

Monday, 6 September 2021 | research report

## Pozbud: hold (new)

POZ PW; POZP.WA | Industrials, Poland

### Diversification as the Way Forward

After a fundamental ownership change in 2020, Pozbud at the moment is taking steps to transform into a diversified holding company. As part of its transformation, Pozbud is venturing out into development and operation of renewable energy systems with a portfolio of 460MW of photovoltaic (PV) and wind farm projects expected to bring in up to PLN 140 million in additional sales from 2024. Pozbud is in talks to onboard an international partner for the RES projects that can bring in the right credentials, technology, and access to new solutions.

Another area where Pozbud recently established a presence is rolling stock maintenance; the Company, along with consortium partner Mag-Train, secured winning bids on two assignments for Poland's intercity train operator, PKP Intercity, with a total value of PLN 594m; the first PLN 70.6m contract is likely to be signed in September, and the bigger, PLN 391.7m booking should be finalized later in the year. In the meantime Pozbud's railway services arm is working on a lucrative GSM-for-Railways (GSM-R) project with at least two-plus more years still left and a remaining revenue of PLN 420m. The plan after the GSM-R job is completed is to return to vying for fiber-optic and other infrastructure jobs for the Polish railways.

In the third major line of business of windows and doors, Pozbud is hoping to leverage Poland's current housing boom to bring annual sales to PLN 100m by 2025 from PLN 28m generated in 2020.

With these initiatives underway, we see Pozbud as being well on track to doubling sales and significantly increasing profits in the next five years.

Using relative valuation and DCF analysis, we initiate coverage of Pozbud with a target price of PLN 5.24 and a hold recommendation.

#### Growth powered by clean energy

Pozbud is currently running feasibility assessments for eight renewable energy projects (solar, wind, and hybrid systems) with a combined capacity of 460 MW. The business model for the RES line of business is to offer turnkey solutions for own needs and to investors, including long-term quality and efficiency management. Pozbud hopes to break ground of the first of these projects by early 2022, and see its first revenue towards the end of that year.

#### Opportunities in rolling stock services

Poland could put into motion a number of major railway infrastructure projects in the near future with funding from Next Generation EU and from the PM-led "New Deal" national recovery program. The Polish long-distance train operator, PKP Intercity, is known to be planning to invest PLN 19bn in rolling stock by 2030. Competition in the Polish market for rolling stock maintenance services is limited, and the market is divided between three major players, one of whom is Pozbud's business partner, Mag-Train.

#### GSM-R and post-project maintenance

The GSM-R agreement offers an option for Pozbud to accept PLN 100m five-year post-contract network maintenance services. With the resources currently tied up in GSM-R, in the future Pozbud plans to go back to bidding for new assignments from the railway sector. It is worth noting that the lead partner in GSM-R, Nokia, has a stake in Nexera, the Polish NGA network operator that in July 2021 secured PLN 1bn financing to build fiber to the home for another 1 million Polish households.

(PLN m)	2019	2020	2021E	2022E	2023E
revenue	197	194	220	338	417
EBITDA (adj.)	37	51	37	44	53
EBITDA margin	18.8%	26.1%	16.7%	13.1%	12.8%
EBIT (adj.)	30	42	28	36	45
net profit (adj.)	16	25	20	23	29
P/E (adj.)	8.5	9.3	11.5	9.9	7.9
P/FCFE	24.5	7.0	7.7	-12.2	9.3
FCFF/EV	4.2%	11.3%	11.4%	-4.5%	8.2%
EV/EBITDA (adj.)	5.5	5.9	7.6	7.2	5.9
DPS	0.00	0.00	0.00	0.00	0.13
DYield	0.0%	0.0%	0.0%	0.0%	2.5%

current price	PLN 5.16
target price	PLN 5.24
mCap	PLN 231m
free float	PLN 73m
ADTV (3m)	PLN 0.7m

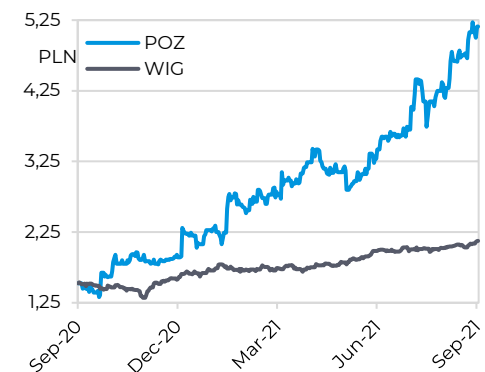
#### Shareholders

Łukasz Fojt	26.6%
Andrzej Raubo	25.3%
NN OFE	16.6%
others	31.5%

#### About

Pozbud is a holding company based in Poznań whose business activity includes production of wooden windows, building and infrastructure, housing development, rolling stock services, and development of solar photovoltaic power plants. At the moment Pozbud is involved in a PLN 720m multi-year GSM-R assignment.

#### POZ vs. WIG



company	target price		recommendation	
	new	old	new	old
Pozbud	5.24	-	hold	-

security	current price	target price	upside
	Pozbud	5.16	5.24

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## Key Risks

### Housing slump

Sales of windows and doors rely closely on the situation in the housing market. As of this writing, new home starts in Poland are rising rapidly amid low interest rates, but any slowdown in the future could dampen demand for windows. This applies in particular to the new development projects that the Company is currently focusing on as part of the growth strategy of the wood windows factory in Słonawy near Poznań. To counteract revenue risk, Pozbud is working to expand its windows business outside of Poland, including by working closely with a partner from the US.

### High costs of materials and labor

Pozbud's profit margins can suffer any time there is an upward trend in costs of timber and other material needed for windowmaking. The risk of losses is mitigated by the fact that the Company targets its windows at the more upmarket clientele.

An increase in costs of materials and services can also affect profits in the other lines of Pozbud's business, including construction services, RES development, and rolling stock services.

### Loss of EU funding

Pozbud's railway arm takes part in many projects funded by the European Union, giving rise to risk of reduced orders if Poland becomes cut off from funding over Community law violations.

### Increase in Labor Costs

The average monthly pay of a Pozbud employee was PLN 3,500-3,800 in the 2017-2018 period, and by 2020 it increased to PLN 7,100. However even after such a rapid rise Pozbud's rates are far from being the highest in the Polish industrial sector. Intensifying pay pressures give rise to risk of higher labor costs in the future.

### Changes in renewable energy regulations

The development of renewable energy sources in recent years has benefitted from generous public funding and a favorable regulatory environment, but if there is a negative shift in policy business conditions could worsen.

Further, as more new companies enter the market, the field of solar and wind farm development is becoming increasingly competitive, giving rise to risk of squeezed profit margins in the future.

Another risk involved in RES development is associated with a need to obtain feed-in permits and other kinds of administrative clearance.

Further, the development of a PV plant requires large funds that remain tied up in working capital for up to a year from the time the plant is sold. As a newcomer to the RES market, Pozbud could face challenges in securing financing from lending institutions, and in case of funding secured from other sources it might have to give up a part of its profits to the financing provider.

Access to financing could also become more difficult for RES companies depending sentiment among equity investors. In order to reduce these risks, Pozbud allows for the possibility of selling some of the projects at the pre-development stage.

### Reduced profits from GSM-R contract

The GSM-R contract to date has generated gross margins over 20% for Pozbud, and it has become the Company's primary earnings driver. That creates major risk to future profits if the margins on the contract should decline.

For now, Pozbud is not seeing any signs of such margin contraction and works is going according to schedule. However under the contract's joint-and-several liability clause all partners in the contract could face financial penalties if one of them violates terms. The customer entity of GSM-R, the railway operator PKP PLK, could contribute to such violations if it delays access to new sites and the next stretches of land for laying ductways.

### Revenue reduction post GSM-R

The GSM-R project is the biggest initiative of this kind in Poland at the moment, and there are no future plans for new ventures on a similar scale. Pozbud is preparing to vie for FTTH infrastructure projects after 2023, and it plans to establish a partnership with a company involved in railway services to improve its success rate in future tenders.

### FX risk

Pozbud is working to increase sales of its windows in the United States and in Western Europe, where it is common practice to choose suppliers based on price. Because of this, Pozbud's future international expansion could be slowed if the zloty appreciates in value relative to the euro.

### Corporate governance risk

In 2020, Pozbud conducted a shareholder-mandated capital raise and merged with its business partner, Agnes, which acquired shares in Pozbud at an attractive price that proved controversial among the minority shareholders of Pozbud. Similar controversy might arise if Pozbud repeats this practice in the future to gain a foothold in other targeted industries.

## Valuation

Using DCF analysis and relative valuation, we set our nine-month per-share price target for Pozbud at PLN 5.24.

### Valuation summary

(PLN)	weight	price
relative valuation	50%	4.57
discounted cash flow	50%	5.19
	valuation	4.88
	<b>9M target price</b>	<b>5.24</b>

Source: mBank

## Multiples Comparison

We compared Pozbud with a group of comparable Polish companies from the industrial sector. The peer group for now excludes rolling stock repairers and RES developers due to the fact that Pozbud is in early stages

of diversifying into these markets. We assign a 10% discount to our final valuation of Pozbud to reflect corporate the governance risk described above.

### Multiples Comparison

	P/E			EV/EBITDA		
	2021E	2022E	2023E	2021E	2022E	2023E
FABRYKI MEBLI FORTE SA	11.3	10.4	12.1	8.0	7.5	8.0
GRUPA KETY SA	12.7	13.8	13.2	9.1	9.8	9.4
STALPRODUKT SA	7.3	10.4	10.7	3.3	3.3	3.1
ALUMETAL SA	7.0	10.4	9.8	6.6	8.2	6.6
WIELTON SA	11.0	8.6	8.6	6.8	5.8	5.4
MANGATA HOLDING SA	10.4	9.8	8.0	7.4	6.6	6.0
AMICA SA	10.9	14.8	13.4	5.5	5.8	5.4
BORYSZEW SA	22.4	14.9	12.3	7.1	6.2	5.4
FAMUR SA	11.1	12.2	12.8	3.1	3.7	3.5
NEWAG SA	7.9	9.6	11.0	5.0	3.9	4.1
FERRO SA	8.4	10.1	9.3	9.3	7.6	7.5
COGNOR SA	4.0	7.8	8.4	2.9	4.6	4.9
PKP CARGO SA	-	-	6.1	-	-	-
maximum	4.0	7.8	6.1	2.9	3.3	3.1
minimum	22.4	14.9	13.4	9.3	9.8	9.4
<b>median</b>	<b>10.6</b>	<b>10.4</b>	<b>10.7</b>	<b>6.7</b>	<b>6.0</b>	<b>5.4</b>
Pozbud	11.5	9.9	7.9	7.6	7.2	5.9
premium / discount	7.9%	-5.2%	-26.0%	14.0%	20.2%	8.5%

### Implied valuation of Pozbud

median	10.6	10.4	10.7	6.7	6.0	5.4
premium / discount	10%	10%	10%	10%	10%	10%
multiple weight		50%			50%	
year weight	33%	33%	33%	33%	33%	33%
<b>equity value per share (PLN)</b>	<b>4.57</b>					

Source: mBank

## DCF Valuation

### Assumptions:

- Beta = 1.3, reflecting risks involved in Pozbud's diversification into new, unchartered markets.
- Cash flow is discounted as of late August 2021.
- Net debt is as at year-end 2020

### DCF Model

(PLN m)	2021E	2022E	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E	+
<b>revenue</b>	<b>220.0</b>	<b>337.8</b>	<b>417.0</b>	<b>416.8</b>	<b>444.0</b>	<b>446.0</b>	<b>448.0</b>	<b>450.1</b>	<b>452.2</b>	<b>454.4</b>	<b>456.6</b>
change	13.6%	53.5%	23.5%	0.0%	6.5%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%
<b>EBITDA</b>	<b>36.8</b>	<b>44.2</b>	<b>53.5</b>	<b>47.5</b>	<b>51.5</b>	<b>51.7</b>	<b>51.9</b>	<b>52.0</b>	<b>52.2</b>	<b>52.5</b>	<b>50.6</b>
EBITDA margin	16.7%	13.1%	12.8%	11.4%	11.6%	11.6%	11.6%	11.6%	11.6%	11.5%	11.1%
D&A expenses	8.5	8.3	8.3	8.1	7.9	7.8	7.6	7.5	7.3	7.2	5.0
<b>EBIT</b>	<b>28.3</b>	<b>35.8</b>	<b>45.2</b>	<b>39.4</b>	<b>43.6</b>	<b>43.9</b>	<b>44.2</b>	<b>44.6</b>	<b>44.9</b>	<b>45.2</b>	<b>45.6</b>
EBIT margin	12.9%	10.6%	10.8%	9.5%	9.8%	9.8%	9.9%	9.9%	9.9%	10.0%	10.0%
tax on EBIT	5.0	6.5	8.2	7.1	7.9	8.0	8.1	8.2	8.4	8.5	8.5
<b>NOPLAT</b>	<b>23.3</b>	<b>29.4</b>	<b>37.0</b>	<b>32.3</b>	<b>35.7</b>	<b>35.9</b>	<b>36.2</b>	<b>36.4</b>	<b>36.5</b>	<b>36.7</b>	<b>37.1</b>
CAPEX	-5.0	-8.0	-5.0	-5.0	-5.0	-5.0	-5.0	-5.0	-5.0	-5.0	-5.0
working capital	-4.7	-60.1	-24.5	-33.6	-34.3	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
<b>FCF</b>	<b>22.1</b>	<b>-30.4</b>	<b>15.8</b>	<b>1.9</b>	<b>4.3</b>	<b>38.6</b>	<b>38.6</b>	<b>38.7</b>	<b>38.7</b>	<b>38.8</b>	<b>37.0</b>
WACC	9.1%	8.7%	8.8%	8.6%	8.6%	8.8%	9.1%	9.5%	9.9%	10.0%	10.0%
discount factor	1.0	0.9	0.8	0.8	0.7	0.6	0.6	0.5	0.5	0.4	0.4
PV FCF	21.5	-27.2	13.0	1.4	3.0	24.5	22.2	19.9	17.6	15.9	13.8
	0.33	1.33	2.33	3.33	4.33	5.33	6.33	7.33	8.33	9.33	10.33
<b>WACC</b>	<b>9.1%</b>	<b>8.7%</b>	<b>8.8%</b>	<b>8.6%</b>	<b>8.6%</b>	<b>8.8%</b>	<b>9.1%</b>	<b>9.5%</b>	<b>9.9%</b>	<b>10.0%</b>	<b>10.0%</b>
cost of debt	6.50%	6.50%	6.50%	6.50%	6.50%	6.50%	6.50%	6.50%	6.50%	6.50%	6.50%
risk-free rate	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%	3.50%
risk premium	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
effective tax rate	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%
net debt / EV	18.1%	27.1%	25.7%	28.3%	30.0%	24.2%	18.0%	10.6%	1.8%	0.0%	0.0%
cost of equity	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%
risk premium	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
beta	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3	1.3

FCF growth after the forecast period	2.0%
terminal value	462.1
present value of terminal value	189.9
present value of FCF in the forecast period	111.9
enterprise value	301.7
net debt	69.2
minority interest	0.0
equity value	232.6
shares outstanding (millions)	44.8
<b>equity value per share (PLN)</b>	<b>5.2</b>
9M cost of equity	7.4%
<b>target price (PLN)</b>	<b>5.6</b>

EV/EBITDA ('22) at target price	7.6
P/E('22) at target price	10.7
TV / EV	62.9%

Source: mBank

### sensitivity analysis

	FCF growth in perpetuity				
	0.0%	1.0%	2.0%	3.0%	5.0%
WACC +1.0 p.p.	3.9	4.2	4.6	5.0	6.4
WACC +0.5 p.p.	4.3	4.6	5.0	5.6	7.3
WACC	4.7	5.1	<b>5.6</b>	6.2	8.3
WACC -0.5 p.p.	5.1	5.6	6.2	6.9	9.5
WACC -1.0 p.p.	5.6	6.1	6.8	7.8	11.1

<b>P&amp;L</b>						<b>Cash Flow</b>					
<b>(PLN m)</b>	<b>2019</b>	<b>2020</b>	<b>2021E</b>	<b>2022E</b>	<b>2023E</b>	<b>(PLN m)</b>	<b>2019</b>	<b>2020</b>	<b>2021E</b>	<b>2022E</b>	<b>2023E</b>
<b>revenues</b>	<b>197</b>	<b>194</b>	<b>220</b>	<b>338</b>	<b>417</b>	<b>operating CF</b>	<b>6</b>	<b>33</b>	<b>27</b>	<b>-22</b>	<b>21</b>
windows	58	28	45	60	75	working capital	-26	-16	-5	-60	-24
real estate development	29	7	5	0	0	<b>investing CF</b>	<b>-7</b>	<b>-1</b>	<b>-5</b>	<b>-8</b>	<b>-5</b>
construction	110	159	170	190	180	CAPEX	-3	-1	-5	-8	-5
GSM-R	96	83	150	170	150	<b>financing CF</b>	<b>-20</b>	<b>-8</b>	<b>-24</b>	<b>7</b>	<b>-10</b>
floors	0	0	0	0	0	dividend	0	0	0	0	-6
RES	0	0	0	64	90	<b>CF</b>	<b>-22</b>	<b>24</b>	<b>-2</b>	<b>-24</b>	<b>6</b>
railway services	0	0	0	24	72	OCF/EBITDA	15%	65%	74%	-51%	39%
<b>pre-tax profit</b>	<b>38</b>	<b>56</b>	<b>41</b>	<b>50</b>	<b>60</b>	FCFF	8	34	32	-14	26
windows	7	-6	9	13	17	<b>FCFF/EV</b>	<b>4%</b>	<b>11%</b>	<b>11%</b>	<b>-5%</b>	<b>8%</b>
real estate development	6	2	2	0	0	FCFE	6	33	30	-19	25
construction	25	60	31	29	27	<b>FCFE/MCAP</b>	<b>4%</b>	<b>14%</b>	<b>13%</b>	<b>-8%</b>	<b>11%</b>
floors	0	0	0	0	0	ROIC	7.5%	12.7%	7.3%	8.5%	9.6%
RES	0	0	0	6	9	ROCE growth	11.2%	18.8%	9.7%	11.4%	13.5%
railway services	0	0	0	2	8	DPS	0.00	0.00	0.00	0.00	0.13
EBIT	25	47	28	36	45	divid. payout ratio	0.0%	0.0%	0.0%	0.0%	25.0%
financing activity	-8	-5	-3	-3	-4	<b>dividend yield</b>	<b>0.0%</b>	<b>0.0%</b>	<b>0.0%</b>	<b>0.0%</b>	<b>2.5%</b>
pre-tax profit	16	40	25	32	41	<b>Key Ratios</b>					
income tax	5	11	5	6	8		<b>2019</b>	<b>2020</b>	<b>2021E</b>	<b>2022E</b>	<b>2023E</b>
minority interest	0	0	0	3	4	P/E	11.7	8.0	11.5	9.9	7.9
net profit	12	29	20	23	29	<b>P/E (adj.)</b>	<b>8.5</b>	<b>9.3</b>	<b>11.5</b>	<b>9.9</b>	<b>7.9</b>
<b>EBITDA (adj.)</b>	<b>37</b>	<b>51</b>	<b>37</b>	<b>44</b>	<b>53</b>	EV/EBITDA	6.4	5.4	7.6	7.2	5.9
<b>net profit (adj.)</b>	<b>16</b>	<b>25</b>	<b>20</b>	<b>23</b>	<b>29</b>	<b>EV/EBITDA (adj.)</b>	<b>5.5</b>	<b>5.9</b>	<b>7.6</b>	<b>7.2</b>	<b>5.9</b>
						P/S	0.7	1.2	1.1	0.7	0.6
						P/B	0.9	1.0	1.0	0.9	0.8
						P/CF	24.5	7.0	8.5	-10.3	11.1
						P/FCFE	24.5	7.0	7.7	-12.2	9.3
						<b>EBITDA margin</b>	<b>18.8%</b>	<b>26.1%</b>	<b>16.7%</b>	<b>13.1%</b>	<b>12.8%</b>
						y/y % EBITDA change	70%	75%	-33%	20%	21%
						net margin	8.3%	12.9%	9.2%	6.9%	7.0%
						<b>y/y % EPS change</b>	<b>58%</b>	<b>45%</b>	<b>-30%</b>	<b>16%</b>	<b>25%</b>
						price (PLN)	5.16	5.16	5.16	5.16	5.16
						shares outst. (millions)	26.8	44.8	44.8	44.8	44.8
						mCap	138	231	231	231	231
						EV	203	301	282	318	316

Source: mBank



#### List of abbreviations and ratios used by mBank:

**EV** (Enterprise Value) – Equity Value + Net Debt; **EBIT** – Earnings Before Interest and Taxes; **EBITDA** – EBIT + Depreciation & Amortisation; **Net Debt** – Borrowings + Debt Securities + Interest-Bearing Loans - Cash and Cash Equivalents; **P/E** (Price/Earnings) – Price Per Share Divided by Earnings Per Share; **P/CE** (Price to Cash Earnings) – Price Per Share Divided by Earnings + Depreciation & Amortisation; **P/B** (Price to Book Value) – Price Per Share Divided by Book Value Per Share; **P/CF** (Price to Cash Flow) – Price Divided by Cash Flow from Operations; **ROE** (Return on Equity) – Earnings Divided by Shareholders' Equity; **ROCE** (Return on Capital Employed) – EBIT x (Average Assets - Current Liabilities); **ROIC** (Return on Invested Capital) – EBIT x (1-Tax Rate) / (Average Equity + Minority Interest + Net Debt); **FCFF** (Free Cash Flow to Firm) – Cash Flow from Operations - CAPEX - Lease Payments; **FCFE** (Free Cash Flow to Equity) – Free Cash Flow to Firm - Net Interest Expense (incl. Debt + Leases) - Lease Payments  
**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

#### Recommendations of Biuro maklerskie mBanku:

A recommendation is valid for a period of 9 months, unless a subsequent recommendation is issued in this period. Expected returns from individual recommendations are as follows:

**BUY** – we expect that the rate of return from an investment will be at least 15%  
**ACCUMULATE** – we expect that the rate of return from an investment will range from 5% to 15%  
**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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#### mBank issued the following recommendations for Pozbud in the 12 months prior to this publication:

##### Pozbud

recommendation	suspended	neutral
date issued	2020-12-08	2020-09-30
target price (PLN)	-	-
price on rating day	1.91	1.65

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