Mpac Group PLC

H1'21 Trading Update – accelerated momentum

8th July 2021

In its Trading Update for the six months ended 30 June 2021 Mpac reports that the upturn seen in H2 2020 has accelerated with H1'21 order intake well above that a year earlier - which had suffered the impact of COVID-19. The update highlights:

- **Strong performance in the Americas, enhanced by the successful integration of Switchback Group, which continues to trade ahead of management expectations, and an expanded regional presence.**
- **A second half order book which is ahead of the opening level of £55.5m. This underpins our full year revenue outlook of £95.0m.**
- **Implementation of unified business processes providing the basis for streamlined operations and a platform for sustained growth.**

Mpac Group occupies a key position in the manufacturing and distribution chain as a specialist provider of automated packaging systems. Its products and services ensure that manufacturers, in its core healthcare, food & beverage, and pharmaceuticals market segments, meet stringent regulatory requirements at high levels of volume output for sealed, packaged and packed product. Sales of equipment are matched by a significant 'whole life' service element (31% of FY20 revenue). Mpac's end-to-end solution is also evolving to solve environmental requirements such as the elimination of single-use plastics, the introduction of 'green' packaging alternatives, and reduced unit sizes. The resulting offering represents an automation ecosystem, originating in design concepts, using augmented reality, accompanied by training programmes and system upgrades, or full line modernisation.

Global presence. Mpac operates worldwide: throughout the Americas (65.9% of FY20 revenue), Europe and the UK (34.5%), Asia Pacific, the Middle East and N. Africa (9.6%). The Group derived 53.8% of FY20 revenue from the healthcare packaging equipment market, a US$6.7bn global market, 41.6% from the food & beverage segment (worth US$30.1bn) and 4.7% from the US$4.0bn pharmaceuticals packaging equipment sector.

FY20 resilience. Mpac demonstrated sound operational and financial resilience during the first year of the COVID-19 pandemic. Although revenue declined by 5.7%YoY and gross profit fell by 6.5%YoY, order intake rebounded in H2 recording £55.5m, compared to £52.2m a year earlier. The 31 December 2020 cash position was £18.9m (supported by strong operating cashflow contribution (£12.8m compared to £5.1m in FY19) and inclusive of the £10.3m initial outlay for the acquisition of Switchback.

FY21 outlook. On the basis of encouraging performance indicators for H121 and backed by evidence of a strong rebound in key markets such as the US, we estimate:

- FY21 revenue of £95m, +13.5%YoY.
- FY21 EBITDA (adj.) of £9.8m, + 24.0% YoY.

This places Mpac on a prospective FY21 EV/EBITDA of 8.3x and PE of 14.8x delivering a ROE of 14.2%. The medium-term outlook to FY23 indicates revenue CAGR at a healthy 8.6% and EBITDA CAGR of 14.4% placing Mpac on an attractive +3 year forward EV/EBITDA of 6.9x.

All of this leads us to conclude a fair value for Mpac shares of 600p.

Company Data

EPIC	AIM: MPAC
Price (last close)	478p
52 weeks Hi/Lo	591p/253p
Market cap	£96.3m
ED Fair Value/share	600p
Proforma net cash	£13.0m

Share Price, p

Source: ADVFN

Description

Mpac Automation Systems Group is a specialist provider of high-speed packaging and automation systems employing c.500 persons.

The Group generates 88% of revenue internationally. Core customer verticals include the healthcare, pharmaceuticals and food/beverage sectors, with clients such as 3M, J&J, Nestlé, GSK, P&G, Philips Advent, AstraZeneca, Unilever, Kellog's, Diageo and Bausch & Lomb.

Mpac Interim Results are expected on 2 September 2021.

Mike Jeremy (Analyst)
0207 065 2690
mike.jeremy@equitydevelopment.co.uk

Hannah Crowe
0207 065 2692
hannah@equitydevelopment.co.uk

FY20: operational and financial resilience

The global COVID-19 pandemic initiated a worldwide downturn in economic activity and trade with a sharp impact on the manufacturing sector. Although not immune, Mpac's performance demonstrated the operational and financial resilience which provided the basis for accelerated earnings momentum in the current period. The main features were:

- A moderate, single digit, decline in business performance. Revenue declined by 5.7%YoY and gross profit by 6.5%YoY, with EBIT margin declining less than 100 bp, from 8.7% to 7.8%.
- Active measures to improve efficiency, such as the integration of its Coventry operations into the Tadcaster centre, realising improvements in operational performance and the benefits of a larger site.
- Successful completion of the latest acquisition; of Switchback Group in the US, for an initial US$13.3m.
- Improved H2 order intake. Order intake closed the year -4%YoY at £83.9m (-14%YoY excluding Switchback), but rebounded in H2 recording £55.5m compared to £52.2m in H219.
- Sound cash management. The year-end cash position was £15.5m (FY19 £18.9m) supported by strong operating cashflow (£12.8m compared to £5.1m in FY19) and inclusive of the £10.3m initial outlay for the acquisition of Switchback. This is underpinned by the 3-year HSBC £10.0m RCF.

As a result, Mpac entered FY21 well-prepared to meet the cyclical recovery of demand in its target markets and address the continuing technical and structural demands of its customer base.

Notwithstanding the ongoing challenge of the pandemic, the current worldwide economic outlook is cautiously positive. As the OECD Business Confidence Indicator survey indicates, three major areas - the US, Euro-area (19) countries and OECD group countries - show a strong rebound in sentiment. Although at an early stage, the rebound is stronger that that experienced in the aftermath of the 2008-2009 'sub-prime' financial crisis, creating a positive backdrop for the demand outlook in Mpac's core markets.

The proximity of the Glasgow COP 26 summit in November is a reminder of the urgent environmental challenges faced by a manufacturing sector increasingly incentivised to reduce its carbon footprint - as emphasised by BlackRock CEO Larry Fink's January 2020 open letter on sustainability – and cut polluting waste. This translates into a continuing challenge to improve the efficiency of packaging equipment and systems whilst adapting to the use of new, less wasteful, 'green' materials.

OECD Business Confidence Indicator

Source: OECD (2021), Business Confidence Index (BCI) (indicator) 11 May 2021

Strategy

Mpac's core growth strategy is built around a number of initiatives:

- Continual **product innovation** ("Ingenuity") as the wellspring for product development, including: client consultation and design with attention to future requirements; installation and training designed to enhance productivity; monitoring services and equipment optimisation; the use of sustainable materials including elimination of single use plastics.
- **Geographic focus** on manageable growth opportunities in Europe and the Americas, backed by suitable acquisition(s).
- **Improved efficiency.** Mpac places emphasis on improved and aligned processes across its group operational centres. Initiatives such as the (2020) roll out of Group ERP systems in the Netherlands and the recent consolidation of UK activities at Tadcaster have resulted in streamlined and unified operations which, as highlighted in the Trading Update, provide the platform for sustained growth.
- Development of **services revenue** streams through whole-life engagement with clients and feedback to product development, including COVID-19 remote business support.

Current priorities include: expansion of the US presence; a focus on developing healthcare sector opportunities, notably in the Americas; introduction of ERP systems in Canada, US and UK; continued development of full-line automated solutions and launch of commercial 'Industry 4.0' products.

FY21-23 outlook

Our FY21 outlook is underpinned by the strength of the indicated H2 order book, a services revenue component at an estimated 23.5% of total, and contribution from Switchback with a revenue run-rate of c.£11.0m and EBITDA contribution c.£1.8m.

This results in estimated FY21 revenue growth of 13.5%YoY, and EBITDA of +24.0%YoY, placing Mpac on a prospective EV/EBITDA of 8.3x and 14.8x PE, underpinned by 14.2% ROE.

This compares to, for example, an average Q1/Q2 21.9x PE for the US Capital Goods Manufacturing Machinery sub-sector (CSI Market) and EV/EBITDA (ED estimate) of 12.4x.

Summary financial outlook to FY23

Yr to 31 Dec (£m)	2019	2020	2021E	2022E	2023E	2021E change	CAGR 2020-23
Revenue	88.8	83.7	95.0	100.0	107.3	13.5%	8.6%
EBITDA (adj)	9.8	7.9	9.8	10.8	11.8	24.0%	14.4%
Pre-Tax Profit (adj)	7.5	6.3	7.5	8.5	9.5	18.9%	14.8%
EPS (adj, p)	38.7	31.4	32.3	36.3	40.0	3.1%	8.4%
Net debt (cash)	18.0	14.6	13.0	11.9	18.9	-10.9%	9.0%
P/E	12.3x	15.2x	14.8x	13.1x	11.9x		
EV/EBITDA	8.3x	10.3x	8.3x	7.6x	6.9x		
Price /sales	0.0x	0.0x	1.01x	0.96x	0.90x		

Source: Company data, Equity Development estimates

Strategic trends – 'Industry 4.0'

Mpac's strategy is aligned with the needs of its clients to improve packaging quality, systems automation and monitoring in an increasingly software-dominated and integrated systems environment. This matches general trends in the manufacturing sector focused on the adoption of digital technology and increased automation. For example, in its 2020 Annual Manufacturing Report, *The Manufacturer* outlined a number of key trends and concerns, within the UK sector within an overall 'search for stability' theme and backed by research by the MIT Sloan Center for Information Systems Research. The survey noted:

- 61% of respondents were not just aware of the availability digital technologies but were prepared for adoption, with 63% seeing digital technologies as having the potential to improve supply chain relationships.
- Far from supplanting or replacing workforce skills, 77% envisaged digital technologies enhancing and introducing new employee skillsets, with 64% seeing adoption as a boost to production and additional employment opportunities.
- Innovation, a core concept in Mpac's approach, was seen as stimulated by digital adoption by 67% of respondents, backed by (73%) the benefits of feedback data from connected systems.

Henrik von Scheel, the technology strategist who first coined the term 'Industry 4.0' to encapsulate automated and digitally-influenced manufacturing techniques, noted as early as 2019 the adoption of advanced technologies (in the UK) by 46% of those involved in additive manufacturing and 33% of those involved in smart automation.

Mpac's vision of 'packaging 4.0'

Mpac highlights a number of '4.0' processes and trends within its own offering:

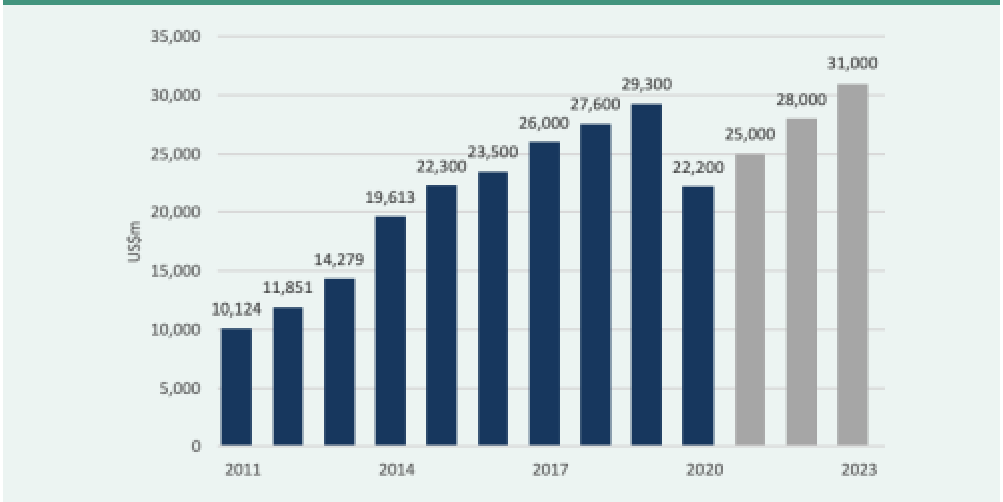
- **Production on demand**. This requires flexible repurposing, increased overall equipment efficiency, integrated monitoring and control platforms, with the addition of component supplier and consumer communication with in-line production.
- **Digital twin**, a virtual 'carbon copy' of physical systems. This enables pre-installation testing and fault identification, improving service life and reducing repairs downtime.
- **Integration of robotic** technology – e.g. Mpac Langen's Cartoner 4.0 based on vision-system FANUC robots – combining high-speed packaging with flexibility and product variety.
- **Advanced HMI** – human machine interface - systems such as dashboards, online manuals, fault finding and training programmes.

Acquisition of Switchback Group

Mpac acquired Switchback Group Inc., a packaging specialist in September 2020, for US$13.3m (£10.2m) plus a performance-based earn-out of up to US$2.0m (£1.6m) comprising US$1.0m (£0.8m) payable in FY21 and FY22, set at US$0.5m on a Switchback annual adjusted EBITDA contribution of >US$1.1m, and an additional 50% above US$1.1m capped at US$2.1m. The chart below shows the management of FY20 cashflow.

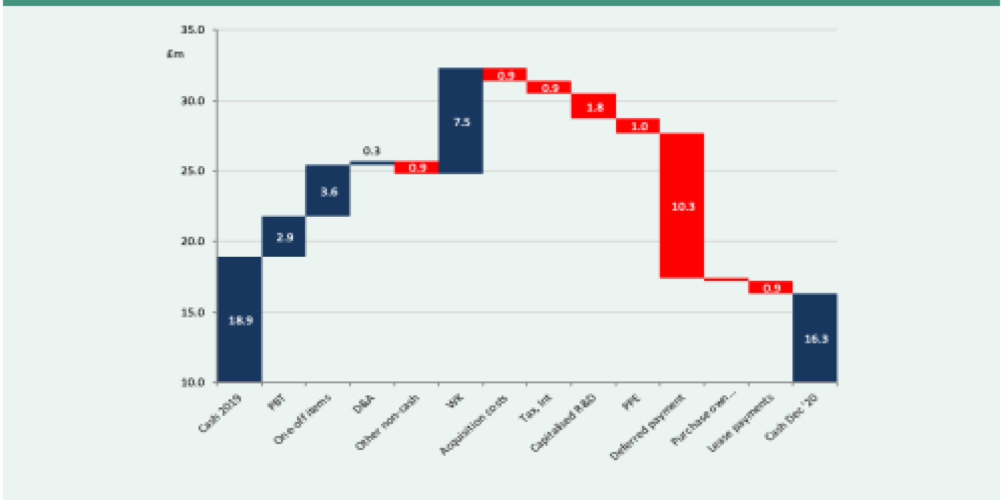
Based near Cleveland, Ohio, Switchback was founded in 2006 and has 45 employees. Supplying the food and beverage (principally craft beer, at 66% of FY20 revenue) and healthcare sectors in the US, Switchback manufactures automated packaging systems for recyclable items, including tray-formers, carton closers, tray packers and labelling and four-sided pouching machinery. The acquisition brings estimated annualised revenue of US$15.0m (£10.7m) and EBITDA of US$2.5m (£1.8m), a 16.7% margin. Craft beer has been a success story in the US, taking 24% of the US retail beer market, with over 8,700 craft breweries in a segment worth US$76.3m in 2019 forecast to grow at a 7.2% CAGR to US153bn by 2029 (source FACT MR, Statista).

US craft beer retail sales 2011 – 2023E



Source: Statista, Equity Development estimates

Mpac FY20 cashflow bridge



Source: Company data

Summary performance and outlook

Profit & Loss

P&L Year to 31 Dec (£m)	FY19	FY20	FY21E	FY22E	FY23E	CAGR 2020-23
Order book Y/E	52.2	55.5	57.0	60.0	64.4	5.1%
Equipment revenue	69.4	64.1	72.6	76.3	82.4	8.7%
Service revenue	19.4	19.6	22.3	23.7	24.9	8.3%
Revenue	**88.8**	**83.7**	**95.0**	**100.0**	**107.3**	**8.6%**
Gross Sum	**26.0**	**24.3**	**29.9**	**31.5**	**33.8**	**11.6%**
Gross Margin	29.3%	29.0%	31.5%	31.5%	31.5%	
COGS	(62.8)	(59.4)	(65.1)	(68.5)	(73.5)	
Distribution	(7.2)	(6.8)	(8.1)	(8.3)	(8.8)	
Admin	(10.3)	(9.9)	(12.5)	(12.9)	(13.5)	
Other	(0.8)	(1.1)	(1.6)	(1.6)	(1.7)	
Sum operating costs	(18.3)	(17.8)	(22.2)	(22.8)	(24.1)	
EBIT Reported	5.3	2.9	4.1	5.1	6.1	
EBIT Adjusted	**7.7**	**6.5**	**7.7**	**8.7**	**9.7**	**14.4%**
Margin	8.7%	7.8%	8.1%	8.7%	9.1%	
Amortisation	(0.2)	(0.3)	(1.0)	(1.0)	(1.0)	
Depreciation	(1.9)	(1.1)	(1.1)	(1.1)	(1.1)	
EBITDA Reported	7.4	4.3	6.2	7.2	8.2	
EBITDA Adjusted	**9.8**	**7.9**	**9.8**	**10.8**	**11.8**	**14.4%**
Margin	11.0%	9.4%	10.3%	10.8%	11.0%	5.3%
Financial income	0.0	0.0	0.0	0.0	0.0	
Financial expense	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)	
PBT Reported	5.4	2.9	3.9	4.9	5.9	
PBT Adjusted	7.5	6.3	7.5	8.5	9.5	14.8%
Tax	0.5	0.4	(1.0)	(1.2)	(1.5)	
PAT Reported	5.9	3.3	2.9	3.7	4.4	
PAT Adjusted	**7.8**	**6.3**	**6.5**	**7.3**	**8.0**	**8.4%**
Basic wtd. Av. shares (m)	20.0	20.0	20.0	20.0	20.0	
Diluted wtd. av. shares (m)	20.1	20.1	20.1	20.1	20.1	
EPS Reported Basic (p)	29.5	16.5	14.5	18.5	22.2	
EPS Reported Diluted (p)	29.3	16.4	14.4	18.4	22.0	
EPS Adjusted Basic (p)	39.1	31.6	32.5	36.6	40.2	
EPS Adjusted Diluted (p)	**38.7**	**31.4**	**32.3**	**36.3**	**40.0**	**8.4%**

Source: Company data, Equity Development estimates

Summary Balance Sheet

Year to 31 Dec (£m)	FY19	FY20	FY21E	FY22E	FY23E
Fixed Assets					
Intangible assets	16.9	27.4	25.6	21.3	20.3
PPE net	5.6	5.1	6.5	8.0	9.7
Property	0.8	0.8	0.8	0.8	0.8
Right of use	4.7	4.0	4.0	4.0	4.0
Employee benefits	20.4	14.0	14.0	14.0	14.0
Deferred tax	1.7	1.8	1.8	1.8	1.8
Sum Fixed Assets	**50.1**	**53.1**	**52.7**	**49.9**	**50.6**
Current Assets					
Inventories	3.2	3.5	3.9	4.1	4.4
Trade receivables	28.0	32.2	31.2	27.4	29.4
Tax assets	0.4	0.8	0.8	0.8	0.8
Cash, Equivalents	18.9	15.5	13.9	12.8	19.8
Contract assets	0.0	0.0	0.0	0.0	0.0
Sum Current Assets	**50.5**	**52.0**	**49.8**	**45.1**	**54.4**
Total Assets	100.6	105.1	102.5	95.0	105.0
Current Liabilities					
Trade payables	(30.9)	(41.1)	(46.8)	(49.3)	(52.9)
Leases	(0.9)	(0.8)	(0.8)	(0.8)	(0.8)
Provisions	(1.3)	(1.4)	(1.4)	(1.4)	(1.4)
Tax, Other	(0.7)	(0.4)	(0.4)	(0.4)	(0.4)
Contract liabilities	0.0	0.0	0.0	0.0	0.0
Sum Current Liabilities	**(33.8)**	**(43.7)**	**(49.4)**	**(51.9)**	**(55.5)**
Total Assets less Current Liabilities	66.8	61.4	53.1	43.1	49.5
Long-term Liabilities					
Borrowings	(0.9)	(0.9)	(0.9)	(0.9)	(0.9)
Employee benefits	(3.1)	(3.0)	(3.0)	(3.0)	(3.0)
Tax	(8.8)	(6.8)	(6.8)	(6.8)	(6.8)
Leases	(3.9)	(3.4)	(3.4)	(3.4)	(3.4)
Deferred cons	(2.6)	(2.9)	(3.2)	(0.7)	0.0
Sum Long-term liabilities	**(19.3)**	**(17.0)**	**(17.3)**	**(14.8)**	**(14.1)**
Total liabilities	(53.1)	(60.7)	(66.7)	(66.7)	(69.6)
Net Assets	47.5	44.4	35.8	28.3	35.4
Capital & Reserves					
Share Capital	5.0	5.0	5.0	5.0	5.0
Share Premium	26.0	26.0	14.5	3.3	6.0
Capital Reserve	5.2	5.2	5.2	5.2	5.2
Retained earnings	11.3	8.2	11.1	14.8	19.2
Equity	**47.5**	**44.4**	**35.8**	**28.3**	**35.4**
Net cash/(debt)	18.0	14.6	13.0	11.9	18.9

Source: Company data, Equity Development estimates

Summary cashflow

Year to 31 Dec (£m)	FY19	FY20	FY21E	FY22E	FY23E
Operating profit	**5.3**	**2.9**	**4.1**	**5.1**	**6.1**
One-off items	2.4	3.6	3.6	3.6	3.6
Amortisation	0.2	0.3	1.0	1.0	1.0
Depreciation	1.9	1.1	1.1	1.1	1.1
Other non-cash	0.3	0.4	1.0	0.0	0.0
Pension	(2.9)	(3.0)	(3.0)	(3.0)	(3.0)
Operating Cash Flow	**7.2**	**5.3**	**7.8**	**7.8**	**8.8**
Working capital					
(Increase)/Decrease inventories	(0.2)	0.2	(0.4)	(0.2)	(0.3)
(Increase)/Decrease in contract assets	(2.4)	(1.7)	(1.5)	(1.0)	0.0
(Increase)/Decrease in receivables	4.7	(0.6)	(0.4)	(0.2)	(0.3)
Increase/(Decrease) in payables	2.8	4.1	5.7	2.5	3.6
(Increase)/Decrease in contract liabilities	(7.4)	5.4	(7.7)	(2.0)	0.0
Increase / Decrease in provisions	0.4	0.1	0.0	0.0	0.0
Movement in working capital	**(2.1)**	**7.5**	**(4.3)**	**(0.9)**	**3.0**
Cash generated by operations	**5.1**	**12.8**	**3.5**	**6.8**	**11.8**
Acquisition costs	(1.0)	(0.9)	0.0	0.0	0.0
Tax (paid)/received	1.0	(0.7)	0.0	0.0	0.0
Net cash from operations	5.1	11.2	3.5	6.8	11.8
Investing activities	0.0	0.0	0.0	0.0	0.0
Interest received	0.0	0.0	0.0	0.0	0.0
Sale of PPE	0.2	0.2	0.5	0.0	0.0
Capitalised R&D	(0.3)	(1.8)	(1.8)	(1.8)	(1.9)
Assets under const	(0.6)	0.0	(0.3)	0.0	0.0
PPE	(1.4)	(1.2)	(2.5)	(2.6)	(2.8)
Acquired cashflow/deferred payment	(10.6)	(10.3)	(0.8)	(3.3)	0.0
Net cash used in investing	**(12.7)**	**(13.1)**	**(4.9)**	**(7.8)**	**(4.6)**
Net OpFCF	**(7.6)**	**(1.9)**	**(1.4)**	**(0.9)**	**7.2**
Financing activities					
Borrowings	0.0	0.0	0.0	0.0	0.0
Interest paid	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)
Purchase own shares	(0.1)	(0.2)	0.0	0.0	0.0
Lease payments	(1.0)	(0.9)	0.0	0.0	0.0
Net cash from financing	(1.2)	(1.3)	(0.2)	(0.2)	(0.2)
Net increase in cash / equivalents	**(8.8)**	**(3.2)**	**(1.6)**	**(1.1)**	**7.0**
Cash at beginning of year	27.9	18.9	15.5	13.9	12.8
Forex	(0.2)	(0.2)	0.0	0.0	0.0
Cash at year end	**18.9**	**15.5**	**13.9**	**12.8**	**19.8**
Net cash/(debt)	**18.0**	**14.6**	**13.0**	**11.9**	**18.9**
Pension adjustments					
Cashflow impact	(2.8)	(4.5)	(3.4)	(3.7)	(3.9)

Source: Company data, Equity Development estimates

Contacts

Andy Edmond
Direct: 020 7065 2691
Tel: 020 7065 2690
andy@equitydevelopment.co.uk

Hannah Crowe
Direct: 0207 065 2692
Tel: 0207 065 2690
hannah@equitydevelopment.co.uk

Equity Development Limited is regulated by the Financial Conduct Authority

Disclaimer

More information is available on our website www.equitydevelopment.co.uk

Equity Development, 15 Eldon Street, London, EC2M 7LD

Contact: info@equitydevelopment.co.uk | 020 7065 2690