18 November 2009

Update

BRE Bank Securities

Oil & Gas
Poland

PKN Orlen

Buy

PKNA.WA; PKN.PW

(Reiterated)

Current price	**PLN 31.97**
Target price	**PLN 38.20**
Market cap	PLN 13.674bn
Free float	PLN 9.204bn
Avg daily trading volume (3M)	PLN 86.39m

Shareholder Structure

State Treasury	27.52%
ING OFE	5.17%
Others	67.31%

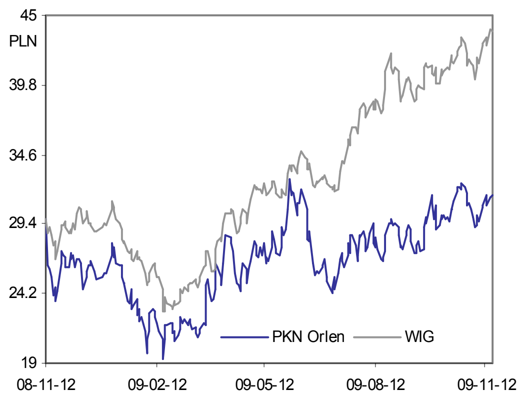
Sector Outlook

Refining fundamentals, and in particular margins and the Urals/Brent spread, have been unfavorable in recent months. However, the trends seem to be slowly shifting. If global fuel demand continues to increase, sentiment to refinery stocks will improve.

Company Profile

PKN Orlen is the largest refinery in the CEE region, with 14.1 million tons of annual capacity. In addition to crude refining, PKN Orlen is also active in the chemicals industry via its subsidiary Anwil, and in petrochemicals through BOP. In 2005, PKN Orlen took over the Czech "Unipetrol" group, followed by the acquisition of Lithuania's Mazeikiu Nafta in 2006.

PKN Orlen vs. WIG



Kamil Kliszcz
(48 22) 697 47 06
kamil.kliszcz@dibre.com.pl
www.dibre.com.pl

Diminished Risk of Covenant Breach

PKN Orlen has underperformed both the WIG20 index, and its peer refiners, in recent weeks, which is unlikely to be solely an effect of persistently low margins. We think that the real reason behind such poor performance is that investors are applying a discount to PKN shares as penalty for the risk of loan covenant breach at the end of the year. In our opinion, however, current exchange rates and the initiatives that PKN has undertaken this quarter to free working capital, rule out such the possibility of breach. Further, the process of disposal of the company's interests in Polkomtel and Anwil is advancing. Finally, PKN's performance going forward will be supported by an expected widening in the Urals/Brent spread. We are reiterating our price target and buy rating on PKN Orlen.

Q309 results: strong Retail, Petchem in the black

As predicted, PKN Orlen generated very strong profits from retail operations in Q3 2009, and moved the petrochemicals business into a positive territory after three quarters of losses. The Refinery business remained under pressure from narrow margins and Urals/Brent differentials, underpinned by downtime on HOG and HC units in Płock. However, after a PLN 307m boost from inventory valuation gains, the Q309 EBIT exceeded our estimated PLN 400m at PLN 423m. PKN generated higher-than-expected gains from exchange differences on translation of foreign-currency payables, which contributed to the quarter's impressive bottom-line profit of PLN 931m.

Urals/Brent spread expected to widen

The macroeconomic environment remains tough for refiners, and, even if demand for fuels improves, low capacity usage across the world is going to keep crack spreads low. However, there is a chance for a rebound in the Urals/Brent spread, fueled by increased petroleum production in OPEC countries (increased supply of heavy crude oil, improved price discount), and narrower crack spreads on HSFO (seasonally weaker demand for asphalt, competitive gas prices).

Breach of covenants an increasingly remote possibility

Concerns that PKN Orlen will once again fail to comply with loan covenants at year-end have been keeping its share price down. In our opinion, if EUR and USD exchange rates remain steady, the company is more than likely to reduce the ratio of net debt to EBITDA below the required level of 3.5. The main factor that will support compliance are high operating cash flows, generated by liberating cash from working capital and lowering FCY-loan valuations. We predict that net debt will reach PLN 12.6bn at 31 December, and, at an estimated EBITDA of PLN 3.7bn, the crucial ratio will stand at 3.4.

(PLN m)	**2007**	**2008**	**2009F**	**2010F**	**2011F**
Revenue	63793.0	79535.2	68342.1	80186.0	86149.2
EBITDA	5035.3	887.6	3745.3	4121.0	4709.0
EBITDA margin	*7.9%*	*1.1%*	*5.5%*	*5.1%*	*5.5%*
EBIT	2603.9	-1603.8	1163.9	1456.4	1839.2
Net income	2412.4	-2505.7	1326.5	1376.4	1370.7
DPS	0.00	1.62	0.00	0.00	0.64
P/E	5.7	-	10.3	9.9	10.0
P/CE	2.8	-953.6	3.5	3.4	3.2
P/BV	0.7	0.8	0.7	0.7	0.6
EV/EBITDA	5.0	32.6	7.7	7.3	6.4
DYield	0.0%	5.1%	0.0%	0.0%	2.0%

Q309 EBIT In Line

PKN Orlen's consolidated Q309 EBIT of PLN 423m was only slightly stronger than predicted because of lower-than-expected depreciation and amortization. The results generated by the different business segments were also in line with expectations. Refinery generated an EBIT of PLN 137m (we forecasted PLN 141m), with LIFO effect at PLN 307m (in line). The performance of the refining business would have been better if it had not been for downtime on HOG and HC units in Płock which cost the company about PLN 150-200m. The Retail segment reported very strong results for the third quarter (EBIT at PLN 363m vs. our estimated PLN 325m), thanks to an expansion in fuel margins (+PLN 108m) and non-fuel margins (+PLN 30m) which was partly offset by a PLN 55m surge in operating expenses (due among others to impairment of receivables). The Petrochemicals segment reported a positive EBIT figure of PLN 65m (we expected PLN 54m).

The consolidated finance gains for the third quarter totaled PLN 685m (we expected PLN 520m), and included the following items: gains from investments accounted for using the equity method (PLN 83m vs. PLN 93m forecasted), gains on foreign-currency loan translations (PLN 376m vs. PLN 342m forecasted), realized exchange differences on trade payables (PLN 350m vs. PLN 280m forecasted), and interest expenses (PLN 116m vs. PLN 160m forecasted). Thanks to these events, the Q3 2009 bottom-line profit came 20% ahead of expectations.

Consolidated third-quarter results

(PLN m)	Q3 2009	Q3 2008	change	Q3 2009F	Actuals vs. Forec.	Consens. Estimates	Actuals vs. Cons.	Q1-Q3 2009F	Q1-Q3 2008	change
Revenue	18 649	23 057	-19.1%	18 077.8	3.2%	18 440	1.1%	50 121.0	63 088.0	-20.6%
EBITDA	1 050	1 120	-6.3%	1 055.4	-0.5%	1 106	-5.1%	2 698.0	4 526.0	-40.4%
EBITDA margin	*5.6%*	*4.9%*	-	*5.84%*	-	*6.0%*	-	*5.4%*	*7.2%*	-
EBIT	423	512	-17.4%	399.4	5.9%	436	-3.0%	763.0	2 724.0	-72.0%
Pre-tax income	1 108	124	-	920.3	20.4%	-	-	1 172.0	3 053.0	-61.6%
Net income	931	21	-	747.4	24.6%	778	19.7%	1 006.0	2 388.0	-57.9%

Source: PKN Orlen, F-forecasts by BRE Bank Securities, consensus estimates by PAP

PKN Orlen reported negative operating cash flows in the amount of PLN 827m in Q309, mainly as a consequence of a PLN 2.2bn surge in working capital, in line with the company's earlier warning about expected court-ordered payouts (PLN 564m) and recognition of a PLN 0.5bn purchase toward the strategic fuel reserve made in Q209. This led to a PLN 1.3bn decrease in liabilities. Further, OCF was also affected by a nearly-PLN 850m increase in inventories which, the company explained, was a temporary buildup resulting from scheduled downtime at refineries. Negative OCF led to a surge in net debt to PLN 13.7bn, although the PLN 431m debt expansion was largely offset by downward revisions in foreign-currency loan payables (a PLN 376m reduction in euro debt, and a PLN 586m reduction in US dollar debt), combined with continued cuts in capital expenses which amounted to PLN 813m in Q309.

Consolidated quarterly results by business segment

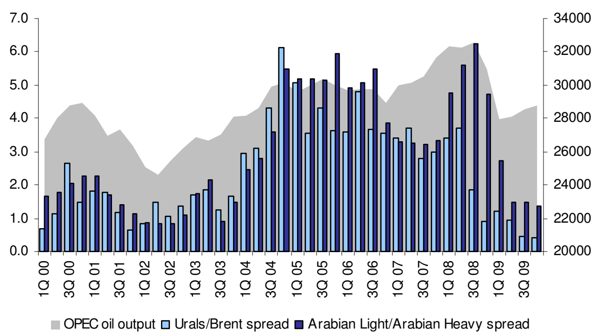
(PLN m)	Q108	Q208	Q308	Q408	Q109	Q209	Q309
Revenue	**17 938**	**22 090**	**23 057**	**16 449**	**14 702**	**16 770**	**18 649**
EBIT	**565**	**1 646**	**512**	**-1 965**	**-320**	**661**	**423**
refinery	330	1 407	184	-1 778	-116	770	137
LIFO	355	845	-316	-2 713	-246	928	307
retail	70	109	247	165	87	223	363
petrochemicals	278	35	104	-97	-162	-180	33
chemicals	0	73	87	33	90	8	-
other	0	74	29	33	0	0	-
unattributed	-113	-52	-139	-321	-219	-160	-142
EBIT (LIFO accounting)	**210**	**801**	**828**	**748**	**-74**	**-267**	**116**
Amortization & depreciation	587	607	608	690	651	656	627
EBITDA	**1 152**	**2 253**	**1 120**	**-1 275**	**331**	**1 317**	**1 050**
Finance gains/losses	225	402	-388	-1621	-951	674	685
Pre-tax income	790	2 048	124	-3 586	-1 271	1 335	1 108
Net income	**626**	**1 668**	**21**	**-3 047**	**-1 095**	**1 171**	**931**

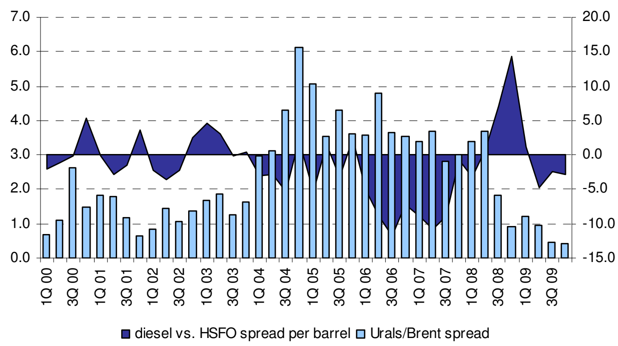
Source: PKN Orlen

Refinery

The refining industry is still suffering from a shrinkage in crack spreads observed since early 2009. US refiners continued to reduce capacity usage in the past few weeks, and European producers followed suit. In keeping with this trend, PKN Orlen cut capacity utilization at its refinery in Mazeikiai, Lithuania. That said, today's recovering economy offers hope for stronger fuel demand, and wider diesel cracks which were affected most severely by the global crisis. The turnaround will occur slowly given the wide gap between demand and capacity, and crack spreads are not likely to rebound within just one or two quarters. On a more positive note, the Urals/Brent spread, the other factor with major impact on PKN's earnings, could experience a rapid expansion fueled by the expected increase in OPEC's oil production (correlated with increasing oil prices). By making significant output cutbacks in H2 2008, OPEC restricted the supply of high-sulfur heavy oil grades like Urals relative to light crudes like Brent. Our expectations are supported by an increasing disparity as widening negative spreads on heavy residue (seasonally low demand for asphalts, increasingly competitive natural gas prices) cannot be offset by weak diesel crack spreads. We do not agree with the view that the shrinkage in the Urals/Brent spread is an effect of concerted efforts of Russian oil producers; monthly sales from Russia to western countries have been consistently on the rise. We have observed signs of a widening in the spread in recent weeks (from $0.3/Bbl to $0.7/Bbl since the beginning of October). An expansion at this rate is not going to do much for PKN's Q409 earnings, but its continuation will validate our predictions.

Light-Heavy crude price differentials vs. OPEC output and diesel/HSFO spread

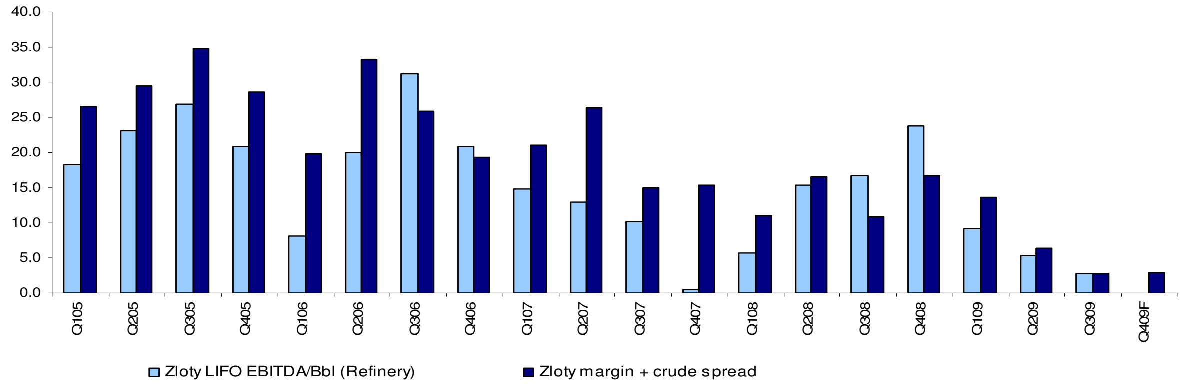


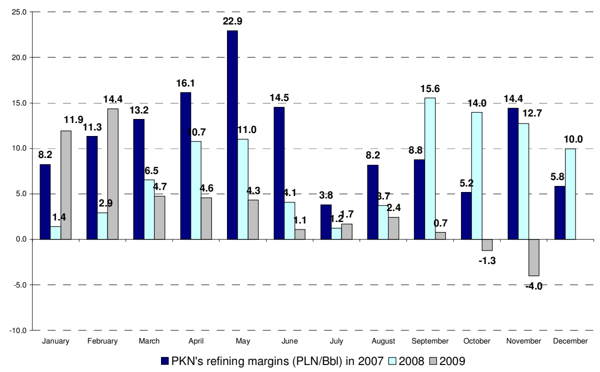


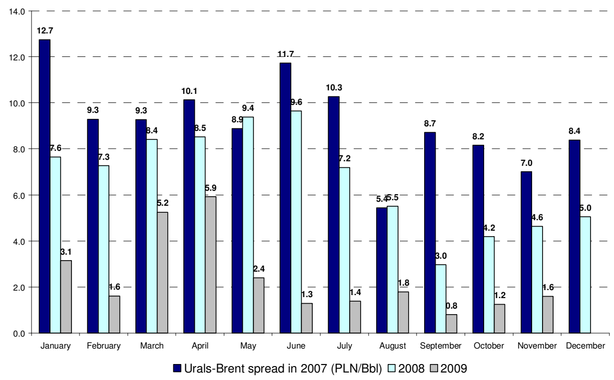
Source: Bloomberg, estimates by BRE Bank Securities

Macro conditions remained unfavorable for refiners during the first three quarters of 2009, as reflected (along with scheduled and unscheduled downtime) in the LIFO EBIT for the period (a PLN 79m loss vs. a PLN 1.2bn profit in the same period of 2008). Reported EBIT for the period ended 30 September 2009 amounted to PLN 0.79bn, but it was achieved mainly thanks to high inventory-revaluation gains (which approximated a combined PLN 1bn across all segments). In Q4 2009, like in past periods, Refinery's EBIT is going to be built chiefly by a positive LIFO effect (over PLN 300m). However, it is going to display a quarter-on-quarter improvement thanks to a lack of maintenance costs incurred in Q309 on HC and HOG units (PLN 150-200m). The 2010 operating profits of the refining business should be much better due to wider crude spreads, slightly better margins, and higher production volumes. The LIFO effect will continue to make positive, although smaller contributions (PLN 326m vs. PLN 1.34bn in 2009) according to our predictions concerning Brent prices and USD/PLN exchange rates.

Refinery earnings and the macroeconomic environment



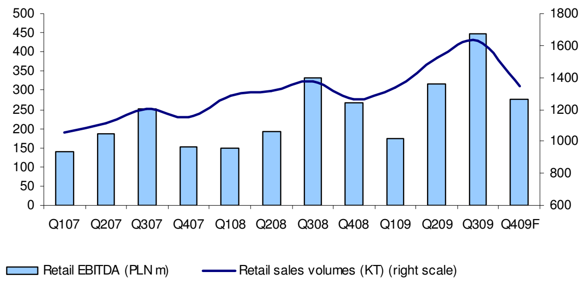


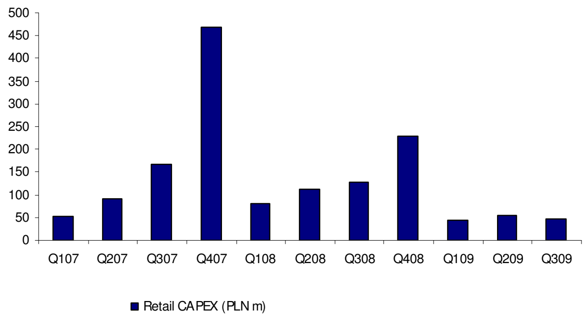


Source: Bloomberg, estimates by BRE Bank Securities

Amid tough macroeconomic conditions, PKN Orlen's service stations are the stabilizing agent for cash flows as well as reported EBIT. In H109, the Retail segment generated an EBIT of PLN 310m vs. PLN 192m a year earlier. The Q309 EBIT reached a record level at more than PLN 363m, driven by higher retail margins, higher volumes (+18% y/y), and higher non-fuel sales (led by an expanding "stop cafe" and "stop cafe bistro" chain). In Q4 2009, seasonal variations will pull the operating profit lower relative to Q209, but favorable weather conditions in October and November will push it higher relative to Q308. To account for this, we raised our full-year EBIT estimate for the Retail segment from PLN 753m to PLN 840m. The segment's financial performance will be further supported by the nearing completion of the service-station revamping program (as reflected in noticeably lower capital expenditure; for example, the company remodeled 78 stations in Q208, and only 14 in Q209).

Retail EBITDA vs. service station fuel sales



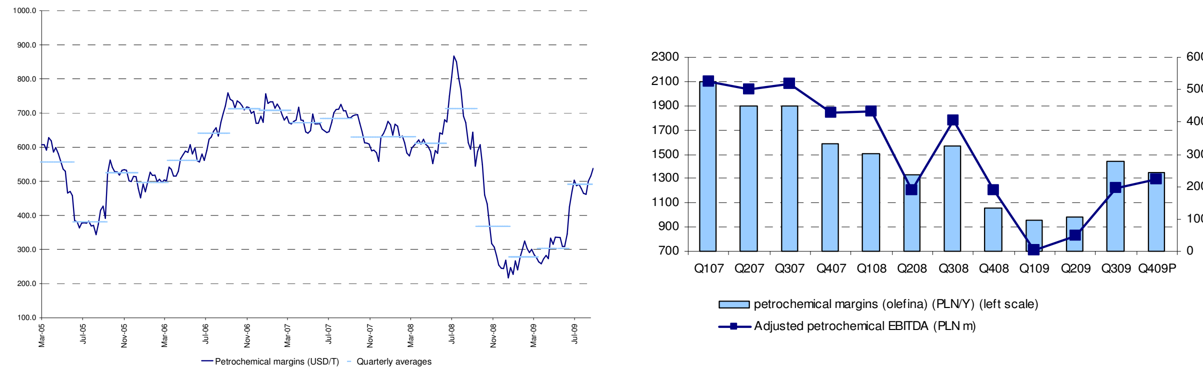


Source: PKN Orlen, BRE Bank Securities

Petrochemicals

Margins earned on petrochemicals, including olefins and polyolefins, have been expanding since July in spite of increasing costs of raw materials fueled by expensive crude. The expansion is an effect of recovering demand for plastics (owed among others to government aid granted to car manufacturers) on the one hand, and of a series of unscheduled plant outages (potential output: 2.5MMT) on the other hand. Unscheduled downtime, combined with earlier cutbacks in capacity usage, contributed to a rapid drop in supply of petrochemicals (in particular propylene, ethylene, and butadiene). Such a shift in demand was reflected in the Q309 EBITDA of PKN's Petchem business (PLN 195m vs. a PLN 13m loss in H109), which we expect to continue improving profitability in Q409. Assuming that market margins on petrochemicals remain steady in 2010, next year's EBIT generated by the segment could grow to PLN 148m from a negative PLN 258m this year.

Petrochemical margins vs. EBITDA generated by the Petchem segment

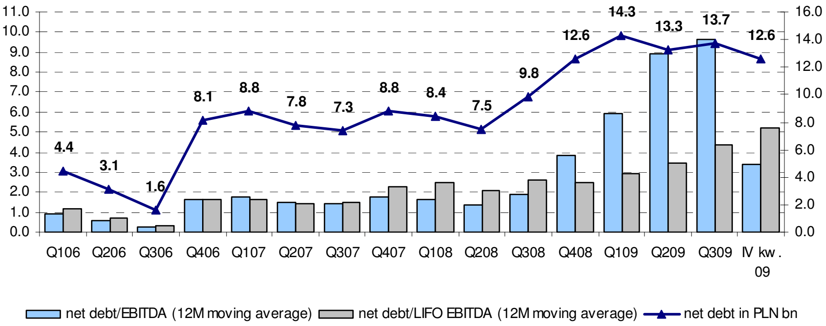


Source: Bloomberg, PKN Orlen, estimates by BRE Bank Securities

Loan Covenants at the End of 2009

Investors are still worried that Orlen will have to return to the negotiating table with its banks if at the end of 2009, when loan covenants are examined again, its net debt exceeds 3.5x EBITDA. According to our estimates, at the current USD/PLN and EUR/PLN exchange rates (2.75 and 4.10, respectively), the company should meet this requirement, in spite of the tough macroeconomic environment (our forecasted net debt/EBITDA ratio is 3.4). It will be aided by high cash flows from operating activities in Q4'09 (over PLN 1.6bn), stemming from a q/q decrease in working capital (increased factoring efforts to reduce outstanding receivables, longer terms of payment to suppliers, possibly operations on mandatory reserves). Along with another revaluation of F/X loans, this should facilitate a reduction in Orlen's net debt from PLN 13.7bn on 30 September to 12.6bn on 31 December. The security buffer is, however, small, and we cannot preclude the possibility than new appendices to loan agreements will be necessary. We believe that given the improvement in global financial markets, as well as the fact that it was possible to reach a mutually satisfactory agreement in April 2009, when the situation was much more difficult, another margin hike should not exceed 100bps. This should not, however, lead to a similar increase in interest expenses, as Orlen's net debt is expected to decrease next year (lower CAPEX, the divestment of Polkomtel and Anwil, perhaps the freeing of cash from mandatory reserves).

Net debt vs. EBITDA



Source: PKN Orlen, estimates by BRE Bank Securities

Divestment Plans (Update)

Among the planned disinvestments, the Management lists Orlen's 24.39% stake in Polkomtel, the mobile operator, and an 85% stake in Anwil, a chemicals manufacturing group. We estimate the after-tax value of these assets at PLN 3.4bn (PLN 8.0 per share) and PLN 1.4bn (PLN 3.2 per share), respectively. Orlen is also selling 12 fuel stations as well as storage facilities with asking price of nearly PLN 100m, and it is going to review its subsidiaries. It estimates the potential profits from divesting some of them at several hundred million zloty within the next three years. Potential candidates for divestment include transportation companies Orlen Transport and Orlen Koltrans, whose value we estimate at PLN 60-65m and PLN 50-55m, respectively. For now, however, it is difficult to say when this cash could be coming in.

Polkomtel

The Polkomtel divestment is proceeding on schedule. This month, investors should receive detailed information concerning the offer. As far as the timeline is concerned, an important aspect is still the agreement that binds the current shareholders, which gives 30-day preemptive rights to the non-divesting partners. For sure, PGE will not be wanting to execute this right (it has announced that it is going to sell its 21.85% stake), but it is hard to say what the other shareholders will do (KGHM 24.39%, Węglokoks 4.98% and Vodafone 24.39%). It seems, however, that only Vodafone might be interested, although recent news reports suggest this might not be the case. If there are no bidders for PKN's and PGE's stakes in open public tendering, stock exchange debut is a possibility – in fact, Polkomtel is already preparing for that option. Under this scenario, however, the whole process would be delayed; in addition, the other shareholders have to agree, which might be difficult to achieve.

Anwil

As far as Anwil is concerned, the due diligence stage has already begun, involving a handful of investors that expressed interest in PKN's offer (informational memoranda were sent to over 100 entities). The company is expecting to receive binding offers by the end of the year and to sit down to the negotiating table with the potential buyer in early 2010. Based on EV/EBITDA (2008/2010 sector median), we estimate the value of Orlen's 85% stake at PLN 1.7bn (PLN 1.4bn after-tax, standalone). At this stage, it is hard to say how likely this transaction is to be finalized. It needs to be stressed, however, that Anwil should be attractive to industry investors due to its integration with the refinery (petroleum supplies), which could be strengthened if capacity is expanded. Also, it should be remembered that this year's weaker earnings are mostly a consequence of the loss generated by the Czech Spolana, which could be left out of the transaction so that it does not weigh the price down.

Macroeconomic Assumptions

Macroeconomic assumptions for the DCF model

$/Bbl	2005	2006	2007	2008	2009F	2010F	2011F	2012F	2013F	2014F	2015F	2016F	2017F	2018F
Brent crude	54.5	65.4	72.8	98.0	61.1	75.0	80.0	90.0	90.0	90.0	90.0	90.0	90.0	90.0
Urals crude	50.4	61.2	69.5	95.1	60.3	73.2	78.0	87.6	87.7	87.7	87.7	87.8	87.8	87.8
Urals-Brent spread	4.1	4.2	3.3	2.9	0.8	1.8	2.0	2.4	2.3	2.3	2.3	2.2	2.2	2.2
PKN's margin	6.3	4.5	6.4	4.9	3.1	3.3	4.0	4.3	4.6	5.0	5.3	5.7	5.5	5.5
Mazeikiu Nafta's margin	5.4	2.1	3.6	2.7	2.6	2.6	4.7	4.9	5.2	5.4	5.7	5.9	6.2	6.2
Unipetrol's margin	8.5	5.9	7.3	9.7	4.8	5.5	5.6	5.8	5.9	6.1	6.2	6.4	6.5	6.5
Oil throughput (millions of tons)														
Orlen	12.8	13.7	14.0	14.2	14.6	15.0	15.7	15.7	15.7	15.7	15.7	15.7	15.7	15.7
Unipetrol	2.6	4.3	4.1	4.5	4.1	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7
Mazeikiu Nafta			5.0	9.2	8.7	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0	9.0
Petrochemical output ('000 of tons)	1923	3051	3059	2956	2577	3204	3375	3804	3575	3804	3575	3804	3575	3805
Chemical products output ('000 of tons)	1326	1804	1826	1759	1750	1778	1798	1878	1878	1878	1878	1878	1878	1878
Chemical & Petrochemical Lines														
Margin on chemicals (EUR/t)	500	535	568	619	551	528	538	565	565	557	557	557	557	557
Margin on petrochemicals ($/t)	498	559	660	566	396	451	465	511	511	497	497	497	497	497
Margin on HDPE+LDPE ($/t)	666	683	660	656	526	531	547	577	577	559	559	559	559	559
Margin on PP ($/t)	679	625	634	671	483	537	553	612	612	593	593	593	593	593
Margin on PTA ($/t)			896	1037	728	866	866	926	1045	926	866	866	926	926

Other macroeconomic assumptions	2005	2006	2007	2008	2009F	2010F	2011F	2012F	2013F	2014F	2015F	2016F	2017F	2018F
USD/PLN exchange rate	3.23	3.11	2.77	2.42	3.12	2.91	2.80	2.69	2.69	2.69	2.69	2.69	2.69	2.69
EUR/PLN exchange rate	4.02	3.90	3.78	3.48	4.30	3.85	3.80	3.70	3.50	3.50	3.50	3.50	3.50	3.50

Source: Bloomberg, PKN Orlen, Mazeikiu Nafta, forecasts by BRE Bank Securities

Earnings Forecast and Valuation

Our DCF model (which factors in PKN's interests in Polkomtel) produced a nine-month per-share target price of PLN 38.2.

DCF Analysis

Model Assumptions

1. Cash flows were discounted as of October 31, 2009. When determining equity value, we took into account net debt as of December 31, 2008, less the February installment of damages received by Mazeikiu Nafta ($63m), plus the price of the 10% stake in MN bought under a put option from the Lithuanian government ($290m). We are also taking into account contractual penalties awarded by the Court of Arbitration to Agrofert (PLN 460m paid in July plus PLN 164m reserve for additional costs stemming from the last claim, which is still being considered).
2. The macroeconomic assumptions are as forecasted above.
3. We added the investment in Polkomtel to equity value, including the shares bought at the end of 2008 (at cost of PLN 733m).
4. The amortization and depreciation expense projected for 2018 is higher than CAPEX, which is unsustainable over the long term, prompting us to revise the D&A expense to PLN 1.9 billion for terminal value calculation purposes.
5. When calculating FCF_{TV}, we based the terminal value calculations on the sales growth rate and EBITDA margins projected for 2018.
6. We assume that FCF after FY2018 will grow at a rate of 1%. Risk-free rate is 6.16%, and beta is 1.0.

DCF Valuation Model for PKN Orlen

(mln PLN)	2009F	2010F	2011F	2012F	2013F	2014F	2015F	2016F	2017	2018	2018+
Revenues	**68 342**	**80 186**	**86 149**	**96 956**	**98 954**	**100 116**	**100 269**	**101 762**	**101 893**	**103 197**	**103 197**
Change	*-14.1%*	*17.3%*	*7.4%*	*12.5%*	*2.1%*	*1.2%*	*0.2%*	*1.5%*	*0.1%*	*1,3%*	*0.0%*
EBITDA	**3 745.3**	**4 121.0**	**4 709.0**	**6 166.4**	**5 958.7**	**5 866.6**	**5 881.2**	**6 155.8**	**6 179.6**	**6 255,1**	**6 255.1**
EBITDA margin	*5.5%*	*5.1%*	*5.5%*	*6.4%*	*6.0%*	*5.9%*	*5.9%*	*6.0%*	*6.1%*	*6,1%*	*6.1%*
Amortization and depreciation	2 581.4	2 664.7	2 869.7	2 902.3	2 716.5	2 467.1	2 346.3	2 296.3	2 177.1	2 155,1	1 943.4
EBIT	**1 163.9**	**1 456.4**	**1 839.2**	**3 264.1**	**3 242.2**	**3 399.6**	**3 535.0**	**3 859.5**	**4 002.5**	**4 099,9**	**4 311.7**
EBIT margin	*1.7%*	*1.8%*	*2.1%*	*3.4%*	*3.3%*	*3.4%*	*3.5%*	*3.8%*	*3.9%*	*4,0%*	*4.2%*
Tax rate on EBIT	221.1	276.7	349.5	620.2	616.0	645.9	671.6	733.3	760.5	779,0	819.2
NOPLAT	**942.7**	**1 179.6**	**1 489.8**	**2 643.9**	**2 626.2**	**2 753.6**	**2 863.3**	**3 126.2**	**3 242.0**	**3 320,9**	**3 492.5**
CAPEX	-3 716	-3 887	-3 185	-2 609	-2 293	-1 943	-1 943	-1 943	-1 943	-1 943	-1 943
Working capital	735	-975	-883	-3 021	-812	-221	-103	-133	-3	-29	-3
Capital investments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0,0	0.0
FCF	**543**	**-1 018**	**292**	**-84**	**2 238**	**3 056**	**3 163**	**3 346**	**3 473**	**3 504**	**3 490**
WACC	*9.1%*	*9.0%*	*9.0%*	*9.1%*	*9.2%*	*9.2%*	*9.3%*	*9.3%*	*9.4%*	*9,4%*	*9.6%*
discount factor	*98.6%*	*90.4%*	*82.9%*	*76.0%*	*69.6%*	*63.8%*	*58.4%*	*53.4%*	*48.8%*	*44,6%*	*44.6%*
PV FCF	535	-920	242	-64	1 558	1 949	1 846	1 786	1 695	1 564	

	2009F	2010F	2011F	2012F	2013F	2014F	2015F	2016F	2017	2018	2018+
WACC	***9.1%***	***9.0%***	***9.0%***	***9.1%***	***9.2%***	***9.2%***	***9.3%***	***9.3%***	***9.4%***	***9,4%***	***9.6%***
Cost of debt	*7.2%*	*7.2%*	*7.2%*	*7.2%*	*7.2%*	*7.2%*	*7.2%*	*7.2%*	*7.2%*	*7,2%*	*7.2%*
Risk-free rate	*6.2%*	*6.2%*	*6.2%*	*6.2%*	*6.2%*	*6.2%*	*6.2%*	*6.2%*	*6.2%*	*6,2%*	*6.2%*
Risk premium	*1.0%*	*1.0%*	*1.0%*	*1.0%*	*1.0%*	*1.0%*	*1.0%*	*1.0%*	*1.0%*	*1,0%*	*1.0%*
Effective tax rate	*19.0%*	*19.0%*	*19.0%*	*19.0%*	*19.0%*	*19.0%*	*19.0%*	*19.0%*	*19.0%*	*19,0%*	*19.0%*
Net debt / EV	*39.3%*	*40.0%*	*39.7%*	*38.6%*	*37.2%*	*36.4%*	*35.6%*	*34.5%*	*33.7%*	*33,0%*	*30.0%*
Cost of Equity	*11.2%*	*11.2%*	*11.2%*	*11.2%*	*11.2%*	*11.2%*	*11.2%*	*11.2%*	*11.2%*	*11,2%*	*11.2%*
Risk premium	*5.0%*	*5.0%*	*5.0%*	*5.0%*	*5.0%*	*5.0%*	*5.0%*	*5.0%*	*5.0%*	*5,0%*	*5.0%*
Beta	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1,0	1.0

FCF growth after the forecast horizon	*1.0%*
Terminal value	40 805
Present value of the terminal value (PV TV)	18 211
Present value of FCF in the forecast horizon	10 192
Net debt	13 397
Minority interests	2 719
Allowance against Agrofert claim	-624
Equity value	11 663
Number of shares (millions)	427.7
Equity value per share (PLN)	**27.3**
Per-share value of interests in Polkomtel	**8.0**
Equity value per share (PLN)	**35.3**
Cost of equity (9M)	*8.4%*
Target Price	**38.2**
EV/EBITDA('09) for the target price	8.7
P/E('09) for the target price	12.3
TV to EV	56%

Sensitivity analysis

	FCF growth in perpetuity				
	0.0%	**1.0%**	**2.0%**	**3.0%**	**4.0%**
WACC +1.0ppt	29.5	33.4	38.2	44.3	52.3
WACC +0.5ppt	31.3	35.6	41.0	48.0	57,2
WACC	33.4	38.2	44.3	52,3	63.1
WACC -0.5ppt	35.6	41.0	48.0	57.2	70.1
WACC -1.0ppt	38.2	44.3	52.3	63.1	78,7

Relative valuation

		P/E				EV/EBITDA			
	Price	2008	2009F	2010F	2011F	2008	2009F	2010F	2011F
MOL	16190	8.5	18.7	10.2	8.8	6.8	7.7	5.9	5.1
OMV	30.3	4.7	11.7	7.3	6.2	3.3	5.0	3.9	3.4
Lotos	28.4	-8.1	5.1	9.4	4.8	41.0	10.0	11.7	5.4
Tupras	26.3	7.5	9.8	8.7	7.8	4.0	6.7	5.9	4.8
Hellenic	7.8	9.1	12.4	12.4	9.8	6.9	8.9	7.9	6.5
Unipetrol (CZK)	137.5	24.5	935.1	15.1	9.5	5.1	7.3	5.3	4.1
SNP Petrom	0.3	7.3	11.5	8.8	7.1	4.5	5.9	4.2	3.6
ERG	10.1	13.0	-26.6	21.8	14.1	4.1	21.6	6.2	5.1
Neste	11.9	6.8	21.2	16.9	9.6	5.4	10.2	8.4	5.9
Motor Oil	11.5	9.2	10.8	9.4	8.5	7.3	8.2	7.2	6.7
INA	1800.1	19.7	25.0	12.3	8.4	8.8	8.1	6.0	4.9
Maximum		24.5	935.1	21.8	14.1	41.0	21.6	11.7	6.7
Minimum		-8.1	-26.6	7.3	4.8	3.3	5.0	3.9	3.4
Median		**8.5**	**11.7**	**10.2**	**8.5**	**5.4**	**8.1**	**6.0**	**5.1**
PKN	32.0	-	10.3	9.9	10.0	22.7	5.4	4.9	4.3
(premium / discount)		-164.4%	-11.6%	-2.9%	17.0%	318.9%	-33.5%	-18.7%	-15.3%
Implied price									
Median		8.5	11.7	10.2	8.5	5.4	8.1	6.0	5.1
Multiple weight			50.0%				50.0%		
Year weight		0.0%	33.3%	33.3%	33.3%	0.0%	33.3%	33.3%	33.3%
Equity value per share (PLN)		**39.2**							

EV/EBITDA based on net debt at year-end 2009

Net debt adjusted for the value of the stake in Polkomtel and mandatory reserves (PLN 5.6bn)

Lotos's multiples were estimated based on net debt from 2007-2010.

Income Statement

(PLN m)	2006	2007	2008	2009F	2010F	2011F	2012F
Revenues	**52 867**	**63 793**	**79 535**	**68 342**	**80 186**	**86 149**	**96 956**
Change	*28.4%*	*20.7%*	*24.7%*	*-14.1%*	*17.3%*	*7.4%*	*12.5%*
EBIT	**2 576.6**	**2 603.9**	**-1 603.8**	**1 163.9**	**1 456.4**	**1 839.2**	**3 264.1**
Refinery	1 614.0	1 689.0	53.0	1 127.8	995.9	989.1	1 731.4
LIFO effect	32.0	1 167.0	-1 843.0	1 345.2	326.5	-102.7	473.9
Retail	439.0	423.0	625.0	857.3	840.1	867.7	914.7
Petrochemicals	842.0	1 068.0	144.0	-257.8	148.7	329.7	916.9
Chemicals	224.0	246.0	285.0	107.4	66.6	253.5	307.9
Other	8.0	-155.0	137.0	0.0	0.0	0.0	0.0
Unattributed costs	-550.4	-667.1	-2 977.8	-670.8	-594.9	-600.8	-606.8
EBIT (LIFO accounting)	**2 544.6**	**1 436.9**	**239.2**	**-181.3**	**1 129.9**	**1 941.9**	**2 790.2**
Profit on financing activity	-68.0	139.8	-1 578.6	118.0	-35.0	-433.9	-306.7
Extraordinary gains/losses	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	220.7	267.4	266.5	262.0	262.0	262.0	262.0
Pre-tax income	**2 729.3**	**3 011.1**	**-2 915.9**	**1 543.9**	**1 683.4**	**1 667.4**	**3 219.3**
Tax	669.1	530.6	-388.8	237.3	319.8	316.8	611.7
Minority interests	74.2	68.0	-21.4	-20.0	-12.9	-20.1	-9.5
Net income	**1 986.0**	**2 412.4**	**-2 505.7**	**1 326.5**	**1 376.4**	**1 370.7**	**2 617.1**
Change	*-56.6%*	*21.5%*	*-203.8%*	*-153.0%*	*3.8%*	*-0.4%*	*90.9%*
margin	*3.8%*	*3.8%*	*-3.2%*	*1.9%*	*1.7%*	*1.6%*	*2.7%*

Amortization and depreciation	2 108.1	2 431.4	2 491.4	2 581.4	2 664.7	2 869.7	2 902.3
EBITDA	**4 684.7**	**5 035.3**	**887.6**	**3 745.3**	**4 121.0**	**4 709.0**	**6 166.4**
Change	*-30.4%*	*7.5%*	*-82.4%*	*321.7%*	*10.0%*	*14.3%*	*30.9%*
EBITDA margin	*8.9%*	*7.9%*	*1.1%*	*5.5%*	*5.1%*	*5.5%*	*6.4%*
Shares at year-end (millions)	427.7	427.7	427.7	427.7	427.7	427.7	427.7
EPS	4.6	5.6	-5.9	3.1	3.2	3.2	6.1
CEPS	9.6	11.3	0.0	9.1	9.4	9.9	12.9
ROAE	*11.2%*	*12.4%*	*-13.3%*	*7.1%*	*6.9%*	*6.6%*	*11.7%*
ROAA	*5.0%*	*5.3%*	*-5.4%*	*2.8%*	*2.7%*	*2.5%*	*4.6%*

Balance Sheet

(PLN m)	2006	2007	2008	2009F	2010F	2011F	2012F
ASSETS	**45 419.1**	**46 103.3**	**46 975.8**	**49 480.2**	**53 799.1**	**55 290.1**	**57 432.4**
Fixed assets	**27 660.8**	**26 736.4**	**29 280.9**	**30 415.7**	**31 638.0**	**31 953.1**	**31 660.2**
Property, plant and equipment	25 199.7	24 833.5	26 268.8	27 421.0	28 642.3	28 972.0	28 701.1
Intangible assets	619.8	531.0	557.0	539.6	540.7	526.1	504.1
Equity interests	716.3	700.3	1 561.1	1 561.1	1 561.1	1 561.1	1 561.1
Other fixed assets	1 125.0	671.5	893.9	893.9	893.9	893.9	893.9
Current assets	**17 758.3**	**19 367.0**	**17 694.9**	**19 064.5**	**22 161.1**	**23 336.9**	**25 772.2**
Inventories	7 398.9	10 365.4	9 089.0	10 670.0	12 563.2	12 892.0	14 083.0
Short-term receivables	6 293.7	6 884.5	6 356.2	6 492.5	7 457.3	8 184.2	9 210.8
Other current assets	1 714.4	618.9	905.4	525.4	525.4	525.4	525.4
Cash and cash equivalents	2 351.3	1 498.2	1 344.2	1 376.6	1 615.2	1 735.3	1 953.0

(PLN m)	2006	2007	2008	2009F	2010F	2011F	2012F
LIABILITIES	**45 419.1**	**46 103.3**	**46 975.8**	**49 480.2**	**53 799.1**	**55 290.1**	**57 432.4**
Equity	**18 850.9**	**19 935.3**	**17 813.1**	**19 357.6**	**20 472.1**	**21 308.0**	**23 393.0**
Share capital	1 057.6	1 057.6	1 057.6	1 057.6	1 057.6	1 057.6	1 057.6
Other equity	17 793.3	18 877.6	16 755.5	18 300.0	19 414.4	20 250.4	22 335.4
Minority shares	**2 731.6**	**2 638.0**	**2 718.6**	**2 698.6**	**2 685.7**	**2 665.6**	**2 656.1**
Long-term liabilities	**8 958.1**	**11 091.4**	**4 634.2**	**13 632.4**	**14 744.4**	**15 163.0**	**15 887.9**
Loans	6 211.2	8 602.7	2 610.7	11 608.9	12 720.9	13 139.5	13 864.4
Other	2 747.0	2 488.7	2 023.5	2 023.5	2 023.5	2 023.5	2 023.5
Short-term liabilities	**14 878.4**	**12 438.7**	**21 809.9**	**13 791.6**	**15 897.0**	**16 153.4**	**15 495.4**
Loans	4 277.9	1 719.2	11 282.1	2 320.0	2 542.2	2 625.9	2 770.7
Trade creditors	8 221.4	9 181.2	8 414.1	10 866.4	12 749.6	12 922.4	12 119.5
Other	2 379.1	1 538.2	2 113.7	605.2	605.2	605.2	605.2
Debt	10 489.1	10 321.9	13 892.8	13 928.9	15 263.1	15 765.4	16 635.1
Net debt	8 137.8	8 823.7	12 548.5	12 552.3	13 648.0	14 030.1	14 682.1
(Net debt / Equity)	*43.2%*	*44.3%*	*70.4%*	*64.8%*	*66.7%*	*65.8%*	*62.8%*
(Net debt / EBITDA)	1.7	1.8	14.1	3.4	3.3	3.0	2.4
BVPS	44.1	46.6	41.6	45.3	47.9	49.8	54.7

Cash Flows

(PLN m)	2006	2007	2008	2009F	2010F	2011F	2012F
Cash flows from operating activities	**3 693.2**	**1 965.1**	**3 616.8**	**3 973.0**	**2 826.3**	**3 509.3**	**2 534.2**
Net income	2 060.2	2 480.4	-2 526.6	1 306.5	1 363.6	1 350.6	2 607.7
Amortization and depreciation	2 108.1	2 431.4	2 491.4	2 581.4	2 664.7	2 869.7	2 902.3
Working capital	-492.8	-2 830.4	1 358.2	735.0	-974.9	-882.9	-3 020.5
Other	17.6	-116.3	2293.8	-650.0	-227.0	171.9	44.7
Cash flows from investing activities	**-6 746.2**	**-2 845.1**	**-4 385.0**	**-4 574.8**	**-3 887.0**	**-3 184.9**	**-2 609.4**
CAPEX	-1 924.6	-3 693.7	-3 969.4	-3 716.3	-3 887.0	-3 184.9	-2 609.4
Equity investment	-5 836.5	-539.5	-736.9	-1 058.5	0.0	0.0	0.0
Other	1015.0	1388.2	321.3	200.0	0.0	0.0	0.0
Cash Flows	**4 277.6**	**27.0**	**612.6**	**634.2**	**1 299.2**	**-204.3**	**292.9**
Stock offering	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt	4 505.3	667.9	1 902.1	516.2	1 334.2	502.3	869.7
Dividend (buy-back)	0.0	0.0	-692.9	0.0	0.0	-272.7	-270.1
Other	-227.8	-640.9	-596.7	118.0	-35.0	-433.9	-306.7
Change in cash	**1 224.5**	**-853.1**	**-155.6**	**32.4**	**238.6**	**120.1**	**217.7**
Cash at end of period	2 351.3	1 498.2	1 344.2	1 376.6	1 615.2	1 735.3	1 953.0
DPS (PLN)	0.00	0.00	1.62	0.00	0.00	0.64	0.63
FCF	-4 238.3	-2 559.0	-2 071.7	-531.8	-1 060.7	324.4	-75.2
(CAPEX / Sales)	*3.6%*	*5.8%*	*5.0%*	*5.4%*	*4.8%*	*3.7%*	*2.7%*

Market multiples

	2006	2007	2008	2009F	2010F	2011F	2012F
P/E	6.9	5.7	-	10.3	9.9	10.0	5.2
P/CE	3.3	2.8	-953.6	3.5	3.4	3.2	2.5
P/BV	0.7	0.7	0.8	0.7	0.7	0.6	0.6
P/S	0.3	0.2	0.2	0.2	0.2	0.2	0.1
FCF/EV	*-17.3%*	*-10.2%*	*-7.2%*	*-1.8%*	*-3.5%*	*1.1%*	*-0.2%*
EV/EBITDA	5.2	5.0	32.6	7.7	7.3	6.4	5.0
EV/EBIT	9.5	9.7	-18.0	24.9	20.6	16.5	9.5
EV/S	0.5	0.4	0.4	0.4	0.4	0.4	0.3
DYield	*0.0%*	*0.0%*	*5.1%*	*0.0%*	*0.0%*	*2.0%*	*2.0%*
Price (PLN)	**31.97**						
Shares at year-end (millions)	427.7	427.7	427.7	427.7	427.7	427.7	427.7
MC (PLN m)	13 674	13 674	13 674	13 674	13 674	13 674	13 674
Equity attributable to minority shareholders (mln PLN)	2 732	2 638	2 719	2 699	2 686	2 666	2 656
EV (PLN m)	24 543	25 136	28 941	28 925	30 007	30 370	31 012

Michał Marczak tel. (+48 22) 697 47 38
Managing Director
Head of Research
michal.marczak@dibre.com.pl
Strategy, Telco, Mining, Metals, Media

Research Department:

Marta Jeżewska tel. (+48 22) 697 47 37
Deputy Director
marta.jezewska@dibre.com.pl
Banks

Analysts:

Kamil Kliszcz tel. (+48 22) 697 47 06
kamil.kliszcz@dibre.com.pl
Fuels, Chemicals, Retail

Piotr Grzybowski tel. (+48 22) 697 47 17
piotr.grzybowski@dibre.com.pl
IT, Media

Maciej Stokłosa tel. (+48 22) 697 47 41
maciej.stoklosa@dibre.com.pl
Construction, Real-Estate Developers

Jakub Szkopek tel. (+48 22) 697 47 40
jakub.szkopek@dibre.com.pl
Manufacturers

Sales and Trading:

Piotr Dudziński tel. (+48 22) 697 48 22
Director
piotr.dudzinski@dibre.com.pl

Marzena Łempicka-Wilim tel. (+48 22) 697 48 95
Deputy Director
marzena.lempicka@dibre.com.pl

Traders:

Emil Onyszczuk tel. (+48 22) 697 49 63
emil.onyszczuk@dibre.com.pl

Grzegorz Stępien tel. (+48 22) 697 48 62
grzegorz.stepien@dibre.com.pl

Tomasz Dudź tel. (+48 22) 697 49 68
tomasz.dudz@dibre.com.pl

Michał Jakubowski tel. (+48 22) 697 47 44
michal.jakubowski@dibre.com.pl

Tomasz Jakubiec tel. (+48 22) 697 47 31
tomasz.jakubiec@dibre.com.pl

Grzegorz Strublewski tel. (+48 22) 697 48 76
grzegorz.strublewski@dibre.com.pl

"Private Broker"

Jacek Szczepański tel. (+48 22) 697 48 26
Director
jacek.szczepanski@dibre.com.pl

Paweł Szczepanik tel. (+48 22) 697 49 47
Sales
pawel.szczepanik@dibre.com.pl

Dom Inwestycyjny
BRE Banku S.A.
ul. Wspólna 47/49
00-950 Warszawa
www.dibre.com.pl

List of abbreviations and ratios contained in the report:
EV *– net debt + market value*
EBIT *– Earnings Before Interest and Taxes*
EBITDA *– EBIT + Depreciation and Amortisation*
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*

Recommendations of BRE Bank Securities
A recommendation is valid for a period of 6-9 months, unless a subsequent recommendation is issued within this period. Expected returns from individual recommendations are as follows:
BUY – we expect that the rate of return from an investment will be at least 15%
ACCUMULATE – we expect that the rate of return from an investment will range from 5% to 15%
HOLD – we expect that the rate of return from an investment will range from –5% to +5%
REDUCE – we expect that the rate of return from an investment will range from -5% to -15%
SELL – we expect that an investment will bear a loss greater than 15%
Recommendations are updated at least once every nine months.

This document has been created and published by BRE Bank Securities S.A. The present report expresses the knowledge as well as opinions of the authors on day the report was prepared. The opinions and estimates contained herein constitute our best judgement at this date and time, and are subject to change without notice. The present report was prepared with due care and attention, observing principles of methodological correctness and objectivity, on the basis of sources available to the public, which BRE Bank Securities S.A. considers reliable, including information published by issuers, shares of which are subject to recommendations. However, BRE Bank Securities S.A., in no case, guarantees the accuracy and completeness of the report, in particular should sources on the basis of which the report was prepared prove to be inaccurate, incomplete or not fully consistent with the facts. BRE Bank Securities S.A. bears no responsibility for investment decisions taken on the basis of the present report or for any damages incurred as a result of investment decisions taken on the basis of the present report.

This document does not constitute an offer or invitation to subscribe for or purchase any financial instruments and neither this document nor anything contained herein shall form the basis of any contract or commitment whatsoever. It is being furnished to you solely for your information and may not be reproduced or redistributed to any other person. This document nor any copy hereof is not to be distributed directly or indirectly in the United States, Australia, Canada or Japan.

Recommendations are based on essential data from the entire history of a company being the subject of a recommendation, with particular emphasis on the period since the previous recommendation. Investing in shares is connected with a number of risks including, but not limited to, the macroeconomic situation of the country, changes in legal regulations as well as changes on commodity markets. Full elimination of these risks is virtually impossible.

It is possible that BRE Bank Securities S.A. renders, will render or in the past has rendered services for companies and other entities mentioned in the present report.

The present report was not transferred to the issuer prior to its publication.

BRE Bank Securities S.A., its shareholders and employees may hold long or short positions in the issuer's shares or other financial instruments related to the issuer's shares. BRE Bank Securities S.A., its affiliates and/or clients may conduct or may have conducted transactions for their own account or for account of another with respect to the financial instruments mentioned in this report or related investments before the recipient has received this report.

Copying or publishing the present report, in full or in part, or disseminating in any way information contained in the present report requires the prior written agreement of BRE Bank Securities S.A.

Recommendations are addressed to all Clients of BRE Bank Securities S.A. This report is not for distribution to third parties.
The activity of BRE Bank Securities S.A. is subject to the supervision of the Polish Financial Supervision Commission.

Individuals who did not participate in the preparation of this recommendation, but had or could have had access to the recommendation prior to its publication, are employees of BRE Bank Securities S.A. authorised to access the premises in which recommendations are prepared, other than the analysts mentioned as the authors of the present recommendation.

Strong and weak points of valuation methods used in recommendations:
DCF – acknowledged as the most methodologically correct method of valuation; it is based in discounting financial flows generated by a company; its weak point is the significant susceptibility to a change of forecast assumptions in the model.
Comparative – based on a comparison of valuation multipliers of companies from a given sector; simple in construction, reflects the current state of the market; weak points include substantial variability (fluctuations together with market indices) as well as difficulty in the selection of the group of comparable companies.

Previous ratings issued for PKN Orlen

Rating	Buy	Buy	Buy
Rating date	2009-02-27	2009-06-02	2009-09-16
Price on rating day	21.45	30.50	27.15
WIG on rating day	21923.27	30781.55	35989.98