Duna House Holding Nyrt.
Hungary, Business Services

SCOPE BB- STABLE

Key metrics

Corporate profile

Publicly listed Duna House Holding Nyrt. was founded in 1998 in Hungary and offers real estate and loan brokerage services as well as other real estate transaction-related services. It operates an integrated platform consisting of an online real estate marketplace together with a national network of both self-operated and franchised physical offices. The group is also active in residential property developments and has – in addition to its own property investments – established Hungary's first public, open-end residential property asset management fund.

			Scope estimates	
Scope credit ratios	**2019**	**2020**	**2021E**	**2022E**
Scope-adjusted EBITDA/interest cover (x)	25.5x	257.4x	5.6x	10.0x
Scope-adjusted debt (SaD)/EBITDA	2.9x	3.5x	1.1x	1.3x
Free operating cash flow/SaD	-26%	-2%	271%	88%
Scope-adjusted free funds from operations/SaD	30%	29%	76%	59%

Rating rationale

Scope Ratings Scope Ratings affirms the issuer rating of BB-/Stable for Duna House Holding Nyrt. The debt class rating for senior unsecured debt is affirmed at BB-.

The affirmation is mainly driven by the stable business risk profile (assessed at BB-) that benefits from the group's market position as one of the leading real estate and loan brokerages in its home market Hungary as well as in Poland. Diversification is still deemed robust as the group currently derives its operating profits from four different segments: real estate and loan brokerage, franchise fees, own real estate developments as well as asset management fees.

Moreover, the group is currently active in three different CEE markets, and we expect a further geographical expansion in the CEE region. Client base granularity is high and further growing since the group is operating as a service provider to retail clients with little recurring transactions from a single client. The issuer's business risk profile remains constrained by the small absolute size of the business and the different segments within the relatively fragmented markets it is operating in. We expect Scope-adjusted EBITDA margins to remain within a range of c. 14% to 16% in our base case financial forecast, also after a small negative impact from the Covid-19 pandemic.

While we expected the execution of business acquisitions in the group's core real estate and loan brokerage business in 2020 and 2021, this inorganic expansion has been postponed to 2022-2024, due to a change in target companies. However, the management's intention is still to acquire other brokerage businesses in Central Eastern and Southern Europe to expand its geographical footprint and realise synergies.

The financial risk profile of the issuer (assessed BB) continues to benefit from its strong interest coverage of 5x to 10x, both on a sustained basis historically and expected going forward, as well as relatively low financial leverage, expected to stay at below 2.0x going forward.

Ratings & Outlook

Corporate rating	BB-/Stable
Senior unsecured rating	BB-

Analyst

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Related Methodology

Corporate Rating Methodology 6 Jul 2021

European Real Estate Corporates Methodology 15 Jan 2021

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However, the financial risk profile is currently constrained by the high volatility of cash flows caused by the real estate development activities as well as a high dependency on the real estate transactions market in CEE. Our assessment of the financial risk profile also incorporates execution and integration risks for the businesses to be acquired and the resulting limited visibility on operating profit contributions from the targeted companies.

Liquidity is considered adequate considering that currently no further financial debt besides the HUF 6.6bn 10-year bond issued in 2020 exists except for one HUF 4.7bn bank loan. That bank loan is tied to a current construction project that we expect to be sold completely in 2021 to 2022.

Outlook and rating-change drivers

The Outlook for Duna House Holding Nyrt. is Stable and incorporates our view of the stability of the core real estate and loan brokerage business and the company's ability to generate cash. Moreover, the Stable outlook reflects our expectation that the issuer will be able to keep financial leverage (SaD/EBITDA) at below 3.0x after the anticipated temporary spike in 2019 and 2020 that was mostly due to the execution of the Forest Hill real estate development project.

A positive rating action would require the issuer to significantly increase visibility on the planned expansion of its business while showing financial leverage of less than 3.0x on a sustained basis including potential acquisitions.

A negative rating action could be warranted if the issuer shows an increase in financial leverage to above 4.0x on a sustained basis. This could be caused by a slump in revenues due to overall transaction market weakness or substantial additional debt-funded investments beyond our financial base case.

Rating drivers

Positive rating drivers	Negative rating drivers
• Strong market position in CEE real estate and loan brokerage (first in Hungary and Poland) • High organic revenue growth • Asset-light business model; hence limited financial debt and moderate financial leverage • Diversified among several real estate-related services and countries; high customer granularity	• Strong dependency on general transaction dynamics in the CEE real estate markets with limited non-transaction-based recurring revenue • Fierce competition in online real estate brokerage • Execution and integration risks posed by planned international expansion via M&A

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• Significantly higher visibility on the planned expansion of the business in terms of size and market shares while showing financial metrics in line with our expectations	• Financial leverage of above 4.0x on a sustained basis

Financial overview

			Scope estimates	
Scope credit ratios	**2019**	**2020**	**2021E**	**2022E**
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Scope-adjusted debt (SaD)/EBITDA (x)	2.9x	3.5x	1.1x	1.3x
Free operating cash flow/SaD	-26%	-2%	271%	88%
Funds from operations/SaD	30%	29%	76%	59%
Scope-adjusted EBITDA in HUF ‘000	**2019**	**2020**	**2021E**	**2022E**
EBITDA	**1,616,281**	**1,557,829**	**1,678,429**	**2,270,402**
Operating lease payments in respective year	0	0	0	0
Scope-adjusted EBITDA	**1,616,281**	**1,557,829**	**1,678,429**	**2,270,402**
Scope-adjusted funds from operations in HUF ‘000	**2019**	**2020**	**2021E**	**2022E**
Scope-adjusted EBITDA	**1,616,281**	**1,557,829**	**1,678,429**	**2,270,402**
less: cash interest as per cash flow statement	-63,497	-6,053	-300,000	-226,680
less: cash tax paid as per cash flow statement	-193,102	-279,226	-269,503	-357,375
add: dividends received from shareholdings	51,543	310,478	250,000	0
Scope-adjusted funds from operations	**1,411,225**	**1,583,028**	**1,358,926**	**1,686,348**
Scope-adjusted debt in HUF ‘000	**2019**	**2020**	**2021E**	**2022E**
Reported gross financial debt	6,380,810	11,674,757	8,674,757	6,974,757
less: cash, cash equivalents	-2,525,673	-6,902,151	-7,621,211	-4,864,100
add: restricted cash	897,947	732,626	732,626	732,626
Scope-adjusted debt	**4,753,084**	**5,505,232**	**1,786,172**	**2,843,283**

Business risk profile: BB-

Industry risk of BB+, driven by core services and additional development risks

In recent years, two-thirds of EBITDA were generated via various business services, mainly through real estate and loan brokerage fees as well as franchise fees. Hence, we apply a blended industry risk approach with a 67% weighting of the industry risk for business services, which is BBB. The remaining third of EBITDA was generated via real estate developments, thus allowing for a 33% weighted industry risk of B for that segment.

Competitive position

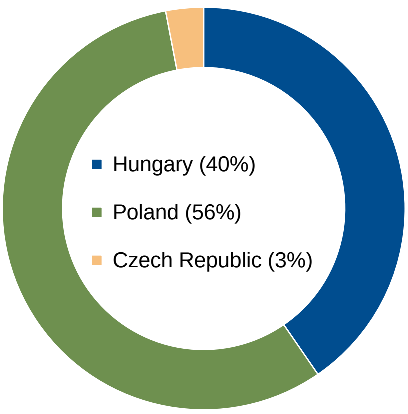
Leading market positions in Hungary and Poland

The issuer's market position remains credit-positive. The group has weathered the Covid-19 pandemic rather well and still operates the largest platform in Poland and one of the two leading real estate brokerage platforms in Hungary. The other one is competitor Otthon Centrum (BB-/Stable), whose size is similar to the issuer's in terms of listings, offices and salespeople. The issuer's market share peaked during a weak phase in the real estate market during 2011-2015. Its current market share in its home market of Hungary ranges from 5% to 8%, both in the real estate and the loan brokerage. Market shares in real estate development and asset management are negligible in our view.

Consolidation might benefit larger players in the medium term

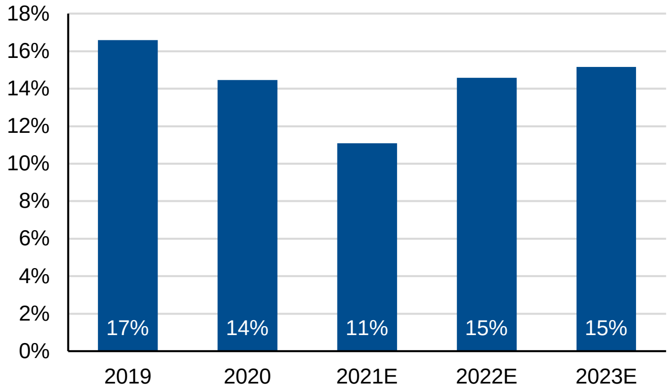
The issuer's single-digit market share despite its market leadership shows the relative fragmentation of its markets. This implies little pricing power but also allows for a potential increase in market share going forward if the real estate brokerage sector continues to consolidate. With the issuer's strategy of supporting its leading network of physical offices with strong online integration and a web-based platform, we deem it likely that the issuer as well as competitor Otthon Centrum will gain further market share in the future.

Figure 1: Geographical diversification, sales



Sources: Duna House Holding, Scope

Figure 2: Profitability (Scope-adjusted EBITDA margin)



Sources: Duna House Holding, Scope

The lion's share of the issuer's revenues is generated in Hungary and Poland. A single digit share of external revenue is from the Czech market and management is planning to grow via acquisitions in the CEE real estate and loan brokerage markets. Geographical diversification is thus spread across but limited to the CEE region.

Customer granularity is very high with the issuer targeting retail brokerage clients and real estate buyers.

In terms of segments, we consider revenues and operating income to be diversified thanks to the different revenue streams from:

1. Real estate brokerage (physical presence and online platform)
2. Loan brokerage

3. Franchise fees
4. Own real estate developments (to be terminated after 2021)
5. Asset management (small EUR 12m real estate fund at this point)

Group operating profitability has ranged from around 15% to 30% in recent years, with fluctuations caused mainly by changes in the segment revenue mix. The group's EBITDA margin has averaged 25%-30% on past real estate developments but is lower on its core brokerage business at 15%-20%. The fast-growing share of loan brokerage fees had the highest EBITDA margins of more than 30% recently.

We expect profitability of around 15% in the Scope-adjusted EBITDA margin in our financial base case which is more conservative than the issuer's business plan.

Positive aspects going forward include the opportunity for the issuer, as one of the two market leaders, to further strengthen its market share if industry consolidation accelerates, which would mitigate price pressure in the medium term.

While we expect the core brokerage business to continue to grow organically and to increase in market share in Hungary and Poland for the coming years, thanks to ongoing industry consolidation, we also expect a reduction in the group's share of own real estate developments after the sales for its projects under development are expected to be completed during 2021 and 2022. This will weigh on profitability and diversification but most likely lead to improvements in its industry risk and lower the volatility of revenues and cash flows, as development project profits were usually clustered around their respective completion dates.

Financial risk profile: BB

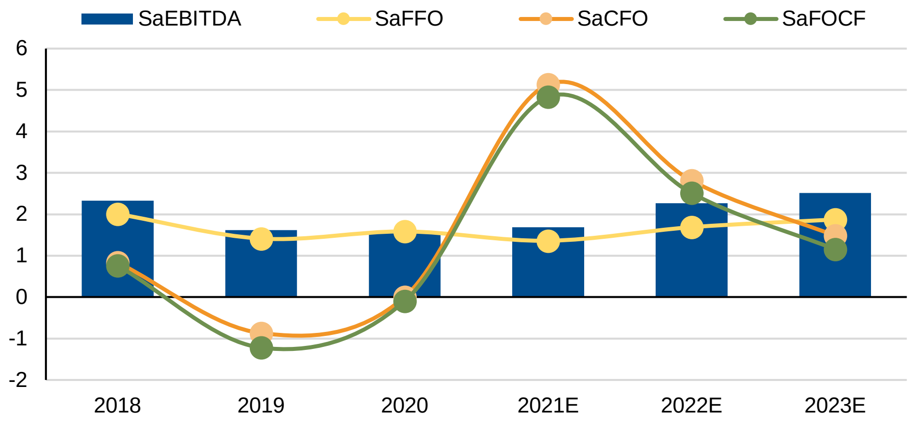
Our rating scenario assumes the following:

1. External revenue growth below issuer's latest business plan forecast as of July 2021 (10% lower p.a. for the forecast period)
2. Increase of all operating costs (COGS, personnel and other expenses) by 3% p.a. above issuer's business plan going forward
3. Average cost of financial debt of 3.25% to 3.5% vs roughly 3% as of today
4. Cash outflows of about HUF 3bn by 2022 for the first instalment payment for one expected larger strategic M&A transaction within the core business segment of real estate and/or loan brokerage. Second instalment of about HUF 2.5bn expected for 2024/25.
5. Complete sale and handover of all remaining units of the real estate development project Forest Hill during 2021 and 2022 and complete repayment of all related project financing
6. No additional development projects besides Forest Hill 2nd stage expected after 2021

Free operating cash flow expected to be smoother after completion of developments

The issuer showed a spike in financial leverage in 2019 and 2020 due to the investment in a real estate development scheduled for delivery in 2019-2021. Going forward we anticipate a return to a moderate leverage of circa 1.2x, even based on lower operating profitability.

Figure 3: Cash flow overview (HUF bn), Scope-adjusted figures

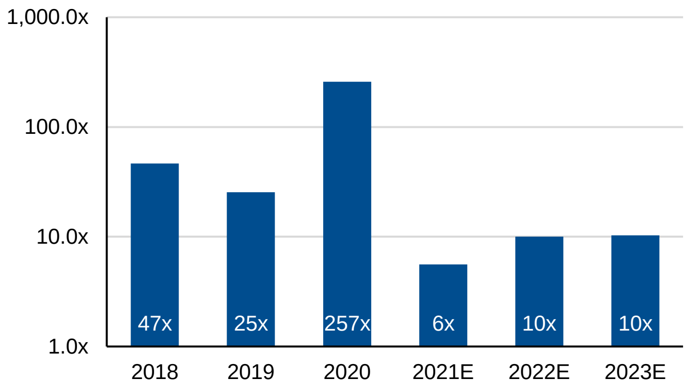


Sources: Duna House Holding, Scope

While Scope-adjusted EBITDA and FFO generation has been relatively stable, we see elevated volatility of free operating cash flows (Figure 3) which is caused by the real estate development activities of the group. Most recently we saw large cash outflows for the start of the Forest Hill development in 2019 and expect another significant cash outlay for the planned acquisition in 2022 and expect as a result a large cash inflow from the sale of all units of Forest Hill in 2021 and 2022.

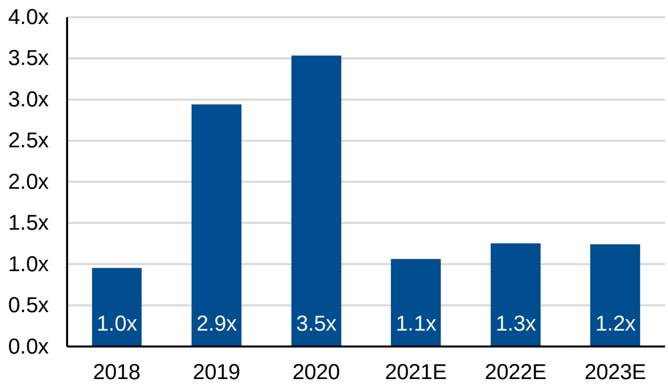
Our current financial base case does not include further real estate development activities after 2022, meaning cash flow is expected to be smoother going forward. We nevertheless point out that the group has remaining land plots, which create the potential for further future developments.

Figure 4: Scope-adjusted EBITDA interest cover



Sources: Duna House Holding, Scope estimates

Figure 5: Leverage (SaD/EBITDA)



Sources: Duna House Holding, Scope estimates

Interest cover, as seen in Figure 4, has been at very comfortable levels and is expected to stay robust thanks to the issuer's asset- and debt-light business model.

Robust interest coverage

Liquidity is adequate. The company's unrestricted cash balance and free operating cash flow excluding discretionary spending cover short-term debt repayment needs by well over 2x going forward, as shown in Figure 6.

Liquidity: adequate

Figure 6: Liquidity

in HUF '000	2020	2021E	2022E
Short-term debt (t-1)	-361,338	-4,751,950	-1,751,950
Unrestricted cash (t-1)	2,525,673	6,902,151	7,621,211
Free operating cash flow (t)[1]	-96,332	4,834,366	2,512,494
Liquidity (internal)	**6.5x**	**2.3x**	**5.3x**
Open committed credit lines (t)	700,000	700,000	798,221
Liquidity (internal and external)	**8.4x**	**2.5x**	**5.8x**

Source: Scope estimates

Long-term debt ratings

Senior unsecured debt: BB-

We affirm the debt instrument rating of BB- for all senior unsecured debt issued by Duna House Holding Nyrt. The debt category rating reflects the ranking status of the debt, ranking below any secured bank financing. While we have computed an above average recovery rate for the issuer's outstanding senior unsecured debt in a hypothetical default scenario as of year-end 2022 based on a distressed liquidation value, we refrain from any adjustment on the debt instrument rating and rate senior unsecured debt at the same level as the issuer rating. This is due to the material uncertainty on the possible asset values of the group in a hypothetical liquidation scenario.

[1] excl. discretionary spending

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