SUMMARY

ALTEO (the "Company") reported first half earnings on 2 September 2019. The Company's revenue grew by 38%, while EBITDA increased by 127%. The main driver in the revenue growth was the higher electricity and gas trading, the growth of the electricity production (both in the market based and KÁT segment) and the increased volume of the energy services. During the first half of the year the Company implemented several investments. The capacity of the renewable segment reached approximately 50 MW (the market based segment has the same capacity).

ALTEO acquired 100% of the EURO GREEN ENERGY Ltd. EURO GREEN ENERGY which is operating 13 wind turbines unites near Böny. The total electricity production capacity of the power plant is 25 MW, which is sold through the KÁT system by 2023. The power plant is able to produce approximately 58,000-60,000 MWh of electricity annually.

Two solar power plants (Balatonberény and Nagykőrös) started their operation in July, in line with our projection. The power plants have a capacity of approximately 14 MW (7-7MW respectively). The power plants will sell the produced electricity in the KÁT system for 25 years. Both of the power plants were implemented as the Company's own construction.

Early 2019 the Company launched its Waste Management division inside the Energy Production and Energy Services segment. The new division will be the third profit center next to the energy production and energy services in this segment. In the second quarter ALTEO bought 66.6 percent of the ECO-FIRST Hulladék Kereskedelmi KFT. ECO-FIRST was established in 2017 and the main service of the company is the collection of garbage, such as expired food from grocery stores which can be utilize in the Company's operated biogas power plant(s).

The Company implemented an R&D project for energy storage in the amount of HUF 1.1 billion. HUF 500 million of that was government subsidy. As a result the Company is able to earn revenue from the primary control of the electricity system.

In the first half of the year the Company made an equity offering (HUF 2 billion) and a bond issuance (HUF 1.7 billion) to finance its further expansions.

On the bottom line the net profit grew by 37 percent from HUF 352 million to HUF 483 million, while the EPS rose from HUF 21.45 to HUF 26.89.

According to our DCF model and the expected investments, our recommendation is buy, with a one year target price of HUF 1049.

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RESULTS BY SEGMENTS

Production of heat/thermal and electricity (market based): the revenue grew by 33% (from HUF 4.93 billion to HUF 6.57 billion) and the EBITDA increased by 125% YoY (from HUF 502 million to HUF 1132 million). The main driver in the revenue growth was the operation of the Zuglo-Therm power plant and the energy storage project which has been in operation since April 2018. Moreover the costs of sales just grew by 19 percent, less than the revenue, which can be translated to higher EBITDA margin.

The segment has higher CO2 costs due to the integration of the Zuglo-Therm. The Company expects further growth in the price of the CO2 quotes. The Company intends to enter into options and forwards contracts to hedge.

Furthermore the Control Center (to learn what is Control Center please see Initiation Report page 6-7) could integrate the wind power systems which exhausted the electricity production in the KÁT system and were reclasiffied into the market based production segment.

The wind power plants are operating efficiently in tandem with gas-fired power plants due to the volatility of the weather. So it is crucial to implement the power plants in the VPP (Control Center). The wind power plants have very low raw material costs and the price of electricity is increasing.

Electricity production (KÁT system): the revenue grew by 134% while the EBITDA grew by 159% YoY. The main drivers behind the growth were the implementations of the new renewable projects: three solar power plants (Monor in the end of 2018 and Balatonberény and Nagykőrös in the summer of 2019) and the acquisition of the EURO-GREEN Energy Ltd. which is operating 13 wind power turbine near Bőny with 25MW capacity. So the Company renewable capacity reaches approximately 50MW.

The semgent was not helped by the exhaustion of the KÁT system of three wind turbines and the water power plant near Gibárt.

This segment has the highest EBITDA margin approximately 65-80%. In the future the solar and wind power plants can improve the earnings of this segment.

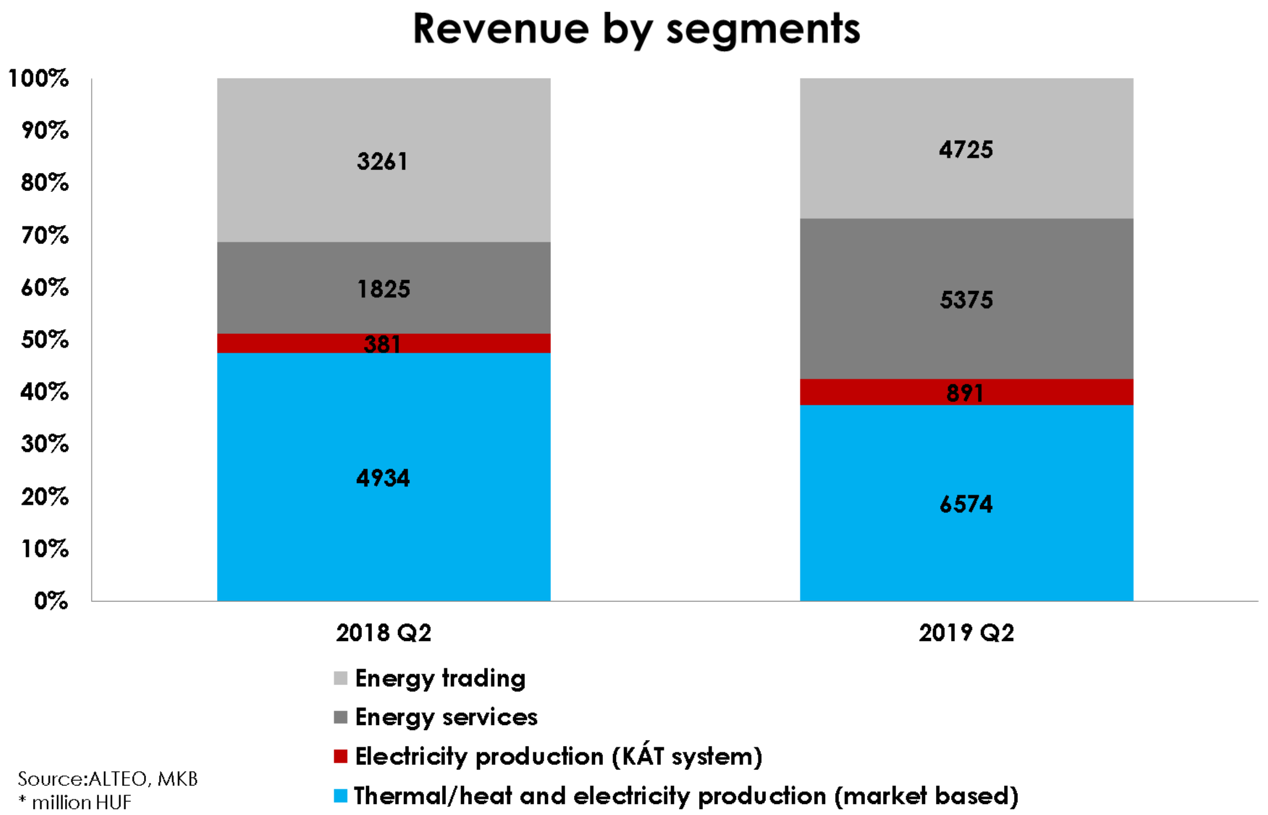
Energy services: the segment's revenue increased by 194% and the EBITDA increased by 89%, (from HUF 594 million to HUF 1122 million). In 2018 and 2019 the Company has focused more on their own solar projects. The segment's internal profits are eliminated which means better rerutns on the own pojects. But the same time the volume of the maintenance services for third party also grew significantly.

Energy trading: in this segment the revenue grew by 45% (from HUF 3261 million to HUF 4725 million), because the electricity sales segment has gained market share. The EBITDA of the segment grew by HUF 60 million to HUF 236 million.

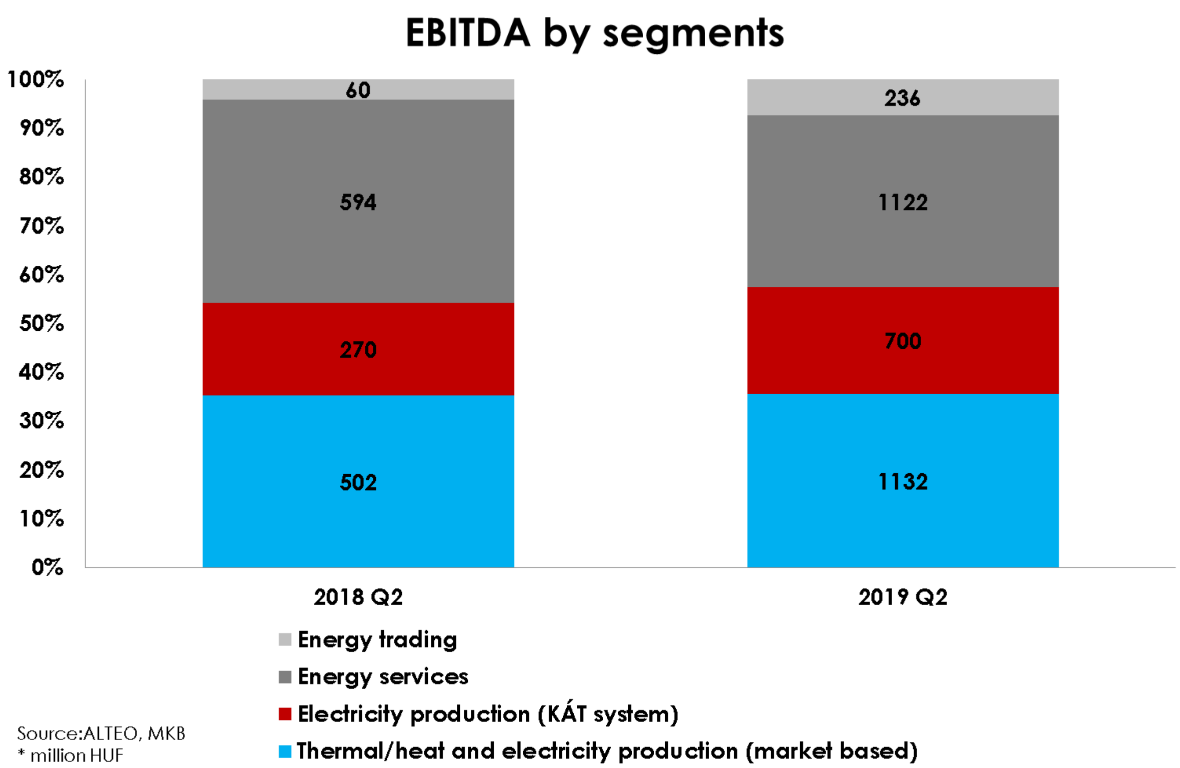
Results by segments

million HUF	2018 Q2	2019 Q2	Δ
Thermal/heat and electricity production (market based)	4934	6574	33%
Electricity production (KÁT system)	381	891	134%
Energy services	1825	5375	195%
Energy trading	3261	4725	45%
Other	167	201	20%
Revenue	**5191**	**6494**	**25%**
Thermal/heat and electricity production (market based)	502	1132	125%
Electricity production (KÁT system)	270	700	159%
Energy services	594	1122	89%
Energy trading	60	236	293%
Other	-453	-349	NA
EBITDA	**936**	**2123**	**127%**
EBITDA margin			
Thermal/heat and electricity production (market based)	10,2%	17,2%	7,0%
Electricity production (KÁT system)	70,9%	78,6%	7,7%
Energy services	32,5%	20,9%	-11,7%
Energy trading	1,8%	5,0%	3,2%

Source: ALTEO, MKB



Source:ALTEO, MKB
* million HUF



Source:ALTEO, MKB
* million HUF

CONCLUSION

The reported earning is in line with our expectations, so we don't change our DCF model. Our 12 month target price is HUF 1049.

million HUF	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019E	2020E	2021E	2022E	2023E
EBITDA	-88	401	453	591	816	719	1428	2312	1806	1828	3229	4365	4463	4564	3906
D&A	9	186	166	291	420	404	950	829	563	798	1244	1538	1538	1538	1538
Capex	-1432	-832	-686	-652	-237	-181	-206	-152	-1950	-9400	-7000	-3000	-1064	-1064	-1064
FCFF									-49	-7151	-3469	862	3284	2972	2797

Source: ALTEO, Bloomberg, MKB

		Total Equity Value		
		Terminal EBITDA Multiple		
		5x	6,5x	8x
Discount	4%	**16 058**	**20 930**	**25 802**
Rate	6%	**14 049**	**18 477**	**22 906**
(WACC)	8%	**12 250**	**16 282**	**20 314**
		One Year Target Price		
		Terminal EBITDA Multiple		
		5x	6,5x	8x
Discount	4%	**912**	**1188**	**1465**
Rate	6%	**798**	**1049**	**1300**
(WACC)	8%	**695**	**924**	**1153**

Source: ALTEO, Bloomberg, MKB

DISCLAIMER

possession of all the relevant information, therefore investors are hereby explicitly advised to read carefully the information material, contractual provisions, conditions list and general business terms in order to be able to decide if the investment is in line with their risk bearing capacity. MKB Bank also recommends collecting information about the tax consequences and other relevant laws concerning investment services in the financial instruments mentioned in this document.

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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://bet.hu/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/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.

Change from the prior research

Our first research was published on 05. December 2017. In that Initial Coverage our price target was HUF 823, but the changes in fundamental factors and the latest acquisition justified the update of our model. Our new price target is HUF 970 which is higher by 18% than our first price target.