EDISON

Fluence Corporation

Contract win

“Landmark” €165m contract win

General industrials

The award of a €165m (US$188m) contract to provide water treatment to Abidjan, the largest city in Ivory Coast, is transformative in our view. This turnkey project will supply 150,000m³/day of water to 4.7 million people and include a range of treatment solutions. The win establishes Fluence as a supplier of large, innovative solutions and leads us to double our FY20 adjusted EPS forecast to US$c3.8. Despite organic revenue growth in FY19 and FY20 of well over 50%, the share price implies an FY20 P/E of 7x.

Year end	Revenue (US$m)	EBITDA* (US$m)	EPS* (c)	EV/revenue (x)	EV/EBITDA (x)	P/E (x)
12/17	33.2	(23.6)	(7.0)	3.7	N/A	N/A
12/18	101.1	(8.5)	(2.5)	1.2	N/A	N/A
12/19e	169.1	1.5	(0.2)	0.7	82.0	N/A
12/20e	266.5	23.0	3.8	0.5	5.3	6.8

Note: *EBITDA and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

“Landmark” contract win

This turnkey CES (custom engineered solution) aims to supply and treat water from Lagune Aghien and deliver it to the nearby city of Abidjan, Ivory Coast’s industrial capital and largest city. It includes the construction of intake, treatment and piping infrastructure as well as the implementation of a range of customised treatment solutions to address the specific pollution problems faced. Completion is still subject to the government agreeing export credit financing terms with the Israel Discount Bank but construction should begin in Q319 and be finished within two years thereafter. It represents (by a factor of three) the largest deal Fluence has signed thus far. Fluence also hopes to win the associated operation and maintenance contract, which would further bolster its recurring revenue base.

Impact on financials

This deal dramatically improves Fluence’s financial profile (see Exhibit 1). While it had indicated it was close to finalising a very large contract in Africa, without visibility on timing or size, we had not factored it into our forecast (see Time for better treatment?). Taking company guidance at face value lifts our FY19 sales forecast by US$20m and FY20 by US$80m (a 13% and 43% increase, respectively). It turns FY19 profitable on an EBITDA basis (to +US$1.5m) and nearly doubles our FY20 EBITDA forecast to US$23.0m. Our FY20 adjusted EPS also doubles to US$c3.8.

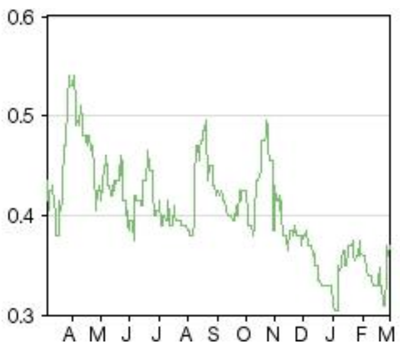
Valuation and context

Fluence’s strategic priority remains growing its higher-margin “smart” product (SPS) and recurring revenue base to build margins and visibility (see Delivering on a demanding target). Nevertheless, this win is transformative in our view. It demonstrates it is also a credible supplier of large, complex turnkey custom solutions. Factoring in the financial impact, Fluence will deliver well over 50% organic revenue growth in both FY19 and FY20. Despite this the shares are currently rated at just 7x adjusted FY20 EPS. A DCF approach that reflects the growth and margins we believe Fluence is ultimately capable of suggests an A$0.75 per share valuation, double the current share price.

4 March 2019

Price	**A$0.37**
Market cap	**A$199m**
	US$/A$0.71
Estimated net cash (US$m) at end 2019	19
Shares in issue	538m
Free float	60%
Code	FLC
Primary exchange	ASX
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	2.8	(3.9)	(19.6)
Rel (local)	(2.8)	(10.3)	(22.1)
52-week high/low		A$0.5	A$0.3

Business description

Fluence is a global supplier of water and wastewater treatment solutions. Its decentralised products provide municipal customers with ‘plug and play’ solutions that are quicker to deploy and substantially cheaper than traditional alternatives.

Next event

Q119 trading update	April 2019

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Edison profile page

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Revenue reclassification and changes to forecasts

Exhibit 1 highlights the significant boost this contract provides to our forecasts. The company also published its full FY18 financials on 27 February which included a $5m revenue reclassification as a result of the recent adoption of hyperinflation accounting in Argentina. Originally Fluence recognised revenue from its PDVSA contract ($27m in FY18) through its Argentinian subsidiary in US$, the currency the contract was priced and paid in. However, the recent publication of a inflation index by the Argentinian government enabled an accurate fx rate to be calculated for the first time and, as a result, the company was obliged to recognise all FY18 Argentinian revenue in local currency and reclassify some revenue as foreign exchange gains. This reclassification has no impact on cash collection, forecasts or valuation. All PDVSA cash (in US$) has already been collected and the expected revenue from this contract in FY19 is less than $2m.

Exhibit 1: Changes to numbers

	FY18			FY19e			FY20e		
	Old	New	%	Old	New	%	Old	New	%
Revenue (US$m)	105.6	101.1	(4.3)	149.1	169.1	13.4	186.5	266.5	42.9
Adjusted EBITDA (US$m)	(17.5)	(8.5)	N/M	(1.8)	1.5	N/M	11.8	23.0	94.9
Adjusted EPS (c)	(4.0)	(2.5)	N/M	(0.7)	(0.2)	N/M	1.8	3.8	113.2

Source: Edison Investment Research

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Exhibit 2: Financial summary

$m	2016	2017	2018	2019e	2020e
Year end 31 December	IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT					
Revenue	0.8	33.2	101.1	169.1	266.5
Cost of Sales	(2.0)	(27.2)	(66.5)	(128.8)	(201.7)
Gross Profit	(1.2)	6.0	34.6	40.3	64.8
EBITDA	(8.8)	(23.6)	(8.5)	1.5	23.0
Operating Profit (before amort. and except).	(9.1)	(24.3)	(20.1)	(1.1)	(11.0)
Amortisation of acquired intangibles	0.0	0.0	0.0	0.0	0.0
Exceptionals	0.1	(1.2)	(52.7)	0.0	0.0
Share-based payments	0.0	0.0	0.0	0.0	0.0
Reported operating profit	(9.1)	(25.4)	(63.7)	(1.1)	20.4
Net Interest	(0.0)	2.6	0.5	0.3	0.3
Joint ventures & associates (post tax)	0.0	0.0	0.0	0.0	0.0
Exceptionals	0.0	0.0	0.0	0.0	0.0
Profit Before Tax (norm)	(9.1)	(21.7)	(10.5)	(0.8)	20.7
Profit Before Tax (reported)	(9.1)	(22.9)	(63.2)	(0.8)	20.7
Reported tax	0.0	(0.7)	(0.4)	0.0	0.0
Profit After Tax (norm)	(9.1)	(22.4)	(10.9)	(0.8)	20.7
Profit After Tax (reported)	(9.1)	(23.6)	(63.6)	(0.8)	20.7
Minority interests	0	0	0	0	0
Discontinued operations	0	0	0	0	0
Net income (normalised)	(9.1)	(22.4)	(10.9)	(0.8)	20.7
Net income (reported)	(9.1)	(23.6)	(63.6)	(0.8)	20.7
Average Number of Shares Outstanding (m)	214	320	477	538	440
EPS - basic normalised ($)	(0.04)	(0.07)	(0.02)	(0.00)	0.04
EPS - diluted normalised ($)	(0.04)	(0.07)	(0.02)	(0.00)	0.04
EPS - basic reported ($)	(0.04)	(0.07)	(0.14)	(0.00)	0.04
Dividend per share ($)	0	0	0	0	0
Revenue growth (%)	N/A	N/A	204.7	67.2	57.6
Gross Margin (%)	(147.5)	18.0	34.2	23.8	24.3
EBITDA Margin (%)	(1,089.3)	(71.1)	(8.4)	0.9	8.6
Normalised Operating Margin	(1,126.1)	(73.1)	(10.9)	(0.7)	7.7
BALANCE SHEET					
Fixed Assets	3.2	72.7	43.8	45.2	46.6
Intangible Assets	2.1	60.2	5.6	5.6	5.6
Tangible Assets	1.0	7.1	14.8	16.2	17.6
Investments & other	0.1	5.5	23.4	23.4	23.4
Current Assets	24.4	131.9	97.7	176.2	190.4
Stocks	0.5	18.5	18.9	41.1	41.2
Debtors	0.7	26.7	33.5	90.8	111.2
Cash & cash equivalents	22.9	75.2	38.7	37.8	31.5
Other	0.3	11.5	6.5	6.5	6.5
Current Liabilities	(2.5)	(95.9)	(78.7)	(159.5)	(154.5)
Creditors	(1.4)	(27.8)	(47.5)	(88.1)	(82.4)
Tax and social security	0.0	(0.1)	(0.9)	(0.9)	(0.9)
Short term borrowings	0.0	(1.1)	(0.4)	(18.7)	(18.7)
Other	(1.1)	(66.9)	(30.0)	(51.8)	(52.5)
Long Term Liabilities	(1.0)	(5.1)	(11.7)	(11.7)	(11.7)
Long term borrowings	0.0	0.0	0.0	0.0	0.0
Other long term liabilities	(1.0)	(5.1)	(11.7)	(11.7)	(11.7)
Net Assets	24.1	103.6	51.1	50.2	70.9
Minority interests	0.0	0.2	1.2	1.2	1.2
Shareholders' equity	24.1	103.8	52.3	51.5	72.1
CASH FLOW					
Op Cash Flow before WC and tax	(8.8)	(23.6)	(8.5)	1.5	23.0
Working capital	1.7	(4.8)	(44.1)	(16.3)	(24.8)
Exceptional & other	0.0	0.2	0.1	0.0	0.0
Tax	0.0	(0.9)	(0.2)	(0.4)	(0.4)
Net operating cash flow	(7.2)	(29.0)	(52.6)	(15.2)	(2.2)
Capex	(0.4)	(3.7)	(2.8)	(4.0)	(4.0)
Acquisitions/disposals	(1.0)	50.6	(1.8)	0.0	0.0
Net interest	0.0	0.5	2.7	(0.1)	(0.1)
Equity financing	22.9	31.3	26.2	0.0	0.0
Dividends	0.0	0.0	0.0	0.0	0.0
Other	(0.2)	1.1	(2.4)	0.0	0.0
Net Cash Flow	14.2	50.8	(30.6)	(19.3)	(6.3)
Opening net debt/(cash)	(8.5)	(22.9)	(74.0)	(38.4)	(19.1)
FX	0.2	2.1	(4.3)	0.0	0.0
Other non-cash movements	0.0	(1.8)	(0.7)	0.0	0.0
Closing net debt/(cash)	(22.9)	(74.0)	(38.4)	(19.1)	(12.8)

Source: Fluence Corporation accounts, Edison Investment Research

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