

Polyus

Company update

- Polyus (PLZL) presented its strategy and operational update.** The company reported its FY17 results on 15 February and presented an operational update on the Capital markets day on 20 March 2018. In 2017, the gold sales increased by 12.7% YoY to 2,158 koz. The gold production increased 10% YoY to 2,160 koz. Revenue increased 10.7% YoY to \$2,721mn in FY17 compared to \$2,548mn in FY16. Polyus total cash cost (TCC) decreased to \$364/oz in FY17 from \$389/oz in FY16. AISC increased to \$621/oz, up 9% YoY. The company reported adjusted EBITDA at \$1,702 mn, up 11% YoY in FY17. The key driver of the operating profitability growth was higher gold sales volumes and lower TCC, despite 13% ruble appreciation during 2017. Adjusted EBITDA margin reached 63% in 2017 compared to 62% in 2016. Net profit of the company decreased from \$1,445mn in FY16 to \$1,241mn in FY17, affected by lower foreign exchange gains and higher financial costs. Capex was \$804mn, mostly driven by Natalka construction. The company's Net debt decreased to \$3,077mn at the end of 2017 from \$3,241mn at the end of 2016. Net debt/EBITDA was 1.8x at the end of 2017. Polyus increased the number of independent directors in the Board to four out of total nine, assuming to meet high corporate governance standards. The dividend policy now targets semi-annual payments at the level of 30% of EBITDA if threshold Net debt/EBITDA less than 2.5x, but not less than \$550mn for FY17 and FY18, and 30% of EBITDA post-2018.
- The completion of main investment projects will drive the production growth during 2018-2019.** Polyus provided update on its project pipeline. The company completed Olimpiada Mill-1 reconfiguration in 2016, expansion at Blagodatnoye mill (stage 1), Kuranakh Mill (stage 1 and 2), Verninskoye (stage 1 and 2) in 2017, BIO-4 at Olimpiada complex is scheduled for 1Q18. Those expansions shall bring additional 370koz gold capacity. Natalka ramp-up shall be completed in 3Q18. New projects include antimony project at Olimpiada for 2018, Olimpiada mills expansion in 2018-2020, Kuranakh mill expansion (2018-2019), and completion of stage 3 at Verninskoye in 2018. The heapleaching at Blagodatnoye postponed. Polyus' engineering team is very positive on its proprietary BIO-oxidation technology implemented at Olimpiada and plans further increase BIO processing capacities. Antimony, another project of Polyus, is targeting up to 16% of the global antimony production once realized. Antimony is a minor metal used in fire-retardant materials, battery production, aircraft manufacturing and other industries. The global antimony mine supply was 82kt in 2017, dominated by China. Polyus controls c 5% of antimony global reserves and plans antimony brownfield project at Olimpiada.
- Polyus high production growth profile might be partially compromised by higher TCC and higher capex in the next two years.** The company's TCC forecast of \$550-600/oz at Natalka compared to \$364/oz for the group brings higher the company's TCC forecast: to \$425/oz in 2018 and to \$450/oz in 2019. Natalka plans ramp-up during 2018 to bring the commercial volumes by the end of the year. The company also provided higher capex guidance for 2018-2020 compared to our forecast. The capex is planned at \$850mn in FY18, and \$650mn in FY19. The total gold production guidance is 2.375-2.425 moz in FY18 and 2.8moz in each FY19 and FY20. The company may pay over \$500mn dividends for shareholders in the next two years, delivering 5%+ dividend yield based on the current MarketCap. We updated our forecasts based on company's guidance and latest results. We change our 12-month target price from \$53/DR to \$49/DR, based on new capex and TCC guidelines. We reiterate Buy rating. We believe the low free float (16%) and exposure to political risk (the major holder Mr. Said Kerimov is representative of Mr. Suleyman Kerimov family) will not allow the company to get over the discount to its global peers in near term.

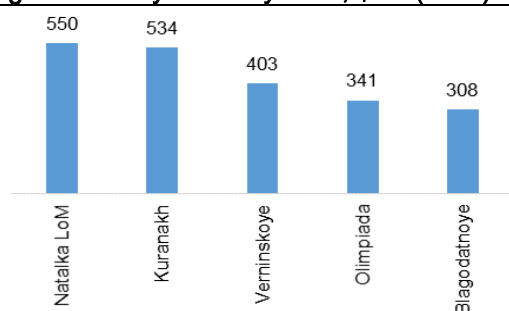
Report date:	23 March 2017
Main exchange	MOEX/LSE
Rating	BUY
Current Price, \$	39
12M Target price, \$	49
Current MCap, \$ mn	10,421
Free float, %	16%

Description:

Polyus is the leading Russian gold producer with long-life high-quality resource base. The company explores several production deposits in Russia, including world-class resources at Olimpiada, Natalka and Sukhoi Log. The stock trade on Moscow Exchange and LSE.

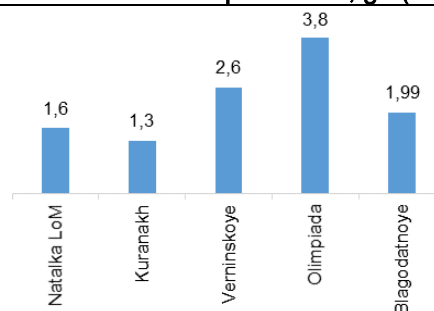
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Figure 1. Polyus TCC by mine, \$/oz (2017)



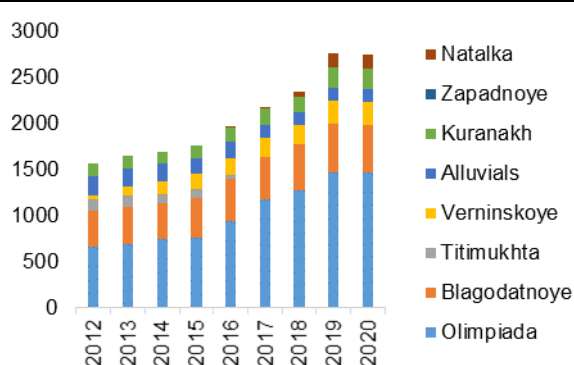
Source: Company data

Figure 2. Grade in ore processed, g/t (2017)



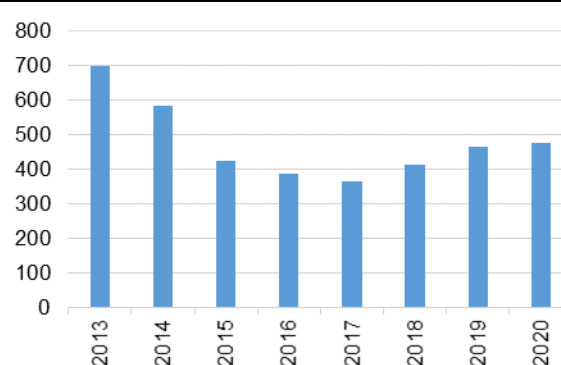
Source: Company data

Figure 3. Polyus gold production by mine, koz



Source: Company data, Hypothesis Research estimates

Figure 4. Polyus TCC dynamics, \$/oz



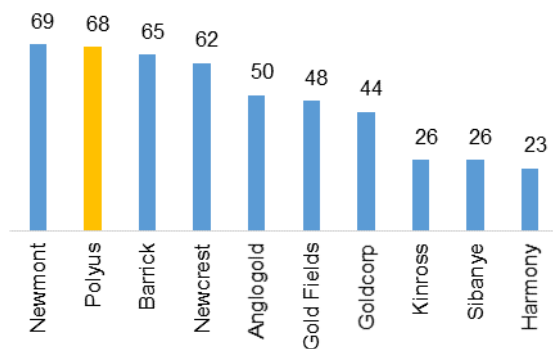
Source: Company data, Hypothesis Research estimates

Figure 5. Comparable multiples for the gold sector

Company	MktCap, \$mn	EV, \$mn	P/E Fwd 1Y	P/E Fwd 2Y	P/E Fwd 3Y	EV/ EBITDA 1Y fwd	EV/ EBITDA 2Y fwd	EV/ EBITDA 3 fwd	EV/ Sales 1y fwd	EV/ Sales 2y fwd	EV/ Sales 3y fwd
Polymetal	4428	6010	10,4	8,3	7,0	7,3	6,3	5,3	3,0	2,6	2,4
Polyus	10379	13569	7,5	6,3	6,5	7,4	5,9	5,7	4,5	3,6	3,4
Alrosa	12066	13563	7,7	7,6	7,5	6,0	6,0	6,0	2,8	2,8	2,7
Gold Fields	3361	4791	21,3	15,0	12,1	3,8	3,2	3,4	1,7	1,5	1,5
Norilsk Nickel	30412	38925	8,7	8,9	9,2	6,8	6,9	6,4	3,4	3,4	3,2
Sibanye Gold	2106	4415	9,7	7,3	5,4	4,4	3,9	3,3	1,0	1,0	0,9
Barrick Gold	14165	20135	15,4	16,5	18,6	5,4	5,8	6,0	2,5	2,6	2,7
Agnico Eagle Mines	9329	9920	59,0	39,2	26,2	11,4	9,7	7,7	4,6	4,2	3,5
AngloGold Ashanti	3991	6087	11,8	9,9	8,2	3,8	3,9	3,4	1,4	1,4	1,4
Goldcorp	11484	14184	29,9	17,9	16,8	8,3	6,0	5,8	4,0	3,1	3,1
Kinross Gold	4501	5244	20,4	18,1	24,0	4,3	4,1	4,0	1,6	1,6	1,6
Newmont Mining	20064	21829	26,7	23,5	24,2	8,3	7,9	8,2	2,9	2,9	3,0
Yamana Gold	2559	4474	27,3	19,3	14,7	5,6	5,5	5,4	2,3	2,1	2,2
IAMGOLD	2408	2068	55,6	38,4	24,8	5,3	4,9	4,0	1,8	1,7	1,5
Newcrest Mining	11722	13230	38,7	16,0	14,5	10,4	7,0	6,7	3,9	3,2	3,1
Randgold Resources	7882	7250	23,3	22,5	22,5	10,2	10,1	10,0	5,5	5,4	5,4
Shandong Gold Mining	8548	10117	35,1	28,2	20,7	13,0	11,6	10,0	1,2	1,2	1,2
Zhongjin Gold Corp	5091	7538	74,7	60,7	58,5	14,8	15,4	16,2	1,3	1,3	1,4
Freeport-McMoRan	26173	38162	8,5	12,4	9,5	4,7	6,3	5,1	2,0	2,3	2,1
Fresnillo	12042	12059	23,3	21,6	17,7	9,6	8,8	7,8	5,0	4,7	4,2
Kaz Minerals	5455	7514	8,3	7,8	7,3	5,3	5,1	5,3	3,3	3,2	3,1
Boliden	9530	9790	10,1	10,6	11,4	5,5	5,6	5,8	1,6	1,5	1,5
Global peer average			27,1	21,3	19,5	7,9	7,4	7,0	2,8	2,7	2,6
Russian peer average			10,9	10,2	11,8	6,1	5,7	5,5	3,1	2,8	2,7
Polyus (discount)/premium to global peers			-72%	-70%	-66%	-7%	-19%	-19%	59%	33%	30%
Polyus (discount)/premium to Russian peers			-31%	-38%	-45%	21%	4%	3%	46%	26%	24%

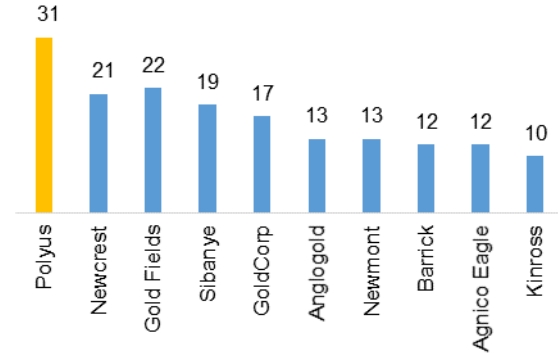
Source: Thomson Reuters

Figure 6. The largest gold reserves base, moz



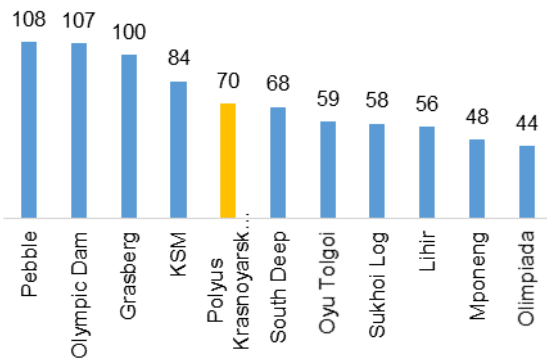
Source: Polyus, companies reports

Figure 7. Life of mines, years



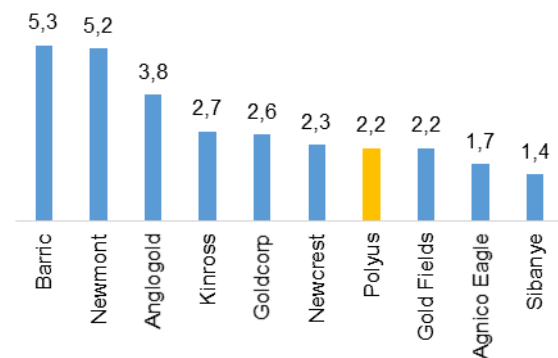
Source: Polyus, companies, reports

Figure 8. Largest gold assets by resources, moz



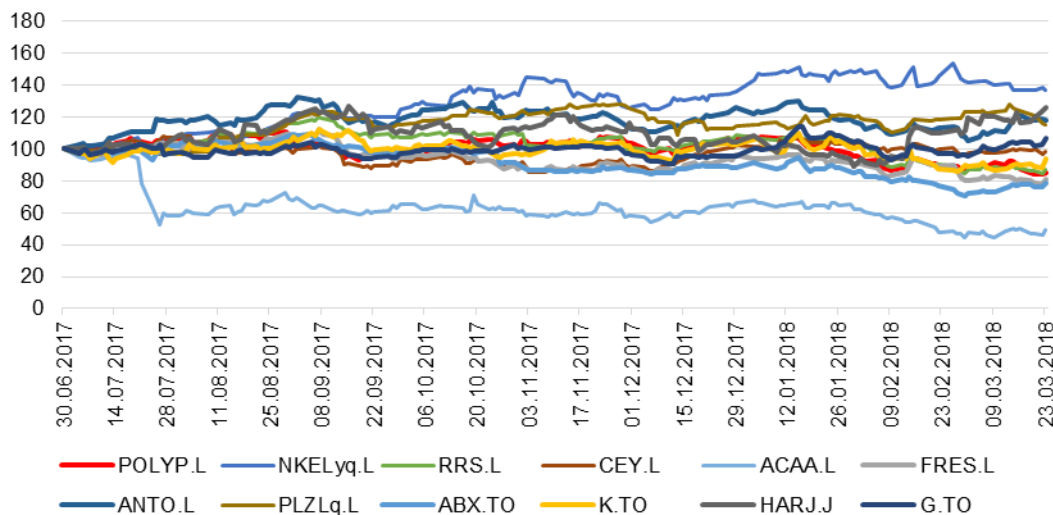
Source: Polyus, companies reports

Figure 9. Largest gold producers (2017), moz



Source: Polyus, companies, reports

Figure 10. The largest gold reserves base, moz



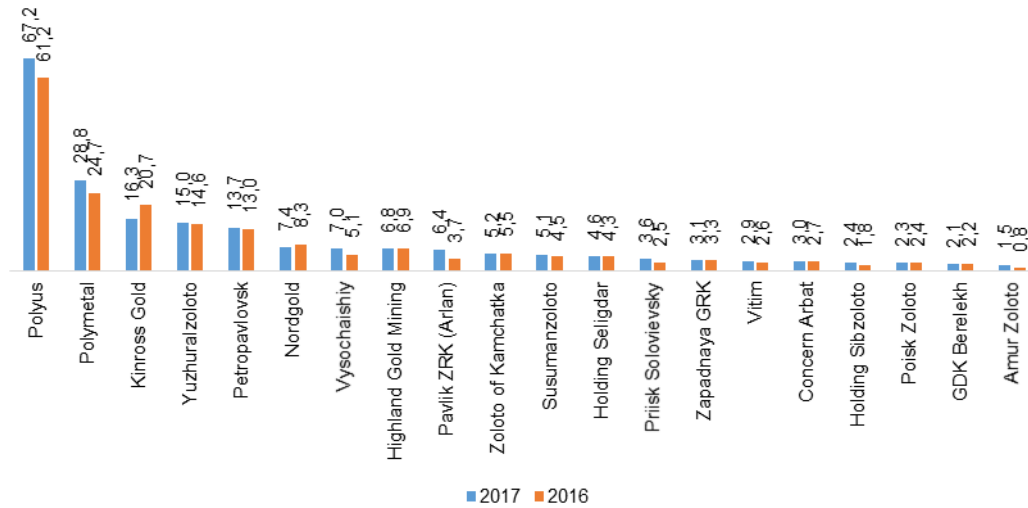
Source: Thomson Reuters

Figure 11. Polyus financial statistics

Income statement						Statements of cash flows					
\$mn	FY15	FY16	FY17	FY18	FY19	\$mn	FY15	FY16	FY17	FY18	FY19
Revenue	2188	2458	2721	3087	3702	Net cash generated by operating activities	1103	1178	1292	1338	1506
Cost of gold sales	-901	-919	-1000	-1236	-1583	Net cash used in investing activities	-688	-280	-618	-822	-622
Gross profit	1287	1539	1721	1851	2119	Net cash generated by financing activities	220	-1015	-1224	-884	-923
General, administrative and selling expenses	-143	-151	-211	-187	-225	Net (decrease)/increase in cash and cash equivalents	635	-117	-550	-368	-39
Other expenses	20	-27	-55	-62	-75	Cash and cash equivalents BOP	1213	1825	1740	1204	836
Reversal of Impairment /(impairment losses)	0	0	0	0	0	Effect of foreign exchange rate changes on cash and cash equivalents	-35	32	14	0	0
Operating profit	1164	1361	1455	1601	1819	Cash and cash equivalents EOP	1825	1740	1204	836	797
Foreign exchange loss, net	149	396	130	0	0	Capex	268	468	804	850	650
Change in fair value of derivative financial instruments	-125	119	118	0	0	Dividends					
Finance income	69	40	28	28	28	Dividend payout	0	340	550	550	515
Finance costs	-45	-145	-200	-125	-130	EBITDA	1292	1509	1633	1836	2081
Profit/Loss before income tax	1212	1771	1531	1504	1717	Net debt	364	3241	3077	3633	3384
Income tax expense	-191	-326	-290	-319	-363						
Profit/Loss from continuing operations	1021	1445	1241	1185	1355						
Balance sheets						Ratios					
USD mn	FY15	FY16	FY17	FY18	FY19		FY15	FY16	FY17	FY18	FY19
Property, plant and equipment, net	2023	2938	4005	4620	5009	Gross margin, %	59%	63%	63%	60%	57%
Derivative financial instruments and investments	411	57	38	38	38	Operating margin, %	53%	55%	53%	52%	49%
Inventories	184	264	300	371	475	Net margin, %	-6%	5%	4%	0%	0%
Deferred tax asset	46	75	60	68	82	Revenue growth	-2%	12%	11%	13%	20%
Other non-current assets	8	37	155	192	245	Net profit growth		42%	-14%	-4%	14%
Total non-current assets	2672	3371	4558	5289	5849	EBITDA growth	26%	17%	8%	12%	13%
Total current assets	2438	2295	1889	1669	1852	Capex growth, %		75%	72%	6%	-24%
Total assets	5110	5666	6447	6958	7700	Payout ratio	0%	24%	44%	46%	46%
Total current liabilities	218	598	417	1077	1391	EBITDA / Interest coverage	28,7	10,4	8,2	14,7	16,0
Borrowings	2151	4698	4269	3881	3402	Net debt/EBITDA	0,3	2,1	1,9	2,0	1,6
Derivative financial instruments	509	456	448	448	448	Net debt/Equity	0,2	-7,8	4,7	3,0	1,7
Deferred tax liability	133	182	217	246	295	Revenues/Assets	0,4	0,4	0,4	0,4	0,5
Other non-current liabilities	20	32	45	56	72	Capex/ EBITDA	0,2	0,3	0,5	0,5	0,3
Total non-current liabilities	2845	5482	5374	4680	4269	RoCE	23,8%	26,9%	24,1%	27,2%	28,8%
Total liabilities	3063	6080	5791	5757	5660	FCF yield	8,0%	6,8%	4,7%	4,7%	8,2%
Total equity	2047	-414	656	1201	2041	RoIC	30%	26%	22%	21%	21%
Total liabilities and equity	5110	5666	6447	6958	7700	ROE	50%	-349%	189%	99%	66%

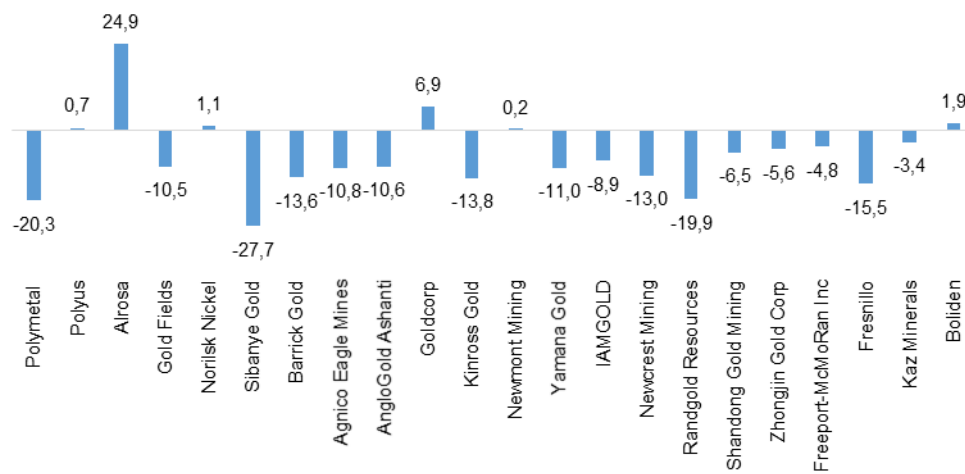
Source: Company data, Hypothesis Research estimates

Figure 12. Top-20 gold producers in Russia (73% of total output from mineral feedstock), t



Source: Association of gold producers of Russia

Figure 13. YTD performance of gold stocks



Source: Thomson Reuters

Important disclosures

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