

Trackwise Designs

H121 results

Progress in both divisions during H121

As flagged in its July trading update, Trackwise Designs' H121 group revenues increased by 71% y-o-y to £4.1m, reflecting the acquisition of Stevenage Circuits in March 2020 and a doubling of IHT revenues, while adjusted EBITDA quadrupled to £0.5m. Management notes the group remains on track to meet market FY21 expectations despite supply chain disruption, so we leave our FY21 and FY22 estimates broadly unchanged.

Year end	Revenue (£m)	EBITDA (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)
12/19	2.9	0.5	0.1	0.8	0.0	287.5
12/20	6.1	0.8	(0.4)	1.4	0.0	164.3
12/21e	9.0	0.9	(0.7)	(1.0)	0.0	N/A
12/22e	22.1	4.3	1.9	6.3	0.0	36.4

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

H121 results show progress in both divisions

H121 group revenues show progress in the improved harness technology (IHT) division, where revenues of £0.6m were 95% of the total reported for the whole of FY20, and in the advanced printed circuit board (APCB) division, where revenues were 6% higher than H220 despite supply chain shortages and the adverse impact of Brexit on trading with customers in mainland Europe. APCB profitability was adversely affected by supply chain shortages and coronavirus related disruption, which resulted in operational inefficiencies. Net cash (excluding IFRS 16 leases) reduced by £8.8m during H121 to £2.6m as management invested £8.7m in plant and property, primarily at the new Stonehouse site. The cash outflow and the remainder of the cost of fitting out the site is covered by the £12.6m raised in December 2020 through a placing and open offer. Management now expects the new site will start production in Q122. The site will be used for high-volume/low-mix IHT work, initially production for the electric vehicle (EV) OEM.

On track to meet FY21 market expectations

Management notes that while trading continues to be affected by supply chain constraints, it is coping with these pressures such that the group remains on track to meet FY21 market expectations. We therefore leave our FY21 and FY22 estimates unchanged except for a slight adjustment to our FY22 EPS estimate (from 6.4p to 6.3p) to reflect the exercise of options.

Valuation: Addressing several high-potential sectors

While our peer multiples-based analysis shows Trackwise trading at a premium to its peers on all metrics, this approach fails to recognise the potential of the IHT business so we have augmented it with a scenario analysis, which is presented in our [initiation note](#). This explores how each of the three key segments in which Trackwise has developed prototype IHT products for customers (EVs, medical devices and aerospace) has the potential to generate revenues of at least £100m at even relatively modest levels of market penetration.

Tech hardware & equipment

29 September 2021

Price 230p

Market cap £66m

Net cash (£m) 30 June 2021 excluding IFRS 16 lease liabilities 2.6

Shares in issue 28.7m

Free float 66.6%

Code TWD

Primary exchange AIM

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs (3.2) (12.2) 32.8

Rel (local) (1.1) 12.2 9

52-week high/low 370p 165.8p

Business description

Trackwise Designs is a UK manufacturer of specialist products using printed circuit technology. These include a lightweight replacement for conventional wiring harnesses known as IHT and RF antennae. In H121 25% of revenues related to exports.

Next event

FY21 results March 2022

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H121 performance

Half-on-half revenue growth in both divisions

As flagged in the company's July trading update, H121 group revenues increased by 71% year-on-year to £4.1m, reflecting the acquisition of Stevenage Circuits (SCL) in March 2020 and a 131% jump in IHT revenues to £0.6m. The results show progress in both IHT and APCB activities. IHT revenues were 95% of the total reported for the whole of FY20 and were backed by deliveries to the UK EV OEM and an industrial customer. H121 revenues in the APCB division were 6% higher than H220 (this is a better comparator than H121 because SCL was acquired part way through H120), despite supply chain shortages and the adverse impact of Brexit on trading with customers in mainland Europe.

Profitability affected by supply chain shortages and coronavirus related disruption

Gross margin declined by 6.1pp compared with H220 to 29.0%. While Trackwise was able to pass price increases caused by supply chain shortages, particularly for copper, onto its customers, temporary shortages of materials and disruptions to working patterns caused by the coronavirus resulted in operational inefficiencies. Adjusted EBITDA reduced by £0.2m compared with H220 to £0.5m, in line with the July trading update. We estimate that around £0.1m of this reduction related to lower gross profit, the remainder to higher indirect costs as the group prepared for expansion onto the third site (see below) in FY22, for example appointing a Chief Operating Officer. The group generated an adjusted operating loss of £0.1m, in line with the July trading update, compared to an adjusted operating profit of £0.2m in H220.

Cash outflow related to new Stonehouse site

Net cash (excluding IFRS 16 leases) reduced by £8.8m during the period to £2.6m at end June 2021. Working capital requirements increased by £1.2m, around half of which was attributable to a rise in debtors. Capital expenditure was £8.7m which includes £2.7m of deposits for equipment which is allocated in Other Receivables. An estimated £1.2m of the expenditure related to SCL to further improve capacity and efficiency, the bulk of the remainder to the acquisition and fitting out of the new Stonehouse site. This value is higher than our full year estimate because management intends to refinance some of the equipment on leases. In August management completed a £2.0m mortgage facility and agreed a £1.3m asset financing facility, which is currently undrawn. We model a £5.4m increase in borrowings during FY21 to cover this.

Stonehouse site provides capacity for high-volume/low-mix IHT

In May 2021, Trackwise acquired a 6,947m² freehold property in Stonehouse, Gloucestershire, for £2.8m. Management expects that the site purchase and expenditure on associated equipment will collectively total around £9m, which is being funded from the £12.6m raised in December 2020 through a placing and open offer. The company is in the process of installing an automated roll-to-roll IHT production line at the site. While the site was originally intended to be fully operational by the end of December 2021, the schedule has been delayed by a few weeks, moving the start of production to Q122. Once operational, the Stonehouse site will be used for high-volume/low-mix IHT work, initially production for the EV OEM, and the 1,812m² Tewkesbury site for low-volume development projects. The Stonehouse site has capacity for the installation of a second line in the future.

Outlook

On track to meet market expectations for FY21

Management notes that while current trading continues to be affected by supply chain constraints, it is coping with these pressures such that the group remains on track to meet market expectations for FY21. The issue with availability of copper-clad substrates experienced in the first half has eased and the company has been successful in passing on price increases to its customers, so we expect gross margin to improve during the second half. In fact, the APCB division's order book is strong (£2.2m+ with a pipeline of new order opportunities of over £3m), encouraging management to add a second shift during H221 to meet production demand. We therefore leave our FY21 estimates broadly unchanged since we treat the additional deferred tax provisions as exceptional items. We also leave our FY22 estimates broadly unchanged except for a slight adjustment to the average number of shares in issue following the exercise of options in July and September, which reduces our FY22 EPS estimate from 6.38p to 6.31p. However, we move some depreciation from indirect to direct costs, in line with the company's treatment. This has no effect on either our FY21 or FY22 PBT estimates but reduces gross margins from 34.6% to 32.4% in FY21 and from 35.5% to 33.0% in FY22.

EV OEM ramp-up underpins FY22 estimates

In June 2021 Trackwise announced that the volume ramp-up for the programme with its UK EV OEM customer was delayed by a quarter to early FY22 and that the customer had extended the term of the manufacture and supply agreement from three to four years, raising the aggregate value for the contract by £16m to up to £54m. This potentially represents IHT revenues of £16–17m in FY23 and FY24. The level in FY22 will depend on the rate of ramp-up during Q122 and, according to management, could be as high as £16m. Our estimates already take a cautious approach, modelling £13m EV revenues in FY22. The EV opportunity continues to expand as Trackwise supplies early-stage samples to other companies in the EV sector including responding to a request from a large European OEM for cell-to-pack interconnect flex up to 2.4m in length, which is ideal for roll-to-roll manufacture.

Volume IHT production for medical sector presents upside to FY22 estimates

Trackwise is working with seven medical catheter manufacturers. The samples for medical devices that Trackwise shipped in FY20 to its lead catheter company, which is a large US medical OEM, are working as designed in trials. Management expects to receive further development orders from this customer in FY21 ahead of potential production revenues in FY22. (We treat the production revenues as upside to our FY22 estimates.) As discussed in our May [flash note](#), Trackwise has signed a seven-year agreement with CathPrint, which has created a novel technique for manufacturing advanced catheters. Assuming the ongoing development project supplying IHT to CathPrint is successful, this potentially represents sales of significant volumes of IHT for medical applications for a five-year period from FY23 onwards.

Aerospace still expected to be largest sector in the longer term

Trackwise is working with over 30 aerospace OEMs and suppliers including GKN on a system for preventing ice forming on aircraft wings, four developers of electric vertical take-off and landing vehicles (eVTOLs), two developers of business jets and two developers of high-altitude pseudo-satellites (HAPS). The company is working on multiple independent projects with a European aerospace OEM including a flying wing demonstrator. Management estimates that one or more of the projects in this sector could progress to production revenues within two to three years.

Valuation

Peer multiples

Trackwise's share price has risen by over 50% since the 170p low reached in July 2021 following the announcement of the delay to the EV OEM ramp-up in June, its lowest point since the announcement of the series production order for the EV manufacturer in September 2020. At current levels, our peer multiples-based analysis shows Trackwise's shares trading at a premium to the sample means on all metrics, implying investor confidence in the IHT opportunity. Based on our estimates, which benefit from a strong ramp-up of IHT revenues in FY22 and a full year of revenues from SCL in FY21, Trackwise is expected to grow revenues much more strongly than any of the sample between FY20 and FY22. This is not surprising given that the companies in the sample are well-established businesses similar to Trackwise's APGB activity, while the IHT business has the potential to deliver growth that is faster than the average for our sample. That is not just for the period covered by our estimates, but for at least several years beyond that, so the peer multiples-based approach fails to recognise the potential of the IHT activity in the longer term. Although we do not present detailed FY23 estimates, we provisionally estimate that expansion could support FY23 revenues of at least £33m. We therefore supplement the peer multiples approach with a scenario analysis.

Exhibit 1: Peer multiples

Name	Market Cap m (\$)	EV/Sales 1FY (x)	EV/Sales 2FY (x)	EV/EBITDA 1FY (x)	EV/EBITDA 2FY (x)	PE 1FY (x)	PE 2FY (x)	CAGR	EBITDA margin 1FY	EBITDA margin 2FY
AT & S	1,511	1.4	1.1	6.9	5.0	31.7	16.0	18.8%	20.4%	23.2%
CMK	256	0.5	0.5	6.8	4.9	20.1	9.2	10.1%	7.6%	9.9%
Compeq Manufacturing	1,642	0.8	0.7	4.4	3.8	9.5	8.0	6.0%	17.9%	18.9%
Ibiden	8,460	2.5	2.3	8.4	7.0	24.9	20.1	14.8%	29.9%	32.8%
KCE Electronics	2,923	6.6	5.7	26.5	21.8	40.8	31.7	22.2%	24.9%	26.1%
Meiko Electronics	772	1.0	0.9	7.9	7.3	10.3	9.1	12.7%	13.0%	13.0%
Tripod Technology	2,217	0.9	0.8	4.7	4.2	9.8	8.9	8.4%	18.3%	19.3%
TTM Technologies	1,351	0.8	0.7	6.0	5.6	9.7	8.3	4.7%	13.0%	13.3%
Unimicron Technology	7,487	2.4	2.0	12.0	8.6	22.4	16.7	16.2%	19.6%	23.1%
Zhen Ding Technology	3,466	0.8	0.7	4.5	3.8	10.5	8.8	12.6%	17.5%	18.7%
Mean		1.8	1.6	8.8	7.2	19.0	13.7		18.2%	19.8%
Trackwise Designs	91	6.1	2.5	64.4	12.8	N/A	36.4	90.9%	9.4%	19.3%

Source: Refinitiv, Edison Investment Research. Note: Prices at 27 September 2021. *CAGR is compound average growth in revenue between year 0 and year 2.

Scenario analysis

In our [initiation note](#), we presented a scenario analysis that looked at the potential revenues achievable if the company was successful in penetrating specific target markets. This approach showed that the three key segments in which Trackwise has developed prototype IHT products for customers (EV, medical devices and aerospace) each has the potential to generate revenues of at least £100m at relatively modest levels of market penetration. The contract with the EV manufacturer announced last September is the first demonstration of uptake of the technology at scale. This means that the share price is very sensitive to any news regarding the relationship with this customer, for example falling from 226p to 190p on 22 June when the delay to the EV OEM ramp-up was announced.

Exhibit 2: Financial summary

	£'m	2019	2020	2021e	2022e
31-December		IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT					
Revenue		2.9	6.1	9.0	22.1
Cost of Sales		(1.8)	(4.4)	(6.1)	(14.8)
Gross Profit		1.1	1.7	2.9	7.3
EBITDA		0.5	0.8	0.9	4.3
Normalised operating profit		0.2	(0.2)	(0.5)	2.4
Amortisation of acquired intangibles		0.0	0.0	0.0	0.0
Exceptionals		(0.0)	(0.1)	0.0	0.0
Share-based payments		(0.2)	(0.2)	(0.3)	(0.3)
Reported operating profit		(0.1)	(0.5)	(0.8)	2.1
Net Interest		(0.1)	(0.2)	(0.2)	(0.5)
Exceptionals		0.0	1.1	0.0	0.0
Profit Before Tax (norm)		0.1	(0.4)	(0.7)	1.9
Profit Before Tax (reported)		(0.1)	0.4	(1.0)	1.6
Reported tax		0.1	0.8	0.3	0.3
Profit After Tax (norm)		0.1	0.3	(0.3)	1.8
Profit After Tax (reported)		(0.0)	1.2	(0.7)	1.9
Basic average number of shares outstanding (m)		14.7	20.7	28.6	28.7
EPS - normalised (p)		0.8	1.4	(1.0)	6.3
EPS - diluted normalised (p)		0.8	1.4	(0.9)	6.1
EPS - basic reported (p)		(0.3)	6.0	(2.5)	6.5
Dividend (p)		0.0	0.0	0.0	0.0
Revenue growth (%)		(16.2)	108.8	48.5	145.4
Gross Margin (%)		37.9	28.3	32.4	33.0
EBITDA Margin (%)		17.8	12.7	9.4	19.3
Normalised Operating Margin		6.9	N/A	N/A	10.8
BALANCE SHEET					
Fixed Assets		6.8	14.7	24.5	24.2
Intangible Assets		4.3	6.5	7.2	7.8
Tangible Assets		2.5	8.2	17.3	16.4
Investments & other		0.0	0.0	0.0	0.0
Current Assets		3.1	18.5	12.9	17.2
Stocks		0.6	2.0	2.2	3.6
Debtors		1.7	1.8	2.1	4.5
Cash & cash equivalents		0.6	13.9	7.8	8.2
Other		0.3	0.8	0.8	0.8
Current Liabilities		(1.4)	(3.0)	(2.3)	(4.1)
Creditors		(1.0)	(2.0)	(1.2)	(3.0)
Tax and social security		0.0	0.0	0.0	0.0
Short term borrowings (including lease liabilities)		(0.3)	(1.1)	(1.1)	(1.1)
Other		0.0	0.0	0.0	0.0
Long Term Liabilities		(2.5)	(5.3)	(10.7)	(10.7)
Long term borrowings (including lease liabilities)		(1.3)	(4.1)	(9.5)	(9.5)
Other long term liabilities		(1.3)	(1.2)	(1.2)	(1.2)
Net Assets		6.0	24.9	24.5	26.6
Minority interests		0.0	0.0	0.0	0.0
Shareholders' equity		6.0	24.9	24.5	26.6
CASH FLOW					
Op Cash Flow before WC and tax		0.5	0.8	0.9	4.3
Working capital		0.1	(0.6)	(1.3)	(2.0)
Exceptional & other		0.0	(0.6)	0.0	0.0
Tax		0.0	0.7	0.3	0.3
Net operating cash flow		0.6	0.3	(0.1)	2.6
Capex		(2.7)	(3.2)	(5.8)	(1.6)
Acquisitions/disposals		0.0	(1.6)	0.0	0.0
Net interest		(0.1)	(0.2)	(0.2)	(0.5)
Equity financing		0.0	17.3	0.0	0.0
Dividends		0.0	0.0	0.0	0.0
Other		0.2	0.1	0.0	0.0
Net Cash Flow		(2.0)	12.7	(6.1)	0.5
Opening net debt/(cash)		(2.3)	1.0	(8.8)	2.8
FX		0.0	0.0	0.0	0.0
Other non-cash movements		(1.3)	(2.9)	(5.4)	0.0
Closing net debt/(cash) including lease liabilities		1.0	(8.8)	2.8	2.3
Lease liabilities		0.7	2.6	8.0	8.0
Closing net debt/(cash) excluding lease liabilities		0.3	(11.3)	(5.2)	(5.7)

Source: Company accounts, Edison Investment Research

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