
RECORD EARNINGS IN THE FIRST QUARTER OF 2023

ALTEO (the “Company”) reported 2023 Q1 earnings on 15. May 2023. In a nutshell the Company’s EBITDA increased by 70% year over year and reached HUF 7.84 billion in the first quarter of 2023. The revenue grew by 89% also from HUF 19.06 billion to HUF 36.06 billion.

The main driver behind the revenue growth was the rising energy prices; the electricity and district heating prices which were fixed at higher levels; the increasing capacity and revenue of the ALTEO Control Center (virtual power plant or “VPP”) and the development of the waste management segment.

It’s worth noting, that the Company has made several acquisitions in the last years. If you would like to find more, please read our previous flash notes on the website of the Budapest Stock Exchange.

From the earnings report of 2022 Q3 ALTEO has changed the classification of the Company’s segments. The classification of the Energy services and Energy trading segments remain the same. At the same time the electricity and heat production has changed based on their operation. Until now the Production of heat/thermal and electricity (market based) segment contained the fossil fuel based power plants, the renewable power plants which exhausted their subsidizing system, the VPP (Virtual Power Plants), energy storage facilities and other complex services. The Electricity production (KÁT system) segment contained the renewable power plants which are operating under KÁT or METÁR (subsidized system).

From now the (new) Renewables-based electricity production segment shows the energy generations from renewable sources, while the (new) Non-renewables-based heat and electricity production and management segment contains the earnings of the conventional power plants (fossil-fuel based), the energy storage facilities, heat production and other complex services, like scheduling services.

In line with the above, we also changed the presentation of the segments which are not comparable with the previous analyses.

Results by segments

million HUF	2022 Q1	2023 Q1	Δ
Non-renewables heat and electricity production and management	12591	29749	136%
Renewables-based electricity production	1654	1295	-22%
Energy services	754	1166	55%
Energy trading	6179	5739	-7%
Waste management	96	928	867%
Other	0	3	NA
Revenue	19066	36056	89%
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Non-renewables heat and electricity production and management	2961	5946	101%
Renewables-based electricity production	1373	803	-42%
Energy services	0	154	NA
Energy trading	508	1173	131%
Waste management	-15	-36	140%
Other	-212	-198	-7%
EBITDA	4616	7840	70%
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EBITDA margin			
Non-renewables heat and electricity production and management	23,5%	20,0%	-3,5%
Renewables-based electricity production	83,0%	62,0%	-21,0%
Energy services	0,0%	13,2%	13,2%
Energy trading	8,2%	20,4%	12,2%
Waste management	-15,6%	-3,9%	11,7%

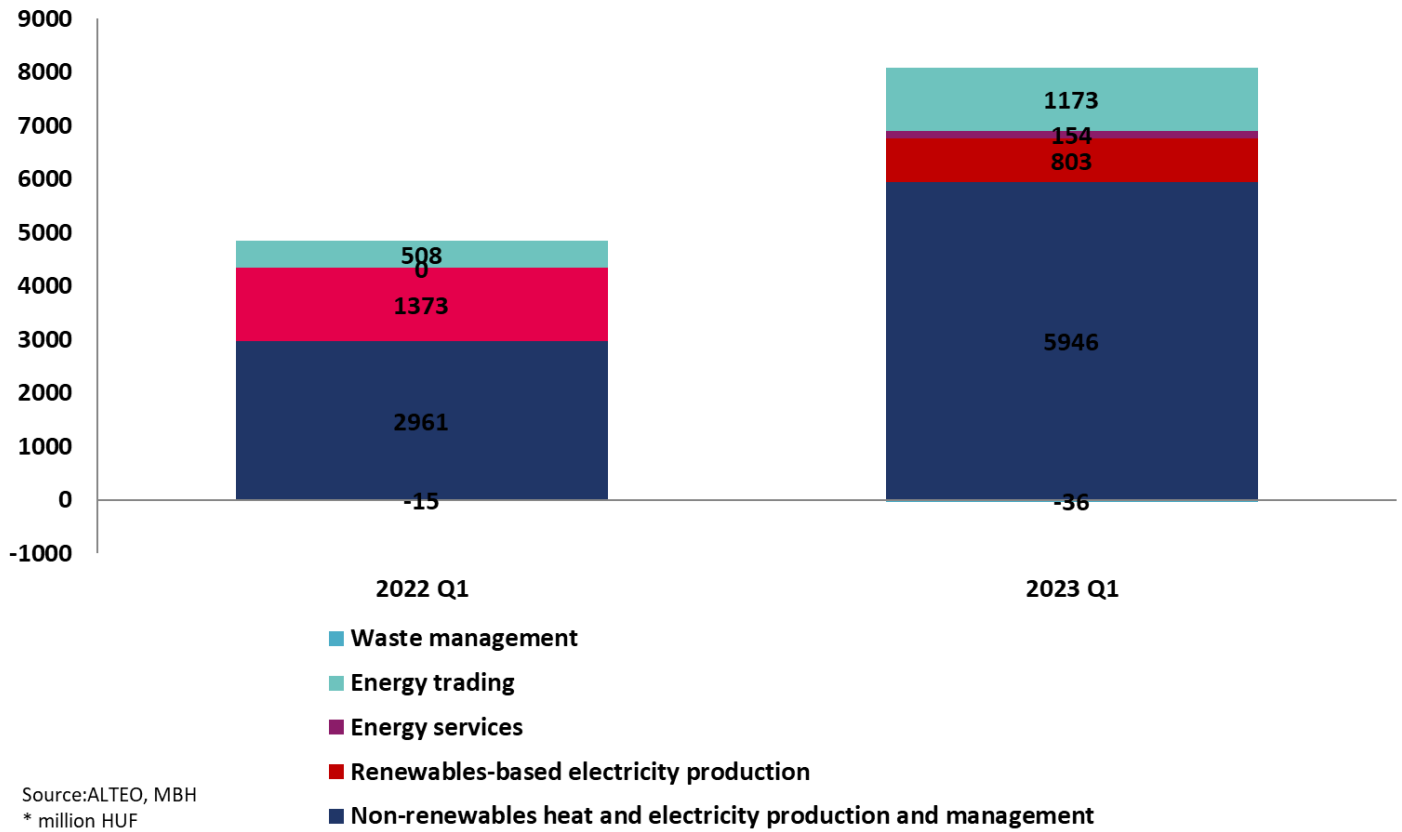
Source: ALTEO, MBH

Results by segments

Non-renewables-based heat and electricity production and management: the revenue and the EBITDA increased by 136% and 101% 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) and the higher electricity prices coupled with higher spark spread (the difference between the gas price used to produce electricity and electricity price).

The segment's costs grew too due to the higher gas prices and the higher CO2 quotas but high margin activities like the capacity market, the balancing prices and scheduling services contributed to the segments' growth.

EBITDA by segments



Renewables-based electricity production: the revenue decreased by 22% while the EBITDA decreased by 41% year over year in the first quarter of 2023. The segment's EBITDA margin was being under pressure because of the higher scheduling cost and the volatile weather, like calm windy wheater and the lower average hours of sunny days.

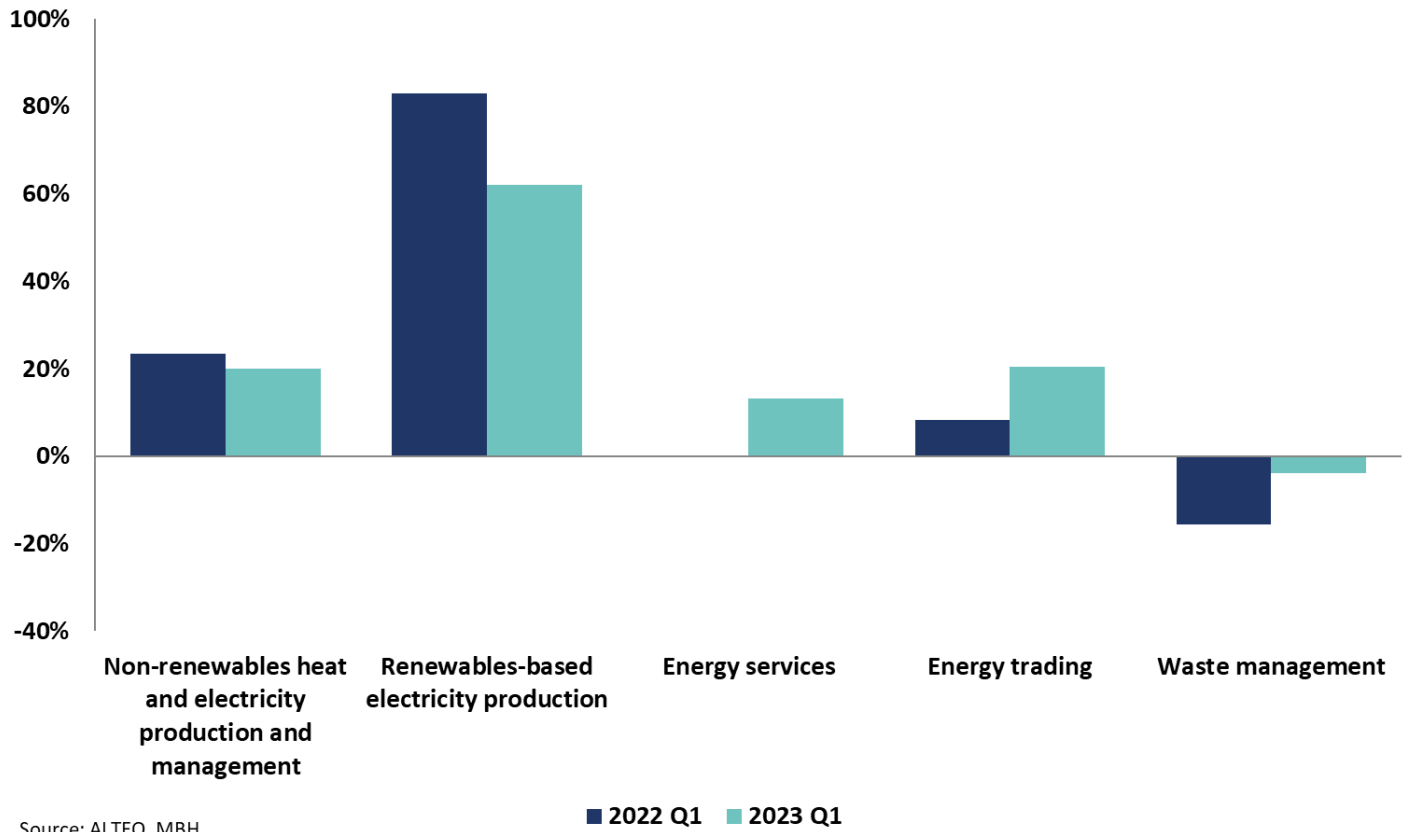
Energy services: The revenue grew by 55% year over year. The EBITDA grew significantly, from HUF 0 to HUF 154 million because of the higher earnings from third party services.

Waste managment: From now the Waste management segment will be presented as a standalone segment. The revenue grew by 868% year over year from HUF 96 million to HUF 928 million. At the same time the EBITDA margin is still negative. According to the management the ALTEO could be a subccontractor to MOL in this segment.

Energy trading: The revenue decreased by 7%, while the EBITDA increased by 131%. The electricity trading was impacted positively by the rising electricity prices (prices were fixed at higher levels), but on the other side the Company didn't renew the contracts of the riskiest consumers.

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

EBITDA margin of the ALTEO Group



Conclusion

Last time we refreshed our DCF-model on 21 February 2023 because of the recent company specific, economic and geopolitical events. At the same time, we think the management's strategy is echoed in our last DCF-models.

Moreover, we believe the recent situation (the Russo-Ukrainian war and the energy market turbulence) positively affected the Company, which could be seen in the last few earnings reports 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.

But one can identify several risk factors. The energy market turbulence is over, at least temporarily. It is a tough task to see the electricity market in the next 5-10 years, which affect the Company's revenue (and earnings) to a large degree. In the last year the monetary and financial environment is changed a lot, too. This has made the external source of capital more expensive (in relative term), which could significantly raise the average cost of capital (WACC) in the future. Thanks to the monetary tightening the financial conditions

become more strictly, which affect the model's discount factor too. (Please note the valuation effect of the change in WACC in the target price scenario's matrix).

Moreover, nowadays the Company has an elevated cash balance which in one hand is the result of the improved net working capital. In the era of higher commodity prices, the financing needs like purchase of gas to operate the gas power plants was a tough and expensive process. We think the cash balance and the net working capital can show a volatile path, which strongly affects the Company's fair value. But now the elevated cash balance means higher interest income.

Currently it is a difficult task to see the Company's near future on the stock market so every possible future scenario (the Company remains public company or becomes private?) can only be predicted with a huge margin of error.

We are closely monitoring the events and we will refresh our research if it is justified.

In this research we raised our one year price target from HUF 3840 to HUF 4116.

		Total Equity Value		
		Terminal EBITDA Multiple		
		5,4x	6,4x	7,4x
Discount	7,5%	64 021	76 025	88 029
Rate	9,5%	58 017	68 964	79 912
(WACC)	11,5%	52 643	62 643	72 643
		One Year Target Price		
		Terminal EBITDA Multiple		
		5,4x	6,4x	7,4x
Discount	7,5%	3 821	4 537	5 254
Rate	9,5%	3 463	4 116	4 769
(WACC)	11,5%	3 142	3 739	4 336

Source: ALTEO, Bloomberg, MBH

million HUF	2023	2024	2025	2026	2027
EBITDA	21439	18815	18241	17756	17225
D&A	4097	4797	5797	6568	7278
Capex	-7000	-10000	-7717	-7098	-6550
FCFF	-4557	-3817	2190	2758	4081
Terminal value	110240				
WACC	9,49%				
Net Debt	-68				

Source: ALTEO, Bloomberg, MKB



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- **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 review:** If new information comes to light, which is expected to change the valuation significantly.

7. 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 revised our target price, so the target price is HUF 4116, which is 7 percent higher than the previous target price of HUF 3840 (21 February 2023).

Prior researches

MBH 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/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/MKB-Bank-Alteo-initiation-report-20171215.pdf>

The flash notes are available on the web page of the BSE (Budapest Stock Exchange):

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14. The valuation procedures used:

Discounted cash flow valuation

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 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 reduce the EV with the net debt. This figure 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).