MASTERPLAST - SUMMARY

- **We maintain our Buy recommendation on Masterplast with slightly increased 12-month target price of HUF 805. The further improving market environment might ensure to achieve the targets.**
- There are mostly positive trends in the building industry. On the most significant markets favorable industrial climate is expected in the coming years.
- The Company increased its revenues by 8% in Q1-Q3 2018, this dynamic expansion is expected to continue in the next few years.
- We slightly improved our estimates for revenues, that has been partially offset by effect of the yield increase on our price target.

Recommendation	BUY
12m target price	HUF 805 per share
Current price	HUF 620 per share
Trading range	HUF 488-718
52 week performance	12%
Market capitalization	9 271 mn HUF
Average daily turnover (number of shares)	10 606
Number of shares	14 601 279
Shareholder's structure	Dávid Tibor - 32.65% Balázs Ács - 28.05% OTP Fund M. - 6.22 % SOH and LPH Kft. - 5.34%
Freefloat	27.74%
Tickers	Bloomberg:MASTERPL HB
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FURTHER GROWTH EXPECTED

Majority of the revenue growth came from Hungary this year, partly due to the extension of the discounted flat VAT rate, and the new CSOK regulation, construction activity may continue to foster. Masterplast will strengthen the services that have been appreciated in the recent years, for example the company undertakes precise delivery to its own vehicles, even in small quantities from a substantial stockpile with a minimum waiting time, this has been really important for customers.

During the first phase of the Hungarian construction boom, it was apparent that the demand for Masterplast's products did not rise substantially. This effect was due to the reason that Masterplast's products are typically used in the final phase of construction. If economic downturn would come in the next few years, it would not basically affect the construction trend in Hungary.

Due to tighter environmental and energy standards, insulation aspects are also appreciated, 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 centimeters, which was only 5-6 cm for 5 years. Meanwhile, the Western European average is 15 cm; hence, the market is expected to move in this direction. These trends are beneficial to Masterplast because in the coming years even with the same area of real estate construction, there is a growing demand for facade insulation material.

In the next 2-3 years, one of the most dynamically growing segments can be the export activity, which is typically Western and South European exports. The largest export market is Italy, but the German and the UK presence are growing steadily.

Besides the 8 subsidiaries, Masterplast does not plan to establish new subsidiaries. In Serbia and Macedonia, convergence in the European Union can bring growth, Croatia's tourism investments can push the industry, while in Hungary and Slovakia, the construction activity is significant.

CHANGE OF SHAREHOLDER STRUCTURE

The two co-founders Dávid Tibor and Balázs Ács together have currently more than 60 percent ownership, and Videoton executive's, Ottó Sinkó and Péter Lakatos, as well as OTP Fund Management have a stake of more than 5 percent; thus, the free float is 27.74 percent. **The two major owners are still committed to reducing their ownership to 50 percent**, which can be achieved by the stock sale of major shareholders, but can also be realized by raising capital, for example this may take place when Masterplast would make an acquisition.

Shareholders of the Company with holding over 5%*

Name	Share %
Dávid Tibor	32.65
Balázs Ács	28.05
SOH and LPH Kft.	5.34
OTP Fund Management	6.22
Free float	27.74
Total	100

NEW DIVIDEND POLICY

At the December investor meeting, management gave a dividend forecast, according to which **maximum up to half of the annual net profit can be paid as dividends**, depending on the change of industrial environment, future investments, acquisition opportunity.

According to the management's prediction **dividend of HUF 34 per share are expected to be paid after 2018**, calculated with the current closing price, that means a 5.6 percent dividend yield. In addition, dividends may increase up to HUF 66 per share by 2021.

INDUSTRIAL DIVISION CAN BE FURTHER STRENGTHENED

At Masterplast, the aim is to reduce the dependence on the construction industry, and thanks to the investments in Kál, it will also be able to produce special construction foams, and for the packaging industry, it does not only advance in quality, but it can also appear in new product segments.

BUX INDEX: LONG TERM GOAL

The entry into the BUX index basket is a long-term goal, but on the one hand the increase in the exchange rate, on the other hand the decline in the ownership of large shareholder is also required, and the free float based market capitalization should be considerably higher to meet the BUX criterion.

DCF VALUATION

We slightly increased our 12-month target price to HUF805 from HUF 789 and maintained the Buy recommendation for Masterplast. Although the Hungarian government bond yields increased in 2018, we slightly improved our estimates for revenues, that has been partially offset by effect of the yield increase on our price target.

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

- Based on our assumptions sales will grow in the next years due to the anticipated positive trends on the real estate markets.
- The discount rate we used to get the present value of future cash flows is 6.8%, however, we assumed a slightly higher rate (7%) for the terminal value based on an assumption of a higher yield environment in the medium term. We presumed that capital structure will remain stable in the future (in the last few months has changed slightly): 49% of equity and 51% of debt.
- Equity risk premium is assumed at 6% in the detailed period and in perpetuity.
- We used 10-year Hungarian government bond yield as the risk free rate in WACC calculation in the terminal value period. We used our 5-year Hungarian government bond yield forecast to 2022 (changed from the previous 2.65% to 2.99%).
- For calculating the target price, we used our forint forecast for the end of 2019.

DCF Model (EURmn)	2018	2019	2020	2021	2022	TV
Sales	97201	105490	107420	109040	110720	112040
Sales growth	*8.46%*	*8.53%*	*1.83%*	*1.51%*	*1.54%*	*1.19%*
EBIT	3 712	4 708	4 882	5 011	5 146	5 229
EBIT margin	*3.82%*	*4.46%*	*4.55%*	*4.60%*	*4.65%*	*4.67%*
Tax rate	*7.0%*	*7.0%*	*7.0%*	*7.0%*	*7.0%*	*7.0%*
Taxes on EBIT	*-259.87*	*-329.56*	*-341.76*	*-350.74*	*-360.24*	*-366.01*
NOPLAT	**3 453**	**4 378**	**4 541**	**4 660**	**4 786**	**4 863**
Free Cash flow to the Firm	**-4298**	**2200**	**3993**	**4219**	**4361**	**5052**
WACC	**6.80%**	**6.80%**	**6.80%**	**6.80%**	**6.80%**	**7.00%**
Discount factor	0.94	0.88	0.82	0.77	0.72	0.67
Discounted free cash flow	-4025	1928	3278	3243	3138	60563
Enterprise value	68126					
Minorities	507					
Net debt	30537					
Equity value	37082					
Number of shares outstanding (mn)	14601					
Cost of equity	9.59%					
Fair value per share (EUR, HUF)	**2.30**	**729**				
12M target price (EUR, HUF)	**2.54**	**805**				

Source: Masterplast, MKB

Sensitivity (per share)

WACC	Terminal value EBIT margin				
	3.66%	**4.16%**	**4.66%**	**5.16%**	**5.66%**
6.00%	1 069	1 069	1 069	1 069	1 069
6.50%	925	925	925	925	925
7.00%	806	806	**806**	806	806
7.50%	704	704	704	704	704
8.00%	618	618	618	618	618

WACC	Terminal value growth				
	0.0%	**0.5%**	**1.0%**	**1.5%**	**2.0%**
6.00%	806	925	1 069	1 244	1 463
6.50%	704	806	925	1 069	1 244
7.00%	618	704	**806**	925	1 069
7.50%	543	618	704	806	925
8.00%	477	543	618	704	806

Source: Masterplast, MKB

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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

https://www.bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/MKB_Bank_Zrt._-_Masterplast_elemzoi_kommentar_-_2018.01.17..pdf1

https://www.bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/MKB_Bank_Zrt._-_Masterplast_elemzoi_kommentar_-_2018.02.28..pdf1

https://bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/MKB_Bank_Zrt._-_Masterplast_Nyrt._negyedeves_elemzes_-_2018.03.09..pdf1

https://bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/MKB-Bank-Ltd-Masterplast-flash-note-20180323

https://bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/MKB-Bank-Ltd-Masterplast-flash-note-20180327

https://bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/mkb-bank-ltd-masterplast-plc.-quarterly-update-20180518

https://bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/mkb-bank-ltd-masterplast-flash-note-20180614

https://bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/mkb-bank-ltd----masterplast-flash-note---2018-08-01

https://bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/mkb-bank-zrt.---masterplast-nyrt.-negyedeves-elemzes---2018.08.29.

https://bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/mkb-bank-ltd-masterplast-flash-note-20180921

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https://bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/mkb-bank-ltd--masterplast-flash-note-20181030

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 775, but the changes in fundamental factors justified the update of our model. Our new price target is HUF 805.