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Rotork

Industrial engineering

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Positioning for growth

Rotork is taking decisive steps to determine its future size and shape. The company is not in a holding pattern awaiting a new CEO. Executive chairman Martin Lamb has taken the reins and end-market dynamics are driving a rethink in regards to innovation and the company's operating footprint. In addition, there is a considerable opportunity to drive aftermarket activity, with the benefits of improved visibility and profitability that should provide. In the short term, management's FY17 expectations have been maintained with stronger H2 delivery in sight; margins are expected to improve to a similar level to FY16.

H117 results reflect cost pressure on margins

Rotork delivered relatively straightforward H117 results, with revenue growth across all divisions. Group revenues grew by 13.6% in the period to £299.7m; currency contributed 11.5% while acquisitions added 2.1% leaving organic growth as flat. However, Controls, which accounts for nearly half of the group, delivered 6.3% and 2.2% organic order and top-line growth respectively. Inflationary cost pressures on labour and materials plus revenue phasing resulted in the group operating margin falling from 19.2% in H116 to 18.2% in H117. However, the company expects H217 margins to improve. End-market dynamics are starting to be more supportive in the upstream oil & gas, power, water and industrial markets, as the company's strategy of diversifying is working. The interim dividend was increased by 5.1% to 2.05p.

Stronger momentum implied from H217

Management has maintained FY17 guidance, with a stated improvement in operating margin. While this leaves FY17 margins just in line with FY16, it should see the company taking strong momentum into 2018. The focus on the innovation funnel supports medium-term expectations with R&D as a percentage of sales set to move up from just 1.7% currently, which will be funded by driving cost efficiencies. Meanwhile, M&A remains a consideration although the current bolt-on pipeline was described as thin. Management will also address the operations footprint, the supply chain and talent development, providing full analysis for the incoming CEO. Building the aftermarket from the installed base should also support profitability.

Valuation: Building for medium-term growth

FY17 is very much skewed to the second half while the overall emphasis is on medium-term delivery. The focus on innovation should drive earnings growth.

Consensus estimates

Year end	Revenue (£m)	PBT (£m)	EPS (p)	DPS (p)	P/E (x)	Yield (%)
12/15	546.5	101.9	10.4	5.05	22.4	2.2
12/16	590.1	91.1	10.0	5.10	23.3	2.2
12/17e	635.3	128.8	10.8	5.33	21.6	2.3
12/18e	661.9	139.3	11.8	5.87	19.8	2.5

Source: Bloomberg

Price	233.2p
Market cap	£2.03bn

Share price graph

Share details

Code	ROR
Listing	LSE
Shares in issue	870.2m

Business description

Rotork is a world-leading manufacturer of actuators and flow control systems. The group addresses the oil & gas, marine, mining, power generation and water treatment markets globally.

Bull

- Order book strength adds visibility
- Focus on product innovation and operations
- Opportunity to build aftermarket

Bear

- End-markets improving but still challenging
- Limited short-term opportunity for bolt-on growth
- Management change may add some caution

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