GONZALEZ-SANEL RESEARCH

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United States

Building Materials Industry

12 Month Rating	**BUY**
	Initiating Coverage
12 Month price target	US$ 42.08
	Prior: -
Current Price	US$ 36.75
Ticker: VMC US	

October 26, 2010

Vulcan Materials Company

We are issuing a buy rating on Vulcan Materials Co. (NYSE: VMC) and we believe **the market is undervaluing the stock price**. After analysis we feel that **the fair 12 month target price is US$42.08 per share**. We believe in the short term the stock price will continue to be undervalued until the market regains confidence on the building materials industry. We put significant emphasis on Vulcan's risk factors in our analysis and we remain bullish on the stock.

We believe that federal spending will remain constant and that the current stimulus will fade in 2012. The state and local spending issue is more complex. As most states (including Vulcan's main states of California and Florida) are dealing with budget concerns, **there could be a decrease in state infrastructure spending going forward**. According to The Fiscal Survey of States, 21 states will make or have made fiscal program cuts in transportation for 2010.

The private sector continues to stumble, only showing a slight uptick in **overall** construction values since the beginning of the year. **Our conclusion here is that VMC is highly dependent on public spending.** We expect this dependency will only increase if private construction weakens. **In terms of risk factors, a delay in stimulus or ongoing state fiscal troubles could have a significantly negative impact on Vulcan's sales.**

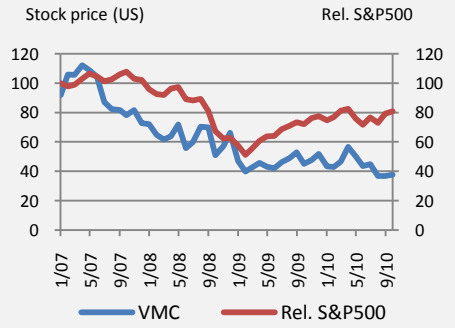
One final concern is the extended price softening on all of VMC's product lines. We believe that the main reason prices remained so elevated in the past involved the government as a major buyer in the market. As demand has fallen, firms have become much more competitive in both the public and private sectors. This delay or stickiness in pricing, along with continuing weak private sector demand, may indicate a lower price hangover for the next several quarters. With this in mind, **we do not expect prices to increase significantly until the private sector assumes a recovery.**

Our analysis factored in all risk factors above. **While these risks should cause concern, we believe the market is currently too pessimistic in regard to VMC's stock price.**

Key Financial Data

Market Cap	US$4.71 B
52 wk range	US$35.61 – 59.90
Volume	1,676,450
Enterprise Value	US$7.44B
Price/Sales	1.82
Price/Book	1.17
EV/Revenues	2.87
EV/EBITDA	18.45
Total Debt	2.75B
Total Cash	46.08M
Shares o/s	128.27M

Stock Performance



Quarterly EPS

	1Q	2Q	3Q	4Q
2009A	($0.29)	$0.14	$0.38	($0.10)
2010E	($0.35)A	($0.18)A	$0.07E	($0.03)E

Please read the disclaimer at the end of this report for important information

Company Description

Vulcan Materials Company ("VMC"), incorporated on February 14, 2007, produces construction materials in the United States and Mexico. The company is headquartered in Birmingham, Alabama. The company's major markets include Birmingham, Atlanta, Chicago, Charlotte, Houston, San Diego, and Los Angeles, and its Yucatan peninsula also ships materials to the southeast US. VMC produces four types of building materials: Aggregates, Asphalt mix, Concrete, and Cement, and its operations are divided into three segments.

Aggregates Segment

VMC transports aggregates from Mexico to the United States principally on its Panamax-class, self-unloading ships. As of December 31, 2009, VMC had 14.2 billion tons of permitted and proven or probable reserves. Additionally, the Company sells ballast to railroads for construction and maintenance of railroad track. It also sells riprap and jetty stone for erosion control along waterways. It has operating facilities across the United States and in Mexico and the Bahamas.

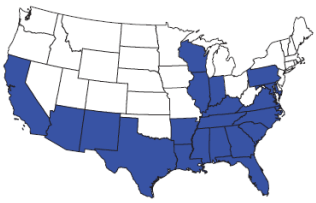
Asphalt Mix and Concrete Segment

Produces and sells asphalt mix and ready-mixed concrete primarily in its mid-Atlantic, Florida, southwestern and western markets. Additionally, it produces and sells in a limited number of these markets other concrete products, such as block, pre-stressed and pre-cast beams, and resells purchased building materials for use with ready-mixed concrete and concrete block. Customers for its asphalt mix and concrete segment are served locally from its production facilities or by truck.

Cement Segment

Cement operations were acquired in the Florida Rock transaction ($4.6B) completed in November 16, 2007. The Company's Newberry, Florida cement plant produces Portland and masonry cement that it sells in both bulk form and bags to the concrete products industry. Its Tampa, Florida facility imports and exports cement and slag. Some of the imported cement is resold, and the balance of the cement is blended, bagged, or reprocessed into specialty cements that are then sold. The slag is ground and sold in blended or unblended form. Its Port Manatee, Florida facility imports cement clinker that is ground into bulk cement and sold. The Company's Brooksville, Florida plant produces calcium products for the animal feed, paint, plastics and joint compound industries.

Exhibit 1
Vulcan Materials U.S. Geographic Footprint



Source: Vulcan Materials Company

Key Insight news

VMC: Understanding the Key Drivers. We believe there are 4 main forces that affect VMC: federal spending (non-stimulus), state and local spending, federal stimulus and the private sector. We think that annual federal spending will either stay constant or see a slight uptick. Additionally, we consider that federal stimulus and private sector growth are, for the most part, mutually exclusive. That is, if there is no private sector growth, we may see a stimulus package. However, if private sector growth increases, we will most likely not see a stimulus. The state and local spending issue is more complex; as most states (including Vulcan's main states of California and Florida) are dealing with budget concerns, we might expect a decrease in state infrastructure spending; this decrease may accelerate if federal stimulus packages are extended where there are no matching state fund provisions.1

Conflicting Information. For the first time since 2002, VMC reported that public spending accounted for 50% of all aggregate shipments. We believe, however, that this number should be much higher. The public infrastructure spending budget has remained fairly constant for over the last 5 years and with the introduction of federal stimulus since 2009, we would expect to see a greater current sales contribution to VMC. Yet, when we use these values we see that public spending fell in 2009, which defies the percentages we are given by VMC. One way to explain this might be an increase in federal spending but an overall slowdown in state spending.2

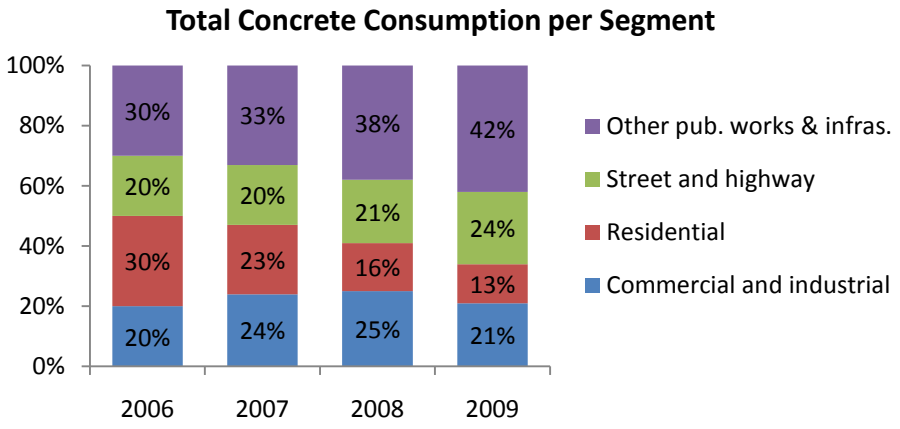
	2005	2006	2007	2008	2009
$ Aggregates	$ 2,107.00	$ 2,405.00	$ 2,445.00	$ 2,404.00	$ 1,838.00
% Public	44%	44%	47%	45%	**50%**
$ Public Spending	$ 927.08	$ 1,058.20	$ 1,149.15	$ 1,081.80	$ 919.00
At least 2008					$ 1,081.80
Public Spending					**59%**

As show above, public spending should have been greater than the last five years because the budget has remained constant and there was additional stimulus. By our valuation, either VMC's dependence on public spending is greater than 59% (with state and federal spending kept constant) or overall state

[1] American Recovery and Reinvestment Act of 2009 (ARRA) Action Plans: http://www.georgia.gov/vgn/images/portal/cit_1210/60/13/144564719DOT%20Action%20Plan-%206.18.09.pdf
[2] If there were a contraction in state and local spending in 2009, it may explain VMC's actual Q2 2010 Earnings Call in which Daniel Sansone states "Total state and local awards are up 11% that excludes all federal activity."

and local spending fell by 15% (while federal was kept constant). However, state and local construction value in 2008 was $80.4 and in 2009 was $81 billion[3]—so state and local spending could not have fallen so drastically. **Our conclusion is that VMC is highly dependent on public spending. We expect this dependency will only increase if private construction weakens. More concerning, a delay in stimulus or state fiscal troubles could be devastating to the firm.** For comparison, the concrete industry, which accounts for the majority of the aggregates consumption, averages around 66% of public spending; this further increases the peculiarity of VMC's low 50% public spend value.

Exhibit 2
Concrete Consumption per Segment in the United States



Source: Vulcan Materials Company, Company Estimates 2010e

VMC has changed their data display in the 2009 report making private vs. federal vs. state inferences much more difficult:

Amounts in millions	2009	2008	2007	2006	2005
Average Unit Sales Price					
Aggregates (freight-adjusted)**	$10.30	$9.98	$9.35	$8.29	$7.23
Asphalt mix	$52.66	$55.16	$48.47	$43.12	$31.76
Ready-mixed concrete	$96.53	$97.75	$95.56	$90.14	$77.80
Aggregates Sales Volume by End Use (estimated)					
Highways	27%	25%	25%	23%	23%
Other nonbuilding infrastructure	15%	13%	11%	10%	10%
Residential buildings	16%	17%	19%	25%	26%
Nonresidential buildings	37%	42%	42%	39%	38%
Nonconstruction	5%	3%	3%	3%	3%
Total	100%	100%	100%	100%	100%
Using public funds	50%	45%	47%	44%	44%
Using private funds	50%	55%	53%	56%	56%
Total	100%	100%	100%	100%	100%

*Source: VMC 2009 Annual Report (**hard to understand what's private vs. public**)

[3] US Census Data http://www.census.gov/const/C30/s&l2009.pdf

Amounts in millions	2005	2004	2003	2002	2001
Aggregates Sales Volume by End Use (estimated)					
Public construction:					
Highways, streets and airports	**23%**	23%	25%	31%	33%
Other public works	**10%**	10%	9%	10%	8%
Government buildings	**11%**	11%	11%	11%	10%
Public subtotal	**44%**	44%	45%	52%	51%
Private construction:					
Residential buildings	**26%**	26%	26%	21%	20%
Private nonresidential buildings	**27%**	27%	25%	23%	25%
Railroads	**1%**	1%	2%	2%	1%
Private nonconstruction:					
Agricultural, chemical and industrial	**2%**	2%	2%	2%	3%
Private subtotal	**56%**	56%	55%	48%	49%
	100%	100%	100%	100%	100%

*Source: VMC 2005 Annual Report (**easy to understand what's private vs. public**)

Another strange comment was made by VMC's CFO Daniel Sansone when asked about state vs. federal funding:

> **Ted Grace (Analyst):** Don, you've kind of reached out kind of outlining your expectations on the federal highway side and then you've obviously been quite clear in your views on non-res. I guess as we think about total, call it road and highway demand, about 40% of total aggregates go to that channel. And as we think about it, about half of that funding comes from the federal government; about half comes from states. And if you look at the spending trends to-date, and it's really every month this year and it even goes back into last year, the numbers have been kind of flat to up on a total reported basis if you look at road and highway construction as the Census Bureau reports it. **If you back out the spending from stimulus, it would suggest that the underlying spending is down substantially.** Year-to-date, call it the underlying spend, is probably 15%. **Now, we know that the federal dollars have been constant because of the extension.** And so, one read on this is that states are under a lot more pressure than the market may be where – and it's something that the industry hasn't really addressed. **So, my question, my first question is, could you speak to your view on the state situation as opposed to the federal highway situation, because it's obviously a huge component of overall road and highway demand for aggregates, and how you're thinking about where we are now, how that trends in the second half of this year and given the budgetary pressures there under – how that looks for 2011?**
>
> ….
>
> **Daniel Sansone (CFO):** Let me give there is a couple of total numbers we'd been able to pull up, if you look at the total state and local awards year-to-date, and this is through – this is through June 30th, so it's the first half of this year compared to the first half of last year. **Total state and local awards are up 11%, that excludes all the federal activity.** The state only awards – state Department of Transportation awards are actually up in the high teens and these are in Vulcan-served states that I'm citing and the local awards are down 4 or 5 or 6% and when you put the state and local together, you're up 11%, first half of this year versus first half last year.

It is not clear how "awards" translates into shipments or sales. However, looking at census data, the seasonally adjusted value of state and local highway construction in Year-to-June actually went down. In

Year-to-June 2009, the value was $81 billion; in Year-to-June 2010 the value was $80.9 billion—a slight decrease.[4]

No Future Stimulus Guarantee. The possibility of future government spending and/or stimulus is uncertain. To quote Keith Hughes of Suntrust Robinson Humphrey:

> SAFETEA-LU, the previous 6-year highway bill that expired September 30, 2009, was effectively extended in March till year end 2010 after numerous shorter-term rollovers. Several in Congress have called for a new 6-year bill with substantially higher funding for some time and the issue was brought back to the table by President Obama calling for $50 billion in more spending. **With Republicans most likely gaining seats and deficit spending on the "outs" with the public, the chance of any new 6-year highway bill seems remote much less one at significantly higher funding rates**.

However, while we believe a 6-year bill to be renewed, we aren't sure whether we will see another infrastructure stimulus in the future[5]. We think the way to assess this situation could be the following: either a stimulus is implemented again or the economy recovers enough not to warrant another stimulus. Either way, the temporary revenue "boost" (or crutch) that VMC experiences (through 2009-2011) will stay constant going forward—either in the form of continued stimulus (the government continues to step in), or a hand-off to a recovering economy (the private sector steps in). However, if political, fiscal conservatism prevents another stimulus from taking place, while the private sector does not recover commensurately, this could have a substantial negative impact on VMC.

Housing and Private Sector Slow to Recover. Housing starts (the number of privately owned new houses on which construction has been started in a given period) have experienced an unprecedented negative shock in the past 3 years. While, the pace of new home construction in the U.S. made a modest rebound in July 2010, building still remains weak as the housing market struggles to gain momentum. Builders in the U.S. turned pessimistic in August this year, with the sign that expiration of a government tax credit will keep depressing home construction. The National Association of Home Builders/Wells Fargo confidence index dropped to 13 in August as well, the lowest level since March 2009, from 14 in July. This uncertainty is underscored by a previous July decline in building permits, which fell 3.1 per cent from June to 565,000. Permits signal future construction and are down 3.7 per cent year-on-year. According to the Associated General Contractors of America:

> Federal investments from the stimulus and other programs are protecting some construction workers from a devastating downturn in private construction activity," said Ken Simonson, the association's chief economist. **"But the industry will continue to be at risk of greater economic hardships as long as private demand for construction continues to shrink."**[6]

California and Florida Evoke Concern as VMC Main States. California and Florida comprise over 36% of Vulcan's sales. Both states are struggling with weak demand and substantial oversupply in the housing

[4] US Census http://www.census.gov/const/C30/s&lsa2009.pdf
[5] We saw $27 billion in highway stimulus with the ARRA act in 2009, roughly 50% will be spent in 2010 and the remaining has been allocated for 2011.
[6] Private Construction Spending Continues "Devastating" Decline
http://www.realestaterama.com/2010/10/01/stimulus-base-realignment-other-federal-programs-drive-total-construction-spending-up-04-percent-to-812-billion-in-august-ID07906.html

market. While, in the long-run these states may become once again fast-growing, we believe that they will not see a recovery to warrant new development until 2015.[7] Beyond the private sector, both states have significant budget concerns; this translates into tremendous pressure on the construction industry:

> "**The lack of a budget is delaying the award of new highway projects. This is having a dramatic impact on our ability to manage and schedule our human and material resources**," said Daniel E. Himick, President of C.C. Myers, Inc. "In Southern California, we have more projects ready to be awarded to us than what we have in place. Therefore we have subcontractors, material suppliers, equipment and labor standing by, not knowing when they can start to work. We bid some of the projects to be concurrent work with our existing projects that we now cannot entirely realize due to the delay of award. **These delays are costly to us, the industry and the public.**"
>
> "It is severely impacting the construction industry. The bidding of many new contracts is being postponed or the awards are being delayed or cancelled. This in turn is delaying the hiring of additional workers and in some cases leading to layoffs of current staff," said Stephen S. Rados, Co-President of Steve P. Rados, Inc., a major freeway contractor. "**Construction in California should not be held hostage by the inability of our representatives in Sacramento to do their job and this crisis just magnifies the need for a stable funding source to build and maintain our infrastructure**."[8]

According to The Fiscal Survey of States by National Governors Association and National Association of State Budget Officers, 21 states will make or have made fiscal program cuts in transportation for 2010.[9] For context, only 15 states made cuts in 2009. For 2010, while California is not listed as slashing its transportation budget, Florida is.

Pricing Concerns. In VMC's 2Q10 report, unit pricing in all of the company's products fell from 2009, with aggregate pricing down 2%. On VMC's 2Q10 analyst call, Ted Grooms with Stephens Research asks:

> Okay and last question and this is one that, I think it has a lot of people kind of scratching their head now. I mean this is your first quarter to ever announce a down price or down year-over-year price that I could ever find. And there is very little price elasticity with aggregates etcetera. And what I'd love to get your view on is, **why now that volumes are just now starting to really improve for the first time in 16 quarters, are we finally starting to see people in this industry getting more aggressive with price? And this is an industry that thus far has had incredible pricing power.**

We believe the pricing puzzle can be explained by the economics of the industry and the government as a major customer. To understand the supply/demand economics of the industry, the production of aggregates is a process that does not require high start-up costs. Beyond this, firms already oversee immense inventory. To illustrate, while aggregate demand in 2030 is expected to be 5 billion tons, VMC alone has proven and probable aggregates reserves of over 14 billion tons. This would normally indicate weak supplier power; however, because of the substantial barriers to entry, the industry has stronger supplier among firms. We think that building material companies may be building their reserves in preparation to environmental regulations that could prevent new quarries to be exploited. A counter-

[7] Latest Housing Recovery Prediction: 2015: http://blogs.wsj.com/developments/2009/05/13/latest-housing-recovery-prediction-2015/
[8] Mobility 21 Warns Budget Impasse Will Cost Thousands of Jobs and Highway Construction Delays http://www.earthtimes.org/articles/press/jobs-highway-construction-delays,1474435.html
[9] The Fiscal Survey of States http://www.nasbo.org/LinkClick.aspx?fileticket=gxz234BlUbo%3d&tabid=65

acting force is that the industry is a highly fragmented industry with approximately 5,000 companies managing more that 10,000 operations.

We believe that the main reason prices remained so elevated given industry fragmentation was that the government was a major buyer in the market. As the government is not known for frugality or disciplined budgeting, we believe that bureaucracy allowed for higher prices than would have normally arisen in a private market. As demand began to fall, firms became much more competitive in both the public and private sectors. This delay or stickiness in pricing, along with weak demand, may indicate a lower price hangover for the next several quarters. With this in mind, we do not expect prices to increase significantly *until the private sector assumes a recovery*.[10] Indeed, if we presume that public spending has stayed constant over time, or has gone slightly up—the only reason to explain the decrease in price is the absence of private sector demand.

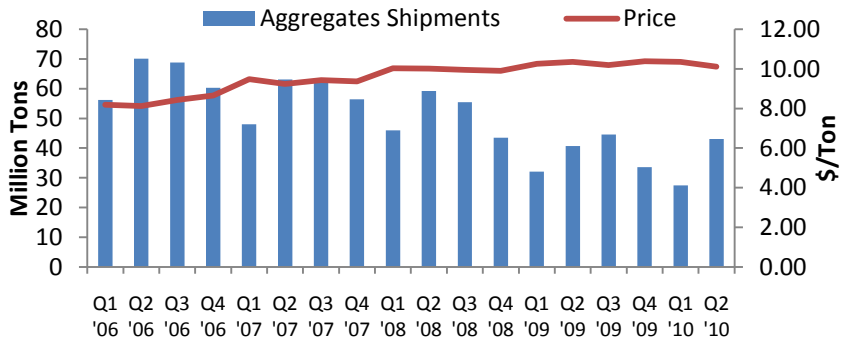
M&A Activity

Given that most of the large building materials companies are overleveraged and some even suffering from financial distress, we do not think that Vulcan will suffer a takeover in the near future.

Product Shipment and Price Analysis

Although, first quarter of 2010 showed weak volume results in a YoY basis, second quarter volumes started to pick up. Historically, sales are higher in the second and third quarter given that weather conditions favor the construction industry. Prices for all value segments are trending lower. We believe this is due to the fall in demand.

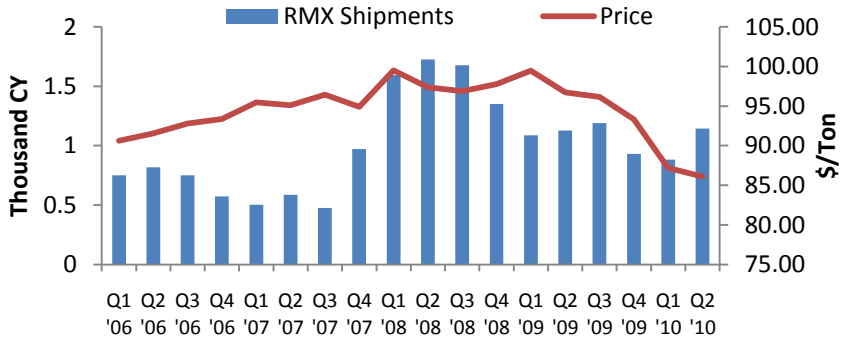
Exhibit 3
VMC's Aggregates Shipments and Price
Million Tons and US $/Ton



Source: Vulcan Materials Company

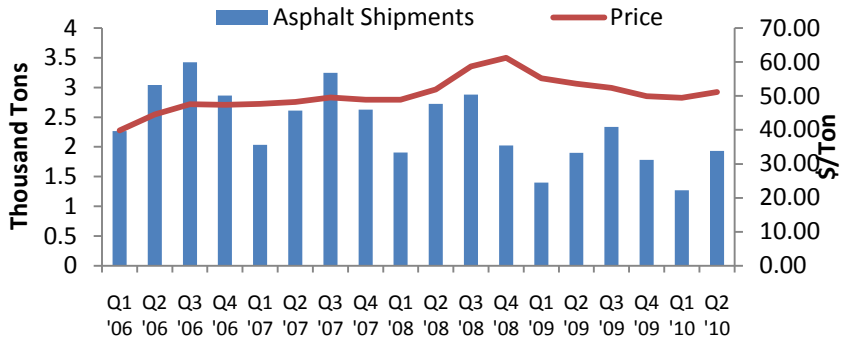
[10] We believe this will be in 2015.

Exhibit 4
VMC's Readymix Shipments and Price
'000 Cubic Yards and US $/CY



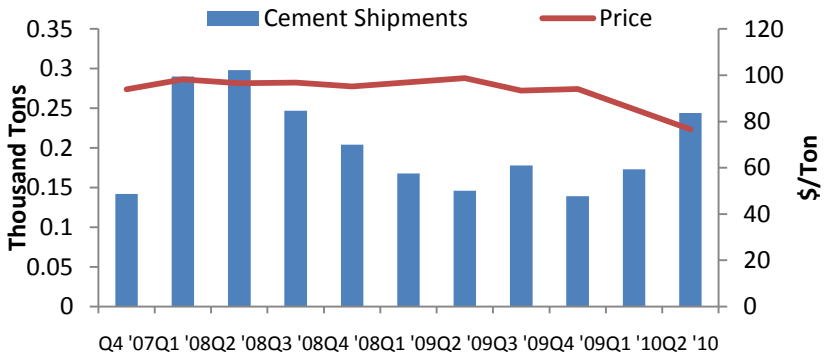
Source: Vulcan Materials Company

Exhibit 5
VMC's Asphalt Mix Shipments and Price
'000 Tons and US $/Ton



Source: Vulcan Materials Company

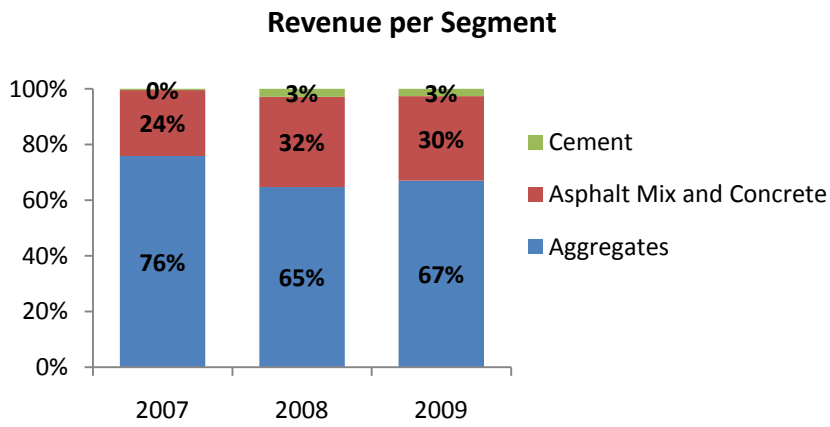
Exhibit 6
VMC's Cement Shipments and Price
'000 Tons and US $/Ton



Source: Vulcan Materials Company

Aggregates continue to be the main revenue segment, however the asphalt and concrete segments have grown in the past two years. We think that Vulcan will continue to increase the aggregates margins through price increases. We believe that the readymix prices will continue to go down.

Exhibit 7
VMC's Revenue per Segment



Source: Vulcan Materials Company

Regression Analysis

We regressed product shipments (aggregates, asphalt, concrete and cement) against GDP and unemployment. Next, we projected shipments using the Economist Intelligence Unit projections of GDP and unemployment. We multiplied these shipment values by our projected price values to estimate the revenues of Vulcan from 2010 to2015.

Assumptions in Regressions

GDP: From 1947 until 2010 the United States' average quarterly GDP Growth was 3.31 percent reaching an historical high of 17.20 percent in March of 1950 and a record low of -10.40 percent in March of 1958. While the economy is in recovery, we do not expect average growth (3.31%) for the next 5 years—most economists are expecting below average growth for the next 5 years. Consensus appears to average at 3% . The Congressional Office Budget director Doug Elmendorf explains their projections for future GDP growth:

Projected growth from 2015 to 2019 is also below historical average growth rates, a difference that is more than accounted for by slower growth in the labor force because of the retirement of the baby boom generation.

With these issues in mind, for our analysis, we felt that using the Economist Intelligence Unit GDP estimates would be most prudent for industry projections instead of the consensus. According to the Economist Intelligence Unit:

> The private sector is creating far fewer jobs than would be the case in a typical recovery. Retail sales are sluggish, with three consecutive monthly falls in May-July. The housing market, which had showed signs of revival in late 2009, has weakened again following the expiry of temporary tax credits in April. **In light of the disappointing data, we have further revised down our GDP forecast for 2010 to 2.3% (2.7% previously). We maintain our forecast of a further slowdown to 1.5% in 2011 but believe downside risks dominate.** The slowdown in growth reflects the withdrawal of fiscal stimulus and the end of the boost from restocking. Export growth will slow in 2011, as base effects from extremely low exports in 2009 fall out of the equation. Consumers will still be rebuilding their balance sheets, and a marked improvement in the labor market is unlikely, with companies set to continue to meet higher demand by squeezing higher productivity out of existing staff rather than taking on new hires.

We decided to use the EIU's estimates because their previous projections have been impressively accurate. For full disclosure, the EIU's estimates were within 0.6% accuracy from 2000 to 2005 where the economy was not under stress. However, during the crisis period of 2006-2009, EIU's predictions were more inaccurate, within 1.2% accuracy. For comparison, the Philadelphia Federal Reserve Bank predictions over the last ten years have fallen within 1.26% accuracy[11].

Unemployment: The concrete industry is strongly correlated with unemployment; much of this has to do with infrastructure efforts and fiscal policy—in times of how unemployment the government will typically seek to stimulate the economy by pursuing infrastructure development, thereby creating jobs.

As part of the annual budget, the Obama Administration released underlying economic assumptions earlier in the year. For unemployment, the forecast is for an average of 10% in 2010, with a decline to 9.2% in 2011, 8.2% in 2012 and 7.3% in 2013. However, we have used the EIU values in our regression, these values are much more conservative: with 9.4% in 2011, 9% in 2012, 8.7% 2013 and 8.4% in 2014.

[11] Specialty Apparel Industry Report, Caplan and Mathivanan

Product Prices: For 2010's average price, we averaged the 1st and 2nd 2010 quarter prices for 2010 (in all cases lowering the price). For the future projections, we returned to 2009 prices for 2011 (recovery and volume growth raises prices). From here, we used the PPI from the Economist Intelligence unit for 2010 and 2011, keeping the 2011 PPI constant throughout the next 5 years up to 2015.

VMC Valuation Analysis

Given VMC's debt to equity level is not constant, we decided to value the business using an APV model. The model accounts for the Net Operating Losses that the firm had during 2009. The base case scenario which considers a terminal growth of 2.4% results in an enterprise value of US$8.2B and a US$42.08 price per share. VMC is trading at US$36.75, which means that the market is undervaluing VMC by 12.6%.

Valuation Sensitivity Analysis

Enterprise Value

Million US	Equity Beta				
Growth Rate	1.08	1.12	1.16	1.20	1.24
2.20%	8,385.22	8,188.09	7,987.26	7,823.10	7,653.85
2.30%	8,482.93	8,280.74	8,074.93	7,906.81	7,733.59
2.40%	8,583.74	8,376.28	8,165.26	7,993.03	7,815.68
2.50%	8,687.80	8,474.83	8,258.39	8,081.86	7,900.22
2.60%	8,795.28	8,576.55	8,354.44	8,173.44	7,987.32

Price per Share

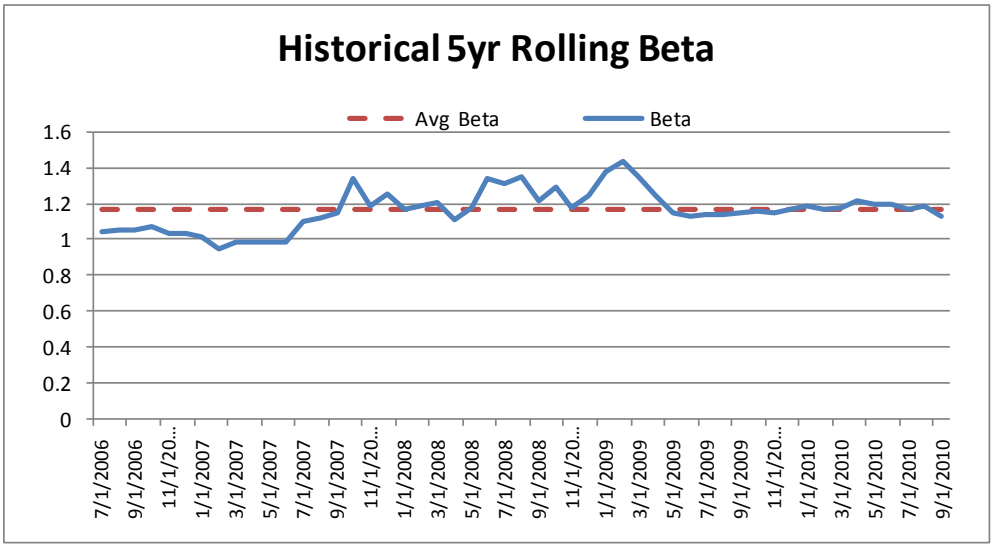
Million US	Equity Beta				
Growth Rate	1.08	1.12	1.16	1.20	1.24
2.20%	43.79	42.25	40.69	39.42	38.10
2.30%	44.54	42.97	41.37	40.07	38.72
2.40%	45.33	43.72	42.08	40.74	39.36
2.50%	46.14	44.48	42.80	41.43	40.02
2.60%	46.97	45.27	43.55	42.14	40.69

Cost of Capital and Equity Beta Analysis

Industry Beta Analysis

Risk Free	2.65%	Source: St. Louis Fed, 10 yr risk free rate
Risk Premium	6.20%	= 7.2% minus 1% to account for Historical Risk Premium
Marginal Tax Rate	30.6%	Source: from Company's 10k

	Vulcan Materials
Beta Equity	1.16
Beta Debt	0.81
D/E	58.26%
Beta Asset	1.06
WACC	8.20%
Unlevered cost Equity (Ra)	9.24%
Levered cost Equity (Re)	9.86%



Valuation Model

Industry Valuation Model		
Tax rate	30.60%	Effective Tax Rate - Company 10k
Rm - rf	6.20%	= 7.2% minus 1% to account for Historical Risk Premium
rf	2.65%	Source: St. Louis Fed, 10 yr risk free rate
Rd	7.69%	BBB rating (10k indicates this is the the weighted average interest on long term debt)
βd	0.81	Implied debt beta
βE	1.16	from Stock return analysis
Re	9.86%	Cost of Equity
βa	1.06	Asset Beta (unlevered beta)
Average D/E	58.26%	Current D/E ratio
WACC	8.20%	
Ra	9.24%	unlevered cost of equity
Growth rate	2.40%	(Sensitivity analysis 2.30% - 2.70%)

Numbers in Million $	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**
Total Revenue	**3327.79**	**3651.44**	**2690.49**	**2499.47**	**2796.94**	**2987.09**	**3167.49**	**3357.55**	**3513.52**	**3724.33**
Aggregates	2,523.72	2,365.94	1,802.61	1,539.97	1,758.59	1,897.87	2,024.03	2,156.20	2,251.97	2,387.09
Asphalt Mix and Concrete	789.53	1,180.81	816.79	903.13	972.24	1,019.16	1,069.20	1,122.65	1,178.12	1,248.81
Cement	14.53	104.69	71.08	56.37	66.11	70.06	74.26	78.70	83.43	88.43
Cost of Goods Sold	**(2,139.23)**	**(2,703.37)**	**(2,097.75)**	**(1,960.66)**	**(2,138.93)**	**(2,258.23)**	**(2,371.73)**	**(2,467.17)**	**(2,559.55)**	**(2,664.50)**
Aggregates	(1,507.44)	(1,594.96)	(1,319.24)	(1,127.02)	(1,248.60)	(1,347.49)	(1,437.06)	(1,530.91)	(1,576.38)	(1,623.22)
Asphalt Mix and Concrete	(618.25)	(1,027.44)	(710.69)	(785.72)	(836.13)	(856.10)	(876.75)	(875.66)	(918.93)	(974.07)
Cement	(13.54)	(80.97)	(67.82)	(47.92)	(54.21)	(54.65)	(57.92)	(60.60)	(64.24)	(67.21)
Gross Profit	**1,188.56**	**948.07**	**592.75**	**538.81**	**658.00**	**728.86**	**795.76**	**890.38**	**953.97**	**1,059.83**
SG&A	(289.60)	(342.60)	(321.60)	(299.94)	(279.69)	(298.71)	(285.07)	(302.18)	(316.22)	(335.19)
Depreciation & Amortization	(271.50)	(389.10)	(394.60)	(199.96)	(223.75)	(298.71)	(316.75)	(402.91)	(456.76)	(521.41)
Operating Income (EBIT)	**627.46**	**216.37**	**(123.45)**	**38.92**	**154.55**	**131.44**	**193.94**	**185.30**	**180.99**	**203.23**
Taxes on EBIT	**(192.00)**	**(51.71)**	**-**	**(11.91)**	**(47.29)**	**(40.22)**	**(59.35)**	**(56.70)**	**(55.38)**	**(62.19)**
NOPLAT	**435.46**	**164.66**	**(123.45)**	**27.01**	**107.26**	**91.22**	**134.59**	**128.60**	**125.61**	**141.04**
Depreciation & Amortization	271.50	389.10	394.60	199.96	223.75	298.71	316.75	402.91	456.76	521.41
Change in Working Capital	(18.06)	57.54	133.75	(1.39)	(20.82)	(13.31)	(12.63)	(13.30)	(10.92)	(3,739.08)
Net CAPEX	(480.50)	(354.20)	(106.20)	(99.98)	(139.85)	(238.97)	(285.07)	(302.18)	(316.22)	(335.19)
Free Cash Flow	**573.36**	**564.50**	**472.33**	**300.63**	**366.20**	**346.82**	**375.43**	**451.12**	**501.25**	**574.28**
Terminal Value										**8,602.73**
Discount Factor				**1.00**	**0.92**	**0.84**	**0.77**	**0.70**	**0.64**	**0.59**
PV FCF				**300.63**	**335.24**	**290.65**	**288.03**	**316.83**	**322.28**	**5,401.47**
NPV FCF	**7,255.14**									

Net Operating Losses Analysis										
Initial NOLs (Tax x EBIT)	-	-	-	37.78	25.87	-	-	-	-	-
Increase	-	-	37.78	-	-	-	-	-	-	-
Decrease	-	-	-	(11.91)	(25.87)	-	-	-	-	-
Ending NOLs	-	-	37.78	25.87	-	-	-	-	-	-
Tax Shield Benefit	-	-	-	11.91	25.87	-	-	-	-	-
Free Cash Flow	0.00	0.00	0.00	11.91	25.87	-	-	-	-	-
Terminal Value										0.00
Discount Factor				1.00	0.93	0.86	0.80	0.74	0.69	0.64
PV Tax Shield				**11.91**	**24.02**	**-**	**-**	**-**	**-**	**-**
NPV Tax Shield	**35.93**									

Debt Benefits										
Debt Balance	521.59	3,656.51	3,547.77	2,738.00	2,116.12	1,980.87	1,678.42	1,418.25	1,158.09	2,157.91
Increase	3,170.10	1,082.50	236.50						1,000.00	
Amortization	(35.18)	(1,191.24)	(1,046.27)	(621.88)	(135.25)	(302.45)	(260.17)	(260.17)	(0.18)	(100.00)
Ending Balance	3,656.51	3,547.77	2,738.00	2,116.12	1,980.87	1,678.42	1,418.25	1,158.09	2,157.91	2,057.91
Interest on debt	48.20	172.80	175.30	164.99	146.05	143.42	118.01	109.98	90.22	168.10
Tax Shield	14.75	41.30	53.64	50.49	44.69	43.89	36.11	33.65	27.61	51.44
Free Cash Flow	14.75	41.30	53.64	50.49	44.69	43.89	36.11	33.65	27.61	51.44
Terminal Value										995.72
Discount Factor				1.00	0.93	0.86	0.80	0.74	0.69	0.64
PV Tax Shield				**50.49**	**41.50**	**37.84**	**28.91**	**25.02**	**19.06**	**671.37**
NPV Tax Shield	**874.19**									

Enterprise Value	**8,165.26**	
Outstanding Debt	2,750.00	as of Oct 8th 2010
Equity Value	**5,415.26**	
Shares Outstanding	**128.70**	million shares
Price per share	**$ 42.08**	

Conclusions

Our APV analysis shows that both the enterprise value and the price per share are below the market data. We are issuing a buy rating on Vulcan Materials and we believe **the market is undervaluing the stock price considering a 12 month horizon**.

To summarize our views, we believe that federal spending will remain constant and that the current stimulus will fade in 2012. As most states (including Vulcan's main states of California and Florida) are dealing with budget concerns, **there could be a further decrease in state infrastructure spending going forward**. Compounding this, the private sector may continue to stumble, only showing a slight uptick in overall construction values since the beginning of the year.

One final concern is the extended price softening on all of VMC's product lines. We believe that the main reason prices remained so elevated in the past involved the government as a major buyer in the market. As demand has fallen, firms have become much more competitive in both the public and private sectors. This delay or stickiness in pricing, along with continuing weak private sector demand, may indicate a lower price hangover for the next several quarters. With this in mind, **we do not expect prices to increase significantly until the private sector assumes a recovery.**

Our conclusion here is that VMC is highly dependent on public spending and faces negative pricing pressure. We expect public dependency and pricing hardship will only increase if private construction weakens. More concerning, a delay in stimulus or ongoing state fiscal troubles could have a significantly negative impact on Vulcan's sales. **However, after completing our valuation with this negativity factored in, the stock price is still significantly undervalued.**

After analysis we feel that **the fair price is US$42.08**. VMC is trading at US$36.75, which means that **the market is undervaluing VMC by 12.6%**.

Back-ups

Economist Intelligence Unit – United States Annual data and forecast (http://www.eiu.com/)

Data and charts

Annual data and forecast

	2005[a]	2006[a]	2007[a]	2008[a]	2009[a]	2010[b]	2011[b]
GDP							
Nominal GDP (US$ bn)	12,638	13,399	14,062	14,369	14,119	14,528	14,982
Real GDP growth (%)	3.1	2.7	1.9	0.0	-2.6	2.3	1.5
Expenditure on GDP (% real change)							
Private consumption	3.4	2.9	2.4	-0.3	-1.2	1.4	1.2
Government consumption	0.3	1.4	1.3	2.8	1.6	0.6	0.9
Gross fixed investment	6.5	2.3	-1.8	-6.4	-18.3	5.5	5.9
Exports of goods & services	6.7	9.0	9.3	6.0	-9.5	11.3	5.5
Imports of goods & services	6.1	6.1	2.7	-2.6	-13.8	14.4	5.2
Origin of GDP (% real change)							
Agriculture	8.6	-5.3	7.0	-0.6	2.0[c]	2.0	2.0
Industry	-2.2	2.6	-1.4	-1.1	-5.5[c]	3.3	1.7
Services	4.2	2.9	2.8	1.7	-2.0[c]	2.1	1.4
Population and income							
Population (m)	295.7	298.4	301.3	304.1	306.8[c]	309.6	312.3
GDP per head (US$ at PPP)	42,736	44,896	46,670	47,258	46,021[c]	46,931	47,965
Recorded unemployment (av; %)	5.1	4.6	4.6	5.8	9.3	9.7	9.4
Fiscal indicators (% of GDP)							
Public-sector balance[d]	-2.6	-1.9	-1.2	-3.2	-10.0	-9.0	-7.1
Public-sector debt interest payments	1.5	1.7	1.7	1.8	1.3	1.4	1.4
Public-sector primary balance	-1.1	-0.2	0.5	-1.4	-8.7	-7.6	-5.6
Net public debt	36.9	36.5	36.2	37.7	53.5	59.0	64.9
Prices and financial indicators							
Exchange rate ¥:US$ (end-period)	117.9	119.0	111.7	90.8	93.1	88.5	90.0
Consumer prices (end-period; %)	3.3	2.5	4.1	0.0	2.8	0.5	1.4
Producer prices (av; %)	4.9	2.9	3.9	6.4	-2.5	4.1	2.1
Stock of money M1 (% change)	-0.3	-0.7	0.5	16.1	6.4[c]	-8.5	0.5
Stock of money M2 (% change)	4.0	6.0	6.0	9.7	3.6[c]	2.9	4.7
Lending interest rate (av; %)	6.2	8.0	8.1	5.1	3.3	3.3	3.4
Current account (US$ m)							
Trade balance	-784	-839	-823	-835	-507	-634	-680
Goods: exports fob	909	1,036	1,160	1,305	1,068	1,267	1,375
Goods: imports fob	-1,693	-1,875	-1,984	-2,140	-1,575	-1,901	-2,055
Services balance	70	80	121	136	132	111	108
Income balance	72	48	100	152	121	79	111
Current transfers balance	-106	-91	-116	-122	-125	-129	-133
Current-account balance	-748	-803	-718	-669	-378	-572	-594
International reserves (US$ m)							
Total international reserves	65	66	71	78	131	-	-

[a] Actual. [b] Economist Intelligence Unit forecasts. [c] Economist Intelligence Unit estimates. [d] Federal government, financial year (October - September).

Source: IMF, International Financial Statistics.

Economic growth

%	2009	2010	2011	2012	2013	2014
GDP	-2.6	2.3	1.5	1.9	2.2	2.4
Private consumption	-1.2	1.4	1.2	1.5	1.8	1.9
Government consumption	1.6	0.6	0.9	1.5	1.5	1.5
Gross fixed investment	-18.3	5.5	5.8	4.6	5.8	6.4
Exports of goods & services	-9.5	11.3	5.5	6.2	6.0	6.1
Imports of goods & services	-13.8	14.4	5.2	5.2	5.5	5.6
Domestic demand	-3.7	3.0	1.6	1.9	2.3	2.4
Agriculture	2.0	2.0	2.0	2.0	2.0	2.0
Industry	-5.5	3.3	1.7	2.5	2.5	2.5
Services	-2.0	2.1	1.4	1.8	2.2	2.4

Ready-mix Concrete Manufacturing Report 2002 – US Census Bureau

Table 1. Historical Statistics for the Industry: 2002 and Earlier Years

[Data based on the 2002 Economic Census and the 2002 Annual Survey of Manufactures (ASM). For information on confidentiality protection, sampling error, nonsampling error, and explanation of terms, see note at end of table. For meaning of abbreviations and symbols, see introductory text]

Industry and year[1]	Companies[2]	All establishments[3]	All employees: Number[4]	All employees: Payroll ($1,000)	Production workers: Number[4]	Production workers: Hours (1,000)	Production workers: Wages ($1,000)	Value added ($1,000)	Total cost of materials ($1,000)	Total value of shipments ($1,000)	Total capital expenditures ($1,000)
327320, Ready-mix concrete manufacturing 2002	2 596	5 570	98 360	3 640 427	79 582	160 454	2 794 396	10 286 897	11 299 472	21 573 773	[r]890 731
2001	N	N	102 790	3 709 915	81 370	172 852	2 716 372	10 017 236	11 459 783	21 472 894	838 234
2000	N	N	101 103	3 622 064	79 796	171 405	2 643 683	9 518 744	11 412 475	20 933 332	938 092
1999	N	N	102 044	3 529 981	81 141	173 135	2 592 088	9 475 861	11 081 867	20 569 578	985 361
1998	N	N	94 401	3 177 079	75 157	158 418	2 346 495	8 832 097	10 533 584	19 388 319	834 318
1997	2 888	5 221	93 136	2 965 346	72 464	147 770	2 153 268	7 780 774	9 418 330	17 219 886	798 851

[1]Statistics presented for years ending in 2 and 7 are census data. Interim census years are derived in a representative sample of manufacturing establishments canvassed in the Annual Survey of Manufactures (ASM).
[2]For the census, a company is defined as a business organization consisting of one establishment or more under common ownership or control.
[3]Includes establishments with payroll at any time during the year.
[4]Number of employees figures represent average number of production workers for pay period that includes the 12th of March, May, August, and November plus other employees for payroll period that includes the 12th of March.

Note: The data in this table are based on the 2002 Economic Census and the 2002 Annual Survey of Manufactures (ASM). To maintain confidentiality, the Census Bureau suppresses data to protect the identity of any business or individual. The census results in this table contain sampling errors and nonsampling errors. Data users who create their own estimates using data from American FactFinder tables should cite the Census Bureau as the source of the original data only. For explanation of terms, see Appendix A. For full technical documentation, see Appendix C.

Producer Price Indexes Data – Bureau of Labor Statistics (http://www.bls.gov/ppi/)

PPI Index Cement

Producer Price Index Industry Data
Original Data Value

Series Id: PCU32731032731002
Industry: Cement manufacturing
Product: Portland cement ASTM type II, hydraulic
Base Date: 200506
Years: 2005 to 2010

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Annual
2005						100.0							
2007	119.5	119.9	116.6	120.5	119.5	119.4	121.8	121.1	120.8	119.5	119.1	118.6	119.7
2008	117.8	117.1	116.7	118.0	115.6	114.8	118.1	117.7	117.3	118.2	118.1	117.5	117.2
2009	121.1	117.9	115.1	116.1	114.1	113.0	110.9	111.1	111.6	111.0	110.5	110.5	113.6
2010	111.0	110.3	109.7	109.2	110.2	109.0	108.9						

PPI Index Aggregates

Producer Price Index Industry Data
Original Data Value

Series Id: PCU212321212321
Industry: Construction sand and gravel mining
Product: Construction sand and gravel mining
Base Date: 198206
Years: 2000 to 2010

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Annual
2000	171.0	172.5	172.6	175.2	176.1	176.2	176.7	177.3	177.1	177.3	177.2	177.0	175.5
2001	178.8	180.2	180.3	181.3	182.0	182.5	182.3	182.6	182.5	182.2	181.9	182.6	181.6
2002	184.6	185.0	184.8	185.6	186.0	186.3	186.3	186.2	186.2	186.3	186.2	186.4	185.8
2003	187.0	187.3	187.2	188.2	188.9	189.6	189.9	189.9	189.9	189.8	190.1	189.0	188.9
2004	191.0	191.5	191.9	194.5	194.8	195.7	195.9	196.0	196.6	196.9	197.7	197.6	195.0
2005	202.8	203.7	204.2	206.8	208.9	209.4	211.1	211.3	213.4	214.5	215.1	217.6	209.9
2006	222.4	222.4	223.2	227.5	228.8	230.1	231.2	232.1	232.3	232.3	233.5	233.7	229.1
2007	240.7	242.8	243.2	247.0	248.2	246.3	246.1	248.3	249.2	250.6	250.8	250.6	247.0
2008	255.2	256.5	258.7	261.4	261.6	262.1	263.0	265.4	265.7	266.1	267.3	268.7	262.6
2009	270.1	270.8	271.8	271.7	272.0	271.7	271.4	270.7	270.4	270.4	271.1	271.5	271.1
2010	269.8	270.2	271.7	270.9	271.6	271.0	269.7						

PPI Index Ready-mix Concrete

Producer Price Index Industry Data
Original Data Value

http://data.bls.gov

Series Id: PCU327320327320
Industry: Ready-mix concrete manufacturing
Product: Ready-mix concrete manufacturing
Base Date: 198106
Years: 1981 to 2009

Year	Annual
1981	98.9
1982	100.9
1983	102.3
1984	105.1
1985	108.6
1986	109.5
1987	109.2
1988	109.7
1989	111.5
1990	114.3
1991	116.9
1992	117.4
1993	121.0
1994	125.8
1995	131.3
1996	135.2
1997	138.0
1998	142.3
1999	145.6
2000	150.2
2001	153.4
2002	153.0
2003	153.9
2004	162.1
2005	181.9
2006	202.5
2007	210.3
2008	216.7
2009	222.1
2010	216.9

Discount rate calculation

Industry Beta Analysis		
Risk Free	2.65%	Source: St. Louis Fed, 10 yr risk free rate
Risk Premium	6.20%	= 7.2% minus 1% to account for Historical Risk Premium
Marginal Tax Rate	30.6%	Source: from Company's 10k

	Vulcan Materials
Beta Equity	1.16
Beta Debt	0.81
D/E	58.26%
Beta Asset	1.06
WACC	8.20%
Unlevered cost Equity (Ra)	9.24%
Levered cost Equity (Re)	9.86%

Quarterly EPS Forecast

Numbers in Million $	2010 Q3	2010 Q4
Total Revenue	**743.25**	**572.82**
Aggregates	464.21	353.84
Asphalt Mix and Concrete	263.64	193.40
Cement	15.40	25.58
Cost of Goods Sold	**(582.19)**	**(448.96)**
Gross Profit	**161.06**	**123.86**
SG&A	(89.19)	(68.74)
Depreciation & Amortization	(74.32)	(57.28)
Operating Income (EBIT)	**(2.45)**	**(2.16)**
Taxes on EBIT	**-**	**-**
NOPLAT	**(2.45)**	**(2.16)**
Depreciation & Amortization	74.32	57.28
Change in Working Capital	(3.65)	11.93
Net CAPEX	(29.73)	(22.91)
Free Cash Flow	**90.59**	**84.31**
Net Income	**8.40**	**(3.24)**
Free Cash Flow	90.59	84.31
Interest expense	(41.25)	(41.25)
Depreciation	(74.32)	(57.28)
Change in WC	3.65	(11.93)
CAPEX	29.73	22.91
EPS	0.07	(0.03)

Aggregates Volume Regression

SUMMARY OUTPUT

Regression Statistics	
Multiple R	0.980713
R Square	0.961797
Adjusted R Square	0.942696
Standard Error	9.026352
Observations	7

ANOVA

	df	*SS*	*MS*	*F*	*ignificance F*
Regression	2	8204.957	4102.478	50.35258	0.001459
Residual	4	325.9001	81.47504		
Total	6	8530.857			

	Coefficients	*ndard Err*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*ower 95.0%*	*pper 95.0%*
Intercept	370.2702	36.91296	10.0309	0.000555	267.7834	472.757	267.7834	472.757
GDP	-0.0027	0.003083	-0.87619	0.430394	-0.01126	0.005859	-0.01126	0.005859
Unemployment	-18.0235	2.067086	-8.71926	0.000953	-23.7626	-12.2843	-23.7626	-12.2843

Readymix Volume Regression

SUMMARY OUTPUT

Regression Statistics	
Multiple R	0.688412323
R Square	0.473911526
Adjusted R Square	0.263476137
Standard Error	1.07380016
Observations	8

ANOVA

	df	*SS*	*MS*	*F*	*ignificance F*
Regression	2	5.193444	2.596722	2.252052	0.200746
Residual	5	5.765234	1.153047		
Total	7	10.95868			

	Coefficients	*ndard Err*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*ower 95.0%*	*pper 95.0%*
Intercept	-2.012780168	3.424745	-0.58772	0.582261	-10.8164	6.790807	-10.8164	6.790807
GDP	0.000274127	0.000285	0.961598	0.380415	-0.00046	0.001007	-0.00046	0.001007
Unemployment	0.342991765	0.238296	1.439349	0.209588	-0.26957	0.955552	-0.26957	0.955552

Asphalt Volume Regression

SUMMARY OUTPUT

Regression Statistics	
Multiple R	0.94973
R Square	0.901987
Adjusted R Square	0.862782
Standard Error	0.504482
Observations	8

ANOVA

	df	*SS*	*MS*	*F*	*ignificance F*
Regression	2	11.71054	5.855272	23.00678	0.003008
Residual	5	1.27251	0.254502		
Total	7	12.98305			

	Coefficients	*tandard Err*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*ower 95.0%*	*pper 95.0%*
Intercept	15.29915	1.608979	9.508611	0.000218	11.16314	19.43517	11.16314	19.43517
GDP	-6.2E-05	0.000134	-0.46564	0.661048	-0.00041	0.000282	-0.00041	0.000282
Unemployment	-0.69219	0.111954	-6.18283	0.001613	-0.97998	-0.40441	-0.97998	-0.40441

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