

## Momentum gathering with potential for recurring revenue

**DXN Ltd (ASX:DXN) is a vertically integrated prefabricated modular data centre business with manufacturing facilities in Perth and the now open for business data centre, SYD01, at Sydney Olympic Park in Sydney. DXN has announced that it has secured a \$2.4m contract with Southern Cross Cable Ltd for three modular cable landing stations in Pacific Islands of Fiji, Tokelau and Kiribati, with the potential to include connectivity to Samoa (Apia). We expect to see ongoing maintenance evolving from this contract, delivering recurring revenue to DXN Modules. The Southern Cross Cable contract closely follows a contract from existing client satellite operator SES Networks to build a second \$200,000 modular unit for its Papua New Guinea operations. DXN has also just completed a fully-underwritten one for four non-renounceable entitlement offer at \$0.055/share to raise \$5m pre costs. Each share subscribed for will have an attached \$0.10/option with an expiry of ~4 November 2020. Funds will be used to double capacity at SYD-01 to 0.8MW ready for service rack space including ancillary infrastructure, provide working capital to DXN Modules and general working capital. Adjusting to the current entitlements offer, our base case DCF valuation is \$0.21/share.**

### Business model

DXN, formerly The Data Exchange Network, has completed construction of an initial 400kW capacity (1.0MW core supporting infrastructure), pre-fabricated modular co-location data centre in leased premises in Sydney. The company has utilised its established engineering and manufacturing facility in Perth to deliver custom-designed, inhouse data centre infrastructure. The company's strategy is to build capacity in stages starting with 400kW or 58 racks in Sydney then moving quickly to 1MW or 145 racks and gradually installing 6MW or 1,000 racks as demand fills existing infrastructure. This enables DXN to maintain a capital light model compared to traditional DCs which build greater capacity upfront. Revenue will be derived from manufacturing data centre modules for third parties, operating and renting rack space in its co-location data centres and from software licence fees for its monitoring, management and access control system. We forecast operational breakeven in H1FY21 with an expectation of DXN module sales of \$11.5m and \$2.5m in sales from SYD-01.

### Q1 result

DXN reported Q1 FY20 cash receipts of \$0.6m, cash expenditure of \$5.6m, including \$2.69m on property, plant and equipment. Net operating cash outflow was \$2.0m. The company expects operating cash outflow in Q2 FY20 to be \$3.37m. This suggests a first half cost base of just under \$6.0m which is lower than our current forecasts which have also factored in more sales than currently visible in H1 FY20. Cash at the end of September was \$1.26m while \$1.18m was drawn on the company's \$5.2m finance facility. The current entitlement offer will position the company for the quarter ahead.

### DCF valuation is \$0.21/share

We have factored in the additional shares being issued in the entitlement offer and have assumed in our valuation that the options are fully exercised in 12 months' time. This delivers a DCF valuation of \$0.21/share (previously \$0.24/share) fully diluted.

#### Earnings History and Estimates

Year end	Revenue(A\$m)	EBITDA(A\$m)	NPAT (A\$m)	EPS (c)	EV/Sales (x)	EV/EBITDA (x)
06/19a	2.6	(7.0)	(7.4)	(3.50)	10.89	na
06/20e	16.0	(3.2)	(3.1)	(0.66)	2.09	na
06/21e	31.6	2.8	1.0	0.15	1.04	11.70
06/22e	41.7	9.0	4.4	0.66	0.97	4.54

Source: RaaS Advisory Estimates, Company Data

## Data Centres

6<sup>th</sup> November 2019

### Share details

ASX Code	DXN
Share price	\$0.069
Market Capitalisation post entitlements offer	\$36.9M
Shares on issue post entitlements offer	451.8M
Enterprise value post entitlement offer	\$31.5M
Net cash at post raise	~\$5.4M
Free float	~58%

### Share performance (12 months)



### Upside Case

- Edge Infrastructure and Manufacturing facility in Perth assists in early cashflows and has capacity to meet both internal and external customer demand
- Capital light compared to traditional data centre operators as building 1MW at a time
- Modularised and smaller data centres will be critical to 5G mobile and the Internet of Things

### Downside Case

- Small player in a market dominated by global players with deep pockets
- Significant data centre capacity in the market currently
- Growth of mature centres reverts to CPI

### Substantial/Institutional Shareholders

JP Morgan Nominees Australia Pty Ltd (Newgate Capital Partners) 16.1%, Carason Ward Pte Ltd (Dean Coetzee and Tim Desmond) 5.42%, SG Hiscock & Company Limited 9.88%

### Board of Directors

Douglas Loh	Non-Executive Chairman
Richard Carden	Non-Executive Director
Terry Smart	Non-Executive Director
John Duffin	Non-Executive Director
John Baillie	Non-Executive Director
Timothy Desmond	Executive Director

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## Entitlement Offer Details

DXN has just finalised a fully underwritten non-renounceable entitlement issue of one share for every 4 shares held at an issue price of \$0.055/share raising just under \$5.0m (pre costs). The offer included free listed option exercisable at \$0.10 per option one year after the date of issue. The entitlement offer has been fully underwritten by lead manager Pinnacle Corporate Finance with sub underwriting to \$250,000 by non-executive director John Baillie. Assuming the new options are fully exercised in 12 months' time, this will generate another \$5.0m in new capital for the company to utilise for its capex program. Funds raised from the entitlement offer will be used to expand the current 400kW with supporting infrastructure at SYD-01 to 800kW with supporting infrastructure, provide working capital to DXN Modules and general working capital.

## DXN Modules Contract Wins

DXN Modules has been gathering momentum with several contract wins in recent months, particularly in the Pacific region. The company has just signed a \$2.4m three modular cable landing station deal with Southern Cross Cable Ltd which will see deployment in Fiji (Savusavu), Kiribati and Tokelau, with Samoa (Apia) as an additional option. The cable landing stations will be part of the critical international data connectivity between the Pacific Island nations and Sydney, Auckland and Los Angeles. We expect to see ongoing maintenance evolve from this contract, delivering recurring revenue to the DXN Modules division. The Southern Cross contract closely follows a second \$200,000 contract win from existing client SES Networks for a modular communications unit for its Papua New Guinea operations and the recently deployed cable landing stations for the Matanua Cable Consortium in the Cook Islands.

## Company update

DXN's CEO Matthew Madden provided an update with the company's quarterly result, noting that in the 10 weeks since he took the helm, the company had achieved several milestones including:

- SYD-01 Data Centre securing Tier III accreditation from the Uptime Institute (making it the first Tier III containerised modular data centre);
- Commissioning and official launch of the SYD-01 Data Centre;
- Successful completion of factory acceptance testing (FAT) of the Niue Prefabricated Cable Landing Station which has now been shipped to site and currently being commissioned;
- Successful FAT completion of two Cook Islands Cable Landing stations shipped to site;
- Contract award SES modular satellite earth station for PNG;
- Production commenced on Radlink radio container modules;
- Appointment of Greg Blenkiron as CFO. Greg joined DXN from LeasePLUS Group where he was CFO; previously he held senior roles including CFO and CEO of manufacturer and importer Tilling Timber and Group Financial Controller of Fleet Partners (now listed on the ASX as Eclix);
- Investor Portal Launched <https://dxnlimited.investorportal.com.au/>

Mr Madden also noted that the unweighted sales pipeline for DXN Modules had now increased to \$300m from \$200m with increased demand being experienced from the market. DXN Modules is well positioned to secure additional market share in the Asia Pacific region following the bankruptcy of its Swedish competitor Flexenclosure. The company has flagged that it expects to close several contracts before the end of November. We are forecasting \$13.85m in sales from DXN Modules in FY20.

## DCF of \$0.21/share fully diluted

We have used the discounted cashflow methodology to value DXN, applying a WACC of 12.1%, beta of 1.9, terminal growth rate of 2.2% and target gearing of 10%, to our base case free cashflows. This derives a valuation of \$0.21 per share, fully diluted for all the equity raisings and options conversions that we have incorporated in our model. We have not incorporated the out of the money 39.3m \$0.30 options currently on issue as we do not expect these to be exercised. These have expiry dates of 30/11/20 and 5/4/21. Given where the current share price is and the per share prices we have set in our model for future raisings, it is our view that these will lapse.

We set out the DCF valuation in the following exhibit. Due to the ongoing capital expenditure required to build the data centres, the bulk of the present value rests in the terminal value. We have included in the valuation all current and anticipated capital raises in our forecasts and the impact of additional future share issues on the share count.

<b>Exhibit 1: DCF valuation</b>	
	<b>Parameters</b>
Discount rate (WACC)	12.1%
Terminal Growth Rate	2.2%
Beta	1.9
Target gearing	10.0%
Present value of free cashflows inc terminal value	100.0
Add net cash inc all capital raises	40.6
Equity value	140.6
Fully diluted shares (inc current raise, options conversion and an additional \$5.9m raise in FY21)	668.4
Equity value per share	\$ 0.21
Source: RaaS estimates	

**Exhibit 2: Financial Summary**

DXN Ltd						Share price (5th November 2019)						A\$	0.069				
Profit and Loss (A\$m)						Interim (A\$m)						H119F	H219F	H120F	H220F	H121F	H221F
Y/E 30 June	FY18A	FY19A	FY20F	FY21F	FY22F	Revenue	2.5	0.1	5.2	10.8	14.3	17.3					
						EBITDA	(2.7)	(4.2)	(2.7)	(0.5)	0.8	2.0					
						EBIT	(2.8)	(4.5)	(3.3)	(1.1)	0.2	1.0					
Revenue	2.0	2.6	16.0	31.6	41.7	NPAT (normalised)	(2.7)	(4.5)	(2.4)	(0.7)	0.2	0.8					
EBITDA	(4.0)	(7.0)	(3.2)	2.8	9.0	Minorities	0.0	0.0	0.0	0.0	0.0	0.0					
Deprn	(0.0)	(0.2)	(1.1)	(1.5)	(2.6)	NPAT (reported)	(2.7)	(4.6)	(2.4)	(0.7)	0.2	0.8					
Amort	(1.7)	(0.0)	(0.1)	(0.1)	(0.0)	EPS (normalised)	(1.6)	(1.3)	(0.5)	(0.1)	0.0	0.1					
EBIT	(5.7)	(7.2)	(4.4)	1.2	6.3	EPS (reported)	(1.6)	(1.3)	(0.5)	(0.1)	0.0	0.1					
Interest	0.0	0.0	(0.0)	0.1	0.0	Dividend (cps)	0.0	0.0	0.0	0.0	0.0	0.0					
Tax	0.0	0.0	1.3	(0.4)	(1.9)	Imputation	30.0	30.0	30.0	30.0	30.0	30.0					
Minorities	0.0	0.0	0.0	0.0	0.0	Operating cash flow	(4.3)	(2.5)	(1.6)	(0.7)	0.1	1.5					
Equity accounted assoc	0.0	0.0	0.0	0.0	0.0	Free Cash flow	(4.4)	(2.6)	(1.7)	(0.9)	(0.1)	1.2					
NPAT pre significant items	(5.7)	(7.4)	(3.1)	1.0	4.4	<b>Divisions</b>	<b>H119F</b>	<b>H219F</b>	<b>H120F</b>	<b>H220F</b>	<b>H121F</b>	<b>H221F</b>					
Significant items	0.0	0.0	0.0	0.0	0.0	Port Melbourne	0.0	0.0	0.2	0.3	0.3	0.0					
<b>NPAT (reported)</b>	<b>(5.7)</b>	<b>(7.4)</b>	<b>(3.1)</b>	<b>1.0</b>	<b>4.4</b>	Homebush	0.0	0.0	0.4	1.2	2.5	3.1					
<b>Cash flow (A\$m)</b>						Edge Infrastructure	1.3	0.1	4.6	9.2	11.5	14.0					
Y/E 30 June	FY18A	FY19A	FY20F	FY21F	FY22F	Software sales	0.0	0.0	0.0	0.0	0.1	0.1					
EBITDA	(4.0)	(7.0)	(3.2)	2.8	9.0	Other income	1.2	0.0	0.0	0.0	0.0	0.0					
Interest	0.0	0.0	(0.0)	0.1	0.0	Total Revenue	2.5	0.1	5.2	10.8	14.3	17.3					
Tax	0.0	0.0	0.0	(0.4)	(1.9)	COGS	2.3	1.1	3.9	7.0	8.8	10.6					
Working capital changes	(1.0)	0.1	0.9	(1.0)	(1.2)	Gross Profit	0.3	(0.9)	1.2	3.8	5.5	6.7					
Operating cash flow	(5.0)	(6.9)	(2.3)	1.5	5.8	Employment costs	1.0	1.8	1.9	2.1	2.5	2.5					
Mtce capex	0.0	0.0	(0.3)	(0.4)	(0.7)	Other operating costs	0.5	0.7	0.6	0.8	0.8	0.8					
Free cash flow	(5.0)	(6.9)	(2.6)	1.1	5.2	Corporate overheads	1.4	1.4	1.4	1.4	1.4	1.5					
Growth capex	(0.5)	(10.4)	(2.6)	(7.8)	(17.0)	Total Operating Costs	3.0	3.9	4.0	4.3	4.7	4.8					
Acquisitions/Disposals	0.0	0.0	0.0	0.0	0.0	EBITDA	(2.7)	(4.8)	(2.8)	(0.5)	0.8	2.0					
Other	(1.1)	(2.0)	0.0	0.0	0.0	Capex required	4.1	0.0	0.0	2.6	5.2	2.6					
Cash flow pre financing	(6.6)	(19.3)	(5.2)	(6.7)	(11.8)	Margins, Leverage, Returns		<b>FY18A</b>	<b>FY19A</b>	<b>FY20F</b>	<b>FY21F</b>	<b>FY22F</b>					
Equity	16.0	10.3	12.6	10.1	4.1	EBITDA		n/a	(264.2%)	(20.2%)	8.9%	21.5%					
Debt	4.4	(0.7)	0.0	0.0	6.8	EBIT		n/a	(274.1%)	(27.6%)	3.8%	15.0%					
Dividends paid	0.0	0.0	0.0	0.0	0.0	NPAT pre significant items		n/a	(279.2%)	(19.3%)	3.0%	10.5%					
Net cash flow for year	13.7	(9.6)	7.4	3.4	(0.9)	Net Debt (Cash)			12.0	2.4	9.8	13.2	5.5				
<b>Balance sheet (A\$m)</b>						Net debt/EBITDA (x)	(x)	n/a	n/a	n/a	4.704	0.617					
Y/E 30 June	FY18A	FY19A	FY20F	FY21F	FY22F	ND/ND+Equity (%)	(%)	n/a	(16.6%)	(59.2%)	(54.6%)	(13.7%)					
Cash	12.0	5.4	12.8	16.2	15.3	EBIT interest cover (x)	(x)	n/a	n/a	n/a	0.1	0.0					
Accounts receivable	1.2	1.0	2.6	5.2	6.9	ROA		n/a	(38.2%)	(15.6%)	3.0%	11.3%					
Inventory	0.2	1.0	0.8	1.3	1.6	ROE			(46.7%)	(14.3%)	3.0%	10.5%					
Other current assets	0.7	0.4	0.4	0.4	0.4	ROIC		0.0%	(32.1%)	(30.5%)	3.6%	18.4%					
<b>Total current assets</b>	<b>14.2</b>	<b>7.8</b>	<b>16.6</b>	<b>23.2</b>	<b>24.2</b>	<b>NTA (per share)</b>		0.08	0.04	0.04	0.06	0.07					
PPE	0.4	11.1	13.0	19.7	34.6	<b>Working capital</b>		0.6	0.9	1.6	3.4	4.7					
Goodwill	0.0	0.0	0.0	0.0	0.0	<b>WC/Sales (%)</b>		<b>27.8%</b>	<b>33.4%</b>	<b>10.0%</b>	<b>10.7%</b>	<b>11.2%</b>					
Investments	0.0	0.0	0.0	0.0	0.0	<b>Revenue growth</b>		n/a	31.1%	505.2%	97.6%	32.1%					
Deferred tax asset	0.0	0.0	1.3	1.3	1.3	<b>EBIT growth pa</b>		n/a	n/a	n/a	(127.5%)	415.2%					
Other assets	1.1	3.4	3.3	3.2	3.2	<b>Pricing</b>		<b>FY18A</b>	<b>FY19A</b>	<b>FY20F</b>	<b>FY21F</b>	<b>FY22F</b>					
<b>Total non current assets</b>	<b>1.4</b>	<b>14.5</b>	<b>17.5</b>	<b>24.2</b>	<b>39.1</b>	No of shares (y/e)	(m)		194	452	625	668	668				
<b>Total Assets</b>	<b>15.6</b>	<b>22.3</b>	<b>34.2</b>	<b>47.4</b>	<b>63.3</b>	Weighted Av Dil Shares	(m)		98	211	618	721	751				
Accounts payable	0.9	1.2	1.8	3.2	3.8	EPS Reported	cps		(5.86)	(3.50)	(0.66)	0.15	0.66				
Short term debt	0.0	0.9	0.9	0.9	0.9	EPS Normalised/Diluted	cps		(5.86)	(3.41)	(0.66)	0.15	0.66				
Tax payable	0.0	0.0	0.0	0.0	0.0	EPS growth (norm/dil)			n/a	n/a	n/a	-123%	339%				
Other current liabilities	0.1	1.3	3.0	3.8	3.8	DPS	cps		-	-	-	-	-				
<b>Total current liabilities</b>	<b>1.0</b>	<b>3.4</b>	<b>5.7</b>	<b>7.8</b>	<b>8.5</b>	DPS Growth			n/a	n/a	n/a	n/a	n/a				
Long term debt	0.0	2.1	2.1	2.1	8.9	Dividend yield			0.0%	0.0%	0.0%	0.0%	0.0%				
Other non current liabs	0.0	0.0	0.0	0.0	0.0	Dividend imputation			30	30	30	30	30				
<b>Total long term liabilities</b>	<b>0.0</b>	<b>2.1</b>	<b>2.1</b>	<b>2.1</b>	<b>8.9</b>	PE (x)			-	-	-	46.0	10.5				
<b>Total Liabilities</b>	<b>1.0</b>	<b>5.5</b>	<b>7.8</b>	<b>9.9</b>	<b>17.4</b>	PE market			15.2	15.2	15.2	15.2	15.2				
<b>Net Assets</b>	<b>14.7</b>	<b>16.9</b>	<b>26.4</b>	<b>37.4</b>	<b>45.9</b>	Premium/(discount)			(100.0%)	(100.0%)	202.6%	(31.0%)					
Share capital	20.1	29.7	42.3	52.4	56.5	EV/EBITDA			(0.3)	(4.1)	(10.3)	11.7	4.5				
Accumulated profits/losses	(5.7)	(13.1)	(16.2)	(15.2)	(10.9)	FCF/Share	cps		(2.6)	(1.5)	(0.3)	0.3	1.0				
Reserves	0.3	0.3	0.3	0.3	0.3	Price/FCF share			(2.7)	(4.5)	(21.7)	23.8	7.1				
Minorities	0.0	0.0	0.0	0.0	0.0	Free Cash flow Yield			(37.6%)	(22.0%)	(4.6%)	4.2%	14.1%				
<b>Total Shareholder funds</b>	<b>14.7</b>	<b>16.9</b>	<b>26.4</b>	<b>37.4</b>	<b>45.9</b>												

Source: RaaS Advisory



# FINANCIAL SERVICES GUIDE

**RaaS Advisory Pty Ltd**

**ABN 99 614 783 363**

**Corporate Authorised Representative, number 1248415**

**of**

**BR SECURITIES AUSTRALIA PTY LTD**

**ABN 92 168 734 530**

**AFSL 456663**

**Effective Date: 26<sup>th</sup> November 2018**

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- how we transact with you
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