KBC Securities

Flash

Sygnity

18 July 2007

Another year in the red

IT, integrator

Poland

Current price PLN 87.5*

Fair Value PLN 78.8

Sell

Rating downgraded

Performance over	1m	3m	12m
Absolute %	22%	-13%	-13%
Rel. WIG20 %	22%	-18%	-34%
12m Hi/Lo	PLN 123.5/70.1		

Reuters	COMW.WA
Bloomberg	CPL PW
Market Cap €	160.7m
Next corporate event 2Q07 figures on 9th August	
PLN / €	3.7535

FY/e 31.12., PLN m	2006A	2007F	2008F	2009F
Sales	927.1	1,289.6	1,403.9	1,509.2
Adj. EBITDA	51.9	36.9	94.6	113.1
Adj. EBIT	24.4	2.9	57.0	73.7
Adj. Net Profit	3.2	-5.3	47.0	60.0
Adj. EPS (PLN)	0.40	-0.49	4.26	5.45
Adj. P/E (x)	194.0	n.m.	20.5	16.1
DPS (PLN)	1.0	1.3	2.0	3.9
Yield (%)	1.1%	1.4%	2.3%	4.5%
Adj. EV/EBITDA (x)	14.1	25.1	10.9	8.9

Source: Sygnity, KBCS; 4Q06-2Q07 Emax cons.; later merger; fully adj. figures

We expect Sygnity to post very poor consolidated figures for 2Q07 with a net loss of PLN 13.6m, flat year-on-year, due to: i) still weak gross profit margins, weighed down by large hardware contracts recognition, ii) an additional depreciation charge and iii) still very low efficiency of the parent company and Emax (before its closure at the end of May). We expect consolidated revenues to come in at PLN 386.7m, up 158% y/y, boosted by large hardware contracts recognition. Consolidated EBIT is expected to come in at a PLN 20.9m loss for 2Q07 versus a PLN 14.5m loss in 2Q06. Please note that the base does not include the consolidation of Emax but incorporates many one-off costs, e.g. the costs of CoLorado implementation, unsuccessful Russian expansion and the merger with Emax. Given the underperformance of the 1Q07 figures, the gloomy outlook for 2Q07 – which indicates the pressing need for in-depth restructuring – and fully including the additional depreciation, we have cut our reported net earnings forecasts for 2007 to a loss of PLN 39.0m versus a net loss of PLN 27.6m in 2006. We have also cut our net earnings forecasts by 32% to PLN 37.6m for 2008 and by 12.3% to PLN 54.4m (up 44.8% y/y) for 2009. As our new fair value estimate at PLN 78.8 per share, down 20.3%, implies 10% downside, we downgrade the stock to Sell.

**Priced at COB 17/07/07*

Downgrade to Sell

- **Disappointing outlook for 2Q07:** Given the outlook for weak gross profit margins, an additional depreciation charge and still very low efficiency of the parent company and Emax (before its closure), we expect Sygnity to record a PLN 13.6m net loss in 2Q07, flat year-on-year.
- **2007 likely in the red, potential rebound no earlier than 2008:** We believe Sygnity requires in-depth restructuring that should lead to optimisation of the capital group structure, headcount cuts in back-office and software production centres as well as higher margin contracts via a combined product offer. In our opinion, any positive effects from restructuring, that we find inevitable, are unlikely to become visible until 2008, as any profits in 2H07 will probably be eaten up by additional depreciation. The company could be helped by a rebound in the public administration, although we believe this is also more likely to occur in 2008.
- **Substantial downgrades to continue:** With the outlook for 2007 being in the red on reported figures, we believe there will be further downgrades to consensus, incorporating in a far longer than expected recovery, lower merger synergy, higher one-off costs and additional deprecation. Our forecasts net earnings are substantially below the consensus for 2007 (PLN 30.8m) and 48% below 2008 expectations.
- **Discount warranted:** Trading at a 2008F P/E of 20.5x, Sygnity is in line with its peers. We believe, however, that a discount is warranted given the risks to any potential rebound in 2008 and onwards.

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