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Construction & Real Estate: August 2018

Construction & Property Developers, Poland

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Construction

- Not much cause for optimism in the industry as **costs continue to rise**, with prices of asphalt soaring 18% during Q2, while crude oil gained 9% and price of concrete moved up by a further 5%.
- In terms of **second-quarter earnings**, we have seen negative surprises so far from most of the rated builders, with Budimex reporting 40% shrinkage in net profit relative to the comparable year-ago period, and net losses registered by Erbud (PLN 34m), Polimex-Mostostal (PLN 20m), and Torpol (PLN 2m). ZUE ended the quarter PLN 3m in the black, but this is a result well below its potential.
- Aside from cost overruns in existing projects, **road builders** at the moment are struggling with a dearth of new orders, with no major project put up for tender since mid-June. At the same time, **railway builders** are finding that their bids on recent assignments run on average 50% over budget, resulting in the cancellation of over PLN 2.5bn-worth of potential bookings. Consequently, the backlogs of ZUE, Trakcja, and Torpol feature very few jobs with potential to turn a profit.
- Against this backdrop, the only two companies still with positive investment calls from us are the residential builders **Unibep and Erbud**. Erbud's preliminary 2018 Q2 earnings proved worse than anticipated by us and by other analysts, who are currently discounting a sustained drop in the Company's future margins by about 50% relative to the historical 15-year average. We think this is an overly pessimistic take, with residential builders poised for a rebound next year after this year's slowdown, while infrastructure firms still have the most ahead of them.
- TOP PICKS:**
OVERWEIGHT ERB & UNI; **UNDERWEIGHT** TRK

Property Developers

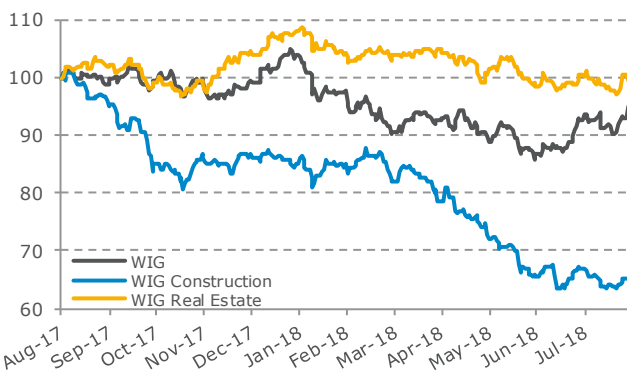
- Residential developers** for the most part reported **2018 Q2 results** in line with expectations, registering slightly softer margins on fast-growing sales. The aggregate net profit of DOM, I2D, LKD, and RON was 89% higher in the period than in the same period last year. Of the releases still to come, we think **LCC** and **1AT** might surprise on the upside.
- After a 15% drop in share price in the course of the past month (-26% ytd), **Atal** is currently trading at 6.2x 2018E P/E, and 1.4 P/B, offering 2019E dividend yield of 15.7%. At these levels, which can be considered attractive for a market leader and potential industry consolidator, 1AT is trading at a 20% discount to rival DOM
- The commercial developer **Echo Investment** has pulled over PLN 500m so far after selling its third office building this year in August, raising expectations for a special dividend which over the next nine months could come up to a combined total of PLN 1.1 per share.
- In the **Archicom vs. Lokum Developer trading pair** of Wrocław-based homebuilders, the former is currently trading at a nearly-30% discount to the latter's price-to-book ratio while offering about 35% more by way of 2019E dividend yield
- Polnord** shares have been on an upward trajectory for the last two weeks for which we can find no good explanation.
- TOP PICKS:**
OVERWEIGHT LCC, ARH, 1AT, LKD, ECH & DOM; **UNDERWEIGHT** PND

MoM* and YTD Price Change

Construction	MoM	YTD
Herkules	+9.4%	+4%
Ulma	+0.7%	+9%
Elbudowa	-3.7%	-28%
ZUE	-3.8%	-2%
Torpol	-5.2%	-35%
Unibep	-5.5%	-47%
Budimex	-6.5%	-39%
Elektrotim	-11.1%	-41%
Trakcja	-13.5%	-50%
Erbud	-36.3%	-51%
WIG Con.	-2.9%	-2.4%
WIG	+1.8%	-4%
Developers	MoM	YTD
Polnord	+9.4%	+3%
Lokum Dew.	+8.7%	+12%
Dom Dev.	+2.2%	-5%
BBi Dev.	+1.8%	-13%
Echo Inv.	+1.6%	+9%
LC Corp	-0.4%	-7%
GTC	-1.1%	-3%
P.A. Nova	-1.4%	-21%
JWC	-3.9%	-23%
i2 Dev.	-7.2%	+20%
Capital Park	-8.5%	-15%
Archicom	-11.6%	-13%
Ronson	-11.6%	-20%
Atal	-14.9%	-26%
WIG Real Est.	-0.7%	-4%
WIG	+1.8%	-4%
Foreign Indices	MoM	YTD
DE Real Est.	+5.4%	+14%
DAX	-2.1%	-3%
AT Real Est.	+1.5%	+8%
ATX	-2.1%	-3%
EU Real Est.	+0.4%	+1%
EU Con.	-2.0%	-2%
EU Equity	-1.4%	-4%

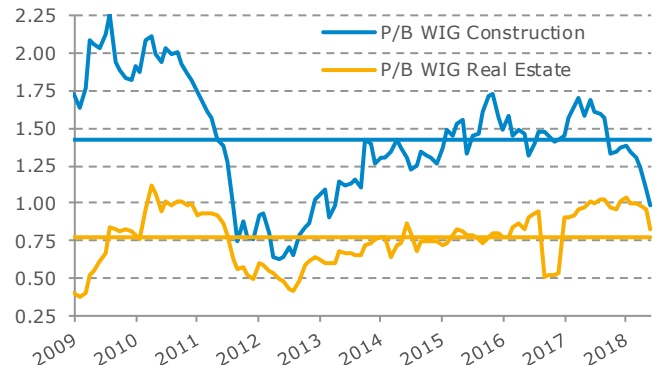
*Jul. 30 - Aug. 28

WIG Construction and WIG Real Estate vs. WIG



Source: Bloomberg

P/B ratios for WIG Construction and WIG Real Estate



EV – net debt + market value (EV – economic value)
EBIT – Earnings Before Interest and Taxes
EBITDA – EBIT + Depreciation and Amortisation
EBIT/EV – operating profit to economic value
EBITDA/EV – EBIT + Depreciation and Amortisation to economic value
P/E – (Price/Earnings) – price divided by annual net profit per share
P/BV – (Price/Book Value) – price divided by book value per share
Net debt – credits + debt papers + interest bearing loans – cash and cash equivalents
MCap – current market capitalization
Monthly price change (MoM price change) – change in the price of a stock since the date of the previous publication or in the course of the past month

ATX – Austrian Traded Index of all companies listed in Austria
DAX – German Stock Index of 30 selected blue chip stocks traded on the Frankfurt Stock Exchange
EPRA Index – FTSE EPRA Global Real Estate Index
FD06 Index (EU Equity) – FTSE Developed Europe Index
GDBR10 Index – German Generic Government Bonds 10 Year Yield

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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HOLD – we expect that the rate of return from an investment will range from -5% to +5%
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DCF – acknowledged as the most methodologically correct method of valuation; it consists in discounting financial flows generated by a company; its weak point is the significant susceptibility to a change of forecast assumptions in the model.

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Economic profits – discounting of future economic profits; the weak point is high sensitivity to changes in the assumptions made in the valuation model.

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NAV – valuation based on equity value, one of the most frequently used method in case of developing companies; the weak point of the method is that it does not factor in future changes in revenue/profits of a company.

mBank issued the following investment recommendations for the companies discussed in this publication in the 12 months prior to this publication

Archicom

Rating	overweight	overweight	overweight
Rating date	2018-06-22	2018-04-26	2018-01-25
Target price (PLN)	-	-	-
Price on rating day	15.00	15.30	15.75

Atal

Rating	buy	accumulate	accumulate	accumulate	accumulate
Rating date	2018-07-04	2018-06-22	2018-04-06	2018-02-02	2017-09-01
Target price (PLN)	42.86	42.86	47.00	49.20	45.00
Price on rating day	36.40	37.30	43.40	42.40	40.40

BBI Development

Rating	neutral	neutral
Rating date	2018-04-26	2018-02-02
Target price (PLN)	-	-
Price on rating day	0.66	0.70

Budimex

Rating	hold	hold	accumulate	buy
Rating date	2018-08-02	2018-06-06	2018-04-06	2018-02-02
Target price (PLN)	125.00	163.00	216.39	246.00
Price on rating day	122.60	153.00	215.00	197.80

Capital Park

Rating	buy	buy
Rating date	2018-04-06	2018-02-02
Target price (PLN)	8.35	8.42
Price on rating day	5.95	5.95

Dom Development

Rating	buy	accumulate	buy	buy	buy
Rating date	2018-08-02	2018-06-22	2018-03-20	2018-02-02	2017-09-01
Target price (PLN)	87.80	87.80	103.10	103.00	101.10
Price on rating day	72.80	85.80	85.80	82.00	82.25

Echo

Rating	buy	buy	buy	buy
Rating date	2018-04-06	2018-02-02	2017-10-02	2017-09-01
Target price (PLN)	5.63	6.31	6.42	6.64
Price on rating day	5.23	5.05	5.19	5.21

Elektrobudowa

Rating	hold	buy	buy	buy
Rating date	2018-06-06	2018-04-06	2018-02-02	2017-09-01
Target price (PLN)	71.00	116.00	113.00	134.00
Price on rating day	69.00	96.40	81.20	109.50

Elektrotim

Rating	neutral	overweight	underweight	neutral
Rating date	2018-05-28	2017-11-16	2017-10-24	2017-09-14
Target price (PLN)	-	-	-	-
Price on rating day	5.80	7.61	9.76	11.98

Erbud

Rating	buy	accumulate	buy	buy	buy	buy	buy
Rating date	2018-06-06	2018-05-09	2018-04-06	2018-03-05	2017-12-15	2017-11-03	2017-09-01
Target price (PLN)	22.00	23.10	29.60	29.40	28.70	29.80	31.30
Price on rating day	14.90	19.40	21.60	21.30	20.60	24.70	26.00

GTC

Rating	hold	accumulate	hold	hold	hold
Rating date	2018-04-06	2018-03-05	2018-02-02	2018-01-05	2017-08-02
Target price (PLN)	9.60	9.70	9.70	10.00	9.59
Price on rating day	9.39	8.64	9.67	9.90	9.62

Herkules

Rating	neutral	neutral
Rating date	2018-01-25	2017-10-24
Target price (PLN)	-	-
Price on rating day	3.67	3.60

i2 Development

Rating	neutral	neutral	overweight
Rating date	2018-06-22	2018-05-28	2018-01-12
Target price (PLN)	-	-	-
Price on rating day	15.40	17.30	14.90

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JWC

Rating	neutral	underweight	neutral
Rating date	2018-06-22	2018-03-29	2018-01-25
Target price (PLN)	-	-	-
Price on rating day	3.48	4.16	4.41

LC Corp

Rating	buy	buy	buy	buy
Rating date	2018-06-22	2018-04-06	2018-02-02	2017-09-26
Target price (PLN)	3.58	3.50	3.74	3.54
Price on rating day	2.39	2.70	3.10	2.69

Lokum Deweloper

Rating	overweight	overweight	overweight	overweight
Rating date	2018-06-22	2018-03-29	2018-01-25	2017-09-14
Target price (PLN)	-	-	-	-
Price on rating day	18.80	17.80	18.00	16.30

PA Nova

Rating	neutral	neutral	neutral
Rating date	2018-03-29	2018-02-28	2017-11-27
Target price (PLN)	-	-	-
Price on rating day	22.30	23.30	24.00

Polnord

Rating	underweight	neutral	neutral
Rating date	2018-06-22	2018-02-02	2017-12-27
Target price (PLN)	-	-	-
Price on rating day	9.04	10.50	8.70

Ronson

Rating	neutral	neutral	underweight	underweight
Rating date	2018-06-22	2018-04-03	2018-03-29	2018-02-02
Target price (PLN)	-	-	-	-
Price on rating day	1.09	1.32	1.32	1.45

Torpol

Rating	neutral	neutral	neutral	neutral	neutral	neutral	overweight
Rating date	2018-05-28	2018-03-29	2018-02-02	2018-01-25	2017-11-27	2017-10-24	2017-09-14
Target price (PLN)	-	-	-	-	-	-	-
Price on rating day	6.40	7.50	7.98	8.16	8.55	10.93	12.05

Trakcja

Rating	underweight	neutral	neutral	neutral	underweight	underweight	neutral
Rating date	2018-05-18	2018-03-29	2018-02-02	2018-01-25	2017-11-27	2017-10-24	2017-09-14
Target price (PLN)	-	-	-	-	-	-	-
Price on rating day	3.65	6.75	7.24	7.56	7.69	10.30	12.80

Ulma

Rating	neutral	neutral	neutral
Rating date	2018-05-28	2018-03-29	2017-11-27
Target price (PLN)	-	-	-
Price on rating day	73.00	66.50	73.90

Unibep

Rating	buy	buy	accumulate	buy	buy
Rating date	2018-04-06	2018-02-02	2018-01-05	2017-11-03	2017-09-01
Target price (PLN)	10.10	10.80	10.80	14.00	15.40
Price on rating day	7.50	8.60	9.76	9.90	12.20

ZUE

Rating	neutral	neutral	neutral	neutral	underweight	underweight
Rating date	2018-05-28	2018-03-29	2018-02-02	2018-01-25	2017-11-27	2017-09-14
Target price (PLN)	-	-	-	-	-	-
Price on rating day	5.86	6.12	6.18	6.44	6.89	9.20

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