

**Manufacturing**

Poland

**ES-SYSTEM**

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**H109 Results****Current Price: PLN 5.88**

ES-System's first-half results fell short of the company's targets. At PLN 67.2m, sales were down 16.81% over year-ago figures. EBIT plunged 54.93% to PLN 3.3m, and net income decreased a staggering 58.80% to PLN 2.3m. Such weak performance was caused by seasonal factors and delays in construction projects. As provider of lighting systems, ES-System experiences peak sales periods in the fall and winter, and a seasonal slowdown in the first and second quarter. Last year, the impact of seasonal fluctuations was not as strong as this year thanks to a booming construction industry. 2009 first-half EBIT was additionally depressed by a deferred tax reserve of approximately PLN 600,000. What is more, due to formal considerations, ES-System could not book a PLN 2m revenue from a shopping-center project completed in Vilnius, but is likely to recognize it in September (after the center is inspected and approved by Lithuanian building inspectors).

**2009 second-quarter and first-half results**

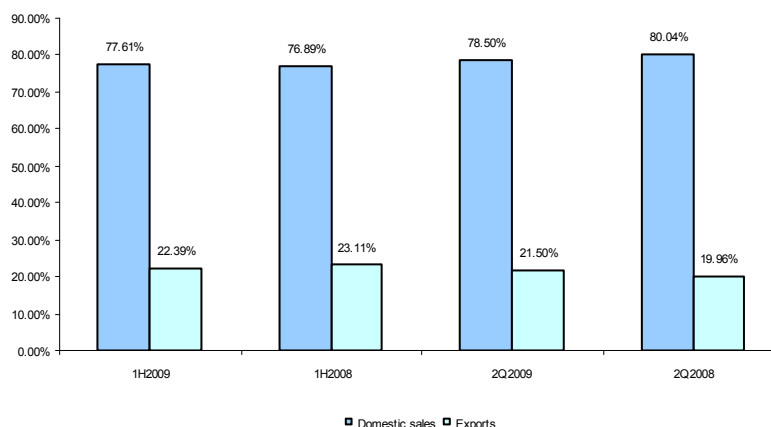
(PLN m)	2Q 2009	2Q2008	change	1H 2009	1H 2008	change
Revenue	33.2	43.2	-23.14%	67.2	80.80	-16..81%
EBITDA	1.5	5.6	-73.50%	6.2	9.7	-35.70%
EBITDA margin	9.31%	12.05%	-	9.31%	12.05%	-
EBIT	0.021	4.4	-99.53%	3.3	7.4	-54.93%
Pre-tax income	-0.2	4.2	-	3.9	7.3	-46.53%
Net income	-0.7	3.2	-	2.3	5.7	-58.80%

Source: ES-System, BRE Bank Securities

The slump in the Polish construction industry had a negative impact on ES-System's two core business segments: architectural lighting systems (which saw a 22% y/y drop in sales ), and industrial lighting systems (where sales fell 27%), which, combined, account for ca. 72% of the company's total sales Further, second-quarter sales displayed a shrinkage vs. the first quarter, when ES-System completed and recognized revenues from several contracts acquired in Q4 2008.

**Sales Breakdown**

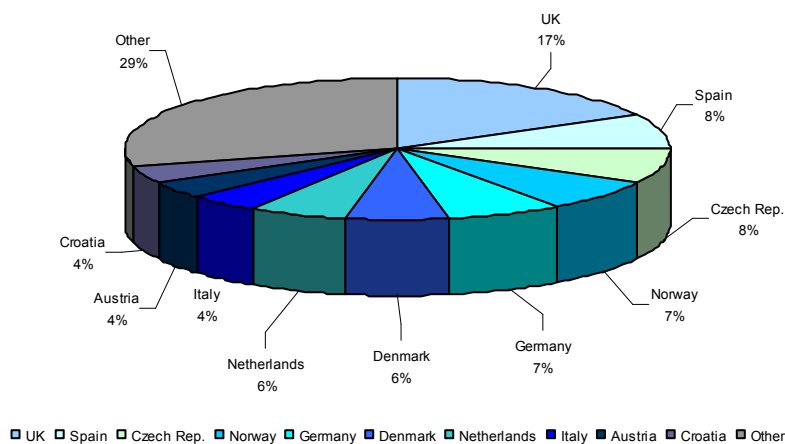
ES-System sells the bulk of its lighting solutions to local buyers (ca. 78% of sales), and exports the remaining 22%, mostly to EU countries. In H109, domestic and export sales fell by 16.03% and 19.42% respectively compared to H108, with Q209 sales dropping 24.62% and 17.24% respectively versus Q208 figures.

**2008/2009 changes in H1 and Q2 domestic and export sales**

Source: ES-System, BRE Bank Securities

ES-System is actively expanding into global markets, and has successfully competed for contracts from new customers in Argentina, Australia, India, Cyprus, Canada, South Africa, Uruguay, Malaysia, and Costa Rica. For now, its main export market is the United Kingdom, with a 17% share in total exports. The share of another key market, the Czech Republic, fell from 15% in 2008 to 8% in H1 2009.

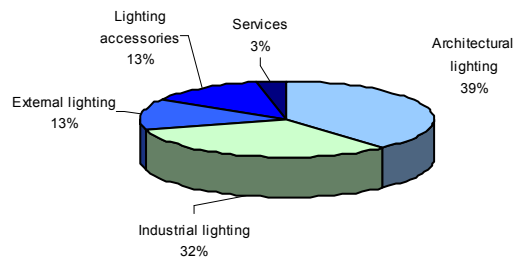
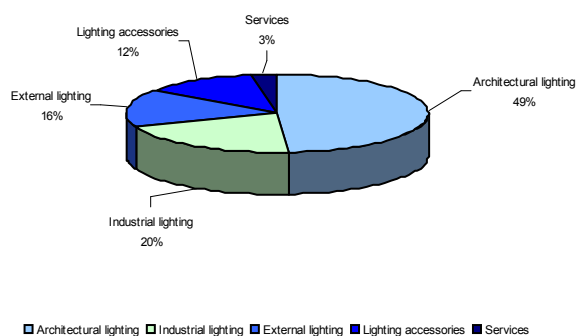
### Exports by country



Source: ES-System, BRE Bank Securities

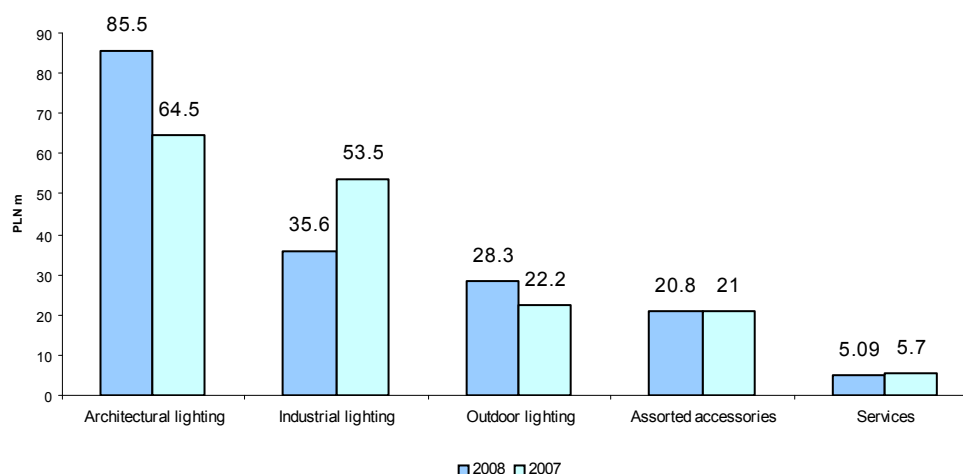
The shares of ES-Systems three main lines in H109 sales remained unchanged: architectural lighting accounted for 52% of the total sales volume (a 13% decrease vs. H108), industrial lighting systems generated 22% of total sales (15% less than a year ago), and external lighting systems, which account for 14% of total sales, fared relatively better, recording a year-on-year decline of just 2%.

### Sales breakdown by business segment: 2008 (left chart) and 2007 (right chart)



Source: ES-System, BRE Bank Securities

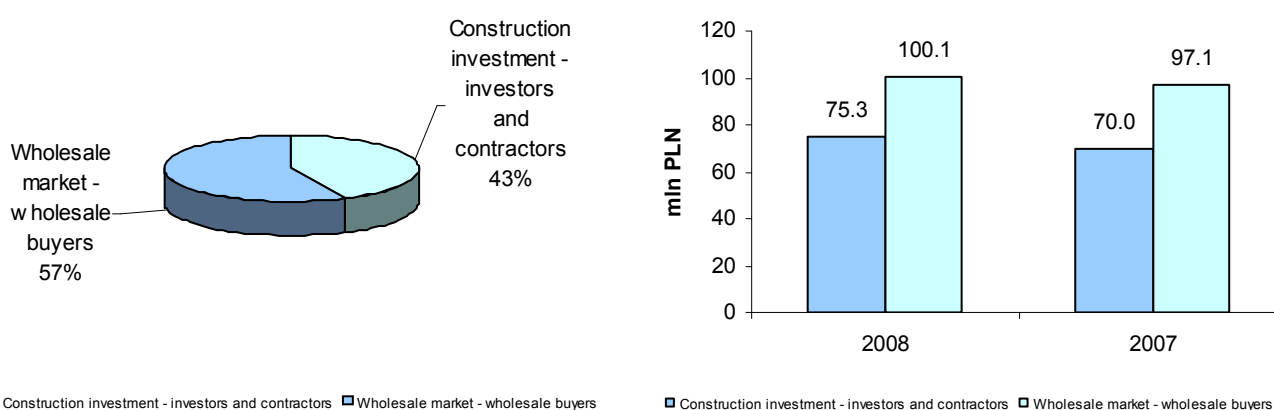
## Sales revenues in 2008 and 2007 by product type



Source: ES-SYSTEM S.A., BRE Bank Securities

The Group is attempting to boost its sales in the Modernization segment. According to the Management, the growth of this segment is driven by the increasing number of export orders. The Company's gains in this segment are illustrated by its revenues from street, industrial and school lighting systems. In the near future, the Group will focus in these areas. The decline in the number of orders in the area of investments was offset in H1 2009 by the increased sale in the wholesale segment. However, due to the lower margins attained in this distribution channel, the Company found it difficult to make up the lost ground. Nonetheless, sales in the segment were relatively high (PLN 26.6m in 2009 vs. PLN 26.9m in 2008). We forecast that sales in the segment will be increasing in the ensuing quarters, due to the improving relations with wholesale partners who settle their payments without generating gridlocks. The Group's 10 biggest wholesale partners account for 80% of revenues in this channel.

## Sales revenues in 2008 and 2007 by product type



Source: ES-SYSTEM S.A., BRE Bank Securities

## Innovation and Environment Protection – Is This the Right Strategy?

The Group is consistently attempting to introduce new, innovative products into the market, which gives it an edge over competition. It focuses on new LED and energy-saving technologies. This appears to be the way to go in the horizon of several years for at least three reasons: (1) importance of environmental protection in the EU (which is the Group's biggest exports market), with the drive towards lower energy consumption stemming not just from economic factors, but from EU legal regulations as well. An important piece of legislation is the EU directive on executive measures concerning tertiary lighting. The directive came into force in all member countries on 13 April 2009. In addition, environmental awareness and the reduction of energy consumption are in fashion in the developed countries, which drives the modernization of existing out-of-date lighting systems. This fact that the Group's revenues in the area of innovative and energy-saving lighting systems have remained positive supports this strategy. In 80% of fluorescent lamp fixtures are now electronically-powered devices, vs. 74% last year. Fluorescent lamp fixtures account for ca. 50% of the Group's sales.

## Not Yielding to Price Pressure

The Polish and international market for lighting systems is very dispersed. The high number of players drives prices and margins down. The Group felt the impact of this factor with particular strength in H1 2009, when buyers started to reduce their cost of investment and modernization and seek the cheapest solutions. ES-SYSTEM is not yielding to price pressure, however, even though it results in lower sales volumes. We believe this is the right approach, because a reduction in margins driven by a reduction in market prices makes a return to the previous (or comparable) pricing levels a difficult and lengthy process. What is more, the Group's strategy focuses on innovative products that involve the use of new technologies. Such products generate a high margin and account for the lion's share of the Company's revenues.

## ES-SYSTEM Sets Up a New Subsidiary

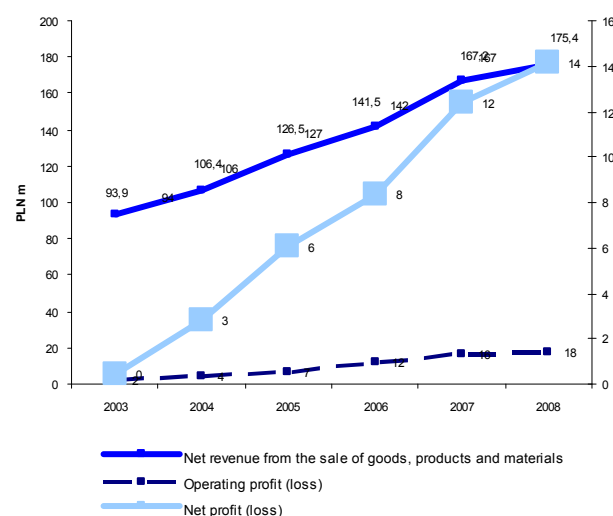
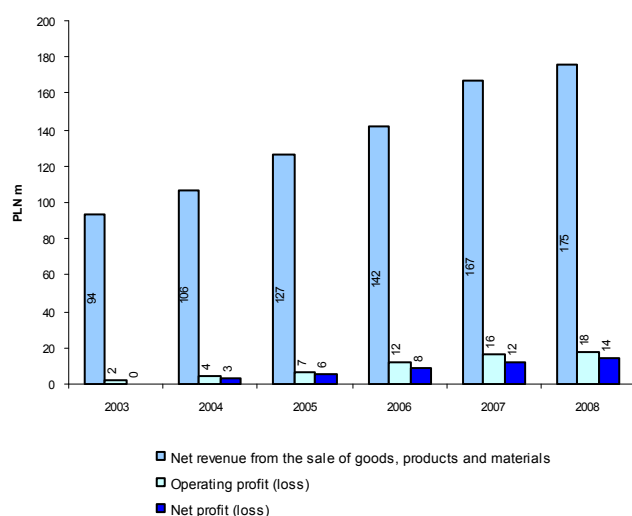
In line with its mission and its growth strategy in the area of environmental protection and energy-savings installations, ES-SYSTEM created a Company which will operate in the area of renewable energy sources. For now, the Company does not want to reveal the details. We do know that EU-subsidies have been applied for. More details are to be made public towards the end of Q4 2009. According to the CEO, the new subsidiary will launch production before June 2010.

## Selected multiples of ES-SYSTEM S.A. vs. LENA LIGHTING S.A.

	2007	2008	3Q08 - 2Q09	2007	2008
	ES-SYSTEM S.A.			LENA LIGHTING S.A.	
P/E	20.31	17.75	22.90	7.56	-
P/S	1.51	1.44	1.56	0.35	0.39
EV/EBITDA	15.79	14.09	14.95	9.90	14.32
P/EBIT	15.69	14.00	16.32	5.06	7.32
P/BV	2.21	2.00	1.97	0.64	0.70

Source: ES-SYSTEM S.A., BRE Bank Securities  
\*Last four quarters, cumulative

## Earnings in 2003—2008



Source: ES-SYSTEM S.A., BRE Bank Securities



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**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

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**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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