

XP Power

FY17 results

Increasing complexity drives growth

Strong demand across all markets and geographies, combined with market share gains and the recent Comdel acquisition, have resulted in record revenues and earnings for XP in FY17. Expanding its product range to include high voltage and RF power solutions has widened the company's addressable market and gives XP the opportunity to support its customers in the development of more complex solutions. With strong cash flow generation and access to debt, XP has the resources to fund growth, whether through internal product development or via acquisition.

Year end	Revenue (£m)	PBT* (£m)	Dil. EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/16	129.8	28.6	115.3	71.0	27.1	2.3
12/17	166.8	36.1	147.0	78.0	21.3	2.5
12/18e	175.8	37.4	158.9	82.0	19.7	2.6
12/19e	184.5	39.9	169.6	85.0	18.5	2.7

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

FY17 – a record year: Revenues +29%, EPS +27%

XP started to see an improvement in demand from the markets it serves from Q316 and this accelerated through the course of 2017. Revenues were further boosted by market share gains in healthcare, a stronger dollar and the Comdel acquisition in Q417. This resulted in record revenues and order intake, which translated into record earnings. Despite borrowing to fund the \$25m acquisition of Comdel, XP's net debt/adjusted EBITDA ratio stood at only 0.22x at year-end. The company has made good progress in moving its product portfolio up the power range and into more technically complex applications. It is focused on winning more designs with higher engineering solutions content, where its ability to support customers through the design process gives it an advantage over lower-cost Asian producers. Expansion of the Vietnam facility is on track and it should start production by the end of 2018, supporting volume growth.

FY18 – further growth with currency headwinds

Strong order intake through 2017 positions the company well for growth in 2018. The underlying level of growth and full-year contribution from Comdel are partially offset by the translation effects of the weaker dollar (we have cut our FY18 rate from \$1.34/£1 to \$1.4/£1). Combined with the lower corporate tax rate, we raise our FY18 EPS by 7.5% and forecast EPS growth of 6.7% in FY19.

Valuation: Reflects consistently profitable growth

On a P/E basis, XP is trading at a premium to global power converter companies and at a small discount to UK electronics companies, with a dividend yield at the top end of the range. XP generates EBITDA and EBIT margins at the top end of its peer group. We see scope for upgrades to earnings estimates from cross-selling and further market share gains in healthcare. The company is well funded to make further acquisitions, while maintaining its strong operating profitability.

Tech hardware & equipment

1 March 2018

Price **3,130p**

Market cap **£598m**

Spot rate: US\$1.4/£1

Net debt (£m) at end FY17 9.0

Shares in issue 19.1m

Free float 90%

Code XPP

Primary exchange LSE

Secondary exchange N/A

Share price performance



%	1m	3m	12m
Abs	(6.3)	(10.0)	64.3
Rel (local)	(2.6)	(8.8)	63.1
52-week high/low		3,740p	1,900p

Business description

XP Power is a developer and designer of power control solutions with production facilities in China, Vietnam and the US, and design, service and sales teams across Europe, the US and Asia.

Next events

Q1 update 13 April 2018

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Investment summary

Company description: Power control solutions for industry

XP Power designs, manufactures and distributes power converter solutions to original equipment manufacturers (OEMs) in the healthcare, technology and industrial markets. The group has its headquarters in Singapore and, to remain close to its global customer base, has a sales, design and engineering presence in the US, Europe and Asia. Unlike many in the industry, XP is vertically integrated; its manufacturing facilities in Asia and the US allow the company to maintain quality control, improve flexibility, reduce product costs and minimise lead times.

Financials: Record year

XP benefited from a combination of positive trends in FY17: good underlying demand in all of its market segments, market share growth in its healthcare business, positive currency effects and the acquisition of Comdel in Q417. The company has seen a strong order intake during FY17 and enters FY18 in a good position to drive further growth. Efficient manufacturing and good cost control mean that XP continues to report operating margins above 20% and lower ongoing tax rates boost our EPS forecasts in FY18 and FY19. Good cash generation should enable XP to pay down debt, maintain its dividend and consider further acquisitions to broaden its product range.

Exhibit 1: Changes to forecasts

	Normalised EPS (p)			PBT (£m)			EBITDA (£m)		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
2017	142.9	147.0	2.9	35.5	36.1	1.7	41.0	41.7	1.7
2018e	147.9	158.9	7.5	38.4	37.4	(2.6)	44.7	43.7	(2.1)
2019e	N/A	169.6	N/A	N/A	39.9	N/A	N/A	46.5	N/A

Source: XP Power accounts, Edison Investment Research

Valuation: Reflects consistently profitable growth

On a P/E basis, the company is trading at a premium to global power converter companies and at a small discount to UK electronics companies, with a dividend yield at the top end of the range. XP generates EBITDA and EBIT margins at the top end of its peer group. Revenue growth is similar to peers, although as a sterling-reporting company, FY18 underlying revenue growth is masked by the translation from US dollars. We see scope for upgrades to earnings estimates from cross-selling and further market share gains in healthcare. We expect the company to return to a net cash position by the end of FY19 – combined with up to \$60m in available debt, the company is in a strong position to make further acquisitions while maintaining its consistently high level of profitability.

Sensitivities: Cyclical, competition, currency

XP Power has cyclical exposure to global industrial, technology and healthcare markets and is therefore sensitive to end-demand and product development expenditure in these markets. Visibility of customer volumes is limited and, as such, individual customer orders can be volatile. With the majority of XP's revenues, manufacturing costs and opex US dollar-denominated, currency will continue to add volatility to XP Power's reported revenues, although it will have less impact at the net income level. XP competes with large global industrial companies as well as low-cost Asian manufacturers, XP also has more limited exposure to the euro/sterling exchange rate; to minimise this, the company enters into forward contracts. Recent acquisitions add integration risk.

Company description: Power control solutions

XP Power designs, manufactures and distributes power converter solutions to OEMs in the industrial, healthcare and technology markets. Power converters take the high-voltage alternating current output from the mains supply and convert it into various lower-voltage, stable direct current outputs that are required to drive most electronic equipment. The company has transitioned from being a distributor to designing and manufacturing the majority of its products. In 2015, the company made two acquisitions, EMCO and a South Korean distributor, for a total of £9.1m and in 2017, acquired Comdel for £18.8m. The group has its headquarters in Singapore and has volume manufacturing facilities in China and Vietnam and specialist high-voltage and radio frequency (RF) power product manufacturing in the US.

Background: Specialist designer and manufacturer

XP Power was formed as a specialist distributor of power converters in 1988 (based in Pangbourne, UK). Subsequently, the business merged with Foresight (California, US) and IPS (New England, US) on flotation in 2000 to form a distributor with more than \$100m of sales. In 2002, the board decided to begin developing its own IP and designs, and bought Switching Systems International (California, US), which designed its own configurable power converters with an outsourced manufacturing model. Since then the group has continued to develop its own products and brand, built out manufacturing capacity in China and Vietnam and completed the transition from distributor to designer and manufacturer. Recent acquisitions have expanded XP's product range from low power AC/DC and DC/DC converters to include high voltage, low power converters (EMCO) and RF power products (Comdel). The company sells through 27 sales offices and multiple distributors across Europe, Asia and North America. XP has engineering service functions in Northern California, Germany and the UK. FY17 revenues were generated in North America (53%), Europe (38%) and Asia (9%).

XP is focused on developing tailored products for applications with high reliability requirements in the technology, industrial and healthcare equipment markets. It avoids developing commodity products for high volume consumer electronics applications. Products in each end-market can have very different life cycles. For example, a medical device could have a product life cycle of 10 years or more. Once a power converter is designed into this product, it is likely to remain in it for the full life of the product. On average, the product life cycle is five to seven years. XP's balanced mix of end-customers means it has a fairly high level of revenues that are recurring in nature and exposure to multiple end-markets mitigates the risk of individual industry cyclicality.

Close to reaching targets for own-IP products

XP Power's business splits along three business lines:

- Own-manufactured product (76% of FY17 revenues). Products designed by XP, ownership of 100% of the IP and manufactured in its Shanghai, Vietnam or US facilities. This includes engineered solutions where XP power supplies are customised for specific customer end-product design requirements ie designing and engineering additional casings, metalwork, circuitry, connectors.
- Labelled products (22%). Customer requirements identified and product design specified by XP, but products sourced from third-party manufacturers and labelled under the XP brand.
- Distribution (2%). Supply of third-party products.

The company had set a target of generating 75% of sales from own-designed product. It hit this target in FY17, growing from 73% of sales in FY16 to 76% in FY17. Management believes this could still trend higher.

In-house manufacturing well-established

The company manufactures power converters and magnetic components in two locations, China and Vietnam, with smaller US facilities acquired through the EMCO and Comdel deals.

China: Main power converter facility

XP built a manufacturing facility in Kunshan, China (near Shanghai) and started production there in 2006. By the end of 2017, the Chinese facility was operating at c 90% capacity. In addition to making power converters at this facility, XP introduced small-scale production of magnetic components (these are components that go into the end-product and were previously bought in from third parties). This gives XP more control over the manufacturing process (important for some customers) and assists the design teams by shortening design cycles. At this facility, magnetic components are mainly produced for prototyping and short lead-time contracts.

Vietnam: Magnetics and less complex power converters

To reduce XP's exposure to rising Chinese labour costs and gain more control over the manufacturing process, XP expanded manufacturing into Vietnam, at a site near Ho Chi Minh City. The first phase (approximately the same size as the Chinese facility) was completed in 2011. The facility first started to produce magnetic components – these have a high labour component, hence the decision to manufacture them in a lower labour cost country. XP now manufactures virtually all of its magnetics requirements in house. In FY17, XP manufactured 6.7m magnetic components (+37% y-o-y).

In 2014, the facility also started manufacturing power converters, starting with some of the less complex converters and, once qualified, shifting production entirely from China to Vietnam. The facility continues to qualify additional converter products and runs production in parallel with the Chinese facility until it achieves acceptable yields on those products. This process frees up capacity in China for more complex product. In FY17, this facility manufactured one million power converters (up from 0.4m in FY16), around 60% of XP's total converter output in the year. To cope with the expected growth in demand, the company has started work on the second facility (Vietnam II) on the same site. Vietnam II is likely to be similar in size to the existing facility. The company broke ground in Q417, with production expected from the end of FY18.

US: Specialist facilities

Through the two US acquisitions, XP has facilities in the US for the more complex high voltage and RF products. EMCO has two facilities, Nevada and California, where it manufactures its high-voltage DC/DC converters. It also uses outsourcing partners for some manufacturing. Comdel has a 60,000 square feet manufacturing facility in Gloucester, Massachusetts. The component manufacturing for Comdel's products is outsourced within the US and final assembly and test is performed in the Comdel facility. We would expect XP to consider shifting some component production for new designs to Asia to reduce the manufacturing cost and to enable the supply of higher volume programmes. As EMCO and Comdel products are typically more complex than XP's low power products (and therefore higher value), it makes sense to retain the specialist expertise of the US-based manufacturing facilities.

Growth strategy

XP's strategy to drive revenue and profitability growth and to gain market share has been in place for a number of years. The current strategy aims to:

- Develop a broad range of competitive products;

- Target key customer accounts where XP can add value;
- Increase vertical penetration of target key accounts;
- Enhance brand awareness through digital marketing and distribution;
- Accelerate operational excellence;
- Lead the industry on environmental matters; and
- Acquire complementary businesses to expand the product offering.

We discuss the progress XP is making below.

Product development: Expand the range of technologies and services available

Historically, XP designed and manufactured low power AC/DC converters, supplying voltages up to 120V, with the majority of products sold supplying 24V. As competition from low cost Asian suppliers has increased, XP has started moving along the complexity scale. While it is investing in engineering resource to develop higher voltage products, it expects to make the majority of major product additions via acquisition, as this is a much faster route.

In 2015, XP bought EMCO to add high voltage, low power converters to its range. EMCO's DC/DC converters can supply voltages up to 40kV, with the majority of products in the 5-12kV range.

In 2017, XP acquired Comdel¹ to add RF power solutions. Comdel designs RF power supplies, DC power supplies, impedance matching networks, multi-channel synthesisers and electrostatic chuck power supplies. It supplies standard, modified and custom products – due to the complexity of the products we understand that there is a higher proportion of custom work compared to XP's product range. Its RF power supplies are sold to the semiconductor production equipment (SPE), thin film, photovoltaics and induction heating industries.

XP aims to have the most comprehensive and up-to-date product range in its target markets. The company introduced 27 new products in 2017 (versus 47 in 2016 which was boosted by the introduction of a new third-party supplier of DC/DC product). In 2017, XP spent £11.5m on R&D (pre-capitalisation and amortisation), up 44% from the £8.0m spent in 2016. The increase was partly due to the addition of Comdel in Q417.

Developing more custom capability; expanding engineering services

XP splits its R&D activities between developing new standard products and developing modifications to existing products to meet specific customer requirements. With competition tending to come from Asian manufacturers of low-complexity converters, the company is focused on serving customers with more complex requirements and undertakes custom design work for large customers. It is building up its engineering services teams globally to provide this face-to-face support during the design process.

Targeting key accounts – new and existing

XP Power has more than 5,000 direct active customers, of which no customer makes up greater than 11% of revenues and no single project makes up more than 4% of revenues. In 2017, the top 30 customers made up 48% of revenues. XP Power supplies power converters to three key markets: industrial, healthcare and technology (see Exhibit 2).

¹ [Entering the RF power supply market](#), 2 October 2017

Exhibit 2: End-market breakdown

Sector	FY17 revenue split	Types of products
Industrial	39%	Factory automation, automated test equipment, industrial control, 3D printing, test & measurement, instrumentation, hazardous environments, defence, avionics.
Healthcare	31%	Medically approved power solutions for use in patient vicinity applications and in the lab environment, including homecare devices, highly efficient convection-cooled designs for low-noise patient area devices and defibrillator-proof DC/DC converters for applied part applications.
Technology	30%	Semiconductor production equipment, audio visual broadcast equipment, mobile & wireless communications, computing and data processing.

Source: XP Power

Leverage approved supplier status

XP's in-house manufacturing helps the company to sign up blue-chip customers, particularly in the medical equipment and semiconductor equipment markets. Stable and secure power supply is so crucial to the operation of these customers' products that they demand complete control over their supply chain and product manufacture to ensure quality. XP has achieved approved or preferred supplier status at a large number of customers, including all of the main healthcare equipment companies, and is now working to expand its share of business at each customer.

Cross-selling from acquisitions

EMCO's customer base has limited crossover with XP's existing customer base. As XP's AC/DC converters often provide the DC input for high-voltage DC/DC converters, there is good cross-selling potential. Currently, the vast majority of Comdel's revenues are generated from sales to SPE manufacturers (95%), with a limited amount of business from industrial customers. XP already supplies the SPE market, and this acquisition will increase its exposure to that market. XP and Comdel have some customers in common, but they do not overlap in terms of products sold.

Focus on operational excellence

XP has generated gross margins approaching 50% and operating margins above 20% since 2010, showing how efficiently the business has been run since shifting to the design and manufacture business model. The company continually looks at ways to maintain and improve on this performance. This includes the focus on lean manufacturing as well as improvements to internal processes to enable the company to share information internally more effectively and to provide better customer service. In 2018, XP will invest in upgrading its SAP ERP software, starting with the China and Vietnam manufacturing facilities.

High-efficiency products support 'green' credentials

XP is a full member of the Responsible Business Alliance (RBA). XP incorporated green technologies into the Vietnamese facility and received the Gold Plus rating by the Singapore Building and Construction Authority (BCA) for non-residential buildings in tropical climates. This is the first BCA Green Mark industrial facility in Vietnam and is the industry's most environmentally friendly building.

Having manufacturing facilities and products that meet high environmental standards helps XP to win approved supplier status with large OEMs, but its main ongoing contribution to sustainability is to design ever-more efficient power converters. For example, a 95% efficient product such as the CCM250 only wastes 5% of the input energy, thereby requiring a lower power input to achieve the same output as a device operating at a lower efficiency. The wasted power is often converted to heat, which in turn requires additional power or physical heat sinks to provide cooling, adding to the upfront and running costs of the product. In FY17, sales of 'green' (ie high-efficiency) products grew 31% to make up 24% of revenues, compared to 23% in FY16 and, of the 27 new products introduced in the year, 19 were high efficiency designs.

Market outlook

Exhibit 3 shows the split of revenues by geography and end-market over the last two years. While all three end-markets generated growth in FY17, the growth in the Technology segment over the course of 2017 has resulted in a more even spread of revenues across end markets.

- **Industrial sector:** this is the most fragmented market. Areas where the company is seeing demand include 3D printing, industrial printing, industrial LED lighting, signage and smart grid. At 9.7% this saw the slowest level of growth of the three end markets, although this came on the back of a year of 23% growth in FY16.
- **Healthcare sector:** XP has corporate approvals from all of the major healthcare companies. The business saw very strong growth of 34.6% as new programmes started placing volume orders, particularly in Europe.
- **Technology sector:** growth from this sector accelerated in FY17, at 56.4% compared to 19.8% in FY16. In FY16, the business saw a pick-up in demand from SPE companies (revenues up 50% to total 12% of group revenues) – demand remained robust in this sector in 2017 resulting in revenues from SPE customers growing more than 80% to make up 56% of the division's revenues and 17% of group revenues. One quarter's worth of Comdel revenues partly contributed to the growth, as nearly all of its revenues come from the SPE sector.

Exhibit 3: Revenues by geography and end market

Healthcare	FY16	FY17	% y-o-y	Industrial	FY16	FY17	% y-o-y	Technology	FY16	FY17	% y-o-y
North America	23.5	31.0	31.9%	North America	23.7	24.2	2.1%	North America	21.4	39.2	83.2%
Europe	12.7	16.1	26.8%	Europe	29.6	33.7	13.9%	Europe	7.1	7.7	8.5%
Asia	1.7	3.9	129.4%	Asia	6.5	7.7	18.5%	Asia	3.6	3.3	-8.3%
Total	37.9	51.0	34.6%	Total	59.8	65.6	9.7%	Total	32.1	50.2	56.4%
% of total revenues	29.2%	30.6%			46.1%	39.3%			24.7%	30.1%	

Source: XP Power

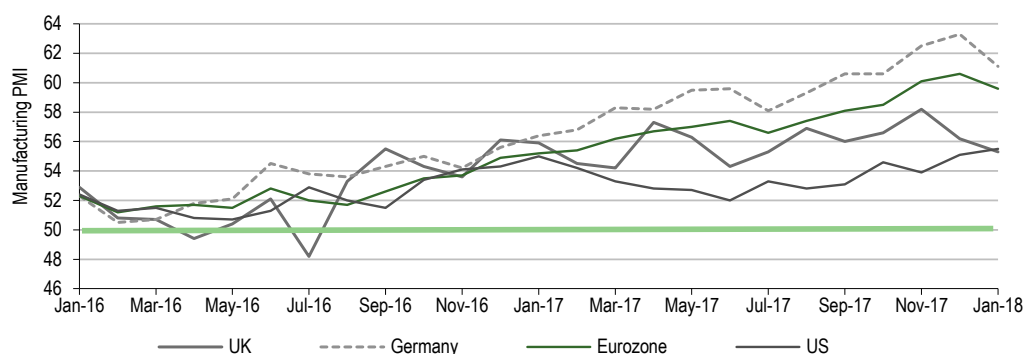
Long-term growth drivers

Key drivers of market growth include:

- **Regulation:** legislation and consumer pressure are driving OEMs to reduce the power consumption of their products. Legislation also extends to the efficiency of power converters, driving demand for new products. XP's new products are designed to maximise efficiency;
- **Healthcare:** as the population ages, while continuing to grow overall, people are living longer with chronic diseases, driving overall healthcare spending;
- **Technology:** several trends are driving demand for processing power and memory, including internet of things (IoT), artificial intelligence (AI), big data, blockchain, augmented and virtual reality, and autonomous vehicles. It is possible that the growth of each of these technologies in parallel could reduce the cyclical nature of the semiconductor industry.
- **Alternative energy:** technologies are evolving for lighting (eg LEDs) and power generation (eg solar, wind), which all have specific power conversion needs; and
- **Innovation:** customers increasingly need to differentiate their products from the competition. XP's in-house design capabilities enable it to develop products for niche applications.

Short-term outlook

The strength of the industrial market depends on the health of the global economy. In 2017, manufacturing PMI data remained above 50 (the level that implies expansion rather than contraction) in the US, UK, Germany and the Eurozone, and in fact all four regions are at levels not seen for several years. This should imply a positive outlook for XP's industrial business in FY18.

Exhibit 4: Manufacturing PMI data – January 2016 to January 2018


Source: Markit

According to Gartner, the global IT market grew 3.8% in 2017, after a small 0.6% decline in 2016. It is forecasting growth of 4.5% in 2018. The semiconductor market is forecast to grow 7% in 2018, after 20.6% growth in 2017 (source: WSTS). According to SEMI, the semiconductor equipment market surpassed its original forecast for 9.3% growth, instead growing 35.6% in 2017. This was after a year of 8.7% growth in 2016. SEMI is forecasting growth of 7.5% for 2018.

The healthcare technology market is expected to show steady growth in the low single-digit percentage range. Philips estimates that the healthcare technology market was worth c €145bn in 2015 and is likely to show a CAGR of 6-7% to 2019. Within that market, diagnostics and treatment technology (just over a third of the total market) is likely to grow at a CAGR of 4% over the same period. The shorter-term performance from the major healthcare equipment manufacturers mirrors this. In 2017, GE Healthcare saw a 6% increase in equipment orders and a 5% increase in revenues. Philips's healthcare diagnosis and treatment business saw constant currency revenue growth of 3% in 2017. Siemens's healthcare business saw constant currency revenue growth of 3% and order growth of 4% in FY17, with order growth of 2% in Q118 (calendar Q417), providing support for steady progress in 2018.

Competitive positioning

Excluding RF power, XP Power operates in a market that was estimated to be worth c \$2.9bn in 2017 (source: Micro-Tech Consultants). The market is fragmented, with no player having more than a 10% global share. Based on Micro-Tech Consultants' market statistics, XP Power estimates its global market share stands at 7.1% (up from 6.1% in 2016), with 11.4% market share in Europe, 11.1% in North America and 1.2% in Asia. XP Power does not operate in the high-volume, low-value commodity power converter markets that supply products such as PCs, laptops and cell phone chargers, or in the market for inverters used for renewable energy. The company estimates that the RF power market is worth c \$800m – annualising Comdel's Q417 revenues implies a market share of c 3%. Exhibit 5 summarises the main competitors in each of the product areas that XP operates in. In the low power, low voltage market, XP competes most often with TDK-Lambda and Mean Well as well as with a number of local Asian suppliers.

Exhibit 5: Competition by product type

Low voltage	High voltage	RF power
Artesyn (Platinum Equity)	Advanced Energy Industries	Advanced Energy Industries
Cosel	Crane Co	COMET Holding
Delta Electronics	Matsusada Precision	MKS Instruments
Mean Well	Spellman High Voltage Electronics	TRUMPF Huettinger
TDK Lambda (TDK Corporation)		

Source: Edison Investment Research

Sensitivities

XP Power is a global electronics company supplying a broad range of end markets. The company is not immune to economic slowdown, but diversification and the low-cost structure afford the company some earnings resilience versus competitors.

- **Economic sensitivity:** the group has cyclical exposure to global industrial, technology and healthcare markets. Therefore, any slowdown in end-demand in these markets or cutbacks in product development expenditure will have an impact on XP's revenues.
- **Order book visibility:** the group has around four months of order book visibility at any one time. Therefore, visibility of customer volumes is limited and, as such, individual customer orders can be volatile.
- **Currency:** around 80% of XP's revenues, c 95% of cost of sales and c 65% of opex are US dollar-denominated. XP Power reports in sterling, exposing the company's results to fluctuations in the US\$/£ exchange rate. While moves in the exchange rate will have an effect on reported revenues, the overall impact of currency at the net income level is much less pronounced. XP is also exposed to fluctuations in the euro versus sterling (c 10% of revenues and c 15% of operating costs are euro-denominated). To minimise the effect, the company enters into forward contracts.
- **Large competitors:** competition ranges from significantly larger players with big balance sheets through to smaller innovative companies. The deeper pockets of large competitors may make it more difficult for XP Power to keep pace with product development.
- **Acquisitions:** XP has recently made acquisitions and continues to assess potential targets, adding integration risk.

Financials

Review of FY17 results

As previously highlighted in its January trading update, XP reported revenue growth of 28.5% for FY17. On a constant currency basis, revenues grew 22%, with 3% of this growth contributed by the acquisition of Comdel in Q417. As previously flagged, the gross margin fell year-on-year, mainly due to the effect of the strengthening of the US dollar versus sterling (average rate of 1.28 in FY17 vs 1.38 in FY16). With more than 90% of revenues generated in US dollars, and close to 80% of cost of sales also US dollar denominated, as these are translated to sterling, a stronger dollar results in higher sterling revenues and gross profits, but reduces the gross margin. We expect the opposite effect in FY18 as the dollar has since weakened against the pound. EBITDA and normalised operating profit came in slightly ahead of our forecasts. Operating expenses excluding depreciation and amortisation increased 24% y-o-y, reflecting increased costs from Comdel, as well as the hiring of engineers for R&D and customer support.

Exceptional charges were acquisition-related: £2.8m reported at half-year for an aborted acquisition and £0.5m incurred in the acquisition of Comdel. XP reported two exceptional tax credits in FY17: the first relates to a £1.3m overpayment of tax in Singapore. The second £1.3m credit is a reduction in the deferred tax liability arising from the reduction in US corporate tax rates from 35% to 21% from the start of FY18. These have been excluded from our normalised profit calculations.

The company announced a final quarterly dividend of 29p (vs 26p a year ago) payable on 20 April to shareholders as at 16 March. This resulted in a full year dividend of 78p, ahead of our 76p forecast. Net debt at year-end of £9.0m came in below our £12.6m forecast, mainly due to lower working capital consumption.

Exhibit 6: Summary financials

Year end December (£m)	FY16	FY17e	FY17	Diff	y-o-y
Revenues	129.8	166.7	166.8	0.0%	28.5%
Gross profit	62.0	77.8	77.6	(0.2%)	25.2%
Gross margin	47.8%	46.6%	46.5%	(0.1%)	(1.2%)
EBITDA	33.0	41.0	41.7	1.7%	26.4%
EBITDA margin	25.4%	24.6%	25.0%	1.6%	(0.4%)
Normalised operating profit	28.8	35.9	36.4	1.5%	26.4%
Normalised operating profit margin	22.2%	21.5%	21.8%	0.3%	(0.4%)
Reported operating profit	28.0	32.7	32.5	(0.5%)	16.1%
Reported operating margin	21.6%	19.6%	19.5%	(0.1%)	(2.1%)
Normalised PBT	28.6	35.5	36.1	1.7%	26.2%
Reported PBT	27.8	32.3	32.2	(0.3%)	15.8%
Normalised net income	22.1	27.4	28.5	4.0%	29.0%
Reported net income	21.3	24.3	28.3	16.4%	32.9%
Normalised basic EPS (p)	116.2	144.4	149.4	3.4%	28.5%
Normalised diluted EPS (p)	115.3	142.9	147.0	2.9%	27.5%
Reported basic EPS (p)	112.0	128.0	148.3	15.8%	32.4%
Dividend per share (p)	71.0	76.0	78.0	2.6%	9.9%
Net debt/(cash)	(3.7)	12.6	9.0	(28.5%)	N/A

Source: XP Power, Edison Investment Research

Debt refinanced in Q417 to fund Comdel acquisition

At the end of H117, XP had debt of £3.3m owing on a term loan, which was repaid in September 2017. When XP acquired Comdel, it entered into a \$40m revolving credit facility with HSBC and Fifth Third Bank, with whom it also has access to a \$20m accordion facility. XP is paying interest at LIBOR+1% on the drawn amount (£24m/\$32.4m at end FY17) and LIBOR+0.4% on the undrawn amount. With cash of £15.0m, the company closed the year with a net debt position of £9.0m. This equated to a net debt/adjusted EBITDA ratio of 0.22x.

Outlook and changes to forecasts

The company received orders worth £184.3m in FY17 (+38% y-o-y, +31% constant currency, +26% organic), of which £46.8m was received in Q417. This resulted in a book-to-bill of 1.11x for FY17 and 1.09x for Q417. Management expects growth in revenues and profits in FY18. We have made the following changes to our forecasts:

- Currency: we have increased the average \$/£ rate from 1.34 to 1.4 for FY18 and FY19.
- Revenues: we have increased underlying revenue growth from 6% to 7% and also increased our Comdel estimate from \$19m to \$23m in FY18. Comdel revenues grew 30% y-o-y in Q417 and Q4 book-to-bill was 1.41x, supporting strong growth in FY18. We have factored in underlying revenue growth of 5% in FY19. The combined effects of these changes reduces our FY18 revenue forecast by 1.9%.
- Capex: we have factored in higher capex to reflect the ERP upgrade programme. We had already factored in the Vietnam expansion.
- Tax: we have reduced our effective tax rate from 25.5% to 17.0%.
- EPS: any negative currency impacts are more than outweighed by the reduction in the tax rate – overall we increase our normalised diluted EPS by 7.5% in FY18.
- Net debt: the Singapore tax refund and better working capital management reduce our end FY18 net debt forecast from £9.3m to £5.5m. We forecast a return to a net cash position by the end of FY19.

Exhibit 7: Changes to forecasts

Year end December (£m)	FY18e		%		FY19e	
	Old	New	change	y-o-y	New	y-o-y
Revenues	179.1	175.8	(1.9%)	5.4%	184.5	5.0%
Gross profit	81.9	81.0	(1.1%)	4.4%	85.1	5.0%
Gross margin	45.7%	46.1%	0.4%	(0.4%)	46.1%	0.0%
EBITDA	44.7	43.7	(2.1%)	4.8%	46.5	6.5%
EBITDA margin	24.9%	24.9%	(0.1%)	(0.1%)	25.2%	0.4%
Normalised operating profit	39.0	38.0	(2.4%)	4.4%	40.5	6.6%
Normalised operating profit margin	21.7%	21.6%	(0.1%)	(0.2%)	22.0%	0.3%
Reported operating profit	38.6	36.6	(5.0%)	12.6%	39.3	7.4%
Reported operating margin	21.5%	20.8%	(0.7%)	1.3%	21.3%	0.5%
Normalised PBT	38.4	37.4	(2.6%)	3.6%	39.9	6.7%
Reported PBT	38.0	36.0	(5.2%)	11.8%	38.7	7.6%
Normalised net income	28.4	30.8	8.7%	8.1%	32.9	6.7%
Reported net income	28.1	29.6	5.6%	4.7%	31.9	7.6%
Normalised basic EPS (p)	149.4	161.4	8.0%	8.1%	172.3	6.7%
Normalised diluted EPS (p)	147.9	158.9	7.5%	8.1%	169.6	6.7%
Reported basic EPS (p)	147.8	155.2	5.0%	4.7%	167.1	7.6%
Dividend per share (p)	79.0	82.0	3.8%	5.1%	85.0	3.7%
Net debt/(cash)	9.3	5.5	(40.9%)	(39.2%)	(4.1)	N/A

Source: Edison Investment Research

Valuation

There is a limited number of listed power converter companies, as many businesses are part of larger industrial companies such as TDK or GE. We show below the financial performance of those listed peers as well as a group of UK-listed companies active in the electronics space.

XP clearly generates EBITDA and EBIT margins at the top end of the peer group. Revenue growth is similar, although as a sterling-reporting company, FY18 underlying revenue growth is masked by the translation from US dollars. On a P/E basis, the company is trading at a premium to global power converter companies and at a small discount to UK electronics companies, with a dividend yield at the top end of the range. We see scope for upgrades to earnings estimates from cross-selling and further market share gains in healthcare, and expect to see the company make further acquisitions to drive growth.

Exhibit 8: Peer group financial performance

	Market	Share	Listing	Revenue growth			EBITDA margin			EBIT margin		
	cap (m)	price	ccy	CY17	CY18e	CY19e	CY17	CY18e	CY19e	CY17	CY18e	CY19e
XP Power	598	3130	GBp	28.5%	5.4%	5.0%	25.0%	24.9%	25.2%	21.8%	21.6%	22.0%
Cosel*	61921	1664	JPY	17.7%	6.6%	2.1%	22.5%	23.8%	23.2%			
Delta Electronics**	361059	139	TWD	4.0%	6.7%	6.7%	13.1%	13.7%	13.7%	8.8%	9.6%	10.1%
Advanced Energy Industries	2643	66.7	USD	38.7%	12.0%	5.3%	31.3%	32.5%	31.3%	29.9%	32.7%	32.6%
Comet Holdings**	1078	139	CHF	32.8%	9.3%	8.3%	15.0%	16.3%	17.1%	12.2%	13.3%	13.7%
CML Microsystems***	90	532.5	GBp	15.4%	6.3%		30.9%	32.4%		13.8%	14.1%	
Diploma*	1258	1111	GBp	18.1%	6.1%	4.3%	16.2%	18.4%	18.6%	15.2%	16.7%	17.0%
Electrocomponents***	2820	638.2	GBp	12.8%	5.0%	4.6%	11.9%	12.2%	12.7%	10.1%	10.5%	10.9%
Gooch & Housego*	351	1435	GBp	30.2%	8.9%	3.8%	17.3%	18.7%	19.0%	11.9%	15.7%	15.8%
TT Electronics**	370	227	GBp	-36.9%	4.1%	4.9%	10.9%	10.7%	11.0%	6.4%	6.7%	6.8%
Average power converter companies				23.3%	8.7%	5.6%	20.5%	21.6%	21.3%	17.0%	18.5%	18.8%
Average UK electronics companies				7.9%	6.1%	4.4%	17.4%	18.5%	15.3%	11.4%	12.7%	12.6%

Source: Edison Investment Research, Bloomberg (as at 27 February). Note: *CY17=y/e 31 May 2018; **CY17 = estimate; ***CY17=y/e 31 March 2018; *CY17=y/e 30 September 2017.

Exhibit 9: Peer group valuation metrics

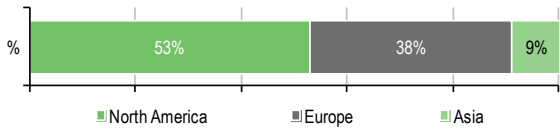
	P/E (x)			EV/EBITDA (x)			Dividend yield (%)		
	CY17	CY18e	CY19e	CY17	CY18e	CY19e	CY17	CY18e	CY19e
XP Power	21.3	19.7	18.5	14.3	13.6	12.8	2.5%	2.6%	2.7%
Cosel	17.4	15.9	15.2	8.5	7.5	7.5	2.0%	2.2%	2.2%
Delta Electronics	19.1	17.3	15.2	11.7	10.5	9.8	3.6%	4.0%	4.3%
Advanced Energy Industries	15.0	12.8	12.3	10.6	9.1	9.0	0.0%	0.0%	0.0%
Comet Holdings	27.9	23.3	20.5	16.5	13.9	12.3	1.1%	1.3%	1.5%
CML Microsystems	23.6	21.4		7.8	7.0		1.6%	1.5%	
Diploma	22.3	20.7	19.6	16.9	14.1	13.4	2.1%	2.3%	2.4%
Electrocomponents	23.5	20.8	18.9	14.5	13.5	12.4	2.0%	2.2%	2.4%
Gooch & Housego	35.6	25.5	24.1	17.4	14.7	14.0	0.7%	0.8%	0.8%
TT Electronics	23.2	19.6	17.6	11.2	10.9	10.1	2.5%	2.6%	2.7%
Average power converter companies	19.9	17.3	15.8	11.8	10.3	9.7	1.7%	1.9%	2.0%
Average UK electronics companies	25.6	21.6	20.0	13.6	12.0	12.5	1.8%	1.9%	2.1%

Source: Edison Investment Research, Bloomberg (as at 27 February)

Exhibit 10: Financial summary

	£'m	2012	2013	2014	2015	2016	2017	2018e	2019e
31-December		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT									
Revenue		93.9	101.1	101.1	109.7	129.8	166.8	175.8	184.5
Cost of Sales		(49.0)	(51.5)	(51.0)	(55.1)	(67.8)	(89.2)	(94.7)	(99.5)
Gross Profit		44.9	49.6	50.1	54.6	62.0	77.6	81.0	85.1
EBITDA		23.3	26.0	27.6	29.7	33.0	41.7	43.7	46.5
Normalised operating profit		21.0	23.3	24.5	25.9	28.8	36.4	38.0	40.5
Amortisation of acquired intangibles		0.0	0.0	0.0	0.0	(0.4)	(0.6)	(1.4)	(1.2)
Exceptionals		0.0	0.0	0.0	(0.3)	(0.4)	(3.3)	0.0	0.0
Share-based payments		0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Reported operating profit		21.0	23.3	24.5	25.6	28.0	32.5	36.6	39.3
Net Interest		(0.8)	(0.4)	(0.2)	(0.2)	(0.2)	(0.3)	(0.6)	(0.6)
Joint ventures & associates (post tax)		0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Exceptional & other financial		0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Profit Before Tax (norm)		20.2	22.9	24.3	25.7	28.6	36.1	37.4	39.9
Profit Before Tax (reported)		20.2	22.9	24.3	25.4	27.8	32.2	36.0	38.7
Reported tax		(4.5)	(4.5)	(4.8)	(5.5)	(6.3)	(3.6)	(6.1)	(6.6)
Profit After Tax (norm)		15.7	18.4	19.5	20.2	22.3	28.8	31.1	33.1
Profit After Tax (reported)		15.7	18.4	19.5	19.9	21.5	28.6	29.9	32.1
Minority interests		(0.2)	(0.2)	(0.1)	(0.2)	(0.2)	(0.3)	(0.3)	(0.3)
Discontinued operations		0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net income (normalised)		15.5	18.2	19.4	20.0	22.1	28.5	30.8	32.9
Net income (reported)		15.5	18.2	19.4	19.7	21.3	28.3	29.6	31.9
Basic average number of shares outstanding (m)		19	19	19	19	19	19	19	19
EPS - basic normalised (p)		81.67	95.84	102.12	105.28	116.22	149.36	161.41	172.30
EPS - diluted normalised (p)		81.35	95.05	101.07	104.32	115.33	147.00	158.91	169.63
EPS - basic reported (p)		81.67	95.84	102.12	103.70	112.02	148.31	155.23	167.06
Dividend (p)		50	55	61	66	71	78	82	85
Revenue growth (%)		(9.4)	7.7	0.0	8.5	18.3	28.5	5.4	5.0
Gross Margin (%)		47.8	49.1	49.6	49.8	47.8	46.5	46.1	46.1
EBITDA Margin (%)		24.8	25.7	27.3	27.0	25.4	25.0	24.9	25.2
Normalised Operating Margin		22.4	23.0	24.2	23.6	22.2	21.8	21.6	22.0
BALANCE SHEET									
Fixed Assets		52.8	53.3	56.1	65.4	73.2	88.1	96.5	100.5
Intangible Assets		38.1	39.1	40.5	48.2	53.0	63.9	65.2	66.7
Tangible Assets		13.2	12.7	14.4	16.1	19.1	22.5	29.6	32.1
Investments & other		1.5	1.5	1.2	1.1	1.1	1.7	1.7	1.7
Current Assets		39.3	42.2	47.0	53.5	65.7	83.5	85.6	93.5
Stocks		19.8	20.4	25.2	28.7	32.2	37.8	41.5	43.6
Debtors		14.2	15.4	16.0	17.5	21.5	23.8	26.5	27.8
Cash & cash equivalents		4.1	5.0	3.8	4.9	9.2	15.0	13.5	18.1
Other		1.2	1.4	2.0	2.4	2.8	6.9	4.0	4.0
Current Liabilities		(20.2)	(22.4)	(18.6)	(19.8)	(25.8)	(25.1)	(26.1)	(27.1)
Creditors		(11.1)	(12.7)	(14.4)	(14.6)	(16.1)	(21.4)	(22.4)	(23.4)
Tax and social security		(1.6)	(1.1)	(1.7)	(1.2)	(3.3)	(3.5)	(3.5)	(3.5)
Short term borrowings		(7.3)	(8.5)	(2.5)	(4.0)	(5.5)	0.0	0.0	0.0
Other		(0.2)	(0.1)	0.0	0.0	(0.9)	(0.2)	(0.2)	(0.2)
Long Term Liabilities		(10.6)	(3.7)	(4.2)	(10.0)	(6.2)	(29.6)	(24.6)	(19.6)
Long term borrowings		(7.4)	0.0	0.0	(4.6)	0.0	(24.0)	(19.0)	(14.0)
Other long term liabilities		(3.2)	(3.7)	(4.2)	(5.4)	(6.2)	(5.6)	(5.6)	(5.6)
Net Assets		61.3	69.4	80.3	89.1	106.9	116.9	131.3	147.2
Minority interests		(0.2)	(0.2)	(0.1)	(0.8)	(0.8)	(0.9)	(1.0)	(1.1)
Shareholders' equity		61.1	69.2	80.2	88.3	106.1	116.0	130.3	146.1
CASH FLOW									
Op Cash Flow before WC and tax		23.3	26.0	27.6	29.7	33.0	41.7	43.7	46.5
Working capital		4.2	(0.3)	(4.1)	(4.6)	(6.1)	0.4	(5.4)	(2.4)
Exceptional & other		0.4	(0.5)	1.9	0.6	5.1	(6.3)	0.0	0.0
Tax		(4.3)	(5.0)	(3.6)	(4.7)	(4.1)	(6.1)	(3.2)	(6.6)
Net operating cash flow		23.6	20.2	21.8	21.0	27.9	29.7	35.1	37.6
Capex		(4.7)	(3.2)	(5.8)	(5.4)	(6.8)	(10.1)	(15.5)	(11.2)
Acquisitions/disposals		(1.6)	0.1	0.1	(8.3)	0.1	(18.3)	0.0	0.0
Net interest		(0.5)	(0.3)	(0.1)	(0.1)	(0.2)	(0.2)	(0.6)	(0.6)
Equity financing		(0.5)	0.1	(0.2)	0.0	0.2	(0.2)	0.0	0.0
Dividends		(9.1)	(10.1)	(11.0)	(12.2)	(13.1)	(14.2)	(15.5)	(16.2)
Other		0.5	0.2	0.1	0.2	0.0	0.0	0.0	0.0
Net Cash Flow		7.7	7.0	4.9	(4.8)	8.1	(13.3)	3.5	9.5
Opening net debt/(cash)		18.6	10.6	3.5	(1.3)	3.7	(3.7)	9.0	5.5
FX		0.3	0.1	(0.1)	(0.2)	(0.5)	0.7	0.0	0.0
Other non-cash movements		0.0	0.0	0.0	0.1	(0.2)	(0.1)	0.0	0.0
Closing net debt/(cash)		10.6	3.5	(1.3)	3.7	(3.7)	9.0	5.5	(4.1)

Source: XP Power, Edison Investment Research

Contact details	Revenue by geography
401 Commonwealth Drive Lobby B #02-02, Haw Par Technocentre Singapore, 149598 +65 64116900 www.xppower.com	
Management team	
CEO: Duncan Penny Duncan qualified as an accountant with Coopers & Lybrand and from 1980 to 1990 held a senior financial management position with LSI Logic and Dell Computer. He joined XP in 2000 as group FD. In February 2003, he was appointed as CEO.	CFO: Gavin Griggs Prior to joining the group in October 2017, Gavin was CFO of Alternative Networks, a listed Telecoms and IT services business until December 2016 when it was acquired by Daisy, whereupon he became FD of the larger group. Gavin has worked in various senior international finance positions including roles at Logica, SABMiller, PepsiCo and Sodexo.
Chairman: James Peters James has over 25 years' experience in the industry with Marconi and Coutant Lambda, before joining Powerline in 1980. In 1988, he founded XP Power. In 2000, he was appointed as European MD. In 2003, he was appointed deputy chairman and in 2014 became chairman.	
Principal shareholders	(%)
Standard Life Aberdeen	17.8
Canaccord Genuity	9.9
James Peters	8.0
Capital Group Companies	7.7
Mawer Investment Management	7.3
Janus Henderson	5.3
Old Mutual	3.5
Companies named in this report	
Advanced Energy Industries, COMET Holding, Cosel, Delta Electronics, TDK Corporation	

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