

# Avon Rubber

## Delivering growth

Avon Rubber's pre-close trading statement demonstrates the underlying growth in both divisions. Success continues to flow from the enhanced product portfolio and order progression is building visibility. We have made modest changes to our forecasts to reflect currency and the Merrick's acquisition.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
09/16	142.9	20.7	70.5	9.5	19.7	0.7
09/17	159.2	25.9	83.3	12.3	16.7	0.9
09/18e	160.8	26.5	74.2	16.0	18.7	1.2
09/19e	166.6	28.5	75.3	20.8	18.5	1.5

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

## Pre-close trading update

Avon's pre-close trading update reflects the strength in its protection markets, with expected full year divisional revenue growth of c 7% on a constant currency basis. This includes slightly higher than guidance deliveries of [M50 mask systems](#) to the US Department of Defense. While activity in the law enforcement area has continued to deliver growth, the fire business has continued to reflect the market softness seen in H118. milkrite I InterPuls has seen a step-up in performance in H218, particularly in North America, and is on track to deliver revenue growth of c 4% on a constant currency basis. In June, the company completed the acquisition of the distribution rights to Merrick's calf nurser product line for \$2.1m.

## Modest forecast adjustments

We have made modest adjustments to our model to reflect the better than expected dollar translation rate for FY18 and the acquisition of Merrick's. Looking forward, improved product mix and operational leverage should support operating margin growth in both divisions. For FY19, in the Protection division we reflect the substantial carry-over of 83,000 M50 mask systems plus future success with the M69 Joint Services Aircrew Mask and the M53A1 combined tactical mask and PAPR system. For milkrite I InterPuls, while the Merrick's acquisition is supportive, we maintain some caution as we keep a watch on feedstock pricing.

## Valuation: Premium justified

Taking an average of our DCF and our sum-of-the-parts valuations gives a fair value price of 1,499p vs 1,450p previously. This reflects the uplift in peer group multiples. On a FY18e P/E of 18.7x, the stock continues to trade at a premium to its UK aerospace and defence peer group. We feel this premium is justified given its exposure to the growing US defence budget environment and the heightened chemical, biological, radiological and nuclear (CBRN) global threat.

## Year-end trading statement

### Aerospace & defence

14 September 2018

Price **1,390.00p**

Market cap **£431m**

\$1.30/£1

Net cash (£m) at 31 March 2018 39.1

Shares in issue 31.0m

Free float 96%

Code AVON

Primary exchange LSE

Secondary exchange N/A

### Share price performance



% 1m 3m 12m

Abs 1.5 (4.8) 47.1

Rel (local) 5.8 0.5 47.8

52-week high/low 1475.0p 909.0p

### Business description

Avon Rubber designs, develops and manufactures product in the protection (70% of 2017 sales) and dairy (30%) sectors. Its major contracts are with national security and safety organisations such as the DoD. 75% of sales are from the US and 25% are from Europe.

### Next events

FY18 results 14 November 2018

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## Changes to financials

The following table outlines the changes to our forecasts.

<b>Exhibit 1: Revised forecasts</b>						
<b>£000s</b>	<b>2018e</b>			<b>2019e</b>		
	<b>Prior</b>	<b>New</b>	<b>% change</b>	<b>Prior</b>	<b>New</b>	<b>% change</b>
Avon Protection	108,702	110,898	2.0%	111,963	114,225	2.0%
milkrite I InterPuls	50,635	49,894	(1.5)%	53,167	52,389	(1.5)%
Total Sales	159,337	160,792	0.9%	165,130	166,614	0.9%
EBITDA	36,254	35,935	(0.9)%	38,373	38,324	(0.1)%
Avon Protection	20,436	20,405	(0.2)%	21,681	21,648	(0.2)%
milkrite I InterPuls	8,203	8,233	0.4%	9,145	9,011	(1.5)%
Unallocated	(2,000)	(2,000)	0.0%	(2,000)	(2,000)	0.0%
Underlying EBITA	26,639	26,638	0.0%	28,825	28,659	(0.6)%
Underlying PTP	26,464	26,453	0.0%	28,479	28,496	0.1%
EPS - underlying continuing (p)	74.3	74.7	0.5%	75.3	75.8	0.6%
DPS (p)	16.0	16.0	0.0%	20.8	20.8	0.0%
Net debt/(cash)	(49,703)	(46,173)	(7.1)%	(67,995)	(64,502)	(5.1)%

Source: Edison Investment Research

**Exhibit 2: Financial summary**

	£000s	2016	2017	2018e	2019e
Year end 30 September		IFRS	IFRS	IFRS	IFRS
<b>PROFIT &amp; LOSS</b>					
Revenue		142,884	159,200	160,792	166,614
Cost of Sales		(90,159)	(101,500)	(102,515)	(106,227)
Gross Profit		52,725	57,700	58,277	60,387
EBITDA		29,922	36,300	35,935	38,324
Operating Profit (before amort. and except.)		24,031	30,300	29,635	32,021
Intangible Amortisation		(3,154)	(4,200)	(2,997)	(3,362)
Exceptionals		(4,808)	(7,000)	(4,002)	(4,004)
Other		(33)	(35)	(36)	(38)
Operating Profit		16,036	19,065	22,600	24,617
Net Interest		(154)	(200)	(148)	(125)
Profit Before Tax (norm)		20,690	25,865	26,453	28,496
Profit Before Tax (FRS 3)		15,882	18,865	22,452	24,492
Tax		1,824	2,900	(3,148)	(4,661)
Profit After Tax (norm)		21,765	25,500	22,750	23,081
Profit After Tax (FRS 3)		17,706	21,765	19,303	19,831
Average Number of Shares Outstanding (m)		30.3	30.4	30.5	30.5
EPS - normalised (p)		70.5	83.3	74.2	75.3
EPS - (IFRS) (p)		58.5	71.5	63.4	65.1
Dividend per share (p)		9.5	12.3	16.0	20.8
Gross Margin (%)		36.9	36.2	36.2	36.2
EBITDA Margin (%)		20.9	22.8	22.3	23.0
Operating Margin (before GW and except.) (%)		16.8	19.0	18.4	19.2
<b>BALANCE SHEET</b>					
Fixed Assets		77,469	66,700	62,946	56,281
Intangible Assets		47,357	40,400	39,332	36,005
Tangible Assets		30,112	26,300	23,614	20,277
Investments		0	0	0	0
Current Assets		52,886	80,500	101,586	122,478
Stocks		20,648	21,800	22,511	23,559
Debtors		19,968	23,800	23,315	24,159
Cash		4,495	26,500	47,560	66,560
Other		7,775	8,400	8,200	8,200
Current Liabilities		(36,641)	(39,000)	(39,913)	(41,654)
Creditors		(34,142)	(37,200)	(38,525)	(39,595)
Short term borrowings		(2,499)	(1,800)	(1,387)	(2,059)
Long Term Liabilities		(51,713)	(52,600)	(52,558)	(52,516)
Long term borrowings		0	0	0	0
Other long term liabilities		(51,713)	(52,600)	(52,558)	(52,516)
Net Assets		42,001	55,600	72,062	84,590
<b>CASH FLOW</b>					
Operating Cash Flow		30,504	29,754	34,490	35,504
Net Interest		(147)	(154)	(200)	(148)
Tax		(17)	2,900	(3,148)	(4,661)
Capex		(6,838)	(5,500)	(8,943)	(6,001)
Acquisitions/disposals		(3,300)	0	4,400	0
Financing		(1,812)	(1,000)	(1,000)	(1,000)
Dividends		(2,430)	(3,200)	(4,126)	(5,366)
Other		(803)	(96)	0	0
Net Cash Flow		15,157	22,704	21,473	18,328
Opening net debt/(cash)		13,161	(1,996)	(24,700)	(46,173)
HP finance leases initiated		0	0	0	0
Other		0	0	0	0
Closing net debt/(cash)		(1,996)	(24,700)	(46,173)	(64,502)

Source: Company reports, Edison Investment Research

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