REDEYE

Update

Equity Research

16 July 2019

Bong

Sector: Industrial Goods & Services

Declining top-line calls for action

Sales dropped sharply in the second quarter, putting pressure on gross margins and sending EBIT back into red numbers. Adjusted for currency effects, sales decreased approximately 10 percent and even a bit more for envelope products. Gross margins in Q2 were only a fraction higher Y/Y and clearly below the first quarter of this year.

Chance to regain margins

Lower volumes appears to be the main reason for the poor profitability. At least raw material prices have been stable in the last few months and the outlook for paper prices is rather favorable from Bongs perspective. Envelope manufacturers now have an opportunity to catch up and regain some margins that was lost during the last two years when paper prices were constantly on the rise.

Bong has also taken a couple of steps in its factory efficiency program. And there is certainly more to come since most units are included in the program. However most of the measures are probably not of the magnitude that they will be communicated publicly.

Entering North Africa

In the report Bong announced that they are establishing production in Tunisia for the North African market. First envelopes and later on also for packaging products. This is quite exciting news for several reasons. First of all this is a very low-cost expansion with a minimum of Capex, since Bong is moving equipment from other facilities in Europe. The North African envelope market is growing and according to Bong competitors are only local players. Also, they expect to reach break-even sometime soon.

If all goes well over the next few years, Bong can continue its expansion in this region by transferring production equipment from Europe. Thereby balancing some of the negative growth and problems with constant over-capacity in the mature European markets.

Near term estimates down

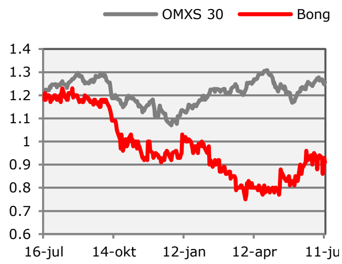
We now need to adjust our near term estimates down on the back of weak Q2-numbers. We still expect improvements in gross margins but volumes appear to drop faster than we anticipated. However our new rating generates a lower WACC and consequently a higher fair value. Our Base case fair value is now SEK 1.4 per share (vs. SEK 1.1 before).

KEY FINANCIALS (SEKm)	2017	2018	2019E	2020E	2021E	2022E
Net sales	2095	2220	2198	2124	2058	1996
EBITDA	91	71	115	135	150	145
EBIT	45	-52	29	49	65	60
EPS (adj.)	-0.1	-0.3	-0.1	0.0	0.1	0.1
EV/Sales	0.2	0.2	0.3	0.3	0.3	0.3
EV/EBITDA	5.4	7.5	6.2	5.2	4.5	4.5
EV/EBIT	11.0	-10.4	24.9	14.3	10.4	10.9
P/E	-16.2	-1.3	-8.1	94.1	10.8	12.8

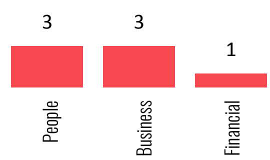
FAIR VALUE RANGE

BEAR	BASE	BULL
0.7	1.4	2.6

VERSUS OMXS30



REDEYE RATING



KEY STATS

Ticker	BONG
Market	Nasdaq
Share Price (SEK)	0.9
Market Cap (MSEK)	184
Net Debt 19E (MSEK)	527
Free Float	70 %
Avg. daily volume ('000)	65

ANALYSTS

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Air pocket in Q2?

The Q2-numbers were lower than we anticipated across the board. The main reason however is the drop in volumes, causing lower top-line, impairing capacity utilization and profitability. Fixed cost items were basically as expected or even a little lower.

Bong: Expected vs. Actual

(SEKm)	Q2' 18	Q2' 19 Actual	Q2'19E	Diff
Net sales	543	507	550	-8%
Whereof Light Packaging	104	105	110	-5%
Gross profit	84	82	96	-15%
EBITDA *	17	19	32	-41%
EBIT	10	-3	10	n.m.
Pre-tax profit	-13	-15	-1	n.m.
Sales growth Y/Y	13%	-7%	1%	
Gross margin	15.5%	16.1%	17.5%	
EBITDA margin	3.1%	3.7%	5.8%	
EBIT margin	1.8%	-0.7%	1.8%	

* EBITDA boosted SEK 15m by IFRS 16 in Q2-19

After a period of two years with continuous top-line growth, revenues fell substantially in Q2. Minus 10 percent organic growth is of course difficult to handle and a little worrying. Brexit and the calendar effect (Easter holiday in Q2 this year) probably added to the decline. But Bong also state in the report that the office supply segment is under strong pressure. The new management's factory efficiency program is obviously necessary and we hope to see a number of actions that can give sustained benefits to Bongs profitability.

Light Packaging sales in Q2 was flat, both Y/Y and Q/Q. Not great but also no reason for concern. Paper carrier bags are still growing vigorously and according to Bong they are actively pushing these products at the expense of plastic bags. Consequently Bongs sales of plastic bags has dropped significantly.

Quarterly performance

(SEK m)	Q2'17	Q3'17	Q4'17	Q1'18	Q2'18	Q3'18	Q4'18	Q1'19	Q2'19
Revenues	481	491	578	538	543	536	603	571	507
whereof Light Packaging	89	93	135	97	104	113	138	106	105
Gross profit	92	84	105	93	84	91	99	100	82
EBITDA *	19	13	34	25	17	18	12	21	6
EBIT	7	2	17	12	10	12	-85	15	-3
Net financial items	-12	-10	-11	-11	-23	-10	-13	-11	-11
Pre tax profit	-4	-8	6	1	-13	1	-98	5	-15
Revenue growth, Y/Y	-4%	0%	0%	-1%	13%	9%	4%	6%	-7%
Gross-margin	19.2%	17.0%	18.2%	17.3%	15.5%	16.9%	16.4%	17.5%	16.1%
EBITDA-margin *	4.0%	2.6%	5.9%	4.6%	3.1%	3.4%	2.0%	3.7%	1.2%
Cash flow after investments	-12	9	27	-1	-48	-12	-6	29	-11
Net debt, excl leasing debt	315	315	294	300	335	346	349	326	360

* Excluding non-recurring items and IFRS 16

Source: Bong, Redeye Research

Forecasts & Valuation

Envelopes

Africa seems promising but still in an early phase

The European envelope market has seen a rather steady decrease of approximately 5 percent annually in the last decade. The decline in Q2 was maybe a little more, but probably caused by some temporary factors. We expect the long-term trend to continue and that Bong will basically follow this general market trend. North Africa is certainly different and seems like a great opportunity for Bong. However this is somewhat unchartered territory for us and a new region for the company. So we are still cautious in our assumptions regarding North Africa.

Chance to restore margins

Bong has not been able to fully compensate for higher paper prices in the last two years. But now pulp and paper prices are softer and envelope manufacturers have a better chance to restore their gross margins. Also Bong is running a factory efficiency program. We expect to see some impact from the price adjustments this year and a further improvement in margins next year from the efficiency program.

Light Packaging

Packaging basically unchanged

Light Packaging has much better prospects for profitable growth. We believe the company can achieve around 5 percent annual growth in the next few years. The market potential in e-commerce and retail solutions is huge and Bong still only has a small share of these markets. The transition from plastic to paper carrier bags in Europe now really seems to accelerate and will continue for many years. Bong apparently has an attractive offer in this category.

With a gradually improving sales mix, more packaging and less envelopes, we expect to see improving and more stable profitability. The shrinking envelope market will require future measures for downsizing. We include annual restructuring costs of SEK 15 m net. In many cases these costs are mitigated by machinery being sold to Asia or real estate divestments. Thus cash flow is not necessarily hit by the full amount of restructuring charges.

Redeye forecasts

SEK m	2016	2017	2018	2019E	2020E	2021E
Envelopes						
Revenues	1736	1680	1767	1723	1620	1523
Growth, Y/Y	-11%	-3%	5%	-2%	-6%	-6%
EBIT *	11	25	-2	13	28	42
EBIT-margin	0.6%	1.5%	-0.1%	0.8%	1.8%	2.8%
Light Packaging						
Revenues	399	415	453	476	504	534
Growth, Y/Y	0%	4%	9%	5%	6%	6%
EBIT *	16	21	27	29	35	37
EBIT-margin	4.0%	5.0%	6.0%	6.0%	7.0%	7.0%
Non-recurring items	-18	0	-77	-13	-15	-15
Total revenues	**2135**	**2095**	**2220**	**2198**	**2124**	**2058**
Growth, Y/Y	-9%	-2%	6%	-1%	-3%	-3%
Gross profit	**373**	**381**	**367**	**374**	**382**	**391**
Gross-margin	17.5%	18.2%	16.5%	17.0%	18.0%	19.0%
EBITDA * **	**79**	**92**	**72**	**128**	**150**	**165**
D.o. marginal	3.7%	4.4%	3.2%	5.8%	7.0%	8.0%
EBIT	**9**	**45**	**-52**	**29**	**49**	**65**
Net financial items **	384	-44	-57	-44	-46	-45
Pre tax profit	393	1	-109	-16	2	20

* Redeyes assessment regarding previous years. ** Whereof SEK 427 million year 2016 following the refinancing.

*** Excluding non-recurring items (but including IFRS 16)

Source: Bong, Redeye Research

Valuation

Fair value: ~SEK 1.4 SEK per share

Our DCF-model indicates an enterprise value of around SEK 650 million. After deducting net debt of SEK 349 m our fair value of equity is about SEK 300 million, or SEK 1.42 per share.

In our previous research update, as of May 2019, the corresponding value was SEK 1.1 per share. The difference is explained only by the fact that we are applying a lower WACC as a result of our new rating model. We are using a 12 percent WACC (vs. 14.5 percent previously). We have lowered our estimates for years 2019-21 somewhat, while no changes have been made in our assumptions for long term growth or profitability:

- Years 2023-27: zero growth, 3 percent EBIT-margin
- Terminal year (2028): 2 percent growth, 3 percent EBIT-margin
- WACC: 12 percent (derived from our new 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 2023-27 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%
WACC					
11.0%	1.19	1.46	1.73	1.99	2.24
12.0%	0.96	1.20	**1.42**	1.66	1.88
13.0%	0.78	0.99	1.19	1.39	1.59

Source: Redeye Research

Multiples are now a little higher

The share is now trading at slightly higher multiples compared to the previous two years, based on our estimates. The most relevant multiple for Bong is EV/EBITDA 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. EV/EBITDA of 6-7x is not unique, but at the low end of shares listed at Nasdaq's main market. In Bongs case probably a reflection of poor profitability in the last few years.

EV/EBITDA:~7x

Earnings multiples

Share price, SEK: 0.87	2017	2018	2019E	2020E	2021E
P/E	neg	neg	>100	82.2	10.6
EV/EBITDA *	5.4	7.6	8.8	7.1	5.9
EV/EBIT	10.9	neg	21.5	14.8	11.1

* 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 1.4 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 2.6 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 0.7 per share.

DCF-value, SEK per share					
Sustainable EBIT-margins	**1.0%**	**2.0%**	**3.0%**	**4.0%**	**5.0%**
Annual growth rate 2023-27					
-3.0%	0.43	0.82	1.21	1.60	2.01
0.0%	0.50	0.96	**1.42**	1.88	2.36
3.0%	0.58	1.10	1.64	2.16	2.71
6.0%	0.65	1.25	1.85	2.44	3.07

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 within a couple of growing market segments.

Financials: 1

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	2017	2018	2019E	2020E	2021E
Net sales	2,095	2,220	2,198	2,124	2,058
Total operating costs	-2,004	-2,148	-2,084	-1,989	-1,908
EBITDA	91	71	115	135	150
Depreciation	-40	-45	-84	-84	-83
Amortization	-6	-2	-2	-2	-2
Impairment charges	0	-76	0	0	0
EBIT	45	-52	29	49	65
Share in profits	0	0	0	0	0
Net financial items	-44	-57	-44	-46	-45
Exchange rate dif.	0	0	0	0	0
Pre-tax profit	1	-109	-16	2	20
Tax	-10	-39	-7	0	-3
Net earnings	-12	-149	-23	2	17

BALANCE SHEET	2017	2018	2019E	2020E	2021E
Assets					
Current assets					
Cash in banks	124	72	72	69	67
Receivables	282	289	286	276	268
Inventories	189	195	198	191	185
Other current assets	73	99	99	99	99
Current assets	668	655	654	635	619
Fixed assets					
Tangible assets	209	179	335	331	334
Associated comp.	0	0	0	0	0
Investments	2	1	1	1	1
Goodwill	575	518	518	518	518
Cap. exp. for dev.	0	0	0	0	0
O intangible rights	29	17	16	15	14
O non-current assets	0	0	0	0	0
Total fixed assets	814	716	871	866	867
Deferred tax assets	144	110	110	110	110
Total (assets)	1,626	1,481	1,635	1,611	1,595
Liabilities					
Current liabilities					
Short-term debt	0	0	0	0	0
Accounts payable	240	221	219	212	205
O current liabilities	250	240	240	240	240
Current liabilities	490	461	459	452	445
Long-term debt	418	421	599	581	555
O long-term liabilities	0	16	16	16	16
Convertibles	0	0	0	0	0
Total Liabilities	908	898	1,074	1,048	1,015
Deferred tax liab	22	14	14	14	14
Provisions	0	0	0	0	0
Shareholders' equity	685	569	547	549	566
Minority interest (BS)	11	0	0	0	0
Minority & equity	696	569	547	549	566
Total liab & SE	1,626	1,481	1,635	1,611	1,595

FREE CASH FLOW	2017	2018	2019E	2020E	2021E
Net sales	2,095	2,220	2,198	2,124	2,058
Total operating costs	-2,004	-2,148	-2,084	-1,989	-1,908
Depreciations total	-46	-123	-86	-86	-85
EBIT	45	-52	29	49	65
Taxes on EBIT	-10	11	-6	-7	-10
NOPLAT	35	-57	22	41	55
Depreciation	46	123	86	86	85
Gross cash flow	81	66	109	127	140
Change in WC	10	-68	-2	9	8
Gross CAPEX	-28	-25	-15	-15	-20
Free cash flow	63	-26	40	55	62

CAPITAL STRUCTURE	2017	2018	2019E	2020E	2021E
Equity ratio	43%	38%	33%	34%	35%
Debt/equity ratio	61%	74%	110%	106%	98%
Net debt	294	349	527	512	488
Capital employed	990	918	1,074	1,060	1,054
Capital turnover rate	1.3	1.5	1.3	1.3	1.3

GROWTH	2017	2018	2019E	2020E	2021E
Sales growth	-2%	6%	-1%	-3%	-3%
EPS growth (adj)	-103%	1,105%	-85%	-109%	774%

DCF VALUATION		CASH FLOW, MSEK	
WACC (%)	12 %	NPV FCF (2018-2020)	172
		NPV FCF (2021-2027)	248
		NPV FCF (2028-)	230
		Non-operating assets	72
		Interest-bearing debt	-421
		Fair value estimate MSEK	302
Assumptions 2023-2027 (%)			
Average sales growth	0 %	Fair value e. per share, SEK	1.4
EBIT margin	3 %	Share price, SEK	0.9

PROFITABILITY	2017	2018	2019E	2020E	2021E
ROE	-2%	-24%	-4%	0%	3%
ROCE	4%	-5%	3%	4%	6%
ROIC	3%	-6%	2%	4%	5%
EBITDA margin	4%	3%	5%	6%	7%
EBIT margin	2%	-2%	1%	2%	3%
Net margin	-1%	-7%	-1%	0%	1%

DATA PER SHARE	2017	2018	2019E	2020E	2021E
EPS	-0.06	-0.71	-0.11	0.01	0.08
EPS adj	-0.06	-0.35	-0.11	0.01	0.08
Dividend	0.00	0.00	0.00	0.00	0.00
Net debt	1.39	1.65	2.50	2.42	2.31
Total shares	211.25	211.25	211.25	211.25	211.25

VALUATION	2017	2018	2019E	2020E	2021E
EV	497.8	538.7	711.1	695.3	671.4
P/E	-16.2	-1.3	-8.1	94.1	10.8
P/E diluted	-16.2	-1.3	-8.1	94.1	10.8
P/Sales	0.1	0.1	0.1	0.1	0.1
EV/Sales	0.2	0.2	0.3	0.3	0.3
EV/EBITDA	5.4	7.5	6.2	5.2	4.5
EV/EBIT	11.0	-10.4	24.9	14.3	10.4
P/BV	0.3	0.3	0.3	0.3	0.3

SHARE PERFORMANCE		GROWTH/YEAR	16/18
1 month	-2.3 %	Net sales	2.4 %
3 month	8.8 %	Operating profit adj	-20.5 %
12 month	-27.5 %	EPS, just	34.9 %
Since start of the year	-8.4 %	Equity	-11.4 %

SHAREHOLDER STRUCTURE %	CAPITAL	VOTES
Stéphane Hamelin	25.0 %	25.0 %
Per-Arne Åhlgren	14.4 %	14.4 %
Svolder	7.7 %	7.7 %
Avanza Pension	5.5 %	5.5 %
Theodor Jeansson	4.7 %	4.7 %
Christian Paulsson	4.3 %	4.3 %
John Elvesjö	2.2 %	2.2 %
Dan Drottman	2.1 %	2.1 %
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	0.9
Total shares, million	211.2
Market Cap, MSEK	183.8

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

FINANCIAL INFORMATION	
Q3 report	November 15, 2019
FY 2019 Results	February 13, 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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Disclaimer

Important information
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Redeye Rating (2019-07-16)

Rating	People	Business	Financials
5p	5	4	0
3p - 4p	32	24	15
0p - 2p	32	41	54
Company N	69	69	69

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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.