COMPANY UPDATE

Transport Trade Services SA

Buy

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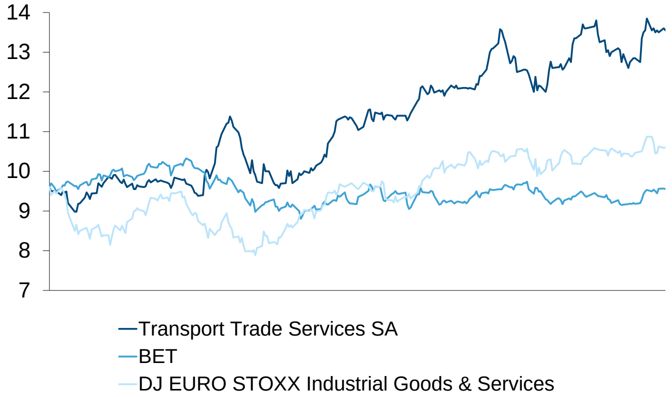
Share price (RON) close as of 30/05/2023	13.6	Reuters	TTS.BX	Free float	67.7%
Number of shares (mn)	60.0	Bloomberg	TTS RO	Shareholders	
Market capitalization (RON mn / EUR mn)	813 / 164	Div. Ex-date	24/05/22		
Enterprise value (RON mn / EUR mn)	879 / 177	**Target price**	**16.6**	Homepage:	https://www.tts-group.ro

Key figures Overview

RON mn	2021	2022	2023e	2024e
Net sales	598.8	934.4	1,504.6	883.4
EBITDA	141.5	283.4	310.3	182.2
EBIT	79.9	210.5	234.0	95.4
EBT	78.9	208.7	235.0	95.0
Net profit	66.4	179.0	197.4	79.8
EPS (RON)	1.11	2.98	3.29	1.33
CEPS (RON)	1.45	-0.09	0.72	0.25
BVPS (RON)	11.04	13.64	15.86	16.78
Dividend/Share (RON)	0.30	0.55	1.32	0.53
EV/EBITDA (x)	10.27	2.56	2.83	4.46
P/E (x)	20.15	3.84	4.12	10.19
P/CE (x)	15.36	-131.68	18.79	55.18
Dividend yield (%)	1.33	4.80	9.71	3.92
EBITDA margin (%)	23.63	30.33	20.62	20.62
Operating margin (%)	13.34	22.53	15.55	10.80
Net profit margin (%)	11.09	19.16	13.12	9.03

Trading data & Statistics

Daily averages	5 days	30 days	last year
Volume	9,921	36,902	26,970
Trading value (RON mn)	0.1	0.5	0.3



Price performance:	1M	3M	6M	12M
in EUR	3.5%	5.2%	22.0%	40.5%

Financial Strength

	2021	2022	2023e	2024e
ROE (%)	12.58	28.46	25.94	9.45
ROCE (%)	10.25	24.96	23.33	8.85
Equity ratio (%)	83.13	81.43	80.32	87.74
Net debt (RON mn)	9.21	-78.24	-65.45	-139.83
Gearing (%)	1.39	-9.56	-6.88	-13.89

1Q23 results: "Carry and cash"

On the back of recent results and prospects for the year, and admittedly considering a worst-case scenario for our valuation, we can still find ample upside in the stock and **maintain our BUY recommendation while increasing our target price to RON16.65/share**.

The 1Q23 results posted by TTS reinforce our positive stance on the company's shares and create a new base for our projections, even in a considered worst-case scenario.

While reviewing the exceptional results posted for the first quarter of the year, we are also attempting to test the resilience of our forecast and the company's ability to withstand a downturn in business that may or not come, on the back of changes in the economic and political environment of the region.

The results are not surprising and attest to the capability of management to adapt to an evolving universe and create a solid base from which to operate and expand. With a favorable tariff environment, especially in the agricultural product segment, profitability thrives and contributes to valuation. However, even under a worst-case scenario, with minimal volume growth and a dramatic drop in tariffs, TTS valuation still shows considerable upside potential, on the back of operating cash flow generation and current CAPEX levels. Subsequent strong quarterly results, showing volume and price resilience, would prompt us to revise our target price upwards, and start accounting for more than a worst-case scenario and more of the full potential of the company.

An exceptionally profitable first quarter

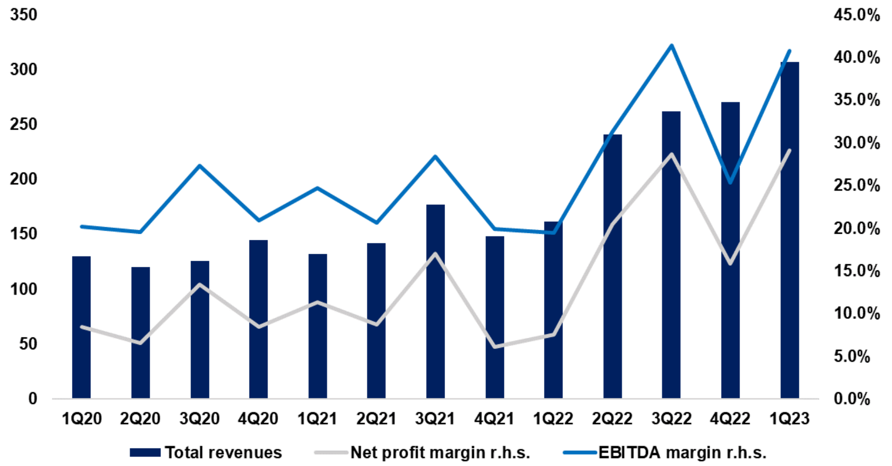
TTS published 1Q23 results that show significant growth in top and bottom line and exceptional margins. The top line advanced about 90% compared to that of 1Q22, reaching over RON300mn, vs the RON162mn of the first quarter of last year. At the same time, operating profit grew more than six times, registering RON104mn, compared to RON16mn during 1Q22. Net profit recorded a similar advance, reaching RON89mn vs the RON12mn of the similar period of last year.

(mn. RON)	1Q23	1Q22	*chng.*	4Q22	*chng.*	1Q21	*chng.*
Total revenues	**306.5**	**161.7**	***89.5%***	**270.4**	***13.4%***	**144.4**	***112.3%***
Materials	-31.2	-27.2	*14.7%*	-32.8	*-4.9%*	-15.4	***102.6%***
COGS	-8.6	-9.1	*-5.5%*	-6.1	*41.0%*	-7.3	***17.8%***
Depreciation	-21	-15.9	*32.1%*	-20.8	*1.0%*	-14.1	***48.9%***
Subcontr.	-96.4	-62.2	*55.0%*	-100.2	*-3.8%*	-51.5	***87.2%***
Wages	-40.3	-26.2	*53.8%*	-41.2	*-2.2%*	-26.4	***52.7%***
Other exp.	-10.4	-12.1	*-14.0%*	-12.7	*-18.1%*	-9.2	***13.0%***
Gains/losses	5.4	6.6	*-18.2%*	-9	*-160.0%*	-4.3	***-225.6%***
Operating expenses	**-202.5**	**-146.1**	***38.6%***	**-222.8**	***-9.1%***	**-128.2**	***58.0%***
Operating profit	**104**	**15.6**	***566.7%***	**47.6**	***118.5%***	**16.2**	***542.0%***
Fin. Rev.	0.9	-0.3	*-400.0%*	0.2	*350.0%*	-0.5	***-280.0%***
Fin. Costs	0.2	-0.7	*-128.6%*	-0.2	*-200.0%*	-0.5	***-140.0%***
Net fin.	**1.1**	**-1**	***-210.0%***	**0.00**		**-1**	***-210.0%***
PBT	**105.1**	**14.6**	***619.9%***	**47.6**	***120.8%***	**15.2**	***591.4%***
Tax	-16	-2.4	*566.7%*	-4.9	*226.5%*	-2.5	***540.0%***
Net Income	**89.1**	**12.2**	***630.3%***	**42.7**	***108.7%***	**12.7**	***601.6%***
Net margin	*29.1%*	*7.5%*		*15.8%*		*8.8%*	
EBITDA	**125**	**31.5**	***296.8%***	**68.4**	***82.7%***	**30.3**	***312.5%***
EBITDA margin	*40.8%*	*19.5%*		*25.3%*		*21.0%*	

Source: Company data, Erste Group Research

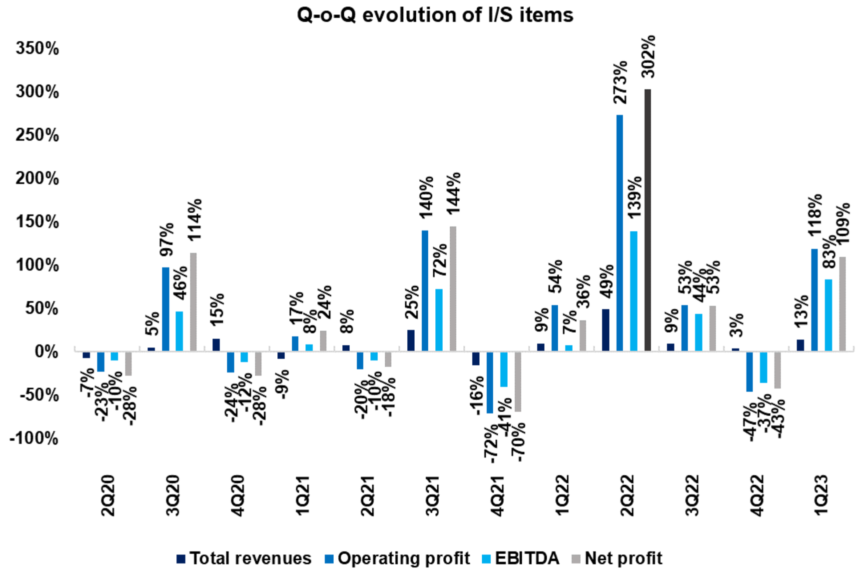
On a quarterly basis, the company posted a 13% top line growth, q-o-q, with more than double operating income and net profit and an EBITDA growth of 83%.

Revenues and profitability (RON, mn, %)



Source: Company data, Erste Group Research

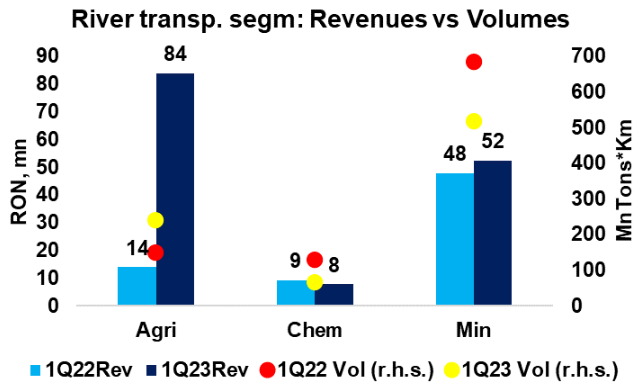
Profitability wise, the figures were equally impressive, with an EBITDA margin of 41% and a net profit margin of 29%, reaching in the same range as the very profitable 3Q22. Actually, the first three months of 2023 were not only the most profitable first quarter recorded by the company, but also the one with the highest consolidated revenues.

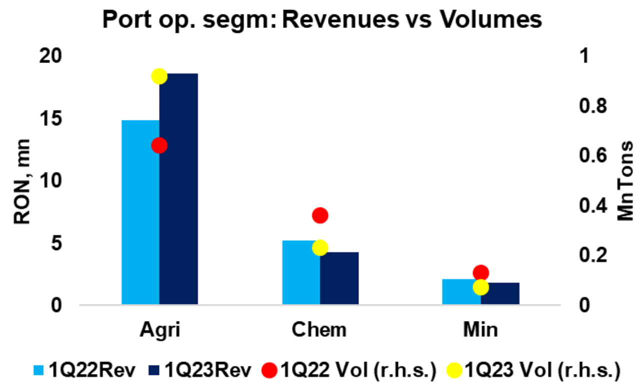


Source: Company data, Erste Group Research

Revenues: agricultural products bounty

During the first quarter of the year, the main driver for the exceptional top line and profitability was the flow of agricultural products, on the back of the reconfiguration of flows related to the war in the Ukraine. Thus, on a yearly basis, the volumes transported by the river fleet of TTS have increased by about 60% in terms of bnTons*km, reaching 0.238bnTons*km vs the 0.149bnTons*km recorded during the first quarter of last year. In terms of port operations, the flow of agricultural products was also increased by 44%, reaching 0.94mn tons, compared to the 0.64mn tons of 1Q22. These are the figures representing only the volumes operated inhouse, without taking into consideration what the forwarding segment contracted with third parties.





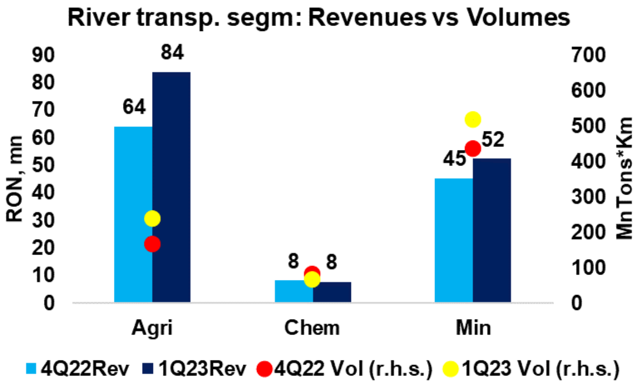
Source: Company data, Erste Group Research

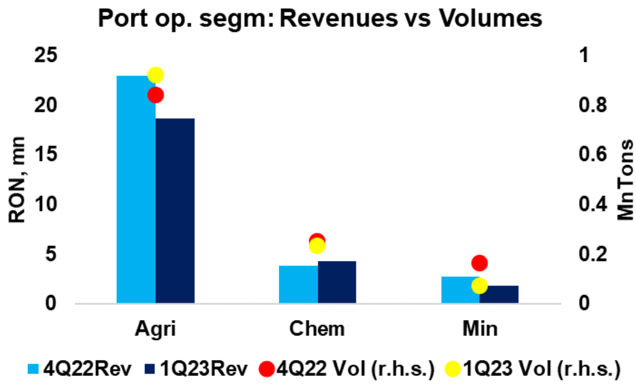
At the same time, the company recorded significant retreats in the volumes transported and operated in chemical and mineral goods. The transport of chemical goods has declined by almost 49% reaching 0.065bnTons*km vs. 0.127bnTons*km in 1Q22 and port operations in the same segment declined by 36% to 0.23mn tons. A similar picture was present in the minerals segment, with a contraction of 25% y-o-y in freight, reaching

0.516bnTons*km during 1Q23 vs. 0.683bnTons*km in 1Q22. Port operated volumes in the minerals segment also declined by 46% reaching 0.07mn tons.

On the back of these changes in flows, it was only natural for revenues to follow. The company managed to exploit adequately the logistics situation and capitalized on the explosive growth of demand with matching tariffs. Thus, on a 44% jump in freight, in the agricultural segment, revenues increased more than six times in the river transportation business. In port operations, the revenue growth followed the escalation of volumes, with showing a 25% increase in receipts. In chemical products, revenues declined in river transport and port operations, in line with the decrease in volumes. The exception was registered in the revenues posted by river transport of mineral products where a 46% drop in freight translated into an actual 10% jump in revenues.

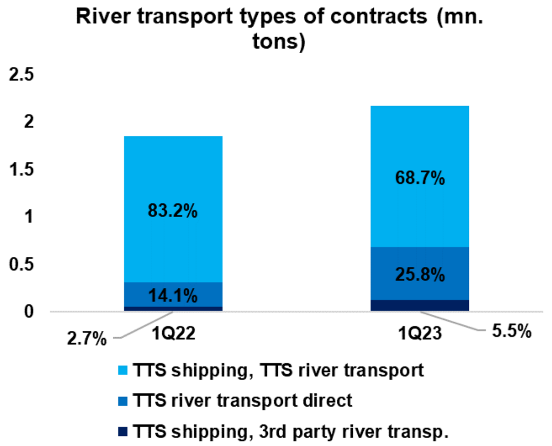
On a quarterly basis, the picture progressed along the same lines, however on a more subdued scale. A q-o-q 44% jump in agricultural river transportation freight was accompanied by a 31% increase in revenues, showing average tariffs on a marginal slide, according to our calculation by -9%. A slight retraction in tariffs on the river transport of minerals (-3%) was compensated by the 19% higher freight (bnTons*km) and resulted in 15% higher revenues. In the chemical river transportation segment, volumes in terms of freight declined by 21%, leading to a 7% drop in revenues.

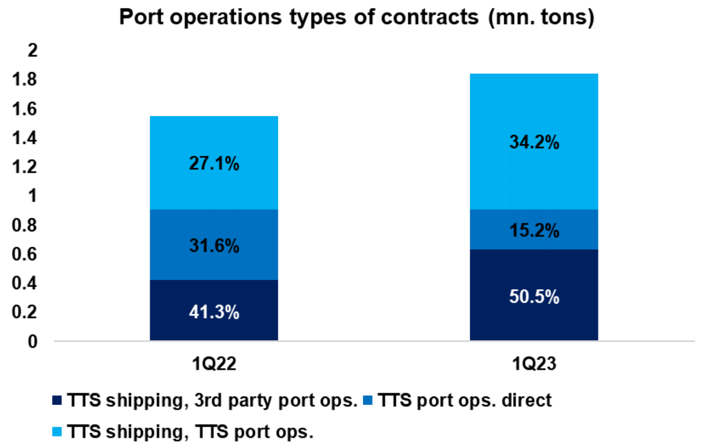




Source: Company data, Erste Group Research

In port operations, on a quarterly basis, agricultural products registered a 10% in volumes, however a 19% drop in revenues. On the same basis, chemicals saw a 8% decline in volumes, but a 12% jump in prices while minerals saw volumes declining by half, followed by a 32% depreciation of receipts.





Source: Company data, Erste Group Research

The structure of contracts also shifted with a higher proportion of overall contracts being performed by river transport segment. It grew from about 14% during the first quarter of 2022 to almost 26% in 1Q23. This led to a shrinking of the share of inhouse river transport volumes contracted, from 83% in 1Q22 to 69% in 1Q23. In the port operations segment, the picture is somewhat different with the share of direct contracts dropping by half y-o-y to 15%, while third party contracts' share growing to 50% of total port operations.

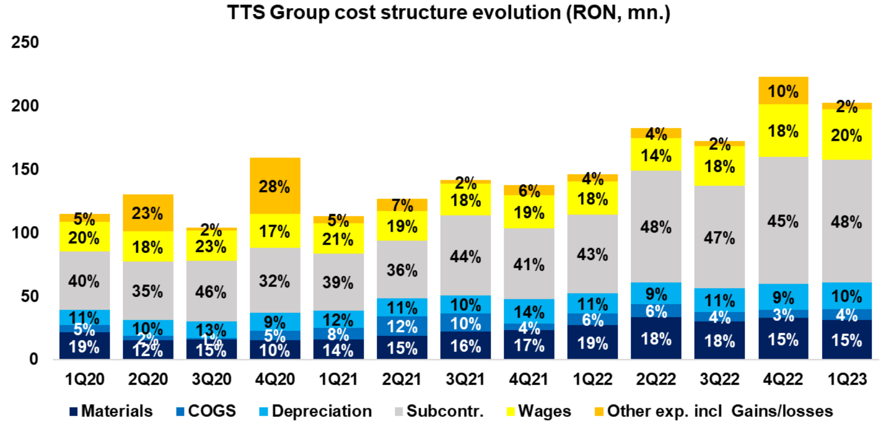
Costs: increasing less than half the revenue growth

Overall, the total operating costs increased by 39% y-o-y but declined by 9% q-o-q. On a yearly basis, the largest increase in costs was naturally that with subcontractors, an expected evolution considering the reconfiguration of logistic chains that implied more rail transport with third parties. Wages followed with a growth y-o-y of 54%. Depreciation expenses grew by 32% and materials – including fuel – by 15% while other costs actually declined.

Percentage of revenues	1Q23	1Q22	4Q22	1Q21	2022	2021	2020
Materials	10.2%	16.8%	12.1%	10.7%	13.2%	13.3%	13.1%
COGS	2.8%	5.6%	2.3%	5.1%	3.5%	7.3%	3.4%
Depreciation	6.9%	9.8%	7.7%	9.8%	7.8%	10.3%	10.0%
Subcontr.	31.5%	38.5%	37.1%	35.7%	35.4%	34.9%	36.7%
Wages	13.1%	16.2%	15.2%	18.3%	13.3%	16.4%	18.6%
Other exp.	3.4%	7.5%	4.7%	6.4%	4.8%	7.0%	7.8%
Gains/losses	-1.8%	-4.1%	3.3%	3.0%	-0.6%	-2.6%	-1.5%

Source: Company data, Erste Group Research

Also, on a yearly basis the share of revenues represented by each cost item declined by a substantial amount, on all cost items. The same trend was also represented on a quarterly basis, with every single cost item representing a lower share of revenues. This was expected considering the exceptional growth in revenues, on the back of agricultural receipts, however, even in absolute terms costs declined compared to the previous quarter. Other than subcontractor fees, as share of total costs, the main shift was in wages and personnel related costs that represented a higher share of total costs – 20%, compared to the 18% of the previous year and of 1Q22.



Source: Company data, Erste Group Research

Balance sheet: stronger than ever

The performance of 1Q23 in terms of revenues and profitability transferred into a exceptionally strong balance sheet. The net debt stayed negative, as at the end of 2022, but the increase in cash and equivalents was remarkable. The company built a cash coffer, most probably in view of corporate actions – see below – and is poised to have ample means for further expansion and CAPEX.

(RON, mn.)	2018	2019	2020	2021	2022	1Q23
Cash & equivalents	38.9	62.4	55.2	58.9	146.0	230.6
ST Debt	54.1	62.9	50.8	41.3	26.8	24.3
LT Debt	64.2	46.1	23.1	26.8	40.9	37.7
Net Debt	79.4	46.6	18.7	9.2	-78.3	-168.6
Net Debt to EBITDA	**1.10**	**0.38**	**0.16**	**0.07**	**-0.28**	**-0.54**

Source: Company data, Erste Group Research

Corporate action: expanding footprint, paying dividends

The management of TTS has shown remarkable adaptability to the challenges of the last year. The reconfiguration of logistic chains, including rail transport and the opening of the floating terminal in Constanta Port are just examples along this line. Recently, the company has announced the acquisition of a new terminal in Constanta Port. It is a solid bulk product terminal, DECIROM S.A. and the transaction – recently approved by authorities – is set to be completed by the end of June. The acquisition, which would enhance the capacity of port operations was priced at around EUR22mn. Along the same lines, the company continues to invest in expanding and improving the river transport fleet with a program of modernization and recertification of barges, together with CAPEX for building new barges that should increase capacity of transport by a cumulative 6,000 tons at the price of EUR5mn. It will also invest in floating cranes in order to streamline port operations and increase operating capacity.

The company declared an amount of RON33mn to be paid in dividends out of 2022 net income. The pay-out ratio is 18%, which could be significantly increased going forward as the company generates ample operating cashflow that could sustain CAPEX and a more substantial dividend payment.

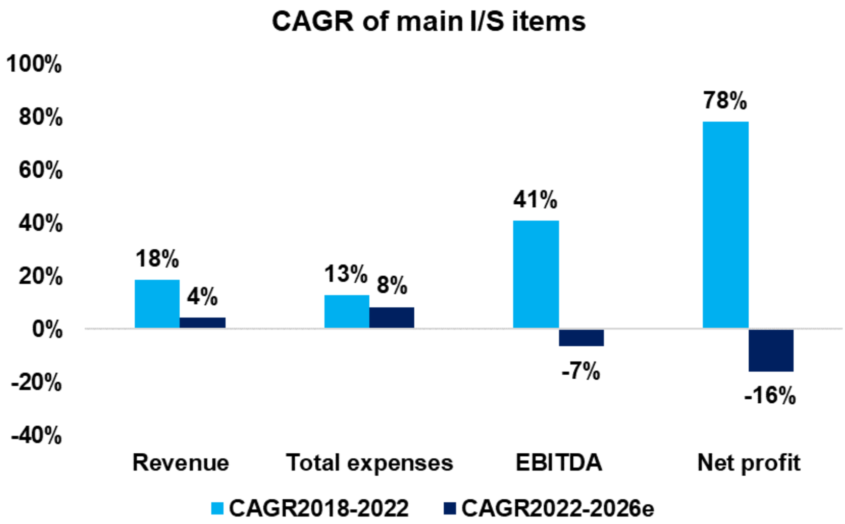
Looking forward: even the most conservative outlook provides upside

As much as we were enthralled by the outstanding performance of the past year and last few quarters, and the stellar growth of 1Q23, we maintain a conservative outlook. Indeed, the explosive increase in profitability came on the back of exceptional circumstances, with the war in the Ukraine providing a demand that exceed considerably that of the previous period. Nevertheless, we cannot ignore the capacity of the company to adapt to a new environment and to capitalize on existing strengths while building for the future.

We attempted in our forecast to provide a worst-case scenario where volumes overall grow only marginally, while costs increase more than revenues, in order to test the strength of our financial forecasts and the resilience potential of the company. Under this conservative scenario, over the next four years volumes of river transport would decline and only reach pre-war levels by the year 2028 while port operations volumes increase only marginally, despite the current acquisition and planned investments.

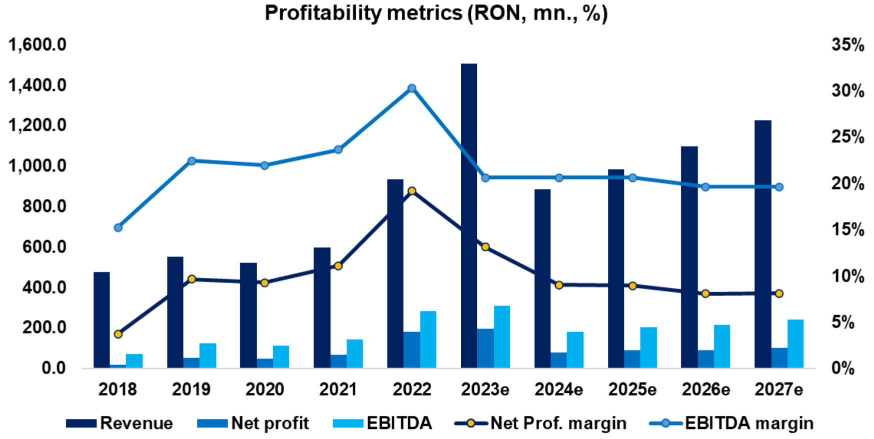
In terms of tariffs for river transport, we applied current tariffs for the rest of the year, and assumed an average drop by half during 2024, followed by an increase with inflation. It is difficult to sustain such a sudden decline in tariffs, considering geopolitical developments that are not showing any immediate dramatic improvement, however we decided to err on the side of caution, showing probably excessive moderation in our outlook.

As a result, our cost forecast provides for a 2022-2026 CAGR twice that of revenues, resulting in a negative 2022-2026 CAGR for EBITDA to the level of -7% and an even more drastic 2022-2026 CAGR for net profit of -16%. This takes into consideration the exceptional year 2022, and an overly conservative view of the industry going forward, however, as we show below, even this worst-case scenario provides ample upside for value.



Source: Company data, Erste Group Research

In the port operations segment we projected a minimal volume growth, of less than 4% CAGR for the next four years. This is indeed an overly conservative assumption, considering the potential of the newly acquired terminal and the potential of the existing assets. Tariff wise, we also forecast a dramatic drop in tariffs during 2024, by about 15%, and a growth with inflation afterwards.

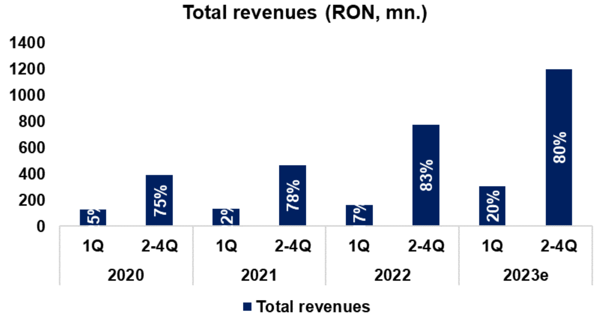


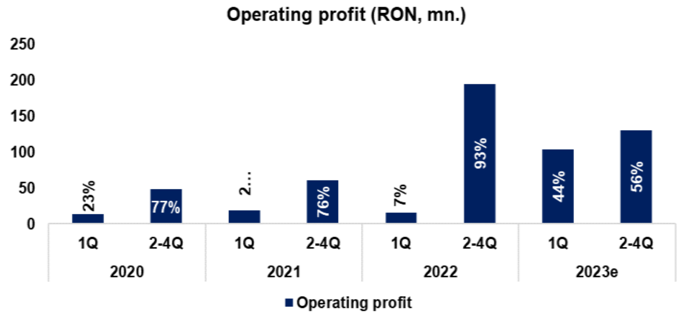
Source: Company data, Erste Group Research

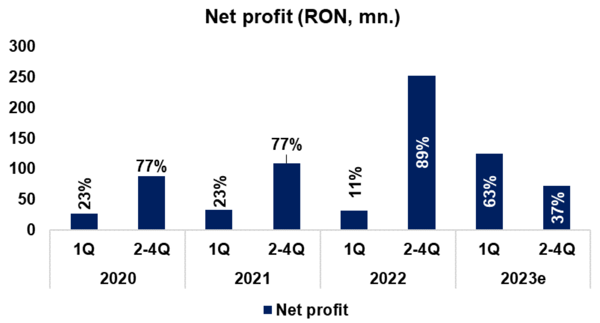
As a consequence of us considering the worst-case scenario, the profitability of the company is set to decline compared to 2022 and 2021 and reach an average consistent with 2019-2020 levels. The drop in profitability forecasted in 2023 is severe and is not sustained by the 1Q23 results that showed actually an increase in profitability versus the same period of last year. Again, we acknowledge this to be a worst-case scenario, establishing – if anything – a bottom valuation for the stock.

Risk entirely on the upside

First quarter results validate entirely our opinion that our outlook is a worst-case scenario. Indeed, the results show that on a historical basis, the first quarter results of 2023 should be harbingers of a much better year than we consider. This is visible on a historical perspective for revenues, however even more consistent regarding operating profits and overwhelmingly so regarding net income. Indeed, in terms of net income the result of 1Q23 should be followed by half much during the next three quarters in order to match a worse-case scenario.



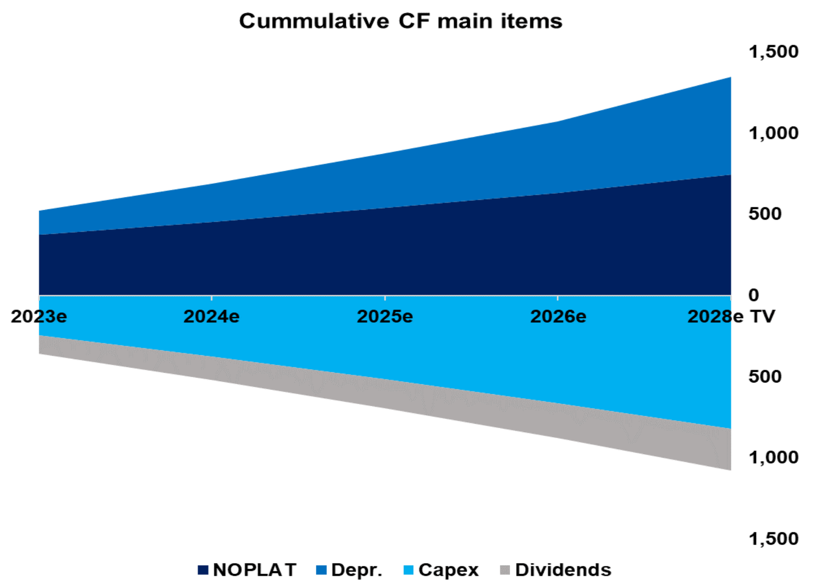




Source: Company data, Erste Group Research

Valuation – we are cheap, and we know it

We performed our valuation exercise under the assumptions presented above: minimal revenue growth, higher cost expansion and declining EBITDA and profits. Nevertheless, even under these dire circumstances, the stock seems to have a considerable upside. Indeed, cash generation is solid, and would accommodate an even more ambitious CAPEX, of about RON120mn a year on the existing asset base. We do not forecast any M&A CAPEX under this exercise, as these activities bring in additional returns on invested capital which we did not account for. Thus, our CAPEX figures are more than ample for current investment programs in fleet and port modernization and expansion, without any additional expenses on acquisitions that would be considered as separate projects bringing value on top and bottom lines and an increase in profitability.



Source: Company data, Erste Group Research

TTS DCF valuation

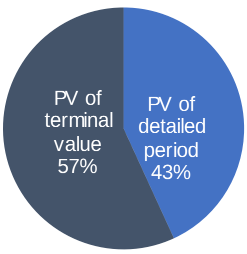
WACC calculation

	2023e	2024e	2025e	2026e	2027e	2028e TV
Risk free rate	8.5%	8.5%	8.5%	8.5%	8.5%	4.3%
Equity risk premium	7.5%	7.5%	7.5%	7.5%	7.5%	7.0%
Beta	1.1	1.1	1.1	1.1	1.1	1.1
Cost of equity	**16.7%**	**16.7%**	**16.7%**	**16.7%**	**16.7%**	**12.0%**
Cost of debt	9.5%	9.5%	9.5%	9.5%	9.5%	5.3%
Effective tax rate	16.0%	16.0%	16.0%	16.0%	16.0%	16.0%
After-tax cost of debt	**8.0%**	**8.0%**	**8.0%**	**8.0%**	**8.0%**	**4.5%**
Equity weight	70%	70%	70%	70%	70%	68%
WACC	**14.1%**	**14.1%**	**14.1%**	**14.08%**	**14.08%**	**9.58%**

DCF valuation

(RON mn)	2023e	2024e	2025e	2026e	2027e	2028e TV
Sales growth	*61.0%*	*-41.3%*	*11.5%*	*11.5%*	*11.5%*	*3.0%*
EBIT	234	95	105	106	119	116
EBIT margin	*15.6%*	*10.8%*	*10.7%*	*9.7%*	*9.7%*	*9.5%*
Tax rate	*16.0%*	*16.0%*	*16.0%*	*16.0%*	*16.0%*	*16.0%*
Taxes on EBIT	-37.4	-15.3	-16.9	-17.0	-19.0	-18.6
NOPLAT	**196.6**	**80.1**	**88.5**	**89.2**	**99.8**	**97.8**
+ Depreciation	76	87	98	109	122	161
Capital expenditures / Depreciation	*165.2%*	*152.5%*	*142.1%*	*133.4%*	*126.0%*	*100.0%*
+/- Change in working capital	79	-68	11	12	14	-25
Chg. working capital / chg. Sales	*13.9%*	*10.9%*	*10.9%*	*10.9%*	*10.9%*	*-20.0%*
- Capital expenditures	-126.0	-132.3	-138.9	-145.9	-153.2	-160.8
Free cash flow to the firm	**226.2**	**-33.0**	**58.4**	**65.0**	**82.0**	**72.4**
Terminal value growth						*3.0%*
Terminal value						1,132.7
Discounted free cash flow - March 30 202:	198.3	-25.3	39.3	38.4	42.4	569.1
Enterprise value - March 30 2023	**862**					
Minorities	106					
Non-operating assets	0					
Net debt (incl. lease liabilities)	-136					
Other adjustments	0					
Equity value - (RON bn) March 30 2023	**891.8**					
Cost of equity	12.0%					
Fair value, RON mn	**998.8**					
Number of shares outstanding (mn)	60.0					
Fair value per share, RON	**16.65**					
Share price	13.55					
Upside/downside Official NAV (%)	*22.86%*					

Enterprise value breakdown



Sensitivity (Equity value - RON mn)

Terminal value EBIT margin

WACC	8.5%	9.0%	9.5%	10.0%	10.5%
8.6%	16.77	17.66	18.55	19.44	20.33
9.1%	15.89	16.70	17.52	18.34	19.15
9.6%	15.14	15.89	**16.65**	17.40	18.16
10.1%	14.49	15.20	15.90	16.60	17.30
10.6%	13.94	14.59	15.25	15.90	16.56

Terminal value growth

WACC	2.0%	2.5%	3.0%	3.5%	4.0%
8.6%	16.65	17.52	18.55	19.78	21.28
9.1%	15.90	16.65	17.52	18.55	19.78
9.6%	15.25	15.90	**16.65**	17.52	18.55
10.1%	14.68	15.25	15.90	16.65	17.52
10.6%	14.17	14.68	15.25	15.90	16.65

Source: Erste Group Research

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Company description

TTS is the premier river transportation and port operations provider in the Danube Basin and the Constanta Port

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