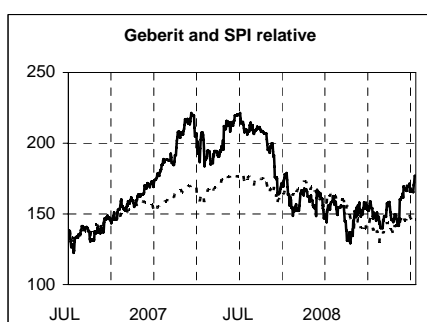


**Company contact**

**Market share gains in sanitary systems and piping; solid margin development despite higher input costs → BUY confirmed**

**BUY**

Market cap.	CHF m	6961	Key figures	2006	2007	2008E	2009E	2010E	CAGR
Last price	CHF	177	(CHF)						05-10E
52 week high	CHF	217	Net revenues (m)	1849	2104	2119	2245	2381	7.7
52 week low	CHF	128	Growth rate (%)	12.7	13.8	0.7	6.0	6.1	
YTD performance	%	13.7	EBITDA (m)	569	638	661	701	743	10.3
<b>Economic value</b>	<b>CHF</b>	<b>197</b>	Margin (%)	30.8	30.3	31.2	31.2	31.2	
Soft factor ded.	%	0	EBIT (m)	482	554	572	610	650	12.1
<b>Fair value NZB</b>	<b>CHF</b>	<b>197</b>	Margin (%)	26.1	26.3	27.0	27.1	27.3	
Div. ranking shs	m	39.4	Net profit (m)	367	463	433	465	498	13.7
Symbols	GEBN.VX, GEBN VX		Dividend	4.0	5.2	4.9	5.3	5.1	15.1



EPS revision	2006	2007	2008E	2009E	2010E	CAGR
EPS new	9.1	11.4	11.0	11.8	12.7	14.5
EPS old			11.0	11.8	12.6	
% change			0.0	0.1	0.1	

Valuation (x)	2006	2007	2008E	2009E	2010E
P / EPS	16.4	15.9	16.1	15.0	14.0
P / CEPS	16.4	15.9	16.1	15.0	14.0
P / BV	5.6	5.2	4.9	4.1	3.5
EV / EBITDA	11.0	11.5	10.4	9.5	8.6
Dividend yield (%)	2.7	2.9	2.8	3.0	2.9

In Q1 2008E, Geberit notched up market share gains in Western Europe and noted positive developments in emerging markets. These results largely compensated for a negative base effect and weaker construction markets, as well as the effects of an early Easter. In addition, the company's margin development was surprisingly solid. During our recent meeting with management, we discussed the potential impact of the economic environment on the company's businesses, and confirmed the margin development in the light of price, mix and volume changes.

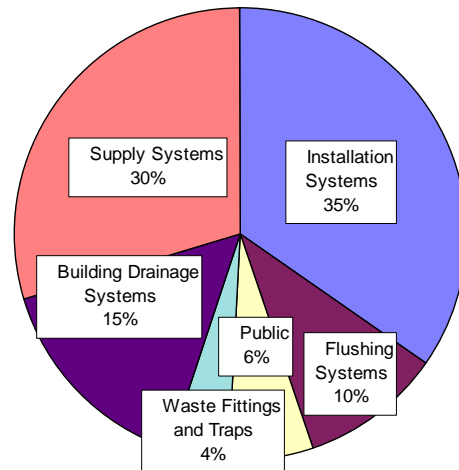
While Geberit's management is still reluctant to provide any guidance for FY 2008, we are convinced that the company will benefit from the strong driving forces currently in place, starting already in 2008. Geberit is gaining market share in sanitary systems (with concealed installation systems) and piping (replacing copper with multilayer pipes). Low penetration markets with double digit growth accounted for 23% of sales in 2007. This has created a solid growth platform that supports organic growth even in the case of stagnating core markets deriving from an economic downturn.

**BUY rating and price target of CHF 190 confirmed**

Geberit has plenty of scope for growth in new countries with low penetration levels, and has potential for further market share gains in its core markets. The group's pricing power is solid. Based on our EVA<sup>®</sup>/DCF model, we have derived an economic value and 'fair value NZB' of CHF 197 per share from our estimates, indicating upside potential of 11%. We therefore recommend purchase of Geberit's shares with a 12-month price target of CHF 190. While our model does not incorporate potential acquisitions, the latter could clearly increase our fair value.

- **Update on Geberit:** We met with Geberit's CFO to get an update on Geberit's business. In addition, we discussed the Piping Systems product area in more detail. While the latter is more cyclical than Sanitary Systems, we consider it very promising with regard to its replacement of copper pipes with innovative materials.

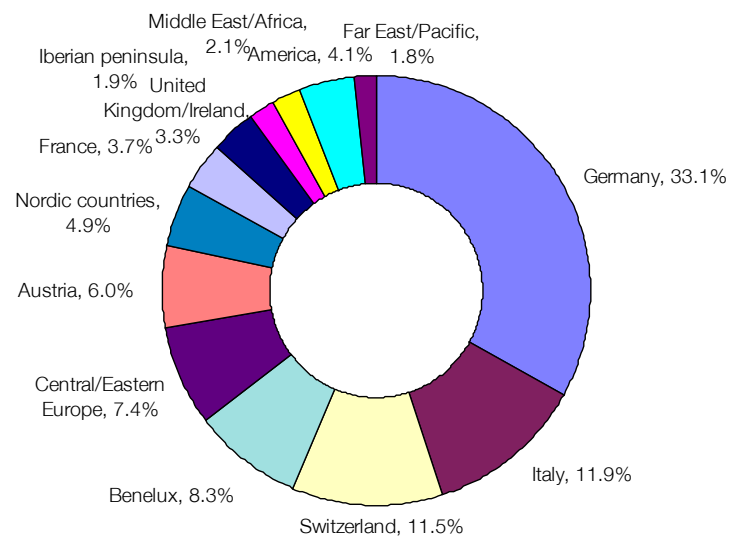
**Figure 1: Gross sales breakdown by product line (2007; CHF 2.487bn)**



Source: Geberit

- **Update on selected markets:** In 2007, Geberit experienced solid organic growth in all markets except the USA due to the streamlining of its product portfolio. In Q1 2008, the negative base effect, the earlier Easter holidays and destocking effects due to new product introductions put pressure on organic sales growth rates (-1.5%). Only the high base from 2007 is expected to have an ongoing negative impact on Q2, while the other effects should see a reversal. The base effect in Q2 should be smaller as Geberit grew organically by 20.5% in Q1 2007, and by 13.5% in Q2 2007.

**Figure 2: Gross sales by market (2007; CHF 2.487bn)**



Source: Geberit

**Germany (33.1% of group sales):** Germany was the main contributor to the decline in group organic sales growth in l.c. of -1.5% for Q1 2008. This was due to a negative base effect from good weather conditions in Q1 2007, and the discontinuation of federal subsidies for family homes ('Eigenheimzulage'). Residential and non-residential construction orders in Germany declined by -4.5% YoY (Figure 3) and -1.5% YoY (Figure 4) respectively in Q1 2008.

Figure 3: Construction orders residential buildings

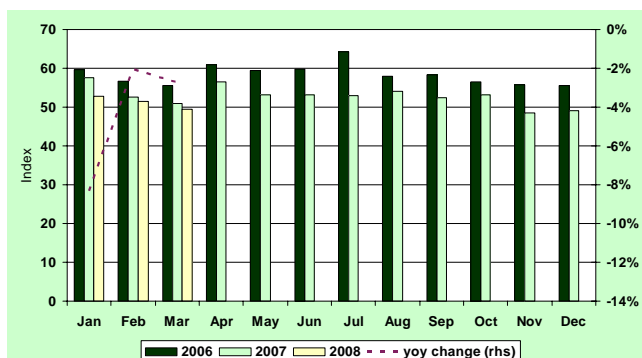
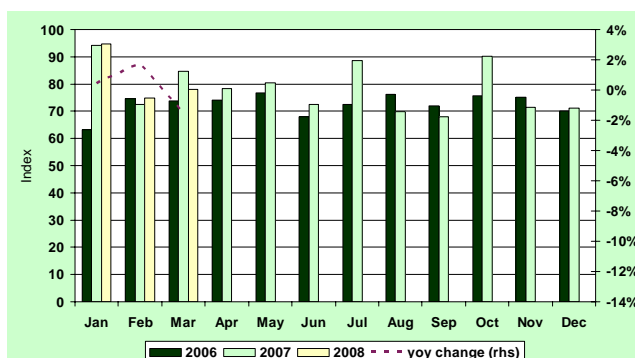


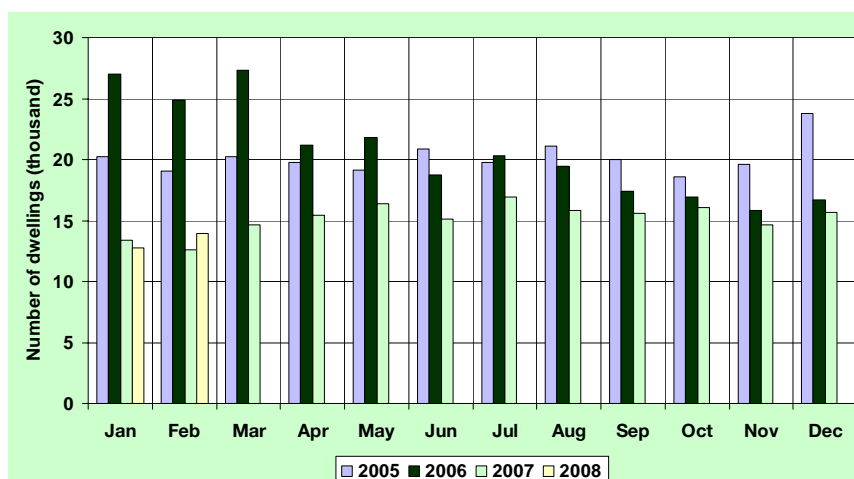
Figure 4: Construction orders non-residential buildings



Source: Deutsche Bundesbank

However, there are signs of improvement in German new construction activity. Residential construction permits (Figure 5) in January and February 2008 were 2.7% above the 2007 level. In terms of value, this increase corresponds to +15.6%, indicating higher construction costs and a trend towards more expensive buildings. Also, the solid development of business confidence as measured by the IFO index is a positive indication for new construction and modernization. The latter is more important for Geberit as renovations account for 70%–80% of its German revenues.

Figure 5: Residential construction permits in Germany



Source: Statistisches Bundesamt

**Rest of Europe (58.9%):** Other European markets in which Geberit has already achieved a high level of penetration with its product range include Italy, Switzerland, the Benelux countries and Austria. These markets accounted for 37.7% of revenues in 2007. The highest growth is reported in central and eastern Europe, UK/Ireland, the Nordic

Region, France and the Iberian Peninsula. These markets represent 21.2% of sales. The diverging growth rates have less to do with construction activity than with different levels of market penetration.

**America (4.1%):** Geberit achieved promising initial results in its attempt to enter the American market with concealed systems. After a lengthy trial-and-error period, the group started a co-operation with Duravit to push installation systems in the North American premium market segment at the beginning of 2007. The German company Duravit is a globally active manufacturer of sanitary ceramics, bath furniture and wellness products. Initial positive results of the co-operation are residential- and hotel project wins with concealed cistern systems. Geberit's strategy in the USA has been based on its tried and proven approach in other markets (e. g. Poland). The first step to entering a new market is to convince the key decision-makers such as designers and architects. This leads to initial demonstration projects that can be used to convince wholesalers, installers and customers. However, the sales volume in the Americas remained small (CHF 103m in 2007, 4.1% of group total), and stagnated due to the streamlining of the acquired US product portfolio. Geberit is predominantly active in public-, institutional- and non-residential construction in the USA. As a result, the company is less exposed to the decline in residential construction.

**Far East/Pacific (1.8%):** Starting from a small base, Geberit's business in China and Australia is performing strongly. The group is gaining increasing acceptance in large residential and non-residential projects in Asia (excluding Japan). Sales in this region grew organically by +32.0% in FY 2007 and +34.6% in Q1 2008.

**Middle East/Africa (2.1%):** In the Middle East and Africa, Geberit is benefiting from its growing presence, increased recognition and booming construction markets. While the percentage of revenues derived from this region is still small, the group boasts a diversified geographic presence. Regional sales growth reached +45.1% in FY 2007 and +13.4% in Q1 2008.

→ **Opinion:** Geberit has only achieved high product penetration in the few markets mentioned above. Elsewhere in the world, the company has achieved promising starting positions, and the importance of these new markets has grown rapidly. Low penetration markets with double digit growth already accounted for 23% of sales in 2007. Increased market share in these new markets should allow Geberit to continue to grow organically even in the face of economic decline. In addition, we are optimistic with regard to new construction in Germany as we hope that the March and April building permit figures will confirm the positive trend reported in the first two months. For the time being we are leaving our sales growth estimates for 2008E unaltered. However, our estimates will be updated when appropriate, based on positive economic releases or unexpectedly strong H1 results.

- **Material prices and margin development:** Geberit demonstrated surprisingly stable margins in Q1 2008. This was mainly due to a positive mix effect (lower proportion of Piping Systems sales) and price increases in H2 2007 and early 2008. Management explained that Piping Systems had been stronger in 2007 due to marketing efforts (Geberit did not pass all raw material price increases to clients) and the stronger proportion of new installation business which tends

to be more piping-intensive. As a result, the mix effect could remain positive throughout 2008E.

Geberit has solid pricing power and can typically pass on higher raw material prices. 53% of its material costs is related to metals, including aluminium, stainless steel, carbon steel as well as copper. Plastics account for 25% of material costs, while the remaining 22% include various items such as purchased electrical components and packaging. While the two single most important raw materials aluminium and polyethylene are currently priced at around the 2007 average, steel is now trading at significantly higher prices.

Figure 6: Aluminium prices

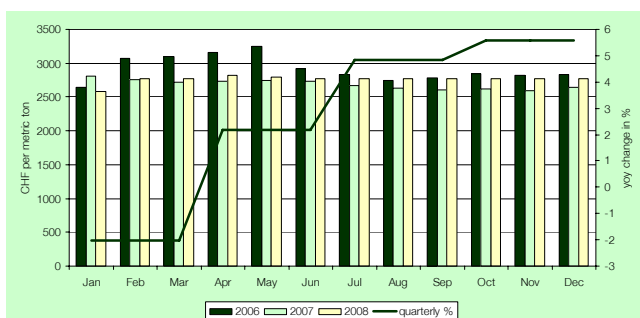
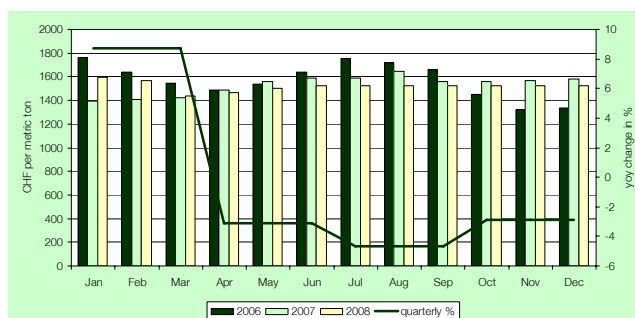


Figure 7: Polyethylene prices



Source: Bloomberg

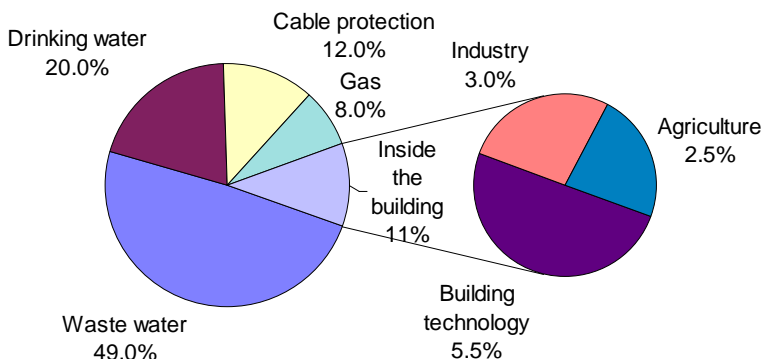
Energy in the form of electricity, combustibles and fuels is another input factor that is subject to higher prices. Nevertheless, Geberit expects to adjust prices if necessary.

➔ **Opinion:** We expect a normalization of Geberit's product mix which should have a beneficial impact on margins throughout 2008E. The lower-margin piping business that is more cyclical in nature is expected to grow less than Sanitary Systems. We expect raw material prices relevant for Geberit to stagnate at a high level in 2008E, and Geberit can pass the increases on to clients without any great difficulty.

- **Review of the piping business:** Geberit Piping Systems manufactures innovative and easy-to-install products that generate sales growth despite lower construction activity. However, Piping Systems is slightly more cyclical in nature than Sanitary Systems. New constructions tend to require more pipes than modernization procedures. As a result, a cyclical downturn in new construction could slow down the growth of Piping Systems. In addition, margins are lower as the product is more material-intensive compared to Sanitary Systems.

Figure 8 below demonstrates with the example of the German plastic pipes market that the relevant segment for Geberit is only a fraction of the overall piping systems market. Pipes within buildings account for about 11% of piping volumes, but due to higher prices they represent about 35% of the total German plastic pipe market of EUR 2bn. Heating applications account for about 65% of the building technology volumes. Building technology and industry are considered the most attractive segment for piping due to better margins and the lowest cyclicity.

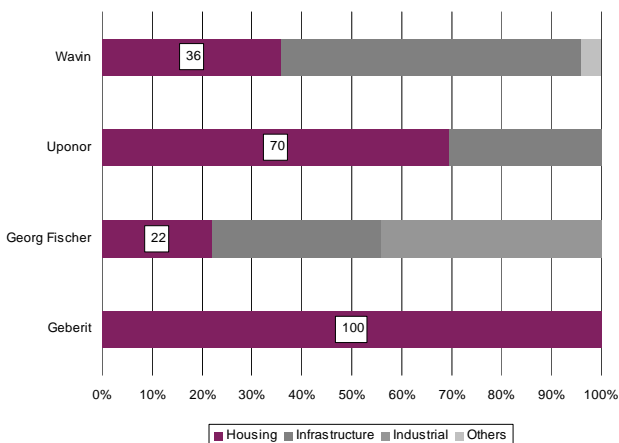
**Figure 8: Applications for plastic pipes in Germany (volumes)**



Source: Kunststoffrohrverband eV

Compared to other important piping manufacturers, Geberit boasts the strongest presence in the housing sector. In particular, infrastructure pipes are volume products with a higher raw material content, higher cyclical and lower margins. This is the reason why Geberit sold its businesses in this segment. However, also within the building, Geberit tends to have a more sophisticated product portfolio with PE building drainage pipes, press fittings and multi-layer pipes. Other companies also manufacture simple plastic pipes for under-floor heating systems.

**Figure 9: Segment exposure**



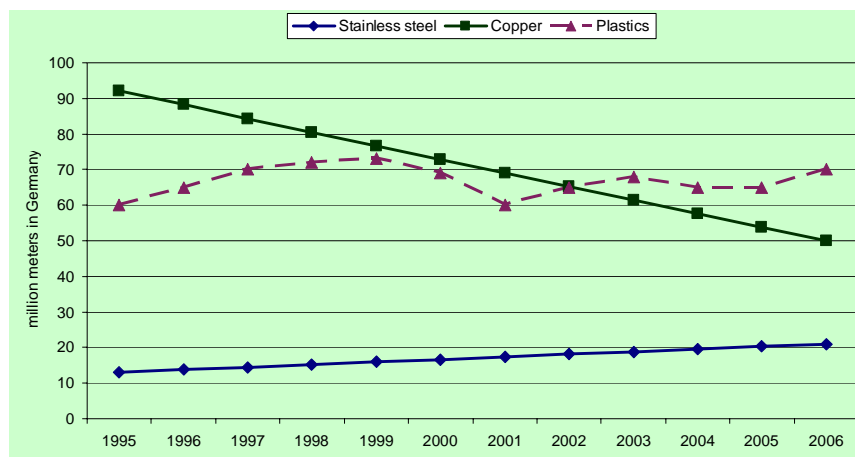
Source: companies

Geberit Piping Systems publishes only the split between Supply Systems and Building Drainage Systems. The latter accounts for about 36% of the piping revenues and produces mainly PE-based fittings. The Supply Systems include Mapress press fittings made of stainless steel, carbon steel and copper. The other important product family is Mepla multilayer pipes.

Geberit is benefitting from the replacement by plastic of expensive copper as a piping material, as shown in Figure 10. However, within plastics, PE and to a lesser degree PP are gaining market share at

the expense of PVC. Multi-layer pipes are making the fastest gains. Geberit is mainly active in multi-layer, PE and stainless steel.

**Figure 10: Materials for in-building drinking water supply in Germany (m meter)**



Source: Kunststoffrohrverband eV

→ **Opinion:** Geberit Piping Systems is expected to gain further market share based on the replacement of copper pipes with other solutions including multi-layer- and steel pipes. This process is not reversible even with lower copper prices due to lower installation times, investments for tools, and the habits of installers. Piping Systems' higher sensitivity to economic cycles is good news as this business has lower margins than the stable Sanitary Systems business. Noteworthy in this context is the fact that Uponor and Wavin are not comparable with Geberit, as the latter derives 55% of its revenues from Sanitary Systems.

- **Share buyback/acquisitions:** Since 21 January 2008, Geberit has repurchased 1.3m shares worth CHF 200m under its 5% share buyback program. The company has thus repurchased about two-thirds of the total volume. The buyback is being executed over the course of this year via a second trading line, and the repurchased shares will be cancelled.

→ **Opinion:** We have incorporated the full 5% share buyback in our model, but are assuming a conservative average buyback price of CHF 170 (average until now CHF 150). The size of the buyback leaves sufficient firing power to fund significant acquisitions. We believe that Geberit could invest up to CHF 2bn for acquisitions (150% gearing, 3x net debt/EBITDA 2008), but it remains difficult to identify available targets that meet Geberit's quality criteria; we see no imminent deal on the horizon. Our model does not incorporate potential acquisitions, but the latter could clearly increase our valuation.

- **Conclusion/recommendation:** We expect Geberit to increase its profits and cash flow even in the event of declining economic growth, thanks to (1) better penetration of existing markets, (2) entry into new markets, (3) replacement of visible flushing cistern systems, (4) replacement of copper piping systems, (5) economies of scale, (6) continuous operational excellence measures and (7) price increases. Based on our EVA<sup>®</sup>/DCF model, we have derived an economic value

and 'fair value NZB' of CHF 197 per share from our estimates, indicating upside potential of 11%. Consequently, we recommend purchase of Geberit shares with a 12-month price target of CHF 190.

**Agenda:**

- |                    |                 |
|--------------------|-----------------|
| - 12 August, 2008  | H1 2008 results |
| - 30 October, 2008 | Q3 2008 results |

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