Kendrion

FY22 results review

Preparing for stronger growth in Automotive

Industrial engineering

Kendrion performed well in FY22 despite the difficult market conditions, such as delayed deliveries of raw materials, inflationary pressures and volatile demand. Organic revenue growth was 8% but margins were lower due to higher input prices and engineering costs. The energy transition will drive growth and higher margins at Kendrion over the next few years, bringing it close to its 2025 financial targets (average organic revenue growth of 5% and an EBITDA margin of >15%). The unweighted average of our three valuation methods points to a fair value of €22.8 per share.

Year end	Revenue (€m)	EBITDA* (€m)	EPS* (€)	DPS (€)	EV/EBITDA (x)	P/E (x)
12/21	463.6	55.8	1.39	0.69	8.2	15.1
12/22	519.3	57.4	1.45	0.72	6.7	10.7
12/23e	552.5	68.3	1.67	0.83	5.6	9.5
12/24e	593.6	80.4	2.23	1.11	4.5	7.1

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

Industrial still going strong, Automotive in recovery

Organic revenue growth of 11% y-o-y in Q422 was better than expected with a strong recovery in Automotive (14%) and continued good growth in Industrial (7%). Group EBITDA in the quarter was up 4% y-o-y and margins were affected by higher input prices and higher engineering costs in preparation for the ramp up of new projects in 2023. As announced on 8 February, the company took an impairment of goodwill and other intangible assets of €57.3m related to the combustion engine activities. The impairment is non-cash and has no impact on the liquidity position and the operational performance of Kendrion. The company's financial position remains solid with net debt/EBITDA at 2.4x, well within the covenant of <3.25x.

Positive outlook supported by energy transition

For FY23, Kendrion expects the uncertain economic environment to continue in H123 with potentially better economic circumstances in H223, which is based on the expectation that China's economy will benefit from the end of the strict zero-COVID policy. Energy transition and accelerating electrification will drive revenue growth and higher margins over the next few years. In 2023, the company will start production of nine new projects in Automotive E (electric vehicles related). We have slightly raised our revenue estimates for FY23–24 but hardly changed our EBITDA estimates: we expect sales growth of 6–8% and a 250bp improvement in the EBITDA margin to 13.6%, mainly driven by operating leverage and cost savings.

Valuation: Ample upside

Kendrion is valued at a 17% discount to peers based on 2023e EV/EBITDA, which could gradually diminish over time as the company demonstrates accelerating growth and higher profitability. We value Kendrion based on three different methods: historical multiples, discounted cash flow and peer comparison. On broadly unchanged estimates and assumptions, the average of these methods now points at a value of €22.8 per share (versus €22.2 previously).

2 March 2023

Price	**€15.92**
Market cap	**€240m**

Net debt (€m) at 31 December 2022	140
Shares in issue	15.1m
Free float	43%
Code	KENDR
Primary exchange	Euronext Amsterdam
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(4.6)	(1.7)	(17.6)
Rel (local)	(4.8)	(4.0)	(21.6)
52-week high/low		€20.25	€13.02

Business description

Kendrion develops, manufactures and markets high-quality actuator products for industrial applications (53% of revenues) and automotive (47%). The geographical spread of FY22 revenues is Europe 68%, the Americas 17% and Asia 15%.

Next events

Q123 results	9 May 2023

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Edison profile page

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FY22 results: Better-than-expected revenue growth

Kendrion performed well in FY22 despite the difficult market conditions, such as a volatile economy, delayed deliveries of raw materials, geopolitical instability and inflationary pressures. Revenues were better than we expected, with growth of 12% y-o-y to €519m (Edison estimate was €515.5m). Acquired 3T (industrial control technology) contributed 2% to FY22 growth and currencies also had a positive impact of 2%. In Q422, revenue growth was also 12% y-o-y with a positive currency impact of 1% and no further acquisition effect from 3T, as it was acquired in September 2021.

Exhibit 1: Kendrion results

€m	Q421	Q422	Change	FY21	FY22	Change
Industrial	62.9	68.0	8%	231.5	276.5	19%
Automotive	53.3	61.6	16%	232.5	242.8	4%
Total revenues normalised	**116.2**	**129.6**	**12%**	**464.0**	**519.3**	**12%**
Industrial	28%	7%		20%	13%	
Automotive	-6%	14%		13%	2%	
Total organic revenue growth	**9%**	**11%**		**16%**	**8%**	
Industrial	N/A	N/A		39.0	47.5	22%
Automotive	N/A	N/A		16.8	9.9	-41%
Total EBITDA normalised	**11.5**	**12.0**	**4%**	**55.8**	**57.4**	**3%**
Industrial	N/A	N/A		16.8%	17.2%	
Automotive	N/A	N/A		7.2%	4.1%	
Total EBITDA margin	**10.0%**	**9.3%**		**12.0%**	**11.1%**	
Exceptionals	(0.4)	(1.3)		(0.8)	(5.3)	
Impairment	(3.3)	(58.7)		(3.3)	(58.7)	
EBIT reported	1.0	(55.2)	N/A	23.9	(34.6)	N/A
Net profit reported	0.3	(59.1)	N/A	14.4	(46.3)	N/A
Net profit normalised	**4.1**	**2.7**	**-34%**	**20.6**	**21.7**	**5%**
EPS reported (€)	0.02	(3.91)	N/A	0.97	(3.09)	N/A
EPS normalised (€)	0.27	0.18	-35%	1.39	1.45	4%

Source: Kendrion, Edison Investment Research

Despite all the market challenges, organic revenue growth in FY22 was a solid 8% y-o-y, with an acceleration to 11% y-o-y in the last quarter. To cope with input pressure, Kendrion has raised its prices by 5% on average. The building blocks for organic revenue growth in Q422 were different compared to the previous three quarters in the year. Whereas Industrial (53% of FY22 revenues) was the driver for growth in 9M22, it was a recovery in Automotive (47% of FY22 revenues) that caused the better-than-expected revenue growth in Q4. Please note that Q421 was a very strong quarter for Industrial thus the comparison base was relatively tough.

Industrial showed strong revenue growth of 19% in FY22, with organic growth of 13%, driven by high demand for actuators for electrification applications. Growth slowed to 7% in Q422, but the comparison base was strong (+28% growth in Q421). Industrial Brakes (29% of total revenues) continued strong growth of 19% y-o-y in FY22, with organic growth of 17%, driven by high demand for electromotors and electrified solutions for intralogistics, robotics and wind power, as well as adding new customers such as Hilti and Nord. Industrial Actuators and Controls (IAC, 24% of revenues) also showed high growth of 21%, of which 9% came from 3T. Organic growth of 11% was driven by higher demand for rotary solenoids for logistics, rotary locks for washing machines and fluid control valves for beverage makers and high demand for inductive heating solutions.

Automotive showed a clear improvement during 2022, with an organic revenue decline of 4% in H122 but ending the year with 2% growth and a strong recovery of 14% in Q422. Car production in Europe was up 5% in Q422 but down 1% in FY22 (source: S&P Global). Kendrion is outperforming the market, fuelled by the ramping up of orders won in previous years. As communicated on 8 February 2023, Kendrion has completed the split of its Automotive activities into 'E' and 'Core', which it announced at its capital markets day in September 2022 (with both full P&L responsibility).

Core focuses on operational excellence and cash flows and manufactures products that are related to the combustion engine. E is focused on innovation and growth to benefit from the strong growth in electric vehicles. In FY22, Core realised revenues of €180m and E had revenues of €63m.

Kendrion's operations in China (one of its strategic growth areas) felt the impact of the zero-COVID policy and as a result FY22 revenues ended up equal to last year. Kendrion is constructing a new factory, which will double capacity towards 28,000 square metres. Kendrion expects the new facility to be finalised in Q123 and fully operational in Q323 after a period of testing and moving activities from the current two locations to the new one (this reflects only a small delay of about one quarter versus previous plans). Kendrion expects to start six new Automotive E projects in China in H223.

Normalised EBITDA in FY22 increased a bit slower than we expected with 3% y-o-y growth to €57.4m, reflecting a 90bp lower margin at 11.1%. According to Kendrion, the 5% revenue growth due to increased average sales prices to offset inflationary pressure on costs had a negative impact on EBITDA margin of 0.5%. Other reasons for the decline were higher energy costs and higher developments costs in Automotive for the preparation of new projects in 2023. The EBITDA margin in Industrial increased 40bp to 17.2%, while the margin in Automotive was 310bp lower at 4.1%.

The reported EBIT loss of €34.6m was affected by one-off restructuring costs (mainly related to reorganisations within automotive) and an impairment of goodwill and other intangible assets of €57.3m as well as a €1.2m deferred asset write-down related to Automotive Core. This was announced on 8 February 2023 and was based on the expectation that the combustion engine will phase out over the next 10–15 years, combined with the increased interest rates.

Normalised free cash flow was stable at €3.1m, thereby absorbing €10m higher capex (mainly due to investments in the facility in China) and higher working capital due to the higher activity level.

Net debt increased from €130.6m in FY21 to €140.3m in FY22, mainly due to the cash part of the dividend of €7m and the €10m higher capex. In line with the company's expectation at the Q322 results last November, inventories and trade receivables were lower at year-end, resulting in a decline in net debt of €13m versus Q322 (free cash flow in Q4 was a solid €16.7m). Net debt/EBITDA was stable at 2.4x and is well within the covenant of below 3.25x.

Positive long-term outlook

For FY23, Kendrion expects the uncertain economic environment to continue in the first half of the year with potentially better economic circumstances in the second half, based on the expectation that China's economy will benefit from the end of the strict zero-COVID policy. Based on its product and project pipeline in Industrial, Kendrion expects further growth in these activities, despite the strong comparison base. In FY23, Kendrion again will compensate for the input pressure by raising its prices. During the analyst call, management commented to expect inflation to decline, which should result in price increases below the 5% achieved in FY22. The energy transition will drive revenue growth and higher profitability for Kendrion over the next few years.

Exhibit 2: Kendrion Automotive nominations

Automotive nominations 2018 - 2022

	Total	Average per year	Revenue 2022	Book/bill average
E	683	137	63	2.2
Core*	817	163	180	0.9

** Adjusted for net effect of cancellations and extensions of legacy revenue*

Source: Kendrion FY22 presentation

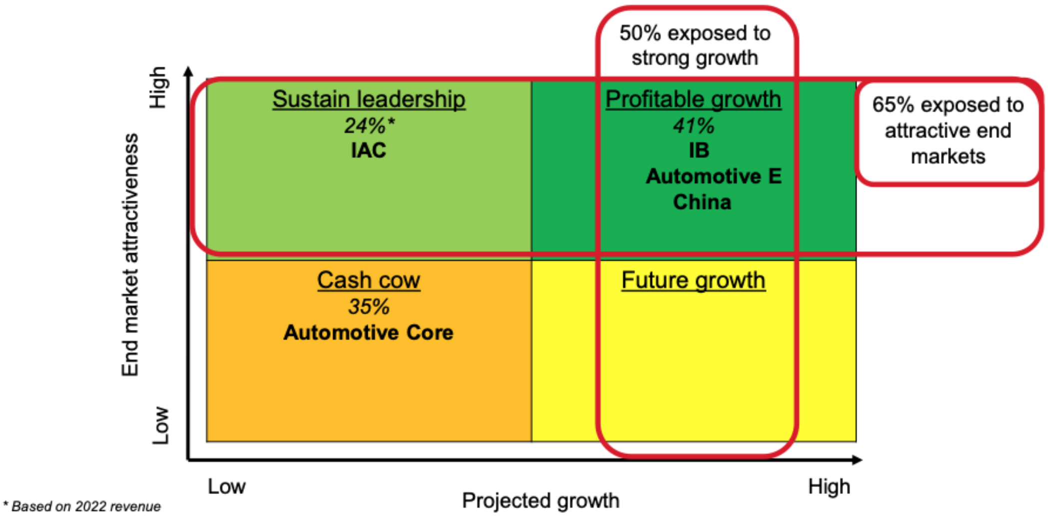
Kendrion won new orders in Automotive worth €305m in FY22, including €207m related to Automotive E. Exhibit 2 shows that over the past five years, total new orders in automotive amounted to €1.5bn and the book-to-bill stands at >1, corrected for cancellations and the extended lifetime of legacy products. Original equipment manufacturers are reducing their investments in legacy products (internal combustion engine related), which shows in the book-to-bill for Kendrion's Automotive Core of 0.9. The strongest growth in order book comes from Automotive E, which had a book-to-bill of 2.2.

During the analyst call, management commented to expect a higher EBITDA margin in 2023, which is fuelled by the previously announced cost savings of €8m, being the €4m due to the split within Automotive and €4m savings due to closure of an automotive plant in Austria. Management does not expect much negative margin impact in H123 from the start-up of the new facility in China, where new Automotive E projects are expected to have a positive contribution margin as from H223.

Despite the difficult market conditions over the past three years, Kendrion remains confident in realising its medium-term targets for the period 2019–2025: organic revenue growth of 5% or more on average per year with an EBITDA margin of at least 15% in 2025 (11.1% in FY22) and return on invested capital of at least 25% in 2025 (FY22: 15.6%).

Kendrion is well positioned to benefit from the energy transition. As Exhibit 3 shows, 50% of the company's revenues is exposed to strong growth, being the activities in Industrial Brakes, Automotive E and China. Automotive Core (35% of revenues) is now set up as a cash cow, while the other 65% of group revenues comes from clean energy applications with exposure to attractive end-markets (for growth and/or profitability).

Exhibit 3: Kendrion's focus on clean energy



Source: Kendrion FY22 presentation

We have raised our FY23 revenue growth estimate from 5% to 6.5% due to the higher-than-expected revenue base in FY22 while raising our growth expectations for the Automotive division from 5% to 8%, driven by the contribution of new projects. For Industrial, we maintain our 5% revenue growth forecast, driven by the continuing electrification trend. For FY24, we stick to our previous growth estimate of 7.5%, which is based on 5% growth in Industrial and 9% in Automotive. As FY22 EBITDA was a bit lower than expected, we have left our EBITDA estimates broadly unchanged despite the raised revenue estimates. This reflects an adjustment of 30bp in margins for both FY23 and FY24, although this still means a decent improvement compared to FY22, which is mainly driven by operating leverage and cost savings. Kendrion seems well on the way to achieving the targeted 15% EBITDA margin in 2025. The CAGR in our estimated EPS in 2022–24e is 25%.

Exhibit 4: Change in estimates

€m	2022			2023e			2024e		
	Old	Actual	Change	Old	New	Change	Old	New	Change
Sales	516	519	0.7%	541	553	2.1%	584	594	1.6%
EBITDA normalised	58.6	57.4	-2.1%	68.7	68.3	-0.6%	81.1	80.4	-0.8%
EBITDA margin	11.4%	11.1%		12.7%	12.4%		13.9%	13.6%	
EBITA margin	6.9%	6.6%		8.1%	7.8%		9.6%	9.3%	
Net profit adjusted	24.2	21.7	-10.3%	29.6	25.2	-15.0%	39.0	33.7	-13.7%
EPS adjusted (€)	1.60	1.45	-9.7%	1.96	1.67	-15.0%	2.58	2.23	-13.7%
DPS (€)	0.80	0.72	-10.3%	0.98	0.83	-15.0%	1.29	1.11	-13.7%

Source: Kendrion, Edison Investment Research

Valuation

For the valuation of Kendrion, we look at three different valuation methods: historical multiples, discounted cash flow (DCF) and peer comparison (as discussed in our report).

Historical valuation: based on our forecast EV/EBITDA multiple for FY23, Kendrion is trading at a discount of 34% compared to its historical valuation of 8.4x. Based on our previous assumption that a small discount of 5% to its historical multiples is justified, given that current profitability is slightly below the historical average, this gives a value of €20.3 per share (down from €20.7 per share previously).

DCF valuation: we have only changed the risk-free rate from 3.0% to 3.5% in our assumptions, bringing the WACC to 8.4% (was 8.0%). We slightly raised our estimates and rolled over our model by one year, which overall has resulted in a higher value per share of €26.9 vs €24.1 previously.

Peer group comparison: we have not changed our assumption that a valuation in line with its peers is merited based on the 2023e EV/EBITDA multiple, versus the current discount of 17%. This assumption delivers a value per share of €21.2, down from €21.9.

The updated average of these valuation methods points to a valuation of €22.8 per share (previously €22.2).

Exhibit 5: Valuation methods for Kendrion

Valuation method	Edison assumptions	Equity value per share (€)
Historical valuation	2023e EV/EBITDA at a small discount of 5% to its historical multiples	20.3
DCF	Terminal growth 1.5%, terminal EBITA margin 7.5%	26.9
Peer group	2023e EV/EBITDA in line with peers	21.2
Average value per share		**22.8**
Current share price		15.9

Source: Edison Investment Research

Exhibit 6: Financial summary

€ m	2020	2021	2022	2023e	2024e	2025e
31-December	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT						
Revenue	396.4	463.6	519.3	552.5	593.6	640.6
Gross Profit	191.0	225.8	249.3	265.7	286.0	309.3
EBITDA normalised	44.6	55.8	57.4	68.3	80.4	94.6
EBITDA reported	40.2	51.7	(6.6)	68.3	80.4	94.6
Depreciation & Amortisation	(25.7)	(23.9)	(23.3)	(25.3)	(25.3)	(25.4)
EBITA normalised	18.9	31.9	34.1	43.0	55.1	69.2
Amortisation of acquired intangibles	(4.4)	(3.9)	(4.7)	(5.0)	(5.0)	(5.0)
Exceptionals (Edison definition)	(4.4)	(4.1)	(64.0)	0.0	0.0	0.0
EBIT reported	10.1	23.9	(-34.6)	38.0	50.1	65.2
Net Interest	(4.4)	(3.7)	(5.1)	(5.2)	(4.6)	(4.0)
Participations	0.0	(0.1)	0.0	0.0	0.0	0.0
Profit Before Tax	5.7	20.1	(39.7)	32.7	45.5	61.2
Reported tax	(1.4)	(5.7)	(6.6)	(11.3)	(15.6)	(20.6)
Profit After Tax	4.3	14.4	(46.3)	21.5	29.9	40.6
Net income (normalised)	11.7	20.6	21.7	25.2	33.7	43.4
Net income (reported)	4.3	14.4	(46.3)	21.5	29.9	41.6
Average number of shares (m)	14.8	14.8	15.0	15.1	15.1	15.1
Total number of shares (m)	14.9	14.9	15.1	15.1	15.1	15.1
EPS normalised before amortisation (€)	0.79	1.39	1.45	1.67	2.23	2.87
EPS reported (€)	0.29	0.97	(3.09)	1.42	1.98	2.75
DPS (€)	0.40	0.69	0.72	0.83	1.11	1.43
Revenue growth	-3.9%	17.0%	12.0%	6.4%	7.4%	7.9%
Gross Margin	48.4%	48.3%	48.1%	48.1%	48.2%	0.0%
EBITDA Margin	11.3%	12.0%	11.1%	12.4%	13.6%	14.8%
Normalised Operating Margin	4.8%	6.9%	6.6%	7.8%	9.3%	10.8%
BALANCE SHEET						
Fixed Assets	299.6	324.5	278.5	273.7	269.7	266.3
Intangible Assets	159.1	183.4	126.5	124.1	121.6	119.2
Tangible Assets	118.7	121.9	131.6	129.2	127.7	126.8
Investments & other	21.8	19.2	20.4	20.4	20.4	20.4
Current Assets	129.5	166.3	198.1	209.0	227.3	251.3
Stocks	61.7	79.7	85.1	90.0	96.0	103.0
Debtors	47.2	56.8	58.8	62.6	67.2	72.5
Other current assets	7.6	11.2	16.4	17.5	18.7	20.2
Cash & cash equivalents	13.0	18.6	37.8	39.0	45.3	55.6
Current Liabilities	87.9	97.6	104.8	110.4	117.3	126.2
Creditors	44.0	51.6	54.9	58.4	62.8	67.7
Other current liabilities	31.9	33.2	38.4	40.5	43.0	46.0
Short term borrowings	12.0	12.8	11.5	11.5	11.5	11.5
Long Term Liabilities	137.8	170.2	196.8	186.8	176.8	166.8
Long term borrowings	104.2	136.4	166.6	156.6	146.6	136.6
Other long term liabilities	33.6	33.8	30.2	30.2	30.2	30.2
Shareholders' equity	203.4	223.0	175.0	185.6	202.9	224.7
Balance sheet total	429.1	490.8	476.6	482.7	497.0	517.7
CASH FLOW						
Op Cash Flow before WC and tax	40.6	54.6	52.1	68.3	80.4	94.6
Working capital	5.4	(17.4)	(4.9)	(4.1)	(5.1)	(5.8)
Tax	(1.3)	(6.2)	(5.2)	(11.3)	(15.6)	(20.6)
Net interest	(2.9)	(3.2)	(4.1)	(5.2)	(4.6)	(4.0)
Net operating cash flow	41.8	27.8	37.9	47.7	55.2	64.2
Capex	(16.0)	(30.0)	(37.7)	(25.5)	(26.3)	(27.1)
Acquisitions/disposals	(78.2)	(18.8)	(0.2)	0.0	0.0	0.0
Equity financing	0.0	0.0	0.0	0.0	0.0	0.0
Dividends	0.0	(4.3)	(7.1)	(10.9)	(12.6)	(16.8)
Other	(6.4)	0.0	0.0	0.0	0.0	0.0
Net Cash Flow	(58.8)	(25.3)	(7.1)	11.2	16.3	20.3
Opening net debt/(cash)	50.4	109.2	134.5	141.6	130.4	114.1
Closing net debt/(cash)	109.2	134.5	141.6	130.4	114.1	93.8

Source: Kendrion, Edison Investment Research

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