

23 August 2010

Update

**Chemicals**

Poland

Current price	PLN 28.27
Target price	PLN 34.50
Market cap	PLN 791.6m
Free float	PLN 304.2m
Avg daily trading volume (3M)	PLN 1.44m

Shareholders

State Treasury	36.68%
Pioneer Pekao IM	18.77%
OFE PZU	6.12%

Others 38.43%

Sector Outlook

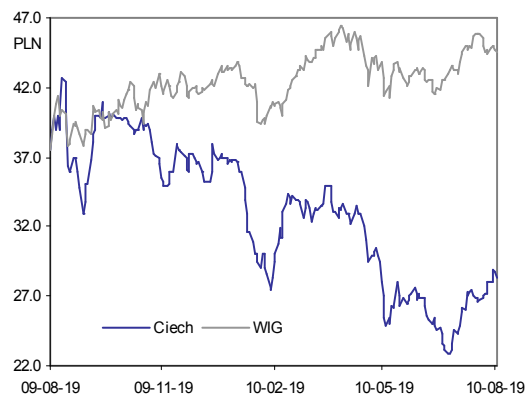
The current revival in the global economic climate has a direct impact on the demand for chemicals. Higher volumes facilitate earnings improvement, and the shrinking surplus of capacity over demand should help margins. For some products, the pressure from Chinese dumping is easing, as the country's internal demand rises.

Company Profile

Ciech is Poland's largest chemicals producer. It has a diversified business portfolio which consists of the Soda Division (second largest soda ash manufacturer in Europe), the Organic Division (TDI, EPI, epoxy resins), and the Agro Division (fertilizers, pesticides). Ciech runs operations in Poland as well as Germany and Romania.

Important dates

31.08 - H1 2010 report
15.11 - Q3 2010 report

Ciech vs. WIG**Kamil Kliszczyk**

(48 22) 697 47 06

kamil.kliszczyk@dibre.com.pl

www.dibre.com.pl

Ciech

CECH.WA; CIE.PW

Buy

(Reiterated)

Share Offering No Longer a Threat

Good news for Ciech has been coming in over the past few weeks: the sale of PTU, an agreement with EBRD and a clear improvement in the macroeconomic environment for the Organic segment. In our opinion, the environment should also improve for soda, where the market has already reached a medium-term trough (both demand and costs are rising, exerting a pressure on prices). We expect a considerable improvement in earnings starting in Q3'10, but in our opinion the second quarter already should bring a better quality EBIT vs. the preceding quarter. Let us also point out that should a negative scenario materialize for the global economy, Ciech should benefit from the security buffer foreign-exchange mechanisms provide (in the last crisis, it failed to work due to the problem of FCY options). In this context, we still see upside potential for the stock (there is an over 30% discount to other soda producers). We value it at PLN 34.5 per share and recommend buying it.

Situation Improves in the Key Markets

We have seen a very clear improvement in margins in the Organic segment, especially for resins (with record high prices 35% above the six-year average) and epichlorohydrin, where there are supply shortages due to the closure and failures at the BPA installation. In our opinion, these positive tendencies will be reflected in third-quarter earnings. In addition, we expect European soda prices to rebound, as a result of a lowered pressure from Chinese and US imports and increases in the prices of gas and coke, which should have less of an impact on Ciech.

Restructuring and Divestment

The long-promised acceleration of the Group restructuring process should be gaining speed in the coming months thanks to the Company's agreement with banks. We expect the finalization of divestment processes kicked off by the sale of PTU and the stake in ZAT. Altogether, selling non-core assets could reduce Ciech's net debt by over PLN 500m. In addition, the Management has promised to improve cost efficiency through the consolidation of companies comprised in the individual divisions. In our opinion, the Company should also review its Romanian investment and present a credible plan of arriving at sustained profitability, or else decide to close the factory down, which investors might welcome given the subsidiary's permanently negative impact on consolidated EBIT.

Minimized Risk of Unfair SPO

In recent months, the price of the stock has been impacted by the investors' concerns about a share offering that could be carried out to reduce debt, because the Treasury would presumably want to sell its preemptive rights. We believe that the recently-signed agreement with the EBRD has eliminated the risk of an unfair share offering, because the Treasury's shares could be acquired by the EBRD.

(PLN m)	2008	2009	2010F	2011F	2012F
Revenues	3 787.1	3 684.2	4 062.5	4 370.4	4 391.4
EBITDA	449.9	365.1	394.7	499.1	494.7
EBITDA margin	11.9%	9.9%	9.7%	11.4%	11.3%
EBIT	246.7	135.0	165.9	258.6	247.8
Net profit	-41.9	-85.5	87.7	92.2	77.4
DPS	2.07	0.00	0.00	0.00	0.00
P/E	-	-	9.0	8.6	10.2
P/CE	4.9	5.5	2.5	2.4	2.4
P/BV	0.9	1.0	0.9	0.8	0.7
EV/EBITDA	5.3	6.4	5.9	4.6	4.6
DYield	7.3%	0.0%	0.0%	0.0%	0.0%



Q2'10: Earnings Quality Expected to Improve

Ciech's operating earnings for Q2'10 should be close to its Q1'10 results, but we expect them to be of better structure thanks to the reduced impact of other operating activities in the Soda segment. We expect the Company to generate an EBIT of PLN 28m in this core area, compared to PLN 25.5m in the preceding quarter, with just ca. PLN 10m in cavern revenues (in Q1'10, the Company recorded one-off revenues of PLN 21m, including gains on the sale of emission credits). The improvement in recurrent earnings in the Soda segment will be a consequence of the slight increase in the zloty price of soda ash, higher volumes and the cost-cutting initiatives in Romania and Germany that the Management has recently promised. We expect a considerable improvement in earnings in the Organic segment, where the recent increases in resin and EPI prices should bring an EBIT of PLN 26m vs. PLN 9.5m in the preceding quarter. A seasonal drop in profits in the Agrochemical segment will be partially offset by a shift in the high season for pesticides, but the q/q difference will nonetheless be big (PLN 8m vs. PLN 26m at the EBIT level). All in all, consolidated EBIT should figure to PLN 39.5m, but due to the high level of interest expenses (ca. PLN 30m), F/X losses on open options (which will no longer be offset by the loan to the German soda subsidiary, already converted to capital) and a loss on the sale of shares in ZAT (PLN 8.3m) the Company will be in the red.

Consolidated quarterly earnings

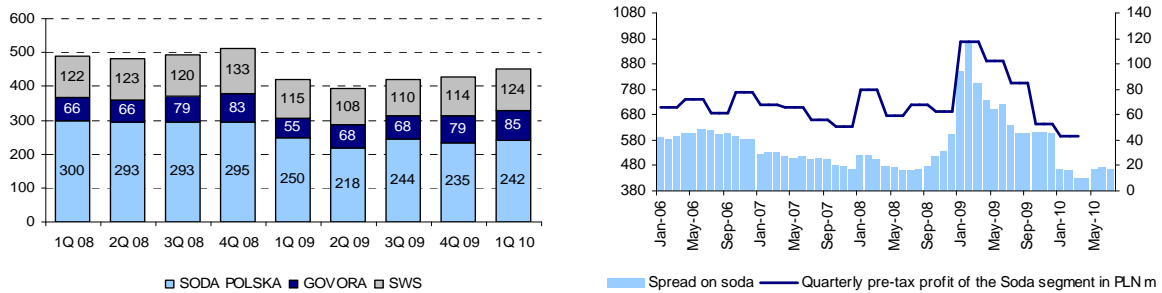
(PLN m)	Q2 2010F	Q2 2009	Change	Q1-2 2010F	Q1-2 2009	Change	2010F	2009	Change
Revenue	1 002.0	901.9	11.1%	1 964.0	1 893.6	3.7%	3 962.3	3 684.2	7.5%
EBITDA	98.4	147.5	-33.3%	199.0	295.1	-32.6%	461.0	365.1	26.3%
Margin	9.8%	16.4%	-	10.1%	15.6%	-	11.63%	10.86%	-
EBIT	39.5	96.1	-58.9%	81.1	181.6	-55.3%	233.0	135.0	72.6%
Pre-tax profit	-2.2	34.0	-	4.0	29.4	-	87.9	-88.0	-
Net profit	-1.8	29.0	-	-4.6	15.1	-	71.2	-85.5	-

Source: Ciech, BRE Bank Securities

Soda: Opportunity to Restore Higher Margins

After 2009 brought record-high profits, in 2010 the Soda segment turned out to be Ciech's biggest disappointment due to a clear deterioration in its profitability. One year ago, Ciech benefited from the weak zloty which hindered imports (especially of the much cheaper American and Turkish soda ash) and the high prices as expressed in foreign currencies (which reflected the European producers' break-even point at the then-high prices of energy and feedstock materials). The high unit margins more than offset the nearly 20% drop in sales volumes. However, already in H2 2009 European producers, faced with shrinking market shares, launched a price war with importers, which soon led to a 30% reduction in prices vs. Q1'09. In addition to having to cut its prices, Ciech suffered as its margin was impacted by the appreciating zloty. In Q1'2010, the effective price in Ciech's soda ash contract was over 38% lower than one year before, which shaved as much as PLN 75m off its adjusted EBITDA (-68%). Importantly, the heavy competition from Turkish natural soda ash, which flowed into southern Europe and depressed spot prices, was of considerable importance for the Romanian subsidiary US Govora, which is responsible for 19% of consolidated volumes. Another factor with impact on the global market was the rise in imports from China, where the government decided to support local producers through the introduction of preferential VAT rates (-9pp). With domestic demand declining, Chinese soda producers increased their export volumes, using dumping prices and squeezing out even the much more cost-effective suppliers, including American producers from ANSAC. The price war soon led to narrower margins, which declined to just few EUR per tonne for European manufacturers of synthetic soda ash, compared to the EUR 40/t average for the past 5 years. This dramatic situation surely accelerated the decision to shut down several soda ash manufacturing plants which had had trouble staying in the black before, e.g. Tata Chemicals' Dutch plant with annual capacity of 420 Kt, or to temporary capacity shutdown by some producers, e.g. the Romanian Ocna Mures (300 Kt) or the Ukrainian Lisichansk (250 Kt, though in the past its capacity was as much as 580 Kt).

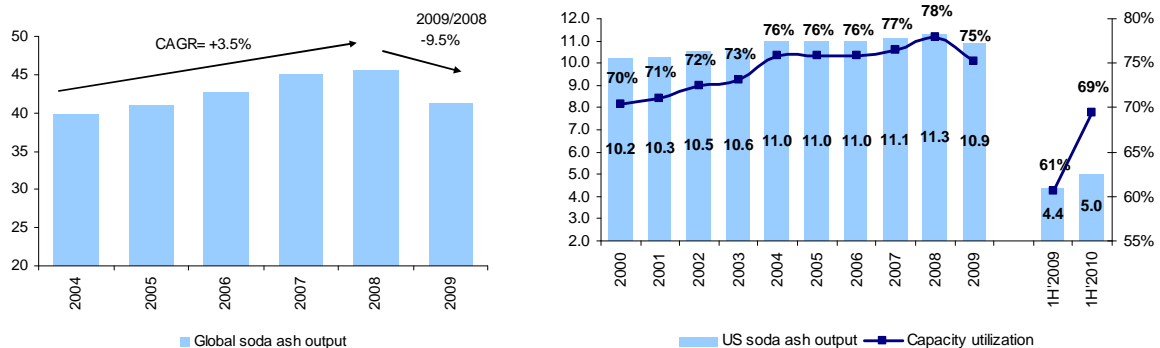
Quarterly soda ash sales, pre-tax income vs. soda ash margins*



*calculated as the spread between the price of one tonne of soda ash and the per-tonne cost of steam coal and coking coal
 Source: Ciech, BRE Bank Securities

In our opinion, there are reasons to believe that the onset of the year was the trough in the global market for soda ash, as a result of which the unfavorable trends will be reversed in the coming months. Industry data on demand suggest that the global demand for soda ash is recovering and that within 2-3 years consumption could return to levels observed before the crisis (in 2009, demand declined by 9.5% to a level last seen in 2005). This would clearly improve the market's equilibrium, by reducing surplus supply and opening an opportunity for an increase in capacity utilization from the historical low of 74%. According to the most recent market data, Chinese soda exports have declined by over 38% in the first half of the year, as a consequence of the rising prices and advantageous demand tendencies in the local market. This, in turn, facilitated the expansion of American soda in other Asian markets, particularly in India (in the first months of the year, ANSAC doubled the volume of exports in this direction), which reduced its supply in Europe (by 25%, with a contribution from the appreciating dollar as well). Another important factor is the rebound observed in the Russian market, where growth reached 20% y/y in the early months of the year, one of the reasons being the opening of a large glass factory.

Global soda ash output, capacity utilization in the USA



Source: USGS, estimates by BRE Bank Securities

According to industry specialists, in the coming years soda ash consumption should increase at 3-4% per year, driven not just by organic recovery, but also new glass factory openings which will add demand for some 0.6 Mt by 2013. When we compare these assumptions with the producers' capacity expansion plans (e.g. in Turkey), while bearing in mind the potential shutdowns of smaller, loss-making plants, we see that after stability has been reached this year, a gradual reduction in surplus supply should be visible in the coming years, which will help margins and prices. From Ciech's point of view, price trends in the markets for core feedstock materials will play an important role as well (coke and electricity, but also gas, used in the process of natural soda calcination, as well as in the form of ammonia in the modified Solvay process used by Chinese factories). In its Polish factories, Ciech commonly uses anthracite instead of the more expensive coke, and it produces energy in its own CHP plants fired with the cheaper Polish coal. Under a positive market scenario, increases in soda prices driven by the cost of feedstock materials will allow Ciech to improve its margins. Under a negative market scenario, a depreciation of the zloty vs. the EUR and the USD will provide cushioning for Ciech (as a reminder, this mechanism failed to work in 2009 due to the Company's huge positions in F/X options).

Soda Assets: Serious Review in Order?

Ciech's Soda division comprises four factories located in Poland, Germany and Romania, which are not uniform as far as the organization of the manufacturing process, quality of installations and economic activity are concerned. Ciech's most valuable assets are two Polish factories whose capacity account's for over 60% of the Group's aggregate potential. They look best as far as both technical parameters and profitability are concerned, thanks to the low cost of energy and feedstock (with in-house coal-fired CHP plants and the use of anthracite instead of coke in the manufacturing process), their strong position in the local market and competitive labor costs. In the case of the German plant, despite the highly advanced technology and low employment levels (with a mere 0.8 employee per tonne of output vs. 1.6 at the Polish plants), production is much less efficient due to the cost of external services (a considerable part of work not directly linked to manufacturing is outsourced) and the high cost of energy. The latter problem is a consequence of the fact that the Strassfurt-based subsidiary buys electricity and heat from a gas-fired CHP plant under a long-term contract based on a pricing formula which does not fully reflect the current shifts in the gas market (the drastic plunge in its price had only a minor impact on the price paid for heat and energy). Profitability is improved by the sale of caverns, as these are systematically emptied of the salt brine used in the Solvay process. Based on data provided by the Company, we estimate that the discounted value of cash flows stemming from the cavern deal with RWE is some PLN 82m. In this context, while the current prices of soda ash do not guarantee a break even at the German subsidiary, there are reasons to keep it operational, since it does not weigh consolidated earnings down in a material way; also, exposure to this part of Europe may help improve volumes in the coming years (the 600 Kt nameplate capacity was used at only 78% in 2009) and make it possible to take advantage of the closures of smaller European plants.

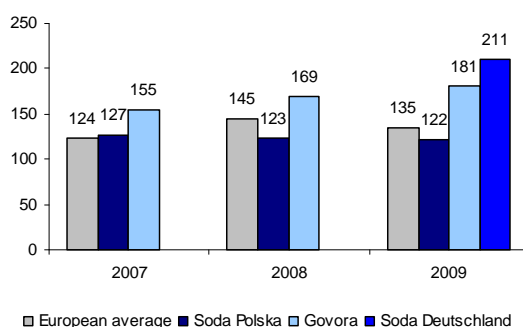
Estimated cash flows from Soda Deutschland's cavern deal

	2010F	2011F	2012F	2013F	2014F	2015F	2016F	2017F
Revenues in EUR ths.	700	2 000	500	9 600	300	3 000	12 000	7 900
Revenues in PLN ths.	2 835	8 000	1 900	35 520	1 050	10 500	42 000	27 650
Tax	0	1 672	722	1 476	2 062	1 397	1 663	532
DCF	2 769	5 752	995	26 675	-735	6 120	25 072	15 563
Total DCF in PLN ths.	82 211							

Source: Ciech, BRE Bank Securities

In this comparison, the Romanian US Govora looks clearly the worst. Due to the old technology employed in it, the costs of feedstock and energy are much higher than in Poland (also in consequence of the use of gas in the manufacturing process and external energy purchases), with another problem in the form overemployment (with three times as many employees as in the German plant despite output at half the level of the latter, and half the employees of the Polish factories with only a quarter of their output). Of course, employment per tonne of output needs to be seen in the context of outsourcing, but as the chart below shows, Govora does look worse than Soda Polska also when unit expenses on materials and services are concerned.

Unit cost of soda ash production, EUR/t



Source: Ciech, CMAI, BRE Bank Securities

Another important factor is the fact that the plant is located in a region where competition is intensive, especially from Turkish suppliers, which forces producers to rely on the more volatile spot contracts. This leads to greater earnings volatility and makes margin management

difficult, given the typically long-term contracts for energy. Finally, despite considerable investment (nearly PLN 118m since 2007), the plant is still plagued by frequent installation failures, as a result of which daily targets are frequently missed.

Financial, operational data for US Govora

(PLN m)	2007	2008	2009
Revenue	145.8	182.3	188.5
incl. soda ash	123.5	163.4	169.9
Sales (thousands of tons)	257	274	213
	0.480	0.596	0.797
Cost of feedstock	150.76	161.54	166.63
per 1t of soda ash	0.587	0.590	0.782
Profit after feedstock and services	-5.0	20.7	21.9
Estimated cost of labor**	61.3	64.8	53.4
EBITDA**	-66.3	-44.0	-31.5
Net profit	-71.1	-88.7	-69.6
CAPEX	35.7	48.0	34.2
Loans	60.9	85.3	52.6

*excluding payroll and depreciation expenses

**our estimates for lack of data

Source: Ciech, BRE Bank Securities

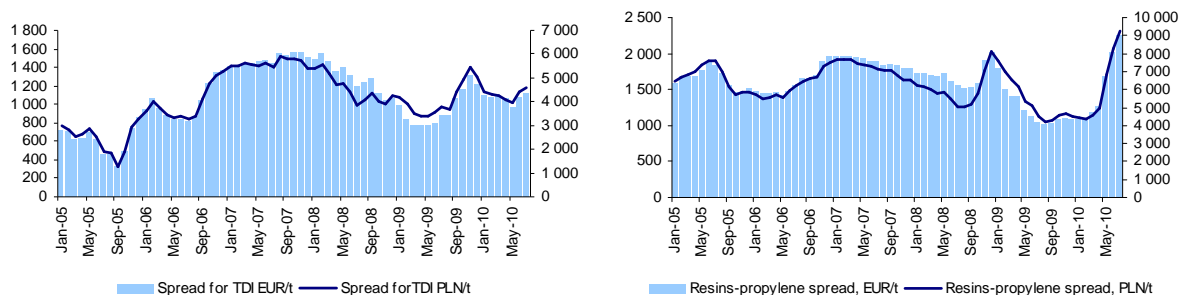
Ciech purchased a 92.9% stake in the Romanian factory in 2006 for PLN 39.8m, although its outlays total PLN 264m including loans and share capital increase (the full amount has already been written off the balance sheet). Despite restructuring and support from Ciech, Govora is consistently in the red, even when macroeconomic conditions seem to be to its advantage. In this context, it is natural to ask whether it makes sense to keep Govora within Ciech. Efforts undertaken so far have failed to bring results; therefore, liquidation of the plant to reduce losses is a scenario that cannot be precluded. In our opinion, the financial agreement with creditor banks should not be an obstacle to such a move, as the collaterals and mortgages which are of importance for them are concentrated in Poland, and Govora's debt will be consolidated by the parent company. A potential problem are the promises Ciech made in the privatization process, which, if broken, would lead to the imposition of a fee in the amount of 10% of the price paid for Govora. Still, this fee would only amount to PLN 4m, which is not a lot in the context of losses Govora generates every year. However, we do not know the legal details of the privatization agreement and we are therefore unable to say whether this would indeed be the only cost associated with the closure of this plant (whose loans are part of Ciech's current net debt). To sum up, we believe that in the current difficult situation in the soda ash market, the Management will have to either present a credible path towards regaining profitability at the Romanian subsidiary, or else decide to shut it down. The market should welcome either of these moves.

Organic Segment: Positive Tendencies in Resins, EPI

Within the organic segment, we have recently been observing a clear improvement in prices and margins on the Company's key products, which in our opinion should allow positive earnings trends to continue. A crucial category are resins and EPI, where margins calculated relative to the main feedstock material (propylene) have now reached record-high levels (30-40% above the 5Y average when expressed in the PLN). Prices started to increase in this market early in the year due to the global resin shortage caused by a combination of a reviving demand and reduced supply of one of the main feedstock materials, BPA (whose cost accounts for ca. 20% of the price of resin). As a result of the crisis, some of the manufacturers stopped production, and the imbalance was further exacerbated by a failure of a large phenol installation at Dow Chemical. To be sure, the share of resins and epichlorohydrin on the segment's total sales is a mere 26-28%, but nevertheless such a considerable expansion in crack spreads should in our view considerably boost the profit. Should these levels be sustained next year, revenue would increase by PLN 70-80m y/y, and this is why we have decided to assume a higher EBIT in the segment. In the case of the most important product of the Organic Division, TDI, the crisis seems to be ending as well, with profitability recovering. However, crack spreads on this product are near the 5Y average and we do not expect them to increase further, all the more so that demand from China (which accounts for ca. 27% of

global consumption) is increasingly satisfied at home (in H1 2010, the share of imports declined from 31% to 23%). Furthermore, new capacity is scheduled for launch in 2011 in China (ca. 300 Kt, i.e. +14%), which may exert an additional pressure in the global market despite the forecasts that demand will be growing at 7% p.a. through 2014.

Processing spreads on TDI* and epoxy resins (EUR/t, PLN/t)

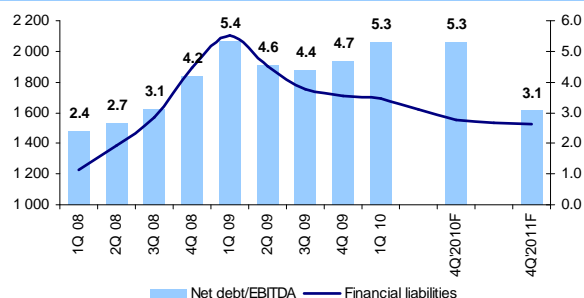


*spread between TDI prices and weighted costs of toluene and nitric acid
 Source: Bloomberg, ICIS-LOR, estimates by BRE Bank Securities

Disinvestments and the Agreement with Banks

In H1 2010, Ciech finalized a refinancing agreement with a consortium of seven banks, which had been the subject of negotiations for over a year. Under the agreement, the banks promised to keep credit open through 2012 (including a new PLN 1.1bn credit line), refinance Ciech's debt towards other banks (PLN 100m) and provide refinancing for liabilities stemming from foreign-currency options (whose negative valuation was PLN 140m as of the day when the agreement was signed). For its part, Ciech undertook to keep quarterly amortization of this debt at no less than PLN 10m, and to repay the entire amount by the end of March 2011 (although the funds must be in the Company's account by the end of 2010). For this reason, as well as in preparation for efforts to secure long-term financing from 2012 onwards (which is also when corporate bonds of PLN 300m mature; the remainder of the consolidated debt total of PLN 252m is in loans the German soda subsidiary took out from Commerzbank, which do not mature until 2014), the Management has prepared a restructuring program whose goal is to increase operating efficiency and carry out certain divestments.

Net debt vs. 12M moving EBITDA



Source: Ciech, BRE Bank Securities

The restructuring program in question foresees the divestment of at least the following assets: stakes in PTU and ZA Tarnów (these transactions have been carried out, bringing an aggregate cash flow of PLN 159m, in addition, PLN 9m was obtained from the sale of Elzab and Ciech Service), in Fosfory, Alwernia, Vitrosilicon and a number of smaller subsidiaries and properties. Coupled with the planned downsizing and cost streamlining in other business areas, these projects should bring ca. PLN 600m in income and savings. Below, we list the key assets earmarked for divestment, including the expected price and the impact of the transaction on consolidated net debt. The calculations suggest that including funds obtained for ZAT and PTU, the grand total is some PLN 420m. Let us point out that due to the considerable indebtedness of some of these subsidiaries, the impact of the transactions on consolidated net debt may be even greater, perhaps in excess of PLN 590m. We are aware, however, that the divestment process is very sensitive to external factors and will be spread out in time, which makes it difficult to factor in such developments into the model at this time. It is also worth remembering that the procedures have already been launched in a number of cases (e.g. Fosfory, the Powązkowska St. property in Warsaw).

**Divestible assets (PLN m)**

Company	Loans at the end of 2009	Equity	Value in Ciech's balance sheet	Potential value of the divestment	Impact on consolidated net debt	Ciech's share
Fosfory Gdańskie	106.2	114.7	20.9	71.8	178.0	89.5%
Vitrosillicon	46.4	66.8	12.3	90.6	137.0	100.0%
Alwernia	15.1	72.9	55.0	44.7	59.8	73.8%
Polfa Ciech	-	9.9	1.9	13.5	13.5	100.0%
Transoda	-	21.0	-	20.9	20.9	99.8%
Transclean	-	7.1	2.2	6.6	6.6	93.7%
Powązkowska St. property	-	-	15.8	20.0	20.0	100.0%

Source: Ciech, BRE Bank Securities

An important element of the agreement with banks is Ciech's promise to repay PLN 400m by the end of March 2011. This will not be feasible on the basis of current operating cash flows and divestments carried out so far, which is why the Management announced a share capital increase or a bond offering were possible. With the Treasury among Ciech's shareholders, investors were concerned about additional supply of preemptive rights, which could be detrimental to the other shareholders. However, as the Company's environment improves in H2 2010, the need for these additional funds will not be that pressing. In this context, the recent mandate letter with the EBRD, which wants to provide up to PLN 300m in financing, is good news as well, as this could be used to meet the terms of the agreement with the banks (by way of example, the EBRD could acquire the Treasury's rights if there is a share capital increase).

Earnings Forecast and Valuation

Based on DCF analysis and relative valuation, we set the per-share price target on Ciech at PLN 34.5.

	Weight	Price
Relative Valuation	50%	30.8
DCF Analysis	50%	33.1
	price	32.0
	9M Target Price	34.5

DCF Analysis

Assumptions:

- The valuation model takes into account Ciech's production plans and macroeconomic factors as presented in the following table.

	2007	2008	2009	2010F	2011F	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F
Sales (thousands of tons)													
Soda ash	1 368	1 973	1 678	1 950	2 131	2 181	2 181	2 181	2 181	2 181	2 181	2 181	2 181
TDI	58	49	63	75	75	75	75	75	75	75	75	75	75
EPI	19	17	10	18	18	18	18	18	18	18	18	18	18
Resins	26	34	37	35	39	39	39	39	39	39	39	39	39
Fertilizers	181	188	123	150	150	150	150	150	150	150	150	150	150
Product prices													
Soda ash (EUR/t)	178	206	220	179	190	200	210	215	217	219	222	224	226
TDI (EUR/t)	2 592	2 850	1 960	2 259	2 367	2 622	2 600	2 665	2 732	2 800	2 870	2 942	3 015
EPI (EUR/t)	1 705	1 698	1 226	1 673	1 824	1 589	1 589	1 589	1 589	1 589	1 589	1 589	1 589
Epoxy resins (EUR/t)	2 787	2 555	1 848	2 666	2 700	2 600	2 600	2 600	2 600	2 600	2 600	2 600	2 600
DAP (USD/t)	423	974	319	490	515	568	578	578	578	578	578	578	578
Average EUR/PLN exchange rate	3.78	3.48	4.33	4.05	4.00	3.80	3.70	3.50	3.50	3.50	3.50	3.50	3.50
Avg. USD/PLN exchange rate	2.77	2.42	3.12	3.08	3.10	2.90	2.80	2.70	2.70	2.70	2.70	2.70	2.70

- Cash flows are discounted to their present value as of 31 August 2010.
- Valuation factors in non-operating assets earmarked for sale with a total value of PLN 198m, which include gas salt caverns (PLN 82.2m after taxes, based on the Company's cash-flow projections through 2017 and excluding funds received in 2009), an office building in Warsaw (PLN 20m), and stakes in Polfa Ciech (PLN 10.5m), Transoda (PLN 20.8m), Transclean (PLN 6.6m), Alwernia (PLN 60.5m) and Boruta-Kolor (PLN 10.3m).
- Disinvestment projects completed in 2010 (a 45.3% stake in PTU, shares in ZA Tarnów, Elzab and shares in Ciech Service) totaling PLN 168m are taken into account in FY10 cash flows as equity investments.
- In the DCF model, EBITDA for FY2010-19 is adjusted for cavern proceeds which are shown under "non-operating assets" in their full discounted amount.
- We adjust our valuation for liabilities stemming from F/X options, which were converted to loans this year.
- When calculating FCF_{TV} , we based terminal value calculations on the sales growth rate and EBITDA margins projected for 2019.
- We assume that FCF will grow at a rate of 1% after FY2019. The risk-free rate is 5.3%, and beta is 1.1%.



DCF Valuation Model

(PLN m)	2010F	2011F	2012F	2013F	2014F	2015F	2016F	2017F	2018F	2019F	2019+
Sales revenue	4 062	4 370	4 391	4 395	4 292	4 334	4 377	4 421	4 466	4 513	4 562
Change	10.3%	7.6%	0.5%	0.1%	-2.4%	1.0%	1.0%	1.0%	1.0%	1.1%	1.1%
adjusted EBITDA	344.9	490.3	490.9	478.5	449.4	465.1	481.2	497.7	511.4	520.8	526.4
EBITDA margin	8.5%	11.2%	11.2%	10.9%	10.5%	10.7%	11.0%	11.3%	11.5%	11.5%	11.5%
D&A expenses	228.9	240.5	246.9	254.0	247.2	251.6	256.2	262.7	270.6	260.7	250.0
adjusted EBITDA	116.0	249.8	244.0	224.5	202.2	213.5	225.0	235.0	240.8	260.1	276.4
EBIT margin	2.9%	5.7%	5.6%	5.1%	4.7%	4.9%	5.1%	5.3%	5.4%	5.8%	5.8%
Tax rate on EBIT	22.0	47.5	46.4	42.6	38.4	40.6	42.7	44.7	45.8	49.4	52.5
NOPLAT	94.0	202.4	197.6	181.8	163.8	173.0	182.2	190.4	195.1	210.7	223.9
CAPEX	-238.0	-319.0	-286.0	-262.0	-254.0	-250.0	-250.0	-250.0	-250.0	-250.0	-250.0
Working capital	-20.1	-16.4	-1.1	-0.2	5.5	-2.2	-2.3	-2.3	-2.4	-2.5	-2.5
Equity investments	168.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
FCF	232.7	107.5	157.4	173.6	162.5	172.3	186.2	200.7	213.3	218.8	221.3
WACC	7.3%	7.5%	7.6%	7.8%	7.9%	8.0%	8.2%	8.3%	8.5%	8.7%	9.7%
discount factor	97.7%	90.9%	84.5%	78.4%	72.6%	67.2%	62.2%	57.4%	52.9%	48.7%	48.7%
PV FCF	227.3	97.7	133.0	136.0	118.0	115.8	115.7	115.2	112.8	106.5	
WACC	7.3%	7.5%	7.6%	7.8%	7.9%	8.0%	8.2%	8.3%	8.5%	8.7%	9.7%
Cost of debt	6.3%	6.3%	6.3%	6.3%	6.3%	6.3%	6.3%	6.3%	6.3%	6.3%	6.3%
Risk-free rate	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%
Risk premium	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%
Effective tax rate	19.0%	19.0%	19.0%	19.0%	19.0%	19.0%	19.0%	19.0%	19.0%	19.0%	19.0%
Net debt / EV	61.8%	59.1%	56.3%	53.4%	51.5%	49.2%	46.7%	44.3%	41.4%	38.1%	20.0%
Cost of Equity	10.8%	10.8%	10.8%	10.8%	10.8%	10.8%	10.8%	10.8%	10.8%	10.8%	10.8%
Risk premium	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
Beta	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
FCF growth after the forecast horizon				1.0%	Sensitivity analysis						
Terminal value				2 546.9	FCF growth in perpetuity						
Present value of terminal value				1 240.1		0.0%	1.0%	2.0%	3.0%	4.0%	
Present value of FCF in the forecast horizon				1 278.2	WACC +1.0pp	26.9	30.9	35.8	42.0	50.1	
Enterprise Value				2 518.3	WACC +0.5pp	28.8	33.2	38.7	45.8	55.1	
Net debt				1 641.1	WACC	30.9	35.8	42.0	50.1	61.0	
Minority interests				37.2	WACC -0.5pp	33.2	38.7	45.8	55.1	68.1	
Value of non-operating assets				198.2	WACC -0.10pp	35.8	42.0	50.1	61.0	76.6	
Value of options converted to debt				110.0							
Equity value				928.2							
Number of shares (millions)				28.0							
Equity value per share (PLN)				33.1							
Cost of equity (9M)				8.0%							
Target Price				35.8							
EV/EBITDA for the target price				5.9							
P/E for the target price				11.4							
TV to EV				49%							



Relative Valuation

We compared Ciech's P/E and EV/EBITDA multiples with the multiples of its peers estimated for FY2010 through FY2012 (since cavern payments are factored into net debt, we exclude bookkeeping revenue on this account from net profit and EBITDA, and we apply the same to the PTU divestment). The peer group consists of European chemical manufacturers with business portfolios similar to Ciech's. They include international holdings with diversified profiles as well as specialized companies whose specialty areas match Ciech's business lines. Companies with large-scale soda manufacturing operations include Solvay, Dow Chemical, Tata Chemicals, Soda Sanayii, Sisecam, Tessenderlo, and Wacker Chemie. Companies whose business mixes include the same products as produced by Ciech, such as agrochemicals and organic chemicals, are Akzel Nobel, Croda, Rhodia, BASF, Dow Chemical, Tata.

	Price	P/E				EV/EBITDA			
		2009	2010F	2011F	2012F	2009	2010F	2011F	2012F
Akzo Nobel	43.42	18.7	12.5	11.3	10.0	6.9	6.1	5.6	5.3
BASF	43.53	21.4	9.9	9.2	8.3	7.4	5.2	4.9	4.6
Croda International	12.62	25.2	14.5	13.3	12.2	13.4	9.2	8.6	8.0
Dow Chemical	25.16	53.9	14.5	10.4	7.7	9.6	7.3	6.4	5.5
FMC	60.72	14.7	12.5	11.2	9.4	8.2	7.2	6.6	n/a
Sisecam	1.91	16.7	9.0	7.6	7.3	6.0	4.9	4.2	3.9
Solvay	71.47	12.7	22.4	20.3	17.2	6.5	8.1	7.8	7.2
Soda Sanayii	1.62	6.8	6.8	5.6	4.7	5.7	6.0	5.2	4.6
Tata Chemicals	378.95	12.5	14.4	12.3	10.1	6.8	7.9	7.2	6.8
Tessenderlo Chemie	22.05	-10.8	30.9	11.9	8.7	15.7	6.4	5.1	4.2
Wacker Chemie	125.40	39.2	14.4	12.5	10.9	11.0	6.1	5.5	5.0
Maximum		53.9	30.9	20.3	17.2	15.7	9.2	8.6	8.0
Minimum		-10.8	6.8	5.6	4.7	5.7	4.9	4.2	3.9
Median		16.7	14.4	11.3	9.4	7.4	6.4	5.6	5.2
Ciech	28.27	-9.2	67.1	8.6	10.3	6.1	6.4	4.5	4.5
(premium / discount)		-	365.6%	-23.4%	9.3%	-17.9%	0.2%	-20.1%	-12.5%
Implied price									
Median		16.7	14.4	11.3	9.4	7.4	6.4	5.6	5.2
Multiple weight			50.0%				50.0%		
Year weight		0.0%	33.3%	33.3%	33.3%	0.0%	33.3%	33.3%	33.3%
Equity value per share (PLN)		30.8							

EV/EBITDA based on net debt at the end of 2009

Net debt is adjusted for the value of non-operating assets and the stake in ZA Tarnów..

Earnings are adjusted for the effects of provision reversals and the proceeds of cavern sales and other divestments.

**Income Statement**

(PLN m)	2006	2007*	2008	2009	2010F	2011F	2012F
Sales revenue	2 174.3	3 415.0	3 787.1	3 684.2	4 062.5	4 370.4	4 391.4
<i>Change</i>	-1.6%	57.1%	10.9%	-2.7%	10.3%	7.6%	0.5%
EBIT by business segment							
Soda Division	n/a	126.1	114.4	204.4	128.9	163.9	165.6
Organic Division	n/a	167.5	-4.0	-33.2	69.0	119.2	97.6
Agro Division	n/a	65.8	97.0	-31.9	39.5	36.1	44.4
Silicates & Glass Division	n/a	9.5	16.1	9.3	12.9	13.8	14.7
Unallocated expenses	n/a	-326.0	23.2	-13.6	-84.4	-74.4	-74.4
EBIT	192.0	43.0	246.7	135.0	165.9	258.6	247.8
<i>Change</i>	33.7%	-77.6%	473.9%	-45.3%	22.9%	55.9%	-4.2%
<i>EBIT margin</i>	8.8%	1.3%	6.5%	3.7%	4.1%	5.9%	5.6%
Profit/loss on financial activity	3.5	-30.0	-250.7	-219.2	-57.6	-144.8	-152.2
Extraordinary gains/losses	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pre-tax profit	197.4	18.1	-7.3	-88.0	108.3	113.8	95.6
Tax	28.2	48.1	24.3	4.4	20.6	21.6	18.2
Minority interests	0.3	1.7	10.4	-6.9	0.0	0.0	0.0
Net profit	195.7	-31.7	-41.9	-85.5	87.7	92.2	77.4
<i>Change</i>	75.4%	-116.2%	32.2%	103.9%	-202.5%	5.1%	-16.0%
<i>Margin</i>	9.0%	-0.9%	-1.1%	-2.3%	2.2%	2.1%	1.8%
D&A expenses	95.9	179.3	203.3	230.1	228.9	240.5	246.9
EBITDA	287.8	222.3	449.9	365.1	394.7	499.1	494.7
<i>Change</i>	22.1%	-22.8%	102.4%	-18.9%	-5.5%	42.2%	0.1%
<i>EBITDA margin</i>	13.2%	6.5%	11.9%	9.9%	9.7%	11.4%	11.3%
Shares at year-end (millions)	28.0	28.0	28.0	28.0	28.0	28.0	28.0
EPS	7.0	-1.1	-1.5	-3.1	3.1	3.3	2.8
CEPS	10.4	5.3	5.8	5.2	11.3	11.9	11.6
ROAE	18.6%	-2.9%	-4.4%	-10.2%	10.1%	9.6%	7.4%
ROAA	8.7%	-0.9%	-1.0%	-2.0%	2.2%	2.2%	1.8%

*Ciech changed the approach to the presentation of earnings by business segment in 2009. Hence, segment EBIT figures for 2007 and 2008 are our estimates.

**Balance Sheet**

(PLN m)	2006	2007	2008	2009	2010F	2011F	2012F
ASSETS	2 859.3	3 966.3	4 346.6	4 024.1	4 075.4	4 222.0	4 245.2
Fixed assets	1 755.3	2 401.8	2 766.3	2 758.1	2 681.3	2 723.8	2 739.8
Property, plant and equipment	1 518.4	2 004.8	2 350.8	2 409.4	2 409.0	2 449.0	2 464.7
Intangible assets	97.7	202.6	192.9	164.9	165.4	167.8	168.2
Goodwill	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Long-term receivables	0.0	0.0	0.0	23.6	23.6	23.6	23.6
Other fixed assets	139.2	194.4	222.6	160.3	83.4	83.4	83.4
Current assets	1 104.1	1 564.5	1 580.3	1 266.1	1 394.1	1 498.3	1 505.4
Inventories	245.8	284.4	437.1	314.2	346.5	372.8	374.5
Short-term receivables	699.3	969.8	930.7	801.0	883.2	950.2	954.7
Accruals	13.3	185.9	100.4	19.2	19.2	19.2	19.2
Overdraft facility	14.3	28.9	66.3	78.6	78.6	78.6	78.6
Cash and cash equivalents	131.3	95.6	45.8	53.0	66.5	77.5	78.3
LIABILITIES	2 859.3	3 966.3	4 346.6	4 024.1	4 075.4	4 222.0	4 245.2
Equity	1 137.3	1 067.5	849.4	823.0	910.6	1 002.8	1 080.3
Share capital	164.1	164.1	164.1	164.1	164.1	164.1	164.1
Other equity	979.4	922.3	777.0	711.2	798.9	891.1	968.5
Long-term liabilities	496.4	1 070.3	879.3	999.3	1 161.6	1 144.5	1 106.7
Loans	316.9	756.0	388.9	665.9	988.0	979.7	945.7
Other	179.6	314.3	490.4	333.4	173.6	164.8	161.0
Short-term liabilities	1 175.5	1 783.6	2 568.5	2 164.7	1 965.9	2 037.5	2 021.1
Loans	316.8	480.6	1 264.9	921.2	628.1	622.8	601.2
Trade creditors	542.7	851.5	881.1	919.2	1 013.6	1 090.4	1 095.6
Accruals	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	301.7	422.6	356.2	245.6	245.6	245.6	245.6
Debt	633.7	1 236.6	1 653.8	1 587.1	1 616.1	1 602.6	1 546.9
Net debt	502.4	1 141.0	1 608.0	1 534.1	1 549.6	1 525.1	1 468.6
(Net debt / Equity)	44.2%	106.9%	189.3%	186.4%	170.2%	152.1%	135.9%
(Net debt / EBITDA)	1.7	5.1	3.6	4.2	3.9	3.1	3.0
BVPS	40.6	38.1	30.3	29.4	32.5	35.8	38.6

**Cash Flows**

(PLN m)	2006	2007	2008	2009	2010F	2011F	2012F
Cash flows from operating activities	176.5	243.2	33.0	393.6	308.3	454.0	474.5
Net profit	195.7	-31.7	-41.9	-85.5	87.7	92.2	77.4
D&A expenses	95.9	179.3	203.3	230.1	228.9	240.5	246.9
Working capital	-55.3	-121.4	-156.7	165.2	-20.1	-16.4	-1.1
Other	-62.8	212.8	136.7	45.9	11.9	137.6	151.3
Cash flows from investing activities	-483.5	-575.8	-426.2	-318.4	-50.1	-283.0	-263.0
CAPEX	-160.6	-244.6	-456.8	-252.2	-238.0	-319.0	-286.0
Equity investments	-300.6	-372.5	-100.2	-71.3	0.0	0.0	0.0
Other	-22.3	40.3	130.8	15.9	187.9	36.0	23.0
Cash flows from financing activities	346.0	296.7	337.6	-64.2	-244.7	-160.0	-210.8
Stock issues	0.0	15.5	0.0	0.0	0.0	0.0	0.0
Debt	367.5	342.4	406.8	-46.9	-81.0	-13.5	-55.7
Dividend (buy-back)	-23.2	-58.5	-58.0	-6.3	0.0	0.0	0.0
Other	1.8	-2.7	-11.3	-11.0	-163.7	-146.4	-155.1
Change in cash	39.0	-35.9	-55.7	11.1	13.5	11.0	0.8
Cash at period-end	131.3	95.6	45.8	53.0	66.5	77.5	78.3
DPS (PLN)	0.80	2.10	2.07	0.00	0.00	0.00	0.00
FCF	-256.7	-564.4	-288.1	218.4	254.1	169.3	208.7
(CAPEX / Sales)	7.4%	7.2%	12.1%	6.8%	5.9%	7.3%	6.5%

Market multiples

	2006	2007	2008	2009	2010F	2011F	2012F
P/E	4.0	-25.0	-18.9	-9.3	9.0	8.6	10.2
P/CE	2.7	5.4	4.9	5.5	2.5	2.4	2.4
P/BV	0.7	0.7	0.9	1.0	0.9	0.8	0.7
P/S	0.4	0.2	0.2	0.2	0.2	0.2	0.0
FCF/EV	-19.8%	-29.2%	-12.0%	9.4%	10.9%	7.3%	9.2%
EV/EBITDA	4.5	8.7	5.3	6.4	5.9	4.6	4.6
EV/EBIT	6.7	45.0	9.7	17.2	14.1	9.0	9.1
EV/S	0.6	0.6	0.6	0.6	0.6	0.5	0.5
DYield	2.8%	7.4%	7.3%	0.0%	0.0%	0.0%	0.0%
Price (PLN)	28.27						
Shares at year-end (millions)	28.0	28.0	28.0	28.0	28.0	28.0	28.0
MC (PLN m)	791.6	791.6	791.6	791.6	791.6	791.6	791.6
Equity attributable to minority shareholders (PLN m)	50.0	44.9	49.4	37.2	37.2	37.2	37.2
EV (PLN m)	1 293.9	1 932.5	2 399.5	2 325.7	2 341.2	2 316.6	2 260.2



Michał Marczak tel. (+48 22) 697 47 38
Managing Director
Head of Research
michal.marczak@dibre.com.pl
Strategy, Telco, Mining, Metals, Media

Research Department:

Kamil Kliszczyk tel. (+48 22) 697 47 06
kamil.kliszczyk@dibre.com.pl
Fuels, Chemicals, Energy, Retail

Piotr Grzybowski tel. (+48 22) 697 47 17
piotr.grzybowski@dibre.com.pl
IT, Media

Maciej Stokłosa tel. (+48 22) 697 47 41
maciej.stoklosa@dibre.com.pl
Construction, Real-Estate Developers

Jakub Szkopek tel. (+48 22) 697 47 40
jakub.szkopek@dibre.com.pl
Manufacturers

Iza Rokicka tel. (+48 22) 697 47 37
iza.rokicka@dibre.com.pl
Banks

Sales and Trading:

Piotr Dudziński tel. (+48 22) 697 48 22
Director
piotr.dudzinski@dibre.com.pl

Marzena Łempicka-Wilim tel. (+48 22) 697 48 95
Deputy Director
marzena.lempicka@dibre.com.pl

Traders:

Emil Onyszczyk tel. (+48 22) 697 49 63
emil.onyszczyk@dibre.com.pl

Grzegorz Stępień tel. (+48 22) 697 48 62
grzegorz.stepien@dibre.com.pl

Tomasz Dudź tel. (+48 22) 697 49 68
tomasz.dudz@dibre.com.pl

Michał Jakubowski tel. (+48 22) 697 47 44
michal.jakubowski@dibre.com.pl

Tomasz Jakubiec tel. (+48 22) 697 47 31
tomasz.jakubiec@dibre.com.pl

Grzegorz Strublewski tel. (+48 22) 697 48 76
grzegorz.strublewski@dibre.com.pl

Michał Stępkowski tel. (+48 22) 697 48 25
michal.stepkowski@dibre.com.pl

Foreign Markets Unit:

Adam Prokop tel. (+48 22) 697 48 46
Foreign Markets Manager
adam.prokop@dibre.com.pl

Michał Roźmiej tel. (+48 22) 697 48 64
michal.rozmiej@dibre.com.pl

Jakub Słotkiewicz tel. (+48 22) 697 48 64
jakub.slotkiewicz@dibre.com.pl

Jacek Wrześniewski tel. (+48 22) 697 49 85
jacek.wrzesniewski@dibre.com.pl

"Private Broker"

Jarosław Banasiak tel. (+48 22) 697 48 70
Manager, "Private Broker" Team
jaroslaw.banasiak@dibre.com.pl

Jacek Szczepański tel. (+48 22) 697 48 26
Director, Active Sales
jacek.szczepanski@dibre.com.pl

Dom Inwestycyjny
BRE Banku S.A.
ul. Wspólna 47/49
00-950 Warszawa
www.dibre.com.pl

**List of abbreviations and ratios contained in the report:**

EV – net debt + market value
EBIT – Earnings Before Interest and Taxes
EBITDA – EBIT + Depreciation and Amortisation
P/CE – price to earnings with amortisation
MC/S – market capitalisation to sales
EBIT/EV – operating profit to economic value
P/E – (Price/Earnings) – price divided by annual net profit per share
ROE – (Return on Equity) – annual net profit divided by average equity
P/BV – (Price/Book Value) – price divided by book value per share
Net debt – credits + debt papers + interest bearing loans – cash and cash equivalents
EBITDA margin – EBITDA/Sales

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Strong and weak points of valuation methods used in recommendations:

DCF – acknowledged as the most methodologically correct method of valuation; it is based in discounting financial flows generated by a company; its weak point is the significant susceptibility to a change of forecast assumptions in the model.
Comparative – based on a comparison of valuation multipliers of companies from a given sector; simple in construction, reflects the current state of the market; weak points include substantial variability (fluctuations together with market indices) as well as difficulty in the selection of the group of comparable companies.

Previous ratings issued for Ciech

Rating	Hold	Accumulate	Buy
Date issued	2009-12-03	2010-03-17	2010-06-02
Price on rating day	37.49	33.40	27.00
WIG on rating day	40141.79	41653.11	40931.54