CONCORDE RESEARCH

CEE Equity Research | Hungary | Real Estate

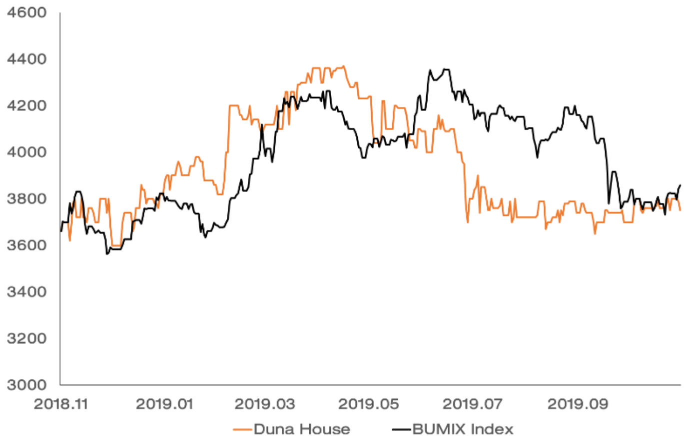
27 November 2019

Duna House

Recommendation: Accumulate

Target price (12M): HUF 4,500

Hun. Core HUF million	2019 Q3	2018 Q3	Ch (%)
Revenues	2,030	1,597	+27%
EBITDA	401	393	+2%
EBIT	345	370	-7%
Cleaned Core EBIT	342	315	+9%
Profit	253	294	-14%
EPS	73	85	-14%
Cumulated EPS	219	421	-48%
No. of transactions (ths)	38	41	-7%



Share price close as of 27/11/2019	HUF 3,800	Bloomberg	DUNAHHOUS HB
Number of shares [million]	3,5	Reuters	DUNAHOUSE.BU
Market capitalization [HUF mn/EUR mn]	12,856 / 37	Free float	30%
Daily turnover 12M [EUR th]	1.46	52 week range	HUF 3,450-4,600

Polish operation mitigated the Hungarian weakness

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In short: Lower transaction numbers in Q3 (-7% y-o-y) due to the MAP+ (Gov. bond for retail) took its toll on DH's financial numbers (especially own offices segment's EBIT which is down -87% y-o-y in Q3) which was partially offset by the surprisingly strong polish operation (profit came to HUF 41 million in Q3 while management guided ca. HUF 75 million FY profit; 9M profit stands at HUF 13 million). In light of the weaker Hungarian real estate market, management expect FY profit to arrive to the lower range of the guidance (HUF 1.1 – 1.4 billion) vs. our HUF 1.053 billion FY profit forecast. Last but not least, management expects the developments to book only next year. Although this sounds as a "delay again", actually it is rational since VAT will increase to 27% - *effective from 2020.01.01*- therefore they will have more pricing power in the next year in our view since those projects are eligible to sell at 5% VAT.

Financials: Q3 EBIT and Profit declined by 7% and 14% respectively because of weak performance of own office segment which offices are mainly concentrated in Budapest (most active area for investor demand for residential units). Cumulative

ANALYST CERTIFIATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 7.

EBIT and profit reached HUF 986 million (-44% y-o-y mainly as a result of high basis due to development completions last year) and HUF 757 million (-46% y-o-y).

In a segment breakdown on EBIT level, the two weaker segments were the own offices segment which contribution plummeted (-87% y-o-y) and the other related segment (-43% y-o-y) where lower transaction number also had a side effect and asset management which achieved lower return (2% vs. 0.5%) in those quarters, thus the lower result. On the other hand, franchise segment and loan intermediation fuelled mainly by the polish operation posted decent growth of 11% and 14% on a yearly basis.

SEGMENT BREAKDOWN ON EBIT LEVEL.

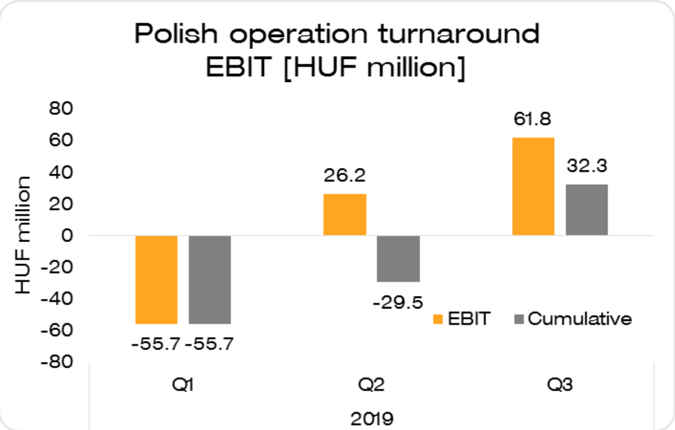
	Q3 2019	Q3 2018	Ch (%)
EBIT	**345**	**370**	**-7%**
Franchise	*92*	*84*	*11%*
Own Offices	*6*	*47*	*-87%*
Loan intermediation	*191*	*167*	*14%*
Other related	*36*	*62*	*-43%*
Real estate mgmt.	*30*	*21*	*40%*
Elimination	*-11*	*-12*	*-11%*

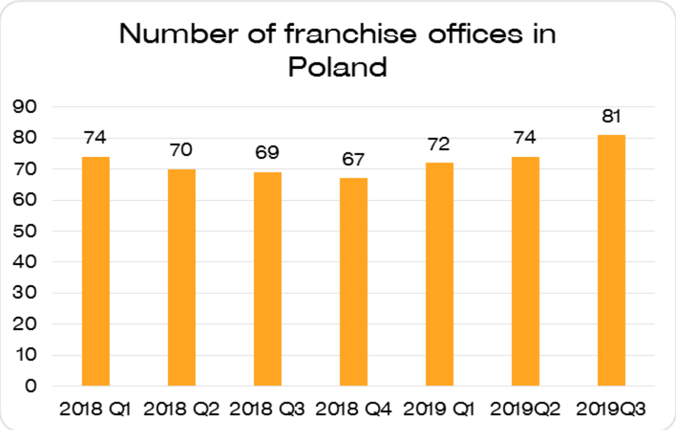
Source: DH, Concorde

Excluding one-offs (ie. revaluation gains, effect of disappearance home savings account contribution) from EBIT, it would have increased by 9% on a yearly comparison, mainly due to the strong polish operation.

On the country breakdown, Polish operation showed the continuation of strong improvement in Q3, posting HUF 62 million EBIT and HUF 41 million profit. So far, cumulative profit stands at HUF 13.5 million due to the large losses in the Q1. Comparing with management FY profit guidance of HUF 50-100 million, we believe it is achievable if the financial improvements continues. We are of the view that the jump in office numbers (+17% y-o-y), and synergies with Gold Finance (latest acquisition) supported the operation in Poland.

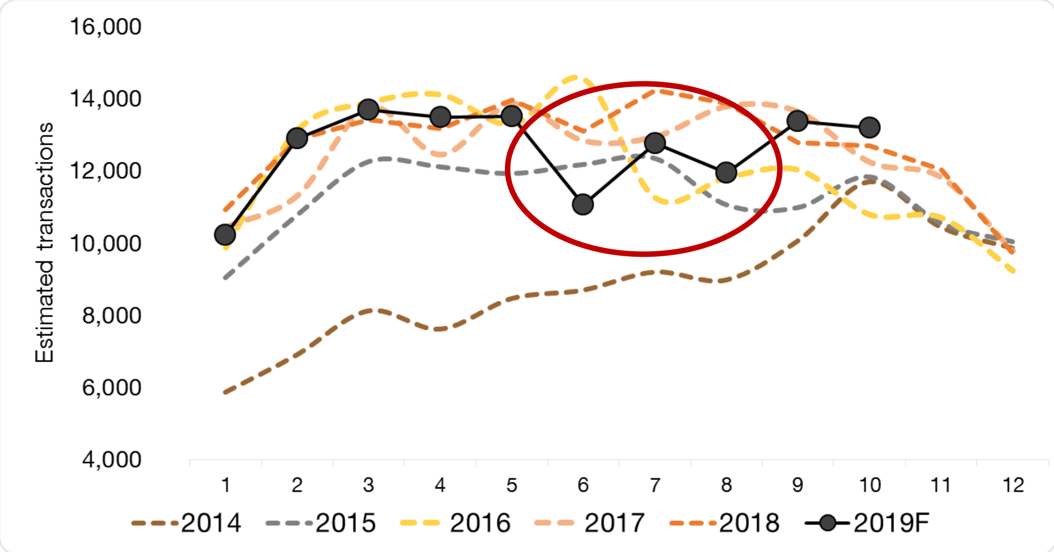
POLISH OPERATION'S FINANCIAL TURNAROUND





Source: DH, Concorde

MONTHLY TRANSACTION NUMBER ACCORDING TO DH'S ESTIMATION



Source: Company reports

Cumulative transaction number is down by 4% compared to last year. We see a few reasons for the phenomena, one is what we had flagged side-effect of the very attractive retail bond of MAP+ that provides ca. 5% avg. yield which could be a substitution of real estate purchase, second is also related to the government's new policy which is the additional family subsidy scheme eligible from 1 July that may have prompted buyers to postpone their purchase to receive the government's help. The latter may turned out to be a fair assumption as transaction numbers were higher by ca. 4-5% for the last two months (September and October) on a yearly basis.
All in all, what we see here is that private investor's intention to purchase residential units could be subdued as long as MAP + gov. bond provides such an attractive risk-return profile. Apart from that, natural demand is considered healthy.

Developments: Management pushed the completions to next year where the new VAT will be in place (27% vs. 5%), due to which we expect better pricing power since the projects are eligible for the lower VAT.

Opinion: All in all, temporary weakness that we saw in the transaction numbers in the middle of the year (may to august) affected Duna House Hungarian operation, especially the own office segment that has relatively higher exposure to Budapest, where most of the investment related residential units purchase is concentrated - *effect of MAP +*). The improvement in the dynamic of transaction numbers (+5% y-o-y) in the last two months (September, October) may convey the message that this transitory period is over. Nevertheless, lower than anticipated earnings in Q2-Q3 prompted management to moderate their FY profit expectation to the lower range of the FY profit guidance of 1.1-1.4 billion, which is in line with our FY profit forecast 1.05 billion for the core operation.

Keeping in mind that all of the developments (excluding Panorama) will be completed next year (ca. HUF 630 per share), and assuming a normalized operation in Hungary (profit of ca. HUF 1 billion) coupled with a strong Polish operation (profit of ca. HUF

150 – 200.), DH trades at 9x P/E (excluding the EPS of the projects). We did not exclude Project Panorama, as it has not been started yet, including it to our calculation adjusted P/E would have been 8.5x.

Admittedly, weaker than expected Q3 results and management moderated expectation of FY profit may put the share price under pressure, however given the extremely strong results for next year (large completions) and the temporary nature of the weakness (transaction numbers are up in September and October) we would recommend to buy the dip – if any materialises. We reiterate our TP and Accumulate recommendation.

Quarterly P&L

	Q3 2019	Q3 2018	Ch (%)
Revenue	**2,030**	**1,597**	**27%**
Operating revenue	1,993	1,564	27%
Other income	37	33	13%
OPEX	**1,685**	**1,220**	**38%**
Cost of materials	15	11	40%
Cost of sold goods and services	293	322	-9%
Used services	1,574	1,026	53%
Personnel expenses	186	156	20%
Depreciation and amortization	56	23	142%
Other operating expenses	-439	-318	38%
EBITDA	**401**	**393**	**2%**
Cleaned Core EBIT	**342**	**315**	**9%**
EBIT	**345**	**370**	**-7%**
Franchise	*92*	*84*	*11%*
Own Offices	*6*	*47*	*-87%*
Loan intermediation	*191*	*167*	*14%*
Other related	*36*	*62*	*-43%*
Real estate mgmt.	*30*	*21*	*40%*
Elimination	*-11*	*-12*	*-11%*
Financial income	15	5	220%
Financial expense	-37	27	-238%
Revaluation	-17	-13	24%
EBT	306	333	-8%
Income tax expense	-53	-39	35%
Net income	**253**	**294**	**-14%**
Transaction Number	38,073	40,902	**-7%**
Intermediated loans [HUF m]	47,506	25,373	**87%**
EPS	73	85	**-14%**
EBIT margin	17%	23%	**-27%**

Source: company reports

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Accumulate	Total return is expected to be in the range of 10-20%
Neutral	Total return is expected to be in the range of 10%-(-10%)
Reduce	Total return is expected to be in the range of -10-(-20%)
Sell	Total return is expected to be lower than -20%
Under Revision	The stock is put Under Revision if covering analyst considers new information may change the valuation materially and if this may take more time.
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