IDMSA DOM MAKLERSKI

Quarterly Results Preview

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PBG

Sector: Construction
Fundamental rating: Hold (→)
Market relative: Neutral (↓)
Price: PLN 233.3
12M EFV: PLN 225.0 (↓)

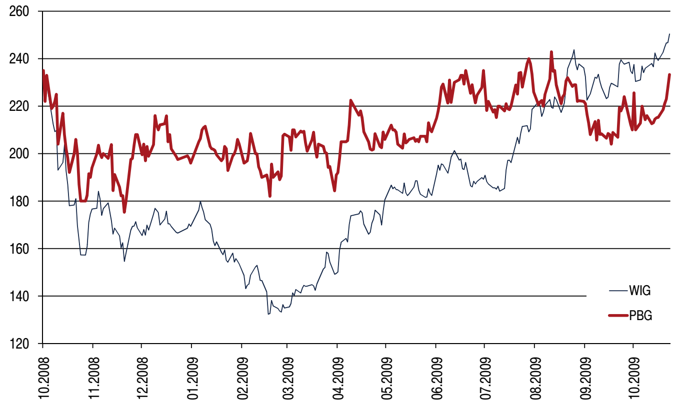
Market Cap.: US$ 1,126 m
Reuters code: PBGG.WA
Av. daily turnover: US$ 2.91 m
Free float: 67%
12M range: PLN 175.30-242.90

Key data

IFRS consolidated		2008	2009E	2010E	2011E
Sales	*PLN m*	2,089.3	2,729.7	3,132.1	3,508.0
EBITDA	*PLN m*	270.3	364.3	399.6	421.7
EBIT	*PLN m*	223.4	317.1	349.6	369.1
Net profit	*PLN m*	158.0	195.4	231.2	253.7
EPS	*PLN*	11.76	13.67	16.17	17.75
EPS yoy chng	*%*	55	16	18	10
Net debt	*PLN m*	507.8	432.5	335.9	189.6
P/E	*x*	19.8	17.1	14.4	13.1
P/CE	*x*	15.3	13.8	11.9	10.9
EV/EBITDA	*x*	13.5	10.3	9.2	8.4
EV/EBIT	*x*	16.3	11.9	10.5	9.5
EV/Sales	*x*	1.7	1.4	1.2	1.0
Gross dividend yield	*%*	0.0	0.0	0.0	0.0
No. of shares (eop)	*ths.*	13,430	14,295	14,295	14,295

Source: Company, DM IDMSA estimates

Stock performance



Source: ISI

Upcoming events

1. 3Q09 results release: November 16, 2009

Catalysts

1. Signing new large environmental protection contracts co-financed by EU
2. Signing new LT and high-margin gas&oil contracts
3. Synergies with Energomontaż Południe

Risk factors

1. Lower margins on stadium contracts

Quarterly results corner; 3Q09E preview

PBG will publish its results for 3Q09 on November 16. We expect the Company's figures to be good (projecting a double digit yoy growth of profits), although in our view this should not come as a major surprise for investors (for details please refer to *Figure 1*).

On the back of a well developed contract portfolio, we project a 38% yoy increase in the Company's quarterly sales. While the backlog is large (almost 100% coverage of our FY09 and FY10 sales forecasts), which materially enhances the visibility of PBG's top line even for 2011, in our view its quality seems mixed. To expand on this, on the one hand we expect the Company to recognise fat margins on contracts signed when prices were at their peak (for example contracts signed with PGNiG), while on the other hand the margins to be made on stadium contracts look feeble (these were signed by Hydrobudowa Polska, its key subsidiary, during times of tight competition and a price war among contractors) and in our opinion these may become a burden for PBG's results starting from 3Q09 (however, please note that the largest part of construction works related to stadiums is scheduled for 2010). Consequently, we forecast that PBG's quarterly operating profit margin will be slightly lower yoy, which translates into a projected yoy rise of 'only' 21% of PBG's quarterly EBIT.

Fig. 1 *PBG; 3Q09 and 1-3Q09 results' forecast*

IFRS consolidated PLN m	3Q09E	3Q08A	yoy change	1-3Q09E	1-3Q08A	yoy change
Sales	750.0	543.2	38%	1698.6	1370.0	24%
EBIT	70.0	57.8	21%	172.5	142.6	21%
EBIT margin	*9.3%*	*10.6%*	-	*10.2%*	*10.4%*	-
Pre-tax profit	56.5	54.1	4%	151.1	122.9	23%
Pre-tax margin	*7.5%*	*10.0%*	-	*8.9%*	*9.0%*	-
Net profit	42.0	34.5	22%	112.2	84.5	33%
Net margin	*5.6%*	*6.4%*	-	*6.6%*	*6.2%*	-

	Realization of the FY figures in:		Realization of the FY figures in:	
	3Q09E	3Q08A	1-3Q09E	1-3Q08A
Sales	27%	26%	62%	66%
EBIT	22%	26%	54%	64%
Pre-tax profit	21%	25%	55%	58%
Net profit	22%	22%	57%	53%

Source: Company, DM IDMSA estimates

At the pre-tax level, we forecast that the Company's numbers will remain broadly flat yoy. The reason for this is an envisaged yoy hike in financial costs stemming from: (i) the higher cost of debt service (the Company had to prolong its debt in the last quarter), and (ii) FX losses due to qoq EUR vs. PLN depreciation (part of its receivables is EUR denominated). However, due to an envisaged lower yoy share of minorities in the Company's net income in 3Q09, we forecast an approx. 22% yoy rise in net profit.

Financial forecast

We have revised our financial forecast for PBG (for details please refer to *Figure 2*). We maintain our sales forecast intact, while our EBIT and NP forecasts decrease in 2009 and beyond by 4-12%

Fig. 2 PBG; Changes in IDM's forecast

IFRS consolidated	2009E			2010E			2011E			2012E		
PLN m	current	previous	change	current	previous	change	current	previous	change	current	previous	change
Sales	2,729.7	2,729.7	0%	3,132.1	3,132.1	0%	3,508.0	3,508.0	0%	3,935.4	3,935.4	0%
EBIT	317.1	330.6	-4%	349.6	377.1	-7%	369.1	412.8	-11%	403.8	460.5	-12%
NI	195.4	198.9	-2%	231.2	242.7	-5%	253.7	267.4	-5%	285.8	304.7	-6%

Source: DM IDMSA estimates

and 2-6% respectively. The reason behind this is the financial results of HBP, a 61% subsidiary of PBG, which are lower than previously projected (we expect small margins on stadium and some environmental protection contracts).

Valuation

As a result of the downgrade in the financial forecast, we decrease our 12M EFV for PBG by 7% to PLN 225 per share.

Recommendation

We maintain our LT fundamental Hold recommendation for PBG, while our ST market-relative stance is decreased by one notch to Neutral (from Overweight previously). Although we expect the Company to make fat margins on contracts signed when prices were at their peak (e.g. those with PGNiG), we expect thin margins on stadium contracts (these were signed by HBP, its key subsidiary, after the peak of the cycle), which in our view may become a burden for the Company's operating margin beginning from 3Q09.

BASIC DEFINITIONS

A/R turnover (in days) = 365/(sales/average A/R))
Inventory turnover (in days) = 365/(COGS/average inventory))
A/P turnover (in days) = 365/(COGS/average A/P))
Current ratio = ((current assets – ST deferred assets)/current liabilities)
Quick ratio = ((current assets – ST deferred assets – inventory)/current liabilities)
Interest coverage = (pre-tax profit before extraordinary items + interest payable/interest payable)
Gross margin = gross profit on sales/sales
EBITDA margin = EBITDA/sales
EBIT margin = EBIT/sales
Pre-tax margin = pre-tax profit/sales
Net margin = net profit/sales
ROE = net profit/average equity
ROA = (net income + interest payable)/average assets
EV = market capitalization + interest bearing debt – cash and equivalents
EPS = net profit/ no. of shares outstanding
CE = net profit + depreciation
Dividend yield (gross) = pre-tax DPS/stock market price
Cash sales = accrual sales corrected for the change in A/R
Cash operating expenses = accrual operating expenses corrected for the changes in inventories and A/P, depreciation, cash taxes and changes in the deferred taxes

DM IDM S.A. generally values the covered non bank companies via two methods: comparative method and DCF method (discounted cash flows). The advantage of the former is the fact that it incorporates the current market assessment of the value of the company's peers. The weakness of the comparative method is the risk that the valuation benchmark may be mispriced. The advantage of the DCF method is its independence from the current market valuation of the comparable companies. The weakness of this method is its high sensitivity to undertaken assumptions, especially those related to the residual value calculation. Please note that we also resort to other valuation techniques (e.g. NAV-, DDM- or SOTP-based), should it prove appropriate in a given case.

Banks

Net Interest Margin (NIM) = net interest income/average assets
NIM Adjusted = (net interest income adjusted for SWAPs)/average assets
Non interest income = fees&commissions + result on financial operations (trading gains) + FX gains
Interest Spread = (interest income/average interest earning assets)/ (interest cost/average interest bearing liabilities)
Cost/Income = (general costs + depreciation + other operating costs)/ (profit on banking activity + other operating income)
ROE = net profit/average equity
ROA = net income/average assets
Non performing loans (NPL) = loans in 'substandard', 'doubtful' and 'lost' categories
NPL coverrage ratio = loan loss provisions/NPL
Net provision charge = provisions created – provisions released

DM IDM S.A. generally values the covered banks via two methods: comparative method and fundamental target fair P/E and target fair P/BV multiples method. The advantage of the former is the fact that it incorporates the current market assessment of the value of the company's peers. The weakness of the comparative method is the risk that the valuation benchmark may be mispriced. The advantage of the fundamental target fair P/E and target fair P/BV multiples method is its independence of the current market valuation of the comparable companies. The weakness of this method is its high sensitivity to undertaken assumptions, especially those related to the residual value calculation.

Assumptions used in valuation can change, influencing thereby the level of the valuation. Among the most important assumptions are: GDP growth, forecasted level of inflation, changes in interest rates and currency prices, employment level and change in wages, demand on the analysed company products, raw material prices, competition, standing of the main customers and suppliers, legislation changes, etc.

Changes in the environment of the analysed company are monitored by analysts involved in the preparation of the recommendation, estimated, incorporated in valuation and published in the recommendation whenever needed.

KEY TO INVESTMENT RANKINGS

This is a guide to expected price performance in absolute terms over the next 12 months:
Buy – fundamentally undervalued (upside to 12M EFV in excess of the cost of equity) + catalysts which should close the valuation gap identified;
Hold – either (i) fairly priced, or (ii) fundamentally undervalued/overvalued but lacks catalysts which could close the valuation gap;
Sell – fundamentally overvalued (12M EFV < current share price + 1-year cost of equity) + catalysts which should close the valuation gap identified.

This is a guide to expected relative price performance:
Overweight – expected to perform better than the benchmark (WIG) over the next quarter in relative terms
Neutral – expected to perform in line with the benchmark (WIG) over the next quarter in relative terms
Underweight – expected to perform worse than the benchmark (WIG) over the next quarter in relative terms

The recommendation tracker presents the performance of DM IDMSA's recommendations. A recommendation expires on the day it is altered or on the day 12 months after its issuance, whichever comes first. Relative performance compares the rate of return on a given recommended stock in the period of the recommendation's validity (i.e. from the date of issuance to the date of alteration or – in case of maintained recommendations – from the date of issuance to the current date) in a relation to the rate of return on the benchmark in this time period. The WIG index constitutes the benchmark. For recommendations that expire by an alteration or are maintained, the ending values used to calculate their absolute and relative performance are: the stock closing price on the day the recommendation expires/ is maintained and the closing value of the benchmark on that date. For recommendations that expire via a passage of time, the ending values used to calculate their absolute and relative performance are: the average of the stock closing prices for the day the recommendation elapses and four directly preceding sessions and the average of the benchmark's closing values for the day the recommendation expires and four directly preceding sessions.

LT fundamental recommendation tracker

Recommendation		Issue date	Reiteration date	Expiry date	Performance	Relative performance	Price at issue/ reiteration (PLN)	12M EFV (PLN)	
PBG									
Hold	–	06.02.2008	-	30.11.2008	-26%	30%	281.60	319.00	–
-	→	-	17.02.2008	-	-	-	317.90	319.00	→
-	→	-	21.02.2008	-	-	-	326.70	352.00	↑
-	→	-	30.03.2008	-	-	-	325.00	358.00	↑
-	→	-	14.04.2008	-	-	-	311.00	357.00	↓
-	→	-	29.04.2008	-	-	-	318.00	361.00	↑
-	→	-	15.05.2008	-	-	-	315.00	361.00	→
-	→	-	01.06.2008	-	-	-	318.00	361.00	→
-	→	-	29.06.2008	-	-	-	268.00	356.00	↓
-	→	-	08.07.2008	-	-	-	238.00	348.00	↓
-	→	-	28.07.2008	-	-	-	245.00	348.00	→
-	→	-	04.08.2008	-	-	-	248.00	348.00	→
-	→	-	31.08.2008	-	-	-	238.00	348.00	→
-	→	-	28.09.2008	-	-	-	232.00	348.00	→
-	→	-	19.10.2008	-	-	-	192.10	305.00	↓
-	→	-	29.10.2008	-	-	-	191.50	305.00	→
-	→	-	06.11.2008	-	-	-	198.30	305.00	→
Buy	↑	30.11.2008	-	16.07.2009	5%	-10%	208.00	305.00	→
-	→	-	11.01.2009	-	-	-	211.50	305.00	→
-	→	-	25.01.2009	-	-	-	192.90	279.00	↓
-	→	-	08.02.2009	-	-	-	208.50	279.00	→
-	→	-	08.03.2009	-	-	-	207.00	279.00	→
-	→	-	05.04.2009	-	-	-	205.00	279.00	→
-	→	-	29.04.2009	-	-	-	209.10	242.00	↓
-	→	-	12.05.2009	-	-	-	208.30	242.00	→
-	→	-	17.05.2009	-	-	-	206.00	242.00	→
-	→	-	08.06.2009	-	-	-	221.30	242.00	→
-	→	-	08.07.2009	-	-	-	215.20	242.00	→
Hold	↓	16.07.2009	-	Not latter than 16.07.2010	7%	-16%	218.50	242.00	→
-	→	-	02.08.2009	-	-	-	226.00	242.00	→
-	→	-	31.08.2009	-	-	-	222.00	242.00	→
-	→	-	12.10.2009	-	-	-	212.60	242.00	→
-	→	-	25.10.2009	-	-	-	233.30	225.00	↓

Market-relative recommendation tracker

Relative recommendation		Issue date	Reiteration date	Expiry date	Price at issue/ reiteration (PLN)	Relative performance
PBG						
Overweight	–	06.02.2008	-	11.01.2009	281.60	30%
-	→	-	17.02.2008	-	317.90	-
-	→	-	21.02.2008	-	326.70	-
-	→	-	30.03.2008	-	325.00	-
-	→	-	14.04.2008	-	311.00	-
-	→	-	29.04.2008	-	318.00	-
-	→	-	15.05.2008	-	315.00	-
-	→	-	01.06.2008	-	318.00	-
-	→	-	29.06.2008	-	268.00	-
-	→	-	08.07.2008	-	238.00	-
-	→	-	28.07.2008	-	245.00	-
-	→	-	04.08.2008	-	248.00	-
-	→	-	31.08.2008	-	238.00	-
-	→	-	28.09.2008	-	232.00	-
-	→	-	19.10.2008	-	192.10	-
-	→	-	29.10.2008	-	191.50	-
-	→	-	06.11.2008	-	198.30	-
-	→	-	30.11.2008	-	208.00	-
Overweight	→	11.01.2009	-	25.10.2009	211.50	-24%
-	→	-	25.01.2009	-	192.90	-
-	→	-	08.02.2009	-	208.50	-
-	→	-	08.03.2009	-	207.00	-
-	→	-	05.04.2009	-	205.00	-
-	→	-	29.04.2009	-	209.10	-
-	→	-	12.05.2009	-	208.30	-
-	→	-	17.05.2009	-	206.00	-
-	→	-	08.06.2009	-	221.30	-
-	→	-	08.07.2009	-	215.20	-
-	→	-	16.07.2009	-	218.50	-
-	→	-	02.08.2009	-	226.00	-
-	→	-	31.08.2009	-	222.00	-
-	→	-	12.10.2009	-	212.60	-
Neutral	→	25.10.2009	-	Not later than 25.10.2010	233.30	-

Distribution of IDM's current recommendations

	Buy	Hold	Sell	Suspended	Under revision
Numbers	18	28	16	1	0
Percentage	29%	44%	25%	2%	0%

Distribution of IDM's current recommendations for companies that were within the last 12M IDM customers in investment banking

	Buy	Hold	Sell	Suspended	Under revision
Numbers	2	3	1	1	0
Percentage	29%	43%	14%	14%	0%

Distribution of IDM's current market relative recommended weightings

	Overweight	Neutral	Underweight	Suspended	Under revision
Numbers	21	23	18	1	0
Percentage	33%	37%	29%	2%	0%

Distribution of IDM's current market relative recommended weightings for the companies that were within the last 12M IDM customers in investment banking

	Overweight	Neutral	Underweight	Suspended	Under revision
Numbers	2	2	2	1	0
Percentage	29%	29%	29%	14%	0%

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