

Wednesday, August 07, 2019 | update

Famur: buy (reiterated)

FMF PW; FMF.WA | Machinery, Poland

All Set To Brave Softer Demand

The inventory of hard coal held by Polish mines is increasing, and as prices of thermal and metallurgical coal fall worldwide this is putting downward pressure on the sales profits of domestic producers. This indicates tighter coal mine earnings next year, additionally weighed down by higher costs of labor, possibly prompting cutbacks in the industry's capital expenditures which, from the highest spend in seven years of PLN 5 billion seen in 2019, might decline to a projected PLN 4.4bn in 2020 (-12% y/y). Reduced mine investment means fewer bookings for mining equipment suppliers like Famur, whose revenue next year is expected by us to be 17% lower than this year at a projected PLN 1.8 billion, with EBITDA likely to post a 15% drop to PLN 469m. The negative impact of diminished volumes on sales margins should be mitigated by a higher share of aftermarket equipment and lower production costs thanks to declines in prices of steel and services, resulting in a higher 2020 EBITDA margin of 26.6% (+0.6 pp). Famur has a dominant position in the Polish market for mining equipment since the takeover of former rival Kopex in 2017, and as such we believe it can successfully navigate a more competitive environment. On our updated estimates, FMF stock is trading at a discount of about 16% to the 2019-2021E P/E and EV/EBITDA ratios of comparable companies. Even though it might take longer next year to collect payments from coal mine customers, Famur's FCF/EV ratio in 2020 and 2021 is expected to average 10%, and the respective dividend yields in the next two years might approximate 9% and 7%. After revising our 2020 and 2021 forecasts, we lower our target price for FMF from PLN 6.71 to PLN 5.33 per share but we maintain a buy rating for the stock.

Increasing coal stocks, low prices

Polish hard coal inventories increased to 4.0mmt in June 2019, the highest level since August 2016, after a relatively warm winter crimped demand for heating fuels. Increasing imports also add significantly to the build-up. Coal prices at ARA ports (adjusting for calorific value and freight) are currently trading close to the prices in the Polish market, and if they fall they will drag the domestic market with them.

Anticipating contraction in 2020 mine investment

Our baseline scenario for the Polish mining equipment market assumes total capital expenditures by local mines of approximately PLN 5 billion in 2019 (+12% y/y), of which PLN 3 billion-worth of orders (+18% y/y) coming from state-run mines. In 2020, we assume CAPEX will decrease to PLN 4.4bn (-12% y/y), followed by further reduction to PLN 4.1bn in 2021 (-8% y/y), and stabilization or another rise in 2022.

Low debt will help weather the slowdown

In 2020, depending on the financial standing of Polish mines, Famur might experience extended payment terms on customer invoices. As a result, the OCF/EBITDA ratio in 2020 might decrease to 75% from a 2009-2018 average of 83%. At the same time, however Famur's net debt at the end of 2020 is expected to be close to zero even after a projected dividend payment of PLN 226m. Even assuming the Company makes an acquisition as part of the strategy to move into the hard rock mining business, and even on the off-chance that it makes no profit on the planned sale of noncore assets, the net debt/EBITDA ratio is not likely to exceed 0.5x in 2020-2021.

(PLN m)	2017	2018	2019E	2020E	2021E
Revenue	1,459.6	2,229.1	2,124.7	1,765.1	1,660.5
EBITDA	308.0	491.4	552.8	469.2	393.5
EBITDA margin	21.1%	22.0%	26.0%	26.6%	23.7%
EBIT	132.9	300.2	390.4	313.9	248.3
Net income	48.5	207.9	452.3	249.2	196.0
P/E	51.0	12.2	5.6	10.2	13.0
P/CE	11.1	6.4	4.1	6.3	7.4
P/B	1.7	1.6	1.6	1.5	1.5
EV/EBITDA	8.7	5.7	4.6	5.3	6.2
DPS	0.00	0.44	0.53	0.39	0.33
Dividend Yield	0.0%	10.0%	12.0%	8.9%	7.4%

Current Price	PLN 4.42
Target Price	PLN 5.33
MCap	PLN 2.5bn
Free Float	PLN 1.3bn
ADTV (3M)	PLN 1.7m

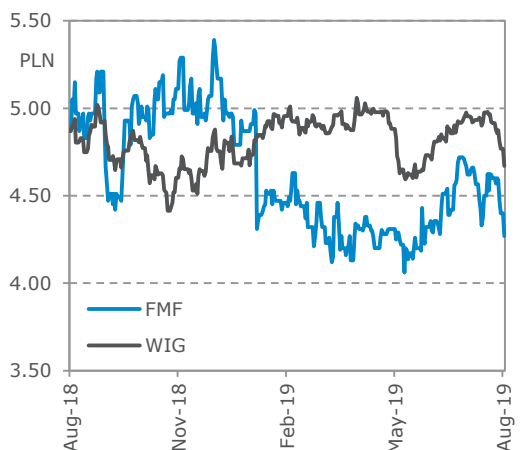
Ownership

Tomasz Domogała	47.30%
OFE NN	10.32%
OFE Aviva	9.64%
Others	16.74%

Business Profile

Famur is a supplier of back-to-back mining solutions including longwall systems, powered roof supports, shearers and roadheaders, transport systems, and hydraulic actuators. Famur's product mix also includes coal handling facilities and coal and slag conveyors for power stations. The Company generates approximately 70% of its annual sales revenues in Poland.

FMF vs. WIG



FMF adjusted for dividend (PLN 0.53 DPS)

Company	Target Price		Rating	
	new	old	new	old
Famur	5.33	6.71	buy	buy

Company	Current Price	9MTP	Upside
Famur	4.42	5.33	+20.6%

Forecast Update	2019E	2020E	2021E
Revenue	-0.9%	-13.7%	-20.4%
EBITDA	+0.8%	-4.7%	-19.0%
Net profit	-0.3%	-9.2%	-21.4%
Underground Revenue	0.0%	-14.9%	-23.2%
Surface Revenue	-5.3%	-10.8%	-11.7%
Underground Margin	0.0pp	+3.1pp	+3.1pp
Surface Margin	+0.0pp	-0.9pp	-0.5pp

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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

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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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.

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

Rating	buy	buy	buy	buy	buy	buy	buy
Rating date	2019-08-02	2019-07-03	2019-06-03	2019-05-09	2019-02-04	2018-11-30	2018-08-02
Target price (PLN)	6.71	6.96	6.67	6.90	6.61	6.41	6.56
Price on rating day	4.47	5.24	4.85	4.82	4.98	5.58	5.20

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