EDISON

Epwin Group

Good end to FY20 and start to FY21

FY20 results and AGM update

Construction & materials

Epwin has entered FY21 with positive revenue momentum, having successfully navigated some extreme market conditions in the prior year. The company has built a solid base from which to grow volumes, and a positive cash generation profile provides headroom to invest organically and via acquisition as post-pandemic markets begin to normalise.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/19	282.1	15.0	8.5	1.8	12.9	1.6
12/20	241.0	5.0	4.0	1.0	27.4	0.9
12/21e	301.7	10.0	5.6	2.5	19.3	2.3
12/22e	306.8	13.3	7.5	3.4	14.4	3.1

Note: *PBT and EPS (fully diluted) are normalised, excluding intangible amortisation and exceptionals, on an IFRS 16 basis from FY19. Dividends: FY19 represents an H1 payment only; FY20 represents our expected final DPS.

Estimates beaten due to end FY20 momentum

Epwin's FY20 results came in c £0.9m ahead of our expected £4.1m PBT (and c £0.6m better on a company-defined basis, excluding share-based payments), with EBIT and net interest both slightly better than anticipated. Overall group revenue and EBIT were down y-o-y by c 15% and c 56% respectively, with a reported group EBIT margin for the year of 3.9% (down 360bp). All of the year-on-year dent occurred in H1 trading, which was most directly affected by initial lockdown conditions at the end of Q1/start of Q2, and H2 revenues rose c 5% y-o-y. Within the divisions, the Extrusion & Moulding (E&M) EBIT margin was slightly lower than we had anticipated, which was more than compensated for by stronger Fabrication & Distribution. Year-end net debt (pre IFRS 16) was in line at c £19m – and up only £2.1m for the year – with all covenants met and no additional in-year funding required. As expected, Epwin declared a 1.0p final dividend.

Good start to FY21, with some caution present

Outlook comments noted that FY21 has started well (being ahead of both FY19 and FY20 in Q1), although PVC polymer price increases and supply tightness have provided an industry challenge in the first part of the year. At this stage the industry is sounding a note of caution regarding supply chain concerns during FY21, but medium/long-term industry drivers appear to be intact, as do previous management's comments regarding the company's prospects. Our EPS estimates (now including the January acquisition of SBS Cumbria) have increased by c 10% for FY21 and c 6% for FY22 (with FY23 introduced for the first time).

Valuation: Outperforming the FTSE All-Share Index

A c 20% rise in Epwin's share price ytd is more than double that of the FTSE All-Share Index. We have modelled earnings exceeding FY19 levels in FY23, by which time the company's P/E and EV/EBITDA (pre IFRS 16) reduces to 12.3x and 5.4x respectively. While sector share prices have travelled well, a general cautionary tone from the quoted arena probably means that underlying consensus earnings increases have been muted so far. Greater clarity on the UK macroeconomic recovery path going into H2 could be the next share price catalyst.

15 June 2021

Price	**109.0p**
Market cap	**£158m**

Covenant net debt (£m) at end December 2020	18.5
Shares in issue	142.9m
Free float	67%
Code	EPWN
Primary exchange	AIM
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	1.4	24.0	47.2
Rel (local)	(0.2)	17.2	22.1
52-week high/low		110.0pp	64.1p

Business description

Epwin Group supplies functional low-maintenance exterior building products (including windows, doors, roofline and rainwater goods) into a number of UK market segments and is a modest exporter. It has a vertically integrated model in windows and doors and a leading market position in roofline products.

Next events

H121 period end	June

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Edison profile page

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FY20 results overview

The trading recovery from a pandemic-affected H1 result gathered momentum as FY20 progressed and Epwin delivered PBT for the year ahead of our expectations, primarily driven by the Fabrication & Distribution divisional performance. Core net debt rose only slightly over the year and cash flows were successfully managed within existing, pre-pandemic banking facilities. FY21 has started well and our increased estimates now include the post year-end acquisition of SBS Cumbria for the first time.

Exhibit 1: Epwin Group divisional and interim splits

£m	H119	H219	2019	H120	H220	2020	% change year-on-year		
							H1	H2	FY
Group Revenue	**140.0**	**142.1**	**282.1**	**93.3**	**147.7**	**241.0**	**-33.4%**	**3.9%**	**-14.6%**
Extrusion & Moulding	87.8	89.8	177.6	60.7	93.6	154.3	-30.9%	4.2%	-13.1%
Fabrication & Distribution	52.2	52.3	104.5	32.6	54.1	86.7	-37.5%	3.4%	-17.0%
Group EBIT Profit - reported	**9.4**	**11.8**	**21.2**	**-1.8**	**11.2**	**9.4**	**-119.1%**	**-5.1%**	**-55.7%**
Extrusion & Moulding	8.6	10.1	18.7	-0.3	8.6	8.3	-103.5%	-14.9%	-55.6%
Fabrication & Distribution	1.8	2.8	4.6	-0.4	3.6	3.2	-122.2%	28.6%	-30.4%
Group costs	-1.0	-1.1	-2.1	-1.1	-1.0	-2.1	10.0%	-9.1%	0.0%
Group EBIT margins %	**6.7%**	**8.3%**	**7.5%**	**-1.9%**	**7.6%**	**3.9%**			
Extrusion & Moulding	9.8%	11.2%	10.5%	-0.5%	9.2%	5.4%			
Fabrication & Distribution	3.4%	5.4%	4.4%	-1.2%	6.7%	3.7%			

Source: Company, Edison Investment Research

Epwin primarily serves the residential RMI market via trade channels with c 70% of revenues generated in this way. The remaining 30% is spread across the newbuild housing, social housing and commercial subsectors, with newbuild being the largest component.

2020 – an unprecedented trading year: the first UK lockdown (which came into effect towards the end of March) was initially disruptive to just about all construction sectors. Having maintained trade market presence for essential repairs, online suppliers were well positioned to facilitate significant increases in residential home improvement demand that ensued, with DIY retailers also relatively quick to restart thereafter, and sector sales recovered strongly over the remainder of the year. Building sites – both commercial and residential newbuild – reopened more gradually and primarily focused on finishing part-completed projects rather than commencing new ones. Consequently, the trade sector response was less rapid and immediate and the builders' merchants' recovery lagged that described for the residential sector. (Reported revenue trends from Kingfisher and Travis Perkins, parent companies of B&Q/Screwfix and Wickes[1]/Tradestation/TP general merchanting respectively illustrate the above sector trends well.) It should be noted that the lockdown hard stop followed by some monthly double-digit like-for-like sales increases in H220 (against undisrupted 2019 trading) in the same 12-month period placed unprecedented strains on suppliers and supply chains and, understandably, the challenges and responses were not uniform. In overall terms, we believe that Epwin's Extrusion & Moulding division – which includes Stormking – probably has a slightly higher newbuild exposure than does Fabrication & Distribution.

Extrusion & Moulding (E&M): *Primarily PVC-based window profile systems, roofline and rainwater goods extrusion activities with wood composite decking products and glass reinforced plastic building products also in the portfolio. Aluminium lines (Stellar, window systems and Adek, decking) have been developed internally and launched in the last two years.*

FY20 revenues dropped by c 13% y-o-y; this all occurred in H1 with H2 c 4% above H219 on the same basis. Profitability also rebounded strongly in the second half in generally firm business conditions and in the absence of any further enforced lockdown guidelines. That said, we did

[1] Travis Perkins owned Wickes for the duration of the 2020 trading year prior to its IPO in April 2021.

observe a partial lag in this EBIT pattern compared to both H2 revenue and H219. Taking group-level reporting as a proxy, we believe that the divisional gross margin recovered – most probably tempered by input prices starting to rise in Q4 – but opex also rebounded reflecting temporary business inefficiencies as demand spiked up, restricting the drop through to E&M profitability in H2.

Reflecting their main end-market exposures, E&M's product line performance varied with roofline, rainwater goods and mouldings having the strongest H2 sales performance, with Window Systems also developing positively, while newbuild-oriented Stormking recovered more slowly. Although the company's decking lines were not specifically referenced, we would have expected residential RMI sales here to have been positive also. In the most active channels/subsectors, Epwin's existing scale and sector presence, product availability and distribution, and up-to-date ranges (eg Optima 22/Stellar window systems and Dekboard/Adek decking products) will all have contributed to market outperformance in the period. Having relocated and consolidated window systems' foiling and finishing activities at a new Telford site towards the end of FY19, an adjacent newbuild warehouse facility was completed during FY20. (The aim is to have all window systems' storage and distribution operations, for both PVC and aluminium systems, on the same site by the end of FY21.) H220 focused on successfully meeting the pick-up in demand experienced and operating efficiencies are expected to improve following a bedding-in period. With a noted rebound in housing starts in Q4, all of the E&M division's main product lines ended FY20 with good trading momentum.

Fabrication & Distribution (F&D): *Downstream manufacture of finished windows and doors (using profiles from E&M) and multi-channel (including own branches) B2B distribution of these and other group finished products. Supply and installation of low-maintenance decking and ancillary products.*

Unsurprisingly, the UK's comprehensive first lockdown had a similar effect on trading in the F&D division at the end of Q1/into Q2 resulting in a c 37% y-o-y sales dip, which recovered to +c 3% in H2 and to a 17% reduction for the year as a whole. While a small trading loss was recorded in H1, a sharp margin recovery (to 6.7%) in H2 following significant volume increases led to a full year profit overall (and an EBIT margin of 3.7%, down just 70bp y-o-y.

The F&D division fabricates and sells windows made from profiles produced by the group and is also a vendor of other E&M product lines (as well as complementary third-party lines) across its branch network, so their trading performances are linked to some extent. We believe that it has slightly greater exposure to the RMI subsector than its sister E&M division. In a rapidly improving market in H2 with tightening supply lines generally, this business linkage should have proved beneficial with greater confidence in product availability compared to independents which, in turn, may have led to market share gains in the second half. Revenues generated from finished window and door fabrications sold to the trade sector grew well in H2, offset by a similar decline in sales to social housing operators. Second-half growth then at the divisional level was driven by a y-o-y uplift in distributed building products, through the F&Ds own branch network and through independent distributor customers in other areas.

SBS Cumbria (an eight-branch distributor in north-west England/south-west Scotland) was acquired in January for £3.8m, which is around two-thirds of revenue. Most obviously, this deal has a good geographic fit with the 15 branches located in north-east England/central Scotland acquired with Amicus Building Products in March 2019 and the total owned branch network is now approaching 100 locations. Otherwise, FY20 results commentary indicated that Q121 F&D revenues were ahead of the first quarters of both FY20 (modestly affected by the pandemic in March) and FY19, although this was not quantified.

Net cash neutral in FY20, despite dent to profitability

Despite the COVID-19-related dip in earnings, net debt (pre-IFRS 16 leases) only increased by £2.1m over FY20 to end the year at £18.5m.

Operating cash flow at c £24m was down c £11m y-o-y, slightly more than the EBITDA reduction over the year, and there was a small increase in non-underlying cash costs relating to restructuring and provision movements. Headline working capital movements (outflows of c £2m in both FY19 and FY20) do not really tell the full story. In a normal year, we would expect to see working capital investment in H1 substantially or completely unwinding in H2. Due to the disrupted trading pattern, the opposite happened in FY20, with a c £4m inflow in H1 (driven mainly by receivables but also lower inventory) exceeded by a c £6m H2 outflow as trading activity levels increased sharply. We note also that while the year-end inventory value was broadly unchanged at c £30m, raw materials/wip accounted for a slightly bigger proportion at the end of FY20 (ie 26% versus 20% a year earlier); this is likely to reflect the twin effects of a busy trading period running down finished goods levels and higher polymer input costs pulling forward buying to some extent.

Cash interest costs (£1.4m) were slightly below the prior year, consistent with average debt levels we believe, and cash tax payments (£0.8m) were also understandably lower y-o-y. Core capex spend was constrained – more so in H1 when trading disruption was greatest – but including c £5m for completing the new Telford II warehouse facility, total capex for the year of £8m was just over 0.8x owned asset depreciation in FY20. Taken together, **FY20 free cash flow was £13.5m** which, in the absence of any cash dividend payments for the year, was applied to and matched by lease principal repayments, leaving a **broadly neutral net cash flow performance for the year** overall.

For the record, IFRS 16 leases increased from £71m to £81m, substantially driven by the completion of the Telford II warehouse facility and the associated sale and leaseback arrangement.

Cash flow outlook: on our revised estimates (see below), we anticipate a significant pick-up in EBIT and free cash flow in FY21 after core capex at 0.9x owned asset depreciation. The acquisition of SBS, a return to the dividend list and ongoing lease principal repayment absorb much of this, but the receipt of £5.2m final proceeds for the Telford II development in Q121 results in c £5m net cash generation overall for FY21 in our model. In the absence of further acquisitions, a growing free cash profile thereafter sees bank debt reduce more rapidly subsequently – after allowing for dividend growth – to leave Epwin in a net cash position by the end of FY23 on our estimates. Having extended existing bank facilities (ie £65m RCF and £10m overdraft arrangements) to June 2024, Epwin has considerable headroom to pursue organic and acquisitive investment opportunities.

Good start to FY21, SBS boosts earnings expectations

Good market momentum appears to have continued into the early months of 2021, with revenue in both divisions ahead of Q1 levels seen in both FY19 and FY20, as referenced earlier. A spike in polymer input prices was seen during this period; to the extent that this is an industry-wide position and demand conditions are firm, we would expect higher raw materials prices to be recovered by higher product prices, albeit with a lag usually. We have factored this into our group revenue expectations as well as a contribution from SBS (acquired in January) for the first time, adding c £0.5m to PBT. Excluding SBS, the underlying EBIT upgrade is modest at this stage and the inflationary cost pressures optically dilute EBIT margins.

Exhibit 2: Epwin Group revised estimates

	EPS, fully diluted, normalised* (p)			PBT, normalised* (£m)			EBITDA** (£m)		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
FY20	2.3	4.0	+73.9%	4.1	5.0	+22.0%	15.3	16.9	+10.5%
FY21e	5.1	5.6	+9.8%	9.0	10.0	+11.1%	20.6	22.6	+11.0%
FY22e	7.2	7.6	+5.6%	12.7	13.3	+4.7%	24.3	26.0	+7.0%
FY23e	N/A	8.9	N/A	N/A	15.7	N/A	N/A	28.5	N/A

Source: Edison Investment Research. *IFRS 16. **Pre IFRS 16. FY20 Old = expected, New = actual; EPS benefitted from a tax credit.

Our dividend expectations (not shown in Exhibit 2) are unchanged with growth largely mirroring that of EPS, with cover ratios between 2-2.2x over our estimate horizon.

Exhibit 3: Financial summary

£m	2015	2016	2017	2017	2018	2019	2020	2021e	2022e	2023e
Year end 31 December	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS*	IFRS*	IFRS*	IFRS*	IFRS*
PROFIT & LOSS				**Restated**						
Revenue	256.0	293.2	298.3	292.8	281.1	282.1	241.0	301.7	306.8	316.0
Cost of Sales	(178.6)	(200.6)	(207.5)	(201.5)	(196.4)	(193.3)	(168.8)	(214.2)	(214.0)	(219.6)
Gross Profit	77.4	92.6	90.8	91.3	84.8	88.8	72.2	87.5	92.8	96.5
EBITDA (pre IFRS 16)	25.6	33.3	30.3	32.1	26.7	26.4	16.9	22.6	26.0	28.5
EBITDA (IFRS 16 norm)						38.2	28.6	35.7	39.1	41.6
Op Profit (pre IFRS 16 norm)	20.1	25.6	22.3	24.2	18.7	19.1	7.3	12.7	15.9	18.2
Op Profit (IFRS 16 norm)						21.2	9.4	14.8	18.0	20.3
SBP	(0.4)	(0.3)	(0.6)	(0.6)	(0.7)	(1.4)	0.0	(0.7)	(0.7)	(0.7)
Net Interest	(0.5)	(1.0)	(1.2)	(1.2)	(1.5)	(4.8)	(4.4)	(4.2)	(4.0)	(3.9)
Intangible Amortisation	(0.0)	(1.1)	(1.1)	(1.1)	(1.2)	(0.3)	(0.3)	(0.3)	(0.3)	(0.3)
Exceptionals	(0.6)	(0.2)	(7.4)	(7.4)	(2.0)	(2.3)	(2.8)	0.0	0.0	0.0
PBT (IFRS 16 norm)	19.2	24.3	20.5	22.4	16.5	15.0	5.0	10.0	13.3	15.7
PBT (statutory)	18.6	23.0	12.0	13.9	13.3	12.4	1.9	9.7	13.0	15.4
Tax	(3.3)	(3.4)	(1.9)	(2.3)	(2.5)	(2.8)	0.7	(1.8)	(2.4)	(2.8)
Profit After Tax (norm)	15.9	20.9	17.6	19.1	14.0	12.1	5.7	8.2	10.9	12.9
Profit After Tax (statutory)	15.3	19.6	10.1	11.6	10.8	9.5	2.6	7.9	10.6	12.6
Average Number of Shares Outstanding (m)	135.2	141.5	142.6	142.6	142.9	142.9	143.0	144.5	144.5	144.5
EPS - normalised (p) – IFRS 16 from 2019	11.8	14.8	12.4	13.4	9.8	8.5	4.0	5.6	7.6	8.9
EPS - normalised (p) FD – IFRS 16 from 2019	11.7	14.7	12.4	13.4	9.8	8.5	4.0	5.6	7.5	8.9
EPS - statutory (p)	11.3	13.8	7.1	7.1	4.1	6.7	1.8	5.4	7.3	8.7
Dividend per share (p)	6.4	6.6	6.7	6.7	4.9	1.8	1.0	2.5	3.4	4.2
Gross Margin (%)	30.2	31.6	30.4	31.2	30.2	31.5	30.0	29.0	30.3	30.5
EBITDA pre IFRS 16 Margin (%)	10.0	11.3	10.2	11.0	9.5	9.3	7.0	7.5	8.5	9.0
Operating Margin pre IFRS 16 norm (%)	7.9	8.7	7.5	8.3	6.7	6.8	3.0	4.2	5.2	5.8
BALANCE SHEET										
Fixed Assets	93.5	108.5	106.2		111.7	125.6	108.3	115.1	113.7	112.1
Intangible Assets	59.7	70.2	69.6		73.7	75.7	75.0	77.0	76.7	76.4
Tangible Assets	33.1	37.9	36.0		37.3	46.1	29.5	34.3	33.2	31.9
Other	0.7	0.4	0.6		0.7	3.8	3.8	3.8	3.8	3.8
Current Assets	87.2	82.6	82.2		75.7	91.5	76.8	98.2	107.0	118.4
Stocks	23.6	28.2	29.6		29.2	30.3	29.6	38.6	38.5	39.5
Debtors	41.5	41.4	45.3		40.4	44.0	45.0	52.4	53.5	55.1
Cash	22.1	13.0	7.3		6.1	17.2	2.2	7.2	15.0	23.8
Current Liabilities	(68.8)	(79.2)	(79.2)		(69.3)	(77.4)	(62.1)	(80.1)	(81.1)	(83.5)
Creditors	(53.2)	(62.9)	(58.2)		(63.7)	(76.1)	(58.7)	(76.7)	(77.7)	(80.1)
Short term borrowings	(15.6)	(16.3)	(21.0)		(5.6)	(1.3)	(3.4)	(3.4)	(3.4)	(3.4)
Long Term Liabilities	(31.8)	(21.0)	(15.5)		(28.1)	(36.7)	(21.4)	(21.4)	(21.4)	(21.4)
Long term borrowings	(20.9)	(17.3)	(11.4)		(25.3)	(32.3)	(17.3)	(17.3)	(17.3)	(17.3)
Other long term liabilities	(10.9)	(3.7)	(4.1)		(2.8)	(4.4)	(4.1)	(4.1)	(4.1)	(4.1)
Net Assets	80.1	90.9	93.7		90.0	103.0	101.5	111.8	118.3	125.7
CASH FLOW										
Operating Cash Flow	23.8	30.8	19.9	18.1	25.8	34.8	23.7	33.3	38.0	40.4
Net Interest	(0.5)	(1.0)	(1.0)	(1.0)	(1.3)	(1.6)	(1.4)	(1.3)	(1.1)	(1.0)
Tax	(2.3)	(3.8)	(2.7)	(2.7)	(2.6)	(3.3)	(0.8)	(3.3)	(2.4)	(2.8)
Capex****	(9.0)	(12.7)	(7.1)	(5.3)	(12.5)	1.5	(8.0)	(4.0)	(9.2)	(9.2)
Acquisitions/disposals	(20.9)	(10.2)	(3.9)	(3.9)	0.0	(2.2)	0.0	(3.8)	0.0	0.0
Financing	0.0	0.0	0.0	0.0	(0.0)	(12.3)	(13.4)	(13.4)	(13.4)	(13.4)
Dividends	(6.7)	(9.1)	(9.5)	(9.5)	(8.8)	(7.1)	0.0	(2.6)	(4.1)	(5.2)
Net Cash Flow	(15.6)	(6.1)	(4.3)	(4.3)	0.6	9.7	0.1	5.0	7.8	8.8
Opening net debt/(cash)	(1.1)	14.4	20.6	20.6	25.1	24.8	16.4	18.5	13.5	5.7
Finance leases	0.4	1.9	(1.4)	(1.4)	(1.1)	0.0	0.0	0.0	0.0	0.0
Other	(0.3)	(2.1)	1.2	1.2	0.8	(1.4)	(2.2)	0.0	0.0	0.0
Closing net debt/(cash)**	14.4	20.6	25.1	25.1	24.8	16.4	18.5	13.5	5.7	(3.1)
IFRS 16 Leases						71.0	80.8	85.8	85.8	85.8

Source: Company accounts, Edison Investment Research. Note: *IFRS 16 from 2019. **Consistent with company-defined pre-IFRS 16 net debt, which includes some other (non IFRS 16) finance leases (H120: £4m). We have assumed this category of leases to be constant in our estimate years (and shown as short-term borrowings). ****FY21 net capex comprises £9.2m gross less £5.2m receipt of Telford II final proceeds.

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