Vp plc

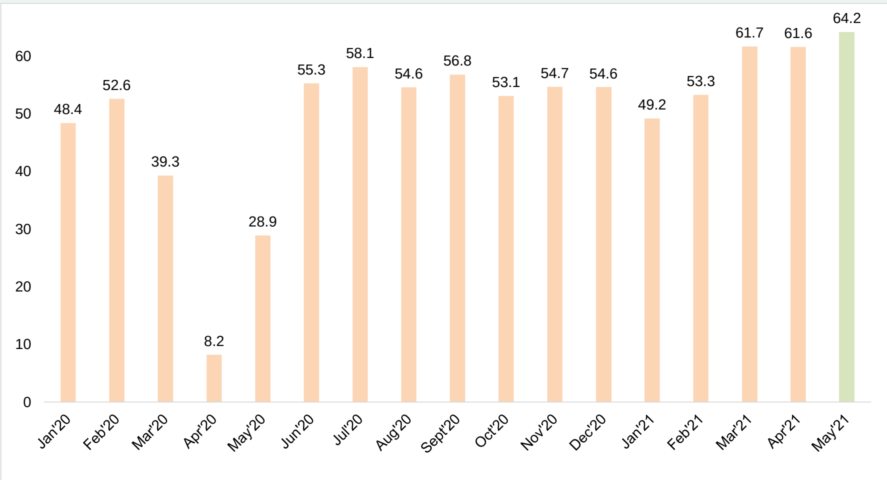
Upgrading forecasts as FY22 "*starts strongly*"

8th June 2021

Today's **upbeat FY21 prelims** from equipment rental specialist Vp provided further evidence of its industry leading status, especially in terms of earning quality, ROCE and cashflow. Posting a better than expected **adjusted PBT** (pre IFRS16) **& diluted EPS of £23.3m & 45.9p on sales of £308m,** alongside providing a "***positive***" outlook. Indeed in our opinion, the group's **through-cycle durability justifies a sector premium**, thanks to its consistent returns, adoption of all-things digital and exposure to systemically important verticals such as water, power, renewables, telecoms & rail.

However, **superior performance** is not the only attraction. Elsewhere, UK construction is powering ahead with May'21 PMIs hitting 64.2 (see below), boosted by home building, commercial, home DIY, RMI and infrastructure.

UK Construction Purchasing Managers Index (PMI)

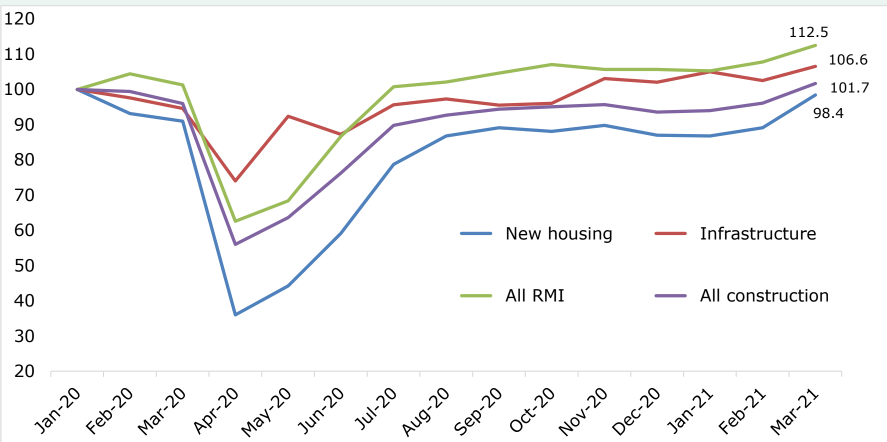


Source: Equity Development (>50 indicates expansion)

Delayed infrastructure projects set to accelerate growth

Similarly, there's a mountain of new work coming down the track (eg fibre-to-the-home, HS2, offshore wind, rail CP6, Hinkley Point, Water AMP7 & the Lower Thames crossing), which should more than offset any possible 'air-pocket' in demand caused by the ending of the UK's stamp duty holiday.

Favourable backdrop across UK Construction

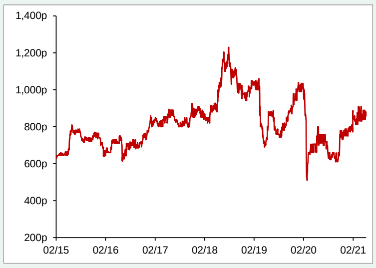


Source: ONS

Company Data

EPIC	LSE: VP.
Price (last close)	870p
52 weeks Hi/Lo	925p/605p
Market cap	£349m
Est. Mar22 net debt (ex IFRS16)	£123m
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 FY'20 turnover), but also overseas.

In terms of sector split: circa 40% sales is derived from infrastructure, 39% construction, 9% housing building, 7% oil & gas and 5% other.

Member of FTSE SmallCap Index.

Next news: AGM 22nd July 2021

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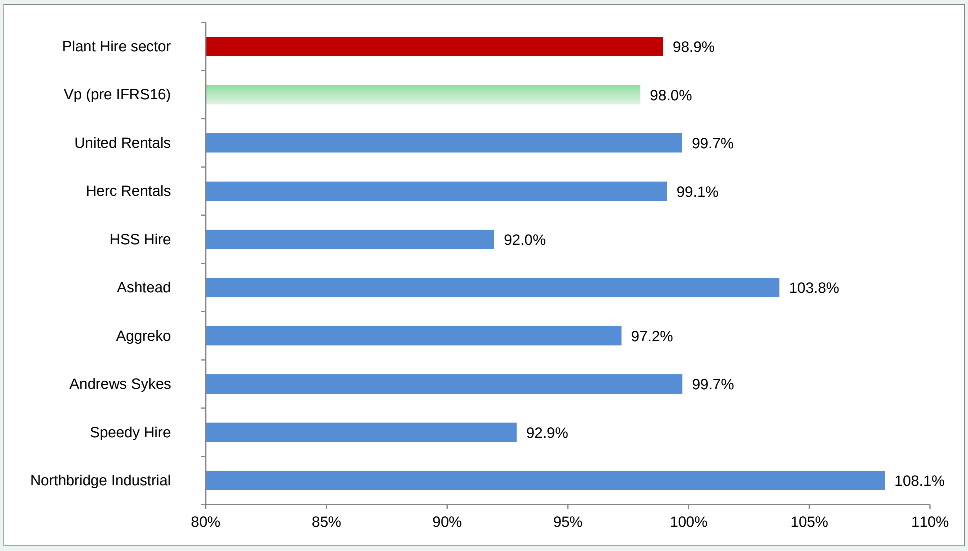
Favourable industry tailwinds

An optimistic view shared by not only the Construction Products Association, who reckon the industry will expand by 12.9% this year (vs -12.5% in 2020) and 5.2% next. But also the Bank of England, after recently lifting their 2021 GDP forecasts from 5% to 7.25% and 5.25% in 2022, due to pent-up demand, £200bn of excess household savings and the success of the NHS's vaccine rollout.

The only minor fly in the ointment being that global demand may actually be a little too hot, since it is causing material/labour shortages and hindering project activity.

Current year sales as a % of pre Covid levels



Source: Equity Development

Profitable despite the "*unprecedented challenges*" of Covid

Nonetheless, these supply chain disruptions should subside in due course. Something that already appears to be happening at Vp, with H2'21 results being significantly ahead of H1 (see below), augmented by £37.9m of cash inflow over the 12 months period.

All told, **adjusted FY21 EBITDA & EBITA and ROCE** (see below, pre IFRS 16) **came in at £72.7m** (£98.1m), **£27.7m** (£51.9m) **and 9.2%** (14.5%) respectively, on turnover -15.5% lower at £308m due to the Covid induced lockdowns. Equally though EBIT margins were 9.0% vs 14.3%, reflecting tight cost control and other overhead savings. Elsewhere, £15.1m of exceptionals were taken relating to a CMA regulatory review and restructuring costs.

Resumption of dividends thanks to excellent cash generation

In relation to the balance sheet, **net bank debt fell to £121.9m** (1.7x EBITDA) benefitting from reduced fleet capex (£40.2m vs £49.1m) and lower debtor days. Leaving plenty of scope to reinstate **a progressive 25p dividend policy** (vs 22p) - equivalent to an **inflation beating 2.9% yield** – with the future payout ratio likely to rise from 33% to nearer 40% of EPS over time.

Resilient FY21 performance

£'000s March yearend	Act H1'20	Act H1'21	%	Act H2'20	Act H2'21	%	Act FY20	Act FY21	%
UK sales	170,016	128,880	*-24.2%*	160,989	152,429	*-5.3%*	331,005	281,309	*-15.0%*
International	16,569	13,209	*-20.3%*	15,353	13,479	*-12.2%*	31,922	26,688	*-16.4%*
Group revenues	**186,585**	**142,089**	***-23.8%***	**176,342**	**165,908**	***-5.9%***	**362,927**	**307,997**	***-15.1%***
Group EBITDA	**51,840**	**34,079**	***-34.3%***	**49,710**	**48,340**	***-2.8%***	**98,050**	**72,701**	***-25.9%***
EBITDA % margin	*27.8%*	*24.0%*		*28.2%*	*29.1%*		*27.0%*	*23.6%*	
EBITDA (post IFRS 16)		*47,444*			*49,216*			*96,660*	
UK	27,245	9,921	*-63.6%*	22,945	17,235	*-24.9%*	50,190	27,156	*-45.9%*
International	1,070	879	*-17.9%*	630	-314	*-149.8%*	1,700	565	*-66.8%*
Group EBITA	**28,315**	**10,800**	***-61.9%***	**23,575**	**16,921**	***-28.2%***	**51,890**	**27,721**	***-46.6%***
EBITA (post IFRS 16)		*12,417*			*18,511*			*30,928*	
UK	*16.0%*	*7.7%*		*14.3%*	*11.3%*		*15.2%*	*9.7%*	
International	*6.5%*	*6.7%*		*4.1%*	*-2.3%*		*5.3%*	*2.1%*	
EBIT % margin	***15.2%***	***7.6%***		***13.4%***	***10.2%***		***14.3%***	***9.0%***	
Interest	-2,383	-2,193	*-8.0%*	-2,359	-2,255	*-4.4%*	-4,742	-4,448	*-6.2%*
PBTA	**25,932**	**8,607**	***-66.8%***	**21,167**	**14,666**	***-30.7%***	**47,099**	**23,273**	***-50.6%***
PBTA (post IFRS16)		8,477			*14,699*			23,176	
Adj EPS - pre IFRS16	**52.5p**	**17.4p**	***-66.8%***	**37.8p**	**29.2p**	***-22.5%***	**90.2p**	**46.7p**	***-48.3%***
Adj EPS - post IFRS16		16.8p			*29.3p*			46.2p	
Dividend	**8.5p**	**22.0p**	***160.4%***	**0.0p**	**25.0p**		**8.5p**	**47.0p**	
Net debt (pre IFRS 16)	-183,746	-118,702	*-35.4%*	-159,806	-121,906	*-23.7%*	-159,806	-121,906	*-23.7%*
Net debt : EBITDA							1.6	1.7	
Group ROCE	***14.5%***	***10.3%***		***14.5%***	***9.2%***		***14.5%***	***9.2%***	

Source: Equity Development.

Ok, but what about the road ahead?

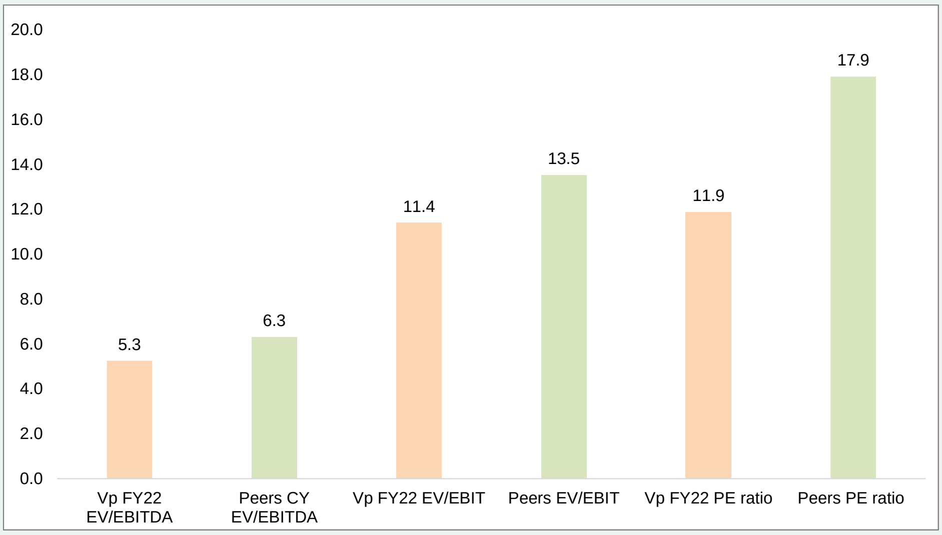
Well, despite the 3rd national lockdown prospects have improved dramatically over the past 6 months, with current trading described as "***strong***", which we have interpreted as being just below pre-Covid levels with Groundforce awaiting the usual upswing once AMP7 (water) becomes fully operational.

Consequently **we have upgraded are FY22 forecasts** to **adjusted PBT of £36.9m** (vs £33.5m B4) **on turnover of £355.7m** (£345m) – ending the year with **£123m of net debt.** The latter factoring in **continued working capital control**, offset by greater fleet capex (£50m).

Shares remain undervalued

Similarly **our valuation ticks up from £11.00 to £11.30/share**. Meaning the shares at 870p trade on modest 11.9x PER, 11.4x EV/EBIT and 5.3x EV/EBITDA multiples vs peer group averages.

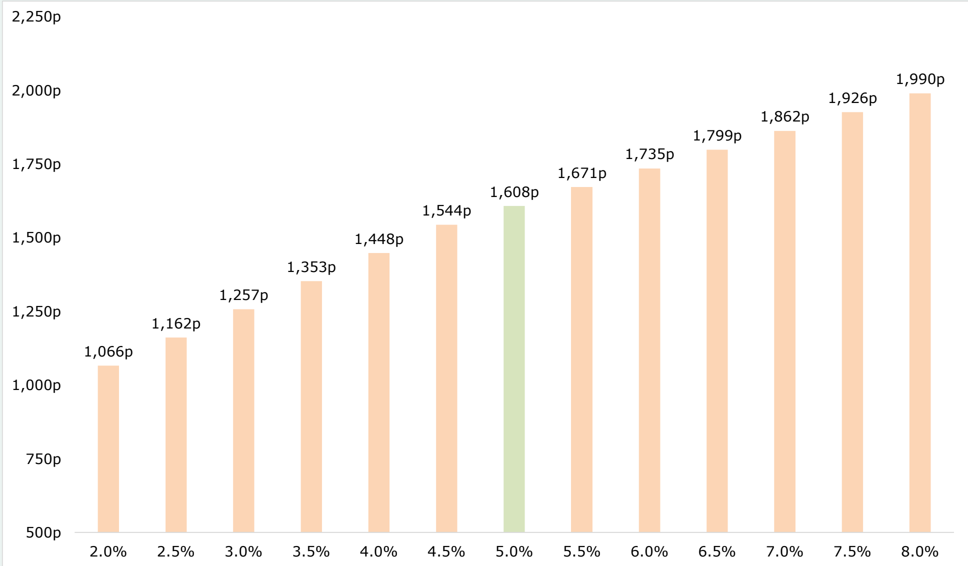
Vp valuation benchmarks vs peers



Source: Equity Development.

What's more, further out we think the stock could readily migrate towards £16.08 by 2024 (see below) - assuming 5% organic top line growth can be achieved across the economic cycle.

Hypothetical **Vp shareprice by 2024 at a range of LFL growth rates**



Source: Equity Development hypothetical price estimates

Plus, eventually Vp may even be able to surpass its own stretching 15% ROCE target (re operating leverage) thanks to a **leaner cost base** & **favourable operating leverage**, augmented by **industry leading ESG credentials** and **digital solutions** (eg online self-service ordering) to take advantage of the post-pandemic world.

"The market backdrop for Vp is very positive"

CEO Neil Stothard commenting: ***"We finished FY21 well*** *[at 95% pre-covid levels]* ***and I am pleased to confirm that we have maintained this into April and May of the new financial year, which has started strongly for us****.*

"Looking ahead, major infrastructure sectors, such as water, rail and transmission are primed for escalating growth in the coming year, added to which other major projects such as HS2 and Hinkley Point will continue to drive demand. We see the residential construction market continuing to be supportive as housebuilders maintain their build programmes. Whilst the general construction sector has been slightly slower to recover, we are seeing positive signs of a sustained improvement in this key and large market.

We are excited about the prospects for the coming year which we approach with increasing confidence."

Executive Chairman Jeremy Pilkington adding: "*As we hopefully return to more normal trading conditions, uninhibited by Government restrictions,* ***we feel the market backdrop for Vp is very positive****. Particularly in the UK, major infrastructure and levelling up projects provide significant upside growth opportunities for the Group over the immediate and longer term.* ***Internationally the prospects for our energy business look better now than they have for some time*** *and the TR business appears set to benefit from effective local pandemic responses. E****xtended supply chains and shortages of certain construction materials provide some challenges in the short term and against which we have taken mitigation measures wherever possible***."

Key risks

- COVID-19 related impacts to demand, customers and building investment.
- 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. Mitigated by c.70% of gross debt being fixed, although falling over the next 3 years (Re £65m fixed rate private placement).
- 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.

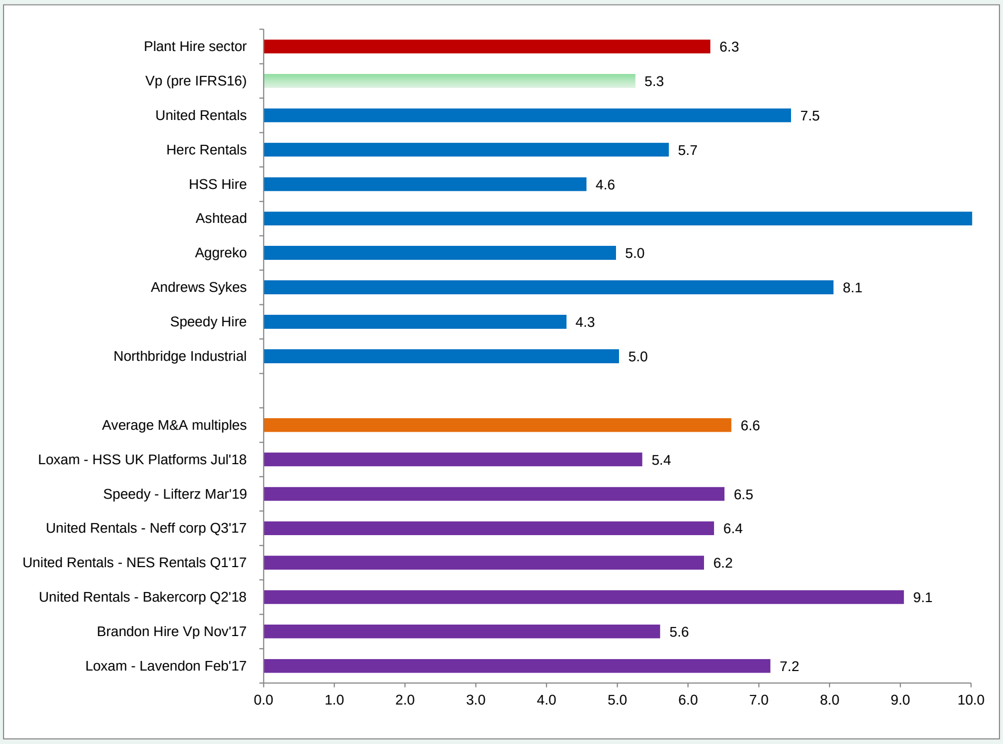
Summary projections

Vp (March year end)	2018 Act £'000s	2019 Act £'000s	2020 Act £'000s	2021 Act £'000s	2022 Est £'000s	2023 Est £'000s	2024 Est £'000s
Turnover							
UK	*271,989*	*350,330*	*331,005*	*281,309*	*324,385*	*343,848*	*354,163*
International	*31,650*	*32,500*	*31,922*	*26,688*	*31,284*	*33,161*	*34,155*
Total	**303,639**	**382,830**	**362,927**	**307,997**	**355,668**	**377,009**	**388,319**
% growth	***22.1%***	***26.1%***	***-5.2%***	***-15.1%***	***15.5%***	***6.0%***	***3.0%***
UK	*23.6%*	*28.8%*	*-5.5%*	*-15.0%*	*15.3%*	*6.0%*	*3.0%*
International	*10.2%*	*2.7%*	*-1.8%*	*-16.4%*	*17.2%*	*6.0%*	*3.0%*
EBITDA	**84,337**	**101,339**	**98,050**	**72,701**	**89,890**	**95,880**	**101,891**
% Margin	*27.8%*	*26.5%*	*27.0%*	*23.6%*	*25.3%*	*25.4%*	*26.2%*
EBITDA (post IFRS16)			*123,817*	*96,660*	*113,849*	*119,839*	*125,850*
Adjusted EBIT							
UK	*43,001*	*49,838*	*50,190*	*27,156*	*38,926*	*42,981*	*47,812*
International	*1,017*	*1,733*	*1,700*	*565*	*2,503*	*2,984*	*3,416*
Total	**44,018**	**51,571**	**51,890**	**27,721**	**41,429**	**45,965**	**51,228**
EBIT (post IFRS16)			55,480	30,928	42,698	46,753	51,584
% Margin	***14.5%***	***13.5%***	***14.3%***	***9.0%***	***11.6%***	***12.2%***	***13.2%***
UK	*15.8%*	*14.2%*	*15.2%*	*9.7%*	*12.0%*	*12.5%*	*13.5%*
International	*3.2%*	*5.3%*	*5.3%*	*2.1%*	*8.0%*	*9.0%*	*10.0%*
Interest charge (pre IFRS 16)	-3,421	-4,742	-4,791	-4,448	-4,500	-4,400	-4,300
Adjusted PBT (pre amortisation)	**40,597**	**46,829**	**47,099**	**23,273**	**36,929**	**41,565**	**46,928**
PBT (post IFRS16)			46,640	23,176	36,832	41,468	46,831
Adjusted earnings	**33,520**	**37,677**	**35,740**	**18,472**	**29,137**	**32,795**	**35,196**
Adjusted Basic EPS (p) - pre IFRS 16	**84.9**	**95.1**	**90.2**	**46.7**	**73.2**	**82.0**	**87.6**
EPS growth rate	*22.1%*	*12.0%*	*-5.2%*	*-48.3%*	*57.0%*	*12.0%*	*6.8%*
Adjusted EPS diluted	***83.9***	***92.9***	***88.8***	***45.9***	***72.1***	***80.7***	***86.2***
Basic EPS (post IFRS16)			*88.9*	*46.2*	*73.0*	*81.8*	*87.4*
Dividend (pence)	**26.0**	**30.2**	**8.5**	**47.0**	**30.0**	**32.0**	**34.0**
Dividend growth	*18.2%*	*16.2%*	*-72.0%*	*456.2%*	*-36.2%*	*6.7%*	*6.3%*
Valuation benchmarks							
P/E ratio (pre IFRS 16)	*10.2*	*9.1*	*9.6*	*18.6*	*11.9*	*10.6*	*9.9*
P/E ratio (post IFRS 16)			*9.8*	*18.8*	*11.9*	*10.6*	*10.0*
EV/Sales	*1.6*	*1.2*	*1.3*	*1.5*	*1.3*	*1.3*	*1.2*
EV/EBITDA (pre IFRS 16)	*5.6*	*4.7*	*4.8*	*6.5*	*5.3*	*4.9*	*4.6*
EV/EBITDA (post IFRS 16)			*4.3*	*5.5*	*4.6*	*4.4*	*4.2*
EV/EBITA (pre IFRS 16)	*10.7*	*9.2*	*9.1*	*17.0*	*11.4*	*10.3*	*9.2*
EV/EBITA (post IFRS 16)			*9.5*	*17.1*	*12.4*	*11.3*	*10.3*
PEG ratio	*0.5*	*0.8*	*-1.9*	*-0.4*	*0.2*	*0.9*	*1.5*
Dividend yield	*3.0%*	*3.5%*	*1.0%*	*5.4%*	*3.4%*	*3.7%*	*3.9%*
Dividend cover	*3.3*	*3.2*	*10.7*	*1.0*	*2.4*	*2.6*	*2.6*
Corporate tax rate	*-17.4%*	*-19.5%*	*-20.0%*	*-21.1%*	*-21.1%*	*-21.1%*	*-25.0%*
Net debt / EBITDA (pre IFRS 16)	*2.0*	*1.7*	*1.6*	*1.7*	*1.4*	*1.1*	*0.9*
Return on average capital employed	*14.8%*	*14.5%*	*14.5%*	*9.2%*	*12.0%*	*14.0%*	*14.0%*
Net cash/(debt) - pre IFRS16	**-179,172**	**-168,100**	**-159,806**	**-121,906**	**-123,000**	**-108,650**	**-96,162**
Fleet capital expenditure (gross)	64,900	63,800	49,100	40,200	50,000	55,000	60,000
Investment as % sales	*21.4%*	*16.7%*	*13.5%*	*13.1%*	*14.1%*	*14.6%*	*15.5%*
Reported sharecount Ks (net Treasury)	*39,476*	*39,603*	*39,618*	*39,595*	*39,793*	*39,992*	*40,192*
Shareprice (p)	**870**						

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

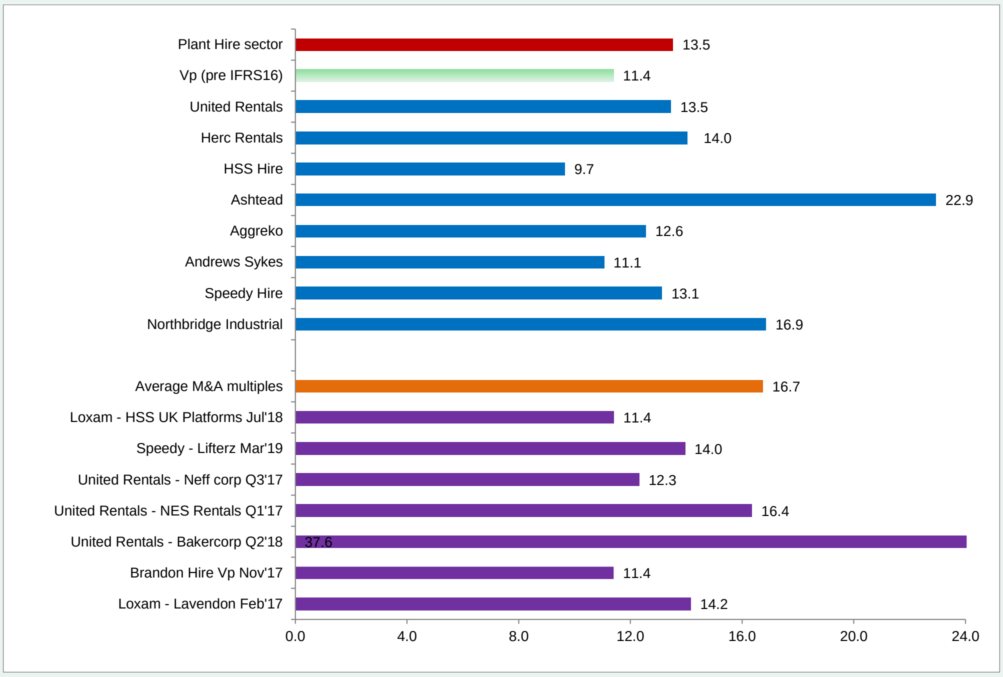
Appendices - sector valuation metrics and KPIs

Current Year (CY) EV / EBITDA vs peers



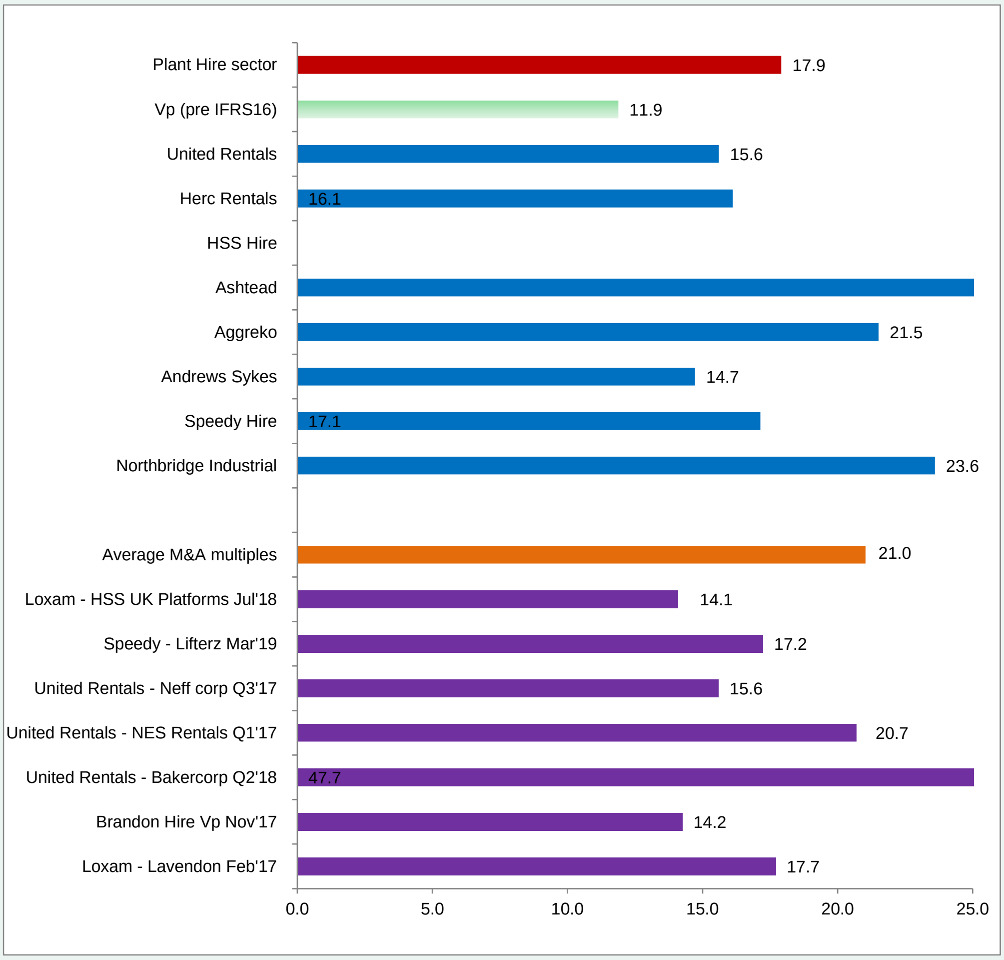
Source: Equity Development

Current Year (CY) EV / EBIT vs peers



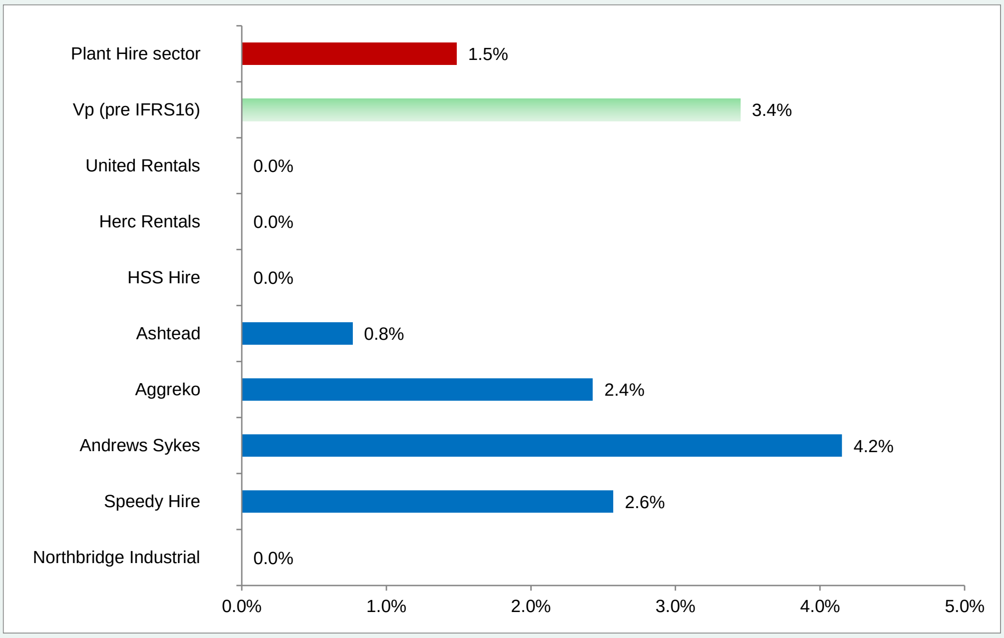
Source: Equity Development

CY PERs vs peers



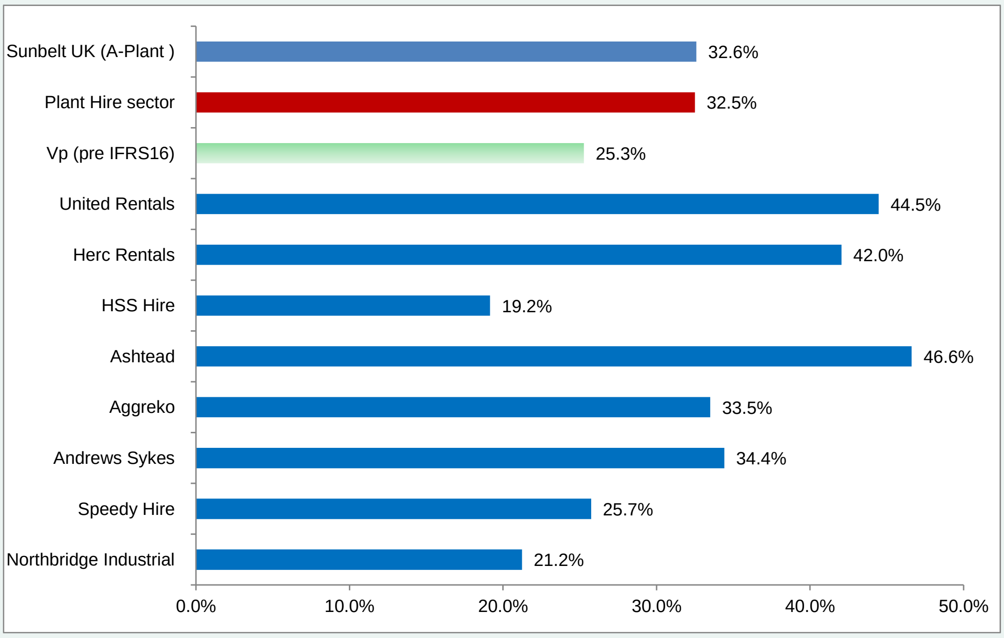
Source: Equity Development

CY dividend yield vs peers



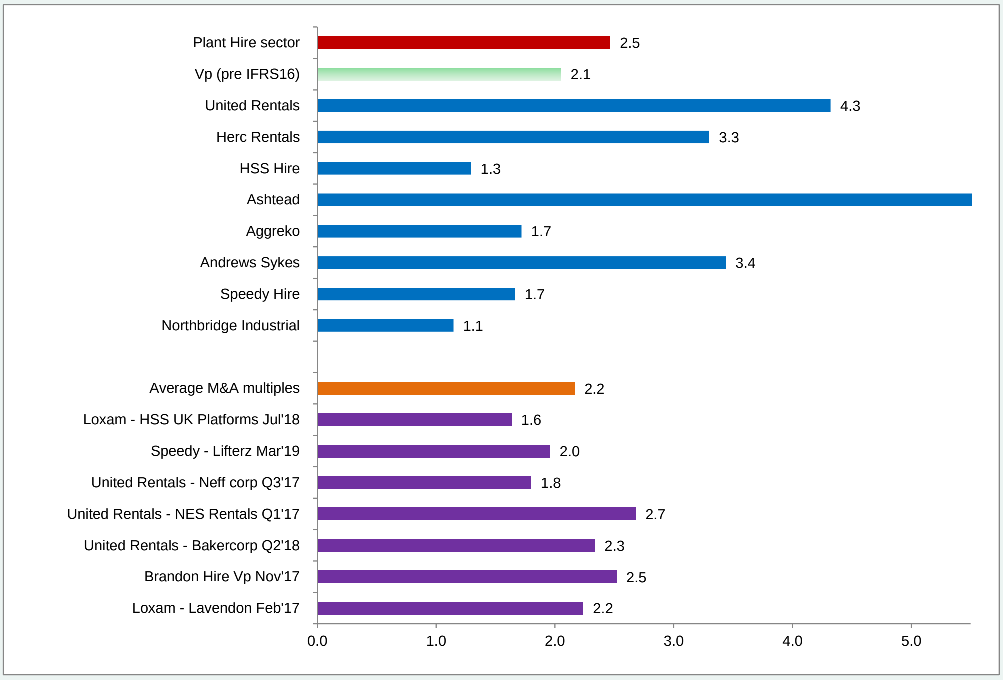
Source: Equity Development

CY % EBITDA margins vs peers



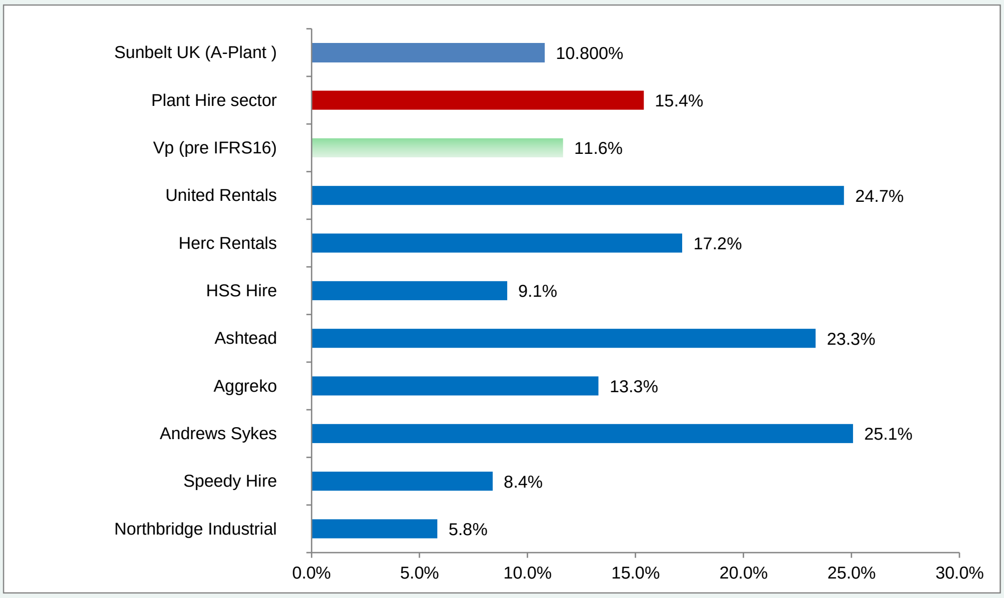
Source: Equity Development

CY Price: Book



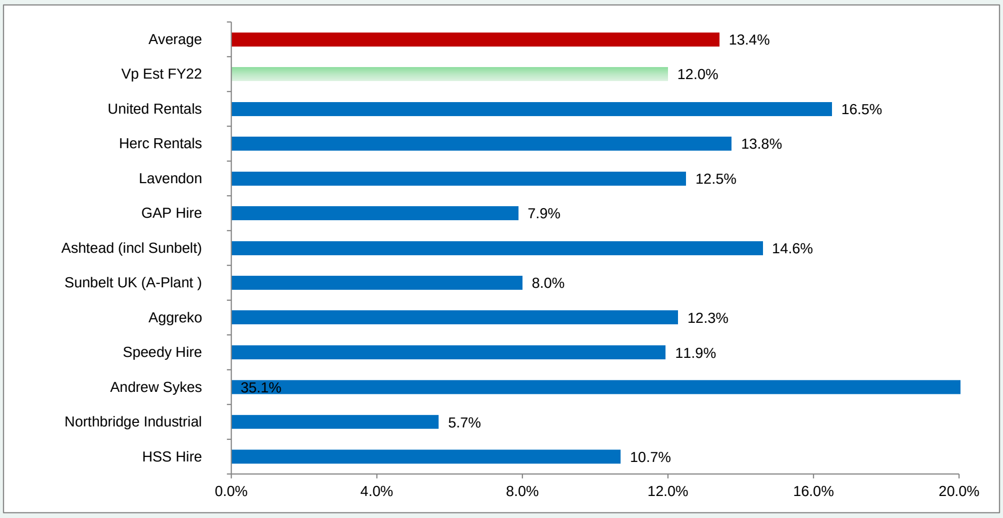
Source: Equity Development

CY % EBIT margins vs peers



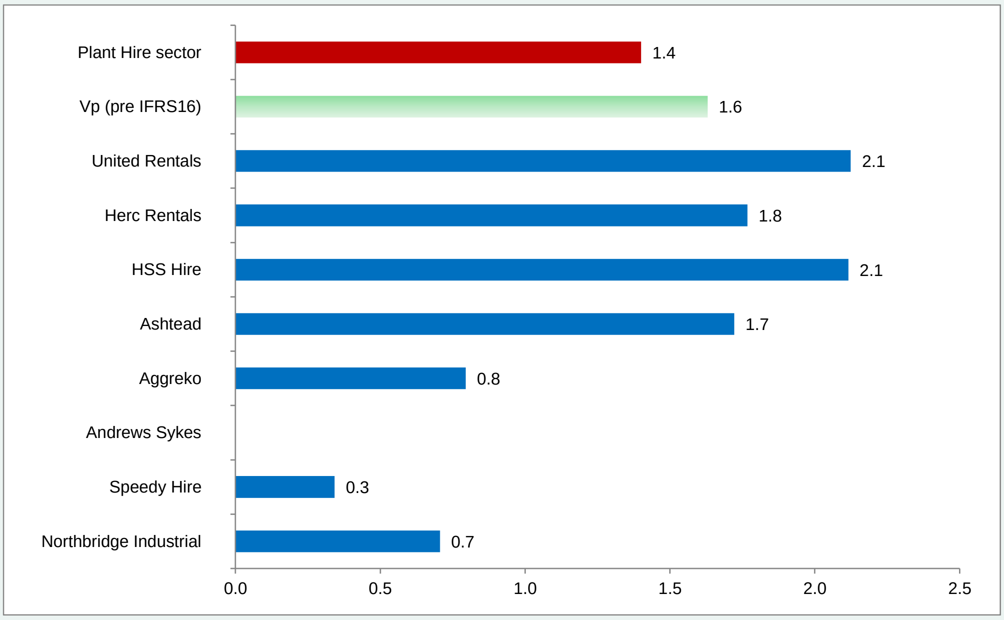
Source: Equity Development

CY % ROCE vs peers



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)
Northbridge Industrial	118.0p	£33.3	-£5.4	£38.8
Speedy Hire	72.0p	£383	-£33	£416
Andrews Sykes	530p	£224	£10	£214
Aggreko	865p	£2,206	-£419	£2,625
Ashtead	5,225p	£23,878	-£4,210	£28,088
HSS Hire	20.0p	£139.3	-£120.4	£259.7
Herc Rentals	$113.0	$3,300	-$1,472	$4,772
United Rentals	$316.0	$22,120	-$8,811	$30,931
Vp	870p	£349	-£123	£472

Source: Equity Development

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