

Update to Price and Investment Stance

Following this week’s publication of the FY21 interim results, we have reviewed our model and maintain our **Hold** recommendation on PG plc (“PG” or the “Group”). After updating our expectations vis-à-vis the Group’s robust H1-21 financial performance, which more specifically was achieved throughout the COVID-19 pandemic, we increased our 1-year price target from €2.00 to €2.10.

Changes to valuation model:

- Rental income:** The decline in rental income incurred by the Group throughout the period in which PG’s retail outlets were closed (March-May), amounted to approximately €0.5m. Nevertheless, in view of the fact that management expect a stronger-than-expected recovery concerning the Group’s rental income segment, we have updated our rental income projections for FY21 and beyond.
- Franchise operations:** Revenue generated from the Group’s franchise operation throughout H1-21 dropped by circa 16% on a comparative basis. Management reported that this decline is significantly less than what was previously expected with both Zara online sales and Zara Home sales registering an improvement of +109% and +26% when compared to H1-20. In this regard, we have also improved our FY21 revenue expectations concerning the Group’s franchise operation.
- Operating expenditure:** In line with the aforementioned improvement in revenue, we have adjusted PG’s operating expenditure to reflect such change.

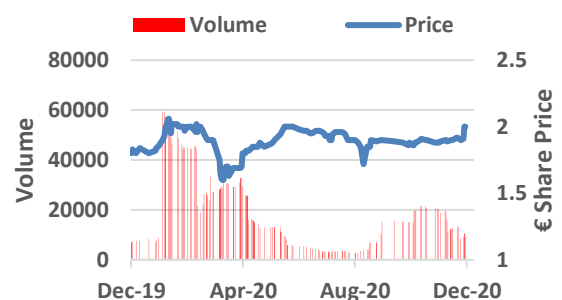
Notwithstanding the challenges presented by the COVID-19 pandemic, the Group continued to exceed expectations and achieved solid results. Evidently, PG has a unique and defensive business model with the ability to maintain a healthy and stable level of revenue, cash flow and profit even during such extraordinary times.

We believe that PG’s favourable cash position and relatively low leveraged balance sheet, might enable the Group to pursue new growth opportunities in its core line of business moving forward.

However, in line with PG’s current limited growth opportunities, in combination with the fact that both Pama and Pavi shopping villages have approached a saturation point, we believe that upon taking into consideration the current price levels and the maintained dividend yield of circa 2.2%, a Hold recommendation on the shares of PG is justified.

Stock Rating	Hold
Price target (1Yr)	€2.10
Country	Malta
Industry	Retail
Ticker	PG
Price (as at 21/12/2020)	€2.00
Price Target (1-Year)	€2.10
Upside/ Downside to PT	5.0%
12m cash div. (Forecast)	0.043
12m Total S’holder Return	7.1%
Market Cap	€216m
Shares Outstanding	108
Free Float	25%
Net Dividend Yield	2.2%
Current P/E	22.8x
1Yr Forward P/E	23.0x
Exchange	Malta Stock Exchange (MSE)
52-week range	€1.60 - €2.06

Price and Volume Movement (20 day moving average)



Source: Malta Stock Exchange

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Company Update

Despite the COVID-19 situation, the Group's liquidity position remained healthy and as a result the Group resolved to retain the same interim dividend pay-out as last year amounting to €2m or €0.0185/ share.

Valuation

Our 1-year price target is €2.10. The price target is calculated using a Price to Earnings (P/E) model of 25x, utilising a discount rate of 7.5%.

€'000s unless otherwise stated	FY18A	FY19A	FY20A	LTM21	FY21F	FY22P
	€'000	€'000	€'000	€'000	€'000	€'000
Revenue	101,238	107,977	119,997	122,786	120,249	126,296
Cost of Sales	(84,885)	(90,166)	(98,681)	(101,597)	(99,600)	(104,609)
Gross Profit	16,353	17,811	21,316	21,189	20,649	21,688
Selling and marketing costs	(1,051)	(1,028)	(852)		(1,202)	(1,262)
Administrative Expenses	(3,179)	(3,439)	(3,377)	(3,530)	(3,006)	(3,157)
Other Income	771	886	726		700	700
EBITDA	12,894	14,230	17,813	17,659	17,141	17,968
Depreciation of right of use asset	-	-	(694)	(694)	(622)	(622)
Depreciation & Amortisation	(1,202)	(1,625)	(2,001)	(2,001)	(2,185)	(2,275)
EBIT	11,692	12,605	15,118	14,964	14,334	15,071
Investment Income	-	-	-	-	-	-
Finance Income	-	-	5	(3)	-	-
Finance Costs on right of use asset	-	-	(1,018)	(1,486)	(1,029)	(1,012)
Finance Costs	(589)	(632)	(574)	-	(361)	(256)
Share of results of associates	(26)	10	(94)	(179)	(100)	(100)
Profit Before Tax	11,077	11,983	13,437	13,296	12,844	13,702
Income tax expense	(3,417)	(3,046)	(3,784)	(3,810)	(3,596)	(3,837)
Profit Available to Ordinary Equity holders	7,660	8,937	9,653	9,486	9,248	9,866
<i>Earnings Per Share</i>	<i>0.071</i>	<i>0.083</i>	<i>0.089</i>	<i>0.088</i>	<i>0.086</i>	<i>0.091</i>

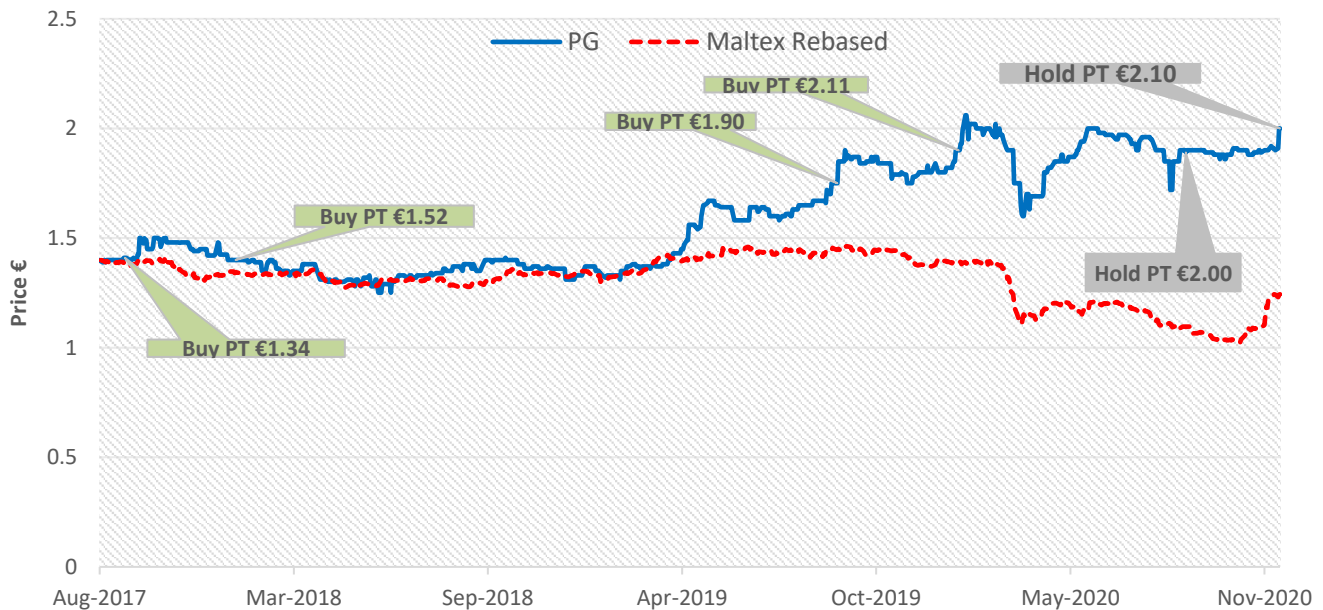
Ratio Analysis	FY18A	FY19A	FY20A	LTM21	FY21F	FY22P
Revenue Growth (YoY)	10.4%	6.7%	11.1%	2.3%	0.2%	5.0%
EBIT Margin	11.5%	11.7%	12.6%	12.2%	11.9%	11.9%
EBITDA Margin	12.7%	13.2%	14.8%	14.4%	14.3%	14.2%
Net Margin	7.6%	8.3%	8.0%	7.7%	7.7%	7.8%
Shares Outstanding (million)	108	108	108	108	108	108
Growth in Normalised EPS (YoY)	4.1%	16.7%	8.0%	-1.7%	-4.2%	6.7%
Earnings Yield	3.5%	4.1%	4.5%	4.4%	4.3%	4.6%
Dividend per Share (€)	0.039	0.042	0.044	0.044	4.3%	5.5%
Dividend pay-out-ratio	55.5%	50.4%	49.7%	50.6%	50.0%	60.0%
Dividend Yield	n/a	n/a	n/a	2.2%	2.1%	2.7%

Historic Solvency Ratios	Apr-18	Apr-19	Apr-20
Gearing Ratio Level 1 (Net Debt / Net Debt and Total Equity)	34.4%	36.8%	42.3%
Gearing Ratio Level 2 (Total Liabilities / Total Assets)	57.1%	55.2%	57.9%
Net Debt / EBITDA	1.4x	1.6x	1.8x
Current Ratio (Current Assets / Current Liabilities)	0.7x	0.5x	0.5x
Interest Coverage Ratio (EBITDA)	21.9x	22.5x	11.2x
Cash from Operations / EBIT	0.9x	0.8x	1.0x

Source: PG's Financial Statements and CC workings

Historical 1-Year Price Target

Reference	Date	Price	Price Target	Analyst	Recommendation
PG	17.12.2020	€2.00	€2.10	Andrew Fenech & Rowen Bonello	Hold
PG	11.09.2020	€1.89	€2.00	Andrew Fenech & Rowen Bonello	Hold
PG	20.01.2019	€1.85	€2.11	Simon Psaila & Andrew Fenech	Buy
PG	17.09.2019	€1.75	€1.90	Simon Psaila & Andrew Fenech	Buy
PG	13.09.2017	€1.41	€1.52	Simon Psaila	Buy
PG	30.03.2017	€1.00	€1.34	Simon Psaila	Buy



Explanation of Equity Research Ratings

Buy: Based on a current 12-month view of total shareholder return (TSR = percentage change in share price from current price to projected target price plus projected dividend yield), we recommend that investors buy the stock.

Sell: Based on a current 12-month view of total shareholder return, we recommend that investors sell the stock.

Hold: We take a neutral view on the stock 12-months out and, based on this time horizon, we do not recommend either a Buy or Sell. Current shareholders should consider buying on dips and selling on peaks.

Newly issued research recommendations and target prices supersede previously published research.

Disclaimer

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Glossary and definitions

Income Statement	
Revenue	Total revenue generated by the Group/Company from its principal business activities during the financial year.
EBITDA	EBITDA is an abbreviation for earnings before interest, tax, depreciation and amortisation. It reflects the Group's/Company's earnings purely from operations.
Operating Profit (EBIT)	EBIT is an abbreviation for earnings before interest and tax.
Depreciation and Amortisation	An accounting charge to compensate for the decrease in the monetary value of an asset over time and the eventual cost to replace the asset once fully depreciated.
Net Finance Costs	The interest accrued on debt obligations less any interest earned on cash bank balances and from intra-group companies on any loan advances.
Net Income	The profit made by the Group/Company during the financial year net of any income taxes incurred.
Profitability Ratios	
EBITDA Margin	EBITDA as a percentage of total revenue.
Operating (EBIT) Margin	Operating margin is the EBIT as a percentage of total revenue.
Net Margin	Net income expressed as a percentage of total revenue.
Return on Common Equity	Return on common equity (ROE) measures the rate of return on the shareholders' equity of the owners of issued share capital, computed by dividing the net income by the average common equity (average equity of two years financial performance).
Return on Assets	Return on assets (ROA) is computed by dividing net income by the average total assets (average assets of two years financial performance).
Earnings per Share (EPS)	Earnings per share (EPS) is the amount of earnings per outstanding share of a Group's/Company's share capital. It is computed by dividing net income by total shares outstanding as at the statement of financial position date.
Dividends Ratios	
Dividend per Share	Dividend per Share is the amount of dividends per outstanding share of a Group's/Company's share capital. It is computed by dividing net dividends by total shares outstanding as at the statement of financial position date.
Sustainable Growth Rate in Dividends	This ratio indicates the sustainable growth rate of dividends given the profitability of the Group/Company and the respective level of dividends distribution.
Dividends Yield as at year-end	This ratio indicates how much a Group/Company pays out in dividends each fiscal year relative to its share price. It is computed by the dividing the Dividend per Share by the share price as at year-end.
Cash Flow Statement	
Free Cash Flows (FCF)	The amount of cash the Group/Company has after it has met its financial obligations. It is calculated by taking Cash Flow from Operating Activities less the Capex of the same financial year.
Balance Sheet	
Total Debt	All debt obligations inclusive of long and short-term debt.
Net Debt	Total debt of a Group/Company less any cash and cash equivalents.
Shares Outstanding	Outstanding shares refer to the Group/Company stock currently held by all its shareholders.
Financial Strength Ratios	
Current Ratio	The Current ratio (also known as the Liquidity Ratio) is a financial ratio that measures whether or not a company has enough resources to pay its debts over the next 12 months. It compares current assets to current liabilities.
Quick Ratio (Acid Test Ratio)	The quick ratio measures a Group's/Company's ability to meet its short-term obligations with its most liquid assets. It compares current assets (less inventory) to current liabilities.
Interest Coverage Ratio	The interest coverage ratio is calculated by dividing EBITDA of one period by cash interest paid of the same period.
Gearing Ratio	The gearing ratio indicates the relative proportion of shareholders' equity and debt used to finance total assets.
Gearing Ratio Level 1	Is calculated by dividing Net Debt by Total Equity.
Gearing Ratio Level 2	Is calculated by dividing Total Liabilities by Total Assets.
Net Debt / EBITDA	The Net Debt / EBITDA ratio measures the ability of the Group/Company to repay its debt through EBITDA generation.
Cash from Operations / EBIT	This ratio measures the ability of the Group/Company to convert its earnings into cash.