

DYNACERT INC. *5a,5b,11

Rating: Buy
Target price: 2.20 CAD
(USD 1.65; EUR 1.40)

Current price: 0.66
03.09.2020 / TSX / 21:59
Currency: CAD

master data:

ISIN: CA26780A1084
WKN: A1KBAV
TSX.V: DYA
OTCQB: DYFSF
DAX: DMJ
Number of shares³: 311.64
Marketcap³: 154,26
EV: 154,26
³ in m / in m CAD
Free float: 24%.

Primary listing: TSX-Venture

Second listing: Frankfurt

Accounting Standard: IFRS

Fiscal year end: 31.12.

Analysts:

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Date and time of study completion: October 5, 2020 (08:45)

Date and time of the first transfer: October 5, 2020 (10:00)

Validity of the price target: until max. 31.12.2021

* Catalogue of possible conflicts of interest on page 44

Company profile

Industry: Clean tech

Focus: Retrofit technology to reduce emissions

Head office: Toronto, Canada

Management: James Payne (President & CEO); Wayne Hoffman (Chairman); Robert Maier (COO); Jean-Pierre Colin (Director and Executive Vice President + Corporate Secretary)

dynaCERT Inc. produces and distributes a technology to reduce carbon dioxide emissions for use with internal combustion engines. As part of the growing global hydrogen economy, its patented technology produces hydrogen and oxygen on demand through a unique electrolysis system and delivers these gases through the air intake to improve combustion, resulting in lower CO2 emissions and greater fuel efficiency. The technology is designed for use with various types and sizes of diesel engines, including road vehicles, refrigerated trailers, off-road applications, power generation, mining and forestry equipment, ships and locomotives.



P&L in CAD million \ FY end	31/12/2019	31/12/2020e	31/12/2021e	31/12/2022e
Sales	1.06	32.00	200.00	350.00
EBITDA	-7.68	-1.24	30.32	55.81
EBIT	-7.73	-1.34	30.02	55.31
Net income for the year	-12.67	-1.34	21.76	40.10

Key figures in million CAD

Earnings per share	-0.04	0.00	0.06	0.11
Dividend per share	0.00	0.00	0.00	0.00

Key figures

EV/Sales	237.44	7.90	1.26	0.72
EV/EBITDA	-32.91	-204.65	8.34	4.53
EV/EBIT	-32.70	-189.32	8.42	4.57
P/E RATIO	-18.67	-177.10	10.87	5.90
KBV	12.49			

**last research from GBC:

Date: Publication / Target price in CAD / Rating
10.08.2020: RS / 2.20 CAD; € 1.40 / BUY
20.09.2019: RS / 1.90 CAD; € 1.30 / BUY

** above-mentioned Research studies can be seen at www.gbc-ag.de, and/or be requested from GBC AG, Halderstr. 27, 86150 Augsburg, Germany

Financial calendar

Notice according to MiFID II regulation for research "Minor non-monetary benefits": This research meets the requirements for classification as "Minor Non-Monetary Benefit". For further information, please refer to the disclosure under "I. Research under MiFID II".

Half-year figures in line with expectations. Significant sales leaps should be achieved in the second half of 2020. Target price confirmed: CAD 2.20, rating: Buy.

in million CAD	H1 2018	H1 2019	H1 2020
Sales	0,01	0,05	0,33
EBITDA	-2,59	-3,65	-4,16
EBIT	-2,69	-3,76	-4,35
Net income for the year	-4,20	-6,02	-4,55

Sources: dynaCERT Inc., GBC AG

In the first six months of the current financial year, sales revenues increased significantly by 580.0% to CAD 0.33 million (previous year: CAD 0.05 million). This was due to the good sales start into the 2020 financial year, although sales and in particular production were significantly restricted due to the corona crisis. A total of 47 units were delivered in the first half of 2020. While sales revenues of CAD 0.31 million were generated in the first quarter of 2020, there were no significant sales contributions in the second quarter. We had already anticipated this development, as the production facility had to remain closed. Currently, production has restarted and we expect significant sales increases in the second half of the year. dynaCERT has maintained the existing employee structure even during the COVID crisis and has received governmental support in the amount of CAD 0.44 million.

As already described in the research report of August 10, 2020, it was announced on May 11, 2020 that KarbonKleen Inc. has been granted exclusive dealer rights for the truck sector in the USA. KarbonKleen receives regional exclusivity and in return has to purchase at least 150,000 HydaGENTM units over the next three years. The first order for 3,000 units was placed on May 9, 2020.

The company also has a wholly owned subsidiary called dynaCERT International Strategic Holdings Inc. ("DISH") to realize international investments in relevant technologies and sales commitments and to implement the subscription model for the dynaCERT units. Thus, 3,000 units were committed to KarbonKleen until December 31, 2021 under a subscription model. Furthermore, dynaCERT indirectly holds 20% of KarbonKleen via DISH. In our opinion, this is an important investment, as KarbonKleen has secured exclusive rights for the truck market in the USA. This is likely to be the most important market for dynaCERT, especially in the near future. Therefore, a 20% share in the most important target market should be very important and could turn out to be a very profitable investment.

In addition, dynaCERT has moved up from the TSX Venture Exchange to the TSX Exchange. We believe this should provide the Company with better access to capital and increased visibility.

Moreover, within the framework of homologation (homologation is a supranational system for the approval of motor vehicles and vehicle parts) of the ABE certificate of conformity in the United Arab Emirates could be achieved. Thus, this market should be well accessible now.

Overall, the first half of the year was in line with expectations, and with the resumption of production it should also be possible to achieve significant sales increases in the second half of 2020.

Forecast confirmed

P&L (million CAD)	FY 2019	GJ 2020e	GJ 2021e	GJ 2022e
Turnover	1.06	32.00	200.00	350.00
EBITDA	-7.68	-1.24	30.32	55.81
<i>EBITDA Margin</i>	<i>-721.5%</i>	<i>-3.9%</i>	<i>15.2%</i>	<i>15.9%</i>
EBIT	-7.73	-1.34	30.02	55.31
<i>EBIT Margin</i>	<i>-726.2%</i>	<i>-4.2%</i>	<i>15.0%</i>	<i>15.8%</i>
Net result	-12.67	-1.34	21.76	40.10
EPS in CAD	-0.04	0.00	0.06	0.11

Source: GBC AG

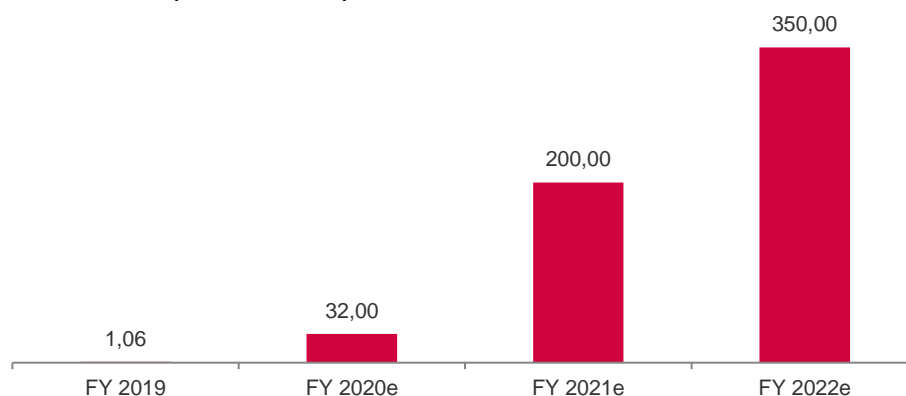
Sales forecast

Production was stopped in the first half of the year and should have resumed in the meantime (August 2020). The company has also started offering leasing solutions. As a result, sales revenues will be lower in the short term, but the margin will be significantly higher, as recurring sales can be booked almost entirely as revenue once the break-even point has been reached.

With dynaCERT technology, there should be considerable savings of diesel, which should lead to strong cost reductions. Companies with a large number of diesel engines, such as logistics companies and mining companies, will particularly benefit from this. The fact is that such companies rely heavily on new technologies for ongoing cost reduction. For example, there is an adoption explosion as soon as a new technology is used. The background to this development is likely to be that market participants who use the new technology work much more efficiently and either drive other market participants out of the market or indirectly force them into adopting the new technology. This is particularly evident in the development of trailer aprons, where market penetration began in 2008. After two years, the adoption rate was already over 60%.

We assume that, on the one hand, the effectiveness of the dynaCERT technology is significantly higher than that of trailer aprons but, on the other hand, the costs are also significantly higher than for trailer aprons. According to the Canadian Council of Energy Ministers, trailer aprons cost between 1500 and 2500 CAD and achieve fuel savings of between 4 and 7%. The dynaCERT technology has shown varying degrees of fuel savings, often between 9% and 15%. This technology, with a sales price of CAD 6000, would be roughly equivalent to the price/performance ratio of trailer skirts.

Sales forecast (in million CAD)



Source: GBC

On the basis of this model, we have prepared our medium-term sales forecast. We expect sales to increase significantly to CAD 32 million in 2020, followed by CAD 200 mil-

lion in 2021 and CAD 350 million in 2022. In view of our assumption regarding comparable developments in trailer skirts, our model can still be considered conservative. At the same time, the management is also relying on leasing models in addition to selling the systems. Leasing should enable the company to penetrate the market much faster, as this is much less capital intensive for customers. However, in the short term, this leads to lower sales at dynaCERT, as the annual leasing rate is lower than the one-time sales price. In the long term, the proportion of recurring sales will increase, which should also make a high contribution to earnings.

Anticipated order fulfillment is approximately 2,500 units and a further 3,000 units in the subscription model. We assume that one unit will be sold at a price of CAD 6,000 and that the leasing will pay for itself in about two years. A capacity limit should not be a limiting factor for the coming years. Currently, the company can produce about 2,000 units per month, or 24,000 units per year, which corresponds to a turnover of about 144 million CAD. This would correspond to one production shift. With three shifts, the capacity could be tripled, i.e. increased to 432 million CAD turnover. We assume that the production line can also be expanded in the medium term, so that no capacity limits are reached.

The high sales growth should be supported by external sales. The high sales growth should be supported by external sales through the company's extensive global dealer network that now exceeds 40 dealers. dynaCERT has dealers in Canada, the USA, Mexico, South America, Europe and the Middle East and India. dynaCERT also recently announced a co-operation with Alltrucks in Europe which is anticipated to facilitate installation and distribution channels.

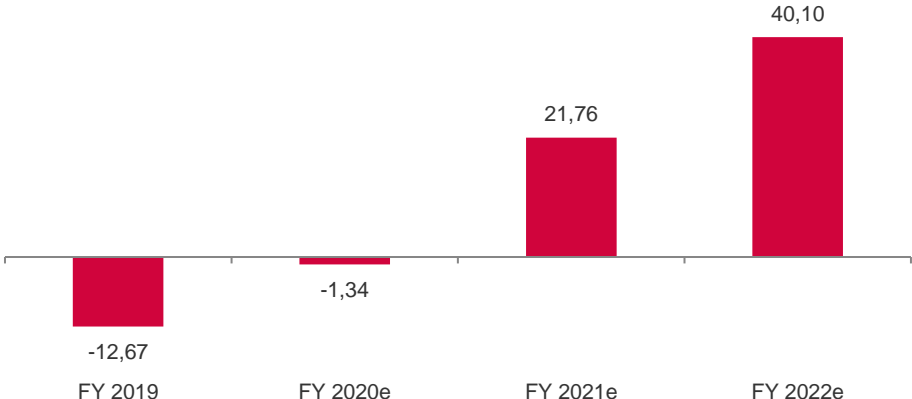
dynaCERT has announced that it is now active in the FreightTech market. FreightTech should be an excellent fit for dynaCERT's portfolio as it addresses very similar customers. This should allow the company to create even more attractive offerings for customers, which could further accelerate the pace of growth in the future.

Our current sales forecast does not yet take into account the enormous potential of CO2 certificates "Carbon Credits". This business area could be even more profitable in the future than the classic sale of dynaCERT equipment. By reducing the fuel consumption of diesel engines while at the same time reducing carbon emissions and other pollutants, the dynaCERT technology can become very lucrative with the worldwide market acceptance of the CO2 certificates. For example, it is estimated that a class 8 truck can generate up to €2,500 per year (3,918 CAD/year) in emission credits at a market price of €25/t CO2. We see this step as the next stage of development for the company and this would again lead to a significant increase in sales revenues.

Results forecast

On the earnings side, we expect dynamic development since, on the one hand, the gross margin is very high at 50% and, on the other hand, the leasing model should generate high recurring revenues at very low variable costs. We assume that costs will remain largely stable and develop disproportionately low. In addition, the gross margin should continue to rise in the medium term, as the unit costs for an increasing number of units should continue to fall. In the R&D area, we continue to expect cost increases, as technology is expected to continue to develop continuously. Furthermore, we assume that business development costs will also continue to rise.

Annual net profit forecast (in millions of CAD)



Source: GBC

In view of the as-yet-unanticipated income from emission credits, we have prepared an income forecast based on the units sold. Currently, we expect after-tax earnings of CAD -1.34 million in the current fiscal year 2020 and CAD 21.76 million in 2021, followed by CAD 40.10 million in 2022.

VALUATION

Model assumptions

dynaCERT Inc. was valued by us using a three-stage DCF model. Starting with the concrete estimates for the years 2020, 2021 and 2022 in phase 1, the second phase covers the period from 2023 to 2027 and includes a forecast of the value drivers. We expect revenue growth of 20.5 %. We have conservatively assumed an EBITDA margin target of 16.0 %. We have included a tax rate of 15.0 % in phase 2. In the third phase, a residual value will be determined by means of the perpetual annuity after the end of the forecast horizon. We assume a growth rate of 2.0 % in the terminal value.

Determination of the cost of capital

The weighted average cost of capital (WACC) of dynaCERT Inc. is calculated from the cost of equity and the cost of debt. To determine the cost of equity, the fair market premium, the company-specific beta and the risk-free interest rate must be determined.

From now on, the risk-free interest rate will be derived from current yield curves for risk-free bonds in accordance with the recommendations of the IDW's Fachausschuss für Unternehmensbewertungen und Betriebswirtschaft (FAUB) (Technical Committee for Company Valuations and Business Administration). The basis for this will be the zero bond interest rates published by the Deutsche Bundesbank using the Svensson method. To smooth short-term market fluctuations, the average yields of the previous three months are used and the result rounded to 0.25 basis points.

The currently used value of the risk-free interest rate is 1.00 %. We use the historical market premium of 5.50 % as a reasonable expectation of a market premium. This is supported by historical analyses of stock market returns. The market premium reflects the percentage by which the equity market is expected to outperform low-risk government bonds.

According to the GBC estimation method, a beta of 2.13 is currently determined.

Using the assumptions made, the cost of equity is calculated at 12,7 % (beta multiplied by risk premium plus risk-free interest rate). Since we assume a sustainable weighting of the cost of equity of 100%, the weighted average cost of capital (WACC) is 12.7%.

We have valued the outstanding options and warrants according to Black Scholes and value them as a liability with a value of CAD 22.69 million. For this purpose, we have assumed the undiluted value of 358.29 million shares.

Evaluation result

Future cash flows are discounted on the basis of the entity approach. We have calculated the corresponding cost of capital (WACC) at 12.7 %. The resulting fair value per share at the end of fiscal 2021 corresponds to a target price of CAD 2.20 (USD 1.65; € 1.40).

CAD to USD Conversion: 1 CAD = 0.746983 USD (16.09.2019 - 15:35 UTC)

CAD to EUR Conversion: 1 CAD = 0.636171 EUR (16.09.2019 - 15:35 UTC)

DCF model

DynaCERT - Discounted Cashflow (DCF) model

Value driver of the DCF model after the estimate phase:

consistency - Phase	
Sales growth rate	20.5%
EBITDA-Margin	16.0%
Depreciation to fixed assets	8.5%
Working Capital to Sales ratio	10.0%

final - Phase	
Eternal growth rate	2.0%
Eternal EBITDA-Margin	15.8%
Eternal effective tax rate	15.0%

Three phases - Model:

Phase in m CAD	estimate			consistency					final
	FY 20e	FY 21e	FY 22e	FY 23e	FY 14e	FY 25e	FY 26e	FY 27e	Terminal value
Sales	32.00	200.00	350.00	421.75	508.21	612.39	737.93	889.21	
Sales changes	2905.7%	525.0%	75.0%	20.5%	20.5%	20.5%	20.5%	20.5%	2.0%
Sales to fixed assets	14.22	48.19	44.41	44.41	44.41	44.41	44.41	44.41	
EBITDA	-1.24	30.32	55.81	67.48	81.31	97.98	118.07	142.27	
EBITDA-Margin	-3.9%	15.2%	15.9%	16.0%	16.0%	16.0%	16.0%	16.0%	
EBITA	-1.34	30.02	55.31	66.81	80.51	97.01	116.90	140.86	
EBITA-Margin	-4.2%	15.0%	15.8%	15.8%	15.8%	15.8%	15.8%	15.8%	15.8%
Taxes on EBITA	0.00	-8.25	-8.30	-10.02	-12.08	-14.55	-17.53	-21.13	
Taxes to EBITA	0.0%	27.5%	15.0%	15.0%	15.0%	15.0%	15.0%	15.0%	15.0%
EBI (NOPLAT)	-1.34	21.76	47.01	56.79	68.43	82.46	99.36	119.73	
Return on capital	-0.50	5.12	3.32	1.73	1.32	1.32	1.32	1.32	112.1%
Working Capital (WC)	2.00	10.00	25.00	42.18	50.82	61.24	73.79	88.92	
WC to Sales	6.3%	5.0%	7.1%	10.0%	10.0%	10.0%	10.0%	10.0%	
Investment in WC	-0.68	-8.00	-15.00	-17.18	-8.65	-10.42	-12.55	-15.13	
Operating fixed assets (OAV)	2.25	4.15	7.88	9.50	11.44	13.79	16.62	20.02	
Depreciation on OAV	-0.10	-0.30	-0.50	-0.67	-0.81	-0.97	-1.17	-1.41	
Depreciation to OAV	4.4%	7.2%	6.3%	8.5%	8.5%	8.5%	8.5%	8.5%	
Investment in OAV	-0.99	-2.20	-4.23	-2.29	-2.75	-3.32	-4.00	-4.82	
Capital employed	4.25	14.15	32.88	51.67	62.26	75.03	90.41	108.94	
EBITDA	-1.24	30.32	55.81	67.48	81.31	97.98	118.07	142.27	
Taxes on EBITA	0.00	-8.25	-8.30	-10.02	-12.08	-14.55	-17.53	-21.13	
Total investment	-1.67	-10.20	-19.23	-19.46	-11.40	-13.74	-16.55	-19.95	
Investment in OAV	-0.99	-2.20	-4.23	-2.29	-2.75	-3.32	-4.00	-4.82	
Investment in WC	-0.68	-8.00	-15.00	-17.18	-8.65	-10.42	-12.55	-15.13	
Investment in Goodwill	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	
Free cash flows	-2.91	11.86	28.28	38.00	57.84	69.69	83.98	101.20	1119.44

Value operating business (due date)	702.51	779.98
Net present value explicit free cash flows	218.20	234.08
Net present value of terminal value	484.31	545.89
Net debt	2.44	-9.42
Value of equity	700.07	789.40
Minority interests	0.00	0.00
Value of share capital	700.07	789.40
Outstanding shares in m (fully diluted)	358.29	358.29
Fair value per share in CAD	1.95	2.20
Fair value per share in USD	1.46	1.65
Fair value per share in EUR	1.24	1.40

Cost of Capital:

Risk free rate	1.0%
Market risk premium	5.5%
Beta	2.13
Cost of Equity	12.7%
Target weight	100.0%
Cost of Debt	1.0%
Target weight	0.0%
Taxshield	1.8%
WACC	12.7%

Return on capital	WACC CAD				
	10.7%	11.7%	12.7%	13.7%	14.7%
110.1%	2.73	2.42	2.18	1.98	1.81
111.1%	2.75	2.44	2.19	1.99	1.82
112.1%	2.77	2.45	2.20	2.00	1.83
113.1%	2.78	2.47	2.22	2.01	1.85
114.1%	2.80	2.48	2.23	2.03	1.86

Return on capital	WACC EUR				
	10.7%	11.7%	12.7%	13.7%	14.7%
110.1%	1.74	1.54	1.38	1.26	1.15
111.1%	1.75	1.55	1.39	1.27	1.16
112.1%	1.76	1.56	1.40	1.27	1.17
113.1%	1.77	1.57	1.41	1.28	1.17
114.1%	1.78	1.58	1.42	1.29	1.18

APPENDIX

I.

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2. the research report is made available simultaneously to all investment service providers interested in it.

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BUY	The expected return, based on the calculated target price, including dividend payment within the corresponding time horizon is $\geq + 10\%$.
HOLD	The expected return, based on the calculated target price, including dividend payment within the corresponding time horizon is $> - 10\%$ and $< + 10\%$.
SELL	The expected return, based on the calculated target price, including dividend payment within the corresponding time horizon is $\leq - 10\%$.

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The GBC AG is currently represented by its board members Manuel Hölzle (Chairman) and Jörg Grunwald.

The analysts responsible for this analysis are

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