

Saudi Basic Industries Co

Overweight

Target price (SAR)	260.00
Share price (SAR)	165.50
Potential total return (%)	57.1

Dec	2006a	2007a	2008e
HSBC EPS	8.20	10.81	11.65
HSBC PE	20.2	15.2	14.2
Performance	1M	3M	12M
Absolute (%)	-15.6	6.8	50.8
Relative ^a (%)	-4.9	-0.6	13.3

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Storm in a teacup

- ▶ **Share price overreaction, in our view, on account of unrealistic Q4'07 expectations and global market weakness**
- ▶ **We see significant long-term value in SABIC Innovative Plastics stemming from access to a specialty asset base, world class supply chain networks, significant raw material offset opportunities, and technology**
- ▶ **We view the recent correction as a buying opportunity; we reiterate Overweight rating and SAR260 target price**

SABIC stock has been very weak since the announcement of the company's Q4'07 and full-year results on 20 January 2008, falling over 25% from its recent high. In our opinion, the company got caught in a perfect storm of events – while the Q4'07 numbers themselves were ahead of our estimates at net income of SAR6.8bn (we were at SAR6.3bn), the thin sell side coverage of the stock makes it susceptible to skews in consensus estimates. In this case, there was at least one estimate at SAR8.8bn, which, in our opinion, wildly skewed expectations, resulting in a perception of weak results that sent the stock down over 10% the day the company reported. Furthermore, the timing of the results, in line with the global sell-off in equity markets, compounded the decline.

Another point of unease in the investor community in recent times has been the May 2007 acquisition of GE Plastics, now called SABIC Innovative Plastics (SIP), and the impact of the acquisition on company margins. We believe that the GE Plastics acquisition was a landmark deal for SABIC that enabled the company to gain access to specialty chemical assets, a world class supply chain and distribution network, technology, and complementary raw material offsets, all of which are critical to SABIC as it pursues its objectives of being a global chemical company. Of all the cost-advantaged companies producing basic plastics in the Middle East, SABIC stands alone in its efforts to broaden its portfolio and geographical reach beyond the region and commodities. Given the company's track record of integrating acquisitions and the synergistic value in the GE Plastics acquisition, we believe that one needs to apply a lens of longer-term perspective when analyzing the deal. We are of the opinion that the recent share price correction and unease over the acquisition are both overblown, and that the current price offers an excellent entry point into the name. We reiterate our Overweight rating with a SAR260 target price.

Index ^a	TADAWUL ALL SHARE INDEX
Index level	9675.02
RIC	2010.SE
Bloomberg	SABIC AB

Source: HSBC

Enterprise value (SARm)	443478
Free float (%)	30
Market cap (USDm)	110,333
Market cap (SARm)	413,750

Source: HSBC

Chemical companies valuation summary (USD)

	APD	BRKM5*	CE	DD	DOW	GGC	HUN	MEOH	NCX	PX	SABIC**	WLK
Current price (as of 2/6/2008)	89	13	39	45	38	8	23	24	27	78	165	19
Ratings: (V) = Volatile	N	OW (V)	OW	OW	OW	UW (V)	UW	OW	N	OW	OW	UW
Target price	105	23	48	55	55	4	15	35	30	100	260	14
Target price set on	12/10/07	9/17/07	11/5/07	11/27/06	3/20/07	1/18/07	11/20/06	10/15/07	1/18/07	12/10/07	1/18/07	1/18/07
Upside/(downside) to target price	18%	78%	23%	23%	45%	-48%	-35%	44%	10%	28%	58%	-28%
HSBC normal valuation												
Trend EPS	4.90	1.45	1.75	2.89	2.59	1.74	0.93	2.41	2.25	4.25	NA	1.53
Trend relative PE	1.21	0.90	1.05	0.98	1.11	0.81	0.90	0.81	0.81	1.31	NA	0.81
Normal S&P 500 PE	17.8	17.8	17.8	17.8	17.8	17.8	17.8	17.8	17.8	17.8	17.8	17.8
Normal value	105	23	33	50	51	25	15	35	32.44	99	NA	22
Upside/(downside)	18%	80%	-16%	13%	34%	228%	-36%	43%	19%	27%	NA	14%
1 standard deviation	NA	41%	45%	17%	40%	50%	41%	50%	50%	NA	NA	50%
Peak PE (1 year prior to 88 peak)	NA	NA	NA	8.4	7.1	4.1	4.8	NA	4.1	NA	NA	4.1
Peak PE (1 year prior to 95 peak)	NA	NA	8.0	24.1	7.9	8.2	5.3	5.9	8.2	NA	NA	8.2
HSBC floor valuation												
Floor valuation	NA	14	18	42	31	13	9	17	16	NA	NA	11
Upside/(downside) to floor	NA	6%	-54%	-6%	-19%	64%	-62%	-28%	-41%	NA	NA	-43%
Recent low	NA	10.01	14	36	25	11	17	1	16	NA	NA	15
Timing of recent low	NA	Jul-07	Apr-05	Sep-02	Sep-00	Oct-07	Jun-06	Apr-00	Oct-01	NA	NA	Aug-04
HSBC peak valuation												
HSBC EPS 2008	4.95	1.60	3.75	3.50	3.30	(1.00)	1.40	2.80	2.60	4.25	11.65	1.40
Implied peak valuation - 87 PE	NA	NA	NA	29	23	NA	7	NA	11	NA	NA	6
Implied peak valuation - 94 PE	NA	NA	30	84	26	NA	7	17	21	NA	NA	11
Upside/(downside) to 88 peak valuation	NA	NA	NA	-34%	-38%	NA	-71%	NA	-61%	NA	NA	-70%
Upside/(downside) to 95 peak valuation	NA	NA	-23%	88%	-31%	NA	-68%	-32%	-22%	NA	NA	-41%
Consensus implied peak valuation												
Consensus EPS 2008	4.92	1.19	3.66	3.41	3.49	(0.81)	1.39	2.62	3.15	4.17	7.92	1.60
Implied peak valuation - 87 PE	NA	NA	NA	29	25	NA	7	NA	13	NA	NA	7
Implied peak valuation - 94 PE	NA	NA	29	82	28	NA	7	15	26	NA	NA	13
Upside/(downside) to 88 peak valuation	NA	NA	NA	-36%	-35%	NA	-71%	NA	-53%	NA	NA	-66%
Upside/(downside) to 95 peak valuation	NA	NA	-25%	83%	-28%	NA	-68%	-36%	-6%	NA	NA	-32%
HSBC DCF valuation												
DCF	100	24	29	51	44	18	22	35	34	80	225	20
Upside/(downside)	12%	87%	-26%	13%	15%	130%	-5%	42%	26%	1%	37%	2%

*In BRL

**In SAR

Source: Corporate reports, Firstcall, HSBC

A perfect storm in a teacup

Share price overreaction: A perfect storm

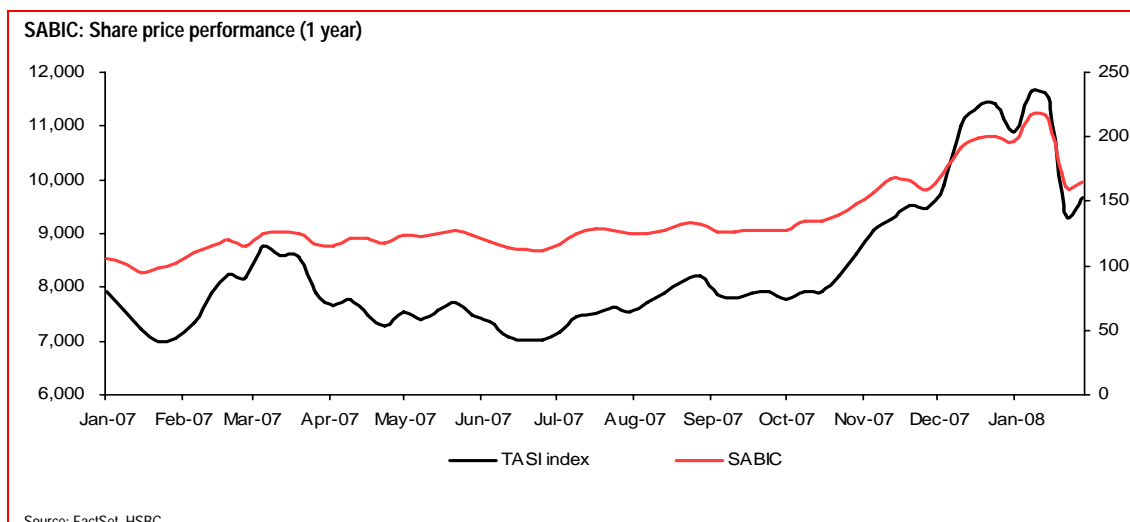
SABIC stock has been very weak over the past month, since the announcement of the company's Q4'07 and full-year results on 20 January 2008. The stock has fallen by over 25% from its 52-week high, leading to a similar decline in the Saudi benchmark index – TASI (see chart at the bottom of the page), which is not surprising given that SABIC is far and away the largest component of the TASI with a weight of 25%. SABIC stock, in our opinion, got caught in a perfect storm of events that triggered a major price decline.

First, the results – SABIC reported Q4'07 net income of SAR6.8bn, or SAR2.75 per share, well ahead of our estimates of SAR6.3bn in net income and our EPS estimate of SAR2.53. However,

given that sell side equity research coverage of SABIC is fairly thin and consists primarily of domestic brokerages, not all of whom necessarily report estimates to consensus aggregators such as Bloomberg, it is possible for a single outlying estimate to skew consensus.

In this case, while we were at SAR6.3bn in net income for the quarter, in light of the fact that the fourth quarter seasonally tends to be among the weakest, there was at least one estimate at SAR8.8bn, which, in our opinion, wildly skewed expectations, resulting in a perception of weak results that sent the stock down over 10% the day the company reported.

The next factor contributing to the share price decline, in our view, was the meltdown in global and particularly emerging market stocks on 20



SABIC: Summary financials (SARm)

	Q4 07	Q3 07	Q4 06	Q3 06	2007	2006
Sales	40,223	32,130	22,732	23,382	126,747	86,327
Cost of sales	-26,868	-19,869	-12,525	-13,785	-79,315	-51,099
Gross profit	13,355	12,261	10,207	9,597	47,432	35,228
Gross profit %	33.2%	38.2%	44.9%	41.0%	37.4%	40.8%
SG&A	-2,245	-1,835	-905	-1,210	-6,681	-4,341
SG&A as a % of sales	5.6%	5.7%	4.0%	5.2%	5.3%	5.0%
Operating income	11,110	10,426	9,302	8,387	40,751	30,887
EBIT margin	27.6%	32.4%	40.9%	35.9%	32.2%	35.8%
Investment and other income	1,044	1,390	962	610	4,244	2,552
Financial charges	-979	-623	-285	-513	-2,649	-1,567
Income before Zakat and MI	11,175	11,193	9,979	8,484	42,346	31,872
Pre tax income margin	27.8%	34.8%	43.9%	36.3%	33.4%	36.9%
Minority Interest	-4,007	-3,402	-3,248	-2,858	-13,517	-10,527
Income before Zakat	7,168	7,791	6,731	5,626	28,829	21,345
Zakat	-300	-390	-550	-200	-1,800	-1,050
Net income	6,868	7,401	6,181	5,426	27,029	20,295
Net income margin	17.1%	23.0%	27.2%	23.2%	21.3%	23.5%
No of shares (m)	2,500	2,500	2,500	2,500	2,500	2,500
EPS (SAR)	2.75	2.96	2.47	2.17	10.81	8.12

Source: Corporate Reports, HSBC

January 2008, as fears of an economic recession in the US and the consequent impact on global economic growth spread, resulting in sharp declines in major indices around the world.

While the global equity markets had stemmed some of their losses by 21 January 2008, when the US Federal Reserve announced an emergency 75bp cut in interest rates, the Saudi market was among the hardest hit, given that it was open for the greatest period of time (Sunday through Tuesday), as Sunday is a working day in the Saudi financial markets.

SABIC thus got caught between results (which, while ahead of our estimates, were still perceived to be disappointing given what we view as unrealistic expectations) and a meltdown in global stock markets, accounting for the 25% drop in the stock price over the two weeks, in our opinion.

We believe that, at current levels, SABIC offers excellent value, and that the recent drop presents investors with a significant buying opportunity.

Addressing the GE Plastics acquisition unease

One of the recurring queries we have been receiving about SABIC over the past few months has been the May 2007 acquisition of GE Plastics, now called SABIC Innovative Plastics (SIP) – namely, the impact of the acquisition on company margins. SIP, with its assets primarily in the US and Europe, does not have the unmatched cost advantage that SABIC's facilities in Saudi Arabia do, and therefore has lower profitability. This is demonstrated by the lower margins in the second half of 2007 – which includes results from SIP – compared to the second half of 2006 (see table at the top of the page). Investor unease regarding the SIP acquisition centers on this difference in profitability and the rationale for the acquisition, in our opinion.

First, it is important to recognize the unique nature of the assets that SABIC has in Saudi Arabia. The profitability of the company's Saudi Arabian assets lies in the company's highly cost-advantaged feedstock position, a situation unique within the global commodity chemical industry to the Middle Eastern region and specifically within

Polyethylene imports by source

Imports 2007 (through October)	000 tons
European Union	
LDPE/LLDPE	516
HDPE	344
China	
LDPE/LLDPE	414
HDPE	191
Imports 2002	000 tons
European Union	
LDPE/LLDPE	217
HDPE	218
China	
LDPE/LLDPE	43
HDPE	22

Source: CMAI, HSBC

Saudi Arabia to SABIC, and Saudi Aramco and its joint ventures.

It would, in our opinion, be facetious to argue that all incremental investments made by SABIC across the world should be held to the same standard of return that SABIC achieves in its Saudi projects. Clearly, the Saudi-based feedstock-advantaged returns are a product of a unique situation; while those returns are sustainable in their current form and are likely to grow as new projects come onstream over the next few years and global energy prices remain at elevated levels, the metric for evaluating global growth opportunities needs to be separate from the return metrics for Saudi projects.

Second, it is essential to note that SIP is not the first asset that SABIC has acquired that is less profitable than its core business – DSM’s European petrochemical assets in 2002 and Huntsman’s European commodity assets in 2006 being prime examples. Furthermore, given the company’s stated intent to continue to grow its business inorganically, it is also unlikely to be the last. Apart from noting that the profitability of each asset is inevitably linked to the price that one pays for the asset, it is also important to stand back and look at the impact the acquisitions have on enabling the rest of the asset portfolio.

Synergy value

The value of existing distribution channels

The words “synergies” and “strategic fit” are much abused in the chemical industry and have often been used in the past to cover all manner of injudicious M&A activity and hefty premiums. However, in the case of SABIC, we believe that their track record of acquisitions has been exemplary and in each case, extremely farsighted.

The acquisition of DSM’s petrochemical assets in Germany and the Netherlands in 2002 was one of SABIC’s first forays into large, cross-border M&A. Pre-2002, per company estimates, SABIC exported roughly 500kt of chemical products into Europe – that number has grown fivefold to over 2.5m tons currently, with over 1m tons of those being polyethylene resins (see table above).

This growth in tonnage sold into Europe is directly attributable to the DSM acquisition, which not only gave SABIC access to production facilities in the region, but also to DSM’s established logistics and distribution networks. We believe that the importance of wide-ranging distribution capabilities in helping producers capture the full value from their advantaged feedstocks is often underrated. Typically, the closer the producer is to the final consumer at the

point of product offtake, the more value one is likely to retain. SABIC, through its DSM acquisition, has demonstrated its ability to integrate a cross-border acquisition, while providing a supply outlet to cost-advantaged product.

SIP gives SABIC a material position in the US, a market in which it was hitherto underrepresented. The US is still the biggest market in the world for petrochemicals, especially in the more specialty markets such as engineering plastics served by SIP. The SIP deal enables SABIC to access the formidable supply chain network built by GE in the US and in Europe, and allows the company to access important end markets such as the automotive industry, with a wide-ranging product slate spanning commodity resins to polycarbonates.

Raw material access

The most significant source of synergies, in our opinion, comes from SABIC's ability to source raw materials more cheaply than GE Plastics would have as a standalone. Indicative economics for Bisphenol-A, the key intermediate that goes predominantly into the production of polycarbonates, show that raw materials make up a very high element of the total cash cost, at around 95%. These raw materials are phenol and acetone, derived from benzene in particular, and

propylene to a lesser extent. SABIC, as a result of its acquisition of Huntsman's assets in the UK, is net long roughly 700kt of benzene, per our estimates, while the benzene requirements for SIP globally are about 900kt.

This benzene long-short position should allow for material offsets at the corporate level, while also allowing for SABIC to structure raw material swaps and achieve significant savings in logistics. With raw materials forming such a major component of the costs, the impact of any such procurement gains would have a relatively material benefit on overall margins and profitability, in our opinion.

Spillover benefits into Kayan

SABIC is a leading partner in Saudi Kayan (35% share post-IPO), which is due to bring a major integrated site into commercial production in 2010 (see table for product slate at the bottom of the page), including a large 260ktpa polycarbonate plant. As a new entrant breaking into the market, SABIC/Kayan would have had fewer options to market to customers other than on price, effectively passing on much of their cost advantage to customers.

Now with SIP in the fold and a 28% share of global polycarbonate capacity, Kayan will benefit from access to best-in-class polycarbonate

Kayan: Product slate and capacity

Product name	000 tons
Ethylene	1478
Propylene	550
Benzene	109
Polyethylene	680
Polypropylene	350
Ethylene Glycols	535
Polycarbonate	260
Ethanolamines	100
Acetone	150
Dimethyl Formamide	50
Ethoxylates	40
Choline Chloride	20
Bisphenol A	240

Source: Corporate Reports, HSBC

technology and production practices, while allowing for an integrated marketing approach that builds on existing customer relations to maintain premium pricing.

The combination of SIP and Kayan also allows for efficient use of logistical networks. For example, SIP currently supplies its compounding facilities in China out of Spain, which would be far more effectively done from Kayan when it comes on stream.

The need for a long-term lens

The main concerns around SABIC, as far as we can tell from our conversations with the investor base, revolve around the SIP deal. Investors appear to be comfortable with the pace of progress of SABIC's facilities slated to come onstream during the course of the year and with the broader chemical outlook in 2008. While some concerns persist around the fallout from a possible recession in the US, it is acknowledged that with its unmatched cost position in basic plastics, SABIC is relatively in a far better position to combat any demand-led downturn than most other companies in the chemical industry.

As far as the two main concerns around the SIP deal go – lower profitability than the core business and strategic rationale – the first point, as it relates to lower profitability than the base business, is, in our opinion, moot. The price paid for the asset reflects its lower profitability, while for SABIC to grow outside the Kingdom of Saudi Arabia would almost inevitably involve buying assets that have lower profitability than the base business, given the unique competitive advantage that the base business enjoys. Furthermore, as SABIC has demonstrated in the past with the acquisition of DSM's European commodity chemical assets, the strategic rationale for cross-border acquisitions and access to distribution networks can often be quite compelling.

SIP gives SABIC access to strong logistics and distribution networks in North America and Europe, as well as allowing it to approach customers with a diverse product slate ranging from commodity resins to the more specialty polycarbonates. The complementary position in benzene – the primary raw material for polycarbonates, with SABIC's European assets being long roughly similar tonnage of benzene as required by SIP – allows for raw material offsets at the group level while also enabling SABIC to benefit from logistical synergies.

We believe that the GE Plastics acquisition was a landmark deal for SABIC that enabled the company to gain access to specialty chemical assets, a world class supply chain and distribution network, technology, and complementary raw material offsets, all of which are critical to the company as it pursues its objectives of being a global chemical company. Of all the cost-advantaged companies producing basic plastics in the Middle East, SABIC is singular in its efforts to broaden its portfolio and geographical reach – beyond the region and commodities.

Given the company's track record of integrating acquisitions and the synergistic value in the GE Plastics acquisition, we believe that one needs to apply a lens of longer-term perspective when analyzing the deal. We are of the opinion that the recent share price correction and unease over the acquisition are overblown, and that the current price offers an excellent entry point into the name. We reiterate our Overweight rating with a SAR260 target price.

Valuation

Our preferred methodology for valuing chemical companies is a normalized valuation approach that looks at a midcycle, or "normalized," earnings based on a historical trend line through a cycle. This methodology, however, is not

applicable to stocks where we neither have long enough earnings history, nor, as is the case with SABIC, historical figures relating to individual product margins in the region. This makes it virtually impossible to do a bottom-up analysis of the normal earnings power of the company.

For SABIC, we base our target price on a replacement value approach. We define replacement value as the cost associated with setting up a greenfield world scale facility to produce a particular chemical product. Using production capacities and our estimate of costs associated with building greenfield facilities for the various products in SABIC's portfolio, we arrive at a replacement value for the company.

In the table that follows, we detail SABIC's valuation according to this metric. We arrive at SABIC's target price via a two-step process. First, on a bottom-up basis, we evaluate the replacement value for each product within SABIC's portfolio, which, as seen in the table, totals SAR422.3bn.

SABIC: Replacement value analysis

Product	__ Base case __		Bull case
	USDm	SARm	SARm
Acetyls	162	615	1,108
Aromatics	10,440	39,673	71,411
Chlor-alkali	1,131	4,296	7,734
Cumene, phenol & polycarbonates	1,186	4,508	8,114
Methanol	13,447	51,100	91,979
Olefins	35,978	136,715	246,087
Polyolefins	12,853	48,840	87,912
Terephthalates & polyester	676	2,568	4,623
Urea and fertilizer	4,854	18,446	33,203
Vinyls	478	1,816	3,268
Other chemicals	11,738	44,604	80,287
Steel	6,600	25,080	45,144
GE Plastics	11,600	44,080	44,080
Total replacement value	111,142	422,341	724,949
Feedstock advantage	39,949	151,807	151,807
Total value	151,091	574,148	876,756
Shares outstanding (m)		2,500	2,500
Value per share (SAR)		230	351

Source: CMAI, HSBC estimates

This analysis is incomplete without layering on the value of SABIC's feedstock advantage. In the second step, we carry out a DCF on SABIC's feedstock advantage. From the company's product

capacities, we can evaluate how much feedstock the company purchases annually. We also know the price SABIC pays for a variety of feedstocks – be they ethane, propane, or naphtha – and similarly we know the price of these feedstocks in the Western world.

Using these three variables, we can come up with a value for the feedstock advantage in a given year, and doing a DCF around this advantage helps us arrive at a valuation for this cost advantage. Adding the replacement value to the feedstock advantage value allows us to arrive at our base case valuation of SAR260 per share, which is our target price for SABIC shares.

As discussed earlier in this report, the Middle East has seen capital cost inflation in the range of 1.8-2.4x over the past few years. Our base-case valuation analysis does not factor any capital cost inflation into the replacement value, which, in our view, is a conservative way to value SABIC. In our bull-case analysis, we factor 1.8x capital cost inflation into our estimates of replacement value and come up with a bull-case valuation of SAR351 per share for SABIC shares.

Risks

SABIC's earnings are closely dependent on overall chemicals industry margins, so significant shifts in this area represent the greatest risk to our forecasts. The biggest risk to petrochemicals demand, we believe, would be a severe downturn in GDP growth, notably in China, which has formed a major engine of global demand growth. However, in a commodity-type business, margins tend to be self-correcting over time, as has been demonstrated throughout the history of the petrochemicals business. It is the relative slowness of these processes that may distort short-term margins, hence the importance of normalized earnings to assess underlying long-term value.

In addition to normal business risk in the petrochemicals market, we see other potential risks that are more difficult to assess, both in terms of probability and effect. Such risks include interruption to production from operating problems or explosion.

Although the bulk of SABIC's production is based in the Middle East, which some investors may associate with increased risk of terrorist attack, the more practical, everyday issue is that of normal risk in a production process involving potentially explosive hydrocarbons, an area in which global standards of health and safety are rigorously applied.

SABIC: Income statement (SARm)

	2001	2002	2003	2004	2005	2006	2007	2008e	2009e	2010e	2011e
Net sales											
Petrochemicals	25,358	29,986	38,682	59,470	66,638	74,066	110,229	113,176	112,309	108,289	102,921
Metals	3,368	3,798	4,901	6,573	7,193	7,612	10,701	12,779	12,037	10,515	10,230
Corporate	48	242	3,199	2,497	4,422	4,649	5,817	6,079	6,094	6,003	5,867
Consolidated net sales	28,775	34,026	46,782	68,539	78,254	86,327	126,747	132,033	130,440	124,807	119,018
Cost of sales	19,814	22,577	26,114	35,181	38,638	45,094	72,198	72,853	78,196	77,271	76,185
Gross profit	8,960	11,449	20,669	33,359	39,615	41,232	54,549	59,180	52,244	47,536	42,833
Administration and marketing expenses	1,316	2,393	3,036	3,429	3,914	4,026	6,494	7,262	6,522	6,240	5,951
Administration and marketing expenses to sales	4.6%	7.0%	6.5%	5.0%	5.0%	4.7%	6.5%	5.5%	5.0%	5.0%	5.0%
D&A expense	3,684	3,762	7,032	6,424	6,531	6,119	7,306	9,095	9,979	10,152	10,094
Unusual charges				1,782							
Operating income	3,960	5,294	10,600	21,723	29,170	31,087	40,749	42,823	35,743	31,144	26,789
Finance charges	(1,575)	(824)	(984)	(1,021)	(1,397)	(1,567)	(2,649)	(2,693)	(2,615)	(2,142)	(1,739)
Other income	608	415	831	1,299	1,237	2,552	4,245	4,000	3,600	3,200	2,800
Income before minority interests and Zakat	2,993	4,886	10,448	22,002	29,010	32,072	42,344	44,130	36,729	32,201	27,850
Zakat	260	305	300	450	750	1,050	1,800	1,765	1,469	1,288	1,114
Zakat rate	9%	6%	3%	2%	3%	3%	4%	4%	4%	4%	4%
Minority interest/other (expense)	(953)	(1,732)	(3,451)	(7,338)	(9,100)	(10,527)	(13,517)	(13,239)	(11,019)	(9,660)	(8,355)
Net income (a)	1,780	2,849	6,696	14,214	19,160	20,495	27,027	29,126	24,241	21,253	18,381
Non rec'g income (expense), after tax											
Net income, ex-non-rec'g's	1,780	2,849	6,696	14,214	19,160	20,495	27,027	29,126	24,241	21,253	18,381
Preferred dividends (b)											
Net income, reported(a+b)	1,780	2,849	6,696	14,214	19,160	20,495	27,027	29,126	24,241	21,253	18,381
EPS	5.93	9.50	22.32	47.38	7.66	8.20	10.81	11.65	9.70	8.50	7.35
EPS recurring	5.93	9.50	22.32	47.38	7.66	8.20	10.81	11.65	9.70	8.50	7.35
Number of shares (diluted) (m)	300	300	300	300	2,500	2,500	2,500	2,500	2,500	2,500	2,500
Dividend per share (SAR)	4.3	3.0	4.9	11.8	3.0	3.9	3.9	3.9	3.9	3.9	3.9
Shares repurchased	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
EBITDA											
EBITDA	7,644	9,056	17,632	28,147	35,701	37,206	48,055	51,918	45,722	41,296	36,883
EBITDA margin	26.6%	26.6%	37.7%	41.1%	45.6%	43.1%	37.9%	39.3%	35.1%	33.1%	31.0%
EBITDA per share	25.48	30.19	58.77	93.82	14.28	14.88	19.22	20.77	18.29	16.52	14.75
EBITDA per share growth	-17.2%	18.5%	94.7%	59.6%	-84.8%	4.2%	29.2%	8.0%	-11.9%	-9.7%	-10.7%
EBIT											
EBIT	3,960	5,294	10,600	21,723	29,170	31,087	40,749	42,823	35,743	31,144	26,789
EBIT margin	13.8%	15.6%	22.7%	31.7%	37.3%	36.0%	32.1%	32.4%	27.4%	25.0%	22.5%
EBIT per share	13.20	17.65	35.33	72.41	11.67	12.43	16.30	17.13	14.30	12.46	10.72
EBIT per share growth	-34.8%	33.7%	100.2%	104.9%	-83.9%	6.6%	31.1%	5.1%	-16.5%	-12.9%	-14.0%
Productivity											
Number of employees	14,364	15,000	16,000	16,500	17,000	19,000	30,000	30,600	31,212	31,836	32,473
Sales per employee, SAR000	2,003	2,268	2,924	4,154	4,603	4,544	4,225	4,315	4,179	3,920	3,665
EBITDA per employee, SAR000	532	604	1,102	1,706	2,100	1,958	1,602	1,697	1,465	1,297	1,136
EBIT per employee, SAR000	276	353	663	1,317	1,716	1,636	1,358	1,399	1,145	978	825
EBIT per pound, SAR/lb		0.10	0.20	0.36	0.43	0.45	0.50	0.48	0.37	0.31	0.26

Source: Corporate reports, HSBC estimates

SABIC: Cash flow statement (SARm)

	2001	2002	2003	2004	2005	2006	2007e	2008e	2009e	2010e	2011e
Operating activities											
Net income for the year before zakat	1,780	2,849	6,696	14,663	19,910	21,343	28,827	30,891	25,710	22,541	19,495
Depreciation and amortization	3,684	3,762	7,032	6,424	6,531	6,119	7,306	9,095	9,979	10,152	10,094
Equity in earnings of associated companies	(47)	(73)	(295)	(332)	(526)	(197)	(849)	(800)	(720)	(640)	(560)
Minority interests in net income of subsidiaries	953	0	0	7,338	9,100	10,528	13,517	13,239	11,019	9,660	8,355
(Increase) decrease in accounts receivable and prepayments	762	(3,134)	(2,329)	(5,481)	(968)	(1,623)	(9,227)	5,390	1,679	805	827
(Increase) decrease in inventories	153	(1,384)	(178)	(2,111)	(1,488)	(3,015)	(8,674)	4,119	836	205	241
Incr (decr) in accounts payable, accrued liab and provisions	(995)	1,762	2,839	3,502	(889)	4,065	4,071	1,806	434	(205)	(241)
Other non-current liabilities liabilities	230	708	(195)	907	1,798	(2)	0	0	0	0	0
Provision for Zakat	260	305	300								
Zakat paid	(63)	(450)	(231)	(376)	(331)	(813)	(1,800)	(1,765)	(1,469)	(1,288)	(1,114)
Net cash provided by operating activities	6,717	4,345	13,640	24,534	33,136	36,405	33,171	61,975	47,468	41,230	37,096
Financing activities											
Long term debt, net	(642)	5,701	2,207	(3,073)	(3,974)	9,763	39,666	(3,300)	0	0	0
Short term bank facilities, net	583	(285)	(243)	24	(132)	256	792	(1,399)	0	0	0
Minority interest, net	(705)	241	228	(3,808)	(6,055)	(5,801)	(8,110)	(7,943)	(6,611)	(5,796)	(5,013)
Dividends paid	(1,298)	(894)	(1,473)	(3,532)	(7,422)	(9,702)	(9,700)	(9,700)	(9,700)	(9,700)	(9,700)
Net cash used in financing activities	(2,062)	4,763	719	(10,389)	(17,582)	(5,483)	22,647	(22,343)	(16,311)	(15,496)	(14,713)
Investing activities											
Additions to property, plant and equipment, net	(2,286)	(5,518)	(9,131)	(4,452)	(7,600)	(18,752)	(56,755)	(29,047)	(14,348)	(11,233)	(10,712)
Investments, net	162	(1,230)	(205)	314	(2,682)	2,563					
Intangible assets, net	0	0	0	612	183	(645)	50	50	50	50	50
Other non-current assets, net	(533)	(3,011)	(725)	(1,995)	(528)	(1,033)	(1,116)	(1,116)	(1,116)	(1,116)	(1,116)
Net cash used in investing activities	(2,658)	(9,759)	(10,061)	(5,521)	(10,627)	(17,866)	(57,821)	(30,114)	(15,415)	(12,299)	(11,778)
Increase (decrease) in cash & equivalents											
Net increase (decrease) in cash and cash equivalents	1,998	(651)	4,297	8,623	4,928	13,055	(2,002)	9,518	15,742	13,435	10,606
Cash at beginning of period	8,977	10,975	10,324	14,620	23,244	28,171	41,227	39,224	48,743	64,485	77,920
Cash at end of period	10,975	10,324	14,620	23,244	28,171	41,227	39,224	48,743	64,485	77,920	88,525
Sources and uses of cash, USD/share											
Operating cash flow	22.39	14.48	45.47	81.78	13.25	14.56	13.27	24.79	18.99	16.49	14.84
Capex	(7.62)	(18.39)	(30.44)	(14.84)	(3.04)	(7.50)	(22.70)	(11.62)	(5.74)	(4.49)	(4.28)
Distributable cash	14.77	(3.91)	15.03	66.94	10.21	7.06	(9.43)	13.17	13.25	12.00	10.55
Cash flow ratios											
Working capital increase/sales change	3.8%	52.5%	-2.6%	18.8%	34.4%	7.1%	34.2%	-214.0%	185.1%	14.3%	14.3%
Reinvestment rate (capex/gross fixed assets)	2.4%	5.3%	8.0%	3.8%	6.1%	13.1%	29.6%	12.6%	5.6%	4.1%	3.6%
Capex/sales	7.9%	16.2%	19.5%	6.5%	9.7%	21.7%	10.0%	22.0%	11.0%	9.0%	9.0%
Depreciation/sales	12.8%	11.1%	15.0%	9.4%	8.3%	7.1%	5.8%	6.9%	7.7%	8.1%	8.5%
D&A less capex	1,398	(1,756)	(2,099)	1,972	(1,069)	(12,633)	(49,449)	(19,952)	(4,369)	(1,080)	(618)
Cash from operations less capex (distributable cash)	4,431	(1,173)	4,508	20,081	25,537	17,653	(23,584)	32,927	33,119	29,998	26,385
Distributable cash flow per share	14.77	(3.91)	15.03	66.94	10.21	7.06	(9.43)	13.17	13.25	12.00	10.55
Cash from operations less capex less dividends	4,431	(1,173)	4,508	20,081	25,537	17,653	(23,584)	32,927	33,119	29,998	26,385
Cash from operations less capex less dividends/share	14.77	(3.91)	15.03	66.94	10.21	7.06	(9.43)	13.17	13.25	12.00	10.55
Dividend payout ratio	72.9%	31.4%	22.0%	24.9%	38.7%	47.3%	35.9%	33.3%	40.0%	45.6%	52.8%

Source: Corporate reports, HSBC estimates

SABIC: Balance sheet (SARm)

	2001	2002	2003	2004	2005	2006	2007e	2008e	2009e	2010e	2011e
Assets											
Cash & equivalents	10,975	10,324	14,621	23,245	28,173	41,228	46,136	48,743	64,485	77,920	88,525
Accounts receivable	4,600	7,579	8,586	13,504	14,521	16,476	25,703	20,313	18,634	17,830	17,003
Inventories	5,483	6,866	7,044	9,155	10,642	13,658	22,332	18,213	17,377	17,171	16,930
Other receivables and prepayments	953	1,109	2,431	2,993	2,945	2,613	4,887	4,887	4,887	4,887	4,887
Total current assets	22,011	25,878	32,682	48,897	56,281	73,975	99,058	92,156	105,383	117,808	127,345
Property, plant & equipment, at cost	94,898	104,345	113,476	118,032	124,272	142,881	192,031	230,173	254,501	275,886	296,691
Less: Accumulated depreciation	34,427	41,684	48,716	54,188	58,175	62,911	70,217	79,312	89,291	99,444	109,537
Property, plant & equipment, net	60,471	62,661	64,760	63,844	66,097	79,971	121,814	150,861	165,210	176,442	187,154
Investments	870	2,173	2,672	2,690	5,898	3,532	5,913	5,913	5,913	5,913	5,913
Intangible assets	0	5,406	7,013	5,999	5,335	5,094	23,753	23,803	23,853	23,904	23,954
Other non-current assets	5,884	3,055	2,172	3,515	3,340	4,018	5,485	6,602	7,718	8,834	9,951
Total assets	89,236	99,172	109,300	124,945	136,950	166,589	256,023	279,335	308,077	332,901	354,317
Liabilities											
Current portion of long-term debt	4,454	3,540	4,498	6,050	6,352	5,521	3,300				
Accounts payable	2,397	3,844	6,046	8,298	7,782	11,066	15,137	16,943	17,377	17,171	16,930
Short-term loans	987	702	459	484	352	608	1,399				
Dividend payable	237						618				
Other accrued liabilities	4,595	5,009	5,743	7,135	7,461	8,530	11,536	11,536	11,536	11,536	11,536
Total current liabilities	12,670	13,095	16,747	21,968	21,947	25,725	31,991	28,479	28,913	28,708	28,466
Long-term debt	24,055	30,669	31,918	27,293	23,017	33,611	75,498	75,498	75,498	75,498	75,498
Other non-current liabilities	3,547	4,255	4,060	4,967	6,765	6,763	14,690	14,690	14,690	14,690	14,690
Total liabilities	40,272	48,019	52,725	54,227	51,729	66,098	122,178	118,667	119,101	118,895	118,654
Minority interest	15,836	16,077	16,306	19,835	22,881	27,607	42,685	45,137	51,824	57,734	62,890
Shareholders' equity	33,128	35,075	40,270	50,882	62,341	72,883	91,160	115,532	137,152	156,272	172,773
Total liability and shareholders equity	89,236	99,172	109,300	124,945	136,950	166,589	256,023	279,335	308,077	332,901	354,317
Financial leverage analysis											
Net debt	(17,534)	(23,886)	(21,795)	(10,098)	(1,197)	2,096	(32,662)	(26,755)	(11,013)	2,422	13,028
Net debt per share	(58.45)	(79.62)	(72.65)	(33.66)	(0.48)	0.84	(13.06)	(10.70)	(4.41)	0.97	5.21
Book value per share	110.43	116.92	134.23	169.61	24.94	29.15	36.46	46.21	54.86	62.51	69.11
Net debt/(net debt + equity)	35%	41%	35%	17%	2%	-3%	26%	19%	7%	-2%	-8%
LTD/(LTD + equity)	42%	47%	44%	35%	27%	32%	45%	40%	36%	33%	30%
Total debt/EBITDA	3.7	3.8	2.1	1.2	0.8	1.1	1.6	1.5	1.7	1.8	2.0
EBIT/interest expense	2.5	6.4	10.8	21.3	20.9	19.8	15.4	15.9	13.7	14.5	15.4
EBITDA/interest expense	4.9	11.0	17.9	27.6	25.6	23.7	18.1	19.3	17.5	19.3	21.2
Working capital analysis											
Working capital	9,342	12,783	15,935	26,929	34,334	48,250	67,067	63,677	76,470	89,100	98,879
Current ratio	1.7	2.0	2.0	2.2	2.6	2.9	3.1	3.2	3.6	4.1	4.5
Trade working capital	7,686	10,601	9,583	14,360	17,381	19,068	32,898	21,584	18,634	17,830	17,003
Trade working capital turnover	3.8	3.7	4.6	5.7	4.9	4.7	4.9	4.8	6.5	6.8	6.8
Accounts receivable days sales outstanding	58.4	81.3	67.0	71.9	67.7	69.7	74.0	56.2	52.1	52.1	52.1
Accounts receivable turnover	6.3	4.5	5.4	5.1	5.4	5.2	5.5	6.5	7.0	7.0	7.0
Inventory cost of sales days outstanding	102.4	99.8	97.2	84.0	93.5	98.3	91.0	101.6	83.1	81.6	81.7
Inventory turnover	3.6	3.7	3.8	4.3	3.9	3.7	3.0	4.0	4.5	4.5	4.5
Accounts payable days outstanding	44.2	62.1	84.5	86.1	73.5	89.6	76.5	84.9	81.1	81.1	81.1
Accounts payable turnover	8.3	5.9	4.3	4.2	5.0	4.1	3.5	4.3	4.5	4.5	4.5
Return on capital											
Return on capital (ROC)	4.0%	4.2%	8.2%	14.8%	17.8%	16.4%	15.8%	13.3%	10.1%	8.0%	6.4%
Return on equity (ROE)	10.0%	10.6%	20.3%	33.4%	36.2%	32.6%	36.0%	30.7%	21.2%	15.9%	12.2%
Return on assets (ROA)	3.6%	3.8%	7.3%	13.0%	15.7%	14.5%	14.0%	11.8%	9.1%	7.3%	5.8%

Source: Corporate reports, HSBC estimates

Disclosure appendix

Analyst certification

The following analyst(s), who is(are) primarily responsible for this report, certifies(y) that the opinion(s) on the subject security(ies) or issuer(s) and any other views or forecasts expressed herein accurately reflect their personal view(s) and that no part of their compensation was, is or will be directly or indirectly related to the specific recommendation(s) or views contained in this research report: Hassan Ahmed and Sriharsha Pappu

Important disclosures

Stock ratings and basis for financial analysis

HSBC believes that investors utilise various disciplines and investment horizons when making investment decisions, which depend largely on individual circumstances such as the investor's existing holdings, risk tolerance and other considerations. Given these differences, HSBC has two principal aims in its equity research: 1) to identify long-term investment opportunities based on particular themes or ideas that may affect the future earnings or cash flows of companies on a 12 month time horizon; and 2) from time to time to identify short-term investment opportunities that are derived from fundamental, quantitative, technical or event-driven techniques on a 0-3 month time horizon and which may differ from our long-term investment rating. HSBC has assigned ratings for its long-term investment opportunities as described below.

This report addresses only the long-term investment opportunities of the companies referred to in the report. As and when HSBC publishes a short-term trading idea the stocks to which these relate are identified on the website at www.hsbcnet.com/research. Details of these short-term investment opportunities can be found under the Reports section of this website.

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Rating definitions for long-term investment opportunities

Stock ratings

HSBC assigns ratings to its stocks in this sector on the following basis:

For each stock we set a required rate of return calculated from the risk free rate for that stock's domestic, or as appropriate, regional market and the relevant equity risk premium established by our strategy team. The price target for a stock represents the value the analyst expects the stock to reach over our performance horizon. The performance horizon is 12 months. For a stock to be classified as Overweight, the implied return must exceed the required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock must be expected to underperform its required return by at least 5 percentage points over the next 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands are classified as Neutral.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation of coverage, change of volatility status or change in price target). Notwithstanding this, and although ratings are subject to ongoing management review, expected returns will be permitted to move outside the bands as a result of normal share price fluctuations without necessarily triggering a rating change.

*A stock will be classified as volatile if its historical volatility has exceeded 40%, if the stock has been listed for less than 12 months (unless it is in an industry or sector where volatility is low) or if the analyst expects significant volatility. However,

stocks which we do not consider volatile may in fact also behave in such a way. Historical volatility is defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility has to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Prior to this, from 7 June 2005 HSBC applied a ratings structure which ranked the stocks according to their notional target price vs current market price and then categorised (approximately) the top 40% as Overweight, the next 40% as Neutral and the last 20% as Underweight. The performance horizon is 2 years. The notional target price was defined as the mid-point of the analysts' valuation for a stock.

From 15 November 2004 to 7 June 2005, HSBC carried no ratings and concentrated on long-term thematic reports which identified themes and trends in industries, but did not make a conclusion as to the investment action that potential investors should take.

Prior to 15 November 2004, HSBC's ratings system was based upon a two-stage recommendation structure: a combination of the analysts' view on the stock relative to its sector and the sector call relative to the market, together giving a view on the stock relative to the market. The sector call was the responsibility of the strategy team, set in co-operation with the analysts. For other companies, HSBC showed a recommendation relative to the market. The performance horizon was 6-12 months. The target price was the level the stock should have traded at if the market accepted the analysts' view of the stock.

Rating distribution for long-term investment opportunities

As of 08 February 2008, the distribution of all ratings published is as follows:

Overweight (Buy)	55%	(22% of these provided with Investment Banking Services)
Neutral (Hold)	30%	(24% of these provided with Investment Banking Services)
Underweight (Sell)	15%	(15% of these provided with Investment Banking Services)

Share price and rating changes for long-term investment opportunities

Saudi Basic Industries Co share price performance SAR vs HSBC rating history



Source: HSBC

Recommendation & price target history

From	To	Date
N/A	Overweight (V)	12 April 2007
Overweight (V)	Overweight	17 December 2007
Target Price	Value	Date
Price 1	155.00	12 April 2007
Price 2	165.00	14 July 2007
Price 3	230.00	17 December 2007
Price 4	260.00	18 January 2008

Source: HSBC

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price Date	Disclosure
SAUDI BASIC INDUSTRIES CO	2010.SE	162.75	07-Feb-2008	2, 5, 6, 7, 11

Source: HSBC

- 1 HSBC* has managed or co-managed a public offering of securities for this company within the past 12 months.
- 2 HSBC expects to receive or intends to seek compensation for investment banking services from this company in the next 3 months.

- 3 At the time of publication of this report, HSBC Securities (USA) Inc. is a Market Maker in securities issued by this company.
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- 9 A covering analyst/s or a member of his/her household has a financial interest in the securities of this company, as detailed below.
- 10 A covering analyst/s or a member of his/her household is an officer, director or supervisory board member of this company, as detailed below.
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Additional disclosures

- 1 This report is dated as at 11 February 2008.
- 2 All market data included in this report are dated as at close 06 February 2008, unless otherwise indicated in the report.
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