

### Key Facts

Company Code	FLC
Closing Price	\$0.44
Date of Report	16/10/18
Company Website	<a href="http://fluencecorp.com">fluencecorp.com</a>
Analyst	Johan Hedstrom

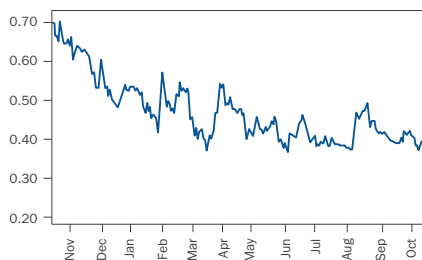
### Company Statistics

12-Month Range (A\$)	\$0.375-\$0.69
Market Cap (A\$Mil)	\$191m
Issued Shares (Mil)	436m
Issued Options (Mil)	49m
Cash (A\$Mil)	\$57.1m

### Major Shareholders

RSL Investments	30.9%
Pond Ventures Nominees	7.7%

### Share Price Performance



## FLC announces Aspiral sales agreement of +US\$45m in China

Fluence has announced its first significant sales agreement in China to ITEST, the entity responsible for the engineering consultancy and supervision of highways in central China. ITEST took delivery of a 200m<sup>3</sup>/day demonstration plant in August this year, and has very quickly followed up with a minimum order of 80 plants, with capacity between 200-600m<sup>3</sup>/day. ITEST has also been granted exclusive rights to Aspiral plants for highways in central China, as long as a minimum volume of 66,000m<sup>3</sup>/day is reached within the next three years. The first 80 plants should cover about half of the volume target to maintain exclusivity, within the next 18 months. We expect revenue to be recognised over the next three years, which should provide a boost to revenue visibility over the short term – a concept the market has grappled with in regards to the FLC story. We do note that the Aspiral units are traditionally one of FLC’s highest margin products – so we expect that should this sales agreement be executed – that it generously hits the bottom line and helps propel the company into cash flow positive through 2H19.

## Product and geography diversification through recent USA wins

Fluence has also announced the first sale of MABR units to Orenco in the USA, for integration into its packaged wastewater treatment plants. The initial units will be installed at an RV Park in Oregon, and we note the significant follow-up potential as Orenco currently services 250 seasonal facilities globally. Orenco stated that it had chosen Fluence’s MABR technology after evaluating multiple water treatment technologies due to MABR’s increased treatment capacity, higher effluent quality and lower operating costs.

## Looking to the September Quarterly for assurance on guidance and revenue recognition of the current backlog

The company will announce its September quarter results at the end of this month. We are expecting revenue of \$25m. We note that our estimates reflect CY18 revenue forecast of US\$86m, which is conservative relative to company estimates for US\$105- \$115m. That said, we do not expect any change to company guidance and expect this to be re-stated in the September Quarterly. We expect quarterly cash flow to be negative at around US\$14m. This will reduce cash to about US\$26m at the end of September. However, we estimate much lower cash burn in the December quarter, leading to US\$24m of cash by the end of the year. We anticipate cash flow to turn positive in the 2H of 2019. We do note that the company stated at the 1H18 result that a contract revenue backlog of US\$84m stands at 30 June 2018, and \$42.9m of that is anticipated to convert into revenue by CY18. We expect revenue recognition of some of this backlog by the September Quarterly, which will only stand to benefit the markets sentiment towards the company meeting CY18 guidance. The September quarterly will also provide further details on the desalination and other water treatment businesses.

## No change to our estimates, upside remains attractive

We are conservatively estimating revenues of US\$86m for 2018 and a gross profit of US\$18m, below the company’s guidance of US\$20-22m. Our risked Target Price is \$0.01 lower at A\$0.96/share, compared to an unrisked value of A\$1.28 due to issued capital being slightly higher and a lower AUD/USD exchange rate.

## Strategy is showing good signs of working

Fluence has consistently said that the China ramp-up will take time, so it is positive to see the first material sales agreement from one of its partners. It is also worth noting that the sharp progression from ITEST’s demonstration plant order to a full scale significant sales order speaks volumes to the company’s technology and execution skills alike. Although ITEST was not the company’s target market of municipal water treatments in China (rather, operating in water treatment at rest locations along highways), it demonstrates the flexibility and large scope of the technology, alongside the company’s growing efficacy in executing in China – a point which the market has been eagerly awaiting.

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# Fluence Corporation Financial Summary

PROFIT AND LOSS US\$						
Year ending December	Unit	2016A	2017A	2018E	2019E	2020E
Revenue	\$m	60.9	33.2	85.6	126.6	233.8
Operating Expenses	\$m	(49.3)	(27.2)	(67.1)	(96.5)	(171.2)
Admin and Other Expenses	\$m	(28.7)	(31.4)	(32.2)	(33.0)	(33.8)
<b>EBITDA</b>	<b>\$m</b>	<b>(17.1)</b>	<b>(23.9)</b>	<b>(13.7)</b>	<b>(2.8)</b>	<b>28.7</b>
Depreciation	\$m	(1.6)	(0.7)	(3.3)	(4.1)	(5.8)
EBIT	\$m	(18.8)	(24.6)	(17.0)	(6.9)	22.9
Net interest (expense)	\$m	6.5	0.1	1.6	0.5	0.2
<b>PBT</b>	<b>\$m</b>	<b>(12.3)</b>	<b>(24.4)</b>	<b>(15.4)</b>	<b>(6.5)</b>	<b>23.2</b>
Tax expense	\$m	(2.8)	0.1	3.8	1.6	(5.8)
<b>NPAT (pre-abnormal)</b>	<b>\$m</b>	<b>(14.9)</b>	<b>(24.3)</b>	<b>(11.5)</b>	<b>(4.8)</b>	<b>17.4</b>
Abnormal items	\$m	-	-	-	-	-
<b>NPAT (reported)</b>	<b>\$m</b>	<b>(14.9)</b>	<b>(24.3)</b>	<b>(11.5)</b>	<b>(4.8)</b>	<b>17.4</b>

CASH FLOW US\$						
Year ending December	Unit	2016A	2017A	2018E	2019E	2020E
<b>OPERATING CASHFLOW</b>						
NPAT	\$m	(14.9)	(24.3)	(11.5)	(4.8)	17.4
Add: non-cash items	\$m	1.6	0.7	3.3	4.1	5.8
Change in working capital	\$m	(7.3)	(6.4)	(45.2)	(6.2)	(16.1)
<b>Operating cash flow</b>	<b>\$m</b>	<b>(20.6)</b>	<b>(30.1)</b>	<b>(53.4)</b>	<b>(6.9)</b>	<b>7.1</b>
<b>INVESTING CASHFLOW</b>						
Net PP&E	\$m	(0.4)	(3.7)	(2.4)	(4.9)	(3.9)
Evaluation	\$m	(0.2)	-	-	-	-
Other/merger	\$m	(3.8)	55.0	-	-	-
<b>Investing cash flow</b>	<b>\$m</b>	<b>(4.4)</b>	<b>51.3</b>	<b>(2.4)</b>	<b>(4.9)</b>	<b>(3.9)</b>
<b>FINANCING CASHFLOW</b>						
Share capital	\$m	3.3	31.3	-	-	-
Interest bearing debt	\$m	4.3	(0.6)	-	0.3	7.5
<b>Financing cash flow</b>	<b>\$m</b>	<b>7.7</b>	<b>30.7</b>	<b>-</b>	<b>0.3</b>	<b>7.5</b>
Change in cash	\$m	(17.3)	51.9	(55.8)	(11.5)	10.7

BALANCE SHEET US\$						
Year ending December	Unit	2016A	2017A	2018E	2019E	2020E
<b>ASSETS</b>						
Cash	\$m	8.0	79.9	24.1	12.7	23.4
Accounts receivable	\$m	3.1	26.7	21.4	31.7	58.4
Property Plant & Equipment	\$m	0.6	7.1	6.2	7.0	5.1
Inventory	\$m	-	18.5	18.5	18.5	18.5
Other	\$m	3.8	72.4	72.4	72.4	72.4
<b>Total assets</b>	<b>\$m</b>	<b>15.5</b>	<b>204.7</b>	<b>142.7</b>	<b>142.2</b>	<b>177.9</b>
<b>LIABILITIES</b>						
Accounts payable	\$m	0.4	59.0	8.6	12.7	23.4
Deferred tax liabilities	\$m	-	1.7	1.7	1.7	1.7
Borrowings	\$m	3.4	2.1	2.1	2.4	10.0
Provisions	\$m	4.2	38.2	38.2	38.2	38.2
<b>Total liabilities</b>	<b>\$m</b>	<b>8.0</b>	<b>101.1</b>	<b>50.6</b>	<b>55.0</b>	<b>73.3</b>
<b>SHAREHOLDER'S EQUITY</b>						
Share capital	\$m	15.8	156.9	156.9	156.9	156.9
Retained earnings	\$m	(10.5)	(51.9)	(63.5)	(68.3)	(50.9)
Reserves & outside equity	\$m	2.2	(1.4)	(1.4)	(1.4)	(1.4)
<b>Total equity</b>	<b>\$m</b>	<b>7.5</b>	<b>103.6</b>	<b>92.1</b>	<b>87.2</b>	<b>104.6</b>
Weighted average NoSh	m	228.6	336.1	425.5	435.9	435.9

FINANCIAL RATIOS						
Year ending December	Unit	2016A	2017A	2018E	2019E	2020E
<b>VALUATION</b>						
NPAT (adjusted)	\$m	(14.9)	(24.3)	(11.5)	(4.8)	17.4
EPS (adjusted)	c/sh	(6.5)	(7.2)	(2.7)	(1.1)	4.0
EPS growth	%		11%	-63%	-59%	-458%
PER	x	-6.8x	-6.1x	-16.2x	-39.5x	11.0x
DPS	c/sh	-	-	-	-	-
Yield	%					
EV/EBITDA	x	-10.9x	-4.8x	-12.4x	-64.0x	6.2x
<b>PROFITABILITY RATIOS</b>						
Gross margin	%			28%	31%	37%
EBITDA margin	%			-16%	-2%	12%
Return on assets	%	-13%	-22%	-7%	-3%	11%
Return on equity	%	-27%	-44%	-12%	-5%	18%
<b>LIQUIDITY &amp; LEVERAGE</b>						
(Net debt) / cash	\$m	5	78	22	10	13
ND / E	%	45%	2%	2%	3%	10%
ND / (ND + E)	%	31%	2%	2%	3%	9%

ASSUMPTIONS						
Year ending December	Unit	2016A	2017A	2018E	2019E	2020E
<b>Volumes</b>						
MABR modules	#	100	100	200	2,000	8,000
Nirobox units	#	10	3	40	75	150
Custom Revenue growth	%	8%	-44%	100%	5%	5%
RaaS agreements	#	-	-	4	5	10

MARGINS						
		2016A	2017A	2018E	2019E	2020E
MABR	%	35%	35%	35%	35%	35%
Nirobox	%	20%	20%	20%	20%	20%
Custom Projects	%	19%	20%	20%	20%	20%
RaaS	%	-	-	50%	50%	50%

CURRENCY						
USD/AUD		0.75	0.78	0.76	0.75	0.74

A\$ SOTP VALUATION AT WACC						
11.9%	Risked			Unrisked		
	NPV (A\$m)	A\$/sh	Risking	NPV (\$m)	A\$/sh	
MABR	269	0.62	75%	358	0.82	
Nirobox	112	0.26	75%	150	0.34	
Custom Projects	98	0.22	100%	98	0.22	
RaaS	42	0.10	75%	56	0.13	
<b>Net asset value</b>	<b>521</b>	<b>1.19</b>		<b>661</b>	<b>1.52</b>	
Corporate overheads	(134)	(0.31)		(134)	(0.31)	
(Net debt) / cash	31			31	0.07	
<b>Equity value</b>	<b>418</b>			<b>559</b>		
# Shares	436			436		
<b>Value per share (\$/sh)</b>	<b>0.96</b>			<b>1.28</b>		

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