

# Bong

Sector: Industrial Goods & Services

## Challenging Year Ahead

Redeye is lowering its forecasts and valuation for Bong in the wake of the Corona crisis. 2020 will be a challenging year for Bong since several business units are affected by the shut-downs in Europe. We expect to see a significant drop in volumes and more restructuring measures. Light Packaging is affected to a lesser extent but will certainly not balance the expected decline in envelopes.

### Bright spots in Q1: Gross margins and Packaging

Q1-numbers were quite ok on group level, although Bong started to see the impact of Covid-19 restrictions at the end of the quarter. Envelope sales dropped by around 15% Y/Y (Fx adjusted). Light Packaging on the other hand showed continued good growth of 8% (Fx adjusted). The main driver is still paper carrier bags with an impressive 57% growth in Q1. Gross margins improved to 18.5%, which is higher than we have seen in the last few years. Paper prices have been rather soft since last summer and this is now probably feeding through to Bongs COGS, which is a bit of a relief.

### Covid-19

Covid-19 related restrictions have a significant impact on Bongs business, particularly in UK and France, which are two of their most important markets. The addressed direct mail (ADM) market will probably decline considerably, since this marketing tool is rather sensitive to the business climate. Moreover, Bong stated in the report that the positive trend in retail gift bags did not continue as a result of Covid-19. At this point we cannot really assess the implications on Bongs sales and earnings. We assume that Q2-Q3 will see a significant decline and then a gradual pick-up during the autumn.

### Estimates adjusted further down

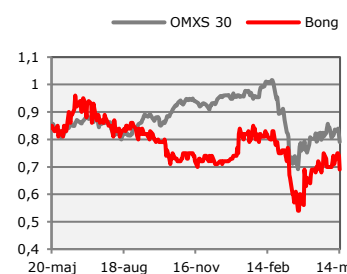
We expect some improvement in gross margins this year. But earnings will probably drop, given a significant decline in sales. Next year Bong should be able to show positive EBIT again. Our Base case fair value is now **SEK 0.9 per share** (vs. SEK 1.0 before).

KEY FINANCIALS (SEKm)	2018	2019	2020E	2021E	2022E	2023E
Net sales	2220	2166	1906	1920	1879	1879
EBITDA	71	121	78	116	145	139
EBIT	-52	32	-14	30	58	56
EPS (adj.)	-0.3	-0.1	-0.2	0.0	0.1	0.1
EV/Sales	0.2	0.3	0.3	0.2	0.2	0.2
EV/EBITDA	7.5	5.0	6.3	4.1	3.0	2.9
EV/EBIT	-10.4	19.1	-35.7	16.0	7.5	7.1
P/E	-1.3	-6.3	-3.3	-19.1	8.5	8.0

### FAIR VALUE RANGE

BEAR	BASE	BULL
0.3	0.9	2.0

### VERSUS OMXS30



### REDEYE RATING



### KEY STATS

Ticker	BONG
Market	Nasdaq
Share Price (SEK)	0.7
Market Cap (MSEK)	144
Net Debt 20E (MSEK)	456
Free Float	70 %
Avg. daily volume ('000)	130

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## Challenging Year Ahead

On group level the Q1-numbers were very much in line with our estimates. Gross margins and Light Packaging sales were the two major positive take-aways from the quarterly report. Envelopes declined by around 15%, currency adjusted. Bong started to see the effect of Covid-19 related restrictions in March when most European countries shut down. And the impact will probably be much more significant in Q2. Bong states that operations in UK and France, two of their most important markets, have been drastically affected.

### Bong: Expected vs. Actual

(SEKm)	Q1'19	Q1' 20 Actual	Q1'20E	Diff
Net sales	571	518	525	-1%
Whereof Light Packaging	106	116	108	7%
Gross profit	100	96	89	8%
EBITDA	37	32	26	23%
EBIT	15	5	4	25%
Pre-tax profit	5	-3	-6	-50%
Sales growth Y/Y	6%	-9%	-8%	
Gross margin	17.5%	18.5%	17.0%	
EBITDA margin	6.5%	6.2%	5.0%	
EBIT margin	2.6%	1.0%	0.8%	

Source: Bong, Redeye Research

Gross margins improved Y/Y and we believe the main reason is that paper prices have declined for some time. This is now feeding through to Bongs COGS. Maybe also the product mix (more packaging and less envelopes). On the other hand, SG&A expenses bounced back and were higher Y/Y as well as Q/Q.

Light Packaging had another quarter of solid growth, particularly in Central- and South Europe, while the Nordics and UK declined somewhat. Paper carrier bags continued to grow at an impressive 57% Y/Y, currency adjusted. E-commerce packaging was also doing well, while retail gift bags started to suffer from the shut-down of retail stores throughout Europe.

### Quarterly performance

(SEK m)	Q1'18	Q2'18	Q3'18	Q4'18	Q1'19	Q2'19	Q3'19	Q4'19	Q1'20
Revenues	538	543	536	603	571	507	520	568	518
whereof Light Packaging	97	104	113	138	106	105	124	155	116
Gross profit	93	84	91	99	100	82	87	96	96
EBITDA *	25	17	18	12	21	4	14	21	22
EBIT	12	10	12	-85	15	-3	7	14	5
Net financial items	-11	-23	-10	-13	-11	-11	-12	-8	-8
Pre tax profit	1	-13	1	-98	5	-15	-6	6	-3
Revenue growth, Y/Y	-1%	13%	9%	4%	6%	-7%	-3%	-6%	-9%
Gross-margin	17.3%	15.5%	16.9%	16.4%	17.5%	16.1%	16.8%	16.9%	18.5%
EBITDA-margin *	4.6%	3.1%	3.4%	2.0%	3.7%	0.8%	2.7%	3.7%	4.1%
Cash flow after investments	-1	-48	-12	-6	42	-11	-7	55	14
Net debt, excl leasing debt	300	335	346	349	326	360	394	346	338

\* Excluding non-recurring items and IFRS 16

Source: Bong, Redeye Research

## Forecasts & Valuation

### Envelopes

We saw some weakness in the European envelope market already before the Corona pandemic. Since March the drop in volumes is of course dramatic given the restrictions in most of the larger countries. Bongs segment Direct Mail will probably suffer the most in 2020, since these clients tend to be very sensitive to the business climate. Bong is taking several actions to lower costs, but we have no details on how comprehensive these measures are. At this point our 2020 estimates are basically "guesstimates" based on very slow activity in Q2-Q3 and a gradual pick-up during next autumn.

*2020E – a guessing game at this point*

On a positive note, pulp and paper prices are lower vs last year. We saw some improvement in Bongs gross margins in Q1 and believe that is sustainable, at least for the near-term future.

### Light Packaging

Light Packaging will probably not be as negatively affected (as envelopes) by the current business conditions. E-commerce should even benefit from the strong trend in this market segment. But altogether, we still believe Light Packaging sales will decline in 2020. Retail gift bags started to see a slowdown in Q1 and Q2 will probably be a lot worse. The transition from plastic to paper carrier bags in Europe is still at an early stage. We believe this product segment will continue to grow in 2020 and beyond, in spite of tougher times for retailers.

*Sales mix improving over time*

In 2019 the Light Packaging segment represented 23 percent of group sales versus 20 percent in 2018. This transition will continue which means a gradually improving sales mix. This trend should allow for Bong to improve profitability over time. The gradual downsizing of envelope production will require future restructuring measures. We are now including annual restructuring costs of SEK 30 m net in 2020-21. In many cases these costs are mitigated by machinery being sold to Asia or real estate divestments. Thus cash flow will probably not be hit by the full amount of restructuring charges.

P&L, historic and forecast						
SEK m	2017	2018	2019	2020E	2021E	2022E
<b>Envelopes</b>						
Revenues	1680	1767	1676	1440	1426	1355
Growth, Y/Y	-3%	5%	-5%	-14%	-1%	-5%
EBIT *	25	-2	14	-7	25	31
EBIT-margin	1.5%	-0.1%	0.8%	-0.5%	1.8%	2.3%
<b>Light Packaging</b>						
Revenues	415	453	490	466	494	524
Growth, Y/Y	4%	9%	8%	-5%	6%	6%
EBIT *	21	27	29	23	35	42
EBIT-margin	5.0%	6.0%	6.0%	5.0%	7.0%	8.0%
Non-recurring items	0	-77	-11	-30	-30	-15
<b>Total revenues</b>	<b>2095</b>	<b>2220</b>	<b>2166</b>	<b>1906</b>	<b>1920</b>	<b>1879</b>
Growth, Y/Y	-2%	6%	-2%	-12%	1%	-2%
<b>Gross profit</b>	<b>381</b>	<b>367</b>	<b>364</b>	<b>333</b>	<b>346</b>	<b>348</b>
Gross-margin	18.2%	16.5%	16.8%	17.5%	18.0%	18.5%
<b>EBITDA **</b>	<b>92</b>	<b>72</b>	<b>132</b>	<b>104</b>	<b>146</b>	<b>160</b>
D.o. marginal	4.4%	3.2%	6.1%	5.5%	7.6%	8.5%
<b>EBIT</b>	<b>45</b>	<b>-52</b>	<b>32</b>	<b>-14</b>	<b>30</b>	<b>58</b>
Net financial items	-44	-57	-42	-40	-39	-37
Pre tax profit	1	-109	-10	-54	-9	21

\* Redeyes assessment regarding previous years. \*\* Excluding non-recurring items (but including IFRS 16)

Source: Bong, Redeye Research

## Valuation

Fair value: ~SEK 0.9 per share

Our DCF-model indicates an enterprise value of just above SEK 530 million. After deducting net debt of SEK 346 m (excluding lease liabilities) our fair value of equity is around SEK 180 million, or **SEK 0.9 per share**. In our most recent update, as of March 2020, the corresponding value was SEK 1.0 per share.

The change in fair value is due to our revisions of 2020-22 estimates. No changes have been made in our assumptions for long term growth or profitability:

- Years 2023-28: zero growth, 3 percent EBIT-margin
- Terminal year (2028): 2 percent growth, 3 percent EBIT-margin
- WACC: 12 percent (derived from our Redeye Rating model)

### Long term assumptions for growth and profitability

As Bongs packaging business expands, the negative growth on group level will level out. For the period 2023-28 we assume zero growth and thereafter 2 percent annually. We expect sustainable EBIT-margins of 3.0 percent. This is based on packaging making up for a larger part of group total, recurring costs for downsizing the envelope business, a general down-turn in the economy or other potential problems during this period.

DCF-value, SEK per share					
Sustainable EBIT-margins	2.0%	2.5%	3.0%	3.5%	4.0%
<b>WACC</b>					
11.0%	0.66	0.91	1.16	1.40	1.65
12.0%	0.46	0.68	<b>0.90</b>	1.12	1.33
13.0%	0.29	0.48	0.67	0.86	1.06

Source: Redeye Research

### Multiples 2021-22E similar to previous years

EV/EBITDA is the most useful key ratio to track, since it takes both the high net debt into account and the fact that depreciations are much higher than Capex. Note that we have excluded the impact from IFRS 16 on this key ration, since these items distort the comparison. Bongs EV/EBITDA multiples 2021-22 are fairly similar to previous years.

Earnings multiples						
Share price, SEK: 0.70	2017	2018	2019	2020E	2021E	2022E
P/E	neg	neg	neg	neg	neg	8.8
EV/EBITDA *	5.4	7.6	8.1	25.8	8.7	5.8
EV/EBIT	10.9	neg	20.8	neg	22.0	11.3

\* Excl impact from IFRS 16 as of 2019

Source: Redeye Research

## Scenarios

Our Base case scenario, which is was outlined on the previous page, is what we believe a probable scenario that corresponds to a fair value of approximately **SEK 0.9 per share**. There is certainly a possibility that the company will develop better than we anticipate, but also worse. We have drafted two scenarios that illustrate this down below.

**Bull case** is based on sales returning to sustainable growth and improving profitability. If the expansion within packaging is really strong Bong may be able to show positive top-line growth on group level and higher margins than we anticipate. The green area in the table below shows the impact on DCF-value for different levels of sustainable margins and growth (all else being equal). These do not appear completely unrealistic, yet quite optimistic. Fair value would then be around **SEK 2 SEK per share**.

**Bear case** could potentially materialize if the negative trend in the envelope market accelerates causing even tougher squeeze on margins and recurring costs for capacity adjustments. It could also happen as a combination of Bongs packaging business stalling in terms of growth and profitability. The orange colored area indicates possible outcomes in this scenario. Fair value would then be only approximately **SEK 0.3 per share**.

<b>DCF-value, SEK per share</b>					
<b>Sustainable EBIT-margins</b>	<b>1.0%</b>	<b>2.0%</b>	<b>3.0%</b>	<b>4.0%</b>	<b>5.0%</b>
<b>Annual growth rate 2023-28</b>					
-3.0%	0.04	0.39	0.76	1.13	1.50
<b>0.0%</b>	0.05	0.46	<b>0.90</b>	1.33	1.77
3.0%	0.06	0.53	1.03	1.53	2.04
6.0%	0.07	0.60	1.17	1.73	2.30

Source: Redeye Research

## Summary Redeye Rating

The rating consists of three valuation keys, each constituting an overall assessment of several factors that are rated on a scale of 0 to 1 points. The maximum score for a valuation key is 5 points.

### Rating changes in the report: No changes

#### People: 3

Management has several years of experience and knows its markets very well. Kai Steigleder is however new on the job as CEO but he has been with Bong since 2007. Most recently as managing director of the largest business unit, Central Europe. The last few years have been characterized by heavy restructuring measures which have been well managed. On the other hand we cannot assess whether management has the ability to create growth, which is now their ambition. The public quarterly reports are quite brief in terms of numbers and information. Hence transparency is limited which makes it more difficult to review and understand the company.

#### Business: 3

All-and-all Bong is a little below average in this category. Primarily because of the negative market trend for envelopes where volumes are going down, products are standardized and competition is tough. Bong has economies of scale and probably better stamina than most of its peers. The envelope business will hardly attract new players, but with shrinking volumes and over capacity, price pressure will remain. For Light Packaging the prospects are clearly better and Bong has a good position withing a couple of growing market segments.

#### Financials: 2

Profitability has been weak during the past several years. In spite of substantial cost-cutting programs margins and earnings are very thin. Since depreciation is substantially higher than capex, cash flows are generally stronger than reported earnings. Bongs financial gearing is relatively high but manageable and the debt is primarily long term. The business is diversified in terms of products and customers but to some extent cyclical. Also, for the longer term there is a recurring need for restructuring measures as the envelope market is declining.

INCOME STATEMENT	2018	2019	2020E	2021E	2022E
Net sales	2,220	2,166	1,906	1,920	1,879
Total operating costs	-2,148	-2,046	-1,828	-1,804	-1,734
EBITDA	71	121	78	116	145
Depreciation	-45	-27	-28	-28	-24
Amortization	-2	-2	0	0	0
Impairment charges	-76	0	-4	0	0
EBIT	-52	32	-14	30	58
Share in profits	0	0	0	0	0
Net financial items	-57	-42	-40	-39	-37
Exchange rate dif.	0	0	0	0	0
Pre-tax profit	-109	-10	-54	-9	21
Tax	-39	-14	10	2	-4
Net earnings	-149	-24	-44	-8	17

BALANCE SHEET	2018	2019	2020E	2021E	2022E
<b>Assets</b>					
<i>Current assets</i>					
Cash in banks	72	100	88	88	86
Receivables	289	223	196	192	188
Inventories	195	200	181	182	178
Other current assets	99	95	95	95	95
Current assets	655	618	560	557	547
<i>Fixed assets</i>					
Tangible assets	179	209	186	163	143
Associated comp.	0	0	0	0	0
Investments	1	1	1	1	1
Goodwill	518	530	526	526	526
Cap. exp. for dev.	0	0	0	0	0
Intangible rights	17	9	10	11	12
Non-current assets	0	0	0	0	0
Total fixed assets	716	854	828	808	787
Deferred tax assets	110	113	113	113	113
Total (assets)	1,481	1,586	1,502	1,479	1,448
<b>Liabilities</b>					
<i>Current liabilities</i>					
Short-term debt	0	0	0	0	0
Accounts payable	221	182	160	161	158
Other current liabilities	240	299	289	289	289
Current liabilities	461	481	449	450	447
Long-term debt	421	446	437	421	377
Other long-term liabilities	16	14	14	14	14
Convertibles	0	0	0	0	0
Total Liabilities	898	941	900	885	838
Deferred tax liab	14	10	10	10	10
Provisions	0	0	0	0	0
Shareholders' equity	569	529	485	477	494
Minority interest (BS)	0	0	0	0	0
Minority & equity	569	529	485	477	494
Total liab & SE	1,481	1,586	1,502	1,479	1,448

FREE CASH FLOW	2018	2019	2020E	2021E	2022E
Net sales	2,220	2,166	1,906	1,920	1,879
Total operating costs	-2,148	-2,046	-1,828	-1,804	-1,734
Depreciations total	-123	-89	-92	-86	-87
EBIT	-52	32	-14	30	58
Taxes on EBIT	11	-7	3	-6	-12
NOPLAT	-57	25	-12	24	46
Depreciation	123	89	92	86	87
Gross cash flow	66	114	80	110	133
Change in WC	-49	14	14	4	5
Gross CAPEX	-6	-23	-6	-6	-6
Free cash flow	11	105	88	108	132

CAPITAL STRUCTURE	2018	2019	2020E	2021E	2022E
Equity ratio	38%	33%	32%	32%	34%
Debt/equity ratio	74%	104%	112%	110%	98%
Net debt	349	452	456	439	397
Capital employed	918	875	835	810	785
Capital turnover rate	1.5	1.4	1.3	1.3	1.3

GROWTH	2018	2019	2020E	2021E	2022E
Sales growth	6%	-2%	-12%	1%	-2%
EPS growth (adj)	1,105%	-84%	82%	-83%	-323%

DCF VALUATION		CASH FLOW, MSEK	
WACC (%)	12.0 %	NPV FCF (2020-2022)	120
		NPV FCF (2023-2028)	206
		NPV FCF (2029-)	210
		Non-operating assets	100
		Interest-bearing debt	-446
		Fair value estimate MSEK	190

Assumptions 2023-2028 (%)			
Average sales growth	0 %	Fair value e. per share, SEK	0.9
EBIT margin	3 %	Share price, SEK	0.7

PROFITABILITY	2018	2019	2020E	2021E	2022E
ROE	-24%	-4%	-9%	-2%	3%
ROCE	-5%	3%	-1%	3%	6%
ROIC	-6%	3%	-1%	3%	6%
EBITDA margin	3%	6%	4%	6%	8%
EBIT margin	-2%	1%	-1%	2%	3%
Net margin	-7%	-1%	-2%	0%	1%

DATA PER SHARE	2018	2019	2020E	2021E	2022E
EPS	-0.71	-0.11	-0.21	-0.04	0.08
EPS adj	-0.35	-0.11	-0.19	-0.04	0.08
Dividend	0.00	0.00	0.00	0.00	0.00
Net debt	1.65	2.14	2.16	2.08	1.88
Total shares	211.25	211.25	211.25	211.25	211.25

VALUATION	2018	2019	2020E	2021E	2022E
EV	538.7	604.4	493.6	476.6	434.2
P/E	-1.3	-6.3	-3.3	-19.1	8.5
P/E diluted	-1.3	-6.3	-3.3	-19.1	8.5
P/Sales	0.1	0.1	0.1	0.1	0.1
EV/Sales	0.2	0.3	0.3	0.2	0.2
EV/EBITDA	7.5	5.0	6.3	4.1	3.0
EV/EBIT	-10.4	19.1	-35.7	16.0	7.5
P/BV	0.3	0.3	0.3	0.3	0.3

SHARE PERFORMANCE		GROWTH/YEAR	18/20E
1 month	-5.6 %	Net sales	-7.3 %
3 month	-15.0 %	Operating profit adj	-48.4 %
12 month	-21.8 %	EPS, just	-26.3 %
Since start of the year	-6.9 %	Equity	-7.7 %

SHAREHOLDER STRUCTURE %	CAPITAL	VOTES
Stéphane Hamelin	25.0 %	25.0 %
Per-Arne Åhlgren	14.9 %	14.9 %
Svolder	7.7 %	7.7 %
Avanza Pension	5.3 %	5.3 %
Theodor Jeansson	4.7 %	4.7 %
Christian Paulsson	4.3 %	4.3 %
Dan Drottman	2.3 %	2.3 %
John Elvesjö	2.2 %	2.2 %
Skandinaviska Enskilda Banken S.A	1.8 %	1.8 %
Mattias Cramby	1.8 %	1.8 %

SHARE INFORMATION	
Reuters code	BONG.ST
List	Nasdaq Small Cap
Share price	0.7
Total shares, million	211.2
Market Cap, MSEK	143.6

MANAGEMENT & BOARD	
CEO	Kai Steigleder
CFO	Carsten Grimmer
IR	
Chairman	Christian Paulsson

FINANCIAL INFORMATION	
Q2 report	July 15, 2020
Q3 report	November 12, 2020

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## Redeye Rating and Background Definitions

### Company Quality

Company Quality is based on a set of quality checks across three categories; PEOPLE, BUSINESS, FINANCE. These are the building blocks that enable a company to deliver sustained operational outperformance and attractive long-term earnings growth.

Each category is grouped into multiple sub-categories assessed by five checks. These are based on widely accepted and tested investment criteria and used by demonstrably successful investors and investment firms. Each sub-category may also include a complementary check that provides additional information to assist with investment decision-making.

If a check is successful, it is assigned a score of one point; the total successful checks are added to give a score for each sub-category. The overall score for a category is the average of all sub-category scores, based on a scale that ranges from 0 to 5 rounded up to the nearest whole number. The overall score for each category is then used to generate the size of the bar in the Company Quality graphic.

### People

At the end of the day, people drive profits. Not numbers. Understanding the motivations of people behind a business is a significant part of understanding the long-term drive of the company. It all comes down to doing business with people you trust, or at least avoiding dealing with people of questionable character.

The People rating is based on quantitative scores in seven categories:

- Passion, Execution, Capital Allocation, Communication, Compensation, Ownership, and Board.

### Business

If you don't understand the competitive environment and don't have a clear sense of how the business will engage customers, create value and consistently deliver that value at a profit, you won't succeed as an investor. Knowing the business model inside out will provide you some level of certainty and reduce the risk when you buy a stock.

The Business rating is based on quantitative scores grouped into five sub-categories:

- Business Scalability, Market Structure, Value Proposition, Economic Moat, and Operational Risks.

### Financials

Investing is part art, part science. Financial ratios make up most of the science. Ratios are used to evaluate the financial soundness of a business. Also, these ratios are key factors that will impact a company's financial performance and valuation. However, you only need a few to determine whether a company is financially strong or weak.

The Financial rating is based on quantitative scores that are grouped into five separate categories:

- Earnings Power, Profit Margin, Growth Rate, Financial Health, and Earnings Quality.



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### Redeye Rating (2020-05-18)

Rating	People	Business	Financials
5p	13	11	4
3p - 4p	106	80	30
0p - 2p	7	35	92
Company N	126	126	126

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### CONFLICT OF INTERESTS

Henrik Alveskog owns shares in the company : No

Viktor Westman owns shares in the company : No

Redeye performs/have performed services for the Company and receives/have received compensation from the Company in connection with this.