IDMSA DOM MAKLERSKI

Company Report

10/2008/CR (347) December 1, 2008

Energomontaż Południe

Armed with patience

Analyst:
Adrian Kyrcz, a.kyrcz@idmsa.pl, +48 (22) 489 94 74

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Energomontaż Południe (EP) is one of few construction companies in Poland focused on power sector construction with extensive experience and references in the most complex projects. Though we see EP as one of top potential beneficiaries of the expected huge expenditures on the Polish power industry, market growth will begin 2010-2011, which makes EP's short-to-mid term outlook rather mediocre.

- The power sector in Poland requires immediate investment or the Polish economy will face electric power shortages in the coming years. According to URE, total expenditures on Poland's power sector may reach an impressive PLN 125 billion by 2030.

- Though the short-to-mid term outlook for the sector seems mediocre, market growth should occur after 2010-2011 on the back of power generation companies' investment schedules. Consequently, in the next three years, EP's results will be driven chiefly by power companies' rather slight renovation outlays. To develop its contract portfolio, EP plans to reinforce its foreign market presence. However, a smooth foreign expansion might be a challenge given the rather limited mobility of its execution potential. We forecast a CAGR of EP's 2009E-2011E EBIT at 7%.

- EP was also active as a residential and commercial space developer, but suspended all its pipeline projects due to current market conditions and plans to focus on its core business. Consequently, EP's financial showing is likely to be supported by one-off profits from sales of its office project and residential assets. As the potential timing of such deals is difficult to predict, we do not account for this transaction in our financial forecast.

- Our SOTP-derived 12M EFV for EP totals PLN 3.4 per share. Despite a material upside, we recommend to Hold EP's shares. The rationale behind that is a material premium visible on 2009E and 2010E multiples that EP's equities are traded vs. its peers. Furthermore, as EP's equity story seems to lack strong ST positive catalysts on the horizon, we recommend an adoption of a neutral stance toward its shares in a short-term market-relative context.

Sector: Construction
Fundamental rating: Hold (–)
Market relative: Neutral (–)
Price: PLN 2.36
12M EFV: PLN 3.4 (–)

Market Cap.: US$ 38 m
Reuters code: EMPD.WA
Av. daily turnover: US$ 0.05 m
Free float: 61%
12M range: PLN 1.86-3.99

Key data

IFRS consolidated		2007	2008E	2009E	2010E
Sales	PLN m	232.3	249.9	272.3	296.8
EBITDA	PLN m	15.1	22.6	21.7	24.0
EBIT	PLN m	10.9	18.1	16.8	18.8
Net profit	PLN m	12.4	9.8	12.2	12.5
EPS	PLN	0.28	0.21	0.26	0.26
EPS yoy chng	%	n.m.	-27	25	2
Net debt	PLN m	-15.6	87.3	85.8	85.8
P/E	x	n.m	11.4	9.2	9.0
P/CE	x	6.3	8.0	6.7	6.5
EV/EBITDA	x	5.8	8.9	9.2	8.3
EV/EBIT	x	8.1	11.1	11.9	10.6
EV/Sales	x	0.4	0.8	0.7	0.7
Gross dividend yield	%	0.0	3.9	3.2	4.0
No. of shares (eop)	ths.	44,000	47,544	47,544	47,544

Source: Company, DM IDMSA estimates

Stock performance

Source: ISI

Upcoming events

1. CSO: November construction output data release: December 18

Catalysts

1. Efficient expansion on the German market
2. Signing large contracts in the power segment
3. Buy-back to be supportive for the share price
4. Synergies with Amontex

Risk factors

1. Inefficient expansion on the German market
2. Delays in the start of the investments in the power sector in Poland
3. Prolonging slowdown (which may lower demand on steel structures)
4. Falling prices of dwellings may entail fall of land prices
5. Possible lack of expected synergies with Amontex

Contents

1. Investment opinion

Poland's power sector requires immediate investment; otherwise, the Polish economy may simply struggle with electric power shortages in the coming years. According to estimates, total power sector outlays in Poland may even reach the impressive total of PLN 125 billion by 2030.

Energomontaż Południe specializes in manufacture of steel structures and assemblies for the power sector. We believe its many years of experience and references in the most complex projects make the Company one of the top potential beneficiaries of expected spending on the power industry.

Although the long term prospects for the sector are bright, the short-to-mid term outlook seems mediocre. On the basis of power generation company investment schedules the major market growth is likely to occur after 2010-2011. To develop its contract portfolio, in the upcoming years EP will need to concentrate on rather slight outlays on the renovations on its home turf. Furthermore, EP plans to reinforce its presence on the German market. However, smooth foreign expansion might be a challenge given market's tight competition and the limited mobility of the Company's construction workforce.

We initiate our coverage of Energomontaż Południe with a long-term fundamental Hold rating and a ST market-relative Neutral bias.

The power sector in Poland is awaiting immediate investments

The power sector in Poland is awaiting immediate investments. First, Poland's power infrastructure is completely outdated and there is a need to replace old power units. Second, due to growing energy consumption (an estimated 1% of GDP growth increases energy consumption by c. 0.4%) the Polish economy may simply struggle with electric power shortage in upcoming years. Estimates indicate total expenditures on the power sector in Poland may even reach the impressive total of PLN 125 billion by 2030.

Energomontaż Południe = top beneficiary of expenditures on power sector in Poland

Energomontaż Południe is one of few construction companies operating on the Polish market whose core business is the manufacture of steel structures and complex assemblies for the power sector. During last 50 years, EP participated in the assembly of over 200 power units domestically and abroad with an impressive total power of c. 15 ths MW (c. 40% of Poland's total power generation capacity). Many years of market experience and references in the most complex projects make it one of the top potential beneficiaries of the expected outflows on the power sector in Poland.

The short-to-mid term prospect for the power sector in Poland seems mediocre

Although the long-term prospects for the sector are bright, the short-to-mid term outlook is rather mediocre. Power generation companies (PGE, Enea) investment schedules clearly show major growth is likely to occur after 2010-2011. To develop its contract portfolio, EP is likely to be required in the nearest years to focus on rather slight outlays on renovation works. Furthermore, EP plans to strengthen its presence on the foreign market. Germany is its main foreign market and is carrying out an extensive new power capacity investment program. However, smooth foreign expansion might be a challenge given the German market's tight competition and the limited mobility of EP's construction potential. Consequently, we forecast the CAGR of EP's operating profit in 2009E-2011E at a mere level of 7% (we forecast acceleration of EP's profits after 2011E).

EP suspended realisation of all of its housing projects

Apart from its power-related construction business, EP was also a residential and commercial developer. However, EP suspended realization of all of its pipeline projects and it plans to fully concentrate on its core activity due to current market conditions (low volumes of homes sold on the market, more strict bank loan granting policies). Consequently, EP's financial showing will be supported by one-off profits from the sale of housing assets and commercial project, we believe. As the potential timing of such deals is difficult to guess, we do not account for such transactions in our financial forecast.

Hold + Neutral

Our SOTP-derived 12M EFV for EP totals PLN 3.4 per share. Despite the upside of our SOTP-derived 12M EFV of EP, we recommend to Hold EP shares, considering material premium visible on 2009E and 2010E multiples that EP's equities are traded vs. its peers. Furthermore, as EP's equity story seems to lack strong ST positive catalysts on the horizon, we recommend an adoption of a Neutral stance towards its shares in a short-term market-relative context.

2. Valuation

▲ **We value EP using the sum-of-the-parts approach (SOTP). We value EP's (i) construction business using the standard DCF FCFF approach, (ii) the office project by dividing the annual net operating income by the market capitalization rate, and (iii) its housing assets by calculating their liquidation value.**

▲ **Our SOTP-derived 12M EFV for Energomontaż Południe is PLN 3.4 per share.**

▲ **The peer relative comparison shows that the discount EP's equities are priced with materially dissappears over time.**

We run a SOTP valuation of EP

We value EP using the sum-of-the-parts approach (SOTP), which we find the most appropriate valuation methodology given the different segments in which the Company operates – where, as we see it, different valuation methodologies should be applied. We value: (i) EP's construction business using the DCF FCFF approach, (ii) the office project by dividing the annual net operating income by the market capitalization rate, and (iii) its housing assets by calculating their liquidation value.

2.1. Construction business

We value EP's construction business using DCF FCFF approach

EP's construction business is valued using the standard DCF FCFF approach (please refer to *Figure 1* for details). We apply a residual growth assumption of 2.0% and all-equity beta of 1.0.

Fig. 1 *Energomontaż Południe; DCF valuation of construction business*

PLN m	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2018E>
Sales	249.9	272.3	296.8	332.4	379.1	432.7	494.0	534.1	557.1	580.0	604.0	
yoy change	*8%*	*9%*	*9%*	*12%*	*14%*	*14%*	*14%*	*8%*	*4%*	*4%*	*4%*	
EBIT margin	7.3%	6.2%	6.3%	6.6%	7.0%	6.8%	6.8%	6.5%	6.0%	5.8%	5.8%	
EBIT	18.1	16.8	18.8	21.9	26.6	29.5	33.8	34.6	33.5	33.8	35.0	
yoy change	*66%*	*-7%*	*12%*	*17%*	*21%*	*11%*	*14%*	*2%*	*-3%*	*1%*	*4%*	
Effective cash tax rate (T)	22%	19%	19%	19%	19%	19%	19%	19%	19%	19%	19%	
EBIT * (1-T)	14.1	13.6	15.2	17.8	21.6	23.9	27.4	28.0	27.1	27.3	28.4	
yoy change	*72%*	*-4%*	*12%*	*17%*	*21%*	*11%*	*14%*	*2%*	*-3%*	*1%*	*4%*	
EBITDA	22.6	21.7	24.0	27.4	32.4	35.7	40.2	41.3	37.9	37.3	39.8	
yoy change	*50%*	*-4%*	*11%*	*14%*	*18%*	*10%*	*13%*	*3%*	*-8%*	*-2%*	*7%*	
EBITDA margin	9.0%	8.0%	8.1%	8.3%	8.6%	8.2%	8.1%	7.7%	6.8%	6.4%	6.6%	
Depreciation	4.5	4.9	5.2	5.5	5.8	6.1	6.4	6.7	4.4	3.5	4.8	
EBIT * (1-T) + D	18.6	18.5	20.4	23.3	27.4	30.0	33.8	34.7	31.5	30.9	33.2	
yoy change	*50%*	*0%*	*10%*	*14%*	*18%*	*10%*	*12%*	*3%*	*-9%*	*-2%*	*7%*	
Capex	-31.4	-5.6	-6.1	-6.4	-5.7	-6.0	-6.3	-6.6	-6.9	-4.5	-4.9	
Change in WC	-20.3	-8.3	-9.1	-13.2	-17.4	-19.9	-22.8	-14.8	-8.5	-8.5	-8.9	
Free cash flow	**-33.1**	**4.6**	**5.2**	**3.7**	**4.3**	**4.2**	**4.7**	**13.3**	**16.1**	**17.8**	**19.4**	
Cost of equity												
Risk free rate (nominal)	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	6.4%	5.0%
Equity risk premium	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%
Unlevered beta	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Beta adjusted for the level of Company's leverage	1.73	1.67	1.66	1.59	1.59	1.74	1.66	1.52	1.53	1.53	1.46	1.46
Required rate of return	**14.2%**	**13.9%**	**13.9%**	**13.5%**	**13.6%**	**14.2%**	**13.9%**	**13.3%**	**13.3%**	**13.3%**	**12.9%**	**11.5%**

Source: Company, DM IDMSA estimates

Fig. 2 Energomontaż Południe; DCF valuation of construction business (continued)

PLN m	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2018E>
Cost of debt												
Cost of debt (pre-tax)	7.4%	7.2%	6.5%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%
Effective tax rate	22%	19%	19%	19%	19%	19%	19%	19%	19%	19%	19%	19%
After-tax cost of debt	**5.8%**	**5.8%**	**5.3%**	**4.9%**	**4.9%**	**4.9%**	**4.9%**	**4.9%**	**4.9%**	**4.9%**	**4.9%**	**4.9%**
WACC												
Weight of debt	48%	45%	45%	42%	42%	48%	45%	39%	39%	40%	36%	36%
Weight of equity	52%	55%	55%	58%	58%	52%	55%	61%	61%	60%	64%	64%
Cost of equity	14.2%	13.9%	13.9%	13.5%	13.6%	14.2%	13.9%	13.3%	13.3%	13.3%	12.9%	11.5%
After-tax cost of debt	5.8%	5.8%	5.3%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%	4.9%
WACC	**10.1%**	**10.2%**	**10.0%**	**9.9%**	**9.9%**	**9.8%**	**9.8%**	**10.0%**	**10.0%**	**9.9%**	**10.0%**	**9.1%**
Discount multiple	1.00	1.09	1.20	1.32	1.45	1.60	1.75	1.93	2.12	2.33	2.56	
Discount factor	1.00	0.91	0.83	0.76	0.69	0.63	0.57	0.52	0.47	0.43	0.39	
PV of free cash flow (PLN m)		**4.2**	**4.4**	**2.8**	**2.9**	**2.6**	**2.7**	**6.9**	**7.6**	**7.7**	**7.6**	
Sum of FCFFs PVs (PLN m)												49.3
Weight of debt in the residual period												36%
Weight of equity in the residual period												64%
Average cost of equity in the definite period												13.2%
Average WACC in the definite period												10.1%
WACC in the residual period												9.1%
Residual growth of FCFFs, base-case scenario												2.0%
Residual value (PLN m)												276.4
Present value of the residual value (PLN m)												107.9
EV of EP's construction business (PLN m)												**157.2**

Source: Company, DM IDMSA estimates

2.2. Office space

We value EP's office space by dividing annual NOI by the market capitalisation rate

We value EP's only office space project (*Legnicka Park – Popowice)* by dividing the annual NOI by the market capitalization rate (please refer to *Figure 3* for details). Applying a vacancy rate of 10%, a market yield of 8.5%, and a net rate at EUR 13 per 1 sq m per month (EP has leased c. 70% of the NSA at that price), our valuation of the project comes to PLN 53.8 million. EP plans to cash in on this project fairly soon. However, since it is difficult to guess the timing of such a deal, we do not account for it in our financial forecast for the Company.

Fig. 3 Energomontaż Południe; Valuation of the Company's office space

Name of the project	Location	Describtion	Rentable area (sq.m.)	Vacancy rate implied	Yearly net operating income (PLN m)	Yield implied	Property value implied (PLN m)
Legnicka Park Popowice	Wrocław	Office space	8.800	10%	4.6	8.50%	53.8

Source: Company, DM IDMSA estimates

2.3. Housing assets

We value EP's housing assets by calculating their liquidation value

We value EP's housing assets by calculating their liquidation value (please refer to *Figure 4* for details). We find this methodology most suitable given current market conditions (weak volumes of new homes sold on the market) and the fact that EP has suspended construction of all of its housing projects.

We value *Osiedle Książęca* Phases 2 and 3 and *Willa nad Potokiem* through a calculation of the land value (construction work has not begun in either of the two projects). We assume that 1 sq m of land equals 5% of the selling price of 1 sq m of a dwelling. For land in Opole, we assume its value is equal to what EP spent to acquire it (the deal was closed in mid-2008 and the construction process has not begun). We value Phase 1 of *Osiedle Książęca* at cost (the construction process has been suspended in the middle phase). Consequently, our total valuation of EP's housing assets is PLN 40.3 million.

Fig. 4 Energomontaż Południe; Valuation of the Company's housing assets

Name of the project	Location	NSA (sq.m.)	Average price per sq m of sellable area	% of dwelling price as a cost of land	Average land price (PLN)	Value to the Company (PLN m)
Osiedle Książęca (Phase 2 and 3)	Katowice-Ligota	36,000	5,000	5%	250	9.0
Willa nad Potokiem	Katowice-Piotrowice	3,500	5,000	5%	250	0.9
Wójtowa Wieś	Opole	42,000				9.0
Osiedle Książęca (Phase 1)	Katowice-Ligota	14,000				21.4
Total (PLN m)						**40.3**

Source: Company, DM IDMSA estimates

2.4. SOTP valuation

Our SOTP-derived 12M EFV of EP is PLN 3.4 per share

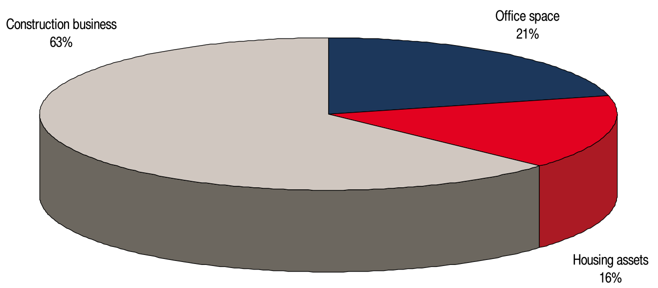
Our SOTP assessment of EP's equity value (please refer to *Figure 5* for details) is a simple sum of our separate valuations of EP's (i) construction business (DCF FCFF approach), (ii) office space (net operating income capitalization), and (ii) housing assets (calculation of the liquidation value). Our SOTP valuation produces an EP equity value of PLN 163.9 million, which is PLN 3.4 per share.

Fig. 5 Energomontaż Południe; SOTP valuation

Asset	Valuation method	Value to the Company (PLN m)	% of total equity
Construction business	DCF FCFF	157.2	63%
Office space	NOI capitalization	53.8	21%
Housing assets	Calculation of the land value	40.3	16%
Total		**251.2**	**100%**
Cash and equivalents		25.7	
Interest-bearing debt		113.0	
NAV		**163.9**	
Value per share		**3.4**	

Source: DM IDMSA estimates

Fig. 6 Energomontaż Południe; SOTP valuation breakdown



Source: DM IDMSA estimates

2.5. Peer-relative comparison

A peer-relative comparison of EP shows the discount of EP's equities priced on 2008E multiples (EV/EBIT, EV/EBITDA) dissappeares over time (note the net debt used in calculation of multiples for EP was adjusted for debt contracted to finance the commercial and residential construction projects). Please refer to *Figure 7* below for details.

Fig. 7 *Energomontaż Południe; peer-relative comparison*

	EV/EBIT			EV/EBITDA		
	2008E	**2009E**	**2010E**	**2008E**	**2009E**	**2010E**
Hydrobudowa Polska	14.9	10.9	8.1	13.1	9.6	7.3
PBG	13.8	10.1	7.0	12.3	9.2	6.6
Polimex-Mostostal	9.1	8.9	7.2	7.2	6.8	5.7
Budimex	10.6	9.2	6.6	5.9	7.8	5.7
Pol-Aqua	6.2	4.3	2.9	3.7	2.7	1.9
Average:	**10.9**	**8.7**	**6.4**	**8.4**	**7.2**	**5.4**
Energomontaż Południe	9.8	10.4	9.3	7.8	8.1	7.3
Premium/discount	-11%	20%	47%	-7%	12%	34%

Source: DM IDMSA estimates

3. Sector

The situation in the construction industry has been improving since 2004, following the crisis that hit the sector in 2000. The market witnessed a boom as of 2006 (construction output grew by 17.5% yoy). Growth dynamics, however, gradually decelerated; in October 2008 construction output rose by 10.5% yoy.

Poland lags behind most of EU countries and the need for investment is apparent. We believe EU funds should fuel growth of the construction industry in the next few years, as Poland ought to receive PLN 67 billion in 2007-2013, as compared to EUR 11.4 billion in 2004-2006. The largest beneficiaries should be the engineering segment (including infrastructure, environmental protection, and power engineering). On the eve of an economic slowdown, however, we are least optimistic on Poland's general construction segment (industrial, residential and commercial construction) which is not supported by EU funds and has already witnessed a slowdown.

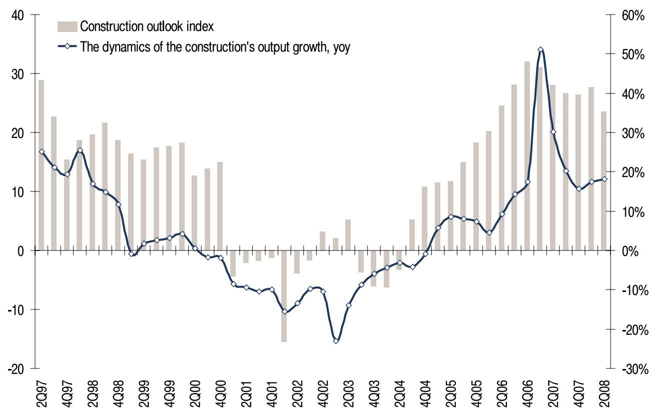
Poland's power sector is awaiting immediate investments. According to URE, the total outlays on Poland's power sector may even reach PLN 135 billion by 2030. Power generation companies' investment schedules clearly show market growth is likely to take place after 2010-2011.

3.1. Sector overview

Boom in the construction sector began in 2006

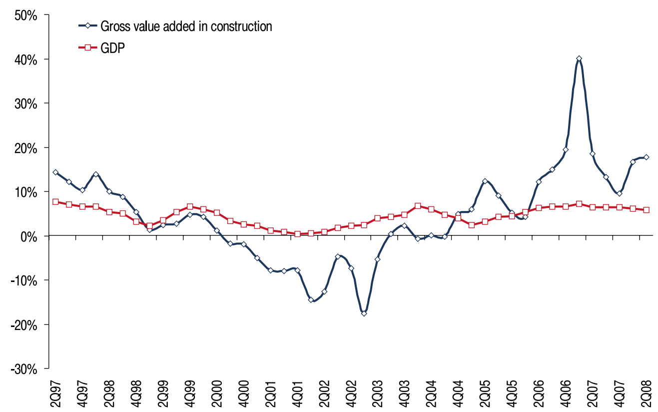
The situation in the construction industry has been improving since 2004, following the crisis that hit the sector in 2000. The first signs of revival were seen in gross value added in construction, which went up by 1.8% in 2004. The next two years brought further growth, exceeding 7% and 14% yoy, respectively. Construction output also started to increase. After poor showings in 2001 and 2002, when output plunged by -2.5% and -7.8% yoy, it began to accelerate and grew by 3.3% and 17.5% in 2005 and 2006, respectively. Poland has been witnessing a boom in the construction sector since 2006 (beginning with 2Q06, construction output has been showing double digit growth). The key reason behind that were (i) Poland's healthy GDP growth (>6%), (ii) great influx of foreign direct investments (in 2005-2007 FDIs totaled in Poland c. EUR 41 billion), (iii) influx of EU funds, and (iv) double digit growth of gross capital expenditures on fixed assets. Growth dynamics, however, have gradually decelerated, though it still remains above 10%. For example, in October 2008 construction output grew by 10.5% yoy vs. 13.2% yoy in September 2008, which might be attributed to the general slowdown in the construction segment (e.g. developers are suspending their investments, there is a lower number of industrial projects, etc.).

Fig. 8 Construction output and construction outlook index



Source: CSO

Fig. 9 GDP and gross value added in construction

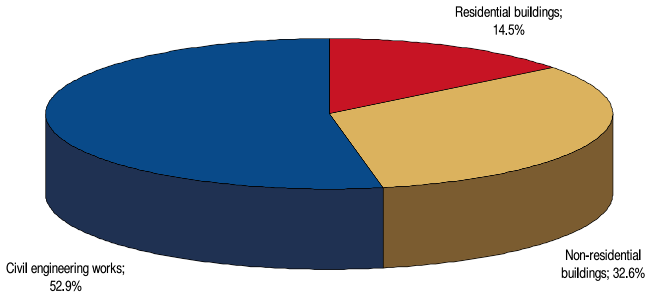


Source: CSO

Construction sector is driven by civil engineering projects

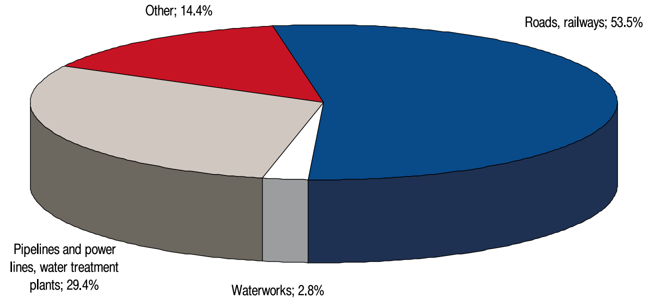
A breakdown of construction output shows the construction sector is particularly driven by civil engineering works (53%), which include road and railroad construction (53% of civil engineering works), pipeline, power line, water treatment plant (30%), and waterworks construction (3%). Residential (14%), and non-residential buildings (33%), as well as industrial, office, or commercial buildings comprise the remainder of construction output.

***Fig. 10** Construction output by project types*



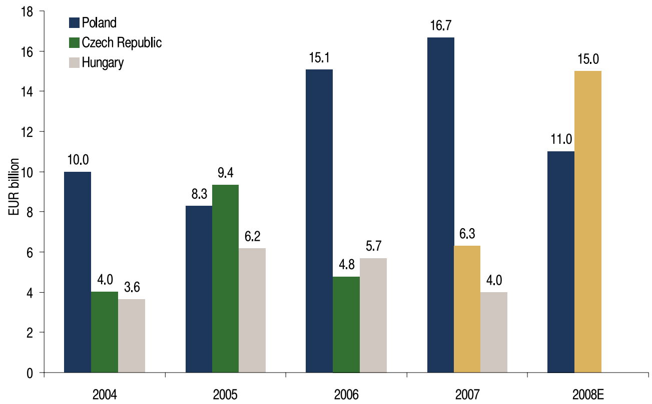
Source: CSO

***Fig. 11** Split of civil engineering works*



Source: CSO

***Fig. 12** Foreign direct investments (FDI)*



Source: NBP, Polska Agencja Informacji i Inwestycji Zagranicznych

3.2. Demand drivers for construction sector

Need for investments in Poland seems to be evident

Poland lags behind most EU countries and its need for investments is apparent. For instance, only 57% of the Poland's total population has access to municipal waste water treatments plants, as compared to 93% in Germany. The situation is even worse with regard to road infrastructure. Poland (population c. 38 million) offers c. 600 kilometers of motorways – the same as Slovenia (population c. 1.8 million). Austria uses 1 ton of asphalt per capita just for modernization purposes, while Poland uses a paltry 0.3 tons for modernization and new construction.

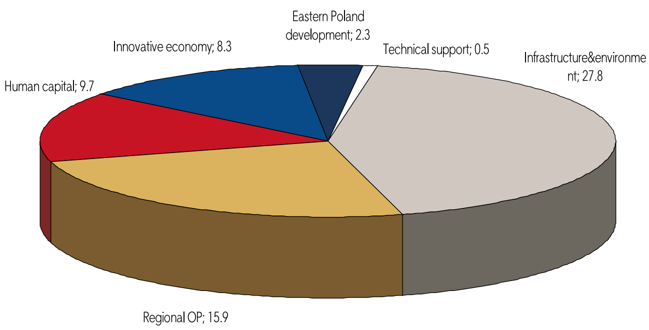
EU funds give Poland a unique chance to improve living conditions

In our opinion, the European Union, through accession and post-accession financial assistance, gives Poland a unique opportunity to improve living conditions in the country. We believe EU funds will drive the construction industry in the mid to long-term horizon. According to the Ministry of Regional Development, in 2007-2013 Poland will receive c. EUR 67.3 billion, an impressive amount compared to the EUR 11.4 billion that the country received in 2004-2006 (the average annual amount of EU funds will more than double).

The key driver of the sector should be engineering segment

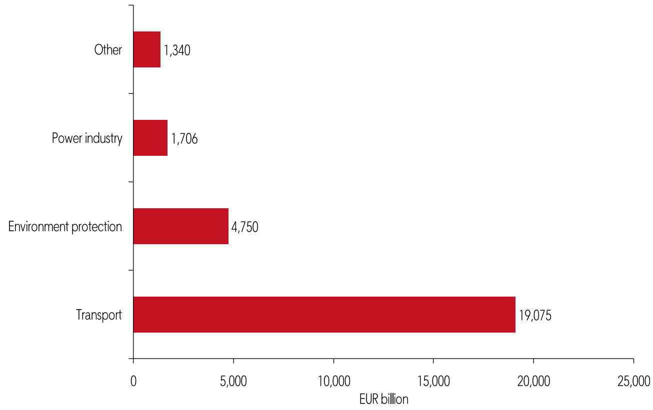
The largest beneficiary of the EU funds should be engineering segment (infrastructure, environmental protection, power engineering). It will receive around EUR 27.8 billion, representing 41% of total EU funds allocated to Poland. It is estimated that total expenditures on the engineering sector between 2007 and 2010 should grow at a CAGR of 27% and reach PLN 250 billion, which should support the stable growth of these segments in the next couple of years, we believe. On the eve of looming economic slowdown, however, we are least optimistic on the Polish general construction segment (industrial, residential and commercial construction) which is not supported by EU funds and has already witnessed a slowdown.

Fig. 13 Breakdown of EU funds allocated for Poland for 2007-2013 (EUR billion)



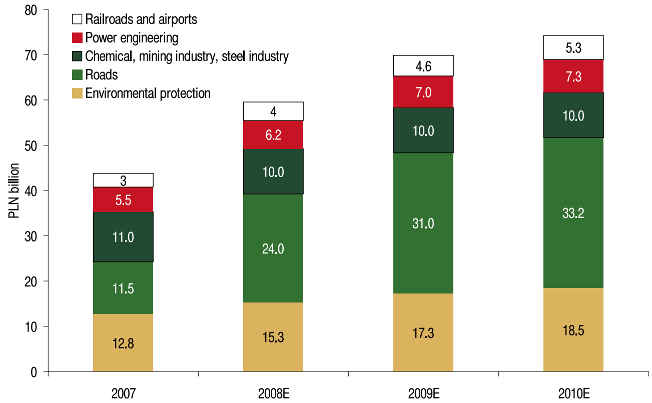
Source: Ministry of Regional Development

Fig. 14 Infrastructure & environment EU funds breakdown



Source: Ministry of Regional Development

Fig. 15 Forecast of total expenditures on engineering segment



Source: PMR

3.3. Euro 2012 Cup – a catalyst for the construction sector

The construction boom in Poland should be supported by investments stemming from organization of Euro 2012

We believe construction sector growth in the next few years should be supported by investments related to Poland's organization of the Euro 2012 Cup. First off, the Euro 2012 Cup requires Poland to complete certain construction contracts by 2012 (such as road, railroad and airport contracts), which also require spending of granted EU funds. Further, Poland is a co-organizer of Euro 2012 and must build new stadiums, which should bring another 2-2.5 billion PLN to contractors. Finally, it is estimated that Euro 2012 will affect the number of foreign guests in Poland and thus the number of hotels that will have to be developed. According to PMR forecasts, expenditures on hotels in Poland should grow at a 2007-2012E CAGR of 17%, and reach PLN 1.1 billion in 2012.

3.4. Spending on power engineering

Spending on power engineering should reach PLN 135 billion by 2030

The power sector in Poland is awaiting immediate investments; this conclusion is supported by three main reasons: (i) no spare generation capacity, (ii) old and often under-capitalized power units, and (iii) EU environmental requirements. Poland has to increase its electric power capacity; otherwise the country will face energy shortages as estimates indicate domestic energy consumption will grow by 30% by 2017, around 3% per year. The existing ageing and wasteful capacity needs to be closed down and replaced with new and more efficient units. Some generation units have been in use for 40 years and can no lnger be refitted or upgraded - they must be replaced. Moreover, Poland will have to meet EU environmental protection requirements. Poland must reduce CO_2 emission by 20% by 2020 and increase 'green' power generation to 20% by 2010.

Lack of significant investments in the domestic power sector over the last 12 years has forced construction companies to seek business abroad, chiefly in Germany, which is implementing a huge new power generation capacity program. Power sector investments should be finally begin soon in Poland. We believe the milestone in this case should be running privatization of power generation companies. According to URE (Energy Regulatory Office) research, power generation companies plan to spend PLN 135 billion by 2030 in Poland, with c. PLN 85.5 billion to be spent in 2008-2015. Power generation companies' investment schedules clearly show, however, that major market growth will occur after 2010-2011.

3.5. Economic slowdown: implications

Looming economic slowdown may hurt Polish construction industry

The looming economic slowdown may hurt the Polish construction sector as construction industry results are highly correlated with the macroeconomic situation, particularly with GDP. However, we believe the extent of the slowdown will materially differ across particular construction industry segments. The general construction segment, including industrial, residential, office and shopping centers, is most sensitive to periodic GDP growth rate fluctuations, i.e. the segment have already experienced deceleration from deferrals and suspensions of projects. Meanwhile, we find the segments benefiting from (i) post accession EU funds influx to Poland, and (ii) investments related to the EURO2012 cup in Poland offer the best opportunity to resist economic slowdown. These are chiefly the road, railroad, and environmental protection construction companies.

4. Business model and strategy

- **Energomontaż Południe is a construction company with many years of market experience and references in the most complex realizations for the power generation industry (manufacturing of steel structures and assemblies).**

- **EP operates domestically and also seeks out business abroad. Export contracts do not generate above average profitability, however, they enable EP to expand its contract portfolio (due to the low number of new contracts available on the domestic market).**

- **EP plans to focus fully on its core activity in the future. It has recently suspended all of its residential construction projects.**

- **During the last year, EP's new management team implemented a comprehensive restructuring process. The effects are visible in the Company's steadily growing profitability.**

- **EP's organic growth is supported by growth via acquisitions. In 2008, EP acquired Amontex, a steel structure manufacturer and seller of assemblies. The acquisition should generate positive synergy in the form of long-term costs savings.**

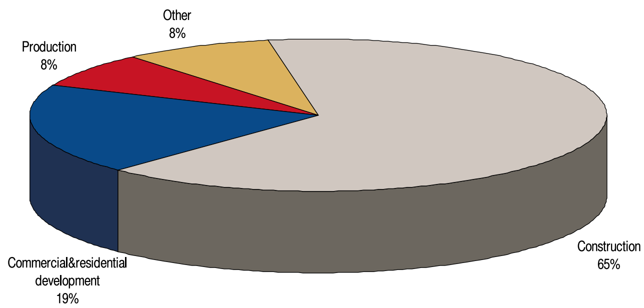
Energomontaż Południe specializes in construction for the power sector

Energomontaż Południe is one of the few construction companies operating in Poland with core business in assemblies for the power sector. EP specializes in renovation and assembly of power installations such as steam boilers, turbines, steel stacks, air and flue gas ducts, steel structures, pipelines etc. Its major clients are heat and power generation companies and entities of such power-absorbing branches as coke, cement, chemical and steel industries. EP has lengthy market experience and references in the most complex realizations. Over the past 50 years, it was involved in the assembly of over 200 power generation units (in domestic and foreign markets) with total power of 15,000 MW, i.e. equal to c. 40% of Poland's current total power generation capacity. The Company's core segment generated c. 65% of EP's 2007 total sales.

Steel structure manufacturing: EP's other business line

EP's other line of business is manufacture of steel plates. These steel structures are the main component of construction for the power sector and EP's own manufacturing division enables it to offer comprehensive services and also internalize the margin. Furthermore, having its own production division partially hedges its exposure to prospective price growth of raw materials. EP's manufacturing facility is in the town of Łagisza, in the vicinity of several power generation companies (e.g. Elektrownia Będzin, Elektownia Rybnik, etc.) that service the Silesian agglomeration. Such proximity materially shortens delivery time and cost. The 'manufacturing' division generated c. 8% of EP's total 2007 sales.

Fig. 16 Energomontaż Południe; Sales breakdown (2007)



Source: Company

EP as developer of residential and commercial space

EP's top line is also driven by a third business line: sales of condominiums and commercial buildings. EP invested in residential and commercial development to diversify its operations. For the time being, however, it has suspended all such projects with a strategy to focus only on core activity. The key reasons behind that step are the current market conditions, i.e. low volumes of new homes sold on the market and banks' stricter lending policies. EP does not rule out a sale of all its residential and commercial assets. This seems reasonable as construction outlays were partially debt financed, and hence generate financial costs. Residential and commercial business generated c. 19% of EP's total 2007 sales, while its contribution to 1-3Q08 numbers was insignificant.

EP's portfolio consists of residential and commercial projects

EP's current portfolio consists of four residential and commercial projects: (i) *Legnicka Park-Popowice (*residential, retail and office project in Wrocław), (ii) *Osiedla Książęca (*residential project in Katowice), (iii) *Willa nad Potokiem (*residential project in Katowice), and (iv) *Wójtowa Wieś* (housing project in Opole). Regarding the details please refer to *Figure 17*.

EP only partially managed to capture the fast growing housing market in Poland

EP only partially managed to capture Poland's rapidly growing housing market. It sold most residential and all the retail space in Legnicka Park-Popowice by the end of 2007 (Poland's housing market began to level out in mid-2007). The office space of that project is 70% pre-leased and is likely to be cashed in, possibly even in 2008. Phase 1 of Osiedle Książęca construction has been suspended mid-phase and construction of its Phases 2 and 3 has not begun, nor has construction begun at all on Willa nad Potokiem. EP acquired land for residential purposes in Opole in mid-2008, which recently received zoning approval, though construction has not begun there either.

Fig. 17 *Energomontaż Południe; Residential and commercial projects*

Name of the project	Description	Location	Completion/progress
Legnicka Park - Popowice	Office, retail and residential complex with 208 condos (48-72 sq.m. each), 4 exclusive condos (100 sq.m. each), retail space, and c. 8.8 ths sq.m. of the office space (B+)	Wrocław (3 km from the central city market square)	Construction completed; 90% of condos and all retail space sold in 2007; EP plans to cash in on the office space even this year.
Osiedle Książęca	Residential project of 22 (4-storey) condominium buildings with total NSA of c. 50,000 ths sq.m.	Katowice - Ligota	Construction of the project's 1st phase (14,000 sq.m. of NSA) has been suspended mid-phase. Phases 2 and 3 have been deferred.
Willa nad Potokiem	9 (3-storey) condo buildings with total NSA of 3,500 sq. m.	Katowice - Piotrowice	Start of construction has been deferred.
Wójtowa Wieś	Land zoned for residential construction purposes acquired in 2008 for c. PLN 9 million (c.40,000 sq m of the NSA).	Opole	The zoning has been recently approved.

Source: Company

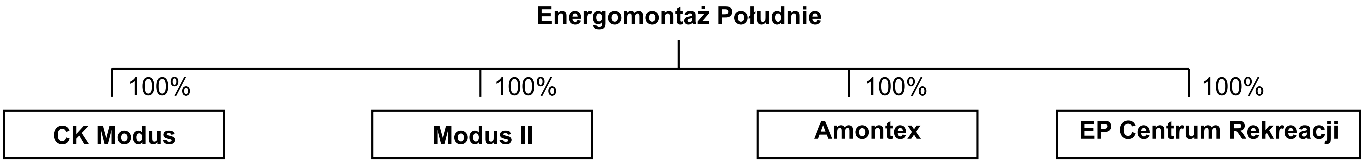
The Group's simple and transparent structure

The group structure of Energomontaż Południe is simple and transparent (for details please refer to *Figure 18*). EP runs its construction and production business through its parent company, Energomontaż Południe SA. CK Modus and Modus II are 100% subsidiaries of EP, established to carry out residential and commercial projects. Amontex is a newly acquired company (acquisition was completed in 2008) specializing in production and assembly of steel structures. EP Centrum Rekreacji provides hotel and gastronomic services – activities with insignificant impact on the Group's financial results.

Domestic market is key for EP

Poland constitutes EP's most important market. EP operates chiefly in the south-central Poland, as its execution potential is located in that region, i.e. Silesia. Consequently, it presents perfect exposure to investments in a number of power entities located in this region. At the same time, EP presents rather scanty exposure to investments running in the north-central Poland, among others those running in refineries of Orlen and Lotos (these are, however, within reach of its closest domestic peer, Energomontaż Północ, a subsidiary of Polimex-Mostostal). EP main projects in Poland have included assembly works in power generation entities in Bełchatów and Łagisza.

Fig. 18 Energomontaż Południe; Group structure

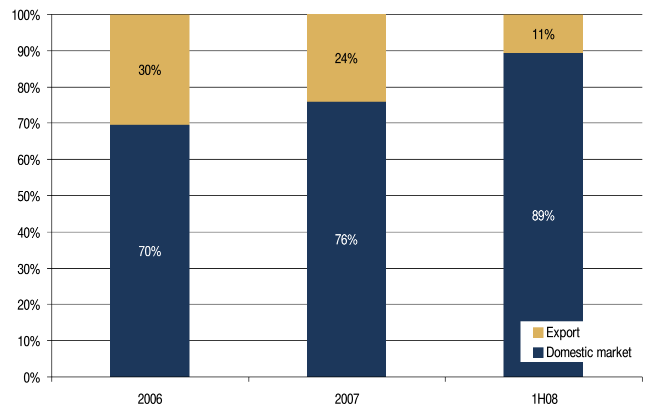


Source: Company

To expand its contract portfolio, EP also seeks business abroad

EP also seeks out business abroad. In 2007, export accounted for c. 24% of its total sales. Germany is EP's key foreign market, as the country is investing extensively in new power generation capacity. Export contracts do not generate above-average margins, but they enable EP to expand its contract portfolio. The current lack of any significant investments Poland's power sector has seemingly forced EP search out export contracts over the next couple of years. EP plans to reinforce its position on the German market. However, high competition on the German market and EP's limited execution potential mobility might be the main threats to smooth foreign expansion.

Fig. 19 Energomontaż Południe; Export vs. domestic sales

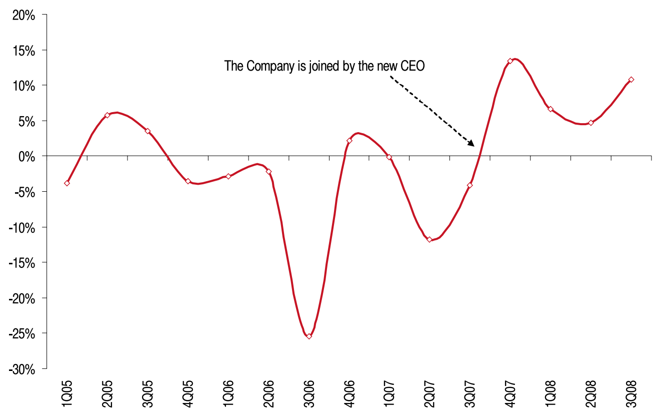


Source: Company

EP's track record is less than stellar

An examination of Energomontaż Południe's track record evidences weak contract management – where that skill is one of the key success factors on the construction market. It seems low profitability of recent years (for details please refer to *Figure 20*) has stemmed from two key reasons. First, the low number of new contracts on the market sparked a price war among contractors. Second, EP suffered from the lack of a professional project management team. Consequently, project costs have usually exceeded EP's budgets, thus deteriorating margins.

Fig. 20 Energomontaż Południe; EBIT margin in 1Q2005-3Q2008



Source: Company

Recent measures by the new management are proving effective

In the course of 2008, EP's new management (which joined the Company in the latter half of 2007) implemented a comprehensive restructuring process, that has resulted in (i) a rationalized manufacturing process, (ii) hiring of a new group of professional project managers and engineers to calculate costs and manage contracts, (iii) new bonus schemes focused on cost reduction for EP managers. In summary, the new management seems to have prioritized profitability. The above measures and a better contract portfolio have recently generated steady improvement in margins.

EP is usually a subcontractor

EP usually tenders for small and medium contracts rather than large ones, due to the high financing requirements of large projects. In consequence, it mainly acts as a subcontractor; EP subcontracts for Polish and foreign contractors such as Polimex-Mostostal, Alstom Power, Austrian Energy & Environment. EP's involvement usually boils down to construction of specific installations, contrary to general contractors, which offer turn-key realization (comprehensive completion). The profitability of small and medium-size contracts is usually lower than large ones (scale effect) limiting EP's room to expand margins. On the other hand, the attendant risk of bad contract management is also materially lower in smaller contracts.

GWE will be a useful vehicle while the number of contracts in the sector appear

Given the bright LT outlook for Poland's power sector and the potential number of tenders on the German market in the short-to-mid term, EP has established and leads an informal industry association named Grupa Wykonawcza Energetyki (GWE). Since mid-2008, GWE has associated several small and medium companies offering complementary services to the power sector (e.g. assembly works and construction design). These are reliable entities proven through cooperation with EP in recent years. The association secures completion potential and enables EP to offer complex construction services and is therefore a very useful vehicle in tendering for contracts.

EP's organic growth is supported by growth via acquisitions

EP's organic growth strategy is supported by growth via the acquisitions, as the latter seems to be a simple an efficient way to strengthen its execution potential and to extend into new construction industry segments. In 2008, EP acquired a 100% stake in Amontex for PLN 32.6 million (EP acquired a 60% stake for PLN 19 million in cash, and the remaining 40% for 4,390,000 of its shares). Amontex is a company experienced in the manufacture and assembly of steel structures used in the power sector and petrochemical industry (Amontex was involved in the assembly of an LPG tank in the gas terminal in Sławków), as well as mining industry, and general construction (offices, shopping centers, residential) – the segments which seems less attractive on the eve of looming ecomonic slowdown. Amontex is fully consolidated by EP as of 3Q08. In addition to a group of experienced employees, the acquisition should bring some positive synergy in the form of long-run cost savings.

5. Financials

▲ **We forecast acceleration of EP's sales and profits after 2011E, along with the inception of Poland's planned huge power sector investment program.**

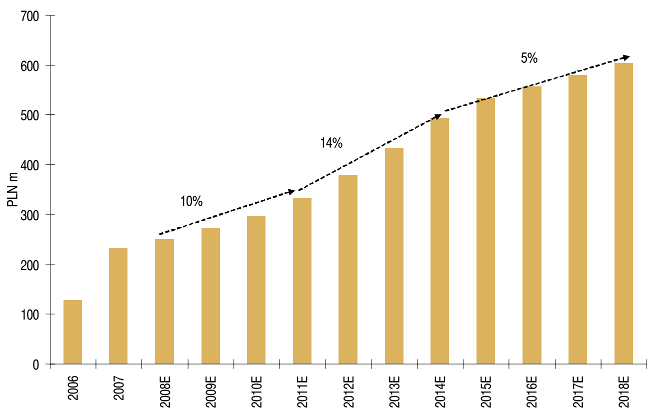
▲ **Our financial forecast for EP does not include possible earnings from the sale of office project and housing assets.**

5.1. Financial forecast

We forecast acceleration of EP's sales and profits after 2011

We forecast mediocre growth of EP's sales and profits in 2009E-2011E (we forecast CAGR of sales at 10% and EBIT of 7% for 2009E-2011E), driven mostly by spending on renovations in the domestic market and export contracts. Beginning 2011E, we forecast acceleration of EP's top line and earnings, due to expected significant growth of the Polish power market (power generation companies will likely begin investments to increase power generation capacity). We forecast CAGR of EP's sales at 14% and operating profit of 16% for 2011E-2014E.

Fig. 21 Energomontaż Południe; Sales in 2006-2018E



Source: Company, DM IDMSA estimates

2007 margin growth was supported by profits from residential construction and real estate activity

EP recorded significant yoy improvement in margins in 2007 (the EBIT margin grew from -6.6% in 2006 to 4.7% in 2007). Such development was supported by profits from real estate and residential construction business; EP completed retail and residential space of Legnicka *Park – Popowice* project in 2007 (EP uses a MSR 18 standard).

Despite the high base, we forecast improved margins in 2008

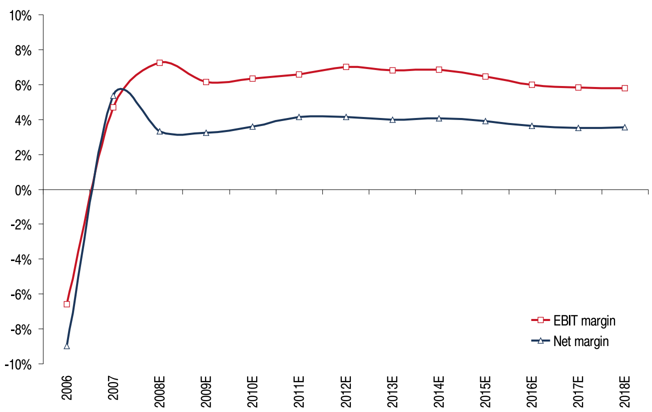
Despite the high base, we forecast yoy growth of EP's EBIT margin in 2008 (to 7.3%). We see two reasons behind that. First, EP completed the majority of the low-margin contracts from its 'old' portfolio in 1H08. Second, new management's recent efforts to improve profitability have shown results; e.g. manufacturing process rationalization pushed the production segment to reach its BEP in 3Q08.

In 2009, however, we forecast a yoy drop of the EBIT margin (to 6.2%), due to (i) a yoy overhead cost increase (note that while 2009 will be the first year of complete consolidation with Amontex, the cost side synergy effects may not yet be visible), (ii) no additional profits from other operating income (these are, however, likely to boost the Company's numbers in 2008), and (iii) higher yoy financial costs (as of 3Q08, EP's net debt totaled PLN 61.9 million vs. net cash of PLN 24.3 million in the base period). Nevertheless, the following years should bring some growth of EP's EBIT and NP margin, mostly due to the scale effect and net debt decrease.

One-off transaction may boost EP's numbers and improve margins

EP plans to cash in on its office space project and sell all of its residential assets (EP suspended all of its residential projects and plans to get rid of them). The timing of such one-off deals is difficult to predict and thus we do not account for any additional profits from this activity in our financial forecast. However, such transactions may shortly materially boost EP's numbers and profitability.

Fig. 22 Energomontaż Południe; Margins in 2006-2018E



Source: Company, DM IDMSA estimates

5.2. FX exposure

FX exposure is a risk factor for EP as c. 27% of its services are delivered abroad. The strengthening of the PLN vs. EUR has a negative impact on its results; however, that influence on the Group's profitability should remain neutral as the majority of costs and revenues are born in the same currency. Furthermore, the EP uses FX hedging.

5.3. Dividends

In 2008, Energomontaż Południe paid a dividend of PLN 0.1 per share from its 2007 net profit, producing a dividend yield of c. 3.6%. In upcoming years, EP plans to maintain its dividend policy, by annually paying out c. 1/3 of its net profit as dividend.

5.4. Buyback program

EP runs a buy back program of its own shares which may support its share price in the short to mid-term horizon. EP plans to acquire up to 4,390,000 shares (9.1% of the share capital) for as much as PLN 8.4 million by March 14, 2009. So far, EP has acquired 845,654 of its shares (1.7%) for the average price of PLN 2.67 per share.

5.5. Net debt

EP's net debt totaled PLN 61.9 million as of 3Q08 vs. net cash of c. PLN 24.3 million as of 3Q07. The net debt is a major risk factor for EP. Even more worrisome is that the debt was largely drawn (in c. 40%) for residential project development that we find currently to be risky assets.

6. Financial statements (IFRS, consolidated)

***Fig. 23** Energomontaż Południe; Balance sheet*

PLN m	2007	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
Fixed assets	**49.7**	**76.6**	**77.3**	**78.1**	**79.0**	**78.8**	**78.7**	**78.6**	**78.5**	**81.0**	**82.0**	**82.2**
Intangibles	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Goodwill	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
Tangible fixed assets	34.8	61.7	62.4	63.3	64.1	64.0	63.9	63.7	63.6	66.2	67.1	67.3
LT receivables	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
LT investments	12.6	12.6	12.6	12.6	12.6	12.6	12.6	12.6	12.6	12.6	12.6	12.6
LT deferred assets	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Current assets	**144.1**	**237.1**	**253.3**	**276.0**	**298.6**	**336.8**	**408.8**	**442.0**	**451.9**	**482.2**	**504.2**	**528.4**
Inventories	45.7	97.4	101.9	106.5	113.2	121.7	132.0	143.8	151.8	156.7	161.3	165.9
ST receivables	58.1	100.0	108.9	118.8	133.0	151.7	173.1	197.6	213.7	222.9	232.0	241.6
ST deferred assets	3.6	12.7	13.8	15.1	16.9	19.3	22.0	25.1	27.2	28.3	29.5	30.7
Cash&equivalents	35.3	25.7	27.2	34.2	34.1	42.7	80.3	74.1	57.9	72.9	80.0	88.8
Other assets	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
Total assets	**193.8**	**313.7**	**330.6**	**354.1**	**377.6**	**415.6**	**487.5**	**520.6**	**530.4**	**563.2**	**586.2**	**610.5**
Equity	**91.4**	**96.8**	**105.4**	**113.4**	**124.3**	**136.2**	**149.1**	**164.3**	**179.4**	**193.5**	**208.1**	**224.0**
Liabilities & reserves	**102.4**	**216.9**	**225.1**	**240.7**	**253.2**	**279.4**	**338.4**	**356.3**	**351.0**	**369.7**	**378.1**	**386.6**
Reserves	11.1	11.9	13.0	14.2	15.9	18.1	20.7	23.6	25.5	26.6	27.7	28.8
LT liabilities	7.4	72.7	72.7	72.7	72.7	82.7	122.7	102.7	82.7	92.7	92.7	92.7
Non-interest-bearing	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7
Interest-bearing	4.7	70.0	70.0	70.0	70.0	80.0	120.0	100.0	80.0	90.0	90.0	90.0
ST Liabilities	60.1	110.3	115.5	127.8	135.5	145.3	157.1	186.6	195.9	201.5	206.7	212.0
Non-interest-bearing	45.1	67.3	72.5	77.8	85.5	95.3	107.1	120.6	129.9	135.5	140.7	146.0
Interest-bearing	15.0	43.0	43.0	50.0	50.0	50.0	50.0	66.0	66.0	66.0	66.0	66.0
Reserves	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Deferred liabilities	23.8	22.0	23.9	26.1	29.2	33.3	38.0	43.4	46.9	49.0	51.0	53.1
Total liabilities and equity	**193.8**	**313.7**	**330.6**	**354.1**	**377.6**	**415.6**	**487.5**	**520.6**	**530.4**	**563.2**	**586.2**	**610.5**

Source: Company, DM IDMSA estimates

Fig. 24 Energomontaż Południe; Income statement

PLN m	2007	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
Sales	**232.3**	**249.9**	**272.3**	**296.8**	**332.4**	**379.1**	**432.7**	**494.0**	**534.1**	**557.1**	**580.0**	**604.0**
COGS	**-214.5**	**-217.6**	**-238.8**	**-260.4**	**-291.7**	**-331.9**	**-380.0**	**-435.3**	**-473.1**	**-496.1**	**-517.6**	**-539.1**
Gross profit on sales	**17.8**	**32.3**	**33.5**	**36.4**	**40.7**	**47.2**	**52.6**	**58.7**	**60.9**	**61.0**	**62.4**	**64.9**
Selling costs	-0.1	-0.1	-0.1	-0.1	-0.1	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
General administration costs	-9.2	-15.3	-16.6	-17.5	-18.6	-20.5	-22.9	-24.7	-26.2	-27.3	-28.4	-29.6
Net profit on sales	**8.5**	**16.9**	**16.8**	**18.8**	**21.9**	**26.6**	**29.5**	**33.8**	**34.6**	**33.5**	**33.8**	**35.0**
Other operating income	14.1	1.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other operating costs	-11.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
EBIT	**10.9**	**18.1**	**16.8**	**18.8**	**21.9**	**26.6**	**29.5**	**33.8**	**34.6**	**33.5**	**33.8**	**35.0**
Financial income	9.7	3.2	4.2	4.2	4.5	2.7	3.4	3.9	3.7	3.7	4.1	4.4
Financial costs	-4.0	-4.9	-5.9	-7.6	-7.2	-7.5	-9.0	-10.1	-9.4	-9.1	-9.4	-9.4
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pre-tax profit	**16.6**	**16.4**	**15.1**	**15.4**	**19.2**	**21.8**	**24.0**	**27.6**	**28.8**	**28.1**	**28.5**	**30.0**
Income tax	-4.2	-6.6	-2.9	-2.9	-3.7	-4.1	-4.6	-5.3	-5.5	-5.3	-5.4	-5.7
Minority interest in net income	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net profit	**12.4**	**9.8**	**12.2**	**12.5**	**15.6**	**17.7**	**19.4**	**22.4**	**23.4**	**22.8**	**23.1**	**24.3**

Source: Company, DM IDMSA estimates

Fig. 25 Energomontaż Południe; Cash flow

PLN m	2007	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
Net profit (loss)	12.4	9.8	12.2	12.5	15.6	17.7	19.4	22.4	23.4	22.8	23.1	24.3
Depreciation and amortization	4.2	4.5	4.9	5.2	5.5	5.8	6.1	6.4	6.7	4.4	3.5	4.8
NWC change:	-48.7	-71.3	-8.3	-9.1	-13.2	-17.4	-19.9	-22.8	-14.8	-8.5	-8.5	-8.9
Change in inventories	-14.0	-51.7	-4.5	-4.6	-6.7	-8.6	-10.3	-11.8	-8.1	-4.9	-4.6	-4.6
Change in receivables	-20.6	-41.9	-9.0	-9.8	-14.2	-18.7	-21.4	-24.5	-16.0	-9.2	-9.2	-9.6
Change in payables	-14.1	22.2	5.2	5.3	7.7	9.8	11.8	13.5	9.3	5.6	5.3	5.2
Other	3.3	-7.0	7.2	6.9	7.2	10.3	11.7	13.0	10.8	9.0	9.0	8.9
Operating cash flow	**-28.8**	**-64.1**	**16.0**	**15.5**	**15.1**	**16.4**	**17.3**	**19.0**	**26.0**	**27.7**	**27.1**	**29.1**
Capital expenditures	-6.2	-31.4	-5.6	-6.1	-6.4	-5.7	-6.0	-6.3	-6.6	-6.9	-4.5	-4.9
Other	14.3	1.8	2.8	2.7	3.0	1.2	1.8	2.3	2.0	2.0	2.3	2.5
Investing cash flow	**8.0**	**-29.6**	**-2.8**	**-3.3**	**-3.3**	**-4.5**	**-4.1**	**-4.0**	**-4.6**	**-5.0**	**-2.2**	**-2.4**
Change in interest-bearing debt	8.7	93.3	0.0	7.0	0.0	10.0	40.0	-4.0	-20.0	10.0	0.0	0.0
Dividends payment	0.0	-4.4	-3.6	-4.5	-4.6	-5.8	-6.5	-7.2	-8.3	-8.6	-8.4	-8.5
Interest	-0.5	-4.9	-8.1	-7.6	-7.2	-7.5	-9.0	-10.1	-9.4	-9.1	-9.4	-9.4
Other	35.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing cash flow	**44.0**	**84.0**	**-11.8**	**-5.1**	**-11.8**	**-3.3**	**24.5**	**-21.3**	**-37.6**	**-7.7**	**-17.8**	**-17.9**
Total cash flow	**23.3**	**-9.6**	**1.5**	**7.0**	**-0.1**	**8.6**	**37.6**	**-6.3**	**-16.2**	**15.0**	**7.1**	**8.8**

Source: Company, DM IDMSA estimates

***Fig. 26** Energomontaż Południe; Ratios*

	2007	2008E	2009E	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E
Sales growth (yoy)	82%	8%	9%	9%	12%	14%	14%	14%	8%	4%	4%	4%
Gross profit growth (yoy)	177%	81%	4%	9%	12%	16%	11%	11%	4%	0%	2%	4%
EBITDA growth (yoy)	n.m.	50%	-4%	11%	14%	18%	10%	13%	3%	-8%	-2%	7%
Operating profit growth (yoy)	n.m.	66%	-7%	12%	17%	21%	11%	14%	2%	-3%	1%	4%
Net income growth (yoy)	n.m.	-21%	25%	2%	25%	13%	10%	15%	4%	-3%	1%	6%
A/R turnover days	75	115	140	140	138	137	137	137	141	143	143	143
Inventory turnover days	66	120	152	146	137	129	122	116	114	113	112	111
A/P turnover days	54	71	85	86	85	84	84	84	86	87	87	88
Cash cycle	87	165	207	200	191	182	175	169	169	169	168	166
NWC/Sales	24%	51%	50%	49%	48%	46%	45%	44%	44%	43%	43%	43%
Gross margin	7.7%	12.9%	12.3%	12.3%	12.2%	12.5%	12.2%	11.9%	11.4%	11.0%	10.8%	10.7%
EBITDA margin	6.5%	9.0%	8.0%	8.1%	8.3%	8.6%	8.2%	8.1%	7.7%	6.8%	6.4%	6.6%
EBIT margin	4.7%	7.3%	6.2%	6.3%	6.6%	7.0%	6.8%	6.8%	6.5%	6.0%	5.8%	5.8%
Pretax margin	7.1%	6.6%	5.5%	5.2%	5.8%	5.7%	5.5%	5.6%	5.4%	5.0%	4.9%	5.0%
Net margin	5.4%	3.9%	4.5%	4.2%	4.7%	4.7%	4.5%	4.5%	4.4%	4.1%	4.0%	4.0%
ROE	19.1%	10.4%	12.1%	11.4%	13.1%	13.5%	13.6%	14.3%	13.6%	12.2%	11.5%	11.3%
ROA	7.6%	3.9%	3.8%	3.6%	4.3%	4.5%	4.3%	4.4%	4.4%	4.2%	4.0%	4.1%
Current Ratio	2.4	2.1	2.2	2.2	2.2	2.3	2.6	2.4	2.3	2.4	2.4	2.5
Quick Ratio	1.6	1.3	1.3	1.3	1.4	1.5	1.8	1.6	1.5	1.6	1.7	1.7

Source: Company, DM IDMSA estimates

BASIC DEFINITIONS

A/R turnover (in days) = 365/(sales/average A/R))
Inventory turnover (in days) = 365/(COGS/average inventory))
A/P turnover (in days) = 365/(COGS/average A/P))
Current ratio = ((current assets – ST deferred assets)/current liabilities)
Quick ratio = ((current assets – ST deferred assets – inventory)/current liabilities)
Interest coverage = (pre-tax profit before extraordinary items + interest payable/interest payable)
Gross margin = gross profit on sales/sales
EBITDA margin = EBITDA/sales
EBIT margin = EBIT/sales
Pre-tax margin = pre-tax profit/sales
Net margin = net profit/sales
ROE = net profit/average equity
ROA = (net income + interest payable)/average assets
EV = market capitalization + interest bearing debt – cash and equivalents
EPS = net profit/ no. of shares outstanding
CE = net profit + depreciation
Dividend yield (gross) = pre-tax DPS/stock market price
Cash sales = accrual sales corrected for the change in A/R
Cash operating expenses = accrual operating expenses corrected for the changes in inventories and A/P, depreciation, cash taxes and changes in the deferred taxes

DM IDM S.A. generally values the covered non bank companies via two methods: comparative method and DCF method (discounted cash flows). The advantage of the former is the fact that it incorporates the current market assessment of the value of the company's peers. The weakness of the comparative method is the risk that the valuation benchmark may be mispriced. The advantage of the DCF method is its independence from the current market valuation of the comparable companies. The weakness of this method is its high sensitivity to undertaken assumptions, especially those related to the residual value calculation. Please note that we also resort to other valuation techniques (e.g. NAV-, DDM- or SOTP-based), should it prove appropriate in a given case.

Banks

Net Interest Margin (NIM) = net interest income/average assets
NIM Adjusted = (net interest income adjusted for SWAPs)/average assets
Non interest income = fees&commissions + result on financial operations (trading gains) + FX gains
Interest Spread = (interest income/average interest earning assets)/ (interest cost/average interest bearing liabilities)
Cost/Income = (general costs + depreciation + other operating costs)/ (profit on banking activity + other operating income)
ROE = net profit/average equity
ROA = net income/average assets
Non performing loans (NPL) = loans in 'substandard', 'doubtful' and 'lost' categories
NPL coverrage ratio = loan loss provisions/NPL
Net provision charge = provisions created – provisions released

DM IDM S.A. generally values the covered banks via two methods: comparative method and fundamental target fair P/E and target fair P/BV multiples method. The advantage of the former is the fact that it incorporates the current market assessment of the value of the company's peers. The weakness of the comparative method is the risk that the valuation benchmark may be mispriced. The advantage of the fundamental target fair P/E and target fair P/BV multiples method is its independence of the current market valuation of the comparable companies. The weakness of this method is its high sensitivity to undertaken assumptions, especially those related to the residual value calculation.

Assumptions used in valuation can change, influencing thereby the level of the valuation. Among the most important assumptions are: GDP growth, forecasted level of inflation, changes in interest rates and currency prices, employment level and change in wages, demand on the analysed company products, raw material prices, competition, standing of the main customers and suppliers, legislation changes, etc.

Changes in the environment of the analysed company are monitored by analysts involved in the preparation of the recommendation, estimated, incorporated in valuation and published in the recommendation whenever needed.

KEY TO INVESTMENT RANKINGS

This is a guide to expected price performance in absolute terms over the next 12 months:
Buy – fundamentally undervalued (upside to 12M EFV in excess of the cost of equity) + catalysts which should close the valuation gap identified;
Hold – either (i) fairly priced, or (ii) fundamentally undervalued/overvalued but lacks catalysts which could close the valuation gap;
Sell – fundamentally overvalued (12M EFV < current share price + 1-year cost of equity) + catalysts which should close the valuation gap identified.

This is a guide to expected relative price performance:
Overweight – expected to perform better than the benchmark (WIG) over the next quarter in relative terms
Neutral – expected to perform in line with the benchmark (WIG) over the next quarter in relative terms
Underweight – expected to perform worse than the benchmark (WIG) over the next quarter in relative terms

The recommendation tracker presents the performance of DM IDMSA's recommendations. A recommendation expires on the day it is altered or on the day 12 months after its issuance, whichever comes first. Relative performance compares the rate of return on a given recommended stock in the period of the recommendation's validity (i.e. from the date of issuance to the date of alteration or – in case of maintained recommendations – from the date of issuance to the current date) in a relation to the rate of return on the benchmark in this time period. The WIG index constitutes the benchmark. For recommendations that expire by an alteration or are maintained, the ending values used to calculate their absolute and relative performance are: the stock closing price on the day the recommendation expires/ is maintained and the closing value of the benchmark on that date. For recommendations that expire via a passage of time, the ending values used to calculate their absolute and relative performance are: the average of the stock closing prices for the day the recommendation elapses and four directly preceding sessions and the average of the benchmark's closing values for the day the recommendation expires and four directly preceding sessions.

LT fundamental recommendation tracker

Recommendation	Issue date	Reiteration date	Expiry date	Performance	Relative performance	Price at issue/ reiteration (PLN)	12M EFV (PLN)
Energomontaż Południe							
Hold –	*01.12.2008*	-	*Not later than 01.12.2009*	-	-	2.36	3.4 –

Market-relative recommendation tracker

Relative recommendation	Issue date	Reiteration date	Expiry date	Price at issue/ reiteration (PLN)	Relative performance
Energomontaż Południe					
Neutral –	*01.12.2008*	-	*Not later than 01.12.2009*	2.36	-

Distribution of IDM's current recommendations

	Buy	Hold	Sell	Suspended	Under revision
Numbers	18	25	6	1	0
Percentage	36%	50%	12%	2%	0%

Distribution of IDM's current recommendations for companies that were within the last 12M IDM customers in investment banking

	Buy	Hold	Sell	Suspended	Under revision
Numbers	2	2	1	1	0
Percentage	33%	33%	17%	17%	0%

Distribution of IDM's current market relative recommended weightings

	Overweight	Neutral	Underweight	Suspended	Under revision
Numbers	19	13	17	1	0
Percentage	38%	26%	34%	2%	0%

Distribution of IDM's current market relative recommended weightings for the companies that were within the last 12M IDM customers in investment banking

	Overweight	Neutral	Underweight	Suspended	Under revision
Numbers	2	2	1	1	0
Percentage	33%	33%	17%	17%	0%

Institutional sales
Director – ***Dariusz Wareluk***
tel.: +48 (22) 489 94 12
d.wareluk@idmsa.pl

Leszek Mackiewicz
tel.: +48 (22) 489 94 23
l.mackiewicz@idmsa.pl

Maciej Bąk
tel.: +48 (22) 489 94 14
m.bak@idmsa.pl

Bartosz Zieliński
tel.: +48 (22) 489 94 13
b.zielinski@idmsa.pl

Research
***Sobiesław Pająk**, CFA*
(IT, Media, Equity strategy)
tel.: +48 (22) 489 94 70
s.pajak@idmsa.pl

***Sylwia Jaśkiewicz**, CFA*
(Construction materials, Retail, Mid-caps)
tel.: +48 (22) 489 94 78
s.jaskiewicz@idmsa.pl

Maciej Wewiórski
(Commodities, Construction, Real estate)
tel.: +48 (22) 489 94 62
m.wewiorski@idmsa.pl

Michał Sobolewski
(Banks)
tel.: +48 (22) 489 94 77
m.sobolewski@idmsa.pl

Jakub Viscardi
(Telco, Retail)
tel.: +48 (22) 489 94 69
j.viscardi@idmsa.pl

Adrian Kyrcz
(Construction)
tel.: +48 (22) 489 94 74
a.kyrcz@idmsa.pl

Łukasz Prokopiuk
(Associate)
tel.: +48 (22) 489 94 72
l.prokopiuk@idmsa.pl

Marek Kaźmierczak
(Associate)
tel.: +48 (22) 489 94 78
m.kazmierczak@idmsa.pl

Dom Maklerski IDMSA
Mały Rynek 7
31-041 Kraków

www.idmsa.pl
Information: (+48) 0 801 900 201