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## McMillan Shakespeare Ltd (MMS)

More lovely and more temperate

**Recommendation**

**Buy** (unchanged)

**Price**

**\$17.63**

**Target (12 months)**

**\$21.00** (previously \$22.20)

**Sector**

Diversified Financials

**Expected Return**

Capital growth	<b>19.1%</b>
Dividend yield	<b>8.5%</b>
Total expected return	<b>27.6%</b>

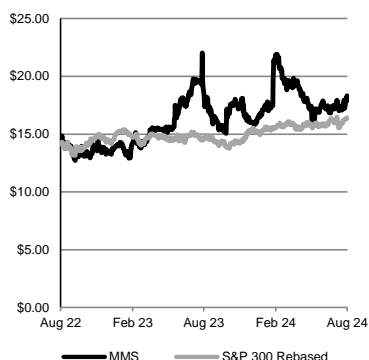
**Company Data & Ratios**

Enterprise value	<b>\$1,656.7m</b>
Market cap	<b>\$1,227.8m</b>
Issued capital	<b>69.6m</b>
Free float	<b>~71%</b>
Avg. daily val. (52wk)	<b>\$4,393,054</b>
12 month price range	<b>\$14.96-\$22.10</b>

**Price Performance**

	(1m)	(3m)	(12m)
Price (A\$)	17.39	17.20	22.03
Absolute (%)	3.0	4.2	-18.7
Rel market (%)	1.7	1.5	-31.3

**Absolute Price**



SOURCE: IRESS

**FY24 result: 4% EPSA beat with good cash generation**

MMS released a very strong result, with FY24 Normalised Revenue/EBITDA/UNPATA growth of +12%/+35%/+38% vs pcp, respectively from continuing operations, lapping on weaker new car supply and delivery. Core EPSA of 154.5¢ps came in +2% above BPe (+4% vs VA cons). Divisionally, GRS delivered a beat at EBITDA, headlined by a 12-month contribution from EV demand and productivity benefits, while PPS missed expectations. AMS was in-line. Net cash (excl. fleet and warehouse debt) improved to \$86.7m with cashflow conversion of 136%. MMS announced a better-than-expected final dividend of 78.0¢ps ff (BPe 75.9¢ps). Other highlights include:

**Discovering new markets:** MMS has soft launched a new brand 'Oly'; designed as a simple and digitised novated leasing solution for small and medium sized businesses. MMS expects to complete rollout during FY25. We forecast higher margin contribution, driven by the favourable yield impact through higher priced EVs and lower refinancing.

**Simply Stronger Program:** MMS expects to finalise strategic initiatives and provided capex guidance of ~\$11m for FY25 (incl. Oly), targeting a seamless client experience with self-service capability. We forecast a step-up for D&A in FY26 upon completion.

**SA Government:** The contract has been transitioned effective 1 July. MMS reiterated that the value represents ~7% of FY23 normalised GRS revenue. We forecast a \$16m headwind, with controllable cost measures partly offsetting the impact.

**Investment view: Maintain Buy rating**

We adjust EPSA forecasts by +5%/+7% in FY25/26e, reflective of AMS strength and weaker PSS revenue expectations. With slowing orderbook growth, we have elected to lower the multiple and our SOTP valuation drops to \$21.00 p/s. A further reduction in vehicle delivery timeframes has been experienced in July, with increased competition on price. Management also advised that settlements for combustion engines are down marginally vs pcp. We remain Buy rated, viewing MMS as a cash generative business with exposure to electrification. FBT legislation is scheduled for a review by mid-2027 and volume growth should be supported new customer segments in Oly.

**Earnings Forecast**

Year Ending 30 June	2024	2025e	2026e	2027e
Sales (\$m)	525.7	537.0	541.7	569.7
EBITDA (Underlying) (\$m)	177.0	167.5	176.3	185.6
NPAT (Reported) (\$m)	90.1	95.1	109.4	115.4
NPATA (Adjusted) (\$m)	107.6	104.1	109.4	115.4
EPSA (Adjusted) (¢ps)	154.5	149.5	157.1	165.7
EPSA Growth (%)	43.2%	-3.3%	5.1%	5.5%
PER (x)	11.4	11.8	11.2	10.6
EV/EBITDA (x)	9.4	9.9	9.4	8.9
FCF Yield (%)	-10.8%	7.3%	11.3%	12.0%
Dividend (¢ps)	154.0	149.5	157.1	165.7
Yield (%)	8.7%	8.5%	8.9%	9.4%
Franking (%)	100.0%	100.0%	100.0%	100.0%
ROE (%)	61.1%	75.6%	88.1%	90.6%

SOURCE: BELL POTTER SECURITIES ESTIMATES

# FY24 result summary

Core EPSA +4% vs. VA cons (+2% vs. BPe) benefitting from improved vehicle supply and revenue carry over release. MMS expects to further progress the Simply Stronger Program and guided to \$11.0m capex in FY25 (vs \$23.0m pcp). MMS expects normalised financials to be provided up to and including FY25, guiding to a final statutory UNPATA adjustment of -\$9.0m, predicated on forecast volume and yield growth.

Figure 1 - FY24 result summary

Year End 30 June (A\$m)	2020a	2021a	2022a	1H23a	2H23a	2023a	1H24a	2H24a	2024a	2024e	Diff %
Group Remuneration Services	214.8	202.6	206.6	110.4	122.4	232.8	142.7	149.8	292.5	292.2	0.1%
Plan & Support Services	0.0	26.2	41.3	23.4	25.2	48.6	26.2	24.4	50.6	52.5	-3.7%
Asset Management Services	173.7	153.5	170.6	107.5	79.9	187.4	90.1	87.7	177.8	172.9	2.8%
Unallocated	0.3	0.2	0.3	1.2	1.4	2.6	2.1	2.7	4.8	2.1	NM
<b>Total Normalised Revenue</b>	<b>388.8</b>	<b>382.5</b>	<b>418.8</b>	<b>242.5</b>	<b>228.9</b>	<b>471.4</b>	<b>261.1</b>	<b>264.6</b>	<b>525.7</b>	<b>519.7</b>	1.2%
... Growth %	-4.0%	-1.6%	9.5%	14.1%	11.0%	12.6%	7.7%	15.6%	11.5%	10.3%	
Group Remuneration Services	103.3	87.1	82.1	40.4	49.8	90.2	64.2	67.6	131.8	131.8	0.0%
Plan & Support Services	0.0	8.5	10.2	4.9	7.4	12.3	6.8	6.3	13.1	15.0	-12.9%
Asset Management Services	17.5	23.4	27.8	15.8	12.9	28.7	15.1	14.4	29.5	27.1	8.9%
Unallocated	(2.6)	(2.1)	(2.1)	(0.2)	0.1	(0.1)	0.8	1.8	2.6	0.0	NM
<b>Normalised EBITDA</b>	<b>118.2</b>	<b>116.9</b>	<b>118.0</b>	<b>60.9</b>	<b>70.2</b>	<b>131.1</b>	<b>86.9</b>	<b>90.1</b>	<b>177.0</b>	<b>173.9</b>	1.8%
... Growth %	-4.0%	-1.1%	0.9%	9.3%	12.7%	11.1%	42.7%	28.3%	35.0%	32.7%	
... EBITDA Margin %	30.4%	30.6%	28.2%	25.1%	30.7%	27.8%	33.3%	34.1%	33.7%	33.5%	
D&A (non-fleet)	(17.6)	(16.5)	(16.0)	(8.0)	(8.4)	(16.4)	(8.4)	(7.8)	(16.2)	(17.5)	-7.3%
Total EBIT	100.6	100.4	102.0	52.9	61.8	114.7	78.5	82.3	160.8	156.4	2.8%
EBIT Margin (%)	25.9%	26.2%	24.4%	21.8%	27.0%	24.3%	30.1%	31.1%	30.6%	30.1%	
Interest Expense	(1.4)	(2.4)	(1.6)	(1.4)	(2.4)	(3.8)	(2.6)	(2.5)	(5.1)	(5.3)	-3.5%
<b>Normalised EBT</b>	<b>99.2</b>	<b>98.0</b>	<b>100.4</b>	<b>51.5</b>	<b>59.4</b>	<b>110.9</b>	<b>75.9</b>	<b>79.8</b>	<b>155.7</b>	<b>151.2</b>	3.0%
Tax Expense	(28.8)	(29.6)	(28.9)	(15.5)	(17.6)	(33.1)	(22.8)	(25.3)	(48.1)	(45.3)	6.1%
<b>Normalised UNPATA</b>	<b>69.3</b>	<b>68.4</b>	<b>71.5</b>	<b>36.0</b>	<b>41.8</b>	<b>77.8</b>	<b>53.1</b>	<b>54.5</b>	<b>107.6</b>	<b>105.8</b>	1.7%
Warehouse	0.0	0.0	(1.7)	(3.3)	(8.2)	(11.5)	(9.3)	(7.9)	(17.2)	(15.0)	14.7%
<b>UNPATA</b>	<b>69.3</b>	<b>68.4</b>	<b>69.8</b>	<b>32.7</b>	<b>33.6</b>	<b>66.3</b>	<b>43.8</b>	<b>46.6</b>	<b>90.4</b>	<b>90.8</b>	-0.5%
Abs. & Extras (Post-Tax)	9.2	7.3	(1.1)	0.0	(0.1)	0.0	0.0	0.0	0.0	0.0	NM
Acquired Amortisation (Tax Effected)	(2.9)	(1.6)	(1.8)	(0.9)	(0.9)	(1.8)	(0.2)	(0.1)	(0.3)	0.0	NM
<b>Reported NPAT (Continuing Operations)</b>	<b>75.6</b>	<b>74.1</b>	<b>66.9</b>	<b>31.8</b>	<b>32.6</b>	<b>64.5</b>	<b>43.6</b>	<b>46.5</b>	<b>90.1</b>	<b>90.8</b>	-0.8%
Dividend (¢ps)	34.0	61.3	108.0	58.0	66.0	124.0	76.0	78.0	154.0	151.9	1.4%

SOURCE: COMPANY DATA AND BELL POTTER SECURITIES ESTIMATES

## Key observations

- Normalised revenue grew +12% vs pcp to \$525.7m (BPe \$519.7m), underpinned by increased demand and availability of EVs which supported sales within novated. GRS grew +26% to \$292.5m, while PSS increased +4% and AMS was down -5%.
- MMS recorded novated sales and order growth of +23% and +8% vs pcp respectively. Carryover revenue decreased from \$32.3m to \$24.8m.
- EVs represented 43% of new novated orders (21% pcp), with a higher proportion from BEVs vs PHEVs.
- Normalised EBITDA grew +35% vs pcp to \$177.0m (BPe \$173.9m). EBITDA margins increased by 5.9ppts to 33.7%, predominantly reflecting the benefit of higher novated yields through vehicle price mix, and the effect of elevated interest rates on the salary packaging float, both dropping down to the bottom-line within GRS. Yield and interest rate delta is expected to be a negligible tailwind in FY25, with divisional revenue driven by volume growth.
- Normalised UNPATA (continuing ops.) increased +38% to \$107.6m (BPe \$105.8m).
- MMS announced a fully franked final dividend of 78.0¢ps (BPe 75.9¢ps), representing a payout ratio of 100% of normalised UNPATA.

# McMillan Shakespeare Ltd (MMS)

## Company Description

McMillan Shakespeare Ltd (MMS) is a leading provider of employee benefits, end-to-end fleet management and disability support services with over 400,000 salary packages and 75,000 novated leases under management. MMS operates a vertically integrated model by offering standalone and complementary products across administration, vehicle sourcing and total life-cycle management, finance procurement and the sale of ancillary product consumables. The employer customer base includes healthcare, government, education, not-for-profit and corporate sector clients.

## Investment Thesis and Valuation

We have a Buy recommendation on MMS and a Target Price of \$21.00 p/s. Our favourable investment view is supported by: (1) the defensive client base with strong employment growth forecast for the health care industry; (2) the *Electric Car Discount Bill (2022)* which exempts low or zero emission vehicles from Fringe Benefits Tax; and (3) moderate growth for participants within the NDIS.

We value MMS utilising a sum-of-the-parts approach. Our SOTP methodology ascribes an EV/EBITDA multiple to each business unit. We have elected to apply: (1) 11.0x to GRS; (2) 5.0x to PSS; and (3) 10.0x to AMS.

## Risks to Investment Thesis

Key downside risks to our investment thesis include (but are not limited to):

**Legislative reform risk:** The provision of products and services within salary packaging administration and novated leasing is underpinned by benefits permitted under our taxation laws. Any adverse change to the *Fringe Benefits Tax Assessment Act 1986* may impact the range of salary packaging benefits offered by MMS and could render several parts of the business as less profitable or redundant. This would materially undermine the Company's operations.

**Economic risk:** MMS is exposed to general economic and business conditions. Any deterioration to the level of Australian employment, utilisation, motor vehicle sales, demand for employer client services and or the addressable base of employee customers could materially adversely affect profitability.

**Competition risk:** The salary packaging and novated leasing industry is a mature market with several providers that offer low cost and undifferentiated products, separated by high levels of service. Targeting non-corporate employer clients with increased competition and or lower bargaining power could, for example, be reflected in lower pricing on tenders, win rates and panel offerings. Any deterioration to the competitive position of MMS could materially adversely affect the operations and financial performance.

**Residual value risk:** MMS may unfavourably realise a loss based on the difference between the final book value and trade disposal price of a vehicle. The residual value is set at the beginning of an operating lease, while realised car prices will oscillate over time. Downward pressure on used car prices would adversely impact the profitability of MMS.

**Employer client contract risk:** Many of the employer contracts that are held with MMS are long-standing partnerships with governments and large public authorities. These are regularly tendered at review dates, where each employer client usually has the right to terminate a contract without clause.

# McMillan Shakespeare Ltd

as at 27 August 2024

Recommendation

Buy

Price

\$17.63

Target (12 months)

\$21.00

Table 1 - Financial summary

June Year End						Price	\$17.63					
Profit & Loss (A\$m)						Recommendation						Buy
	2023	2024	2025e	2026e	2027e	Shares on Issue (m)						69.6
Sales Revenue	471.4	525.7	537.0	541.7	569.7	Market Cap (\$m)						1,227.8
... % Change	12.6%	11.5%	2.1%	0.9%	5.2%	Target Price (A\$ps)						\$21.00
<b>EBITDA</b>	<b>131.1</b>	<b>177.0</b>	<b>167.5</b>	<b>176.3</b>	<b>185.6</b>	<b>Valuation Ratios</b>						
... % Change	11.1%	35.0%	-5.4%	5.3%	5.3%	<b>Core EPSA (¢ps)</b>	<b>2023</b>	<b>2024</b>	<b>2025e</b>	<b>2026e</b>	<b>2027e</b>	
D&A (non-fleet)	(16.4)	(16.2)	(16.5)	(17.2)	(18.0)	107.9	154.5	149.5	157.1	165.7		
<b>EBIT</b>	<b>114.7</b>	<b>160.8</b>	<b>151.0</b>	<b>159.1</b>	<b>167.6</b>	... % Change	16.8%	43.2%	-3.3%	5.1%	5.5%	
Net Interest	(3.8)	(5.1)	(2.3)	(2.8)	(2.8)	DPS (¢ps)	124.0	154.0	149.5	157.1	165.7	
<b>EBT</b>	<b>110.9</b>	<b>155.7</b>	<b>148.7</b>	<b>156.3</b>	<b>164.9</b>	P/E (x)	16.3	11.4	11.8	11.2	10.6	
Tax Benefit/(Expense)	(33.1)	(48.1)	(44.6)	(46.9)	(49.5)	P/CF (x)	251.3	-9.3	13.7	8.9	8.3	
Minorities	-	-	-	-	-	EV/EBITDA (x)	12.6	9.4	9.9	9.4	8.9	
<b>Normalised UNPATA</b>	<b>77.8</b>	<b>107.6</b>	<b>104.1</b>	<b>109.4</b>	<b>115.4</b>	EV/EBIT (x)	14.4	10.3	11.0	10.4	9.9	
Warehouse	(11.5)	(17.2)	(9.0)	-	-	NTA (\$ps)	14.4	18.1	17.0	16.9	17.0	
<b>UNPATA</b>	<b>66.3</b>	<b>90.4</b>	<b>95.1</b>	<b>109.4</b>	<b>115.4</b>	P/NTA (x)	1.2	1.0	1.0	1.0	1.0	
Acquired Amortisation	(1.8)	(0.3)	-	-	-	<b>Perf. &amp; Leverage Ratios</b>						
Abs. & Extras (Post-Tax)	-	-	-	-	-	<b>2023</b>	<b>2024</b>	<b>2025e</b>	<b>2026e</b>	<b>2027e</b>		
<b>Reported NPAT</b>	<b>64.5</b>	<b>90.1</b>	<b>95.1</b>	<b>109.4</b>	<b>115.4</b>	EBITDA Margin (%)	27.8%	33.7%	31.2%	32.6%	32.6%	
<b>Cashflow (A\$m)</b>						EBIT Margin (%)	24.3%	30.6%	28.1%	29.4%	29.4%	
<b>EBITDA</b>	<b>179.3</b>	<b>227.3</b>	<b>223.1</b>	<b>231.1</b>	<b>240.0</b>	OCF Realisation (%)	26.1%	-85.6%	85.7%	116.3%	116.9%	
Changes in Working Capital	21.8	26.5	(22.8)	0.3	2.0	FCF Realisation (%)	6.5%	-123.1%	86.0%	126.8%	127.5%	
Changes in Fleet	(29.5)	(73.1)	(35.1)	(31.2)	(21.8)	ROA (%)	6.9%	7.1%	7.5%	9.0%	9.5%	
Changes in P&I Receivable	(81.0)	(227.5)	(6.0)	(3.3)	(11.9)	ROE (%)	34.1%	61.1%	75.6%	88.1%	90.6%	
<b>Gross Cash Flow</b>	<b>90.6</b>	<b>(46.9)</b>	<b>159.3</b>	<b>196.9</b>	<b>208.2</b>	ROIC (%)	30.2%	33.2%	26.9%	29.0%	32.4%	
Net Interest Expense	4.9	(2.3)	(2.3)	(2.8)	(2.8)	Payout Ratio (%)	114.9%	99.7%	100.0%	100.0%	100.0%	
Income Tax Paid	(18.1)	(17.7)	(44.6)	(46.9)	(49.5)	Dividend Yield (%)	7.0%	8.7%	8.5%	8.9%	9.4%	
Residual Operating Items	(52.8)	(39.1)	(9.0)	-	-	Franking (%)	100.0%	100.0%	100.0%	100.0%	100.0%	
<b>Operating Cash Flow</b>	<b>24.6</b>	<b>(106.0)</b>	<b>103.3</b>	<b>147.2</b>	<b>155.9</b>	Net Interest Cover (x)	30.2	31.5	64.8	56.5	60.3	
Finance Leases	(3.2)	(4.8)	(3.1)	(3.1)	(3.1)	Net Debt/EBITDA (x)	1.7	2.2	2.4	2.1	1.8	
<b>Lease Adjusted OCF</b>	<b>21.4</b>	<b>(110.8)</b>	<b>100.2</b>	<b>144.1</b>	<b>152.8</b>	Net Debt/Equity (%)	149.8%	301.2%	325.6%	292.3%	257.7%	
Capital Expenditure	(16.3)	(21.6)	(10.7)	(5.4)	(5.7)	Net Debt/Net Debt+Equity (%)	60.0%	75.1%	76.5%	74.5%	72.0%	
<b>Free Cash Flow</b>	<b>5.1</b>	<b>(132.4)</b>	<b>89.5</b>	<b>138.7</b>	<b>147.1</b>	<b>Segment Revenue (A\$m)</b>						
Dividends Paid	(91.9)	(98.9)	(101.2)	(106.5)	(112.1)	<b>2023</b>	<b>2024</b>	<b>2025e</b>	<b>2026e</b>	<b>2027e</b>		
Other Investing Items	(37.0)	58.0	-	-	-	GRS	232.8	292.5	295.7	313.3	334.1	
Share Issues/(Buy-Backs)	(90.2)	(3.0)	-	-	-	PSS	48.6	50.6	52.0	54.9	57.2	
Change in Borrowings	113.9	268.7	(52.9)	(13.7)	-	AMS	187.4	177.8	186.1	170.2	175.0	
<b>Net Change in Cash</b>	<b>(100.2)</b>	<b>92.4</b>	<b>(64.5)</b>	<b>18.5</b>	<b>35.0</b>	<b>Total</b>	<b>468.8</b>	<b>520.9</b>	<b>533.8</b>	<b>538.4</b>	<b>566.3</b>	
<b>Balance Sheet (A\$m)</b>						<b>Segment EBITDA (A\$m)</b>						
Cash and Equivalents	60.6	153.0	88.4	107.0	141.9	<b>2023</b>	<b>2024</b>	<b>2025e</b>	<b>2026e</b>	<b>2027e</b>		
Trade Receivables	40.0	39.5	45.6	46.0	48.4	GRS	90.2	131.8	127.1	137.8	147.0	
P&I Receivables	109.1	336.6	342.6	345.9	357.8	PSS	12.3	13.1	13.5	15.6	17.8	
Fleet Assets	205.0	227.8	207.3	183.8	151.2	AMS	28.7	29.5	28.5	24.7	22.7	
Right-of-Use Assets	30.1	25.9	25.9	25.9	25.9	<b>Total</b>	<b>131.2</b>	<b>174.4</b>	<b>169.2</b>	<b>178.1</b>	<b>187.5</b>	
P,P&E	13.7	11.8	10.0	8.3	6.8	<b>Assumptions</b>						
Intangibles (incl. Goodwill)	73.4	83.2	82.4	75.4	67.7	<b>2023</b>	<b>2024</b>	<b>2025e</b>	<b>2026e</b>	<b>2027e</b>		
Other	517.8	425.2	425.2	425.2	425.2	Novated Sales (#)	21,813	26,830	27,579	30,287	32,710	
<b>Total Assets</b>	<b>1,049.6</b>	<b>1,303.1</b>	<b>1,227.4</b>	<b>1,217.4</b>	<b>1,225.0</b>	PSS Customers (#)	31,771	35,030	38,184	41,418	43,666	
Trade Payables	73.1	99.9	83.2	84.0	88.3	Fleet Residual Value (%)	67.4%	88.0%	65.0%	60.0%	50.0%	
Provisions	16.7	18.3	18.3	18.3	18.3							
Borrowings	278.6	541.0	488.1	474.4	474.4							
Lease Liabilities	46.5	40.9	40.9	40.9	40.9							
Other	489.0	474.1	474.1	474.1	474.1							
<b>Total Liabilities</b>	<b>904.0</b>	<b>1,174.2</b>	<b>1,104.7</b>	<b>1,091.7</b>	<b>1,096.0</b>							
<b>Net Assets</b>	<b>145.6</b>	<b>128.8</b>	<b>122.8</b>	<b>125.7</b>	<b>129.0</b>							
Contributed Equity	68.6	68.6	68.6	68.6	68.6							
FX Translation Reserve	(2.8)	-	-	-	-							
General Reserves	(0.5)	(2.4)	(2.4)	(2.4)	(2.4)							
Retained Profits/(Losses)	80.2	62.7	56.6	59.6	62.8							
<b>Total Equity</b>	<b>145.6</b>	<b>128.8</b>	<b>122.8</b>	<b>125.7</b>	<b>129.0</b>							
Net Debt/(Cash)	218.0	388.0	399.7	367.5	332.5							

SOURCE: BELL POTTER SECURITIES ESTIMATES

**Recommendation structure**

**Buy:** Expect >15% total return on a 12 month view. For stocks regarded as 'Speculative' a return of >30% is expected.

**Hold:** Expect total return between -5% and 15% on a 12 month view

**Sell:** Expect <-5% total return on a 12 month view

*Speculative Investments are either start-up enterprises with nil or only prospective operations or recently commenced operations with only forecast cash flows, or companies that have commenced operations or have been in operation for some time but have only forecast cash flows and/or a stressed balance sheet.*

*Such investments may carry an exceptionally high level of capital risk and volatility of returns.*

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