

Cohort

Extending a sound interest

Cohort has completed the acquisition of ELAC Nautik from Wartsila for a headline consideration of €11.25m, as previously announced. ELAC extends Cohort's maritime offering and has attractive medium- to long-term prospects. It will make an initial five-month contribution and should be modestly earnings enhancing. More detail should be available with interim results next week, but the lack of a trading comment suggests the ongoing activities remain on track to meet market expectations.

| Year end | Revenue (£m) | PBT* (£m) | EPS* (p) | DPS (p) | P/E (x) | Yield (%) |
|----------|--------------|-----------|----------|---------|---------|-----------|
| 04/19 | 121.2 | 15.9 | 33.6 | 9.1 | 18.2 | 1.5 |
| 04/20 | 131.1 | 17.5 | 37.1 | 10.1 | 16.5 | 1.7 |
| 04/21e | 142.1 | 17.7 | 33.6 | 11.1 | 18.2 | 1.8 |
| 04/22e | 158.9 | 19.4 | 36.3 | 12.2 | 16.8 | 2.0 |

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

ELAC extends maritime offering

Cohort has completed the acquisition of ELAC Nautik of Germany from Wartsila, following German regulatory clearance in November. The headline price of €11.25m is as initially announced in December 2019. The acquired company will change its name to ELAC SONAR and will operate as the sixth standalone division of Cohort. It is a market leader in sonar systems for both naval surface ships and submarines accounting for 80–90% of revenues and complements and extends Cohort's existing maritime presence, notably with SEA. ELAC is export oriented and adds Germany as a domestic market for the group. With almost a century of experience and based in Kiel with around 130 employees, ELAC produces sonars, underwater communications and echo sounders, some of which can be used for commercial applications. It supplies several navies around the globe.

Financially robust with attractive prospects

The headline price does not recognise a substantial cash balance being acquired, which almost offsets the consideration. There will be the usual working capital adjustments but we expect the overall effect on FY21 year-end net debt to be less than £1m, although there is a pension liability of around €9m, which requires modest annual funding of around €0.5m. Trading has been tougher in FY21 partially due to delays caused by the pandemic, and management expect ELAC's revenues in 2020 to fall slightly to €20.7m (2019: €21.4m), generating an EBIT of €1.0m (2019: €1.4m). The order backlog at 31 October 2020 was €26.0m, with c €12.0m for delivery in calendar year 2021. Cohort believes ELAC has attractive medium-term opportunities as it exploits its latest technology developments.

Valuation: Discount to sector peers

We estimate ELAC enhances EPS by c 2% in FY22. However, our EPS estimates fall by 5% in FY21 and 4% in FY22 due to a higher charge to more correctly reflect the EID and Chess minorities. Cohort appears robust in the current challenging economic climate but trades at a c 5% FY22e P/E discount to UK defence peers.

Acquisition of ELAC completed

Aerospace & defence

4 December 2020

Price 611p
Market cap £251m

| | |
|--------------------------------|-------|
| Net debt (£m) at 30 April 2020 | 4.7 |
| Shares in issue | 41.0m |
| Free float | 72% |
| Code | CHRT |
| Primary exchange | AIM |
| Secondary exchange | N/A |

Share price performance



| | | | |
|------------------|-------|--------|------|
| % | 1m | 3m | 12m |
| Abs | 2.5 | (0.7) | 5.7 |
| Rel (local) | (9.2) | (11.2) | 14.3 |
| 52-week high/low | 729p | 432.5p | |

Business description

Cohort is an AIM-listed defence and security company operating across six divisions: MASS (31% of FY20 sales), SEA (24%), MCL (11%), the 80%-owned Portuguese business EID (14%), the 81%-owned Chess Technologies based in the UK (19%), and the newly acquired ELAC SONAR.

Next events

| | |
|--------------|------------------|
| H121 results | 10 December 2020 |
|--------------|------------------|

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Revision to estimates

The revision to FY21 and FY22 estimates to add ELAC SONAR are summarised in the table below. As can be seen, the adjusted PBT is modestly enhanced in FY21 and by 4% in FY22.

Our underlying assumption for the continuing Cohort businesses remains unchanged ahead of H120 results on 10 December 2020, although we have increased the minority charge to correctly reflect Chess and EID stakes. This has led to an overall 5% reduction in our adjusted EPS estimates for FY21 and 4% in FY22.

Exhibit 1: Cohort earning revisions

| Year to April (£m) | 2021e | | | 2022e | | |
|--------------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|
| | Prior | New | % change | Prior | New | % change |
| <u>Revenue</u> | | | | | | |
| MASS | 41.5 | 41.5 | 0.0 | 44.0 | 44.0 | 0.0 |
| SEA | 34.6 | 34.6 | 0.0 | 35.6 | 35.6 | 0.0 |
| MCL | 15.5 | 15.5 | 0.0 | 16.0 | 16.0 | 0.0 |
| EID | 18.6 | 18.6 | 0.0 | 19.5 | 19.5 | 0.0 |
| Chess | 26.9 | 26.9 | 0.0 | 28.8 | 28.8 | 0.0 |
| ELAC SONAR | | 5.0 | | | 15.0 | |
| Intra group sales | 0.0 | 0.0 | | 0.0 | 0.0 | |
| Total group revenue | 137.1 | 142.1 | 3.6 | 143.9 | 158.9 | 10.4 |
| EBITDA | 21.1 | 21.4 | 1.5 | 22.2 | 23.3 | 4.8 |
| <u>Adjusted operating profit</u> | | | | | | |
| MASS | 9.0 | 9.0 | 0.0 | 9.5 | 9.5 | 0.0 |
| SEA | 3.8 | 3.8 | 0.0 | 4.0 | 4.0 | 0.0 |
| MCL | 1.7 | 1.7 | 0.0 | 1.8 | 1.8 | 0.0 |
| EID | 3.2 | 3.2 | 0.0 | 3.4 | 3.4 | 0.0 |
| Chess | 3.8 | 3.8 | | 4.0 | 4.0 | |
| ELAC SONAR | | 0.3 | | | 0.9 | |
| HQ Other and intersegment | (3.0) | (3.0) | 0.0 | (3.0) | (3.0) | 0.0 |
| Adjusted operating profit | 18.5 | 18.8 | 1.3 | 19.7 | 20.6 | 4.6 |
| Adjusted PBT | 17.6 | 17.7 | 0.3 | 18.8 | 19.4 | 3.6 |
| EPS - adjusted continuing (p) | 35.4 | 33.6 | (4.9) | 37.7 | 36.3 | (3.8) |
| DPS (p) | 11.1 | 11.1 | 0.0 | 12.2 | 12.2 | 0.0 |
| Net cash / (debt) | (4.2) | (5.0) | 19.5 | 5.1 | 4.4 | (14.4) |

Source: Edison Investment Research

Exhibit 2: Financial summary

| | £m | 2019 | 2020 | 2021e | 2022e |
|--|----|--------|--------|--------|--------|
| Year end 30 April | | IFRS | IFRS | IFRS | IFRS |
| PROFIT & LOSS | | | | | |
| Revenue | | 121.2 | 131.1 | 142.1 | 158.9 |
| Cost of Sales | | (78.1) | (80.0) | (86.7) | (97.0) |
| Gross Profit | | 43.0 | 51.0 | 55.3 | 61.9 |
| EBITDA | | 17.3 | 20.9 | 21.4 | 23.3 |
| Operating Profit (before amort. and except.) | | 16.2 | 18.2 | 18.8 | 20.6 |
| Intangible Amortisation | | (9.5) | (7.4) | (6.8) | (5.1) |
| Exceptionals | | (0.7) | (0.1) | 0.0 | 0.0 |
| Other | | 0.0 | 0.0 | 0.0 | 0.0 |
| Operating Profit | | 5.9 | 10.7 | 12.0 | 15.5 |
| Net Interest | | (0.3) | (0.8) | (1.1) | (1.1) |
| Profit Before Tax (norm) | | 15.9 | 17.5 | 17.7 | 19.4 |
| Profit Before Tax (FRS 3) | | 5.7 | 10.0 | 10.9 | 14.4 |
| Tax | | (0.6) | (0.3) | (1.9) | (2.7) |
| Profit After Tax (norm) | | 13.3 | 15.2 | 14.8 | 15.9 |
| Profit After Tax (FRS 3) | | 5.1 | 9.7 | 8.9 | 11.7 |
| Average Number of Shares Outstanding (m) | | 40.7 | 40.7 | 40.8 | 40.8 |
| EPS - fully diluted (p) | | 33.4 | 36.7 | 33.3 | 35.9 |
| EPS - normalised (p) | | 33.6 | 37.1 | 33.6 | 36.3 |
| EPS - (IFRS) (p) | | 13.4 | 23.5 | 19.5 | 25.8 |
| Dividend per share (p) | | 9.1 | 10.1 | 11.1 | 12.2 |
| Gross Margin (%) | | 35.5 | 38.9 | 38.9 | 38.9 |
| EBITDA Margin (%) | | 14.3 | 15.9 | 15.0 | 14.7 |
| Operating Margin (before GW and except.) (%) | | 13.3 | 13.9 | 13.2 | 12.9 |
| BALANCE SHEET | | | | | |
| Fixed Assets | | 72.9 | 74.3 | 78.3 | 74.6 |
| Intangible Assets | | 61.9 | 55.3 | 54.0 | 49.0 |
| Tangible Assets | | 11.0 | 12.1 | 16.4 | 17.7 |
| Right of Use assets | | | 6.9 | 7.9 | 7.9 |
| Investments | | 0.0 | 0.0 | 0.0 | 0.0 |
| Current Assets | | 75.6 | 80.1 | 107.2 | 102.0 |
| Stocks | | 13.5 | 11.5 | 16.8 | 17.2 |
| Debtors | | 42.7 | 47.1 | 50.4 | 54.8 |
| Cash | | 18.8 | 20.6 | 39.1 | 29.1 |
| Other | | 0.6 | 0.9 | 0.9 | 1.0 |
| Current Liabilities | | (36.2) | (32.8) | (35.7) | (39.4) |
| Creditors | | (36.1) | (32.8) | (35.7) | (39.4) |
| Short term borrowings | | (0.1) | (0.1) | 0.0 | 0.0 |
| Long Term Liabilities | | (35.3) | (39.8) | (63.6) | (44.3) |
| Long term borrowings | | (25.1) | (25.2) | (44.0) | (24.7) |
| Lease liabilities | | | (7.5) | (8.5) | (8.5) |
| Other long term liabilities | | (10.1) | (7.1) | (11.1) | (11.1) |
| Net Assets | | 77.0 | 81.8 | 86.2 | 92.9 |
| CASH FLOW | | | | | |
| Operating Cash Flow | | 11.6 | 13.0 | 15.2 | 21.7 |
| Net Interest | | (0.3) | (0.8) | (1.1) | (1.1) |
| Tax | | (2.7) | (0.6) | (2.8) | (3.5) |
| Capex | | (2.1) | (2.7) | (2.8) | (3.1) |
| Acquisitions/disposals | | (21.0) | (1.2) | (4.5) | 0.0 |
| Financing | | 0.1 | (2.2) | 0.0 | 0.0 |
| Dividends | | (3.5) | (3.9) | (4.2) | (4.7) |
| Other | | 0.0 | 0.0 | 0.0 | 0.0 |
| Net Cash Flow | | (17.8) | 1.7 | (0.3) | 9.3 |
| Opening net debt/(cash) | | (11.3) | 6.4 | 4.7 | 5.0 |
| HP finance leases initiated | | 0.0 | 0.0 | 0.0 | 0.0 |
| Other | | 0.0 | 0.0 | 0.0 | 0.0 |
| Closing net debt/(cash) (excluding leases) | | 6.4 | 4.7 | 5.0 | (4.4) |
| Total financial liabilities | | | 12.2 | 13.5 | 4.1 |

Source: Company reports, Edison Investment Research

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