

Drake & Scull International

Initiate with Overweight (V): A value play

- ▶ **Able to offset Dubai exposure faster than others**
- ▶ **Strong balance sheet means further M&A likely, possible AED0.4/share accretion on our estimates**
- ▶ **Initiate with Overweight (V) and AED1.20 target: a value play**

Overweight (V)

Target price (AED)	1.20
Share price (AED)	0.90
Potential total return (%)	33.3

	2009 a	2010 e	2011 e
HSBC EPS	0.15	0.092	0.091
HSBC PE	5.86	9.79	9.87
Performance	1M	3M	12M
Absolute (%)	-9.7%	7.5%	17.3%
Relative^ (%)	-3.4%	-4.2%	9.3%

Note: (V) = volatile (please see disclosure appendix)

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Ability to offset Dubai exposure faster than others: As an end-to-end contractor operating primarily in the GCC, Drake & Scull International's (DSI) backlog dropped c27% y-o-y in 2009 due to the economic crisis. However, we believe 2009 is likely to represent the trough in its backlog; the company's diversified business model should allow it to offset its exposure to Dubai (36% of 2010e backlog) faster than others in the region. Bidding momentum has picked up in the GCC so far this year and DSI also has other advantages – a strong cash position and zero direct exposure to Nakheel. These are key positives that should work in the company's favour when tendering for contracts and raising working capital funding.

Greater competition will take its toll on 2010 industry margins: The economic crisis in Dubai has led to the contracting market there effectively being closed, leading to a loss of contractor bargaining power across the GCC. An unprecedented amount of contracting capacity for residential and commercial projects is now tapping the region for new work to compensate for the lack of awards in Dubai. With competition fierce, this will feed through to industry margins in 2010 – we assume an EPS decline of 23% CAGR 2009-11 for DSI. However, the company is targeting expansion into the higher margin and faster growing infrastructure market and the more rapidly this is carried out, the more positive our earnings growth outlook would be. DSI's acquisition of Passavant-Roediger in Q4 2009 is a step in this direction, adding expertise and c28% to the 2010e backlog, in the high-growth and more profitable water sector projects market.

Initiate with OW(V) – a value play: Our DCF-based valuation yields a 12-month target price of AED1.20 for DSI, implying a 33% potential return. The stock presents a value play, in our view, and we initiate coverage with an Overweight (V) rating. DSI trades on 9.8x 2010e earnings – our valuation implies 13.4x – versus 15x for its electro mechanical industry peers, yet its net cash position is 55% of market cap. The company's cash position means more M&A is likely and could potentially add a further AED0.4 per share to our valuation. We think DSI is also a good example of the 'reinvestment play' theme, given its diversified business model and geographic reach across the GCC. Downside risks to our rating include lower-than-expected awards, greater-than-expected competition and risks associated with potential M&A.

Index^	DUBAI FINANCIAL MARKET INDEX
Index level	5,785.54
RIC	DSI.DU
Bloomberg	DSI DB

Source: HSBC

Enterprise value (AEDm)	1,528
Free float (%)	55
Market cap (USDm)	554
Market cap (AEDm)	2,025

Source: HSBC

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Financials & valuation

Financial statements

Year to	12/2009a	12/2010e	12/2011e	12/2012e
Profit & loss summary (AEDm)				
Revenue	2,212	1,869	2,030	2,143
EBITDA	285	256	258	311
Depreciation & amortisation	-70	-54	-56	-59
Operating profit/EBIT	215	202	202	252
Net interest	77	22	21	27
PBT	337	209	207	262
HSBC PBT	337	209	207	262
Taxation	-1	-1	-1	-1
Net profit	334	200	199	251
HSBC net profit	334	200	199	251

Cash flow summary (AEDm)

Year to	12/2009a	12/2010e	12/2011e	12/2012e
Cash flow from operations	-239	378	324	314
Capex	-21	-126	-53	-79
Cash flow from investment	-314	-126	-53	-79
Dividends	-152	-60	-60	-75
Change in net debt	659	199	-112	-75
FCF equity	-83	251	270	234

Balance sheet summary (AEDm)

Year to	12/2009a	12/2010e	12/2011e	12/2012e
Intangible fixed assets	822	787	752	718
Tangible fixed assets	461	568	599	654
Current assets	3,118	2,644	2,814	2,928
Cash & others	1,160	961	1,073	1,149
Total assets	4,401	3,999	4,165	4,299
Operating liabilities	1,222	1,046	1,148	1,161
Gross debt	663	441	359	292
Net debt	-743	-544	-656	-731
Shareholders funds	2,477	2,465	2,604	2,779
Invested capital	2,018	1,991	1,944	1,989

Ratio, growth and per share analysis

Year to	12/2009a	12/2010e	12/2011e	12/2012e
Y-o-y % change				
Revenue	28.6	-15.5	8.6	5.6
EBITDA	58.0	-10.3	0.9	20.6
Operating profit	38.1	-6.1	0.1	24.7
PBT	59.2	-38.0	-0.8	26.2
HSBC EPS	59.3	-40.1	-0.8	26.3
Ratios (%)				
Revenue/IC (x)	1.4	0.9	1.0	1.1
ROIC	16.2	11.8	12.0	14.6
ROE	14.2	8.1	7.8	9.3
ROA	9.1	5.3	5.3	6.3
EBITDA margin	12.9	13.7	12.7	14.5
Operating profit margin	9.7	10.8	10.0	11.8
Net debt/equity	-29.5	-21.7	-24.7	-25.7
Net debt/EBITDA (x)	-2.6	-2.1	-2.5	-2.3
Per share data (AED)				
EPS reported (fully diluted)	0.15	0.09	0.09	0.12
HSBC EPS (fully diluted)	0.15	0.09	0.09	0.12
DPS	0.07	0.03	0.03	0.03
Book value	1.14	1.13	1.20	1.28

Key forecast drivers

Year to	2009	2010e	2011e	2012e
Backlog execution	n/a	1,576	312	55
% of revenue	n/a	84%	15%	3%
New awards	1,495	3,618	3,876	4,076
% y-o-y	-33.7%	142.0%	7.1%	5.2%
Closing backlog	1,976	3,725	5,571	7,503
% y-o-y	-26.6%	88.5%	49.5%	34.7%

DCF analysis

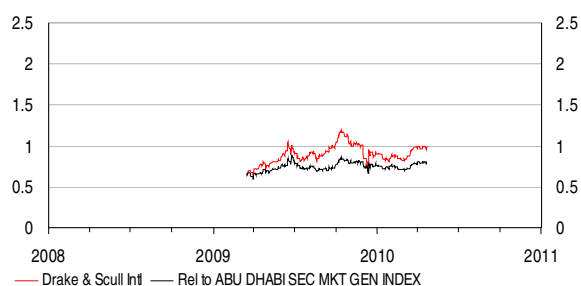
HSBC assumptions	DCF, comprising		
PV of free cash flow	1,007	Cost of equity	14.6%
PV of continuing value	623	WACC	12.04%
DCF-based EV	1,630	Perpetual growth rate	2.0%

Valuation data

Year to	12/2009a	12/2010e	12/2011e	12/2012e
EV/sales	0.57	0.78	0.67	0.60
EV/EBITDA	4.40	5.71	5.26	4.16
EV/IC	4.97	6.19	5.75	4.52
PE*	5.86	9.79	9.87	7.81
P/Book value	0.79	0.80	0.75	0.71
FCF yield (%)	-5.2%	11.7%	12.7%	10.6%
Dividend yield (%)	7.78%	3.07%	3.04%	3.84%

Note: * = Based on HSBC EPS (fully diluted)

Price relative



Source: HSBC

Note: price at close of 26 Apr 2010

Summary

- ▶ Able to offset Dubai exposure faster than others
- ▶ Strong balance sheet means further M&A is likely, possible AED0.4 per share accretion on our estimates
- ▶ Initiate with Overweight (V) and AED1.20 target – a value play

Business model

Drake & Scull International (DSI) opened the year with a backlog of AED2.1bn (USD544m), 1x 2009 sales and a Q1 2010e backlog of AED2.6bn. DSI's backlog offers the lowest revenue visibility versus its GCC peers (1.3x), but has the strongest potential for growth in 2010-11, in our view.

The company's core operations are mechanical, electrical and plumbing contracting services (MEP, 52% of backlog), and more recently water and power (IWP, 31%), following its acquisition of a water and sludge treatment company, in addition to civil contracting services (c18%).

In spite of its geographical diversification efforts, Dubai is still DSI's single largest market (36% of 2010e backlog), but the company has no direct exposure to Nakheel.

DSI: 2010e backlog by market and segment (AED2.1bn)

	Total	Electro mechanical	Water & power	Civil
Dubai	35.8%	29.7%	4.1%	2.0%
Abu Dhabi	17.0%	1.4%	3.2%	12.4%
Europe	9.1%	0.0%	9.1%	0.0%
Others	8.3%	11.6%	7.6%	0.0%
Qatar	7.8%	7.8%	0.0%	0.0%
Saudi	6.8%	0.7%	6.2%	0.0%
Thailand	6.1%	11.8%	0.0%	0.0%
Jordan	5.7%	0.0%	18.7%	0.0%
Kuwait	3.3%	0.0%	0.0%	3.3%
Total	100%	51.7%	30.7%	17.6%

Source: DSI, HSBC estimates

Market has bottomed

In our view, the residential and commercial projects market in the GCC has bottomed. Project suspensions, cancellations and contract revisions appear to be over since the start of the year and we think the worst is now behind us. 2010 may start to see these suspensions gradually come back to the market.

Within the GCC, Saudi Arabia (7% of DSI's backlog) and Abu Dhabi (17% of backlog) are the markets we expect to lead the Gulf region into a recovery, although not enough to replenish backlogs back to 2008 levels. This will take at least 3-4 years and come at a much higher price. Dubai alone represented c30% of the 2008 construction spend and at least 35% of planned projects pre-crisis, relative to the GCC region as a whole.

Without a pick-up in Dubai, those contractors based there will continue to search the region for project awards. This will eat away at the market share of existing players and put pressure on profit margins. Further, the majority of Saudi Arabia and Abu Dhabi's spending plans are geared towards general public infrastructure – such as power and utilities, transportation and, in selective markets, oil & gas.

Bidding pipeline in Abu Dhabi, Saudi Arabia and Qatar by project type (based on engineering, procurement and construction contract values)

(USDm)	Abu Dhabi	Saudi Arabia	Qatar	Total	% share
Residential & commercial	15,457	17,726	5,597	38,780	32.0%
Industrial	19,450	12,094	1,380	32,924	27.2%
Utilities	6,311	5,920	960	13,191	10.9%
Infrastructure	16,198	18,793	1,366	36,357	30.0%
Total	57,416	54,533	9,303	121,252	
% share	47.4%	45.0%	7.7%		

Source: MEED, Zawya, HSBC

No direct exposure to Nakheel

While DSI has zero direct exposure to Nakheel, we think there is an indirect impact on the broader market. The risk that we see with the Nakheel restructuring proposal is that it faces the following headwinds:

- ▶ **Loss of trust with end-user customers** may mean longer cash conversion cycles.
- ▶ **Re-tendering of contracts could result in more delays.**
- ▶ **Banks may be less willing to fund working capital** on Nakheel-related projects

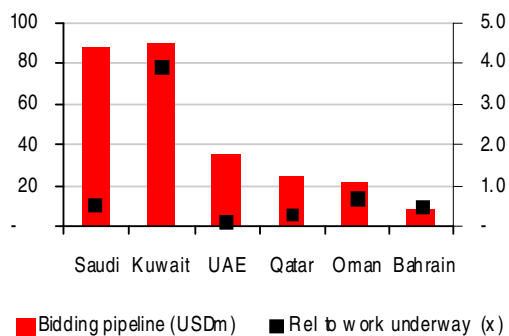
We calculate that the total value of Nakheel's projects – where it is both a project owner and shareholder – is close to USD110bn.

Able to offset Dubai exposure faster than others

Across our coverage of Middle East construction stocks, we use only the value of projects where clients have invited contractors to bid for projects as pipelines. This more advanced stage for projects typically implies a higher likelihood that a contract award is imminent, with the client having spent time and money on project design, government approvals, hired a consultant and, equally important, secured project financing.

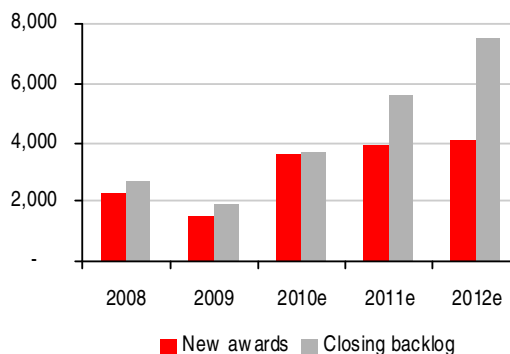
DSI's relatively more mobile scope of work, well-established regional presence and healthy balance sheet, means it is better positioned to offset its Dubai exposure faster than others. By 2012, we expect Dubai to represent closer to 15% of the company's backlog, compared with the 36% in 2010e.

Bidding pipeline relative to work underway in the GCC



Source: MEED, Zawya, HSBC

DSI: new contract awards and backlog (AEDm)



Source: DSI, HSBC estimates

2009: trough for backlog, but peak for margins

Broadly speaking, we believe contractor backlogs are close to their trough, except for less diversified UAE-based pure residential contractors. Contractors in the UAE were forecasting at least 20% backlog growth in 2009. The crisis instead resulted in a 20% drop in backlog and an aggregate USD360bn worth of projects, mostly in Dubai, being suspended. The existing supply/demand situation is in favour of clients. Also, as existing project backlogs are executed, there will be even more freed up contracting capacity, so the competitive landscape could potentially worsen.

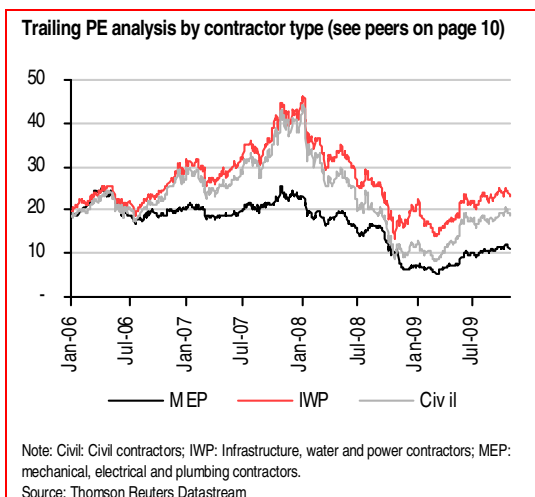
So, while the backlog may have troughed, margins have yet to reflect the impact of the crisis and for DSI we forecast a CAGR 2009-11 EPS decline of 23%. For DSI to maintain its earnings unchanged, the company would need to win AED3bn more new awards per annum to offset the margin decline.

Initiate with Overweight (V) and AED1.20 target

We believe DSI presents a good value play, with potential for growth opportunities thanks to its strong cash position. DSI trades on 9.8x 2010e earnings – our valuation implies 13.4x – versus 15x for MEP industry peers, yet its net cash position represents close to 55% of its market cap. Also, note approximately 80% of our 2010 earnings estimates are secured by existing backlog, where we see reasonable project progress.

We value DSI using DCF methodology, based on a WACC of 12.04% and a perpetual growth rate of 2%. Our forecasts yield a 12-month fair value of AED1.20 per share; implying a 33.3% potential total return; we therefore initiate coverage with an Overweight (V) rating.

Our valuation for DSI implies 13.4x 2010e PE, in line with its peers but inflated by its strong net cash position (ex-cash implied PE is 5.8x). Trailing PE analysis suggests that the market assigns a premium to infrastructure-exposed contractors, versus electro mechanical and civil contractors. This supports our view that the faster DSI expands away from the residential projects market and towards infrastructure, the more positive we would be.



Cash-financed acquisition could add AED0.4

The company is looking at acquisitive growth this year, financed by its significant AED1.2bn cash position. We run a scenario analysis to quantify how much its cash position could add to our 2010 backlog assumption and our AED1.2 per share valuation. Assuming it pays a PE multiple of 12x (M&A sector average for GCC) for an MEP contractor in the region operating with a net margin of 8% and a 0.5x book/bill ratio, DSI's cash position could add a further AED0.4 per share to our valuation.

Scenario for cash-financed acquisition: based on paying a PE multiple of 12x for an GCC MEP contractor operating with a net margin of 8% and a 0.5x book/bill ratio

(AEDm)	2010e	2011e	2012e	2010-12e change
Revenue	2,289.7	2,487.1	2,626.2	22.5%
EBITDA	315.1	320.2	385.5	23.6%
Net profit	238.3	225.7	290.6	16.1%

Source: HSBC estimates

Over the past six months, two of DSI's three acquisitions have been sister companies.

Acquiring another sister company would also enhance margins on projects in the respective markets where it would have previously outsourced to the sister company.

Drake and Scull Group (DSG) which is DSI's parent company also has investments in other MEP and civil contractors in the region. In any deal to acquire a regional contractor, DSI could be buying out DSG's share, which may create a conflict of interest for DSI shareholders. That said, we calculate that the company's acquisitions so far were based on a 6.0-9.5x PE multiples

versus 13.5x average for previous global construction M&A deals.

Risks

Downside risks to our investment case include: lower-than-expected project awards and backlog growth; greater-than-expected competition lowering DSI's bargaining power and, in turn, profit margins; variability of quarterly operating results; receivables risk; and corporate governance issues related to potential acquisitions of sister companies where there is cross-ownership by DSI shareholders. Also, we think DSI has relatively high dependence on a few key executives.

Construction sector M&A deals

Company	Country	Date	Deal value (USDm)	Stake (%)	PE (x)
Entreprise Industrielle	France	Jun-99	98	65.1	12.20
EPTE	Brazil	Mar-99	74	19.5	12.60
Barcom PLC	United Kingdom	May-98	65	100.0	14.20
Oliver Ashworth Group PLC	United Kingdom	Aug-98	57	100.0	14.20
McConnell Dowell Corp Ltd	Australia	Mar-99	52	63.8	9.60
Teplarny Brno as	Czech Republic	Jan-00	52	n/a	17.90
Majestic Contractors Ltd	Canada	Jan-93	44	95.1	19.70
Avonside Services Group Ltd	United Kingdom	Oct-07	36	100.0	10.80
Sanki Engineering Co Ltd	Japan	Jan-00	34	n/a	13.80
Romanoff Electric Corp	United States	Aug-98	33	100.0	12.50
Furukawa Engineering & Const	Japan	Oct-09	27	100.0	10.30
Naylor Industries Inc	United States	Jul-93	23	100.0	16.00
Hibiya Engineering Ltd	Japan	Jan-00	11	n/a	16.30
Hibiya Engineering Ltd	Japan	Jan-00	10	n/a	10.70
Daimei Telecom Engineering	Japan	Jan-00	8	n/a	12.80
Smith Contracting Services Ltd	United Kingdom	Jan-05	8	100.0	17.20
Kokusai Densetsu Co Ltd	Japan	Oct-05	8	72.8	9.00
Hitachi Plant Construction	Japan	Jan-00	2	n/a	7.90
Goldfield Corp	United States	Jan-00	1	n/a	16.60
Insituform East Inc	United States	Nov-90	0	2.2	10.60
GTCC	UAE	Jan-07	43	80%	9.50
Passavant-Roediger	E Europe	Nov-09	20	82%	n/a
Drake & Scull Kuwait	Kuwait	Dec-09	22	75%	n/a
Drake & Scull Qatar	Qatar	Apr-10	23	100%	5.97
Average					13.53

Source: Thomson Reuters Datastream, HSBC

Valuation

- ▶ DCF based 12-month valuation of AED1.20 – Overweight (V)
- ▶ DCF fair value implies 10% discount to mid-cycle multiple
- ▶ Contract awards likely to be key share price trigger

Methodology

Our valuation of DSI is based on discounted cash flow methodology. For Dubai stocks, HSBC applies a risk-free rate of 7.8% and an equity risk premium of 7.5%, which would give a cost of equity of 15.25%. We opt to apply a weighted average cost of equity assumption based on DSI's backlog exposure by market, as shown below. This means we think the faster DSI expands away from the UAE, the lower the discount applied to the stock.

We calculate a weighted average cost of equity of 14.6% and a WACC of 12.0%. We assume a sector average beta of 1.2, given DSI's short trading history, and a perpetual growth rate of 2%.

This yields a 12-month valuation for DSI of AED1.20 per share. Relative to the 26 April 2010 closing of AED0.90, our valuation implies a potential total return of 33% and we therefore initiate coverage on DSI with an Overweight (V) rating.

DCF inputs

	Backlog exposure	Risk premium	Risk-free rate	CoE
Dubai	35.8%	7.5%	7.8%	15.25%
Abu Dhabi	17.0%	6.5%	5.0%	11.50%
Saudi Arabia	6.8%	5.5%	4.0%	9.50%
Kuwait	3.3%	5.5%	4.0%	9.50%
E Europe	9.1%	5.0%	7.0%	12.00%
Qatar	7.8%	5.5%	4.0%	9.50%
Others	20.2%	5.5%	4.0%	9.50%
Beta adjusted weighted average CoE				14.6%
WACC				12.0%

Source: HSBC estimates

DCF valuation summary (AEDm)

PV of free cash flow	1,003
PV of continuing value	613
DCF-based EV	1,616
Add: cash	1,391
Less debt	663
DCF-based equity value	2,344
Outstanding shares (m)	2,178
Equity value (AED per share)	1.08
HSBC 12-month equity value (AED per share)	1.20

Source: HSBC estimates

Free cash flow calculations

(AEDm)	2008	2009	2010e	2011e	2012e	2013e	2014e	2015e
NOPLAT	105	156	202	202	252	282	298	315
Depreciation	15	25	54	56	59	63	69	75
Gross Cash Flow	121	181	256	258	311	346	367	391
Working Capital chg	(50)	(186)	100	43	(25)	15	(25)	(26)
Capex	(55)	(97)	(126)	(53)	(79)	(106)	(136)	(166)
Free Cash to Investors	16	(102)	230	249	208	255	207	198
% growth	-76.24%	-742.78%	-325.51%	8.41%	-16.49%	22.53%	-18.85%	-4.13%

Source: HSBC estimates

Relative valuation

Our DCF-based valuation for DSI implies a 2010e EV/EBITDA of 6.3x and PE of 13.4x. This compares with almost 15x 2010e PE for its global MEP industry peers (see pages 10-11) and 17.7x relative to an average of MEP, civil and infrastructure contractors.

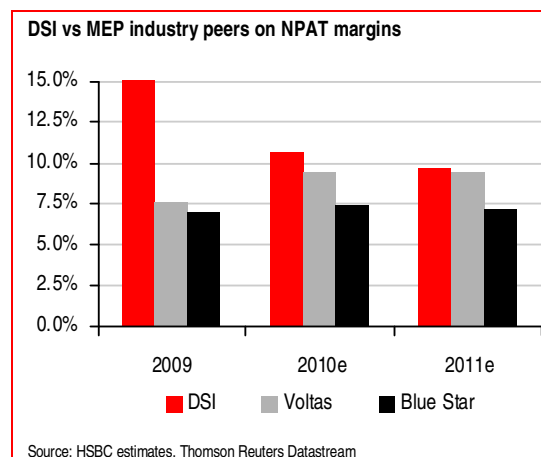
DCF-based implied valuation (x)				
	2009a	2010e	2011e	2012e
PE	8.03	13.41	13.52	10.71
EV/EBITDA	5.66	6.31	6.26	5.19

Source: HSBC estimates

We believe Voltas (VOLT.BO, INR183, N(V)) and Blue Star (BLSTR IN, INR411.6, not rated) represent the most comparable peers to DSI's core business, electro mechanical contracting, especially Voltas. However, Voltas acts more as a project manager and executes a relatively lower share of the MEP contract in-house, unlike DSI. Also, the company is highly exposed to the GCC region – c67% of Voltas' backlog currently comes from the GCC, mainly from Qatar, Abu Dhabi and Saudi Arabia. The balance of Voltas' backlog comes from its domestic market, India.

Blue Star is a pure local MEP player in India and, similar to DSI, executes a larger share of the contract in-house.

Voltas' services represent the main competition to DSI in the UAE MEP market, although the market remains relatively fragmented, especially in Abu Dhabi. According to HSBC analyst, Sandeep Somani, Voltas is planning to expand more aggressively into new markets such as Saudi Arabia and Oman. An invitation to bid is often conditional on prior experience, technical capability and financial strength, and we think Voltas poses competition to DSI on all these counts, with the exception of on-ground experience in the Gulf, especially the UAE, and supplier relationships.



Trailing analysis suggests mid cycle multiple of 15x for DSI

A trailing PE multiple analysis for select global civil, infrastructure and electro mechanical contractors suggests that contractors exposed to infrastructure projects warrant a higher multiple: 19.5x mid cycle, versus 11.5x for MEP contractors. This supports our view of the more favourable contracting market dynamics in infrastructure.

Trailing PE multiples during various economic cycles (x)

	Civil	Utilities	Electro mechanical	Average
2001-04	5.7	9.3	10.0	8.3
2005-07	21.0	20.5	15.1	18.9
2008-March 2009	18.7	25.4	10.7	18.3
April 2009 - to date	20.2	22.6	10.2	17.7
Average	16.4	19.5	11.5	

Source: HSBC, Thomson Reuters Datastream

Using DSI's backlog weight by division (52% MEP, 31% IWP and 17% civil) suggests a mid cycle multiple of 15x for the company, suggesting our DCF valuation implied multiple of 13.4x is conservative.

2010 EPS 25% below consensus

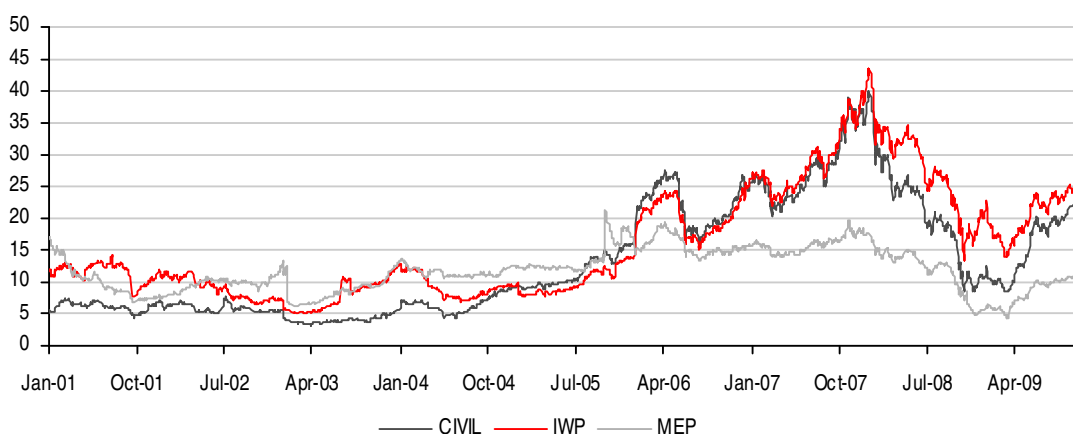
Our earnings forecasts are 25% below consensus estimates for 2010 and 20% below consensus for 2011. We think this is primarily due to our relatively lower margin assumptions for new project wins.

HSBC vs consensus

(AEDm)	2010e	2011e
Revenue	-4.5%	1.8%
EBIT	-12.4%	-11.7%
Net profit	-25.3%	-19.9%

Source: Thomson Reuters Datastream, HSBC estimates

Trailing PE analysis by contractor type (see page 10 for peers)



Note: Civil: Civil contractors; IWP: Infrastructure, water and power contractors; MEP: mechanical, electrical and plumbing contractors.
Source: Thomson Reuters Datastream

Global industry peers on valuation and growth

Stock	Ticker	Rating	Price	EV/Revenue (x)			Revenue CAGR 2009-11	EV/EBITDA (x)			EBITDA CAGR 2009-11	PE (x)			EPS CAGR 2009-11
				2009e	2010e	2011e		2009e	2010e	2011e		2009e	2010e	2011e	
Arabtec Holding	ARTC.DU	Underweight (V)	AED2.43	0.5	0.5	0.6	-6.5%	4.6	4.3	4.5	6.2%	5.9	6.0	5.9	0.1%
Larsen & Toubro	LART.BO	Neutral (V)	INR1,578	2.9	2.7	2.0	17.5%	25.7	22.2	18.5	15.5%	34.1	32.2	25.8	15.0%
IVRCL Infrastructure	IVRC.BO	Neutral (V)	INR178	1.2	1.0	0.9	20.6%	13.4	11.3	9.7	24.1%	21.1	21.4	17.8	9.0%
Nagarjuna Construction	NGCN.BO	Overweight (V)	INR178	1.2	1.0	0.9	17.8%	13.2	10.3	8.8	22.4%	26.5	23.4	19.1	17.6%
Hindustan Construction	HCNS.BO	Neutral (V)	INR134	1.8	1.5	1.3	21.0%	13.6	10.9	9.7	20.9%	45.3	34.0	25.4	33.5%
Punj Lloyd	PUJL.BO	Underweight (V)	INR168	0.6	0.6	0.6	12.8%	9.4	7.2	6.9	24.0%	19.5	12.6	10.9	33.8%
China State Construction	3311.HK	Overweight (V)	HKD2.60	0.3	0.7	0.6	26.5%	5.7	11.9	10.0	29.1%	12.1	11.3	9.2	14.9%
Al-Mojil	1310.SE	Neutral (V)	SAR21.95	1.4	1.8	1.1	-0.5%	8.3	9.5	5.9	7.3%	68.5	35.7	11.4	145.0%
Samsung Eng	028050.KS	Overweight (V)	KRW119,000	1.2	0.9	0.6	30.7%	13.2	9.5	6.5	33.9%	17.2	13.4	10.3	-17.5%
Hyundai Eng	000720.KS	Overweight (V)	KRW57,000	0.4	0.4	0.3	11.3%	7.7	6.3	5.4	20.8%	13.9	13.2	11.3	-9.5%
Hyundai Dev	012630.KS	Neutral (V)	KRW30,200	1.2	0.8	0.7	14.2%	15.8	7.4	6.2	37.3%	46.3	10.8	9.7	122.1%
Average civil				2.0	1.8	1.4	17.3%	18.7	15.7	13.0	20.1%	28.9	24.4	19.3	16.5%
Larsen & Toubro	LART.BO	Neutral (V)	INR1,578	2.9	2.7	2.0	17.5%	25.7	22.2	18.5	15.5%	34.1	32.2	25.8	15.0%
IVRCL Infrastructure	IVRC.BO	Neutral (V)	INR178	1.2	1.0	0.9	20.6%	13.4	11.3	9.7	24.1%	21.1	21.4	17.8	9.0%
Nagarjuna Construction	NGCN.BO	Overweight (V)	INR178	1.2	1.0	0.9	17.8%	13.2	10.3	8.8	22.4%	26.5	23.4	19.1	17.6%
Hindustan Construction	HCNS.BO	Neutral (V)	INR134	1.8	1.5	1.3	21.0%	13.6	10.9	9.7	20.9%	45.3	34.0	25.4	33.5%
Punj Lloyd	PUJL.BO	Underweight (V)	INR168	0.6	0.6	0.6	12.8%	9.4	7.2	6.9	24.0%	19.5	12.6	10.9	33.8%
China State Construction	3311.HK	Overweight (V)	HKD2.60	0.3	0.7	0.6	26.5%	5.7	11.9	10.0	29.1%	12.1	11.3	9.2	14.9%
Samsung Eng	028050.KS	Overweight (V)	KRW119,000	1.2	0.9	0.6	30.7%	13.2	9.5	6.5	33.9%	17.2	13.4	10.3	-17.5%
Hyundai Eng	000720.KS	Overweight (V)	KRW57,000	0.4	0.4	0.3	11.3%	7.7	6.3	5.4	20.8%	13.9	13.2	11.3	-9.5%
Hyundai Dev	012630.KS	Neutral (V)	KRW30,200	1.2	0.8	0.7	14.2%	15.8	7.4	6.2	37.3%	46.3	10.8	9.7	122.1%
China Railway Group	0390.HK	Overweight (V)	HKD5.53	0.3	0.3	0.2	22.1%	9.3	7.0	5.4	29.1%	16.2	12.0	9.6	30.0%
China Railway Construction	1186.HK	Overweight (V)	HKD9.56	0.2	0.1	0.1	23.5%	4.6	2.7	2.0	30.0%	18.0	13.0	10.0	34.1%
China Communications	1800.HK	Overweight (V)	HKD7.51	0.6	0.6	0.5	21.2%	9.1	8.3	7.2	15.9%	13.6	11.8	9.7	18.6%
OCI	OCIC.CA	Neutral (V)	EGP277.05	2.9	2.2	1.7	28.1%	13.8	9.7	6.7	43.5%	26.8	15.0	11.7	51.3%
Institutform Technology	INSU.O	NR	USD16.08	1.4	1.2	1.1	NA	12.1	9.1	7.7	NA	21.4	10.8	9.2	NA
Layne Christensen	LAYN.O	NR	USD21.42	1.0	0.6	0.5	9.9%	0.4	6.2	5.9	10.8%	4.5	107.1	24.1	30.9%
Average IWP				1.3	1.1	0.9	20.9%	12.9	10.4	8.5	24.8%	22.0	17.9	14.0	24.5%
Churchill	CUQ.TO	NR	CAD9.38	0.3	0.2	0.2	2.0%	3.2	3.2	3.0	3.6%	5.1	4.9	4.6	10.1%
Dycom Industries	DY	NR	USD7.49	0.4	0.4	0.4	NA	4.6	4.9	4.2	NA	5.4	62.4	20.5	NA
EMCOR Group Inc	EME	NR	USD18.27	0.2	0.2	0.2	NA	4.0	5.1	4.8	NA	8.0	10.3	8.8	NA
ROK	ROK.L	NR	GBP57.25	0.4	0.4	0.4	3.4%	9.3	9.4	9.6	1.4%	578.3	8.0	7.6	NA
Volta Ltd	VOLT.BO	Neutral (V)	INR184	1.3	1.0	0.9	13.6%	20.0	10.7	10.3	29.6%	26.9	18.3	17.7	23.3%
Blue Star Ltd	BLUS.BO	NR	INR166	1.4	1.5	1.3	17.4%	13.5	13.3	11.0	17.0%	8.8	8.0	6.7	16.2%
Nass Corporation	NASS.BH	NR	BHD0.13	0.4	0.4	0.4	-0.9%	3.7	3.5	3.4	4.5%	3.2	3.7	3.5	-4.6%
Drake & Scull International	DSI.DU	OW(V)	AED0.90	0.6	0.9	0.8	-4.2%	4.4	5.7	5.3	-4.9%	5.86	9.79	9.87	-22.9%
Average MEP				0.7	0.6	0.5	6.4%	9.0	7.1	6.4	10.6%	22.2	14.6	10.9	8.6%
Global average				1.3	1.1	0.9	19.8%	12.6	10.2	8.3	23.8%	22.2	17.7	13.7	24.3%

Source: Thomson Reuters Datastream for non-rated stocks, HSBC estimates for rated stocks

Global industry peers on returns

Stock	Ticker	Rating	Price	EBITDA margin			ROE (%)			Dividend yield (%)			PAT margin		
				2009e	2010e	2011e	2009e	2010e	2011e	2009e	2010e	2011e	2009e	2010e	2011e
Arabtec Holding	ARTC.DU	Underweight (V)	AED2.43	10.0%	12.6%	12.9%	18.3%	15.1%	13.4%	0.0%	0.0%	0.0%	6.5%	7.3%	7.4%
Larsen & Toubro	LART.BO	Neutral (V)	INR1,578	11.4%	12.0%	11.0%	23.3%	19.9%	15.5%	0.7%	0.8%	0.7%	8.0%	8.2%	7.8%
IVRCL Infrastructure	IVRC.BO	Neutral (V)	INR178	8.6%	9.0%	9.1%	11.3%	9.5%	10.1%	0.4%	0.6%	0.7%	4.6%	3.9%	3.8%
Nagarjuna Construction	NGCN.BO	Overweight (V)	INR178	9.0%	9.9%	9.7%	8.1%	10.2%	9.6%	0.6%	0.7%	0.8%	3.7%	4.1%	4.1%
Hindustan Construction	HCNS.BO	Neutral (V)	INR134	13.0%	13.4%	13.0%	9.3%	6.7%	8.2%	0.6%	0.6%	0.7%	2.3%	3.0%	3.3%
Punj Lloyd	PUJL.BO	Underweight (V)	INR168	6.8%	8.4%	8.2%	-712.2%	-2.0%	10.2%	0.2%	0.4%	0.4%	2.2%	3.4%	3.4%
China State Construction	3311.HK	Overweight (V)	HKD2.60	5.5%	5.7%	5.7%	12.7%	8.9%	8.5%	2.6%	3.0%	3.8%	5.3%	4.9%	4.7%
Al-Mojil	1310.SE	Neutral (V)	SAR21.95	16.7%	18.5%	19.4%	2.0%	3.5%	10.0%	0.0%	1.3%	4.4%	1.8%	5.3%	10.7%
Samsung Eng	028050.KS	Overweight (V)	KRW119,000	8.7%	9.0%	9.2%	41.0%	38.0%	35.9%	1.3%	1.3%	1.3%	8.3%	8.4%	8.1%
Hyundai Eng	000720.KS	Overweight (V)	KRW57,000	5.2%	6.1%	6.2%	12.4%	12.7%	13.5%	0.9%	0.9%	0.9%	4.9%	4.7%	4.9%
Hyundai Dev	012630.KS	Neutral (V)	KRW30,200	7.3%	10.8%	10.6%	2.7%	7.0%	8.1%	1.7%	1.7%	1.7%	2.3%	8.1%	8.3%
Average civil				9.7%	10.5%	10.0%	-2.1%	18.0%	16.0%	0.8%	0.9%	1.0%	6.6%	7.1%	7.0%
Larsen & Toubro	LART.BO	Neutral (V)	INR1,578	11.4%	12.0%	11.0%	23.3%	19.9%	15.5%	0.7%	0.8%	0.7%	8.0%	8.2%	7.8%
IVRCL Infrastructure	IVRC.BO	Neutral (V)	INR178	8.6%	9.0%	9.1%	11.3%	9.5%	10.1%	0.4%	0.6%	0.7%	4.6%	3.9%	3.8%
Nagarjuna Construction	NGCN.BO	Overweight (V)	INR178	9.0%	9.9%	9.7%	8.1%	10.2%	9.6%	0.6%	0.7%	0.8%	3.7%	4.1%	4.1%
Hindustan Construction	HCNS.BO	Neutral (V)	INR134	13.0%	13.4%	13.0%	9.3%	6.7%	8.2%	0.6%	0.6%	0.7%	2.3%	3.0%	3.3%
Punj Lloyd Ltd	PUJL.BO	Underweight (V)	INR168	6.8%	8.4%	8.2%	NA	-2.0%	10.2%	0.2%	0.4%	0.4%	2.2%	3.4%	3.4%
China State Construction	3311.HK	Overweight (V)	HKD2.60	5.5%	5.7%	5.7%	12.7%	8.9%	8.5%	2.6%	3.0%	3.8%	5.3%	4.9%	4.7%
Samsung Eng	028050.KS	Overweight (V)	KRW119,000	8.7%	9.0%	9.2%	41.0%	38.0%	35.9%	1.3%	1.3%	1.3%	8.3%	8.4%	8.1%
Hyundai Eng	000720.KS	Overweight (V)	KRW57,000	5.2%	6.1%	6.2%	12.4%	12.7%	13.5%	0.9%	0.9%	0.9%	4.9%	4.7%	4.9%
Hyundai Dev	012630.KS	Neutral (V)	KRW30,200	7.3%	10.8%	10.6%	2.7%	7.0%	8.1%	1.7%	1.7%	1.7%	2.3%	8.1%	8.3%
China Railway	0390.HK	Overweight (V)	HKD5.53	3.7%	4.0%	4.1%	6.5%	7.9%	9.4%	1.4%	1.9%	2.4%	1.9%	2.1%	2.2%
China Railway Construction	1186.HK	Overweight (V)	HKD9.56	4.5%	4.7%	5.0%	7.5%	9.6%	11.1%	1.3%	1.8%	2.3%	1.8%	2.1%	2.3%
China Communications	1800.HK	Overweight (V)	HKD7.51	7.1%	6.7%	6.5%	6.5%	6.6%	7.7%	2.0%	2.3%	2.8%	3.2%	3.0%	3.0%
OCI	OCIC.CA	Neutral (V)	EGP277.05	20.7%	22.4%	26.0%	10.1%	13.8%	15.3%	4.0%	4.0%	3.8%	10.0%	12.7%	14.0%
Insituform Technology	INSU.O	NR	USD16.08	12.0%	13.0%	14.1%	7.2%	10.4%	10.9%	0.0%	0.0%	0.0%	4.8%	6.2%	NA
Layne Christensen	LAYN.O	NR	USD21.42	240.7%	9.2%	9.2%	NA	3.5%	3.4%	NA	0.0%	0.0%	9.2%	0.7%	2.0%
Average IWP				9.9%	9.1%	9.3%	12.5%	12.7%	12.7%	1.5%	1.8%	2.0%	4.9%	5.4%	5.4%
Churchill Corp	CUQ.TO	NR	CAD9.38	8.5%	7.3%	7.2%	25.7%	20.1%	18.4%	0.0%	0.0%	0.0%	5.6%	4.9%	4.9%
Dycom Industries	DY	NR	USD7.49	7.9%	8.6%	9.5%	10.1%	10.0%	NA	0.0%	0.0%	0.0%	-2.8%	0.5%	1.4%
EMCOR Group Inc	EME	NR	USD18.27	5.6%	4.9%	4.9%	14.1%	9.5%	8.6%	0.0%	0.0%	0.0%	2.8%	2.4%	2.7%
North Midland Construction	NMD.L	NR	GBP157.5	2.9%	2.8%	NA	NA	NA	NA	0.1%	0.1%	NA	NA	NA	NA
ROK Plc	ROK.L	NR	GBP57.25	4.1%	4.1%	3.9%	17.0%	16.8%	NA	0.0%	0.0%	0.0%	0.8%	1.5%	1.9%
Voltas Ltd	VOLT.BO	Neutral (V)	INR184	6.5%	9.5%	8.5%	29.7%	31.1%	26.0%	0.9%	1.1%	1.1%	5.2%	6.5%	6.2%
Blue Star Ltd	BLUS.BO	NR	INR166	10.3%	11.2%	11.4%	50.3%	41.4%	38.6%	5.4%	4.8%	5.4%	6.2%	7.5%	7.6%
Nass Corporation	NASS.BH	NR	BHD0.13	11.4%	12.8%	12.7%	22.4%	12.2%	10.9%	17.7%	15.6%	19.5%	8.6%	7.7%	7.8%
Drake & Scull International	DSI.DU	OW(V)	AED0.90	12.9%	13.7%	12.7%	14.2%	8.1%	7.8%	7.8%	3.1%	3.0%	15.1%	10.7%	9.8%
Average MEP				6.4%	7.0%	6.8%	24.4%	20.4%	17.2%	1.5%	1.9%	2.0%	5.1%	5.9%	5.6%
Global average				9.8%	9.1%	9.3%	4.6%	13.0%	12.9%	1.5%	1.7%	2.0%	4.9%	5.4%	5.5%

Source: HSBC estimates

DSI shares have a foreign ownership limit of 49%, which means that at least 51% has to be owned by shareholders who are GCC nationals. As at 21 April 2010, according to the DFM, foreign ownership (Arab and foreign nationals) stands at 38.2% of DSI shares, versus the 49% limit.

Permitted versus actual ownership of shares

	National	GCC	Arab	Foreigners
Permitted	100%	100.0%	49.0%	49.0%
Actual ¹	51.31%	10.46%	29.86%	8.37%

Note: (1) As at 21 April 2010.
Source: DFM

Cash-financed acquisition could add AED0.4 further

The company continues to look at acquisitive growth, to be financed by its significant AED1.2bn cash position. DSI raised this money through its IPO in July 2008, the majority of which was locked into bank deposits yielding 6-8.5%. DSI management has expressed its target of acquiring majority shares in its sister companies in Saudi Arabia. The company targets a year closing cash position of AED500m. For more sizeable opportunities, the company could choose to lever up, retaining its cash in AED-denominated deposits and borrowing in USD-denominated accounts, to benefit from the favourable interest rate spread (currently 200-250bp).

We have run a scenario analysis to quantify how much a AED700m cash-financed acquisition would accrete to our 2010 backlog assumption and our AED1.2 per share valuation. Assuming a PE multiple of 12x (M&A sector average for GCC), a net margin of 8% and a 0.5x book/bill ratio, DSI's cash position could accrete AED0.4 per share to our valuation.

Acquiring a sister company would also enhance margins on projects in the respective markets where it would have previously outsourced to the sister company.

Scenario for cash-financed acquisition

(AEDm)	2010e	2011e	2012e	2010-12e change
Revenue	2,289.7	2,487.1	2,626.2	22.5%
EBITDA	315.1	320.2	385.5	23.6%
Net profit	238.3	225.7	290.6	16.1%

Source: HSBC estimates

Key risks

Downside risks to our rating include:

- ▶ Lower-than-expected project awards and backlog growth.
- ▶ Greater-than-expected competition, lowering DSI's bargaining power and, in turn, profit margins.
- ▶ Client or project exposure, although we believe the worst is over in terms of project cancellations and suspensions.
- ▶ High dependence on few key executives. DSI is managed, and its business strategies formulated, by a relatively small number of key executive officers and other personnel. The loss of these key personnel could have an adverse effect on the company.
- ▶ Variability of quarterly operating results. We believe the margin of error to revenue, margin and earnings forecasts is high when considering quarterly performance compared to year-end estimates. This is typical for contracting companies using the percentage of completion method to recognise revenue.
- ▶ Receivables risk. As a result of the financial crisis, DSI agreed less stringent payment terms with clients than were initially proposed. The company's receivables days-in-hand has lengthened therefore from 133 days at end-2008 to 190 days as at September 2009. DSI confirms that there are no issues with specific client payment, and we believe that the risk has diminished since the start of the year.

The company's cash position is more than sufficient to cover any shortfall in working capital but lengthier receivables or potential non client payment would be a key downside risk, in our view.

- ▶ Corporate governance issues. According to DSI, DSG owns MEP contracting companies in Qatar, Kuwait, Bahrain, Oman, Egypt and Saudi Arabia. Where possible, DSI management would outsource MEP services of a contract to its sister companies owned by DSG (Drake and Scull Group), DSI's parent company, which currently owns 5% of DSI. DSI plans to lower its outsourcing levels by acquiring a majority share in its sister companies. There is limited information disclosed on the size and ownership structure of DSI's sister companies.

Operations & market opportunity

- ▶ All three of DSI's divisions are heavily exposed to the residential and commercial projects market...
- ▶ ...our least preferred construction segment, given the limited amount of new work and the oversupply of capacity resulting in loss of bargaining power
- ▶ The faster DSI expands into non-residential construction, the greater the earnings growth opportunities, in our view

Summary

- ▶ DSI's backlog is **heavily reliant on** our least preferred construction market of **Dubai** and the construction segment of **residential and commercial work**.

DSI January 2010 backlog estimate by market and segment

(AEDm)	Total	MEP	IWP	Civil
Dubai	761	631	88	42
Abu Dhabi	360	30	67	262
Saudi Arabia	145	14	131	-
Kuwait	70	-	-	70
Europe	193	-	193	-
Qatar	166	166	-	-
Others	428	257	171	-
Total	2,123	1,098	651	374
% of total	-	52%	31%	18%

Source: DSI, HSBC estimates

- ▶ While project suspensions, cancellations and contract revisions appear to be over since the start of 2010 and we think the worst is behind us, the supply/demand balance for MEP and civil contracting continues to be in favour of clients and not contractors.
- ▶ **The faster DSI expands into the higher margin and faster growth infrastructure sector, the more positive our earnings growth outlook would be.**
- ▶ The acquisition of Passavant-Roediger was a step in the right direction, but, before this, DSI's **infrastructure, water and power (IWP) division had only been exposed to district cooling projects**, demand for which is linked to mega residential and commercial developments.
- ▶ We expect 2009 to represent the trough for contractor backlogs, but the peak for margins; outside the infrastructure space, we forecast deteriorating margins until 2011.
- ▶ We calculate the MEP projects pipeline in the GCC at USD136bn, of which USD20bn (down from USD70bn pre crisis) represents more imminent projects as tenders have already been issued to contractors. One-third of the total GCC MEP market comes from Saudi Arabia.

Market opportunity

The market has bottomed

Our analysis shows that actual spending on infrastructure, mainly transportation, power and utilities, outside of Dubai, is up following the crisis. DSI has yet to fully tap into the opportunities offered by the infrastructure sector and, in the medium term, the outlook for the residential and commercial projects market will remain the determinant of DSI's backlog growth.

In our view, the residential and commercial projects market has bottomed. Project suspensions, cancellations and contract revisions appear to be over since the start of 2010. We think the worst is behind us and that we may start to see these suspensions gradually come back to the market.

Saudi Arabia (7% of backlog) and Abu Dhabi (17% of backlog) are the markets that we expect to lead the Gulf region into recovery. However, these markets are not enough to lead to backlog growth, or even backlog replenishment, for residential contractors because of the rise in competition following the project standstill in Dubai. The latter alone represented c30% of 2008 construction spend and at least 35% of planned projects pre-crisis relative to the GCC region as a whole, over 90% of which was in the residential and commercial space. Without a pick-up in Dubai, contractors based there will continue to search the region for project awards, especially Abu Dhabi and Saudi Arabia. This will eat away at the market share of existing players and put pressure on profit margins.

Further, the majority of Saudi Arabia and Abu Dhabi's spending plans are geared towards general public infrastructure – such as power and utilities, transportation and, in selective markets, oil & gas. The planned infrastructure build-out in the GCC is actually higher than pre-crisis levels, as is the case worldwide. We are therefore more

positive on contractors exposed to infrastructure-related sectors. In the case of DSI's more diversified scope of work, the faster the company expands into infrastructure and water, the more bullish we would be.

Indirect exposure to Nakheel

Despite the restructuring proposals agreed for Dubai World and Nakheel, the latest data from Dubai on the contracting market indicate that spending has not been reinstated as yet.

Nakheel's restructuring proposal

- ▶ Equitisation of the USD1.2bn due to the Government of Dubai, with an injection of cUSD8bn of new funds from DFSF, subject to a closing of the restructuring.
- ▶ Near-term projects to be completed using a significant proportion of new funds provided by DFSF.
- ▶ Trade creditors offered 100% recovery, through a 40% cash payment (to be made soon), with the remaining 60% in the form of a publicly traded securities at a commercial rate.
- ▶ Imminent payment of up to AED0.5m to each of Nakheel's creditors. This is anticipated to halve the number of creditors.
- ▶ Bank creditors to receive 100% of principal and accrued interest or profit through either a rollover/extension on existing facilities referencing EIBOR/LIBOR (secured creditors) or a new debt facility (unsecured creditors).

Impact on broader market

While DSI has zero direct exposure to Nakheel, we think there is a significant indirect impact on the broader market.

We believe the Nakheel restructuring proposal faces the following headwinds:

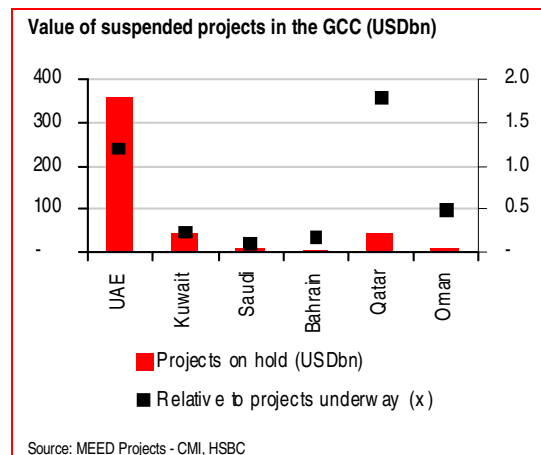
- ▶ Loss of trust with end-user customers means that instalment payments could be delayed, resulting in a longer cash conversion cycle as contractors' receivables mount. We have seen this throughout the crisis, and continued construction without stronger guarantees that customers will not walk away from their contract is likely to mean greater receivables.
- ▶ Re-tendering of contracts could result in more delays. Local contractors are likely to opt to continue working on Nakheel-related projects, which had been suspended, but we are sceptical that the same would apply to regional and foreign contractors, which, we believe, have left Dubai over the past two years. This means Nakheel or the sub-developer would have to re-tender some work, requiring a lead time of no less than six months.
- ▶ Contractors face severe working capital issues, and we do not believe Nakheel's payments will fully rectify this. Banks, which could relieve these issues for contractors, may be less willing to fund working capital on Nakheel-related projects.

We calculate that the total value of Nakheel's projects – where it is both a project owner and shareholder – is close to USD110bn, but it is difficult to quantify the value of outstanding work, and which of these projects are near completion and are likely to be re-initiated by Nakheel.

A buyers' market

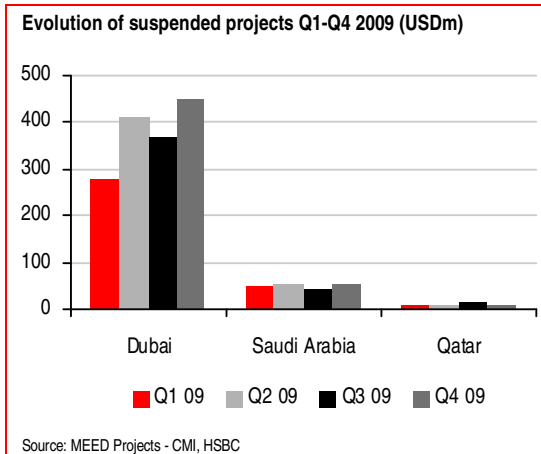
The supply/demand situation in the GCC residential and commercial projects market is in favour of developers or clients. Going into 2010, the total value of projects on hold in the GCC as a result of the financial crisis stood at close to USD630bn. This is equivalent to 70% of projects that are under construction. The sheer value of

suspended work, especially in the UAE, has left an abundance of contractors looking for work. It is for this reason that we believe contractors are in a buyers' market. Contract awards are now more likely to be subject to competitive tendering as opposed to direct one-on-one negotiation, further evidence of increased contracting supply.



In the MENA region, just 7%, or USD64.5bn, of the USD946bn worth of deals planned for 2009 were awarded in first seven months of the year, according to regional projects tracker MEED Projects-CMI. Although developers have delayed awards on infrastructure schemes, the main cause of the shortfall is the real estate sector, in particular the suspension of activity on the multi-billion-dollar master-planned cities that developers want to build across the region.

Although the market started to bottom out in Q3 2009, Dubai World's announcement increased the number of troubled projects in Dubai in Q4 2009.



The number of tender bidders for each project in the GCC residential and commercial projects market comprises at least six and as many as 12 bidders now, according to industry participants. Also, there is an increasing trend towards contractors partnering up to bid – a sign of the need to lower competition and increase market share.

Post vs pre crisis pipelines

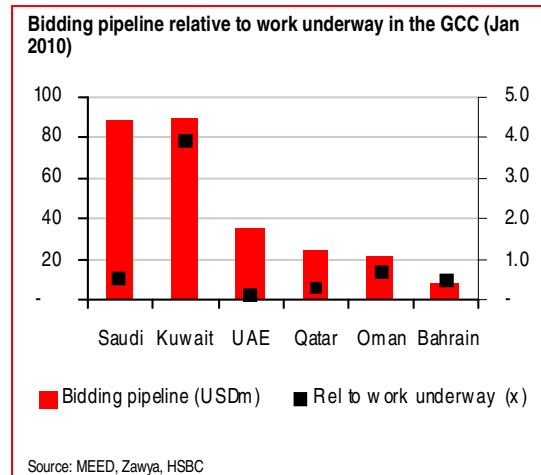
Defining the market

Government statements translate into a build-out in the GCC of over the USD2trn mark (no time frame set). Abu Dhabi's most recent announcement (2 November 2009) to spend USD1trn on major infrastructure, property and manufacturing projects over the medium term is a case in point. There is not much detail in the announcement and the scale of such a build-out could be undermined by Dubai's continued indebtedness.

Given the crisis, we believe a closer look at the pipeline of the GCC's planned USD2trn of spending is warranted. There are also higher than average lead times associated with construction projects during crisis periods.

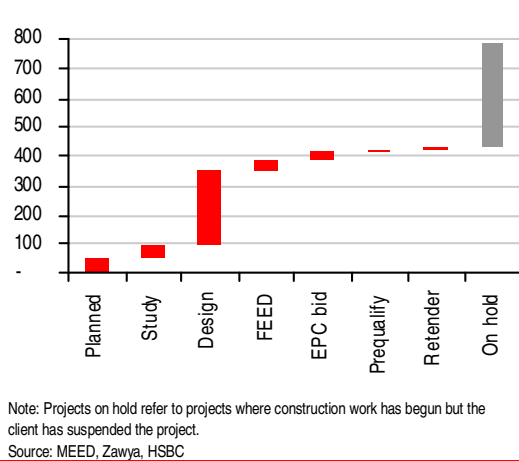
Across our coverage of Middle East construction stocks, we use the value of projects where clients have invited contractors to bid for projects as pipelines. This more advanced stage for projects

suggests a higher likelihood of a contract award, given that the client has spent time and money on project design, government approvals, consultants and, equally important, has secured project financing.



In the UAE, developers are currently inviting contractors to tender close to USD29bn – 4.4% of the announced pipeline, of which engineering, procurement and construction (EPC) contractors have pre-qualified for almost half of this, implying that contract awards are imminent. To put this into context, the bidding pipeline represents less than 10% of work under construction in the UAE alone, and less than 5% if we were to include projects that were under construction but on hold as a result of the crisis. The remaining 96% of the UAE's USD790bn pipeline we would consider as long term. We think it is too early to assume timelines for projects in the design phase will come to the market under the current economic conditions in the UAE, especially because the majority of these projects are either residential or commercial projects.

Breakdown of UAE pipeline by project status – Oct 2009 (USDbn)



lesser extent, regional contractors, in favour of local players for two reasons. First, the government will be the main spender and public entities usually prefer to work with domestic operators, where expertise is available. Second, we expect to see foreign contractors, especially Asian players, relocate capacity in their domestic markets, or at least just maintain existing capacity in the GCC. This comes on the back of unprecedented growth in state spending on public infrastructure in some Asian countries, notably China.

A primer on DSI operations

Electro mechanical & plumbing services

Working alongside the main civil contractor, electro mechanical and plumbing contractors can take on many types of projects; industrial, commercial and residential. Primary activities include providing distribution systems for electrical power, low-voltage systems heating, ventilation, AC, refrigeration, district cooling, plumbing, lighting systems, process and high purity piping systems.

In MEP (mechanical, electrical and plumbing) contracting services, the company works directly

MEP services of a building can range from 15% to 60% of the total construction cost, depending on the facility type, ie hotel, commercial, residential or other, and, based on average backlog figures, represents 30% of the total EPC contract. This puts our estimate for the MEP market in the GCC at USD20bn, given that approximately 25% of this pipeline falls under the residential and commercial projects market. This compares to a pre-crisis pipeline of USD70bn.

More awards to domestic players

We expect to see a lower share of infrastructure construction projects allocated to foreign and, to a

Defining the MEP services market in the GCC

(USDm)	Total pipeline	of which EPC bid/pre-qualified	% of total pipeline	% of projects put on hold	% of work underway
UAE	786,761	34,460	4.4%	9.6%	11.6%
Saudi Arabia	479,706	88,480	18.4%	223.0%	53.2%
Qatar	123,554	24,449	19.8%	285.5%	27.2%
Oman	74,824	21,971	29.4%	398.8%	68.1%
Kuwait	288,030	89,991	31.2%	219.3%	393.5%
Bahrain	60,487	9,296	15.4%	106.2%	50.8%
Total GCC	1,813,362	268,647	14.8%	58.0%	42.8%
MEP services					
UAE	59,007	2,585			
Saudi Arabia	35,978	6,636			
Qatar	9,267	1,834			
Oman	5,612	1,648			
Kuwait	21,602	6,749			
Bahrain	4,537	697			
Total GCC	136,002	20,149			

Source: MEED, Zawya, HSBC estimates

with the project developers (including corporations, municipalities and other governmental entities, owners/developers, and tenants of buildings) as a part of contract team or as a subcontractor to the main civil contracting company. The MEP contractor is the second-largest contractor on site after the main EPC contractor.

The 1990s oil boom attracted regional MEP contractors to the UAE market, such as ETA Star (not listed), BK Gulf (not listed) and Voltas (VOLT.BO, INR183, N(V)), a subsidiary of Tata Group in India. Voltas' services represent the main competition to DSI in the UAE MEP market, although the market remains relatively fragmented, especially in Abu Dhabi. According to HSBC analyst, Sandeep Somani, Voltas is planning to expand more aggressively into new markets such as Oman and Saudi Arabia. Currently, more than two-thirds of Voltas' project backlog is represented by projects in Qatar and Abu Dhabi. An invitation to bid is often conditional on prior experience, technical capability and financial strength, and we believe Voltas ranks competitive to DSI on all these counts, with the exception of on-ground experience in the UAE and supplier relationships.

Based on 2007 data compiled by Deloitte, DSI's market share in each of Dubai and Abu Dhabi was 6%, with different players competing in each market.

UAE MEP contracting market share data (2007)

Dubai		Abu Dhabi	
ETA	20%	EEI	10%
Thermo	8%	MAPCO	8%
Trans Gulf	8%	Pivot	8%
BK Gulf	6%	Al Jaber Group	7%
DSI	6%	Thermo	5%
Others	52%	DSI	6%
		Others	56%

Source: Deloitte

Competitive factors in the MEP services business include: the availability of qualified and/or licensed personnel; reputation for integrity and quality;

safety record; cost structure; relationships with customers; geographic diversity; ability to control project costs; and experience in specialized markets; and adequate working capital.

The MEP division, currently c52% of backlog, generated the majority of DSI's 9M 2009 revenue, with a net margin of 15.4%

DSI's MEP divisional performance

(AEDm)	Q1 2009	Q2 2009	Q3 2009	9M 2009
Revenue	290	290	255	844
% of group	59.4%	56.6%	63.9%	57.3%
Gross profit	59	58	63	180
Gross margin	20.3%	20.0%	24.7%	21.3%
Net profit	47	37	46	130
Net margin	16.2%	12.8%	18.0%	15.4%
% of group	60.9%	42.7%	66.7%	55.9%

Source: DSI

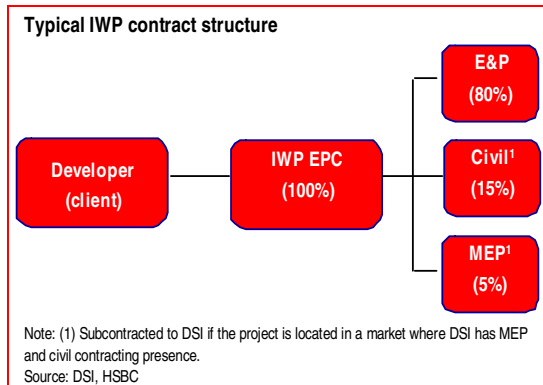
Infrastructure, water and power services

DSI's infrastructure, water and power (IWP) services, established in 2006, entail design & build projects in:

- 1 Water treatment: sewage treatment & distribution, sewage pumping & storage, infrastructure works, centralised chilled water generation.
- 2 Distribution: power generation & distribution, oil and gas distribution & storage, street & airport lighting, data and communication infrastructure.

DSI is the leader in the region for the design and building of district cooling projects. The IWP unit operates on an EPC (engineering, procurement and construction) and EPCM (engineering, procurement and construction management) basis, taking on a project management role. This means that in-house, project management, engineering and procurement is carried out in-house, with construction sub-contracted either to its own civil contracting division, or a local company if the project is outside of the UAE. The construction

sub-contracts are paid on a lump sum basis, lowering the risk to DSI's project profitability.



This division currently represents c31% of DSI's backlog; with existing contracts being water sector projects (90%) after DSI acquired 82% in Passavant Roediger, or district cooling plants (10%).

A district cooling system (DCS) distributes thermal energy in the form of chilled water from a central source to multiple locations through a network of underground pipes. It consists of three primary components: the central plant; the distribution network; and the consumer system. The use of a central cooling plant eliminates the need for separate systems in individual buildings.

District cooling systems are new alternatives to ordinary air conditioning systems and have a number of advantages over regular air cooled chillers in that they save energy, reduce construction costs, increase revenue generating area and are environmentally friendly. DCS consume around 50% less energy (electricity) than air cooled chillers. Furthermore, total government investment on per KW of electricity is AED12,605 for air cooled chillers and on average around AED6,267 for DCS. Also, they have a significantly longer operating life, higher operating efficiency and greater reliability.

Given its capital intensity, district cooling is feasible in areas with appreciable concentration of cooling loads, such as industrial complexes, high rises, densely populated urban areas and high density

building clusters. A single district cooling plant can satisfy the cooling needs of several buildings and customers, through a network of underground pipes. On the contrary, district cooling is usually not viable in residential villa compounds, due to high construction costs and areas that require low cooling capacities, due to economic viability.

Possible locations for district cooling

Institutional	Commercial	Tourism	Residential
Military complexes	Office towers	Hotels	High-rise towers
Government buildings	Shopping malls	Stadiums	Housing compounds (non-villas)
Universities & schools	Industrial parks	Amusement parks	
Hospitals	Airports	Cinemas	
Mosques	Ports	Theatres	

Source: Tabreed

The advantages of district cooling can be split into three categories: infrastructure, economic and environmental. These advantages are shared by building owners and development projects and thus are key factors in the decision to switch to or start using district cooling. Regional governments are keen to use district cooling because of its potential. Press sources including MEED point to the fact that on large new developments, Dubai Electricity and Water Authority (Dewa) is limiting the supply of air conditioning power to that sufficient for district cooling, making the use of single-building chiller systems impossible.

There are still obstacles to district cooling taking off. The tendency to subsume utility bills in overall monthly rental payments means that residential offtakers might not see the decrease in prices. District cooling is also costly, at an estimated USD2,700 per TR, including plant and pipeline network. Correct tariff setting, accurate load estimates, careful consideration of project costs and attention to initial capital costs, given payback periods of 20 years and more, are all essential for district cooling developers. Financing in the past has not been difficult for district cooling

plants because government involvement in real estate construction has ensured its availability. Going forward, there may be limited government funds, especially in Dubai.

The popularity of district cooling is to a large extent correlated to the boom in real estate developments, in our view. Our concern, however, is that there is limited new developments of large enough scale to justify investment in district cooling and its accompanying plant.

DSI's IWP division, 31% of current backlog, generated 18.5% of group 9M 2009 revenue, with a net margin of 8.4%.

DSI's IWP divisional performance

(AEDm)	Q1 2009	Q2 2009	Q3 2009	9M 2009
Revenue	99	92	76	273
% of group	20.3%	18.0%	19.0%	18.5%
Gross profit	11	19	11	41
Gross margin	11.1%	20.7%	14.5%	15.0%
Net profit	7	11	5	23
Net margin	7.1%	12.0%	6.6%	8.4%
% of group	9.1%	12.7%	7.3%	9.9%

Source: DSI

Wastewater and water treatment market

Passavant-Roediger (82% owned by DSI, 18% by Bilfinger Berger) has advanced research and development centres for wastewater, water and sludge treatment, providing high quality solutions including: raw water treatment; desalination/demineralisation; ground water and surface water treatment; treatment of residues; municipal wastewater treatment; industrial wastewater treatment; sludge treatment; mechanical & biological waste treatment .

The past real estate boom resulted in as much as a 20% increase in the GCC region's sewage needs since 2005. Kuwait and the emirates of Dubai and Abu Dhabi have experienced some of the highest annual growth in sewage inflows, putting pressure on the region's sewerage infrastructure.

The global financial crisis has eased the growing pressure on Gulf's utilities. In Dubai, for example, prior to the downturn forecasts suggested inflows could reach 700,000 cm/d by 2010, a figure which is no longer regarded as accurate. Dubai's leading real estate developer Nakheel appears to share this view – in the first three months of 2009, it reduced in scope or cancelled a number of large-scale wastewater projects as a result of the correction in the Dubai real estate market. Our view is that utilities across MENA will need to invest in wastewater projects due to:

- 1 Ageing infrastructure
- 2 High rates of indigenous population growth (Saudi Arabia, Egypt)
- 3 Cost for new greenfield sewage treatment plant is down 20-30% y-o-y in 2009
- 4 Gulf target of 100% reuse of treated sewage effluent within the next few years

There is already USD22bn worth of wastewater treatment projects across the GCC underway. The pipeline in the GCC currently shows a further USD11.9bn worth of projects being tendered, with the UAE representing close to half of the opportunity.

Water sector projects tender pipeline

Market	(USDm)
UAE	5,648
Kuwait	2,290
Saudi Arabia	2,051
Qatar	785
Oman	735
Bahrain	380
Total GCC	11,889

Note: Pipeline classified as projects where contractors have been invited to tender, an EPC contractor has pre-qualified or a contract is being re-tendered.
Source: MEED Projects, HSBC

Dubai's only existing sewage treatment plant at Al-Aweer is being overused – its designed capacity is 260,000 cubic metres a day (cm/d) of wastewater, but at its peak use was treating as

much as 475,000 cm/d at the end of 2008, up from c460,000 cm/d in 2007, according to MEED.

Abu Dhabi's wastewater infrastructure is in a similar situation. With a design capacity of 360,000 cm/d, the plant is treating 475,000 cm/d at peak times in 2008.

We expect to see the greatest shortage in Saudi Arabia, with a requirement for 2.2m cm/d in extra wastewater treatment capacity, followed by the UAE, which MEED expects to need 1.3m cm/d more. To increase water and wastewater network coverage to 100% – sewage collection currently covers only 45% of the country – Saudi Arabia is planning to invest USD40bn in its sewage collection and treatment, and water distribution infrastructure over the next 20 years.

DSI's sister company has a presence in Egypt, which would be synergistic for Passavant-Roediger. Our database of projects suggests that Egypt's spending plan on water sector projects is the highest within the MENA region. The most imminent water sector projects fall within the government's PPP (public-private partnerships) spending plan, shown below, at a total cost of USD1.02bn.

Water sector projects in Egypt		
Project	Capacity (m ³ /day)	Cost (USDm)
Water treatment projects		
Red Sea (with pipelines)	90,000	405
Aswan	75,000	28
Ismailia	52,000	18
Wastewater projects		
Alexandria	1,000,000	424
Giza plant	200,000	110
Alexandria (expansion)	100,000	37
Total	1,517,000	1,022

Source: Ministry of Finance, Ministry of Investment, Egypt, MEED

We think the main competition to DSI's wastewater treatment business in the Middle Easter region is Metito (not listed) which is UAE-based and international player Veolia Water (not listed).

Civil contracting services

The primary activities of the civil contracting services division are infrastructure work (cabling/piping); design & build turnkey projects involving district cooling, sewage treatment and water purification; operation & maintenance of projects and independent execution of low and high rise buildings. This division suffers the most competition, but from a strategic perspective adds value to the business.

DSI began in-house civil contracting operations in January 2007, after acquiring 80% of Gulf Technical Construction Company (GTCC), its civil contracting arm for USD43.1m. The rationale of the acquisition was to lower sub-contracting levels for cost saving purposes and faster project execution. Also, developers in the MENA region generally prefer to work with contractors with lower outsourcing levels.

This division can also take on third party work. We calculate that 50% of DSI's civil contract awards since 2007 were third party work.

The civil contracting division, 18% of the current backlog, generated 24% of DSI's 9M 2009 revenue, with a net margin of 9.3%.

DSI's civil contracting divisional performance				
(AEDm)	Q1 2009	Q2 2009	Q3 2009	9M 2009
Revenue	119	130	99	356
% of group	24.4%	25.4%	24.8%	24.2%
Gross profit	17	28	21	66
Gross margin	14.3%	21.5%	21.2%	18.5%
Net profit	6	17	10	33
Net margin	5.0%	13.1%	10.1%	9.3%
% of group	7.8%	19.6%	14.5%	14.2%

Source: DSI

Forecasts

- ▶ Potential for contract awards higher than industry average
- ▶ 2010-11 earnings depressed by less lucrative backlog additions
- ▶ Strong cash position allows for potential upward revisions to forecasts

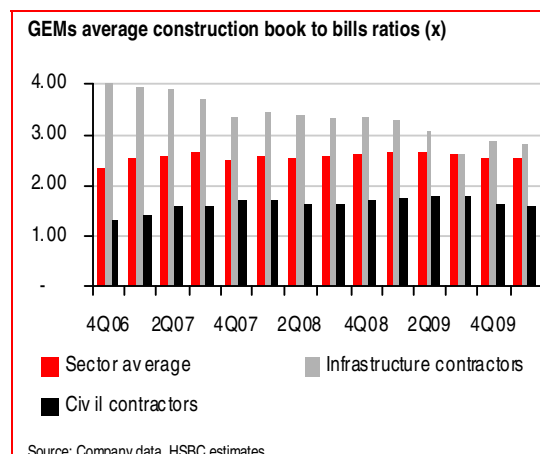
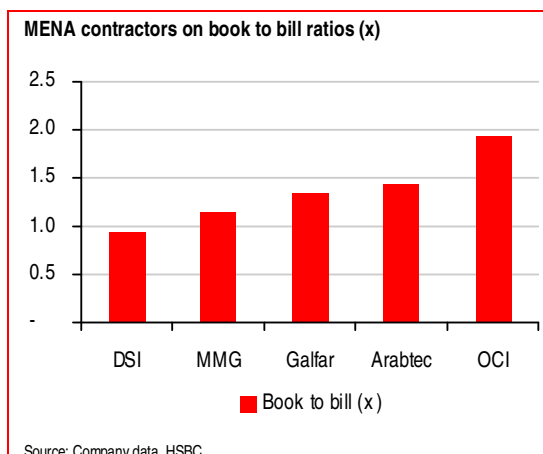
Backlog

We calculate DSI's 2010 opening project backlog at AED2.1bn (USD544m), equivalent to 1x 2009 sales. Our backlog estimate strictly includes projects where there is an official letter of award to DSI.

We calculate the average age of DSI's backlog is 12 months, assuming no delays. The average completion rate for DSI's contracts on our estimates is 30%, but relative to the total EPC contract, we believe the completion rate is over 60%, especially for the MEP division (c50% of backlog). This lowers the risk of project suspension or contract revisions. Relative to our MENA coverage, project concentration also ranks well: the largest three projects on DSI's book together represent less than 30% of the total. The single largest project is c12% of backlog.

Compared with other contractors in MENA under HSBC coverage, DSI's backlog offers lower visibility. The average book to 2009 bill is 1.4x versus 1.0x for DSI.

The cyclical nature of construction is important in this respect, but more important is the contracting expertise of the company. The following chart shows the evolution of book to bill ratios for HSBC's average GEM construction coverage. We include infrastructure project contractors as part of the sector average, but also separately to show the relatively higher book to bill ratio. We think the premium for infrastructure contractors' book to bill ratios will expand further because of the unprecedented amount of infrastructure spend that should work its way through to the market as the recovery takes hold.



2009 is the trough for backlog, but peak for margins

We believe DSI's backlog has troughed after only adding AED1.5bn (AED1.8bn including acquired backlog) in 2009, down c35% y-o-y. Developers were at a standstill for the most part of 2009, even outside of Dubai, waiting for property prices to bottom and given the deflation occurring in construction costs.

We estimate that market activity in the UAE will continue to be around two-thirds of what it was in 2008. This lower demand environment should result in DSI's market share dropping by 2%.

We look for AED3.6bn of new awards in 2010 for DSI (+142% y-o-y) and AED3.9bn in 2011 (+7%), based on the following assumptions:

- ▶ A reasonable share of DSI's awards during 2009 came from projects that were already underway when the financial crisis hit.
- ▶ Approximately 60% of awards will be civil contracting work thanks to synergies from MEP and IWP. Our addition assumptions in the IWP division from the company's recently acquired wastewater treatment business are conservative, at approximately AED500m per annum.
- ▶ Our 2010 new awards estimate of AED3.6bn includes Q1 2010 awards of AED1bn.
- ▶ Our model excludes potential additions on the back of the announced intentions for inorganic growth..

DSI: backlog breakdown and new award assumptions

(AEDm)	2010e	2011e	2012e	2013e	
Backlog execution	1,576	312	55	2	
% of revenue	74.30%	14.70%	2.60%	0.10%	
Backlog breakdown by region	Backlog breakdown by division				
Dubai	35.80%	MEP	52%		
Abu Dhabi	17.00%	IWP	31%		
Europe	9.10%	Civil	18%		
Qatar	7.80%				
Saudi Arabia	6.80%				
Kuwait	3.30%				
Other	20.20%				
	2009	2010e	2011e	2012e	2013e
New awards assumptions	1,495	3,618	3,876	4,076	4,288
% y-o-y	-33.70%	142.00%	7.10%	5.20%	5.20%
Closing backlog (AEDm)	1,976	3,725	5,571	7,503	9,575
Closing backlog (USDm)	538	1,014	1,516	2,042	2,606
% y-o-y	-26.60%	88.50%	49.50%	34.70%	27.60%

Source: DSI, HSBC estimates

Unified industry costs mean DSI's above-average margins likely to see most pressure

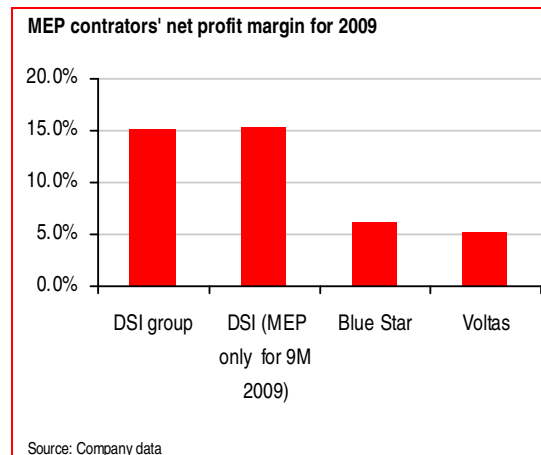
The cost structure of MEP contractors is heavily dependent on the cost of raw material procurement, which typically represents 60% of the total costs of a project. We estimate that direct labour costs are 10% and overheads, such as management prelims and corporate costs, account for the remaining 30% of the project cost.

The significant majority of DSI's MEP contracts are fixed price contracts, which is an industry norm. The terms of these contracts would require DSI to guarantee the price of its services and assume any risk that the costs associated with its performance will be greater than the company anticipated. DSI primarily sources raw materials from local suppliers. The main materials procured by the company are air compressors, air handling units, aluminium cladding, chillers, generators, grills & diffusers, transformers, valves, water storage tanks, water transfer pumps, public address systems, sprinklers, fuel transfer pumps, fan coil units, fire detection systems, fire extinguishers, and central emergency battery systems.

We believe fixed price or lump sum contracts are higher margin than cost plus contracts, as clients are willing to pay a premium to the contractor for visibility of the project cost. Maintaining fixed price project profitability even during inflationary times will then be a function of the effectiveness of the contractor's cost management skills. Larger contractors are able to hedge against the rise in material prices through long-term contracts and quantity discounts with their material suppliers. This takes advantage of their ability to carry large inventories, but is not a balance sheet risk, in our view, as it is passed down the value chain.

In turn, MEP contractors to a large extent have unified cost structures, yet DSI's profit margins on

its MEP business alone are almost two-fold the industry average (15.5% in 9M 2009) and that of its key competitor, Voltas (5.2% for 2009). The lack of financing charges for DSI, given its strong cash position, also helps inflate the company's net margin.



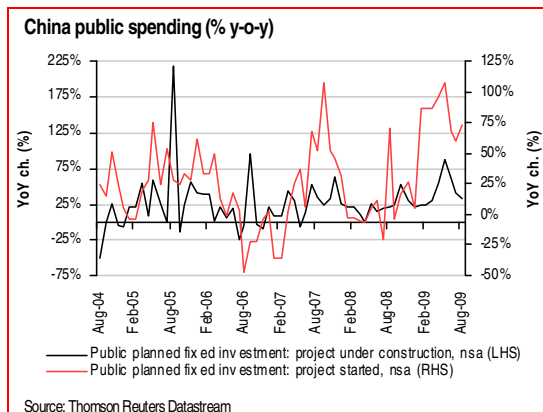
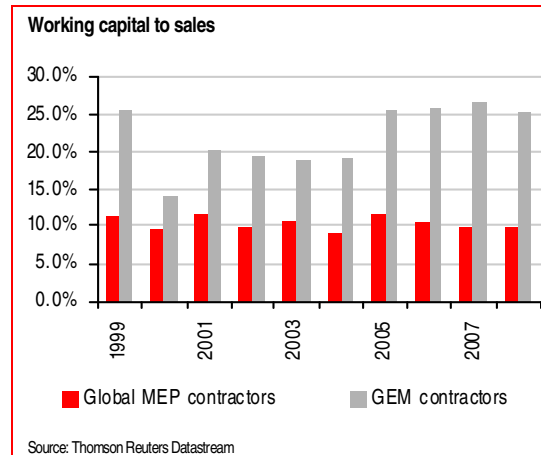
Given our view that the financial crisis and the resulting slowdown in Dubai has left contractors in the region in a buyers' market, we think there is relatively higher downside to DSI's margins than its peers. Due to high-priced backlog execution, margins in 2009 and H1 2010 should hold up relatively well, while H2 2010 and 2011 should start to see a gradual deterioration.

DSI also boasts above industry average profitability for its civil contracting business, where we also see downward pressure on margins because of the oversupply.

For infrastructure, water and power projects, on the other hand, we think sector profit margins should hold up well. The region plans to invest more in infrastructure, water and power than it did pre-crisis. Against this, the supply of more specialised infrastructure contractors in the region is becoming increasingly limited, as foreign contractors leave to take on the higher volume of domestic projects. In total, we estimate that foreign contractors' share of the infrastructure projects market in the GCC was 25-30% over 2005-08 and regional contractors' share was approximately 18%.

The most obvious case in point is China's domestic infrastructure investment, which is up 70% since the crisis. The value of fixed asset investment in water provision and sewerage grew 61% y-o-y in August 2009 and 29% y-o-y in electric and heating power. The respective figure for general public utilities was 43%. On a cumulative basis, the value of projects under construction as a result of planned public FAI grew by 36.2% y-o-y in the first eight months of 2009. The respective figure for project starts was 81.7%. HSBC forecasts public construction output in China will grow by 28.0% in FY 2009, 18.5% in 2010 and a further 12.8% in 2011. Our forecasts are underpinned by the RMB4trn stimulus package, which is focused on infrastructure investment.

average ratio, excluding cash – and 10% for global MEP contractors.



Civil contracting companies have two categories of suppliers: distributors of materials and components and sub-contractors which provide specialised services (such as electrical installation or bricklaying) and this varies by type of project. The relatively low level of consolidation in the cement and steel industry translates into relatively low supplier power, but this is less of the case with other materials, such as cables, for instance, which is a more consolidated industry. DSI also has strong bargaining power over its sub-contractors, because of the fragmented nature of these companies in MENA.

Cash position supportive of working capital funding

Working capital represented a source of cash for contractors in the MENA region during the boom times. The chart below illustrates how, as construction markets started to pick up, contractors improved working capital via more favourable supplier terms. Contractors continue to have relatively good negotiating power with suppliers compared with other emerging markets, with delays in receivables mostly passed down the value chain.

DSI raised AED1.22bn (USD332.6m) through its IPO in March 2009, the majority of which continues to sit on the company's balance sheet, locked into bank deposits yielding 6-8.5%. This leaves the company in a strong net cash position and so raising working capital funding from banks is less of an issue for DSI, even in the UAE.

Our view is that working capital across the sector should deteriorate, but remain in positive territory. In 2008, the GEM construction sector working capital/sales average was 25% – in line with DSI's

Income statement summary

(AEDm)	2008	2009	2010e	2011e	2012e	2013e	2012e	2013e
Revenue	1,720	2,212	1,869	2,030	2,143	2,216	2,343	2,477
% y-o-y	n/a	28.6%	-15.5%	8.6%	5.6%	3.4%	5.7%	5.7%
% secured by backlog	n/a	n/a	84.4%	15.3%	2.6%	0.1%	0.1%	0.1%
Contract costs	(1,396)	(1,776)	(1,521)	(1,685)	(1,784)	(1,845)	(1,951)	(2,063)
Gross profit	324	436	348	344	359	371	392	415
Gross profit margin	18.8%	19.7%	18.6%	17.0%	16.8%	16.7%	16.7%	16.7%
SG&A expenses	(168)	(183)	(146)	(142)	(107)	(89)	(94)	(99)
EBITDA	181	285	256	258	311	346	367	391
EBITDA margin	10.5%	12.9%	13.7%	12.7%	14.5%	15.6%	15.7%	15.8%
Depreciation	25	32	19	21	24	29	34	41
Amortisation	-	38	35	35	35	35	35	35
EBIT	156.0	215.4	202.2	202.3	252.3	282.4	298.4	315.4
EBIT margin	9.1%	9.7%	10.8%	10.0%	11.8%	12.7%	12.7%	12.7%
Interest income	12	94	35	29	32	34	39	42
Finance cost	(9)	(17)	(13)	(7)	(6)	(5)	(5)	(5)
Management fees	(14)	(17)	(15)	(16)	(17)	(18)	(19)	(20)
Other income	68	62	-	-	-	-	-	-
Net profit after tax & minority	210	334	200	199	251	283	301	319
% y-o-y	n/a	59%	-40%	-1%	26%	13%	7%	6%
Net profit margin	12.2%	15.1%	10.7%	9.8%	11.7%	12.8%	12.9%	12.9%
EPS	0.10	0.15	0.09	0.09	0.12	0.13	0.14	0.15
% y-o-y	110%	59%	-40%	-1%	26%	13%	7%	6%

Source: DSI, HSBC estimates

Cash flow statement summary

(AEDm)	Nov-08	Dec-09	Dec-10e	Dec-11e	Dec-12e	Dec-13e
Operating income	174.9	229.3	262.5	262.9	320.4	357.7
Change in current assets and liabilities						
Development Properties	17.1	(15.3)	6.1	(2.9)	(2.0)	(1.3)
Inventories	1.1	54.9	1.9	(1.2)	(0.7)	(0.4)
Contract WIP	(74.7)	(8.5)	58.2	(37.6)	(22.5)	(13.9)
Contract Receivable	(186.5)	(296.3)	164.7	(15.0)	(17.3)	1.5
Due From Related Party	(14.3)	(18.6)	6.1	16.7	16.7	0.0
Prepayments and Other Receivable	(74.4)	(31.4)	38.2	(17.9)	(12.6)	(8.1)
Accounts Payable and accruals	158.0	(64.7)	(118.9)	72.2	(5.7)	25.1
Due to related parties	(142.9)	(18.1)	(11.7)	5.5	3.9	2.5
Advances received from customers	126.0	(96.6)	(30.8)	14.5	10.2	6.5
Excess billings	5.1	70.8	(14.1)	9.1	5.5	3.4
Net cash used in operating activities	(10.6)	(194.5)	362.3	306.3	295.8	373.0
Cash flows from investing activities	(4.0)	44.4	(16.0)	(17.3)	(18.2)	(17.7)
Loan to a related party						
Payment for purchase of fixed assets and other assets	(97.0)	(20.9)	(126.2)	(52.8)	(78.9)	(106.3)
Net cash flow used in investing	(98.5)	(342.8)	(126.2)	(52.8)	(78.9)	(106.3)
Cash flows from financing activities						
Term Loan	166.9	352.6	(222.6)	(82.0)	(66.3)	(32.0)
Interest Paid	(7.2)	(17.1)				
Movement in TD & Bank ST	46.6	(302.7)				
Dividends Paid	0.0	0.0	(212.5)	(59.6)	(75.2)	(84.8)
Net cash flow provided by financing activities	1,401.1	1,283.5	(435.1)	(141.6)	(141.5)	(116.7)
Net increase in cash and cash equivalent	1,291.9	746.2	(199.1)	112.0	75.3	149.9
Cash and cash equivalent opening balance	32.4	0.0	746.2	547.1	659.1	734.4
Others	77.7	(2.9)	(2.9)	(2.9)	(2.9)	(2.9)
Cash and cash equivalent closing balance	1,402.1	743.2	544.1	656.1	731.4	881.3

Source: DSI, HSBC estimates

Balance sheet

(AEDm)	Nov-08	Dec-09	Dec-10e	Dec-11e	Dec-12e	Dec-13e
Development properties	21.1	39.4	33.3	36.1	38.1	39.4
Inventories	2.1	12.9	11.0	12.2	12.9	13.4
Contract WIP	226.2	405.1	346.9	384.5	407.0	420.9
Contract receivables	520.0	983.9	819.1	834.2	851.5	850.0
Due from related Parties	14.7	39.6	33.4	16.7	0.0	0.0
Prepayments and other receivables	115.1	246.0	207.8	225.8	238.4	246.5
Trading securities	12.1	135.1	135.1	135.1	135.1	135.1
Loan to a shareholder	45.0	95.9	95.9	95.9	95.9	95.9
Bank balances and cash	1,402.1	1,160.3	961.2	1,073.2	1,148.5	1,298.4
Total current assets	2,358.4	3,118.2	2,643.9	2,813.8	2,927.5	3,099.6
Non current assets						
Gross property plant and equipment	220.4	242.9	369.1	421.9	500.8	607.1
Less accumulated depreciation	(48.9)	(31.4)	(50.5)	(71.8)	(96.2)	(124.9)
Net fixed assets	171.5	211.5	318.6	350.1	404.6	482.2
Goodwill	830.5	474.5	474.5	474.5	474.5	474.5
Other intangible assets		347.3	312.6	277.8	243.1	208.4
Other non current assets	12.6	249.0	249.0	249.0	249.0	249.0
Total long term assets	1,014.6	1,282.4	1,354.7	1,351.5	1,371.3	1,414.2
Total Assets	3,372.9	4,400.6	3,998.6	4,165.3	4,298.8	4,513.8
Current liabilities						
Accounts payable and accruals	531.9	785.5	666.6	738.8	733.1	758.2
Due to related parties	17.0	75.2	63.5	69.0	72.8	75.3
Advances received from customers	280.9	198.5	167.7	182.2	192.4	198.9
Due to Banks	83.8	122.2	122.2	122.2	122.2	122.2
Term loans	168.6	381.3	190.6	140.6	106.3	106.3
Excess billings	27.5	98.3	84.2	93.3	98.8	102.1
Total current liabilities	1,109.6	1,660.9	1,294.9	1,346.1	1,325.6	1,363.1
Non current liabilities						
Employee end of service benefit	19.8	34.6	34.6	34.6	34.6	34.6
Term loan	9.5	159.9	127.9	95.9	64.0	32.0
Due to related parties	0.0	29.8	29.8	29.8	29.8	29.8
Total non current liabilities	29.2	224.2	192.3	160.3	128.3	96.3
Total liabilities	1,138.9	1,885.2	1,487.1	1,506.4	1,453.9	1,459.4
Capital and reserves						
Share capital	2,177.8	2,177.8	2,177.8	2,177.8	2,177.8	2,177.8
Statutory reserves	0.0	33.7	53.7	73.5	98.6	126.9
Pre incorporation profit	42.0	0.0	0.0	0.0	0.0	0.0
Fair value adjustment reserve	0.0	(6.7)	(6.7)	(6.7)	(6.7)	(6.7)
Retained earnings	0.0	300.7	268.5	387.7	538.1	707.7
Treasury shares		(28.6)	(28.6)	(28.6)	(28.6)	(28.6)
Total shareholders' equity	2,219.7	2,476.8	2,464.6	2,603.7	2,779.2	2,977.0
Minority interest	14.3	38.6	46.9	55.2	65.7	77.4
Total equity	2,234.1	2,515.4	2,511.5	2,658.9	2,844.9	3,054.4
Total liabilities	3,372.9	4,400.6	3,998.6	4,165.3	4,298.8	4,513.8

Source: DSI, HSBC estimates

Notes

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Disclosure appendix

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DRAKE & SCULL INTL	DSI.DU	0.89	28-Apr-2010	1, 4, 5

Source: HSBC

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