Marshall of Cambridge

A year of strategic focus

11 July 2022

2021 proved to be an eventful year for MCH. The new Board sought to re-engineer the Group into a structure that maximises shareholder value over the medium term. This involved several disposals, not least the motor retail arm in advance of changes in the industry, as well as other non-core divisions. We expect the proceeds will be used to clear debt, invest in growth, and a return of cash to shareholders. The decision by the UK MoD to retire its C-130J fleet from March 2023, has focused the Board on securing further international contracts within its aerospace and defence core. The pipeline of opportunities remains strong throughout the Group, with recovery at Land Systems and Fleet Solutions likely to underpin profits growth.

Our sum-of-the-parts valuation, based on conservative EBITDA expectations and ratings, suggests a fair value / share of 523p, representing a 23.1% premium to the last traded price.

The 12 months to December 2021 proved significant to Marshall of Cambridge holdings (MCH). The pandemic continued to impact the business and coupled with the phased installation of new ERP software, changes to working practices, and supply chain issues, underlying profitability declined yoy.

The decision by the UK MoD to retire its Hercules C-130J fleet from March 2023 represents both an opportunity for the Aerospace division, as well as a threat. In advance of the decision, the Group had begun to seek out additional international air force customers, adding the US Marine Corps from late 2020 and India in early 2022, taking the client list to 18. An office was opened in Washington DC to seek other US DoD MRO contracts on the airframe, in view of the positive feedback on the initial USMC contract.

Several disposals were announced during 2021, the largest in Q4 as the motor retail division, MMH was taken over by Constellation Holdings (completed in May 2022). The consideration for the Group's stake amounted to c.£202m, representing a significant uplift on the listed valuation pre-bid. The civil aerospace focused Aeropeople, the early-stage investor Martlet Capital and the Land North of Cherry Hinton development were sold during the year, with considerations payable from 2022 to 2024.

The disposals give management choices with regards to the use of the proceeds. We think a combination of the repayment of indebtedness, a return of cash to shareholders and growth investment in the retained businesses are the most likely destinations for the cash.

The introduction of targets for returns demonstrates a new focus on shareholder value, which we find encouraging, with the disposals highlighting that there are no sacred cows in the Group. We think returns and profitability are likely to improve from here, reflecting more efficient business models post-implementation of the ERP software and newly introduced working practices.

The pipeline of new opportunities remains strong throughout the Group, not least within the core divisions. The combination of new customer wins, improved manufacturing processes at Land Systems, the prospect of recovery in the food service and hospitality sectors within Fleet Solutions and growth in renewables, plus continued cash generation and rising profitability of Group Property augurs well for the future and recovery in profitability over the medium term.

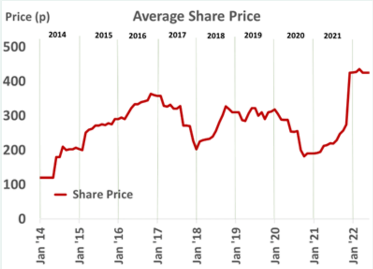
Sum-of the-parts valuation

We have generated a sum-of-the-parts valuation from our model using conservative ratings and FY25 EBITDA expectations to determine a fair value / share. The implied equity value of £309m equates to 523p per NVPO share.

Marshall of Cambridge Holdings Ltd

Last matched trade	425p
Implied market cap	£251.1m
ED fair value / NVPO share	523p
Ordinary share count	59.1m
Preference shares	£8.4m
Net debt (Dec '21)	£41.2m

Share Price, p



Source: James Sharp & Co

Description

Founded in 1909, Marshall of Cambridge (Holdings) Ltd (MCH) is a private, family-owned company, employing c.2,000 staff. The world-class applied engineering services and technology business to the aerospace and defence sectors is the core of the Group, comprising Aerospace, Land Systems and Advanced Composites. The property division, MGP, is in the process of unlocking value from its 900-acre estate at Cambridge airport.

The non-voting private ordinary shares (NVPOs) can be traded freely via a special off-exchange matching facility administered by Stockbroker James Sharp & Co. The contact there is Josh McArdle. Tel. 0161 764 4043.

David O'Brien (Analyst)
0207 065 2690
david@equitydevelopment.co.uk

Andy Edmond
0207 065 2691
andy@equitydevelopment.co.uk

A significant year

2021 proved to be a significant year in the history of Marshall of Cambridge Holdings in several ways. Not only did the pandemic continue to impact the business, but several decisions were made that will result in the business changing forever.

Owing to one such decision, the year-end was temporarily moved to 31 March 2022 and as such, the results are interim in nature but covering the 12 months to 31 December 2021. The year-end is to revert to December at the end of 2022.

The pandemic was again notable during FY21 across much of the business, not only in its effect on working practices but more significantly on how it affected the supply chain, resulting in markedly higher levels of inventory. Fleet Solutions struggled the most due to such shortages, albeit its y-o-y performance was surprisingly good under such challenging circumstances.

A significant event was the news received in March, that the UK government's Integrated Review of Security, Defence, Development and Foreign Policy included the intention to advance the out of service date for the RAF's C-130J fleet to March 2023. The Aerospace division is predominantly focused on the C-130 and as such, the UK government's decision placed the business at a crossroads. However, the Group is exploring expansion in North America, with Aerospace opening an office in Washington DC and Land Systems announcing additional manufacturing capacity in Canada. December 2021 witnessed the third US Marine Corps C-130J undergoing maintenance in Cambridge.

The decision was made to focus the portfolio of businesses, with several non-core, niche businesses sold (including Aeropeople and Martlet Capital), along with the Land North of Cherry Hinton (LNCH). A large element of deferred consideration was included within the sale agreements, with initial cash proceeds generally light albeit except for Martlet Capital.

However, the most significant disposal was the decision to sell the stake in the motor retail business, Marshall Motor Holdings, breaking a 100+-year association with the Group. The consideration was sizeable, generating a net c.£200m for Marshall of Cambridge Holding's (MCH) stake (64.41%) and potentially funding opportunities for the expansion of other parts of the MCH business. The motor retail industry has witnessed significant changes in its distribution model, accelerated by the pandemic and utilising technology. There is uncertainty over whether an agency model will be the way forward, reducing the retailer to the OEMs agent (and potentially impacting future margins). We published a separate note (*Motors disposal completes, 13 June 2022*) and as such, we do not intend to repeat comments on this transaction, other than to highlight the likely use of proceeds within the Financials section later.

The disposals leave a core of six businesses, of which three are centred on aerospace and defence markets (Aerospace, Land Systems and Advanced Composites), one property (Marshall Group Properties), one the provision and maintenance of refrigerated trucks (Fleet Solutions), an apprentice training business (Marshall Skills Academy) and a business accelerator (Futureworx).

The new Local Plan for Cambridge included the airport site (Cambridge East) as a preferred option during September. With expectations of 7,000 homes, plus 1.5m to 2m sq ft of commercial space once completed, the airport site will transform the city. Interest from buyers stretches both nationally and internationally. Cranfield was announced as the preferred option for the relocation of the airport and its facilities, with the moving date brought forward to the latter part of the current decade.

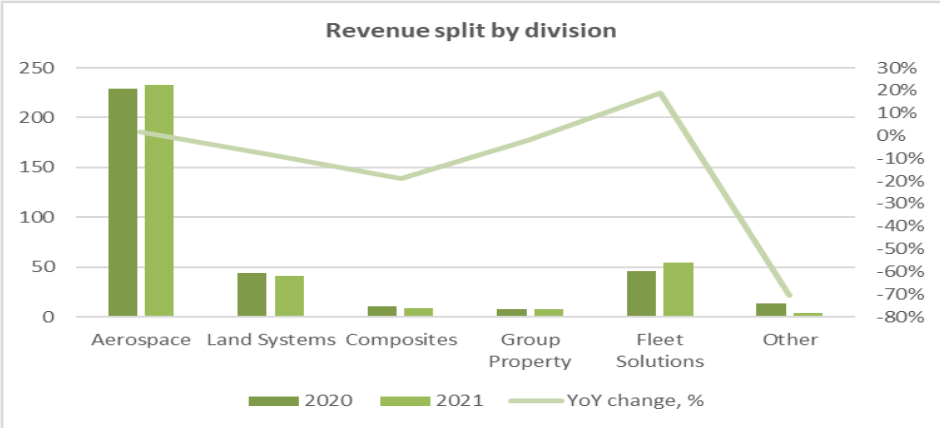
As if the disposals, the ongoing pandemic, and disruption of the supply chain was not enough to deal with, management introduced new ERP software to improve the flow of critical information throughout the Group. The ERP system is expected to drive efficiencies throughout the business, although it is also an agent of change to existing operating models. In some cases, the installation at first proved disruptive, but the medium-term benefits overshadow any teething problems. The process is ongoing.

The combination of the disposals, plus investment in the retained core, introduction of the new ERP software and the business transformation project point to **a renewed focus on growing shareholder value**. The introduction of targets for returns by division, will, aided by investment and management support, further drive profitability over the medium term. We will discuss where we believe margins could rise to as a result. This will also form the focus of our valuation section, utilising medium-to-long-term profitability levels.

Divisional breakdown

Group revenues increased 2.8% y-o-y to £343.1m. The drivers of the improvement were the two largest divisions, Aerospace (+1.5% y-o-y) and Fleet Solutions (+18.8%). The remainder of the Group delivered y-o-y declines, to varying degrees, with the 'Other' category most prominent, which included the non-core Aeropeople, sold during April 2021.

Divisional split of revenue

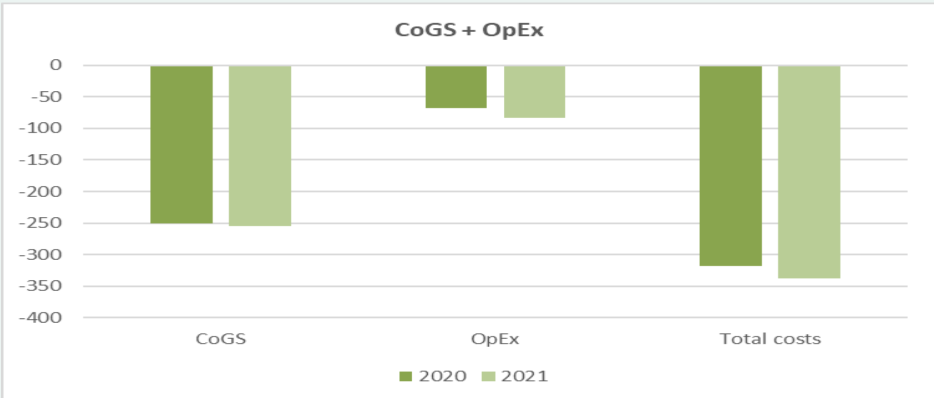


Source; Company

Notwithstanding the issues within the Land Systems and Advanced Composites divisions, the revenues from the older classification of Aerospace and Defence were 14.4% below the FY16 peak, -0.8% on a year ago and down 8.5% on FY19, the last year before the pandemic started. Overall, revenues declined 5.2% from the levels of two years ago, pre-COVID-19.

Costs rose 6.2% to £337m overall, driven by a 23.0% rise in operating expenses. The change in working practices, component shortages and issues within Land Systems were contributory factors in the rise in costs. However, proportionately overall costs rose most significantly within Fleet Solutions (+18.9%) and within Land Systems (+11.0%), while declining in Advanced Composites (-21.4%) and Property (-142.7%).

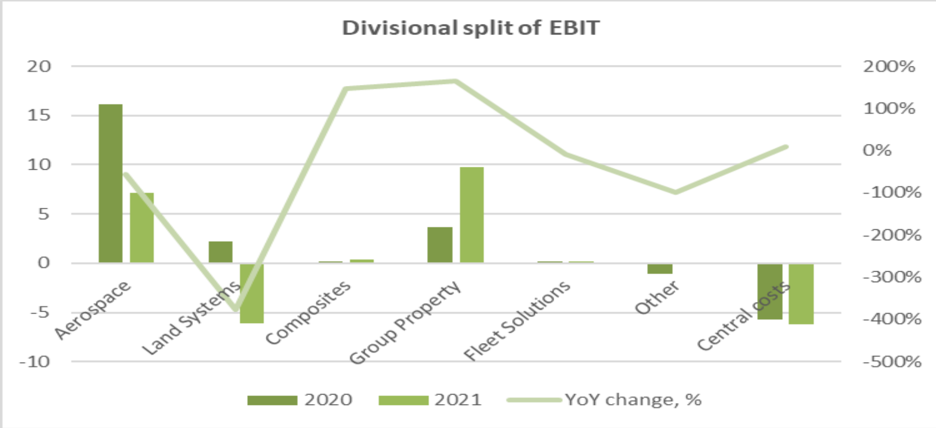
Total costs, £m



Source; Company

EBIT fell by two-thirds to £5.2m, exacerbated by the decline into loss within Land Systems comprising a £8.2m turnaround. The Group EBIT margin declined to 1.5%, compared to 4.7% in FY20. Improvements in both EBIT and margins were experienced within Advanced Composites and in Property.

Divisional split of EBIT, £m



Source; Company

Divisional analysis

Aerospace (revenue: £232.7m, +1.5%; EBIT: £7.1m, -55.8%)

The 12 months to December 2021 proved a pivotal year for the Aerospace division. The decision by the UK MoD to retire its Hercules fleet led to a reduction in engineering upgrade work and in particular a slowing of the level of the centre wing replacement programme (which remains ongoing). However, world events meant that the C-130J fleet was called into action due to the humanitarian evacuation of Kabul, requiring Marshall Aerospace to work around the clock to ensure availability of the airframe.

The looming exit of the RAFs fleet resulted in the search for additional customers, with the US Marine Corps added in late 2020 and a contract with the Indian Air Force's fleet secured in early 2022. Of note during the year was a strong performance with the Royal Canadian Air Force, as a support contract was extended and MRO with the Netherlands' Air Force. Contract extensions were signed with the French and Danish governments for MRO work on their C-130 fleets. Excluding the C-130J, a three-year £46m MRO contract has been secured in the UAE to provide support to a Special Missions Aircraft, delivered in the Sultanate. The target of £150m for new order intake was subsequently met during FY21.

Marshall Aerospace continues to collaborate with the UK MoD on its ongoing requirements on its C-130J fleet. The current conflict in the Ukraine has presented opportunities for Marshall and highlighted the mission critical nature of the airframe to the UK's armed forces. Ahead of disposal further MRO work will be required on the airframe to ensure the highest possible consideration is received from purchasers (and potentially, new customers of the division's services).

Efficiency levels were hindered by the ongoing change in working practices due to COVID-19, albeit the disruption to the supply chain and increase in inventory (and in debtor days) has arguably been a greater issue within the division in the twelve months to December.

The move to Cranfield from the Cambridge Airport site has been confirmed, with the next step a planning application to Central Bedfordshire Council during Q3 '22. The recent milestone achieved by the Aerostructures sub-division was the delivery of the 1,000th auxiliary fuel tank on the P-8 maritime patrol aircraft programme for Boeing.

Land Systems (revenues: £40.6m, -8.3%; EBIT: -£6.1m vs £2.2m)

2021 proved mixed for the Land Systems division, ultimately moving to a loss. The scaling of the DVOW programme resulted in operational issues in production, exacerbated by the implementation of the new ERP system, employee absences (COVID-19) and related supply chain issues. As a result, a new divisional MD, Gary Moynehan was appointed, tasked with returning the business to profitability and returning the top-line to growth.

The focus of the business moving forward will be on the deployable operational infrastructure market internationally, including new markets in Europe and in the Middle East and North Africa. The new strategy includes a simplification of the production process, introducing more flexible and scalable processes based on interchangeable product modularisation.

The performance in the division's Canadian operations was better. A new 83,000 sq ft facility in Moncton, New Brunswick, Canada is expected to open in Q1 2023 and provides capacity to expand the scale of work with the Canadian military, with a hope of securing additional contracts as part of the Defence Investment Plan. A new contract has jus been secured for the Canadian site to supply over 200 ammunition storage containers (MatlogCo) for a division of the Royal Netherlands Army.

The key programme targeted is part of the General Dynamics bid for the LVM programme, which represents the replacement of the Canadian military's fleet of light and heavy vehicles, logistics vehicles, trailers, and containers. A ten-year lease was signed on the facility, which will be utilised in the expansion internationally.

Several contracts were signed during the period, not least for deployable CT scanners from the Australian and Canadian governments, plus additional shelters for Kongsberg and BAE Systems. A strategic partnership was signed with others to support the UK MoD to deliver several programmes (Team Project), with a separate collaboration agreement with Intracom Defence to develop advanced hybrid power solutions.

Advanced Composites (revenues: £8.3m, -19%; EBIT: £0.4m, +146%)

The manufacturing process and workforce of Advanced Composites was overhauled at the end of FY20, with lean manufacturing techniques introduced.

Further efficiency improvements were made, including a 20% reduction in energy consumption, and coupled with design changes resulted in rising margins despite the decline in revenues.

The order book declined during the period, reflecting delays of two orders, now expected to commence from Q4 2022. Marshall has secured a partnering design contract on the next generation Tempest future combat air system programme (FCAS) with BAE Systems, further strengthening the collaborative relationship between the two parties. Contracts with two new customers were signed during the period, commencing in the current year.

A design contract has been secured on the new tempest fighter jet

Source: Company

Looking forward, the division is developing new advanced materials alongside specialist partners, utilising new manufacturing techniques. FY22 should see the division achieving NADCAP approval, with the accreditation potentially opening additional doors in commercial and military aerospace and naval defence programmes.

Property (revenues: £7.9m, -1.9%; EBIT: £9.8m, +164.5%)

The sharp jump in profitability excludes the exceptional gain of £21.1m from the disposal of LNCH and receipts from Marleigh's jv partner, Hill, received in Q1 2021. Instead, it relates to residential sales within the first phase of the Marleigh site. September witnessed the development included within the Local Plan for Greater Cambridgeshire. The LNCH joint venture was disposed of in March, generating £9.1m of initial consideration with the final annual payment due in 2024.

In all, 118 dwellings were sold during the period, of which 76 were private, the remainder shared ownership. Phases 1b and 1c are now up for sale/reserve, with the former comprising 88 dwellings. In October, reserved matters consent was secured for the second phase of the Marleigh development, consisting of 421 homes, with the construction commencing in Q1 '22.

The demolition of motor retail showrooms and the existing Land Systems facility are underway in advance of construction of phase three of the Marleigh site, a new facility is required for the Land Systems business in Cambridge. The relocation of the Aerospace businesses to Cranfield will be submitted for planning approval during Q3 '22 to Central Bedfordshire council.

The new commercial space (7/11 store), a primary school and the community centre are expected to open in September. Marleigh and the jv partners, Hill, will provide additional funding to equip the school appropriately.

Marleigh development – 7/11 store, a community centre and a Primary school, opening in September

Source: ED

Marleigh development – Wide vistas

Source: ED

Marleigh development – Design led / Green space

Source: ED

Fleet Solutions (revenue: £54.3m, +18.8%; EBIT: £0.2m, -8.2%)

In view of the food service and hospitality sectors failing to demonstrate a meaningful level of recovery during the period owing to the ongoing pandemic, we think the top-line outcome is outstanding: growth of 18.8% yoy and the highest revenue reported by the division since FY11. Manufacturers were unable to produce reasonable quantities of new vehicles owing to component shortages, resulting in a negative knock-on effect to installations of Thermo King refrigerated units, down 35% versus a typical non-COVID-19 year.

Lost revenues were replaced by a combination of service contracts with other customers (supermarkets) and a greater frequency of call outs reflecting the older, less reliable equipment. The rising demand for home delivery of groceries ensured demand from its supermarket customers. The contract with its largest retail customer, Tesco, was renewed for a further three years and in the process was extended to cover a wider geographical area.

Despite the rising activity levels (120,000 service calls attended), the high levels of customer service were recognised with an award from an industry magazine.

The period included two separate significant events, which will underpin growth over the medium to longer term. The first was the launch of the Renewables division, seeking to provide new products to reduce carbon emissions, initially with an alternative vegetable fuel (following the removal of government subsidies on red diesel) and, Titan, a hybrid solar and kinetic energy system that can be retrofitted to power refrigeration units.

Secondly, the decision was made to invest in the new ‘supersite’ in Tamworth, opening Q2 2022. The state-of-the-art facility will accommodate the expansion of its Thermo King dealership and workshops, tail lift/lifting decks, drawbar couplings/vehicle mounted cranes, shutter doors, transport heating, pharmaceutical support, and nationwide parts and accessories business. The new facility will also provide training facilities for the industry.

Other (revenues: £3.9m; EBIT: £0.0m)

The key revenue generators within the ‘Other’ category during the 12-months to December 2021 were Aeropeople and Martlet Capital. Aeropeople was sold in April, reflecting the parlous state of the civil aerospace industry due to the pandemic and the heavy losses incurred in FY20 (-£1m). The business delivered £3.4m of revenues ahead of its disposal during the period and compared to £12.8m in FY20.

The early-stage investor, Martlet Capital was sold in October. No fair value gains or impairment provisions were recognised in the period and only one disposal from the portfolio, which occurred in March.

The two newer businesses, Marshalls Skills Academy and Futureworx delivered modest levels of revenues during 2021. The former was impacted by the pandemic, with training less of a priority and contracts were delayed, thereby suffering a small loss during the 12-months to December. The cost base was right sized during Q3 ’21. The business secured a contract with Bombardier to deliver Level 3 Aircraft Maintenance Engineering Apprenticeship training from September 2022. The division is in discussion with third parties on additional aerospace engineering apprenticeship training contracts, which should result in the business generating a profit in FY22.

Futureworx was established in 2021 as a business accelerator within the Cambridge eco-system and utilising the Marshall name to form strategic relationships with other organisations across several markets. Several projects are at the formative stage, although those more advanced include a drone-based solution to survey offshore wind energy infrastructure and, the refuelling of liquid hydrogen powered aircraft (including the conversion of existing craft).

Financials

Owing to the uncertainty created by the decision of the MoD to retire its fleet of Hercules C-130J aircraft, we have suspended estimates until further clarity is forthcoming.

However, we remain optimistic on the outlook for the Group as its transformation continues, in reflection of:

- Additional customer wins, taking the number of C-130J customers to 18 (US, Bangladesh, India)
- The ramping up of the US Marine Corps contract should replace the lost RAF revenues over the medium term
- The opening of an Aerospace office in Washington DC targets additional US C-130J MRO activity
- A possibility of gaining alternative MRO contracts from the UK MoD
- A turnaround of the Land Systems business, as new working practices and a simplification of the production process are introduced
- Potential contract wins with the Canadian Armed Forces
- Additional manufacturing capacity coming on stream at Land Systems in Canada, expanding the geographical reach into new geographical markets
- A new contract has been secured with the Royal Netherlands Army to supply military container systems for the storage of ammunition (MatlogCo)
- Increasing residential sales within Marshall Property
- Planning consents coming through later in the year for the later phases of the Marleigh development
- Recovery of food service and hospitality income streams at Fleet Solutions
- Higher revenues generated by a widening of the contract with Tesco
- The new Tamworth ‘supersite’ opening during Q2 2022
- Growth from the Renewables sub-division of Fleet Solutions
- A move to profitability for the two newer divisions, Marshall Skills Academy and Futureworx.

Summary Income Statement					
Year to Dec, £m	**2017A**	**2018A**	**2019A**	**2020A**	**2021A**
Aerospace				229.3	232.7
Land Systems				44.2	40.6
Advance Composites				10.3	8.3
Aerospace & Defence	295.4	247.8	307.6	283.8	281.6
Property	8.0	8.0	7.8	8.1	7.9
Fleet Solutions	42.8	47.4	53.0	45.7	54.3
Other				13.2	3.9
Intercompany	-24.2	-6.1	-6.5	-17.1	-4.6
Revenue	322.0	297.1	361.8	333.7	343.1
Y-o-Y growth		-7.7%	21.8%	-7.8%	2.8%
CoGS	-228.6	-181.0	-238.5	-250.7	-255.0
Gross profit	93.4	116.1	123.3	83.0	88.1
Gross margin	29.0%	39.1%	34.1%	24.9%	25.7%
Aerospace				16.2	7.1
Land Systems				2.2	-6.1
Advanced Composites				0.2	0.4
Aerospace & Defence	3.5	15.4	18.2	18.5	1.4
Property	3.4	2.1	2.9	3.7	9.8
Fleet Solutions	-1.4	-1.4	-1.2	0.2	0.2
Other	0.0	0.0	0.0	-1.1	0.0
Central shared services	-7.0	-6.2	-8.2	-5.7	-6.2
Adj. EBIT (pre-amortisation)	-1.4	9.7	11.9	15.6	5.2
Aerospace & Defence	1.2%	6.2%	5.9%	6.5%	0.5%
Property	42.7%	26.3%	37.7%	45.8%	123.6%
Fleet Solutions	-3.3%	-3.0%	-2.2%	0.4%	0.3%
Other				-8.1%	-0.3%
Total % EBIT margin	-0.4%	3.3%	3.3%	4.7%	1.5%
Net Interest	-8.9	-5.7	-6.6	-0.1	0.0
PBT (Adjusted)	-10.3	4.0	5.3	15.5	5.1
Adj. Tax	-6.7	-11.1	-6.7	-4.6	-1.4
Adj. PAT	-16.9	-7.1	-1.4	10.9	3.8
Minority interests	-15.0	-2.0	-3.9	-0.6	0.0
Pref. dividends	-0.7	-0.7	-0.7	-0.7	-0.7
Earnings	-32.6	-9.8	-6.0	9.5	3.0
EPS (Adjusted) (p)	9.8	33.9	35.3	41.3	5.1
Dps (p) - Voting, ordinary	4.0	4.0	1.0	7.0	5.9
DPS (p) - NVPO	6.0	6.0	3.0	9.0	7.9
Ave no of shares (FD) (m)	59.1	59.1	59.1	59.1	59.1

Source: Company historics

We highlighted earlier the greater focus on shareholder value and targeted divisional returns. What do we think this means moving forward? Historical data consists of the core division as Aerospace and Defence, since split into three. EBIT margins peaked at 6.2% in FY18. On that basis, we suspect a demanding but potentially achievable medium term margin target for the three is c.6.25% (FY21 actual amounted to £1.4m or 0.5%, albeit in the middle of a pandemic).

We envisage different growth rates by segment, with the Aerospace facilities operating at or close to full capacity and therefore requiring investment into additional facilities to further expand beyond any change in working practices post-pandemic. In view of the decline within Land Systems in FY21 and the new capacity coming on stream in Canada in early FY23, we have assigned a higher rate of growth of a CAGR of 7.5% to 2025. Similarly, while there remains a degree of capacity within Advanced Composites, we suspect further investment is required to 'push the envelope' and have therefore suggested a CAGR of 6% to 2025. **The combination of growth rates and efficiency improvements underway and anticipated, a margin of 7%+ is not out of the question, in our opinion. That would suggest EBIT of c.£26m is achievable in FY25F.**

MGP, the Group's property division, is by its nature relatively unpredictable with profitability dependent not only on sales of completed dwellings but also rental income and the 'lumpier' sales of individual (commercial) properties or parcels of land. However, we see little reason why the cash and profits stream shouldn't improve from here (phases 2 and 3 of Marleigh are yet to sell, with phase 1 only part-completed). On this basis, we surmise that £10m pa is likely to be comfortably achieved by FY25.

With MFS now consistently in the black (for the second successive year), the next stage is to improve margins. A sub-1% margin is unacceptable but investment within the business, coupled with the return of commercial vehicle sales and the new (green) income streams, is expected to result in a pick-up in top-and-botttom lines, Again, a suggested 6% top-line growth pa and a margin of 4% (squeezed by its master franchisor, Thermo King and the supermarkets), hints at EBIT of c.£2.7m by FY25.

The Skills Academy and Futureworx should be relatively well established by FY25 but will remain relatively small in the context of the wider group. On this basis, we have assigned little by way of revenues and EBIT to remain conservative.

We think the above suggests that Group EBIT could well rise to c.£38m by FY25 on revenues of £400m+.

Use of the consideration for MMH

The consideration for MMH amounted to c.£202m before associated costs. Further monies will be forthcoming from the three separate disposals completed in either FY21 or during Q1 2022. Options for use of the proceeds centre around the following:

- Repayment of debt
- Growth capital to be utilised within several of the remaining businesses
- A return of capital to shareholders.

Period end net debt of £41.2m, net proceeds of c.£220m (including a portion of the deferred consideration of the non-motor related disposals), suggests net cash of £170m+, excluding the return of cash to investors. Also, the current banking facility has a borrowing ceiling of £75m, suggesting significant headroom for further expansion of the Group.

What is the likely focus of growth capital? We think the securing of the Group's first US C-130J MRO contract, with the hope of securing further US DoD work is likely to result in MCH examining a dedicated facility in the US.

Similarly, funds have already been committed to the expansion in Canada, with a new manufacturing facility to be completed by the end of 2022 in Moncton, New Brunswick, creating an estimated 65 new roles.

With the RAF of potentially less importance from Q2 2023, there is an argument for moving to smaller UK facilities at Cranfield earlier than previously anticipated, simultaneously expanding the network of international aerospace MRO sites, to better service ongoing customers.

The debt increased markedly during the 12-months to December, albeit it remains at comfortable levels (net debt/EBITDA of < 2x, gearing of 33.7%). The increase in indebtedness reflected the sharp rise in working capital as the Group sought to maintain its high service levels to customers in the face of supply chain shortages. As the shortages ease, this is expected to result in a reversal and a subsequent inflow of cash.

Capex, or rather the disposal of assets and most prominently the Land north of Cherry Hinton (LNCH), was a key feature during the year. Apart from Martlet Capital, the bulk of the proceeds from the disposals announced in FY21 will be received in FY22 to FY24. The net level of M&A amounted to zero, reflecting the receipt for the bulk of Martlet Capital was payable in FY22.

Summary Cash Flow (FY17-FY19A incls. MMH)

Year to Dec, £m	2017A	2018A	2019A	2020A	2021A
EBITDA	76.4	75.5	67.3	14.8	2.2
Working capital movement	9.8	34.4	24.5	-12.7	-34.7
Other	25.2	-58.4	-19.7	-1.2	-0.6
Operating cash flow	111.4	51.5	72.1	0.9	-33.1
Net Interest	-8.4	-6.4	-7.1	-0.3	-0.4
Pref. dividends	-0.7	-0.7	-0.7	-0.7	-0.7
Minority payment	-1.6	-1.8	-2.6	0.0	0.0
Taxation	-2.6	-6.7	-3.4	1.1	-2.3
Cash earnings	98.0	35.8	58.3	1.0	-36.5
Net capex	-31.3	-39.9	-45.6	-19.2	12.8
Post capex cash flow	66.7	-4.1	12.7	-18.2	-23.6
Dividends	-3.3	-3.3	-3.3	-3.3	-3.3
Free cash flow	63.4	-7.4	9.4	-21.4	-26.9
Net (Acqns)/Disposals	44.3	-0.1	-28.2	0.0	0.0
Share Issues	0.0	-1.0	-0.7	0.0	0.0
Other financial	20.3	0.1	-3.0	-0.1	1.7
Increase Cash/(Debt)	128.1	-8.3	-22.5	-21.5	-25.3
Opening Net Cash/(Debt)	-122.2	5.9	-2.4	5.6	-15.9
Closing Net Cash/(Debt)	5.9	-2.4	-24.9	-15.9	-41.2

Source: Company historics, Equity Development estimates

The balance sheet remains asset heavy, even following the disposal of the motor retail division. However, most of the assets are included at cost, hiding the real value. The value of the Cambridge Airport site has started to be unlocked, although excluding the Marleigh and LNCH developments, a further 670 acres remain available for development.

Ultimately, it is envisaged that the Airport site could provide up to 7,000 homes (c.13 per acre), suggesting that any development could well stretch well into the 2030s and generate substantial levels of cash and profits for the Group.

The sharp rise in working capital reflects a combination of the need to increase inventory levels to ensure a continuity of service to customers and an increase in the amounts owed by joint ventures, specifically relating to the Marleigh development and the associated land transfers.

The balance sheet highlights that the pension fund is no longer in deficit and as such, there will be no ongoing payments required in the medium term, reflecting changes in discount rates.

Abbreviated Balance Sheet (FY17-FY19A incls. MMH)

Year to Dec, £m	2017A	2018A	2019A	2020A	2021A
Intangible Assets	106.4	86.4	87.0	13.1	12.0
Tangible Assets	218.9	237.9	271.7	100.8	87.4
Investments/other	4.8	6.6	7.9	42.3	5.3
Net Working Capital	-15.7	-17.4	-17.9	17.2	110.0
Capital Employed	314.4	313.5	348.6	173.4	214.7
Other	-18.4	-23.5	-28.1	-18.9	-19.0
Net Cash/(Debt)	5.9	-2.4	-24.9	-15.9	-41.2
Provisions	-71.3	-36.5	-25.1	-11.8	-18.0
Pension liability			0.0	-4.6	0.0
Shareholders' funds	167.7	188.0	205.6	122.1	136.5
Non-controlling interest	-63.0	-63.1	-64.9	0.0	0.0
Net Assets	230.7	251.1	270.6	122.1	136.5

Source: Company historics, Equity Development estimates

Valuation

Sum-of-the-Parts valuation

We believe the ideal methodology in determining the value of MCH today is a sum-of-the-parts model (SOTP).

Commencing with the **Aerospace and Defence** business, we have assigned 85% of the 2025 average EV/EBITDA sector multiple to an estimate of the divisional EBITDA.

The discounted average multiple for FY22 is 85% of 12.1x, equating to 10.3x and our expectation for FY2025F EBITDA, is £26m, discounted by 12% per annum suggesting a valuation of £190.3m.

The property business, **MGP**, is at a relatively early stage of the development process of the Cambridge Airport site. To date, two developments have commenced/achieved outline planning permission - Marleigh, comprising 160 acres and 1,300 homes and developed via a joint venture partnership, and LNCH which was sold in April.

The 230 acres utilised across Marleigh and the recently disposed LNCH forms part of the 900-acre site. It is anticipated that the relocation of the airport would ultimately result in approximately 7,000 residential properties, up to two million square feet of business and commercial space and several schools, community centres and high-speed public transport connections.

For every 100 acres that is freed up, excluding Marleigh's three phases and LNCH, we estimate this to be worth an incremental £40m to MGP.

The development should be sufficiently advaced to enable the airport site and related hangars to re-locate to a new home by 2030.

We anticipate two cash streams generated by MGP, rental and profits on disposal.

- Profits from developments
- Rental stream

The former we have valued at the estimated cash flow, discounted at 10% per annum, suggesting £93.3m. The property rental stream has been assigned a multiple of 10x on FY21 EBIT to produce, £97.9m.

On this basis, we feel that a reasonable valuation for MGP is £191.2m.

The proceeds from the disposal of MMH, the Group's motor retail subsidiary was received during June 2022, amounting to c £202m.

The **MFS** division delivered a modest profit during FY21. We expect the division to build on this, with profitability to continue to improve over the medium term as the range of services increase (to include renewables) and the food service and hospitality sectors return.

We have afforded the division a modest valuation (6x EV/EBITDA) on estimated FY25 profitability (EBITDA) and discounted back by a very conservative 12% per annum. **On this basis, we anticipate MFS to be worth c.£25.4m.**

Aeropeople was disposed of in March for a valuation equating to its NAV, that is, £0.6m. A loan of £0.6m was provided to the business ahead of disposal, which results in expected cash proceeds £1.2m in due course.

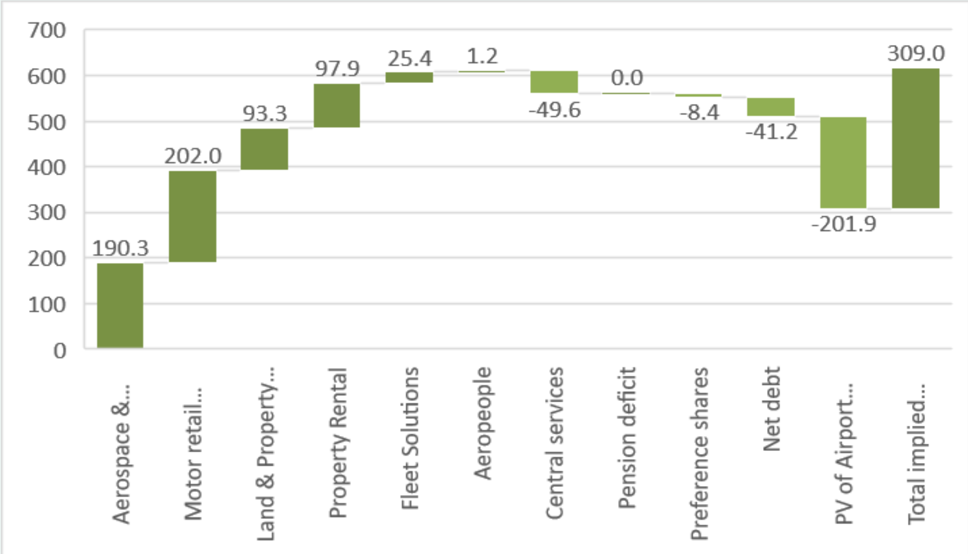
To reach the valuation as stated in the SOTP chart, we exclude the following:

- Central services (8x central costs), equating to £49.6m
- Pension deficit of £0.0m at the end of FY21
- Preference shares of £8.4m

With net debt on the balance sheet of £41.2m as of 31 December 2021, this produces an implied equity value of £309.0m and equates to 523p per NVPO share. The value per share represents a 23.1% premium to the last traded share price of 425p.

It is worth noting that we have factored in the cash flows from the property development streams up to and including 2030. The date reflects our expectation of the timing of the move to the new airport site, with the PV of the cost of the move discounted back to 2022. However, significant cash flow is expected to emerge between 2030 and 2040, with the newly vacated airport developed as part of the plan for Cambridge East.

SOTP valuation, £m



Source: ED

Assumptions underpinning our SOTP valuation

	£m	Assumptions
Aerospace & Defence	190.3	85% of 2022 Sector rating x FY2025 EBITDA, discounted at 12% pa
Motor retail proceeds	202	Proceeds of disposal of MMH
Land & Property Develpt.	93.3	Est. cashflow, discounted at 10% pa
Property Rental	97.9	10x 2021 EBIT
Fleet Solutions	25.4	6x 2025 EV/EBITDA, discounted at 12% pa
Aeropeople	1.2	Disposal proceeds and loan provided
Central services	-49.6	10x FY21 central costs
Pension deficit	0.0	No pension deficit as at the end of FY21
Preference shares	-8.4	Hypothetical 7% yield into perpetuity
Net debt	-41.2	As at December 2021
PV of Airport move	-201.9	£500m cost at 2030, discounted at 12% pa
Total implied Equity Value	309.0	
Shares in issue, m	59.082	Voting & non-voting shares
Valuation per share	523p	
Current share price	425p	
Difference	23%	

Source: Equity development

Contacts

Andy Edmond
Direct: 020 7065 2691
Tel: 020 7065 2690
andy@equitydevelopment.co.uk

Hannah Crowe
Direct: 0207 065 2692
Tel: 0207 065 2690
hannah@equitydevelopment.co.uk

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More information is available on our website www.equitydevelopment.co.uk

Equity Development, 16-18 Finsbury Circus, London, EC2M 7EB

Contact: info@equitydevelopment.co.uk | 020 7065 2690