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This report is prepared for the Warsaw Stock Exchange SA within the framework of the Analytical Coverage Support Program. 3.0. This is an excerpt from the Polish version of DM BOŚ SA's research report.

Analyst: Maciej Wewiórski

Sector: Construction materials
Fundamental rating: Buy (-)
Market relative: Overweight (-)
Price: PLN 15.34
12M EFV: PLN 20.6 (-)

Market Cap: US\$ 61 m
Bloomberg code: GRN PW
Av. daily turnover: US\$ 0.16 m
12M range: PLN 9.00-17.10
Free float: 34.2%

Grodno

The Company provides comprehensive solutions for buildings and belongs to the leading Polish distributors of electrotechnical merchandise and lighting products. With the market share at c. 9% Grodno is the second player on Poland's electrotechnical equipment distributors market worth c. PLN 8 billion. We combined 2 methods in our valuation of the Company; these are the DCF FCF method and peer relative comparison. Our 12M EFV stands at PLN 20.6 per share which is c. 34% above the Company's market price at the moment. We initiate our coverage of Grodno with LT fundamental Buy recommendation and ST relative Overweight rating.

Decarbonization and programs such as the European Green Deal enforce fast and dramatic changes on the electricity and heat market. The Institute for Renewable Energy expects that in 2022 the photovoltaic system capacity should double and in the 2025-end it should reach even 15 GW.

Grodno provides comprehensive solutions for PV installations, starting from a delivery of proper components and installation project through the assembly and handing-over the project to the energy provider as well as it offers assistance in the clearance of grants and installation maintenance afterwards. The Company's client base encompasses households, SMES, local and regional government units, and industrial plants as well.

It is estimated that in 5-10 years heat pumps will be able to replace a considerable part of the solid fuel boilers market in the segment for single-family buildings. Grodno's offer includes heat pumps and heating systems components of leading manufacturers present on the Polish market. The Company provides full technical advice in this respect.

The Company expects a 50% increase in the Group's sales in the area of PV and heat pumps by the financial year of 2022/23 while by 2024/25 the

Guide to adjusted profits

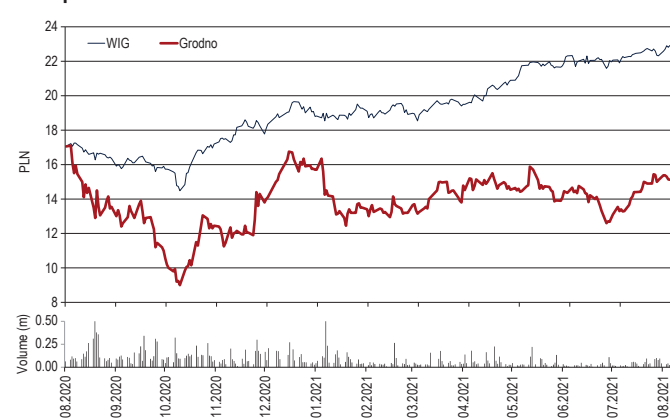
No factors necessitating adjustments.

Key data

IFRS consolidated		2020/21	2021/22E	2022/23E	2023/24E
Sales	PLN m	711.7	961.2	1,057.3	1,141.9
EBITDA	PLN m	24.6	44.4	48.7	52.5
EBIT	PLN m	18.8	36.9	40.6	43.8
Net income	PLN m	13.7	27.2	29.5	32.2
EPS	PLN	0.89	1.77	1.92	2.09
EPS yoy chg	%	19.0	98.1	8.5	8.9
Net debt	PLN m	63.9	98.3	104.1	97.1
P/E	x	17.2	8.7	8.0	7.3
P/CE	x	12.0	6.8	6.3	5.8
EV/EBITDA	x	12.2	7.5	7.0	6.3
EV/EBIT	x	16.0	9.1	8.4	7.6
EV/Sales	x	0.4	0.3	0.3	0.3
Gross dividend yield	%	0.5	1.4	3.5	3.8
DPS	PLN	0.08	0.21	0.53	0.58
No. of shares (eop)	m	15.4	15.4	15.4	15.4

Source: Company, DM BOŚ SA estimates

Stock performance



Source: Bloomberg

Upcoming events

1. Financial results release for 1H21/22: December 16
2. Financial results release for 3Q21/22: February 1, 2022

RES segment should contribute 35% of consolidated revenues. Besides, apart from strengthening its position in the RES market, Grodno intends to pursue further development of a sales network and expand its offer in the area of electrotechnology of heating systems.

Catalysts

1. Warehouse space optimization
2. Rising electricity price for end-users
3. New support programs for the RES segment investors
4. Further acquisitions of peer companies (to date Grodno has concluded 10 takeovers)
5. Automation of warehouse storage and distribution processes
6. Successful development of e-commerce channel in B2C and B2B segments

Risk factors

1. Rising generation costs of suppliers because of raw materials prices growth and lack of possibility to transfer the prices growth onto customers
2. Wages growth pressure
3. Sales seasonality
4. Dependence on main suppliers
5. Insolvency of buyers
6. Bad inventories management
7. IT system crashes
8. Impact of the majority shareholders controlling 79.3% of the votes on the GSA
9. Inability to reach strategic goals (annual growth of sales at 10% by 2024/25)
10. Withdrawal/ limits imposed on the government support programs for the RES segment investors
11. Inability to continue further lucrative acquisitions of peer companies
12. COVID-19 pandemic (shortages of components necessary for production or lack of goods due to broken supply chains)

Competitive advantages

1. Strong geographic diversification (one of the most extensively developed sales network among independent distributors of electrotechnical materials)
2. Exposure to the fast growing segments of the electrotechnical market (photovoltaics and heat pumps currently, earlier LED lighting)
3. Complex offer including consulting services, design and construction
4. Numerous acquisitions all of which proved to be value accretive
5. A vast client base including households, SMES, local and regional government units, and industrial plants as well
6. Lack of dependence on one/few suppliers
7. Multiple points of sale (suppliers more willing to cooperate with the big partner with a well-developed logistic base)

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	Not rated
Numbers	49	22	5	10	0	1
Percentage	56%	25%	6%	11%	0%	1%

Distribution of DM BOŠ's current market relative recommended weightings

	Overweight	Neutral	Underweight	Suspended	Under revision	Not rated
Numbers	39	27	10	10	0	1
Percentage	45%	31%	11%	11%	0%	1%

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	Not rated
Numbers	10	4	0	1	0	1
Percentage	63%	25%	0%	6%	0%	6%

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	Not rated
Numbers	6	6	2	1	0	1
Percentage	38%	38%	13%	6%	0%	6%

LT fundamental recommendation tracker

Analyst	Recommendation	Report date	Reiteration date	Distribution date	Expiry date	Performance	Relative performance	Price at issue/ reiteration*	EFV (12 months)		
Grodno											
Maciej Wewiórski	Buy	–	31.08.2021	-	31.08.2021	Not later than 31.08.2022	-	-	15.34	20.60	-

* 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	
Grodno								
Maciej Wewiórski	Overweight	–	31.08.2021	-	31.08.2021	Not later than 31.08.2022	15.34	-

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

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The report was not shown to the analyzed company before the distribution of the report.

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