| Utility | Update | Czech Republic |

CEZ

Record electricity prices will have a positive effect

Buy

Price 10.12.21	**CZK 801**
12m target	**CZK 905**
Upside to TP	**13.1%**
Dividend	**CZK 44**
Total return	**18.6%**

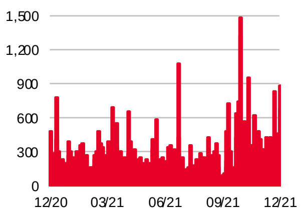
Sector stance
Overweight

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			460.5 - 837
Market cap. (CZKbn)			430.7
Market cap. (EURbn)			16.9
Free float (%)			30
Performance (%)	**1m**	**3m**	**12m**
Share	7.0	17.1	70.3
Rel. to PX Index	4.6	7.0	18.3

Source: Bloomberg

The latest analysis and report:
https://bit.ly/CEZ_upd2007ENG
https://bit.ly/CEZ_BGRexit_EN
https://bit.ly/CEZ_3Q21_results_EN

Investment case: We reiterated Buy recommendations for CEZ with a new target price of CZK905. The previous target price was CZK621.

Due to high inflation in energy commodity prices, there has been a significant rise in electricity prices. This should have a positive effect on CEZ's performance, especially from 2023. Due to the sharp increase, however, the effect should also be visible in next year's results. The planned closure of conventional emissions power plants across Europe is also positive for the price of electricity. CEZ's big advantage is that it produces more than half of its electricity from zero-emissions nuclear power plants. Combined with the upgraded coal power plants that CEZ feeds from its own mines, this means that CEZ possesses a relatively low emissions intensity and an indisputable competitive advantage in a period of high prices of emissions allowances. We anticipate the full use of nuclear power plants with minimal shutdowns only for refueling and standard maintenance. Investments should focus on renewables, the transformation of emissions production into low emissions, distribution and the development of ESCO services.

CEZ has a very attractive dividend policy. It distributes up to 100% of adjusted net profit among its shareholders. In addition, as this year, the payout next year will be increased by part of the funds from the sale of Bulgarian assets.

We used the discounted cash flow method to valuate CEZ shares. We estimated the fair value at the level of CZK854, the target price is then set 6% higher at CZK905 due to the sector recommendation Overweight and the attractiveness of the company. The stock is traded at multiples of 2022 P/E 17.3x vs. Western European utilities 13.6x (all of Europe 12.6x), 2022 EV/EBITDA 8.5x vs. 8.5x (7.9x) with a dividend yield of 5.5% vs. 4.5% (4.2%).

Major risks: The main risks clearly include the availability of production facilities, especially nuclear power plants, where margins are highest, and a decline in the price of electricity. Due to pre-sales for the coming years, it would not affect the economy immediately, but with a delay. However, we do not expect electricity prices to fall over the 2025 horizon. On the contrary, they should remain at high levels. Compared to the prices of recent years, these should be record levels.

Financial data	2020	2021f	2022f	2023f
Revenues (CZK bn)	213.7	214.9	240.7	243.9
EBITDA margin (%)	30.3	27.9	27.6	29.5
Net income (CZK bn)	5.5	8.7	24.4	28.8
EPS (CZK)	42.6	39.9	46.4	54.6
Dividend/share (CZK)	34.0	52.0	44.0	46.0
Interest cover (x)	2.6	4.7	9.6	11.2
Payout (%)	96.8	122.7	110.7	99.5
Net debt/equity (%)	0.6	0.6	0.6	0.6

Ratios	2020	2021f	2022f	2023f
P/E (x)	12.1	18.7	16.1	13.7
Price/free cash flow (x)	5.0	7.5	15.7	18.1
Dividend yield (%)	6.6	7.0	5.9	6.2
Price/book value (x)	1.2	1.9	1.9	1.8
P/S (x)	1.3	1.9	1.7	1.6
EV/S (x)	2.0	2.5	2.2	2.2
EV/EBITDA (x)	6.6	9.0	8.1	7.4
EV/IC (x)	1.2	1.6	1.6	1.6

Upcoming events: CEZ's results for the full-year 2021 should be published in March 2022.

SOCIETE GENERALE GROUP

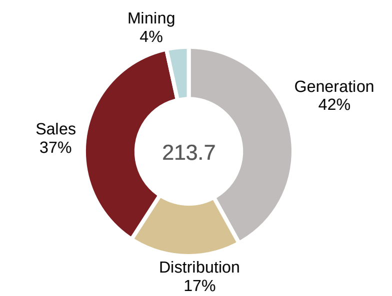
Bohumil Trampota
(420) 222 008 560
bohumil_trampota@kb.cz

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

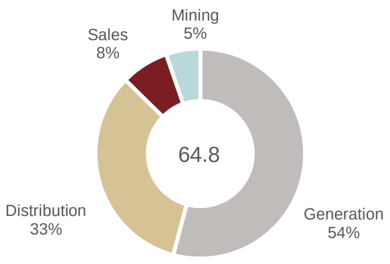
Opportunities	Threats
▪ Dividend policy with a chance of extraordinary dividend payment ▪ Subsidies from the Modernisation Fund for investments in RES ▪ Increasing carbon prices with a positive impact on CEZ profitability due to the anticipated decrease in their needs ▪ Closure of nuclear and coal-fired power plants in Western Europe	▪ 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 ▪ Sector taxation or other form of levy on the state budget or the specialised fund

2020 revenues by segment



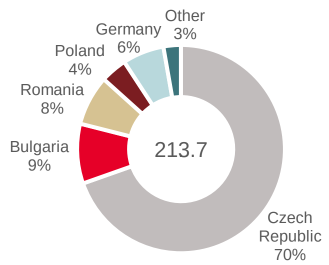
Source: CEZ; * figures are in CZKbn

2020 EBITDA by segment



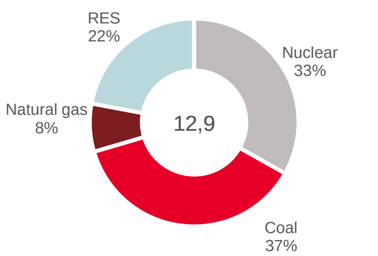
Source: CEZ; * figures are in CZKbn

2020 revenues by region



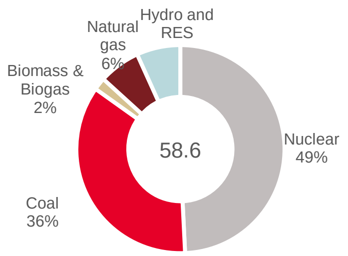
Source: CEZ; * figures are in CZKbn

2020 installed capacity by fuel



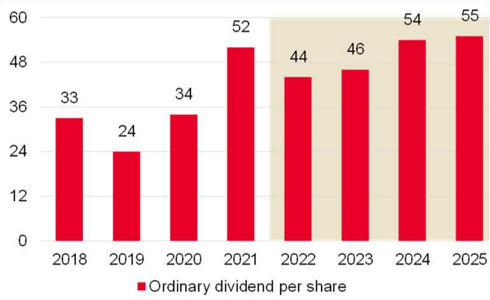
Source: CEZ;* figure is in GW

2020 electricity generation by fuel



Source: CEZ;* figure is in TWh

Dividend per share (CZK)



Source: CEZ; Economic & Strategy Research, Komerční banka

Sector trends

Electricity prices

Power prices have literally skyrocketed this year, easily surpassing historical highs. At the beginning of the year, electricity traded at €50 per MWh. Now the price is around €180, which means about +260% since the beginning of the year. There was a sharp increase in the second half of 2021. Not surprisingly, this is due to the growth of energy commodities. Especially gas, but of course also emissions allowances and coal. Of course, the ongoing decommissioning of conventional power plants, especially nuclear power plants, not only in Germany, does not help. Everyone is asking whether the decommissioned capacity can be fully replaced and with what.

Futures contracts suggest that in the coming years the price should fall to about €80 per MWh.

Gas

Record gas prices due to supply uncertainty.

The price of gas has risen 400% since the beginning of the year to €92 per MWh from €19. In October, the price even exceeded €120, followed by a correction for today's quotations. Growth began in the first half of the year. The storage tanks were, after last winter, not filled as a year ago. But the main reason is probably that there is a question mark over deliveries before the current winter season. According to futures contracts, the price of gas should gradually fall back to €20.

CO_2 Emissions allowances

Emissions allowed at all-time highs.

Now the price of the CO_2 allowance is at all-time highs just below €80 per tonne from €30 at the beginning of the year. This means growth of almost 170%. Behind this is the large growth in demand associated with the economic recovery from the pandemic lockdown. This, combined with lower supply and certainly with the help of investors speculating on growth, meant current growth. Stricter greenhouse gas reduction targets have certainly not helped either.

We note that the emissions trading system is a political project that was intended to protect the environment. Due to the high surplus, the so-called Market Stability Reserve (MSR), which regulates the surplus of allowances, started operating in 2019.

Coal

The price of coal has also risen significantly.

At the beginning of the year, coal cost $70 per ton. At the beginning of October, the price reached $190, followed by a correction to $106. In relative terms, this means "moderate" +50% YTD growth compared to the other commodities mentioned. The reason is the high demand stemming from China, which has stopped taking coal from Australia due to the political situation.

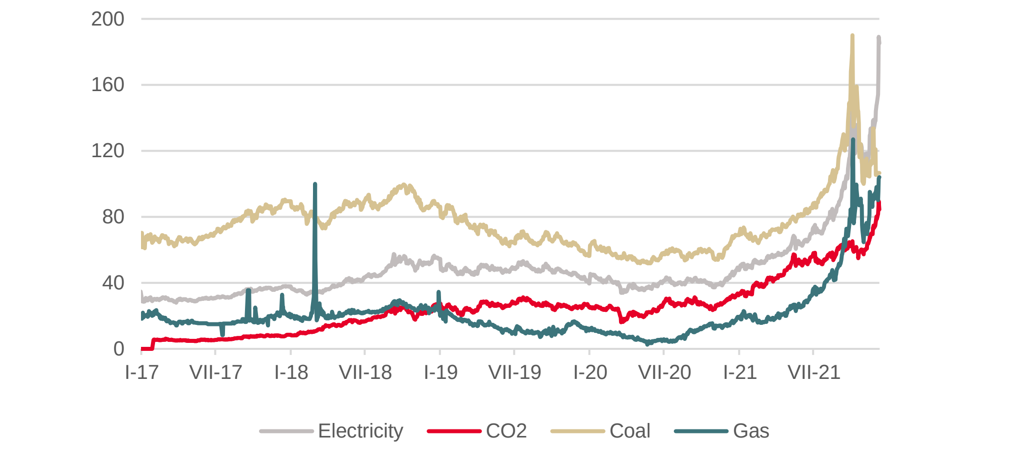
Power plant closures

Decommissioning of conventional power plants.

The closure of conventional coal and nuclear power plants is taking place, not only in Germany. Germany will close its last nuclear power plant at the end of next year. And the new government, in which the Greens are represented, plans to end coal production as early as 2030. This is a significant difference from the 2038 that Merkel's cabinet had anticipated. Missing capacity should be replaced with renewables, probably in combination with gas-fired power plants. Last year, renewable sources generated 50.5% of electricity. However, in the first half of this year, the production of renewable resources fell to 44%.

The potential lack of stable sources is one of the reasons for rising electricity prices. By their very nature, renewables may not be able to fully compensate for the reduction in conventional capacity.

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

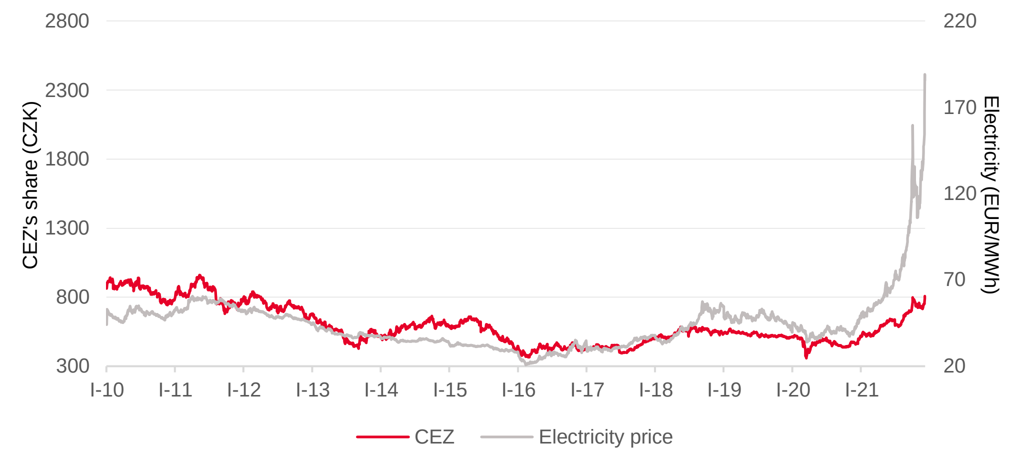


Source: Bloomberg

CEZ's share price lags behind the power price.

CEZ's results respond to the growth or changes in the price of electricity with a delay. This is due to the company's policy of hedging for years to come. The company's shares have historically more or less correlated with the development of power prices. Recently, there has been some divergence in the last three years. In 2019 and 2020, this was the uncertainty arising from the planned completion of a new nuclear power plant. The construction of the core should not have a negative impact on CEZ. We describe this below. And this year there was a sharp rise in electricity prices, to which CEZ shares did not react. The reason is the inflation of energy commodities; emissions allowances, coal and especially gas.

Development of CEZ's shares vs. German electricity prices



Source: Bloomberg

Company results

The year 2020

Guidance for this year has increased again. The EBITDA target is CZK59-60bn and net profit is CZK19-21bn.

Whenever CEZ has reported quarterly results this year, the full-year goals were also increased. The last time this happened was on November 9. EBITDA profit should now be in the range of CZK59-60bn (previous CZK58-60bn). In terms of net profit, the company is expected to deliverer CZK19-21bn (previous CZK18-20bn). The reasons for the increase in the projection are the higher profit from commodity trading and interest related to the refunded overpayment of the gift tax on emissions allowances, which will only affect net profit. In our opinion, the biggest risk is the availability of generating facilities. We assume CEZ will meet its guidance.

In our estimates, we expect EBITDA at the upper end of CEZ's target at CZK59.9bn. In terms of net profit, our projections assume CZK21.4bn, which is slightly above the company's target. Total revenues should then be CZK214.9bn. The volume of electricity production should fall to 55.7 TWh from 60.9 TWh. The decline is due to the sale of the Romanian wind farm, i.e. a decrease in production from renewable sources. For coal, this is the sale and closure of some power plants. For gas, high prices for both gas and emissions allowances. Unfortunately, this will not be able to compensate for the higher production in nuclear power plants. In a year-on-year comparison, electricity sales prices will be higher. These should climb to €52 / MWh for 2021 from €45.5 in 2020. In the distribution segment, we estimate a slight decrease in the volume of electricity distributed and sold to end customers. The mining sector will also be lower due to lower production, especially of own coal-fired power plants.

KB estimates of 2021 results

CZKbn	2020	2021e	change
Revenues	213.7	214.9	0.5%
EBITDA	64.8	59.9	-7.5%
EBIT	12.6	19.0	50.6%
Net profit	5.5	8.7	59.4%
Adjusted net profit	22.8	21.4	-6.2%

Source: CEZ, Economic & Strategy Research, Komerční banka

Divestment of Romanian and Bulgarian assets

CEZ completed the sale of Romanian and Bulgarian assets this year.

At the end of the first quarter, CEZ managed to complete the sale of Romanian assets. These were the Fântânele and Cogealac wind farms and a sales and distribution company. We remind you that about a third of these funds were paid to shareholders in addition to the standard dividend.

The sale of Bulgarian assets (distribution and sale) took place at the end of July. The sale price is €335 million, which is approx. CZK8.6bn or CZK16 per share. As in the case of Romania, we expect CEZ to pay part of the proceeds to shareholders. See below - dividend.

The sale of Polish assets is cancelled.

In addition to assets in the Balkans, CEZ is also trying to sell Polish heating plants. Unfortunately, due to the low prices offered, the sale was stopped and CEZ will continue to operate them.

Turkish operations have also been sold for many years, but even in this case without success.

The possible construction of a new nuclear unit should be 100% financed by the state.

Construction of a new nuclear unit

The uncertainty associated with the construction of a new nuclear unit had a negative effect on CEZ's share price. **The new nuclear units should be 100% state-funded.**

The decision to build a new nuclear bloc should be made by the new government that is now being formed. The tender, which will probably be announced next year, should be attended by three applicants: the French EdF, the Canadian Westinghouse and the Korean company KHNP. All three applicants received a security questionnaire, which they returned in November. Now it is necessary to evaluate them, and the government will decide on the future. We assume that the whole project must also be approved by the EU.

If this gigantic project is implemented, we would divide it into two parts, administrative, where it is necessary to solve all the paperwork and the actual implementation of the construction. Both should last about 10 years. The first, administrative, part could end around 2029. The construction phase and its completion is expected around 2036. We remind you that all current constructions of new nuclear units are much longer and more expensive. These dates seem really optimistic to us. The first phase involves minimal capital investment. However, with the physical construction, which should begin in almost 10 years, the investment costs will skyrocket.

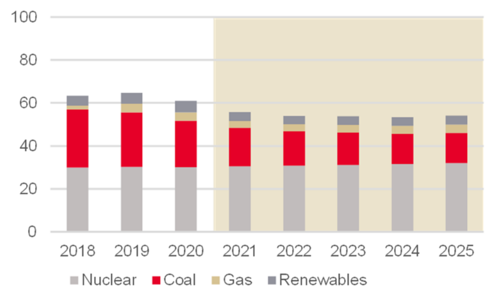
If it starts at all, the government will change several times during the first administrative phase. We cannot estimate how and if a new block will be built. However, it should be funded entirely by the state. So the threat of CEZ itself participating in this very risky project has disappeared. If the new nuclear unit were actually built, CEZ would provide its know-how and operate the unit and of course, it would collect a management fee.

Long-term forecasts

Increasing production from renewable sources and nuclear power plants. Decrease of electricity generated from coal.

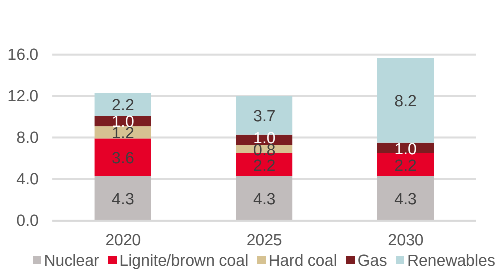
Existing nuclear power plants will have a significant share in CEZ's electricity production. We expect the shortest possible shutdowns for the necessary tasks (fuel change, regular inspections/repairs). Production should reach up to 32 TWh in 2025 from this year's expected 30.5 TWh. We do not expect to expand the portfolio of nuclear power plants. As for emissions sources, especially coal production, it should gradually decrease. The installed capacity of coal-fired power plants will be reduced to 3.0 GW in 2025 and 2.2 GW in 2030 from 4.8 GW in 2020. Only the retrofitted power plants in Prunerov, Tusimice and Ledvice should operate. Sources without state-of-the-art equipment and coal-fed from CEZ's own Severoceske doly will be shut down. From 2038, no coal-fired power plants should be in operation. We expect the installed capacity of the CCGT plant, which is relatively new, to be around 1 GW without changes. Production from renewable sources will fall significantly this year. This is due to the sale of the Romanian wind farm at the end of the first quarter. Gradually, however, it should increase again. The development of RES will also be supported by subsidies from the Modernization Fund. From 2.2 GW of installed capacity in 2020, capacity should increase in 2025 to 3.7 GW.

CEZ electricity generation (TWh)



Source: CEZ, Economic & Strategy Research, Komerční banka

CEZ generation capacity estimate (GW)



Source: CEZ, Economic & Strategy Research, Komerční banka

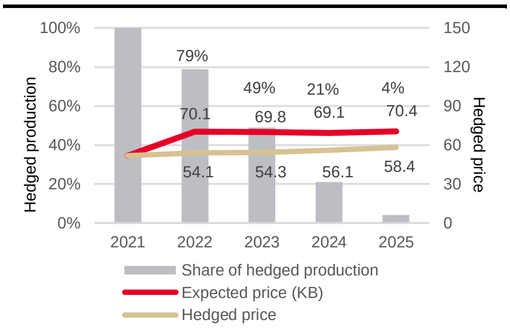
Realised prices will increase

The sharp rise in electricity prices will have a positive effect on company's numbers.

As can be seen from the chart on page 4, the price of electricity has been rising sharply since the beginning of this year. The reason is the rise in the prices of energy commodities, emissions allowances, coal and especially gas. At the beginning of the year, electricity was traded on the stock exchange for about €50; now it is around €150. Given that CEZ sells electricity in advance, especially for the next two years, its price increase should not affect the company's finances until 2023. However, due to the huge increase, the positive effect will be visible also next year. However, the price of futures contracts for the following years is gradually falling from €180 for 2022 to €90 for 2025.

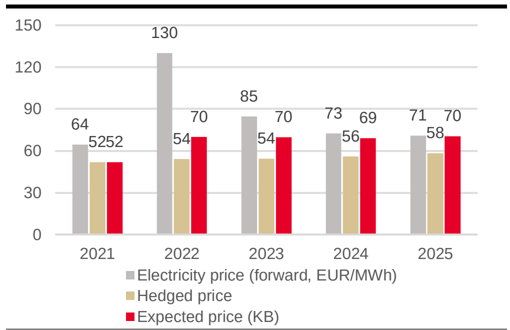
This year, CEZ sold about €52 per MWh of electricity production. Next year, we expect growth of about 30% to €69. We estimate the selling price of the secured electricity supply (base load) in the following years at about €70 / MWh. However, the overall average price will be higher. It will also include peak load sales. The total price of electricity could thus reach the level of €80 or even higher. The lower right chart shows the hedged price, our estimates 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

CEZ's earnings projections

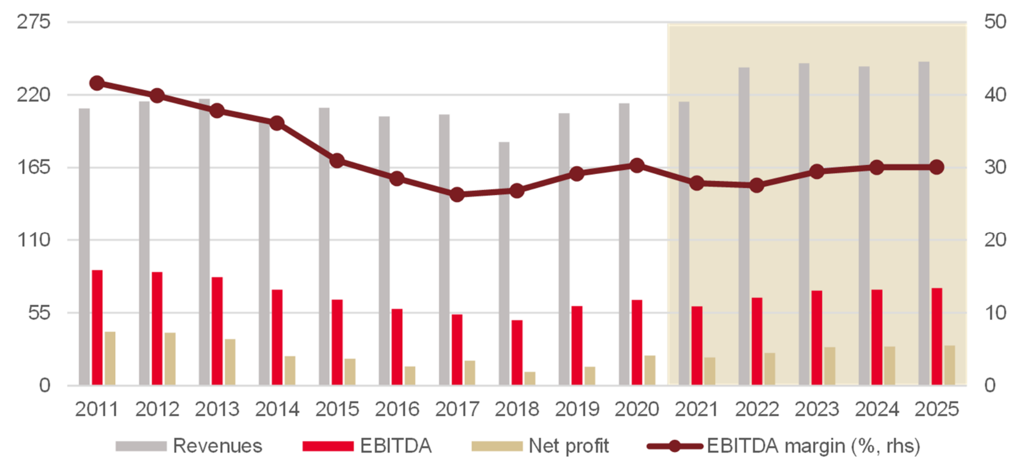
EBITDA is headed above CZK70bn.

In the forecasted period (2021-2025), we assume that sales will grow at an average annual rate of 3.3%. Of the CZK213.8bn reported in 2020, they should reach CZK244.6bn in 2025.

EBITDA in 2020 was CZK65bn. This year, we estimate this indicator at CZK60bn. The decline is due to sales of Bulgarian and especially Romanian assets. In our projections, we estimate average growth of 5.2%. In the last monitored year, EBITDA should reach CZK73.4bn. Management's projection for this year's result is CZK59-60bn.

Adjusted net profit should climb to CZK30.1bn in 2025. This year we expect CZK21.4bn after last year's CZK22.8bn. We remind you that adjusted net profit serves as the basis for calculating the dividend. Higher earnings mean higher dividends. See below.

CEZ results forecasts (CZKbn)



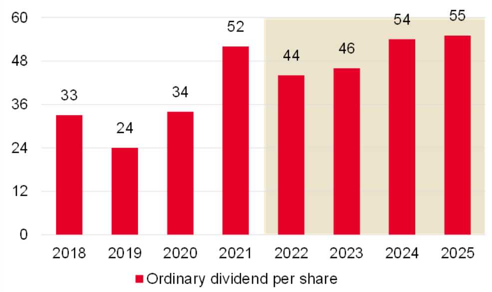
Source: CEZ, Economic & Strategy Research, Komerční banka

Dividend policy

In addition to the 100% payout of net profit, part of the funds from the sale of Bulgarian assets should be distributed.

The current dividend payout ratio is 80% to 100% of net profit adjusted for one-off effects. This year, CEZ paid CZK52 per share. This corresponds to 100% of consolidated net profit adjusted for extraordinary effects plus a portion of the funds from the sale of Romanian assets. (approx. CZK42 + CZK10). The dividend for next year, i.e. from this year's profit, will also be sweetened by the payment of funds from the sale of Bulgarian assets. We estimate that the total dividend could be CZK44 (CZK39 + 5). This would correspond to a gross yield of about 5.5%. Due to the expected economic growth and strong cash generation, we assume CEZ will be able to pay out more than CZK50. This should mean a gross dividend yield of around 7%.

Expected dividend payment per share (CZK)



Source: CEZ, Economic & Strategy Research, Komerční banka

Apart from next year, when there will be an extraordinary payout from the sale of Bulgarian assets, we do not expect another extra dividend. CEZ tried to sell its Polish assets, but that tender has been cancelled. Turkish operations have also failed to sell for a long time.

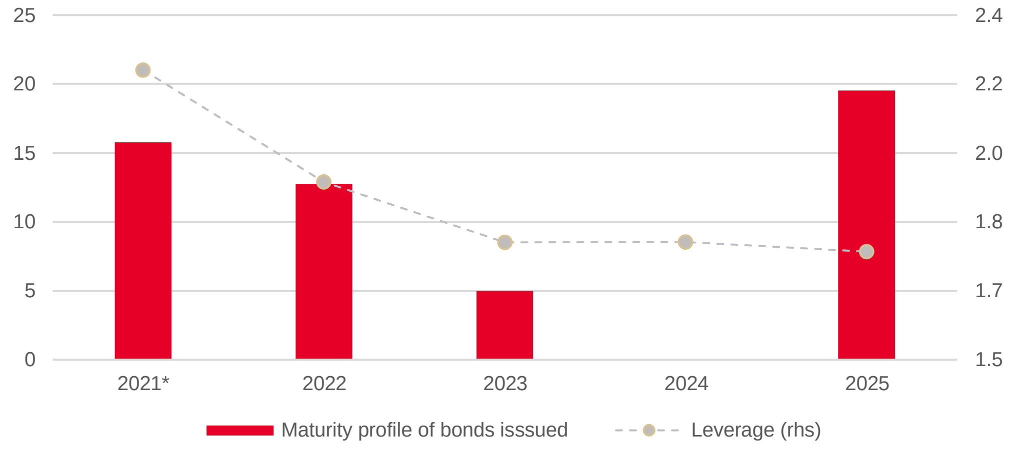
Indebtedness

Leverage is comfortable. Lower debt service due to cheaper refinancing.

CEZ's goal is to keep its leverage below 3.0 times (net debt to EBITDA). According to management forecasts, it should reach 2.5x in 2025 and 3.0x in 2030. In the first nine months of this year, the debt is 2.1x and therefore remains comfortably within the targeted range.

In the coming years, CEZ expects debt refinancing in the order of approximately CZK40bn. This could translate into lower interest costs. While in 2020 CEZ paid CZK5.3bn in interest, in the coming years we estimate that debt service will be around CZK4.2bn.

Maturity profile of the issued bonds (CZKbn)



Source: CEZ, Economic & Strategy Research, Komerční banka

Valuation

Sector comparison

CEZ is trading mixed with the sector. The high dividend stands out.

We compared the current market valuation of CEZ shares with the development of its competitors in Western and Central Europe. The following table shows that the valuation is much closer to the valuation of companies in Western Europe. P/E and EV/EBITDA multiples are mixed. For forward indicators, CEZ is traded with a slight discount to its competitors. In addition, it offers a high dividend yield.

Peer comparison

	P/E akt.	P/E 2022	P/E 2023	P/S akt.	P/S 2022	EV/ Sales 2022	EV/ Sales 2023	EV/ EBITDA akt.	EV/ EBITDA 2022	EV/ EBITDA 2023	Div. yield akt.	Div. yield 2022	Div. yield 2023
ČEZ (KB estimate)	**20.2**	**17.3**	**14.8**	**2.0**	**1.8**	**2.4**	**2.3**	**9.5**	**8.5**	**7.9**	**5.1**	**5.5**	**5.7**
ČEZ (consensus)	**n/a**	**24.5**	**17.4**	**2.0**	**2.1**	**2.7**	**2.6**	**15.9**	**9.5**	**8.4**	**5.1**	**6.5**	**6.5**
EDP - Energias de Portugal SA	20.0	23.2	20.6	1.4	n/a	2.8	2.6	10.1	10.3	9.6	3.9	4.4	5.4
E.ON SE	7.7	12.7	12.5	0.4	n/a	0.9	0.9	6.8	7.7	7.8	4.2	4.4	4.6
Electricite de France SA	7.1	9.3	8.4	0.5	n/a	1.2	1.1	5.1	4.8	4.3	5.8	5.6	8.2
Endesa SA	15.6	12.5	12.2	0.9	n/a	1.5	1.5	7.9	7.6	7.3	6.0	6.9	6.6
Enel SpA	30.3	12.3	11.9	0.9	1.0	2.3	2.2	11.8	9.2	8.8	5.9	5.7	6.0
Engie SA	n/a	10.9	10.5	0.5	n/a	1.0	1.0	7.7	5.6	5.5	4.1	7.2	8.0
EVN AG	22.6	18.4	18.3	2.1	n/a	2.4	2.3	9.8	8.2	8.5	n/a	1.9	1.9
Fortum Oyj	87.4	14.6	16.9	0.3	0.3	0.5	0.4	n/a	8.8	9.5	4.1	4.2	4.6
Iberdrola SA	19.0	17.2	15.4	1.7	n/a	3.3	3.1	11.9	11.2	10.3	5.7	4.7	5.1
RWE AG	n/a	18.9	18.6	1.4	n/a	1.9	1.9	12.8	9.3	8.8	0.9	2.6	2.8
Verbund AG	45.9	44.0	31.1	13.6	n/a	11.5	9.4	25.5	23.8	17.8	n/a	1.3	1.8
MEDIAN Western Europe	**20.8**	**13.6**	**14.0**	**0.9**	**0.6**	**1.7**	**1.7**	**9.8**	**8.5**	**8.6**	**4.9**	**4.6**	**4.8**
PGE Polska Grupa Energetyczna	3.9	4.8	13.3	0.3	0.4	0.4	0.4	2.1	2.1	2.9	0.0	0.0	0.0
Energa SA	2.7	n/a	n/a	0.2	n/a	n/a	n/a	3.4	n/a	n/a	n/a	0.0	0.0
Enea SA	n/a	2.8	3.5	0.2	0.2	0.3	0.3	11.6	1.7	1.9	0.0	0.0	0.0
Tauron Polska Energia SA	n/a	4.7	5.5	0.2	0.2	0.8	0.7	53.8	4.1	4.8	0.0	0.0	0.0
MEDIAN Central Europe	**3.3**	**4.7**	**5.5**	**0.2**	**0.2**	**0.4**	**0.4**	**7.5**	**2.1**	**2.9**	**0.0**	**0.0**	**0.0**
SECTOR MEDIAN	**19.0**	**12.6**	**12.9**	**0.5**	**0.3**	**1.3**	**1.3**	**9.9**	**7.9**	**8.1**	**4.1**	**4.2**	**4.6**
ČEZ vs. sector (consensus)	*0%*	*94%*	*34%*	*284%*	*616%*	*103%*	*100%*	*60%*	*19%*	*3%*	*23%*	*54%*	*42%*
ČEZ vs. sector (KB estimate)	*7%*	*37%*	*14%*	*284%*	*519%*	*76%*	*81%*	*-4%*	*7%*	*-3%*	*23%*	*30%*	*25%*

Source: Bloomberg, Economic & Strategy Research, Komerční banka

Target price

We used the DCF model to value the company and set a target price of CZK905 per share.

To determine the fair value of the company's shares, we used the discounted free cash flow model until 2025, the main parameters and outputs of which are shown in the table on the following page. Based on our model, we estimate the fair value of the company's shares at CZK854 per share. To achieve the target price, we reflect three parameters that may be assigned values ranging from -10% to +10% each, which means the target price may range from 70% to 130% of the fair value.

- **Sector appeal (+3%):** Our parent company Société Générale recommends overweighting the utilities sector as a defensive segment and due to the interesting dividend yield. We keep this factor at +3%.
- **Company appeal (+3%):** The shares offer an interesting dividend yield. In our opinion, the 100% payout ratio is sustainable. The eventual implementation of a new nuclear source should be fully under the control of the state and the dividend will therefore not be endangered. Furthermore, CEZ has a clear plan to transform it into low emissions production, develop renewable resources and constantly modernise its operations. We increase this factor to +3%.

▪ **Speculative appeal (0%):** CEZ shares are traded mixed compared to the closesed peers. For the coming years, the multiples are more or less comparable to Western European competitors.

Using the above parameters, we increased the target price for CEZ shares to CZK905 (fair value plus 6%). One of the main arguments is the positive impact of higher electricity prices and cash flow generation.

CEZ valuation

	2021	2022	2023	2024	2025	
	2021	**2022**	**2023**	**2024**	**2025**	**LT**
Calculation of the required rate of return						
risk-free rate	2.0%	3.4%	3.1%	2.8%	2.8%	2.8%
beta	0.81	0.81	0.81	0.81	0.81	0.81
equity risk premium	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%
country risk premium	0.6%	0.6%	0.6%	0.6%	0.6%	0.6%
cost of equity	6.9%	8.2%	8.0%	7.7%	7.7%	7.7%
weight of debt	37.7%	36.9%	36.4%	36.6%	36.7%	36.7%
cost of debt (after tax)	2.5%	2.9%	2.8%	2.8%	2.8%	2.8%
WACC	**5.2%**	**6.3%**	**6.1%**	**5.9%**	**5.9%**	**5.9%**
Discounted cash flow model (CZKbn)						
EBITDA	59.9	66.6	71.9	72.6	73.7	
Amortization of nuclear fuel	4.2	4.3	4.3	4.4	4.4	
Taxes paid	-5.2	-7.4	-8.6	-8.8	-8.9	
Change in working capital and provisions	29.5	2.3	-5.5	-2.7	-1.6	
CAPEX	-35.0	-40.0	-40.0	-40.0	-40.0	
FCFF	**53.5**	**25.8**	**22.0**	**25.4**	**27.6**	
price / free cash flow	8.1	16.8	19.6	17.0	15.7	
Present value of FCFF	50.8	23.1	18.6	20.2	20.7	
Sum of present values of FCFF until 2025	133.5					
Present value of FCFF after 2025	546.1					
Net debt	145.8					
Nuclear, mining and other provisions	80.7					
Financial investments	3.5					
Joint ventures and associates	4.1					
Minorities	1.2					
Estimated value of equity	459.5					
Fair value (CZK per share)	854					
Target price (CZK per share)	**905**					

Source: Economic & Strategy Research, Komerční banka

The following table provides a snapshot of the sensitivity of CEZ's target price to changes in WACC and the long-term growth rate.

Sensitivity analysis

Long-term growth	WACC 4.9%	5.4%	5.9%	6.4%	6.9%
1.0%	908	780	678	595	526
1.5%	1075	908	780	678	595
2.0%	1294	1071	**905**	778	676
2.5%	1618	1299	1075	908	780
3.0%	2109	1618	1299	1075	908

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 reform** – From time to time, politicians appear to increase taxation on big companies. There is no additional tax on energy companies on the table for now. However, the introduction of a sectoral tax would result in lower net profit, which would be reflected in a lower dividend payout.

CEZ financials

CZKm	2017	2018	2019	2020	2021f	2022f	2023f	2024f	2025f
INCOME STATEMENT									
Sales	205,092	184,486	206,192	213,737	214,869	241,133	243,947	241,478	245,185
Cost of materials, services and fuel	-127,126	-105,564	-118,395	-120,320	-120,815	-135,410	-135,866	-134,481	-136,702
Salaries (total)	-22,086	-25,620	-28,820	-30,855	-30,398	-31,918	-32,556	-33,207	-33,539
Other costs	-1,938	-4,213	-6,282	-3,753	-3,337	-7,234	-3,659	-1,207	-1,226
EBITDA	53,921	49,535	60,175	64,783	59,915	66,571	71,865	72,582	73,717
D&A and impairments	-29,535	-29,905	-33,876	-52,346	-40,956	-29,436	-29,286	-28,994	-29,432
Operating profit (loss)	25,620	19,759	26,429	12,585	18,959	37,135	42,580	43,588	44,285
Interest income	235	315	403	377	321	358	393	411	423
Interest expense	-3,761	-5,177	-5,473	-5,269	-4,313	-4,207	-4,182	-4,157	-4,132
Interest on provisions	-1,618	-1,800	-1,893	-1,955	-2,131	-2,173	-2,297	-2,814	-2,958
Other financial income/expense	2,277	420	-1,055	2,168	204	-500	-500	-500	-400
Profit (loss) before taxes	22,753	13,517	18,411	7,906	13,040	30,612	35,993	36,528	37,218
Taxes	-3,794	-3,017	-3,911	-2,438	-4,324	-6,122	-7,199	-7,306	-7,444
Net profit (loss)	18,959	10,500	14,500	5,468	8,716	24,490	28,794	29,222	29,775
Impairments	-1,741	-2,600	-4,400	-17,332	-12,665	-500	-500	-500	-500
Guided net profit (loss)	20,700	13,100	18,900	22,800	21,381	24,990	29,294	29,722	30,275
BALANCE SHEET									
Share Capital	49,722	50,265	50,914	50,954	50,954	50,954	50,954	50,954	50,954
Retained Earnings	200,296	184,456	199,847	182,917	163,775	164,692	168,842	169,135	169,444
Shareholders' Funds	250,018	234,721	250,761	233,871	214,729	215,646	219,796	220,089	220,398
Long-term Debt	132,475	142,440	142,570	122,102	115,997	115,417	114,840	114,266	113,694
Other Long-term Liabilities	3,335	31	31	34	34	34	34	34	34
Capital Employed	385,828	377,192	393,362	356,007	330,760	331,097	334,670	334,389	334,126
Fixed Assets	428,019	415,908	428,088	410,372	402,617	406,564	410,003	413,854	417,702
Intangible Assets	26,804	31,127	37,429	24,244	32,553	34,087	35,622	37,156	38,691
Financial Investments	74,961	142,943	113,332	138,768	117,758	102,555	104,194	105,863	107,561
Cash and Marketable Securities	12,623	7,278	9,755	6,064	12,753	16,148	15,326	13,039	11,864
Inventories	18,716	26,458	37,682	48,951	66,738	67,188	70,035	87,659	87,150
Receivables	53,027	73,855	67,218	65,140	66,574	74,325	75,255	74,470	75,608
Other Assets	9,756	9,874	11,070	8,919	9,097	9,370	9,651	9,941	10,239
Short Term Debt	21,832	18,526	29,323	29,725	29,428	29,133	28,842	28,554	28,268
Payables	48,263	63,346	66,872	73,744	74,140	80,657	79,086	75,810	74,446
Trade Provisions	93,284	92,497	110,138	124,709	122,242	128,766	135,292	141,819	148,349
Other Liabilities	74,699	155,882	104,879	118,273	151,519	140,585	142,197	161,411	163,624
Capital Employed	385,828	377,192	393,362	356,007	330,760	331,097	334,670	334,389	334,126
Total assets	623,906	707,443	704,574	702,458	708,089	710,239	720,086	741,983	748,814
CASH FLOW									
Profit (loss) before taxes	22,753	13,517	18,411	7,906	13,040	30,612	35,993	36,528	37,218
Depreciation	29,305	28,139	29,016	28,284	28,291	28,936	28,786	28,494	28,932
Amortization of nuclear fuel	3,725	4,027	4,096	4,197	4,239	4,281	4,324	4,367	4,411
Other non-cash items	2,565	7,986	21,409	19,596	1,132	4,965	4,906	4,864	4,729
Change in working capital	-5,524	-10,396	-20,990	21,206	29,399	2,157	-5,630	-2,876	-1,732
Tax paid	-4,207	-3,327	-4,136	-3,748	-5,196	-7,357	-8,650	-8,779	-8,944
Interest paid, net	-3,286	-4,777	-5,023	-5,307	-3,992	-3,850	-3,790	-3,746	-3,709
Dividend received	481	182	148	23	23	23	23	23	23
Operating cash flow	45,812	35,351	42,931	72,157	66,935	59,767	55,962	58,876	60,927
Cash flow from investing activities	-20,212	-25,901	-32,363	-33,723	-4,611	-40,000	-40,000	-40,000	-40,000
Dividends paid	-17,859	-17,613	-12,861	-18,139	-27,858	-23,572	-24,644	-28,930	-29,466
Cash flow from financing activities	-24,203	-14,795	-8,091	-42,125	-55,635	-16,372	-16,784	-21,162	-22,102
Change in cash	1,397	-5,345	2,477	-3,691	6,689	3,395	-822	-2,287	-1,175

Source: Economic & Strategy Research, Komerční banka

CEZ financials

	2017	2018	2019	2020	2021f	2022f	2023f	2024f	2025f
RATIOS (%)									
EBITDA margin	26.3	26.9	29.2	30.3	27.9	27.6	29.5	30.1	30.1
Operating margin	12.5	10.7	12.8	5.9	8.8	15.4	17.5	18.1	18.1
Pre-tax margin	11.1	7.3	8.9	3.7	6.1	12.7	14.8	15.1	15.2
Net margin (adjusted)	10.1	7.1	9.2	10.7	10.0	10.4	12.0	12.3	12.3
EBIT/Interest (x)	7.3	4.1	3.6	2.6	4.7	9.6	11.2	11.6	11.9
Net debt/Equity (x)	0.6	0.7	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Net debt/EBITDA (x)	2.6	3.1	2.7	2.3	2.2	1.9	1.8	1.8	1.8
ROE	8.2	5.4	7.8	9.4	9.5	11.6	13.5	13.5	13.7
ROA	3.3	2.0	2.7	3.2	3.0	3.5	4.1	4.1	4.1
ROCE	5.2	3.4	4.9	6.1	6.2	7.6	8.8	8.9	9.1
Dividend payout	90.4	85.8	98.6	96.8	122.7	110.7	99.0	99.2	99.6
DATA PER SHARE (CZK)									
EPS (adj.)	38.7	24.5	35.3	42.6	39.9	46.6	54.7	55.5	56.5
Book value	467.9	438.7	468.7	437.2	400.8	402.5	410.3	410.8	411.4
Free cash flow	53.9	31.2	18.0	103.8	99.8	48.1	41.2	47.5	51.5
Gross dividend	33.0	33.0	24.0	34.0	52.0	44.0	46.0	54.0	55.0
MARKET VALUATION									
P/E (x)	12.8	21.8	14.4	12.1	20.2	17.3	14.8	14.5	14.3
Price/Operating cash flow (x)	5.0	6.6	5.2	3.4	5.7	6.1	6.3	6.1	5.9
Price/free cash flow (x)	9.2	17.1	28.3	5.0	8.1	16.8	19.6	17.0	15.7
Price/book value (x)	1.1	1.2	1.1	1.2	2.0	2.0	2.0	2.0	2.0
Price/sales (x)	1.3	1.6	1.3	1.3	2.0	1.8	1.8	1.8	1.8
Dividend yield (%)	6.6	6.2	4.7	6.6	6.4	5.5	5.7	6.7	6.8
EV/revenues (x)	2.0	2.4	2.1	2.0	2.7	2.4	2.3	2.4	2.3
EV/EBITDA (x)	7.6	9.0	7.3	6.6	9.5	8.5	7.9	7.8	7.7
EV/IC (x)	1.1	1.2	1.1	1.2	1.7	1.7	1.7	1.7	1.7

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.

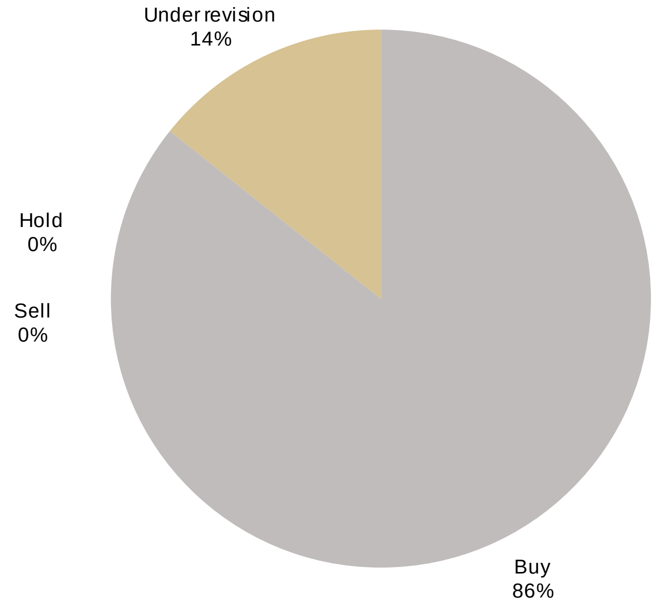
The recommendation in this document and/or the document itself was not disclosed to the issuer before its dissemination.

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

	Avast	Ceska zbrojovka	CEZ	Kofola	MONETA Money Bank	O2 CR	PFNon-wovens	Philip Morris CR	Vienna Insurance
Overview of last investment research and recommendations related to stocks of particular issuers									
Recommendation	Buy	In revison	Buy	Buy	Buy	Buy	End	Buy	End
Target price	GBp 600	In revison	CZK 905	CZK 367	CZK 109.7	CZK 362	of coverage	CZK 16 512	of coverage
Date	11.02.2021	31.03.2021	10.12.2021	12.01.2021	31.08.2021	26.03.2021	15.02.2021	20.11.2020	22.11.2019
Price on the day of the publication	CZK 147	CZK 370	CZK 802	CZK 246	CZK 87.1	CZK 259	CZK 800	CZK 14 320	EUR 24.7
Investment horizon	12 months		12 months	12 months	12 months	12 months		12 months	
Author	B. Trampota	B. Trampota	B. Trampota	B. Trampota	B. Trampota	B. Trampota		B. Trampota	
Overview of investment researches and recommendations for last 12M (quarterly)									
Recommendation	Buy	Buy	Buy	In revision	In revison	Buy	In revision	Buy	Buy
Target Price	GBp 466	CZK 357	CZK 621	In revision	In revison	CZK 293	In revision	CZK 18308	EUR 27
Date	30.08.2019	27.11.2020	23.07.2020	26.11.2020	07.05.2021	08.01.2020	30.04.2020	03.12.2018	11.09.2018
Recommendation	In revision		Buy	Buy	Buy	Buy	Buy	Buy	Buy
Target Price	In revision		CZK 717	CZK 482	CZK 97	CZK 298	CZK 924	CZK 17546	EUR 26
Date	14.08.2019		10.06.2019	04.07.2019	29.10.2019	12.12.2018	01.04.2019	22.08.2017	03.03.2017
Recommendation	Buy		Buy	Buy	Buy	Hold	Hold	Hold	
Target Price	GBp 342		CZK 620	CZK 484	CZK 97	CZK 270	CZK 924	CZK 13500	
Date	15.06.2018		11.06.2018	26.09.2018	07.03.2019	18.08.2017	26.10.2018	25.05.2017	
Recommendation			Buy		Buy	Hold	In revision	Buy	
Target Price			CZK 542		CZK 93	CZK 267	In revision	CZK13500	
Date			20.09.2017		06.03.2018	31.01.2017	17.05.2018	13.06.2016	
Valuation methods	DFCF	DFCF	DFCF	DFCF	DFCF DDM ERM	DFCF DDM	DFCF	DDM	DDM ERM
Frequency of rec. (per year)	once	once	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	no	no
Other significant financial interest of KB and/or its linked persons in the issuer	no	no	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	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	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	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	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	no	no
KB market making for common stocks of the issuer	no	no	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