

This report is prepared for the Warsaw Stock Exchange SA within the framework of the Analytical Coverage Support Pilot Program. This is a translation of the Polish analytical report.

Ferro

7/2021/GPW (33) March 31, 2021

Analyst: Sylwia Jaśkiewicz, CFA

Sector: Construction materials
 Fundamental rating: Buy (→)
 Market relative: Overweight (→)
 Price: PLN 27.00
 12M EFV: PLN 30.8 (→)

Market Cap: US\$ 146 m
 Bloomberg code: FRO PW
 Av. daily turnover: US\$ 0.07 m
 12M range: PLN 11.20-28.40
 Free float: 67%

Recommended action

We uphold our ST market relative Overweight bias and LT fundamental Buy rating for the Company. 4Q20 financials are good and in line with our expectations.

This year the Group's development will garner support from the recently acquired companies Termet and Tester offering solutions in the segment of modern management of heat sources and energy efficiency which has a considerable growth potential stemming from increasing ecological awareness and supportive regulatory environment. Thanks to these acquisitions Ferro has gained an access to the market of gas condensing boilers. Ferro informed that Termet's FY20 revenues reached PLN 158 million (up 25% yoy) with EBITDA at PLN 12-14 million. According to our estimates, based on the maximum price for a 71% stake in Termet (PLN 54 million) and cash balance in the acquired company (PLN 10 million) the EV/EBITDA multiple of the transaction stands at 5x which we deem attractive. For Tester Ferro paid PLN 7 million. In our financial model we assumed the revenues and EBITDA of the acquired entities at PLN 144 million and PLN 12 million, respectively, in FY20. The Company considers launching another – apart from Skawina and Znojmo in Czechia – logistic center within the framework of logistic processes streamlining and facilitating access to key markets such as Southern Europe.

Valuation

We keep intact our financial forecasts and 12M EFV for the Company – representing a 50%-50% mix of the outcome of the DCF FCFF and peer-relative valuations – at PLN 30.8. The DCF/peer-relative valuation yields PLN 31.8/ PLN 29.9 per share.

Guide to adjusted profits

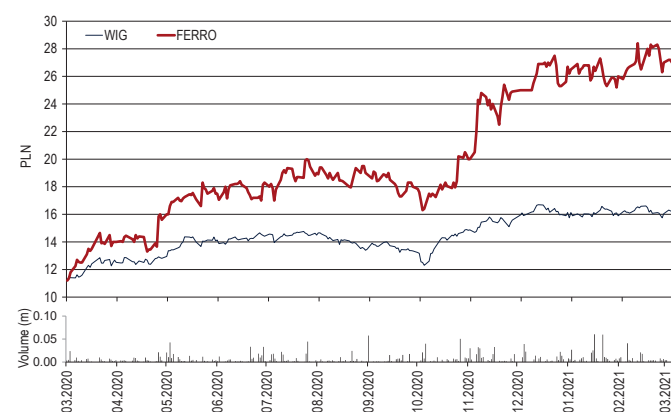
Income tax.

Key data

IFRS consolidated		2020	2021E	2022E	2023E
Sales	PLN m	519.1	665.3	705.2	740.4
EBITDA	PLN m	83.2	90.8	95.6	101.8
EBIT	PLN m	75.8	80.8	83.9	88.9
Net income	PLN m	62.1	60.5	62.3	66.6
Adj EPS	PLN	2.92	2.85	2.93	3.13
Adj EPS yoy chg	%	45	-3	3	7
Net debt	PLN m	31.8	88.2	72.5	52.4
P/E	x	9.2	9.5	9.2	8.6
EV/EBITDA	x	7.3	7.5	7.1	6.4
EV/EBIT	x	8.0	8.5	8.1	7.4
DPS	PLN	0.40	1.71	1.71	1.76
Gross dividend yield	%	1.5	6.3	6.3	6.5
Number of shares (eop)	m	21.2	21.2	21.2	21.2

* excl. minority stake in Termet
 Source: Company, DM BOS SA estimates

Stock performance



Source: Bloomberg

Upcoming events

1. Release of 1Q21 consolidated results: May 27
2. Release of 1H21 consolidated results: September 30
3. Release of 3Q21 consolidated results: November 29

Risk factors

1. Economic slowdown in Europe
2. Falling demand for new flats
3. Falling frequency of renovations
4. Workforce shortage
5. Wage pressure
6. High/volatile raw materials prices (of copper and zinc, in particular)
7. Unfavorable/volatile FX rates (currency risk when PLN and CZK weaken against US\$ and EUR)
8. Own brands developed by shopping chains

Catalysts

1. Continuous demand for new apartment flats
2. Development of the market for renovations
3. Expansion in European markets
4. Strengthening position on the existing markets
5. New products (expanding the product offer)
6. Repositioning of the Company's own brands (new upper segment brands)
7. Favorable/stable FX rates and raw materials prices
8. Brand promotion (intensifying online activities)
9. Acquisitions

4Q20 financial results review

The Group's 4Q20 financial results are good and in line with our expectations. Lower net financial costs stand behind slightly higher NI.

4Q20 revenues at PLN 135 million (up 18% yoy) slightly exceeded our forecast. 4Q20 sales on the domestic market increased by 10% yoy and delivered 35% of consolidated revenues. Sales yoy dynamic in Romania/ Czechia/ Slovakia/ Hungary/ other markets reached 27%/ 8%/ 4%/ 59%/ 59% in 4Q20.

4Q20 EBIT at PLN 13 million (up 19% yoy) was in line with our expectations; we assumed the lack of intensive marketing campaigns and expected travel and sale costs to decline yoy. We also assumed the cost of wages to rise in connection with the strategy implementation (in 1H20 numerous projects were suspended due to big uncertainty on the market). At the end of 2020 employment at the Company stood at 235 persons (up 22% yoy).

4Q20 net financial costs were close to 0 (due to FX gains) while we forecasted PLN 1.5 million. In result, the gross profit at PLN 13 million and NI at PLN 10 million slightly exceeded our expectations. The effective tax rate was 24% vs 65% in 4Q19 (a PLN 5.5 million CIT lowered the result).

The Group's FY20 revenues totaled PLN 519 million (up 15% yoy); sales in Poland (up 9% yoy)/ Romania (up 24% yoy)/ Czechia (up 7% yoy)/ Slovakia (up 6% yoy)/ Hungary (up 54% yoy)/ other markets (up 42% yoy) contributed 35%/ 22%/ 22%/ 8%/ 4%/ 9% of consolidated revenues. The batteries and accessories/ installation fittings segments delivered sales at PLN 323 million (up 17% yoy)/ PLN 189 million (up 13% yoy) which constituted 62%/ 36% in the Group's sales.

The Group's FY20 EBIT stood at PLN 76 million (up 25% yoy) with EBIT margin at 14.6% vs 13.4% in FY19. FY20 NI reached PLN 62 million (up 55% yoy).

Fig. 1. Ferro; 4Q20 financials vs forecasts

IFRS consolidated (PLN m)									4Q20 results						
	1Q19	2Q19	3Q19	4Q19	1Q20	2Q20	3Q20	4Q20	vs forecasts	4Q20E	yoy chg	2019	2020	2020E	yoy chg
Sales	109.4	105.8	122.1	113.9	124.8	112.0	147.7	134.6	→	123.0	18%	451.3	519.1	507.5	15%
EBITDA	18.7	14.4	21.5	12.3	21.8	17.3	29.4	14.7	→	14.6	20%	66.9	83.2	83.1	25%
EBITDA margin	17.1%	13.6%	17.6%	10.8%	17.5%	15.4%	19.9%	10.9%	-	11.9%	-	14.8%	16.0%	16.4%	-
EBIT	17.5	12.7	19.8	10.6	20.0	15.4	27.6	12.7	→	12.9	19%	60.6	75.8	76.0	25%
EBIT margin	16.0%	12.0%	16.2%	9.3%	16.1%	13.8%	18.7%	9.4%	-	10.5%	-	13.4%	14.6%	15.0%	-
Pre-tax profit	16.1	11.7	17.7	8.5	20.2	14.5	29.1	12.7	↑	11.4	50%	54.0	76.5	75.2	42%
Pre-tax profit margin	14.7%	11.1%	14.5%	7.4%	16.2%	12.9%	19.7%	9.4%	-	9.3%	-	12.0%	14.7%	14.8%	-
Net profit	13.0	9.5	14.5	2.9	16.5	12.3	23.6	9.6	↑	8.2	227%	40.0	62.1	60.7	55%
Net profit margin	11.9%	9.0%	11.9%	2.6%	13.2%	11.0%	16.0%	7.1%	-	6.7%	-	8.9%	12.0%	12.0%	-

Source: The Company, DM BOŚ SA 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 BOŠ 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 BOŠ S.A.'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.

Distribution of DM BOŠ's current recommendations

	Buy	Hold	Sell	Suspended	Under revision
Numbers	41	29	5	9	0
Percentage	49%	35%	6%	11%	0%

Banks

Net Interest Margin (NIM) = $\text{net interest income}/\text{average assets}$
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 = $(\text{general costs} + \text{depreciation})/(\text{profit on banking activity} + \text{other net operating income})$
ROE = $\text{net profit}/\text{average equity}$
ROA = $\text{net income}/\text{average assets}$
Non performing loans (NPL) = loans in 'basket 3' category
NPL coverage ratio = $\text{loan loss provisions}/\text{NPL}$
Net provision charge = $\text{provisions created} - \text{provisions released}$

DM BOŠ 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.

Distribution of DM BOŠ's current recommendations for the companies which DM BOŠ has supplied with material investment services within the last 12 months

	Buy	Hold	Sell	Suspended	Under revision
Numbers	6	6	0	2	0
Percentage	43%	43%	0%	14%	0%

Distribution of DM BOŠ's current market relative recommended weightings

	Overweight	Neutral	Underweight	Suspended	Under revision
Numbers	35	29	11	9	0
Percentage	42%	35%	13%	11%	0%

Distribution of DM BOŠ's current market relative recommended weightings for the companies which DM BOŠ has supplied with material investment services within the last 12 months

	Overweight	Neutral	Underweight	Suspended	Under revision
Numbers	3	7	2	2	0
Percentage	21%	50%	14%	14%	0%

LT fundamental recommendation tracker

Analyst	Recommendation	Report date	Reiteration date	Distribution date	Expiry date	Performance	Relative performance	Price at issue/reiteration*	EFV (12 months)	
Ferro										
Sylwia Jaśkiewicz	Hold	-	21.07.2019	-	22.07.2019	04.12.2019	11%	20%	13.70	17.10 -
Sylwia Jaśkiewicz	-	→	-	30.07.2019	31.07.2019	-	-	-	13.50	17.10 →
Sylwia Jaśkiewicz	-	→	-	01.09.2019	02.09.2019	-	-	-	12.05	17.10 →
Sylwia Jaśkiewicz	-	→	-	10.09.2019	11.09.2019	-	-	-	12.10	17.10 →
Sylwia Jaśkiewicz	-	→	-	15.09.2019	16.09.2019	-	-	-	12.65	17.10 →
Sylwia Jaśkiewicz	-	→	-	13.10.2019	14.10.2019	-	-	-	13.40	17.10 →
Sylwia Jaśkiewicz	-	→	-	24.10.2019	25.10.2019	-	-	-	13.00	17.10 →
Sylwia Jaśkiewicz	-	→	-	17.11.2019	18.11.2019	-	-	-	13.00	17.10 →
Sylwia Jaśkiewicz	-	→	-	18.11.2019	19.11.2019	-	-	-	13.00	17.10 →
Sylwia Jaśkiewicz	Buy	↑	04.12.2019	-	05.12.2019	28.01.2020	17%	15%	15.20	17.80 ↑
Sylwia Jaśkiewicz	-	→	-	08.12.2019	09.12.2019	-	-	-	15.00	17.80 →
Sylwia Jaśkiewicz	-	→	-	09.01.2020	10.01.2020	-	-	-	16.30	17.80 →
Sylwia Jaśkiewicz	Hold	↓	28.01.2020	-	29.01.2020	22.07.2020	-4%	5%	17.80	18.50 ↑
Sylwia Jaśkiewicz	-	→	-	04.02.2020	05.02.2020	-	-	-	17.90	18.50 →
Sylwia Jaśkiewicz	-	→	-	06.02.2020	07.02.2020	-	-	-	17.50	18.50 →
Sylwia Jaśkiewicz	-	→	-	03.03.2020	04.03.2020	-	-	-	15.20	18.50 →
Sylwia Jaśkiewicz	-	→	-	30.03.2020	31.03.2020	-	-	-	12.25	18.50 →
Sylwia Jaśkiewicz	-	→	-	22.04.2020	23.04.2020	-	-	-	14.00	18.50 →
Sylwia Jaśkiewicz	-	→	-	23.04.2020	24.04.2020	-	-	-	14.00	18.50 →
Sylwia Jaśkiewicz	-	→	-	19.05.2020	20.05.2020	-	-	-	13.65	18.50 →
Sylwia Jaśkiewicz	-	→	-	15.06.2020	16.06.2020	-	-	-	16.60	18.50 →
Sylwia Jaśkiewicz	-	→	-	13.07.2020	14.07.2020	-	-	-	17.90	18.50 →
Sylwia Jaśkiewicz	Buy	↑	22.07.2020	-	23.07.2020	Not later than 22.07.2021	61%	45%	17.00	20.30 ↑
Sylwia Jaśkiewicz	-	→	-	01.09.2020	02.09.2020	-	-	-	18.60	20.30 →
Sylwia Jaśkiewicz	-	→	-	17.09.2020	18.09.2020	-	-	-	18.90	20.30 →
Sylwia Jaśkiewicz	-	→	-	29.09.2020	30.09.2020	-	-	-	18.70	19.90 ↓
Sylwia Jaśkiewicz	-	→	-	08.10.2020	09.10.2020	-	-	-	19.00	19.90 →
Sylwia Jaśkiewicz	-	→	-	03.11.2020	04.11.2020	-	-	-	17.30	22.00 ↑
Sylwia Jaśkiewicz	-	→	-	08.11.2020	09.11.2020	-	-	-	17.25	22.00 →
Sylwia Jaśkiewicz	-	→	-	19.11.2020	20.11.2020	-	-	-	18.40	23.40 ↑
Sylwia Jaśkiewicz	-	→	-	26.11.2020	27.11.2020	-	-	-	20.00	23.40 →
Sylwia Jaśkiewicz	-	→	-	06.12.2020	07.12.2020	-	-	-	24.80	25.70 ↑
Sylwia Jaśkiewicz	-	→	-	05.01.2021	05.01.2021	-	-	-	25.50	25.70 →
Sylwia Jaśkiewicz	-	→	-	28.01.2021	29.01.2021	-	-	-	26.50	25.70 →
Sylwia Jaśkiewicz	-	→	-	09.02.2021	10.02.2021	-	-	-	25.70	30.80 ↑
Sylwia Jaśkiewicz	-	→	-	28.02.2021	01.03.2021	-	-	-	26.10	30.80 →
Sylwia Jaśkiewicz	-	→	-	31.03.2021	01.04.2021	-	-	-	27.00	30.80 →

* prices at issue/reiteration are the closing prices at the report or reiteration date

Market-relative recommendation tracker

Analyst	Relative Recommendation	Report date	Reiteration date	Distribution date	Expiry date	Price at issue/reiteration*	Relative performance
Ferro							
Sylwia Jaśkiewicz	Neutral	-	21.07.2019	-	22.07.2019	18.11.2019	13.70 -2%
Sylwia Jaśkiewicz	-	→	-	30.07.2019	31.07.2019	-	13.50 -
Sylwia Jaśkiewicz	-	→	-	01.09.2019	02.09.2019	-	12.05 -
Sylwia Jaśkiewicz	-	→	-	10.09.2019	11.09.2019	-	12.10 -
Sylwia Jaśkiewicz	-	→	-	15.09.2019	16.09.2019	-	12.65 -
Sylwia Jaśkiewicz	-	→	-	13.10.2019	14.10.2019	-	13.40 -
Sylwia Jaśkiewicz	-	→	-	24.10.2019	25.10.2019	-	13.00 -
Sylwia Jaśkiewicz	-	→	-	17.11.2019	18.11.2019	-	13.00 -
Sylwia Jaśkiewicz	Overweight	↑	18.11.2019	-	19.11.2019	28.01.2020	13.00 41%
Sylwia Jaśkiewicz	-	→	-	04.12.2019	05.12.2019	-	15.20 -
Sylwia Jaśkiewicz	-	→	-	08.12.2019	09.12.2019	-	15.00 -
Sylwia Jaśkiewicz	-	→	-	09.01.2020	10.01.2020	-	16.30 -
Sylwia Jaśkiewicz	Neutral	↓	28.01.2020	-	29.01.2020	23.04.2020	17.80 -1%
Sylwia Jaśkiewicz	-	→	-	04.02.2020	05.02.2020	-	17.90 -
Sylwia Jaśkiewicz	-	→	-	06.02.2020	07.02.2020	-	17.50 -
Sylwia Jaśkiewicz	-	→	-	03.03.2020	04.03.2020	-	15.20 -
Sylwia Jaśkiewicz	-	→	-	30.03.2020	31.03.2020	-	12.25 -
Sylwia Jaśkiewicz	-	→	-	22.04.2020	23.04.2020	-	14.00 -
Sylwia Jaśkiewicz	Overweight	↑	23.04.2020	-	24.04.2020	Not later than 23.04.2021	14.00 53%
Sylwia Jaśkiewicz	-	→	-	19.05.2020	20.05.2020	-	13.65 -
Sylwia Jaśkiewicz	-	→	-	15.06.2020	16.06.2020	-	16.60 -
Sylwia Jaśkiewicz	-	→	-	13.07.2020	14.07.2020	-	17.90 -
Sylwia Jaśkiewicz	-	→	-	22.07.2020	23.07.2020	-	17.00 -
Sylwia Jaśkiewicz	-	→	-	01.09.2020	02.09.2020	-	18.60 -
Sylwia Jaśkiewicz	-	→	-	17.09.2020	18.09.2020	-	18.90 -
Sylwia Jaśkiewicz	-	→	-	29.09.2020	30.09.2020	-	18.70 -
Sylwia Jaśkiewicz	-	→	-	08.10.2020	09.10.2020	-	19.00 -
Sylwia Jaśkiewicz	-	→	-	03.11.2020	04.11.2020	-	17.30 -
Sylwia Jaśkiewicz	-	→	-	08.11.2020	09.11.2020	-	17.25 -
Sylwia Jaśkiewicz	-	→	-	19.11.2020	20.11.2020	-	18.40 -
Sylwia Jaśkiewicz	-	→	-	26.11.2020	27.11.2020	-	20.00 -
Sylwia Jaśkiewicz	-	→	-	06.12.2020	07.12.2020	-	24.80 -
Sylwia Jaśkiewicz	-	→	-	05.01.2021	05.01.2021	-	25.50 -
Sylwia Jaśkiewicz	-	→	-	28.01.2021	29.01.2021	-	26.50 -
Sylwia Jaśkiewicz	-	→	-	09.02.2021	10.02.2021	-	25.70 -
Sylwia Jaśkiewicz	-	→	-	28.02.2021	01.03.2021	-	26.10 -
Sylwia Jaśkiewicz	-	→	-	31.03.2021	01.04.2021	-	27.00 -

* prices at issue/reiteration are the closing prices at the report or reiteration date

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The report is an investment research within the meaning of Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organizational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive. This report constitutes a recommendation within the meaning of Commission Delegated Regulation (EU) 2016/958 of 9 March 2016 supplementing Regulation (EU) No 596/2014 of the European Parliament and of the Council with regard to regulatory technical standards for the technical arrangements for objective presentation of investment recommendations or other information recommending or suggesting an investment strategy and for disclosure of particular interests or indications of conflicts of interest. This report is for information purposes only.

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This report was prepared with due diligence and scrutiny. The information used in the report is based on all public sources such as press and branch publications, company's financial statements, current and periodic reports, as well as meetings and telephone conversations with company's representatives prior to the date of report's release. We believe the above mentioned sources of information to be reliable, however we do not guarantee their accuracy and completeness. All estimates and opinions included herein represent our judgment as of the date of the issue. All opinions, forecasts, calculations and estimates herein constitute the author's subjective assessment as of the date of the issue and can be modified at any time without prior notice. DM BOŚ SA informs that this report will be updated in the manner as referred to in the Agreement, at least once a year.

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