

### Key Facts

Company Code	HRL:ASX
Closing Price (04/8/17)	A\$8.5c
Price Target	A\$0.12
Date of Report	07/08/17
Company Website	<a href="http://www.hrlholdings.com">www.hrlholdings.com</a>
Analyst	Warren Jeffries

### Company Statistics

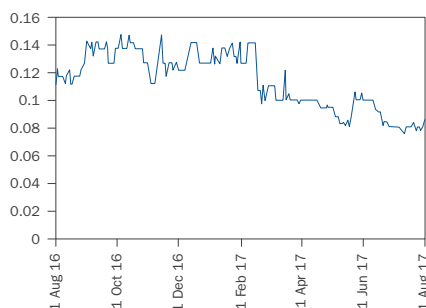
12-Month Range	A\$0.08 - A\$0.16
Market Cap (A\$Mil)	\$20.8m
Issued Shares	244.2m
Issued Options	7.9m
Cash (A\$Mil)	A\$0.7m

### Major Shareholders

	%
Kevin Maloney (Tulla Group)	25.1%
Viburnum Funds Pty Ltd	12.3%
Daren Anderson*	17.7%

\*includes family interests. D Anderson's direct holding 21.2m shares.

### Share Price Performance



Canaccord Colts provide research coverage on a select group of early-stage ASX-listed microcap companies that our institutional research team believes have strong development trajectories.



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**Disclaimer:** Canaccord Genuity (Australia) Limited has received a fee as the Lead Manager to the HRL Holdings capital raising announced on 16 February 2017.

HRL Holdings (HRL.ASX) is an emerging environmental services company, with operations in Australia and New Zealand. HRL was established in 2014 through the acquisition of Octief (Australia) and then soon after Precise Consulting (New Zealand) which both operate within the environmental services industry, and more specifically provide a range of testing and analysis services around hazardous materials. HRL has recently expanded its capabilities through the acquisition of Morrison Geotechnic, who provide geotechnical services in Australia, while also acquiring specialist software provider to the hazardous materials market in Octfolio. Having established capabilities within the hazardous materials and geotechnical industries, HRL is well positioned to leverage its capabilities into new sectors including air & water and agriculture & food.

### Key points

**Mid-market opportunity** – HRL currently operates in ~12% of the broader environmental services market which is estimated at ~\$4bn in Australia. The broader market has a number of larger established participants with global operations, in addition to a long tail of smaller, state based or local operators that lack scale and a vertically integrated solution. The opportunity is there for HRL to establish themselves as a dynamic, mid-market player in both Australia and New Zealand.

**Platform for growth established** – with operations largely established through the acquiring of private companies, HRL has had to also invest in a corporate overhead to support these businesses. To that extent, we believe HRL now has its corporate overhead and platform established, and will be able to leverage earnings from organic and acquisition growth going forward.

**New business wins across the group** – having only recently completed the acquisitions of Morrison and Octfolio, HRL has recently announced that a new 3-year service agreement was secured by Morrison with Queensland Department of Transport & Main Roads, Octfolio was granted approved contractor status with South 32 (ASX: S32) and Octief was awarded a new 6-month contract with the Northern Territory Government.

**Risks** – The key risks to our investment thesis include (i) Acquisition risk - we deem much of HRL's ability to grow its market share and enter new segments will be dependent on further acquisition activity of small, private operators; (ii) Limited history – HRL was effectively established in 2014 through acquisition, and the business remains at an early stage of its evolution; and (iii) Competition which is ever present.

**Catalysts** – Key short term catalysts for the stock include: (i) FY17 result – will provide some confirmation that HRL have been able to bring together multiple businesses and deliver profitable earnings; (ii) New contract wins – reflecting organic growth opportunities for which recent announcement's positively reflect; and (iii) Strong construction and infrastructure market for which HRL has some meaningful exposure now via Morrison.

**Valuation and recommendation** – We initiate coverage on HRL with a Buy recommendation and \$0.12 Target Price. We are mindful that HRL is at an early stage of its evolution, however has established a sound business platform in the environmental and testing services market.

Figure 1: HRL Holdings Limited (HRL) Canaccord Genuity forecasts

Profit & Loss (\$m)					Valuation ratios				
	2016A	2017F	2018F	2019F		2016A	2017F	2018F	2019F
<b>Sales Revenue</b>	<b>8.4</b>	<b>13.5</b>	<b>22.1</b>	<b>23.1</b>	EPS (cps) - underlying	0.2	0.2	0.4	0.5
<b>EBITDA</b>	<b>1.1</b>	<b>1.4</b>	<b>3.2</b>	<b>3.5</b>	EPS (cps) - normalised	0.4	0.4	0.7	0.8
Depreciation	-0.2	-0.4	-0.7	-0.7	PER (x)	23.0	21.6	12.2	10.7
<b>EBITA</b>	<b>0.9</b>	<b>1.1</b>	<b>2.5</b>	<b>2.8</b>	PER Rel - All Ind.	56%	32%	-21%	-27%
Amort - Intangibles	-0.3	-0.5	-1.0	-1.0	PER Rel - Small Ind.	71%	26%	-19%	-20%
EBIT	0.6	0.5	1.5	1.8	Enterprise Value (\$m)	14.5	20.4	18.9	17.0
Net Interest Expense	-0.1	-0.1	-0.0	0.0	EV / EBITDA (x)	13.5	14.4	5.9	4.9
<b>NPBT</b>	<b>0.5</b>	<b>0.5</b>	<b>1.5</b>	<b>1.8</b>	EV / EBIT (x)	24.9	37.9	12.3	9.5
Tax expense	-0.1	-0.1	-0.5	-0.5	DPS (cps)	0.0	0.0	0.0	0.0
OEI	0.0	0.0	0.0	0.0	Dividend Yield (%)	0.0%	0.0%	0.0%	0.0%
NPAT - Pre NRI's	0.4	0.3	1.0	1.3	Franking (%)	100%	100%	100%	100%
<b>NPAT - normalised</b>	<b>0.6</b>	<b>0.7</b>	<b>1.7</b>	<b>1.9</b>	CFPS (cps)	0.1	0.0	0.8	1.0
Significant items	-0.3	-0.2	0.0	0.0	P / CFPS (x)	85.7	298.9	11.2	8.8
<b>NPAT - reported</b>	<b>0.1</b>	<b>0.1</b>	<b>1.0</b>	<b>1.3</b>					
Cash Flow (\$m)					Profitability ratios				
	2016A	2017F	2018F	2019F		2016A	2017F	2018F	2019F
<b>Operating EBITDA</b>	<b>1.1</b>	<b>1.4</b>	<b>3.2</b>	<b>3.5</b>	EBITDA Margin (%)	12.8	10.5	14.5	14.9
- Interest & Tax Paid	0.2	0.6	0.5	0.5	EBITA Margin (%)	10.6	7.9	11.3	11.9
+/- change in Work. Cap.	-0.8	-1.6	-0.8	-0.6	EBIT Margin (%)	7.0	4.0	7.0	7.7
- other	-0.1	-0.8	0.0	0.0	ROE (%)	5.6	2.2	6.3	7.2
<b>Operating Cashflow</b>	<b>0.2</b>	<b>0.1</b>	<b>1.9</b>	<b>2.4</b>	ROA (%)	10.2	6.1	14.6	16.7
- Capex	-0.2	-0.4	-0.4	-0.4	ROIC (%)	19.3	7.0	11.7	13.5
- other	-0.1	0.0	0.0	0.0					
- acquisitions	-1.5	-6.3	0.0	0.0	Balance Sheet ratios				
<b>Free Cashflow</b>	<b>-1.6</b>	<b>-6.6</b>	<b>1.5</b>	<b>2.0</b>	Net Debt (cash)	1.0	-0.4	-1.8	-3.8
- Ord Dividends	0.0	0.0	0.0	0.0	Net Gearing (%)	14.6	cash	cash	cash
- Equity /other	-0.0	8.5	0.0	0.0	Interest Cover (x)	13.9	24.9	96.0	cash
<b>Net Cashflow</b>	<b>-1.7</b>	<b>1.9</b>	<b>1.5</b>	<b>2.0</b>	NTA per share (\$)	0.0	0.0	0.0	0.1
Cash at beginning of period	0.9	0.4	0.7	1.8	Price / NTA (x)	0.0	0.0	0.0	0.0
+/- borrowings / other	1.2	-1.6	-0.4	0.0	Shares on issue	158.9	244.2	244.2	244.2
<b>Cash at end of period</b>	<b>0.4</b>	<b>0.7</b>	<b>1.8</b>	<b>3.8</b>	EFPOWA (m) - fully diluted	158.9	179.4	244.2	244.2
Balance Sheet					Growth ratios				
	2016A	2017F	2018F	2019F		2016A	2017F	2018F	2019F
Cash	0.4	0.7	1.8	3.8	Sales revenue (\$m)	n/a	60.9%	63.6%	4.8%
Inventories	0.0	0.0	0.0	0.0	EBITDA (\$m)	n/a	32.1%	126.2%	8.0%
PP&E	0.7	1.3	1.0	0.7	EBIT (\$m)	n/a	-7.7%	185.6%	16.6%
Debtors	1.4	3.5	4.4	5.0	NPAT (\$m)	n/a	-9.0%	203.4%	23.5%
Intangibles	5.7	10.9	9.9	9.0	EPS (cps)	n/a	6.5%	76.8%	14.2%
Other assets	1.0	1.8	1.8	1.8	DPS (cps)	n/a	100.0%	200.0%	300.0%
<b>Total Assets</b>	<b>9.1</b>	<b>18.2</b>	<b>18.9</b>	<b>20.2</b>	Interim Analysis				
Borrowings	1.4	0.4	-0.0	-0.0		<b>1H16A</b>	<b>2H16A</b>	<b>1H17A</b>	<b>2H17F</b>
Trade Creditors	0.7	0.8	0.9	0.9	Revenues	19.0	-10.7	5.5	8.0
Other Liabilities	0.4	1.7	1.7	1.7	EBITDA	3.1	-2.0	0.4	1.0
<b>Total Liabilities</b>	<b>2.4</b>	<b>2.9</b>	<b>2.5</b>	<b>2.6</b>	EBITDA margin (%)	16.3%	19.2%	6.8%	13.0%
<b>NET ASSETS</b>	<b>6.7</b>	<b>15.4</b>	<b>16.4</b>	<b>17.7</b>	EBIT	2.9	-2.3	0.0	0.5
					NPAT - underlying	1.8	-1.4	-0.0	0.3
					EPS -underlying	1.1	-0.9	-0.0	0.2
					DPS	0.0	0.0	0.0	0.0
Board of Directors / Substantial Shareholders					Valuation				
Name	Shareholding		%						
Kevin Maloney - Non-Executive Chairman	61.2		25.1%		<b>Normalised EBITDA multiple (x)</b>				
Darren Anderson* - Executive Director	43.3		17.7%		EBITDA (\$m)	3.2			
Mark Elliot - Non-Executive Director	3.1		1.3%		Target EBITDA multiple (x)	8.1			
John Taylor - Non-Executive Director	1.7		0.7%		Net Debt (cash) (\$m)	-1.8			
Frederick Kempson - Alternative Non-Executive Director	0.0		0.0%		Implied Valuation	27.7			
					<b>Per Share</b>	<b>\$0.11</b>			
Substantial Shareholders					Target PE Multiple				
	Shareholding		%						
Kevin Maloney (Tulla Group)	61.2		25.1%		EPS (c)	0.7			
Viburnum Funds Pty Ltd	29.9		12.3%		PER Target (x)	13.6			
Darren Anderson*	43.3		17.7%		<b>Per Share</b>	<b>\$0.10</b>			
					Discounted Cash Flow				
					Cost of equity	11.0%	WACC	11.2%	
					Cost of debt	4.8%	Terminal Growth Rate	2.5%	
					Net Debt / Net debt + equity	0.0%	<b>Per Share</b>	<b>\$0.12</b>	

\* Includes family interests. D. Anderson direct holding 21.2m shares

## Company background

HRL Limited is engaged in environmental technical services in Australia and New Zealand, with a focus on hazardous materials and geotechnical testing & analysis.

Formerly known as Hot Rock Limited (ASX: HRL), the Company took a change of strategic direction with the acquisition of Octief in September 2014, followed by the New Zealand based Precise Consulting and Laboratory Ltd ('Precise') in March 2015. The operations of both Octief and Precise provide a range services around hazardous materials which include chemical contamination testing, methamphetamine screening, asbestos assessment & management and occupational hygiene from air quality screening to workplace drug & alcohol testing.

With capabilities around hazardous materials established, HRL recently expanded into geotechnical services through the acquisition of Morrison Geotechnic Holdings Pty Ltd ('Morrison'). Geotechnical services incorporates geotechnical investigations and studies for infrastructure, commercial, industrial and multi-use developments, temporary work design and inspection and construction phase verification.

HRL has also acquired the business of Integrated Holdings Group Pty Ltd (IHG), which is the holding entity of Octfolio Pty Ltd. Octfolio is a specialist software vendor providing an information management solution for asbestos and hazardous materials compliance, and prior to the acquisition HRL was Octfolio's largest customer. We note that IHG was also the former owner of Octief, and a business owned and operated by interests which include current HRL board members and major shareholders Kevin Maloney, Chairman, and Darren Anderson, Executive Director.

From largely a standing start in 2014, HRL today is a profitable environmental services business with a scalable platform for future growth. We are currently forecasting FY17 and FY18 EBITDA of \$1.4m and \$3.2m respectively with HRL trading on a FY18 EV/EBITDA of 5.9x.

We note also a highly aligned board and management team which collectively represents a shareholding in HRL of >40%, whilst the largest institutional investor is small cap specialist Viburnum Funds with 12.3%.

We initiate coverage on HRL with a BUY recommendation and Target Price of \$0.12/share.

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Figure 2: Corporate History

<b>2008 – 2014</b>	Unsuccessful geothermal company Hot Rocks (ASX: HRL). Significant shareholder value destruction.
<b>2014</b>	Change in strategic direction. Acquisition of OCTIEF. Kevin Maloney & Darren Anderson join the board.
<b>2015</b>	\$5m capital raise. Acquisition of Precise Consulting (NZ) & AAC Environmental (ACT). Organic branch rollout in NZ & Australia.
<b>2016</b>	Acquisition of RJL & Associates (NZ). Consolidate acquisitions. Organic branch rollout in NZ & Australia.
<b>2017</b>	5m rights issue & \$2.75m placement. Acquisition of Morrison Geotechnic & Octfolio.
<b>2017 →</b>	Continue to build out a scaled business in the environmental services industry. Leverage establish corporate cost base and footprint.

Source: Company Reports

## Acquisitions

**Morrison Geotechnic:** Morrison was established over 17 years ago and offers geotechnical engineering and construction soil testing services to clients primarily within South East Queensland. The company predominately services the civil, engineering and construction industries, with a blue-chip client base including a number of large civil contractors and government departments.

Located in South East Queensland, Morrison operates from three NATA (National Association of Testing Authorities) accredited laboratory facilities, and recently secured ISO 9001:2008 accreditation, which reflects a commitment to quality and improvement and is expected to help the business bid for a broader range of work.

Morrison has been acquired for a maximum purchase price of A\$4.5m, which includes initial consideration of A\$3.75m in cash, and earn-out consideration of up to \$0.75m should Morrison deliver EBIT of at least \$1.5m for 12-month period to 31 March 2018, while no earn-out is payable if EBIT is <\$1.1m.

We deem the Morrison acquisition timely given the Australian Council Industry Forum (ACIF) is forecasting growth of 23% in the period out to 2024/25 across the various sectors serviced by Morrison within the Brisbane and the broader Queensland market.

**Octfolio:** Octfolio is an Australian-based specialised software provider focused on the development and implementation of information management software solutions for asbestos and hazardous materials, field management and customized compliance solutions & applications relating to workplace health & safety.

HRL was previously Octfolio's largest client and acquiring the business is seen as a move to protect what is a complementary and enhanced service offering with Octfolio as part of HRL's environmental services capabilities.

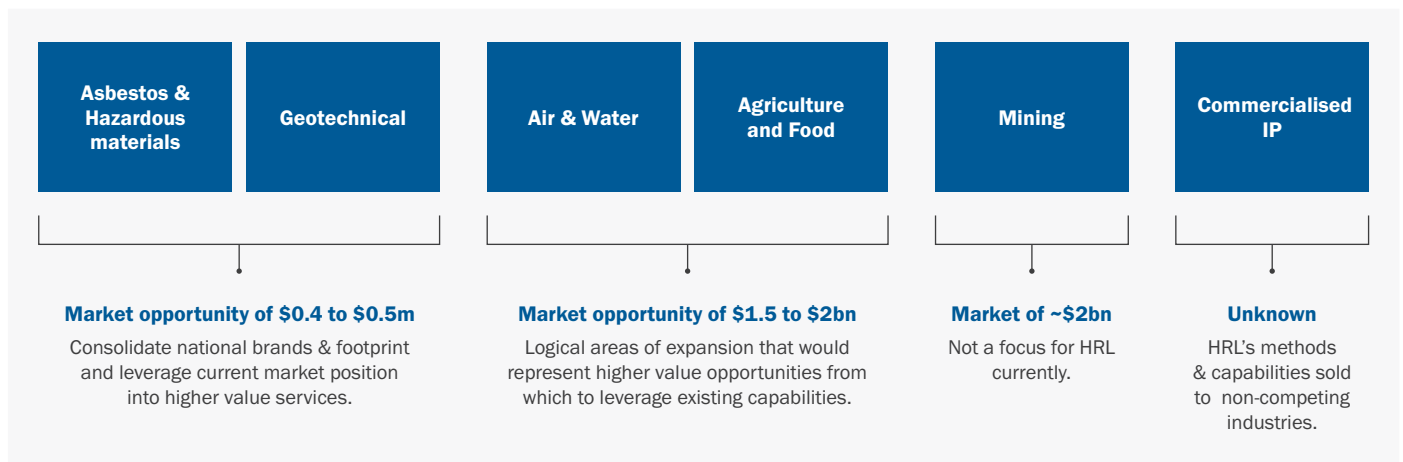
Octfolio's flagship product is its 'Octfolio Hazardous Material Compliance Software' which is a cloud-based platform that provides hazardous materials, environmental and OH&S management services to clients in Australia and New Zealand.

The business has been acquired from existing Board members in Kevin Maloney, Executive Chairman, and Darren Anderson, Executive Director, who have shareholdings in HRL of 25.1% and 17.7% respectively. Mr Anderson's holding includes broader family interests also, which includes his direct holding of 21.2m shares or 8.7%.

## Market opportunity & growth strategy

HRL currently is a relatively small, but integrated environmental services business, that is operating in a domestic market estimated broadly at ~A\$4bn. We note however that HRL's current focus on hazardous materials and geotechnical testing and analysis reflects ~12% of that market, or up to A\$500m.

Figure 3: Markets & opportunities

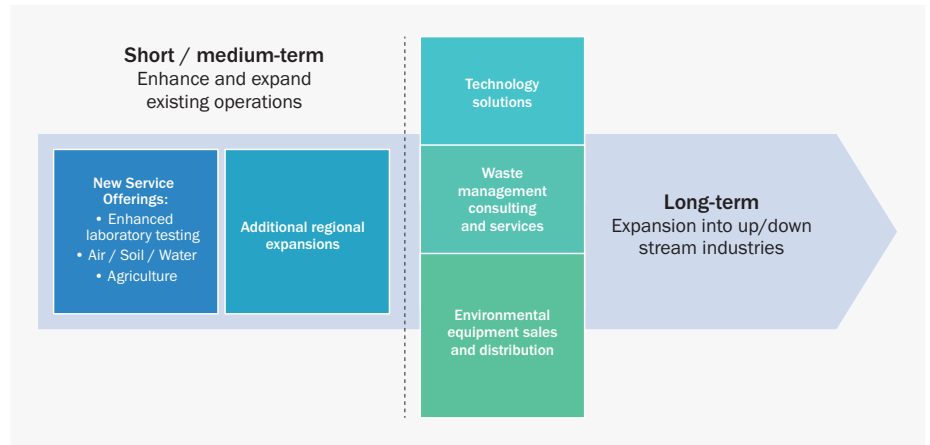


Source: Company Reports

We do expect however that HRL will look to expand that market opportunity into air & water and agriculture & food, which represents a logical extension to current capabilities, however the minerals/commodities market is not of interest at this stage.

Expansion within both existing and new verticals likely to come from a combination of organic growth and further acquisitions, the latter being more likely in order for HRL to expand market reach.

**Figure 4: Growth strategies**



Source: Company Reports

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A key feature of HRL's current operations is a single point of offer that captures initial field sampling through to laboratory analysis and reporting, with HRL now able to also provide clients an ongoing asset management solution via Octfolio.

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## Industry dynamics

The Australian and New Zealand environmental services industry comprises a number of larger industry participants, a number being publically listed companies with global capabilities, in addition to a long tail of smaller, state based participants. We believe that the current industry dynamic provides a significant opportunity at a 'mid-market' level, for a vertically integrated participant such as HRL.

Listed global players operating in Australia that provide assurance, testing, laboratory services, asset management & reporting amongst a broad range of environmental testing and analysis include:

- ALS Limited (ASX: ALS): domestic market share of ~12%;
- SGS SA (SWX: SGSN): domestic market share of ~8%;
- Bureau Veritas (BVI:FR): domestic market share of ~6%;
- Intertek Group (ITRK:GB): domestic market share of ~3%; and
- Eurofins (ERF:FR): small domestic market share.

All business listed above have an established footprint in Australia, as part of global operations, while we note both ALS and Eurofins are largely laboratory services only.

Other meaningful players of size and relevance to HRL's business include Coffey Environmental, acquired by Tetra Tech Int in 2016, Cardno (ASX: CDD) and Greencap Environmental, acquired by Wesfarmers in 2013 Wesfarmers (ASX: WES).

## Core capabilities and verticals

HRL is primarily focused on field sampling, laboratory analysis & technology, asset management and reporting solutions, which are specific to the asbestos / hazardous materials and geotechnical industries currently.

A key feature of HRL's current operations is a single point of offer that captures initial field sampling through to laboratory analysis and reporting, with HRL now able to also provide clients an ongoing asset management solution via Octfolio.

Mobile capabilities allow HRL to provide clients a 24 hour turnaround from sampling to analysis, something that provides clients with a significant reduction in downtime and associated costs, particularly in the case of hazardous materials.



## Customers

HRL's customer base incorporates a number of blue chip corporate customers and government departments in both Australia and New Zealand, with much of the work relating to large scale government and infrastructure projects.

HRL has little concentration risk across the business, albeit some significant clients include HRL's largest client in Housing New Zealand, while project work for Chorus, represents around 20% of Precises' current business, or ~\$0.7m per annum.

None of HRL's operations currently service the mining sector.

## Geographic locations provide solid base of laboratory services

HRL now has a footprint of 12 locations, of which 10 sites combine both laboratory and consulting services. HRL laboratories are all NATA accredited in Australia and IANZ accredited in New Zealand which represents the highest level of accreditation in the relative markets.

Geographically HRL now has four operating entities being **OCTIEF**, with locations in Brisbane (Yatala), Darwin, Canberra (AAE acquisition) and Perth, **Morrison Geotechnic**, with locations on the Gold Coast, Brisbane (Darra) and the Sunshine Coast and **Precise Consulting**, in New Zealand with locations in Auckland, Palmerston North, Wellington, Christchurch and Dunedin.

**Octfolio's** sales and development office is located also in Brisbane.

We note HRL may seek to differentiate the branding of its laboratory services from its filed testing operations at some time in the future, given there is demand from third parties, some of which are competitors, for its laboratory services.

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Around 75% of all HRL's current business reflects large scale project work on fixed contracts (6–18 months) and work for ongoing multi-year relationship clients, the majority of which is subject to long-term contracted rates.  
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Figure 5: HRL Group locations



Source: Company Reports

### An opportunity to expand into VIC, NSW or SA?

Given one of HRL's competitive advantages is local access to owned and operated labs, giving them a faster testing turnaround time for clients, we expect they will look to expand into Victoria, New South Wales (ex ACT) and South Australia over the coming 12 to 24 months.

Capex for building out their own small local labs can vary from ~\$100k to ~\$250k depending on the types of tests the lab will conduct and the services being offered. We understand a regional hub laboratory/office could likely exceed \$250k to establish, and therefore acquiring a more significant base of operations with an existing customer base may be more attractive.

## Revenue mix

**Project work and recurring business:** Around 75% of all HRL's current business reflects large scale project work on fixed contracts (6-18-months) and work for ongoing multi-year relationship clients, the majority of which is subject to long-term contracted rates.

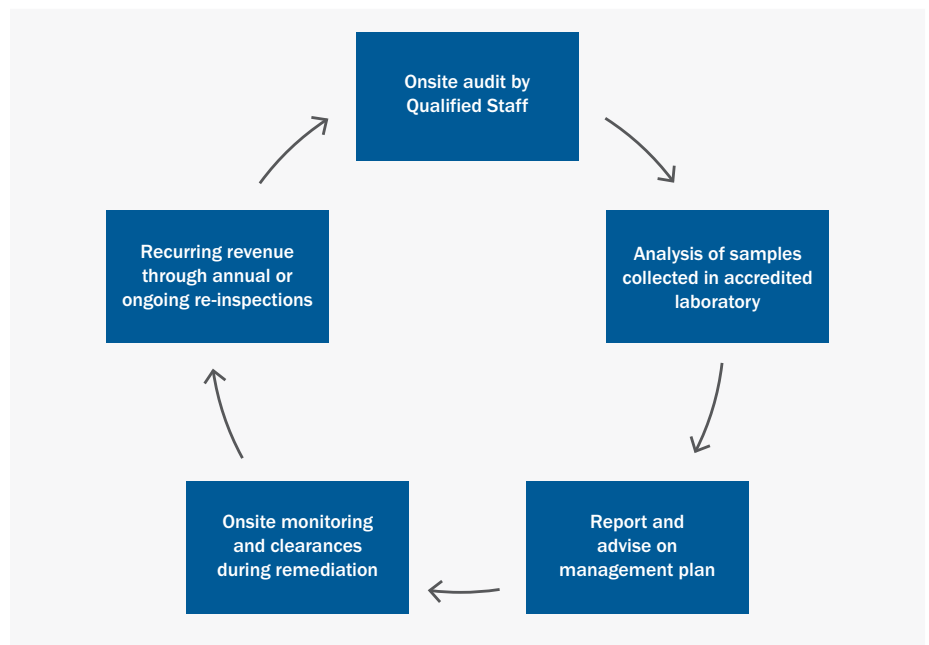
Irregular, one-off engagements represents less than 15% of business profile.

With regards to the type of work being undertaken across HRL's current operations, ~80% of business represents field sampling and subsequent laboratory testing, while the balance is laboratory testing only for third parties.

**Cash collection:** HRL is dealing largely with large blue chip customers and government, with debtor and creditor terms running largely in alignment, ensuring a predictable cash conversion rate of earnings.

We expect a cash conversion of EBITDA to Operating cashflow before interest and tax (OCFBIT) of approximately 75% from established operations in FY18, for which we expect improvement longer-term and the business expands and operational synergies are gained.

Figure 6: Revenue cycle



Source: Company Reports

## Earnings - 1H17A

Figure 7: 1H17A HRL underlying results

	OCTIEF	Precise	Total	Corporate	Consolidated
Revenues	1.97	3.50	5.47	0.00	5.47
Underlying EBITDA	0.19	0.79	0.98	-0.61	0.37
Underlying PBT	0.08	0.58	0.66	-0.66	0.00
NRI	0.00	0.00	0.00	-0.04	-0.04
PBT	0.08	0.58	0.66	-0.70	-0.04
Tax					0.04
NPAT					-0.01

Source: Company Reports, Canaccord Genuity estimates

1H17 revenues increased by 29% to \$5.5m, however underlying EBITDA declined to \$0.4m, from ~\$0.8m in the PCP. The decline in EBITDA reflecting the significant level of investment across the business for increased capacity, in addition to the ongoing establishment of a corporate overhead necessary for future expansion. Key areas of expansion during 1H17 included:

- The establishing of a new branch in Auckland, including the set up and accreditation of a new laboratory facility; and
- Organic expansion in leveraging the existing operations, which included a number of senior appointments.

We estimate total 1H17 OPEX investment for growth was ~\$0.5m, while the group continued to build out a corporate overhead which was reported at \$0.6m for the period, and we forecast a FY17 corporate overhead charge of \$1.4m.

### 1H17A pro-forma – Morrison and Octfolio

Figure 8: 1H17A HRL pro-forma

(\$m) – unless stated	HRL	Morrison	Octfolio	Consolidated
Revenues	5.47	4.83	0.32	10.61
Underlying EBITDA	0.37	0.92	0.13	1.42
Underlying EBITA	0.24	0.80	0.13	1.17
Underlying EBIT	0.05	0.80	0.13	0.98
Underlying PBT	0.00	0.79	0.13	0.92
NRI's	-0.04	-0.03	-0.09	-0.16
PBT	-0.04	0.76	0.04	0.76
Tax	0.04	-0.23	-0.01	-0.20
NPAT	-0.01	0.53	0.03	0.55
NPAT adj.				0.68

Source: Company Reports, Canaccord Genuity estimates

On a 1H17 pro-forma basis HRL delivered underlying EBITDA and NPAT of \$1.4m and \$0.6m respectively. On revenues of \$10.6m an underlying EBITDA margin of 13.4% was achieved, which while healthy, we do expect margin expansion going forward as synergies and leverage emerges across the business.

1H17 contributions to 1H17 pro-forma from recent acquisitions are as follows:

- Morrison: revenues of \$4.8m and EBITDA of \$0.9m, and
- Octfolio: revenues of \$0.3m and EBITDA of \$0.1m.

## Forecasts & valuation

Figure 9: Earnings estimates

(\$m) – unless stated	FY16A	FY17F	FY18F	FY19F
<b>Revenues</b>				
- Octief	4.0	5.1	5.5	5.8
- Precise	4.4	6.3	6.9	7.2
- Morrison		2.3	9.4	9.7
- Octfolio		0.1	0.7	0.8
- eliminations		(0.2)	(0.5)	(0.5)
<b>Total Revenues</b>	<b>8.4</b>	<b>13.5</b>	<b>22.1</b>	<b>23.1</b>
<b>EBITDA</b>				
- Octief	0.7	1.0	1.2	1.3
- Precise	1.5	1.3	1.8	1.9
- Morrison		0.5	1.5	1.6
- Octfolio		0.1	0.3	0.4
- Corporate	(1.2)	(1.4)	(1.6)	(1.7)
<b>Total EBITDA</b>	<b>1.1</b>	<b>1.4</b>	<b>3.2</b>	<b>3.5</b>
<b>EBITDA margin</b>	<b>12.8%</b>	<b>10.5%</b>	<b>14.5%</b>	<b>14.9%</b>
<b>Depreciation</b>	<b>(0.2)</b>	<b>(0.4)</b>	<b>(0.7)</b>	<b>(0.7)</b>
<b>EBITA</b>	<b>0.9</b>	<b>1.1</b>	<b>2.5</b>	<b>2.8</b>
<b>NPATA - underlying</b>	<b>0.6</b>	<b>0.7</b>	<b>1.7</b>	<b>2.0</b>
<b>less Amort – Intangibles</b>	<b>(0.2)</b>	<b>(0.4)</b>	<b>(0.7)</b>	<b>(0.7)</b>
<b>less Significant items</b>	<b>(0.3)</b>	<b>(0.2)</b>	<b>0.0</b>	<b>0.0</b>
<b>NPAT - reported</b>	<b>0.1</b>	<b>0.1</b>	<b>1.0</b>	<b>1.3</b>

Source: Company Reports, Canaccord Genuity estimates



On a segmented basis we forecast that all business units will contribute profitable EBITDA for FY17 pre corporate overheads. We note that our medium-term forecasts for both Morrison and Octfolio assume that the full earn-outs are paid.

We note also the decline in forecasts FY17 EBITDA for Precise as work in relation to the Christchurch earthquake recovery projects came to an end during the period, while management concurrently invested in geographical expansion and services being provided.

## Balance sheet estimates

Figure 10: Balance sheet estimates

(\$m) – unless stated	2016A	2017F	2018F	2019F
Cash	0.4	0.7	1.8	3.8
Inventories	0.0	0.0	0.0	0.0
PP&E	0.7	1.3	1.0	0.7
Debtors	1.4	3.5	4.4	5.0
Intangibles	5.7	10.9	9.9	9.0
Other assets	1.0	1.8	1.8	1.8
<b>Total Assets</b>	<b>9.1</b>	<b>18.2</b>	<b>18.9</b>	<b>20.2</b>
Borrowings	1.4	0.4	0.0	0.0
Trade Creditors	0.7	0.8	0.9	0.9
Other Liabilities	0.4	1.7	1.7	1.7
<b>Total Liabilities</b>	<b>2.4</b>	<b>2.9</b>	<b>2.5</b>	<b>2.6</b>
<b>NET ASSETS</b>	<b>6.7</b>	<b>15.4</b>	<b>16.4</b>	<b>17.7</b>

Source: Company Reports, Canaccord Genuity estimates

**Funding:** On the back of the recent capital raising, and the recent release of HRL's 4Q17 quarterly cashflow report, cash on hand as at 30 June 2017 will be \$0.7m, with an additional \$1.5m of undrawn loan facilities out of a total facility of \$2.3m currently.

On the back of the Morrison acquisition capex has increased to ~\$0.4m in FY17, from ~\$0.2m p.a. in the PCP. The increased spend attributable predominately to vehicles and to that extent for Morrison.

We estimate cash on hand of ~\$0.7m which allows management to adequately fund operations from current cash flow, while we have made no allowance at this stage for any further acquisitions and/or capital raising activity.

## Valuation – \$0.12 cps

For HRL we have derived an A\$0.12 Target Price based on a DCF Valuation methodology.

Our DCF Valuation methodology incorporates a WACC of 11.2% which is derived from a 4.25% risk free rate, a 1.35x beta and a 5.0% equity risk premium.

For NVL we have assumed a terminal growth rate of 2.5%.

Figure 11: DCF Valuation Summary

Valuation	(\$m)
PV of Cash flows 2018 to 2020	5.2
PV of Cash flows 2021 to 2027	11.1
PV of Terminal Cash flow	13.2
<b>Total PV</b>	<b>29.5</b>
Less: Net Debt	(0.4)
Less: Minority Interest	0.0
<b>PV Equity</b>	<b>29.9</b>
<b>PV per share</b>	<b>\$0.12</b>

Source: Company Reports, Canaccord Genuity estimates

## Peer group comparison

Figure 12: Peer group metrics

Company		Market Cap (Loc)	PER		EV/EBITDA	
			FY17F (x)	FY18F (x)	FY17F (x)	FY18F (x)
ALQ-AU	ALS LIMITED	3741.3	25.1	21.0	12.8	11.3
BVI-FR	BUREAU VERITAS	8506.3	20.3	19.1	11.7	11.0
ERF-PAR	EUROFINS SCIENTIFI	7931.8	37.5	32.2	16.1	14.3
ITRK-GB	INTERTEK GROUP	6941.4	23.5	21.9	13.8	12.8
SGSN-SWX	SGS SA	16724.4	24.6	22.8	13.8	12.8
	Average		26.2	23.4	13.6	12.5
	Median		24.6	21.9	13.8	12.8
HRL-AU	HRL HOLDINGS LTD	19.8	21.6	12.2	14.4	5.9
	Prem. / (disc't) - median		-12%	-44%	5%	-54%

Source: Company Reports, Canaccord Genuity estimates / Prices as at 1 August 2017.

We have established a broader based peer group of businesses operating in the environmental testing and services market sector globally, and based on consensus estimates for peers, HRL is currently trading on a material discount to our broader-based peer group for FY18 on both a PER and EV/EBITDA basis.

We do note however that our peer group are businesses that operating across a broader spectrum of industries to HRL, while they are also larger in size with a significantly expanded and established global capability.

## Key Investment Risks

### Competition

Competition is significant, and in the form of large international players for whom Australia represents an established, albeit relatively small contributor to the group operations, or smaller state based operators without a comprehensive and vertically integrated solution.

### Consolidation can be challenging

HRL have done a sound job of establishing the business through acquisition, however the ongoing consolidation and integration of smaller businesses will represent challenges.

### Limited history and track record

HRL was effectively formed through the back door listing of Octief in September 2014, hence the business remains at an early stage relatively young and continues to build scale, predominantly through acquisition which provides another layer of complexity to an emerging business.

## Management and Board of Directors

### Steven Dabelstein - CEO

Mr. Dabelstein has a strong financial and operational background in various roles, including most recently as General Manager Commercial and Old Mining/Maintenance Services with Diversified Mining Services Limited. His experience includes public practice accounting, manufacturing, service and the construction industries. Previous roles have provided exposure to large-scale international businesses reporting through and working with companies in the US, Asia and Europe.

### Michael Harvey - CFO

Mr. Harvey is a Chartered Accountant and Chartered Secretary. He has more than 15 years in the accountancy profession in Australia, having worked for PKF (now BDO) for eight years in audit, and subsequently over five years in commercial roles as financial controller for a number of listed companies mainly in the property and resources sector.

### Kevin Maloney - Chairman

Mr Maloney is the founder and Chairman of Australian investment entity Tulla Group and has built an extensive career in retail banking, finance and resources. Kevin joined Elders Resources in 1981 after 20 years with ANZ Bank. During his time at Elders Resources, Kevin held numerous positions including CEO of Elders Resources Finance Limited. Kevin was also founder and Executive Chairman of The MAC Services Group (The MAC), which was sold to Oil States International in 2010 for \$651million. Kevin is currently also Chairman of ASX listed Altona Mining Ltd (ASX: AOH) and has been involved with numerous public companies as both an executive and non-executive director.

**Darren Anderson – Executive Director**

Mr Anderson was formerly the Executive Director and Chief Operating Officer of Diversified Mining Services Ltd which is an unlisted public company that at its peak in mid-2012 had consolidated revenue in excess of \$200 million and 850 personnel.

His career includes 15 years spent as founder and Managing Director of the Anderson Group of Companies, which grew from a single person operation in Mackay to a company with >300 employees and 12 operating divisions across both Queensland and New South Wales that serviced the Australian and international coal industries.

**Dr Mark Elliot – Non Exec Director**

Dr Elliott is a chartered practicing geologist with more than 39 years' experience in economic geology, exploration, mining, project development and corporate management. He has extensive experience in managing companies and exploration/mining operations in a wide range of commodities including energy. He is currently a non-executive director of Nexus Energy Limited.

**John Taylor - Non Exec Director**

Mr Taylor is the founding partner of Taylors Solicitors, Mackay, and a Senior Counsellor of the Queensland law Society and has over 30 years' experience in commercial and property transactions and litigation.

John Taylor was, from 2006 to 2010, a director of ASX listed The Mac Services Group Limited where he was Chair of the Remuneration and Nomination Committee and a member of the Audit and Risk Management Committee. He is also a former Chair of the Mackay Port Authority and a Board member of Tourism Mackay and Mackay Regional Economic Bureau.

**Paul Marshall – Company Secretary**

Mr Marshall is a Chartered Accountant. He holds a Bachelor of Law degree, a post Graduate Diploma in Accounting and is a member of the Institute of Chartered Accountants in England and Wales. He has more than 25 years in the accountancy profession, with Ernst and Young for ten years, and subsequently fifteen years spent in commercial roles as Company Secretary and CFO for a number of listed and unlisted companies mainly in the resources sector.

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### Site Visit Disclaimer\*\*

A site visit has been conducted.

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