4iG Nyrt
Hungary, Telecommunication services

SCOPE **BB-** Positive

Key metrics

			Scope estimates	
Scope credit ratios	**2021**	**2022**	**2023E**	**2024E**
Scope-adjusted EBITDA/interest cover	5.7x	6.3x	2.7x	3.6x
Scope-adjusted debt/EBITDA	35.4x	6.3x	5.3x	4.2x
Scope-adjusted funds from operations/debt	2%	10%	11%	16%
Scope-adjusted free operating cash flow/debt	3%	-1%	-3%	5%

Rating rationale

We have raised the Outlook to Positive from Stable on 4iG's BB- issuer rating.

The business risk profile (assessed at BBB-) is supported by the good market share in mobile and strong position in fixed broadband. The company's degree of diversification remains moderate as it is highly concentrated in telecoms in Hungary. Profitability is likely to continue improving with progressive merger-related cost savings and the progressive removal of sector-specific taxes.

The company's financial risk profile (assessed at B+) is supported by a slightly improved forecasted leverage as measured by Scope-adjusted debt/EBITDA around 4.2x in 2024. The company benefits from equity financing from state-owned holding company Corvinus Zrt supporting interest coverage at more than 3x. 4iG has no significant debt maturing in the next three years as maturities, including the recent issuance, are spread over an extended period time. Scope deems liquidity adequate in the short term.

As regards supplementary rating drivers, we assess 4iG's financial policy as a negative rating driver (by one notch): with an originally limited exposure to telecoms and very large, mainly debt-funded acquisitions, it leads to increased execution risks.

Outlook and rating-change drivers

The Positive Outlook on 4iG's rating reflects the expected deleveraging in line with the company's stated financial policy and progress in the integration of acquisitions, with no significant M&A.

An upgrade may be warranted if profitability improved beyond Scope's base case and a better communication of capital allocation priorities could potentially remove the financial policy notching applied, and with Scope-adjusted debt/EBITDA maintained below 4x.

A return to Stable Outlook may be warranted if 4iG is deemed unable to deleverage, with Scope-adjusted debt/EBITDA remaining above 4x. Further ratings downside is possible if the Scope-adjusted debt/EBITDA remained high at around 5x, but the probability of such a negative action is seen as remote in the short to medium term.

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
6 Jan 2023	Upgrade	BB-/Stable
9 Nov 2022	Placement under review	B+ under review for a possible upgrade
2 Dec 2021	Downgrade	B+/Stable
24 Sep 2021	Placement under review	BB- under review for a possible downgrade

Ratings & Outlook

Issuer	BB-/Positive
Senior unsecured debt	BB-

Analyst

Jacques de Greling
+33 1 82 88 23 70
j.degreling@scoperatings.com

Related Methodology

General Corporate Rating Methodology; October 2023

Scope Ratings GmbH

Lennéstraße 5
10785 Berlin

Phone +49 30 27891 0
Fax +49 30 27891 100

info@scoperatings.com
www.scoperatings.com

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Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• Number two mobile operator in Hungary and market leader in fixed broadband in Hungary • Market leader in mobile services in Albania and Montenegro, number two position in fixed broadband in Albania • Low cyclicity of telecoms • Improved telecoms revenue diversification and wider customer base, with Hungary remaining the core market (around 85% of revenue) • Solid EBITDA margin, above 30%	• Financial policy and weak credit metrics as mostly debt-financed acquisitions • Heightened execution and integration risks related to recent acquisitions

Positive rating-change drivers	Negative rating-change drivers
• Stabilisation of the group structure with no new material M&A; successful integration of the acquired companies and a better communication of capital allocation priorities • Scope-adjusted debt/EBITDA maintained below 4x	• A return to Stable Outlook may be warranted if 4iG is deemed unable to deleverage, with Scope-adjusted debt/EBITDA remaining above 4x • Further downside possible if Scope-adjusted debt/EBITDA remains high around 5x

Corporate profile

4iG was originally one of the largest players in Hungary's fragmented IT market and has recently engaged in strong M&A-driven growth, which transformed the group into a telecom-focused group, as telecoms now represent about 70% of group revenue. All acquired telecoms businesses are now regrouped under the 77% subsidiary Antenna Hungaria (of which the Hungarian state owns 23%), both in Hungary (DIGI, Invitech) and abroad (One in Albania and Montenegro). The joint acquisition of Vodafone Hungary by Antenna Hungary and state-owned holding Corvinus Zrt has more than double 4iG's telecoms revenue. The company is listed on the premium segment of the Budapest Stock Exchange, with Gellért Jászai as a controlling shareholder.

Financial overview

				Scope estimates		
Scope credit ratios	**2020**	**2021**	**2022**	**2023E**	**2024E**	**2025E**
Scope-adjusted EBITDA/interest cover	> 20x	5.7x	3.1x	2.7x	3.6x	4.3x
Scope-adjusted debt/EBITDA	Net cash	35.4x	6.3x	5.3x	4.2x	3.8x
Scope-adjusted funds from operations/debt	Net cash	2%	10%	11%	16%	19%
Scope-adjusted free operating cash flow/debt	Net cash	3%	-1%	-3%	5%	4%
Scope-adjusted EBITDA in HUF m						
EBITDA	5,048	12,096	74,054	184,800	212,400	233,400
Dividends received	0	0	2,251	0	0	0
Other items	0	0	0	-15,000	0	0
Scope-adjusted EBITDA	**5,048**	**12,096**	**76,305**	**169,800**	**212,400**	**233,400**
Funds from operations in HUFm						
Scope-adjusted EBITDA	5,048	12,096	76,305	169,800	212,400	233,400
less: (net) cash interest paid	-41	-2,109	-24,568	-62,000	-59,000	-54,000
less: cash tax paid per cash flow statement	-773	-1,426	-4,002	-10,500	-11,500	-13,000
add: dividends from associates	0	0	0	0	0	0
Change in provisions	0	0	0	0	0	0
Funds from operations	**4,234**	**8,561**	**47,735**	**97,300**	**141,900**	**166,400**
Free operating cash flow in HUFm						
Funds from operations	4,234	8,561	47,735	97,300	141,900	166,400
Change in working capital	-1,504	5,782	-9,115	-23,000	23,000	-2,000
Non-operating cash flow	795	3,623	-25,978	4,112	0	0
less: capital expenditure (net)	-1,229	-9,849	-15,640	-75,000	-88,000	-91,000
less: lease amortisation	-162	3,502	-3,646	-32,640	-32,640	-32,640
Free operating cash flow (FOCF)	**2,134**	**11,619**	**-6,644**	**-29,228**	**44,260**	**40,260**
Net cash interest paid in HUFm						
Net cash interest per cash flow statement	41	2,109	24,568	62,000	59,000	54,000
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	**41**	**2,109**	**24,568**	**62,000**	**59,000**	**54,000**
Scope-adjusted debt in HUFm						
Reported gross financial debt	4,012	425,813	475,610	889,000	884,000	887,000
less: subordinated (hybrid) debt	0	0	0	0	0	0
less: cash and cash equivalents	-7,205	-266,530	-45,961	-56,020	-95,280	-138,540
add: non-accessible cash	0	266,530	45,961	56,020	95,280	138,540
add: pension adjustment	0	0	0	0	0	0
add: operating lease obligations	0	0	0	0	0	0
Other items	627	2,456	4,888	9,000	9,000	9,000
Scope-adjusted debt	**-2,566**	**428,269**	**480,498**	**898,000**	**893,000**	**896,000**

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Environmental, social and governance (ESG) profile[1]

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)

Recent growth in telecoms through debt-financed acquisitions

While Mr Jászai (52% controlling shareholder) plays a key role in the company, 4iG has appropriate governing bodies and an experienced management. The group has significantly expanded its management team following its recent growth. The recent growth in telecoms within the group's activities was achieved through acquisitions, mostly debt-financed, leading to significant execution and integration risks

[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.

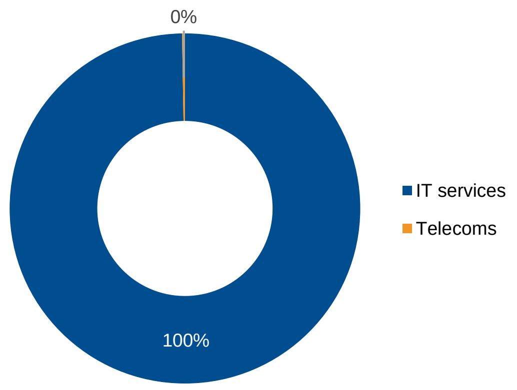
Business risk profile: BBB-

Industry risk profile: A

The industry risk profile for telecoms stands at A, based on low cyclicality (subscriptions are for a basic, necessary service), medium entry barriers (licences, network rollout), and medium-to-low substitution risk (over-the-top services).

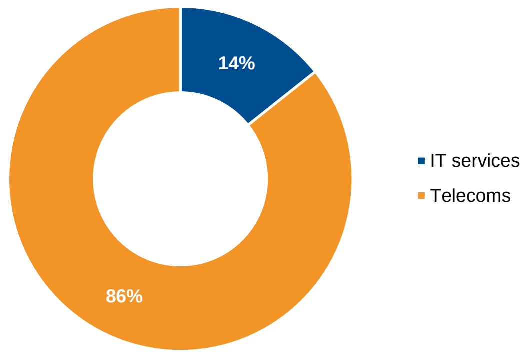
4iG's revenue mix has shifted significantly from being almost exclusively IT-focused in 2020 to mostly telecoms. The acquisition of Vodafone Hungary in January 2023 has reinforced this trend, as we expect IT services to represent about 14% of total revenue in 2023.

Figure 1: FY 2020 4iG group revenue by business (%)



Source: 4iG

Figure 2: FY 2023E 4iG group revenue by business (%)



Sources: 4iG, Scope estimates

4iG has made the following telecoms acquisitions:

- June 2021: HDT, a Hungarian very-small-aperture terminal service provider with a revenue of HUF5bn;

- September 2021: Invitech, a Hungarian corporate telecoms & IT service provider, with a revenue of HUF25bn;

Numerous telecoms acquisitions

- December 2021: Telenor Montenegro, a mobile-only operator in Montenegro, with a revenue of HUF15bn;

- January 2022: DIGI, a Hungarian fixed broadband provider, with a revenue of HUF70bn;

- March 2022: ALBtelecom, an Albanian mobile (and fixed broadband) operator, with a revenue of HUF20bn;

- March 2022: One Telecommunication, an Albanian mobile-only operator, with a revenue of HUF25bn

- January 2023: Vodafone Hungary, the number two telecoms operator in Hungary, with a revenue of HUF281bn

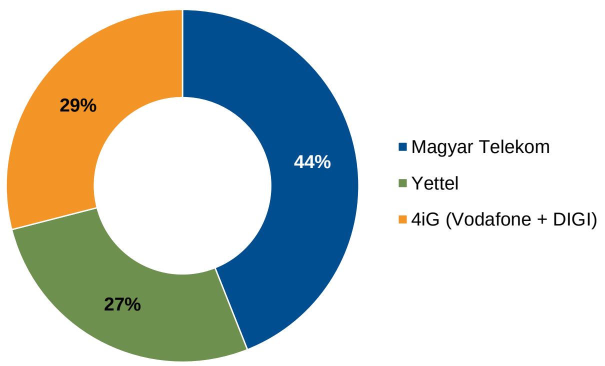
In April 2022, the state-owned national TV and radio broadcaster Antenna Hungaria (with a revenue of HUF40bn) was taken over by 4iG, with 4iG bringing all its telecoms activities. 4iG now owns 77% of Antenna Hungaria (and the state owns 23%), which now own all telecoms activities. In January 2023, 4iG finalised the control of Vodafone Hungary, a Hungarian mobile and fixed broadband provider with a revenue of about HUF280bn, while state-owned holding Corvinus Zrt acquired a minority share (49%). In March 2023, Antenna Hungaria swapped its 25% stake in mobile operator Yettel to Corvinus Zrt in exchange for an additional 19.5% stake in Vodafone, raising Antenna Hungaria's stake to 70.5%.

Number two on the Hungarian mobile market

The acquisition of Vodafone Hungary provides 4iG with a substantial market share in the large domestic mobile market, where DIGI's share was negligible; these two subsidiaries put together have about 3.2m subscribers, broadly on par with Yettel. We do not foresee that the forthcoming change of control of Yettel (by Emirati e&) will change the Hungarian mobile market. In the smaller fixed broadband market, Vodafone Hungary's and DIGI's combined share (Vodafone having previously acquired UPC Hungary) makes 4iG the market leader with about 1.5m subscribers, ahead of the incumbent Magyar Telekom, a rare situation in Europe. In the TV market, 4iG is now the market leader with about 47% of combined market share. With the Vodafone acquisition, the market share of 4iG within the Hungarian telecoms market is now good.

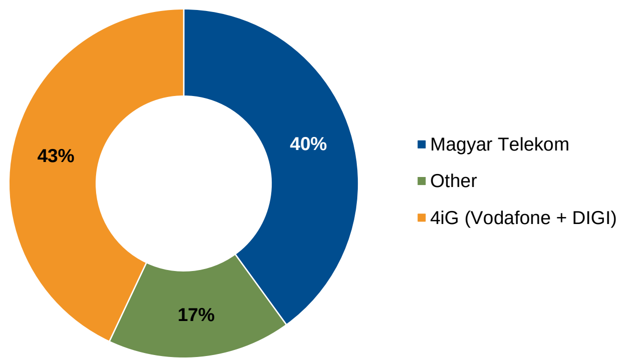
Market leader in broadband in Hungary

Figure 3 Mobile market shares in Hungary (% subscribers)



Source: 4iG, Scope estimates

Figure 4: Fixed broadband market shares in Hungary (% subscribers)



Sources: 4iG, Scope estimates

In Albania (about 9% of group revenue), 4iG's business is complemented by two operators ALBtelecom and One Telecommunication, now merged under the brand One, making it the clear market mobile leader, with a market share of about 50% (facing competition from only one other mobile operator), an exceptionally high level in Europe. In Montenegro, the subsidiary is the market leader (in revenue) in a three-player mobile market.

Diversification remains moderate as the acquisition of Vodafone Hungary has increased service diversification (mobile) and widened the customer base, but this is somewhat compensated by the higher concentration of revenue in Hungary (about 85% in 2023).

In 2024 and 2025, with the end of the utility tax in Hungary and the end of the special transitory telecommunication tax and progressive synergies (bundled offers, network and management sharing), we forecast EBITDA margins above 30% for 4iG, compared with 31% (excluding capital gain on mobile assets of DIGI) reported by 4iG group for the first nine months of 2023.

Financial risk profile: B+

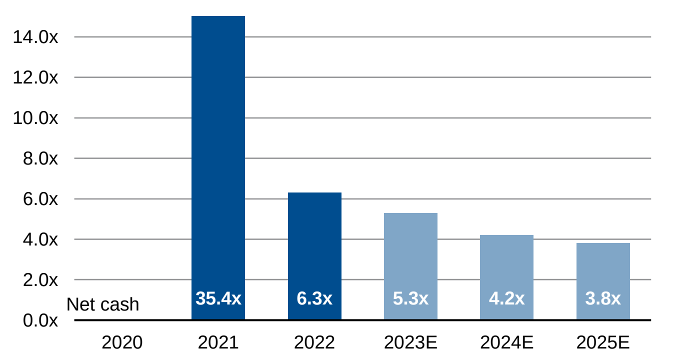
No cash netting

We do not include cash and cash equivalent in our Scope-adjusted debt calculation, as due to the size and complexity of transactions as well as the pledges granted for the new loans, cash and cash equivalent might not be permanent and accessible.

Scope-adjusted debt/EBITDA trending to 4.0x

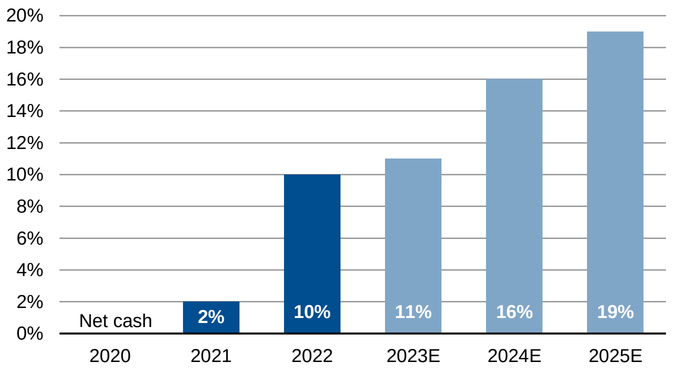
Leverage has been partly distorted in the past by the fact that not all newly acquired subsidiaries were consolidated over 12 months. Following the acquisition of Vodafone Hungary end of January 2023, we expect that in 2024 (with the new subsidiary consolidated over 12 months), Scope-adjusted debt/EBITDA will be around 4.2x, helped by synergies starting to show and the end of the utility tax. Similarly, we expect Scope-adjusted funds from operations/debt to be around 16% in 2024.

Figure 5: 4iG group Scope-adjusted debt/EBITDA (x)



Source: 4iG, Scope estimates

Figure 6: 4iG group Scope-adjusted debt/EBITDA (x)

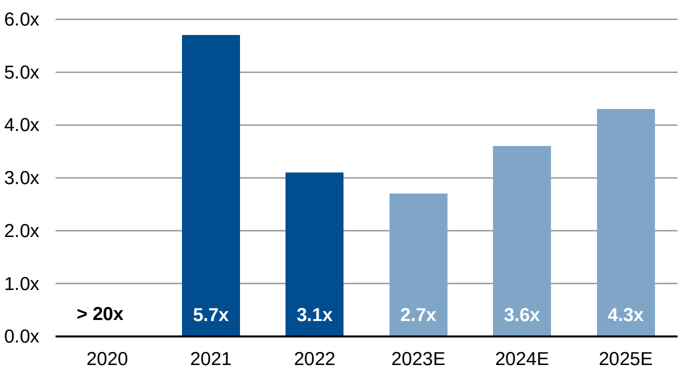


Sources: 4iG, Scope estimates

EBITDA/interest cover trending above 3x

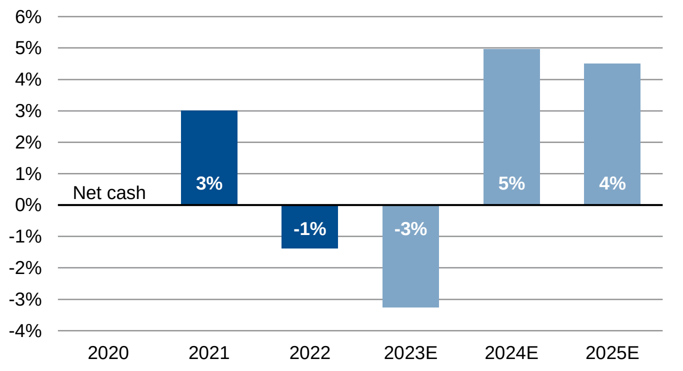
Following the acquisition of Vodafone Hungary, the average cost of debt for the group has increased slightly, as the average bond interest rate was around 6%, but interest cover will improve progressively above 3x with the expected EBITDA improvement, driven by synergies starting to show up and the end of sector-specific taxes in Hungary.

Figure 7: Scope-adjusted EBITDA/interest cover (x)



Source: 4iG, Scope estimates

Figure 8: Scope-adjusted FOCF/debt (%)



Sources: 4iG, Scope estimates

Scope-adjusted FOCF/debt expected to remain below or at 5%

We expect Scope-adjusted FOCF/EBITDA to remain weak in the coming years as the group will make significant investments to integrate all acquired telecoms subsidiaries, in particular IT systems, and leases outflows. As a result, we expect Scope-adjusted FOCF/debt to remain below 5% in the forecasting period, partly compensated by the disposal of DIGI mobile assets following the acquisition of Vodafone. 4iG has agreed in November 2023 with the Hungarian government to reach some fixed broadband coverage and 5G mobile coverage by 2028.

Adequate liquidity

Liquidity is adequate in the short term. Nevertheless, it could become an issue, e.g. in the event of sharp working capital swings, large capex or M&A or if approaching debt maturities were not refinanced. The 20-year loans for the acquisition of Vodafone have no maturity for the first 10 years. For 2024, we expect short-term financial debt to be more than 2x covered by a combination of available cash and cash equivalents as well as positive expected free operating cash flow.

Balance in HUF m	2023E	2024E	2025E
Unrestricted cash (t-1)	45,961	56,020	95,280
Open committed credit lines (t-1)	0	0	0
Free operating cash flow	-29,228	44,260	40,260
Short-term debt (t-1)	7,713	12,000	7,000
Coverage	> **200%**	> **200%**	> **200%**

Supplementary rating drivers: - 1 notch

Credit-negative financial policy

We note the strong involvement of the state into 4iG via the provision of equity, loans and guarantees. As regards supplementary rating drivers, we assess 4iG's financial policy as a negative rating driver. This is due to its very large, mainly debt-funded acquisitions and originally limited exposure to telecoms services, leading to heightened execution and integration risks. As a result, we have adjusted 4iG's standalone credit quality of BB downwards by one notch.

Long-term debt rating: BB-

In March 2021 and December 2021, 4iG Nyrt. issued a HUF 15bn senior unsecured bond (ISIN: HU0000360276) and HUF 370bn senior unsecured bond (ISIN: HU0000361019) through the Hungarian Central Bank's Bond Funding for Growth Scheme. The bond proceeds were used for acquisitions in telecoms (Invitech's Hungarian operations, DIGI's Hungarian operations, Telenor Montenegro, and ALBtelecom and One Telecommunication, both in Albania). The bonds have a tenor of 10 years and a fixed coupon of respectively 2.9% and 6.0%. Bond repayment is in four tranches starting from 2026, with 10% of the face value payable yearly, and a 50% balloon payment at maturity. Scope notes that 4iG's senior unsecured bond issued under the Hungarian Central Bank's bond scheme has several accelerated repayment clauses. The clauses require 4iG to repay the nominal amount (HUF 385bn) in case of rating deterioration (twoyear cure period for a CCC rating; repayment within respectively 10 and 60 days after the bond rating falls below CCC, which could have default implications). In addition to the rating deterioration covenant, bond covenants include a financial covenant of maximum 5.0x net debt/EBITDA to be first measured on YE 2024 results where breaches in three consecutive years would cause an event of default (meaning the earliest is a risk when checked in 2027 spring based on 2024-26 results). There is also a list of soft covenants listed in the bond prospectuses.

Senior unsecured debt rating: BB-

Our recovery analysis indicates an 'average recovery' for senior unsecured debt. Scope sees some pressure on expected recovery rates due to i) pledges in favour of creditors, which could lead to restrictions on the transfer of funds within the group, and ii) future debt issuance will mainly take place at the level of 4iG's subsidiaries, resulting in structural subordination of senior unsecured debt at the level of 4iG. This expectation translates into a BB- rating for this debt category, the same level as the issuer rating. The recovery is based on an expected distressed enterprise value as a going concern in a hypothetical default scenario in 2025.

Scope Ratings GmbH

Headquarters Berlin

Lennéstraße 5
D-10785 Berlin

Phone +49 30 27891 0

Frankfurt am Main

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389 0

Paris

10 avenue de Messine
FR-75008 Paris

Phone +33 6 6289 3512

Oslo

Karenslyst allé 53
N-0279 Oslo

Phone +47 21 09 38 35

Madrid

Paseo de la Castellana 141
E-28046 Madrid

Phone +34 91 572 67 11

Milan

Via Nino Bixio, 31
20129 Milano MI

Phone +39 02 30315 814

Scope Ratings UK Limited

London

52 Grosvenor Gardens
London SW1W 0AU

Phone +44 20 7824 5180

info@scoperatings.com
www.scoperatings.com

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