# AC

# Temporary deceleration

**Disappointing 2Q20 preliminary results have revealed that the impact of the coronavirus on the auto gas segment is stronger than we had initially expected. We assume that 3Q/4Q20 results will also be weaker on a y/y basis due to omnipresent restrictions resulting in lower demand from foreign markets. Higher demand for kits for tow bars and recent supportive changes from the Russian market should partially offset poorer results and cause only a temporary deceleration for AC. Thus, we downgrade our recommendation for AC to a HOLD and slightly increase our fair value from PLN 40.80 to PLN 42.00 per share, which implies 5% upside potential. Based on our forecasts, AC trades at a 2020E P/E of 18.8x. This is a 14% premium to the median of peer multiples. On our forecasts, AC trades at 2020 EV/EBITDA of 10.8x, a 19% premium to peers.**

**Supportive changes in the Russian market.** According to the Eurasian Economic Commission, introduction of regulations regarding admission and registration of cars with gas installations which could prove highly negative for AC, has been postponed by one year to July 2021 due to spread of the coronavirus infection. Moreover, Russian government increased the share of budget subsidy for the purpose of conversions to CNG from 30% to 60% for medium-sized enterprises and citizens impacted by the coronavirus. Another 30 percent of expenses will be subsidized by Gazprom. The government estimates 10-12 thousand cars will be converted togas this year as a result of the program vs 15 thousand cars converted in 2019. We assume that these changes will strengthen AC's position on the Russian market and estimate an increase in revenues in Russia from PLN 18m in 2020 to PLN 27m in 2021 and 10% growth in ensuing years.

**Dividend to be maintained.** AC reported that the management has recommended PLN 1.25 DPS (DY of 3.1%) which is broadly in line with our previous assumption of PLN 1.5 DPS (50% DPR). We maintain our assumption that the company will maintain its dividend policy given the end of its intensive CAPEX program and strong balance sheet with a quite conservative long-term 80% DPR after 2020. Our assumption translates into PLN 1.7 (4.3% DY) in 2021E.

**2Q20E results preview.** We expect 59% lower revenues y/y in the sequential gas injection system segment, amounting to PLN 18.8m, due to low gasoline prices, reduction of used car imports, disruption in global logistics, weakening of business partners' local currencies against the EUR and USD and all social distancing rules affecting mobility and other restrictions. Kits for the towing hook segment will be a positive surprise this time, driven mainly by an increase in revenues from the sale of wiring sets for tow bars as a result of the popularization of car tourism and motorhome travel. We expect SG&A costs to be approx. 20% down q/q (reduced worktime, suspension of incentive scheme). Therefore, we forecast PLN 6.3m EBITDA in 2Q20 (down 57% y/y and 61% q/q) and net income to arrive at only PLN 3.0m (down 68% y/y and 74% q/q) in 2Q20.

Figure 1. AC results summary

| | 2016 | 2017 | 2018 | 2019 | 2020E | 2021E |
|---|---|---|---|---|---|---|
| Revenues (PLN m) | 185 | 194 | 237 | 223 | 173 | 201 |
| EBITDA (PLN m) | 45 | 47 | 59 | 58 | 37 | 43 |
| EBIT (PLN m) | 37 | 39 | 50 | 46 | 26 | 30 |
| Net profit (PLN m) | 30 | 31 | 39 | 38 | 21 | 24 |
| EPS (PLN) | 3.06 | 3.11 | 3.95 | 3.87 | 2.12 | 2.44 |
| DPS (PLN) | 5.00 | 2.70 | 2.50 | 3.94 | 1.25 | 1.70 |
| EV/EBITDA (x) | 5.2 | 7.6 | 6.7 | 8.3 | 10.8 | 9.3 |
| P/E (x) | 7.5 | 11.5 | 10.1 | 12.1 | 18.8 | 16.4 |

*Source: Company, IPOPEMA Research*

Industrials

## AC

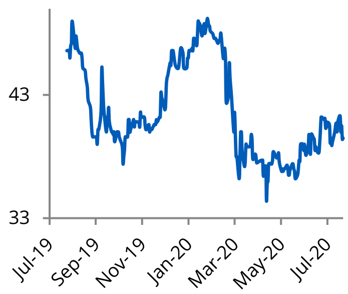
## HOLD

## FV PLN 42.00 from PLN 40.8

5% upside

Price as of 4 August 2020 PLN 40.00

Downgrade




Share data

| | |
|---|---|
| Number of shares (m) | 10.0 |
| Market cap (EUR m) | 90.5 |
| 12M avg daily volume (k) | 0.8 |
| 12M avg daily turnover (EUR m) | 0.01 |
| 12M high/low (PLN) | 49.4/34.2 |
| WIG weight (%) | 0.1 |
| Reuters | ACGP.WA |
| Bloomberg | ACG PW |

Total performance

| | |
|---|---|
| 1M | -2% |
| 3M | 5% |
| 12M | -14% |

Shareholders

| | |
|---|---|
| OFE PKO Bankowy | 9.1% |
| WIM | 7.6% |
| WASKULIT FIZ | 7.1% |
| Dariusz Kowalczyk | 5.5% |
| NN OFE | 5.2% |

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# ACG

## HOLD — FV PLN 42.00

Mkt Cap EUR 90m — Upside +5%

| Valuation multiples | 2017 | 2018 | 2019 | 2020E | 2021E |
|---|---|---|---|---|---|
| P/E (x) | 11.5 | 10.1 | 12.1 | 18.8 | 16.4 |
| EV/EBITDA (x) | 7.6 | 6.7 | 8.3 | 10.8 | 9.3 |
| EV/Sales (x) | 1.9 | 1.7 | 2.2 | 2.1 | 1.7 |
| P/BV (x) | 3.7 | 3.5 | 4.0 | 2.9 | 2.7 |
| FCF yield (%) | 5.2% | 5.9% | 5.4% | 4.7% | 5.4% |
| DY (%) | 7.3% | 6.8% | 10.6% | 3.4% | 4.6% |

| Per share | 2017 | 2018 | 2019 | 2020E | 2021E |
|---|---|---|---|---|---|
| No. of shares (m units) | 9.9 | 9.9 | 9.9 | 10.0 | 10.0 |
| EPS (PLN) | 3.1 | 3.9 | 3.9 | 2.1 | 2.4 |
| BVPS (PLN) | 9.8 | 11.3 | 11.6 | 12.4 | 13.1 |
| FCFPS (PLN) | 2.9 | 3.3 | 3,1 | 2.0 | 2.3 |
| DPS (PLN) | 2.70 | 2.50 | 3.94 | 1.25 | 1.70 |

| Change y/y (%) | 2017 | 2018 | 2019 | 2020E | 2021E |
|---|---|---|---|---|---|
| Revenues | 5.2% | 22.1% | -6.2% | -22.2% | 15.7% |
| EBITDA | 6.3% | 24.4% | -1.9% | -36.0% | 15.6% |
| EBITDA adj. | 6.3% | 24.4% | -1.9% | -36.0% | 15.6% |
| EBIT | 5.3% | 25.8% | -6.6% | -43.8% | 14.1% |
| Net profit | 1.6% | 27.1% | -2.1% | -44.6% | 14.7% |

| Leverage/return | 2017 | 2018 | 2019 | 2020E | 2021E |
|---|---|---|---|---|---|
| Gross margin (%) | 35.9% | 37.0% | 36.2% | 29.4% | 32.3% |
| EBITDA margin (%) | 24.3% | 24.8% | 25.9% | 21.3% | 21.3% |
| EBIT margin (%) | 20.3% | 20.9% | 20.8% | 15.0% | 14.8% |
| Net margin (%) | 15.8% | 16.4% | 17.1% | 12.2% | 12.1% |
| Net debt / EBITDA (x) | 0.14 | -0.01 | 0.34 | 0.20 | -0.08 |
| Net debt / Equity (x) | 0.1 | 0.0 | 0.2 | 0.1 | 0.0 |
| Net debt / Assets (x) | 0.0 | 0.0 | 0.1 | 0.0 | 0.0 |
| ROE (%) | 31.8% | 34.9% | 33.3% | 17.1% | 18.6% |
| ROA (%) | 20.4% | 23.4% | 21.8% | 11.4% | 13.3% |
| ROIC (%) | 32.7% | 42.7% | 33.9% | 18.0% | 21.4% |

| Assumptions | 2020E | 2021E |
|---|---|---|
| **Growth assumptions in LPG markets** | | |
| Poland | -60% | 40% |
| Russia | -10% | 50% |
| Ukraine | -20% | 15% |
| South Korea | -20% | 15% |
| Mexico | -10% | 15% |
| Kazakhstan | -20% | 10% |
| Uzbekistan | 0% | 0% |
| Balkanian countries | 0% | 10% |
| Spain | 0% | 10% |
| Azerbaijan, Armenia | 0% | 0% |
| African countries | -10% | 5% |
| Brazil | -5% | -5% |
| Other countries | 0% | 0% |

| P&L (PLN m) | 2016 | 2017 | 2018 | 2019 | 2020E | 2021E |
|---|---|---|---|---|---|---|
| Revenues | 184.9 | 194.4 | 237.4 | 222.7 | 173.3 | 200.5 |
| COGS | 119.0 | 124.6 | 149.5 | 142.0 | 122.4 | 135.8 |
| **Gross profit** | **65.8** | **69.8** | **87.9** | **80.7** | **50.9** | **64.8** |
| Selling costs | 16.8 | 18.8 | 22.7 | 20.2 | 16.1 | 19.3 |
| G&A costs | 13.5 | 13.4 | 15.7 | 16.4 | 13.1 | 15.8 |
| Other operating income (cost) ne | 1.9 | 1.8 | 0.1 | 2.2 | 4.4 | 0.0 |
| **EBITDA** | **44.5** | **47.3** | **58.9** | **57.7** | **37.0** | **42.7** |
| EBITDA adj. | 42.6 | 45.5 | 58.8 | 55.6 | 37.0 | 42.7 |
| **EBIT** | **37.4** | **39.4** | **49.6** | **46.3** | **26.0** | **29.7** |
| Financial income (cost) net | 0.3 | -1.5 | -1.1 | 0.2 | 0.1 | 0.3 |
| **Pre-tax profit** | **37.7** | **37.9** | **48.4** | **46.5** | **26.1** | **30.0** |
| Income tax | 7.5 | 7.2 | 9.4 | 8.3 | 5.0 | 5.7 |
| Minorities | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| **Net profit** | **30.2** | **30.7** | **39.0** | **38.2** | **21.2** | **24.3** |
| Net profit adj. | 30.2 | 30.7 | 39.0 | 38.2 | 21.2 | 24.3 |

| BALANCE SHEET (PLN m) | 2016 | 2017 | 2018 | 2019 | 2020E | 2021E |
|---|---|---|---|---|---|---|
| **Non-current assets** | **71.8** | **73.8** | **89.9** | **101.6** | **102.8** | **100.6** |
| Goodwill and intangible assets | 3.2 | 3.6 | 5.4 | 5.8 | 5.1 | 4.4 |
| PP&E | 63.1 | 65.1 | 79.8 | 92.0 | 93.9 | 92.4 |
| Other non-current assets | 5.5 | 5.0 | 4.7 | 3.8 | 3.8 | 3.8 |
| **Current assets** | **59.3** | **76.3** | **76.5** | **73.2** | **82.3** | **81.9** |
| Inventories | 36.8 | 34.9 | 50.6 | 50.8 | 45.1 | 46.7 |
| Trade receivables | 14.2 | 19.3 | 18.0 | 15.8 | 19.0 | 19.2 |
| Cash and equivalents | 3.3 | 17.7 | 4.7 | 2.4 | 13.9 | 11.7 |
| Other current assets | 5.1 | 4.4 | 3.2 | 4.3 | 4.3 | 4.3 |
| **Total assets** | **131.1** | **150.1** | **166.4** | **174.8** | **185.1** | **182.5** |
| **Equity** | **89.9** | **96.4** | **111.8** | **114.7** | **123.4** | **130.8** |
| Minorities | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| **Non-current liabilities** | **16.2** | **14.8** | **22.1** | **17.9** | **21.1** | **23.1** |
| Loans and borrowings | 0.1 | 0.1 | 0.1 | 0.0 | 0.0 | 0.0 |
| Other non-current liabilities | 16.1 | 14.6 | 22.0 | 17.9 | 21.1 | 23.1 |
| **Current liabilities** | **25.0** | **38.9** | **32.6** | **42.2** | **40.6** | **28.7** |
| Trade payables | 10.7 | 6.3 | 14.4 | 8.2 | 7.1 | 8.2 |
| Loans and borrowings | 6.8 | 24.3 | 4.3 | 21.7 | 21.2 | 8.2 |
| Other current liabilities | 7.5 | 8.3 | 13.8 | 12.2 | 12.2 | 12.2 |
| **Equity & liabilities** | **131.1** | **150.1** | **166.4** | **174.8** | **185.1** | **182.5** |
| Cash conversion cycle (days) | 79 | 90 | 83 | 96 | 120 | 105 |
| Gross debt (PLN m) | 6.8 | 24.3 | 4.3 | 21.7 | 21.2 | 8.2 |
| **Net debt (PLN m)** | **0.1** | **0.1** | **0.0** | **0.3** | **0.2** | **-0.1** |

| CASH FLOW (PLN m) | 2016 | 2017 | 2018 | 2019 | 2020E | 2021E |
|---|---|---|---|---|---|---|
| **Operating cash flow** | **37.3** | **31.5** | **50.7** | **41.6** | **37.6** | **40.7** |
| Net income | 30.2 | 30.7 | 39.0 | 38.2 | 21.2 | 24.3 |
| D&A | 7.1 | 7.9 | 9.3 | 11.5 | 11.0 | 13.1 |
| Minorities | 0.0 | 1.0 | 2.0 | 3.0 | 4.0 | 5.0 |
| Change in WC | -0.8 | -5.8 | -3.3 | -3.8 | 1.4 | -0.7 |
| Other | 0.8 | -2.3 | 3.7 | -7.3 | 0.1 | -0.9 |
| **Investment cash flow** | **-11.1** | **-9.1** | **-21.6** | **-23.5** | **-13.0** | **-13.0** |
| Change in intangibles and PP&E | -7.9 | -10.3 | -21.6 | -23.7 | -13.0 | -13.0 |
| Other | -3.1 | 1.2 | 0.1 | 0.2 | 0.0 | 0.0 |
| **Financial cash flow** | **-40.7** | **-7.7** | **-42.4** | **-20.4** | **-13.0** | **-29.9** |
| Change in equity | 0.3 | 0.2 | 0.9 | 0.9 | 0.0 | 0.0 |
| Change in debt | 6.8 | 17.5 | 0.0 | 17.4 | 0.0 | 0.0 |
| Interest paid | 0.0 | -0.3 | -0.3 | -0.6 | 0.0 | 0.0 |
| Dividend | -48.5 | -26.2 | -24.5 | -38.9 | -12.4 | -16.9 |
| Other | 0.6 | 1.1 | -18.5 | 0.8 | -0.5 | -13.0 |
| **Change in cash** | **-14.5** | **14.8** | **-13.3** | **-2.4** | **11.6** | **-2.2** |
| **Cash as of eop** | **3.3** | **18.0** | **4.7** | **2.3** | **13.9** | **11.7** |

*Source: Company data, IPOPEMA Research*

# Contents

# COVID-19 impact

We are disappointed by preliminary 2Q20 revenues, which amounted to PLN 32.2m (44% down y/y), demonstrating that the impact of the coronavirus pandemic is stronger than we had initially expected. Autogas system sales' anti-cyclicality will be outweighed by negative factors such as low gasoline prices, a reduction of used car imports in particular markets, disruption in global logistics, weakening of business partners' local currencies against the EUR and USD and all social distancing rules affecting mobility.

Among the main risks we still see are disturbances in global logistics, postponing orders in specific countries due to local regulations and generally lower demand in export markets due to reluctance to replenish inventories in the face of uncertain demand. Some clients which are the most affected by the epidemic may also require price reductions, which AC will likely have to accept.

On the other hand, we see some positives. We still believe that people will tend to convert the cheapest cars in order to resign from public transport on the back of the epidemic, but have postponed these decisions for the third and fourth quarters of this year, which suggests that such a strong decline in y/y results as observed in the second quarter will no longer take place.

We also believe that the results in the third quarter will be better due to the large number of vacation trips by private cars, which may contribute to an increase in number of conversions, as well as numerous conversions planned but delayed due to the prevailing pandemic.

We do not see much positive impact from high number of infections in Italy, where competitors do not seem to weaken due to a high level of inventories and not very restrictive approach to pandemic bans. Therefore, we do not expect a strong rebound in conversions in the coming months, thus the result should be lower by 25% y/y in 3Q20 and one-digit lower y/y in 4Q20. Then we expect a gradual rebound based mostly on Polish and Russian markets.

We expect results improvement in kits for the tow bars segment due to the popularization of vehicle tourism and motorhome travels, thus increased demand for such products offered by AC. We forecast a 20% revenue increase y/y in the segment to PLN 26.3m in 2020 and 27.62m in 2021.

On the cost side, we see approx. a 20% decline in SG&A costs y/y due to reduced remunerations for white-collar workers, suspension of incentive systems based on share ownership for the managerial staff (PLN 2.5m provisions for this purpose a year ago) and no business trips/fairs. We also assume that the company will slightly limit unnecessary CAPEX in 2020 to approx. PLN 13m.

# Supportive changes in Russian market

So far the biggest question mark for AC has been the Russian market, which according to our calculations accounts for around 12% of company revenues. Just to recap, a new law on conversion to auto gas came into force in 2019. New rules requiring tests of converted cars in accredited laboratories were postponed until 1 July 2020 to properly prepare the relevant laboratories. Currently, according to the Board of the Eurasian Economic Commission, introduction of new regulations regarding admission and registration of cars with a gas installation has been postponed again to July 2021 due to the spread of the coronavirus infection.

Moreover, the Russian government supported the energy minister's proposal to double the share of the budget subsidy for the purpose of conversions to CNG from 30 to 60 percent for medium-sized enterprises and citizens impacted by the coronavirus. Another 30 percent of expenses will be subsidized by Gazprom; therefore, car owners will have to pay only 10 percent of total conversion cost. Switching to compressed natural gas (CNG) will cut drivers' fuel expenses by 60-65 percent, providing fuel savings of 4-5bn rubles within three years. The Russian government will allocate 50bn rubles to the development of the gas engine industry in 2020-2024 - 3.5bn rubles annually for the development of gas stations and 700m rubles for conversions. According to government estimates, 10-12 thousand cars will be converted to LPG this year as a result of the program vs 15 thousand cars converted in the whole year 2019. With the onset of the pandemic, the demand for this type of service fell sharply.

We assume that the abovementioned changes will help strengthen AC's position on the Russian market, characterized by much higher margins than in Poland. We estimate around 50% revenue growth in Russia in 2021 vs 2020, from PLN18m to PLN 27m, and 10% growth in years ahead. This should help AC to mitigate a potentially prolonged slowdown in other foreign markets caused by the pandemic.

**Figure 2. Estimated revenues structure in 2020**

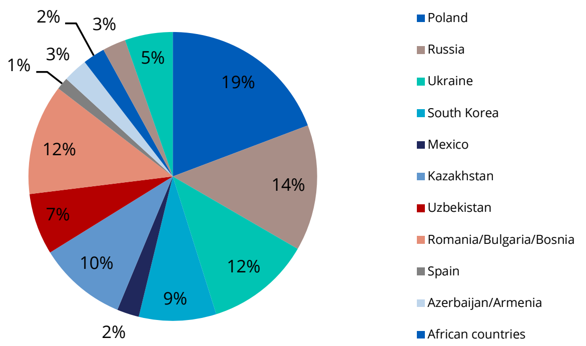
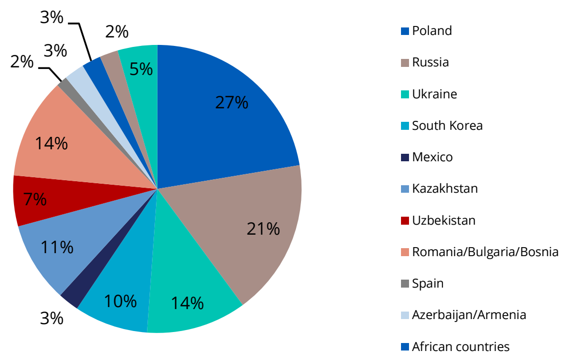



**Figure 3. Estimated revenues structure in 2021**




*Source: Company, IPOPEMA Research*

# 2Q20E results preview

AC is set to publish its full 2Q20E results on 10 August 2020.

On 1 July 2020 AC published preliminary 2Q20 revenues which amounted to PLN 32.2m (44% down y/y), which we perceive as disappointing. As the main reasons, AC mentioned low gasoline prices, despite the still favourable gasoline/gas ratio, reduction of used car imports, disruption in global logistics, weakening of business partners' local currencies against the EUR and USD and all social distancing rules affecting mobility and other restrictions.

**Sequential gas injection systems**. We expect 59% lower revenues y/y in the sequential gas injection system segment, amounting to PLN 18.8m. In our view, the segment sales will be the most negatively impacted. Due to the restrictions we expect no new orders from Ukrainian and Kazakh markets in the quarter as customers already had warehouses stocked up a quarter earlier. Moreover, the level of orders should be influenced by certain logistical difficulties, especially in distant markets such as Latin America or South Korea.

**Kits for the towing hook segment** will most likely prove to be a positive surprise this time, driven mainly by an increase in revenues from the sale of electronics sets and wiring sets for tow bars as a result of the popularization of car tourism and motorhome travels. We expect revenues in the segment to be 85% higher y/y.

**SQ&A.** As an incentive system based on company's shares for the managerial staff was suspended for 2020 and the company has operated with the work schedule reduced by 20% in the May-July period with a proportionate reduction in employee remuneration, excluding specialized departments serving the full-scale tow bar area, we expect SG&A costs to be approx. 20% down q/q.

**EBITDA.** We expect PLN 6.3m EBITDA in 2Q20 (down 57% y/y and 61% q/q).

**Other operating income**. AC will book co-financing received from the anti-crisis shield in the amount of PLN 2.3m in 2Q20. Moreover, AC should book an approx. 0.6m boost from the sale of unnecessary machinery parts in the quarter.

**Net profit.** We expect AC's net income to arrive at only PLN 3.0m (down 68% y/y and 74% q/q) in 2Q20.

**Figure 4. 2Q20 Results Preview IPOPEMA**

| (PLN m) | 1Q19 | 2Q19E | 3Q19 | 4Q19 | 1Q20E | 2Q20E | *yoy* | *qoq* |
|---|---|---|---|---|---|---|---|---|
| Revenues (prel.)) | 63.5 | 57.5 | 55.2 | 46.5 | 62.4 | 32.2 | *-44%* | *-48%* |
| Sequential gas injection systems | 51.3 | 46.0 | 43.3 | 37.1 | 49.8 | 18.8 | *-59%* | *-62%* |
| Vacuum LPG systems | 1.2 | 0.9 | 1.2 | 0.7 | 1.0 | 0.5 | *-42%* | *-46%* |
| Kits for towing hooks | 4.5 | 5.2 | 7.6 | 4.3 | 6.8 | 9.6 | *85%* | *41%* |
| Other products and services | 3.1 | 2.2 | 2.2 | 1.8 | 2.2 | 1.4 | *-37%* | *-36%* |
| Trade goods and materials | 3.4 | 3.2 | 3.2 | 2.8 | 2.7 | 1.9 | *-40%* | *-29%* |
| Gross profit | 23.7 | 20.4 | 20.0 | 16.5 | 22.5 | 7.3 | *-64%* | *-68%* |
| **EBITDA** | **17.9** | **14.6** | **15.8** | **9.4** | **16.0** | **6.3** | *-57%* | ***-61%*** |
| EBIT | 15.2 | 11.8 | 12.9 | 6.4 | 13.4 | 3.6 | *-69%* | *-73%* |
| Net profit | 12.4 | 9.4 | 11.1 | 5.3 | 11.6 | 3.0 | *-68%* | *-74%* |
| EBITDA margin | 28.3% | 25.3% | 28.6% | 20.3% | 25.6% | 19.4% | *-2.6pp* | *5.3pp* |
| EBIT margin | 23.9% | 20.5% | 23.4% | 13.7% | 21.5% | 11.3% | *-2.5pp* | *7.7pp* |
| Net margin | 19.5% | 16.3% | 20.2% | 11.4% | 18.5% | 9.2% | *-1pp* | *7.2pp* |

*Source: Company, IPOPEMA Research*

# ESG

**Environment**. Installation of modern gas installations offered by AC, by using alternative fuel, contributes to reducing harmful gas and dust emissions to the atmosphere, and thus to improving the conditions of the natural environment. The company's activity has no significant impact on the quality of air, water, or soil, nor does it emit noise and electromagnetic fields. AC S.A. bears fees for using the environment, and cooperates with a recovery organization. In recent years, there were no exceedances in areas defined by permits and no direct nuisance was caused to the local community.

Only in 2019 did AC take several steps to be more environmentally-friendly, for example through reduction of its electricity consumption in the field of lighting by replacing fluorescent lamps with LED lighting, developing rules, a monitoring program and monitoring the results of activities related to reducing paper consumption and introducing the principle of municipal waste segregation in all organizational units of the company.

**Social responsibility**. AC decided to establish the AC Foundation at the end of April 2011. The foundation's primary goal is to conduct Occupational Therapy Workshops for people with disabilities. At the beginning of 2019, the sponsorship policy was formalized and placed on the company's website. An example of sponsoring actions are: support of the passion of workshop with employees, sponsorship of the Ekstraklasa football team - Jagiellonia Białystok, care for young talents and sponsorship of Motoheart activities, as well as co-financing of the WOW Winter Orchestra Workshop for young promising musical talents. Another noteworthy activity is the creation of the STAG LPG Cup class during the Bialystok Automobile Championships and a social campaign entitled: I am a Safe Driver, which promotes road safety.

**Governance**. AC presents transparent and continuous communications with its employees and shareholders. The CEO and the vice-CEO (CFO) have been involved in company operations from the very beginning. Both of them hold more than 1% share in the company's share capital. The company holds regular meeting with investors, and the board is ready to answer shareholders' questions.

**AC's accountability is established and communicated clearly, ensuring that** sustainability is integrated with other business goals. The company used to set its EBITDA goals for the two coming years and share it with investors, which helps to assess effectiveness of the company's operations. The managerial options program is based on set goals, so bonuses are directly related to the company's results. Since the company is listed on the WSE, it has presented a transparent dividend policy with 80% DPR.

All in all, we maintain a positive opinion on AC's environmental and social responsibility, and corporate governance involvement.

# Valuation summary

We value AC via two methods, applying a 50% weight to our DCF-based valuation and a 50% weight to our DDM-based valuation.

Based on our forecasts, we arrive at a fair value of 42.0 PLN per share, which is above the current market price and implies a HOLD recommendation.

Figure 5. AC valuation summary

| AC, valuation summary | |
|---|---|
| **I Method: DCF** | |
| Fair Value (PLN per share) | 41.7 |
| Weight | 50% |
| **II Method: DDM** | |
| Fair Value (PLN per share) | 42.3 |
| Weight | 50% |
| **Fair Value (PLN per share)** | **42.0** |

*Source: Company, IPOPEMA Research*

## Discounted cash flow model

Our assumptions for cost of equity were established by using a risk free rate of 2% (vs 2.5% in previous report) and adding a 5.0% equity risk premium in each year. At the same time, we consistently use an unleveraged beta of 1 so as not to distort the WACC and comparability of our valuations. We use tax rate of 19% based on tax payments of recent years.

Figure 7. AC DCF 2020E-2024E valuation

| DCF (PLN m) | 2020E | 2021E | 2022E | 2023E | 2024E | Terminal Year |
|---|---|---|---|---|---|---|
| Revenue Growth Rate | -22.2% | 15.7% | 3.8% | 3.0% | 3.0% | 1.0% |
| Revenues | 173 | 201 | 208 | 215 | 221 | 228 |
| Gross margin | 29% | 32% | 34% | 35% | 37% | |
| SG&A costs | 29 | 35 | 40 | 42 | 44 | |
| EBIT | 26 | 30 | 31 | 34 | 37 | 38 |
| EBIT margin | 15% | 15% | 15% | 16% | 17% | 17% |
| Effective Tax Rate | 19% | 19% | 19% | 19% | 19% | 19% |
| NOPAT | 21 | 24 | 25 | 27 | 30 | 31 |
| + Depreciation | 11 | 13 | 14 | 13 | 14 | 14 |
| EBITDA | 37 | 43 | 45 | 47 | 51 | 52 |
| - Capex | -13 | -13 | -14 | -14 | -14 | -14 |
| - Change in WC | 1 | -1 | 1 | 1 | -2 | -2 |
| FCF | 20 | 23 | 26 | 29 | 28 | 29 |
| Terminal Value | | | | | | 481 |
| WACC | 7.0% | 7.0% | 7.0% | 7.0% | 7.0% | 7.0% |
| Present Value of FCF | 19 | 21 | 22 | 22 | 21 | 327 |

| | |
|---|---|
| NPV FCF | 105 |
| + Present Value of Terminal Value | 327 |
| Operating Assets of the Firm = | 432 |
| + Value of Cash | 2 |
| Value of Firm = | 434 |
| - Value of Outstanding Debt = | -22 |
| - Dividend = | 0 |
| Value of Equity = | 412 |
| Number of shares (m) | 10 |
| Fair Value of Equity per share (PLN) | 41.7 |

| Key Assumptions | |
|---|---|
| Revenue CAGR 2020E-2024E | 6.3% |
| Average EBIT margin in 2020E-2024E | 15.4% |
| Market Risk Premium | 5.0% |
| Beta | 1.00 |
| Growth in residual period | 1.0% |
| Average WACC in 2020E-2024E | 7.1% |

| | | WACC in perpetuity | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | | 8.5% | 8.0% | 7.5% | 7.0% | 6.5% | 6.0% | 5.5% |
| | 0.5% | 33.5 | 35.1 | 37.0 | 39.2 | 41.7 | 44.8 | 48.4 |
| Terminal Growth | 1% | 35.1 | 37.0 | 39.2 | 41.7 | 44.8 | 48.4 | 52.8 |
| | 1.5% | 37.0 | 39.2 | 41.7 | 44.7 | 48.4 | 52.8 | 58.3 |

*Source: IPOPEMA Research*

# DDM valuation

On 5 May 2020 AC informed that the management board suspended its previous recommendation concerning PLN 2.80 DPS as it is unable to foresee the effects of the epidemic. Then, on 29 July the management recommended PLN 1.25 DPS (DY of 3.1%) which is broadly in line with our previous assumption of PLN 1.5 DPS (50% DPR) and reflects extremely difficult macro environment. Supervisory board approved the motion. We maintain our assumption that the company will maintain its dividend policy given the end of its intensive CAPEX program and strong balance sheet with a quite conservative long-term 80% DPR after 2020. Our assumption translates into PLN 1.7 (4.3% DY) in 2021E.

In the DDM model, we applied the same assumptions as in the DCF model with regards to cost of capital and unlevered beta.

Figure 9: AC DDM 2020E-2024E valuation

| AC: DDM | 2020E | 2021E | 2022E | 2023E | 2024E | Terminal Year |
|---|---|---|---|---|---|---|
| **DPS (PLN)** | **1.2** | **1.7** | **1.9** | **2.0** | **2.2** | **2.9** |
| Risk free rate | 2.0% | 2.0% | 2.0% | 2.0% | 2.0% | |
| Equity premium risk | 5.0% | 5.0% | 5.0% | 5.0% | 5.0% | |
| Unlevered beta | 1.00 | 1.00 | 1.00 | 1.00 | 1.00 | |
| Levered beta | 1.05 | 1.02 | 1.02 | 1.02 | 1.02 | |
| Cost of Equity | 7.2% | 7.1% | 7.1% | 7.1% | 7.1% | |
| Discount multiple | 0.95 | 0.89 | 0.83 | 0.77 | 0.72 | |
| Discounted DPS (PLN) | 1.2 | 1.5 | 1.6 | 1.6 | 1.6 | |
| **Sum of discounted DPS in forecast period (PLN)** | **7.5** | | | | | |
| Terminal growth | | | | | | 1.0% |
| Terminal Cost of Equity | | | | | | 7.1% |
| **Present value of terminal value (PLN)** | | | | | | **34.8** |
| | | | | | | |
| **Fair Value (PLN ps)** | | | | | | **42.3** |

*Source: IPOPEMA Research*

## Relative valuation

Based on our forecasts, AC trades at 2020E P/E of 18.8x. This is a 14% premium to the median of peer multiples. On our forecasts, AC trades at 2020 EV/EBITDA of 10.8x, 19% premium to peers.

Figure 10: AC relative valuation 2020E-2022E

| COMPANY | Last price | Market Cap | P/E | | | EV/EBITDA | | | DY | ND/EBITDA | NI CAGR | EBITDA CAGR | EBITDA margin |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | EUR m | 2020E | 2021E | 2022E | 2020E | 2021E | 2022E | 2020E | 2020E | 2020-22E | 2020-22E | 2020E |
| LANDI RENZO SPA | EUR 0.7 | 74 | na | na | 7.6 | 4.6 | 3.2 | 2.5 | 0.0% | 0.0 | *na* | *na* | 8.8% |
| SOGEFI | EUR 0.9 | 110 | 24.3 | 18.4 | 14.6 | 13.3 | 11.4 | 8.9 | 0.0% | 0.3 | *na* | *28.8%* | 9.1% |
| GLOBAL PMX CO LTD | TWD 167.5 | 51,312 | 17.4 | 14.4 | 11.8 | 11.0 | 9.4 | na | 4.1% | 0.2 | *28.9%* | *19.4%* | 23.0% |
| ALTRA INDUSTRIAL MOTION COF | USD 35.5 | 1,952 | 15.8 | 11.8 | 9.9 | 7.8 | 6.6 | 5.8 | 0.9% | na | *na* | *na* | 19.9% |
| ALUMETAL SA | PLN 37.7 | 133 | na | 13.3 | 12.5 | 9.4 | 6.6 | 6.3 | 6.1% | 0.0 | *na* | *na* | 6.7% |
| BORYSZEW SA | PLN 3.6 | 203 | 14.5 | 14.6 | 11.0 | 8.8 | 8.7 | 7.0 | 0.0% | 0.3 | *na* | *22.1%* | 4.7% |
| **MEDIAN** | | | **16.6** | **14.4** | **11.4** | **9.1** | **7.6** | **6.3** | **0.5%** | **0.2** | **28.9%** | **22.1%** | **9.0%** |
| AC | 40.0 | 90 | 18.8 | 16.4 | 15.9 | 10.8 | 9.3 | 8.9 | 3.1% | 0.0 | *8.9%* | *10.0%* | 21.3% |
| premium/discount to all peers (median) | | | *14%* | *14%* | *39%* | *19%* | *22%* | *41%* | | | | | |
| | | | | | | | | | | | | | |
| **Implied Price (PLN)** | | | **35.2** | **35.2** | **28.7** | **33.7** | **32.7** | **28.3** | | | | | |

*Source: IPOPEMA Research*

# Changes in estimates

Figure 6. Chenges in estimates

| PLNm | 2020E New | 2020E Old | Diff. % | 2021E New | 2021E Old | Diff. % | 2022E New | 2022E Old | Diff. % |
|---|---|---|---|---|---|---|---|---|---|
| Sales | 173.3 | 210.5 | -17.7% | 200.5 | 219.3 | -8.6% | 208.2 | 222.9 | -6.6% |
| EBITDA | 37.0 | 43.3 | -14.6% | 42.7 | 49.7 | -14.0% | 44.8 | 51.1 | -12.4% |
| Net profit | 21.2 | 25.0 | -15.4% | 24.28 | 29.5 | -17.8% | 25.1 | 29.8 | -15.7% |

*Source: Company, IPOPEMA Research*

# Financials

Figure 7. AC P&L account 2016-2024E

| Income statement (PLN m) | 2016 | 2017 | 2018 | 2019 | 2020E | 2021E | 2022E | 2023E | 2024E |
|---|---|---|---|---|---|---|---|---|---|
| **Revenues** | **185** | **194** | **237** | **223** | **173** | **201** | **208** | **215** | **221** |
| *y/y change (%)* | | *5%* | *22%* | *-6%* | *-22%* | *16%* | *4%* | *3%* | *3%* |
| Costs of goods sold | 119 | 125 | 149 | 142 | 122 | 136 | 137 | 138 | 140 |
| **Gross profit** | **66** | **70** | **88** | **81** | **51** | **65** | **71** | **76** | **81** |
| Selling and marketing costs | 17 | 19 | 23 | 20 | 16 | 19 | 22 | 23 | 25 |
| Administrative costs | 13 | 13 | 16 | 16 | 13 | 16 | 18 | 19 | 20 |
| Other operating income/costs | 2 | 2 | 0 | 2 | 4 | 0 | 0 | 0 | 0 |
| **EBIT** | **37** | **39** | **50** | **46** | **26** | **30** | **31** | **34** | **37** |
| *y/y change (%)* | | *5%* | *26%* | *-7%* | *-44%* | *14%* | *4%* | *10%* | *9%* |
| **EBITDA** | **45** | **47** | **59** | **58** | **37** | **43** | **45** | **47** | **51** |
| *y/y change (%)* | | *6%* | *24%* | *-2%* | *-36%* | *16%* | *5%* | *6%* | *8%* |
| Financial income / cost | 0 | -1 | -1 | 0 | 0 | 0 | 0 | 0 | 0 |
| **Pretax profit** | **38** | **38** | **48** | **46** | **26** | **30** | **31** | **34** | **37** |
| Income tax | 8 | 7 | 9 | 8 | 5 | 6 | 6 | 7 | 7 |
| **Net income** | **30** | **31** | **39** | **38** | **21** | **24** | **25** | **28** | **30** |
| **EPS (PLN)** | **3.06** | **3.11** | **3.95** | **3.87** | **2.12** | **2.44** | **2.52** | **2.78** | **3.04** |

| Profitability ratios | 2016 | 2017 | 2018 | 2019 | 2020E | 2021E | 2022E | 2023E | 2024E |
|---|---|---|---|---|---|---|---|---|---|
| Gross margin | 35.6% | 35.9% | 37.0% | 36.2% | 29.4% | 32.3% | 34.2% | 35.5% | 36.7% |
| EBITDA margin | 24.1% | 24.3% | 24.8% | 25.9% | 21.3% | 21.3% | 21.5% | 22.1% | 23.2% |
| EBIT margin | 20.2% | 20.3% | 20.9% | 20.8% | 15.0% | 14.8% | 14.8% | 15.8% | 16.8% |
| Net margin | 16.3% | 15.8% | 16.4% | 17.1% | 12.2% | 12.1% | 12.1% | 12.9% | 13.7% |
| ROE | 33.6% | 31.8% | 34.9% | 33.3% | 17.1% | 18.6% | 18.4% | 19.3% | 19.9% |

*Source: Company, IPOPEMA Research*

Figure 8. AC balance sheet 2016-2024E

| Balance sheet (PLN m) | 2016 | 2017 | 2018 | 2019 | 2020E | 2021E | 2022E | 2023E | 2024E |
|---|---|---|---|---|---|---|---|---|---|
| **Total current assets** | **59** | **76** | **77** | **73** | **82** | **82** | **92** | **104** | **117** |
| Inventory | 37 | 35 | 51 | 51 | 45 | 47 | 48 | 47 | 48 |
| Receivables | 14 | 19 | 18 | 16 | 19 | 19 | 17 | 18 | 18 |
| Cash and equivalents | 3 | 18 | 5 | 2 | 14 | 12 | 23 | 35 | 46 |
| Other current assets | 5 | 4 | 3 | 4 | 4 | 4 | 4 | 4 | 4 |
| **Total non-current assets** | **72** | **74** | **90** | **102** | **103** | **101** | **98** | **96** | **93** |
| Property, plant and equipment | 63 | 65 | 80 | 92 | 94 | 92 | 90 | 88 | 86 |
| Intangible assets | 3 | 4 | 5 | 6 | 5 | 4 | 4 | 3 | 3 |
| Other non-current assets | 6 | 5 | 5 | 4 | 4 | 4 | 4 | 4 | 4 |
| **Total assets** | **131** | **150** | **166** | **175** | **185** | **182** | **190** | **200** | **209** |
| **Stockholders` equity** | **90** | **96** | **112** | **115** | **123** | **131** | **136** | **144** | **152** |
| **Total non-current liabilities** | **16** | **33** | **13** | **30** | **29** | **16** | **16** | **16** | **16** |
| Other non-current liabilities | 16 | 33 | 13 | 30 | 29 | 16 | 16 | 16 | 16 |
| **Total current liabilities** | **21** | **14** | **27** | **22** | **25** | **27** | **29** | **31** | **32** |
| Trade and other payables | 11 | 6 | 14 | 8 | 7 | 8 | 9 | 9 | 9 |
| Loans and borrowings | 7 | 24 | 4 | 22 | 21 | 8 | 8 | 8 | 8 |
| Other current liabilities | 4 | -17 | 8 | -8 | -3 | 11 | 12 | 14 | 14 |
| **Total equity & liabilities** | **131** | **150** | **166** | **175** | **185** | **182** | **190** | **200** | **209** |
| BVPS (PLN) | 9 | 10 | 11 | 12 | 12 | 13 | 14 | 14 | 15 |
| Net debt | 3 | 7 | 0 | 19 | 7 | -3 | -14 | -27 | -38 |
| Net debt / EBITDA | 0.1x | 0.1x | 0.0x | 0.3x | 0.2x | -0.1x | -0.3x | -0.6x | -0.7x |
| **Balance sheet ratios** | **2016** | **2017** | **2018** | **2019** | **2020E** | **2021E** | **2022E** | **2023E** | **2024E** |
| Current ratio | 2.8 | 5.4 | 2.8 | 3.3 | 3.3 | 3.0 | 3.2 | 3.4 | 3.7 |
| Quick ratio | 1.1 | 3.0 | 1.0 | 1.0 | 1.5 | 1.3 | 1.5 | 1.9 | 2.1 |
| Debt / assets | 5% | 16% | 3% | 12% | 11% | 5% | 4% | 4% | 4% |
| Debt / equity | 8% | 25% | 4% | 19% | 17% | 6% | 6% | 6% | 5% |

*Source: Company, IPOPEMA Research*

Figure 9. AC cash flow 2016-2024E

| Cash flow (PLN m) | 2016 | 2017 | 2018 | 2019 | 2020E | 2021E | 2022E | 2023E | 2024E |
|---|---|---|---|---|---|---|---|---|---|
| Net income | 30 | 31 | 39 | 38 | 21 | 24 | 25 | 28 | 30 |
| Depreciation and amortisation | 7 | 8 | 9 | 11 | 11 | 13 | 14 | 13 | 14 |
| Other (incl. WC change) | 0 | -7 | 2 | -8 | 5 | 3 | 5 | 5 | 2 |
| **Operating cash flows** | **37** | **32** | **51** | **42** | **38** | **41** | **44** | **46** | **47** |
| Capital expenditures | -8 | -10 | -22 | -24 | -13 | -13 | -14 | -14 | -14 |
| Other | -3 | 1 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| **Investing cash flows** | **-11** | **-9** | **-22** | **-24** | **-13** | **-13** | **-14** | **-14** | **-14** |
| Change in debt | 7 | 17 | -20 | 17 | -1 | -13 | 0 | 0 | 0 |
| Dividends paid | -48 | -26 | -24 | -39 | -12 | -17 | -19 | -20 | -22 |
| Other | 1 | 1 | 2 | 1 | 0 | 0 | 0 | 0 | 0 |
| **Financing cash flows** | **-41** | **-8** | **-42** | **-20** | **-13** | **-30** | **-19** | **-20** | **-22** |
| Beginning cash | 18 | 3 | 18 | 5 | 2 | 14 | 12 | 23 | 35 |
| Increase / decrease in cash | -15 | 15 | -13 | -2 | 12 | -2 | 11 | 13 | 10 |
| **Ending cash** | **3** | **18** | **5** | **2** | **14** | **12** | **23** | **35** | **46** |
| DPS (PLN) | 5.0 | 2.7 | 2.5 | 3.9 | 1.2 | 1.7 | 1.9 | 2.0 | 2.2 |

*Source: Company, IPOPEMA Research*

# Risks to fair value

### Unfavourable petrol-LPG spread and CNG price relationship

High prices for conventional fuels are the main driver of interest in converting cars to Auto gas. Problems on the supply side in the Auto gas/crude oil market stemming from, for example, armed conflicts or cartel agreements would result in significant narrowing of the Auto gas/petrol spread and thus less interest in converting cars to Auto gas.

### Risk of tax policy changes for Auto gas

Tightening tax policies or reducing subsidies for Auto gas as an alternative, ecological fuel would result in a drop in the number of conversions to LPG. We see little long-term predictability regarding such policies and potential increases in "hidden" taxes for Auto gas in relation to other conservative fuels among the potential risks.

**Risk related to the macroeconomic situation in key markets**

Deterioration of the macroeconomic situation in major markets (especially in Russia, Ukraine and Kazakhstan) may lead the population to look for savings, and thus a reduction in spending on car travel and a reluctance to invest in LPG systems as well as lower profitability of such an investment. Russia, Ukraine and Kazakhstan in total account for over 30% of AC's revenues.

**Risk of political change and armed conflict**

As a large part of the company's sales is directed to Russia and Ukraine (over 20% of AC's total revenues), the risk of changes to political regulations is high. Additionally, exports to Russia and Ukraine, as in the case of other export markets (the Balkans and the Middle East countries), may be affected by political tensions, trade embargoes or armed conflict. According to our calculations, over 50% of AC's revenues are at such risk.

**Risk of labour/raw materials price increases**

Under our assumptions, over 65% of the company's costs are related to raw material prices (electronic components, electric wires, plastics – PCV, polypropylene, PA, ABS, POM, and metals – steel, aluminium, copper, tin), hence increases in these costs would cause margins to shrink. In the same way, labour costs (which we estimate account for 20% of production costs).

**Risk of FX changes**

The bulk of the company's revenues are in EUR and USD. Despite the large share of imported raw materials and a significant share of export sales (about 60%), the strengthening of the PLN against the EUR and the USD is a risk for AC.

**Risk of competitive vehicle technology (incl. electric vehicles)**

We perceive increased penetration of electric cars as a risk for the company, although it might also present an opportunity. We believe that electric cars may become significantly more competitive for the following reasons: the price of electric cars will match the price of combustion cars; a dense network of charging infrastructure will be built and charging time will be reduced, so the distance travelled on one charge will be similar to the distance travelled on one tank of fuel. Such changes over several years would completely change the profile of AC's activity in the field of gas installations (currently about 80% of business).

**Potential consolidation of customers/distributors**

AC primarily sells its products through several dozen customers, including authorized distributors of car parts. Significant risk to company's results comes from the potential consolidation of gas distributors in their respective domestic markets, excessively high revenue exposure to one export destination, and significant foreign distributors ending their relationship with AC.

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Net F&C – Net fee and commission income – fee and commission income minus fee and commission expense.
LLP – loan loss provisions – an expense set aside as an allowance for bad loans.
NPL – non-performing loan – loans that are in default or close to be in default.
Cost/Income – operating expenses divided by total banking revenue.
ROE – return on equity – net income (or adjusted net income) divided by the average shareholders' equity.
ROA – return on assets – net income (or adjusted net income) divided by the average assets.
EBIT – earnings before interests and tax.
EBITDA – earnings before interests, tax, depreciation and amortization.
EPS – earnings per share – the net income (or adjusted net income divided by the number of shares outstanding.
P/E – price to earnings ratio – price divided by earnings per share.
PEG – P/E ratio divided by the annual EPS growth, usually over a certain period of time.
CAGR – compound annual growth rate.
BVPS – book value per share, the book value of the Company's equity divided by the number of shares outstanding.
P/BV – price to book value - price divided by the BVPS.
DPS – dividend per share – dividend of a given year divided by the number of shares outstanding.
DY – dividend yield – dividend of a given year divided by the current price.
DDM – dividend discount model – a fundamental method of valuation based on the assumption that the value of stock equals the sum of all discounted future dividends.
FV – Fair Value, calculated based on valuation methods outlined in the document.

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| Hold | 11 | 26% |
| Sell | 8 | 19% |
| Total | 42 | 100% |

Rating History – AC

| | | | | |
|---|---|---|---|---|
| 02/08/2019 | BUY | PLN 53.0 | PLN 46.6 | Piotr Jusiński |
| 24/04/2020 | BUY | PLN 40.8 | PLN 36.0 | Piotr Jusiński |