

Energomontaż Południe

Investment story, recommendation & valuation

With high exposure to the constructions for the power sector, i.e. the segment with probably the most attractive LT outlook within the construction industry, at the moment Energomontaż Południe should rank among the most preferred construction equity exposures, with the financial markets likely to discount the envisaged financial results improvement stemming from looming spendings growth on power units renovation and capacity expansion in the coming years (the sectoral outlays may reach as much as PLN 100-200 billion by 2025). We believe that thanks to (i) acquisitions scheduled for 2010 (which are likely to enlarge the Company's execution potential and support EPD with designing activity (which will enable it to conduct contracts as a general contractor)), (ii) cooperation with PBG – its strategic shareholder, characterized with excellent project management skills – and (iii) secured large contracts' financing (thanks to recent share issue), the Company may become one of the key players in executing investments in the Polish power sector and boost its profits in the coming years. True, the investments in Poland are to get the pace no sooner than in one or two years, but thanks to well-recognized position in Germany (where the investment program is currently running) the Company does well in its backlog development and has already partially secured its sales both for 2010 and 2011. Apart from core-business operations, we believe that on the back of recovering housing market in Poland, the residential activities of EP will finally start bearing fruits and generate fat cash flows within next two years (of even c. PLN 72 million, according to our estimates). Finally, we believe that after the economic slowdown in 2009, the steel structures manufacturing business may finally rebound this year, and that Amontex will start positively contributing to the Company's profits.

We increase our 12M EFV by 8% to PLN 4.86 per share (on the back of slightly lower NWC financing needs and valuation horizon forward shift). Given double-digit valuation gap (which emerged after the recent share market price decline), our conviction that it is the right time to discount the looming spendings' growth on power units buildings, as well as our preference towards small and mid-sized contractors rather than large ones (given their flexibility to adjust the possible construction costs rebound in 2H09), we upgrade our LT fundamental recommendation for EPD to Buy (from Hold). Given, however, uninspiring 1Q10E financial results, we maintain our ST market-relative Neutral bias unchanged.

Quarterly results corner; 1Q10E preview

Energomontaż Południe is to release its quarterly results on May 17, which we forecast to be mediocre. We project the Company's sales

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Sector: Construction
Fundamental rating: Buy (↑)
Market relative: Neutral (→)
Price: PLN 4.28
12M EFV: PLN 4.86 (↑)

Market Cap.: US\$ 101 m
Reuters code: EMPD.WA
Av. daily turnover: US\$ 0.12 m
Free float: 60%
12M range: PLN 3.33-5.50

Guide to adjusted profits

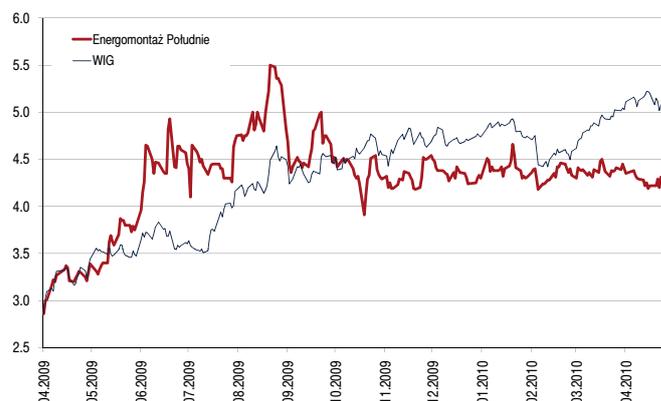
No factors necessitating adjustments.

Key data

IFRS consolidated		2009	2010E	2011E	2012E
Sales	PLN m	275.7	419.2	503.8	484.7
EBITDA	PLN m	30.2	35.5	42.7	45.0
EBIT	PLN m	23.5	26.6	30.7	30.8
Net profit	PLN m	14.3	17.3	23.3	23.6
EPS	PLN	0.30	0.24	0.33	0.33
EPS yoy chng	%	-10	-17	34	1
Net debt	PLN m	65.6	10.2	-1.7	-6.8
P/E	x	14.5	17.5	13.0	12.9
P/CE	x	9.9	11.6	8.6	8.0
EV/EBITDA	x	9.0	8.8	7.1	6.6
EV/EBIT	x	11.6	11.8	9.9	9.6
EV/Sales	x	1.0	0.7	0.6	0.6
Gross dividend yield	%	2.5	1.7	2.1	2.8
No. of shares (eop)	m	48.4	71.0	71.0	71.0

Source: Company, DM IDMSA estimates

Stock performance



Source: ISI

Upcoming events

1. Release of 1Q10 financial results: May 17, 2010

Catalysts

1. Efficient expansion on the German market
2. Signing large contracts in the power segment
3. Synergies with PBG
4. Pick up in volume of flats sold
5. Growing prices of dwellings

Risk factors

1. Inefficient expansion on the German market
2. Delays in the start of the investments in the power sector in Poland
3. Prolonging slowdown (which may lower demand on steel structures)
4. Possible lack of expected synergies with PBG
5. Upturn in construction material prices and subcontracting costs

at PLN 53 million, flattish yoy. The Company's operating profit will be under pressure of PLN vs. EUR appreciation (which is unfavorable for Energomontaż given high share of export contracts in its backlog) and, as a result, we project quarterly operating loss of c. PLN -0.5 million vs. operating profit of PLN 1.5 million in 1Q09).

However, the Company's net FX exposure was hedged in 100% and, consequently, we forecast net financial income at c. PLN 1.2 million in 1Q10 (helped with gains on FX hedging), with the in bottom line slightly in the black territory (and flattish yoy).

Financial forecast

We have moderately revised our mid-term financial forecast for Energomontaż Południe (chiefly on the back of slightly higher than previously envisaged gains from leasing of the office space in Wrocław). Our financial forecasts for the Company (we project 2010-2015 EBIT and NP CAGRs at, respectively, 11% and 16%) are based – the way we see it – on conservative assumptions and, all in all, the expected sectoral spendings' growth should (if materializes) enable the Company to beat our long-term projections.

Fig. 1 Energomontaż Południe; 1Q10 results' forecast

IFRS consolidated PLN m	yoy		Realization of the FY figures in:		
	1Q10E	1Q09A		change	1Q10E
Sales	53.0	54.1	-2%	13%	20%
Gross profit on sales	4.2	7.3	-42%	8%	19%
Gross profit on sales margin	8.0%	13.5%	-	-	-
EBIT	-0.5	1.5	n.m.	-2%	6%
EBIT margin	-0.9%	2.8%	-	-	-
Pre-tax profit	0.7	1.5	-52%	3%	8%
Pre-tax margin	1.3%	2.7%	-	-	-
Net profit	0.6	0.6	-2%	3%	4%
Net margin	1.1%	1.1%	-	-	-

Source: Company, DM IDMSA estimates

Fig. 2 Energomontaż Południe; Changes in IDM's forecast

IFRS consolidated PLN m	2010E			2011E			2012E		
	current	previous	change	current	previous	change	current	previous	change
Sales	419.2	419.2	0%	503.8	503.8	0%	484.7	484.7	0%
EBIT	26.6	24.5	9%	30.7	28.4	8%	30.8	28.3	9%
NP	17.3	18.6	-7%	23.3	23.6	-1%	23.6	23.5	0%

Source: DM IDMSA estimates

Fig. 3 Energomontaż Południe; DCF valuation of construction business

PLN m	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E	>2019E
Sales	419.2	503.8	484.7	537.8	585.2	628.4	653.9	679.0	705.2	732.4	
yoy change	52%	20%	-4%	11%	9%	7%	4%	4%	4%	4%	
EBIT margin	6.4%	6.1%	6.4%	6.5%	6.6%	6.2%	6.2%	5.8%	5.8%	5.8%	
EBIT	26.6	30.7	30.8	34.7	38.8	38.9	40.5	39.4	40.9	42.5	
yoy change	13%	15%	1%	13%	12%	0%	4%	-3%	4%	4%	
Effective cash tax rate (T)	22%	22%	19%	19%	19%	19%	19%	19%	19%	19%	
EBIT * (1-T)	20.8	23.9	25.0	28.1	31.4	31.5	32.8	31.9	33.2	34.4	
yoy change	9%	15%	4%	13%	12%	0%	4%	-3%	4%	4%	
EBITDA	35.5	42.7	45.0	47.8	50.0	51.3	54.0	54.2	57.1	60.2	
yoy change	18%	20%	6%	6%	5%	3%	5%	0%	5%	5%	
EBITDA margin	8.5%	8.5%	9.3%	8.9%	8.5%	8.2%	8.3%	8.0%	8.1%	8.2%	
Depreciation	8.9	12.0	14.2	13.0	11.2	12.4	13.5	14.8	16.2	17.7	
EBIT * (1-T) + D	29.6	35.9	39.2	41.2	42.6	43.9	46.3	46.7	49.3	52.1	
yoy change	15%	21%	9%	5%	3%	3%	6%	1%	6%	6%	
Capex	-47.6	-23.2	-25.5	-20.9	-14.3	-12.1	-13.4	-14.6	-16.0	-18.2	
Change in WC	4.1	6.2	1.5	-5.9	-5.1	-3.9	-2.8	-2.0	-2.8	-3.0	
Equity issue proceeds	77.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Free cash flow	64.0	18.9	15.2	14.3	23.2	27.9	30.1	30.1	30.5	30.9	
Cost of equity											
Risk free rate (nominal)	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	5.0%
Equity market premium	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%	4.5%
Unlevered beta	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Beta adjusted for leverage	1.19	1.19	1.18	1.17	1.15	1.14	1.13	1.12	1.12	1.11	1.11
Required rate of return	11.4%	11.3%	11.3%	11.3%	11.2%	11.1%	11.1%	11.0%	11.0%	11.0%	10.0%
Cost of debt											
Cost of debt (pre-tax)	7.5%	6.5%	6.5%	6.5%	6.5%	6.5%	6.5%	6.5%	6.5%	6.5%	6.5%
Effective tax rate	22%	22%	19%	19%	19%	19%	19%	19%	19%	19%	19%
After-tax cost of debt	5.9%	5.1%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%
WACC											
Weight of debt	20%	19%	18%	17%	15%	14%	14%	13%	13%	12%	12%
Weight of equity	80%	81%	82%	83%	85%	86%	86%	87%	87%	88%	88%
Cost of equity	11.4%	11.3%	11.3%	11.3%	11.2%	11.1%	11.1%	11.0%	11.0%	11.0%	10.0%
After-tax cost of debt	5.9%	5.1%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%
WACC	10.3%	10.1%	10.2%	10.2%	10.3%	10.3%	10.3%	10.3%	10.3%	10.3%	9.4%
Discount multiple	1.00	1.07	1.18	1.30	1.43	1.58	1.74	1.92	2.12	2.33	
Discount factor	1.00	0.94	0.85	0.77	0.70	0.63	0.58	0.52	0.47	0.43	
PV of free cash flow	-	17.7	12.9	11.1	16.2	17.7	17.3	15.7	14.4	13.3	
Sum of FCFs PVs											136.3
Weight of debt in the residual period											12%
Weight of equity in the residual period											88%
Average cost of equity in the definite period											11.2%
Average WACC in the definite period											10.3%
WACC in the residual period											9.4%
Residual growth of FCFs, base-case scenario											2.5%
Residual value											457.5
Present value of the residual value											196.0
Dividends											5.3
EV of EP's construction business											337.6

Source: Company, DM IDMSA estimates

Fig. 4 *Energomontaż Południe; SOTP valuation*

Asset	Valuation method	Value to the Company (PLN m)
Housing assets	Land value	17.7
Construction business	DCF FCF	337.6
Cash and equivalents (2010E eop)		70.2
Interest-bearing debt (2010E eop)		80.5
NAV		345.1
Value per share (PLN)		4.86

Source: DM IDMSA estimates



Financial statements (IFRS consolidated)

Fig. 5 *Energomontaż Południe; Balance sheet*

PLN m	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
Fixed assets	195.2	234.0	245.2	256.4	264.4	267.5	267.2	267.0	266.9	266.7	267.2
Intangibles	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
Goodwill	27.9	27.9	27.9	27.9	27.9	27.9	27.9	27.9	27.9	27.9	27.9
Tangible fixed assets	57.3	96.0	107.2	118.5	126.4	129.5	129.2	129.1	128.9	128.7	129.2
LT receivables	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
LT investments	94.0	94.0	94.0	94.0	94.0	94.0	94.0	94.0	94.0	94.0	94.0
LT deferred assets	14.3	14.3	14.3	14.3	14.3	14.3	14.3	14.3	14.3	14.3	14.3
Other	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Current assets	288.6	292.7	324.6	321.7	347.2	372.5	406.1	434.7	463.0	492.6	522.9
Inventories	67.3	35.8	25.1	24.1	26.7	29.1	31.4	32.7	34.1	35.4	36.8
ST receivables	164.6	152.1	182.8	175.9	195.1	212.3	228.0	237.3	246.4	255.9	265.7
ST deferred assets	34.2	34.2	34.2	34.2	34.2	34.2	34.2	34.2	34.2	34.2	34.2
Cash & equivalents	22.1	70.2	82.2	87.3	90.9	96.6	112.2	130.2	148.0	166.8	185.9
Other assets	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3
Total assets	483.8	526.6	569.8	578.2	611.5	640.0	673.3	701.8	729.9	759.3	790.1
Equity	197.6	209.7	226.6	241.5	258.9	278.8	298.0	318.7	338.4	359.8	382.4
Liabilities & reserves	286.2	317.0	343.2	336.6	352.7	361.2	375.3	383.0	391.5	399.5	407.7
Reserves	12.7	12.7	12.7	12.7	12.7	12.7	12.7	12.7	12.7	12.7	12.7
LT liabilities	91.9	91.9	91.9	91.9	91.9	91.9	91.9	91.9	91.9	91.9	91.9
Non-interest-bearing	61.4	61.4	61.4	61.4	61.4	61.4	61.4	61.4	61.4	61.4	61.4
Interest-bearing	30.5	30.5	30.5	30.5	30.5	30.5	30.5	30.5	30.5	30.5	30.5
ST Liabilities	160.8	191.6	217.8	211.2	227.3	235.8	249.9	257.6	266.1	274.1	282.3
Non-interest-bearing	103.6	141.6	167.8	161.2	177.3	191.8	205.9	213.6	222.1	230.1	238.3
Interest-bearing	57.2	50.0	50.0	50.0	50.0	44.0	44.0	44.0	44.0	44.0	44.0
Deferred liabilities	20.8	20.8	20.8	20.8	20.8	20.8	20.8	20.8	20.8	20.8	20.8
Total liabilities and equity	483.8	526.6	569.8	578.2	611.5	640.0	673.3	701.8	729.9	759.3	790.1

Source: Company, DM IDMSA estimates

Fig. 5 *Energomontaż Południe; Income statement*

PLN m	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
Sales	275.7	419.2	503.8	484.7	537.8	585.2	628.4	653.9	679.0	705.2	732.4
COGS	-236.3	-368.8	-445.5	-426.3	-473.2	-515.7	-557.0	-579.6	-604.4	-627.6	-651.9
Gross profit on sales	39.4	50.4	58.3	58.4	64.6	69.6	71.4	74.4	74.6	77.5	80.5
Selling costs	-0.3	-1.7	-2.0	-2.0	-2.2	-2.4	-2.5	-2.6	-2.7	-2.8	-3.0
General administration costs	-17.9	-22.6	-26.2	-26.2	-28.5	-29.3	-30.8	-32.0	-33.3	-34.6	-35.9
Net profit on sales	21.3	26.1	30.1	30.3	33.9	38.0	38.1	39.7	38.6	40.1	41.7
Other operating income	12.8	5.4	5.4	5.4	5.4	5.4	5.4	5.4	5.4	5.4	5.4
Other operating costs	-10.6	-4.9	-4.9	-4.9	-4.6	-4.6	-4.6	-4.6	-4.6	-4.6	-4.6
EBIT	23.5	26.6	30.7	30.8	34.7	38.8	38.9	40.5	39.4	40.9	42.5
Financial income	9.5	3.4	4.5	3.5	2.7	2.8	3.1	3.6	4.2	4.7	5.3
Financial costs	-15.5	-7.8	-5.2	-5.2	-5.2	-5.0	-4.8	-4.8	-4.8	-4.8	-4.8
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pre-tax income	17.5	22.2	29.9	29.1	32.2	36.5	37.2	39.3	38.8	40.8	43.0
Income tax	-3.3	-4.9	-6.6	-5.5	-6.1	-6.9	-7.1	-7.5	-7.4	-7.8	-8.2
Minority interest in net income	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net income	14.3	17.3	23.3	23.6	26.1	29.6	30.1	31.8	31.4	33.1	34.8

Source: Company, DM IDMSA estimates

Fig. 8 Energomontaż Południe; Cash flow

PLN m	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
Net income (loss)	14.3	17.3	23.3	23.6	26.1	29.6	30.1	31.8	31.4	33.1	34.8
Depreciation and amortization	6.7	8.9	12.0	14.2	13.0	11.2	12.4	13.5	14.8	16.2	17.7
NWC change:	-108.4	4.1	6.2	1.5	-5.9	-5.1	-3.9	-2.8	-2.0	-2.8	-3.0
Change in inventories	-7.8	31.5	10.7	1.1	-2.6	-2.4	-2.3	-1.3	-1.4	-1.3	-1.4
Change in receivables	-103.1	-65.4	-30.7	6.9	-19.3	-17.2	-15.6	-9.3	-9.1	-9.5	-9.9
Change in payables	2.4	38.0	26.2	-6.6	16.0	14.5	14.1	7.7	8.5	7.9	8.3
Other	63.7	8.4	0.7	1.7	2.5	2.2	1.7	1.2	0.7	0.1	-0.5
Operating cash flow	-23.8	38.7	42.3	41.0	35.8	37.9	40.4	43.7	44.8	46.5	49.1
Capital expenditures	-10.6	-47.6	-23.2	-25.5	-20.9	-14.3	-12.1	-13.4	-14.6	-16.0	-18.2
Other	70.8	3.4	4.5	3.5	2.7	2.8	3.1	3.6	4.2	4.7	5.3
Investing cash flow	60.2	-44.2	-18.7	-21.9	-18.3	-11.5	-8.9	-9.7	-10.4	-11.2	-12.9
Change in interest-bearing debt	16.9	-7.2	0.0	0.0	0.0	-6.0	0.0	0.0	0.0	0.0	0.0
Dividends payment	-5.2	-5.3	-6.4	-8.6	-8.7	-9.7	-11.0	-11.2	-11.8	-11.6	-12.2
Interest	-7.6	-11.8	-5.2	-5.2	-5.2	-5.0	-4.8	-4.8	-4.8	-4.8	-4.8
Equity issue proceeds and other	-26.3	77.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financing cash flow	-22.2	53.7	-11.6	-13.9	-14.0	-20.7	-15.8	-16.0	-16.6	-16.5	-17.1
Total cash flow	14.3	48.1	11.9	5.2	3.6	5.7	15.6	18.0	17.8	18.8	19.1

Source: Company, DM IDMSA estimates

Fig. 7 Energomontaż Południe; Ratios

	2009	2010E	2011E	2012E	2013E	2014E	2015E	2016E	2017E	2018E	2019E
Sales growth (yoy)	15%	52%	20%	-4%	11%	9%	7%	4%	4%	4%	4%
Gross profit growth (yoy)	6%	28%	16%	0%	11%	8%	3%	4%	0%	4%	4%
EBITDA growth (yoy)	1%	18%	20%	6%	6%	5%	3%	5%	0%	5%	5%
Operating profit growth (yoy)	-7%	13%	15%	1%	13%	12%	0%	4%	-3%	4%	4%
Net income growth (yoy)	-9%	21%	34%	1%	11%	14%	2%	6%	-1%	5%	5%
A/R turnover days	189	138	121	135	126	127	128	130	130	130	130
Inventory turnover days	96	51	25	21	20	20	20	20	20	20	20
A/P turnover days	125	106	114	128	119	120	120	122	122	122	122
Cash cycle	160	83	32	29	27	27	28	28	28	28	28
NWC/ Sales	24%	-4%	-4%	-5%	-3%	-2%	-1%	-1%	0%	0%	0%
Gross margin	14.3%	12.0%	11.6%	12.0%	12.0%	11.9%	11.4%	11.4%	11.0%	11.0%	11.0%
EBITDA margin	11.0%	8.5%	8.5%	9.3%	8.9%	8.5%	8.2%	8.3%	8.0%	8.1%	8.2%
EBIT margin	8.5%	6.4%	6.1%	6.4%	6.5%	6.6%	6.2%	6.2%	5.8%	5.8%	5.8%
Pre-tax margin	6.4%	5.3%	5.9%	6.0%	6.0%	6.2%	5.9%	6.0%	5.7%	5.8%	5.9%
Net margin	5.2%	4.1%	4.6%	4.9%	4.8%	5.1%	4.8%	4.9%	4.6%	4.7%	4.8%
ROE	9.2%	8.5%	10.7%	10.1%	10.4%	11.0%	10.4%	10.3%	9.6%	9.5%	9.4%
ROA	3.6%	3.4%	4.3%	4.1%	4.4%	4.7%	4.6%	4.6%	4.4%	4.4%	4.5%
Current ratio	1.8	1.5	1.5	1.5	1.5	1.6	1.6	1.7	1.7	1.8	1.9
Quick ratio	1.4	1.3	1.4	1.4	1.4	1.5	1.5	1.6	1.6	1.7	1.7

Source: Company, DM IDMSA estimates

BASIC DEFINITIONS

A/R turnover (in days) = $365/(\text{sales}/\text{average A/R})$

Inventory turnover (in days) = $365/(\text{COGS}/\text{average inventory})$

A/P turnover (in days) = $365/(\text{COGS}/\text{average A/P})$

Current ratio = $(\text{current assets} - \text{ST deferred assets})/\text{current liabilities}$

Quick ratio = $(\text{current assets} - \text{ST deferred assets} - \text{inventory})/\text{current liabilities}$

Interest coverage = $(\text{pre-tax profit before extraordinary items} + \text{interest payable})/\text{interest payable}$

Gross margin = $\text{gross profit on sales}/\text{sales}$

EBITDA margin = $\text{EBITDA}/\text{sales}$

EBIT margin = EBIT/sales

Pre-tax margin = $\text{pre-tax profit}/\text{sales}$

Net margin = $\text{net profit}/\text{sales}$

ROE = $\text{net profit}/\text{average equity}$

ROA = $(\text{net income} + \text{interest payable})/\text{average assets}$

EV = $\text{market capitalization} + \text{interest bearing debt} - \text{cash and equivalents}$

EPS = $\text{net profit}/\text{no. of shares outstanding}$

CE = $\text{net profit} + \text{depreciation}$

Dividend yield (gross) = $\text{pre-tax DPS}/\text{stock market price}$

Cash sales = $\text{accrual sales corrected for the change in A/R}$

Cash operating expenses = $\text{accrual operating expenses corrected for the changes in inventories and A/P, depreciation, cash taxes and changes in the deferred taxes}$

DM IDM S.A. generally values the covered non bank companies via two methods: comparative method and DCF method (discounted cash flows). The advantage of the former is the fact that it incorporates the current market assessment of the value of the company's peers. The weakness of the comparative method is the risk that the valuation benchmark may be mispriced. The advantage of the DCF method is its independence from the current market valuation of the comparable companies. The weakness of this method is its high sensitivity to undertaken assumptions, especially those related to the residual value calculation. Please note that we also resort to other valuation techniques (e.g. NAV-, DDM- or SOTP-based), should it prove appropriate in a given case.

KEY TO INVESTMENT RANKINGS

This is a guide to expected price performance in absolute terms over the next 12 months:

Buy – fundamentally undervalued (upside to 12M EFV in excess of the cost of equity) + catalysts which should close the valuation gap identified;

Hold – either (i) fairly priced, or (ii) fundamentally undervalued/overvalued but lacks catalysts which could close the valuation gap;

Sell – fundamentally overvalued (12M EFV < current share price + 1-year cost of equity) + catalysts which should close the valuation gap identified.

This is a guide to expected relative price performance:

Overweight – expected to perform better than the benchmark (WIG) over the next quarter in relative terms

Neutral – expected to perform in line with the benchmark (WIG) over the next quarter in relative terms

Underweight – expected to perform worse than the benchmark (WIG) over the next quarter in relative terms

The recommendation tracker presents the performance of DM IDMSA's recommendations. A recommendation expires on the day it is altered or on the day 12 months after its issuance, whichever comes first. Relative performance compares the rate of return on a given recommended stock in the period of the recommendation's validity (i.e. from the date of issuance to the date of alteration or – in case of maintained recommendations – from the date of issuance to the current date) in a relation to the rate of return on the benchmark in this time period. The WIG index constitutes the benchmark. For recommendations that expire by an alteration or are maintained, the ending values used to calculate their absolute and relative performance are: the stock closing price on the day the recommendation expires/ is maintained and the closing value of the benchmark on that date. For recommendations that expire via a passage of time, the ending values used to calculate their absolute and relative performance are: the average of the stock closing prices for the day the recommendation elapses and four directly preceding sessions and the average of the benchmark's closing values for the day the recommendation expires and four directly preceding sessions.

Banks

Net Interest Margin (NIM) = $\text{net interest income}/\text{average assets}$

NIM Adjusted = $(\text{net interest income adjusted for SWAPs})/\text{average assets}$

Non interest income = $\text{fees\&commissions} + \text{result on financial operations (trading gains)} + \text{FX gains}$

Interest Spread = $(\text{interest income}/\text{average interest earning assets})/(\text{interest cost}/\text{average interest bearing liabilities})$

Cost/Income = $(\text{general costs} + \text{depreciation} + \text{other operating costs})/(\text{profit on banking activity} + \text{other operating income})$

ROE = $\text{net profit}/\text{average equity}$

ROA = $\text{net income}/\text{average assets}$

Non performing loans (NPL) = loans in 'substandard', 'doubtful' and 'lost' categories

NPL coverage ratio = $\text{loan loss provisions}/\text{NPL}$

Net provision charge = $\text{provisions created} - \text{provisions released}$

DM IDM S.A. generally values the covered banks via two methods: comparative method and fundamental target fair P/E and target fair P/BV multiples method. The advantage of the former is the fact that it incorporates the current market assessment of the value of the company's peers. The weakness of the comparative method is the risk that the valuation benchmark may be mispriced. The advantage of the fundamental target fair P/E and target fair P/BV multiples method is its independence of the current market valuation of the comparable companies. The weakness of this method is its high sensitivity to undertaken assumptions, especially those related to the residual value calculation.

Assumptions used in valuation can change, influencing thereby the level of the valuation. Among the most important assumptions are: GDP growth, forecasted level of inflation, changes in interest rates and currency prices, employment level and change in wages, demand on the analysed company products, raw material prices, competition, standing of the main customers and suppliers, legislation changes, etc.

Changes in the environment of the analysed company are monitored by analysts involved in the preparation of the recommendation, estimated, incorporated in valuation and published in the recommendation whenever needed.

LT fundamental recommendation tracker

Recommendation		Issue date	Reiteration date	Expiry date	Performance	Relative performance	Price at issue/reiteration (PLN)	12M EFV (PLN)	
Energomontaż Południe									
Hold	-	01.12.2008	-	03.04.2009	28%	30%	2.36	3.40	-
-	→	-	09.01.2009	-	-	-	2.65	4.00	↑
-	→	-	11.01.2009	-	-	-	2.65	4.00	→
-	→	-	08.02.2009	-	-	-	2.53	4.00	→
-	→	-	08.03.2009	-	-	-	2.47	4.00	→
Buy	↑	03.04.2009	-	06.07.2009	52%	33%	3.01	5.00	↑
-	→	-	05.04.2009	-	-	-	3.01	5.00	→
-	→	-	15.05.2009	-	-	-	3.59	5.00	→
-	→	-	17.05.2009	-	-	-	3.59	5.00	→
-	→	-	08.06.2009	-	-	-	4.50	5.00	→
Hold	↓	06.07.2009	-	28.04.2010	-4%	-33%	4.58	4.50	↓
-	→	-	08.07.2009	-	-	-	4.47	4.50	→
-	→	-	02.08.2009	-	-	-	4.75	4.50	→
-	→	-	31.08.2009	-	-	-	4.81	4.50	→
-	→	-	12.10.2009	-	-	-	4.40	4.50	→
-	→	-	05.11.2009	-	-	-	4.19	4.50	→
-	→	-	14.12.2009	-	-	-	4.36	4.50	→
-	→	-	07.01.2010	-	-	-	4.42	4.50	→
-	→	-	03.02.2010	-	-	-	4.40	4.50	→
-	→	-	17.02.2010	-	-	-	4.42	4.50	→
-	→	-	01.03.2010	-	-	-	4.30	4.50	→
-	→	-	29.03.2010	-	-	-	4.39	4.50	→
Buy	↑	28.04.2010	-	Not later than 28.04.2011	-	-	4.28	4.86	↑

Market-relative recommendation tracker

Relative recommendation		Issue date	Reiteration date	Expiry date	Price at issue/reiteration (PLN)	Relative performance
Energomontaż Południe						
Neutral	-	01.12.2008	-	03.04.2009	2.36	30%
-	→	-	09.01.2009	-	2.65	-
-	→	-	11.01.2009	-	2.65	-
-	→	-	08.02.2009	-	2.53	-
-	→	-	08.03.2009	-	2.47	-
Overweight	↑	03.04.2009	-	31.08.2009	3.01	37%
-	→	-	05.04.2009	-	3.01	-
-	→	-	15.05.2009	-	3.59	-
-	→	-	17.05.2009	-	3.59	-
-	→	-	08.06.2009	-	4.50	-
-	→	-	06.07.2009	-	4.58	-
-	→	-	08.07.2009	-	4.47	-
-	→	-	02.08.2009	-	4.75	-
Neutral	↓	31.08.2009	-	05.11.2009	4.81	-15%
-	→	-	12.10.2009	-	4.40	-
Overweight	↑	05.11.2009	-	17.02.2010	4.19	0%
-	→	-	14.12.2009	-	4.36	-
-	→	-	07.01.2010	-	4.42	-
-	→	-	03.02.2010	-	4.40	-
Neutral	↓	17.02.2010	-	Not later than 17.02.2011	4.42	-11%
-	→	-	01.03.2010	-	4.30	-
-	→	-	29.03.2010	-	4.39	-
-	→	-	28.04.2010	-	4.28	-

Distribution of IDM's current recommendations

	Buy	Hold	Sell	Suspended	Under revision
Numbers	23	28	16	1	0
Percentage	34%	41%	24%	1%	0%

Distribution of IDM's current recommendations for companies that were within the last 12M IDM customers in investment banking

	Buy	Hold	Sell	Suspended	Under revision
Numbers	2	4	0	1	0
Percentage	29%	57%	0%	14%	0%

Distribution of IDM's current market relative recommended weightings

	Overweight	Neutral	Underweight	Suspended	Under revision
Numbers	22	28	17	1	0
Percentage	32%	41%	25%	1%	0%

Distribution of IDM's current market relative recommended weightings for the companies that were within the last 12M IDM customers in investment banking

	Overweight	Neutral	Underweight	Suspended	Under revision
Numbers	1	2	3	1	0
Percentage	14%	29%	43%	14%	0%

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