paragon

H122 results

Building momentum in Q222

Automobiles and parts

paragon's Q222 results show an acceleration of revenue growth across the business and, while adjusted EBITDA was modestly lower, management has increased guidance. It now expects FY22 revenues of €170m while continuing to expect an EBITDA margin over 15%, with free cash flow (FCF) of €12m. While the equity value remains subordinate to financing bond redemption issues, we anticipate positive progress by the year end.

Year end	Revenue (€m)	PBT* (€m)	EPS* (€)	DPS (€)	P/E (x)	Yield (%)
12/20**	127.2	(6.0)	0.79	0.00	6.1	N/A
12/21**	146.9	1.2	0.27	0.00	17.7	N/A
12/22e	170.8	2.9	0.47	0.00	10.2	N/A
12/23e	188.1	7.4	1.19	0.00	4.0	N/A

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments. **Restated following the disposal of Voltabox, excluded from FY20 and FY21 as discontinued.

All businesses show revenue growth in H122

Despite lower global vehicle production, paragon continued to make positive progress with revenues growing 14% to €86.4m in H122 (H121: €75.7m). All four of the Electronics Division's strategic business units (SBUs) and the Mechanics division, which is comprised of the Kinematics SBU, grew revenues in H122. With China recovering following the most recent lockdowns in H122, global market conditions may improve in H222 as paragon initiates production against several important new long-term contracts, which already underpinned paragon's H222 revenues as well as the growth strategy. Absent the €3.1m of one-off charges seen in H122, the FY22 EBITDA margin progression to over 15% looks plausible as operational leverage improves.

Refinancing remains the key issue

The operational performance remains encouraging as management seeks to deliver against its FY26 targets for revenues of €250–300m with EBITDA margins of 20%. That should support progressive improvement in FCF. However, the clear immediate priority is to fund the bond repayments due over the next 12 months. The company has to address the refinancing of the outstanding CHF21.0m (€21.4m) maturity of the Swiss franc (CHF) bond due for redemption in 2023. Management expects to present information around possible solutions for the FY23 bond repayments to the market in the autumn.

Valuation: Equity rating dependent on refinancing

Assuming the bond issues can be resolved including the additional Eurobond early repayments, we would expect the equity valuation to start to reflect increased confidence in the execution of the growth strategy. If further debt reductions are subsequently achieved, we would expect the share price to trend towards potential cash valuations. Our capped DCF valuation has increased modestly to €19.8 per share (from €19.6), reflecting the better-than-expected progress so far in FY22.

30 August 2022

Price	**€4.78**
Market cap	**€22m**

Adjusted net debt (€m) at 30 June 2022 (excludes lease liabilities €12.6m)	91.1
Shares in issue	4.5m
Free float	50.7%
Code	PGN
Primary exchange	Frankfurt Xetra
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	19.7	(2.3)	(55.5)
Rel (local)	25.2	9.6	(45.3)
52-week high/low		€10.55	€3.65

Business description

Based in Delbrück, Germany, paragon designs and supplies automotive electronics and solutions, selling directly to OEMs, including sensors, interior, digital assistance, body kinematics and power. It has production facilities in Germany, Croatia and China.

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H122 results

paragon's automotive activities continued to perform strongly in H122, aided by the introduction of new products and the bias towards the premium end of the vehicle market. This was despite continued supply chain constraints in global car markets, exacerbated by the Russian invasion of Ukraine and some continued effect from pandemic lockdowns, which led to an overall decline in global car production in the first half of the year. All five SBUs grew revenues, contributing to the group increase of 14% to €86.4m, and while EBITDA was €3.3m lower this was largely due to €3.1m of non-recurring charges. Adding these back, the H122 EBITDA margin was 13.9%, which is aligned with management's FY22 guidance.

Exhibit 1: paragon H122 results summary

€m	H121	H122	% change
Electronics	*54.5*	*59.6*	*9.3%*
Body Kinematics	*21.2*	*26.8*	*26.4%*
Revenues	**75.7**	**86.4**	***14.1%***
Gross Profit	**43.0**	**50.2**	***16.6%***
Gross margin	*56.8%*	*58.1%*	*2.2%*
Electronics	*9.1*	*8.6*	*-5.6%*
Body Kinematics	*2.0*	*0.3*	*-82.9%*
Eliminations	*0.2*	*0.0*	
EBITDA	**11.2**	**8.9**	***-20.7%***
EBITDA margin	*14.8%*	*10.3%*	*-30.5%*
EBIT	**2.7**	**1.2**	***-55.1%***
PBT reported	(0.3)	(1.8)	*554.7%*
PBT adjusted*	**1.7**	**3.3**	***91.0%***
EPS (€) – reported	(0.12)	(0.60)	*421.4%*
EPS (€) – adjusted*	**0.22**	**0.24**	***12.4%***
FCF	**(0.7)**	**2.0**	***n.m.***
Adjusted net debt (excludes lease liabilities)	**(102.3)**	**(91.1)**	***-11.0%***
Lease liabilities	(12.1)	(12.6)	*4.5%*
Net financial liabilities (IFRS)	(114.4)	(103.7)	*-9.4%*

Source: paragon reports, *Edison Investment Research adjustments and estimates

The Electronics segment, which accounted for 69% of H122 group sales, grew revenues by 9.3% to €59.6m (FY21: €54.5m). In terms of the constituent SBU revenues, Sensors saw revenues grow by 4% primarily due to increasing demand for air quality sensors. Interior sales showed the strongest growth in the division, rising 14% due to strong demand for cockpit display instruments, while Digital Assistance grew 6.0%. The nascent Power SBU also developed positively.

The Mechanics division, which consists of the body Kinematics SBU, delivered the strongest revenue growth of 26.4% in H122 with revenues of €26.8m (H121: €21.2m). A relatively flat Q122 performance was followed by a strong improvement in Q222, where sales increased to €14.7m.

Exhibit 2: paragon H122 revenue development

€m	Q121	Q221	H121	Q122	Q222	H122	Q1 vs Q1	Q2 vs Q2	H1 vs H1
– Sensors	*12.59*	*11.45*	*24.04*	*12.59*	*12.47*	*25.06*	*0.0%*	*8.9%*	*4.2%*
– Interior	*12.66*	*12.45*	*25.11*	*13.95*	*14.56*	*28.51*	*10.2%*	*16.9%*	*13.6%*
– Digital Assistance	*2.30*	*3.03*	*5.33*	*2.67*	*2.98*	*5.65*	*16.0%*	*-1.6%*	*6.0%*
– GB Power	*0.00*	*0.03*	*0.03*	*0.36*	*0.02*	*0.38*		*-25.0%*	*1271.4%*
Electronics	**27.55**	**26.96**	**54.51**	**29.57**	**30.03**	**59.60**	**7.4%**	**11.4%**	**9.3%**
Mechanics	**11.66**	**9.53**	**21.19**	**12.11**	**14.68**	**26.79**	**3.9%**	**54.1%**	**26.4%**
Revenues	**39.21**	**36.49**	**75.69**	**41.68**	**44.71**	**86.39**	**6.3%**	**22.5%**	**14.1%**

Source: paragon reports

The divisional EBITDA contributions were both down on the prior year, although €3.1m of non-cash costs were charged across the two divisions, with Electronics contributing €8.6m (H121: €9.1m) and Mechanics €0.3m (FY21: €2.0m). The €3.1m of one-off non-cash charges is made up of book losses on the disposal of the Aachen site (€0.45m) and the former Voltabox production facility (€1.75m). The €0.9m balance was a non-cash exchange rate loss incurred on the CHF bond.

While the reported group H122 EBITDA margin fell to 10.3% compared to 14.8% in H121, adding back the one-off charges increases the H122 margin to 13.9%.

Adjusted net debt (excluding lease liabilities) fell by €10.2m to €91.1m, as the latest CHF8.75m (€8.6m) CHF bond partial repayment was completed in April, funded from a combination of improved operating cash flow, and asset disposals.

We expect management to discuss potential solutions to the funding of the 2023 bond repayments in the autumn. Alongside various alternative potential bonds, the possibility of a business disposal remains an option, but only at the right price.

Outlook

As we discussed in our recent note paragon appears well positioned to achieve its growth targets, with a very strong booked business backlog. As paragon is expected to increase its global market penetration and products are applicable across brands, models and fuel types, we expect it to continue to outperform the general market trend. In recent months, market forecasts for global vehicle production have continued to anticipate growth both for FY22 (following a weaker H122) and through FY23, although deteriorating macroeconomic conditions could dampen demand next year.

Earnings revisions

We have increased our revenue forecasts to reflect the latest guidance, with the improvement mainly coming from the Mechanics division.

We expect paragon to continue to grow group revenues by over 10% next year, with a further improvement in EBITDA margins.

Exhibit 3: paragon earnings revisions

Year to December (€m)	2022e			2023e		
	Prior	New	*% change*	Prior	New	*% change*
Electronics	121.7	120.6	*-0.9%*	135.1	133.9	*-0.9%*
Mechanics	44.2	50.2	*13.6%*	47.7	54.2	*13.6%*
Total group revenues	**165.9**	**170.8**	***3.0%***	**182.8**	**188.1**	***2.9%***
Electronics	21.9	21.7	*-0.9%*	25.7	25.4	*-0.9%*
Mechanics	3.1	4.0	*29.9%*	4.8	5.4	*13.6%*
HQ Other and intersegment	0.2	0.2	*0.0%*	0.2	0.2	*0.0%*
EBITDA (company reported)	**25.2**	**25.9**	***2.9%***	**30.6**	**31.0**	***1.4%***
Underlying PBT	**2.3**	**2.9**	***26.8%***	**6.9**	**7.4**	***7.2%***
EPS – underlying continuing (€)	**0.4**	**0.5**	***26.8%***	**1.1**	**1.2**	***7.2%***
DPS (€)	0.0	0.0		0.0	0.0	
Net cash/(debt), excluding leases	(91.9)	(89.0)	*-3.1%*	(89.9)	(83.8)	*-6.8%*

Source: Edison Investment Research estimates

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Exhibit 4: Financial summary

€m	2020	2021	2022e	2023e
Year end 31 December	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS				
Revenue	127.2	146.9	170.8	188.1
Cost of Sales	(69.2)	(72.6)	(80.3)	(86.5)
Gross Profit	58.0	74.4	90.5	101.6
EBITDA	13.8	20.0	25.9	31.0
Operating Profit (before amort. and except).	6.6	13.3	17.1	21.9
Intangible Amortisation	(6.0)	(6.0)	(6.4)	(7.5)
Exceptionals	(11.2)	(6.5)	(7.1)	(4.0)
Other	(37.1)	(5.9)	0.0	0.0
Operating Profit	(47.7)	(5.1)	3.6	10.4
Net Interest	(6.5)	(6.1)	(7.8)	(7.0)
Profit Before Tax (norm)	(6.0)	1.2	2.9	7.4
Profit Before Tax (FRS 3)	(54.2)	(11.3)	(4.2)	3.4
Tax	9.6	(0.2)	1.1	(0.9)
Profit After Tax (norm)	3.6	1.2	2.1	5.4
Profit After Tax (FRS 3)	(44.7)	(11.4)	(3.1)	2.4
Average Number of Shares Outstanding (m)	4.5	4.5	4.5	4.5
EPS - normalised (€)	0.79	0.27	0.47	1.19
EPS - normalised fully diluted (€)	0.79	0.27	0.47	1.19
EPS - (IFRS) (€)	(9.87)	(2.52)	(0.68)	0.54
Dividend per share (€)	0.00	0.00	0.00	0.00
Gross Margin (%)	45.6	50.6	53.0	54.0
EBITDA Margin (%)	10.8	13.6	15.2	16.5
Operating Margin (before GW and except.) (%)	5.2	9.1	10.0	11.6
BALANCE SHEET				
Fixed Assets	143.1	115.0	104.9	104.1
Intangible Assets	81.5	76.4	78.9	80.8
Tangible Assets	47.0	36.2	23.6	21.0
Right of use asset	13.1	1.8	1.8	1.8
Investments	1.5	0.6	0.6	0.6
Current Assets	57.4	44.7	47.2	48.3
Stocks	27.3	24.0	25.6	26.8
Debtors	11.6	10.9	11.1	11.1
Cash	5.7	1.5	1.5	1.5
Other	12.7	8.4	9.0	8.9
Current Liabilities	(90.6)	(125.5)	(37.5)	(40.7)
Creditors	(41.3)	(31.9)	(37.5)	(40.7)
Short term borrowings	(49.3)	(93.6)	0.0	0.0
Long Term Liabilities	(96.6)	(30.9)	(111.2)	(106.0)
Long term borrowings	(67.6)	(10.2)	(90.5)	(85.3)
Lease liabilities	(18.7)	(12.1)	(12.1)	(12.1)
Other long-term liabilities	(10.4)	(8.6)	(8.6)	(8.6)
Net Assets	13.2	3.3	3.3	5.8
CASH FLOW				
Operating Cash Flow	11.6	19.8	29.0	32.2
Net Interest	(6.5)	(6.1)	(7.8)	(7.0)
Tax	9.6	0.0	(0.8)	(2.0)
Capex	(7.7)	(17.5)	(17.1)	(17.9)
Acquisitions/disposals	0.0	8.4	0.0	0.0
Financing	1.9	6.5	10.0	0.0
Dividends	0.0	0.0	0.0	0.0
Net Cash Flow	8.9	11.1	13.3	5.2
Opening net debt/(cash)	117.4	111.2	102.3	89.0
HP finance leases initiated	0.0	0.0	0.0	0.0
Other	(2.7)	(2.2)	0.0	0.0
Closing net debt/(cash) (excluding leases)	111.2	102.3	89.0	83.8
Total financial liabilities	130.0	114.4	101.1	95.9

Source: company accounts, Edison Investment Research

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