EDISON

Kendrion

Q322 results review

Industrial continues on strong growth path

Industrial engineering

Kendrion's Q322 results showed a relatively good performance under difficult market conditions, with continued pressure from a shortage of materials, volatile demand and inflation. Revenues in the quarter were stronger than we expected; the Industrial division remained the top performer, with revenues up 27% y-o-y, while the Automotive division returned to growth with an 8% top-line increase. Kendrion expects the current difficult environment to continue for the rest of the year and into 2023 but is confident that the trends towards electrification and clean energy will drive strong growth in the medium term. The average of our three valuation methods points to a fair value of €22.2 per share.

Year end	Revenue (€m)	EBITDA* (€m)	EPS* (€)	DPS (€)	EV/EBITDA (x)	P/E (x)
12/20	396.4	44.6	0.79	0.40	8.3	20.9
12/21	463.6	55.8	1.39	0.70	8.2	15.1
12/22e	515.5	58.6	1.60	0.80	6.7	10.0
12/23e	541.3	68.7	1.96	0.98	5.6	8.2

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

Industrial: Strong performance continues

Kendrion's better than expected performance in Q322 was again driven by strong revenue growth in Industrial (27% of which 18% was organic). The division continues to benefit from the trend towards cleaner energy and the company remains focused on adding high-growth segments such as automated guided vehicles and collaborative robots. Automotive returned to growth with revenue up 8% (5% organic) despite the challenging market conditions (volatile demand, inflation and material shortages).

Medium-term outlook remains positive

Kendrion expects the unpredictability of the economic environment to continue into 2023, although there are signs that input cost pressures are easing in some market segments. Based on order books, management expects Industrial's performance to remain strong, while it is on track to realise €8m in cost savings in Automotive, with the full effect in 2023. In China, Kendrion is on track to double its manufacturing footprint by Q123, which would enable strong growth in that region (in both Industrial and Automotive). We have raised our revenue and EBITDA estimates by 3% for FY22, driven by the better-than-expected Q3 results. For FY23 and FY24, we have left our estimates unchanged given the uncertain economic outlook. These assumptions deliver a CAGR in normalised EPS for 2021–24 of 23%.

Valuation: Still offering ample upside

Kendrion is valued at an EV/EBITDA multiple for FY22e of 6.7x and a P/E of 10.0x. For its valuation we look at historical multiples, discounted cash flow (DCF) and peer multiples. We have not changed much in our estimates and valuation assumptions, and the average outcome of these valuation methods has not changed much either: €22.2 per share versus €21.7 previously.

22 November 2022

Price	**€16.00**
Market cap	**€242m**

Net debt (€m) at 30 September 2022	154
Shares in issue	15.1m
Free float	43%
Code	KENDR
Primary exchange	Euronext Amsterdam
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	18.9	5.5	(21.4)
Rel (local)	9.2	6.8	(9.0)
52-week high/low		€22.40	€13.02

Business description

Kendrion develops, manufactures and markets high-quality actuators for industrial applications (54% of 9M22 revenues) and automotive applications (46%). The geographical spread of FY21 revenues was Germany 39%, other Europe 30%, the Americas 16% and Asia 15%.

Next events

FY22 results	28 February 2023

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Edison profile page

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Q322 results: Stronger than expected growth

Kendrion has published its Q322 results, with stronger than expected revenue growth of 17% y-o-y to €133m, despite the continuing economic turmoil, inflation and demand volatility particularly in Automotive. According to management, market conditions in Q3 have not changed materially compared to the first half. 3T (an electronics and embedded systems expert acquired in September 2021) added 2% to revenues and positive exchange rates had an impact of 3%. Organic revenue growth of 12% y-o-y was better than we expected and showed an acceleration from the 2% growth in Q222 (or 5% when corrected for management's estimated impact of the lockdowns in China of €3.5m on Q2 revenues). Group volumes in Q3 were up 6%, which is a good improvement from slightly lower volumes in Q2. Price increases also contributed 6% to the overall organic revenue growth and that is at the same level as in Q222.

Exhibit 1: Kendrion's Q322 divisional revenues

€m	Q321	Q322	Change	Change constant scope	Change organic
Industrial Brakes	31.3	40.1	28%	24%	24%
Industrial Actuators & Controls	25.8	32.5	26%	14%	11%
Automotive	56.1	60.3	8%	5%	5%
Total revenues	**113.2**	**132.9**	**17%**	**14%**	**12%**

Source: Kendrion

The industrial activities benefited from high demand for products related to the transition towards cleaner energy. Industrial Brakes continued its strong performance, reporting 28% y-o-y growth of which 24% was organic. Industrial Actuators & Controls showed 26% growth, of which 12% came from 3T and 3% from positive exchange rate effects. Automotive returned to growth, showing 8% y-o-y growth (5% organic) after the decline in the first half, despite continuing semiconductor shortages, demand volatility and inflation. Within Automotive, developments in commercial vehicles are relatively stable with larger demand volatility in passenger cars. Commercial vehicles still have mostly diesel engines, but there is a big push for electric ones, which will drive the electrification trend in this market segment over the next few decades.

In China (around 10% of group revenues), production caught up with the backlog caused by lockdowns during H1. The construction of the new factory, which will double the manufacturing footprint towards 28,000m² is on schedule and Kendrion expects the plant to be operational in Q123.

Exhibit 2: Kendrion's Q322 results

€m	Q321	Q322	Change
Revenues	113.2	132.9	17%
Gross margin	48.0%	47.3%	
EBITDA normalised	**12.4**	**14.9**	**20%**
EBITDA margin	**11.0%**	**11.2%**	
Depreciation	(5.9)	(6.0)	2%
Amortisation, acquisition related	(1.0)	(1.2)	20%
EBIT normalised	5.5	7.7	40%
EBIT margin	4.9%	5.8%	
Non-recurring items	(0.5)	(1.6)	
EBIT reported	5.0	6.1	22%
Financial income and expenses	(0.8)	(0.5)	
Pre-tax income	4.2	5.6	34%
Taxes	(1.3)	(1.6)	23%
Net profit	2.9	4.0	38%
Net profit normalised	4.0	6.1	53%
Shares outstanding, average (m)	14.9	15.1	1%
EPS – reported (€)	0.19	0.27	37%
EPS – normalised (€)	0.27	0.40	51%

Source: Kendrion

Despite higher input prices, Kendrion managed to keep its gross margin relatively stable. As price increases of input materials are passed on to customers without margin, the gross margin was 70bp lower at 47.3% in Q3 (H122 +40bp). Continued operating leverage in Industrial and the higher revenue share of higher-margin Industrial Brakes resulted in an increase in normalised EBITDA margin of 20bp to 11.2%, despite weaker profitability in Automotive. This increase compares to the decline in EBITDA margin of 170bp in the first half, resulting in a 110bp decline in the first nine months of the year (9M22).

Within Automotive, Kendrion is on schedule to finalise the closure of the factory in Austria in Q422, which should result in annual savings of €4m. The company is also making good progress with the organisational change into Core and E as announced during its capital markets day on 8 September 2022, which should lead to cost savings of €4m in 2023.

The one-offs related to the organisation change within Automotive are now estimated at €5m (at the capital markets day, management estimated €6m), with €1.6m taken in Q322 and the remaining €3.4m will fall in Q422, according to management. The cash outflow from these P&L one-offs will be largely in FY23. With stable depreciation, lower financing costs and a lower tax rate, normalised net profit before amortisation in Q322 increased 53% to €6.1m.

Kendrion's financial position remains solid with net debt/EBITDA at 2.6x (covenant is <3.25x) and an equity ratio of 43%. Net debt in Q3 increased €8m to €154m versus Q2, mainly due to higher capex for the new production facility in China and new production lines in Automotive. Inventories remained at a high level but were slightly lower compared to Q2. Kendrion expects net debt to be lower at year end. At the Q222 analyst meeting in August, management indicated to expect a positive free cash flow in H222 and this was reiterated on the Q322 analyst call. This means that the free cash flow in Q4 must be higher than €9m, which was the level of negative free cash flow in Q3. This will mainly be realised via lower working capital in Q4, which is normally the weakest quarter of the year with a corresponding lower working capital.

Positive outlook despite difficult market conditions

Kendrion expects the current difficult economic environment to continue for the rest of the year and into 2023, but is confident that the trends towards electrification and clean energy will drive growth in the medium term. At the Q322 analyst meeting, management commented that, based on the order book, it expects the performance of Industrial to remain strong. In FY22, Kendrion is investing in product lines for projects in Automotive that will ramp up from 2023. There seems to be some easing in semiconductor shortages, but in Automotive there is still scarcity of certain components. It might change for the better over the next couple of months, but uncertainty is high. The company is on track to realise €8m in cost savings within its Automotive division, with the main benefit in 2023 (€4m related to the split in Automotive into Core and E and €4m related to the closure of its factory in Austria).

Kendrion's financial targets for 2019–25 are unchanged: organic revenue growth of at least 5% on average per year, an EBITDA margin of at least 15% in 2025 (12.0% in FY21) and return on invested capital of at least 25% in 2025 (FY21: 15.6%).

Exhibit 3: Change in estimates

€m	2022e			2023e			2024e		
	Old	New	Change	Old	New	Change	Old	New	Change
Revenue	500	516	3.0%	537	541	0.9%	582	584	0.4%
EBITDA normalised	57.0	58.6	2.9%	68.6	68.7	0.1%	81.3	81.1	(0.2%)
EBITDA margin	11.4%	11.4%		12.8%	12.7%		14.0%	13.9%	
EBITA margin	6.8%	6.9%		8.2%	8.1%		9.7%	9.6%	
Net profit adjusted	22.3	24.2	8.4%	29.6	29.6	0.2%	39.1	39.0	(0.1%)
EPS adjusted (€)	1.48	1.60	8.4%	1.96	1.96	0.2%	2.58	2.58	(0.1%)
DPS (€)	0.74	0.80	8.4%	0.98	0.98	0.2%	1.29	1.29	(0.1%)

Source: Edison Investment Research

We have raised our revenue estimate for FY22 after the better-than-expected results in Q322, and now expect 11% growth versus 8% previously, with an uplift in both divisions (Industrial from 17% to 20% growth and Automotive from -1% to 2%). Due to the economic uncertainty, we have left our revenue estimates for FY23 and FY24 broadly unchanged despite the higher basis in FY22. We expect revenue growth of 5% in FY23 and 8% in FY24, with stronger growth in Automotive as market research is still anticipating a recovery from the lower levels caused by the COVID-19 pandemic and supply chain constraints. Kendrion's underlying growth is still driven by the long-term trends of electrification and clean energy.

We have left our EBITDA margin estimates broadly the same for FY22–24, which reflects a slight increase in our EBITDA estimate for FY22, in line with the raised revenue forecast. This reflects a decline in EBITDA margin of 60bp for the full year after the decline of 110bp in 9M22. For FY23 and FY24 we expect further margin improvement, fuelled by the announced cost savings in Automotive and the operating leverage within Industrial. The easing of the shortage in materials will also help, but the timing of this is difficult to predict.

Our new estimates assume a CAGR in EPS in 2021–24e of 23%.

Valuation offers upside

For the valuation of Kendrion, we look at three different valuation methods: historical multiples, DCF and peer comparison (for more details see our recent outlook report).

Historical valuation: Kendrion is trading at a discount of 20% compared to its historical EV/EBITDA valuation of 8.4x (last eight years), based on our estimates for FY22. As the company's current profitability is somewhat below its eight-year average, with margins in automotive under pressure, we now assume a small discount of 5% to its historical multiples is justified (down from the valuation in line with historical multiples). This slightly changed assumption leads to a value per share of €20.7 per share (from €22.2 previously).

DCF valuation: we have left the assumptions in our DCF model unchanged and, in our earnings estimates, we only slightly raised our revenue and EBITDA forecasts for FY22 and have left FY23 and FY24 broadly the same. As a result, and using an unchanged WACC of 8.0%, the DCF outcome has not varied much since our last update in September: a value per share of €24.1, versus €23.9 previously.

Peer group comparison: we still think that a valuation in line with its peers is merited, based on the 2022e EV/EBITDA multiple, versus the current discount of 18%. As peer multiples have increased in the past few months, this delivers a higher value per share of €21.9, versus €18.8 previously.

The average of the three valuation methods is shown in Exhibit 4 and points to a valuation of €22.2 per share (previously €21.7).

Exhibit 4: Valuation methods for Kendrion

Valuation method	Edison assumptions	Equity value per share (€)
Historical valuation	2022e EV/EBITDA at a small discount of 5% to its historical multiples	20.7
DCF	Terminal growth 1.5%, terminal EBITA margin 7.5%	24.1
Peer group	2022e EV/EBITDA in line with peers	21.9
Average value per share		**22.2**
Current share price		16.0

Source: Edison Investment Research

Exhibit 5: Financial summary

€m	2019	2020	2021	2022e	2023e	2024e
Year end 31 December	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT						
Revenue	412.4	396.4	463.6	515.5	541.3	584.2
Gross Profit	193.3	191.0	225.8	248.7	262.8	284.2
EBITDA normalised	43.8	44.6	55.8	58.6	68.7	81.1
EBITDA reported	38.1	40.2	51.7	51.2	68.7	81.1
Depreciation & Amortisation	(24.0)	(25.7)	(23.9)	(22.8)	(24.6)	(24.7)
EBITA normalised	19.8	18.9	31.9	35.8	44.1	56.3
Amortisation of acquired intangibles	(2.2)	(4.4)	(3.9)	(4.8)	(4.8)	(4.8)
Exceptionals (Edison definition)	(5.7)	(4.4)	(4.1)	(7.4)	0.0	0.0
EBIT reported	11.9	10.1	23.9	23.6	39.3	51.5
Net Interest	(0.9)	(4.4)	(3.7)	(3.3)	(3.0)	(2.4)
Participations	0.0	0.0	(0.1)	0.0	0.0	0.0
Profit Before Tax	11.0	5.7	20.1	20.3	36.3	49.2
Reported tax	(2.7)	(1.4)	(5.7)	(5.8)	(10.3)	(13.8)
Profit After Tax	8.3	4.3	14.4	14.5	26.0	35.4
Net income (normalised)	12.6	11.7	20.6	24.2	29.6	39.0
Net income (reported)	8.3	4.3	14.4	14.5	26.0	35.4
Average number of shares (m)	13.5	14.8	14.8	15.1	15.1	15.1
Total number of shares (m)	14.9	14.9	14.9	15.1	15.1	15.1
EPS normalised before amortisation (€)	0.94	0.79	1.39	1.60	1.96	2.58
EPS reported (€)	0.62	0.29	0.97	0.96	1.72	2.34
DPS (€)	0.00	0.40	0.70	0.80	0.98	1.29
Revenue growth	-8.1%	-3.9%	17.0%	11.2%	5.0%	7.9%
Gross Margin	47.4%	48.4%	48.3%	48.3%	48.5%	48.6%
EBITDA Margin	10.6%	11.3%	12.0%	11.4%	12.7%	13.9%
Normalised Operating Margin	4.8%	4.8%	6.9%	6.9%	8.1%	9.6%
BALANCE SHEET						
Fixed Assets	244.8	299.6	324.5	337.7	334.2	331.8
Intangible Assets	115.5	159.1	183.4	181.6	179.0	176.4
Tangible Assets	111.4	118.7	121.9	136.9	136.0	136.2
Investments & other	17.9	21.8	19.2	19.2	19.2	19.2
Current Assets	113.2	129.5	166.3	172.7	178.9	199.7
Stocks	56.3	61.7	79.7	88.1	91.9	98.6
Debtors	42.9	47.2	56.8	63.2	66.3	71.6
Other current assets	6.9	7.6	11.2	12.5	13.1	14.1
Cash & cash equivalents	7.1	13.0	18.6	9.0	7.6	15.5
Current Liabilities	73.8	87.9	97.6	107.1	111.8	119.7
Creditors	41.3	44.0	51.6	57.4	60.3	65.0
Other current liabilities	26.9	31.9	33.2	36.9	38.8	41.8
Short term borrowings	5.6	12.0	12.8	12.8	12.8	12.8
Long Term Liabilities	80.7	137.8	170.2	176.2	160.2	150.2
Long term borrowings	48.9	104.2	136.4	136.4	126.4	116.4
Other long term liabilities	31.8	33.6	33.8	39.8	33.8	33.8
Shareholders' equity	203.5	203.4	223.0	227.2	241.1	261.7
Balance sheet total	358.0	429.1	490.8	510.5	513.1	531.5
CASH FLOW						
Op Cash Flow before WC and tax	36.1	40.6	54.6	57.2	62.7	81.1
Working capital	13.0	5.4	(17.4)	(6.5)	(2.9)	(5.1)
Tax	(6.1)	(1.3)	(6.2)	(5.8)	(10.3)	(13.8)
Net interest	(2.1)	(2.9)	(3.2)	(3.3)	(3.0)	(2.4)
Net operating cash flow	40.9	41.8	27.8	41.6	46.5	59.8
Capex	(20.0)	(16.0)	(30.0)	(40.8)	(25.9)	(27.1)
Acquisitions/disposals	0.1	(78.2)	(18.8)	0.0	0.0	0.0
Equity financing	23.3	0.0	0.0	0.0	0.0	0.0
Dividends	(8.1)	0.0	(4.3)	(10.4)	(12.1)	(14.8)
Other	(3.1)	(3.4)	4.0	0.0	0.0	0.0
Net Cash Flow	33.1	(55.8)	(21.3)	(9.6)	8.6	17.9
Opening net debt/(cash)	80.5	47.4	103.2	124.5	134.1	125.5
Closing net debt/(cash)	47.4	103.2	124.5	134.1	125.5	107.6

Source: Kendrion accounts, Edison Investment Research

EDISON

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