

Treatt

FY18 results

A more normal year

Treatt has reported yet another set of strong results in FY18. The company remains in the sweet spot of current consumer trends, with ingredients that help to deliver better-for-you products with clean labels and without compromising on taste. The US expansion is on track and on budget, and will be fully operational in H119. The UK relocation is progressing well, although it is more complex and the timetable has slipped by about six months. FY19 has started well, and at this stage we leave our estimates broadly unchanged. Our DCF-derived fair value remains 510p.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
09/17	101.3	12.8	18.5	4.8	22.7	1.1
09/18	112.2	13.8	20.3	5.1	20.7	1.2
09/19e	116.1	14.2	19.1	5.1	22.0	1.2
09/20e	120.7	14.8	20.0	5.3	21.1	1.3

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

Expansion continues

The strong growth over the last few years caused a need for an expansion of capacity at Treatt's US facility. The increase will be substantial, adding over 80% of prior capacity, and the project has so far been delivered on time and on budget, which is testament to management's disciplined approach. The UK relocation is more significant and more complex. The design phase has taken longer than expected, hence the slippage in the timetable. We note the overall cost has crept up over time, but this is in part due to management's decision rightly to hold back capital investment at the old facility, hence there is a degree of catch-up on the new facility.

Pricing pressure weighs on margins

Increased raw material costs and some pricing pressure on new business wins resulted in gross margins falling c 20bp in FY18. Adverse FX movements were also unhelpful. As expected, a large increase in working capital is attributable to timing issues and increased costs, but also to longer payment terms with a number of larger customers. Following the equity raise in November 2017, the balance sheet remains well-funded with a net cash position of £10.1m at end September 2018.

Valuation: fair value of 510p

We value Treatt using a DCF model, which indicates a fair value of 510p (unchanged). Treatt trades at 22.0 FY19e P/E and 16.9x FY19e EV/EBITDA. On P/E it trades at a c 20% discount to its peer group, and on EV/EBITDA it is at a c 5% discount.

Food & beverages

4 December 2018

Price **421.00p**
Market cap **£246m**

Net cash (£m) at 30 September 2018 10.1

Shares in issue 58.4m

Free float 100%

Code TET

Primary exchange LSE

Secondary exchange N/A

Share price performance



%	1m	3m	12m
Abs	(7.3)	(13.6)	(14.1)
Rel (local)	(6.3)	(7.4)	(10.6)

52-week high/low 508.0p 397.0p

Business description

Treatt provides innovative ingredient solutions from its manufacturing bases in Europe, North America and Africa, principally for the flavours and fragrance industries and multinational consumer goods companies, with particular emphasis on the beverage sector.

Next events

Q3 trading update March 2019

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FY results

FY18 results were broadly in line with our expectations. Following our slight [downgrade](#) in October with the pre-close trading update, our sales forecast was £110.5m and FY revenues came in slightly higher at £112.2m. Adjusted PBT was £12.6m, vs our £12.5m forecast, or 8% growth vs FY17. Adjusted EPS (on an IFRS basis) was up c 10% to 18.0p. We illustrate the slight changes to our P&L forecasts in Exhibit 1 below.

Exhibit 1: Old vs new key P&L forecasts

	2018			2019e			2020e		
	Forecast	Actual	Diff	Old	New	Diff	Old	New	Diff
Revenue	110,545	112,163	1.5%	116,073	116,089	0.0%	120,715	120,732	0.0%
PBT*	12,479	12,642	1.3%	13,122	13,088	-0.3%	13,631	13,667	0.3%
Basic EPS*	15.7	18.0	14.5%	16.5	17.2	3.8%	17.2	17.9	4.4%

Source: Edison Investment Research. Note: *Stated on IFRS basis.

Valuation

We illustrate Treatt's relative valuation versus its ingredients peer group in Exhibit below. Treatt trades at a discount to its peer group on a P/E basis, and broadly in line on an EV/EBITDA basis. We believe some discount is justified to reflect its small size and because some of its products are relatively 'upstream' in the ingredients spectrum, particularly the bulk ingredients that are sold to other ingredients companies.

Exhibit 2: Comparative valuation

	Market cap (m)	P/E (x)		EV/EBITDA (x)		Dividend yield (%)	
		2019e	2020e	2019e	2020e	2019e	2020e
Givaudan	CHF 22,477	29.3	26.1	20.2	17.8	2.5	2.6
IFF	\$15,118	23.1	23.0	16.4	11.7	2.0	2.0
Symrise	CHF 9,316	33.2	28.9	17.3	15.7	1.3	1.4
Chr Hansen	DKK 77,229	39.6	35.0	25.9	23.3	0.3	0.3
Kerry	€ 15,709	25.6	23.2	18.2	16.7	0.8	0.8
Ingredion	\$7,434	15.2	13.9	8.6	8.3	2.3	2.3
Peer group average		27.7	25.0	17.8	15.6	1.5	1.6
Treatt	239.0	22.0	21.1	16.9	14.3	1.2	1.3
Premium/(discount) to peer group (%)		(20.3%)	(15.7%)	(4.9%)	(8.5%)	(19.7%)	(20.2%)

Source: I/B/E/S (prices as of 27 November 2018).

Our DCF-derived fair value is unchanged at 510p as our forecast changes are minor. Our longer-term sales growth forecast remains at 5.0% pa, falling to 2% growth in perpetuity. Our DCF is calculated based on a WACC of 6.8% (encompassing a beta of 0.8, an equity risk premium of 5.0% and a borrowing spread of 5.0%) and a terminal growth rate of 2%.

Exhibit 3: Financial summary

	£000's	2015	2016	2017	2018	2019e	2020e
Year end September		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS							
Revenue		85,934	88,040	101,250	112,163	116,089	120,732
Cost of Sales		(66,955)	(67,639)	(75,985)	(84,407)	(88,058)	(91,339)
Gross Profit		18,979	20,401	25,265	27,756	28,031	29,394
EBITDA		10,307	11,604	15,049	16,627	15,837	18,617
Operating Profit (before amort., except and sbp.)		9,063	10,257	13,650	15,108	14,135	14,946
Intangible Amortisation		(175)	(142)	(137)	(124)	0	0
Share based payments		(198)	(566)	(966)	(1,040)	(1,096)	(1,144)
Other		0	0	0	0	0	0
Operating Profit		8,690	9,549	12,547	13,944	13,039	13,802
Net Interest		(740)	(703)	(851)	(1,302)	49	(135)
Exceptionals		(174)	(553)	0	(1,105)	0	0
Profit Before Tax (norm)		8,323	9,554	12,799	13,806	14,184	14,811
Profit Before Tax (FRS 3)		7,776	8,293	11,696	11,537	13,088	13,667
Profit Before Tax (company)		7,950	8,846	11,696	12,642	13,088	13,667
Tax		(1,786)	(2,144)	(3,129)	(2,284)	(3,337)	(3,485)
Profit After Tax (norm)		6,537	7,410	9,670	11,522	10,846	11,326
Profit After Tax (FRS 3)		5,990	6,149	8,567	9,253	9,750	10,182
Discontinued operations					2,976		
Average Number of Shares Outstanding (m)		51.5	51.9	52.2	56.8	56.8	56.8
EPS - normalised (p)		12.7	14.3	18.5	20.3	19.1	20.0
EPS - normalised & fully diluted (p)		12.6	14.1	17.9	19.8	18.6	19.4
EPS - (IFRS) (p)		11.6	11.8	16.4	21.5	17.2	17.9
Dividend per share (p)		4.0	4.4	4.8	5.1	5.1	5.3
Gross Margin (%)		22.1	23.2	25.0	24.7	24.1	24.3
EBITDA Margin (%)		12.0	13.2	14.9	14.8	13.6	15.4
Operating Margin (before GW and except.) (%)		10.5	11.7	13.5	13.5	12.2	12.4
BALANCE SHEET							
Fixed Assets		13,381	16,161	19,532	21,863	43,321	54,462
Intangible Assets		1,736	3,364	3,331	752	752	752
Tangible Assets		10,998	11,361	14,821	20,038	41,496	52,637
Investments		647	1,436	1,380	1,073	1,073	1,073
Current Assets		45,045	54,435	68,230	102,401	102,706	105,039
Stocks		25,799	29,990	42,878	39,642	40,797	42,188
Debtors		17,635	17,853	19,973	28,828	29,605	30,548
Cash		1,477	6,588	4,748	32,304	32,304	32,304
Other		134	4	631	1,627	0	0
Current Liabilities		(13,481)	(16,388)	(27,003)	(35,781)	(40,258)	(43,773)
Creditors		(12,675)	(15,834)	(19,266)	(16,479)	(16,611)	(16,672)
Short term borrowings		(567)	(487)	(7,680)	(19,244)	(23,647)	(27,101)
Provisions		(239)	(67)	(57)	(58)	0	0
Long Term Liabilities		(11,760)	(17,021)	(14,281)	(6,858)	(16,480)	(18,008)
Long term borrowings		(7,065)	(7,755)	(7,293)	(3,001)	(11,823)	(13,551)
Other long term liabilities		(4,695)	(9,266)	(6,988)	(3,857)	(4,657)	(4,457)
Net Assets		33,185	37,187	46,478	81,625	89,289	97,720
CASH FLOW							
Operating Cash Flow		8,667	10,804	4,683	3,580	15,019	16,144
Net Interest		(740)	(703)	(913)	(609)	49	(135)
Tax		(1,469)	(2,022)	(2,822)	(2,978)	(3,337)	(3,485)
Capex		(924)	(679)	(5,111)	(6,190)	(23,161)	(14,811)
Acquisitions/disposals		(103)	(861)	(1,667)	8,357	1,100	0
Financing		147	280	270	21,090	0	0
Dividends		(1,978)	(2,095)	(3,025)	(2,876)	(2,895)	(2,895)
Net Cash Flow		3,600	4,724	(8,585)	20,374	(13,225)	(5,181)
Opening net debt/(cash)		9,584	6,155	1,654	10,225	(10,059)	3,166
HP finance leases initiated		0	0	0	0	0	0
Other		(171)	(223)	14	(90)	1	0
Closing net debt/(cash)		6,155	1,654	10,225	(10,059)	3,166	8,348

Source: Company data, Edison Investment Research

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