

Intelligent Energy Holdings

Trading in line with expectations

Interim results

Alternative energy

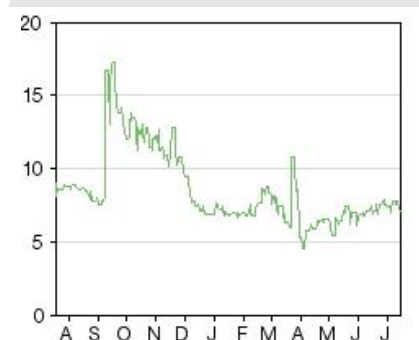
17 July 2017

Price 7.10p
Market cap £15m

Net debt (£m) at end March 2017 9.0
*Convertible loan notes treated as £22.0m debt

Shares in issue 206.2m
Free float 58.9%
Code IEH
Primary exchange LSE
Secondary exchange N/A

Share price performance



%	1m	3m	12m
Abs	(4.1)	20.3	(17.7)
Rel (local)	(2.7)	19.6	(26.5)
52-week high/low		17.2p	4.5p

Business description

Intelligent Energy Holdings delivers clean energy solutions for the distributed energy, diesel replacement, automotive and aerial drone markets. Working with international companies, Intelligent Energy aims to embed its fuel cell stack technology into applications across its target markets.

Next events

Preliminary results November 2017

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Intelligent Energy's interims were in line with the guidance given at the AGM in March. The results demonstrate that management has succeeded in reducing cash burn to its stated target of c £1.6m/month. It intends to bring the group to a cash break-even position within the next two years through volume roll-out of standard air-cooled products. Project wins during the period indicate there is appetite for Intelligent Energy's fuel cell stacks in the target markets, although we note that additional funding will be required to support this process. We leave our estimates unchanged.

Year end	Revenue (£m)	EBITDA* (£m)	PBT** (£m)	EPS (p)	DPS (p)	P/E (x)
09/14	13.6	(52.4)	(58.0)	(30.4)	0.0	N/A
09/15	78.2	(46.2)	(51.8)	(21.4)	0.0	N/A
09/16	91.8***	(33.4)	(42.8)	(20.2)	0.0	N/A
09/17e	24.6	(13.2)	(21.7)	(9.1)	0.0	N/A

Note: *Adjusted as per company presentation. **PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

***Including £85.1m revenues from power management activity.

Cash-burn reduction target achieved

Stripping out revenues from the power management activity, which was discontinued in November (£16.7m H117, £40.9m H116), revenues dropped from £3.0m to £2.0m. Total adjusted EBITDA losses more than halved from £21.6m to £9.1m, reflecting the cost-reduction programme implemented during H216. Cash consumption during the half-year period totalled £7.7m, of which £2.0m was interest on the convertible loan notes, leaving £13.0m at the end of March. Our model shows that if costs are maintained at these levels, the group has sufficient cash to support the expected growth in commercial products during FY17, but will need to secure additional funding to reach positive cash flow. Management is in discussions with potential customers to deliver a trading-related solution.

First sales of commercial B2B products

During H117, Intelligent Energy was reshaped to focus on driving sales of commercially ready B2B products. The group exited from its Indian energy management business and won contracts in two of its target segments: stationary power and drones. It sold technology demonstration units for stationary power applications in China, India, Japan and the US. In May, it was appointed technology lead on a €3.5m EU programme involving Toyota Motor Europe, among others, to provide a blueprint for fully automated mass manufacture of fuel cell stacks for the automotive market. The existing relationship with Suzuki continues.

Valuation: Negative impact of funding uncertainty

Our analysis indicates that Intelligent Energy is trading on EV/sales multiples that are towards the lower end of the range of its peers. We believe that removal of the funding uncertainty will be a key catalyst for the share price performance.

Product roll-out

During H117, Intelligent Energy was reshaped to focus on near-term opportunities to deliver products for deployment in distributed power generation and UAVs. It has already won contracts in both segments. The first is to supply 600 1kW fuel cell modules to US-based Luxfer-GTM Technologies for integration into Luxfer-GTM's Zero-Set Lite portable light towers. These are used to supply portable lighting for events and entertainment, roadside construction, military and disaster response situations. Fuel cells are an ideal substitute for diesel generators at entertainment and sporting events because the technology is silent and does not generate harmful particulates. The second contract is with PINC to supply fuel cell systems for powering UAVs. Switching from battery to fuel cell more than trebles flight times, which substantially improves drone efficiency.

Intelligent Energy will be providing the fuel cell stacks for a fleet of Suzuki Burgman scooters that will be used as part of a hydrogen fuel cell fleet trial by the London Metropolitan Police planned for this summer. The programme confirms that the relationship of over ten years with Suzuki continues. The scooters will deploy IEH's 4kW air-cooled fuel cells. This is a compact, lightweight package that meets automotive requirements, standards and safety criteria. In May, Intelligent Energy was also appointed as technology lead on a €3.5m EU programme involving Toyota Motor Europe, among others, to provide a blueprint for fully automated mass manufacture of fuel cell stacks for the automotive market.

In line with its focus on commercially ready B2B products, in June the group launched a range of fuel cell module products designed specifically for portable and stationary power applications including telecommunications, disaster recovery, portable power generation, back-up power, micro-grids, auxiliary power units and material handling equipment. The new products deliver a range of power outputs from 1kW-4kW and are optimised for hybridisation with batteries, enabling further efficiency.

Financial performance

P&L

Stripping out revenues from the power management activity, revenues dropped from £3.0m to £2.0m. Revenues from the power management operation in India fell from £40.9m to £16.7m as activity was discontinued on 30 November 2016. Total adjusted EBITDA losses more than halved from £21.6m to £9.1m, £2.3m of which was attributable to the discontinued power management activity. The narrowing of losses reflects the cost reduction programme implemented during H216. R&D costs (excluding £3.7m restructuring costs in H116) declined from £6.9m to £1.5m, as effort was focused on the air-cooled technology. The group retains the IP and capability for the evaporatively cooled technology and consumer applications, and will be able to engage in funded projects deploying this IP going forward. Operations and Application Engineering costs (excluding £19.3m write-downs in H116) decreased from £11.1m to £6.9m. Administration costs were cut from £4.5m to £2.6m. However, finance costs increased from £1.1m to £3.2m because of the interest on the convertible loan notes issued in H216 (13.0% per annum on £30.0m), £2.0m of which was a cash charge.

Cash flow

Cash consumption during the half-year period totalled £7.7m, of which £2.0m was interest on the convertible loan notes, leaving £13.0m at the end of March. Working capital reduced by £0.8m, as stocks fell by £0.6m, primarily because there is no longer need to hold diesel for the power

management activity. A minimal £0.1m was expended on capex and £0.7m on patent application activity as the group continued to invest its IP portfolio.

Estimates

The contracts discussed above underpin our assumptions of £5.0m revenues from the provision of engineering services and £3.0m from product sales during FY17, so we leave our estimates unchanged. The stacks for the contracts discussed above are being manufactured on an existing line at IEH's headquarters in Loughborough. Current staffing levels are sufficient for this and for the provision of engineering services. While management is not able to reduce the R&D and operating cost base further without adversely affecting core capability, management is implementing c £0.3m/pa savings by reducing the costs relating to being a listed company, while retaining plc status. These measures include non-executive director Mike Muller stepping down from the board at end FY17. Paul Heiden, non-executive chairman, also intends to step down at that point.

Our model shows that if costs are maintained at H117 levels, the group has sufficient cash to support the expected growth in commercial products during FY17 but will need to secure additional funding to reach positive cash flow. Management is in discussions with potential customers to deliver a trading-related solution. We note that the last date for conversion of the loan notes, which is at the holders' option, is 17 May 2019.

Valuation: Removal of funding uncertainty required

Exhibit 1: EV/sales multiples for listed peers			
Company	Market cap	Historical EV/sales (x)	Current EV/sales (x)
AFC Energy	£42m	39.9	9.2
Ballard Power Systems	£372m	4.9	3.8
Ceres Power Holdings	£116m	98.4	39.8
Electro Power Systems	£48m	7.7	3.4
FuelCell Energy	£58m	0.7	1.0
Heliocentris Energy Solutions	£0.2m	0.4	-
Hydrogenics	£95m	4.0	2.4
ITM Power	£53m	25.7	8.9
Proton Power Systems	£19m	27.8	-
Plug Power	£352m	5.5	3.4
SFC Energy	£31m	0.9	0.7
Mean		11.7	4.1
Intelligent Energy (excluding Power Management revenues)	£16m	2.5	2.1
Intelligent Energy (excluding Power Management revenues) – all convertible loan notes converting	£45m	3.7	3.1

Source: Bloomberg, Edison Investment Research. Note: Grey shading indicates exclusion from mean. Prices at 10 July 2017.

For calibration, we examine sales-based peer group multiples. (Note: IEH's multiples strip out the revenues attributable to the Indian energy management activity because this has been discontinued and generated minimal margins.) The comparison shows that IEH is trading on multiples towards the lower end of the range of its peers. However, until the company's funding issues have been resolved, this valuation gap is largely irrelevant. Nonetheless, it does indicate the potential for valuation upside in the event of successful funding leading to product volume-based revenues and, in due course, positive cash flows. We note the potential impact of the convertible loan notes issued in May 2016 (£30.0m at 8p). This action secured financing through to FY18, but introduced a source of significant potential dilution. If all of these loan notes are converted to shares, this represents an additional 375m shares to the 206m currently in issue.

Exhibit 2: Financial summary

	£m	2014	2015	2016	2017e
Year end 30 September		IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS					
Revenue		13.6	78.2	91.8	24.6
Cost of Sales		(9.9)	(75.9)	(90.0)	(23.7)
Gross Profit		3.7	2.3	1.8	0.9
EBITDA		(52.4)	(46.2)	(33.4)	(13.2)
Operating Profit (before amort. and except.)		(46.0)	(51.2)	(38.1)	(17.8)
Amortisation of acquired intangibles		0.0	0.0	0.0	0.0
Exceptionals		(7.1)	(0.3)	(21.6)	(0.5)
Share based payments		(2.6)	(2.3)	(0.2)	0.0
Operating Profit		(55.6)	(53.8)	(59.9)	(18.3)
Net Interest		(4.0)	(1.3)	(2.7)	(3.9)
Share of losses from JVs and exceptionals		0.0	0.7	(2.0)	0.0
Profit Before Tax (norm)		(58.0)	(51.8)	(42.8)	(21.7)
Profit Before Tax (FRS 3)		(59.6)	(54.4)	(64.6)	(22.2)
Tax		11.4	11.6	(18.1)	3.0
Profit After Tax (norm)		(46.6)	(40.2)	(39.0)	(18.7)
Profit after tax (FRS 3)		(48.2)	(42.8)	(82.7)	(19.2)
Average Number of Shares Outstanding (m)		153.4	188.2	193.3	206.2
EPS - normalised (p)		(30.4)	(21.4)	(20.2)	(9.1)
EPS - normalised fully diluted (p)		(30.4)	(21.4)	(13.5)	(2.5)
EPS - (IFRS) (p)		(31.4)	(22.7)	(42.8)	(9.3)
Dividend per share (p)		0.00	0.00	0.00	0.00
Gross Margin (%)		27.4	2.9	2.0	3.7
EBITDA Margin (%)		N/A	N/A	N/A	N/A
Operating Margin (before GW and except) (%)		N/A	N/A	N/A	N/A
BALANCE SHEET					
Fixed Assets		37.9	59.8	10.7	8.5
Intangible Assets		14.7	29.4	7.9	6.8
Tangible Assets		6.9	8.5	2.8	1.7
Deferred tax assets		16.3	21.9	0.0	0.0
Current Assets		107.5	45.2	33.0	17.1
Stocks		4.1	5.3	1.6	1.6
Debtors		11.1	11.5	7.8	9.1
Cash and short-term deposits		88.9	24.2	20.6	3.4
Current tax assets		3.4	4.2	3.0	3.0
Current Liabilities		(17.6)	(14.3)	(8.7)	(9.8)
Creditors		(17.6)	(14.3)	(8.4)	(9.5)
Short term borrowings		0.0	0.0	(0.3)	(0.3)
Long Term Liabilities		0.0	(3.0)	(22.8)	(24.0)
Long term borrowings		0.0	0.0	(21.0)*	(22.2)**
Other long term liabilities		0.0	(3.0)	(1.8)	(1.8)
Net Assets		127.8	87.7	12.2	(8.2)
CASH FLOW					
Operating Cash Flow		(50.6)	(51.5)	(31.4)	(13.9)
Net Interest		0.3	0.1	(1.1)	(3.9)
Tax		3.8	4.8	5.1	3.0
Capex		(6.8)	(19.4)	(3.8)	(2.4)
Acquisitions/disposals		1.1	1.0	0.0	0.0
Equity financing		108.4	0.2	1.1	0.0
Dividends		0.0	0.0	0.0	0.0
Forex/Other		(0.0)	0.1	0.1	0.0
Net Cash Flow		56.1	(64.7)	(30.0)	(17.2)
Opening net debt/(cash)		(13.1)	(88.9)	(24.2)	0.7
HP finance leases initiated		0.0	0.0	0.0	0.0
Other		19.7	0.0	5.1	(1.2)
Closing net debt/(cash)		(88.9)	(24.2)	0.7	19.1

Source: *Including £20.7m liability of convertible loan notes. **Including £22.0m liability of convertible loan notes.

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