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Orange Polska – Forecast of 2017 Q4 Results

Rating: buy | target price: PLN 7.30 | current price: PLN 6.10

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Ahead of the 2017 fourth-quarter earnings announcement, slated for February 20th, the following is a summary of our expectations as to Orange Polska's performance in the period. We anticipate worsened quarterly KPIs due to the new strategy focused on maximizing the value for each existing customer (after a period of aggressive acquisition using low pricing), a new pricing strategy (including the cancellation of the cheapest mobile plans), and customer switching from post-paid to pre-paid. On the plus side, Orange is expected to have curbed the downward trend in revenues in Q4 thanks to the success of 'Orange Love' bundles, coupled with a 19% reduction in selling expenses. As a result, we anticipate that the core EBITDA will show year-over-year growth of 2.9% for the first time in eleven quarters at an estimated PLN 659m. The reported EBITDA figure will be lower at PLN 479m after additional costs of severance benefits totaling PLN 180m, and the bottom line will probably show a net loss to the tune of PLN 188m, but this should be outweighed by the improvement in core earnings and the noticeable cost savings. We maintain our contrarian buy call for OPL despite the stock's >18% outperformance versus the WIG benchmark after the price gains logged in the last three months.

The Q4 2017 revenue of Orange Polska at an estimated PLN 2,861m will show y/y shrinkage of 4%. Revenues from mobile device sales are set to be lower than in the same period in 2016 (we assume a 7% drop vs. increases of 16.2% in Q2 and 13.1% in Q3) after a shift from discount pricing aimed at maximizing customer acquisition to an increased focus on monetization of the existing subscriber base, underpinned by high base effects. We expect the quarterly retail mobile revenue to come in at PLN 892m, with wholesale revenue at ca. PLN 308m. Fixed-line revenue is estimated at PLN 1,142m, showing the first flat year-over-year growth after a long period of falls. Reduced narrowband revenues will be offset by rising broadband revenues owed to the success of 'Orange Love.'

As for costs, we expect that in Q4 2017 Orange reduced payroll costs by 3.3% y/y to PLN 397m, and cut the costs of services by 6% to PLN 1,730m, and we anticipate a substantial, 19% drop in selling expenses.

We assume Orange will recognize a one-time gain of PLN 25m on a real estate sale in Q4.

All told, the adjusted Q4 2017 EBITDA at a projected PLN 659m is set to show year-over-year growth of 2.9%. The reported EBITDA before PLN 188m severance costs should approximate PLN 479m. After stable D&A expenses, net financing costs of PLN 68m, and a PLN 44m tax credit, the bottom line will show a net loss of PLN 188m.

Summary Q4 2017 earnings expectations

(PLN m)		Q4'16	Q1'17	Q2'17	Q3'17	Q4'17E	change
Revenue		2,981	2,818	2,839	2,814	2,861	-4.0%
	Mobile revenue	1,638	1,554	1,568	1,502	1,524	-7.0%
	Fixed revenue	1,162	1,134	1,135	1,153	1,142	-1.7%
	Other revenue	181	130	136	159	195	7.7%
EBIT		-1,848	109	169	128	-164	n/a
margin		-62.0%	3.9%	6.0%	4.5%	-5.7%	-
EBITDA		640	748	812	776	479	-25.2%
margin		21.5%	26.5%	28.6%	27.6%	16.7%	-
EBITDA (adjusted)		640	748	820	776	659	2.9%
margin		21.5%	26.5%	28.9%	27.6%	23.0%	-
	Net financing costs	-88	-71	-86	-88	-68	
	Tax	38	-7	-12	-12	44	
Net profit		-1,898	31	71	28	-188	n/a

Source: Orange Polska, E - estimates by Dom Maklerski mBanku

List of abbreviations and ratios contained in the report.
EV – net debt + market value (EV – economic value)
EBIT – Earnings Before Interest and Taxes
EBITDA – EBIT + Depreciation and Amortisation
PBA – Profit on Banking Activity
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

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UNDERWEIGHT (UW) – a rating which indicates that we expect the stock to underperform the broad market

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