

Sell off appears way over done

12th October 2022

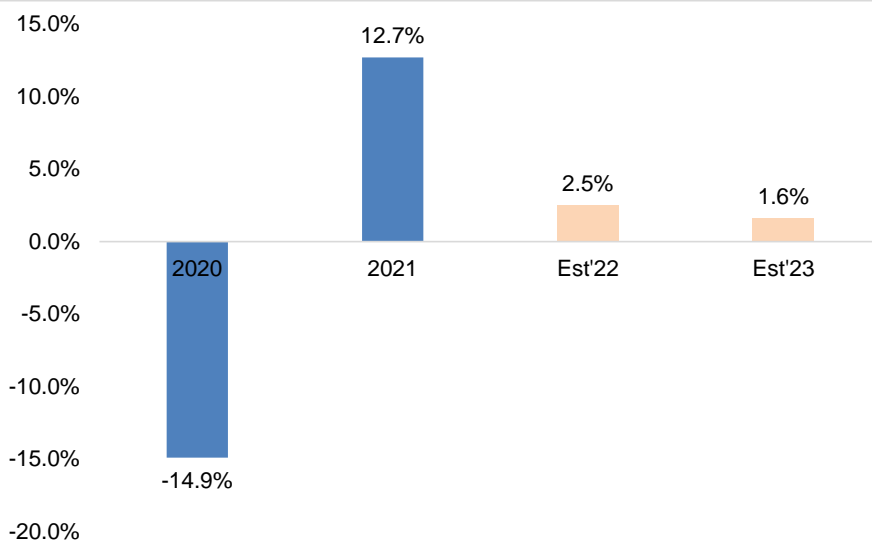
It's very easy to get negative on the UK. There's a cost-of-living crisis (re CPI 10%), the £ has plummeted and interest rates are set to tip 5.5% by mid-2023. Yet equally, the country has been through this and much worse many times before, bouncing back strongly after the 1980s and 1990s recessions, 2008/9 Global Financial Crisis, Brexit and the 2020 pandemic.

Likewise, I'm sure we'll do so again, with the Bank of England predicting GDP to start recovering in late 2024 after a shallow 2-year recession. Or in other words, nowhere near as bad as the Armageddon scenarios presently being priced into high quality names like Vp that provide essential and specialist rental equipment/services to the infrastructure, construction and housebuilding sectors.

Long term secular growth markets

Industry experts, the Construction Products Association, don't believe demand will fall off a cliff either. Instead, they are **anticipating relatively calmer waters ahead, supported by vital and overdue infrastructure projects** (+8.5% 2022 & 3.8% 2023) in regulated areas such as roads, rail, water and electricity. Alongside this sits the **build out of multi-year projects like HS2, Thames Tideway and Hinkley Point C.**

Forecast of UK construction output



Source: Construction Products Association (July'22)

Trading in line with expectations

Indeed this 'glass is half full' outlook is also not dissimilar to how Vp sees it.

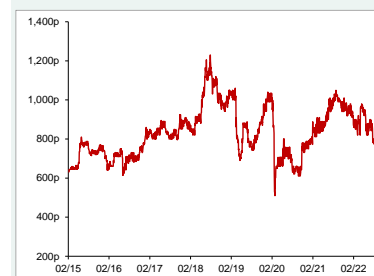
In their trading update yesterday, VP says that the **domestic homebuilding and infrastructure markets were "supportive" in H1'22**, with construction "stable". Here the Group experienced **"good" power transmission demand** (re renewables & offshore wind) **augmented by AMP7 water & civil engineering which both "picked up" in Q2.**

Elsewhere construction was "satisfactory, with repair & maintenance remaining "positive", albeit offset by quieter activity in new build (eg offices).

Company Data

EPIC	LSE: VP.
Price (last close)	£7.15
52 week Hi/Lo	£10.25/£7.15
Market cap	£287m
Est Mar23 net debt (ex IFRS16)	£130m
Share count	40.154m
ED valuation	1,130p/share

Share Price, p



Source: Yahoo Finance

Description

Vp is a specialist equipment rental business providing equipment and services to a wide range of markets including civil engineering, rail, oil/gas exploration, construction, outdoor events and industry, primarily within the UK (91% of pre-covid turnover), but also overseas.

In terms of sector split: circa 36% sales is derived from infrastructure, 41% construction, 7% housing building, 9% Energy and 7% other.

Member of FTSE SmallCap Index.

Next news: Interims 29th Nov'22

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Granted the recent labour strikes have crimped output in rail with Phase 2 (north of Birmingham) of HS2 also slowing slightly due to delays. Nonetheless, these are ultimately temporary issues that should iron themselves out in future periods.

Better still, the previously highlighted headwinds of **cost inflation and supply chain disruption have begun to ease** on the back of shorter lead times. Plus, internationally, **Airpac Rentals and TR delivered “good” growth YoY**.

So what does this all mean?

Well putting this altogether, we believe the **outlook remains favourable**, with **the business in “excellent shape to invest in further growth, as and when market conditions improve”**.

CEO Neil Stothard adding: Vp “*has an **exemplary record of delivering returns through adverse trading conditions** most recently in the last global downturn and then in the Covid 19 pandemic. So, whilst the near term uncertainty in the economy is a factor. **We have every confidence that our experience, and the inbuilt resilience, will yet again see the Group continue to make good progress and in line with FY’23 expectations.***”

Significantly undervalued, high quality GARP stock

Lastly in terms of the numbers, we reiterate our **FY’23 adjusted PBTA & EPS forecasts of £41.4m & 78.1p** respectively on revenues up 4.2% to £365m, with **net debt (pre IFRS 16) closing Mar’23 at £130m** (ie flat YoY), equivalent to a **comfortable 1.4x EBITDA**.

This in turn puts Vp on **attractive 4.5x EV/EBITDA and 9.2x PE multiples**, whilst paying a 5.4% dividend yield and generating a 15% ROCE. Consequently, we think **the stock is materially undervalued** and instead estimate its worth (at least) **£11.30/share – offering more than 50% potential upside from current levels**.

Summary projections (£'000s)							
Vp (March year end)	2018 Act £'000s	2019 Act £'000s	2020 Act £'000s	2021 Act £'000s	2022 Act £'000s	2023 Est £'000s	2024 Est £'000s
Turnover							
UK	271,989	350,330	331,005	281,309	320,203	333,011	343,001
International	31,650	32,500	31,922	26,688	30,712	32,555	33,531
Total	303,639	382,830	362,927	307,997	350,915	365,566	376,533
% growth	22.1%	26.1%	-5.2%	-15.1%	13.9%	4.2%	3.0%
UK	23.6%	28.8%	-5.5%	-15.0%	13.8%	4.0%	3.0%
International	10.2%	2.7%	-1.8%	-16.4%	15.1%	6.0%	3.0%
EBITDA	84,337	101,339	98,050	72,701	88,868	92,241	98,076
% Margin	27.8%	26.5%		23.6%	25.3%	25.2%	26.0%
EBITDA (post IFRS16)			123,817	96,660	112,827	116,200	122,035
Adjusted EBIT							
UK	43,001	49,838	50,190	27,156	41,829	43,835	48,580
International	1,017	1,733	1,700	565	1,504	1,920	2,313
Total	44,018	51,571	51,890	27,721	43,333	45,755	50,893
EBIT (post IFRS16)			55,480	30,928	45,601	47,607	52,352
% Margin	14.5%	13.5%	14.3%	9.0%	12.3%	12.5%	13.5%
UK	15.8%	14.2%	15.2%	9.7%	13.1%	13.2%	14.2%
International	3.2%	5.3%	5.3%	2.1%	4.9%	5.9%	6.9%
Interest charge (pre IFRS 16)	-3,421	-4,742	-4,791	-4,448	-4,428	-4,328	-4,228
Adjusted PBT (pre amortisation)	40,597	46,829	47,099	23,273	38,905	41,427	46,665
PBT (post IFRS16)			46,640	23,176	38,808	41,330	46,568
Adjusted earnings	33,520	37,677	35,740	18,435	28,210	31,070	34,999
Adjusted Basic EPS (p) - pre IFRS 16	84.9	95.1	90.2	46.6	71.2	78.1	87.5
EPS growth rate	22.1%	12.0%	-5.2%	-48.4%	53.0%	9.6%	12.1%
Adjusted EPS diluted	83.9	92.9	88.8	45.8	70.5	77.3	86.6
Basic EPS (post IFRS16)			88.9	46.2	72.5	77.9	87.3
Dividend (pence)	26.0	30.2	8.5	47.0	36.0	38.6	43.3
Dividend growth	18.2%	16.2%	-72.0%	456.2%	-23.4%	7.3%	12.1%
Valuation benchmarks							
P/E ratio (pre IFRS 16)	8.4	7.5	7.9	15.4	10.0	9.2	8.2
P/E ratio (post IFRS 16)			8.0	15.5	9.9	9.2	8.2
EV/Sales	1.4	1.1	1.1	1.4	1.2	1.1	1.1
EV/EBITDA (pre IFRS 16)	4.9	4.1	4.3	5.7	4.7	4.5	4.3
EV/EBITDA (post IFRS 16)			3.8	4.9	4.2	4.1	3.9
EV/EBITA (pre IFRS 16)	9.5	8.1	8.0	15.0	9.6	9.1	8.2
EV/EBITA (post IFRS 16)			8.5	15.3	10.4	10.0	9.1
PEG ratio	0.4	0.6	-1.5	-0.3	0.2	1.0	0.7
Dividend yield	3.6%	4.2%	1.2%	6.6%	5.0%	5.4%	6.1%
Dividend cover	3.3	3.2	10.7	1.0	2.0	2.0	2.0
EBIT drop through rate (%)		9.5%	-1.6%	44.0%	36.4%	16.5%	46.8%
Corporate tax rate	-17.4%	-19.5%	-20.0%	-21.1%	-26.0%	-25.0%	-25.0%
Net debt / EBITDA (pre IFRS 16)	2.0	1.7	1.6	1.7	1.5	1.4	1.3
Return on average capital employed	14.8%	14.5%	14.5%	9.2%	14.5%	15.0%	15.0%
Net cash/(debt) - pre IFRS16	-179,172	-168,100	-159,806	-121,906	-130,604	-130,000	-124,793
Fleet capital expenditure (gross)	64,900	63,800	49,100	40,200	59,800	55,000	60,000
Investment as % sales	21.4%	16.7%	13.5%	13.1%	17.0%	15.0%	15.9%
Reported sharecount Ks (net Treasury)	39,476	39,603	39,618	39,595	39,597	39,795	39,994
Shareprice (p)	715						

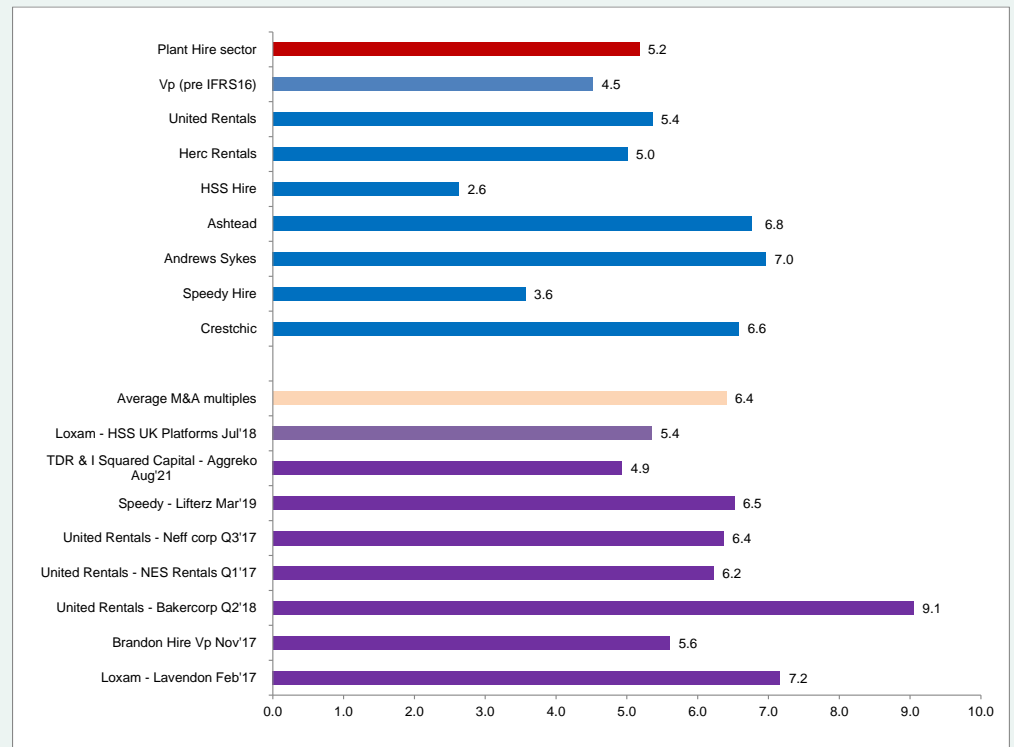
Source: Equity Development – FY21 includes special dividend of 22p/share

Key risks

- In light of Vp's operational gearing, if the economy stalled then this could impact earnings as costs are predominantly fixed. That said, investment in the hire fleet can be flexed as conditions change.
- Competitive pricing pressures and higher interest rates that could lift funding costs.
- 50.26% of the equity is owned by a number of trusts connected to Exec-Chairman Jeremy Pilkington (re possible hypothetical impact on minority interests), although this should also help ensure the group is run to maximise shareholder value.

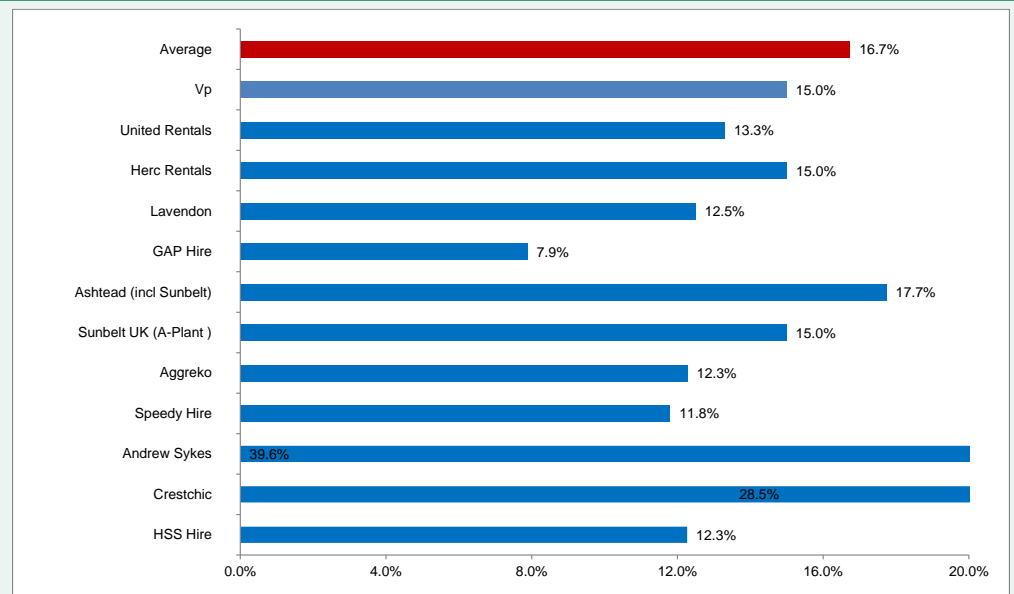
Appendices - sector valuation metrics and KPIs

Current Year (CY) EV / EBITDA multiples vs peers



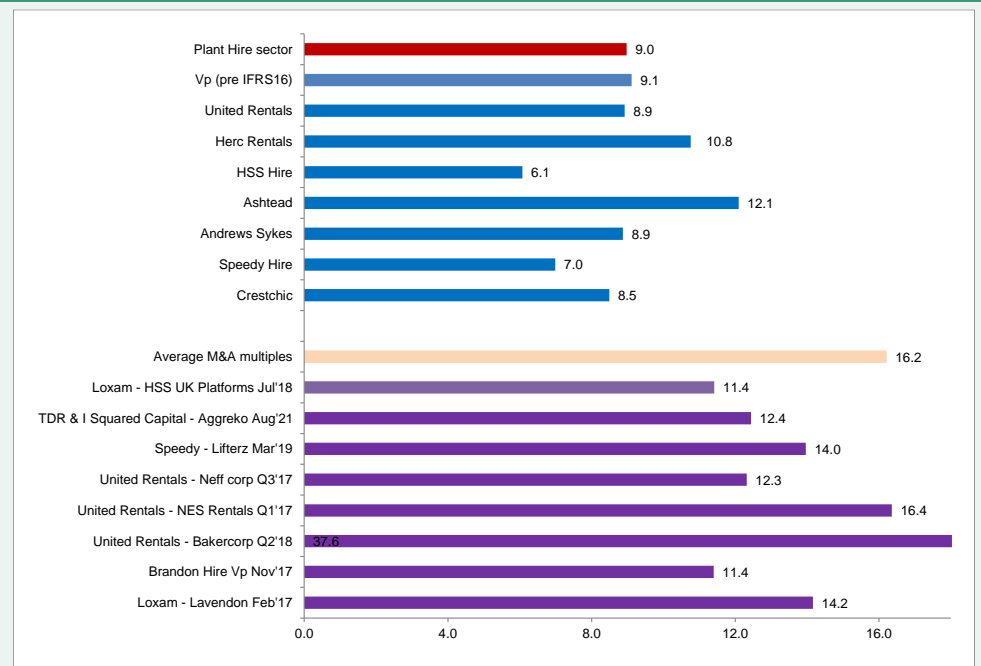
Source: Equity Development

CY % ROCE vs peers



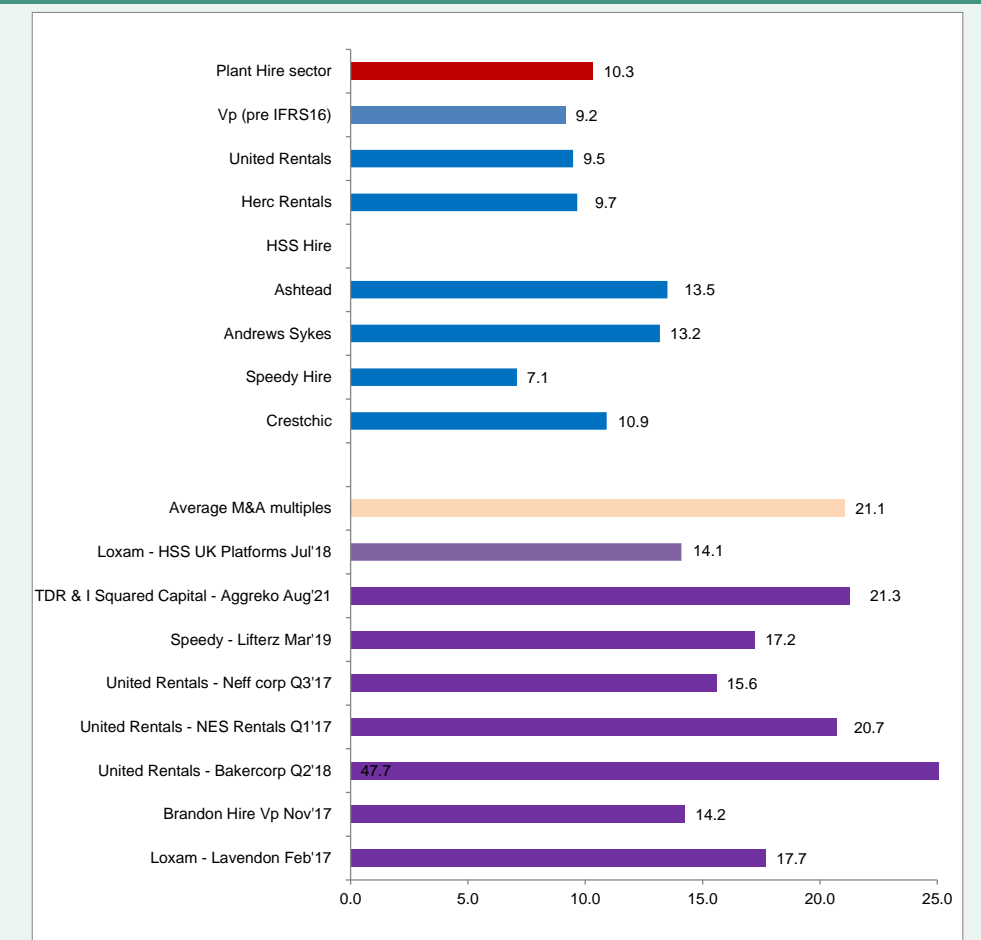
Source: Equity Development

Current Year (CY) EV / EBIT multiples vs peers



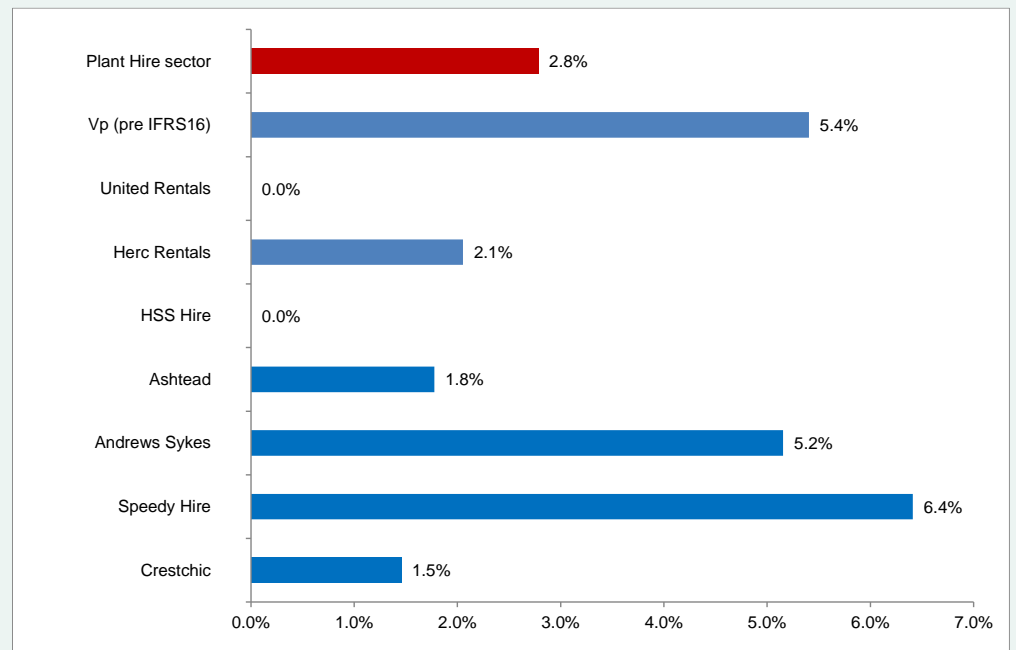
Source: Equity Development

CY PERs vs peers



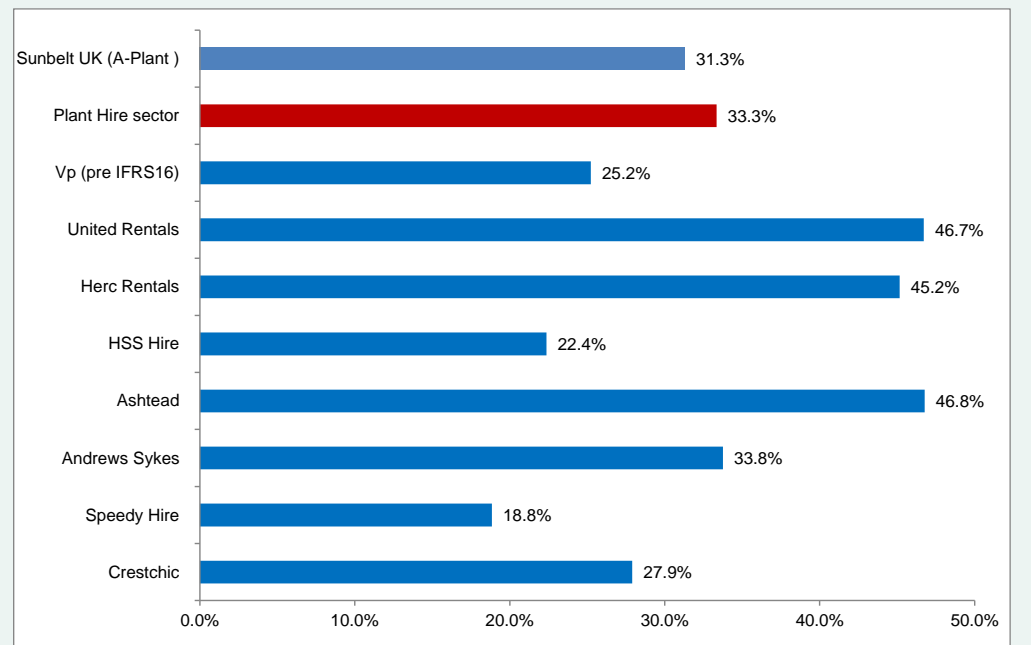
Source: Equity Development

CY dividend yield vs peers



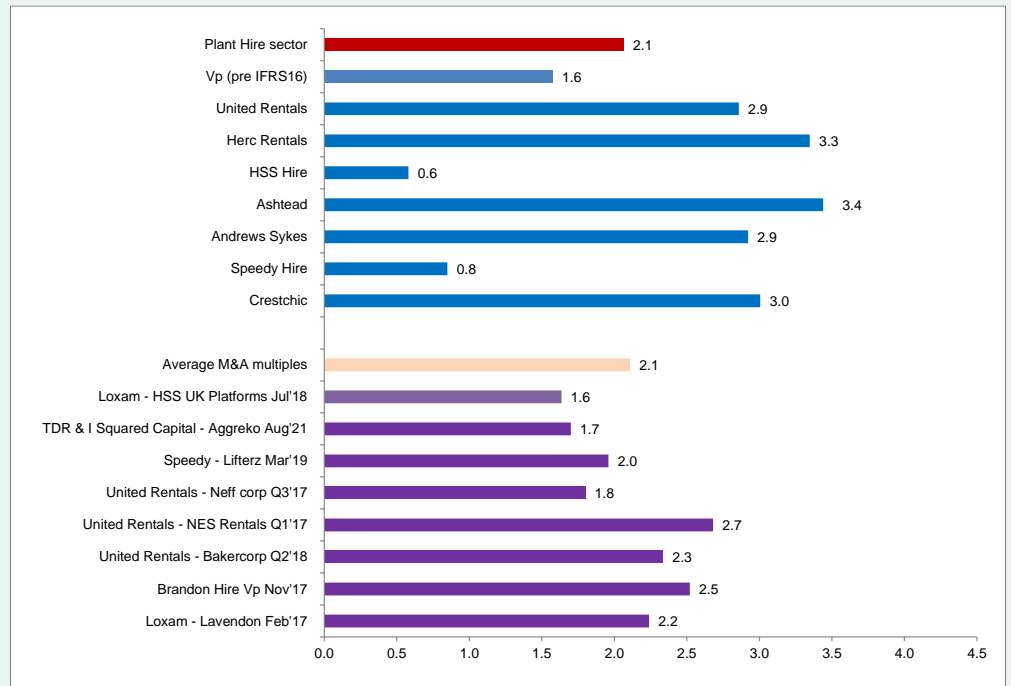
Source: Equity Development

CY % EBITDA margins vs peers



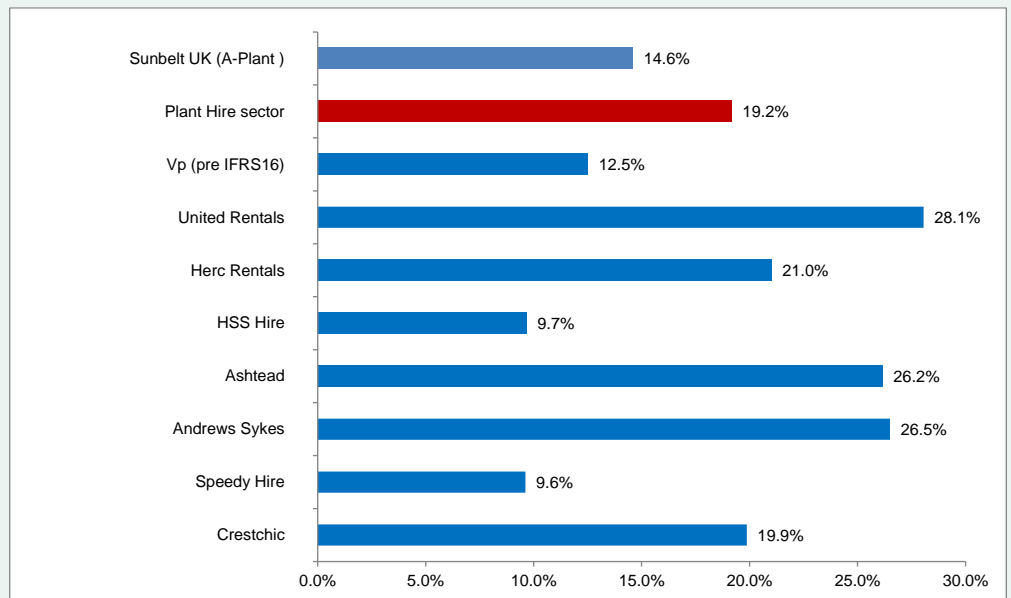
Source: Equity Development

CY Price: Book



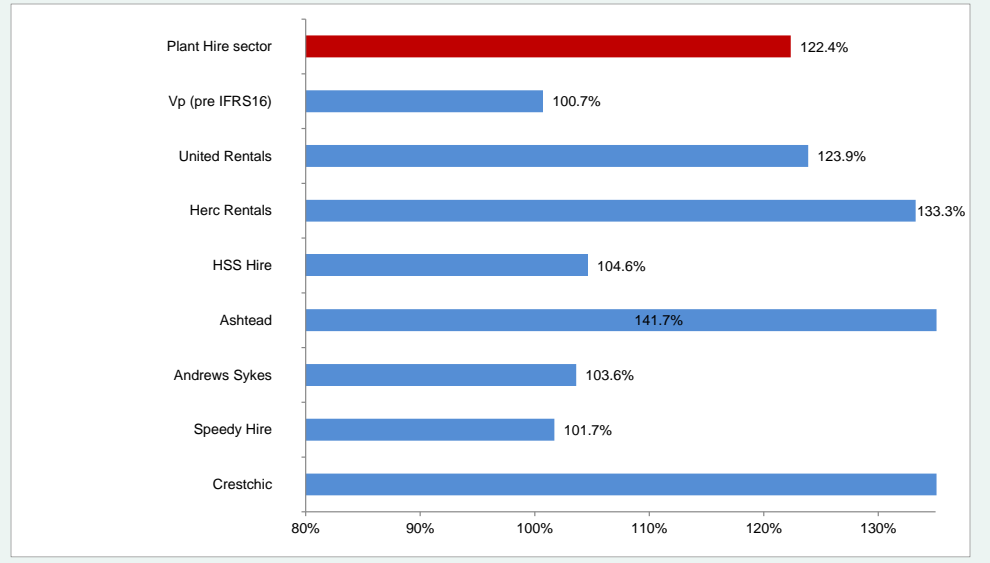
Source: Equity Development

CY % EBIT margins vs peers



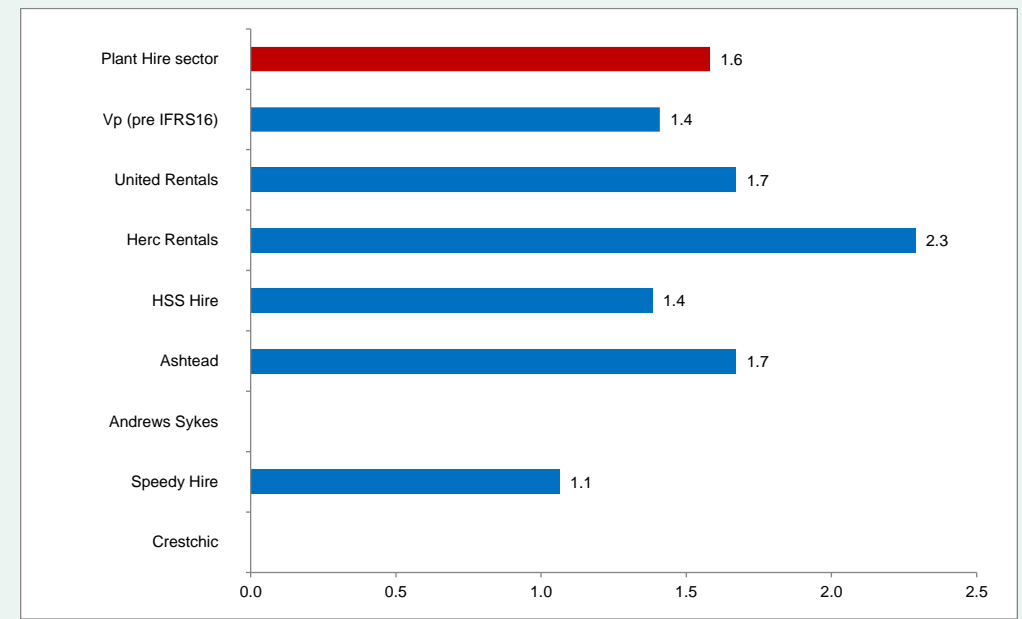
Source: Equity Development

Current year sales as a % of pre Covid levels



Source: Equity Development.

CY Net debt : EBITDA



Source: Equity Development

Market capitalisation of peers

	Shareprice	Mrk Cap (Ms)	CY net cash / (debt) Ms	Enterprise Value (Ms)
Crestchic	275.0p	£81.5	£2.5	£79.0
Speedy Hire	39.0p	£195	-£83	£278
Andrews Sykes	485p	£205	£17	£188
Ashtead	\$4,820.7	\$21,597	-\$7,088	\$28,685
HSS Hire	13.5p	£94.0	-£104.6	£198.6
Herc Rentals	\$112.0	\$3,270	-\$2,754	\$6,024
United Rentals	\$285.0	\$19,950	-\$9,048	\$28,998
Vp	715p	£287	-£130	£417

Source: Equity Development



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