

Saipem

Backlog, margin improvement and profit guidance support our positive stance

- Saipem's 4Q net income of €18m was well ahead of the €100m market consensus. EPS of €0.27 was up 13% q/q and 114% y/y. The dividend was raised 53% to €0.29/share, giving a 1.5% yield.
- **Strong margin improvement.** In our view the key feature of 4Q results was a sharp improvement in overall EBIT margin to 8.5% vs 7.5% in 3Q. This was driven by a jump in onshore margins to 5.5% vs 3.6% in 3Q, a much faster improvement from the integration of Snamprogetti than we had expected.
- **Backlog bodes well.** Saipem's backlog reached a record of €3.2bn at end-4Q vs €1.28bn at end-3Q, with particularly strong q/q growth from offshore drilling. Furthermore, management highlighted another €1.5bn of new orders so far in 2007.
- **Good growth guidance.** Management's initial guidance for 2007 is for revenues of at least €9bn (+20%) and growth in net income of at least 20%, implying income of over €460m (€1.04/share).
- **Estimates:** we have raised our revenue estimates slightly, but our EPS changes are broadly neutral (see p2). We are confident in our 07E projections given that our forecast EBIT margin of 8.3% is below the 4Q actual, and not much above the 2H06 average.
- **Target price raised to €23/share.** Saipem remains our top pick in the European Services sector and we see nothing in the latest newsflow to change this view. We have raised our multiple-based year-end price target to €23/share from €22 (see p2) and see good prospective catalysts in several forthcoming West African deepwater awards in 1H07.

Saipem (SPMI.MI;SPM IM)

	2005A	2006E	2007E	2008E	2009E
Adj. EPS FY (€)	0.58	0.92	1.13	1.41	1.64
Cash EPS FY (€)	1.14	1.39	1.73	2.07	2.33
Dividend (Gross) FY (€)	0.15	0.18	0.20	0.21	0.24
Revenue FY (€ mn)	4,528	7,505	9,002	10,047	11,315
EBITDA FY (€ mn)	561	810	1,003	1,197	1,337
EBIT FY (€ mn)	366	614	751	924	1,051
EBIT margin FY	8.1%	8.2%	8.3%	9.2%	9.3%
Net Attributable Income FY (€ mn)	255	406	497	624	724
Adj P/E FY	34.9	22.0	17.9	14.3	12.3
EV/CF FY	24.26	14.75	11.92	9.99	8.94

Source: Company data, Reuters, JPMorgan estimates.

Overweight

€20.22

21 February 2007
Price Target: €23.00

Integrated Oils - Europe

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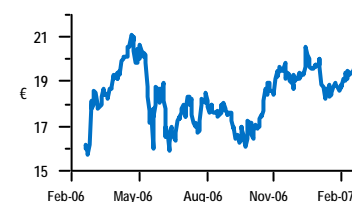
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Price Performance



	YTD	-1M	-3M	-12M
Absolute	0.6%	7.3%	3.9%	24.0%

Source: RIMES, Reuters.

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Company Data

Price (€)	20.22
Date Of Price	21 Feb 07
52-week Range (€)	21.33 - 13.85
Mkt Cap (€ bn)	9.1
Fiscal Year End	Dec
Shares O/S (mn)	450

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Investment view

Saipem remains our top pick among the European Oil Services stocks in our coverage. We discussed our investment view on Saipem in a comprehensive report published in October ([Strong growth catalysts - upgrading to overweight](#), 19/10/06). We find nothing in the latest results or company outlook to alter this view.

There are four main reasons for our positive view:

- Exposure to what we see as the two strongest areas of industry spend over the next few years: deepwater developments and LNG liquefaction. As an integrated player, Saipem is arguably less cyclical than other niche players.
- Three new major pieces of capex that we think will materially affect earnings from 2008 onwards: the Gimboa FPSO, the Scarabeo 8 semi-submersible drilling unit, and a new coldwater pipelay vessel.
- Further scope for margin progression from involvement in LNG liquefaction in the future via Snamprogetti. In Offshore Construction too, the larger size of projects in backlog compared to smaller players also means that higher margins (such as SURF, 12-13%) will naturally take longer to feed through to earnings.
- A significant increase to revenues and margins in offshore construction due to our view of Saipem's prospects for success in a string of projects to be awarded in deepwater West Africa in 2007.

Table 1: Saipem, adjusted EPS changes, 2007-09E (€)

	2007E	2008E	2009E
Adj. EPS			
Current	1.13	1.41	1.64
Previous	1.10	1.43	1.64
Change	3%	-1%	0%

Source: JPMorgan estimates.

EPS changes

We have made minor changes to our EPS estimates, which result in a 3% increase to 2007E but negligible changes thereafter. Beyond 2007, higher revenue projections are largely offset by the effect of higher capex on forecast debt levels.

Valuation

On our estimates, Saipem trades at a 2008E P/E of below 14x, which is the cheapest multiple in our European coverage and close to 15% below Technip. The shares P/CF ratio of 9.4x 08E is also below the sector and Technip (10.1x) but Saipem is more expensive than Technip on EV/CF (11.0x vs 8.7x) due to its much higher balance sheet leverage.

Target price raised from €2/share to €3/share

We have raised our year end 2007 target price to €3/share to reflect increasing confidence in our estimates and as a result, where we think Saipem should trade vs its peers. This target is based on a 2008E P/CF multiple on around parity with Technip, which would be equivalent to around a 5% P/E discount. This looks undemanding to us in view of Saipem's superior record of project delivery.

Risks to our rating and target price: in our view the main generic risks are from a general downturn in capital expenditure in the oil and gas industry, and political instability in key areas of operations such as the Middle East or West Africa. Specific risks could come from failure to secure offshore West African contract wins this year, or a more general slow-down in the backlog trend.

Quarterly comments: [please see our earlier note](#) for more detailed comment

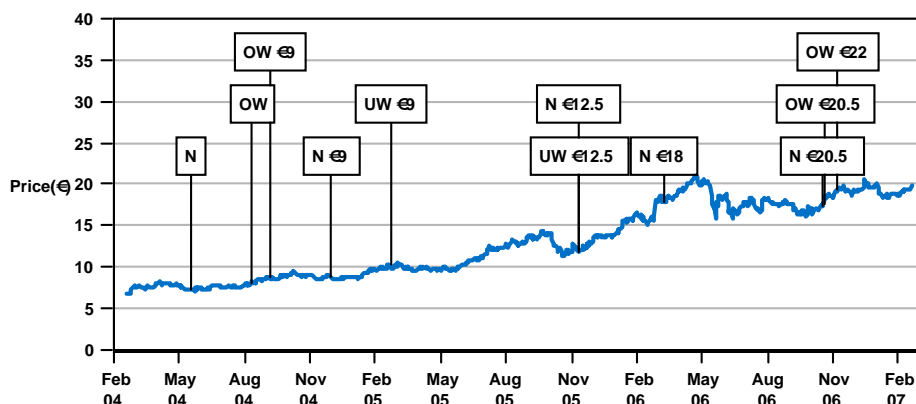
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Saipem (SPMI.MI) Price Chart



Date	Rating	Share Price (€)	Price Target (€)
20-May-04	N	7.19	-
12-Aug-04	OW	8.17	-
29-Nov-04	N	8.89	9.00
21-Feb-05	UW	10.22	9.00
11-Nov-05	N	11.75	12.50
19-Oct-06	OW	17.67	20.50

Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends.
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