IDMSA DOM MAKLERSKI

Quarterly Results Review

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Energomontaż Południe

Sector: Construction
Fundamental rating: Buy (→)
Market relative: Overweight (→)
Price: PLN 3.59
12M EFV: PLN 5.0 (→)

Market Cap.: US$ 52 m
Reuters code: EMPD.WA
Av. daily turnover: US$ 0.04 m
Free float: 63%
12M range: PLN 1.86-3.69

- **1Q09 results – mixed.** Energomontaż Południe (EP) released its results for 1Q09 on May 14 (after the session). The numbers posted were mixed, with strong top line, operating profit below our forecast, and the bottom line fully in line with our projections (regarding the details please refer to *Figure 1* below).

Fig. 1 *Energomontaż Południe; 1Q09 results compared to expectations*

IFRS consolidated PLN m	1Q09A	1Q09E (IDM)	1Q09A vs. IDM	1Q08	yoy change
Sales	54.1	46.5	↑	39.2	38%
EBIT	1.5	3.7	↓	2.4	-37%
NI	0.6	0.6	→	0.5	12%

Source: Company, DM IDM estimates

- **Strong quarterly top line.** The Company's quarterly sales were strong and reached PLN 54.1 million, which marks 38% yoy increase and rests 16% above our expectation. The reason for such development was the expanding contract portfolio of EP. Please note that the Company positively surprised in recent times with its smooth foreign expansion and increased its backlog falling on 2009 up to PLN 303 million (which covers almost 100% of our FY09 sales forecast).

- **Quarterly operating profit – below the expectations.** Although EP increased yoy its quarterly gross profit on sales by as much as 80%, the operating profit declined yoy and amounted to PLN 1.5 million vs. our forecast of PLN 3.7 million. We see two reasons behind that. First, the Company recognized other net operating costs of PLN -1.6 million in 1Q09, which we clearly underestimated; please note that in 1Q09 the Company incurred costs of administration of the office building called 'Legnicka Park Popowice' (including one-off costs on arrangement of the office space for tenants), while it recognized only c. 40% of profits from the leasing agreements (the Company should recognize 100% of related profits beginning from 2Q09, after having completed the adaptation works). Furthermore, due to seasonal reasons, the product mix in 1Q09 was slightly less favorable than we assumed (the high margin assembly works should start already in 2Q09, favorably contributing to the Company's profit numbers, we believe).

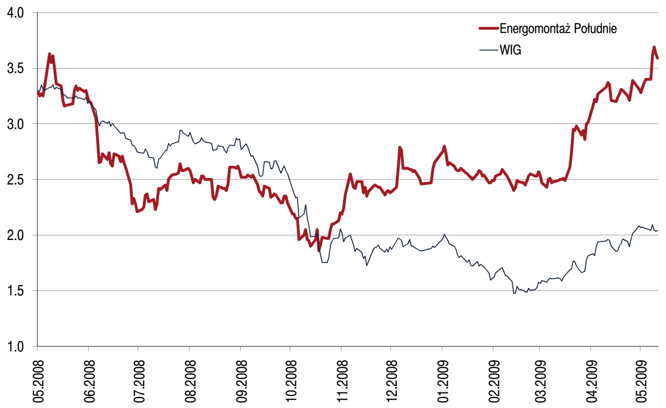
- **Quarterly net profit – fully in line with our projection.** The Company's quarterly pre-tax profit of PLN 1.5 million outperformed our forecast (PLN 0.8 million), as we underestimated translation gains (favorable impact of qoq appreciation of EUR vs. PLN). However, due to higher than envisaged effective CIT rate, the Company's 1Q09 net profit of PLN 0.6 million proved fully in line with our forecast.

Key data

IFRS consolidated		2008	2009E	2010E	2011E
Sales	*PLN m*	239.8	311.1	331.4	367.8
EBITDA	*PLN m*	29.8	36.3	37.9	38.8
EBIT	*PLN m*	25.3	31.4	32.4	32.6
Net profit	*PLN m*	15.6	16.8	19.6	22.0
EPS	*PLN*	0.33	0.35	0.41	0.46
EPS yoy chng	*%*	16	7	17	12
Net debt	*PLN m*	63.2	38.0	49.2	49.8
P/E	*x*	10.9	10.2	8.7	7.8
P/CE	*x*	8.5	8.0	6.9	6.2
EV/EBITDA	*x*	7.8	5.8	5.9	5.8
EV/EBIT	*x*	9.3	6.7	6.9	6.9
EV/Sales	*x*	1.0	0.7	0.7	0.6
Gross dividend yield	*%*	2.5	3.4	3.6	4.3
No. of shares (eop)	*ths.*	47,544	47,544	47,544	47,544

Source: Company, DM IDMSA estimates

Stock performance



Source: ISI

Upcoming events

1. Release of 1H09 results: August 31, 2009

Catalysts

1. Efficient expansion on the German market
2. Signing large contracts in the power segment
3. Synergies with Amontex

Risk factors

1. Delays in the start of the investments in the power sector in Poland
2. Falling prices of dwellings may entail fall of land prices
3. Possible lack of expected synergies with Amontex

- **Financial forecast – unaltered.** We do not change our financial forecast for EP. The Company should improve, we believe, its results in the following quarters, with the following arguments supporting this rationale: (i) dynamically improving backlog of high margin contracts thanks to smooth foreign expansion, (ii) improving management of large projects (which used to be a weakness of EP before the new team of project managers joined the Company in 1H08), and (iii) increasing profitability of the production division (which reached BEP in 2H08). Furthermore, positive impact on the Company's numbers should be exerted by decreasing construction costs as well as relatively weak Zloty (the Company only partially hedges its FX exposure). We expect all the above positive developments to shine from EP's financial results from 2Q09E onwards.

- **Valuation – unchanged.** Our 12M EFV for EP continues to dwell at PLN 5.0 per share.

- **Recommendations: Buy + Overweight.** We maintain our LT fundamental Buy recommendation and ST market-relative Overweight bias for EP's equities, due to: (i) material upside to our 12M EFV, (ii) expected healthy pace of results improvement in the coming quarters (secured by the German expansion) and years (on the back of local power sector investments launch in 2011E) and (iii) our conviction that EP constitutes a "forgotten" and out of favor company, which in case of its "re-discovery" by the market may present the investors with an appealing investment story**.**

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

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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*	-	*03.04.2009*	28%	30%	2.36	3.40	–
-	→	-	*09.01.2009*	-	-	-	2.65	4.00	↑
-	→	-	*11.01.2009*	-	-	-	2.65	4.00	→
-	→	-	*08.02.2009*	-	-	-	2.53	4.00	→
-	→	-	*08.03.2009*	-	-	-	2.47	4.00	→
Buy	↑	*03.04.2009*	-	*Not later than 03.04.2010*	19%	6%	3.01	5.00	↑
-	→	-	*05.04.2009*	-	-	-	3.01	5.00	→
-	→	-	*15.05.2009*	-	-	-	3.59	5.00	→

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	30%
-	→	-	*09.01.2009*	-	2.65	-
-	→	-	*11.01.2009*	-	2.65	-
-	→	-	*08.02.2009*	-	2.53	-
-	→	-	*08.03.2009*	-	2.47	-
Overweight	↑	*03.04.2009*	-	*Not later than 05.04.2010*	3.01	6%
-	→	-	*05.04.2009*	-	3.01	-
-	→	-	*15.05.2009*	-	3.59	-

Distribution of IDM's current recommendations

	Buy	Hold	Sell	Suspended	Under revision
Numbers	15	29	11	1	0
Percentage	27%	52%	20%	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	3	0	1	0
Percentage	33%	50%	0%	17%	0%

Distribution of IDM's current market relative recommended weightings

	Overweight	Neutral	Underweight	Suspended	Under revision
Numbers	19	15	21	1	0
Percentage	34%	27%	38%	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	1	2	2	1	0
Percentage	17%	33%	33%	17%	0%

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