

“Minimal” exposure to Carillion

17 January 2018

Carillion’s high profile bankruptcy on Monday has certainly hit the headlines. Politicians on both sides of the aisle have been throwing stones at one another. An official investigation into the fiasco has been announced. But perhaps worst of all, the future of 10,000s of hard-working employees, pensioners and businesses (eg Balfour Beatty, Speedy Hire, Galliford Try, etc) have been affected.

However, contrary to yesterday’s 10%+ plunge in the stockprice, Gattaca said this morning that its **net balance sheet exposure to Carillion was “less than £100,000”** – with **existing contracts contributing Net Fee Income of around £0.5m pa.**

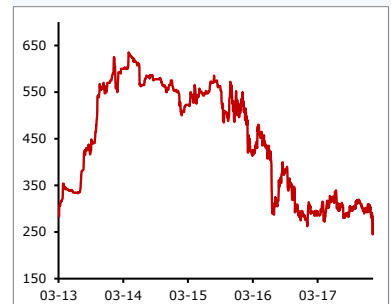
To us, given Gattaca is forecast to deliver FY18 NFI of £79.3m (£74.7m LY), then **this is not material**. Sure, it’s something to watch, but **management have been carefully monitoring the situation for some time**, and accordingly arranged credit insurance to cover any bad debts. Moreover they have been “*actively engaging with the relevant Carillion counterparties to ascertain how to support the related underlying projects*” in order to ensure continuity of service.

Consequently, **we make no change to our numbers or 380p/share valuation**, and in fact have been impressed by the Board’s risk management strategies and prompt actions. Indeed we look forward to the H1’18 pre-close trading statement on 8th February, where we expect to hear news of a gradually improving demand picture - led by continued strength in International and UK Engineering, alongside further recovery in UK Technology.

Company Data

EPIC	AIM:GATC
Price (last close)	250p
52 week Hi/Lo	340p/225p
Market cap	£79m
ED Valuation	380p/share

Share Price, p



Source: Yahoo.co.uk

Description

Gattaca is the UK's #1 specialist engineering and #5 technology recruitment agency, providing contract, temporary and permanent staff (Source: Recruitment International). It derives 21% of NFI overseas (excluding international placements supplied from the UK), and circa 75% from temporary contractors (9,500 on assignment), with the remaining 25% coming from permanents.

The global engineering and technology recruitment markets are valued at circa \$26bn and \$57bn respectively (Source: Staffing Industry Analysts) – offering substantial long term potential.

Next News: Update 8th February

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Summary financials

Gattaca (continuing operations) (July yearend)	2014 Act £'000s	2015 Act £'000s	2016 Act £'000s	2017 Act £'000s	2018 Est £'000s	2019 Est £'000s	2020 Est £'000s
Turnover (continuing activities)	451,591	495,682	616,832	642,365	680,173	701,229	729,955
% growth	10.4%	9.8%	24.4%	4.1%	5.9%	3.1%	4.1%
Net Fee Income (NFI) : Gross profit							
UK Engineering	27,077	37,853	40,865	43,080	47,148	48,562	50,505
UK Technology	17,905	14,605	17,413	16,178	16,016	16,497	17,157
International			14,109	15,450	16,174	16,821	17,662
Total	44,982	52,458	72,387	74,708	79,338	81,880	85,323
NFI growth rate							
UK Engineering	13.2%	39.8%	8.0%	5.4%	9.4%	3.0%	4.0%
UK Technology	23.9%	-18.4%	19.2%	-7.1%	-1.0%	3.0%	4.0%
International				9.5%	4.7%	4.0%	5.0%
Total NFI growth rate	17.2%	16.6%	38.0%	3.2%	6.2%	3.2%	4.2%
NFI margin	10.0%	10.6%	11.7%	11.6%	11.7%	11.7%	11.7%
UK Engineering	10,548	13,105	23,126	23,758	24,849	25,656	26,763
UK Technology	3,073	4,242	8,229	7,061	7,367	7,753	8,235
International			6,868	5,619	6,470	7,065	7,771
Central overheads			-16,726	-19,050	-19,611	-20,218	-21,046
Adjusted EBIT	13,621	17,347	21,497	17,388	19,076	20,256	21,723
Adj NFI / EBITA conversion	30.3%	33.1%	29.7%	23.3%	24.0%	24.7%	25.5%
Net interest	-1,015	-1,074	-1,076	-1,196	-1,296	-1,346	-1,296
Adjusted PBT	12,606	16,273	20,421	16,192	17,780	18,910	20,427
Adjusted diluted EPS (p) - excl. minorities	37.1	43.8	44.1	33.8	36.0	39.1	41.7
Adjusted EPS growth rate	17.5%	18.2%	0.5%	-23.4%	6.5%	8.7%	6.7%
Dividend (p)	20.0	22.0	23.0	23.0	23.0	23.0	23.0
Dividend yield	8.0%	8.8%	9.2%	9.2%	9.2%	9.2%	9.2%
Dividend cover	1.9	2.0	1.9	1.5	1.6	1.7	1.8
Valuation benchmarks							
P/E ratio (diluted)	6.7	5.7	5.7	7.4	6.9	6.4	6.0
EV/NFI	2.7	2.3	1.7	1.6	1.5	1.5	1.4
EV/EBITDA (diluted)	8.9	7.0	5.7	7.0	6.4	6.0	5.6
PEG ratio	0.38	0.31	10.89	-0.32	1.06	0.74	0.89
Adjusted corporate tax rate	-23.3%	-14.5%	-30.9%	-31.4%	-31.9%	-32.4%	-32.9%
Adj ROACE	30.6%	21.5%	19.7%	15.6%	16.7%	17.0%	17.3%
EBITDA drop through rate as % NFI	48.9%	53.8%	21.3%	-186.7%	37.0%	47.6%	43.7%
Cash conversion (EBITDA - Capex - W/Cap)/EBIT	103%	109%	93%	68%	70%	79%	76%
Unlevered/adj. free cashflow yield	4.5%	13.5%	12.9%	5.5%	6.3%	8.1%	8.0%
Net cash/(debt)	-3,109	-33,644	-25,013	-40,288	-41,949	-39,455	-37,050
Net debt : EBITDA	0.22	1.83	1.11	2.20	2.10	1.86	1.63
Diluted sharecount (Adj for 2015)	26,073	31,730	32,040	32,392	32,549	32,707	32,866
Shareprice (p)	250						

Source: Equity Development estimates, Company historic data

Key risks

- Economic downturn affecting engineering and technology recruitment.
- Greater competition, especially from new technology platforms (eg LinkedIn, Monster).
- Overseas expansion along with foreign exchange fluctuations.
- Acquisition integration, albeit management have a decent batting average.
- Consolidation of customer base (eg takeovers of Atkins:SNC-Lavalin and CH2M:Jacobs).
- Political interference which could impact UK infrastructure spend (eg cancellation of rail electrification projects).



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