

Wednesday, October 31, 2018 | periodic publication

Industrials Update for October 2018

Industrials, Poland

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Industrials

- Industrial stocks** covered by MSCI World and Europe indices are **trading lower** on **weak third-quarter earnings**, with Atlas Copco, Daimler, Goodyear, VW, Valeo, and VoestAlpine, among others, issuing **profit warnings** in recent weeks. Automakers blame the weaker profits on **softer car sales** in China and Europe, where new car registrations dropped after the entry into force of the Euro 6 emissions standard. More broadly, the negative industrial sector sentiment reflects concerns over the fallout of the **US-China trade war**. The **auto sector**, as tracked by MSCI Auto/Components, has been the **weakest performer** in the past month.
- In Poland**, the 2018 **Q3 earnings season** in the industrial sector is set to be a continuation of the pickup started in Q2, with 65% of rated industrial companies expected to report improvement from the year-ago period. The ones most likely to deliver **positive surprises** are **Amica, Cognor, Famur, Kernel, and Pozbud**.
- The sustained **rise in prices of electric power** this year creates **cost pressures next year** for the most energy-intensive manufacturers, with the companies facing the biggest **setbacks against 2019 EBITDA** (in descending order from worst to less bad) identified as Cognor, PKP Cargo, Pfeiderer, Mangata, Forte, Tarczyński, Stelmet, KGHM, JSW, Boryszew, and Grupa Kęty. On top of expensive feedstock, Polish manufacturers are also facing the third straight year of **rising pay pressures** in 2019, with labor costs likely to grow by a further 5%. Looking at **disappointing Manufacturing PMI** data lately, the **2019 earnings outlook for European industrial companies looks bleak**.
- Short term, we have the following three **top picks for November**:
 - Amica (AMC)** reversed a downward trend in core profits in Q2 2018, but nevertheless it continues to trade at double-digit discounts to comparable appliance makers as well as being valued 20%-30% below its own historical P/E and EV/EBITDA ratios (see chart on p. 9).
 - Famur (FMF)** is set for further stronger-than-priced earnings growth in the quarters ahead, and at the current share price its 2019 dividend yield would come close to 8%.
 - Kernel (KER)** broke the downward trend in Q2 2018, embarking on a sustained upward momentum set to last through 2019.
- Pozbud (POZ)** remains the **top pick among smaller caps**.
- We have a **bearish call** on **Grupa Kęty (KTY)**, whose 2019 earnings outlook is squeezed by higher costs and intensified competition, and which more likely than not will have to cut dividends in the next two years. As of today we also **downgrade Forte (FTE)** from overweight to neutral after abysmal Q3 preliminaries which forced us to cut our FY2018 EBITDA forecast by 17% and slash the net profit target by 57%. To boot, Forte's **net debt/EBITDA** ratio probably jumped to **6.0x** as of September.
- TOP PICKS – OVERWEIGHT: AMC, FMF, KER, POZ; UNDERWEIGHT: KTY**

Chemicals

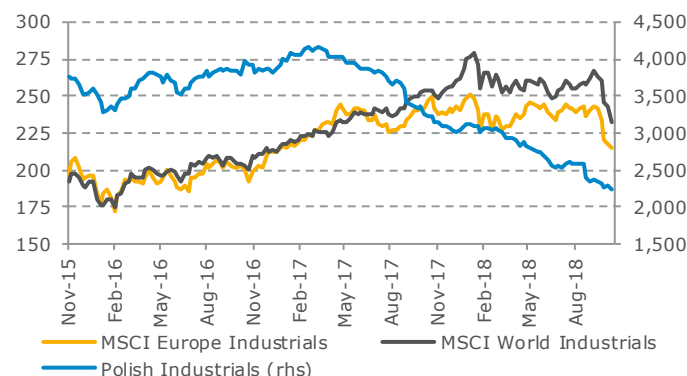
- Chemical companies have **underperformed** over the past month on **rising energy costs** and fears over the impact of the **US-China trade war** on future sales.
- November might bring a **positive shift in sentiment** for **Ciech (CIE)** and **Grupa Azoty (ATT)**, in the former case triggered by a **more positive 2019 price outlook** for its core product, soda ash, coming out of a recent world industry conference in China, and in the latter case spurred by a **downward shift in the prices of natural gas and carbon allowances**, accompanied by recovering prices of urea.

MoM* and YTD Price Change

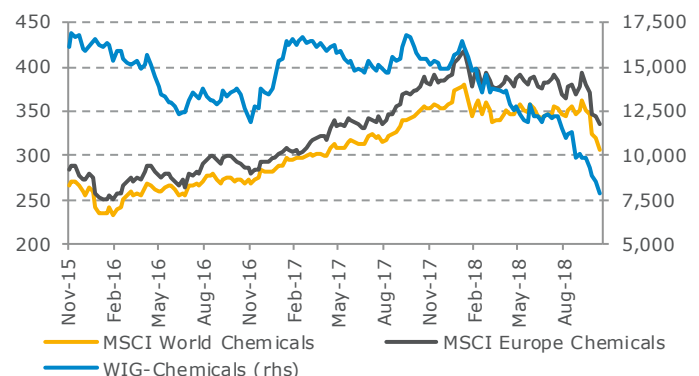
Industrials	MoM	YTD
Berling	+17.2%	+9%
TOYA	+13.3%	-21%
Patentus	+11.2%	-3%
Ropczyce	+10.4%	+34%
Cognor	+10.0%	+42%
Stalexport	+7.2%	-15%
Tarczyński	+6.0%	+30%
Mangata	+5.8%	-24%
Decora	+5.8%	+18%
Protektor	+5.6%	+27%
Groclin	+5.0%	-43%
Orzeł Biały	+4.2%	-11%
Kęty	-11.6%	-16%
Feerum	-12.5%	-60%
Izostal	-15.9%	-32%
Impexmet.	-16.0%	-27%
Pfeiderer	-18.1%	-13%
Global Cos.	-18.8%	-67%
Stalprofil	-19.6%	-37%
Selena FM	-21.3%	-45%
PGO dlew.	-23.4%	-43%
Bumeh	-28.6%	-19%
Ursus	-39.5%	-71%
Forte	-40.5%	-49%
Chemicals	MoM	YTD
Polwax	+3.9%	-37%
Mercator	+1.1%	-15%
PCC Rokita	-3.7%	-13%
Ciech	-11.4%	-16%
ZA Puławy	-17.0%	-49%
Police	-22.4%	-36%
Azoty	-23.4%	-65%
Krakchemia	-27.2%	-49%
WIGCHEM	-16.8%	-47%
WIG	-7.4%	-14%

*Sep. 29 - Oct. 30

Polish Industrials vs. MSCI Index



WIG-Chemicals vs. MSCI Index



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

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

Alumetal

Rating	neutral
Rating date	2018-08-23
Target price (PLN)	-
Price on rating day	51.00

Amica

Rating	overweight	overweight	overweight
Rating date	2018-09-13	2018-06-06	2018-01-05
Target price (PLN)	-	-	-
Price on rating day	112.80	121.00	130.00

Apator

Rating	neutral
Rating date	2018-02-28
Target price (PLN)	-
Price on rating day	24.00

Borysław

Rating	neutral	neutral
Rating date	2018-09-05	2017-11-30
Target price (PLN)	-	-
Price on rating day	6.25	9.85

Ciech

Rating	buy	buy	buy	buy	buy	buy	buy	buy
Rating date	2018-08-02	2018-07-04	2018-06-06	2018-05-09	2018-04-06	2018-03-05	2018-02-02	2017-10-02
Target price (PLN)	82.52	81.14	88.64	89.71	85.40	85.87	90.13	79.54
Price on rating day	56.95	53.05	60.20	55.00	57.00	55.90	61.25	65.16

Elemental

Rating	neutral
Rating date	2018-04-27
Target price (PLN)	-
Price on rating day	1.09

Ergis

Rating	neutral	neutral
Rating date	2018-04-27	2018-01-29
Target price (PLN)	-	-
Price on rating day	4.06	4.77

Famur

Rating	buy	buy	buy	buy	buy	buy
Rating date	2018-08-02	2018-05-09	2018-04-06	2018-03-05	2018-02-02	2018-01-05
Target price (PLN)	6.56	6.95	7.06	7.28	7.29	7.24
Price on rating day	5.20	5.94	6.04	6.10	6.20	6.18

Forte

Rating	neutral	overweight	neutral	neutral	neutral
Rating date	2018-10-31	2018-07-27	2018-04-27	2018-02-02	2018-01-29
Target price (PLN)	-	-	-	-	-
Price on rating day	40.60	40.60	50.70	43.00	49.10

Grupa Azoty

Rating	hold	hold	hold	hold	hold	hold	hold	hold	hold
Rating date	2018-09-03	2018-08-02	2018-05-25	2018-05-09	2018-03-05	2018-02-02	2018-01-05	2017-12-01	2017-10-02
Target price (PLN)	41.13	42.13	44.40	60.99	67.13	73.42	73.64	78.52	80.77
Price on rating day	38.00	42.20	42.60	51.10	56.55	72.00	74.40	71.30	79.80

Kernel

Rating	buy	hold	hold	hold	accumulate	accumulate
Rating date	2018-07-23	2018-05-09	2018-03-05	2018-02-02	2017-12-01	2017-11-03
Target price (PLN)	59.18	53.04	53.46	53.47	57.20	58.70
Price on rating day	50.50	50.80	48.80	50.90	47.51	48.25

Grupa Kęty

Rating	sell	hold	hold	hold	hold	hold	hold	hold	hold
Rating date	2018-10-29	2018-09-03	2018-08-02	2018-06-06	2018-05-09	2018-04-06	2018-03-05	2018-02-02	2018-01-05
Target price (PLN)	309.30	367.45	355.61	371.08	363.01	357.21	379.66	391.41	390.72
Price on rating day	365.50	387.50	321.50	360.50	353.00	346.00	352.50	385.00	408.00

Kruszwica

Rating	neutral	underweight
Rating date	2018-10-16	2018-08-02
Target price (PLN)	-	-
Price on rating day	43.90	65.40

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Mangata

Rating	neutral	underweight	neutral	underweight
Rating date	2018-10-01	2018-09-13	2018-06-22	2018-03-29
Target price (PLN)	-	-	-	-
Price on rating day	65.40	91.20	90.00	95.60

Pfleiderer Group

Rating	neutral	overweight	overweight	overweight
Rating date	2018-09-28	2018-08-08	2018-04-27	2017-11-08
Target price (PLN)	-	-	-	-
Price on rating day	36.45	37.30	37.30	36.65

Pozbud

Rating	overweight	overweight
Rating date	2018-09-04	2017-11-13
Target price (PLN)	-	-
Price on rating day	3.57	2.98

Stelmet

Rating	buy	buy	buy	buy	buy
Rating date	2018-09-03	2018-07-04	2018-05-09	2018-03-05	2018-02-02
Target price (PLN)	20.45	20.24	26.48	27.72	28.37
Price on rating day	11.35	10.70	14.75	17.15	19.20

Tarczyński

Rating	neutral	neutral	overweight
Rating date	2018-05-30	2018-01-29	2017-11-20
Target price (PLN)	-	-	-
Price on rating day	14.50	13.05	11.00

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