

Friday, September 18, 2020 | update

Play: buy (upgraded)

PLY PW; PLY.WA | Telecommunications, Poland

Undeserved Price Crash, Buy For Big Dividends

Stocks in Play have taken a huge, 17.6% hit in the past month, representing 12pp underperformance relative to the broad market. One of the reasons behind the price crash was most likely Poland's cybersecurity bill, which might force the Telecom to oust Huawei from its network infrastructure. Another reason is the ending lock-up period that has followed the May 2020 share issue, which ends today. Finally, investors are presumably selling other stocks to buy Allegro. Play released a note on 16 September giving an estimate of the potential costs of having to cut ties with Huawei and replace its equipment. At an estimated PLN 900m over an assumed phase-out period of seven years, the costs would be equivalent to 0.36x of the Company's annual EBITDA and expected 2020E FCFE. Even in the worst-case scenario (currently featured in our updated models as the base-case scenario), according to our calculations Play would not have to change anything in its current dividend policy, and could continue making annual distributions of PLN 1.65 per share, with the implied dividend yield at an attractive 6.3%. Play can offer uninterrupted dividends because it has the ability to generate high free cash flow, reflected in our 2020 FCFE estimate close to PLN 920m (Yield = 13.8%). In 2021-22, assuming PLN 130m has to be spent per year to replace Huawei equipment, we are forecasting respective yearly FCFE of PLN 700m and PLN 760m, with the implied yield still a much more than decent 11-12% – a prospect which should be recognized as a major upside catalyst. On our estimates, at today's price PLY is trading at attractive ratios of 5.3x 2020E EV/EBITDA and 7.2x P/E. We upgrade the Telecom to buy to reflect 35% upside potential to our new target price of PLN 35.20, representing a only small downward adjustment to the old target after higher peer valuations used in multiples comparison mostly offset the negative effects of factoring in Huawei risks.

Huawei Risk

The cybersecurity bill proposes that providers of telco network infrastructure should be categorized according to the risk they pose to Poland's cybersecurity. Based on this, any equipment bought from "high-risk" vendors would have to be decommissioned and replaced within five years, and the buying of any new equipment from them would be forbidden. It is probably safe to assume that Huawei would get the high-risk label under the new criteria. As said, Play estimates the costs of replacing the Huawei equipment it is currently using at PLN 900m over a seven-year period.

No Impact on Dividends

Our updated models assume conservatively that Play will have to spend PLN 129m a year over seven years (to make a total of PLN 900m) to oust Huawei from its network, starting from 2021. This suggests 14% CAPEX/Sales in 2021-22 and 12% subsequently. Even with the extra spend, we are confident Play is capable of generating consistently high FCFE. Assuming sustained DPS and a PLN 550m payment for 5G frequencies, the Company will most likely end FY2021 with a net debt/EBITDA ratio of approximately 2.5x. In short, the cybersecurity bill does not at all diminish Play's value, especially while interest rates remain historically low, as a dividend-paying company offering PLN 1.65 DSPS and high yields every year without fail.

(PLN m)	2018	2019	2020E	2021E	2022E
Revenue	6,855.7	7,040.8	7,101.6	7,211.5	7,360.7
EBITDA (adj.)	2,185.5	2,436.1	2,530.5	2,602.7	2,683.1
EBITDA margin	31.9%	34.6%	35.6%	36.1%	36.5%
EBIT	1,396.7	1,499.7	1,566.6	1,574.1	1,618.6
Net profit	770.6	867.0	927.1	940.7	936.9
P/E	8.6	7.7	7.2	7.1	7.1
P/CE	4.3	3.7	3.6	3.4	3.4
P/B	-	20.6	8.0	4.9	3.6
EV/EBITDA (adj.)	6.1	5.4	5.3	5.1	5.0
DPS	2.57	1.45	1.65	1.65	1.65
DYield	9.8%	5.5%	6.3%	6.3%	6.3%

Current Price	PLN 26.16
Target Price	PLN 35.20
MCap	PLN 6.64bn
Free Float	PLN 3.29bn
ADTV (3M)	PLN 29.3m

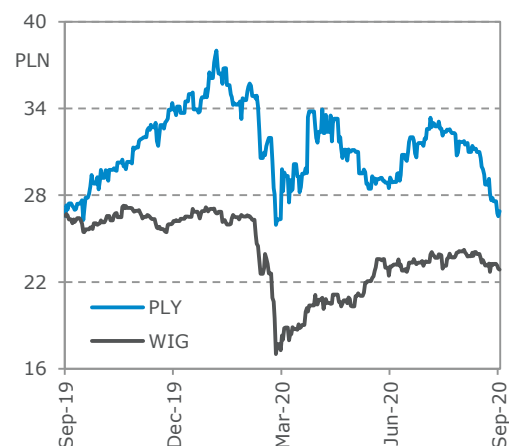
Ownership

Kenbourne Invest S.A.	20.1%
Tollerton Investments Ltd	20.1%
NN OFE	5.6%
Others	54.2%

Business Profile

Play is the largest mobile network operator in Poland with 15.3 million subscribers. It caters mainly to individuals in big cities, as well as delivering B2B services. Play is estimated to be the fourth most valuable Polish brand. Its customer base is 65.5% comprised of contract subscribers which account for 43.9% of annual revenue.

PLY vs. WIG



Company	Target Price		Rating	
	new	old	new	old
Play	35.20	35.70	buy	accumulate

Company	Current Price	Target Price	Upside
Play	26.16	35.20	+34.5%

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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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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%
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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 Play in the 12 months prior to this publication:
Play

Rating	accumulate	buy	buy	accumulate	buy	buy	hold
Rating date	2020-08-04	2020-05-15	2020-03-25	2020-02-05	2019-11-14	2019-09-12	2019-09-05
Target price (PLN)	35.70	35.70	33.50	36.00	36.00	33.10	34.20
Price on rating day	32.54	31.02	29.04	34.80	31.30	27.16	33.34

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