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Industrials Update for June 2020

Industrials, Poland

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Industrials (neutral)

- Industrial stocks worldwide are showing bullish price momentum** even as analysts cut their earnings expectations.
- For our **Polish coverage universe**, the 2020 Q1 earnings season ended with **positive profit surprises from 53% of rated companies**, with only 7% missing the mark. The proportion of **firms reporting improvement** relative to the year-ago period **increased** to 53% from 47% in Q4 2019 and 29% in 3Q'19 (see page 3 for detailed statistics).
- When it comes to second-quarter profits, however, looking at [Polish industrial production numbers for May](#), we maintain it is shaping up to be the worst quarter of the year for most industrial companies. However the slump will most be followed by a **recovery in the second half of the year**, facilitated by the zloty's weakness versus the euro, an easing of pay pressures, and lower prices of raw materials like plastics, metals, steel, and natural gas, combined with cheaper electricity. With this in mind, we **change our view on industrial stocks to neutral** after many months of being negative. Low interest rates can give an additional boost to Polish small- and mid-cap valuations, including industrials, with bank customers expected to be shifting their savings from deposits to investments.
- As of today we **upgrade Forte (FTE) from neutral to overweight** based on a recovering outlook for the furniture industry (see charts on p. 9), which includes slower falls in prices of wood-based panels, less upward pressure on costs of wood and labor, and, for Polish exporters, a weak zloty.
- Our **top picks** for the next month include **Astarta (AST)**, benefitting from a structural shift in the Ukrainian sugar market, and trading at an unparalleled FCF/EV ratio of close to 50%. We also favor **TIM**, offering one of the highest dividend yields in the sector at 7%, with its sales not affected by lockdown thanks to a strong online presence.
- We **downgrade Kruszwica (KSW)** to neutral in anticipation of weak 2020 second-quarter results after a decrease in demand for vegetable oils for biodiesel production.
- We would avoid **Boryszew (BRS)**, which might have to raise capital after violating loan covenants.
- TOP PICKS – OVERWEIGHT:** AST, FTE, STL, TIM; **UNDERWEIGHT:** BRS

Chemicals (underweight)

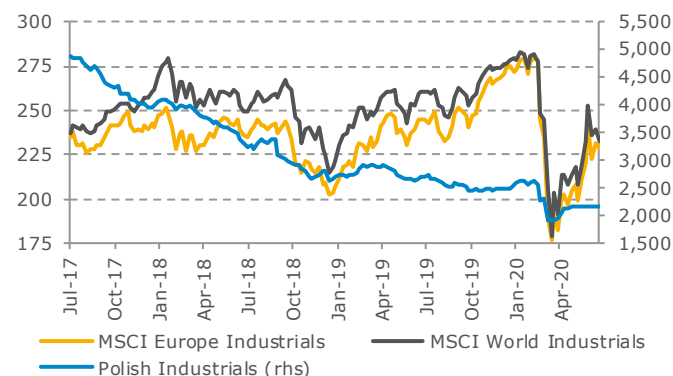
- We **downgrade our view** on the chemical sector **from neutral to underweight** to reflect worsened prospects for the second-quarter reporting season. Moreover, chemical stocks are part of the same upward price trend as industrial stocks as traders ignore outlook downgrades by equity analysts.
- European [markets for nitrogen fertilizer have been in a downtrend](#) since mid-June, putting downward pressure on producer profits, not offset by low costs of natural gas feedstocks. For **Grupa Azoty**, as its plastics and chemicals business lines yield to economic pressures, this might spell a **downgrade of analyst' expectations for the rest of the year** (see expectations chart on p. 17).
- Ciech** reported disappointing earnings results for Q1 2020, not saved by low costs of gas and coking coal fuels, and its **second-quarter prospects do not look promising** looking at the [May declines in Polish production of glass and salt](#) – two commodities which constitute a major share of the Company's sales mix.

1M* & YTD Performance

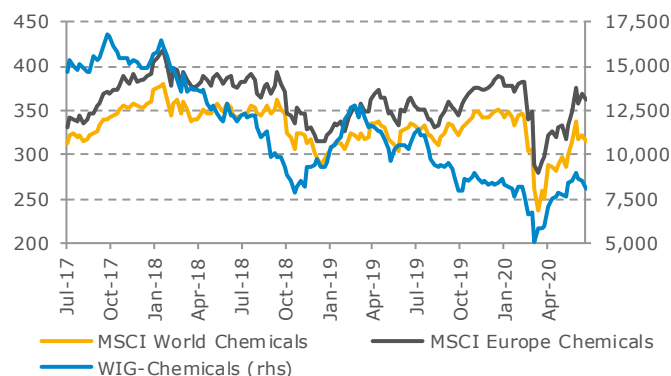
Industrials	1M	YTD
Bumeh	+44.4%	-1%
Pozbud	+37.7%	+4%
Global Cos.	+35.4%	+215%
Rafamet	+34.1%	+94%
Kęty	+33.6%	+28%
Otmuchów	+31.4%	+21%
Mercor	+28.3%	-9%
Elemental	+24.5%	-17%
Amica	+23.2%	-12%
ZPUE	+21.9%	+38%
Cognor	+21.5%	-16%
Radpol	+19.2%	+17%
Dębica	-0.3%	-11%
Tarczyński	-0.7%	-10%
Feerum	-0.8%	+1%
Ceramika NG	-1.6%	-15%
Gobarto	-2.2%	-1%
Ferrum	-2.4%	-1%
Boryszew	-2.5%	-17%
Mangata	-5.6%	-31%
Selena FM	-5.7%	-26%
Groclin	-9.3%	-12%
Astarta	-9.6%	-3%
Primetech	-13.7%	-33%
Chemicals	1M	YTD
Mercator	+97.6%	+747%
Krakchemia	+48.5%	+62%
Police	+23.6%	+30%
ZA Puławy	+14.2%	+9%
Polwax	+13.2%	+18%
PCC Rokita	+2.9%	+1%
Azoty	+2.5%	+5%
Ciech	-20.7%	-22%
WIGCHEM	-4.5%	-4%
WIG	+7.4%	-14%

*May 20 - Jun. 28

Polish Industrials vs. MSCI Index



WIG-Chemicals vs. MSCI Index



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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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%
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DCF – acknowledged as the most methodologically correct method of valuation; it consists 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 better than DCF; weak points include substantial variability (fluctuations together with market indices) as well as difficulty in the selection of the group of comparable companies.

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.

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

AC

Rating	neutral	neutral	neutral	neutral	neutral	underweight
Rating date	2020-06-29	2020-05-21	2020-04-01	2019-12-05	2019-10-30	2019-08-30
Target price (PLN)	-	-	-	-	-	-
Price on rating day	38.50	36.50	39.00	43.20	41.00	43.60

Alumetal

Rating	neutral	neutral	neutral	neutral	neutral	neutral	neutral	underweight
Rating date	2020-06-29	2020-05-21	2020-04-01	2020-02-27	2020-01-30	2019-12-05	2019-10-07	2019-08-30
Target price (PLN)	-	-	-	-	-	-	-	-
Price on rating day	40.10	37.00	34.60	43.50	42.80	39.30	35.40	34.50

Amica

Rating	neutral	neutral	neutral	neutral
Rating date	2020-06-29	2020-04-01	2019-12-05	2019-09-20
Target price (PLN)	-	-	-	-
Price on rating day	120.00	84.30	133.20	118.00

Aparator

Rating	neutral	neutral	neutral	neutral	neutral	underweight	neutral
Rating date	2020-06-29	2020-04-01	2020-03-04	2020-01-30	2019-12-05	2019-10-18	2019-09-20
Target price (PLN)	-	-	-	-	-	-	-
Price on rating day	20.80	16.20	20.00	20.70	21.10	22.00	22.60

Astarta

Rating	overweight	overweight	overweight	overweight	overweight	overweight
Rating date	2020-05-11	2020-04-01	2020-01-30	2019-12-05	2019-10-30	2019-09-05
Target price (PLN)	-	-	-	-	-	-
Price on rating day	11.75	11.50	15.90	15.90	16.85	23.00

Boryszew

Rating	underweight	underweight	underweight	neutral	neutral	underweight	underweight
Rating date	2020-06-08	2020-04-01	2020-01-30	2019-12-05	2019-10-30	2019-09-20	2019-07-26
Target price (PLN)	-	-	-	-	-	-	-
Price on rating day	3.59	3.74	4.54	4.09	4.29	4.54	4.49

Ciech

Rating	hold	buy	buy	buy	buy	hold	buy
Rating date	2020-05-29	2020-04-14	2020-02-13	2019-12-05	2019-09-05	2019-07-03	2019-06-03
Target price (PLN)	38.94	45.14	47.46	44.41	42.03	41.72	55.00
Price on rating day	39.25	31.80	39.40	36.40	34.00	41.60	42.65

Cognor

Rating	hold	hold	hold	hold	accumulate	hold	accumulate	accumulate	overweight
Rating date	2020-04-22	2019-12-06	2019-12-05	2019-11-04	2019-09-05	2019-07-25	2019-07-03	2019-06-14	2019-06-03
Target price (PLN)	0.94	1.25	1.25	1.55	2.00	1.84	1.84	1.79	-
Price on rating day	0.95	1.20	1.17	1.52	1.65	1.75	1.77	1.64	1.60

Ergis

Rating	suspended	neutral	neutral
Rating date	2019-12-05	2019-10-30	2019-08-30
Target price (PLN)	-	-	-
Price on rating day	3.84	3.20	2.48

Famur

Rating	hold	buy	buy	buy	buy	buy	buy
Rating date	2020-04-30	2020-03-04	2019-12-05	2019-08-07	2019-08-02	2019-07-03	2019-06-03
Target price (PLN)	2.20	4.58	5.18	5.33	6.71	6.96	6.67
Price on rating day	2.08	2.73	2.98	4.42	4.47	5.24	4.85

Forte

Rating	overweight	neutral	underweight	underweight	underweight	neutral	neutral
Rating date	2020-06-29	2020-05-21	2020-04-01	2020-03-20	2020-01-30	2019-12-05	2019-09-20
Target price (PLN)	-	-	-	-	-	-	-
Price on rating day	20.25	17.60	11.20	11.80	32.30	28.15	23.25

Grupa Azoty

Rating	hold	buy	buy	buy	hold	hold	hold	hold	hold	accumulate	accumulate
Rating date	2020-04-17	2020-03-04	2020-02-06	2020-02-05	2019-12-05	2019-11-06	2019-10-07	2019-09-05	2019-08-02	2019-07-03	2019-06-03
Target price (PLN)	28.42	30.55	30.31	30.31	32.75	37.12	34.09	39.77	45.93	45.93	44.42
Price on rating day	28.00	22.24	27.50	26.10	30.00	36.58	31.18	39.98	42.30	42.10	39.86

Kernel

Rating	hold	hold	hold	reduce	reduce	buy
Rating date	2020-06-03	2020-02-05	2019-12-05	2019-10-07	2019-08-19	2019-06-03
Target price (PLN)	44.58	47.25	41.60	40.76	42.70	58.63
Price on rating day	43.80	47.20	41.20	42.90	48.60	46.50

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Grupa Kęty

Rating	hold	hold	hold	hold	hold	hold	hold	hold	reduce
Rating date	2020-06-25	2020-04-07	2020-03-04	2019-12-05	2019-11-06	2019-10-07	2019-09-05	2019-07-03	2019-06-03
Target price (PLN)	453.70	335.96	360.29	335.44	333.45	298.64	327.11	345.32	326.37
Price on rating day	432.00	339.00	381.00	338.50	313.50	283.00	310.00	337.00	347.50

Kruszwica

Rating	neutral	overweight	overweight	overweight	overweight	overweight	overweight
Rating date	2020-06-29	2020-05-21	2020-05-13	2020-01-30	2019-12-05	2019-10-07	2019-09-20
Target price (PLN)	-	-	-	-	-	-	-
Price on rating day	60.40	59.00	54.80	52.20	45.80	44.40	43.00

Mangata

Rating	neutral	neutral	neutral	neutral
Rating date	2020-06-29	2020-04-01	2019-12-05	2019-09-20
Target price (PLN)	-	-	-	-
Price on rating day	50.50	50.00	72.00	66.00

Pfleiderer Group

Rating	suspended	underweight	underweight
Rating date	2019-09-20	2019-07-29	2019-07-26
Target price (PLN)	-	-	-
Price on rating day	26.20	28.00	28.00

PKP Cargo

Rating	hold	hold	reduce	reduce	reduce
Rating date	2020-05-05	2020-02-26	2020-02-05	2019-12-05	2019-11-26
Target price (PLN)	12.37	13.89	16.40	18.13	20.44
Price on rating day	11.46	13.66	17.50	20.00	22.40

Pozbud

Rating	neutral	neutral	neutral	neutral
Rating date	2020-06-29	2020-04-01	2019-12-05	2019-09-05
Target price (PLN)	-	-	-	-
Price on rating day	1.70	0.81	1.80	2.14

Stelmet

Rating	buy	accumulate	hold	hold	hold	hold
Rating date	2020-04-01	2020-02-05	2019-12-05	2019-10-07	2019-09-05	2019-07-03
Target price (PLN)	9.04	8.92	8.78	8.10	6.50	7.95
Price on rating day	6.75	7.85	8.20	7.90	6.70	7.00

Tarczyński

Rating	suspended	neutral	neutral
Rating date	2019-12-05	2019-10-07	2019-09-20
Target price (PLN)	-	-	-
Price on rating day	15.60	16.30	15.90

TIM

Rating	overweight	overweight	overweight
Rating date	2020-06-29	2020-04-01	2019-12-05
Target price (PLN)	-	-	-
Price on rating day	10.90	9.20	10.90

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