

Tuesday, October 13, 2020 | special comment

Lotos – Forecast of 2020 Q3 Results

Rating: buy | target price: PLN 47.09 | current price: PLN 33.91

LTS PW; LTS.WA | Oil & Gas, Poland

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Lotos is slated to release its 2020 third-quarter results on October 29th, 2020.

We expect to see adjusted LIFO-based EBITDA of PLN 0.29 billion for the quarter, about two-thirds less than in the same period a year earlier – a consequence of much tighter refining margins generated on much lower sales volumes amid the coronavirus pandemic, combined with low prices of hydrocarbons which in turn impacted the upstream business. Reported figures could be higher after positive LIFO effects.

If we are correct in our forecast, Lotos will have achieved close to 75% of our FY2020 LIFO EBITDA forecast in the year to 30 September, and we are fairly confident the Company can fulfill the expectations for the remainder of the year with refining margins poised for a likely rebound (improvement is already observed in October), and with sharply improved gas prices. Moreover, the retail business and the E&P operations have both achieved better performance this than we had originally anticipated.

In Downstream, after accounting for changes in the refinery slate since the launch of the new delayed coker (DCU), the third-quarter model refining margin in zlotys, including the Urals/Brent pricing differential, was 80% lower than in the same quarter last year (the DCU did not make much of a difference judging by Lotos's monthly production reports in a period of razor-thin margins). At the same time, the coronavirus pandemic caused an 8% decrease in refinery output in Q3.

After factoring in lower costs of natural gas feedstocks and improved geographic premiums, we expect the adjusted segmental Downstream LIFO EBITDA to come in at PLN 0.13bn vs. PLN 0.33bn in Q2 2020 and PLN 0.69bn in Q2 2019. The reported figure might be boosted by FX gains of roughly PLN 15m and positive LIFO effects of PLN 0.17bn.

In Retail, based on Poland's traffic statistics showing 4-5% year-over-year rebound in traffic in September after flat growth in the two preceding months, we expect Lotos to report slightly higher third-quarter retail sales volumes. With retail margins also higher than in Q3 2019, we see Retail EBITDA as topping the year-ago all-time-high result by 7%.

In Upstream, production in the third quarter was probably not as high as in the quarter before, and compared to a high year-ago base sales most likely suffered a slump as bad as 20%. Nevertheless, relative to the previous quarter we, are anticipating higher Upstream EBITDA of PLN 68m, achieved thanks to higher prices of gas and oil. When set against Q3 2019 the segmental EBITDA will probably be similar thanks to extra costs incurred last year.

Financing activity in Q3 2020 most likely generated a gain after FX adjustments to dollar-denominated obligations (+PLN 18m) and currency hedging on EUR/USD and USD/PLN (+PLN 48m).

2020 Q3 estimates vs. prior quarters

(PLN m)	Q1 19	Q2 19	Q3 19	Q4 19	Q1 20	Q2 20	Q3 20E	YoY	2020E	YTD
Revenue	6,741.0	7,662.0	7,877.8	7,212.5	6,095.8	4,245.5	5,047.6	-36%	20,638.7	75%
EBITDA	575.4	871.4	723.1	665.5	-1,083.5	23.3	477.3	-34%	-118.4	-
Upstream	205.6	178.3	70.6	268.9	-111.8	-392.4	68.0	-4%	-428.6	-
Upstream (adj.)	205.6	178.3	70.6	175.0	184.2	46.4	68.0	-4%	306.2	97%
Downstream	313.2	609.8	562.2	425.3	-1,005.3	375.7	313.8	-44%	125.0	-
Downstream (adj.)	369.7	521.7	694.8	378.9	444.0	334.7	125.1	-82%	1,350.5	67%
LIFO effect	-41.4	43.7	-121.4	-22.1	-1,402.1	405.6	173.7	-	-856.5	96%
Retail	63.5	78.5	89.2	6.1	37.8	49.1	95.5	7%	185.1	99%
Retail (adj.)	63.5	78.5	89.2	27.4	46.4	49.1	95.5	7%	193.7	99%
Other	-6.9	4.8	1.1	-34.8	-4.2	-9.1	0.0	-	0.0	-
LIFO EBITDA (adj.)	631.9	783.3	855.7	590.1	670.4	421.1	288.6	-66%	1,850.5	75%
D&A expenses	213.1	212.7	226.8	213.1	275.4	272.7	260.9	15%	1,107.0	73%
EBIT	362.3	658.7	496.3	452.4	-1,358.9	-249.4	216.5	-56%	-1,225.5	-
Financing activity	-70.1	7.4	-333.2	118.4	-371.0	19.8	37.6	-	-341.7	-
Pre-tax profit	292.2	666.1	163.1	570.8	-1,729.9	-229.6	254.1	56%	-1,567.2	-
Net profit	172.5	500.5	125.9	354.0	-1,311.6	-76.4	185.5	47%	-1,051.2	-

Source: Lotos, E - estimates by mBank

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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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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