Crius Energy Trust.

Resuming Coverage

USGE Provides Enhanced Footprint, Diversification & Cross-Sell Potential

KWH.un (T)	Cdn$10.14
Stock Rating:	Outperform (Was Restricted)
Target:	Cdn$13.00 (Was Restricted)
Risk Rating:	Average (Was Restricted)
Est. Total Return	35.9%

Stock Data:	
Cash Yield	7.7%
Implied Price Return	28.2%
52-week High-Low	$11.32-$7.76
Bloomberg/Reuters:	KWH-U CN / KWH_u.TO

Forecasts (US$) FYE Mar. 31	2016a	2017e	2018e
Revenue (mln)	$744	$908	$1,066
EBITDA (mln)	$59.2	$84.2	$111.1
DCPS	$0.91	$1.02	$1.28
Dividend (C$)	$0.74	$0.78	$0.79
Payout	61%	58%	46%
DC Yield	8.9%	13.4%	16.8%
EV/EBITDA	5.4x	3.8x	4.8x
P/DCPS	8.4x	7.5x	6.0x

Financial Data (Pro-forma USGE):	
Basic Shares Outstanding (mln)	55.4
Market Capitalization (C$ mln)	$561.7
Net Debt (US$ mln)	$106.8
Enterprise Value (C$ mln)	$703.7
Net Debt to Capitalization	16%
Net Debt to 2018e EBITDA	1.0x

Industry Rating: Market Weight
(NBF Economics & Strategy Group)

Company Profile:
Crius Energy Trust is an independent energy retailer, offering electric, gas and solar solutions to over ~1.4 mln (post USGE acquisition) customers through an innovative family-of-brands strategy and multi-channel marketing approach.

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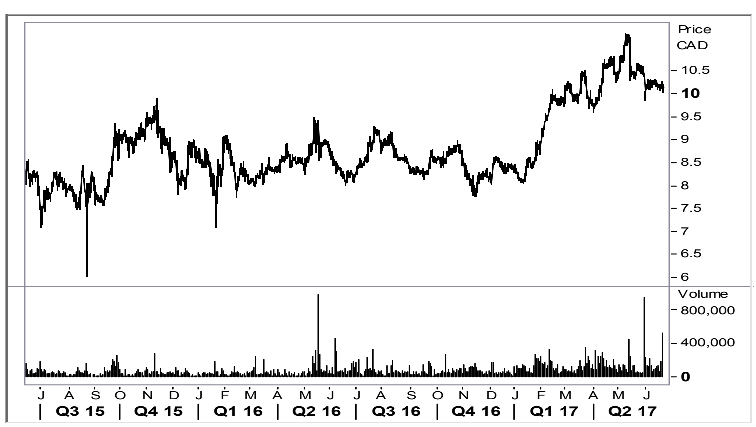
HIGHLIGHTS

- **Off restriction post financing**
We are resuming coverage following KWH's C$110 mln equity raise, with an additional ~C$16.5 mln of proceeds available should the over-allotment be exercised within 30 days (which we anticipate). KWH issued 11.2 mln units priced at $9.80/unit, reflecting a 28% increase and taking market cap to >$500 mln.
- **Set to acquire USGE early next month**
The C$110+ mln of proceeds are slated to partially fund the US$172.5 mln acquisition (which includes US$20 mln in working capital) of U.S. Gas & Electric (USGE), owned by private equity fund MVC Capital. The balance of the total purchase price is from US$47.5 mln of non-amortizing sellers' notes, US$30 mln in KWH units to USGE & US$20 mln drawn on the Macquarie credit facility. The Florida based energy retailer provides electricity and natural gas solutions to ~375k commercial and residential customers (RCE's) in 11 U.S. states and D.C. The transaction is scheduled to close July 5.
- **Multiple considerations support the acquisition**
Including: 1) grows KWH's RCE book +37% in predominately familiar markets, while expanding into new (Michigan, Kentucky); 2) higher quality customer profile, with USGE gross margin >US$200/RCE (KWH ~$160/RCE); 3) a complimentary sales mix that adds new distribution channels; 4) better customer mix, with natural gas increasing from ~6% to ~14% of the book; 5) leverage remains a comfortable ~1x net debt to '18e EBITDA (TSX diversified income peers averaging ~2.4x), with an est. >US$25 mln dry powder and positioned for a new expanded credit facility; 6) provides a greater footprint to cross-sell high the high IRR solar offering and leverage legacy exclusive channel relationships (i.e., Comcast); 7) The aggregate purchase price implies a favourable 4.7x LTM EBITDA multiple, below public peers and recent relevant transactions (typically 6x-9x); and 8) highly accretive, our '18e DCPU forecast increasing 20% to $1.28 (with add'l upside from likely synergies). This translates to a sub-50% payout ratio, further supporting our view that KWH has arguably the best income growth potential in our universe.
- **Target increased to $13 (from $12) & reiterate Outperform**

Stock Performance (Thomson)



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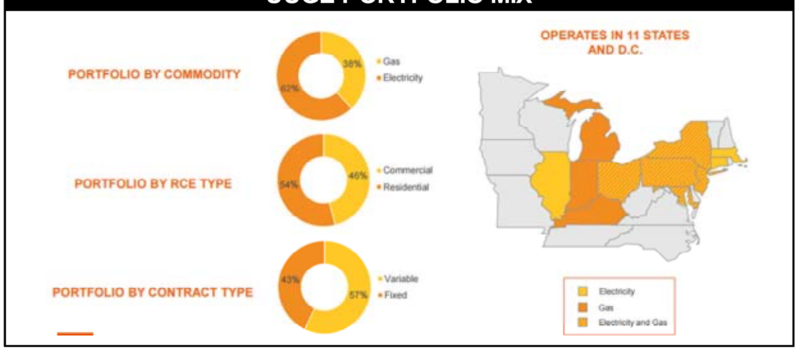
Transaction Summary

KWH is acquiring U.S. Gas & Electric (USGE), a retailer of electricity and natural gas since 2003 to commercial and residential customers in Connecticut, D.C, Illinois, Indiana, Kentucky, Maryland, Massachusetts, Michigan, New Jersey, New York, Ohio and Pennsylvania. USGE is to be acquired for and aggregate purchase price of US$152.5 mln plus ~US$20 mln in working capital, which implies a 4.7x LTM acquisition multiple. We highlight the implied transaction multiple represents a significant discount to comparable integrated retailers and industry transactions (typically 6x-9x). The transaction is expected to close early Q3/17 pending regulatory approval.

- **USGE acquisition adds scale and high-quality customers**
  Upon closing of the acquisition KWH will move into the top ten largest energy retailers in North America, increasing its customer count by ~375k to ~1.4 mln. The addition of USGE's customer book should improve overall gross margins per customer as KWH's existing gross margin per RCE of ~US$160 is well below USGE's LTM US$200 per RCE. Contributing to USGE's more favourable profitability is its larger residential customer base (54% residential / 46% commercial) which typically yields higher margins. Also supporting the enhanced profitability is USGE's customer base which is largely enrolled in purchase of receivables (POR) programs, which contractually requires investment-grade credit rated utility companies to purchase USGE's customer receivables. The process effectively high-grades USGE's receivables resulting in lower exposure to bad debts.

USGE PORTFOLIO MIX



Source: Company Reports, NBF

- **Improved direct consumer channels**
  USGE's traditional customer marketing channels compliment KWH's focus on more innovative business development and sales approaches (i.e., Viridian / commercial partnerships). Enhanced telemarketing, door to door sales and broker network expertise bolsters KWH's already high performing customer acquisition strategies.

- **Portfolio diversification**
  Comparable to KWH's portfolio, USGE's commodity portfolio is primarily composed of electricity (62% USGE exposure vs. 94% KWH legacy). However USGE's portfolio offers investor's significantly more exposure to natural gas given its 38% portfolio composition compared to just 6% for KWH's legacy portfolio. Pro-forma the acquisition, KWH's total natural gas exposure increases to ~14%, which we argue is positive given the diversification benefits reducing both commodity price and product concentration risks. In addition, 30% / 70% of KWH's pro-forma contracts will be variable / fixed compared to 20% / 80% previously, while its customer segmentation is largely unchanged at 62% residential and 38% commercial (previously 65% residential / 35% commercial).

- **Enhancing footprint in existing markets, entering two new states**
  There is significant geographic overlap between the USGE and KWH portfolios, with USGE currently operating in 10 of KWH's existing markets, while offering the company access to two new states, Michigan and Kentucky. In our view, the complimentary nature of both companies' sales practices (USGE more traditional, KWH more innovative), combined with USGE's proportionally larger natural gas operation and KWH's solar offering should generate synergies, cross-selling and organic growth opportunities, all while reducing competition.

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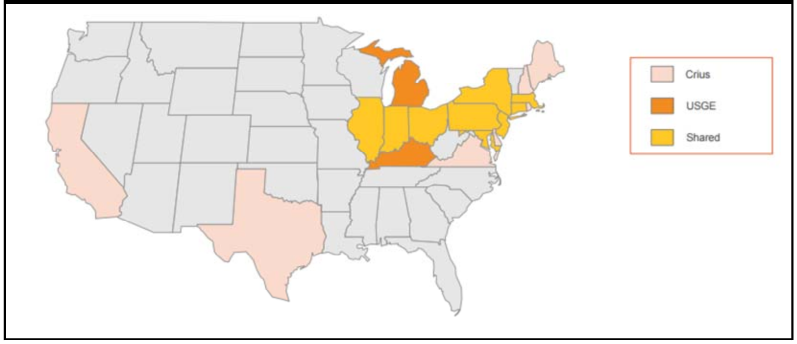
PRO-FORMA PORTFOLIO



Source: Company Reports, NBF

- **Ticks all the key boxes**
  Including: 1) highly accretive, our 2018e DCPU forecast increasing +20%, which assumes ~US$5 mln of synergies that we believe could total US$10+ mln over time as costs are rationalized and sales synergies exploited; 2) balance sheet health maintained, with net debt to 2018e EBITDA a comfortable ~1x; and 3) dry powder remains to finance near-term growth opportunities, we calculate US$25+ mln in available credit, but note that given KWH's aggressive growth in recent years it is well positioned to secure a larger / more attractive credit facility than the one it currently has with Macquarie.

Investment Summary

At 4.8x 2018e EV/EBITDA and 6x P/CF KWH trades at a sharp discount to all of its peer groups (TSX dividend equities, North American energy retailers), a gap we expect will continue to narrow as its unique combination of yield and growth are further demonstrated. The addition of USGE is both strategic and lucrative for investors, who we expect will be rewarded with ongoing dividend growth (+2%/Q since Q1/16) given a sub-50% payout ratio. Our target price increases to $13 (was $12 prior to restriction) which implies an unchanged ~5.75x 2018e EV/EBITDA valuation, and we reiterate an Outperform rating.

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