

## Robust outcome to a year of great change

16 August 2021

MCH performed strongly in what proved to be a challenging year. Profitability improved year-on-year and the Group maintained the payment of dividends throughout the pandemic. Cash flow was such that the group ended the year with net cash, even after investment in a new ERP system to be installed across the MADG. The order book within MADG remains strong, with new contracts signed in FY20 expected to ramp up during FY21. MMH has increased adj. PBT guidance for FY21 to record levels, with an intention to resume dividends as soon as possible. The Property division (MGP) has been active, with further house sales and a disposal of the Land North of Cherry Hinton with planning permission.

Considering all the above, we think the recent price of shares traded fails to reflect the good news and inherent value. While the decision by the UK MoD to retire its C-130 fleet is disappointing, if not unexpected, we still see many grounds for optimism. The level of the last matched share trade sits at a substantial discount to both our estimate of fair value and to the Group FY20 NAV, which we believe to be unwarranted.

FY20 proved to be an eventful year for MCH, with many of the services offered by MADG and Fleet Solutions ultimately deemed to be essential. Conversely, MMH dealerships closed throughout the two lockdown periods. MGP sold the initial homes on its Marleigh joint venture development, signalling the start of a growing profits stream from the land surrounding the Cambridge Airport site. MCH revenues declined modestly, while profitability improved y-o-y with a reinstatement of the dividend.

Several new contracts were secured, with several others extended. The highlight was the **10-year enabling agreement with the US Marine Corps (USMC)** for MRO on their 66-strong C-130 fleet and the initial 'trial' airframe delivered to MADG in December. We think this contract could prove highly significant over time, taking the number of customers on the aircraft to 17 and the USMC fleet dwarfing that of any other Group customer.

Since the year end, the UK MoD has announced that it is to retire the RAF's 14-strong fleet of C-130's in 2023. The early retirement of the fleet had been subject to rumour ahead of the announcement. Over the medium to longer term, the opportunity is whether MADG can secure the modification and repair work required by the new owners of the old RAF fleet. Should the trial with the USMC prove successful, the related and ongoing work is likely to more than compensate for the loss of the RAF's C-130 fleet. Other opportunities include the future siting of the Group's main aerospace MRO operations.

The year-end order book remains strong at £742m within MADG, and significantly the book-to-bill ratio remains above 1. The importance of the RAF declined during FY20 as new customers were signed. Hangar utilisation remains strong, which augurs well for the full-year outlook for MADG.

The Property division disposed of its interest in the Land North of Cherry Hinton in March 2021, resulting in a significant profit. This will have a positive result on both cash flows and divisional profitability. **MMH again increased guidance, due to the strong trading continuing into early Q3 and suggesting that FY21 adj. PBT would be not less than £40m, notwithstanding the repayment of £4m of government funds.**

### Inherent value

The most recent traded share price of 231p is materially below our retained fair value of 591p and stands at a large 39% discount to the FY20 Shareholder's Funds. Prospects remain exciting across the Group's portfolio as economic growth and confidence recovers.

### Marshall of Cambridge Holdings Ltd

Last matched NVPO trade	231p
Implied market cap	£137m
ED Fair Value per NVPO	591p
Ordinary share count	59.1m
Preference shares	£8.4m
Net cash (Dec '20)	£12.9m

### Share Price, p



Source: James Sharp & Co, ED

### Description

Founded in 1909, Marshall of Cambridge (Holdings) Ltd (MCH) is a private, family-owned company, employing 6,256 staff.

In 2020, the business generated c.£65.7m (FY19: £59.6m) of EBITDA on revenues of £2.49bn (FY19: £2.64bn) and has significant organic opportunities ahead. The world-class applied engineering services and technology business to the aerospace/defence sectors (MADG), is the core of the Group. The 64.41% owned motor retail business (MMH) delivers the bulk of revenues. The property division, MGP, is in the process of unlocking value from its 900-acre estate at Cambridge airport. Finally, the Group has a stake in high-tech venture capital investments, Martlet Capital.

The non-voting priority 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](mailto:david@equitydevelopment.co.uk)

### Andy Edmond

0207 065 2691  
[andy@equitydevelopment.co.uk](mailto:andy@equitydevelopment.co.uk)

## Preliminary results

**Marshall of Cambridge Holdings (MCH) has issued results for the full year to December 2020. The key features of the results are:**

- Revenues declined 5.7% to £2.49bn
- Strong performances within MADG, where revenues declined just 6.2% despite the disruption to working practices
- MMH significantly outperformed its markets, as revenues fell by only 5.3%, following lengthy dealership closures
- MGP saw revenues increase to £8.1m, a y-o-y increase of 3.9%
- Progress in profitability within all sub-divisions, except for Aerospace and Defence, where adj. PBT fell 3.4% to £17.5m. The reduction mostly reflected the performance at Aeropeople due to the sharp decline in civil aerospace
- Strong growth during H2, representing 57.9% of annual revenues, versus 49.0% in H2 2019 and a record half-yearly level of turnover
- Despite declining revenues as the restaurant/food service sector declined markedly, Fleet Solutions returned to profitability
- Adjusted PBT increased 11.1% to £39.1m
- A marked improvement to MGP's margin, reflecting the sale of an office property and the initial sales of homes on the Marleigh development
- Adjusted EPS increased 17% to 41.3p
- Three dividends paid/announced during the year, compared to one in 2019. However, the actual cash shareholders received in July and December was maintained at pre-pandemic levels
- Net cash of £12.9m by the year end, which compares to net debt of £24.9m a year earlier
- Shareholder's funds of £211.5m, which equates to 358p per share versus a current share price of 220p

## In summary

We think the FY20 outcome is a very positive one considering the disruption caused by the pandemic across every part of the business. From March 2020 onwards, working practices were overhauled, contracts reviewed with customers and each site saw working practices changed to best protect employees.

Nor has the progress gone unnoticed:



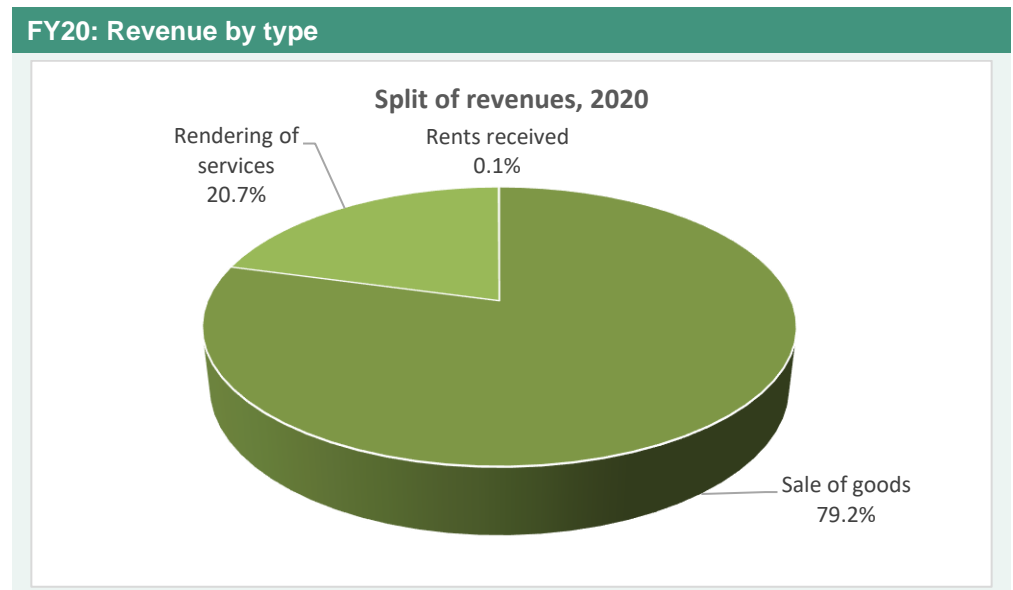
**2020 Preliminary results**

<b>£m, to 31 December</b>	<b>H1 19A</b>	<b>H2 19A</b>	<b>FY19A</b>	<b>H1 20A</b>	<b>H2 20A</b>	<b>FY20A</b>	<b>Change, y-o-y</b>
Aerospace and Defence	138.0	169.6	307.6	132.9	153.8	286.6	-6.8%
Property	3.8	4.0	7.8	3.3	4.8	8.1	3.9%
Ventures - Motor retail	1183.3	1092.9	2276.1	895.3	1259.1	2154.4	-5.3%
Ventures - Fleet Solutions	23.2	29.7	53.0	19.7	26.0	45.7	-13.7%
Consolidation adjustments	-2.3	-4.2	-6.5	-2.8	-3.9	-6.7	3.3%
Total revenue	1345.9	1292.0	2638.0	1048.3	1439.8	2488.1	-5.7%
Cost of sales	-1174.7	-1079.1	-2253.8	-891.5	-1275.4	-2167.0	-3.9%
Gross profit	171.2	213.0	384.1	156.8	164.4	321.2	-16.4%
Gross margin, %	12.7%	16.5%	14.6%	15.0%	11.4%	12.9%	
Operating expenses	-148.9	-194.8	-343.8	-185.9	-121.5	-307.3	-10.5%
Other Op income	0.1	1.1	1.2	17.2	15.3	32.5	
Aerospace and Defence	7.0	11.2	18.2	0.2	17.3	17.5	-3.8%
Property	1.5	1.4	2.9	1.5	2.8	4.3	50.2%
Ventures - Motor retail	18.7	11.2	29.9	-4.5	34.7	30.2	1.3%
Ventures - Fleet Solutions	-0.7	-0.4	-1.2	-0.2	0.4	0.2	-115.6%
Ventures - Martlet Capital						0.0	
Unallocated central costs	-4.0	-4.2	-8.2	-8.9	3.1	-5.8	-28.3%
Group adj. EBIT	22.4	19.2	41.6	-11.9	58.2	46.3	11.4%
Aerospace and Defence	5.1%	6.4%	5.8%	0.2%	11.2%	6.1%	
Property	39.3%	34.6%	36.9%	46.5%	58.0%	53.3%	
Ventures - Motor retail	1.6%	1.0%	1.3%	-0.5%	2.8%	1.4%	
Ventures - Fleet Solutions	-3.2%	-1.4%	-2.2%	-1.1%	1.5%	0.4%	
Group adj. EBIT, %	1.7%	1.5%	1.6%	-1.1%	4.0%	1.9%	
Net interest charge	-3.3	-3.3	-6.6	-3.6	-3.7	-7.2	9.7%
Exceptional items	-2.7	-5.3	-8.0	-3.8	-4.9	-8.6	7.9%
Adj. PBT	19.1	16.0	35.2	-15.5	54.5	39.1	11.1%
Taxation	-3.9	-2.8	-6.7	-0.3	-8.2	-8.5	27.3%
Tax, %	20.2%	17.4%	15.9%	-1.6%	15.1%	21.7%	36.0%
Minority interests	-3.5	-0.4	-3.9	4.9	-8.4	-3.5	-9.9%
Adj. Earnings	11.7	16.2	27.9	-20.6	47.0	26.3	-5.6%
Adj. EPS (p)	17.9	17.4	35.3	-18.4	59.7	41.3	17.0%
Div. on ordinary shares (p)	1.0	0.0	1.0	1.0	6.0	7.00	600.0%
Div. on NVPO shares (p)	3.0	0.0	3.0	3.0	6.0	9.00	200.0%
Net cash/(debt)	-12.3	-24.9	-24.9	25.7	12.9	12.9	-151.8%
Gearing, %	6.2%	9.2%	9.2%	-13.8%	-4.5%	-4.5%	
Interest cover (x)	6.8	6.3	6.3	n/a	6.4	6.4	
Shareholder's Funds per share (p)	334.4	348.1	348.1	314.6	365.8	365.8	5.1%

Source: Company

## Full Year trading by division

The split of revenue by type can be analysed as follows:



Source: Company

**Of total group revenue, the quantum recognised from long term contracts amounted to £278.4m (FY19: 291.1m), representing 54.0% of services rendered (FY19: 53.1%).**

### MADG

Revenues within MADG declined just 6.8% to £286.6m, which is a commendable achievement in view of the change in working practices and a significant number of the division's employees working remotely at times during 2020. Underlying PBT declined modestly to £17.5m (FY19: £18.2m), as a revised operating model was implemented, in turn removing duplicated costs and improving engineering utilisation. The associated exceptional cost of £2.4m, coupled with the £1.1m cost of creating the COVID-19 secure working environments were added to the £0.8m relating to R&D on the Exovent ventilator project as separately disclosed items.

### Marshall Aerospace

Forty-four aircraft were delivered to a widening customer base during FY20, following varying elements of maintenance. With customers generally consisting of national governments, most contracts were deemed essential and as a result, the hangars in Cambridge were full throughout most of the year, despite the delays and disruption caused by the necessity for Covid-19 safe working environments.

The strategic objective to diversify beyond the UK MoD continued, with **45% of 2020 aerospace revenues derived from international customers** (FY19: 36%). With the refurbishment of hangars now completed, capacity at the Cambridge Airport site has increased.

Several new contracts were secured during 2020, not least:

- The potentially game-changing ten-year enabling contract with the US Marine Corps, signed in October
- Delivery of the first centre-wing replacement aircraft to the RAF during 2020, with two further in FY21 (11 to complete)
- The signing of an option agreement for a 150-year lease within Cranfield University's Air Park

- Delivery of 'Fat Albert' C-130 for the US Navy's Blue Angels display team
- The renewal of a six-year MRO contract with the Danish and Norwegian Air forces (on their eight C-130s combined)
- Delivery of the final 'Global 6000 Integration' airframe
- 17<sup>th</sup> national C-130 MRO customer secured
- The first contract gained to install the new generation of lightweight cockpit armour on the Danish Air Force's C-130Js
- Re-painting of an RAF Voyager

### Land Systems

Revenues increased 6% to £43m (FY19: 40.5m) within the Land Systems sub-division. The year was a mixed bag with a strong performance as the DVOW (1,632 container systems to be supplied to the Dutch Armed Forces) contract ramped up to full production. Of this, 415 shelters were delivered throughout 2020, with margins as expected.

However, several projects were deferred, not least DALO (40 container-based advanced protected network and communication systems for the Danish Armed Forces).

The Gasket contract (upgrading existing counter chemical, biological, radiological, nuclear, and explosive vehicles for the UK MoD), secured in 2019, hit delays. The deferrals reflected customer-led design changes, impacting the margin. The Canadian Armed Forces received a shelter-based deployable CT scanner.

### Advanced Composites/Aerostructures/Aeropeople

Following the re-organisation of **Advanced Composites** in late 2019, the performance of the business was much improved, with the business moving back into the black. The improved performance was despite revenues declining to £10.4m (FY19: £12.7m). The outcome was aided by the re-bidding on a sizeable contract - cockpit panels for Lockheed Martin's C-130.

Following the cessation of 2019's supply chain disruption, trading within **Aerostructures** was predictable. The contract with Boeing to provide a lightweight fuel tank for the P8 military aircraft hit a milestone, with the 600<sup>th</sup> tank delivered during the year.

The loss-making **Aeropeople** secured a large contract at London Stansted Airport during FY20. However, in view of the disruption within the civil aerospace market due to the pandemic, the outcome for FY20 proved to be disappointing, if not unexpected. Revenues declined 50% to £12.5m y-o-y, with a re-sizing of the business undertaken during FY20. The sub-division was disposed of in mid-April 2021, with the consideration amounting to the net asset value of the business, £0.6m.

### Marshall Group Properties (MGP)

Revenues amounted to £8.1m (FY19: £7.8m), with EBIT rising markedly to £4.3m (FY19: £2.9m). The upwards spike in EBIT reflects residential house sales within the Marleigh development. Also, the sale and leaseback of an office building on the Cambridge Airport site, realised net proceeds of £10m and a profit on disposal of £7.4m.

The Marleigh development has witnessed **strong sales during FY20**, with the sales office opening in March and closing shortly thereafter. A high proportion of sales have been managed online. Despite the restrictions on site, the first residents moved into their new homes in November 2020 and ten completions were achieved by the year-end. The strong sales trend has continued into H1 2021, aided by the temporary Stamp Duty holiday and the Help-to-Buy scheme.

**Planning approval was granted** for the land North of Cherry Hinton (LNCH), with the s.106 legal agreement signed in December. The land was later sold in March 2021 to a developer. We discuss this in further detail at a later stage.

MGP continues to work alongside its development partners with the local planning authorities to ensure that Cambridge East is included in the Local Plan from 2030. The local authorities are expected to reveal the preferred sites for the next Local Plan later in the current year.

## Marshall Ventures

### Marshall Motor Holdings (MMH)

Despite the closure of all dealerships for several months post-23 March, **the outcome for MMH was extremely positive**. Following the re-opening of dealerships in June 2020, the business benefitted strongly from a combination of pent-up demand and a desire to avoid public transport for many of the public. All the following numbers for MMH are as reported externally in IFRS).

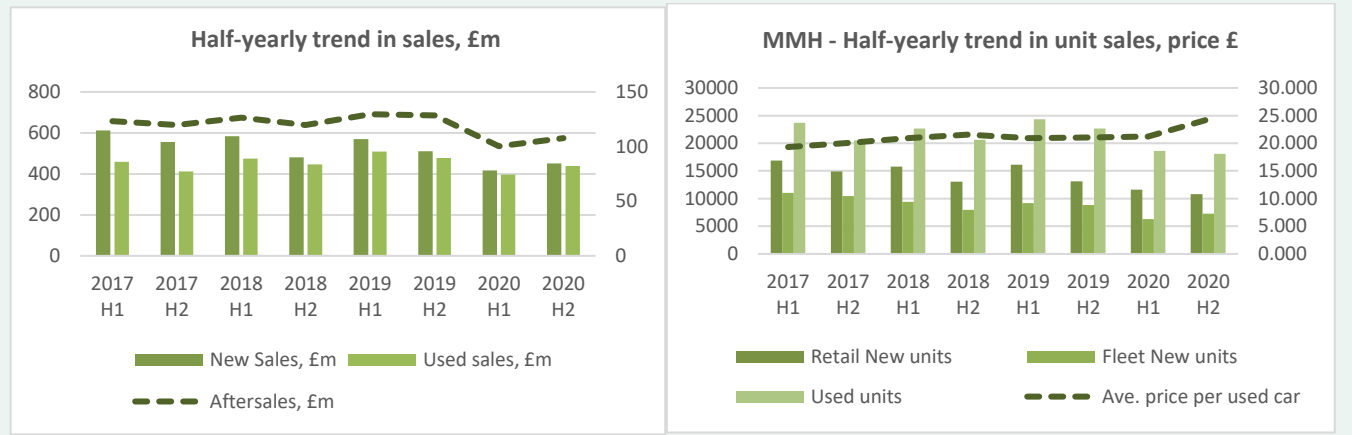
Overall divisional revenues fell 5.3% in total, equating to 13.5% on a like-for-like basis, to £2.15bn (FY19: 2.28bn). Adj. PBT of £20.9m was modestly lower y-o-y (FY19: £22.1m) but comfortably beat expectations, which increased from £15m to £19m in early December. The improvement in profitability, despite the closure of dealerships for long periods during the year, reflected the strong H2, cost control measures, partner support and government initiatives. The transition from physical to omni-channel retailing generated sales during lockdown (via the introduction of online reservation services and click-and-collect), and reflected the division's strong media presence, including:

- Motor Trader Awards, Winner in the social media category
- The Car Dealer Used Car Awards, Highly Commended in the social media category
- 6m visits to [www.marshall.co.uk](http://www.marshall.co.uk) (+0.3% yoy)
- TV advertising in live sports events

Once again, **the company significantly outperformed the wider car market**.

Revenues generated from new car sales declined 16.1% y-o-y on a l-f-l basis to £869m (FY19A: £1,035.7m) and compared to a 26.6% decline of the overall market for new passenger vehicles. Used vehicle revenues declined 10.1% y-o-y on a l-f-l basis, to £834.9m (£928.8m), while the wider market declined 14.9% y-o-y.

The ratio of used to new car ratio (retail) improved to 1.64:1 (FY19A: 1.59:1), partially offsetting the decline in revenues. Significantly, and aiding margins, used car revenues improved 11.0% on a H2/H1 sequential basis in FY20A and compared to an 8.2% uplift in H2 new car revenues.

**MMH: Half-yearly trend in sales and unit sales**


Source: Company, ED

Gross profit fell 8.7% to £238.2m (FY19A: £260.8m), resulting in a gross margin of 11.1%, representing a shortfall of just 40 bps, y-o-y. The gross margin on new cars was affected by the reduction in volumes, which resulted in lower manufacturer bonuses, declining 84 bps overall to 6.6%. A strong recovery in the used car market following the re-opening of showrooms in June, coupled with rising prices (+15.4% y-o-y), meant the used margin fell just seven basis points to 6.6%

The overall divisional gross margin benefitted from a changing mix in aftersales revenues, as a higher proportion of service revenue improved the outcome and reflected workshops re-opening to the public (non-key workers). Aftersales saw its GP margin rise 74 bps to 45.1% in 2020, in turn accounting for 45.8% of the Group's total gross profit, which was significant in the context of the sharp decline in vehicle sales during the year.

Four sub-scale franchised outlets were closed during FY20 (Cambridge Hyundai, Bury St. Edmunds Ford, Knebworth Vauxhall and Poole Mercedes Benz Commercial Vehicles). One new franchise was purchased, Aylesbury Volkswagen. Relocations and major rebuilds included:

- Newbury Audi
- Wimbledon Audi
- Derby Volvo
- Welwyn Volvo
- Oxford SEAT
- Kings Lynn Ford Commercial Vehicles

MMH sought to conserve cash during the year. This was achieved ahead of expectations through lower working capital requirement (reflecting the slowdown in activity), working capital declining to just £8.5m, net asset disposals of £1.4m (despite £3.2m of freehold purchases) and M&A falling to an outflow of just £2.9m (FY19A: -£27.4m).

**As a result, there was a £59.4m swing from debt to net cash of £28.8m during the year.**

### Marshall Fleet Solutions (MFS)

The Fleet Solutions business delivered a positive result for the year, notwithstanding lockdown related issues within the food service and hospitality sector, which removed a source of revenue for prolonged periods stretching into 2021. Not surprisingly, revenues declined 14% to £45.7m (FY19: £53.0m).

The restructuring of the business in H2 2019, with a new management team appointed and a reorganisation into five regional depots helped, lowering central costs, and returning the division to profitability (underlying PBT in FY20: £0.1m vs FY19: -£1.5m).

Most of the Fleet Solutions team were designated key workers, owing to their role in the distribution of food, pharmaceuticals, and other essential supplies. New contracts were secured in 2020, adding to the major agreement with Tesco home shopping fleet.

#### Successes included:

- The addition of the NHS as a customer (the rental of 179 trailers)
- The rapid growth in online grocery shopping (c.1.2m deliveries every week), and,
- Food distribution to supermarkets.

### Martlet Capital

Martlet Capital is an early-stage investor based in Cambridge, providing patient capital to deep technology and life science start-ups with high growth potential. No disposals occurred during FY20.

#### **The combined funds witnessed a fair value increase to £11.6m (FY19: £7.9m) during FY20.**

Six new companies and eight follow-on investments were made in the early-stage technology fund, Martlet Capital, with a combined value of £1.6m. Provisions of £0.4m were recognised during the year, reflecting the follow-on investment rounds completed at lower prices or an unlikely prospect of realisation. Also, a fair value increase of £0.2m (FY19: £0.2m) emerged in FY20.

The larger MarQuity fund completed three follow-on investments during 2020, amounting to a further £0.6m. The fair value of the fund increased £1.7m to £6.6m at the year end, including £0.9m on a company since disposed of. Six investments remain.



## Strong order books

### MADG

#### Marshall returns the first USMC KC-130J



Source: Jane's

The opening up of the US C-130 aircraft support market to international competition has benefitted MADG.

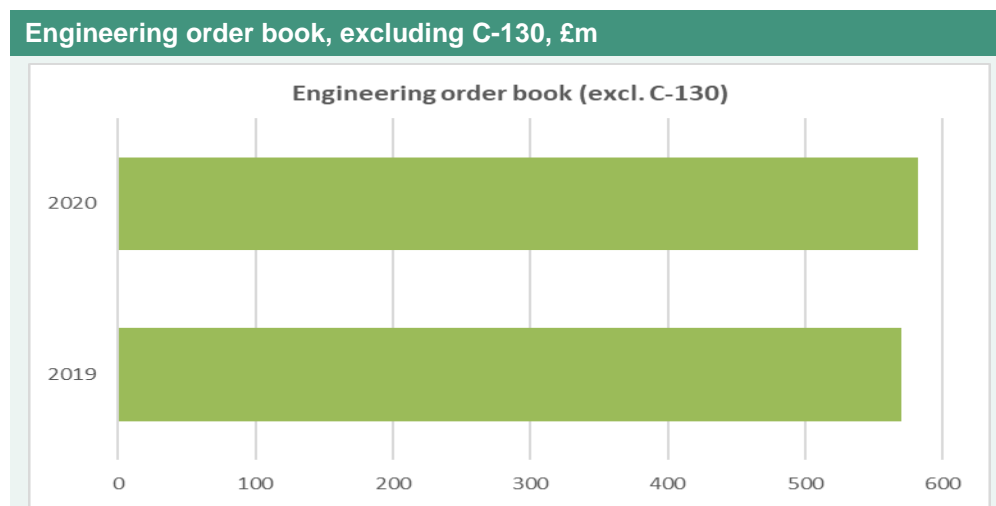
The securing of the first enabling contract with the US DoD and specifically, the US Marine Corps, saw the first aircraft delivered to Cambridge in December. The first tanker-transport airframe was returned to its USMC squadron in North Carolina in early July, following planned maintenance and repairs. With 66 C-130s, albeit competing (on time, quality, and price) with a third-party MRO operator, the potential for the USMC contract is significant.

The book-to-bill ratio amounted to 1.1:1 (FY19: 1.6:1), excluding the Hercules contract with the UK MoD, as orders of £192m (FY19: £334m) were received during the year. **The overall MADG order book stood at £742m at the year-end** (FY19: £817m) and, excluding the UK MoD C-130 contract, at £582m (FY19: £570m). This highlights the declining impact of the RAF C-130 on revenues, at 21.6% (FY19: 30.2%).

#### MADG rolling order book



Source: Company



Source: Company

In Land Systems, with the relatively 'standard' container-based systems complete, work has commenced on the more complex and added-value units in the contract with the Dutch Armed Forces.

MADG has also secured contracts with Canada, under its current Defence Investment Plan, on several equipment programmes over the next five years. Further contracts have been secured in programmes, particularly in deployable systems and mobile CT scanners.

Within Aerostructures, the Advanced Structures business is set to benefit from an extension of its key contract with Boeing to at least 2024, with scope for further extensions.

## MGP

In mid-March 2021, Marshall Group Properties (MGP) completed the sale of the land known as Land North of Cherry Hinton (LNCH) for £34.5m. The initial proceeds amounted to £8m, with the remainder payable in four equal annual instalments of £6.625m. **The profits related to the disposal amount to £22m**, subject to adjustments for land remediation and transaction costs. The purchaser was Bellway Latimer Cherry Hinton LLP, who will develop up to 1,200 homes, a primary school, secondary school, local centre, and spine road.

The extension of the Stamp Duty holiday until the end of June 2021, with a rise in the threshold to £250,000 until 30<sup>th</sup> September will continue to provide stimulus to the Group's property sales at Marleigh during H1 2021. The old Help-to-Buy scheme ended on 31<sup>st</sup> March 2021, with a replacement scheme running until the end of March 2023.

To date, a further 70 reservations have been made on phase one of the Marleigh development, with completion during 2021. We anticipate further reservations to be made in the remainder of the current year.

Planning approval was granted in November for the next element of phase one of the Marleigh development, increasing the number of dwellings to 547 in total in phase one. Approval was also granted for the sports facilities and pitches and the primary school (opening date September 2022). Phase two of the Marleigh development, comprising 400 dwellings, has entered the planning phase with the local authority.

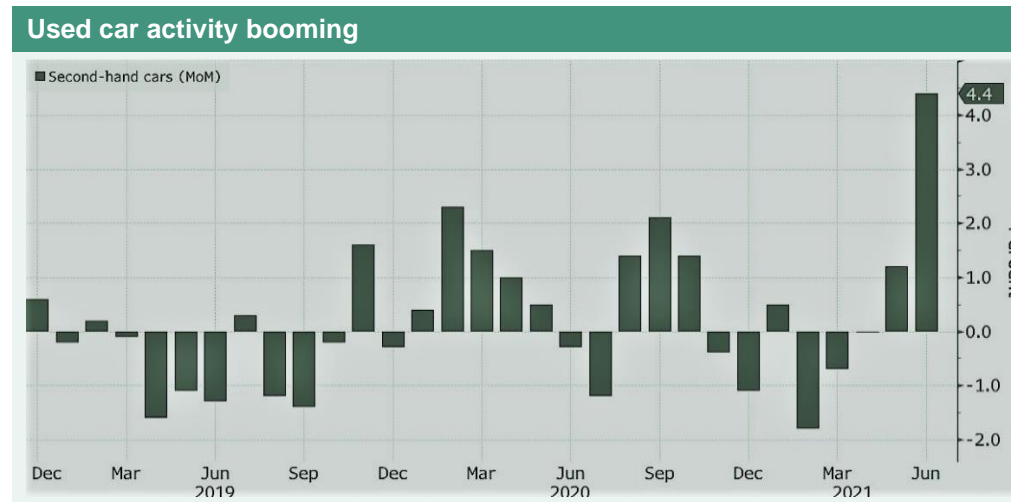
The required demolition and relocation of several franchised dealerships run by MMH, in preparation of phase three of the Marleigh joint venture has commenced, with a link road to be constructed over time.

The Local Authorities are due to publish a first draft of its Preferred Options Local plan for consultative purposes during H2 2021, setting out its preferred development strategy from 2030. MGP remains confident that Cambridge East will be central to those plans.

## Marshall Ventures

### MMH

Despite the lockdown which saw dealerships reopening during April, the SMMT estimated in August that the new car market is forecast to grow by 11.7% to 1.822m units in 2021. By comparison, the used car market is forecast to grow by 3.9% (source: Cox Automotive, mid-case estimate). The new car market will be affected by supply chain issues (semiconductor shortages), which could be in part offset by a strengthening of sterling versus the euro, potentially resulting in attractive consumer offers.



Source: ONS

Used vehicle price inflation rose to a 20-year high in June 2021, at 4.4% month-on-month (source: ONS) and equating to 15.3% y-o-y (source: Autovista), the highest level in Europe by some margin. The increases reflect a combination of the build-up of savings during the various lockdowns, a desire to avoid public transport and a significant drop in the supply of new vehicles compared to 2019. While a normalisation in automotive markets is likely, the automotive retailers continue to benefit from the price inflation.

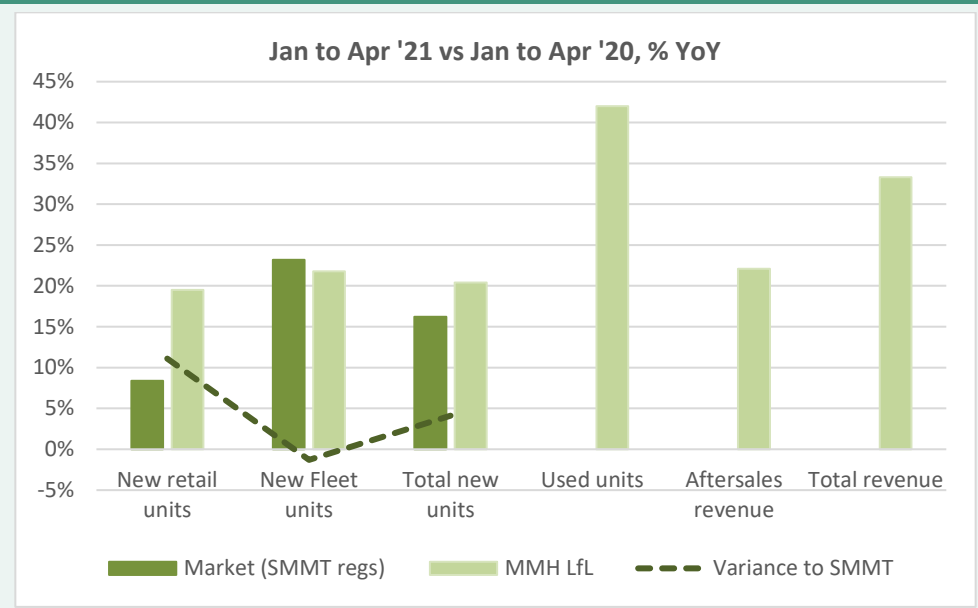
In late 2020 MMH secured the opportunity to represent Ford Commercial Vehicles in Kings Lynn and Seat in Oxford. Both new businesses commenced trading in early 2021, following a re-branding process.

The trading update on 20 May, suggested a continuation of the strong outperformance versus the market in the first four months of the year. In the January to April period, sales of new passenger vehicles increased 19.5% on a I-f-I basis, compared to an 8.4% rise in the wider market.

Sales of new fleet cars increased 21.8% y-o-y on a I-f-I basis, which was modestly below the rise in the market (-1.3%). Used rose 42.0% (I-f-I and y-o-y), while aftermarket revenues improved 22.1% y-o-y.

What is significant is that in 2021, the dealerships were closed for the first three-and-a-half months of the year, versus five weeks in 2020 due to lockdown. In the first three months of 2021, reflecting available data from the SMMT, the used passenger vehicle market declined 8.9% y-o-y.

**By contrast, the performance at MMH was a shortfall of just 1.7% on a I-f-I basis, again suggesting significant outperformance.**

**MMH YoY change in trading, by category, January to April 2021**


Source: Company, SMMT

Following the encouraging H1 performance and notwithstanding, the potential ongoing impact of COVID-19 and global semiconductor supply shortages, MMH is currently targeting adj. PBT of at least £40m. post-repayment of government subsidies received in the period. This usurps previous guidance and represents the third upgrade to expectations YTD, as well as a record outcome profits. The government monies received equate to the Coronavirus job retention scheme (CJRS) and non-essential retail sector grants. It is worth mentioning that MMH reports under the IFRS framework, with MCH using UK GAAP. To date, the MMH record adj. PBT of £25.4m was delivered in FY16 (under IFRS, which equates to c.£18.5m under UK GAAP, reflecting higher amortisation).

### Fleet Solutions

With all lockdown restrictions and social distancing expected to end in H2 2021, a relative return to normality is anticipated within the restaurant and food service sector, which ceteris paribus is likely to benefit revenues within Fleet Solutions. Further contracts have been sought to diversify the spread of revenues, with some progress made in the year to date. The rationalisation of the business in late 2019, coupled with a return to revenue growth is likely to result in the division building on its return to profitability during FY20.

### Martlet Capital

One of the investments within the MarQuity investment fund was sold for £2.1m in March 2021, representing a 2.4x return on investment. An increase in fair value of £0.9m was recognised in 2020 and as a result, no profit on disposal will arise in 2021.

## The greatest challenge or opportunity?

The Defence Command Paper issued on the 22 March 2021, announced the decision by the UK Government to retire the RAF's 14-strong C-130 fleet from service by 31 March 2023. Although, the completion date for the process was earlier than anticipated and results in some uncertainty for the business, it also creates opportunities.

MADG has a strong record in securing the MRO contracts for C-130's and not just ones sold by the RAF to overseas air forces. However, such negotiations take time.

MADG maintains C-130's for 16 nations, excluding the UK, the recent 10-year enabling contract with the US Marine Corps (USMC) may well significantly dwarf the contract with the RAF (representing 14 aircraft). In total, the USMC contract, which commenced with the trial of one aircraft, enables MADG to bid for a substantial portion of their 66-strong fleet (subject to their performance within the trial).

**MADG is the last remaining UK sovereign maintenance operator and modifier of large transport aircraft.** In a post-Brexit environment, we think that Marshall could benefit as a result.

The Board had previously announced its decision to relocate its Aerospace activities and operations in 2019. In Q4 2020, MCH announced that it had entered an option with Cranfield Airport for a long-term lease on the land. Following the decision by the MoD to retire the UK RAF's 14 remaining Hercules military transport aircraft, all the Group's remaining customers will be based outside of the UK by the end of March 2023.

As of result of the decision, several options might present themselves to MADG:

- With all the C-130 MRO customers based outside of the UK from FY23, does the UK base necessarily have to be so large (hangar space currently amounts to 1.5m ft<sup>2</sup>)?
- Could the operations be split, to ensure they are closer to customers?
- Potentially, should the current track record prove successful, the single largest customer within MADG will be the US Marine Corps
- Securing additional MRO business with existing nation state customers on other airframes
- A further expansion of the C-130 customers beyond the current 17 (16 from FY23)

As we highlighted earlier, the UK's significance as a customer of the Group's aerospace services has been declining in recent years, albeit it remains significant. The above options strongly suggest that while the transitional period may result in some turbulence, the longer-term future of the Aerospace business remains rosy, wherever it is situated, owing to the world-class engineering capabilities within the Group.

## A plethora of recent news

### Major contract signed

Marshall Aerospace and Defence Group (“MADG”) will provide maintenance to US Marine Corps’ 66-strong fleet of KC-130J tanker aircraft in Cambridge, which operate from numerous locations globally. The contract award follows the successful work on the three Kuwait Air Force KC-130s purchased from the US Government, plus the recent, prestigious, in-depth modification and re-painting work earlier this year on the US Navy’s ‘Fat Albert’ C-130J support aircraft.

To place the contract in context, MADG currently supports the C-130 platform for 17 government operators, including the RAF, responsible for a total of 150 airframes. Worldwide, the Hercules C-130 is operational with the air forces of 61 countries and in turn, 1,167 aeroplanes. The US currently operates 552 of those or 47.1% of the total worldwide, including the 66-tanker KC-130J aircraft with the US Marine Corps.

The award of the enabling contract represents a **powerful endorsement** of the world-class facilities, workforce, and project management capabilities of MADG.

There is competition within the contract, comprising a third-party operator, and the award of future work is dependent upon performance and availability. Hangar 16 at Cambridge has recently been refurbished and is now available for new contracts. Our understanding is that MADG has the capability to undertake work on four aircraft simultaneously in said hangar. The duration of the maintenance programme typically amounts to between three and four months, suggesting a maximum of 12 to 16 airframes per annum.

### Next step in developing the Cambridge site

In further news, MADG announced in October 2020 that it had entered into a non-exclusive option agreement with Cranfield Airport, for a 150-year lease on land at the University’s Air Park development. The modest annual option payment secures a potential new site for MADG ahead of its anticipated relocation in 2030. MADG is currently collaborating with Cranfield University on several R&D projects. The option provides a degree of security, while also ensures that the Group has time to see how its business develops post-RAF C-130s before finally deciding on the new home for the parts of the business that need to relocate.

Ultimately, the relocation from Cambridge would free up the existing airport site for development by Marshall Group Properties (MGP). The current and proposed developments at Marleigh and Land North of Cherry Hinton (LNCH) cover 230 acres out of a total 900 for the Airport site. The redeveloped site is expected to provide 12,000 homes and c. 5m sq ft of commercial space.

Construction on the forthcoming Primary Academy on the Marleigh site has broken ground, with the first pupils anticipated from September 2022. The school, which will focus on STEM subjects, is to have a capacity of 420 primary and 52 nursery aged children.

### MADG wins another Queen’s Award for Enterprise for International Trade

MADG’s military aerospace division was awarded a prestigious Queen’s Award for Enterprise for International Trade in 2021, which was in recognition of the significant growth of its C-130 customer base.

The division now supports 17 global military operators, including the more recently signed contracts with the US Marine Corps, Cameroon, and Bangladesh. In addition, Norway and Denmark extended their existing maintenance contracts on the C-130 Hercules for a further seven years at the end of 2020. Over the last three years, MADG has delivered export sales of more than £162m on the C-130 airframe.

The award represents the third such Queens Award within the last eight years, securing one within the Innovation category in 2013 for deployable CT scanners with several international armed forces and, for Enterprise in 2016.

### **Modernisation of NATO's secure communications systems**

NATO has awarded MADG a contract to modernise NATO's Deployable Air Command and Control Component's (DACCC) communications systems, on behalf of its Communications and Information Agency (NCI). The upgrades follow on from ongoing experiences with the Danish and Royal Netherlands armed forces, and in this instance, involves an upgrading of the method by which NATO's transportable shelters transmit, relay, and receive critical mission data.

Voice-over internet protocol (VoIP) will form the basis of the upgrade, thereby future proofing the system. The communications systems will be secure against cyber and physical attacks and will be utilised in the planning, tasking and execution of all air command and control operations.

### **MADG design and engineering of the negative pressure ventilator**

Along with other businesses, Marshall became involved at the design stage of the new Exovent negative pressure ventilator assistance devices. The Exovent consortium of academics, medics, and MADG identified the potential for the application of the technology to provide additional treatment options for patients with respiratory conditions in a critical care environment. The benefit of the negative pressure ventilator is the greater patient comfort provided, as there is no need to put an artificial airway in place and the patient remains conscious, breathing via a mask.

Marshall has shared its knowledge and working prototypes with UK manufacturer Portsmouth Aviation, who will accelerate the production of the device. The expectation is that the device will be submitted for approval by August and there is a hope that confirmation of such will be in place by the year end. The next step is to commence volume manufacturing from 2022.

The development cost to MADG during 2020 of the Exovent negative pressure ventilator amounted to £0.8m. The Group will not benefit from the sale of the ventilator once produced, except for a possible R&D tax credit which should be received during 2021.

### **Sale of Aeropeople**

The strategy to focus on the core strategic growth areas within the MADG organisation, has resulted in the disposal of the loss-making Aeropeople recruitment, line maintenance and CAMO business with the consideration matching the net assets of the business, £0.6m. The business provides manpower within the aerospace, aviation, engineering, motorsport, automotive and defence industries. The Line Maintenance operation is based within Stansted Airport, while CAMO is in Cambridge.

The purchaser of the business was Bishill Holdings, which is run by a previous manager of the Aeropeople business.

### **The proposed opening of a new production facility in Canada**

The announcement in June 2021, highlighted plans to extend the Group's footprint in Canada via the opening of a dedicated Land Systems production facility in New Brunswick province (with the Canadian army's largest base nearby). The expectation is that the new facility will enable MADG to further grow its Land and Air businesses in North America and, in turn, bid and partner the Canadian government's future programmes.

The immediate target is LVM, the replacement of the Canadian Army's fleet of light and heavy logistic vehicles, trailers, and containers. The new site will more than double the number of employees in the country, from the current 75, when it opens prior to the end of FY22. The target is the larger programmes under the Defence Investment Plan, which require high levels of Canadian content.



### MMH continues its consolidation of the automotive retail sector

MMH acquired the Cheltenham and Gloucester Jaguar Land Rover dealership from Heritage Motors in early June 2021. This takes the number of Jaguar dealerships within the MMH portfolio to seven and Land Rover outlets to nine, making the Group one of two most significant partners to the brands. There are plans to relocate the business to a new freehold location, which will be redeveloped and result in the requirement for additional headcount. No consideration was mentioned within the press release.

In early July 2021, MMH acquired the Nissan dealership in Leicester, purchasing the business from Renault Retail Group and adding to its existing franchises for the Japanese OEM in Grantham and Lincoln. MMH has also purchased the three-acre site, including a multi-brand showroom, which previously housed the Renault, Nissan and Dacia franchises. The consideration for the dealership was not provided in the press release. The two acquisitions completed YTD highlights MMH's strategy to grow scale with existing brand partners in new regional territories.

### Management changes

FY20 and the new financial year have witnessed several Board changes.

**Kathy Jenkins** was appointed as the new Group CEO in April 2021, following four years' service within the business, the latter two years as COO. Kathy and her team ensured that the operations successfully navigated the challenges of COVID-19, in turn, delivering a strong financial performance under difficult circumstances. Previously, Kathy gained both operational and management experience with GEC-Marconi and Thales.

In August 2020, MCH's Vice Chairman and its ex-CEO, **Robert Marshall**, stood down from the Board and his roles within the business following 27 years with the Group. Robert remains a shareholder in the family business and will focus his time on building Martlet Capital as an independent, early-stage investment vehicle.

**Charlie Marshall** was appointed as a new Non-Executive Director. Charlie is the fourth-generation descendent of the Group's founder, David Marshall, and is a successful business owner in his own right.

From 01 October, **Justin Read** will join the Board of MCH as a Non-Executive Director. Justin will succeed Philip Yea as the Chairman of the Audit and Risk Committee, who in 2020 became the Chairman of Mondi, the FTSE 100 paper and packaging business. Justin commenced his career in corporate finance, post graduating from Oxford University, before moving into investor relations. Justin moved into the construction/services/property sectors in a variety of corporate development and finance director roles before commencing a plural NED career in 2017. Justin's expertise within the construction and property sectors is likely to prove invaluable to MGP.



## Financials

Summary Income Statement				
Year to Dec, £m	2017A	2018A	2019A	2020A
Aerospace & Defence (MADG)	295.4	247.8	307.6	286.6
Property Rental	8.0	8.0	7.8	8.1
Marshall Motor (MMH)	2232.0	2186.9	2276.1	2154.4
Fleet Solutions	42.8	47.4	53.0	45.7
Intercompany	-24.2	-6.1	-6.5	-6.7
Revenue	2554.0	2483.9	2638.0	2488.1
Y-o-Y growth (%)		-2.7%	6.2%	-5.7%
CoGS	-2202.2	-2112.2	-2253.8	-2167.0
Gross profit	351.7	371.8	384.1	321.2
Gross margin (%)	13.8%	15.0%	14.6%	12.9%
EBITDA	61.7	57.7	59.6	65.7
% margin	2.4	2.3	2.3	2.6
Aerospace & Defence (MADG)	13.8	15.4	18.2	17.5
Property Rental	3.4	2.1	2.9	4.3
Marshall Motor (MMH)	34.1	32.0	29.9	30.2
Fleet Solutions	-1.4	-1.4	-1.2	0.2
Land sales & property development	0.0	0.0	0.0	0.0
Martlet	0.0	0.0	0.0	0.0
Central shared services	-7.0	-6.2	-8.2	-5.8
Adj. EBIT (pre-amortisation)	43.0	41.7	41.8	46.3
Aerospace & Defence (MADG)	1.2%	6.2%	5.9%	6.1%
Property Rental	42.7%	26.3%	37.7%	53.3%
Marshall Motor (MMH)	1.7%	1.5%	1.3%	1.4%
Fleet Solutions	-3.3%	-3.0%	-2.2%	0.4%
Total % EBIT margin	1.4%	1.7%	1.6%	1.9%
Net Interest	-8.9	-5.7	-6.6	-7.2
PBT (Adjusted)	34.7	36.0	35.2	39.1
Adj. Tax	-6.7	-11.1	-6.7	-8.5
Adj. PAT	28.0	25.0	28.5	30.6
Minority interests	-15.0	-1.9	-3.9	-3.5
Pref. dividends	-0.7	-0.7	-0.7	-0.7
Earnings	5.8	22.2	23.9	26.3
EPS (Adjusted) (p)	31.1	35.9	35.3	41.3
Dps (p) - Voting, ordinary	4.0	4.0	1.0	7.0
DPS (p) - NVPO	6.0	6.0	3.0	9.0
Ave no of shares (FD) (m)	59.1	59.1	59.1	59.1

Source: Company historic, Equity Development estimates

That revenues declined by only 5.7% in a year beset by uncertainty and two lockdown periods is nothing short of a formidable performance. This highlights not only the resilience of the Group, and essential nature of its services, but also an ability to adapt. The sale of the first homes on the Marleigh site was significant, highlighting the transition of the Cambridge airport site and a growing emerging profits stream.

EBITDA and EBIT margins improved by c. 30 bps to 2.6% and 1.9%, respectively, reflecting a combination of efficiency gains and government assistance and notwithstanding the modest deterioration in the top-line.

With adj. EPS rising 18% to 41.3p, three dividends were paid/announced during the year, compared to one in 2019. However, the actual cash shareholders received in July and December was maintained at pre-pandemic levels. The latter of those dividends was paid in July 2021. The increase in actual dividends announced highlights management's confidence in the outlook.

The level of exceptional charges increased to a net £8.6m. The exceptional items include the write down in the carrying value of franchise agreements within MMH (-£6.5m); restructuring across the Group including Fleet Solutions and Aeropeople, (-£7.7m); COVID-19 related expenses (-£1.6m); Exovent ventilator development costs (-£0.8m) and a profit on the disposal of property (+£8.0m). The most significant property transaction related to the sale and leaseback of an office building within the Cambridge Airport, realising £10m of proceeds and a profit on disposal of £7.4m.

The net reversal of deferred tax assets and liabilities is expected to reduce the FY21 tax charge by £1.5m, reflecting fixed asset timing differences and the utilisation of brought forward tax losses.

### Summary Cash Flow

Year to Dec, £m	2017A	2018A	2019A	2020A
EBITDA	76.4	75.5	67.3	72.5
Working capital movement	9.8	34.4	24.5	29.5
Other	25.2	-58.4	-19.7	-16.1
Operating cash flow	111.4	51.5	72.1	85.9
Net Interest	-8.4	-6.4	-7.1	-7.4
Pref. dividends	-0.7	-0.7	-0.7	-0.7
Minority payment	-1.6	-1.8	-2.6	-1.9
Taxation	-2.6	-6.7	-3.4	-7.3
Cash earnings	98.0	35.8	58.3	68.6
Net capex	-31.3	-39.9	-45.6	-24.2
Post capex cash flow	66.7	-4.1	12.7	44.4
Dividends	-3.3	-3.3	-3.3	-3.3
Free cash flow	63.4	-7.4	9.4	41.1
Net (Acqns)/Disposals	44.3	-0.1	-28.2	-3.0
Share Issues	0.0	-1.0	-0.7	0.0
Other financial	20.3	0.1	-3.0	-0.3
Increase Cash/(Debt)	128.1	-8.3	-22.5	37.9
Opening Net Cash/(Debt)	-122.2	5.9	-2.4	-24.9
Closing Net Cash/(Debt)	5.9	-2.4	-24.9	12.9

Source: Company histories, Equity Development estimates

Cash flow was strong during FY20, with a £36m turnaround from a net debt position at the end of FY19 to net cash of £12.9m by the FY20 year end. Working capital was positive and strong as in recent years, with EBITDA approaching FY18 highs, resulting in operating cash flow equating to 118% of EBITDA.

Within capex is £12.8m of expenditure on a new Group-wide ERP system. A further £3.1m will be expensed across the subsidiary businesses on related software in 2021.

The M&A relates to MMH. In December 2019, eight Volkswagen franchises were purchased, with completion of the purchase of the trade and assets of the 9<sup>th</sup> in July 2020 from the same vendor.

By number of locations, MMH is now the Volkswagen Group's largest partner. The level of M&A by MMH was lower than in recent years, in part reflecting the pandemic. However, we believe that MMH remains a major consolidator within the sector and would not be surprised to see further activity during FY21.

The £0.7m received by MADG to cover furlough staff payments (Coronavirus Job Retention Scheme, CJRS) during the initial lockdown in 2020 was repaid in March 2021. MADG also utilised the VAT deferral scheme, with £4.3m of liabilities to be repaid in instalments between March 2021 and January 2022. All deferred PAYE liabilities were repaid in June 2020.

Similarly, MMH repaid all deferred VAT owed in September 2020. In the recent trading update MMH highlighted that the profits guidance is after repaying c.£4m of 2021 CJRS and non-essential retail grants.

As of 31 December 2020, £364.9m (FY19: £443.7m) of finished goods were held under vehicle funding arrangements within MMH.

Working capital also includes 50% of the fair value of land transferred to the joint ventures within MGP and amounting to £29m (FY19: 27.6m). The loan of £16.5m (FY19: £16.1m), to the joint ventures represents a loan from Homes England. £3.1m of this is within short-term creditors

The Group, excluding MMH, has a revolving credit facility (RCF) amounting to £75m, with £24.7m utilised at the end of 2020. The facility has an accordion option, allowing the RCF to be extended by a further £15m, subject to financial covenants and bank approval. Owing to the performance of the Group exceeding uncertain expectations at the start of the pandemic, the Group has exceeded all covenant tests to date, with original covenants applying from June 2021.

The MMH RCF amounts to £120m. The facility was extended in July 2020 until 2023, with a mutual option to reduce the RCF by £20m in July 2021.

### Abbreviated Balance Sheet

Year to Dec, £m	2017A	2018A	2019A	2020A
Intangible Assets	106.4	86.4	87.0	94.1
Tangible Assets	218.9	237.9	271.7	271.1
Investments/other	4.8	6.6	7.9	12.1
Net Working Capital	-15.7	-17.4	-17.9	-44.7
Capital Employed	314.4	313.5	348.6	332.6
Other	-6.1	-13.6	-28.1	-29.6
Net Cash/(Debt)	5.9	-2.4	-24.9	12.9
Provisions	-71.3	-36.5	-25.1	-31.2
Pension liability	-12.3	-9.9	-3.0	-4.6
Shareholders' funds	167.7	188.0	202.7	211.5
Non-controlling interest	-63.0	-63.1	-64.2	-68.6
Net Assets	230.7	251.1	267.6	280.1

Source: Company histories, Equity Development estimates



## Contacts

### Andy Edmond

Direct: 020 7065 2691

Tel: 020 7065 2690

[andy@equitydevelopment.co.uk](mailto:andy@equitydevelopment.co.uk)

### Hannah Crowe

Direct: 0207 065 2692

Tel: 0207 065 2690

[hannah@equitydevelopment.co.uk](mailto:hannah@equitydevelopment.co.uk)

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Equity Development, 15 Eldon Street, London, EC2M 7LD

Contact: [info@equitydevelopment.co.uk](mailto:info@equitydevelopment.co.uk) | 020 7065 2690