

Alexium International Group Ltd

Buy

AJX's 4C and updated CY16 guidance

Materials / Diversified Chemicals

2 November 2016

Company Update

Ticker	AJX AU
Stock Price	\$0.620
Target Price	\$0.997
Forecast Capital Return	62.0%
Forecast Dividend Yield	0.0%
Estimated Total Return - 12 Mth Forward	62.0%

Company market data

Market Cap.	\$181.9m
Free Float (%)	42.9
Enterprise Value	\$170.7m
52 Week Range	\$0.48 - \$0.96
Shares Out.	295.8m
Avg. Daily Value	\$0.0m

Estimates changes	2016a	2017e	2018e	2019e
Core NPAT - old	(12.2)	1.9	4.2	8.0
Core NPAT - new	(15.4)	(6.2)	1.7	4.9
% Change	27.0	(429.3)	(59.6)	(38.3)
Core EPS dil. (€) - old	(4.4)	0.6	1.4	2.7
Core EPS dil. (€) - new	(5.5)	(2.1)	0.6	1.7
% Change	27.0	(429.3)	(59.6)	(38.3)
DPS (€) - old	0.0	0.0	0.0	0.0
DPS (€) - new	0.0	0.0	0.0	0.0
% Change	-	-	-	-

All figures are in AUD unless otherwise specified.

Share price performance

Alexium International Group Ltd vs. AS52 (rebased index)



Analysts

Olivia Bible

+61 2 8288 5408

olivia.bible@moelis.com

Ronan Barratt

+61 2 8288 5426

ronan.barratt@moelis.com

Event

AJX reported its 1QFY17 4C on 31 October 2016. Cash receipts for the quarter were A\$3.8m, an increase of 440% over last reporting period with a significant further increase in receipts forecasted for the remainder of the calendar year. This brings AJX's cash receipts for the 9 months ending September 2016 to A\$5.9m.

Cash payments for the quarter equated to A\$5.5m with significant increases in staff and administration costs. Additionally, A\$0.85m of capex was spent in the quarter, over 4 times FY16's capex spend of \$0.2m. We view the vast majority of this capex spend as one-off in nature as AJX moved into its new facility in Greer.

Update on CY16 guidance and potential licencing deals

AJX commented that, "As at the end of October 2016, Alexium is currently tracking at A\$15m for CY2016 with licencing revenue and additional contract revenues to year end, yet to be included as part of the earlier US\$18.5m CY2016 projection." We have reduced our FY17 revenue estimates to be in-line with CY16 revenue of A\$15m. We understand that there have been delays as some planned contract revenues are now set to arrive in early 2017 following longer than expected customer end product certification processes. AJX commented that the quantum of potential revenue in each case where delay has occurred has significantly increased as the relevant customers have increased the product range under the respective contracts.

While it is disappointing that AJX is not currently tracking in-line with its original guidance of US\$18.5m, we believe this was already factored into the share price. In addition, the expanded contracts and potential licencing deals (structured with upfront payments) could represent upside to our CY16 revenue estimate of A\$15m. AJX commented that the quarter showed a marked increase in customer interest and requests for licencing and exclusivity arrangements for its products and is currently evaluating and/or negotiating 7 separate agreements in the FR cotton, epoxy and cooling market spaces. "Licences may include upfront payments which may be received in the December quarter with ongoing royalties and minimum sales payments over the respective terms of such licences."

Investment View

We reiterate our BUY rating but reduce our 12 month target price from \$1.20 to \$1.00. We view AJX as a strategic investment leveraging increased scrutiny on stringent fire safety regulations and banning of toxic and harmful chemicals in traditional brominated and halogenated flame retardant products.

Y/E Jun 30	2016a	2017e	2018e	2019e
EBITDA	(15.3)	(5.8)	2.8	7.4
EV/EBITDA	nm	nm	60.3x	22.9x
Core NPAT	(15.4)	(6.2)	1.7	4.9
Core EPS (Diluted) (€)	(5.5)	(2.1)	0.6	1.7
P/E	nm	nm	107.9x	37.0x
EPS growth	87.2%	(62.3%)	(127.2%)	191.5%
DPS (€)	0.0	0.0	0.0	0.0
Yield	0.0%	0.0%	0.0%	0.0%
DPS growth	-	-	-	-
Dividend Payout Ratio	0.0%	0.0%	0.0%	0.0%

All figures are in AUD.

Changes to our estimates

We have reduced our FY17 estimates to be in-line with AJX's CY16 revenue run rate of A\$15m (US\$11.5m based on the current spot rate of \$0.765). The timing delays in CY16 have had a flow-on effect for our FY17, FY18 and FY19 estimates given we forecast by contract. Based on the current revenue run-rate, assuming no licencing deals and that AJX only converts one trial customer to a meaningful revenue customer per year, we now estimate that AJX will be profitable in FY18 rather than FY17. We acknowledge that there is upside risk to our estimates, especially in FY18 and beyond. We note that our estimates do not factor in explicit estimates for the carpets division and Alexicool Phase Change Material Solutions.

Figure 1: Moelis' estimate changes

A\$m	Old	New	% chg
FY17E			
Revenue	41.7	32.7	-21.5%
EBITDA	2.5	(5.8)	-329.4%
EBIT	2.2	(6.2)	-377.2%
NPAT	1.9	(6.2)	-429.3%
FY18E			
Revenue	55.1	48.1	-12.7%
EBITDA	6.0	2.8	-53.0%
EBIT	5.5	2.4	-57.4%
NPAT	4.2	1.7	-59.6%
FY19E			
Revenue	76.9	62.2	-19.1%
EBITDA	11.5	7.4	-35.3%
EBIT	10.8	7.0	-35.5%
NPAT	8.0	4.9	-38.3%

Source: Company, Moelis Analysis

Update on regulatory changes

In our view, one of the biggest drivers for new contract wins will be regulatory changes banning the use of harmful flame retardant chemicals. We see the regulatory environment continuing to shift in favour of eco-conscious flame retardant products.

The US Environmental Protection Agency recently announced the first 5 chemicals for immediate review and action under the recently signed update to the Toxic Substances Control Act. Included are 2 commonly used, dangerous flame retardants (Deca and Tris). AJX is well positioned for growth if the EPA acts to remove these chemicals from the marketplace. In addition, the US Consumer Product Safety Commission is expected to issue regulations outlawing the use of certain kinds of flame retardant products in the marketplace. Specifically, in the transport sector, AJX has successfully produced and scaled-up chemical solutions that meets new, strict environmental regulations including VOC and fogging requirements currently being implemented for model year 2018. This makes AJX's chemistries superior to those now available.

Estimates by end-user markets and by contract

Below we estimate revenue and gross profit by end user market. Given the ramp-up profile of the contracts, we have weighted our CY16 revenue estimates approximately 20% in 2H FY16 and 80% in 1H FY17. We have reduced this back end weighting in future years.

Bedding and decorative fabrics

Figure 2: Moelis' estimates for the bedding and decorative fabrics market

A\$m	FY16A	Moelis estimates								
		1H17E	2H17E	FY17E	1H18E	2H18E	FY18E	1H19E	2H19E	FY19E
No. trial customers in the pipeline	13	13	12	12	12	11	11	11	10	10
No. revenue customers	4	4	5	5	5	6	6	6	7	7
Sales (USD)	0.6	3.4	4.2	7.6	4.4	5.3	9.7	5.6	6.5	12.1
Sales (AUD)	0.9	3.7	5.5	9.2	5.9	7.0	12.9	7.4	8.7	16.2
% chg				947%	60%	27%	40%	27%	24%	25%
Gross Profit		1.5	2.2	3.7	2.6	3.2	5.8	3.4	3.9	7.3
Margin		40%	40%	40%	45%	45%	45%	45%	45%	45%

Source: Company, Moelis Analysis

Key achievements in bedding and decorative fabrics division for 1Q FY17 include:

1. Selected by 2 producers of mattress ticking fabric to provide an all-in-one FR / cooling / anti-odour package for one of the world's largest mattress brands; and
2. Developed a cooling solution for a key player in pillow manufacturing for department stores and retailers and are in exclusivity negotiations.

Military and work wear

Figure 3: Moelis' estimates for the military and work wear market

A\$m	FY16A	Moelis estimates								
		1H17E	2H17E	FY17E	1H18E	2H18E	FY18E	1H19E	2H19E	FY19E
No. trial customers in the pipeline	13	13	12	12	12	11	11	11	10	10
No. revenue customers	2	2	3	3	3	4	4	4	5	5
Sales (USD)	0.1	1.4	2.1	3.4	2.1	2.8	4.9	2.9	3.6	6.4
Sales (AUD)	0.2	1.5	2.7	4.2	2.8	3.7	6.5	3.8	4.8	8.6
% chg				2337%	86%	37%	55%	37%	29%	32%
Gross Profit		0.6	1.1	1.7	1.3	1.7	2.9	1.7	2.2	3.9
Margin		40%	40%	40%	45%	45%	45%	45%	45%	45%

Source: Company, Moelis Analysis

Key achievements in the military and work wear division include:

1. Participation in all submissions with multiple vendors and working with government agencies to promote its new green technology;
2. AJX has conducted top level meetings with the United States Marine Corps to discuss its innovative FR treatment for uniforms and has provided FR treated fabrics to the Marine Corps for testing and review. The Marine Corps is seeking to enhance the FR capabilities of its uniforms in the next year; and
3. AJX continued to establish critical supply chain partnerships including entering exclusivity negotiations with the current holders of a major US military program.

Automotive and transport

Figure 4: Moelis' estimates for the automotive and transport market

A\$m	FY16A	Moelis estimates									
		1H17E	2H17E	FY17E	1H18E	2H18E	FY18E	1H19E	2H19E	FY19E	
No. trial customers in the pipeline	8	8	7	7	7	6	6	6	6	5	5
No. revenue customers	5	5	6	6	6	7	7	7	7	8	8
Sales (USD)	0.2	2.8	3.4	6.1	3.6	4.1	7.7	4.4	5.0	9.4	
Sales (AUD)	0.3	3.0	4.4	7.5	4.7	5.5	10.2	5.9	6.7	12.6	
% chg				2553%	55%	25%	37%	25%	22%	23%	
Gross Profit		0.9	1.3	2.2	1.6	1.9	3.6	2.1	2.4	4.4	
Margin		30%	30%	30%	35%	35%	35%	35%	35%	35%	

Source: Company, Moelis Analysis

AJX's customers in Europe and elsewhere have issued purchase orders for final stage plant trials to add Alexiflam chemistry to automotive body cloth fabric for upcoming model years.

Outdoor fabrics

Figure 5: Moelis' estimates for the outdoor fabrics market

A\$m	FY16A	Moelis estimates								
		1H17E	2H17E	FY17E	1H18E	2H18E	FY18E	1H19E	2H19E	FY19E
No. trial customers in the pipeline	4	4	3	3	3	2	2	2	1	1
No. revenue customers	1	1	2	2	2	3	3	3	4	4
Sales (USD)	0.1	1.4	2.8	4.1	2.9	4.4	7.3	4.6	6.1	10.7
Sales (AUD)	0.2	1.5	3.6	5.1	3.8	5.8	9.6	6.1	8.2	14.3
% chg				2995%	156%	59%	87%	59%	41%	48%
Gross Profit		0.6	1.5	2.1	1.7	2.6	4.3	2.8	3.7	6.4
Margin		40%	40%	40%	45%	45%	45%	45%	45%	45%

Source: Company, Moelis Analysis

Key achievements in the outdoor fabrics division in 1Q FY17 include:

1. AJX has scheduled a bulk customer trial in Asia for December with 2 weeks dedicated to ensure the successful plant implementation of the Alexiflam technology; and
2. AJX has initiated parallel programs with adjacent tenting fabric suppliers.

Coatings and polymers

Figure 6: Moelis' estimates for the coatings and polymers market

A\$m	FY16A	Moelis estimates								
		1H17E	2H17E	FY17E	1H18E	2H18E	FY18E	1H19E	2H19E	FY19E
No. trial customers in the pipeline	17	17	16	16	16	15	15	15	14	14
No. revenue customers	7	7	8	8	8	9	9	9	10	10
Sales (USD)	0.5	2.5	2.8	5.3	3.0	3.4	6.5	3.6	4.0	7.7
Sales (AUD)	0.7	2.7	3.8	6.5	4.0	4.5	8.6	4.9	5.4	10.3
% chg				823%	49%	21%	33%	21%	20%	20%
Gross Profit		0.5	0.8	1.3	1.0	1.1	2.1	1.2	1.4	2.6
Margin		20%	20%	20%	25%	25%	25%	25%	25%	25%

Source: Company, Moelis Analysis

Key achievements in the coatings and polymers division in 1Q FY17 include:

1. AJX saw a 150% increase in sampled customers with laboratory projects; and
2. AJX entered in final UL certification with one of the largest circuit board manufacturers in the world and is a final candidate with one of the largest Epoxy manufacturers in the USA.

Profit and Loss (\$m)	2015a	2016a	2017e	2018e	2019e
Revenue	0.1	3.2	32.5	47.8	62.0
<i>Growth</i>	(75.6%)	5,241.6%	927.0%	47.3%	29.5%
EBITDA	(6.4)	(15.3)	(5.8)	2.8	7.4
<i>Growth</i>	132.8%	140.4%	(61.9%)	(148.6%)	162.9%
Dep'n & Amort	(0.1)	(0.2)	(0.4)	(0.5)	(0.5)
EBIT	(6.5)	(15.5)	(6.2)	2.4	7.0
<i>Growth</i>	128.7%	138.5%	(59.9%)	(138.1%)	194.7%
Net Interest Expense	(0.4)	0.0	0.0	0.0	0.1
Profit Before Tax	(6.9)	(15.4)	(6.2)	2.4	7.0
Tax	0.0	0.0	0.0	(0.7)	(2.1)
<i>Tax Rate (%)</i>	0.0%	0.0%	0.0%	30.0%	30.0%
Minorities	0.0	0.0	0.0	0.0	0.0
NPAT (Underlying)	(6.9)	(15.4)	(6.2)	1.7	4.9
<i>Growth</i>	106.9%	125.0%	(59.9%)	(127.2%)	191.5%
One-Off Items	(4.9)	0.0	0.0	0.0	0.0
NPAT (Reported)	(11.8)	(15.4)	(6.2)	1.7	4.9
EPS (Underlying) (€)	(3.0)	(5.5)	(2.1)	0.6	1.7
<i>Growth</i>	56.8%	87.2%	(62.3%)	(127.2%)	191.5%

Balance Sheet (\$m)	2015a	2016a	2017e	2018e	2019e
Cash	11.6	11.2	12.0	17.3	26.0
Inventory	0.0	0.0	0.0	0.0	0.0
Current Receivables	0.1	0.2	3.3	4.4	5.6
PPE	0.4	0.8	1.5	1.5	1.7
Intangibles	0.2	0.1	0.1	0.1	0.1
Other	0.3	1.8	1.8	1.8	1.8
Total Assets	12.6	14.2	18.8	25.1	35.2
Current Payables	0.6	2.8	13.2	17.5	22.3
ST Debt	0.0	0.0	0.0	0.0	0.0
LT Debt	0.0	0.0	0.0	0.0	0.0
Provisions	0.1	0.1	0.1	0.1	0.1
Other	0.1	0.0	0.0	0.0	0.0
Total Liabilities	0.8	2.9	13.3	17.6	22.4
Net Assets	11.8	11.3	5.4	7.5	12.8
Equity & Reserves	45.8	60.7	61.1	61.4	61.8
Retained Profits	(34.0)	(49.4)	(55.6)	(53.9)	(49.0)
Shareholders' Equity	11.8	11.3	5.5	7.5	12.8
Minorities	0.0	0.0	0.0	0.0	0.0
Total Equity	11.8	11.3	5.5	7.5	12.8

Cashflow (\$m)	2015a	2016a	2017e	2018e	2019e
EBITDA	(6.4)	(15.3)	(5.8)	2.8	7.4
Net Interest	(0.1)	0.0	0.0	0.0	0.1
Tax	0.0	0.1	0.0	(0.7)	(2.1)
Δ in Working Capital	(6.5)	(15.5)	7.3	3.2	3.6
Other	8.6	20.6	0.0	0.0	0.0
Operating Cash Flow	(4.3)	(10.1)	1.5	5.4	9.0
<i>Growth</i>	38.7%	136.0%	(114.7%)	263.2%	66.7%
Capex	(0.1)	(0.2)	(1.1)	(0.5)	(0.6)
Acquisitions	0.0	0.0	0.0	0.0	0.0
Divestments	0.0	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0
Investing Cash Flow	(0.1)	(0.2)	(1.1)	(0.5)	(0.6)
Equity Raised	11.9	9.5	0.0	0.0	0.0
Dividends Paid	0.0	0.0	0.0	0.0	0.0
Net Borrowings	(0.8)	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0
Financing Cash Flow	11.1	9.5	0.0	0.0	0.0
FX / Non Cash Items	0.7	0.4	0.4	0.4	0.4
Change in Cash	7.4	(0.4)	0.8	5.3	8.7
Free Cash Flow	(4.4)	(10.3)	0.4	4.9	8.3

Valuation Summary	
Current Mkt Capitalisation	181.9
Shares on Issue	295.8
Last Price	0.620
12 Mth Target Price	0.997
Total Estimated 12 Mth Return	62.0%
12 Mth Fwd Capital Return	62.0%
12 Mth Fwd Dividend Yield	0.0%

Valuation Ratios	2015a	2016a	2017e	2018e	2019e
EPS (Underlying) (€)	(3.0)	(5.5)	(2.1)	0.6	1.7
<i>Growth</i>	56.8%	87.2%	(62.3%)	(127.2%)	191.5%
P/E (x)	nm	nm	nm	107.9x	37.0x
Small Industrials (ex Fin's)	0.0x	17.3x	15.3x	13.6x	12.9x
Premium / (Discount)	nm	nm	nm	692.8%	186.3%
EV/EBITDA (x)	nm	nm	nm	60.3x	22.9x
Small Industrials (ex Fin's)	0.0x	22.4x	10.8x	9.8x	8.8x
Premium / (Discount)	nm	nm	nm	517.1%	159.3%
DPS (€)	0.0	0.0	0.0	0.0	0.0
<i>Growth</i>	-	-	-	-	-
Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Payout Ratio (%)	0.0%	0.0%	0.0%	0.0%	0.0%
Franking (%)	0.0%	0.0%	0.0%	0.0%	0.0%
NTA	11.6	11.1	5.3	7.4	12.6
NTA/Share (\$)	0.05	0.04	0.02	0.02	0.04

Performance Ratios	2015a	2016a	2017e	2018e	2019e
ROA	(54.4%)	(109.1%)	(33.0%)	6.7%	14.0%
ROE	(58.1%)	(137.1%)	(113.6%)	22.5%	38.4%
ROIC	(3,505.7%)	(31,626.8%)	94.7%	(16.9%)	(37.0%)
Net Debt (Cash) (\$m)	(11.6)	(11.2)	(12.0)	(17.3)	(26.0)
Net Debt/EBITDA (x)	1.8x	0.7x	2.1x	(6.1x)	(3.5x)
ND/(ND + Equity) (%)	(6,274.0%)	(22,907.2%)	183.2%	176.9%	197.1%
Interest Cover (x)	(15.1x)	(351.8x)	(86.5x)	50.2x	114.7x
Working Capital	(0.5)	(0.9)	(8.2)	(11.4)	(15.0)
Working Capital/Sales (%)	(882.0%)	(29.6%)	(25.3%)	(23.9%)	(24.2%)

Cash Flow Metrics	2015a	2016a	2017e	2018e	2019e
FCF/Share (\$)	(0.02)	(0.04)	0.00	0.02	0.03
Price/FCPS (x)	nm	nm	442.6x	37.2x	21.8x
Free Cash Flow Yield (%)	(3.1%)	(6.0%)	0.2%	2.7%	4.6%
Gross Cash Conversion	0.0%	66.4%	(25.9%)	215.4%	148.7%
Capex/Sales (%)	(199.5%)	(6.6%)	(3.3%)	(1.0%)	(1.0%)
Capex/Depreciation (x)	0.9x	1.0x	2.8x	1.0x	1.3x

Margins	2015a	2016a	2017e	2018e	2019e
EBITDA	(10,743.7%)	(483.4%)	(17.9%)	5.9%	12.0%
EBIT	(10,970.9%)	(489.9%)	(19.1%)	4.9%	11.2%
NPAT	(11,595.1%)	(488.5%)	(19.1%)	3.5%	7.9%

Valuation Methodology	
WACC (%)	10.9%
Discounted Cash Flow Valuation	0.879
Sum-of-the-Parts Valuation	0.000
Average Valuation	0.879
12 Mth Target Price	0.997

RESEARCH & SALES RESPONSIBILITIES

Equities

Simon Scott	Head of Equities	+612 8288 5418
Elliot Leahey	Operations Manager	+612 8288 5402
Sarah Sagvand	Desk Assistant	+612 8288 5401

Equities Sales & Trading

John Garrett	+612 8288 5409
Angus Murnaghan	+612 8288 5411
Ian McKenzie	+612 8288 5404
Bryan Johnson	+612 8288 5412
Andrew Harvey	+612 8288 5428
Mitchell Hewson - <i>Head of Execution</i>	+612 8288 5417
Aaron Payne - <i>Real Estate</i>	+612 8288 5405

Equities Research

Real Estate

Hamish Perks	+612 8288 5419
Edward Day	+612 8288 5424
Ronan Barratt	+612 8288 5426

Industrials

Garry Sherriff	+612 8288 5421
Olivia Bible	+612 8288 5408
Benjamin Atkinson	+612 8288 5422
Sarah Mann	+612 8288 5407
Keiran Hoare	+612 8288 5423

US Distribution Partner - Weeden & Co.

Matthew McCloghry	+1 646 227 5575
<i>mmccloughry@weedenco.com</i>	

email: firstname.lastname@moelis.com

DISCLOSURE APPENDIX

ANALYST CERTIFICATION

The Analysts, Olivia Bible, Ronan Barratt, responsible for the content of this research report, in whole or in part, certifies that with respect to the companies or securities that the individual analyses, that (1) the views expressed in this report accurately reflect his or her personal views on the subject companies and securities, and (2) no part of his or her compensation was, is, or will be directly or indirectly linked to the specific recommendations or views expressed in this research report.

COMPANY SPECIFIC DISCLOSURES

Our related body corporate Moelis Australia Advisory Pty Ltd (ACN 142 008 446 AFSL 345499) ("Moelis Advisory") was appointed as Bookrunner by the Alexium International Group Ltd (AJX AU) for a capital raising as announced to ASX on 14 April 2016 for which Moelis Advisory received compensation.

RATING DEFINITIONS

All companies under coverage are assigned a rating of Buy, Hold or Sell based on the expected 12 month total return estimated by the analyst(s). The total return is a combination of the estimated capital gain or loss, in addition to the estimated 12 month forward dividends or distributions. In relation to all companies that Moelis Australia Securities conducts research coverage on the relevant total return bands that derive the ratings are:

Buy: >15% **Hold:** 5% to 15% **Sell:** <5%.

RATINGS DISTRIBUTION TABLE

Distribution of Ratings as at 2 November 2016

SELL	HOLD	BUY
5.9%	43.1%	51.0%

Rating and Price Target History: Alexium International Group Ltd (AJX AU) as of 1/11/2016



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