

# discoverIE Group

## Factoring in COVID-19 disruption

Trading update

discoverIE's year-end trading update confirms that coronavirus-related disruption in China is expected to modestly affect FY20 earnings. While trading elsewhere has been as expected, with good order wins, efforts to contain the virus in Europe and North America could reduce demand and introduce supply constraints over at least the next quarter. We have revised our forecasts to take a more cautious stance in H121 before factoring in a recovery starting in H221.

Year end	Revenue (£m)	PBT* (£m)	Diluted EPS* (p)	DPS (p)	P/E (x)	Yield (%)
03/18	387.9	22.6	23.0	9.0	19.3	2.0
03/19	438.9	28.4	28.4	9.6	15.6	2.2
03/20e	463.1	31.0	27.0	10.0	16.4	2.3
03/21e	463.6	28.8	23.8	10.4	18.6	2.3
03/22e	497.8	36.2	29.9	10.7	14.8	2.4

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

## China disruption in Q420

The measures taken to contain coronavirus in China in the first quarter of 2020 have had a negative impact on trading for discoverIE, through a combination of manufacturing closures (two facilities in Guangdong province), reduced Chinese customer demand, and reduced supply of components from China. Manufacturing is now returning to planned levels and the other issues within China are also normalising. While trading elsewhere has been in line with expectations and the company saw a good level of order intake in March, the disruption in China is expected to have a modest impact on FY20 earnings.

## Risk elsewhere prompts more cautious stance

While China appears to have successfully contained the virus, clearly it has spread to Europe, North America and other parts of Asia. Currently, discoverIE's manufacturing facilities are operating normally and the group is maintaining operational continuity in its diversified businesses. However, it is unclear what effect virus containment efforts will have on customer demand or discoverIE's ability to manufacture and supply product or sign up new business. We have reduced our FY21 forecasts to reflect weaker demand in H121 before the start of a recovery in H221. The company notes that it currently has a gearing ratio of 1.5x and has additional debt headroom of more than £100m.

## Valuation: Reflects more cautious outlook

The stock has declined 21% over the last month. FY21 P/E is essentially unchanged compared to when we last wrote in January, on 18.6x on our revised forecasts. While the stock currently trades at a premium to the peer group average, this comparison is complicated by the fast-moving nature of virus containment efforts and the fact that not all companies have reported on trading or updated guidance.

Electronic & electrical equipment

24 March 2020

**Price** 443p

**Market cap** £393m

€1.07: US\$1.15: £1

Net debt (£m) at end H120 55.4

Shares in issue 88.7m

Free float 96%

Code DSCV

Primary exchange LSE

Secondary exchange N/A

### Share price performance



% 1m 3m 12m

Abs (22.0) (20.3) 10.2

Rel (local) 18.2 23.6 59.3

52-week high/low 586p 378p

### Business description

discoverIE is a leading international designer and manufacturer of customised electronics to industry, supplying customer-specific electronic products and solutions to 25,000 industrial manufacturers.

### Next events

FY20 results June 2020

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## Changes to forecasts

We have revised down our H220 forecasts to reflect disruption in China. We have also revised down our FY21 forecasts, assuming that the current coronavirus crisis will affect demand for discoverIE's products, and potentially add supply constraints. We assume that this affects H121 trading before starting to recover in H220. We introduce FY22 forecasts, which show a resumption of growth in margins and profitability.

**Exhibit 1: Changes to forecasts**

£m	FY20e old	FY20e new	Change	y-o-y	FY21e old	FY21e new	Change	y-o-y	FY22e new	y-o-y
Revenues	475.4	463.1	(2.6%)	5.5%	498.5	463.6	(7.0%)	0.1%	497.8	7.4%
Custom supply	173.3	170.6	(1.5%)	(1.2%)	175.0	170.2	(2.8%)	(0.3%)	178.7	5.0%
Design & manufacturing	302.1	292.4	(3.2%)	9.8%	323.4	293.4	(9.3%)	0.3%	319.0	8.8%
Gross margin	33.3%	33.3%	0.0%	0.3%	33.3%	33.3%	0.0%	(0.0%)	33.3%	0.0%
EBITDA	50.4	47.7	(5.4%)	28.9%	54.4	45.6	(16.2%)	(4.3%)	53.0	16.2%
EBITDA margin	10.6%	10.3%	(0.3%)	1.9%	10.9%	9.8%	(1.1%)	(0.5%)	10.7%	0.8%
Underlying operating profit	37.2	34.5	(7.3%)	12.7%	41.4	32.6	(21.3%)	(5.4%)	40.0	22.6%
Underlying operating margin	7.8%	7.5%	(0.4%)	0.5%	8.3%	7.0%	(1.3%)	(0.4%)	8.0%	1.0%
Normalised operating profit	38.4	35.7	(7.1%)	12.3%	42.6	33.8	(20.7%)	(5.2%)	41.2	21.8%
Normalised operating margin	8.1%	7.7%	(0.4%)	0.5%	8.6%	7.3%	(1.3%)	(0.4%)	8.3%	1.0%
Normalised PBT	33.7	31.0	(8.1%)	9.1%	37.6	28.8	(23.4%)	(7.2%)	36.2	25.7%
Normalised net income	25.4	23.3	(8.1%)	8.7%	28.3	21.7	(23.5%)	(7.0%)	27.3	25.7%
Normalised diluted EPS (p)	29.4	27.0	(8.1%)	(5.1%)	31.1	23.8	(23.5%)	(11.9%)	29.9	25.7%
Reported basic EPS (p)	19.5	17.0	(12.6%)	(14.9%)	21.3	13.8	(35.2%)	(18.8%)	20.1	45.5%
Net (debt)/cash	(77.1)	(71.1)	(7.9%)	12.2%	(69.1)	(64.6)	(6.6%)	(9.1%)	(55.1)	(14.6%)
Net debt/EBITDA (x)	1.8	1.5			1.4	1.6			1.2	

Source: Edison Investment Research

**Exhibit 2: Financial summary**

	£m	2015	2016	2017	2018	2019	2020e	2021e	2022e
Year end 31 March		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
<b>PROFIT &amp; LOSS</b>									
Revenue		271.1	287.7	338.2	387.9	438.9	463.1	463.6	497.8
Cost of Sales		(186.7)	(195.1)	(227.2)	(261.2)	(293.9)	(308.7)	(309.2)	(332.0)
Gross Profit		84.4	92.6	111.0	126.7	145.0	154.3	154.4	165.8
EBITDA		16.6	19.8	24.3	29.3	37.0	47.7	45.6	53.0
Operating Profit (before am, SBP and except.)		14.0	17.0	20.6	25.2	31.8	35.7	33.8	41.2
Operating Profit (before am. and except.)		13.4	16.3	20.0	24.5	30.6	34.5	32.6	40.0
Amortisation of acquired intangibles		(2.1)	(2.8)	(3.9)	(4.9)	(5.9)	(7.6)	(8.0)	(8.0)
Exceptionals		(5.2)	(2.1)	(8.4)	(2.3)	(2.0)	(3.1)	(3.2)	(3.2)
Share-based payments		(0.6)	(0.7)	(0.6)	(0.7)	(1.2)	(1.2)	(1.2)	(1.2)
Operating Profit		6.1	11.4	7.7	17.3	22.7	23.8	21.4	28.8
Net Interest		(1.6)	(1.8)	(2.8)	(2.6)	(3.4)	(4.7)	(5.1)	(5.1)
Profit Before Tax (norm)		12.4	15.2	17.8	22.6	28.4	31.0	28.8	36.2
Profit Before Tax (FRS 3)		4.3	9.4	4.8	14.6	19.3	19.0	16.2	23.6
Tax		(1.4)	(2.2)	(1.3)	(4.0)	(4.7)	(4.7)	(4.0)	(5.8)
Profit After Tax (norm)		10.0	11.8	13.6	17.1	21.5	23.3	21.7	27.3
Profit After Tax (FRS 3)		2.9	7.2	3.5	10.6	14.6	14.3	12.3	17.8
Ave. Number of Shares Outstanding (m)		57.6	63.3	65.4	70.8	73.0	83.9	88.7	88.7
EPS - normalised & diluted (p)		16.4	17.8	19.9	23.0	28.4	27.0	23.8	29.9
EPS - IFRS basic (p)		5.0	11.4	5.3	15.0	20.0	17.0	13.8	20.1
EPS - IFRS diluted (p)		4.8	10.9	5.1	14.2	19.4	16.5	13.4	19.6
Dividend per share (p)		7.6	8.1	8.5	9.0	9.6	10.0	10.4	10.7
Gross Margin (%)		31.1	32.2	32.8	32.7	33.0	33.3	33.3	33.3
EBITDA Margin (%)		6.1	6.9	7.2	7.6	8.4	10.3	9.8	10.7
Operating Margin (before am, SBP and except.) (%)		5.2	5.9	6.1	6.5	7.2	7.7	7.3	8.3
<b>BALANCE SHEET</b>									
Fixed Assets		88.6	108.4	122.2	136.4	149.2	232.9	219.6	206.3
Intangible Assets		69.9	88.2	100.7	107.2	119.7	187.6	179.5	171.4
Tangible Assets		13.8	14.7	16.0	23.4	24.4	40.2	35.0	29.8
Deferred tax assets		4.9	5.5	5.5	5.8	5.1	5.1	5.1	5.1
Current Assets		127.3	128.3	147.1	165.9	179.1	177.6	179.3	196.0
Stocks		39.8	42.9	48.8	58.1	66.2	69.8	69.9	75.0
Debtors		60.2	65.5	77.3	84.6	88.7	96.4	96.5	103.6
Cash		26.7	19.9	21.0	21.9	22.9	10.1	11.6	16.1
Current Liabilities		(62.1)	(61.7)	(78.1)	(94.0)	(96.0)	(107.6)	(107.9)	(109.3)
Creditors		(61.9)	(60.9)	(77.1)	(87.6)	(94.3)	(99.2)	(99.5)	(106.4)
Lease liabilities		0.0	0.0	0.0	0.0	0.0	(6.7)	(6.7)	(1.2)
Short term borrowings		(0.2)	(0.8)	(1.0)	(6.4)	(1.7)	(1.7)	(1.7)	(1.7)
Long Term Liabilities		(61.1)	(73.1)	(68.7)	(81.5)	(97.6)	(100.2)	(85.4)	(76.1)
Long term borrowings		(45.5)	(57.2)	(50.0)	(67.9)	(84.5)	(79.5)	(74.5)	(69.5)
Lease liabilities		0.0	0.0	0.0	0.0	0.0	(7.9)	(1.2)	0.0
Other long term liabilities		(15.6)	(15.9)	(18.7)	(13.6)	(13.1)	(12.8)	(9.7)	(6.6)
Net Assets		92.7	101.9	122.5	126.8	134.7	202.8	205.7	216.9
<b>CASH FLOW</b>									
Operating Cash Flow		6.6	14.6	20.5	21.7	30.0	39.4	43.8	45.8
Net Interest		(1.6)	(1.8)	(2.8)	(2.6)	(3.4)	(4.7)	(5.1)	(5.1)
Tax		(3.3)	(4.3)	(3.0)	(3.7)	(3.8)	(6.7)	(7.1)	(8.9)
Capex		(2.5)	(2.3)	(3.4)	(4.3)	(5.4)	(6.4)	(6.5)	(6.5)
Acquisitions/disposals		(37.3)	(19.8)	(11.8)	(25.4)	(22.4)	(74.7)	(3.0)	0.0
Financing		52.7	0.0	13.6	(1.5)	0.1	53.9	(6.7)	(6.7)
Dividends		(3.6)	(4.9)	(5.2)	(6.2)	(6.7)	(8.6)	(9.0)	(9.2)
Net Cash Flow		11.0	(18.5)	7.9	(22.0)	(11.6)	(7.8)	6.5	9.4
Opening net cash/(debt)		1.8	(19.0)	(38.1)	(30.0)	(52.4)	(63.3)	(71.1)	(64.6)
HP finance leases initiated		0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other		(31.8)	(0.6)	0.2	(0.4)	0.7	0.0	0.0	0.0
Closing net cash/(debt)		(19.0)	(38.1)	(30.0)	(52.4)	(63.3)	(71.1)	(64.6)	(55.1)

Source: discoverIE Group, Edison Investment Research

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