Duna House Holding Nyrt.
Hungary, Business Services

SCOPE BB- STABLE

Key metrics

			Scope estimates	
Scope credit ratios	**2021**	**2022**	**2023E**	**2024E**
Scope-adjusted EBITDA/interest cover	94x	net cash interest	39x	14x
Scope-adjusted debt/EBITDA	3.3x	3.3x	5.0x	2.9x
Scope-adjusted funds from operations/debt	31%	24%	18%	26%
Scope-adjusted free operating cash flow/debt	16%	73%	25%	29%

Rating rationale

The rating of Duna House continues to reflect its leading market position as a real estate broker in Hungary and Poland and the improved diversification following the acquisition of Hgroup, one of the top three loan brokerage companies in Italy. It also reflects the strong customer granularity as most transactions target single clients. The business risk profile suffers from Duna's small size in highly fragmented markets and weakening profitability over the years. We anticipate a decline in the Scope-adjusted EBITDA margin in 2023 due to Hgroup integration costs combined with weaker-than-expected revenue. The weakening profitability will put leverage under pressure, but we expect profitability to recover from 2024 based on the higher demand for loans in H2 2023.

Duna House's asset-light business ensures strong interest coverage, supporting the rating. However, the expansion strategy and real estate development business has driven up leverage in the past years and made cash flows volatile. Liquidity is adequate as the only substantial debt amounts are two bonds to be repaid from 2026.

Outlook and rating-change drivers

The Outlook is Stable and reflects our expectation that Duna House will maintain strong interest cover thanks to its net cash position and that Scope-adjusted debt/EBITDA, after peaking in 2023, will return below 4x in 2024 due to recovering EBITDA. The Stable Outlook also reflects the expectation that the issuer can maintain its credit metrics within the rating case even amid weaker demand.

A positive rating action would require the issuer to sustain Scope-adjusted debt/EBITDA leverage below 3.0x.

A negative rating action could be warranted if the issuer showed an increase in Scope-adjusted debt/EBITDA to around 4.0x on a sustained basis. This could be caused by weaker-than-expected revenue due to overall transaction market weakness or debt-funded investments at levels substantially beyond the rating base case.

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
16 Nov 2023	Affirmation	BB-/Stable
14 Nov 2022	Affirmation	BB-/Stable
22 Dec 2021	Affirmation	BB-/Stable

Ratings & Outlook

Issuer	BB-/Stable
Senior unsecured debt	BB-

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Related Methodologies:

Corporate Rating Methodology; October 2023

European Real Estate Methodology; January 2023

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Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• Strong position in Central and Eastern European real estate and loan brokerage markets (ranked first in Hungary, second in Poland) and in the Italian loan brokerage market (top three) • Asset-light business model, hence little financial debt and moderate financial leverage • Diversified among several real estate-related services and countries; high customer granularity • Most debt at fixed rates	• Dependency on general transaction dynamic in the real estate and loan markets in Central and Eastern Europe and Italy, with little non-transaction-based recurring revenues • Fierce competition in online real estate brokerage • International expansion via M&A bearing execution and integration risks, particularly given the size and complexity of the recent acquisition in Italy • Volatile cash flows

Positive rating-change drivers	Negative rating-change drivers
• Scope-adjusted debt/EBITDA sustained at around or below 3.0x	• Scope-adjusted debt/EBITDA sustained at around 4.0x

Corporate profile

Duna House Holding Nyrt. was founded in 1998 as a real estate company based in Budapest providing consulting services to foreign investors. In 2003 the company adopted a franchise business model, leading to its expansion across Hungary. In 2004, Duna House further expanded to provide the full range of services to seller and buyers, which today includes real estate brokerage, loan brokerage, loan insurance, other financial services and property appraisals. The company is market leader in real estate in Hungary and Poland and is top three in loan brokerage in Hungary and in Italy, and n. 5 in Poland. The group is also present in the Czech Republic.

Table of Content

Environmental, social and governance (ESG) profile[1]

Environment		Social		Governance	
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)		Labour management		Management and supervision (supervisory boards and key person risk)	Grey leaf
Efficiencies (e.g. in production)		Health and safety (e.g. staff and customers)		Clarity and transparency (clarity, quality and timeliness of financial disclosures, ability to communicate)	Grey leaf
Product innovation (e.g. transition costs, substitution of products and services, green buildings, clean technology, renewables)		Clients and supply chain (geographical/product diversification)		Corporate structure (complexity)	Grey leaf
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	Grey leaf

Legend

Green leaf (ESG factor: credit positive)
Red leaf (ESG factor: credit negative)
Grey leaf (ESG factor: credit neutral)

Neutral ESG considerations

No material ESG risk identified.

As a real estate agency, the major ESG risks Duna House is exposed to are typically regulatory and reputational as well as governance-related. Environmental risks are not significant given the asset-light business model. However, ESG risks could materialise from a mis-selling of loans (social) and the current lack of independent oversight of the board (governance).

We acknowledge a good level of transparency and timely disclosure of financial information.

[1] These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Financial overview

				Scope estimates		
Scope credit ratios	**2020**	**2021**	**2022**	**2023E**	**2024E**	**2025E**
Scope-adjusted EBITDA/interest cover	26x	94x	net cash interest	39x	14x	13x
Scope-adjusted debt/EBITDA	3.9x	3.3x	3.3x	5.0x	2.9x	3.2x
Scope-adjusted funds from operations/debt	21%	31%	24%	18%	26%	22%
Scope-adjusted free operating cash flow/debt	-9%	16%	73%	25%	29%	16%
Scope-adjusted EBITDA in HUF m						
EBITDA	1,527	1,949	4,451	3,402	4,422	4,814
less: EBITDA from development project	-	-	-1,000	-933	-545	-888
Scope-adjusted EBITDA	**1,527**	**1,949**	**3,451**	**2,469**	**3,877**	**3,926**
Funds from operations in HUF mHUF m						
Scope-adjusted EBITDA	1,527	1,949	3,451	2,469	3,877	3,926
less: (net) cash interest paid	-59	-21	64	-64	-283	-312
less: cash tax paid per cash flow statement	-219	-253	-1,007	-597	-668	-744
add: dividends from associates	-	370	194	398	-	-
Funds from operations (FFO)	**1,249**	**2,045**	**2,702**	**2,206**	**2,926**	**2,870**
Free operating cash flow in HUF mHUF m						
Funds from operations	1,249	2,045	2,702	2,206	2,926	2,870
Change in working capital	-1,520	-893	5,320	886	807	-278
less: capital expenditure (net)	-113	-110	511	138	-292	-292
less: lease amortisation	-128	-3	-237	-221	-221	-221
Free operating cash flow (FOCF)	**-512**	**1,039**	**8,296**	**3,009**	**3,220**	**2,079**
Net cash interest paid in HUF mHUF m						
Net cash interest per cash flow statement	-59	-21	64	-64	-283	-312
Net cash interest paid	**-59**	**-21**	**64**	**-64**	**-283**	**-312**
Scope-adjusted debt in HUF mHUF m						
Reported gross financial debt	11,795	11,283	14,821	14,413	13,900	13,900
Operating leases	283	449	1,762	1,980	1,980	1,980
less: cash and cash equivalents[2]	-6,902	-6,497	-5,369	-4,146	-4,633	-3,123
add: non-accessible cash	733	1,270	93	1	0	0
Scope-adjusted debt (SaD)	**5,909**	**6,505**	**11,307**	**12,248**	**11,247**	**12,757**

[2] Netting of cash is generally only applicable to ratings in the BB category or higher and only if the cash is permanent and accessible. When calculating Scope-adjusted debt, we have only netted 50% of the available cash for the period 2022-2025E, as we assume that some of the available cash will be used for future acquisitions and/or property development activities. This results in a difference from the unrestricted cash reported in the liquidity section (page 7) where as “unrestricted cash’ we consider the total cash minus the non-accessible cash.

Business risk profile: BB-

Industry risk profile: BBB-

Duna House is a Hungarian real estate agency whose services include loan brokerage, insurance, real estate brokerage, real estate management and property appraisal.

The industry risk profile is moderate for Duna House. Until recently, the company was active in real estate development but in the future will be mostly exposed to business services. The business services industry has medium levels of cyclicality, entry barriers and substitution risk.

Leading market position in Hungary, Poland and Italy…

The issuer's market position is credit-positive. The group has the leading platform in Poland and one of the two largest real estate brokerage platforms in Hungary (the other is Otthon Centrum's, whose size is similar in terms of listings, offices and salespersons). With the recent acquisition of Hgroup, Duna House is now also a top three loan broker in Italy.

… but relatively small size

All markets are very fragmented, which implies little pricing power but also allows for a potential increase in market share if the real estate and loan brokerage sector continues to consolidate. We expect Italy to be a major growth driver going forward. While Hgroup still has little penetration in real estate loan brokerage, the recently signed partnership with Professione Casa, a major Italian real estate agency, is expected to bring in customers. With the agreement, Hgroup purchased a 10% stake in Professione Casa and will exclusively provide loan brokerage services to Professione Casa clients for a fee.

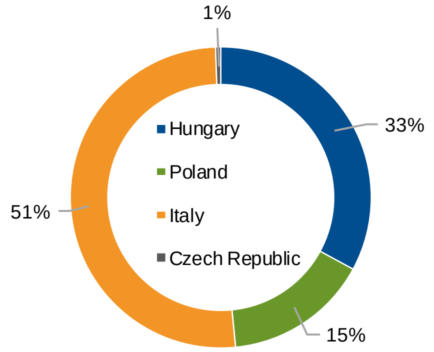
Improved geographical and product diversification

The business risk profile also benefits from greater diversification following Hgroup acquisition, which reduced the dependency on two similar markets. Going forward, we expect even more revenues from Italy, driven by the Professione Casa partnership. Hgroup has now also expanded its range of services, with revenues from not only real estate but also salary-backed loans, personal loans and insurance brokerage.

Nonetheless, we highlight that group revenue will become increasingly dependent on Italy. In H1 2023, this market represented 51% of revenue.

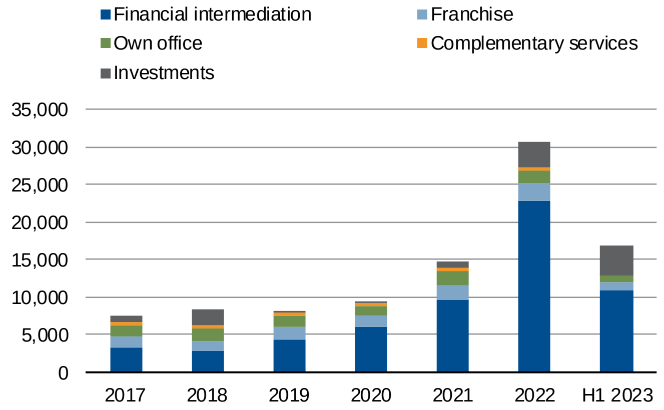
Customer granularity is very high as the issuer targets only retail clients. Going forward, we expect client diversification to remain stable.

Figure 1: Geographical diversification by revenue (H1 2023)



Sources: Duna House

Figure 2: Revenue breakdown per type of service (HUF m)

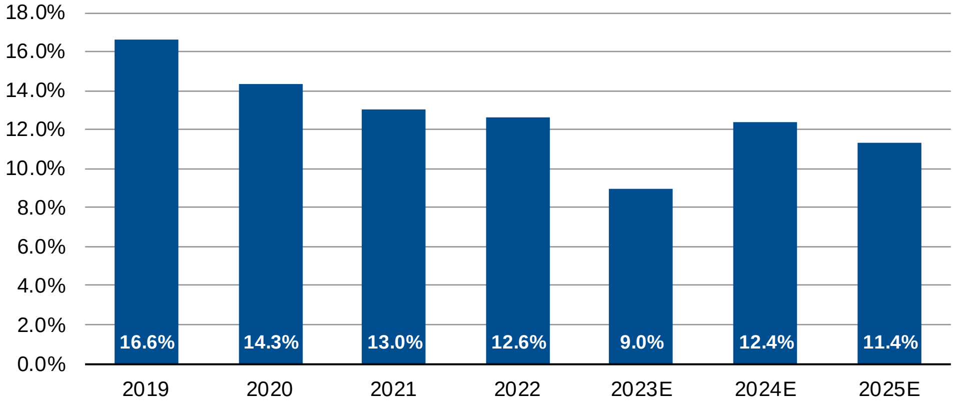


Sources: Duna House

Profitability to temporarily decline

The issuer's operating profitability, measured by the Scope-adjusted EBITDA margin, ranged from 15% to 30% in recent years. However, despite growing revenue, EBITDA margins have declined over the years after the aggressive expansion policy. In 2023 we anticipate the margin to reduce to around 9% based on stable revenue and higher staff costs. We note that despite unfavourable real estate conditions, Duna House is likely to keep revenue stable in 2023, thanks to inorganic growth (Hgroup acquisition) and the slightly recovering markets in Hungary and Poland in H2 2023. Hungarian consumers are adapting to the slowing macroeconomy since H1 2023, while in Poland government subsidies (2% fixed rate for first-home buyers) are stimulating growth. We anticipate the positive trend to continue into 2024 and Duna House's margin to recover to around 11%-12%, also sustained by the successful integration of Hgroup and the collaboration with Professione Casa.

Figure 3: Scope-adjusted EBITDA margin[3]



Sources: Duna House, Scope estimates

Financial risk profile: BB

We continue to assess the financial risk profile at BB, reflecting strong interest coverage and liquidity, but constrained by the volatility of the leverage and cash flows, amid the expansion strategy and the non-core real estate development business.

Robust interest coverage

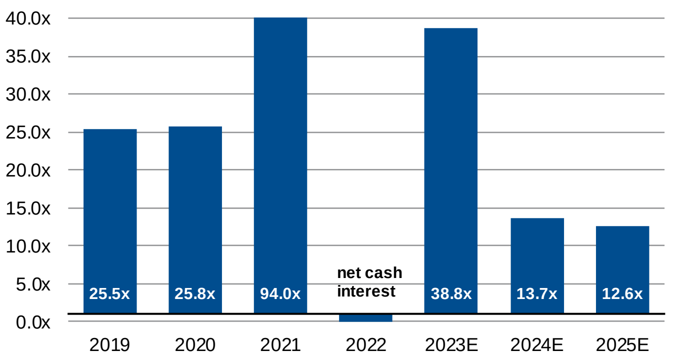
Scope-adjusted EBITDA interest cover has been robust over the years thanks to the asset- and debt-light business model. Favourable interest rates on cash deposits are also yielding substantial net interest income. Even though the interest rate might reduce going forward, interest coverage would remain largely above 10x.

Historically volatile cash flow

While EBITDA and funds from operations have been relatively stable, free operating cash flow has been more volatile. This was due to the real estate development activities, especially for Forest Hill (Hungary) from 2019. In 2022, the sale of some of the Forest Hill units generated significant cash flow and caused net working capital to decrease. Cash flow will continue to depend on developments, but we anticipate less volatility as no significant projects are in the pipeline.

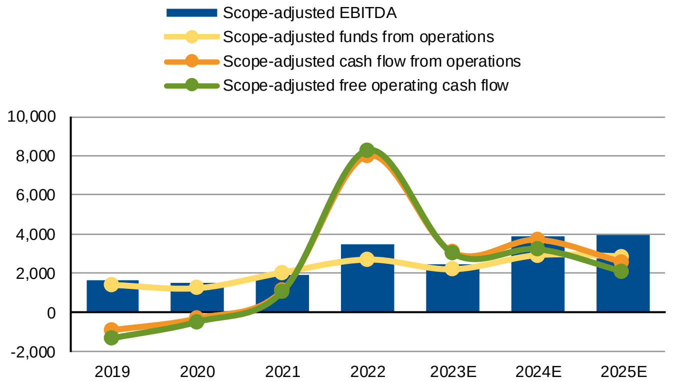
[3] Scope-adjusted EBITDA margin excludes the EBITDA and revenue from the real estate development sale as considered non-core business.

Figure 4: Scope-adjusted EBITDA interest cover



Sources: Duna House, Scope estimates

Figure 5: Cash flows (HUF m)



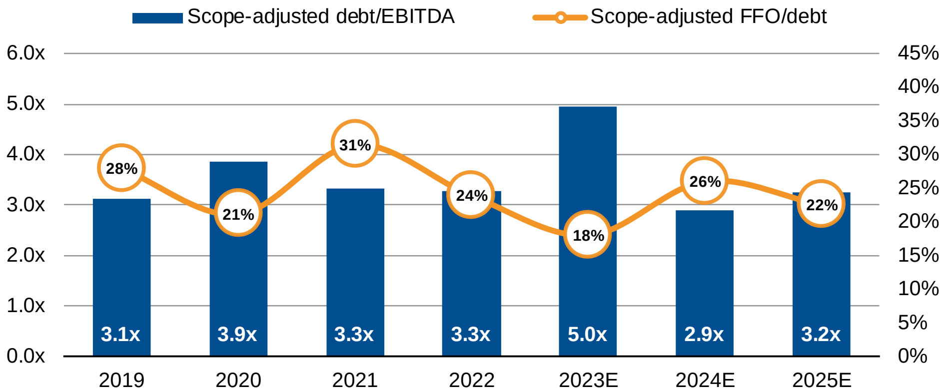
Sources: Duna House, Scope estimates

Lower EBITDA to put temporary pressure on leverage…

…but stable outlook in the medium term

While debt-financed acquisitions caused leverage to rise significantly in 2020 and 2021, in 2022 Scope-adjusted debt/EBITDA reduced following the repayment of long-term debt associated with the Forest Hill project. We anticipate leverage to increase in 2023 due to lower EBITDA but to improve in the medium term on the back of an EBITDA recovery and stable indebtedness. Although Forest Hill units' sales have been slower than expected, the issuer does not expect additional costs related to the project.

Figure 6: Leverage



Sources: Duna House, Scope estimates

Adequate liquidity

Liquidity is adequate. Unrestricted cash improved following the repayment of Forest Hill project debt in July 2022. In addition to free operating cash flows excluding discretionary spending, short-term debt repayment will be covered well over 200% going forward. Further, the two outstanding bonds will only amortise from 2026.

Balance in HUF mHUF m	2022	2023E	2024E
Unrestricted cash (t-1)	5,226	10,646	8,292
Open committed credit lines (t-1)	-	-	-
Free operating cash flow	8,296	3,009	3,220
Short-term debt (t-1)	4,373	357	940
Coverage	**>200%**	**>200%**	**>200%**

Long-term debt rating

Senior unsecured debt rating: BB-

We affirmed the BB- senior unsecured debt rating. Our recovery analysis incorporates a default scenario in 2025 and is based on Duna House's liquidation value since the company still has modest assets from real estate development, resulting in an 'average' recovery. We see material uncertainty regarding the group's asset values in a hypothetical default scenario, which would likely be driven by increased competition, a loss of confidence in the business/brand and/or the departure of many licensees and agents.

Duna House has issued two bonds through the Hungarian central bank's Bond Funding for Growth Scheme. The first bond was issued in September 2020 (HUF 6.9bn, HU0000359914) with a tenor of 10 years and a fixed coupon of 3%. Bond repayment start in 2026 with 20% yearly amortisation. The second bond was issued in January 2022 (HUF 6bn, HU0000361217), with a tenor of 10 years and a fixed coupon of 4.5%. Bond repayment starts in 2028 with a 20% yearly amortisation.

Duna House's senior unsecured bonds under the Hungarian bond scheme have accelerated repayment clauses requiring repayment of the nominal amount in case of a rating deterioration (two-year cure period for a B/B- rating; repayment within 15 days after the bond rating falls below B-, which could have default implications). Other bond covenants in addition to the rating deterioration covenant include non-payment, insolvency proceedings, cross-default, pari passu and negative pledge.

Appendix: Peer comparison (as at last reporting date)

	Duna House Holding Nyrt	Otthon Centrum Kft.	Pannon Work Zrt.	Mobilbox Kft.	Progress Étteremhálózat Kft.
	BB-/Stable	BB-/Negative	B+/Stable	BB/Stable	BB/Stable
Last reporting date	31 December 2022	31 December 2022	31 December 2021	31 December 2020	31 December 2022
Business risk profile					
Service offered	Loan brokerage, real estate brokerage and other financial and management services	Loan brokerage, real estate brokerage and other financial and management services	Human resource services	Rental and sales of office, storage and special containers	Franchisor of McDonalds restaurants in Hungary
Scope-adjusted EBITDA (EUR m)	9.1	3.9	2.4	17.4	20.6
Scope-adjusted EBITDA margin	9-13%	7-13%	5-7%	40-43%	13-18%
Financial risk profile					
Scope-adjusted EBITDA/interest cover	net cash interest	net cash interest	11.6x	24.8x	13x
Scope-adjusted debt/EBITDA	3.3x	0.7x	4.5x	0.5x	3.2x
Scope-adjusted funds from operations/debt	24%	125%	14%	173%	28%
Scope-adjusted free operating cash flow/debt	73%	69%	-7%	70%	-14%

Sources: Public information, Scope

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