| Utility | Update | Czech Republic |

CEZ

Price of power remains high, WFT expected to be abolished

Buy

Price 06.09.23	**CZK 923**
12m target	**CZK 1,034**
Upside to TP	**12.0%**
Dividend	**CZK 64**
Total return	**19.0%**

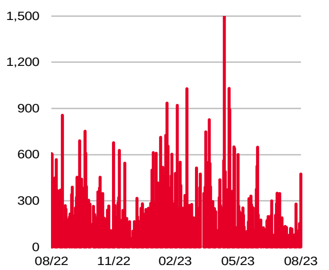
Sector stance
Overweight

Investment type
Commodity price exposure
High dividend yield

1 year performance

Source: Bloomberg

Trading volume (in ths of shares)



Source: Bloomberg

Share data

RIC CEZsp.PR	Bloom CEZ CP		
52-week range			723 - 1225
Market cap. (CZKbn)			496.6
Market cap. (EURbn)			20
Free float (%)			30.00
Performance (%)	**1m**	**3m**	**12m**
Share	-3.4	-8.4	0.9
Rel. to PX Index	-1.4	-10.5	-14.2

Source: Bloomberg

The latest analysis and report:

https://bit.ly/CEZ_analysis_20220607_EN
https://bit.ly/CEZ_1Q23_EN
https://bit.ly/CEZ_2Q23_EN

Investment case: We reiterate our Buy rating on CEZ shares with a new price target of CZK1,034 (previous rating and TP: Buy and CZK1,393).

The environment of high electricity prices has a positive impact on CEZ's performance. CEZ should achieve the highest realized prices this year and next year. On the other hand, special taxes are a negative factor. There is a cap on revenues according to the source of production and a windfall profits tax, both resulting in brutally high taxation. However, the special taxes are temporary. The former expires this year and the latter is valid for 2023-2025, but will probably be repealed as of January 1, 2024. Given CEZ's low emissions intensity, the high price of the allowance is a positive factor for the company, which generates most of its power from high-margin, zero-emission plants.

CEZ's current dividend policy is to pay out 60-80% of adjusted net profit. This year, CZK145 per share was paid, which represented a very high yield of +14.3% and a payout ratio of almost 100%. This was higher than the original proposal of the CEZ Board of Directors of CZK117 (80% payout). However, the state, or rather the Ministry of Finance, agreed to its own proposal of the CZK145 at the Annual General Meeting. The reason for this was an effort to reduce the high deficit in the state budget. For the same reason, we expect a 100% dividend in the coming years. However, it is important to note that the dividend will be negatively affected by the WFT, at least next year. Although it is in effect valid for three years, we believe that the special tax will be abolished for 2024 and 2025. But we do not include it in the model. We estimate a dividend of CZK64 next year and about CZK110 in the following years after the abolition of the WFT.

Valuation: Using the discounted cash flow model we set our new target price at CZK1,034. Compared to the current market price, our TP offers an upside of +19.0%. It values CEZ at 5.5x EV/EBITDA, a discount to the Western European utility median of 7.4x. CEZ also offers a decent dividend yield of +6.2%. This is better or higher than its peers (+4.6%).

Major risks: The main risk factors are the availability of generation facilities, especially nuclear power plants, where the company achieves the highest margins. This is followed by the price of energy commodities, especially prices of generated electricity, emission allowances and commodity trading. Developments in special taxes should also be monitored. And, of course, the geopolitical situation remains unpredictable and brings resulting risks.

Financial data	2022	2023f	2024f	2025f
Revenues (CZK bn)	288,5	364,1	364,8	363,9
EBITDA margin (%)	45,6	33,5	32,6	32,6
Net income (CZK bn)	80,7	34,5	34,2	33,7
EPS (CZK)	146	65	64	63
Dividend/share (CZK)	48	145	64	64
Interest cover (x)	84,3	32,0	31,7	24,6
Payout (%)	115,8	99,5	99,0	100,0
Net debt/equity (%)	0,6	0,5	0,7	0,7

Ratios	2022	2023f	2024f	2025f
P/E (x)	6,4	16,0	16,1	16,4
Price/free cash flow (x)	-4,2	4,4	11,9	11,7
Dividend yield (%)	5,2	14,0	6,2	6,2
Price/book value (x)	1,9	2,6	2,6	2,6
P/S (x)	1,7	1,5	1,5	1,5
EV/S (x)	2,3	1,8	1,9	1,9
EV/EBITDA (x)	5,1	5,5	5,9	6,0
EV/IC (x)	1,7	2,0	2,1	2,1

Upcoming events: CEZ's 3Q or 9M results are scheduled for November 9.

SOCIETE GENERALE GROUP

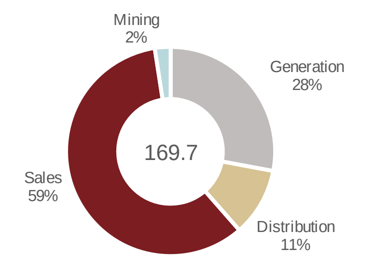
Bohumil Trampota
(420) 222 008 560
bohumil_trampota@kb.cz

Company overview

Strengths	Weaknesses
▪ Strong position of the company throughout Europe ▪ Vertical integration from coal mining and electricity generation to distribution ▪ A wide portfolio of production sources ▪ Provides services in the field of energy savings and smart solutions (ESCO services) ▪ Low emissions intensity	▪ Government influence and impact of political decisions on the company's management ▪ Less efficient operation of some coal-fired power plants ▪ Strict state regulation of electricity generation and the distribution process ▪ Uncertainty of natural gas sourcing due to geopolitical tensions

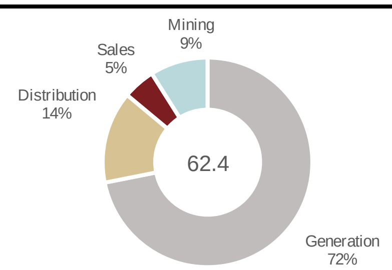
Opportunities	Threats
▪ Dividend policy with maximum payout potential ▪ Subsidies from the Modernisation Fund for investments in RES ▪ Increasing carbon prices with a positive impact on CEZ profitability due to the anticipated decrease in their needs ▪ Closure of nuclear and coal-fired power plants in Western Europe ▪ Expected abolition of the special WFT, as the reasons for its introduction have disappeared.	▪ Construction of a new nuclear block without state guarantees ▪ Lower support for electricity generation from renewable sources ▪ Increased demand for emissions allowances in the case of production failure by non-emissions sources ▪ Special taxes: The cap on sales by production source and windfall profits tax continues.

Revenues by segment (1H23)



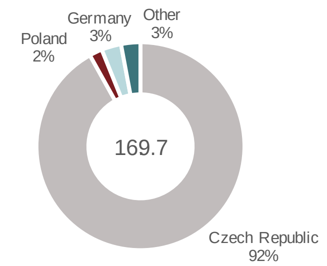
Source: CEZ; * figures are in CZKbn

EBITDA by segment (1H23)



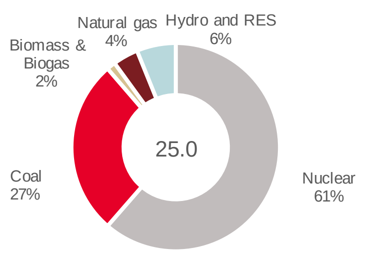
Source: CEZ; * figures are in CZKbn

Revenues by region (1H23)



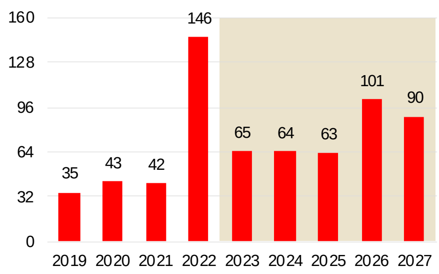
Source: CEZ; * figures are in CZKbn

Electricity generation by fuel (1H23)



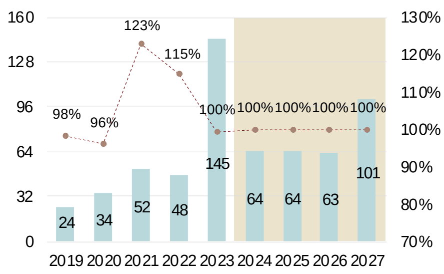
Source: CEZ;* figure is in GW

EPS (CZK)



Source: CEZ; Economic & Strategy Research, Komerční banka

Dividend per share (CZK)



Source: CEZ; Economic & Strategy Research, Komerční banka; in year in which is paid

Sector trends

Electricity prices

The current market price for electricity has dropped significantly compared to 2022 and is around EUR140MWh. The last year has been very volatile. From lows at the beginning of the year of just over EUR110/MWh, the price shot up to EUR1,000/MWh. The average price for the year was around EUR300/MWh. The reason for the turbulent development was the high increase in energy commodity prices (gas, coal, emission rights). The development of commodity prices is shown in the graph below.

Electricity prices are expected to fall in the coming years. Futures contracts indicate a drop from the current EUR140/MWh to EUR92/MWh in 2027.

Gas

Gas is one of the factors that has fundamentally affected the price of electricity.

The sharp increase in the price of gas is one of the main factors behind the sharp rise in electricity prices. This is due to the geopolitical situation and risk factors such as uncertainty about future supplies. Russian gas supplies to other European countries have been largely replaced by other sources. The annual contract price is now EUR55/MWh, down from almost EUR90 at the beginning of the year. Even more striking is the comparison with the all-time high of EUR280 exactly one year ago. This was caused by a combination of empty storage on the eve of the new winter season and supply uncertainty. The issue has been resolved, and the price has fallen to today's already moderated EUR 55. The average gas price for the last decade 2010-2020 is EUR20.

CO_2 emissions allowances

Emission allowances near an all-time high.

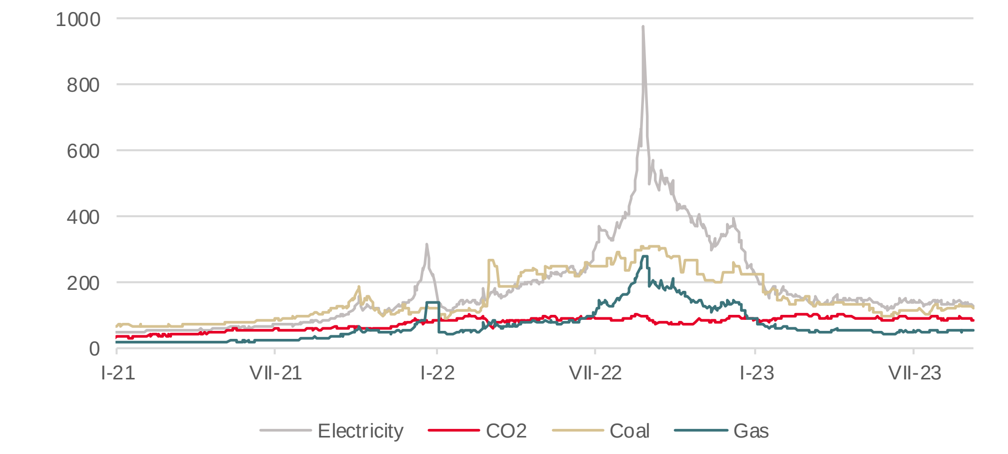
The volatility of the CO2 price has decreased significantly compared to 2022, when it was very high. It is trading at around EUR90/t. This is close to the maximum price of EUR105 (Feb23). The allowance price started to rise at the beginning of 2021. In 2020, the average price was around EUR26. In 2021, it was already at EUR55 and last year it was EUR87. The increase of the allowance is caused by increased social responsibility (climate policy) and substitution of coal by gas. The emission intensity of coal sources is much higher (c2x) compared to gas sources. This has influenced the demand for emission allowances.

Coal

Coal prices have fallen from last year's highs.

The chart of coal price evolution is practically the same as in the previous two cases. A significant increase in the price was seen in 2021, and especially last year, when it reached historic highs. From last year's record levels of just over USD300/t, the price has fallen to today's USD130/t. The average price before the turbulent period (2018-2020) was around USD70/t. The reasons are the same as above.

Power prices (€/MWh), CO_2 (€/MWh), coal ($/t) and gas (€/MWh)

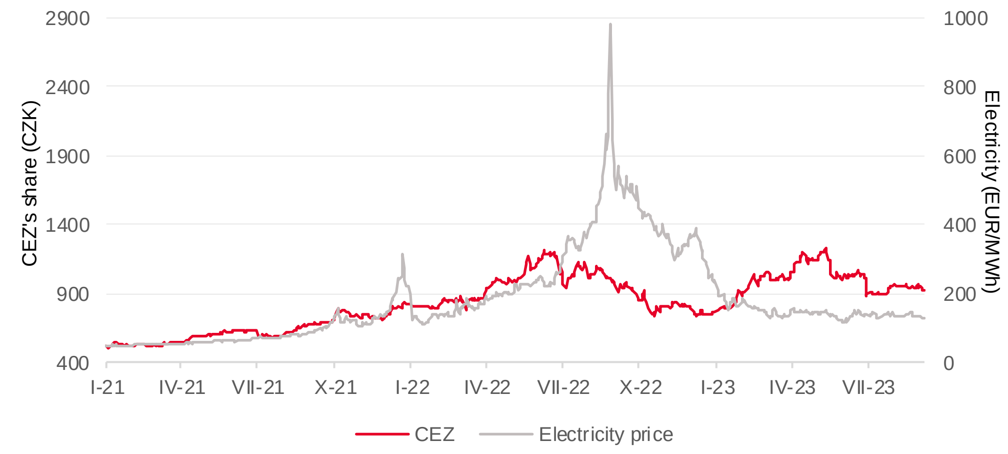


Source: Bloomberg

The price of electricity is rising faster than the price of CEZ shares.

The chart below shows that the CEZ share price was more or less correlated with the development of electricity prices. The reversal came with the change in the geopolitical situation, which significantly pushed up electricity prices. The trading of CEZ shares was affected by information about a possible restructuring of the company, but also by special taxes, which massively increased the company's tax burden. Since the beginning of the year, the CEZ share price has risen by about +22%, while the electricity price has fallen by 43%.

Development of CEZ's shares vs. German electricity prices



Source: Bloomberg

Company results

2Q23

Significant growth.

The reported figures for the second quarter were significantly higher than in the previous year and exceeded the highest market estimates. In addition to the generation segment (higher electricity prices) and surprisingly strong trading, sales (winter/summer commodity price difference and one-off income from the dispute with SZ) are also significantly better. EBITDA increased by +91% yoy to CZK43.7bn on sales of CZK76bn (+28.6% yoy). Net profit reached CZK11.6bn, up +68% yoy.

CEZ reiterated its guidance for the FY. EBITDA is expected to reach CZK105-115bn and adjusted net profit is expected to reach CZK33-37bn. The upper limit of net profit for the maximum payout suggests a dividend of almost CZK70 per share (yield +7.6%). The results for the first half of the year represent approximately 57% of EBITDA and 63% of net profit.

According to our forecasts, we expect EBITDA of almost CZK122bn and net profit of CZK34,8bn this year on total revenues of CZK364bn. Our EBITDA estimate is slightly above CEZ's target of CZK105-115bn. Our net profit forecast is in middle of CEZ's guidance.

According to our estimates, CEZ should produce 51.6TWh of electricity, compared to 54.3TWh last year. The decrease is mainly due to coal-fired generation. We expect the realized power price to be EUR136/MWh, up from EUR110 last year.

2Q22 results

CZKbn	2Q22	2Q23	y/y	KB estimate	Consensus
Sales	54.5	76.3	40%	75.5	75.0
EBITDA	15.6	29.8	91%	24.0	22.6
margin	*28.6%*	*39.1%*	*10.5pps*	*31.1%*	*30.1%*
Operating profit	8.1	21.0	161%	15.7	14.7
Adjusted net profit	6.9	11.6	68%	6.7	6.3

Source: CEZ, Economic & Strategy Research, Komerční banka

Possible restructuring of CEZ

Politicians are considering restructuring.

In the spring of 2022, politicians first mentioned the possibility of restructuring or splitting CEZ. The main reason why politicians want to take control of CEZ seems to be the energy crisis. The restructuring would allow the state to control critical infrastructure, including electricity generation, especially by nuclear power plants, and increased oversight of the planned construction of new nuclear units. There is no information about a possible split, including whether the deal is in the works, so the whole situation is shrouded in a thick fog. Politicians rarely comment on the split of CEZ. In addition, the government's draft law on CEZ transformation, which must pass the Parliament, the Senate and be signed by the President, is opposed by minority shareholders. In case of its approval, they plan to pursue legal actions that would most likely paralyze the whole situation for many years.

We continue to believe that if any restructuring of CEZ were to take place, the state should settle fairly with minority shareholders. That would mean a substantial premium.

The new nuclear units will be 100% financed by the state.

One of the main reasons for the speculation about the split of the company is the construction of new nuclear power plants. We would like to remind you that the tender for the completion of one unit of the Dukovany power plant is underway. All three bidders (Westinghouse, EDF and KHNP) should submit their final offers by the beginning of October. The government is expected to make a decision in 2024. As a reminder, the state will be a 100% investor in the construction of the new nuclear unit. The tender, rather than the actual implementation of the project, is a very complex project in many respects. This has probably been one of the reasons why the share price has been under pressure, especially given the uncertainty surrounding this huge project. Please note that the **new nuclear units will be 100% financed by the state**.

Special taxes

They were introduced to **finance extraordinary expenses of the state budget**. These are the levies on excess sales and the windfall profits tax. **They should be temporary**.

Windfall tax

The WFT has been **introduced for 2023, 2024 and 2025** and applies to **energy production and trade**, among other sectors. Anything that is or will be **above the 2018-2021 average, plus 20%**, is considered a windfall or excess profit to which the 60% tax will be applied.

The standard corporate income tax rate is 19%.

The **windfall profit is then subject to 19% corporate tax plus 60% WFT. The resulting excess profits tax rate is a brutal 79%**.

According to CEZ's own latest estimates, it will pay CZK22-30bn in WFT this year. According to our model, it should be almost CZK28bn.

The WFT is now in place for 2023, 2024 and 2025. However, in our view, the **reasons for its introduction, which were to offset high energy prices, have passed**. **Finance Minister Stanjura has admitted that there will be a discussion about its abolition**, probably from 2024. In our model, although we include the WFT for the whole period (2023-2025), **we expect it to be abolished from 2024**. This would of course have a **positive impact on net income in 2024 and 2025**. As net income is the basis for the dividend calculation, the **dividend itself would also increase**, assuming the current dividend policy is maintained.

Levy on excess revenues

This special tax applies to revenues from electricity generation above the caps. It is set at **90% of the revenue above the caps**. It applies from **December 2022 for the whole of 2023**. Thus, it will not apply in 2024.

In our view, CEZ will be subject to the levy on revenues from nuclear generation. The ceiling is set at EUR70/MWh. 90% above that is the excess revenue levy.

CEZ management estimates the levy for this year at CZK8-13bn. Our estimates are slightly above the upper end of the company's forecast.

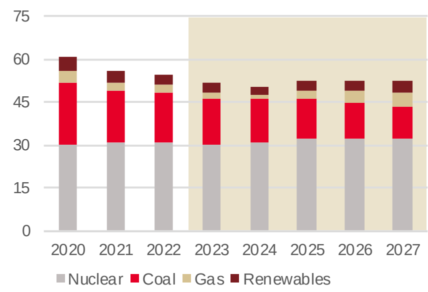
Long-term forecasts

Nuclear power plants dominate the energy mix.

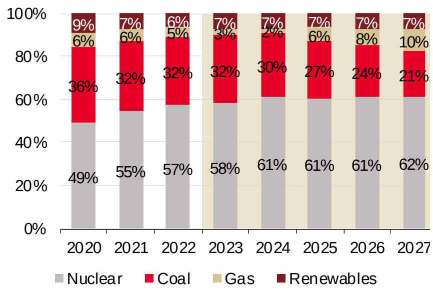
Nuclear power plants produced 57% of CEZ's total electricity last year, generating 31TWh. We expect nuclear generation to remain dominant, rising slightly to 32.2TWh in 2027. Its share of the total should rise to just over 60%. There will certainly be no new nuclear capacity in the forecast period (2023-2027). If there are any, they are likely to be small modular reactors, but only after 2040. The "dirtiest" sources, the coal-fired power plants that produce the most emissions, will be phased out. The installed capacity of coal-fired power plants will decline from 4.3GW in 2022 to 2.2GW in 2030, and their share of electricity generation will fall from 32% in 2020 to 25% in 2025 and to 12.5% in 2030, when only modernized plants will be in operation. Given the uncertainty of gas supply, we do not foresee an expansion of the gas-fired power plant portfolio. On the contrary, generation or new renewable capacity is expected to increase.

From the current 2.2GW, 1.5GW of new renewable capacity should be added by 2025 and a further 6GW by 2030.

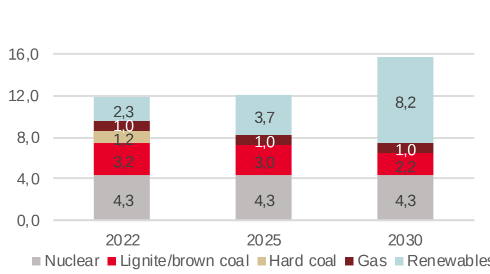
CEZ electricity generation (TWh)



Generation by source



CEZ generation capacity estimate (GW)



Source: CEZ, Economic & Strategy Research, Komerční banka

Electricity prices will be significantly higher than in previous years.

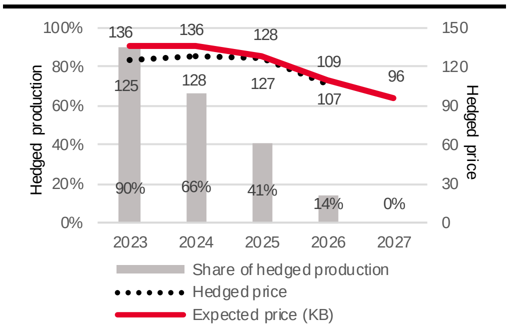
High realized power prices

Last year was a very turbulent year for electricity prices. The peak jumped to an almost unbelievable EUR1,000/MWh. The average price for 2022 was around EUR300. The reason for the increase was the geopolitical situation and the uncertainty of gas supply, which affected the price of energy commodities. This year, the price of electricity is around EUR140. The price of futures contracts for the following years continues to fall, from EUR136 for 2024 to EUR95 for 2027.

This year, CEZ sold the generated electricity for EUR125/MWh. However, as of June 30, it still had an open position of 7% of the volume. Therefore, the resulting average price will be higher. We assume that it will include peak sales. For this year, we estimate the **average power price to be EUR136**. For next year, we assume roughly the same price.

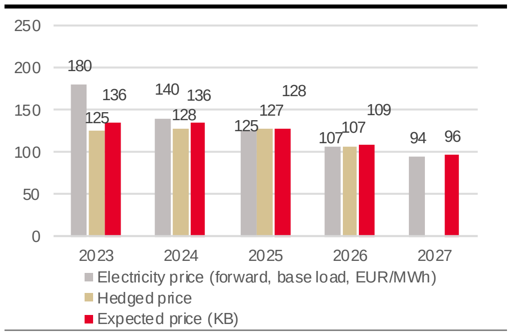
The right chart below shows the hedged price, our estimated price and the forward price.

Hedged sales and average prices (EUR/MWh)



Source: CEZ, Economic & Strategy Research, Komerční banka

Expected higher realised prices (EUR/MWh)



Source: CEZ, Bloomberg

As the price of electricity drops, the numbers will come down from record highs.

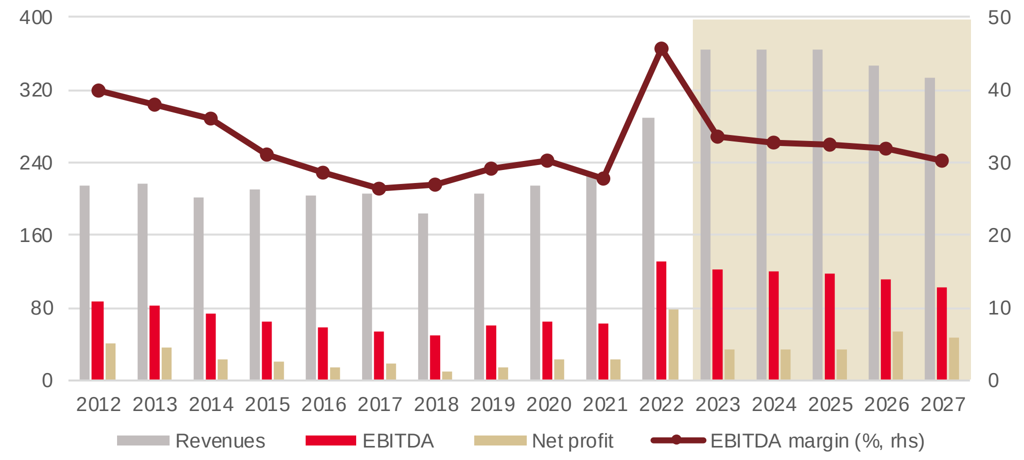
Earnings estimates

Last year, total sales were CZK289bn. This year, we expect CZK364bn. The increase in electricity prices is the main reason for this growth. By the end of the forecast period (2027), we expect revenues to decline slightly to CZK334bn. The reason for the downward trend is again the electricity price (see above).

According to CEZ's own estimates, EBITDA should be in the range of CZK105-115bn this year, after a record CZK131.6bn in 2022. According to our estimates, EBITDA should reach CZK121.9bn this year. For the first half of the year, EBITDA is about 57% of the total annual EBITDA expected by CEZ management. EBITDA will decline similarly to sales due to falling electricity prices. In the last year of the forecast period (2027), we expect this profit to reach CZK101bn.

Adjusted net profit will decline significantly this year. According to our estimates, it should decline from CZK78.4bn to around CZK34.8bn. CEZ's full-year target is CZK33-37bn. The significant yoy decline is due to WFT (see above). For the first half of the year, the net profit is CZK22.5bn, or 63% of the full-year forecast. In the final year, 2027, we expect the adjusted net profit to be CZK48bn.

CEZ results forecasts (CZKbn)



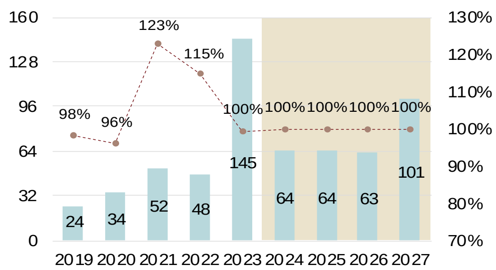
Source: CEZ, Economic & Strategy Research, Komerční banka

Dividend policy

The CEZ' guidance for this year suggests a dividend of up to CZK70.

According to the current dividend policy, CEZ should distribute 60-80% of the adjusted net profit to its shareholders. This year, CEZ paid a dividend of CZK145 per share. The CEZ management's original proposal was CZK117, which corresponds to the upper limit of the payout ratio, i.e. 80% of net profit. However, the state, through the Ministry of Finance, which exercises shareholder rights on behalf of the state, contradicted its initial statement that it would not demand a higher dividend by finally proposing to pay out the entire (100%) profit. This is equivalent to a dividend of CZK145 per share. We had expected this. Given that the state controls almost 70% of all shares in CEZ, the approval at the June AGM was a mere formality. We believe that the main reason for the higher payout is the government's effort to reduce the high budget deficit.

Expected dividend payment per share (CZK)



Source: CEZ, Economic & Strategy Research, Komerční banka; in year in which is paid

Please note that the high dividend payout in 2021 and 2022 consists of two components. First, the adjusted net income and second, the extraordinary payout reflecting the divestment of Romanian and Bulgarian assets.

From this year's profit, we estimate a dividend of CZK64 to be paid next year, which corresponds to a gross yield of +6.2%.

In the coming years, we expect CEZ to pay out the entire net profit.

In the coming years, **we expect to pay out 100% of net income again**, which is higher than the current dividend policy of 60-80%. **The reason for this is the same as this year, when the high dividend helped ease the government's budget situation**.

In the next three years, however, the **dividend will be affected by special taxes, in particular the WFT**. In our model, we conservatively assume that the WFT will remain in place for the full three years, but we expect that it will be abolished for 2024 and 2025 and will only apply in 2023. If this change were to occur, the **dividends paid in 2025 and 2026 would increase from CZK64 and CZK63 to CZK114 and CZK110**.

Indebtedness

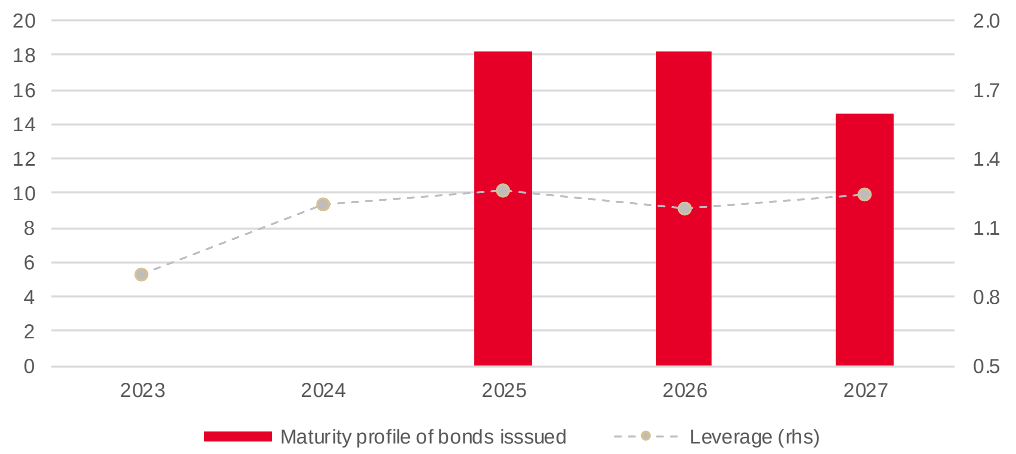
Low leverage will increase by the end of the year but will still be well below CEZ's target.

Leverage was at a very low level of 0.3x (net debt / EBITDA) at the end of the first half of 2023. This is well below CEZ's target of 2.5-3.0x.

We expect leverage to increase by the end of this year for several reasons. The main one is the dividend payment (CZK78bn), which started August 1. Then there is the repayment of state loans and taxes. We expect the leverage ratio to be around 1.0x for the period.

There are no bonds maturing this year or next (see chart below). From 2025 to 2027, up to CZK20bn of bonds will mature annually.

Maturity profile of the issued bonds (CZKbn)



Source: CEZ, Economic & Strategy Research, Komerční banka

M&A

Planned participation in a possible tender for GasNet.

In recent days, the media have reported the **possible sale of the gas distribution network GasNet**. It is the main gas supplier in the Czech Republic (outside of Prague and the South Bohemia region). Its current owner, Macquarie Asset Management, is reportedly considering a sale. CEZ **deputy chairman Pavel Cyrani said that CEZ is ready to make a quality offer**.

According to GasNet's annual report, the company has an EBITDA of CZK9,3bn and CZK8.2bn in 2021 and 2022. With an EV/EBITDA multiple of 10.4x industry peers, this suggests a price of around CZK90bn. In case of a successful offer, this would likely increase CEZ's leverage towards 2.0x. We consider this a comfortable level, well below CEZ's target of 2.5-3.0x. CEZ would have no problem with a possible acquisition of GasNet.

Valuation

Sector comparison

CEZ trades at a discount to its peers.

We have selected competitors operating in both Western and Central Europe. CEZ's valuation corresponds more to its Western European counterparts, as shown by the table below. On the EV/EBITDA multiple it offers a discount to its peers. It should also outperform the rest of the group in terms of dividend yield.

Peer comparison

	P/E akt.	P/E 2023	P/E 2024	P/S akt.	P/S 2023	P/S 2024	EV/ EBITDA akt.	EV/ EBITDA 2023	EV/ EBITDA 2024	EV/S akt.	EV/S 2023	EV/S 2024	Div. yield 2024
CEZ (KB estimate)	**8,3**	**16,0**	**16,1**	**1,7**	**1,5**	**1,5**	**4,9**	**5,5**	**5,9**	**2,0**	**1,8**	**1,9**	**6,2**
CEZ (consensus)	**13,6**	**13,0**	**14,6**	**1,6**	**1,6**	**1,7**	**4,5**	**4,0**	**4,5**	**1,7**	**1,7**	**1,8**	**15,7**
ENDESA SA	15,7	13,9	13,3	0,9	0,9	0,8	8,5	8,1	7,8	2,1	2,0	2,0	4,6
ENEL SPA	10,4	11,4	11,9	0,3	0,3	0,3	7,3	7,6	7,6	0,6	0,6	0,7	4,5
ENGIE	12,4	37,1	38,1	0,2	0,2	0,2	8,3	20,3	21,7	0,2	0,2	0,2	n/a
EVN AG	12,4	11,5	10,1	0,8	0,8	0,8	6,0	5,7	5,4	1,1	1,2	1,2	8,4
FORTUM OYJ	10,1	9,4	9,1	0,6	0,6	0,6	7,2	6,9	6,8	1,4	1,4	1,4	6,6
IBERDROLA SA	7,0	8,4	8,7	0,4	0,4	0,4	4,3	4,6	4,5	0,7	0,7	0,7	9,7
RWE AG	9,4	10,6	9,9	1,3	1,3	1,3	7,7	7,7	7,5	1,8	1,9	1,9	2,3
VERBUND AG	9,3	10,5	11,0	1,5	1,6	1,7	6,0	6,8	7,0	1,7	1,9	2,0	7,4
MEDIÁN západní Evropa	14,6	14,0	13,1	1,2	1,2	1,2	9,6	9,2	8,6	2,6	2,6	2,5	4,6
PGE SA	7,8	11,4	13,8	0,7	0,7	0,8	4,5	5,4	5,8	0,8	0,9	0,9	2,4
ENERGA SA	11,0	11,5	12,1	2,5	2,6	2,7	7,1	7,4	7,7	2,8	3,0	3,0	3,3
MEDIAN Western Europe	**10,4**	**11,4**	**11,9**	**0,8**	**0,8**	**0,8**	**7,2**	**7,4**	**7,5**	**1,4**	**1,4**	**1,4**	**4,6**
ENEA SA	4,0	5,1	4,2	0,2	0,2	0,2	2,4	3,0	2,7	0,2	0,3	0,4	n/a
TAURON POLSKA ENERGIA SA	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a
MEDIÁN střední Evropa	1,8	4,4	3,4	0,1	0,2	0,2	2,4	4,8	4,3	0,3	0,4	0,4	n/a
SEKTOROVÝ MEDIÁN	2,3	4,2	3,2	0,1	0,2	0,2	3,4	4,7	4,1	0,5	0,6	0,7	n/a
MEDIAN Central Europe	**2,3**	**4,4**	**3,4**	**0,1**	**0,2**	**0,2**	**2,4**	**4,7**	**4,1**	**0,3**	**0,4**	**0,4**	n/a
SECTOR MEDIAN	**9,8**	**11,0**	**10,6**	**0,6**	**0,7**	**0,7**	**6,6**	**6,8**	**6,9**	**1,0**	**1,0**	**1,1**	**4,6**
CEZ vs. sector (consensus)	*39%*	*19%*	*38%*	*152%*	*140%*	*146%*	*-31%*	*-41%*	*-35%*	*78%*	*66%*	*71%*	*241%*
CEZ vs. sector (KB estimate)	*-15%*	*46%*	*53%*	*166%*	*130%*	*125%*	*-24%*	*-20%*	*-14%*	*107%*	*76%*	*81%*	*34%*
CEZ vs. WE (KB estimate)	*-21%*	*40%*	*36%*	*115%*	*83%*	*83%*	*-31%*	*-26%*	*-21%*	*48%*	*31%*	*37%*	*34%*

Source: Bloomberg, Economic & Strategy Research, Komerční banka

Target price

Based on the DCF model, we set a new target price of CZK1,034 per share.

A two-stage discounted cash flow (DCF) model with a five-year explicit forecasting period was used to determine the fair value of CEZ shares. The main parameters and outputs are shown in the table on the next page. Free cash flow is discounted using a weighted average cost of capital (WACC) in the range of 7.7-9.3% for the explicit period. We assume a long-term growth rate of 2%. Based on the DCF model, we set our fair value target price at CZK1,034 per share. The key factor is the positive impact of high electricity prices on the company's profitability and cash flow generation.

CEZ valuation

	2023	2024	2025	2026	2027	LT
Calculation of the required rate of return						
risk-free rate	4.2%	3.8%	3.8%	3.9%	3.9%	3.9%
beta	0.86	0.86	0.86	0.86	0.86	0.86
equity risk premium	5.9%	5.9%	5.9%	7.4%	8.9%	8.9%
country risk premium	0.9%	0.9%	0.9%	0.9%	0.9%	0.9%
cost of equity	10.2%	9.8%	9.8%	11.2%	12.5%	12.5%
weight of debt	33.5%	39.8%	40.9%	35.7%	35.4%	35.4%
cost of debt (after tax)	3.7%	3.7%	3.6%	3.6%	3.6%	3.6%
WACC	**7.5%**	**6.7%**	**6.6%**	**8.5%**	**9.3%**	**9.3%**
Discounted cash flow model (CZKbn)						
EBITDA	121.8	119.1	118.5	110.5	101.3	
Amortization of nuclear fuel	3.9	4.0	4.0	4.1	4.1	
Taxes paid	-12.1	-12.0	-11.8	-4.1	-3.6	
Change in working capital and provisions	55.9	-20.2	-15.1	-12.3	1.7	
CAPEX	-42.0	-44.0	-48.0	-50.0	-50.0	
FCFF	**127.7**	**46.9**	**47.6**	**48.2**	**53.5**	
price / free cash flow	4.4	11.9	11.7	11.5	10.4	
Present value of FCFF	118.8	40.9	38.9	36.3	36.9	
Sum of present values of FCFF until 2027	271.7					
Present value of FCFF after 2027	512.1					
Net debt	109.2					
Nuclear, mining and other provisions	121.9					
Financial investments	0.9					
Joint ventures and associates	3.7					
Minorities	1.4					
Estimated value of equity	556.0					
Fair value (CZK per share)	1,034					
Target price (CZK per share)	**1,034**					

Source: Economic & Strategy Research, Komerční banka

The following table provides a snapshot of the sensitivity of CEZ's target price to changes in key parameters of the valuation, namely forward electricity prices, WACC and the long-term growth rate.

Sensitivity analysis

Long-term growth	WACC: -100bps	-50bps	7,7 % / 9,3 % *	+50bps	+10
1,0%	1 035	970	912	861	8
1,5%	1 110	1 035	970	912	8
2,0%	1 194	1 108	**1 034**	968	9
2,5%	1 298	1 196	1 110	1 035	9
3,0%	1 418	1 298	1 196	1 110	1 0

Forward prices	WACC: -100bps	-50bps	7,7 % / 9,3 % *	+50bps	+100
-20%	912	847	791	743	7
-10%	1 048	975	912	858	8
0%	1 184	1 103	**1 034**	973	9
10%	1 319	1 231	1 155	1 088	1 0
20%	1 455	1 359	1 276	1 203	1 1

Note: * the first value corresponds to the average for the years 2022-26, the second value after 2026;
Source: Economic & Strategy Research, Komerční banka

Major risks

▪ **Electricity prices** - CEZ share prices are significantly affected by the development of electricity prices on European markets. A significant deviation of German electricity prices from our forecasts may cause a different development of CEZ's profits than we currently expect.

▪ **Production mix** - In the coming years, we expect full utilisation of nuclear power plants. This has an impact on the development of profit margins. Should longer nuclear block shutdowns occur, it would lead to lower margins.

▪ **Renewal of the production portfolio** - CEZ has completed the modernisation of its coal-fired power plants. The highest share of investment should go to distribution, renewables and the closure and transformation of production from coal to low emissions. Any contribution to the construction of a new nuclear unit could have a strong negative impact on our valuation.

▪ **Regulation** - The energy sector suffers from strict regulation and in some countries also comes under political and public pressure. The potential reduction in support for electricity production from renewable sources is also a major risk.

▪ **Exchange rate developments** – Although the company is naturally hedged against fluctuations of the EUR/CZK exchange rate, the stronger-than-expected appreciation of CZK against EUR would be negative for CEZ. The impact on electricity prices (Czech prices are derived from German prices in EUR) could outweigh the euro-debt reduction. The weakening of the Turkish lira against USD leads to a decline in profits from affiliates and joint ventures and an increase in financial liabilities due to the loan guarantee provided to the Turkish company AkCEZ.

▪ **Acquisitions** – Potential acquisitions are not included in our forecasts. Big M&A deals would likely increase CEZ’s consolidated profits as well as its debt. The impact on our target price and recommendation might be either positive or negative depending on the parameters of the transaction.

▪ **Tax burden** – Special taxes, the revenue cap and the windfall profits tax are intended to be temporary. However, if they were to be extended, they would have a negative impact on earnings and subsequently on dividend payments. Any additional special or sectoral taxes would have a similar negative effect.

CEZ financials

CZKm	2019	2020	2021	2022	2023f	2024f	2025f	2026f	2027f
INCOME STATEMENT									
Sales	206,192	213,737	227,793	288,485	364,149	364,763	363,867	345,788	333,913
Cost of materials, services and fuel	-118,395	-120,320	-127,285	-162,010	-191,655	-200,346	-199,250	-188,708	-184,532
Salaries (total)	-28,820	-30,855	-30,591	-33,915	-37,723	-38,477	-39,247	-40,032	-40,832
Other costs	-6,282	-3,753	-1,924	-1,890	-12,925	-6,847	-6,916	-6,552	-7,201
EBITDA	60,175	64,783	63,240	131,568	121,845	119,093	118,454	110,495	101,348
D&A and impairments	-33,876	-52,346	-47,427	-29,893	-38,196	-36,697	-36,608	-34,800	-33,612
Operating profit (loss)	26,429	12,585	16,098	101,927	83,650	82,396	81,846	75,696	67,735
Interest income	403	377	431	3,804	2,920	2,495	1,728	1,687	1,821
Interest expense	-5,473	-5,269	-4,206	-5,013	-5,534	-5,091	-5,058	-5,025	-4,993
Interest on provisions	-1,893	-1,955	-2,014	-2,861	-7,116	-3,569	-3,464	-3,625	-3,786
Other financial income/expense	-1,055	2,168	3,117	1,766	2,851	-176	-76	-76	-76
Profit (loss) before taxes	18,411	7,906	13,426	99,623	76,771	76,055	74,976	68,657	60,702
Taxes	-3,911	-2,438	-3,517	-18,918	-42,224	-41,830	-41,237	-14,418	-12,747
Net profit (loss)	14,500	5,468	9,909	80,705	34,547	34,225	33,739	54,239	47,954
Impairments	-4,400	-17,332	-12,391	2,305	-221	-221	-221	-221	-221
Guided net profit (loss)	18,900	22,800	22,300	78,400	34,768	34,446	33,960	54,460	48,175
BALANCE SHEET									
Share Capital	50,914	50,954	52,376	52,465	52,465	52,465	52,465	52,465	52,465
Retained Earnings	199,847	182,917	108,722	206,421	162,960	162,753	162,061	182,406	176,024
Shareholders' Funds	250,761	233,871	161,098	258,886	215,425	215,218	214,526	234,871	228,489
Long-term Debt	142,570	122,102	95,925	140,234	122,004	121,394	120,787	120,183	119,582
Other Long-term Liabilities	31	34	32	31	31	31	31	31	31
Capital Employed	393,362	356,007	257,055	399,151	337,459	336,643	335,344	355,085	348,101
Fixed Assets	428,088	410,372	403,092	435,119	433,821	428,361	425,044	421,009	417,317
Intangible Assets	37,429	24,244	23,854	24,423	32,377	33,384	34,391	35,397	36,404
Financial Investments	113,332	138,768	533,820	320,528	241,935	192,691	192,713	185,678	181,196
Cash and Marketable Securities	9,755	6,064	26,640	36,609	64,031	28,827	21,435	38,793	42,858
Inventories	37,682	48,951	33,480	55,009	55,594	55,791	56,000	56,222	56,457
Receivables	67,218	65,140	148,521	218,674	101,663	121,818	136,477	144,001	139,121
Other Assets	11,070	8,919	13,674	17,018	17,529	18,054	18,596	19,154	19,729
Short Term Debt	29,323	29,725	41,965	61,912	51,212	50,700	50,193	49,691	49,194
Payables	66,872	73,744	88,176	101,238	106,315	106,467	106,246	101,788	98,860
Trade Provisions	110,138	124,709	130,034	159,862	161,183	143,067	150,285	157,504	164,725
Other Liabilities	104,879	118,273	665,851	385,217	290,781	242,050	242,588	236,185	232,200
Capital Employed	393,362	356,007	257,055	399,151	337,459	336,643	335,344	355,085	348,101
Total assets	704,574	702,458	1,183,081	1,107,380	946,950	878,926	884,655	900,254	893,080
CASH FLOW									
Profit (loss) before taxes	18,411	7,906	13,426	99,623	76,771	76,055	74,976	68,657	60,702
Depreciation	29,016	28,284	31,628	32,757	37,975	36,476	36,387	34,579	33,391
Amortization of nuclear fuel	4,096	4,197	4,110	3,907	3,946	3,986	4,025	4,066	4,106
Other non-cash items	21,409	19,596	-14,732	98,839	300	3,278	3,915	3,927	3,763
Change in working capital	-20,990	21,206	32,312	-224,255	55,625	-20,537	-15,440	-12,569	1,337
Tax paid	-4,136	-3,748	-3,550	-5,409	-12,073	-11,960	-11,790	-4,122	-3,645
Interest paid, net	-5,023	-5,307	-4,051	-397	-2,613	-2,595	-3,330	-3,338	-3,171
Dividend received	148	23	13	27	27	27	27	27	27
Operating cash flow	42,931	72,157	59,156	5,092	159,958	84,729	88,771	91,225	96,510
Cash flow from investing activities	-32,363	-33,723	-7,118	-36,712	-42,000	-44,000	-48,000	-50,000	-50,000
Dividends paid	-12,861	-18,139	-27,963	-25,649	-78,009	-34,431	-34,431	-33,893	-54,337
Cash flow from financing activities	-8,091	-42,125	-31,462	41,589	-90,535	-75,933	-48,162	-23,867	-42,446
Change in cash	2,477	-3,691	20,576	9,969	27,422	-35,204	-7,392	17,358	4,064

Source: Economic & Strategy Research, Komerční banka

CEZ financials

	2019	2020	2021	2022	2023f	2024f	2025f	2026f	2027f
RATIOS (%)									
EBITDA margin	29.2	30.3	27.8	45.6	33.5	32.6	32.6	32.0	30.4
Operating margin	12.8	5.9	7.1	35.3	23.0	22.6	22.5	21.9	20.3
Pre-tax margin	8.9	3.7	5.9	34.5	21.1	20.9	20.6	19.9	18.2
Net margin (adjusted)	9.2	10.7	9.8	27.2	9.5	9.4	9.3	15.7	14.4
EBIT/Interest (x)	3.6	2.6	4.3	84.3	32.0	31.7	24.6	22.7	21.4
Net debt/Equity (x)	0.6	0.6	0.7	0.6	0.5	0.7	0.7	0.6	0.6
Net debt/EBITDA (x)	2.7	2.3	1.8	1.3	0.9	1.2	1.3	1.2	1.2
ROE	7.8	9.4	11.3	37.3	14.7	16.0	15.8	24.2	20.8
ROA	2.7	3.2	2.4	6.8	3.4	3.8	3.9	6.1	5.4
ROCE	4.9	6.1	7.3	23.9	9.4	10.2	10.1	15.8	13.7
Dividend payout	98.6	96.8	122.7	115.8	99.5	99.0	100.0	99.8	99.8
DATA PER SHARE (CZK)									
EPS (adj.)	35.3	42.6	41.6	145.7	64.6	64.0	63.1	101.2	89.5
Book value	468.7	437.2	300.7	482.2	400.4	400.0	398.8	436.6	424.7
Free cash flow	18.0	103.8	128.3	-222.3	237.3	87.2	88.4	89.6	99.4
Gross dividend	24.0	34.0	52.0	48.0	145.0	64.0	64.0	63.0	101.0
MARKET VALUATION									
P/E (x)	14.4	12.1	19.9	6.4	16.0	16.1	16.4	10.2	11.5
Price/Operating cash flow (x)	5.2	3.4	6.6	45.8	3.2	5.6	5.4	5.6	5.4
Price/free cash flow (x)	28.3	5.0	6.4	-4.2	4.4	11.9	11.7	11.5	10.4
Price/book value (x)	1.1	1.2	2.8	1.9	2.6	2.6	2.6	2.4	2.4
Price/sales (x)	1.3	1.3	1.9	1.7	1.5	1.5	1.5	1.6	1.7
Dividend yield (%)	4.7	6.6	6.3	5.2	14.0	6.2	6.2	6.1	9.8
EV/revenues (x)	2.1	2.0	2.4	2.3	1.8	1.9	1.9	2.0	2.0
EV/EBITDA (x)	7.3	6.6	8.8	5.1	5.5	5.9	6.0	6.2	6.7
EV/IC (x)	1.1	1.2	2.2	1.7	2.0	2.1	2.1	1.9	2.0

Source: Economic & Strategy Research, Komerční banka

Disclaimer

The information herein is not intended to be an offer to buy or sell, or a solicitation of an offer to buy or sell any securities. All information and opinions have been obtained from or are based on sources believed to be reliable, but their completeness and accuracy are not guaranteed by Komerční banka, a.s., even though Komerční banka, a.s. believes them to be fair and not misleading or deceptive. The views of Komerční banka, a.s. reflected in this document may change without notice.

Komerční banka, a.s. and its affiliated companies may from time to time deal in, profit from the trading of, hold or act as market makers of securities, or act as advisers, brokers or bankers in relation to securities or derivatives thereof emitted by persons, firms or entities mentioned in this document.

Employees of Komerční banka, a.s. and its affiliated companies, or individuals connected to them may from time to time have a position in or be holding any of the investments or related derivatives mentioned in this document. The authors of this document are not authorized to acquire the investment instruments mentioned in this document. This does not apply to cases when the investment recommendation mentioned in this document represents dissemination of an investment recommendation earlier produced by third parties according to Chapter III of regulation (EU) 2016/958. Komerční banka, a.s. and its affiliated companies are under no obligation to provide any services to their clients on the basis of this document.

Komerční banka, a.s. does not accept any liability whatsoever arising from the use of the material or information contained herein beyond what is required by law. This research document is primarily intended for professional and qualified investors. Should a private customer obtain a copy of this report, they should not base their investment decisions solely on the basis of this document and should seek independent financial advice. The investors must make their own informed decisions regarding the appropriateness of their investments because the securities discussed in this report may not be suitable for all investors.

The performance attained by investment instruments in the past may not under any circumstance serve as an guarantee of future performance. The estimates of future performance are based on assumptions that may not be realized. Investment instruments and investments are connected with different investment risks, the value of any investment can rise and fall and there is no guarantee for the return of the initial invested amount. Investment instruments denominated in foreign currencies are also subject to fluctuations caused by changes in exchange rates, which can have both positive and negative influences particularly on the prices of the investment instrument and consequently on the investment return.

This publication is issued by Komerční banka, a.s. which is a bank/stockbroker according to the applicable legislation and thus regulated by the Czech National Bank. Komerční banka, a.s. applies various measures to prevent conflict of interests in the process of creating investment recommendations, such as the implementation of an appropriate internal separation including information barriers between different departments of Komerční banka, a.s. in compliance with the requirements imposed by applicable regulation. The employees of Komerční banka, a.s. proceed in accordance with the internal regulations governing conflict of interest.

The evaluation of employees creating investment recommendations is never by any means tied with the volume or profit of the trades with instruments mentioned in this document done by Komerční banka, a.s., or the trades of Komerční banka, a.s. with the issuers of such instruments. However, the evaluation of the authors of this document is linked to the profits of Komerční banka, a.s. which also partially include the results of trading with investment instruments.

The recommendations mentioned in this document are intended for the public and the document before its publication is not available to persons not involved in the creation of this document. As per our practice, the issuers do not receive a copy of research reports prior to their publication. Each author of this research report hereby states that (i) the views expressed in the research report accurately reflect his or her personal views about any and all of the securities or issuers at stake.

This document and its contents is not designed for persons with permanent residence or seat in the United States of America and to persons who are deemed as “U.S. persons”, as defined in Regulation S under the US Securities Act of 1933, as amended.

Please refer to our website http:\\www.trading.kb.cz for more details.

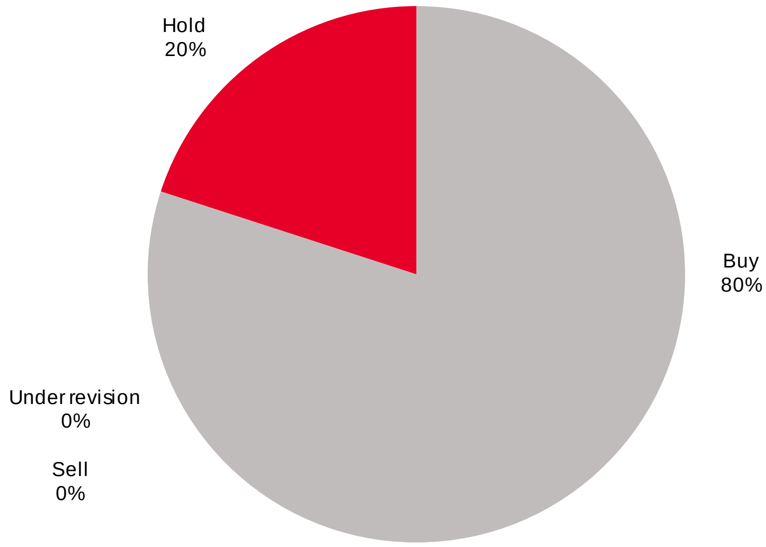
The recommendation in this document and/or the document itself was not disclosed to the issuer before its dissemination.

This recommendation is not updated at regular intervals. The date of the next update has not yet been determined and finally will be influenced by relevant changes of the facts used as the ground for this recommendation to reflect proper development in the industry and/or the analyzed company.

The main methods KB is using for setting target price for stocks are discounted free cash flow analysis and sector comparison. Other methods may also be used if deemed appropriate by the analyst (e.g. sum of parts valuation, discounted dividend valuation, discount / premium to NAV). Target price is set for the time period of 12 months. KB is using three grades of investment recommendation: buy, hold and sell. The recommendation is set for the time period of the next 3-6 months. The most important factor for setting the recommendation is the difference between actual market price and target price calculated by KB equity research. The recommendation also reflects other factors the analyst expects to influence the stock and market in the time period of 3-6 months after its publication. The target price substantially above current price does not automatically mean a buy recommendation for the 3-6 months following the first period of 3-6 months since publication of the recommendation. Valuation methods and factors key for setting the recommendation are explained in the text of each analysis.

The chart below shows the structure of grades of valid investment recommendations of equity research of KB Economic & Strategy Research (8 recommendations).

Investment recommendations of KB equity research



Source: Economic & Strategy Research, Komerční banka

KB Equity Research ratings on a 12 month period

BUY: absolute total shareholder return forecast of 15% or more over a 12 month period.

HOLD: absolute total shareholder return forecast between 0% and +15% over a 12 month period.

SELL: absolute total shareholder return forecast below 0% over a 12 month period.

Total shareholder return means forecast share price appreciation plus all forecast cash dividend income, including income from special dividends, paid during the 12 month period. Ratings are determined by the ranges described above at the time of the initiation of coverage or a change in rating (subject to limited management discretion). At other times, ratings may fall outside of these ranges because of market price movements and/or other short term volatility or trading patterns. Such interim deviations from specified ranges will be permitted but will become subject to review by research management.

Overview of recommendations published by KB and relationships with particular issuers

	CEZ	Colt CZ Group SE	Kofola	MONETA Money Bank	Philip Morris CR	Avast	O2 CR
Overview of last investment research and recommendations related to stocks of particular issuers							
Recommendation	Buy	Buy	Buy	Buy	Hold	End	End
Target price	CZK1,034	CZK652	CZK313	CZK104.6	CZK18,349	of coverage	of coverage
Date	07.09.2022	16.12.2022	29.05.2023	05.09.2022	03.03.2023	07.09.2022	25.02.2022
Price on the day of the publication	CZK923	CZK559	CZK244	CZK73.2	CZK17,200	CZK205.1	CZK270
Investment horizon	12 months	12 months	12 months	12 months	12 months		
Author	B. Trampota	B. Trampota	B. Trampota	B. Trampota	B. Trampota		
Overview of investment researches and recommendations for last 12M (quarterly)							
Recommendation	Buy	Buy	Buy	Buy	Buy	Buy	Buy
Target Price	CZK1,393	CZK645	CZK381	CZK109.7	CZK18,183	GBp600	CZK362
Date	07.06.2022	17.01.2022	12.05.2022	31.08.2021	11.02.2022	11.02.2021	26.03.2021
Recommendation	In revison	In revison	In revison	In revison	Buy	Buy	Buy
Target Price	In revison	In revison	In revison	In revison	CZK16,512	GBp466	CZK293
Date	10.05.2022	31.03.2021	15.02.2022	07.05.2021	20.11.2020	30.08.2019	08.01.2020
Recommendation	Buy	Buy	Buy	Buy	Buy	In revision	Buy
Target Price	CZK905	CZK357	CZK367	CZK97	CZK18,308	In revision	CZK298
Date	10.12.2021	27.11.2020	12.01.2021	29.10.2019	03.12.2018	14.08.2019	12.12.2018
Recommendation	Buy		In revision	Buy	Buy	Buy	Hold
Target Price	CZK621		In revision	CZK97	CZK17,546	GBp342	CZK270
Date	23.07.2020		26.11.2020	07.03.2019	22.08.2017	15.06.2018	18.08.2017
Valuation methods	DFCF	DFCF	DFCF	DFCF DDM ERM	DDM	DFCF	DFCF DDM
Frequency of rec. (per year)	once	once	once	once	once	once	once
Direct or indirect share (5% or more) of the issuer of the registered capital of KB	no	no	no	no	no	no	no
Other significant financial interest of KB and/or its linked persons in the issuer	no	no	no	no	no	no	no
KB direct or indirect share (0.5% or more) of the registered capital of the issuer.	no	no	no	no	no	no	no
Author's direct or indirect share (0.5% or more) of the registered capital of the issuer.	no	no	no	no	no	no	no
Signific. fin. interest in the issuer of the persons partic. in elaboration of inv. research and rec.	no	no	no	no	no	no	no
Relationships of Komerční banka with particular issuers							
KB Management or co- management of public offerings in the past 12 month	no	yes	no	no	no	no	no
Agreements or contractual relations for providing investment services with the issuer	KB can have concluded agreements with the issuer for providing investment services. This information is protected by bank secret and could not be disclosed.						
Agreement with the issuer on production and dissemination of the research	no	no	no	no	no	no	no
KB market making for common stocks of the issuer	no	no	no	no	no	no	no

Note: DFCF – Discounted free cash flow model, DDM – Discounted dividend model, ERM – Excess return model
Source: Economic & Strategy Research, Komerční banka