

Treatt

Growth continues apace

FY17 results & share placement

Food & beverages

Treatt has posted yet another year of excellent growth, with revenues up 25% and adjusted PBT up c 45%. The company has reached its FY20 financial objectives three years early, and the management has therefore updated its strategy to take the company through to the next phase. A new facility is being built in the UK, and the US site is being expanded. Both projects are on track and Treatt has now announced a share placing to fund these projects. This was always flagged as a possibility. We update our forecasts to reflect the FY17 results and the share placement. Our fair value is 515p (from 522p previously).

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
09/16	88.0	9.6	14.3	4.4	33.6	0.9
09/17	109.6	14.0	20.4	4.8	23.5	1.0
09/18e	117.3	14.4	19.2	4.6	25.0	1.0
09/19e	123.2	15.5	20.7	4.9	23.2	1.0

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

FY17 was a record year

FY17 was a record year for the company, with revenues topping £100m for the first time (£109.6m), adjusted PBT of £12.9m and EPS of 18.3p on a company adjusted basis. The growth rate achieved in FY17 will be hard to replicate and should not be considered the new norm, but it does demonstrate the company is successfully embracing the sweet spot in flavour ingredients. We note management's comments that FY18 has started well, and the growth in FY17 was broad-based – both in terms of geography and product mix – which sets a good base for the future.

New strategy builds on previous foundations

Treatt's new strategy is an evolution of the previous one. The focus remains on the company's core areas of citrus, tea and sugar reduction. The theme of deep customer relationships continues: this has served the company well and should further help to speed up the innovation and success rate with its customers. The management is also focused on enhancing the company's technical abilities to drive the business forward through product innovation and operational efficiencies, which in turn should drive margin expansion. The UK relocation and US expansion will help achieve these objectives.

Valuation: Fair value is 515p

We value Treatt using a DCF model, which now indicates a fair value of 515p (previously 522p), an attractive c 7% upside to the current share price. We have incorporated the share placement into our forecasts, hence reducing our net debt and increasing the number of shares. We have assumed net proceeds of c £22m. Treatt trades at 24.6x and 14.8x calendar P/E and EV/EBITDA multiples for 2018, representing discounts of c 15% and 20% to its ingredients peer group, respectively. Given the current growth trajectory of the business, and our forecast for low double-digit CAGR EPS for 2016-20, we believe this level of discount is unwarranted.

30 November 2017

Price **481.75p**

Market cap **£251m**

Net debt (£m) at 30 September 2017 10.2

Shares in issue 52.1m

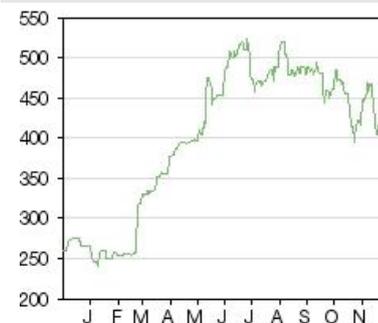
Free float 100%

Code TET

Primary exchange LSE

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs 14.1 (0.6) 86.7

Rel (local) 15.6 (1.7) 69.3

52-week high/low 523.0p 239.8p

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

EGM 18 December 2017

Trading update February 2018

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Forecast revisions

FY17 results were broadly in line with our expectations. Following our upgrades in October with the pre-close trading update, our sales forecast was £108.7m and FY revenues came in slightly higher at £109.6m. Adjusted PBT was £12.9m, or an impressive c 45% growth vs FY16. Adjusted EPS was up c 40% to 18.3p. We illustrate the slight changes to our P&L forecasts in Exhibit 1 below. We have incorporated the share placement into our forecasts and have therefore made some changes to our net debt assumptions. We have assumed a placement equivalent to 10% of the share capital, placed at 410p, to give net proceeds of c £22m. We illustrate these in Exhibit 2 and these affect our PBT and EPS forecasts through lower interest charges and a higher number of shares.

Exhibit 1: Old vs new key P&L forecasts

	EPS (p)*			PBT (£000s)*			Revenue (£000s)		
	Old	New	% change	Old	New	% change	Old	New	% change
2018e	19.3	17.3	-10.1%	13,479	13,352	-0.9%	116,340	117,301	0.8%
2019e	19.2	18.7	-2.8%	13,429	14,380	7.1%	122,157	123,166	0.8%

Source: Edison Investment Research. Note: *Stated on IFRS basis.

Exhibit 2: Old vs new net (debt)/cash forecasts, £000s

	Old	New	% change
2018e	(26,984)	(2,728)	-89.9%
2019e	(38,642)	(15,531)	-59.8%

Source: Edison Investment Research

Valuation update

We illustrate Treatt's valuation versus its ingredients peer group in Exhibit 3 below. Treatt trades at a significant discount to its peer group on all metrics. Some discount can be applied 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. However, we believe a 15-25% discount on EV/EBITDA and P/E is unwarranted.

Exhibit 3: Benchmark valuation

	Market cap (m)	P/E (x)		EV/EBITDA (x)		Dividend yield (%)	
		2018e	2019e	2018e	2019e	2018e	2019e
Givaudan	CHF 20,665	28.2	26.4	19.5	18.1	2.6%	2.8%
IFF	\$12,207	26.7	24.6	17.5	16.1	1.7%	1.9%
Symrise	CHF 10,690	31.2	28.5	16.5	15.2	1.3%	1.4%
Frutarom	ILS 18,312	33.8	28.3	22.0	18.9	0.3%	0.4%
Chr Hansen	DKK 73,969	40.7	35.8	26.4	23.4	1.6%	1.8%
Kerry	€ 15,502	25.9	23.8	18.6	16.8	0.7%	0.8%
Ingredient	\$10,043	18.1	16.8	10.3	9.6	1.5%	1.7%
Peer group average		29.2	26.3	18.7	16.9	1.2%	1.3%
Treatt	£247.4	24.6	22.9	14.8	12.7	1.0%	1.0%
Premium/(discount) to peer group (%)		-15.9%	-13.1%	-20.6%	-25.0%	-18.1%	-22.2%

Source: Bloomberg (prices as of 30 November 2017). Note: Treatt figures are calendarised to aid comparison.

Our DCF-derived fair value is now 515p (previously 522p) following the changes to our model detailed in our forecast review section above. Our longer-term sales growth forecast is 5% pa, falling to 2% growth in perpetuity. Our DCF is calculated based on a WACC of 7.3% (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	2015	2016	2017	2018e	2019e	2020e
Year end September		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS							
Revenue		85,934	88,040	109,627	117,301	123,166	128,093
Cost of Sales		(66,955)	(67,639)	(82,819)	(88,258)	(92,055)	(95,609)
Gross Profit		18,979	20,401	26,808	29,043	31,111	32,483
EBITDA		10,307	11,604	16,307	17,317	20,539	22,680
Operating Profit (before amort., except and sbp)		9,063	10,257	14,908	15,362	16,886	17,840
Intangible Amortisation		(175)	(142)	(137)	(160)	(160)	(160)
Share-based payments		(198)	(566)	(966)	(915)	(986)	(1,053)
Other		0	0	0	0	0	0
Operating Profit		8,690	9,549	13,805	14,287	15,741	16,626
Net Interest		(740)	(703)	(913)	(936)	(1,361)	(1,260)
Exceptionals		(174)	(553)	0	0	0	0
Profit Before Tax (norm)		8,323	9,554	13,995	14,427	15,525	16,580
Profit Before Tax (FRS 3)		7,776	8,293	12,892	13,352	14,380	15,366
Profit Before Tax (company)		7,950	8,846	12,892	13,352	14,380	15,366
Tax		(1,786)	(2,144)	(3,347)	(3,405)	(3,667)	(3,918)
Profit After Tax (norm)		6,537	7,410	10,648	11,022	11,858	12,661
Profit After Tax (FRS 3)		5,990	6,149	9,545	9,947	10,713	11,448
Average Number of Shares Outstanding (m)		51.5	51.9	52.2	57.4	57.4	57.4
EPS - normalised (p)		12.7	14.3	20.4	19.2	20.7	22.1
EPS - normalised & fully diluted (p)		12.6	14.1	19.8	18.7	20.1	21.4
EPS - (IFRS) (p)		11.6	11.8	18.3	17.3	18.7	19.9
Dividend per share (p)		4.0	4.4	4.8	4.6	4.9	5.2
Gross Margin (%)		22.1	23.2	24.5	24.8	25.3	25.4
EBITDA Margin (%)		12.0	13.2	14.9	14.8	16.7	17.7
Operating Margin (before GW and except.) (%)		10.5	11.7	13.6	13.1	13.7	13.9
BALANCE SHEET							
Fixed Assets		13,381	16,161	19,532	43,176	63,211	62,132
Intangible Assets		1,736	3,364	3,331	3,171	3,011	2,851
Tangible Assets		10,998	11,361	14,821	38,625	58,820	57,901
Investments		647	1,436	1,380	1,380	1,380	1,380
Current Assets		45,045	54,435	68,230	71,295	74,129	76,392
Stocks		25,799	29,990	42,878	45,410	47,434	49,076
Debtors		17,635	17,853	19,973	21,137	21,947	22,569
Cash		1,477	6,588	4,748	4,748	4,748	4,748
Other		134	4	631	0	0	0
Current Liabilities		(13,481)	(16,388)	(27,003)	(28,722)	(38,444)	(33,244)
Creditors		(12,675)	(15,834)	(19,266)	(23,737)	(24,924)	(25,921)
Short term borrowings		(567)	(487)	(7,680)	(4,984)	(13,519)	(7,323)
Provisions		(239)	(67)	(57)	0	0	0
Long Term Liabilities		(11,760)	(17,021)	(14,281)	(9,877)	(13,945)	(10,646)
Long term borrowings		(7,065)	(7,755)	(7,293)	(2,492)	(6,760)	(3,661)
Other long term liabilities		(4,695)	(9,266)	(6,988)	(7,385)	(7,185)	(6,985)
Net Assets		33,185	37,187	46,478	75,872	84,952	94,634
CASH FLOW							
Operating Cash Flow		8,667	10,804	4,683	19,343	18,691	21,215
Net Interest		(740)	(703)	(913)	(936)	(1,361)	(1,260)
Tax		(1,469)	(2,022)	(2,822)	(3,405)	(3,667)	(3,918)
Capex		(924)	(679)	(5,111)	(25,760)	(23,847)	(3,921)
Acquisitions/disposals		(103)	(861)	(1,667)	0	0	0
Financing		147	280	270	20,759	0	0
Dividends		(1,978)	(2,095)	(3,025)	(2,506)	(2,618)	(2,820)
Net Cash Flow		3,600	4,724	(8,585)	7,497	(12,803)	9,295
Opening net debt/(cash)		9,584	6,155	1,654	10,225	2,728	15,531
HP finance leases initiated		0	0	0	0	0	0
Other		(171)	(223)	14	0	0	0
Closing net debt/(cash)		6,155	1,654	10,225	2,728	15,531	6,236

Source: Edison Investment Research, Treatt accounts

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