

24 January 2024

Price (p)	480.60
Shares in issue (m)	385
Mkt Cap (£m)	1,849
Net debt (£m)	1,356
EV (£m)	3,205
BVPS (p)	328.0

Share price performance

1m	-0.9%
3m	8.4%
12m	-27.1%
12 m high/low	695/395
Ave daily vol (30D)	1,117,294

Shareholders

Invesco Ltd	7.7%
Vanguard Group	4.9%
Blackrock Inc	4.9%
Orbis Allan Gray Ltd	4.3%
Schroders Plc	3.9%
Jupiter	3.7%
Dimensional Fund	3.2%
Bank Of America	2.9%
Emirate Abu Dhabi	2.7%
Royal London Asset	2.5%
Total for top 10	40.6%
Free float	99.7%
Source: Bloomberg	18 Jan 24

Next news Finals Q1

Business description

Integrated biomass, hydro and storage IPP



Research

Adam Forsyth
adam.forsyth@longspur.com
+44 (0) 131 357 6770

Max Campbell

max.campbell@longspur.com
+44 (0) 7900 206039

Distribution

Adam Robertson
adam.robertson@longspur.com
+44 (0) 203 940 6602

NAO CALLS FOR REVIEW MONITORING

The NAO has criticised a lack of evaluation of government approaches to monitoring biomass sustainability. It does not say that these approaches are inappropriate, merely that they cannot be demonstrated to be appropriate. It therefore supports a detailed review of monitoring which we see as consistent with already announced plans. Overall, we do not see anything here as particularly onerous for Drax and see better monitoring as building credibility for the BECCS solution.

NAO Report on Support for Biomass

The UK's National Audit Office (NAO) has reported on the government's support for biomass. This covers all biomass usage including heating where biomass accounts for 6.4% of UK heat generation including domestic and commercial use of biomass pellets in boilers. For Drax, who are pursuing a bioenergy and carbon capture and storage (BECCS) strategy, the report helpfully acknowledges the net decrease in emissions delivered by BECCS and confirms use of biomass at critical times to support the electricity grid. The report also stresses that the lifecycle sustainability criteria already set by government needs to be met if biomass is to deliver on its low carbon potential. This includes ensuring that biomass is from well-managed forests where carbon can be reabsorbed in a relatively short time as it regrows.

Plans to Strengthen Sustainability Criteria Already Announced

While the NAO acknowledges that the government has already announced plans to strengthen sustainability criteria for any future support, it is critical of government for not evaluating whether the current arrangements provide adequate assurance although a pilot review is underway. The NAO supports OFGEM in calling for a proper assessment. It also supports the already tabled move to require 100% of woody biomass, including that used for heating, to meet sustainability criteria rather than the current 70%. We do not see any of this as particular onerous for Drax and as a supplier of sustainably sourced woody biomass there is a potential opportunity although we doubt it will target the UK heating market.

Biomass Contribution to Net Zero

The report highlights that if biomass cannot make the contribution to net zero additional action will be required to hit the net zero target legally imposed by the Climate Change Act 2008. With the main other alternative being direct air capture (DAC), which is less proven technically, expensive and consumes more power, this would put the net zero target at risk in our view.

£,000 Dec	2021a	2022a	2023e	2024e	2025e	2026e
Sales	5,174	8,159	5,712	5,834	5,988	5,318
EBITDA	370	709	1,158	1,066	1,212	601
PBT	101	405	808	707	855	274
EPS	22.3	85.1	115.3	92.0	168.6	55.5
CFPS	34.7	25.2	112.3	70.3	165.2	165.7
DPS	18.8	21.0	23.1	25.4	27.9	30.7
Net Debt (Cash)	1,170	1,356	1,097	1,004	536	59
Debt/EBITDA	3.2	1.9	0.9	0.9	0.4	0.1
P/E	21.5	5.6	4.2	5.2	2.9	8.7
EV/EBITDA	8.2	4.5	2.5	2.7	2.0	3.2
EV/sales	0.6	0.4	0.5	0.5	0.5	0.6
FCF yield	7.2%	5.2%	23.4%	14.6%	34.4%	34.5%
Div yield	3.9%	4.4%	4.8%	5.3%	5.8%	6.4%

FINANCIAL MODEL

Profit and Loss Account

£,000, Dec	2021a	2022a	2023e	2024e	2025e	2026e
Turnover						
Power Generation	4,682	7,358	4,641	4,541	4,522	3,701
B2B Energy Supply	2,360	4,143	2,816	3,015	3,229	3,458
Pellet production	450	803	691	774	795	781
Central, int gp and depn	-2,318	-4,145	-2,435	-2,496	-2,558	-2,622
Total	5,174	8,159	5,712	5,834	5,988	5,318
Operating profit						
Power Generation	352	679	1,153	1,073	1,217	594
B2B Energy Supply	6	26	55	41	45	49
Pellet production	86	134	101	105	107	100
Central, int gp and depn	-273	-369	-407	-422	-444	-413
Operating profit	170	469	901	797	926	330
P&L Account	2021a	2022a	2023e	2024e	2025e	2026e
Turnover	5,174	8,159	5,712	5,834	5,988	5,318
Operating Profit	170	469	901	797	926	330
Investment income	0	0	0	0	0	0
Net Interest	-70	-64	-94	-90	-71	-55
Pre Tax Profit (UKSIP)	101	405	808	707	855	274
Goodwill amortisation	0	0	0	0	0	0
Exceptional Items	21	-327	0	0	0	0
Pre Tax Profit (IFRS)	122	78	808	707	855	274
Tax	-12	-67	-364	-353	-206	-61
Post tax exceptionals	-30	72	0	0	0	0
Minorities	1	3	0	0	0	0
Net Profit	80	85	444	354	649	214
Dividend	-71	-80	-87	-96	-106	-116
Retained	9	5	357	258	543	98
EBITDA	370	709	1,158	1,066	1,212	601
EPS (p) (UKSIP)	22.31	85.06	115.32	92.03	168.56	55.55
EPS (p) (IFRS)	20.01	21.25	115.32	92.03	168.56	55.55
FCFPS (p)	34.66	25.20	112.30	70.29	165.19	165.66
Dividend (p)	18.80	21.00	23.10	25.40	27.90	30.70

Source: Company data, Longspur Research estimates

KEY POINTS

- Pricing drops revenue in FY 23 but profitability remains
- Net interest balanced between cashflow and capex
- Higher tax due to windfall tax in FY 23 and FY 24, lower in FY 25 as pricing starts to normalise
- Dividend remains covered throughout

Balance Sheet

£,000, Dec	2021a	2022a	2023e	2024e	2025e	2026e
Fixed Asset Cost	4,166	4,482	5,008	5,387	5,693	5,605
Fixed Asset Depreciation	-1,855	-2,094	-2,351	-2,619	-2,905	-3,177
Net Fixed Assets	2,311	2,388	2,657	2,768	2,788	2,428
Goodwill	416	424	424	424	424	424
Other intangibles	189	142	142	142	142	142
Investments	125	145	145	145	145	145
Stock	501	536	375	383	393	349
Trade Debtors	642	1,227	859	877	901	800
Other Debtors	1,324	1,294	1,194	1,244	1,294	1,294
Trade Creditors	-1,211	-1,528	-1,070	-1,093	-1,121	-996
Other Creditors <1yr	-966	-1,013	-1,013	-1,013	-1,013	-1,013
Creditors >1yr	-767	-877	-877	-877	-877	-877
Provisions	-86	-59	-59	-59	-59	-59
Pension	0	0	0	0	0	0
Capital Employed	2,476	2,680	2,778	2,943	3,018	2,639
Cash etc	317	238	546	628	522	991
Borrowing <1yr	56	67	67	67	67	67
Borrowing >1yr	1,431	1,527	1,576	1,565	991	984
Net Borrowing	1,170	1,356	1,097	1,004	536	59
Share Capital	48	48	48	48	48	48
Share Premium	432	433	433	433	433	433
Retained Earnings	198	194	550	808	1,352	1,449
Other	607	636	636	636	636	636
Minority interest	22	13	13	13	13	13
Capital Employed	2,476	2,680	2,778	2,943	3,018	2,639
Net Assets	1,307	1,324	1,681	1,939	2,482	2,580
Total Equity	1,307	1,324	1,681	1,939	2,482	2,580

Source: Company data, Longspur Research estimates

KEY POINTS

- Working capital remains comfortable across period
- Goodwill increases in FY 21 with pellet acquisition
- Net debt rises with acquisition and then drops with cashflow
- Sale of OCGTs reduces net debt further in FY 26

Cashflow

£,000, Dec	2021a	2022a	2023e	2024e	2025e	2026e
Operating profit	170	469	901	797	926	330
Depreciation	199	239	257	268	286	271
Provisions	-4	-29	0	0	0	0
Other	-42	14	0	0	0	0
Working capital	32	-374	-233	-2	133	154
Operating cash flow	355	320	925	1,064	1,345	755
Tax paid	12	-39	-67	-364	-353	-206
Capex (less disposals)	-209	-173	-426	-429	-356	88
Investments	-20	-8	0	0	0	0
Net interest	-60	-74	-94	-90	-71	-55
Net dividends	-71	-79	-80	-87	-96	-106
Residual cash flow	7	-52	259	93	468	476
Equity issued	2	1	0	0	0	0
Change in net borrowing	363	187	-259	-93	-468	-476
Adjustments	-359	-136	0	0	0	0
Total financing	7	52	-259	-93	-468	-476

Source: Company data, Longspur Research estimates

KEY POINTS

- Working capital negative in FY 23 but some reversal further out
- Capex slightly down in FY 20 as signalled by company
- Sale of OCGTs in FY 26 reflected in capex
- Further capex on pellet business expansion
- Windfall tax outflows in FY 24 and FY 25

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Longspur Research
10 Castle Street,
Edinburgh. EH2 3AT
UK

Longspur Capital
20 North Audley Street,
London. W1K 6WE
UK