

Brandon acquisition was a masterstroke

4th June 2019

M&A doesn't always work, such as RBS' disastrous €71bn acquisition of ABN Amro in 2007, and Hewlett-Packard's £10.2bn take-over of Autonomy 4 years later. However, where the stars and genetics align, then the outcome can be materially beneficial for all stakeholders.

Take Vp's £69.2m purchase of Brandon Hire in Nov'17, which at the time was generating c. £6.0m of EBIT. Here there was not only a compelling logic and cultural fit, but also the risks were appropriately priced and the integration executed in line with plan.

On track to generate >£4m pa of synergies

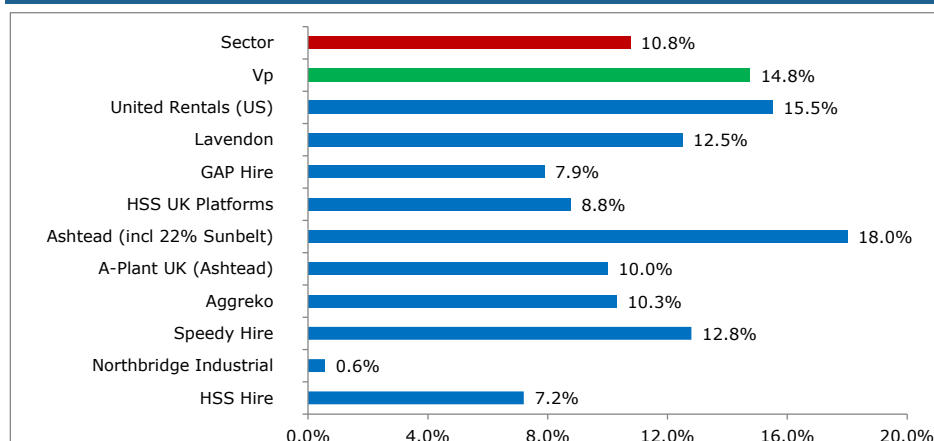
What's more 18 months on, we reckon Vp is on track to deliver >£4m pa of synergies by Dec'19, thanks mostly to cost/procurement savings, economies of scale and greater asset/inventory utilisation. In turn, boosting the original RoI to around 14% from 8.7% initially – and significantly above Vp's 'through cycle' cost of capital, even after allowing for £3.5m of exceptional costs, split £3.0m FY19 and £0.5m FY18. CEO Neil Stothard adding **"synergies identified have already been delivered, and margins & returns have improved considerably"**.

But that's not all. The rest of the group, particularly those units associated with UK construction, infrastructure and housebuilding, are delivering against expectations too.

Trading in line with expectations

FY19 revenues, adjusted EBITDA, PBTA, EPS and the dividend **all climbed to record levels** of £382.8m (+26%), £101.3m (+20%), £46.8m (+15%), 95.1p (+16%) and 30.2p (+16%) respectively. Sure ROCE dropped slightly to 14.5% (vs 14.8% LY), yet this was simply a function of owning Brandon for a full 12 months and is towards the top end of the peer group anyway (see below).

Current year (CY) ROCE (includes intangibles)



Source: Equity Development (arithmetic average for sector).

Company Data

EPIC	LSE: VP.
Price (last close)	730p
52 week Hi/Lo	1,230p/696p
Market cap	£293m
March '19 net debt	£174m
Share count	40.154m
ED valuation/share	£11.50
Daily volume	6,000

Share Price, p



Source: Share Cast

Description

Vp is a specialist 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, but also from overseas.

In terms of sector split: 34.6% H1'19 sales came from infrastructure, 40.6% construction, 8.9% housing building, 8.2% oil & gas and 7.7% other.

Member of FTSE SmallCap Index.

Next news: AGM in late June 2019

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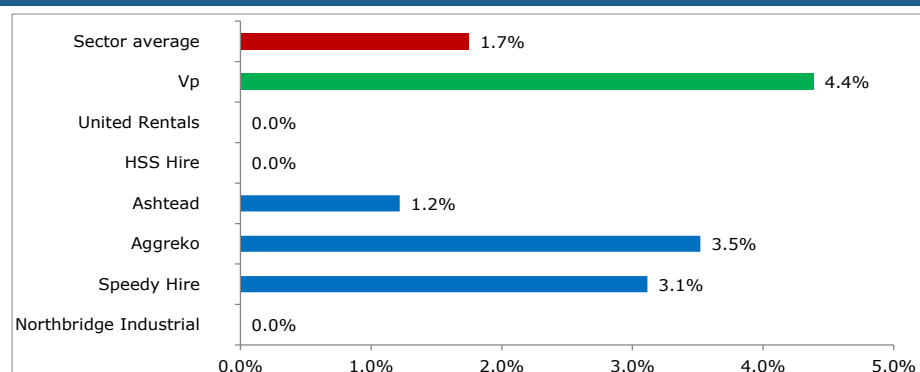
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Prospective 7.3x PER and a 4.4% dividend yield

Executive Chairman, Jeremy Pilkington, commenting **"Vp is reporting another strong set of full year results, with key financial metrics ahead of last year. In light of these excellent figures, I am pleased to announce a final dividend recommendation of 22.0p, making a total for the year of 30.2p/share, an increase of 16% on last year"**.

"We have entered the new financial year in excellent shape, and we look forward to the challenges and opportunities of the future with confidence and excitement".

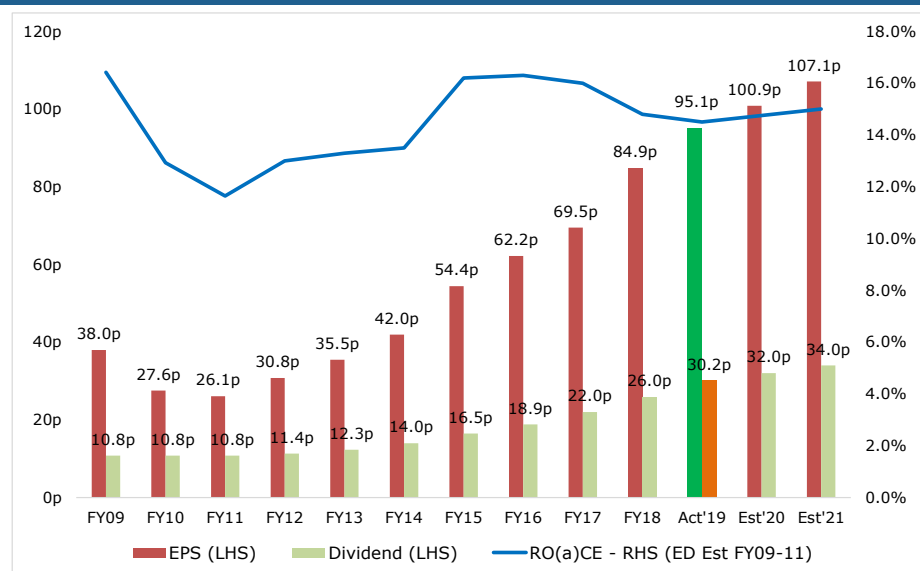
CY Dividend yield



Source: Equity Development.

Long term value creation

Positive long term shareholder returns



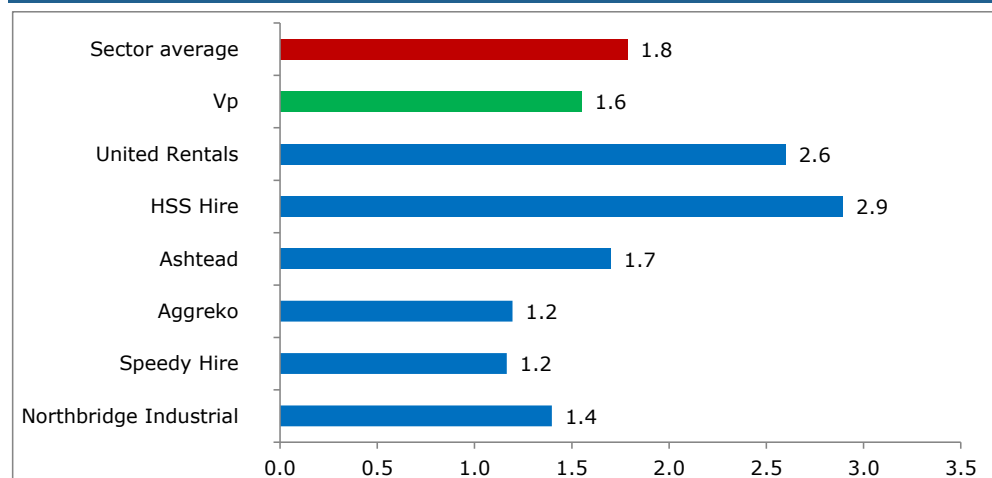
Source: Equity Development

Comfortable gearing level, and set to fall further

Likewise costs and cashflow are being tightly managed, with **net debt declining to £168.1m** (vs £179.2m LY) - equivalent to a comfortable EBITDA multiple of 1.7x, falling to 1.6x 12 months' later (see below) - despite investing £63.8m on fleet capex, offset by £20m (£18.5m

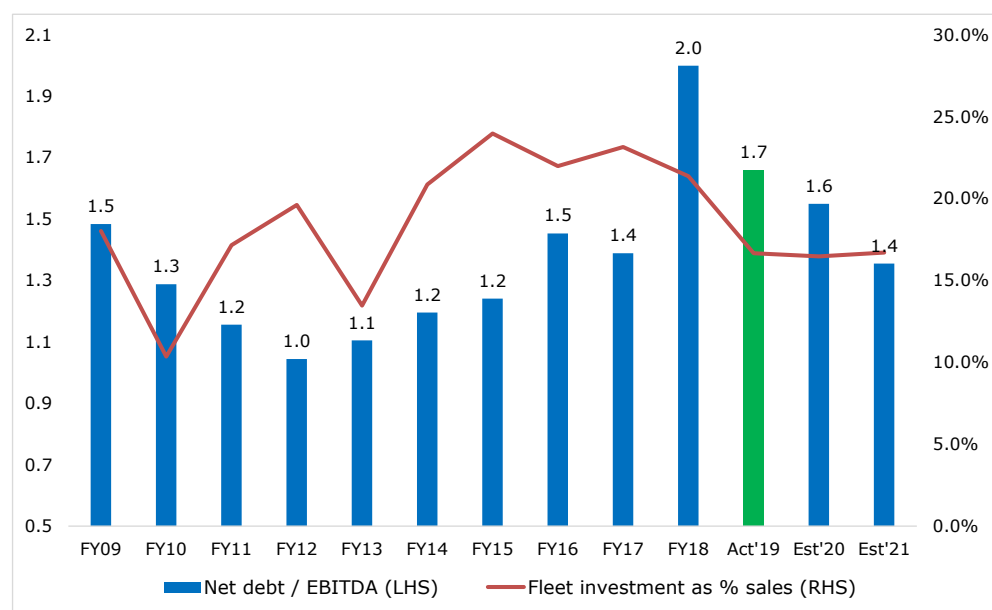
LY) of equipment disposals. Post period end, Vp snapped up Sandhurst Limited for £3.33m, a specialist excavator attachment rental firm which complements the UK Piling business.

Current year (CY) net debt to EBITDA ratios



Source: Equity Development (arithmetic average for sector)

Strong balance sheet



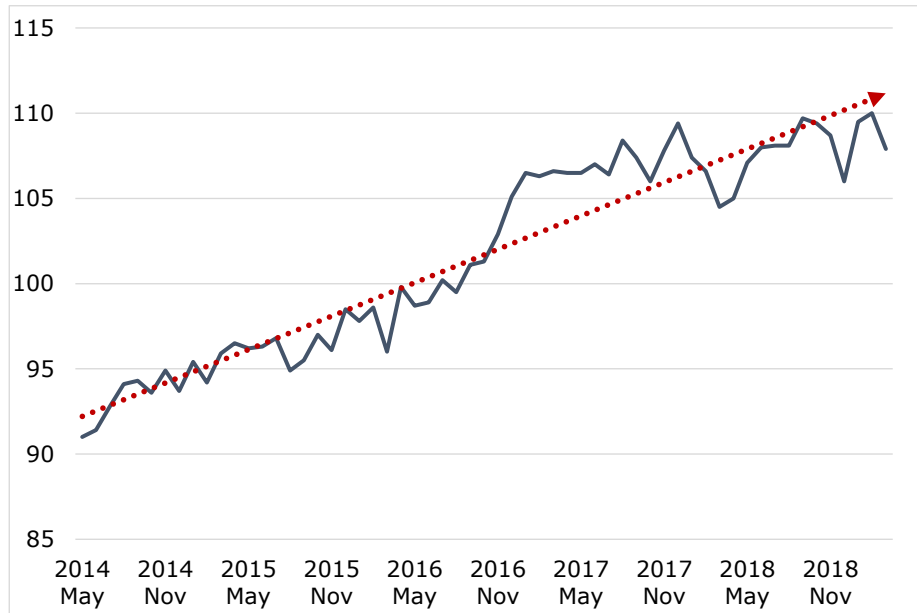
Source: Equity Development

Domestic demand remains supportive...

From a macro perspective, we don't think the UK economy is about to seize up either, irrespective of the ongoing Brexit miasma hanging over the market. In fact if anything, we suspect Chancellor Philip Hammond and Bank of England Governor Mark Carney would probably stimulate GDP further under a 'no deal' scenario.

Granted house price appreciation has been slowing for some time, especially in central London, yet equally the fundamentals for new-build are robust, reflecting near-record levels of employment, low interest rates, good mortgage availability and the Government's popular Help to Buy scheme.

Index of UK construction output

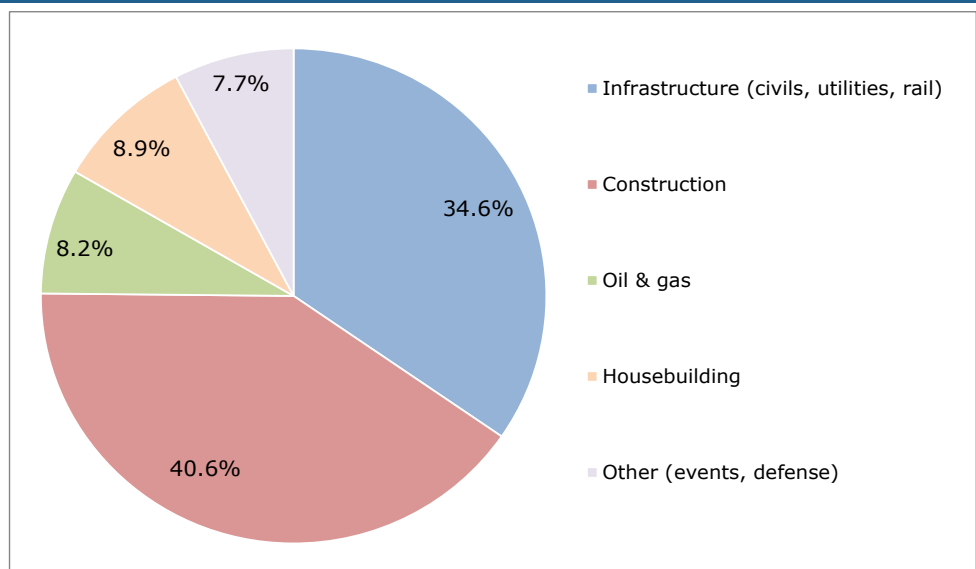


Source: ONS (10th May 2019)

.. which continues to drive UK operations forward

Divisionally, the **UK was the standout**, contributing 91.5% and 96.7% respectively of total revenues and EBIT – due to robust performances from construction, housebuilding, AMP6 water spend and infrastructure (re Hire Station and Groundforce). Indeed a number of major sites were serviced, including Battersea Power Station, Hinkley Point and the Luton Airport Dart project. Although partially offset by a more challenging environment in general construction and the delayed 5G wireless network roll out.

Estimated FY'19 revenue (£382.8m) split by market



Source: Equity Development

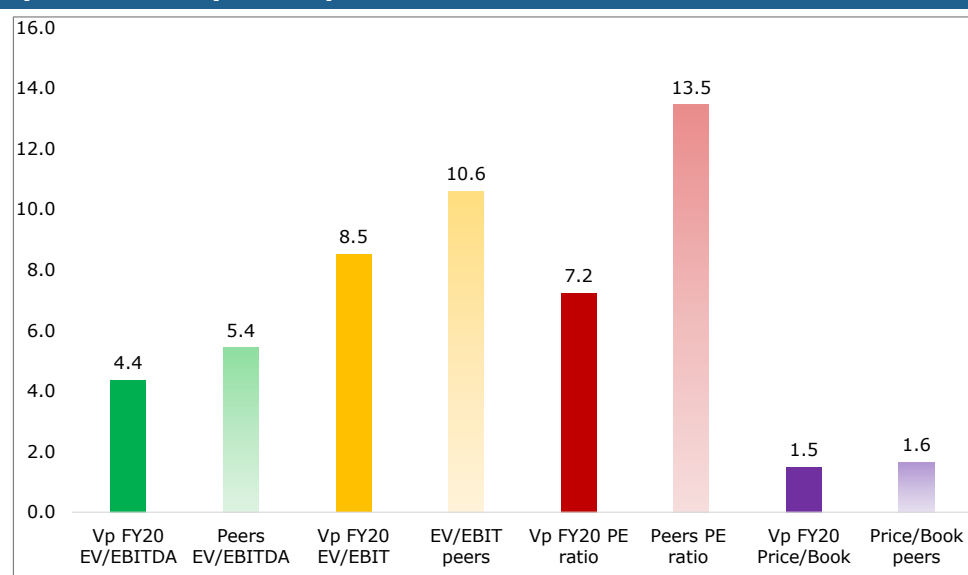
...alongside improving overseas markets

Internationally, Airpac Bukom continued to experience tough conditions within oil/gas, albeit it did see “tentative signs of improvement” as the year progressed, and expects a better FY20 thanks to greater client activity. Elsewhere, TR delivered in line with plan and has several exciting product/service offers planned for this year and beyond.

No change to forecasts or £11.50/share valuation

Looking ahead, **we have retained our FY20 PBT forecasts and £11.50p/share valuation** – offering potential >55% upside to investors. Additionally, the stock at 730p appears substantially undervalued on just about all metrics (see below/appendices), especially considering its strong cash generation and robust balance sheet.

Vp FY20 multiples vs peers



Source: Equity Development

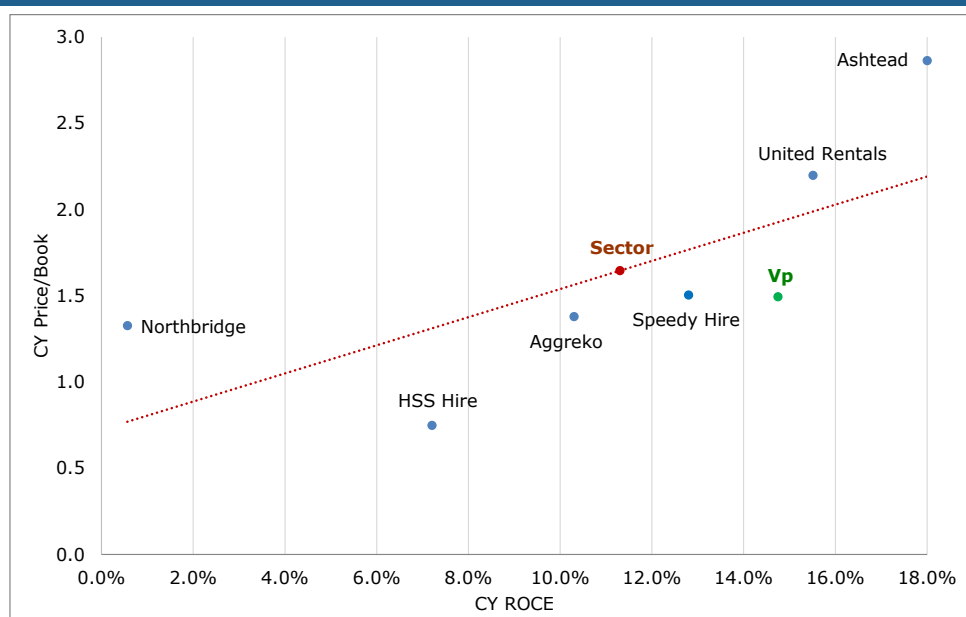
Confident outlook underpinned by solid fundamentals

CEO, Neil Stothard concluding “**Vp has started the new financial year positively and in line with our expectations. We anticipate that our main markets in the UK will continue to be supportive**, but with slightly slower overall growth than experienced in recent years influenced by the current political and economic uncertainty.

I am pleased to say that the international backdrop is also broadly positive, with opportunities in Australasia with TR Group and the wider oil and gas exploration and maintenance sectors too.”

“The year ended 31 March 2019 was one of significant development for Vp, and **we were particularly pleased with the quality of the Brandon Hire integration.**”

Current Year ROCE vs Price: Book



Source: Equity Development

£4.5m one-off provision made for CMA investigation

Lastly, it is worth mentioning the ongoing Competition and Markets Authority (CMA) investigation. Here, the CMA has provisionally concluded that 3 major suppliers of groundwork products – including Vp's Groundforce unit - were involved in suspected anti-competitive behaviour.

The findings are however provisional at this stage, and do not mean that any company breached competition law. As such, it is impossible to accurately assess the likely costs associated with this enquiry. Nonetheless, in line with accounting standard IAS 37, Vp has included an exceptional charge of £4.5m within its FY19 accounts.

The figure is in the arithmetic midpoint of a range of possible outcomes (£0m to £9.0m) that the Board have calculated based upon previous cases and CMA published guidance – importantly though without any admission of blame. Consequently, whilst the case is undoubtedly something to watch, **we suspect that it won't ultimately end up being material in the context of the Group's £293m market capitalisation.**

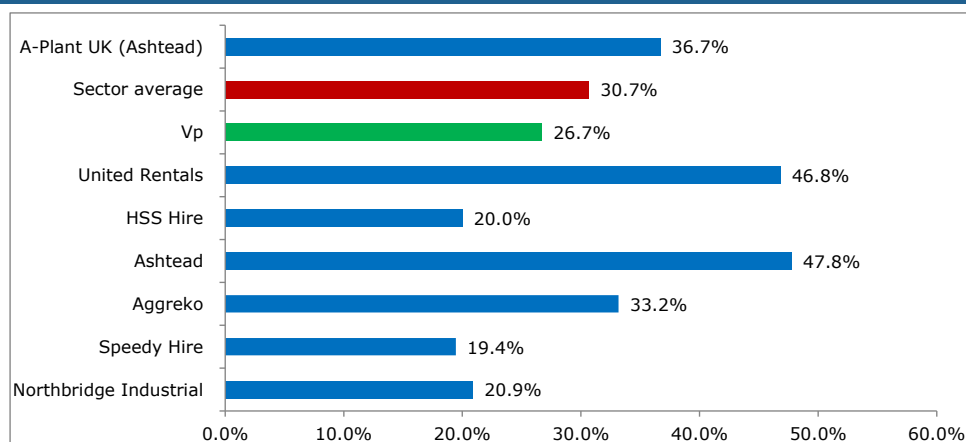
Forecasts (£'000s)

Vp (March year end)	2015 Act £'000s	2016 Act £'000s	2017 Act £'000s	2018 Act £'000s	2019 Act £'000s	2020 Est £'000s	2021 Est £'000s	2022 Est £'000s	2023 Est £'000s
Turnover									
UK	184,142	193,555	220,015	271,989	350,330	360,840	371,665	382,815	394,300
International	21,460	15,191	28,725	31,650	32,500	33,800	35,152	36,558	38,020
Total	205,602	208,746	248,740	303,639	382,830	394,640	406,817	419,373	432,320
% growth	12.3%	1.5%	19.2%	22.1%	26.1%	3.1%	3.1%	3.1%	3.1%
UK		5.1%	13.7%	23.6%	28.8%	3.0%	3.0%	3.0%	3.0%
International		-29.2%	89.1%	10.2%	2.7%	4.0%	4.0%	4.0%	4.0%
EBITDA	53,803	59,266	71,238	84,337	101,339	105,469	108,911	112,841	116,885
% Margin	26.2%	28.4%	28.6%	27.8%	26.5%	26.7%	26.8%	26.9%	27.0%
Adjusted EBIT									
UK	26,027	30,659	35,871	43,001	49,871	51,613	53,022	54,769	56,569
International	2,753	1,232	1,886	1,017	1,700	2,553	3,003	3,553	4,114
Total	28,780	31,891	37,757	44,018	51,571	54,166	56,025	58,322	60,683
% Margin	14.0%	15.3%	15.2%	14.5%	13.5%	13.7%	13.8%	13.9%	14.0%
UK	14.1%	15.8%	16.3%	15.8%	14.2%	14.3%	14.3%	14.3%	14.3%
International	12.8%	8.1%	6.6%	3.2%	5.2%	7.6%	8.5%	9.7%	10.8%
Underlying Interest charge	-2,023	-2,093	-2,906	-3,421	-4,742	-4,600	-4,400	-4,100	-3,800
Adjusted PBT (pre amortisation)	26,757	29,798	34,851	40,597	46,829	49,566	51,625	54,222	56,883
Adjusted earnings	21,201	24,226	27,262	33,520	37,677	40,148	42,849	45,004	47,213
Adjusted Basic EPS (p)	54.4	62.2	69.5	84.9	95.1	100.9	107.1	112.0	116.9
EPS growth rate	29.7%	14.3%	11.7%	22.1%	12.0%	6.0%	6.2%	4.5%	4.4%
Dividend (pence)	16.5	18.9	22.0	26.0	30.2	32.0	34.0	35.5	37.1
Valuation benchmarks									
P/E ratio	13.4	11.7	10.5	8.6	7.7	7.2	6.8	6.5	6.2
EV/Sales	2.2	2.2	1.9	1.5	1.2	1.2	1.1	1.1	1.1
EV/EBITDA	8.6	7.8	6.5	5.5	4.6	4.4	4.2	4.1	3.9
EV/EBITA	16.0	14.5	12.2	10.5	8.9	8.5	8.2	7.9	7.6
PEG ratio	0.5	0.8	0.9	0.4	0.6	1.2	1.1	1.4	1.4
Dividend yield	2.3%	2.6%	3.0%	3.6%	4.1%	4.4%	4.7%	4.9%	5.1%
Dividend cover	3.3	3.3	3.2	3.3	3.2	3.2	3.2	3.2	3.2
Corporate tax rate	-20.8%	-18.7%	-21.8%	-17.4%	-19.0%	-19.0%	-17.0%	-17.0%	-17.0%
Net debt / EBITDA (proforma)	1.2	1.5	1.4	2.0	1.7	1.6	1.4	1.2	1.0
Return on average capital employed	16.2%	16.3%	16.0%	14.8%	14.5%	14.8%	15.0%	15.3%	15.5%
Net cash/(debt)	-66,764	-86,134	-98,933	-179,172	-168,100	-163,500	-147,615	-130,575	-113,293
Fleet capital expenditure (gross)	49,300	45,900	57,600	64,900	63,800	65,000	68,000	70,000	73,000
Investment as % sales	24.0%	22.0%	23.2%	21.4%	16.7%	16.5%	16.7%	16.7%	16.9%
Reported sharecount Ks (net Treasury)	38,940	38,942	39,215	39,476	39,603	39,801	40,000	40,200	40,401
Shareprice (p)	730								

Source: Company historic data, ED estimates

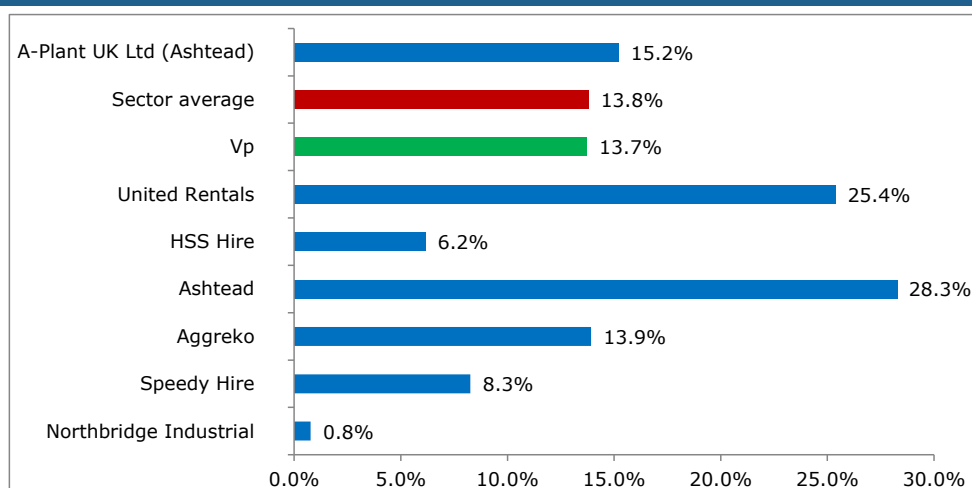
Appendix - Sector valuation metrics and KPIs

Current Year (FY20) EBITDA margins vs peers



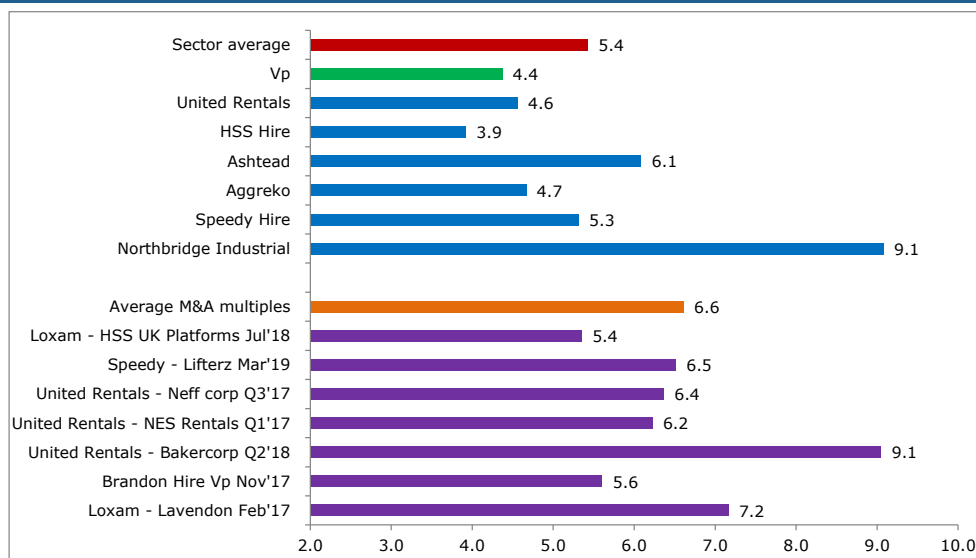
Source: Equity Development : arithmetic average for sector

Current Year (CY) EBIT margins vs peers



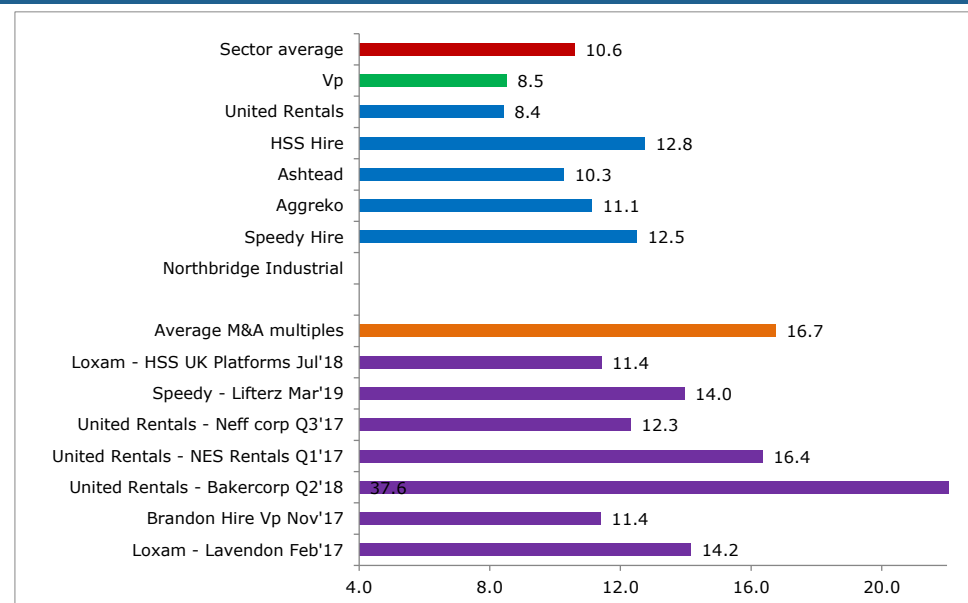
Source: Equity Development : arithmetic average for sector

CY EV / EBITDA



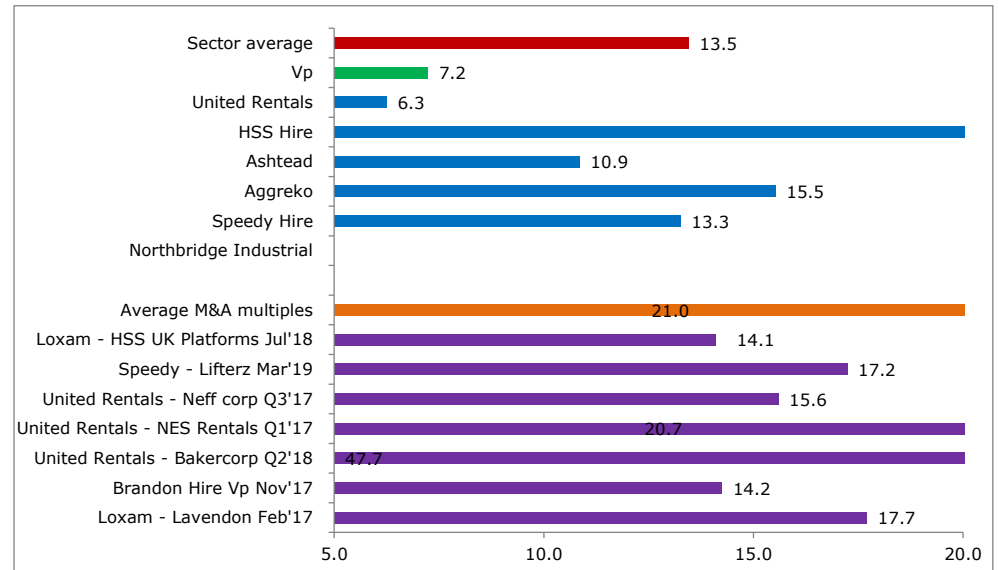
Source: Equity Development, arithmetic average for sector

CY EV / EBIT



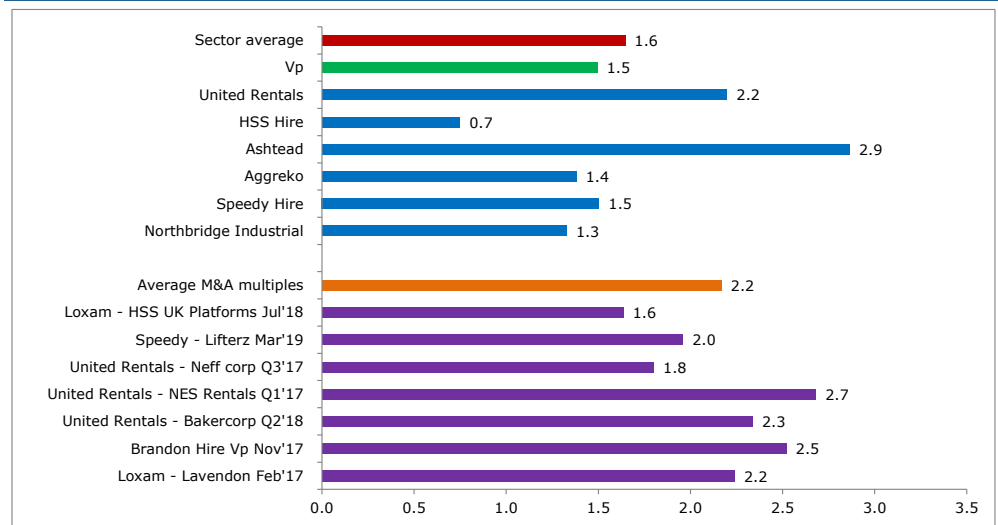
Source: Equity Development, arithmetic average for sector

CY PER



Source: Equity Development : arithmetic average for sector

CY Price : Book



Source: Equity Development : arithmetic average for sector

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 as occurred during the 2008/9 recession.
- Competitive pricing pressures and higher interest rates that could lift funding costs, albeit 40% of gross debt is fixed.
- Acquisition integration, albeit the management's track record to date has been good.
- 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.



Investor Access

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