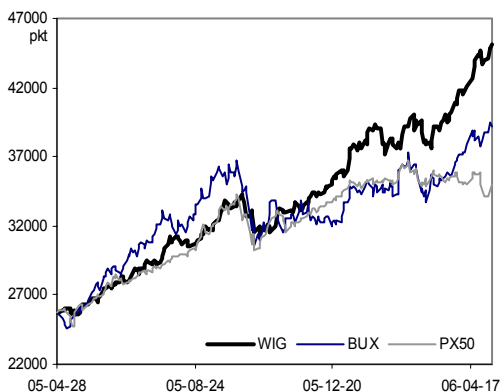


9 May 2006

Periodic Report


**Equity Market**  
**Macroeconomics**

<b>WIG</b>	<b>45 591</b>
Average P/E 2006	17,0
Average P/E 2007	17.5
Avg daily trading volume	PLN 1063m

**WIG vs. indices in the region**

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# Monthly Report

## May

**Equity market**

Profit margins of companies worldwide could be threatened by a slowdown in global growth and a volumes, though the risk is probably greater for companies operating in mature markets. What is more, this would be another anti-inflationary impulse.

**Company News**

**Banks.** The Polish government struck a deal with UCI. The Italian bank was also granted voting rights as shareholder of BPH. We still do not know the legal procedure which will be applied to incorporation into Pekao of 280 BPH branches and sale of the remaining 200 branches and the "BPH" brand name. Several banks have already released their first-quarter results. They show a promise of a good year and further growth in income from core operations.

**Telecommunications.** Anna Streżyńska was nominated Head of the Office for Electronic Communications (UKE), which is in charge of regulating the telecommunications market. The nomination marks the end of a months-long "interregnum" which was a major obstacle on the path to break up the TPSA monopoly. Ms. Streżyńska is an advocate of fast market liberalisation based on the British model, according to which Poland should catch up with the UK in three years' time.

**IT.** Large contracts from the public sector are lurking on the horizon. The Ministry of the Interior and Administration is launching an initiative to computerise all state data registers. ComArch redeemed the last of its convertible bonds. Computerland reported a new contract in the Russian banking sector. The large tender for an eastern border control system is still underway, with Computerland and Emax as bidding rivals. Prokom Software wants to increase its shareholding in Comp, so, it bought extra shares in Safe Computing, while Softbank sold its subsidiary Mediabank to Prokom Investments.

**Construction.** Polimex, in consortium with Austrian Energy & Environment AG, signed a PLN 228.5m agreement for an FGD system with the Rybnik Power Plant. Budimex Dromex signed new contracts with a total value of over PLN 230m. Elektrobudowa raised its 2006 financial forecast and signed a contract with the Państwów Power Plant worth PLN 26.5m. Rafako showed weak first-quarter results. Prochem's sales target for this year is set at over PLN 250m, and net profit target is PLN 10m.

**Pharmaceuticals.** The new list of reimbursable drugs is scheduled for release in June. PGF's Management will recommend dividend payout at PLN 2.40 per share. Bioton will buy a manufacturing plant in India, carry out a stock split, and issue new shares worth up to PLN 340m. Bioton will expand its product offering by an oral diabetes medication.

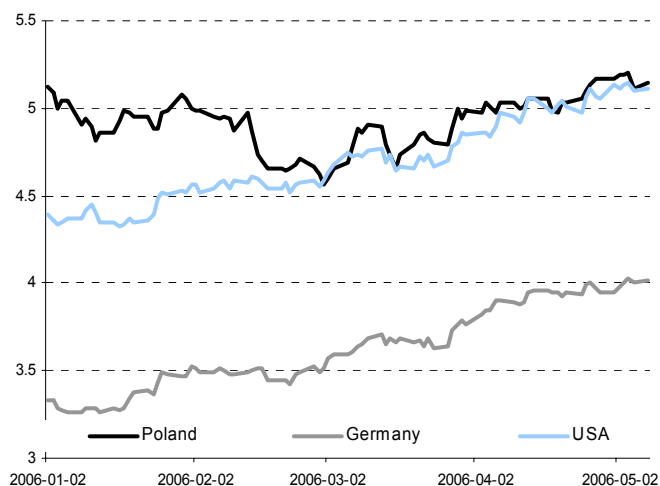
**Gas and Oil.** Fuel companies did not have a good start of the year due to a less favourable market than in 2005, stoppages in gas deliveries, and a harsh winter which affected fuel demand. We expect the second and third quarters to be much better, driven by growing demand and higher margins and oil prices. PKN Orlen's performance should be boosted by the high dividends it is planning to pay out if its Lithuanian acquisition plans fail.

## Equity market

### The risk that is not there

The equity market ignored the hike in market interest rates. Bond yields both in Poland and on mature market increased by ca. 50 basis points in a matter of one and a half months without hurting the stock markets. The expectations of a correction proved futile.

#### Polish, German and U.S. bond yields



If we treat the DCF model simply as a fraction where the numerator are the operating figures of companies (profits, cash flows), and the denominator is the cost of capital (interest rates, risk premium), the market's behaviour will show us that there is more faith in a much stronger positive impact of profit growth than fear of a negative impact of increasing yields. There is good macroeconomic data coming from virtually areas: production, employment, income, inflation. The inflation data is especially important here. Regardless of the reasons of its current low level, the lack of inflation fears offsets the impact of market rate hikes.

In an environment of a strong economic momentum, increasing demand, and rising corporate earnings, the only threat which remains is inflation, which, obviously, is not there. This means that the risk of inflation increase is low, and there is a growing consensus as to its global weakness. As the consensus becomes broader, stock prices continue to rise.

So, the market is waiting to see whether the current corporate news will confirm its expected earnings growth. The P/E ratio is high, reflecting the level of expectations. The quarterly earnings are generally confirming the trend. The fact that investors are betting on good corporate news may at a certain point weaken the market after the wave of quarter earnings news.

Naturally, the key question is still the horizon of the current bull market. Corporate earnings increase on the back of growing sales volumes or prices (in this case mainly materials). Low global inflation could be a cause of concern about margins and profits. But profits are still on the rise, despite a strong upward pressure on costs (materials), hitting record highs both in Europe and the U.S. This is thanks to operating leverage (volumes) and global outsourcing (keeping tabs on costs, no salary pressure). In such an environment, profit margins of companies worldwide could only be threatened by a slowdown in global growth and a volumes, though the risk is probably greater for companies operating in mature markets. What is more, this would be another anti-inflationary impulse.

All in all, we seem to be witnessing a "new deal" in the global economy, which is especially favourable for equity markets. The situation depends on structural changes in India and China, and those two countries seem to be of key importance when forecasting future trends. For now, there are no negative signs in sight. So, waiting for the market to plunge still means waiting for a correction, not merely a trend reversal. And this is how the birth of a correction is delayed. Right now, we can only enjoy a handful of stocks falling on the heels of disappointing earnings.

**Recommendation changes in the last month**

Company	Recommendation	Previous	Target price	Date issued
ABG	Hold		8.70	2006-04-13
BZWBK	Accumulate	Hold	191.30	2006-04-26
KĘTY	Buy	Buy	154.10	2006-04-28
KREDYT BANK	Hold	Accumulate	17.70	2006-05-02
KOGENERACJA	Buy		61.80	2006-04-28
MONDI	Hold	Hold	64.00	2006-05-08
TORFARM	Hold	Accumulate	49.40	2006-04-21

**Recommendation Statistics**

Statistics	All					For issuers to which BRE Bank Securities S.A. has rendered services				
	Sell	Reduce	Hold	Accumulate	Buy	Sell	Reduce	Hold	Accumulate	Buy
number	1	4	14	7	3	1	3	4	3	1
percent	3.4%	13.8%	48.3%	24.1%	10.3%	8.3%	25.0%	33.3%	25.0%	8.3%

# Financial Sector

## Banking Sector

### Consumer loan potential

According to a survey commissioned by the European Credit Research Institute, Poland is among the markets with the largest growth potential in consumer loans alongside the UK, Czech Republic, Portugal, Hungary, Spain and Italy. We are currently one of the fastest-growing markets in Europe. Our ratio of payment cards per citizen is the weakest, at half a card per one Pole (vs. 2.5 per one Brit; and 2 per one Portuguese, Spaniard, Belgian and Norwegian). These results are similar to those regarding the growth potential of the Polish mortgage loan market. In the current macroeconomic climate, Poles are more willing to seek external financing. We agree with the survey outcomes, and think that different types of cash loans and credit card debt will move strongly upwards over the next few years.

### Banking services

According to a survey by Capgemini, prices in the Polish banking sector are on a par with the European and global average. Last year, the price slippage in Poland was much stronger than abroad. Polish prices shed an average 10%, compared to 1.5% worldwide. The downfall was mainly due to the shift toward electronic payment channels, and zloty strengthening against the euro. The survey outcomes are translated to the single currency. The strengthening zloty slightly distorts the survey results. Banking prices in Poland are admittedly high, but we should remember that the availability of banking services in Poland is much lower than in other countries, and that the majority of Poles still do not use electronic and remote (and hence cheaper) banking channels.

*Rzeczpospolita* quotes a CBOS survey indicating that 57% of all Poles have bank accounts. 88% of the respondents are satisfied with their banking service, vs. only 8% disappointed customers. 74% of the respondents think that their savings are safe with banks, 39% find the loan offer attractive, while 37% think that are not satisfied. 51% of the respondents said that small businesses have problems obtaining financing. A whopping 75% of all the survey participants find banking services too expensive.

### 2005 profit distribution

The table below shows proposed or Management-approved dividends of the different banks.

#### Dividends

	stock price (at close 28.04.06)	DPS	gross DY	2005 profit payout rate	GA date	date of record	payout
PKO BP**	38.6	0.8	2.1%	46%	18 Apr 06	10 Jul 06	1 Aug 06
Pekao**	206	7.4	3.6%	80%	4 May 06	19 May 06	2 Jun 06
BPH	792	30	3.8%	84%	6 Jun 06.	23 Jun 06	10 Jul 06
ING BSK**	704	27.5	3.9%	65%	27 Apr 06	18 May 06	5 Jun 06
BZ WBK*	186	6	3.2%	85%	6 Apr 06	21 Apr 06	11 May 06
Bank Handlowy	72	3.6	5.0%	76%	n/a	5 Jul 06	31 Aug 06
Kredyt Bank	17.2	0.22	1.3%	14%	n/a	n/a	n/a
Millennium**	6.9	0.54	7.8%	81%	6 Apr 06	5 Jul 06	19 Jul 06

Source: BRE Bank Securities, banks

\* post-record date

\*\* dividends approved by shareholders

## Mergeocracy

### Arrangements with the KNB

On April 5th, the Commission for Banking Supervision ("KNB") granted UCI voting rights as BPH's shareholder. The clearance was given on the same day that UCI and the Polish government reached an agreement on the Pekao/BPH merger. Later, the KNB released the documents which it had received from UCI when the latter applied for the voting permission. Article 14 of the document (page 10) contains a declaration that the whole of BPH's assets would be transferred to Pekao by the end of 2006 in exchange for shares which Pekao is to issue to BPH's shareholders. According to the document, the transfer of BPH's assets to Pekao will take place by the end of 2006. This is contrary to our information about the deal between the Polish government and UCI, namely that only a part of BPH is to be merged with Pekao. But the Treasury Ministry claims that the two banks will not be merged in whole. The plan is to first sell BPH's branches and brand name. Moreover, the understanding says that the parties have 30 months to complete the procedure.

## Financial Sector

### Polish government's deal with UCI

The Polish government and UCI signed a preliminary agreement regarding the BPH / Pekao merger on April 5th. On April 19th, the final version of the agreement was initialled by both parties. It was not disclosed to the general public, except for a press release which did not contain any details of how the merger of a part of BPH with Pekao is going to proceed, or how the banks will select branches for sale.

According to the official press release, "BPH will comprise 200 branches with capacity to offer the same range of products as they do now. The branches will receive all the necessary facilities and support services (i.e. IT infrastructure, back office systems, and related services) facilitating the operation of a profitable banking business, including trademark rights and the right to use the name "BPH." The release did not say anything about how banking products and services will be assigned to individual branches. UCI will select the 200 branches from among BPH and Pekao's outlets based on their respective "distribution ranges". In our opinion, this means that UCI was given a free hand to choose the most convenient locations. The understanding also confirmed that the employees of both banks will get employment guarantees until March 31st 2008, that 200 BPH branches and the "BPH" brand with the accompanying infrastructure will be sold to an independent third party within the framework of an international competitive and transparent procedure, and that two seats in BPH's Supervisory Board will be reserved for State Treasury delegates. UCI is under the obligation to complete all required procedures within 30 months (2.5 years). The remaining BPH branches (280) will be incorporated into the expanded Pekao network.

According to Vice-Treasury Minister Paweł Szalamacha, the process of selling the 200 BPH outlets and brand name should start in the second half of 2006 and end in 2007.

Because the Treasury Ministry is still standing by the scenario that BPH branches and brand will be sold first, followed by incorporation of the remaining BPH assets into Pekao, it prepared some draft amendments to the banking laws to facilitate such an operation. The draft amendments designed to enable the division of BPH are almost ready. The Treasury Ministry is working on the basis of the Polish Code of Commercial Companies. If the amendments are handled as "urgent" legislation, they can be passed within two months. According to experts, the amended regulations would enable division of BPH, incorporation of some of its outlets into Pekao (280), and sale of the rest of the branches with lower capital. Such an operation would require approval by the KNB, which would condition its decision on stability and cautious approach to managing the bank.

### European Commission

The European Commission received an answer to its March 8th letter to the Polish government. The letter was the Commission's first step toward initiating a procedure against Poland for violating the EU principle of free flow of capital. In the letter, the Commission asked for an explanation of why the government was blocking the merger between Pekao and BPH with disregard to the Commission's earlier clearance and determination that mergers of HVB's and UCI's subsidiaries would not affect competition in any of the EU member states. In its response, Poland reiterated its stance against the merger. The European Commission is still looking into the government's arguments and the deal between Poland and UCI which was supposed to be reported to the Commission after signing.

Vice Minister Paweł Szalamacha met with the Commission's delegates after the deal on the Pekao/BPH merger and sale of the BPH brand name was finally struck. The Commission warned Poland that the fact that a compromise was reached will not mean that it would abandon its action against Poland regarding the merger. The Polish side also did not withdraw the motion it filed with the European Court of Justice to initiate proceedings against the European Commission regarding its assessment of the impact of the HVB-UCI merger on the Polish market.

## Pekao

### Divestment of holdings

The sale of 75% shares of Pekao Development to Pirelli Real Estate for EUR 20m will be booked in the second quarter of 2006. It will not have any major impact on the bank's financials. Having obtained all the requisite permits, the new company launched its operations under the new name of Pirelli Pekao Real Estate.

## Financial Sector

### Bond retirement

Pekao retired 59709 A-series bonds, and changed its bylaws accordingly.

### Xelion

Pekao group's financial intermediary Xelion will reach its profitability threshold in 2008. Last year, the subsidiary reported a net loss of PLN 23.2m. Because Xelion's financial results are a minor contribution to Pekao's consolidated figures, this news will have no impact on Pekao's stock.

## BPH

### Rating

Fitch Ratings affirmed its support rating for BPH at "1". According to Fitch, "the rating is based on the extremely strong potential support available from its controlling shareholder, UniCredito Italiano (UCI) and follows the announcement of an agreement between the Polish government and UCI which will allow the planned merger of BPH and Pekao to proceed". It is now UCI's turn to make a move. The information we have about UCI's deal with the Polish government is still very unspecific, and nothing is decided yet.

### Q1 results

BPH's CEO announced that the bank's first-quarter results will be much better than last year, showing growth by several dozen percent against Q12005 (when the bank earned PLN 205m). That increase will be a result of improving operating income, driven by recurring items. In our forecast, we estimated BPH's Q1 net profit at PLN 284m, and a 38.3% growth. The bank will release its earnings report on May 11th.

## PKO BP

### Acquisitions in Central and Eastern Europe

PKO BP was shortlisted to bid for the twelfth largest bank in Serbia, the Panonska Banka (PB). Other bidders are Alpha Bank (Greece), National Bank of Greece, BA CA, MKB (Hungary), Sanpaolo IMI (Italy). At the end of June 2005, PB had EUR 126.8m in assets and an equity worth EUR 32.5m. PKO BP is also bidding for the Serbian Vojvodjanska Banka, but, according to the press, VB is more likely to be sold to the National Bank of Greece which has offered EUR 500m (compared to preliminary estimates by local analysts of EUR 200m–300m).

PKO BP's CEO also reiterated plans to continue expansion in the Ukraine, where the bank is already present through its subsidiary Kredobank (formerly Kredyt Bank Ukraina).

PKO BP is not going to buy the Croatian Splitska Banka. The deal was awarded to Societe Generale, which offered over EUR 1bn, at 4.7 times the book value. Earlier press reports indicated that SG was willing to pay EUR 750m–800m. Investors who wanted to see PKO BP grow through international acquisitions are likely to be disappointed with this news. We did not take into account the bank's international expansion plans in our valuation model, so, this information has no impact on our valuation.

### Business expansion

PKO BP sold mortgage loans worth PLN 2.1 billion in the first quarter of 2006 (50% more than the year before). The currency breakdown of the mortgage sales has not changed: 40% of the loans are in Polish zlotys, and 60% are in foreign currencies (mainly Swiss francs). PKO BP confirmed its sales target of PLN 9.6 billion in mortgage loans sold by the end of 2006. Loan sales in March amounted to PLN 860m, and the bank is hoping to achieve average monthly sales this year of PLN 800m. PKO BP's CEO said that the merger of BPH and Pekao will create an opportunity to strengthen the bank's positioning in mortgage financing, as the new bank will not sell mortgage loans denominated in foreign currencies.

The CEO also confirmed the goal of gaining a 25% share of the consumer loan market by the end of this year, or at the beginning of the next. PKO BP's sales grow at a rate of 15% year over year, and its market share is 22.3%.

### Q1 financial results

PKO BP's CEO also said that the first-quarter results will be better than last year's (net profit totalled PLN 416m). The bank will release its earnings report on May 12th.

## Financial Sector

### Sale of NPLs

PKO BP will sell another NPL portfolio. As the last time, the buyer is S-Collect. The portfolio is worth PLN 750m.

### Supervisory Board reshuffle

On April 18th, PKO BP's General Assembly decided to make some replacements in the bank's Supervisory Board. The Board was reduced from 9 to 7 members, with five newly appointed members.

## Millennium

### Q12006 results

Millennium posted PLN 69.7m in first-quarter consolidated net profit. This was 30.8% more than our estimated PLN 53m. The following factors contributed to the better-than-expected result: higher fee and commission income (PLN 77.4m, topping our forecast by PLN 7.5m), lower amortisation and depreciation (PLN 16.5m, which is PLN 4.7m lower than our forecast), and lower provisions (PLN -6.7m vs. our estimated PLN -13.8m). The first-quarter results have prompted us to revise our 2006 full-year net profit forecast to PLN 250m. In our opinion, low provisions are non-recurring, the cost of risk should increase later in the year, and lower amortisation and depreciation expense is a temporary effect which will end as the bank opens new outlets. We must give Millennium credit for its fee and commission income figure, which proves its dynamic growth.

### BCP to increase holdings in Millennium

Millennium's strategic investor, the Portuguese BCP, plans to increase its shareholding in Millennium from the current 50% to the 66% cap, and has already filed the relevant application with the supervision bodies. BCP will release more details of the transaction at a later time. A 66-percent holding in a company does not give rise to an obligation to hold a tender offer for its outstanding shares. Aside from BCP with its 50% stake, Millennium's shareholders also include: M+P Holding SA (9.99%), Carothers Trading Limited (9.99%), and PRIORITY Investments Corporation (9.99%). Reports do not specify whether the shareholding will be raised by buying back the stakes of the other investors, or by buying shares on the stock market. We think that BCP will choose the option to buy back shares from the holders of the 9.99%-stakes.

### Rating upgrade

Moody's upgraded its financial strength rating for Millennium from "D- with positive outlook" to "D with stable outlook". It quoted the bank's growing ability to meet its strategic goals, operating profitability, and declining risk profile, as the reasons for the upgrade. As usual, ratings are a reflection of what has already been noticed and factored in the financial results. The bank is improving its operating performance. This year, we expect its recurring net profit growth rate to surge 20%. However, the past improvements, as well as the positive outlook, have already been discounted into the current prices.

### Network expansion

Millennium's first Financial Centre, designed in line with the bank's new business formula, which will serve mass retail customers, Prestige's clientele, and small businesses, will launch its operations in May. Millennium is also planning to open 26 new outlets this year, and redo the 31 existing ones. It will also close down 14 Prestige outlets. The bank's new business formula combines three segments into one. This means that its new outlets will be larger than the 3-4 staff branches it operates now. The formula of the new "Financial Centres" requires 6 to 8 staff on average. Refer to our latest analytical report for more information on Millennium's network expansion plans. This news is inline with our projections.

## Kredyt Bank

### Q1 results – operating income: better but still not great

KB released its first-quarter results, posting PLN 88m in profit, which was 6.4% lower year over year and 2.4% lower quarter on quarter. Operating income increased by 24.5% YoY. The Q1 results show that the bank effectively implements its operating improvement strategy. Revenue from banking operations climbed 3%, falling short of our expectations (we estimated a 10% growth). We were slightly disappointed with KB's top line figure, although we remember that the Q12005 results included one-time items (the largest being PLN 18m earned on securities sale following portfolio reclassifications after transition to IAS reporting). We were positively sur-

## Financial Sector

prised by KB's cost figures. We expected that expenses would grow, driven by new promotion of the new corporate image and network expansion. But the bank showed costs practically flat from Q12005 (PLN 219m in Q12006 vs. PLN 220m in Q12005), proving that it is capable of financing its expansion and self-promotion from its savings (a C/I ratio of 72% still gives plenty of room to enhance performance though cost cuts). To sum up, KB's Q1 results were a disappointment, but they have not prompted us to revise our assessment of the bank's ability to achieve our forecasted net profit figure, and improve income quality.

### Business growth plans

Kredyt Bank's target is to have one million customers by the end of 2006. At the end of 2005, the customer base was 878.4 thousand, recording a rise 6% year on year. Key growth areas were retail customers and small and medium-sized businesses.

KB also wants to have 100,000 of its credit cards in circulation by the end of the year. End of 2005, it had issued 66.3 thousand cards, which was 73% more than in the preceding year. The credit card sales plans do not take into account the card scheme launched by "Żagiel", KB's financial intermediary (by issuing credit cards to Żagiel's clientele, KB wants to reduce customer rotation, which is very high in case of paying agents).

KB reiterated its plans to open 40 new outlets by the end of the year. It is finishing off the last details, working toward launching the new branches on a mass scale starting in May. The bank is currently working on a strategy and locations for the next outlet batch (remember that KB's target is to open 120 outlets by the end of 2008).

KB is planning to sell mortgage loans worth PLN 1.1bn in 2006 (vs. PLN 950m in 2005). FCY loans account for 57% of the bank's total home loan portfolio. 40% of the new sales are PLN loans, the rest are FCY loans.

KB launched a new deposit-and-investment product which it wants to bring PLN 300m in 2006.

KB's CEO did not specify a ROE target, saying only that the bank's priority would be to keep it at over 16%. The bank's Vice President Bohdan Mierzwiński said that net profit this year may be lower than last year's PLN 416m. Operating income, however, should improve.

### Dividend

KB's management wants to pay out PLN 0.22 per share from the 2005 profit as dividends. This means that the payout will amount to PLN 60m (PLN 416.5m), with a payout rate of 14.37%. The bank underwent a turnaround after it had reported losses for several consecutive years. KB's CEO stated that KB will operate in compliance with the policies of its strategic investor, the Belgian KBC. KBC applies a policy of steady dividend growth. News of profit payout right after the end of restructuring was a surprise. Obviously, those are not dividends which could produce a gross yield matching that of other banks'. But it is a sign that the period of internal restructuring, capital rebuilding, and focus on turnaround, has come to an end. The payout is subject to approval by the Commission for Banking Supervision. We do not see any threats to completion of the turnaround, and believe that the bank will obtain the necessary clearance. In May, KB will announce the date of its General Assembly, which will approve the 2005 financial statements and decide on profit distribution.

### Sale of NPLs

On April 14th, Kredyt Bank announced that it is going to sell its own and Żagiel's (its wholly owned subsidiary) non-performing loans. The maximum total value of the NPL portfolio will be PLN 1.045bn. Execution of the disposition agreement is scheduled for the first half of June 2006, so, the gains from the deal should be reflected in Kredyt Bank's financial results in the second quarter. The sale agreement was signed with "BEST I Niestandaryzowany Sekurytyzacyjny Fundusz Inwestycyjny Zamknięty". This means that the bank will recognise one-time items again this year, which will shape the full-year financials. For more information on the impact that the NPL sale will have on Kredyt Bank's financial performance, refer to our analytical research dated May 2nd 2006. Our current forecast assumes a PLN 95m impact on the bank's revenues.

From what we know from KB's representatives, the NPLs for sale will mainly include retail debt (though we would rather have expected Kredyt Bank to sell its corporate loans), the bulk coming from Żagiel. KB reported that, after the sale, the share of NPLs in gross loans will be 20.6% (now at 27.2%), and the ratio of provisions to NPLs will amount to 66%.

## Financial Sector

### ING BSK

#### Franchise-based network

ING BSK launched a trial franchise outlet in Poznań. A further 2–3 outlets will be opened soon. The trial period will last 2-3 months, during which the bank will establish the final franchising procedures. Franchise outlets will not have cash registers, but instead will use ATMs and CDMs. ING BSK's franchising plans have been known for some time. For now, the franchise initiative is only a test whose outcomes will determine the future network expansion. This strategy offers growth potential with respect to product sales going forward, as the franchise outlets will be focused on sales, not transaction services. For more information, refer to our analytical research on ING BSK of February 1st.

#### Supervisory Board reshuffle

ING BSK's General Assembly (April 27th) appointed four new members of the Supervisory Board following resignations by four former members. The new Board members are: Ralph Hamers, Jerzy Hausner, Mirosław Kośmider, Wojciech Popiołek. The purpose of the reshuffle was to ensure compliance with good public company practices (which was the official reason for two resignations) which provide that the maximum term of office for supervisory board members should be no more than 12 years.

#### Other

Handlowy-Heller changed its name to ING Commercial Finance. Holland's ING Commercial Finance acquired Handlowy Heller at the beginning of the year. As a result, ING CF signed an agreement with ING BSK for cooperation in providing factoring services.

### BZ WBK

#### Q1 results

BZ WBK earned PLN 175m in the first quarter of the year, recording a 47% year over year increase. The net profit figure is much above our estimates, which proved rather conservative even with an over-20% improvement projection. Such booming results were achieved thanks to better recurring profits (revenue from banking operations increased 24.2%, including gains from the sale of LZPS Protektor equal to PLN 7.8m). The BZ WBK group's investment banking division was the top performer, contributing a lion's share to the bank's excellent results. We also appreciate the bank's cost monitoring policy. Costs increased by 6% YoY, driven mainly by personnel costs (+15.5% YoY), while YoY amortisation and depreciation fell 3.5%, and administrative expenses shed 1.6%. Growth at such a high rate cannot be achieved without a cost inflation, and maintenance of highly skilled staff is a good investment in the current market. We have also noticed a major change in loan volumes from what we had observed still in mid-2005. The loan portfolio's growth rate might not be very impressive just yet (4.8% YoY, 2.4% QoQ), but we should remember that, last year, the portfolio was on the decline. Private loans rose 20%, and corporate loans gained 3%. BZ WBK is still reporting high cash loan sales (PLN 686m at the end of March 2006, 114% growth YoY). Aside from the excellent first-quarter results, BZ WBK also revealed its network expansion plans. It wants to add a further forty-something outlets to its current network, located mainly in large cities. Exact locations are still being determined. There was also talk of launching a new business, which would operate via franchise outlets, offering basic banking products such as cash loans. But that initiative is still in its concept phase. BZ WBK may once again pay out over 90% of its net profit generated in 2006. The bank's CEO said that such profit distribution is very likely. The aim is to achieve a capital adequacy ratio of 12%, now at 16%. What we learned from BZ WBK's Management prompted us to revise our earnings forecast for the bank. The PLN 1bn in gross profit announced by BZ WBK's CEO seems very much feasible.

### Getin Holding

#### Further growth founded on WBC

WBC entered the next stage of the business plan it presented to the KNB when it was being taken over by Getin Holding. It will establish an Investment Fund Company (TFI). Launch of the TFI is set at September 2006. It will offer services complementary to WBC's current operations. That WBC, soon to be turned into "Noble Bank" offering financial advisory to wealthy clients would include investment funds in its offering, could be expected. To date, Open Finance, the Getin group's financial intermediary serving mass customers, offered units of other funds. Aside from its own range of services, WBC will also act as agent selling the products of other banks.

## Financial Sector

Noble Bank, Getin Holding's new financial intermediary, will open its first outlet on May 20th. Noble Bank outlets are expected to become profitable in net terms after six months from launch. NB will act as financial agent for wealthy retail customers. The bank is also planning to launch its own investment fund in September. It is going to open a total of 20 branches within the next three years.

### **Factoring expansion**

Factor In Bank, the factoring arm of Getin Holding, bought debt worth PLN 72m in the first quarter of 2006 (10% more than in the last quarter of 2005), and acquired 70 factoring clients and 600 contracting partners. Factor In Bank has purchased debt worth a total of PLN 185m since launch.

### **Fiolet's sales performance**

Getin Holding's financial intermediary Fiolet sold 2.7 thousand loans worth PLN 106m in the first quarter of 2006, a staggering 489% more than the year before. Still, that amount is equal to just 17% of this year's target of PLN 622m in sales. First-quarter sales usually account for less than 25% of the full-year sales. We think that Fiolet has a very good chance to achieve its sales target set for this year.

### **Debt issue scheme**

Getin Bank, a subsidiary of Getin Holding, acquired 49998 shares of Getin Finance Plc at GBP 1 each. Getin Finance Plc's share capital is GBP 50000. It is a special-purpose vehicle which Getin will use to launch a debt issue scheme on international markets.

Getin Finance Plc issued 150,000 bonds worth EUR 150m (PLN 584.115m). The bonds were floated on the London Stock Exchange. The entire issue scheme will comprise bonds worth EUR 1bn, most of which will be allocated to finance Getin Bank's lending business.

## IT Sector

### IT

#### **Big deals a-coming**

The National Bank of Poland (NBP) is going to allocate ca. PLN 200m toward construction of a new vault and computer centre in Zegrze. The IT-related part of the work will include a server room and security systems (including break-in signalling systems, access control, CCTV). NBP did not specify the size of the IT allotment. Potential candidates with relevant experience to carry out the project include: ABG Ster-Projekt, Qumak-Sekom and Computerland which already has NBP as its key account.

BGŻ wants to allocate ca. PLN 64m to IT projects. Contracts under those projects will most probably be awarded to several IT companies. BGŻ has been working with many IT companies in its past projects, including Softbank, Asseco and ABG Ster-Projekt.

Poland's General Police Headquarters announced a tender for upgrade of the Police Information System by adding a data warehouse. The net contract value is PLN 11m. Submissions will be accepted until May 15th. At the beginning of January, the Police HQ released a tender schedule for 2006, providing that investments in IT and telecommunications this year may reach PLN 200m. Last year's contract winners included Prokom Software, Comp, Emax, ABG Ster-Projekt, and Computerland.

The Finance Ministry is planning to spend ca. PLN 300m this year. A large portion of this allocation will go to IT companies. The largest tenders will be for software and hardware (incl. a central database, the "e-podatki" electronic tax return system, etc.). One of the beneficiaries of the Ministry's IT budget could be Comarch, which won a tender for a State budget management system in 2004. Allocations to this purpose will amount to PLN 25m this year. The Ministry also wants to spend ca. PLN 1.3m on an IT outsourcing analysis, which may be an indication of its IT outsourcing plans.

#### **KGHM holds SCM project**

KGHM held its IT project for supply chain management system worth ca. PLN 100m. The short list of bidders included Prokom (jointly with IBM and SAP as subcontractors), Computerland, and HP. KGHM did not explain why it was holding the project. According to the company, its investment practices have become subject to audits. The bidders stressed that the solutions they put forth in their offers were successfully implemented at companies with similar business profiles as KGHM. If KGHM decides to resume the tender, the short list will probably be composed of the same companies. This is bad news both for Prokom and for Computerland. Prokom was considered the favourite, but some of the solutions were going to be contracted to the other bidders. The decision to hold the project was probably a result of the recent management reshuffle at KGHM. We are not able to tell at the moment when the tender will be resumed.

#### **Interior Ministry to computerise data registers**

The Ministry of the Interior and Administration (MSWiA) is expected to hold a tender for computerization of State registers (including an upgrade of the PESEL database and a register of official IDs). The project budget is over PLN 200m including 75% in EU financing. The budget allocations to this purpose have to be expended by the end of 2007 (with an option to extend the deadline to the end of Q108). The Ministry decided after consultations that the PESEL 2 project will be divided into parts and contracted to several providers. The Ministry will act as project integrator. The first in a series of contract tenders will be held in July. This will be the first project carried out on such a large scale in the public sector. To date, all large contracts were carried out by one provider. This is good news for small companies which would otherwise not stand a chance of taking part in such a large project.

## ComArch

#### **ComArch' annual report**

Comarch released its standalone FY2005 financial statements showing the same financial figures for the parent as disclosed in the Q405 report. An analysis of the results of subsidiaries, however, leads to some interesting conclusions. The highest profit figures were reported by Interia.pl (PLN 39.7m in sales, PLN 2.2m in net profit) and NetBrokers (sales at PLN 41.1m, net profit at PLN 1m). The least profitable subsidiaries are Comarch Global, Inc. (USA) with sales at PLN 9.4m and a net loss of PLN 3.5m, Comarch Software AG (Germany) with sales at PLN 10.7m and a net loss of PLN 0.7m, and Comarch Panama, reporting sales at PLN 1.5m

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and a net loss of PLN 0.6m. Combined, the subsidiaries reported a total net loss of approximately PLN 2 million, which is an improvement from the preceding year (net loss at ca. PLN 6m). Interia was the main driving force of the improvement, turning its net loss of PLN 3 million recorded in 2004 to a net profit of PLN 2 million in 2005.

### Retirement of convertible bonds

Following early redemption of convertible bonds, Comarch notified redemption and retirement of 293 CVs. Those were the last of Comarch's CVs outstanding. Earlier this quarter, the bond holders converted over 3.2 thousand bonds to over 560,000 Comarch shares.

### New contracts

Comarch's new contracts include:

A contract for data warehouse implementation at TUIR Warta with an undisclosed value.

A contract with the University of Gdańsk for development, implementation and maintenance of an integrated management support system, worth PLN 2.8m.

A deal with Polkomtel S.A. for the inter-operator billing system "Comarch InterPartner Billing". Comarch InterPartner Billing will be used to settle inter-operator payments and as support for settlements with MVNOs, Service Providers and ESPs working with Polkomtel. The contract value is PLN 12.4m. Deadline is set at May 2007.

## Computerland

### Computerland's annual report

Computerland released its FY2005 report, showing PLN 858.1m in sales, an EBIT of PLN 34.1m, and a net profit of PLN 11.4m. Compared to the figures disclosed in the Q405 report, the differences are minor: PLN 858.6m in revenues, an EBIT of PLN 33.8m, and net profit at PLN 11.4m.

### Insider deals

On March 31st, a buyer closely affiliated with a member of the Issuer's governing bodies bought 7,000 shares of ComputerLand S.A. at PLN 99.89 per share.

On April 5th, a seller closely affiliated with a member of the Issuer's governing bodies sold 10,000 shares of ComputerLand S.A. at PLN 105.01 per share.

On May 2nd, a buyer closely affiliated with a member of the Issuer's governing bodies bought 9,000 shares of ComputerLand S.A. at PLN 103.43 per share.

### New contracts

Computerland's Russian subsidiary CSBI won a contract for implementation of the retail modules of its proprietary software "Bankier" at the Russian Mosstrojekonombank. The value of the contract was not disclosed. This is CSBI's first contract with a Russian bank in a long time. Computerland is still taking part in a dozen or so tenders in the Russian banking sector. The latest Russian contract was awarded to another of Computerland's subsidiaries, Support (delivery of the proprietary Carusso Pension system for US \$1.2m).

Computerland will implement an ERP system at Bank Pocztowy. The deadline is set at the end of November. The same system is already operating, among others, at BGŻ, PKO BP, BPH, Kredyt Bank and BZ WBK. The value of the contract was not disclosed.

Computerland signed a service agreement with the National Health Fund (NFZ) covering a system which supports NFZ's operations at the HQ and 8 regional branches. The agreement is valid through this year. Its gross value is PLN 13.4m.

Computerland signed a two-year agreement with Rabobank Polska for Disaster Recovery Center service, to ensure business continuity in case of a disaster or system failure. The service will include movement of the bank's servers to Computerland's special hosting centres. The value of the contract was not disclosed.

### Trouble on the eastern border?

According to Polska Izba Informatyki i Telekomunikacji (PIIT), the requirements set out by the

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Polish Border Guard Services regarding a land border control system, are much too demanding. This means that the deadlines set for the EUR 52.5m border control system project will most likely not be kept. The project deadline is scheduled at Autumn 2007, but offerors say that, with the budget that the Border Guard Services allocated to that purpose, it will take at least two years to carry out. In addition, *Puls Biznesu* reports that the project is becoming less and less popular among the Border Guard officials themselves, who are considering a "safer" way to spend the EU subsidies. This is bad news for companies who are bidding for the contract. Excessive project demands pose a threat to the deadlines, possibly entailing penalties for the successful contractor. Suggestions that the project might be called off altogether will also weigh on those companies.

## Emax

### Board member divests

On March 29th, a member of Emax's Management Board sold 3,625 Emax shares (issued under a Management Stock Option Plan) at PLN 119.5 per share. On the same day, an Emax employee sold 900 shares at the same price.

### New contracts

Emax's subsidiary Winuel signed two contracts: one with Enion SA for delivery of a local energy market operator support system worth PLN 0.76m, and one with Dolnośląska Spółka Gazownicza for delivery of IT solutions worth PLN 0.82m.

A consortium of Winuel S.A. (a subsidiary of Emax), Consortia Sp. z o.o. and Zakład Elektronicznej Techniki Obliczeniowej Sp. z o.o. signed an agreement with the Regional Police Headquarters in Katowice for delivery of a complete system, including software, for fax traffic and electronic mail management. The rollout will cover 120 locations, scheduled for completion by July 2006. The net value of the agreement is PLN 4m.

## Prokom

### Dividends

Prokom Software's CEO announced that the company and its subsidiaries will pay out 30% of their respective last year's profits as dividends. This means that Prokom Software's shareholders will receive a total of PLN 20m, i.e. PLN 1.5 per share.

### Pioneer Pekao IM and PZU AM reduce holdings in PS

Pioneer Pekao Investment Management reduced its interest in Prokom from 5.29% (5.02% of total votes) to 5.23% (4.96% of votes). PP IM now holds 726,400 shares in Prokom Software.

PZU Asset Management S.A. reported sale of 30 thousand Prokom Software shares from the investment portfolios of PZU AM SA clients, which means that its share of GA votes fell below 5 percent. Before the sale, the securities portfolios managed by PZU AM SA comprised a total of 731,769 shares which accounted for 5.27% of equity and carried 5.0% of votes.

### Acquisition of Safe Computing

Prokom Software reported that, on Friday, April 21st, it acquired 1,910 shares in Safe Computing Sp. z o.o. from NET Technology S.A., accounting for 39.00% of share capital and votes, for a total of PLN 12.48m. As a result, Prokom now holds 4,408 shares in Safe Computing, representing 90.00% of the company's share capital and votes. The purchase is a step toward increasing shareholding in Comp. Prokom holds an option to purchase a 20% stake from Comp's CEO, which, if exercised, would lead Prokom to exceed the 33% shareholding threshold which necessitates another tender offer, driving Prokom's expenses to ca. PLN 100 million. Instead of holding a tender offer, Prokom could make a non-cash contribution to Comp (e.g. of Safe Computing shares) in exchange for new shares. The recent increase by Prokom of its shareholding in Safe Computing indicates that the company might have chosen the latter option. We are expecting a final decision in that matter by the end of May.

Comp's CEO Jacek Papaj stated that the way Prokom Software increased its shareholding (to 90%) in Safe Computing indicates that an in-kind contribution of Safe Computing's shares in exchange of new-issuance shares is a more probable scenario for increasing shareholding in Comp than exercise of his 20% stock option. The CEO said that Safe Computing can turn out to be an interesting investment. Comp has not received any specific proposal from Prokom

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Software yet, but Mr. Papaj says that there is a good chance that an agreement will be signed by the end of this quarter. This information confirms our conclusion that Prokom is more likely to contribute Safe Computing in kind to Comp than make the capital-intensive move of exercising a stock option.

### The "academic" contract

A consortium of Prokom Software, SAP and Siemens won a contract for computerisation of four colleges. The consortium offered PLN 66m. The project is scheduled to take five years, followed by 10 years of systems maintenance work.

### More PS in Softbank

On April 26th, Prokom Software purchased 315,000 shares of Softbank SA, increasing its stake from 33.01% to 34.26%. The value of the stake is approximately PLN 12m, i.e. some PLN 38.6 per share.

### Annual statements

Prokom Software released its FY 2005 report, showing PLN 1.854bn in sales, an EBIT of PLN 151m, and a net profit of PLN 80.3m. Compared to the figures disclosed in the Q405 report, revenues are slightly higher (vs. PLN 1.843bn), EBIT is lower (vs. PLN 162.8m), as is net profit (vs. PLN 82.6m).

### Sale of ABG Ster-Projekt's HQ delayed

ABG Ster-Projekt reported that not all of the conditions precedent of a preliminary property sale agreement had been met by 31st March 2006, and, consequently, execution of that agreement was moved forward by three months, to June 30th 2006. Pursuant to the conditional preliminary agreement, RONSON DEVELOPMENT 2000 Sp. z o.o. will purchase the property, located at ul. Magazynowa in Warsaw, for PLN 21m. Investors have been aware of the plans to sell the HQ building for some time. The deal will probably be finalised in the third quarter of this year.

### ABG Ster-Projekt's large deal with MEN

A consortium of Bull Polska and ABG Ster-Projekt signed a contract with the Ministry of Education for delivery of computers to school labs. The contract value is PLN 58m. We reported the contract award to the consortium in mid-December of last year, however, the contract signing was delayed by three months.

### ABG Ster-Projekt's annual report

ABG Ster-Projekt released its FY2005 pro-forma report, showing PLN 407.3m in consolidated sales, an EBIT of PLN 14.5m, and a net profit of PLN 22.8m. Compared to the pro-forma figures disclosed in the Q405 report, revenues are slightly higher (vs. PLN 404m), EBIT is lower (vs. PLN 26.3m), as is net profit (vs. PLN 28m). The financial results were affected by recognition of a provision against VAT on licence sales generated in 2001 (PLN 6.2m), originally derecognised in the fourth quarter of last year.

### Comp's standalone annual report

Comp's FY2005 standalone report shows revenues of PLN 83.5m, EBIT at PLN 8m, and a net profit of PLN 7.1m. The full-year figures are lower than presented in the Q4'05 report (showing PLN 84.6m in revenues, PLN 8.7m in EBIT, and PLN 8.6m in net profit). In addition to the PLN 1m-lower revenues, the main difference between the full-year figures and the quarterly estimates are the much higher financing costs (PLN 2.7m vs. PLN 1.3m disclosed in the Q405 report). This is an effect of disclosure in the full-year report of a revaluation expense (PLN 1.4m) on Comp's shares in Radcomp SA. The expense will have no impact on the consolidated figures (it will be excluded in consolidation adjustments). Last year, Radcom posted PLN 4.5m in revenues and PLN 92,000 in net profit. Comp holds a 66.9% stake (78.5% of votes) in Radcomp SA.

### Spin's annual report

Spin released its consolidated FY2005 report, showing PLN 181.5m in sales, an EBIT of PLN 13.5m, and a net profit of PLN 9m. The full-year figures are slightly better than reported in the Q405 report (PLN 179.9m, PLN 13m, PLN 8.5m respectively), and should have no impact on Spin's stock performance.

Spin signed a PLN 14m contract with the National Health Fund (NFZ). Spin operates its proprietary system at 8 NFZ branches, in consortium with Kamsoft. NFZ awards service contracts each year.

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### Softbank

#### Mediabank sold

On April 28th, Softbank sold 100% of its interest in the subsidiary AWiM Mediabank S.A., owner of the PiN 102 FM radio station, to Prokom Investments S.A. The selling price was PLN 4.5m. The current book value of the AWiM Mediabank S.A. shares as disclosed in Softbank's account is also PLN 4.5m, which means that the sale will not have any impact on the company's financial performance. The sale agreement will enter into force after authorisation by the Office for Competition and Consumer Protection (UOKiK) and the National Broadcasting Council. Softbank S.A. will receive the payment in cash within 21 days of the authorisation. In an independent valuation report, KPMG Corporate Finance estimated that the fair market value of all the AWiM Mediabank S.A. shares as of December 31st, 2005, ranges between PLN 3.9m and PLN 5.1m. Despite continuing improvement, Mediabank consistently posted losses (PLN 2.6m in 2005, PLN 4.2m the year before), which means that the sale was a good move.

#### Softbank's annual report

Softbank released its FY2005 financial statements. Consolidated sales amounted to PLN 539m, EBIT stood at PLN 49.5m, and profit netted PLN 42m. Compared to the figures disclosed in Softbank's Q405 report, the full-year results are slightly higher in sales terms (PLN 537m end-Q405), but lower in EBIT and net profit terms (PLN 52.3m and PLN 44.7m end-Q405 respectively). Net profit was affected by higher cost of sales, a lower balance on other operating activity, and higher tax charges.

#### Asseco Poland broadens partnership with Dominet Bank

Asseco Poland signed a contract with Dominet Bank for an upgrade of its proprietary "defBank Pro" system implemented at the bank in 2003. The value of the contract was not disclosed. The project deadline is set for October 2006. Proprietary software implementation and upgrades are a high margin-earning business with significant impact on performance, even with small contract values.

#### Dividends: Softbank...

Softbank's management will recommend payout of 30% of last year's net profit to shareholders. This means that shareholders will receive a total of PLN 16.1m, i.e. PLN 0.64 per share.

#### ...Asseco Poland...

Asseco Poland will distribute 31% of its 2005 net profit as dividends. Shareholders will receive a total of PLN 7m, i.e. PLN 1.82 per share. The date of record is set at April 8th, with payout on May 16th.

#### ...and Softlab

Asseco Poland's subsidiary Softlab will distribute a portion of its 2005 profit to shareholders with some PLN 1m going to the parent.

## Media

### Agora

#### **Acquisitions and dividends**

Agora announced that it would modify its strategy, especially regarding acquisitions. In an interview for *Parkiet*, Wanda Rapaczyńska suggested that Agora would be looking for investment opportunities not only in Poland, but also in the CEE region and Western Europe. Furthermore, Agora now allows for the possibility of taking over minority holdings in the companies it takes over. Before, full control was the preferred solution. The new approach can open a door for Agora to start talking with national radio stations (such as RMF and Radio Zet) and TV stations (TVN or Polsat) and forge closer partnerships and equity affiliations.

Agora's CEO denied a comment regarding dividends and buy-back. The Supervisory Board will discuss profit distribution on May 25th. Agora's dividend strategy announced a year ago provides for payouts at PLN 0.50 per share each year, and distribution of all cash surplus (PLN 120m toward buy-back in 2005).

#### **Gazeta Wyborcza price slash**

Agora decided to lower the price of the daily issues of *Gazeta Wyborcza* ("GW") from an average PLN 2.2 to PLN 1.5 in response to launch by Axel Springer of a new nationwide daily on April 18th. The price reduction will considerably affect GW's sales income (by some 30%) which stood at PLN 189m in 2005. On the other hand, a lower price is a good defence against the new player, potentially boosting the number of GW copies sold. If, however, there is a downturn, it will be less consequential than if the price were to remain the same and Agora relied only on qualitative competition. What is more, there is a chance that lower prices will encourage new readers who, to date, were discouraged by high prices. Agora did not state whether it is also going to change GW's content.

#### **Dziennik's success**

According to Axel Springer, daily average sales of *Dziennik* in its first week since launch hit 317,000 copies. 380,000-400,000 copies of *Dziennik* were sold on the first day, falling to 290,000-310,000 toward the end of the first week. If sales stay on the same level in a long term (2007/08), *Dziennik* can gain a ca. 20% share of the newspaper advertising market (ca. PLN 200m of a total PLN 1.05bn). It is difficult to predict just yet to what extent the launch of the new daily will increase press advertising expenses, and how much of the advertising budgets will shift from title to title.

## Telecommunications

### UKE's new boss

Anna Streżyńska was appointed President of the Office for Electronic Communications (UKE) which is in charge of regulating the telecommunications market. The nomination marks the end of a months-long "interregnum" which was a major obstacle on the path to break up the TPSA monopoly.

Ms. Streżyńska is an advocate of fast market liberalisation based on the British model, according to which Poland should catch up with the UK in three years' time. Her candidacy was pushed by the government even though she had not been put on the short list of top candidates, showing the administration's determination to change Poland's telecommunications landscape. Several major laws, which are already in the making, and which will redefine the telecom market, should soon see the light of day. The regulations will include bitstream access (wholesale access to the Internet, the first step toward local loop unbundling), framework agreement, mobile interconnection (we discussed those problems at length in our December 2005 report). All those solutions will weaken the market position of TPSA. We believe that the market liberalisation processes will not have much bearing in Netia's case, as a number of new strong foreign players will emerge on our market.

### Polkomtel

On May 10th, Polkomtel's shareholders will vote on 2005 profit distribution and changes in the company's management. According to TDC, one of Polkomtel's owners, it has already been decided that the company will pay out the whole of its 2005 profit and retained earnings, making for a total of PLN 2.4 billion. However, this was not confirmed by Polkomtel's shareholders. If the profit distribution reports prove true, KGHM and PKN Orlen will get PLN 470m in dividends from Polkomtel each, which would be reflected in their respective second-quarter statements.

## TPSA

### 1st quarter results

TPSA's first-quarter performance is a bit disappointing in terms of EBIT and net profit (22% below consensus). But we would like to point out the excellent operating profit figure posted for the fixed-line business (EBITDA margin at 52%). This time, Centertel (reporting an EBIT fall from PLN 351m to PLN 232m) was at fault for the deterioration in TPSA's consolidated EBITDA (PLN 2.0bn vs. PLN 2.1bn; margin at 44% vs. 47% the year before). We are positively surprised by the consolidated revenue figure, reported 2.7% higher against the first quarter of 2005. It was driven both by a weaker-than-expected decline in fixed-line revenues (-5%), and a strong revenue growth posted by Centertel (+20%). TPSA stepped up its investments (+30%, mainly in fixed line telephony), which, combined with a higher EBITDA, only contributed to a PLN 385m reduction in net debt, and which investors are not likely to be very happy about. Based on still-incomplete information coming from TPSA, we give a neutral rating to its financial results.

### Centertel posts weaker EBIT

The increase in Centertel's costs and a disappointing operating performance (operating margin fell from 24% to 14%) were due mainly to two factors:

- Interconnect costs (+PLN 123m). Centertel recorded an unfavourable imbalance with respect to its outgoing traffic to other operators and incoming traffic. The company intends to offset that imbalance by introducing more special offers on internal network traffic, which should at least slow down the growth rate of the related costs in the second quarter.
- Costs of subscriber acquisition and retention (+PLN 130m). In our opinion, the increase in customer acquisition and retention costs is largely an effect of introduction of mobile number portability, necessitating stepped-up expenditure on subscriber retention. We expect those costs to continue to climb going forward.

Note also that Centertel has only recently started to pay a fee to FT equal to 1.6% of its revenue (an extra PLN 25m in costs).

### Cash flow

Operating cash flow was similar to the level reported after Q12005 (PLN 1.72bn, down 4%). Investments were stepped up in line with the management's expectations (PLN 553m vs. PLN 421m). TPSA reduced its debt by PLN 1.1bn, mainly by trimming its cash. Net debt decreased by PLN 385m.

### New reporting standards

Unfortunately, TPSA changed its quarterly reporting format (to comply with FT's standards). The quarter report lacks a detailed breakdown of costs and revenues (including subscriber

## Telecommunications

data), rendering an assessment of the cost and income items impossible.

### **New call plans**

TPSA is going to introduce new subscription packages designed to increase the fixed-line traffic and reduce the negative impact of traffic migration from landline to mobile networks. One obstacle to the new call plan campaign is the vacancy in the position of Head of the Office for Electronic Communications (UKE) who is responsible for approving call fees. The election process is very slow. The choice has been narrowed down to three candidates. We will not see a resolution until May, which means that TPSA will be able to market the new call plans some time around June.

## Netia

### **P4 delayed**

Netia believes that P4 can launch its commercial operations still this year. One problem which is yet to be resolved are the locations of transmitter masts. Another concern is the key issue of internal roaming without which the operator cannot exist. After the first quarter of 2006, mobile telephony penetration already stood at 80.5%, which means that Netia will have to steal customers from other operators rather than look for new market areas to occupy (niches). This is bound to be an expensive undertaking.

### **Acquisitions**

Netia wants to take over a small telecom operator ProFuturo from NFI Jupiter. It has bid PLN 75m-80m for the company's shares and debt. We do not know the specifics. ProFuturo specialises in access services and VoIP. Its sales in 2004 amounted to PLN 50.5m. ProFuturo posts large operating and net losses. ProFuturo's book value as disclosed in Jupiter's assets is PLN 23.5m.

## Construction

### Construction

#### Investments in rail infrastructure

Polish Railways (PKP) released a list of the rail routes which it wants to modernise between 2007 and 2013. Total appropriations toward that purpose will amount to EUR 8.4bn, including EUR 6.7bn in EU subsidies. The list was submitted for approval by the Ministry of Transport and Construction. The investment plans include construction of a fast railway route from Wrocław to Warsaw. The public construction companies Polimex Mostostal and Budimex reported that they were interested in acquiring a rail construction company to enter on the promising rail market.

### Polimex Mostostal

#### FGD deal

Polimex, in consortium with Austrian Energy & Environment AG (the leader), signed a contract for wet flue gas desulphurisation facilities with the Rybnik Power Plant. The total contract value is PLN 228.5m, with Polimex's share of PLN 119m. This news is a follow-up to the February reports.

### Budimex

#### Bypass around the Upper Silesian Conurbation

Budimex Dromex signed a contract with the Bytom district authorities, covering the second stage of construction of a bypass around Poland's Upper Silesian (Górny Śląsk) conurbation. The contract value is PLN 61m. The construction is scheduled for completion by the end of June 2008. We expect the road construction contracts to bring high margins.

#### Conditional residential/office building deal

Budimex Dromex signed a conditional agreement for detailed designs and construction of a building shell of an apartment-and-office building with commercial space under the name of "Atelier Residence". The contract value is PLN 85.7m, with a 20-month deadline. Its entry into force is conditioned on the outcome of the investor's financing negotiations. It should take place within six months from the contract date. This is a considerable contract from the general construction segment. It should earn Budimex a higher margin than road construction contracts.

#### PLN 91.2m-worth of deals

Budimex reported that its subsidiary Budimex Dromex signed a contract with PPUP "Poczta Polska" for construction of a Dispatch Centre in Wrocław. The contract value is just under PLN 70m. Deadline is May 2007. *Parkiet* reports that a consortium of Budimex Dromex (the leader) and Ferroviaria won a PLN 21.2m contract for a sports hall for the Agricultural University of Lublin. The consortium's share of the construction work is 70%. Budimex's new contracts in the public building segment have so far amounted to PLN 91.2m. This segment brings higher margins than road construction.

### Elektrobudowa

#### Forecast raise

Elektrobudowa revealed the specifics of its 2006 budget allocations. Sales are projected at PLN 382.9m, and net profit attributable to majority shareholders is estimated at PLN 10.1m. Those targets are higher than those presented by Elektrobudowa in December 2005 (PLN 362.6m and PLN 9.3m respectively). They may be exceeded, propelled by a thriving construction market.

#### Pątnów contract

Elektrobudowa signed a contract with Rafako for comprehensive upgrading of a power evacuation facility for units 3 and 4, and an FGD plant for units 1 to 4 at the Pątnów I Power Plant. The contract value is PLN 26.5m. The work is scheduled for completion by the end of 2007. Power generation is one of Elektrobudowa's key business segments. The deadlock in that segment in the past few years made the company increase its involvement in industrial engineering. The expected rebound in the energy engineering segment, evidenced by the projects ordered by the Łagisza and Bełchatów power plants, should boost Elektrobudowa's financial performance.

# Construction

## Rafako

### Liquidation of subsidiary

Rafako's subsidiary ECO was struck from the National Court Register of businesses. Rafako had announced its plans to liquidate the company some time ago, so, it will have no impact on the company's financial performance.

### PLN 7.8m contract for PEC Gliwice, acquisitions

According to *Parkiet*, Rafako won a contract for boiler upgrade and electrostatic precipitator delivery worth over PLN 7.8m from Przedsiębiorstwo Energetyki Ciepłej of Gliwice. Rafako is also expecting to be awarded FGD contracts by the Łódź CHP (over PLN 30m) and the Skawina Power Plant (PLN 90m). In anticipation of the expected investment rally in the energy sector, Rafako is going to issue shares and take over selected industry players. The aim of the acquisition is to expand the manufacturing technologies (supercritical boilers) and gain access to new markets. One potential acquiree is the German Alstom Power Boiler (with revenues close to PLN 600m). The improvement in the Rafako's financial performance is already discounted in its current market price, which is a resultant of the sector rally and emerging contract news. Due to postponement of the Bełchatów project, a portion of the project revenues will be carried forward to subsequent years, which may affect the 2006 results.

### More business for Rafako

Rafako signed a further two contracts. The first EUR 12m-deal was signed with Hitachi Power Europe GmbH, and is for manufacture of the pressure component of a supercritical boiler system for a 670MW unit at Germany's Boxberg Power Plant. The contract also provides for an option of additional non-pressure-part deliveries and engineering work, which increases its value. The second contract (PLN 22.5m) is with Karrena sp. z o.o. for design and construction of two reinforced concrete stacks for units 1 to 4 at the Pałnów I Power Plant. The deadline is May 2007. The combined value of the two contracts is almost PLN 70m, with an option to earn extra profit by performing extra work.

### Q106 performance

(PLN m)	Q12006	Q12005	change	2006	2005
revenue	120.3	105.3	14.3%	881.2	503.0
EBITDA	2.6	8.3	-68.2%	32.6	24.5
margin	2.2%	7.9%	-	3.7%	4.9%
EBIT	0.1	5.0	-98.1%	19.4	14.4
gross profit	0.8	4.0	-80.5%	16.7	7.4
net profit	0.5	2.6	-82.6%	12.4	5.2

Source: Rafako, BRE Bank Securities

Rafako's financial results posted after the first quarter of 2006 were much weaker than the year before. EBIT and net profit were also much below our cautious estimates. Even though revenues increased to PLN 120.3m (+14.3% YoY), low profitability led to a significant decrease in EBIT (-98.1% YoY) and net profit (-82.6% YoY). The first-quarter performance was affected by adverse weather conditions and the fact that the company did not carry out the most profitable pressure contracts (boilers). We expect Rafako to improve its financial figures in the next quarters. However, as work in Bełchatów has been postponed, we are considering a revision of our full-year profit forecast for Rafako. The Bełchatów contract was postponed to the following quarters, which means that the gains will be posted at a later period.

## Prochem

### 2006 earnings forecast

Prochem published its financial forecast for 2006. Sales target is set at over PLN 250m, and net profit target is PLN 10m. Prochem's management is going to recommend payout of PLN 5.46m from the net profit as dividends (PLN 1.4 per share). The management's forecast is in line with earlier recurring profit projections of PLN 8m-10m. Prochem is only going to distribute a portion of its 2005 profit to shareholders, because the balance will be allocated to finance a new real estate development project. In light of the expected boom in the construction market, the management's net profit target seems overly cautious.

## Construction

### Energomontaż Północ

#### Norwegian deal

EP signed an assembly contract as part of a gas refining and distribution terminal construction project in Norway. The income to be earned on the contract this year will amount to EUR 3.7m. Next year, the gain should be "more considerable". The Norwegian market offers great opportunities to Energomontaż Północ. EP has already reported this year that it had signed a contract for steel sections and modules for two drilling platforms worth EUR 18m. All of EP's contracts signed this year have exceeded PLN 100m. The company should also benefit from the imminent energy construction rally in Poland.

### Instal Kraków

#### Going into real estate development

Instal Kraków will carry out its first real-estate project on its own site in Cracow. The company signed a contract with Chemobudowa for a housing estate. The contract value is PLN 28.5m. The construction is scheduled for completion by the end of 2007. Instal Kraków has large cash resources (ca. PLN 23m net) enabling it to become involved in real estate development. We do not know the value of the land on which the estate will be built, or how much IK paid for it. If we factor in the land cost, the value of the project may amount to PLN 40-50m. Budimex's gross margin on its real state development business in 2005 was 18%. Assuming a 20% return, we can expect Instal Kraków to earn PLN 8m-10m in gross sales terms (PLN 9.4m in 2005). The current benign housing demand climate mitigates the risk of failure.

#### Environmental contract

Instal Kraków signed a PLN 3.6m contract with Miejskie Przedsiębiorstwo Wodociągów i Kanalizacji (MPWiK) for filter modernisation at the Raba I water treatment plant. Combined, all of the company's contracts with MPWiK signed over the last 12 months are worth PLN 7.9m.

### Mostostal Warszawa

#### PLN 124m office building deal

MW signed a general contracting deal with Bonifraterska Development for design and delivery of the Belvedere Centrum office building with retail space, and with a gross usable floor area of ca. 51,000 sq m, located in Warsaw. The value of the deal is EUR 31.7m (ca. PLN 124m). The contract is scheduled for completion by January 2008. This is a sizeable contract from the public construction sector.

### Remak

#### Remak goes to Germany

According to *Parkiet*, Remak is carrying out assembly work worth EUR 10m for the Italian "Ansaldo", one of the subcontractors building new power generating units for German power plants. Remak is also hoping to win some business from Foster Wheeler, for a new fluidised-bed boiler at the Łagisza Power Plant. Both contracts are within the framework of Remak's core business. A sideline business which it has recently moved to is general contracting for environmental protection projects. Both markets offer considerable business opportunities. The only question which remains are margins: general contracting for water and sewage systems is a new line of business for Remak, posing a risk of an error when calculating the gains on such contracts. The assembly work market, in turn, has just started to come back to life, which means that it will take several quarters to go back to higher margins.

#### A small contract for Sefako

Remak signed a PLN 4.7m contract with Sefako for installation of a boiler and boiler accessories at Germany's Trea Leuna 2.

## Construction

### PBG

#### **The first deal with NATO**

PBG signed a PLN 23m contract with NATO for upgrading and expansion of the fuel storage in Gardeja. The project timeline is 24 months from approval of the detailed design. Set against PBG's total revenues, this is a small contract, which, however, may be the first step toward the company's future partnership with NATO.

#### **ZREW**

ZREW signed a turbine renovation contract with International Paper Kwidzyn. The contract value is PLN 2.9m. The deadline is set for the end of 2005.

# Metals

## Grupa Kęty

### First quarter results

#### Flexible Packaging Segment

Even though Kęty's Flexible Packaging Segment had to halt sales for about two weeks in the wake of the fire which took place in January (55% of the capacity was out of service), the company has succeeded in achieving a 4% growth in its revenue. Kęty was able to resume sales and contract delivery so quickly by renting machines from other manufacturers (based in the Czech Republic, and Łódź), enabling it to retain its key accounts. Customer loss was the major concern in case of failure. Kęty should have its full capacity restored as early as in June, which should help it return to earning 14%-16% margins. One proof of the segment's good condition is the fact that the company has no intention of giving up the capacity it now leases in Łódź after recovery of its own. The plan is to acquire new orders which, toward the end of the year, will be moved for processing on the new printing machine which Kęty plans to buy this year (achieving greater capacity than before the fire).

#### Extruded Product Segment

According to the Management, Kęty recorded a ca. 40% increase in EPS's sales volume, mainly on the back of strong domestic demand. This was possible, among others, by maintaining low selling prices (despite aluminium price hikes on the LME) owing to the company's metal inventories built toward the end of 2005 (2 months of 1Q'06). Kęty is gradually increasing the prices of its products (which went up 6%-8% in the first quarter), which should protect its mark-ups in the following quarters.

### Grupa Kęty's first-quarter results

(PLN m)	Q12005	Q12006	change	Q12006*	change
Revenue	166.2	224.1	-25.9%	228.1	37.3%
EBITDA	28.1	22.3	25.7%	35.3	25.8%
EBIT	19.6	11.4	71.5%	24.4	24.8%
Net profit	17.4	9.2	88.9%	20.0	15.1%

Source: BRE Bank Securities based on Grupa Kęty's figures, estimates net of fire impact

Looking at Kęty's first quarter results, we see the considerable impact of the January fire. The table above shows our earnings estimates after exclusion of that impact. The adjustment concerns three elements:

Revenues from lost sales are PLN 5m higher (with a growth rate of not 4%, but 14%; the Management had even projected 20%)

EBIT is PLN 4m higher owing to higher margins (12% instead of 5%). We excluded the costs of printing on third-party printers (normalised segment margin is 14%-16%)

EBIT is PLN 9m better based on destroyed asset cost posting.

Looking from that viewpoint, we rate Kęty's financial results as very good, keeping in mind that the second and third quarters are the best season for the company.

#### Aluminium Systems

The segment of aluminium systems posted a 80% growth in revenues, owing to the takeover of Aluprof and new business acquisitions by Metalplast. Organic business growth amounted to 35%, driven in half by higher prices (raw materials), and in half by higher volumes. The key contributor to the segment's growth was the airport terminal contract (totalling PLN 36m). It is obvious that Kęty wants to develop that segment, among others through further acquisitions.

#### Extra income in Q2

In the first quarter, Kęty posted PLN 9m in costs incurred from asset losses in the wake of the January fire. All of the assets were insured. The company expects to receive the insurance compensation in the second quarter (from a consortium of PZU and Hestia). The payment should not be lower than disclosed in the report (though it may be higher). Note also that the asset destruction costs reported by the company were not the only expense charged against the first-quarter income. Kęty also incurred costs on cleaning up after the fire, site development, and securing external capacity, all of which affected the company's operating profit in the first months of the year. Those costs will not be repeated in Q2.

## Metals

### Acquisitions

After taking over Aluprof, Kęty is looking for other acquisition targets. The Management pointed out two areas of interest: The first is to buy Metalplast Złotów, manufacturer of door handles and window fittings, from the State Treasury. That company's line of business fits the needs of the Aluminium Systems Segment which is currently buying those products from external providers. Kęty estimates that half of Metalplast's output would stay within the group, and the other half would be sold on the Polish market, which is currently flooded by imports (weak, pre-restructuring domestic companies). This seems like a reasonable strategy, especially considering the notable rally in construction which is bound to last for several more years. Metalplast Złotów's annual revenues are ca. PLN 40m. The tender for Metalplast should be resolved in the second half of the year. Kęty is not the only bidder.

Kęty are also looking to the German market in search of potential acquisition targets. It is eyeing several distributors of aluminium systems for the construction industry. This is an interesting, though highly competitive segment. The Management estimates that a takeover of a distributor with annual sales of 50m euros would make Kęty into a major European player in that field.

## KGHM

### Q1'06 performance

KGHM's net profit reported after the first quarter of 2006 stood at PLN 871m, topping the Q12005 figure by 66.7%. Analysts surveyed by PAP had expected KGHM to record a bottom line of PLN 789m. The market should welcome both the quarter results and the Management's preliminary earnings estimates. We will revise our projections and recommendation after a more in-depth analysis of KGHM's quarter figures, without taking into account the recent hikes in metal prices.

Net sales were reported at PLN 2.46bn (+46.6% YoY). The surge was an effect of the bullish metal exchanges. The average price of copper on the LME was US \$4,944 /t (+51.2%), and the average price of silver was US \$312 /kg (+39.3%). KGHM increased its copper sales volumes by 13.1% to 144.7k tons, and silver sales volumes went up by 2.3% (329 tons). In Q12006, the total unit cost of copper amounted to PLN 8,460/t vs. PLN 7,138/t in the corresponding period of the preceding year (+18.5%). The increase was brought about by greater use (up 31%) of third-party loads, as well as growing costs of labour and preparatory work. The unit cost of copper derived from processing internally produced concentrate was 8.9% higher than the year before. KGHM reported a PLN 51m gain from its financing activities (gains on F/X differences, interest, revaluation, and settlement of derivatives).

### Quarterly and annual figures

(PLN m)	Q12006	Q12005	change	2005	2004	change	2006*	2005	change
Revenue	2 460.1	1 677.8	46.6%	7 883.9	6 158.0	28.0%	10 500.0	7 883.9	33.2%
EBITDA	1 034.1	573.9	80.2%	2 793.3	1 643.9	69.9%		2 793.3	-100.0%
margin	42.0%	34.2%	22.9%	35.4%	26.7%	32.7%		26.7%	-100.0%
EBIT	949.2	503.3	88.6%	2 501.5	1 371.0	82.5%		2 501.5	-100.0%
Gross profit	100.5	553.9	-81.9%	2 589.0	1 446.8	78.9%		2 589.0	-100.0%
Net profit	871.9	523.0	66.7%	2 349.6	1 398.1	68.1%	3 500.0	2 349.6	49.0%

Source: KGHM, \* new preliminary Management forecast

### Hedges

KGHM's price hedging exercise covered ca. 29% of its copper sales and ca. 38% of its silver sales. In US dollar terms, the company hedged 13% of its total sales. KGHM recorded gains on US dollar hedge contracts and losses on metal hedging.

At the end of Q1 2006, the revaluation reserve amounted to PLN -1.68bn vs. PLN -1.02bn at the end of December 2005. Over the first three months of the year, KGHM decreased the negative value by PLN 975m, and transferred a PLN 312m loss from equity to the income statement. The company's 2006 hedge programme covers ca. 34% of its copper sales, to be reduced to ca. 16% in 2007. The same values for silver are 31% and 8% respectively, or 18% and 9% in US dollar terms. At the end of March, the fair value of KGHM's open positions in derivatives stood at PLB -1.85bn. If the current macroeconomic conditions are sustained, that amount will be charged against KGHM's 2006 and 2007 profit.

### New earnings guidance

KGHM's Management is working on a new budget with a revised net profit

## Metals

estimate (from the current PLN 1.8bn). Preliminary estimates are as follows: copper prices at US \$5,800/t, silver at US \$11/troy oz, PLN/USD exchange rate of 3.25, CAPEX at PLN 858m, electrolytic copper output of 550,000 tons, and silver output of 1,156 tons. The Management also plans to buy extra shares in Polkomtel by the end of the year.

Based on those estimates, the Management projects that KGHM's net profit will reach PLN 3.5bn, with sales at PLN 10.5bn. Total unit cost of electrolytic copper is estimated at PLN 9,045/t max.

### Dividend

KGHM increased its proposed dividend from PLN 3.5 per share to PLN 5.5 per share. The final dividend decision will be taken at the next General Assembly scheduled at May 31st. KGHM will propose June 21st as ex-dividend day, with payout at July 11th.

### Dialog's future

KGHM's Management announced that it will decide on the further course of action with respect to Dialog divestment in May. A short list of bidders has already been drawn up. Considering KGHM's current financial standing, we should not expect it to go ahead with the sale of its telecommunications assets unless the potential buyer offers a very good price (PLN 1.2-1.4bn for Dialog). If the company manages to get its asking price, it will be a great success for the Management, though buyers might feel differently.

## Gas & Oil

### PKN Orlen

#### Mazeikiu sale still unresolved

There is still no word on who will be selected as strategic investor for the Mazeikiu refinery. Nothing has changed in that respect since March. The transparency of the award procedures still leaves a lot to be desired. We know that the Lithuanian government, which is the one calling the shots even though the majority stake is being sold by Yukos, is still in talks with the bidders. We also know that PKN Orlen filed an official offer both to Yukos and the Lithuanian government. The selling price is a secret, but PKN Orlen is reportedly prepared to pay US \$2.5 billion for the stake and shell out an extra US \$1 billion to invest in the refinery, logistics, and distribution. Moreover, PKN Orlen pledged that, if awarded the deal, it will signed contracts with oil suppliers to secure continuous deliveries. According to Lithuanian press, PKN Orlen's chances have increased, but it is still hard to assess that the odds of winning really are. The delay may be a sign that the Lithuanian government is afraid of selling the refinery to a non-Russian investor, but at the same time does not want to sell it much cheaper than PKN Orlen's bid which is allegedly the highest.

Acquisition of Mazeikiu Nafta now would present a big challenge for PKN Orlen, especially given that it has not yet finished its integration with Unipetrol, that the fate of the fuel stations in Germany is still undecided, and that there is still much to be done in the company's own backyard (make retail more effective, expand capacity at the refinery and the petrochemical division). On the other hand, one should not pass on a buy opportunity, and leaving Mazeikiu in the hands of a Russian investor would pose significant risk for Polish refineries in the long term (threat of a quick expansion into Poland). That is why we see the acquisition of the Ukrainian refinery as a "necessary evil" which, with right management and integration with the existing operations, may be turned into a value driver in the future. We are not worried about PKN Orlen's ability to finance the purchase. At the end of 2005, the company had approximately PLN 1.4 billion in liquid financial assets, a PLN 2.8 billion net stake in Polkomtel, and several subsidiaries in the Czech Republic which it is in the process of selling (their value is some PLN 400m-500m). The ratio of Interest-Bearing Debt to Assets was 13.5%, offering a possibility to increase leverage by approximately PLN 8-10 billion (prior to the acquisition) with the debt remaining at a relatively safe level. All in all, we estimate PKN Orlen's financial capacity at ca. PLN 12-14.5 billion excluding cash generated from operations during the year.

#### Conditional dividends

After its full-year earnings report, PKN Orlen proposed to pay out dividends at PLN 4.5 per share, representing 50% of the 2005 free cash flow, in line with its profit distribution policy announced weeks before. However, the payout will be conditional: shareholders will get dividends only if the company loses its bid for Mazeikiu and retains the cash necessary to make the payout. The problem is that the Lithuanian refinery may not be sold by the time PKN Orlen holds its General Assembly (scheduled tentatively for June). PKN Orlen is currently looking into whether it can establish a conditional dividend and then cancel it if it is picked as the successful buyer, or make the payout and count it toward the 2006 profit distribution next year.

PLN 4.5 per share is a very generous dividend which investors are likely to be very pleased with. PKN Orlen pays out the highest dividends of all the companies in the region: its dividend yield is 7%, while the dividend yield of MOL is 1.2%, OMV's is 1.7%, Neste's is 1.5%-3.0%, and Lotos will not make any payout at all this year.

#### No management changes

PKN Orlen's Supervisory Board did not make any further changes in the Management Board, which does not mean that the incumbent management has managed to prove its worth to the State Treasury. Rather, the lack of replacements is due to a lack of appropriate candidates, and the government wants to avoid the turmoil which took place at PGNiG after a few of its Management Board members resigned in November of last year. Another reason could be that there are no solid grounds to call off the current management: the financial performance is good despite some slowdown in the first quarter, business is growing, and the company is planning major investments and acquisitions. Anyway, we find that PKN Orlen's execs are fully professional and effective in increasing the company's value, and enjoy the trust of financial investors. Their successors would have to be even more highly skilled and respected to become accepted by the other shareholders. In our opinion, the government will want to avoid yet another controversy after the Pekao/BPH merger turmoil, especially since it is not certain whether the State Treasury would be able to outvote the other shareholders at a GA showdown, given that it only controls 28% of PKN Orlen's shares.

But we think that the recent government reshuffle and two new parties joining the coalition may cause more pressure on changes in state-controlled companies, posing a threat to both PKN Orlen and Lotos.

## Gas & Oil

### A weak first quarter

According to unofficial reports, PKN Orlen's first-quarter earnings, scheduled for release on May 15th, will be weak. Sales will show an increase, driven mainly by the consolidation of Unipetrol, incorporated into the group in June 2005. Margins in the first three months were weak, as was the Ural / Brent differential. Also, the problems with gas deliveries which we saw in January led to production cutbacks at Anwil and BOP. We expect sales to be reported at PLN 13.95 billion, i.e. double the last year's figure, while EBIT will plunge 32% to PLN 550m, and net profit will decline to PLN 427m.

We will see an improvement in the second quarter, when the demand will restructure itself in favour of high-margin product manufacturers (gasoline, diesel). The market conditions are also more favourable (larger Ural / Brent differential, better refining margins, increase in product prices). Polkomtel's dividend payout might be another profit driver. According to unofficial data, Polkomtel may pay out its total profit plus retained earnings, which, according to our estimates, represents gross income of PLN 470m to be earned by PKN Orlen in the second quarter.

## Lotos

### Deal with Shell Trading

Lotos signed an agreement with Shell Trading securing deliveries of feedstock for the new systems which will be launched after completion of an upgrading and development initiative at the refinery in Gdańsk. The deal is worth PLN 11 billion, and will probably enter into force in 2009 for a term of 12 years.

Lotos's investment programme is the company's biggest challenge at the moment, promising a chance for cost cuts and sales increase in the future. Lotos wants to end the financing arrangement stage in early 2007. Naturally, the fact that Lotos has secured feedstock deliveries for itself this early in the process is a good thing, however, we do not know enough details to assess whether and to what extent the company's interests are also secure with such a long-running agreement.

### No dividends, increase of stake in Petrobaltic possible

Lotos's CEO Paweł Olechnowicz said that the company is currently discussing 2005 profit distribution with the State Treasury. The Management would prefer to retain the whole of the profit at the company without paying out dividends. However, Lotos will probably buy a 31% stake in Petrobaltic, thus handing some of the cash over to the State Treasury.

Acquisition of an extra stake in Petrobaltic would be a good move, as Lotos would then have full control over that mining company. We think that, as things stand, retention of the total profit would be reasonable, providing Lotos with the necessary cash to finance its investment and expansion plans. The only problematic issue here would be that one shareholder would be given preferential treatment and receive a quasi-dividend.

## PGNiG

### PGNiG finally has Boss

PGNiG's Supervisory Board named Mr. Bogusław Marzec as President of the Management Board. Mr. Marzec, formerly Vice-President in charge of finances, was appointed to sit on the Management Board on February 17th. The Board President elections announced in November were not successful. Mr. Marzec's background is in the shipbuilding industry, where he held the post of Management Board member and headed several shipyards.

We find it good that PGNiG finally got its President, and the Management Board is almost complete. PGNiG has to finally start its investments, and sit down with Gazprom to negotiate gas deliveries, which is impossible without a solid management. We expect the new Board President to announce a strategy overview for his company.

### Employees want stocks

PGNiG's employees are demanding the free stocks which they were supposed to receive within 6 months from the public offering. The government is stalling the decision, fearing that an increased free float on the market would facilitate PGNiG's takeover, e.g. by the Russian Gazprom. Even though the government would still hold a majority interest in the company, a new investor would have a considerable influence on its operations, and could hamper delivery negotiations, or block the search for alternative gas supplies. So, the government wants to first introduce some form of protection against a hostile takeover of PGNiG.

A higher free float would be good, though, even if employees get the promised stock still this year, it will probably be subject to restrictions preventing sale earlier than two years from vest-

## Gas & Oil

ing. A hostile takeover of PGNiG is not unlikely, especially considering the Russians' appetite for a European expansion. After grant to employees, the free float would increase to ca. 30% - a stake carrying potentially large influence on a company's business.

### **A promise of dividends: cash for investors, assets for the State**

The press speculates that, following suspension of its investments, PGNiG may pay out the entire 2005 profit as dividends (PLN 0.17 per share). The State would receive dividends in kind (transmission assets), while financial investors would get cash. An investment hold is not a good move in a long term, potentially leading to profit deterioration, especially with lesser activity in oil and gas mining.

Last year, PGNiG earned PLN 2.7bn, and then lost its management, putting all strategic decisions on hold, which is harmful to business. Investors would certainly be very happy to receive dividends, but we think that PGNiG should only make payout after it completes the necessary cash-earning investments, not before. Dividends in the form of assets owing to the State are a part of the settlements related to transmission asset leases.

### **Lower crude stock**

PGNiG adjusted its crude oil reserves in Lubiatów and Grotów by 300,000 tons down to 1.1 million tons in 2008. Given the current crude prices, the company's profit will decline by approximately PLN 500m. PGNiG stated that those estimates are subject to change depending on the outcomes of further research.

# Pharmaceutical Manufacturers and Distributors

## Drug Market

### Reimbursable drug list

The new list of reimbursable medications will be released on June 15th. Over 1000 applications for inclusion are pending approval. One of the formal requirements for listing a drug as reimbursable is statement of detailed cost and pricing information. This requirement was designed to serve as a threshold for inclusion of innovative drugs in the list. The National Health Fund (NFZ) estimates that drug reimbursement expenses will increase by 5% in 2006, to PLN 6.63bn. The bad situation in public healthcare and the fact that the government has no money to increase physicians' salaries, may force the Health Ministry to follow a cautious reimbursement policy of not introducing innovative drugs in the reimbursable list. This may affect the growth rate of the Polish drug market. This is probably one of the reasons why the rate of growth forecasted by IMS Health for the drug market for 2006 was revised downward from 6.8% to 5.2%. For now, however, we do not see any reason to revise our one-year projections for pharmaceuticals distributors.

## PGF

### Dividend: PLN 2.40 per share

PGF's Management will recommend profit distribution at PLN 2.40 per share, implying payout of almost 50% of the standalone net profit. Last year, dividends amounted to PLN 2.20 per share. The dividend news is in line with market expectations.

## Bioton

### Bioton buys factory in India

SciGen purchased a biopharmaceutical company from India's Shreya Biotech. The value of the deal was not disclosed. Before, Shreya Biotech acted as contract manufacturer for SciGen and other biopharmaceutical manufacturers. According to SciGen's press release, the capacity of the newly acquired factory will suffice to meet the needs of both SciGen and its partners for the next decade. It will also facilitate continued contract manufacture for other biotech manufacturers. The purchase will be finalised by the end of May 2006. This is another news indicating that Bioton is expanding its capacity. It is currently building a manufacturing plant in Russia which will cover the Eastern European market. SciGen's plans also include manufacturing facilities in Israel (to cover Western Europe, the U.S. and Canada), as well as in China (serving the Chinese market).

### Issue of 2m shares cleared

Bioton registered its raised share capital following placement of 2.02 million shares (addressed to SciGen shareholders). Bioton's share capital now comprises 180.1m shares.

### Stock issue and split

Bioton (24%) formed a joint-venture with Hefei (25%) and Scigen (51%) under the name of Hefei-SciGen-Bioton Biopharmaceutical Company Ltd, dedicated to manufacture and sales of finished dosage forms of biotech products in China and other countries, as well as development research on biotech products. The new entity's share capital is US \$12.5m; Bioton will contribute US \$3m of that amount in cash. This is a follow-up to Bioton's December plans.

At the June GA, Bioton's management will recommend a one-to-five stock split and issuance of new shares worth PLN 340m. The gains will be allocated to acquisitions and other investments. Contrary to the issuance plans, the stock split is a new development.

### Oral diabetes medication added to product range

Bioton bought rights to use the marketing authorisations and manufacturing technologies of a medicinal product called Avaron from Biovena Pharma. This is an oral diabetes drug, complementary to Bioton's product portfolio. The Polish market of oral diabetes drugs in 2005 totalled PLN 240m, with the subsegment represented by Avaron amounting to PLN 60m. Avaron sales are set to be launched two months after contract execution. Oral drugs help in diabetes management. Their addition to the product portfolio is in line with Bioton's plans. We do not know any details of the Avaron contract. We can predict that sales in the few initial years from launch will range from several to ten-odd millions of zlotys. This is good news, though without major impact on Bioton's financial performance in the initial years from launch.

## Food sector

### Polmos Lublin

#### Preliminary Q1 results

(PLN m)	Q12006	Q12005	change	2006F	2005	change
Revenue	116.8	67.5	73.1%	393.8	349.3	12.7%
Sales excl. excise tax	30.5	21.0	45.1%	115.9	101.7	
EBITDA	3.9	3.6	8.7%	23.9	14.2	68.4%
margin	3.4%	5.3%	-	6.1%	4.1%	-
EBIT	2.8	2.7	1.1%	19.2	10.4	84.6%
net profit	2.0	1.3	57.1%	13.7	2.9	370.7%

Source: Polmos Lublin, BRE Bank Securities

Despite sizeable revenue growth, EBITDA margin plummeted. This was due to both the increased share of low-margin vodkas in total sales, and the expenses incurred on enhancing the image of the flagship brand, the "Wódka Żołądkowa Gorzka" bitter-sweet digestive vodka. The fight for market share (currently at 9%) is conducted at the expense of margins. According to Polmos Lublin's management, future efforts will focus more on improving profitability. The company operates on a bearish market, which, in our opinion, may significantly hamper its return to higher margins. Polmos Lublin is still, though to a lesser degree than in the past, dependent on its main distributor, the CEDC. This exposes it to the risk of reduced sales possibilities in case of a conflict. In light of Polmos Lublin's quarterly results, there is a risk that the company will not meet our annual earnings forecast.

## Other Sectors

### Kogeneracja

#### Very good standalone Q1 results

As we had expected, Kogeneracja's standalone first-quarter results were much better than posted after the first quarter of last year. Such excellent performance was mainly owed to the harsh winter which led to higher sales volumes in heating (+10.6% YOY) and electricity (+3.1% YoY). Q1 overheads were stable, while non-recurring expenses increased only due to higher output volumes (coal prices did not increase). Kogeneracja will publish its consolidated Q1 results in May.

(PLN m)	Q12006	Q12005	change
Revenue	186.8	158.8	17.6%
EBITDA	60.3	53.6	12.5%
margin	32.3%	33.8%	-
EBIT	49.1	41.6	18.0%
gross profit	49.8	42.3	17.7%
net profit	39.8	33.8	17.8%

Source: Polmos Lublin, BRE Bank Securities

### Mondi

#### Q106 performance

Mondi's Q106 revenue was reported at PLN 328m, with EBITDA at PLN 76.8m and net profit at PLN 39.3m, showing a year-over-year growth by 0.7% and 11.7% respectively. Lower financial income (positive F/X differences in Q12005) resulted in a net profit which was 14.6% lower than the year before. Considering the macroeconomic conditions, Mondi's performance in the first quarter was good. In Q1, Mondi recorded a 3.9% increase in the prices of its products in PLN terms quarter to quarter, reflecting the improving situation on the European paper market. Realised paper prices were still 5.1% short of the Q12005 levels, mainly due to a 4.8% appreciation of the zloty and a high year base for euro prices (the cycle hit its low only in August 2005). According to our estimates, PLN prices in the second quarter should start to go up at a rate of 1%-2% YoY), resulting in further margin widening. Compared to the first quarter, average PLN prices in the second quarter are 6%-7% higher. In the first quarter of 2006, output sales were nearly 10,000 tons (+ ca. 5%) higher than in the corresponding period of last year, largely offsetting the lower paper prices and facilitating revenue growth. Unit cost of scrap paper and wood dropped by 16.9% and 6.1% respectively. In our forecast, we project that the unit cost will stay flat from 2005 (vs. +2% earlier). Scrap paper and wood account for ca. 25% of the total costs.

#### Quarterly and annual figures

(PLN m)	Q12006	Q12005	change	2005	2004	change
Revenue	328.2	325.9	0.7%	1 282.5	1 304.5	-1.7%
EBITDA	76.8	68.7	11.7%	304.5	375.3	-18.9%
margin	23.4%	21.1%	11.0%	23.7%	28.8%	-17.5%
EBIT	50.1	42.6	17.6%	197.2	265.8	-25.8%
Gross profit	49.6	55.5	-10.7%	166.6	269.8	-38.2%
Net profit	39.3	46.0	-14.6%	135.4	289.8	-53.3%

Source: Mondi, \* new preliminary Management forecast

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

**EV** – net debt + market value (EV – economic value)  
**EBIT** – Earnings Before Interest and Taxes  
**EBITDA** – EBIT + Depreciation and Amortisation  
**PBA** – Profit on Banking Activity  
**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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**BUY** – we expect that the rate of return from an investment will be at least 15%  
**ACCUMULATE** – we expect that the rate of return from an investment will range from 5% to 15%  
**HOLD** – we expect that the rate of return from an investment will range from -5% to +5%  
**REDUCE** – we expect that the rate of return from an investment will range from -5% to -15%  
**SELL** – we expect that an investment will bear a loss greater than 15%  
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