# Sector Report
## Polish Construction

- Road construction spendings are to be massively cut in the near future and replaced by power fleet modernization and the Polish railway system upgrade
- Polish construction companies are undertaking a strategic shift towards the next revenue sources
- From the best outlook sectors we prefer power engineering to railway construction on the back of private vs. public funding sources given the austerity measures
- We prefer high-risk Polimex-Mostostal to PBG and low-risk Mostostal Warszawa to Budimex

### Recommendations

| Company | Recommendation | TP |
|---|---|---|
| Polimex-Mostostal | Buy | 2.05 |
| Mostostal-Warszawa | Buy | 30.0 |
| Budimex | Hold | 96.0 |
| PBG | Hold | 64.0 |

*Source: Raiffeisen Centrobank*

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## No more de-rating, now stock-picking counts

We have turned more bullish on Polish construction after the sector experienced a massive de-rating last year. We believe the valuations are now in line with the growth prospects and we find the sector attractive again. We believe, however, that stock-picking is the right strategy.
We lift our recommendations for Polimex-Mostostal and Mostostal Warszawa to "buy" and re-initiate PBG and Budimex with "hold" recommendations.
We like Polimex-Mostostal due to its diversified revenue sources, exposure to the next booms of power engineering and railway construction and high export capacities. We, however, have to point out the elevated leverage, lower balance sheet quality and - in our view - aggressive accounting for road contracts.

Mostostal Warszawa's involvement in the troubling road construction is to decrease massively this year, which in combination with a massive loss recognition expected in 4Q 11 and the power engineering engagement (PLN 9.4 bn Opole project) should support the most dynamic earnings momentum. Furthermore, we appreciate the top-quality balance sheet financed with almost no debt and relatively good working capital management.

Budimex is slightly less preferable compared to Mostostal Warszawa from these two net cash companies. We admire its experience in road construction (negative cash conversion cycle with top margins), yet fear what will come next after massive road spendings will be cut already in 2013. We appreciate the company's decision to move towards railway construction – as the priority of the next EU budget for the years 2014-2020 and given the tremendous modernization needs of the Polish railway system. Yet, we fear heavy overemployment of PNI (the railway acquisition), which is difficult to restructure in light of employment guarantees. We also see power engineering superior to railway construction (Budimex will not really engage in the former apart from some general construction works) on the back of private vs. public funding sources. Furthermore, there is no clear alternative to compensate for the declining road revenues yet. We also do not know whether excellent working capital management can be performed in the niches to be explored.

We appreciate PBG's flexibility and determination to re-position towards potential booms, as evidenced by history and the recent acquisitions. We see PBG as the major beneficiary of the massive power fleet modernization exercise to be conducted in Poland on the back of Rafako's incorporation into the group structure and an aggressive tender participation approach. We have to warn on high tender preparation costs and potential contract execution risks. We also appreciate the company's exit strategy from large infrastructure projects, which apart from boosted revenues has so far only resulted in elevated leverage and refinancing risk, depressed margins and working capital mismanagement. Yet, 2012 figures will still be affected by the PLN 1.9 bn order backlog for roads. We perceive PBG's refinancing risk as high and also consider the goodwill impairment risk (constituting 50% of the existing equity) as rather material.

## Investment case

***We do not see scope for further sector de-rating***

The Polish construction sector experienced a massive de-rating last year, which proved to be in line with our hypothesis of valuation convergence towards the European peers. We believe that despite an incredible increase of total output, the micro scale looked way less appealing on the back of the Polish market openness which resulted in fierce competition, squeezing profitability. We do not see any more sector-specific room for de-rating and believe it is time for stock-picking. We like the companies exposed to the power engineering and railway construction sectors, with improving working capital cycles, low leverage and low refinancing risks. We look for diversified companies with export capacities and revenues biased towards private funding sources. We appreciate high-quality balance sheets with dividend potential. Our paper splits the four companies we cover into low-leverage/high-balance sheet quality companies on the one hand (Budimex and Mostostal Warszawa) with the preference for the latter as well as highly-leveraged, high-goodwill-distorted balance sheet companies on the other hand (Polimex-Mostostal and PBG) with our preference for the former.

The Polish construction sector is on the verge of a massive fundamental change, where low-margin road contracts that require high working capital are to be replaced with power engineering projects demanding know-how (yet of high execution risk due to their unprecedented scale in Poland) as well as the EU-funded railway system modernization program. We see companies like Polimex-Mostostal (power and railways) and Mostostal Warszawa (power) to a certain extent as incumbents in those sectors. Budimex and PBG, however, are undergoing a strategic repositioning towards these sectors accompanied by acquisition exercises (railway construction company PNI for the former and one of the most experienced power engineering companies, Rafako, in case of the latter). We have to point out that we somewhat prefer power engineering to railway construction on the back of the private vs. public funding.

***Polimex-Mostostal upgraded to "buy" on the back of high order backlog and desirable sector exposure***

We upgrade our recommendation for Polimex-Mostostal to "buy" as we appreciate the company's experience in both of the aforementioned sectors. We like the company's order backlog and high export potential (predominantly to EU countries). We do not like the highly leveraged balance sheet with quite a substantial goodwill balance and consider the company's accounting practices for road construction as aggressive.

***Mostostal Warszawa will report the most dynamic earnings momentum; upgraded to "buy"***

We also upgrade our recommendation for Mostostal Warszawa to "buy" as having road construction significantly diminished in the 2012 sales mix and having the 4Q 11 profits impacted by a massive roads related loss recognition, we expect the company's earnings momentum to be the most dynamic. We also expect the company to benefit from the power engineering boom and only to some extent from railway construction (no specialized works), and we like the company's high-quality balance sheet combined with an expected net cash position at end-2011.

***Budimex re-initiated with "hold" on the back of unclear outlook***

We re-initiate our Budimex coverage with a "hold" recommendation. The company has the highest net cash position (amounting to PLN 1.7 bn) and a negative cash conversion cycle, despite a very high engagement in road construction. Yet, the company is facing a material road construction related revenue decrease from 2013 on, hence the desirable repositioning. Firstly, the management has decided to turn towards railway construction via the acquisition of PNI and secondly, niches such as waste management, facility management, road and railway maintenance are to be explored. We appreciate that move yet we see profitability problems in the case of the former and no clear outlook yet in the latter. We are also not sure whether the company will be able to transfer its excellent working capital management know-how to the new fields.

***PBG will be the major beneficiary of the power engineering boom, yet we see the biggest risk there; re-initiated with "hold"***

We also re-initiate our PBG coverage with a "hold" recommendation. We consider PBG as the most risky play with an elevated and unsustainable leverage and high refinancing risk resulting from working capital mismanagement and an overinvestment to some extent. We also do not like the low-quality, high-goodwill balance sheet making the company highly vulnerable to any impairment risk. On the other hand, however, we consider PBG to be the major beneficiary of the expected power engineering boom as the company has one of the top credentials available on the Polish market after Rafako's acquisition as well as pursues a very aggressive strategy regarding the participation in power tenders (which on the other hand triggers massive offer preparation costs not yet recognized in the P&L). We also appreciate the group's strategy to exit the margin-depressing highway and expressway construction contracts, yet the order backlog of those still constitutes more than 30% of the current portfolio. We expect margins and the working capital cycle to improve in 2013 only.

## Scorecard

### Poland's "big four" construction companies

| Influencing factor | Most preferred | Least preferred | Comment |
|---|---|---|---|
| Road construction exposure | Mostostal Warszawa | Budimex | All companies are engaged in the road infrastructure boom in Poland, with Budimex, however, deriving as much as 65% of its construction revenues from roads. |
| Railway segment exposure | Polimex-Mostostal, Budimex | PBG | Polimex-Mostostal with Torpol and Budimex with PNI are the best positioned to benefit from the railway construction boom either as a general contractor (competition is rather high) or a subcontractor (capacities are quite limited in Poland). |
| Power engineering exposure | PBG, Polimex-Mostostal, Mostostal Warszawa | Budimex | PBG participates in all the open tenders in Poland, whereas Mostostal Warszawa has chosen a very selective approach to limit the incurred offer-preparation costs. Budimex has no credentials, yet wants to participate in the boom via general construction. |
| Order backlog | Budimex, Polimex-Mostostal | PBG, Mostostal Warszawa | Budimex has the highest sales coverage with the current order backlog in 2012e. Mostostal Warszawa, on the other hand, has the lowest share of road construction. |
| Leverage | Budimex, Mostostal Warszawa | PBG, Polimex-Mostostal | Engagement in the working capital intensive road construction contracts substantially deteriorated the balance sheet conservativeness of the construction companies but Budimex. Additionally, PBG's debt burden has increased after the recent Rafako acquisition. |
| Refinancing | Budimex-Mostostal Warszawa | PBG, Polimex-Mostostal | The refinancing risk has also increased, and companies like Polimex-Mostostal and PBG only cover around 20-30% of their short-term debts with the cash balance. |
| Operating leverage | Budimex | Polimex-Mostostal | Budimex seems to be the most flexible company to us, where most of the work is subcontracted and the company maintains low fixed costs (however, the PNI acquisition will change that).<br>Polimex-Mostostal is the opposite, however, we have to indicate that its production segment is predominantly behind the high operating leverage. |
| Working capital management | Budimex, Mostostal Warszawa | PBG, Polimex-Mostostal | The working capital management has encountered a number of challenges following the companies' engagement in large road construction contracts.<br>Despite that, Budimex - which derives the majority of its revenues from roads - keeps its working capital financing needs at a very low level, and actually quite often utilizes its suppliers and subcontractors.<br>PBG seems to be struggling the most, yet we expect a considerable amount of cash to be released after the stadium contracts are paid and the road contract engagement decreases. |
| Valuation | Mostostal Warszawa, Polimex-Mostostal | PBG | The valuation of Polish construction companies has converged towards the Western European peers according to the thesis we have been advocating since last year.<br>PBG's valuation looks the richest. Polimex-Mostostal trades on par with PBG, yet we see much more space for improvement in 2013.<br>Mostostal Warszawa has turned out to be the cheapest stock on EV/EBIT basis. |
| Dividend | Budimex | PBG, Polimex-Mostostal | We see the balance sheets of PBG and Polimex-Mostostal too stretched to pay out any dividend in 2012. 2013 might also be challenging.<br>Budimex and Mostostal Warszawa are in a comfortable position to pay out dividends. We do not think, however, that Budimex's high absolute DPS will be sustainable given the deteriorating road construction outlook.<br>We also do not think that Mostostal Warszawa will pay out any dividends from 2011 profits given its negative profitability. |
| Exports | Polimex-Mostostal | Budimex | We like the companies diversifying their revenue sources outside Poland.<br>Polimex-Mostostal derives almost 30% of its revenues from abroad, particularly from its steel products as well as the power-engineering and chemicals construction know-how. |
| Balance sheet quality, goodwill | Mostostal Warszawa | PBG, Polimex-Mostostal | Both PBG's and Polimex-Mostostal's balance sheets and valuations are distorted by the recognized goodwill.<br>We like Mostostal Warszawa's quality balance sheet. The company also looks the cheapest on P/BV basis after adjusting for goodwill. |
| Client mix | PBG | Budimex | Given the ongoing austerity measures and downside risk to public investments, we favour companies skewed to the private client, particularly clients with deep pockets (utilities, etc.).<br>Hence, we favour PBG and see Budimex's dependence on public contracts as a disadvantage. |

*Source: Companies, Raiffeisen Centrobank*

## Outlook of sub-sectors

***Power engineering, railway construction and waste incinerator construction facing the best outlooks***

Our sector ranking is presented in the table below. We prefer sectors with a promising outlook (power engineering, railway construction and incinerator construction), low competition (power engineering, incinerator construction, oil&gas and chemicals), high margins (power engineering, oil&gas and chemicals) and private clients, given the austerity measures undertaken by governments (power engineering, oil&gas, chemicals, residential construction and partially non-residential buildings). We give the highest weight to the outlook. Our preference lies in the power engineering, incinerator construction and railway modernization sectors. We avoid companies specialized in road construction and the residential segment.

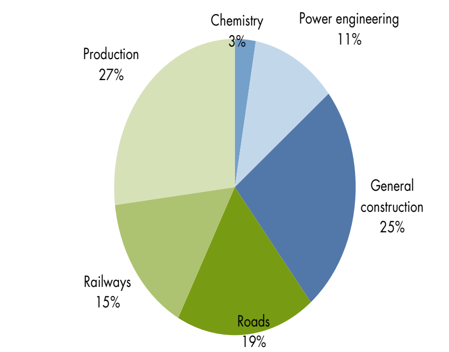
## Sector ranking

| Ranking | Sector/Companies | Comment | Sector developments |
|---|---|---|---|
| 1 | Power engineering<br><br>PBG, Polimex-Mostostal, Mostostal Warszawa | Good outlook, low competition, high margins and a private client | - Given the outdated electricity capacities in combination with increasing electricity demand, Poland requires massive power engineering capex in the form of either construction of new blocks or existing fleet modernization.<br>- Currently called tenders are valued at approximately PLN 40 - 50 bn, and we believe there are a few more to come.<br>- Additionally the PLN 9.5 bn contract for construction of two Opole blocks has been awarded to the consortium of Polimex-Mostostal, Mostostal Warszawa and Rafako (of PBG Group).<br>- Furthermore, abundant investments are needed in the green energy segment (wind parks, biomass and biogas combustion blocks, Energa's hydro fleet extension).<br>- The outlook for off-shore wind farms seems to be bright with some experts estimating the total investment value amounting to PLN 200 bn. Energomontaz Polnoc of Polimex-Mostostal deals with the construction of artificial islands.<br>- PGE plans the erection of two nuclear power blocks of 6,000 MW capacity.<br>- Power groups' balance sheets support the investment programs.<br>- Technology in the form of turbines can only be provided by foreign suppliers, boilers are also produced in Poland by Rafako. - Most of the construction work, besides technology, is likely to be conducted by Polish construction companies with specialized skills (Polimex-Mostostal, Mostostal Warszawa, PBG, Elektrobudowa). |
| 2 | Incinerators construction<br><br>PBG, Polimex-Mostostal, Mostostal Warszawa, Budimex | Good outlook, low competition, moderate margins and a public client | - The value of the potential contracts is estimated to stand at PLN 5 bn.<br>- Each Polish city with the number of inhabitants exceeding 100 ths is obliged to have one waste incinerator in place.<br>- Probably 12-14 incinerators will be erected in Poland, currently 5 projects are quite advanced with respect to the tender process with PBG recently submitting the lowest bid (of PLN 704 mn) on the incinerator construction in Krakow.<br>- None of the Polish companies owns viable technology. |
| 3 | Railway construction<br><br>Polimex-Mostostal, Budimex | Good outlook, moderate competition, moderate margins and a public client | - In 2011 the value of all the railway modernization contracts amounted to PLN 3.7 bn, with a total outlook amounting to PLN 20.5 bn in the years 2011-2013.<br>- The new EU budget would shift funds from road construction to railway modernization.<br>- Funding, however, might remain a problem, given the weak financial position of PKP PLN and likely investment cuts by the central government.<br>- Competition remains moderate, however, we see more and more foreign players entering the market.<br>- On the other hand, however, the number of subcontractors with the right machinery and know-how is quite limited in Poland with the market divided between Torpol (Polimex-Mostostal), Feroco, Trakcja Polska, PNI, PKP Energetyka and ZUE. |
| 4 | Oil&gas<br><br>PBG, Polimex-Mostostal | Moderate outlook, low competition, high margins and a private client | - Massive investments of PGNiG as well as Gas-System in gas transmission infrastructure (pipelines), gas storage facilities, LNG terminal, interconnections between Poland and neighbouring countries.<br>- PGNiG's capex for the years 2011-2015 amounts to PLN 27 bn, thereof PLN 6 bn is to be spent on distribution investments and PLN 1.6 bn on storage facilities.<br>- NATO investments, including fuel storage depots.<br>- Probably too early to judge, yet the shale gas fantasy in Poland may lead to a boom in related infrastructure investments. |
| 5 | Hydro engineering<br><br>PBG, Polimex-Mostostal, Budimex | Moderate outlook, moderate competition, moderate margins and a public client | - Investments are co-financed with EU funds and predominantly concentrated on flood protection (increase in the capacity of storage reservoirs in Poland, reconstruction of embankments and river engineering). |
| 6 | Chemicals<br><br>Polimex-Mostostal | Weak outlook, low competition, high margins and a private client | - Outlook for the chemical sector remains weak after the major investors (Lotos and PKN Orlen) will have completed their major investments and are predominantly concentrated on decreasing leverage at the moment.<br>- Yet, modernization efforts are undertaken by chemicals companies. Investments planned for 2012 amount to PLN 1.3 bn. |
| 7 | Residential construction<br><br>Budimex, PBG, Mostostal Warszawa | Weak outlook, high competition, low margins and a private client | - The number of flats on sale in the six largest Polish cities is on record-high levels (in terms of both completed flats and those under construction).<br>- We believe that lending limits due to tighter regulations and high interest rates will be a drag on mortgage demand.<br>- Furthermore, the government has introduced some serious limitations to the subsidies program. |
| 8 | Non-residential construction<br><br>PBG, Polimex-Mostostal, Mostostal Warszawa, Budimex | Weak outlook, high competition, low margins and a private and public client | - Most of the non-residential construction contracts come from public clients (state, municipalities, universities, etc.) and are EU-co-funded.<br>- Given the elevated leverage of the public entities and uncertainties concerning the future EU budget we project demand to be weak.<br>- On the other hand, however, Poland still remains an attractive country to place factories and offices (good prospects for outsourcing services) there. Also, the country seems to be underpenetrated with regard to retail space. |

| | | | |
|---|---|---|---|
| 9 | Roads construction<br><br>PBG, Polimex-Mostostal, Mostostal Warszawa, Budimex | Weak outlook, high competition, low margins, public client | - Poland spent PLN 18.4 bn in 2009 as well as PLN 20.4 bn and PLN 26.4 bn in 2010 and 2011, respectively, on highway and expressway construction.<br>- Expenditures are expected to peak at PLN 29.6 bn this year and then to substantially drop to PLN 7 bn in the following year.<br>- The outlook for road expenditures looks grim and the new EU budget for the years 2014-2020 is to emphasize railway construction rather than roads.<br>- The tough competition from domestic and foreign contractors has reduced the already low margins, which sank further as prices of construction materials, fuels and subcontractors' services rose.<br>- Data from the Road Chamber indicates that about 70% of the road companies are currently generating losses.<br>- We expect the margin pressure on currently contracted work to ease in 2013 as the pressure on transportation costs and building materials such as asphalt and aggregate will ease after most of the large projects are completed.<br>- Yet, we think that the competition on new projects will even increase but also that many of the companies will disappear from the market.<br>- We prefer low operating-leverage companies or those which can relocate their machinery and equipment to other markets (like STRABAG). |

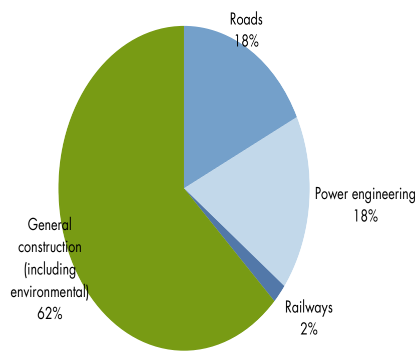
*Source: Raiffeisen Centrobank*

### Polimex-Mostostal's order backlog (11-end)



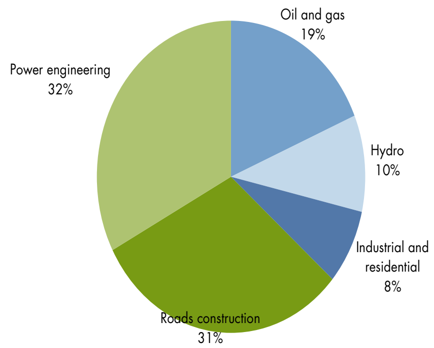

*Source: Polimex-Mostostal, Raiffeisen Centrobank estimates*

### Mostostal Warszawa's order backlog (11-end)



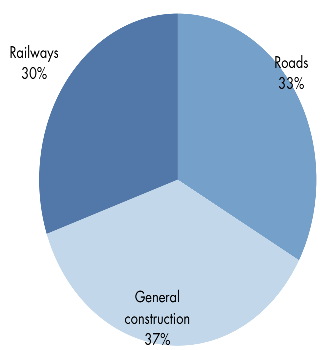

*Source: Mostostal Warszawa, Raiffeisen Centrobank estimates*

### PBG's order backlog (11-end)




*Source: PBG, Raiffeisen Centrobank*

### Budimex' order backlog (11-end)



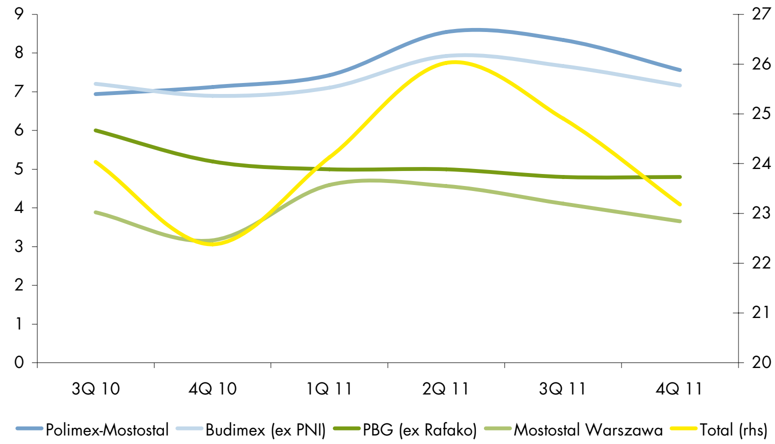

*Source: Budimex, Raiffeisen Centrobank*

## Order backlog

***Order backlogs are trending down***

To us, it looks as if the peak in order backlog caused by the infrastructure-related boom is already behind us. Yet, we would expect a rebound already this year following the power engineering kick-off. We do not think that Budimex's order backlog could increase substantially from the current levels, however. In our view, the repositioning towards railway construction might not be enough to compensate for the roads. Please note that the chart below does not include Rafako (in case of PBG) and PNI (in case of Budimex) in order to show the trend.

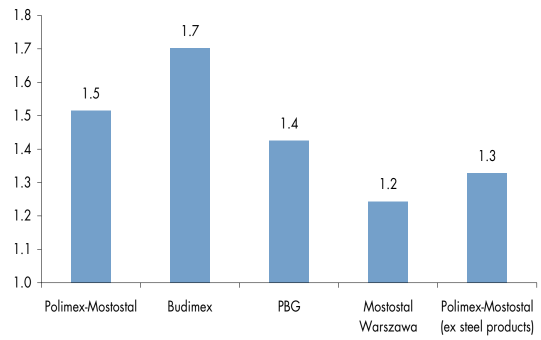
### *Order backlog (in PLN bn)*




*Source: Companies, Raiffeisen Centrobank*

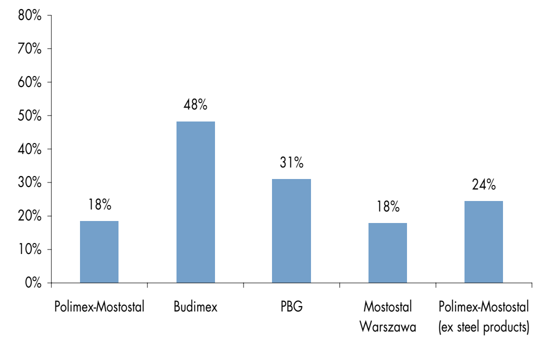
We also look at the 2012e sales coverage with the current order backlog (end-2011) as well as the order backlog quality with respect to the share of low-margin road construction contracts. Polimex-Mostostal's and Budimex's order backlog seem to be the largest, with Polimex-Mostostal having only an 18% share regarding roads. We also adjust Polimex-Mostostal's backlog and sales for the steel product segment, as part of the demand is generated internally.

### *Order backlog / 2012e sales*




*Source: Companies, Raiffeisen Centrobank estimates*

### *Road contracts in the order backlog*




*Source: Companies, Raiffeisen Centrobank estimates*

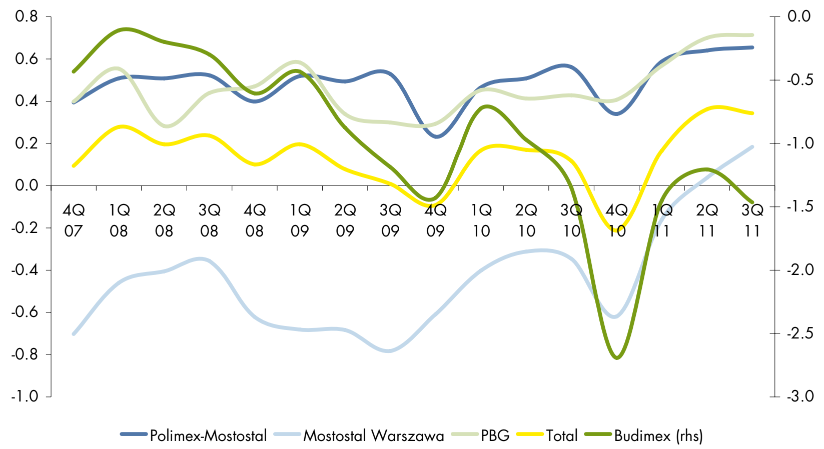
Please note that Polimex-Mostostal's highway construction contracts stretch beyond the peak time of 2012 after which we believe that pressure on construction material prices (particularly aggregate and asphalt) as well as transportation costs (not fuel, though) should somewhat decrease. We also believe that the availability of subcontractors' services should become easier and cheaper.

## *Leverage and refinancing risk*

***Leverage and refinancing risk the highest for PBG***

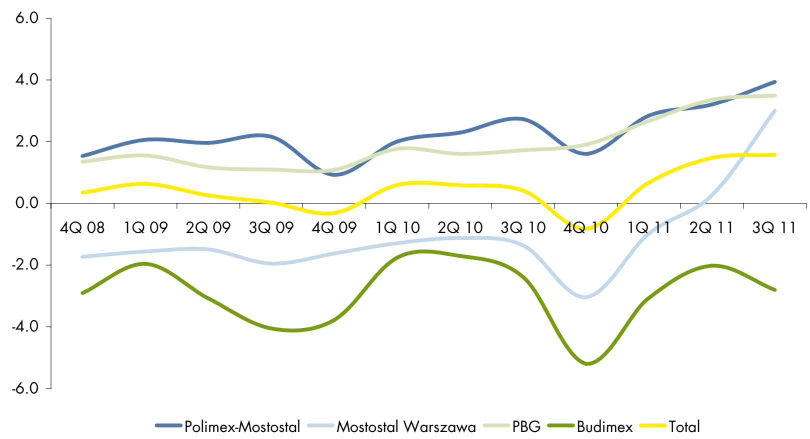
Engagement in highway and expressway construction has led to troubles for companies like Covec (China) or DSS (Poland) on the back of financing gaps triggered by the prolonged working capital management cycle (it takes some procedures and time until the road authorities reimburse companies for the work conducted). Hence, the leverage of the companies has quite increased, predominantly that of Polimex-Mostostal and PBG. Furthermore, even the conservatively financed Mostostal Warszawa with its traditionally substantial net cash position turned into net debt last year. The ratios, however, should have quite improved in 4Q 11 (apart from PBG), as the last quarter of the year tends to ease the working capital financing pressure as quite a part of the receivables is settled (especially for the road contracts). Hence, we would expect Mostostal Warszawa to turn net cash positive again, and the other companies to come back to safer levels.

### Net debt/equity ratio (x)




*Source: Companies, Raiffeisen Centrobank*

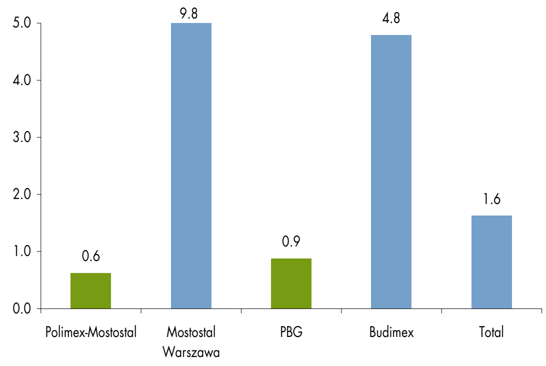
### Net debt/EBITDA (x)




*Source: Companies, Raiffeisen Centrobank*

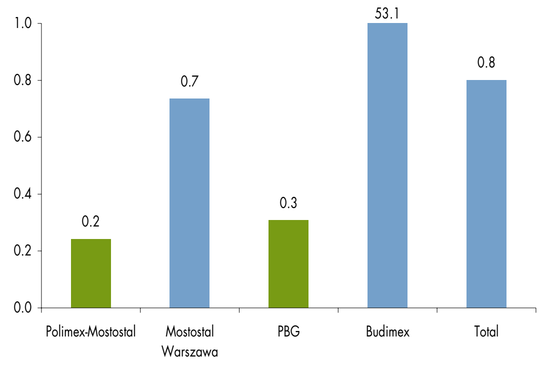
Furthermore, the refinancing risk have substantially increased, particularly in case of Polimex-Mostostal and PBG.

### Cash/short-term debt (4Q 07-end)




Source: Companies, Raiffeisen Centrobank

### Cash/short-term debt (3Q 11-end)



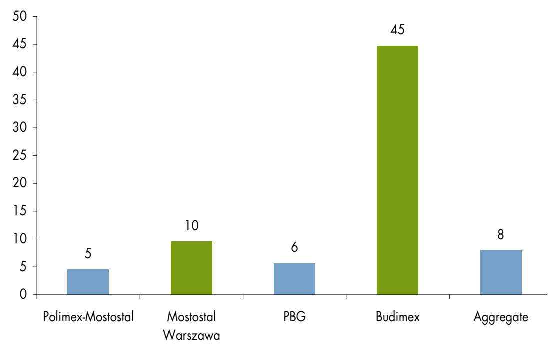

Source: Companies, Raiffeisen Centrobank

## Operating leverage

***Polimex-Mostostal operates on the highest operating leverage***

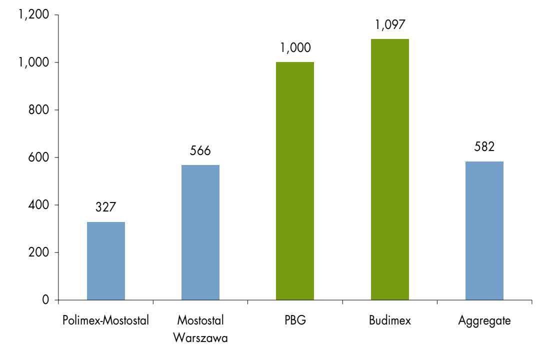
We also look at the operating leverage of the companies, particularly in the light of slowing demand. We see Budimex as the most flexible group (however, the situation is likely to change after the PNI acquisition) and Polimex-Mostostal to be the most heavily leveraged from the operating point of view when we take fixed assets as well as employment into account. Please note that after the acquisition of PNI by Budimex, 1,700 new employees will be incorporated into the group, hence the Sales/Employee ratio will decrease by some 25%, making Budimex a somewhat less flexible company, particularly in the light of the employment guarantees in place.

### Fixed assets turnover (x) (2011)




Source: Companies, Raiffeisen Centrobank

### Sales/employee (PLN ths, 2011)



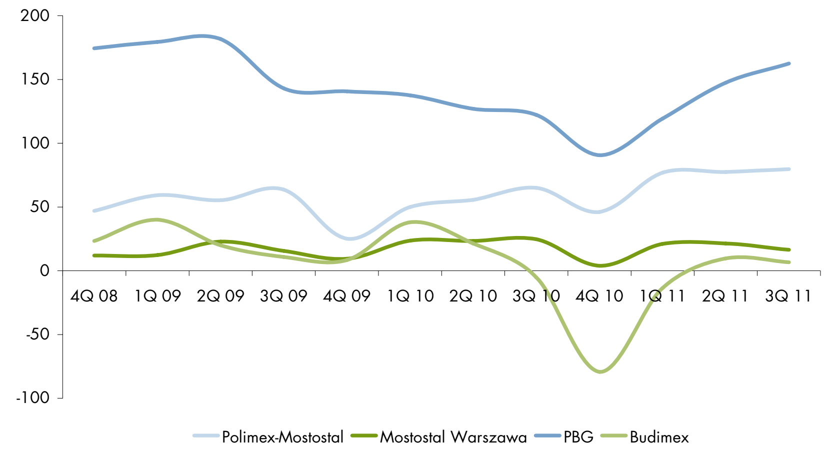

Source: Companies, Raiffeisen Centrobank

## Working capital management

***Budimex has an excellent working capital management***

The working capital environment has deteriorated on the back of large working capital needs connected to the Polish infrastructure boom. Despite overall complaints about the payment delays from road authorities, we admire Budimex's working capital management despite the fact that the company is the most engaged in road construction from the "big four". We expect the conditions to improve once the share of large road contracts diminishes in both the order backlog as well as the top line figure. We expect all the companies to report substantial improvements at the end of this year.

*Cash conversion cycle (in days)*



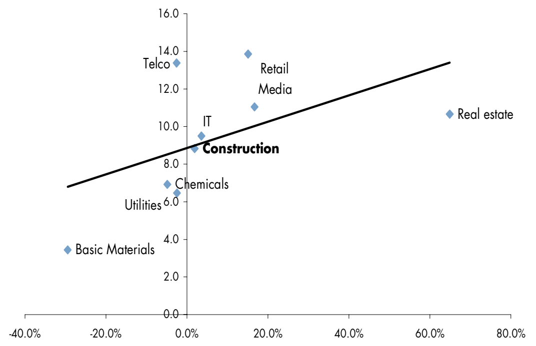

*Source: Companies, Raiffeisen Centrobank*

## Valuation

***Valuation converged and looks reasonable on the basis of expected growth***

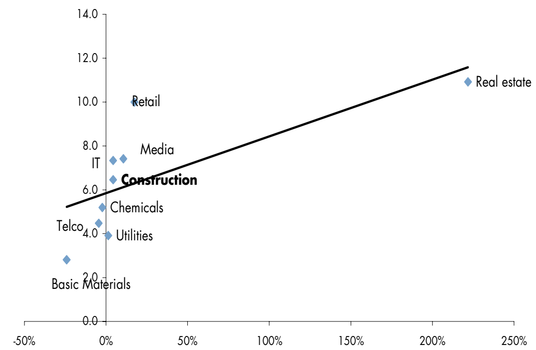
The Polish construction sector seems to be trading on slightly depressed valuations in comparison to other Warsaw-listed sectors when regressed vs. the 2011e-2013e CAGR earnings estimates as presented by the charts below.

***2011-2013 EBIT CAGR vs. 12e EV/EBIT***



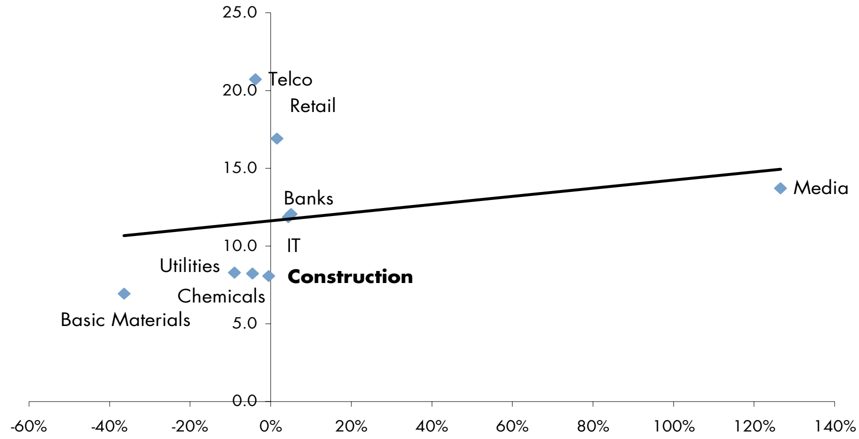

*Source: Bloomberg, Raiffeisen Centrobank estimates*

***2011-2013 EBITDA CAGR vs. 12e EV/EBITDA***




*Source: Bloomberg, Raiffeisen Centrobank estimates*

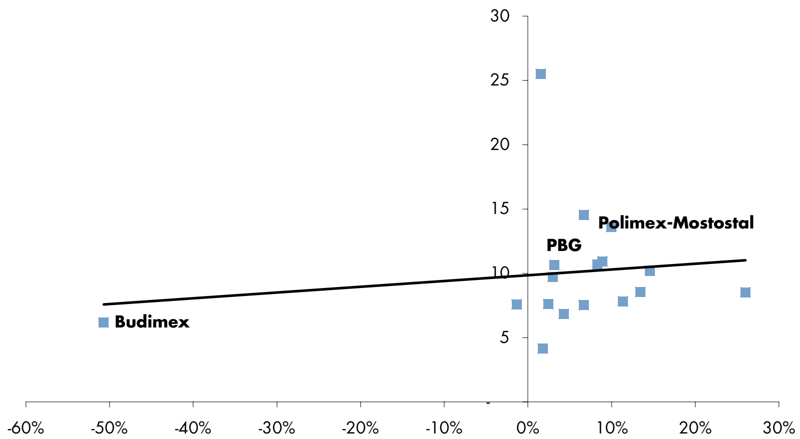
***2011-2013 Net Income CAGR vs. 12e P/E***




*Source: Bloomberg, Raiffeisen Centrobank estimates*

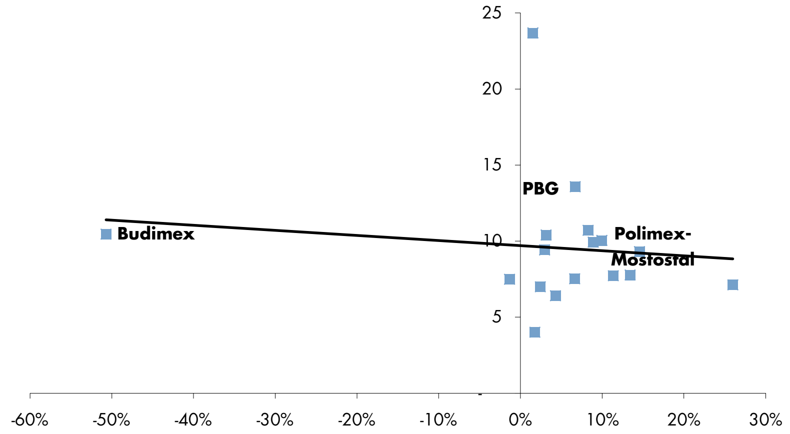
Furthermore, as already indicated in our previous construction updates, we are the advocates of valuation convergence, i.e. we believe that the Polish companies should not be trading at any premium vs. the Western European companies given the openness of the Polish construction market and the tough competition. We believe, however, that following the massive de-rating in 2011, the valuation multiples of the Polish companies (please note that we favour the EV/EBIT multiple) seem to be in line with the Western peers, as presented by the chart below. Please note that we have decided to use the 2011-2014 CAGR in order to capture the power engineering potential. Please note also that Mostostal Warszawa is excluded from the chart due to its expected EBIT loss for 2011.

***2012e EV/EBIT vs. 2011e-2014e EBIT CAGR***




*Source: Bloomberg, Raiffeisen Centrobank estimates*

### 2013e EV/EBIT vs. 2011e-2014e EBIT CAGR




*Source: Bloomberg, Raiffeisen Centrobank estimates*

### Peers valuation*

| | 2012e EV/EBIT | 2013e EV/EBIT | 2011-2014e CAGR | 2012e P/E | 2013e P/E | 2011-2014e CAGR |
|---|---|---|---|---|---|---|
| Vinci | 9.7 | 9.7 | 2.9% | 11.5 | 11.0 | 2.7% |
| Bouygues | 7.6 | 7.6 | -1.3% | 7.3 | 7.0 | 2.2% |
| Hochtief | 9.3 | 9.3 | 78.4% | 12.9 | 11.8 | n.a. |
| Skanska | 10.9 | 10.9 | 8.9% | 14.6 | 13.6 | 10.6% |
| STRABAG SA | 10.6 | 10.6 | 3.1% | 14.2 | 13.6 | -0.7% |
| Balfour Beatty | 7.7 | 7.7 | 2.4% | 8.3 | 7.9 | 2.1% |
| Eiffage | 14.5 | 14.5 | 6.7% | 11.2 | 9.4 | 12.8% |
| Bilfinger Berger | 7.5 | 7.5 | 6.6% | 12.6 | 13.1 | -7.7% |
| Koninklijke BAM | 13.5 | 13.5 | 11.8% | 8.0 | 7.3 | -1.3% |
| Carillion | 6.5 | 6.5 | 8.6% | 7.0 | 6.6 | 7.4% |
| NCC | 7.8 | 7.8 | 11.4% | 9.3 | 9.1 | 16.5% |
| Taylor Wimpey | 8.8 | 8.8 | 26.0% | 14.7 | 11.3 | 42.2% |
| Sacyr Vallehermosso | 25.4 | 25.4 | 1.5% | 7.2 | 6.4 | n.a. |
| Peab | 10.2 | 10.2 | 14.6% | 9.0 | 8.1 | 23.1% |
| Morgan Sindall | 4.2 | 4.2 | 1.8% | 9.8 | 9.5 | n.a. |
| OHL | 8.5 | 8.5 | 13.4% | 10.0 | 8.6 | 13.9% |
| Impregilo | 9.4 | 9.4 | n.a. | 13.6 | 11.7 | 12.0% |
| Average | 10.1 | 10.1 | | 10.7 | 9.8 | |
| Median | 9.4 | 9.4 | | 10.3 | 9.5 | |
| Weighted | | | 7.0% | | | 12.1% |
| Polimex-Mostostal | 13.6 | 10.0 | 10.0% | 14.8 | 8.0 | 0.8% |
| Mostostal Warszawa | 15.9 | 9.5 | n.a. | 19.4 | 9.2 | n.a. |
| Budimex | 6.3 | 10.6 | -50.7% | 11.2 | 17.8 | -31.1% |
| PBG | 10.6 | 10.6 | 8.3% | 7.6 | 6.4 | -25.2% |
| Weighted | | | -0.3% | | | -5.5% |

*Source: Bloomberg, Raiffeisen Centrobank estimates, *EV based on last reported net debt*

Our preferred transaction multiple remains EV/EBIT to somehow account for different financing strategies as well as approaches concerning the usage of leasing. As presented by the table below, Polimex-Mostostal and PBG look the most expensive, however, with a substantial improvement for the following year in case of the former. Budimex is also the only company with multiples actually increasing when 2013 is taken into account. Mostostal Warszawa looks the cheapest to us.

***Multiple valuations*-***

| | 2012e EV/EBIT | 2013e EV/EBIT | 2012e P/E | 2013e P/E |
|---|---|---|---|---|
| Polimex-Mostostal | 9.5 | 5.4 | 16.3 | 8.8 |
| Mostostal Warszawa | 7.8 | 4.0 | 19.9 | 9.5 |
| Budimex | 3.7 | 8.2 | 11.0 | 17.4 |
| PBG | 9.0 | 7.4 | 9.6 | 8.1 |
| **Average** | **7.5** | **6.2** | **14.2** | **10.9** |

*Source: Raiffeisen Centrobank estimates,*EV is based on the projected net debt*

## Dividends

***Only Budimex can afford a dividend payment this year***

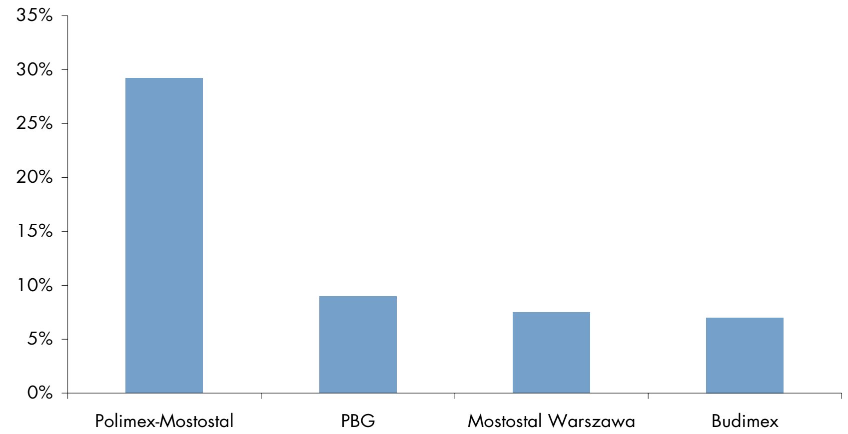
As a consequence of the rather leveraged balance sheets of PBG and Polimex-Mostostal, we do not expect the companies to pay out any dividends from 2011 profits and rather to concentrate on liquidity enhancement. We would expect Mostostal Warszawa to pay out a dividend.

## Expansion abroad

***Polimex-Mostostal derives the most from exports vs. the other construction companies***

We believe the Polish construction market is quite competitive, particularly in the road, non-residential, residential and more and more also in the railway construction segments. Hence, we appreciate the companies diversifying their revenue sources to other markets and thus being less vulnerable to domestic construction market developments.

***Share of exports in total sales (%)***




*Source: Companies, Raiffeisen Centrobank*

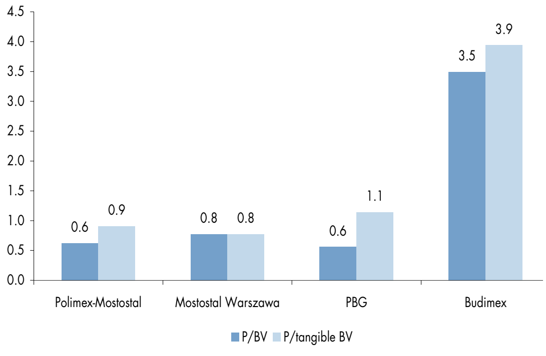
Momentarily, the big Polish construction companies are essentially offering their services on the Polish market. Polimex-Mostostal stands above the crowd and sells almost 30% of its products and services outside the domestic market (steel products, power engineering services, railway construction). Mostostal Warszawa predominantly exports power engineering know-how via its subsidiary Remak, and PBG, after the recent acquisition of Rafako, sells its power engineering technology abroad. Budimex had quite some expansion plans to the neighbouring markets of Slovakia and the Czech Republic as well as Romania, however, the plans seem to be suspended for the moment.

## Balance sheet quality

***We like Mostostal Warszawa's balance sheet quality the most. PBG's is highly distorted by massive goodwill.***

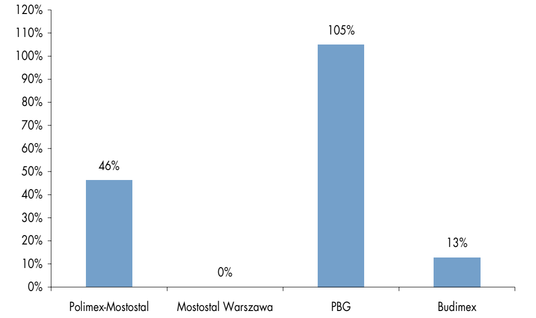
We are not big fans of the massive goodwill some of the companies have recognized on the balance sheets. This issue particularly concerns Polimex-Mostostal (PLN 491 mn at 3Q 11 vs. PLN 1.55 bn of equity, i.e. 32% of equity) and PBG (PLN 882 mn which translates into 51% of equity at the end of last year). We consider Mostostal Warszawa's balance sheet with no goodwill recognized to be of the highest quality. Mostostal Warszawa looks also cheaper than PBG and Polimex-Mostostal on a P/Tangible BV basis.

**P/BV and P/Tangible BV (x)**




*Source: Companies, Bloomberg, Raiffeisen Centrobank*

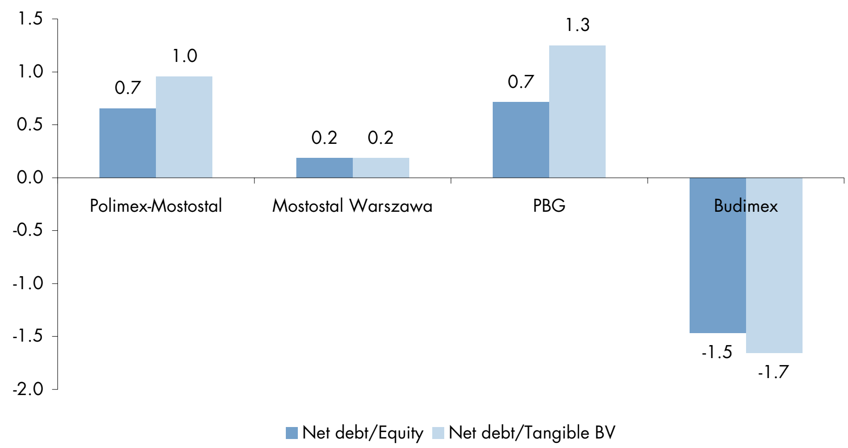
**P/Tangible BV vs. P/BV – valuation difference**




*Source: Companies, Bloomberg, Raiffeisen Centrobank*

Furthermore, the leverage ratios look less appealing if we consider equity adjusted for the recognized goodwill.

**Net debt/Tangible equity**



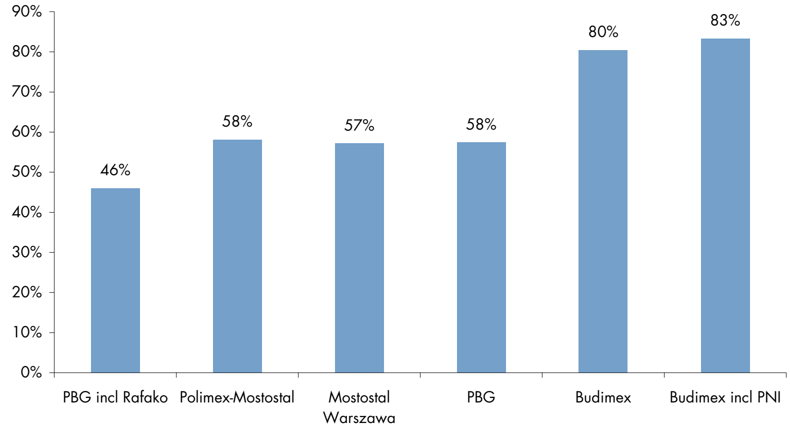

*Source: Companies, Raiffeisen Centrobank*

## Client mix

***We prefer less public funded projects in the order backlog***

Given the ongoing issues with the public budget deficit as well as the municipalities' indebtedness, we consider the public client to be less desirable these days (also because of the public procurement law, which favours companies/consortia bidding with the lowest (sometimes at margins close to 0) prices). We see the public investment program at risk, however, admit that there is EU funding support. Budimex seems to have the least desirable client mix, with some 80% of its order backlog derived from public tenders. We consider PBG's order backlog the most biased towards private investors (including utilities, PGNiG and Gaz-System), particularly after Rafako's inclusion. The chart below presents our estimates of the share of public clients in the client mix of the order backlog.

### *Order backlog from public clients*




*Source: Companies, Raiffeisen Centrobank estimates*

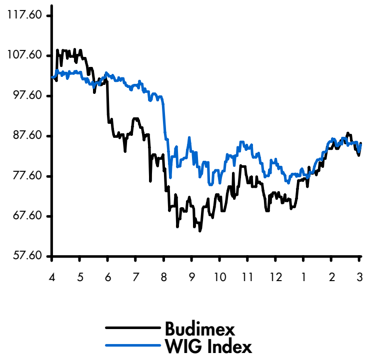
# Company Update

## Budimex

March 9, 2012 | Construction & Materials/Poland

## Hold

| | |
|---|---|
| Price 08.03.12* | 85.80 |
| Price target | 96.00 |
| Volatility risk | n.a. |
| Year high/low | 109.20/64.00 |
| Currency | PLN |
| PLN/EUR | 4.10 |
| GDR rate | n.a. |
| Shares outstanding eoy in mn | 25.53 |
| Market capitalisation (total shares) in EUR mn | 534.6 |
| Free float | 35.3% |
| Free float in EUR mn | 188.6 |
| Avg. daily turnover (12 m) in EUR mn | 0.30 |
| Index | WIG |
| ISIN code | PLBUDMX00013 |
| Bloomberg | BDX PW |
| Reuters | BMEX.WA |
| www.budimex.com.pl | |




*Source: Raiffeisen Centrobank*

## No clear path yet

We re-initiate the coverage of Budimex with a "hold" recommendation and a cum-dividend 12-month target price of PLN 96. We consider Budimex to be the best managed large construction company listed on the Warsaw Stock Exchange with massive liquidity (cash position) and an excellent working capital management, particularly in the light of its competitors struggling with short-term liquidity because of skyrocketing working capital balances due to the execution of road construction contracts. The problem, however, lies in Budimex's predominant revenue source and competence, i.e. road construction. The peak of spending on road construction is expected this year and afterwards we expect a substantial decrease approaching PLN 2 bn in 2014 (from almost PLN 30 bn planned for this year). Hence, the company is in the process of a strategic repositioning. The first step has already been undertaken which has resulted in the acquisition of one of the few existing railway construction companies with its own machinery base located in Poland. This was a good move in our view, on the back of the good outlook for railway construction spending, yet overemployment and a high fixed costs base will drag on the group's profitability. Furthermore, the company aims to explore the niches of facility management (cleaning, security), waste management, road and railway maintenance. Probably it is the right move, yet the outlook remains unclear to us with the potential change of the business profile of the company towards a utility. Nevertheless, the company has meanwhile become one of the largest residential developers and wooden house producers.

**4Q 11 figures:** The results came in very strong, topping the analysts' estimates on the back of a 33% yoy revenue increase. Margins remained in line, with the projections, however, following the general trend of a contraction observed also for the peers as a consequence of rising construction, transportation and oil products costs.

**Valuation and recommendation:** Budimex trades with a discount to the Polish and international peers, which however is justified given the deteriorating outlook in the roads segment and no firm position yet in the niches the company aims to explore. Our DCF valuation yields a 12-month target price of PLN 96 (including the dividend), which given the limited upside translates into our "hold" recommendation.

### Key figures and ratios

| PLN | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|
| Sales (mn) | 4,430 | 5,517 | 5,680 | 4,794 | 3,503 |
| EBITDA (mn) | 353 | 349 | 234 | 151 | 70 |
| EBIT (mn) | 331 | 319 | 202 | 119 | 38 |
| Net profit a.m. (mn) | 267 | 261 | 196 | 124 | 51 |
| Earnings per share (adj.) | 10.47 | 10.22 | 7.70 | 4.85 | 2.00 |
| EPS adjusted growth | 54.0% | -2.4% | -24.7% | -36.9% | -58.8% |
| Adjusted PE ratio | 9.5 | 7.5 | 11.1 | 17.7 | 42.9 |
| DPS | 8.93 | 8.69 | 6.54 | 4.13 | 1.70 |
| Dividend yield | 9.0% | 11.4% | 7.6% | 4.8% | 2.0% |
| EV/EBITDA | 2.0 | 1.0 | 3.4 | 6.7 | 19.6 |
| Price book value | 3.7 | 2.8 | 3.2 | 3.4 | 3.7 |

*Source: Budimex, Raiffeisen Centrobank estimates*

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Disclosures: www.rcb.at
Supervisory authority: Financial Market Authority
* The indicated price is the last price as available at 6.30 AM on 09.03.12

Raiffeisen RESEARCH

Raiffeisen CENTROBANK

### Share price triggers

| Trigger | Momentum | Explanation |
|---|---|---|
| **PNI restructuring** | neutral | ▪ We assume that the railway segment will be in red for the next two years<br>▪ More efficient and rapid restructuring should result in a valuation boost |
| **EU budget 2014-2020** | neutral | ▪ Budimex positions itself towards benefiting again from EU money flows to Poland<br>▪ This strategy is quite risky given the ongoing eurozone problems<br>▪ Yet, allocation of a similar size to the 2008-2013 budget should result in another re-rating of the construction sector |
| **Strategic positioning** | neutral | ▪ Budimex aims to diversify its revenues source away from the road construction segment, which is expected to decline<br>▪ Some ideas have been presented, yet we have no clarity regarding the potential revenue generation coming from the niches the company wants to explore |

*Source: Raiffeisen Centrobank*

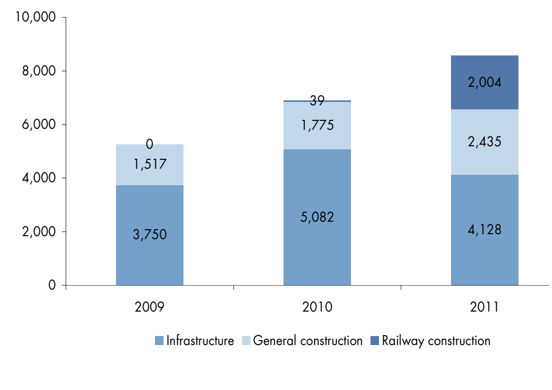
## Company description, strategic positioning

***Repositioning from road to railway construction. Still, however, highly dependent on public investments.***

Budimex is the largest Polish construction company listed on the Warsaw Stock Exchange with respect to market capitalization. Budimex group predominantly concentrates on road construction, with the current road order backlog constituting around 50% of the total portfolio (of PLN 8.6 bn in total). Yet, following the expected massive decrease in spending on roads by the Polish road authorities, the company tries to find its strategic position. After the recent acquisition of PNI – one of the largest Polish railway engineering companies (we estimate its market share to range between 10-15%), the group positions itself toward the expected railway construction boom. The PKP PLK budget looks quite ambitious with respect to railway modernization in Poland (to triple in the years 2014-2015 from last year's level of PLN 3.7 bn). Furthermore, supposedly the EU budget for 2014-2020 is to prioritize modernization of the railway network, vs. new road construction currently. The move per se looks right to us but a) PNI could be potentially a difficult animal to restructure on the back of overemployment and employment guarantees in place and b) the current order backlog quality does not look too appealing and in combination with the high fixed costs of the company, we only expect PNI to break even on operating profitability in 2014. On the other hand, the company possesses a number of non-core assets, predominantly in the form of real estate properties, hence there is potential for extra cash inflow from disposal. Budimex paid PLN 225 mn for the company which holds an order portfolio of PLN 1.3 bn. Please note that Budimex has also managed to win a railway construction contract of PLN 689 mn, yet we believe on margins hovering around 0%.

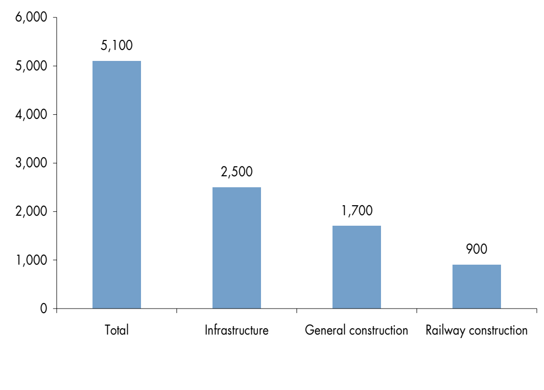
Furthermore, the order backlog consisting of general construction contracts has been dynamically increasing, with the company also diversifying towards the hydro-engineering segment.

### Order backlog development (PLN mn)




*Source: Budimex, Raiffeisen Centrobank*

### Contracts portfolio for 2012 (PLN mn)

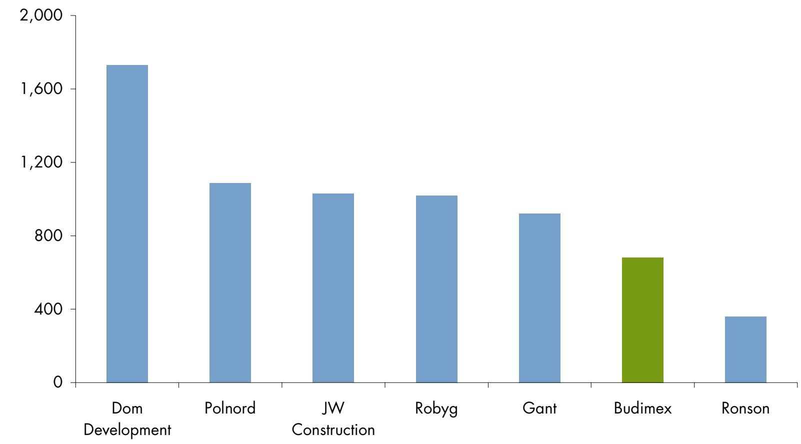



*Source: Budimex, Raiffeisen Centrobank*

***One of the largest residential developers in Poland***

In addition to that, Budimex group has quite a developed residential development subsidiary (Budimex Nieruchomosci), which places it among the top Warsaw-listed residential developers.

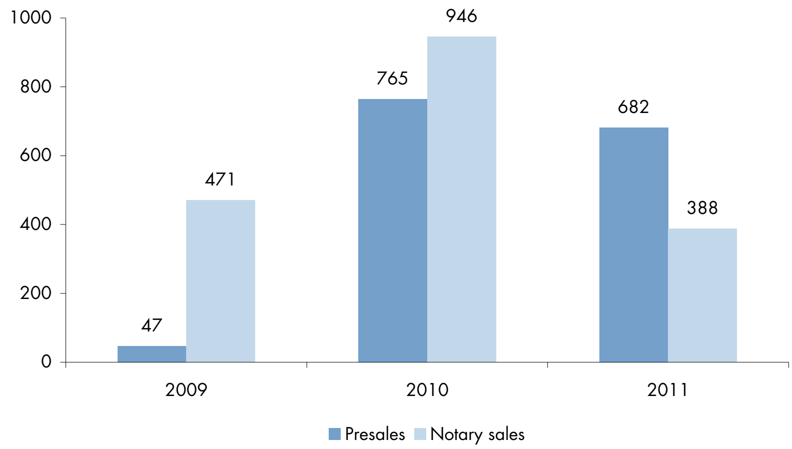
### *2011 residential units pre-sales*




*Source: Companies, Raiffeisen Centrobank*

Last year, Budimex Nieruchomosci managed to pre-sell 682 units and recognized 388 units in the P&L (with a gross profitability amounting to 17%, slightly below the industry average of more than 20%).

### *Pre-sales and notary sales (in units)*



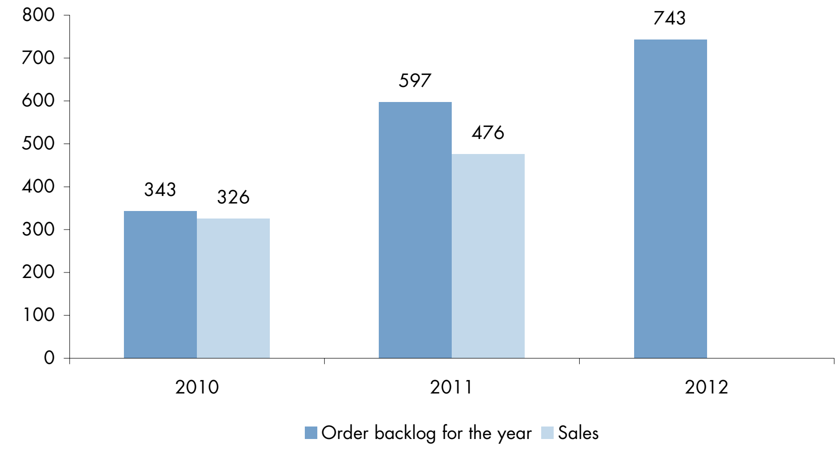

*Source: Budimex, Raiffeisen Centrobank*

Currently, the company has slightly more than 1,600 flats in inventories (70) and under construction (1,558), and 46% thereof are pre-sold. Given the completion schedule (4 out of 6 projects are to be completed this year), we expect a substantial revenue increase in this segment for 2012.

***Increasing wooden houses production, however facing capacity constraints***

Budimex group, in the form of its subsidiary Danwood, carries on construction operations of wooden houses, which so far has been very successful with sales and order backlog substantially rising in the last years. Yet, it looks to us as if the company has encountered capacity constraints, which basically implies no substantial growth in the future. Please note that most of the production is exported to Germany (90% of 2011 sales).

**Danwood in units**




*Source: Budimex, Raiffeisen Centrobank*

Budimex also tries to position itself somehow towards the upcoming power engineering boom, yet the company has no credentials and experience to manage projects of this scale or know-how requirements, hence the management has decided to avoid unnecessary risks (project management) and to rather concentrate on the subcontractor role for general construction elements of the power projects.

Additionally, the company participates in tenders for waste incinerators (the total capex is estimated at PLN 5 bn). Budimex has also arranged a PPP projects management cell (yet we see this sector to be slowly developing), will try to concentrate on facility management (technical maintenance, cleaning, security), road maintenance services (the market is valued at PLN 5 bn annually), railway tracks maintenance (thanks to PNI) as well as waste management activities (also valued at some PLN 5 bn). For this very moment, however, it is difficult to estimate Budimex's potential in the new segments as they are about to emerge only gradually and we assume that a substantial part of the road construction sales will not be offset by the diversification efforts undertaken.

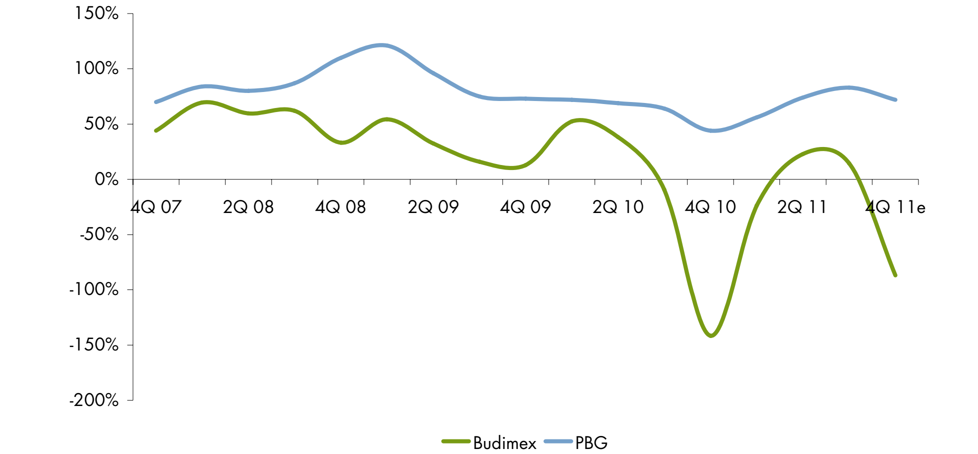
## Balance sheet quality and working capital management

***Great balance sheet quality with a substantial net cash position and an excellent working capital management***

Budimex is the lowest-leverage construction group from the large WSE-listed construction companies. The company reported a massive net cash position amounting to PLN 1.58 bn for end-2011 a a slight decrease yoy (from PLN 1.75 bn), but the figure is quite increasing after the dividend payment of PLN 232 mn and the PNI acquisition of PLN 225 mn.

Furthermore, in terms of both leverage and working capital management the company looks the opposite to other companies that are heavily engaged in road construction, particularly compared to PBG and Polimex-Mostostal (despite the fact that the latter derives only 20-30% of total revenues from road construction vs. around 60% in the case of Budimex). We believe the chart below is predominantly a consequence of the long-term experience Budimex has gained in the road construction sector.

### Working capital investment/equity: Best managed Budimex vs. PBG




*Source: Companies, Raiffeisen Centrobank estimates*

Yet, we have to admit that we are not sure whether Budimex will be able to pass on that working capital management experience to other sectors the company wants to diversify into. Hence, we see a downside risk to the working capital cycle of the company.

Furthermore, as already indicated in the introductory section of this report, Budimex and Mostostal Warszawa, have the highest quality balance sheets with respect to goodwill balances (Budimex PLN 73 mn (11% of the equity) vs. 50% for PBG and 30% for Polimex-Mostostal). Furthermore, this is the only company from those discussed capable of paying dividends from 2011 profits.

## 4Q 11 review

***Strong top line with slightly deteriorating profitability***

Budimex reported a strong set of figures for 4Q 11 topping the street projections in absolute terms, however, in line regarding profitability. The relatively warm weather in 4Q 11 translated into a massive output increase amounting to 33%, with the total top line standing at PLN 1.7 bn. On the other hand, however, Budimex follows the general trend of weakening margins, particularly in the road construction sector on the back of skyrocketing fuel prices (vs. the offer assumptions).

### Budimex's 4Q 11 figures

| In PLN mn | 4Q 11 | 4Q 10 | +/-% | 3Q 11 | +/-% | Consensus | +/-% |
|---|---|---|---|---|---|---|---|
| Sales | 1694.0 | 1,269.6 | 33.4% | 1,573.8 | 7.6% | 1,495.2 | 13.3% |
| Gross profit | 138.9 | 116.8 | 18.9% | 118.3 | 17.4% | n.a. | n.a. |
| EBITDA | n.a. | 77.9 | n.a. | 99.2 | n.a. | 73.5 | n.a. |
| EBIT | 82.5 | 72.0 | 14.6% | 91.5 | -9.9% | 67.1 | 22.9% |
| Net profit | 67.0 | 60.1 | 11.5% | 74.1 | -9.6% | 57.8 | 15.9% |
| Gross margin | 8.2% | 9.2% | | 7.5% | | n.a. | |
| EBITDA margin | n.a. | 6.1% | | 6.3% | | 4.9% | |
| EBIT margin | 4.9% | 5.7% | | 5.8% | | 4.5% | |
| Net margin | 4.0% | 4.7% | | 4.7% | | 3.9% | |

*Source: Budimex, PAP Consensus, Raiffeisen Centrobank*

## Planning model

***High order backlog, repositioning to railway construction, margin contraction expected on overemployed railway engineering arm***

Our planning model is based on the following assumptions:

- Order backlog of PLN 5.1 bn for 2012, thereof PLN 2.5 bn on roads, PLN 0.9 bn on railways (with a negative gross profitability, however) and PLN 1.75 bn on general construction
- Given the completion schedule for residential projects we assume the company to hand over at least 640 residential units (up 65% yoy).

- Given the record high order backlog for the wooden house, but also production capacity constraints we assume approx. 500 units to be sold per annum (vs. 476 in 2011).
- We expect the profitability in the roads segment to decrease on the back of even fiercer competition once the GDDKiA budget gets massively squeezed (starting from 2013 on). We assume the road spendings in Poland to decrease to PLN 2 bn in the years 2014-2015 and then slightly increase based on the new EU budget (please note that GDDKiA has prepared projects for PLN 65 bn).
- We estimate the revenues derived from general construction to slightly come down in 2013 following the current financial turmoil and then slowly to rebound at an annual pace of 5%.
- Given the railway modernization program, we think the company can exceed PLN 1 bn of revenues in the segment (we assume a market share drop from 15% currently to 10% on the back of increasing competition) already in 2014. We think, however, that the segment will be in the reds for the next two years and then the profitability should start gradually improving.
- We do not include any substantial revenues from facility management and waste management yet – segments into which the company wants to expand.

**Budimex planning model**

| In PLN mn | 2011 | 2012e | 2013e | 2014e | Comment |
|---|---|---|---|---|---|
| Roads revenues | 3,155 | 2,500 | 1,678 | 300 | 2012-2013 revenues are backed by already signed contracts, yet from 2014 we assume GDDKiA's spending to decrease from around PLN 30 bn planned for 2012 to only PLN 2 bn |
| Railway revenues | 100 | 900 | 980 | 1,040 | We price in a 10% market share of PNI as well as rising PKP PLK spending on railway construction |
| General construction revenues | 1,753 | 1,683 | 1,599 | 1,678 | We expect a slight drop for the years 2012-2013 following a slowdown in GDP growth. The 2012 figure, however, is fully backed by the current order backlog |
| Residential revenues | 247 | 322 | 263 | 209 | We assume notary sales of 644 units in 2012, 525 in 2013 and 418 in 2014 based on the current project pipeline |
| Other revenues (Danwood) | 261 | 275 | 275 | 275 | The company should manage to sell 500 units per annum given the strong order backlog and production capacity limits |
| Total revenues | 5,516 | 5,680 | 4,794 | 3,503 | |
| Gross profit | 469 | 379 | 296 | 212 | We assume roads profitability to remain in line with 2011 figures, however, the railway segment to remain in the reds for the next 2 years squeezing the total margin, particularly in the light of growing importance of the railway segment in the sales mix |
| Gross profit margin | 8.5% | 6.7% | 6.2% | 6.1% | |
| EBIT | 319 | 202 | 119 | 38 | 2014 will be impacted by a substantial cut in road spendings combined with an increasing share of railway construction (with projected improving profitability, however) |
| EBIT margin | 5.8% | 3.6% | 2.5% | 1.1% | |
| EBITDA | 349 | 234 | 151 | 70 | |
| EBITDA margin | 6.3% | 4.1% | 3.2% | 2.0% | |
| Net profit | 261 | 196 | 124 | 51 | |
| Net margin | 4.7% | 3.5% | 2.6% | 1.5% | |

*Source: Budimex, Raiffeisen Centrobank estimates*

## RCB vs. consensus estimates

***We are more bullish than the consensus on sales, yet the street seems not to price in the railway section being in the reds for the next two years***

We are much more optimistic than the street in terms of 2012e top line projections (19% difference). Please note that the order backlog in the construction segment only (excluding the residential units and wooden houses production) amounts to PLN 5.1 bn for 2012, i.e. slightly higher than the street's total revenues view. Hence we expect some upgrades here. On the other hand, however, we are much more cautious on profitability. We think the consensus does not account for a very low (in our projections slightly negative) profitability of the railway unit (as well as on the contract signed by Budimex on its own) and the increasing share of the railway construction part in the total sales mix. Obviously, we think the consensus will come down with its estimates once the fully consolidated figures (with PNI) are reported (1Q 11).

### RCB vs. Consensus on Budimex estimates

| | RCB | | Consensus | |
|---|---|---|---|---|
| In PLN mn | 2012e | 2013e | 2012e | 2013e |
| Revenues | 5,680 | 4,794 | 5,056 | 4,663 |
| EBITDA | 234 | 151 | 268 | 238 |
| EBITDA margin | 4.1% | 3.2% | 5.3% | 5.1% |
| EBIT | 202 | 119 | 240 | 204 |
| EBIT margin | 3.6% | 2.5% | 4.8% | 4.4% |
| Net income | 196 | 124 | 203 | 171 |
| Net margin | 3.5% | 2.6% | 4.0% | 3.7% |

*Source: Budimex, Raiffeisen Centrobank estimates*

**Risks**

***Upside risks dominate in our view***

Obviously the biggest risk in our view is a further margin squeeze below the levels projected in the planning model as well as a delay in the railway modernization program.

We, however, see a couple of upside risks to the company. Namely, there is a number of niches Budimex wants to explore like the already mentioned facility management, PPP, waste management, etc. potentially substantially improving the revenues profile in the years to come (not 2012, however). Furthermore, we believe that the company may restructure PNI in a more efficient way than expected by us and give a massive boost to its profitability.

## Valuation

***"Hold" recommendation with a 12-month TP of PLN 96***

As indicated in the introductory section, Budimex seems to be fairly priced (with a discount on EV/EBIT basis) given the deteriorating prospects of the company's core business – road construction. We also apply a DCF approach which yields a 12-month target price of PLN 95 (PLN 87 ex-dividend), which given the limited upside triggers a "hold" recommendation. We believe this recommendation fully justifies our view of a rather unclear outlook for the company post the road boom and the question of where it is going to position itself.

## DCF Valuation

| FCF projection (PLN mn) | 2012e | 2013e | 2014e | 2015e | 2016e | 2017e | TV CF |
|---|---|---|---|---|---|---|---|
| **Consolidated sales** | **5,680** | **4,794** | **3,503** | **3,587** | **3,975** | **4,097** | **4,535** |
| EBITDA | 234 | 151 | 70 | 93 | 139 | 144 | 162 |
| EBITA | 202 | 119 | 38 | 61 | 107 | 112 | 130 |
| Taxes paid on EBITDA | -46 | -29 | -7 | -12 | -20 | -21 | -25 |
| **NOPLAT** | **164** | **97** | **31** | **50** | **87** | **91** | **105** |
| Adj. NOPLAT | 164 | 97 | 31 | 50 | 87 | 91 | 105 |
| Depreciation of PPE & intangibles | 32 | 32 | 32 | 32 | 32 | 32 | 32 |
| Gross investment in PPE & intangibles | -35 | -35 | -35 | -35 | -35 | -35 | -36 |
| Change in working capital | -176 | -114 | -167 | 15 | 70 | 22 | 20 |
| NWC/Sales | -18.1% | -18.0% | -17.9% | -17.9% | -17.9% | -17.9% | -18% |
| Change in LT provisions other than tax | 4 | 0 | -50 | n.a. | n.a. | n.a. | |
| Net acquisitions & disposals | 0 | 0 | 0 | 0 | 0 | 0 | |
| Free cash flow to firm | -12 | -21 | -189 | 62 | 153 | 110 | 121 |
| **Adj. free cash flow to firm** | **-12** | **-21** | **-189** | **62** | **153** | **110** | **121** |
| **EV DCF, mid-year assumption** | **1,066** | **1,193** | | | | | |
| + MV of non-operating assets eop | 14 | 14 | | | | | |
| - MV of net debt eop | -1,387 | -1,164 | | | | | |
| - MV of minorities eop | 0 | 0 | | | | | |
| Adjustments to EV eop | 0.0 | 0.0 | | | | | |
| **Fair value of equity** | **2,466** | **2,372** | | | | | |
| Shares outstanding (mn) | 26 | 26 | | | | | |
| **Fair value per share (in PLN)** | **96.60** | **92.89** | | | | | |

| Value drivers | 2012e | 2013e | 2014e | 2015e | 2016e | 2017e | TV CF |
|---|---|---|---|---|---|---|---|
| Consolidated sales yoy | 3.0% | -15.6% | -26.9% | 2.4% | 10.8% | 3.1% | 2.5% |
| EBITDA margin | 4.1% | 3.2% | 2.0% | 2.6% | 3.5% | 3.5% | 3.6% |
| Rate of taxes paid | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% |
| Working capital/sales | -18.1% | -18.0% | -17.9% | -17.9% | -17.9% | -17.9% | -17.9% |
| Capex/depreciation | 110.0% | 110.0% | 110.0% | 110.0% | 110.0% | 110.0% | 112.8% |
| Free cash flow margin | -0.2% | -0.4% | -5.4% | 1.7% | 3.9% | 2.7% | 2.7% |

| WACC | 2012e | 2013e | 2014e | 2015e | 2016e | 2017e | TV CF |
|---|---|---|---|---|---|---|---|
| Target capital structure (at MV) | 90.0% | 90.0% | 90.0% | 90.0% | 90.0% | 90.0% | 90.0% |
| Debt/equity ratio (at MV) | 11.1% | 11.1% | 11.1% | 11.1% | 11.1% | 11.1% | 11.1% |
| Risk free rate (local) | 4.4% | 5.1% | 5.1% | 5.7% | 5.7% | 5.4% | 4.8% |
| Equity market premium | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% |
| Levered beta | 1.1 | 1.1 | 1.1 | 1.1 | 1.1 | 1.1 | 1.1 |
| Cost of equity | 9.9% | 10.6% | 10.6% | 11.2% | 11.2% | 10.9% | 10.3% |
| Cost of debt | 5.4% | 6.1% | 6.1% | 6.7% | 6.7% | 6.4% | 5.8% |
| Tax rate | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% |
| **WACC** | **9.3%** | **10.0%** | **10.1%** | **10.6%** | **10.6%** | **10.3%** | **9.7%** |

## Sensitivity analysis

| Growth sensitivity (PLN) | | | Terminal growth rate | | | | |
|---|---|---|---|---|---|---|---|
| **WACC** | **1.0%** | **1.5%** | **2.0%** | **2.5%** | **3.0%** | **3.5%** | **4.0%** |
| 8.2% | 100.4 | 103.4 | 106.9 | 111.0 | 115.9 | 121.9 | 129.2 |
| 8.7% | 96.5 | 99.1 | 102.0 | 105.4 | 109.4 | 114.2 | 120.0 |
| 9.2% | 93.1 | 95.3 | 97.8 | 100.7 | 104.0 | 107.9 | 112.5 |
| 9.7% | 90.2 | 92.0 | 94.2 | **96.6** | 99.4 | 102.6 | 106.4 |
| 10.2% | 87.5 | 89.2 | 91.0 | 93.1 | 95.4 | 98.1 | 101.3 |
| 10.7% | 85.2 | 86.6 | 88.2 | 90.0 | 92.0 | 94.3 | 96.9 |
| 11.2% | 83.0 | 84.3 | 85.7 | 87.2 | 89.0 | 90.9 | 93.2 |

| Margin sensitivity (PLN) | | | FCF margin TV | | | | |
|---|---|---|---|---|---|---|---|
| **WACC** | **1.2%** | **1.7%** | **2.2%** | **2.7%** | **3.2%** | **3.7%** | **4.2%** |
| 8.2% | 83.7 | 92.8 | 101.9 | 111.0 | 120.1 | 129.2 | 138.3 |
| 8.7% | 81.1 | 89.2 | 97.3 | 105.4 | 113.5 | 121.7 | 129.8 |
| 9.2% | 78.9 | 86.1 | 93.4 | 100.7 | 108.0 | 115.2 | 122.5 |
| 9.7% | 76.9 | 83.5 | 90.0 | **96.6** | 103.2 | 109.7 | 116.3 |
| 10.2% | 75.2 | 81.2 | 87.1 | 93.1 | 99.0 | 105.0 | 110.9 |
| 10.7% | 73.7 | 79.1 | 84.6 | 90.0 | 95.4 | 100.8 | 106.2 |
| 11.2% | 72.4 | 77.4 | 82.3 | 87.2 | 92.2 | 97.1 | 102.1 |

*Source: Raiffeisen Centrobank estimates*

| Income statement (PLN mn) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| **Consolidated sales** | **3,290** | **4,430** | **5,517** | **5,680** | **4,794** | **3,503** |
| Cost of sales | -2,877 | -3,946 | -5,055 | -5,300 | -4,498 | -3,290 |
| **Gross profit** | **413** | **484** | **462** | **379** | **296** | **212** |
| Other operating income | 71 | 85 | 67 | 0 | 0 | 0 |
| Selling expenses | -23 | -23 | -24 | -25 | -21 | -16 |
| Administrative expenses | -129 | -123 | -149 | -152 | -155 | -158 |
| Other operating expenses | -131 | -91 | -35 | 0 | 0 | 0 |
| **EBITDA** | **222** | **353** | **349** | **234** | **151** | **70** |
| Adjusted EBITDA | 222 | 353 | 349 | 234 | 151 | 70 |
| Depreciation of PPE and intangibles | -21 | -21 | -30 | -32 | -32 | -32 |
| **EBITA** | **201** | **331** | **319** | **202** | **119** | **38** |
| Amortisation, impairment of goodwill | 0 | 0 | 0 | 0 | 0 | 0 |
| **EBIT** | **201** | **331** | **319** | **202** | **119** | **38** |
| Adjusted EBIT | 201 | 331 | 319 | 202 | 119 | 38 |
| Investment income | 0 | 0 | 0 | 0 | 0 | 0 |
| Net interest income | 22 | 4 | 6 | 42 | 35 | 26 |
| Other financial result | 2 | -3 | -3 | -1 | -1 | -1 |
| **Financial result** | **24** | **0** | **3** | **41** | **34** | **25** |
| **Earnings before taxes** | **224** | **332** | **322** | **243** | **153** | **63** |
| Taxes on income | -51 | -64 | -61 | -46 | -29 | -12 |
| Extraordinary result | 0 | 0 | 0 | 0 | 0 | 0 |
| **Net profit before minorities** | **174** | **267** | **261** | **196** | **124** | **51** |
| Minority interests | 0 | 0 | 0 | 0 | 0 | 0 |
| **Net profit after minorities** | **174** | **267** | **261** | **196** | **124** | **51** |
| Adjusted Net profit | 174 | 267 | 261 | 196 | 124 | 51 |

| Changes yoy | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| Consolidated sales yoy | -1.8% | 34.7% | 24.5% | 3.0% | -15.6% | -26.9% |
| EBITDA yoy | 65.3% | 59.0% | -0.9% | -33.1% | -35.3% | -53.6% |
| EBITA yoy | 78.7% | 65.3% | -3.6% | -36.8% | -40.9% | -67.9% |
| EBIT yoy | 78.7% | 65.3% | -3.6% | -36.8% | -40.9% | -67.9% |
| EBT yoy | 60.7% | 48.0% | -2.9% | -24.7% | -36.9% | -58.8% |
| Net profit after minorities yoy | 65.8% | 54.0% | -2.4% | -24.7% | -36.9% | -58.8% |

| Margins | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| Gross margin | 12.5% | 10.9% | 8.4% | 6.7% | 6.2% | 6.1% |
| EBITDA margin | 6.7% | 8.0% | 6.3% | 4.1% | 3.2% | 2.0% |
| EBITA margin | 6.1% | 7.5% | 5.8% | 3.6% | 2.5% | 1.1% |
| EBIT margin | 6.1% | 7.5% | 5.8% | 3.6% | 2.5% | 1.1% |
| EBT margin | 6.8% | 7.5% | 5.8% | 4.3% | 3.2% | 1.8% |
| Net margin | 5.3% | 6.0% | 4.7% | 3.5% | 2.6% | 1.5% |

| Profitability | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| Return on assets | 6.3% | 8.0% | 6.2% | 4.6% | 3.1% | 1.7% |
| Return on equity | 28.2% | 42.2% | 37.5% | 28.2% | 18.7% | 8.3% |
| Return on capital employed | 20.7% | 37.3% | 34.0% | 24.8% | 16.6% | 7.8% |

| Cash flow statement (PLN mn) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| **Earnings before taxes** | **224** | **332** | **322** | **243** | **153** | **63** |
| Taxes paid | -101 | -101 | -194 | -46 | -29 | -12 |
| Amortisation and depreciation | 21 | 21 | 32 | 32 | 32 | 32 |
| Other non-cash items | 492 | 299 | -102 | 4 | 0 | -50 |
| **Cash flow from result** | **637** | **551** | **58** | **232** | **156** | **33** |
| Change in working capital | 400 | 640 | -446 | -167 | -162 | -236 |
| **Operating cash flow** | **1,036** | **1,191** | **-388** | **65** | **-6** | **-203** |
| Capex PPE and intangible assets | -307 | -8 | -41 | -35 | -35 | -35 |
| Acquisitions | 0 | 0 | 0 | 0 | 0 | 0 |
| Disposal of fixed assets (total) | -72 | 0 | 0 | 0 | 0 | 0 |
| Other items (investments) | 2 | 2 | 19 | -2 | 9 | 13 |
| **Investing cash flow** | **-376** | **-5** | **-22** | **-37** | **-27** | **-23** |
| Dividend payments | -149 | -174 | -228 | -222 | -167 | -105 |
| Other changes in equity | 0 | 0 | 0 | 0 | 0 | 0 |
| Change in financial liabilities | -105 | -281 | -31 | 8 | 0 | 0 |
| Other items | 0 | 0 | -140 | 4 | -23 | -34 |
| **Financing cash flow** | **-254** | **-455** | **-398** | **-210** | **-190** | **-139** |

*Source: Budimex, Raiffeisen Centrobank estimates*

| Balance sheet (PLN mn) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| **Current assets** | **2,822** | **3,434** | **3,730** | **3,812** | **3,232** | **2,346** |
| Liquid funds | 1,130 | 1,862 | 1,688 | 1,507 | 1,284 | 920 |
| Receivables | 525 | 550 | 917 | 1,136 | 959 | 701 |
| Inventories | 1,129 | 991 | 1,103 | 1,136 | 959 | 701 |
| Other assets | 38 | 31 | 22 | 33 | 30 | 25 |
| **Fixed assets** | **276** | **276** | **284** | **289** | **283** | **274** |
| Property, plant & equipment | 107 | 113 | 124 | 127 | 130 | 134 |
| Intangible assets | 0 | 0 | 0 | 0 | 0 | 0 |
| Goodwill | 73 | 73 | 73 | 73 | 73 | 73 |
| Financial assets | 96 | 89 | 87 | 88 | 80 | 67 |
| **Deferred tax assets** | **242** | **357** | **313** | **313** | **313** | **313** |
| **Total assets** | **3,340** | **4,067** | **4,327** | **4,414** | **3,828** | **2,933** |
| **Current liabilities** | **2,335** | **3,132** | **3,256** | **3,351** | **2,832** | **2,074** |
| Short-term borrowings | 63 | 18 | 20 | 20 | 20 | 20 |
| Notes & trade payables, payments received | 2,029 | 2,830 | 2,940 | 3,027 | 2,555 | 1,867 |
| Other current liabilities | 243 | 284 | 295 | 304 | 256 | 187 |
| **Long-term liabilities** | **418** | **255** | **362** | **378** | **355** | **272** |
| Long-term borrowings | 230 | 13 | 92 | 100 | 100 | 100 |
| Long-term provisions | 83 | 106 | 127 | 131 | 131 | 81 |
| Other long-term liabilities | 105 | 136 | 143 | 148 | 125 | 91 |
| **Hybrid & other mezzanine capital** | **0** | **0** | **0** | **0** | **0** | **0** |
| **Shareholders' equity** | **586** | **680** | **709** | **684** | **641** | **587** |
| **Minority interests** | **0** | **0** | **0** | **0** | **0** | **0** |
| **Deferred tax liabilities** | **0** | **0** | **0** | **0** | **0** | **0** |
| **Total liabilities** | **3,340** | **4,067** | **4,327** | **4,414** | **3,828** | **2,933** |

| Balance sheet (PLN mn) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| Net working capital | -581 | -1,542 | -1,193 | -1,026 | -864 | -629 |
| Net interest-bearing debt | -837 | -1,832 | -1,576 | -1,387 | -1,164 | -800 |
| Capital employed | 879 | 711 | 821 | 804 | 761 | 707 |
| Market capitalisation | 1,864 | 2,540 | 1,953 | 2,190 | 2,190 | 2,190 |
| Enterprise value | 1,006 | 693 | 363 | 790 | 1,012 | 1,377 |

| Financing (x) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| Interest cover | 12.3 | 10.8 | n.a. | 45.3 | 26.5 | 14.0 |
| Internal financing ratio | 3.4 | 156.7 | -9.6 | 1.8 | -0.2 | -5.8 |
| Net gearing | -142.8% | -269.2% | -222.1% | -202.7% | -181.6% | -136.3% |
| Quick ratio | 0.7 | 0.8 | 0.8 | 0.8 | 0.8 | 0.8 |
| Fixed assets cover | 3.6 | 3.4 | 3.8 | 3.7 | 3.5 | 3.1 |
| Capex / depreciation | 14.5 | 0.4 | 1.4 | 1.1 | 1.1 | 1.1 |
| Equity ratio | 17.6% | 16.7% | 16.4% | 15.5% | 16.7% | 20.0% |

| Per share data (PLN) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| Weighted avg. no. of shares (mn) | 25.5 | 25.5 | 25.5 | 25.5 | 25.5 | 25.5 |
| EPS reported | 6.80 | 10.47 | 10.22 | 7.70 | 4.85 | 2.00 |
| Earnings per share (adj.) | 6.80 | 10.47 | 10.22 | 7.70 | 4.85 | 2.00 |
| Operating cash flow per share | 40.58 | 46.66 | -15.20 | 2.54 | -0.23 | -7.94 |
| Book value per share | 22.96 | 26.65 | 27.79 | 26.80 | 25.11 | 22.98 |
| DPS | 6.80 | 8.93 | 8.69 | 6.54 | 4.13 | 1.70 |
| Payout ratio | 100.0% | 85.2% | 85.0% | 85.0% | 85.0% | 85.0% |

| Valuation (x) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| PE reported | 10.7 | 9.5 | 7.5 | 11.1 | 17.7 | 42.9 |
| Adjusted PE ratio | 10.7 | 9.5 | 7.5 | 11.1 | 17.7 | 42.9 |
| Price cash flow | 1.8 | 2.1 | -5.0 | 33.8 | -381.3 | -10.8 |
| Price book value | 3.2 | 3.7 | 2.8 | 3.2 | 3.4 | 3.7 |
| Dividend yield | 9.3% | 9.0% | 11.4% | 7.6% | 4.8% | 2.0% |
| Free cash flow yield | 39.1% | 46.6% | -22.0% | 1.4% | -1.9% | -10.9% |
| EV/sales | 0.3 | 0.2 | 0.1 | 0.1 | 0.2 | 0.4 |
| EV/EBITDA | 4.5 | 2.0 | 1.0 | 3.4 | 6.7 | 19.6 |
| EV/EBIT | 5.0 | 2.1 | 1.1 | 3.9 | 8.5 | 36.0 |
| EV/operating cash flow | 1.0 | 0.6 | -0.9 | 12.2 | -176.2 | -6.8 |
| Adjusted EV/CE | 2.5 | 3.6 | 2.5 | 2.9 | 3.0 | 3.3 |
| Adjusted EV/CE vs. ROCE/WACC | | | 0.0 | 1.1 | 1.8 | 4.2 |

*Source: Budimex, Raiffeisen Centrobank estimates*

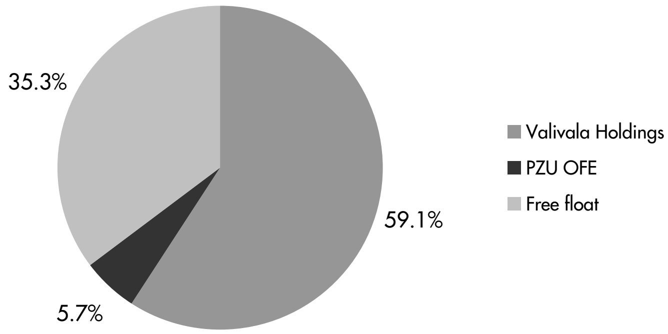
# Budimex

## Fact Sheet

### *Company description*

Budimex's history started in 1968, when the "Budimex Construction Foreign Trade Center" was established. The company was privatized in 1992 and was transferred into a joint stock company two years later before Budimex was listed on the Warsaw Stock Exchange in 1995. Since the year 2000 the Spanish Ferrovial Group has been holding a controlling stake in Budimex which currently amounts to 59.1%. Ferrovial has repeatedly communicated that there are no plans to take over the outstanding shares and delist the company. Budimex is the second largest Polish construction company in terms of sales and the largest in terms of the market capitalization. Being heavily geared towards the Polish home market and to infrastructure projects Budimex is an attractive play on the largest CEE economy and the current heavy infrastructure investments. Budimex provides a wide range of construction services such as civil engineering with the focus on road construction and building construction for industrial and public facilities, commercial & retail facilities and also environmental construction works. Budimex participates in construction projects as both a general contractor or as a sub-contractor. Ontop of this the company pursues own development projects with the main objective of immediate sales upon completion.

### *Shareholder structure*




### *Strengths/Opportunities*

- Virtual pure play on the Polish construction industry and infrastructure investments
- Good visibility thanks to an order backlog of about PLN 8.6 bn at eop 4Q 11 and conversion of 65-70% into revenues in 2011e
- Increasing real estate development activity
- Attractive dividend play with high net cash position
- Excellent working capital management
- Diversification towards railway construction

### *Weaknesses/Threats*

- High dependance on public-financed infrastructure projects
- Expected massive decrease in roads contruction output
- No clear path yet with respect to dropping road revenues substitution
- Risk of lack of competences in the new sectors currently being expolored

| *Income statement (PLN mn)* | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|
| Consolidated sales | 5,517 | 5,680 | 4,794 | 3,503 |
| EBITDA | 349 | 234 | 151 | 70 |
| EBIT | 319 | 202 | 119 | 38 |
| EBT | 322 | 243 | 153 | 63 |
| Net profit bef. min. | 261 | 196 | 124 | 51 |
| Net profit after min. | 261 | 196 | 124 | 51 |
| ***Balance sheet*** | | | | |
| Total assets | 4,327 | 4,414 | 3,828 | 2,933 |
| Shareholders' equity | 709 | 684 | 641 | 587 |
| Goodwill | 73 | 73 | 73 | 73 |
| NIBD | -1,576 | -1,387 | -1,164 | -800 |
| ***Cash flow statement*** | | | | |
| Operating cash flow | -388 | 65 | -6 | -203 |
| Investing cash flow | -22 | -37 | -27 | -23 |
| Change NIBD | -256 | -189 | -222 | -364 |

| *Per share data (PLN)* | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|
| EPS pre-goodwill | 10.22 | 7.70 | 4.85 | 2.00 |
| Adj. EPS diluted | 10.22 | 7.70 | 4.85 | 2.00 |
| Operating cash flow | -15.20 | 2.54 | -0.23 | -7.94 |
| Book value | 27.79 | 26.80 | 25.11 | 22.98 |
| Dividend | 8.69 | 6.54 | 4.13 | 1.70 |
| Payout ratio | 85.0% | 85.0% | 85.0% | 85.0% |
| ***Valuation (x)*** | | | | |
| PE pre-goodwill | 7.5 | 11.1 | 17.7 | 42.9 |
| Adj. PE diluted | 7.5 | 11.1 | 17.7 | 42.9 |
| Price cash flow | -5.0 | 33.8 | -381.3 | -10.8 |
| Price book value | 2.8 | 3.2 | 3.4 | 3.7 |
| Dividend yield | 11.4% | 7.6% | 4.8% | 2.0% |
| FCF yield | -22.0% | 1.4% | -1.9% | -10.9% |
| EV/EBITDA | 1.0 | 3.4 | 6.7 | 19.6 |
| EV/EBIT | 1.1 | 3.9 | 8.5 | 36.0 |
| EV/operating CF | -0.9 | 12.2 | -176.2 | -6.8 |

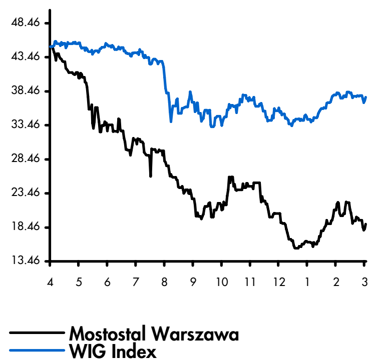
*Source: Budimex, Raiffeisen Centrobank estimates*

# Company Update
## Mostostal Warszawa

March 9, 2012 | Construction & Materials/Poland

### Buy

| | |
|---|---|
| Price 08.03.12* | 18.97 |
| Price target | 30.00 |
| Volatility risk | medium |
| Year high/low | 45.00/15.40 |
| Currency | PLN |
| PLN/EUR | 4.10 |
| GDR rate | n.a. |
| Shares outstanding eoy in mn | 20.00 |
| Market capitalisation (total shares) in EUR mn | 92.6 |
| Free float | 23.8% |
| Free float in EUR mn | 22.0 |
| Avg. daily turnover (12 m) in EUR mn | 0.08 |
| Index | WIG |
| ISIN code | PLMSTWS00019 |
| Bloomberg | MSW PW |
| Reuters | MOWA.WA |
| www.mostostal.waw.pl | |




*Source: Raiffeisen Centrobank*

## Earnings momentum expected

We significantly raise our target price for Mostostal Warszawa to PLN 30 and upgrade the stock to "buy", following the valuation convergence, depressed valuation vs. the Polish peers particularly on a 2013 basis and expected earnings momentum. We would not be surprised if Mostostal Warszawa's profitability overshoots our estimates in 2012 after the substantial recognition of reserves on losses in the 4Q 11 figures, predominantly on the cash-burning and probably loss-generating highway construction contracts. Furthermore, we recognize the quality of Mostostal Warszawa's balance sheet and expect the net debt position to reverse already in 4Q 11 and to strengthen further towards the end of 2012 on the back of the completion of road construction contracts. We also recognize the company's credentials in the power engineering segment and expect it to benefit from the upcoming boom as a general contractor (like in the recently awarded Opole power plant construction contract) or as a subcontractor. We see the company to selectively approach the ongoing power tenders and also somehow appreciate the conservative approach given the risks related to the general contractor position in such massive projects (no company has ever run power projects valued at PLN 8-10 bn). We also see the company positioning itself towards the construction of waste incinerators. Mostostal Warszawa also tries to benefit from railway contracts, yet we see it more as a general construction company as a consequence of the lack of the right know-how and machinery.

**4Q 11 preview:** The figures (to be published on March 20) should be substantially impacted by the losses on road construction contracts estimated and charged against the P&L, predominantly on the back of massive increase in construction materials and transportation costs (shortage of transportation capacities for the aggregate, increasing oil prices lifting asphalt costs, etc). Hence, we expect the company to report negative EBIT of almost PLN 50 mn and a net loss of PLN 42 mn. On the other hand, we see a boost to the top line from the warm weather recorded in 4Q 11, and we see the top line up a massive 60% yoy. Our previous 2011 top line estimates are expected to be overshot by more than 7%. We also expect the company to reverse its temporary net debt position (only for two quarters).

**Recommendation and valuation:** We are closing our bet on Mostostal Warszawa's valuation convergence and at this moment we would position ourselves towards the earnings momentum expected. The company is to substantially improve its profits in the years to come (no more low-margin/loss-making road contracts, more power engineering), and based on our estimates will report the highest earnings momentum from all the Polish construction companies. Our DCF model yields a 12-month target price of PLN 30 (from PLN 19.6) and we upgrade our recommendation to "buy".

### Key figures and ratios

| PLN | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|
| Sales (mn) | 2,712 | 2,570 | 3,450 | 3,031 | 2,627 |
| EBITDA (mn) | 209 | 120 | -24 | 75 | 99 |
| EBIT (mn) | 181 | 84 | -66 | 29 | 48 |
| Net profit a.m. (mn) | 117 | 62 | -59 | 20 | 41 |
| Earnings per share (adj.) | 5.87 | 3.12 | -2.96 | 0.98 | 2.06 |
| EPS adjusted growth | 44.6% | -46.7% | -194.7% | n.a. | 109.9% |
| Adjusted PE ratio | 10.4 | 19.6 | -5.4 | 19.3 | 9.2 |
| DPS | 1.40 | 0.55 | 0.00 | 0.25 | 0.52 |
| Dividend yield | 2.3% | 0.9% | 0.0% | 1.3% | 2.7% |
| EV/EBITDA | 4.5 | 7.8 | -19.5 | 2.9 | 1.9 |
| Price book value | 2.5 | 2.4 | 0.7 | 0.8 | 0.8 |

*Source: Mostostal Warszawa, Raiffeisen Centrobank estimates*

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Disclosures: www.rcb.at
Supervisory authority: Financial Market Authority
* The indicated price is the last price as available at 6.30 AM on 09.03.12

### Share price triggers

| Trigger | Momentum | Explanation |
|---|---|---|
| **Earnings momentum** | positive | ▪ After substantial losses to be recorded in 4Q 11, we expect Mostostal Warszawa to report the highest earnings momentum<br>▪ We also see an upside risk to the road contracts that had been written-off on potential claims for additional work |
| **Power engineering** | positive | ▪ The company very selectively approaches the ongoing tenders in order to keep the participation costs at a minimum<br>▪ We see high chances of its subsidiaries, however, to participate in the boom regarding subcontractors' work and hence diminishing the contracts' execution risk |
| **Competition** | negative | ▪ Mostostal Warszawa seems to be suffering the most on the back of fierce competition on the Polish market<br>▪ A substantial share of its order backlog consists of low-margin/low-value general construction projects, where we consider the competition to be among the highest due to relatively low barriers of entry |

*Source: Raiffeisen Centrobank*

## 4Q 11 preview

***Massive top line increase expected, yet profitability to be impacted by loss recognition on road contracts***

The last quarter of 2011 is supposed to be a quarter characterised by contract profitability revision, where we believe that substantial losses on highway and expressway construction contracts will be charged against the P&L, where the company mismanaged the pressure on rising building materials and transportation costs. Despite an impressive 60% top line increase (relatively warm 4Q 11 and high order backlog), we expect the EBIT margin to be negative at 4.6%. We see the EBIT loss to amount to PLN 49.5 mn, forecast an EBITDA loss of PLN 39 mn and the net loss to come to PLN 42.5 mn. We also expect a reversal of the net debt position as a consequence of seasonally decreasing working capital and predominantly the receivables balance.

### Mostostal Warszawa 4Q 11 preview

| In PLN mn | 4Q 11e | 4Q 10 | +/-% | 3Q 11 | +/-% |
|---|---|---|---|---|---|
| Revenues | 1,083 | 682 | 59% | 941 | 15% |
| Gross profit | -32 | 29 | -212% | -8 | 295% |
| EBIT | -49 | 12 | -507% | -28 | 77% |
| EBITDA | -39 | 21 | -285% | -17 | 123% |
| Net income a.m. | -42 | 7 | -746% | -25 | 68% |
| Gross profit margin | -3.0% | 2.7% | | -0.8% | |
| EBIT margin | -4.6% | 1.1% | | -2.6% | |
| EBITDA margin | -3.6% | 1.9% | | -1.6% | |
| Net margin | -3.9% | 0.6% | | -2.3% | |

*Source: Mostostal Warszawa, Raiffeisen Centrobank estimates*

## Planning model

***Opole power plant to boost revenues and profitability from 2013 on***

We have modified our planning model on the back of a still massive order backlog amounting to PLN 3.7 bn at the end of last year (excluding the Opole construction power plant contract of PLN 9.4 bn, with Mostostal Warszawa's share amounting to 24%), thereof we estimate almost PLN 3 bn to be worked through in 2012. Furthermore, we assume a negative margin (of -1%) on the remaining road construction contracts (PLN 490 mn remaining at the end of 2011), 4% average gross margin on other contracts and a 10% gross margin on the Opole power plant construction contract with substantial revenues kicking in from 2013 only and peaking in 2015.

### Mostostal Warszawa planning model

| | Old | | | New | | |
|---|---|---|---|---|---|---|
| In PLN mn | 2011e | 2012e | 2013e | 2011e | 2012e | 2013e |
| Revenues | 3,213 | 2,892 | 2,602 | 3,450 | 3,031 | 2,627 |
| Gross profit | 96 | 110 | 130 | 7 | 101 | 122 |
| Gross profit margin | 3.0% | 3.8% | 5.0% | 0.2% | 3.3% | 4.6% |
| EBIT | 23 | 34 | 53 | -66 | 29 | 48 |
| EBIT margin | 0.7% | 1.2% | 2.0% | -1.9% | 0.9% | 1.8% |
| EBITDA | 61 | 77 | 100 | -24 | 75 | 99 |
| EBITDA margin | 1.9% | 2.7% | 3.8% | -0.7% | 2.5% | 3.8% |
| Net income a.m. | 14 | 23 | 42 | -59 | 20 | 41 |
| Net income margin | 0.4% | 0.8% | 1.6% | -1.7% | 0.6% | 1.6% |

*Source: Raiffeisen Centrobank estimates*

*In line with consensus on 2012e, yet more cautious on 2013e*

**RCB vs. Consensus**

We are quite in line with the consensus estimates on 2012, however, remain more cautious on profitability from 2013 on, on the basis of expected fierce competition in the general construction segment.

**RCB vs. Consensus on Mostostal Warszawa**

| | RCB | | Consensus | |
|---|---|---|---|---|
| In PLN mn | 2012e | 2013e | 2012e | 2013e |
| Revenues | 3,031 | 2,627 | 2,940 | 2,779 |
| EBITDA | 75 | 99 | 76 | 115 |
| EBITDA margin | 2.5% | 3.8% | 2.6% | 4.1% |
| EBIT | 29 | 48 | 35 | 74 |
| EBIT margin | 0.9% | 1.8% | 1.2% | 2.7% |
| Net income a.m. | 20 | 41 | 23 | 53 |
| Net income margin | 0.6% | 1.6% | 0.8% | 1.9% |

*Source: Bloomberg, Raiffeisen Centrobank estimates*

## Valuation

*Upgrade to "buy" with a 12-month target price of PLN 30*

Following our paper on the construction companies' valuation convergence towards the European peers published in May 2011 ("Still too expensive"), Mostostal Warszawa's share price has almost halved. Now, the stock looks attractively priced for us and we see a substantial earnings momentum potential lying ahead of the company after an expected very poor 4Q 11. We apply our DCF valuation approach, which yields a 12-month target price of PLN 30, which given the upside potential triggers the recommendation change from "reduce" to "buy".

## DCF Valuation

| FCF projection (PLN mn) | 2011e | 2012e | 2013e | 2014e | 2015e | 2016e | TV CF |
|---|---|---|---|---|---|---|---|
| **Consolidated sales** | **3,450** | **3,031** | **2,627** | **3,065** | **3,310** | **3,163** | **3,451** |
| EBITDA | -24 | 75 | 99 | 139 | 160 | 157 | 154 |
| EBITA | -66 | 29 | 48 | 84 | 104 | 96 | 65 |
| Taxes paid on EBITDA | -24 | -5 | -9 | -16 | -20 | -18 | -12 |
| **NOPLAT** | **-54** | **23** | **39** | **68** | **85** | **78** | **53** |
| Adj. NOPLAT | -54 | 23 | 39 | 68 | 85 | 78 | 53 |
| Depreciation of PPE & intangibles | 42 | 46 | 51 | 56 | 56 | 61 | 89 |
| Gross investment in PPE & intangibles | -62 | -51 | -56 | -61 | -59 | -65 | -100 |
| Change in working capital | -361 | 299 | -0 | -55 | -79 | 3 | -2 |
| NWC/Sales | 6.7% | -2.2% | -2.6% | -0.4% | 2.0% | 2.0% | 2% |
| Change in LT provisions other than tax | -0 | 0 | 0 | 0 | 0 | 0 | |
| Net acquisitions & disposals | 0 | 0 | 0 | 0 | 0 | 0 | |
| Free cash flow to firm | -435 | 318 | 34 | 8 | 2 | 76 | 40 |
| **Adj. free cash flow to firm** | **-435** | **318** | **34** | **8** | **2** | **76** | **40** |
| **EV DCF, mid-year assumption** | **682** | **437** | | | | | |
| + MV of non-operating assets eop | 0 | 0 | | | | | |
| - MV of net debt eop | 84 | -232 | | | | | |
| - MV of minorities eop | 66 | 67 | | | | | |
| Adjustments to EV eop | 0.0 | 0.0 | | | | | |
| **Fair value of equity** | **532** | **601** | | | | | |
| Shares outstanding (mn) | 20 | 20 | | | | | |
| **Fair value per share (in PLN)** | **26.61** | **30.05** | | | | | |

| Value drivers | 2011e | 2012e | 2013e | 2014e | 2015e | 2016e | TV CF |
|---|---|---|---|---|---|---|---|
| Consolidated sales yoy | 34.2% | -12.1% | -13.3% | 16.7% | 8.0% | -4.4% | 2.5% |
| EBITDA margin | -0.7% | 2.5% | 3.8% | 4.5% | 4.8% | 5.0% | 4.5% |
| Rate of taxes paid | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% |
| Working capital/sales | 6.7% | -2.2% | -2.6% | -0.4% | 2.0% | 2.0% | 2.0% |
| Capex/depreciation | 148.1% | 109.6% | 109.7% | 109.7% | 106.8% | 107.1% | 112.8% |
| Free cash flow margin | -12.6% | 10.5% | 1.3% | 0.2% | 0.1% | 2.4% | 1.2% |

| WACC | 2011e | 2012e | 2013e | 2014e | 2015e | 2016e | TV CF |
|---|---|---|---|---|---|---|---|
| Target capital structure (at MV) | 100.0% | 100.0% | 100.0% | 100.0% | 95.0% | 95.0% | 95.0% |
| Debt/equity ratio (at MV) | 0.0% | 0.0% | 0.0% | 0.0% | 5.3% | 5.3% | 5.3% |
| Risk free rate (local) | 4.9% | 4.8% | 4.6% | 5.1% | 5.5% | 6.1% | 4.8% |
| Equity market premium | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% |
| Levered beta | 1.3 | 1.3 | 1.3 | 1.3 | 1.3 | 1.3 | 1.3 |
| Cost of equity | 11.2% | 11.1% | 11.2% | 11.7% | 11.8% | 12.4% | 11.1% |
| Cost of debt | 6.4% | 6.3% | 6.1% | 6.6% | 7.0% | 7.6% | 6.3% |
| Tax rate | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% |
| **WACC** | **11.2%** | **11.1%** | **11.2%** | **11.7%** | **11.4%** | **12.0%** | **10.8%** |

## Sensitivity analysis

| Growth sensitivity (PLN) | | | Terminal growth rate | | | | |
|---|---|---|---|---|---|---|---|
| **WACC** | **1.0%** | **1.5%** | **2.0%** | **2.5%** | **3.0%** | **3.5%** | **4.0%** |
| 9.3% | 31.7 | 32.6 | 33.6 | 34.8 | 36.1 | 37.7 | 39.6 |
| 9.8% | 30.3 | 31.1 | 32.0 | 33.0 | 34.1 | 35.5 | 37.0 |
| 10.3% | 29.2 | 29.8 | 30.6 | 31.4 | 32.4 | 33.5 | 34.8 |
| 10.8% | 28.1 | 28.7 | 29.3 | **30.1** | 30.9 | 31.8 | 32.9 |
| 11.3% | 27.1 | 27.6 | 28.2 | 28.8 | 29.5 | 30.3 | 31.3 |
| 11.8% | 26.2 | 26.7 | 27.2 | 27.7 | 28.4 | 29.0 | 29.8 |
| 12.3% | 25.4 | 25.8 | 26.2 | 26.7 | 27.3 | 27.9 | 28.6 |

| Margin sensitivity (PLN) | | | FCF margin TV | | | | |
|---|---|---|---|---|---|---|---|
| **WACC** | **-0.3%** | **0.2%** | **0.7%** | **1.2%** | **1.7%** | **2.2%** | **2.7%** |
| 9.3% | 13.9 | 20.8 | 27.8 | 34.8 | 41.8 | 48.7 | 55.7 |
| 9.8% | 14.1 | 20.4 | 26.7 | 33.0 | 39.3 | 45.6 | 51.9 |
| 10.3% | 14.3 | 20.0 | 25.7 | 31.4 | 37.1 | 42.8 | 48.6 |
| 10.8% | 14.5 | 19.7 | 24.9 | **30.1** | 35.3 | 40.5 | 45.6 |
| 11.3% | 14.6 | 19.3 | 24.1 | 28.8 | 33.6 | 38.3 | 43.1 |
| 11.8% | 14.7 | 19.0 | 23.4 | 27.7 | 32.1 | 36.4 | 40.8 |
| 12.3% | 14.7 | 18.7 | 22.7 | 26.7 | 30.7 | 34.8 | 38.8 |

*Source: Raiffeisen Centrobank estimates*

| *Income statement (PLN mn)* | *12/2008* | *12/2009* | *12/2010* | *12/2011e* | *12/2012e* | *12/2013e* |
|---|---|---|---|---|---|---|
| **Consolidated sales** | **2,211** | **2,712** | **2,570** | **3,450** | **3,031** | **2,627** |
| Cost of sales | -1,994 | -2,400 | -2,414 | -3,443 | -2,931 | -2,505 |
| **Gross profit** | **217** | **312** | **157** | **7** | **101** | **122** |
| Other operating income | 38 | 39 | 31 | 26 | 0 | 0 |
| Selling expenses | -1 | -2 | -1 | -2 | -1 | -1 |
| Administrative expenses | -75 | -90 | -87 | -69 | -71 | -72 |
| Other operating expenses | -57 | -78 | -16 | -28 | 0 | 0 |
| **EBITDA** | **143** | **209** | **120** | **-24** | **75** | **99** |
| Adjusted EBITDA | 143 | 209 | 120 | -24 | 75 | 99 |
| Depreciation of PPE and intangibles | -21 | -28 | -35 | -42 | -46 | -51 |
| **EBITA** | **122** | **181** | **84** | **-66** | **29** | **48** |
| Amortisation, impairment of goodwill | 0 | 0 | 0 | 0 | 0 | 0 |
| **EBIT** | **122** | **181** | **84** | **-66** | **29** | **48** |
| Adjusted EBIT | 122 | 181 | 84 | -66 | 29 | 48 |
| Investment income | -3 | -6 | -4 | 0 | 0 | 0 |
| Net interest income | 10 | 13 | 8 | -2 | -3 | 5 |
| Other financial result | -9 | -18 | 0 | 0 | 0 | 0 |
| **Financial result** | **-2** | **-12** | **4** | **-2** | **-3** | **5** |
| **Earnings before taxes** | **119** | **169** | **88** | **-69** | **26** | **54** |
| Taxes on income | -27 | -43 | -22 | 11 | -5 | -10 |
| Extraordinary result | 0 | 0 | 0 | 0 | 0 | 0 |
| **Net profit before minorities** | **92** | **126** | **66** | **-58** | **21** | **43** |
| Minority interests | -11 | -9 | -3 | -1 | -1 | -2 |
| **Net profit after minorities** | **81** | **117** | **62** | **-59** | **20** | **41** |
| Adjusted Net profit | 81 | 117 | 62 | -59 | 20 | 41 |

| *Changes yoy* | *12/2008* | *12/2009* | *12/2010* | *12/2011e* | *12/2012e* | *12/2013e* |
|---|---|---|---|---|---|---|
| Consolidated sales yoy | 14.7% | 22.7% | -5.2% | 34.2% | -12.1% | -13.3% |
| EBITDA yoy | 85.5% | 46.5% | -42.7% | -120.2% | n.a. | 32.2% |
| EBITA yoy | 107.0% | 48.7% | -53.5% | -178.6% | n.a. | 68.5% |
| EBIT yoy | 107.0% | 48.7% | -53.5% | -178.6% | n.a. | 68.5% |
| EBT yoy | 91.6% | 41.9% | -48.1% | -177.9% | n.a. | 109.9% |
| Net profit after minorities yoy | 53.2% | 44.6% | -46.7% | -194.7% | n.a. | 109.9% |

| *Margins* | *12/2008* | *12/2009* | *12/2010* | *12/2011e* | *12/2012e* | *12/2013e* |
|---|---|---|---|---|---|---|
| Gross margin | 9.8% | 11.5% | 6.1% | 0.2% | 3.3% | 4.6% |
| EBITDA margin | 6.5% | 7.7% | 4.7% | -0.7% | 2.5% | 3.8% |
| EBITA margin | 5.5% | 6.7% | 3.3% | -1.9% | 0.9% | 1.8% |
| EBIT margin | 5.5% | 6.7% | 3.3% | -1.9% | 0.9% | 1.8% |
| EBT margin | 5.4% | 6.2% | 3.4% | -2.0% | 0.8% | 2.0% |
| Net margin | 3.7% | 4.3% | 2.4% | -1.7% | 0.6% | 1.6% |

| *Profitability* | *12/2008* | *12/2009* | *12/2010* | *12/2011e* | *12/2012e* | *12/2013e* |
|---|---|---|---|---|---|---|
| Return on assets | 8.4% | 9.3% | 4.9% | -3.3% | 1.7% | 3.0% |
| Return on equity | 26.1% | 28.6% | 12.5% | -12.3% | 4.3% | 8.5% |
| Return on capital employed | 22.5% | 23.3% | 11.4% | -8.1% | 4.2% | 7.5% |

| *Cash flow statement (PLN mn)* | *12/2008* | *12/2009* | *12/2010* | *12/2011e* | *12/2012e* | *12/2013e* |
|---|---|---|---|---|---|---|
| **Earnings before taxes** | **119** | **169** | **88** | **-69** | **26** | **54** |
| Taxes paid | -32 | -71 | -41 | -24 | -5 | -10 |
| Amortisation and depreciation | 23 | 28 | 35 | 42 | 46 | 51 |
| Other non-cash items | 8 | 7 | 6 | -0 | 0 | 0 |
| **Cash flow from result** | **118** | **133** | **88** | **-50** | **67** | **94** |
| Change in working capital | -51 | 81 | 40 | -361 | 299 | -0 |
| **Operating cash flow** | **67** | **214** | **127** | **-411** | **366** | **94** |
| Capex PPE and intangible assets | -22 | -67 | -29 | -62 | -51 | -56 |
| Acquisitions | 0 | 0 | 0 | 0 | 0 | 0 |
| Disposal of fixed assets (total) | 0 | 0 | 0 | 40 | 0 | 0 |
| Other items (investments) | -3 | -3 | -7 | 1 | 0 | 0 |
| **Investing cash flow** | **-26** | **-69** | **-36** | **-22** | **-51** | **-56** |
| Dividend payments | 0 | 0 | -28 | -11 | 0 | -5 |
| Other changes in equity | 0 | 0 | 0 | 0 | 0 | 0 |
| Change in financial liabilities | -10 | -15 | -19 | 134 | -130 | -50 |
| Other items | -9 | -10 | -13 | -4 | -0 | 0 |
| **Financing cash flow** | **-20** | **-24** | **-60** | **119** | **-130** | **-55** |

*Source: Mostostal Warszawa, Raiffeisen Centrobank estimates*

| Balance sheet (PLN mn) | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| **Current assets** | **1,029** | **1,112** | **1,221** | **1,450** | **1,206** | **1,064** |
| Liquid funds | 310 | 430 | 461 | 146 | 332 | 315 |
| Receivables | 516 | 459 | 463 | 552 | 485 | 420 |
| Inventories | 41 | 36 | 66 | 96 | 86 | 66 |
| Other assets | 162 | 187 | 231 | 656 | 303 | 263 |
| **Fixed assets** | **198** | **331** | **359** | **339** | **344** | **349** |
| Property, plant & equipment | 188 | 285 | 301 | 321 | 326 | 331 |
| Intangible assets | 2 | 2 | 6 | 6 | 6 | 6 |
| Goodwill | 0 | 0 | 0 | 0 | 0 | 0 |
| Financial assets | 7 | 44 | 52 | 12 | 12 | 12 |
| **Deferred tax assets** | **49** | **62** | **48** | **82** | **82** | **82** |
| **Total assets** | **1,276** | **1,505** | **1,627** | **1,871** | **1,631** | **1,494** |
| **Current liabilities** | **827** | **825** | **925** | **1,222** | **1,042** | **866** |
| Short-term borrowings | 30 | 30 | 36 | 150 | 100 | 50 |
| Notes & trade payables, payments received | 353 | 326 | 427 | 552 | 485 | 420 |
| Other current liabilities | 444 | 468 | 463 | 520 | 457 | 396 |
| **Long-term liabilities** | **41** | **118** | **109** | **129** | **49** | **49** |
| Long-term borrowings | 29 | 60 | 61 | 80 | 0 | 0 |
| Long-term provisions | 8 | 9 | 9 | 9 | 9 | 9 |
| Other long-term liabilities | 4 | 49 | 39 | 40 | 40 | 40 |
| **Hybrid & other mezzanine capital** | **0** | **0** | **0** | **0** | **0** | **0** |
| **Shareholders' equity** | **338** | **482** | **518** | **447** | **467** | **503** |
| **Minority interests** | **65** | **74** | **70** | **66** | **67** | **69** |
| **Deferred tax liabilities** | **5** | **6** | **6** | **6** | **6** | **6** |
| **Total liabilities** | **1,276** | **1,505** | **1,627** | **1,871** | **1,631** | **1,494** |

| Balance sheet (PLN mn) | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| Net working capital | -77 | -113 | -130 | 231 | -68 | -68 |
| Net interest-bearing debt | -251 | -340 | -365 | 84 | -232 | -265 |
| Capital employed | 462 | 647 | 684 | 744 | 634 | 623 |
| Market capitalisation | 984 | 1,218 | 1,223 | 320 | 379 | 379 |
| Enterprise value | 798 | 946 | 928 | 470 | 215 | 184 |

| Financing (x) | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| Interest cover | 34.5 | 55.6 | 10.4 | n.a. | 7.9 | 23.8 |
| Internal financing ratio | 3.0 | 3.2 | 4.4 | -6.6 | 7.2 | 1.7 |
| Net gearing | -62.2% | -61.1% | -62.1% | 16.3% | -43.4% | -46.3% |
| Quick ratio | 1.2 | 1.3 | 1.2 | 1.1 | 1.1 | 1.2 |
| Fixed assets cover | 2.2 | 2.0 | 1.9 | 1.9 | 1.7 | 1.8 |
| Capex / depreciation | 1.1 | 2.4 | 0.8 | 1.5 | 1.1 | 1.1 |
| Equity ratio | 31.6% | 37.0% | 36.1% | 27.5% | 32.8% | 38.3% |

| Per share data (PLN) | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| Weighted avg. no. of shares (mn) | 20.0 | 20.0 | 20.0 | 20.0 | 20.0 | 20.0 |
| EPS reported | 4.06 | 5.87 | 3.12 | -2.96 | 0.98 | 2.06 |
| Earnings per share (adj.) | 4.06 | 5.87 | 3.12 | -2.96 | 0.98 | 2.06 |
| Operating cash flow per share | 3.35 | 10.69 | 6.37 | -20.55 | 18.31 | 4.68 |
| Book value per share | 16.88 | 24.12 | 25.88 | 22.37 | 23.36 | 25.17 |
| DPS | 0.00 | 1.40 | 0.55 | 0.00 | 0.25 | 0.52 |
| Payout ratio | 0.0% | 23.9% | 17.6% | 0.0% | 25.0% | 25.0% |

| Valuation (x) | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| PE reported | 12.1 | 10.4 | 19.6 | -5.4 | 19.3 | 9.2 |
| Adjusted PE ratio | 12.1 | 10.4 | 19.6 | -5.4 | 19.3 | 9.2 |
| Price cash flow | 14.7 | 5.7 | 9.6 | -0.8 | 1.0 | 4.1 |
| Price book value | 2.9 | 2.5 | 2.4 | 0.7 | 0.8 | 0.8 |
| Dividend yield | 0.0% | 2.3% | 0.9% | 0.0% | 1.3% | 2.7% |
| Free cash flow yield | 4.3% | 11.4% | 7.6% | -122.6% | 70.6% | 8.5% |
| EV/sales | 0.4 | 0.3 | 0.4 | 0.1 | 0.1 | 0.1 |
| EV/EBITDA | 5.6 | 4.5 | 7.8 | -19.5 | 2.9 | 1.9 |
| EV/EBIT | 6.5 | 5.2 | 11.0 | -7.1 | 7.5 | 3.8 |
| EV/operating cash flow | 11.9 | 4.4 | 7.3 | -1.1 | 0.6 | 2.0 |
| Adjusted EV/CE | 2.4 | 2.1 | 2.0 | 0.8 | 0.9 | 0.8 |
| Adjusted EV/CE vs. ROCE/WACC | | | | -1.1 | 2.3 | 1.2 |

*Source: Mostostal Warszawa, Raiffeisen Centrobank estimates*

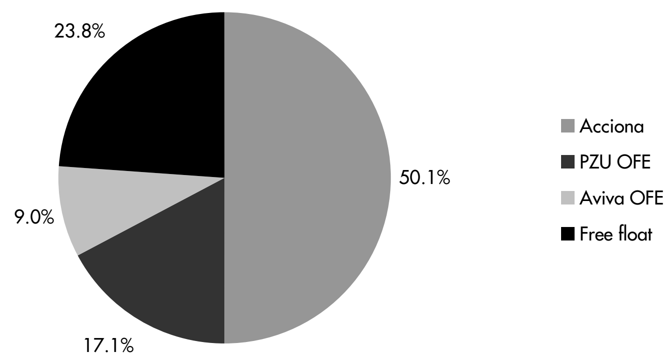
# Mostostal Warszawa

## Fact Sheet

### *Company description*

Mostostal Warszawa is the fifth largest construction company in terms of sales operating on the Polish market. Mostostal Warszawa also ranks number 4 in terms of market capitalization among the listed construction companies on the Warsaw Stock Exchange. The strategic investor and partner to the company is Acciona from Spain owning 50.09% of the shares. The Group is active on all basic sectors of the construction market and acts as a general contractor of investment projects and provides turnkey execution of construction assignments. The Group splits its activities into five segments: general construction (residential and public buildings), industrial construction (halls, warehouses, and steel structures), civil engineering (tunnels, bridges, grade separated junctions), road construction (national and local roads) and environmental engineering (water and sewage treatment plants, water purification plants).

### *Shareholder structure*




### *Strengths/Opportunities*

- Strong order backlog supporting sales growth
- Low leverage
- Diversification of revenue sources
- Exposure to the next boom sectors, particularly power engineering
- EU fund flows on construction projects
- Attractiveness of the Polish economy

### *Weaknesses/Threats*

- Increased competition squeezing margins
- Likely increase in raw material prices
- Delay in power engineering projects
- Never-ending story with the Polish government's project management
- Potential conflict of interest with the strategic investor
- Low liquidity of the shares

| *Income statement (PLN mn)* | *12/2010* | *12/2011e* | *12/2012e* | *12/2013e* |
|---|---|---|---|---|
| Consolidated sales | 2,570 | 3,450 | 3,031 | 2,627 |
| EBITDA | 120 | -24 | 75 | 99 |
| EBIT | 84 | -66 | 29 | 48 |
| EBT | 88 | -69 | 26 | 54 |
| Net profit bef. min. | 66 | -58 | 21 | 43 |
| Net profit after min. | 62 | -59 | 20 | 41 |
| ***Balance sheet*** | | | | |
| Total assets | 1,627 | 1,871 | 1,631 | 1,494 |
| Shareholders' equity | 518 | 447 | 467 | 503 |
| Goodwill | 0 | 0 | 0 | 0 |
| NIBD | -365 | 84 | -232 | -265 |
| ***Cash flow statement*** | | | | |
| Operating cash flow | 127 | -411 | 366 | 94 |
| Investing cash flow | -36 | -22 | -51 | -56 |
| Change NIBD | 25 | -448 | 315 | 33 |

*Source: Mostostal Warszawa, Raiffeisen Centrobank estimates*

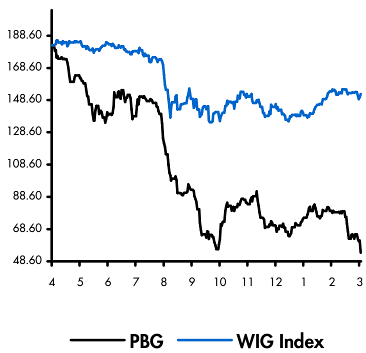
| *Per share data (PLN)* | *12/2010* | *12/2011e* | *12/2012e* | *12/2013e* |
|---|---|---|---|---|
| EPS pre-goodwill | 3.12 | -2.96 | 0.98 | 2.06 |
| Adj. EPS diluted | 3.12 | -2.96 | 0.98 | 2.06 |
| Operating cash flow | 6.37 | -20.55 | 18.31 | 4.68 |
| Book value | 25.88 | 22.37 | 23.36 | 25.17 |
| Dividend | 0.55 | 0.00 | 0.25 | 0.52 |
| Payout ratio | 17.6% | 0.0% | 25.0% | 25.0% |
| ***Valuation (x)*** | | | | |
| PE pre-goodwill | 19.6 | -5.4 | 19.3 | 9.2 |
| Adj. PE diluted | 19.6 | -5.4 | 19.3 | 9.2 |
| Price cash flow | 9.6 | -0.8 | 1.0 | 4.1 |
| Price book value | 2.4 | 0.7 | 0.8 | 0.8 |
| Dividend yield | 0.9% | 0.0% | 1.3% | 2.7% |
| FCF yield | 7.6% | -122.6% | 70.6% | 8.5% |
| EV/EBITDA | 7.8 | -19.5 | 2.9 | 1.9 |
| EV/EBIT | 11.0 | -7.1 | 7.5 | 3.8 |
| EV/operating CF | 7.3 | -1.1 | 0.6 | 2.0 |

# Company Update
## PBG

March 9, 2012 | Construction & Materials/Poland

## Hold

| | |
|---|---|
| Price 08.03.12* | 54.00 |
| Price target | 64.00 |
| Volatility risk | high |
| Year high/low | 182.60/54.00 |
| Currency | PLN |
| PLN/EUR | 4.10 |
| GDR rate | n.a. |
| Shares outstanding eoy in mn | 14.30 |
| Market capitalisation (total shares) in EUR mn | 188.4 |
| Free float | 41.0% |
| Free float in EUR mn | 77.3 |
| Avg. daily turnover (12 m) in EUR mn | 1.62 |
| Index | WIG |
| ISIN code | PLPBG0000029 |
| Bloomberg | PBG PW |
| Reuters | PBGG.WA |
| www.pbg-sa.pl | |




*Source: Raiffeisen Centrobank*

## Built on dreams

We reinitiate our coverage of PBG with a "hold" recommendation. We are fans of the visionary nature of this construction company and its efficient positioning towards the most booming and (not always) profitable segments of the Polish construction sector. The group started off with high-margin oil and gas as well as hydro construction, added road construction (not so successful in our view) and is now positioning itself to benefit from the upcoming and massive power fleet modernization in Poland. Whereas we see the orientation towards the highway construction segment as unsuccessful on the back of substantial margin pressure and a very demanding working capital cycle, the strategic shift towards power engineering seems to be the right one. We expect the power groups to spend on modernization of generation capacities and their sound balance sheets should be capable of accommodating such an intensive capex effort. We also appreciate PBG's aggressive tender participation strategy. Yet, we have to point out the risks of high offer preparation costs yet to impact the P&L as well as the project management risks and resulting penalty fees on the back of a lack of competences. Despite incorporating Rafako, probably the most experienced power engineering group in Poland with its own boiler technologies, no company in Poland has the credentials of running a PLN 10 bn project, as that recently awarded to Rafako and its consortium. Furthermore, the demanding capital cycle and an aggressive acquisition strategy have substantially lifted PBG's leverage approaching a Net debt/EBITDA ratio of renegotiated covenants breaching 4x. We do not expect too much of an improvement to come this year, as the company will still derive a substantial portion of its revenues from highway construction. Furthermore, we perceive the group's balance sheet highly vulnerable to a potential goodwill impairment risk. The goodwill balance has exceeded PLN 800 mn following Rafako's acquisition and amounts to as much as 50% of total equity.

**4Q 11 review**: PBG reported a massive, 62% yoy increase in its top line as a result of a) Rafako's full consolidation starting at the beginning of November 2011 and contributing some PLN 231 mn and b) the relatively warm winter particularly benefiting road construction. Furthermore, margins have followed the general trend of contraction and have come in below the consensus estimates, yet one-off impacts (Rafako's goodwill impairment, high effective tax rate) make the picture a bit more confusing. We do not see the seasonal receivables balance decrease (after adjusting for Rafako's figures) and thus the short-debt financing remains on very high and unsustainable levels.

**Valuation and recommendation**: Our DCF model yields a 12-month target price of PLN 64 after applying a dilution discount, which translates into a "hold" recommendation.

### Key figures and ratios

| PLN | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|
| Sales (mn) | 2,740 | 3,734 | 4,575 | 3,881 | 4,231 |
| EBITDA (mn) | 308 | 312 | 328 | 330 | 384 |
| EBIT (mn) | 262 | 251 | 266 | 265 | 319 |
| Net profit a.m. (mn) | 190 | 171 | 97 | 116 | 164 |
| Earnings per share (adj.) | 13.32 | 11.98 | 6.82 | 8.09 | 11.50 |
| EPS adjusted growth | -11.2% | -10.1% | -43.1% | 18.7% | 42.2% |
| Adjusted PE ratio | 16.0 | 5.9 | 7.9 | 6.7 | 4.7 |
| DPS | 1.40 | 1.40 | 0.00 | 0.00 | 0.00 |
| Dividend yield | 0.7% | 2.0% | 0.0% | 0.0% | 0.0% |
| EV/EBITDA | 12.8 | 9.7 | 6.8 | 5.4 | 4.4 |
| Price book value | 1.9 | 0.6 | 0.4 | 0.4 | 0.4 |

*Source: PBG, Raiffeisen Centrobank estimates*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Supervisory authority: Financial Market Authority


* The indicated price is the last price as available at 6.30 AM on 09.03.12

Raiffeisen RESEARCH

Raiffeisen CENTROBANK

### Share price triggers

| Trigger | Momentum | Explanation |
|---|---|---|
| **Power engineering** | positive | ▪ PBG has effectively reoriented its business strategy towards power engineering following the acquisition of Rafako and is undertaking an aggressive approach towards the open power engineering projects<br>▪ We believe the group has quite a chance to be the major beneficiary of the expected boom |
| **2014-2020 EU budget** | neutral | ▪ Budimex positions itself towards benefiting again from EU money flows to Poland<br>▪ This strategy is quite risky given the ongoing eurozone problems<br>▪ Yet, allocation of a similar size to the 2008-2013 budget should result in another re-rating of the construction sector |
| **Working capital management** | negative | ▪ Following the engagement in large road construction projects, the working capital management of the company has substantially deteriorated, impacting the short-term financing<br>▪ We do not see much room for improvement in working capital management this year as a consequence of a still large infrastructure order backlog, hence, we see the refinancing risk as elevated |
| **Refinancing, leverage** | negative | ▪ PBG is the highest leveraged construction company with the majority of its debt to be rolled over this year<br>▪ To us the refinancing risk looks material |

*Source: Raiffeisen Centrobank*

## Company description, strategic positioning

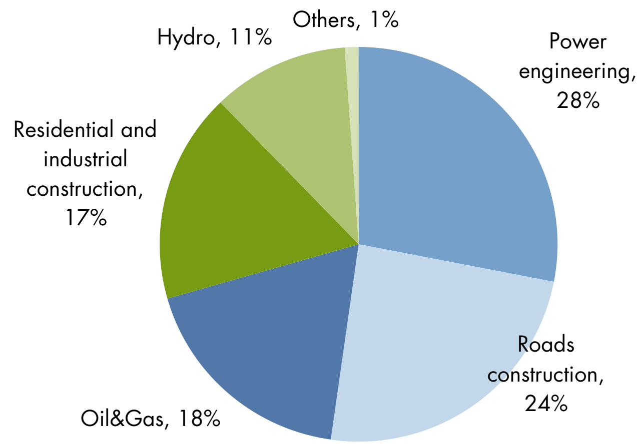
***Strong in oil and gas related construction as well as hydro engineering; repositioning towards power engineering***

PBG is one of the largest Polish construction companies specialized in the following segments:

- Natural gas, crude oil and fuels related construction: installations, storage capacities, pipelines, fuel depots, LNG installations
- Hydro construction: pipelines, sewage systems, water treatment plants, hydro-engineering facilities (dams, storage reservoirs, flood-control reservoirs), renovations
- Industrial and residential construction: waste disposal plants, commercial and residential construction, industrial infrastructure and buildings
- Road construction
- Power engineering: assembly, modernization and after Rafako's acquisition also boiler manufacturing, environmental installations, complete power generation units.

The chart below presents the 2011 sales mix including Rafako's sales (actually only consolidated from November 1, 2011, yet for presentation purposes we assume full-year consolidation).

### Sales mix (on 2011 figures)

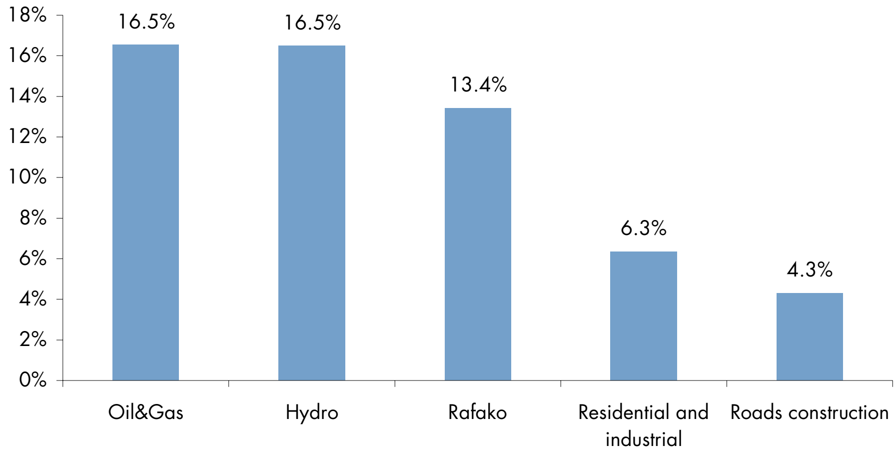



*Source: PBG, Rafako, Raiffeisen Centrobank*

PBG also aims to reposition itself away from the low-margin road construction that is expected to substantially decline towards higher-margin (and yet higher-risk) power engineering. Last year the group consolidated the power engineering competences by increasing its stake in Energomontaz Poludnie (and later on sold to Rafako), a company specializing in power engineering and industrial installations and by acquiring a 66% stake in Rafako – one of the largest European boiler producers, offering also complete power generation units and environmental installations (2011 top line amounted to PLN 1.1 bn, EBIT to PLN 61 mn and net profit to PLN 56 mn). The total transaction value (acquisition of 50% + 1 share by Mr. Solorz-

Zak, 12.42% of the shares on the stock exchange and the remaining via a tender offer) stood at approx. PLN 570 mn.

***Gross margins by segment (2011)***



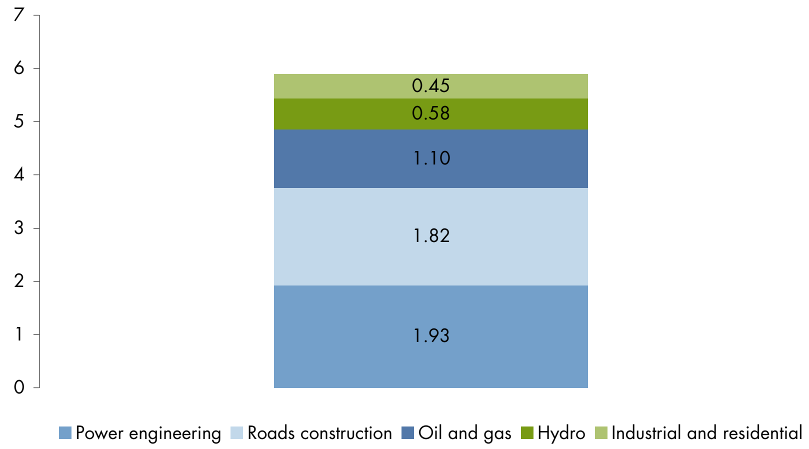

*Source: PBG, Rafako, Raiffeisen Centrobank*

Furthermore, PBG has been very aggressively (in terms of frequency) participating in all the power engineering tenders called (please compare it to Mostostal Warszawa's very selective approach), predominantly in consortium with Alstom. Given a limited amount of competences in Poland and a number of tenders announced, we see PBG's chances (together with Rafako) to manage at least two projects as high (Rafako is already part of the consortium for the Opole power plant valued at PLN 9.4 bn net with a share of approx. 35%). Furthermore, Rafako should also be one of the major beneficiaries of the boom in terms of subcontractor works and technology supplies (Rafako is one of the four boiler manufacturers operating in Europe). Two aspects of the aforementioned considerations have to be pointed out, however:

1. There is not much experience in Poland to run such large projects like the Opole project, hence we see risks in terms of mismanagement, delays etc. eventually resulting in high penalties (the recent dispute between PGE and Alstom on the back of massive power block construction delays in Belchatow is rumoured to be valued at PLN 300-350 mn).
2. Offer preparation costs run in the millions, a majority of which have not been charged against the P&L yet (prepaid expenses on the balance sheet) and with a value reaching approx. PLN 50 mn. We expect this amount to impact the SG&A line this year and next.

We also appreciate the group's strategy to step away from the highway and expressway construction sector, where the company has been operating on low, single-digit margins as well as absolutely mismanaged its working capital cycle with a massive receivables increase combined with elevated leverage at unsustainable levels. Still, however, the road order backlog amounts to as much as 31%, the majority of which (around PLN 1.5 bn) is scheduled to be worked through this year.

*PBG's end-2011- order backlog (total PLN 5.9 bn)*




*Source: PBG, Raiffeisen Centrobank*

## Balance sheet, working capital, leverage

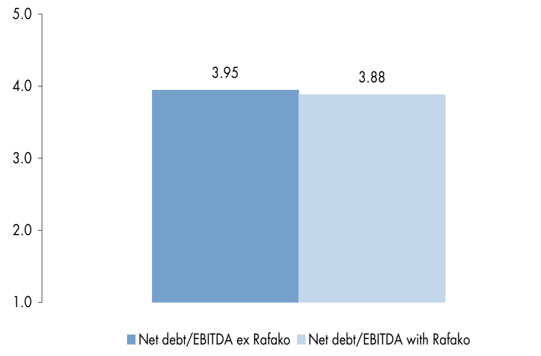
***High leverage and refinancing risk triggered by the poor working capital management on road contracts***

As already indicated in the introductory part PBG has the worst working capital management from all the companies discussed in this report. This is predominantly a consequence of a large commitment in the working capital intensive road infrastructure projects and the payment cycle by the road authorities (GDDKiA). Furthermore, a seasonal receivables repayment to PBG in 4Q did not happen on the back of delayed invoice submission. Given a high road contracts portfolio for 2012, we do not expect the situation to materially improve, however. In our opinion, though, refocusing the sales mix from roads to power engineering should substantially improve the development of the working capital position, but we expect this to materialise only in 2013. Please note that a) Rafako has a substantially lower receivables balance vs. its sales and b) large power projects are associated with quite substantial prepayments (amounting to 8% in case of the Opole power project, 2% thereof should be deposited in the consortium's account in 2012 already).

As a result of the working capital mismanagement and overinvestment (please note that the goodwill amounts to as much as half of equity, making the company extremely sensitive to any goodwill impairments), PBG's debt financing has increased to unsustainable levels, with a very high refinancing risk (PLN 1.4 bn of short-term financing). We are of the opinion that a high engagement in road contracts in 2012 would not substantially improve the leverage of PBG. On the other hand, however, a cash injection from PGE (of approx. PLN 65 mn) for construction of the Opole power plant and completion of the stadium contracts (receivables amount to PLN 75 mn) should ease some refinancing pressure.

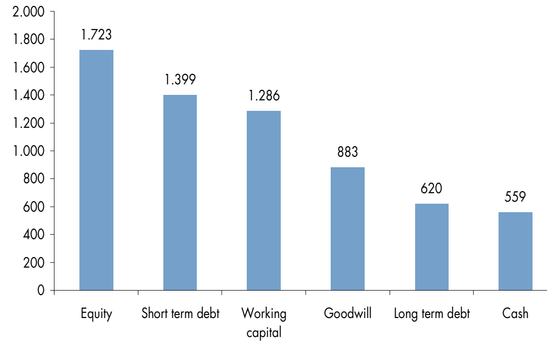
As already indicated, PBG's balance sheet is dominated by the recognized goodwill following a number of acquisitions the group has conducted (13% of total assets, 50% of equity). The goodwill is dominated by a couple of transactions; predominantly Rafako, Hydrobudowa 9 and Energomontaz Poludnie (please refer to the chart below for the goodwill mix). We are not big fans of too big a goodwill and point out the sensitivity of the company to any impairment, which could substantially affect the P&L as well as the leverage perception.

### Net debt/EBITDA x (2011)



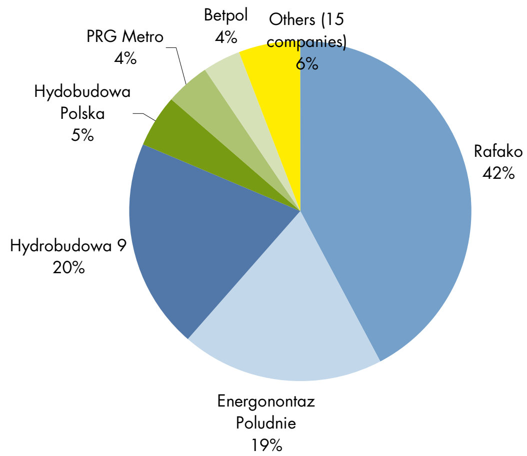

Source: PBG, Rafako, Raiffeisen Centrobank

### Debt and working capital (in PLN mn, 2001)




Source: PBG, Raiffeisen Centrobank

### Goodwill composition



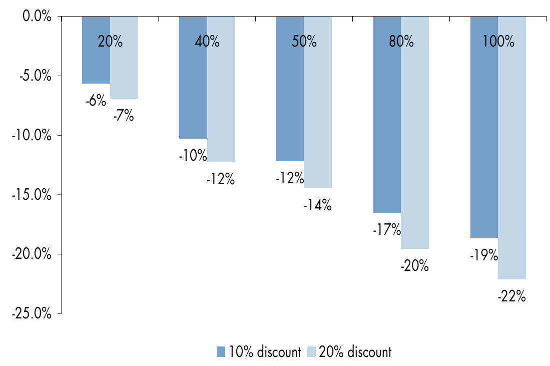

Source: PBG, Raiffeisen Centrobank

## Capital increase

PBG announced a rescue (in our view) capital increase to be conducted in 2Q 11 (subject to the AGM approval at the beginning of April). The maximum amount to shares to be issued stands to 100% of the current outstanding. Alternatively, PBG will issue convertible bonds of a maximum value of PLN 1.2 bn (vs. the current outstanding debt exceeds PLN 2 bn). Furthermore, PBG aims to engage a strategic investor into the deal. Yet, we somehow see it as less likely that a strategic investor would like to engage in the deal where no controlling stake is granted (please note that a) Mr Wisniewski holds 40.57% of the total votes possessing only 27.15% of the shares outstanding and b) even a 100% capital increase would give no controlling stake to the strategic investor (41%). We anyway believe that the dilution effect is likely to be quite substantial.

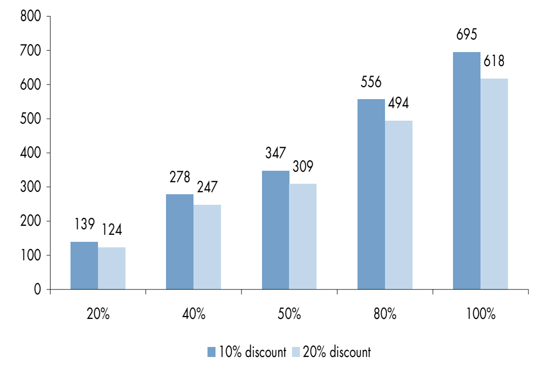
The chart below presents the sensitivities of the valuation to the discount (10% and 20%) to the current target price and a 20%, 40%, 50%, 80% and 100% capital increase. We also present the amount of cash to be collected given different scenarios (gross of flotation costs).

### Valuation sensitivities




Source: Raiffeisen Centrobank estimates

### Funds to be raised (in different increase scenarios)




Source: Raiffeisen Centrobank estimates

## 4Q 11 review

***Margins adjusted for one-offs look alright, yet the receivables balance remained unusually high given the seasonality***

PBG reported a PLN 1.35 bn top line, i.e. an increase of 62% yoy, overshooting the estimates by 34%. Please note that PBG has consolidated Rafako since the beginning of November, which added PLN 218 mn of revenues. Still, the adjusted revenue dynamics looks impressive (36% yoy). Most of the (ex. Rafako) revenue dynamics has come from the roads segment (up 180% yoy), as a result of warmer weather in 4Q 11. The Oil and gas segment reported a 30% drop in revenues (to PLN 240 mn) and the hydro segment a decline by 11% yoy (to PLN 177 mn). The Industrial and residential segment posted growth dynamics of 20% yoy to PLN 220 mn.

Gross margin of 11.8% looks slightly worse than last year (13.3%), which is in line with the ongoing trend. A substantial improvement was observed vs. the previous quarter (gross margin of 9.8%), predominantly on the back of improved profitability in the roads segment. Please note that the addition of Rafako's high-margin performance also had a positive effect (power engineering segment margins amount to 16.7%).

The EBIT line of PLN 70.1 mn has come in below the street estimates (by 3.8%) and on substantially lower margins (5.2% vs. 7.2%), yet the company has booked goodwill impairment on Rafako of PLN 21.9 mn. Adjusted EBIT exceeds expectations and profitability is almost in line.

Net profit came in at PLN 30.9 mn, i.e. 60% down yoy and missing the consensus by 8%. Yet, the bottom line has been impacted by an unusually high effective tax rate of 33% - a reversal of an unusually low effective tax rate reported in 1-3Q 11 of 14% (we do not fully understand the tax rate undervaluation conducted by PBG in 1-3Q 11). After adjustment for the normalized, 19% tax rate and the goodwill impairment, net profit would substantially overshoot the projections and net profitability would exceed 5% (vs. 3.3% expected).

Leverage remains high and slightly below 4x Net debt/EBITDA if we account for full-year Rafako and PBG figures. Receivables have remained on elevated levels (higher than in 3Q 11 and after subtracting Rafako's balance), which is contrary to the industry trend of seasonally decreasing receivables in 4Q.

We find the figures rather neutral after adjusting for the one-offs. We like the revenues increase, however, do not find the working capital and leverage appealing. We would, however, expect the company to improve its standing towards the end of this year.

**PBG's 4Q 11 figures**

| In PLN mn | 4Q 11 | 4Q 10 | +/-% | 3Q 11 | +/-% | Consensus | +/-% |
|---|---|---|---|---|---|---|---|
| Sales | 1,353 | 835.3 | 62.0% | 923.6 | 46.5% | 1,011.4 | 33.8% |
| Gross profit | 160.3 | 110.7 | 44.7% | 90.4 | 77.3% | n.a. | n.a. |
| EBITDA | 89.1 | 131.9 | -32.4% | 82.3 | 8.3% | 85.9 | 3.7% |
| EBIT | 70.1 | 120.5 | -41.8% | 65.7 | 6.8% | 72.9 | -3.8% |
| Net profit | 30.9 | 71.6 | -56.9% | 78.1 | -60.5% | 33.6 | -8.1% |
| Gross margin | 11.8% | 13.3% | | 9.8% | | n.a. | |
| EBITDA margin | 6.6% | 15.8% | | 8.9% | | 8.5% | |
| EBIT margin | 5.2% | 14.4% | | 7.1% | | 7.2% | |
| Net margin | 2.3% | 8.6% | | 8.5% | | 3.3% | |

*Source: PBG, PAP Consensus, Raiffeisen Centrobank*

## Planning model

***Planning model included high order backlog, repositioning from road construction to power engineering and working capital cycle improvement from 2013 on***

Our planning model is based on the following assumptions:

- Order backlog of PLN 5.9 bn, thereof PLN 4.3 bn is to be worked through in 2012, with road and power engineering contracts accounting for the largest share (35% and 30%, respectively).
- We project the industrial and residential construction segment output to decrease substantially on the back of completion of the stadium contracts (which amounted to approx PLN 350 mn of revenues in 2011). We expect the segment revenues to increase in 2013, however, on the back of contracts for construction of waste incinerators (they are to be built until 2015, and the company has submitted the lowest bid for the Krakow project worth PLN 702 mn).
- Power engineering should be a dominant sector from 2013 on. We include the Opole power project (total value of PLN 9.4 bn net, Rafako's share 35%). We are convinced the company can win at least one more contract in the near future as a consequence of its competences (predominantly in terms of incorporating Rafako into the group's structure) and an aggressive tender participation strategy.
- Road segment output will still amount to some PLN 1.5 bn in 2012 on the back of the current order backlog. We estimate this share to massively decrease to PLN 0.4 bn in the following year and then to insignificant PLN 100 mn the year after. We stick to the company's announcement of not participating in any larger road infrastructure projects (apart from those contracts already awarded) and to limit its activities to some selective local road construction projects (higher margins, less risk). Output in 2013 will still be the result of current order backlog.
- We assume that the company will charge its hitherto capitalized power tender preparation costs against the P&L in the years 2012 and 2013, quite substantially impacting its SG&A line.
- We project the working capital cycle to improve following the completion of the road contracts and skewing its sales mix towards power engineering. Consequently, the leverage should decrease.
- We incorporate a disposal of the investment properties amounting to PLN 100 mn in 2012 (Skalar Office in Poznan, predominantly). It should have a neutral impact on the P&L on the back of the properties revaluation policy pursued by the group (mark-to-market on the balance sheet day), yet will impact the cash flows from investments.
- Please note that there has been a change in accounting policy as the company aims to book its interest income above EBIT. We keep the old approach in our modelling in order to make the income statement more comparable to that of other construction companies.

*PBG's planning model*

| In PLN mn | 2011 | 2012e | 2013e | 2014e |
|---|---|---|---|---|
| Oil and gas segment revenues | 851 | 766 | 766 | 804 |
| Hydro segment revenues | 510 | 485 | 485 | 509 |
| Residential and industrial construction revenues | 790 | 395 | 435 | 435 |
| Roads revenues | 1,113 | 1,500 | 400 | 100 |
| Power engineering revenues | 413 | 1,401 | 1,766 | 2,353 |
| Other revenues | 56 | 28 | 29 | 31 |
| Total revenues | 3,734 | 4,575 | 3,881 | 4,231 |
| Gross profit | 416 | 488 | 501 | 553 |
| Gross profit margin | 11.2% | 10.7% | 12.9% | 13.1% |
| EBIT | 251 | 266 | 265 | 319 |
| EBIT margin | 6.7% | 5.8% | 6.8% | 7.5% |
| EBITDA | 312 | 328 | 330 | 384 |
| EBITDA margin | 8.4% | 7.2% | 8.5% | 9.1% |
| Net profit | 206 | 97 | 116 | 164 |
| Net margin | 5.5% | 2.1% | 3.0% | 3.9% |

*Source: PBG, Raiffeisen Centrobank estimates*

## RCB vs. Consensus estimates

***We are more pessimistic on net profitability given the excessive leverage impacting the financial result***

Given the 2011 order backlog amounting to PLN 4.32 bn excluding the Opole power plant construction contract, our 2012 top line estimates look more realistic than the consensus outlook on the top line, particularly in 2012. Whereas our EBIT and EBITDA lines are more or less in line with the consensus, we are much more pessimistic with respect to the net line given a) high interest costs expected resulting from elevated leverage, which in our view is not going to ease substantially until the end of next year and b) a relatively high minorities line on the back of an only 66% stake in Rafako. We also include the tender preparation costs to be charged against the income statement in 2012 and 2013.

*RCB vs. Consensus on PBG's estimates*

| | RCB | | Consensus | |
|---|---|---|---|---|
| In PLN mn | 2012e | 2013e | 2012e | 2013e |
| Revenues | 4,575 | 3,881 | 4,170 | 3,923 |
| EBITDA | 328 | 330 | 329 | 348 |
| EBITDA margin | 7.2% | 8.5% | 7.9% | 8.9% |
| EBIT | 266 | 265 | 259 | 282 |
| EBIT margin | 5.8% | 6.8% | 6.2% | 7.2% |
| Net income | 97 | 116 | 156 | 168 |
| Net margin | 2.1% | 3.0% | 3.7% | 4.3% |

*Source: Bloomberg, Raiffeisen Centrobank estimates*

## Risks

We have identified a couple of upside risks to our planning model, above all in the power engineering and the industrial construction segment due to the output increase as a result of aggressive tender participation in incinerator construction projects and power engineering.

Most of the downside risk comes from the margin squeeze (on road contracts particularly), refinancing risk, working capital management risk, goodwill impairment as well as high penalties on power engineering contracts.

# Valuation

***"Hold" recommendation with a 12-month target price of PLN 64***

We base our valuation approach on the DCF methodology and the planning model. We account for a higher beta of PBG on the back of high leverage, poor balance sheet quality and the industry cyclicality. Our DCF yields a 12-month target price of PLN 80 per share. Furthermore, we apply a 20% discount to the valuation to exclude for any uncertainties related to the capital increase (please refer to the section below, where we present the valuation sensitivities to different capital increase scenarios). Hence, our target price amounts to PLN 64.

## DCF Valuation

| FCF projection (PLN mn) | 2012e | 2013e | 2014e | 2015e | 2016e | 2017e | TV CF |
|---|---|---|---|---|---|---|---|
| **Consolidated sales** | **4,575** | **3,881** | **4,231** | **4,627** | **4,262** | **4,360** | **4,754** |
| EBITDA | 328 | 330 | 384 | 412 | 360 | 359 | 333 |
| EBITA | 266 | 265 | 319 | 347 | 295 | 294 | 268 |
| Taxes paid on EBITDA | -29 | -35 | -61 | -66 | -56 | -56 | -51 |
| **NOPLAT** | **215** | **215** | **258** | **281** | **239** | **238** | **217** |
| Adj. NOPLAT | 215 | 215 | 258 | 281 | 239 | 238 | 217 |
| Depreciation of PPE & intangibles | 62 | 65 | 65 | 65 | 65 | 65 | 65 |
| Gross investment in PPE & intangibles | 32 | -72 | -72 | -72 | -72 | -72 | -73 |
| Change in working capital | 393 | 343 | -87 | -94 | 87 | -23 | -28 |
| NWC/Sales | 27.7% | 23.8% | 23.8% | 23.8% | 23.8% | 23.8% | 24% |
| Change in LT provisions other than tax | -1 | -17 | 8 | n.a. | n.a. | n.a. | |
| Net acquisitions & disposals | 0 | 0 | 0 | 0 | 0 | 0 | |
| Free cash flow to firm | 701 | 534 | 174 | 180 | 320 | 208 | 180 |
| **Adj. free cash flow to firm** | **701** | **534** | **174** | **180** | **320** | **208** | **180** |
| **EV DCF, mid-year assumption** | **2,572** | **2,298** | | | | | |
| + MV of non-operating assets eop | 53 | 53 | | | | | |
| - MV of net debt eop | 897 | 461 | | | | | |
| - MV of minorities eop | 606 | 606 | | | | | |
| Adjustments to EV eop | 0.0 | 0.0 | | | | | |
| **Fair value of equity** | **1,123** | **1,284** | | | | | |
| Shares outstanding (mn) | 14 | 14 | | | | | |
| **Fair value per share (in PLN)** | **78.58** | **89.85** | | | | | |

| Value drivers | 2012e | 2013e | 2014e | 2015e | 2016e | 2017e | TV CF |
|---|---|---|---|---|---|---|---|
| Consolidated sales yoy | 22.5% | -15.2% | 9.0% | 9.4% | -7.9% | 2.3% | 2.5% |
| EBITDA margin | 7.2% | 8.5% | 9.1% | 8.9% | 8.4% | 8.2% | 7.0% |
| Rate of taxes paid | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% |
| Working capital/sales | 27.7% | 23.8% | 23.8% | 23.8% | 23.8% | 23.8% | 23.8% |
| Capex/depreciation | -50.7% | 110.0% | 110.0% | 110.0% | 110.0% | 110.0% | 112.8% |
| Free cash flow margin | 15.3% | 13.8% | 4.1% | 3.9% | 7.5% | 4.8% | 3.8% |

| WACC | 2012e | 2013e | 2014e | 2015e | 2016e | 2017e | TV CF |
|---|---|---|---|---|---|---|---|
| Target capital structure (at MV) | 50.0% | 50.0% | 50.0% | 50.0% | 50.0% | 50.0% | 50.0% |
| Debt/equity ratio (at MV) | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |
| Risk free rate (local) | 4.4% | 5.1% | 5.1% | 5.7% | 5.7% | 5.4% | 4.8% |
| Equity market premium | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% |
| Levered beta | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 | 1.7 |
| Cost of equity | 12.6% | 13.3% | 13.4% | 14.0% | 14.0% | 13.7% | 13.1% |
| Cost of debt | 8.4% | 9.1% | 9.1% | 9.7% | 9.7% | 9.4% | 8.8% |
| Tax rate | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% | -19.0% |
| **WACC** | **9.7%** | **10.3%** | **10.4%** | **10.9%** | **10.9%** | **10.6%** | **10.1%** |

## Sensitivity analysis

| Growth sensitivity (PLN) | | | Terminal growth rate | | | | |
|---|---|---|---|---|---|---|---|
| **WACC** | **1.0%** | **1.5%** | **2.0%** | **2.5%** | **3.0%** | **3.5%** | **4.0%** |
| 8.6% | 90.0 | 97.1 | 105.4 | 114.9 | 126.3 | 139.8 | 156.3 |
| 9.1% | 80.0 | 86.1 | 93.0 | 101.0 | 110.4 | 121.4 | 134.5 |
| 9.6% | 71.1 | 76.3 | 82.3 | 89.0 | 96.8 | 105.9 | 116.6 |
| 10.1% | 63.2 | 67.7 | 72.8 | **78.6** | 85.2 | 92.8 | 101.6 |
| 10.6% | 56.0 | 60.0 | 64.4 | 69.4 | 75.0 | 81.4 | 88.8 |
| 11.1% | 49.6 | 53.1 | 56.9 | 61.2 | 66.0 | 71.5 | 77.8 |
| 11.6% | 43.7 | 46.8 | 50.2 | 53.9 | 58.1 | 62.8 | 68.1 |

| Margin sensitivity (PLN) | | | FCF margin TV | | | | |
|---|---|---|---|---|---|---|---|
| **WACC** | **2.3%** | **2.8%** | **3.3%** | **3.8%** | **4.3%** | **4.8%** | **5.3%** |
| 8.6% | 67.7 | 83.4 | 99.2 | 114.9 | 130.7 | 146.5 | 162.2 |
| 9.1% | 58.7 | 72.8 | 86.9 | 101.0 | 115.1 | 129.2 | 143.3 |
| 9.6% | 50.9 | 63.6 | 76.3 | 89.0 | 101.7 | 114.4 | 127.1 |
| 10.1% | 44.1 | 55.6 | 67.1 | **78.6** | 90.1 | 101.6 | 113.0 |
| 10.6% | 38.0 | 48.5 | 58.9 | 69.4 | 79.8 | 90.3 | 100.7 |
| 11.1% | 32.6 | 42.1 | 51.7 | 61.2 | 70.7 | 80.3 | 89.8 |
| 11.6% | 27.7 | 36.5 | 45.2 | 53.9 | 62.6 | 71.4 | 80.1 |

*Source: Raiffeisen Centrobank estimates*

| Income statement (PLN mn) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| **Consolidated sales** | **2,573** | **2,740** | **3,734** | **4,575** | **3,881** | **4,231** |
| Cost of sales | -2,183 | -2,399 | -3,317 | -4,086 | -3,379 | -3,678 |
| **Gross profit** | **390** | **342** | **416** | **488** | **501** | **553** |
| Other operating income | 31 | 63 | 23 | 0 | 0 | 0 |
| Selling expenses | 0 | -0 | -10 | -79 | -79 | -64 |
| Administrative expenses | -110 | -109 | -129 | -144 | -157 | -171 |
| Other operating expenses | -27 | -34 | -50 | 0 | 0 | 0 |
| **EBITDA** | **332** | **308** | **312** | **328** | **330** | **384** |
| Adjusted EBITDA | 332 | 308 | 312 | 328 | 330 | 384 |
| Depreciation of PPE and intangibles | -47 | -47 | -61 | -62 | -65 | -65 |
| **EBITA** | **284** | **262** | **251** | **266** | **265** | **319** |
| Amortisation, impairment of goodwill | 0 | 0 | 0 | 0 | 0 | 0 |
| **EBIT** | **284** | **262** | **251** | **266** | **265** | **319** |
| Adjusted EBIT | 284 | 262 | 251 | 266 | 265 | 319 |
| Investment income | 0 | 0 | 0 | 0 | 0 | 0 |
| Net interest income | -28 | -29 | -15 | -111 | -82 | -64 |
| Other financial result | 4 | 2 | 0 | 0 | 0 | 0 |
| **Financial result** | **-24** | **-27** | **-15** | **-111** | **-82** | **-64** |
| **Earnings before taxes** | **260** | **234** | **236** | **155** | **183** | **255** |
| Taxes on income | -41 | -50 | -49 | -29 | -35 | -48 |
| Extraordinary result | 0 | 0 | 0 | 0 | 0 | 0 |
| **Net profit before minorities** | **220** | **185** | **187** | **126** | **149** | **207** |
| Minority interests | -11 | 6 | -16 | -28 | -33 | -42 |
| **Net profit after minorities** | **209** | **190** | **171** | **97** | **116** | **164** |
| Adjusted Net profit | 209 | 190 | 171 | 97 | 116 | 164 |

| Changes yoy | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| Consolidated sales yoy | 23.0% | 6.5% | 36.3% | 22.5% | -15.2% | 9.0% |
| EBITDA yoy | 23.0% | -7.0% | 1.2% | 5.1% | 0.6% | 16.3% |
| EBITA yoy | 27.2% | -8.0% | -4.1% | 5.9% | -0.3% | 20.3% |
| EBIT yoy | 27.2% | -8.0% | -4.1% | 5.9% | -0.3% | 20.3% |
| EBT yoy | 21.8% | -10.0% | 0.7% | -34.3% | 18.2% | 39.0% |
| Net profit after minorities yoy | 33.8% | -8.9% | -10.1% | -43.1% | 18.7% | 42.2% |

| Margins | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| Gross margin | 15.2% | 12.5% | 11.2% | 10.7% | 12.9% | 13.1% |
| EBITDA margin | 12.9% | 11.3% | 8.4% | 7.2% | 8.5% | 9.1% |
| EBITA margin | 11.1% | 9.5% | 6.7% | 5.8% | 6.8% | 7.5% |
| EBIT margin | 11.1% | 9.5% | 6.7% | 5.8% | 6.8% | 7.5% |
| EBT margin | 10.1% | 8.6% | 6.3% | 3.4% | 4.7% | 6.0% |
| Net margin | 8.1% | 6.9% | 4.6% | 2.1% | 3.0% | 3.9% |

| Profitability | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| Return on assets | 7.9% | 5.8% | 4.3% | 3.6% | 3.9% | 4.7% |
| Return on equity | 18.0% | 12.8% | 10.3% | 5.5% | 6.2% | 8.2% |
| Return on capital employed | 11.6% | 8.5% | 6.5% | 5.6% | 6.2% | 7.6% |

| Cash flow statement (PLN mn) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| **Earnings before taxes** | **260** | **234** | **271** | **155** | **183** | **255** |
| Taxes paid | -55 | -54 | -82 | -29 | -35 | -48 |
| Amortisation and depreciation | 47 | 47 | 61 | 62 | 65 | 65 |
| Other non-cash items | -32 | 19 | 38 | -1 | -17 | 8 |
| **Cash flow from result** | **220** | **246** | **289** | **187** | **197** | **280** |
| Change in working capital | 85 | 188 | -774 | 393 | 343 | -87 |
| **Operating cash flow** | **305** | **434** | **-486** | **580** | **540** | **193** |
| Capex PPE and intangible assets | -99 | -268 | -130 | 32 | -72 | -72 |
| Acquisitions | 0 | 0 | 0 | 0 | 0 | 0 |
| Disposal of fixed assets (total) | 0 | 0 | 0 | 0 | 0 | 0 |
| Other items (investments) | -251 | -262 | -20 | 0 | 0 | 0 |
| **Investing cash flow** | **-351** | **-530** | **-150** | **32** | **-72** | **-72** |
| Dividend payments | 0 | -20 | -20 | -20 | 0 | 0 |
| Other changes in equity | 182 | -0 | 3 | 0 | 0 | 0 |
| Change in financial liabilities | 278 | 227 | 615 | -619 | -400 | 0 |
| Other items | -43 | -62 | -101 | -28 | -33 | -42 |
| **Financing cash flow** | **417** | **145** | **497** | **-668** | **-433** | **-42** |

*Source: PBG, Raiffeisen Centrobank estimates*

| Balance sheet (PLN mn) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| **Current assets** | **2,998** | **3,156** | **4,385** | **3,985** | **3,481** | **3,812** |
| Liquid funds | 660 | 709 | 559 | 503 | 539 | 618 |
| Receivables | 1,837 | 1,729 | 2,689 | 2,379 | 1,940 | 2,116 |
| Inventories | 238 | 294 | 464 | 461 | 461 | 461 |
| Other assets | 262 | 425 | 672 | 643 | 541 | 617 |
| **Fixed assets** | **1,018** | **1,594** | **2,228** | **2,134** | **2,140** | **2,147** |
| Property, plant & equipment | 561 | 1,038 | 1,133 | 1,039 | 1,046 | 1,052 |
| Intangible assets | 0 | 0 | 0 | 0 | 0 | 0 |
| Goodwill | 321 | 347 | 883 | 883 | 883 | 883 |
| Financial assets | 135 | 209 | 212 | 212 | 212 | 212 |
| **Deferred tax assets** | **0** | **0** | **14** | **14** | **14** | **14** |
| **Total assets** | **4,015** | **4,750** | **6,627** | **6,133** | **5,636** | **5,973** |
| **Current liabilities** | **1,827** | **1,944** | **3,566** | **3,016** | **2,420** | **2,585** |
| Short-term borrowings | 642 | 535 | 1,399 | 800 | 400 | 400 |
| Notes & trade payables, payments received | 1,059 | 1,312 | 1,867 | 1,918 | 1,767 | 1,909 |
| Other current liabilities | 126 | 97 | 300 | 298 | 253 | 276 |
| **Long-term liabilities** | **562** | **980** | **731** | **710** | **694** | **702** |
| Long-term borrowings | 493 | 914 | 620 | 600 | 600 | 600 |
| Long-term provisions | 69 | 66 | 111 | 110 | 94 | 102 |
| Other long-term liabilities | 0 | 0 | 0 | 0 | 0 | 0 |
| **Hybrid & other mezzanine capital** | **0** | **0** | **0** | **0** | **0** | **0** |
| **Shareholders' equity** | **1,394** | **1,591** | **1,723** | **1,801** | **1,916** | **2,081** |
| **Minority interests** | **225** | **226** | **606** | **606** | **606** | **606** |
| **Deferred tax liabilities** | **41** | **8** | **0** | **0** | **0** | **0** |
| **Total liabilities** | **4,048** | **4,750** | **6,627** | **6,133** | **5,636** | **5,973** |

| Balance sheet (PLN mn) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| Net working capital | 1,152 | 1,038 | 1,658 | 1,266 | 923 | 1,009 |
| Net interest-bearing debt | 475 | 740 | 1,460 | 897 | 461 | 382 |
| Capital employed | 2,754 | 3,266 | 4,348 | 3,806 | 3,522 | 3,686 |
| Market capitalisation | 2,905 | 3,045 | 1,015 | 772 | 772 | 772 |
| Enterprise value | 3,594 | 3,941 | 3,027 | 2,221 | 1,786 | 1,706 |

| Financing (x) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| Interest cover | 6.2 | 4.1 | 4.9 | 2.7 | 3.6 | 5.0 |
| Internal financing ratio | 3.1 | 1.6 | -3.7 | -18.4 | 7.6 | 2.7 |
| Net gearing | 29.3% | 40.7% | 62.7% | 37.3% | 18.3% | 14.2% |
| Quick ratio | 1.5 | 1.5 | 1.1 | 1.2 | 1.2 | 1.3 |
| Fixed assets cover | 2.1 | 1.8 | 1.4 | 1.5 | 1.5 | 1.6 |
| Capex / depreciation | 2.1 | 5.7 | 2.1 | -0.5 | 1.1 | 1.1 |
| Equity ratio | 40.3% | 38.3% | 35.1% | 39.2% | 44.8% | 45.0% |

| Per share data (PLN) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| Weighted avg. no. of shares (mn) | 13.9 | 14.3 | 14.3 | 14.3 | 14.3 | 14.3 |
| EPS reported | 15.00 | 13.32 | 11.98 | 6.82 | 8.09 | 11.50 |
| Earnings per share (adj.) | 15.00 | 13.32 | 11.98 | 6.82 | 8.09 | 11.50 |
| Operating cash flow per share | 21.89 | 30.33 | -33.97 | 40.57 | 37.76 | 13.54 |
| Book value per share | 97.49 | 111.32 | 120.56 | 125.97 | 134.06 | 145.56 |
| DPS | 0.00 | 1.40 | 1.40 | 0.00 | 0.00 | 0.00 |
| Payout ratio | 0.0% | 10.5% | 11.7% | 0.0% | 0.0% | 0.0% |

| Valuation (x) | 12/2009 | 12/2010 | 12/2011 | 12/2012e | 12/2013e | 12/2014e |
|---|---|---|---|---|---|---|
| PE reported | 13.5 | 16.0 | 5.9 | 7.9 | 6.7 | 4.7 |
| Adjusted PE ratio | 13.5 | 16.0 | 5.9 | 7.9 | 6.7 | 4.7 |
| Price cash flow | 9.3 | 7.0 | -2.1 | 1.3 | 1.4 | 4.0 |
| Price book value | 2.1 | 1.9 | 0.6 | 0.4 | 0.4 | 0.4 |
| Dividend yield | 0.0% | 0.7% | 2.0% | 0.0% | 0.0% | 0.0% |
| Free cash flow yield | 6.6% | 5.1% | -38.0% | 44.4% | 34.0% | 8.9% |
| EV/sales | 1.4 | 1.4 | 0.8 | 0.5 | 0.5 | 0.4 |
| EV/EBITDA | 10.8 | 12.8 | 9.7 | 6.8 | 5.4 | 4.4 |
| EV/EBIT | 12.6 | 15.1 | 12.1 | 8.4 | 6.7 | 5.4 |
| EV/operating cash flow | 11.8 | 9.1 | -6.2 | 3.8 | 3.3 | 8.8 |
| Adjusted EV/CE | 1.5 | 1.4 | 0.8 | 0.7 | 0.7 | 0.6 |
| Adjusted EV/CE vs. ROCE/WACC | | | | 1.3 | 1.1 | 0.9 |

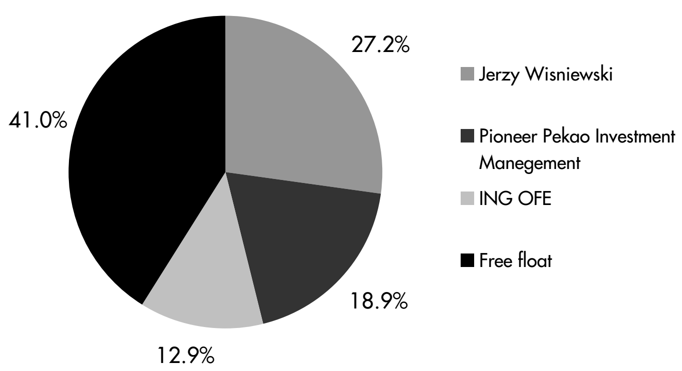
*Source: PBG, Raiffeisen Centrobank estimates*

# Fact Sheet

### Company description

PBG currently is the largest listed Polish construction company by market cap and ranks fourth in terms of sales among the major local players. In 1994 current CEO Jerzy Wisniewski and Malgorzata Wisniewska established Piecobiogaz s.c. with the business proposition to provide comprehensive services for reduction and metering stations and the construction of gas pipelines. Until today the oil & gas business is the backbone and core-competence of the company given the high margins and the relatively higher entry barriers. PBG also has a long history of entering new markets through acquisitions. For instance, in 2002 it extended its business operations into environmental protection by purchasing shares in a company today known as Hydrobudowa Polska S.A. which currently is again the potential target for a transaction. In 2004 both the legal form and the name were changed to PBG S.A. and the company debuted on the Warsaw Stock Exchange on July 2, raising PLN 96.33 mn. Other acquisitions such as Metorex or KWG followed and PBG also entered the road construction business through a number of smaller acquisitions. Recently, the company has decided to exit the working capital intensie and margin depressing roads construction segment and to diversify towards the power engineering following the acquisition of the stake in Rafako

### Shareholder structure




### Strengths/Opportunities

- Strong in oil and gas related contruction as well as the hydro engineering
- Repositioning towards the next boom of power engineering via the aquisition of the most experienced on Polish market Rafako
- Aggressive power contracts tender participation strategu
- Experienced and visionary management

### Weaknesses/Threats

- High leverage triggered by poor working capital management
- Balance sheet distorted by a very high goodwill amounting to 50% of the total equity
- Still a considerable portfolio of roads contracts in the order backlog
- High costs of power engineering tenders participation
- Execution risks related to the enourmous power engineering contracts

| ***Income statement (PLN mn)*** | ***12/2011*** | ***12/2012e*** | ***12/2013e*** | ***12/2014e*** |
|---|---|---|---|---|
| Consolidated sales | 3,734 | 4,575 | 3,881 | 4,231 |
| EBITDA | 312 | 328 | 330 | 384 |
| EBIT | 251 | 266 | 265 | 319 |
| EBT | 236 | 155 | 183 | 255 |
| Net profit bef. min. | 187 | 126 | 149 | 207 |
| Net profit after min. | 171 | 97 | 116 | 164 |
| ***Balance sheet*** | | | | |
| Total assets | 6,627 | 6,133 | 5,636 | 5,973 |
| Shareholders' equity | 1,723 | 1,801 | 1,916 | 2,081 |
| Goodwill | 883 | 883 | 883 | 883 |
| NIBD | 1,460 | 897 | 461 | 382 |
| ***Cash flow statement*** | | | | |
| Operating cash flow | -486 | 580 | 540 | 193 |
| Investing cash flow | -150 | 32 | -72 | -72 |
| Change NIBD | -720 | 563 | 435 | 80 |

| ***Per share data (PLN)*** | ***12/2011*** | ***12/2012e*** | ***12/2013e*** | ***12/2014e*** |
|---|---|---|---|---|
| EPS pre-goodwill | 11.98 | 6.82 | 8.09 | 11.50 |
| Adj. EPS diluted | 11.98 | 6.82 | 8.09 | 11.50 |
| Operating cash flow | -33.97 | 40.57 | 37.76 | 13.54 |
| Book value | 120.56 | 125.97 | 134.06 | 145.56 |
| Dividend | 1.40 | 0.00 | 0.00 | 0.00 |
| Payout ratio | 11.7% | 0.0% | 0.0% | 0.0% |
| ***Valuation (x)*** | | | | |
| PE pre-goodwill | 5.9 | 7.9 | 6.7 | 4.7 |
| Adj. PE diluted | 5.9 | 7.9 | 6.7 | 4.7 |
| Price cash flow | -2.1 | 1.3 | 1.4 | 4.0 |
| Price book value | 0.6 | 0.4 | 0.4 | 0.4 |
| Dividend yield | 2.0% | 0.0% | 0.0% | 0.0% |
| FCF yield | -38.0% | 44.4% | 34.0% | 8.9% |
| EV/EBITDA | 9.7 | 6.8 | 5.4 | 4.4 |
| EV/EBIT | 12.1 | 8.4 | 6.7 | 5.4 |
| EV/operating CF | -6.2 | 3.8 | 3.3 | 8.8 |

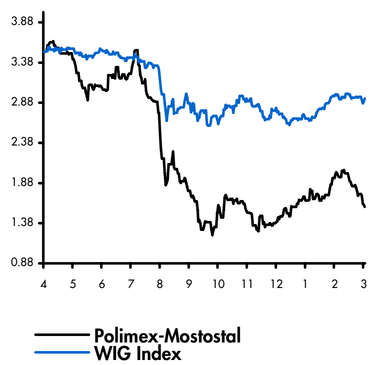
*Source: PBG, Raiffeisen Centrobank estimates*

# Company Update
## Polimex-Mostostal

**March 9, 2012** **Construction & Materials/Poland**

## Buy

| | |
|---|---|
| Price 08.03.12* | 1.58 |
| Price target | 2.05 |
| Volatility risk | medium |
| Year high/low | 3.64/1.23 |
| Currency | PLN |
| PLN/EUR | 4.10 |
| GDR rate | n.a. |
| Shares outstanding eoy in mn | 520.92 |
| Market capitalisation (total shares) in EUR mn | 200.9 |
| Free float | 75.1% |
| Free float in EUR mn | 150.9 |
| Avg. daily turnover (12 m) in EUR mn | 0.87 |
| Index | WIG |
| ISIN code | PLMSTSD00019 |
| Bloomberg | PXM PW |
| Reuters | MOSD.WA |
| www.polimex-mostostal.pl | |




*Source: Raiffeisen Centrobank*

## *No risk, no fun*

We raise our recommendation for Polimex-Mostostal to "buy" and lift the target price to PLN 2.05. We consider both Polimex-Mostostal and PBG to be high-risk Polish construction companies on the back of highly leveraged balance sheets additionally distorted by considerable goodwill. Yet, we accept the elevated risk and like the company for its sectors exposure (predominantly power engineering and railway construction), high order backlog (further boosted by the recently signed contract for the construction of two coal-fuelled power blocks in Opole for PLN 9.4 bn) and because it is the most export-oriented company and less dependent on public clients which are driven by austerity measures from among the discussed Polish construction companies. We are also in favour of the efforts to dispose of none-core assets (predominantly properties) and see the goal of PLN 100 mn to be raised in 2012 as realistic. We have to admit, however, that the company also displays the highest operating leverage (we look at the tangible assets turnover and sales generation capacity per employee). On the other hand, however, the leverage is predominantly the result of its steel products and galvanizing capacities and seems to be relatively low as far as the declining sector of road construction is concerned.

**4Q 11 preview:** We think the results (which are published on March 20) should be a non-event and in line with the recent, unofficial guidance of the CEO implying a 20% yoy top line increase for 2011 as a whole, and the net profit matching that reported in 2010. We, however, see the figures to be partially impacted by the release of employment related reserves of around PLN 30 mn. The core business should remain impacted by the general margin squeeze. We expect a good performance of the construction and roads and railways segments (higher value of the railway contracts in the sales mix) and a weak showing of the chemistry and petrochemistry (low top line) and power engineering (affected by the power construction tender costs incurred) segments. We estimate the revenues to amount to PLN 1.48 bn and forecast EBITDA of PLN 118 mn, EBIT of PLN 94 mn and the bottom line at PLN 60 mn. Moreover, we expect a net debt improvement by some PLN 400 mn and a substantially (and seasonally) decreased working capital commitment (predominantly in the receivables from road contracts).

**Valuation and recommendation:** For almost a year we have been advocates of the valuation convergence thesis of the Polish construction companies towards the European peers on the back of the Polish construction market openness and a fierce competition squeezing the margins. We see the valuation to be in line now, hence see further de-rating very limited. Furthermore, our updated DCF-model yields a 12-month target price of PLN 2.05, which triggers the recommendation raise to "buy".

### *Key figures and ratios*

| PLN | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|
| Sales (mn) | 4,397 | 4,161 | 4,950 | 4,845 | 5,210 |
| EBITDA (mn) | 344 | 302 | 276 | 241 | 296 |
| EBIT (mn) | 265 | 213 | 179 | 138 | 186 |
| Net profit a.m. (mn) | 156 | 110 | 104 | 56 | 103 |
| Earnings per share (adj.) | 0.33 | 0.23 | 0.20 | 0.10 | 0.19 |
| EPS adjusted growth | 30.3% | -29.9% | -15.1% | -47.1% | 84.2% |
| Adjusted PE ratio | 12.1 | 17.4 | 8.5 | 15.3 | 8.3 |
| DPS | 0.04 | 0.04 | 0.04 | 0.02 | 0.04 |
| Dividend yield | 1.0% | 1.1% | 2.4% | 1.4% | 2.5% |
| EV/EBITDA | 6.6 | 8.5 | 5.2 | 5.1 | 3.1 |
| Price book value | 1.5 | 1.4 | 0.6 | 0.5 | 0.5 |

*Source: Polimex-Mostostal, Raiffeisen Centrobank estimates*

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* The indicated price is the last price as available at 6.30 AM on 09.03.12

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### *Share price triggers*

| *Trigger* | *Momentum* | *Explanation* |
|---|---|---|
| **Power engineering** | positive | ▪ Polimex-Mostostal is engaged in most of the power engineering contracts that are currently running<br>▪ We expect some of them to be concluded this year (for instance, Kozienice for Enea, Ostroleka for Energa) |
| **Railway construction** | positive | ▪ Spendings on railway infrastructure are to gradually increase<br>▪ We see the competition on a general contractor position rising, yet the capacities in terms of machines and equipment available in Poland are limited<br>▪ Hence, we expect Polimex-Mostostal to substantially increase its railway related order backlog<br>▪ The new EU budget is supposedly to be concentrated more on railway construction |
| **EU budget for 2014-2020** | neutral/positive | ▪ According to a preliminary draft, Poland is to receive a higher funds allocation than in the previous budget ending in 2013<br>▪ The street is, however, sceptical about a higher allocation<br>▪ We think that figures coming close to the current budget should inject some more optimism into the valuation of the construction sector |
| **Net debt** | positive | ▪ We expect an improvement of the liquidity position of Polimex-Mostostal in 4Q 11 and thereafter another increase via the advances of the Opole power plant construction which will amount to a couple of hundred million PLN as well as via the improvement of the working capital cycle as a result of the completion of road construction contracts |
| **Road construction** | negative | ▪ Polimex-Mostostal keeps reporting relatively high margins on road contracts<br>▪ We are suspicious about those figures and expect the profitability to be substantially hit upon the contracts' completion |

*Source: Raiffeisen Centrobank*

## 4Q 11 preview

***4Q 11 should be in line with the CEO's recent unofficial guidance with the profitability impacted by the reserves release***

We see Polimex-Mostostal's 4Q results to reflect the recent, unofficial guidance of the CEO stating a 20% yoy top line increase in 2011 and the net profit to exceed PLN 100 mn last year. We, thus, expect the group's revenues to reach almost PLN 1.5 bn in 4Q 11 (the highest quarterly sales ever recorded by the company) and net profit to slightly exceed PLN 60 mn. Yet, we see the profitability to be impacted by the release of reserves for employment expenses following an agreement with the trade unions. We estimate the impact to amount to PLN 30 mn, i.e. 30% of the expected 4Q 11 EBIT. Hence the normalized EBIT margin should hover around 4.3% (vs. the reported 6.3%), an improvement on a qoq basis, yet quite a squeeze when compared to 4Q 10 (a trend observed among all the large Polish construction companies).

We expect the production segment's top line to increase by some 10% yoy with a slight normalized margin improvement. Yet the actual margins should be boosted by the aforementioned reserves release (most of Polimex-Mostostal's employment is concentrated around the production facilities). The construction segment should increase by some 9% as well, on the back of quite a significant order backlog. We also expect a margin improvement in comparison to the previous quarter. The petrochemical and chemical segment should remain weak, with subdued sales as a consequence of poor order backlog. We project the segment to be in the red in 4Q 11. Power engineering's margins should still be affected by the tender participation costs (offer preparation) which Polimex-Mostostal incurs and we expect revenues to be only slightly higher yoy. The roads and railways construction segment is to be the strongest performer with the top line increasing by about 65% (a result of both high order backlog as well as a warm 4Q 11) and a slight margin improvement coming from an increase of the railway construction works in the sales mix.

Furthermore, we expect the net-debt balance to shrink substantially from 3Q 11 figures as a result of lower working capital commitment (seasonally decreasing receivables). We think the further improvement should materialise in the next 1-1.5 years following the completion of road construction projects by Polimex-Mostostal and its consortium members. We also see the cash flow from operations to break even in 2011 as a whole after an outflow of almost PLN 400 mn reported after the first three quarters of last year.

**Polimex-Mostostal 4Q 11 preview**

| In PLN mn | 4Q 11e | 4Q 10 | +/-% | 3Q 11 | +/-% |
|---|---|---|---|---|---|
| Revenues | 1,482 | 1,186 | 25% | 1,362 | 9% |
| Gross profit | 129 | 145 | -11% | 63 | 105% |
| EBIT | 94 | 90 | 4% | 15 | 534% |
| EBITDA | 118 | 107 | 10% | 39 | 203% |
| Net income a.m. | 60 | 53 | 14% | 15 | 301% |
| Gross profit margin | 8.7% | 12.2% | | 4.6% | |
| EBIT margin | 6.3% | 7.6% | | 1.1% | |
| EBITDA margin | 8.0% | 9.0% | | 2.9% | |
| Net margin | 4.1% | 4.4% | | 1.1% | |

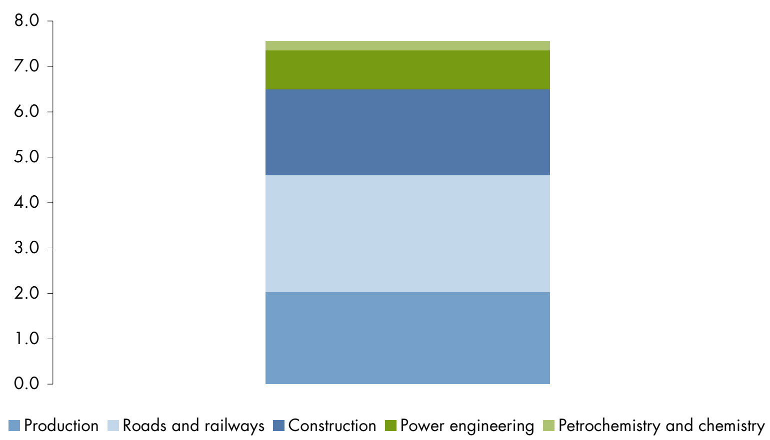
*Source: Polimex-Mostostal, Raiffeisen Centrobank estimates*

## Planning model

***Record-high order backlog after Opole power contract supporting strong sales***

Considering the current order backlog of PLN 7.6 bn estimated at the end of 2011 and the Opole power blocks construction contract with a total value of PLN 9.4 bn (Polimex-Mostostal share amounts to 42%), we have upgraded our planning model. We basically lift our revenue estimates across all the sectors, particularly in the production and power engineering businesses. We have turned much more cautious on profitability, though, and considerably slash our assumptions in terms of gross profit margins for the petrochemical and chemical segment, railway construction on the back of increasing competition as well as the roads project, where we assume no profits to be generated in 2012. Our view is that the company has been recognizing its roads contracts' profitability too aggressively and sooner or later will have to revise its assumptions.

**2011-end estimated order backlog composition (ex Opole)**




*Source: Polimex-Mostostal, Raiffeisen Centrobank estimates*

Moreover, we assume Polimex-Mostostal to liquidate PLN 100 mn of its real estate properties, yet with a 10% loss (booked in the other operating loss line).

### *Polimex-Mostostal planning model*

| | Old | | | | | |
|---|---|---|---|---|---|---|
| ***In PLN mn*** | ***2011e*** | ***2012e*** | ***2013e*** | ***2011e*** | ***2012e*** | ***2013e*** |
| Total revenues | 4,468 | 4,508 | 4,070 | 4,950 | 4,845 | 5,210 |
| Production revenues | 621 | 558 | 475 | 676 | 744 | 670 |
| Production margins | 12.7% | 15.0% | 15.0% | 14.7% | 15.0% | 15.0% |
| Construction and other revenues | 1,297 | 1,167 | 992 | 1,337 | 1,204 | 1,204 |
| Construction margins | 7.9% | 8.0% | 8.0% | 6.7% | 7.0% | 7.0% |
| Power engineering revenues | 931 | 931 | 1,025 | 994 | 1,093 | 1,464 |
| Power engineering margins | 8.7% | 10.0% | 10.0% | 6.1% | 10.0% | 10.0% |
| Chemistry revenues | 395 | 395 | 395 | 424 | 424 | 424 |
| Chemistry margins | 12.7% | 12.0% | 12.0% | 4.3% | 5.0% | 5.0% |
| Roads and railways revenues | 1,224 | 1,456 | 1,183 | 1,518 | 1,380 | 1,448 |
| Roads and railways margins | 5.9% | 6.4% | 6.9% | 6.2% | 2.2% | 4.0% |
| Gross profit | 386 | 411 | 382 | 363 | 356 | 411 |
| Gross profit margin | 9.8% | 10.0% | 10.1% | 7.3% | 7.4% | 7.9% |
| Net income | 73 | 78 | 78 | 104 | 56 | 103 |
| Net income margin | 2.7% | 2.7% | 2.8% | 2.1% | 1.1% | 2.0% |

*Source: Raiffeisen Centrobank estimates*

### RCB vs. Consensus

***RCB seems to be more cautious than the consensus on profitability***

We stay slightly more cautious on 2012 figures, particularly on profitability. Our margins are a bit lower than the consensus projections - we believe on the back of our more conservative assumptions regarding the road contracts execution as well as a probable loss to be generated on the property disposal. In terms of 2013 revenues we are more aggressive (pricing in the Opole project), yet still slightly more conservative on profitability for fear of the ongoing competitive pressure. We also price in potential high interest costs on the back of an elevated leverage.

### *RCB vs. Consensus on Polimex-Mostostal*

| | RCB | | | |
|---|---|---|---|---|
| ***In PLN mn*** | ***2012e*** | ***2013e*** | ***2012e*** | ***2013e*** |
| Revenues | 4,845 | 5,210 | 4,981 | 4,962 |
| EBITDA | 241 | 296 | 282 | 311 |
| EBITDA margin | 5.0% | 5.7% | 5.7% | 6.3% |
| EBIT | 138 | 186 | 169 | 186 |
| EBIT margin | 2.8% | 3.6% | 3.4% | 3.8% |
| Net profit | 56 | 103 | 80 | 101 |
| Net margin | 1.1% | 2.0% | 1.6% | 2.0% |

*Source: Bloomberg, Raiffeisen Centrobank estimates*

## *Valuation*

***We raise our recommendation to "buy" and raise our TP to PLN 2.05***

We stick to our DCF model, which yields a 12-month target price of PLN 2.05. This translates into a recommendation upgrade from "hold" to "buy".

## DCF Valuation

| *FCF projection (PLN mn)* | *2011e* | *2012e* | *2013e* | *2014e* | *2015e* | *2016e* | *TV CF* |
|---|---|---|---|---|---|---|---|
| **Consolidated sales** | **4,950** | **4,845** | **5,210** | **5,653** | **6,133** | **6,515** | **6,778** |
| EBITDA | 276 | 241 | 296 | 232 | 337 | 358 | 373 |
| EBITA | 179 | 138 | 186 | 232 | 227 | 241 | 230 |
| Taxes paid on EBITDA | -30 | -13 | -15 | -23 | -22 | -24 | -23 |
| **NOPLAT** | **161** | **130** | **171** | **210** | **205** | **217** | **207** |
| Adj. NOPLAT | 161 | 130 | 171 | 210 | 205 | 217 | 207 |
| Depreciation of PPE & intangibles | 97 | 103 | 110 | 0 | 110 | 118 | 143 |
| Gross investment in PPE & intangibles | -106 | -113 | -121 | -129 | -121 | -129 | -158 |
| Change in working capital | -189 | 162 | 14 | -47 | -272 | -48 | -21 |
| NWC/Sales | 12.6% | 9.5% | 8.6% | 8.7% | 12.5% | 12.5% | 13% |
| Change in LT provisions other than tax | 17 | -2 | 8 | 10 | n.a. | n.a. | |
| Net acquisitions & disposals | 0 | 0 | 0 | 0 | 0 | 0 | |
| Free cash flow to firm | -21 | 279 | 182 | 43 | -78 | 158 | 171 |
| **Adj. free cash flow to firm** | **-21** | **279** | **182** | **43** | **-78** | **158** | **171** |
| **EV DCF, mid-year assumption** | **1,572** | **1,450** | | | | | |
| + MV of non-operating assets eop | 15 | 16 | | | | | |
| - MV of net debt eop | 588 | 405 | | | | | |
| - MV of minorities eop | 10 | 10 | | | | | |
| Adjustments to EV eop | 0.0 | 0.0 | | | | | |
| **Fair value of equity** | **989** | **1,051** | | | | | |
| Shares outstanding (mn) | 521 | 521 | | | | | |
| **Fair value per share (in PLN)** | **1.90** | **2.02** | | | | | |

| *Value drivers* | *2011e* | *2012e* | *2013e* | *2014e* | *2015e* | *2016e* | *TV CF* |
|---|---|---|---|---|---|---|---|
| Consolidated sales yoy | 19.0% | -2.1% | 7.5% | 8.5% | 8.5% | 6.2% | 2.5% |
| EBITDA margin | 5.6% | 5.0% | 5.7% | 4.1% | 5.5% | 5.5% | 5.5% |
| Rate of taxes paid | -10.3% | -5.5% | -8.2% | -9.8% | -9.8% | -9.8% | -9.8% |
| Working capital/sales | 12.6% | 9.5% | 8.6% | 8.7% | 12.5% | 12.5% | 12.5% |
| Capex/depreciation | 110.0% | 110.0% | 110.0% | 0.0% | 110.0% | 110.0% | 110.2% |
| Free cash flow margin | -0.4% | 5.8% | 3.5% | 0.8% | -1.3% | 2.4% | 2.5% |

| *WACC* | *2011e* | *2012e* | *2013e* | *2014e* | *2015e* | *2016e* | *TV CF* |
|---|---|---|---|---|---|---|---|
| Target capital structure (at MV) | 64.4% | 60.9% | 69.3% | 90.2% | 90.0% | 90.0% | 90.0% |
| Debt/equity ratio (at MV) | 55.2% | 64.2% | 44.2% | 10.9% | 11.1% | 11.1% | 11.1% |
| Risk free rate (local) | 4.9% | 4.8% | 4.6% | 5.1% | 5.5% | 6.1% | 4.8% |
| Equity market premium | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% |
| Levered beta | 1.4 | 1.4 | 1.4 | 1.4 | 1.4 | 1.4 | 1.4 |
| Cost of equity | 12.0% | 12.0% | 11.8% | 12.3% | 12.6% | 13.2% | 12.0% |
| Cost of debt | 7.9% | 7.8% | 7.6% | 7.1% | 8.5% | 9.1% | 8.8% |
| Tax rate | -10.3% | -5.5% | -8.2% | -9.8% | -9.8% | -9.8% | -9.8% |
| **WACC** | **10.2%** | **10.2%** | **10.3%** | **11.7%** | **12.1%** | **12.7%** | **11.5%** |

## Sensitivity analysis

| *Growth sensitivity (PLN)* | | | *Terminal growth rate* | | | | |
|---|---|---|---|---|---|---|---|
| ***WACC*** | ***2.0%*** | ***2.5%*** | ***3.0%*** | ***3.5%*** | ***4.0%*** | ***-27.5%*** | ***-17.5%*** |
| 10.0% | 2.0 | 2.1 | 2.2 | 2.4 | 2.5 | 2.7 | 2.9 |
| 10.5% | 1.9 | 1.9 | 2.0 | 2.2 | 2.3 | 2.4 | 2.6 |
| 11.0% | 1.7 | 1.8 | 1.9 | 2.0 | 2.1 | 2.2 | 2.3 |
| 11.5% | 1.6 | 1.6 | 1.7 | **1.8** | 1.9 | 2.0 | 2.1 |
| 12.0% | 1.4 | 1.5 | 1.6 | 1.6 | 1.7 | 1.8 | 1.9 |
| 12.5% | 1.3 | 1.4 | 1.4 | 1.5 | 1.6 | 1.6 | 1.7 |
| 13.0% | 1.2 | 1.3 | 1.3 | 1.4 | 1.4 | 1.5 | 1.6 |

| *Margin sensitivity (PLN)* | | | *FCF margin TV* | | | | |
|---|---|---|---|---|---|---|---|
| ***WACC*** | ***2.0%*** | ***2.5%*** | ***3.0%*** | ***3.5%*** | ***4.0%*** | ***-27.5%*** | ***-17.5%*** |
| 10.0% | 1.2 | 1.6 | 2.0 | 2.4 | 2.8 | 3.2 | 3.5 |
| 10.5% | 1.1 | 1.5 | 1.8 | 2.2 | 2.5 | 2.9 | 3.2 |
| 11.0% | 1.0 | 1.3 | 1.6 | 2.0 | 2.3 | 2.6 | 2.9 |
| 11.5% | 0.9 | 1.2 | 1.5 | **1.8** | 2.1 | 2.4 | 2.6 |
| 12.0% | 0.8 | 1.1 | 1.4 | 1.6 | 1.9 | 2.1 | 2.4 |
| 12.5% | 0.8 | 1.0 | 1.2 | 1.5 | 1.7 | 2.0 | 2.2 |
| 13.0% | 0.7 | 0.9 | 1.1 | 1.4 | 1.6 | 1.8 | 2.0 |

*Source: Raiffeisen Centrobank estimates*

# Polimex-Mostostal

| Income statement (PLN mn) | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| **Consolidated sales** | **4,301** | **4,397** | **4,161** | **4,950** | **4,845** | **5,210** |
| Cost of sales | -3,871 | -3,887 | -3,723 | -4,586 | -4,488 | -4,799 |
| **Gross profit** | **430** | **510** | **438** | **363** | **356** | **411** |
| Other operating income | 36 | 18 | 26 | 30 | 0 | 0 |
| Selling expenses | -32 | -27 | -30 | -38 | -37 | -40 |
| Administrative expenses | -185 | -213 | -210 | -175 | -172 | -185 |
| Other operating expenses | -20 | -23 | -10 | 0 | -10 | 0 |
| **EBITDA** | **265** | **344** | **302** | **276** | **241** | **296** |
| Adjusted EBITDA | 265 | 344 | 302 | 276 | 241 | 296 |
| Depreciation of PPE and intangibles | -37 | -79 | -89 | -97 | -103 | -110 |
| **EBITA** | **228** | **265** | **213** | **179** | **138** | **186** |
| Amortisation, impairment of goodwill | 0 | 0 | 0 | 0 | 0 | 0 |
| **EBIT** | **228** | **265** | **213** | **179** | **138** | **186** |
| Adjusted EBIT | 228 | 265 | 213 | 179 | 138 | 186 |
| Investment income | 3 | 6 | -1 | 0 | 0 | 0 |
| Net interest income | -72 | -56 | -57 | -44 | -68 | -58 |
| Other financial result | -0 | 0 | 0 | 0 | 0 | 0 |
| **Financial result** | **-69** | **-49** | **-58** | **-44** | **-68** | **-58** |
| **Earnings before taxes** | **159** | **216** | **155** | **135** | **69** | **128** |
| Taxes on income | -18 | -40 | -36 | -30 | -13 | -24 |
| Extraordinary result | 0 | 0 | 0 | 0 | 0 | 0 |
| **Net profit before minorities** | **140** | **175** | **119** | **105** | **56** | **104** |
| Minority interests | -20 | -19 | -10 | -1 | -1 | -1 |
| **Net profit after minorities** | **120** | **156** | **110** | **104** | **56** | **103** |
| Adjusted Net profit | 120 | 156 | 110 | 104 | 55 | 102 |

| Changes yoy | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| Consolidated sales yoy | 15.4% | 2.2% | -5.4% | 19.0% | -2.1% | 7.5% |
| EBITDA yoy | 33.9% | 29.8% | -12.2% | -8.6% | -12.7% | 23.1% |
| EBITA yoy | 38.5% | 16.1% | -19.7% | -15.8% | -23.2% | 35.3% |
| EBIT yoy | 38.5% | 16.1% | -19.7% | -15.8% | -23.2% | 35.3% |
| EBT yoy | 3.3% | 35.8% | -28.0% | -13.1% | -48.5% | 84.2% |
| Net profit after minorities yoy | 14.9% | 30.3% | -29.9% | -5.0% | -46.5% | 84.2% |

| Margins | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| Gross margin | 10.0% | 11.6% | 10.5% | 7.3% | 7.4% | 7.9% |
| EBITDA margin | 6.2% | 7.8% | 7.3% | 5.6% | 5.0% | 5.7% |
| EBITA margin | 5.3% | 6.0% | 5.1% | 3.6% | 2.8% | 3.6% |
| EBIT margin | 5.3% | 6.0% | 5.1% | 3.6% | 2.8% | 3.6% |
| EBT margin | 3.7% | 4.9% | 3.7% | 2.7% | 1.4% | 2.5% |
| Net margin | 2.8% | 3.6% | 2.6% | 2.1% | 1.1% | 2.0% |

| Profitability | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| Return on assets | 8.4% | 6.6% | 4.6% | 2.5% | 2.8% | 3.7% |
| Return on equity | 12.1% | 13.7% | 8.1% | 7.0% | 3.6% | 6.4% |
| Return on capital employed | 14.9% | 11.7% | 8.0% | 4.3% | 4.9% | 6.8% |

| Cash flow statement (PLN mn) | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| **Earnings before taxes** | **159** | **216** | **155** | **135** | **69** | **128** |
| Taxes paid | -45 | -57 | -21 | -30 | -13 | -24 |
| Amortisation and depreciation | 70 | 79 | 88 | 97 | 103 | 110 |
| Other non-cash items | 32 | 32 | 45 | 13 | -2 | 8 |
| **Cash flow from result** | **217** | **270** | **267** | **214** | **157** | **222** |
| Change in working capital | 139 | 275 | -230 | -189 | 162 | 14 |
| **Operating cash flow** | **355** | **544** | **37** | **25** | **319** | **236** |
| Capex PPE and intangible assets | -226 | -344 | -131 | -106 | -113 | -121 |
| Acquisitions | 0 | 0 | 0 | 0 | 0 | 0 |
| Disposal of fixed assets (total) | 0 | 0 | 0 | -26 | 2 | -5 |
| Other items (investments) | -77 | -5 | 3 | 11 | 0 | 0 |
| **Investing cash flow** | **-303** | **-349** | **-128** | **-122** | **-112** | **-126** |
| Dividend payments | 0 | 0 | 0 | -22 | -21 | -11 |
| Other changes in equity | 0 | 0 | 0 | 0 | 0 | 0 |
| Change in financial liabilities | 143 | -8 | 96 | 132 | -200 | 0 |
| Other items | -43 | -45 | -68 | 24 | -3 | 207 |
| **Financing cash flow** | **100** | **-53** | **27** | **133** | **-224** | **196** |

*Source: Polimex-Mostostal, Raiffeisen Centrobank estimates*

| *Balance sheet (PLN mn)* | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| **Current assets** | **2,031** | **2,142** | **2,211** | **2,825** | **2,463** | **2,876** |
| Liquid funds | 303 | 454 | 385 | 412 | 395 | 700 |
| Receivables | 1,322 | 1,328 | 1,383 | 1,930 | 1,696 | 1,719 |
| Inventories | 395 | 351 | 433 | 470 | 360 | 443 |
| Other assets | 11 | 10 | 10 | 13 | 12 | 13 |
| **Fixed assets** | **1,317** | **1,599** | **1,648** | **1,689** | **1,698** | **1,714** |
| Property, plant & equipment | 711 | 948 | 1,028 | 1,037 | 1,047 | 1,057 |
| Intangible assets | 23 | 31 | 25 | 26 | 26 | 27 |
| Goodwill | 486 | 487 | 487 | 491 | 491 | 491 |
| Financial assets | 97 | 134 | 108 | 134 | 133 | 138 |
| **Deferred tax assets** | **67** | **86** | **64** | **64** | **64** | **64** |
| **Total assets** | **3,416** | **3,828** | **3,924** | **4,578** | **4,225** | **4,654** |
| **Current liabilities** | **1,635** | **1,627** | **1,708** | **2,190** | **1,806** | **1,928** |
| Short-term borrowings | 318 | 155 | 317 | 400 | 200 | 200 |
| Notes & trade payables, payments received | 1,190 | 1,358 | 1,293 | 1,683 | 1,502 | 1,615 |
| Other current liabilities | 128 | 114 | 98 | 107 | 105 | 112 |
| **Long-term liabilities** | **612** | **798** | **733** | **823** | **819** | **1,035** |
| Long-term borrowings | 436 | 603 | 552 | 600 | 600 | 600 |
| Long-term provisions | 79 | 82 | 92 | 109 | 107 | 115 |
| Other long-term liabilities | 98 | 113 | 89 | 114 | 112 | 320 |
| **Hybrid & other mezzanine capital** | **0** | **0** | **0** | **0** | **0** | **0** |
| **Shareholders' equity** | **1,033** | **1,243** | **1,449** | **1,531** | **1,566** | **1,658** |
| **Minority interests** | **115** | **141** | **10** | **10** | **10** | **10** |
| **Deferred tax liabilities** | **21** | **19** | **24** | **24** | **24** | **24** |
| **Total liabilities** | **3,416** | **3,828** | **3,924** | **4,578** | **4,225** | **4,654** |

| *Balance sheet (PLN mn)* | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| Net working capital | 411 | 217 | 435 | 624 | 462 | 448 |
| Net interest-bearing debt | 450 | 304 | 483 | 588 | 405 | 100 |
| Capital employed | 1,902 | 2,141 | 2,327 | 2,541 | 2,376 | 2,467 |
| Market capitalisation | 1,416 | 1,843 | 2,084 | 865 | 823 | 823 |
| Enterprise value | 1,961 | 2,263 | 2,562 | 1,447 | 1,222 | 916 |

| *Financing (x)* | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| Interest cover | 2.4 | 4.8 | 4.1 | n.a. | 3.2 | 4.2 |
| Internal financing ratio | 1.6 | 1.6 | 0.3 | 0.2 | 2.8 | 1.9 |
| Net gearing | 39.2% | 22.0% | 33.1% | 38.2% | 25.7% | 6.0% |
| Quick ratio | 1.0 | 1.1 | 1.0 | 1.1 | 1.2 | 1.3 |
| Fixed assets cover | 1.3 | 1.4 | 1.3 | 1.4 | 1.4 | 1.6 |
| Capex / depreciation | 6.2 | 4.4 | 1.5 | 1.1 | 1.1 | 1.1 |
| Equity ratio | 33.6% | 36.1% | 37.2% | 33.7% | 37.3% | 35.8% |

| *Per share data (PLN)* | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| Weighted avg. no. of shares (mn) | 464.4 | 464.4 | 464.4 | 520.9 | 520.9 | 520.9 |
| EPS reported | 0.26 | 0.34 | 0.24 | 0.20 | 0.11 | 0.20 |
| Earnings per share (adj.) | 0.25 | 0.33 | 0.23 | 0.20 | 0.10 | 0.19 |
| Operating cash flow per share | 0.77 | 1.17 | 0.08 | 0.05 | 0.61 | 0.45 |
| Book value per share | 2.23 | 2.68 | 2.78 | 2.94 | 3.01 | 3.18 |
| DPS | 0.01 | 0.04 | 0.04 | 0.04 | 0.02 | 0.04 |
| Payout ratio | 3.9% | 11.9% | 20.0% | 20.0% | 20.0% | 20.0% |

| *Valuation (x)* | 12/2008 | 12/2009 | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|---|---|
| PE reported | 11.8 | 11.8 | 16.9 | 8.3 | 14.8 | 8.0 |
| Adjusted PE ratio | 12.1 | 12.1 | 17.4 | 8.5 | 15.3 | 8.3 |
| Price cash flow | 4.0 | 3.4 | 49.9 | 33.9 | 2.6 | 3.5 |
| Price book value | 1.4 | 1.5 | 1.4 | 0.6 | 0.5 | 0.5 |
| Dividend yield | 0.3% | 1.0% | 1.1% | 2.4% | 1.4% | 2.5% |
| Free cash flow yield | 8.4% | 10.1% | -4.5% | -9.2% | 24.6% | 13.8% |
| EV/sales | 0.5 | 0.5 | 0.6 | 0.3 | 0.3 | 0.2 |
| EV/EBITDA | 7.4 | 6.6 | 8.5 | 5.2 | 5.1 | 3.1 |
| EV/EBIT | 8.6 | 8.5 | 12.0 | 8.1 | 8.9 | 4.9 |
| EV/operating cash flow | 5.5 | 4.2 | 68.8 | 56.8 | 3.8 | 3.9 |
| Adjusted EV/CE | 1.2 | 1.3 | 1.3 | 0.7 | 0.7 | 0.7 |
| Adjusted EV/CE vs. ROCE/WACC | | | | 1.7 | 1.4 | 1.0 |

*Source: Polimex-Mostostal, Raiffeisen Centrobank estimates*

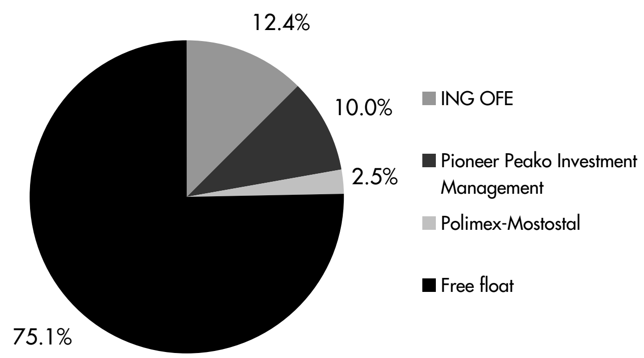
# Polimex-Mostostal

## Fact Sheet

### Company description

Polimex-Mostostal S.A. is an engineering and construction company active on the market since 1945 and is considered one of the leading companies on the Polish construction market. The company offers a wide range of construction and installation services and is a general contractor in the following segments: power engineering, road and railway construction, environmental protection, chemicals and petrochemicals, oil and gas, industry as well as housing, Furthermore, the company is one of the most important Polish manufacturers and exporters of steel products including platform gratings. Polimex-Mostostal is also the leader with respect to modern corrosion protection, in particular hot dip galvanizing.

### Shareholder structure




### Strengths/Opportunities

- Diversification of revenue sources
- Strong order backlog protecting against potential slowdown
- Exposure to niche segments delivering above-average margins: steel constructions, power engineering, railway and chemical segment
- Strong position to thrive in the two booming segments next: power engineering and railway construction
- Funds flowing to Poland and the attractiveness of the economy

### Weaknesses/Threats

- Increasing competition
- Likely increase in raw material prices
- Delay in power engineering projects resulting from unfavourable CO2 emission certificate grants
- Uncertainty regarding funding for railway modernization projects
- Uncertainly regarding EU funding beyond 2013
- Never -ending story of delays in projects managed by the Polish government

| Income statement (PLN mn) | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|
| Consolidated sales | 4,161 | 4,950 | 4,845 | 5,210 |
| EBITDA | 302 | 276 | 241 | 296 |
| EBIT | 213 | 179 | 138 | 186 |
| EBT | 155 | 135 | 69 | 128 |
| Net profit bef. min. | 119 | 105 | 56 | 104 |
| Net profit after min. | 110 | 104 | 56 | 103 |
| **Balance sheet** | | | | |
| Total assets | 3,924 | 4,578 | 4,225 | 4,654 |
| Shareholders' equity | 1,449 | 1,531 | 1,566 | 1,658 |
| Goodwill | 487 | 491 | 491 | 491 |
| NIBD | 483 | 588 | 405 | 100 |
| **Cash flow statement** | | | | |
| Operating cash flow | 37 | 25 | 319 | 236 |
| Investing cash flow | -128 | -122 | -112 | -126 |
| Change NIBD | -178 | -105 | 183 | 305 |

*Source: Polimex-Mostostal, Raiffeisen Centrobank estimates*

| Per share data (PLN) | 12/2010 | 12/2011e | 12/2012e | 12/2013e |
|---|---|---|---|---|
| EPS pre-goodwill | 0.24 | 0.20 | 0.11 | 0.20 |
| Adj. EPS diluted | 0.23 | 0.20 | 0.10 | 0.19 |
| Operating cash flow | 0.08 | 0.05 | 0.61 | 0.45 |
| Book value | 2.78 | 2.94 | 3.01 | 3.18 |
| Dividend | 0.04 | 0.04 | 0.02 | 0.04 |
| Payout ratio | 20.0% | 20.0% | 20.0% | 20.0% |
| **Valuation (x)** | | | | |
| PE pre-goodwill | 16.9 | 8.3 | 14.8 | 8.0 |
| Adj. PE diluted | 17.4 | 8.5 | 15.3 | 8.3 |
| Price cash flow | 49.9 | 33.9 | 2.6 | 3.5 |
| Price book value | 1.4 | 0.6 | 0.5 | 0.5 |
| Dividend yield | 1.1% | 2.4% | 1.4% | 2.5% |
| FCF yield | -4.5% | -9.2% | 24.6% | 13.8% |
| EV/EBITDA | 8.5 | 5.2 | 5.1 | 3.1 |
| EV/EBIT | 12.0 | 8.1 | 8.9 | 4.9 |
| EV/operating CF | 68.8 | 56.8 | 3.8 | 3.9 |

### Budimex

#### Publication schedule

| Date | Publication |
|---|---|
| 20.03.2012 | 4Q Earnings release |
| 25.04.2012 | 1Q Earnings release |
| 25.07.2012 | 2Q Preliminary results |
| 31.08.2012 | 2Q Earnings release |
| 29.10.2012 | 3Q Earnings release |

#### Recommendation history

| Date | Rating | Target Price | Prev. day's close | Upside |
|---|---|---|---|---|
| 20.04.2011 | Hold | 112.00 | 108.40 | 3.3% |

### Mostostal Warszawa

#### Publication schedule

| Date | Publication |
|---|---|
| 20.03.2012 | 4Q Earnings release |
| 15.05.2012 | 1Q Earnings release |
| 31.08.2012 | 2Q Earnings release |
| 14.11.2012 | 3Q Earnings release |

#### Recommendation history

| Date | Rating | Target Price | Prev. day's close | Upside |
|---|---|---|---|---|
| 08.09.2011 | Reduce | 19.60 | 20.15 | -2.7% |
| 31.05.2011 | Sell | 27.50 | 34.00 | -19.1% |
| 14.04.2011 | Reduce | 40.00 | 43.20 | -7.4% |

### PBG

#### Publication schedule

| Date | Publication |
|---|---|
| 15.05.2012 | 1Q Earnings release |
| 31.08.2012 | 2Q Earnings release |
| 14.11.2012 | 3Q Earnings release |

#### Recommendation history

| Date | Rating | Target Price | Prev. day's close | Upside |
|---|---|---|---|---|
| 15.04.2011 | Reduce | 205.00 | 174.20 | 17.7% |

### Polimex-Mostostal

#### Publication schedule

| Date | Publication |
|---|---|
| 20.03.2012 | 4Q Earnings release |
| 14.05.2012 | 1Q Earnings release |
| 30.08.2012 | 2Q Earnings release |
| 09.11.2012 | 3Q Earnings release |

#### Recommendation history

| Date | Rating | Target Price | Prev. day's close | Upside |
|---|---|---|---|---|
| 14.09.2011 | Hold | 1.60 | 1.40 | 14.3% |
| 27.05.2011 | Hold | 3.20 | 3.10 | 3.2% |

*Coverage universe recommendation overview*

| | buy | hold | reduce | sell | suspended | UR |
|---|---|---|---|---|---|---|
| Universe | 38 | 47 | 6 | 3 | 27 | 6 |
| Investment banking services | 8 | 13 | 1 | 0 | 5 | 0 |

*Source: Raiffeisen Centrobank*

# Acknowledgements

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Buy: Buy stocks are expected to have a total return of at least 15% (20% for shares with a high volatility risk) and are the most attractive stocks in our coverage universe on a 12 month horizon.
Hold: Hold stocks are expected to deliver a positive total return of up to 15% (20% for shares with a high volatility risk) within a 12-month period.
Reduce: Reduce stocks are expected to achieve a negative total return up to -10% within a 12-month period.
Sell: Sell stocks are expected to post a negative total return of more than -10% within a 12-month period.
Price targets are determined by the fair value derived from a peer group comparison and/or our DCF model. Other fundamental factors (M&A activities, capital markets transactions, share buybacks, sector sentiment etc.) are taken into account as well.
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