EDISON

# 4iG

Q321 update

## New regional ICT/telecoms group emerging

IT services

**4iG's management is delivering on its promises, with the creation of a new regional ICT/telecoms group, funded by a bond placing (HUF371bn raised in December 2021) and HUF125bn equity raise (ongoing). 4iG has also announced a strategic partnership with Rheinmetall, a leading German defence group, which has agreed to take a 25.1% stake in 4iG, as part of the equity placing, alongside Gellért Jászai (4iG's chairman and CEO), who will retain a majority stake in the group. The placing will be at a share price of HUF670 (an 18% discount to 4iG's latest closing share price). Although our estimates do not take into account recent and pending M&A (a further four M&A deals are expected to complete in Q122 - Spacecom, Antenna Hungária, One and ALBtelecom), Scope Ratings expects total pro forma FY21 revenues of c HUF380bn and EBITDA above HUF100bn.**

| Year end | Revenue (HUFbn) | PBT* (HUFbn) | EPS* (HUF) | DPS (HUF) | P/E (x) | Yield (%) |
|---|---|---|---|---|---|---|
| 12/19 | 41.1 | 3.3 | 31.5 | 22.0 | 26.1 | 2.7 |
| 12/20 | 57.3 | 4.2 | 37.2 | 22.5 | 22.1 | 2.7 |
| 12/21e | 82.7 | 7.3 | 55.5 | 36.5 | 14.8 | 4.4 |
| 12/22e** | 93.0 | 8.5 | 62.0 | 40.0 | 13.3 | 4.9 |

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments. **FY22 estimates not yet adjusted for M&A.

## 9M21 results: 4iG on track to meet revenue estimates

4iG reported net revenues for the first nine months of FY21 (9M21) of HUF53bn, a 58% rise y-o-y (9M20: HUF34bn), with EBITDA up 25% to HUF3.5bn (9M20: HUF2.8bn) and net profit of HUF2.9bn, a 56% rise y-o-y (9M20: HUF1.9bn). The 9M21 EBITDA margin is 6.6%, meaningfully lower than the group's 9M20 margin of 8.4%. As a result, although 4iG has delivered 64% of our FY21 revenue estimate, the group has reached only 40% of our EBITDA estimate ytd. However, we recognise that Q4 is 4iG's seasonally strongest quarter and will be further boosted by the acquisition of Invitech and other deals closing in Q421. Management is confident that 4iG remains on track to become the leading Hungarian IT systems integrator in 2022, as well as having a significant presence in the Western Balkans.

## New strategic partnership with Rheinmetall

Following the announcement in November 2021, 4iG confirmed on 25 January 2022 that Rheinmetall intended to take a 25.1% stake in 4iG, becoming its largest international strategic investor and accelerating its position as a leading security technology systems supplier in CEE. Rheinmetall, together with iG COM, Gellért Jászai's investment vehicle, and Alpac Capital, a private equity group, has agreed to subscribe to a HUF125bn private placing in 4iG at HUF670 per share, a 20% discount to 4iG's average closing price (HUF835) prior to approval of the resolution.

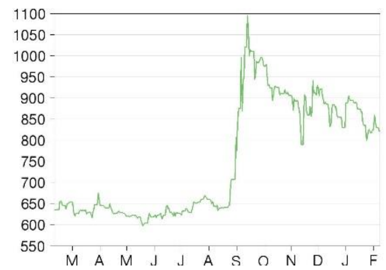
## Valuation: Focus on the enlarged group

Pre-close of its announced M&A deals, 4iG trades on an FY21e P/E of 14.8x and EV/EBITDA of 9.1x, offering a historical yield of 2.7%. On a pro forma basis, based on Scope Ratings estimates, the acquisitions look set to lead to run rate FY21 revenues of HUF380bn (c €1.1bn) and EBITDA of HUF100bn (c €280m). This would transform 4iG's prospects, creating a group with more attractive EBITDA margins, higher recurring revenues and an expanding regional footprint.

**9 February 2022**

| | |
|---|---|
| **Price** | **HUF822** |
| **Market cap** | **HUF84.1bn** |
| | HUF353/€ |
| Net debt (HUFbn) at 30 June 2021 | 11.8 |
| Shares in issue | 102.4m |
| Free float | 35.6% |
| Code | 4iG |
| Primary exchange | Budapest |
| Secondary exchange | N/A |

### Share price performance




| % | 1m | 3m | 12m |
|---|---|---|---|
| Abs | (8.1) | (8.2) | 29.5 |
| Rel (local) | (9.6) | (6.0) | 8.3 |
| 52-week high/low | HUF1094 | HUF598 | |

### 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

| | |
|---|---|
| FY21 preliminary results | February 2022 |

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Edison profile page

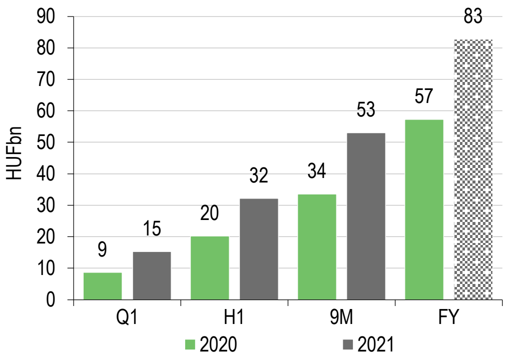

***4iG is a research client of Edison Investment Research Limited***

# 9M21 results

## 9M21 revenues on track

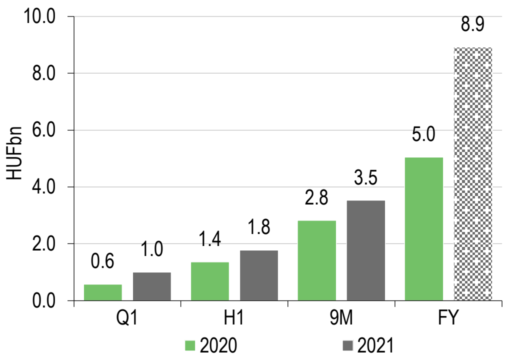
4iG reported 9M21 net revenues of HUF53bn, a 58% rise y-o-y (9M20: HUF34bn), with EBITDA up 25% to HUF3.5bn (9M20: HUF2.8bn) and net profit of HUF2.9bn, a 56% rise y-o-y (9M20: HUF1.9bn). The 9M21 EBITDA margin is 6.6%, meaningfully lower than the group's 9M20 margin of 8.4% due to staff costs rising 71% to HUF10.1bn and opex rising by 151% to HUF4.2bn with a significant rise in M&A related costs. As a result, although 4iG has delivered 64% of our FY21 revenue estimate, the group has only achieved 40% of our FY21 EBITDA estimate ytd. On the face of it, this looks like a challenging target even for 4iG's seasonally strongest quarter. However, the results will be further boosted by the acquisition of Invitech and other deals closing in Q421.

**Exhibit 1: FY21e revenues on track**




Source: 4iG reports, Edison Investment Research

**Exhibit 2: FY21e EBITDA bridgeable**




Source: 4iG reports, Edison Investment Research

4iG did not disclose details of its forward contract pipeline with its results. However, management is confident that the company remains on track to become the leading Hungarian IT systems integrator (displacing T-Systems) by 2022, as well as having a significant presence in the Western Balkans.

# Partnership with Rheinmetall and HUF125bn placing

As part of its digitisation strategy and 'as a token of [its] special commitment to Hungary', Rheinmetall announced in November that it intended to take a 25.1% stake in 4iG, becoming its largest international strategic investor and accelerating its position as a leading security technology systems supplier in CEE.

From 4iG's perspective, Rheinmetall, a leading German defence group, has acquired a substantial minority stake in 4iG at HUF670 per share, validating 4iG's strategy and underpinning the group's valuation. The partnership also positions 4iG for future revenue opportunities, with 4iG operating as a strategic IT partner to Rheinmetall, using the relationship to identify and address new digital market opportunities.

Rheinmetall has agreed to purchase 24.9m 4iG shares off-market from KZF (an investment vehicle controlled by Gellért Jászai). Rheinmetall has also agreed to participate in a HUF125bn share placing, with iG COM (a separate investment vehicle controlled by Gellért Jászai) and a fund managed by Alpac Capital also participating alongside Rheinmetall. 4iG shares are to be issued at a price of HUF670, a 20% discount to 4iG's average closing price (HUF835) prior to the date of the vote on the enabling resolutions, and a discount of 18% to the current market price. Gellért Jászai (4iG's chairman and CEO) will retain a majority stake in 4iG.

The main steps of the transaction are as follows:

- iG COM will subscribe to HUF78bn of shares in 4iG, subject to a 12-month lock-up;
- 4iG will convene a general meeting to approve the new Articles of Association of 4iG and appoint a new member of the Supervisory Board nominated by Rheinmetall AG;
- assuming approval at the general meeting, Rheinmetall will purchase 24.9m 4iG shares from KZF, as well as subscribing to HUF33.65bn shares in 4iG. Both tranches of shares will be subject to a 24-month lock-up; and
- Alpac Capital will subscribe to HUF13.2bn of shares in 4iG.

Rheinmetall and 4iG have indicated that they will establish a separate joint venture to manage critical IT infrastructure and services in Hungary, owned 49% by 4iG and 51% by Rheinmetall. As well as their planned activities in critical infrastructure, 4iG and Rheinmetall see potential for cooperation in IT security, sensor technology, AI, robotics and satellite communications.

## M&A: Execution first, then the challenge of integration

As we have discussed in recent notes (Executing at pace on its five-year plan and M&A set to launch 4iG into orbit), 4iG has announced an ambitious M&A-led strategic agenda. As can be seen in Exhibit 3 below, Invitech was the first of these deals to complete in Q321, with Telenor Montenegro closing in December 2021 and DIGI Group in January 2022. This leaves 4iG with four further deals expected to complete in Q122 (Spacecom, ALBtelecom, One and Antenna Hungária – 4iG announced the termination of negotiations over the acquisition of a 70% stake in TeleGroup on 28 January 2022). Consideration multiples and contribution from these deals have yet to be disclosed, so our estimates remain unchanged until we are in a position to include these acquisitions (we last upgraded our estimates in June 2021).

That having been said, in the Q421 analyst presentation, management provided further detail on the acquisition terms for DIGI Group, confirming that the group was acquired for an enterprise value of €625m (c HUF630m), a transaction multiple of 11.6x FY20 EV/EBITDA and c 9x management's estimated run-rate FY22 EV/EBITDA (including synergies).

**Exhibit 3: Status of recently announced transactions**

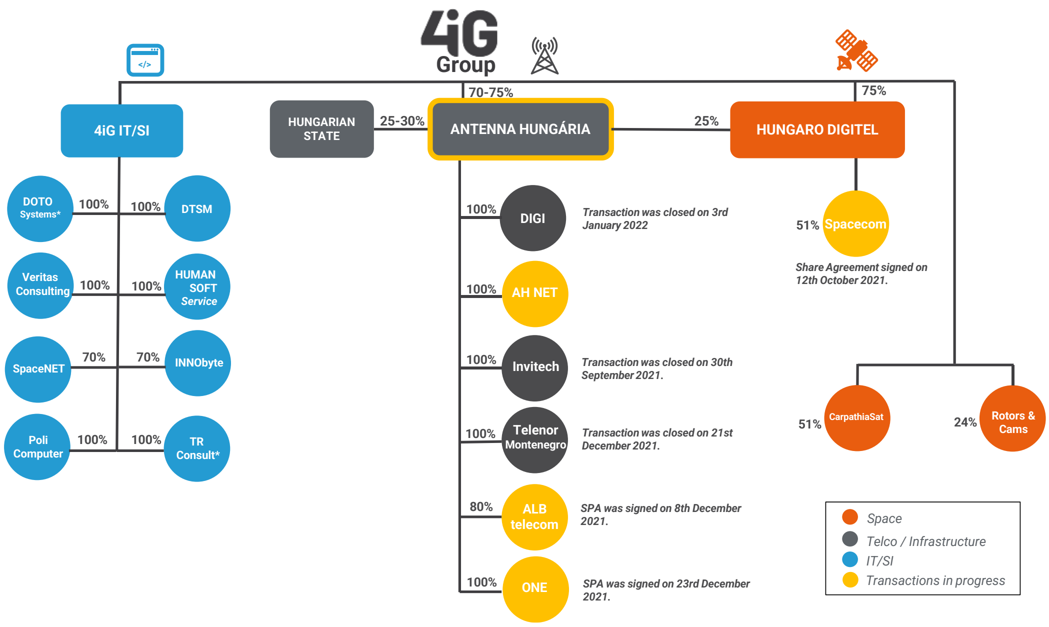
| # | TARGET COMPANIES | ACQUISITION STATUS | |
|---|---|---|---|
| 1 | invitech | • SPA was signed on 13th September 2021. ✓<br>• Transaction was closed on 30th September 2021. ✓ | Acquisitions |
| 2 | telenor Montenegro | • SPA was signed on 27th October 2021. ✓<br>• Transaction was closed on 21st December 2021. ✓ | Acquisitions |
| 3 | DIGI | • SPA was signed on 29th November 2021. ✓<br>• Transaction was closed on 3rd January 2022. ✓ | Acquisitions |
| 4 | SPACECOM MAKING SPACE FEEL CLOSER | • Due diligence completed. ✓<br>• Share Agreement was signed on 12th October 2021. ✓<br>• Closing is expected in February 2022. | Acquisitions |
| 5 | ALBtelecom | • Due diligence completed. ✓<br>• SPA was signed on 8th December 2021. ✓<br>• Closing is expected in February 2022. | Acquisitions |
| 6 | One | • Due diligence completed. ✓<br>• SPA was signed on 23rd December 2021. ✓<br>• Closing is expected in February 2022. | Acquisitions |
| 7 | antenna HUNGÁRIA | • Due diligence completed. ✓<br>• Term sheet was signed on 25th August 2021. ✓<br>• Contribution Agreement signing is expected in February 2022.<br>• Closing is expected in February 2022. | Capital Increase |

Source: 4iG. Note: Telenor Montenegro has subsequently closed in December 2021.

Management is aiming for 4iG to become the number one IT systems integrator in Hungary by the end of FY22 (displacing current market leader, T-Systems), and a significant regional player across

CEE and the Western Balkans. The announced acquisitions accelerate 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 and increasing 4iG's recurring revenue base.

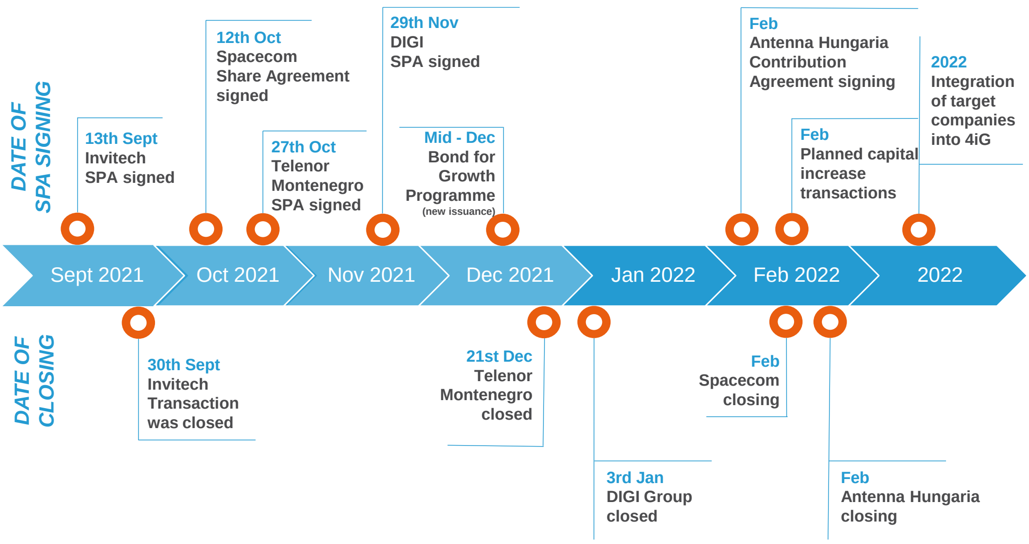
**Exhibit 4: 4iG pro forma group structure (including transactions pending)**




Source: 4iG

4iG's CarpathiaSat JV (August 2020) with its strategic partner, Antenna Hungária, laid the groundwork for 4iG's ambitions in space. 4iG's investment in Hungaro DigiTel (HDT) represented the next step in its strategic relationship with Antenna Hungária, 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. Its majority investment in Spacecom will take 4iG's exposure to space and satellite communications to another level, delivering revenue-generating operating satellites as well as a team with significant technical and launch experience. The acquisition of DIGI Group is expected to strengthen the group's position as a leading telecoms services provider, further moving the group's centre of gravity away from IT services and infrastructure, and diversifying its revenues away from Hungary.

**Exhibit 5: Strategic timeline H221–FY22**




Source: 4iG

On 8 December 2021, 4iG announced a further step in its expansion into the Western Balkans, by agreeing to acquire an 80.3% stake acquire in ALBtelecom, the Albanian national telecoms provider. ALBtelecom is the owner of the largest fibre network in Albania and the country's leading fixed line internet and TV operator, as well as an Albanian mobile operator with a significant owned network. The Albanian state will continue to hold a stake in ALBtelecom, through a 13.8% stake held by the Albanian Ministry of Finance and Economy and a 2.5% stake held by the Albanian Post.

Through the transaction, Çalik Holding, a large Turkish conglomerate, will also acquire a c 3.2% in 4iG. The transaction could open up further joint business opportunities for Çalik Holding and 4iG in the Balkans and Central Asia. The terms of the transaction were not disclosed, but the acquisition is expected to close in February 2022, subject to the approval of the Albanian authorities.

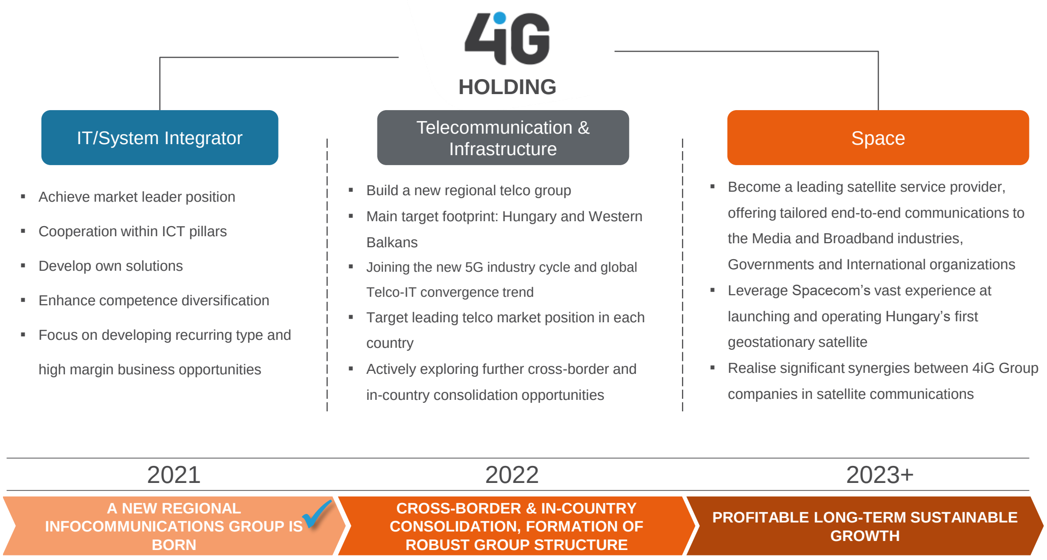
## M&A supports 4iG's strategic direction

Having consolidated the announced acquisitions, 4iG retains significant ambitions for its future growth and development.

These ambitions are set out in full in Exhibit 6 below, but the most important goals are:

- To become the leading IT services/systems integrator in Hungary by the end of 2022.
- To build a new regional telecoms group, leveraging 4iG's position in its domestic Hungarian market and expanding across the Western Balkans ahead of EU accession talks (these appear unlikely to be before 2026 at the earliest).
- Leveraging Spacecom's expertise to launch and operate Hungary's first geostationary satellite to become a leading satellite services provider, offering end-to-end communications for media, broadband and public sector clients.

**Exhibit 6: Strategic goals by division**




Source: 4iG

## Scope Ratings downgrades 4iG from BB- to B+

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 in March 2021. Subsequently, in June 2021, 4iG's BB- rating was placed under review for a developing outcome, pending completion of the Spacecom and DIGI Group transactions. In September 2021, 4iG's rating was changed again to BB- under review for a possible downgrade, reflecting heightened execution and integration risk given its large and numerous potential acquisitions.

In December 2021, Scope Ratings downgraded 4iG's issuer rating to B+/Stable from BB- under review for a possible downgrade. The downgrade reflects a weakened financial risk profile, and heightened execution and integration risk from large, mainly debt-funded acquisitions, which outweigh the positive impact on 4iG's business risk profile from the significant growth being pursued.

4iG's outlook is stable with assumptions underpinning the rating including:

- the successful placement of a HUF350bn bond in Q421 (HUF371bn achieved);
- a successful equity placing totalling more than HUF100bn in Q421–Q122 (outstanding);
- completion of the announced M&A strategy (ongoing); and
- Scope Ratings' adjusted debt[1]/EBITDA below 5x in the medium term (TBC).

## Over-subscribed 10-year bond issue

In December 2021, 4iG completed a HUF371bn senior unsecured bond issue (exceeding the HUF350bn targeted) under the Hungarian National Bank's Bond Funding for Growth Scheme, the largest such bond ever issued under the programme. The bond was raised through two auctions, both offering a 6% coupon and 10-year tenor, with 10% annual amortisation from 2026 and a 50% bullet at maturity in 2031 (Exhibit 7). The first tranche of HUF291bn offered a 5.8% yield to maturity, with the second tranche of HUF82bn offering a 6.2% yield to maturity. The proceeds will be used for acquisitions as well as to refinance the existing HUF100bn Magyar Fejlesztési Bank (MFB) bond.

**Exhibit 7: New bond structure under the Bond Funding for Growth programme**

| ISSUER | 4iG PLC. |
|---|---|
| Security | Senior Unsecured |
| Maturity / repayment | 10 years<br>Year 5-9: 10%<br>Year 10: 50% |
| Amount | HUF 350bn |
| Currency | HUF |
| Use of Proceeds | Financing new acquisitions |

Source: 4iG

Total 2021 pro forma revenue of the enlarged group is expected to reach around HUF380bn and pro forma EBITDA should exceed HUF100bn, which is far above 4iG's 2020 revenue of HUF57bn and EBITDA of HUF5bn. In terms of industries, telecom services, including satellite communications, are expected to account for a dominant share of total revenue and EBITDA. The remainder is mainly IT, IT infrastructure and media/event services.

[1] Scope Ratings adjusted debt excludes cash and cash equivalents.

## Revision to our estimates pending

Our estimates were last upgraded in June 2021 and do not currently take account of the significant M&A completed in H221 and expected to complete in Q122. Until the announced deals close and we have better clarity on the terms and impact of the outstanding acquisitions and their funding, we are not in a position to revise our estimates.

However, following a detailed credit review of the acquisitions and their funding, Scope Ratings noted the following expectations in its credit rating downgrade announced on 2 December 2021:

- FY21 pro forma revenue for the enlarged group to reach c HUF380bn, with pro forma EBITDA in excess of HUF100bn.
- Estimated FY21 pro forma group EBITDA margin of 25–30%.
- FY21 pro forma group recurring revenues are expected to exceed 60%, compared to below 20% for 4iG in FY20.
- In terms of divisional mix, telecoms services, including satellite communications, are expected to account for a dominant share of total revenue and EBITDA, with a minority of revenues deriving from IT services and IT infrastructure services.
- The group is expected to benefit from a broader geographical footprint, with FY21 pro forma group revenues derived from Hungary expected to decline to around 75–80% of overall revenues, from more than 95% in FY20. International revenues will be derived from the Western Balkans, with other regions (mainly CEE, the Middle East and sub-Saharan Africa) acquired via 4iG's investment in Spacecom.

Scope Ratings also commented on 4iG's 'very weak position in the Hungarian mobile market', as well as strong competition in the enlarged group's main markets, including IT services and satellite communications.

**Exhibit 8: Financial summary**

| 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 | 97.3 | 102.4 |
| EPS - basic normalised (HUF) | | 31.54 | 37.17 | 55.45 | 61.97 |
| EPS - diluted normalised (HUF) | | 30.77 | 36.09 | 54.74 | 61.21 |
| EPS - basic reported (HUF) | | 30.82 | 37.68 | 59.73 | 66.05 |
| Dividend (HUF) | | 22.00 | 22.49 | 36.47 | 40.00 |
| 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 | 70,236 |
| 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 | 26,588 |
| 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 | 29,464 |
| Minority interests | | 64 | (376) | (414) | (462) |
| Shareholders' equity | | 5,556 | 7,303 | 17,967 | 29,002 |
| **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) | (3,764) |
| Other | | 36 | (323) | 0 | 0 |
| Net Cash Flow | | 5,626 | (878) | (8,413) | 2,346 |
| 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 | 3,327 |

Source: 4iG accounts, Edison Investment Research

## General disclaimer and copyright



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## New Zealand



## United Kingdom



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