

KGL *summary of report*

neutral

plastic packaging

previous recommendation: neutral

Current price: 11.7

Target price: 12.0

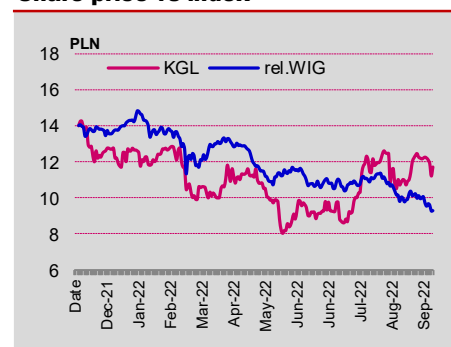
The company is catching its breath

KGL's results in the second quarter positively surprised us and the company improved its EBIT y/y for the first time since 2020 (PLN 5.1 million vs. PLN 4.8 million a year earlier and our expectation of PLN 1.9 million). We believe that the company is starting to benefit from renegotiated contracts and the beginning of a downward trend in commodity prices. It is possible that the worst for the company is over, but the rising energy costs will be a challenge. KGL had a net debt of PLN 128.4 million at the end of June 2022, which was 3.9x EBITDA for the last four quarters. Debt remains a significant problem, but has recently remained stable. Due to the rebound in margins, we are slightly raising our earnings forecasts for this year and, more clearly, for the coming years. We are increasing our valuation of 1 KGL share from PLN 9.3 to PLN 12.0. At the same time, with the current price of PLN 11.7 per share, we maintain our neutral recommendation.

Our valuation and recommendation assume an improvement in margins in the coming quarters. In the past, the company has improved its results when raw material (plastic) prices have fallen, which has been happening in recent months. The price of polypropylene in PLN has already dropped by 32% compared to the peak in April, and the price of PET has fallen by 17% from the peak in July. This means that the very strong pressure on margins visible in the previous quarters should decrease significantly (which was visible in Q2). KGL in the first half of the year renegotiated contracts with product recipients, which was also supposed to improve profitability. On the other hand, the renegotiations were supposed to result in a faster adjustment of product prices to changes in the prices of raw materials. This may mean that the fall in plastic prices will not expand margins, as was the case in the past. An additional risk is the strong increases in energy costs. If they are not fully transferred to customers, the annual result may be reduced by several or several dozen million PLN.

The Management Board of KGL made a decision on the possible reclassification of the real estate owned and the change of the financing model for selected assets. The aim is to optimize the use of owned assets from the point of view of operational processes, to improve the costs of financing the business and the asset financing model. The Management Board will consider potential scenarios in terms of possible directions of use of the real estate, not excluding the sale of selected assets and a change in the formula of their use. We believe that the management board's decision stems from the difficult financial situation, especially high debt. The company may be looking for ways to debt relief by selling real estate, although this is probably not the best time to look for a buyer. It is also possible to increase the debt secured on real estate and reduce the share of leasing, which is more expensive. Possible decisions may result from pressure from banks.

Share price vs index



Max/min 52 weeks (PLN)	17.4 / 9.7		
Shares issued (m)	7,2		
Market cap. (m PLN)	84		
EV (m PLN)	206		
Free float (m PLN)	20		
Average turnover (m PLN)	0,1		
Main shareholders	Krzysztof Gromkowski, Ireneusz Strzelczak, każdy po:		
% of shares, % of votes	19.06%, 21.19%		
	1 m	3 m	12 m
Price change	6,4%	20,1%	-25,5%
Change rel. WIG	14,9%	34,5%	9,3%

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	Sales	EBIT	EBITDA	Profit before tax	Net profit	EPS	CEPS	BVPS	P/E	P/BV	DY (%)	EV /EBIT	EV /EBITDA	ROE (%)
2021	575,8	11,5	37,2	7,0	5,2	0,73	4,33	18,7	16,0	0,6	3,0	17,9	5,5	4,0
2022p	692,2	13,4	38,8	0,4	0,3	0,05	3,59	18,8	254,9	0,6	0,0	15,3	5,3	0,2
2023p	774,8	19,7	43,5	7,8	6,3	0,89	4,22	19,7	13,2	0,6	0,0	10,5	4,7	4,7
2024p	799,3	22,2	44,7	13,3	10,8	1,50	4,65	21,2	7,8	0,6	0,0	9,3	4,6	7,6

p - forecasts BM Bank Millennium, mn PLN

The report was prepared by Millennium Dom Maklerski S.A. on the order of the Warsaw Stock Exchange S.A. within the Program of Analytical Coverage Support Information regarding the links between Millennium Dom Maklerski S.A. with the company being the subject of this report and other required information were placed on the last page of the report.

Risk factors:

The most important risk factors that may affect the operations of KGL company include:

- **Regulatory risks.** The EU tries to influence the limitation of the use of plastic and increase the share of its recycling through restrictions and taxes. The impact of these regulations on the company is difficult to determine at the moment without knowing the details of the regulations being implemented. The fact that plastic is negatively perceived by lawmakers is certainly a threat to the industry.
- **Risk of exchange rates and commodity prices.** A significant part of goods and materials is purchased in foreign currencies (mainly EUR). Due to higher liabilities in EUR than receivables in EUR, the unrealized negative exchange rate differences with a 1% increase in EUR / PLN would amount to approx. PLN 0.67 million (sensitivity at the end of 2021). The prices of raw materials depend to a large extent on oil prices. As a result of the increase in oil prices, the company's revenues and costs are rising, but at the same time the margin decreases and the net effect is negative.
- **The risk of rising remuneration costs and shortage of employees.** The share of employee costs in total costs was growing systematically (from 19.3% in 2015 to 22.6% in 2021) as a result of employee shortages and growing wage pressure.
- **The risk of a conflict of interest.** In the company, four long-term managers and founders hold a total of 84.5% of votes at the company's AGM. Additionally, four members of the supervisory board have family ties to them. In such a situation, there is a risk of a conflict of interest at the expense of minority shareholders (mitigated by two independent members of the supervisory board).
- **Risk of over-indebtedness.** After 4 years of intensive investments, the company significantly increased its interest debt reaching the level of 3.3x adjusted EBITDA, with simultaneous significant financing by suppliers.

The risks that we consider to be high include regulatory issues (political decisions are quite unpredictable and have a large impact on the company), indebtedness and the risk of commodity prices.

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Explanation of the professional terminology used in the report

EV - market valuation of the company + net interest debt
EBIT - operating profit
EBITDA - operating profit + depreciation
P/CE - ratio of the share price to net profit per share plus depreciation per share
P/E - ratio of the share price to the net profit per share
P/BV - ratio of the share price to the book value per share
ROE - return on equity
ROA - return on assets
EPS - net profit per share
CEPS - net profit and depreciation per share
BVPS - book value per share
DPS - dividend per share

The scale of recommendation used in Biurow Maklerskie Banku Millennium S.A.

BUY - we believe that the company's shares have more than 20% upside potential
ACCUMULATE - we believe that the company's shares have more than 10% upside potential
NEUTRALALLY - we believe that the price of the company's shares will remain stable (+/- 10%)
REDUCE - we think that the company's shares are overvalued by 10-20%
SELL - we believe that the company's shares are overvalued by over 20%

Recommendations issued by Biurow Maklerskie Banku Millennium S.A. are valid for 6 months from the date of issue, unless they are previously updated. Biurow Maklerskie Banku Millennium S.A. updates the issued recommendations depending on the market situation and the analyst's assessment.

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The recommendations are based on the following valuation methods (selected 2 out of 3): DCF method (discounted cash flow model) - the method considered the most suitable for the valuation of enterprises. The disadvantage of the DCF method is the sensitivity of the valuation obtained in this way to the adopted assumptions concerning both the company itself and its macroeconomic environment. Comparable companies method (comparison of relevant market indicators, where a company with a similar ratios for other companies in the same industry or related industries is listed) - better than the DCF method reflects the perception of the industry in which the company operates, by investors. The disadvantage of the comparable companies method is the sensitivity to the selection of the adopted comparative group and the indicators being compared, as well as the high variability of the valuation depending on the market situation. ROE-P / BV method (a model that makes the right P / BV ratio dependent on the company's profitability) - the method considered the most suitable for the valuation of banks. The disadvantage of this method is the sensitivity of the valuation obtained in this way to the adopted assumptions regarding both the company itself (profitability, effectiveness) and its macroeconomic environment.

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The work related to the preparation of the report was completed on October 3, 2022 at 8:00 am, the date of the first dissemination of the report is the date of the report, October 3, 2022 at 9:00 am.

BM Bank Millennium S.A. recommendations for the last 12 month

Company	Recommendation	Date of the recommendation	Market price on the day of recommendation issue	Target price	Author
KGL	Neutral	2021-10-13	15,0	15,6	Marcin Palenik
Selvita	Neutral	2021-12-14	86,0	78,2	Marcin Palenik
Agora	Buy	2021-12-20	6,66	16,2	Adam Zajler
Ambra	Buy	2022-03-08	21,00	28,5	Marcin Palenik
Mostostal Zabrze	Buy	2022-03-31	1,56	3,50	Adam Zajler
Selvita	Neutral	2022-04-27	78,1	77,0	Marcin Palenik
KGL	Neutral	2022-05-16	9,9	9,3	Marcin Palenik
Agora	Buy	2022-06-10	5,6	10,4	Adam Zajler
Mostostal Zabrze	Buy	2022-09-12	1,8	3,2	Adam Zajler
Ambra	Buy	2022-09-20	20,4	25,6	Marcin Palenik

Source: BM Bank Millennium S.A., recommendations issued by BM Bank Millennium are valid for 6 months from the date of issue, unless updated earlier.

Ambra, Agora, KGL and Mostostal Zabrze participate in the WSE Program of Analytical Coverage Support, for which BM Bank Millennium receives remuneration.

Structure of BM Bank Millennium S.A. recommendations for the last 12 months

	Number of recommendat	% share
Buy	6	60%
Accumulate	0	0%
Neutrally	4	40%
Reduce	0	0%
Sell	0	0%

Structure of BM Banku Millennium DM recommendations for companies for which Millennium DM S.A. provided investment banking services*

No recommendation was issued for companies for which Millennium DM S.A. provided investment banking services *

*last 12 months, including companies for which BMBM S.A. is a market maker