Eddie Stobart Logistics

Interim results

Interims show delivery on growth plans

Industrial support services

Eddie Stobart Logistics' (ESL) H1 numbers, well trailed at the trading update in July, showed high levels of growth (13% revenues and 14% EBIT) consistent with management guidance and market expectations. New contract wins, which totalled £25m in the first half, were bolstered by organic growth in key business units. The iForce acquisition is integrating well, with the post-period acquisitions of Speedy Freight (announced at the trading update) and the remaining 50% of the Logistics People (announced yesterday) set to benefit earnings. Taken together, these growth drivers helped ESL achieve a slight increase in EBIT margin from 5.8% to 5.9%, which is well above other listed logistics firms. Also, H117 witnessed the announcement of the company's maiden dividend of 1.4p. We increase our earnings and FY17 acquisition charge to reflect post-balance sheet events and nudge up our fair value to 203p.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
11/15	496.5	21.0	5.4	0.0	29.6	N/A
11/16	570.2	26.1	6.9	0.0	23.2	N/A
11/17e	648.2	41.4	10.8	5.4	14.8	3.4
11/18e	750.2	51.7	12.5	6.3	12.8	3.9

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

Contract wins plus M&A remain the drivers

We were reassured to see double-digit revenue and EBITDA expansion driven by the growth businesses of E-Commerce and Manufacturing, Industrial & Bulk (MIB), as well as £25m of new contract wins and contributions from the iForce acquisition. With two further acquisitions post-period, ESL is well-placed to deliver future growth. In short, we retain the view expressed in our initiation note, that ESL's strategy of allocating capital to high-growth business units and maintaining margin discipline offers investors an attractive blend of growth and downside protection. Also of note also was ESL's high cash conversion, with (company-defined) free cash flow as a percentage of EBITDA at 56% vs -19% in H116.

Underlying earnings forecasts tweaked upwards

We slightly increase our underlying revenue, EBITDA and EBIT growth forecasts to account for the acquisitions. Our 14% three-year revenue CAGR and 16% EBIT CAGR are attractive in a sector context. We have also increased the capex charge for the post-balance sheet acquisitions.

Valuation: Increased to 203p per share

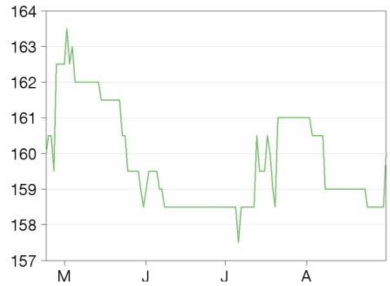
The net effect of increased underlying earnings forecasts and increased acquisition costs results in a marginally increased fair value of 203p per share, which offers investors 27% upside to the current price. We continue to base our fair value on EVA and DCF methodologies.

1 September 2017

Price	**160p**
Market cap	**£573m**

Estimated net debt (£m) at 30 November 2017	90.3
Shares in issue	357.9m
Free float	72.2%
Code	ESL
Primary exchange	AIM
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	(0.6)	1.0	N/A
Rel (local)	(1.3)	2.0	N/A
52-week high/low		163.5p	157.5p

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

FY17 results	January 2018

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H117 in line with expectations, FY17 looking strong

Under the current reporting system, Road Transport accounts for the majority of revenue and almost all EBITDA. In this context, 15% h-o-h EBITDA growth for Road Transport is very strong. E-Commerce and MIB, as well as acquisitions and new contracts, are the largest drivers behind group revenue growth. Given the strong growth already delivered in E-Commerce plus the impact of acquisitions, we are confident of a strong H2 during the peak E-Commerce season.

Exhibit 1: Divisional analysis

Revenues	H116	H117	% change
Road Transport	191.6	199.3	4
CL & Warehousing	45.5	49.1	8
EU Transport	18.8	19.9	6
Other divisions, central and eliminations	10.5	18.5	76
Total reported	266.4	286.8	8
Total less discontinued	**253.6**	**286.8**	**13**
Underlying EBITDA			
Road Transport	16.3	18.7	15
CL & Warehousing	2.2	2.6	18
EU Transport	1.6	0.8	(50)
Other divisions, central and eliminations	(1.2)	(2.2)	83
Total reported	18.9	19.9	5
Total less discontinued	**17.9**	**19.9**	**11**
Underlying EBITDA margin			
Road Transport	8.5%	9.4%	
CL & Warehousing	4.8%	5.3%	
EU Transport	8.5%	4.0%	
Other divisions, central and eliminations	-11.4%	-11.9%	
Total reported	**7.1%**	**6.9%**	

Source: Eddie Stobart logistics, Edison Investment Research

Management has indicated that it may change its reporting segments to be consistent with its key end-markets, as shown in Exhibit 2. As can be seen, in keeping with management guidance, MIB and E-Commerce are providing the bulk of revenue growth. For now there is no margin information given for each of these segments. However, we note that, excluding the effect of discontinued businesses, each segment is growing in absolute terms and well ahead of the end-market growth rate. Retail, for instance, grew at 10% (versus the -5% reported) excluding discontinued businesses while E-Commerce grew at 51%, not 42% as reported at headline level, which is impressive, especially considering there was only a one-month benefit from iForce.

Exhibit 2: Divisional revenue split by end-market

Revenues	H116	H117	% change
Retail	84.2	80.0	(5)
Consumer	71.4	74.7	5
MIB	66.3	80.9	22
E-Commerce	26.0	36.9	42
Non-sector specific	18.5	14.3	(23)
Total	266.4	286.8	8
Total less discontinued	253.6	286.8	13

Source: Eddie Stobart logistics, Edison Investment Research

Financials and forecasts

We have nudged up our earnings forecasts from FY18 to reflect full year contributions from the Speedy Freight and the Logistics People (TLP) acquisitions. We have also added the acquisition costs for both, which increases our net debt forecasts. We have added a £6m exceptional refinancing charge, accounted for in net interest. This comes on top of several non-recurring exceptional items already included in our forecast, which includes restructuring and listing charges from earlier in the year. A summary of all of our earnings changes in included in Exhibit 3.

Exhibit 3: Earnings forecast changes

£m		2017e	2018e
New revenues		**648**	**750**
Old revenues		648	742
+/- New vs old		0.0%	1.1%
New EBITDA		**55.7**	**65.3**
Old EBITDA		55.7	64.4
+/- New vs old		0.0%	1.4%
New EPS (p)		**10.8**	**12.5**
Old EPS		10.9	12.3
+/- New vs old		-1.3%	1.8%
New DPS (p)		**5.4**	**6.3**
Old DPS		5.5	6.2
+/- New vs old		-1.3%	1.8%
New capex & acquisitions		**(53.6)**	**(7.0)**
Old Capex & acquisitions		(52.5)	(7.0)
+/- New vs old		2.0%	0.0%
New net debt		**90.3**	**78.1**
Old net debt		79.1	66.9
+/- New vs old		14.2%	16.8%

Source: Edison Investment Research

Valuation

We increase our valuation slightly to 203p. This is based on an average of a DCF (WACC 7.3%, terminal growth 1%) of 200.5p and an EVA analysis, which implies 206.3p.

Exhibit 4: DCF model

DCF valuation	£m	p/share				
EV (£m)	807.9	225.7				
FY17e net debt (£m)	90.3	15.9				
Current number of shares (m)	357.9					
Fair value (£m)	717.7	200.5				
Current market cap (£m)	569.1	159.0				
Upside/(downside) (%)	26.1%					
DCF	**2017e**	**2018e**	**2019e**	**2020e**	**2021e**	**Terminal Value**
EBIT	48.6	57.2	65.4	70.0	74.9	
Less cash taxes	(2.8)	(6.8)	(8.2)	(8.7)	(9.4)	
Tax rate	5.7%	11.9%	12.5%	12.5%	12.5%	
NOPLAT	45.9	50.4	57.3	61.3	65.6	
Working Capital	(12.7)	(11.9)	(15.1)	(15.9)	(16.7)	
Add back depreciation	7.0	8.1	9.3	9.8	10.3	
Less capex	(7.5)	(7.0)	(7.0)	(7.4)	(7.7)	
Free cash flow	32.7	39.6	44.4	47.8	51.4	51.9
FCF growth		21.1%	12.1%	7.6%	7.6%	1.0%
WACC	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%
Year	0.0	1.0	2.0	3.0	4.0	
Discount factor	1.00	0.93	0.87	0.81	0.75	0.75
Discount cash flow	32.7	36.9	38.6	38.7	38.8	622.2
NPV	807.9	775.2	738.3	699.7	661.0	622.2
EV/EBITDA	14.5x	12.4x	10.8x	10.1x	9.5x	

Source: Edison Investment Research. Note: Prices as at 31 August 2017.

As shown in Exhibit 5, ESL currently trades on 11.3x one-year forward EV/EBIT and 12.7x one-year forward P/E. We believe that the stock should trade above these levels based on its high growth trajectory.

Exhibit 5: Market-implied multiples

Reverse valuations		FY17e	FY18e	FY19e
Market cap (£m)		569	569	569
Net debt (£m)		90	78	64
EV (£m)		659	647	634
EBIT (£m)		48.6	57.2	65.4
Market implied EV/EBIT		**13.6x**	**11.3x**	**9.7x**
Price per share (p)		159.0	159.0	159.0
Underlying earnings per share (p/share) (Edison definition, pre-amortisation)		10.80	12.55	14.50
P/E		**14.7x**	**12.7x**	**11.0x**

Source: Edison Investment Research

We use a one-year forward EVA calculation, which includes both the capital employed and adds back the lease expense. We include the fair value per share of 206p in our fair value calculation. As argued in our initiation, we believe this definition is prudent as it includes the operating lease liability and asset, as well as accounting for the lease cost as interest.

Exhibit 6: Economic value-added valuation

£m	2016	2017e	2018e
Simple ROCE calculation			
Capital employed (total fixed assets incl amort + current assets - current liabilities)	288.3	327.7	336.1
NOPAT (underlying EBIT - tax)	40.7	45.9	50.4
ROCE (%)	14.1%	14.0%	15.0%
WACC (%)	7.3%	7.3%	7.3%
ROCE/WACC multiple (x)	1.9x	1.9x	2.1x
Net debt	165.5	90.3	78.1
Net debt/ EBITDA (x)	3.4x	1.6x	1.2x
EVA fair value (ROCE/WACC* capital employed - liabilities)	392.3	538.3	612.7
Fair value per share (pence per share)		150.4	171.2
Excluding intangibles ROCE calculation			
Capital employed (total fixed assets incl amort + current assets - current liabilities)	288.3	327.7	336.1
Intangibles	219.3	209.8	200.3
Capital employed less intangibles	68.9	117.9	135.8
NOPAT (underlying EBIT - tax)	40.7	45.9	50.4
ROCE (%)	59.1%	38.9%	37.1%
WACC (%)	7.3%	7.3%	7.3%
ROCE/WACC multiple (x)	8.1x	5.3x	5.1x
Net debt	165.5	90.3	78.1
Net debt/ EBITDA (x)	3.4x	1.6x	1.2x
EVA fair value (ROCE/WACC* capital employed - liabilities)	392.3	538.3	612.7
Fair value per share (pence per share)		150.4	171.2
Including operating lease ROCE calculation			
Capital employed (total fixed assets incl amort + current assets - current liabilities)	288.3	327.7	336.1
Intangibles	219.3	209.8	200.3
Operating lease liability	462.2	462.2	462.2
Capital employed less intangibles plus operating lease liability	531.1	580.1	598.0
NOPAT (underlying EBIT - tax)	40.7	45.9	50.4
Operating lease cost	71.5	72.0	72.0
EBIT pre operating lease cost	112.2	117.9	122.4
ROCE (%)	21.1%	20.3%	20.5%
WACC (%)	9.5%	9.5%	9.5%
ROCE/WACC multiple (x)	2.2x	2.1x	2.2x
Net debt (adjusted for £472m operating lease liability)	637.5	562.3	550.1
Net debt/ EBITDA (x)	5.3x	4.4x	4.0x
EVA fair value (ROCE/WACC* capital employed - liabilities)	543.6	678.5	738.5
Fair value per share (pence per share)		189.6	**206.3**

Source: Edison Investment Research, Note: *Return on capital employed (ROCE) divided by the weighted average cost of capital (WACC).

Exhibit 7: Financial summary

£m	2015	2016	2017e	2018e	2019e
Year-end 30 November	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS					
Revenue	496.5	570.2	648.2	750.2	844.5
EBITDA	44.5	48.2	55.7	65.3	74.7
Operating Profit (before amort. and except.)	37.7	42.0	48.6	57.2	65.4
Intangible Amortisation	(9.5)	(9.5)	(9.5)	(9.5)	(9.5)
Exceptionals	(3.1)	(2.4)	(15.0)	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0
Operating Profit	25.1	30.1	24.1	47.7	55.9
Net Interest	(16.7)	(16.0)	(7.2)	(5.5)	(5.3)
Profit Before Tax (norm)	21.0	26.1	41.4	51.7	60.1
Profit Before Tax (FRS 3)	8.5	14.1	16.9	42.2	50.6
Tax	(1.6)	(1.3)	(2.8)	(6.8)	(8.2)
Profit After Tax (norm)	19.4	24.7	38.7	44.9	51.9
Profit After Tax (FRS 3)	6.8	12.8	14.1	35.4	42.4
Minority interest	0.0	0.0	0.9	1.3	3.2
Net Income (norm)	19.4	24.7	39.5	46.2	55.1
Net Income (FRS 3)	6.9	12.8	15.0	36.7	45.6
Average Number of Shares Outstanding (m)	357.9	357.9	357.9	357.9	357.9
EPS (pence per share) - normalised	5.4	6.9	10.8	12.5	14.5
EPS (pence per share) - normalised and fully diluted	5.4	6.9	10.8	12.5	14.5
EPS (pence per share) - (IFRS)	1.9	3.6	4.0	9.9	11.8
Dividend per share (pence per share)	0.0	0.0	5.4	6.3	7.3
EBITDA Margin (%)	9.0	8.4	8.6	8.7	8.9
Operating Margin (before GW and except.) (%)	7.6	7.4	7.5	7.6	7.7
BALANCE SHEET					
Fixed Assets	262.7	258.1	295.1	284.5	272.7
Intangible Assets	225.5	219.3	209.8	200.3	190.8
Tangible Assets	36.8	37.9	84.4	83.3	81.0
Investments	0.4	0.9	0.9	0.9	0.9
Other	0.0	0.0	0.0	0.0	0.0
Current Assets	120.9	150.3	167.6	198.1	228.3
Stocks	1.9	2.4	2.7	3.1	3.5
Debtors	114.9	133.8	145.6	168.5	189.7
Cash	4.1	14.1	19.3	26.5	35.1
Current Liabilities	(109.7)	(120.1)	(135.1)	(146.5)	(153.0)
Creditors	(99.6)	(110.6)	(125.5)	(137.0)	(143.4)
Short term borrowings	(5.5)	(6.2)	(6.2)	(6.2)	(6.2)
Other	(4.5)	(3.3)	(3.3)	(3.3)	(3.3)
Long Term Liabilities	(197.2)	(198.8)	(113.3)	(108.3)	(103.3)
Long term borrowings	(168.5)	(173.4)	(103.4)	(98.4)	(93.4)
Employee benefits	0.0	0.0	0.0	0.0	0.0
Other long term liabilities	(28.7)	(25.5)	(10.0)	(10.0)	(10.0)
Net Assets	76.8	89.4	214.3	227.8	244.7
CASH FLOW					
Operating Cash Flow	32.7	29.7	28.0	53.5	59.6
Net Interest	(12.8)	(10.3)	(7.2)	(5.5)	(5.3)
Tax	(3.9)	(1.7)	(2.8)	(6.8)	(8.2)
Capex	(7.7)	(8.1)	(7.5)	(7.0)	(7.0)
Acquisitions/disposals	18.7	5.5	(46.1)	0.0	0.0
Financing	0.5	0.0	117.1	0.5	0.5
Dividends	0.0	0.0	(6.4)	(22.5)	(25.9)
Net Cash Flow	27.6	15.2	75.2	12.2	13.6
Opening net debt/(cash)	191.4	169.9	165.5	90.3	78.1
HP finance leases initiated	0.0	0.0	0.0	0.0	0.0
Other	(6.1)	(10.8)	0.0	(0.0)	(0.0)
Closing net debt/(cash)	169.9	165.5	90.3	78.1	64.5

Source: Company accounts, Edison Investment Research

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