Solvay's Profit Goal Threatened by Europe Crisis

Brussels-based chemicals and plastics company Solvay wants to increase profits by nearly half in the next four years but some analysts consider this target ambitious given the group's exposure to Europe's ailing construction sector.

Last year, almost a third of Solvay's sales came from its plastics division, which is heavily reliant on demand from Europe's construction industry through PVC used, for example, in drainage pipes and window frames.

Solvay's new boss Jean-Pierre Clamadieu, who took charge on May 11, hopes to achieve the profit goal partly through a focus on higher margin products.

These include consumer chemicals -- used in the production of cosmetics, detergents and agrochemicals -- produced by French rival Rhodia that Solvay bought last year for €3.4 billion.

The deal turned the 150-year old Belgian company into one of Europe's biggest chemical groups. And it has raised expectations among some chemical industry analysts that the new boss will shake up the company, which is also the world's biggest soda ash maker, an ingredient in making glass.

The group still has two members of the founding Solvay family on the board of directors, one of whom, Denis Solvay, owns about 5% of Solvac, which itself owns about a third of Solvay.

Clamadieu, who also headed of Rhodia, has a reputation as a cost-cutter and plans to save €400 million ($511 million) by 2014. But some analysts are not convinced this will be enough to compensate for the difficulties faced by Solvay's plastics division.

He has also said Solvay could consider selling its PVC operations.

Clamadieu's plans have divided analysts over his chances of reaching the profit goal.

According to Starmine, 12 banks and brokerages have Solvay as a buy or a strong buy, while nine recommend holding the stock and five advise selling.
Buy

Clamadieu unveiled his **new target of a recurring core profit (EBITDA) of €3 billion ($3.83 billion) in 2016**, compared with 2.1 billion for 2011 at an investor day in London last month.

He hopes to fuel this with double-digit growth on businesses such as **Solvay's speciality polymers** and **Rhodia's consumer chemicals and advanced materials**, which contributed almost half of Rhodia's recurring core profit in 2011.

"After this capital markets day I became more optimistic on the financial dynamism, more ambitious targets and a different style of management," said ABN AMRO analyst Mark van der Geest.

He upgraded Solvay to "buy" from "reduce" following the event.

Cost-cutting initiatives already helped Solvay beat profit expectations in the first quarter, sending its shares up earlier this month by as much as 12%.

Over the past 12 months, the shares have fallen by around 17%.

UBS believes that Solvay could even beat its 2016 profit target, saying in a note that the target was "conservative".

It has a "buy" recommendation and added Solvay to its Key Calls list last week.

"Mr Clamadieu's track record of restructuring and efficiency delivery at Rhodia is a very supportive precedent and indicator for what can be delivered at Solvay," it said.

Sell

But some analysts have questioned Clamadieu's growth plans in the light of Europe's current economic problems.

Christian Faitz of Macquarie, who has an "underperform" rating, expressed doubts.

"I would say let's see about 2012 first, because that seems to be the more challenging year," he said.

Unemployment in the euro zone equalled record highs in March, while the region's output stagnated in the first quarter.
It means companies are wary about investing in new projects, particularly
construction which is a key customer for Solvay's PVC products.

"We do believe that Solvay has one of the more cyclical portfolios, despite the
Rhodia acquisition, simply because they are fully exposed to ... the general
economy," said Faitz.

Solvay missed analysts' expectations in the fourth quarter after sales of PVC fell
by 10% in Europe.

"We expect Solvay's relatively weak industry positioning to be magnified by
economic weakness in Europe in 2012," say analysts at Goldman Sachs who have a
"sell" rating.

"In our view Solvay remains overvalued on a fundamental basis as the cyclically
exposed businesses remain challenged," said the broker.