



14 November 2019

**Market data**

EPIC/TKR	NDT.MI
Price (€)	3.44
12m High (€)	4.50
12m Low (€)	2.66
Shares (m)	13.1
Mkt Cap (€m)	45
EV (€m)	87
Free Float*	36%
Market	Italian AIM

\*As defined by AIM Rule 26

**Description**

Neodecortech is an Italian vertically-integrated paper manufacturer and printer of specialist décor papers for the furniture and flooring industry. 67% of its revenues are generated outside Italy.

**Company information**

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[www.neodecortech.it](http://www.neodecortech.it)**Key shareholders**

Valentini family	64%
Azimet Capital	5%
ARCA Fondi	3%
Mediolanum	3%

**Diary**

Mar'20	Preliminary results
Sep'20	Interim results

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# NEODECORTECH

## Robustly positioned for 2019/20

Neodecortech (NDT) has performed well in 2019, in our view, against a difficult economic backdrop. 1H, 3Q and October revenue rose 2%, 6% and 9%, respectively. We are forecasting the year to end strongly, with full-year revenue up 5% and adjusted EBITDA fractionally ahead, at €19.4m. NDT is planning to move to the Main Market in 1Q'20, and the controlling family has reduced its stake to 64%. NDT trades at a ca.28% EV/EBITDA discount to its nearest peers – a 20%+ narrowing since February this year.

- **Strategy:** NDT uses its vertical integration model to ensure continuity of affordable supply and flexibility in responding to an ever-changing market place. Margin efficiencies are coming through as plant capacity grows, and new designs and products are leveraging the company's Italian design heritage.
- **Trading:** Circumstances are not easy currently, with customers reluctant to commit to orders. NDT is focusing on growing the plastic printed film range used in the production of luxury vinyl flooring tiles. Raw material prices have continued to weaken through 2019, encouraging purchasers to wait for further falls.
- **Valuation:** NDT is trading cheaply on our forecast multiples. At a ca.28% EV/EBITDA discount to its nearest quoted peers, the market is more than adequately discounting for its smaller scale and lack of secondary market liquidity. Our central DCF valuation comes out at €5.27 per share (see page 22).
- **Risks:** The key risk in the immediate term is the economic outlook for the construction business generally, but in western Europe in particular. In addition, raw material price fluctuations and the possibility of more direct competition from Chinese manufacturers are general concerns in the medium term.
- **Investment summary:** NDT specialises in high-quality décor paper and plastic film, and has strong relationships with its customers. It is looking to invest in further improvements in its machinery and new technologies. It listed on the Italian AIM market in September 2017 and is moving to the Main Market in the new year. As familiarity grows and the new products comprise a larger proportion of the business, we would expect the valuation discount to continue to narrow.

**Financial summary and valuation**

Year-end Dec (€m)	2016	2017	2018E	2019E	2020E
Sales	116	128	134	140	147
EBITDA	15.6	15.2	18.0	17.4	19.4
EBIT	9.2	7.9	10.6	9.4	11.2
Net financial costs	-3.3	-2.7	-3.0	-2.7	-2.5
Pre-tax profit	6.0	5.2	7.6	6.7	8.7
Net income	4.5	4.1	6.0	5.3	7.0
Adjusted net income	1.3	4.8	7.3	6.3	7.0
Statutory EPS (€)		0.31	0.46	0.40	0.53
Adjusted EPS (€)		0.36	0.54	0.39	0.51
Shares issued (m)		13	13	13	13
P/E (x)		8.1	6.9	8.9	6.7
EV/EBITDA (x)		5.8	5.0	5.0	4.5

Source: Hardman &amp; Co Research

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# Trading update

## Challenging FY19, NDT outperforming

Hampered by negative external economic environment

Trading in the first half of 2019 was tricky, with the external economic environment being especially unhelpful. Overall, NDT reported revenue up 2%, boosted by the inclusion of the Corbetta acquisition. Organic revenue was down 4%. Within the group, décor paper revenue was up 10% (or -5% ex-Corbetta), paper was down 11% and energy was up 9%.

By comparison, Ahlstrom-Munksjö reported 1H revenue in décor paper down 4%. At Surteco, NDT's other close comparator, revenue in décor paper was down 3% and down 11% in impregnated paper. Ahlstrom-Munksjö has also recently reported 3Q revenue in its décor business down 8%.

In the trading update to the end of October, NDT reported consolidated revenue of €116m, up 4% on the comparable period last year. We estimate that this equates to 3% organic growth in 3Q and 9% in October. We now assume that revenue will grow 8% in the final two months of the year, to arrive at our estimate of €140m for the full year, up 5% on last year.

### Décor paper division

NDT commented that, in its déco paper business, plastic printed film (PPF) sales had also slowed in 1H'19, despite a strong showing in 2H'18. However, it explained that it thought this was due largely to destocking at a key customer, rather than a weakness in the underlying market. It intends to continue to roll out new PPF and PPLF (plastic printed laminated film) products, as that is where it sees the growth to be. It is also broadening the plastic films business into PP (polypropylene) from PVC, which is seen to be a less environmentally-friendly solution.

It noted that it had seen a sharp upswing in this division in the two months after the end of the first half.

### Paper division

The paper division had a tough first half, with sales down 11%, not helped by a weather incident in February that closed production for 22 days. NDT received €1.4m in insurance compensation but incurred some additional manpower costs in restarting the plant.

Lower raw material costs helped margins, but, with the market anticipating further falls, some customers held off ordering.

The division saw strong sales growth in Italy but a significant decline elsewhere in Europe, notably in Turkey.

### Energy division

The energy division generated 14% more power in 1H'19 compared with the previous half, and sold 24% more to the grid, with internal usage down slightly. Power prices were high at the beginning of the year but fell steadily through the period.

Lower prices in 2019 will feed through into higher incentive payments next year. Raw material prices are steady.

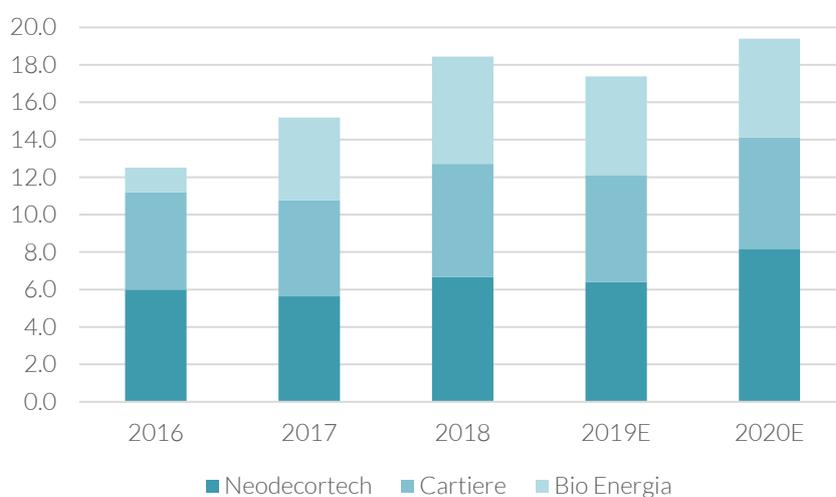
## Profitability

Reported EBITDA for the first half, at €7.1m, was 14% below last year's €8.2m. On an adjusted basis, stripping out share awards and some IPO costs, EBITDA was €8.5m, down only 3% on last year's adjusted €8.7m.

## Financial position

Net debt fell by €4.9m to €48.3m, after NDT invested €3.8m in capex. By the end of October, it had fallen further, to €43.5m, registering an improvement of €8.9m compared with the same period last year.

### Neodecortech: EBITDA by division, 2016-20E (€m)



Source: Neodecortech, Hardman & Co estimates

**Our forecasts for FY19 and FY20 have not changed significantly**

We are forecasting full-year revenue growth of 5%, followed by a further 5% for 2020. Our EBITDA expectation is €17.4m, or €19.4m on an adjusted basis, fractionally ahead of last year. For 2020, we estimate reported EBITDA of €19.4m (€20.4m after adding back a further €1m of share-based payments).

Debt was relatively high, at 76% of equity, at the end of 2018, but we forecast it falling to 67% at the end of FY19 and to around 58% by 2020. The interest cost is well covered by operating cashflow.

In October, NDT sold a subsidiary consisting solely of some life insurance policies. It will receive the €2.5m proceeds in January. It will also save US\$400k of annual cash outflow.

Our forecasts have not changed significantly since our initiation note, published in February (*Innovative décor paper printer*). Broadly, we are now forecasting revenue of €140m (€145m) for FY19 and €147m (€159m) for FY20, and reported EBITDA is down a similar amount, on our estimates: €17.4m (€18.9m) for FY19 and €19.4m (€20m) for FY20.

## Risks

We identify four risks, in addition to normal business risks:

- ▶ The business is inevitably sensitive to the economic cycle and the construction sector in particular.
- ▶ Any sharp slowdown will make our forecasts difficult to achieve. Rises in raw material prices cannot be passed on straightaway, and so can cause a delay in profitability.
- ▶ The Chinese are large players in this sector, although currently are largely confined to their domestic market and to lower-quality products – any change in these two factors could provide additional competition for NDT.
- ▶ Shareholders should remember that they are a minority in the company, with the Valentini family now controlling 64% of the company. The Valentini family sold 1.2m shares in October, at €3.40, and the percentage holding should come down further over time, as NDT looks to issue equity to invest in growth in the business.

## Valuation

Our central DCF valuation comes out at  
€5.27 per share

NDT trades at a significant discount to its two most closely-related listed peers – Ahlstrom-Munksjö (Finland) and Surteco (Germany) – although both are on a recovery track, after lower profits in 2018. At the current price, NDT is trading at a 29% EV/EBITDA discount to the average of its two peers for FY19 and at 27% for FY20.

Our central DCF valuation of €5.27 per share would put NDT on 10% and 7% discounts to the average EV/EBITDA multiples for 2019 and 2020, respectively – justified, we believe, by NDT's smaller scale.

### *Move to Main Market*

We would expect liquidity in NDT to improve following the reduction in the Valentini family stake and the intended move to the MTA<sup>1</sup> of the Borsa Italiana, possibly the STAR segment. It is expected that the move will be completed in the first half of March 2020.

STAR is the market segment of MTA dedicated to mid-size companies with a capitalisation of less than €1bn, which voluntarily adhere to and comply with the following strict requirements:

- ▶ high transparency and high disclosure requirements;
- ▶ high liquidity (free float of minimum 35%); and
- ▶ corporate governance in line with international standards (i.e. a set of rules that determine the company's management).

<sup>1</sup> Mercato Telematico Azionario

## Specialty paper business

### Operates under three sites

NDT is a vertically-integrated business from power generation through to paper manufacturing, through to printing and impregnating paper. It specialises in high-quality printed décor paper and film in natural patterns to sell to the interior decoration industry, including furniture and flooring manufacturers.

### The largest décor paper printer in Italy...

Formed out of businesses from the Valentini Group, it is now a focused business growing in efficiency, and developing new products and new markets worldwide. The business is inevitably linked to the property and construction cycle but is generally more exposed to refurbishment than new build, which is a more subdued cycle. With three quarters of its revenues generated outside its domestic Italian market, it has a wide spread of clients.

The vertical integration of the business provides security of supply and competitively-priced power. It also assists the company in staying fashionable, and responding flexibly to an ever-changing market place. Both the paper manufacturing business and the power generation unit also sell into the wider market – so they need to perform efficiently.

### ...competing with larger competitors in other countries on quality of product and wide range

The décor paper market is a small part of the speciality paper market, which itself is a small part of the global paper and packaging market. NDT is the largest décor paper printer in Italy, but it is a fraction of the size of its largest competitors, which are largely private German companies. It competes on the quality of the product and its wide range. It has over 900 patterns in its catalogue, and is constantly adding new ones. It has also developed a laminated film based on PVC (with polypropylene and polyethylene on the way) to sell into the luxury vinyl tile (LVT) market.

The capital intensity of the business is a substantial barrier to entry. The reconstruction of the assets of the business would cost three times the net book value. This is a substantial deterrent to any new entrants into the market.

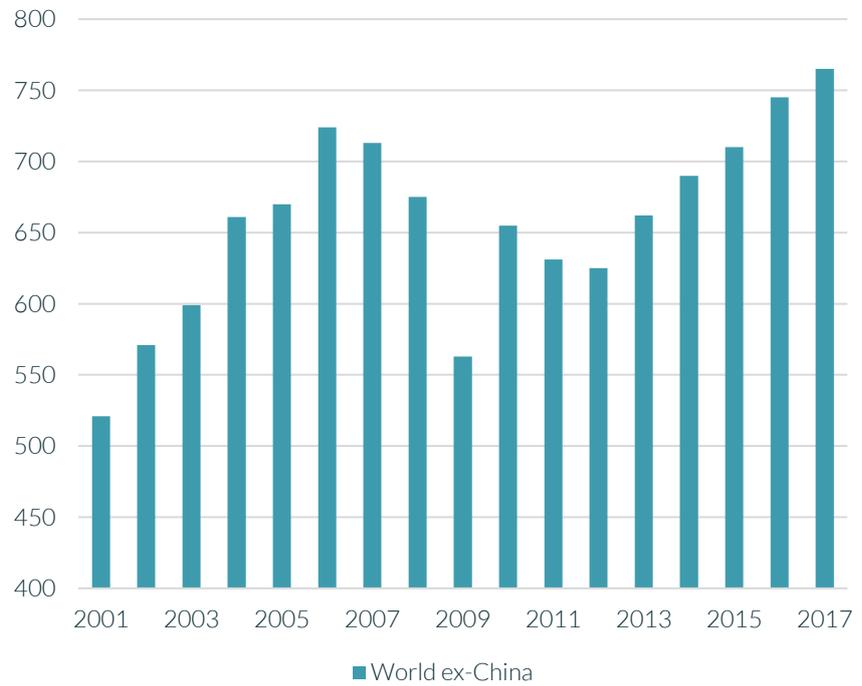
## The paper market

### Both growth and declines in décor paper production over 2001-17

NDT is in a very small, specialist part of the paper market. Approximately 7% of the 400 million ton global paper market, excluding China, is in speciality paper, and the 745,000 ton décor paper market is only a small fraction of that, making it ca.0.2% of the total world market.

Décor paper has seen a classic production cycle: between 2001 and 2006, there was 6.8% annual growth in tonnage; then, in the global slowdown, it saw a decline to the bottom in 2012 of 2.6% p.a.; between 2012 and 2017 (the latest figures we have), it grew again, at 4.5% p.a. It took until 2016 to pass the peak of 2006.

The global (ex-China) décor paper market (tons)



Source: Décor Paper Market Research 2017, Ahlstrom-Munksjö

Outside China, market dominated by Western Europe and, in particular, Germany

When discussing the décor paper market, it is normal to exclude China. This is partly because it produces much lower-quality paper, and so it is not competing directly with the likes of NDT, and partly because it is so huge (it produces about half of the global total tonnage) – but nearly all of the production is absorbed internally. The only net exporting regions are China and Western Europe.

Outside China, this market is dominated by Western Europe and, in particular, Germany. There is some production in Eastern Europe but very little in the rest of the world.

Different parts of world have different traditions in choice of floor covering

A large percentage of the décor paper market ends up in flooring, and different parts of the world have different traditions when it comes to their choice of floor covering. In most of the Southern Hemisphere and Asia Pacific, ceramic floors completely dominate the market.

In North America, the dominant covering is carpet (as it is in the UK), with only 14% being wood or laminate. In Europe and the former Soviet Union, the coverings are more varied, and wood/laminate makes up a 20%-25% market share.

The laminate flooring market has shown modest growth since 2008, with Asia growing fastest, at 2.0% p.a., and Europe slowest, at 1.3%, leading to overall market growth of 1.6% p.a.

Europe represents approximately 60% of the market, Asia 30% and the Americas just 10%.

Some insulation from global economic downturns

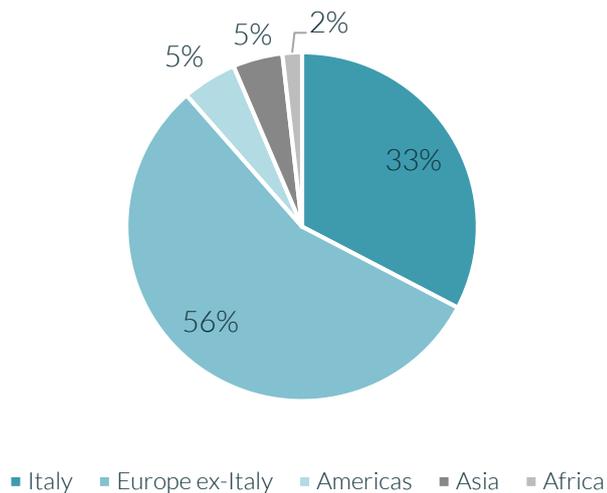
*Economic sensitivity*

Inevitably, the décor paper market is linked to global economic activity – and construction in particular. It is refurbishment that is the key, rather than new build, as floors and furnishings are constantly being replaced. This possibly provides a little insulation from the global economic cycle as, in downturns, there tends to be more focus on refurbishing, rather than new building.

Like the market, NDT is a global business: in 2018, a third of its external sales were within Italy, another half were to the rest of Europe, 5% went to the Americas, 5% to Asia and the balance to Africa. At the 2019 half-way stage, these percentages were little changed.

In the paper division, only Italy saw an improvement in sales, as NDT managed to increase its penetration of the main domestic panel makers. There was a sharp drop in sales to Turkey in the second half, as its economy and currency tumbled. In décor paper, both Italy and Europe increased sales, while the rest of the world contracted. The growth in Italy was driven by a widening customer base and sales of PPF.

Neodecortech: destination of revenues, 2018



Source: Neodecortech

German companies dominate

*Competition*

The competition for NDT is dominated by German companies – most of them privately-owned. Among the top four players in the global décor paper market, there is a Polish company, called (confusingly) Malta Décor, and the other three are German.

The top four companies account for 87% of the revenue of the top nine. NDT's share is just 5%. There are two other, smaller Italian companies. The two largest, like NDT, compete with a very wide range of papers. The smaller players tend to be more specialist.

In printing and impregnating, the picture is very similar. Three of the top four measured by revenue are German, and the fourth is Polish.

Here, the top four account for 78% of the revenue of the top 10 players. NDT has just a 2% market share.

We would expect NDT to be able to grow faster than the market

*Growth prospects*

Such is NDT’s scale that its own individual actions are probably more important than the market as a whole. We would expect the company to be able to grow faster than the market for reasons discussed below: notably, investment in new capacity and efficiency, and the development of new products.

Once a manufacturer has a reliable supplier for such a specialist product, it is not going to change readily

*Client and supplier concentration*

While NDT supplies many different customers, its top 10 account for over half of its sales, and its top five for 38%. We see this as a strength, rather than a weakness. It has genuine partnerships with its customers in developing and supplying new products, tying them in to a symbiotic relationship. Once a manufacturer has a reliable supplier for such a specialist product, it is not going to change readily.

On the supplier side, it makes sense to concentrate its buying power, and the top five suppliers (excluding energy) make up nearly half of all NDT’s inputs; the top 10 account for over 70%.

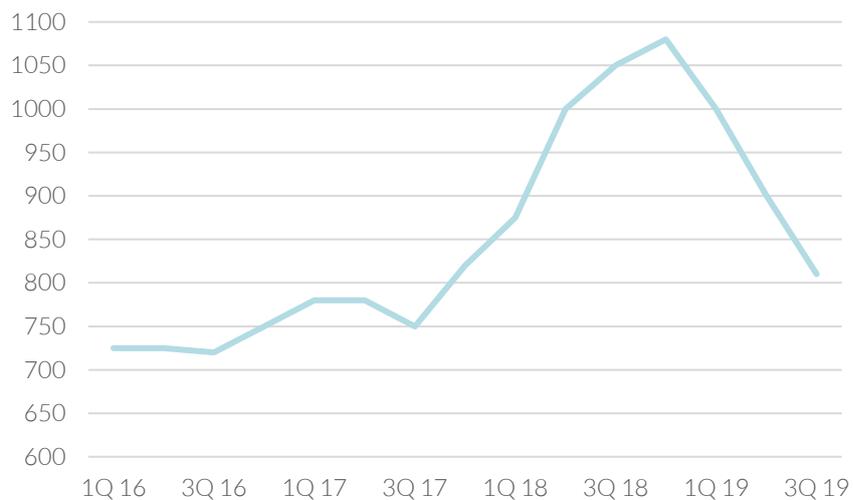
Two key prices for NDT are TiO<sub>2</sub> and pulp

*Raw material prices*

Prices are an important input for NDT. For paper production, the two key prices are titanium dioxide (TiO<sub>2</sub>) and pulp. In 2017, NDT spent €47.5m on raw materials in Cartiere di Guarcino, out of total revenue (before inter-group eliminations) of €66.4m. In other words, 72% of revenue is simply material inputs. Pulp accounted for 24% of revenue and TiO<sub>2</sub> 39%.

Pulp prices, having been reasonably stable in 2015 and 2016, rose steadily in 2017 and throughout 2018 (in Euros). Short fibre prices rose from ca.€630 (all prices per metric ton) at the beginning of 2017 to €830 at the end of 2017 and to ca.€900 in the third and fourth quarters of 2018. Short fibre generally comes from Brazil and Indonesia. Long fibre, on the other hand, is generally sourced from Scandinavia, and rose from €750 to €850 in 2017, before climbing to over €1,000 in 2018, due to poor weather in Northern Europe and strong demand from China.

Long fibre pulp prices (€ per ton)

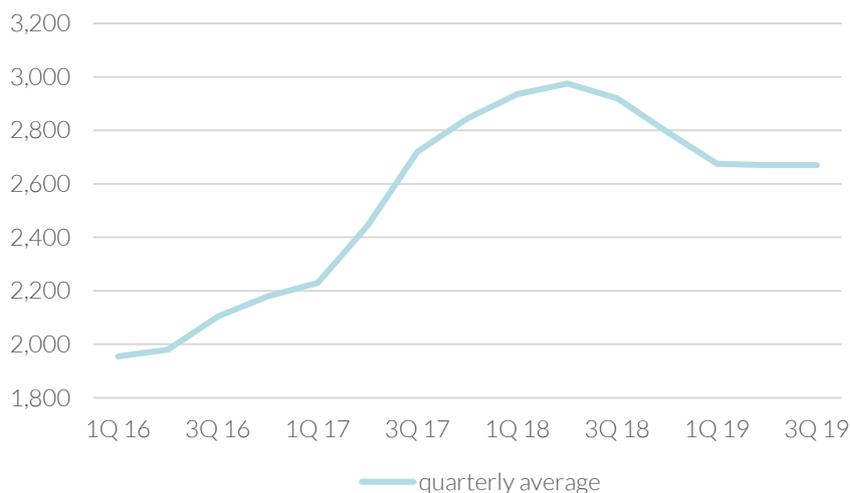


Source: FOEX

In 2019, the long fibre price has fallen right back to around €800 per tonne, due partly to the US/China trade stand-off.

TiO<sub>2</sub> prices followed a similar pattern to prices: they had been falling, but began to rise from a low in the middle of 2016 of €2 per kg to €2.25 at the beginning of 2017, and then to €2.80 by the end of 2017. In 2018, the price peaked at just under €3 in 2Q, before coming off a bit and averaging €2.8 in 4Q. The price fall continued into the beginning of 2019 and, as widely expected, stabilised for the remainder of the year. It remains high relative to historical levels.

#### TiO<sub>2</sub> prices (€ per kg)



Source: ICIS

Raw material costs for impregnating business are around a third of revenues; two-thirds for décor paper business

To some extent, changing raw material prices only impact the timing of profitability. Price increases will be passed on with a lag, and falling prices likewise. All NDT's competitors are impacted in the same way, and there is unlikely to be any product substitution in the short term. Clearly, over the longer term, if prices were to rise disproportionately, this could have a structural impact on the demand for décor paper, but we are not expecting such a shift.

In the tables below, we show the proportion of revenues for the paper business spent on raw materials.

#### Cartiere di Guarcino – raw material cost as % of revenues

	2017	2018
Pulp	21%	21%
TiO <sub>2</sub>	37%	32%
Other	9%	9%
Cartiere di Guarcino	67%	63%

Source: Neodecortech

By the end of the first half of 2018, 90% of the price rises from 2017 had been passed on to NDT's customers. The company chose not to pass on all the price increases, as it had made significant improvements in productivity and it did not want to put unnecessary pressure on its key customers. The impact of the fall in the TiO<sub>2</sub> price is clearly visible, as it fell from 37% of revenues in 2017 to 32% in 2018.

The weaker prices in 2019 saw the pulp percentage fall to 20% in 1H'19 and the TiO<sub>2</sub> percentage to 29%, with raw materials making up 61% of revenues.

For the decorative printing business, the raw material price impact was fairly neutral, with the overall material cost holding steady at 54% of revenues. In 1H'19, this rose to 57%, as the laminates business came on stream.

#### Neodecortech: raw material cost as % of revenues

	2017	2018
Resins	11%	10%
Inks	4%	3%
PVC	4%	4%
Untreated paper	35%	34%
Other	1%	3%
Neodecortech	54%	54%

Source: Hardman & Co Research

#### Power costs

For the power generation business, the picture is not so clear. NDT switched from using palm oil in 2015 to tallow oil. This is much less volatile due to government incentives, which vary in line with the current energy price. Bio Energia Guarcino receives further subsidies if it uses approved, environmentally-friendly animal fats.

With NDT taking slightly less than half of Bio Energia Guarcino's electricity, if the price of electricity rises, the group will benefit from the power sales back to the grid, although this upside will be partly offset by falling incentive payments.

In 2018, Bio Energia produced 27% more power for roughly the same cost of animal fats.

## The businesses

NDT has three businesses: printing and impregnating, décor paper making and power generation.

Most important business is printing and impregnating

### Printing and impregnating (Confalonieri)

The most important of NDT's three businesses is printing and impregnating, based in Filago, Bergamo, about 50km northeast of Milan, trading under the name of Confalonieri. It produces 51 products, divided into four main categories, with over 900 separate designs:

- ▶ decorative printing;
- ▶ finish foil;
- ▶ melamine film; and
- ▶ plastic printed film (PPF) and plastic printed laminate film (PPLF) for luxury vinyl tiles (LVT).

The biggest part – decorative printing – produces high-quality printed papers for wood-based panel manufacturers. The printed papers accurately replicate natural surfaces, such as wood or stone, and are attached to a wood-based panel, such as chipboard or MDF. It is, in effect, a modern artificial veneer, at much lower cost. These are used in the furniture and flooring industries.

Melamine film is printed décor paper impregnated with melamine resin. This gives the surface resistance to scratching or damage from chemical substances spilled on it. This too is sold to furniture and flooring manufacturers.

Finish foil takes the process a step further, and attempts to replicate not only the look of natural materials but also their feel.

The PPF and PPLF for LVT once again produce the look of natural materials but, instead of being printed on a paper, they are printed on a plastic substrate. Originally produced only on PVC, NDT has developed a product based on polypropylene and polyethylene films that are much more environmentally-friendly. The LVTs are used mainly in flooring, but also on some vertical surfaces.

Sales of PPLF would consolidate NDT's position as one of the European leaders in the laminate market

### Laminates

In September 2018, NDT acquired the business division of Corbetta, a company belonging to NDT's controlling shareholder, the Valentini Group. It specialises in laminate production using continuous pressing lamination (CPL) technology. The purchase increases NDT's presence in the LVT market. Corbetta had ca.€8m of sales in FY17 and made a small positive EBITDA margin. In FY18, it made a contribution of €2.6m in revenue and €0.7m in EBITDA. The price, including debt acquired with the business, was approximately €2.5m.

At the lamination production facility, in Casoli di Atri, it is possible to laminate PPF with a transparent plastic film to obtain a composite film that, once embossed and lacquered, produces PPLF. This new product was launched in January 2019 and should allow those producers of flooring, who are not yet fully part of the LVT production chain, to access the designer vinyl flooring market with reinforced high density fibreboard (HDF). Laminate flooring is composed of a wood composite

support material laminated with melamine paper and a transparent impregnated paper film overlay, which provides mechanical resistance to the surface of the product.

NDT has high expectations for the sales of PPLF, as it would consolidate its position as one of the European leaders in this new market segment, which is characterised by both double-digit growth and substantial margins. It is also much “greener” than PVC, which makes it more popular in Germany and Northern Europe generally.

## The process

Investment in R&D important approach to business

An important part of NDT’s approach to business is its investment in R&D. It develops its own products, constantly making new designs, and working closely with its customers. This also helps it to develop new products like PPLF.

As with any design business, fashion is important. NDT attends important international trade fairs, and its Italian heritage is a clear advantage in the design world.

Once the design is finalised, it is translated onto printing cylinders used in the rotogravure process; usually, there are three cylinders per pattern. Each cylinder costs several thousand euros, and NDT has over 3,000 of them. The engraving of the cylinders is one of the few things that NDT does not do in-house. This is a precision process and is necessary to provide the high-image quality needed in decorative printing. The cost of the design and the cylinder means that, to be economical, each run must be either very long or regularly repeated.

NDT uses digital printers for producing new samples or one-off panels.

There are seven printing machines with various capacities and four impregnating lines. It has

annual production capacity of 18,000 metric tons. In 2017, production was 7,750 tons of printed paper and plastic, and 2,550 of impregnated paper – or utilisation of ca.60% capacity. As sales build, improved efficiency should push the operating margins higher.

## Financial metrics

In 2017, this business reported €43.8m of sales, with an EBITDA margin of 12.9%. In 2018, this increased to €50.9m of sales, and EBITDA rose 18% to €6.7m. The increase was driven by a mixture of the contribution from Corbetta (consolidated for four months) and from higher sales, particularly of PPF (up 44%) and the core decorative printing division (+13%).

Confalonieri: revenues, EBITDA and EBIT (2018 vs. 2017, €m)			
	2017	2018	Change
Revenue	43.8	50.9	+16%
EBITDA	5.6	6.7	+18%
EBITDA margin	12.9%	13.1%	+20bps
Depreciation/amortisation	-2.2	-2.4	+9%
EBIT	3.5	4.3	+23%

Source: Neodecortech

NDT reported that its customers in the decorative printing market all experienced a double-digit drop in turnover in the first months of 2019, caused by the uncertain macroeconomic environment. Reported first-half sales were +10% (-8% ex-Corbetta) and EBITDA fell to €2.6m, from €3.6m. 3Q showed some further improvement.

NDT's consistent and successful approach to these difficulties is to focus on the higher- margin growth areas of PPF and PPLF. In the second half of 2019, it has installed or extended production lines in the Filago site: expansion of the impregnation line; extension of the embossing line for PPLF; and installation of a new lacquering line for the production of a new EOS low-pressure product similar to the TITAN (anti-fingerprint) product, which has seen very strong take-up. The first was up and ready in September; the other two will be functioning before the end of the year.

## Décor paper (Cartiere di Guarcino)

### Produces a wide range of décor papers

Cartiere di Guarcino is located in Guarcino, about 100km east of Rome. The company has 171 employees and a production capacity of 50,000 tons per year. Last year, it manufactured 42,000 tons of speciality paper. To put that in context, the two largest European producers of décor paper have capacity of ca.190,000 tons each.

The company manufactures décor papers for high- and low-pressure lamination, as well as for flooring. It makes a wide range of décor papers: print base papers, backer papers, underlay papers, edge banding papers and unicolour papers.

For reporting purposes, the product is split into three categories:

- ▶ base papers;
- ▶ unicolours; and
- ▶ backer papers.

Base papers are what printers like NDT use to produce their natural texture effects. They have a smooth gloss surface, which best suits the rotogravure high-quality printing process.

Unicolours are single colour sheets, which are not glossy, but they are opaque and have low porosity. The papers are used by laminators to produce high- and low-pressure panels.

Backer papers, the smallest part of the business, are more industrial in nature. They are used on the underside of flooring laminates to offset the tendency of the melamine resin layer to shrink as it hardens.

The paper business is, by nature, more of a commodity product, even in the specialist area of décor papers. The EBITDA margins are inevitably thinner, at ca.9%. It is also an energy- and water-intensive business. The company has to be very particular to ensure that the water that flows through its plant comes out no more polluted than when it went in. Problems with the water supply in November 2018 caused two weeks of lost production that year.

### Cartiere di Guarcino: revenues, EBITDA and EBIT (2017 vs. 2018, €m)

	2017	2018	Change
Revenue	67.4	65.4	-3%
EBITDA	5.1	6.1	+18%
EBITDA margin	7.6%	9.3%	+170bps
Depreciation/amortisation	2.0	2.3	+17%
EBIT	3.2	3.8	+19%

Source: Neodecortech

As with Confalonieri, the economic backdrop has not been helpful in 2019, although NDT reported that the first two months were on budget, before a slowdown had a negative impact in March. Many customers delayed ordering in expectation of weaker raw material prices feeding through into lower paper prices. First-half revenues ended down 11%, with EBITDA down 22%, at €2.3m.

Destocking should be largely finished now, so demand is expected to return to normal levels shortly.

### Captive supply from Bio Energia Guarcino critical to paper mill's commercial viability

## Power generation (Bio Energia Guarcino)

Bio Energia Guarcino is a zero CO<sub>2</sub> emission electrical and thermal energy producer that uses three endotherm diesel generators powered by tallow oil. Its production capacity is nine steam tons and 20 MWh. Manufacturing paper is an energy-intense process, and electricity in Italy is very expensive compared with other paper-producing countries – so the captive supply from Bio Energia Guarcino is critical to the paper mill's commercial viability.

The company estimates that owning its own power plant saves it nearly €5m each year, which would be the additional cost of purchasing power from the grid.

In the first half of 2017, the power plant was hit by being out of production for a period. It has operated fully since. In 2018, it produced 140,000 MWh, up 27% on 2017. With lower fuel costs, EBITDA rose 30% to €5.7m. Lower incentives in 2019, due to the higher energy process achieved in 2018, will result, we estimate, in a lower EBITDA contribution in 2019, although, at the halfway stage, EBITDA was up 17%, on revenue up 9%, helped by lower raw material costs.

Energy prices were sharply higher at the beginning of 2019 but the price fell throughout the first half. Consequently, we expect the incentives to rise again in 2020.

## Future developments

NDT has three specific investment plans for the future:

- ▶ The first is a €10m investment in machine improvements. It wants to enhance the output from its paper mill by reducing the variability in weight and size across the paper. It also wants to improve its flatness and printability.
- ▶ Secondly, it wants to invest €15m in geographical expansion – not to move manufacturing overseas but to grow its international sales business. The money would be spent on beefing up the sales force and in buying small local companies that could increase its penetration of international markets. The key target area is Germany. It is also looking to expand into markets such as Turkey, Russia, and North and South America. Acquisitions would be paid for in a mixture of cash and shares.
- ▶ Lastly, it wants to enhance its printing capability. It is looking to invest €10m in digital printing and PPF lamination. On digital printing, it is looking for ways to make small printing batches commercial and expanding its product portfolio.

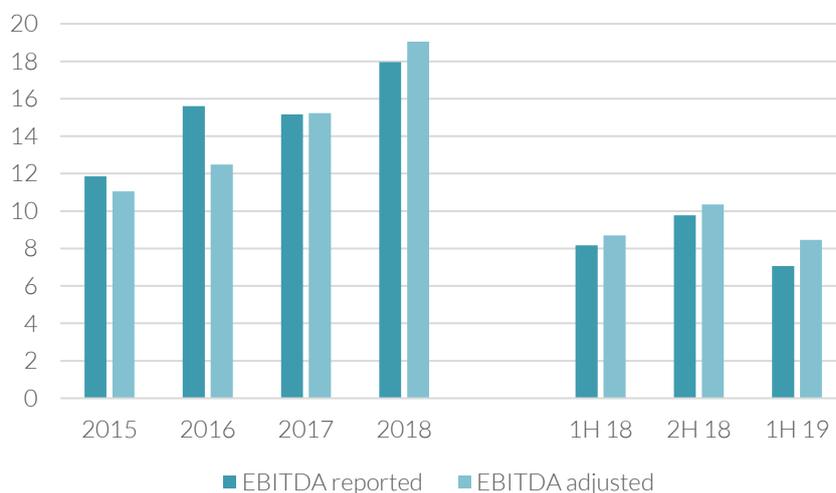
## Financials

NDT is a relatively new listed company, coming to the Italian AIM market in September 2017, and investors have yet to see a full year's set of results

NDT has existed in its current form only since June 2017, when the Confalonieri company acquired the paper mill (Cartiere di Guarcino) and power business (Bio Energia Guarcino), and renamed itself Neodecortech, ahead of its IPO in September 2017. The formal figures for the group therefore only included the paper mill and power plant for six months of 2017. The company prepared pro forma figures for both 2016 and 2017, assuming the group had been in its current form since the beginning of 2016.

Furthermore, there are some adjustments that were made to the EBITDA and net profit figures to give a better representation of the underlying performance of the group.

### Neodecortech: EBITDA, reported and adjusted, 2015-1H'19 (€m)



Source: Hardman & Co Research

The main adjustments in the 2016 financial year included extraordinary income from insurance payments of €2.2m, transactions generating income of €1.9m, exchange rate gains of €0.25m and contingent assets of €0.67m. The extraordinary costs included contingent liabilities of €1.3m, capitalised costs for general services of €0.4m, which were the share of capitalised R&D costs in Cartiere di Guarcino, and higher energy costs of €0.8m.

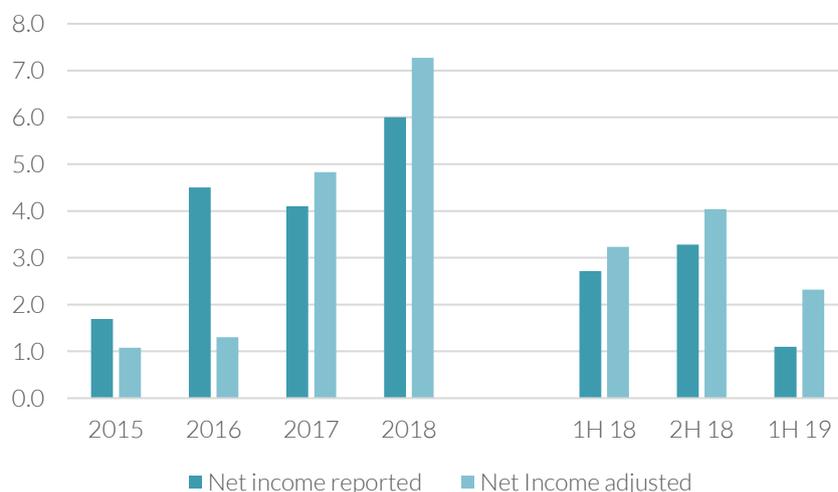
Adjustments for 2017 included a commercial transaction with a supplier that generated income of €0.65m, contingent assets of €0.3m and capitalised costs for general services of €0.4m, which were the share of capitalised R&D costs in Cartiere di Guarcino. Adjustments for extraordinary costs in 2017 included contingent liabilities of €1.2m, redundancy incentives of €0.1m and damages paid to clients of €0.2m.

For 2018, the key adjustments were for the IPO costs and the provision for stock grants. Both these adjustments were repeated in 1H'19, with stock grants costing €1.1m in the period and a further €0.2m of IPO costs.

The same adjustments have an impact on the net income. With the numbers clarified, the progress being made by the company becomes clear, particularly in the half-year numbers. This is a result of the improvement in plant efficiency and the growing scale

of the business. In this respect, 1H'19 has seen a small setback in the progress previously established, against a background of very tough market conditions.

#### Neodecortech: net income, reported and adjusted, 2015-1H'19 (€m)



Source: Hardman & Co Research

## Forecasts

For 2019, we expect revenues in the paper business and Bio Energia Guarmino to be largely flat, as we see challenges from the slowing Italian economy. We expect revenue growth in Confalonieri, with the introduction of new products, to which we add the additional eight months of Corbetta, which were not included in the 2018 comparatives. We hold the EBITDA margin assumption roughly constant in paper, we see a small decline in energy, as the incentives are lower, and we see further organic improvements in déco paper, as it moves further into higher-margin products.

The depreciation and amortisation charge rises to €8m for 2019E, which is also approximately the level of normal capex the company plans to spend on maintaining the plant before the improvements mentioned above.

We assume the tax rate to stay at ca.21%.

NDT's investment plans could not be funded out of internally-generated cash alone. Acquisitions may be paid for with new shares, and the company has the authorisation for a capital increase of up to €10m. It has also issued a free warrant with each share. Four warrants can be converted into one share at a price of €4 per share. Since these are out of the money, they are not included in our EPS calculations.

Divisional forecasts					
Year-end Dec (€m)	2016	2017	2018E	2019E	2020E
Revenue					
Confalonieri		43.8	50.9	57.2	62.9
Cartiere di Guarcino		56.4	50.8	49.3	50.8
Bio Energia Guarcino		23.2	29.2	30.7	30.7
Other		4.2	2.7	2.8	2.6
<b>Total</b>		<b>127.7</b>	<b>133.7</b>	<b>140.0</b>	<b>147.0</b>
Growth					
Confalonieri			16.1%	12.4%	10.0%
Cartiere di Guarcino			-10.0%	-3.0%	3.0%
Bio Energia Guarcino			25.8%	5.0%	0.0%
Other			-36.0%	5.0%	0.0%
<b>Total</b>			<b>4.6%</b>	<b>4.8%</b>	<b>5.0%</b>
EBITDA (adjusted)					
Confalonieri	6.0	5.6	6.7	6.4	8.2
Cartiere di Guarcino	5.2	5.1	6.1	5.7	5.9
Bio Energia Guarcino	1.3	4.4	5.7	5.3	5.3
Other	3.1	0.0	-0.5		
<b>Total</b>	<b>15.6</b>	<b>15.2</b>	<b>18.0</b>	<b>17.4</b>	<b>19.4</b>
adjustment	-3.1	0.1	1.1	2.0	1.0
<b>Adjusted EBITDA</b>	<b>12.5</b>	<b>15.2</b>	<b>19.0</b>	<b>19.4</b>	<b>20.4</b>
EBITDA margin					
Confalonieri		12.9%	13.1%	11.2%	13.0%
Cartiere di Guarcino		7.6%	9.3%	9.0%	9.1%
Bio Energia Guarcino		16.7%	18.3%	16.0%	16.0%
Other					
<b>Total</b>		<b>11.9%</b>	<b>13.4%</b>	<b>12.4%</b>	<b>13.2%</b>

Source: Hardman &amp; Co Research

## Financial statements

Income statement					
Year-end Dec (€m)	2016	2017	2018	2019E	2020E
Revenue	115.6	130.0	133.7	140.0	147.0
Operating costs	-100.0	-114.8	-115.7	-122.6	-127.6
Gross profit	15.6	15.2	18.0	17.4	19.4
Depreciation and amortisation	-6.3	-6.3	-7.2	-8.0	-8.2
Impairment	-0.1	-0.9	0.2	0.0	0.0
EBIT	9.2	7.9	10.6	9.4	11.2
Net financial costs	-3.3	-2.7	-3.0	-2.7	-2.5
Pre-tax profit	6.0	5.2	7.6	6.7	8.7
Tax	-1.5	-1.1	-1.6	-1.4	-1.7
Net income	4.5	4.1	6.0	5.3	7.0
Adjusted net income	1.3	4.8	7.3	6.3	8.0
No. of shares (m)		13.1	13.1	13.1	13.1
No. of shares fully diluted (m)		13.3	13.5	13.6	13.6
Statutory EPS (€)		0.31	0.46	0.40	0.53
Adjusted EPS (€)		0.36	0.54	0.39	0.51
DPS (€)		0.11	0.15	0.12	0.15
Gross profit margin	13.5%	11.7%	13.4%	12.4%	13.2%
EBIT margin	8.0%	6.1%	7.9%	6.7%	7.6%
Tax rate	25%	22%	21%	21%	20%
Revenue growth		12%	3%	5%	5%
EBITDA growth		-3%	18%	-3%	12%
Pre-tax profit growth		-13%	47%	-12%	30%

Source: Hardman & Co Research

Cashflow statement					
Year-end Dec (€m)	2016	2017	2018	2019E	2020E
EBITDA	15.6	15.2	18.0	17.4	19.4
Working capital	1.0	-2.6	0.0	-1.6	-2.9
Capex	-4.6	-7.6	-7.7	-7.5	-8.0
Other	-0.7	-3.1	0.5	0.0	0.0
Operating free cashflow	11.3	1.9	10.7	8.3	8.5
Tax	-1.5	-0.8	-0.3	-1.4	-1.7
Interest	-3.5	-1.8	-1.7	-2.7	-2.5
Dividends	-1.0	-1.0	-2.0	-2.0	-2.0
Equity	1.8	11.4	-0.1		
Debt	2.5	-3.1	-6.2		
Net cashflow	9.6	6.6	0.4	2.2	2.3

Source: Hardman & Co Research

**Balance sheet statement**

<b>@ 31 Dec (€m)</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>	<b>2019E</b>	<b>2020E</b>
Property, plant & equipment	72.8	72.6	76.7	76.0	77.0
Goodwill		1.3	0.0		
Intangible assets	2.0	3.3	3.5	3.5	3.5
Other non-current assets	5.5	3.7	3.9	4.0	4.1
Fixed assets	80.3	80.9	84.0	83.5	84.6
Trade receivables	29.8	26.3	24.1	25.2	27.0
Inventories	26.3	32.1	35.9	37.7	39.9
Other current receivables	4.8	7.8	5.8	6.0	6.5
Cash and equivalents	1.3	6.1	6.5	8.6	10.6
Current assets	62.3	72.3	72.3	77.5	84.1
Total assets	142.5	153.2	156.3	160.9	168.6
Trade payables	-28.0	-33.6	-33.2	-34.8	-36.5
Other payables	-7.6	-3.6	-4.3	-4.0	-4.0
Tax payable	-1.7	-1.2	-1.9	-2.0	-2.0
Debt	-26.0	-22.0	-20.7	-20.7	-20.7
Current liabilities	-63.3	-60.5	-59.9	-61.4	-63.1
Pension provisions	-3.1	-2.9	-2.9	-2.9	-2.9
Other provisions	-0.9	-0.5	-0.5	-0.5	-0.5
Deferred tax liabilities	-3.2	-3.5	-4.3	-4.3	-4.3
Long-term debt	-33.3	-31.8	-30.1	-30.1	-30.1
Non-current liabilities	-40.5	-38.7	-37.7	-37.8	-37.8
Total liabilities	-103.8	-99.2	-97.7	-99.2	-100.9
Net assets	38.7	54.0	58.6	61.8	67.8
Share capital	8.5	16.2	16.2	16.2	16.2
Reserves	30.2	37.8	42.4	45.6	51.5
Total equity	38.7	54.0	58.6	61.8	67.8
Net book value per share (€)		4.12	4.5	4.7	5.2
Net debt	-57.1	-46.9	-44.3	-42.2	-40.2
Debt/equity	148%	87%	76%	68%	59%

Source: Hardman & Co Research

## Valuation

**Simplest valuation methodology is peer comparison...**

The simplest valuation methodology is to compare the valuation of the company with similar listed businesses. In NDT's case, there are similar businesses, but they tend to be substantially larger and, inevitably, while the operations are alike, they are not identical. The two most comparable companies, in our view, are Ahlstrom-Munksjö, listed in Finland, and Surteco, listed in Germany. The former is a producer of speciality paper, but is not a printer, and only ca.16% of its revenue is derived from décor papers. The latter produces decorative foils on paper and plastic. We show their valuation multiples in the table below.

The "Neodecortech @ value" is the valuation at our central DCF value of €5.27 per share, down from €5.84 previously, reflecting our slightly reduced EBITDA forecasts.

### Peer group valuation comparison

Company	Price (€)	Mkt cap (€m)	EV (€m)	EV/EBITDA 2019E (x)	EV/EBITDA 2020E (x)	P/E 2019E (x)	P/E 2020E (x)	Growth 2019/18E	Growth 2020/19E
Neodecortech	3.44	45	87	5.0	4.5	8.9	6.7	-27%	32%
Neodecortech @ value	5.27	69	111	6.4	5.7	13.1	9.9	-27%	32%
Ahlstrom-Munksjö	13.56	1,567	2,558	7.9	6.4	17.2	10.9	44%	58%
Surteco	20.15	310	509	6.2	5.8	13.0	10.6	26%	23%

Source: Hardman & Co Research; based on prices as at 07/11/19

NDT trades at a discount of ca.28% to the average of both peers' EV/EBITDA multiples and even more to P/E multiples. Some of this may be reasonably attributed to the lower liquidity in the shares and the scale of the business generally, and the valuation at our central DCF value looks closer to what may be thought reasonable. Of course, the smaller scale also gives NDT the chance to grow faster, from its ability to move more nimbly.

## DCF

**...while objective form is a DCF**

The objective form of valuation is a discounted cashflow (DCF) calculation. The problems with the DCF method are well documented – most notably the huge sensitivity to both assumed growth rates and the discount rate used. We tend to use a central assumption of 10% cost of equity and value the equity in the business. We also typically use a nominal 3% growth rate for the perpetuity calculation – equivalent to a conservative long-run estimate of nominal GDP growth. For NDT, we have assumed growth in cashflows between 2020 (our last forecast year) and 2025 of 5% for our central case.

### DCF valuation

€m	2018	2019	2020	2021	2022	2023	2024	2025
Revenue	133.7	140.0	147.0	154.3	162.0	170.1	178.6	187.6
EBITDA	18.0	17.4	19.4	20.4	21.4	22.5	23.6	24.8
Working capital	0.0	-1.6	-2.9	-3.0	-3.2	-3.4	-3.5	-3.7
Capex	-7.7	-7.5	-8.0	-8.4	-8.8	-9.3	-9.7	-10.2
Tax	-0.3	-1.4	-1.7	-1.8	-1.9	-2.0	-2.1	-2.2
Net cashflow	10.0	6.9	6.8	7.1	7.5	7.8	8.2	8.6
Discount factor	10%		1.1	1.2	1.3	1.4	1.6	1.7
Discounted cashflow			6.4	6.1	5.8	5.5	5.3	5.0

Source: Hardman & Co Research

### DCF summation

Value components	€m
2020-25E	34.1
2026E onwards	74.2
Total	108.3
less net debt end-2019E	-39.3
Equity value	69.0
Equity value per share (€)	5.27

Source: Hardman & Co Research

#### Our central DCF valuation is €5.27

NDT has announced that it has sold a dormant subsidiary whose sole asset was a collection of life insurance policies. It was sold for its €2.5m book value. The proceeds will be received in the new year. Here we have subtracted €2.5m from our forecast year-end net debt.

Our forecast range of values, based on the DCF methodology, gives a value of €2.98 to €9.03 per share, with a central value, at a 5% mid-term growth rate and using our 10% discount rate, of €5.27.

### DCF sensitivity table

Discount rate/mid-term growth	3%	4%	5%	6%
8%	7.61	8.07	8.54	9.03
10%	4.63	4.94	5.27	5.60
12%	2.98	3.21	3.45	3.69

Source: Hardman & Co Research

Lastly, it is worth noting that our estimated 2018 book value of the company equates to €4.73 per share and that the replacement cost of the assets is substantially higher.

## Risks

The four key risks, other than usual business risks, that we see for NDT are the economic cycle, raw material prices, the competition from China and the minority shareholding position.

- ▶ The company is clearly exposed to the economic cycle and, if there is a marked downturn, especially affecting the construction sector, then our forecasts are unlikely to be met. NDT's debt is well-structured, and there should be no problem servicing it in any short-lived recession, in our view.
- ▶ Raw material prices, as previously noted, should only have a timing issue on profitability, as the price moves get passed on – in both directions. However, if there were a sustained increase in prices, then the products NDT produces might be subject to substitution.
- ▶ China is a big producer of décor paper – about half the global total. Currently, its production tends to be at the lower-quality end and is mostly absorbed domestically. In the future, a shortfall in demand and/or a move up the quality spectrum could make China a more intense competitor of western European producers.
- ▶ Shareholders in NDT have to remember that they are minority holders; the Valentini family now controls 64% of the equity, having sold down 1.2m shares at €3.40 in October 2019.

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