In its twenty-fourth year
ISSN 1476 895X
May 2023

"Relative strength is the only growth variable that consistently beats the market"

The Momentum Investor

STOCKMARKET NEWSLETTER

Authoritative Independent Monthly Share Selections using Technical & Fundamental Analysis

This Issue

- - -

FTSE-100: 7843
FTSE-All Share: 4260
Small-Cap: 6180

Next issue on Saturday 20 May

Volution

Sector: Construction | Share Price: 414p | Epic Code: FAN

Key Data

Address:	Fleming Way, West Sussex, Crawley, RH10 9YX
Telephone:	01293 441 662
Shares in issue:	198m
Market Capitalisation:	£819.7m
Next Results:	Finals: October

Global warming has increased the odds of more frequent, extreme and longer heatwaves. Last year we saw extreme heatwave events across the world: the 100 degree heatwaves in California and the UK; wildfires in Europe; and the most powerful snowstorm, hurricane and typhoon in living memory in New York, Florida and Japan, respectively.

Jeremy Clarkson, host of Clarkson's Farm, might sarcastically say that the only way the UK can become carbon neutral is if we all turn to Zoom to see our friends and also, "if animals such as cows and giraffes and any other animal that burps methane becomes illegal."

Against that genuinely alarming backdrop, the Paris international treaty in 2015 (renewed by COP-27) has moved from a time for words to a time for action with a cap on temperature rises to just 1.5 degrees above pre-industrial levels by cracking down on carbon emissions. To get there, greenhouse gas emissions must peak by 2025 and decline 43% by 2030. This has led to a blizzard of ever tighter building regulations not just for new builds but also existing ones, creating a potential boom in heating and ventilation products and this is one reason why I have alighted on Volution, a highly profitable market leader in domestic ventilation, which makes almost 70% of its sales from carbon reducing products.

As the chart on page 2 shows, the shares have performed well, but that only gives partial credit to the terrific record of CEO Ronnie George, who I met again with over the month. Between FY'09 and its listing in 2014, Volution's sales had risen from £72m to £121m and EBIT profit from £15m to £26.5m while as a quoted entity they've taken off again to £308m and £64.9m, respectively, in FY'22 (year-end June), implying eight-year growth of 155% and 145%. In light of the recent interim results ended December, which were ahead of forecast, brokers have upgraded and now expect sales of £324m, £337m and £355m between FY'23-'25 for EBIT of £67.6m, £69.7m and £72.8m.

History

Volution can trace its origins back to 1936 when Vent-Axia, a long-established high-end ventilation firm, invented the world's first window ventilation unit, which was electrically operated and made of Bakelite. In 2002, the business was subject to a management buy-out from industrial conglomerate Smiths Group and after being fattened by the acquisitions of Baxi Air Management (centralised ventilation, heat recovery systems) and Manrose (budget residential and commercial ventilation), it was flipped from Montagu Private Equity to ABN Amro and then Towerbrook in 2012, with the latter appointing Ronnie George as CEO.

Acquisitions: 18% ROIC hurdle

I originally met George shortly after it listed at 150p in 2014. At that time Volution was dominated by its market leading UK operation, complemented by a small European business in Sweden and Germany, but he made clear to me his ambition to become the number one in Continental Europe and like Ronseal he has pretty much delivered what was written on the tin with an impressive 19 acquisitions completed since listing. George says Volution has a well-drilled approach to acquisitions including a minimum hurdle of 18% return on invested capital within three years, by adding new products from the wider group; improving supply chain / better buying; innovation to reduce the acquired firm's costs; better pricing discipline; coaching for owner managers on how to work in a larger company - typically acquired ones make just 2-4% turnover of Volution and persuading them to stay long-term.

19 acquisitions

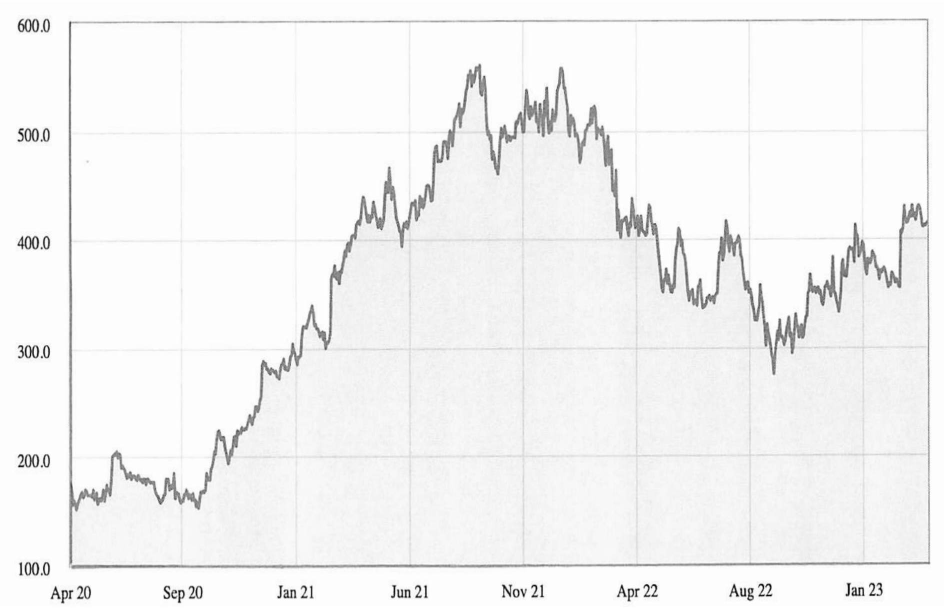
Within its first two years after listing it had snapped up smaller European rivals Fresh and Pax in Sweden (a combined £20.5m) followed by inVENTer, a leader in heat recovery systems in Germany (£20.1m), Ventilair in the Benelux (£11.6m) and Energy Technique (£9m, adding fan coils). Average price paid for these was a keen 7.4x EBITDA.

George says while Volution could have expanded organically, the credibility of owning a local brand is key to cracking these markets, while in recent years he has been prepared to pay more for companies with commanding market shares. These larger deals include Simx in 2018, a 40-year old market leader of residential ventilation systems in New Zealand for £37.8m, which sells both Manrose but also its own higher value brands such as Smart Vent (whole house ventilation) and Heat Trans (heat transfer systems).

Piggyback £630 billion climate renovation funding

In a move to piggyback on generous EU funding for renovation, with the EU's Green Deal for 2021-2027 allocating a massive £1,900 billion including one-third for climate projects, Volution later acquired 75% of ClimaRad (£38m), market leader in the Netherlands for "de-centralised" (single room) heat recovery ventilation systems. Adding manufacturing expertise, it then bought Energy Recovery Industries (ERI) in 2021, which makes low-carbon heat exchanger cells in North Macedonia and supplies the Italian, Spanish and UK markets for £20.8m. These deals added expertise in heat and energy recovery ventilation systems (32% group sales) providing entry to a new and large market projected to grow from US$3,019m in 2020 to reach US$4,467m by 2028 (+5.6% CAGR).

The prices paid for those deals were between 11.1-11.8x EBITDA, which sounds a touch pricey but pre-synergies Simx was already making EBIT margins of 16.7%, ClimaRad a whopping 41.8% and ERI 17.6%. As George says, the best way to view Volution's progress is to look back at the IPO, when its European operation was generating EBIT margins of just 10%. That has since soared to 24% as at H1 '23. Also, Volution now has three extremely profitable geographical territories and has expanded its footprint into Continental Europe and Australasia (the UK is now just £15.6m or 43% EBITDA with Continental Europe similar at £15.4m and Australasia (mainly NZ) £5.5m).



Three product categories

Volution is the dominant supplier of domestic ventilation products and systems in the UK, Continental Europe and Australasia. Its products include extractor fans (axial and centrifugal), ventilation and heat recovery systems as well as associated fittings and ducting. Increasing awareness of the link between pollution and lung diseases such as asthma, bronchitis, emphysema, as well as the shocking death of a boy living in Rochdale social housing, which led to tighter Government regulations (Awaab's Law requires housing associations to fix mould issues within specified timeframes) has increased demand for its products. Aside from a manufacturing plant in Macedonia, it's mainly an assembler of equipment for use in ventilation, using bought in electric motors and printed circuit boards (PCBs). Its footprint comprises seven UK facilities (including an injection moulding

Playtech (PTEC), 550p

Gambling operators such as **Entain**, 1302p (which owns Ladbrokes, Coral and Sportingbet) and **Flutter**, 15055p (Paddy Power, Fanduel) are betting the house on the extraordinary growth in US regulated online gaming, which grew 61% to an estimated US$12.2 billion in 2022 including US$6.9 bn in sports betting and US$5.5bn in igaming (casinos, slots, bingo etc.).

With US states eyeing up the tax revenue opportunities, this market is forecast to reach US$23 bn in 2026 with sports betting seeing the fastest growth at 20%. There's also a less heralded but equally exciting opportunity in South America where Mexico (population: 129 billion), Columbia and Argentina are thriving markets, while Brazil, the most populous (213 bn) with a GDP equivalent to over 40% of the whole of that Continent, has just legalised online betting. As a provider of software platforms to run online gaming websites (forming the bedrock of its B2B division) Playtech, which holds licenses in nine US states as well as a strong presence in Mexico and Columbia, is perfectly positioned to benefit. Indeed, the fruits are already showing with revenues from the Americas rising 43% to €145m in FY'22 and now represent almost a quarter of B2B EBITDA, which grew 15% to €160.2m, beating forecasts. Momentum is such that management has just introduced a new target to add €90m to B2B EBITDA to take it to €250m over the medium term, with Americas expected to be a higher contributor of an enlarged base.

Playtech is unique in that it not only provides software to run gaming websites and the content to run online casinos, blackjack, slots, sportsbooks and lottery but it also provides associated support services, such as player protection, CRM and data analysis to drive customer loyalty. Clients include Entain (the former GVC), Flutter, Caesars, Rank, Skybet, Betfred and Bet 365. Playtech usually charges 10-15% royalty on operators' sales and contracts are for three to five years.

The company has also been extraordinarily innovative and can now facilitate "mega" jackpots, linking millions of players across multiple countries and gaming operators, plus bonus features. A big opportunity is in "live" casino gaming where punters play with real croupiers. These feature a revolving studio and augmented reality with dealers dressed as Alice in Wonderland characters and roulette numbers replaced with iconic animals from those stories and where landing on them can generate 4x normal payouts. The number of live players increased 90% in 2022 while it's just won over Fanduel and launched a new live facility in Peru, taking total live studios to 10. The other opportunity is migrating customers towards a new SaaS offering, allowing customers to "plug in' anywhere around the world to access Playtech content but without the overheads, while set up costs and customization is also reduced. SaaS revenues grew 87% to €32m and management target €60m-80m medium term, and excitingly this will be higher margin as the investment has already been sunk.

Elsewhere, Playtech's B2C division Snaitech, which operates 1,600 betting shops and corners in Italy as well as an online version, has also been shooting the lights out with EBITDA up 39% to €245m. Here, management have set a medium term target to hit €300-350m and if all targets are met including B2B, group EBITDA could soar 50% to €600m!

Peel Hunt forecasts EBITDA of €428m for eps of 59.6 cents (52.3p) this year and €459m and 66.6 cents (58.4p) next, dropping the prospective PE to 9.5 and has set a 800p price target. Clearly if it hits its growth targets there will be large upgrades, while low leverage (net debt / EBITDA just 0.2x) leaves scope for acquisitions. *I am a buyer.* TMI

Kooth (KOO), 265p

According to an article in general medical journal, The Lancet, mental health disorders account for at least 18% of the global disease burden, and the associated annual costs are projected to be US$6 trillion by 2030. While evidence-based interventions do exist, only a small proportion of people, typically with the most acute symptoms, receive adequate treatment and waiting lists for CAMHS (NHS child and adolescent mental health services) can be more than a year. Against this backdrop shares in Kooth, the largest digital mental health provider for the NHS for children and young people aged 10-25, have doubled this year and over the month I met with its CEO, Tim Barker.

If you look at Kooth's forecasts (no profit is expected until after 2025) you might wonder what the fuss is about but Barker is following the Jeff Bezos (founder of Amazon) school of exploiting first mover advantage by reinvesting all profits and then some more to land grab as much market share as possible. That's resulted in sales more than doubling from £8.7m to £20.1m between FY'19-'22 and from 2024 they could really go into orbit after Kooth won the two largest contracts in its history with the US states of Pennsylvania (US$3m p.a.) and California.

As Barker says, California recently allocated US$4.76 billion for Child and Youth Behavioural Health and this contract, which covers all six million of its 13-25 year olds, is estimated by Panmure to initially be worth US$15m with scope for further increases and will result in a sales forecast upgrade when Kooth provides further contract details (in 4-8 weeks). Barker is also seeking further deals in the US with New York and North Carolina allocating US$50m and US$175m, respectively, for youth mental health funding and two dozen governors included the teenage mental health crisis in their "state of the state" addresses.

Kooth was founded in 2001 when therapist Elaine Bousfield had an idea to make access to mental health services available everywhere online, and reduce the stigma attached in asking for help.

Around 60% of users get self-help support through articles and advice to help improve mood (e.g. music to boost endorphins) as well as access to community support where they can chat with other users. The other 40% need professional support, perhaps for anxiety, depression and OCD, either through a one-off chat or more structured ongoing counselling and treatment, such as cognitive behavioural therapy. As Barker says, it's about finding the problem and creating goals and tools to cope. New users can remain anonymous as they must only divulge their age, sex and geographic region (name, address and phone number are not required) as well as complete a short questionnaire. It's clinically accredited by the British Association for Counselling and Psychotherapy and Kooth's directly employed team of 257 practitioners, counsellors and clinicians (total head count 460) decide what level of service is required.

Metrics show that between 70-75% of users say the service has been beneficial while the NHS is believed to save £3 for every £1 spent on Kooth; earlier intervention reduces costly treatments in residential CAMHS units, GP visits and school absenteeism. For the notoriously pricey US healthcare system that ratio is estimated to be an astonishing £12: £1!

Kooth has significantly increased market share within the NHS, while also operating a "land and expand" strategy to add older youths and adults and its service is now available to 16.7m young people (from 8m in 2019).

One other attractive feature is that contracts are multi-year and annual recurring revenue grew 25% to £21m last year (over 100% FY'22 turnover), underpinning forecasts for sales of £24.3m, £28.6m and £30.8m for FY'23-'25, which I expect will be upgraded on upcoming California news. *A classic concept stock revelling in the large addressable market; I am a buyer.*

plant in Reading), Germany, Netherlands, Belgium, Sweden, Bosnia, Italy, Spain, N. Macedonia and two sales offices in Australia and New Zealand. Its UK market share was c. 35% at IPO and is now "too high to disclose," says George, while it notably has 25% in Germany, a large market for heat recovery systems.

Push and pull model

Volution adopts a "push and pull" model for getting its product to market. It "pushes" its product to smaller end-users such as local builders, builders merchants, electrical wholesalers and hybrid retailers like Screwfix, while it "pulls" through product with contract specifiers (architects, mechanical & electrical contractors), developers and large house builders including a recent tie-up with Barratts. Around 30% group sales are for new builds and the remainder is RMI.

As George says, there are three tiers of spending: traditional extractor fans (de-centralised systems) used in bathrooms, kitchens and utility rooms typically costing £100-£150 for a 3-4 bedroom house; more onerous carbon reducing ones (£200-£400) and mechanical ventilation including heat recovery (MVHR) systems for the whole house (centralised systems), which cost up to £1,000 including accessories.

Innovation and smart technology also play their part in lifting average selling prices. As Aldous Huxley might say, it's a brave new world for gadgets. As examples, George says if you have a party and the amount of carbon dioxide rises to a level that could affect your health (making you feel sluggish) a sensor might now automatically increase the air flow, while those on holiday can remotely, from an app, put the system into holiday mode to reduce energy consumption. There are also key applications in the public sector where Housing Association landlords can use an app to track whether a tenant is using their fan correctly and for the right amount of time if there's a dispute over damp or mould issues.

Higher value Heat Recovery

The Holy Grail for Volution is to encourage purchasers to trade up from low tech single room fans to higher value low carbon and in particular the larger centralised systems, and there are two tail-winds driving this trend. The first is Volution's expansion into heat recovery ventilation systems, boosted by the acquisitions of ClimaRad and ERI.

Heat recovery ventilation systems are used to heat or cool the incoming outside air and replace it with the stale outgoing air to maintain a stable overall temperature. Depending on the season it also either removes excess moisture or adds more (usually air is more humid in summer and drier in winter), which also reduces the energy required to control the building's climate. A further important benefit is that heat recovery ventilators eliminate the pathogens, bacteria and viruses from the outside air going into the building.

Tighter Building Regs drive demand

A second tail-wind driving demand for its higher value systems is the political push to end carbon emissions. The UK Government became the first major economy in the world to pass laws to achieve "Net Zero" in 2019, effectively ending its contribution to global warming by 2050. Interestingly, Blighty had already reduced emissions by 42% from 1990 levels, in large part by reducing the energy consumption emitted by homes (30% of total energy consumption). Successive Governments have tightened building regulations for new homes (Part L) to improve energy and power conservation and prevent carbon escaping into the atmosphere; George says a typical AC fan used to require 30-40 watts, now it's just 5. As a result, new buildings have become more air tight but they must also comply with Part F (ventilation) as air tight buildings need better air flow without losing warmth and this double whammy has been great for Volution.

£125m for acquisitions

With even tighter building regs in the pipeline, the outlook is therefore positive but there's one other factor that could also drive eps growth - further M&A. With little capex required, Volution throws off considerable amounts of free cash flow and George expects net debt / EBITDA to drop from 0.8x to just 0.4x this year and zero in FY'24 and with a maximum headroom of 2.0x, that implies firepower of up to £125m for further acquisitions.

Therefore, while at first blush the prospective PE of 16.9 (eps: 24.5p) falling to 16.2 (25.5p) next year doesn't appear cheap, it could fall sharply as deals flow in. The fact that 76% of its plastic is recycled may also attract ESG focused funds to its shares. *I am a buyer.*

Restaurant Group

Sector: Travel & Leisure | Share Price: 39p | Epic Code: RTN

Key Data

Address:	5-7 Marshalsea Road, Borough, London, SE1 1EP
Telephone:	020 3117 5001
Shares in issue:	765m
Market Capitalisation:	£298.4m
Next Results:	Interims: September

As the pandemic raged, according to the Local Data Company (LDC), which monitors 3,000 areas across England, Scotland and Wales, 700 outlets disappeared from the UK restaurant sector in the two years to March '22. Italian and pizza restaurant chains fared the worst, shedding a net 448 sites while American-themed chains fell by 151 outlets. Anecdotally, Byron, Gourmet Burger Kitchen and Italian chains Strada, Carluccio's, Prezzo, Pizza Express and Bills have been among the casual dining brands forced to shed dozens of sites

Apres le deluge, the survivors are getting stronger and it's no coincidence that Restaurant Group, whose 410-strong estate includes *Frankie & Benny's* (American themed), *Wagamamas* (Asian cuisine) as well as a collection of pubs, airport concessions and smaller brands, has put out strong trading figures for the eight weeks to 26th February, notably a 16% rise in dine-in sales at Wagamamas. But having again met with the head of corporate development at Restaurant Group, I believe there are nine other reasons to buy the shares, which even after a mini rally are still well below former highs of 540p.

History

Restaurant group can be traced back to 1979 when restaurant entrepreneur Philip Kaye founded Garfunkels, a London-based concept combining British and American dishes popular with tourists. Garfunkels had its time in the sun and for a while so did its next concept, Frankie & Benny's, a casual dining concept styled on a 1950s New York Italian diner, located in edge of town retail and leisure parks. Eps rose from 6.3p to 30p between 2001-2014 but management committed unforced errors by over-pricing and removing a much loved budget package and sales declined.

More than halved rent bill

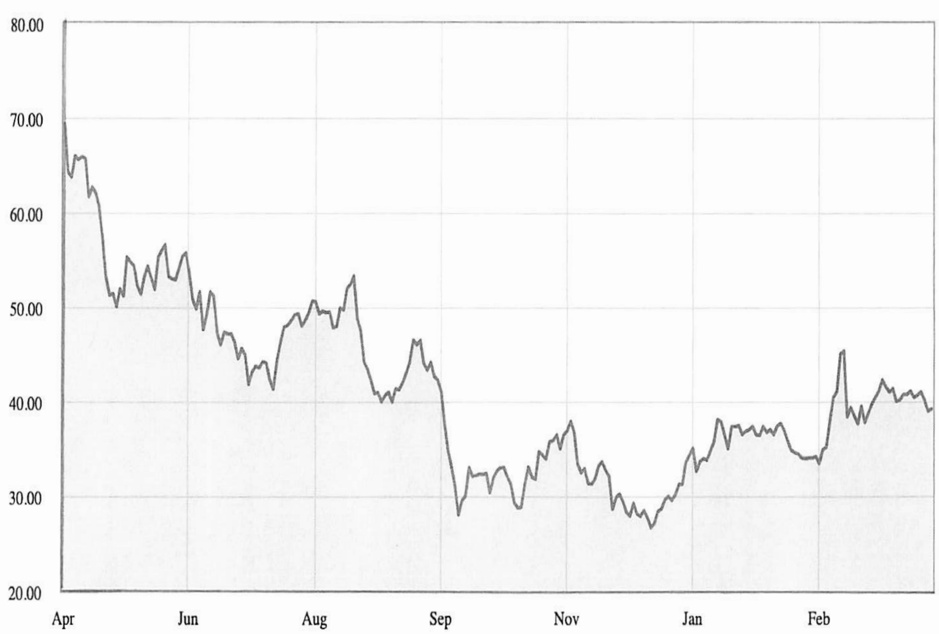
While a new team grappled with this problem it somehow found time to make the largest acquisition in the company's history of Wagamamas, a fast-growing pan-Asian chain of restaurants but the hefty £559m purchase price was controversial because it was obliged to scrap a chunky 17p dividend and conduct a hefty 13:9 rights issue at 108.5p alongside the assumption of significant debt. Nevertheless, Wagamamas' subsequent outperformance meant it entered the Pandemic in stronger shape than might have been expected.

New CEO Andy Hornby authorized two placings (at 57p in April '20 and 100p in March '21), increasing the share count by 55%, while more than halving the mammoth rental charges from £933m to £435m via lease exits, administrations, CVAs and concessions renegotiations, which alongside Government support has reduced net debt / EBITDA to 2.2x.

Five divisions

Restaurant Group reports across five segments which at FY'22 had the following number of outlets:

- Wagamamas: 156
- Pub Restaurants:79
- Concessions: 42
- Leisure: 116
- Barburrito: 17



Wagamamas shooting lights out

It's no exaggeration to say that the acquisition of Wagamamas has transformed Restaurant Group's fortunes. Market research firm Coffer Peach says its sales outperformed the sector by 3% in FY'22 and interestingly, by a cumulative 23.9% in the three years between FY'17- FY'19 before the Pandemic. Meanwhile, its NPS is joint top (with Nandos) of 10 casual dining brands at 47 with Prezzo and Zizzi joint bottom on 30.

Founded in 1992 in Bloomsbury by restauranteur Alan Yau, Wagamamas quickly grew under successive private equity ownerships of Graphite Capital, Lion Capital and Duke Street Capital. Today there are 156 outlets in the UK, making it more than three times the size of nearest rivals Yo Sushi with 73 and Giggly Squid with 30 and these are located mainly in towns and cities and shopping centres.

ROCE: 35-40%

The Wagamamas concept was inspired by fast-paced Japanaese ramen bars with its Asian inspired menu backed up by a focus on fresh ingredients and rapid service. Main dishes include curry, ramen, donburi, teppanyaki and kokuru bowls with popular choices including chicken katsu, chilli squid and sticky ribs. Its core audience is students and young professionals although it's popular with other demographics also. Average spend per head is £14-£15.

An indicator of its potential is that new openings, which cost £1.2m-£1.4m, achieve nearly £500,000 EBITDA per annum (on weekly sales of £40-£45,000) with return on capital employed (ROCE) running between 35-40%. Management intend to open five new outlets per year with expansionary capex £27m in FY'23, rising to £32.2m in '24 (total capex: £45m and £53m).

International opportunities

When buying into Wagamamas, management also took on board a small "dark kitchens" (delivery only) business, which has struggled post lock-down and pared back from 8 to 3 sites. More promising is its international business (20% interest), a joint venture based in the USA and run by a local partner. This side owned two new restaurants in FY'22 in Atlanta and Tampa with another two in Dallas and Arlington slated to open this year and the plan is to expand to 25-35 by the end of 2027. The international arm also comprises 65 franchised restaurants, with seven opened last year mainly in Italy and the Middle East. Excitingly, if things go well Restaurant Group has an option to buy back the 80% it doesn't already own in 2027.

Pubs going well

Restaurant Group is lucky that two other segments have also shot out of the blocks in the first eight weeks including its pubs (like for like sales: +14%) and concessions businesses. The former consists of a small chain of character properties in rural locations, with limited direct competition. These target a more affluent and older customer base, typically 25,000 ABC1s within 15 minute driving time, while 60% of sites have outdoor space for 100 covers. Local managements are given autonomy to jazz up the core menu of fish and chips, steak and burgers with Asian and Mediterranean cuisine. The original plan was to double its footprint but that's been put on hold until debt is reduced.

Prospects within concessions (+56% like-for-like sales) are also bright. Here, it operates 42 concessions (39 airports, 3 rail) with 70% revenue generated from major UK airports such as Heathrow, Gatwick, Manchester and Luton as well as contributions from Scottish airports. These are typically on turnover-based rents rather than fixed.

Nine reasons to buy shares

In my opening I highlighted nine reasons to Buy rate the shares. First and foremost the company has announced a new target to increase EBITDA margins 2.5%-3.5% by FY'25, from its recent low point of 8.3% in FY'22, via volume and pricing increases (especially Wagamama), cost efficiencies at corporate level, gas & electricity deflation (as energy hedges roll off) and supplier contract negotiations such as for food & drink. With pro-forma EBITDA margins having been 14% as recently as FY'19, this target could ultimately prove conservative.

Less competition

Secondly, management are conducting a second review of casual dining capacity in the areas they operate in this summer (after a previous one 18 months ago highlighted a 21% reduction in sites) and the company believes it will indicate this shrinkage has significantly accelerated, which could make it easier to drive price increases and attract more customers.

Third, as well as less competition, the other tangible benefit for those operators still standing is rock-bottom commercial rents (down as much as 40% from former peaks) and Restaurant Group, whose goal is to grow Wagamamas from the current 156 to 200 outlets, is opening five new outlets a year, while its recently acquired Mexican chain, *Barburritos*, purchased last July for £7m, will see an additional three a year from FY'24 from a base of 17.

Cutting losing sites

Fourth, while "running its winners" it's also restructuring the under-performing elements, targeting a reduction of up to 35 of the 116 sites within its Leisure division (mainly Frankie & Benny's). A significant number of the 35 are loss-making while others operate only marginally above break-even and are projected to go into loss. Usefully, 13 of these sites will have no cash cost to exit because the lease is expiring or there's a break, another seven are freeholds which will raise c. £5m, a further 1-3 will be converted to Wagamamas and the remainder (up to 20) will require a lease provision for an accelerated disposal.

Improved food offering

Fifth, the company has radically overhauled its Leisure menu, eliminating frozen food offerings in favour of fresh ingredients, as well as reducing menu items by 20% to support the above and reduce wait times. Brand health tracker, BrandVue, says Frankie & Benny's net promoter score or NPS (measuring customer loyalty, satisfaction and enthusiasm) has already improved 10% while Leisure like-for-like sales, which were flat in FY'22, are 2% higher in the first eight weeks.

Sixth, its concessions business, which comprises 42 outlets predominantly situated in the largest and busiest UK airports, is enjoying a strong recovery as consumers switch from DIY and sofas to longed for overseas holidays. Passenger volumes are projected to grow from 75% of pre-pandemic levels to 85% this year and 100% by FY'25.

Debt reduction on track

Seventh, unlike many of its rivals it enjoys a robust financial position. Net debt has fallen from £286m in FY'19 to £186m at FY'22 (net debt: EBITDA: 2.2x) with management's target to reduce leverage to 1.5x by FY'25. After restructuring its bank facilities including an interest rate cap on £125m of debt at 0.75% (saving £4m a year at a bank rate of 4%) it has available headroom of more than £145m and if things get tight could release equity from its largely freehold pubs chain, which has a book value of £160m.

Low valuation attracts predator

Eighth, the shares are cheap, with broker Jefferies estimating they trade on an enterprise value / EBITDA of just 5.8x, which is pricing in a 20% downgrade that now looks unlikely given self help targets.

Ninth, and perhaps attracted by the above, activist investor Oasis Management, a Hong-Kong-based hedge fund, which owns 6.5% of the business, was quoted in the Financial Times as "aiming to push Restaurant Group into a virtuous circle where it can reduce debt, reduce interest, resume dividends…get a higher stock rating and market cap and attract better people." Oasis released a public letter calling for a change of governance and has called for a seat on the board. Clearly, if Restaurant Group's self-help efforts don't bear fruit quickly enough it's ripe for take-over.

Trading ahead of expectations

With 2022 results having beaten expectations (pretax profit £20.3 vs £17.1m forecast) there is clear momentum going into this year and beyond. Peel Hunt has upgraded pretax forecasts from £10m to £15.8m (eps: 1.8p), £19.9m to £24.3m (2.6p) and from £24.3m to £36.1m (4.0p) for FY'23-'25, dropping the prospective PE to just over 15 for next year, and then 10. Its price target is 60p while Jefferies has an even punchier DCF-based price target of 105p, recalling EV / EBITDA valuation multiples last seen when the business was performing well pre-2015. *I am a buyer.*

Updates, upgrades and downgrades

UP Global Sourcing (UPGS) 148p
Sector: Household Goods

UP Global's H1 revenues rose by 2% year-on-year to a record £87.6m, a resilient outcome given the challenging macro backdrop and limited product price inflation. Revenues via online channels rose strongly by 78% (24% mix changes) vs 15% last year with buoyant online demand for energy efficient and money saving products offsetting a decline in revenues to supermarkets and discounters who faced overstocking issues post the pandemic. Encouragingly, stock levels at these customers appear to be receding in the UK and more normal patterns of order placing have started to recommence. Gross margins increased by 30bps to 24.7% driven by the positive mix benefit from higher online sales coupled with benefit of lower freight rates towards the end of the period. Strong cost control helped by increased use of process automation to drive efficiencies and productivity improvements, offset inflationary pressures, leaving adj. EBITDA level yoy at £11.2m. The balance sheet remains in good shape with strong cash flow reducing leverage (net debt / EBITDA) from 1.9x to 1.0x.

Eps is forecast to rise from 14.3p to 14.7p year to July, and then 15.4p and 17.0p in FY'24 and '25. Canaccord highlights multiple revenue opportunities together with margin expansion potential and strong forecast free cash flow generation, allowing for further business investment and dividends with leverage forecast to halve to 0.5x by FY'25. *I am a buyer.*

At the time of going to press, the editorial team held the following shares mentioned in this issue: Luceco, Restaurant Group, UPGS, S4 Cpaital

Updates, upgrades and downgrades

Central Asia Metals (CAML) 234p
Sector: AIM, Mining

Having registered a high of 292p the shares have rattled back to 234p on news of a US$55m impairment charge at its zinc / lead *Sasa* mine in Macedonia attributed to management now not expecting ore throughput to step up to 900ktpa from FY'25 but rather remaining at 830ktpa as it means the mine life rises to 2039 from 2037. But the investment case hasn't changed.

While full year EBITDA of US$132m was a shade below forecasts (US$136m) and free cash flow US$90m (US$100m forecast) the US$187m debt taken on to fund Sasa has been repaid and net debt has swung from US$36.2m in FY'20 to net cash of US$59.2m. A 10p final dividend and total of 20p gives a yield of 8.5%. Adjusted eps were 48.2 cents (FY'21: 47 cents).

At *Sasa*, EBITDA was US$56.4 million (FY'21: US$57.5 million), with a margin of 52% (56%). The average zinc price increased 11% but lead reduced 4%. Treatment charges reduced but overall costs increased due to rising electricity, mitigated by weaker Macedonian Denar to US$. Lower gas prices should create a tail-wind from H2. This year will be a transitional one, from the sub-level caving mining method to a paste fill approach but elevated capex of US$28m-US$30m (including US$12m to complete cut and fill) will reduce sharply from 2024.

At *Kounrad* (Kazakhstan) EBITDA was US$94.9 million (FY'21: US$106.0 million), with margin of 77% (80%). Profit decreased due to an 8% drop in copper prices and increase in costs due to employee pay rises, mitigated by the weaker Kazakhstani Tenge vs US Dollar. I expect the resurgent Chinese economy and tight supply to reinvigorate copper prices later this year, with CAML remaining unhedged.

Another acquisition wouldn't go amiss given the cash burning CAML's pocket. I continue to hold.

Energean (ENOG) 1304p
Sector: Fossil Fuels

The shares spiked by almost £3 after Energean revealed a 20% increase in 2P reserves to 1,161 million barrels oil equivalent (boe) after five out of five discoveries including the *Athena, Zeus* and *Hera* structures, in the *Olympus* block. Revenues rose 48% to US$737m while EBITDA before exploration was US$422m (+99% year-on-year) on production of 41,200 boepd (FY'21: 41,000), far exceeding Peel Hunt's EBITDA forecasts of US$347m. Net debt rose a quarter to just over US$2.5 billion.

First gas at the flagship *Karish* block in Israel was achieved in Q4'22 and (reiterated) forecast production is for 131,000 boepd this year rising to over 200,000 in H2 '24.

Capex is expected to remain elevated this year at US$814m (FY'22: US$866m) but mainly switching from Israel to the smaller Egypt and Italy assets before falling to US$539m in '24. In turn, net debt is forecast to increase to US$2.6bn before falling to US$2bn in '24.

Nevertheless the reliability of the long-term fixed priced contracts for Karish gas in Israel has led to another 30 cent quarterly dividend and analysts expect a 141 cents pay-out this year and 169 cents (137.4p) next for a prospective yield of 10.5%. Ultimately, the plan is to return US$1bn a year when debt is lower, for an estimated payout, based on the current 171m shares in issue, of 437p a share!

Peel Hunt forecasts eps of 341 cents this year and 560 cents next. Its share price target is 1850p while Investec is gunning for 2150p.

Gain since my original piece at 515p in August '18 is 153%. A fantastic "total return stock" to date, I am running profits.

Vistry (VTY) 808p
Sector: Home Construction

Vistry reported in line results with pretax profit up 21% at £418m and sales increasing 14% to £3.07bn. Eps rose 18% at 137p and the dividend was 55p (FY'22: 60p) reflecting higher share count to fund Countryside, which also reduced net cash to £118m from £235m.

In Housebuilding (EBIT profit +26% to £383m) it delivered 11,951 completions, up 8% year-on-year, with average selling prices up 6% at £324,000. Forward order book was unchanged at £1.32bn. A key stand-out is that while its peers expect build cost inflation of 4-6%, Vistry has guided to unchanged costs, helped by the extra scale from Countryside at a time when peers are seeing material drop in volumes.

Within Partnerships, profit was £100m (also +26%) whilst the forward order book is £2.84bn, with 69% mixed tenure volumes. The appetite from Housing Associations remains strong while a growing number of local authorities are engaging with Vistry to develop their land. Institutional demand for PRS has returned after a hiatus in Q4'22.

Like others, Vistry has seen an improving trend in the first few months of 2023 with average private sales rate per site up sharply from a low of 0.46 in Q4 '22 to 0.62 in the past four weeks, while target synergies from Countryside have been upgraded by £10m to £60m with £25m expected in 2023.

Peel Hunt's forecast is for pretax profit of £458m, £506m and then £583m for FY'23-'25 and eps of 93.3p, 104.7p and 122.1p, respectively.

Its price target is 1075p, conservatively based on 1x tangible NAV for house building and a PE of 11 for Partnerships. *A main buy at 653p in December. I am still a buyer.*

Judges Scientific (JDG) 9260p
Sector: AIM, Electronic & Electrical Equip.

New share price highs are as rare as hens teeth in present markets but Judges Scientific is one, rising to £96 in February after final results beat upwardly revised expectations. Sales rose 24% to £113.2m, with Rest of World up 19%, USA and China +6% while Rest of Europe and UK were down 2.5% and 28%, respectively. Eps rose 53% to almost 364p (5% beat) and pretax profit was +56% to £31m, with EBIT margins jumping from 21% to almost 27%. Oil services firm, Geotek, its largest ever deal, contributed to this and achieved the full-earnout (total consideration: £80m) after hitting its target of £11.3m EBIT profit in 2022. That deal also increased net debt to £52m from £1m cash.

Organic order intake rose 0.5% to a new record and after a weak H2 there was a strong recovery in December as Covid restrictions were lifted in China while capex freezes amongst clients are said to have become less severe.

Shore Capital forecasts eps of 352p this year and 370p next, for a PE of 25.3 and then 24.1p. High but its track record, growth prospects (including more acquisitions) and cash generation more than justify the rating. *I am continuing to hold.*

Sanderson (SDG) 131.5p
Sector: AIM, Household Utilities

Sanderson has entered into two major multi-year licensing agreements. The first gives Next exclusive rights to produce a range of *Clarke & Clarke* homeware products including bedding, towelling, tableware, furniture and lighting. The agreement will run for a period of five years from product launch in spring/summer 2024. Licensed products will be available in Next stores and online at next.co.uk, and will also be wholesaled to third parties.

Most recently it signed a deal with J Sainsbury, in which the supermarket group's *Habitat* homewares brand and *Tu* clothing brand will develop a wide range of licensed products in collaboration with SDG's *Morris & Co*. and *Scion* brands, marking this the first time that the Company has collaborated with Sainsbury's. Specifically, Habitat will launch homeware products featuring designs from the Morris & Co. and Scion brands and womenswear and childrenswear with Tu for launch next spring.

The multi year licensing income underpins unchanged forecasts from Investec for eps of 13.7p for the year that started 1 February, rising to 14.4p in FY'25. The shares are cheap on a prospective PE of just 9.6 and the broker's 210p price target shows the upside potential. *I am a buyer ahead of results of 26th April.*

Updates, upgrades and downgrades

Luceco (LUCE) 113p
Sector: Electronic & Electrical Equip.

Luceco is shaping up to be a potential winner for 2023. Although results showed revenue down 10% to £206.3m and adjusted EBIT of £22m (down 43.5%) these are backward looking. Gross margin has improved from 37.1% in FY'21 to 38.1% in H2 '22 and cost inflation (energy, freight rates) and de-stocking are expected to reverse.

De-stocking affected its most profitable wiring accessories business (switches and sockets, circuit protection, junction boxes, cable management) as large customers such as Screwfix reduced orders in response to DIY demand being switched off when the Ukraine crisis hit, after previously booming when people were locked down. Wiring accessories' EBIT margins fell from 27.9% to 18.9%, dragging EBIT profit down 52% to £13.9m on revenue lower by 30% to £73.7m but I expect a recovery, the catalyst being the fall in mortgage swap rates, a reversal in bank rates plus lower energy costs.

Portable power profit fell 27% to £4.7m due to weakness in electric vehicle charger sales, albeit Luceco is cutting costs by insourcing production to China. One bright spot was the counter-cyclical LED Lighting business (sales +29% to £81.2m; profit unchanged at £3.4m), thanks to first time contributions from DW Windsor (makes outdoor street lighting) and Kingfisher Lighting (outdoor lighting for sports, high masts and rail) as well as demand for energy saving retrofits.

Thanks to its strong cash generation net debt fell from £38.1m to £29.4m (net debt / EBITDA: 1x), leaving headroom of £56.9m and is forecast to reduce to just £3.3m by FY'24, providing considerable firepower for more acquisitions.

Numis forecasts eps of 8.8p rising to 10.8p and then 13.7p in FY'25 but there's considerable upside potential. *I am a buyer.*

Ten Entertainment (TEG) 285p
Sector: Tourism & Leisure

The ten-pin bowling operator again (slightly) beat expectations with revenues of £126.9m and EBITDA of £39.6m (Liberum's estimate was £37.8m), for an EBITDA margin of 31%.

Bowling revenues almost doubled from £30m to £55m; food & beverage went from £19m to £35.3m and machines, amusements & other from £18.6m to £35.6m. Having positioned itself in the value pricing segment it's capitalising on the increasing popularity of social entertainment while digital innovation (online bookings, comparing scores etc.) and a newly launched loyalty app have added to its universal appeal. Revenue per head increased 8.9%, in spite of lowering average realized price per game marginally to £5.13, as promotions and cheap deals (a family of four can bowl for just over £20) drove footfall up almost 42%! Like-for-like sales rose in the first ten weeks by 2.7%, against tough comparables.

There were two new additions (Walsall and Harlow) in FY'22 and Crewe has opened this year, taking the estate to 49 units. Out of the c. 320 UK sites only **Hollywood Bowl,** 254p, is bigger with 67. Work is underway at Milton Keynes and Dundee with a fourth close to signing and several under negotiation, says Liberum. The group also undertook six full refurbishments, as well as five bowling upgrades, adding 10 escape rooms, 10 karaoke rooms and 10 additional lanes and completing the Pins and Strings roll-out. Capex was £20.3m (FY'21: £16.3m) but year-end net cash was £10.1m (FY'21: debt: £2.5m).

Highlighted as a New Year Nap at 244.5p the shares have gained 16.6% but on unchanged eps forecasts (32.8p in FY'23), the PE is just 8.7. *With the broker's price target 400p, I am a buyer.*

S4 Capital (SFOR) 157p
Sector: Media

While the shares have been battered by concerns over the US economy (its biggest market) S4's results beat expectations with EBITDA of £124.2m beating its guidance of £120m, on sales of £891m (+24%). Adjusted eps was 11.8p (consensus: 11.7p) and net debt was £110.2m (beating guidance for £130m-£170m). As broker Citi notes there will be a sigh of relief that "concerns over whether the complexity of the roll-up nature of the business would hinder operational / financial performance) have been allayed." Without highly rated paper for more deal, Sorrell has rolled his sleeves up on basic housekeeping with strong cost control / staff utilization and this time avoiding a delay to results.

Admittedly it's pared back organic revenue guidance to just 8-12% for the current year (not helped by losing one contract) but that's countered by slightly higher EBITDA margin assumptions of 15-16%.

Citi has shaded revenue forecasts growth from 15% to around 12.5% (£1,199m) in FY'23 but with EBITDA margin towards the top of the range, giving pretax profit of £114.7m and eps of 12.7p (from 13.1p). That doesn't justify the low prospective PE of around 12. Remember the shares were on a PE of nearly 70 at the old high of 873p! *While it can be dangerous to fight the market, with debt levels under control, I am a speculative buyer.*

Essentra (ESNT) 195p
Sector: Industrial Services

Results for 2022 offered the first glimpse of Essentra's rosy future as a stand-alone components business. It recorded 12% revenue growth (c. 6.5% organic) and lucrative EBIT margins of 18.9% before central costs which, as Berenberg says, "demonstrates an ability to protect profitability and drive growth despite the challenging macroeconomic backdrop." The broker goes on: "from here the story is compelling: cash disposal proceeds will fund the restructure of the group, invest in a new enterprise resource planning (ERP) system to drive growth; build out its digital offering; drive enhanced customer offering and cross-selling; conduct M&A; and return £150m to shareholders" (it recently went ex a £90m (29.8p) special dividend and is conducting a £60m share buy-back). "Further, it's paid down US$247m of US$350m private placement notes, significantly reducing the interest burden…A medium term ambition to triple operating profits offers attractive shareholder returns…. Pro-forma modelling suggests c. 20% annual returns for investors are available (5% M&A, 5% organic, 10% margin uplift)"

Looking forward, customer de-stocking in the US is a short-term drag, but China is opening up and Europe is robust; year-on-year order intake is up 8%. Last December' purchase of Wixroyd is performing as expected and "is the first of multiple acquisitions in fragmented end-markets."

Unchanged expectations mean Berenberg forecasts EBIT of £46m (from £43m), rising to £54m in FY'24 for eps of 10.7p and 13.7p. Cluster buying by directors adds further confidence. *I am a buyer.*

Michelmersh (MBH) 93p
Sector: AIM, Construction

In spite of tough conditions for brick manufacturing Michelmersh's results were ahead of expectations. Helped by price rises to mitigate cost inflation revenues and pretax profit rose 15% to £68.4m and £12.5m, respectively. Net cash was £10.6m thanks to strong free cash flow while there's a £20m undrawn borrowing facility to support M&A. Last November it acquired FabSpeed, a fabricator of pre-built brick products such as chimneys, arches and dormers, for an initial £6.25m (just 5.3x EBITDA) and more deals are set to follow.

Berenberg puts its outperformance down to its smaller volumes and high end / specialist projects and more diversified order book, allowing it to charge premium prices; EBIT margins were a resilient 18.6%.

Trading on a prospective PE of 9.1 and 6.0x EV / EBIT Berenberg says the shares are very cheap. The broker's price target is 170p. *I will look to buy on dips*.

Moonpig (MOON) 115.5p
Sector: Retailers

A good end to the year for Moonpig, with its strongest-ever Mothers' Day. Greetz's trading followed a very similar trend and while recent acquisition Buyagift was slower after Xmas, it was in line with expectations. As a result, Moonpig has clawed back ground lost from a weak Xmas where the postal strikes dented confidence in delivery (as final posting dates were brought forward) and has maintained EBITDA guidance of £84m.

Looking ahead to FY24, management expects sales to grow in high single digits (below long-term guidance to which it should return the year after), and that the nature of the growth will be H2 weighted. Peel Hunt forecasts eps of 10.1p for the year to April '23, rising to 11.8p and then 13.8p in FY'25. *Trading on a soon-to-be prospective PE of 9.8, well below its old rating, the shares are a buy.*

TMI Trader Portfolio 2

With bank and interest rate nervousness casting a shadow over small cap shares, the TMI Trader Portfolio rose 1.4%, marginally outperforming the Small-Cap index.

With a busy month for news, the portfolio reflects a receipt of the 29.8p special dividend from Essentra. Now shorn of its lower margin healthcare packaging and filters divisions, Essentra recorded lucrative EBIT margins of almost 19% alongside 12% organic sales growth in its first results following the disposal. Berenberg is expecting further acquisitions but even without one, next year's prospective PE drops to 14.2. Seven directors "cluster bought" around current levels with the Chairman and CFO together acquiring almost 25,000.

Elsewhere, a director also bought Central Asia Metals after its results, which confirmed that all the (US$187m) debt used to fund its purchase of the Sasa zinc / lead mine in N. Macedonia has been repaid in its entirety with the business swinging to net cash of US$59.2m. All eyes should now be on the copper price, which has recovered above US$4/lb after an earlier wobble - especially as CAML is now running an unhedged position, making this a swing factor.

DX has announced the opening of four new sites at its parcels division (Merseyside, Shropshire, Bracknell, Swindon) - reducing stem mileage and facilitating new customer wins and the shares look cheap on a prospective PE dropping to just 7.3 (FY'24 eps forecast: 4.0p) on 1st July.

Two other constituents, Reach (AGM and trading update 3rd May) and H&T (AGM: 10th May) are expected to update on current trading shortly.

This month I feature a new name, Volution (page 1), a highly profitable market leader in domestic ventilation, which has more than quadrupled EBIT profit in the past 13 years. In an era where climate change and violent weather events dominate headlines, Volution, which makes almost 70% of its sales from carbon reducing products and 32% of sales from heat recovery products, is well placed to prosper. The business has modest gearing and has considerable firepower for acquisitions.

I have also revisited Restaurant Group, where key brand *Wagamamas* put out a 16% jump in like-for-like sales for the eight weeks to 26 February, while it has set a target to increase EBITDA margins by up to 3.5% by FY'25, by closing a large number of unprofitable sites and cutting costs. Jefferies has a punchy DCF-based price target of 105p, recalling EV / EBITDA valuation multiples last seen when the business was performing well pre-2015.

Lastly, I also include Kooth. With mental health disorders accounting for at least 18% of the global disease burden, and the associated costs projected to be US$6 trillion by 2030, the digital mental health services firm Kooth enjoys a growing base of recurring revenue from NHS Trusts but has just struck the big time in the larger US market with two contract wins. I may revisit if its winning streak continues.

PERFORMANCE TABLE

	Current Value	Change on One Month	Change Since Start
TMI Trader Portfolio 2		+1.4%	-2.8%
FTSE-100	7843	+6.0%	+32.8%
FTSE-Small Cap	6180	+0.9%	+3.6%

TMI TRADER PORTFOLIO 1

Starting Capital (25.3.02):	£100,000
Termination Value (11.12.20):	£618,710
Portfolio gain:	+518.7%
FTSE-100 gain in period:	+24.7%
FTSE-All Share gain:	+44.6%

EPIC	Quantity	Description	Date Bought	Acquisition price (p)	Book Cost (£)	Current Price (p)	Current Value (£)	Change (%)
DX.	45,000	DX Group	16/11/20	19.5	8,820	29	13,050	+48
CAML	4,250	Central Asia Metals	21/12/20	224	9,565	234	9,945	+4
RCH	3,600	Reach	21/6/21	263	9,560	75.5	2,718	-72
ESNT	3,000	+ Essentra	22/11/21	284.2	8,571	195	5,850	-32
SUR	12,000	Sureserve	10/3/22	79	9,525	88	10,560	+11
SRC	11,000	SigmaRoc	16/3/22	83	9,175	55.5	6,105	-33
BAB	2,800	Babcock	14/4/22	323	9,134	296	8,288	-9
HAT	2,600	H&T	7/7/22	361	9,431	460	11,960	+27
PTEC	2,400	Playtech	26/9/22	378	9,162	551	13,224	+44

Stock value	£81,700
Cash	£15,482
Total fund value	£97,182

* Part profits taken + Acquisition price adjusted for special dividend

Starting capital £100,000 (December 2020)

Current holdings in the portfolio are valued at mid-prices and include dealing commission

The Momentum Investor is published 12 times a year. It reviews the market for companies whose earnings, sales or stock prices are rising. We place less emphasis on price earnings ratios and more on the search for relative strength and quality. The latter can include superior management, product or a key franchise. Our aim is to help you buy companies that deliver positive earnings surprises and see upward earnings estimate revisions, and sell those with negative surprises and downward revisions. Quite often a previous tip is again rated a buy. This normally arises where subsequent good news justifies buying at the higher price. Selling, though, is the essential second half of any successful investment deal. TMI's philosophy is not to sell a stock just because it is "expensive," but to only advise selling if the momentum breaks, or the fundamentals deteriorate. Where appropriate, we will suggest levels, to protect gains and minimise losses.

• *Unless otherwise stated, share prices quoted are correct as at 13/4/23*

ISSN 1476-895X