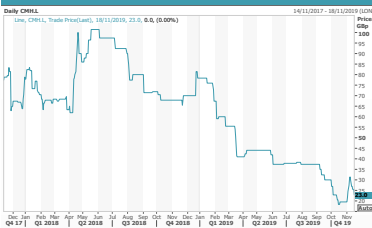




19 November 2019

## Industrial Engineering



Source: Refinitiv

## Market data

EPIC/TKR	CMH
Price (p)	25.0
12m High (p)	97
12m Low (p)	17
Shares (m)	8.3
Mkt Cap (£m)	2.0
EV (£m)	7.4
Free Float*	40%
Market	AIM

\*As defined by AIM Rule 26

## Description

Chamberlin is a UK-based industrial engineering company operating in two divisions – Foundries and Engineering. Around 75% of sales are exported.

## Company information

CEO	Kevin Nolan
CFO	Neil Davies
Chairman	Keith Butler-Wheelhouse
	+44 1922 707100
	<a href="http://www.chamberlin.co.uk">www.chamberlin.co.uk</a>

## Key shareholders

Rights & Issues IT	12.5%
Miton Capital Partners	12.5%
Janus Henderson	9.9%
Chelverton	6.3%
Thornbridge IM	6.3%
Schroders	4.4%

## Diary

Jun'20	Final results
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## Analyst

Paul Singer	020 7194 7622
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## CHAMBERLIN

## Management actions yield cautious optimism

Trading remains difficult, and cost reduction measures continue to be implemented. Chamberlin is still on track strategically, and the group continues to develop its product offering most favourably. The group has been financially de-risked, and the shares remain attractively valued against the peer group on most methodologies, in our view.

- ▶ **Trading outlook:** Trading in the second half will reflect new customer orders, as well as initiatives and the actions taken to restructure the cost base. The combination of higher revenues and a significantly lower cost base is expected to give rise to second-half operating margins of ca.3%.
- ▶ **Business developments most positive:** Management's ongoing negotiations with customers include higher volumes from existing automotive customers, including increased utilisation of machining capacity, a new contract for non-automotive light castings and general selling price increases, on average, of ca.5%.
- ▶ **Financial forecasts:** We have further adjusted our 2019/20 forecasts to reflect the continued challenging operating environment and the company's view that results will move from the positive side of breakeven at the interim stage to a small loss for the year.
- ▶ **Risks:** Potential risks include developments with the automotive industry, Brexit uncertainties, foreign currency and raw material price fluctuations. From a financial standpoint, the group has been significantly de-risked, with the Exidor disposal proceeds used to reduce the pension scheme deficit and pay down debt.
- ▶ **Investment summary:** The shares offer the opportunity to invest in a cyclical stock with good operational leverage and a valuation that we consider attractive compared with the peer group, but they are likely to tread water until significantly brighter prospects become more evident.

## Financial summary and valuation

Year-end Mar (£m)	2018	2019	2020E	2021E
Sales	30.2	33.0	28.2	29.1
Gross profit	4.7	3.8	3.1	3.9
EBITDA	1.2	0.9	0.5	1.5
Underlying EBIT	-0.3	-0.9	-0.5	0.5
Underlying PBT	-0.7	-1.3	-0.6	0.4
Underlying EPS (p)	-12.3	-16.6	-5.8	4.0
Net (debt)/cash*	-8.9	-5.4	-4.6	-4.4
P/E (x)	-	-	-	6.2
EV/sales (x)	0.3	0.3	0.3	0.3

\*Net debt after cash position; Source: Hardman &amp; Co Research

## Current business developments

### *Trading conditions remained challenging*

Trading conditions have remained challenging for all business areas. Customer schedules for the European turbocharger market have suffered significant reductions, and there are continuing uncertainties relating to Brexit. The Scunthorpe Foundry was affected by a general industry slowdown, including the British Steel administration. The Petrel business (Lighting and Control equipment to, primarily, the oil and gas sector) has also experienced difficult trading.

### **Management actions undertaken and have enhanced outlook**

Management, consequently, has reassessed revenue expectations, and has made substantial adjustments to the cost base. Principally, compared with the beginning of the calendar year, the headcount has reduced by 28%, with up to 40% cuts in some areas.

### **New customer orders**

In addition, management's ongoing negotiations with customers have been most positive, resulting in increased revenue expectations. These include higher volumes from existing automotive customers – including increased utilisation of machining capacity, a new contract for non-automotive light castings and general selling price increases, on average, of ca.5%. Furthermore, a new customer for heavy castings, with potentially large volumes, has been secured, and new products have been launched at Petrel.

# Financials

## Profit and Loss

- ▶ 2019/20 interim results were below our forecasts, with revenues from continuing operations down 9.3% to £12.8m. Gross profit was £0.9m, with margins at 7.5% and an underlying operating loss before tax of £0.9m. This reflected the continued deterioration in performance of the principal foundry operations.
- ▶ Our 2019/20 full-year forecasts have been adjusted to reflect the current tough, but improving, trading conditions. Revenues are set to decline by around 15%, on our estimates, but we forecast gross margins to increase from 11.4% to 12% in 2019/20, with administrative costs also remaining under control.
- ▶ Our 2019/20 forecasts reflect management's view that, excluding the restructuring cost of £0.7m, results will move from the positive side of breakeven at the interim stage to a small loss for the year.

Profit & Loss				
Year-end Mar (£m)	2018	2019	2020E	2021E
<b>Sales</b>	<b>30.15</b>	<b>32.96</b>	<b>28.20</b>	<b>29.12</b>
COGS	-25.48	-29.19	-25.09	-25.19
<b>Gross profit</b>	<b>4.68</b>	<b>3.77</b>	<b>3.10</b>	<b>3.93</b>
<b>Gross margin</b>	<b>15.5%</b>	<b>11.4%</b>	<b>11.0%</b>	<b>13.5%</b>
Sales & marketing	-0.50	-0.05	-0.05	-0.06
Administrative expenses	-4.50	-3.74	-3.55	-3.37
<b>EBITDA</b>	<b>1.18</b>	<b>0.89</b>	<b>0.50</b>	<b>1.50</b>
<b>EBITDA margin</b>	<b>3.9%</b>	<b>2.7%</b>	<b>1.8%</b>	<b>5.2%</b>
Depreciation & amortisation	-1.50	-1.77	-1.00	-1.00
Licensing/Royalties	0.00	0.00	0.00	0.00
Other income	0.00	0.00	0.00	0.00
<b>Underlying EBIT</b>	<b>-0.32</b>	<b>-0.88</b>	<b>-0.50</b>	<b>0.50</b>
Share-based costs	0.00	0.00	0.00	0.00
Exceptional items	0.00	0.00	-0.68	0.00
<b>Statutory operating profit</b>	<b>-0.32</b>	<b>-0.88</b>	<b>-1.18</b>	<b>0.50</b>
Net financials	-0.35	-0.38	-0.09	-0.09
<b>Underlying PBT</b>	<b>-0.66</b>	<b>-1.27</b>	<b>-0.59</b>	<b>0.41</b>
Reported PBT	-1.11	1.59	-1.27	0.41
Tax payable/receivable	-0.24	-0.06	0.11	-0.07
<b>Underlying net income</b>	<b>-0.99</b>	<b>-1.33</b>	<b>-0.49</b>	<b>0.34</b>
Statutory net income	-1.35	1.53	-1.17	0.34
<b>Underlying basic EPS (p)</b>	<b>-12.3</b>	<b>-16.6</b>	<b>-5.8</b>	<b>4.0</b>
Statutory basic EPS (p)	-16.9	19.1	-13.9	4.0
<b>Underlying fully-dil. EPS (p)</b>	<b>-12.3</b>	<b>-16.6</b>	<b>-5.8</b>	<b>4.0</b>
Statutory fully-dil. EPS (p)	-16.9	19.1	-13.9	4.0
<b>DPS (p)</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

Source: Hardman & Co Research

## Balance sheet

- ▶ The group had a net debt position at 30 September 2019 of £6.1m, compared with £5.4m at 31 March 2019.
- ▶ The group's defined pension scheme at 30 September 2019 was in a £2.8m deficit (£2.6m at 31 March 2019); the increase in the deficit since March 2019 is due mainly to a rise in the value of liabilities as a consequence of a reduction in bond yields lowering the discount rate.
- ▶ We forecast net debt (including cash) of around £4.6m at the end of 2019/20.

Balance sheet				
@ 31 Mar (£m)	2018	2019	2020E	2021E
Shareholders' funds	3.2	4.9	3.7	4.0
Cumulated goodwill	0.0	0.0	0.0	0.0
Total equity	3.2	4.9	3.7	4.0
Share capital	2.0	2.0	2.0	2.0
Reserves	1.2	2.9	1.7	2.0
Provisions/liabilities	5.3	2.8	2.8	2.8
Deferred tax	-1.5	-0.9	-0.8	-0.8
Long-term debt	1.9	3.0	3.0	3.0
Short-term loans	7.0	2.7	2.0	1.7
less: Cash	0.0	0.3	0.3	0.3
less: Marketable secs.	0.0	0.0	0.0	0.0
<b>Invested capital</b>	<b>15.8</b>	<b>11.2</b>	<b>10.3</b>	<b>10.4</b>
Fixed assets	11.7	7.8	7.6	7.4
Intangible assets	0.4	0.3	0.3	0.3
Goodwill	0.0	0.0	0.0	0.0
Inventories	3.6	2.7	2.4	2.7
Trade debtors	8.0	6.1	5.4	5.8
Other debtors	0.0	0.0	0.0	0.0
Tax credit/liability	0.0	0.0	0.0	0.0
Trade creditors	-8.0	-4.6	-4.8	-5.1
Other creditors	0.0	-1.0	-0.6	-0.7
Debtors less creditors	0.0	0.5	0.0	0.1
<b>Invested capital</b>	<b>15.7</b>	<b>11.2</b>	<b>10.3</b>	<b>10.4</b>
<b>Net debt</b>	<b>8.9</b>	<b>5.4</b>	<b>4.6</b>	<b>4.4</b>

Source: Hardman & Co Research

## Cashflow

- ▶ Group 2018/19 capital expenditure was £1.2m. For 2019/20, capital expenditure will now be around £0.8m, on our estimates, marginally lower than previous expectations.
- ▶ Working capital management remains well controlled.

<b>Cashflow statement</b>				
<b>Year-end Mar (£m)</b>	<b>2018</b>	<b>2019</b>	<b>2020E</b>	<b>2021E</b>
<b>Trading profit</b>	<b>-0.3</b>	<b>-0.9</b>	<b>-0.5</b>	<b>0.5</b>
Depreciation	1.4	1.8	1.0	1.0
Amortisation	0.1	0.0	0.0	0.0
Working capital	-0.3	-0.6	1.1	-0.4
Other	0.0	7.3	0.0	0.0
<b>Company op. cashflow</b>	<b>0.8</b>	<b>7.6</b>	<b>1.6</b>	<b>1.1</b>
Net interest	0.0	0.0	-0.1	-0.1
Tax paid/received	-0.1	-0.2	0.0	0.0
<b>Operational cashflow</b>	<b>0.7</b>	<b>7.4</b>	<b>1.5</b>	<b>1.0</b>
Capital expenditure	-3.0	-1.2	-0.8	-0.8
Other	0.0	0.0	0.0	0.0
<b>Free cashflow</b>	<b>-2.3</b>	<b>6.3</b>	<b>0.7</b>	<b>0.2</b>
Dividends	0.0	0.0	0.0	0.0
Acquisitions	0.0	0.0	0.0	0.0
Disposals	0.0	0.0	0.0	0.0
Other investments	-1.2	0.0	0.0	0.0
<b>Cashflow after investments</b>	<b>-3.5</b>	<b>6.3</b>	<b>0.7</b>	<b>0.2</b>
Share repurchases	0.0	0.0	0.0	0.0
Share issues	0.0	0.0	0.0	0.0
<b>Change in net debt</b>	<b>-3.5</b>	<b>6.3</b>	<b>0.7</b>	<b>0.2</b>

Source: Hardman & Co Research

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