PBG

Growth story is over

Maintained
Sell

Poland
Construction & Materials

Market cap	PLN2,987.7m
Bloomberg	PBG PW

After the sale of majority stakes in two subsidiaries, we believe PBG will struggle to show EPS growth in 2011 and 2012. The planned expansion into new segments, the power industry and waste disposal plants, will deteriorate profit margins. Our 2011F EPS forecasts are 11% below consensus but we believe the growth story is over unless the company can manage to attract new large signings in the coming months. SELL with a new TP of PLN180.

Investment case

In September 2010, PBG announced its intention to sell a 51% stake in subsidiary Hydrobudowa Polska (HBP PW; PLN2.72; NR) as well as a 51% stake in road construction subsidiary Aprivia in a transaction valued at €126.5m to Spanish contractor OHL. The company expects completion of the deal as of beginning 2Q11. After the transaction, PBG will retain a 13% stake in HBP. In order to consolidate HBP's results as an associated company, PBG will gradually increase its stake to 20% on the WSE. The alliance with OHL should enable the expansion of PBG's gas&oil operations in Western Europe and South America. The company also has hopes on a joint bidding process in the prospective local highway concession business in the future.

We exclude HBP from PBG's model as of the beginning of 2Q11. The transaction has a very high probability of success we believe. Following the sale of HBP, the company's backlog decreases from PLN5.2bn to around PLN2.4bn as of the beginning of December 2010. Of PBG's backlog, more than PLN2.2bn constitutes gas&oil contracts, with the remaining PLN0.2bn attributable to small size power industry contracts. Given an estimated PLN1.7bn in revenue, PBG's backlog coverage of forward revenues will amount to 16 months compared with 19 and 29 months as of the beginning of 2010 and 2009, respectively.

In mid January, founder and CEO Jerzy Wisniewski sold 500,000 shares or 2.6% of equity in off-session transactions at PLN208.5 per share. No details regarding a reason for the sale or the use of the PLN104m cash proceeds were provided. After the transaction, the CEO's stake in PBG decreased to 26.1% in equity and 41.4% in voting rights. The disposal of shares is negative in our view, especially given PBG's high transparency and highly rewarded relations with its investors in the past.

PBG remains bullish for 2011. Latest management statements see net profit flat YoY. Given PLN220m net profit guidance in 2010 and our 2011F top line of PLN2.0bn translates into 10.7% net profit margin, but 12.9% if we exclude HBP and Aprivia from 1Q11 results. Since inception in 1994, PBG has never reported net profit margins in excess of 9%.

SELL maintained, with our DCF and peer valuation-based TP cut to PLN180. PBG trades at 2011/12F PER of 14.0/14.9x, in line with peers in 2011 but a double-digit premium for 2012F.

Price (14/01/11)	PLN209.0
	Previously PLN200.0
Target price (12-mth)	PLN180.0
Forecast total return	-13.2%

4Q10 preview

Revenue growth at 12.5% stemming primarily from intensification of gas&oil contracts, Wierzchowice and LMG. EBIT margin down to 10.1% from 14.0% in 4Q09 following a deterioration of profit margins at Hydrobudowa Polska due to a higher share in revenues of lower margined industrial construction contracts.

4Q10F results preview (21 March) (PLNm)

	4Q09	4Q10F
Revenue	926.9	1,041.5
EBITDA	141.8	115.8
EBIT	130.8	104.7
Net profit	101.5	83.2
EPS (PLN)	7.1	5.8

Source: Company data, ING estimates

Earnings drivers and outlook

Given the current backlog of only PLN1.8bn, we worry about the 2012F top line. PBG's key contracts, LNG terminal and LMG, secure almost PLN0.5bn of next year's revenues but the award of contracts in new segments, the power industry (alliance with Alstom for joint bidding both on gas and coal block tenders) and waste disposal plants, will be the driver behind future growth. In 2011 and 2012, the company wants to attract at least one contract in the power segment out of a total of PLN28bn and several in waste disposal plants (PLN6bn). In new businesses for PBG we expect a challenging 2012. Our current forecast sees 2011F net profit at PLN213m and a further decrease to PLN200m in 2012F. Our estimates are 11% below 2011F net profit market consensus of PLN240m and 23% lower than PLN260m consensus for 2012F. We do not include the potential positive book impact from the sale of HBP and Aprivia in our 2011F. Other operating income following that transaction might reach even tens of million PLN and would be booked in 2Q11.

Drivers of PBG's earnings and, simultaneously, the share price in the coming months will be the potential acquisition of listed power industry contractor, Energomontaz Poludnie (EPD PW; PLN3.75; NR), in which PBG holds a 25% stake and intends to gain the controlling interest but faces resistance from other shareholders. Alternatively, PBG wants to enter the power segment via the acquisition of a private company. The envisaged takeover of a company experienced in the power segment will in our view be crucial to investors' perception of PBG's ambitions in that segment. Among share price drivers, we also see 2011 guidance announcement scheduled for early 2Q11 and large contract signings in excess of PLN0.5bn.

Tomasz Czyz Warsaw +48 22 820 5046 tomasz.czyz@pl.ing.com

Newsflow

Date	Description
To be announced	

Source: Company data, ING

Major shareholders (%)

Jerzy Wisniewski	26.1
Pioneer mutual funds	14.4
ING pension fund	12.5
Aviva pension fund	8.7

Source: Company data, ING

Share data

Avg daily volume (3-mth)	28,064
Free float (%)	78.4
Market cap (PLNm)	2,987.7
Net debt (1F, PLNm)	316
Enterprise value (1F, PLNm)	3,513
Dividend yield (1F, %)	0.67

Source: Company data, ING estimates

Share price performance

Source: ING

Company profile

PBG is the largest Polish construction company, active in hydro engineering and gas & oil construction. In 2005-07, PBG acquired three companies active in environmental protection and is also constructing three stadiums for the UEFA Euro 2012 championships.

Risks

Risk factors remain a faster than expected award of a power block construction contracts, which might even double PBG's backlog with expectations of above-average profit margins in 2012 and 2013. EPS consensus for the coming two years would move up significantly as a result of the announcements.

Financials

Year end Dec (PLNm)	2007	2008	2009	2010F	2011F	2012F
Income statement						
Revenues	1,407	2,091	2,578	2,973	1,994	1,613
EBITDA	164	267	328	319	277	228
EBIT	139	226	286	277	249	212
Net interest	7	(10)	(24)	(6)	0	5
Associates	0	0	0	0	0	0
Other pre-tax items	0	0	0	0	12	25
Pre-tax profit	**146**	**216**	**263**	**271**	**261**	**241**
Tax	(27)	(26)	(41)	(48)	(47)	(41)
Minorities	(15)	(32)	(11)	(1)	0	0
Other post-tax items	0	0	0	0	0	0
Net profit	**104**	**158**	**211**	**226**	**213**	**200**
Normalised net profit	**104**	**158**	**211**	**226**	**213**	**200**
Balance sheet						
Tangible fixed assets	365	437	391	482	244	260
Intangible fixed assets	13	15	33	33	33	33
Other non-current assets	340	466	607	663	354	354
Cash & equivalents	410	290	660	725	899	770
Other current assets	1,131	1,651	2,318	2,371	1,270	1,085
Total assets	**2,259**	**2,859**	**4,008**	**4,274**	**2,800**	**2,502**
Short-term debt	467	671	642	500	400	200
Other current liabilities	675	663	1,181	1,325	700	529
Long-term debt	259	370	493	541	250	250
Other long-term liabilities	73	40	69	69	45	45
Total equity	785	1,114	1,623	1,839	1,405	1,477
Total liabilities & equity	**2,259**	**2,859**	**4,008**	**4,274**	**2,800**	**2,502**
Net working capital	540	1,031	1,182	1,106	509	433
Net debt (cash)	315	752	475	316	(249)	(320)
Cash flow						
Cash flow EBITDA	96	194	195	212	194	180
Tax, interest & other	(200)	(527)	(216)	23	549	39
Change in working capital	(16)	(147)	(210)	21	227	19
Net cash from op activities	(73)	(441)	(162)	309	1,018	274
Capex	(123)	(114)	15	(89)	210	(32)
Net acquisitions	0	0	0	0	0	0
Net financing cash flow	620	335	381	(83)	(1,005)	(175)
Dividends & minority distrib'n	0	0	0	(20)	(22)	(128)
Net ch in cash & equivalents	323	(303)	96	30	366	(122)
FCF	(195)	(556)	(147)	220	1,228	242
Performance & returns						
Revenue growth (%)	108.5	48.6	23.3	15.3	-32.9	-19.1
Normalised EPS growth (%)	64.4	50.4	29.6	2.0	-4.2	-6.1
Normalised EBITDA mgn (%)	11.6	12.8	12.7	10.7	13.9	14.1
Normalised EBIT margin (%)	9.9	10.8	11.1	9.3	12.5	13.1
ROACE (%)	12.3	12.3	11.7	9.8	10.1	10.6
Reported ROE (%)	18.6	18.9	18.1	14.7	14.3	14.5
Working capital as % of sales	38.4	49.3	45.9	37.2	25.5	26.9
Net debt (cash)/EBITDA (x)	1.9	2.8	1.4	0.99	(0.90)	(1.4)
EBITDA net interest cvg (x)	n/a	27.6	13.8	53.2	n/a	n/a
Valuation						
EV/revenue (x)	2.4	1.9	1.4	1.2	1.4	1.7
EV/normalised EBITDA (x)	20.4	14.7	11.2	11.0	10.1	12.0
EV/normalised EBIT (x)	24.0	17.4	12.9	12.7	11.3	12.9
Normalised PER (x)	26.7	17.7	13.7	13.4	14.0	14.9
Price/book (x)	3.7	3.0	2.1	1.8	2.2	2.1
Dividend yield (%)	0.0	0.0	0.0	0.67	0.75	4.3
FCF yield (%)	n/a	n/a	n/a	6.3	43.9	8.9
Per share data						
Reported EPS (PLN)	7.83	11.78	15.27	15.57	14.92	14.01
Normalised EPS (PLN)	7.83	11.78	15.27	15.57	14.92	14.01
Dividend per share (PLN)	0.00	0.00	0.00	1.40	1.57	8.95
Equity FCFPS (PLN)	(14.67)	(41.37)	(10.63)	15.39	85.89	16.94
BV/share (PLN)	55.90	69.11	97.61	114.0	94.09	99.15

Source: Company data, ING estimates