Premier Technical Services Group

Initiation of coverage

Head for heights

Industrial support services

Premier Technical Services Group (PTSG) has strong positions in its specialist services sectors, focused on safe building-operating environments. It has an outstanding organic- and acquisition-driven profit growth track record and a robust business model that drives efficiencies in operational performance. The share price has moved sideways for much of this year; the current rating anticipates healthy growth and we consider that a combination of existing organic momentum and M&A potential will be able to deliver this.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/16	39.2	7.5	7.6	1.4	23.7	0.8
12/17	52.9	10.2	9.7	1.6	18.6	0.9
12/18e	67.6	14.0	11.3	1.8	15.9	1.0
12/19e	74.3	15.6	12.0	1.9	15.0	1.1

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

Robust operational and acquisitive business model

PTSG's core markets are the provision of specialist services concerning safe operation largely in regulated building environments, particularly working at height, and the management of risk around fire, lightning and electrical installations and appliances. The efficient, national deployment of employed qualified field engineers using a proprietary integrated ERP system underpins the company's service offering, financial model and industry position. It also forms a robust template for assessing and acquiring complementary businesses, which have subsequently generated significant uplifts in their profitability under PTSG's ownership.

Significant progress made in H118

H118 saw another period of significant group progress for PTSG to record levels of revenue and profit. It included good organic growth and contributions from three FY17 acquisitions that are now fully integrated into the group. Strong momentum in Electrical Services and Fire Solutions comfortably carried temporarily quieter trading periods elsewhere to deliver 34% and 30% increases respectively in underlying PBT and EPS. A good underlying cash flow performance and a 13% increase in the interim dividend completed the H1 trading picture.

Valuation: Good growth and potential for more

PTSG's share price performed strongly in 2017 (rising 23%) but in 2018 to date has largely traded between 170p and 200p; it is now sitting towards the lower end of this range. The company has a strong earnings growth record and our model generates a three-year EPS CAGR to FY20 of 9.0%. This results in the current-year P/E of 15.9x becoming 14.3x in FY20, with EV/EBITDA moving from 12.8x to 9.8x. In our view, this anticipates faster growth and our analysis suggests our CAGR could double from reinvesting cash generated in acquisitions. By implication and subject to the right opportunities arising, the additional use of external debt and/or equity funding could accelerate growth further.

8 October 2018

Price	**180p**
Market cap	**£199m**

Net debt* (£m) at end June 2018 *Company definition	11.8
Shares in issue	110.5m
Free float	59%
Code	PTSG
Primary exchange	AIM
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(1.4)	(5.3)	0.6
Rel (local)	(0.5)	(3.2)	1.1
52-week high/low		210.0p	158.5p

Business description

Premier Technical Services Group is an independent provider of regulated and safety related specialist building services in four divisions across the UK. It listed on AIM in February 2015 at 52p.

Next events

H118 DPS to be paid	26 October 2018

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Premier Technical Services Group Group is a research client of Edison Investment Research Limited

Investment summary

Company description: Specialist building services

PTSG is an independent provider of regulated and safety-related specialist building services in four divisions effectively across the whole of Great Britain. Established in 2007 it has grown strongly through acquisitions and organic development. Its well-established business model, which generates excellent margins through operational efficiency, has continued to deliver good growth since the company's IPO in 2015.

Valuation: Good growth with potential for more

PTSG has clearly delivered strong growth in revenue and profitability in established market sectors subject to regulatory oversight and with good recurring income. We anticipate a three-year EPS CAGR (FY18 to FY20) of 9.0%; a PEG of 2.1x appears to be discounting faster growth. On our estimates, the current year P/E of 15.9x becomes 14.3x by FY20, while EV/EBITDA moves from 12.8x to 9.8x over the same period. Our analysis suggests PTSG could realistically double our forecast earnings growth by reinvesting annual net cash flow on acquisitions using typical multiples from the company's track record in this area. This would certainly align earnings growth with the current rating. Accessing additional debt or equity funding could potentially drive higher growth rates, subject to finding suitable target companies at the right price. The organic and acquisitive growth model has been very successful and we expect ongoing business investment to be prioritised although measured dividend growth is also likely. The prospective dividend yield is 1.0%, with earnings cover above 6x.

Financials: Rising profits, generating cash for reinvestment

PTSG's current annualised revenues and EBIT are approaching £70m and £15m respectively. In our model, underlying divisional revenue growth of 7–9% supplemented by acquisition effects (from relatively recently acquired companies) and a stable gross margin assumption drives modest incremental progress in group EBIT margin from FY18 to FY20. This is the foundation of the 9.0% EPS CAGR referred to above. Historically, PTSG has substantially reinvested the cash generated to support organic growth and has drawn on external funding sources to part-fund acquisitions. We expect to see higher underlying operating cash flows driven by EBITDA uplifts and more modest net working capital investment and, in the unlikely event that no more acquisitions are made, anticipate PTSG would be broadly funds neutral by the end of FY20.

Sensitivities: Process rigour required in service delivery

The demand for PTSG's services is substantially underpinned by regulatory compliance in the construction and ongoing usage of buildings and structures and the safety of people in those environments. The company's national field engineer workforce across four divisions is a significant competitive strength and, subject to continued alignment of training and experience with prevailing regulations, should be a driver of market share gain. Around half of revenue comes from testing and maintenance services, which have high levels of recurring business, while the other half relates to the more variable installation work. PTSG has a rigorous systems and training regime and appropriate levels of commercial risk management are required to minimise potential exposure to project liabilities. As a people and service-based business, effective use and retention of management and staff is a key business requirement; efficient engineer utilisation will continue to be heavily dependent on the company's proprietary IT system. Lastly, acquisition activity has paid an important part in the group's development to date and is likely to continue to do so, subject to suitable targets becoming available at the right price. All the usual risks apply in these cases.

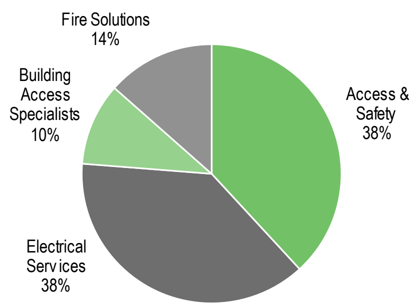
Company description: GB building services specialist

PTSG is an independent provider of specialist building services in Great Britain in safety-critical and regulated activities. These include façade and roof access, and electrical and fire protection services from a network of regional hubs using directly employed specialist staff across the UK. The business has grown rapidly through a combination of organic progress and acquisitions, which is also expected to characterise future business development.

Multi-disciplinary technical building services provider

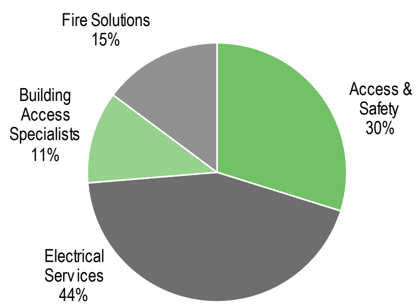
PTSG's services focus on providing safe building environments. It has 17 office locations including the Castleford head office from which it deploys **service engineers** (of which there are c 450) to client sites more or less **nationally** within a regional structure. Relatively local engineer resource reduces travel time and cost, theoretically increases the number of jobs that can be serviced (and revenue earned) and facilitates **high service levels and competitive pricing** to customers. The keys to generating attractive profitability are client density and high engineer utilisation levels. Trained engineers specialise by service (reported under four divisions, see below) and workflows are split into **installation** and **scheduled service/maintenance** streams, which contribute broadly equally to total revenue. The latter category is managed using **Clarity**, a proprietary integrated ERP software system that is used to schedule, monitor, certify and invoice jobs and provide a workflow audit trail. High annual client renewal rates (88%+ in test and maintenance in 2017) provide a good recurring income revenue base, increasingly under multi-year agreements. Following an expansion into the fire protection services segment, PTSG now reports under four divisions and their relative importance in terms of contribution to the group in FY17 is shown below.

Exhibit 1: FY17 revenue £52.9m



Source: Company

Exhibit 2: FY17 EBIT £10.6m



Source: Company

Access & Safety and Electrical Services have clearly been the largest revenue and profit generators to date; there are still some acquisition effects (from FY17 and FY18) to come through.

- **Access & Safety** – maintenance, inspection and testing of working safely at height solutions and design, installation and testing of permanent façade access and fall arrest equipment.
- **Electrical Services** – portable appliance and fixed wire testing and design, installation and testing of complete building lightning and surge protection systems.
- **Building Access Specialists** – high level building services including surveys, installation, maintenance, remedial works and cleaning.
- **Fire Solutions** – design, installation, testing, replacement, maintenance and certification of fire protection and suppression systems (including dry risers, sprinklers, alarms, emergency lighting and extinguishers).

Functional performance of products/systems (ie initial installation, ongoing use, maintenance) and workplace buildings are governed by legislation and regulations. Personnel concerned with these activities require an appropriate level of training, updated for relevant regulatory regime changes.

Established buy and build business model

PTSG has a well-established template visible in both its pre (2007–2014) and post (2015) IPO stages. Management's buy and build strategy, including 24 acquisitions since being founded, has created a business with the four specialist divisions shown above and annualised revenues of c £70m. Its operating model typically facilitates an improvement in the gross margin of acquired companies through greater efficiencies, adding service engineer resource, raising revenues and leveraging a controlled cost base. The benefits of group applied to newly acquired companies additionally include shared central services (eg HR, finance) and the potential to cross-sell multiple business lines. We understand that only c 5% of customers by number currently do so, which represents a good organic growth opportunity, in our view. With effectively national coverage, PTSG is also able to offer clients with multiple locations (eg retailers) a single, multi-discipline supplier package. The broad spread of service activities means in the short term the company is not overly reliant on any one revenue stream nor exposed to regulatory change. The latter effect is a positive long-term business driver, in our view.

Experienced management team, aligned shareholder interests

PTSG's founders chairman John Foley and CEO Paul Teasdale have each founded other specialist service businesses, MacLellan Group and TASS Europe respectively, and worked together when TASS acquired MacLellan in 2004. COO Roger Teasdale and CFO Mark Watford worked in the same divisional team at Smith & Nephew prior to joining PTSG towards the end of 2014, ahead of its IPO the following year. As well as obvious relevant experience in building companies in this space, the board has very strong finance oversight. We note that the directors mentioned above are significant PTSG shareholders and collectively account for c 40% of the share register.

Regulation as a key business driver

PTSG's services assist stakeholders in the ownership, management and operation of buildings to meet certain duty of care obligations to employees and members of the public. This primarily but not exclusively concerns working environments. General and specific requirements are contained in wide-ranging legislation, regulation and guidelines and apply to building construction, alterations and ongoing usage.

The company's 2015 IPO document (pages 21–22) listed the main regulations that generate demand for PTSG's building services; these are shown in Exhibit 3 together with the divisions to which they are most relevant. Clearly, there are overlaps between the five regulatory areas shown and others.

Exhibit 3: Primary regulatory framework for PTSG operations

	Access & Safety	Electrical Service	Building Access Solutions	Fire Solutions
Working at height regulations				
Construction design and management regulations				
Lightning protection regulations				
Regulatory reform (fire safety) order				
Portable appliance testing (PAT) regulations				

Source: Company, Edison Investment Research

Common requirements across these regulations include:

- Risk assessment – identification and evaluation of potential sources and outcomes of risk
- Action – taking practicable and reasonable steps to reduce risk, including test and maintenance
- Record – procedures for dealing with adverse events with appropriate training
- Review – regular repetition of the above steps

The responsibility lies with those who create or manage the building-related risks. In principle, failure to undertake these steps could result in action being taken by enforcement agencies (eg the Health & Safety Executive or local authorities, of which there are over 400 in Great Britain). In practice, the approach is understood to be ‘work with’ rather than ‘work against’ and greater focus is given to higher perceived risk facilities. However, if an adverse event occurs, failure to manage a building environment in keeping with the above requirements potentially exposes stakeholders to significant legal and financial liabilities and may invalidate commercial insurance cover. Hence, regulatory requirements and the consequences of non-compliance are key drivers of demand for PTSG’s services. Installation work (apart from retrofitting) is also driven by new building and construction activity, which is more cyclical than core test and maintenance revenue streams.

PTSG is able to assist at each of the four stages indicated above. It employs accredited engineers with the appropriate level of training and experience who are specifically qualified to install, test, maintain or repair systems (eg emergency lighting, fall arrest and fixed wire systems) and discrete products (eg access cradles, electrical appliances, extinguishers). These engineers are considered ‘competent persons’ who are able to certify their work. Through outsourcing, customers benefit from broad and up-to-date experience of PTSG’s engineers and are able to comply with regulatory requirements in a cost-effective manner.

Clarity IT system: Core driver of business performance

In each division, PTSG differentiates test and maintenance activities from installation work. The former workstream benefits from being a highly visible and typically recurring business. To schedule this effectively, PTSG uses its unique proprietary Clarity ERP system to deploy and manage its remote-working engineers. This enables the company to achieve high utilisation levels of its directly employed workforce who are contracted to 47.5 hours per week.

Workflow generator: renewal rates on this type of work have historically run in excess of 85%, creating a high-quality revenue stream, some of which is under multi-year contracts. Clarity’s database is a repository for previous work undertaken and is a CRM tool that generates prompts to re-engage with clients on their next inspection, assessment etc, at an appropriate frequency. Once agreed, the jobs are collated into a forward-looking programme of work.

Engineer management: PTSG has c 30 labour controllers (managing up to 18 engineers each) who then allocate jobs on a week-ahead basis to optimise the engineer schedule (most obviously through reducing travel time). This then becomes a real-time dashboard showing engineer location and movements. The engineers are linked to the dashboard through smart handheld devices with a live work app, which provide site support (eg traffic feeds, risk assessment protocols, lone worker alarms), and GPS tracking, which provides an audit trail of the work undertaken (including route and dwell time) as well as generating certification for this work prior to leaving site.

Finance and customer interface: Clarity is integrated with the company’s Sage accounting software. Once a job is signed off as complete, the system generates an invoice email for the customer who is also able to view this and other documentation (eg certificate of work, digital images) via a portal. This end-to-end functionality underpins PTSG’s service offering, competitive position (including pricing) and financial model, in our view.

Business penetration: the Clarity system is now on its third roll-out phase. It is operational in cradle maintenance and fall arrest systems (both in Access & Safety) and in Electrical Services is in being adopted in lightning protection, with electrical testing expected to be concluded by the year end. Fire Solutions is scheduled to follow in Q119. The proprietary nature of the software means PTSG is in a position to continue to update its software and capabilities. We show a graphical representation of the Clarity system on the following page.

Exhibit 4: PTSG test & maintenance workflow management using proprietary Clarity system

PTSG function	Clarity system	Notes

Sales	Database of work undertaken
	
	Central record for current work on hand
		• Generates test/maintenance reminders from previous workflow.
		• Confirmed orders logged
		    • Workflow detail (vs history/benchmark)
		    • Appointment confirmed

Site engineers	Work scheduling Workflow management > Engineer support > Tracking & recording > Work self-certification	• Collective and individual week-ahead diary schedule for engineers for best utilisation. • Device-based GPS tracking (inc. live traffic feed). • Engineer & site risk assessment protocol. • Tariff menu to support advisory repairs & maintenance flagged to client. • Repository for engineer notes (inc. job pictures). • Generation and issuance of certification on site on completion.
Finance	Interface with Sage accounting systems Customer portal	• Invoice generated from completed workflow log • emailed & available via customer portal • Accessible record of work undertaken, with specific job details and certification records.

Source: Edison Investment Research

Strong acquisition record: Genuine buy and build

PTSG's acquisition model is clearly focused on applying its efficient practices (on scheduling and utilisation) to improve revenue and gross margin contribution while using central services to control opex. We believe the company has clearly demonstrated an ability to both acquire complementary businesses on sensible initial multiples and deliver meaningful uplifts in profitability under PTSG's ownership.

Pre IPO: between formation in 2007 and 2014 the company made 12 acquisitions, substantially in the Access & Safety and Electrical Services divisions, although the largest and last at that point (Acescott) effectively established what is now the Building Access Solutions division. The combined pre-acquisition revenue and EBIT from these deals were £11.3m and £0.5m respectively, which rose to a reported £18m and £4m respectively in FY14, with some annualised Acescott benefit to come. The profit increase is particularly noticeable here and even after taking into account deferred consideration, the run rate multiples were still a lowly 0.5x revenue and 2.2x EBIT.

Post IPO: between 2015 and 2017 a further 11 acquisitions completed for an initial net cash cost of c £19m, equivalent to 0.6x revenue and 4.1x PBT both on a pre-acquisition basis. PTSG entered the Fire Solutions space for the first time (three deals in all). Brook Edgley (BEST; in lightning protection) in 2017 was the largest single deal and was accompanied by a placing, which raised £15m gross proceeds for the company.

Aggregating the pre-acquisition financials from both phases generates:

- Revenue of c £42m and c £5.1m EBIT (this assumes neutral interest effects for the 2015 to 2017 deals, ie EBIT equalled PBT overall).

Pro forma FY17 results (ie adjusting for full-year effects of acquisitions in that year) yields:

- Estimated annualised FY17 group revenue c £60m, EBIT c £12m.

So, in the first 10 years of the company's existence, it delivered organic growth in excess of 40% in revenue and more than doubled the profitability of the businesses acquired during this time.

We now look at the above pro forma financials in the context of the total acquisition payments that we have identified to date. (We are aware there is still some deferred consideration outstanding, notably BEST, but this will also be dependent on higher profitability so is unlikely to materially affect our analysis.) Adding all pre-IPO consideration, post-IPO initial net cash paid, c £9m deferred acquisition payments (comprising deferred consideration and deferred contingent consideration) and c £2.7m loan notes outstanding suggests:

- total consideration c £40m overall: equivalent to 0.67x revenue, 3.33x EBIT (FY17 annualised)

To us, this clear evidence the PTSG model, when applied to identified and acquired companies, is able to materially drive down initial acquisition multiples, which are low compared to its own rating, and generate good returns for shareholders.

Lastly, we note that PTSG has made one further acquisition in FY18 to date, **M&P Fire Protection** in July. PTSG initially paid £1m cash (for a business that generated £2.1m revenue and £0.2m PBT in its last financial year). Deferred consideration of up to £2.5m over the next five years is contingent on unspecified profit targets. This looks like a typical PTSG deal structure and adds complementary installation and maintenance revenue streams (in sprinkler and wet and dry riser systems) in the south east of England.

Sensitivities

Well-established and wide-ranging UK **legislation and regulations** govern the construction and ongoing use of buildings; their owners and managers in both public and private sectors have a duty of care to provide a safe environment for employees and members of public. The challenge and opportunity for service providers such as PTSG is keeping abreast of changing, increasingly onerous regulations (including maintaining certified and approved installer statuses) and continuing to serve clients cost effectively. We believe that better operators should take market share over time.

PTSG provides services across and within a number of different sectors providing **revenue diversity**. Having the capability to do so effectively on a national basis means there is also regional spread, albeit solely in the UK. Around half of revenue is generated from testing and maintenance services with high levels of recurring business that have good visibility. The other half relates to installation work, chiefly on new buildings, especially in the Access & Safety, Fire Solutions (which is also seeing good retro-fit demand currently) and, to a lesser extent, Electrical Services divisions. New building activity usually exhibits cyclicality and we expect associated project work to do the same. In any particular year, new installation work tends to be one off and subject to typical subcontracting risk. PTSG is required to have an **appropriate commercial risk management** framework (eg counter-party assessment, operational and financial controls and insurance, including professional indemnity cover) to ensure it is not unduly exposed to potentially material project liabilities.

Staff costs account for c 40–45% of revenues so an effective workforce is a central requirement for financial success. High levels of utilisation of c 450 qualified field **engineers** who are connected into other business systems characterises PTSG operationally. We understand that retention levels are high, which means the ongoing need to attract and retain additional engineers can be substantially to support business growth. At **board level**, the chairman and CEO are the two founding directors and both significant shareholders. Other directors and senior management are also shareholders and partly incentivised through share options. Since the IPO, PTSG's free float has increased from c 18% to c 59%, largely through new equity issued for acquisition funding. Periodic change in either the board composition and/or director share ownership will be closely watched by investors.

We believe that **Clarity, PTSG's proprietary IT system,** is a source of significant competitive differentiation bringing both internal management and client interface advantages. Consequently, business disruption effects could be material in a systems failure or downtime. PTSG is required to have suitable back-up capability and recovery plans to reduce the risks associated with such an occurrence. As the PTSG business develops, it is likely Clarity will itself need to evolve to facilitate growth.

As noted earlier, **acquisitions** have been a regular feature of PTSG's development during both its pre- and post-IPO phases. Since coming to the market, it has entered the fire protection market through acquisitions, creating a new division in the process, as well as building a regional footprint in its other three divisions. To date, its M&A track identification, execution and subsequent development track record appears strong without assuming historic legacy or contracting risks with these new businesses. It is clear that PTSG has grown the profitability of acquired companies; the absence of further deals would almost certainly reduce group growth rate potential in any particular year as well as the subsequent ones. Our estimates are based on the company as currently constituted, so acquisitions could enhance our forecasts. The challenge to management is to add companies where applying the PTSG business model can build post-deal profitability and, in the context of a larger group, for them to be of sufficient scale. Additional management oversight may be required to continue to control a larger number of operating companies effectively.

Valuation

Existing earnings growth expectations are reasonably good in our opinion, although we believe PTSG's valuation anticipates growth faster than we have modelled. This may well reflect a market anticipation of further complementary acquisition activity. As we have seen, the company's track record in this area is good; we believe the same is true of the appetite for further deals. Our estimates are based solely on the group as currently constituted and our analysis concludes that acquisitions can realistically make a meaningful contribution to further enhance growth. We believe that a DCF valuation is not directly applicable as the company heavily relies on acquisitive growth.

Valuing growth

Over the last six years (three as a private company and three since IPO), PTSG has clearly delivered strong growth in revenue and profitability with annualised FY17 EBIT of around £12m. It operates in established market sectors with regulatory demand drivers and good levels of recurring earnings. Including organic growth, some FY17 annualised effects and the M&P acquisition in mid-2018, our estimates for the group anticipate a three-year earnings CAGR to FY20 of 9.0%. Against a trailing P/E of 18.6x, the PEG of 2.1x is high by conventional standards. By FY20 the projected P/E multiple reduces to 14.7x, while the corresponding EV/EBITDA figure is 10.1x. We believe that the company will continue to seek to supplement its organic growth with acquisitions and, with a ROCE of 20%+ versus a WACC of c 8.5%, investors should expect management to prioritise investment in the business over distribution to shareholders, in our view. Nevertheless, PTSG has declared and increased dividends since coming to the market so some incremental growth to the FY17 payout (yielding 0.9%, covered more than 6x by earnings) is factored into our estimates.

Assessing the impact of acquisitions on earnings growth

We now provide illustrative acquisition activity and assess the potential impact on earnings growth over our forecast horizon. The primary assumptions used are:

- **Consideration** equal to our current net cash flow projections per year for 2017–20
- **Acquisition multiples**: from 3x to 7x PAT
- **Profit progression:** all relative to annual pre-acquisition earnings
  - Year 1 (year of acquisition) 50%; effectively assumes mid-year deal(s)
  - Year 2 +25%, Year 3 +50%, Year 4 +75% and Year 5 +100%

In other words, PTSG doubles acquired earnings in five years. (We also allow for a notional interest adjustment on cash consideration paid.) The resulting 2017–2020 EPS CAGRs are shown below:

Exhibit 5: Illustrative impact of acquisitions on 2017–2020 EPS CAGR

PAT multiple x	3.0	4.0	5.0	6.0	7.0
Group EPS CAGR	22%	19%	17%	16%	15%

Source: Edison Investment Research. Note: Our current model generates a group CAGR of 8.2%.

This analysis could be refined further (eg investing at a faster rate by recycling the additional cash generated, using additional debt or equity funding) and, for simplicity, we have assumed an all initial/no deferred structure here, but we believe this is a realistic and clearly fundable base case. We should add that our illustration would yield a doubling of profitability generated from these acquisitions by FY23 compared to FY20 as the improvement assumptions work through (especially on Year 3 deals).

We note that the 4x to 5x PAT input yields 2017–2020 EPS CAGRs around 18%; applied to the trailing P/E, this would generate a PEG nearer to 1x. Hence, these cases would appear to be a reasonable benchmark to both assess current market expectations and by which to judge actual acquisition activity if/when announced.

H118 results overview

The first half of 2018 saw another period of significant group progress for PTSG to record levels of revenue and profit. It included good organic growth and contributions from three FY17 acquisitions that are now fully integrated into the group. This successful business model also demonstrated the benefit of diversity, overcoming short-term variations in individual sub-sector activity levels. A good underlying cash flow performance and a 13% increase in the interim dividend completed the H1 trading picture.

Exhibit 6: PTSG interim and divisional splits

£m	H117	H217	2017	H118	% chg y-o-y	% chg y-o-y
					H118 actual	H118 LFL
Group revenue	**21.9**	**31.0**	**52.9**	**30.2**	**38**	**14**
Access & Safety	9.1	11.1	**20.2**	7.9	-13	-13
Electrical Services	7.4	12.8	**20.2**	13.4	82	16
Building Access Specialists	3.0	2.5	**5.4**	2.7	-9	-9
Fire Solutions	2.5	4.6	**7.1**	6.2	147	77
Group operating profit*	**4.4**	**6.3**	**10.6**	**5.9**	**35**	**11**
Access & Safety	1.5	1.7	**3.2**	1.3	-14	-14
Electrical Services*	1.7	3.0	**4.7**	2.8	66	19
Building Access Specialists	0.7	0.6	**1.2**	0.6	-10	-10
Fire Solutions*	0.6	1.0	**1.6**	1.3	121	76
Group	0.0	0.0	**0.0**	-0.1		

Source: Company. Note: *H118 LFL operating profit figures are Edison Investment Research estimates.

Access & Safety: maintenance, inspection and testing of working safely at height solutions and design, installation and testing of permanent façade access and fall arrest equipment.

There were no acquisitions in this division in the prior year so the headline performance is entirely organic. Revenue declined 13% due to the absence of large cradle installation contracts of which there were three, all in London, in the prior half year. Maintenance-related revenues actually grew by 12% in the period although this is obviously masked by the headline revenue movement. While these performance variations would have improved the gross margin mix of the division, lower revenues on a substantially unchanged overhead base effectively offset this benefit leaving the overall EBIT margin very slightly lower at 15.9%.

Electrical Services: portable appliance and fixed wire testing and design, installation and testing of complete building lightning and surge protection systems.

The acquisition of BEST in July 2017 was PTSG's largest deal to date, with £14m initial cash consideration paid. BEST mainly operates in the lightning protection sub-sector and we estimate that it contributed a maiden c £5m revenue and c £1m EBIT compared to H117, suggesting top-line organic growth for this division of c 14%. This based on commentary that states organic growth in lightning systems test and inspection (+31%) and electrical testing (+20%) were both ahead of the overall organic growth rate. Consequently, the contributions from these higher gross margin revenue streams should have benefitted underlying divisional margin development. Our estimates suggest that BEST's EBIT margin diluted the overall divisional margin (which was down 190bp to 21.2% in the first half), most likely due to additional post-acquisition marketing costs. Initial impressions are favourable here, with both a step up in renewal rates (from 50% to 85%) and 600+ new multi-year contracts signed.

Business Access Specialists: high-level building services including surveys, installation, maintenance, remedial works and cleaning.

As in Access & Safety, the trading performance shown in Exhibit 6 above is entirely organic from an unchanged divisional composition. Although revenue declined in H118, this may have been partly due to a reorienting of the business towards more specialist, and implicitly higher margin, services.

It is perhaps in a phase of building these activities through greater focus and this has yet to compensate for reduced revenues elsewhere. As acknowledged earlier, engineer utilisation is a central to profitability. The H118 results presentation did reference some strong contract win activity during the period (in steeple-jacking and abseil equipment installation); this was not quantified, but we would expect it to feed into an improving top-line profile as the year progresses.

Fire Solutions: design, installation, testing, replacement, maintenance and certification of fire protection and suppression systems (including dry risers, sprinklers, alarms, emergency lighting and extinguishers).

Although the acquisition of UK Sprinklers in September 2017 was relatively small (initial cash consideration of £1.3m), its subsequent growth is having a material impact on divisional progress. Compared to pre-acquisition levels, the run rate of revenue has doubled while that for profitability has more than trebled (and we estimate contributions of c £3.2m and c £0.6m respectively in H118). This y-o-y uplift fed into the 77% organic revenue progress of the division and we estimate a similar uplift at the EBIT level. This is currently the fastest-growing part of the group as momentum from 2016 acquisitions (especially UK Dry Risers Maintenance) continues to be strong. The outlook for UK Sprinklers appears to be excellent with an order book three times above pre-acquisition revenues suggesting a rising book to bill ratio and a further £50m of live order quotes. Bearing in mind this company reported annual revenue of c £3.5m at the point of acquisition, the scale of interest in its services is exceptional. Note that M&P Fire Protection was acquired after the period end, so did not contribute to the H118 trading result but will do so in future.

Positive signs of improving working capital performance

The company's reported end June net debt position (excluding finance leases) was £11.8m. Adjusted for a £4.2m temporary cash benefit at the period end (a tax payment receipt from the COO on share-based payment awards, which has since been forwarded to HMRC), underlying net debt was £16m. This is c £2.3m below the start year level.

Underlying operating cash inflow[1] (excluding the above tax receipt) was c £7m in H118 versus c £3m in H117. As well as a £1.8m EBITDA uplift, the modest positive working capital movement was particularly noteworthy as it included a reported £0.3m debtor inflow. So, in comparison to a £3.5m outflow in H117 and in the context of good organic revenue growth and a historically high debtor day position, this is a welcome achievement.

The y-o-y operating cash flow delta was sustained at the free cash flow level with no material talking points on the intervening lines. Below this, acquisition-related spend in the period (including deferred, contingent deferred and integration costs) was £3.4m. As in previous years, there was no cash dividend payment in the first half because PTSG pays the prior-year final and the in-year interim in the second half of the year.

Cash outlook: the temporary tax receipt held at the end of June has already been forwarded to HMRC, so this will optically distort H2 cash flows but on an annual view the effect is clearly neutral. Putting this to one side, we have factored in a c £1m initial consideration payment for M&P, c £0.5m for other acquisition-related cash flows and £1.9m for the first Integral Cradles loan note tranche to be repaid (although some or all of this could be in shares) as well as the declared dividend payout. We think H2 underlying free cash flow will modestly exceed these items in aggregate, leaving the year-end net debt position c £1m below the £16m 'true position' noted above at the interim stage. Otherwise, we will continue to monitor workings capital performance to identify if structural progress is being achieved in this area.

[1]Our underlying operating cash flow is defined as cash EBITDA (ie excluding non-cash items) adjusted for working capital movements. The company also includes capex in its definition.

Financials

PTSG made its first acquisition in 2007 and, with a further 23 so far plus organic growth, has lifted annualised revenue and EBIT to approaching £70m and £15m respectively for the business as currently constituted. Our estimates include annualised effects of the three acquisitions made in 2017 and one in 2018 but otherwise make now allowances for further deals. We fully expect further deals to feature and any such activity will be reflected in forecasts as announced.

Top-line growth and gross margin stability drive estimates

Revenue: excluding acquisition effects, our underlying annual divisional growth expectations are in the 7–9% range – arising from economic growth, increasing regulation and market share gains – beyond the current year, where we have factored c 12% growth based on prior year momentum. Divisionally, acquisitions made in Fire Protection in 2017 and 2018 support higher growth expectations.

Gross margin: the divisional and group mix is affected by the relative proportions of installation and maintenance work. The former typically includes third-party product costs with a dilutive margin impact. This work was evenly balanced in FY17. We assume a flat gross margin at FY17 levels in our model.

EBIT margin: three of PTSG's four divisions generated EBIT margins over 20% in FY17 while Access & Safety's FY17 EBIT margin was still a very respectable 15.8%. We have assumed modest incremental progress in group EBIT margins over our forecast period, primarily due to factoring in improvement in the fast-growing Fire Solutions. We note that asset disposal profits arising on fleet renewal activities have featured regularly in reported results. We do not explicitly forecast future profit streams from this source but assume any expectation of such is factored into management's overall financial guidance to the market.

After allowing for higher bank and finance costs in FY18 (declining thereafter) and a group tax charge of 13% in FY18 rising to 18% thereafter, the above assumptions generate EPS and DPS CAGRs of 9.0% and 7.7% respectively over our forecast horizon.

Cash flow reinvested, improving generation profile modelled

PTSG ended FY17 with £18.4m company defined net debt (cash net of bank debt, excluding finance leases of £1.1m and non-interest bearing deferred consideration notes of £2.7m).

In the three-year post IPO period (FY15 to FY17), aggregate cash flows have been as follows:

- £27m EBITDA
- £18m working capital investment
- £3m non-recurring costs (eg reorganisation, rebranding, IPO, acquisition integration)

  = c £6m operating cash flow
- Interest and tax together just over £3m
- Net capex just over £1m (gross approaching £3m before asset disposal proceeds)

  = c £1m free cash flow

Cash profits generated have been substantially reinvested for organic business growth. Also, discretionary cash flow has been invested in acquisitions and paid out to shareholders, as follows:

- Acquisitions £28m (including deferred and contingent consideration payments)
- Dividends just over £3m

  = net £30m outflow (before financing)

Acquisition activity has been part funded by new equity funding of almost £20m (including £4.7m net at IPO and c £14m net placing proceeds in FY17).

Looking forward, our model includes a more positive underlying operating cash flow performance (of c £14m in the current year, rising to c £18m by FY20) driven by EBITDA uplifts and more modest net working capital investment, particularly trade debtors. Below this, higher profitability feeds through into higher cash tax payments and we have factored in net interest at or above FY17 levels (higher in FY18, reducing modestly thereafter) and gross capex in line with depreciation (lower on a net basis after recurring disposal activities related to the management of field engineers' vehicle fleet). Even after allowing for the M&P initial consideration, loan note repayment and some dividend growth, our projections indicate that PTSG will have attained a broadly funds neutral balance sheet position by the end of FY20, absent any further acquisitions.

Balance sheet reflects acquisition activity and debtor book

Given PTSG's acquisition track record, it is unsurprising that there was a significant c **£26m of intangible assets** on the company's balance sheet at the end of H118, the majority of which was goodwill. **Net book value of tangible fixed assets** accounted for a **further £5.1m** and around half of this related to motor vehicles. (Approximately one third of the fleet is renewed each year and – assuming that the number of office locations is going to be relatively stable – vehicles acquired under financing arrangements will represent the primary capex item.) These two items together were almost exactly matched by gross debt, finance leases and deferred consideration notes, suggesting a **funding for long-term investment strategy**. For the record, PTSG has a £12m revolving credit facility in place (to September 2020) and an £8m annual overdraft facility (net of cash on hand).

Group net assets were **£34.9m** (or 32p per share) at the end of H118 and, by definition, this was substantially equivalent to the remaining asset base (including £0.9m non-current deferred tax) net of current operating liabilities. By far the most significant items related to **trade receivables c £19m** (work carried out and invoiced) and **accrued income c £10m** (contracts in progress, yet to be invoiced). In the context of annualised revenues of c £70m, this represents over 100 debtor days. Note the receivables figure is net of bad debt provisions which stood at £1m at the end of FY17 (and some £0.3m of this related to Carillion outstanding amounts, which we assume is unrecoverable now). A small number of larger (installation) contracts may straddle the year end but they are typically less than a year long, so in our view scope to accumulate bad large contracts and significant adverse profit hits is limited. That said, there is a clear onus on close financial management of the debtor book and we believe a reduction in the number of days is desirable. Cash on hand at the end of H118 was £13.9m and in isolation, the **remaining individual line items were relatively small.** They included modest inventory (£1.3m, largely consumable items), trade payables (c £3.3m, see inventory and installation project equipment) and other payables (c £4.7m, largely operating costs including staff), and modest other items. Both cash on hand and payables were temporarily inflated by a one-off HMRC tax receipt and pending payment – as mentioned in the earlier H118 results commentary – with a neutral overall balance sheet effect. It is important to note that PTSG has no exposure to defined benefit pension schemes.

Group development including in-year acquisitions makes it difficult to calculate an accurate ROCE figure. The main FY17 acquisition (BEST) was acquired in July with two smaller ones in January and September. Taking a simple average of the end FY16 and FY17 data as an illustration, we estimate that average capital employed in 2017 was c £48m. Compared to the reported FY17 operating profit of £10.6m, this represents ROACE in excess of 20%.

Exhibit 7: Financial summary

£m	2011	2012	2013	2014	2015	2016	2017	2018e	2019e	2020e
December	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS										
Revenue	9.0	12.1	13.9	18.0	25.8	39.2	52.9	67.6	74.3	79.4
Cost of Sales	(3.7)	(4.9)	(5.5)	(7.7)	(11.8)	(18.9)	(25.9)	(33.0)	(36.3)	(38.8)
Gross Profit	5.3	7.1	8.4	10.3	14.0	20.3	27.1	34.6	38.0	40.6
EBITDA	2.0	3.3	3.8	4.7	6.2	9.0	12.3	16.9	18.7	20.2
Operating Profit (before GW and except.)	1.6	2.9	3.2	4.0	5.3	7.9	10.6	14.6	16.2	17.5
Intangible Amortisation	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Exceptionals	(0.9)	(0.1)	(0.5)	(2.5)	(4.2)	(4.8)	(8.4)	(7.8)	(1.7)	(1.6)
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Operating Profit	0.7	2.8	2.6	1.5	1.1	3.0	2.3	6.8	14.6	15.9
Net Interest	(0.0)	(0.0)	(0.1)	(0.3)	(0.3)	(0.4)	(0.5)	(0.7)	(0.6)	(0.5)
Profit Before Tax (norm)	1.6	2.8	3.0	3.7	5.0	7.5	10.2	14.0	15.6	17.0
Profit Before Tax (FRS 3)	0.7	2.8	2.5	1.2	0.8	2.6	1.8	6.2	14.0	15.4
Tax	(0.1)	(0.6)	(0.6)	(0.6)	(0.3)	(0.3)	(0.5)	(1.6)	(2.3)	(3.1)
Profit After Tax (norm)	1.3	2.2	2.4	2.9	4.2	6.7	9.4	12.1	13.3	13.9
Profit After Tax (FRS 3)	0.5	2.2	1.9	0.5	0.5	2.3	1.3	4.5	11.6	12.3
Average Number of Shares Outstanding (m)				77.1	85.9	88.1	96.8	107.5	110.5	110.5
EPS - normalised (p)				3.77	4.87	7.63	9.73	11.29	12.03	12.62
EPS - FRS 3 (p)				0.69	0.57	2.61	1.37	4.19	10.53	11.15
Dividend per share (p)				0	1.00	1.40	1.60	1.80	1.90	2.00
Gross Margin (%)	58.9	59.2	60.5	57.3	54.3	51.9	51.2	51.2	51.2	51.2
EBITDA Margin (%)	22.3	27.2	27.1	26.2	24.0	23.0	23.3	25.0	25.1	25.4
Operating Margin (before GW and except.) (%)	18.1	23.6	22.8	22.3	20.5	20.0	20.1	21.6	21.9	22.0
BALANCE SHEET										
Fixed Assets	2.5	3.4	4.6	5.0	13.9	16.0	32.1	33.6	33.0	32.4
Intangible Assets	1.8	2.4	3.5	3.6	10.7	12.4	26.2	26.3	25.7	25.0
Tangible Assets	0.6	0.9	1.1	1.3	2.4	3.2	4.3	6.4	6.4	6.4
Investments	0.1	0.0	0.0	0.0	0.8	0.4	1.6	0.9	0.9	0.9
Current Assets	2.5	4.3	5.9	8.3	13.5	27.4	40.8	42.8	44.5	55.6
Stocks	0.1	0.1	0.1	0.2	0.4	0.5	1.2	1.6	1.7	1.8
Debtors	2.4	3.6	5.4	8.1	13.1	20.3	32.5	34.2	37.4	39.8
Cash	0.1	0.6	0.4	0.0	0.0	6.5	7.0	7.0	5.4	14.0
Current Liabilities	(2.2)	(3.3)	(4.8)	(8.5)	(9.3)	(17.9)	(24.7)	(24.0)	(15.5)	(16.6)
Creditors	(2.0)	(3.1)	(3.2)	(5.7)	(8.3)	(8.6)	(11.2)	(13.3)	(14.8)	(15.9)
Short term borrowings	(0.2)	(0.3)	(1.6)	(2.7)	(1.0)	(9.4)	(13.5)	(10.7)	(0.7)	(0.7)
Long Term Liabilities	(0.1)	(0.3)	(4.6)	(3.6)	(9.2)	(13.4)	(15.7)	(13.9)	(13.9)	(13.1)
Long term borrowings	(0.1)	(0.3)	(4.1)	(3.1)	(6.6)	(10.8)	(13.1)	(13.1)	(13.1)	(13.1)
Other long term liabilities	0.0	0.0	(0.5)	(0.5)	(2.5)	(2.6)	(2.7)	(0.8)	(0.8)	(0.0)
Net Assets	2.7	4.1	1.2	1.1	8.9	12.0	32.4	38.5	48.1	58.3
CASH FLOW										
Operating Cash Flow	2.0	2.4	1.8	2.6	(0.5)	0.6	(0.8)	11.7	14.5	16.4
Net Interest	(0.0)	(0.0)	(0.1)	(0.3)	(0.3)	(0.4)	(0.5)	(0.7)	(0.6)	(0.5)
Tax	(0.3)	(0.2)	(0.9)	(0.6)	(0.5)	(0.8)	(0.8)	(0.8)	(1.6)	(2.3)
Capex	(0.5)	(0.2)	(0.1)	(0.2)	(0.1)	(0.4)	(0.7)	(1.1)	(1.8)	(2.0)
Acquisitions/disposals	(0.1)	(0.3)	(0.8)	(0.7)	(3.3)	(2.7)	(16.1)	(3.2)	0.0	(0.8)
Financing	0.0	0.0	(4.0)	0.0	4.7	0.2	15.8	0.0	0.0	0.0
Dividends	(0.8)	(0.7)	(0.8)	(0.8)	(0.5)	(1.1)	(1.5)	(1.9)	(2.0)	(2.2)
Net Cash Flow	0.4	0.9	(4.9)	0.1	(0.6)	(4.7)	(4.6)	4.0	8.4	8.6
Opening net debt/(cash)	0.6	0.3	(0.1)	5.3	5.8	7.6	13.6	19.5	16.8	8.4
HP finance leases initiated	(0.0)	(0.3)	(0.4)	(0.5)	(0.6)	(1.0)	(1.0)	(0.7)	0.0	0.0
Other	0.0	(0.2)	(0.1)	(0.1)	(0.5)	(0.2)	(0.4)	(0.6)	0.0	0.0
Closing net debt/(cash)	0.3	(0.1)	5.3	5.8	7.6	13.6	19.5	16.8	8.4	(0.2)
Closing net debt/(cash) - company definition*	(0.1)	(0.6)	4.6	5.0	6.3	12.1	18.4	15.0	6.6	(2.0)

Source: Company, Edison Investment Research. Note: PTSG was listed on AIM in February 2015; FY15 (and the FY14 comparative) were fully reported in April of that year and the prior year information shown above was taken from the company's IPO document. Company-defined net debt differs from the other net debt line shown as it excludes finance leases. Neither definition includes outstanding loan notes (Integral Cradles deferred consideration), which are non-interest bearing but are expected to flow out as cash in FY18 £1.9m and FY20 £0.8m (included in acquisitions/disposals).

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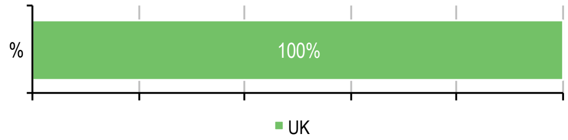
Revenue by geography



Management team

CEO: Paul Teasdale

Co-founder. Previously founded TASS Europe Ltd in 1999 to 2004 (when it was acquired by MacLellan Group) and continued as its post-acquisition Managing Director until 2006. This business was in similar sectors to those served by PTSG.

CFO: Mark Watford

Appointed September 2014, prior to IPO. Previously a vice president of finance at Smith & Nephew and a member of the global management team of its advanced wound management division.

Chairman: John Foley

Co-founder. Previously CEO of MacLellan Group, a facilities service company from 1994 to 2006, when it was acquired by Interserve. Qualified Chartered Accountant and barrister.

Managing Director: Roger Teasdale

Appointed November 2014, prior to IPO. Previously at Smith & Nephew for 25 years in a number of senior roles and latterly as president of the advanced wound management division. Qualified Chartered Accountant

Principal shareholders	(%)
Paul Teasdale	17.8
John Foley	16.9
First Pacific Advisors	15.3
Hawk Investment Holdings	11.0
Roger Teasdale	5.7
Didner & Gerge Fonder	4.3
Blackrock	4.2

Companies named in this report

N/A