

Thursday, November 05, 2020 | Monthly Market Outlook, an excerpt

Cognor buy (no change)

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The negative effects of the coronavirus epidemic on the steel industry have been less damaging to Cognor and other producers using electric arc furnace (EAF) technology because they have the ability to adjust production more flexibly than BOF steelmakers, plus their long steel products, which are used mostly for construction, remain more in demand. Cognor generated better-than-expected financial results in Q3 2020, supported by government stimulus and lower losses on inventory adjustments and plant maintenance costs than incurred in the same period a year earlier. Operating cash flow in Q3 2020 was similar to the OCF generated the year before, facilitating further reduction in net debt. In Q4 2020 Cognor is guiding for higher profits than in Q4 2020 and a small improvement relative to the quarter before, indicating a potential positive surprise in the earnings results for the full year. According to our estimates Cognor will keep the net debt/EBITDA ratio at 2.1x for the year, a level which would allow it to resume paying dividends again in 2021, offering dividend yield as high as 10% (adjusted for dilution). We maintain a buy rating for COG.

Current Price	1.15 PLN	Upside
9M Target Price	2.03 PLN	+77.3%

	rating	target price	issued
unchanged	buy	2.03 PLN	2020-09-25

Key Metrics			COG PW	vs. WIG
Ticker	COG PW	1M Price Chng	-8.4%	-4.8%
ISIN	PLCNTSL00014	YTD Price Chng	-7.7%	+10.6%
Outst. Stock (m)	175.0	ADTV 1M		PLN 0.1m
MC (PLN m)	200.3	ADTV 6M		PLN 0.1m
EV (PLN m)	437.8	EV/EBITDA 12M fwd	3.2	-14.6%
Free Float	-	EV/EBITDA 5Y avg	3.7	discount

Earnings Projections

(PLN m)	2018	2019	2020P	2021P	2022P
Revenue	2,082	1,902	1,696	1,873	1,969
EBITDA adj.	200	93	107	93	89
EBITDA margin	9.6%	4.9%	6.3%	5.0%	4.5%
EBIT adj.	156	47	59	46	44
Net income adj.	69	19	32	22	20
P/E adj.	2.9	10.5	6.3	9.2	10.2
P/B	0.7	0.8	0.7	0.7	0.7
EV/EBITDA adj.	2.1	4.8	4.1	4.5	4.6
DPS	0.07	0.21	0.00	0.11	0.09
DYield	5.9%	18.0%	0.0%	9.6%	7.6%

Forecast Update (% change)	2020P	2021P	2022P
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%

Financial Highlights

(PLN m)	2018	2019	2020P	2021P	2022P
Ferrostal volume (k tons)	401	424	399	470	505
HSJ volume (k tons)	237	237	213	223	228
Zlomrex volume (k tons)	173	142	130	137	140
Ferrostal spread (PLN/t)	1,191	1,127	1,121	1,131	1,145
HSJ spread (PLN/t)	1,723	1,508	1,423	1,490	1,506
Operating cash flow	232	142	76	88	83
D&A	44	46	48	47	45
Working capital	44	61	-22	1	0
Investing cash flow	-38	-56	-50	-33	-35
CAPEX	38	56	50	33	35
Financing cash flow	-196	-84	-24	-39	-35
Dividends/Buyback	-12	-36	0	-19	-15
FCF	179	102	27	56	50
FCF/EBITDA	90%	101%	25%	60%	56%
OCF/EBITDA	116%	141%	71%	95%	94%

Key Balance Sheet Figures

(PLN m)	2018	2019	2020P	2021P	2022P
Assets	1,001	1,052	995	1,035	1,060
Fixed assets	379	487	481	459	445
Equity	278	259	291	293	298
Minority interests	278	259	291	293	298
Net debt	209	226	219	203	189
Net debt/EBITDA (x)	1.0	2.2	2.1	2.2	2.1
Net debt/Equity (x)	0.8	0.9	0.8	0.7	0.6

Relative Valuation Summary

	P/E			EV/EBITDA		
	20P	21P	22P	20P	21P	22P
Minimum	1.1	6.9	5.2	2.0	1.0	1.1
Maximum	22.9	100.4	34.9	64.8	15.5	8.6
Median	13.6	12.9	9.5	8.4	5.9	5.5
Weight	17%	17%	17%	17%	17%	17%

DCF Analysis

(PLN m)	20P	21P	22P	23P	24P	25P	26P	27P	28P	29P	+
Sales volume	612	693	733	756	776	790	804	806	808	808	808
Product prices	2,045	2,054	2,067	2,080	2,092	2,103	2,113	2,123	2,133	2,141	2,149
Scrap prices	1,027	1,008	1,008	1,008	1,008	1,008	1,008	1,008	1,008	1,008	1,008
Revenue	1,696	1,873	1,969	2,030	2,087	2,129	2,172	2,187	2,203	2,213	2,224
EBITDA	107	93	89	103	99	94	93	92	92	88	85
EBITDA margin	6.3%	5.0%	4.5%	5.1%	4.7%	4.4%	4.3%	4.2%	4.2%	4.0%	3.8%
EBIT	59	46	44	59	56	52	50	48	48	44	41
Tax	7	5	5	8	7	6	6	5	5	5	4
CAPEX	-50	-33	-35	-35	-36	-38	-40	-43	-43	-43	-43
Working capital	-22	1	0	-3	-3	-2	-2	-1	-1	0	0
FCF	27	56	50	57	53	49	46	43	43	40	37
PV FCF	27	52	43	46	39	33	29	25	23	20	
WACC	7.1%	7.2%	7.3%	7.5%	7.5%	7.6%	7.7%	7.7%	7.8%	7.8%	7.8%
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%

DCF Summary

(PLN m)	
Beta	1.2
FCF perp. growth rate	2.0%
PV FCF	337
Net debt	262
Other adj.	18
Value per share (PLN)	2.17

Valuation Summary

(PLN)	Weight	Price
Relative Val.	50%	1.61
DCF Val.	50%	2.17
Implied Price		1.89
Cost of equity (9M)		7.2%
9M Target Price		2.03

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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Relative – based on a comparison of valuation multipliers of companies from a given sector; simple in construction, reflects the current state of the market better than DCF; weak points include substantial variability (fluctuations together with market indices) as well as difficulty in the selection of the group of comparable companies.

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Discounted Dividends (DDM) – discounting of future dividends; the weak point is high sensitivity to changes in the assumptions as to future dividends made in the valuation model.

NAV - valuation based on equity value, one of the most frequently used method in case of developing companies; the weak point of the method is that it does not factor in future changes in revenue/profits of a company.

mBank issued the following investment recommendations for the Company in the 12 months prior to this publication

Rating	buy	buy	hold	hold	hold	hold
Rating date	2020-09-25	2020-08-04	2020-04-22	2019-12-06	2019-12-05	2019-11-04
Target price (PLN)	2.03	1.98	0.94	1.25	1.25	1.55
Price on rating day	1.10	0.93	0.95	1.20	1.17	1.52

Comparable Companies Used In Relative Valuation Models

Cognor AK Steel, Alumetal, 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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