26th of October, 2023

Opus Global Valuation Update

Company Data	
Recommendation	**hold**
Target price*	**423**
Closing price	HUF 389
52-week range	HUF 101 - HUF 437.5
Market cap (HUF, mn)	276,449
Annual avg. daily turnover (number of shares)	1,026,531
Bloomberg code	OPUS HB

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Valuation Update

After the H1 results, we have put our target price (then HUF 232 per share) and recommendation for Opus Global under review, as we intended to update our valuation model.

There are two changes in valuation that affect all segments. We adjusted the cost of capital to reflect a moderation of the rate environment that took place since our last model update in November, 2022. We also adjusted our expectations of the financial performance of the segments upwards, in light of the strong performance in the first half of 2023. Segment-specific details are outlined in the corresponding parts of this research report.

The stock performance has been remarkable since May this year. Besides stellar earnings results posted for the first quarter and the first half of this year, this increase was likely fuelled by the stock repurchase program to a great extent as well (details of which was released on 21 July this year by the company). After the buyback program reached the announced limit amount of HUF 1 billion on 17 October, Opus announced a buyback auction to be held on 29 February next year, at which the company intends to buy up to HUF 2 billion of own shares. The purchase price shall not be above 30 percent of the previous day's closing price, and shall not exceed HUF 489 per share, the book value of equity capital per share as reported for end-2022 by the company.

We believe that these announcements sent a strong signal towards market participants about the management's expectations for future performance of Opus Global. A considerable increase in traded volume of Opus Global stock also took place as the price went up considerably, well exceeding the amount only attributable to the company's own purchases.

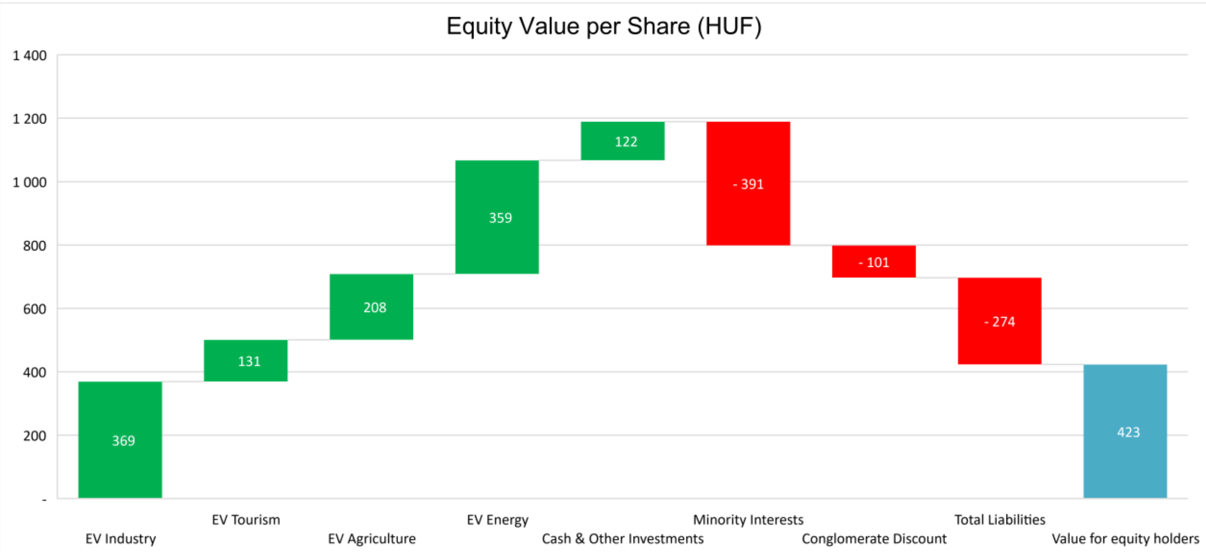
Our new expectations for the financial performance of the conglomerate and the segments are presented in the table below. Given that we perceive improved clarity in the outlook as major acquisitions have not been carried out lately, we abandoned the approach of weighted scenarios for the segments. On conglomerate level we adjust for minority interests, while on segment level we do not.

*The target price was based on the fundamental analysis of the company and it is not guaranteed that the price of the share will reach the given target price.

	Segments	2023	2024	2025	2026	2027	2028
Revenue	Conglomerate	461 757 985	446 117 073	424 757 091	412 609 489	449 793 448	476 442 535
Revenue	Industry	401 810 448	300 474 731	241 385 572	205 377 318	234 114 725	252 484 175
Revenue	Turism	39 812 907	50 939 327	59 837 932	62 764 997	65 837 118	69 061 522
Revenue	Agriculture	119 671 746	113 162 778	122 850 752	133 142 212	144 068 371	155 661 882
Revenue	Energy	232 032 387	291 519 093	275 931 807	266 251 642	287 920 348	297 756 741
operating expenses	Conglomerate	440 360 535	427 449 222	397 749 801	382 170 438	408 471 123	430 711 653
operating expenses	Industry	357 452 146	274 358 919	220 308 375	189 594 775	214 823 919	231 506 707
operating expenses	Turism	37 605 256	46 302 931	50 800 751	52 045 167	53 630 959	54 888 120
operating expenses	Agriculture	104 807 706	94 971 950	99 060 665	106 474 741	114 966 315	124 232 153
operating expenses	Energy	238 889 086	294 977 360	274 183 870	259 269 855	268 691 911	278 151 675
FCFF	Conglomerate	18 081 761	17 908 960	30 998 750	34 160 815	44 362 932	48 585 800
FCFF	Industry	39 418 049	23 100 333	18 631 408	13 903 799	17 027 167	18 522 325
FCFF	Turism	1 758 069	3 831 067	7 609 501	9 058 056	10 336 711	12 030 927
FCFF	Agriculture	2 912 390	4 467 983	16 911 175	19 416 589	21 516 360	23 516 083
FCFF	Energy	- 16 184 806	- 4 660 327	114 969	5 072 930	16 212 784	16 550 902

Source: Equilor

As for valuation of the total Opus Global group, the individual valuation of the segments and free cash, which are lowered by minority interest, total liabilities, and a 15 percent conglomerate discount, are shown in the table below. The cash amount is based on end-2022 figures as reported by the company, given that the DCF valuation is based on full-year values for 2023. Minority interests were calculated according to the most recent available knowledge.



Source: Equilor

Based on our updated model, our new 12-month target price is HUF 423 per share. As the close price of Opus Global stock on the date of this research report was HUF 389 per share, this target price yields a hold recommendation for the stock.

Segment details and risks are summarized as follows.

Industry Segment

The performance of the industry segment in 2023 H1 significantly outperformed the 2022 H1 period. 93% of the H1 revenue was generated by the construction segment, which includes Mészáros és Mészáros Zrt, RM International Kft., and R-Kord Kft. The performance of the construction segment is highly dependent on government contracts and the status of the EU funds.

Revenues of Mészáros & Mészáros are modeled based on active contract numbers, assuming an average revenue per contract. For 2024 and 2025 we modeled stagnating and decreasing contract numbers, while for later periods we expected 5 contracts increase per year. In R-Kord we expected decrease in revenues in FY2024, and then we expect slight increase in the later periods. For RM International we assumed that the only project of RM international is the Budapest-Belgrade railway line, which will be finished by the end of FY2025 based on the projections of Opus Global. We assumed that personnel expenses grow at the projected annual inflation rate. In the planning period we assumed that capital expenses will be slightly above depreciation replacement level.

To reflect changes in the capital markets, we updated the cost of capital calculation as well. Return on equity was modeled using CAPM, the cost of capital was calculated using WACC. We used input information from Aswath Damodaran and Government Debt Management Agency.

Tourism Segment

The tourism segment posted a remarkably strong performance in the first half of 2023, surpassing the domestic tourism sector growth, driven by above industry occupancy rates. HUNGUEST Hotels Zrt. is the flagship of this division, mainly driving the majority of growth in the segment. The total room capacity increased by 92 rooms in the second quarter, due to the opening of Hotel Aquarell. In the first half of 2023 approximately 20% of the total rooms were out of commission due to renovations, Hunguest Hotels will operate at full capacity by the end of 2024.

We modeled revenues based on revenue per available room (RevPAR), where RevPAR is expected to grow at a higher pace in FY2023, based on 2023 H1 performance. Then we expect RevPAR to normalize over the planning period, slightly above the annual inflation rate. Thus, revenue increase was mainly driven by two factors: increase in the number of rooms available, and increase in RevPAR. Material expenses were modeled using material expenses per available room, expenses are assumed grow at the projected annual inflation rate. Personnel expenses are assumed to grow at the projected annual inflation rate. Depreciation and amortization was modeled based on depreciation and amortization per available room. We assumed, that capital expenses will be slightly higher, than the depreciation and amortization.

To reflect changes in the capital markets, we updated the cost of capital calculation as well. Return on equity was modeled using CAPM, the cost of capital was calculated using WACC. We used input information from Aswath Damodaran and Government Debt Management Agency.

Agriculture Segment

The agriculture segment also showed an improvement in the first half compared to the same period last year. A positive sign is that, at the operating level, both KALL Ingredients (maize processor) and VIRESOL (wheat processor) made a profit. Especially notable is the improvement on the side of KALL Ingredients, where operating performance improved from a loss of HUF 1.99 billion in the first half of 2022 to an EBIT of HUF 1.02 billion in 2023. VIRESOL was able to further increase its already positive operating profit, with EBIT increasing from HUF 1.11 billion in the first half of 2022 to HUF 5.37 billion in 2023.

Revenue outlook in the agriculture segment is based on available market proxies for alcohol-, liquid sugar- and gluten-related product prices, with a long-term growth rate of 3 percent for these products. Input feedstock prices are also modeled in a similar fashion and with the same long-run growth rate. As for energy costs, we assumed some efficiency improvement based on recent announcements. KALL ingredients was granted a non-repayable aid to carry out energy efficiency-enhancing investments as part of the so-called Factory Saving Program ("Gyármentő Program") by the government. Also, the company entered into an agreement with Norway-based Kyoto Group to ship a so-called 'Heatcube', that is planned to replace the current natural gas supply used in KALL's production process.

Depreciation and amortization was modeled based on a fixed depreciation and amortization rate. Personnel expenses are assumed to grow at the projected annual inflation rate. We assumed, that capital expenses will be slightly higher, than the depreciation and amortization.

Energy Segment

The energy segment operates in a highly regulated segment, where the prices (use of system charges) are set by the Hungarian Energy and Public Utility Regulatory Authority on an annual basis, reflecting the expenses of the previous fiscal year. Due to this neither the energy distribution nor the gas distribution segments have any pricing power. On the other hand, expenses of the energy segment are mainly driven by market forces, such as cost of energy, and cost of natural gas for replacing network losses. Therefore, a lag can be observed in revenues, which can cause significant temporal losses and profit, which normalizes over time. Due to this, and the volatile energy market in 2022, the energy distribution segment suffered significant losses in the first half of 2023. The natural gas distribution segment was profitable in the same period, due to revised use of system charges.

In our model for the energy segment we expected, that in the long-term fluctuations in costs and revenues balance each other out, and revenues and costs per kWh and m3 of natural gas distributed normalize on spreads that could be observed earlier.

The energy distribution segment delivers energy in Eastern Hungary, in Hajdú-Bihar, Jász-Nagykun-Szolnok and Szabolcs-Szatmár-Bereg counties. Currently there are significant developments in this region, namely the CATL and BMW factory in Debrecen, which based on press information will significantly increase the distributed energy in the future. Therefore, our model shows significant increases both in revenue and expenses compared to FY2022. We expected significant decrease in the natural gas distributed in FY2023, but projected slight increase in line with projected GDP growth. Personnel expenses are assumed to grow at the projected annual inflation rate. Depreciation and amortization was modeled based on a fixed depreciation and amortization rate. We assumed, that capital expenses will be slightly higher, than the depreciation and amortization.

To reflect changes in the capital markets, we updated the cost of capital calculation as well. Return on equity was modeled using CAPM, the cost of capital was calculated using WACC. We used input information from Aswath Damodaran and Government Debt Management Agency.

Risks to our valuation outcome

There are several risks that could affect our valuation outcome. As the company's flagship industrial segment is heavily relying on public procurement, any change in this regard could affect revenue prospects, and therefore profitability, substantially. Downside risks could arise from a possible scenario where the government lowers its procurement activity due to budget constraints, or a lack of EU fund inflow.

The energy segment is operating in a heavily regulated environment, therefore this segment's performance is highly sensitive to changes in regulation. A possible scenario could be a freezing of use of system charges without compensation to the companies, or other similar changes. While the moderation of energy prices since last year decreased this risk, it cannot be ruled out fully that such scenario materializes in the future.

Commodity price volatility could also be a risk that may affect multiple segments. As for energy prices, a considerable increase would add to the costs borne by the tourism sector and the food sector, and could increase the price of energy purchased to cover network loss in the energy segment as well. While the latter should normally be compensated in subsequent price setting periods by regulators, unfavorable price developments may affect the energy segment's profitability negatively. As for commodities affecting the food segment, an unfavorable change in the relative price of products manufactured (edible and medical alcohols, starch, gluten and isosugars) compared to feedstock prices (wheat and maize) could affect profitability in this segment in a negative way.

An unforeseeable change in macroeconomic conditions also represent risk. A less favorable real GDP growth domestically could negatively affect demand especially in the tourism segment, while lower external demand for the food segment's products is also a risk. Higher than expected inflation could push costs up, while unfavorable currency movements could affect export revenue (in the tourism and food segments) or cause a negative revaluation impact due to the difference in the currency of bookkeeping and the currency denomination of loans.

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The report was closed on the 26th of October, 2023.

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