

EQUITY NOTE: ZWACK UNICUM

Recommendation: HOLD

Target price (12M): HUF 17,781

6 February 2018

Equity Analyst:
Orsolya Rátkai

Phone:
+36 1 374 7270

Email:
ratkaio@otpbank.hu

Highlights

We revise our rating on Zwack Unicum (Zwack HB; ZWCG.BU) to HOLD from previous BUY recommendation with a new 12M target price of 17,781 HUF/share, 1% higher than the HUF 17,550 closing price on February 6. Total return is estimated at 7% on a 12-month forecast period.

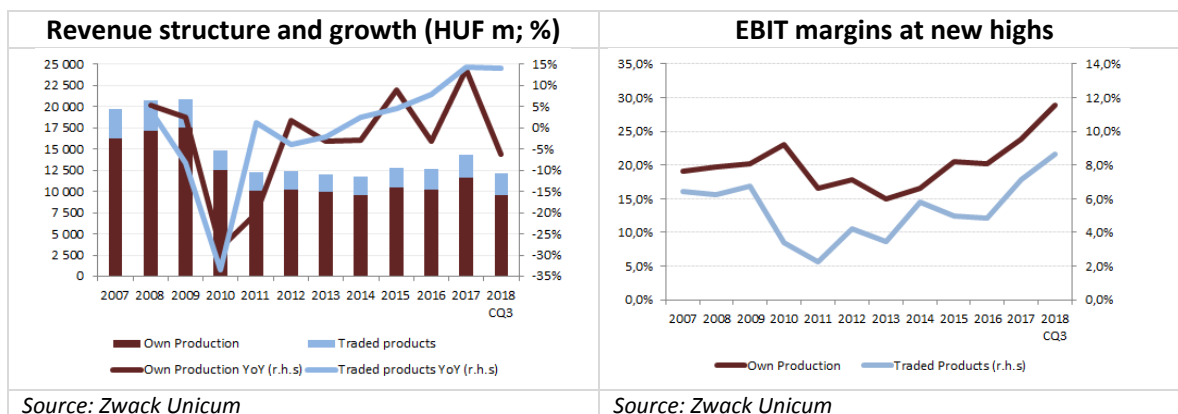
Summary/Earnings Highlights

- As it was expected, net sales revenues declined due to previous stockpiling.
- Q3 EPS increased to HUF 800, a level not seen in the past three years. ROE and ROA also improved
- Recent earnings results are in line with our expectations, we maintain our whole-year net profit forecast of HUF 2.0bn. This is in sync with the Management's recently raised net profit forecast of over HUF 2.0bn, compared to HUF 1.7bn projected earlier.
- As our earnings forecast remained the same, our stock price trajectory also remained unchanged. Although the present interest rate environment is challenging, volatility is undoubtedly present, we are in a wait and see stance regarding the revision of our interest rate forecast. The present change in the stock's target price is due to the progress we have made in time.
- Consumption growth fuels improving sales prospects, however seasonal (calendar) effects add downside risks to the long-term sales forecasts.

Financial highlights of Q3 earnings report

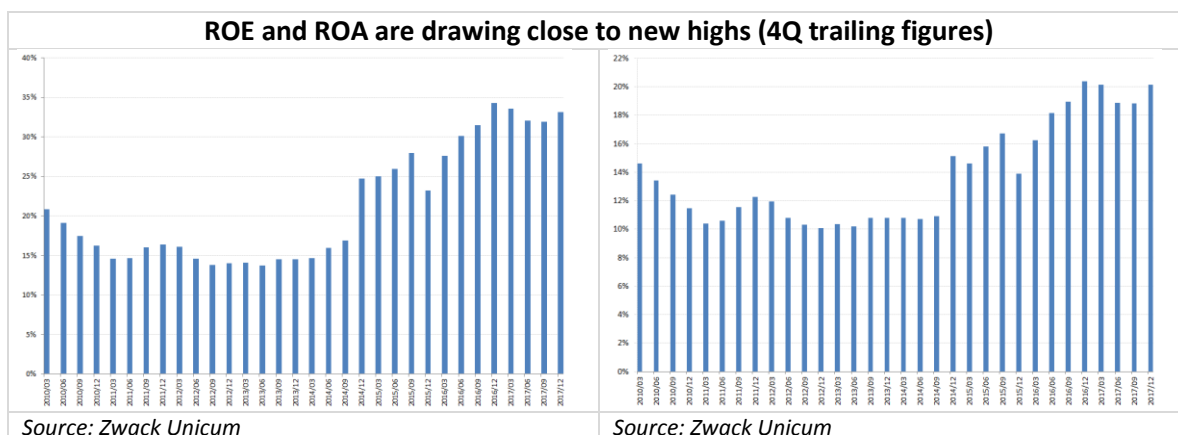
Declining sales with sparkling details. Zwack Unicum reported HUF 5.7bn net sales in Q3, 5% lower than in the same period of the last financial year. High base-period sales due to heavy stockpiling at the end of 2016 resulted in 7% decrease of domestic sales in October-December 2017, though the unexpected growth of Unicum digestive and the successful introduction of high-end digestive 'Unicum Riserva' partly offset the falling vodka sales. Exports increased by 12% YoY in Q3. Although detailed information is not available on this last individual quarter, favourable macro-environment in Germany (cumulative 20% YoY) and particularly in Romania (cumulative 17% YoY) must have had a significant role in growing export sales.

In terms of segmentation, sales of own production fell 9% YoY in Q3 after 7% decline in Q2 as flagship Kalinka sales lost momentum. Sales of Diageo products (with about 40% weight in the sales of the traded portfolio) increased by 18% YoY, while the sale of other distributed products (exclusive of own production) increased by 6%, resulting in a total 11% growth in the sales of off-production segment



Slightly declining margins with counterbalancing effect of corporate tax rate cut. Considering individual quarters, profit margins are close to the level Zwack usually performs in this period of the year. However, in year/year comparison, margin data lag behind the last financial year’s figures. The reason behind the slight deterioration is the decline of own sales with higher profit margin (40% in FYQ3, doubling margins in the previous two financial quarters), while the sales of the traded portfolio bearing tighter margin (11% in FYQ3) rose. Corporate tax cut – effective from January 1, 2017 – benefited the company, and resulted in 29% after-tax profit ratio, the highest in the past ten years. Quarterly net income rose to HUF 1,629 million (6% gain YoY). EPS amounts to HUF 800, while 4Q trailing EPS is nearing previous highs.

Profitability is drawing close to new highs. 4Q rolling ROE and ROA improved compared to the first two quarters of the present financial year. 4Q trailing ROE and ROA improved to 33% and 20% respectively, well above the industry average. In historical comparison, the figures of this latest quarter are the third best in the last seven years beginning from the legalization of home distilleries in 2010.



Economic environment – Supporting macro environment, strong competition in the spirits market. The current macro-environment is still expected to be favourable for Zwack, as the ongoing fast wage growth with low unemployment will result in fast consumption growth and is likely to positively affect demand for its products. Monetary policy is also supportive, as not only euro, but also HUF interest rates could remain low for an extended period, while the National Bank is expected to keep the HUF at current levels, but an appreciation would result in stronger price competition through imported spirits.

Positive outlook with possible calendar effect. The management of Zwack also announced in its earnings release that after-tax profit in Q1-Q3 exceeded the company’s

expectation. In light of the latest results, the management is going to raise its profit target for the FY 2018/2017 to HUF 2.0bn. This matches our earlier expectation. We forecast HUF 2,056m net profit and HUF 1,010 EPS. On a longer run it must be considered that due to calendar effect, the next financial year may result in only modest growth. This year Easter (a very high season of spirit sales) falls to end of March – this means that Zwack's current financial year benefits from two Easter holidays, while its next financial year, which starts in April, will lack this holiday.

Valuation. We raise our 12-month target price to HUF 17,781/share from previous HUF 17,668/share. As this recent earnings release is in line with our expectations, our stock price trajectory also remained unchanged. Although the present interest rate environment is challenging, volatility is undoubtedly present, we are in a wait and see stance regarding the revision of our interest rate forecast. The present change in the stock's target price is due to the progress we have made in time. As a result, and due to price movements in the past weeks, Zwack shares offer lower estimated total return than before. We changed our rating to HOLD from previous BUY recommendation.

Risks surrounding Zwack's economic activity

Regulatory risk: In recent years regulatory changes in the industry made headwinds to the company's profitability. The most notable was the liberalization of spirit distillation at home in small quantities in 2010. However, the company's financial health is outstanding, so if a new regulatory change occurs in the future, Zwack most likely will be able to adjust to it.

Exchange-rate risk: As the company operates in foreign markets as well, and the share of export is increasing among the revenues, exchange-rate risk could be an issue in the future, if not managed properly. Moreover the price of most of its new raw materials is denominated in EUR, so a significant depreciation of the HUF against the EUR could decrease the company's profitability. But in the short run, the fundamentals of the Hungarian economy are strong, so the risk of sharp HUF depreciation is low. Moreover the loss on exchange rates could be somewhat offset by the higher export revenue.

Cost-inflation risk: Due to the improving economic conditions and labour shortages in various industries, real wages started to increase significantly in 2016 and they are expected to do so in the near future. As Zwack's business is labour-intensive (the share of personnel cost is almost 45%), it will be heavily affected by future wage increases which could erode margins.

Company name		
Recommendation		HOLD
12M Target price	HUF	17 781
Estimated Total Return	%	7%
Key market data		
Market cap	(HUF bn)	35,7
Free float		24%
Shares outstanding		2 035 000
Average daily trading volume	(HUFm)	8,3
Shareholder structure		
Domestic institutions		2,15%
Foreign institutions		78,09%
Domestic private investors		12,02%
Foreign private investors		5,99%
Management and employees		0,03%
Convertible preferred stocks		1,72%
Free float		24%
Key financial data		
Book value / share	HUF	2 755
EPS (4Q-rolling)	HUF	1083
Dividend / share	HUF	1050
Dividend yield	%	6,0
Debt to Equity	%	6,0
Net debt / Equity	%	-28,0
Net debt / EBITDA	%	-29,6
ROE (4Q-rolling)	%	18,6
ROA (4Q-rolling)	%	12,8
P/E	%	16,2
P/BV	%	6,4
Price Performance		
52-w range	HUF	16 660-17 910
52-w performance	%	2,33
Relative performance vs BUX	%	-17,5
Relative performance vs BUMIX	%	-106,8
Beta		0,36
Valuation		
DCF		17 781
DDM		17 710
Multiples Analysis		16 518
Analyst		
Name	Orsolya Rátkai	
Mail:	ratkai@otpbank.hu	
Phone:	+36/1 374-7270	

Sources: Bloomberg, OTP Research

Notes:

[The initiation report, which contains the assumptions of the models used, is available here.](#)

[The valuation methodology used in this present equity research note to determine our price targets and recommendations is available here. \(Also available in Hungarian\)](#)

This investment recommendation has not used proprietary models.

The risk warning, which includes the adequate explanations of the length of time of the investment to which the recommendation relates as well as a sensitivity analysis of the assumptions, is indicated in the part of this recommendation where the length of time and the risks of the investment are presented.

Any information relating to the date and time for the price mentioned in this recommendation is revealed in the part of the recommendation where the given price is indicated.

OTP Bank Plc's recommendations and price targets history for Zwack Unicum in the past twelve months:

Date	Recommendations	Target Price	Publication
15/12/2017	BUY	HUF 17,668	Initiation of coverage

[The list of all recommendations made in the past 12 months is available here.](#)

Disclaimer 1

This research/commentary was prepared by the assignment of the Budapest Stock Exchange Ltd. (registered seat: 1054 Budapest, Szabadság tér 7. Platina torony I. ép. IV. emelet; company registration number: 01-10-044764, hereinafter: BSE) under the agreement that was concluded by and between BSE and OTP Bank Plc (registered seat: H-1051 Budapest, Nádor utca 16., Hungary, company registration number: 01-10-041585, hereinafter: OTP Bank or Investment Service Provider).

The BSE shall not be liable for the content of this research/commentary, especially for the accuracy and completeness of the information therein and for the forecasts and conclusions. The Service Provider is entitled to all copyrights regarding this research/commentary however BSE is entitled to use and advertise/disseminate it without amending its content.

This research/commentary shall not be qualified as investment advice specified in Point 9 Section 4 (2) of Act No. CXXXVIII of 2007 on Investment Firms and Commodity Dealers and on the Regulations Governing their Activities. Furthermore, this document shall not be qualified as an offer or call to tenders for the purchase, sale or hold of the financial instrument(s) concerned by the research/commentary.

Disclaimer 2

1. Pursuant to the Commission-delegated regulation 2017/565/EU of the European Parliament, the content of this document shall be considered as an investment research, which recommends or suggests an investment strategy, explicitly or implicitly concerning one or more financial instruments or the issuers of financial instruments, including any opinion as to the present or future value or price of such instruments. The statements in this investment research contain objective or independent explanation. Furthermore, pursuant to Directive 2014/65/EU of the European Parliament and of the Council, this document shall be considered as investment recommendation. This document does not take into account investors' individual interests, circumstances, or objectives; therefore, in the absence of personal recommendation, it shall not be considered as an investment advice.

OTP Bank intends to make this document available to its clients or to the public, or to make it accessible to other persons in a way that allows this document to be disseminated to the public.

2. Information herein reflects the market situation at the time of writing. It provides only momentary information and may change as market conditions and circumstances develop. Additional information may be available on request. Where a figure relates to a period on or before the date of communication, the figure relates to the past and indicates a historic data. Past performance is not a reliable indicator of future results and shall be not treated as such. OTP Bank makes no representation or warranty, express or implied, is made regarding future performance of any financial instrument mentioned in this communication. OTP Bank shall have no liability for the information contained in this for any loss or damage whether direct, indirect, financial, economic, or consequential, whether or not caused by the negligent act or omission of OTP Bank, provided that such limitation of liability shall not apply to any liability which cannot be excluded or limited under the applicable law.
3. The issuer of this report does not claim that the information presented herein is perfectly accurate or complete. However it is based on sources available to the public and widely believed to be reliable. Also the opinions and estimates presented herein reflect a professional subjective judgment at the original date of publication and are therefore subject to change thereafter without notice. Furthermore there can be no guarantees that any market developments will unfold as forecasted. Opinions and estimates constitute our judgment and are subject to change without notice.
4. The issuer(s) of the product(s) mentioned in this document do not hold more than 5% of OTP Bank's registered capital. OTP Bank is a market maker of the financial instrument that is discussed in this document. Neither was OTP Bank a lead-manager (organizer) or joint lead manager (organizer) of any public placement of the issuer's financial instruments (e.g. securities) in the previous 12 months. Regarding investment services defined in Sections A and B of Annex 1 of Directive 2014/65/EU, OTP Bank is not a party of the agreement with the issuer. OTP Bank maintains a conflict of interest policy and it keeps such records, and is has requirements that regulate the transmission of bank secrets and securities secrets, which requirements shall be considered as the effective internal organizational and management solutions as well as information barriers to prevent or manage conflicts of interest. The remuneration of the person(s) participating in preparing the recommendation is not directly related to the transactions carried out as part of the investment services specified in Sections A and B of Annex 1 of Directive 2014/65/EU, or to transactions carried out by them or by other legal entities of the same group or to trading fees that they or another legal person of the same group receive. OTP Bank does not hold net long or short positions that exceed 0.5% threshold of the issuer's total registered capital.
5. OTP Bank has developed appropriate internal procedures for (i) the personal transactions and tradings of financial analysts and other relevant persons, (ii) the physical separation of the financial analysts involved in the production of investment research and other relevant persons; moreover, information barriers have been implemented, (iii) for accepting and managing incentives and remuneration.
6. This communication does not contain a comprehensive analysis of the described issues; it is only for information purposes. No part, chapter, or the entirety of this information shall be considered as investment advice, not even if any part of this document contains a description of a certain financial instrument in terms of its possible price or yield development, and the related investment options. This information shall not be considered as legal, tax or accounting advice.
7. This information reflects the market situation at the time when the document was prepared. You may request more information from OTP Bank. This document was prepared based on publicly accessible information made available to OTP Bank from one or more sources. This document was prepared using data, facts and information from the following essential sources: Bloomberg, Reuters, Hungarian Central Statistical Office, Eurostat, Magyar Nemzeti Bank (Hungary's central bank), and European Central Bank (ECB). Although the information in this document has been prepared in good faith from sources that OTP Bank believes to be reliable, we do not represent or warrant its accuracy or completeness. This document represents the opinion and estimations of analysts at OTP Research, based on publicly available data. You may receive different recommendation from the staff of OTP Bank, in particular if you are provided investment advice based on an investment advice agreement. The content of this document is based on the opinion of OTP Research's analyst at the time when the document was prepared, and they may be subject to change at any time in the future without further notice.

8. Please be informed that, irrespective of the statements of this investment research, OTP Bank is entitled to deal or trade as market maker, acting in good faith and in accordance with the usual way of market-making, with the financial instruments distributed by the issuer(s) specified in this document, as well as to provide other investment activities or ancillary (investment) services, and/or other financial or ancillary financial services to the issuer and other persons.
9. This document shall not be a basis for any further analysis in relation to the financial instruments contained therein. Any reference in this document to the future distribution of a financial instrument shall be construed as indicative, preliminary and informative, and any analysis of such financial instrument is exclusively based on publicly available information listed in the respective prospectus or announcement. The content of this document shall not imply that OTP Bank acts as an agent, a fiduciary, or an advisor to, or on behalf of, any prospective purchaser of the financial instruments discussed herein.
10. For certain persons, access to the products and/or services discussed in this document may not be granted, or it may be limited. The act of preparing this document by OTP Bank, its uploading to the website, its publication may under no circumstances be considered as OTP Bank's intention to make available product and/or service information in the prospectus to persons whom any country or state prohibits from having or obtaining the given product and/or service, including the promotion and the advertisement thereof. This communication and any of the financial instruments and information contained herein are not intended for the use of private investors in the UK and US. OTP Bank is not allowed to provide direct investment services to US investors. Any individual decision or investment made based on this publication is made solely at the risk of the client and OTP Bank shall not be held responsible for the success of the investment decisions or for attaining the Client's target.
11. This publication contains generic presentation of information and knowledge, thus it does not take into account the individual clients' unique and special interests, financial condition, or their ability and willingness to take risks. Therefore please contact our staff or contact your banking consultant for advice before you make an investment decision. The assessment and the consideration of the individual circumstances is provided by the suitability and compliance tests that assess clients' financial knowledge, experience, risk-taking abilities, as well as the examination of the target market.
12. Before making an informed decision to invest and to use the services, please carefully read through all documents, including the documentation, prospectus, regulations, terms and conditions, announcements and key information documents for that product/service, and carefully consider the subject, the risk, the fees and costs of your investment, the possibility of any loss, and seek information about the tax regulations regarding the product and the investment. The prices of financial instruments and securities are changing, outright sales are realized at then current market prices, which may involve losses. The information and opinions in this document do not substitute or take the place of the issuance documentation for the given financial assets (e.g. prospectus, fund management rules), or their brochures or announcements.
13. You assume total responsibility and risk for any specific decision or investment; OTP Bank shall not be held responsible for the effectiveness of investment decisions or for reaching your purpose, nor for the individual investment decision made based on this document or any part thereof, or for their consequences. Investments in financial instruments carry a certain degree of risk, which may affect the effectiveness of the investment decision, and investors may not receive the whole amount they had expected the investment to yield in their investment targets; they may not preserve even the invested amount, therefore the invested capital might even decrease, be wholly lost, or even lead to additional payment obligation.
14. Trading with leveraged products (such as foreign exchange contracts, or shares and indices that have underlying products) carries a considerable amount of risk, and these products are not suitable for all investors. Trading with leveraged products carries the risk of losing all capital, and it may incur losses that exceed the amount invested.
15. **The figures and information described herein refer to the past, and past performance is not a reliable indicator of future yields, changes, or performance.** The changes on money and capital markets, the fluctuation of prices, the development of investments and their yields are influenced by the combined effect of multiple

factors; one important factor of them is the change in investors' expectations. **The development of prices, the future yield of financial assets, indices or indicators, the examination of their changes, trends, and future performance is based on estimations and forecasts, which forecasts do not allow reliable conclusions to be drawn about the future moves of prices, real future yields, changes, or performance.** For each product and service, please assess their tax accounting implications, and other tax consequences, taking into account that they cannot be precisely assessed without knowing the effective tax regulations of the client's individual circumstances; and these legislative provisions as well as the circumstances may change over time.

16. OTP Bank reserves the right to modify this document in the future, without prior notice. The planned frequency of updates to the recommendation is quarterly. The initiation report preceding this research was published on 18 December 2017.
17. OTP Bank (business registration number: 01-10-041-585; registered seat: Nádor utca 16., Budapest H-1051, Hungary; authorised by Magyar Nemzeti Bank (former supervisory authority: Hungarian Financial Supervisory Authority, 'PSZÁF'). Supervisory authority: Magyar Nemzeti Bank (National Bank of Hungary – H-1054 Budapest, Szabadság tér 9); financial customer services: H-1013 Budapest, Krisztina krt. 39. The terms and conditions of this equity research and disclaimer shall be governed by and construed in accordance with Hungarian law.
18. Please note that the Internet is not a secure environment and OTP Bank does not accept any liability for any loss caused by the result of using this report in a form altered or delayed by the wilful or accidental interception, corruption or virus infection.
19. OTP Bank, in compliance with the applicable law, assumes no responsibility, obligation, warranty or guarantee whatsoever for any direct or indirect damage (including losses arising from investments), or for the costs or expenses, detrimental legal consequences or other sanctions (including punitive and consequential damage) sustained by any natural or legal person as a result of the purchase or sale of financial instruments or engaging investment services described herein, even if OTP Bank was warned of the possibility of such occurrences.
20. If you received this document from OTP Bank Plc, then it was sent to you with your previous consent. You may withdraw this permission by sending an e-mail to research@otpbank.hu or writing a letter addressed to 'Research Center', Hungary H-1051, Budapest, Nádor utca 21. Please refer to your name and e-mail address in both cases.

This document was prepared by:
Orsolya Rátkai
Senior Equity Analyst
OTP Research

This document was finalized at **8:47:32 PM** on 06 February 2018