

Genex Power (ASX:GNX)

Excellent progress for Kidston green energy hub in North QLD

Key Facts

Company Code	GNX
Closing Price (10/8/17)	0.25
Price Target	0.57
Date of Report	11/8/17
Company Website	www.genexpower.com.au
Analyst	Johan Hedstrom

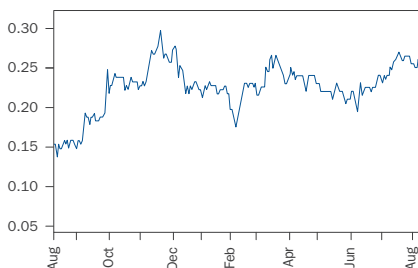
Company Statistics

12-Month Range	A\$0.15 - A\$0.31
Market Cap (A\$Mil)	A\$69m
Issued Shares	284
Issued Options	47
Cash (A\$Mil)	A\$16m

Major Shareholders

Shareholder	%
Zhefu Hydropower (China)	11.0%
Rivonia Pty Ltd	9.9%
Acorn Capital	8.7%
KFT Capital	7.3%

Share Price Performance



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Stage 1 Solar on schedule and budget for November generation

A site visit to Kidston has demonstrated very good progress for the 50MW Stage 1 Solar project. The contractor UGL has about 90 personnel on site, and believes it is on track for completion in November 2017. The 300ha site has been cleared, with the old tailings dumps having proved ideal for consistent ground conditions. While only 12% of the 540,000 PV panels have been installed to date, all material is on site and the streamlined construction process is impressive. We maintain a Buy recommendation on Genex.

Pumped Hydro and Stage 2 Solar take promising steps forward

The Pumped Hydro and Stage 2 Solar (250+270MW) is technically ready to go, with management's focus on PPA and funding. Through extensive discussions with power buyers in the market, Genex believes a PPA package with a single buyer is advantageous to splitting the various revenue streams. Funding discussions are progressing with banks, infrastructure investors and potential equity partners. The project has also reached the due diligence stage with the Northern Australia Infrastructure Fund (NAIF), one of only four projects to do so. Another positive sign for the project is the Queensland Government's commitment to fund a \$150m higher capacity transmission line to connect with the main grid. We also note that Kidston is one of only two State projects granted "critical infrastructure" status, along with the proposed Adani Carmichael coal mine. Unlike the mine, Kidston has support from all stakeholders.

Key milestones ahead

Genex is very happy with progress of the Stage 1 Solar project at Kidston. Management focus is shifting to Financial Close on the Pumped Hydro and expanded Solar project.

- PPA agreement will be critical for all of the funding arrangements.
- An equity partnership is likely to be with the same party as the PPA, but not necessarily so.
- An infrastructure fund may also buy into the project.
- Debt funding from a banking syndicate, probably including CEFC on similar terms.
- Debt funding from NAIF, which will be sub-ordinated to bank funding, and on generous terms.
- Grants from ARENA.

Valuation reduced to \$0.57 due to minor capex changes

Our risked valuation has decreased 7% as we have increased the capex for the Pumped Hydro project in line with guidance. The new price target of \$0.57 still represents more than 100% upside, and if the project is genuinely de-risked, we see value of \$1.00/share.

Financial Summary

Genex Power

PROFIT AND LOSS						
Year ending June	Unit	2016A	2017E	2018E	2019E	2020E
Revenue	\$m	0.7	-	6.7	14.2	102.8
Operating Expenses	\$m	-	-	(1.6)	(1.6)	(37.3)
Admin and Other Expenses	\$m	(7.7)	(5.1)	(4.1)	(4.2)	(4.3)
EBITDA	\$m	(7.0)	(5.1)	1.0	8.3	61.2
Depreciation	\$m	-	-	(10.0)	(10.0)	(35.0)
EBIT	\$m	(7.0)	(5.1)	(9.0)	(1.7)	26.2
Net interest (expense)	\$m	(0.1)	0.2	-	(5.0)	(5.0)
PBT	\$m	(7.1)	(4.9)	(9.0)	(6.7)	21.2
Tax expense	\$m	-	-	2.3	1.7	(5.3)
NPAT (pre-abnormal)	\$m	(7.1)	(4.9)	(6.8)	(5.0)	15.9
Abnormal items	\$m	-	-	-	-	-
NPAT (reported)	\$m	(7.1)	(4.9)	(6.8)	(5.0)	15.9

CASH FLOW						
Year ending June	Unit	2016A	2017E	2018E	2019E	2020E
OPERATING CASHFLOW						
NPAT	\$m	(7.1)	(4.9)	(6.8)	(5.0)	15.9
Add: non-cash items	\$m	4.7	2.0	11.0	11.0	36.0
Change in working capital	\$m	(7.3)	2.7	(1.0)	(1.1)	(13.3)
Operating cash flow	\$m	(9.7)	(0.2)	3.2	4.9	38.6
INVESTING CASHFLOW						
Net PP&E	\$m	(0.4)	-	(160.0)	(120.0)	(90.0)
Evaluation	\$m	(0.2)	(4.0)	(2.0)	(2.0)	(2.0)
Other	\$m	(3.8)	-	-	-	-
Investing cash flow	\$m	(4.4)	(4.0)	(162.0)	(122.0)	(92.0)
FINANCING CASHFLOW						
Share capital	\$m	3.3	18.5	-	-	-
Interest bearing debt	\$m	4.3	-	137.1	117.9	62.3
Financing cash flow	\$m	7.7	18.5	137.1	117.9	62.3
Change in cash	\$m	(6.5)	14.3	(21.6)	0.7	8.9

BALANCE SHEET						
Year ending June	Unit	2016A	2017E	2018E	2019E	2020E
ASSETS						
Cash	\$m	8.0	22.3	0.7	1.4	10.3
Accounts receivable	\$m	3.1	-	1.7	3.5	25.7
Property Plant & Equipment	\$m	0.6	0.6	150.6	260.6	315.6
Inventory	\$m	-	2.0	3.0	4.0	5.0
Other	\$m	3.8	3.8	3.8	3.8	3.8
Total assets	\$m	15.5	28.7	159.8	273.4	360.4
LIABILITIES						
Accounts payable	\$m	0.4	-	0.7	1.4	10.3
Deferred tax liabilities	\$m	-	-	-	-	-
Borrowings	\$m	3.4	3.4	140.5	258.4	320.6
Provisions	\$m	4.2	4.2	4.2	4.2	4.2
Total liabilities	\$m	8.0	7.6	145.4	264.0	335.1
SHAREHOLDER'S EQUITY						
Share capital	\$m	15.8	34.3	34.3	34.3	34.3
Retained earnings	\$m	(10.5)	(15.4)	(22.1)	(27.2)	(11.2)
Reserves & outside equity	\$m	2.2	2.2	2.2	2.2	2.2
Total equity	\$m	7.5	21.1	14.4	9.4	25.3
Weighted average NoSh	m	169.3	228.8	277.4	277.4	277.4

FINANCIAL RATIOS						
Year ending June	Unit	2016A	2017E	2018E	2019E	2020E
VALUATION						
NPAT (adjusted)	\$m	(7.1)	(4.9)	(6.8)	(5.0)	15.9
EPS (adjusted)	c/sh	(4.2)	(2.1)	(2.4)	(1.8)	5.7
EPS growth	%		-49%	14%	-26%	-417%
PER	x	-5.9x	-11.7x	-10.3x	-13.8x	4.4x
DPS	c/sh	-	-	-	-	-
Yield	%					
EV/EBITDA	x	-9.3x	-10.0x	211.7x	39.2x	6.2x
PROFITABILITY RATIOS						
EBITDA margin	%			15%	59%	60%
EBIT margin	%			-134%	-12%	25%
Return on assets	%	-32%	-22%	-7%	-2%	5%
Return on equity	%	-50%	-34%	-38%	-42%	92%
LIQUIDITY & LEVERAGE						
(Net debt) / cash	\$m	5	19	(140)	(257)	(310)
ND / E	%	45%	16%	977%	2758%	1268%
ND / (ND + E)	%	31%	14%	91%	97%	93%

ASSUMPTIONS						
Year ending June	Unit	2016A	2017E	2018E	2019E	2020E
PRICES						
PPA for Solar Stage 1	\$/MW		88.0	88.0	88.0	88.0
Off Peak Power Cost	\$/MW	10.0	15.0	30.0	30.8	31.5
Peak Power Price	\$/MW	150.0	130.0	133.3	136.6	140.0
LGC's (only on Solar)	\$/MW	75.0	75.0	75.0	80.0	75.0
CURRENCY						
USD/AUD		0.75	0.74	0.73	0.72	0.72

POWER GENERATION F'CAST						
	Unit	2016A	2017E	2018E	2019E	2020E
Solar Stage 1 (50MW)	MWh	-	-	72,270	144,540	144,251
Solar Stage 2 (250MW)	MWh	-	-	-	-	-
Pumped Hydro (250MW)	MWh	-	-	-	-	638,750
Total	MWh			72,270	144,540	783,001

SOTP VALUATION AT WACC						
8.1%	Risky			Unrisky		
	Net MWNPV (\$m)	\$/sh	Risky	NPV(\$m)	\$/sh	
Solar Stage 1 (50MW)	50	41	0.15	100%	41	0.15
Solar Stage 2 (270MW)	270	44	0.16	50%	89	0.32
Pumped Hydro (250MW)	250	75	0.27	50%	150	0.54
Net asset value	570	160	0.58		280	1.01
(Net debt) / cash		(3)			(3)	(0.01)
Equity value		157			277	
No Sh diluted for placement + SPP		277			277	
Value per share (\$/sh)		0.57			1.00	

Kidston Stage 1 Solar Project

Figure 1. Aerial view of Stage 1 Solar



Source: Canaccord Genuity

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The electrical substation has completed most of its work, being readied to take the power to the coastal grid through existing transmission line.

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The 50MW Solar Project is under construction since the beginning of the year. Genex has awarded the contract to construct, commission and maintain the project to UGL Ltd, which is one of the most experienced solar farm contractors in Australia. Both UGL and Genex anticipate the project to be completed in late November - December 2017, on budget of \$115m (we assume \$120m).

Power generation will gradually ramp up during this period, with UGL receiving a higher proportion of the cash flows, the earlier the project is completed.

Key observations from the project:

- All land (over 300 hectares) has been cleared and prepared for the installation of the solar panels, and associated infrastructure (access roads, inverters, substations, power lines etc.)
- As the land used is from the old tailings dumps the previous mining activity, it is flat and very consistent for piling, making it ideal for the purpose.
- Installation is progressing well, with about 65,000 (12%) of the 540,000 panels installed so far. At a rate of 4 rows per day, with each row containing 900 panels, another 4-5 months indicates the timeline of November is achievable.
- The solar panels are mounted on racks that will track the sun, facing east in the morning and west in the evening. While this costs a little bit more, it increases the capacity factor from 27% to +33%, which is very high for solar farms, aided by the sunny location (>300 days of sunshine).
- Almost all hardware has been delivered to site, with one more delivery in September.
- UGL has about 90 workers on site at present, which could ramp up to about 100.
- The electrical substation has completed most of its work, being readied to take the power to the coastal grid through existing transmission line.
- Accommodation village for workers upgraded and fully functional.

Figure 2. Solar panels and racking awaiting installation



Source: Canaccord Genuity

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The Pumped Hydro project’s technical and engineering details are complete, with a current capex of \$370m, which is \$70m higher than we had assumed, and the reason for our slightly lower valuation.

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Figure 3. Solar panels close up, with tracking mechanism



Source: Canaccord Genuity

Stage 2 Solar expansion and Pumped Hydro

The Pumped Hydro (250MW) and Stage 2 Solar (270MW) plans are making good progress as well, with a number of encouraging steps towards a development decision in 2018.

The Pumped Hydro project’s technical and engineering details are complete, with a current capex of \$370m, which is \$70m higher than we had assumed, and the reason for our slightly lower valuation.

The company is considering an expansion to the upper water reservoir, to enable 9 hours of power generation, rather than the base case of 6 hours. The suggested capex estimates of only \$20-30m appear low for a 50% increase in output. Furthermore, as the pumped hydro will be selling into the peak demand periods of morning and evening, prices are unlikely to be as high for a 9 hour period as for 6 hours.

Nevertheless, a sensitivity scenario of spending \$50m on the additional 3 hours of generation capacity, at a 10% lower average price would increase the risked valuation by about \$0.20/share. This looks attractive, but will ultimately depend on what the market can take, the nature of the PPA and the equity partner.

The Stage 2 Solar project is very much linked to the decision to go ahead with the Pumped Hydro. Genex has secured another 1,800 hectares of land adjacent to the existing solar farm, providing ample space for such an expansion. Ground conditions will be more variable, but is generally flat and lightly vegetated. However, the next generation of solar panels are expected to be both better and cheaper, so the net cost installed is thought to be about \$2m/MW, a bit lower than Stage 1 at \$2.3m/MW.

Figure 4. Pumped Hydro site, showing old open pits from Kidston Gold mine



Source: Canaccord Genuity

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As supply to the grid becomes more dependent on intermittent sources such as wind and solar, the need for storage with quick response times will increase, and may in fact become a regulatory requirement.

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PPA is the next key step

Discussions with energy consumers/utilities regarding a PPA have led management to conclude that Genex will be better off selling all the power generation, back-up capacity, voltage stability, frequency regulation and other services as a package, rather than in separate parts.

As supply to the grid becomes more dependent on intermittent sources such as wind and solar, the need for storage with quick response times will increase, and may in fact become a regulatory requirement. Genex management believes, and we tend to agree, that the commercial and strategic value of the Kidston energy hub is only improving.

The timing of a PPA is hard to predict, and is the key step required before a funding package can be finalised. The company is hoping that the project will reach Financial Close in 2018, and we would therefore expect a PPA to be agreed this calendar year. Once the PPA is in place, the subsequent steps could occur in quick succession. The PPA is also likely to be with an incoming equity partner in the 30-50% range. The most natural partners would include companies like AGL and Origin Energy, but Queensland corporations like Stanwell, CS Energy, Ergon Energy and Energex are obvious candidates as well.

Funding partners are being lined up

Genex has discussed funding options with a range of providers, including Government agencies, banks and infrastructure investors. The company has already received two grants from ARENA, including a \$4m facility for the Pumped Hydro study, and \$8m for Stage 1 Solar. Further grants from ARENA can be anticipated when a go-ahead is taken.

We are also very encouraged by the recent announcement that the \$5B NAIF (established by the Commonwealth Government in 2016 for a 5 year period) is proceeding with due diligence on the project. The NAIF is yet to provide funding for any project, and only 4 projects have reached the due diligence stage, from the 124 projects being looked at, which we take as a good sign. NAIF funding is designed to assist projects for the public

good north of the tropic of Capricorn, and be sub-ordinated to commercial debt. The NAIF website indicates 30 year terms at lower than commercial interest rates (but not below long term bond rates), and more patient repayment schedules etc. Genex indicated that they would look for 35% funding from NAIF, equivalent to \$287m assuming overall capex of \$820m.

A commercial bank facility of \$350m is envisaged, with support evident from CEFC, which is already a lender to the Stage 1 Solar project, in conjunction with SocGen.

Interest from infrastructure investors is also evident, as a number of local and international funds look for investments such as these. With pumped hydro schemes lasting up to 100 years, this project has added attraction to long term investors.

Depending on the level of equity sold down by Genex, to an infrastructure investor plus an energy partner, and the considerable debt funding indicated above, we think the company will not need to raise significant equity funds, despite the large capex of \$820m for a company capitalised at around \$70m.

Possible funding scenario for the Pumped Hydro and Stage 2 Solar:

Capex	\$m
Banks + CEFC	350
NAIF	280
Infrastructure Fund	100
Equity Partner	50
ARENA	10
Equity GNX	30
Total	820

Summary

We maintain a positive investment view on Genex, with a Buy recommendation and a Price Target of \$0.57/share. First cash flow from the Stage 1 Solar project is less than 6 months away, and momentum for the Pumped Hydro and Stage 2 Solar is very promising.

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Sydney

Level 26, 9 Castlereagh Street,
Sydney, 2000
Ph: +61 2 9263 2700

Melbourne

Level 4, 60 Collins Street,
Melbourne, 3000
Ph: +61 3 8688 9100