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Verbrec Limited

Renewed growth focus delivers upside

Verbrec have reported 1H24 results with revenue and EBITDA ahead of forecasts on a continuing operations basis. These are promising signs as management has addressed many of the issues previously impacting the company. We anticipate cleaner reporting to commence in 2H24 with no material impacts of discontinued operations and the finalisation of legacy projects. We have made slight amendments to our forecasts with improved gross margins. Our DCF derived fair value is unchanged at $0.21 per share (90% upside).

- **1H24 results beat forecasts:** Revenue declined 15% YoY to $50.0m vs. 47.3m Veritas estimate (6% beat). As anticipated the decline was due to the divestment of the unprofitable Site Skills Training business (c$4m revenue per half) and a stringent selection of projects for margin expansion. Gross profit margins increased 820bps to 34.9% vs. 32.5% Veritas estimate (7% beat). Normalised EBITDA increased 12% to $5.0m vs. $3.3m Veritas estimate (50% beat).
- **Overhang gone:** The company is now entering clear air with the finalisation of the legacy projects completed, which has plagued the company for several years, and the sale of the unprofitable training business will result in cleaner reporting going forward. The company also completed a capital raise in the period, raising $3.95m to fund growth and reduce net debt.
- **Investment thesis unchanged:** New leadership and a renewed operational focus underpins the growth of the business. We anticipate seeing an improving cash position from 2H24 onwards.
- **Changes to forecasts:** Revenue in FY24 is slightly lower than forecasted due to more payable working days in the first-half compared to the second-half (Figure 1). Strong growth in gross margins from a focus on selecting more economically attractive projects has resulted in an upgrade to our EBITDA forecasts. EBITDA increases 14% and 11% in FY24 and FY25 respectively against previous forecasts on gross margins increasing 160bps and 200bps in respective years.
- **90% upside:** Our DCF derived fair value is unchanged at $0.21 per share. At our fair value the company trades on an EV/EBITDA multiple of 5.3x in FY26 versus 2.9x currently in FY26.

Figure 1: Changes to Veritas forecasts for VBC

	FY24E			FY25E			FY26E		
Year ended June 30 ($m)	Old	New	Chg.	Old	New	Chg.	Old	New	Chg.
Revenue	98.5	97.3	-1.1	111.0	111.0	0.0	122.7	122.7	0.0
Growth (% YoY)	-16.7	-17.6	-1.0	12.7	14.0	1.3	10.6	10.6	0.0
Underlying EBITDA	7.4	8.4	1.0	9.2	10.2	1.0	11.2	12.4	1.1
Margin (%)	7.5	8.6	1.1	8.3	9.2	0.9	9.2	10.1	0.9
Profit before tax	4.7	4.7	0.1	6.7	7.7	1.0	9.2	10.4	1.1
Normalised dil. EPS (cps)	1.8	1.9	0.0	2.3	2.7	0.4	3.2	3.6	0.4
Capex	-1.0	-0.6	0.3	-1.1	-0.8	0.3	-1.2	-0.9	0.4
Free Cash Flow	2.5	3.3	0.8	7.3	8.6	1.3	11.1	12.4	1.3

Source: Company data, Veritas estimates

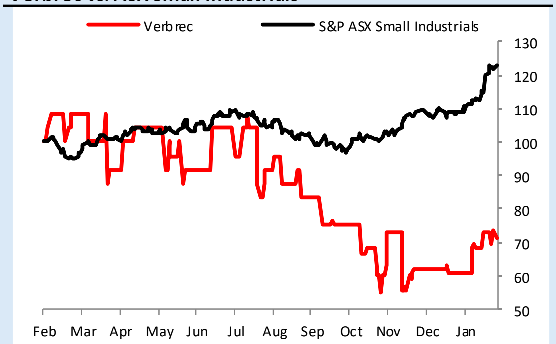
VBC.ASX BUY

Monday, 4 March 2024

Share Price	$0.11
Price Target	$0.21
Valuation Method	DCF
Market capitalisation	$32m
Enterprise value	$36m
GICS sector	Construction and Engineering
12 month price range	$0.06 - $0.13
Average monthly t/o	2.3m
Shares in issue	287.4m
Top 20 holders	177.3m
Previous rating	Buy

Year ended June 30		FY23	FY24E	FY25E	FY26E
Revenue	$m	118.2	97.3	111.0	122.7
Growth	%	(2.6)	(17.6)	14.0	10.6
Normalised EBITDA	$m	4.4	8.4	10.2	12.4
Margin	%	3.7	8.6	9.2	10.1
NPAT	$m	(9.5)	3.8	7.7	10.4
EPS	¢ps	(0.1)	1.9	2.7	3.6
CFPS	¢ps	(1.7)	1.5	3.3	4.6
DPS	¢ps	0.0	0.0	0.0	0.0
Franking	%	0.0	0.0	0.0	0.0
Dividend Yield	%	0.0	0.0	0.0	0.0
PER	x	N/A	5.9	4.1	3.1
EV/Revenue	x	0.3	0.4	0.3	0.3
EV/Gross profit	x	1.1	1.1	0.9	0.8
EV/EBITDA	x	N/A	4.9	3.6	2.9
EV/EBIT	x	244.4	6.2	4.3	3.4
Fixed charge cover	x	0.2	5.0	10.6	52.8
Return on capital	%	0.4	29.7	859.0	44.8

Verbrec vs. ASX Small Industrials



Source: Factset, Veritas

Verbrec Limited is a mid-tier engineering, training and infrastructure services business executing work across Australia and the Pacific.

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Verbrec Limited

Share Price: $0.110 ps **Valuation: $0.21 ps**

Financial Performance (A$m)

Year ended June 30	**FY22**	**FY23**	**FY24E**	**FY25E**	**FY26E**
Revenue	**121.4**	**118.2**	**97.3**	**111.0**	**122.7**
Cost of Goods Sold	(86.0)	(87.8)	(63.8)	(72.1)	(78.5)
Normalised Gross Profit	**42.1**	**33.9**	**33.5**	**38.8**	**44.2**
Other income	0.6	0.5	0.1	0.2	0.2
Operating costs	(32.7)	(30.1)	(25.3)	(28.8)	(32.0)
Normalised EBITDA	**10.1**	**4.4**	**8.4**	**10.2**	**12.4**
Non-recurring and legacy items	(7.1)	(9.2)	(0.9)	0.0	0.0
Statutory EBITDA	**3.0**	**(4.8)**	**7.4**	**10.2**	**12.4**
Depreciation and amortisation	(4.9)	(4.2)	(2.5)	(1.7)	(1.8)
Normalised EBIT	**5.2**	**0.1**	**5.9**	**8.5**	**10.6**
Associate income	0.0	0.0	0.0	0.0	0.0
Net interest	(0.7)	(0.9)	(1.2)	(0.8)	(0.2)
Normalised Pre-tax Profit	**4.5**	**(0.8)**	**4.7**	**7.7**	**10.4**
Normalised tax	0.3	0.4	0.0	0.0	0.0
Profit attributable to minorities	0.0	0.0	0.0	0.0	0.0
Normalised profit to holders	**4.8**	**(0.3)**	**4.7**	**7.7**	**10.4**
One off items (post-tax)	(7.2)	(9.2)	(0.9)	0.0	0.0
Reported profit to holders	**(2.4)**	**(9.5)**	**3.8**	**7.7**	**10.4**

Cash Flow Statement (A$m)

Year ended June 30	**FY22**	**FY23**	**FY24E**	**FY25E**	**FY26E**
Statutory EBITDA	**3.0**	**(4.8)**	**7.4**	**10.2**	**12.4**
Cash net interest	(0.7)	(0.9)	(1.2)	(0.8)	(0.2)
Cash tax (paid)/received	0.3	0.4	0.2	0.0	0.0
Working capital/other	0.5	1.4	(2.5)	0.0	1.1
Operating Cash Flow	**3.1**	**(3.9)**	**3.9**	**9.4**	**13.3**
Capex	(1.0)	(0.8)	(0.6)	(0.8)	(0.9)
Free Cash Flow	**2.1**	**(4.7)**	**3.3**	**8.6**	**12.4**
Net Borrowings	(1.4)	6.0	0.2	(1.5)	(1.5)
Payments on Finance Leases	(2.7)	(2.8)	(2.8)	(2.7)	(2.5)
Equity raised/buybacks	0.1	0.0	4.0	0.0	0.0
Dividends paid	0.0	0.0	0.0	0.0	0.0
Asset disposal/other	(2.7)	(3.3)	(4.5)	(2.7)	(2.5)
Net increase/(decrease) cash	**(1.8)**	**(2.0)**	**2.9**	**4.4**	**8.4**
Cash at beginning	8.3	6.4	4.5	7.4	11.8
Cash at end	6.4	4.5	7.4	11.8	20.3

Balance Sheet (A$m)

Year ended June 30	**FY22**	**FY23**	**FY24E**	**FY25E**	**FY26E**
Cash to hand	6.4	1.6	4.5	8.9	17.3
Restricted cash	0.0	2.9	2.9	2.9	2.9
Receivables	18.6	17.1	16.9	21.9	23.5
Contract assets	6.9	5.8	3.5	3.5	3.5
Other current assets	0.1	0.3	0.3	0.3	0.3
Current Assets	**32.0**	**27.6**	**28.1**	**37.5**	**47.6**
Property, Plant & Equipment	1.5	1.5	1.3	1.7	2.2
Intangibles	14.6	12.6	10.4	10.2	10.0
Right-of-use assets	6.4	4.8	6.7	8.3	9.7
Deferred tax assets	7.5	7.6	7.8	7.8	7.8
Other non current assets	0.0	0.0	0.0	0.0	0.0
Non Current Assets	**30.1**	**26.4**	**26.2**	**28.0**	**29.6**
Total Assets	62.1	54.1	54.3	65.5	77.2
Payables	14.4	14.7	11.7	16.7	19.5
Borrowings	0.7	6.8	7.0	5.5	4.0
Lease Liabilities	7.7	6.1	6.9	6.9	6.9
Employee Benefits	6.4	5.5	5.0	5.0	5.0
Other liabilities	10.2	8.0	4.7	4.7	4.7
Total Liabilities	**39.5**	**41.0**	**35.3**	**38.8**	**40.0**
Shareholder Funds	**22.5**	**13.0**	**19.1**	**26.8**	**37.1**

Directors and Key Management Personnel		**Shares**	**Holding**
Brian O'Sullivan AM	Non Exec Director	69.4m	24.2%
Mark Read	CEO	0.1m	0.0%
Phillip Campbell	Chairperson and Non Exec Direct	0.7m	0.2%
Matthew Morgan	Non Exec Director	0.4m	0.2%
Sarah Zeljko	Non Exec Director	0.0m	0.0%

Major Shareholders (excluding nominees)	**Shares**	**Holding**
Brian O'Sullivan and Related Holdings	69.4m	24.2%
Thorney Holdings Pty Ltd	24.7m	8.6%
Candyblossom and Bloemhof Pty Ltd	21.8m	7.6%
GFNA Bartley Family Pty Ltd	17.9m	6.2%
Forager Funds Management Pty Ltd	14.3m	5.0%
Top 20 shareholders	**177.3m**	**61.7%**

Source: Company data, Veritas Research

Valuation Metrics

Price Target (ps)	$0.21	90%
Share Price (ps)	$0.110	
FY24 EV/EBITDA (x)	4.9	
Implied FY24 EV/EBITDA (x)	7.8	58%
Implied FY25 EV/EBITDA (x)	6.4	30%
Market Capitalisation (A$m)	32	
Enterprise Value (A$m)	36	

Valuation Multiples

Year ended June	**FY22**	**FY23**	**FY24E**	**FY25E**	**FY26E**
P/E (x)	5.2	N/A	5.9	4.1	3.1
Price/Cash Flow (x)	8.1	N/A	7.2	3.4	2.4
EV/Revenue (x)	0.3	0.3	0.4	0.3	0.3
EV/Gross profit (x)	0.9	1.1	1.1	0.9	0.8
EV/Normalised EBITDA (x)	3.6	8.3	4.4	3.6	2.9
EV/Statutory EBITDA (x)	12.2	N/A	4.9	3.6	2.9
EV/EBIT (x)	7.0	244.4	6.2	4.3	3.4
Equity FCF yield (%)	6.7	-14.9	10.4	27.3	39.4
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
EV/capital (x)	1.3	4.7	2.2	1.2	0.7
Price to book value (x)	1.1	1.9	1.5	1.2	0.9

Per Share Data

Year ended June 30	**FY22**	**FY23**	**FY24E**	**FY25E**	**FY26E**
EPS diluted - adjusted (¢ps)	**2.13**	**(0.14)**	**1.86**	**2.68**	**3.60**
EPS diluted (¢ps)	2.17	(0.15)	1.86	2.68	3.60
Cash flow per share (¢ps)	1.35	(1.74)	1.53	3.28	4.63
Free cash flow per share (¢ps)	0.93	(2.10)	1.29	3.00	4.33
Cash (¢ps)	2.84	0.69	1.76	3.10	6.04
Net assets (¢ps)	9.98	5.79	7.50	9.32	12.92
DPS (¢ps)	0.00	0.00	0.00	0.00	0.00
Franking (%)	0	0	0	0	0
Shares on issue - avg. basic (m)	221	221	254	287	287
Shares on issue - avg. diluted (m)	226	225	254	287	287

Segmental

Year ended June 30	**FY22**	**FY23**	**FY24E**	**FY25E**	**FY26E**
Work-in-hand (Start of Period)	76.6	77.4	66.0	65.0	75.0
Work-in-hand (% of Revenue)	*71.4*	*74.6*	*73.0*	*63.1*	*65.9*
Engineering Services	107.3	103.8	90.4	103.0	113.7
Training Services	14.1	14.4	7.0	8.0	9.0
Revenue ($m)	**121.4**	**118.2**	**97.3**	**111.0**	**122.7**
Engineering Services Growth	20.1	(3.3)	(12.9)	13.9	10.5
Training Services Growth	74.3	2.4	(51.6)	15.0	12.0
Revenue Growth (%)	**24.6**	**(2.6)**	**(17.6)**	**14.0**	**10.6**
Engineering Services Gross Profit	34.8	26.5	29.5	34.2	39.0
Training Services Gross Profit	7.3	7.5	4.1	4.6	5.2
Underlying Gross Profit ($m)	**42.1**	**33.9**	**33.5**	**38.8**	**44.2**
Engineering Services Margin	32.4	25.5	32.6	33.2	34.3
Training Services Margin	52.0	52.0	58.4	58.0	58.0
Underlying Gross Profit Margin (%)	**34.7**	**28.7**	**34.4**	**35.0**	**36.0**
Engineering Services EBITDA	12.6	4.4	7.5	8.8	10.5
Training Services EBITDA	(2.5)	(0.0)	0.9	1.4	1.8
Underlying EBITDA ($m)	**10.1**	**4.4**	**8.4**	**10.2**	**12.4**
Engineering Services Margin	11.7	4.2	8.3	8.6	9.3
Training Services Margin	(18.0)	(0.1)	12.7	17.1	20.4
Underlying EBITDA Margin (%)	**8.3**	**3.7**	**8.6**	**9.2**	**10.1**

Performance Ratios (%)

Year ended June 30	**FY22**	**FY23**	**FY24E**	**FY25E**	**FY26E**
Operating cost margin	26.9	25.5	26.0	26.0	26.1
Gross profit growth	23.8	(19.4)	1.2	15.8	13.7
Cost growth	17.4	(8.0)	15.9	14.0	11.0
Statutory EBITDA margin	2.5	-4.1	7.6	9.2	10.1
Statutory EBITDA growth	907.4	(261.3)	253.7	37.5	21.1
Normalised EPS growth	48.9	(106.8)	1,361.2	44.3	34.5
Tax rate	(6.6)	56.9	0.0	0.0	0.0
Return on capital	30.7	0.4	29.7	859.0	44.8

Balance Sheet Ratios

Balance Sheet (A$m)	**FY22**	**FY23**	**FY24E**	**FY25E**	**FY26E**
Gross debt ($ m)	0.7	6.8	7.0	5.5	4.0
Net debt/(cash) ($ m)	(5.7)	5.2	2.5	(3.5)	(13.4)
Fixed charge cover (x)	7.5	0.2	5.0	10.6	52.8
Net assets/(Assets - Right of use)	40%	26%	40%	47%	55%

RATING

BUY – anticipated stock return is greater than 10%
SELL – anticipated stock return is less than -10%
HOLD – anticipated stock return is between -10% and +10%
SPECULATIVE – high risk with stock price likely to fluctuate by 50% or more

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