

Tuesday, January 14, 2014 | special comment

Cinema City to merge with Cineworld

Rating: hold | target price: PLN 33.50 | current price: PLN 35.00

CCI PW; CCI.WA | Media, Poland

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We view the merger of Cinema City's cinema operations with Cineworld as beneficial for CCI shareholders. We estimate the post-merger value of Cineworld at EUR 890 million, 24.9% of which will belong to CCI. Including cash, a near-40% stake in the property developer Ronson, and other real-estate holdings (mainly assets purchased in December 2012 and the seven cinemas which will be leased to Cineworld after the merger), Cinema City's post-merger equity value is roughly EUR 600 million, subject to a conservative 15% downward adjustment for a holding company discount reflecting our uncertainty as to the Company's plans with respect to the EUR 180m cash it will have at its disposal after the merger and after debt payments. We think the Company may use the bulk of the cash to fund the construction of the "Park of Poland," Poland's first major amusement park located near the town of Grodzisk Mazowiecki. CCI does not intend to disclose the details of the project until mid-2014. We believe a tentative valuation of PLN 41.50 per share accurately reflects the risks entailed in the project.

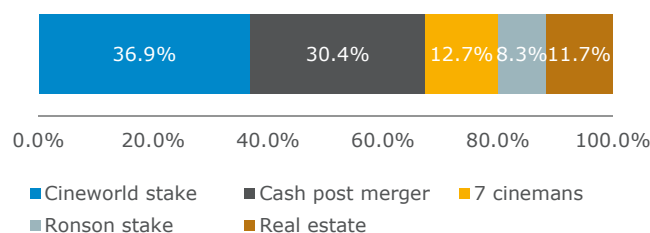
The merger

Cinema City agreed to sell its cinema business (valued at GBP 503 million) to the British cinema operator Cineworld in exchange for a cash price of GBP 272m, a 24.9% stake in the merged business, a cash payment of EUR 14.5m, and an earnings consideration of EUR 25.9m or EUR 28.9m depending on whether the deal is closed before the end of February or in or after March. After the merger, Cinema City will be the largest shareholder in Cineworld's dispersed ownership structure. Further, CCI's founding executives, CEO Mooky Greidinger and CFO Israel Greidinger, will serve as CEO and COO, respectively, of the merged Cineworld. Cinema City intends to use the merger proceeds to repay EUR 169m debt. CCI shareholders will vote on the merger on February 24th. The Company is retaining ownership of seven cinemas which it will lease to Cineworld.

Park of Poland

CCI has not shared much detail as regards the Park of Poland project, and it does not intend to until mid-2014. What is more, it has also postponed the announcement of its choice of strategic investor for the amusement park until mid-year instead of the end of 2013 as originally promised. From what we have been able to determine so far, the first stage of the project is expected to cost EUR 100m (including the EUR 20m Cinema City already paid for the land). CCI is in the process of negotiating partnership terms with a strategic investor (apparently a large amusement park operator with a presence in Europe) who will play a key role in mitigating the huge risks involved in such a project. We think it is likely Cinema City will allocate a large portion of the merger proceeds (ca. EUR 180m) to the Park of Poland project, although we must add that its Management has been hinting at other investment plans as well.

Cinema City post merger



Source: Dom Maklerski mBanku

Valuation

We applied an NPV of zero to the Park of Poland project. Note that if the investment needs prove larger than expected Cinema City can use dividends from Cineworld and Ronson to increase financing. We did not apply a control premium to our valuation of CCI's stakes in Ronson and Cineworld.

(EUR m)	Cineworld pre deal (2013)	Cinema City's cinema	Cineworld post deal
Revenue	488.3	269.4	757.7
EBITDA	88.9	63.3	152.2
Net debt	145.9		390.1
Net debt/EBITDA	1.6x		2.6x
Median peer 2013 EV/EBITDA			8.4x
Equity value based on 2013 EV/EBITDA'13			889.4

Source: Dom Maklerski mBanku, Bloomberg (iCineworld data and multiples)

Tentative valuation of Cineworld post merger

(EUR m)	Value	Assumption
Cineworld stake	221.4	24.9% stake in estimated Cineworld equity
Cash post merger	182.4	GBP 272m + EUR 15.5m less Cinema City net debt
7 cinemas (incl. one in Rishon LeZion)	76.0	NOI = EUR 7.6m, market cap rate = 10%
Ronson stake	49.7	39.65% stake at market price
Real estate	70.0	
Incl. Park of Poland land property	20.0	Value as at December 2012 + land acquired in 2013
Incl. Mall of Rousse	35.0	NOI = EUR 3.5m, market cap rate = 10%
Incl. other	15.0	Other assets acquired in December 2012 at 50% discount
TOTAL		EUR 599.6m
Number of shares		51.2
Per-share valuation		EUR 11.7
Holding company discount (15%)		EUR 1.8
Discounted per-share evaluation		EUR 9.4
EURPLN		4.2
Zloty value per share		PLN 41.5

Source: 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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