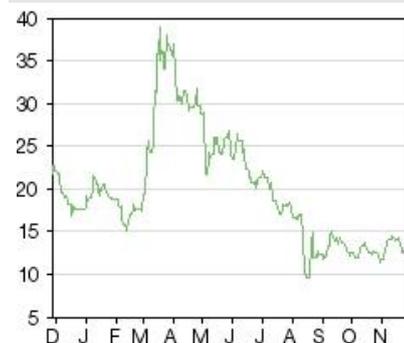


27 November 2019

**Price** €12.54  
**Market cap** €56m

Net debt (€m) at 30 September 2019	134.5
Shares in issue	4.5m
Free float	50%
Code	PGN
Primary exchange	Frankfurt (Xetra)
Secondary exchange	N/A

**Share price performance**


%	1m	3m	12m
Abs	5.0	9.5	(45.9)
Rel (local)	2.2	(3.6)	(53.6)
52-week high/low	€39.00	€9.62	

**Business description**

paragon designs and supplies automotive electronics and solutions, selling directly to OEMs, including sensors, interior, digital assistance and body kinematics. Production facilities are in Germany, the US and China. It retains 60% of Voltabox, which supplies battery power systems.

**Next events**

FY19 results	March 2020
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While Q319 results confirm the anticipated issues in Electromobility (Voltabox), with a more robust performance from the automotive segments (Electronics and Mechanics), there are signs that management is addressing the shortcomings. Indeed, some more positive elements are evident at this early stage, notably the trade receivables reduction as planned. A more prudent view of growth with stronger profitability and positive cash flow is indicated by initial FY20 guidance. The challenge now is to rebuild confidence in the investment, with a focus on reducing costs, improving operational performance and executing to plan.

Year end	Revenue (€m)	PBT* (€m)	EPS* (€)	DPS (€)	P/E (x)	Yield (%)
12/17	124.8	5.9	(0.09)	0.25	N/A	2.0
12/18	187.4	14.8	1.45	0.25	8.6	2.0
12/19e	200.1	(5.3)	(0.43)	0.25	N/A	2.0
12/20e	233.4	9.5	1.39	0.25	9.0	2.0

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

**Q3 trading**

The Electronics and Mechanics segments continued to deliver robust Q319 revenue performance and an improved EBITDA. The Electromobility segment suffered the anticipated shortfall in sales and profits arising from the production delays caused by supply chain issues in the period and the deferral of a major new contract. Encouragingly, the situation has not deteriorated further. In addition, the cash performance appears to be in line with management's plan, with the large trade receivable from Triathlon being settled as scheduled, and the major benefits of destocking yet to be realised progressively into FY20.

**Expectations for profitable growth in FY20**

The Q319 report also gave the first view of management expectations for FY20. Voltabox has adopted a more rigorous and prudent approach to its forecasting methodology aided by external consultants. We feel this is reflected in FY20 guidance commentary. With management cost reduction initiatives already in train, Voltabox is indicating revenues of €85–100m with EBITDA margins of 15% and an EBIT margin of 5–7%. Both margins are ahead of our estimates. For the group as a whole, management expects FY20 revenues of €225–240m, with EBITDA of €34–39m (EBITDA margin of 15–16%) and EBIT of €12–17m (EBIT margin of 5–7%). Again, our earnings estimates are below guidance, so if management can execute to plan there is upside potential.

**Valuation: An encouraging start to rebuilding**

The encouraging FY20 outlook and the stabilisation of cash flow in H219 provide initial encouragement. However, the test will come as FY20 progresses where delivery of the more rigorously developed plan is essential to allow the rating to recover, rebase and reset the growth path and deliver improving cash flows. The FY20 P/E of 9.0x on our below-guidance estimate appears undemanding.

## Q319 results

The Automotive-facing businesses have not been the main support for the growth story, but both the Electronics and Mechanics segments provide a solid backbone in the face of a still challenging market backdrop. Both grew revenues in Q319, by 17% and 43%, respectively, meaning for the nine months to date Automotive sales were up 24% to €30.9m (FY18: €24.9m) with both segments contributing to the growth. The gross profit contribution in Q319 rose 18% to €16.4m (Q318: €13.9m), although gross margin fell 290bp to 53.0%. The combined Automotive Q319 EBITDA contribution improved 16% to €3.34m (Q318: €2.89m).

In stark contrast Electromobility (Voltabox) saw revenues drop by over 60% in Q319. The performance had already been foreshadowed by the change to guidance in August, with significant disruption to Voltabox production and deliveries in Europe arising from the battery cell supply issue and the US business falling victim to deferral of orders. Costs and resources had been built in anticipation of higher sales levels, and in Europe as production stoppages were required, there was overhead under recovery, which drove a €5.8m Q319 EBITDA loss (Q318: €3.3m profit). Although management has already initiated cost efficiency programmes, these had little effect in the period.

Overall Q319 group revenues fell 9% to €36.6m (Q318: €40.2m), generating an EBITDA loss of €2.9m (Q318: €6.1m). Again, management cost and efficiency initiatives across the segments should show progressive benefit through the remainder of the year and in FY20.

### Exhibit 1: paragon Q319 analysis

€m	Q318	Comprised of		Q319	Comprised of		% change		
	paragon	Voltabox	Automotive	paragon	Voltabox	Automotive	paragon	Voltabox	Automotive
<b>Revenues</b>									
- Sensors	8.1		8.1	8.1		8.1	-0.4%		-0.4%
- Interior	9.9		9.9	11.9		11.9	19.7%		19.7%
- Digital Assistance	0.0		0.0	1.2		1.2			
<b>Electronics</b>	<b>18.1</b>		<b>18.1</b>	<b>21.2</b>		<b>21.2</b>	<b>17.3%</b>		<b>17.3%</b>
<b>Mechanics</b>	<b>6.8</b>		<b>6.8</b>	<b>9.7</b>		<b>9.7</b>	<b>42.5%</b>		<b>42.5%</b>
- Voltabox Germany	13.7	13.7		4.6	4.6		-66.5%	-66.5%	
- Voltabox of Texas (US)	1.7	1.7		1.1	1.1		-31.0%	-31.0%	
<b>Electromobility</b>	<b>15.3</b>	<b>15.3</b>		<b>5.7</b>	<b>5.7</b>		<b>-62.7%</b>	<b>-62.7%</b>	
<b>Total group revenues</b>	<b>40.2</b>	<b>15.3</b>	<b>24.9</b>	<b>36.6</b>	<b>5.7</b>	<b>30.9</b>	<b>-9.0%</b>	<b>-62.7%</b>	<b>24.2%</b>
<b>Gross profit</b>	<b>25.3</b>	<b>11.4</b>	<b>13.9</b>	<b>17.4</b>	<b>1.1</b>	<b>16.4</b>	<b>-31.1%</b>	<b>-90.5%</b>	<b>17.7%</b>
Gross margin	63.0%	74.5%	55.9%	47.6%	18.9%	53.0%	-24.4%	-74.6%	-5.2%
<b>EBITDA</b>	<b>6.1</b>	<b>3.3</b>	<b>2.9</b>	<b>(2.9)</b>	<b>(5.8)</b>	<b>3.0</b>	<b>-146.4%</b>	<b>-279.4%</b>	<b>3.3%</b>
EBITDA margin	15.3%	21.2%	11.6%	-7.8%	-101.9%	9.6%			
Electronics	1.7		1.7	(1.7)		(1.7)			
Mechanics	(0.4)		(0.4)	0.8		(0.7)			
Electromobility	2.2	2.2		(7.7)	(7.7)				
Eliminations	(0.7)		(0.7)	(0.1)		1.5			
<b>EBIT</b>	<b>2.9</b>	<b>2.2</b>	<b>0.6</b>	<b>(8.7)</b>	<b>(7.7)</b>	<b>(1.0)</b>			
<b>PBT</b>	<b>1.9</b>	<b>2.2</b>	<b>(0.3)</b>	<b>(10.2)</b>	<b>(7.9)</b>	<b>(2.3)</b>			
EPS (€)	0.07			(1.11)					
<b>FCF</b>	<b>(16.8)</b>	<b>(18.3)</b>	<b>1.5</b>	<b>(3.6)</b>	<b>(0.9)</b>	<b>(2.8)</b>			

Source: paragon reports

Probably the most encouraging factor was in cash performance, where the free cash outflow of €3.6m in Q319 was significantly improved versus both the prior year (outflow of €16.8m) and H119 despite continued inventory build. Voltabox's c€45m trade receivable outstanding at Triathlon has started to be paid to schedule and was reflected in a significant fall in overall trade receivables during the quarter ending the period at €50.7m compared to €83.5m at H119. Most of the outstanding amount should flow back to the group in Q419 and inventory levels should start to reduce as manufactured stock items are deployed to amenable customers with good pricing.

Overall company defined net debt increased by €11.2m in Q319, as other available liquidity pools reduced by €8.6m. On our standard definition (gross debt less gross cash), net debt rose just €2.6m in Q319 compared to a €63.2m H119 increase, ending the period at €134.5m (H119: €132.0m).

Management guidance for FY19 remains unchanged (see our [note](#) published in October).

<b>Exhibit 2: Liquidity analysis</b>									
€m	FY18			H119			Q319		
	paragon	Voltabox	Automotive	paragon	Voltabox	Automotive	paragon	Voltabox	Automotive
Gross cash	41.8	28.2	13.6	10.1	4.2	5.9	5.6	3.4	2.2
Gross debt	(110.6)	(3.7)	(106.9)	(142.0)	(18.7)	(123.3)	(140.1)	(18.9)	(121.2)
<b>Net debt (Edison definition)</b>	<b>(68.8)</b>	<b>24.5</b>	<b>(93.3)</b>	<b>(132.0)</b>	<b>(14.6)</b>	<b>(117.4)</b>	<b>(134.5)</b>	<b>(15.5)</b>	<b>(119.0)</b>
Other liquidity	7.1	0.0	7.1	21.4	14.4	7.0	12.8	7.5	5.3
<b>Net debt (company defined)</b>	<b>(61.7)</b>	<b>24.5</b>	<b>(86.2)</b>	<b>(110.6)</b>	<b>(0.1)</b>	<b>(110.4)</b>	<b>(121.7)</b>	<b>(7.999)</b>	<b>(113.7)</b>
<b>Change (€m)</b>									
Gross cash				(31.8)	(24.0)	(7.7)	(4.5)	(0.8)	(3.7)
<b>Net debt (Edison definition)</b>				<b>(63.2)</b>	<b>(39.1)</b>	<b>(24.1)</b>	<b>(2.6)</b>	<b>(0.9)</b>	<b>(1.6)</b>
Other liquidity				14.3	14.4	(0.1)	(8.6)	(6.9)	(1.7)
<b>Net debt (company defined)</b>				<b>(48.9)</b>	<b>(24.6)</b>	<b>(24.2)</b>	<b>(11.2)</b>	<b>(7.9)</b>	<b>(3.3)</b>

Source: paragon reports

## Guidance for FY20

The managements of both Voltabox and paragon have for the first time indicated expectations for FY20.

For Voltabox:

- Revenues of between €85m and €100m – Edison estimate €91.3m.
- EBITDA margin of 15% – Edison estimate 13.0%.
- EBIT margin of 5–7% – Edison estimate 2.2%.
- Free cash inflow between €0 and €10m.
- Investment of €12.5m, of which c 70% should be own work capitalised (development costs).

For the group as a whole:

- Revenues of between €225m and €240m – Edison estimate €233.4m.
- EBITDA of €34–39m – Edison estimate €31.9m. Guided EBITDA margin of 15–16% – Edison estimate 13.7%.
- EBIT of €12–17m – Edison estimate €12.7m. Guided EBIT margin of 5–7% – Edison estimate 5.4%.
- Free cash inflow between €0 and €10m.
- Investment of €32.5m, of which c 60% should be own work capitalised (development costs).

While our revenue expectations appear aligned with the guidance, we feel our earnings estimates currently err on the cautious side. If indeed the new planning approach by management does prove to be more conservative, our estimates could prove to be unduly so.

**Exhibit 3: Financial summary**

	€m	2017	2018	2019e	2020e
Year end 31 December		IFRS	IFRS	IFRS	IFRS
<b>PROFIT &amp; LOSS</b>					
Revenue		124.8	187.4	200.1	233.4
Cost of Sales		(72.4)	(96.7)	(116.1)	(116.7)
Gross Profit		52.5	90.7	84.1	116.7
EBITDA		18.3	30.3	13.6	31.9
Operating Profit (before amort. and except.)		13.3	23.4	5.6	22.9
Intangible Amortisation		(3.0)	(4.3)	(5.0)	(6.2)
Exceptionals		(4.9)	(4.2)	(4.0)	(4.0)
Other		0.0	0.0	0.0	0.0
Operating Profit		5.4	14.8	(3.4)	12.7
Net Interest		(4.4)	(4.2)	(5.9)	(7.1)
Profit Before Tax (norm)		5.9	14.8	(5.3)	9.5
Profit Before Tax (FRS 3)		1.0	10.6	(9.3)	5.5
Tax		(5.0)	(7.2)	2.5	(1.5)
Profit After Tax (norm)		(0.4)	7.6	(3.9)	6.9
Profit After Tax (FRS 3)		(4.0)	3.4	(6.8)	4.0
Average Number of Shares Outstanding (m)		4.5	4.5	4.5	4.5
EPS - normalised (€)		(0.09)	1.45	(0.43)	1.39
EPS - normalised fully diluted (€)		(0.09)	1.45	(0.43)	1.39
EPS - (IFRS) (€)		(0.30)	0.52	(1.07)	0.76
Dividend per share (€)		0.25	0.25	0.25	0.25
Gross Margin (%)		42.0	48.4	42.0	50.0
EBITDA Margin (%)		14.7	16.2	6.8	13.7
Operating Margin (before GW and except.) (%)		10.7	12.5	2.8	9.8
<b>BALANCE SHEET</b>					
Fixed Assets		104.1	172.9	196.0	216.9
Intangible Assets		67.4	122.1	131.2	138.9
Tangible Assets		36.4	50.5	64.5	77.7
Investments		0.3	0.3	0.3	0.3
Current Assets		203.8	189.4	181.7	186.6
Stocks		17.3	58.9	66.0	65.4
Debtors		32.7	70.7	70.1	72.4
Cash		145.8	41.8	21.8	21.8
Other		8.0	17.9	23.7	27.1
Current Liabilities		(46.4)	(84.4)	(39.6)	(42.8)
Creditors		(27.4)	(42.2)	(39.6)	(42.8)
Short term borrowings		(19.0)	(42.2)	0.0	0.0
Long Term Liabilities		(70.2)	(71.7)	(140.4)	(159.8)
Long term borrowings		(67.3)	(68.4)	(136.5)	(156.2)
Other long term liabilities		(2.8)	(3.3)	(4.0)	(3.6)
Net Assets		191.4	206.2	197.6	200.9
<b>CASH FLOW</b>					
Operating Cash Flow		0.8	(42.0)	(0.2)	31.2
Net Interest		(4.4)	(4.2)	(5.9)	(7.1)
Tax		(6.3)	(7.2)	1.4	(2.6)
Capex		(21.8)	(48.8)	(40.1)	(40.1)
Acquisitions/disposals		(15.9)	(26.3)	0.0	0.0
Financing		143.2	1.5	0.0	0.0
Dividends		(1.1)	(1.1)	(1.1)	(1.1)
Net Cash Flow		94.4	(128.3)	(45.8)	(19.8)
Opening net debt/(cash)		34.9	(59.5)	68.8	114.6
HP finance leases initiated		0.0	0.0	0.0	0.0
Other		0.0	0.0	0.0	0.0
Closing net debt/(cash)		(59.5)	68.8	114.6	134.4

Source: Company reports, Edison Investment Research estimates

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