

<u>Recommendation</u>	<u>Previous</u>	<u>From date</u>	<u>52-week target</u>
Market Perform	-	-	BGN 18.10

## Polimeri

### Business Summary

Polimeri was established in 1961, when the first plant for production of chlorine and polyvinylchloride started its operation. In late 70's was put in operation the second plant for chlorine and polyvinylchloride. Later on an installation for production of dichlorethane with a total annual capacity of 120 thousand tons, designed by Toyo Engineering, Japan started its operation. In 1991 was started a new chlorinealkyne electrolyze, licensed by HUCKER. Polimeri is the sole Bulgarian producer of chemical products, based on the chlorinealkyne electrolyze like sodium acid, chlorine, chlorine acid, dichlorethane, bleach, ferrichloride, etc. Half of the production is sold abroad, mainly to Turkey.

### Current Market Activity

Shares of Polimeri moved above the level of BGN 14.00. The current price activity could mark a period of consolidation or even correction which will provide better entry levels. The difficulty to jump above BGN 15.00 is due to the higher multiples than the averages for the market. Most of the buyers entered the position last year with the anticipation of change in ownership, followed by the needed investments in new equipment. This created additional volatility. Institutional investors also acquired minority stakes in Polimeri. The position moved in line with the market and also posted correction after January's peak. Volumes were higher during the period of stable prices in January which is due to larger transactions and could provide support for the price in short-term.



### Financial Summary

Polimeri improved its financial results during the first half of the year but mainly due to the revenues from currency exchange rates. Costs decreased slightly as a percentage of revenues. However, the positive effect was subdued by imposed act by the tax administration totaling BGN 1.3 million. The audited report of 2006 financial statement showed three problematic points: deferred tax liabilities for BGN 3.344 million not included in the balance sheet; expired receivables for BGN 11.299 million without confirmations; investments in associated companies for BGN 3.215 million without information for the value of those investments.

### Valuation Ratios

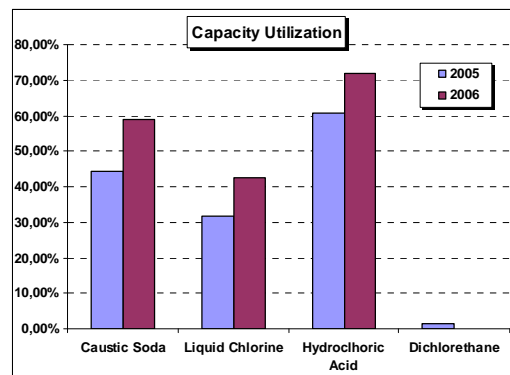
Enterprise Value	74 674 672
Dividend Yield - Gross	-
Trailing P/E (ttm)	59.20
Forward P/E (2007)	28.55
PEG Ratio (5yr expected)	-
Price/Sales (ttm)	1.67
Price/Book (mrq)	0.78
Enterprise Value/Revenues (ttm)	1.67
Enterprise Value/EBITDA (ttm)	17.02

### Profitability and Growth Ratios

Return on Capital	1.48%
Return on Equity	1.32%
Return on Assets	1.17%
EBITDA Margin	9.79%
Net Profit Margin	2.87%
Revenue Growth	12.05%
EPS Growth	157%
Capital Growth	2.20%
Assets Growth	6.32%

## Production Specifics

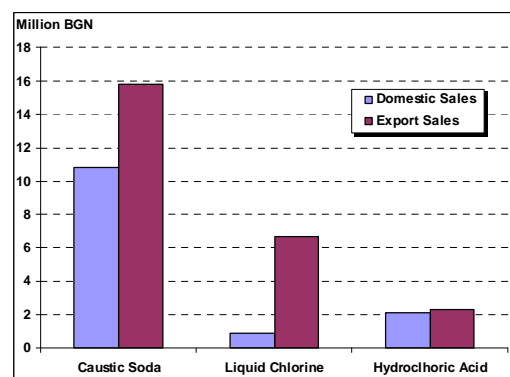
Polimeri is working at low capacity utilization for all its products and sales could rise substantially. The company is using chlor-alkali electrolysis for the production of liquid chlorine. The electrolysis process to manufacture chlorine and its essential co-product caustic soda requires considerable electrical power which represents up to 70% of the variable cost of production. However, it is less energy-intensive and more environmental friendly process than using mercury cells. Polimeri replaced the old mercury electrolysis in 1983. Several years ago, the company sold its equipment for production of PVC to cover debts.



Source: Polimeri  
Calculations: ELANA Trading

## Markets

Polimeri is relying on the exports for its revenue growth during the last several years. Sales abroad of hydrochloric acid posted the higher growth in 2006, which compensated the decrease of domestic sales of the product. Export of dichlorethane ceased in 2006 due to the lack of special transportation terminal which also requires investments. Polimeri is exporting its production to clients in Turkey, Romania, Bosna and Macedonia. Domestic market demand is rising slower last year. Main domestic clients are the paper mill Svilosa, producers of glass containers and power plants. Svilosa is planning to increase substantially its capacity in 2008 and we can expect solid growth of caustic soda sales.



Source: Polimeri  
Calculations: ELANA Trading

## Quarterly Data

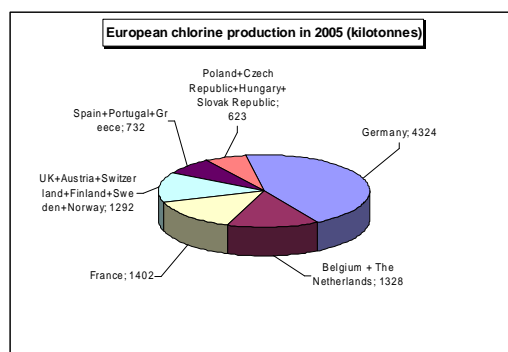
Sales of Polimeri aren't under any seasonal pattern. The last three years showed solid increase of revenues and lower growth of production volumes. The company managed to increase the exports and to maintain the solid growth rate. EPS showed higher volatility as the net profit of Polimeri is under the influence of exchange rates and the extraordinary items. In addition, Polimeri is source of financing for related companies, including soccer team. The company is buying resources from salt mine which also supplies Solvey Sodi and is not seasonally dependant.

Revenues/Earnings Data				
Revenues (Thousand BGN)				
	2004	2005	2006	2007
1Q	4 437	9 081	11 135	12 059
2Q	4 840	8 839	10 563	12 254
3Q	8 196	10 014	n/a	
4Q	11 026	11 080	n/a	
Year	28 499	39 014	43 881	
Earnings per Share (BGN)				
	2004	2005	2006	2007
1Q	-0,03	0,46	0,10	0,10
2Q	-0,02	0,30	0,01	0,17
3Q	0,08	0,22	0,30	
4Q	-0,02	-0,77	-0,18	
Year	0,00	0,22	0,23	

Source: Polimeri  
Calculations: ELANA Trading

## Perspectives

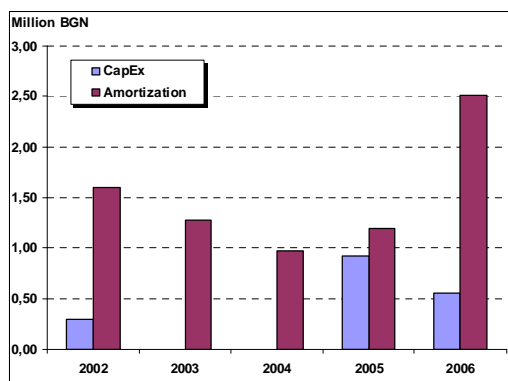
The stable economic growth in Europe provides good environment for chlorine producers. However, some companies closed their mercury production facilities and switched to membrane technology or exited this sector. European capacity utilization rates averaged 85% during last three years. Germany is the largest producer, followed by France. The strong demand of caustic soda kept average stocks at historically low levels. Among western peers only Bayer is operating facilities that use chloroalkyne electrolyze. Most of the companies are vertically integrated chemical producers that guarantee sales.



Source: Euro Chlor Association

## Investment Program

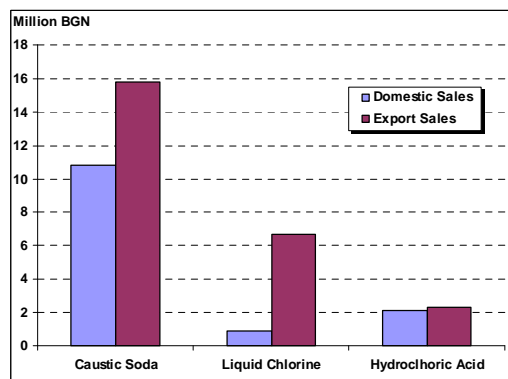
Polimeri decreased slightly its electricity costs after the adoption of direct negotiations with power plants. The company has own co-generation facility but is relying on electricity from the national grid for the electrolyze. The capital expenditures are well below the amortizations. Polimeri is in process of acquiring assets for BGN 2.9 million, mainly for the production of pipes. The company has an ambitious investment program for EUR 20 million and 8 years of accomplishment. It includes conversion to membrane technology, modernization of production facilities, energy efficiency and production of household chemistry goods.



Source: Polimeri  
Calculations: ELANA Trading

## Ecology

The ecology problems of chemistry facilities near Devnya are inherited from the industrialization of the region. Polimeri joined the "Responsible Care" World Initiative of the enterprises in the chemical industry. EU regulations are covering large varieties of chlorinate organic compounds, which emissions should be reduced. The carbon dioxide emissions by electricity producers also are limited and the rising energy consumption will require additional expenses from power plants that could be transferred to consumers through higher electricity prices.



Source: Polimeri  
Calculations: ELANA Trading

## Ownership

The ownership is divided between the Panamanian company JURISKANDO CONSULTANTS with 36.60% of the capital and AKB Fores with 24.80%. Both company bought their shares in the second half of 2006 from AKB Corporation and this could be restructuring of ownership and not real change.

## Stock Information

Last Price	14.00	Market Cap	74 543 182	1Y Range	4.97-14.46	Average Volume (3m)	2 287
Beta	-	1Y Change	+181.12%	SOFIX Change	+73.30%	BG40 Change	126.62%

## Valuation

Prices of Polimeri shares jumped solidly and the valuation ratios also increased as the financial results were unable to sustain such growth. The market is pricing in lots of good news and only the positive perspectives for the company.

### Multiples Analysis

Most multiples of Polimeri are above the market averages for Bulgarian industrial companies. Moreover, the expected profit for 2007, based on 15% sales growth and slightly improved margins, also shows forward P/E multiple above 30. The ratio that currently supports the price is P/B of 0.78. The market capitalization is lower than the shareholders' equity and could provide additional support for the price in short term horizon. However, better profits are required to support further price gains as the P/E and EV/EBITDA ratios are high. The low capacity utilization resulted in the combination of higher P/S and low P/B.

Last Price	14,00
Number of Shares	5 324 513
Market Capitalization	74 543 182
Net Profit (ttm)	1 261 000
P/E	59,11
Revenues (ttm)	44 805 000
P/S	1,66
Equity	95 318 000
P/B	0,78
EV	74 568 182
EBITDA	4 388 000
EV/EBITDA	16,99
EV/Revenues	1,66

Source: Polimeri  
Calculations: ELANA Trading

### Peers Comparison

Most of the chlorine facilities in Europe are owned by large multinational companies like Solvay, Rhodia, BASF, Dow Chemical and Bayer. They are vertically integrated companies that can afford to maintain very low margins in the chlorine and caustic soda production. Peers with similar profile are the two Czech companies and the Romanian Oltchim. BASF and Akzo Nobel production of chlorine and caustic soda have EBIT margin of 12% and 9.5%, respectively. Polimeri has lower EBIT margin which will bear the burden of tax act and the volatile currency rates this year.

		P/E	P/B	P/S	EV/EBITDA	EV/Sales	RoA	RoE	EBITDA Margin	EBIT M	Net M
Tessenderlo Chemie	Belgium	57,70	1,63	0,50	7,32	0,65	1,13%	2,58%	8,90%	3,00%	0,86%
Spolek Pro Chem	Czech Rep.	10,25	0,63	0,26	6,97	0,64	2,14%	6,02%	9,22%	4,03%	2,72%
Spolana Neratovice	Czech Rep.	6,11	0,84	0,18	4,28	0,42	4,80%	14,64%	10,93%	4,34%	3,02%
Arkema	France	48,53	1,63	0,50	9,21	0,55	0,87%	2,25%	5,93%	2,24%	1,08%
Ercros	Spain	218,18	1,05	0,44	6,46	0,44	0,55%	1,46%	6,82%	1,67%	0,21%
Oltchim	Romania	310,98	10,87	2,01	32,65	2,00	0,87%	3,50%	6,13%	1,57%	0,64%
Solvay	Belgium	12,58	3,64	0,97	7,24	1,18	6,29%	17,12%	16,23%	10,87%	7,67%
Rhodia	France	37,18	n/a	0,63	6,96	0,98	1,85%	n/a	14,07%	7,92%	1,75%
BASF	Germany	13,93	4,61	0,83	5,77	1,00	8,58%	18,16%	17,37%	12,63%	6,56%
Bayer	Germany	23,93	n/a	1,28	10,16	1,67	3,44%	11,41%	16,46%	9,48%	5,32%
Akzo Nobel	Netherlands	21,80	4,95	1,41	8,99	1,53	6,59%	20,81%	14,66%	10,02%	6,98%

Source: Reuters

## Price Target

The imposed act by the tax administration makes 2007 profit uncertain. However, the improved profit margins due to higher capacity utilization, electricity generation and investments in new equipment will result in better net profits for 2007 and 2008. Increased production of paper mill Svilosa will also contribute to sales. Our price target for end-2007 is in the range between BGN 14.49 to 17.16 based on the expectations for 35 P/E and 0.80 P/B ratios.

	2006	2007	2008
Revenues	43 881 000	50 463 000	58 032 000
EBITDA	4 558 000	5 551 000	6 964 000
Net Profit	1 246 000	2 611 000	3 883 000
Equity	93 854 000	96 465 000	100 348 000
Expected P/E		35	30
Price Target		17,16	21,88
Expected P/B		0,80	1,00
Price Target		14,49	18,85

Calculations: ELANA Trading

## Recommendation

The one year target for mid-2008 is the average of the two ranges for end-2007 and end-2008 or **BGN 18.10**. The two ratios P/E and P/B have equal weight for the calculation but the more conservative approach is the calculation by P/B. Any positive earning surprises could turn the attention to profits. If Polimeri maintains the sales growth in 2008, which looks probable due to the expected increase of domestic demand and the economic boom in the region, P/E of 30 to 35 could send share price above BGN 20. Moreover, the news of majority ownership change could also provide solid support for Polimeri shares.

The one year price target of BGN 18.10 is 29% above the current level and is in line with our expectations for at least 30% increase of Bulgarian stock market for the same period. This is the reason to give Market Perform recommendation for Polimeri shares. The company's financial results are volatile and any negative surprises will raise the question for the risks of corporate governance, collection of receivables and energy inefficient production.

## Financial Data

Statement of Income (in thousand BGN)	2002	2003	2004	2005	2006
Sales	34 806	27 304	28 499	39 014	43 881
Production expenses	28 504	22 453	23 486	34 349	32 637
Personnel expenses	4 903	4 660	3 124	4 044	4 720
Net income from financial activities	311	1 155	(738)	2 055	(1 966)
Other revenues and expenses	92	64	143	0	0
EBITDA	1 802	1 410	1 294	2 676	4 558
Depreciation	1 598	1 274	968	1 197	2 515
EBIT	204	136	326	1 479	2 043
Interest expense	(16)	(102)	(259)	(99)	(168)
Pretax income	188	34	67	1 380	1 875
Taxes	107	18	42	212	629
Net income	81	16	25	1 168	1 246
Earnings per share in BGN	0,015	0,003	0,005	0,22	0,23
Balance Sheet (in thousand BGN)	2002	2003	2004	2005	2006
Total Assets	145 257	66 950	67 761	100 659	103 626
Equity subscriptions receivable	0	0	0	0	0
Fixed assets	124 553	42 966	42 935	69 021	64 754
Tangible fixed assets	101 792	18 361	17 725	52 806	51 148
Financial investments	3 492	3 492	3 493	3 435	3 376
Current assets	20 704	23 984	24 826	31 638	38 872
Inventory	2 407	2 852	3 287	3 365	2 999
Receivables	18 235	20 842	21 407	27 896	35 504
Financial assets and cash	62	289	84	252	247
Total liabilities + equity	145 257	66 950	67 761	100 659	103 626
Equity	135 080	55 060	55 863	92 482	93 854
Registered capital	5 325	5 325	5 325	5 325	5 325
Capital funds	129 572	130 972	131 706	162 327	85 427
Earnings	183	(81 237)	(81 168)	(75 170)	3 102
Liabilities	10 177	11 890	11 898	8 177	9 772
Long-term payables	0	1 331	553	2 490	1 573
Long-term bank loans	0	0	0	0	0
Short-term bank debt	754	929	0	0	0
Short-term payables	9 423	9 487	11 345	5 687	7 348
Other liabilities	0	0	0	0	0
Working capital	10 527	13 568	13 481	25 951	31 524

## Financial Data

Cash Flow Statement (in thousand BGN)	2002	2003	2004	2005	2006
Net income	81	16	25	1 168	1 246
Depreciation	1 598	1 274	968	1 197	2 515
Changes in Working capital	3 055	3 041	(87)	12 470	5 573
Other operating cash flow items	(770)	(5 892)	(3 010)	(13 516)	(7 503)
<b>Net cash from operating activities</b>	<b>3 964</b>	<b>(1 561)</b>	<b>(2 104)</b>	<b>1 319</b>	<b>1 831</b>
Capital expenditures	(290)	0	0	(923)	(561)
Other investing cash flow items	0	1 799	1 899	71	(2 230)
<b>Net cash from investing activities</b>	<b>(290)</b>	<b>1 799</b>	<b>1 899</b>	<b>(852)</b>	<b>(2 791)</b>
Issuance/ Retirement of Stock, Net	0	0	0	0	0
Issuance/ Retirement of Debt, Net	(4 295)	0	0	(299)	955
Dividends paid	0	0	0	0	0
Other financing cash flow items	0	0	0	0	0
<b>Net cash from financing activities</b>	<b>(4 295)</b>	<b>0</b>	<b>0</b>	<b>(299)</b>	<b>955</b>
<b>Net change in cash</b>	<b>(621)</b>	<b>238</b>	<b>(205)</b>	<b>168</b>	<b>(5)</b>
Beginning-of-period cash	1 092	51	289	84	252
End-of-period cash	471	289	84	252	247
<b>Cash per share</b>	<b>0,09</b>	<b>0,05</b>	<b>0,02</b>	<b>0,05</b>	<b>0,05</b>
<b>Number of shares:</b>	<b>5 324 513</b>	<b>5 324 513</b>	<b>5 324 513</b>	<b>5 324 513</b>	<b>5 324 513</b>
<b>Price in BGN - period end:</b>	<b>0,45</b>	<b>0,57</b>	<b>1,60</b>	<b>5,59</b>	<b>5,04</b>
<b>Financial and Performance Indicators</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>
<b>Valuation Ratios</b>					
Price/Earnings (P/E)	29,58	189,69	340,77	25,48	21,54
Book Value (BV)	25,37	10,34	10,49	17,37	17,51
Price/Book (P/B)	0,02	0,06	0,15	0,32	0,29
Sales Per Share	6,54	5,13	5,35	7,33	8,24
Price/Sales (P/S)	0,07	0,11	0,30	0,76	0,61
Price/Cash flow	1,43	2,35	8,58	12,59	7,14
EV (in BGN)	3 088	3 675	8 435	29 512	26 589
EV/Sales	0,09	0,13	0,30	0,76	0,61
EV/EBITDA	1,71	2,61	6,52	11,03	5,83
EV/EBIT	15,14	27,02	25,87	19,95	13,01
<b>Liquidity</b>					
Current ratio	2,03	2,30	2,19	5,56	5,29
Quick ratio	1,80	2,03	1,90	4,97	4,88
<b>Debt Management</b>					
Debt to total assets	7,0%	17,8%	17,6%	8,1%	9,4%
Interest coverage	12,75	1,33	1,26	14,94	12,16
LT Debt/Equity	0,00	0,02	0,01	0,03	0,02
Total Debt/Equity	7,53%	21,59%	21,30%	8,84%	10,41%
<b>Asset Management</b>					
Inventory turnover	14,46	9,57	8,67	11,59	14,63
Days sales outstanding	189	275	270	257	291
Fixed asset turnover	0,28	0,64	0,66	0,57	0,68
Total asset turnover	0,24	0,41	0,42	0,39	0,42
<b>Profitability</b>					
Profit margin on sales	0,2%	0,1%	0,1%	3,0%	2,8%
EBITDA margin	5,2%	5,2%	4,5%	6,9%	10,4%
Basic earning power	0,1%	0,2%	0,5%	1,5%	2,0%
Return on assets	0,1%	0,0%	0,0%	1,2%	1,2%
Return on equity	0,1%	0,0%	0,0%	1,3%	1,3%
Return on investments	0,1%	0,0%	0,0%	1,2%	1,3%
<b>Dividend Information</b>					
Dividend Yield	n/a	n/a	n/a	n/a	n/a
Dividend per share	n/a	n/a	n/a	n/a	n/a
<b>Number of shares:</b>	<b>5 324 513</b>	<b>5 324 513</b>	<b>5 324 513</b>	<b>5 324 513</b>	<b>5 324 513</b>
<b>Price in BGN - period end:</b>	<b>0,45</b>	<b>0,57</b>	<b>1,60</b>	<b>5,59</b>	<b>5,04</b>

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<b>Positive</b>	More than 5% higher as compared to SOFIX and BG40 performance
<b>Neutral</b>	Market performance, +/-5% as compared to SOFIX and BG40
<b>Negative</b>	More than 5% lower as compared to SOFIX and BG40 performance

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