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VRG – 2020 Q1 Results Come Out Ahead of Forecasts

Rating: hold | target price: PLN 2.00 | current price: PLN 2.40

VRG PW; VRGP.WA | Retail, Poland

Analyst: Piotr Bogusz +48 22 438 24 08

- **VRG's 2020 first-quarter EBITDA exceeded market expectations, and it topped our estimate** which assumed higher SG&A expenses. The positive surprise acknowledged, note that the quarterly results showed substantial falls from the same period a year earlier, expected to be even greater in the second quarter.
- Total revenue in Q1 2020 was down 8% y/y at PLN 197.5m, with **contraction in revenues per square meter experienced across all clothing lines**.
- **Gross margin decreased by 1.4pp to 47.6%,** with the sales margin in the fashion segment reduced by 1.6pp, accompanied by a decline of 1.4pp in the jewelry segment.
- Total quarterly SG&A expenses showed a 1% y/y decline at PLN 105.8m, and **SG&A per square meter were down 5% on the year,** owing mainly to a 7% reduction in the costs of store operation.
- First-quarter EBIT showed an operating loss of PLN 11.9m – an increase from an EBIT loss of PLN 1.2m posted in Q1 2019. Of this, the loss generated by the fashion segment came in at PLN 12.8 vs. PLN 5.1m the year prior, while the jewelry segment was able to post an operating profit of PLN 0.7m, albeit lower than the year-ago EBIT of PLN 4m.
- **Operating cash flow** ex. IFRS 16 effects was negative at PLN -51.6m in Q1 2020, but it improved from PLN -71.2m a year ago after a slower rise in inventories and lower payments on financial obligations. Inventories as of 31 March 2020 were 9% higher per square meter than in March 2019 at PLN 10,188. Net debt ex. IFRS 16 effects stood at PLN 142.5m in March 2020 vs. PLN 126m the year prior. The net debt/EBITDA ratio was 1.4xas of 31 March.
- **In conclusion, VRG delivered a positive surprise with Q1 2020 results which, on the downside, were substantially worse than in Q1 2019. With stores on lockdown for the better part of the quarter, revenues in Q2 2020 most likely fell even more. On a positive note, we were impressed by VRG's tight cost management already in Q1. The OCF improvement through reduced working capital was consistent with the Company's plans. Going forward, VRG's prospects for the rest of the year depend on successful rent negotiations with property owners, and the rate of return in footfall now that stores have reopened. Overall, however, earnings in the quarters to come are likely to be weak.**

Overview of 2020 Q1 results

(PLN m)	1Q'20	1Q'19	change	1Q'20 (ex. IFRS 16)	1Q'20P (ex. IFRS 16)	differ.	Consensus (median)	differ.	2020E	2019	change
Revenue	197.5	214.4	-7.9%	197.5	196.5	0.5%	194.6	1.5%	740.0	1 068.3	-30.7%
EBITDA	17.4	24.6	-29.4%	-6.5	-11.9		8.7	100.0%	-15.2	111.1	
margin	8.8%	11.5%	-2.68p.p.	-3.3%	-6.1%		4.5%	4.3p.p.	-2.1%	10.4%	
EBIT	-11.9	-1.2	860.0%	-12.2	-17.6		-16.4		-37.0	87.5	
Pre-tax profit	-35.1	-4.0	784.3%	-17.2	-21.4				-60.4	79.4	
Net profit	-32.0	-2.4	1227.0%	-14.0	-20.3		-25.0		-61.6	64.0	

Source: VRG, E - mBank estimates; Consensus estimates provided by PAP;

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

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 S.A.
Senatorska 18
00-950 Warszawa
http://www.mbank.pl/

Research Department

Kamil Kliszcz
director
+48 22 438 24 02
kamil.kliszcz@mbank.pl
energy, power generation

Michał Marczak
+48 22 438 24 01
michal.marczak@mbank.pl
strategy

Michał Konarski
+48 22 438 24 05
michal.konarski@mbank.pl
banks, financials

Jakub Szkopek
+48 22 438 24 03
jakub.szkopek@mbank.pl
industrials, chemicals, metals

Paweł Szpigiel
+48 22 438 24 06
pawel.szpigiel@mbank.pl
media, IT, telco

Piotr Bogusz
+48 22 438 24 08
piotr.bogusz@mbank.pl
retail, gaming

Aleksandra Szklarczyk
+48 22 438 24 04
aleksandra.szklarczyk@mbank.pl
construction, real-estate development

Piotr Poniatowski
+48 22 438 24 09
piotr.poniatowski@mbank.pl
industrials

Mikołaj Lemańczyk
+48 22 438 24 07
mikolaj.lemanczyk@mbank.pl
financials

Sales and Trading

Traders

Piotr Gawron
director
+48 22 697 48 95
piotr.gawron@mbank.pl

Krzysztof Bodek
+48 22 697 48 89
krzysztof.bodek@mbank.pl

Tomasz Jakubiec
+48 22 697 47 31
tomasz.jakubiec@mbank.pl

Adam Prokop
+48 22 697 47 90
adam.prokop@mbank.pl

Magdalena Bernacik
+48 22 697 47 35
magdalena.bernacik@mbank.pl

Andrzej Sychowski
+48 22 697 48 46
andrzej.sychowski@mbank.pl

Sales, Foreign Markets

Bartosz Orzechowski
+48 22 697 48 47
bartosz.orzechowski@mbank.pl

Jędrzej Łukomski
+48 22 697 49 85
jedrzej.lukomski@mbank.pl

Private Client Sales

Kamil Szymański
director
+48 22 697 47 06
kamil.szymanski@mbank.pl

Jarosław Banasiak
deputy director
+48 22 697 48 70
jaroslaw.banasiak@mbank.pl