

Integer.pl

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Analysts: Adrian Kyrzcz, a.kyrzcz@idmsa.pl, +48 (22) 489 94 74
Marek Kaźmierczak, m.kaźmierczak@idmsa.pl, +48 (22) 489 94 64

Sector: Consumer discretionary
Fundamental rating: Buy (→)
Market relative: Overweight (→)
Price: PLN 59.0
12M EFV: PLN 72.8 (→)

Market Cap.: US\$ 121 m
Reuters code: ITGRWA
Av. daily turnover: US\$ 0.07 m
Free float: 49%
12M range: PLN 15.45-67.45

Quarterly
Results Preview

Investment story & recommendation

With double-digit fundamental upside to our 12M EFV (maintained at PLN 72.8 per share) we reiterate our LT fundamental Buy recommendation and ST market-relative Overweight bias for Integer.pl's equities. We view Integer.pl as a typical 'growth' company, with impressive business track record and an appealing long-term investment story, commanding (i) strong profits growth in 2010E and in the following years (we forecast the Company's 2010-2013 EBIT and NP CAGRs both at 50%), (ii) a robust business model (continued inflow of new clients unhappy with the services provided by the Polish Post), (iii) a well-conceived strategy of launching new innovative postal services (including e-commerce market), and (iv) great effectiveness in winning EU funding (in the next two years we expect the Company to be granted as much as PLN 45 million for its services development). Additionally, 1Q10 results of the Company (envisaged top line/ EBIT yoy growth of approx. 70%/ 60%) should, in our view, once again reinforce the investors' confidence in Integer's ability to monetize its market share gains.

Quarterly results corner; 1Q10E preview

Integer.pl will release its consolidated results for 1Q10 on May 17, 2010. Although we expect the Company's quarterly results to be burdened by one-off costs incurred in relation to the "Paczkomaty" project development (promotion), and in spite of more aggressive pricing policy initiated by Poczta Polska in the past few months, we forecast material yoy and qoq improvement of the Company's operating profits in 1Q10, which – in our view – should be applauded by the investors.

We forecast the Company's quarterly sales at PLN 42.0 million, which marks 72% increase yoy. Sales growth should be driven by the projected increase in postal deliveries. Please note that we forecast the Company to deliver approx. 31 million items of mail in 1Q10 vs. 29 million in 4Q09 and c. 11.3 million in 1Q09, which should translate into c. PLN 32.5 million of sales generated by the postal division in the quarter (vs. PLN 9 million in 1Q09 and PLN 31.9 million in 4Q09). We forecast Integer.pl's quarterly revenues from unaddressed distribution at PLN 8.9 million (broadly flat yoy), which we would view as a good result in the light of the unaddressed distribution market's generally poor performance.

We expect the Company to show strong quarterly operating profit (up by c. 64% yoy), despite the envisaged one-off costs incurred in 1Q10 for the promotion of the "Paczkomaty" project. In our view, the reason for this will be rising efficiency stemming from the Company's increasing scale of operations (which we also expect to support the margins in the following quarters).

Guide to adjusted profits

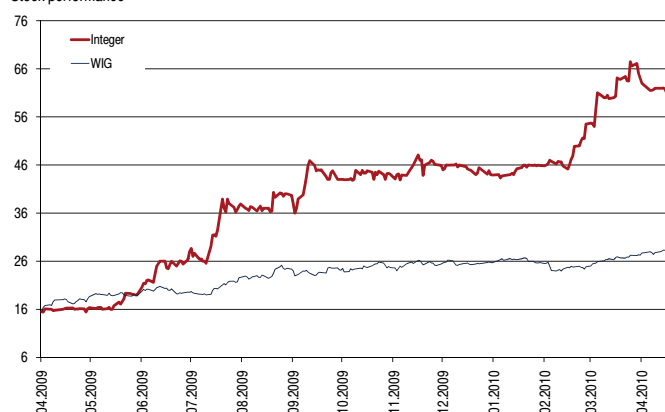
No factors necessitating adjustments.

Key data

IFRS consolidated		2009	2010E	2011E	2012E	2013E
Sales	PLN m	139.9	228.3	299.3	364.7	398.1
EBITDA	PLN m	16.9	31.9	38.8	44.6	75.9
EBIT	PLN m	13.2	24.9	31.1	36.3	67.0
Net profit	PLN m	10.2	17.3	22.4	27.7	54.5
EPS	PLN	1.72	2.91	3.78	4.66	9.17
EPS yoy chng	%	58	69	30	23	97
FCFF	PLN m	-23.9	-15.6	9.7	17.1	56.6
Net debt	PLN m	29.8	40.8	7.9	-12.9	-72.5
P/E	x	34.2	20.2	15.6	12.7	6.4
P/CE	x	25.1	14.4	11.6	9.7	5.5
EV/EBITDA	x	22.5	12.2	9.2	7.6	3.7
EV/EBIT	x	28.8	15.7	11.5	9.3	4.1
EV/Sales	x	2.7	1.7	1.2	0.9	0.7
Gross dividend yield	%	0.0	0.0	0.0	0.0	0.0
No. of shares (eop)	m	5.9	5.9	5.9	5.9	5.9

Source: Company, DM IDMSA estimates

Stock performance



Source: ISI

Upcoming events

1. Release of FY09 consolidated results: April 30, 2010
2. Release of 1Q10 consolidated results: May 17, 2010
3. Release of 1H10 consolidated results: August 31, 2010
4. Release of 3Q10 consolidated results: November 15, 2010

Catalysts

1. Poor performance of the incumbent (Polish Post)
2. Full liberalization of the postal market in 2013
3. Low risk of increased competition in the domestic market in the mid-term
4. Steadily growing saturation of alternative operator friendly mail boxes ('Euroboxes') in Poland
5. Probably the best price to value offer on the market
6. Launch of new products and services
7. Achieving the economies of scale
8. Defensive customer base
9. New products ('Paczkomaty', 'Hybrid Post') success

10. Foreign expansion (if successful)
11. Beneficiary of EU funding

Risk factors

1. Delays in full liberalization of the postal market in 2013
2. Growing competition in the long-term
3. New products ('Paczkomaty', 'Hybrid Post') failure
4. Protracted stagnation/decline of the unaddressed distribution market
5. FX risk (CIRS)
6. Foreign expansion (if unsuccessful)

On the back of projected yoy increase of the Company's net debt in 1Q10 (and – consequently – envisaged higher yoy financial costs (please note that as of the end of 2009 the Company's net debt was PLN 29.8 million vs. PLN 0.7 million as of the end of 2008)), as well as assumed 1Q10E effective CIT rate at a statutory level of 19% in comparison to PLN 0.3 million of deferred tax assets recognized in the base quarter of 1Q09, we forecast 'only' 25% yoy increase of the reported quarterly bottom line.

Fig. 1 Integer.pl; 1Q10 results forecast

IFRS consolidated PLN m			yoy change	Realization of the FY figures in 1Q:	
	1Q10E	1Q09A		2010E	2009
Sales	42.0	24.4	72%	18%	17%
EBIT	5.2	3.2	64%	21%	24%
<i>EBIT margin</i>	<i>12.5%</i>	<i>13.1%</i>	-	-	-
Pre-tax profit	4.5	2.6	72%	21%	20%
<i>Pre-tax margin</i>	<i>10.8%</i>	<i>10.8%</i>	-	-	-
Net profit	3.7	2.9	25%	21%	28%
<i>Net margin</i>	<i>8.8%</i>	<i>12.0%</i>	-	-	-

Source: Company, DM IDMSA estimates

Financial forecast

We keep our full-year financial forecasts for Integer.pl unchanged.

Valuation

Our 12M per share EFV for Integer.pl (constituting a 50%-50% mix of the outcomes of the DCF and peer-relative exercises) continues to dwell at PLN 72.8 per share.

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)
Integer.pl								
Buy	-	08.06.2009	-	31.08.2009	84%	49%	21.60	40.10 -
-	→	-	06.07.2009	-	-	-	26.40	40.10 →
-	→	-	08.07.2009	-	-	-	26.00	40.10 →
-	→	-	02.08.2009	-	-	-	37.88	40.10 →
Hold	↓	31.08.2009	-	17.12.2009	13%	9%	39.69	45.30 ↑
-	→	-	12.10.2009	-	-	-	44.00	49.00 ↑
-	→	-	14.12.2009	-	-	-	45.75	49.00 →
Buy	↑	17.12.2009	-	01.03.2010	22%	23%	45.00	51.30 ↑
-	→	-	07.01.2010	-	-	-	43.80	51.30 →
-	→	-	03.02.2010	-	-	-	46.30	51.30 →
Hold	↓	01.03.2010	-	17.03.2010	17%	9%	54.70	51.30 →
Buy	↑	17.03.2010	-	Not later than 17.03.2010	-8%	-11%	64.10	72.80 ↑
-	→	-	29.03.2010	-	-	-	67.10	72.80 →
-	→	-	20.04.2010	-	-	-	59.00	72.80 →

Market-relative recommendation tracker

Relative recommendation		Issue date	Reiteration date	Expiry date	Price at issue/reiteration (PLN)	Relative performance
Integer.pl						
Overweight	-	08.06.2009	-	31.08.2009	21.60	49%
-	→	-	06.07.2009	-	26.40	-
-	→	-	08.07.2009	-	26.00	-
-	→	-	02.08.2009	-	37.88	-
Neutral	↓	31.08.2009	-	12.10.2009	39.69	10%
Overweight	↑	12.10.2009	-	01.03.2010	44.00	22%
-	→	-	14.12.2009	-	45.75	-
-	→	-	17.12.2009	-	45.00	-
-	→	-	07.01.2010	-	43.80	-
-	→	-	03.02.2010	-	46.30	-
Neutral	↓	01.03.2010	-	17.03.2010	54.70	9%
Overweight	↑	17.03.2010	-	Not later than 17.03.2010	64.10	-11%
-	→	-	29.03.2010	-	67.10	-
-	→	-	20.04.2010	-	59.00	-

Distribution of IDM's current recommendations

	Buy	Hold	Sell	Suspended	Under revision
Numbers	20	31	15	1	0
Percentage	30%	46%	22%	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	24	24	18	1	0
Percentage	36%	36%	27%	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%

Institutional sales

Director – **Dariusz Wareluk**
tel.: +48 (22) 489 94 12
d.wareluk@idmsa.pl

Leszek Mackiewicz

tel.: +48 (22) 489 94 23
l.mackiewicz@idmsa.pl

Maciej Bąk

tel.: +48 (22) 489 94 14
m.bak@idmsa.pl

Bartosz Zieliński

tel.: +48 (22) 489 94 13
b.zielinski@idmsa.pl

Research

Sobiesław Pająk, CFA
(IT, Media, Equity strategy)

tel.: +48 (22) 489 94 70
s.pajak@idmsa.pl

Sylwia Jaśkiewicz, CFA

(Construction materials, Retail, Mid-caps)
tel.: +48 (22) 489 94 78
s.jaskiewicz@idmsa.pl

Maciej Wewiórski

(Commodities, Construction, Real estate)
tel.: +48 (22) 489 94 62
m.wewiorski@idmsa.pl

Michał Sobolewski, CFA

(Banks)
tel.: +48 (22) 489 94 77
m.sobolewski@idmsa.pl

Jakub Viscardi

(Telco, Retail)
tel.: +48 (22) 489 94 69
j.viscardi@idmsa.pl

Adrian Kyrzcz

(Construction)
tel.: +48 (22) 489 94 74
a.kyrzcz@idmsa.pl

Łukasz Prokopiuk

(Chemicals)
tel.: +48 (22) 489 94 72
l.prokopiuk@idmsa.pl

Marek Kaźmierczak

(Associate)
tel.: +48 (22) 489 94 64
m.kazmierczak@idmsa.pl

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