Tox Free Solutions

Blackswan Equities

Ready for takeoff

Buy

26 February 2010

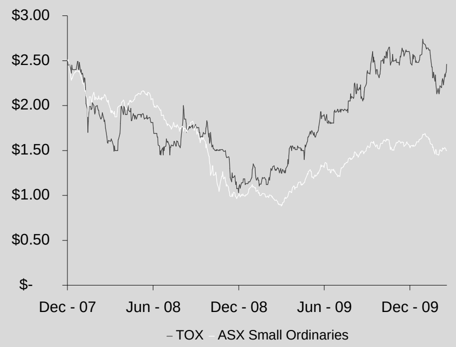
Company Information

Code	TOX
Last Price	$2.37
12 Month Price Target	$2.82
Total Shareholder Return	19.1%
Valuation	$2.57 - 2.82
Shares on Issue	90.4m
Market Capitalisation	$214.2m
Monthly Turnover (12 month average)	$5.7m

Financial Summary

	FY08a	FY09a	FY10e	FY11e
Revenue ($m)	34	88	107	129
EBITDA ($m)	13.6	22.3	27.0	33.3
D&A ($m)	2.8	7.6	9.0	9.7
EBIT ($m)	10.8	14.8	18.0	23.6
Net Interest ($m)	1.2	3.5	2.6	1.5
Income Tax ($m)	3.2	3.0	4.6	6.6
Reported NPAT ($m)	**6.4**	**7.6**	**10.8**	**15.5**
Adjusted NPAT ($m)	**6.4**	**8.3**	**10.8**	**15.5**
EPS (¢)	9.2	10.6	12.1	16.4
EPS growth (%)	172.1	16.2	14.2	35.0
CFPS (¢)	9.6	12.3	18.3	22.5
DPS (¢)	0.0	0.0	0.0	0.0
Yield (%)	0.0	0.0	0.0	0.0
Net debt ($m)	16.9	32.9	12.0	-1.5
Net debt / equity (%)	51.0	61.1	13.5	net cash
Interest cover (x)	8.6	4.2	6.9	16.0
ROE (%)	22.1	19.0	15.1	16.0
ROA (%)	22.9	19.3	17.2	20.6
ROFE (%)	25.9	21.6	19.2	23.1
NTA per share	18.7	42.5	77.7	93.8
PE (x)	25.9	22.3	19.5	14.5
EV/EBITA (x)	21.7	16.9	12.7	9.1

Share Price Performance



Analyst Details
Rob Martino
+618 9346 0317
Rmartino@blackswanequities.com.au

Source: Blackswan Equities, TOX, IRESS.

Event

- TOX reported 1H10 earnings.
- We have downgraded FY10 and FY11 EPS by 3.7% and 2.8% due to revised interest expense.

Analysis

- **Defensive revenue streams maintained.** 1H10 EBITA of $7.1m was up 19.6% on pcp and revenue of $46.9m was up 12.9% on pcp. The result was significantly driven by strong hazardous and solid waste contributions, relative to both 1H09 and 2H09.
- 1H10 gearing (net debt/equity) of 10.0% was down from FY09 of 61.1%, supported by the $25m capital raising and relatively low capex of $6.1m. 1H10 earnings to cash conversion measured by EBITDA to un-geared pre-tax cash flow was strong at 88.9%.
- **A prime beneficiary of WA's oil and gas activity.** TOX maintains a dominant market position in the North West WA region with strategically located assets boasting relatively low competition and high barriers to entry, relationships with key project proponents (Chevron, Woodside, Rio), and significant technical experience.
- TOX remains a prime beneficiary of Western Australia's oil and gas and mineral development activities. We acknowledge the potential for increased competition and believe this is partially mitigated by land availability, government approval processes, and TOX's existing contracts.
- **Organic and acquisitive opportunities on the horizon.** We are forecasting a FY11 net cash position of $1.5m, supported by the recent ~$25m equity raising and contributions from recent contract wins (Gorgon, Rio, Woodside).
- We anticipate TOX will continue to assess organic and acquisitive opportunities in key mineral and oil and gas geographies where it does not have a presence including QLD and NT.

Recommendation and Price Target

- **Buy recommendation maintained.** We are attracted to TOX's defensive revenue streams, strategic assets and relationships, strong core market outlooks, and organic and acquisitive growth opportunities.
- **$2.82 Price Target.** Our price target is based on a mid-cycle EV/EBITA multiple of 10.25x, and our mid-cycle EBITA assumption of $24.2m. Our price target does not include the potential for further contract wins currently tendered and acquisitive and organic growth opportunities.
- Key price catalysts include the award of new waste management and increased scope of existing contracts. We believe there is continued upside risks to our earnings forecasts associated with these near-term price catalysts.

Defensive revenue stream maintained

- We have detailed TOX's 1H10 earnings result in Table 1 below.

Table 1. 1H10 earnings summary

	1H09a	2H09a	FY09a	1H10a	2H10e	FY10e	Variance on pcp
Sales Revenue	$41.4m	$46.6m	$88.0m	$46.7m	$60.4m	$107.1m	12.9%
EBITDA	$10.0m	$12.3m	$22.3m	$11.5m	$15.5m	$27.0m	15.0%
Depreciation	$4.0m	$3.5m	$7.6m	$4.4m	$4.6m	$9.0m	8.3%
EBITA	**$6.0m**	**$8.8m**	**$14.8m**	**$7.1m**	**$10.9m**	**$18.0m**	**19.6%**
Amortisation	$0.0m	$0.0m	$0.0m	$0.0m	$0.0m	$0.0m	n/a
EBIT	**$6.0m**	**$8.8m**	**$14.8m**	**$7.1m**	**$10.9m**	**$18.0m**	**19.6%**
EBIT Margin	14.4%	18.9%	16.8%	15.3%	18.0%	16.8%	
Net interest expense	$2.0m	$1.6m	$3.5m	$1.3m	$1.3m	$2.6m	-30.8%
Profit before tax	$4.0m	$7.2m	$11.2m	$5.8m	$9.6m	$15.4m	44.0%
Income tax expense	$1.2m	$1.8m	$3.0m	$1.7m	$2.9m	$4.6m	44.5%
Underlying NPAT	**$2.8m**	**$5.5m**	**$8.3m**	**$4.0m**	**$6.7m**	**$10.8m**	**43.9%**
Underlying NPAT Margin	*6.8%*	*11.7%*	*9.4%*	*8.7%*	*11.2%*	*10.1%*	
Abnormal Items	$0.0m	($0.6m)	($0.6m)	$0.0m	$0.0m	$0.0m	n/a
Minorities	$0.0m	$0.0m	$0.0m	$0.0m	$0.0m	$0.0m	n/a
Reported NPAT	$2.8m	$4.8m	$7.6m	$4.0m	$6.7m	$10.8m	43.9%
Underlying EPS	**3.8c**	**6.7c**	**10.6c**	**4.8c**	**7.2c**	**12.1c**	**27.1%**
Underlying EPS growth	*-15.1%*	*39.3%*	*16.2%*	*27.1%*	*7.4%*	*14.2%*	
Gross CFPS	6.8c	9.0c	15.8c	8.4c	11.4c	19.8c	22.9%

Source: Blackswan Equities Research, TOX.

- 1H10 EBITA of $7.1m was up 19.6% on pcp and revenue of $46.9m was up 12.9% on pcp. The result was significantly driven by strong hazardous and solid waste contributions, relative to both 1H09 and 2H09.
- The group 1H10 EBITA margin of 15.3% was up on pcp of 14.4%, with the pcp impacted by cost-input issues in the Hazardous division which we believe are now resolved. We note the group 1H10 margin was down on 2H09 of 18.9% due to a ramp-up in BDM, project, and contract management staff costs of recently awarded contracts (Gorgon, RIO, WPL).
- TOX reported 1H10 net debt of $8.3m down from $32.9m at FY09, representing 1H10 gearing (net debt/equity) of 10.0% down from FY09 of 61.1%. The balance sheet was supported by a $25m capital raising and relatively low capex of $6.1m.
- We are forecasting FY10 gearing of 12.0% due to increased 2H capex of ~$14m substantially associated with the recent Gorgon (~$6m) and RIO ($3.5m) contracts. 1H10 earnings to cash conversion measured by EBITDA to un-geared pre-tax cash flow was strong at 88.9%.

Earnings ready for takeoff

- We are forecasting FY10 EBITA of $18.0m up 22.2% on pcp and revenue of $107.1m up 21.7% on pcp. Management expectations of a 1H:2H earnings skew of 40:60% are in line with our forecasts (EBITA level).

- The 2H result will be partially driven by initial contributions from the RIO contract (annualised value ~$7.5-8m) which commences in March 2010. Further we anticipate significant 2H growth due to the ramp up on the recently awarded Gorgon contract and continued realisation of operational efficiencies from the Barry Bros. acquisition.
- We are forecasting a 2H group EBITA margin of 18.0% up from 1H of 15.3%. We anticipate the 2H margin will partially benefit from fixed cost leverage and relatively stable BDM, project and contract management staff costs.
- FY11 earnings will be significantly driven by ramp-up in the RIO and Gorgon contracts. Management noted TOX is currently tendering on four waste management and industrial services contracts which would provide further support to our FY11 forecasts.
- We anticipate TOX will also continue to assess organic and acquisitive opportunities in key mineral and oil and gas geographies where it does not have a presence including QLD and NT.

Valuation $2.57- 2.82, Price Target $2.82

- We have detailed the trading multiples of companies leveraged to similar Australian oil and gas and industrial related activity, similar as TOX.

Fig 1. Peer Group Valuations

Code	FY11e EV/EBITA	FY11e P/E	FY11e gearing (net debt/equity)	FY11e EPS Growth	FY11e Yield
CLO	7.8x	11.7x	net cash	14.1%	3.0%
MND	9.9x	16.0	net cash	0.7%	5.8
MRM	10.4x	14.3x	51.0%	1.5%	3.2%
Average	**9.3x**	**14.0x**	**5.4%**	**5.4%**	**4.0%**
TOX	9.1x	14.5x	net cash	35.0%	0.0%

Source: Blackswan Equities Research.

- We have selected an EV/EBITA valuation multiple range of 9.25 – 10.25x, reflecting TOX's defensive revenue streams, strategic assets and relationships and strong core market outlook. Our valuation is based on a mid-term EBITA (FY11-FY12) adequately reflecting: 1) the integration of Barry Bros. and its associated forecast earnings upside; 2) the full impact of recent contract wins (RIO, Gorgon), and 3) the return on recent capex associated with contract wins.

Fig 2. Valuation $2.57 – 2.82

	Low	High
Mid term EBITA ($m)	**24.2**	**24.2**
EV/EBITA multiple (x)	9.25	10.25
Total ($m)	223.7	247.9
Valuation per share		
Net debt adjustment ($m)	-11.6	-11.6
Option exercise adjustment ($m)	10.4	10.4
Company Valuation ($m)	**245.8**	**269.9**
Fully diluted shares on issue (m)	95.7	95.7
Value per share	**$2.57**	**$2.82**

Source: Blackswan Equities Research.

- Key price catalysts include the award of new waste management contracts and increased scope of existing contracts, including Chevron's Gorgon, Apache's Devil Creek, and Woodside's Pluto. We believe there is upside risks to our earnings forecasts associated with these potential contract opportunities.

Tox Free Solutions	
Shares on Issue	90.1m
Market Capitalisation	$213.5m
Year End	30-June

Recommendation	BUY
Date	26-Feb-10
Share Price	$2.37
12 month Target Price	$2.82

Profit and Loss

Full Year Summary ($m)	2008a	2009a	2010e	2011e
Sales Revenue	33.5	88.0	107.1	129.4
EBITDA	13.6	22.3	27.0	33.3
Depreciation & Amortisation	2.8	7.6	9.0	9.7
EBIT	**10.8**	**14.8**	**18.0**	**23.6**
Net Interest Expense	1.2	3.5	2.6	1.5
Profit Before Tax	9.5	11.2	15.4	22.1
Income Tax Expense	3.2	3.0	4.6	6.6
Net Profit after Tax	**6.4**	**8.3**	**10.8**	**15.5**
Minority Interests	0.0	0.0	0.0	0.0
Abnormal Items	0.0	-0.6	0.0	0.0
Reported NPAT	**6.4**	**7.6**	**10.8**	**15.5**
Adjusted NPAT	**6.4**	**8.3**	**10.8**	**15.5**

Half Year Summary ($m)	1H09a	2H09a	1H10a	2H10e
Sales Revenue	41.4	46.6	46.7	60.4
EBITDA	10.0	12.3	11.5	15.5
Depreciation & Amortisation	4.0	3.5	4.4	4.6
EBIT	**6.0**	**8.8**	**7.1**	**10.9**
Net Interest Expense	2.0	1.6	1.3	1.3
Profit Before Tax	4.0	7.2	5.8	9.6
Income Tax Expense	1.2	1.8	1.7	2.9
Net Profit after Tax	**2.8**	**5.5**	**4.0**	**6.7**
Minority Interests	0.0	0.0	0.0	0.0
Abnormal Items	0.0	-0.6	0.0	0.0
Reported NPAT	**2.8**	**4.8**	**4.0**	**6.7**
Adjusted NPAT	**2.8**	**5.5**	**4.0**	**6.7**

Valuation, Price Target, 12 Month Return

Valuation per share	Low	High
Mid Cycle EBITA	24.2	24.2
EV/EBITA Multiple	9.25	10.25
Total	**223.7**	**247.9**
Net debt adjustment	-11.6	-11.6
Option exercise adjustment	10.4	10.4
Enterprise Value	**245.8**	**269.9**
Fully diluted shares on issue	95.7	95.7
Valuation range per share	**$2.57**	**$2.82**

12 Month Price Target	
Based on an 10.25x mid-cycle EV/EBITA multiple	$ 2.82

12 month return	
Capital Return	19.1%
Dividend Yield	0.0%
12 month total return	**19.1%**

FY10 Peer Group Comparison

Code	P/E	EV/EBITA	EPS Growth	Gearing (Net debt/equity)
CLO	11.7x	7.8x	14.1%	-43.1%
MND	16.0x	9.9x	0.7%	-100.6%
MRM	14.3x	10.4x	1.5%	51.0%
Average	**14.0x**	**9.4x**	**5.4%**	**-30.9%**
TOX	**14.5x**	**9.1x**	**35.0%**	**-1.5%**

Source: Blackswan Equities Research, Consensus

Cash Flow

Full Year Summary ($m)	2008a	2009a	2010e	2011e
Profit Before Tax	**9.5**	**11.2**	**15.4**	**22.1**
Depreciation and Amortisation	2.8	7.6	9.0	9.7
Income Tax Paid	-2.6	-5.1	-3.0	-4.6
Inc/(Dec) in Working Capital	-3.3	-9.4	-3.1	-3.7
Other Items	0.4	5.5	-1.7	-2.0
Operating Cash Flow	**6.8**	**9.8**	**16.6**	**21.5**
Capital Expenditure (incl. HP lease)	-9.6	-9.7	-20.0	-8.0
Acquisitions	-6.8	-10.4	0.0	0.0
Asset Sales	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0
Investing cash flow	**-16.4**	**-20.2**	**-20.0**	**-8.0**
Equity Raised	0.3	12.6	24.3	0.0
Dividends Paid	0.0	0.0	0.0	0.0
Inc/(Dec) in Borrowings	6.7	0.7	-7.0	-7.5
Other Items	0.0	0.0	0.0	0.0
Financing Cash Flow	**7.0**	**13.3**	**17.3**	**-7.5**
Movement in net cash	**-2.6**	**3.0**	**13.9**	**6.0**

Free Cash Flow ($m)	2008a	2009a	2010e	2011e
EBITDA	13.6	22.3	27.0	33.3
Depreciation & Amortisation	2.8	7.6	9.0	9.7
EBIT	10.8	14.8	18.0	23.6
NPAT	6.4	8.3	10.8	15.5
Capital Expenditure (incl. HP lease)	-9.6	-9.7	-20.0	-8.0
Free Cash Flow	**-0.4**	**6.1**	**-0.2**	**17.2**

Balance Sheet

Full Year Summary ($m)	2008a	2009a	2010e	2011e
Cash	1.6	4.6	18.5	24.5
Debtors	8.6	22.1	26.9	32.5
Inventory	0.1	0.1	0.2	0.2
PP&E	23.4	46.7	57.6	55.9
Investments	0.0	0.0	0.0	0.0
Intangibles	23.3	25.0	25.0	25.0
Other	0.5	2.8	2.8	2.8
Total Assets	**57.5**	**101.3**	**131.0**	**140.9**
Creditors	3.6	7.7	9.4	11.4
Current Debt	1.9	3.6	3.6	3.6
Non Current Debt	16.6	33.9	26.9	19.4
Other	2.3	2.2	2.2	2.2
Total Liabilities	**24.4**	**47.4**	**42.1**	**36.6**
Shareholders' Equity	29.3	42.0	66.3	66.3
Minorities	0.0	0.0	0.0	0.0
Other	3.8	11.8	22.6	38.1
Total Shareholders' Equity	**33.1**	**53.9**	**88.9**	**104.4**

Ratios

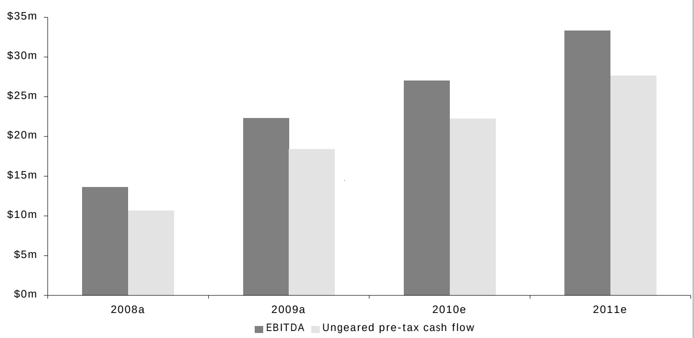
Earnings	2008a	2009a	2010e	2011e
Revenue Growth	67.6%	162.3%	21.7%	20.9%
EBIT Growth	48.9%	36.9%	22.2%	30.8%
EBITDA / sales	40.6%	25.4%	25.2%	25.7%
EBIT / sales	32.1%	16.8%	16.8%	18.2%
EPS	9.2¢	10.6¢	12.1¢	16.4¢
EPS growth	172.1%	16.2%	14.2%	35.0%
CFPS	9.6¢	12.3¢	18.3¢	22.5¢

Balance Sheet	2008a	2009a	2010e	2011e
Net debt / (cash)	$16.9m	$32.9m	$12.0m	-$1.5m
Gearing (net debt / equity)	51.0%	61.1%	13.5%	net cash
EBITA interest cover	8.6x	4.2x	6.9x	16.0x
Return on equity	22.1%	19.0%	15.1%	16.0%
Return on assets	22.9%	19.3%	17.2%	20.6%
Return on funds employed	25.9%	21.6%	19.2%	23.1%
NTA per share	$0.19	$0.43	$0.78	$0.94
EFPOWA	71.6m	79.1m	90.5m	95.7m

Valuation	2008a	2009a	2010e	2011e
P/E	25.9x	22.3x	19.5x	14.5x
EV/EBIT	21.7x	16.9x	12.7x	9.1x
EV/EBITDA	17.9x	11.6x	8.8x	6.8x

Dividends	2008a	2009a	2010e	2011e
Dividend per share	0.0¢	0.0¢	0.0¢	0.0¢
Dividend yield	0.0%	0.0%	0.0%	0.0%
Dividend franking	0%	0%	0%	0%
Dividend payout ratio	0.0%	0.0%	0.0%	0.0%

EBITDA to cash flow conversion



Sales		**Email**	**Telephone**
Michael Bartley	Dealers' Assistant	mbartley@blackswanequities.com.au	+61 8 9346 0352
Brian Bates	Head of Retail Desk	bbates@blackswanequities.com.au	+61 8 9346 0314
Paul Berson	Senior Investment Advisor	pberson@blackswanequities.com.au	+61 8 9346 0328
Michael Bowden	Senior Investment Advisor	mbowden@blackswanequities.com.au	+61 8 9346 0307
Paul Cooper	Investment Adviser	pcooper@blackswanequities.com.au	+61 8 9346 0316
Nick Dempster	Senior Investment Advisor	ndempster@blackswanequities.com.au	+61 8 9346 0357
Ana Gomes	Dealers' Assistant	agomes@blackswanequities.com.au	+61 8 9346 0343
Phil Grant	Senior Investment Advisor	pgrant@blackswanequities.com.au	+61 8 9346 0306
Tony Kenny	Director - Senior Investment Advisor	tkenny@blackswanequities.com.au	+61 8 9346 0302
Guy Lyons	Institutional Investment Advisor	glyons@blackswanequities.com.au	+61 8 9346 0331
Simon Lyons	Chief Executive Officer	slyons@blackswanequities.com.au	+61 8 9346 0304
Tim Lyons	Executive Chairman	tlyons@blackswanequities.com.au	+61 8 9346 0324
Jamie Mann	Senior Investment Advisor	jmann@blackswanequities.com.au	+61 8 9346 0301
Elise Ntoumenopoulos	Dealers' Assistant	entoumenopoulos@blackswanequities.com.au	+61 8 9346 0330
Rob Pass	Investment Advisor / Sales Trader	rpass@blackswanequities.com.au	+61 8 9346 0370
Jessica Ridley	Dealers' Assistant	jridley@blackswanequities.com.au	+61 8 9346 0313
Tim Weir	Senior Investment Advisor	tweir@blackswanequities.com.au	+61 8 9346 0303
Steve Wood	Director - Senior Investment Advisor	swood@blackswanequities.com.au	+61 8 9346 0305

Research		**Email**	**Telephone**
Tony Lofthouse	Research Analyst - Resources	tlofthouse@blackswanequities.com.au	+61 8 9346 0315
Rob Martino	Research Analyst - Industrials	rmartino@blackswanequities.com.au	+61 8 9346 0317
Mark Savich	Research Analyst - Resources	msavich@blackswanequities.com.au	+61 8 9346 0320

Corporate		**Email**	**Telephone**
Alex Eastwood	Senior Advisor - Corporate	aeastwood@blackswanequities.com.au	+61 8 9346 0355
Tom Loh	Senior Advisor - Corporate	tloh@blackswanequities.com.au	+61 8 9346 0353

Administration		**Email**	**Telephone**
Emma Della Bosca	Portfolio Administrator	edellabosca@blackswanrequities.com.au	+61 8 9346 0321
Sandy Entwistle	Administration Assistant	sentwistle@blackswanequities.com.au	+61 8 9346 0338
Karen Kernaghan	Manager - Portfolio Administration	kkernaghan@blackswanequities.com.au	+61 8 9346 0371
Adriana Kostov	Legal and Compliance Manager	akostov@blackswanequities.com.au	+61 8 9346 0327
Jessamyn Lyons	Administration Manager / Account	jlyons@blackswanequities.com.au	+61 8 9346 0308
Deb Meyer	Portfolio Administrator	dmeyer@blackswanequities.com.au	+61 8 9346 0318
Grant Ormerod	Financial Controller	gormerod@blackswanequities.com.au	+61 8 9346 0341
Ellie Peppler	Administration Assistant	epeppler@blackswanequities.com.au	+61 8 9346 0319
Lip Teh	Legal and Compliance Manager	lteh@blackswanequities.com.au	+61 8 9346 0305

Research Disclaimer