

Tuesday, March 19, 2019 | special comment

## KGHM - Possible change in the mining tax formula

Rating: hold | target price: PLN 92.41 | current price: PLN 105.70

**KGH PW; KGH.WA | Mining & Metals, Poland**

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Yesterday Parliament published a draft of amendment to the mining tax filed by PiS deputies. The draft assumes that the financial effect of reducing the silver and copper tax will reduce state budget income by PLN 180 million in 2019 and PLN 240 million in subsequent years. Our estimates suggest that the change in the copper and silver tax formula will translate into savings for KGHM in the amount of PLN 179 million in 2019, PLN 202 million in 2020 and PLN 197 million in 2021. Potential tax reduction results in an increase in our valuation by PLN 8.5 / share (from PLN 92.41 /

share to PLN 100.92 / share). The DCF valuation itself is growing by PLN 12.2 / share (from PLN 87.3 / share to PLN 99.5 / share). It is worth noting that in the wage negotiations in the KGHM Group in 2019, it was established that at the time of changes in mining tax, the parties will start discussions regarding the payment of an additional annual bonus for earning profit. Our calculations of the impact of tax reduction on valuation do not include additional employee rewards.

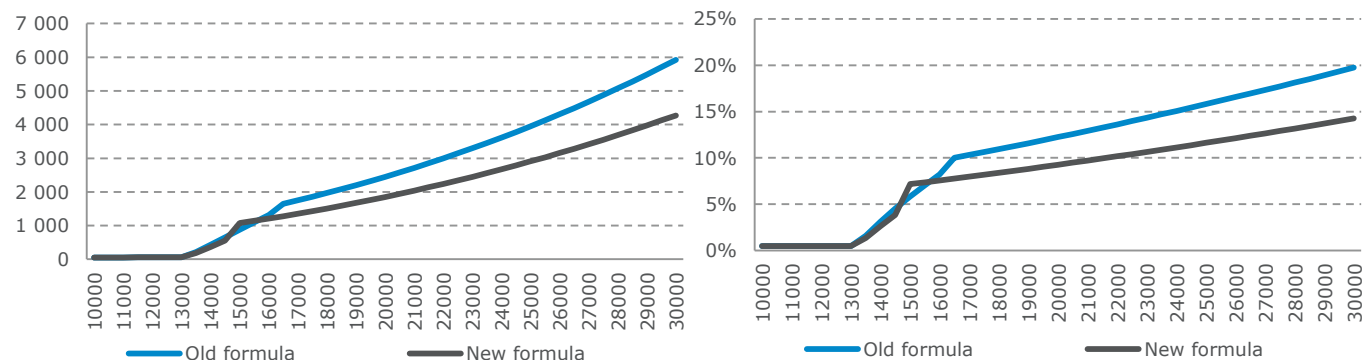
### The effect of changes in forecasts on the potential update of the formula in mining tax

Forecast change	2018	2019E	2020E
EBITDA (adj.)	0.0%	3.4%	3.9%
Net profit (adj.)	0.0%	7.7%	9.6%

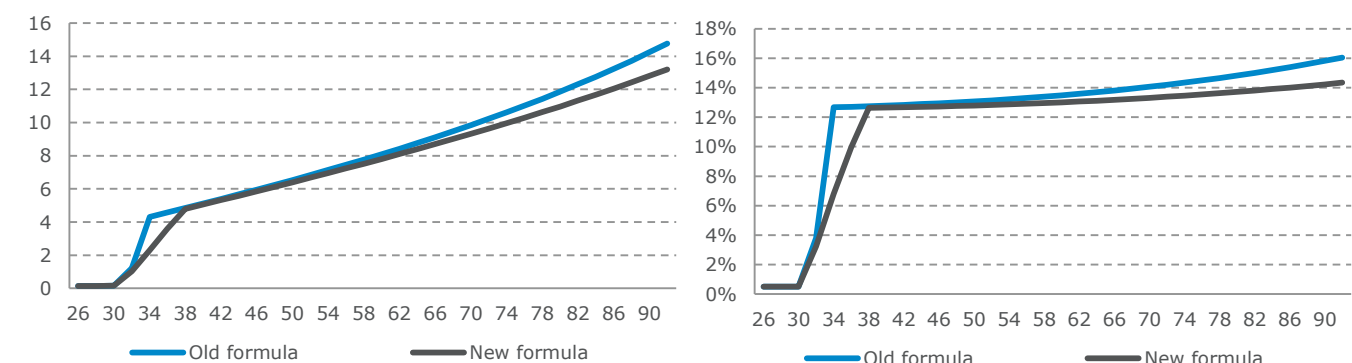
### Value of the mining tax according to the old and new formula (PLN million)

	2019E	2020E	2021E	2022E
Old formula	1,804	1,972	1,927	1,923
New formula	1,625	1,770	1,730	1,726
<b>Difference</b>	<b>179</b>	<b>202</b>	<b>197</b>	<b>197</b>

Value of mining tax on copper extraction before and after possible changes (left graph, horizontal axis copper price PLN / t, vertical axis mining tax PLN / t) and tax value in relation to the copper price (right graph, horizontal axis copper price PLN / t, vertical axis %)



The value of the mining tax on silver extraction before and after the changes (left graph, horizontal axis price of silver PLN / kg, vertical axis mining tax PLN / kg) and tax value in relation to the silver price (right graph, horizontal axis silver price / kg, vertical axis %)



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

**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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**Economic profits** – discounting of future economic profits; the weak point is high sensitivity to changes in the assumptions made in the valuation model.  
**Discounted Dividends (DDM)** – discounting of future dividends; the weak point is high sensitivity to changes in the assumptions as to future dividends made in the valuation model.  
**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.

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