

Magyar Telekom Nyrt

Hungary, Telecommunications Services



Key metrics

Scope credit ratios	2020	2021	Scope estimates	
			2022E	2023E
Scope-adjusted EBITDA/interest cover	11.5x	12.3x	11.8x	12.5x
Scope-adjusted debt/EBITDA	2.0x	2.1	1.9x	1.7x
Scope-adjusted funds from operations/debt	43%	44%	45%	50%
Scope-adjusted free operating cash flow/debt	3%	12%	3%	13%

Rating rationale

The business risk profile (BBB+) benefits mainly from the low cyclical nature in the telecom industry and the company's leading position in mobile and broadband markets in Hungary, which strongly supports its competitive position. Magyar Telekom has a share of different segments of its domestic market that are above those of most other European telecoms operators. The company's share of the mobile market shrank marginally in 2021, while the company increased slightly again its share of the broadband market. As the Hungarian telecommunications market is mature, Scope does not expect a significant change in market share. The purchase by Hungarian IT-telecommunication group 4iG of broadband provider DIGI, followed by recently announced project of the acquisition of Vodafone Hungary, is unlikely to materially affect Magyar Telekom's competitive positioning in the short to medium term. The group also benefits from a strong position in North Macedonia, though that provides only limited diversification for the group as it represents just 11% of the group's revenues. The company's profitability is stable, recording a 30.9% EBITDA margin after leases in 2021, somewhat below that of main European peers, partly due to telecom and utility taxes in Hungary. Nevertheless, the group faces narrower profit margins in 2022 and 2023, to contract by about 3pp, after the Hungarian government introduced a temporary supplementary telecommunications tax (equivalent to an extra cost of about HUF 25bn a year). Profitability should recover to previous levels as long as the tax does not become permanent. The company has also recently introduced clauses in its General Terms and Conditions allowing inflation adjusted price changes based on the official consumer price index, thereby offering some protection against potential inflation effects.

Magyar Telekom's financial risk profile (A-) is underpinned by the Scope-adjusted debt (SaD)/EBITDA ratio having peaked at around 2x when the group acquired spectrum in 2020 (5G) and 2021 (2G and 4G renewal). SaD/EBITDA stood at 2.0x end-December 2021, a stable level, and should decline progressively through this year, albeit slowed by the imposition of the new tax. 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 SaD at the end of 2021. The group also benefits from good debt protection, with EBITDA/interest cover of more than 10x, even after the spectrum acquisitions of 2021. SaD/EBITDA will return to below 2.0x in the coming three years. The company's policy is for shareholder returns (dividends and share buybacks) to run at between 60% to 80% of adjusted net profit. Magyar Telekom's liquidity is adequate, not least as it is 61%-owned by Deutsche Telekom AG.

Ratings & Outlook

Issuer	BBB+/Stable
Senior unsecured debt	BBB+

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Related Methodology and Related Research

[Corporate Rating Methodology](#)
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Bloomberg: RESP SCOP



Magyar Telekom's integration within the Deutsche Telekom group (cash pooling, financing) is such that, while Deutsche Telekom is more indebted, Scope deems 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.

Outlook and rating-change drivers

The Stable Outlook incorporates assumptions of leverage with SaD/EBITDA of below 2.0x, following spectrum auctions in Hungary in 2020 and 2021, and temporary telecommunication tax in 2022 and 2023.

A positive rating action is possible if deleveraging happened faster than expected, with SaD/EBITDA falling below 1.5x on a sustained basis.

A negative rating action is possible in case of significant change in competitive positioning following the acquisition of Vodafone Hungary by 4iG, or in case of the payment of higher shareholder returns and higher capex that lead to a significant increase in leverage towards 3.0x on a sustained basis

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
27/09/2022	Affirmation	BBB+/Stable
22/10/2021	Affirmation	BBB+/Stable
28/10/2020	New	BBB+/Stable



Positive rating drivers

- Strong leader in Hungarian mobile market with 45% share
- Market leader in broadband in Hungary with market share of 40%
- Average historical Scope-adjusted debt/EBITDA at 1.9x
- Market leader in North Macedonia with a market share in mobile of 50%
- Large, diversified customer base

Negative rating drivers

- Dependence on one single market (Hungary)
- Temporary increase in leverage with spectrum auctions
- Profitability somewhat lower than European peers

Positive rating-change drivers

- Scope-adjusted debt/EBITDA decreasing to a sustained level of below 1.5x

Negative rating-change drivers

- Scope-adjusted debt/EBITDA moving toward 3.0x on sustained basis

Corporate profile

Magyar Telekom remains Hungary's largest incumbent telecommunications operator, with consolidated revenues of HUF 700bn (EUR 1.95bn) in 2021. It leads the market with 5.6m customers in mobile, 1.3m in fixed voice and 1.4m 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 61%. Its only significant foreign subsidiary is Macedonian Telekom, the incumbent operator in North Macedonia.








Financial overview

			Scope estimates		
Scope credit ratios	2020	2021	2022 E	2023 E	2024 E
Scope-adjusted EBITDA/interest cover	11.5x	12.3x	11.8x	12.5x	15.2x
Scope-adjusted debt/EBITDA	2.0x	2.0x	1.9x	1.7x	1.4x
Scope-adjusted funds from operations/debt	43%	44%	45%	50%	64%
Scope-adjusted free operating cash flow/debt	3%	12%	3%	13%	22%
Scope-adjusted EBITDA in HUF m					
EBITDA	225,882	240,771	235,700	244,700	276,450
Operating lease payments	0	0	0	0	0
Other items	0	0	0	0	0
Scope-adjusted EBITDA	225,882	240,771	235,700	244,700	276,450
Funds from operations in HUF m					
Scope-adjusted EBITDA	225,882	240,771	235,700	244,700	276,450
less: (net) cash interest paid	-19,630	-19,604	-20,000	-19,500	-18,200
less: cash tax paid per cash flow statement	-12,700	-14,471	-14,000	-13,150	-15,650
add: dividends from associates	52	57	50	50	50
Change in provisions	0	0	0	0	0
Funds from operations	193,604	206,753	201,750	212,100	242,650
Free operating cash flow in HUF m					
Funds from operations	193,604	206,753	201,750	212,100	242,650
Change in working capital	-3,092	-12,599	-3,000	-2,000	-2,000
Non-operating cash flow	-4,557	616	-3,500	-3,500	-3,500
less: capital expenditure (net)	-145,270	-108,953	-151,800	-121,000	-126,000
less: operating lease payments	-25,114	-28,972	-28,972	-28,972	-28,972
Free operating cash flow	15,571	56,845	14,478	56,628	82,178
Net cash interest paid in HUF m					
Net cash interest per cash flow statement	19,630	19,604	20,000	19,500	18,200
add: interest component, operating leases	0	0	0	0	0
Change in other items	0	0	0	0	0
Net cash interest paid	19,630	19,604	20,000	19,500	18,200
Scope-adjusted debt in HUF m					
Reported gross financial debt	388,242	331,111	354,933	331,805	289,927
less: subordinated (hybrid) debt	0	0	0	0	0
less: cash and cash equivalents	-14,689	-13,463	-13,463	-13,463	-13,463
add: non-accessible cash	0	0	0	0	0
add: pension adjustment	0	0	0	0	0
add: operating lease obligations	0	0	0	0	0
Spectrum liabilities	76,084	-156,082	-111,082	-106,082	-101,082
Scope-adjusted debt	449,637	473,730	452,552	424,424	377,546

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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 manement 	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 case of corruption (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.

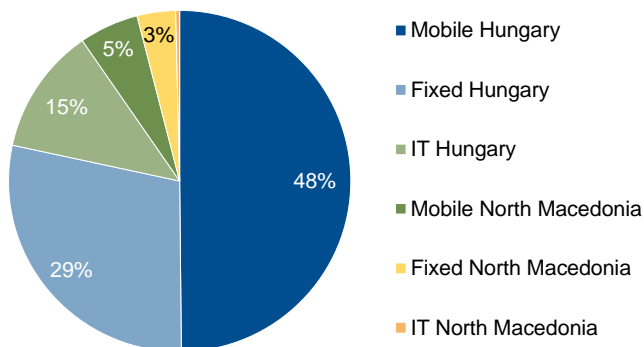
¹ These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Business risk profile: BBB+

Industry risk profile: A

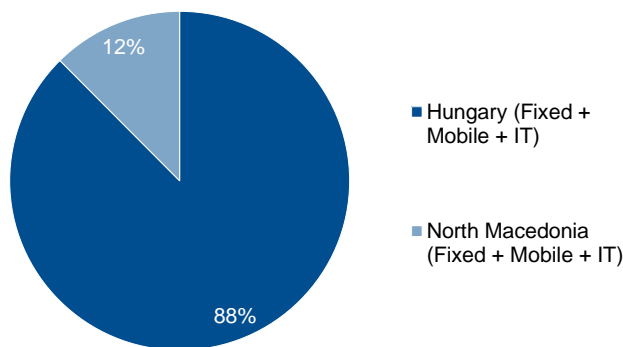
The industry risk profile for telecommunication services stands at A, based on low cyclicity (subscriptions for what is now considered a basic service), medium entry barriers (licences, network roll-out), and medium to low substitution risk (over-the-top services).

Figure 1: Magyar Telekom, revenues in 2021 (HUF 700bn)



Source: Magyar Telekom

Figure 2: Magyar Telekom, EBITDA after leases in 2021 (HUF 216bn)



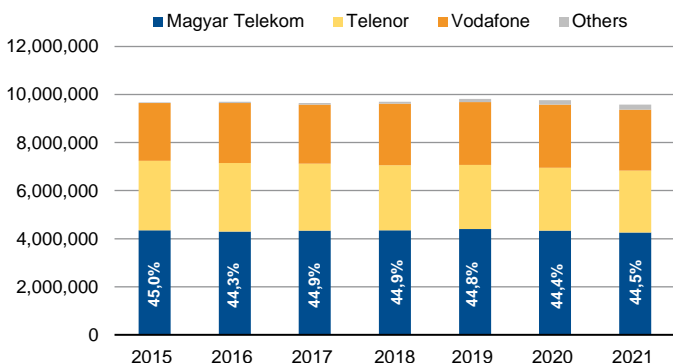
Source: Magyar Telekom

Market leader in Hungary

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 pandemic, by around 2% in 2020 and 5% in 2021, driven by mobile revenues and equipment sales, a situation not common in Europe.

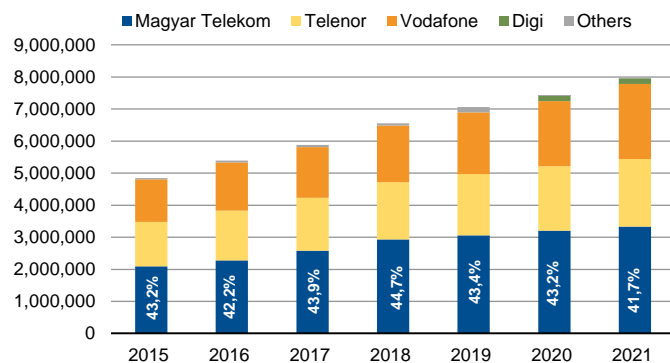
In Hungary, where mobile penetration is somewhat lower than in most European countries, the group is the clear leader with a market share of around 44% (by subscribers). This level has remained remarkably stable (marginal erosion in 2021) and far above those of the two main competitors, Vodafone and Telenor-PPF (now renamed Yettel). The group's market share in terms of revenue is around 48%, which is above that of most market leaders in Europe.

Figure 3: Magyar Telekom market share in Hungary, 2015-21 (% of active SIM card with voice traffic)



Source: NMHH

Figure 4: Magyar Telekom market share in Hungary, 2015-21 (% of active SIM card with internet traffic)



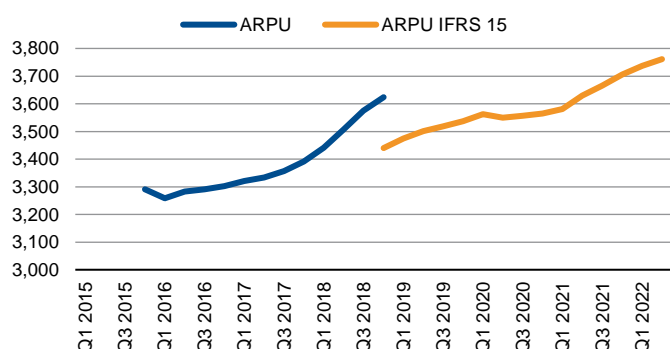
Source: NMHH

5G auctions took place in Hungary in March 2020 (HUF 87bn for Magyar Telekom), followed by some spectrum renewal in January 2021 (HUF 84bn for Magyar Telekom) at reasonable prices. DIGI, a broadband provider, which had been acting as a mobile virtual network operator with a marginal 1,800 MHz of spectrum purchased in 2014 (with service

starting in 2019), tried to participate in these auctions. National regulator NMHH determined that DIGI did not fulfil the conditions for applying, preventing DIGI's full entry into the Hungarian mobile market. Magyar Telekom's average revenue per user (ARPU) for mobile has been increasing by about 3% over the last few years, a rare feat in Europe. According to the latest European Commission benchmark, Hungary is among the most expensive markets for mobile services.

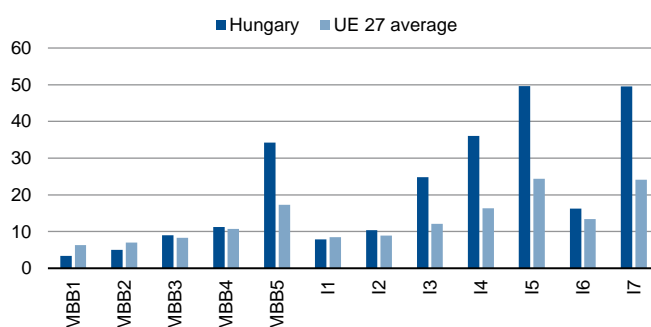
In August 2022, Hungarian IT-telecommunication group 4iG, which purchased DIGI in 2021, announced it would take over Vodafone's Hungarian business (mobile and fixed), with the help of a state-owned holding.

Figure 5: Magyar Telekom mobile ARPU (HUF), 12-month rolling average, 2015-22



Source: Magyar Telekom

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

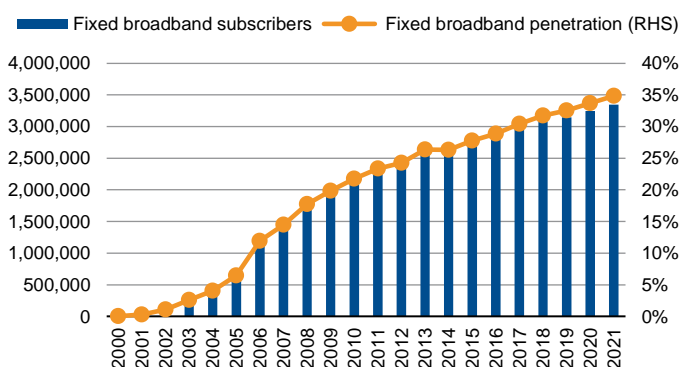


Source: European Commission

Hungary: strong position for cable

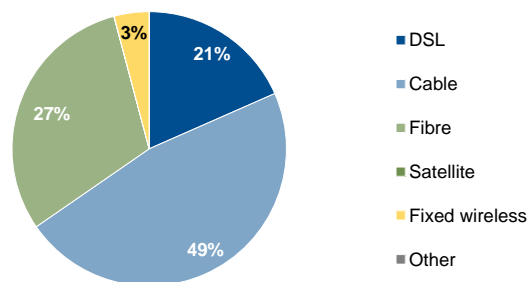
Magyar Telekom is also Hungary's leader in the growing market of fixed broadband, where subscriber numbers are increasing by around 3% a year. Cable operators own much of Hungary's fixed-broadband market, which is not common in Europe. Even more unusual is that Magyar Telekom owns (and sometimes rents)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

Figure 7: Fixed broadband subscribers and penetration in Hungary, 2000-21



Sources: ITU, NMHH, Scope estimates

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



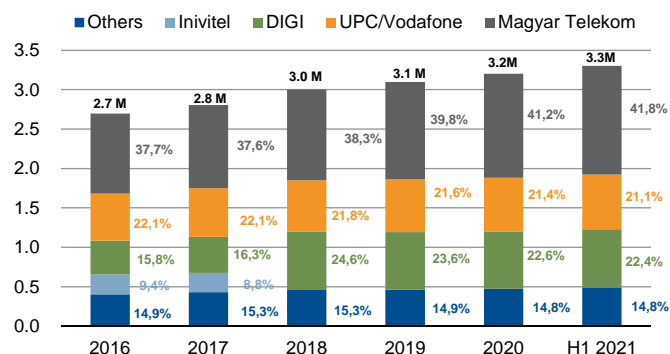
Source: OECD

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. At about the same time, DIGI bought the smaller fixed service operator Invitel and became the second largest player in Hungary. 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 42% of customers against 6% seven years ago) and supported by the acquisition of smaller cable operators. Pricing for these services in Hungary are generally

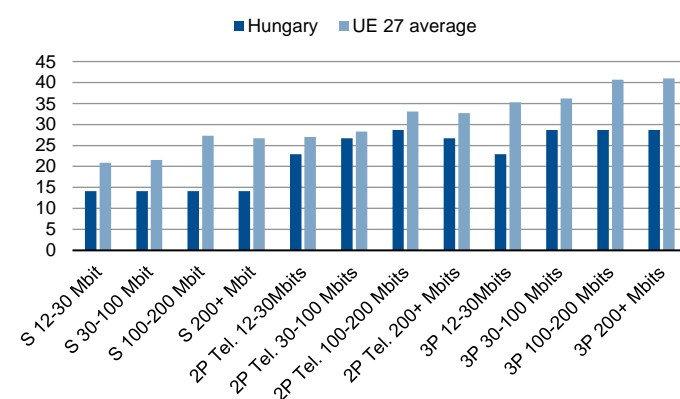
lower than the EU average: of the latest 12 European Commission broadband baskets, the average price is 29% below the EU-27 average.

Figure 9: Fixed broadband market share in Hungary



Sources: Magyar Telekom, NMHH

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



Source: European Commission

The pending acquisition of Vodafone Hungary by 4iG, which already controls DIGI, could lead to a new market leader in broadband, slightly above Magyar Telekom. Even so, it is unlikely that such an acquisition would materially affect Magyar Telekom's competitive position in the short to medium term.

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 brand), with its market share estimated at about 16%.

In terms of diversification, the group is mostly focused on telecommunications services in Hungary and, to a 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 margin (EBITDA margin after leases of 31% in 2021) is lower than for most European incumbents focused domestically, typically at around 40%, partly due to significant telecoms and utility taxes in Hungary.

Financial risk profile: A-

The main driver of debt in the last years at Magyar Telekom are its investments in spectrum, with auctions in 2020 and 2021 and some payments made in early 2022. Additionally, in the first half of 2022, the Hungarian government announced a temporary supplementary telecommunications tax for 2022 and 2023 of about HUF 25bn, which will put pressure on group margins (about 3pp). Finally, the group recently included clauses in its general terms and conditions that allow price changes based on the consumer price index, which could apply from April 2023.

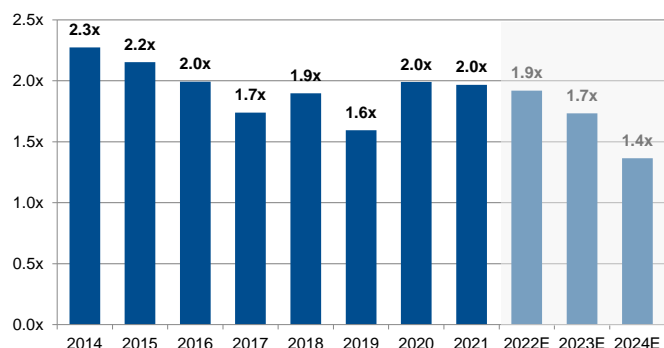
Leverage stood at 2.0x at YE 2021 after declining in recent years but picked up following the spectrum investments. We expect leverage to decrease slightly in the coming years and at a faster pace in 2024 once the temporary telecoms tax is lifted, thus remaining below 2.0x. Scope-adjusted funds from operations/EBITDA should follow a similar trend.

Debt movement driven by spectrum payments and supplementary telecom tax

Leverage expected to remain below 2.0x

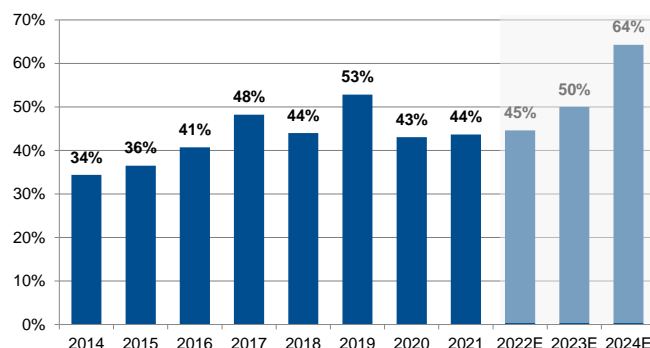


Figure 11: Scope-adjusted debt/EBITDA, 2014-24E



Sources: Magyar Telekom, Scope estimates

Figure 12: Scope-adjusted funds from operation/debt, 2014-24E



Sources: Magyar Telekom, Scope estimates

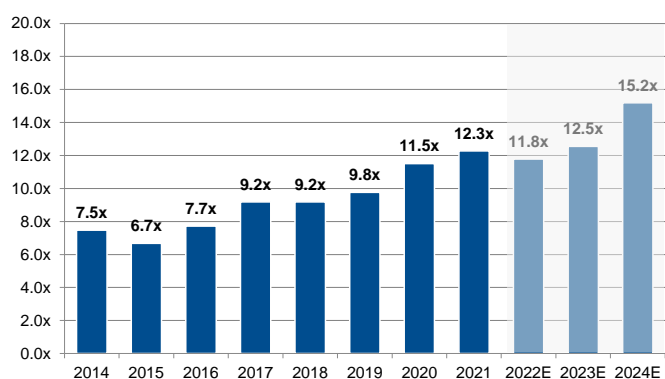
Very strong debt protection

We expect debt protection to remain very strong at well above 10%, even with spectrum investments.

Good cash flow cover

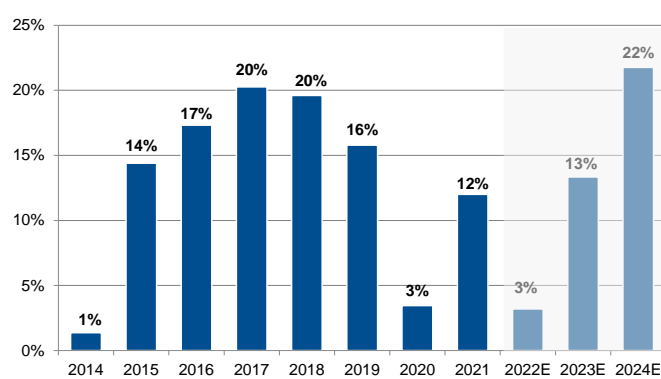
Over the last eight years, Scope-adjusted free operating cash flow/debt ratio has averaged 13%, with a peak of 20% in 2017 and 2018. Excluding exceptional figures in 2014 and 2020 when Magyar Telekom made spectrum investments, the average would be 17%. We expect the ratio to reduce significantly in 2022 due to spectrum payments and to stand at 13% and 22% in 2023 and 2024 respectively.

Figure 13: EBITDA/interest cover, 2014-24E



Sources: Magyar Telekom, Scope estimates

Figure 14: Scope-adjusted free operating cash flow/debt, 2014-24E



Sources: Magyar Telekom, Scope estimates

Adequate liquidity

Over the last eight years, the combination of cash, free operating cash flow and undrawn committed lines has averaged 1.4x of short-term debt, reaching 1.1x at end-2021. 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	2022E	2023E	2024E
Unrestricted cash (t-1)	13,463	13,463	13,463
Open committed credit lines (t-1)	43,500	43,500	43,500
Free operating cash flow	14,478	56,628	82,178
Short-term debt (t-1)	38,087	38,087	38,087
Coverage	188%	>200%	>200%



Supplementary rating drivers: +/- 0 notches

Although Magyar Telekom is strongly financially integrated into the Deutsche Telekom group (which owns 61% 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, we do not consider that the parent's credit risk profile to constrain Magyar Telekom's creditworthiness

Long-term rating: BBB+

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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