

Friday, 26 January 2024 | update

LPP: buy (reiterated)

LPP PW; LPP.WA | Retail, Poland

Improved Medium-Term Growth Profile

LPP reported solid results for 3Q of FY'23/24, and we expect an equally strong 4Q with a greater-than-anticipated focus on cost optimization. This, coupled with a steep recovery in gross margin led by underlying industry trends (freight rates, PLN's rise vs. USD, better negotiating position vis-à-vis Asian suppliers, and lower discounts) will lead to an improved operating margin. We expect these trends to continue into 2024, and after merely fine-tuning our margin assumptions for 2024-2025, this year we currently expect a 60bp increase in gross margin along with a 90bp decline in EBIT margin due to higher labor costs and marketing spend.

Since our last update, LPP has issued an updated guidance for FY2024, significantly stepping up the pace of planned 2024 store area growth and pointing to the upper end of the previously guided range for 2025 and 2026. We believe that the decision to accelerate was partly due to a more cautious approach to growth taken by rival Pepco, which has decided to slow its roll-out in order to focus on profitability. LPP, on the other hand, maintains a high level of profitability and will use its strong balance sheet position to grow market share. LPP's actions appear to be an attempt at taking advantage of its rival's temporary weakness to capture a larger share of the addressable market.

We expect stronger sales growth in 2024 than LPP's guidance (we expect revenue of PLN 21.8bn vs. PLN 20bn) as we assume real wage growth, a rising minimum wage, and new fiscal stimulus, will boost consumer spending on mostly discretionary categories. The main risk to this assumption is if consumers opt to allocate their higher disposable income to savings rather than additional spending.

Based on LPP's faster store area growth plans, coupled with a greater focus on costs, we have revised our EBITDA estimates for 2024E/2025E around 3%/7% higher, respectively.

At ca. 7.2x 2024E EV/EBITDA, LPP is trading in line with the peer group. We think that LPP's growth profile at current multiples is more than appealing as we do not believe the current multiples accurately reflect the company's improved medium-term growth profile: in the next three years, LPP's EBITDA is expected to grow at an annual rate of 16% compared to 8% for the peer group. As a result, we raise our target price for LPP to PLN 20,000 with a reiterated buy recommendation.

Upside Still There from Additional Fiscal Expansion

Poland's current ruling coalition made a lot of promises during last year's election campaign, one of their flagship proposals being an increase in tax-free income. Whether Poland's budget can accommodate this promise is open to question, but its passing would potentially contribute to an increase in LPP's sales in 2025, which we estimate to be at least at 1%.

Dividend Yields Should Further Support Valuation

LPP has indicated that it might distribute around 70% of the previous year's net profit in 2024 as dividends to shareholders (the upper end of the dividend policy range). We assume a similar payout ratio will be applied in 2025. At current prices, this would imply a dividend yield of 4.2%/5.2% for 2024E/25E, higher than the peer group's 2.6%/3.1%.

(PLN m)	2022	2023E	2024E	2025E	2026E
Revenue	15,926.6	17,365.1	21,837.0	26,507.2	30,555.5
EBITDA (adj.)	2,588.9	3,720.1	4,347.6	5,080.1	5,780.0
Margin	16.3%	21.4%	19.9%	19.2%	18.9%
EBIT	1,184.4	2,342.5	2,751.5	3,245.7	3,738.9
Net profit	486.7	1,655.2	2,076.0	2,465.2	2,855.4
P/E	57.1	16.8	13.4	11.3	9.8
P/S	1.7	1.6	1.3	1.1	0.9
P/B	7.0	5.8	4.9	4.1	3.5
EV/EBITDA	14.1	8.4	7.2	6.2	5.4
DPS	349.6	429.8	624.2	782.9	929.7
Dividend Yield	2.3%	2.9%	4.2%	5.2%	6.2%

current price	PLN 15,000
target price	PLN 20,000
mCap	PLN 27.8bn
free float	PLN 12.8bn
ADTV (3M)	PLN 66.1m

*Price as of January 25, 2024, 5:00 PM

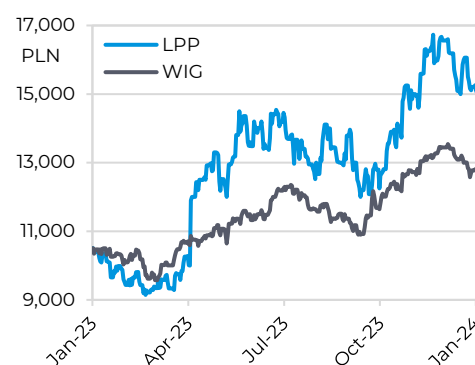
Shareholders

Semper Simul Foundation	31.2%
Sky Foundation	8.7%
Others	60.1%

About LPP

LPP Group is Poland's leading fashion retailer and one of the largest companies on the fashion market in the CEE region. The Group operates both brick-and-mortar and e-commerce sales channels. In Q3 2023/24 (LTM) the company's revenue stood at PLN 16.8bn, 25% of which was attributable to online sales. LPP's geographic presence spans 39 countries, and its fashion labels include Reserved, Cropp, House, Mohito, and Sinsay.

LPP vs. WIG



name	target price		recommendation	
	new	old	new	old
LPP	20,000	18,200	buy	buy

name	current price	target price	upside
LPP	15,000	20,000	+33.3%

forecast update	2023E	2024E	2025E
revenue	-1.4%	0.0%	+3.8%
EBITDA	+5.1%	+3.4%	+6.6%
net profit	+6.9%	+8.0%	+11.4%
SG&A/Sales	-1.2 p.p.	-0.5 p.p.	-0.4 p.p.
sales area	+0.2%	+4.4%	+7.4%

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List of abbreviations and ratios used by mBank:

EV (Enterprise Value) – Equity Value + Net Debt; **EBIT** – Earnings Before Interest and Taxes; **EBITDA** – EBIT + Depreciation & Amortisation; **Net Debt** – Borrowings + Debt Securities + Interest-Bearing Loans - Cash and Cash Equivalents; **P/E** (Price/Earnings) – Price Per Share Divided by Earnings Per Share; **P/CE** (Price to Cash Earnings) – Price Per Share Divided by Earnings + Depreciation & Amortisation; **P/B** (Price to Book Value) – Price Per Share Divided by Book Value Per Share; **P/CF** (Price to Cash Flow) – Price Divided by Cash Flow from Operations; **ROE** (Return on Equity) – Earnings Divided by Shareholders' Equity; **ROCE** (Return on Capital Employed) – EBIT x (Average Assets - Current Liabilities); **ROIC** (Return on Invested Capital) – EBIT x (1-Tax Rate) / (Average Equity + Minority Interest + Net Debt); **FCFF** (Free Cash Flow to Firm) – Cash Flow from Operations - CAPEX - Lease Payments; **FCFE** (Free Cash Flow to Equity) – Free Cash Flow to Firm - Net Interest Expense (incl. Debt + Leases)
EBITDA margin - EBITDA/Sales

OVERWEIGHT (OW) – a rating which indicates that we expect a stock to outperform the broad market
NEUTRAL (N) – a rating which indicates that we expect the stock to perform in line with the broad market
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NAV – valuation based on equity value, one of the most frequently used method in case of developing companies; the weak point of the method is that it does not factor in future changes in revenue/profits of a company.

mBank issued the following recommendations for LPP in the 12 months prior to this publication:

LPP (Janusz Pięta)

Rating	buy	buy	buy	buy
Rating date	2023-12-01	2023-10-02	2023-07-03	2023-04-03
Target price (PLN)	18,200.00	17,100.00	17,700.00	13,700.00
Price on rating day	14,880.00	13,000.00	14,010.00	9,580.00

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