

Highly synergistic £15m acquisition

Patience is a virtue, and an essential ingredient for M&A. Carefully surveying the environment, not swinging for every ball, nurturing the best ideas and thoroughly doing the due diligence. Before finally putting pen to paper, and signing on the dotted line.

Likewise this morning, after waiting 18 months for the right deal, MPAC announced that it had purchased [Lambert Automation Limited](#) for £15.0m (excluding a 3 year £2.5m earnout). To us, **this strategic acquisition is synergistic, relatively low risk** (re similar businesses) **and value accretive**. Not only from the perspective of being **earnings enhancing**, but also more importantly delivering RoIs significantly above the enlarged group's cost of capital.

Nice size, perfect fit and at a keen price

Here, Lambert employs circa 160 staff, is HQ'd in Tadcaster (North Yorkshire) and is one of the country's leading designers, manufacturers and project managers of bespoke automated production line equipment (see below). Supporting MPAC's key medical, healthcare, food and FMCG verticals (eg Procter & Gamble, Philips and ConvaTec), alongside offering back office, property, supply chain, procurement and overhead savings, as the 2 firms are integrated over the next 12-24 months.

Picture of a Lambert high speed production machine



Source: Company

Substantial client benefits to boot

What's more, there are **considerable top line synergies too**. X-selling products/services into each other's extensive customer lists. Further internationalising Lambert's revenues (23% UK) over MPAC's broader geographical footprint, especially in North America, Europe and AsiaPac.

And lastly, offering clients **total 'end-to-end' production/packaging solutions from design & build, through to installation & aftermarket support**. Duly simplifying their entire procurement, commissioning and operating processes, coupled with reducing 'whole of life' costs.

1st May 2019

Company Data

EPIC	AIM:MPAC
Price (last close)	135p
52 week Hi/Lo	230p/109p
Market cap	£27.2m
Net cash (Est Dec'19)	£9.0m
Share count (incl Treasury)	20.172m
ED valuation/ share	245p
Avg. daily volume	25,000

Share Price, p



Source: Web Financial

Description

MPAC is a specialist provider of high speed packaging machines (79% of sales) and complementary services (21%, eg spares/maintenance) with c. 350 staff. The group (80% non UK), encompasses the design/manufacture of cartoning equipment, case packers, end-of-line and robotic solutions, as well as undertaking turnkey projects involving the design/integration of packaging systems. Here it has sites in Canada and the Netherlands, plus service engineers based throughout the world.

In Coventry (UK), the firm develops innovative technology and associated production/packaging machinery. Core verticals are Pharmaceutical (10% sales), Healthcare (35%) and Food/Beverage (55%), supporting the likes of Nestlé, GSK, AstraZeneca, Unilever, Kellogg's, Diageo, Ferrero, Hollister and CooperVision.

Next news: H1'19 trading update July

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Complementary skillsets, ethos and aspirations

Similarly, there should be scope to leverage both organisation's design, consultancy & turn-key teams across a much wider base. Therefore enhancing resource management, engineer utilisation and customer service.

So what about the numbers? Well for the period 2016-18, Lambert posted average annualised turnover, EBITDA & EBIT of £20.6m, £1.8m & £1.0m respectively (see below). Moreover, in 2018 the company registered its 2nd best ever level of bookings at £24.5m, ending December with a bumper backlog.

Audited headline results for Lambert Automation Ltd

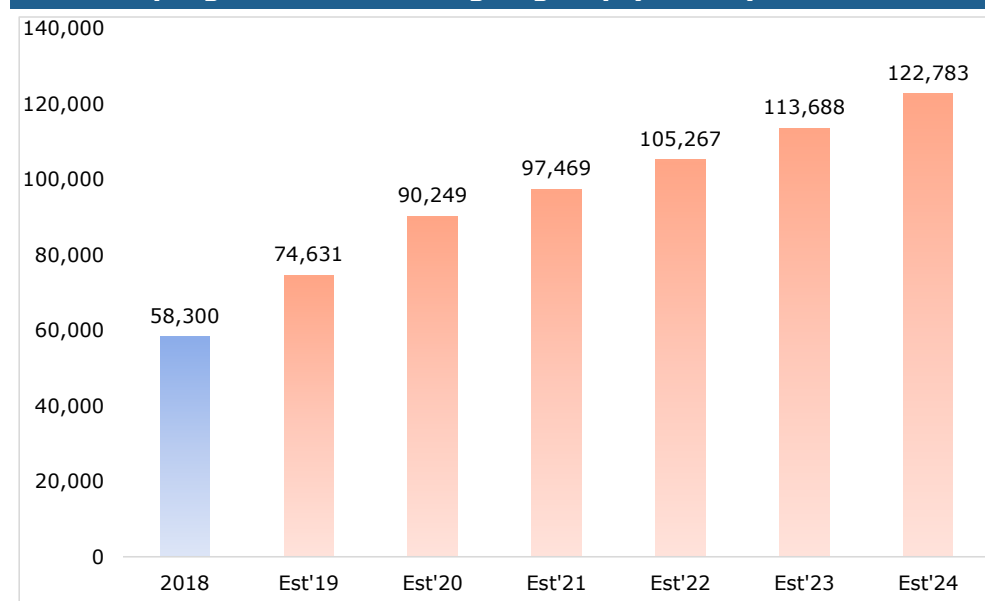
£'000s	2016	2017	2018	3 year average	Multiple at £15m	Sector benchmarks
Revenues	22,663	21,158	17,925	20,582	0.73	1.76
Gross profit	8,990	8,704	7,229	8,308		
% margin	39.7%	41.1%	40.3%	40.4%		
EBITDA	2,066	2,240	1,022	1,776	8.4	10.6
% margin	9.1%	10.6%	5.7%	8.6%		
Adjusted EBIT	1,220	1,416	234	957	15.7	12.9
% margin	5.4%	6.7%	1.3%	4.6%		

Source: Equity Development

Consequently using the above figures, the £15m price-tag equates to average 3 year trailing EV/sales, EV/EBITDA & EV/EBIT multiples of 0.73x, 8.4x and 15.77x, vs sector benchmarks of 1.77x, 10.5x and 13.1x.

Additionally, the transaction is "***immediately materially earnings enhancing***" and comparatively low risk, in light of the Board's prior knowledge of Lambert, alongside the complementary **cultural, skillset and genetic fit**. Thus enabling the group to invest more in next generation technology, product-development and bolstering its 'competitive moat'.

Revenue progression for enlarged group (£'000s)

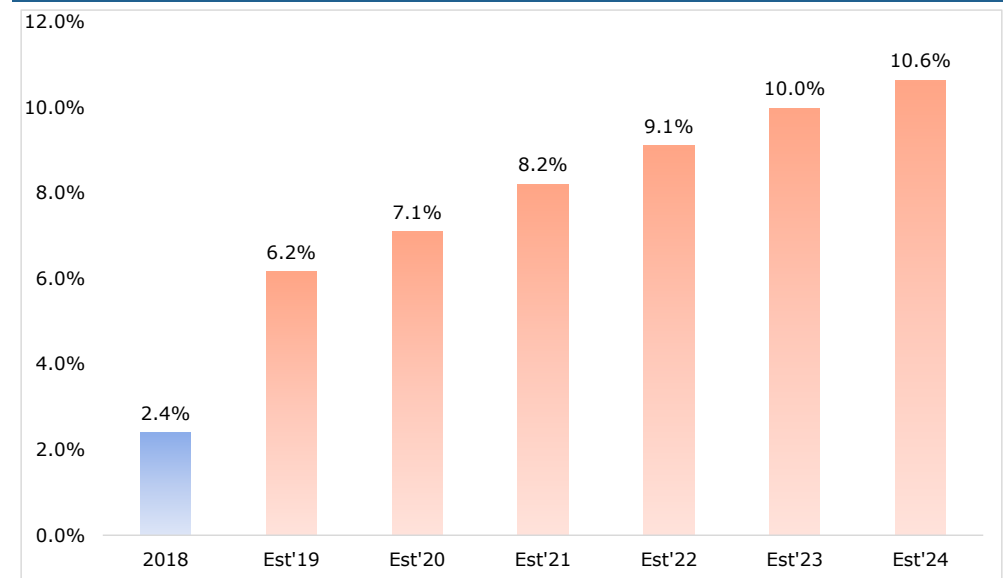


Source: Equity Development

Substantial economies of scale

Clearly all of this won't happen overnight. Yet push the clock forward and we are confident that ultimately across the economic cycle, MPAC will be able to grow LFL sales at least in the high single digits, and importantly realise adjusted EBIT margins of >10% (see below).

Higher and more predictable EBIT margins anticipated



Source: Equity Development

Plus, after baking in a realistic level of productivity gains, **there should be no reason why the acquisition cannot achieve a RoI of above 12%**. Indeed, according to our forecasts by 2021, Lambert will have driven an incremental £2.5m EBIT increase – equivalent to a healthy RoI of 16.7%.

Continuity should ensure smooth integration

Going forward, 3 of Lambert's existing shareholders, including Warren Lambert, Managing Director, will remain in place to ensure a smooth handover, and the transaction's strategic benefits are attained.

CEO Tony Steels, commenting: ***"Lambert is a high-quality business with proven performance and long-standing embedded relationships with global blue-chip customers. Clear synergies exist in the market, technologies and supply chain which will provide our customers and potential new customers even greater confidence in the delivery of complete turn-key packaging solutions. Lambert entered 2019 with a significantly higher order book than the previous year and I am excited about the potential of the combined business and the momentum it brings to the fulfilment of our strategic plans."***

Trading on track with 2019 expectations

Lastly, ahead of tomorrow's AGM, **results in the period Jan-April has been "in line with expectations"**. Here, **order intake and RFP activity remains strong**, whilst the **backlog is significantly above last year**. Additionally, extra cost savings have been realised following the restructuring exercise completed in H2'18.

From a macro perspective, we don't think the global economy is about to fall off a cliff either, regardless of investor fears over trade tariffs, Brexit and/or a slowdown in Europe/China. In fact if anything, we suspect global monetary policy will have to stay accommodative in order to neutralise the threat of deflation. Hence, keeping the consumer and GDP in positive territory.

Tony Steels adding ***"I am pleased to report good progress in the trading performance for 2019, of the existing business, supported by growth in order intake and sales over the prior year in both equipment and services backed by a strong orderbook, good levels of quote activity and prospects."***

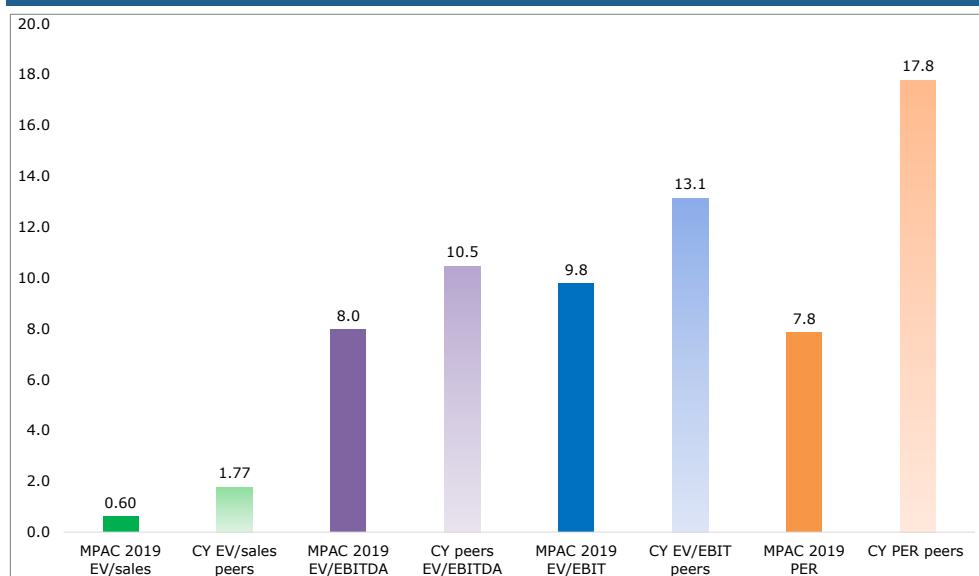
The Group has continued the momentum from H2'18 into the start of 2019 and I am confident that we will be able to deliver results for the full year in line with expectation."

Forecasts and valuation raised to 245p/share

So what does this all mean? Well, given the continued favourable outlook, robust fundamentals and today's deal, **we have upgraded our 2019 and 2020 PBT forecasts to £4.6m (vs £3.5m before) & £6.4m (£4.4m) respectively.** In turn, lifting adjusted EPS to 17.2p (vs 13.0p) and 23.8p (16.5p) for the next two years, and likewise pushing up the **valuation from 200p to 245p/share.**

Lastly, it is worth noting that at 135p the stock trades at an unwarranted discount (see below) to its engineering/packaging peers.

MPAC 2019 valuation benchmarks vs peers



Source: Equity Development (MPAC figures have been pension adjusted, except for PER)

Key risks

- As demonstrated in past recessions, capital equipment volumes are typically exposed to the cyclical nature of the global economy.
- The large size of the UK (£377.7m of liabilities) & US (£22.5m of liabilities) defined benefit pension schemes compared to MPAC's market capitalisation.
- Currency exposure, trade tariffs, raw material price increases (eg steel, aluminium) and competition.
- MPAC is smaller than its rivals/clients (eg German and Italian) and could see margins squeezed.
- Slower than expected growth, higher costs and/or lower cash generation.
- Industry suffers occasionally from lumpy orders, protracted customer purchasing decisions and irregular cashflows over the period end.
- Long term trend towards clients outsourcing production to 'low cost' contract manufacturers.
- Continued industry consolidation could impact pricing and margins.

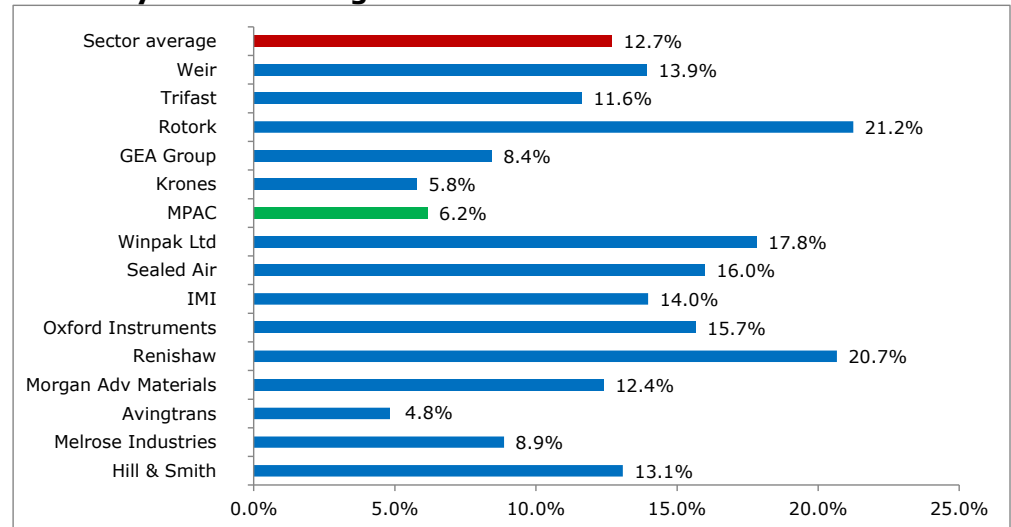
Adjusted financial projections

MPAC plc - continuing (December year end)	2016 Act £'000s	2017 Act £'000s	2018 Act £'000s	2019 Est £'000s	2020 Est £'000s	2021 Est £'000s	2022 Est £'000s	2023 Est £'000s	2024 Est £'000s
Closing orderbook	25,500	34,400	39,800						
<i>Growth</i>		35%	16%						
Equipment	28,800	40,400	46,200	49,896	53,888	58,199	62,855	67,883	73,314
Service	12,700	13,000	12,100	13,068	14,113	15,243	16,462	17,779	19,201
Lambert Automation				11,667	22,248	24,028	25,950	28,026	30,268
Turnover	41,500	53,400	58,300	74,631	90,249	97,469	105,267	113,688	122,783
<i>Equipment</i>		40.3%	14.4%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%
<i>Service</i>		2.4%	-6.9%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%
<i>Lambert Automation</i>					90.7%	8.0%	8.0%	8.0%	8.0%
Total % YoY growth		28.7%	9.2%	28.0%	20.9%	8.0%	8.0%	8.0%	8.0%
Equipment	5,400	9,200	9,300	11,476	12,664	13,968	15,399	16,971	18,438
Service	5,600	5,300	4,700	5,227	5,645	6,097	6,585	7,112	7,680
Lambert Automation				4,667	8,899	9,611	10,380	11,210	12,107
Total gross margin	11,000	14,500	14,000	21,370	27,208	29,676	32,364	35,293	38,226
<i>Equipment</i>	18.8%	22.8%	20.1%	23.0%	23.5%	24.0%	24.5%	25.0%	25.2%
<i>Service</i>	44.1%	40.8%	38.8%	40.0%	40.0%	40.0%	40.0%	40.0%	40.0%
<i>Lambert Automation</i>				40.0%	40.0%	40.0%	40.0%	40.0%	40.0%
% Margin	26.5%	27.2%	24.0%	28.6%	30.1%	30.4%	30.7%	31.0%	31.1%
EBITDA	450	2,200	2,200	5,644	7,620	9,302	10,977	12,840	14,653
% Margin	1.1%	4.1%	3.8%	7.6%	8.4%	9.5%	10.4%	11.3%	11.9%
Distribution	-5,300	-5,400	-5,000	-7,050	-9,230	-9,782	-10,408	-11,074	-11,783
Administration	-6,600	-7,300	-7,200	-9,264	-11,074	-11,370	-11,824	-12,297	-12,789
Other	-300	-500	-400	-456	-504	-524	-545	-567	-589
Adjusted EBIT	-1,200	1,300	1,400	4,600	6,400	8,000	9,587	11,354	13,064
% Operating Margin	-2.9%	2.4%	2.4%	6.2%	7.1%	8.2%	9.1%	10.0%	10.6%
Underlying interest charge	-330	-170	0	0	0	0	0	0	0
Adjusted Profit before Tax	-1,530	1,130	1,400	4,600	6,400	8,000	9,587	11,354	13,064
Adjusted EPS (p)	-6.0	4.2	4.5	17.2	23.8	29.7	35.5	42.2	48.6
<i>EPS growth rate</i>			7.8%	281.4%	38.4%	24.8%	19.2%	19.0%	15.1%
Dividend (pence)	1.25	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Reported sharecount (Ks - incl Treasury)	20,172	20,172	20,172	20,172	20,172	20,172	20,172	20,172	20,172
Valuation benchmarks									
<i>P/E ratio</i>		32.3	29.9	7.8	5.7	4.5	3.8	3.2	2.8
<i>PER (adjusted for pension recovery payments)</i>					15.3	9.1	6.6	4.9	4.0
<i>EV/Sales (pension adjusted)</i>	1.08	0.84	0.77	0.60	0.50	0.46	0.43	0.40	0.37
<i>EV/EBITDA (pension adjusted)</i>		20.4	20.4	8.0	5.9	4.8	4.1	3.5	3.1
<i>EV/EBIT (pension adjusted)</i>		34.6	32.1	9.8	7.0	5.6	4.7	4.0	3.4
<i>PEG ratio</i>			3.81	0.03	0.15	0.18	0.20	0.17	0.18
<i>Corporate tax rate</i>	20.0%	26.5%	35.7%	25.0%	25.0%	25.0%	25.0%	25.0%	25.0%
<i>EBITDA drop through rate</i>			0.0%	21.1%	12.7%	23.3%	21.5%	22.1%	19.9%
<i>Return on equity (%)</i>		1.9%	2.2%	7.8%	9.8%	10.9%	11.6%	12.1%	12.2%
Net cash/(debt)	800	29,400	27,000	9,010	8,435	9,997	12,796	16,968	22,472
Information only - Estimated non-underlying Pension charges									
UK pension recovery payments			-1,900	-1,940	-1,981	-2,022	-2,065	-2,108	-2,152
UK pension admin costs			-900	-900	-900	-900	-900	-900	-900
UK tax shield			532	540	547	555	563	572	580
US pension recovery payments (net tax shield)			-790	-751	-701	-651	-601	-551	-501
Cashflow effect			-3,058	-3,051	-3,034	-3,018	-3,002	-2,987	-2,973
Net cash/(debt) - pence per share		146	134	45	42	50	63	84	111
Net assets / diluted share (p)	175	212	201	218	242	272	308	350	398
Shareprice (p)	135								

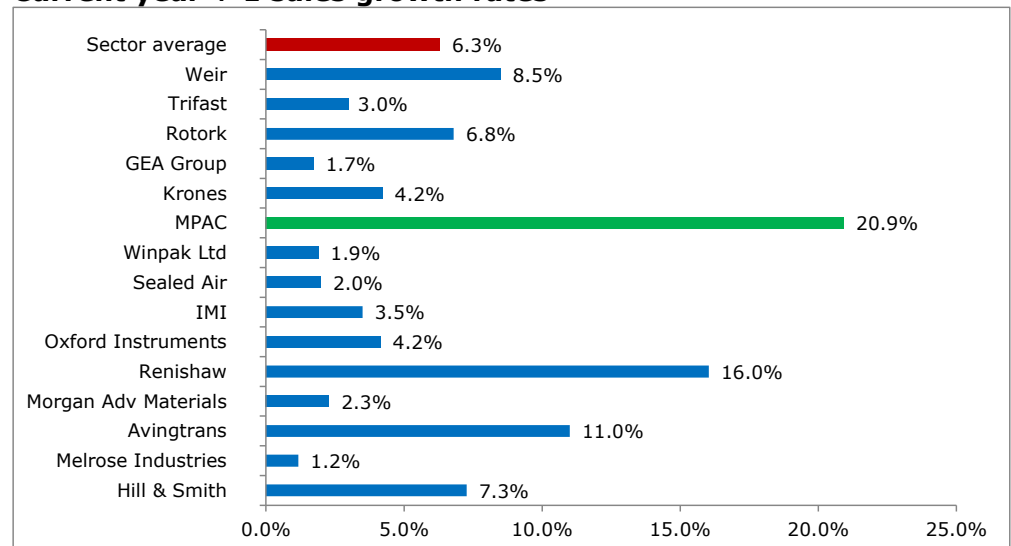
Source: Equity Development. MPAC's EV has been adjusted for pension. The cost of UK PPF levy is included within EBIT.

Appendix - Valuation benchmarks & industry KPIs

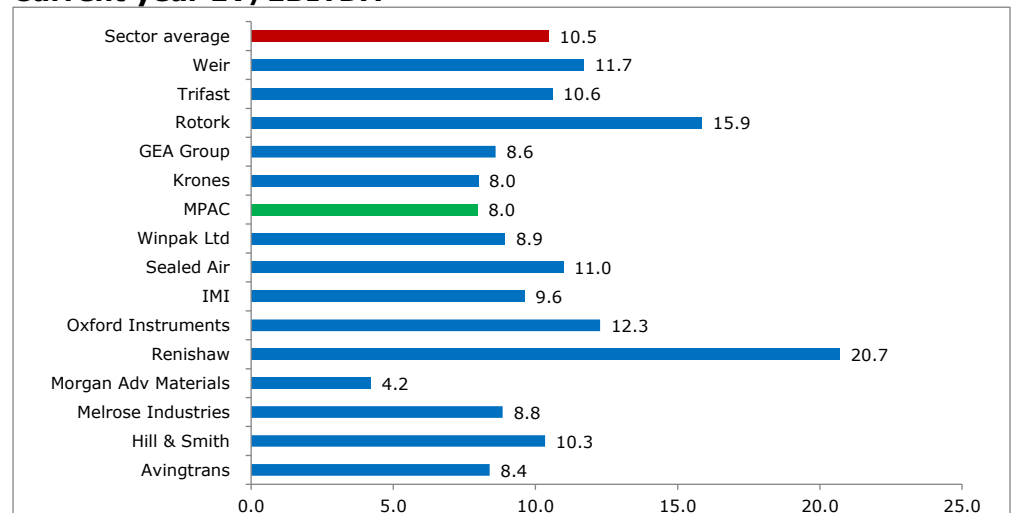
Current year EBIT margins



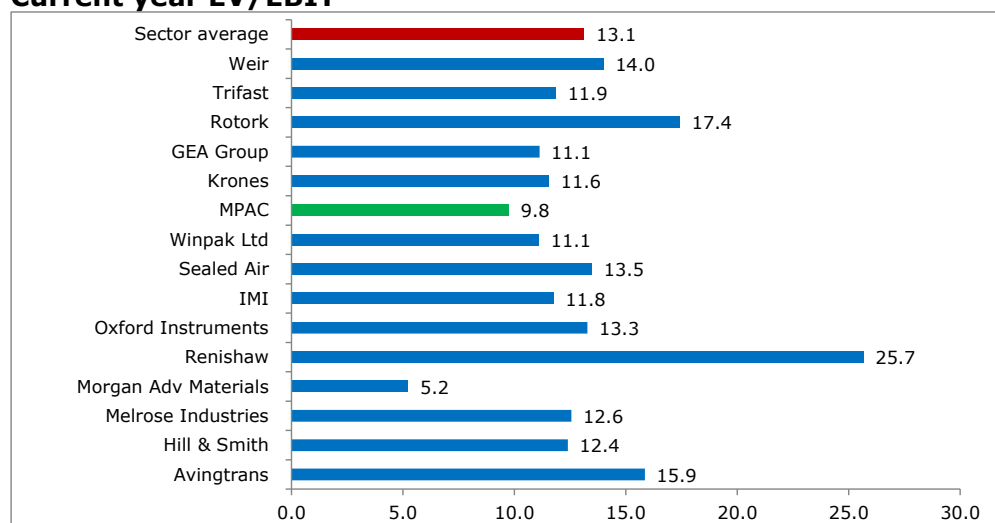
Current year + 1 sales growth rates



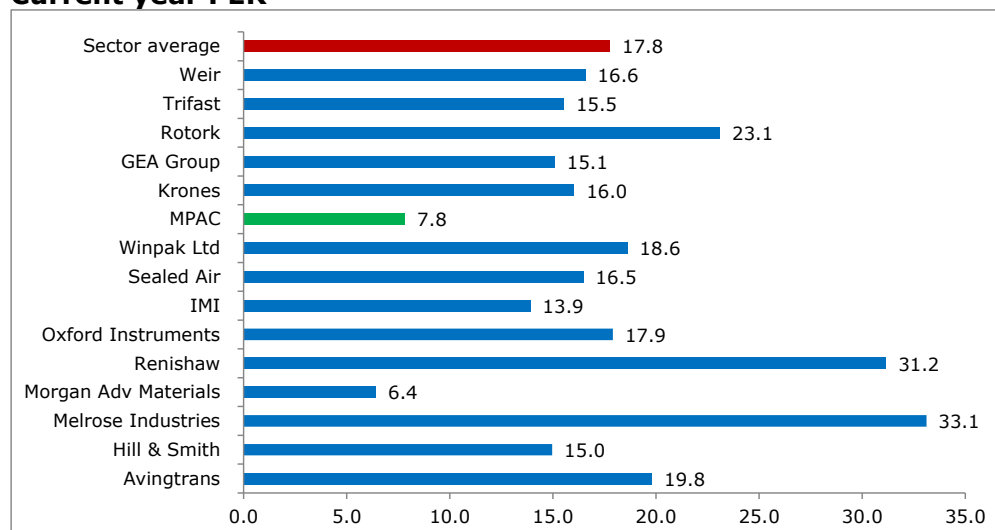
Current year EV/EBITDA



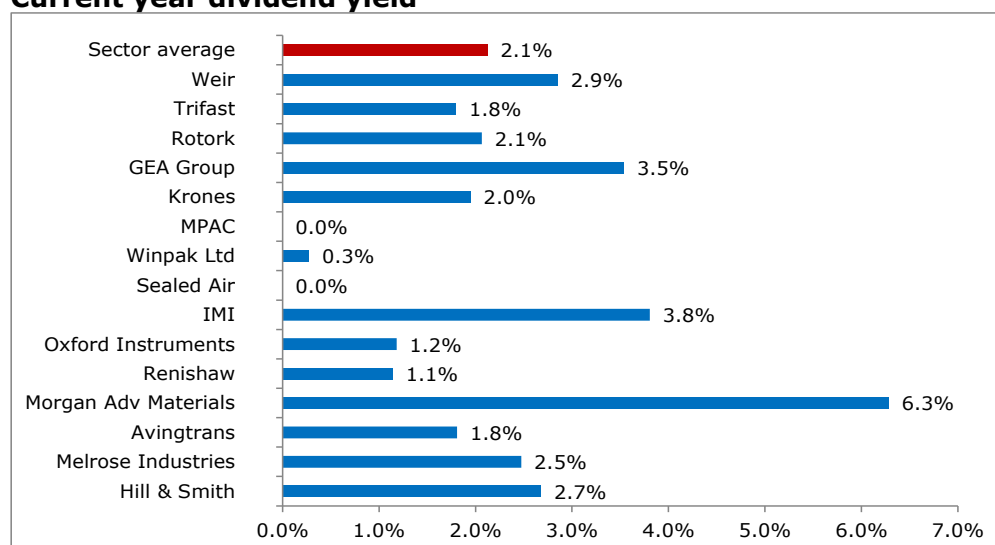
Current year EV/EBIT



Current year PER



Current year dividend yield



All Appendix tables: source ED, various websites



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