

Low and Bonar

Q3 trading update

Tough conditions persisting in H2

While volume growth is being achieved in several divisions, some of the factors that affected H1 trading – most notably higher input costs – have not receded as quickly as anticipated. Underlying operational improvements are happening but have not been enough to offset these pressures to date. We have lowered FY18 earnings expectations sharply – slowing the rate of net debt reduction a little – with a flat DPS profile now.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
11/16	400.0	29.2	6.0	3.0	6.7	7.5
11/17	446.5	30.7	6.3	3.1	6.3	7.6
11/18e	426.5	18.5	3.9	3.1	10.3	7.6
11/19e	439.3	24.0	5.1	3.1	7.8	7.6

Note: *PBT and EPS (fully diluted) are normalised, excluding amortisation of acquired intangibles and exceptional items. Excludes disposed grass yarns business.

Some H1 trading features continue into H2

We understand that volumes are growing modestly in all three core business units. Polymer costs account for almost two-thirds of COGS (or approaching half of revenue); they have risen further in H2 to date rather than fallen as expected and are +10% ytd. A lagged pass-through, including some competitive market effects, is providing a drag on profitability, as is mix, as seen in H1. We believe mix evolution has been due to relative subsector demand patterns rather than a trading-down effect. Internally, phased efficiency improvement at Coated Technical Textiles is progressing slowly and the Civil Engineering business unit disposal process is underway, although our sense is that neither will be complete by the year-end. More positively, the two largest profit generators (Building & Industrial and Interiors & Transportation) have been relatively resilient, although still affected by higher input costs. Lastly, management's business improvement is gaining traction with both cost and inventory reductions noted.

Year-end earnings momentum key to dividend

EBIT was lower y-o-y in H1 and we now expect this to be the case in H2 also (having been flat in our previous estimates). This c £5.6m adjustment to FY18 PBT estimates (and smaller reductions subsequently) led to a c 24% EPS reduction (followed by c 13% and 5%, respectively). Our end-FY18 net debt projection is now c £133m (down c £5m y-o-y), which represents almost 3.1x trailing EBITDA. As things stand, any dividend increase is very unlikely now in our view – we have moved to a flat payout profile in all three years – and in our view the near-term outlook will depend on earnings momentum at the year-end.

Valuation: NAV discount

The post-Q3 update share price move and earnings reduction for FY18 have been in step, leaving a current year P/E of 10.3x (6.7x EV/EBITDA). Even on our lower estimates, the P/E compresses to 6.4x by FY20 and if this trajectory can be achieved the current dividend payout (yielding 7.6%) could be sustained, but this is not a given. Absent any M&A related write-downs, our end-FY18 NAV is 50p.

General industrials

27 September 2018

Price **40.0p**

Market cap **£132m**

£/€ 1.12

Net debt (£m) at end May 2018 140.3

Shares in issue 330.0m

Free float 99%

Code LWB

Primary exchange LSE

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs (21.0) (22.5) (48.9)

Rel (local) (20.2) (22.0) (50.6)

52-week high/low 82.2p 40.0p

Business description

Low & Bonar produces specialist performance materials for a variety of end-markets by combining polymers with specialty additives and pigments. It reports as four global business units: Building & Industrial (19% of FY17 revenue), Civil Engineering (23%), Coated Technical Textiles (31%), and Interiors & Transportation (27%).

Next events

Year end November

FY18 results 30 January 2019

Analyst

Toby Thorrington +44 (0)20 3077 5721

industrials@edisongroup.com

[Edison profile page](#)

Low and Bonar is a research client of Edison Investment Research Limited

Exhibit 1: Financial summary

£m	2014	2015	2015	2016	2017	2018e	2019e	2020e
Year-end 30 November	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS	IAS19R	IAS19R	Restated IAS19R	IAS19R	IAS19R	IAS19R	IAS19R	IAS19R
Revenue	410.6	395.8	362.1	400.0	446.5	426.5	439.3	450.6
Cost of Sales	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Gross Profit	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
EBITDA	45.6	46.9	46.0	52.8	55.8	43.4	50.8	55.6
Operating Profit (ex SBP)	32.3	33.4	32.5	35.6	36.2	24.0	30.4	35.2
Net Interest	(5.0)	(4.2)	(4.3)	(5.4)	(4.6)	(5.6)	(5.5)	(5.3)
SBP	(0.6)	(0.6)	(0.6)	(0.9)	(0.7)	0.3	(0.7)	(0.7)
Saudi JV	(1.1)	(1.8)	0.0	0.0	0.0	0.0	0.0	0.0
PNFC	(0.4)	(0.2)	(0.2)	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)
Profit Before Tax (company norm)	25.2	26.5	27.4	29.2	30.7	18.5	24.0	29.1
Intangible Amortisation	(5.2)	(4.1)	(4.1)	(4.0)	(3.7)	(2.8)	(2.8)	(2.8)
Exceptionals	(3.3)	(10.1)	(1.9)	0.7	(47)	(22)	0	0
Profit Before Tax (FRS 3)	16.7	12.4	21.4	25.9	(19.7)	(5.9)	21.2	26.3
Tax	(4.9)	(6.3)	(6.2)	(8.2)	2.1	(3.4)	(6.3)	(7.6)
Minorities	(0.3)	(0.5)	(0.5)	(0.6)	(0.6)	(0.6)	(0.6)	(0.6)
Other			(9.0)	(3.2)				
Profit After Tax (norm)	18.3	18.6	19.0	19.9	21.4	13.2	17.3	21.0
Profit After Tax (FRS 3)	11.8	6.1	5.7	13.9	(18.2)	(9.9)	14.3	18.0
Average Number of Shares Outstanding (m)	327.0	328.1	328.1	329.0	329.4	329.8	330.0	330.0
EPS FD- normalised (p)	5.4	5.5	5.8	6.0	6.3	3.9	5.1	6.2
EPS - FRS 3 (p)	3.5	1.7	1.7	5.2	(5.5)	(3.0)	4.3	5.5
Dividend per share (p)	2.7	2.8	2.8	3.0	3.1	3.1	3.1	3.1
Gross Margin (%)								
EBITDA Margin (%)	11.1	11.8	11.8	13.2	12.5	10.2	11.6	12.3
Operating Margin (before amort. and except) (%)	7.9	8.4	8.4	8.9	8.1	5.6	6.9	7.8
BALANCE SHEET								
Fixed Assets	230.2	232.0		261.2	257.0	249.1	248.3	247.5
Intangible Assets	105.8	89.9		104.8	91.7	77.9	76.1	74.3
Tangible Assets	119.3	132.0		150.3	144.5	146.5	147.5	148.5
Investments	5.1	10.1		6.1	20.8	24.7	24.7	24.7
Current Assets	192.0	187.6		202.9	222.4	230.6	239.6	250.5
Stocks	90.9	82.6		97.5	97.3	90.9	91.7	92.0
Debtors	62.8	62.9		63.4	72.3	68.1	69.1	69.9
Other	12.5	8.2		15.7	14.6	14.4	16.1	16.1
Cash	25.8	33.9		26.3	38.2	57.2	62.7	72.5
Current Liabilities	(87.7)	(114.4)		(88.9)	(93.3)	(97.2)	(103.9)	(108.7)
Creditors	(87.7)	(82.9)		(88.8)	(90.6)	(97.2)	(103.9)	(108.7)
Short term borrowings	0.0	(31.5)		(0.1)	(2.7)	0.0	0.0	0.0
Long Term Liabilities	(147.6)	(133.3)		(171.5)	(204.4)	(218.5)	(215.2)	(211.9)
Long term borrowings	(113.8)	(104.5)		(137.2)	(173.9)	(190.5)	(190.5)	(190.5)
Other long term liabilities	(33.8)	(28.7)		(34.3)	(30.5)	(28.0)	(24.7)	(21.4)
Net Assets	186.9	171.9		203.7	181.7	164.0	168.8	177.4
CASH FLOW								
Operating Cash Flow	34.1	35.3		33.9	32.2	45.6	48.4	53.6
Net Interest	(4.5)	(4.5)		(4.9)	(4.4)	(5.6)	(5.5)	(5.3)
Tax	(7.7)	(7.5)		(10.8)	(10.3)	(4.9)	(6.3)	(7.6)
Capex	(20.2)	(33.7)		(22.2)	(34.4)	(23.0)	(21.0)	(21.0)
Acquisitions/disposals	3.0	0.0		21.7	3.8	3.0	0.0	0.0
Financing	0	(1)		(0)	(1)	0	0	0
Dividends	(8.8)	(9.0)		(9.2)	(10.0)	(10.1)	(10.1)	(10.1)
Net Cash Flow	(4.0)	(20.2)		8.4	(23.9)	5.2	5.6	9.7
Opening net debt/(cash)	86.8	88.0		102.1	111.0	138.4	133.3	127.8
HP finance leases initiated	0.0	0.0		0.0	0.0	0.0	0.0	0.0
Other	2.8	6.1		-17.3	-3.5	-0.1	0.0	0.0
Closing net debt/(cash)	88.0	102.1		111.0	138.4	133.3	127.8	118.0

Source: Low and Bonar accounts, Edison Investment Research

Edison is an investment research and advisory company, with offices in North America, Europe, the Middle East and AsiaPac. The heart of Edison is our world-renowned equity research platform and deep multi-sector expertise. At Edison Investment Research, our research is widely read by international investors, advisers and stakeholders. Edison Advisors leverages our core research platform to provide differentiated services including investor relations and strategic consulting. Edison is authorised and regulated by the [Financial Conduct Authority](#). Edison Investment Research (NZ) Limited (Edison NZ) is the New Zealand subsidiary of Edison. Edison NZ is registered on the New Zealand Financial Service Providers Register (FSP number 247505) and is registered to provide wholesale and/or generic financial adviser services only. Edison Investment Research Inc (Edison US) is the US subsidiary of Edison and is regulated by the Securities and Exchange Commission. Edison Investment Research Pty Limited (Edison Aus) [46085869] is the Australian subsidiary of Edison. Edison Germany is a branch entity of Edison Investment Research Limited [4794244]. www.edisongroup.com

DISCLAIMER

Copyright 2018 Edison Investment Research Limited. All rights reserved. This report has been commissioned by Low and Bonar and prepared and issued by Edison for publication globally. All information used in the publication of this report has been compiled from publicly available sources that are believed to be reliable, however we do not guarantee the accuracy or completeness of this report. Opinions contained in this report represent those of the research department of Edison at the time of publication. The securities described in the Investment Research may not be eligible for sale in all jurisdictions or to certain categories of investors. This research is issued in Australia by Edison Investment Research Pty Ltd (Corporate Authorised Representative (1252501) of Myonlineadvisers Pty Ltd (AFSL: 427484)) and any access to it, is intended only for "wholesale clients" within the meaning of the Corporations Act 2001 of Australia. The Investment Research is distributed in the United States by Edison US to major US institutional investors only. Edison US is registered as an investment adviser with the Securities and Exchange Commission. Edison US relies upon the "publishers' exclusion" from the definition of investment adviser under Section 202(a)(11) of the Investment Advisers Act of 1940 and corresponding state securities laws. As such, Edison does not offer or provide personalised advice. We publish information about companies in which we believe our readers may be interested and this information reflects our sincere opinions. The information that we provide or that is derived from our website is not intended to be, and should not be construed in any manner whatsoever as, personalised advice. Also, our website and the information provided by us should not be construed by any subscriber or prospective subscriber as Edison's solicitation to effect, or attempt to effect, any transaction in a security. The research in this document is intended for New Zealand resident professional financial advisers or brokers (for use in their roles as financial advisers or brokers) and habitual investors who are "wholesale clients" for the purpose of the Financial Advisers Act 2008 (FAA) (as described in sections 5(c) (1)(a), (b) and (c) of the FAA). This is not a solicitation or inducement to buy, sell, subscribe, or underwrite any securities mentioned or in the topic of this document. This document is provided for information purposes only and should not be construed as an offer or solicitation for investment in any securities mentioned or in the topic of this document. A marketing communication under FCA Rules, this document has not been prepared in accordance with the legal requirements designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of the dissemination of investment research. Edison has a restrictive policy relating to personal dealing. Edison Group does not conduct any investment business and, accordingly, does not itself hold any positions in the securities mentioned in this report. However, the respective directors, officers, employees and contractors of Edison may have a position in any or related securities mentioned in this report. Edison or its affiliates may perform services or solicit business from any of the companies mentioned in this report. The value of securities mentioned in this report can fall as well as rise and are subject to large and sudden swings. In addition it may be difficult or not possible to buy, sell or obtain accurate information about the value of securities mentioned in this report. Past performance is not necessarily a guide to future performance. Forward-looking information or statements in this report contain information that is based on assumptions, forecasts of future results, estimates of amounts not yet determinable, and therefore involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of their subject matter to be materially different from current expectations. For the purpose of the FAA, the content of this report is of a general nature, is intended as a source of general information only and is not intended to constitute a recommendation or opinion in relation to acquiring or disposing (including refraining from acquiring or disposing) of securities. The distribution of this document is not a "personalised service" and, to the extent that it contains any financial advice, is intended only as a "class service" provided by Edison within the meaning of the FAA (ie without taking into account the particular financial situation or goals of any person). As such, it should not be relied upon in making an investment decision. To the maximum extent permitted by law, Edison, its affiliates and contractors, and their respective directors, officers and employees will not be liable for any loss or damage arising as a result of reliance being placed on any of the information contained in this report and do not guarantee the returns on investments in the products discussed in this publication. FTSE International Limited ("FTSE") © FTSE 2018. "FTSE®" is a trade mark of the London Stock Exchange Group companies and is used by FTSE International Limited under license. All rights in the FTSE indices and/or FTSE ratings vest in FTSE and/or its licensors. Neither FTSE nor its licensors accept any liability for any errors or omissions in the FTSE indices and/or FTSE ratings or underlying data. No further distribution of FTSE Data is permitted without FTSE's express written consent.