KBC Securities

PBG

23 February 2012

Over-leveraged

Construction		**Current price**	PLN 72.00*	**Sell**
Poland		**Fair value**	PLN 60.42	Rating downgraded

Performance over	1M	3M	12M
Absolute	-6%	-3%	-64%
Rel. WIG20	-14%	-15%	-37%
12M Hi/Lo	PLN 205 / 56.1		

Reuters	PBGG.WA
Bloomberg	PBG PW
Market cap	€ 246.8m
Next corporate event	
4Q11 results on 29 February 2012	
PLN / EUR	4.17

PLN m	2010	2011F	2012F	2013F
Sales	2,740.3	3,401.5	4,386.7	4,469.0
EBITDA	319.4	298.4	310.1	396.0
EBIT	272.7	250.6	241.1	319.1
Net profit	224.3	206.1	130.5	184.2
EPS (PLN)	15.7	13.5	9.1	12.9
P/E (x)	4.6	5.0	7.9	5.6
DPS (PLN)	1.4	1.4	0.0	4.2
Dividend Yield (%)	1.9%	1.9%	0.0%	5.8%
EV/EBITDA (x)	5.3	8.8	9.1	7.1

Source: KBC Securities ** Priced at COB 22 February 2012*

PBG is scheduled to leave the WIG20 index after the session on 16 March 2012. We expect this negative trading news to put a drag on the share price in the weeks ahead. We see the acquisition of energy-oriented Rafako and Energomontaz as a wise move as it will secure the backlog over the long term, although the influence will be limited in the short and medium term. Meanwhile, PBG is likely to struggle with high debt and another capital-intensive year of road deals. We have cut our underlying net profit forecasts by 38.6% to PLN 130.5m for 2012 and 31.2% to PLN 184.2m for 2013. Our fair value of PLN 60.42 per share implies 16.1% downside. We downgrade our rating to Sell.

Rating downgraded to Sell

- **Leaving the WIG20:** The Warsaw Stock Exchange plans to replace PBG and financial group Getin Holding with car parts producer Boryszew and chemicals group Synthos in its blue-chip WIG20 index. PGB and Getin will in turn replace Boryszew and Synthos on the bourse's mWIG40 index. The switch will take place on 16 March 2012. We expect the change to put a significant drag on PBG's share price in the weeks ahead.
- **Limited growth possibilities in key segments:** As the Wierzchowice and LMG contracts taper off towards end-1H12 and end-2012, we expect the portion of PBG's revenues from high margin oil & gas contracts to drop from 23.3% in 2011 to 13% in 2012. Instead the company will book a record-high participation in road contracts (37.3% of sales, gross margin of 3%). While we acknowledge the leap the Rafako and Energomontaz acquisitions represent in terms of PBG's exposure to the energy segments, the EBIT margins of both firms are significantly lower than those of PBG group: 4.5% at Rafako, -3.1% at Energomontaz versus 7.4% at PBG in 2011F.
- **Extreme gearing:** The high leverage connected to the financing of road contracts (record high 37.3% of revenues expected from roads in 2012) as well as the Rafako and Energomontaz acquisitions will weigh on PBG's financials in the medium term. On the back of Alstom's claim to Rafako, we expect PBG's net debt/EBITDA ratio to stand at an extreme 5.9x as of end-2012 before declining to 4.4x in 2013 as road contracts finally taper-off. We do not factor in any asset disposals in 2012, which could potentially smooth these ratios.
- **No dividend on the horizon:** According to PBG's deputy CEO and CFO Mr Szkudlarczyk in a recent interview with PAP, the management is likely to recommend that shareholders leave 2011 net profit in the firm. This seems to be justified as we expect PBG to record negative operating cash flow in 2012 as the firm is still bogged down with road contracts and the Opole contract might not influence the P&L and OCF in 2012 as the market expects. We expect revenues at a mere PLN 30m and no significant prepayments connected to the Opole deal in 2012.
- **Discount valuation:** A 2012F P/E of 7.9x puts PBG at a 30.7% discount to domestic peers. We see the discount as justified by the firm's high financial gearing and falling exposure to the high-margin oil & gas segment, which will be replaced by the low margin road segment in 2012. Also, the performance of the energy segment is blurred by delays in the Opole contract, the restructuring story at Energomontaz and Alstom's PLN 135m claim on Rafako.

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Important Polish Disclosure

Belgian Banking and Finance Commission is exercising the Supervision over KBC Securities NV Branch in Poland.
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The definitions of terms applied in the publication:

EBITDA = EBIT + amortization and depreciation

EPS = Net profit / No of shares outstanding

DPS = Dividend per Share

NBV per share = Net Book Value / No of shares outstanding

EBITDA margin = EBITDA / Revenue

EBIT margin = EBIT / Revenue

CFPS = Cash flow / No of shares outstanding

Net Financial Debt = Financial debt – Cash equivalents

ROE = Net profit / Average Equity

EV = Market Capitalization + Net Financial Debt

P/E = Stock Price / EPS

P/CF = Stock Price / (Net Profit + amortization and depreciation)

P/BV = Stock Price / NBV per share

P/S = Market Capitalization / Revenue

Gross Dividend Yield = Dividend per share / Stock

List of recent recommendations concerning PBG shares issued by KBC Securities NV Branch in Poland

Date of issue	Valuation	Market price	Recommendation
22 January 2010	Buy	219.0	245.3
26 April 2010	Buy	218.0	247.0
09 September 2010	Hold	250.2	261.64
08 October 2010	Buy	241.0	273.50
21 February 2011	Hold	201.5	215.60
20 May 2011	Buy	142.0	171.45
23. February 2012	Sell	72.0	63.81

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During the last quarter KBC Securities NV Branch in Poland issued 48 recommendations:

19 BUY	40%
19 HOLD	40%
10 SELL	20%

The views expressed in this publication accurately reflect the personal view of the authors, in accordance with the state in time of the preparation.

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