

Treatt

FY19 trading update

Another good year despite citrus price deflation

Treatt has had another successful year: notwithstanding the decline in citrus prices, revenues were up 0.5%, or down 2% at constant currency. This demonstrates the transformation that has occurred at the company over the last few years, from a commodity trading house to a provider of value-added, technical flavour and fragrance solutions. While orange oil prices were down 50% and revenue from the citrus category was down 10%, Treatt's broadened portfolio was able to withstand the decline by registering significant growth elsewhere, notably in tea, health & wellness and fruit & vegetables. Management's outlook for FY20 is positive, despite citrus pricing continuing to have an adverse effect.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
09/17	101.3	12.8	18.5	4.8	21.8	1.2
09/18	112.2	13.8	20.3	5.1	19.9	1.3
09/19e	112.7	14.4	18.7	5.1	21.6	1.3
09/20e	115.0	15.3	19.9	5.9	20.4	1.5

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

Balanced portfolio is robust

Treatt's portfolio is well-suited for the current consumer trends of clean labels and more natural, better-for-you products, without compromising on taste. The fact that the organic (constant currency) revenue decrease was only 2%, despite pressure on citrus pricing due to raw materials weakness, demonstrates the strength of the portfolio. The citrus category represented 54% of group revenue and was down 10% in revenue terms, but this was offset by substantial growth in the remaining categories. The non-citrus categories continue to display significant growth potential, and the news in the latest trading statement is that cold brew coffee will be a new market opportunity for Treatt from FY20.

Expansion a key step for the future

FY19 witnessed the completion of the US expansion, which occurred on budget and on schedule. The capacity in non-citrus was doubled, and the size of the technical and innovation centre was quadrupled. The UK relocation continues, with construction beginning last month, and occupancy scheduled for fiscal Q420.

Valuation: Remains attractive

We value Treatt using a DCF model, which indicates a fair value of 530p (previously 517p). The increase is due to slightly higher profit forecasts and a reduction in our net debt forecasts. Treatt trades at 20.4x FY20e P/E and 14.1x FY20e EV/EBITDA. On both P/E and EV/EBITDA multiples it trades at a c 15% discount to its peer group.

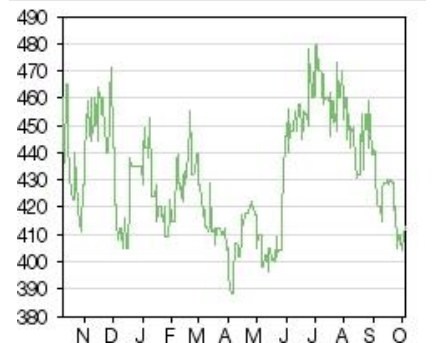
Food & beverages

7 October 2019

Price 404.00p
Market cap £238m

Net cash (£m) at 30 September 2019	15.8
Shares in issue	59.5m
Free float	100%
Code	TET
Primary exchange	LSE
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	(4.4)	(13.8)	(14.0)
Rel (local)	(2.6)	(9.1)	(10.8)
52-week high/low	480.00p	388.00p	

Business description

Treatt provides innovative ingredient solutions from its manufacturing bases in Europe, North America and Africa, principally for the flavours and fragrance industries and multinational consumer goods companies, with particular emphasis on the beverage sector.

Next events

FY19 results 26 November 2019

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Forecasts

We trim our FY19 sales forecasts slightly in light of the FY19 trading statement, and to reflect lower citrus prices. Our operating profit and PBT forecasts nudge up slightly as the favourable mix would have improved margins. Our net debt forecasts are also updated to reflect the fall in inventories and in receivables due to the depressed citrus prices.

Exhibit 1: Old vs new key P&L forecasts

	EPS* (p)			PBT* (£000s)			Revenue (£000s)		
	Old	New	% change	Old	New	% change	Old	New	% change
2019e	15.1	15.3	1.6%	13,064	13,250	1.4%	113,845	112,724	-1.0%
2020e	17.2	17.6	2.7%	13,614	13,979	2.7%	116,122	114,978	-1.0%
2021e	18.3	18.9	3.5%	14,477	14,990	3.5%	120,767	119,577	-1.0%

Source: Edison Investment Research. Note: *Stated on company normalised basis, which is pre-exceptional but after amortisation of acquired intangibles and share-based payments.

Exhibit 2: Old vs new net cash/(debt) forecasts

£000s	Old	New	% chg
2019e	(3,000)	15,904	N/A
2020e	(7,204)	10,812	N/A
2021e	4,274	23,513	450.2%

Source: Edison Investment Research

Valuation

We illustrate Treatt's relative valuation versus its ingredients peer group in Exhibit 3 below. Treatt trades at a discount to its peer group on both a P/E and EV/EBITDA basis. We believe some discount is justified to reflect its small size and because some of its products are relatively 'upstream' in the ingredients spectrum, particularly the bulk ingredients that are sold to other ingredients companies.

Exhibit 3: Comparative valuation

	Market cap (m)	P/E (x)		EV/EBITDA (x)		Dividend yield (%)	
		2019e	2020e	2019e	2020e	2019e	2020e
Givaudan	CHF 24,963	31.4	28.2	22.1	20.1	2.3	2.4
IFF	\$12,591	19.1	17.9	15.1	14.2	2.5	2.6
Symrise	CHF 11,422	34.7	29.7	17.7	15.7	1.2	1.3
Chr Hansen	DKK 76,107	40.1	36.2	26.6	24.3	2.0	1.9
Kerry	€ 18,611	27.1	24.7	19.5	17.9	0.7	0.8
Ingredion	\$5,218	11.8	11.0	7.4	7.1	3.1	3.2
Peer group average		27.3	24.6	18.1	16.5	2.0	2.0
Treatt	238.6	21.6	20.4	15.0	14.1	1.3	1.5
Premium/(discount) to peer group (%)		(20.9%)	(17.3%)	(17.0%)	(14.6%)	(35.8%)	(28.6%)

Source: Refinitiv, Edison Investment Research. Note: Prices as of 4 October 2019

Our DCF-derived fair value increases to 530p (from 517p previously), due to the slight increase in our profit forecasts and our lower net debt (now net cash) forecasts. Our longer-term sales growth forecast remains at 5.0% pa, falling to 2% growth in perpetuity. Our DCF is calculated based on a WACC of 6.8% (encompassing a beta of 0.8, an equity risk premium of 5.0% and a borrowing spread of 5.0%) and a terminal growth rate of 2%.

Exhibit 4: Financial summary

	£000s	2016	2017	2018	2019e	2020e	2021e	2022e
Year end September		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS								
Revenue	88,040	101,250	112,163	112,724	114,978	119,577	124,361	
Cost of Sales	(67,639)	(75,985)	(84,407)	(84,829)	(86,066)	(89,269)	(92,591)	
Gross Profit	20,401	25,265	27,756	27,895	28,913	30,308	31,769	
EBITDA	11,604	15,049	16,627	16,281	17,406	20,629	21,621	
Operating Profit (before amort., except. and share-based payments.)	10,257	13,650	10,257	13,650	15,108	14,616	15,490	
Intangible Amortisation	(142)	(137)	(124)	(105)	(90)	(76)	(65)	
Share based payments	(566)	(966)	(1,040)	(1,061)	(1,221)	(1,310)	(1,388)	
Other	0	0	0	0	0	0	0	
Operating Profit	9,549	12,547	13,944	13,450	14,179	14,902	15,746	
Net Interest	(703)	(851)	(1,302)	(200)	(200)	88	144	
Exceptionals	(553)	0	(1,105)	(825)	0	0	0	
Profit Before Tax (norm)	9,554	12,799	13,806	14,416	15,290	16,376	17,344	
Profit Before Tax (FRS 3)	8,293	11,696	11,537	12,425	13,979	14,990	15,891	
Profit Before Tax (company)	8,846	11,696	12,642	13,250	13,979	14,990	15,891	
Tax	(2,144)	(3,129)	(2,284)	(3,379)	(3,565)	(3,822)	(4,052)	
Profit After Tax (norm)	7,410	9,670	11,522	11,038	11,725	12,553	13,292	
Profit After Tax (FRS 3)	6,149	8,567	9,253	9,046	10,414	11,168	11,839	
Discontinued operations	0	978	2,976	(1,800)	0	0	0	
Average Number of Shares Outstanding (m)	51.9	52.2	56.8	59.1	59.1	59.1	59.1	
EPS - normalised (p)	14.3	18.5	20.3	18.7	19.9	21.3	22.5	
EPS - normalised & fully diluted (p)	14.1	17.9	19.8	18.5	19.6	21.0	22.2	
EPS - (IFRS) (p)	11.8	16.4	21.5	15.3	17.6	18.9	20.0	
Dividend per share (p)	4.4	4.8	5.1	5.1	5.9	6.3	6.7	
Gross Margin (%)	23.2	25.0	24.7	24.7	25.1	25.3	25.5	
EBITDA Margin (%)	13.2	14.9	14.8	14.4	15.1	17.3	17.4	
Operating Margin (before GW and except.) (%)	11.7	13.5	13.5	13.0	13.5	13.6	13.8	
BALANCE SHEET								
Fixed Assets	16,161	19,532	21,863	42,784	55,502	49,378	45,257	
Intangible Assets	3,364	3,331	752	647	557	481	416	
Tangible Assets	11,361	14,821	20,038	41,064	53,872	47,824	43,768	
Investments	1,436	1,380	1,073	1,073	1,073	1,073	1,073	
Current Assets	54,435	68,230	102,401	82,953	83,061	85,331	87,825	
Stocks	29,990	42,878	39,642	25,750	26,035	27,554	29,154	
Debtors	17,853	19,973	28,828	24,463	24,722	25,472	26,367	
Cash	6,588	4,748	32,304	32,304	32,304	32,304	32,304	
Other	4	631	1,627	436	0	0	0	
Current Liabilities	(16,388)	(27,003)	(35,781)	(27,063)	(30,206)	(21,775)	(14,490)	
Creditors	(15,834)	(19,266)	(16,479)	(16,130)	(15,878)	(15,915)	(15,930)	
Short term borrowings	(487)	(7,680)	(19,244)	(10,934)	(14,328)	(5,861)	1,439	
Provisions	(67)	(57)	(58)	0	0	0	0	
Long Term Liabilities	(17,021)	(14,281)	(6,858)	(10,124)	(11,621)	(7,187)	(3,337)	
Long term borrowings	(7,755)	(7,293)	(3,001)	(5,467)	(7,164)	(2,930)	720	
Other long term liabilities	(9,266)	(6,988)	(3,857)	(4,657)	(4,457)	(4,257)	(4,057)	
Net Assets	37,187	46,478	81,625	88,549	96,737	105,746	115,254	
CASH FLOW								
Operating Cash Flow	10,804	4,683	3,580	34,345	16,409	18,197	18,942	
Net Interest	(703)	(913)	(609)	(200)	(200)	88	144	
Tax	(2,022)	(2,822)	(2,978)	(3,379)	(3,565)	(3,822)	(4,052)	
Capex	(679)	(5,111)	(6,190)	(23,127)	(14,725)	1,706	(365)	
Acquisitions/disposals	(861)	(1,667)	8,357	1,100	0	0	0	
Financing	280	270	21,090	0	0	0	0	
Dividends	(2,095)	(3,025)	(2,876)	(2,895)	(3,012)	(3,468)	(3,719)	
Net Cash Flow	4,724	(8,585)	20,374	5,845	(5,092)	12,702	10,950	
Opening net debt/(cash)	6,155	1,654	10,225	(10,059)	(15,904)	(10,812)	(23,513)	
HP finance leases initiated	0	0	0	0	0	0	0	
Other	(223)	14	(90)	0	0	0	0	
Closing net debt/(cash)	1,654	10,225	(10,059)	(15,904)	(10,812)	(23,513)	(34,463)	

Source: Company accounts, Edison Investment Research

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