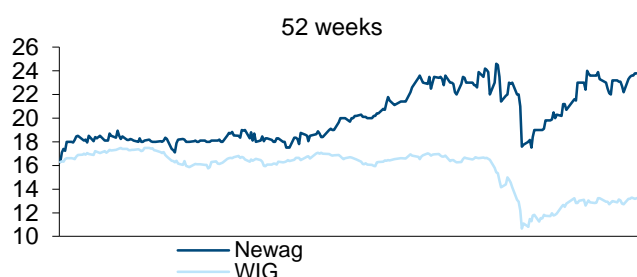


# Newag

from Buy to Accumulate

PLN mn	2019e	2020e	2021e	2022e
Net sales	906.5	1 249.5	1 259.3	1 219.0
EBITDA	170.1	219.9	226.2	218.9
EBIT	136.1	185.7	189.9	182.6
Net result after min.	88.7	123.7	163.8	126.6
EPS (PLN)	1.97	2.75	3.64	2.81
CEPS (PLN)	2.73	3.51	4.45	3.62
BVPS (PLN)	12.23	14.31	16.62	18.32
Div./share (PLN)	0.75	0.67	1.33	1.11
EV/EBITDA (x)	8.7	7.4	6.9	6.7
P/E (x)	12.2	8.7	6.6	8.5
P/CE (x)	8.8	6.8	5.4	6.6
Dividend Yield	3.1%	2.8%	5.6%	4.6%



Performance	12M	6M	3M	1M
in PLN	47.2%	20.0%	2.1%	1.7%

Share price (PLN) close as of 27/05/2020	24.0	Reuters	NWGP.WA	Free float	47.8%
Number of shares (mn)	45.0	Bloomberg	NWG.PW	Shareholders	Jonariuszy Newag (52.2%)
Market capitalization (PLN mn / EUR mn)	1,080 / ,244	Div. Ex-date	19/08/19		NN OFE (8.83%)
Enterprise value (PLN mn / EUR mn)	1,476 / ,337	<b>Target price</b>	<b>29.4</b>	Homepage:	<a href="https://www.newag.pl/">https://www.newag.pl/</a>

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## Still going strong (but slightly less so in 2022-24)

Our positive view on the stock persists, even though the COVID-19 pandemic may leave some mark on the company in the long run. Newag managed to sign its first contract on hybrid units and even more importantly, no other entity was willing to compete in this kind of tender in Poland. The company also proved successful in contract acquisition, having almost fulfilled our 2021 forecast in less than six months.

2020 should still be a record year for Newag. Despite the fact that the company has managed to deal with the COVID-19 pandemic quite successfully (especially when compared to its industrial peers), some negative developments emerged. For example, the weakness of the PLN relative to the EUR may cause some upward pressure on component costs. Also, the tough schedule leads us to assume that the approx. PLN 100mn backlog will be shifted to 2021. Either way, the results should show a significant, positive, double-digit dynamic relative to 2019.

While we are quite confident when it comes to our forecasts in 2020-21, some negative developments may appear in 2022-24. This leads us to decrease our assumptions for 2022-24. We reduce sales in 2022-24 to a total of PLN 3.66bn vs. the PLN 3.9bn expected previously. What is more, we slightly decrease our average gross margin forecast for 2020-24, from over 23% to 22.8%.

**For these reasons, we have decided to downgrade our recommendation from Buy to Accumulate with a target price of PLN 29.4.**

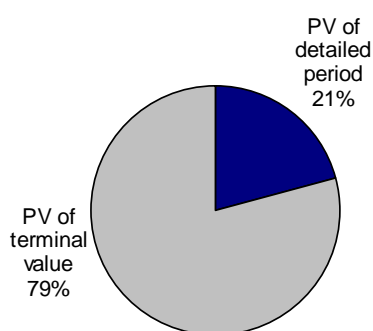
### WACC calculation

	2020e	2021e	2022e	2023e	2024e	Term. value Normalized
Risk free rate	2.1%	2.1%	2.1%	2.1%	2.1%	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>8.1%</b>	<b>8.1%</b>	<b>8.1%</b>	<b>8.1%</b>	<b>8.1%</b>	<b>9.0%</b>
Cost of debt	3.1%	3.1%	3.1%	3.1%	3.1%	5.0%
Effective tax rate	23.0%	23.0%	23.0%	23.0%	23.0%	21.0%
<b>After-tax cost of debt</b>	<b>2.4%</b>	<b>2.4%</b>	<b>2.4%</b>	<b>2.4%</b>	<b>2.4%</b>	<b>4.0%</b>
Equity weight	63%	66%	69%	71%	77%	100%
<b>WACC</b>	<b>6.0%</b>	<b>6.1%</b>	<b>6.3%</b>	<b>6.4%</b>	<b>6.8%</b>	<b>9.0%</b>

### DCF valuation

(PLN mn)	2020e	2021e	2022e	2023e	2024e	Normalized
Sales growth	37.8%	0.8%	-3.2%	4.4%	-8.4%	1.0%
EBIT	185.7	189.9	182.6	192.4	129.8	176.6
EBIT margin	14.9%	15.1%	15.0%	15.1%	11.1%	15.0%
Tax rate	23.0%	2.1%	23.0%	23.0%	23.0%	21.0%
Taxes on EBIT	-42.7	-4.0	-42.0	-44.2	-29.8	-37.1
<b>NOPLAT</b>	<b>143.0</b>	<b>185.9</b>	<b>140.6</b>	<b>148.1</b>	<b>99.9</b>	<b>139.5</b>
+ Depreciation	34.3	36.3	36.3	36.3	36.3	37.4
Capital expenditures / Depreciation	181.6%	166.7%	100.0%	100.0%	100.0%	105.0%
+/- Change in working capital	-221.6	-6.9	26.0	-34.8	58.4	-7.0
Chg. working capital / chg. Sales	-64.6%	-70.8%	-64.4%	-64.4%	-54.6%	-60.0%
- Capital expenditures	-62.3	-60.5	-36.3	-36.3	-36.3	-39.3
<b>Free cash flow to the firm</b>	<b>-106.6</b>	<b>154.8</b>	<b>166.6</b>	<b>113.4</b>	<b>158.4</b>	<b>130.7</b>
Terminal value growth						1.0%
Terminal value						1 780.5
Discounted free cash flow - Dec 31 2019	-100.5	137.6	139.2	89.0	116.5	1 201.4
<b>Enterprise value - Dec 31 2019</b>	<b>1 583.1</b>					
Minorities	0.0					
Non-operating assets	0.0					
Net debt	395.9					
Other adjustments	0.0					
<b>Equity value - Dec 31 2019</b>	<b>1 187.2</b>					
Number of shares outstanding (mn)	45.0					
Cost of equity	8.1%					
<b>12M target price per share (PLN)</b>	<b>29.4</b>					
Share price (PLN) May 27	24.0					
Up/Downside	22.7%					

### Enterprise value breakdown



source: Erste Group Research

### Sensitivity (per share)

		Terminal value EBIT margin				
		14.0%	14.5%	15.0%	15.5%	16.0%
WACC	8.0%	31.3	32.5	33.7	34.9	36.1
	8.5%	29.2	30.3	31.4	32.6	33.7
	9.0%	27.3	28.4	<b>29.4</b>	30.5	31.6
	9.5%	25.7	26.7	27.7	28.7	29.7
	10.0%	24.2	25.2	26.1	27.1	28.0
		Terminal value growth				
		0.0%	0.5%	1.0%	1.5%	2.0%
WACC	8.0%	35.2	34.4	33.7	33.0	32.2
	8.5%	32.8	32.1	31.4	30.7	30.1
	9.0%	30.7	30.1	<b>29.4</b>	28.8	28.2
	9.5%	28.9	28.3	27.7	27.1	26.5
	10.0%	27.3	26.7	26.1	25.6	25.0

## Peer valuation

The peer valuation with regard to Polish industrials reveals that the company is, dependent on ratio, under- or overpriced for 2020E.

### Polish industrials peer group comparison

	P/E			EV/EBITDA			P/BV		
	2020e	2021e	2022e	2020e	2021e	2022e	2020e	2021e	2022e
Forte	12.9	9.7	n.a.	16.2	8.3	7.1	0.7	0.7	n.a.
Apator	10.5	10.3	9.3	6.4	6.2	6.3	1.4	1.5	n.a.
Kęty	11.4	12.2	12.4	7.7	8.0	7.5	2.1	2.1	n.a.
Stalprodukt	n.a.	n.a.	n.a.	2.9	2.6	2.1	0.8	0.8	0.7
Alumetal	19.8	13.1	n.a.	7.7	6.5	5.2	3.3	2.8	2.2
Wielton	n.a.	n.a.	n.a.	7.9	6.0	5.2	4.1	3.5	3.0
Amica	12.0	8.9	n.a.	5.8	5.1	4.5	0.8	0.7	n.a.
<b>Median total</b>	<b>12.0</b>	<b>10.3</b>	<b>10.9</b>	<b>7.7</b>	<b>6.2</b>	<b>5.2</b>	<b>1.4</b>	<b>1.5</b>	<b>2.2</b>
<b>Newag</b>	<b>8.66</b>	<b>6.54</b>	<b>8.46</b>	<b>7.37</b>	<b>6.87</b>	<b>6.62</b>	<b>1.66</b>	<b>1.43</b>	<b>1.30</b>
<i>Premium/discount</i>	<i>-28%</i>	<i>-37%</i>	<i>-22%</i>	<i>-4%</i>	<i>11%</i>	<i>27%</i>	<i>21%</i>	<i>-5%</i>	<i>-42%</i>
<b>Implied value [PLN per share]</b>	<b>32.9</b>	<b>37.6</b>	<b>30.5</b>	<b>25.2</b>	<b>20.4</b>	<b>16.9</b>	<b>19.7</b>	<b>25.1</b>	<b>40.9</b>

Source: Factset, Erste Group Research

We also show the company's comparison with global rolling stock producers.

### Global peer group comparison

	P/E			EV/EBITDA			P/BV		
	2020e	2021e	2022e	2020e	2021e	2022e	2020e	2021e	2022e
Alstom	18.7	15.3	13.7	10.4	8.5	7.3	2.4	2.1	2.0
CRRC	9.3	8.3	7.5	7.4	6.8	6.3	0.8	0.7	0.7
Bombardier Transportation	n.a.	n.a.	n.a.	16.7	10.6	9.1	n.a.	n.a.	n.a.
Stadler Rail	29.4	20.3	17.1	14.2	11.4	10.0	4.6	4.1	3.7
Hyundai Rotem	87.3	86.5	37.8	22.8	19.4	16.6	1.7	1.6	1.6
CAF	12.5	9.1	7.5	6.1	5.3	4.8	1.2	1.1	1.0
Talgo	13.9	8.7	9.2	8.0	5.1	5.6	1.6	1.4	1.2
<b>Median total</b>	<b>16.3</b>	<b>12.2</b>	<b>11.5</b>	<b>10.4</b>	<b>8.5</b>	<b>7.3</b>	<b>1.6</b>	<b>1.5</b>	<b>1.4</b>
<b>Newag</b>	<b>8.66</b>	<b>6.54</b>	<b>8.46</b>	<b>7.37</b>	<b>6.87</b>	<b>6.62</b>	<b>1.66</b>	<b>1.43</b>	<b>1.30</b>
<i>Premium/discount</i>	<i>-47%</i>	<i>-46%</i>	<i>-26%</i>	<i>-29%</i>	<i>-19%</i>	<i>-9%</i>	<i>2%</i>	<i>-5%</i>	<i>-8%</i>
<b>Implied value [PLN per share]</b>	<b>44.9</b>	<b>44.4</b>	<b>32.3</b>	<b>30.7</b>	<b>29.3</b>	<b>25.9</b>	<b>20.0</b>	<b>21.6</b>	<b>23.5</b>

Source: Factset, Erste Group Research

The data reveals that Newag is still underpriced compared to global peers and we argue that this is to a large extent driven by its solely local scope of operations and underperformance in cash flow generation.

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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>789.87</b>	<b>1 021.56</b>	<b>906.52</b>	<b>1 249.53</b>	<b>1 259.32</b>	<b>1 218.99</b>
Cost of goods sold	685.63	816.92	699.15	952.71	962.43	932.87
<b>Gross profit</b>	<b>104.23</b>	<b>204.63</b>	<b>207.37</b>	<b>296.82</b>	<b>296.89</b>	<b>286.13</b>
SG&A	68.18	74.38	77.02	106.16	106.99	103.57
Other operating revenues	18.83	22.91	17.71	0.00	0.00	0.00
Other operating expenses	9.37	25.21	11.98	5.00	0.00	0.00
<b>EBITDA</b>	<b>79.41</b>	<b>164.39</b>	<b>170.06</b>	<b>219.94</b>	<b>226.23</b>	<b>218.89</b>
Depreciation/amortization	33.89	36.44	33.98	34.28	36.32	36.32
<b>EBIT</b>	<b>45.51</b>	<b>127.95</b>	<b>136.08</b>	<b>185.66</b>	<b>189.90</b>	<b>182.56</b>
Financial result	-10.70	-12.12	-20.51	-25.03	-22.59	-18.13
Extraordinary result	0.00	0.00	0.00	0.00	0.00	0.00
<b>EBT</b>	<b>34.82</b>	<b>115.83</b>	<b>115.57</b>	<b>160.63</b>	<b>167.32</b>	<b>164.44</b>
Income taxes	5.16	22.43	26.84	36.95	3.48	37.82
Result from discontinued operations	0.00	0.00	0.00	0.00	0.00	0.00
Minorities and cost of hybrid capital	-0.08	0.05	0.00	0.00	0.00	0.00
<b>Net result after minorities</b>	<b>29.74</b>	<b>93.35</b>	<b>88.72</b>	<b>123.69</b>	<b>163.83</b>	<b>126.62</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	36.16	30.94	30.94	30.94	30.94	30.94
Tangible assets	313.91	366.38	416.92	444.89	469.11	469.11
Financial assets	93.14	87.82	87.82	87.82	87.82	87.82
<b>Total fixed assets</b>	<b>443.21</b>	<b>485.13</b>	<b>535.68</b>	<b>563.65</b>	<b>587.86</b>	<b>587.86</b>
Inventories	237.26	223.21	277.74	378.47	382.33	370.59
Receivables and other current assets	279.16	419.42	422.21	581.97	586.53	567.75
Other assets	0.00	0.00	0.00	0.00	0.00	0.00
Cash and cash equivalents	13.80	63.51	70.00	90.00	110.00	130.00
<b>Total current assets</b>	<b>558.56</b>	<b>725.72</b>	<b>789.54</b>	<b>1 070.03</b>	<b>1 098.45</b>	<b>1 087.93</b>
<b>TOTAL ASSETS</b>	<b>1 001.77</b>	<b>1 210.85</b>	<b>1 325.22</b>	<b>1 633.67</b>	<b>1 686.31</b>	<b>1 675.79</b>
Shareholders'equity	403.49	495.27	550.41	644.09	747.93	824.54
Minorities	0.11	0.16	0.00	0.00	0.00	0.00
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	0.08	0.39	0.39	0.39	0.39	0.39
Interest-bearing LT debts	79.97	185.98	291.03	415.62	367.80	282.97
Other LT liabilities	0.00	0.00	0.00	0.00	0.00	0.00
<b>Total long-term liabilities</b>	<b>117.65</b>	<b>220.12</b>	<b>325.73</b>	<b>451.16</b>	<b>400.14</b>	<b>316.77</b>
Interest-bearing ST debts	204.01	203.32	174.88	224.88	224.88	224.88
Other ST liabilities	276.51	291.98	274.20	313.54	313.37	309.59
<b>Total short-term liabilities</b>	<b>480.52</b>	<b>495.30</b>	<b>449.08</b>	<b>538.43</b>	<b>538.25</b>	<b>534.48</b>
<b>TOTAL LIAB. , EQUITY</b>	<b>1 001.77</b>	<b>1 210.85</b>	<b>1 325.22</b>	<b>1 633.67</b>	<b>1 686.31</b>	<b>1 675.79</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	44.38	17.68	48.15	-62.34	188.36	191.15
Cash flow from investing activities	-33.58	-12.04	-84.53	-62.25	-60.54	-36.32
Cash flow from financing activities	-1.35	44.28	42.87	144.59	-107.82	-134.83
<b>CHANGE IN CASH , CASH EQU.</b>	<b>9.41</b>	<b>49.71</b>	<b>6.49</b>	<b>20.00</b>	<b>20.00</b>	<b>20.00</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	41.3%	29.3%	-11.3%	37.8%	0.8%	-3.2%
EBITDA margin	10.1%	16.1%	18.8%	17.6%	18.0%	18.0%
EBIT margin	5.8%	12.5%	15.0%	14.9%	15.1%	15.0%
Net profit margin	3.8%	9.1%	9.8%	9.9%	13.0%	10.4%
ROE	7.4%	20.8%	17.0%	20.7%	23.5%	16.1%
ROCE	4.3%	11.9%	9.7%	11.2%	13.1%	10.1%
Equity ratio	40.3%	40.9%	41.5%	39.4%	44.4%	49.2%
Net debt	270.2	325.8	395.9	550.5	482.7	377.9
Working capital	78.0	230.4	340.5	531.6	560.2	553.4
Capital employed	711.5	855.4	981.0	1 230.1	1 262.9	1 236.2
Inventory turnover	-3.0	-3.5	-2.8	-2.9	-2.5	-2.5

Source: Company data, Erste Group estimates

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 Newag | Industrial Goods & Services | Poland  
 28 May 2020  
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**Company description**

Newag SA Rolling stock producer

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