

Tuesday, May 05, 2020 | Monthly Market Outlook, an excerpt

Cognor hold (no change)

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The coronavirus crisis is having an immense negative impact on the steel industry, creating a global glut, evidenced by growing stockpiles in China (currently close to 20mmt vs. a high of 15mmt recorded this week in the last five years). As rebar prices fall, so do the profit margins of steelmakers. In addition, in Q1 2020, electric arc furnaces (EAF) of the kind used by Cognor lost much of their previous cost advantage over basic oxygen furnaces (BOF). We currently expect Cognor to post a 9% decrease in sales in 2020 due to weaker demand, accompanied by a reduction in operating profit of PLN 138m, driven by lower sales prices. Further, with no state compensation offered this year for high electricity prices, expected to rise 7% relative to 2019, the Company faces additional costs of a projected PLN 17m. On the upside, Cognor might realize savings this year thanks to lower prices of graphite electrodes used in EAF steel making (PLN 60m), improved performance after capacity upgrades (PLN 31m), and lower costs of payroll and services incurred on lower sales (PLN 30m). Nevertheless we see FY2020 EBITDA as falling 30% to PLN 70m, resulting in a higher but still safe leverage ratio of 3.5x. Cognor will probably put shareholder distributions on hold for the foreseeable future. We maintain a hold for Cognor, with an unchanged target price of PLN 0.94 per share.

Financial Highlights

(PLN m)	2018	2019	2020P	2021P	2022P
Ferrostal volume (k tons)	401	424	371	456	502
HSJ volume (k tons)	237	237	228	250	255
Zlomrex volume (k tons)	173	142	145	148	151
Ferrostal spread (PLN/t)	1,191	1,127	1,107	1,126	1,140
HSJ spread (PLN/t)	1,723	1,508	1,255	1,266	1,279
Operating cash flow	232	142	48	66	62
D&A	44	46	48	47	45
Working capital	44	61	-21	0	-1
Investing cash flow	-38	-56	-50	-33	-35
CAPEX	38	56	50	33	35
Financing cash flow	-196	-84	-24	-20	-20
Dividends/Buyback	-12	-36	0	0	0
FCF	179	102	-1	34	29
FCF/EBITDA	90%	101%	-1%	50%	45%
OCF/EBITDA	116%	141%	69%	98%	97%

DCF Analysis

(PLN m)	20P	21P	22P	23P	24P	25P	26P	27P	28P	29P	+
Sales volume	599	706	757	787	813	828	843	845	846	846	846
Product prices	1,956.2	1,940.5	1,956.5	1,970.3	1,982.9	1,992.9	2,002.8	2,012.4	2,022.1	2,029.5	2,037.0
Scrap prices	1,040	1,008	1,008	1,008	1,008	1,008	1,008	1,008	1,008	1,008	1,008
Revenue	1,630	1,828	1,944	2,019	2,085	2,128	2,171	2,186	2,202	2,212	2,223
EBITDA	70	67	64	80	76	72	72	72	74	72	70
EBITDA margin	4.3%	3.7%	3.3%	3.9%	3.7%	3.4%	3.3%	3.3%	3.3%	3.2%	3.1%
EBIT	22	20	19	36	34	30	29	29	30	28	26
Tax	0	0	0	3	3	2	2	2	2	2	1
CAPEX	-50	-33	-35	-35	-36	-38	-40	-43	-43	-43	-43
Working capital	-21	0	-1	-3	-3	-2	-2	-1	-1	0	0
FCF	-1	34	29	38	34	31	29	27	28	27	25
PV FCF	-1	30	24	29	25	21	18	16	16	14	
WACC	6.7%	6.8%	6.8%	6.9%	6.9%	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%
Risk-free rate	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%	3.5%

Current Price 0.91 PLN **Upside**
9M Target Price 0.94 PLN **+3.3%**

	rating	target price	issued
unchanged	hold	0.94 PLN	2020-04-22

Key Metrics			COG PW	vs. WIG
Ticker	COG PW	1M Price Chng	+11.2%	+2.8%
ISIN	PLCNTSL00014	YTD Price Chng	-26.6%	-4.5%
Outst. Stock (m)	175.0	ADTV 1M		PLN 0.1m
MC (PLN m)	159.2	ADTV 6M		PLN 0.1m
EV (PLN m)	403.5	EV/EBITDA 12M fwd	5.2	+34.7%
Free Float	-	EV/EBITDA 5Y avg	3.8	premium

Earnings Projections

(PLN m)	2017	2018	2019	2020P	2021P
Revenue	1,902	2,082	1,902	1,630	1,828
EBITDA adj.	146	200	93	70	67
EBITDA margin	7.7%	9.6%	4.9%	4.3%	3.7%
EBIT adj.	104	156	47	22	20
Net income adj.	32	94	11	2	0
P/E adj.	5.0	1.7	14.2	75.9	322.4
P/B	0.7	0.6	0.6	0.6	0.6
EV/EBITDA adj.	3.4	1.9	4.3	6.1	6.1
DPS	0.00	0.07	0.21	0.00	0.00
DYield	0.0%	7.4%	22.6%	0.0%	0.0%
Forecast Update (% change)			2019	2020P	2021P
Revenue			0.0%	0.0%	0.0%
EBITDA			0.0%	0.0%	0.0%
Net income			0.0%	0.0%	0.0%
Sales volume			0.0%	0.0%	0.0%
Product prices			0.0%	0.0%	0.0%
Scrap prices			0.0%	0.0%	0.0%

Key Balance Sheet Figures

(PLN m)	2018	2019	2020P	2021P	2022P
Assets	1,001	1,052	950	992	1,016
Fixed assets	379	487	481	459	445
Equity	278	259	261	261	261
Minority interests	278	259	261	261	261
Net debt	209	226	247	234	226
Net debt/EBITDA (x)	1.0	2.2	3.5	3.5	3.5
Net debt/Equity (x)	0.8	0.9	0.9	0.9	0.9

Relative Valuation Summary

	P/E			EV/EBITDA		
	19P	20P	21P	19P	20P	21P
Minimum	2.6	4.6	4.1	3.7	1.2	0.7
Maximum	42.8	25.5	365.2	8.7	22.6	9.5
Median	8.1	12.0	10.5	5.2	7.4	6.0
Weight	0%	25%	25%	0%	25%	25%

DCF Summary

(PLN m)	
Beta	1.2
FCF perp. growth rate	2.0%
PV FCF	192
Net debt	262
Other adj.	18
Value per share (PLN)	0.96

Valuation Summary

(PLN)	Weight	Price
Relative Val.	50%	0.53
DCF Val.	50%	0.96
Implied Price		0.88
Cost of equity (9M)		7.0%
9M Target Price		0.94

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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HOLD – we expect that the rate of return from an investment will range from -5% to +5%
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mBank issued the following investment recommendations for the Company in the 12 months prior to this publication
Cognor

Rating	hold	hold	hold	hold	accumulate	hold	accumulate	accumulate	overweight	neutral
Rating date	2020-04-22	2019-12-06	2019-12-05	2019-11-04	2019-09-05	2019-07-25	2019-07-03	2019-06-14	2019-06-03	2019-05-09
Target price (PLN)	0.94	1.25	1.25	1.55	2.00	1.84	1.84	1.79	-	-
Price on rating day	0.95	1.20	1.17	1.52	1.65	1.75	1.77	1.64	1.60	1.59

Comparable Companies Used In Relative Valuation Models
Cognor

AK Steel, Alumental, ArcelorMittal, Baoshan Iron & Steel, Commercial Metals, HeSteel, Hitachi Metals, Hyundai Steel, JFE Holdings, JSW Steel, Kloeckner & Co, Metalurgica Gerdau, Nippon Yakin Kogyo, Nucor, Olympic Steel, Outokumpu, POSCO, Salzgitter, SSAB, Steel Authority Of India, Steel Dynamics, Tata Steel, thyssenkrupp, United States Steel Corp, voestalpine

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