

# Genex Power

## Solar not as bright but K2H is getting closer

### SPECULATIVE BUY

(no change)

Current price:	A\$0.23
Target price:	A\$0.30
Previous target:	A\$0.36
Up/downside:	30.4%
Reuters:	GNX.AX
Bloomberg:	GNX AU
Market cap:	US\$62.33m A\$92.42m
Average daily turnover:	US\$0.09m A\$0.13m
Current shares o/s	312.4m
Free float:	69.3%

#### Key changes in this note

FY20F revenue down by 11%.

KS1 maximum output down to 47.7MW.

K2H SPV capex up by 5%.



Price performance	1M	3M	12M
Absolute (%)	-11.5	0	-19.3
Relative (%)	-6.8	-1	-21.7

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Analyst(s) own shares in the following stock(s) mentioned in this report:

– Genex Power

- GNX generated positive EBITDA for the first time in FY19 but FY19 results weren't as strong as we hoped (NPAT -\$1.2m on our forecast). Output from the KS1 solar farm was less than forecast but this was offset by an R&D refund and liquidated damages from the KS1's contractor.
- We've reduced our estimated value of KS1 by 3cps due to output restrictions and costs from ancillary services charged by the market operator (AEMO).
- We've also increased our capex forecast for K2H by 5% to \$287.5m (GNX share) which lowers our value estimate by 3cps.
- SPECULATIVE BUY rating maintained and our price target is reduced to 30cps which offers 30% upside to current prices.

### GNX began generating EBITDA in FY19 but result a miss overall

EBITDA was up by \$7.1m on the back of a full year's production to generate \$5.6m compared to -\$1.7m in FY18. Frequency Control and Ancillary Services (FCAS) fees charged by AEMO reduced revenue more than we thought (these charges are netted off revenue in the accounts) and output was lower. There was an R&D refund (\$1.9m) and liquidated damages (\$2.4m) recovered from UGL which offset the misses so revenue was in line with our forecast but these items are one-offs. Net profit after tax was worse than we thought (-\$5.5m vs -\$3.3m) though, partly as a result of GNX not recognising tax assets from its FY19 loss.

### KS1 missed our forecast but we expect FY20 will be higher

KS1's energy output is less than we'd forecast and its registered maximum capacity has been reduced to 47.7MW. Over FY19, KS1 produced 126.8GWh of energy which is less than our forecast of 144.5GWh. Output from KS1 was lower in 2H19 than the first half (see Figure 3). Weather issues from North Queensland's wet season, including Cyclone Owen, affected the January to March quarter and then network issues curtailed output in the following quarter but these issues have been resolved. We have reduced our FY20 output forecast to 133.9GWh to allow for potential uncertainty in volumes.

### Pumped hydro capex forecast increased

We understand there have been some design changes to the K2H project that could increase the capital cost of the project. GNX hasn't released its costings but we've increased our estimate by 5% to \$287.5m (GNX share) to allow for it. This has reduced our estimated value of K2H by 3cps. We don't expect further increases to the project's cost as we understand that GNX has a fixed price agreement with its contractors which, without any further scope changes, will keep costs stable.

### Upside potential as K2H gets closer

Despite the downward revisions to our forecast the recent share price weakness offers substantial upside potential. There are two significant conditions outstanding for K2H: a transmission line agreement with the Queensland Government owned Powerlink and a binding offtake agreement with EnergyAustralia. GNX expects both of these items will be resolved in the next six months which we think will trigger a significant rerate upwards. We maintain our SPECULATIVE BUY rating and reduce our target price to 30cps with a potential 30% upside to the current price.

#### Financial Summary

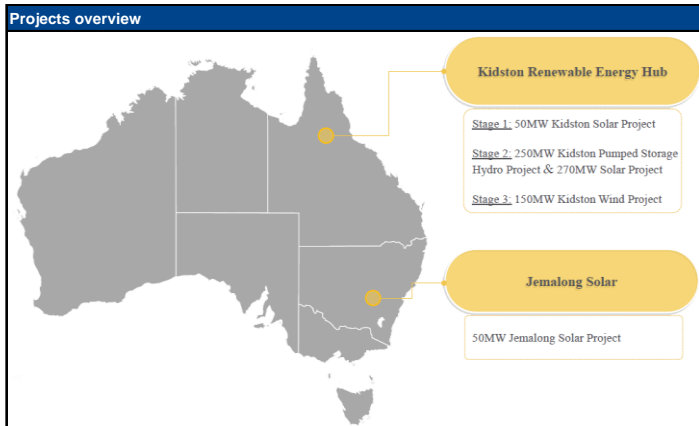
	Jun-18A	Jun-19A	Jun-20F	Jun-21F	Jun-22F
Revenue (A\$m)	8.27	10.82	18.58	24.39	23.86
Operating EBITDA (A\$m)	-1.72	5.59	15.18	20.31	19.71
Net Profit (A\$m)	-7.46	-5.48	12.06	4.02	2.37
Normalised EPS (A\$)	(0.025)	(0.018)	0.044	0.012	0.007
Normalised EPS Growth	(33.3%)	(28.8%)		(72.2%)	(41.2%)
FD Normalised P/E (x)	NA	NA	5.21	18.70	31.81
DPS (A\$)	-	-	-	-	0.004
Dividend Yield	0.00%	0.00%	0.00%	0.00%	1.65%
EV/EBITDA (x)	NA	30.62	18.64	14.45	14.28
P/FCFE (x)	NA	NA	NA	27.08	15.59
Net Gearing	596%	1187%	288%	262%	243%
P/BV (x)	4.57	8.51	1.60	1.51	1.50
ROE	(43.3%)	(46.2%)	45.7%	8.3%	4.7%
% Change In Normalised EPS Estimates			(6.5%)	(15.4%)	(68.3%)
Normalised EPS/consensus EPS (x)			6.31	-2.05	0.36

SOURCE: MORGANS, COMPANY REPORTS

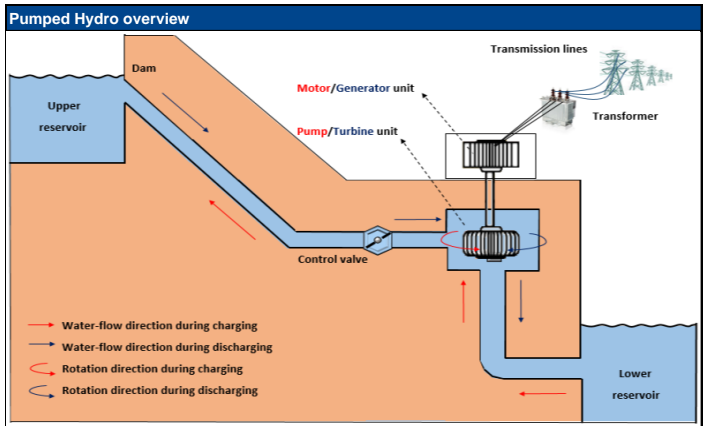
**Figure 1: Business snapshot**

Genex Power (as at 30-08-19)		GNX AU / GNX.AX	Utilities
Market cap (A\$m):	71.9	Rating:	SPECULATIVE BUY
Shares outstanding (m):	312.4	Price (A\$):	0.23
Free float (%):	69%	Target price (A\$):	0.30
Company website:	<a href="https://www.genexpower.com.au/">https://www.genexpower.com.au/</a>	Upside/downside to target price (%):	30.4%

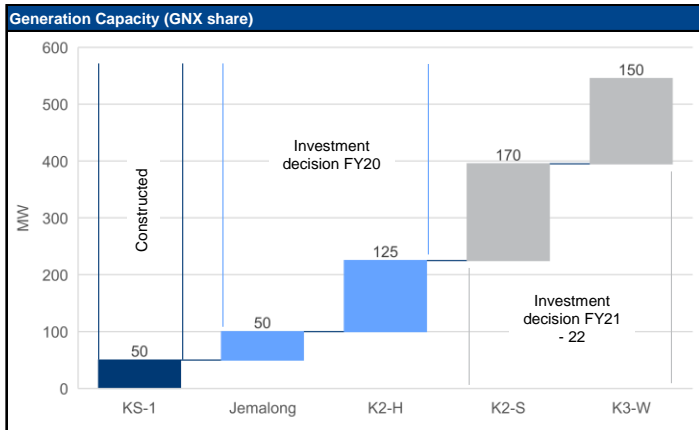
**Company description**  
 GNX is redeveloping an old gold mine in North Queensland into an energy storage project and has developed a 50MW solar farm adjacent to the mine. GNX also has plans to expand its energy generation with a second stage solar farm up to 270MW and a potential 150MW wind farm, on or near the same site, and a 50MW solar farm in central NSW. The output of the 50MW solar farm is contracted to the Qld government for 20 years and the company is in discussions with Energy Australia to develop and sell the output of the energy storage (pumped hydro) project for a term of at least 25 years. GNX has also obtained approval for up to \$610m of low cost debt finance from the Northern Australia Infrastructure Facility. GNX was founded in 2011 and was listed on the ASX in 2015. The CEO, James Harding, was appointed on the 7th of May 2018 and the Chairman, Dr Ralph Craven, has held his position since the company listed.



SOURCE: GNX



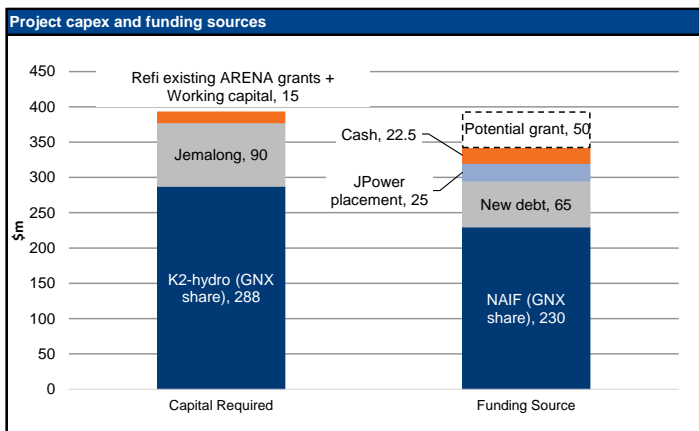
SOURCE: Journal of Power Technologies (2017)



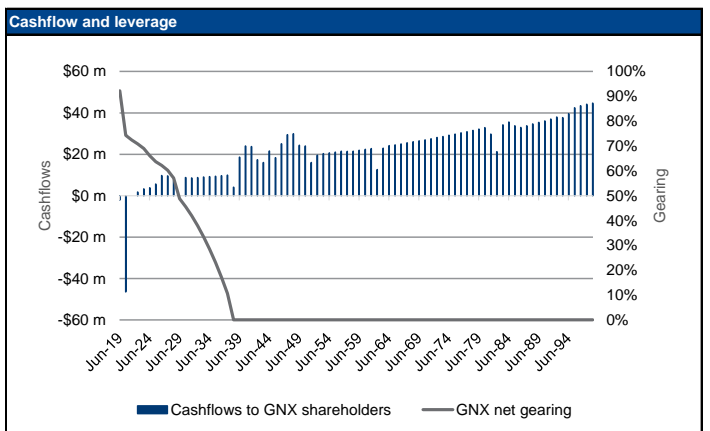
SOURCES: MORGANS, GNX

- Risks and Drivers**
- Value drivers:**
- Solar output of Stage 1 as price is contracted and locked in.
  - Price of the pumped hydro offtake agreement - not yet finalised.
  - NSW spot price of electricity as Jemalong will likely be uncontracted.
  - Spot price of LGCs as Jemalong will likely be uncontracted.
  - If carbon reduction targets increase, the value of future renewables projects will also increase.
- Risks:**
- Securing the final offtake agreement for the pumped hydro project at an attractive price.
  - Price of engineering contract to build K2-H pumped hydro project.
  - Cost to access new transmission line for K2-H pumped hydro project.
  - Construction risk during construction of the K2-H pumped hydro project.
  - Access to concessional funding (e.g. ARENA) to fund projects at low costs of capital.
  - Electricity network congestion if too many other renewables projects nearby get constructed.
  - Marginal Loss Factors (MLF) on all projects other than KS-1.
  - Technological changes driving energy efficiency and alternative generation.
  - Interest rates.
  - Changes to tax regimes.

SOURCE: MORGANS



SOURCES: MORGANS, GNX

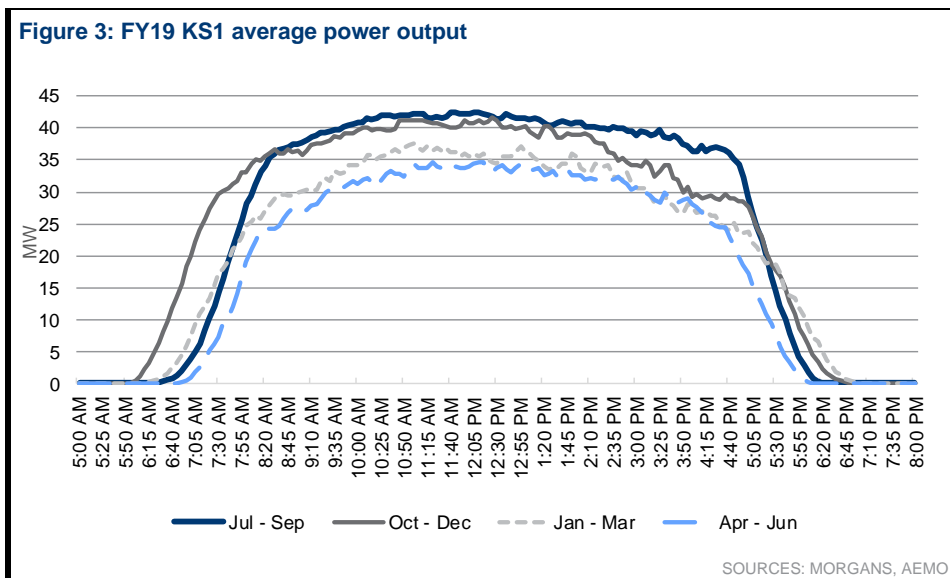


SOURCE: MORGANS

Figure 2: Financial summary

Key multiples & gearing	FY18A	FY19A	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E	FY26E	FY27E	FY28E
EV/EBITDA (x)	N/A	30.8	19.8	14.4	14.3	13.8	13.6	13.0	12.9	12.0	11.7
Price-to-earnings (x)	N/A	N/A	N/A	N/A	10	4.2	2.4	2.2	2.2	2.0	2.0
Dividend yield (%)	-	-	-	-	1.6	3.0	3.5	5.2	9.1	8.9	6.7
Net Debt / ND+E (%)	85.6	92.2	74.6	72.7	71.2	69.2	66.3	63.9	62.4	60.5	57.3
Profit and loss (\$m)	FY18A	FY19A	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E	FY26E	FY27E	FY28E
Net Revenue	8.3	10.8	18.6	24.4	23.9	23.9	23.7	24.0	23.6	24.5	24.2
Other inc	1.7	4.8	4.3	4.4	4.5	4.6	4.7	4.8	4.9	5.0	5.1
Expenses	(11.7)	(10.0)	(7.7)	(8.5)	(8.6)	(8.8)	(9.0)	(9.2)	(9.4)	(9.6)	(9.8)
EBITDA	(1.7)	5.6	15.2	20.3	19.7	19.6	19.3	19.5	19.1	19.9	19.5
D&A	(3.0)	(6.4)	(6.8)	(8.0)	(8.0)	(8.0)	(8.0)	(8.0)	(8.0)	(8.0)	(8.0)
Operating EBIT	(4.7)	(0.8)	8.3	12.3	11.7	11.6	11.4	11.6	11.2	11.9	11.6
Net Interest Expense	(2.7)	(4.7)	(4.9)	(5.3)	(5.0)	(4.7)	(4.4)	(4.1)	(3.9)	(3.6)	(3.3)
K2H equity accounted profit	-	-	13.8	(1.3)	(3.4)	0.9	6.9	7.3	7.6	8.0	8.3
Profit Before Tax	(7.5)	(5.5)	17.2	5.7	3.4	7.9	13.9	14.7	15.0	16.3	16.6
Tax	-	-	(5.2)	(1.7)	(1.0)	(2.4)	(4.2)	(4.4)	(4.5)	(4.9)	(5.0)
Statutory Net Profit	(7.5)	(5.5)	12.1	4.0	2.4	5.5	9.7	10.3	10.5	11.4	11.6
Exceptional items (post tax)	-	-	(9.7)	-	-	-	-	-	-	-	-
Underlying Net Profit	(7.5)	(5.5)	2.4	4.0	2.4	5.5	9.7	10.3	10.5	11.4	11.6
Cashflows (\$m)	FY18A	FY19A	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E	FY26E	FY27E	FY28E
EBITDA	(1.7)	5.6	15.2	20.3	19.7	19.6	19.3	19.5	19.1	19.9	19.5
K2H SPV distributions	-	-	-	-	-	-	-	-	6.4	5.6	5.2
WC & non-cash adjustments	(0.5)	(0.8)	5.0	(6.0)	0.0	0.0	(0.5)	(0.0)	0.0	(0.0)	0.0
Gross operating cashflow	(2.2)	4.8	20.2	14.3	19.7	19.6	18.8	19.5	25.5	25.4	24.8
Net interest paid	(3.9)	(4.3)	(4.9)	(5.3)	(5.0)	(4.7)	(4.4)	(4.1)	(3.9)	(3.6)	(3.3)
Cash paid for Tax	-	-	(0.9)	(1.7)	(1.0)	(1.4)	(2.1)	(2.2)	(4.1)	(4.2)	(4.0)
<b>Operating cashflow</b>	<b>(6.1)</b>	<b>0.5</b>	<b>14.4</b>	<b>7.3</b>	<b>13.7</b>	<b>13.5</b>	<b>12.3</b>	<b>13.2</b>	<b>17.6</b>	<b>17.7</b>	<b>17.4</b>
Capex (GNX not K2H SPV)	(82.3)	(12.3)	(145.0)	-	-	-	-	-	-	-	-
<b>Investing cashflow</b>	<b>(82.3)</b>	<b>(12.3)</b>	<b>(145.0)</b>	-	-	-	-	-	-	-	-
Equity issuance/(returns)	3.2	2.1	46.5	-	-	-	-	-	-	-	-
Debt drawdown/(repaid)	85.1	2.2	110.0	(3.3)	(6.8)	(7.0)	(7.3)	(7.6)	(7.8)	(8.1)	(8.4)
Dividends paid	-	-	-	-	(1.8)	(3.3)	(3.8)	(5.6)	(9.8)	(9.6)	(7.2)
<b>Financing cashflow</b>	<b>88.3</b>	<b>4.3</b>	<b>156.5</b>	<b>(3.3)</b>	<b>(8.6)</b>	<b>(10.3)</b>	<b>(11.1)</b>	<b>(13.2)</b>	<b>(17.6)</b>	<b>(17.7)</b>	<b>(15.6)</b>
<b>Net cashflow</b>	<b>(0.1)</b>	<b>(7.5)</b>	<b>25.9</b>	<b>4.0</b>	<b>5.1</b>	<b>3.3</b>	<b>1.3</b>	-	-	-	<b>1.8</b>
Balance sheet (\$m)	FY18A	FY19A	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E	FY26E	FY27E	FY28E
Cash	11.0	3.5	29.3	33.3	38.4	41.7	42.9	42.9	42.9	42.9	44.7
Receivables	0.9	2.0	1.3	1.2	1.2	1.2	2.5	2.5	2.5	2.6	2.5
Fixed Assets	118.2	113.3	196.4	188.4	180.5	172.5	164.5	156.6	148.6	140.6	132.7
SPV equity	-	1.9	70.7	69.4	66.0	67.0	73.9	81.2	82.5	84.9	88.0
Tax assets	-	-	-	-	-	-	-	-	-	-	-
Other	5.6	14.0	14.0	14.0	14.0	14.0	14.0	14.0	14.0	14.0	14.0
<b>Total Assets</b>	<b>135.6</b>	<b>134.5</b>	<b>311.7</b>	<b>306.3</b>	<b>300.1</b>	<b>296.3</b>	<b>297.8</b>	<b>297.1</b>	<b>290.5</b>	<b>285.0</b>	<b>281.9</b>
Debt	102.1	103.7	222.5	219.2	212.4	205.4	198.1	190.5	182.7	174.6	166.2
Deferred Tax from SPV)	-	-	4.3	4.3	4.3	5.2	7.3	9.5	9.9	10.6	11.6
Other liabilities	18.3	22.4	19.0	12.9	12.9	12.9	13.7	13.7	13.7	13.7	13.8
<b>Total Liabilities</b>	<b>120.4</b>	<b>126.1</b>	<b>245.8</b>	<b>236.4</b>	<b>229.6</b>	<b>223.5</b>	<b>219.0</b>	<b>213.7</b>	<b>206.3</b>	<b>199.0</b>	<b>191.5</b>
<b>Net Assets</b>	<b>15.3</b>	<b>8.4</b>	<b>65.9</b>	<b>69.9</b>	<b>70.5</b>	<b>72.8</b>	<b>78.7</b>	<b>83.4</b>	<b>84.2</b>	<b>86.0</b>	<b>90.4</b>
<b>Ave shares on issue (m)</b>	<b>303.9</b>	<b>312.4</b>	<b>467.4</b>	<b>467.4</b>	<b>467.4</b>	<b>467.4</b>	<b>467.4</b>	<b>467.4</b>	<b>467.4</b>	<b>467.4</b>	<b>467.4</b>

SOURCE: MORGANS RESEARCH, COMPANY



**Base case valuation**

Our base case valuation is a blend between a Free Cash Flow to Equity (FCFE) DCF and a multiples based valuation. Figure 4 summarises our sum-of-the-parts FCFE DCF which assumes a cost of equity of 8%.

Figure 5 summarises our multiples based valuation. Our key assumptions are:

- Jemalong and K2-H are completed by the end of FY23.
- K2-S and K3-W have been progressed but not completed and are valued on a lower multiple compared to Jemalong and KS1.
- The FY23 equity value is discounted at 8% pa to a FY20 basis.

Figure 4: GNX valuation sum of the parts			Figure 5: Base case summary – valuation on multiples					
Component	Value (\$m)	Value (cps)	Asset	MW	Multiple (\$ / W)	EV (\$m)	Debt (\$m)	Equity (\$m)
KS1 & Jemalong	16.7	5	Jemalong + KS1	97.7	2.4	236.4	(164.3)	72.1
GNX share of K2-H	50.6	16	K2-H	125	2.1	262.5	(230.0)	32.5
K2-S & K3-W	21.8	7	K2-S + K3-W	320	0.3	80.0	-	80.0
<b>Total</b>	<b>89.1</b>	<b>29</b>	<b>Total</b>	<b>542.7</b>	<b>1.1</b>	<b>578.9</b>	<b>(394.3)</b>	<b>184.6</b>
<b>Estimated future number of shares</b>								<b>467.4</b>
<b>Discounted equity value (cps)</b>								<b>31</b>

SOURCES: MORGANS SOURCE: MORGANS

Our combined base case valuation is a 50/50 weighting of the DCF and multiples based valuation and is therefore 30cps.

### Bull case valuation

Our key assumptions are:

- All projects are completed by FY23.
- The FY23 equity value is discounted at 8% pa to a FY20 basis.
- Multiples are based on the top quartile of comparable transactions.

**Figure 6: Bull case summary**

Asset	MW	Multiple (\$ / W)	EV (\$m)	Debt (\$m)	Equity (\$m)
Jemalong + KS1	97.7	3.1	302.9	(164.3)	138.5
K2-H	125	2.1	262.5	(230.0)	32.5
K2-S + K3-W	320	3.1	992.0	(440.0)	552.0
<b>Total</b>	<b>542.7</b>	<b>2.9</b>	<b>1,557.4</b>	<b>(834.3)</b>	<b>723.0</b>
<b>Estimated future number of shares (m)</b>					<b>1015.4</b>
<b>Discounted equity value (cps)</b>					<b>57</b>

SOURCE: MORGANS

### Bear case valuation

Our key assumptions are:

- Jemalong is completed.
- K2-H, K2-S and K3-W do not proceed.

**Figure 7: GNX valuation bear case**

Component	Value (\$m)	Value (cps)
KS1 & Jemalong	16.7	5

SOURCES: MORGANS

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Kedron	+61 7 3350 9000
Mackay	+61 7 4957 3033
Milton	+61 7 3114 8600
Noosa	+61 7 5449 9511
Redcliffe	+61 7 3897 3999
Rockhampton	+61 7 4922 5855
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Sydney: Reynolds	+61 2 9373 4452
Securities	
Sydney: Currency	+61 2 8216 5111
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