Hunting PLC

In-line FY23 update, further progress anticipated

10 January 2024

Good revenue progress, a strong EBITDA uplift (and margin expansion), an ungeared year-end balance sheet and the in-year launch of an ambitious 2030 strategy represents a healthy FY23 scorecard for Hunting. In addition, order book growth and unchanged management guidance positions the company well to achieve further progress. Delivery against the roadmap to 2030 – especially the development of non-oil and gas markets – will be keenly watched. Progress here can serve as a significant valuation driver, in our opinion.

Strong progress in FY23

While markets were not universally positive in FY23, strong performances from Hunting's OCTG, Advanced Manufacturing and Subsea Technologies product groups drove a c.28% group revenue uplift and, we believe, were the primary drivers behind a c.90% EBITDA increase (and a c.10.5% group margin). The implicit c.US$98m EBITDA is in the middle of the US$96m-100m guidance range which had itself been raised during the course of the year. A number of large contract awards announced at the end of FY22 and as FY23 progressed contributed meaningfully to the FY23 outturn. In addition, Hunting ended the year with a record US$575m order book (versus US$473m a year earlier).

Hunting's balance sheet is confirmed to be broadly funds neutral at the end of FY23 indicative, we believe, of good cash collection in H2/Q4 on an elevated revenue base. Together with further anticipated earnings progress in FY24 and FY25 feeding into positive cash generation, this provides a strong platform for prospective M&A activity and potential further earnings upside.

Valuation: Scope for rerating from strategic delivery

Hunting's share price has edged lower compared to when we initiated coverage on 8 November (versus FTSE All Share Index +c.4%). Noting that our existing FY24e EBITDA is slightly below maintained company guidance for the year, our estimates are unchanged at this stage. As a result, conventional valuation metrics have compressed slightly over the last two months and remain undemanding in the context of both immediate and longer-term growth targets. Previously identified peer group discounts of c 20-30% are unchanged.

Using the same hybrid PER and DCF analysis as before, our fair value per share estimate is also unchanged in US dollar terms but now translates to 407p, allowing for FX movements (ie £/US$1.269 now versus 1.23 previously) almost 50% higher than current levels.

Summary financials

Yr to December (US$m)	2021	2022	2023E	2024E	2025E
Revenue	521.6	725.8	948.3	1,033.4	1,115.7
EBITDA*	3.1	52.0	99.3	121.5	146.0
Pre-Tax Profit	(40.6)	10.2	51.0	76.9	102.6
EPS (US c)	(27.1)	4.7	21.8	32.3	43.7
DPS (US c)	8.0	9.0	10.0	11.0	12.0
Net cash / (debt)	103.5	20.6	(0.5)	34.4	78.8
P/E (x)	*n/m*	*73.7*	*16.0*	*10.8*	*8.0*
EV/EBITDA (x)	*151.6*	*10.6*	*5.8*	*4.4*	*3.4*
Dividend yield	*2.3%*	*2.6%*	*2.9%*	*3.2%*	*3.4%*

*Source: Company Annual Reports, Equity Development. £/US$1.27, *company basis*

Company Data

EPIC	HTG.L
Price (last close)	274p
52 weeks Hi/Lo	354p/190p
Market cap	£452m
ED Fair Value / share	407p
FY23e Net cash (debt)	(US$1m)
Average daily volume (3 months)	367k

NB all at £/US$ 1.27

Share Price, p

Source: ADVFN

Description

Hunting is a global engineering group that provides precision-manufactured equipment and premium services with a diverse product portfolio. The company has a global footprint from operations in 11 countries including 27 production locations and 13 distribution centres.

The energy industry accounted for c 92% of FY23 revenue while also serving non-oil & gas customers in the medical, aerospace, defence and space sectors. Hunting is seeking to grow rapidly in adjacent Energy Transition product sub-sectors as well as deepening its presence in other non-oil & gas ones.

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FY23 EBITDA meets raised guidance

When the H123 results were announced in August, management raised FY23 EBITDA guidance for the third time during the year and to US$96m-100m. Based on revenue and margin figures in the FY23 year-end update, the full year outturn appears to around the middle of this range. In addition, good cash collection in H2/Q4 has resulted in an effectively ungeared balance sheet at the year end, as expected. Moreover, with a record order book position at the year-end, company guidance for FY24e (ie EBITDA US$125-135m) has been maintained.

Healthy double-digit group revenue increase + c.330bp EBITDA margin uplift

Indicative FY23 group revenue is stated to be c.US$925m-930m range (versus ED estimate of US$948m) with an improved EBITDA margin of c.10.5% (ED estimate 10.5%). Together, at the revenue midpoint, this generates FY23 EBITDA of c.US$97.4m (ED estimate US$99.3m). On this basis, in year-on-year terms, group revenue and EBITDA are ahead by c.28% and c.88% respectively. The c.330bp EBITDA margin uplift is notable given a relatively subdued top line performance from the highest margin product group in the prior year. This suggests more general improvement elsewhere and a more rounded profit contribution overall.

Within the **Product Group** mix, four out of the five groups saw improved revenues in FY23 (Perforating Systems was the exception) and three of these are now achieving revenues in excess of the pre-COVID levels seen in FY19. (A short description of each product group is shown in the Company Overview summary on p4.)

Oil Country Tubular Goods, or OCTG (FY23 revenue + c.53% compared to FY22): A confirmed uptick from FY22 was achieved, noting also that y-o-y progress was greater in H1 (+95%) compared to H2 (+ c 23%). This partly reflects a higher base comparator in H222 after three halves of sequential progress and, relatedly, the pattern of shipments of larger orders (eg CNOOC award in August 2022). Implicitly, underlying activity levels excluding the CNOOC order delivery continued to rise throughout the year. We believe that shipments under the Cairn Oil & Gas/Vedanta contract contributed to this profile.

Perforating Systems (- c.3 to 4%): Historically, this product group's revenues have substantially been generated in North America. Headline revenue declined by c.11% in H2 after a 4% uplift in H1; in the context of a lower US onshore rig count (down approaching 20% over 2023 as a whole) this performance appears to be relatively good. This perhaps reflects some share gain but also a more stable Canadian rig count and a stated increase in international sales (not quantified). We also note that the US rig count was stable to slightly better from early November lows to the year end.

Advanced Manufacturing (+ c.45%): Increased activity levels seen in H1 were sustained in value terms in H2, representing a strong y-o-y revenue uplift in both periods (H1 +56%, H2 +c.36%). This product group generates the highest proportion of non-oil and gas revenue currently (ie 37% of FY22 sales) and winning programme positions for precision machined parts (eg in aerospace, defence and medical applications) is a key growth driver here. We believe that the proportion of non-oil and gas revenue will have increased in FY23.

Subsea Technologies (+ c.40%): Strong momentum in Subsea is confirmed, with a further acceleration in revenue growth in H2 after +20% in H1. Having secured orders on offshore projects in Guyana, Brazil and, latterly, the Black Sea, the revenue profile reflects the pull-through of related shipments. Interestingly, all three primary lines – couplings, stress joints and, more recently, flow access modules - have all seen increases in product demand.

Other Manufacturing (+c.5%): Some topline progress was made in the year though this was all generated in the first half. The quieter H2 trading period probably reflected the same US rig count effect as seen in Perforating Systems, partly offset by international sales progress.

Order book growth supports unchanged management guidance

Group order book development continued to a record c.US$575m level at the end of FY23, compared to US$473m a year earlier (of which c.85% was expected to be delivered in 2023). Typically, the OCTG, Advanced Manufacturing and Subsea Technologies' product groups have longer manufacturing lead times and order books. (Perforating Systems and Other Manufacturing tend to have less forward visibility, being more sensitive to well activity levels with orders serviced from inventory via a distribution network to respond to shorter demand cycles.)

Given that the group order book stood at US$511m at the end of September. A US$59m titanium stress joint order for deployment in South America announced in October effectively accounts for the majority of the net c US$64m order book uplift in Q4. This suggests that underlying order intake elsewhere in the group remained strong during the period, with a book to bill at or marginally above c 1x. As Hunting enters FY24, management guidance is unchanged, namely:

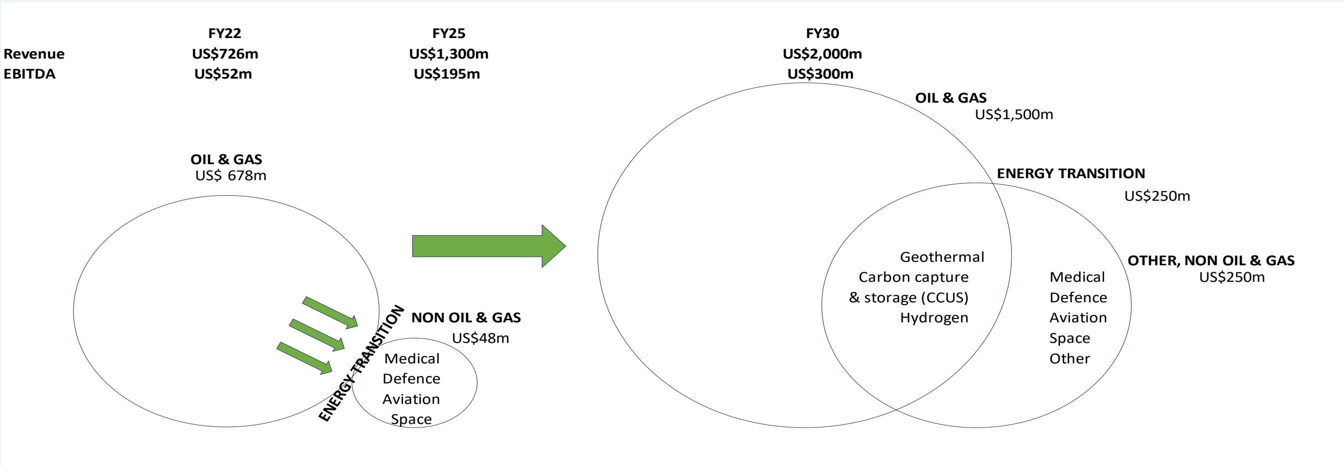
- **FY24e**: EBITDA US$125m-135m
- **FY25e:** 14-16% EBITDA margin

Noting that our existing projections (ie FY24e EBITDA US$121.5m and FY25e EBITDA margin 13.1%) are slightly below the above guidance, we are making no change to estimates at this stage. We will review estimates and roll out to FY26e when FY23 results are published on 29 February.

2030 Strategy: bigger and broader

In September, Hunting presented an ambitious strategy with explicit financial targets to raise group FY22 revenues **by almost 2.8 times** to c. US$2bn per annum by 2030, with EBITDA increasing almost sixfold to c. US$300m p.a. over the same timeframe. Continuing improvement in underlying energy demand is anticipated to provide a favourable backdrop for the oil and gas sector. In addition, Hunting is targeting a significant uplift in non-oil and gas revenue from c. 6% of FY22 revenue to c. 25% by FY30, with half of this to come from Energy Transition sector exposure. The simple graphic below summarises the financial and sector targets of the 2030 strategy.

Hunting: 2023-2030 strategic growth targets



Source: Company, Equity Development. NB Chart illustrative, not to scale; segment revenue (Oil & gas, Energy Transition, Other non-oil & gas) shown in chart

As far as FY23 trading is concerned, management notes that non-oil and gas represented c 8% of group revenues in the year; equivalent to c.US$73m on our estimates. This represents an increase of over 50% y-o-y and infers that H1 and H2 revenues were comparable following a strong sequential uplift in H123. We expect Energy Transition exposure to gain a progressive higher profile going forward as part of Hunting's strategic growth targets.

Company Overview

Hunting has a leading presence in core upstream oil and gas field activities built upon a diverse, technical product portfolio. Over time, the company has strengthened its position by acquiring complementary businesses and innovative product development. It is well placed operationally to meet strengthening demand in its traditional sectors and to penetrate the nascent Energy Transition sub-sectors.

Hunting comprises five Product Groups:

Perforating Systems (**35%** of FY22 revenue): Used in the well completion stage to penetrate installed downhole tubing and casing to access reservoirs of oil and gas held within adjacent geological formations. Perforating Systems carry and direct explosive charges and, in broad terms, comprise housings, detonating cord, detonators and energetics. Hunting manufactures component parts, pre-loaded guns and integrated gun systems as well as downhole measurement instrumentation and wireline accessories. Primarily used in onshore and especially shale rig applications.

Oil Country Tubular Goods or OCTG (**36%**): Generic term for piping and associated fittings used in well bore drilling, casing and tubing, typically formed from high performance steel alloy materials. Hunting provides proprietary precision threading services (ie machining to apply threads) to piping, couplings, connections and related accessories enabling pipe sections to be joined together and extend to the length of the wellhole. Hunting has its own proprietary families or premium connections and has operations in North America, EMEA and Asia-Pacific to serve energy and geothermal markets globally.

Subsea Technologies (**9%**): This product grouping addresses the offshore and deepwater floating, production, storage and offloading (FPSO) system market. Reported separately for the first time in FY23 (previously included in the North America region), it comprises three acquired, independent operating companies. The product portfolio includes hydraulic control valves and seal couplings (National Couplings), titanium and steel stress joints for risers connecting subsea flowlines to FPSOs (RTI/Spring) and modular production system technology for enabling efficient subsea wellhead flow access and intervention (Enpro).

Advanced Manufacturing (**10%**): In the oil and gas segment, operations in this product group are largely related to downhole measurement tool (MWD – measuring while drilling, LWD – logging while drilling) equipment. They provide specialist, high precision, complex machined metal components using a range of processes and coatings as well as electronic printed circuit boards, power supplies and systems integration for harsh environment applications. Additionally, c. 37% of FY22 revenue was generated in non-oil and gas segments, with products and services also supplied to aerospace and defence, power generation, space and medical equipment customers in the period.

Other Manufacturing (**10%**): Downhole Well Intervention tool components, equipment and services account for around half of this product group's revenues, typically used on either slickline (single strand) or E-line (electrical power and data transmission) cables. Other product categories include hollow tube and MWD consumable components. A third revenue stream, organic oil recovery (using chemical formulations to enhance well yield) is being developed via a collaboration agreement.

Financials Summary

INCOME STATEMENT										
Year End: December	**US$m**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023E**	**2024E**	**2025E**
				IFRS16	IFRS16	IFRS16	IFRS16	IFRS16	IFRS16	IFRS16
Revenue		**724.9**	**911.4**	**960.0**	**626.0**	**521.6**	**725.8**	**948.3**	**1,033.4**	**1,115.7**
Gross Profit		175.4	275.1	266.4	124.8	100.6	171.4	230.0	255.8	281.7
EBITDA - ED*		68.6	155.5	136.0	23.4	1.5	52.7	97.1	119.3	143.8
EBITDA - HTG		56.0	142.3	139.7	26.1	3.1	52.0	99.3	121.5	146.0
EBIT - HTG norm		**14.3**	**104.7**	**94.3**	**(16.4)**	**(35.1)**	**14.6**	**56.9**	**80.0**	**104.0**
Net Bank Interest		(0.7)	(1.0)	(0.9)	(1.1)	0.3	0.4	(4.0)	(3.9)	(3.4)
IFRS16 Interest				(2.2)	(1.9)	(1.5)	(1.2)	(1.2)	(1.2)	(1.2)
Other financial		(0.8)	0.3	1.9	0.0	(0.8)	(0.9)	(1.5)	(1.5)	(1.5)
Associates/JVs		(1.3)	0.0	0.0	0.0	(3.5)	(2.7)	0.8	3.5	4.7
Profit Before Tax (HTG norm)		**11.5**	**104.0**	**93.1**	**(19.4)**	**(40.6)**	**10.2**	**51.0**	**76.9**	**102.6**
Intangible Amortisation		(29.1)	(29.3)	(28.5)	(17.3)	(7.0)	0.0	0.0	0.0	0.0
Other Non-Underlying Items		(10.0)	0.0	(19.0)	(186.3)	(37.9)	(12.6)	0.0	0.0	0.0
Profit Before Tax (reported)		**(27.6)**	**74.7**	**45.6**	**(223.0)**	**(85.5)**	**(2.4)**	**51.0**	**76.9**	**102.6**
Tax		(1.0)	11.0	(4.2)	(15.2)	(4.2)	(1.3)	(12.5)	(18.4)	(24.5)
Other		2.5	3.6	(1.7)	3.5	3.9	(0.9)	(2.0)	(4.5)	(5.0)
Profit After Tax (reported)		(26.1)	89.3	39.7	(234.7)	(85.8)	(4.6)	36.4	54.0	73.1
EPS FD - HTG norm (p)		**8.0**	**49.6**	**43.9**	**(10.0)**	**(27.1)**	**4.7**	**21.8**	**32.3**	**43.7**
EPS FD - reported (p)		**(16.0)**	**52.3**	**23.5**	**(143.1)**	**(53.2)**	**(2.8)**	**21.8**	**32.3**	**43.7**
Dividend per share (p)		**0.0**	**9.0**	**5.0**	**9.0**	**8.0**	**9.0**	**10.0**	**11.0**	**12.0**
Shares – Basic Weighted Avge (m)		163.3	164.1	165.2	163.9	161.2	160.3	159.0	159.0	159.0
Shares - Period End (m)		164.2	165.1	166.9	164.9	164.9	164.9	164.9	164.9	164.9
Margins (%)										
Gross Profit		**24.2**	**30.2**	**27.8**	**19.9**	**19.3**	**23.6**	**24.3**	**24.8**	**25.3**
EBITDA - ED		9.5	17.1	14.2	3.7	0.3	7.3	10.2	11.5	12.9
EBITDA - HTG		7.8	15.6	14.6	4.3	0.6	7.2	10.5	11.8	13.1
EBIT HTG norm		**2.0**	**11.5**	**9.8**	**(2.6)**	**(6.7)**	**2.0**	**6.0**	**7.7**	**9.3**

Source: Company, Equity Development

CASH FLOW STATEMENT										
Year End: December	**US$m**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023E**	**2024E**	**2025E**
				IFRS16	IFRS16	IFRS16	IFRS16	IFRS16	IFRS16	IFRS16
EBITDA - HTG (pre SBP)		67.9	155.5	148.8	35.1	12.3	61.9	109.3	131.5	156.0
Change in working capital		(39.9)	(96.6)	7.6	38.8	22.8	(86.6)	(47.2)	(9.6)	(18.7)
Other		11.3	(3.6)	(11.5)	(17.9)	(7.1)	(8.2)	0.6	0.0	0.0
Operating Cash Flow		**39.3**	**55.3**	**144.9**	**56.0**	**28.0**	**(32.9)**	**62.6**	**121.9**	**137.3**
Tax paid		6.5	(2.6)	(7.7)	(5.0)	0.6	(3.9)	(10.0)	(14.7)	(19.6)
Investing Activities		**(10.2)**	**(6.7)**	**(46.6)**	**(46.6)**	**9.2**	**(11.7)**	**(34.7)**	**(40.0)**	**(40.0)**
Associates & JV income		0.0	0.0	0.0	(0.9)	0.0	0.0	0.6	0.0	0.0
Tangible Fixed Assets purchased		(9.1)	(24.3)	(30.4)	(11.7)	(5.7)	(15.9)	(25.0)	(35.0)	(35.0)
Tangible Fixed Assets disposed		1.8	12.5	0.9	2.0	2.2	6.6	1.3	0.0	0.0
Intangibles		(5.5)	(6.6)	(10.2)	(4.3)	(2.7)	(5.6)	(10.0)	(5.0)	(5.0)
Acquisition consideration		0.0	0.0	(12.5)	(32.8)	0.0	0.0	0.0	0.0	0.0
Disposal proceeds		0.6	0.0	3.0	0.6	31.5	0.0	0.0	0.0	0.0
Other business investments		2.0	11.7	2.6	0.5	(16.1)	3.2	(1.6)	0.0	0.0
Financing Activities		**(2.3)**	**(14.0)**	**(31.2)**	**(33.2)**	**(31.4)**	**(30.0)**	**(38.8)**	**(32.2)**	**(33.4)**
Net finance income (cost)		(2.4)	(2.0)	0.1	(0.3)	(0.4)	(2.9)	(4.0)	(3.9)	(3.4)
IFRS16 lease payments				(10.6)	(10.4)	(10.6)	(8.0)	(11.0)	(11.0)	(11.0)
Equity Issued		0.1	(5.4)	(4.1)	(14.3)	(7.6)	(7.7)	(8.5)	0.0	0.0
Dividends paid		0.0	(6.6)	(16.6)	(8.2)	(12.8)	(13.6)	(15.3)	(17.3)	(19.0)
Other		0.0	0.0	0.0	0.0	0.0	2.2	0.0	0.0	0.0
Net Cash Flow		**33.3**	**32.0**	**59.4**	**(28.8)**	**6.4**	**(78.5)**	**(20.8)**	**35.0**	**44.3**
Opening net cash/(debt) - pre IFRS16		**(2.7)**	**30.4**	**61.3**	**123.1**	**97.8**	**103.5**	**20.6**	**(0.5)**	**34.4**
Change in Net Cash		33.3	32.0	59.4	(28.8)	6.4	(78.5)	(20.8)	35.0	44.3
Other		(0.2)	(1.1)	2.4	3.5	(0.7)	(4.4)	(0.3)	(0.0)	0.0
Closing net cash/(debt) - pre IFRS16		**30.4**	**61.3**	**123.1**	**97.8**	**103.5**	**20.6**	**(0.5)**	**34.4**	**78.8**
IFRS16 lease liabilities				**(45.2)**	**(40.3)**	**(31.8)**	**(30.6)**	**(26.7)**	**(26.7)**	**(26.7)**

Source: Company, Equity Development

BALANCE SHEET										
Year End: December	**US$m**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023E**	**2024E**	**2025E**
				IFRS16	IFRS16	IFRS16	IFRS16	IFRS16	IFRS16	IFRS16
Non-Current Assets		**749.0**	**721.8**	**735.0**	**581.1**	**535.7**	**515.3**	**514.4**	**523.4**	**533.0**
Intangible Assets - Goodwill		230.3	229.9	230.2	164.2	164.1	155.5	154.4	154.4	154.4
Intangible Assets - Other		125.4	99.8	78.5	42.9	36.2	35.7	40.4	39.4	38.4
Tangible Assets - Owned		383.3	360.2	354.7	307.1	274.4	256.7	254.1	260.6	266.6
Tangible Assets - RoU		0.0	0.0	36.7	29.8	24.7	26.0	23.4	23.4	23.4
Other Fixed Assets		10.0	31.9	34.9	37.1	36.3	41.4	42.1	45.6	50.2
Current Assets		**533.2**	**647.2**	**682.1**	**532.4**	**475.9**	**534.0**	**665.0**	**716.8**	**786.6**
Inventory		281.0	348.2	350.8	288.4	204.4	272.1	318.1	324.3	328.8
Trade Receivables		161.0	201.7	176.1	119.9	137.2	190.2	228.5	239.0	260.0
Other Debtors		54.8	29.4	26.6	21.2	25.9	42.3	26.9	26.9	26.9
Cash		36.4	67.9	128.6	102.9	108.4	29.4	91.6	126.5	170.9
Current Liabilities		**(144.5)**	**(159.5)**	**(145.3)**	**(84.7)**	**(99.0)**	**(163.8)**	**(271.9)**	**(287.7)**	**(303.2)**
Trade Payables		(47.3)	(62.3)	(56.3)	(26.4)	(40.5)	(66.8)	(86.6)	(93.7)	(100.5)
Other Creditors		(95.1)	(94.5)	(77.6)	(46.9)	(48.6)	(83.0)	(89.1)	(97.8)	(106.5)
IFRS16 Lease Liabilities		0.0	0.0	(9.8)	(10.2)	(8.9)	(9.1)	(8.0)	(8.0)	(8.0)
Short-term Borrowings		(2.1)	(2.7)	(1.6)	(1.2)	(1.0)	(4.9)	(88.2)	(88.2)	(88.2)
Non-Current Liabilities		**(25.6)**	**(18.4)**	**(48.0)**	**(52.2)**	**(41.3)**	**(39.3)**	**(38.5)**	**(42.2)**	**(47.1)**
Long-term Borrowings		(3.9)	(3.9)	(3.9)	(3.9)	(3.9)	(3.9)	(3.9)	(3.9)	(3.9)
IFRS16 Lease Liabilities		0.0	0.0	(35.4)	(30.1)	(22.9)	(21.5)	(18.7)	(18.7)	(18.7)
Other Long-term Liabilities		(21.7)	(14.5)	(8.7)	(18.2)	(14.5)	(13.9)	(15.9)	(19.6)	(24.5)
Net Assets		**1,112.1**	**1,191.1**	**1,223.8**	**976.6**	**871.3**	**846.2**	**869.0**	**910.2**	**969.3**

Source: Company, Equity Development

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