EDISON

Eddie Stobart Logistics

H118 results

Strong revenue growth boosted by contract wins

General industrials

Eddie Stobart Logistics (ESL) published its H1 results on 30 August, reporting 25% revenue growth, including 10% organic. Organic growth was boosted by a higher than average level of contract wins and a good performance from the e-commerce division. A flip side of the contract wins was that they incurred network reoptimisation costs and this was the main reason that the EBIT margin declined from 5.9% to 5.0%. Management maintained full-year guidance.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
11/16	570.2	24.0	7.9	N/A	16.0	N/A
11/17	623.9	37.8	9.8	5.8	12.9	4.6
11/18e	780.2	51.3	12.1	6.1	10.4	4.8
11/19e	910.1	61.5	13.4	6.7	9.4	5.3

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

Revenue boosted by contract wins

ESL achieved 25% revenue growth, including 10% organic, in H1. Management believes that the 10% organic growth is above the UK logistics market. We thought the main point of interest from the H1 results was ESL's high level of contract wins. The company won £158m of annualised contracts in H1 compared to £89m across the whole of last year. In particular, ESL won larger sized contracts, including winning back the Britvic contract. It was also encouraging to see the strong performance of the e-commerce division reflecting both changes in the UK retail market and ESL's initiatives to build-up its capabilities in this area. Total revenue growth was 25%, boosted by the iForce and Speedy Freight acquisitions, both of which performed well.

EBIT margin held back by contract wins

While revenue rose by 25%, EBIT increased by only 7%, with the EBIT margin declining from 5.9% to 5.0% largely due to the network reoptimisation costs associated with the new contracts, especially as they were large contracts. These costs are temporary, though, hence management's confidence in reiterating guidance. We think the good outlook is underscored by the 10% dividend increase.

Valuation: DCF offers 51% upside

We use a DCF model to value ESL. Our DCF valuation of 190p/share provides 51% potential upside to the current share price of 126p. We use a WACC of 6.9% and a terminal growth rate of 1%. The next scheduled event will be the full year pre-close statement in November, which could be a positive catalyst if the current growth rate continues and the margin recovers.

5 September 2018

Price	**126p**
Market cap	**£478m**

Net debt (£m) at end November 2017	109.5
Shares in issue	379.3m
Free float	72.5%
Code	ESL
Primary exchange	AIM
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(7.0)	(10.6)	(21.3)
Rel (local)	(4.9)	(7.5)	(22.3)
52-week high/low		160p	123p

Business description

Eddie Stobart Logistics is a market leader in end-to-end, multi-modal transport and logistics. Operations are primarily focused in the UK with some activities in mainland Europe. Key customer segments include retail, consumer, industrials and increasingly, e-commerce.

Next events

FY pre-close	November 2018

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Eddie Stobart Logistics is a research client of Edison Investment Research Limited

H118 results show strong organic revenue growth

Exhibit 1: Results summary

(£m)	H117	H118	% change
Revenue	286.8	359.3	25.3%
EBITDA	19.9	22.4	12.6%
EBITDA margin (%)	6.9%	6.2%	
EBIT	16.9	18.1	7.1%
EBIT margin (%)	5.9%	5.0%	
Adjusted PAT	10.5	14.1	34.3%
Adjusted EPS (p)	3.6	3.9	8.3%
DPS (p)	1.40	1.54	10.0%
Adjusted free cash	16.9	0.3	(98.2%)
Net debt	97.7	114.2	16.9%

Source: ESL

Revenue

Revenue showed strong growth of 25%, of which 10% was organic. Management pointed out at the results meeting that organic revenue growth of 10% was substantially ahead of the UK logistics market. The rest of the growth in revenue was largely due to the iForce (+20% like-for-like growth) and Speedy Freight (+52%) acquisitions, which will act as a tailwind for group organic growth into H2 as the acquisitions annualise. The £53m acquisition, after the period-end, of The Pallet Network will be earnings accretive this year, according to management.

We thought the main highlight from the results was the level of new contract wins. ESL won £158m (annualised) value of contracts in H1 compared to £89m in the whole of FY17. At the results presentation, management highlighted how growth had been weighted towards large contracts including Britvic (c £30m), Homebase (c £20m), CEMEX UK (c £10m) and Knauf (c £9m). Management pointed out that normally large contracts are in the range of £5-10m. A new contract with PepsiCo (c £30m) was won after period-end. We think the contracts won so far this year should provide a useful backdrop for continued revenue growth.

Management added that the Homebase contract, which was won before the recent change of ownership, is being closely managed, with cash controls. However, we note the positive news that on 31 August, the day after ESL's results, Homebase reached agreement with its creditors to pass its Company Voluntary Agreement (CVA) plan.

Also interesting, in our view, was the strong growth of the e-commerce division, with revenue more than doubling in the period (Exhibit 2). The division won c £18m (annualised) of new contracts including MedicAnimal, Made.com, Steamer Trading and The Works. Growth in the e-commerce market has been supported by traditional retailers looking to further develop their e-commerce offering and also new e-commerce entrants. ESL has continued to augment its e-commerce capability through the iForce acquisition, proprietary software and a multi-user offering (ie Corby Euro Hub).

Consumer was the only sector that declined, due to the loss of the Britvic contract which has now been re-secured.

Exhibit 2: Sector revenue

Sector	H117 (£m)	H118 (£m)	Growth (%)	Proportion of H118 revenue (%)
Retail	80.0	102.0	27.5%	28%
Manufacturing, Industrial and Bulk	80.9	91.6	13.2%	25%
e-Commerce	36.9	80.3	117.6%	22%
Consumer	74.7	70.1	(6.2%)	20%
Non-sector specific	14.3	15.3	7.0%	4%
Total	**286.8**	**359.3**	**25.3%**	**100%**

Source: ESL

EBIT

A strong revenue performance was in part offset by a reduction in the margin from 5.9% to 5.0%. This was mainly caused by network reoptimisation of the business to handle the high level of new contract wins, eg the need for extra agency staff and adding warehouse capacity, which takes time to fill.

These extra costs are temporary and this was reflected in management's outlook statement, which stated: "As with previous years, we now move into the traditionally stronger second half with costs of new contract wins absorbed in the first half. The second half has started well and the Board remain confident of delivering full year in line with expectations."

Cash flow

Free cash declined from £16.9m to £0.3m, which was also mainly due to the 'cost' of higher revenue (Exhibit 3).

Exhibit 3: Cash flow (£m)

	H117	H118
Underlying EBITDA	19.9	22.4
Net capex	(4.1)	(7.2)
Working capital	6.1	(11.1)
Tax	0.6	(2.2)
Other items	(5.6)	(1.6)
Total	**16.9**	**0.3**

Source: ESL

Capex increased from £4.1m to £7.2m due to the cost of fitting-out of new warehouse assets (expected to be at full capacity by year end) and technology spend on scheduling systems. Management said that capex was front-end loaded for H1 so will be lower in H2. Working capital swung from an inflow of £6.1m to an outflow of £11.1m (Exhibit 4). The net investment was due mainly to significant contract wins and increased levels of revenue.

Exhibit 4: Working capital movement (£m)

	H117	H118
34% increase in sales Q218 vs Q217	-	(6.8)
Britvic contract run off in 2017 and build up in 2018	5.4	(0.7)
Management shares	3.4	-
Other items	(2.7)	(3.6)
Total	**6.1**	**(11.1)**

Source: ESL

Net debt

Net debt rose from £97.7m in H117 to £114.2m, but at 2.0x EBITDA is still at management's target level. The increase was due mainly to three factors:

- Acquisition of 50% stakes in both The Logistics People and Speedy Freight.

- A decision to use finance leasing rather than operating leasing for some specialist equipment due to the lower cost
- The increase in working capital

Valuation and estimates

Our DCF value offers 51% upside to the current share price

We use a DCF model to value ESL. We think a DCF is especially suitable for cash-generative companies like ESL. Our DCF value for ESL is 190p/share, which provides 51% potential upside to the current share price of 126p (Exhibit 5). We use a WACC of 6.9% and a terminal growth rate of 1%. Previously, we used a combined DCF/EVA methodology with a 203p/share valuation (see September 2017 update for more details).

Exhibit 5: DCF valuation for ESL

(£m unless stated)	
Total discounted cash flows (FY19 to FY29)	431
Discounted terminal value	377
Total EV	**807**
Net debt (FY18)	(86)
Equity value	**721**
Number of shares (m)	379
Value per share (p)	**190**

Source: Edison Investment Research

We have made minor adjustments to our forecasts, with FY18e PBT reducing from £51.7m to £51.3m, while EBITDA increases from £65.3m to £67.9m. Our FY19e EBITDA and PBT estimates are up slightly from £75m and £60m to £77m and £62m respectively.

Exhibit 6: Financial summary

£m	2016	2017	2018e	2019e	2020e
November year end	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS					
Revenue	570	624	780	910	973
EBITDA	47.4	55.3	67.9	77.2	84.6
Operating Profit (before amort. and except.)	41.3	48.5	59.4	67.3	74.0
Intangible Amortisation	(9.5)	(11.1)	(11.1)	(11.1)	(11.1)
Exceptionals	(3.3)	(17.2)	(0.4)	0.0	0.0
Other	(1.2)	(0.6)	(0.6)	(0.6)	(0.6)
Operating Profit	27.2	19.6	47.2	55.5	62.2
Net Interest	(16.0)	(9.6)	(7.0)	(5.1)	(3.7)
Profit Before Tax (norm)	24.0	37.8	51.3	61.5	69.6
Profit Before Tax (FRS 3)	11.2	9.9	38.4	50.4	58.5
Tax	(1.3)	(5.0)	(7.7)	(10.5)	(13.2)
Profit After Tax (norm)	22.7	32.8	43.6	51.0	56.4
Profit After Tax (FRS 3)	9.9	4.9	30.7	39.9	45.3
Average Number of Shares Outstanding (m)	276.7	326.8	357.9	379.3	379.3
EPS - normalised (p)	7.9	9.8	12.2	13.5	14.9
EPS - normalised and fully diluted (p)	7.9	9.8	12.1	13.4	14.8
EPS - (IFRS) (p)	3.3	1.2	8.6	10.5	11.9
Dividend per share (p)	0.0	5.8	6.1	6.7	7.4
EBITDA Margin (%)	8.3	8.9	8.7	8.5	8.7
Operating Margin (before GW and except.) (%)	7.2	7.8	7.6	7.4	7.6
BALANCE SHEET					
Fixed Assets	259	339	330	322	314
Intangible Assets	219	272	260	249	238
Tangible Assets	38	60	63	66	69
Investments	2	7	7	7	7
Current Assets	150	163	201	233	248
Stocks	2	2	3	3	4
Debtors	134	149	186	217	232
Cash	14	12	12	12	12
Other	0	0	0	0	0
Current Liabilities	(119)	(142)	(174)	(201)	(214)
Creditors	(112)	(134)	(167)	(193)	(206)
Short term borrowings	(6)	(8)	(8)	(8)	(8)
Long Term Liabilities	(201)	(147)	(129)	(122)	(113)
Long term borrowings	(173)	(114)	(91)	(80)	(69)
Other long term liabilities	(28)	(34)	(39)	(42)	(44)
Net Assets	89	212	228	231	235
CASH FLOW					
Operating Cash Flow	30	30	50	59	65
Net Interest	(10)	(8)	(6)	(4)	(3)
Tax	(2)	(3)	(8)	(10)	(13)
Capex	(1)	(6)	(6)	(7)	(8)
Acquisitions/disposals	(2)	(48)	(16)	(4)	(4)
Financing	(5)	38	28	0	0
Dividends	0	(5)	(19)	(22)	(26)
Net Cash Flow	10.0	(2.4)	23.0	10.7	11.0
Opening net debt/(cash)	170	166	109	86	76
HP finance leases initiated	0	0	0	0	0
Other	(6)	58	0	0	0
Closing net debt/(cash)	166	109	86	76	65

Source: Eddie Stobart Logistics (historics), Edison Investment Research (forecasts)

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