amount of debt. Meanwhile, we adopted the justified P/B model to value **GB Capital**, which led to a total equity value of EGP4.5bn. Moreover, we ran a sensitivity analysis of AUTO's valuation, relying on our assumptions for GB Capital's ROE and terminal growth rate, which yielded a valuation range of EGP2.6-5.2/share.
- **Conclusion:** For some, it may seem that investing in AUTO should be avoided given the issues it faces in the auto business coupled with its large amount of debts. Meanwhile, others do like GB Capital's story and believe that the worst has already been inflected upon the auto business, and now could be a good time to invest in the stock. In our opinion, we think that investing in AUTO should be driven by catalysts that give a somewhat clear long-term view. One of these catalysts has already occurred, i.e. the interest rate cut. Other catalysts that should be kept under close observation by market participants are: (1) any signs of recovery in the company's local passenger cars segment, (2) the application of the automotive directive which should give incentives to local assemblers and producers, (3) loosening the regulations on the three-wheelers segment, (4) continuation of the strong performance of the company's regional operations, and (5) any further interest rate cut of course. All in all, AUTO's consensus target price of EGP6.8/share indicates that analysts in the market believe in the future of AUTO and its turnaround chances.

Our SOTP valuation for AUTO

Business	EGPmn	EGP/share
Auto segment	(646)	(0.59)
GB Capital	4,530	4.14
Total GB Auto	**3,884**	**3.55**
Market value	4,595	4.20
Upside/(downside)	*-15%*	*-15%*

Source: SHUAA Securities Egypt.

AUTO's valuation sensitivity analysis to GB's Capital ROE & TGR

TGR \ ROE	25%	26%	27%	28%	29%
11%	3.92	4.24	4.56	4.88	5.21
10%	3.44	3.70	3.97	4.24	4.51
9%	3.09	3.32	3.55	3.78	4.01
8%	2.83	3.03	3.23	3.44	3.64
7%	2.63	2.81	2.99	3.17	3.35

Source: SHUAA Securities Egypt.

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Tracing H1 2019 Pre-sales Patterns of Leading Property Developers

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With numerous projects launching in what seems to be an already-crowded property market, some companies still managed to close out Q2 2019 with growing numbers. But this was not the typical case as evidenced by a sample of the largest EGX-listed real estate companies by market cap. Leading property developers **TMGH**, **OCDI**, **ORHD**, and **MNHD** saw their aggregate pre-sales in Q2 2019 fall by 28% y/y to c.EGP11.7bn, which was widely expected due to spiraling prices, waning purchasing power, and a stagnant secondary market. Normalizing these figures by removing the fraction of sales made by new launches, they would reflect how limited actual buyers are and how interest in existing projects is fading.

- **Sales performance in H1 2019:**
  - **TMG Holding** (TMGH) launched *Privado*, a new private community within *Madinaty*, spanning over 276 feddans, in May 2019. Since launch, the project generated EGP4.8bn in sales (12.6% of its inventory), accounting for 41% of the company's H1 2019 sales. Total pre-sales, however, declined y/y by 26% in H1 2019 and by 44% in Q2 2019. This indicates that *Celia*, a project that has been launched in the **New Administrative Capital** in May 2018, gained greater momentum than *Privado*.
  - **Sixth of October Development & Investment Co.** (OCDI) launched new projects in *Allegria Residence*, *V Residences* and *EDNC*, bringing in sales of EGP2.3bn (-4% y/y) in H1 2019, but Q2 2019 sales of EGP1.4bn came higher by 61% q/q and 18% y/y.
  - **Orascom Development Egypt** (ORHD) is placing itself in a different camp in terms of market share with the launch of *O West* in **Sixth of October City** in Q1 2019, which produced EGP2.8bn in sales (67% of total pre-sales), leading the company to break its own records. Nonetheless, a 9% decline in the number of units sold in *El-Gouna*, coupled with a 19% increase in price per sqm, has left the company's El-Gouna sales relatively flat.
  - **Madinet Nasr Housing & Development**'s (MNHD) sales decreased by c.19% y/y. Yet, its *Sarai* project has been picking up stronger momentum than all the rest of MNHD's, especially *Taj City*. *Sarai* has achieved 12% higher sales y/y, while *Taj City saw* its sales slump 64% y/y. In this mix, the launch of the company's commercial component, *Cobalt Business District*, added EGP620mn worth of presales, accounting for 30% of total sales in H1 2019.

Change in pre-sales quarterly and annually

EGPmn	Q1 2018	Q2 2018	% q/q	Q1 2019	% y/y	Q2 2019	% y/y	% q/q	H1 2018	H1 2019	% y/y
TMGH	2,930	12,900	340%	4,490	53%	7,226	(44%)	61%	15,830	11,716	(26%)
…of which Privado was						*4,800*				*4,800*	
… % of pre-sales						*66%*				*41%*	
ORHD	368	1,200	226%	1,500	308%	2,700	125%	80%	1,568	4,193	167%
…of which O West was										*2,779*	
… % of pre-sales										*66%*	
OCDI	1,200	1,200	0%	881	(27%)	1,419	18%	61%	2,400	2,300	(4%)
MNHD	1,583	946	(40%)	1,720	9%	338	(64%)	(80%)	2,529	2,058	(19%)
…of which Cobalt Business District was										*620*	
… % of pre-sales										*30%*	
Aggregate	6,081	16,246	167%	8,591	41%	11,683	(28%)	36%	22,327	20,267	(9%)

Source: Company data.

Thursday, 29 August 2019

SKPC – Initiating coverage; A Play on Hydrocarbon–Olefin Spread

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- Earlier this morning, we just initiated coverage on **Sidi Kerir Petrochemicals Co.** (SKPC), a key materials player in the Egyptian market. SKPC produces ethylene and polyethylene (PE) through processing the Western Desert ethane/propane (E/P) mixture. Exaggerated hikes of feedstock costs and cheaper polyethylene have been eroding SKPC's operating margins over the last seven years. After PE prices continued to weaken SKPC's performance in H1 2019, the stock price implied an EV/ton of USD851 vs. USD4,193 for its 20%-owned Egyptian Ethylene & Derivatives Co.'s (ETHYDCO) based on its investment cost in 2011. We see the EGP/USD rate significantly impacting SKPC's operating income in the near future. We assigned the stock a Neutral / High Risk rating and a 12M PT of EGP12.0/share (+20%).

  For further details, please download the full report from this link.

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