

# Orège

On track to reach our FY19 growth forecast

FY18 results update

General industrials

15 April 2019

**Price** €1.90

**Market cap** €35m

Net debt (€m) at 31 December 2018 44.4

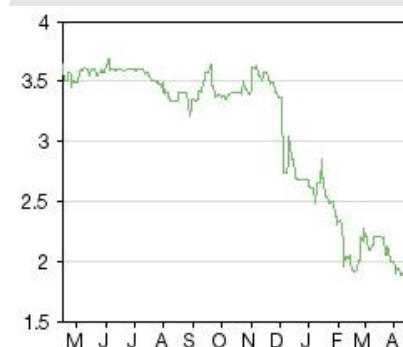
Shares in issue 18.6m

Free float 18%

Code ORÈGE

Primary exchange Euronext

## Share price performance



% 1m 3m 12m

Abs (14.5) (29.1) (47.5)

Rel (local) (18.0) (37.9) (48.8)

52-week high/low €3.69 €1.88

## Business description

Founded in 2006 and listed on Euronext in 2013, Orège is a clean-tech company that has developed an innovative, patented technology (solid, liquid, gas – SLG) to significantly reduce sludge treatment costs and improve environmental sustainability of the treatment process. Its core markets include North America, the UK, Germany and France.

## Next events

H1 results September 2019

## Analyst

Dario Carradori +44 (0)20 3077 5700

[industrials@edisongroup.com](mailto:industrials@edisongroup.com)

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Orège's FY18 results showed a significant revenue pick-up (six times restated 2017 revenues), with EBITDA and net income marginally ahead of our forecasts. The ytd ramp-up in orders implies that Orège is on track to reach our FY19 forecast of €6.3m revenues (2.8x FY18 revenues). The current share price is close to our bear case, which skews risk significantly to the upside in our view. Key share price catalysts are the continued ramp-up in orders and successful completion of the capital increase required by the end of 2019.

Year end	Revenue (€m)	EBITDA (€m)	EBIT (€m)	Net income (€m)	EV/sales (x)
12/17**	0.7	(10.1)	(11.4)	(13.5)	97.3
12/18	2.3	(7.7)	(8.5)	(10.9)	35.3
12/19e	6.3	(5.9)	(6.7)	(9.8)	12.7
12/20e	11.0	(3.8)	(4.6)	(8.5)	7.3

Note: \*Net income is normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments. \*\*FY17 results have been restated by the company and will be updated once the full accounts are made available.

## FY18 results confirm pick-up in orders

In FY18 Orège experienced a strong pick-up in orders, which led to revenue almost six times higher than 2017 (restated), albeit from a low base. Orège reported FY18 EBITDA and net income marginally better than our expectations, with revenue 13% lower than our expectations more than offset by lower operating expenses. Orège made progress on its order book as it stated that at the date of the FY18 results announcement (10 April), the overall value of the order book was €2.5m (vs €2.3m revenues in FY18) and several further contracts are expected to be signed in H119. Assuming the trend of commercial development continues, we believe Orège is well placed to achieve our unchanged FY19 revenue forecast of €6.3m, which implies 178% y-o-y growth.

## Long-term growth opportunity

Orège's proprietary and patented SLG technology reduces sludge treatment costs for utilities by up to 80%, with a strong investment case for its clients (payback periods of less than three years) and large environmental sustainability advantages. We estimate a €439m annual addressable market size for SLG technology (current applications only) in North America, the UK, Germany and France. Growth potential in Asia and Southern Europe could add to this estimate. We forecast revenues increasing from €6.3m in FY19 to our estimated base case revenue potential of €57m in FY23 (bear-bull range of €22–93m). We expect strong margin improvement, leading to positive EBITDA in FY21 and cash flow in FY22.

## Valuation: Current share price close to our bear case

Due to the early stage of commercial deployment, we believe investors should assess a range of potential growth outcomes and valuations. Following the recent decline, the current share price is closer to our bear case (€1.64/share), which skews risk significantly to the upside in our view (base case €3.84/share, bull case €9.31/share). Key share price catalysts are the continued ramp-up in orders and completion of the capital increase required by the end of 2019.

## On track to reach our FY19 growth forecast

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Orège's FY18 results showed a significant revenue pick-up (six times restated 2017 revenues). EBITDA and net income were marginally ahead of our forecasts as lower revenues were more than compensated by lower operating expenses. We believe the ytd ramp-up in orders puts Orège on track to reach our FY19 forecast of €6.3m revenues (2.8x FY18 revenues). The recent share price decline means the risks to valuation are significantly skewed to the upside, in our view.

### FY18 results confirm pick-up

In FY18 Orège experienced a strong pick-up in orders, which led to revenue almost six times higher than 2017 (restated), albeit from a low base. Orège reported FY18 EBITDA and net income marginally better than our expectations, with revenue lower than our expectations more than offset by lower operating expenses. Highlights of the FY18 results are as follows:

- Revenues of €2.26m, an almost sixfold increase on restated 2017 revenues of €0.39m. Revenues were 13% below our forecast of €2.59m.
- The EBITDA loss was €7.7m, >20% smaller than 2017 and 2% better than our forecast of €7.9m. This was driven by lower operating expenses than we previously expected, more than offsetting the lower revenues.
- Net loss was €10.9m, 20% smaller than 2017 and 3% better than our expectations.
- Net debt of €44.4m was broadly in line with our forecast (€44.0m).

### FY19 ramp-up in orders in line with our forecasts

We continue to believe that a significant ramp-up in orders is one of the key catalysts for the re-rating of the stock. Orège made progress over the last few months as it stated that at the date of the FY18 results announcement (10 April), the overall value of the order book was €2.5m (vs €2.3m revenues in FY18) and several further contracts are expected to be signed in H119. Assuming this trend of commercial development continues, we believe Orège is well placed to achieve our maintained FY19 revenue forecast of €6.3m, which implies 178% y-o-y growth. The order book was boosted by a contract in January 2019 for a six-year lease agreement for three SLG solutions with the City of Orlando, US, for over \$1.3m (we estimate a revenue contribution of around \$1m for FY19).

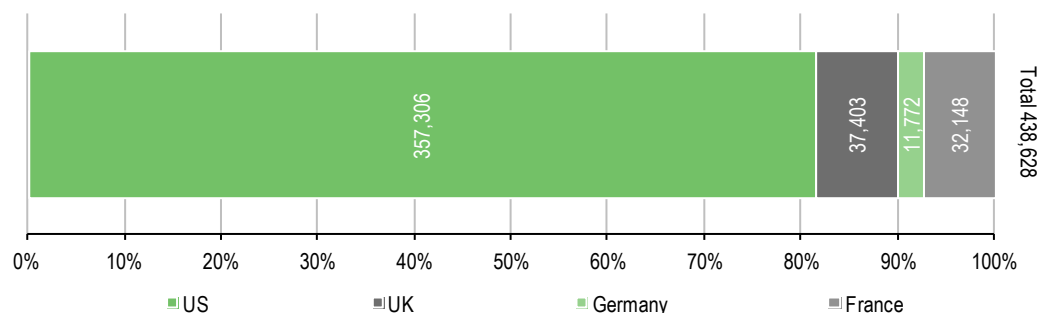
### Long-term growth: Innovation in environmental sustainability

Orège operates in the global wastewater equipment market (\$9.5bn per year market size with 5–6% annual growth, according to Global Water Intelligence). It has developed a proprietary and patented technology (solid, liquid, gas – SLG) that reduces sludge treatment costs for utilities by up to 80%, with a strong investment case for its clients (payback periods of less than three years). In addition to large economic savings, SLG brings important environmental sustainability advantages to the sludge treatment process (lower energy use and lower volumes transported, improved sludge quality, etc). Over the last few years, Orège has developed several successful references for various applications and geographies and is now ready to achieve its full commercial potential, particularly in the UK and North America. Client feedback on the technology strongly supports its effectiveness.

We derived our forecasts for Orège's top line by applying a range of penetration rate assumptions to the estimated size of the core market opportunities for the flagship product SLG in the key countries for Orège: the UK, North America, Germany and France. Our estimates are based on a forecast of a €439m annual addressable market size for SLG technology (current applications only)

in North America, the UK, Germany and France (we provided detailed calculations in our initiation note, [Innovation in environmental sustainability](#), published on 17 October 2018). These estimates do not include significant growth opportunities in Asia (especially following the signing of a partnership for distribution and integration of SLG solutions in Japan with ITCMT, a subsidiary of the Japanese ITOCHU Corporation) and in Southern Europe, which we understand Orège is also targeting.

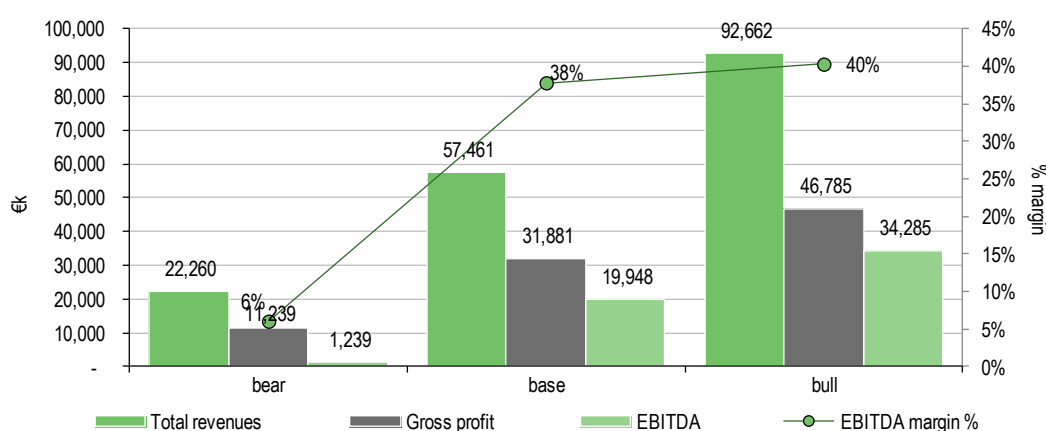
**Exhibit 1: Estimated annual addressable market for SLG (equipment + services, €000s)**



Source: Edison Investment Research

We forecast revenues increasing from €6.3m in FY19 to our estimated base case revenue potential of €57m in FY23 (in our [initiation note](#), we identified a bear-bull range of €22–93m revenues). We expect high operational leverage to drive a strong margin improvement, leading to positive EBITDA in FY21 and cash flow in FY22.

**Exhibit 2: Scenario analysis: bull-bear-base case revenues and earnings**



Source: Edison Investment Research

## We expect FY19 to confirm revenue growth trend

We continue to expect a significant revenue ramp-up and have made only small changes to our FY19/20 forecasts, with revenues broadly unchanged and marginally smaller EBITDA and net income losses, reflecting lower operating expenses.

**Exhibit 3: Forecast changes**

€000s		FY18	FY19e	FY20e
Revenues	New	2,260	6,281	11,007
	Old	2,588	6,291	11,042
	% change	(13%)	0%	0%
EBITDA	New	(7,749)	(5,943)	(3,802)
	Old	(7,888)	(6,086)	(3,940)
	% change	(2%)	(2%)	(3%)
EBIT	New	(8,537)	(6,743)	(4,602)
	Old	(8,888)	(6,886)	(4,740)
	% change	(4%)	(2%)	(3%)
Net income	New	(10,915)	(9,849)	(8,477)
	Old	(11,212)	(9,966)	(8,574)
	% change	(3%)	(1%)	(1%)
Net debt	New	44,382	55,350	65,219
	Old	43,999	54,784	64,160
	% change	1%	1%	2%

Source: Orège data, Edison Investment Research. Note: FY18 new = actual.

Importantly, as Orège's net equity fell below half of its called-up share capital in 2017, there is a requirement for it to proceed with a capital increase by the end of FY19. We believe clarity on the financial structure is the other important catalyst for the stock. Until then, investors have visibility on the short-term sustainability of the activities, as majority shareholder Eren (69% stake) has provided a €7m credit line to cover the financing needs in FY19.

## Valuation: Current share price close to our bear case

Due to the risks resulting from the early stage of commercial deployment, we believe investors should assess a large range of potential growth outcomes and valuations. As explained in our [initiation note](#), we used a valuation methodology similar to the one we use for early stages biotech companies: we estimated the addressable market size, assumed penetration rates and used a DCF methodology to take into account the future prospects of the group. We have used a 12.5% WACC, consistent with the rate we use for companies at a similar stage of development. The terminal value is based on median EV/Sales, EV/EBITDA, EV/EBIT values of more mature water/wastewater equipment companies (Exhibit 4).

**Exhibit 4: Valuation multiples for more mature water/wastewater equipment companies**

Company	EV/sales (x)			EV/EBITDA (x)			EV/EBIT (x)			P/E (x)		
	FY0	FY1	FY2	FY0	FY1	FY2	FY0	FY1	FY2	FY0	FY1	FY2
Fluence	1.8	1.1	0.7	N/A	90.9	7.9	N/A	-165.3	8.9	15.8	N/A	N/A
Alfa Laval	2.4	2.2	2.1	13.5	11.6	11.0	13.5	14.1	13.2	16.9	18.1	16.9
Mueller Water Products	2.1	1.9	1.8	11.4	9.1	8.4	11.4	12.5	11.0	N/A	N/A	N/A
Xylem	3.2	3.1	2.9	17.8	15.5	14.0	17.8	20.8	18.2	28.2	24.6	21.3
Evoqua Water Technologies	1.8	1.7	1.7	12.6	10.5	9.6	12.6	17.5	15.7	N/A	N/A	N/A
Gorman-Rupp	2.1	2.0	1.9	13.0	N/A	N/A	13.0	N/A	N/A	19.7	20.6	18.9
Franklin Electric	2.0	1.9	1.8	14.8	13.7	12.7	14.8	17.3	16.0	N/A	N/A	N/A
Andritz	0.7	0.7	0.6	9.0	7.1	6.7	9.0	9.8	9.0	18.2	12.6	11.5
Beijing Enterprises Water Group	3.9	3.6	3.3	11.9	11.1	9.8	11.9	11.8	10.4	10.2	8.9	7.8
Watts Water Technologies	1.9	1.9	1.8	12.5	11.8	11.3	12.5	14.4	13.6	22.5	20.7	19.2
Pentair	2.9	2.7	2.6	15.1	13.2	12.4	15.1	14.8	13.9	N/A	N/A	N/A
Itron	1.2	1.2	1.1	18.9	10.7	8.9	18.9	14.9	10.6	N/A	N/A	N/A
Forterra	1.7	1.7	1.6	8.1	7.6	7.3	8.1	9.1	8.7	N/A	N/A	N/A
<b>Median</b>	<b>2.0</b>	<b>1.9</b>	<b>1.8</b>	<b>12.6</b>	<b>11.4</b>	<b>9.7</b>	<b>12.6</b>	<b>14.3</b>	<b>12.1</b>	<b>18.2</b>	<b>19.3</b>	<b>17.9</b>

Source: Refinitiv. Note: Prices as at 10 April 2019.

Our valuation approach returns a base case valuation of €3.84/share (broadly unchanged vs €3.86/share previously). The base case valuation reflects a sustained growth in revenues (+74% FY19–23 CAGR), mostly in the UK and North America. If Orège can establish its technology as



industry standard and its products become widely adopted, we believe there is significant upside to the current share price (our valuation would be €9.31/share vs €9.36/share previously). On the contrary, the bear case of €1.64 (unchanged) reflects the impact of potential delays in ramping up the commercial development of the company.

Following a large decline over the last few months, the current share price is now closer to our bear case, which skews risks to the upside in our view. We believe that continued ramp-up in the order book and clarity on the financial structure would represent the most important positive catalysts for the share price.

Key risks to our forecasts and valuations include delays in ramping up commercial development, including risks associated with the requirement to organise public tenders for municipal clients; higher/lower competition and its impact on profit margins; and the potential impact of Brexit and friction on global trade (most of the addressable market is in the UK and North America).

**Exhibit 5: Financial summary**

Accounts: IFRS, year-end: December, €000s	2016	2017*	2018	2019e	2020e	2021e	2022e	2023e
<b>INCOME STATEMENT</b>								
Total revenues	703	706	2,260	6,281	11,007	19,996	37,236	57,461
Cost of sales	(1,568)	(597)	(600)	(2,358)	(4,464)	(8,367)	(16,188)	(25,579)
Gross profit	(865)	109	1,660	3,923	6,543	11,629	21,047	31,881
SG&A (expenses)	(14,103)	(10,238)	(9,409)	(9,866)	(10,346)	(10,849)	(11,378)	(11,933)
Depreciation and amortisation	(2,241)	(1,242)	(788)	(800)	(800)	(900)	(1,000)	(1,100)
Reported EBIT	(17,209)	(11,371)	(8,537)	(6,743)	(4,602)	(121)	8,669	18,848
Finance income/(expense)	(822)	(1,739)	(2,378)	(3,107)	(3,874)	(4,565)	(4,951)	(4,791)
Other income/(expense)	168	(411)	0	0	0	0	0	0
Exceptionals and adjustments	0	0	0	0	0	0	0	0
Reported PBT	(17,864)	(13,520)	(10,915)	(9,849)	(8,477)	(4,686)	3,719	14,057
Income tax expense (includes exceptionals)	114	0	0	0	0	0	0	0
Reported net income	(17,750)	(13,520)	(10,915)	(9,849)	(8,477)	(4,686)	3,719	14,057
Basic average number of shares, m	18.7	18.7	18.7	18.7	18.7	18.7	18.7	18.7
Basic EPS	(0.95)	(0.72)	(0.59)	(0.53)	(0.45)	(0.25)	0.20	0.75
DPS (€)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Adjusted EBITDA	(14,968)	(10,129)	(7,749)	(5,943)	(3,802)	779	9,669	19,948
Adjusted EBIT	(17,209)	(11,371)	(8,537)	(6,743)	(4,602)	(121)	8,669	18,848
Adjusted PBT	(17,864)	(13,520)	(10,915)	(9,849)	(8,477)	(4,686)	3,719	14,057
Adjusted EPS (€)	(0.95)	(0.72)	(0.59)	(0.53)	(0.45)	(0.25)	0.20	0.75
Adjusted diluted EPS (€)	(0.95)	(0.72)	(0.58)	(0.53)	(0.45)	(0.25)	0.20	0.75
<b>BALANCE SHEET</b>								
Property, plant and equipment	1,455	987	599	599	599	599	599	599
Intangible assets	242	190	190	190	190	190	190	190
Other non-current assets	1,857	2,779	2,779	2,779	2,779	2,779	2,779	2,779
Total non-current assets	3,554	3,956	3,568	3,568	3,568	3,568	3,568	3,568
Cash and equivalents	950	506	506	506	506	506	506	506
Inventories	1,860	1,354	953	2,621	3,474	4,558	6,173	6,827
Trade and other receivables	164	467	2,317	5,152	9,029	11,481	14,965	18,475
Other current assets	1,212	872	872	872	872	872	872	872
Total current assets	4,186	3,200	4,648	9,152	13,881	17,417	22,516	26,681
Non-current loans and borrowings	20,672	33,810	44,991	55,959	65,828	71,333	69,059	57,209
Other non-current liabilities	149	143	143	143	143	143	143	143
Total non-current liabilities	20,821	33,953	45,134	56,102	65,970	71,476	69,202	57,352
Trade and other payables	1,416	1,014	1,019	3,604	6,142	8,058	10,913	12,071
Current loans and borrowings	265	323	323	323	323	323	323	323
Other current liabilities	1,658	1,176	1,165	1,165	1,165	1,165	1,165	1,165
Total current liabilities	3,339	2,513	2,507	5,092	7,630	9,546	12,401	13,559
Equity attributable to company	(16,421)	(29,310)	(39,425)	(48,474)	(56,151)	(60,037)	(55,518)	(40,662)
Non-controlling interest	0	0	0	0	0	0	0	0
<b>CASH FLOW STATEMENT</b>								
Profit for the year	(17,750)	(13,520)	(10,915)	(9,849)	(8,477)	(4,686)	3,719	14,057
Taxation expenses	(114)	0	0	0	0	0	0	0
Profit before tax	(17,864)	(13,520)	(10,915)	(9,849)	(8,477)	(4,686)	3,719	14,057
Net finance expenses	822	1,739	2,378	3,107	3,874	4,565	4,951	4,791
EBIT	(17,041)	(11,781)	(8,537)	(6,743)	(4,602)	(121)	8,669	18,848
Depreciation and amortisation	5,409	1,327	788	800	800	900	1,000	1,100
Share based payments	0	0	0	0	0	0	0	0
Other adjustments	2,243	(692)	800	800	800	800	800	800
Movements in working capital	(791)	(341)	(1,443)	(1,918)	(2,192)	(1,620)	(2,244)	(3,007)
Cash from operations (CFO)	(10,180)	(11,487)	(8,392)	(7,061)	(5,194)	(40)	8,225	17,741
Capex	(2,168)	(870)	(400)	(800)	(800)	(900)	(1,000)	(1,100)
Acquisitions & disposals net	4	3	0	0	0	0	0	0
Other investing activities	0	0	0	0	0	0	0	0
Cash used in investing activities (CFIA)	(2,164)	(867)	(400)	(800)	(800)	(900)	(1,000)	(1,100)
Net proceeds from issue of shares	23	(72)	0	0	0	0	0	0
Movements in debt	12,487	11,480	11,181	10,967	9,869	5,506	(2,274)	(11,850)
Dividends paid	0	0	0	0	0	0	0	0
Other financing activities	(164)	(23)	(2,378)	(3,107)	(3,874)	(4,565)	(4,951)	(4,791)
Cash from financing activities (CFF)	12,346	11,385	8,803	7,861	5,994	940	(7,225)	(16,641)
Currency translation differences and other	(1)	525	(11)	0	0	0	0	0
Increase/(decrease) in cash and equivalents	0	(444)	0	0	0	0	0	0
Cash and equivalents at end of period	950	506	506	506	506	506	506	506
Net (debt)/cash	(19,560)	(33,201)	(44,382)	(55,350)	(65,219)	(70,724)	(68,450)	(56,600)
Movement in net (debt)/cash over period	(19,560)	(13,641)	(11,181)	(10,967)	(9,869)	(5,506)	2,274	11,850

Source: Orège data, Edison Investment Research. Note: \*FY17 results have been restated by the company and will be updated once the full accounts are made available.

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