

Genex Power

K2-H is the keystone to build value

ADD (previously SPECULATIVE BUY)

Current price:	A\$0.27
Target price:	A\$0.35 ▲
Previous target:	A\$0.29
Up/downside:	31.1%
Reuters:	GNX.AX
Bloomberg:	GNX AU
Market cap:	US\$57.97m
	A\$82.79m
Average daily turnover:	US\$0.05m
	A\$0.07m
Current shares o/s	303.9m
Free float:	69.3%

Key changes in this note

Removal of the 10% risk factors from the DCF.
Change to a blended valuation methodology.



Price performance	1M	3M	12M
Absolute (%)	20.5	6	-5.4
Relative (%)	19.7	4.6	-10.5

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

– Genex Power

- JPower, one of Japan's largest hydropower operators and developers, has agreed to acquire up to 20% of GNX at up to \$25m following financial close of K2-H.
- GNX appears to have the majority of its funding conditionally in place, waiting for the final investment decision (FID) on K2-H by Energy Australia.
- We are a lot more confident in the K2-H project proceeding and upgrade our rating to ADD from SPECULATIVE BUY and lift our target price to 35cps.
- Our forecast potential 12-month TSR is 31%.

Key equity investor in place for K2-H

JPower is one of Japan's largest generators and owns and operates 61 hydroelectric power plants with a total capacity of 8,572MW with a market share of 17% of Japan's hydropower. JPower also owns power stations in six other jurisdictions including Thailand, the United States and China. JPower has agreed to a share placement of between 15-20% of the expanded equity of GNX on the basis that K2-H goes ahead.

\$25m share placement not at a discount to the market

The price of the issued shares will be the greater of the volume weighted average price (VWAP) of the five-day period immediately prior to financial close, or the five-day period following it. We understand that the price may be capped as the agreement allows JPower to acquire a minimum of 15% of the expanded equity for \$25m. There are currently ~303m shares of GNX on issue which means JPower would acquire ~53m shares at the minimum 15% percentage which implies a maximum price of 47cps. The acquisition is dependent upon a shareholder vote at an extraordinary general meeting (EGM) in addition to financial close on both the NAIF funding and the off-take agreement with Energy Australia.

Looking at M&A multiples as well as at DCFs

We update our base case valuation methodology to look at relevant M&A multiples as well as our DCF. We are using the median \$/MW multiple of transactions listed in Figure 3 and Figure 4 to estimate a multiples-based fair value. We have also updated our DCF to remove the risk factors that we'd placed on K2-H and later projects. We use an equally weighted blend of the updated DCF and multiples-based value to derive our updated target price of 35cps.

The blocks are in place waiting for the keystone

GNX has conditional approval on the bulk of its required funding for K2-H. The outstanding issue to bring it all together appears to be Energy Australia's FID decision. Once the offtake agreement is binding then we expect funding to proceed smoothly. This project will not only deliver significant value in its own right but also paves the way for value to be realised by the second stage solar (K2-S) and wind (K3-W) projects. We note again that a lot is riding on this one project but GNX has taken another step in de-risking it. We upgrade our rating to ADD and forecast a potential 12-month TSR of 31%.

Financial Summary	Jun-17A	Jun-18A	Jun-19F	Jun-20F	Jun-21F
Revenue (A\$m)	0.00	8.27	12.52	20.29	25.80
Operating EBITDA (A\$m)	-7.12	-1.72	5.95	16.50	21.26
Net Profit (A\$m)	-8.61	-7.46	-3.48	3.14	3.99
Normalised EPS (A\$)	(0.037)	(0.025)	0.043	0.010	0.013
Normalised EPS Growth	(18.5%)	(33.3%)		(75.8%)	26.9%
FD Normalised P/E (x)	NA	NA	6.23	25.68	20.24
DPS (A\$)	-	-	-	-	-
Dividend Yield	0%	0%	0%	0%	0%
EV/EBITDA (x)	NA	NA	33.39	17.87	13.47
P/FCFE (x)	NA	NA	1.32	NA	57.84
Net Gearing	35%	596%	176%	297%	265%
P/BV (x)	4.06	5.27	2.01	1.90	1.79
ROE	(64.5%)	(43.3%)	43.3%	7.6%	9.1%
% Change In Normalised EPS Estimates			0.76%	1.28%	1.28%
Normalised EPS/consensus EPS (x)			10.64	-3.44	13.09

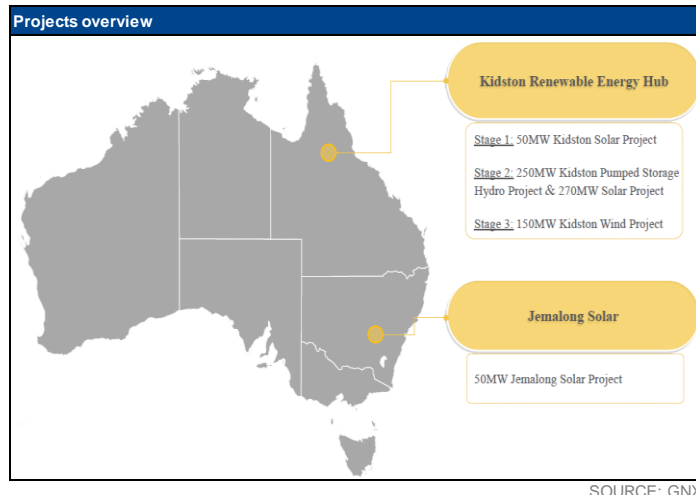
SOURCE: MORGANS, COMPANY REPORTS

Figure 1: Business snapshot

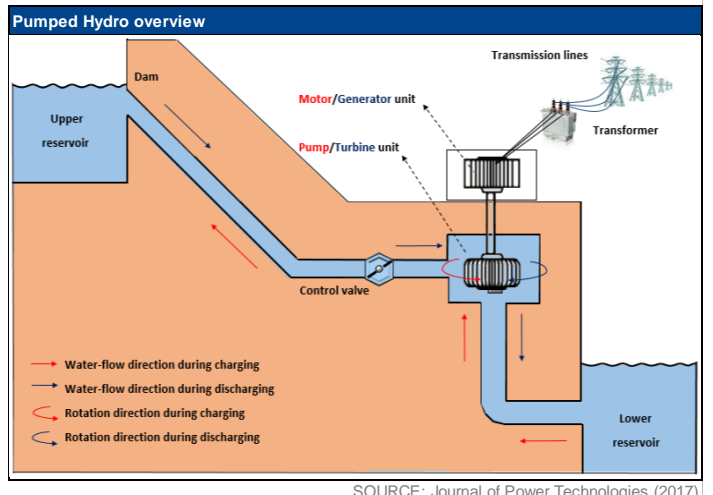
Genex Power (as at 06-06-19)		GNX AU / GNX.AX		Utilities	
Market cap (A\$m):	80.5	Rating:		ADD	
Shares outstanding (m):	303.9	Price (A\$):		0.265	
Free float (%):	69%	Target price (A\$):		0.347	
Company website:	https://www.genexpower.com.au/	Upside/downside to target price (%):		31.1%	

Company description

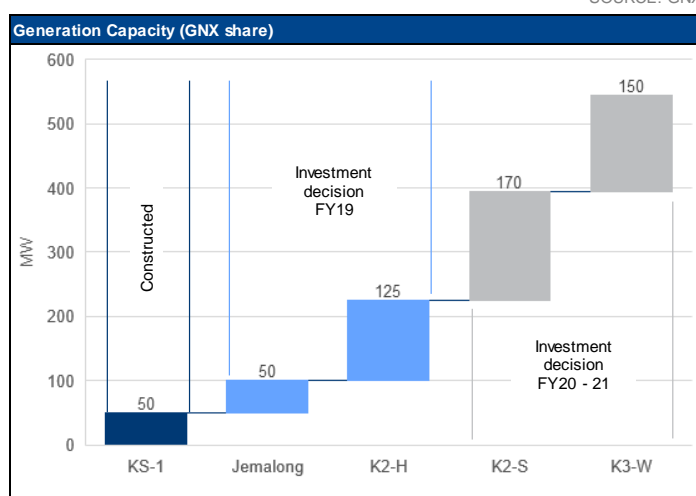
GNX is redeveloping an old gold mine in North Queensland into an energy storage project and has developed a 50MW solar farm adjacent to the mine. GNX also has plans to expand its energy generation with a second stage solar farm up to 270MW and a potential 150MW wind farm, on or near the same site, and 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 conditional approval for up to \$516m 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



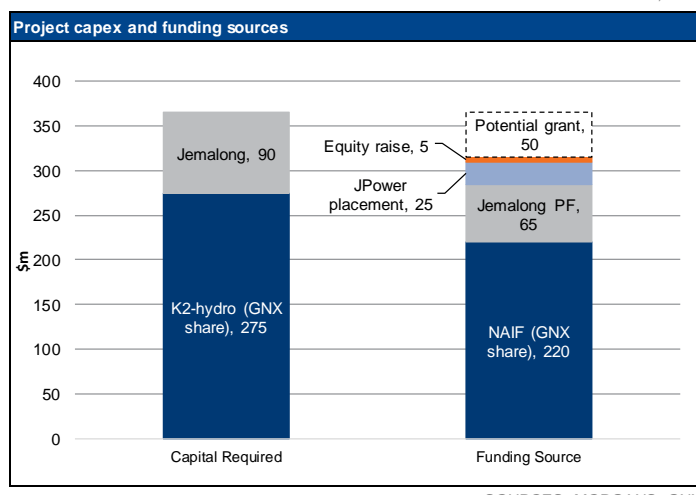
SOURCE: Journal of Power Technologies (2017)



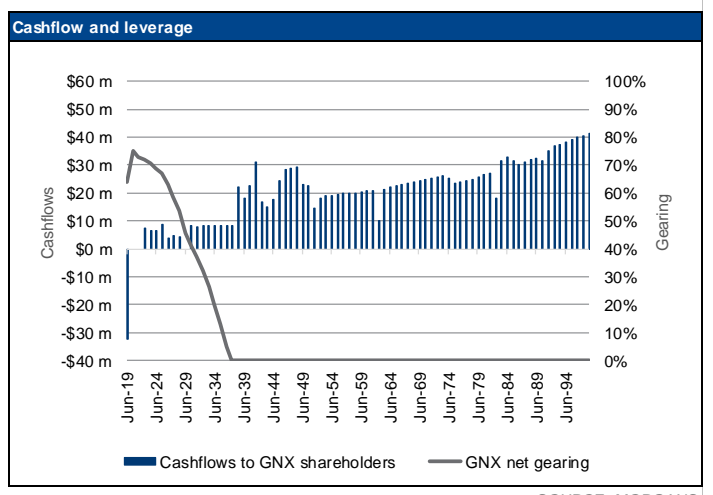
SOURCES: MORGANS, GNX

- 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. NAIF, 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	FY19E	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E	FY26E	FY27E	FY28E
EV/EBITDA (x)	N/A	32.2	17.3	13.1	13.0	12.7	13.2	11.6	12.0	10.2	10.5
Price-to-earnings (x)	N/A	N/A	N/A	N/A	4	2.6	2.8	2.3	2.5	2.1	2.2
Dividend yield (%)	-	-	-	-	7.1	6.3	6.2	8.3	3.7	4.3	3.8
Net Debt / ND+E (%)	85.6	63.7	74.8	72.6	72.0	70.3	68.6	66.9	63.0	58.3	53.4
Profit and loss (\$m)	FY18A	FY19E	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E	FY26E	FY27E	FY28E
Revenue	8.3	12.5	20.3	25.8	25.5	25.5	24.3	26.4	24.7	27.0	25.4
Other inc (K2H cost recovery)	1.7	2.7	5.4	5.5	5.7	5.8	5.9	6.1	6.2	6.3	6.4
Expenses	(11.7)	(9.2)	(9.2)	(10.1)	(10.3)	(10.5)	(10.8)	(11.0)	(11.2)	(11.5)	(11.7)
EBITDA	(1.7)	6.0	16.5	21.3	20.8	20.8	19.4	21.5	19.7	21.8	20.1
D&A	(3.0)	(6.0)	(6.8)	(8.0)	(8.0)	(8.0)	(8.0)	(8.0)	(8.0)	(8.0)	(8.0)
Operating EBIT	(4.7)	(0.1)	9.7	13.3	12.9	12.8	11.5	13.5	11.7	13.9	12.2
Net Interest Expense	(2.7)	(4.2)	(4.0)	(5.0)	(4.7)	(4.5)	(4.2)	(4.0)	(3.7)	(3.3)	(2.9)
K2H equity accounted profit	-	20.0	(1.2)	(2.6)	1.5	4.9	5.3	5.6	6.0	6.3	6.7
Profit Before Tax	(7.5)	15.7	4.5	5.7	9.7	13.3	12.6	15.2	14.0	16.9	16.0
Tax	-	(5.2)	(1.3)	(1.7)	(2.9)	(4.0)	(3.8)	(4.6)	(4.2)	(5.1)	(4.8)
Statutory Net Profit	(7.5)	10.5	3.1	4.0	6.8	9.3	8.8	10.6	9.8	11.8	11.2
Exceptional items (post tax)	-	(14.0)	-	-	-	-	-	-	-	-	-
Underlying Net Profit	(7.5)	(3.5)	3.1	4.0	6.8	9.3	8.8	10.6	9.8	11.8	11.2
Cashflows (\$m)	FY18A	FY19E	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E	FY26E	FY27E	FY28E
EBITDA	(1.7)	6.0	16.5	21.3	20.8	20.8	19.4	21.5	19.7	21.8	20.1
K2H SPV distributions	-	-	-	-	-	-	2.0	3.1	3.3	3.4	3.5
Working capital	(9.7)	5.5	(0.7)	(6.0)	0.0	0.0	(0.4)	(0.1)	0.2	(0.2)	0.1
Gross operating cashflow	(11.4)	11.5	15.8	15.2	20.9	20.8	21.0	24.4	23.1	25.1	23.8
Net interest paid	(2.7)	(4.2)	(4.0)	(5.0)	(4.7)	(4.5)	(4.2)	(4.0)	(3.7)	(3.3)	(2.9)
Cash paid for Tax	-	-	(0.6)	(1.7)	(1.8)	(2.5)	(2.8)	(3.8)	(3.4)	(4.2)	(3.8)
Operating cashflow	(14.1)	7.3	11.3	8.5	14.4	13.8	14.0	16.7	16.0	17.6	17.1
Capex (GNX not K2H SPV)	(74.0)	(49.3)	(90.0)	-	-	-	-	-	-	-	-
Investing cashflow	(74.0)	(49.3)	(90.0)	-	-	-	-	-	-	-	-
Equity issuance/(returns)	-	32.1	-	-	-	-	-	-	-	-	-
Debt drawdown/(repaid)	-	116.4	(6.2)	(6.5)	(6.8)	(7.1)	(7.5)	(7.8)	(8.2)	(8.5)	(8.9)
Dividends paid	-	-	-	-	(7.6)	(6.7)	(6.6)	(8.9)	(3.9)	(4.5)	(4.1)
Financing cashflow	-	148.5	(6.2)	(6.5)	(14.4)	(13.8)	(14.0)	(16.7)	(12.1)	(13.1)	(13.0)
Net cashflow	(88.2)	106.4	(84.9)	2.0	-	-	-	-	3.9	4.5	4.1
Balance sheet (\$m)	FY18A	FY19E	FY20E	FY21E	FY22E	FY23E	FY24E	FY25E	FY26E	FY27E	FY28E
Cash	11	118	33	35	35	35	35	35	39	43	47
Receivables	1	1	1	1	1	1	3	3	3	3	3
Fixed Assets	118	114	197	189	181	173	165	157	149	141	133
SPV equity	-	65	64	61	63	68	71	74	76	79	82
Tax assets	-	1	-	-	-	-	-	-	-	-	-
Other	6	8	8	8	8	8	8	8	8	8	8
Total Assets	136	306	303	294	288	285	282	276	275	275	274
Debt	102	218	212	206	199	192	184	176	168	160	151
Deferred Tax from SPV)	-	6	6	6	7	9	10	10	11	12	13
Other liabilities	18	24	24	18	18	18	19	19	19	19	19
Total Liabilities	120	249	243	230	224	219	213	206	199	191	183
Net Assets	15	57	61	65	64	66	69	70	76	83	91
Ave shares on issue (m)	299	369	435	435	435	435	435	435	435	435	435

SOURCE: MORGANS RESEARCH, COMPANY

Comparable transactions

Figure 3 below shows a list of comparable energy transactions which we use for the base and bull case valuations. We also note that we do not use the median multiple to value K2-S and K3-W in the base case. We have assumed a multiple of \$0.3/W in the base case for those projects as we're assuming that they're only partially developed by FY22.

We are using the same transactions as in our previous note but now also extract the median \$/MW multiple for the base case as well as the top quartile multiple for the bull case.

Figure 3: Comparable renewable energy transactions

Transaction	Country	Date	Fuel	Consideration (m)	EV / MW
Manildra	Australia	Jun-18	Solar	A\$ 113	2.4
Bald Hills	Australia	Feb-17	Wind	N/A	3.0
Cullerin range wind farm	Australia	Jun-16	Wind	A\$ 72	2.4
Pacific Hydro	Australia	Dec-15	Hydro / Wind	A\$ 3,000	3.3
CHORUS Clean Energy	Europe	May-16	Solar / Wind	€ 296	3.2
Enel Green Power	Europe	Nov-15	Solar / Wind / Hydro	€ 9,620	1.8
Finerge-Gestao	Europe	Sep-15	Wind	N/A	1.5
				Top quartile	3.1
				Median	2.4

SOURCES: MORGANS, DUET AND TILT INDEPENDENT EXPERT REPORTS, COMPANY REPORTS

Figure 4: Comparable fast start energy transactions

Transaction	Country	Date	Fuel	Consideration (m)	EV / MW
Smithfield	Australia	May-19	Gas	A\$ 74	0.6
Landfill gas and power	Australia	Apr-16	Landfill gas	N/A	2.1
Energy Developments	Australia	Jul-15	Gas	A\$ 1,369	2.1
Colongra Power Station	Australia	Dec-14	Gas	A\$ 234	0.4
Clarke Energy	Australia	Jun-14	LNG	A\$ 23	0.8
Envirogen	Australia	Apr-14	Gas	A\$ 25	0.6
Clarke Energy	Australia	Feb-14	LNG	A\$ 21	1.0
Infinis plc	UK	Oct-16	Landfill gas	£185	2.6
Infinis Energy	UK	Oct-15	Landfill gas	£555	4.1
				Top quartile	2.1
				Median	2.1

SOURCES: MORGANS, DUET AND TILT INDEPENDENT EXPERT REPORTS, COMPANY REPORTS

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 5 summarises our sum-of-the-parts FCFE DCF which assumes a cost of equity of 8%.

Figure 5: Base case DCF valuation

Component	Value (\$m)	Value (cps)
KS1 & Jemalong	34.6	11
GNX share of K2-H	48.1	16
K2-S & K3-W	12.9	4
Total	95.7	31

SOURCE: MORGANS

Figure 6 summarises our multiples based valuation. Our key assumptions are:

- Jemalong and K2-H are completed by FY22.
- K2-S and K3-W have been progressed but not completed and are valued on a lower multiple compared to Jemalong and KS1.
- The FY22 equity value (\$199.5m) is discounted at 8% p.a. to a FY19 basis.
- A total of \$30m equity is raised to complete K2-H.

Figure 6: Base case multiples based valuation

Asset	MW	Multiple (\$ / W)	EV (\$m)	Debt (\$m)	Equity (\$m)
Jemalong + KS1	100	2.4	242.0	(165.0)	77.0
K2-H	125	2.1	262.5	(220.0)	42.5
K2-S + K3-W	320	0.3	80.0	-	80.0
Total	545	1.1	584.5	(385.0)	199.5
Estimated future number of shares					416.6
Discounted equity value (cps)					38

SOURCE: MORGANS

Our combined base case valuation on a 50/50 weighting is therefore ~35cps.

Bull case valuation

Our key assumptions are:

- All projects are completed by FY22.
- The FY22 equity value (\$739.5m) is discounted at 8% p.a. to a FY19 basis.
- Multiples are based on the top quartile of comparable transactions.

Figure 7: Bull case summary

Asset	MW	Multiple (\$ / W)	EV (\$m)	Debt (\$m)	Equity (\$m)
Jemalong + KS1	100	3.1	310.0	(165.0)	145.0
K2-H	125	2.1	262.5	(220.0)	42.5
K2-S + K3-W	320	3.1	992.0	(440.0)	552.0
Total	545	2.9	1,564.5	(825.0)	739.5
Estimated future number of shares (m)					946.9
Discounted equity value (cps)					62

SOURCE: MORGANS

Bear case valuation

Our key assumptions are:

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

Figure 8: GNX valuation bear case

Component	Value (\$m)	Value (cps)
KS1 & Jemalong	34.6	11

SOURCE: MORGANS

Queensland

Brisbane	+61 7 3334 4888
Stockbroking, Corporate Advice, Wealth Management	
Brisbane: Edward St	+61 7 3121 5677
Brisbane: Tynan	+61 7 3152 0600
Partners	
Brisbane: North Quay	+61 7 3245 5466
Bundaberg	+61 7 4153 1050
Cairns	+61 7 4222 0555
Caloundra	+61 7 5491 5422
Gladstone	+61 7 4972 8000
Gold Coast	+61 7 5581 5777
Holland Park	+61 7 3151 8300
Ipswich/Springfield	+61 7 3202 3995
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
Spring Hill	+61 7 3833 9333
Sunshine Coast	+61 7 5479 2757
Toowoomba	+61 7 4639 1277
Townsville	+61 7 4725 5787

New South Wales

Sydney	+61 2 9043 7900
Stockbroking, Corporate Advice, Wealth Management	
Sydney: Grosvenor	+61 2 8215 5000
Place	
Sydney: Reynolds	+61 2 9373 4452
Securities	
Sydney: Currency	+61 2 8216 5111
House	
Armidale	+61 2 6770 3300
Ballina	+61 2 6686 4144
Balmain	+61 2 8755 3333
Bowral	+61 2 4851 5555
Chatswood	+61 2 8116 1700
Coffs Harbour	+61 2 6651 5700
Gosford	+61 2 4325 0884
Hurstville	+61 2 8215 5079
Merimbula	+61 2 6495 2869
Mona Vale	+61 2 9998 4200
Neutral Bay	+61 2 8969 7500
Newcastle	+61 2 4926 4044
Orange	+61 2 6361 9166
Port Macquarie	+61 2 6583 1735
Scone	+61 2 6544 3144
Wollongong	+61 2 4227 3022

Victoria

Melbourne	+61 3 9947 4111
Stockbroking, Corporate Advice, Wealth Management	
Brighton	+61 3 9519 3555
Camberwell	+61 3 9813 2945
Domain	+61 3 9066 3200
Geelong	+61 3 5222 5128
Richmond	+61 3 9916 4000
South Yarra	+61 3 8762 1400
Southbank	+61 3 9037 9444
Traralgon	+61 3 5176 6055
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South Australia

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Norwood	+61 8 8461 2800
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