

EQUITY NOTE: RÁBA Automotive Holding

Recommendation: SELL (unchanged)

Target price (12M): HUF 1,115 (unchanged)

21 November 2022

Highlights

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We maintain our SELL recommendation and 12M target price on Rába Automotive Holding (RABA HB; RABA.BU) at 1,115 HUF / share. The company had strong revenue growth in Q3 as well, however, energy and labour costs have reached unprecedented levels, which has put record pressure on profitability. There was also a large exchange rate loss, which is largely responsible for the weak Q3 bottom line. Additionally, the economic outlook keeps deteriorating given rising interest rates and slowing GDP growth, which could potentially result in lower demand for Rába's products. It is worth mentioning that Rekard now operates as a wholly owned subsidiary following the acquisition of the remaining 75.1% stake on July 1. The practical implementation of the Rába Modernisation Programme 2025 has started as well, which could have longer-term positive impact on operations, likely from late 2024.

In terms of revenues the company had a very strong Q3, group sales increased to HUF 15.84bn (+66.4% YoY), domestic numbers rose to HUF 4.21bn (+41.4% YoY) and export reached HUF 11.63bn (+77.7% YoY). Export activities were strong in the EU and USA, but revenues for the 'other markets' segment were up as well. In compliance with sanctions in force against Russia, Rába had no commercial activities with Russian partners in Q2-Q3.

The uncertainties caused by the Russia-Ukraine situation and the impact of sanctions raised inflationary pressures to unprecedented levels, the long-term outlook is still uncertain. The company faced extremely high energy prices in Q3, while steel prices still exceeded the level of the base period considerably. As a result, direct cost of sales rose by 61.9% in Q3 on a YoY basis to HUF 13.32bn, while G&A expenses grew by 41.6% YoY to HUF 2.17bn. Overall, the company had an operating profit of HUF 335 million and a net loss of HUF 563 million primarily due to the above-mentioned exchange rate loss.

The broader economic outlook keeps deteriorating, the EC's latest economic forecast now projects only a 0.3% real GDP growth in 2023 in the EU, while inflation is projected to remain elevated at 7% next year.

Financial highlights of Q3 2022 earnings report

HUFm	2022 Q3	2021 Q3	YoY Change
Domestic sales	4 212	2 978	41%
Export sales	11 627	6 542	78%
Net sales income	15 839	9 520	66%
Direct cost of sales	13 320	8 225	62%
Gross profit	2 519	1 295	95%
Cost of sales and marketing	127	100	27%
General managing costs	2 175	1 536	42%
Other operating expenses	67	133	-50%
Total operating expenditures	2 369	1 769	34%
Other incomes	184	95	93%
EBIT	335	-379	-
Net financial profit	-787	-215	-
Pre-tax profit	-452	-619	-
Tax	111	47	136%
After-tax profit	-563	-665	-

	2022 Q3	2021 Q3	YoY Change
EPS (HUF)	-42	-50	-
4Q-rolling EPS (HUF)	-52	164	-
EBITDA (HUFm)	1 005	215	368%
Gross profit rate	15.9%	13.6%	2.3pp
EBIT rate	2.1%	-3.9%	6pp
EBITDA rate	6.3%	2.3%	4pp
ROE	-2.7%	-3.1%	0.4pp
ROA	-0.1%	-0.1%	0pp

Source: Rába Automotive

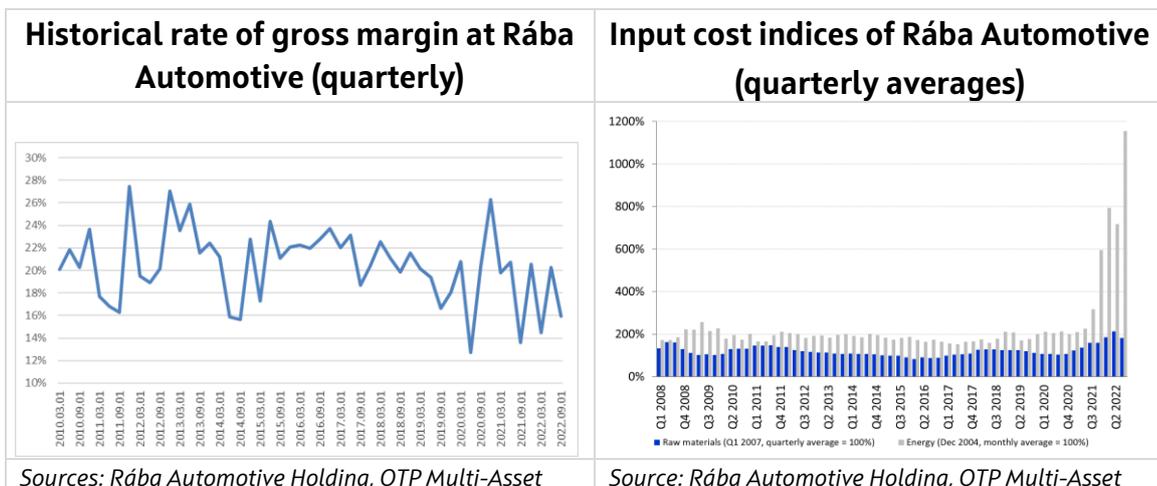
Strong export growth in EU and USA, further support coming from Rekard

Rába Automotive's net sales revenue increased to HUF 15.84bn (+66.4% YoY) in Q3 2022, with domestic sales rising to HUF 4.21bn (+41.4% YoY) and export revenues rising to HUF 11.63bn (+77.7% YoY). Overall, in Q1-Q3 2022 net sales revenue was up by 38% to HUF 45.8bn. The group level sales figures, however, include revenues from Rekard the first time (~HUF 1bn), where Rába acquired an additional 75.1% stake on July 1 and now operates as a wholly owned subsidiary. The company mentioned that due to the Russia-Ukraine situation the European passenger vehicle market was characterised by a strong decline in volumes, but this has not been felt so far in Q1-Q3 in the European commercial vehicle and the global agricultural vehicle segments.

Export revenues to the USA jumped by 70.2% to HUF 1,244 million in Q3 2022 on a YoY basis. There was very strong revenue growth in the EU markets as well, exports were up by 88.6% in HUF-terms (~9.7bn) YoY including Rekard figures as well (~74% growth YoY w/o Rekard). The CIS geographical segment did not perform well, but revenues for the 'other markets' segments were up by 42% YoY. These markets, however, represent a relatively smaller portion of the overall revenues (~4% in Q3 2022). The company stated as well that in compliance with sanctions in force against Russia, Rába had no commercial activities with Russian partners in Q2-Q3 2022.

In terms of business units, the export performance was driven by 'Axles' in Q3 as USA sales jumped by 70.2% to HUF 1.24bn and EU sales were up by 95.8% to HUF 7bn YoY, while 'other markets' revenue was also up by 41.6% to HUF 722 million. The 'Automotive Components' segment performed good as well, EU sales grew by 10.5% YoY to HUF 1.73bn, while the 'Vehicles' segments delivered HUF 211 million

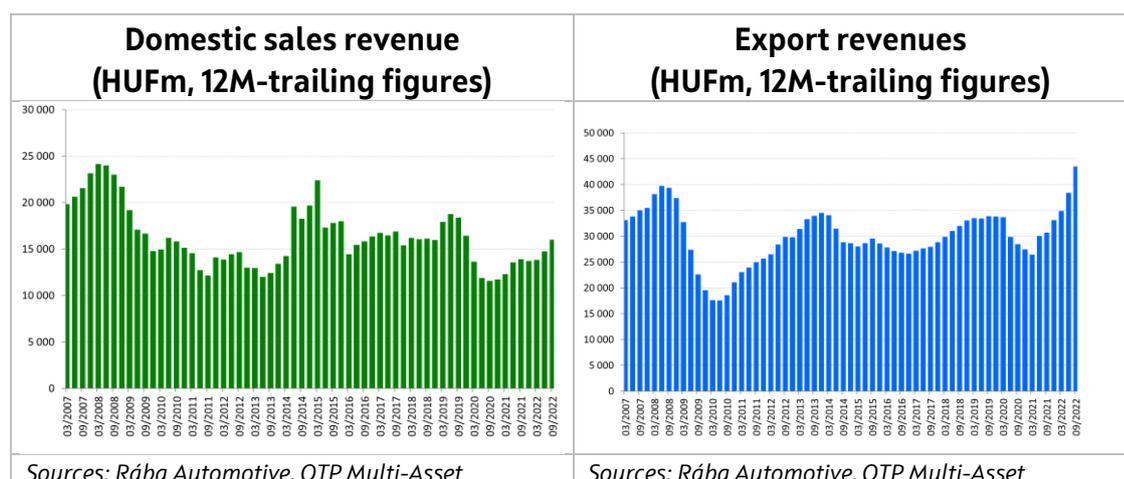
export revenues during Q3 2022 (none in base period). The new Rekard business segment contributed HUF 753 million to EU exports.



As a result of continued strong export revenue growth on a Group level, the export's share in total sales volume increased to 73.4% in Q3 2022, the same ratio was 68.7% in Q3 2021.

Significant growth in domestic sales contributed to Group results as well

Domestic sales performance was very strong in Q3 as well, revenues jumped by 41.4% YoY to HUF 4.21bn. The 'Axles' unit was able to expand in the domestic market by 43.6% YoY to HUF 1.58bn. The 'Automotive Components' segment performed good as well, domestic sales were up by 17.3% YoY to HUF 3.5bn. At the same time, the 'Vehicles' segment was down by 16.4% YoY to HUF 239 million.



Elevated purchase prices, increasing expenses and significant uncertainty

The company notes that in Q3 2022 the price of energy and labour costs have reached unprecedented levels, which has put record pressure on the profitability of operation. At the same time, steel purchase prices after a minor decline still

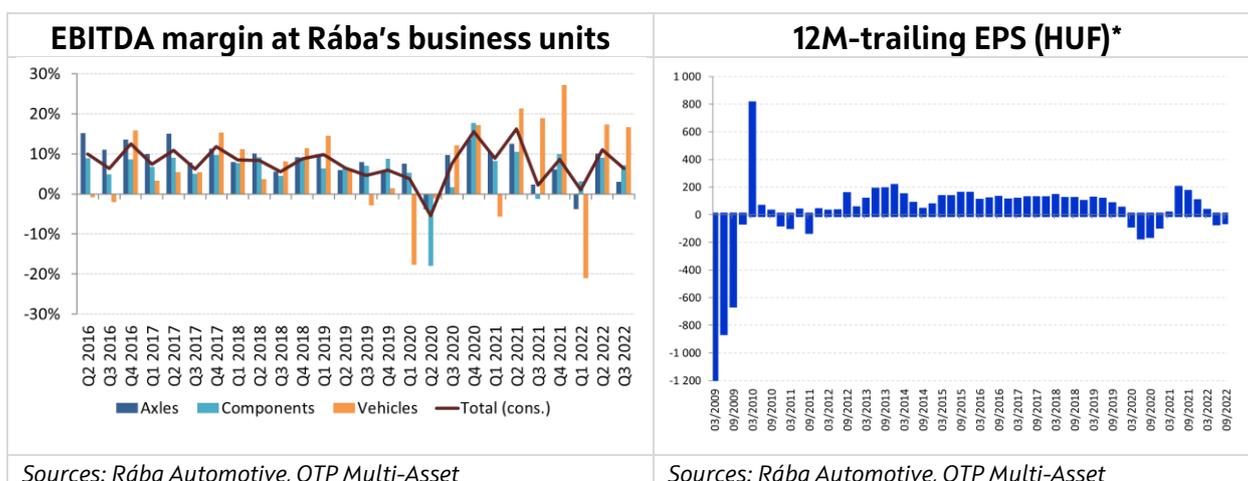
exceeded the level of the base period considerably. It is worth noting, that European natural gas prices have somewhat moderated recently, but they are still elevated (above 100 EUR / MWh). Electricity prices are also still high, while oil is around USD 90 / barrel (Brent). The company mentions that their contracting terms made it difficult to fix energy purchase prices, so they primarily manage the effects of the energy crisis by increasing integrity and making sales prices more flexible.

The direct cost of sales rose by 61.9% in Q3 on a YoY basis to HUF 13.32bn, while G&A expenses grew by 41.6% YoY to HUF 2.17bn. Overall, in Q1-Q3, direct cost of sales jumped by 40.1%, while G&A expenses are up by 31.3%, which compares to a 38% increase in sales revenues.

Significant cost pressures and FX losses negatively impacted the bottom line

Quarterly gross profit rose by 94.6% YoY in the July-September period, to HUF 2.52bn, while EBIT was HUF 335 million (vs. minus HUF 378 million a year ago). Gross profit rate was 15.9% in Q3 and 2.3pp higher YoY given strong revenue growth. The EBITDA rate was 6.3% (HUF 1bn), up by 4.0pp YoY. The 'Axles' unit generated minus HUF 146 million, the 'Automotive Components' unit HUF 289 million, while the 'Vehicle' segment HUF 73 million operating profit in Q3. The new Re kard segment contributed HUF 118 million in terms of operating profits.

Net financial loss amounted to HUF 787 million, which heavily weighed on quarterly profitability (mostly a result of exchange rate loss). After taxation, quarterly loss was HUF 563 million after HUF 317.6 million profit in Q2 2022 and a HUF 569.6 million loss in Q1 2022 (Q3 2021 quarterly loss was HUF 665 million). As a result, quarterly EPS was minus HUF 42, while it was minus HUF 50 a year before. The significantly negative EPS is, however, mostly the result of the above-mentioned FX losses.



*Q2 and Q3 2021 EPS w/o one-off effect of property sale in Q2 2021.

Comments

- **The registration figures of medium and heavy-duty trucks in the EU** showed a good improvement of 18.3% in September YoY (25,720 vs. 21,739). All major markets positively contributed to overall growth, where Spain and Germany posted the biggest gains (+22.8% and +11.9% YoY) according to ACEA. Over the first 9M of 2022, medium and heavy-duty vehicle registrations in the EU grew by 1.5%, where Central European countries largely contributed to the positive performance. It is worth noting that the medium and heavy-duty market is holding up significantly better than the light commercial vehicles market, which registered a 21.2% decline over the 9M of 2022 and 11.3% in September YoY.
- The **demand for medium and heavy buses & coaches in the EU** remained flat in September YoY (2,370 vs. 2,372). Overall, new bus and coach registrations across the EU over the first 9M of 2022 declined by 4.8% to 20,457 units. Among the key markets Spain was the only one to post growth (+29.3%), while Germany, France and Italy all suffered significant declines.
- **Significantly lower GDP growth is expected in the EU in 2023 coupled with elevated inflation figures.** The seasonally adjusted GDP in Q3 2022 increased by 0.2% in both the euro area and the EU QoQ according to Eurostat. Compared with the same quarter of the previous year, seasonally adjusted GDP increased by 2.1% in the euro area and by 2.4% in the EU. The EC's latest economic forecast (European Economic Forecast – Autumn 2022) projects that real GDP will grow by 3.3% in 2022 and 0.3% in 2023 in the EU. The Summer 2022 forecast had 2.7% GDP growth in 2022 and 1.5% GDP growth in 2023. On the other hand, inflation is forecast to increase by 9.3% this year in the EU and while it is expected to decline in 2023 but it will remain elevated at 7%. Monetary policy is expected to continue its tightening path and ECB is assumed to keep hiking its policy rate throughout 2023.
- Management noted that in Q3 2022 **the practical implementation of the Rába Modernisation Programme 2025 has started.** This encompasses the reorganisation of the entire production structure at the central Győr plant, as well as reinstallation of the production lines in the individual production halls and movement within plant sections of individual activities. There will be also substantial capital expenditure programme into machinery and the modernisation of the real estate infrastructure and optimization of energy consumption. Positive impacts on operation and profitability will mostly be felt from 2nd half of 2024 and in 2025.

Valuation

- The group had strong revenue growth in Q3, however, energy prices are still very high and inflationary pressures remain, while the economic outlook is clearly deteriorating. The outlook in terms of profitability remains challenging, while uncertainties abound in both the revenue and the cost sides, which makes forecasting difficult.
- The company acquired the remaining 75.1% of Re kard Hajtómű és Gépgyártó Kft. (Phase 2) using the option offered to Rába after H1 closing on July 1. As a result, Re kard now operates as a wholly owned subsidiary of Rába. In 2021, Re kard had a revenue of HUF 3.43bn (69% from exports), EBIT of HUF 40 million and net income of HUF -0.6 million. In Q3 2022, Re kard contributed ~HUF 1bn to group revenues, HUF 167 million to EBITDA and HUF 118 million to operating profit.
- We have increased our revenue expectations for 2022 from HUF 55.9bn to HUF 60.2bn given strong sales growth in 9M and the above-mentioned acquisition. We expect HUF 1.61bn EBIT and HUF 3.98bn EBITDA in 2022, up from HUF 1.12bn and HUF 3.49bn, respectively.
- After 12M EPS of HUF 94 last year, our forecasts suggest 12M EPS could decrease to minus HUF 36 in 2022 given heavy net financial losses incurred over the year (mostly FX losses). We assume no dividends paid in 2022 and 2023 given the challenges.
- We left our 12M target price flat at 1,115 HUF/share. The TP reflects the stronger sales growth, which is largely offset by rising costs and interest rates, while the economic outlook keeps deteriorating. Our valuation model focuses on the forecast horizon between 2022 and 2026. Over the long-term (post 2024) the ongoing modernization programme can add value to the company, which offsets near-term losses.
- The new 12M TP is 15.8% lower than the HUF 1,325 closing price on 21 November.

Deduction of 12M target price

Rába's valuation (HUFm)	2020	2021	2022	2023	2024	2025	2026	FCFF in the explicit period
FCFF	2 466	-2 450	-4 581	291	733	777	1 564	
Discount factor	0,95	0,94	0,91	0,81	0,73	0,68	0,63	
DCF	2 334	-2 300	-4 148	237	538	526	982	-1 865
Terminal value (HUFm)								48 005
Net present value (HUFm) of TV								30 128
Enterprise Value (incl. possible future property sale) HUFm								30 006
Net debt								16 246
Equity value - Dec 31 2022, HUFm								13 761
Number of shares								13 352 765
Expected return on equity								8,2%
12M Target price								1 115
Current price								1 325
Upside/Downside								-15,8%
TR Upside/Downside								-15,8%

Source: OTP Multi-Asset

CONSOLIDATED INCOME STATEMENT		HUFm				
	2019	2020	2021	2022E	2023E	2024E
Domestic sales	16 257	11 560	13 578	15 887	15 290	15 443
Export sales	33 525	27 194	32 857	44 357	41 339	41 753
Total sales revenue	49 782	38 754	46 436	60 244	56 629	57 196
Direct cost of sales	-40 463	-30 722	-37 617	-49 099	-46 153	-46 042
Gross profit	9 319	8 032	8 819	11 145	10 476	11 153
Indirect costs of sales	-7 979	-7 806	-6 841	-9 537	-9 684	-9 437
EBIT	1 340	227	1 978	1 608	793	1 716
EBITDA	3 455	2 568	4 370	3 976	3 138	4 037
Net financial profit/loss	-411	-900	-208	-1 693	-300	-300
Profit before tax	1 004	-669	1 775	23	493	1 416
Tax	-433	-361	-503	-500	-153	-439
After-tax profit	572	-1 030	1 272	-477	340	977
Dividend	267	0	0	0	0	177
EPS	43	-77	94	-36	25	73
Adjusted EPS**	43	-77	33	-36	25	73
DPS	20	0	0	0	0	15

*Unconfirmed, estimated on the basis of official consolidated total sales and preliminary export sales figures.

**W/o one-off effect of property sale terminated in Q2 2021

CONSOLIDATED BALANCE SHEET		HUFm				
	2019	2020	2021	2022E	2023E	2024E
Property, plant, equipment	25 394	25 986	25 417	26 644	26 911	27 180
Intangible assets	175	89	41	11	6	4
Non-current assets	26 563	26 979	26 285	27 424	27 686	27 549
Inventories	7 651	5 863	9 942	15 663	15 007	14 609
Receivables and other current assets	6 488	5 948	7 683	12 651	12 742	12 583
Cash and cash equivalents	805	3 303	1 246	1 506	1 416	1 716
Current assets	15 006	15 226	18 872	29 821	29 164	28 908
TOTAL ASSETS	41 569	42 205	45 156	57 245	56 850	56 457
Share capital	13 473	13 473	13 473	13 473	13 473	13 473
Own shares	-109	-109	-109	-109	-109	-109
Capital reserve	0	0	0	0	0	0
Stock option reserve	0	0	0	0	0	0
Retained earnings	7 833	6 533	7 816	7 339	7 679	8 460
Total Equity	21 197	19 897	21 180	20 703	21 043	21 825
Long-term loans and other liabilities	3 567	6 207	8 253	12 470	13 717	13 031
Provisions	237	40	0	0	0	0
Non-current liabilities	3 917	6 540	8 516	12 692	13 826	13 142
Loans and credits	5 354	3 505	2 128	5 282	4 035	4 721
Payables and other short-term liabilities	10 929	11 811	12 781	17 719	17 158	16 015
Current Liabilities	16 455	15 769	15 460	23 850	21 981	21 490
TOTAL EQUITY AND LIABILITIES	41 569	42 205	45 156	57 245	56 850	56 457

CONSOLIDATED CASH FLOW		HUFm				
	2019	2020	2021	2022E	2023E	2024E
EBITDA	3 455	2 568	4 370	3 976	3 138	4 037
Cash flow from operation	8 379	5 541	-1 468	-2 272	2 897	2 918
Cash flow from investment	-8 658	-3 074	-981	-2 308	-2 606	-2 185
FCFF	-278	2 466	2 450	-4 581	291	733
FCFE	111	2 499	2 843	1 097	84	526

Sources: Rába Automotive, OTP Multi-Asset

Risks surrounding Rába's economic activity

Liquidity risk: In the current covid crisis, liquidity and debt issues came to the fore as companies must maintain liquidity and solvency at a time when revenues decline in a better case, or simply vanish for a period in the worst case. In industry comparison, Rába operates with relatively low liquidity, which further decreases in times of economic distress (e.g. the financial crisis of 2008/2009). Earlier data prove that Rába's liquidity position already weakened by end-2019 and remained at the same low level in Q1 2020. In Q2, liquidity ratios deteriorated, but by end-Q4 2020 current ratio, quick ratio and cash ratio also improved compared to end-2019. When assessing Rába's indebtedness, it stands out that it is lower than it was in 2008/2009. The company had a Net Debt / EBITDA ratio of 2.5x at the end of 2020, while it was 2.1x at the end of 2021.

FX risk: As export sales have a dominant share in Rába's sales performance, the company is exposed to exchange rate fluctuations. About 60–70% of the total sales revenue is FX-dominated, which climbed from 65% in 2017, to 67% in 2018 and in 2019, to 70% in 2020, and to 71% in 2021. Exports' weight in sales revenues is expected to remain above 70% in the coming years.

With the Hungarian economy returning to the path of recovery and as inflation came to fore, the MNB started a tightening cycle and raised the base rate from 0.6% to 10.75% in several steps. The aim was to reverse the HUF's weakening trend and tackle inflation, but the results were mixed. The tightening of monetary conditions is expected to cause gradual HUF appreciation and consequently, the strengthening HUF stops supporting Rába's HUF-denominated export performance.

Raw material & energy prices: Steel prices on the global commodity market started to decline in mid-2018. Since the second half of 2018, benchmark steel prices have been dropping, and by the middle of 2019, prices fell more than 20%, when comparing quarterly averages. Steel benchmark kept on falling throughout the second half of Y2019 and the first half of 2020 and bottomed out in Q3 2020. Since then, hot-rolled coil benchmark price has skyrocketed: the average price in Q4 2021 was 230% above the quarterly average registered in Q4 2020, however, this was followed by a sharp downturn towards the end of the year. This did not last long, and prices bounced back after the start of the Russia-Ukraine conflict. Recently, however, due to recessionary fears raw material prices have fallen back again.

Economic environment: The economic landscape radically changed in Q1 2020 due to the coronavirus pandemic, and economies went off from their previously expected growth paths. There is still a lot of uncertainty considering the possible recovery and normalization, which also adds downside risk to our forecast. And while Hungary's monetary and exchange rate policies are also changing, in case of an external shock, like the current one, we can see that the monetary policy will be able to accommodate itself to that situation through exchange rates.

Risks surrounding Rába's property for sale: According to Rába's earlier announcement on the resolutions of the BoD on behalf of the shareholders' AGM in 2020, the

management was authorized the sell part of the company's property portfolio. It is expected to be fulfilled in one year's time. When it happens, the sales revenue as a one-off item will add some 83 HUF/share to Rába's enterprise value, calculated based on the disclosed data. However, in the current environment, companies may postpone their investment plans, while administrative and regulatory hurdles may also hinder the transaction.

Labour supply: Labour market developments, particularly the labour shortage that prevailed earlier, may have arrived at a point when it may harm the companies' growth potential, and result in higher labour costs, or extra capex need to substitute labour force with robotization, or may lead to chronic capacity shortage. Rába is located in Western Hungary, where unemployment practically vanished, and the local labour market is very supply-driven. However, covid may change the landscape in this sense as well, but its effect is hardly palpable at this point, as wage dynamics in the manufacturing industry remained at an elevated level this year, the latest statistics show.

With the fast recovery of the Hungarian economy, the unemployment caused by the pandemic may get absorbed very quickly, and result in tight labour market. This will further strengthen wage dynamics, which did not really lose steam even in the period hit by the pandemic. Further increasing payroll expenses may dent Rába's profitability again.

Ownership: In mid-July Rába announced an ownership change concerning Rába's main shareholder MNV (Hungarian National Asset Management Inc.). Under the recently amended decree, Nemzeti Védelmi Ipari Innovációs Zártkörűen Működő Részvénytársaság (National Defence Industry Innovation Ltd.; NVII) has been appointed to exercise all of the rights and obligations of the state as owner, as of 4 June, 2021. The shares of Rába Automotive Holding owned by the Hungarian state were transferred on 20 July 2021 from the securities account of MNV Zrt to the securities account of NVII. On 23 August, Rába published an announcement about the disposal of voting rights, informing that the influence of NVII in Rába Automotive has changed. According to media reports, which offer more details, the tight-lipped official announcement covers that 20% of Rába's voting right has been placed from NVII to the 'Foundation for Széchenyi University'. Furthermore, the company announced on 18 February 2022 that the remaining voting rights of NVII have been acquired by the Ministry for Innovation and Technology. As a result, the voting rights of NVII decreased from 54.83% to 0%.

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 Rába Automotive Holding in the past twelve months:

Period	Recommendations	Percent of Recommendations
Q4 2021	BUY	0%
	HOLD	100%
	SELL	0%
Q1 2022	BUY	0%
	HOLD	100%
	SELL	0%
Q2 2022	BUY	0%
	HOLD	0%
	SELL	100%
Q3 2022	BUY	0%
	HOLD	0%
	SELL	100%

Date	Recommendation	Target Price	Publication
01/09/2021	HOLD	HUF 1476	Equity Note
18/11/2021	HOLD	HUF 1400	Quarterly Earnings Update
25/02/2022	HOLD	HUF 1350	Quarterly Earnings Update
22/04/2022	HOLD	HUF 1350	Equity Note
23/05/2022	SELL	HUF 1100	Quarterly Earnings Update
29/08/2022	SELL	HUF 1115	Quarterly Earnings Update
10/10/2022	SELL	HUF 1115	Equity Note

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

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