

12 May 2011

Buy

Target price
Dh1.10

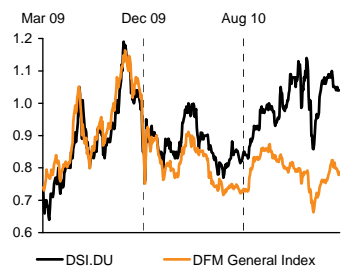
Price
Dh1.07

Short term (0-60 days)
n/a

Market view
No Weighting

Price performance

	(1M)	(3M)	(12M)
Price (Dh)	1.08	1.08	0.89
Absolute (%)	-0.9	-0.9	20.5
Rel market (%)	-4.1	-1.4	30.5
Rel sector (%)	-0.9	-0.9	20.5



Market capitalisation
Dh2.33bn (€443.61m)

Average (12M) daily turnover
Dh8.41m (US\$2.42m)

Sector: European-DS Tot Mrkt
RIC: DSI.DU, DSI UH
Priced Dh1.07 at close 11 May 2011.
Source: Bloomberg

Analysts

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Drake & Scull

Solid qtr, healthy backlog aggregation

DSI reported solid quarterly results on account of stronger project execution. Also the company maintained its strong backlog momentum by securing new projects worth Dh2.8bn year-to-date.

Key forecasts

	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue (Dhm)	1,917	1,854	2,382	2,601	2,799
EBITDA (Dhm)	263.9	187.7	272.8	297.8	319.9
Reported net profit (Dhm)	260.7	164.4	215.7	224.9	238.8
Normalised net profit (Dhm)	260.7	164.4	215.7	224.9	238.8
Normalised EPS (Dh)	0.12	0.08	0.10	0.10	0.11
Dividend per share (Dh)	0.07	0.00	0.00	0.00	0.00
Dividend yield (%)	6.54	0.00	0.00	0.00	0.00
Normalised PE (x)	8.89	14.00	10.60	10.20	9.61
EV/EBITDA (x)	8.02	13.20	9.78	9.11	8.26
EV/invested capital (x)	0.92	0.93	0.89	0.85	0.80
ROIC - WACC (%)	n/a	n/a	n/a	n/a	n/a

Accounting standard: IFRS
Source: Company data, Rasmala forecasts

year to Dec, fully diluted

Top line beat on better execution

DSI's 1Q11 revenue rose 67% yoy to Dh645m on the back of stronger project execution. The revenue comfortably beat our and Bloomberg consensus estimates of Dh534m and Dh580m, respectively. However, EPS was below our expectations, indicating margins remained under pressure owing to stiff competition in the construction space. EPS was Dh0.021 (up 7% yoy), below our forecast of Dh0.023.

Backlog maintained its growth momentum

After increasing 81% in 2010, DSI's backlog continued to grow at a brisk pace during the quarter, reaching Dh7.5bn, vs Dh4.9bn at end-2010. Year-to-date, the company secured Dh2.8bn worth of projects, equivalent to c57% of its 2010 year-end backlog. In contrast, during the same period, regional peer Arabtec secured Dh2.8bn worth of new contracts, equivalent to c19% of Arabtec's 2010 year-end backlog. All the new project wins came from geographies outside Dubai, with the company securing a major project in Saudi worth Dh2bn. Furthermore, DSI expects to maintain its momentum in 2H11.

Valuation

We expect to re-examine our forecasts and target price pending detailed financials and/or company feedback on its outlook. We value DSI at Dh1.10 per share using a DCF approach, as we believe this method best captures the backlog and earnings growth potential of the contractors. We assume an 11.4% WACC, a 6% revenue CAGR for the next 10 years, a long-term operating margin of 7.8% and a terminal growth rate of 3%. Our WACC estimate is based on cost of debt of 5.0% and cost of equity of 13.1%. We derive our cost of equity using a risk-free rate of 4.0%, an equity market risk premium of 7% and a beta of 1.3.

Important disclosures can be found in the Disclosures Appendix.

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Income statement

Dhm	FY09A	FY10A	FY11F	FY12F	FY13F
Revenue	1917	1854	2382	2601	2799
Cost of sales	-1529	-1516	-1977	-2178	-2362
Operating costs	-123.8	-150.0	-132.1	-124.6	-117.3
EBITDA	263.9	187.7	272.8	297.8	319.9
DDA & Impairment (ex gw)	-83.0	-62.9	-68.7	-82.6	-92.9
EBITA	180.9	124.8	204.1	215.2	227.0
Goodwill (amort/impaird)	0.00	0.00	0.00	0.00	0.00
EBIT	180.9	124.8	204.1	215.2	227.0
Net interest	28.7	11.5	-6.71	-10.6	-10.0
Associates (pre-tax)	0.00	0.00	0.00	0.00	0.00
Other pre-tax items	57.6	24.1	23.8	26.0	28.0
Reported PTP	267.2	160.5	221.2	230.7	244.9
Taxation	-0.86	4.67	0.00	0.00	0.00
Minority interests	-5.60	-0.72	-5.53	-5.77	-6.12
Other post-tax items	0.00	0.00	0.00	0.00	0.00
Reported net profit	260.7	164.4	215.7	224.9	238.8
Tot normalised items	0.00	0.00	0.00	0.00	0.00
Normalised EBITDA	263.9	187.7	272.8	297.8	319.9
Normalised PTP	267.2	160.5	221.2	230.7	244.9
Normalised net profit	260.7	164.4	215.7	224.9	238.8

Source: Company data, Rasmala forecasts

year to Dec

Balance sheet

Dhm	FY09A	FY10A	FY11F	FY12F	FY13F
Cash & market secs (1)	878.4	523.0	568.5	525.3	595.2
Other current assets	2240	2670	3344	3623	3847
Tangible fixed assets	211.5	214.4	281.6	388.6	441.2
Intang assets (incl gw)	821.8	902.2	868.6	835.1	801.5
Oth non-curr assets	249.0	122.2	122.2	122.2	122.2
Total assets	4401	4431	5185	5494	5807
Short term debt (2)	503.5	520.2	520.2	520.2	520.2
Trade & oth current liab	1157	1196	1560	1719	1864
Long term debt (3)	159.9	147.3	387.3	387.3	387.3
Oth non-current liab	64.3	41.4	41.4	41.4	41.4
Total liabilities	1885	1905	2509	2668	2813
Total equity (incl min)	2515	2526	2676	2827	2995
Total liab & sh equity	4401	4431	5185	5494	5807
Net debt	-215.0	144.6	339.0	382.2	312.3

Source: Company data, Rasmala forecasts

year ended Dec

Cash flow statement

Dhm	FY09A	FY10A	FY11F	FY12F	FY13F
EBITDA	263.9	187.7	272.8	297.8	319.9
Change in working capital	-325.0	-337.4	-293.0	-109.7	-173.0
Net interest (pd) / rec	-58.8	1.28	2.91	2.39	1.85
Taxes paid	-1.39	0.00	0.00	0.00	0.00
Other oper cash items	-52.4	16.7	3.30	12.8	120.2
Cash flow from ops (1)	-173.7	-131.7	-13.9	203.3	269.0
Capex (2)	-16.2	-29.6	-102.4	-156.0	-112.0
Disposals/(acquisitions)	1.75	0.13	0.00	0.00	0.00
Other investing cash flow	-418.9	-124.3	31.2	34.8	35.3
Cash flow from invest (3)	-433.4	-153.8	-71.2	-121.2	-76.6
Incr / (decr) in equity	0.00	0.00	0.00	0.00	0.00
Incr / (decr) in debt	263.5	24.8	240.0	0.00	0.00
Ordinary dividend paid	0.00	-151.4	-71.4	-79.9	-77.1
Preferred dividends (4)	0.00	0.00	0.00	0.00	0.00
Other financing cash flow	-240.3	-107.2	-37.9	-45.4	-45.4
Cash flow from fin (5)	23.2	-233.8	130.7	-125.2	-122.5
Forex & disc ops (6)	-2.95	-19.7	0.00	0.00	0.00
Inc/(decr) cash (1+3+5+6)	-586.8	-539.1	45.6	-43.2	69.9
Equity FCF (1+2+4)	-189.9	-161.3	-116.3	47.2	157.0

Source: Company data, Rasmala forecasts

year to Dec

Recommendation structure

Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price and only reflects capital appreciation. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%.

Performance parameters and horizon: Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Market or sector view: This view is the responsibility of the strategy team and a relative call on the performance of the market/sector relative to the region. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.

Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

Valuation and risks to target price

Drake & Scull (RIC: DSI.DU, Rec: Buy, CP: Dh1.07, TP: Dh1.10): We value DSI using a DCF methodology. Key risks to our target price include project delays in the UAE that may reduce robust growth expectations from 2011 onward. Also, the company may need to reduce management expectations of a 20-25% revenue CAGR over the next five years.

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