

Magyar Telekom Nyrt

Hungary, Telecommunications Services



Key metrics

Scope credit ratios	2021	2022	Scope estimates	
			2023E	2024E
Scope-adjusted EBITDA/interest cover	12.3x	12.6x	10.3x	11.0x
Scope-adjusted debt/EBITDA	2.0x	1.9x	1.5x	1.3x
Scope-adjusted funds from operations/debt	44%	45%	54%	65%
Scope-adjusted free operating cash flow/debt	12%	0%	16%	22%

Rating rationale

The Positive Outlook reflects Magyar Telekom's improving profitability, benefitting from its introduction of inflation-based fee adjustments in early 2023 and from the recently announced memorandum of understanding with the Hungarian government on network roll-outs associated with the removal of sector-specific taxes in 2024 and 2025.

The business risk profile (BBB+) benefits mainly from the low cyclicality of the telecoms industry and the company's leading position in Hungary's mobile and broadband markets, which strongly supports its competitive position. Magyar Telekom's domestic market shares in several segments outperform those of most telecoms operators in Europe. The company's share of the mobile market increased in 2022, while its broadband market share continues to increase gradually. The purchases by Hungarian IT-telecoms group 4iG of broadband provider DIGI and Vodafone Hungary have not had a material effect on Magyar Telekom's competitive position. Similarly, the probable purchase of Hungarian mobile operator Yettel by e& (Etisalat) is not expected to change the Hungarian market. The group also benefits from a strong position in North Macedonia, though this provides only limited diversification, accounting for just 12% of its revenues. The company's profitability is stable, with a 29.7% EBITDA margin after leases in 2022. This is somewhat below that of main European peers, partly due to the telecoms and utility taxes in Hungary. In Q2 2023, the company's introduction of inflation-based fee adjustments in its general terms and conditions led to its EBITDA margin after leases improving to 33.5%.

Magyar Telekom's financial risk profile (A-) is underpinned by the expectation that Scope-adjusted debt/EBITDA ratio will improve after peaking at around 2x after the group acquired spectrum in 2020 (5G) and 2021 (2G and 4G renewal). Scope-adjusted debt/EBITDA was stable at 1.9x at end-December 2022 and should decline through 2023 towards 1.5x as profitability improves. Once the recently announced agreement with the Hungarian government on telecommunication tax (which have changed repeatedly over the last years) is implemented, leverage should lower further. The company issued its first senior unsecured bond (HUF 70bn) in 2020 as part of the Hungarian central bank's bond programme, which represented 15% of Scope-adjusted debt at end-2022. The group also benefits from good debt protection, with EBITDA/interest cover of more than 10x, even after the spectrum acquisitions of 2021. The company's policy is for shareholder returns (dividends and share buybacks) to run at 60%-80% of adjusted net profit. Magyar Telekom's liquidity is adequate, helped by its 64% ownership by Deutsche Telekom AG

Magyar Telekom's integration within the Deutsche Telekom group (cash pooling, financing) is such that, while Deutsche Telekom is more indebted, we deem it a remote risk that the parent company's activities would adversely affect Magyar Telekom's ability to meet its own contractual financial debt obligations as a going concern on time and in full.

Ratings & Outlook

Issuer	BBB+/Positive
Senior unsecured debt	BBB+

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Related Methodology

[Corporate Rating Methodology; July 2022](#)

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Outlook and rating-change drivers

The Positive Outlook on Magyar Telekom's rating reflects its moderate capital expenditure and the stable competition in Hungary incorporated in our base case as well as improving credit metrics with Scope-adjusted debt/EBITDA declining towards 1.5x.

An upgrade may be warranted if profitability improved significantly, helped by the lowered telecoms taxes, leading to better credit metrics, particularly a Scope-adjusted debt/EBITDA sustained well below 1.5x. This might nevertheless be constrained by the current lower sovereign rating of Hungary of BBB/Stable.

Outlook revision to stable may be taken if Scope-adjusted debt/EBITDA fails to go below 1.5x, with lower than expected profitability, or more generous shareholder returns. Further negative action may be taken if competition in Hungary increased notably, leading to declining credit metrics, with Scope-adjusted debt/EBITDA reaching significantly above 2.5x. However, such a negative rating action is a remote possibility in the short to medium term.

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
27 Sep 2022	Affirmation	BBB+/Stable
22 Oct 2021	Affirmation	BBB+/Stable
28 Oct 2020	New	BBB+/Stable



Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
<ul style="list-style-type: none">• Strong leader in Hungarian mobile with 45% market share• Leader in Hungarian broadband with 40% market share• History of good credit metrics• Market leader in North Macedonia with a mobile market share of 50%• Large, diversified customer base	<ul style="list-style-type: none">• Dependence on one single market (Hungary)• Profitability somewhat lower than European peer levels partly due to sector-specific taxes
Positive rating-change drivers	Negative rating-change drivers
<ul style="list-style-type: none">• Lower leverage, with Scope-adjusted debt/EBITDA maintained well below 1.5x	<ul style="list-style-type: none">• Increased leverage, with Scope-adjusted debt/EBITDA sustained above 2.5x

Corporate profile

Magyar Telekom is Hungary's largest incumbent telecommunications operator, with consolidated revenues of HUF 746bn (EUR 1.91bn) in 2022. It leads the market with 6.1m customers in mobile, 1.3m in fixed voice and 1.5m in broadband. It was created in 1989 as a separate division from Hungary's post office and was commonly known as Matav, a shorter version of its former name, Magyar Tavkozlesi RT. It was privatised in 1993 through a partial sale to a consortium that included Deutsche Telekom, which now has the controlling stake with 64%. Its only significant foreign subsidiary is Macedonian Telekom, the incumbent operator in North Macedonia.








Financial overview

				Scope estimates		
Scope credit ratios	2020	2021	2022	2023E	2024E	2025E
Scope-adjusted EBITDA/interest cover	11.5x	12.3x	12.6x	10.3x	11.0x	13.7x
Scope-adjusted debt/EBITDA	2.0x	2.0x	1.9x	1.5x	1.3x	0.9x
Scope-adjusted funds from operations/debt	43%	44%	45%	54%	65%	90%
Scope-adjusted free operating cash flow/debt	3%	12%	0%	16%	22%	37%
Scope-adjusted EBITDA in HUF m						
EBITDA	225,882	240,771	247,946	292,200	329,500	381,000
Operating lease payments	0	0	0	0	0	0
Other items	0	0	0	0	0	0
Scope-adjusted EBITDA	225,882	240,771	247,946	292,200	329,500	381,000
Funds from operations in HUF m						
Scope-adjusted EBITDA	225,882	240,771	247,946	292,200	329,500	381,000
less: (net) cash interest paid	-19,630	-19,604	-19,730	-28,500	-29,900	-27,800
less: cash tax paid per cash flow statement	-12,700	-14,471	-18,615	-22,000	-27,000	-33,000
add: dividends from associates	52	57	76	50	50	50
Change in provisions	0	0	0	0	0	0
Funds from operations	193,604	206,753	209,677	241,750	272,650	320,250
Free operating cash flow in HUF m						
Funds from operations	193,604	206,753	209,677	241,750	272,650	320,250
Change in working capital	-3,092	-12,599	-7,372	-5,000	-3,000	-2,000
Non-operating cash flow	-4,557	616	-6,542	-3,500	-4,500	0
less: capital expenditure (net)	-145,270	-108,953	-164,376	-130,000	-138,000	-146,000
less: lease amortisation	-25,114	-28,972	-33,328	-33,328	-33,328	-33,328
Free operating cash flow	15,571	56,845	-1,941	69,922	93,822	-138,922
Net cash interest paid in HUF m						
Net cash interest per cash flow statement	19,630	19,604	19,730	28,500	29,900	27,800
add: interest component, operating leases	0	0	0	0	0	0
Change in other items	0	0	0	0	0	0
Net cash interest paid	19,630	19,604	19,730	28,500	29,900	27,800
Scope-adjusted debt in HUF m						
Reported gross financial debt	388,242	331,111	373,895	357,573	333,751	278,529
less: subordinated (hybrid) debt	0	0	0	0	0	0
less: cash and cash equivalents	-14,689	-13,463	-12,861	-12,861	-12,861	-12,861
add: non-accessible cash	0	0	0	0	0	0
add: pension adjustment	0	0	0	0	0	0
add: operating lease obligations	0	0	0	0	0	0
Other items (spectrum)	76,084	156,662	106,662	101,662	96,662	91,662
Scope-adjusted debt	449,637	473,730	467,696	446,374	417,552	357,350

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Environmental, social and governance (ESG) profile¹

Environment	Social	Governance
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)	Labour management 	Management and supervision (supervisory boards and key person risk) 
Efficiencies (e.g. in production)	Health and safety (e.g. staff and customers)	Clarity and transparency (clarity, quality and timeliness of financial disclosures, ability to communicate) 
Product innovation (e.g. transition costs, substitution of products and services, green buildings, clean technology, renewables)	Clients and supply chain (geographical/product diversification)	Corporate structure (complexity) 
Physical risks (e.g. business/asset vulnerability, diversification)	Regulatory and reputational risks	Stakeholder management (shareholder payouts and respect for creditor interests) 

Legend

Green leaf (ESG factor: credit positive)

Red leaf (ESG factor: credit negative)

Grey leaf (ESG factor: credit neutral)

Past corruption case (settled)

In 2011, Magyar Telekom settled (for USD 95m) with US authorities its case of corruption related to blocking a third mobile operator from entering Macedonia in 2005. The company has taken remedial measures (including enhanced compliance programmes).

No significant ESG factor

Environmental, social and governance (ESG) considerations have no effect on the credit.

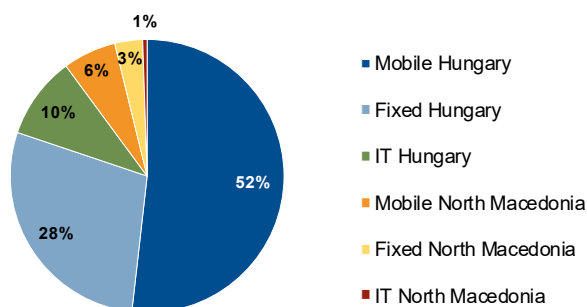
¹ These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Business risk profile: BBB+

Industry risk profile: A

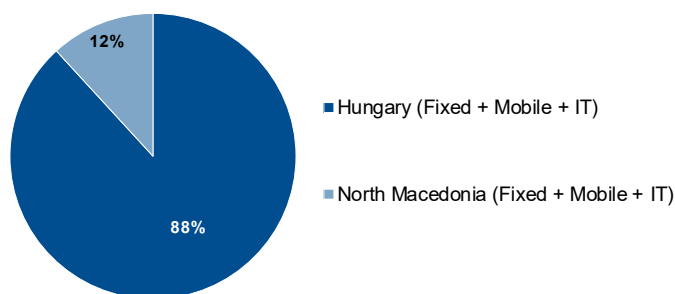
The industry risk profile for telecommunication services stands at A, based on low cyclicality (subscriptions for what is now considered a basic service), medium entry barriers (licences, network roll-out), and medium to low substitution risk (over-the-top services).

Figure 1: Magyar Telekom, revenues in 2022 (HUF 746bn)



Source: Magyar Telekom

Figure 2: Magyar Telekom, EBITDA after leases in 2022 (HUF 248bn)



Source: Magyar Telekom

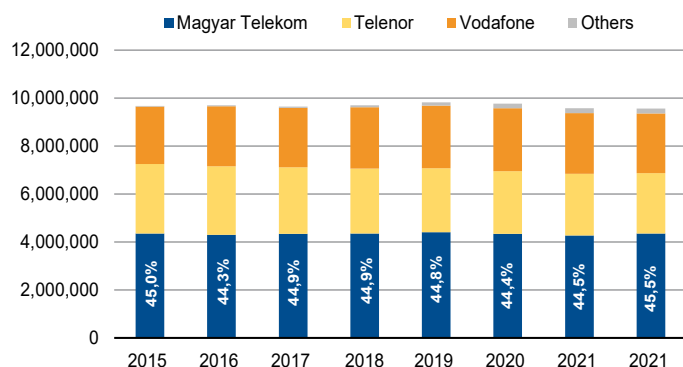
The group's home market of Hungary (9.7m inhabitants) represents 90% of its revenue. Magyar Telekom as the incumbent operator is market leader. Its telecoms revenues continued to grow during the Covid-19 pandemic, by around 2% in 2020, followed by 5% in 2021 and 8% in 2022, driven by mobile revenues and equipment sales, a situation not common in Europe.

Hungarian market growing

Strong market leader in mobile

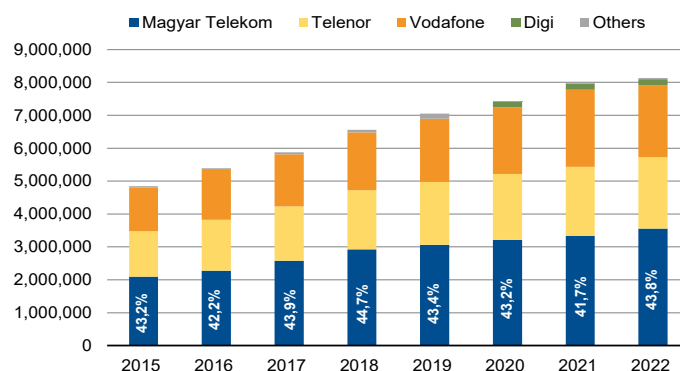
In Hungary, where mobile penetration is somewhat lower than in most European countries, the group is the clear leader with a market share of around 44% (by subscribers). This level has remained remarkably stable over the last years (but increased slightly in 2022 to almost 45%), far above those of the two main competitors, Vodafone and Telenor-PPF (now renamed Yettel). The group's market share in terms of revenue is around 46%, which is above that of most market leaders in Europe.

Figure 3: Magyar Telekom market share in Hungary, 2015-2022 (% of active SIM cards with voice traffic)



Source: NMHH

Figure 4: Magyar Telekom market share in Hungary, 2015-2022 (% of active SIM cards with internet traffic)

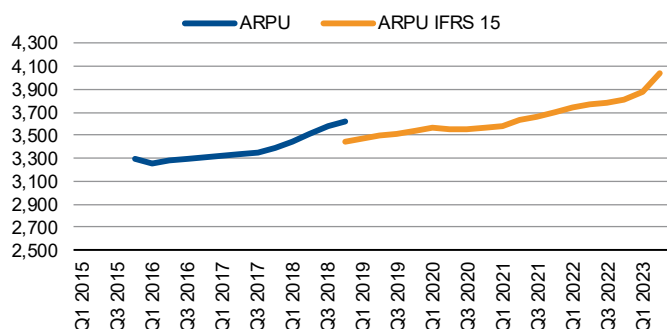


Source: NMHH

The purchase of Vodafone Hungary in January 2023 by 4iG, which previously acquired Hungarian broadband provider Digi with its marginal mobile activity, has not changed materially the competitive position of Magyar Telekom in its domestic mobile market. We also expect a minimal impact from the planned acquisition by Middle-East operator E& (Etisalat) of Hungarian mobile-only Yettel, announced two months ago.

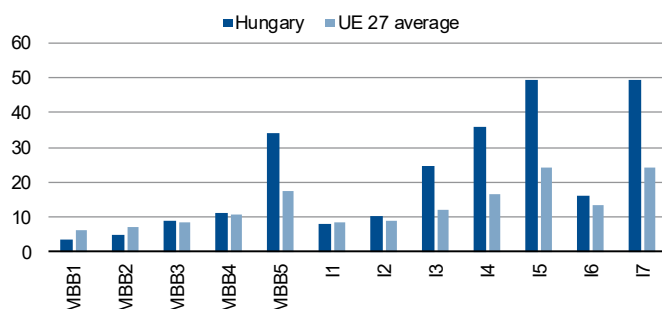
In September 2022, the company added in its general terms and conditions a fee adjustment clause based on inflation, effective from March 2023, to manage the inflation in energy, personnel and other costs. Magyar Telekom's average revenue per user (ARPU) for mobile has been increasing by about 3% over the last few years, a rare feature in Europe. But in Q2 2023, the first quarter with the effect of the price indexation, mobile ARPU was up 16.2%. According to the latest European Commission benchmark, Hungary is among the most expensive markets for mobile services.

Figure 5: Magyar Telekom mobile ARPU (HUF), 12-month rolling average, 2015-2023



Sources: Magyar Telekom, Scope.

Figure 6: Mobile prices in Hungary vs EU average (EUR PPP) for 12 mobile baskets (2021)

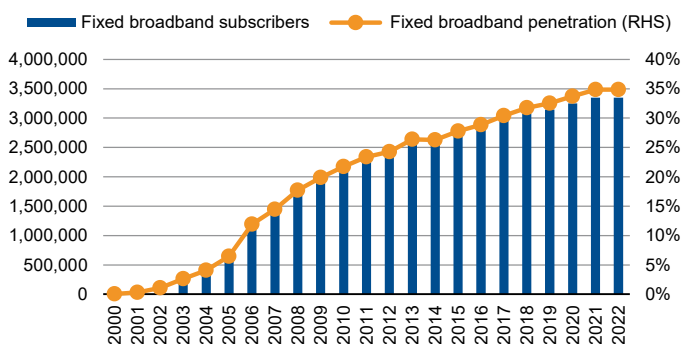


Sources: EU Commission

Hungary: strong position for cable

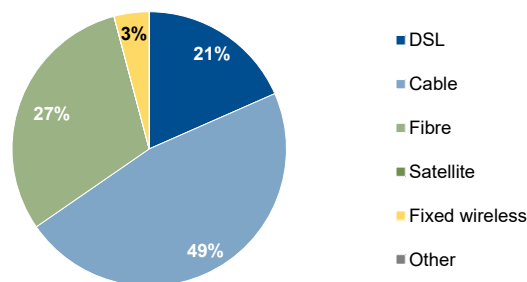
Magyar Telekom is also Hungary's leader in the growing market of fixed broadband, where subscriber numbers are increasing annually by around 3% over the last years. Cable operators own much of Hungary's fixed-broadband market, which is not common in Europe. Even more unusual is that Magyar Telekom owns (and sometimes rents) a significant number of broadband access points through cable technology.

Figure 7: Fixed broadband subscribers and penetration in Hungary, 2000-2022



Sources: ITU, NMHH, Scope estimates

Figure 8: Fixed broadband market by technology in Hungary (end-2020)²



Source: OECD (detail no longer published since 2021)

40% market share in broadband through DSL, fibre and cable

Magyar Telekom holds above 40% of Hungary's fixed-broadband market, a level slightly above the average for European incumbents (38%). In 2018, Vodafone became a key player in Hungarian fixed broadband after it acquired cable operator UPC. Around the same time, Digi, a large player in the broadband market bought the smaller fixed-service operator Invitel and became the second largest player in Hungary. 4IG's purchase of Digi and more recently of Vodafone Hungary expanded its market share to about 42%. These acquisitions did not change Magyar Telekom's competitive position substantially, however, due to the unusual market dynamics, with Magyar Telekom steadily gaining

² According to OECD, fibre percentage as of December 2022 was 37%.

market share, as illustrated in Figure 9. Magyar Telekom's share of the broadband market has slowly but continually increased in recent years, mostly through the roll-out of fibre (now representing 46% of customers against 6% seven years ago) and supported by the acquisition of smaller cable operators. Pricing for these services in Hungary are generally lower than the EU average: of the latest 12 European Commission broadband baskets, the average price is 29% below the EU-27 average.

Figure 9: Fixed broadband market share in Hungary, 2018-2022

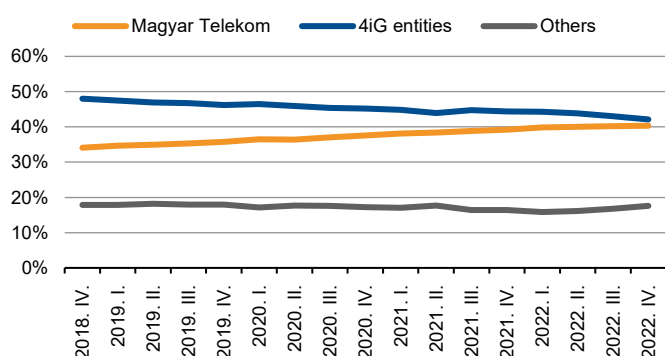
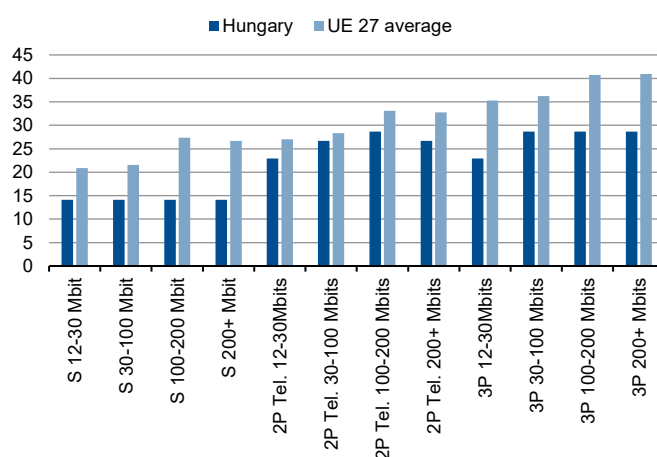


Figure 10: Broadband prices in Hungary vs EU average (EUR PPP) for 12 broadband baskets (2021)



Sources: NMHH, Scope, Invitel, Invitech, Digi and Vodafone aggregated as 4iG.

Source: European Commission

In North Macedonia (2.1m inhabitants), Magyar Telekom's 51% subsidiary is the incumbent operator (still 35% owned by the government), with almost 50% of the mobile market and about 40% of fixed-broadband subscribers.

Magyar Telekom is also the leading IT provider in Hungary's very fragmented market (through the T-Systems and T-Business brands), with a market share estimated at about 12%.

In terms of diversification, the group is mostly focused on telecommunications services in Hungary and, to much lower extent, in North Macedonia. The weight of IT services in group EBITDA is also rather limited.

In terms of profitability, Magyar Telekom's EBITDA after leases margin, at 29.7% in 2022, is lower than that of most European incumbents focused domestically, typically at around 40%. This is partly due to the significant telecoms and utility taxes in Hungary.

Financial risk profile: A-

Magyar Telekom's financial risk profile is mainly sustained by the group strong leverage and good cash flow cover.

The main driver of the issuer's debt in the last years was investment in spectrum, with auctions in 2020 and 2021 and some payments in early 2022. Additionally, in the first half of 2022, the Hungarian government announced a temporary supplementary telecoms tax for 2022 and 2023 of about HUF 25bn, which will put pressure on group margins (about 3pp). In May 2023, the government announced that this tax will remain for 2024. On 15 September 2023, Magyar Telekom signed a memorandum of understanding with the government on network roll-outs, with the removal of a utility telecoms tax in 2024 and the cancellation of the temporary supplementary telecoms tax from 2025.

Finally, in September 2022, the group included clauses in its general terms and conditions that allow price changes based on the consumer price index from March 2023.

All fixed fees for all customers were increased at this date by 14.5%. Q2 2023 was the first period with the full effect of the price change, leading to a higher EBITDA margin after leases of 33.0% from 28.2% in Q2 2022 and 32.3% in Q2 2021.

Leverage expected to remain below 2.0x

Leverage stood at 1.9x at YE 2022 after declining in recent years but picked up following the spectrum investments. We expect leverage to decrease to around 1.5x in 2023. This will be due to higher profitability thanks to the subscription fee increases, the completion of spectrum investment and the policy to pay out 60%-80% of net adjusted profits as dividends and share buy-backs. The ratio will improve further, once the telecoms taxes are removed in 2024 and 2025.

Figure 11: Scope-adjusted debt/EBITDA, 2014-2025E

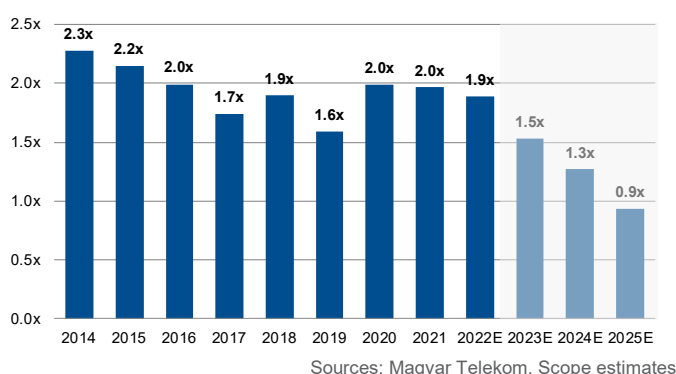
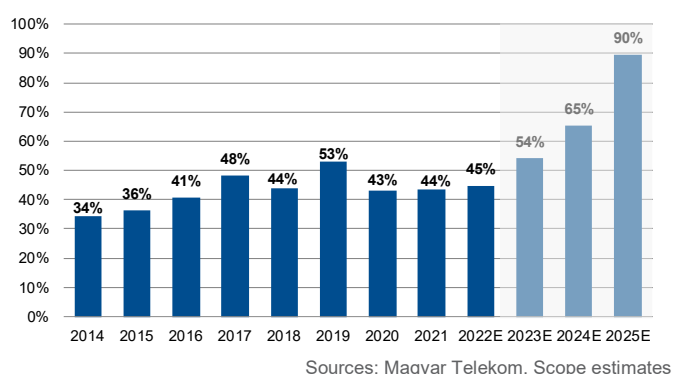


Figure 12: Scope-adjusted funds from operation/debt, 2014-2025E



Very strong debt protection

We expect debt protection to remain very strong at above 10x, even with increased interest costs.

Good cash flow cover

Over the last eight years, the Scope-adjusted free operating cash flow/debt ratio has averaged 11.5%, with a peak of 20% in 2017-2018. Excluding exceptional figures in 2014, 2020 and 2022, when Magyar Telekom made spectrum payments, the average would be just below 17%. We expect the ratio to normalise in 2023 as no spectrum payments are expected, before increasing significantly 2024 and 2025 as profitability improves (fee increases and tax removal).

Figure 13: EBITDA/interest cover, 2014-2025E

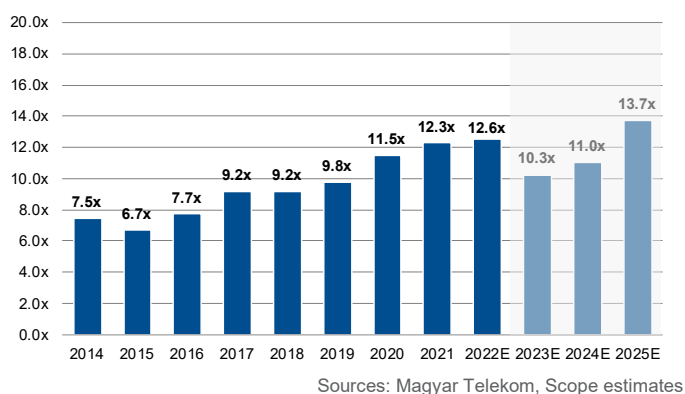
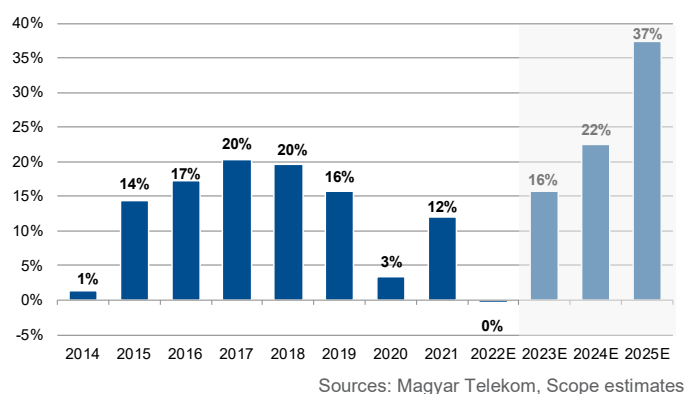


Figure 14: Scope-adjusted free operating cash flow/debt, 2014-2024E



Adequate liquidity

Over the last nine years, the combination of cash, free operating cash flow and undrawn committed lines has averaged 1.4x of short-term debt, reaching 2.0x at end-2022. The issuer's parent company, Deutsche Telekom, which has been providing most current and non-current financial liabilities at Magyar Telekom for many years, is also ensuring adequate liquidity for its subsidiary.



Balance in HUF m	2023E	2024E	2025E
Unrestricted cash (t-1)	12,861	12,861	12,861
Open committed credit lines (t-1)	45,500	45,500	45,500
Free operating cash flow	69,922	93,822	133,922
Short-term debt (t-1)	65,700	65,700	65,700
Coverage	195%	>200%	>200%

Supplementary rating drivers: +/- 0 notches

Although Magyar Telekom is strongly financially integrated into the Deutsche Telekom group (which owns 64% of the issuer) in terms of cash pooling and financing, we deem it a remote risk that the parent company's behaviour would adversely affect Magyar Telekom's credit quality in the foreseeable future. Deutsche Telekom's creditworthiness is driven by its strong position in mobile and broadband in Germany, its growing share of the US mobile market, and the increased leverage and execution risks accompanying its merger with Sprint, after which Deutsche Telekom's leverage has stayed above 3.0x. However, the parent's credit risk profile does not constrain Magyar Telekom's creditworthiness.

Long-term debt rating

Reflecting our view of Magyar Telekom's ability to meet contractual and financial debt obligations as a going concern, on time and in full out of its operating business, we rate senior unsecured debt issued by the company at BBB+, the same level as the issuer rating.

Senior unsecured debt rating:
BBB+



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