Company Analysis | DR. KALLIWODA | INTERNATIONAL RESEARCH GmbH | Equity Research

30th May 2017

Europe | Poland | Marketing

DR. KALLIWODA
INTERNATIONAL RESEARCH GmbH

Initial Coverage

BUY

Target price: PLN 5.15

Industry:	Marketing
Country:	Poland
ISIN:	PLINTMS00019
Reuters:	IMS.Pap
Google Finance	WSE:IMS
Website:	www.ims.fm

Last price:		3.40
	High	**Low**
Price 52 weeks:	3.19	3.69
Market cap. (PLNm)		113.90
Avg 20d volume (shares)		2000
No of shares (m)		33.50

Shareholders

Management Board	41%
Supervisory Board	12%
Others	24%
Free float	24%

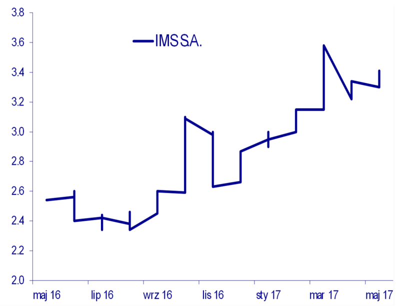
Performance

4 weeks	1%
13 weeks	9%
52 weeks	45%
YTD	18%

Dividend

	in PLN	in %
2012	0.02	2.11%
2013	0.04	2.33%
2014	0.08	3.33%
2015	0.23	8.75%
2016	0.12	3.48%

Price Chart



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IMS S.A.

Still a lot of room for growth

- **Market leader in sensory marketing in Poland**. IMS S.A. (the Group) is a leader of specialised sensory marketing services in Poland with unique competitive advantage. The company operates in the media and modern technology segment and provides methods that help effectively create and build a positive atmosphere at a point of sale.
- **Business model**. The Group's business model is categorized by some the most desired features by investors: relatively low marginal cost of subscription acquisition and retention, relatively low fixed costs, low capex needs, and low working capital financing needs. These suggest: high scalability of business, high net profitability, and high free cash generation capacity. The Group has been systematically increasing market share, every year by boosting number of subscribers at CAGR of 49% during the last 5 years.
- **High profit margins**. The Group increased net revenues and maintained high margins during the latest quarter, achieving net sales of PLN 9.37m in 3M/2017 (vs. 3M/16: PLN 9.0m) and EBITDA of PLN 2.2m (vs. 3M/16: PLN 2.3m) that translates into 23.5% EBITDA margin. During 3M/2017, the Group generated operating cash flows of PLN 3.0m (vs. 3M/16: PLN 2.9m) and high profitability ratios with ROE above 27%.
- **Still a lot of room for growth**. The Group benefits from growth in sensory marketing market. The global digital signage market size was more than $14.9bln in 2015 and is estimated to increase at 5.2% CAGR from 2016 to 2023 impelled by the growing technological advancements and urbanized infrastructure in emerging markets. The global digital scent technology market is predicted to be $0.13bln in 2014 with CAGR of 32.02% and is set to achieve $1.2 billion by 2022. In consequence, the Group seems poised for further growth: our forecast provides for ≥30% CAGR of the Company's subscribers, revenues and EBITDA over the next seven years.
- **Corporate enhancements**. We believe that positive impact of the bottom line enhancement will come soon (e.g. logistics, reducing underperforming segments) and should be seen in boosting margins in mid-2017 and translate to significant increase in free cash flow margin. With regards to short-term market perspective, the 2Q/17 financials should come out good providing potential catalyst for the performance of the share market price.
- **Based on our valuation framework we set a 12 month target price of PLN 4.87 an upside of c.50% at the current price**. We initiate our favourable view of the Group because of its careful business attitude, low volatility of earnings and sales, balanced growth prospects and strong current efficiency. With a substantial fundamental upside to our 12M target price, we think the Group may offer an excellent value on top of a balanced business growth. Though, we do not expect the Group to match the size of the largest players in Europe in near time, we consider the stock to be unfairly ignored by the investors. In our view a constantly deep discount for IMS's equities the market calls for is unjustified. We consider the Group's shares strongly undervalued

Key Facts

in PLNm	2013	2014	2015	2016	2017E	2018E	2019E
Net sales	32.7	38.4	42.1	43.4	48.4	53.5	58.6
EBITDA	8.7	9.8	12.0	10.9	13.4	15.6	18.1
EBIT	5.2	6.9	8.8	7.5	9.4	11.5	13.7
Net income	3.7	5.5	6.8	5.7	7.2	8.8	10.5
EPS	0.1	0.2	0.2	0.2	0.2	0.3	0.3
BVPS	0.4	0.5	0.5	0.6	0.6	0.7	0.8
RoE	27.2%	31.8%	41.3%	30.2%	34.2%	37.9%	41.5%
EBITDA margin	26.7%	25.5%	28.5%	25.0%	27.7%	29.1%	30.9%
P/E	30.61x	20.65x	16.64x	20.02x	15.86x	12.95x	10.80x
P/BV	8.32x	6.56x	6.87x	6.05x	5.43x	4.91x	4.48x

Content

1. Group Profile

IMS S.A. (IMS Group, the Group) is a leader of specialised sensory marketing services in Poland, quoted on the Warsaw Stock Exchange.

The company video device in one of the shopping centre.

The company operates in the media and modern technology segment where use methods that help effectively create and build a positive atmosphere at a point of sale.

IMS S.A.'s structure comprises of departments that provide various type of knowledge and products:

- **IMS sensory** (sensory marketing services). IMS Sensory offers innovative and comprehensive solutions based on the newest sensory marketing technologies, such as Aromamarketing and Audiomarketing,
- **IMS media** (advertising), IMS Media offers advertisements shown on displays at shopping centres and in service networks in the Digital Signage System, Mall TV, Instore radio and non-standard media,
- **IMS r&d** (product technology and development), IMS r&d provides services in the area of innovation, technology and technical service for sensory marketing: audio marketing, scent marketing, Digital Signage and Instore advertising,

- **IMS events** (advertising and special actions), IMS events offers comprehensive event marketing services: launches of new products, conferences, trainings, incentive trips and overall marketing campaigns.

The company deliver modern marketing solutions in sensory marketing and new media at a point of sale, including the following services:

- Audio marketing Audio marketing – preparing music formats and production and broadcasting of audio advertisements by means of Instore radio.
- Digital Signage Digital Signage covers production and broadcasting of advertisements as well as image and information content on such media as e.g. LED screens located in shopping centres.
- Scent marketing Activities in this area include creation of individual scents and fragrances with focus on the brand image and the place of sale.
- Event marketing Event marketing activities include organization of events, trainings, incentive trips and special actions: Pop Up Store, You Tubers on GH, Spirits Marketing, Digital Signage Entertainment.
- Technology and development include services in the area of innovation, technology and technical service for sensory marketing: audio marketing, scent marketing, Digital Signage and Instore advertising. Production of servers intended for displaying video materials helps manage displayed content later on.

Sources: The Group website.

2. SWOT Analysis

Strengths	Weaknesses
- Specific business expertise and technological competence at customized solutions for marketing sector - Diversified customer structure - Excellent skills in project management - Fast-growing marketing company with operating margins of 20-30% - Solid balance sheet with low level of debt and improvment in cash conversion cycle - Rising number of active subscriptions - Highly scalable business model allows for significant dividend payouts in the long run - Medium to high barriers of entry - Innovation leader in the areas of sensory merketing solutions - Dynamic growth of sales (CAGR 2016-2009: +28%) - Free float of 21% - Low marginal cost of subscription acquisition and retention, relatively low fixed costs, low capex needs, and low working capital financing needs	- Competition from smaller market players - Rise in total managment compansation (fixed) from 0.87m to PLN 1.37m inspite of the same sales levels. - Dependence on the Polish market, which accounts for almost 92% of total revenues - Share buy-backs with provision to sale the shares inside the company are too frequent, excessive and drag down free float
Opportunities	**Risks**
- Potential for scale up business in Europe and Asia without excessive capex expenditures - Potential for developing new products and services - Benefits due to the development of technology - IMS should keep benefiting from relatively low wage costs in Poland - Growing importance of providing content through digital signage that serves as an efficient marketing strategy for enterprises - Value-accretive M&As e.g. acquisitions of companies with a deep sector expertise	- Loss of key employees - Pricing pressures - Management compansations (fixed) may augument without reason - Changes of respective laws and regulations in retail sector - Economic slowdown as the advertisement market is strongly correlated with the economic cycle - Strong PLN in relation to USD : unfavorable impact on the results from foreign contracts after translation - International expansion; The Management Board is unsuccesful so far in acquiring a notable int. company, hence we are not sure how they deal with managing and supervising foreign entity - Insufficient sales staff

Source: Dr. Kalliwoda International Research GmbH

3. Valuation

In order to account for current market valuations, we have valued the Group by using DCF model. With WACC (weighted average cost of the capital) of 10%, our DCF-based fair value of IMS S.A. is PLN 5.15.

a. DCF-model

2 Main assumptions

Weighted Average Cost of Capital	**10%**
Perpetual Growth Rate	**2%**

3 Basic Financials

In PLNm	2017E	2018E	2019E	2020E	2021E	2022E	2023E	Normalised
Profit and loss statement								
Sales	48.4	53.5	58.6	63.6	68.4	72.8	76.8	78.3
EBITDA	13.4	15.6	18.1	19.3	20.5	21.4	22.3	23.1
- Depreciation and amortization	4.0	4.1	4.4	4.7	5.0	5.3	5.5	0.6
= EBIT	9.4	11.5	13.7	14.6	15.4	16.2	16.8	22.5
Balance Sheet								
Fixed assets	15.7	17.4	19.0	20.7	22.2	23.7	25.0	25.4
+ Working Capital	11.7	12.9	14.1	15.3	16.5	17.5	18.5	18.9
= Capital Employed	27.4	30.3	33.2	36.0	38.7	41.2	43.5	44.3

4 Financial ratios and normalised cash flow assumptions

	2017E	2018E	2019E	2020E	2021E	2022E	2023E	Normalised
Growth rate	12%	11%	10%	9%	8%	7%	6%	**2.0%**
EBITDA Margin	27.7%	29.1%	30.9%	30.4%	30.0%	29.4%	29.0%	**29.5%**
Operating Cash Flow Margin	21.6%	22.7%	24.2%	23.9%	23.7%	23.4%	23.2%	**23.2%**
EBIT Margin	19.4%	21.4%	23.4%	23.0%	22.6%	22.2%	21.8%	**28.7%**
After tax EBIT Margin (tax rate of 19%)	15.7%	17.3%	18.9%	18.6%	18.3%	18.0%	17.7%	**23.3%**
After tax return on capital employed (tax rate of 19%)	27.8%	30.6%	33.4%	32.9%	32.3%	31.8%	31.2%	**41.1%**
Fixed assets / Turnover ratio	32.5%	32.5%	32.5%	32.5%	32.5%	32.5%	32.5%	**32.5%**
Working capital / Turnover ratio	24.1%	24.1%	24.1%	24.1%	24.1%	24.1%	24.1%	**24.1%**
Asset turnover	1.8x	1.8x	1.8x	1.8x	1.8x	1.8x	1.8x	**1.8x**

5 Free cash flows calculation

In PLNm	2017E	2018E	2019E	2020E	2021E	2022E	2023E	Normalised
EBIT	9.4	11.5	13.7	14.6	15.4	16.2	16.8	**22.5**
- Corporate income tax (19%)	(1.8)	(2.2)	(2.6)	(2.8)	(2.9)	(3.1)	(3.2)	**(7.9)**
+ Depreciation and amortization	4.0	4.1	4.4	4.7	5.0	5.3	5.5	**(0.6)**
- Change in working capital	1.2	1.2	1.2	1.2	1.1	1.1	1.0	**(0.4)**
- Capital expenditures	(0.8)	(1.3)	(1.5)	(1.2)	(0.3)	(0.2)	0.1	**0.1**
Operating Cash Flow	10.4	12.1	14.2	15.2	16.2	17.0	17.8	**18.2**
- Capital expenditures	(0.8)	(1.3)	(1.5)	(1.2)	(0.3)	(0.2)	0.1	**0.1**
Free cash flow	**10**	**11**	**13**	**14**	**16**	**17**	**18**	**16**

6 Free cash flows present value

In PLNm	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Discounting factor	0.93	0.85	0.77	0.70	0.63	0.58	0.52
Free cash flow present value	8.95	9.16	9.77	9.78	10.11	9.76	9.45
Terminal value							105.44
Total present value in PLNm	172.44						
12M Target Price per share in PLNm	***5.15***						

Source: Group data, Dr. Kalliwoda International Research GmbH

b. Peer Group Analysis

There are two notable competitors: M4B (Poland) and Clear Channel (USA). Both companies has capability to compete at the same market as the Group. There is no point to perform peer valuation as the universe of peers is insufficient to make a reasonable assessment.

In brief, M4B trades P/E 61x and P/S 16x, Clear Channel is unprofitable company with bad period at the NYSE exchange, currently trading at P/S 0.49 and reporting ROE of -50%. On the other hand the Group trades at relatively healthy and stable multiples, P/E c.20x and P/S c.2.6.

c. Piotroski F-Score

Piotroski F-Score assigns a score from 0 (more likely to go bankrupt) to 9 (strong financials) based on 9 PASS/FAIL tests. This analysis influences our forecast of trends and cost of equity. We use TTM values (3M/16 – 3M-17).

Piotroski F-Score	
Profitability	**Yes (1) or NO (0)**
Positive net income	1
Positive Operating CF	1
Higher ROA	0
Operating CF > Net Income	1
Leverage Components	
Lower debt	0
Higher Current Ratio	1
Lack of shares dilution	1
Operating Efficiencies	
Higher Gross Mgn	0
Higher Asset Turn	0

Source: Group data, Dr. Kalliwoda International Research GmbH

IMS Group's F-Score = 5 (range: 0 – 9)

d. Summary:

Due to the fact the peer group analysis is based on only two strict comparable firms, the valuation based on this method should not yield fair value of the Group. Therefore, we do not use the conclusion from peer group analysis into calculating the target price, but rather along with Piotroski F-Score we use them as a plausibility check of the valuation.

Hence, based on our DCF valuation framework, **our target price for the stock equals to PLN 5.15.**

4. 9M/15 Financial Results

a. Revenues, Profitability

The Group published its first-quarter results for period ending on 31 May 2017. The Group generated total sales of PLN 9.36m, which corresponded to a growth of +3.9% y-o-y. Net profit amounted to PLN 1.04m vs. PLN 1.23m in 1Q/2016. In the first quarter of 2017, operating expenses increased by PLN 0.21m vs. 1Q/2016. PLN (increase over the period of 3%). The largest increase in costs was noticed in the costs related to consumption of materials and energy with increase by PLN 0.17m - mainly due to higher consumption of aromas and depreciation with increase by PLN 0.10m. Furthermore, the costs of outsourced services and salaries increased, that is associated with the systematic increase of sales staff in the Group.

3M/17 vs. previous year period			
in PLNm	**3M/17**	**3M/16**	**change (%)**
Net sales	9.37	9.02	*3.9%*
EBITDA	2.20	2.33	*-5.4%*
EBITDA margin	23.5%	25.8%	
EBIT	1.31	1.54	*-15.0%*
EBIT margin	14.0%	17.1%	
Net income	**1.04**	**1.23**	*-15.9%*
Net margin	11.1%	13.7%	

Source: Group data, Dr. Kalliwoda International Research GmbH

The Group maintained high EBITDA margin during the latest three months, achieving margin of 23.5 %. The Group generated revenues mainly from domestic sources, which constitutes 95% of revenues.

The number of subscriptions at 31 March 2017 amounted to 11981 and is lower than at the end of 2016. The drop in the number of subscriptions compared to the end of 2016 is due to the overlap of several factors. The decline in the aroma segment is the result of the uninstallation in the first quarter of this year some devices that had been installed for the holiday season in order to service various kinds of promotional events. The drop in audio location is attributed to the fact that customers decided on a one-time purchase rather than renew a subscription contract and as well as the Group decided to reduce the number of existing locations, including smaller locations due to unsatisfactory profitability. On the other hand, the number of licenses increased on y-o-y basis from 10692 in 1Q/2016 to 11981 in 1Q/2017.

Number of licenses 1Q/2017 vs. 1Q/2016			
in numbers	***1Q/2017***	***1Q/2016***	***Change in %***
audio & video subsc.	9 667	8 663	12%
aroma subsc.	2 314	2 029	14%
total	**11 981**	**10 692**	**12%**

Source: Group data, Dr. Kalliwoda International Research GmbH

Moreover, we can observe sales diversification with regards to segments. More importantly, the growth in sales was accompanied with maintaining growth in almost all segments.

Sales structure 1Q/2017 vs. 1Q/2016			
in PLN '000	*1Q/2017*	*1Q/2016*	*Change in %*
audio & video subsc.	3 841	3 558	8%
digital signage	1 560	1 477	6%
aroma subsc.	1 436	1 203	19%
audio advertisement	1 165	1 645	-29%
events	807	614	31%
others	550	521	6%

Source: Group data, Dr. Kalliwoda International Research GmbH

b. Balance Sheet and Cash Flow

As of 31 March 2017, the most important position on the Group´s balance sheet were fixed assets of PLN 10.3m and cash and equivalents of PLN 9.1m. Total assets amounted to PLN 33.2m.

In the 3M period, the Group generated an operating cash flows of positive PLN 2.97m (vs. 3M/16: PLN 2.94m), which was higher than last year mainly due to positive change in trade receivables, attributed to one-time payments (rather than subscriptions) made by clients. Purchases of assets for PLN 0.17m was the main factor contributing to negative cash flows from investing activities of PLN -0.17m (vs. 3M/16: PLN –0.36m). The Group generated negative cash flow from financing activity of PLN -0.6m (vs. 3M/16: PLN -2.2m), mainly due to the leasing payments. In total, change in cash was positive of PLN 2.2m (vs. 3M/16: PLN 0.4m).

5. Outlook

a. Micro factors

IMS Group is the market leader in sensory marketing in Poland, and has been increasingly developing its services in other countries. At the end of 2016, the Group provided its services to 12,417 subscription locations in Poland and abroad (localization of a single audio, video or aromabox device for which a subscription fee is charged).

Subscription services are mostly based on long-term, several-year contracts. Subscription revenues account for 46% of all Group revenues.

Sources of competitive advantage of the Group are primarily based on comprehensive approach to sensory marketing and respective clients. This concerns marketing, sales, technical and logistical competencies. The Group has its own teams to carry out these specific tasks.

Direct customer service departments, built on top-of-the-line professionals for years, provide the company a tremendous competitive edge, which is hard to catch up with today's IMS Group and the close replication of these skills and competencies is unlikely to be possible for competitors.

Subscription services offered by the Group are constantly changing and refined to meet the switching needs and expectations of the market and the customer. Since its inception, the Group has been pursuing subscription services to build a positive sales environment through the use of senses. Modifications primarily take place in the service sales strategy. Variable elements are price policy, commercial documentation and diversification of services to better match market expectations.

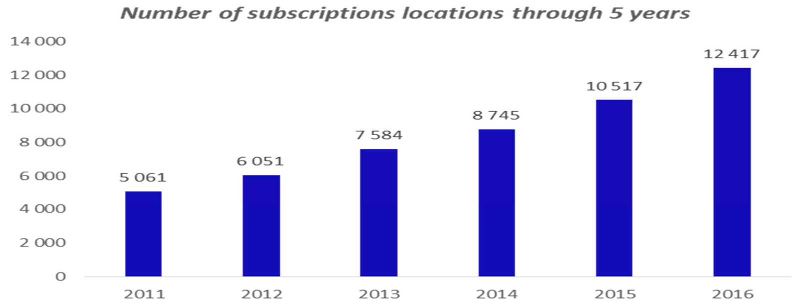
The Group's Management Board is accelerating the pace of obtaining subscription locations by expanding sales teams and extensive communication activities, providing benefits from the effectiveness of the solutions provided by the Group and the high quality of the services provided.

The Group aims to increase the number of locations reached by approximately 2,500-3,000 per year from 2018. The number of locations over the past five years has grown by 1,471 locations on average over the past five years, with an average annual increase of 1,130 in audio and video locations, and aroma location is 342.

Number of subscriptions locations through 5 years

in numbers	2011	2012	2013	2014	2015	2016	CAGR
audio & video	4 296	5 027	*6 328*	*7 238*	*8 558*	*9 944*	*46%*
aroma	765	1 024	*1 256*	*1 507*	*1 959*	*2 473*	65%
Total	**5 061**	**6 051**	**7 584**	**8 745**	**10 517**	**12 417**	***49%***

Source: Group data, Dr. Kalliwoda International Research GmbH



Source: Group data, Dr. Kalliwoda International Research GmbH

Sales structure

The IMS Group has a diversified portfolio of clients. In 2016, the Group did not enter into any deal with any client with a purchase agreement of value exceeding 10% of the total sales created by the Group. The Group look for a acquisition target in Europe and actively acquire clients in other countries. Still, the vast of sales is generated in Poland.

Sales in other countries in 2016-2015		
in PLN '000	**2016**	**2015**
Export	2 951	2 553
Poland	40 486	39 573
Export share	**7.29%**	**6.45%**

Source: Group data, Dr. Kalliwoda International Research GmbH

Largest external markets in 2016-2015		
in PLN '000	**2016**	**2015**
Slovakia	1 199	1 190
Czehc Republik	315	434
United Arab Emirates	215	0
Bulgaria	185	20
Hungary	175	219

Source: Group data, Dr. Kalliwoda International Research GmbH

Management compensation

Some questions may be asked to the Management Board why the fixed compensation increased so significantly. We believe that this issue should be closely monitored by investors. While we believe that bonus-based salaries are in line with a bit lower net income, the fixed part of salaries are above the line and may raise some concerns. Furthermore, the management purchased 860000 shares at solid discounted price during buy-back period in 2016. On the other hand the total compensation (fixed + variable salaries) is relatively constant or in line with company bottom line performance.

Management compansation (fixed) in 2016-2015 vs. Perfromance			
in PLN '000	**2016**	**2015**	Change in %
Fixed compensation	1 371	868	58%
Net Sales	43 437	42 126	3%
Net Income	5 689	6 845	-17%

Source: Group data, Dr. Kalliwoda International Research GmbH

b. Market, Macro factors

The IMS Group's operations depend on the macroeconomic situation in Poland, in particular: GDP growth rate, investment level, inflation rate, and unemployment rate and in results in consumer spendings.

The decline of the ecoeconomic situation might impact on the condition of the Group's customers, which may result in a reduction in advertising spending, the decrease in the value of investments in the sales network development or limiting the sales network among others, by closing unprofitable sales points, which will affect the number of subscription services provided to the customer. Negative changes in Poland's macroeconomic situation may generate a risk for the Group's business and thus affect its financial results.

The drivers that influence sales of the company is retail industry development and perception of retailers towards utilizing sensory marketing. The perception and willingness to use such marketing tools depends on the effectiveness of these methods. There are many factors that should stimulate usage of new, uncovered techniques of sales increase in nowadays retail industry marketplace.

Retail industry - strive for market share

The levels of competition within the retail industry gets into a hot phase. In order to please clients, retailers use changing methods to strive for market share. Several goes for big advertising investment, appealing campaigns and non-stop marketing promotions. When these are not enough, growing customer added-value by offering enjoyable shopping experience becomes an advantageous way for retailers to differentiate themselves and offer a distinctive brand experience.

Furthermore, it has also been recognized that consumers of these days want to be captivated by psychological elements where links can be created; making it vital to comprehend the components of emotional character that attracts and impact the behavior of customers, impacting on their perception. Based on this, a new marketing method, sensory marketing, has emerged, which stimulates the five senses of human (visual, sound, scent, touch and taste).

Sensory Marketing – new frontier

Sensory marketing is growing. It stands to explanation that as technology can make sensory integration more functional and cost-effective, marketers will be looking to it as the sensible new frontier. As companies broaden their product choices, new sensory marketing strategies will far better enable consumers to test a new product prior to purchasing.

Likewise, sensory cues such as sound and smell will assist companies develop more significant emotional connections to their brands. The senses impact our emotions and decision-making. Touch, smell, taste, sound, and the look of a merchandise all play an essential role in our perceptions, behaviour and consumption of a product. Understanding those roles provides a valuable advantage in today's marketplace.

Sensory marketing combines all of the senses into the marketing program. It's regarding capitalizing on what we know about our sensory hyperlinks to recall feelings and utilizing that information to enhance brands and improve sales.

Global Digital Scent Technology Market

The Global Digital Scent Technology market is predicted to be $0.13 billion in 2014 with CAGR of 32.02% and is set to achieve $1.2 billion by 2022. The Digital Scent Technology uses hardware devices like as e-nose and scent synthesizer to sense and produce various types of smells. Whereas, high cost is restricting the growth of market.

The challenges faced by the market are chemical substances used for smell generation may impact human health. Scent synthesizers use a cartridge to generate smells. The marketplace for e-noses is anticipated to grow at a high rate during the forecast period due to constant technological development and reducing cost.

Digital Signage Market

The digital signage market size was more than $14.9 billion for 2015. We estimate that Global Digital Signage Market share is set to increase at 5.2% CAGR from 2016 to 2023 impelled by the growing technological advancements and urbanized infrastructure.

Developing production and distribution of content through digital signage functions as an efficient marketing strategy for enterprises and is expected to push the digital signage market over the forecast period. This progress is attributed to the capability of the technology to provide fast and affordable means for advertising in comparison to the print media.

Breakthroughs in methods of display-panel production have generated a considerable drop in cost and are expected to positively affect digital signage market trends. Outdoor digital displays segment of the digital signage industry provide an available and a more attractive experience to customers in contrast to traditional static signage. It facilitates the firm to function and utilize money efficiently.

Additionally, it rewards the firms by helping them to focus on a specific audience and thus, enhance user experience. Content management systems form an essential part of the digital signage market ecosystem and allows users to control the content on their displays.

Content inventors (like IMS S.A.) are those marketing or advertising firms that create contents such as text messages, photos, visuals, and movies to make an effect on the targeted audience in order to keep them longer in the store or/and buy more items.

Sensory marketing market in Poland

Based on polish market data, there are > 500,000 service and retail outlets in Poland, whose business profile matches to the profile of current IMS customers. In several of them, there might be more than one subscription per location (eg. aroma, audio and video in one location). This indicates that the size of the Polish market is massive.

We expect the Group will speed up acquisition process, and show more rapid sales growth in domestic market. On the other hand, the acquisitions depends on willingness of retailers to offer sensory solutions to their customers. Should the retailers understand the benefits from sensory marketing, the Group revenue growth will accelerate at higher level.

We believe that, many polish food, beverage, health and beauty aide, retail, furniture and hotel brands will have come to realize that smell, taste, sound, feel, texture, visual image and packaging all combine in the brain may create indelible impressions and enhance experiences. This should come along with the advancements of wealth and life standard of polish society and need for more pleasures at places that they visit.

c. Summary of outlook

Our financial estimates for 2017E-2019E

Our estimates 2017E-2019E			
in PLNm	**2017E**	**2018E**	**2019E**
Net sales	48.4	53.5	58.6
EBITDA	13.4	15.6	18.1
EBITDA margin	**27.7%**	**29.1%**	**30.9%**
EBIT	9.4	11.5	13.7
EBIT margin	19.4%	21.4%	23.4%
Net income	7.2	8.8	10.5
Net margin	**14.8%**	**16.4%**	**18.0%**

Source: Group data, Dr. Kalliwoda International Research GmbH

Following strong 12M2016, and decent 1Q/2017, the 12M/2017 sales figures should not come as a surprise compared to the official forecast of the Group. Because of appealing enhancements of the business, we do expect the four quarters of 2017 to bring in increase in y-o-y sales and material y-o-y improvement of operating cash flows. We expect the Group to deliver good recurring results in 2017. Specifically, we are looking at approx. PLN 48m in sales for the group and PLN 7m of net income. We expect c. PLN 13.0m of consolidated EBITDA vs. c. PLN 10.9m of recurring EBITDA a year ago. We forecast a good bottom line level of PLN 7.2m.

Looking at the Group's perspectives, we get the feeling that the Group seems to be managed in the right direction. The Group focuses both on the top line improvement (acquisition of new markets, introducing new segments of business) and on the bottom line enhancement.

The bottom line enhancements plan assumes corporate changes that focuses on:

- Optimisation of logistics and sales process within the Group
- Optimisation of business segments – reduction of unprofitable segments
- Motivating the Management Board by shares buy-back program.

The steps undertaken by the Group allow to increase in productivity of labour and make assets utilisation higher. In results the corporate enhancements should generate substantial increase in profitability in 2017.

In our view total sales should constantly increase due to the growth in sensory marketing market and increase level of consumption spending in Poland. Although long-term margins trend might go downwards due to increase in competition, our study assumes strong, positive operating cash flows in 2017E - 2019E.

We see some risks to the 2017 financials of the Group such as: (i) PLN strengthening vs. USD or EUR negatively affecting the net margin on sales from other countries (currently 5%-10% of total output), (ii) Changes of respective laws and regulations in retail sector, (iii) risk of unsuccessful international expansion, (iv) pricing pressure – the Group place itself as a high quality provider of marketing sensory services, asking above-average rates for above-average functionality. While so far clients have been frequently agreeing, this cannot be taken for given going forward, should one of the competitors provide equivalent functionality at discount pricing, such development might make the Company reduce its tariffs, leading to decline in average rate per subscriber. We adjusted our estimates taking into account also more general risks of a.) global terrorist threat, with consequent potential decrease of traffic in shopping centres, and b.) the natural risk (due to high margins) of an increase in competition both in domestic and international markets.

On the other hand, the Polish economy expansion should positively affect the LFL sales development at consumer sentiment driven companies in the high-end part of the market. What's more, the corporate activity regarding searching for foreign subscriptions should position the Group very competitive to capture a hefty share of the European market in sensory marketing market. Although we may not see effects of this strategy in the short term, the Group has been growing as an international corporate in our view.

The company operates at highly growing market. We believe that only proper management may be able to utilize the good prospects due to the increasing competition emerging from all around the world. The current management proved that is capable to step by step increase market share while keep operating costs at reasonable level.

Obviously, looking at the future developments of the market, lower costs associated with operating at this market, will carry on to reduce entry barriers for potential network owners. However, just due to the fact considerably more organizations get commenced doesn't necessarily imply that more will be profitable in the long-term. In fact, we anticipate the percentage of successful network operators to decrease as more new firms jump in and then quickly make a termination. But one the other side of the coin, more new companies shows more innovation, more new and different business models, and ideally more pathways to success. We continue to see the strongest growth from new customers starting relatively small networks. But the next biggest growth area is from small- to medium-sized networks growing their existing operations. For all that, though, there are plenty of networks that have fallen by the wayside.

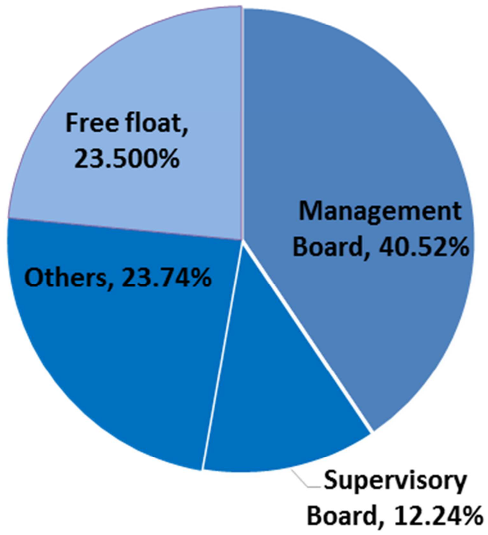
We initiate our favourable view of the Group because of its careful business attitude, low volatility of earnings and sales, balanced growth prospects and strong current efficiency. With a substantial fundamental upside to our 12M target price, we think the Group may offer an excellent value on top of a balanced business growth. Although we do not expect the Company to match the size of the largest players in Europe, we nevertheless consider the stock to be unfairly ignored by the investors. We also think the continuing activity at the M&As space confirms structural attractiveness of the industry per se, as well as, in our view a constantly deep discount for IMS's equities the market calls for is unjustified.

As a final sum-up, we see that there is a positive turnaround in the Group's business model and quality of management. In our opinion, the Group's sales growth, deliberate and well-knit long-term strategy, debt reduction, strong cash-flow along with the convincing growth in polish consumer spending are strong support for good direction of stable, organic development of the Group with proper sales management and cost structure on hand.

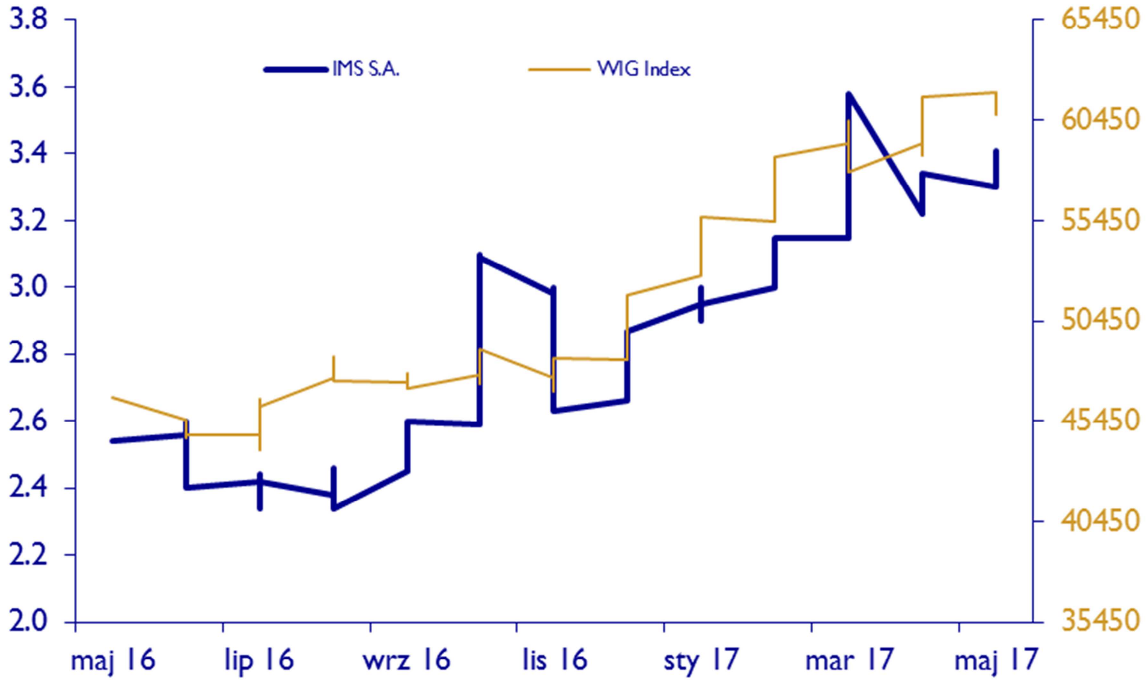
We initiate our coverage of IMS S.A. with a *Buy rating*.

5. Shareholder Structure and market price development

Shareholder Structure



Market price development (relative to WIG index)



Source: Group data, Dr. Kalliwoda International Research GmbH

6. Financials

Profit and loss statement

Profit and loss statement										
	Fiscal year									
in PLNm	2012	2013	2014	2015	2016	2017E	2018E	2019E	2020E	2021E
Revenues	**28.30**	**32.72**	**38.41**	**42.13**	**43.44**	**48.43**	**53.52**	**58.60**	**63.58**	**68.35**
Cost of goods sold	-25.94	-27.23	-31.49	-33.37	-35.76	-38.83	-41.83	-44.66	-48.70	-52.62
Gross profit	**2.36**	**5.49**	**6.92**	**8.76**	**7.68**	**9.60**	**11.68**	**13.94**	**14.88**	**15.74**
Other operating income	-0.13	-0.15	-0.32	-0.29	-0.27	-0.30	-0.33	-0.36	-0.39	-0.42
S&GA Costs	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Other operating expenses	-0.72	-0.46	-0.34	-0.22	-0.45	-0.50	-0.55	-0.61	-0.66	-0.71
EBITDA	**5.73**	**8.74**	**9.79**	**11.99**	**10.86**	**13.41**	**15.57**	**18.10**	**19.33**	**20.48**
Depreciation	-3.96	-3.56	-2.89	-3.16	-3.37	-4.02	-4.11	-4.41	-4.71	-5.04
Operating income	**1.77**	**5.18**	**6.90**	**8.83**	**7.49**	**9.40**	**11.46**	**13.69**	**14.61**	**15.45**
Net financial result	-0.74	-0.46	-0.19	-0.26	-0.38	-0.42	-0.47	-0.51	-0.55	-0.59
EBT	**1.03**	**4.73**	**6.71**	**8.57**	**7.11**	**8.98**	**10.99**	**13.18**	**14.06**	**14.85**
Income taxes	0.25	-1.00	-1.19	-1.73	-1.43	-1.80	-2.20	-2.64	-2.81	-2.97
Net income / loss	**1.28**	**3.72**	**5.52**	**6.85**	**5.69**	**7.18**	**8.79**	**10.55**	**11.25**	**11.88**
EPS	0.04	0.11	0.16	0.20	0.17	0.21	0.26	0.31	0.34	0.35
DPS	0.00	19.76	39.61	79.55	230.00	129.77	161.82	190.38	174.31	188.67
Change y-o-y										
Revenues		15.63%	17.36%	9.69%	3.11%	11.50%	10.50%	9.50%	8.50%	7.50%
Cost of goods sold		4.96%	15.63%	5.97%	7.17%	8.58%	7.74%	6.76%	9.04%	8.04%
Gross profit		133.01%	25.95%	26.60%	-12.34%	25.11%	21.67%	19.30%	6.76%	5.74%
Other operating income		19.38%	109.74%	-10.53%	-7.96%	11.50%	10.50%	9.50%	8.50%	7.50%
EBITDA		52.72%	11.99%	22.44%	-9.43%	23.55%	16.05%	16.28%	6.77%	5.99%
Depreciation		-9.99%	-18.85%	9.28%	6.59%	19.34%	2.33%	7.31%	6.87%	6.84%
Operating income		192.82%	33.17%	27.95%	-15.16%	25.44%	21.91%	19.50%	6.73%	5.71%
Net financial result		-37.94%	-58.30%	34.55%	47.08%	11.50%	10.50%	9.50%	8.50%	7.50%
EBT		357.85%	42.03%	27.76%	-17.03%	26.18%	22.45%	19.92%	6.66%	5.64%
Income taxes		-508.13%	18.92%	44.81%	-17.58%	25.99%	22.45%	19.92%	6.66%	5.64%
Net income / loss		191.16%	48.27%	24.07%	-16.89%	26.23%	22.45%	19.92%	6.66%	5.64%
EPS		191.16%	48.27%	24.07%	-16.89%	26.23%	22.45%	19.92%	6.66%	5.64%
Share in total sales										
Revenues	100.00 %	100.00 %	100.00 %	100.00 %	100.00 %	100.00 %	101.00 %	102.00 %	103.00 %	104.00 %
Cost of goods sold	-91.67 %	-83.22 %	-81.99 %	-79.21 %	-82.33 %	-80.17 %	-78.17 %	-76.21 %	-76.59 %	-76.98 %
Gross profit	8.33 %	16.78 %	18.01 %	20.79 %	17.67 %	19.83 %	21.83 %	23.79 %	23.41 %	23.02 %
Other operating income	-0.46 %	-0.47 %	-0.84 %	-0.69 %	-0.61 %	-0.61 %	-0.61 %	-0.61 %	-0.61 %	-0.61 %
S&GA Costs	0.00 %	0.00 %	0.00 %	0.00 %	0.00 %	0.00 %	0.00 %	0.00 %	0.00 %	0.00 %
Other operating expenses	-2.53 %	-1.41 %	-0.88 %	-0.51 %	-1.04 %	-1.04 %	-1.04 %	-1.04 %	-1.04 %	-1.04 %
EBITDA	20.23 %	26.72 %	25.49 %	28.46 %	24.99 %	27.70 %	29.09 %	30.89 %	30.39 %	29.97 %
Depreciation	-13.98 %	-10.88 %	-7.52 %	-7.49 %	-7.75 %	-8.29 %	-7.68 %	-7.52 %	-7.41 %	-7.37 %
Operating income	6.25 %	15.84 %	17.97 %	20.96 %	17.25 %	19.40 %	21.41 %	23.36 %	22.98 %	22.60 %
Net financial result	-2.61 %	-1.40 %	-0.50 %	-0.61 %	-0.87 %	-0.87 %	-0.87 %	-0.87 %	-0.87 %	-0.87 %
EBT	3.65 %	14.44 %	17.47 %	20.35 %	16.38 %	18.53 %	20.54 %	22.49 %	22.11 %	21.73 %
Income taxes	0.87 %	-3.07 %	-3.11 %	-4.10 %	-3.28 %	-3.71 %	-4.11 %	-4.50 %	-4.42 %	-4.35 %
Net income / loss	4.52 %	11.37 %	14.37 %	16.25 %	13.10 %	14.83 %	16.43 %	17.99 %	17.69 %	17.38 %

Source: Dr. Kalliwoda International Research GmbH

Equity Research DR. KALLIWODA | INTERNATIONAL RESEARCH GmbH Company Analysis

Balance sheet

Balance sheet								
	Fiscal year							
in PLNm	2012	2013	2014	2015	2016	2017E	2018E	2019E
Assets								
Cash and equivalents	2.5	5.3	8.8	5.3	6.9	7.6	8.4	9.2
Trade accounts and notes receivables	4.9	5.9	7.7	10.4	9.3	10.3	11.4	12.5
Inventories	1.2	1.5	1.5	1.7	2.1	2.3	2.6	2.8
Other current assets	0.3	0.5	0.4	0.4	1.0	1.2	1.3	1.4
Current assets, total	**8.9**	**13.2**	**18.4**	**17.9**	**19.2**	**21.5**	**23.7**	**26.0**
Property, plant and equipment	11.4	7.3	8.0	9.4	10.8	12.1	13.3	14.6
Intangibles	2.3	2.1	2.4	2.1	2.9	3.2	3.5	3.9
Long Term Investemnts	0.0	0.0	0.0	0.3	0.0	0.0	0.0	0.0
Other long-term assets	1.0	0.7	0.9	0.6	0.4	0.5	0.5	0.6
Non-current assets, total	**14.7**	**10.0**	**11.3**	**12.4**	**14.1**	**15.7**	**17.4**	**19.0**
Total assets	**23.6**	**23.3**	**29.7**	**30.3**	**33.4**	**37.2**	**41.1**	**45.0**
Liabilities								
Trade payables	1.9	2.0	4.1	4.7	4.8	5.4	5.9	6.5
Short-term financial debt	3.7	1.9	1.5	0.2	0.0	0.0	0.0	0.0
Short-term leasing	2.2	1.4	1.3	1.5	2.0	2.2	2.4	2.6
Other short-term liabilities	1.52	2.71	2.73	3.38	2.01	2.24	2.48	2.71
Current liabilities, total	**9.2**	**8.0**	**9.6**	**9.8**	**8.8**	**9.8**	**10.8**	**11.8**
Long-term financial debt	2.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Long-term leasing	1.1	0.9	2.0	3.5	5.2	5.8	6.4	7.0
Other short-term liabilities	1.0	0.6	0.8	0.4	0.6	0.6	0.7	0.8
Long-term liabilities, total	**4.2**	**1.6**	**2.8**	**3.9**	**5.8**	**6.4**	**7.1**	**7.8**
Total liabilities	**13.5**	**9.6**	**12.4**	**13.7**	**14.5**	**16.2**	**17.9**	**19.6**
Shareholders equity, total	**10.1**	**13.7**	**17.4**	**16.6**	**18.8**	**21.0**	**23.2**	**25.4**
Minority interests	-0.5	0.0	0.0	0.0	-0.1	-0.1	-0.1	-0.1
Total liabilities and equity	**23.6**	**23.3**	**29.7**	**30.3**	**33.4**	**37.2**	**41.1**	**45.0**

Source: Dr. Kalliwoda International Research GmbH

Equity Research DR. KALLIWODA | INTERNATIONAL RESEARCH GmbH Company Analysis

Cash flow statement

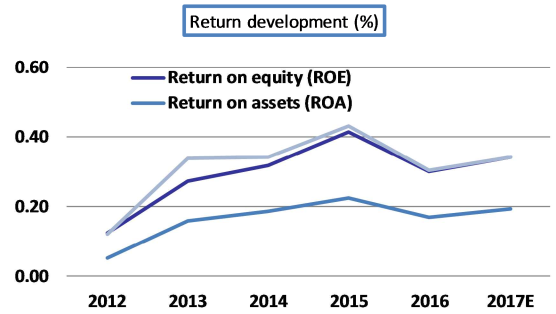
Cash flow statement								
	Fiscal year							
in PLNm	2012	2013	2014	2015	2016	2017E	2018E	2019E
Net income / loss	1.3	3.7	5.5	6.8	5.7	7.2	8.8	10.5
Depreciation	4.0	3.6	2.9	3.2	3.4	4.0	4.1	4.4
Others	0.1	0.8	0.8	-1.7	0.2	-0.8	-0.8	-0.8
Net operating cash flow	**5.4**	**8.1**	**9.2**	**8.3**	**9.2**	**10.4**	**12.1**	**14.2**
Cash flow from investing	**-3.6**	**-2.2**	**-4.6**	**-0.9**	**-1.2**	**-2.5**	**-2.6**	**-2.0**
Free cash flow	1.8	5.9	4.6	7.4	8.0	7.9	9.6	12.2
Cash flow from financing	**-1.6**	**-3.1**	**-1.1**	**-10.9**	**-6.9**	**-6.1**	**-6.9**	**-8.4**
Change of cash	0.2	2.8	3.5	-3.5	1.1	1.9	2.7	3.8
Cash at the beginning of the period	2.3	2.5	5.3	8.8	5.3	6.9	7.6	8.4
Others	0.0	0.0	0.0	0.0	0.4	-1.1	-1.9	-3.0
Cash at the end of the period	2.5	5.3	8.8	5.3	6.9	7.6	8.4	9.2

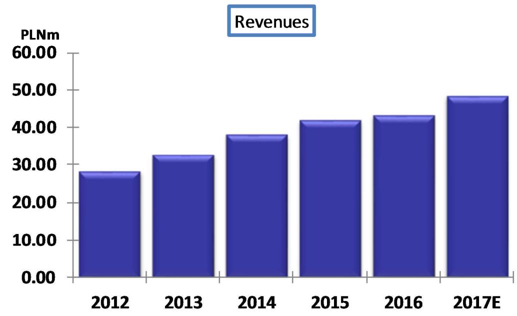
Source: Dr. Kalliwoda International Research GmbH

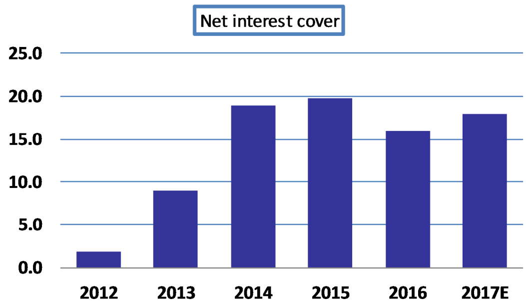
Financial ratios

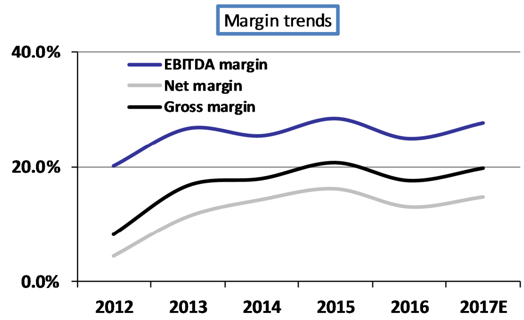
Fiscal year	2012	2013	2014	2015	2016	2017E	2018E	2019E
Gross margin	8.3%	16.8%	18.0%	20.8%	17.7%	19.8%	21.8%	23.8%
EBITDA margin	20.2%	26.7%	25.5%	28.5%	25.0%	27.7%	29.1%	30.9%
EBIT margin	6.3%	15.8%	18.0%	21.0%	17.2%	19.4%	21.4%	23.4%
Net margin	4.5%	11.4%	14.4%	16.2%	13.1%	14.8%	16.4%	18.0%
Return on equity (ROE)	12.6%	27.2%	31.8%	41.3%	30.2%	34.2%	37.9%	41.5%
Return on assets (ROA)	5.4%	16.0%	18.5%	22.6%	17.1%	19.3%	21.4%	23.4%
Return on capital employed (ROCE)	12.3%	34.0%	34.2%	43.1%	30.5%	34.3%	37.8%	41.3%
Equity ratio	132.8%	69.8%	71.4%	82.6%	77.2%	77.2%	77.2%	77.2%
Current ratio	1.0	1.7	1.9	1.8	2.2	2.2	2.2	2.2
Quick ratio	0.27	0.66	0.92	0.54	0.78	0.78	0.78	0.78
Net interest cover	1.9	9.0	19.0	19.8	16.0	18.0	19.9	21.7
Net debt/EBITDA	0.59	-0.39	-0.75	-0.43	-0.63	-0.57	-0.54	-0.51
Tangible BVPS	439.82	299.28	338.45	369.37	421.37	469.83	519.16	568.48
CAPEX/Sales	12.77%	7.13%	11.74%	1.93%	3.03%	3.10%	2.33%	0.57%
Working capital/Sales	-1.3%	16.0%	23.0%	19.3%	24.1%	24.1%	24.1%	24.1%
EV/Sales	3.70	3.20	2.73	2.49	2.41	2.16	1.96	1.79
EV/EBITDA	18.31	11.99	10.71	8.74	9.66	7.82	6.73	5.79
EV/EBIT	59.23	20.23	15.19	11.87	13.99	11.15	9.15	7.66
P/Tangible BVPS	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01
P/E	89.12	30.61	20.65	16.64	20.02	15.86	12.95	10.80

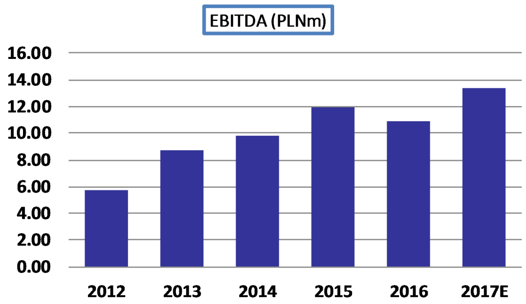
Source: Dr. Kalliwoda International Research GmbH

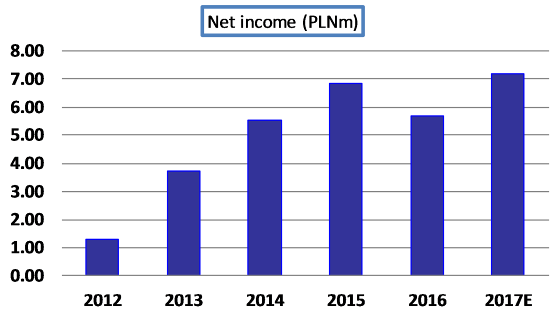


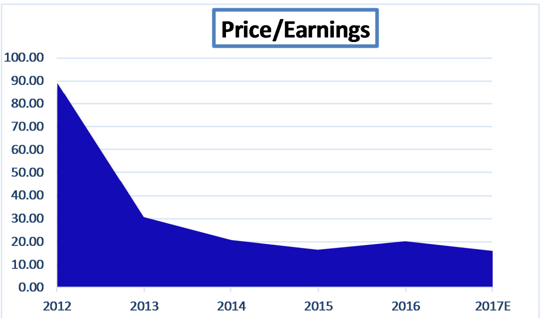


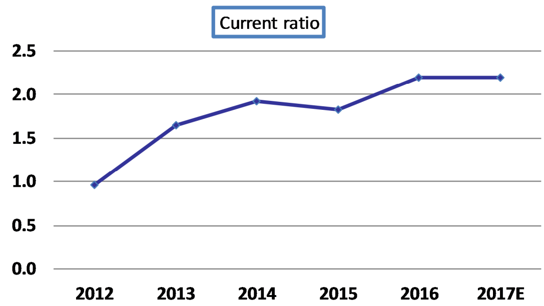












Source: Dr. Kalliwoda International Research GmbH

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3. Date of first publication of this document: 30th of May 2017

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