Milan, 24 July 2023

Italian Equity Research – 2Q23 Preview

PIRELLI & C

OUTPERFORM

Sector: Industrials

Price: Eu4.84 - **Target: Eu6.00**

Solid 2Q23 Expected; FY23 Guidance to be Confirmed; No G.Power Disruption

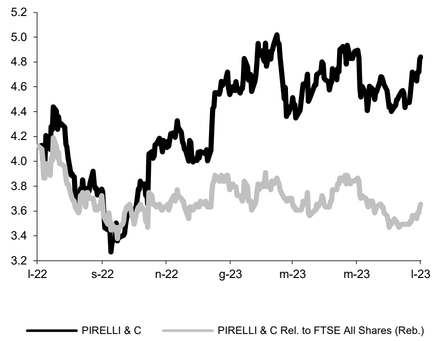
Gianluca Bertuzzo +39-02-77115.429
gianluca.bertuzzo@intermonte.it

Stock Rating			
Rating:			Unchanged
Target Price (Eu):			Unchanged
	2023E	**2024E**	**2025E**
Chg in Adj EPS	0.0%	0.1%	0.2%

Next Event

Results Out 27 of July (after market)

PIRELLI & C - 12M Performance



Stock Data			
Reuters code:			PIRC.MI
Bloomberg code:			PIRC IM
Performance	**1M**	**3M**	**12M**
Absolute	9.2%	3.9%	17.4%
Relative	5.2%	0.8%	-15.2%
12M (H/L)			5.02/3.27
3M Average Volume (th):			2,132.98

Shareholder Data	
No. of Ord shares (mn):	1,000
Total no. of shares (mn):	1,000
Mkt Cap Ord (Eu mn):	4,840
Total Mkt Cap (Eu mn):	4,840
Mkt Float - Ord (Eu mn):	1,848
Mkt Float (in %):	38.2%
Main Shareholder:	
Marco Polo International Italy Srl	45.5%

Balance Sheet Data	
Book Value (Eu mn):	5,516
BVPS (Eu):	5.66
P/BV:	0.9
Net Financial Position (Eu mn):	-2,299
Enterprise Value (Eu mn):	7,307

- **2Q23 preview: price/mix continues to offset cost inflation.** We expect PIRC to report a solid quarter, with price/mix offsetting cost inflation, ForEx headwinds and a slight drop in volumes. Overall, we project revenues up +3% YoY to €1.73bn, with price/mix +9%, volumes -1% and ForEx -5%. Price/mix should largely have benefited from price hikes but also the mix, despite a negative channel mix, as OE production rebounded and replacement demand was still muted. Adj. EBIT is foreseen at €255mn, +1% YoY for a 14.8% margin, thanks to price/mix and efficiencies, more than negating cost inflation (€-90mn headwind in total, -5% of revenues), adverse ForEx and negative volumes.
- **2023 guidance: expecting some tweaks to drivers, but overall figures confirmed; still in line with upper end of range.** We are expecting PIRC to confirm adj. EBIT and cash flow guidance in light of 1H23 results and implicit 2H23 figures. We see this happening with some tweaks to drivers, consistent with 1H trends: stronger price/mix, slightly lower volumes and more negative ForEx. In 2H, pricing should continue to benefit from the carryover effect from 2022 and the last increase applied from May/June, while cost inflation should reduce its bite on earnings thanks to raw material and energy costs. Our estimates remain consistent with the high-end of the range and envisage: revenues of €6.7bn (guidance €6.6-6.8bn), adj. EBIT of €984mn for a 14.6% margin (guidance €929-988mn, >14-14.5% margin) and net cash flow of €471mn (guidance €440-470mn).
- **Golden Power: non-disruptive outcome.** In mid-June, the Italian Cabinet announced the outcome of the golden power review in relation to the renewal of the shareholder agreement between China National Tire and Rubber Corporation (CNRC) and Camfin. In brief, the proceeding led to a scenario consistent with our view, limiting CNRC's influence on PIRC; it ensures PIRC management's independence and the financial nature of CNRC's investment. Harsher scenarios, including the freezing of CNRC voting rights and/ or a forced sale of its shares have been avoided. In light of this situation, we believe there is little pressure on CNRC to sell its stake and any transaction concerning its stake will be handled in an orderly manner (i.e. no share placement).
- **BRE+PIRC combination: any deal should offer a premium to PIRC shareholders.** In a recent report (link here), we analysed the potential consequences of BRE's proposal to relocate its registered office to Netherlands to provide shareholders a strengthened voting rights mechanism to be exploited in M&A. We found FIVE smoking guns clearly pointing to PIRC as the candidate for the transformational deal BRE is seeking. We are nevertheless sceptical on the short-term value creation potential of such a deal from business and valuation perspectives, and find the rationale relatively weak for minority shareholders. However, we expect any deal to include a premium to PIRC shareholders, as they would basically cede control to BRE's main shareholder.
- **Change in estimates.** We are adjusting our top line forecast as explained above (P&M+, Vol-, ForEx-), but our EBIT and cashflow estimates are unchanged thanks to P&M.
- **Investment case.** We expect PIRC to report a solid quarter and confirm guidance, with indications that may point to the upper end of the range. While recently the stock has recovered slightly, it had been weak since mid-May, probably due to the Golden Power proceedings. As explained above, however, we believe the outcome will not be disruptive, with management's autonomy and the financial nature of CNRC's investment reiterated. In addition, while we are not including any speculative premium, deeming it premature, BRE's moves suggest PIRC would be the M&A candidate and the change in control should deserve a premium. Given the resilient business model, last year's underperformance, and the attractive valuation despite higher cash generation, we confirm our OUTPERFORM rating on the stock.

Key Figures & Ratios	**2021A**	**2022A**	**2023E**	**2024E**	**2025E**
Sales (Eu mn)	5,331	6,616	6,727	6,971	7,228
EBITDA Adj (Eu mn)	1,211	1,408	1,424	1,511	1,578
Net Profit Adj (Eu mn)	469	570	516	585	633
EPS New Adj (Eu)	0.469	0.570	0.516	0.585	0.633
EPS Old Adj (Eu)	0.469	0.570	0.516	0.584	0.632
DPS (Eu)	0.161	0.218	0.164	0.199	0.226
EV/EBITDA Adj	6.9	5.3	5.1	4.5	3.9
EV/EBIT Adj	10.3	7.6	7.4	6.3	5.5
P/E Adj	10.3	8.5	9.4	8.3	7.6
Div. Yield	3.3%	4.5%	3.4%	4.1%	4.7%
Net Debt/EBITDA Adj	2.4	1.8	1.6	1.3	1.0