

07 JUNE 2010

SONAE SGPS

RETAIL/HOLDING

ANALYST: SÉRGIO MARTINS

COMPANY REPORT

Growing abroad...

... Consolidating at home

We have downgraded our **price target** since the last *Company Alert* to **€1.234 (-6%)**, though we have kept our **BUY** recommendation, representing now a **62.8% upside**. We fine-tuned our Sonae's estimations and adjusted the discount rates (WACC) used in our *sum-of-the-parts* valuation.

Sonae SGPS is highly levered when compared to its peers (PSI-20 Index members). Nevertheless, we strongly believe that Sonae will be able to meet all its debt obligations. **We highlight here that are no significant refinancing needs in the next 12 months**. As a result of the high leverage, we believe Sonae SGPS stock price will have a high volatility throughout 2010, oscillating significantly when news related to indebt of Portugal and other European countries appear in the Press.

Sonae MC (33% of EV) has been consolidating its leadership position in Portugal gaining market share, 1.5% last quarter (based on data from Nielsen and TNS) and, is looking for an International Investment (Angola seems to be the 1st choice).

Sonae SR (9% of EV) is implementing a very aggressive organic growth strategy (includes the internalization process). The EBITDA margins were affected by the crisis, through the expansion to the Spanish market although SR has led to continuing growth in turnover (1Q10 grew 11.8% YoY).

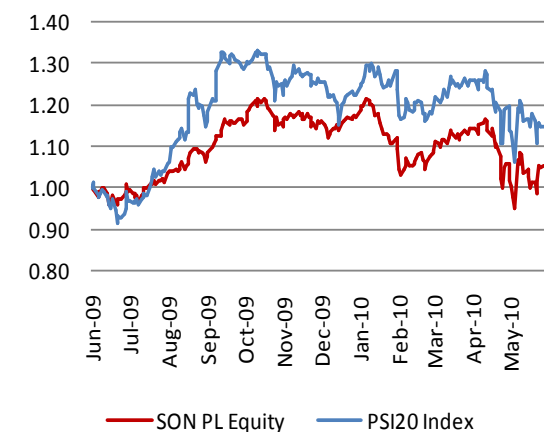
Sonae RP (29% of EV) outlook for 2010 is the asset monetization transactions through Sales & Leaseback (S&L). The idea is to release capital to invest in other business units. For instance, this year the company S&L one logistic centre and two Modelos, registering a capital gain of circa €10 million.

Sonae Sierra (17% of EV) has been posting negative results due to an increase in the European yields; the effect was balanced by the operating improvement and positive yields evolution in Brazil.

Sonaecom (10% of EV) merged the fixed and mobile businesses which we expect to result in higher EBITDA margins caused by cost savings. The Joint Venture (JV) with Vodafone allows a higher number of homes passed with Fibre To The Home. **This JV allows the company to have a significant position in the fibre business with low capital expenditures.**

Recommendation:	BUY
<i>Vs Previous Recommendation</i>	BUY
Price Target FY10:	1.234 €
<i>Vs Previous Price Target</i>	1.313 €
Price (as of 7-Jun-10)	0.747 €
Reuters: SON.LS, Bloomberg: SON PL	
52-week range (€)	0.646-0.983
Market Cap (€m)	1494
Share Capital (€m)	2000
Free Float	47%

Source: Bloomberg



Source: Bloomberg

(Values in € millions)	2009	2010E	2011E
Turnover	5,665	5,944	6375
EBITDA	667	694	725
EBIT	349	369	381
Net profit	94	119	144
P/E	15.93	12.52	10.39
EPS	0.05	0.06	0.07
P/BV	1.22	1.16	1.10
ROE	7.7%	9.2%	10.6%
ROIC	7.1%	8.2%	7.9%
Net Debt / EBITDA	5.06	4.54	4.39
Interest Coverage	2.84	3.01	3.10

Source: Analyst Estimate

Company description

Sonae SGPS, a holding with a highly concentrated portfolio in the Retail sector, is the market leader in food and specialized retail in Portugal. Sonae SGPS has two major partnerships: Sonaecom, a telecommunication company, and SonaeSierra an international specialist in shopping centres.

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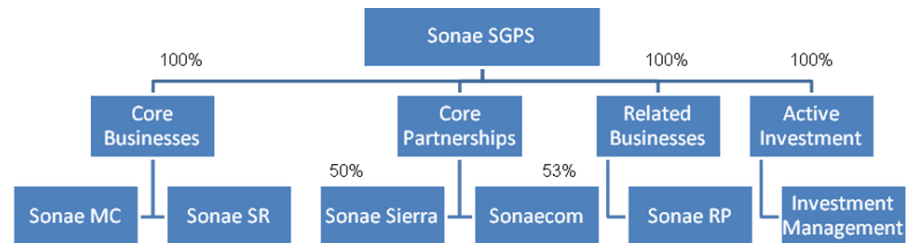
Company overview

Sonae SGPS is a **holding company** with a highly concentrated portfolio in the Retail sector. It has been strengthening its leadership position in the food and specialized **retail segments**. The company has two major partnerships in the **shopping centres** and **telecommunications** sectors through SonaeSierra and Sonaecom, respectively.

Sonae's former CEO, Belmiro de Azevedo, transformed a small industrial unit of decorative laminate into a diversified business portfolio in half a century. Blending ambition and innovation was the key success factor, with Sonae launching in Portugal the 1st hypermarket in 1985 and the 1st shopping centre in 1991. The challenge for Sonae in the future is to strength its international presence in order to leverage its future growth and profitability.

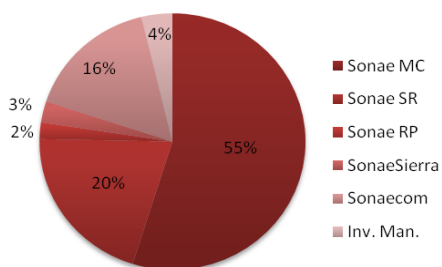
Company description

Figure 1: Company organigram



Source: Company data

Figure 2: Turnover Breakdown 2010



Source: Analyst estimates



Core Businesses (75% of overall turnover)

Sonae MC (55% of overall turnover)

Sonae MC is responsible for the Food Retail and is currently the largest retailer in Portugal. The leadership position started being strengthened in 1985, when Sonae launched its first¹ of many hypermarkets (Continente), the first hypermarkets chain in Portugal. Nowadays, the firm offers a wide range of high quality products and private label products through distinctive store formats: Continente (hypermarket), Modelo and Modelo Bonjour (supermarkets), Área Saúde (para-pharmacies), Bom Bocado (restaurants), Book.it (book shop/stationery).

The stores are mainly located at major shopping centres in regions with high population density. With an average sales area of 9,000m², Continente offers an extensive and diversified range of products (circa 70.000 items) with a promotional

¹ Opened in 1985 in Matosinhos, through a Joint Venture between Sonae Distribuição and Promodés

approach² that is strongly recognized within the Portuguese society (Top 2 preferred place to go shopping among young people (4/12 years old), which strongly influences the family's consumption pattern)³. The promotional and social projects helped to build a closer relationship with its consumers⁴, which Continente wants to leverage through the use of its loyalty card, allowing the customization of sales promotions. Last year, 84% of sales were made using such card, demonstrating the success of its implementation.

Modelo is a chain of hypermarkets and supermarkets with an average sales area of 2,000m² and 800m²⁵, respectively. The main rationale behind such concept is to target the daily shopping needs of the Portuguese consumers with more than 40.000 items⁶. Convenience is the key word behind the success of this format; the stores are located in small shopping malls with car parking lots. Moreover, Sonae SGPS is also present in other retail segments such as clothing, consumer electronic, among several others.

Área Saúde, Bom Bocado and Book.it are a complementary offer to the hyper and supermarkets. Área Saúde is a Para-pharmacy, a recent European concept, that offers beauty and health products that do not require medical prescription. Bom Bocado is a cafeteria and restaurant chain that adapts its offer to the region in which is included, combining convenience with a personalized service. Finally, the Book.it business, which targets young people through an informal atmosphere merging three business concepts in one: book shop, Stationery store and tobacco.

Sonae SR (20% of overall turnover)

Sonae SR has a wide range of brands in the Non-food retail segment. The concepts are the following: Loop (footwear), Modalfa (clothing), SportZone (sports clothing and equipment), Vobis (computer equipment), Worten (goods and consumer electronics), Worten Mobile (mobile telecommunications) and Zippy (clothing for babies and children).

Over the last years, Sonae SR has been able to conciliate its strong investment in new stores and concepts with a sustained growth. Sonae MC is the market leader in the consumer electronics (Worten) and sport goods (Sport Zone).

² Loyalty card discounts and promotional flyers are a constant in the company's marketing strategy

³ The "Net Generation" in Portugal and its Importance for Strategic Marketing: A Longitudinal Research, 2009, Dutschke G., Chaves M. and Liz C.

⁴ In 2009 "Missão Sorriso" raised approximately 500 000 Euros which reverted to the implementation of projects under the Pediatric Inpatient, Outpatient or Humanization in 11 hospitals. As in previous years, funds were raised through the sale of a Product Mission Smile. In 7 years, Continente, Modelo and its clients raised approximately 4 million Euros.

⁵ Company data

⁶ Company data

The Sonae SR is committed with the internationalization expansion plan to Spain. The chosen concepts were Sport Zone, Worten and Zippy, albeit the fact that other formats may be added in 2010.

Related Businesses (2% of overall turnover)

Sonae RP (2% of overall turnover)

Sonae RP is the business unit in charge of managing Sonae's retail properties. It is currently divided into two different teams: Asset Management and Property Management. Sonae RP is responsible for managing retail asset base (including asset development and new investments) and for managing the tenants. It has a crucial role in Sonae SGPS strategy since one of its directives is to release capital in those assets⁷. In 2009, the Invested Capital in this business unit amounted €1.5 billion.

Core Partnerships (19% of overall turnover)

SonaeSierra (3% of overall turnover)

SonaeSierra is an international shopping centre specialist equally owned by Sonae SGPS and Grosvenor. This important partnership enables the sharing of know-how, increases the investment capacity and dilutes the risk associated with this segment. In order to invest abroad, Sierra is now focused on finding local partnerships that may add supplementary knowledge regarding market environment and its specifications. The company has an integrated approach: ownership, development and management. Sonae Sierra currently owns 52 Shopping Centres, with a GLA of about 2.0 million m². Under management Sierra has more than 2,200 thousand m² of GLA and over 8,450 tenants⁸.

Sonae Sierra has a strong presence in Europe and Brazil.

The company is divided in four different business units: Sierra Investments, Sierra Management, Sierra Developments and Sierra Brazil (Figure 3).

Sonaeacom (16% of overall turnover)

Sonaeacom is focused on three different areas: Telecommunications, Software and Information System and Media. Sonae SGPS has a stake of 53% and France Telecom is a strategic minority partner with 20%. The main brand is Optimus, which offers a wide range of services and products in the telecommunication sector. In

Sonae Sierra has 35 partners from 11 different countries:

- Spread risk
- A way to be local

Figure 3: SonaeSierra structure



Source: Company data

⁷ For further detail please refer Sonae RP analysis

⁸ Company data

2009, the mobile business ended with a market share close to 20%. The other major brands are WeDo Technologies, a worldwide leader in the telecoms revenue assurance market, and Público, a Portuguese newspaper.

Sonaecom has also an important partnership with Vodafone Portugal in the Fibre segment.

Investment Management (4% of overall turnover)

The Investment Management area is a vehicle to support the implementation of corporate and business strategy through M&A planning and execution. Sonae SGPS views this business as a way to reinforce its networking with the stakeholders. The current portfolio includes Maxmat (DIY retail), Geostar (travel agency) and MDS (insurance brokerage). The company is always looking for M&A deals that fit with the pursuit strategy and create value.

Figure 4: Shareholder Structure

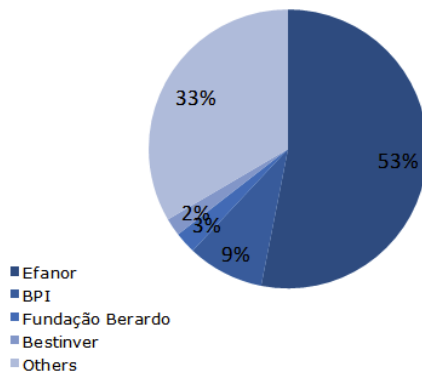
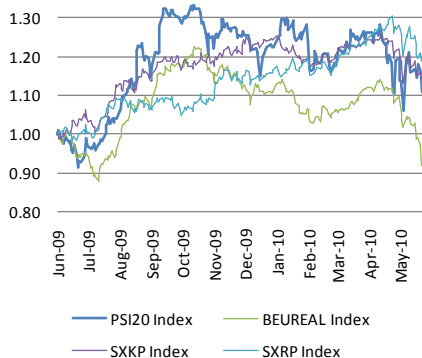


Figure 5: Sonae SGPS vs. Comparable Index per business arm



Source: Bloomberg

Shareholder structure

Sonae SGPS has a very stable shareholder structure since Efanor, owned by its Chairman Belmiro de Azevedo, holds approximately 53% of the shares and respective voting rights, exerting control over whole company. The company has also three more shareholders with a qualified participation⁹, BPI, Fundação Berardo and Bestinver.

Investment Considerations

We reiterate our **BUY** recommendation with a Price Target of **€1.234** per share due to the operational performance of the three business arms of Sonae SGPS.

Sonae SGPS was a quite volatile stock during the past two years (47%)¹⁰. In 2008, it was the second major loser of the PSI20 with a loss of 45%. Nevertheless, last year it was the best performer with an annual return of 99%. **Figure 5** depicts the evolution of Sonae SGPS versus comparables index per business arms, Retail, Telecommunications and Real Estate.

The businesses related to **Retail** are the core of this holding company. We expect **Sonae MC** Turnover to grow at a CARG (2010-2020) of 4.1% and an EBITDA of 4.0% in the same period. The Portuguese retail Modern Grocery Portuguese market will grow above inflation and MC, the food retailer leader, will consolidate its position.

⁹ Participation over 2% have to be public announced, CMVM rules

¹⁰ Computed with weekly data from 18/04/2008 until 23/04/2010, already adjusted for dividends and stock splits

Sonae SR Turnover with a CARG of 5% in the next 10 years

We forecast **Sonae SR** Turnover growing at a CARG of 5%, while EBITDA should grow at 7.3%. This business margins were fiercely affected during the past year. In the medium/long term the margins will consolidate both in Portugal (market leader in several segments) and Spain (SR is trying to gain an enough market share to become profitable). **Sonae RP** and the S&L strategy in our opinion adds an important value since it allows the company to maintain its capital expenditures and expansion plans without incurring in additional debt.

Sierra might benefit in the long run with a decrease in yields

Sonae Sierra has been reporting negative results due to an increase in the real estate yields (indirect net profit). Operationally speaking, Sierra has proven to be quite resilient in Europe (especially in Portugal and Germany) and the improvement in Brazil has proven to be crucial in the expansion of the number of shopping centres. **Since the negative results are from an indirect source, we have valued Sierra's NAV with a discount of 10% (due to yields and market expectations), however, we want to reinforce the potential of the sector.**

A potential M&A is enough to make Sonaecom very attractive

Sonaecom will drive the EBITDA margins up as soon as ANACOM announces the MTR glide path. Regarding, the fixed business we expect half of the customer revenues (50 million Euros) in 2016 to come from the Fibre investment. We have used Nova Equity Research Price Target of €1.728 vs. current price €1.381, meaning an upside of 25.1%. A potential M&A deal with Zon could trigger the stock price to €2.08 per share, representing here an upside of 50.7%.

Risk and mitigation factors:

High levered company

*However, we believe the company will be able to meet its debt obligations with no problem. **Additionally, we once again highlight the fact that the company have no refinancing needs within the next 12 months.** Part of the value of Sonae is hidden in the real estate business. The Shopping malls account for 26% of the overall Net Debt and the value of the assets are more than enough to pay the debt. The collateral is the asset itself.*

Real Estate Yields

Yields are already giving signs of stabilization.

Negative EBITDA margins from the Spanish retail unit

Last quarter the company reported positive results and we believe it was expectable given the aggressive expansion plan.

Macroeconomic Analysis

World Economy

Recovering at different speed, Emergents are stars as usual

The world economy has been recovering better than expected, though at very different speeds. The emerging economies are recovering faster and in a more solid way than its developed peers. The IMF expects a world growth rate of 4%¹¹, while the Euro-zone is expected to grow at a 1% and Portugal at 0.3% this year (Table 1 and 2). Due to the fear of a deep recession, the governments across the world have created stimulus packages to rescue its fragile economies and, as a result of such measures, several countries started posting positive GDP growth rates in end of last year. However, the legacy of the crisis is deeper: high unemployment rates, weak private demand, distortions in the financial sectors and, finally, high public deficits that have led to the recent debt crisis in Europe. Among the developed economies, Europe has been showing the greatest difficulties, especially among the southern countries. Thus the capability of the Governments, Families and Companies to proceed with the necessary deleveraging process will be essential. Throughout the previous month we have seen how the sovereign risks in developed countries may undermine the financial and economic stability in Europe, and ultimately, extend the crisis.

Table 1: Euro area and Greek Real GDP (%)

Real GDP (%)	2008	2009	2010	2011	2015
Euro Area	0.6	-4.1	1.0	1.5	1.7
Greece	2.0	-2.0	-2.0	-1.1	1.4

Source: IMF World Economic Outlook, April 2010

When the issue worldwide is bankruptcy, highly levered companies have high volatility

UE and Greece

As stated before several countries posted positive GDP growth rates and the rescue packages had a predominant role worldwide. The measures to boost demand and stabilize the financial sector were essential, despite governments are facing large public deficits. The Greek government is struggling with solvency problems which affected the whole Euro area. Furthermore, 80% of the debt holders are European Banks¹² and the risk of contamination is considerably high, meaning, that countries with higher Public Deficits could be affected with the spillover effect (i.e. Ireland, Lithuania, Portugal, Spain and United Kingdom)

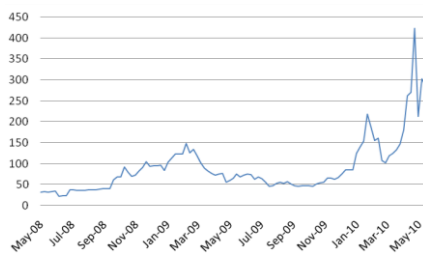
Only a concerted and determined response calmed down the market in the beginning of May with EU bailing out Greece.

Given this scenario we expect an uneven GDP growth among the European countries. The IMF projected a 1% and 1.5% growth for 2010 and 2011 (Table 2).

¹¹ World Economic Outlook, April 2010, International Monetary Fund

¹² Source: Citigroup trough and article at Business Insider: "Here's Who's Getting Pounded When Greek Debt Holders Take Their Haircut" (April 27, 2010)

Figure 6: Portuguese CDS Eur SR 5Y Corp. (bps)



Source: Bloomberg

Portugal

The economic recovery is expected to be moderate at least in Portugal. The main barriers to further growth are the high Public Deficit, the rigid labour law, low exportations growth (narrowed by external demand, particularly in its main trade partner - Spain), credit constraints, and higher unemployment. As a consequence of this challenging scenario, the cost of financing of the Portuguese government, companies and families has increased dramatically (Figure 6).

The Portuguese Prime Minister and Government outlined an ambitious plan to reduce the Public Deficit to 2.8% until 2013¹³. The Portuguese SGP¹⁴ measures were clearly not sufficient to achieve the target number and, consequently, the Portuguese Government had to take additional measures (cutting wages through supplementary taxes and increase in VAT), which ultimately led to a decrease on the disposable income.

Portugal is by far the most significant market to Sonae SGPS since 94% of the total turnover and 217% of the total operational profit before tax¹⁵ came from the domestic market in 2009. The impact off a higher cost of debt is partially offset by an expected decrease in Sonae's leverage position, the total net debt decreased 2.5% in 2009(YoY) and, according to our model, a further reduction is expected for the following years.

Spain

Spain is in a similar position, facing a mix between high unemployment rates, negative GDP growth and a high Public Deficit. The main differences are the historical GDP growth and a higher unemployment rate, which is explained by a more elastic response to output.

Sonae SR is internationalizing three non food retail brands. The market environment has not been favourable in operational terms to this segment (EBITDA decreased from -6m to -23m YOY). Sonae SR's target for international organic growth is to reach EBITDA breakeven in 2012, which might be at risk due to a harsh market environment conditions.

The cost of debt is not that relevant in this market since Sonae SR does not own the majority of the stores, implying a lower initial investment and reduced operating costs.

Table 2: Portuguese economic data

Portugal	2008	2009	2010	2011	2015
Real GDP (%)	0.0	-2.7	0.3	0.7	1.4
Consumer Prices (%)	2.7	-0.9	0.8	1.1	1.8
Unemployment rate (%)	7.6	9.5	11.0	10.3	n.a.
Public Deficit (%)	2.8	9.4	7.3	4.6	n.a.

Sources: IMF World Economic Outlook, April 2010, Instituto Nacional de Estatística (Public Deficit, 2008 and 2009) and Portuguese Government (Target Public Deficit, 2010 and 2011)

Table 3: Spanish economic data

Spain	2008	2009	2010	2011	2015
Real GDP (%)	0.9	-3.6	-0.4	0.9	1.7
Consumer Prices (%)	4.1	-0.3	1.2	1.0	1.8
Unemployment rate (%)	11.3	18.0	19.4	18.7	n.a.

Source: IMF World Economic Outlook, April 2010

¹³ Portuguese Government Target Public Deficit announced in May 2010

¹⁴ Stability and Growth Programme (SGP)

¹⁵ Sonae Report & Accounts 2009 – Segment Information

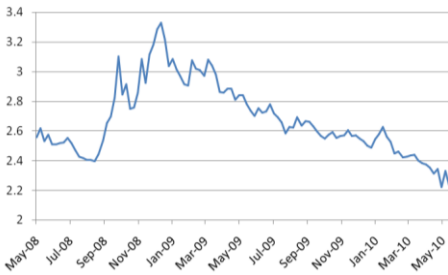
Table 4: Brazilian economic data

Brazil	2008	2009	2010	2011	2015
Real GDP (%)	5.1	-0.2	5.5	4.1	4.1
Consumer Prices (%)	5.7	4.9	5.1	4.6	4.5

Source: IMF World Economic Outlook, April 2010

Brazil

As most emergent markets, Brazil has already sustained a strong rebound and in the 1st Quarter the economy grew 9.84% QoQ¹⁶. The Brazilian financial system has not suffered as much as the developed countries did and the unemployment rates did not soar. Meanwhile, Finance Minister Guido Mantega said that the country would generate two million jobs in 2010. Nevertheless, the country faces inflationary pressures due to economic overheating.

Figure 7: EURBRL Currency

Source: Bloomberg

In Brazil Sonae SGPS only has shopping malls' through Sierra Brazil. We believe Sonae faces a favorable macroeconomic environment. The real estate yields have been recovering fast which offsets the negative impact from Europe. The positive macro environment also allowed Sierra Brazil to improve its operational activities. Currency is also a key factor to Sierra, however, given the macro environment prospects it is more probable a Real appreciation against the Euro (Figure 7).

Sonae SGPS Valuation

We valued Sonae SGPS using the Sum Of the Parts (SOP) approach by summing up the Enterprise Value (EV) of each business unit and subtracting the Net Holding Debt. The Core and the Related Businesses were evaluated by discounting the forecasted Free Cash Flows and SOP afterwards. In order to assess the EV of SonaeSierra we have applied an NAV forecast (Net Asset Value). To evaluate Sonaecom we applied our price target of €1.728 per share. The Investment Management unit was valued according to its Equity Value, which is computed by subtracting the net Debt from the Book Value. All units were fully consolidated except SonaeSierra which was proportionally consolidated (50%)¹⁷. We detail further ahead our approach and assumptions for each business unit.

A holding discount of 7.5% was applied for two reasons¹⁸. Firstly, Sonae SGPS has a large stake in an unrelated business to its core, Sonaecom. On the one hand Sonae SGPS claims to be a Retail company, on the other hand, has a 53% stake in Sonaecom (that is also a member of PSI20). The portfolio theory teaches us that any investor can easily diversify its portfolio at a lower cost. A potential M&A deal could bring down the holding discount because we could consider Sonaecom has a financial participation (4.8% of the holding discount). Another reason, are the

¹⁶ Central Bank Index of Economic Activity (ECB-Br)

¹⁷ For further detail regarding Balance Sheets, Income Statement and Cash Flow Statement please refer Financials % Other Appendixes

¹⁸ For further details please address Appendix: Why a Holding Discount? – Page 36

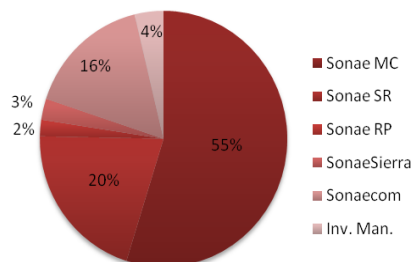
additional costs to keep this structure while the benefits do not seem clear. The holding discount includes holding costs and represents 2.8%.

SOP – Sonae SGPS

(€million)	Equity Value	Stake	Eq. V @ Stake	Weight on Sonae's Eq. V	Methodology
Retail Businesses	2,309	100%	2,309	71%	DCF
Sonae Sierra	1,098	50%	549	17%	NAV forecast
Sonaeacom	633	53%	335	10%	Eq. V (PT: €1.7)
MDS	57	100%	57	2%	EV
Sonae's EV			3,251		
Net Holding Debt			-598		
Equity Value			2,653		
Outstanding shares			2,000		
YE10 Fair Value			1.327		
Holding Discount			7.5%		
YE10 Price Target			1.234		
Current Market Price			0.747		
Upside			65.2%		

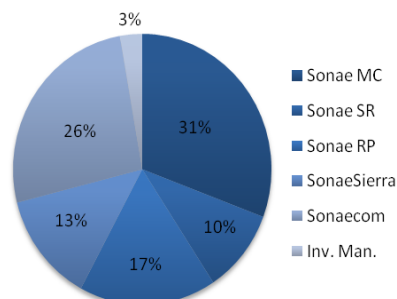
A holding company with a clear focus on Retail

Figure 8: Turnover Breakdown 2010E



Source: Analyst Estimate

Figure 9: EBITDA Breakdown 2010E



Source: Analyst Estimate

We reduce our YE10 price target to €1.234 per share, but we maintain the buy recommendation meaning an upside of 65.2%. Without the holding discount the price target would be €1.327 per share and the upside would be 77.6%. The Nova Equity Research Team computed the synergies of a potential merger between ZON and Sonaeacom¹⁹. The price target of Sonaeacom would be €2.08 meaning an increase of our price target to €1.266 per share and an upside of 69.5%.

The **Retail businesses**, including the real estate (Sonae RP), represents 71% of the Sonae SGPS EV which corroborates the strategic goal of being more a retail company instead of being a holding company. Sonae MC, the food retail business accounts for 55% of the total turnover and 31% of the EBITDA. The second largest contributor in turnover is Sonae SR which is currently expanding its portfolio to Spain.

SonaeSierra contributes with 17% of the total EV. We applied a discount of 10% to the NAV reported in the 1Q10. The discount was computed given our expectations about how the yields will evolve. The market expects a stabilization of the real estate yields throughout 2010. The company believes it might recover in end of the year. However, we have a more conservative perspective in terms of yields than the market. We believe given the current macro environment that it will take longer. We also computed the NAV (FY09) / Price (06/04/2010) to comparable companies and then we compute an average of these ratios and we obtain 90% which means that Sierra's comparable are also trading, on average, at a discount of 10%.

¹⁹ For further detail please refer our ZON and Sonaeacom equity research published in 06/04/2010

Sonaecom has an important weight in terms of EBITDA for Sonae SGPS, representing 26% in 2010 but only represents 10% of the total EV.

Retail (Core & Related Businesses)

Retail Market Overview

Retail Market in Portugal (Food and Specialized)

On the one hand, the Retail sector is mainly influenced by the purchasing power which in operating terms is translated in dominating positions in the respective segment and store location in accordance with the pursuit strategy. On the other hand it is also influenced by the population trends, which reflects: wages, inflation, job security. However, in the Food Retail business we believe inflation and the number of stores are the main drivers to estimate the turnover.

Food Retail

High concentration: Top 5 players have 70% market share

Sonae MC and Jerónimo Martins are undoubtedly the leaders in a mature market

The retail in Portugal is regarded as a mature market with a high concentration level, which is in accordance with the European trend, since the first 5 players add up to 70% market share. The danger of being squeezed out of the market is therefore dominant. Sonae and Jerónimo Martins (both players have at least 20% market share each), the unchallenged leaders in the Portuguese Food retail sector, have strengthened their positions through the acquisitions of Carrefour hypermarkets and Plus, respectively. Their strength also resulted in the market exit of Alisuper for instance. Carrefour was the first player to announce the divestiture in non core markets, which includes Portugal given the low EBITDA margins. The amount of retail space has been growing faster than the Like-for-like sales of the main players for many years, which means that costs per unit sold are rising. These higher costs have been especially obtained by better conditions from suppliers.

The market entry of Lidl and recently Aldi combined with the macroeconomic environment in 2008 and 2009 squeezed the EBITDA margins of the whole market. Sonae MC and Jerónimo Martins introduced price cuts across the board and extended their offering of convenience foods, premium products and private label products. This allowed the two main players to increase the turnover while the food retail sector struggled with deflation (2009)²⁰. Only trendy budget chains with a high turnover of goods, luxury labels and exclusive niche suppliers can keep pace, like El Corte Inglés or a few Gourmet stores.

²⁰ INE (Instituto Nacional de Estatística) Monthly reports throughout 2009

Table 5: Portuguese Retail Market evolution

	2006	2007	2008	2009	CAGR
Sonae MC	2.215	2.391	2930	3.106	12%
Jerónimo Martins	2.458	2.745	3.172	3.407	12%
Intermarché	1.243	1.393	1.484	1.581	8%
Jumbo	753	n.a.	903	1100	13%
Carrefour (Minipreço)	1110	976	908	915	-6%
Lidl	n.a.	819	935	957	8%
Others	5.006	5.487	5.624	5.969	6%
Total	12.785	13.811	15.955	17.305	10%

Source: TNS, Planet Retail and Nova Equity Research Team Estimates

The evolution of the Portuguese Retail Market is described in table 5.

Food Retail Sales accounted for 50% of the sales as a direct result of the low income levels registered in Portugal, however the Modern Grocery Distribution (MGD) represented €17.305 mn in 2009.

The gap between Portugal and the remaining European countries in terms of income levels coupled with the macroeconomic scenario of Portugal levels room for improvement in this market. Therefore we assumed low growth rates for the next years, set up marginally above the foreseen inflation rate due to the discrepancy in terms of income levels. If the Portuguese economy recovers from the crisis the market is expect to react and grow at a higher pace.

The following table resumes the MGD forecast for the Portuguese market:

Table 6: Portuguese Modern Grocery Forecast

	2010E	2011E	2012E	2013E	2014E	2015E	CAGR
Sonae MC	3.289	3.489	3.682	3.889	4.036	4.176	4.89%
Jerónimo Martins	3.592	3.714	3.969	4.181	4.366	4.499	4.60%
Others	10.504	10.634	10.973	11.42	11.994	12.621	3.74%
Total	17.385	17.834	18.624	19.49	20.396	21.296	4.14%

Source: Nova Equity Research Team Estimates

In short, the market is expected to grow at a CARG of 4.1% until 2015, with Sonae and Jerónimo Martins increasing their market shares to 21% and 20%.

Non Food Retail

In the Non Food foreigners have been consolidating their positions

The Non Food or Specialized sector has the same influences and characteristic as the food retail. It is a sector that is becoming saturated (strong competition, pressure on costs and margins). Nevertheless, is more dependent on purchasing power. Comprehensively a consumer easily spends its money in food during a recession. However, if the economy grows the consumer starts spending a higher percentage of its available income on non food products.²¹ In the non food sector, the major foreign suppliers are increasing their market positions and they are leaders in some categories (e.g. furniture, clothing, and consumer electronics). The successes of foreign companies and Sonae SR brands in non-food retailing have led to ongoing market consolidation. The store network expansion plans of those players tend to drive out small independent retailers.

²¹ Engel law

Spanish Retail Market (Specialized)

Table 7: Commercial density per country

Country	Commercial density (enterprises/10,000 population)
Germany	30.7
UK	33.6
Netherland	50.5
France	69.8
Belgium	70.8
Italy	119.6
Spain	124.5
Portugal	172.1

Source: 2007 ANGED Annual Report

The Spanish market is highly fragmented when compared to other European countries, with a commercial density ratio of 124.5 (number of enterprises over 10,000 population)²². We believe the market will naturally consolidate (integration process) as in other large countries like Germany and UK. The market consolidation might speed up due to the recent crisis since small companies with less financial capacity were extremely affected. Larger players will tend to increase market shares and Sonae SR can also take advantage. According to TNS Wordpanel consultancy, large chains like Inditex (owner of the popular signatures Zara, Bershka and Massimo Dutti, among others), Cortefiel and Decathlon have increased market shares since 2007 and the market shares at the time were: 10.7%, 4% and 1.8%, respectively²³.

As we will describe Sonae SR entered in a very competitive market. The important segments to Sonae SR are electronics (Worten), sports clothing (SportZone) and children's clothing (Zippy).

Clothing

Table 8: Average money spent on clothing

Average money spent on clothing (€)	2005	2006	2007	2008	2009
Spain	651	640	621	584	536
% change YoY		-1.7%	-3.0%	-6.0%	-8.2%

Source: TNS Worldpanel

The Spanish consumers have been losing purchasing power and, consequently, the average money spent in clothing has been reducing drastically, in 2009 (YoY), the decrease was over 8%.

The competition is fierce in every segment. The Sport clothing segment is dominated by Decathlon, owned by the French group Mulliez (also owner of Alcampo, Leroy Merlin and Norauto) that arrived in Spain in 1992, has over 75 opened stores (2009), 4 logistic warehouses, and has an estimated market share of 60%²⁴ in the specific segment. The second largest player is Intersport with 350 outlets and other important player is Décimas with 280 outlets under management.

In the children's segment, Zippy, will directly compete with Inditex although other international players are also relevant: Chicco, PreNatal and C&A.

A fierce market with several hard discount companies

²² 2007 ANGED (Asociación Nacional de Grandes Empresas de Distribución) Annual Report

²³ TNS Worldpanel information through: <http://www.diariodecadiz.es/article/economia/85271/inditex/cortefiel/y/decathlon/ya/copan/casi/tercio/mercado/textil.html>

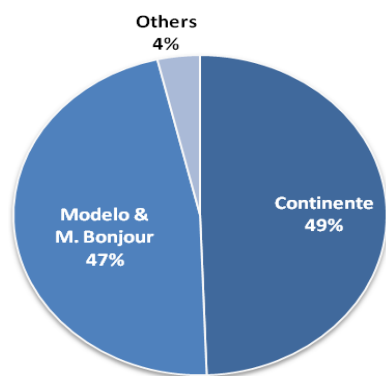
²⁴ <http://www.isgf.es/ISWEB/cuerpo.asp>

Retail Businesses (71% of EV)

Sonae SGPS has the entire food retail portfolio concentrated in Portugal. We have updated our estimations given the FY09 and 1Q10 results and the recent new updates in the economical environment. Sonae SR is the market leader in Portugal and is expanding some brands to Spain. The related business, Sonae RP, manages the real estate properties. We also applied the SOP methodology to evaluate the retail business by forecasting the discounting free cash flows. However, to consolidate accounts we also include Investment Management as Sonae does through Sonae Investments.

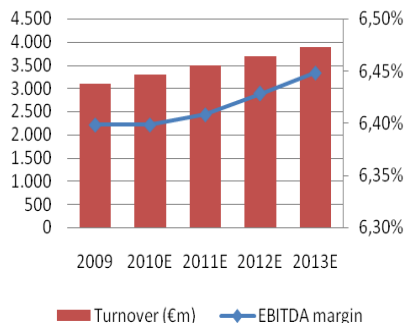
SOP – Retail Business

Figure 10: Sonae MC Turnover 2010E



Source: Analyst estimate

Figure 11: Sonae MC Operational Performance



Source: Analyst estimate

(€million)	EV	Stake	EV @ Stake	Weight on Sonae's EV	Methodology
MC	1,669	100%	1,669	46%	DCF
SR	428	100%	428	12%	DCF
RP	1,492	100%	1,492	42%	DCF
Sonae's EV			3,589		
YE10 Net Debt			1,212.8		
Minority Interest			74		
Financial Investments			41		
Equity Value			2,261		
Outstanding shares			1,000		
YE10 Price Target			2.26		

Valuation - Sonae MC (46% of EV on Retail Businesses)

We estimate a turnover of €3,289 in 2010 (5.91% growth YoY). Continente and Modelo represent 96% of the total turnover. The other brands, área saude, bom bocado and book.it, in 2010 will only represent 4%. Nevertheless, we expect a boost in turnover over time of these three brands mainly due to a significant increase in the number of stores and it will represent 7% of the total turnover in 2020. We are assuming a CARG 2010 – 2020 for Sonae MC Turnover of 4.1%. From a pure operational perspective we strongly believe Sonae MC will be able to consolidate its leadership position in the Food Retail business (35% market share²⁵). We recall that in 2009 the sector faced a deflation period and from our analysis the market leaders, Sonae and Jerónimo Martins, benefited from it. Besides, from now on, we expect a more favourable market environment and, consequently, the deflation period is over. The Food Retail EBITDA margin in 2009 was 6.4% and will increase to 6.5% in 2015 as a result of the leading position, the consolidation synergies with the ex-Carrefour stores.

²⁵Company Data, 1Q10, based on data from Nielson and TNS

Table 9: Sonae MC Highlights and Estimations

Sonae MC highlights

Sonae MC Estimates	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	CARG 10-15	CARG 10-20
Turnover (€m)	3106	3289	3489	3682	3889	4036	4176	4319	4461	4604	4748	4893	4.9%	4.1%
Turnover growth	5.99%	5.91%	6.08%	5.53%	5.62%	3.79%	3.47%	3.41%	3.29%	3.22%	3.13%	3.06%		
EBITDA	199	210	224	237	251	261	271	279	287	295	302	310	5.2%	4.0%
EBITDA margin	6.40%	6.40%	6.41%	6.43%	6.45%	6.47%	6.49%	6.46%	6.43%	6.40%	6.37%	6.34%		
EBIT	124	131	137	143	149	153	156	157	159	160	162	163	3.4%	2.2%
CAPEX	137	130	124	115	118	121	124	127	130	133	136	139		
CAPEX to Sales	4.42%	3.95%	3.55%	3.12%	3.03%	3.00%	2.97%	2.94%	2.91%	2.89%	2.86%	2.84%		

Source: Analyst Estimate

A strong turnover growth

We compute the total **turnover** by summing up the turnover of each concept²⁶. We estimate a strong turnover growth in the short and medium term because of an increase in the number of stores, consolidation of some formats and there is an inversion in the trend of inflation, meaning that we do not expect another deflation period in the food retail like in 2009. In the long term we believe a turnover growth above inflation (2%) because Sonae MC is the market leader and will use, as always, its position to grow organically.

EBITDA margins around 6.4%

The **EBITDA margins** should keep stable between 6.3% and 6.5% reflecting a mature and very competitive market. Even if Sonae MC would be able to increase those margins it would be preferable to give them to the clients in order to retain and attract new clients.

CAPEX to sales reduction over time

We believe Sonae MC in the short and medium term will decrease the **CAPEX** expenses mainly since the expansion plan will not be made through own stores and also because Sonae MC is postponing the restructure of some stores. We expect an increase in CAPEX in long term due to inflation, as it will be more expensive to restructure the required stores. However, the Capex to Sales ratio will decrease from 4.42% in 2009 to 2.89% in 2020, resulting from the explained expansion strategy of decreasing the total owned stores.

Table 10: Sonae MC Turnover per concept

Concept	2009	2010E	2011E	2012E	2015E	2020E	CARG 10-20
Continente	1568	1626	1714	1810	2014	2250	3.3%
Modelo	1458	1542	1626	1699	1920	2307	4.1%
bom bocado	18	31	38	45	59	78	9.6%
área Saude	52	70	86	97	140	214	11.7%
Book.it	5	11	15	19	28	29	10.0%
Others	4	9	10	12	15	16	6.5%
Sonae MC	3106	3289	3489	3682	4176	4893	4.1%

Source: Analyst Estimate

Sales estimations per concept

As stated before, Sonae MC has a diversified offer and we are especially optimistic with the complementary brands, bom bocado, área Saude and Book.it. We believe Sonae will increase considerably the number of stores, 10 – 20 CARG above 4.8% (Table 12) in those formats for three reasons. The first one as a **high potential growth**, with a 10 – 20 CARG turnover above 9.6% for each concept (Table 10), the second one is the ability to establish a closer relation with its clients due to a more specialized offer than its competitors. The last reason is that Sonae MC has the perfect platform to implement it with the real estate galleries (space almost occupied

²⁶ See sales estimations per concept

Table 11: Sonae SR Turnover / Sales Area ('000m2) per concept

Concept	2009	2010E	2011E	2012E	2015E	2020E	CARG 10-20
Continente	5.5	5.3	5.4	5.5	5.8	6.5	2.0%
Modelo	6.7	6.7	6.8	6.9	7.0	7.3	0.8%
bom bocado	4.5	3.7	3.8	4.1	4.6	5.4	3.9%
área Saúde	4.7	6.3	6.9	7.0	8.8	11.5	6.2%
Book.it	1.0	2.0	2.0	2.1	2.4	2.5	2.2%
Others	0.8	1.7	2.0	2.4	2.9	3.2	6.5%
Sonae MC	5.9	5.8	5.9	6.0	6.3	6.8	1.6%

by Modelo and Continente format) managed by Sonae RP, which means a small CAPEX to expand these formats.

The expansion plans for the most important formats, **Modelo and Continente**, are completely different. On one side, we believe Sonae will increase the number of Modelo stores (3.37% 10 – 20 CARG) because it is a more convenient format to its clients since it tries to satisfy the day to day shopping needs. The average sales area is 2,000m2 and 800m2 (hypermarkets and supermarkets) which means a lower CAPEX and also it is easier to get the required licenses and can be opened on Sundays. On other side, Continente will open only two hypermarkets (average 8,000m2).

Table 12: Sonae MC Stores per concept

Concept	2009	2010E	2011E	2012E	2015E	2020E	CARG 10-20
Continente	39	41	43	45	47	47	1.4%
Modelo	125	130	136	141	156	181	3.4%
bom bocado	80	129	150	172	203	228	5.9%
área Saúde	115	137	151	162	189	220	4.8%
Book.it	14	21	26	30	38	40	6.7%
Others	5	5	5	5	5	5	0.0%
Sonae MC	378	463	511	555	638	721	4.5%

Source: Analyst Estimate

Table 13: Sonae SR Sales area '000m2 per concept

Concept	2009	2010E	2011E	2012E	2015E	2020E	CARG 10-20
Continente	284	307	317	332	349	349	1.3%
Modelo	218	229	239	247	274	318	3.3%
bom bocado	4	8	10	11	13	14	5.5%
área Saúde	11	11	12	14	16	19	5.2%
Book.it	5	6	8	9	11	12	7.7%
Others	5	5	5	5	5	5	0.0%
Sonae MC	527	566	591	618	667	716	2.4%

Source: Analyst Estimate

Sonae MC - DCF

Table 15: Sonae MC WACC

WACC - Sonae MC	
WACC	7.72%
Re	9.18%
Rf	3.20%
Beta Equity	0.9
Market Premium	6.34%
Rd	6.30%
Tax Rate	26.50%
D/EV	32%
E/EV	68%
g	1.50%

Source: Analyst Estimate

The **Continente turnover will be 3.3%** 10 – 20 CARG mainly due to a **reversion in the deflation** in food retail and benefits from the customer loyalty cards. We predict Modelo turnover growing settled in the increase in the number of stores but also as a result of a 0.75% 10 – 20 CARG growth in the turnover/sales area. We estimate only 0.75% based on the fierce competition in this specific segment with important players namely: Pingo Doce, Minipreço, Intermarché and LIDL.

Table 14: Sonae MC Discounted Cash Flow

YEAR	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	CARG 10-20
EBIT	131	137	143	149	153	156	157	159	160	162	163	2.2%
+ Depreciation	79	84	89	94	97	100	104	107	111	114	118	4.1%
- Change in NWC	-55	-25	-22	-28	-21	-15	-13	-13	-13	-13	-12	
Operating Cash Flow	266	247	253	271	271	274	279	284	288	293	293	1.0%
- CapEx	130	124	115	118	121	124	127	130	133	136	139	0.7%
Cash Flow after investments	136	123	138	153	150	147	147	149	151	152	154	1.3%
-Income Taxes	35	36	38	39	40	41	42	42	42	43	43	2.2%
FCF	101	86	100	113	109	106	106	107	108	110	111	0.9%
Terminal Value											1,804	
DF	1.00	0.93	0.86	0.80	0.74	0.69	0.64	0.59	0.55	0.51	0.48	
Discounted Cash Flow	101	80	87	91	81	73	68	64	60	56	910	
Enterprise Value	1,669											

Source: Analyst Estimate

We have applied a WACC of 8.33% to discount the Free Cash Flows²⁷, which implies an **EV/EBITDA of 8x and 7.6x** in 2010 and 2011²⁸, respectively. The sector average EV/EBITDA is 7.4x and 6.8x for the same period (Table 16). Therefore, our growth perspective is slightly above the industry which can be explained by Sonae MC being the market leader in Portugal. We applied a terminal growth rate of 1.5% which is below the expected inflation rate of 2% because we believe it is already a mature market and will consolidate even more. The competition will be fierce and is likely prices to go down for this reason.

²⁷ For further detail about the estimations and main assumptions please refer Appendix: Valuation Summary – Page 37

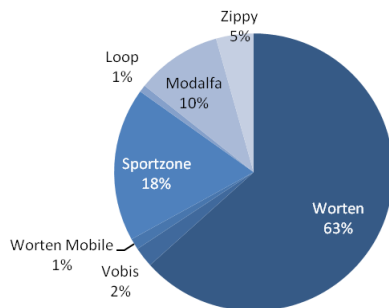
²⁸ Analyst Estimate

Table 16: Sonae MC Comparables

	EPS					CAGR	P/E				EV/EBITDA			
	10E	11E	12E	13E			10E	11E	12E	13E	10E	11E	12E	13E
Tesco	0.3	0.4	0.4	0.5	11%	14.7	13.3	11.9	10.6	9.6	8.7	8.1	7.2	
Carrefour	2.3	2.8	3.2	3.6	16%	16.5	13.8	12.1	10.6	8.0	7.3	6.7	6.1	
Metro	2.9	3.5	4.1	4.6	17%	15.8	12.8	11.1	9.9	5.4	4.9	4.4	4.2	
Ahold	0.8	0.9	1.0	1.1	9%	12.0	10.8	9.8	9.2	6.0	5.7	5.4	5.2	
Casino	5.1	5.7	6.3	6.7	10%	12.8	11.4	10.5	9.7	6.6	6.2	5.8	5.6	
Sainsbury	0.3	0.3	0.3	0.4	10%	15.1	14.0	12.6	11.2	7.2	6.7	6.1	5.7	
Delhaize	5.4	5.8	6.3	6.1	4.50%	11.5	10.6	9.9	10.1	5.6	5.3	5.0	5.0	
Morrison	0.2	0.3	0.3	0.3	13%	14.7	12.8	11.6	10.7	7.9	7.1	6.5	6.1	
Colruyt	10.3	11.2	12.1	13.1	8%	17.9	16.4	15.3	14.0	10.1	9.3	8.8	8.0	
Sector					11%	14.6	12.9	11.6	10.7	7.4	6.8	6.3	5.9	

Source: Bloomberg

Figure 12: Sonae SR Breakdown Turnover 2010E



Source: Analyst estimate

Valuation - Sonae SR (12% of EV on Retail Businesses)

We have forecasted a turnover of €1.239 in 2010 (9.45% growth YoY). Sportzone, Worten and Modalfa represented 93% of the total turnover (Figure 12). We also expect **Sportzone and Worten to increase their representativeness** in Sonae's turnover in the following years as they expand to the Spanish market.

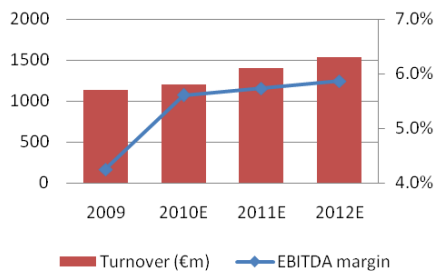
We expect a CARG (2010-2015) for Sonae SR Turnover of 9.1% in the first two years, which can be explained by the **increase in the number of stores**, mostly in Spain. The CARG (2010-2020) of 5.0% is well below the previous one, though still quite high. We believe the turnover growth after 2016 will slow down because the **Portuguese and Spanish markets will consolidate**, with the competition increasing significantly. The market is still complicated for specialized retailers since demand is more elastic than the one faced by food retailers. Nevertheless, we expect the EBITDA margin to stabilize and thereafter consolidate around to 6.9% in the long term.

Table 17: Sonae SR Highlights and Estimates

Sonae SR Estimates	2009	2010E	2011E	2012E	2015E	2020E	CARG 10-15	CARG 10-20
Turnover (€m)	1132	1198	1406	1531	1850	1959	9.1%	5.0%
Turnover growth	22.0%	5.9%	17.3%	8.9%	7.2%	0.5%		
EBITDA	48	67	81	90	116	135	11.5%	7.3%
EBITDA margin	4.2%	5.6%	5.7%	5.9%	6.3%	6.9%		
EBIT	10	30	37	43	59	75	14.2%	9.5%
CAPEX	97	102	114	107	89	74	-2.7%	-3.1%
CAPEX to Sales	8.6%	8.5%	8.1%	7.0%	4.8%	3.8%		

Source: Analyst estimate

Figure 13: Sonae SR Operational Performance



Source: Analyst estimate

In order to compute the turnover of Sonae MC, we have estimated the turnover of each concept separately. The main value driver of SR is the number of stores²⁹ it operates, as well as the expected inflation for the following years.

Table 18: Sonae SR Turnover per concept

Concept	2009	2010E	2011E	2012E	2015E	2020E	CARG 10 - 20
Worten	708	759	901	977	1183	1231	4.95%
Vobis	45	28	28	28	31	35	2.30%
Worten Mobile	15	16	17	18	20	22	3.60%
Sportzone	205	215	250	280	337	362	5.37%
Loop	5	10	14	18	33	46	16.54%
Modalfa	115	119	130	136	151	159	2.91%
Zippy	39	52	64	73	95	104	7.18%
Sonae SR	1132	1198	1406	1531	1850	1959	5.04%

Source: Analyst Estimate

Table 19: Sonae SR Turnover / Sales Area ('000m2) per concept

Concept	2009	2010E	2011E	2012E	2015E	2020E	CARG 10 - 20
Worten	4.8	5.0	5.1	5.3	5.3	5.3	0.59%
Vobis	5.6	5.6	5.6	5.7	6.3	7.1	2.30%
Worten Mobile	15.0	11.1	12.7	13.5	13.9	15.1	3.09%
Sportzone	0.2	0.2	0.2	0.2	0.2	0.2	-0.05%
Loop	102.5	102.2	87.2	98.3	97.8	96.5	-0.57%
Modalfa	0.1	0.2	0.3	0.3	0.5	0.7	14.38%
Zippy	2.5	2.4	2.5	2.5	2.6	2.7	1.10%
Sonae SR	3.7	3.8	3.9	4.0	4.2	4.3	1.13%

Source: Analyst Estimate

Table 21: Sonae SR Stores per concept

Concept	2009	2010E	2011E	2012E	2015E	2020E	CARG 10 - 20
Worten	146	152	163	169	189	196	2.57%
Vobis	17	9	7	5	5	5	-5.71%
Worten Mobile	48	50	52	54	58	58	1.50%
Sportzone	89	101	115	125	142	144	3.61%
Loop	11	20	27	33	51	60	11.61%
Modalfa	99	107	116	120	129	129	1.89%
Zippy	44	58	71	80	100	105	6.11%
Sonae SR	454	497	551	586	674	697	3.44%

Source: Analyst Estimate

Table 20: Sonae SR Sales area '000m2 per concept

Concept	2009	2010E	2011E	2012E	2015E	2020E	CARG 10 - 20
Worten	148	153	176	185	223	234	4.34%
Vobis	8	5	5	5	5	5	0.00%
Worten Mobile	1	1	1	1	1	1	0.49%
Sportzone	78	80	90	99	112	114	3.65%
Loop	2	2.1	2.87	2.85	3.45	3.75	5.97%
Modalfa	51	52	57	59	63	63	1.89%
Zippy	16	21	26	29	37	38	6.11%
Sonae SR	304	314	358	381	445	459	3.86%

Source: Analyst Estimate

The Capex will increase in the next two years in order to support the international expansion. After 2013, the Capex will slow down and, in the long

run, should mainly be spent on refurbishments (revamping). Sonae SR prefers to expand its stores through renting, since it allows a significant reduction of operational costs. Thus, the Capex to Sales ratio will decrease from 8.6% in 2009 to 2.8% in 2020.

Sales estimations per concept

We have estimated the evolution kpi Turnover per Sales area ('000m2) for each concept and, then, we have multiplied by the sales area in that specific year. We have forecasted the Sales area taking into account the average stores to sales area of each segment and we have then projected the number of stores³⁰. We have also considered an adjusted period of 2 months until a recently opened store have the approximately same kpi of other stores³¹.

In terms of turnover per sales area (Table 19), we expect a high CARG (2010 – 2020) for Modalfa, Worten Mobile and Vobis. Modalfa was highly affected by the crisis and we believe it will organically recover in the following years as consumer income starts rising again. Vobis has a high CARG since we expect the company to shut down this brand, leading to a liquidation process in several stores through low prices to sell off all the products. Consequently, we have considered a negative EBITDA margin from this business. The **anchor stores**, Sportzone and Worten, have a CARG (2010 – 2020) of -0.05% and 0.59% (Table 19), respectively, though the turnover for these brands should be high due to a strong increase in number of stores. We expect low numbers due to the fierce competition in those segments in both Portugal and Spain. Decathlon, Fnac, Media Market and Radio Popular should also push down the prices.

Loop has the highest potential regarding new store openings with an 11.61% CARG (2010 – 2020) in our model (Table 21). Loop stores are expected to open in different shopping centres, as well in some real estate galleries owned by Sonae RP. Beginning in 2013, we have considered the opening of 5 stores to test the implementation of this brand in Spain. We believe the company just postponed the

²⁹ For further detail please refer "Close look at Spain"

³⁰ Es estimation of the number stores considering Company Data, expansion strategy and Analyst expectations about how the market will evolve and consolidate in the future

³¹ Conversation with a Sonae SGPS employee

timeframe and, in our opinion, the probability of Loop entering in the Spanish market is quite high. For that reason we have consider an increase of 5 testing stores in 2013.

Sonae SR - DCF

Table 22: Sonae SR Implied ratios

Implied Ratios	2010E	2011E	2012E	2015E	2020E
EV / Sales	0.4x	0.3x	0.3x	0.2x	0.2x
EV / EBITDA	6.1x	5.1x	4.5x	3.5x	3x

Source: Analyst Estimate

Table 24: Sonae SR WACC

WACC - Sonae SR	
WACC	8.53%
Re	10.36%
Rf	3.20%
Beta Equity	1.13
Market Premium	6.34%
Rd	6.30%
Tax Rate	26.50%
D/(E+D)	32%
E/(E+D)	68%
g	2.00%

Source: Analyst Estimate

Table 23: Sonae SR Discounted Cash Flow

YEAR	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	CARG 10-20
EBIT	30	37	43	49	52	59	62	66	69	72	75	9.5%
+ Depreciation	40	47	52	56	58	62	64	65	65	66	66	5.0%
- Change in NWC	-15	-20	-15	-15	-5	-14	-3	-2	-4	-3	-3	
Operating Cash Flow	86	105	109	120	116	135	129	132	138	141	144	5.3%
- CapEx	102	114	107	98	92	89	83	83	77	76	74	-3.1%
Cash Flow after investments	-16	-9	2	22	25	46	46	50	61	65	69	
-Income Taxes	8	10	11	13	14	16	17	17	18	19	20	9.5%
FCF	-24	-19	-9	9	11	31	29	32	42	46	49	7.5%
Terminal Value											772	
DF	1.00	0.92	0.85	0.78	0.72	0.66	0.61	0.56	0.52	0.48	0.44	
Discounted Cash Flow	-24	-18	-8	7	8	20	18	18	22	22	362	
Enterprise Value	428											

Source: Analyst Estimate

We have the traditional approach to estimate the Free Cash Flows and then we applied we applied a WACC of 8.53%³² to discount (Table 24). The implied EV/EBITDA of 6.1x and 5.1x in 2010 and 2011 (Table 23), respectively. The weighted³³ average EV/EBITDA multiple is 6.4x and 5.3x for the same period (Table 25). Therefore, in 2010 we will be slightly below the industry but in 2011 we will be above due to a consolidation of the Spanish.

Close look at Spain

Sonae SR is **internationalizing** some of its brands. In the 1Q10 the turnover from this market represented 18.5% of the unit turnover. We recall that the 1st store, Sportzone, was opened in the 2Q08 in a shopping mall (Islazul, Madrid). In Portugal, Sonae SR brands are usually located in shopping centres or inside real estate galleries with a food retailer. The strategy in Spain is exactly the same. Sierra owns 11 shopping centres in Spain which serve as a lever to implement the internationalization plan. We believe this is vital to SR success, since it allows brand and customer perception testing. As stated in the retail overview, Sonae SR has been entering in a very competitive market. We believe the best approach is to have a strong presence in the shopping centres, if the company follows this strategy, in theory the potential market are the 530 shopping centres in Spain³⁴. However, we believe in our analysis period that no brand will have more than 50 opened stores. The required Capex to a more aggressive strategy would be very high (Sonae SGPS also wants to internationalize the food retail business, Sonae MC) and the EBITDA margins would take a longer period to consolidate. We estimate positive EBITDA

Table 25: Sonae SR Comparables

	EV/Sales		EV/EBITDA			
	10E	11E	10E	11E	12E	13E
European electronic						
Best Buy	0.1	0.1	6.2	4.9	4.3	4.3
DGSI	0.1	0.1	3.9	3.6	2.9	2.0
Kesa	0.1	0.1	2.6	2.3	2.0	1.7
Sector average	0.1	0.1	4.3	3.6	3.1	2.7
European Textile and Sports						
H&M	3.0	2.7	11.4	10.1	8.9	8.0
Inditex	2.0	1.9	11.3	9.1	7.9	6.8
Next	1.2	1.2	7.0	6.1	5.6	5.3
JDSports	0.4	0.4	5.6	4.1	3.0	2.4
Sector average	1.7	1.5	8.8	7.4	6.3	5.6
Weighted multiple	0.7	0.6	6.4	5.3	4.6	4.0

Source: Analyst Estimate

³² For further detail about the estimations and main assumptions please refer Appendix: Valuation Summary – Page 37

³³ Weight in turnover of 65% to Electronics and 35% to Clothing and Sports and, 54% / 46% in terms of EBITDA

³⁴ Aguirre Newman: Estudio del Mercado de Centros Comerciales marzo 2010

Table 26: Historical data of Sonae SR in Spain

Sonae SR - Spain	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10
Number of stores	1	3	16	17	23	27	38	40
Worten	0	0	10	10	11	12	14	15
Sport Zone	1	3	6	7	10	11	14	15
Zippy	0	0	0	0	2	4	10	10
Sales Area ('000 m2)	2	5	33	34	39	45	56	59
Worten	0	0	24	24	26	30	34	36
Sport Zone	2	5	9	10	12	13	17	19
Zippy	0	0	0	0	1	2	4	4

Source: Company data

margins throughout 2011 and thereafter. The turnover has been increasing mainly due to an increase in the number of stores. The strategy is focused in gaining market share and then in medium term to consolidate its position. Table 26 and 27 summarize the information up to now.

Table 27: Historical data of Sonae SR in Spain

Sonae SR - Spain (million)	2Q08	3Q08	4Q08	1Q09	2Q09	3Q09	4Q09	1Q10
Turnover	0.8	2.0	27.2	25.2	34.3	38.0	46.4	50.7
Turnover/Sales Area ('000 m2)	0.4	0.4	0.8	0.7	0.9	0.8	0.8	0.9
EBITDA	-0.6	-0.9	-4.7	-4.1	-8.2	-5.9	-4.5	-3.9
EBITDA margin	-70.1%	-44.1%	-17.2%	-16.2%	-23.9%	-15.5%	-9.6%	-7.6%
Invested Capital	1.3	4.6	16.3	56.5	60.0	69.8	71.1	105.9
% Turnover of SR	0.4%	0.8%	8.6%	11.2%	13.8%	13.4%	12.3%	18.5%

Source: Company data

Table 28: Sonae RP Highlights and Estimations

Sonae RP Estimates	2009	2010E	2011E	2012E	2015E	2020E	CARG 10-15	CARG 10-20
Turnover (€m)	123	119	117	120	130	172	1.2%	3.7%
Turnover growth	12.5%	-3.1%	-1.5%	1.9%	3.6%	6.4%		
EBITDA	111	112	108	109	118	155	1.2%	3.2%
EBITDA margin	90.1%	94.2%	92.1%	91.1%	90.1%	90.1%		
EBIT	83	84	81	82	88	116	1.1%	3.2%
CAPEX	91	46	40	36	23	5		
CAPEX to Sales	73.8%	38.2%	34.4%	30.5%	17.6%	2.9%		

Source: Analyst Estimate

Valuation - Sonae RP (42% of EV on Retail Businesses)

Sonae RP is the business unit in charge for managing the retail property, and consequently, the EBITDA mostly reflects internal rents. Sonae SPGS sets rents in line with the market yields, which affect the underlying investment value. We estimate a turnover for 2010 of 117 million Euros. The EBITDA margins will consolidate around 90% and the Capex to Sales ratio will reduce every year because the company prefers to rent spaces as an alternative of being the owner (Table 28). Capex includes the acquisition of additional retail area and investment expenses related to future openings. We estimate for 2010 EV/Sales and EV/EBITDA ratios of 12.5x and 13.3x, respectively (Table 29).

Table 29: Sonae RP Implied Ratios

Implied Ratios	2010E	2011E	2012E	2020E
EV / Sales	12.5x	12.7x	12.5x	8.7x
EV / EBITDA	13.3x	13.8x	13.7x	9.3x

Source: Analyst Estimate

The outlook for this unit is an asset monetization transactions (adjust non income generating assets into those that generate) through operations of Sales & Leaseback (S&Lb). This strategy will release capital to invest or pay down debt.

Recycling capital

The goal for 2010 was to S&Lb one logistic centre and a portfolio of 20 Modelo stores³⁵. On 20th of May 2010, Sonae announced the conclusion of the planned initial phase with the S&Lb of Azambuja logistic platform and 2 Modelo stores involving property assets valued at 45.4 million Euros. Sonae registered a capital gain of circa 10 million Euros. The logistic platform was sold to international investors, has been valued at 33.2 million (initial yield of 7.62% on a "Triple Net" basis³⁶) Euros and the leaseback has a duration period of 20 years. The Modelo stores have been valued at 12.2 million Euros (initial yield of 7.23% on a "Triple Net" basis) with a renting period of 15years. The deals are in-line with the strategy of releasing capital defined to 2010.

³⁵ Company Report & Accounts 2009³⁶ Rents, operating expenses, insurance, tax and maintenance costs assumed by the tenant

We believe Sonae RP will carry on with this strategy in the following years in order to be able to invest and internationalize its core businesses: Food and Specialized Retail.

A S&Lb operation is a commercial real estate transaction that consists on selling a property and promptly lease it back. Typically, the assets are on the Balance Sheet (BS) at book value and the market value is higher but investors do not perceive that value. A S&Lb operation frees up equity that is locked on the BS by converting it into cash and, at the same time forces the investors to realize the intrinsic value of those assets. Nevertheless, there are additional benefits. For instance, lease payments are expenses which will shield the company against high taxation and not only allow a focus on the core business but also transfers risk to the new owner and reduces the company's results to fluctuations in the real estate yields. The improvement of the financial ratios is also relevant (ROA or current ratio).

To evaluate Sonae RP we have the DCF methodology. Table 30 summarizes the approach used. In order to discount the FCF we have applied a wacc of 7.5% (Table 31). The main assumptions are summarized on Table 31. Therefore, this unit Enterprise Value is 1,492 million Euros.

Table 31: Sonae RP WACC

WACC - Sonae RP	
WACC	7.5%
Re	8.9%
Rf	3.2%
Beta Equity	0.9
Market Premium	6.34%
Rd	6.30%
Tax Rate	26.5%
D/(E+D)	32.0%
E/(E+D)	68.0%
g	1.0%

Source: Analyst Estimate

Table 30: Sonae RP Discounted Cash Flow

YEAR	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E	CARG
EBIT	84	81	82	84	86	88	92	96	102	109	116	3.2%
+ Depreciation	28	28	27	29	29	31	31	34	37	41	45	5.0%
- Change in NWC	1	0	7	0	0	0	0	-1	-1	-1	-1	
Operating Cash Flow	112	108	102	113	115	119	123	131	140	150	162	3.8%
- CapEx	46	40	36	33	25	23	19	18	15	9	5	-19.8%
Cash Flow after investments	66	67	66	80	90	96	104	113	125	141	157	9.0%
-Income Taxes	22	21	22	22	23	23	24	26	27	29	31	3.2%
FCF	44	46	44	57	67	72	80	87	98	113	126	11.1%
Terminal Value											1,950	
DF	1.00	0.93	0.86	0.80	0.75	0.70	0.65	0.60	0.56	0.52	0.48	
Discounted Cash Flow	44	43	38	46	50	50	52	52	55	59	1,004	
Enterprise Value	1,492											

Source: Analyst Estimate

Figure 14: European presence and number of shopping centres per country

Shopping Centres

Market Overview

The primary influences in a real estate investment are rents, occupancy rate, location, and population migration trends³⁷. We believe the consumer preferences depend on the diversity of offered stores within the shopping mall, anchor stores and location (proximity). The main value drivers in the industry are high rents and low vacancy rates. Whereas, high turnover of tenants can have a negative impact on results because usually it increases significantly the costs (refurbishment expenditures) and typically it is not possible to compensate through a rent increases or have an



Source: SonaeSierra Data

³⁷ Real Estate market Valuation and Analysis, J. Kahr and M. C. Thomsett, 2005, Willey Finance

efficiency gain. Shopping mall managers are dependent on large clients, for example, Inditex or C&A.

Europe

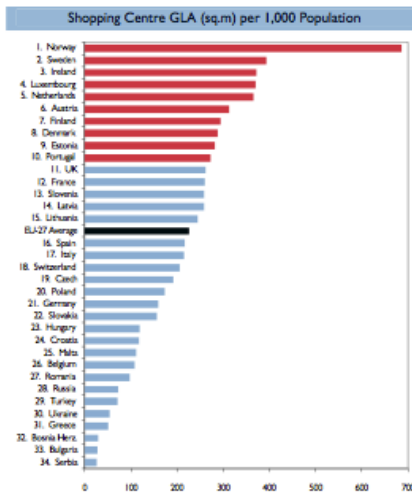
The real estate properties across Europe are still suffering the effects of the financial crisis. The negative consequences were an increase in the real estate yields and a diminishing rent per sqm (declined by 2.4% in 2009)³⁸. DG HYP in the same report stated that the downward trend might persist in 2010. Despite, the economic crisis, new shopping centres were opened and C&W bets on a quicker recovery than expected and a large number of under revision shopping centres projects can be revitalized soon³⁹.

We will focus our analysis in the countries where Sierra is present (Figure 14).

Portugal is the 10th country in Europe in terms of GLA per 1,000 Population (Figure 15)⁴⁰ which means the market is becoming highly saturated. Lisbon, Oporto and other more populated cities have the highest concentration, although the players are expanding to secondary locations, for example, Torres Vedras⁴¹ or to other counties with less than 100,000 habitants. The expansion to secondary locations will be, in our opinion, the key growth driver. According to the company Jones Lang LaSalle, the commercial area will grow 26% until 2012⁴² (assuming all the announced projects will be carried on). The Portuguese shopping mall and retail park market is dominated by five players: Sonae Sierra, Amorim Imobiliária, Mundicenter, Multi developments and Bouyges.

The EU-27 average GLA per 1000 Population stands at 225.6⁴³. Spain is the first country below average and the 16th country in Europe. As stated in the market overview about the retail in Spain is highly fragmented. Thus, we expect a market consolidation, as large clients will tend to prefer shopping malls to expand its stores since to deal in the tenant market is more complex than to negotiate with a specialized company. Italy (Sierra has 4 Shopping centres) shares the same trends as Spain. Regarding the remaining countries where Sonae is present, we can see that clearly Germany, Greece and Romania fall behind the EU-27 average of retailing space. In spite of having a high unexplored potential, each has a set of specificities

Figure 15: European Shopping Centre GLA (sqm) per 1.000 Population



Source: Marketbeat Shopping centre development report Europe, March 2010, C&W

Growth Potential:

Sierra is present in several countries with low GLA/1000 population.

³⁸ Real Estate Market 2010|1, DG HYP, March 2010

³⁹ "Development of shopping centres will decline to a low point in 2011, March 2010, C&W

⁴⁰ Figure 15 in more detail in Financials & Appendixes

⁴¹ Torres Vedras has 77.566 habitants, Source: Portuguese Census 2008

⁴² http://economico.sapo.pt/noticias/numero-de-centros-comerciais-em-portugal-ja-comecou-a-decrescer_82991.html

⁴³ Marketbeat Shopping centre development report Europe, March 2010, C&W

that conditions growth. Germany has weak sales growth in retail⁴⁴, whereas Greece's debt poses an obstacle to project financing (Sierra is revising two projects), Romania on the other hand presents high economic growth rates (7.5% and 5.13% in 2010 and 2011, respectively)⁴⁵ but has a significant country risk though.

Given the above mentioned country analysis we believe that given the current downward trend, until a suitable location is found, GLA expansion should be postponed in these countries.

Brazil

Brazil is in 1st place of Top 10 overseas property investments in 2010⁴⁶, the steep economic growth made it attractive to European and North American investors.

Domestically, the investors are also keen to acquire properties, especially, pension funds⁴⁷. In December 2009 the total number of shopping centres was 396⁴⁸ while Sierra has only 10. The projected pipeline for 2010 is the opening of 17 new shopping centres; Sierra will open one of them. In 2012, Sierra will open two more. The Southeast is the more populated and richest area⁴⁹, includes São Paulo and Rio de Janeiro, and as expected has the largest number of centres (Table 32). The Northeast has the lowest number of centres per population and, thus has a high potential growth in terms of #centres and GLA.

Valuation - Sonae Sierra (17% of EV)

Sonae Sierra represents 17% of the overall EV of Sonae SGPS. The company had a negative consolidated net profit in 2008 and 2009 due to an increase in the real estate yields which clearly this affected the Real Estate NAV per share that decreased from €52.59 in 2007 to €37.78 in 2009 (Table 33).

We valued Sonae Sierra through a forecast of its NAV reported in the 1Q10. The NAV is assessed by an independent real estate specialist, Cushman & Wakefield (C&W). C&W appraises the investment properties fair value every quarter⁵⁰ using the standard practices of the RICS Appraisal and valuation Manual. When changes in fair value occur it is accounted in the respective quarter. In the 1Q10 Sonae Sierra reported a NAV of 1,208 million Euros, which corresponds to a NAV per share of €37.14 (Figure 16). C&W evaluates the market value of the investment properties by

Table 32: Number of Shopping centres per region in 2009

#Shoppings per region	# Centres	GLA (000's m ²)	Population (millions)
North	11	297	8%
Northeast	55	1,287	27%
Center-West	36	771	7%
Southeast	213	5,385	43%
South	77	1,411	15%
Total	392	9,151	100%

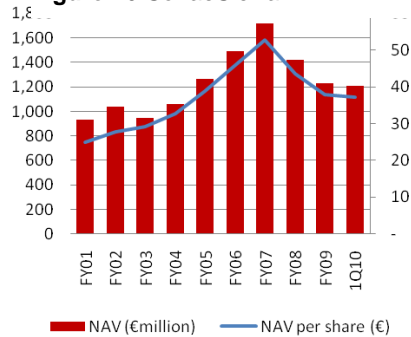
Source: Brazilian Shopping Centers Association (ABRASCE) and Instituto Brasileiro de Geografia e Estatística (IBGE)

Table 33: Sierra Highlights

Sierra Highlights	2006	2007	2008	2009
Real Estate NAV per share (€)	45.82	52.59	43.55	37.78
Real Estate NAV as of 31 Dec. (€million)	1,490	1,713	1,416	1,228
OMV of assets under management (€million)	4,721	6,154	6,166	6,340
Consolidated Net Profit - IAS (€million)	271	300	-198	-160
Consolidated NOI - IAS (€million)	149	156	179	180
# of tenant contracts under management (€million)	7,293	8,162	8,455	8,924
GLA owned in operating centres (000's m ²)	1,660	1,855	1,963	2,059
GLA under management (000's m ²)	2,001	2,183	2,163	2,284

Source: Company Data

Figure 16: SonaeSierra NAV



Source: Company Data

⁴⁴ Real Estate Market 2010|1, DG HYP, March 2010

⁴⁵ World Economic Outlook, April 2010, International Monetary Fund

⁴⁶ Homesoverseas.co.uk ranking

⁴⁷ "Global Market Perspective: A BRIC built recovery?", March 2010, Jones Lang LaSalle

⁴⁸ Portaldosshoppings.com.br

⁴⁹ According to Instituto Brasileiro de Geografia e Estatística (IBGE) represents circa 60% of the overall GDP

⁵⁰ A full valuation is only compulsory to Half and Full Year Reports

estimating and discounting the Net operating Income (NOI) of each shopping centre for the subsequent 10 years. The terminal value is computed by applying an Exit Yield (or Cap rate) on the projected 11th year NOI. The Exit Yields are computed by dividing NOI by the price of selling the asset, taking into account comparables. In order to apply the DCF model the first step should be delineate the retail trade area taking into account the distance and intercept locations^{51,52}.

Table 34: Comparables quoted at Discount/Premium

Euros	NAV FY09	Price (04-06-10)	Discount / Premium
Fonciere des regions	79.2	74.9	95%
Unibail-Rodanco	128.2	126.8	99%
Klepierre	28.7	21.8	76%
Average			90%

Source: Bloomberg and Analyst estimation

We applied a discount of 10% to the last reported NAV (1,208 €million). Due to the low liquidity⁵³ of its assets when compared to alternative investments; the evolution of the real estate yields, which are still stabilizing; the market sentiment and time⁵⁴.

The liquidity reason is linked to the market sentiment. Shopping centres that are near to opening date will tend to have a higher value (lower discount) as the probability of selling that asset increases significantly. The market sentiment captures more than the specific risk of one security or asset⁵⁵. With the aim of analyzing whether Sierra NAV should trade at discount or premium we have computed a NAV FY09 to Price (04-06-2010) ratio to several comparable companies (Table 34). Then we have computed average and we got a value of 90%. Thus, we have applied the 10% discount which is in-line with how we believe the real estate yields will evolve.

We analyzed the variation in fair value of the investment properties for each shopping⁵⁶ and per country (Table 35 and 36). The only two countries with a positive evolution were Brazil and Germany, mostly explained by the opening of two shopping centres (one in each country). If we exclude these two shopping centres, only Brazil had a positive change while Germany was negative by 3.3% due to high real estate yields that affected all Europe. It is also important to analyze the behavior of the yields in the referred markets (maximum, minimum and average) throughout 2008 and 2009 (Table 37).

Table 35: Fair Value of the investment properties per country (€million)

Country	Amount		Change in Amount
	FY09	FY08	
Portugal	1,451.1	1,577.7	-8.0%
Brazil	360.6	183.3	96.7%
Spain	702.5	825.2	-14.9%
Italy	299.6	365.2	-18.0%
Germany	468.9	327.8	43.1%
Romania	30.0	37.5	-20.2%
Greece	36.97	43.593	-15.2%
Total	1898.5	1782.6	6.5%

Source: Company Data

Table 36: Fair Value of the investment properties per country excluding the shopping opened in 2009(€million)

Country	Amount		Change in Amount
	FY09	FY08	
Portugal	1,451.1	1,577.7	-8.0%
Brazil	287.4	183.3	56.8%
Spain	702.5	825.2	-14.9%
Italy	299.6	365.2	-18.0%
Germany	317.1	327.8	-3.3%
Romania	30.0	37.5	-20.2%
Greece	36.97	43.593	-15.2%
Total	1898.5	1782.6	6.5%

Source: Company Data

Table 37: Shopping centres market yields per country

	Shopping Centres market yields								
	2008			2009			y.o.y		
	Max	Avg	Min	Max	Avg	Min	Max	Avg	Min
Portugal	7,5%	5,8%	5,4%	8,3%	6,7%	6,0%	0,8pp	0,89pp	0,6pp
Spain	9,4%	6,5%	5,7%	9,1%	7,1%	6,4%	-0,3pp	0,6pp	0,7pp
Italy	7,7%	6,4%	5,8%	7,7%	6,6%	6,0%	0pp	0,27pp	0,2pp
Germany	6,0%	5,9%	5,8%	6,3%	6,1%	6,0%	0,25pp	0,17pp	0,25pp
Greece	7,0%	7,0%	7,0%	7,0%	7,0%	7,0%	0pp	0pp	0pp
Romania	8,0%	8,0%	8,0%	9,0%	9,0%	9,0%	1pp	1pp	1pp
Brazil	9,8%	8,6%	8,3%	9,5%	8,5%	8,30%	0,25pp	0,07pp	0pp

Source: Company Data

⁵¹ Real Estate Market Valuation and Analysis, J. Kahr and M. C. Thomsett, 2005, Willey Finance

⁵² Is not feasible to evaluate given the number of Sierra shopping centers and its competitors per region

⁵³ Funds held with high percentage on real estate usually trade, *ceterus paribus*, at discount (refer to the following footnote)

⁵⁴ Leverage and NAV discount: evidence from Italian real estate, G. Morri and P. Benedetoo, February 2009, Journal of European Real Estate Research Vol. 2 No. 1, 2009 pp. 33-55

⁵⁵ Refer to the previous footnote

⁵⁶ Refer to Financial and Appendixes: Sierra

Closer look at Sierra Brasil

Sonae Sierra Brasil S.A. requested on last March 2nd a registration of a preliminary prospectus for a possible IPO. For that reason and, because it was the only country creating value at *fair value* in 2009 (Table 36), and since it has highest potential growth, we will look more specifically to this business unit.

The opening of Manauara was the highlight last year

Sonae Sierra Brazil is a Joint Venture (JV) with the American company Developers Diversified Realty (DDR). **After the opening of Manauara Shopping (April 2009), the company is currently managing a portfolio of 10 shopping centres, which correspond to 365,900 m2 of GLA.** In the company's expansion plans are three projects under development, two of them will be opened in 2011 (Boulevard Londrina and Uberlândia) and the other one in 2012 (Passeio das Águas).

The JV with DDR and the partnerships with local players like Multiplan, Tivoli EP and Enplanta Engenharia not only add investing capacity (capital) and experience but also dilute the business risk.

With the continuing increase in Brazil's GDP growth, we expect a turnover improvement at a rate above inflation, while vacancy levels are likely to fall.

Under development projects

Sierra Brazil has under development the following projects: Boulevard Londrina Shopping; Uberlândia Shopping; Passeio das Águas Shopping. Boulevard will be built in two phases. The first has a projected GLA of 48,300 m2 (203 stores) and in the second phase will be built 13,000 m2 GLA. The two phases construction also applies to Uberlândia, which offers 37,800 m2 of GLA (201 stores) and, after the second phase, offers an additional 13,300 m2. The other shopping has a projected GLA of 78,100 m2 and will become the 2nd largest centre in Sierra Brazil portfolio.

Operational performance above expected

In 2009 the company has increased the tenant sales by 13.8% and 5.4% like-for-like⁵⁷ YoY. The number of visitants to its shopping were around 92,639 thousand people, which represented an increase of 4.5%. The total rents have also increased by 19.4%⁵⁸. In the beginning of 2009 the company had 195 vacant units, though it was able to do an impressive reduction to 72 (fall 63% YoY).

Having a presence in Brazil means high growth opportunities

While economic revitalization remains a mirage in Europe, Brazil seems to be a very interesting alternative. The Operating margin grew by 24% in 2009 and the outlook seems to be quite favorable, with our model forecasting a turnover growth above inflation.

⁵⁷ SonaeSierra Annual Report 2009

⁵⁸ Valued computed using the company data in Reais

Telecommunications

For further details, please refer to our Company Report – Sonaecom.

Sonaecom valuation was also done using the DCF methodology. Nova Equity Research (NER) upgraded the recommendation by 4.7% from hold to buy, assigning a price target of €1.728 meaning an upside of 25.1% vs the current price. NER, also stressed the possibility of a M&A with Zon, a scenario that if confirmed, increases the price target up to €2.08 which means an upside of 50.1%⁵⁹.

The operational performance of Sonaecom has been an interesting. The full integration of the fixed and mobile businesses enabled important cost control programs which implied higher EBITDA margins.

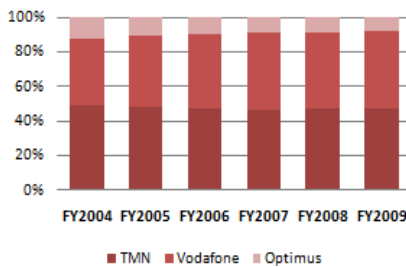
ANACOM's decision regarding the Mobile Termination Rates (MTR) glide path will be published in August. We expect a positive impact to Optimus because the firm it a net payer concerning MTR, achieving 29% in 2016.

Also a **Buy recommendation**

PT: €1.728

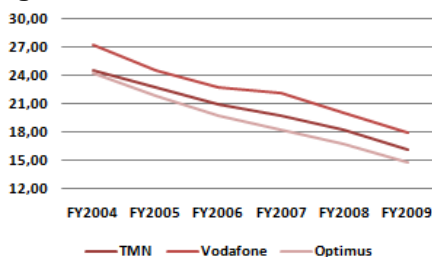
Upside: 25.1%

Figure 17: Market Share Turnover



Source: ANACOM and Nova Equity Research

Figure 18: ARPU



Source: ANACOM and Companies data

Telecommunications market

The industry is characterized by some monopolistic structures (especially PT), partially regulated by ANACOM, and a price war between the three major mobile players TMN with a market share of 42% , Vodafone with 40% and Optimus with 7.5% (Figure 17).

The consumer prefers companies that offer bundles of different communication services and high calling clubs⁶⁰.

The rising number of mobile phone users and technological progress lead to constantly rising demand for telecommunications services. Nevertheless, the time of remarkably rapid growth seems to be coming to an end since the Portuguese telecom market is becoming saturated with market penetration of circa 150%. The mix of high penetration rate and fierce competition has the expected consequence of decreasing the ARPU (Average Revenue Per User) for the 3 operators⁶¹ (Figure 18).

Current situation and outlook

The **number of telecommunications subscribers rose in 2009** but sales stagnated because sales per customer declined. Despite the economic downturn, consumer spending should continue to rise and support demand. However, the sector should barely be able to report further sales growth in 2010 and 2011.

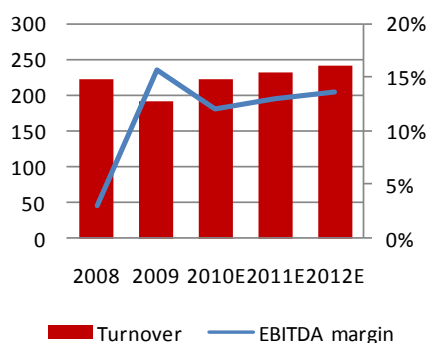
⁵⁹ Sonaecom and Sonae SGPS seem to be favorable to a potential M&A deal

⁶⁰ Customer preferences for bundled content services, Timber Haaker and Henny de Vos, Telematica Instituut

⁶¹ Anacom data and Nova ER

Figure 19: Investment Management

Operational performance



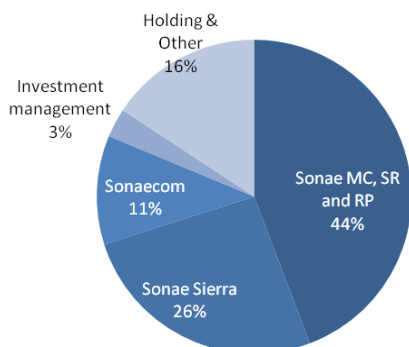
Source: Company data and Analyst Estimate

Investment management (2% of EV)

The portfolio in the Investment management business unit includes a DIY retail unit (Maxmat), travel agencies (GeoStar) and an insurance brokerage business (MDS).

We valued the Investment management at its equity value according to the invested capital at book value minus the net debt. The equity value is 57 million Euros. This unit is consolidated through Sonae Investments.

The investment business unit is also affected by the consumption spending, especially, the travel agency unit. Historically, this business has a seasonal turnover and it is more elastic to consumption than for instance food retail.

Figure 20: Net Debt per Business Unit

Source: Company data and Analyst Estimate

Is Sonae SGPS too levered?

Nowadays leverage has been the main topic among financial analysts, with countries struggling with a high debt burden and low confidence levels among investors. In this type of scenario high levered companies tend to be harshly penalized by the market. The purpose here is to analyze whether or not Sonae is too levered when compared to other Portuguese companies.

In order to proceed with such analysis we have computed the Weighted Average⁶² of some of the most relevant Liquidity and Leverage ratios. We summarize our findings in the Table 38:

Table 38: Sonae SGPS vs. PSI-20 components

	Altri	Brisa	Galp	JMT	Mota Engil	PT	EDP	Zon	Sonae	(PSI-20)
Net Debt/ Equity	389%	233%	51%	62%	608%	234%	140%	418%	190%	132%
D/E	529%	245%	61%	83%	674%	295%	163%	511%	204%	155%
Interest Coverage¹	0,57	1,57	6.01	5.15	1.26	2.3	4.09	3.02	2.84	3.74
Quick ratio²	0,55	0,3	0.32	0.17	0.55	0.85	0.27	0.53	0.19	0.42
Current ratio³	0,79	0,37	0.88	0.42	0.93	1.09	0.57	0.8	0.63	0.82
CFO/Debt	0,15	0,05	0.48	0.62	0.09	0.23	0.31	0.3	0.17	0.3
Market Cap.	409	2.987	9.246	4.475	477	6.33	9.452	1.01	1.494	n.a.

Source: Bloomberg and Analyst estimate

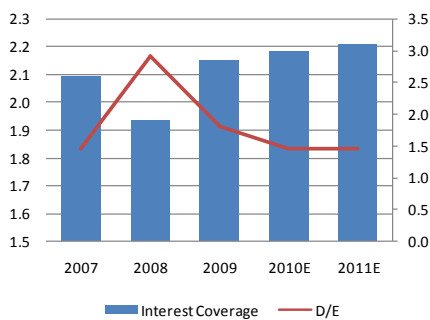
⁶² The weight attributed to each company was based in its current market capitalization

As we can see, Sonae is in fact more levered than the Weighted Average Leverage position of the PSI-20 index. Additionally, we can also observe that its liquidity position is also worst than its other peers, with all the three Liquidity ratios underperforming.

However, if we look at the Debt to Equity ratio and Interest Coverage (**Figure 21**), we realize the company will be able to improve its Leverage and Liquidity position in the following years according to our model.

Caveats when analyzing Sonae's leverage ratios:

Figure 21: Sonae SGPS Interest Coverage and D/E



Source: Company data and Analyst Estimate

The majority of the gross debt is attributable to the Shopping Centers business (represents 26% of the total Net Debt – Figure 20), which is fully and exclusively guaranteed by the specific assets of each single project. Therefore, it is our belief that this fact should be taken into consideration when analyzing Sonae SGPS's Leverage position. Furthermore, ratios such as Net Debt to EBITDA and Interest Coverage are not directly applicable to real estate companies, since the assets behind those projects allow companies to increase their leverage without endangering financial stability and their liquidity. Furthermore, the Total Debt to Total Assets is always below 44%⁶³, meaning that only the 44% of the Total Assets are financed through Debt.

Additional, we highlight that the holding net debt does not have to be refinanced until 2013. There exist refinance to be made in 2011 and 2012 to some business unit. However, it is not relevant for now unless the market deteriorates even further, which in our opinion is quite unlikely. Additionally, Sonae SGPS can always speed up its S&L process through Sonae RP or sell a few shopping malls in order to increase liquidity or reduce Debt.

Conclusion: we agree that Sonae SGPS is highly levered. Nonetheless, the firm was always able to meet its debt obligations and, from our perspective, there are no reasons to believe the opposite.

Highly levered but...

⁶³ Company data and Analyst estimate

Will Carrefour sell Minipreço?

Not an interesting deal for Sonae SGPS given the international expansion plan

The French retailer Carrefour might be planning to sell its stores in Portugal, according to information released by the French and Portuguese press on 7th April. Carrefour has 524 hard discount stores named Minipreço. We recall that Sonae SGPS bought, in 2007, 12 hypermarkets (7 owned and 5 leased), 8 gas stations and 11 licenses (selling area of 77,000 sqm) for an estimated enterprise value of 662 million Euros, leading to a EV/Sales multiple of 1.12x⁶⁴. Minipreço generated last year a turnover of 915 million Euros (-0.9% YoY).

The press refers two potential buyers: Sonae and Jerónimo Martins (JM). Sonae has an estimated market share of 35%⁶⁵ and JM around 23%⁶⁶. **Since the two players have such a large market share the regulatory authorities will hardly accept the operation. Additionally, both companies have aggressive international expansion plans, so it does seem reasonable to strengthen a position in a matured market like.** Other important issues are the stores size, overlapping and cannibalism. Pingo Doce, Modelo and Minipreço are competitors in many places (especially with the first one). In our opinion, if Carrefour wants to sell its stores as a whole it should look for other players, for instance Aldi, Lidl, Auchan or other retail company that might be interested in Portugal. However, we believe for now Carrefour will not find any buyer and it will keep losing market share and EBITDA margins.

In the end what matters is price...

In terms of pricing Carrefour will be willing to sell for a value between 0.41x EV/Turnover (Average ratio in Europe) and 0.51x (Sonae EV/Turnover10E), 375 and 467 million Euros. The market consensus seems to be around 500 million Euros. In our opinion, it is an implicit EV/Turnover too high for a hard discount brand that had a -0.9% YoY Turnover last year.

Finally, in the last company's conference call the company has clearly declared it was not interested in the business, stating the following reasons: (i) only 10% of the portfolio has an interesting sales area (Minipreço stores are too small) and, (ii) Sonae does not see any potential buyer given their poor performance in the retail market.

⁶⁴ We estimate for Sonae MC to 2010 an EV/Sales multiple of 0.5x

⁶⁵ Estimated in the 1Q10 by Nielson and TNS and provided through Company data

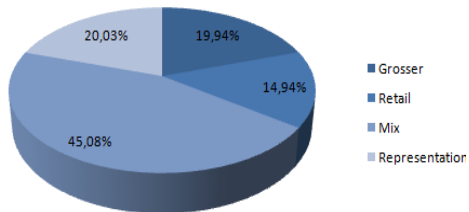
⁶⁶ Estimated in the end of 2009 by Nielson and TNS, excluding Recheio from the analysis

Maybe a high ROIC but high risk for sure

Retail International Investments

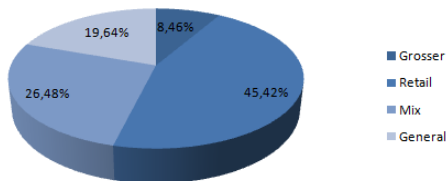
Angola

Figure 22: Big Size Commercial Stores



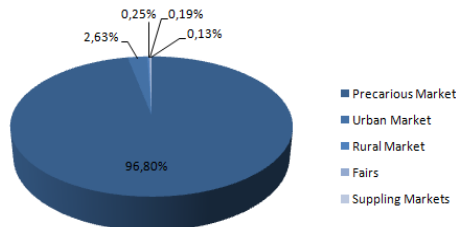
Source: www.dnci.net/abccomercial/estatisticas/

Figure 20: Small & Medium Size Commercial Stores



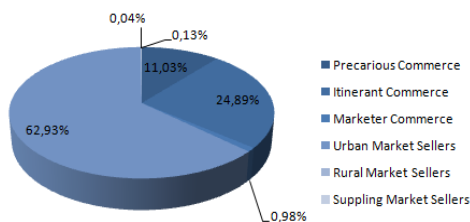
Source: www.dnci.net/abccomercial/estatisticas/

Figure 21: Precarious Commercial Network



Source: www.dnci.net/abccomercial/estatisticas/

Figure 23: Traders & Economic Agents



Source: www.dnci.net/abccomercial/estatisticas/

Both 2009 and 2010 were fertile in news about a potential investment of Sonae MC in Angola⁶⁷. According to Sonae's CEO, Paulo Azevedo, Angola is a very attractive market due to the opportunities to modernize retail, distribution and agriculture⁶⁸. The retail industry in spite of having several players has very few with country wide coverage, NossoSuper is nevertheless the one with higher coverage since it is present in all province capitals, most companies are focused in Luanda. NossoSuper⁶⁹ is integrated in PRESILD, a Governmental initiative whose purpose was to create a distribution hub supported in 4 logistic distribution centers, 31 supermarkets, 26 proximity stores, pedagogic stores and a procurement center⁷⁰. Angola has a tremendous agriculture potential nevertheless the majority of the products distributed have origin abroad namely: Brazil, Portugal, and South Africa. NossoSuper bigger competitors are Shoprite with three stores and Jumbo with one. By analyzing Angola's retail sector, one can conclude that the Luanda, concentrates 48% of the country's commercial establishments. NossoSuper is a "joint venture" between Angola Government and a Brazilian company called Construtora Odebrecht.

In order to be successful in Angola a strategic partnership is almost necessary, thus an agreement has been established between Sonae and Isabel dos Santos, the daughter of Angola's President José Eduardo dos Santos. Although it does not assure success, this partnership is definitely a door opener. The mode of entry is still being studied, after Sonae's experience in Brasil (until 2005) it realized that foreign direct investment (FDI) in retail requires long-term commitment, and it will only be successful if it is desired by all stakeholders. Paulo Azevedo's tenure has already produced changes in the way Sonae foresees entrance modes. At the moment several options are being evaluated specially franchising and joint-ventures or minority interests, has they can be seen has risk mitigating entrance modes versus FDI, moreover the main risks of entering in Angola are the political and exchange rate. Sonae modus operandi settles on the creation of Producers Association to ensure price and quality controls over the products, but also to foster local agriculture, share best practices with local producers and adequate fit between with the distribution chain.

67 http://economico.sapo.pt/noticias/sonae-confirma-interesse-em-angola-em-parceria-com-isabel-dos-santos_81333.html

68 <http://www.briefing.pt/content/view/3356/8/>

69 <http://www.dnci.net/noticias/nacionais/relatorio24NossoSuper.aspx>

70 <http://www.dnci.net/abccomercial/presild/>

Financials & Other Appendices

Sonae SGPS:

Table 39: Sonae SGPS Consolidated Income Statement

Income Statement	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
Turnover	5,353	5,665	5,944	6,375	6,729	7,069	7,306	7,597	7,807	8,013	8,208	8,400	8,590
EBITDA	620	667	694	725	755	771	793	818	838	859	881	903	926
EBIT	332	349	369	381	395	408	418	430	440	450	461	472	484
Net Financials	-174	-123	-123	-123	-123	-123	-123	-123	-123	-123	-123	-123	-123
Others	15	2	2	2	2	2	2	2	2	2	2	2	2
EBT	173	229	249	260	274	287	298	309	319	329	340	351	363
Taxes	-2	-38	-50	-52	-55	-57	-60	-62	-64	-66	-68	-70	-73
Minority Interest	-12	-19	-19	-19	-19	-19	-19	-19	-19	-19	-19	-19	-19
Direct Net Income	159	171	180	188	200	210	219	228	236	244	253	262	271
Indirect Net Income	-79	-77	-61	-45	-21	3	27	43	59	75	91	107	123
Net Income Group Share	80	94	119	143	179	213	246	271	295	319	344	369	394

Source: Analyst Estimate

Table 40: Sonae SGPS Consolidated Balance Sheet

Balance Sheet	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
Fixed Assets	5,871	6,108	6,332	6,637	6,897	7,169	7,465	7,681	7,886	8,161	8,359	8,552	8,742
Inventories	560	603	652	705	747	791	833	854	879	903	926	948	969
Debtors	215	208	221	227	234	240	246	253	260	267	274	281	289
Liquidity	249	231	199	164	259	425	442	643	864	983	1,206	1,458	1,738
Others	411	402	379	369	400	432	445	458	472	486	501	516	531
Current Assets	1,436	1,444	1,451	1,465	1,640	1,888	1,966	2,209	2,475	2,640	2,906	3,203	3,528
Total Assets	7,306	7,552	7,783	8,102	8,537	9,057	9,431	9,889	10,360	10,800	11,265	11,755	12,270
Shareholders	1,151	1,224	1,298	1,370	1,471	1,592	1,708	1,816	1,930	2,035	2,148	2,267	2,392
Minority Interests	412	478	505	535	575	622	667	709	754	795	839	886	935
Total Equity	1,563	1,701	1,803	1,905	2,045	2,214	2,375	2,525	2,683	2,831	2,987	3,152	3,327
Long term (lt) Debt	3,016	2,944	2,920	3,085	3,313	3,587	3,740	3,977	4,226	4,458	4,704	4,965	5,240
Other lt creditors	543	617	641	652	667	683	697	712	718	722	727	732	737
N. current creditors	3,560	3,561	3,561	3,737	3,980	4,270	4,437	4,689	4,944	5,181	5,432	5,697	5,977
Short term Debt	370	314	324	343	368	399	416	442	470	495	523	552	582
Trade creditors	1,050	1,220	1,335	1,360	1,385	1,410	1,435	1,460	1,485	1,510	1,535	1,560	1,585
Others	763	755	759	757	758	763	768	773	778	783	788	793	798
Current creditors	2,184	2,289	2,419	2,461	2,512	2,572	2,619	2,676	2,733	2,789	2,846	2,905	2,966
Total Liabilities	5,744	5,850	5,981	6,198	6,492	6,843	7,057	7,365	7,677	7,970	8,278	8,603	8,943
T. Liabilities + Equity	7,306	7,552	7,783	8,102	8,537	9,057	9,431	9,889	10,360	10,800	11,265	11,755	12,270

Source: Analyst Estimate

Table 39: Sonae SGPS Consolidated Cash Flow Statement

Cash Flow Statement	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
EBITDA	667	694	725	755	771	793	818	838	859	881	903	926
- Change in NWC	-123	93.4	249.7	337.3	368.9	338.6	325.9	365.0	365.9	379.8	395.9	412.2
- Taxes Paid	38	49.7	51.9	54.8	57.4	59.5	61.8	63.8	65.9	68.0	70.3	72.6
Operating Cash Flow	752	551.2	422.9	363.2	345.1	394.9	429.9	409.2	427.5	433.1	437.2	441.3
- Capex	556	548.6	648.7	620.6	635.6	670.7	604.0	603.4	684.1	618.4	624.2	632.5
Cash Flow After Investments	196	2.6	-225.8	-257.4	-290.5	-275.8	-174.1	-194.1	-256.6	-185.3	-187.1	-191.2
- Net Financial Expenses	123	122.8	122.8	122.8	122.8	122.8	122.8	122.8	122.8	122.8	122.8	122.8
- Dividends Paid	60	76.4	92.4	114.4	128.0	164.8	189.7	206.4	239.5	258.0	276.8	295.7
+ Changes in Equity	172	219.7	245.4	319.5	382.4	406.3	421.3	453.4	466.6	500.3	534.5	568.7
Other Items	-92	-42.5	-22.7	17.0	20.5	3.9	3.2	13.5	14.4	14.5	15.0	15.5
Change in Loans	-129	-12.8	183.5	253.3	304.2	169.9	262.9	277.3	257.7	273.5	289.5	305.3
Initial Net Debt	3138	3026.3	3045.7	3264.0	3422.1	3560.5	3713.6	3775.7	3832.2	3970.2	4021.5	4058.6
Change in Net Debt	-111	19.3	218.3	158.1	138.4	153.1	62.1	56.5	138.0	51.3	37.1	25.5
Ending Net Debt	3026	3045.7	3264.0	3422.1	3560.5	3713.6	3775.7	3832.2	3970.2	4021.5	4058.6	4084.0

Source: Analyst Estimate

Table 40: Financial Data per Business Unit

Turnover	2007	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
Sonae MC	2,391	2,930	3,106	3,289	3,489	3,682	3,889	4,036	4,176	4,319	4,461	4,604	4,748	4,893
Sonae SR	765	928	1,132	1,198	1,406	1,531	1,669	1,727	1,850	1,889	1,920	1,937	1,951	1,959
Sonae RP	92	109	123	119	117	120	122	126	130	136	143	152	161	172
Sonae Sierra	140	158	156	160	164	168	168	171	174	176	178	180	182	184
Sonaeacom	893	976	949	968	988	1,008	1,028	1,048	1,069	1,091	1,112	1,135	1,157	1,180
Inv. Man.	204	221	192	222	231	241	216	222	220	219	219	220	220	220
Petrol stations	0	151	133	126	123	124	126	129	132	134	137	140	143	145
El. & Adj.	-103	-121	-127	-139	-142	-144	-150	-152	-154	-156	-158	-160	-162	-164
Sonae	4,382	5,353	5,665	5,944	6,375	6,729	7,069	7,306	7,597	7,807	8,013	8,208	8,400	8,590

EBITDA	2007	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
Sonae MC	141	187	199	210	224	237	251	261	271	279	287	295	302	310
Sonae SR	53	52	48	67	81	90	100	106	116	121	125	129	132	135
Sonae RP	95	110	111	112	108	109	112	115	118	123	129	137	145	155
Sonae Sierra	77	90	90	90	91	92	93	94	94	94	95	95	96	96
Sonaeacom	162	160	176	179	183	186	188	190	192	194	196	198	200	202
Inv. Man.	13	7	30	27	30	33	18	19	19	18	18	19	19	19
El. & Adj.	-4	14	13	8	8	8	9	9	9	9	9	9	9	10
Sonae	536	620	667	694	725	755	771	793	818	838	859	881	903	926

EBIT	2007	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
Sonae MC	96	124	124	131	137	143	149	153	156	157	159	160	162	163
Sonae SR	34	28	10	30	37	43	49	52	59	62	66	69	72	75
Sonae RP	74	88	83	84	81	82	84	86	88	92	96	102	109	116
Sonae Sierra	77	89	89	89	90	91	92	93	93	93	94	94	94	95
Sonaeacom	22	3	24	24	25	25	26	26	26	26	27	27	27	27
Inv. Man.	9	1	25	19	19	20	18	19	19	18	18	19	19	19
El. & Adj.	-15	0	-5	-9	-9	-9	-9	-10	-10	-10	-10	-10	-10	-10
Sonae	298	332	349	369	381	395	408	418	430	440	450	461	472	484

Source: Company Data and Analyst Estimation

Sonae MC, SR, RP and Investment Management Consolidated through Sonae Investimentos

Table 41: Balance Sheet

YEAR	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
Tangible assets	1924.3	2198.5	2288.5	2494.9	2673.2	2833.2	2975.7	3108.5	3229.5	3346.5	3453.6	3551.5	3642.1
Goodwill	521.0	519.9	521.0	521.0	521.0	521.0	521.0	521.0	521.0	521.0	521.0	521.0	521.0
Intangible assets	164.3	162.4	195.4	213.0	228.2	241.9	254.1	265.4	275.7	285.7	294.9	303.2	310.9
Investments in associated companies	64.7	2.4	2.4	2.4	2.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Others financial investments	2.4	0.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Deferred tax assets	67.4	90.5	93.5	101.5	107.9	114.5	118.7	124.0	127.7	131.3	134.7	138.0	141.3
Other Non-Current Assets	2.3	4.3	4.5	4.9	5.2	5.5	5.7	5.9	6.1	6.3	6.5	6.6	6.8
Total Non-Current Assets	2,746.4	2,978.7	3,105.3	3,337.6	3,535.6	3,716.0	3,875.1	4,024.9	4,160.1	4,290.8	4,410.6	4,520.4	4,622.1
Inventories	530.8	589.0	622.0	675.1	717.8	761.4	789.5	824.9	849.5	873.4	895.9	918.0	939.8
Account receivables and other CA	209.9	226.1	232.5	252.3	268.3	284.6	295.0	308.3	317.5	326.4	334.8	343.1	351.2
Other financial investments	62.8	57.7	59.6	64.7	68.8	73.0	75.6	79.0	81.4	83.7	85.8	88.0	90.0
Cash and cash equivalents	115.3	110.8	321.3	364.3	424.9	450.1	484.5	543.8	582.8	603.2	608.2	627.9	660.0
Total Current Assets	918.9	983.5	1,235.4	1,356.4	1,479.8	1,569.1	1,644.7	1,756.0	1,831.2	1,886.7	1,924.8	1,977.0	2,041.0
Non current assets held for sale	5.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
TOTAL ASSETS	3,671.1	3,962.2	4,340.7	4,694.0	5,015.4	5,285.1	5,519.8	5,780.9	5,991.3	6,177.5	6,335.3	6,497.4	6,663.1
Share capital	1000	1000	1000	1000	1000	1000	1000	1000	1000	1000	1000	1000	1000
Own Shares	0	0	0	0	0	0	0	0	0	0	0	0	0
Reserves and retained earnings	-251	-164	-62	33	123	200	269	341	403	454	494	535	578
Net Profit to the shareholders	171	136	207	215	226	225	234	245	254	264	275	287	299
Total equity to the shareholders	920	972	1144	1248	1348	1426	1504	1586	1657	1719	1769	1822	1877
Minority interests	11	74	74	74	74	74	74	74	74	74	74	74	74
TOTAL EQUITY	932	1046	1219	1322	1423	1500	1578	1660	1732	1793	1844	1897	1952
Loans	1243	1282	1401	1520	1636	1725	1815	1909	1991	2062	2120	2181	2244
Other non-current liabilities	12	16	12	12	12	12	12	12	12	12	12	12	12
Deferred tax liabilities	81	97	97	97	97	97	97	97	97	97	97	97	97
Provisions	13	9	9	9	9	9	9	9	9	9	9	9	9
Total non current liabilities	1349	1404	1519	1638	1754	1843	1932	2027	2109	2180	2238	2299	2362
Loans	153	104	122	132	142	150	158	166	173	179	184	190	195
Suppliers and other CL	1235	1405	1479	1599	1694	1790	1849	1925	1975	2023	2067	2110	2152
Provisions	2	2	2	2	2	2	2	2	2	2	2	2	2
Total current liabilities	1391	1512	1603	1734	1839	1943	2009	2093	2151	2205	2254	2302	2349
TOTAL Liabilities	2740	2916	3122	3372	3593	3785	3942	4120	4260	4384	4492	4601	4712
Total Equity + Liabilities	3671	3962	4341	4694	5015	5285	5520	5781	5991	6177	6335	6497	6663

Source: Analyst Estimation

Table 43: Income Statement

YEAR	2008	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
Sales	4220	4560	4714	5116	5440	5770	5983	6251	6438	6619	6789	6957	7122
EBITDA	366	359	425	451	477	490	509	532	550	569	588	608	628
D&A	-126	-141	-154	-167	-178	-189	-196	-205	-211	-217	-222	-228	-233
EBIT	240	218	271	283	299	301	313	327	339	352	366	380	395
Net Financial Income (expense)	-72	-58	-51	-55	-59	-63	-65	-68	-70	-72	-74	-75	-77
Profit (Loss) related to ass. Comp.	13	-1	0	0	0	0	0	0	0	0	0	0	0
Profit (Loss) related to investments	1	2	5	5	5	6	6	6	6	6	7	7	7
EBT	182	161	224	233	245	244	254	265	276	287	299	311	325
Income Taxes	-11	-24	-16	-16	-17	-17	-18	-19	-19	-20	-21	-22	-23
Net Income	171	137	208	216	228	227	236	247	256	266	278	289	302
Attributable to:													
Equity holders of the Parent Company	171	136	207	215	226	225	234	245	254	264	275	287	299
Minority interests	0	1	2	2	2	2	2	2	2	2	2	2	2

Source: Analyst Estimation

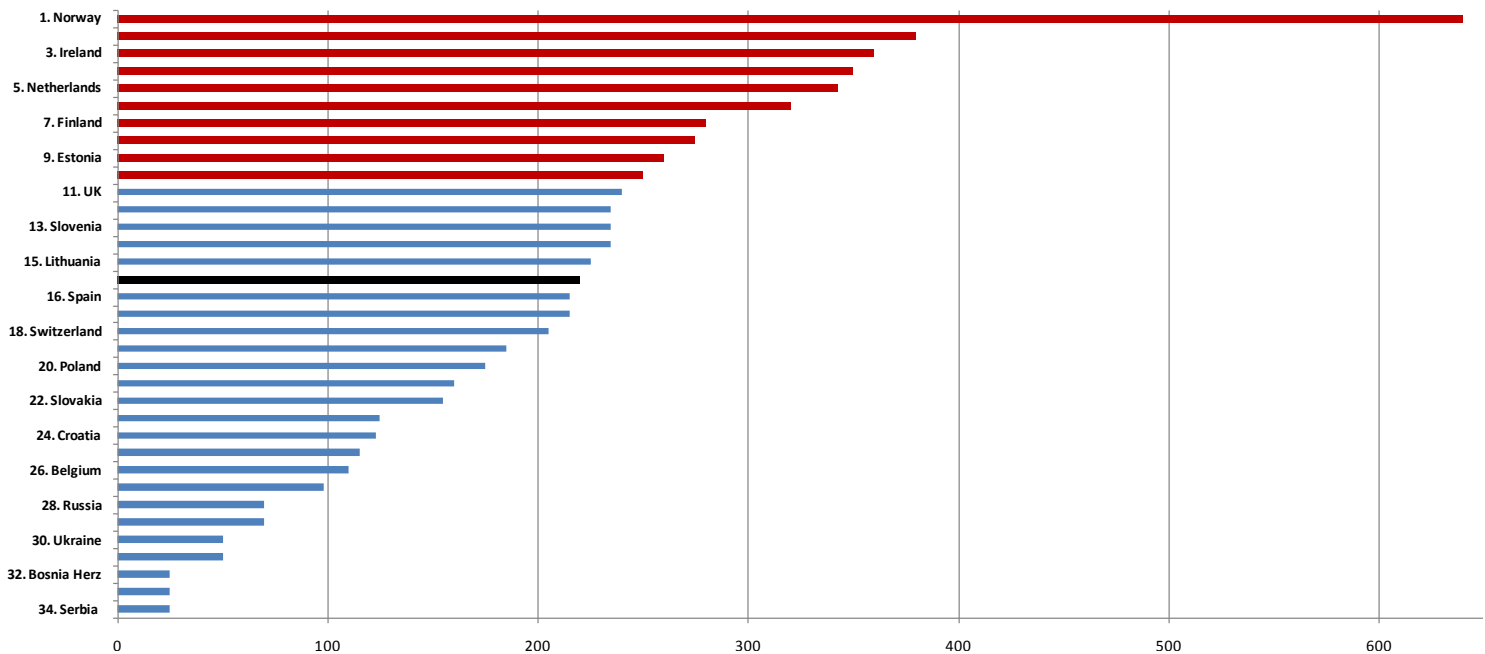
Table 42: Cash Flow Statement

YEAR	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	2020E
EBIT	218.1	270.7	283.2	298.7	301.4	313.3	327.1	339.0	351.9	365.6	380.0	394.9
+ Depreciation	141.2	154.3	167.5	178.1	188.9	195.9	204.6	210.7	216.7	222.3	227.7	233.1
- Change in NWC	-95.6	-34.0	-47.4	-36.2	-36.3	-20.5	-27.1	-16.2	-15.1	-13.4	-12.6	-11.9
- Taxes Paid	24.3	15.9	16.5	17.3	17.3	18.0	18.8	19.5	20.3	21.1	22.0	23.0
Operating Cash Flow	430.6	443.2	481.7	495.7	509.3	511.6	540.0	546.5	563.4	580.1	598.4	617.0
- Capex	412.4	278.4	391.4	371.7	362.5	350.5	348.8	342.1	343.6	338.5	334.1	331.4
- Net Financial Investments	-69.0	1.2	5.1	1.7	4.2	2.7	3.4	2.4	2.3	2.2	2.1	2.1
Cash Flow After Investments	87.2	163.5	85.1	122.3	142.6	158.4	187.8	202.0	217.6	239.4	262.2	283.4
- Net Financial Expenses	58.0	51.1	55.5	59.0	62.5	64.9	67.8	69.8	71.7	73.6	75.4	77.2
- Dividends Paid	85.4	104.2	119.0	136.7	147.7	165.4	172.7	192.0	213.1	235.9	246.0	256.4
+ Changes in Equity	63.2	68.4	6.2	9.6	-2.4	7.2	8.4	7.2	8.2	8.9	9.5	9.9
Other Items	-1.5	-3.5	-3.4	-1.4	-1.2	1.4	0.5	2.4	2.7	3.1	3.3	3.5
Change in Loans	-10.1	137.3	129.4	125.8	96.4	97.6	103.0	89.1	76.8	63.1	66.1	68.9
Initial Cash	115.3	110.8	321.3	364.3	424.9	450.1	484.5	543.8	582.8	603.2	608.2	627.9
Change in Cash	-4.5	210.5	42.9	60.7	25.2	34.4	59.3	38.9	20.4	5.0	19.7	32.1
Ending Cash	110.8	321.3	364.3	424.9	450.1	484.5	543.8	582.8	603.2	608.2	627.9	660.0

Source: Analyst Estimation

Sonae Sierra

Figure 24: European Shopping Centre GLA (sqm) per 1.000 Population (equal to Figure 15/Same Source)



Sonae Sierra

Table 44: Fair Value of the investment properties (€million)

	31.12.09				31.12.08				Change in		
	% of consolidation	10 yr discount rate	Exit Yield	Amount	% of consolidation	10 yr discount rate	Exit Yield	Amount	10 yr discount rate (bp)	Change in Exit Yield	Change in Amount
Portugal:				1,451.12				1,577.74			-8.0%
AlgarveShopping	100%	8.60%	6.35%	133.8	100%	7.90%	5.65%	149.1	0.7	0.7	-10.3%
ArrábidaShopping	50%	9.05%	6.80%	82.6	50%	8.25%	6.00%	90.5	0.8	0.8	-8.7%
CascaShopping	50%	8.50%	6.25%	160.2	50%	7.75%	5.50%	175.9	0.8	0.8	-8.9%
Centro Colombo	50%	8.35%	6.10%	364.3	50%	7.75%	5.50%	396.9	0.6	0.6	-8.2%
Centro Vasco da Gama	50%	8.25%	6.00%	148.7	50%	7.30%	5.40%	157.6	1.0	0.6	-5.7%
CoimbraShopping	100%	10.55%	8.30%	22.6	100%	9.35%	7.10%	25.3	1.2	1.2	-10.9%
Estação Viana	100%	9.50%	7.25%	72.7	100%	8.75%	6.50%	82.5	0.8	0.7	-11.9%
GaiaShopping	50%	9.05%	6.80%	75.3	50%	8.20%	5.95%	87.3	0.8	0.9	-13.7%
GuimarãesShopping	100%	9.40%	7.15%	56.6	100%	8.80%	6.55%	46.7	0.6	0.6	21.3%
MadeiraShopping	50%	9.80%	7.55%	36.2	50%	9.15%	6.90%	37.7	0.7	0.6	-4.1%
MaiaShopping	100%	10.00%	7.75%	48.2	100%	9.10%	6.85%	54.7	0.9	0.9	-11.9%
NorteShopping	50%	8.30%	6.05%	188.1	50%	7.70%	5.45%	203.1	0.6	0.6	-7.4%
Parque Atlântico	50%	9.90%	7.65%	32.0	50%	9.15%	6.90%	34.4	0.8	0.7	-7.0%
Torre Colombo Ocidente	25%	9.50%	7.25%	1.7	25%	9.75%	7.50%	1.7	-0.3	-0.3	-0.4%
Torre Colombo Oriente	0%	0.00%	0.00%		25%	9.75%	7.50%	1.8	-	-	-
ViaCatarina	50%	9.75%	7.50%	28.3	50%	8.95%	6.70%	32.5	0.8	0.8	-13.0%
Brazil:				360.6				183.3			96.7%
Parque D. Pedro	50%	12.75%	8.25%	165.7	50%	13.45%	8.25%	108.068	-0.7	0.0	53.4%
Pátio Boavista	50%	14.00%	9.50%	13.1	50%	14.95%	9.75%	9.639	-0.9	-0.3	36.1%
Manauara Shopping	50%	13.00%	8.50%	73.2	-	-	-	-	-	-	-
Shopping Metrópole (*)	50%	13.00%	8.50%	47.0	50%	13.70%	8.50%	26.374	-0.7	0.0	78.3%
Shopping Penha (73,18%)	50%	13.50%	9.00%	25.7	50%	14.45%	9.25%	15.851	-0.9	-0.3	62.1%
Shopping Plaza Sul (30%)	50%	12.75%	8.25%	16.6	50%	13.70%	8.50%	11.747	-1.0	-0.3	41.3%
Sierra Enplanta	50%	-	-	19.2	50%	-	-	11.652	-	-	64.7%
Spain:				702.5				825.2			-14.9%
Avenida M40	100%	-	-	-	100%	12.35%	9.35%	30.7	-	-	-
Dos Mares	100%	9.55%	7.05%	48.8	100%	9.25%	6.25%	54.1	0.3	0.8	-9.9%
El Rosal	100%	10.40%	7.90%	89.9	100%	9.90%	6.90%	110.9	0.5	1.0	-19.0%
Grancasa	50%	8.90%	6.40%	79.6	50%	8.70%	5.70%	94.5	0.2	0.7	-15.8%
Max Center	50%	9.25%	6.75%	72.3	50%	8.75%	5.75%	83.2	0.5	1.0	-13.1%
La Farga	50%	11.40%	8.90%	22.0	50%	10.40%	7.40%	27.6	1.0	1.5	-20.3%
Luz del Tajo	100%	9.10%	6.60%	92.4	100%	9.35%	6.35%	96.8	-0.3	0.3	-4.5%
Plaza Éboli	100%	11.10%	8.60%	35.3	100%	10.60%	7.60%	46.4	0.5	1.0	-23.9%
Plaza Mayor	100%	11.55%	9.05%	53.2	100%	11.80%	8.80%	58.0	-0.2	0.3	-8.2%
Plaza Mayor Shopping	100%	9.25%	6.75%	64.1	100%	9.60%	6.60%	63.6	-0.4	0.2	0.8%
Parque Principado	50%	9.25%	6.75%	77.7	50%	9.20%	6.20%	85.0	0.1	0.6	-8.6%
Valle Real	50%	9.10%	6.60%	45.8	50%	9.10%	6.10%	49.0	0.0	0.5	-6.5%
Zubiarte	50%	11.20%	8.70%	21.5	50%	11.00%	8.00%	25.4	0.2	0.7	-15.3%
Italy:				299.6				365.2			-18.0%
Airone	100%	9.00%	7.70%	15.2	100%	8.70%	7.70%	17.8	0.3	0.0	-14.4%
Valecenter/Warner Village	100%	8.00%	6.90%	133.9	100%	8.00%	6.90%	147.3	0.0	0.0	-9.1%
Freccia Rossa	50%	8.10%	6.00%	68.4	50%	8.10%	5.80%	76.4	0.0	0.2	-10.5%
Gli Orsi	100%	9.50%	7.00%	82.1	100%	8.50%	6.20%	123.7	1.0	0.8	-33.6%
Germany:				468.9				327.8			
Alexa	50%	6.50%	6.00%	158.1	50%	6.50%	6.00%	171.5	0.0	0.0	-7.8%
Loop 5	50%	6.75%	6.25%	151.8	-	-	-	-	-	-	-
Münster Arkaden	100%	6.50%	6.00%	159.0	100%	6.50%	5.75%	156.3	0.0	0.3	1.7%
Romania:				30.0				37.5			-20.2%
River Plaza Mall	100%	10.75%	9.00%	30.0	100%	9.75%	8.00%	37.5	1.0	1.0	-20.2%
Greece:				37.0				43.6			-15.2%
Pantheon Plaza	50%	10.75%	7.00%	37.0	50%	10.75%	7.00%	43.6	0.0	0.0	-15.2%
Total				1,898.5				1,782.6			6.5%

Source: Company Data

Why a Holding discount?

A holding discount of 10% was applied for two reasons. Firstly, Sonae SGPS has a large stake in an unrelated business to its core, Sonaecom. There exists empiric evidence that the distance to core business might towards down the firm value. Cláudia Custódio (2008) found that “increasing non-core business sales weight by 10% decreases firm value up to 3%”⁷¹. From this study is possible to understand that unrelated to core businesses typically do not add value. If we think specifically about Sonae SGPS which SGPS claims to be a Retail company but, at the same time, has a 53% stake in Sonaecom (that is also a member of PSI-20). The portfolio theory teaches us that any investor can easily diversify its portfolio at a lower cost. We used Cláudia Custódio (2008) numbers to compute the worst scenario to Sonae SGPS and for a conservative reason we have used in our holding discount.

The second reason is the additional costs to maintain this structure while it is not clear the benefits. The 7.5% holding discount includes the holding costs. In our discount we include the holding costs. The following table summarizes how the holding discount is divided:

Table 45: Breakdown Holding discount

Holding Discount	7.5%	0.09 €
Holding Costs	2.70%	0.03 €
Sonaecom	4.80%	0.06 €

Source: Analyst Estimation

The 4.8% discount was computed assuming that 10% turnover of unrelated business decreases the company’s value by 3%. Sonaecom has 16% of the overall turnover. Thus, we got the 4.8% by multiplying Sonaecom’s Turnover by 3% divided by 10%, meaning a 4.8% discount.

We estimate Holding costs for 2010 of 73 million Euros. Therefore, we divided that number by the Equity Value and we got the 2.7%, which represents €3 per share.

⁷¹ “Core-business Expertise, Managerial Discretion and Corporate Diversification”, 2008, Cláudia Custódio, FMG-London School of Economics

Valuation Summary

We valued Sonae MC, Sonae SR and Sonae RP with the Discounted Cash Flow approach. Thus, to discount the FCF we have computed the WACC for each business:

$$WACC = \frac{E}{D + E} \times R_e + \frac{D}{D + E} \times \text{Cost of Debt} \times (1 - T_c)$$

Betas

For each business we looked for comparable companies⁷² and then we compute the levered beta:

$$\text{Beta}_i = \text{Cov}(R_i; R_{\text{Market}}) / \text{Var}(\sigma_{\text{Market}})$$

Then, we compute the Unlevered Beta of each company:

$$\beta_{\text{unlevered}} = \frac{\beta_{\text{levered}}}{1 + \frac{D}{E} \times (1 - T_c)} \quad 73$$

The next step was to compute the Beta levered to our company given the D/E and tax rate:

$$\beta_{\text{levered}} = \beta_{\text{unlevered}} \times \left(1 + \frac{D}{E} \times (1 - T_c)\right)$$

After that we compute the return on equity:

$$R_e = R_f + \beta_{\text{levered}} \times (\text{Market Risk Premium})$$

Other assumptions and calculations:

Risk-free: 10-year German Sovereign Bond

Market Risk Premium:

$$\text{Market Premium} = \text{CDS spread} \times \frac{\text{Equity Index Volatility}}{\text{Bond Holding Returns Volatility}}$$

We had a slightly more conservative approach in our previous research therefore we have fine-tuned our approach and assumptions.

Currently, the market risk premium to Portugal is high. The CDS spreads have increased dramatically as we have shown in our macroeconomic analysis and, therefore, even if an investor does not believe in the Portuguese default, he requires a higher return given the higher risk he is incurring. Thus, we computed the country risk premium using the 10 year CDS adjusted for volatilities of the Equity Index (PSI-20) and the Portuguese's 10 year bonds.

⁷² To Sonae SR we attribute a weight to the average of the sector given the turnover per segment (Clothing, Sports and Electronics)

⁷³ We have assumed Beta of debt equal to zero

Disclosures and Disclaimer

Research Recommendations

Buy	Expected total return (including dividends) of more than 15% over a 12-month period.
Hold	Expected total return (including dividends) between 0% and 15% over a 12-month period.
Sell	Expected negative total return (including dividends) over a 12-month period.

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