ALTEO price target update – Flash note

13 March 2024

DCF-model update after FY 2023

ALTEO (the "Company") reported FY 2023 earnings on 29 February 2024. In a nutshell the Company's EBITDA decreased by 4% compared to a year ago and reached HUF 19.4 billion in 2023 compared to HUF 20.2 billion in 2022. The revenue declined by 4% too, from HUF 103 billion to HUF 98.9 billion.

The main driver behind the decreasing revenue was that the electricity prices decreased and stabilized in a lower level which had a negative effect on the electricity production and the energy trading segment. At the same time the development of the waste management segments could partially offset these negative effects.

The cost of sales increased because of the higher amortization cost due to the higher level of assets and the staff costs were rising too.

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.

After the closed FY 2023 we refreshed our DCF model, based on the ongoing company, economic and geopolitical specific events.

It is already known fact that the energy chaos of 2022 (and partly in 2023) has positively affected the Company's earnings. The higher gas and electricity prices have meant that the margin of the renewable power plants, outside the subsidy system, improved and the energy contracts which were fixed at higher price level contributed to better revenue and margins. The spark spread (the difference between the electricity price and the cost of natural gas) has widened too which means the market-based segment reached extraordinary profit.

The revenue from the scheduling of renewable power plants for third party customers, the capacity market and balancing activity (the regulatory revenue) were growing, which is a low cost/high profit margin segment. At the same time the capacity and balancing prices follow the trend of the market price of the electricity, which has been in a downtrend in the recent quarters. This has a negative effect on the EBITDA of the market-based segment (the capacity and balancing activity is part of the market-based segment).

The energy chaos had some negative effects on the daily operation too which affected the Company's valuation. The need for working capital raised significantly mostly due to the higher gas prices, the prepayments, etc.

We believe that in the near future the commodity and electricity prices will normalize. Several researches are predicting that the prices will return to the pre-Covid and pre-war levels. Of course, taking into consideration the times behind us, this can be questioned, because it is a tough task to see the electricity market in the next 5-10 years, which affects the Company's fundamental.
We see the early runup of the waste management business, thanks to the MOL (MOHU) contract. 2 years ago, we thought the segment's EBITDA will be much lower than we see today.

The path of the capital expenditures - the investment pipeline - in the next 3-5 years will be very important, because it will be the basis of the future profit growth and/or margin expansion.

The interest rate environment has changed since our last model update. The risk-free rate and the equity risk premium became lower so the average cost of capital of the Company, too.

Our one-year target price has not changed significantly at all. Based on the above our new one-year price target is HUF 4000, our recommendation is buy.

million HUF	2024	2025	2026	2027	2028
EBITDA	18158	17328	17442	18942	20442
D&A	4938	5558	6558	7408	8217
Capex	-10000	-8502	-8090	-9667	-8895
FCFF	3918	6919	5348	7522	5735
PV of FCFF	22384				
PV of TV	49613				
WACC	9,36%				
Net Debt	2287				

Source: ALTEO, Bloomberg, MBH

		Total Equity Value		
		Long term growth rate		
		0%	2%	4%
Discount	7,4%	**76 030**	**95 472**	**139 781**
Rate	9,4%	**59 284**	**69 710**	**88 992**
(WACC)	11,4%	**48 414**	**54 726**	**65 129**

		One Year Target Price		
		Long term growth rate		
		0%	2%	4%
Discount	7,4%	**4 363**	**5 479**	**8 022**
Rate	9,4%	**3 402**	**4 000**	**5 107**
(WACC)	11,4%	**2 778**	**3 141**	**3 738**

Source: ALTEO, Bloomberg, MBH

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Closing the research: 16:00 12/03/2024

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- **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 4000, which is 0.025 percent lower than the previous target price of HUF 4001 (16 November 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 Exc hange): https://bet.hu/pfile/file?path=/site/Magyar/Dokumentumok/Tozsdetagoknak/Tozsdetagok-elemzesei/MKB-Bank-Alteo-initation-report-20171215.pdf
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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).