Mpac Group plc

Well placed and cash rich

6th May 2020

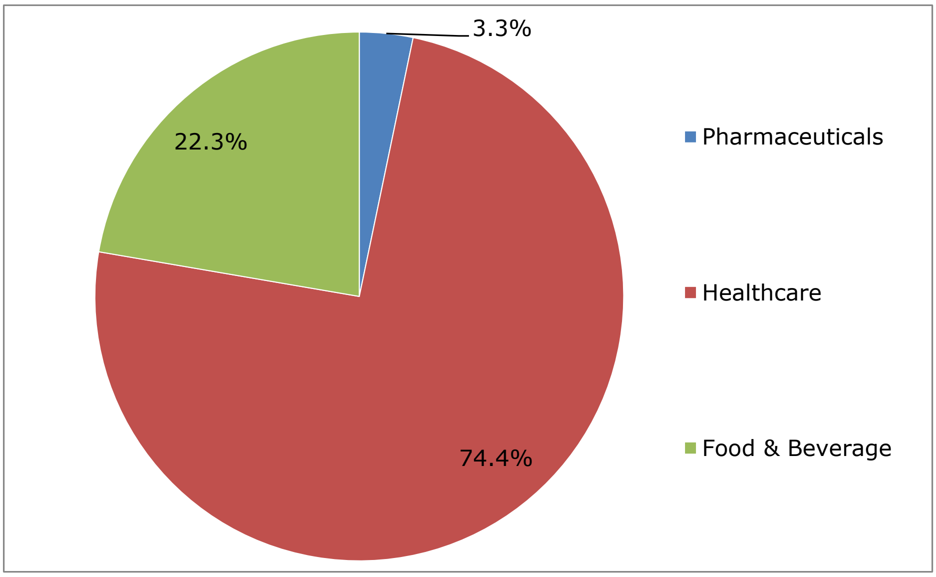
Few capital goods companies are better positioned than Mpac to survive the COVID-19 induced downturn, exploit opportunities that arise and flourish when the economy eventually gets back on its feet (hopefully in 2021). Why?

Firstly this high speed packaging & automation solution firm sports a £18.1m net cash balance (or 89p/share as at Feb'20), on top of an undrawn £10m credit facility. Providing ample fire-power to not only weather even the most extreme of scenarios, but also take advantage if some less well capitalised rivals ever became available at distressed levels.

What's more, with a global footprint and fully integrated smart technology (eg remote diagnostics, firmware, etc) underpinning its industry leading products, there should be further scope to gain market share organically, as clients standardise on best-in-class OEMs offering worldwide service & support.

In fact this may already be happening, since we understand Mpac is still winning new business despite a small number of orders being deferred because of the pandemic. **Covering vital machinery, spares & engineering expertise to strategically important sectors** like healthcare, pharmaceuticals and food/beverage (see below), which are needed to keep people healthy & fed throughout this challenging period.

2019 revenue (£88.8m) break-down by customer segment



Source: Equity Development

Shares are attractively priced

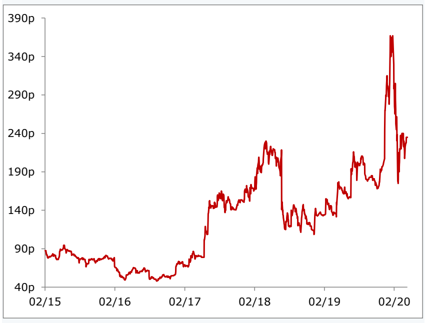
In the meantime, the Board is sensibly cutting its cloth – namely reducing/deferring capex (£2.3m 2019) and discretionary spend, alongside utilising available government aid programs. Mindful however not to harm long term design and operational capability.

With regards to valuation, the stock at 235p remains attractively priced - trading on a 2019 EV/EBIT multiple of 7.4x (see below) vs 11x–15x typically for peers (pre CV19).

Company Data

EPIC	**AIM:MPAC**
Price (last close)	235p
52 week Hi/Lo	367p/154p
Market cap	£47.4m
Net cash Dec '19	£18.0m
Share count (incl Treasury)	20.172m
ED valuation/share	Withdrawn
Avg. daily volume	250,000

Share Price, p



Source: Share Cast

Description

Mpac is a specialist provider of **full line, high speed packaging & automation solutions,** employing c. 510 staff.

The group not only develops & manufactures niche factory equipment and robotics, but also undertakes turnkey projects involving the design & integration of such systems. More than 80% of revenues are generated outside of the UK, hence providing a natural hedge against sterling weakness.

Core verticals are Healthcare, Pharmaceutical and Food/Beverage, supporting the likes of 3M, J&J, Nestlé, GSK, P&G, Philips Advent, ConvaTec, AstraZeneca, Unilever, Kellogg's, Diageo, Ferrero, Bausch + Lomb & CooperVision.

Next news: Trading update mid July

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Sure the coronavirus will impact 2020 numbers, yet ultimately we believe Mpac will prosper. Benefitting from secular tailwinds (eg Industry 4.0, Direct-to-consumer deliveries), improving margins, a large installed base, positive cashflows and a host of loyal, blue-chip customers.

Range of sector valuation benchmarks pre COVID-19 crisis

	Mpac 2019 Trailing	Typical Packaging equipment & Engineering multiples pre COVID-19	
		Low	High
EV/Sales (pension adjusted)	0.6	1.0	1.5
EV/EBITDA (pension adjusted)	5.8	8.0	12.0
EV/EBIT (pension adjusted)	7.4	11.0	15.0
PER	5.9	14.0	18.0
EBIT margin	8.7%	10.0%	15.0%

Source: Equity Development

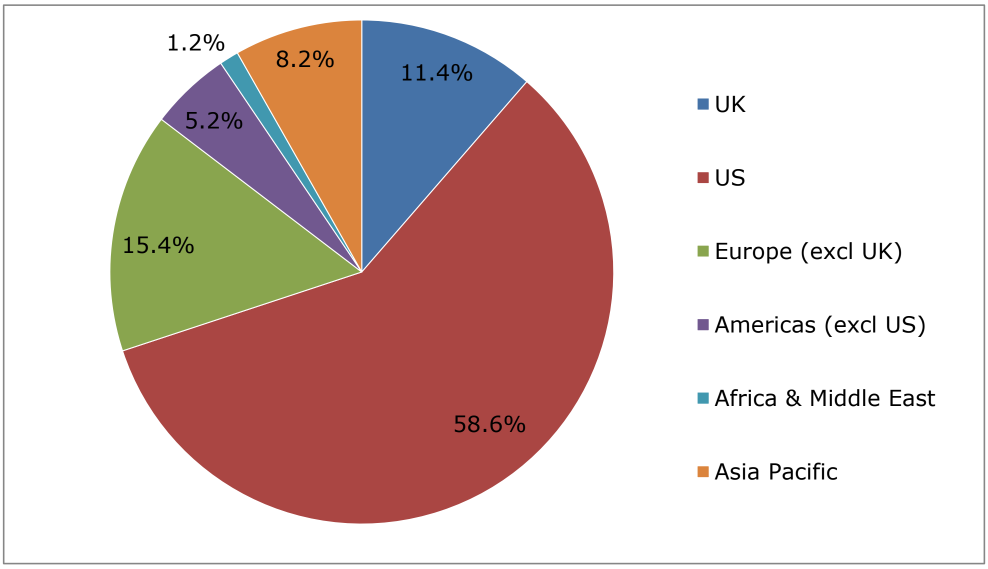
The world is gradually getting back to work

Elsewhere, the actuarial deficit on the UK pension scheme (re £35.2m as at the June 2018 triennial valuation) may have increased slightly over the past 2 months – reflecting lower gilt yields, higher spreads on corporate bonds and the recent equity market turmoil.

That said, the worst of March's credit crunch seems to be behind us, thanks to massive central bank intervention and 'do whatever it takes' monetary stimulus.

From a medical perspective too, encouraging progress is being made on tackling the disease (re flattening the curve). Thus allowing several countries to slowly reboot their economies. Indeed over the past week, roughly 20 US states have tentatively lifted 'stay-at-home' orders, Mpac's largest region (see below). Which hopefully will further prompt the UK & the rest of Europe set to follow suite in the not too distant future, after similar moves from Germany & Denmark.

2019 regional sales (£88.8m) split



Source: Equity Development

Key risks

- COVID-19 impacts last longer than expected. Plus in past recessions, capital equipment volumes are typically exposed to the cyclical nature of the global economy.
- The large size of the UK (£403.2m of liabilities as at December 2019) & US (£13.5m 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.

Historical results

Mpac plc - continuing (December year end)	**2016 Act £'000s**	**2017 Act £'000s**	**2018 Act £'000s**	**2019 Act £'000s**
Closing orderbook	**25,500**	**34,400**	**53,100**	**52,200**
Growth		*34.9%*	*54.4%*	*-1.7%*
Equipment	28,800	40,400	46,200	69,400
Service	12,700	13,000	12,100	19,400
Turnover	**41,500**	**53,400**	**58,300**	**88,800**
Equipment		*40.3%*	*14.4%*	*50.2%*
Service		*2.4%*	*-6.9%*	*60.3%*
Total % YoY growth		***28.7%***	***9.2%***	***52.3%***
Equipment	5,400	9,200	9,300	18,200
Service	5,600	5,300	4,700	7,800
Total gross margin	**11,000**	**14,500**	**14,000**	**26,000**
Equipment	*18.8%*	*22.8%*	*20.1%*	*26.2%*
Service	*44.1%*	*40.8%*	*38.8%*	*40.2%*
% gross margin	***26.5%***	***27.2%***	***24.0%***	***29.3%***
EBITDA	**450**	**2,200**	**2,200**	**9,800**
% Margin	*1.1%*	*4.1%*	*3.8%*	*11.0%*
Distribution	-5,300	-5,400	-5,000	-7,200
Administration	-6,600	-7,300	-7,200	-10,300
Other	-300	-500	-400	-800
Adjusted EBIT	**-1,200**	**1,300**	**1,400**	**7,700**
% Operating Margin	*-2.9%*	*2.4%*	*2.4%*	*8.7%*
Underlying interest charge	-330	-170	0	-200
Adjusted Profit before Tax	**-1,530**	**1,130**	**1,400**	**7,500**
Adjusted EPS (p)	**-6.0p**	**4.2p**	**4.5p**	**39.5p**
EPS growth rate			*7.5%*	*777.7%*
Dividend (p)	***1.3p***	***0.0p***	***0.0p***	***1.5p***
Yield	*0.5%*	*0.0%*	*0.0%*	*0.6%*
Reported sharecount (Ks - incl Treasury)	20,172	20,172	20,172	20,172
Valuation benchmarks				
P/E ratio		*56.1*	*52.2*	*5.9*
PER (adjusted for pension recovery payments)				
EV/Sales (pension adjusted)	*1.37*	*1.06*	*0.97*	*0.64*
EV/EBITDA (pension adjusted)		*25.8*	*25.8*	*5.8*
EV/EBIT (pension adjusted)		*43.6*	*40.5*	*7.4*
PEG ratio				
Corporate tax rate	*-20.0%*	*-26.5%*	*-35.9%*	*5.2%*
EBITDA drop through rate			*0.0%*	*24.9%*
Return on equity (%)		*1.9%*	*2.2%*	*16.6%*
Net cash/(debt)	**800**	**29,400**	**27,000**	**18,000**
Information only - Estimated non-underlying Pension charges				
UK pension recovery payments			-1,900	-1,940
Topup UK pension payments above £5.5m EBIT			0	-726
UK pension admin costs			-900	-1,200
UK tax shield			532	735
US pension recovery payments (net tax shield)			-790	-790
Cashflow effect			**-3,058**	**-3,921**
Net cash per share		**146**	**134**	**89**
Net assets / diluted share (p)	175	212	201	235
Shareprice (p)	**235p**			

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

Investor Access

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