

EQUITY NOTE: RÁBA Automotive Holding

Recommendation: HOLD (under revision)

Target price (12M): HUF 1,350 (under revision)

22 April 2022

Highlights

Equity Analyst:
Ákos Szemán

Phone:
+36 1 486 6277

Email:
akos.szeman@otpbank.hu

Rába issued a profit warning on the 20th of April after trading hours, which states that based on preliminary assessments the Q1 2022 consolidated operating profit of the Group is likely to be negative, potentially meaning a loss of HUF 500 million at group level. This is primarily the result of significantly higher energy prices attributable to the Russia-Ukraine situation and generally tight commodity markets. The company aims to pass through some of these costs to customers and to increase efficiency, while introducing cost management measures. It remains to be seen how efficiently Rába can implement these steps to mitigate the negative global developments and it is also crucial, whether we will see some normalization in the level of raw material and energy prices over the following months. For now, we put our HUF 1,350 price target and HOLD recommendation under revision and will update our model once 2022 Q1 results are published.

Profit warning due to elevated energy prices

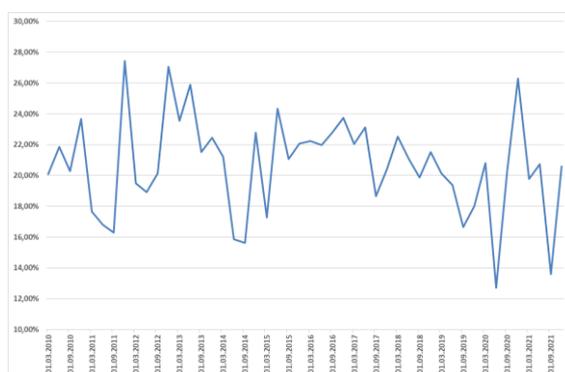
Rába announced on the 20th of April after trading hours that based on a preliminary assessment of unaudited information currently available **the Q1 2022 consolidated operating profit of the Group is likely to be negative, potentially meaning a loss of nearly HUF 500 million at group level.** The main reason for the expected negative operating result is primarily related to the considerable loss suffered by Rába Axle Ltd., which is an energy-intensive operation. The likely loss will occur due to the drastic increase in energy prices, which remained elevated over 2022 as well given the Russia-Ukraine conflict and the already tight market. In order to mitigate the negative effects, the company increased the flexibility of production and introduced stringent cost management measures and also focuses on improving the efficiency of production processes and technology. Rába also mentioned that in order to maintain the stability of operations, a key objective is to continue to charge the customers with the energy costs growth and to enforce this growth in sales prices.

In our previous note, published on 25 February 2022, we revised down our 12M target price on Rába to 1,350 HUF / share from 1,400 HUF with a HOLD

recommendation. We noted that significant export activities fuelled the company's growth in Q4, net sales revenue increased to HUF 13.2bn (+20% YoY), which was the strongest Q4 result of the past five years. On the other hand, we mentioned as well, that raw material and energy prices remained extremely high during the quarter, putting high pressure on the bottom line. **Our conclusion was that given the market environment and the escalation of the Russia-Ukraine conflict the short-term outlook is dim in terms of profitability.**

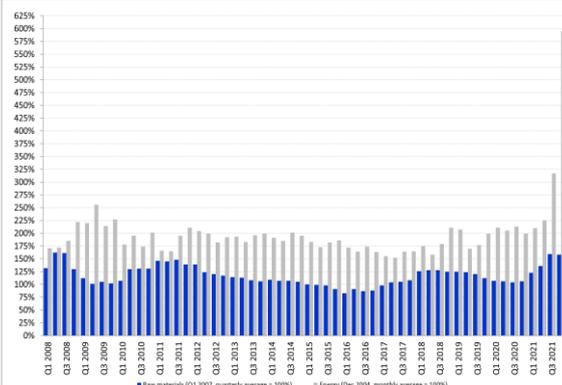
Over the past several quarters, cost-side pressures intensified in the automotive industry given elevated energy and raw material prices, which cast shadow on profitability. **Rába's direct cost of sales rose by almost 30% in Q4 on a YoY basis** from HUF 8,099 million to HUF 10,490 million, which had a significant negative impact on profitability despite the impressive export revenue growth (EBIT was down 56% YoY, after-tax profit by 90% YoY). The company noted that the substantial increase in costs is passed on by the Rába Group to its trading partners under the terms of the existing agreements and as a result of negotiations, with a quarterly delay in the case of the majority of the products.

Historical rate of gross margin at Rába Automotive (quarterly)



Sources: Rába Automotive Holding

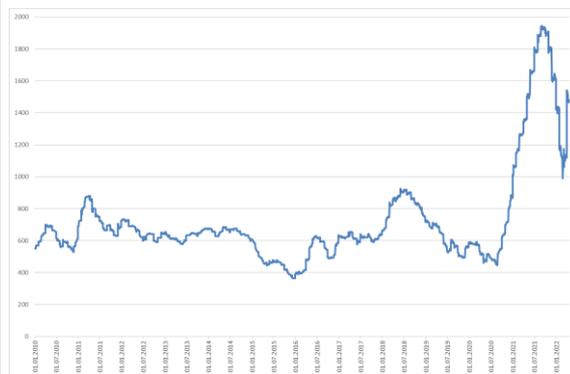
Input cost indices of Rába Automotive (quarterly averages)



Source: Rába Automotive Holding

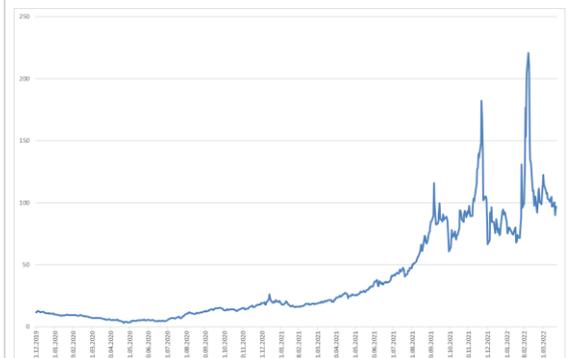
Steel and energy prices – including gas and electricity - remain elevated and close to record high levels, which can be attributed to the Russia-Ukraine situation and to a generally tight commodity market (for example higher cost of steel production due to rising coking coal and iron ore prices etc.). We expect that prices will somewhat normalize in due course, however, it is difficult to estimate how long this process may take given the ongoing geopolitical issues.

Steel market prices bounced back, close to record high levels (hot-rolled coil, USD/MT)



Source: Bloomberg

Gas prices remain elevated, way above long-term average (ICE Dutch TTF, EUR/MWh)



Source: Bloomberg

The profit warning issued by Rába shows that the above-mentioned issues (inflationary pressure, supply-chain disruption, high raw material and energy prices and so on) put high pressure on the profitability of the automotive industry participants. It remains to be seen how efficiently the company can pass through some of these costs to customers and whether steel and energy prices will indeed moderate towards the end of the year. **As a result, we put our HUF 1,350 price target and HOLD recommendation under revision for now and will update our model once 2022 Q1 results are published.**

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. However, by end-2020 leverage increased and net debt/EBITDA climbed to 3.0x from 2.4x at end-2019. Debt/EBITDA ratio grew from 2.7x at the end-2019 to 5.7 by the end of 2020.

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 2.9% 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 as a consequence, 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. Steel prices are now lower, but still above their long-term average.

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
Q2 2021	BUY	0%
	HOLD	100%
	SELL	0%
Q3 2021	BUY	0%
	HOLD	100%
	SELL	0%
Q4 2021	BUY	0%
	HOLD	100%
	SELL	0%
Q1 2022	BUY	0%
	HOLD	100%
	SELL	0%

Date	Recommendation	Target Price	Publication
18/02/2021	HOLD	HUF 1280	Quarterly Earnings Update
21/05/2021	HOLD	HUF 1353	Quarterly Earnings Update
26/08/2021	HOLD	HUF 1476	Quarterly Earnings Update
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

[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 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 which was concluded by and between BSE and OTP Bank Plc (registered seat: 1051 Budapest, Nádor u. 16., company registration number: Cg. 01-10-041585, hereinafter: Investment Service Provider). This research/commentary was made with the joint, equally proportional financing of the BSE and the company that is the subject of this research/commentary.

The Investment Service Provider's policies and procedures ensure the independence of this research/commentary, and the Investment Service Provider has undertaken not to accept any instructions or additional remuneration from the company involved in the research/commentary.

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 shall be solely liable for these. The Service Provider is entitled to all copyrights regarding this research/commentary however BSE is entitled to use and advertise/spread it but BSE shall not modify 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. This research/commentary cannot be deemed as an incentive to enter into contract or covenant.

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 it 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.
21. The personal data in this investment research are processed by OTP Bank. The legal basis for processing the data is the legitimate interest of OTP Bank. The detailed information about the processing of personal data and the related rights of data subjects is available [here](#).

This document was prepared by:

Ákos Szemán
Equity Analyst
OTP Research

This document was finalized at 8:02:30 AM on 22 April 2022