ALTEO Energiaszolgáltató Nyrt
Hungary, Utilities

BBB- STABLE

Key metrics

			Scope estimates	
Scope credit ratios	**2022**	**2023**	**2024E**	**2025E**
Scope-adjusted EBITDA interest cover	>20x	Net interest	>20x	6.1x
Scope-adjusted debt/EBITDA	0.6x	0.2x	1.5x	2.8x
Scope-adjusted free operating cash flow/debt	98%	420%	11%	-6%
Liquidity	>200%	>200%	>200%	>200%

Rating rationale

The affirmation reflects our view that ALTEO will be able to withstand pressure on its credit metrics stemming from rising debt levels due to increased expansion capex, as these should be largely offset by the associated growth in EBITDA. Furthermore, the rating is also supported by the addition of new renewable capacities, as well as new revenue streams from waste management and maintenance services.

Outlook and rating-change drivers

The Stable Outlook reflects the expectation that ALTEO’s financial position will remain solid in the context of its expansion strategy as reflected by a medium-term leverage (Scope-adjusted debt/EBITDA) settling between 1.5-3.0x and an EBITDA interest coverage of around 6-5x. The Stable Outlook also reflects a largely unchanged shareholder structure.

A positive rating action is considered unlikely in the foreseeable future, given the company's limited size and reach.

A negative rating action could be warranted if the execution of the company's growth strategy or its operating performance led to a deterioration of its financial risk profile, as indicated by a Scope-adjusted leverage above 4.0x or a Scope-adjusted EBITDA coverage below 4.0x on a sustained basis.

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
27 May 2024	Affirmation	BBB-/Stable
22 Jun 2023	Upgrade	BBB-/Stable
12 Dec 2022	Under Review placement	BB+ under review for a possible upgrade
04 Oct 2022	Affirmation	BB+/Stable
30 Jun 2022	Affirmation	BB+/Stable
29 Jul 2021	Affirmation	BB+/Stable

Ratings & Outlook

Issuer	BBB-/Stable
Short-term debt	S-2
Senior unsecured debt	BBB-

Analyst

Kamila Hoppe
+49 30 27891 405
k.hoppe@scoperatings.com

Related Methodologies and Related Research

General Corporate Rating Methodology; October 2023

European Utilities Rating Methodology; March 2023

ESG considerations for the credit ratings of utilities; April 2021

Scope Ratings GmbH

Lennéstraße 5
10785 Berlin

Phone +49 30 27891 0
Fax +49 30 27891 100

info@scoperatings.com
www.scoperatings.com

Bloomberg: RESP SCOP

Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• A gradually growing and solidly balanced energy generation portfolio of regulated renewable generation capacity with a remaining regulatory life of around nine years, as well as non-regulated renewable energy and thermal generation capacity. • Ability to provide reserve capacity, which provides cash flow upside from the provision of balancing services, through the operation of gas-fired power plants and a 'virtual power plant' across Hungary, including volatile renewables and peak-load gas-fired power plants (ESG factor: credit-positive environmental factor). • Exposure to quasi-monopolistic heat generation and supply. Integrated business model covering generation, supply, energy and waste management services. • Integrated business model covering generation, supply, complemented by energy and waste management services • New business opportunities thanks to cooperation with MOL, ALTEO's new shareholder from 2023. • Strong financial ratios in terms of leverage and debt protection, together with a solid liquidity profile	• Small, niche energy supplier with insignificant share of the Hungarian power generation and energy supply markets • Almost all business exposure to Hungary for the foreseeable future, which could create regulatory risks for regulated renewable capacity under the KÁT and METAR systems • Margin dilution from supply and energy services and no new capacity included in tariff system • Higher regulatory risks in Hungary than in other Western European markets (e.g. Robin Hood tax on utilities, new solar tax, new balancing tax) • Weakening of debt protection metrics (EBITDA interest coverage) due to the significant increase in gross financial debt, which carries much higher interest rates on average than in the past.

Positive rating-change drivers	Negative rating-change drivers
• Considered remote given the company's medium-term size and reach	• Leverage deteriorating above 4.0x or Scope-adjusted EBITDA interest coverage dropping below 4.0x on a sustained basis

Corporate profile

ALTEO is an integrated utility with activities in regulated and non-regulated power generation, energy supply (electricity and gas), a diversified business profile with waste management and energy services. The company has grown strongly through a multi-billion HUF investment plan focused on organic growth and opportunistic acquisitions.

Financial overview

			Scope estimates		
Scope credit ratios	**2022**	**2023**	**2024E**	**2025E**	**2026E**
Scope-adjusted EBITDA interest cover	53.6x	Net interest	20.8x	6.1x	4.8x
Scope-adjusted debt/EBITDA	0.6 x	0.2x	1.5x	2.8x	3.0x
Scope-adjusted free operating cash flow/debt	98%	420%	11%	-6%	-2%
Scope-adjusted EBITDA in HUF '000s					
Reported EBITDA	20,220,628	19,431,572	17,410,200	24,123,600	36,079,640
One-off items[1]	1,057,645	223,232	755,837	1,152,169	1,238,068
Scope-adjusted EBITDA	**21,278,273**	**19,654,804**	**18,166,037**	**25,275,769**	**37,317,708**
Funds from operations in HUF '000s					
Scope-adjusted EBITDA	21,278,273	19,654,804	18,166,037	25,275,769	37,317,708
less: (net) cash interest paid	(397,065)	1,301,991	(872,773)	(4,114,381)	(7,725,285)
less: cash tax paid per cash flow statement	(2,913,444)	(3,120,515)	(2,860,000)	(3,651,000)	(4,703,000)
Other non-operating charges before FFO	-	-	-	-	-
Funds from operations (FFO)	**17,967,764**	**17,836,280**	**14,433,265**	**17,510,387**	**24,889,423**
Free operating cash flow in HUF '000s					
Funds from operations	17,967,764	17,836,280	14,433,265	17,510,387	24,889,423
Change in working capital	(17,004,930)	(1,728,295)	1,448,000	(1,910,000)	(996,000)
Non-operating cash flow	15,237,185	8,202,952	2,330,305	(78,231)	(1,125,241)
less: capital expenditure (net)	(3,595,223)	(10,034,376)	(15,161,800)	(19,844,800)	(24,578,800)
less: lease amortisation	391,600	530,566	-	-	-
Free operating cash flow (FOCF)	**12,996,396**	**14,807,127**	**3,049,770**	**(4,322,644)**	**(1,810,618)**
Net cash interest paid in HUF '000s					
Net cash interest per cash flow statement	361,449	(1,363,743)	784,000	3,968,000	7,517,000
add: interest component on operating leases	-	-	-	-	-
add: interest related to AROs	35,616	61,752	88,773	146,381	208,285
Net cash interest paid	**397,065**	**(1,301,991)**	**872,773**	**4,114,381**	**7,725,285**
Scope-adjusted debt in HUF '000s					
Reported gross financial debt	29,078,414	29,771,500	39,878,106	83,636,855	120,326,982
less: cash and cash equivalents	(16,465,328)	(24,345,080)	(10,893,265)	(12,593,690)	(10,730,107)
add: asset retirement obligations	941,417	1,235,039	1,775,456	2,927,625	4,165,693
less: derivatives/margining	(324,160)	(3,138,813)	(3,138,813)	(3,138,813)	(3,138,813)
Scope-adjusted debt (SaD)	**13,230,343**	**3,522,646**	**27,621,485**	**70,831,977**	**110,623,756**

[1] Includes share-based payments and asset retirement obligations (AROs)

Table of Content

Environmental, social and governance (ESG) profile[2]

Environment		Social		Governance	
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)		Labour management		Management and supervision (supervisory boards and key person risk)	
Efficiencies (e.g. in production)		Health and safety (e.g. staff and customers)		Clarity and transparency (clarity, quality and timeliness of financial disclosures, ability to communicate)	
Product innovation (e.g. transition costs, substitution of products and services, green buildings, clean technology, renewables)		Clients and supply chain (geographical/product diversification)		Corporate structure (complexity)	
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	

Legend

Green leaf (ESG factor: credit positive)

Red leaf (ESG factor: credit negative)

Grey leaf (ESG factor: credit neutral)

Virtual power plant enhances ALTEO's market position and cash flow profile

Our assessment of a positive environmental credit driver relates to ALTEO's combined operation of volatile renewable energy power plants, cogeneration, and storage facilities, which are operated individually but also as a combined 'virtual power plant' through the company's own Power Plant Control Centre. The virtual power plant is a technical and commercial solution that allows several small stand-alone power plants to enter the electricity and system services market as a single, large power plant, thereby implementing a very effective, flexible, and economical energy production technology. In this way ALTEO can meet outright demand and provide balancing capacity to the national grid operator, thereby supporting its credit quality in terms of market position, profitability, and cash flow.

No credit-negative aspects from Governance

ALTEO has implemented a Corporate Governance Practise based on the Corporate Governance Recommendations of the Budapest Stock Exchange. In addition, we highlight the newly implemented long-term incentives that have been set for ALTEO's Board of Directors. These incentives relate to (1) financial KPIs and (2) sustainability targets. As a result, we are more confident that ALTEO's operations will be managed in a prudent and conservative manner in the interest of creditors.

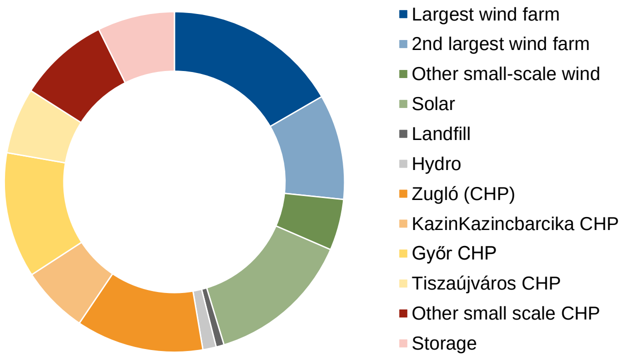
[2] These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Business risk profile: BB+

Asset growth amid substantial investment phase gradually reducing concentration risks

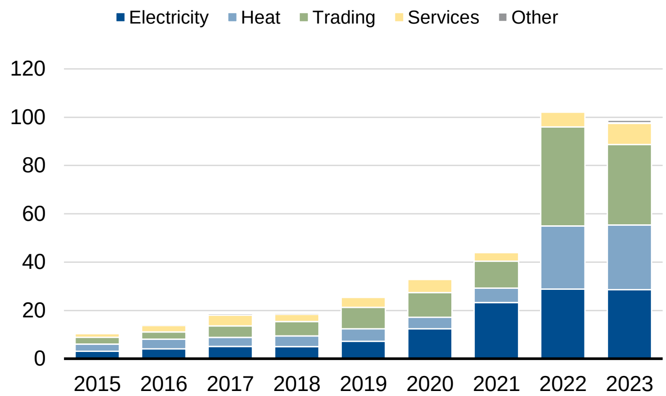
The rating continues to reflect a BB+ business risk profile assessment. While the assessment remains constrained by ALTEO's limited geographic reach and still comparatively small size, we expect the company's competitive position to be further strengthened as it enters an intensive investment phase over the next few years. The focus of the investment phase remains on the expansion of renewable capacity, battery storage and investment in conventional generation capacity, which would further reduce the concentration risks related to individual assets within the current power generation portfolio (~200MW_{th}). The 20 MW solar power plant (Edelyn Solar Kft.), which will be commissioned in Q2 2024, will already significantly increase the company's renewable generation portfolio to more than 90 MW. The company's consistently growing exposure to renewable energy generation capacity, combined with its ability to provide grid balancing, ensures a solid market position and reduces transition risks (ESG factor: credit-positive environmental factor). Moreover, ALTEO's further growth through the expansion of its energy services and waste management will likely broaden ALTEO's cash flow streams and make it less dependent on external uncontrollable parameters such as weather developments, fluctuating energy prices and gas procurement or government intervention.

Figure 1: Revenue split by geography



Sources: ALTEO, Scope

Figure 2: Revenue split by segment (in HUF bn)

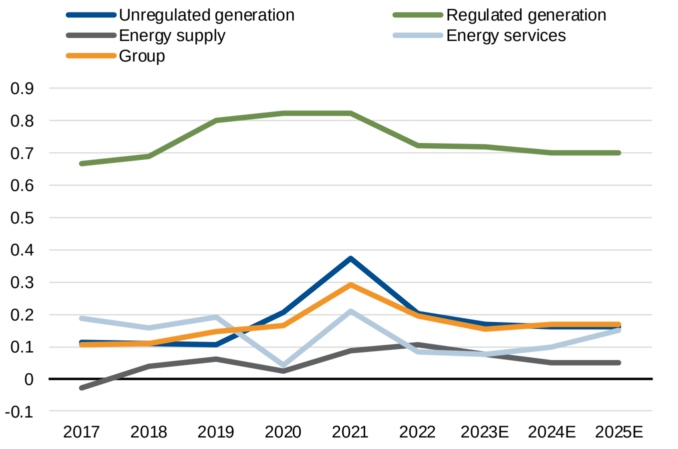


Sources: ALTEO, Scope

Satisfactory margin profile

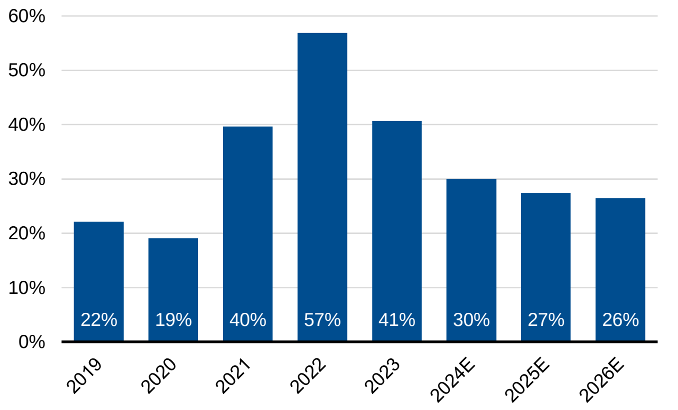
The company performed very well during the energy crisis in Europe. Elevated energy prices had a significant positive impact on its financial performance, especially in its energy trading and supply division and in the provision of balancing energy. However, the normalisation of energy prices, together with an intensive investment programme, is likely to weaken the company's profitability in the medium term until the results of the investments are reflected in a sustained improvement in financial performance in the long term. As a result, we expect the group margin to fluctuate between 9-15% in 2024-2026, compared with 15-20% previously. At the same time, we expect profitability to be continuously underpinned by a very strong ROCE of 25-30%.

Figure 3: ALTEO's reported EBITDA margin per segment



Sources: ALTEO, Scope estimates

Figure 4: Scope-adjusted ROCE



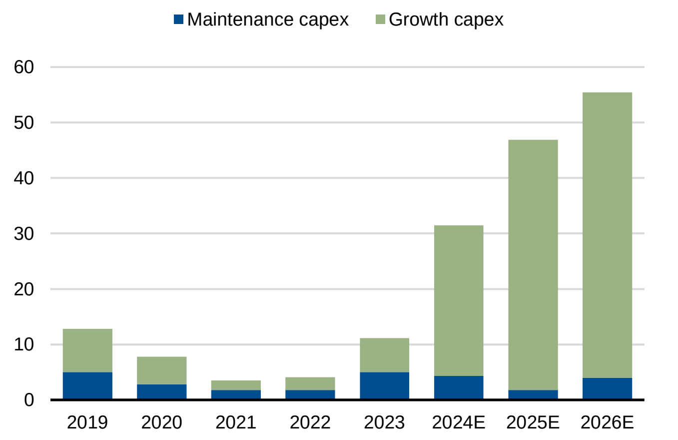
Sources: ALTEO, Scope estimates

Financial risk profile: BBB+

Current strong credit metrics are not sustainable in the medium term

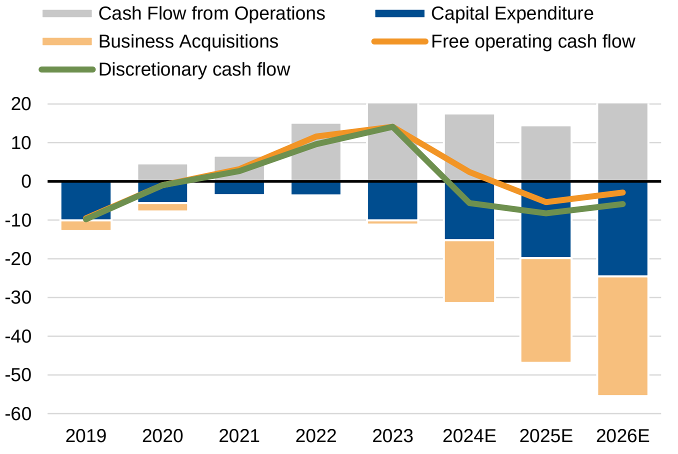
The rating support is based on our view of ALTEO's solid financial risk. While the very strong financial metrics reported in 2022 and 2023 are not considered representative of the company's medium- to long-term financial position, we expect sustained improvement in credit metrics over the medium term. Additionally, we highlight the company's ambitious capex plan, which is mainly related to organic and dynamic growth capex, which could exceed HUF 130bn in total between 2024 and 2026 (see Figure 5).

Figure 5: Steep ramp-up of capex programme (HUF bn)



Sources: ALTEO, Scope estimates

Figure 6: ALTEO's cash flow profile (HUF bn)

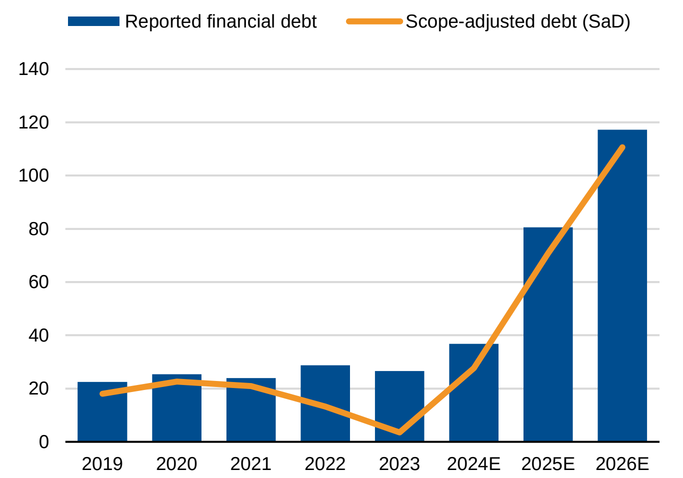


Sources: ALTEO, Scope estimates

Significant increase in debt, which affects medium-term debt forecast

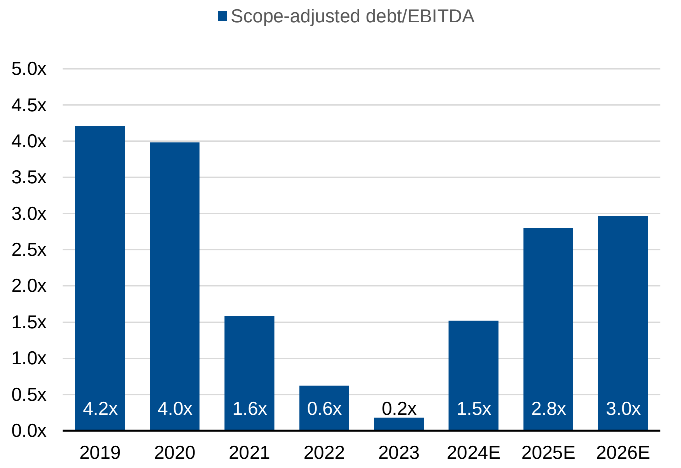
While such a large capex programme is expected to be financed by the current operating cash flow and the large cash buffer of over HUF 17bn as of March 2024, a large part of the capex will be financed by newly raised debt. As a result, we expect the company's gross debt to increase significantly to around HUF 120bn by YE 2026 from HUF 27bn as at YE 2023. However, such an increase in debt can be partially absorbed by the company's expected operating performance, as evidenced by EBITDA of around HUF 20-35bn over the medium term. As a result, we expect the company's sustainable leverage - as measured by Scope-adjusted debt/EBITDA - to settle at 1.5-3.0x in the medium term, up from 0.2x in 2023 (see Figure 8).

Figure 7: Development of indebtedness (in HUF bn)



Sources: ALTEO, Scope estimates

Figure 8: Expected development of leverage



Sources: ALTEO, Scope estimates

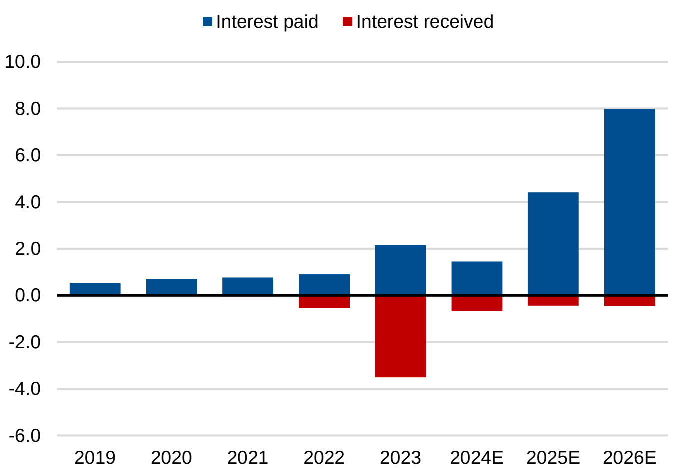
Free operating cash flow under pressure in 2025 and 2026

In our view, maintenance and an increased organic growth capex will likely deteriorate the company's internal funding capacity to slightly negative territory, especially in 2025 and 2026. Consequently, discretionary capex for dynamic growth is likely to require additional external funding.

Interest coverage expected to deteriorate

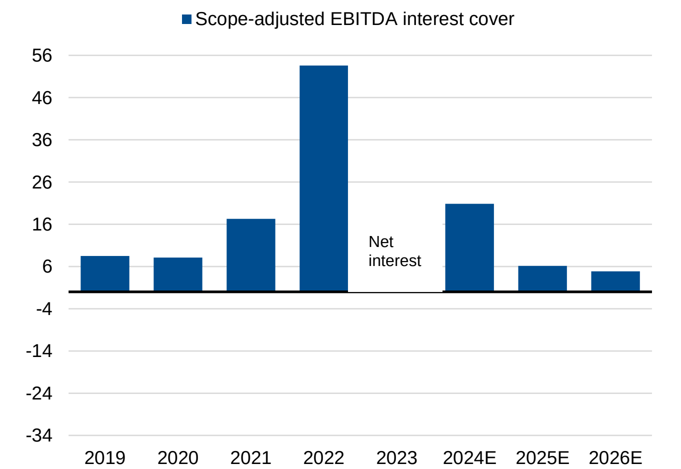
Medium-term debt protection, as measured by Scope-adjusted EBITDA interest coverage, is expected to settle at 5-6x. While the near-term debt protection is largely supported by the company's low leverage and significantly positive interest income on the cash buffer, ALTEO's interest coverage is expected to be impacted by the growing debt exposure and overall higher average interest rates on outstanding debt positions. As a result, ALTEO's net interest burden is expected to increase to around HUF 7.7bn in 2026 from net interest income in 2023.

Figure 9: Development of net interest (in HUF bn)



Sources: ALTEO, Scope estimates

Figure 10: Expected development of debt protection



Sources: ALTEO, Scope estimates

Sound liquidity profile

In our view, ALTEO's liquidity position remains very solid. Upcoming debt maturities between 2024 and 2026, totalling HUF 6.4bn, should be comfortably covered by the company's cash buffer (HUF 17.3bn as of end-March 2024) and available overdraft facilities (HUF 2.5bn as of March 2024).

A major debt refinancing will occur in 2029, when the bullet payment of the first MNB bond (HUF 8.6bn) comes due. From today's perspective, we are not very concerned about a successful refinancing of this maturity, especially after the change in the company's shareholder structure.

We are aware that the credit facilities from Erste Bank and OTP are only provided on a rolling basis; however, we consider them equivalent to committed lines as we can see that most of them are in place for at least 5 years. However, we believe that ALTEO will not need such credit facilities in 2024-2026 as internal liquidity sources are fully sufficient for debt refinancing and organic capex.

Despite its small size, ALTEO has good access to external financing, as evidenced by its continuous bond issuance (first bond in 2011) and well-established credit relationships not only with Hungarian banks such as MTB and OTP, but also with Austria's Erste and Italy's Unicredit. While the larger debt maturities - the two zero-coupon bonds ALTEO 2022/I (HUF 650m) and ALTEO 2022/II (HUF 1.7bn) - have been repaid with cash, ALTEO retains good refinancing alternatives in case of a need for bridge financing.

Liquidity sources and uses in HUF '000s	2022	2023	2024E	2025E	2026E
Unrestricted cash (t-1)	3,679,253	16,465,328	24,345,080	10,893,265	12,593,690
Open committed credit/factoring lines (t-1)	1,273,735	2,500,000	2,500,000	2,500,000	2,500,000
FOCF (t)	12,996,396	14,807,127	3,049,770	(4,322,644)	(1,810,618)
Short-term debt (t-1)	2,731,916	7,185,732	1,703,817	1,538,806	1,588,086
Coverage	**>200%**	**>200%**	**>200%**	**>200%**	**>200%**

Supplementary rating drivers: +/- 0 notches

Financial policy: credit-neutral

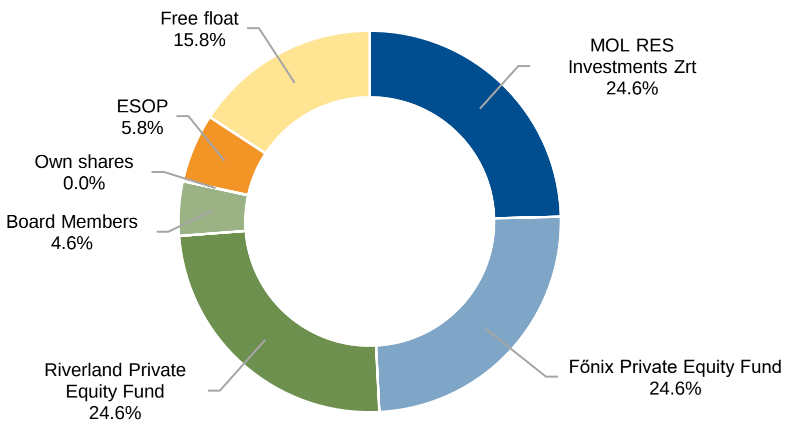
ALTEO maintains a prudent financial policy, which we do not expect to change. While the company is planning the above-mentioned strong investment programme over the next few years, including dynamic growth opportunities, M&A activities are likely to relate to smaller bolt-on acquisitions, e.g. ready-to-build projects or smaller operating ventures in the utility's core segments, generation or services. We do not see major integration risks or major delays in earnings accretion, so acquired businesses are likely to be accretive to earnings growth. We expect shareholder remuneration to continue to be linked to ALTEO's operating performance and not to jeopardise credit quality. Shareholder remuneration would likely be adjusted if necessary to maintain the company's credit profile, which we believe is a clear focus for management, as happened in 2020 during the Covid-19 crisis. Finally, we highlight introduced long-term incentives set for the ALTEO Board of Directors. These incentives relate to i) financial KPIs and ii) sustainability targets. As such, we are more confident that ALTEO's business will be managed in a prudent and conservative manner in the interest of creditors.

No direct rating impact from shareholder structure

The shareholder structure of the utility is reflected in the rating as credit-neutral and does not result in any rating adjustments to the stand-alone credit assessment. Following the completion of the takeover bid by the new consortium of shareholders led by MOL RES Investments Zrt, there is no longer a de facto controlling shareholder of ALTEO (each of the three shareholders, including Főnix Private Equity Fund and Riverland Private Equity Fund, holds 24.6%). However, we consider the Hungarian oil and gas incumbent MOL (the ultimate parent company of MOL RES Investments Zrt) to be the leader among the new shareholders. We believe that MOL has a long-term investment horizon for ALTEO and views the utility as an associated subsidiary that could strengthen MOL's ambitions to diversify outside its core business. We view MOL's creditworthiness as slightly better than

ALTEO's standalone credit profile, with much stronger financial strength in terms of size and funding channels. This implies that MOL would likely be able to provide financial support to ALTEO if needed, either to execute capex or for refinancing needs. Overall, the shareholder structure does not result in any rating adjustments, it justifies ALTEO's investment-grade rating.

Figure 11: ALTEO's new shareholder structure as of Q1 2024



Sources: ALTEO, Scope

Long-term and short-term debt ratings

Senior unsecured debt rating: BBB-

Senior unsecured debt issued by ALTEO is rated at the same level as the issuer rating. This is aligned with our general rating approach for senior unsecured debt of investment-grade rated issuers.

Short-term debt rating: S-2

ALTEO's short-term debt rating is based on the underlying BBB-/Stable issuer rating and the company's solid liquidity profile, characterised by consistently strong liquidity and an adequate access to external funding channels.

Scope Ratings GmbH

Headquarters Berlin

Lennéstraße 5
D-10785 Berlin

Phone +49 30 27891 0

Frankfurt am Main

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389 0

Paris

10 avenue de Messine
FR-75008 Paris

Phone +33 6 6289 3512

Oslo

Karenslyst allé 53
N-0279 Oslo

Phone +47 21 09 38 35

Madrid

Paseo de la Castellana 141
E-28046 Madrid

Phone +34 91 572 67 11

Milan

Via Nino Bixio, 31
20129 Milano MI

Phone +39 02 30315 814

Scope Ratings UK Limited

London

52 Grosvenor Gardens
London SW1W 0AU

Phone +44 20 7824 5180

info@scoperatings.com
www.scoperatings.com

Disclaimer