## RECORD EARNINGS IN THE FIRST QUARTER OF 2022

ALTEO (the "Company") reported 2022 Q1 earnings on 16 May 2022. In a nutshell the Company's EBITDA increased by 101% year over year and reached HUF 4.6 billion in the first quarter of the year. The revenue grew by 101% also from HUF 9.5 billion to HUF 19.1 billion in the first quarter.

The main driver behind the growth was the rising energy prices, the volume increase of the energy trading segment; the increasing capacity and revenue of the Alteo Control Center (virtual power plant or "VPP") and the weather impact on the weather related portfolio. Nowadays the Company's renewable segment's capacity is approximately 65-70 MW and the market-based segment also reached cca. 70 MW.

### Results by segments

| million HUF | 2021 Q1 | 2022 Q1 | Δ |
|---|---|---|---|
| **Thermal/heat and electricity production (market based)** | 4419 | 12591 | 185% |
| **Electricity production (KÁT system)** | 1277 | 1654 | 30% |
| **Energy services** | 687 | 850 | 24% |
| **Energy trading** | 3819 | 6179 | 62% |
| **Other** | 0 | 0 | 0% |
| **Revenue** | **9484** | **19066** | **101%** |
| | | | |
| **Thermal/heat and electricity production (market based)** | 1103 | 2939 | 166% |
| **Electricity production (KÁT system)** | 1090 | 1360 | 25% |
| **Energy services** | 68 | 12 | -82% |
| **Energy trading** | 224 | 517 | 131% |
| **Other** | -182 | -212 | -16% |
| **EBITDA** | **2302** | **4616** | **101%** |
| | | | |
| **EBITDA margin** | | | |
| **Thermal/heat and electricity production (market based)** | 25,0% | 23,3% | -1,6% |
| **Electricity production (KÁT system)** | 85,4% | 82,2% | -3,1% |
| **Energy services** | 9,9% | 1,4% | -8,5% |
| **Energy trading** | 5,9% | 8,4% | 2,5% |

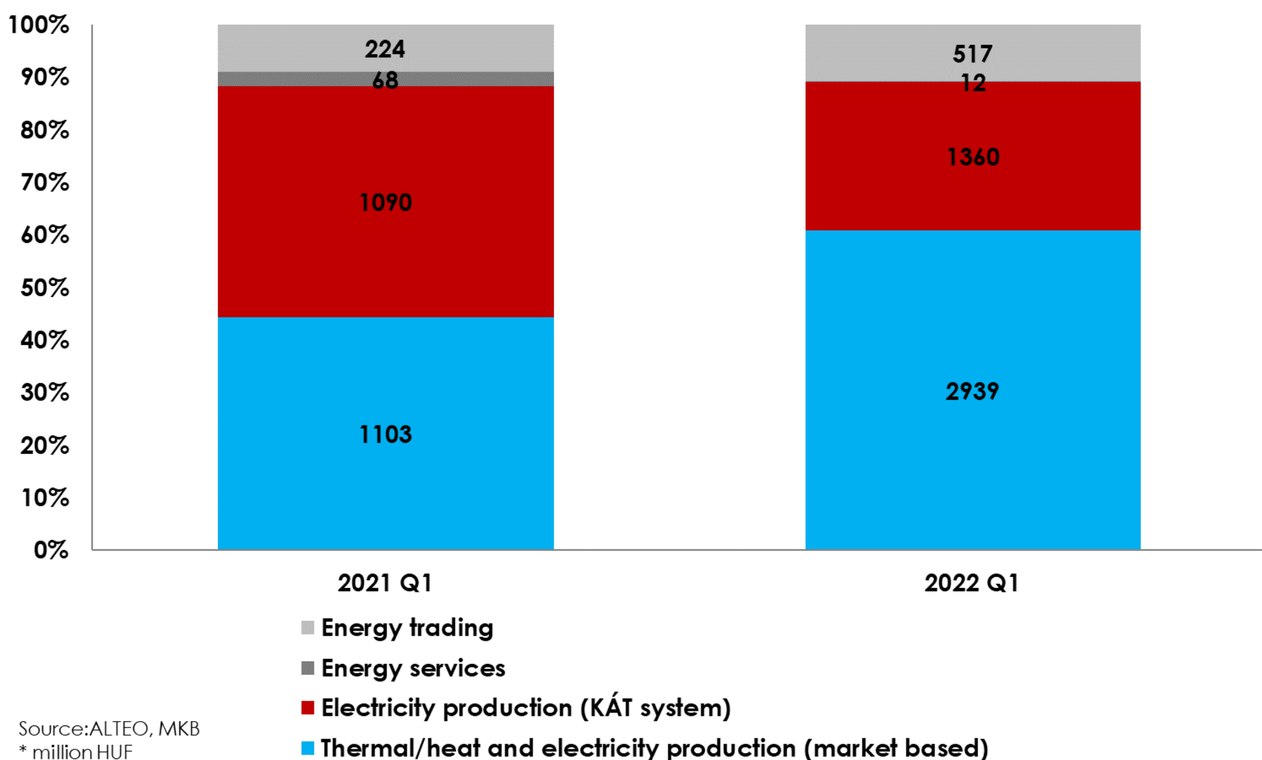
Source: ALTEO, MKB

## RESULTS BY SEGMENTS

Production of heat/thermal and electricity (market based): the revenue and the EBITDA increased by 185% and 166% year over year thanks to the capacity market revenue, the rise of the balancing prices and the regulatory revenue (both of them are high margin activities).

In recent years some wind power plant and hydropower systems has been integrated into the Alteo Control Center, which exhausted the electricity production in the KÁT system, and this process will continue in the future.

The costs grew too thanks to the higher gas prices, the higher CO2 quotas but these items are dwarfed by the high margin activities like the capacity market, the balancing prices and the forecasting service. Moreover, the material expenses increased at lower rate than the sales revenue which indicates that significant amount of the revenue and EBITDA comes from the high margin activities.




Electricity production (KÁT system): the revenue increased by 30% while the EBITDA increased by 25% year over year in the first quarter of 2022. The segment grew mainly due to the windier weather at the beginning of the year. Except the wind power plants the segment sales and EBITDA volume matched with the previous year's.

Energy services: The revenue grew by 24% but the EBITDA decreased by 82%. The energy services' EBITDA from the self-implemented projects was HUF 0, so all of the EBITDA was realized through services to third parties.

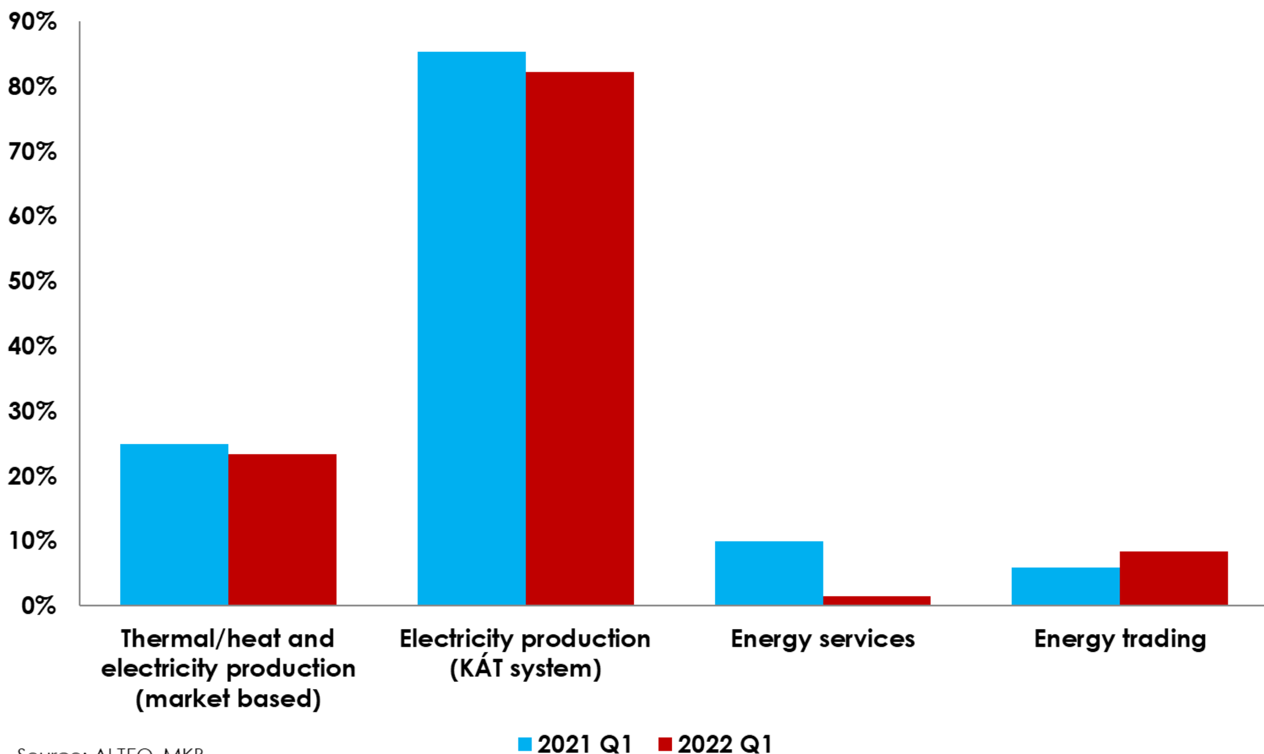
The revenue decreased due to the lower construction works for third parties. The revenue from maintenance services for third parties was the same as the previous year.

The waste management segment didn't show significant increase compared to the last comparable period. This is largely due to the effect of the recent pandemia.

The profit of the E-mobility segment matched with the management's expectations. But it is worth noting that both of these segments are not yet significant.

Energy trading: The revenue and EBITDA increased by 62% and 131% year over year in the first quarter of 2022. The electricity trading was impacted positively by the rising electricity prices, but on the other side the Company didn't renew the contrcts of the riskiest consumers.

The gas trading segment benefited from the reduction of the gas supply competitors.




Source: ALTEO, MKB

## OTHER COMPANY RELATED ANNOUCEMENTS

On 21 April 2022 the Company informed the shareholders that the Board of Directors of the Company approved the 2024 and 2025 Remuneration Policy of the ALTEO Employee Share Ownership Organization. Based on this approval the Board of Directors decided to issue a total of 545.200 New Shares.

It is worth nothing that the remuneration may be paid in the event of an improvement in the Company's economic performance between 31 December 2021 and 31 December

2023. In the case of the failure of the Company's economic improvement the renumeration will be failed. So the above mentioned new issuance is approximately 3% of the existing shares which is also linked to a specific improvement. We think sahre dilution can be minimal so the annousement as a whole is neutral.

On 2 May 2022 the Company announced that will pay HUF 103 dividend after the business year of 2021. The dividend rate is higher what investors got in the past years. At the same time we continue to belive that the story of ALTEO is a growth story so we don't want value the Company based on the dividend. Valuing an utility company on dividend is a self-evident assumption, but in the case of ALTEO not yet. Recent years we have seen how fast changed the utility market and the position of various companies.

## CONCLUSION

We think the Company's growth, environment and operations have reached a new level. Last time we refreshed our DCF-model on 1 March 2022. We think the management's strategy is echoed in our last two DCF-models.

To take into consideration the recent company specific, economic and geopolitical events we refresh our DCF-model again. We had to raise the risk-free rate, adjusted the cost of capital and the Company's net debt. We calculated the expected impact of the share dilution if the above mentioned specific economic improvement fully implemented.

Moreover, we believe the recent situation (the Russo-Ukrainian war and the energy market turbulence) positively affected the Company, which can be seen in the recent earnings report too. The higher gas and electricity prices mean that the margin of the renewable power plants may improve but at the same time the maintenance cost of these power plants won't change significantly. At the same time the spark spread (the difference between the electricity price and the cost of natural gas) has widened significantly which means the market-based segment reached extraordinary profits. Based on the above we slightly changed the financial assumptions for this and the next year.

Other assumptions of the model remained unchanged. See our flash note on 23. November 2021 an on 01. March 2022 on the website of the Budapest Stock Exchange.

Based on the above we slightly raise our one-year target price from HUF 2259 to HUF 2423. Our recommendation is neutral.

| | | Total Equity Value<br>Terminal EBITDA Multiple | | |
|---|---|---|---|---|
| | | 5,4x | 6,4x | 7,4x |
| **Discount** | 6,1% | **36 841** | **46 282** | **55 724** |
| **Rate** | 8,1% | **32 001** | **40 601** | **49 200** |
| **(WACC)** | 10,1% | **27 669** | **35 515** | **43 361** |

| | | One Year Target Price<br>Terminal EBITDA Multiple | | |
|---|---|---|---|---|
| | | 5,4x | 6,4x | 7,4x |
| **Discount** | 6,1% | **2199** | **2762** | **3326** |
| **Rate** | 8,1% | **1910** | **2423** | **2936** |
| **(WACC)** | 10,1% | **1651** | **2120** | **2588** |

Source: ALTEO, Bloomberg, MKB

| million HUF | **2022** | **2023** | **2024** | **2025** | **2026** |
|---|---|---|---|---|---|
| **EBITDA** | 15541 | 12090 | 11131 | 12090 | 12672 |
| **D&A** | 4177 | 5397 | 6617 | 7746 | 7858 |
| **Capex** | -10000 | -10000 | -10000 | -6971 | -7072 |
| **FCFF** | 2121 | -746 | -1433 | 2576 | 2997 |
| **Terminal value** | 81099 | | | | |
| **WACC** | 8,06% | | | | |
| **Net Debt** | 18548 | | | | |

Source: ALTEO, Bloomberg, MKB

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**Change from the prior research**

Our first research was published on 15. December 2017. In that Initial Coverage our price target was HUF 823. The changes in fundamental factors and the operation in the Company required regular updates of our model and the target price. Based on the recent changes, we have revised our target price, the new target price is HUF 2423, which is 7.2% higher than the previous target price of HUF 2249 (01 March 2022).

**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://bet.hu/Kibocsatok/BET-elemzesek/elemzesek/alteo-elemzesek

MKB Bank wrote flash notes on 12 January 2018, and on 31 January 2018, 8 February 2018, 2 March 2018, 19 March 2018 and 11 May 2018. These researches are available on the web page of the BSE (Budapest Stock Exchange):

https://bet.hu/Kibocsatok/BET-elemzesek/elemzesek/alteo-elemzesek

**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.