1 April 2021 Corporates

OPUS Global Nyrt. Hungary, Holdings

BB STABLE

OPUS Global Nyrt. is a Hungarian investment holding company resulting from a merger between OPUS and Konzum in 2019. With about HUF 200bn (EUR 600m) in market capitalisation, it is the fifth largest entity on the Hungarian stock exchange.

The group's investment philosophy focuses on holding majority positions over four industrial sectors: industrials, food processing, energy and tourism. Through its long-term 'buy-and-build' approach, OPUS acquires companies it deems undervalued and then exercises tight operational control to create growth and value. During the last 12 months, several large transactions were undertaken, mainly in the energy division, which is already transitioning away from fossil fuels and into renewables and services. In addition, the size of its asset management division, which traditionally holds minority positions, was significantly decreased to enable a focus on the four core divisions.

Key metrics

			Scope estimates	
Scope credit ratios	**2019**	**2020E**	**2021E**	**2022E**
Total recurring cost cover (x)	6.9	3.0	3.2	3.0
LTV (Scope-adjusted debt/ portfolio market value) (%)	39	33	42	43
Liquidity (%)	2.1	44	44	33

Rating rationale

Scope Ratings has affirmed its BB/Stable issuer rating on Hungary's OPUS Global Nyrt together with the BBB- senior unsecured debt rating (HUF 28.6bn bond maturing in 2029 with a 2.8% coupon).

The ratings continue to reflect OPUS' strong financial risk profile and very sound cost coverage on the holding level, which continue to be supported by a sound liquidity policy in the context of an active M&A phase aimed at reorienting its energy segment. OPUS can easily fund the executed acquisition of electricity distributor E.ON Tiszántúli Áramhálózati Zrt. (Titasz) and the upcoming takeover of gas distributor Tigáz Zrt. through recurring revenues, strong and rising dividend income from core construction activities, divestiture proceeds from Mátrai Erőmű and Buzsák, and new debt.

OPUS plans to issue another bond with a volume of HUF 39bn under the Bond Funding for Growth Scheme of the Hungarian National Bank (MNB). This issuance and the large investment needed to refurbish the hotels of tourism subsidiary Hunguest Hotels Zrt. are likely to cause some deterioration in key credit metrics from 2021. This is not critical, however, because cost coverage was already far above the level needed for the ratings. The ratings also reflect our view of OPUS' buy-and-build investment approach, which is conservative and focused on long-term growth and value through its active control over the subsidiaries' operations.

We also consider the company to be resilient to macroeconomic downturns. This has been shown by the Covid-19 crisis' limited impact on three core segments (tourism as the exception) because they are non-cyclical and governed by long-term trends.

Ratings & Outlook

Corporate ratings	BB/Stable
Senior unsecured rating	BBB-

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Related Methodology

Corporate Rating Methodology, February 2020

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Portfolio diversification improved over the last 12 months, with the sizeable energy segment turning its focus on services and away from production. This improvement is despite all dividends coming from the main industrial company (Mészáros Építőipari Holding Zrt.). OPUS' exposure to four distinct, relatively non-cyclical and less correlated sectors supports its business risk profile. Most of its subsidiaries also have significant growth potential, based on high order backlogs at its construction companies and the substantial recent expansion and modernisation at its food processing companies. Both segments have had high growth in revenues and operating profitability in the past two years. Wheat-processing company Viresol Kft., in contrast, was particularly hit by production delays in the wake of the current crisis. However, dividend income continues to be very highly concentrated, reflecting delayed payouts from the food companies and Hunguest Hotels – the latter for at least two years, in our view, due to the Covid-19 crisis and necessary refurbishments. Thus, income diversification does not support the ratings. By value, diversification is significantly better: there is sizeable value in the companies that are not paying dividends at the moment. In addition, we believe underlying asset values are conservative, also for recovery assumptions (just 50% of asset values used).

The rating reflects increased balance sheet debt at the end of 2021, through the existing 2019 bond (HUF 28.6bn) and the envisaged bond (HUF 39bn). Both issuances along with the sales of subsidiaries have led to strong cash inflow, even after deducting cash used for acquisitions and intercompany loans. This strong liquidity provision serves as a short-term buffer but will need to be used for intercompany loans and the Tigáz acquisition. The two large acquisitions of Titasz and Tigáz were structured to preserve liquidity, enabled by the close joint-venture-like funding of OPUS with Status Energy Kft. This will be supported by plans to sell the Buzsák solar park, which will generate a significant windfall.

While cost coverage seems to cause no issues, leverage as expressed by the loan-to-value ratio (LTV; Scope-adjusted debt to portfolio net asset value) is likely to increase above 40% in the current year, reflecting the significantly increased debt. While this does not threaten the ratings, we have maintained the main driver of the financial risk profile as the cost coverage ratio, which is likely to continue be high at about 3x in 2021. The LTV ratio might also be (conservatively) distorted by the use of underlying asset values reflective of historical book values – especially for the industrial and food processing companies – and thus are likely understated.

We have affirmed the BBB- debt rating to senior unsecured debt issued by OPUS. This reflects the debt's ranking below an insignificant amount of senior secured bank debt and accounts for a significant and growing portfolio net asset value. Senior unsecured debt will be enlarged by the HUF 39bn bond to be placed in 2021. We expect a 'superior' recovery (70%-90%) for outstanding senior unsecured debt in a hypothetical default scenario in 2022. Even discounting this value by 50% and adding guarantees and suretyships of about HUF 43bn, the bond is still likely fully recovered. The senior unsecured debt category rating is two notches above the issuer rating, reflecting superior recovery prospects.

Our assessment assumes no cross-default clauses in the portfolio companies' debt documentation.

Outlook and rating-change drivers

The Stable Outlook incorporates a broadly unchanged investment portfolio over the next 1-2 years, no material dividend payments to OPUS shareholders, a focus on developing the existing portfolio, no major M&A activity (other than the transaction planned for the energy division), and cost coverage of above 1.0x.

A positive rating action could be warranted by improved concentration risks, especially for dividend income. However, we do not foresee material changes in this regard in the short to medium term.

A downgrade could be triggered by total cost coverage reaching below 1.0x on a sustained basis.

Rating drivers

Positive rating drivers	Negative rating drivers
• Conservative buy-and-build strategy • Strong cost coverage ratio • No dividend payments	• Energy segment strengthened • High dividend concentration • Covid crisis negatively affecting Hunguest Hotels (tourism)

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• Improvement in dividend diversification	• Large debt-funded acquisition • Cost coverage of below 1x on a sustained basis

Financial overview

		Scope estimates		
Scope credit ratios	**2019**	**2020E**	**2021E**	**2022E**
Total cost coverage from recurring income (x)	6.9	3.0	3.2	3.0
Total cost coverage including non-recurring income (x)	8.0	8.0	6.0	3.0
LTV (%)	39	28	42	41
Liquidity (%)	2.1	44	44	33
Cash flows (HUF m)	**2019**	**2020E**	**2021E**	**2022E**
Recurring cash inflows	6,476	8,661	10,660	11,265
Non-recurring cash inflows	1,478	19,286	12.738	0
Balance sheet/ indebtedness (HUF m)	**2019**	**2020E**	**2021E**	**2022E**
Net asset value	164,564	170,690	213,390	238,000
Gross financial debt	32,868	29,507	68,335	68,335
less: available cash	-12,466	-25,802	-23,728	-14,743
Guarantees and suretyships	43,201	44,529	44,529	35,636
Scope-adjusted debt (SaD)	63,604	48,234	89,136	98,123

Business risk profile

Conservative investment approach

OPUS has a long-term, value-oriented, buy-and-build investment strategy with an active entrepreneurial approach under which tight control is exercised over subsidiaries to create growth and value. This is also reflected by the group's targeting of majority positions which allow control. The group also uses its balance sheet resources to finance subsidiaries. We regard buy-and-build strategies to be positive for an investment holding's credit quality.

M&A transactions are usually rare, but there was more activity in the last 12 months than we expected. This still aligns with OPUS' stated philosophy, however, as: i) the separation from Matrai (lignite) and subsequent focus on renewables and services in the energy sector was already flagged; and ii) the other transactions (mainly 4IG, Hotel Alpenblick, and CIG Pannonia) were all in the asset management division and thus were non-core activities.

The large acquisition of Tigáz is structured as an indirect 50% stake by OPUS; the same approach was used for Titasz. The other half of Tigáz is owned by Status Energy Kft, which is controlled by OPUS' main shareholder, Lorinc Meszaros. OPUS now plans to acquire the remaining 50% from MET Holding AG. We believe the acquisition of solar park operator Buzsák from a Greek company and its subsequent sale to MET Holding AG after gaining feed-in tariff licenses needs to be seen in context of the other transactions mentioned.

For the medium term, OPUS aims to generate dividend income from all its subsidiaries. Presently, this is only the case for a few. For example, food processing companies Viresol and KALL Ingredients are expanding capacity and reorienting; thus, they are less able to pay dividends for now and we did not reflect their dividends in the rating.

We believe OPUS' investment approach is more conservative than a timing-sensitive trading approach. It is supported by a lean cost structure (no dividend payments to OPUS shareholders), making cost coverage relatively independent of the overwhelming part of dividends received.

OPUS increasingly provides management services to subsidiaries as an additional income source.

Main portfolio companies by segment

Industrials: 2020 sales estimated at HUF 155bn, +11% vs 2019; EBITDA margin estimated at about 13%; HUF 37bn order backlog

- Meszaros es Meszaros Kft (M+M): 51% owned; general contractor for typically large public procurement construction projects such as for utilities (water, waste management, infrastructure), water and underground, and roads and railways
- R-Kord Kft.: 51% owned; general contractor for large public procurement projects in railway construction
- RM International Zrt.: 51% owned; 50% participation held in consortium to develop high-speed railway between Budapest and Belgrade
- Wamsler SE: 100% owned; a fireplace and stove manufacturer; largest player in central and eastern Europe, with about 7% of the market (about a third in Hungary)

Food processing: 2020 sales estimated at HUF 65bn, +60% vs 2019; EBITDA margin estimated at about 7%

- KALL Ingredients Kft.: 83% owned; acquired in 2018; corn processor with extensive product portfolio including isosugar and liquid sugars; new EUR 160m plant started operations two years ago
- Viresol Kft.: 51% owned; acquired in 2018; wheat processor with extensive product portfolio including starches, industrial alcohol, gluten and raw material for fodder; started operations in early 2019 after significant investment
- Csabataj Zrt: 74% owned; mixed farming (livestock breeding, egg production and crop production)

Energy: 2020 sales estimated at HUF 60bn, +20% vs 2019; EBITDA margin estimated at 31%

- E.ON Tiszantuli Aramhalozati Zrt. (Titasz): 50% indirectly owned from the third quarter of 2021; electricity distribution in eastern Hungary reaching more than 700,000 customers
- Tigáz Zrt.: 50% indirectly owned from 2021; owner and operator of Hungary's largest natural gas distribution network

Tourism: 2020 sales of HUF 13bn, -60%; EBITDA margin slightly negative

- Hunguest Hotels Zrt**:** 100% indirectly owned; a leading hotel operator in Hungary; 25 locations in Hungary, Austria and Montenegro; strong acquisition activity in 2018 led to 62% growth

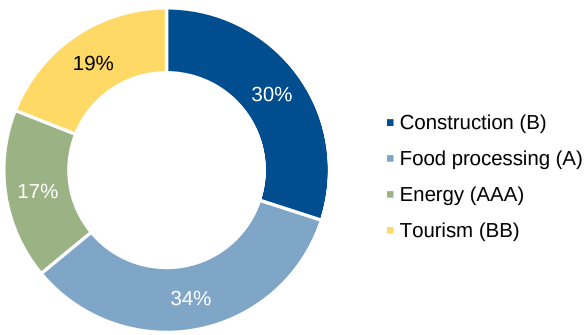
Underlying industries in portfolio have relatively little cyclicality

OPUS' exposure to four distinct, relatively non-cyclical and less correlated sectors continues to support its business risk profile. The majority of the portfolio segments have low or medium cyclicality. OPUS' construction subsidiaries have a large exposure to public projects such as railway infrastructure, telecoms and utility works, which is beneficial in the event of macroeconomic weakness.

In addition, most of the subsidiaries have significant growth potential, either due to a high order backlog (e.g. for M+M) or substantial, recent expansion through capital expenditure (KALL Ingredients and Viresol).

By asset value, the group's largest exposure was formerly to its industrials and food processing segments (more than two-thirds). Recent investments in energy and tourism have led to a more even distribution. Still, the holding company's industrial exposure continues to be a mix of low-rated construction activities and the high-rated food processing and energy segments. We believe that a blended mix of BB is representative of OPUS' current portfolio of participations.

Figure 1: Improved diversification (net asset value)



Source: OPUS

High concentration risk

We do not assess portfolio diversification purely in terms of a group's number of shareholdings. We also evaluate asset quality, underlying industry exposures, geographical exposures, concentration risks embedded in dividend exposure and net asset value.

Portfolio diversification – a very important rating driver for holding companies – has benefitted from heavy investments in various participations over the past two years and from the merger.

Portfolio diversification by value is good, but not yet by income and geography, which are coupled with evolving dynamics at KALL Ingredients and Viresol. The food segment has developed favourably in the last two years after OPUS put two new factories into action. The division now claims to be first in Hungary for wheat starch, isoglucose and fructose. However, Viresol was hit by production delays caused in part by the Covid-19 crisis. Based on these developments, the segment's 2020 revenues are expected to be around HUF 70bn (compared to about HUF 40bn in 2019), having generated an EBITDA margin of about 7% (4.5% in 2019), while the nine-month 2020 margin was already at 10%.

On the other side, dividend income continues to be very highly concentrated, reflecting delays in dividend payments from the food companies and Hunguest Hotels. Thus, portfolio diversification by income is still not supportive for the ratings. By value, it is significantly better: there is sizeable value in the companies that are not paying a dividend at the moment. In addition, we believe that underlying asset values are conservative, also for recovery assumptions (just 50% of asset values used).

Geographic diversification is improving as non-Hungarian sales are expected to rise above 10% in the next few years, from about 7% two years ago.

The majority of OPUS' holdings are unlisted. This may appear negative in terms of the ability to extract divestiture proceeds if needed. However, it also affords independence from market-timing requirements and potential stock price volatility. OPUS is not overly dependent on divestiture proceeds – except for the larger transactions just executed – given its comfortable cost coverage. Compared to last year, however, its flexibility reserve in its asset management arm has been significantly depleted due to the divestments.

Neutral corporate governance

We assess corporate governance as neutral to the ratings. There is no majority individual shareholder, although the Meszaros family has over 30% of the voting rights (directly; including the Konzum PE stake it is above 50%). OPUS' position as one of the largest companies on the Hungarian stock exchange means it must meet transparency and disclosure requirements. We therefore believe that existing structures at the group ensure adequate corporate governance.

Financial risk profile

Credit metrics still solid, but lower due to the impact of the acquisitions

The rating reflects the increased balance sheet debt at the end of 2021, through the existing 2019 bond (HUF 28.6bn) and the envisaged bond (HUF 39bn). These issuances and the sales of subsidiaries have led to strong cash inflow, even after deducting cash used for acquisitions and intercompany loans. This strong liquidity provision serves as a buffer in the short term but will need to be expensed for intercompany loans and the acquisition of Tigáz. The two large acquisitions, Titasz and Tigáz, have been structured to preserve liquidity, enabled by a close joint-venture-like funding of OPUS together with Status Energy. Also supportive in this context is the sale of the Buzsák solar park to MET Holding AG, which will generate a significant windfall.

Holding income rose strongly in 2020, as projected, and is expected to rise again in 2021 due to a significantly higher dividend payout from the construction companies – HUF 9.5bn in 2021, according to management. Management fees are also expected to contribute from 2021 while interest income from the bond passed through to subsidiaries (mainly in the food processing sector) was paused as part of the 2020 moratoriums on debt and interest repayments in response to the Covid crisis. Afterwards, payments will ramp up gradually as Hunguest Hotels is scheduled to accrue interest during its investment phase, while OPUS already paid bond coupons in full in 2020. Assuming the new bond is placed towards the end of 2021, interest payments would increase only slightly in 2021 year-on-year, with the full effect visible only in 2022. We also expect increases for other (discretionary) costs related to M&A and advisory.

Recurring cost cover estimated at 3x in 2021

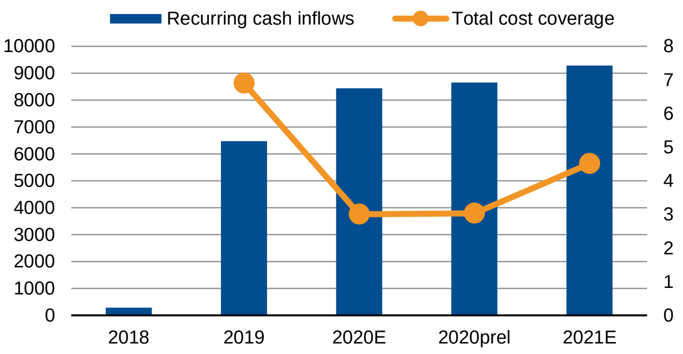
While cost coverage seems to cause no issues, leverage as expressed by LTV (Scope-adjusted debt to portfolio net asset value) is likely to increase above 40% in the current year, reflecting the significantly increased debt. While this does not threaten the ratings, we have maintained the main driver of the financial risk profile as the cost coverage ratio, which is likely to continue be high at about 3x in 2021. The LTV ratio might also be (conservatively) distorted by the use of underlying asset values reflective of historical book values – especially for the industrial and food processing companies – and thus are likely understated.

The cost side continues to be supported by the fact that no dividends are paid to OPUS shareholders currently. OPUS has also decided to apply the debt payment moratorium in Hungary (aimed at minimising cash calls during the current crisis) to its holdings for 2020 and 2021.

Our main base case assumptions for the next two years are the following:

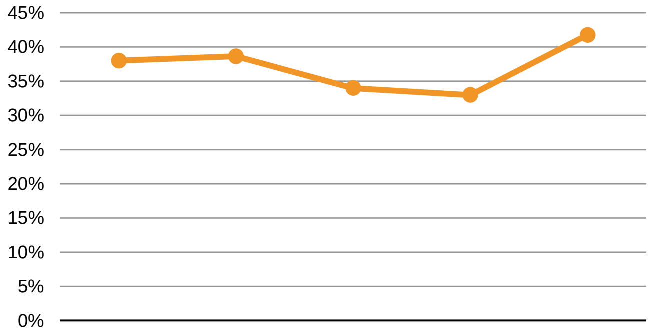
- Increased recurring income in the medium term, mainly based on continued strong contributions from the construction companies
- No dividend income expected from the food and tourism companies until 2023
- No dividend paid until 2023
- Most proceeds from the new HUF 39bn bond to fund acquisitions of Titasz and Tigáz

Figure 2: Solid cost coverage to prevail



Source: Scope estimates

Figure 3: LTV expected to increase



Source: Scope

Projected LTV of about 30%

We forecast that LTV will increase to about 40% in the coming years, reflecting the slightly larger debt in comparison to asset values. We note that the portfolio's asset values generally apply a conservative focus on book values. We also highlight the significant impact on Hunguest Hotels from the Covid crisis.

Neutral financial policy

We believe that financial policy is not relevant to the ratings at present. We view the history of the two founding parties of the merger (OPUS and Konzum) as positive, as both almost exclusively used pure equity funding for the portfolio expansion. In the last 12 months, management deviated somewhat from its stated focus to integrate and realise growth at the core companies. There was also significantly more M&A in 2020 and 2021 than we expected. However, the transactions' financing is favourable for debt-holders as the rating was not negatively affected.

Senior unsecured debt with superior recovery

We have affirmed the BBB- debt rating to senior unsecured debt issued by OPUS Global Nyrt. The debt category rating reflects the ranking of the debt below an insignificant amount of senior secured bank debt and accounts for a significant and growing portfolio net asset value. Senior unsecured debt will be enlarged by the new HUF 39bn bond to be placed in 2021. We expect a 'superior' recovery (70%-90%) for outstanding senior unsecured debt in a hypothetical default scenario in 2022. Even when discounting this value by 50% and adding guarantees and suretyships of about HUF 45bn, a significant amount of bond volume is still likely recovered. The senior unsecured debt rating thus continues to be two notches above the issuer rating, reflecting the superior recovery prospects.

Our assessment assumes no cross-default clauses in the portfolio companies' debt documentation.

Still conservative liquidity profile

OPUS continues to manage liquidity very conservatively. This is due to both its provision of ample balance sheet cash (which, however, is partly linked to the subsidy eligibility for Hunguest Hotels and to own investments to be made at hotels) and its now very low dependence on bank debt (only HUF 700m).

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