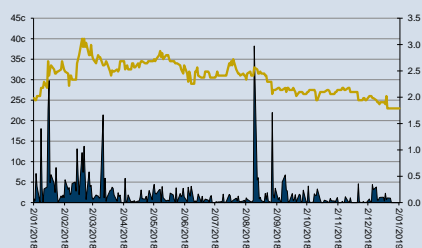


BUY

Current Price \$0.23
Valuation \$0.42

Ticker:	VMX.ASX		
Sector:	Engineering & Contracting		
Shares on Issue (m):	124.6		
Market Cap (\$m):	28.7		
Net Debt / (Cash) (\$m):	0.1		
Enterprise Value (\$m):	28.8		
52 wk High/Low:	0.40	0.23	
12m Av Daily Vol (m):	0.21		
Key Metrics			
	19F	20F	
EV/EBITDA (x)	3.3	2.7	
EV/EBIT (x)	4.1	3.2	
P/E (x)	5.8	4.5	
Ratios			
	18A	19F	20F
ND / Equity	0.4%	-13.8%	-21.8%
EBITDA Mgn	4.7%	7.3%	7.9%
RoA	7.7%	13.2%	15.9%
RoE	10.8%	14.7%	16.6%
Financials:			
Normalised*:	18A	19F	20F
Revenue (\$m)	103.2	120.0	135.0
EBITDA (\$m)	4.9	8.8	10.6
NPAT (\$m)	2.6	5.0	6.4
* Adj. for one-offs & amortisation			
Net Assets (\$m)	31.5	35.8	41.5
Op CF (\$m)	-2.8	6.4	5.8
Per Share Data:			
	18A	19F	20F
Norm. EPS (cps)	2.6	4.0	5.1
DPS (cps)	0.00	0.00	0.00
Div Yield	0.0%	0.0%	0.0%
NTAPS (cps)	27.6	26.4	31.6
CFPS (cps)	-2.7	5.2	4.7

Share Price Graph



Please refer to important disclosures at end of the report (from page 3)

Wednesday, 2 January 2019

Valmec (VMX)

Cheap given tailwinds

Analyst | Ian Christie, CFA

Quick Read

Heading into 2019 and the interim reporting season, we have reviewed our forecasts and valuation. Despite heightened global concerns, we maintain a positive view on the tailwinds behind gas construction and operations services in Australia. As a result our forecasts and valuation of \$0.42 are unchanged. On our numbers VMX is trading on undemanding forward multiples, suggesting considerable share price upside potential. BUY maintained.

Impact | Attractive multiples on current forecasts

Factoring in the risks: As highlighted in our broad comment on cyclical industrials (“Into 2019 – factoring in the risks”, 3 January 2019), we believe we need to address two key issues; firstly the risks to forecasts in a slower, credit-constrained world, and secondly, the impact that greater uncertainty has on market valuations.

AGM upbeat: Recent contract wins and AGM commentary provide a positive backdrop for 2019. In October, contracts worth \$18m were awarded, and in December, a further \$25m contracts were announced. Importantly, these contracts include a significant amount of recurring services revenue, which will help boost this segment’s contribution to the targeted 35-40% of total revenue. VMX indicates a strong outlook, which echoes our positive thematic view on gas infrastructure construction and maintenance spend.

No change to forecasts: Post the annual results in August we built more conservatism into our forecasts (see “[Opportunity](#)”, 28 August 2018), and we see no need to change these numbers. To recap, the FY18 accounts were difficult to analyse in that reported EBITDA was impacted by a one-off, non-cash accounting gain as well as a one-off cost provision. As only the value of the gain was itemised, our calculation of underlying EBITDA of \$4.9m is understated, and FY19 growth is not as dramatic as our numbers suggest. We believe our FY19 margin and earnings forecast to be achievable, and assume a weighting to the 2H (see detail overleaf).

Cash flow to improve in FY19: The provision highlighted above also impacted cash flow in FY18. It relates to ongoing litigation against John Holland with regard to the Northlink project, and a win here could have a significant positive impact on cash flow. Regardless, we anticipate operating inflows in FY19.

Recommendation

Although our forecasts are unchanged, we have introduced more conservatism into our cash flow discount rate and the multiples we use to value the business (see valuation detail overleaf). However, as we now use FY20 as the basis for earnings capitalisation, our blended valuation remains unchanged at \$0.42. This is well ahead of the current price and we maintain a BUY call.

Valmec

Equity Research

Ian Christie

Recommendation	BUY
Current Price (\$)	0.230
Valuation (\$)	0.42

Sector	Engineering & Contracting
Market Cap (\$m)	28.7
Date	2 January 2019

Trading Metrics	FY17A	FY18A	FY19F	FY20F
EV / EBITDA (x)	7.0	5.9	3.3	2.7
EV / EBIT (x)	9.6	8.2	4.1	3.2
P/E (x)	12.1	8.9	5.8	4.5
Dividend Yield (%)	0.0%	0.0%	0.0%	0.0%

Per Share Data	FY17A	FY18A	FY19F	FY20F
Reported EPS (cps)	1.90	3.71	3.44	4.62
Adjusted EPS (cps)	1.90	2.59	3.98	5.14
Div. per share (cps)	0.00	0.00	0.00	0.00
NTA per share (cps)	18.76	27.60	26.43	31.58
CF per share (cps)	1.03	-2.71	5.17	4.69

Underlying P&L (\$m)*	FY17A	FY18A	FY19F	FY20F
Revenue	72.9	103.2	120.0	135.0
EBITDA	4.1	4.9	8.8	10.6
Depreciation	(1.1)	(1.4)	(1.7)	(1.7)
EBIT	3.0	3.5	7.0	8.9
PBT	2.2	2.6	6.8	8.9
NPAT	1.6	2.6	5.0	6.4
Reported NPAT	1.6	3.8	4.3	5.8

* Normalised for one-off items & amortisation

Cash Flow (\$m)	FY17A	FY18A	FY19F	FY20F
Receipts	66.7	93.5	119.4	131.3
Payments	(65.1)	(95.3)	(110.9)	(122.9)
Other / Prepayments	(0.8)	(1.0)	(2.1)	(2.5)
Cash from Operations	0.8	(2.8)	6.4	5.8
Property, Plant & Equip	(0.4)	(0.5)	(1.4)	(1.7)
Payment for Subsidiary	-	(2.6)	-	-
Other	1.0	0.2	-	-
Cash From Investing	0.6	(2.9)	(1.4)	(1.7)
Issue of Shares	-	10.4	-	-
Net Borrowing	(0.9)	(1.0)	(0.9)	(1.8)
Dividends / Other	-	-	-	-
Cash From Financing	(0.9)	9.4	(0.9)	(1.8)
Net Cash Flow	0.5	3.7	4.2	2.3
Ending Cash	(1.0)	2.7	6.9	9.2

Balance Sheet (\$m)	FY17A	FY18A	FY19F	FY20F
Cash (incl. overdraft)	2.3	2.7	6.9	9.2
Receivables	19.4	29.0	29.6	33.3
Inventory / Other	7.4	7.7	9.7	10.8
Current Assets	29.1	39.5	46.2	53.4
Property, Plant & Equip	7.0	10.6	10.2	10.3
Other NC Assets	5.4	5.1	4.5	3.8
Non-Current Assets	12.4	15.8	14.7	14.1
Total Assets	41.5	55.2	61.0	67.5
Payables	15.7	19.0	21.3	23.8
Borrowings	7.1	2.9	2.0	0.2
Provisions / Other	1.4	1.9	1.9	1.9
Total Liabilities	24.3	23.8	25.2	25.9
Net Assets	17.2	31.5	35.8	41.5
Ordinary Equity	6.2	16.6	16.6	16.6
Reserves	0.3	0.4	0.4	0.4
Retained Earnings	10.7	14.5	18.8	24.5
Total Equity	17.2	31.5	35.8	41.5

Valuation	Calcs.	\$m	\$ps
DCF Valuation:			
Discount Rate / WACC (%)	13.0%		
PV Free Cash Flow (\$m)		57.2	
Less Net Debt / Plus Cash (\$m)		(0.1)	
Unpaid Capital (\$m)		-	
Equity Value (\$m)		57.1	0.46

Earnings Capitalisation Valuation:			
FY20 EBITDA multiple	4.5	47.8	0.38
FY20 PE multiple	8.0	51.3	0.41
Valuation (\$/share) - blend of DCF & earnings cap			0.42

Underlying P&L (\$m)*	1H18A	2H18A	1H19F	2H19F
Revenue	49.8	53.4	56.0	64.0
EBITDA	3.4	1.5	4.0	4.8
Depreciation	(0.6)	(0.8)	(0.9)	(0.9)
EBIT	2.8	0.7	3.2	3.9
PBT	2.3	0.3	3.0	3.8
NPAT	1.6	1.0	2.2	2.7
Reported NPAT	1.6	2.2	1.9	2.4

* Normalised for one-off items & amortisation

Cash Flow (\$m)	1H18A	2H18A	1H19F	2H19F
Receipts	46.1	47.4	56.0	63.4
Payments	(45.4)	(49.9)	(52.0)	(58.9)
Other / Prepayments	(0.5)	(0.4)	(0.9)	(1.1)
Cash from Operations	0.2	(2.9)	3.1	3.4
Property, Plant & Equip	(0.3)	(0.2)	(0.7)	(0.7)
Payment for Subsidiary	-	(2.6)	-	-
Other	0.2	0.0	-	-
Cash From Investing	(0.1)	(2.8)	(0.7)	(0.7)
Issue of Shares	-	10.4	-	-
Net Borrowing	(0.3)	(0.7)	(0.5)	(0.5)
Dividends / Other	-	-	-	-
Cash From Financing	(0.3)	9.7	(0.5)	(0.5)
Net Cash Flow	(0.3)	4.0	2.0	2.2
Ending Cash	(1.2)	2.7	4.7	6.9

Financial Ratios	FY17A	FY18A	FY19F	FY20F
Growth				
Revenue growth (%)	43.5%	41.6%	16.3%	12.5%
Norm. EPS growth (%)	733.9%	36.9%	53.3%	29.3%
Profitability Ratios				
GP Margin (%)	16.1%	14.0%	16.1%	16.1%
EBITDA Margin (%)	5.6%	4.7%	7.3%	7.9%
Return on Assets (%)	8.3%	7.7%	13.2%	15.9%
Return on Equity (%)	9.5%	10.8%	14.7%	16.6%
ROIC (%)	13.0%	12.3%	14.8%	18.7%
Balance Sheet Ratios				
Net Debt (ND) / Equity (%)	28.2%	0.4%	-13.8%	-21.8%
ND / ND + Equity (%)	22.0%	0.4%	-16.1%	-27.9%
Current Ratio (x)	1.4	1.8	1.9	2.1
Net Interest Cover (x)	3.8	5.7	27.9	113.1
Cash Flow Ratios				
Free Cash Flow Yield (%)	2.1%	-25.2%	17.7%	14.3%
Cash Conversion (x)	0.2	(0.6)	0.7	0.5

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