

paragon

Full year results

€1bn lifetime order backlog poised for delivery

paragon's full year results highlighted the substantial progress the group has made in both its historic core businesses and the new divisions. With record sales, operating profit and an order book in excess of €1bn, the group has significant visibility over the next five years. 2016 is likely to be a year of more moderate growth ahead of a planned ramp-up in electromobility that will accelerate from 2017. With further potential catalysts anticipated as new product launches come to market, we believe that paragon is clearly aligned to automotive megatrends.

Year end	Revenue (€m)	PBT* (€m)	EPS* (€)	DPS (€)	P/E (x)	Yield (%)
12/14	79.0	4.3	0.67	0.0	39.6	N/A
12/15	95.0	5.0	0.83	0.0	32.0	N/A
12/16e	105.6	7.4	1.20	0.0	22.1	N/A
12/17e	134.7	11.4	1.86	0.0	14.3	N/A

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

Full year results highlight progress

Paragon's FY15 results demonstrated the group's growth potential, with revenues up 20.2% to €95.0m, 65% of which were single source, while EBIT increased by 24.9% to €7.8m in line with our forecast. This was achieved despite a year of significant investment in new product development, opening of production facilities in the US and China and further development of electromobility. Excluding one-off incremental expenses related to new business areas, adjusted EBIT margins increased to 12.6% (FY14: 11.7%), highlighting the underlying margin potential. Our forecasts reflect more moderate growth in 2016 before a further ramp-up in 2017.

Positioned for substantial growth

The group has clearly positioned itself to capitalise on the automotive megatrends of health, connectivity and CO₂ reduction across its business. Through its development approach, it is poised to continue to see benefits from both increased volumes and increased value per vehicle, with the group's average price per product in 2015 increasing by c 16% compared to 2014. With the core business continuing to grow, new product areas such as electromobility accounting for a substantial portion of the order backlog and the opening of the new international facilities, we believe that paragon is set to sustain its growth trajectory. This is supported by several new orders received across all divisions.

Valuation: Visibility of order book not yet recognised

We believe that the current rating of c 14x CY17 EPS does not fully reflect the substantial visibility afforded to paragon by the €1bn lifetime order backlog, including 95% cover for FY16 forecasts. Our DCF-derived fair value, attempting to capture future growth potential from existing contracts, increases to €33.8/share (previous €29.7) to reflect backlog phasing. We also see further upside potential as new contracts are won and the ramp-up is achieved over the next three years.

Automobiles & parts

14 April 2016

Price €26.5

Market cap €109m

Net debt (€m) at 31 December 2015 39.4

Shares in issue 4.1m

Free float 48%

Code PGN

Primary exchange Frankfurt

Secondary exchange N/A

Share price performance



Business description

paragon designs and manufactures advanced automotive electronics solutions as a direct supplier to the automotive industry. Products include sensors, acoustics, cockpit, electromobility and body kinematics. Production facilities are in Germany, the US and China.

Next events

Q1 interim report/AGM 27 April 2016

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Poised for accelerating growth

2015 results highlight growth potential

paragon's 2015 results highlighted the impact of the growth across all business lines:

- **Revenues** increased by 20.2% to €95.0m, with double-digit growth across all business segments including the traditional core with a 16% increase in the Cockpit segment to €31.9m and 11% growth in both Sensors and Acoustics to €34.6m and €16.1m respectively. A substantial ramp-up in Body Kinematics, up 32% to €5m, and Voltabox, up 260% to €7.4m, highlighted how these new segments have entered a growth phase.
- **EBITDA** increased by 35% to €14.2m despite significant investment in R&D and new product development providing a 170bp increase in EBITDA margin from 13.3% to 15.0%. Adjusted EBITDA, excluding c €4.4m of one-off expenses related to investment in the new business areas, increased by 37.9% to €18.6m at an adjusted EBITDA margin of 19.6% (FY14: 17.1%).
- **EBIT** increased by 25% to €7.8m, a 30bp increase in EBIT margin from 7.9% to 8.2%. Adjusted EBIT, excluding €4.2m of one-off expenses related to the investment in the new segments, increased by 29.6% to €12.0m at an adjusted EBIT margin of 12.6% (FY14: 11.7%).

Importantly, 2015 also signalled the peak year of investment at €32.3m, opening international production operations in Texas, US and Kunshan, China, while also expanding existing product lines and through the acquisition of SphereDesign, which is now integrated into the cockpit division. As a result, we see investment dropping in FY16 to €14m and subsequently dropping further again in FY17 to a more normalised level of maintenance capex, around €3-4m. This should see cash generation improving further and net debt levels dropping from our assumed peak of €43.1m in FY16. Focus will turn from the high levels of investment to delivering the ramp-up, particularly in Voltabox, which we forecast will become the largest contributor post 2017.

Contract wins provide a further impetus

Over the past five years, paragon has been successful in ensuring that it has been developing key technologies that support a number of the global automotive megatrends. In particular, the combination of the group's historic sensors business, with a detailed understanding of electronic control systems, has enabled it to concentrate on the key areas of health, connectivity and CO₂ reduction across the group. 2015 demonstrated that paragon's significant investment in R&D over the past decade has positioned it in the sweet spot of current requirements, with a number of divisions securing new contracts as a result, as shown in Exhibit 1 below.

Exhibit 1: Significant contract wins in 2015

Contract win	Division	Megatrend
Bulk order starter batteries for German automotive OEM (€72m over 6 years)	Voltabox	Electromobility (CO2 reduction)
High-performance batteries for trolley buses, commercial vehicles and intralogistics	Voltabox	Electromobility (CO2 reduction)
Spoiler systems for six vehicle types	Body Kinematics	CO2 reduction
Air Quality Sensors for Chinese customers	Sensors	Health
Belt microphone for a new model	Cockpit	Connectivity
Gauges for various vehicles	Cockpit	Connectivity
Charging tray for contactless charging	Cockpit	Connectivity

Source: paragon, Edison Investment Research

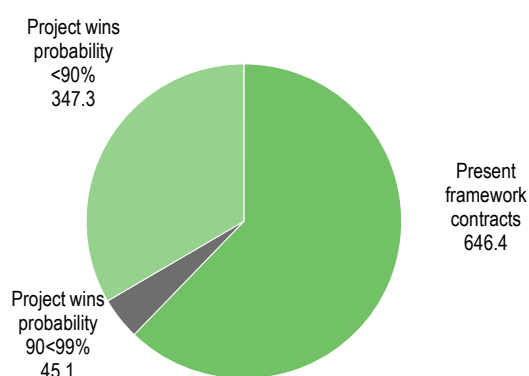
The product offensive also developed further during 2015 with several new launches at both the Frankfurt Motor Show, IAA in September 2015 and at the Consumer Electronics Show (CES) in January 2016. We visited the IAA and witnessed firsthand the new products, with many integrated on the Artega Scalo. New products included MirrorPilot wireless smartphone integration to the vehicle display, a lightweight surround sound audio system and numerous efficient electric motors, inverters and battery packs. Each of these developments highlights the approach paragon takes

with respect to identifying trends and developing solutions that the automotive manufacturers then adopt.

Backlog development highlights growth opportunity

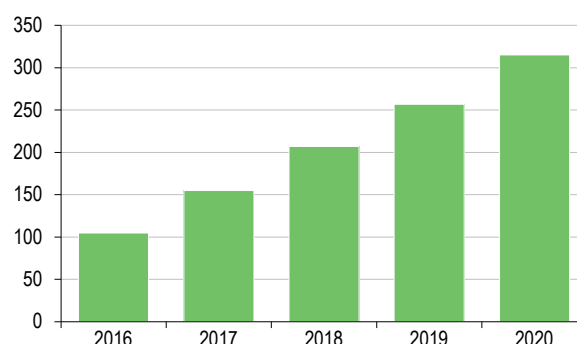
Exhibit 2 below highlights that paragon has a lifetime order backlog of over €1bn, or more than 10 years at current revenue rates. Of this, c €650m of those orders are already under framework contracts providing significant visibility to the group. Of the total backlog, c 35% relates to the electromobility segment, while a further 5% is derived from Body Kinematics. Exhibit 3 below highlights management's expected order phasing, with a significant growth trajectory highlighted in the order book. We note that our forecasts are more conservative than those suggested in the backlog, which we believe is prudent at this ramp-up stage as serial production commences in the new segments.

Exhibit 2: Order backlog by type (€m)



Source: paragon FY15 results presentation

Exhibit 3: Order backlog phasing



Source: paragon FY15 results presentation

Forecasts adjusted for mix and backlog

Following the FY15 results, we are broadly maintaining our forecasts with a minor adjustment in the relative business mix and phasing across 2016/17, as shown in Exhibit 4 below.

Exhibit 4: Edison forecasts by business segment

€m	FY14	FY15	FY16e 'old'	FY16e 'new'	Change	FY17e 'old'	FY17e 'new'	Change
Revenue								
Sensors	31	35	34	35	2.5%	34	36	4.5%
Acoustics	14	16	15	16	7.9%	15	17	12.2%
Cockpit	28	32	34	33	-4.8%	35	34	-3.9%
Body Kinematics	4	5	12	7	-41.1%	18	14	-21.4%
Voltabox (Germany)	1	4	5	5	0.0%	15	15	0.0%
Voltabox (US)	1	4	10	10	0.0%	18	19	5.6%
Group	79	95	110	106	-4.1%	135	135	-0.6%
Other income	7	17	10	14	44.8%	8	9	17.8%
Group operating performance	86	112	120	119	-0.1%	143	144	0.4%
COGS	-42	-56	-58	-60	3.5%	-72	-75	4.2%
Gross Profit	44	57	61	59	-3.6%	71	69	-3.4%
Personnel expenses	-22	-26	-27	-27	-2.3%	-33	-32	-3.5%
Depreciation of PPE & amortisation of intangibles	-4	-6	-7	-6	-12.9%	-7	-6	-12.9%
Impairment of PPE & intangibles	0	0	0	0	n/m	0	0	n/m
Other operating expenses	-12	-16	-17	-16	-1.8%	-18	-17	-1.8%
Group EBIT	6	8	10	9	-4.2%	14	13	-0.8%
Underlying Net Interest	-2.0	-2.8	-2.1	-2.1	0.0%	-2.0	-2.0	0.0%
PBT (EBT)	4.3	5.0	7.8	7.4	-5.3%	11.6	11.4	-0.9%
Tax	-1.5	-1.6	-2.6	-2.4	-5.3%	-3.8	-3.8	-0.8%
Net Profit	2.8	3.4	5.2	4.9	-5.3%	7.7	7.7	-1.0%
EPS (normalised)	0.67	0.83	1.27	1.20	-5.3%	1.88	1.86	-1.0%

Source: Edison Investment Research

Valuation supported by backlog phasing

We continue to provide a fair value view based on a DCF-derived valuation methodology as we believe that this best captures the value of the growth opportunity. Our DCF-based fair value is €33.8/share as shown in Exhibit 5 below. This is backed up by the lifetime order backlog and we feel this could prove to be conservative if paragon can deliver further contract wins and/or delivers the existing ramp-up quicker than we forecast.

Exhibit 5: DCF fair value assessment												
€m	2016e	2017e	2018e	2019e	2020e	2021e	2022e	2023e	2024e	2025e	2026e	
Assumptions												
Sales	106	135	155	170	179	188	197	203	209	213	218	
% change	n/a	27.6%	15.00%	10.00%	5.00%	5.00%	5.00%	3.00%	3.00%	2.0%	2.0%	
EBIT	9	13	16	18	19	20	21	21	22	22	23	
% margin	9.0%	10.0%	10.2%	10.4%	10.5%	10.5%	10.5%	10.5%	10.5%	10.5%	10.5%	
% change	n/a	41.8%	17.5%	12.2%	6.0%	5.0%	5.0%	3.0%	3.0%	2.0%	2.0%	
Tax	(2)	(4)	(5)	(6)	(6)	(7)	(7)	(7)	(7)	(7)	(8)	
% tax rate	33.0%	33.0%	33.0%	33.0%	33.0%	33.0%	33.0%	33.0%	33.0%	33.0%	33.0%	
NOPAT	7	10	11	12	13	13	14	14	15	15	15	
% margin	6.7%	7.2%	6.8%	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%	
% change	n/a	37.2%	9.5%	12.2%	6.0%	5.0%	5.0%	3.0%	3.0%	2.0%	2.0%	
Depreciation & Amortisation	6	6	7	8	8	8	9	9	9	10	10	
Change in working capital	0	(5)	(5)	(5)	(5)	(5)	(4)	(4)	(4)	(4)	(4)	
Capex	(14)	(5)	(3)	(3)	(3)	(3)	(3)	(3)	(3)	(3)	(3)	
Free cash flow to firm	(1)	6	10	12	13	13	16	16	17	18	18	
WACC	9.0%	9.0%	9.0%	9.0%	9.0%	9.0%	9.0%	9.0%	9.0%	9.0%	9.0%	
Year	1	2	3	4	5	6	7	8	9	10	11	
Discount factor	1.09	1.19	1.30	1.41	1.54	1.68	1.83	1.99	2.17	2.37	2.58	
Present value free cash flow	(1)	5	7	8	8	8	9	8	8	8	7	
Cumulative present value	(1)	4	12	20	28	36	45	53	61	68	76	
Net present value - forecast FCF	76							WACC				
Net present value - terminal year	103				34.32	7.0%	8.0%	9.0%	10.0%	11.0%		
Enterprise Value	179				41.9	34.2	28.3	23.6	19.8	41.9		
					47.0	37.7	30.7	25.3	21.1	47.0		
Net debt	(39)				54.2	42.3	33.8	27.5	22.7	54.2		
Minorities	0				65.0	48.8	38.0	30.4	24.6	65.0		
Value attributable to shareholders	139				82.9	58.5	43.8	34.1	27.2	82.9		
Shares outstanding (m)	4.1											
Value per share (€)	33.8											

Source: Edison Investment Research

Exhibit 6: Financial summary

	€m	2011	2012	2013	2014	2015	2016e	2017e
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS								
Revenue		67.1	70.4	73.9	79.0	95.0	105.6	134.7
Other operating income		1.9	2.0	1.1	1.4	3.2	3.4	3.6
Increase or decrease in inventory of finished goods / WIP		0.1	0.6	0.3	0.8	1.4	0.5	0.5
Other own work capitalised		1.3	2.0	1.7	5.2	12.8	10.0	5.0
Group operating performance		70.3	75.1	76.9	86.3	112.4	119.5	143.8
Cost of Sales		(33.7)	(37.0)	(36.3)	(41.8)	(55.5)	(60.3)	(74.8)
Gross Profit		36.7	38.1	40.6	44.5	56.9	59.2	69.0
EBITDA		12.9	11.7	12.2	10.5	14.1	15.8	19.9
Operating Profit (before amort. and except.)		8.8	7.8	7.9	6.2	7.8	9.5	13.4
Intangible Amortisation		0.0	0.0	0.0	0.0	0.0	0.0	0.0
Exceptionals		0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other		0.0	0.0	0.0	0.0	0.0	0.0	0.0
Operating Profit		8.8	7.8	7.9	6.2	7.8	9.5	13.4
Net Interest		(1.3)	(1.1)	(1.5)	(2.0)	(2.8)	(2.1)	(2.0)
Profit Before Tax (norm)		7.5	6.7	6.4	4.3	5.0	7.4	11.4
Profit Before Tax (FRS 3)		7.5	6.7	6.4	4.3	5.0	7.4	11.4
Tax		(2.2)	(2.1)	(2.5)	(1.5)	(1.6)	(2.4)	(3.8)
Profit After Tax (norm)		5.3	4.6	3.9	2.8	3.4	4.9	7.7
Profit After Tax (FRS 3)		5.3	4.6	3.9	2.8	3.4	4.9	7.7
Average Number of Shares Outstanding (m)		4.1	4.1	4.1	4.1	4.1	4.1	4.1
EPS - normalised (€)		1.30	1.13	0.96	0.67	0.83	1.20	1.86
EPS - normalised and fully diluted (€)		1.30	1.13	0.96	0.67	0.83	1.20	1.86
EPS - (IFRS) (€)		1.30	1.13	0.96	0.67	0.83	1.20	1.86
Dividend per share (€)		0.00	0.00	0.00	0.00	0.00	0.00	0.00
Gross Margin (%)		54.7	54.1	55.0	56.3	59.8	56.1	51.2
EBITDA Margin (%)		19.2	16.6	16.6	13.3	14.8	15.0	14.8
Operating Margin (before GW and except.) (%)		13.2	11.0	10.7	7.9	8.2	9.0	10.0
BALANCE SHEET								
Fixed Assets		17.1	18.6	18.8	30.1	59.7	64.3	60.0
Intangible Assets		3.3	4.9	5.6	9.4	24.7	22.7	20.7
Tangible Assets		13.3	13.5	13.0	20.2	34.6	41.2	38.9
Investments		0.6	0.1	0.2	0.5	0.4	0.4	0.4
Current Assets		24.3	25.4	33.1	32.3	32.9	32.9	38.9
Stocks		6.9	7.3	7.5	6.9	11.2	12.2	15.2
Debtors		2.1	4.0	8.0	12.2	13.2	12.2	15.2
Cash		11.2	10.1	16.3	11.8	8.5	8.5	8.5
Other		4.1	4.0	1.3	1.5	0.0	0.0	0.0
Current Liabilities		(14.4)	(13.9)	(12.2)	(16.2)	(27.1)	(16.4)	(15.4)
Creditors		(11.7)	(11.5)	(9.3)	(10.7)	(17.8)	(7.1)	(6.1)
Short term borrowings		(2.7)	(2.4)	(2.9)	(5.5)	(9.3)	(9.3)	(9.3)
Long Term Liabilities		(17.2)	(17.1)	(33.6)	(41.9)	(59.2)	(62.9)	(60.1)
Long term borrowings		(12.5)	(12.3)	(20.2)	(24.7)	(38.5)	(42.3)	(39.4)
Other long term liabilities		(4.7)	(4.8)	(13.4)	(17.1)	(20.7)	(20.7)	(20.7)
Net Assets		9.8	13.0	6.2	4.3	6.2	17.8	23.4
CASH FLOW								
Operating Cash Flow		11.4	9.2	8.4	10.3	16.4	15.8	14.9
Net Interest		(1.2)	(1.0)	(1.4)	(1.9)	(2.9)	(2.1)	(2.0)
Tax		(1.6)	(2.4)	(1.9)	(1.4)	(0.7)	(2.4)	(3.8)
Capex		(2.0)	(2.7)	(2.3)	(10.5)	(18.8)	(14.0)	(3.1)
Acquisitions/disposals		(1.3)	(3.5)	(2.5)	(5.2)	(13.5)	0.0	0.0
Financing		0.0	0.0	0.0	0.0	0.0	0.0	(2.1)
Dividends		0.0	0.0	(1.4)	(1.0)	(1.0)	(1.0)	(1.0)
Net Cash Flow		5.3	(0.3)	(1.2)	(9.7)	(20.5)	(3.7)	2.9
Opening net debt/(cash)		13.6	4.0	4.6	6.7	18.4	39.4	43.1
HP finance leases initiated		0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other		4.4	(0.2)	(1.0)	(1.9)	(0.5)	0.0	0.0
Closing net debt/(cash)		4.0	4.6	6.7	18.4	39.4	43.1	40.3

Source: Company accounts, Edison Investment Research

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