

BULGARTABAC HOLDING
INDUSTRY: TOBACCO
BACK IN THE GAME

BULGARTABAC HAS OVERCOME THE SHAREHOLDERS' CONFLICT AND IS GROWING BOTH ITS LOCAL AND FOREIGN MARKETS. PROFITABILITY NORMALIZES TO PRE-CONFLICT LEVELS AND ABOVE EXPECTATIONS WITH EBITDA UP 112% Y-O-Y IN Q2'15 DUE BOTH TO RISING SALES AND IMPROVED EFFICIENCY. OWNERSHIP TRANSPARENCY REMAINS THE MAJOR RISK

SOLID GROWTH ON ALL FRONTS

A year after the peaks in the shareholders' conflict, Bulgartabac is returning to normal with solid growth on all fronts. As the conflict seems to be resolved, revenues are up 8% y-o-y in H1'15 to 263m lead by significant growth in both domestic sales and exports. EBITDA is up 111% y-o-y to BGN 55.2m, normalized net income increased more than threefold to BGN 36.6m and net income after extraordinary items is up 46% y-o-y to 36.2m. EBITDA margin doubled to 20.96% closer to industry average due to better efficiency on the cost side.

RESULTS OUTPERFORM ESTIMATES

Results outperform our base case scenario bottom line and significantly outperform our negative scenario both on the top and the bottom line. This makes us much more comfortable with the base case scenario going forward. Nevertheless, due to continuing lack of transparency from the company we remain cautious and keep our forecasts for a base case 3% growth on the top line, 15% EBITDA margin and 9.4% net income margin for FY2015.

DIVIDEND IS BACK

Bulgartabac reinstated dividend payments in 2015 at the top of the preliminary announced DPS range. The company paid a total of BGN 31m or BGN 4.20 DPS out of 2014 profits, yielding 9%. We consider this an improvement in the corporate governance and a better alignment of shareholders' interest. We also expect dividend policy to continue at the current pace.

LACK OF TRANSPARENCY REMAINS A MAJOR RISK

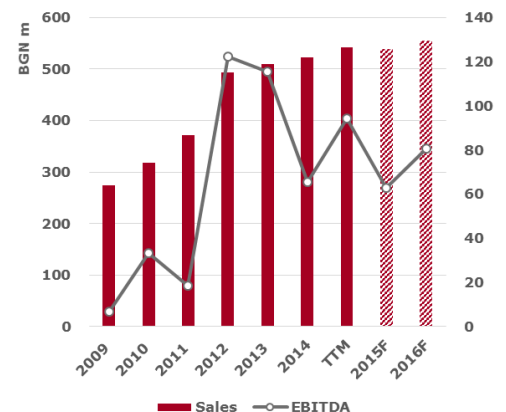
Nevertheless, transparency remains a major problem, especially, when it comes to the major beneficiary owners of the company. According to media reports, Bulgartabac's majority shareholders ownership structure has changed at the beginning of 2015. The latter has so far not been announced by Bulgartabac and it preceded the dividend reinstatement announcement. Such an ownership change signals an end to the major shareholders conflict that peaked with the fall of Corporate Commercial Bank. While the latter triggered the stock sell off, the continuing lack of ownership transparency and low liquidity is fueling local investors' distrust in the stock. Thus, the rebound in fundamentals has not yet been reflected in the price, offering an excellent buy opportunity.

VALUATION: We reiterate our BUY recommendation and our target price of BGN 93.75 per share as the company performed better than our base case scenario and significantly outperformed our negative scenario. Thus, it offers a 104% upside **RISKS:** Poor corporate governance.

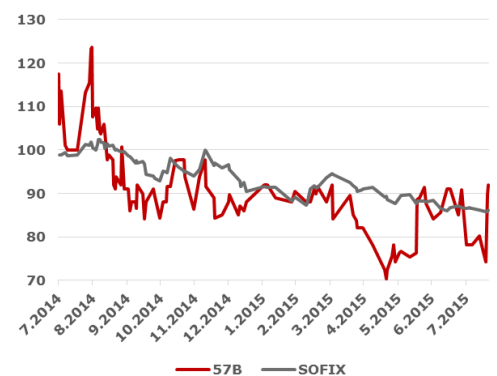
Individual results ('000 BGN)	2013	2014	2015F	2016F
Revenues	508 892	522 338	538 008	554 148
EBITDA	115 284	65 586	80 701	91 434
Net profit	67 722	31 195	50 573	63 561
Equity	354 145	390 147	403 506	465 485
ROE	19.12%	8.00%	12.53%	13.65%
ROA	9.40%	4.61%	4.90%	5.77%
EBITDA margin	22.65%	12.56%	15.00%	16.50%
Net profit margin	13.31%	5.97%	9.40%	11.47%
EPS	9.19	4.23	6.86	8.63
Debt/equity	0.38	0.24	0.27	0.15
P/E	11.42	10.63	6.69	5.32
P/B	2.18	0.85	0.84	0.73
EV/EBITDA	7.76	6.12	5.06	4.06
DPS	0	4.20	4.25	5.52
Dividend yield	0%	9%	9.26%	12.03%

RESULTS ANALYSIS
BUY
ONE YEAR PRICE TARGET: BGN 93.74
CURRENT PRICE: BGN 45.90
EXCHANGE RATES
EUR/BGN (FIXED): 1.95583
USD/BGN: 1.7714
MARKET DATA

Shares Outstanding:	7.37m
Share Capital:	7.37m
Free-float:	1.9%
Treasury Shares	0%
Market Cap.:	BGN 338 m
Avg. Daily Vol.:	BGN 8 000
52 Weeks Range:	BGN 32.75 – 57.45
BSE Ticker	57B
Bloomberg Ticker	57B BU

EBITDA RECOVERY UNDERWAY


Source: Elana Trading 2015 estimates

STOCK YET TO RECOVER


Source: Bloomberg

BULGARTABAC'S CONSOLIDATED RESULTS REVIEW

One year after the peak of the major shareholders' conflict, Bulgartabac holding is overcoming the drawbacks and is registering solid growth on all fronts. The top and bottom lines performed above expectations vs both our base and negative case scenarios.

Local sales volumes up 12.6% in H1'15

Revenues: In H1'15, sales are up 8.2% y-o-y to BGN 263 m vs. a cautious 3% our base case sales growth expectations for FY2015. Major drivers were both local sales and exports. Exports picked up in Q4'14 due to sales to Russia, the Adriatic region and the Far and Middle East. In H1'15 exports growth subsided a bit as local sales registered significant improvement. Bulgartabac reports local sales volumes up 15.6% y-o-y in Q2'15 and 12.6% y-o-y in H1'15 thanks to lower illicit market in the country. The company also reports an increase in its market share – up 0.7% y-o-y to about 34% of the local market.

Sales in Bulgaria up substantially above expectations

Overall, the local cigarette market has registered 7.9% in H1'15. This is an exceptionally high pace of growth and significantly above our expectations. It can be attributed mostly to the new government's efforts in fighting illicit cigarette production and trade. According to media reports, the Customs have increased their supervision over local cigarette production and import which lead to a significant decline in the illegal market. No immediate legal and illegal market stats are yet out, however, the government reports higher revenue collection including from cigarette excise tax (up 7% y-o-y as of May 2015). Bulgartabac reports 10% y-o-y higher paid taxes in H1'15 to BGN 336m, mostly excise.

Excise changes may further support local sales

In addition, the new government postponed the expect 16% excise tax hike and according to media reports may be changing the excise structure to the benefit the lower priced brand producers as Bulgartabac. Initially, the tax increase was planned for 2015, then for 2016. Recent media reports reveal that the hike may again be postponed (EU deadline is Jan. 1st, 2018) and the government may propose an excise tax structure change increasing the ad valorem weight but lowering the specific volume based weight. We think there is a 50/50 chance of changing the excise structure depending on state budget effect estimations as it would trigger consumers to migrate to lower priced cigarettes. Nevertheless, we keep our sales forecast at a more cautious pace of 2% CAGR for 2015-2019 and expect Bulgartabac to continue to rely more on its much bigger exports base vs. local sales. The company gave no immediate numbers on H1'15 exports. It did mention it increased its portfolio mix in the Philippines, Taiwan and the Adriatic region and started exports to Kazakhstan.

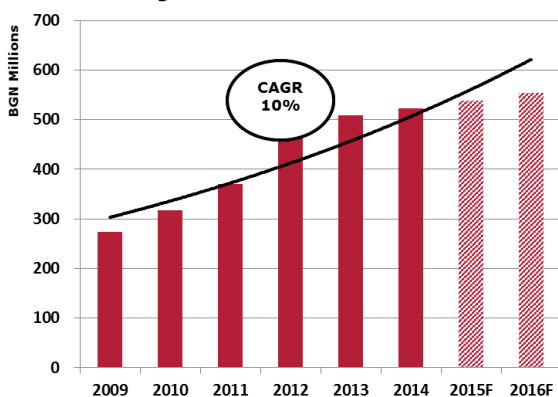
H1'15 profitability above expectations

Profitability: In H1'15, the top line significantly outperformed expectations. EBITDA up 111% y-o-y to BGN 55.2m, normalized net income increased more than threefold to BGN 36.6m and net income after extraordinary items up 46% y-o-y to 36.2m. EBITDA margin doubled to 20.96% closer to industry average due to better efficiency.

Cost efficiency measures were already evident in Q1'15 and continued in Q2'15. Despite the rising US dollar material costs are down 20% y-o-y, labor costs are down 12.6% while external service cost slowdown their upward trend and are up 31.6% y-o-y. Management explains higher external services costs with its efforts to expand in exports markets and increase the product mix where it the company is already present. Partially, more efficient numbers can be attributed also to minority shareholders efforts in instating a financial controller in the company. Such a controller was allowed this spring upon the request of E.Miroglio Finance that owns 7.22% of Bulgartabac.

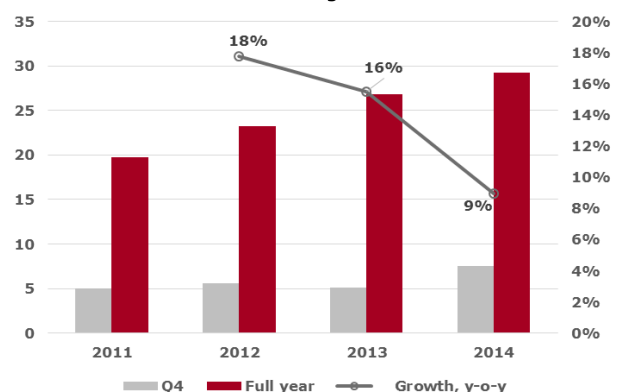
Transparency: In 2015, Bulgartabac reinstated dividend payments arguing better performance in Q4'14. In July 2015, the AGM approved a DPS at the top bound of the pre-announced range. However, recent media reports state that the dividend reinstatement announcement was preceded by a change in the Company's shareholder structure. According to media reports, on the 2nd January 2015, the Liechtenstein entity Stiga ANSALT acquired 50% of BT Invest from another Liechtenstein entity - LIVERO Establishment. The latter owns directly 79.83% of Bulgartabac and as of today, the company has not announced any shareholder structure changes. Following that there are no management changes which makes us confident that such a change may be a signal that the previous shareholders' conflict has been resolved.

Exhibit 3: Revenue growth at 10% CAGR over the last 7 years



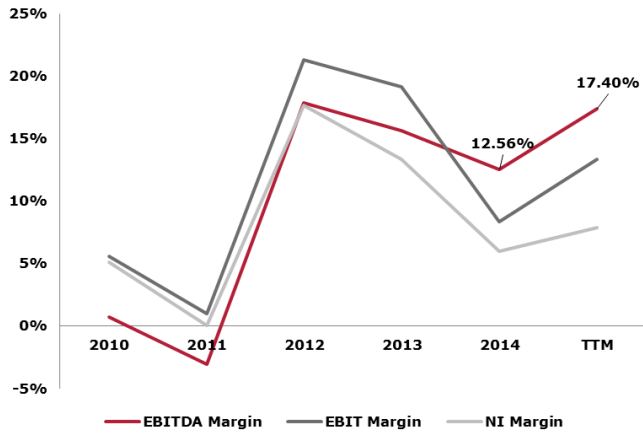
Source: Company data; Elana Trading Estimate

Exhibit 4: Volumes continued to grow in H1' 2015



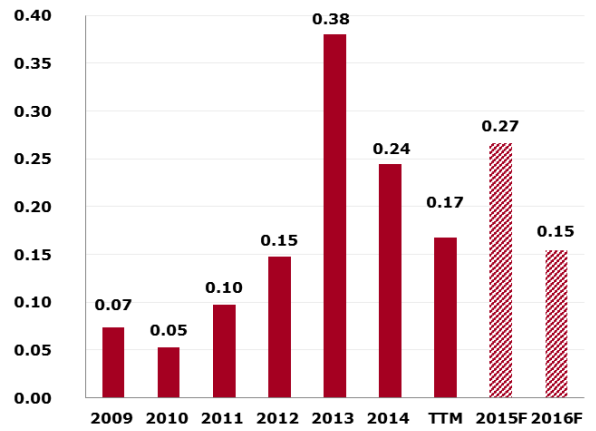
Source: Company data; No full H1'15 volumes available yet

Exhibit 5: EBITDA margin recovered in mid 2015



Source: Company data

Exhibit 6: D/E recovering faster than expected



Source: Company data; Elana Trading estimates

CONSOLIDATED FINANCIAL DATA

INCOME STATEMENT (IN '000 BGN)	2012	2013	2014	H1 2014	H1 2015	TTM
Revenues from Cont. Operations	475 799	472 447	510 778	242 820	255 933	523 891
Other revenue	17 351	36 445	11 560	591	7 460	18 429
Total Revenues	493 150	508 892	522 338	243 411	263 393	542 320
Operating Expenses	-387 938	-411 550	-478 611	-227 616	-219 155	-470 150
Change in Inventories	-1 361	-12 899	11 879	11 670	255	464
Cost of Material	-237 049	-268 485	-307 827	-161 418	-129 187	-275 596
Cost of Labor	-72 594	-67 128	-73 756	-38 592	-33 732	-68 896
Cost of External Services	-48 357	-32 845	-50 978	-19 553	-25 885	-57 310
Depreciation and Amortization	-17 017	-17 942	-21 859	-10 627	-10 971	-22 203
Net Book Value of Assets Sold	-2 619	-1 143	-22 628	-3 966	-13 692	-32 354
Other Costs	-8 941	-11 108	-13 442	-5 130	-5 943	-14 255
EBIT	105 212	97 342	43 727	15 795	44 238	72 170
Financial revenues	466	997	-18 321	-23	57	-18 241
Financial expenses	-1 790	-6 717	-12 077	-5 056	-3 019	-10 040
Interest expense	-1 382	-6 206	-6 389	-3 598	-2 880	-5 671
EBT	103 888	91 622	13 329	10 716	41 276	43 889
Income Tax Expense	-10 134	-6 663	-3 424	-1 254	-4 645	-6 815
Income Before XO Items	93 754	84 959	9 905	9 462	36 631	37 074
Extraordinary Loss Net of Tax On Discontinued Operations	-3 962	-14 824	21 216	15 516	0	5 700
Minority Interests	2 742	2 413	-74	212	448	162
Net Income	87 050	67 722	31 195	24 766	36 183	42 612
EARNINGS PER SHARE IN BGN	11.82	9.19	4.23	3.36	4.91	5.78

BALANCE SHEET (IN '000 BGN)	2012	2013	2014	H1 2014	H1 2015	TTM
CASH AND NEAR CASH ITEMS	62 509	13 865	25 932	20 823	15 345	15 345
SHORT-TERM INVESTMENTS	0	0	45	81	45	45
ACCOUNTS AND NOTES RECEIVABLE	141 736	75 543	94 292	165 287	95 177	95 177
INVENTORIES	159 702	196 223	156 603	179 859	125 661	125 661
OTHER CURRENT ASSETS	2 761	189 188	11 655	10 976	4 541	4 541
TOTAL CURRENT ASSETS	366 708	474 819	288 527	377 026	240 769	240 769
LT INVESTMENTS AND LT RECEIVABLES	25 160	884	106 711	96 751	219 732	219 732
NET FIXED ASSETS	215 885	224 881	224 839	242 607	215 361	215 361
OTHER LONG-TERM ASSETS	8 698	19 678	56 613	1 375	62 507	62 507
TOTAL LONG-TERM ASSETS	249 743	245 443	388 163	340 733	497 600	497 600
TOTAL ASSETS	616 451	720 262	676 690	717 759	738 369	738 369
ACCOUNTS PAYABLE	172 925	166 125	91 734	81 325	118 094	118 094
SHORT-TERM BORROWINGS	28 445	125 405	44 832	95 624	44 480	44 480
OTHER SHORT-TERM LIABILITIES	2 353	4 607	84 359	105 819	110 662	110 662
TOTAL CURRENT LIABILITIES	203 723	333 746	220 925	282 768	273 236	273 236
LONG-TERM BORROWINGS	24 798	9 397	50 702	31 255	26 698	26 698
OTHER LONG-TERM LIABILITIES	15 425	15 526	14 916	17 271	14 157	14 157
TOTAL LONG-TERM LIABILITIES	40 223	24 923	65 618	48 526	40 855	40 855
TOTAL LIABILITIES	243 946	358 669	286 543	331 294	314 091	314 091
TOTAL PREFERRED EQUITY	0	0	0	0	0	0
MINORITY INTEREST	11 632	7 448	4 973	10 862	6 609	6 609
SHARE CAPITAL & APIC	7 367	7 367	7 367	7 367	7 367	7 367
RETAINED EARNINGS & OTHER EQUITY	353 506	346 778	377 807	368 236	410 302	410 302
TOTAL EQUITY	360 873	354 145	390 147	386 465	424 278	424 278
TOTAL SE & LIABILITIES	616 451	720 262	676 690	717 759	738 369	738 369

NUMBER OF SHARES:	7 367 222	7 367 222	7 367 222	7 367 222	7 367 222	7 367 222
PRICE IN BGN - PERIOD END:	78	105	45	102	40.8	45.9
MARKET CAP IN BGN - PERIOD END:	574 643 316	773 550 943	331 524 990	751 456 644	300 214 297	338 155 490

Source: Company IFRS Financial Statements Audited; Elana Trading Estimates

Bulgartabac Holding Overview

COMPANY PROFILE

Bulgartabac Holding is the leading Bulgarian cigarette producer. Ex state incumbent, currently, the company has about 30-34% market share selling about 3.6-3.8bn cigarette sticks annually.

The holding is a vertically integrated company with two modernized cigarette producing factories in Bulgaria in the cities of Blagoevgrad and Sofia. It has a tobacco processing factory in the city of Pleven and recently acquired a cigarette producing factory in Banja Luka and significant control over the major cigarette packaging producer in Bulgaria – Yuri Gagarin (4PX BU).

The Group is export oriented with 30% CAGR of exported volumes in the last seven years. Its major export markets are in the Far and Middle East, Russia and South Eastern Europe. 10% overall sales growth over the last six years.

The Group has a diversified product portfolio with 10+ well position brands in the mid to low priced segments of the market. Victory is the most well recognized cigarette brand in Bulgaria and 2nd in sales in the country.

The Company was privatized in October 2011 by a Vienna based entity – BT Invest.

FUNDAMENTAL STORY

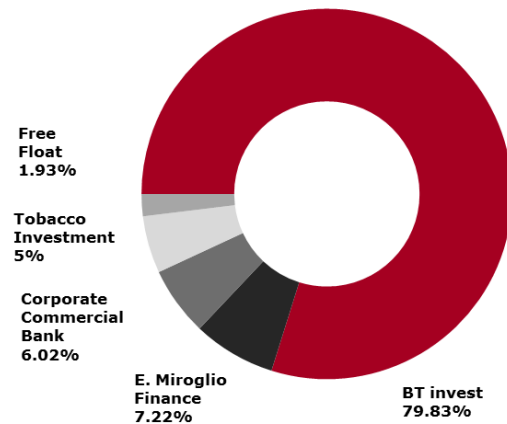
Bulgartabac Holding has a leading market position in Bulgaria in the mid to low priced segment of the cigarette market. Over the last decade it re-focused on exports and currently 80%+ of sales come from foreign markets. Recently, it renew sales to Russia and targets low regulation high growth emerging markets for export growth.

Local political protection supports its base in Bulgaria and it slowly started regaining market share after sharply losing it in the 2007-2011 period.

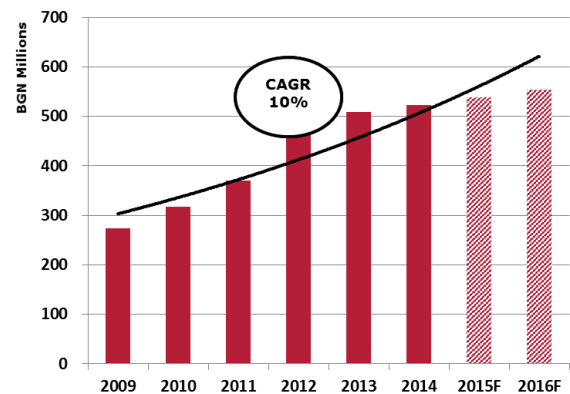
STRENGTHS & OPPORTUNITIES

- Stable and growing local market position
- Strong export focus
- Declining debt levels
- Experienced and well-seasoned management

SHAREHOLDERS' STRUCTURE



SALES GROWTH



WEAKNESSES & THREATS

- Susceptible to political influence
- Unknown real majority owner
- Poor corporate governance

Disclaimer

Regulatory Restrictions: No publication of ELANA Trading should be construed as an offer (or solicitation of an offer) to **U.S. persons** to buy or sell financial instruments or any financial product, make any investment or participate in any particular trading strategy (collectively "Offers"). No Publication of ELANA Trading should be construed as an Offer (or solicitation of an offer) in any jurisdiction in which such Offer would be illegal. Any such perceived Offer will not be honoured by ELANA Trading.

Analyst Certification: The research analyst(s) certifies that: (1) all of the views expressed in this document accurately reflect his or her personal views about any and all of the subject securities or issuers; (2) no part of any of the research analyst's compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed by the research analyst(s) in this document.

Financial Interest: ELANA Trading may trade or own shares of the analyzed companies. The research analyst(s) is not holding shares of the analyzed companies, unless otherwise noted.

Regulatory Authority: Financial Supervisory Commission, *Budapest Street 18, 1303 Sofia, Bulgaria*

Information Disclosure: All reasonable care has been taken to ensure the facts stated are accurate and opinions given are fair and reasonable. Our recommendations are based on information available to the public that we consider to be reliable but for the completeness and accuracy of which we assume no liability. Neither ELANA Trading, nor its directors, officers or employees shall in any way be responsible for its contents. The views expressed may differ from the views of other firm departments or representatives. Additional information is available upon request. Unless otherwise noted, sources for all information in charts and tables are ELANA Trading's calculations.

Risks for Investors: Information in this document should not be regarded as an offer to buy or sell any financial instruments. The investment possibilities discussed in this document may not be suitable for certain investors depending on their specific investment objectives and time horizon or in the context of their overall financial situation. In particular, the risks associated with an investment in the securities or the financial instruments under discussion are not explained in its entirety.

The prices or values of the securities may go down as well as up and can fluctuate and fall against the investor. The securities or investments may cause the investor to lose the amount invested. Past performance is not a guide to future performance. Changes in exchange rates may have an adverse effect on the value, price or income of the securities or investments.

Valuation Methods: Company valuations are based on the following methods: multiple-based (P/E, P/B, EV/EBITDA), historical valuation approaches, peer comparisons, discount models (DCF, DDM) or asset-based evaluation methods. Valuation models are dependent on macroeconomic factors, including interest rates, foreign exchange rates, prices of raw materials, and any expectations about the economy, the market sentiment. The valuation is based on expectations that might change rapidly and without notice, depending on developments specific to individual industries and countries. Recommendations and target prices derived from the models might therefore change accordingly. The application of models depends on forecasts of a range of economic variables, thus there is a range of reasonable variations within models. Any valuation is dependent upon inputs that are based on the subjective opinion of the analysts carrying out this valuation.

Recommendations: Analyst(s) recommendations are based on the specific factors for the company, sector, country and global developments, as compared to market indices. Recommendations and opinions reflect ELANA Trading's expectations over the 12-month period following publication from the perspective of long-only investment clients. ELANA Trading reserves the right to express different or contrary recommendations and opinions for different timescales or for other types of investment client. Except as otherwise noted, expected performance over next 12 months vary for different recommendations for Bulgarian stocks as follows:

BUY	Target price is more than 10% above current quotes
HOLD	Target price in +/-10% range of the current quotes
SELL	Target price is more than 10% below the current quotes

Frequency of Recommendations: No schedule of recommendations is available. The frequency of recommendations depends on specific factors to individual companies and the opinion of the analyst(s) for the necessity of minor or major changes.

Copyrights: The copyrights of ELANA Trading analyses belong to the Research Department of the brokerage and their content cannot be used for commercial purposes. Replication and redistribution of ELANA Trading analyses content is expressly prohibited without the prior written consent of the appointed contacts listed below.

For more information, please contact:

Research analyst:	Phone:	E-mail:	Internet:
Tatyana Vasileva	+ 359 2 810 00 24	vasileva@elana.net	www.elana.net
Tsvetoslav Tsachev	+359 2 810 00 23	tsachev@elana.net	www.elana.net