MASTERPLAST – MODEL UPDATE, INVESTOR FORUM 2019

DCF VALUATION

We increased our 12-month target price to HUF 910 from HUF 874 and maintained the Buy recommendation for Masterplast.

We used the following parameters and methodology during our DCF calculations:

- Based on our assumptions sales will grow in the next years due to tighter environmental and energy standards, dynamically growing export segments activity, whereby the expanding „CSOK" also boosts the renovation of family houses.
- The discount rate we used to get the present value of future cash flows is 6.96%, however, we assumed a slightly higher rate (7.26%) for the terminal. As a result of the successful bond issue, the discount rate decreased by 0.06%-point. We presumed that capital structure will remain stable in the future.
- Equity risk premium is assumed at 6% in the detailed period and in perpetuity.

The following factors support the higher than expected revenue increase:

- **Due to tighter environmental and energy standards, insulation aspects are changed**, and their continuous integration into the regulatory environment will result in a permanent market expansion. The applied thermal insulation thickness in Hungary is close to 10 centimetres, which was only 5-6 cm 5 years ago. Meanwhile, the Western European average is 15 cm; hence, the market is expected to move in this direction.

- **In the next 2-3 years, one of the most dynamically growing segments can be the export activity**, which means typically Western and South European exports. The largest export market is Italy, but the German and the UK presence have been growing steadily. A typical trend here is the shortening of supply chains, meaning that manufacturers sell products directly to the end user or retailer.

With the further increasing production output of the Company the own production segment has become more efficient and profitable. EBITDA and net profit margins are expected to continue to improve.

- **The Company also announced a new investment to strengthen its position in the manufacture of diffusion roofing foil.** This will be an investment of EUR 1.3 million; by purchasing German technology to start the own production of a strategic product. Production is expected to start in the second quarter of 2020.

- **Self-manufactured products ensure profitable growth at Masterplast and the target is to increase their share of sales to 50 % by 2020** (from the current 41 %). The Company's long-term goal is to have its own manufacturing in all strategic product lines, to further strengthen its market position and to have a 65% share of self-manufactured products by 2030.

- This year, profitability continued to improve at the Company. The proportion of self-manufactured products is constantly increasing; as a result, profit margins show continuous improvement. In the last quarters, operating profit was able to expand more than sales growth. Due to improved margins, EBITDA share and net profit share (compared to sales) may expand significantly over the next few years.

DCF Model (EURmn)	2018	2019	2020	2021	2022	TV
Sales	97339	106630	112823	116916	118874	119691
Sales growth	*8,61%*	*9,55%*	*5,81%*	*3,63%*	*1,67%*	*0,69%*
EBIT	8 310	9 889	10 974	11 654	11 923	11 970
EBIT margin	*8,54%*	*9,27%*	*9,73%*	*9,97%*	*10,03%*	*10,00%*
Tax rate	*7,0%*	*7,0%*	*7,0%*	*7,0%*	*7,0%*	*7,0%*
Taxes on EBIT	*-581,73*	*-692,21*	*-768,18*	*-815,79*	*-834,58*	*-837,91*
NOPLAT	**7 729**	**9 197**	**10 206**	**10 838**	**11 088**	**11 132**
Free Cash flow to the Firm	**165**	**1452**	**3361**	**4408**	**5143**	**5954**
WACC	**6,96%**	**6,96%**	**6,96%**	**6,96%**	**6,96%**	**7,26%**
Discount factor	0,93	0,87	0,82	0,76	0,71	0,67
Discounted free cash flow	154	1269	2746	3368	3674	59423
Enterprise value	70634					
Net debt	29135					
Equity value	41499					
Number of shares outstanding (mn)	14601					
Cost of equity	9,59%					
Fair value per share (EUR, HUF)	**2,57**	**824**				
12M target price (EUR, HUF)	**2,84**	**910**				

Source: Masterplast, MKB

INVESTOR FORUM 2019

Masterplast held an investor forum on 9th December 2019, where the management of the Company presented the update of the strategy. The three most important pillars of the strategy are the following: **growth in sales, increased production output, improving profitability.**

The Company raised its net profit expectations for this year due to the favourable foreign exchange environment and expects further improving profitability in the coming years, partly due to the positive effects of the T-Cell acquisition and partly due to the bond issue.

The Company projected increasing dividend payments for the next few years. Dividend policy conditions: dividend payment up to max. 50% of the net income, depending on the changes of the industrial environment and of future investments (2017 was the first year when the Company decided to pay dividend.)

According to the management revenues may increase dynamically in the coming years:

	Sales (mln EUR)	EBITDA (mln EUR)	EBITDA (%)	Net income (mln EUR)	Max. dividend (%)
2019 forecast	~ 107	~ 7.3	~ 6.8%	~ 4.8	50%
2020 forecast	~ 117	~ 8.4	~ 7.2%	~ 5.5	50%
2021 forecast	~ 125	~ 9.5	~ 7.6%	~ 6.5	50%
2022 forecast	~ 132	~ 10.6	~ 8.0%	~ 7.5	50%

Source: Masterplast, MKB

However, the after-tax profit may be higher than expected due to the favourable foreign exchange environment: it may reach EUR 4.8 million instead of EUR 4 million. The Company currently expects a net profit of EUR 5.5 million by 2020, EUR 5.5 million by 2021 and EUR 7.5 million by 2022.

BUX INDEX: SHORT TERM GOAL

Management expressed its intention to get included in the BUX index basket, but the free-float based market capitalization should be considerably higher to meet the BUX criterion. The Company is currently looking for acquisition opportunities, and to finance the transaction second public offering (SPO) can be expected in the future, which may also satisfy the BUX criterion

INVESTMENTS

Recently, Masterplast has been actively investing in three new production sites. One is the fiberglass factory, with a EUR 16 million investments; Masterplast is the second largest European and third largest global fiberglass manufacturer. The EPS plant has also been supported by an acquisition (T-Cell), the exploitation of synergies has begun and 2020 will be the year when synergies can be better exploited. The segment will be one of the flagships of manufacturing growth.

DECENTRALIZED BUSINESS MODEL

The goal is to maintain a decentralized business model. Masterplast has 8 subsidiaries and successful in those countries where the subsidiaries are able to operate independently as the market and regulatory environment are different.

The management has set the following goals for production:

- **Efficiency**: Higher output, further improving quality, enhancing profitability
- **Innovation**: Upgrading existing product portfolio, tailor-made products on specified demand
- **Development**: Launch new manufacturing processes, strengthening existing portfolio, comprehensive automation.

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Prior researches

MKB Bank wrote an initiation report on 15 December 2017. The research is available on the web page of the BSE (Budapest Stock Exchange):

https://www.bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/MKB-Bank-Masterplast-initation-report-20171215.pdf

The flash notes are available on the web page of the BSE (Budapest Stock Exchange):

https://www.bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/MKB_Bank_Zrt._-_Masterplast_elemzoi_kommentar_-_2018.01.10..pdf1

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Methodology used for equity valuation and recommendation of covered companies

The discounted cash flow valuation is a method of valuing a company (or project, assets, business, etc.) with the time value of the money. The model forecasts the company's free cash flow (free cash flow to firm) and discounts it with the average cost of capital (WACC). The cash flow is simply the cash that is generated by a business and which can be distributed to investors. The free cash flow represents economic value, while accounting metric like net earning doesn't. The WACC represents the required rate of return by the investors. If a business is risky the required rate of return, the WACC will be higher.

Discounted cash flow model (DCF): We analyze the companies using five year forecast period and set a terminal value based on the entity's long term growth or on different exit multiples like EV/EBITDA or EV/EBIT. In certain cases the forecast period may differ from five years. In this case the analysts must define the reason for difference. The cash flows are discounted by the company's WACC unless otherwise specified.

In the first step we have to forecast the company's cash flow. The free cash flow to firm (FCFF) is based on the earnings before interest and taxes (EBIT), the tax rate, depreciation and amortization (D&A), net change in working capital (which is based on the current assets and current liabilities) and the capital expenditures (CAPEX). The model requires a terminal value which can be based on the long term growth or on an exit multiple like EV/EBITDA, or EV/EBIT. Forecasting the terminal value is a crucial point because in most cases it makes up more than 50% of the net present value.

The discount rate (WACC): The average cost of capital of the company is dependent on the industry, the risk free rate, tax, the cost of debt and the equity risk premium. The cost of equity is calculated by the CAPM model, where the independent variables are the risk free rate, the industry specific levered beta, and the equity risk premium. The WACC is dependent on the capital structure, so the forecast of the equity/debt mix is crucial.

At the end we get the enterprise value (EV). The EV is the market capitalization plus the total debt and preferred equity and minority interest, minus the company's cash. In the last step we have to reduce the EV with the net debt. This figures divided by the shares outstanding we arrive at the target share price.

The discounted cash flow model includes sensitivity analysis which takes the effects of the change in the WACC, the long term growth or the used exit multiples on which the terminal value is based.

Our target price is based on a 12 month basis, ex-dividend unless stated otherwise.

Peer group valuation: For comparison we use peer group valuation. The analysis based on important indicators and multiples like P/E, EV/EBITDA, EV/EBIT, market capitalization, P/S, EBITDA margin, net debt to

EBITDA, EBITDA growth, dividend yield and ROIC. If the industry justifies we may use other multiples. The peer group is compiled according to the companies' main business, with respect to the region (DM or EM market).

Recommendations

- Overweight: A rating of overweight means the stock's return is expected to be above the average return of the overall industry, or the index benchmark over the next 12 months.
- Underweight: A rating of underweight means the stock's return is expected to be below the average return of the overall industry, or the index benchmark over the next 12 months.
- Equal-weight: A rating of equal-weight means the stock's return is expected to be in line with the average return of the overall industry, or the index benchmark over the next 12 months.
- Buy: total return is expected to exceed 10% in the next 12 months.
- Neutral: Total return is expected to be in the range of -10 - +10% In the next 12 months.
- Sell: Total return is expected to be below -10% in the next 12 months.
- Under revision: If new information comes to light, which is expected to change the valuation significantly.

Change from the prior research

Our first research was published on 15 December 2017. In that Initial Coverage our price target was HUF 874, but the changes in fundamental factors justified the update of our model. Our new price target is HUF 910.