Epwin Group

FY18 results

Improving ongoing business footprint

Construction & materials

Steps were successfully taken by Epwin to consolidate its ongoing operational footprint in FY18, a challenging trading year. We expect growth to resume this year with a small contribution from PVS (acquired after the year-end) also. It is too soon to call a significant uptick in market conditions but the start to FY19 has been encouraging according to management comments. An 8.3x P/E multiple offers a reasonable entry point and investors can collect a 3.9% yield with the final dividend payment (and 6.0% prospectively for FY19).

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/17**	292.8	22.4	13.4	6.7	6.7	8.1
12/18	281.1	16.5	9.8	4.9	8.5	5.9
12/19e	291.3	17.6	10.1	5.0	8.3	6.0
12/20e	296.2	18.7	10.7	5.3	7.8	6.3

Note: *PBT and EPS (fully diluted) are normalised, excluding intangible amortisation and exceptionals. **Restated to exclude discontinued operations.

Some positive signals in tough FY18 trading year

FY18 results matched our expectations with respect to earnings and year-end net debt levels in subdued market conditions. Epwin did post both volume and price uplifts in underlying terms for the ongoing businesses and both divisions recorded increased profitability from these operations in H2. Some successful restructuring actions were taken during the year though the effects of client losses in the prior year together with input cost pressures pared back headline revenues and underlying EBIT by 4% and 23%, respectively. Cash flow control was evident with a stable net debt position at c £25m despite the profit reduction and increased capex, with working capital inflows contributing well to this outturn.

PVS adds to an encouraging start to FY19

FY19 to date has seen a continuation of the positive volume and price momentum referred to above and the additions of Amicus (March 2018) and PVS (January 2019) will contribute to the forward momentum that we expect in the current year. Significant restructuring work has been undertaken and with a further warehouse consolidation move planned for later this year, the ongoing operational footprint changes should be substantially complete in Q120 Our earnings estimates are marginally lower for FY19 and higher for FY20 (versus our prior estimates) and we expect to see year-on-year growth in all three forecast years.

Valuation: Resuming growth

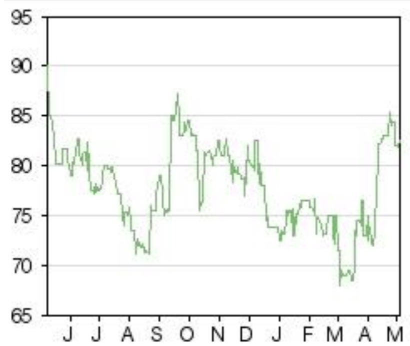
After a period of decline to a March low of 68p, Epwin's share price has rebounded well following the FY18 results, returning to levels last seen in October last year. We expect FY18 to have been the trough earnings year; while our compound growth expectations are currently modest, corporate messaging is likely to become more positive in our view as restructuring activities taper down. The current year P/E and EV/EBITDA multiples are 8.3x and 5.1x, respectively, with a prospective 6.0% dividend yield (or 3.9% with the FY18 final).

7 May 2019

Price	83.0p
Market cap	£118m

Net debt (£m) at end December 2018	24.8
Shares in issue	142.9m
Free float	67%
Code	EPWN
Primary exchange	AIM
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	14.6	7.6	(6.6)
Rel (local)	12.1	3.6	(4.4)
52-week high/low		90.0p	68.0p

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

FY18 final DPS 3.20p ex dividend	9 May
AGM	21 May
FY18 final DPS to be paid	3 June

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Edison profile page

Epwin Group is a research client of Edison Investment Research Limited

FY18 results overview

FY18 saw lower headline revenues and operating profit reflecting the annualised effects of two significant client losses towards the end of the prior year, compounded by input cost pressures in the year and, as flagged with the FY17 results, management rebased the full year dividend. That said, underlying trading contained some positive indicators – including volume and price increases – and a number of restructuring projects were successfully completed in the year. Year-end net debt was stable at c £25m, or 0.9x EBITDA.

Exhibit 1: Epwin Group divisional and interim splits

£m	2017	2017R	2018	FY
				% chg y-o-y
Group revenue	298.3	292.8	281.1	**-4.0%**
Extrusion & Moulding	183.6	183.6	177.4	-3.4%
Fabrication & Distribution	114.7	109.2	103.7	-5.0%
Group underlying operating profit	22.3	24.2	18.7	**-22.7%**
Extrusion & Moulding	21.5	21.5	17.5	-18.6%
Fabrication & Distribution	2.4	4.3	2.9	-32.6%
Group costs	(1.6)	(1.6)	(1.7)	

Source: Epwin, Edison Investment Research. Note: 2017 was restated (R) at the end of FY18 for discontinued operations (ie the Northampton-based glass-sealed unit operations). H118 was presented before the disposal and, as the numbers were not comparable, we have not shown an H1/H2 split.

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.*

Headline revenue and operating profitability fell by c 3% and c 19%, respectively, in FY18. The annualised effect of client status changes[1] in FY17 collectively more than accounted for the year-on-year reductions in revenue and profitability (c £16.7m and c £4.9m attributed, respectively). Adjusting for this suggests underlying revenue growth of c 6% with EBIT up c 5%; price and sales volume increases were the main positive contributors to this underlying performance and input cost inflation (only partly covered in the period by price increases) constrained further profit growth.

Window systems – just under half of divisional revenues – grew strongly (+11% overall including +16% for the relatively new Profile 22 Optima range); we believe that this would have been driven by annualised effects of new Optima fabricators added in FY17, new ones secured during FY18 and higher prices. In other product groups, **roofline** was most affected by the SIG/Entu changes but ongoing volumes grew modestly otherwise, while **rainwater/drainage** goods and Stormking's **GRP moulding** products both rose by c 6%, reflecting exposure to the newbuild housing sector. **Decking** product volumes rose modestly also.

The divisional footprint underwent further consolidation in FY18 with the relocation of extrusion lines from Macclesfield to other group sites, which was completed by the end of the year. The proposed construction of a new warehouse facility at Telford – commencing in H219, completing Q120 – would represent the final phase of major consolidation activity in this division in our view. This would accommodate four smaller satellite facilities and leave Telford, Tamworth and Scunthorpe as the core extrusion sites focused on specific profile market and segments giving rise to operational efficiencies and capacity to grow.

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[1] August 2017: Sale of SIG's plastic building products branches to competitor GAP, Entu enters administration. March 2018: Acquisition of Amicus – becomes an internal group customer and moves external sales to F&D on consolidation.

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 and third-party finished products.*

As shown in Exhibit 1, reported revenue (-5%) and EBIT (c -33%) declined in FY18. Sales volumes and price increases both made modest positive underlying contributions to FY18 performance. The bigger influences were structural in nature, being:

- the prior year administration of customer Entu (as in E&M, but a bigger negative impact here including Epwin's sale of its Indigo Products subsidiary at the end of FY17);
- closure of the Cardiff window fabrication facility (during H2); and
- acquisition of Amicus Building Products (in March).

Excluding Amicus, like-for-like revenues were down 18% for the ongoing businesses and in the order of 30% for operating profit. (Note that glass sealed unit operations, which were previously reported in this division, were sold in January 2019 and classified as discontinued, hence not included in the above figures.)

We estimate that Distribution activities now represent around two-thirds of annualised sales in this division and Fabrication the remaining one-third. For the ongoing businesses, the former grew sales by c 5% in FY18, while the Fabrication top line (including the Cardiff and Indigo effects) declined by c 30%. There are now 83 distribution branches (including 15 with Amicus) carrying a range of plastic building products. Epwin has retained independent branding for the clusters of branches that it has brought into the group over time, but there is evidence of increasing commonality in lines carried and we expect ranges and administrative support platforms to evolve jointly. After restructuring and disposals, Epwin now has just three fabrication facilities: at Telford (Wrekin Windows), Paignton (Sierra Windows) and Upton-on-Severn (Safedoor/Permadoor). Since the year end, Epwin has acquired PVS, a decking installation business located in the east of England with a range of public and private sector customers. Potential synergies here include product supply from other group companies and expanding the installer base into other parts of the country from its current base.

Stable net debt position currently, reducing by end FY21

Year-end net debt stood at c £25m, marginally down from a year earlier. Free cash flow (FCF) of c £9m and, as the Amicus acquisition was cash neutral (ie net of cash acquired with the business), after the reduced cash dividend payout (at £8.8m), there was a small net cash inflow overall for the year.

EBITDA declined by c £5m y-o-y to £27m, but this was more than compensated for by an improved working capital performance, from an outflow of £7m in the prior year to a c £5m inflow in FY18. Inventory reduction inflows were achieved at the half-year stage and substantially retained at the year end. For the year overall, there was a modest receivables inflow (generated in H2, possibly from lower year-end activity levels) and a stronger positive payables effect. Non-trading outflows relating to restructuring and discontinued activities were comparable in both years at £6–7m. As a result, FY18 operating cash inflow (after all discontinued cash effects) was c £26m.

The other notable cash flow item was a step-up in capex in the year to £12.5m in total, of which £12m related to tangible fixed assets. The largest component of the c £7m increase arose from site moves (essentially consolidating Macclesfield equipment into the Telford and Scunthorpe facilities) at a cost approaching £4m. There was also spend of below £1m relating to a new aluminium profile window system, which is expected to be launched shortly. The base, maintenance level of capex has risen gradually over the last four years to £4.5m in FY18; this and the total capex spend compares to the £8.3m depreciation charge in the year.

Cash flow outlook: We expect a neutral cash flow performance in FY19, with a small FCF increase applied to acquisitions (c £2.8m covering PVS and a small deferred payment for Amicus) and the rebased dividend (£7.0m). Thereafter, we expect FCF to rise to c £13m and c £16m in FY20 and FY21, respectively, covering cash dividend payments by around 2x. Consequently, there is a meaningful reduction in our projected net debt by the end of FY21 as currently modelled. The new warehouse facility in Telford is expected to start construction in H2 with completion in early FY20 and is likely to be leased by the company.

Estimates now include PVS acquisition

Management is not flagging any material changes in market conditions, although reported an encouraging start to FY19 supported by recovery of input cost increases, core volume growth (unquantified) and some benefits from the reshaped manufacturing footprint starting to come through. New decking and window system products in FY19 are positive markers of renewed outward focus in our view, following a period of internal restructuring.

Our earnings estimates are broadly unchanged overall. In underlying terms, our revenue expectations have been adjusted downwards slightly from the FY18 base level and we have made small margin changes in the two divisions (E&M lower, F&D higher). The resulting small net reduction is matched by our expected PVS EBIT contribution in FY19. Hence the mild downward PBT movement for this year is effectively an interest cost effect. In FY20, PVS moves our estimates marginally ahead (versus our prior estimate).

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.
FY18	9.7	9.8	0.5	17.0	16.5	-2.9	27.2	27.0	-0.7
FY19e	10.2	10.1	-1.8	17.9	17.6	-1.7	28.2	28.2	---
FY20e	10.6	10.7	0.7	18.6	18.7	0.8	28.9	29.5	+1.9
FY21e	N/A	11.1	N/A	N/A	19.4	N/A	N/A	30.3	N/A

Source: Edison Investment Research. Note: 2018 old = estimate, new = actual.

Exhibit 3: Financial summary

£m	2013	2014	2015	2016	2017	2017	2018	2019e	2020e	2021e
Year end 31 December	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						**Restated**				
Revenue	255.3	259.5	256.0	293.2	298.3	292.8	281.1	291.3	296.2	300.9
Cost of Sales	(185.8)	(186.7)	(178.6)	(200.6)	(207.5)	(201.5)	(196.4)	(203.3)	(206.8)	(210.0)
Gross Profit	69.5	72.8	77.4	92.6	90.8	91.3	84.8	88.0	89.5	90.9
EBITDA	21.4	24.5	25.6	33.3	30.3	32.1	27.0	28.2	29.5	30.3
Operating Profit (before GW and except.)	15.6	19.5	20.1	25.6	22.3	24.2	18.7	19.7	20.7	21.3
Intangible Amortisation	(1.7)	(1.7)	(0.0)	(1.1)	(1.1)	(1.1)	(1.2)	(0.5)	(0.5)	(0.5)
Exceptionals	(5.1)	2.3	(0.6)	(0.2)	(7.4)	(7.4)	(2.0)	0.0	0.0	0.0
Other	0.0	(0.8)	(0.4)	(0.3)	(0.6)	(0.6)	(0.7)	(0.7)	(0.7)	(0.7)
Operating Profit	8.8	19.3	19.1	24.0	13.2	15.1	14.8	18.5	19.5	20.1
Net Interest	(1.0)	(0.7)	(0.5)	(1.0)	(1.2)	(1.2)	(1.5)	(1.4)	(1.3)	(1.2)
Profit Before Tax (norm)	14.6	18.0	19.2	24.3	20.5	22.4	16.5	17.6	18.7	19.4
Profit Before Tax (FRS 3)	7.9	18.6	18.6	23.0	12.0	13.9	13.3	17.1	18.2	18.9
Tax	(1.3)	(3.5)	(3.3)	(3.4)	(1.9)	(2.3)	(2.5)	(3.2)	(3.4)	(3.5)
Profit After Tax (norm)	12.4	14.4	15.9	20.9	17.6	19.1	14.0	14.4	15.3	15.9
Profit After Tax (FRS 3)	5.1	15.1	15.3	19.6	10.1	11.6	10.8	13.9	14.8	15.4
Average Number of Shares Outstanding (m)	122.3	128.0	135.2	141.5	142.6	142.6	142.9	142.9	142.9	142.9
EPS - normalised (p)	10.1	11.2	11.8	14.8	12.4	13.4	9.8	10.1	10.7	11.1
EPS - normalised (p) FD		11.2	11.7	14.7	12.4	13.4	9.8	10.1	10.7	11.1
EPS - FRS 3 (p)	4.2	11.8	11.3	13.8	7.1	7.1	4.1	9.7	10.4	10.8
Dividend per share (p)	0.0	4.2	6.4	6.6	6.7	6.7	4.9	5.0	5.3	5.5
Gross Margin (%)	27.2	28.1	30.2	31.6	30.4	31.2	30.2	30.2	30.2	30.2
EBITDA Margin (%)	8.4	9.4	10.0	11.3	10.2	11.0	9.6	9.7	9.9	10.1
Operating Margin (before GW and except.) (%)	6.1	7.5	7.9	8.7	7.5	8.3	6.7	6.7	7.0	7.1
BALANCE SHEET										
Fixed Assets	54.7	53.8	93.5	108.5	106.2		111.7	113.9	113.6	113.1
Intangible Assets	26.4	24.7	59.7	70.2	69.6		73.7	75.2	74.7	74.2
Tangible Assets	25.1	26.2	33.1	37.9	36.0		37.3	38.0	38.2	38.2
Other	3.2	2.9	0.7	0.4	0.6		0.7	0.7	0.7	0.7
Current Assets	62.1	62.3	87.2	82.6	82.2		75.7	80.9	83.6	89.2
Stocks	21.7	22.4	23.6	28.2	29.6		29.2	32.2	33.3	33.8
Debtors	40.1	37.6	41.5	41.4	45.3		40.4	42.6	44.2	45.2
Cash	0.3	2.3	22.1	13.0	7.3		6.1	6.1	6.1	10.2
Current Liabilities	(54.5)	(49.0)	(68.8)	(79.2)	(79.2)		(69.3)	(74.1)	(68.9)	(66.2)
Creditors	(51.5)	(48.6)	(53.2)	(62.9)	(58.2)		(63.7)	(63.7)	(64.7)	(66.2)
Short term borrowings	(3.0)	(0.4)	(15.6)	(16.3)	(21.0)		(5.6)	(10.4)	(4.2)	0.0
Long Term Liabilities	(25.7)	(4.3)	(31.8)	(21.0)	(15.5)		(28.1)	(23.8)	(23.8)	(23.8)
Long term borrowings	(16.0)	(0.8)	(20.9)	(17.3)	(11.4)		(25.3)	(21.0)	(21.0)	(21.0)
Other long term liabilities	(9.7)	(3.5)	(10.9)	(3.7)	(4.1)		(2.8)	(2.8)	(2.8)	(2.8)
Net Assets	36.6	62.8	80.1	90.9	93.7		90.0	96.9	104.5	112.3
CASH FLOW										
Operating Cash Flow	12.1	19.8	23.8	30.8	19.9	18.1	25.8	23.4	26.8	29.4
Net Interest	(0.9)	(0.7)	(0.5)	(1.0)	(1.0)	(1.0)	(1.3)	(1.4)	(1.3)	(1.2)
Tax	(0.9)	(1.7)	(2.3)	(3.8)	(2.7)	(2.7)	(2.6)	(2.7)	(2.9)	(3.0)
Capex	(4.9)	(5.6)	(9.0)	(12.7)	(7.1)	(5.3)	(12.5)	(9.3)	(9.3)	(9.3)
Acquisitions/disposals	(0.2)	0.0	(20.9)	(10.2)	(3.9)	(3.9)	0.0	(2.8)	0.0	0.0
Financing	0.0	10.0	0.0	0.0	0.0	0.0	(0.0)	0.0	0.0	0.0
Dividends	0.0	(1.9)	(6.7)	(9.1)	(9.5)	(9.5)	(8.8)	(7.0)	(7.2)	(7.6)
Net Cash Flow	5.2	19.9	(15.6)	(6.1)	(4.3)	(4.3)	0.5	0.2	6.2	8.3
Opening net debt/(cash)	23.2	18.7	(1.1)	14.4	20.6	20.6	25.1	24.8	25.3	19.1
HP finance leases initiated	(0.5)	(0.3)	0.4	1.9	(1.4)	(1.4)	(1.1)	(0.7)	0.0	0.0
Other	(0.1)	0.2	(0.3)	(2.1)	1.2	1.2	0.9	(0.0)	(0.0)	0.0
Closing net debt/(cash)	18.6	(1.1)	14.4	20.6	25.1	25.1	24.8	25.3	19.1	10.8

Source: Epwin accounts, Edison Investment Research. Note: FY13 to FY17 EPS benefited in part from recovered tax losses. FY17 restated for discontinued operations.

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