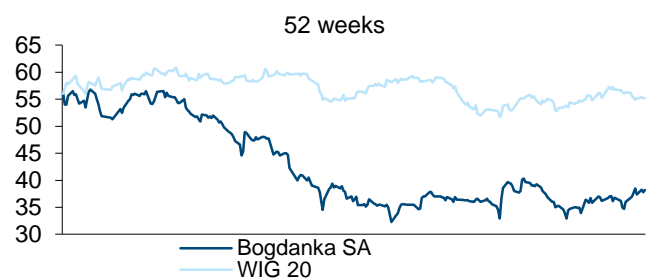


# Bogdanka SA

from Hold to Buy

PLN mn	2019e	2020e	2021e	2022e
Net sales	2 207.5	2 242.8	2 041.0	2 061.6
EBITDA	834.9	791.8	585.8	581.7
EBIT	411.5	352.7	118.6	98.9
Net result after min.	335.8	288.3	97.6	80.1
EPS (PLN)	9.87	8.48	2.87	2.36
CEPS (PLN)	22.32	21.38	16.60	16.55
BVPS (PLN)	95.86	100.38	99.86	101.07
Div./share (PLN)	0.75	3.95	3.39	1.15
EV/EBITDA (x)	1.2	1.2	1.7	1.7
P/E (x)	3.9	4.5	13.3	16.2
P/CE (x)	1.7	1.8	2.3	2.3
Dividend Yield	2.0%	10.3%	8.9%	3.0%



Performance	12M	6M	3M	1M
in PLN	-31.8%	3.2%	10.9%	6.7%
Reuters	LWBP.WA	Free float	34.0%	
Bloomberg	LWB.PW	Shareholders	Enea (66.0%)	
Div. Ex-date	09/07/19			
Target price	46.1	Homepage:	www.lw.com.pl	

Share price (PLN) close as of 27/11/2019	38.2
Number of shares (mn)	34.0
Market capitalization (PLN mn / EUR mn)	1,299 / ,302
Enterprise value (PLN mn / EUR mn)	1,044 / ,242

## Analyst:

Tomasz Duda  
 +48 22 330 6253  
 tomasz.duda@erstegroup.com

## Stronger performance of LW Bogdanka vs. more profound deterioration of coal market fundamentals

LW Bogdanka out-performed our expectations during 9M19 with respect to both cost and pricing (by some 1-1.5% each). This achievement prompts us to increase our forecast for operational cash flow by 9% vs. our July forecast. At the same time, the company cut its 2019 CAPEX guidance by 12%, while execution of the new guidance remains low at only 58% after 9M19. Such a performance makes us significantly increase our free cash flow forecasts for 2019e and 2020e, which results in a much higher net cash position expected at the end of 2020e at PLN 346mn (vs. PLN 193mn previously). The strong balance sheet might be especially supportive, given the ongoing significant deterioration of Polish coal market fundamentals.

On the other hand, the fundamentals of the Polish thermal coal market deteriorated to a much higher degree than we expected, as a result of: 1) the decline of demand for power by 0.6% in 10M19 vs. 1% growth expected; 2) much higher power imports expected now at 10TWh in 2019e, which push out coal units from the market. This makes us cut our forecast for 2020e demand for thermal coal from the power sector by 3.1%. Already now, coal inventories in Poland are the highest since 4Q15 at 12.3mn tonnes, i.e. 127 days of consumption. The consequence of such high inventories has usually been a decline of prices, which we expect to see in 2020-21e (though power companies guide for flat 2020e prices).

**The improved FCF outlook and much stronger balance sheet leads us to revise up our recommendation for LW Bogdanka to Buy and set our target price at PLN 46.1.**

## Valuation

We employed a DCF model as our primary valuation tool, based on our forecasts for 2020-24e. We used a discount rate based on WACC and a terminal value based on perpetuity and the diluted number of shares. The DCF model reflects the value of LW Bogdanka in a more proper way than a peer comparison, as it includes future prospects.

### Assumptions

Our estimates are based on the following assumptions:

- Risk-free rate at 2.0%, equity premium at 6%, debt premium of 2%.
- CAPEX in line with company guidance and later forecast along with mining output and volume of preparatory work forecast. We reduced our previous CAPEX forecasts due to low execution of CAPEX plans seen in 9M19.
- Thermal coal price is assumed to be driven by deficit/oversupply expectations for Polish coal market. Hence, we assume thermal coal price to rise by approx. 15.5% y/y in 2019e (vs. 14% in our previous report) and then to stay flat in 2020e, due to pressure from low international prices, and then to decline by approx. 7% in 2021e, due to expected pressure on pricing from expected high domestic inventories.
- EBIT margin assumption in Terminal Year is lowered from 7.0% to 6.5% due to deterioration of thermal coal market fundamentals seen throughout 2019.
- Cost side is expected to reflect both savings efforts as well as need for particular volume of preparatory work. Volume of preparatory work in 2019e is expected to decline from record-high figure seen in 2018 and remain at comparable level thereafter.
- Nominal tax rate assumed at 19% in 2020-24e.

The terminal value growth rate at 0% is to account for risks embedded in the pricing forecasts, reserves replacement risks and power market structure and power demand risks.

### WACC calculation

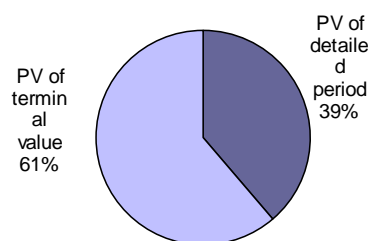
	2020e	2021e	2022e	2023e	2024e	NY / TV
Risk free rate	2.0%	2.0%	2.0%	2.0%	2.0%	4.0%
Equity risk premium	6.0%	6.0%	6.0%	6.0%	6.0%	5.0%
Beta	1.0	1.0	1.0	1.0	1.0	1.0
<b>Cost of equity</b>	<b>8.0%</b>	<b>8.0%</b>	<b>8.0%</b>	<b>8.0%</b>	<b>8.0%</b>	<b>9.0%</b>
Cost of debt	4.0%	4.0%	4.0%	4.0%	4.0%	6.0%
Effective tax rate	19.0%	19.0%	19.0%	19.0%	19.0%	19.0%
<b>After-tax cost of debt</b>	<b>3.2%</b>	<b>3.2%</b>	<b>3.2%</b>	<b>3.2%</b>	<b>3.2%</b>	<b>4.9%</b>
Equity weight	99%	99%	99%	99%	99%	99%
<b>WACC</b>	<b>8.0%</b>	<b>8.0%</b>	<b>8.0%</b>	<b>8.0%</b>	<b>8.0%</b>	<b>9.0%</b>

### DCF valuation

(PLN mn)	2020e	2021e	2022e	2023e	2024e	NY / TV
<i>Sales growth</i>	1.6%	-9.0%	1.0%	1.0%	0.0%	0.0%
EBIT	352.7	118.6	98.9	81.1	81.1	135.4
<i>EBIT margin</i>	15.7%	5.8%	4.8%	3.9%	3.9%	6.5%
<i>Tax rate</i>	19.0%	19.0%	19.0%	19.0%	19.0%	19.0%
Taxes on EBIT	-67.0	-22.5	-18.8	-15.4	-15.4	-25.7
<b>NOPLAT</b>	<b>285.7</b>	<b>96.1</b>	<b>80.1</b>	<b>65.7</b>	<b>65.7</b>	<b>109.6</b>
+ Depreciation	439.1	467.1	482.8	496.5	496.5	496.5
<i>Capital expenditures / Depreciation</i>	113.9%	107.0%	103.6%	100.7%	100.7%	99.3%
+/- Change in working capital	1.1	-6.1	0.6	0.6	0.0	0.6
<i>Chg. working capital / chg. Sales</i>						
- Capital expenditures	-500.0	-500.0	-500.0	-500.0	-500.0	-500.0
<b>Free cash flow to the firm</b>	<b>223.7</b>	<b>69.3</b>	<b>62.3</b>	<b>61.5</b>	<b>62.2</b>	<b>105.5</b>
<i>Terminal value growth</i>						0.0%
Terminal value						1 177.4
Discounted free cash flow - Dec 31 2019	207.2	59.4	49.5	45.3	42.4	803.1
<b>Enterprise value - Dec 31 2019</b>	<b>1 206.9</b>					
Minorities	10.2					
Net debt	-265.9					
Other assets	0.0					
Other adjustments	0.0					
<b>Equity value - Dec 31 2019</b>	<b>1 462.7</b>					
Number of shares outstanding (mn)	34.0					
Cost of equity	8.0%					
<b>12M target price per share (PLN)</b>	<b>46.1</b>					
Current share price (PLN)	38.2					
<i>Up/Downside</i>	20.7%					

### Enterprise value breakdown

### Sensitivity (per share)



Source: Erste Group Research

		Terminal value EBIT margin				
		2.5%	4.5%	6.5%	8.5%	10.5%
WACC	8.0%	31.1	40.2	49.3	58.4	67.5
	8.5%	30.5	39.0	47.6	56.2	64.8
	9.0%	29.9	38.0	<b>46.1</b>	54.2	62.3
	9.5%	29.4	37.1	44.8	52.4	60.1
	10.0%	29.0	36.3	43.6	50.9	58.1
		Terminal value growth				
		-2.0%	-1.0%	0.0%	1.0%	2.0%
WACC	8.0%	43.6	46.1	49.3	53.4	58.9
	8.5%	42.5	44.8	47.6	51.2	55.9
	9.0%	41.5	43.6	<b>46.1</b>	49.3	53.4
	9.5%	40.6	42.5	44.8	47.6	51.2
	10.0%	39.8	41.5	43.6	46.1	49.3

Peer group comparison

	P/E			EV/EBITDA		
	2019e	2020e	2021e	2019e	2020e	2021e
GLENCORE PLC	26.8	13.9	11.7	6.8	5.9	5.4
WHITEHAVEN COAL LTD	14.6	12.3	13.1	6.0	5.4	5.4
CNX RESOURCES CORP	7.0	20.7	12.0	5.6	5.2	5.6
PEABODY ENERGY CORP	63.0	neg	neg	2.2	2.8	2.8
ARCH COAL INC - A	4.8	6.1	6.0	2.8	3.1	3.2
CHINA SHENHUA ENERGY CO-A	7.9	7.9	8.9	4.0	4.0	4.0
COAL INDIA LTD	7.1	6.7	6.6	4.0	3.7	3.5
BUMI SERPONG DAMAI PT	10.3	11.5	10.3	9.6	9.0	8.5
ADARO ENERGY TBK PT	6.6	7.1	7.1	3.5	3.5	3.6
BANPU PUBLIC CO LTD	17.6	12.5	11.4	11.7	11.6	10.5
YANZHOU COAL MINING CO-H	3.7	3.9	4.2	5.5	5.8	5.9
SHANXI COKING CO LTD-A	7.0	6.4	6.5	na	na	na
<b>Median total</b>	<b>7.5</b>	<b>7.9</b>	<b>8.9</b>	<b>5.5</b>	<b>5.2</b>	<b>5.4</b>
<b>LW Bogdanka</b>	<b>3.9</b>	<b>4.5</b>	<b>13.3</b>	<b>1.2</b>	<b>1.2</b>	<b>1.7</b>
<i>Premium/discount</i>	<i>-48%</i>	<i>-43%</i>	<i>50%</i>	<i>-77%</i>	<i>-77%</i>	<i>-68%</i>
<b>Implied value</b>	<b>73.8</b>	<b>67.3</b>	<b>25.5</b>	<b>126.6</b>	<b>111.5</b>	<b>84.2</b>

Source: Factset, Erste Group Research

**Erste Group Research – Company Report**  
 Bogdanka SA | Mining & Metals | Poland  
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<b>Income Statement</b>	<b>2017</b>	<b>2018</b>	<b>2019e</b>	<b>2020e</b>	<b>2021e</b>	<b>2022e</b>
(IAS, PLN mn, 31/12)	31/12/2017	31/12/2018	31/12/2019	31/12/2020	31/12/2021	31/12/2022
<b>Net sales</b>	<b>1 780.32</b>	<b>1 756.67</b>	<b>2 207.52</b>	<b>2 242.80</b>	<b>2 041.01</b>	<b>2 061.57</b>
Cost of goods sold	-859.16	-1 583.97	-1 631.25	-1 704.94	-1 753.81	-1 792.39
<b>Gross profit</b>	<b>921.16</b>	<b>172.70</b>	<b>576.27</b>	<b>537.86</b>	<b>287.19</b>	<b>269.18</b>
SG&A	-75.02	-144.49	-181.57	-184.47	-167.87	-169.57
Other operating revenues	5.10	34.62	19.00	1.50	1.50	1.50
Other operating expenses	-3.98	-0.81	-2.19	-2.19	-2.19	-2.19
<b>EBITDA</b>	<b>1 203.64</b>	<b>469.19</b>	<b>834.88</b>	<b>791.78</b>	<b>585.75</b>	<b>581.72</b>
Depreciation/amortization	356.37	407.16	423.37	439.08	467.12	482.79
<b>EBIT</b>	<b>847.27</b>	<b>62.03</b>	<b>411.51</b>	<b>352.70</b>	<b>118.63</b>	<b>98.93</b>
Financial result	-18.51	2.89	3.00	3.20	1.90	0.00
Extraordinary result	0.00	0.00	0.00	0.00	0.00	0.00
<b>EBT</b>	<b>828.76</b>	<b>64.92</b>	<b>414.51</b>	<b>355.90</b>	<b>120.53</b>	<b>98.93</b>
Income taxes	-160.84	-11.12	-78.76	-67.62	-22.90	-18.80
Result from discontinued operations	0.00	0.00	0.00	0.00	0.00	0.00
Minorities and cost of hybrid capital	0.31	0.17	0.00	0.00	0.00	0.00
<b>Net result after minorities</b>	<b>668.24</b>	<b>53.97</b>	<b>335.75</b>	<b>288.28</b>	<b>97.63</b>	<b>80.13</b>
<b>Balance Sheet</b>	<b>2017</b>	<b>2018</b>	<b>2019e</b>	<b>2020e</b>	<b>2021e</b>	<b>2022e</b>
(IAS, PLN mn, 31/12)						
Intangible assets	59.96	58.84	58.84	58.84	58.84	58.84
Tangible assets	3 240.31	3 270.29	3 346.93	3 407.85	3 440.73	3 457.94
Financial assets	128.54	134.69	147.64	161.89	177.56	194.80
<b>Total fixed assets</b>	<b>3 428.81</b>	<b>3 463.82</b>	<b>3 553.41</b>	<b>3 628.58</b>	<b>3 677.14</b>	<b>3 711.58</b>
Inventories	62.56	83.38	88.30	89.71	81.64	82.46
Receivables and other current assets	232.58	215.29	309.85	314.61	287.37	290.15
Other assets	0.00	0.00	0.00	0.00	0.00	0.00
Cash and cash equivalents	434.93	170.86	300.00	400.00	350.00	350.00
<b>Total current assets</b>	<b>730.07</b>	<b>469.53</b>	<b>698.15</b>	<b>804.32</b>	<b>719.01</b>	<b>722.61</b>
<b>TOTAL ASSETS</b>	<b>4 158.87</b>	<b>3 933.35</b>	<b>4 251.56</b>	<b>4 432.91</b>	<b>4 396.15</b>	<b>4 434.19</b>
Shareholders'equity	2 901.53	2 950.12	3 260.36	3 414.34	3 396.65	3 437.73
Minorities	10.00	10.18	10.18	10.18	10.18	10.18
Hybrid capital and other reserves	0.00	0.00	0.00	0.00	0.00	0.00
Pension and other LT personnel accruals	0.00	0.00	0.00	0.00	0.00	0.00
LT provisions	0.00	0.00	0.00	0.00	0.00	0.00
Interest-bearing LT debts	16.97	13.93	17.03	27.14	31.22	27.19
Other LT liabilities	495.47	522.50	522.50	522.50	522.50	522.50
<b>Total long-term liabilities</b>	<b>512.44</b>	<b>536.43</b>	<b>539.53</b>	<b>549.64</b>	<b>553.72</b>	<b>549.69</b>
Interest-bearing ST debts	305.15	3.21	17.03	27.14	31.22	27.19
Other ST liabilities	401.71	410.22	401.25	408.36	381.10	386.08
<b>Total short-term liabilities</b>	<b>744.91</b>	<b>446.80</b>	<b>451.67</b>	<b>468.93</b>	<b>445.77</b>	<b>446.77</b>
<b>TOTAL LIAB. , EQUITY</b>	<b>4 158.87</b>	<b>3 933.35</b>	<b>4 251.56</b>	<b>4 432.91</b>	<b>4 396.15</b>	<b>4 434.19</b>
<b>Cash Flow Statement</b>	<b>2017</b>	<b>2018</b>	<b>2019e</b>	<b>2020e</b>	<b>2021e</b>	<b>2022e</b>
(IAS, PLN mn, 31/12)						
Cash flow from operating activities	608.52	458.87	637.74	714.08	557.16	547.10
Cash flow from investing activities	-372.05	-418.23	-500.00	-500.00	-500.00	-500.00
Cash flow from financing activities	-342.64	-304.78	-8.60	-114.08	-107.16	-47.10
<b>CHANGE IN CASH , CASH EQU.</b>	<b>-106.18</b>	<b>-264.14</b>	<b>129.14</b>	<b>100.00</b>	<b>-50.00</b>	<b>0.00</b>
<b>Margins &amp; Ratios</b>	<b>2017</b>	<b>2018</b>	<b>2019e</b>	<b>2020e</b>	<b>2021e</b>	<b>2022e</b>
Sales growth	-0.3%	-1.3%	25.7%	1.6%	-9.0%	1.0%
EBITDA margin	67.6%	26.7%	37.8%	35.3%	28.7%	28.2%
EBIT margin	47.6%	3.5%	18.6%	15.7%	5.8%	4.8%
Net profit margin	37.5%	3.1%	15.2%	12.9%	4.8%	3.9%
ROE	25.7%	1.8%	10.8%	8.6%	2.9%	2.3%
ROCE	22.0%	1.6%	9.9%	8.1%	2.7%	2.2%
Equity ratio	69.5%	74.7%	76.4%	76.8%	77.0%	77.3%
Net debt	-112.8	-153.7	-265.9	-345.7	-287.6	-295.6
Working capital	-14.8	22.7	246.5	335.4	273.2	275.8
Capital employed	3 274.2	3 308.7	3 506.7	3 580.9	3 621.4	3 654.4
Inventory turnover	12.8	21.7	19.0	19.2	20.5	21.8

Source: Company data, Erste Group estimates

## Erste Group Research – Company Report

Bogdanka SA | Mining & Metals | Poland

29 November 2019

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**Erste Securities Polska S.A.**  
Analysis Department  
Ul. Królewska 16  
00-103 Warszawa  
Erste Securities Polska S.A Homepage.: [www.esp.pl](http://www.esp.pl)

and

**Erste Group Bank AG**  
Group Research  
1100 Vienna, Austria, Am Belvedere 1  
Head Office: Wien  
Commercial Register No: FN 33209m  
Commercial Court of Vienna  
Erste Group Homepage: [www.erstegroup.com](http://www.erstegroup.com)