

3/2023/GPW (9) March 2, 2023

This report is prepared for the Warsaw Stock Exchange SA within the framework of the Analytical Coverage Support Program 3.0.

Grodno

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Analyst: Maciej Wewiórski

Grodno

Sector: Construction materials

Fundamental rating: Buy (→)

Market relative: Neutral (→)

Price: PLN 13.22

12M EFV: PLN 17.30 (→)

Market Cap: US\$ 46 m

Bloomberg code: GRN PW

Av. daily turnover: US\$ 0.1 m

12M range: PLN 12.34-20.50

Free float: 34.2%

Recommended action

Due to a slump in the construction and assembly industry we expect the demand for traditional electrotechnical goods to weaken. At the same time however the Company may experience a growing demand in the RES segment (photovoltaic installations and heat pumps). We believe that the Company's business perspectives in the long term look favorable, therefore our LT fundamental Buy recommendation stays intact.

3Q22/23 financial results review

3Q22/23 results are good and beating our expectations. Sales did not surprise the market as the Company reports regularly monthly estimations. The meager sales growth (+3% yoy in 3Q22/23 vs +6% in 1-3Q22/23) stems from the high base effect coupled with a slowdown in the construction and electrotechnical markets observed from the beginning of 2022. The high base results mainly from the change of photovoltaic installations accounting system for prosumers in force since April last year. It is worth reminding that in 4Q21 a number of PV installations connections reached c. 141,000 while in 4Q22 it was merely 33,000.

Our concerns for falling margins did not come true. The Company managed to improve the EBITDA and EBIT margins qoq.

Due to the need to be well stocked with heat pumps Grodno's working capital requirements are high. At the same time the Company manages to maintain operational efficiency. The working capital to sales ratio is almost flat yoy, so is the inventory to revenue ratio.

Guide to adjusted profits

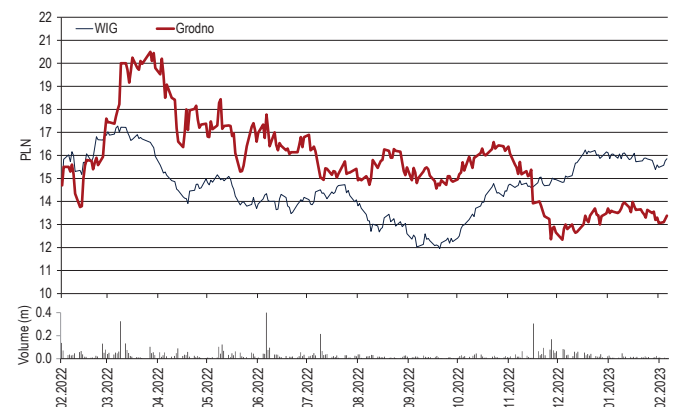
No factors necessitating adjustments.

Key data

IFRS consolidated		2021/22	2022/23E	2023/24E	2024/25E
Sales	PLN m	1,196.0	1,198.2	1,317.4	1,422.8
EBITDA	PLN m	64.1	50.0	54.8	58.5
EBIT	PLN m	57.0	41.5	46.1	49.8
Net income	PLN m	43.8	28.6	30.7	35.6
EPS	PLN	2.85	1.86	1.99	2.31
EPS yoy chg	%	218.5	-34.6	7.2	16.0
Net debt	PLN m	54.5	92.7	78.8	64.9
P/E	x	4.6	7.1	6.6	5.7
P/CE	x	4.0	5.5	5.2	4.6
EV/EBITDA	x	4.0	5.9	5.1	4.6
EV/EBIT	x	4.5	7.1	6.1	5.4
EV/Sales	x	0.2	0.2	0.2	0.2
Gross dividend yield	%	1.6	6.4	3.9	6.0
DPS	PLN	0.21	0.84	0.52	0.80
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. Release of the financial report for 4Q22/23: July 2023
2. Release of the financial report for 1Q23/24: August 2023
3. Release of the financial report for 2Q23/24: December 2023
4. Release of the financial report for 3Q23/24: February 2024

Fig. 1. Grodno; 3Q22/23 financial results

IFRS, consolidated (PLN m)	3Q22/23	3Q21/22	yoy chg	3Q22/23E DM BOŚ	Results vs forecasts	1-3Q22/23	1-3Q21/22	yoy chg
Sales	346.7	335.4	3%	344.6	→	931.0	877.3	6%
EBITDA	14.1	19.3	-27%	12.4	↑	39.1	47.1	-17%
EBITDA margin	4.1%	5.7%	-	3.6%	↑	4.2%	5.4%	-
EBIT	11.8	17.4	-32%	10.4	↑	32.9	41.9	-22%
EBIT margin	3.4%	5.2%	-	3.0%	↑	3.5%	4.8%	-
Net income	8.6	13.3	-35%	6.4	↑	22.4	32.6	-31%
Net income margin	2.5%	4.0%	-	1.9%	↑	2.4%	3.7%	-

Source: Company, DM BOŚ SA estimates

4Q22/23 financial results preview

The Company's 4Q22/23 financials will be probably released in the end of July.

We do not expect big surprises at the top line level as the Company reports monthly revenues estimates. In January and February Grodno's revenues reached PLN 87.3 million and PLN 93.9 million, respectively, and for March we forecast PLN 95 million, albeit last year's March base is very high due to the later change of photovoltaic installations accounting system for prosumers (from April 2022).

With regard to profits we assume the EBITDA margin to stay flat qoq close to 4.1% vs 5.3% in 4Q21/22. We believe, this expected yoy fall of profitability stems from a drop in the demand for traditional electrotechnical goods caused by a slowdown in the construction and assembly industry and smaller interest in PV installations.

Financial forecasts and valuation

Incorporating our expectations for 4Q22/23 we slightly modify our FY22/23 (ending in March this year) forecasts. Our valuation of the Company's equities stays intact.

Fig. 2. Grodno; 4Q22/23 financial results forecast

IFRS consolidated (PLN m)	4Q22/23E	4Q21/22	yoy chg	Realization of the full-year figures in 4Q:	
				2022/23E	2021/22
Sales	267.2	318.7	-16%	22%	27%
EBITDA	11.0	17.0	-36%	22%	27%
EBITDA margin	4.1%	5.3%	-	-	-
EBIT	8.7	15.1	-43%	21%	27%
EBIT margin	3.2%	4.7%	-	-	-
Net income	6.2	11.2	-44%	22%	26%
Net income margin	2.3%	3.5%	-	-	-

Source: Company, DM BOŚ SA

Fig. 3. Grodno; Changes in DM BOŚ's forecasts

IFRS consolidated (PLN m)	2022/23E		
	current	previous	change
Sales	1 198,2	1 219,8	-2%
EBIT	41,5	40,3	3%
Net income	28,6	26,7	7%
Net debt	92,7	92,7	0%

Source: DM BOŚ SA estimates

Catalysts

1. Warehouse space optimization
2. Rising electricity prices 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. Pressure on wages growth
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 from/ 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 fallout (shortages of components necessary for the 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. Comprehensive 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 BOŚ 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 BOŚ 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 BOŚ's current recommendations

	Buy	Hold	Sell	Suspended	Under revision	Not rated
Numbers	40	32	7	9	0	2
Percentage	44%	36%	8%	10%	0%	2%

Distribution of DM BOŚ's current market relative recommended weightings

	Overweight	Neutral	Underweight	Suspended	Under revision	Not rated
Numbers	31	35	13	9	0	2
Percentage	34%	39%	14%	10%	0%	2%

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

	Buy	Hold	Sell	Suspended	Under revision	Not rated
Numbers	6	6	1	1	0	2
Percentage	38%	38%	6%	6%	0%	13%

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

	Overweight	Neutral	Underweight	Suspended	Under revision	Not rated
Numbers	5	4	4	1	0	2
Percentage	31%	25%	25%	6%	0%	13%

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	16.08.2022	4%	30%	15.34	20.60 →
Maciej Wewiórski	-	-	31.08.2021	31.08.2021	-	-	-	15.86	20.60 →
Maciej Wewiórski	-	-	07.10.2021	07.10.2021	-	-	-	15.60	20.60 →
Maciej Wewiórski	-	-	01.11.2021	02.11.2021	-	-	-	15.96	20.39 ↓
Maciej Wewiórski	-	-	04.11.2021	04.11.2021	-	-	-	16.42	20.39 →
Maciej Wewiórski	-	-	16.11.2021	17.11.2021	-	-	-	16.82	23.30 ↑
Maciej Wewiórski	-	-	05.12.2021	06.12.2021	-	-	-	16.10	23.30 →
Maciej Wewiórski	-	-	16.01.2022	17.01.2022	-	-	-	17.24	23.30 →
Maciej Wewiórski	-	-	07.02.2022	07.02.2022	-	-	-	18.10	23.30 →
Maciej Wewiórski	-	-	28.02.2022	28.02.2022	-	-	-	15.50	23.30 →
Maciej Wewiórski	-	-	14.04.2022	14.04.2022	-	-	-	19.98	23.30 →
Maciej Wewiórski	-	-	24.04.2022	25.04.2022	-	-	-	19.80	26.60 ↑
Maciej Wewiórski	-	-	26.05.2022	26.05.2022	-	-	-	17.48	26.60 →
Maciej Wewiórski	-	-	07.06.2022	08.06.2022	-	-	-	17.28	26.60 →
Maciej Wewiórski	-	-	15.07.2022	15.07.2022	-	-	-	16.14	26.60 →
Maciej Wewiórski	-	-	08.08.2022	09.08.2022	-	-	-	15.16	26.60 →
Maciej Wewiórski	Buy	16.08.2022	-	16.08.2022	Not later than 16.08.2023	-16%	-21%	15.74	26.60 →
Maciej Wewiórski	-	-	02.09.2022	02.09.2022	-	-	-	15.80	26.60 →
Maciej Wewiórski	-	-	07.10.2022	07.10.2022	-	-	-	15.12	26.60 →
Maciej Wewiórski	-	-	28.10.2022	28.10.2022	-	-	-	15.34	26.60 →
Maciej Wewiórski	-	-	14.11.2022	14.11.2022	-	-	-	16.28	24.30 ↓
Maciej Wewiórski	-	-	01.12.2022	01.12.2022	-	-	-	15.72	24.30 →
Maciej Wewiórski	-	-	04.12.2022	05.12.2022	-	-	-	15.18	24.30 →
Maciej Wewiórski	-	-	22.12.2022	23.12.2022	-	-	-	12.90	17.30 ↓
Maciej Wewiórski	-	-	13.01.2023	13.01.2023	-	-	-	13.38	17.30 →
Maciej Wewiórski	-	-	03.02.2023	03.02.2023	-	-	-	13.96	17.30 →
Maciej Wewiórski	-	-	10.02.2023	10.02.2023	-	-	-	13.64	17.30 →
Maciej Wewiórski	-	-	02.03.2023	02.03.2023	-	-	-	13.22	17.30 →

* 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	16.08.2022	15.34	30%
Maciej Wewiórski	-	-	31.08.2021	31.08.2021	-	15.86	-
Maciej Wewiórski	-	-	07.10.2021	07.10.2021	-	15.60	-
Maciej Wewiórski	-	-	01.11.2021	02.11.2021	-	15.96	-
Maciej Wewiórski	-	-	04.11.2021	04.11.2021	-	16.42	-
Maciej Wewiórski	-	-	16.11.2021	17.11.2021	-	16.82	-
Maciej Wewiórski	-	-	05.12.2021	06.12.2021	-	16.10	-
Maciej Wewiórski	-	-	16.01.2022	17.01.2022	-	17.24	-
Maciej Wewiórski	-	-	07.02.2022	07.02.2022	-	18.10	-
Maciej Wewiórski	-	-	28.02.2022	28.02.2022	-	15.50	-
Maciej Wewiórski	-	-	14.04.2022	14.04.2022	-	19.98	-
Maciej Wewiórski	-	-	24.04.2022	25.04.2022	-	19.80	-
Maciej Wewiórski	-	-	26.05.2022	26.05.2022	-	17.48	-
Maciej Wewiórski	-	-	07.06.2022	08.06.2022	-	17.28	-
Maciej Wewiórski	-	-	15.07.2022	15.07.2022	-	16.14	-
Maciej Wewiórski	-	-	08.08.2022	09.08.2022	-	15.16	-
Maciej Wewiórski	Overweight	16.08.2022	-	16.08.2022	22.12.2022	15.74	-19%
Maciej Wewiórski	-	-	02.09.2022	02.09.2022	-	15.80	-
Maciej Wewiórski	-	-	07.10.2022	07.10.2022	-	15.12	-
Maciej Wewiórski	-	-	28.10.2022	28.10.2022	-	15.34	-
Maciej Wewiórski	-	-	14.11.2022	14.11.2022	-	16.28	-
Maciej Wewiórski	-	-	01.12.2022	01.12.2022	-	15.72	-
Maciej Wewiórski	-	-	04.12.2022	05.12.2022	-	15.18	-
Maciej Wewiórski	Neutral	22.12.2022	-	23.12.2022	Not later than 22.12.2023	12.90	-2%
Maciej Wewiórski	-	-	13.01.2023	13.01.2023	-	13.38	-
Maciej Wewiórski	-	-	03.02.2023	03.02.2023	-	13.96	-
Maciej Wewiórski	-	-	10.02.2023	10.02.2023	-	13.64	-
Maciej Wewiórski	-	-	02.03.2023	02.03.2023	-	13.22	-

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

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The production of the report was completed on March 2, 2023 at 5.25 p.m.

The report was distributed on March 2, 2023 at 5.35 p.m.

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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DM BOŚ SA has not held any long or short position net exceeding 0.5% of the issuer's basic capital in total with respect to the company/companies indicated.

During the last 12 months DM BOŚ S.A rendered investment services on behalf of Grodno S.A. pursuant to the agreement signed and received a remuneration by virtue of this.

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Stockbrokers

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