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# Tarczyński – 2017 Q3 Earnings Conference Highlights

Rating: overweight (upgraded) | current price: PLN 11.00

## TAR PW; TAR.WA | Food Producers, Poland

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**Tarczyński revealed during the third-quarter earnings conference that, by taking a range of streamlining initiatives in the period, including the discontinuation of loss-making products, a greater focus on production efficiency, improved purchasing processes, and reduced costs of transportation, it has grown the average revenue per kilogram of meat product. The effects of these initiatives will continue to support sales revenues in the quarters ahead.**

**In spite of an expected increase in costs next year, driven by higher marketing expenses (likely to rise to PLN 7.0m from PLN 1.4m this year) and upward pressure on employee salaries, on our 2018E estimates, Tarczyński is currently trading at 7.8x P/E and 5.1x EV/EBITDA. With that in mind, even though the Company is not ready to declare dividends for 2018 (we assume 4.5% DYield at PLN 0.50 per share and 2.8x 2018E net debt/EBITDA), in anticipation of a strong rebound in the earnings results for Q4 2017, after revising our expectations for FY2017- 2018, we are upgrading TAR from neutral to overweight.**

- Tarczyński posted an 11.9% year-over-year increase in revenue in Q3 2017, driven by 8.8% expansion in revenue per kilogram owed to changes in the sales mix, specifically the discontinuation of unprofitable products. Moreover, at the beginning of the third quarter Tarczyński terminated relationships with customers who refused to accept revised pricing.
- Exports made further gains as a revenue driver in Q3, reaching 20% of total sales and accounting for 52% of the total sales growth, as well as generating higher profit margins than domestic sales.
- Aside from dropping loss-making products, Tarczyński undertook a number of other streamlining initiatives during Q3, including efforts to reduce transportation costs, negotiations with suppliers to extend payment terms and find areas for savings, and continued measures to improve the efficiency of production (automation, longer runs).
- Tarczyński observes that its chain customers have increased the frequency of 'limited-time-only' flash sales, which in one case already exceed the level of regular sales. Sales generated from such 'In & Out'-type campaigns are less predictable, but they allow suppliers like Tarczyński to use more flexible pricing and adjust prices during periods of increased cost volatility.
- Tarczyński ran virtually no advertising in the year through September, resulting in marginal ad expenses of PLN 0.3m in Q3, but in 2018 it is planning a big three-part marketing campaign.
- CAPEX next year will exceed D&A expenses at PLN 30+ million as the Company works to eliminate bottlenecks in storage and sorting, and as it invests in further growing export sales.
- Tarczyński says it will consider paying dividends in 2018 depending on resources remaining after all planned investment is covered without affecting the balance sheet.
- When it comes to the outlook for the fourth quarter of 2017, thanks to falling costs of fresh meat, coupled with the streamlining effects and low advertising expenses, on a revenue of PLN 189.6m (up 3.4% y/y), we expect Tarczyński to deliver EBITDA growth of 48% to a projected PLN 14.3m, and increase net profit by a staggering 855% to PLN 4.4m.

### Historical and projected trading multiples of Tarczyński

| | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017P | 2018P |
|---|---|---|---|---|---|---|---|---|
| **Price** | **11.00** | **11.00** | **11.00** | **11.00** | **11.00** | **11.00** | **11.00** | **11.00** |
| P/E | 21.5 | 6.5 | 13.4 | 10.7 | 6.2 | 12.7 | 6.8 | 7.8 |
| EV/EBITDA | 7.4 | 4.8 | 6.8 | 6.4 | 5.0 | 6.1 | 4.7 | 5.1 |
| DY | 0.0% | 6.5% | 1.0% | 0.0% | 0.0% | 5.9% | 5.9% | 4.5% |
| Net debt / EBITDA | 3.4 | 2.7 | 3.0 | 3.4 | 2.7 | 3.4 | 2.6 | 2.8 |
| P/B | 0.9 | 1.1 | 1.1 | 1.0 | 0.9 | 0.8 | 0.8 | 0.7 |

Source: Tarczyński, P - projections by Dom Maklerski mBanku mBank Dom Maklerski

## Historical financials and updated 2017-2018 projections

| (PLN m) | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017P | 2018P |
|---|---|---|---|---|---|---|---|---|
| **Revenue** | **378.8** | **386.7** | **448.4** | **494.4** | **542.0** | **648.2** | **734.0** | **770.0** |
| Y/Y change | | 2.1% | 15.9% | 10.3% | 9.6% | 19.6% | 13.3% | 4.9% |
| Gross profit | 67.2 | 77.2 | 85.9 | 105.8 | 121.2 | 123.6 | 139.0 | 143.1 |
| margin | 17.7% | 20.0% | 19.2% | 21.4% | 22.4% | 19.1% | 18.9% | 18.6% |
| Selling expenses | 48.1 | 45.3 | 56.4 | 63.9 | 79.1 | 85.5 | 88.3 | 95.5 |
| Administrative expenses | 11.2 | 11.5 | 14.3 | 17.8 | 14.9 | 18.3 | 22.1 | 22.8 |
| Other operating gains/losses | 1.8 | 0.9 | 2.1 | -2.5 | 5.2 | -0.1 | 1.8 | 1.8 |
| **EBIT** | **9.6** | **21.2** | **17.3** | **21.6** | **32.2** | **19.7** | **30.4** | **26.6** |
| margin | 2.5% | 5.5% | 3.9% | 4.4% | 5.9% | 3.0% | 4.1% | 3.5% |
| **EBITDA** | **20.8** | **33.3** | **32.9** | **41.8** | **54.7** | **45.5** | **59.0** | **55.4** |
| margin | 5.5% | 8.6% | 7.3% | 8.5% | 10.1% | 7.0% | 8.0% | 7.2% |
| Pre-tax income | 4.7 | 14.1 | 11.9 | 15.0 | 25.0 | 12.6 | 23.2 | 20.0 |
| **Net income** | **3.9** | **10.8** | **9.3** | **11.7** | **20.0** | **9.9** | **18.5** | **16.0** |
| margin | 1.0% | 2.8% | 2.1% | 2.4% | 3.7% | 1.5% | 2.5% | 2.1% |
| **Sales volume ('000 tonnes)** | 27.1 | 24.3 | 26.3 | 26.9 | 28.6 | 35.2 | 37.7 | 38.9 |
| Y/Y change | | -10.3% | 8.1% | 2.3% | 6.6% | 23.0% | 7.1% | 3.0% |
| **Avg. sales price (PLN/kg)** | **14.0** | **15.9** | **17.1** | **18.4** | **18.9** | **18.4** | **19.4** | **19.8** |
| Y/Y change | | 13.8% | 7.2% | 7.8% | 2.8% | -2.7% | 5.7% | 1.9% |
| **Margin (gross profit + D&A) per kilogram** | **2.9** | **3.7** | **3.9** | **4.7** | **5.0** | **4.2** | **4.4** | **4.4** |
| Advertising expenses (PLN m) | n/a | n/a | n/a | 6.3 | 9.7 | 6.5 | 1.4 | 7.0 |
| Shares outstanding (millions) | 7.6 | 6.3 | 11.3 | 11.3 | 11.3 | 11.3 | 11.3 | 11.3 |
| Capitalization (PLN m) | 83.1 | 69.8 | 124.8 | 124.8 | 124.8 | 124.8 | 124.8 | 124.8 |
| Net debt (PLN m) | 71.1 | 90.6 | 98.5 | 140.8 | 149.8 | 152.8 | 154.8 | 156.1 |
| BV (PLN m) | 91.3 | 65.1 | 115.4 | 127.1 | 146.4 | 148.9 | 160.0 | 170.3 |
| Dividends (PLN m) | - | 4.5 | 1.3 | 0.0 | 0.0 | 7.4 | 7.4 | 5.7 |

Source: Tarczyński, P - projections by Dom Maklerski mBanku

**List of abbreviations and ratios contained in the report:**
**EV** – net debt + market value
**EBIT** – Earnings Before Interest and Taxes
**EBITDA** – EBIT + Depreciation and Amortisation
**P/CE** – price to earnings with amortisation
**MC/S** – market capitalisation to sales
**EBIT/EV** – operating profit to economic value
**P/E** – (Price/Earnings) – price divided by annual net profit per share
**ROE** – (Return on Equity) – annual net profit divided by average equity
**P/BV** – (Price/Book Value) – price divided by book value per share
**Net debt** – credits + debt papers + interest bearing loans – cash and cash equivalents
**EBITDA margin** – EBITDA/Sales

**OVERWEIGHT (OW) –** a rating which indicates that we expect a stock to outperform the broad market
**NEUTRAL (N) –** a rating which indicates that we expect the stock to perform in line with the broad market
**UNDERWEIGHT (UW) –** a rating which indicates that we expect the stock to underperform the broad market

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| **Rating** | **Neutral** |
|---|---|
| Rating date | 2017-05-31 |
| Price on rating day | 11.20 |
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