Company Report

Duda

Poland, Food & Beverages

Hold

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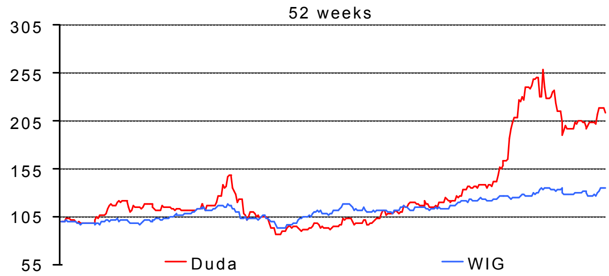
PLN mn	2005	2006e	2007e	2008e
Net sales	870.0	1,029.3	1,635.2	1,993.9
EBITDA	53.7	80.1	105.2	147.8
EBIT	38.7	61.5	79.7	116.8
Net profit	27.1	49.8	61.8	88.1
EPS (PLN)*	0.56	0.95	0.64	0.91
CEPS (PLN)*	0.87	1.33	0.90	1.23
BVPS (PLN)*	4.29	4.12	4.75	5.00
Div/share (PLN)	0.00	0.00	0.00	0.64
EV/EBITDA (x)*	15.4	18.8	14.7	10.6
P/E (x)*	24.7	14.6	21.8	15.3
P/CE (x)*	16.1	10.5	15.4	11.3
Dividend yield	0.0%	0.0%	0.0%	4.6%



Performance	12M	6M	3M	1M
in PLN	113.8%	126.4%	57.6%	-0.8%
in EUR	111.9%	129.6%	57.8%	-3.2%

Share price (PLN)	13.9	Reuters	DUDA.WA	Free float	75.0%
Number of shares (mn)*	96.8	Bloomberg	DUD PW	Shareholders	Duda family (25%)
Market capitalization (PLN mn / EUR mn)	1,345.5 / 345.9	Div. ex-date	-		
Enterprise value (PLN mn /EUR mn)	1,544.7 / 397.2	**Target price**	**14.3**	Homepage:	www.zmduda.pl

** We assumed that the number of shares increased to 96.8mn on the record date of subscription rights, which particuarly impacts 2006 numbers*

Big capex to spur growth…and risk

- **Duda recently disclosed its acquisition targets, shed more light on future plans and carried out a capital increase, prompting us to update our view. We have set a new 12M target price of PLN 14.3 (PLN 25.6 before the subscription rights issue). Hence, we have an Hold recommendation on the stock.**
- **Duda is forging ahead with its ambitious plans, which involve capex of PLN 300-380mn. The firm has already swallowed up two considerable companies and is eyeing the next two. Duda also intends to invest in pig farms, entertains hopes of expanding in Ukraine and envisions cost savings from own bio-gas plants.**
- **To start, Duda took over the Biernacki company, which comprises a large beef/pork slaughterhouse and cold storage facility. Biernacki has approx. PLN 330mn in annual revenue and a 2-3% net margin. Secondly, the company bought Stol Polski, a significant distribution company with six distribution centers and a dissecting plant. Stol Polski is also a producer of cured meat with sales close to PLN 250mn and a net margin of 1-2%.**
- **The enlarged Duda has become a local meat giant, benefiting from many potential synergies, scale effects and exposure to more diversified growth, thanks to its beef and meat processing activities and the development of its Ukrainian arm.**
- **Two further acquisitions (in Poland and Ukraine) are still pending and are expected to be completed in 1H07. Moreover, the company plans to invest PLN 100mn in own pig farms (to lift margins) and bio-gas plants to reduce utilization of manure and energy costs. Given the uncertainty of its success, we do not include the bio-gas project in our valuation.**
- **The entire strategic plan is to be financed via a share issue (PLN 150mn) and debt. The new share price has been set at PLN 3.0. Since the issue has involved subscription rights, the stock has recently declined by the theoretical value of these rights (approximately PLN 12.0 as of December 2006). These rights will be traded separately on the WSE In January.**
- **Duda has decided to set up a joint venture in the bio-ethanol industry to leverage its farming know-how and profit from this lucrative segment. We feel that such diversification does not necessarily fit into the firm's business model. Given this assessment and the project's high risk, we have not included it in our primary valuation. However, based on conservative assumptions (an EBITDA margin of 24%, revenues of PLN 300mn), its value add-in is close to PLN 6.0 per share.**

Forecasts

For FY07, we expect revenue of PLN 1.63bn, representing 58.9% y/y growth. For 2008, we anticipate revenue of PLN 1.99bn, a 21.9% y/y advance. The operating margin should hover between 5% and 6%. The results should be driven by:

- the acquisitions of Biernacki and Stol Polski (adding sales of PLN 330mn and PLN 250mn, respectively, with capex of PLN 122.5mn), with Biernacki to be consolidated as of 2Q07;

- the development of distribution in Poland, resulting in a further PLN 100mn in sales as of 2008 (either via acquisition or organic growth), with capex at PLN 50mn;

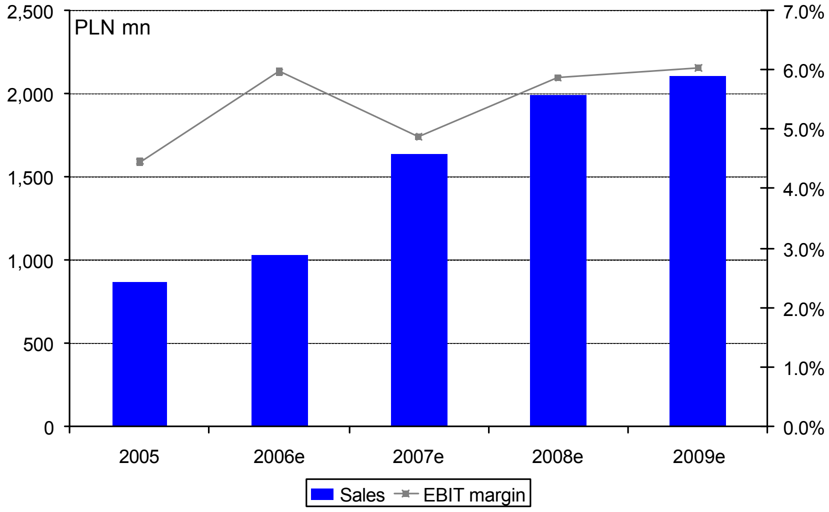
- swift expansion in Ukraine, coupled by takeovers, increasing sales by more than PLN 100mn in 2008 (capex 60mn);

- the development of a raw material supply (pig farms) with capex of PLN 60mn;

- organic growth in 2007e and 2008e of 12% and 6%, respectively;

- the pigmeat price in 2007 at PLN 3.53/kg.

Sales and margins



Source: Duda, Erste Bank estimates

Consequently, EBIT arrives at PLN 80mn in 2007 (up 30% y/y) and at PLN 117mn in 2008 (up 47% y/y). Net profit should hit PLN 62mn in 2007 and PLN 88mn in 2008. Compared to 2006, the other operating result is obviously lower, as PLN 8.5mn was gained on the revaluation of an investment in 2005. The financial result is likely to be in the red in 2007, as it was propped up by a PLN 4.2mn profit on the sale of an investment in 2006.

Changes

PLNmn	2006e			2007e		
	Now	Previously	Change	**Now**	Previously	Change
Revenue	**1,029.3**	**1,040.7**	-1.1%	**1,635.2**	**1,218.7**	34.2%
COGS	**-896.1**	-920.5	-2.7%	**-1,427.3**	-1,068.3	33.6%
Gross profit	**133.3**	**120.1**	10.9%	**207.9**	**150.4**	38.3%
S&GA	**-91.0**	-83.7	8.8%	**-139.7**	-97.0	44.0%
Other operating net	**19.2**	18.2	5.8%	**11.4**	11.0	4.1%
EBIT	**61.5**	**54.7**	12.4%	**79.7**	**64.4**	23.7%
Financial net	**-1.1**	-0.9	20.8%	**-3.3**	-7.7	-57.3%
Net profit	**49.8**	**44.3**	12.4%	**61.8**	**45.3**	36.4%

Source: Erste Bank

In comparison with our previous note on Duda, the bulk of growth on the top line should stem from the acquisitions of Biernacki and Stol Polski. We also postponed any acquisition in the distribution arm from 2007 until 2008. The organic growth rates remain the same. The expected drop in profitability in 2007 is a result of the consolidation of Biernacki and Stol Polski, which have thinner margins and need restructuring, which we assumed would be completed successfully as of 2008.

We do not include in our basic scenario the potential building of bio-gas plants (capex PLN 40mn, unknown savings) or a bio-ethanol installation (capex PLN 100-120mn, uncertain return).

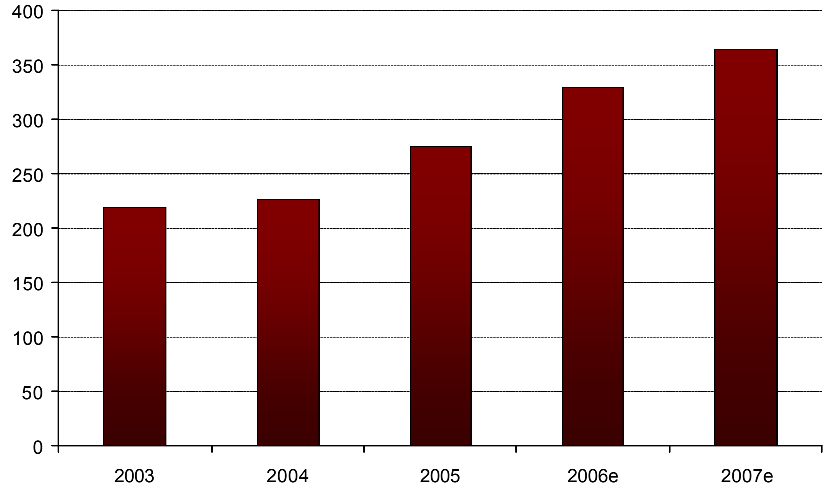
Investment story

Considerable growth of production potential

The Biernacki company consists of a beef/pork slaughterhouse and a large cold storage facility. Over 50% of its revenue is derived from exports (with 95% of beef produced and 50% of pork headed abroad). This takeover boosts Duda's capacities in pork by 71% and by six to seven times in beef. The greater potential will enable the firm to cut the cost of supplies and benefit from vast scale effects. Additionally, it more than doubles Duda's cold storage capacity to 55,000 tons. This capacity is lent to external clients and yields thick EBITDA margins of above 25%. Running two slaughterhouses under one management will help to trim overheads. Duda also plans to invest in production automation to shield itself against rising employment costs.

Biernacki increased its revenue from PLN 219mn in 2003 to an estimated PLN 330mn in 2006. The net margin yielded by this company is anticipated at 2-3%, but this is mainly generated by the high-margin cold storage. The stand-alone slaughterhouse is much less profitable than Duda, and hence has some restructuring potential.

Revenues Biernacki 2003-2007e (PLN mn)

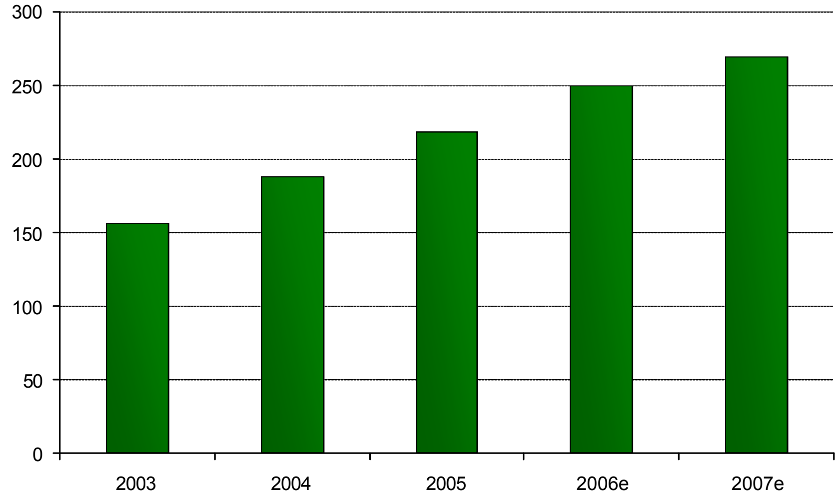


Source: Duda, Erste Bank estimates

Stol Polski comprises four distribution centers (increasing the total number in Duda's group to ten and nicely supplementing the national coverage) and two dissecting plants (one together with the cured meat production facility). The company offers five own brands in the premium segment, which will be developed and promoted via Duda's entire distribution chain. 2006 revenue is anticipated at PLN 250mn, with own production making up 33% of the total. This translates into 60% growth compared to the 2003 level (CAGR of 17%). Profitability is low, due to the fact that the bulk of profits come from distribution. Stol Polski yields a net margin of around 1.3-1.4%.

Duda intends to consolidate its dissecting process, which will result in doubling the capacity for cured meat at the Ciechanowiec plant and significantly lower costs. The company will also benefit from its strong position in the wealthiest Polish market, Warsaw; after this acquisition, its share there jumped to about 60%. Furthermore, Duda's bargaining power over suppliers and customers should improve greatly.

Revenues Stol Polski 2003-2007e (PLN mn)



Source: Duda, Erste Bank estimates

Duda is continuing the development of its Ukrainian arm and is mulling another acquisition. The company currently has a pig farm (with expected capacity of 100,000 pigs p.a.) and a small slaughterhouse in Ukraine. The firm should be able to generate about PLN 50mn in 2007 in Ukraine, yielding a 15% net margin. Duda plans to buy a company that comprises almost the full value chain, from farms to meat processing. Duda has earmarked PLN 50mn for this acquisition. The sales of the target company are approximately PLN 50mn, with a net margin of 11%. We regard this acquisition as quite likely and include it in our model.

Bio-fuel dreams

Duda plans to build a bio-ethanol installation with annual capacity of 100,000 tons in a joint venture with Lurgi, an engineering company (and potentially with a foreign receiver that could guarantee the market). The installation would be fed with 330,000 tons of corn. The bio-fuel industry is in a fledgling stage, but definitely has high growth potential. Given the worldwide wave of environmental protection regulations and eco-awareness, more and more bio-components are added to fuels to decrease pollution. In Poland, current capacities for bio-ethanol amount to 0.4mn tons, which is mostly used by distilleries; the estimated demand in 2010 is 1.2mn tons. The anticipated capex for this project is PLN 120mn, with the lion's share to be financed by Duda. The venture's target revenue for 2009 is PLN 300mn, with an EBITDA margin in the range of 30-35%. In our second scenario projection, we have been slightly more conservative, and assume a sliding margin (from 30% down to 24% in perpetuity).

Risky and rewarding

At present, the prospects for this segment seem to be very sound. Nonetheless, it is an industry that barely exists in Poland, and the risk and uncertainty are therefore taken to be very high. Duda decided to invest, lured by low competition and visions of fat margins. It plans to leverage its contacts, knowledge and experience in agriculture and use own farmland. Additionally, the byproduct is DDGS, a protein-rich product used in the manufacture of pig-feed. However, the links with the current business are rather weak, and we treat this as a step into an almost completely new area, rather than as an enhancement of recent operations. Hence, given the risks, we decided to not include the value of this project in our target price and only show the potential impact on the valuation.

Target price including bio-ethanol PLN 20

Assuming the bio-fuel installation starts operating in late fall 2008, we calculated first revenue as of 2009 (PLN 300mn). We included PLN 120mn full capex and a 24% EBITDA margin. 10% is financed by Lurgi, with the remainder debt-financed by Duda. Consequently, we derived a 12M target price of PLN 20 per share. However, Duda's competition might speed up the building of installations, while greater capacities could shrink margins and EU regulations could become less favorable. This last factor is the least likely, in our opinion. Very strong demand is expected from abroad.

Impact of Bio-fuel - Sensitivity

		EBITDA margin				
		18.0%	**21.0%**	**24.0%**	**27.0%**	**30.0%**
Biofuel TV growth	**0%**	17.8	18.5	19.2	20.0	20.7
	0.60%	18.1	18.9	19.7	20.5	21.3
	1.20%	18.5	19.4	**20.2**	21.1	22.0
	1.80%	19.0	19.9	20.9	21.8	22.8
	2.40%	19.6	20.6	21.6	22.7	23.7

Source: Erste Bank

This table presents the value of Duda's share, provided that the bio-ethanol project is included in the calculations and has the detailed parameters (EBITDA margin, TV growth).

The entire capex plan scheduled for 2007-08 (PLN 380-500mn) will be financed by a share issue (proceeds of PLN 145mn), generated cash flow (EBITDA at PLN 105mn in 2007 and PLN 148mn in 2008) and debt. Duda is in the middle of the capital increase, including the issue of 48.2mn rights, each entitling to subscribe for 1 new share at PLN 3.0. The record date for the rights was on December 8, 2006 and as of this date the price was adjusted by the theoretical value of the rights, which will be traded separately (the prospectus has to be approved by market watchdog), most likely in January. Although the court approval is still pending, to reflect the factual impact of the capital increase and the subsequent fair value of the company's shares we assumed that the number of shares increased to 98.4mn and that proceeds were booked already in December. This impacts substantially the EPS and P/E figures calculated only for FY2006, as to comply with the IFRS, we used time-weighted average number of shares. As the issue is assumed in December, the EPS is overstated and P/E understated (the P/E based on 98.4mn number of shares is 27).

The Duda family recently cashed in some of the profits accrued since the company was set up, selling a 12.23% stake and decreasing their holding to 23.2%. Around 4.56mn shares have been sold at an average price of PLN 26.23 (with subscription rights) and 1.33mn at an average price of PLN 15.5 (without subscription rights). In case the additional 1.33mn subscription rights are executed and not sold, the stake held by the Duda family will amount to 25.0%

2007: Expansion continues, operating risk rising

Duda still has very strong growth potential and room for profitability enhancements. The new acquisitions fit in well with the general strategy and supplement the product assortment with interesting and robust niches. The Ukrainian market offers rapid growth and sound prospects. Furthermore, there are plenty of takeover targets for the long-term hunt both in Poland and throughout the region. On the other hand, the loosely connected bio-ethanol project will change the business profile and investment risk involved, but will not necessarily decrease the firm's value. We believe that Duda will not seek further needless diversification and will focus on its core business, meat. The company is currently facing the very challenging job of consolidating its newly-acquired companies in 2007. All in all, we have an hold recommendation on Duda shares.

Valuation

We employed a DCF model as our valuation tool to estimate the fair value of the company. The DCF is based on our forecasts for the years 2006-11. We used a discount rate based on WACC and a terminal value based on perpetuity. We discount all free cash flows for the firm on December 31, 2006 and subtract the forecasted net debt as of December 31, 2006. We then divide the equity value per number of shares. Afterwards, we compound this by the cost of equity (with the appropriate number of months). We thus arrive at a target price that represents our valuation of the stock price as it is expected to be 12 months into the future. The DCF led us to a target price of PLN 14.3 per share. The peer comparison indicates that Duda is currently traded at a 37% premium, which we believe is justified, given the company's growth prospects.

On top of the assumptions used for our financial forecasts, we based our calculations on:

- a risk free rate of 5%; equity premium 5%; debt premium 1.5%
- beta 1.0
- terminal value growth 1.5%

WACC

	2006e	2007e	2008e	2009e	2010e	2011e	beyond 2011
WACC	**8.6%**	**8.8%**	**8.5%**	**8.4%**	**8.4%**	**8.4%**	**8.4%**
Equity cost	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	9.9%
Debt cost	5.4%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%
Equity weighting	69.0%	74.5%	67.7%	67.0%	66.6%	66.7%	66.7%
Debt weighting	31.0%	25.5%	32.3%	33.0%	33.4%	33.3%	33.3%
Risk free rate	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
Equity risk premium	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
Beta	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Debt premium	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%
Tax rate	17.0%	19.0%	19.0%	19.0%	19.0%	19.0%	19.0%

Source: Erste Bank estimates

DCF

	2006e	2007e	2008e	2009e	2010e	2011e	beyond 2011
EBIT	**61,464**	**79,691**	**116,749**	**127,054**	**136,322**	**146,898**	**146,898**
Tax rate	17%	19%	19%	19%	19%	19%	19%
Tax on EBIT	10,449	15,141	22,182	24,140	25,901	27,911	27,911
NOPLAT	**51,015**	**64,549**	**94,567**	**102,913**	**110,421**	**118,987**	**118,987**
Depreciation	24,226	31,112	31,032	33,012	35,120	37,361	
Capital expenditures	60,000	144,600	92,000	33,012	35,120	37,361	
Change in working capital	12,644	65,113	38,831	11,923	11,311	11,943	
Free cash flow	**2,596**	**-114,052**	**-5,233**	**90,991**	**99,109**	**107,044**	
Terminal value	1,761,812						
PV of FCF	0	-104,833	-4,434	71,106	71,436	71,162	
Sum of PV of FCF	104,438						
PV of terminal value	1,171,243						
Enterprise value	**1,275,681**						
Non-operating assets	0						
Net debt at 31.12.2006	24,238						
Fair value at 31.12.2006	**1,251,443**						
Number of shares	96,400						
Fair value per share at 31.12.2006	**13.0**						
Cost of equtiy	10.0%						
Target Price	**14.3**						
Stock price	13.9						
Premium/discount	3%						

Source: Erste Bank estimates

Peers

	P/E			EV/Sales			EV/EBITDA			Valuation		
	2006e	2007e	2008e	2006e	2007e	2008e	2006e	2007e	2008e	2006e	2007e	2008e
Implied fair value	975,523	935,650	1,160,814	623,328	908,530	977,559	633,979	745,685	972,349			
Number of shares	96,400	96,800	97,200	96,400	96,800	97,200	96,400	96,800	97,200	**7.7**	**9.1**	**10.0**
Implied fair value per share	10.1	9.7	11.9	6.5	9.4	10.1	6.6	7.7	10.0			
12 month target price										**8.5**	**10.1**	**11.0**
Median for international peer group	**19.6**	**15.1**	**13.2**	**0.6**	**0.6**	**0.5**	**8.2**	**7.3**	**6.7**			
Nikas	12.98	10.76		1.3	1.2	1.0	8.6	7.3	7.0			
Ter Beke	17.43	15.93	13.44	0.5	0.4	0.4	5.9	5.3	4.8			
Hk Ruokatalo	19.69	16.91	12.67	0.7	0.6	0.5	10.6	8.2	6.6			
Cremonini SpA	21.84	17.16	21.29	0.4	0.4	0.4	6.8	6.4	6.7			
Devro International	15.84	13.99	13.17	1.5	1.4	1.4	7.9	7.3	6.9			
Atria Oyj	20.27	13.68	11.99	0.6	0.5	0.5	8.7	7.4	6.7			
Fleury Michon SA	19.48	15.83	13.83	0.5	0.5	0.5	5.7	4.8	4.3			
Sardus AB	30.19	14.46	10.25	0.7	0.6	0.6	10.2	8.3	6.9			

Source: JFC, Erste Bank estimates

Income Statement (IAS, PLN mn, 31/12)	2004	2005	2006e	2007e	2008e
Sales revenues	**533.4**	**870.0**	**1,029.3**	**1,635.2**	**1,993.9**
Cost of goods sold	-465.4	-765.4	-896.1	-1,427.3	-1,727.7
Gross profit	**68.0**	**104.6**	**133.3**	**207.9**	**266.3**
SG&A	-47.6	-82.7	-91.0	-139.7	-163.5
Other operating, net	9.6	16.8	19.2	11.4	14.0
EBITDA	**39.0**	**53.7**	**80.1**	**105.2**	**147.8**
Depreciation	-8.9	-15.0	-18.6	-25.5	-31.0
EBIT	**30.1**	**38.7**	**61.5**	**79.7**	**116.8**
Financial result	-0.2	-6.3	-1.1	-3.3	-7.9
EBT	**29.9**	**32.5**	**60.4**	**76.4**	**108.9**
Tax expenses	-5.0	-6.1	-10.3	-14.5	-20.7
Extraordinary result	-0.2	0.0	0.0	0.0	0.0
Minority interests	-1.4	0.7	-0.3	-0.1	-0.1
Net result after minorities	**23.3**	**27.1**	**49.8**	**61.8**	**88.1**

Balance Sheet (IAS, PLN mn, 31/12)	2004	2005	2006e	2007e	2008e
Intangible assets	78.1	90.5	95.3	95.3	95.3
Tangible assets	140.2	168.2	209.6	328.7	389.6
Financial assets	12.2	10.7	24.3	25.3	25.9
Total fixed assets	**230.5**	**269.4**	**329.1**	**449.2**	**510.8**
Inventories	49.3	58.9	67.2	107.0	129.6
Receivables and other current assets	100.3	119.9	272.5	204.4	249.2
Other assets	1.4	1.9	3.1	4.9	6.0
Cash and cash equivalents	14.0	16.9	10.3	16.4	19.9
Total current assets	**165.0**	**197.5**	**353.1**	**332.7**	**404.7**
TOTAL ASSETS	**395.5**	**467.0**	**682.2**	**781.9**	**915.5**
Shareholders' equity	**178.1**	**206.7**	**397.3**	**459.5**	**486.2**
Minorities	**6.0**	**-0.3**	**0.0**	**0.1**	**0.2**
Other reserves	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Interest-bearing LT debts	56.6	103.0	107.0	94.2	139.3
Other LT liabilities	2.2	1.1	1.9	1.9	1.9
Total long-term liabilities	**58.8**	**104.1**	**108.9**	**96.1**	**141.2**
Interest-bearing ST debts	84.5	73.8	71.3	121.3	92.9
Other ST liabilities	68.1	82.7	104.7	104.9	195.0
Total short-term liabilities	**152.6**	**156.5**	**176.0**	**226.2**	**287.9**
TOTAL LIAB. & EQUITY	**395.5**	**467.0**	**682.2**	**781.9**	**915.5**

Cash Flow Statement (IAS, PLN mn, 31/12)	2004	2005	2006e	2007e	2008e
Cash flow from operating activities	-9.5	-0.4	47.7	95.7	90.6
Cash flow from investing activities	-85.3	-27.3	-192.5	-61.2	-92.0
Cash flow from financing activities	74.7	30.5	138.2	-28.4	5.0
CHANGE IN CASH & CASH EQU.	**-20.1**	**2.9**	**-6.6**	**6.1**	**3.6**

Margins & Ratios	2004	2005	2006e	2007e	2008e
Sales growth	62.7%	63.1%	18.3%	58.9%	21.9%
EBITDA margin	7.3%	6.2%	7.8%	6.4%	7.4%
EBIT margin	5.6%	4.5%	6.0%	4.9%	5.9%
Net profit margin	4.4%	3.1%	4.8%	3.8%	4.4%
ROE	16.4%	14.1%	16.5%	14.4%	18.6%
ROCE	11.0%	7.8%	10.7%	10.1%	13.0%
Equity ratio	46.5%	44.2%	58.2%	58.8%	53.1%
Capital employed	313.4	367.4	567.2	660.7	700.6
Inventory turnover	14.2	14.2	14.2	16.4	14.6

Source: Company data, Erste Bank estimates

Company Report

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Rating history

Date	Product	Rating	Price	Price target
22. Feb 06	IC/CR	initiate coverage with Buy	12.80	16.00
4. Sep 06	CR	Buy	12.90	16.00

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Company	Disclosure	Comment
Duda	--	--

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