

Newag - Accumulate

Target Price: PLN 29.44 | Close as of 21/09/2020: PLN 26.50

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Q2 P&L results affected by negative one-offs; CF & BS deteriorates

Newag showed its final Q2'20 results with following highlights:

- Q2'20 revenues, EBITDA & net income in line with preliminary figures
- Q2'20 EBITDA was negatively affected by PLN 8.8mn reserves and write-offs
- Q2'20 gross margin of services & products at 26.3% vs. 21.9% expected
- Q2 net debt/EBITDA at 2.39x vs 2.17x in previous quarter and 2.39x in Q2'19
- Q2 OCF at PLN -55.7mn vs PLN 35.4mn in previous quarter and PLN 10.9mn in Q2'19 mainly due to increase in inventory (semi-finished products)
- Q2 FCF at PLN -79.8mn due to among others higher than expected capex

Quarterly snapshot

IFRS (PLN, mn)	Reported			Expected				Reported			
	Q2'20	Q2'19	Q1'20	y/y	q/q	ERSTE	Cons.	Preliminary	vs. ERSTE	vs. Cons.	vs. Prelim
Revenues	300.2	239.2	269.1	26%	12%	311.4	252.7	300.2	-3.6%	18.8%	0.0%
EBITDA	56.1	30.0	55.8	87%	1%	55.3	45.5	56.1	1.4%	23.3%	-0.1%
adj. EBITDA	65.6	33.8	58.4	94%	12%						
EBIT	47.1	21.6	47.3	118%	0%	46.8	37.0		0.6%	27.4%	
Net income	29.3	13.7	32.6	113%	-10%	31.9	25.5	29.5	-8.1%	15.2%	-0.7%
EBITDA margin	18.7%	12.5%	20.7%			17.8%	18.0%	18.7%			
EBIT margin	15.7%	9.0%	17.6%			15.0%	14.6%				
Net income margin	9.8%	5.7%	12.1%			10.2%	10.1%	9.8%			

Source: Company Data, Erste Group Research

OPINION: **NEUTRAL**

Overall, we evaluate Q2'20 results as neutral given one-offs in P&L figures (after adjustments P&L figures would be improved) and negative developments in CF and BS.

Higher than expected margin levels together with negative one-offs affecting EBITDA and net income are a plus and bode well for results in H2'20.

On the other hand low OCF and higher than expected capex & indebtedness are a negative surprise. Management wrote in a comment that higher debt is a seasonal effect that may appear in Q2 & Q3 given the increased scale. Still, those figure exceed our expectations and if the

situation won't change in next quarters this may lead to some downward valuation adjustments.

P & L (PLN m)	Q2'19	Q3'19	Q4'19	Q1'20	Q2'20	YoY	QoQ	H1'19	H1'20	YoY
Revenues	239.2	159.2	356.1	269.1	300.2	90%	-24%	380.7	569.3	50%
COGS	194.5	114.0	258.9	199.3	222.0	63%	-23%	316.8	421.4	33%
Gross profit on sales	44.7	45.3	97.3	69.7	78.2	262%	-28%	64.0	147.9	131%
Sales cost	0.2	0.7	0.6	0.2	0.1	-4%	-68%	0.4	0.3	-26%
Management costs	19.0	17.9	21.7	19.6	21.4	4%	-10%	37.8	41.0	9%
Other income/ (expense), net	-3.8	5.6	-3.2	-2.7	-9.5	-168%	-17%	0.1	-12.2	
Operating profit	21.6	32.2	71.8	47.3	47.1	1012%	-34%	25.9	94.4	265%
EBITDA	30.0	40.4	80.3	55.8	56.1	322%	-31%	43.2	111.9	159%
adj. EBITDA	33.8	34.8	83.5	58.4	65.6	530%	-30%	43.0	124.1	188%
Financial income / (expense)	-3.5	-6.3	-6.4	-5.9	-3.8	56%	-8%	-7.3	-9.6	
Profit before tax	18.1	25.9	65.4	41.4	43.3	8104%	-37%	18.6	84.7	356%
Income tax expense	5.3	2.8	8.4	8.7	13.9	377%	3%	7.1	22.7	
Net profit attr. to Parent	13.7	23.1	54.1	32.6	29.3	-2385%	-40%	12.3	61.9	402%
Profitability ratios	Q2'19	Q3'19	Q4'19	Q1'20	Q2'20			H1'19	H1'20	
Gross margin	18.68%	28.43%	27.31%	25.91%	26.04%			16.80%	25.98%	
EBIT margin	9.03%	20.25%	20.16%	17.58%	15.68%			6.8%	16.6%	
EBITDA margin	12.53%	25.38%	22.54%	20.73%	18.68%			11.3%	19.7%	
Net profit margin	5.74%	14.51%	15.18%	12.10%	9.77%			3.2%	10.9%	
Segments	Q2'19	Q3'19	Q4'19	Q1'20	Q2'20	YoY	QoQ	H1'19	H1'20	YoY
Revenues										
Services & products	238.6	159.0	356.2	267.8	297.3	91%	-25%	379.2	565.1	49%
Trade goods & materials	0.59	0.24	-0.03	1.22	2.92	27%	-3597%	1.6	4.1	166%
Gross profit										
Services & products	44.7	45.2	97.5	69.1	78.1	271%	-29%	63.4	147.3	132%
Trade goods & materials	-0.03	0.08	-0.21	0.58	0.06	-5%	-377%	0.6	0.6	9%
Gross margin										
Services & products	18.7%	28.4%	27.4%	25.8%	26.3%			16.7%	26.1%	
Trade goods & materials	-5.1%	31.4%	602.9%	47.7%	1.9%			37.5%	15.4%	
Balance sheet & cash flow	Q2'19	Q3'19	Q4'19	Q1'20	Q2'20	YoY	QoQ	H1'19	H1'20	YoY
Operational CF	10.9	-39.0	58.6	35.4	-55.7	-3537%	-40%	9.9	-20.3	-306%
Capex	20.6	14.4	10.6	24.3	24.1	-8%	129%	47.1	48.5	3%
FCF	-9.8	-53.4	48.0	11.0	-79.8	-140%	-77%	-37.3	-68.8	84%
Net debt	393.4	510.4	453.4	447.1	556.7	22%	-1%			
Equity	473.8	496.9	551.8	584.4	613.7	18%	6%			
Net debt/EBITDA	2.4	2.7	2.8	2.2	2.4					

Results vs. forecasts

IFRS (PLN, mn)	Reported		2020 results (report)		2019 results		
	H1'20	H1'19	y/y	Erste Group	% done	Reported	% done
Revenues	569.3	380.7	50%	1 249.5	45.6%	569.3	66.9%
EBITDA	111.9	43.2	159%	219.9	50.9%	111.9	38.6%
adj. EBITDA	124.1	43.0	188%				
EBIT	94.4	25.9	265%	185.7	50.8%	94.4	27.4%
Net income	61.9	12.3	402%	123.7	50.0%	61.9	19.9%
EBITDA margin	19.7%	11.3%					
EBIT margin	16.6%	6.8%					
Net income margin	10.9%	3.2%					

Source: Company Data, Erste Group Research

Most of Q2 P&L figures were in line with the estimates given preliminarily. However, full report revealed that EBITDA was affected by PLN 8.8mn non-cash one-off, which we evaluate as a positive surprise. Gross margin for products was higher than our expectations at 26.3% vs 21.9%. It looks like higher cost of components bought with EUR will appear in later quarters. Management costs at PLN 21.2mn were slightly above PLN 20mn expected by us, but still show improvement in relation to sales (7.1% vs 7.3% in previous quarter and 8% in Q2'19).

We positively evaluate decreased financing charges at PLN 4.9mn vs PLN 6.9mn in previous quarter (interest on debt in Q2 at PLN 3.8mn vs PLN 4.1mn in previous quarter), despite increased total debt by PLN 110mn.

Looks like the lower interest rates are starting to kick-in.

Net income was negatively affected by hiked tax rate at 32.2% vs 21.1% in previous quarter.

P&L results vs our assumptions in H1'20 looks promising amid stronger second half of the year (taking into consideration Management comments on more even distribution of results in 2020).

Out of potential contracts Newag informed of participating in a tender for Industrial Division for 10 new locomotives.

That would be all regarding positive news that we saw in full report.

We negatively evaluate increased indebtedness by PLN 110mn even though it is partially understandable given expected major improvement in scale in 2020. Net debt/EBITDA ratio is also higher than in previous quarter at 2.39x vs 2.17x.

Q2 OCF is very weak PLN -55.7mn comparing both y/y & q/q. Moreover, capex at PLN 48.5mn almost reaches our annual estimate of PLN 51.8mn. Our expectations regarding FCF this year were not really ambitious at PLN -90.3mn, but company came close to that with PLN -68.8mn after H1'20.

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