# PBG

**Poland, Construction**

Reuters: PBGG.WA Bloomberg: PBG PW

**24 August 2004**

# Upbeat prospects become reality

## Initiating coverage with Accumulate rating and TP of PLN 42.8 per share

PBG's shares offer a unique exposure to both the inflow of EU structural funds to Poland as well as a booming market in gas engineering facilities. We expect the company, which is now flush with PLN 96m in IPO capital, to record a CAGR of 27% in EPS between 2003 and 2006. We initiate coverage of PBG with an Accumulate rating and target price of PLN 42.8 per share.

We expect PBG to nearly double its sales in the hydro-construction segment in 2005, to PLN 90m. The company has placed offers totalling PLN 1.8bn in tenders financed by EU pre-accession funds, the completion of which is expected by year-end in most cases. A new set of tenders, to be launched in autumn, is likely to further augment the company's exposure to these lucrative growth opportunities.

Additionally in 2004, PBG intends to bid for projects in the area of oil and gas engineering, the combined value of which amounts to app. US$ 60m. The company's strong expertise and track record in the respective market segment allows us to assume a 50% success ratio and more than 50% increase in PBG's sales to the sector in 2005.

Taking into account the recent IPO proceeds incorporation in PBG's financial statements, as well as a 49% y/y increase in backlog to PLN 164m ytd, and the company's current ability to execute more projects we raise our earnings estimates 15% to PLN 18.6m for 2004 and 45% to PLN 29.8m for 2005. We expect a CAGR of 27% in EPS between 2003 and 2006.

PBG's shares trade at 2004E and 2005E P/E ratios of 18.7x and 13.8x, respectively, vs. the average of 15.1x and 13.8x as recorded for the European construction companies. Using a DCF model and our revised forecasts, we arrive at PBG's current fair value of PLN 41.2 per share. We issue an Accumulate recommendation on the stock with a target price of PLN 42.8 at the end of 2004, 9% above the current market price.

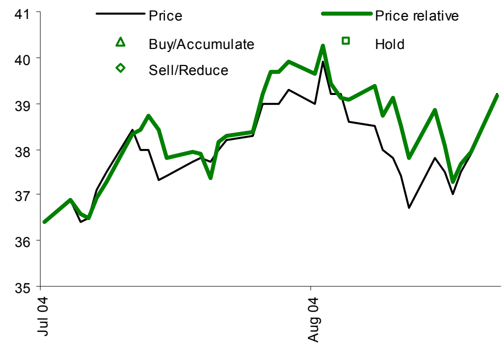
**PBG: Financial summary**

*PLN in millions, unless otherwise stated*

| | 2002 | 2003 | 2004E | 2005E | 2006E |
|---|---|---|---|---|---|
| Sales | 162.1 | 180.7 | 213.2 | 302.5 | 337.4 |
| EBITDA | 14.4 | 21.0 | 29.9 | 43.7 | 48.0 |
| EBIT | 9.2 | 14.3 | 23.3 | 35.1 | 39.2 |
| Net profit | 4.6 | 11.3 | 18.6 | 29.8 | 33.8 |
| EPS (PLN) | 0.64 | 1.57 | 2.10 | 2.83 | 3.21 |
| P/E (x) | 61.0 | 25.0 | 18.7 | 13.8 | 12.2 |
| EV/EBITDA (x) | 27.1 | 18.6 | 13.0 | 8.9 | 8.1 |

*Source: Company data, DM BZ WBK estimates*

| Recommendation | Accumulate |
|---|---|
| Price (PLN, 23 August 2004) | 39.2 |
| Fair value (PLN, current) | 41.2 |
| Target price (PLN, year-end 2004) | 42.8 |
| Market cap. (PLN m) | 412.8 |
| Enterprise value (PLN m) | 389.5 |
| Free float (%) | 31.6 |
| Number of shares (m) | 10.5 |
| Average daily turnover 3M (shares) | 22,741 |
| EURPLN | 4.43 |
| USDPLN | 3.63 |




The price relative chart measures performance against the WIG 20 index. On 23/08/04 the WIG 20 index closed at 1702.77.

| | Price | Performance | |
|---|---|---|---|
| | | absolute | relative |
| 1 month | 38.2 | 3.2% | 2.7% |
| since debut | 36.4 | 7.7% | 7.6% |
| since IPO | 32.0 | 22.5% | 21.2% |

O – Outperform, N –Neutral, U – Underperform, B – Buy, A – Accumulate, H – Hold, R – Reduce, S – Sell
DM BZ WBK changed its rating system from relative to absolute recommendations on July 15, 2004.

| Main shareholders | % of voting rights |
|---|---|
| Jerzy Wisniewski | 52.2 |
| Malgorzata Wisniewska | 14.0 |
| Marek Grunt | 8.8 |
| Tomasz Woroch | 4.4 |

**Company description**

PBG provides engineering and construction services in the area of oil and gas production and transmission as well as hydro-construction

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# Investment summary

***An unique exposure on the inflow of EU structural funds and booming market of gas engineering facilities***

PBG's shares offer a unique exposure to the inflow of EU structural funds supporting development of water systems in Poland as well as to a booming market in gas engineering facilities. In this report we present our updated forecast for PBG, incorporating into our models the company's recent capital increase of PLN 96m through an IPO on the WSE as well as taking into account the company's current ability to participate in and execute an increased number of projects.

***PBG placed offers worth in total PLN 1.8bn in UE financed hydro-construction tenders…***

Poland's accession to the EU has given a boost to the Polish market of water and sewage systems construction. The value of currently ongoing tenders in the area of hydro-construction that are set to be financed by EU pre-accession funds amounts to PLN 1.8bn and PBG has its offers placed in all of them. We expect the company to succeed in 10% of tendered projects in value terms and nearly double its revenues from the sector in 2005 to PLN 90m. What is notable is that we do not expect a slowdown in the market of water and sewage systems construction in 2005-06, as a new set of tenders, financed by EU funds, is likely to be launched in autumn.

***…and will bid for US$ 60m contracts in oil and gas engineering***

In 2004, PBG has already, or intends to place its offer in six sizeable tenders in the area of oil and gas engineering, the combined value of which the company estimates at US$ 60m. This includes four gas plants (Gorzyca, Zielin, Paproc I and Paproc II), the Odolanow gas compressor, and a nitrogen rejection unit in Grodzisk. The company's strong expertise and track record in the respective market segment allows us to assume a 50% success ratio and above 50% y/y surge in revenues from oil and gas engineering facilities construction in 2005.

***Wierzchowice behind schedule, but still likely***

With a net cash position of PLN 23m as of the end of June, PBG is fully prepared to compete for two oil and gas engineering mega-projects that are likely to be launched next year: Wierzchowice underground gas storage construction (US$ 100m) and Miedzychod oil plant construction (US$ 100m). The former was supposed to be launched yet in 2004; however, a change in structure of the project's financing put it behind schedule. We believe the Wierzchowice project will set off in 2005 and PBG will be among the top leaders to execute it. Moreover, PBG's plans of further development do not exclude acquisition or involvement in BOT (Build Operate Transfer) projects.

***We expect PBG to record CAGR of 27% in EPS between 2003 and 2006***

Having incorporated IPO proceeds into PBG's financial statements, a 49% y/y increase in backlog to PLN 164m as of now, as well as taking into account the company's current ability to execute more projects we raise our earnings estimates. We nudge up our 2004 revenues and EBIT estimates 8% to PLN 213.2m and 3% to PLN 23.3m, respectively. As for 2005's figures, we raise our revenues forecast 21% to PLN 302.5m and net profit forecast 45% to PLN 29.8m. We expect PBG to record a CAGR of 23% in sales and 27% in EPS between 2003 and 2006.

***We issue Accumulate recommendation on PBG with target price of PLN 42.8 at the end of 2004***

PBG's shares trade at 2004E and 2005E P/E ratios of 18.7x and 13.8x, respectively, vs. the average of 15.1x and 13.8x as recorded for the European construction companies. Using a DCF model and our revised forecasts, we arrive at PBG's current fair value of PLN 41.2 per share. We issue an Accumulate recommendation on the stock with a target price of PLN 42.8 at the end of 2004, 9% above the current market price.

# Valuation

### Peer comparison

*PBG trades in line with its European peers on 2005E P/E basis…*

Western European engineering companies trade at an average 2005E P/E ratio of 15.8x, and European construction stocks at an average multiple of 13.0x. The average in the whole sample amounts to 13.8x.

PBG, with 2005E P/E of 13.8x, trades exactly in line with its European peer group. However, the comparison of EPS growth rates between 2003 and 2005 (34.3% for PBG vs. a mere 5.5% among European construction stocks) suggests that a higher valuation for PBG would be justified.

*…and at 52% discount to Budimex*

We also compared PBG to its domestic sector peer – Budimex, trading at 2005E P/E of 29.0x. In this case PBG's stock represents a discount of 52%.

**Figure 1. PBG: Comparable valuation: European peers**

| Company | Country | Price | P/E (x) | | | 2003-2005 EPS |
|---|---|---|---|---|---|---|
| | | (local) | 2003 | 2004E | 2005E | CAGR (%) |
| **Engineering/Construction** | | | | | | |
| Technip | France | 122.4 | -145.7 | 122.4 | 46.2 | nm |
| Wood Group | GB | 1.2 | 22.1 | 19.2 | 15.8 | 18.1% |
| Saipem | Italy | 8.6 | 19.2 | 19.1 | 17.5 | 4.9% |
| ABB (ADR US) | Switzerland | 5.5 | -8.7 | 26.5 | 14.4 | nm |
| AMEC | GB | 3.1 | 15.0 | 14.7 | 12.9 | 5.5% |
| **Mediana** | | | **15.0** | **19.2** | **15.8** | **5.5%** |
| **General construction** | | | | | | |
| NCC | Sweden | 76.8 | -18.7 | 13.7 | 13.5 | nm |
| Skanska | Sweden | 65.0 | 9.8 | 14.4 | 13.0 | -13.1% |
| MOWLEM | GB | 1.7 | 6.5 | 14.1 | 9.0 | -15.4% |
| ACS | Spain | 13.8 | 13.8 | 10.8 | 9.5 | 11.7% |
| Acciona | Spain | 49.9 | 16.3 | 15.4 | 14.1 | 7.4% |
| Ferrovial | Spain | 37.1 | 15.5 | 15.9 | 14.6 | 3.0% |
| Vinci | France | 88.0 | 13.6 | 12.7 | 11.9 | 6.7% |
| Hochtief | Germany | 18.8 | 72.2 | 35.4 | 20.9 | 86.1% |
| Bilfinger Berger | Germany | 27.7 | 8.0 | 14.2 | 12.5 | -19.8% |
| **Median** | | **-** | **11.9** | **14.2** | **13.0** | **4.9%** |
| **Median total** | | **-** | **12.7** | **15.1** | **13.8** | **5.5%** |
| **PBG** | | **39.2** | **25.0** | **18.7** | **13.8** | **34.3%** |
| *PBG's Premium/(Discount)* | | - | *97%* | *24%* | *0%* | - |
| Budimex | | 43.5 | 23.8 | 72.5 | 29.0 | -6.0% |
| *PBG's Premium/(Discount)* | | - | *5%* | *-74%* | *-52%* | - |

*Source: Bloomberg, I/B/E/S, DM BZ WBK estimates*

## DCF

*Our DCF analysis implies PBG's fair equity value at PLN 41.2 per share*

We based our DCF model on the following assumptions:

- We forecast PBG's sales to grow at a CAGR of 11.8% between 2003 and 2013. As in our previous note, we arrive at this through explicit bottom-up forecasts for 2004-2006 and assume growth in line with nominal GDP thereafter.
- Keeping our assumptions as to PBG's gross margin largely intact, we reduced our long-term forecast of SG&A costs from 12.8% of sales to 12.0%. In 1H04 PBG surprised as positively with a 30% decline in its SG&A costs to 11.8% of sales (from 24.8% in 1H04) resulting from the Hydrobudowa Wloclawek divestiture.
- We estimate PBG's WACC at 9.7%, based on 11.8% cost of equity, 6.5% after tax cost of debt and 39% debt to capital ratio. Please see figure 2 for detailed calculations.
- We calculate the terminal growth rate based on the formula: terminal growth rate = reinvestment rate X return on invested capital (see figure 3). An increase in forecasted EBIT margin (result of lower SG&A costs) lifts our ROIC forecast to 25.6% and terminal growth rate from 2.5% to 3.5%.

**Our DCF analysis implies PBG's fair equity value at PLN 41.2 per share and sets a target price of PLN 42.8 at the end of 2004.**

**Figure 2. PBG: WACC calculation**

| | |
|---|---|
| Risk free rate (10-year Polish T-bond yield) | 7.0% |
| Unlevered beta* | 0.70 |
| Levered beta | 1.07 |
| Equity risk premium | 4.5% |
| **Cost of equity** | **11.8%** |
| Risk free rate (10-year Polish T-bond yield) | 7.0% |
| Debt risk premium | 1.0% |
| Tax rate | 19% |
| **After tax cost of Debt** | **6.5%** |
| % Debt | 39% |
| % Equity | 61% |
| **WACC** | **9.7%** |

**European construction stocks, January 2004, Bloomberg. Source: Bloomberg, Company data, DM BZ WBK estimates*

**Figure 3. PBG: Terminal growth rate calculation**
*PLN in millions, unless otherwise stated*

| | Value | Comment |
|---|---|---|
| NOPAT (t+1) | 50 | EBIT less adjusted taxes |
| Net investment | 7 | Net capex + chge in WC |
| Reinvestment rate (RR) | 13.5% | Net investment/NOPAT |
| ROIC | 25.6% | NOPAT/Invested Capital |
| **FCF growth rate (g)** | **3.5%** | **RR*ROIC** |

*Source: DM BZ WBK estimates*

**Figure 4. PBG: DCF valuation**
*PLN in millions, unless otherwise stated*

| | 2004E | 2005E | 2006E | 2007E | 2008E | 2009E | 2010E | 2011E | 2012E | 2013E |
|---|---|---|---|---|---|---|---|---|---|---|
| **Net sales** | **213** | **303** | **337** | **363** | **391** | **418** | **448** | **480** | **514** | **550** |
| EBIT | 23 | 35 | 39 | 40 | 43 | 46 | 50 | 53 | 56 | 60 |
| Cash taxes on EBIT | 4 | 7 | 7 | 8 | 8 | 9 | 9 | 10 | 11 | 11 |
| **NOPAT** | **19** | **29** | **32** | **33** | **35** | **38** | **40** | **43** | **45** | **48** |
| Depreciation | 7 | 9 | 9 | 8 | 9 | 11 | 13 | 16 | 18 | 20 |
| Change in operating WC | 6 | 16 | 6 | 5 | 5 | 5 | 5 | 6 | 6 | 7 |
| **Capital expenditure** | **11** | **15** | **17** | **18** | **19** | **19** | **20** | **20** | **21** | **20** |
| Net investment | 10 | 23 | 14 | 15 | 14 | 13 | 12 | 10 | 9 | 7 |
| **Free cashflow** | **9** | **6** | **18** | **18** | **21** | **25** | **29** | **33** | **37** | **42** |
| WACC | 9.7% | | | | | | | | | |
| PV FCF 2004-2013 | 129 | | | | | | | | | |
| Terminal growth rate | 3.5% | | | | | | | | | |
| Terminal Value (TV) | 690 | | | | | | | | | |
| PV TV | 273 | | | | | | | | | |
| Total EV (1 January 2004) | 402 | | | | | | | | | |
| **Total EV (1 July 2004)** | **421** | | | | | | | | | |
| Net debt (1 July 2004) | -23 | | | | | | | | | |
| **Equity value (1 July 2004)** | **425** | | | | | | | | | |
| Number of shares (m) | 10.5 | | | | | | | | | |
| Value per share (1 July 2004, PLN) | 40.4 | | | | | | | | | |
| Month | August | | | | | | | | | |
| **Current value per share (PLN)** | **41.2** | | | | | | | | | |
| **Value per share at end 2004 (PLN)** | **42.8** | | | | | | | | | |
| **Growth rates** | | | | | | | | | | |
| Revenue growth | 18.0% | 41.9% | 11.5% | 7.6% | 7.6% | 7.1% | 7.1% | 7.1% | 7.1% | 7.1% |
| EBIT growth | 62.7% | 51.0% | 11.5% | 3.0% | 7.6% | 7.1% | 7.1% | 6.2% | 6.1% | 6.1% |
| NOPAT growth | 88.1% | 51.0% | 11.5% | 3.0% | 7.6% | 6.9% | 7.0% | 6.2% | 6.1% | 6.1% |
| FCF growth | -78.2% | -31.3% | 193.8% | 1.1% | 17.2% | 19.2% | 15.9% | 13.4% | 12.4% | 13.7% |
| **Margins and ratios** | | | | | | | | | | |
| EBIT margin | 10.9% | 11.6% | 11.6% | 11.1% | 11.1% | 11.1% | 11.1% | 11.0% | 10.9% | 10.8% |
| Nopat margin | 8.9% | 9.4% | 9.4% | 9.0% | 9.0% | 9.0% | 9.0% | 8.9% | 8.8% | 8.8% |
| Capex/Revenues | 5.2% | 5.0% | 5.0% | 5.0% | 4.8% | 4.6% | 4.4% | 4.2% | 4.0% | 3.5% |
| Change in WC/Revenues | 2.7% | 5.3% | 1.9% | 1.3% | 1.3% | 1.2% | 1.2% | 1.2% | 1.2% | 1.2% |
| Change in WC/Change in revenues | 17.9% | 17.9% | 17.9% | 17.9% | 17.9% | 17.9% | 17.9% | 17.9% | 17.9% | 17.9% |

*Source: DM BZ WBK estimates*

# Medium term growth drivers

### Hydro-construction: EU financing gives sector a boost

***A necessity to consume pre-accession EU funds sparked a boom in hydro-construction***

Over the last couple of months Poland's hydro-construction sector witnessed a huge increase in number of announced tenders. Such a development was sparked by a necessity to launch projects that would consume EU pre-accession funds (mainly ISPA). A majority of announced tenders is likely to be finalized by end of the year.

***PBG placed offers worth a total of PLN 1.8bn…***

PBG, in a consortium with Hydrobudowa Wloclawek, succeeded in two sizable tenders to date, which are set to generate for PBG revenues of EUR 5.8m (PLN 25.7m). Moreover, the company placed its offer in other tenders, the total value of which amounts to EUR 399m (PLN 1.8bn). PBG expects most tender winners to be announced by autumn, with the deadline for signing the contracts at the end of the year.

***…of which we expect the company to secure for itself some 10%***

We expect PBG to secure for itself some 10% of the contracts it bids for in value terms. This implies the company will secure contracts worth app. 180m, with average execution time lasting untill mid 2007.

***We do not expect any slowdown in hydro-construction in Poland in 2005-06***

Notably, we do not expect a slowdown in the market of water and sewage systems construction in 2005-06, as a new set of tenders, financed by EU funds, is likely to be launched in autumn.

### Oil and gas production and engineering facilities

***PBG declares to bid for 6 projects…***

Currently we have more clarity with regards to the specific projects PBG declares it will bid for in the area of oil and gas production and engineering facilities. All these projects Polish Oil and Gas Company (PGNiG) is set to launch next year, with the procurement procedures being completed yet in 2004.

***…worth in total US$ 60m***

Specifically, PBG already has, or intends to place its offer in six sizeable tenders, the combined value of which the company estimates at US$ 60m. This includes four gas plants (Gorzyca, Zielin, Paproc I and Paproc II), the Odolanow gas compressor, and a nitrogen rejection unit in Grodzisk. For details please look at the following figure.

**Figure 5. Oil and gas production and engineering facilities tenders PBG declares to bid for**

| Project | Value (US$ m) |
|---|---|
| Grorzyca gas plant | 6 |
| Zielin gas plant | 6 |
| Paproc I gas plant | 6 |
| Paproc II gas plant | 3 |
| Odolanow gas compressor | 4 |
| Nitrogen rejection unit in Grodzisk | 36 |
| **Total** | **60** |

*Source: Company data, DM BZ WBK estimates*

***We expect 50% success ratio in oil and gas tendered projects***

We expect PBG to succeed in 50% of the above-described tenders in value terms, or secure contracts worth app. US$ 30m to be executed by mid 2006. Although a 50% success ratio may seem overly optimistic, we believe it to be feasible due to PBG's strong track record in gas plant construction (the company constructed Poland's largest gas plant in Koscian) as well as unique expertise in other engineering facilities and access to modern technology.

### Mega-tenders: Wierzchowice and Miedzychod

***We are likely to witness completion of two mega-tenders next year: Wierzchowice gas storage and Miedzychod oil plant***

In addition to the tenders we detailed in the preceding paragraphs, there are two large-scale projects that PBG is likely to participate in: Wierzchowice gas storage facility and Miedzychod oil plant. The value of each project amounts to app. US$ 100m. We do not include the two tenders into our forecasts, although we believe that PBG has strong credentials to participate in them. However, it has been traditional to observe significant delays in the completion of tenders of this size.

- Wierzchowice gas storage facility

  Unlike what we had expected, the US$ 100m tender for the construction of Wierzchowice underground gas storage facility was not completed, but rather cancelled. This is due to the fact that PGNiG decided to execute the project through a joint-venture with a partner providing financing, versus the original intention of financing the project using its own balance sheet only. We expect the project to be launched next year and PBG to be among the top choices to execute it.

- Miedzychod oil plant

  Miedzychod crude oil plant is yet another sizeable project that PBG has declared its intention to tender for. According to the company, PGNiG intends to launch the construction of the crude oil plant in Miedzychod in 2005, with the whole project value estimated at US$ 100m and an execution time of three years.

# 2Q04 review

***PBG doubled its sales in 2Q04 to PLN 43.8m…***

PBG posted a very sound set of second quarter results. The company's sales doubled to PLN 43.8m in 2Q04, bringing the year to date figure to PLN 60.6m. PBG's major sales drivers in 1H were contracts for the construction works at Bronsko gas field and Szamotuły gas compressing facility.

***…posted sound EBIT of PLN 4.0m…***

At the EBIT level PBG reported a profit of PLN 4.0m in 2Q04 vs. a loss of 0.2m in the corresponding period a year ago and PLN 2.6m in 1Q04. The improvement in PBG's operating performance was due to higher sales and reduction in SG&A costs, which surprised us positively. In 2Q04 PBG reduced its SG&A costs 24% y/y to PLN 4.1m.

***…and net profit of PLN 3.1m***

At the bottom line, PBG posted a net profit of PLN 3.1m in 2Q04 vs. a loss of PLN 1.8m in 2Q03. Year to date the company reported net earnings of PLN 3.5m vs. our revised FY2004 estimate of PLN 18.6m.

**Figure 6: PBG: 2Q04 results**
*PLN in millions, unless otherwise stated*

| | 2Q04 | 2Q03 | %, y/y | 1H04 | 1H03 | %, y/y |
|---|---|---|---|---|---|---|
| **Sales** | **43.8** | **21.9** | ***100%*** | **60.6** | **40.9** | ***48%*** |
| COGS | 34.8 | 16.4 | *112%* | 47.6 | 32.7 | *46%* |
| **Gross profit** | **9.0** | **5.5** | ***63%*** | **12.9** | **8.2** | ***59%*** |
| *Gross margin (%)* | *20.5%* | *25.1%* | - | *21.4%* | *20.0%* | - |
| SG&A costs | 4.1 | 5.4 | *-24%* | 7.1 | 10.2 | *-30%* |
| Other operating income, net | -0.9 | -0.3 | *nm* | 0.8 | -0.4 | *nm* |
| **EBIT** | **4.0** | **-0.2** | ***nm*** | **6.6** | **-2.4** | ***nm*** |
| *EBIT margin (%)* | *9.1%* | *-1.1%* | - | *10.9%* | *-5.9%* | - |
| Net financial costs | -1.0 | -1.4 | *nm* | -1.7 | -1.7 | *nm* |
| Goodwill amortisation, net | 0.1 | 0.1 | *-36%* | 0.1 | 0.3 | *-68%* |
| **Pre-tax profit** | **2.9** | **-1.8** | ***nm*** | **4.9** | **-4.4** | ***nm*** |
| Tax | 0.3 | 0.0 | *nm* | 1.5 | -1.2 | *nm* |
| Income form associates and minorities interest | 0.4 | 0.0 | *nm* | 0.2 | 0.0 | *nm* |
| **Net profit** | **3.1** | **-1.8** | ***nm*** | **3.5** | **-3.2** | ***nm*** |

*Source: Company data*

# Forecast revision

***We upgrade our 2005E forecast for PBG…***

We have updated earnings forecasts for PBG, incorporating into our model the capital increase, the company's increase ability to execute more contracts as well as recent industry developments.

***…raising sales 21% to 302.5m…***

We upgrade our 2004 and 2005 sales forecasts 8% to PLN 213.2m and 21% to 302.5m, respectively. PBG's current backlog of PLN 164.2m (including already invoiced contracts) is 49% above the figure recorded in August 2003 (PLN 110m) vs. 27% as recorded in June. As for 2005, we increase the company's revenues forecast in hydro-construction to PLN 92m from PLN 50m and in oil and gas engineering to PLN 92m from PLN 81m. In both cases our rational is that PBG, supplied with new capital, is currently able to participate, win and execute more contracts.

***…EBIT 26% to PLN 35.1m…***

In 1Q04 PBG surprised us positively with a 30% decline in its SG&A costs to 11.8% of sales (from 24.8% in 1H04), resulting from the Hydrobudowa Wloclawek divestiture. Given this we decrease our SG&A costs forecast from 12.8% to 12% and consequently lift our EBIT margin assumptions to 11.6% from 11.1% in the 2005-06 period. We nudge up our 2004 EBIT forecast 3% to PLN 23.3m and 2005's 26% to PLN 35.1m.

***…and net profit 45% to PLN 29.8m***

We increase our net profit forecast for PBG 15% to PLN 18.6m in 2004 and 45% to PLN 29.8m in 2005. Increased operating earnings and a reduction in net interest costs both attributed to this.

**Figure 7. PBG: Earnings forecast revision**
*PLN in millions, unless otherwise stated*

| | 2002 | 2003 | 2004E | | | 2005E | | | 2006E | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | new | old | *% change* | new | old | *% change* | new | old | *% change* |
| Revenues | 162.1 | 180.7 | 213.2 | 198.2 | *8%* | 302.5 | 249.1 | *21%* | 337.4 | 274.4 | *23%* |
| *EBIT margin (%)* | *5.7%* | *7.9%* | *10.9%* | *11.4%* | - | *11.6%* | *11.1%* | - | *11.6%* | *11.1%* | - |
| EBIT | 9.2 | 14.3 | 23.3 | 22.7 | *3%* | 35.1 | 27.8 | *26%* | 39.2 | 30.5 | *29%* |
| Net profit | 4.6 | 11.3 | 18.6 | 16.1 | *15%* | 29.8 | 20.6 | *45%* | 33.8 | 23.4 | *45%* |

*Source: DM BZ WBK estimates*

# Financial statements

**Figure 8. PBG: Income statement forecasts**
*PLN in millions, unless otherwise stated*

| | 2001 | 2002 | 2003 | 2004E | 2005E | 2006E |
|---|---|---|---|---|---|---|
| **Net sales** | **120.4** | **162.1** | **180.7** | **213.2** | **302.5** | **337.4** |
| COGS | 95.8 | 132.9 | 142.2 | 164.2 | 229.9 | 256.5 |
| Depreciation | 3.5 | 5.2 | 6.7 | 6.6 | 8.6 | 8.9 |
| **Gross profit** | **24.6** | **29.3** | **38.5** | **49.0** | **72.6** | **81.0** |
| SG&A | 10.6 | 18.9 | 23.0 | 25.6 | 36.3 | 40.5 |
| Other operating income, net | 0.0 | -1.2 | -1.2 | -0.2 | -1.2 | -1.3 |
| **EBITDA** | **17.5** | **14.4** | **21.0** | **29.9** | **43.7** | **48.0** |
| **Operating profit** | **14.0** | **9.2** | **14.3** | **23.3** | **35.1** | **39.2** |
| Net financial costs (income) | 2.0 | 4.4 | -0.1 | 0.2 | -1.9 | -2.8 |
| interest income | 1.1 | 2.4 | 1.5 | 3.2 | 4.1 | 4.3 |
| interest costs | 4.0 | 6.1 | 6.4 | 3.4 | 2.2 | 1.5 |
| other financial costs (income) | -0.9 | 0.7 | -4.9 | 0.0 | 0.0 | 0.0 |
| Goodwill amortisation, net | 0.0 | 0.4 | 0.6 | 0.3 | 0.4 | 0.4 |
| **Profit before tax** | **12.0** | **4.4** | **13.8** | **22.8** | **36.6** | **41.5** |
| Income tax | 4.0 | -0.4 | 2.9 | 4.3 | 7.0 | 7.9 |
| Income from associates and minority interest | 0.0 | -0.2 | 0.5 | 0.1 | 0.1 | 0.2 |
| **Net profit** | **8.0** | **4.6** | **11.3** | **18.6** | **29.8** | **33.8** |
| Gross margin | 20.4% | 18.1% | 21.3% | 23.0% | 24.0% | 24.0% |
| EBITDA margin | 14.5% | 8.9% | 11.6% | 14.0% | 14.4% | 14.2% |
| Operating margin | 11.6% | 5.7% | 7.9% | 10.9% | 11.6% | 11.6% |
| Pre-tax margin | 10.0% | 2.7% | 7.6% | 10.7% | 12.1% | 12.3% |
| Net margin | 6.7% | 2.9% | 6.3% | 8.7% | 9.9% | 10.0% |
| Sales growth | n.a. | 34.7% | 11.4% | 18.0% | 41.9% | 11.5% |
| Gross profit growth | n.a. | 19.1% | 31.3% | 27.5% | 48.1% | 11.5% |
| EBITDA growth | n.a. | -17.8% | 46.0% | 42.3% | 46.2% | 10.0% |
| Operating profit growth | n.a. | -34.3% | 55.6% | 62.7% | 51.0% | 11.5% |
| Net profit growth | n.a. | -42.4% | 144.3% | 64.4% | 60.5% | 13.4% |

*Source: Company data, DM BZ WBK forecasts*

**Figure 9. PBG: Cash flow statement forecasts**
*PLN in millions, unless otherwise stated*

| | 2002 | 2003 | 2004E | 2005E | 2006E |
|---|---|---|---|---|---|
| **Cash flow from operations** | **-6.2** | **27.4** | **19.2** | **19.4** | **35.3** |
| Net profit | 4.6 | 11.3 | 18.6 | 29.8 | 33.8 |
| Provisions | 4.6 | -3.7 | 1.5 | 1.7 | 0.7 |
| Depreciation and amortisation | 5.2 | 6.7 | 6.6 | 8.6 | 8.9 |
| Changes in WC, o/w | -1.4 | 14.1 | -3.5 | -9.5 | -3.7 |
| inventories | -2.8 | 2.4 | -0.4 | -1.2 | -0.5 |
| receivables | -23.2 | 5.7 | -11.2 | -30.6 | -12.0 |
| payables | 24.6 | 6.0 | 8.1 | 22.3 | 8.7 |
| Other, net | -19.2 | -1.1 | -4.1 | -11.2 | -4.4 |
| **Cash flow from investment** | **-48.5** | **13.4** | **-8.2** | **-1.2** | **-14.1** |
| Additions to PPE and intangibles | -42.2 | 16.9 | -11.0 | -15.1 | -16.9 |
| Change in long-term investments | -0.6 | -16.6 | 3.2 | 10.2 | 1.1 |
| Other, net | -5.8 | 13.1 | -0.4 | 3.7 | 1.7 |
| **Cash flow from financing** | **59.2** | **-35.3** | **69.9** | **-10.0** | **-10.0** |
| Change in long-term borrowing | 34.5 | -18.4 | 0.0 | -10.0 | -10.0 |
| Change in short-term borrowing | 13.0 | -1.8 | -25.0 | 0.0 | 0.0 |
| Change in equity and profit distribution | -1.5 | -2.2 | 94.9 | 0.0 | 0.0 |
| Dividends paid | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Other, net | 13.2 | -12.9 | 0.0 | 0.0 | 0.0 |
| **Net change in cash and equivalents** | **4.4** | **5.5** | **80.8** | **8.1** | **11.2** |
| Beginning cash and equivalents | 0.8 | 5.2 | 10.7 | 91.5 | 99.7 |
| Ending cash and equivalents | 5.2 | 10.7 | 91.5 | 99.7 | 110.8 |

*Source: Company data, DM BZ WBK forecasts*

**Figure 10. PBG: Balance sheet forecasts**
*PLN in millions, unless otherwise stated*

| | 2001 | 2002 | 2003 | 2004E | 2005E | 2006E |
|---|---|---|---|---|---|---|
| **Current assets** | **52.3** | **103.9** | **101.9** | **198.7** | **251.0** | **279.4** |
| cash and equivalents | 0.8 | 5.2 | 10.7 | 91.5 | 99.7 | 110.8 |
| other short term investments | 0.0 | 2.5 | 2.0 | 2.0 | 2.0 | 2.0 |
| accounts receivable | 44.5 | 67.7 | 62.0 | 73.2 | 103.8 | 115.8 |
| inventories | 1.9 | 4.7 | 2.4 | 2.8 | 4.0 | 4.4 |
| prepaid expenses | 5.0 | 23.8 | 24.8 | 29.3 | 41.6 | 46.4 |
| **Fixed assets** | **28.9** | **69.0** | **59.4** | **62.2** | **58.2** | **64.7** |
| PPE | 27.5 | 63.9 | 40.8 | 44.6 | 51.0 | 58.9 |
| long-term investments | 1.0 | 1.5 | 18.1 | 14.9 | 4.7 | 3.6 |
| intangibles | 0.4 | 1.0 | 0.5 | 1.0 | 1.2 | 1.3 |
| goodwill | 0.0 | 2.6 | 0.0 | 1.7 | 1.3 | 0.9 |
| Long-term deferred charges | 1.4 | 10.9 | 4.7 | 5.6 | 7.9 | 8.8 |
| **Total assets** | **82.5** | **183.9** | **166.0** | **266.5** | **317.1** | **352.9** |
| **Current liabilities** | **45.9** | **89.8** | **87.8** | **73.0** | **100.9** | **111.9** |
| bank debt | 20.1 | 33.0 | 31.2 | 6.2 | 6.2 | 6.2 |
| accounts payable | 14.5 | 39.1 | 45.1 | 53.2 | 75.5 | 84.2 |
| other current liabilities | 11.3 | 17.7 | 11.5 | 13.5 | 19.2 | 21.4 |
| Deferred income | 0.6 | 2.6 | 2.1 | 2.5 | 3.5 | 3.9 |
| **Long-term liabilities** | **14.1** | **48.6** | **40.7** | **40.7** | **30.7** | **20.7** |
| bank debt | 14.1 | 48.6 | 30.2 | 30.2 | 20.2 | 10.2 |
| other long-term liabilities | 0.0 | 0.0 | 10.5 | 10.5 | 10.5 | 10.5 |
| Provisions | 1.7 | 6.2 | 2.6 | 4.1 | 5.8 | 6.5 |
| **Equity** | **20.3** | **23.4** | **32.5** | **145.9** | **175.8** | **209.6** |
| share capital | 7.2 | 7.2 | 7.2 | 10.5 | 10.5 | 10.5 |
| capital reserves | 5.1 | 10.3 | 16.4 | 119.2 | 137.8 | 167.6 |
| other reserve capital, incl. undistributed loss | 0.0 | 1.3 | -2.4 | -2.4 | -2.4 | -2.4 |
| net income | 8.0 | 4.6 | 11.3 | 18.6 | 29.8 | 33.8 |
| **Minority Interest** | **0.0** | **13.2** | **0.3** | **0.3** | **0.3** | **0.3** |
| **Total liabilities and equity** | **82.5** | **183.9** | **166.0** | **266.5** | **317.1** | **352.9** |
| Net debt | 33.4 | 76.5 | 50.8 | -55.0 | -73.2 | -94.4 |
| Net debt/Equity | 164% | 327% | 156% | -38% | -42% | -45% |

*Source: Company data, DM BZ WBK forecasts*

**Figure 11. PBG: Key ratios**
*PLN, unless otherwise stated*

| | 2001 | 2002 | 2003 | 2004E | 2005E | 2006E |
|---|---|---|---|---|---|---|
| EPS | 1.12 | 0.64 | 1.57 | 2.10 | 2.83 | 3.21 |
| BVPS | 2.8 | 3.2 | 4.5 | 16.5 | 16.7 | 19.9 |
| EBITDA/share | 2.43 | 2.00 | 2.92 | 3.37 | 4.15 | 4.56 |
| DPS | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Cash Earnings/share | 3.5 | 2.6 | 4.5 | 5.5 | 7.0 | 7.8 |
| Net interest cover | 4.8 | 2.5 | 3.0 | 124.7 | -18.3 | -14.1 |
| Tax rate (%) | -33.0 | 9.1 | -21.3 | -19.0 | -19.0 | -19.0 |
| Payout ratio (%) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Dividend yield (%) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Net gearing (%) | 164.4 | 327.0 | 156.1 | -37.7 | -41.6 | -45.0 |
| ROCE (%) | 25.3 | 8.7 | 16.6 | 24.5 | 32.4 | 32.2 |
| ROE (%) | 49.3 | 21.2 | 40.4 | 20.8 | 18.5 | 17.5 |
| ROIC (%) | 32.4 | 10.6 | 10.8 | 22.3 | 30.2 | 29.7 |

*Source: Company data, DM BZ WBK forecasts*

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