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Haitong Bank restarted coverage on R22 with a BUY rating and FV at PLN 67.6.

#### **Valuation Methodology**

We value R22 Group using two methods: DCF (Sum of the Parts), EV/EBITDA where each method has an equal weight of 50%. We value R22 Group at PLN 958m or PLN 67.6/share, which implies 25% upside potential.

#### **Risks to Fair Value**

**M&A execution risk:** The increase in the number of customers is to take place both through organic growth and through acquisitions. The possibility of acquiring potential targets or not being able to obtain them at a price regarded by R22 as attractive may have a negative impact on R22's future assets and financial position as well as its market position.

**Risk of changes in the rules of domain registration in Poland:** One of the activities of R22 Group is hosting, among others, and sales of domain names. Internet domains sold by H88 entities are registered by the NASK, which is a state research institute supervised by the Ministry of Digitalization. NASK acts as a national register of Internet names in the .pl domain, ie. pl, org.pl, info.pl, com.pl, net.pl, regional domains like waw.pl, and gov.pl domains, is an active member of the CENTR (Council of European National Top-Level Domain Registries) and works closely with the organization that coordinates the Internet Corporation for Assigned Names and Numbers (ICANN). Possible legislative changes, leading to a change in the entity conducting the national Internet name register or change of the registration rules could adversely affect the future financial situation of R22 as well as its market position.

**The risk of changing the rules of transferring Internet domains between entities in Poland:** An important issue relating to how the Internet domain market works is the ability to transfer domains between hosting companies. In R22's opinion, the existing practise is unfavorable for domain owners because it is based on the need to generate special requests and to obtain permission to change the domain controller from its hosting company. Implementing regulations to facilitate the transfer of domains based on the model of the telecommunications market would significantly change the hosting market, which would, on the one hand, involve the risk of exposing some of H88's customers to competition. On the other hand it would give R22 the opportunity to acquire some of its competitors. Liberalising the market in terms of domain transferability could have a negative impact on the business, development prospects, financial position or performance of the R22 Group.

**Risks associated with activity in the telecommunications market in Poland:** The telecommunications market in Poland is characterized by strong competition and relative fragmentation of the entities operating in it, which translates into low - against other European Union countries - prices of access to telecommunications services. In addition, the market is clearly seeing a fixed-to-mobile substitution trend with the displacement of fixed services by mobile services. After the 800/2600MHz spectrum auction, all mobile operators are investing in an LTE network rollout and are starting to offer LTE mobile data packages as an alternative for low quality fixed-internet. At the same time, we should see increased investment in fixed-line networks as some operators upgrade their networks to NGA (Next generation Access) technology. This can result in increased competition in the market and risk of client erosion or ARPU pressure

**The risk associated with the possibility of introducing payments for frequencies needed to offer the Internet by radio:** The R22 Group operates in the telecommunications market via the Oxyllion Group. One of the activities is the provision of the Internet by radio, which is provided via frequency bands that do not incur state fees, or concession fees. However, there is a risk of introducing concession fees or other public law fees, like the charges for using frequencies used by mobile telephony, which could have a negative impact on the business, its development prospects, financial situation or group results.

**Risk of operating costs of the Omnichannel Communication segment:** The R22 Group conducts multi-channel communications with the use of electronic channels (omnichannel communication). One of its elements is the mass mailing of SMS messages via telecom operators, provided by the Vercom Group. On January 31st, 2017, the Telco Regulator (UKE) decided to liberalise wholesale prices of SMS in the wholesale market from May 2017, ie transactions between telecommunications operators. Earlier the price was regulated and was PLN 0.05 per message. Despite the fact that R22 has not recorded any significant changes in wholesale purchase prices since then, as a result of market liberalization SMS prices may fluctuate, both lower and higher than previously, which may adversely affect its business, development prospects, financial situation or results.

**Risk of losing competitive position in the market:** Due to the relatively short period of operation of the areas in which R22 operates (especially Vercom), they may undergo significant and dynamic changes as well as significant changes in competition also coming from consolidation processes in all of R22's markets.

**Risk of loss of customers:** Increasing competition in R22 markets, technological development and consolidation processes can lead to intensified competition resulting in the client base reduction of R2 Group.

**Risk related to the failure of equipment and IT systems:** R22's business is based on modern IT and telecommunication systems, including external and internal servers. R22 clients expect properly-functioning equipment and computer hardware which may break, resulting in a worsening client perception of R22 services and ultimately the client leaving.

**Risk of cyber-attacks:** Given its management of IT infrastructure, especially servers belonging to the R22 Group and its clients (own servers), the business activities of R22 are exposed to attacks by cybercriminals. The two most serious types of potential attacks include attacks aimed at damaging infrastructure and so-called DDoS attacks, which is to block the servers, with very large, artificially loaded traffic. Despite the systematic improvement and modernisation of the solutions used, it cannot be ruled out that they will prove insufficient in the future, which may adversely affect R22's results and financial position.

**Risk related to the use of Oxyllion Group infrastructure by other R22 entities:** H88 Group and Vercom Group use infrastructure under the control of Oxyllion Group. If R22 decides to cease providing services related to Internet access or data transmission for any reason, including possible disposal of some or all of the assets that make up the Oxyllion Group, the conditions of access to the Internet and the data transmission service may deteriorate for other entities of R22 Group and may increase the costs of these services.

**Risk related to the large-scale processing of personal data:** As part of its day to day operations, R22 Group processes large amounts of personal data which must be carried out in a manner consistent with the provisions concerning the protection of personal data in force in Poland. There is a risk that despite the application of technical and organizational measures to protect the processing of personal data, there will be a breach of legal obligations by any entity of the R22 Group in this regard, in particular the disclosure of personal data to unauthorized persons. In case of a breach of legal regulations related to the protection of personal data, in particular the disclosure of personal data in an unlawful manner, R22 Group may be exposed to criminal or administrative sanctions and this may have a negative impact on R22's business, development prospects, financial position or results.

**Risks associated with the operation of search engines on the Internet:** Many brands of R22 Group acquire customers through Internet marketing mechanisms. In particular, they are included in the search results, primarily in Google Search, which provides over 90% of searches in Poland. This means any change in search algorithms used by Google may affect the visibility of the Issuer's brand pages in search results and, consequently, affect the way it reaches potential customers.

**Risk related to the macroeconomic environment:** Changes in the macroeconomic environment, including economic growth, inflation, unemployment and interest rates, can affect R22's ability to create value. This in particular concerns the activities of the Vercom Group, whose services are more prone to the economic downturn than those offered by the H88 Group and the Oxyllion Group.



Risk related to cost increases: Prices of services offered are calculated on the basis of the analysis of variable costs and fixed costs, including, in particular, the costs of leasing telecommunications infrastructure and the costs of purchasing telecommunications services. Due to the construction of some contracts with clients that do not allow for an increase in the remuneration for services provided by companies within the R22 Group over the life of the contract, significant changes in unit variable costs (some or all) or loss of control over fixed costs may have a negative impact on activity, development prospects, financial position or results of the R22 Group.

The risk of changes in the law: Frequently changing legislation, which entails a change in their interpretation, significantly impedes business operations and significantly limits the predictability of financial results. Particularly important are the provisions that shape the tax system, which are frequently modified.

#### **IMPORTANT DISCLOSURES**

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