EDISON

4iG

H121 update

M&A set to launch 4iG into orbit

IT services

Driven by a combination of organic growth and M&A, 4iG reported H121 net revenues of HUF32.1bn, 59% y-o-y growth. Gross profit rose by 65% y-o-y to HUF10.2bn with EBITDA rising 30% y-o-y to HUF1.8bn, as EBITDA margins fell to 5.5%. Together with a forward order book of HUF42.7bn, 4iG looks on track to meet our FY21e revenue estimate. However, 4iG also has a full M&A pipeline, with five deals still expected to complete in H221, DIGI Group, Spacecom, Antenna Hungária, Telenor Montenegro and TeleGroup, which will transform the group. We estimate that, collectively, these deals will deliver run-rate EBITDA in excess of c HUF88bn (c US$300m). Although we are not yet in a position to update our estimates for these acquisitions, on our current forecasts 4iG trades on an FY21 P/E of 16.1x and EV/EBITDA of 9.7x, offering an historic dividend yield 2.5%.

Year end	Revenue (HUFbn)	PBT* (HUFbn)	EPS* (HUF)	DPS (HUF)	P/E (x)	Yield (%)
12/19	41.1	3.3	31.5	22.0	28.9	2.4
12/20	57.3	4.2	37.2	22.5	24.5	2.5
12/21e	82.7	7.3	56.6	37.2	16.1	4.1
12/22e	93.0	8.5	64.5	42.0	14.1	4.6

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

H121 results: On track to meet revenue estimates

H121 revenues were driven by a combination of organic growth and M&A. 4iG reported H121 net revenues of HUF32.1bn, 59% growth y-o-y. Gross profit rose by 65% y-o-y to HUF10.2bn with EBITDA rising 30% y-o-y to HUF1.8bn, as H121 EBITDA margins fell to 5.5% from 6.7% in H120. Employee costs rose substantially in H121, with a doubling of headcount year-on-year (to 1,256 employees) and rising wages in a tight employment market. Following its H121 HUF15.5bn bond issue, to support M&A net debt rose to HUF11.8bn. H121 revenues, together with a forward order book of HUF42.7bn, total HUF74.8bn, 90% of our FY21e revenue estimate.

H221 M&A not yet included in our estimates

4iG completed four acquisitions in H121: Poli Computer and SpaceNET in IT services, Rotors & Cams in space and defence and Hungaro DigiTel (HDT) in telecoms services, together adding HUF7bn to FY21 revenues and HUF1.8bn to EBITDA. Invitech completed in Q321, but 4iG still has five deals expected to complete in H221 (DIGI Group, Spacecom, Antenna Hungária, Telenor Montenegro and TeleGroup). These are major deals but, with consideration, multiples and sources of funding to be disclosed, our estimates remain unchanged for now as we are not yet in a position to include these acquisitions in our estimates.

Valuation: FY21 discount to peers

Pre-close of the DIGI Group, Spacecom, Antenna Hungária, Telenor Montenegro and TeleGroup deals, 4iG trades on an FY21 P/E of 16.1x and EV/EBITDA of 9.7x, offering a historic yield of 2.5%. On a pro-forma basis, the acquisitions of DIGI Group and Spacecom look set to generate a run-rate EBITDA of HUF88bn (c US$300m), transforming 4iG and creating a substantially enlarged group.

13 October 2021

Price	**HUF910**
Market cap	**HUF87.9bn**
	HUF360.4/€
Net debt (HUFbn) at 30 June 2021	11.8
Shares in issue	98.4m
Free float	35.6%
Code	4iG
Primary exchange	Budapest
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(10.8)	44.9	55.8
Rel (local)	(13.9)	26.8	(5.6)
52-week high/low	HUF1,094	HUF505	

Business description

4iG is a leading Hungarian IT services and systems integrator, working with public sector clients, large corporates and SMEs. Management is focused on becoming the market leader in Hungary by FY22 as well as targeting expansion in Central and Eastern Europe.

Next events

Q321 results	25 November 2021
FY21 summary results	February 2022

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Edison profile page

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H121 results

H121 results on track, overshadowed by pending M&A

H121 revenues were driven by a combination of organic growth and M&A. 4iG reported H121 net revenues of HUF32.1bn, 59% growth y-o-y (H120: HUF20.2bn). Gross profit rose by 65% y-o-y to HUF10.2bn (H120: HUF6.2bn) with EBITDA rising 30% y-o-y to HUF1.8bn (H120: HUF1.4bn), as H121 EBITDA margins fell to 5.5% from 6.7% in H120. Employee costs rose substantially in the period, both from a year-on-year doubling of headcount (H121: 1,256 employees, H120: 644) and rising wages in a tight domestic employment market. Net income fell 36% y-o-y to HUF0.5bn (H120: HUF0.8bn), with EPS falling by 38% to HUF5.3 (H120: HUF8.5). H121 net debt rose to HUF11.8bn, from net cash of HUF2.7bn for FY20 (H120: HUF0.0bn). The major cash outflows have been to fund working capital (trade creditors increased to HUF10.7bn in H121, from HUF4.6bn in H120) as the business has grown, together with HUF11.5bn (H120: HUF0.5bn) spent on M&A, funded by 4iG's maiden HUF15.45bn bond issue.

Exhibit 1: Summarised H121 results

HUFbn	H120	H121	Y-o-y growth	FY20	H220	H221e	Y-o-y growth	FY21e
Net revenues	20.2	32.1	59%	57.3	37.1	50.6	36%	82.7
Gross profit	6.2	10.2	65%	15.9	9.8	14.8	52%	25.0
margins	*30.6%*	*31.7%*		*27.8%*	*26.3%*	*29.3%*		*30.2%*
EBITDA	1.4	1.8	30%	5.0	3.7	7.1	94%	8.9
margins	*6.7%*	*5.5%*		*8.8%*	*9.9%*	*14.1%*		*10.8%*
Operating profit	1.0	0.9	(7)%	4.2	3.2	7.1	120%	8.0
PBT	1.0	0.8	(16)%	4.2	3.2	6.4	102%	7.3
PAT	0.8	0.5	(36)%	3.4	2.7	5.5	105%	5.9
EPS - basic reported (HUF)	8.5	5.3	(38)%	37.7	29.2	55.7	91%	61.0
Net debt/(cash)	0.0	11.8		(2.7)	(2.7)	5.7		5.7

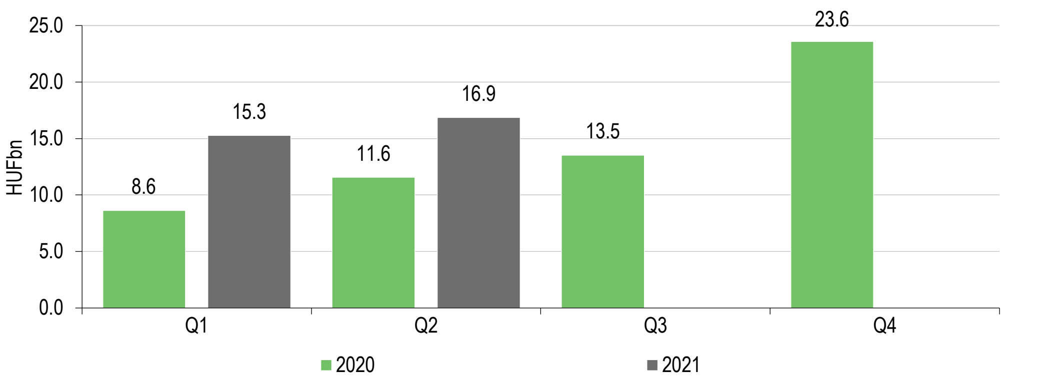
Source: Company accounts, Edison Investment Research

HUF43bn order book for FY21

H1 revenues are typically c 40% of annual revenues, with H121 revenues c 39% (H120: 35% of FY20) of our FY21 revenue estimate of HUF82.7bn. The FY21 forward order book reached HUF42.7bn on 27 August 2021 (H120: HUF20.8bn). As an indicator, total revenues, including H121 and the identified forward order book, adds up to HUF74.8bn, 90% of our FY21 revenue estimate, with the expectation of additional orders to be received during the remaining four months of the year. With significant acquisitions also expected to be completed in H221 (notably Antenna Hungaria, DIGI Group and Spacecom), we have few concerns the FY21 revenue target will be met. However, we are yet to be in a position to reflect these acquisitions in our forecasts.

With the acquisition of Poli Computer and HDT, employee headcount increased to 1,256, a third higher than 31 March 2021 (Q121: 944), bringing in specialist expertise and greater capacity.

Exhibit 2: Quarterly revenues – FY21 vs FY20

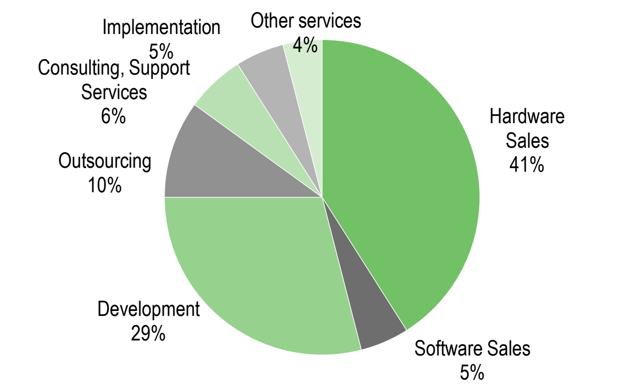


Source: 4iG

Segmental analysis: Strengthening development capabilities

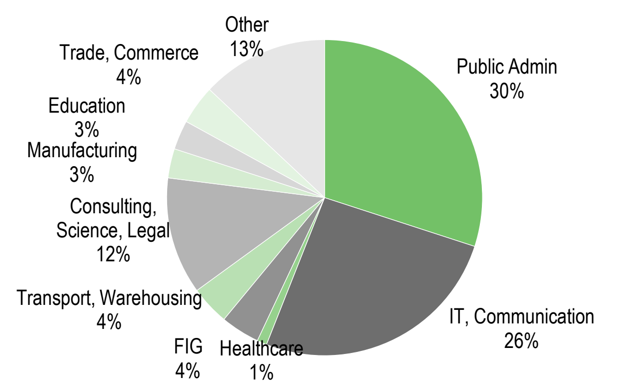
The breakdown of revenue by segment has shifted somewhat from H120, with acquisitions driving an increase in higher margin software development revenues (+9pp y-o-y), largely at the expense of hardware and software reselling revenues (together, -12pp y-o-y) which were partly constrained by global supply chain challenges. 4iG has also been awarded a number of large, multi-year development projects, providing revenue visibility over multiple years. At 17%, recurring revenues continue to increase slowly as a proportion of total revenues, from 16% as at H120 and 14% as at FY20.

Exhibit 3: H121 revenues by service line



Source: 4iG

Exhibit 4: H121 revenues by client type



Source: 4iG

Public sector clients continue to represent the majority of 4iG's business (H121: 68%), with large corporates 19% of the total and SMEs 13%. In terms of sectors, public administration, together with IT and telcos remain the largest two sectors, representing 56% of total revenues in H121, up from 41% for H120. Consulting, science and legal was the only other sector with double-digit revenue share (12%).

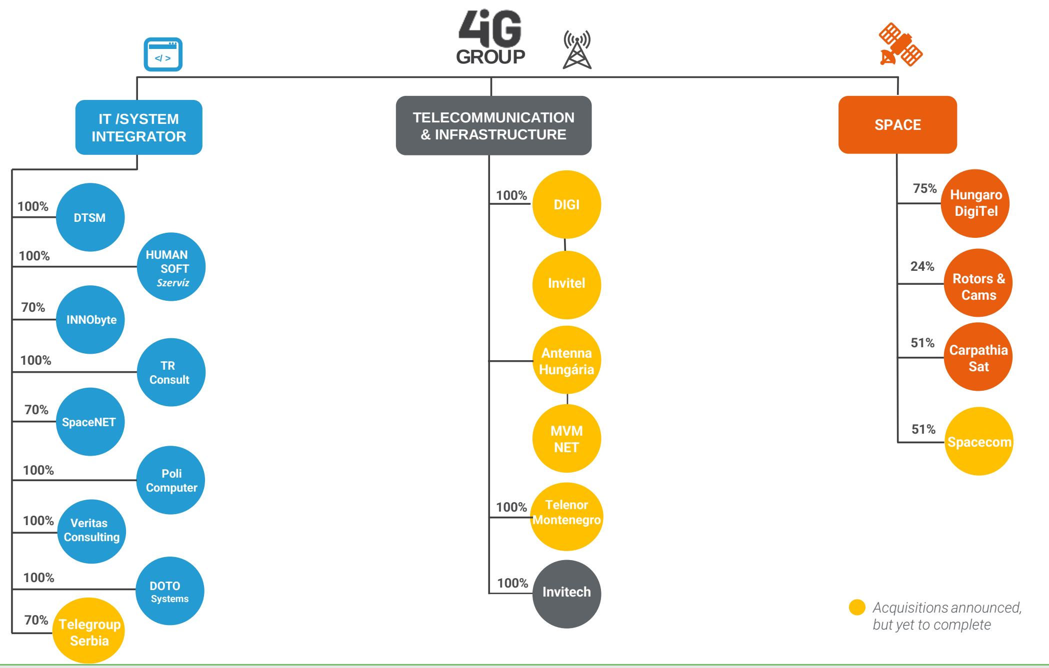
4iG M&A focused for FY21

Building its three-pillar strategy for market leadership

Management is aiming for 4iG to become the number one IT systems integrator in Hungary by the end of FY22, and a significant regional player across the CEE and the Balkans. This strategy accelerates 4iG's move away from a lower-margin software and hardware reselling business model towards the higher margins and longer-term contracts available in telecoms services (although we would note the fall in H121EBITDA margins to 5.5%, although we expect these to strengthen in H221). Where a skillset does not exist internally, management expects to hire or acquire expertise, with acquisitions also used to broaden the company's geographical footprint, sector expertise and track record.

4iG's CarpathiaSat JV (August 2020) with its strategic partner, Antenna Hungária, laid the groundwork for 4iG's ambitions in space, further consolidated by its H121 minority investment in Rotors & Cams. 4iG's Q121 majority investment in HDT represented the next step in 4iG's strategic relationship with Antenna Hungária (which retains a 25% minority holding in HDT), diversifying 4iG's presence in the telecoms and infrastructure sector and offering better revenue visibility through longer-term contracts and higher EBITDA margins than IT services. When it completes, DIGI Group will complement HDT, strengthening the group's position as a leading Hungarian telecoms services provider.

Exhibit 5: Acquisitions have driven new focus sectors



Source: 4iG. Note: Orange circles denote acquisitions that have been announced but have yet to complete.

M&A: H121, a busy period for acquisitions

4iG's M&A strategy remains aligned with its growth strategy, with management expecting continued robust organic growth (4% growth forecast in Hungarian IT market 2020–25) to be complemented by acquisitions in the coming years. Management also remains open to considering strategic partnerships and JVs, including long-term cooperation with European or other international groups with complementary resources.

In H121, 4iG announced five acquisitions, four of which have completed (DIGI Group is expected to complete in H221): Poli Computer and SpaceNET in IT services, Rotors & Cams in space and defence and HDT in telecoms services, adding a further HUF7bn to FY21 revenues and HUF1.8bn to EBITDA. We have already discussed these acquisitions in our note Executing at pace on its five-year plan. Additionally, the acquisition of Invitech was announced and completed in September 2021 (summarised below).

Five further transactions expected to complete in H221

Following the four transactions completed in H121 and Invitech, that completed in Q321, 4iG has a further five announced deals that have yet to complete. Consideration, acquisition multiples and sources of funding have not been disclosed for these acquisitions, however, on a pro-forma basis, the acquisitions of DIGI Group and Spacecom alone look set to generate run-rate EBITDA of HUF88bn (c US$300m), unlocking substantial debt funding capacity for the enlarged group.

- **Invitech**: in September 2021, 4iG both announced and completed the acquisition of Invitech, a corporate telecoms and IT/network infrastructure solutions provider, following clearance by the Hungarian Competition Authority. Invitech provides broadband, data centre, IT security and cloud solutions, with more than 600 employees, it provides wholesale services to more than 5,000 corporate, institutional, and wholesale customers. The company has its own fibre-optic network, the second largest in Hungary, as well as five data centres, and its infrastructure services are used by all the domestic mobile operators. Invitech's FY20 revenues were HUF24.8bn (US$84m), with EBITDA of HUF9.0bn.
- **DIGI Group**: on 29 March 2021, 4iG signed a preliminary, non-binding agreement with the Romanian RCS & RDS consortium to acquire the Hungarian telecoms services business, DIGI Távközlési Szolgáltató and its subsidiaries (DIGI Group). The acquisition is subject to due diligence and competition authority approvals, but management expects it to complete in H221. Although consideration has not been disclosed, based on FY20 figures, DIGI Group would add a further HUF70bn of revenues and HUF19bn of EBITDA (27% margin), implying pro-forma group FY21 revenues of HUF153bn and EBITDA of HUF28bn (c 18% margin). DIGI Group employs over 3,000 people and serves more than 1.1m subscribers and, as such, is a transformative acquisition that would position 4iG as a leading Hungarian telecoms services company.
- **Telenor Montenegro**: on 9 June 2021, 4iG entered into a non-binding preliminary agreement with PPF Telecom Group to acquire Telenor Montenegro. Telenor Montenegro is the leading mobile operator in Montenegro, with 338,000 subscribers, 150 base stations and national 4G coverage. Following due diligence, the successful completion of the transaction is subject to the approval of the Montenegro authorities, expected in H221.
- **Spacecom**: in June 2021, 4iG, HDT and CarpathiaSat entered into a preliminary agreement to acquire a 51% stake in Spacecom, a geosynchronous satellite operator and service provider listed on the Tel Aviv Stock Exchange. On 12 October, a further announcement confirmed that completion is no longer subject to due diligence and as such, completion is subject only to approval by Spacecom's General Assembly at an extraordinary general meeting (EGM) and the approval of the Israeli Ministry of Communications. Spacecom provides satellite services in Hungary and the region through three AMOS satellites. The acquisition provides knowledge transfer to 4iG and will also help the group to develop international strategic partnerships.
- **Antenna Hungária**: on 25 August 2021, 4iG announced it had entered into a preliminary agreement with the Hungarian government to acquire a majority stake in Antenna Hungária. Under the terms of the agreement, 4iG's telecoms assets will be injected into a company jointly held with the Hungarian state, together with Antenna Hungária. The terms of the transaction and the respective final shareholdings are to be agreed following due diligence and an asset valuation exercise, to be concluded by mid-October 2021. The intention of both parties is to establish a strategic champion in the telecoms services sector, backed by both public and private capital, to represent Hungarian national interests.
- **TeleGroup**: on 20 September 2021, 4iG announced the acquisition of a 70% majority stake in TeleGroup, a family-owned IT systems integrator in the west Balkans, with a 28-year track record in Serbia, Bosnia and Herzegovina and Montenegro. The acquisition is expected to complete in FY21, subject to due diligence and competition authority approval. TeleGroup employs over 250 staff in the Balkans, with FY20 revenues of €64m and EBITDA of €5.3m (8.3% EBITDA margin). TeleGroup provides IT solutions and telecoms engineering services and is a systems integrator for network and data centre services, IoT, cybersecurity and

managed IT solutions. The group supports large public and private sector companies primarily in the healthcare, finance, energy, transportation, retail, and education sectors.

With the Hungarian market still highly fragmented, management continues to review M&A opportunities. Although we do not anticipate any further major deals to be announced before the completion of DIGI Group, thereafter we expect 4iG to follow an opportunistic regional expansion strategy, building on client contracts to land and expand in nearby or adjacent markets.

Credit rating: 4iG rated BB- by Scope Ratings

Scope Ratings gave 4iG a BB-/Stable issuer rating ahead of its acquisition of HDT and the issue of the group's initial 10-year bond as part of the Central Bank of Hungary's growth bond programme. 4iG issued the HUF15.45bn (c €43m) bond on 29 March 2021, with a 10-year maturity and offering a 2.9% coupon. Subsequently, on 25 June 2021, Scope Ratings placed 4iG's BB- issuer rating under review for a developing outcome, pending completion of the Spacecom and DIGI Group transactions. Most recently, on 24 September 2021, Scope Ratings changed 4iG's BB- issuer rating to under review for a possible downgrade, reflecting heightened execution and integration risk given 4iG's large and numerous potential acquisitions as well as its limited exposure to telecom services.

4iG reported net debt of HUF11.8bn at 30 June 2021 (net cash of HUF2.7bn at 31 December 2020), reflecting its HUF15.45bn (c €43m) 10-year bond, less cash spent on its H121 acquisitions and increases in working capital. Given a lightly geared balance sheet, together with contributions from DIGI Group and Spacecom that look set to generate run-rate EBITDA of HUF88bn (c US$300m), we would expect management to fund the acquisitions with a substantial increase in debt as well as equity.

Upward revision to our estimates pending

Our estimates do not take account of the significant M&A expected to complete in Q421. Until we have better clarity on the terms and impact of the outstanding acquisitions, we are not in a position to revise our estimates as 4iG has yet to provide any details of the structure or consideration for the announced deals. However, given 4iG's lightly geared balance sheet with the significant additional debt capacity from the enlarged group, we would not be surprised if 4iG went back to the bond markets to part-fund its acquisitions with a further bond issue.

Exhibit 6: Financial summary

Year end 31 December	HUFm	2019	2020	2021e	2022e
INCOME STATEMENT		IFRS	IFRS	IFRS	IFRS
Revenue		41,129	57,300	82,710	93,048
Cost of Sales		(30,126)	(41,372)	(57,723)	(64,936)
Gross Profit		11,003	15,928	24,987	28,112
EBITDA		4,075	5,047	8,916	9,903
Normalised operating profit		3,332	4,211	8,000	8,897
Amortisation of acquired intangibles		0	0	(133)	(133)
Exceptionals		0	0	0	0
Share-based payments		0	0	0	0
Reported operating profit		3,332	4,211	7,867	8,764
Net Interest		(18)	(36)	(747)	(386)
Joint ventures & associates (post tax)		0	0	0	0
Exceptionals		0	0	0	0
Profit Before Tax (norm)		3,314	4,175	7,254	8,511
Profit Before Tax (reported)		3,314	4,175	7,120	8,377
Reported tax		(488)	(736)	(1,306)	(1,617)
Profit After Tax (norm)		2,827	3,439	5,923	6,868
Profit After Tax (reported)		2,827	3,439	5,815	6,760
Minority interests		66	(46)	(526)	(526)
Discontinued operations		0	0	0	0
Net income (normalised)		2,893	3,393	5,398	6,342
Net income (reported)		2,893	3,393	5,289	6,235
Basic average number of shares outstanding (m)		91.7	91.3	95.3	98.4
EPS - basic normalised (HUF)		31.54	37.17	56.62	64.49
EPS - diluted normalised (HUF)		30.77	36.09	55.88	63.67
EPS - basic reported (HUF)		30.82	37.68	60.99	68.74
Dividend (HUF)		22.00	22.49	37.24	42.00
Revenue growth (%)		193.6	39.3	44.3	12.5
Gross Margin (%)		26.8	27.8	30.2	30.2
EBITDA Margin (%)		9.9	8.8	10.8	10.6
Normalised Operating Margin		8.1	7.3	9.7	9.6
BALANCE SHEET					
Fixed Assets		1,948	3,989	20,193	23,966
Intangible Assets		890	2,043	9,975	13,271
Tangible Assets		322	777	5,015	5,493
Lease rights		636	966	3,000	3,000
Investments & other		101	203	2,203	2,203
Current Assets		22,161	33,874	59,634	70,306
Stocks		523	3,360	4,041	5,195
Debtors		12,892	17,494	24,813	27,914
Cash & cash equivalents		6,238	7,205	20,243	26,658
Other		2,508	5,815	10,538	10,538
Current Liabilities		(18,225)	(29,117)	(39,952)	(43,245)
Creditors		(16,361)	(25,628)	(36,464)	(39,756)
Tax and social security		0	0	0	0
Short term borrowings		(1,500)	(3,019)	(3,019)	(3,019)
Other (including finance lease liabilities)		(364)	(470)	(470)	(470)
Long Term Liabilities		(392)	(1,067)	(21,494)	(21,494)
Long term borrowings		0	0	(19,042)	(19,042)
Other long term liabilities		(392)	(1,067)	(2,451)	(2,451)
Net Assets		5,493	7,679	18,381	29,534
Minority interests		64	(376)	(414)	(462)
Shareholders' equity		5,556	7,303	17,967	29,072
CASH FLOW					
Op Cash Flow before WC and tax		4,075	5,047	8,916	9,903
Working capital		3,587	(797)	(1,886)	(964)
Exceptional & other		(5)	91	0	0
Tax		(415)	(773)	(950)	(1,617)
Net operating cash flow		7,243	3,568	6,080	7,322
Capex		(1,471)	(1,230)	(4,527)	(825)
Acquisitions/disposals		3	(383)	(7,007)	0
Net interest		(13)	(42)	(747)	(386)
Equity financing		185	(495)	0	0
Change in finance lease		(356)	28	0	0
Dividends		0	(2,001)	(2,212)	(3,694)
Other		36	(323)	0	0
Net Cash Flow		5,626	(878)	(8,413)	2,416
Opening net debt/(cash)		1,587	(4,039)	(2,740)	5,673
FX		0	30	0	0
Other non-cash movements		0	(451)	0	0
Closing net debt/(cash)		(4,039)	(2,740)	5,673	3,257

Source: 4iG accounts, Edison Investment Research

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