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Momentum Group AB (MMGR.B.SE)

Q2 2023 Earnings Call

CORPORATE PARTICIPANTS

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Chief Financial Officer & Executive Vice President, Momentum Group AB

MANAGEMENT DISCUSSION SECTION

Ulf Christian Lilius

President & Chief Executive Officer, Momentum Group AB

Welcome to the presentation of Momentum Group's interim report for Q2 2023. I'm Ulf Lilius, CEO from Momentum Group. And I'm here with my colleague Niklas Enmark, Executive Vice President and CFO. And we will guide you through our report today.

Our agenda today is to give you some information about the highlights from Q2 and the development during the quarter as well as financial information. We will round off with our growth strategy note to the highlights in our report.

The business situation remained satisfactory for most of our operations during the second quarter of the year. The period was marked also continuing high inflation, component shortages within some areas. But where the picture is generally that the situation gradually now improving and continued stable customer demand despite clear signals in the outside world over the recession. The weak Swedish krona has had no major impact on earning, but is a factor that our companies have to deal with in their pricing.

Pleasingly, we have continued to strengthen the group with the number of interesting companies this year. During the first half of the year, we have completed five acquisition with a combined annual turnover of approximately SEK 415 million and an addition 40 talented employees whom we warmly welcome to the Momentum Group.

During the second quarter, we acquired the Danish Regal which strengthen our position in Denmark through their established market position in transmission and electrical automation. Through our largest acquisition to date, Askalon, we take an important position in industrial valves in Sweden, Denmark, Finland and Iceland. At the end of the quarter, we entered into the acquisition of Items which strengthen our offer with instrumentation for demanding operations.

The acquisitions are clear examples of the path taken for the group with the focus on the acquisition of strong companies with a clear quality and sustainability focus which strengthen our offer within profitable product verticals.

For the group, turnover increased during the quarter by 23% or [indiscernible] (02:13) 7% for comparable units and the EBITDA growth of 20%. Our profitability measure, EBITDA through working capital, remained at higher levels and that ensures our focus on keeping low and stable working capital within all our operations. After the second quarter of the year, our operating net debt is SEK 305 million compared with SEK 48 million last year where the change is explained by acquisitions and the dividend we paid during the quarter. Our cash flow,

together with cash and cash equivalents, including granted credit that we did not use in total SEK 704 million, provides security and guarantees a good financial position with room for action also going forward.

Even though the future market situation is difficult to assess, we must have a good starting point to be able to grow in both our business areas. We will do through further develop our operations through clear internal focus on three basic requirements: growth, profitability, and development based on active ownership and decentralized responsibility and, of course, development coworkers. Acquisition are also still part of our everyday life and we will add more fine companies to our group with whom we can further develop together with the entrepreneurs.

Now, I will hand over to Niklas who will guide you through our Q2 report.

Niklas Enmark

Chief Financial Officer & Executive Vice President, Momentum Group AB

Thank you, Ulf. During second quarter of the financial year, the group's revenue increased by 23% to SEK 549 million, where the growth for comparable units, adjusted for trading days and currency, was 7%. As Ulf mentioned, the business climate in our main markets in the Nordic region remained satisfactory, particularly in the industrial sector. The economic turbulence that characterized the market in the wake of inflation, interest rates, and the deterioration of certain sectors has not yet had any tangible impact on our customers' behavior. Component shortage in general showing signs of improvement although delivery times remain relatively low in certain product areas. Under the circumstances, the companies are maintaining a high delivery capacity. Purchase price and cost increases are continuing but at a more moderate rate than we have seen previously but we are still taking measures to compensate for this.

As regards pricing, the weak Swedish krona has had no major impact on sales to-date, but is a factor that operations was managed in their pricing decisions. During the quarter, we also had a strong contribution from acquisitions adding an additional SEK 77 million, corresponding to 17% revenue growth, not least from the acquisition of Askalon that we consolidate as of June. And that had a very good start in the group, also strong performance there from our new company in Denmark, Regal A/S that were consolidated during the quarter. The period included one less trading day versus last year.

Our EBITA in the group increased by 20% to SEK 65 million for the quarter, corresponding to an EBITA margin of 11.8% versus 12.1% the previous year, contributing to the profit growth were the increased revenue both organic and from acquisitions as well as strong and improving gross margins and a very strong EBITA growth in the business area components. The slight deterioration in EBITA margin for the group compared to last year during the quarter is related to lowered margins in the business area services that I will come back to.

Operating profit rose by 20% to SEK 59 million, corresponding to an operating margin of 10.7%. And operating profit was charged with amortization of intangibles, non-current assets of SEK 6 million arising in conjunction with acquisitions and with depreciation [ph] or right of (06:14) use assets and tangible non-current assets of SEK 17 million. No exchange rate translation effect impacted the operating profit. Profit after the financial items totaled SEK 55 million and profit after-tax amounted to [ph] SEK 43 million (06:32).

When we summarize the first half of the financial year, we can report that our revenue increased by 24% which 8% was attributed to comparable units. Adding to this revenue from acquisitions that added an additional 15% revenue growth. Our operating profit rose by 33% to SEK 140 million, corresponding to an operating margin of 10.8%. And our EBITA increased by 28% to SEK 125 million, corresponding to EBITA margin of 11.9%. Profit for the period increased by 31% to SEK 85 million, corresponding to an earnings per share of SEK 0.0175.

Commenting on the rolling 12 months numbers. For June 2023, we see that we are very close to SEK 2 billion in revenue, up 22% compared to one year ago and approximately SEK 400 million more than at the time of our listing in March of last year. This is, of course, thanks to the [indiscernible] (07:39) acquisitions that we have made during this period, but also the strong organic revenue growth during this period. Our EBITA is at SEK 231 million, increasing by 23% compared to the corresponding rolling 12-month period. Our EBITA margin has increased to 11.9%. Earnings per share on rolling 12 months was SEK 3.20, an increase by 33% compared to the corresponding rolling 12-month period. One reason for the larger increase in EPS being the share repurchases that we have made during the period.

And now to some comments per business area, and I will start with the components business area. Sales and earnings in the components business area were positive also during the second quarter. We'd say it's increasing by 29% to SEK 461 million, and EBITA increasing by 32% to SEK 66 million. Our EBITA margin increased to 14.3% compared to 14% the previous year. Revenue growth for comparable units was 10%. The business area's return on working capital measured as EBITA over working capital was 69%.

Momentum Industrial continued its strong performance during the quarter with a healthy rate of sales and volume and earnings growth. Growth was particularly favorable in the mining, paper, and automotive segments. The launch of the company's upgraded business system at the end of the preceding quarter has been successful. During the quarter, the recently acquired company, LocTech, was also integrated into Momentum Industrial's business.

The specialist companies generally performed well during the quarter with favorable demand and growth in sales and earnings. Some companies continued to experience delivery disruptions, although the general outlook is somewhat better. During the quarter, the acquisitions of Askalon and Regal was completed, both of which had a positive impact on the business area's earnings. Askalon noted very healthy demand from customers during the quarter, including customers in the nuclear power industry. After the end of the quarter, the acquisition of Processkontroll Items was completed.

Most of the companies in the business area services had a stable revenue trend during the quarter. However, revenue declined by 2% to SEK 91 million compared with the same quarter last year. And for comparable units, the revenue declined by 7%. This is due to the large units, Rörick and Mekano having certain delays for some larger deliveries and somewhat lower project sales which affected the business areas revenue for the quarter. However, the situation improves toward the end of the quarter with scheduled work at favorable capacity utilization ahead of the summer.

During the quarter, it was also announced that Carl A, with its operations in Helsingborg will emerge with Mekano's operations in the same city. The business areas operations in digitalized maintenance, Intertekna and Mytolerans, noted increased customer activity and an improvement in the month toward end of the quarter. EBITA amounted to SEK 7 million corresponding to an EBITA margin of 7.7%, down from 9.7% compared to one year ago. The business areas profitability measured as return on working capital increased however to 61%.

The group's profitability measured as return on working capital amounted to 60% for the reporting period, and that is measured over [indiscernible] (11:30) 12 months. The return on equity for the same period was 32%, an increase from 28%. Positive to note, this is [ph] showing (11:39) a cash flow for the period. Cash flow from operating activities before changes in working capital for the reporting period totaled SEK 123 million compared to SEK 66 million for comparable period. During the reporting period, inventories increased by SEK 60 million. Operating receivables and operating liabilities declined by SEK 90 million and SEK 40 million respectively. And

accordingly, cash flow from operating activities for the reporting period amounted to SEK 112 million, up from the SEK 46 million of the previous year.

Cash flow from investing activities for the reporting period amounted to SEK 289 million which includes acquisitions of SEK 284 million and net investments in non-current assets of SEK 5 million during the period. IFRS 16 effects from cash flow is in total zero of course but with a positive contribution to operations of SEK 31 million and corresponding negative effect on financing. At the end of the period, the group's operational net liability amounted to SEK 305 million compared with SEK 48 million at the beginning of the financial year. The difference is largely attributable to cash flow from operating activities of course, but also the acquisitions made during the reporting period as well as the dividend that we paid out during the quarter. Cash and cash equivalents including unutilized granted credit facilities totaled SEK 704 million, so we have ample room to grow with the acquisitions.

Ulf Christian Liljus

President & Chief Executive Officer, Momentum Group AB

Thank you, Niklas. Now, we'll give you some input about the growth strategy going forward. Looking at the acquisition candidates we normally approach, we want them to show a number of characteristics. They should have a strong and defensible position in the value chain with well-developed customer and supplier relationships with an ambition to further develop these into strong partnerships. As we focus on certain verticals, we look for companies that are market leaders or have the potential to become market leaders in these new verticals. We define a vertical in terms of several layers including, one, which type of business, is it off the market, OEM; two, place in the value chain; three, type of offers, spare parts, service installation; four, technology area, for example, hydraulics; and five, customer market application, for example, food and beverage, pulp and paper, etcetera.

Finally, we seek companies that are profitable and, through various activities, can become even more profitable or grow with existing level of profitability. The target company should be or have the potential to be at least 10% EBITA margin, meaning we should turn over working capital about 5 times to achieve a sufficient profitability EBITA through working capital.

We have proven processes and resources to work on acquisitions in three areas to evaluate and implement the acquisitions. We work with add-on acquisitions on a subsidiary level. Add-on acquisition is to strengthen the current offering or geographical expansion based on our capital allocation model or as we call it, our internal focus model which helps each company prioritize their goals and activities. The subsidiary's CEO is commercially responsible with support from the group if the company meets the profitability target.

The acquisition at business level with the focus in three areas: aftermarket, companies that can complement the operation within Momentum Industrial in Sweden, Norway and Finland; specialist, companies in leading specialist positions in the market niche in the Nordic region; technical service, companies with technical industrial service primarily in Sweden. Acquisition at group level are larger acquisitions where we support the companies and business areas with specific expertise in transactions, financial analysis, communication, and more.

Since our listing in March 2022, we have acquired 10 companies with a total annual turnover of around SEK 600 million. And they will be managed as independent niche companies, all in accordance with the philosophy of decentralized business responsibility.

Pleasingly, we have continued to strengthen the group with a number of interesting companies this year. During the first half of the year, we have completed five acquisitions with a combined annual turnover of approximately SEK 450 million and added 140 employees whom we warmly welcome to Momentum Group.

During the second quarter, we acquired the Danish Regal, which strengthen our position in Denmark through their established market position in transmission and electrical automation. Through our largest acquisition to date, Askalon, we take an important position in the industrial valves in Sweden, Denmark, Finland and Iceland. At the end of the quarter, we entered the acquisition of Items where we strengthened our offer with instrumentation for demanding operations.

The acquisitions are clear examples of the path taken for the group, with the focus on the acquisition of strong companies with clear quality and sustainability focus which strengthen our offer within profitable product verticals. A decentralized business model is a key where we develop each company individually based on its own merits, and as a group, build up competencies, several industry niches. Looking ahead, we have a strong platform and good businesses, which means we can work with a strong focus on our selected product and service verticals in our decision process.

Our focus is develop Momentum Group further in the next half year in 2023 by growing organically as well as by making carefully selected acquisitions. We continue on the set path of developing the group with leading position in various niches and we are at the same time well-prepared for additional downward to affect our operations. In order to be able to do so, we focus on our cash flow and the margin around double digits in order to maintain EBITA through working capital larger than 45% to finance our expansion. As I mentioned before, our operating net debt is SEK 305 million compared to SEK 48 million where the change is explained by acquisitions and the dividend we paid during the quarter. Our cash flow together with cash and cash equivalents including granted credit that we did not use, in total SEK 704 million provides security and guarantees good financial position and room for acquisition also going forward and to still have a reasonable net debt through EBITA.

We will continue to work in a structured way with our capital allocation through share buybacks when it's favorable for us as well as add-on acquisitions to strengthen the offering or geographical expansion based on our capital allocation model or internal focus model, which helps each company prioritize their goals and activities to focus on all in all with the aim to increase earnings per share.

Thank you for your time and interest listening to our Q2 presentation which are available with the report on our website. If you have any question or specific request, do not hesitate to contact us through our IR mail or by phone. Thank you very much and have a nice day.

QUESTION AND ANSWER SECTION

Ulf Christian Lilius

President & Chief Executive Officer, Momentum Group AB

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Welcome to the Q&A session of Momentum Group's Interim Report for Q2 2023. I'm Ulf Lilius, CEO for Momentum Group; and I'm here with my colleague, Niklas Enmark, Executive Vice President and CFO. And we will guide you through the Q&As.

So, the first question we have received, is the decentralized organization a benefit when onboarding acquired businesses given the pace that you have today?

I would say absolutely. One reason that we can maintain this pace in acquisition is that we have increased the number of people working with not only sourcing, but also deal processing and onboarding. Each acquisition is handled by a team comprising of a commercial responsible, [indiscernible] (19:42) each responsible for his group of companies together with financial people from the organization. As the process has run over several months and are bilateral, we can together with the seller plan for an efficient process. As we grow, we will continue to strengthen the organization. While there's still ample number of acquisition candidates in the sweet spot of the market, do you see that you will be forced to move to other areas? We don't see that the sweet spot is limiting factor today or is in the foreseeable future.

However, that said, we must always develop which means we are continuously evaluating business opportunities in new product verticals based on the trends we see in our society. One such interesting area is in the field of critical infrastructure where we have dipped our toes with the recent acquisition of Askalon but also with [ph] BPS (20:35). We would likely pursue that area a bit more going forward.

How is the M&A market right now? Our perception is that the market is quite active and that the competitive landscape is like before. The valuations have come down a bit which is logical given the high interest rates that everyone is experience. We also got a question if we have noticed a difference in demand at Momentum Industrial from the beginning of the quarter to the end. And if we can mention something which customer segment has been the weakest in the quarter. I would say that the situation has been quite stable during the whole quarter for Momentum Industrial. As we mentioned in the report, pulp and paper, automotive, and mining have all been good sectors during the quarter. Some sectors, steel, food, and beverage and other industry have been stable so not really in a segment that has been weak during the quarter.

Niklas Enmark

Chief Financial Officer & Executive Vice President, Momentum Group AB

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So, thank you, Ulf. I will continue with some questions and some answers. You have made 10 acquisitions in 2022 and 2023 altogether, adding about SEK 640 million in revenue. How much of this revenue is included in the rolling 12-month numbers and how much is then yet to be included? So of the acquired revenue, a bit more than SEK 400 million has thus far not been consolidated in our numbers, but are yet to be consolidated on.

The equity, the asset ratio has decreased quite significantly in the year, down to 32% compared to 44% one year ago. Can you explain the changes? So the greatest change has come this latest quarter, and the reason is really the increased pace in acquisitions together with the dividend payout after the Annual Meeting. Our total assets have increased by some SEK 500 million since the start of the year, combined with the fact that we have not seen the annualized effect in profits from the acquisitions made thus far.

Next question, what is the total consideration paid for the acquisitions this year? And so, as you can see from the report, the total consideration is about SEK 350 million with an effect on the net debt position in the group of about SEK 285 million.

And what is the leverage ratio measured as net debt to EBITDA after this quarter? So adjusting for IFRS 16 effects, the leverage ratio is about 1.3 times. But if we include the annualized effect from acquisitions, the ratio is, of course, lower. Thank you.

Ulf Christian Lilius

President & Chief Executive Officer, Momentum Group AB

Thank you for your time and interest listening to our Q&A presentation which also available with the report on our website. If you have any question or specific request, do not hesitate to contact us through our IR email or by phone. Thank you very much and have a nice day.

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