

Treatt

Positive momentum continues

FY trading update

Food & beverages

12 October 2021

Price 1,050p
Market cap £628m

Net debt (£m) at 30 September 2021 6
Shares in issue 59.6m
Free float 100%
Code TET
Primary exchange LSE
Secondary exchange N/A

Share price performance



| % | 1m | 3m | 12m |
|------------------|-----|--------|------|
| Abs | 5.5 | (7.9) | 63.3 |
| Rel (local) | 5.2 | (7.8) | 35.6 |
| 52-week high/low | | 1,225p | 600p |

Business description

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

Next events

FY21 results 30 November 2021

Analysts

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Treatt has had yet another strong year, with momentum in the business continuing. Revenue growth was 14% during the year, or 18% at constant currency, and was driven by continued strength in the healthier living segments, although slightly below our forecasts. Margins also continued to benefit from the positive mix as Treatt's products increasingly move towards more value-added solutions. FY21 PBT is still expected to be in line with prior guidance.

| Year end | Revenue (£m) | PBT* (£m) | EPS* (p) | DPS (p) | P/E (x) | Yield (%) |
|----------|--------------|-----------|----------|---------|---------|-----------|
| 09/19 | 112.7 | 14.0 | 19.0 | 5.5 | 55.1 | 0.5 |
| 09/20 | 109.0 | 15.8 | 21.3 | 6.0 | 49.2 | 0.6 |
| 09/21e | 124.3 | 21.7 | 29.4 | 8.5 | 35.7 | 0.8 |
| 09/22e | 131.7 | 23.5 | 32.0 | 9.2 | 32.8 | 0.9 |

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

Flavours and fragrances continues to be attractive

The flavours and fragrances market continues to be attractive and Treatt successfully embraces the sweet spot. Its portfolio is well suited for the consumer trends of clean labels and more natural, better-for-you products. For example, the consumer shift away from categories such as beer towards products such as craft beers, alcoholic seltzers and cocktails – which all contain natural flavourings – serves as a material driver of growth for the whole flavour industry and for Treatt in particular. The return of the on-trade following the lifting of COVID-19 restrictions, coupled with an increase in new launches that were postponed from the height of the pandemic, has resulted in further growth, particularly in the tea category, which was up 113% in revenue terms.

Positive mix still driving margin improvement

Treatt's continued focus on value-added products continues to be a driver of margin expansion as the group moves away from commodity products. Faster growth in the higher-margin categories was also of help during FY21 and hence management upgraded its PBT outlook with the H121 results. In terms of costs, increases in freight and logistics costs have not materially affected the group as it tends to transport concentrated product, hence logistics costs are less significant. The company reported ending FY21 with net debt of c £6m on a pre-IFRS 16 basis.

Valuation: Dividend uplift expected

We note the current share price is discounting medium-term sales growth of 4.5%, falling to 2.0% in perpetuity, with a WACC of 5.7% and a terminal EBIT margin of 20.0%. We expect a significant uplift in the dividend in FY21 as the company has a very modest net debt position. Our earnings estimates remain broadly unchanged following the announcement. On a calendarised basis, Treatt trades at 32.8x FY22e P/E and 20.9x FY22e EV/EBITDA. On both P/E and EV/EBITDA multiples, it trades at a c 10% premium to its peer group.

Forecast revisions

We update our forecasts to reflect the latest trading. We cut our FY21 revenue estimates to £124m, as per the trading update, but our profit forecasts remain broadly unchanged as higher margins than expected have compensated for the lower growth than expected versus our forecasts. We illustrate the changes in Exhibit 1 below. We also update our net debt forecast to reflect the guidance in the trading statement.

Exhibit 1: Old versus new key P&L forecasts

| | 2021 | | | 2022 | | | 2023 | | |
|---|---------|---------|--------|-----------|-----------|--------|------------|------------|--------|
| | Old | New | Diff | Old | New | Diff | Old | New | Diff |
| Revenue (£000) | 127,549 | 124,278 | -2.6% | 135,202 | 131,735 | -2.6% | 143,314 | 139,639 | -2.6% |
| EBITDA (£000) | 10,307 | 25,478 | 147.2% | 11,604 | 30,123 | 159.6% | 15,049 | 32,106 | 113.3% |
| Operating profit (£000) | 20,464 | 20,436 | -0.1% | 22,097 | 22,057 | -0.2% | 23,853 | 23,800 | -0.2% |
| PBT (pre-exceptional) Treatt (£000)* | 20,450 | 20,417 | -0.2% | 22,099 | 22,051 | -0.2% | 23,906 | 23,848 | -0.2% |
| PBT (pre-exceptional) Edison (£000) | 21,736 | 21,701 | -0.2% | 23,597 | 23,546 | -0.2% | 25,514 | 25,453 | -0.2% |
| Basic EPS (pre-exceptional) Treatt (p)* | 27.3 | 27.3 | -0.2% | 29.5 | 29.5 | -0.2% | 32.0 | 31.9 | -0.2% |
| Basic EPS (pre-exceptional) Edison (p) | 29.5 | 29.4 | -0.2% | 32.0 | 32.0 | -0.2% | 34.6 | 34.6 | -0.2% |
| Net debt/(cash) (£000) | 5,945.4 | 6,022.6 | 1.3% | (5,384.6) | (5,264.2) | -2.2% | (16,137.6) | (15,969.3) | -1.0% |

Source: Edison Investment Research. Note: *Stated on company normalised basis, which is pre-exceptional but after amortisation of acquired intangibles and share-based payments.

The outlook for FY22 is positive and the board expects to see growth across all its product categories.

Valuation

We illustrate Treatt's relative valuation versus its ingredients peer group in Exhibit 2 below. For 2022, Treatt trades at a c 10% premium to its peer group on both a P/E and EV/EBITDA basis. Although it is smaller than its peers, its portfolio of products is increasingly specialised and the company has demonstrated its resilience with a robust performance despite the COVID-19 pandemic.

Exhibit 2: Comparative valuation

| | Market cap (m) | P/E (x) | | EV/EBITDA (x) | | Dividend yield (%) | |
|---|----------------|--------------|--------------|---------------|-------------|--------------------|----------------|
| | | 2021e | 2022e | 2021e | 2022e | 2021e | 2022e |
| Givaudan | CHF39,277 | 42.0 | 39.0 | 28.8 | 27.6 | 1.6 | 1.7 |
| IFF | \$35,135 | 24.2 | 21.5 | 18.6 | 15.9 | 2.1 | 2.3 |
| Symrise | CHF15,715 | 39.9 | 37.0 | 21.3 | 20.0 | 1.0 | 1.0 |
| Chr Hansen | DKK67,088 | 42.6 | 36.7 | 25.3 | 22.9 | 2.0 | 1.6 |
| Kerry | €20,545 | 30.5 | 27.7 | 20.8 | 19.6 | 0.8 | 0.9 |
| Ingredion | \$6,364 | 14.3 | 13.3 | 8.7 | 8.2 | 2.8 | 2.8 |
| Peer group average | | 35.4 | 32.3 | 26.3 | 20.6 | 1.6 | 1.7 |
| Treatt | £628.3 | 35.7 | 32.8 | 24.6 | 20.8 | 0.8 | 0.9 |
| Premium/(discount) to peer group (%) | | 10.6% | 12.3% | 19.7% | 9.8% | (52.6%) | (48.9%) |

Source: Refinitiv, Edison Investment Research. Note: Priced at 8 October 2021.

Exhibit 2: Financial summary

| | £000s | 2017 | 2018 | 2019 | 2020 | 2021e | 2022e | 2023e | 2024e |
|--|-------|----------|----------|----------|----------|----------|----------|----------|-----------|
| Year end September | | IFRS | IFRS | IFRS | IFRS | IFRS | IFRS | IFRS | IFRS |
| PROFIT & LOSS | | | | | | | | | |
| Revenue | | 101,250 | 112,163 | 112,717 | 109,016 | 124,278 | 131,735 | 139,639 | 148,017 |
| Cost of Sales | | (75,985) | (84,407) | (84,060) | (77,140) | (85,951) | (90,713) | (95,737) | (101,037) |
| Gross Profit | | 25,265 | 27,756 | 28,657 | 31,876 | 38,327 | 41,022 | 43,902 | 46,980 |
| EBITDA | | 15,049 | 16,627 | 15,785 | 17,862 | 25,478 | 30,123 | 32,106 | 34,237 |
| Operating Profit (before amort., except and SBP) | | 13,650 | 15,108 | 14,226 | 16,053 | 21,720 | 23,553 | 25,405 | 27,396 |
| Intangible Amortisation | | (137) | (124) | (90) | (75) | (64) | (54) | (46) | (39) |
| Share based payments | | (966) | (1,040) | (637) | (886) | (1,220) | (1,441) | (1,559) | (1,685) |
| Other | | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Operating Profit | | 12,547 | 13,944 | 13,499 | 15,092 | 20,436 | 22,057 | 23,800 | 25,672 |
| Net Interest | | (851) | (1,302) | (199) | (291) | (19) | (7) | 48 | 104 |
| Exceptionals | | 0 | (1,105) | (755) | (1,060) | (1,400) | 0 | 0 | 0 |
| Profit Before Tax (norm) | | 12,799 | 13,806 | 14,027 | 15,762 | 21,701 | 23,546 | 25,453 | 27,500 |
| Profit Before Tax (FRS 3) | | 11,696 | 11,537 | 12,545 | 13,741 | 19,017 | 22,051 | 23,848 | 25,776 |
| Profit Before Tax (company) | | 11,696 | 12,642 | 13,300 | 14,801 | 20,417 | 22,051 | 23,848 | 25,776 |
| Tax | | (3,129) | (2,284) | (2,673) | (2,896) | (4,083) | (4,410) | (4,770) | (5,155) |
| Profit After Tax (norm) | | 9,670 | 11,392 | 11,263 | 12,762 | 17,617 | 19,136 | 20,683 | 22,345 |
| Profit After Tax (FRS 3) | | 8,567 | 9,253 | 9,872 | 10,845 | 14,934 | 17,640 | 19,078 | 20,621 |
| Discontinued operations | | 978 | 2,976 | (1,084) | 0 | 0 | 0 | 0 | 0 |
| Average Number of Shares Outstanding (m) | | 52.2 | 56.8 | 59.1 | 59.8 | 59.8 | 59.8 | 59.8 | 59.8 |
| EPS - normalised (p) | | 18.5 | 20.1 | 19.0 | 21.3 | 29.4 | 32.0 | 34.6 | 37.3 |
| EPS - adjusted (p) | | 18.3 | 18.0 | 17.8 | 19.7 | 27.3 | 29.5 | 31.9 | 34.5 |
| EPS - (IFRS) (p) | | 16.4 | 16.3 | 16.7 | 18.1 | 25.0 | 29.5 | 31.9 | 34.5 |
| Dividend per share (p) | | 4.8 | 5.1 | 5.5 | 6.0 | 8.5 | 9.2 | 9.9 | 10.7 |
| Gross Margin (%) | | 25.0 | 24.7 | 25.4 | 29.2 | 30.8 | 31.1 | 31.4 | 31.7 |
| EBITDA Margin (%) | | 14.9 | 14.8 | 14.0 | 16.4 | 20.5 | 22.9 | 23.0 | 23.1 |
| Operating Margin (before GW and except.) (%) | | 13.5 | 13.5 | 12.6 | 14.7 | 17.5 | 17.9 | 18.2 | 18.5 |
| Operating Margin (%) | | | 12.4 | 12.0 | 13.8 | 16.4 | 16.7 | 17.0 | 17.3 |
| BALANCE SHEET | | | | | | | | | |
| Fixed Assets | | 19,532 | 21,863 | 31,730 | 54,048 | 62,917 | 61,769 | 62,116 | 62,456 |
| Intangible Assets | | 3,331 | 752 | 845 | 1,358 | 1,294 | 1,240 | 1,194 | 1,155 |
| Tangible Assets | | 14,821 | 20,038 | 29,485 | 50,159 | 60,265 | 59,171 | 59,564 | 59,943 |
| Investments | | 1,380 | 1,073 | 1,400 | 2,531 | 1,358 | 1,358 | 1,358 | 1,358 |
| Current Assets | | 68,230 | 102,401 | 98,158 | 69,472 | 77,335 | 81,115 | 93,329 | 109,210 |
| Stocks | | 42,878 | 39,642 | 36,799 | 36,050 | 41,633 | 43,868 | 46,221 | 48,698 |
| Debtors | | 19,973 | 28,828 | 23,020 | 24,167 | 27,963 | 29,509 | 31,140 | 32,860 |
| Cash | | 4,748 | 32,304 | 37,187 | 7,739 | 7,739 | 7,739 | 15,969 | 27,652 |
| Other | | 631 | 1,627 | 1,152 | 1,516 | 0 | 0 | 0 | 0 |
| Current Liabilities | | (27,003) | (35,781) | (28,905) | (15,989) | (22,224) | (14,823) | (13,266) | (13,322) |
| Creditors | | (19,266) | (16,479) | (11,784) | (12,640) | (13,049) | (13,173) | (13,266) | (13,322) |
| Short term borrowings | | (7,680) | (19,244) | (16,860) | (3,203) | (9,174) | (1,650) | 0 | 0 |
| Provisions | | (57) | (58) | (261) | (146) | 0 | 0 | 0 | 0 |
| Long Term Liabilities | | (14,281) | (6,858) | (13,876) | (16,411) | (18,348) | (14,386) | (13,361) | (13,161) |
| Long term borrowings | | (7,293) | (3,001) | (4,369) | (3,450) | (4,587) | (825) | 0 | 0 |
| Other long term liabilities | | (6,988) | (3,857) | (9,507) | (12,961) | (13,761) | (13,561) | (13,361) | (13,161) |
| Net Assets | | 46,478 | 81,625 | 87,107 | 91,120 | 99,680 | 113,675 | 128,819 | 145,183 |
| CASH FLOW | | | | | | | | | |
| Operating Cash Flow | | 4,683 | 3,580 | 20,544 | 15,677 | 15,108 | 26,266 | 28,015 | 29,895 |
| Net Interest | | (913) | (609) | (199) | (191) | (19) | (7) | 48 | 104 |
| Tax | | (2,822) | (2,978) | (2,208) | (2,191) | (4,083) | (4,410) | (4,770) | (5,155) |
| Capex | | (5,111) | (6,190) | (10,392) | (23,909) | (13,864) | (5,476) | (7,095) | (7,220) |
| Acquisitions/disposals | | (1,667) | 8,357 | 855 | (1,041) | 0 | 0 | 0 | 0 |
| Financing | | 270 | 21,090 | 622 | (69) | 0 | 0 | 0 | 0 |
| Dividends | | (3,025) | (2,876) | (3,080) | (3,378) | (3,590) | (5,086) | (5,493) | (5,941) |
| Net Cash Flow | | (8,585) | 20,374 | 6,142 | (15,102) | (6,449) | 11,287 | 10,705 | 11,683 |
| Opening net debt/(cash) | | 1,654 | 10,225 | (10,059) | (15,958) | (427) | 6,023 | (5,264) | (15,969) |
| HP finance leases initiated | | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Other | | 14 | (90) | (243) | (429) | (0) | 0 | 0 | 0 |
| Closing net debt/(cash) | | 10,225 | (10,059) | (15,958) | (427) | 6,023 | (5,264) | (15,969) | (27,652) |

Source: Edison Investment Research, company data

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