

EL.En

Betting on Laser

Buy

Initiation

Current €27.60

Target €33.10

Previous €NA

Current price equivalent

\$40.92

Market cap

€133.2m

\$197.4m

52-week high/low

€36.04/€27.52

Price perf.	1M	3M	12M
Price (€)	31.7	30.7	27.9
Absolute (%)	-13.0	-10.0	-1.1
Rel market (%)	-6.4	-3.8	5.0
Rel sector (%)	-5.4	-5.4	-13.2

EPS change	1M	3M	12M
EPS FY1 (%)	N/A	N/A	N/A
IBES EPS (%)	N/A	N/A	N/A
Sector EPS (%)	-3.9	-4.9	-0.9
Market EPS (%)	N/A	N/A	N/A

Source: DKIB Research, Thomson IBES

Reuters **Bloomberg**
ELEN.MI ELN IM Equity

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Over the last two years EL.En.'s share has been flat. Investor concerns have focused on its suboptimal financial structure and high minorities, which lower the visibility on earnings yields. Some of these issues might be addressed in coming months. Due to the outstanding performance posted in the last quarters, a further 24% fall in the share price since its May peak is unjustified in our view.

EL.En forecasts

Year	Sales EUR m	Gross margin %	EBITA margin %	Pre-tax profit excl except EUR m	Attrib profit excl except EUR m	Dil EPS excl except EUR	P/E x	EV/ EBITDA x	FCF Yield %	Yield %
Dec-2005A	118.3	54.8	(4.3)	15.5	9.6	2.06	13.4	3.8	15.9	2.0
Dec-2006A	154.4	53.3	3.3	7.2	1.6	0.35	79.2	10.4	(8.6)	1.1
Dec-2007E	196.8	55.8	5.6	25.1	4.8	1.00	7.9	8.1	9.2	3.7
Dec-2008E	229.7	56.7	12.5	30.6	6.9	1.42	19.0	6.9	4.0	2.1
Dec-2009E	267.2	57.1	13.1	36.9	8.5	1.76	15.4	5.8	6.2	2.5

Source: Company data, Dresdner Kleinwort Research estimates

- ▶ We initiate coverage of EL.En. with a BUY recommendation and a target of €33.1 per share, corresponding to an upside of 20%. Extraordinary gains of €14m and additional net cash of €21m at the parent company expected at YE07 should bolster confidence and give the stock more speculative appeal.
- ▶ Management commitment to the Chinese, Japanese and Brazilian markets, effective turnaround of some loss-making subsidiaries like Lasercut and Deka Lms and possible EPS benefits from the Italian tax reform to be approved in the coming weeks, represent further catalysts for the stock.
- ▶ Over the last quarters, the group's top line results and margins have been supported by a healthy laser industry. By addressing the fastest growing market niches like liposuction, air removal or skin rejuvenation, EL.En is well placed to benefit from the sustainable fundamentals of laser market.
- ▶ With an estimated 2007 net cash position of €30m at parent company and €84m at group level, combined with a market cap. of €131m, the financial structure is now massively underleveraged. We believe that further delay or lack of visibility on the use of cash should undermine confidence in the stock.

- ▶ EL.En. is a leading laser manufacturer in Europe and one of the main players in the fast growing laser industry. EL.En and its subsidiaries manufacture and market globally multidisciplinary laser systems for industrial and medical applications used in dermatology, aesthetics, physiotherapy, dentistry and gynaecology. Trough Cynosure (Nasdaq CYNO), listed in December 2005, fully consolidated and now 23% controlled, the group addresses the key niches of the aesthetic lasers used to perform a wide range of non-invasive procedures

Online research:

www.dresdnerkleinwort.com/research

Bloomberg:

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including skin rejuvenation, hair removal and cellulite reduction.

- ▶ Over the last four quarters EI.En. has released a strong set of results with Q3'07 revenues at €46.7m, +33.0% yoy, and EBITDA at €6.8m (vs -3.9m in Q3'06). The combination of strong demand and continued operating efficiency have enabled Cynosure to post record results, with US-denominated revenues jumping 70%, reflecting rapid market penetration by products like Smartlipo, BodySculpting workstation and Affirm, a new anti-ageing multi-energy platform. By contrast, volatile trading hit the industrial segment due to higher prices (c€1m per laser) and lower sales volumes.
- ▶ Taking into account an average €/€ exchange rate of 1.38 at YE2007 and 1.45 in 2008, we estimate revenue growth of 15.8% in the next 3 years fuelled by the aesthetic segment and the gradual takeoff of the industrial applications. EBITDA should improve to 20.6% also due to boosted operating efficiency at Lasercut and Deka, which should drive EBITDA margin from 14.2% in 2007 to 16.1% in 2010. Attributable EPS Cagr '07'11 should achieve 41.3%.
- ▶ We consider the aesthetic a killer application with solid and sustainable fundamentals. Ageing baby boomers, affordability and accessibility of treatments, cultural and media influences, cost-effective of minimally/non invasive and safe procedures can improve usage of treatments allowing a deeper penetration into a wide base of consumers worldwide. Moreover target end-user market is recently penetrating wellness and spa centre offering laser applications in addition to traditional dermatologists and plastic surgeons.
- ▶ We see different catalysts for the stock. Year 2007 will end up with strong profits giving to the stock more speculative appeal. In light of the €21m extra cash in stemming from the sale of its 950,000 Cynosure shares announced last week, the parent company should have a positive financial position of c€30m. Due to this transaction, EI.En's Q4'07 earnings will benefit from a €14.0m capital gain with a limited tax impact estimated at €1.0, under the Italian participation exemption rule (33% tax rate over 86% of the capital gain).
- ▶ Following a recent meeting with the management, we have sensed that no M&A projects are imminent and see little likelihood of either an extraordinary dividend distribution or buyback programmes. Nevertheless, the company is strongly committed to speeding up its recent ventures in China, Japan, India and Brazil and to performing an effective turnaround in some loss-making subsidiaries (e.g. Laser Cut). This should further improve sentiment on the stock while decreasing the historical dependence of EI.En.'s earnings on Cynosure and increasing the Group earnings yields due to lower minorities.
- ▶ Though not included in our estimates, we point out that EI.En.'s EPS should benefit from the Italian tax reform, which should reduce corporate tax (IRES) from the current 33% to a proposed 27.5%. Due to its debt-free parent company structure, the Group should not be impacted by the widening of the taxable income base that seems to be in the pipeline.
- ▶ We initiate coverage of EI.En. with a BUY recommendation. Based on a 3-stage DCF and an estimated full equity WACC of 9.6%, we set a target price of €33.1, suggesting an upside of 20%. We have stripped out Cynosure's minorities of €212m and other minorities of €30m from Group EV. The DCF-based valuation of Cynosure's total equity stands at \$33 per share, 19.5% above the current price and in line with the recent transaction of US\$32.65 per share. We highlight that after the sale of Cynosure's share, the elasticity of EI.En. price to a 1 USD fluctuation in Cynosure price stands at 0.42x.
- ▶ At current prices EI.En. adjusted for the minorities is trading at 6.9x EV/EBITDA 08e and 19.0x FY08e. Based on our price target, the stock would trade at 22.6x FY08e, which is not challenging considering that the EPS is expected to grow by 41.3% in the next three years. Stripping out Cynosure's value, we estimate that other Group assets are currently trading at 6.3x EV/EBITDA 08e and 18.4x FY08e.
- ▶ By contrast, low visibility on the use of cash, slower than expected rump-up of the Chinese and Brazilian JV and ineffective turnaround of Lasercut and Deka Lms should undermine investor sentiment and weigh on our bullish view on the stock.

EURm	2005	2006	2007E	2008E	2009E	2010E
Revenues	118.3	154.4	196.8	229.7	267.2	305.3
<i>growth %</i>	25.2	30.4	27.5	16.7	16.3	14.3
Change in inventory	4	6.5	7.8	8.9	10.1	11.2
Other income	2	1.8	1.8	2.1	2.4	2.8
Value of Production	124.3	162.8	206.4	240.7	279.7	319.3
Purchase of raw materials	-50.2	-65	-76.3	-87.5	-101	-114.8
Change in inventory	1.7	1.1	0.9	1	1.2	1.4
Other direct costs	-11	-16.6	-21	-23.9	-27.2	-30.5
Gross Margin	64.8	82.3	109.9	130.3	152.7	175.4
Other operating costs	-23.4	-38.6	-39.6	-46.4	-54.3	-62.3
Value Added	41.5	43.7	70.3	83.9	98.4	113.1
Labour cost	-26.6	-33.1	-42.3	-49	-56.5	-64
EBITDA	14.9	10.7	28	34.9	41.9	49.1
<i>EBITDA Margin %</i>	12.6	6.9	14.2	15.2	15.7	16.1
D&A	-4.9	-5.2	-5.2	-6.1	-6.8	-7.6
EBIT	9.9	5.5	22.8	28.8	35.1	41.5
<i>EBIT Margin %</i>	8.4	3.5	11.6	12.5	13.1	13.6
Net financial income	0.9	2.1	1.5	1.8	1.8	2
Profit of Associated	0	-0.4	-0.1	0	0	0
Other Income/Expences	19.6	0	12.7	0	0	0
EBT	30.5	7.2	36.9	30.6	36.9	43.5
Taxes	-4.4	-4.5	-14.2	-14.2	-15.9	-18.3
Group Net Profit	26.1	2.6	22.7	16.4	21.1	25.2
Minorities	-1.4	-1	-6.1	-9.5	-12.6	-15.1
Net Profit post Minorities	24.7	1.6	16.6	6.9	8.5	10.1

Source: Company data, Dresdner Kleinwort Research estimates

EURm	2005	2006	2007E	2008E	2009E	2010E
Intangible asset	7.4	7.193	7.5	8.3	9.2	9.8
Tangible asset	11.3	13.7	18	20.9	24.1	27.9
Financial asset	4.4	4.9	4.9	4.9	4.9	4.9
Net Fixed Asset	23.1	25.8	30.4	34.1	38.2	42.7
Inventories	32.8	38.6	44.1	50.8	58.8	66.8
Receivables	30.6	36.7	46.8	54.6	63.5	72.6
Other Current Asset	4.8	10.4	13.3	15.5	18	20.6
Trade payables	-20.3	-23.6	-31.4	-36.4	-42.1	-47.6
Other liabilities	-13.4	-15.9	-18.6	-21.6	-24.9	-28.2
Reserve	-4.8	-4.8	-6.1	-7.2	-8.3	-9.5
Working capital	29.8	41.4	48	55.8	65	74.6
Reserve for Personnel	-2.2	-2.6	-3.3	-3.8	-4.4	-5
Net Invested Capital	50.7	64.6	75.1	86.1	98.8	112.3
Short Term Financial Debt	2.2	1.3	2	2	2	2
M/LT Financial Debt	2	1.9	1.9	1.9	1.9	1.9
Cash and Deposit	77.1	24.4	87.4	87.8	93.4	101.7
Treasury Stock	0.5	34	0.4	0.4	0.4	0.4
Net Financial Debt	-73.4	-55.1	-83.9	-84.3	-89.9	-98.2
Group Shareholder Equity	73.7	72.1	87.2	89.1	94.8	101.5
Minorities Shareholder Equity	50.4	47.7	71.8	81.3	93.9	109
Total Shareholder Equity	124.1	119.7	159	170.4	188.7	210.5

Source: Company data, Dresdner Kleinwort Research estimates

EURm	2005	2006	2007E	2008E	2009E	2010E
Beginning NFP	8.7	73.4	55.1	83.9	84.3	89.9
Net income/loss	26.1	2.6	22.7	16.4	21.1	25.2
Depreciation & Amortization	2.8	3.4	3.6	4.3	5.0	5.7
Change in working capital	-7.1	-11.6	-6.6	-7.9	-9.2	-9.6
Net change in reserve	0.5	0.4	0.7	0.5	0.6	0.6
Cash flows from operations	22.3	-5.2	20.5	13.3	17.4	21.9
Intangible assets	-0.1	-0.5	-0.7	-1.1	-1.3	-1.0
Tangible assets	-4.0	-5.9	-7.6	-6.8	-7.8	-9.2
Financial Investments	-1.5	-0.5	0.0	0.0	0.0	0.0
Other change	3.9	0.9	0.0	0.0	0.0	0.0
Cash flows from investing	-1.8	-6.0	-8.3	-7.9	-9.1	-10.2
FREE CASH FLOW	20.6	-11.2	12.2	5.4	8.3	11.7
Change in Equity	45.7	-4.5	18.0	0.0	0.0	0.0
Dividends	-1.6	-2.6	-1.4	-5.0	-2.7	-3.4
Change in NFP	64.7	-18.2	28.8	0.4	5.6	8.3
Final NFP	73.4	55.1	83.9	84.3	89.9	98.2

Source: Company data, Dresdner Kleinwort Research estimates

Disclosure appendix

Disclosures under US regulations

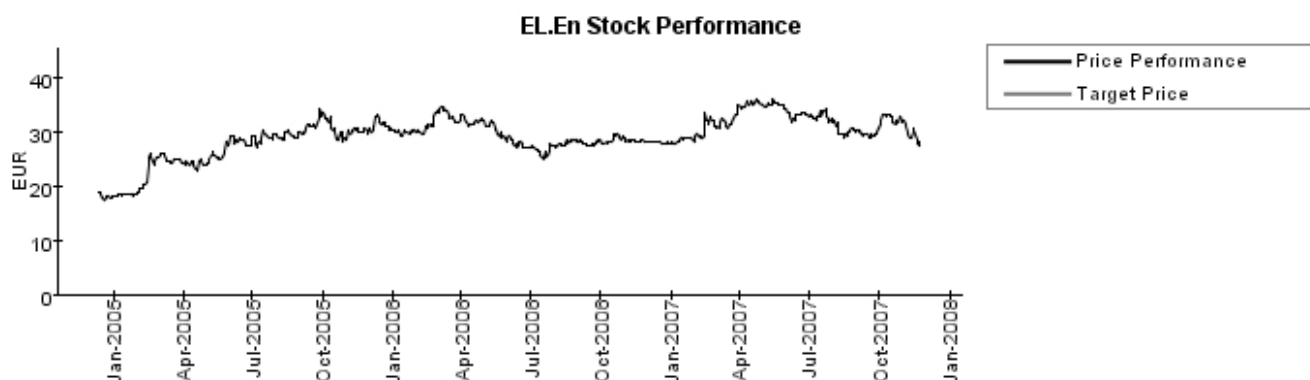
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Buy:	10% or greater increase in share price	Sell:	10% or more decrease in share price
Add:	5-10% increase in share price	Reduce:	5-10% decrease in share price
Hold:	+5%/-5% variation in share price		

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Hold	138	24%	25	18%
Sell/Reduce	69	12%	7	10%
Total	580		148	

Source: Dresdner Kleinwort

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