NEXUS INFRASTRUCTURE

CONSTRUCTION

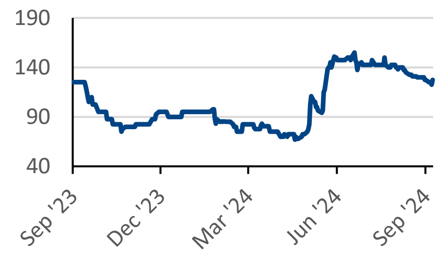
24 September 2024

NEXS.L

135p

Market Cap: £12.2m

SHARE PRICE (p)



12m high/low	155p/67p

Source: LSE Data (priced as at prior close)

KEY DATA

Net (debt)/cash	£9.2m *(at 31/03/24)*
Enterprise value	£3m
Index/market	AIM
Next news	FY trading update, Oct
Shares in issue (m)	9.0
Chairman	Richard Kilner
Chief Executive	Charles Sweeney
Finance Director	Dawn Hillman

COMPANY DESCRIPTION

Civil engineering and infrastructure services for housebuilders, focused in the South-East and London

www.nexus-infrastructure.com

NEXUS INFRASTRUCTURE IS A RESEARCH CLIENT OF PROGRESSIVE

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Engineered to lead housebuilding revival

The Labour government's ambitious plan to build 1.5 million homes in five years comes as Nexus Infrastructure has re-engineered its subsidiary, Tamdown, to focus on 'front end' civil engineering for the UK's top housebuilders. After aligning the cost base in the face of sector and economic headwinds, our initial estimates indicate the group should return to modest profit by 2H 25E. Thereafter, operational gearing could offer substantial earnings growth under a range of scenarios – arguably ignored in the current valuation.

- **Focused on 'front end' civil engineering for housebuilders.** Nexus, which has operated for over 45 years, divested its utility connections businesses for £78m in 2023, returning £61m to shareholders. The remaining Tamdown business is focused on a range of civil engineering services for major housebuilders, from early earthworks to housing foundations (p.2). Profits were hit by the slowing market and failure of customer ilke Homes. However, Nexus responded with tight cost and cash management, leaving it, according to the latest interims, 'well positioned for the market upturn'.
- **Housebuilding recovery boosted by new government.** Recent updates from leading housebuilders have indicated completion volumes will meet or beat previous guidance. Site openings and housing starts are more important for Nexus, which expects gradual recovery in FY25E. Nexus serves all the top-5 UK housebuilders, as well as mixed-tenure developers.
- **Longer-term infrastructure opportunities.** Over the medium term, the group is considering diversifying into vital infrastructure. Of this, water supply and sewage, flood protection and energy are urgent national priorities. Longer term, a major opportunity could be Labour's plans for 'new towns', given Tamdown's experience in large, complex sites.
- **Turning point for profitability.** Revenue for Tamdown was boosted significantly in FY22 and the first half of FY23 by housebuilders' rush to start homes ahead of tougher Building Regulations from June 2023. The subsequent decline in starts was exacerbated by rising mortgage rates and cost inflation. Our initial estimates assume reduced losses in FY24E and a modest loss in FY25E (p.3). Alternative scenarios beyond our formal forecast range suggest EPS could reach 14.6p-28.0p by FY27E.
- **Valuation ignoring opportunities and operational gearing?** Our formal forecasts indicate a dividend yield of 2.6% in FY25E. Our two alternative longer-term scenarios indicate a PER as low as 4.8x for FY27E.

FYE SEP (£M)	2021	2022	2023	2024E	2025E
Revenue	77.3	98.4	88.7	55.9	67.1
Fully Adj PBT	-3.0	-0.9	-5.0	-2.4	-0.5
Fully Adj EPS (p)	-3.9	-2.2	-34.5	-25.8	-4.5
Dividend per share (p)	2.0	1.0	3.0	3.0	3.5
PER (x)	N/A	N/A	N/A	N/A	N/A
EV/EBITDA (x)	-3.1x	1.7x	-1.2x	2.7x	1.1x
Dividend yield	1.5%	0.7%	2.2%	2.2%	2.6%

Source: Company Information and Progressive Equity Research estimates.

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Please refer to important disclosures at the end of the document.

A leading force in reviving housebuilding market

Nexus Infrastructure, via its principal trading business Tamdown, is a leading provider of civil engineering services, principally to major housebuilders. The group is aiming to expand its activities to critical infrastructure, including water, flood protection and energy.

- **Recent history.** Nexus has been operating for over 45 years. In February 2023, the group completed the disposal of TriConnex (connection of water, energy etc for housebuilders) and eSmart Networks (power connections for industrial and commercial customers) to private investment group FitzWalter Capital for a cash consideration of £78m; c.£61m was subsequently returned to shareholders by way of a tender offer. In June 2023, Nexus announced it was owed c.£2m from the failed modular housing manufacturer ilke Homes, and that it had been anticipating additional turnover of c.£4m for the remainder of FY23. In October 2023, the group reported losses on a further reduction in revenue amid slowing housebuilding along with inflationary pressures, responding with a series of cost-cutting actions and other proactive measures to improve margins. The interim results in May signalled 'confidence in delivering in H2 and beyond'.
- **Broad range of activities.** The group's activities comprise a wide range of civil engineering services, including earthworks, roads, drainage and foundations. These activities are weighted towards the opening of new housebuilding sites.
- **Leading housebuilding customers.** Clients include the UK's top five listed housebuilders – Barratt Developments, Vistry Group, Taylor Wimpey, Persimmon and Bellway – as well as leading private groups including Bloor Homes, partnership specialist Keepmoat and housing associations. The group operates mainly in London and the South East.
- **Multi-year opportunities.** The most immediate prospects, we believe, are housebuilders increasing the number of new sites they open. This was already looking likely, evidenced by accelerated land buying, but has been given added impetus by the new Labour government's commitment to build 1.5 million homes in the current parliament. The group expects this to boost site work by 2H 25E. Over the medium term, Nexus is considering diversifying into vital infrastructure. Of this, water and energy are urgent national priorities. Longer term, a major opportunity could be Labour's plans for 'new towns', given Tamdown's experience in large, complex sites. A start on these would probably require at least five years for land assembly and planning.
- **Technical, financial and operational strengths.** Tamdown has a broad range of technical abilities, a strong brand and well-established relationships with most of the leading housebuilders. This sector is going through a process of consolidation (including the Barratt-Redrow merger), adding demand for the group's capabilities in large, complex, multi-phase developments, in which the largest developers predominate. The group's robust balance sheet is of increasing importance for major customers, amid a rash of supply-chain failures afflicting the wider industry. Also significant for major customers is Tamdown's record in health & safety, demonstrated by 15 consecutive annual Royal Society for the Prevention of Accidents (RoSPA) Gold Awards.
- **Fragmented industry structure.** Competition is fragmented among Tamdown's smaller peers, but we expect a phase of consolidation, either through loss of market share, company failures or M&A. With diversification a key pillar of its strategy, we would anticipate acquisition activity in the short to medium term, and believe targets would aim to create value by adding complementary skills or market opportunities.
- **ESG.** The group's Building Bright Futures programme provides guiding sustainability principles for employees (including a Wellbeing programme), community (encouraging volunteering) and planet (reducing carbon footprint and environmental impact).

Growing sales and operational gearing to drive profits

Profitability at a turning point after double whammy of headwinds; magnitude of recovery influenced by operational gearing

A 'double whammy' of market and economic headwinds caused revenue and gross profit to fall significantly in H2 FY23 and H1 FY24, leading to operating losses (Figure 1). In response, the group cut operating expenses, but our estimates assume only modest PBT by FY25E. While we believe it is too early to provide formal estimates for the following two years, we provide varying scenarios that suggest profits could rise substantially.

Rush to start homes ahead of CY 2023 mid-year regulatory change was followed by slowdown, exacerbated by rising mortgage rates and build costs

Revenue for Tamdown was boosted significantly in FY22 and the first half of FY23 by the rush from housebuilders to open sites or start individual plots (in reality only requiring basic foundations) ahead of tougher Building Regulations from June 2023. The subsequent decline in starts was exacerbated by rising mortgage rates and build cost inflation. The first half of FY24E (to March) showed a 49% Y/Y fall in revenue to £25.8m. Gross profit fell by a lower 39%, to £3.5m, but this did not cover operating expenses of £4.8m, resulting in an operating loss of £1.3m for the period.

Improvements likely to start in second half of FY24E, leading to a reduced operating loss

Our estimates for FY24E include a 37% decline in revenue to £55.9m, but with a 16% recovery between H1 and H2. We have assumed that reduced building cost inflation will support a slight improvement in the gross margin to 13.6% in H2, from 13.5% in H1, and operating expenses bottoming out at £9.3m. This implies a reduction in the loss before exceptionals and tax in H2. We anticipate these at c.£300k, reflecting restructuring costs.

Return to modest profitability in FY25, supported by further growth in revenue and gross margin evolution

We expect an increase in new site openings by housebuilders to support a continuation in revenue growth seen in H2 FY24E feeding through to FY25E and beyond. Our estimates for FY25E assume a 20% increase in revenue. This assumption is underpinned by a 57% increase in the order book to £72m between the FY23 year-end and H1 FY24E, including contract awards from Taylor Wimpey, Vistry, Persimmon and Bellway. We have also factored in a further improvement in the gross margin to 14.3% and operating expenses edging up by c.5% to £9.8m. This should lead to a very modest loss before tax – however, operational gearing could lead to breakeven if there is a further increase in revenue.

Tight cash management maintains robust balance sheet

As well as focusing on cost reduction during the recent challenging market conditions, the group has maintained tight control on cashflow (Figure 2). Capex has been minimal in FY23 and H1 FY24. A reduction in revenue in FY23 and tight management of cash during the year led to only a modest working capital outflow of £1.3m. In the first half of FY24E, the working capital outflow was 41% below the comparative period in FY23. However, as revenue revives, we expect a build-up in working capital requirements and anticipate net cash, pre-IFRS16 leases, to remain at c.£10m for both FY24E and FY25E.

Alternative scenarios demonstrate potential longer-term upside

Too early to provide estimates for FY26E and FY27E, but two scenarios point to significant earnings potential from operational gearing

We believe it is too early to provide formal estimates for FY26E and FY27E, given uncertainty about the precise timing and pace of recovery in the market and the high degree of operational leverage. However, it is likely this leverage could translate into significant increases in earnings – arguably not reflected in the current valuation. We have run a couple of illustrative scenarios. In both cases we have assumed that administrative expenses continue to increase by 5% in both years and that interest remains unchanged from the FY25E estimate. On our more conservative assumption, of revenue rising 15% for both years, to £88.7m (the three-year average for FY21-FY23) and at a gross margin only slightly up at 14.5%, EPS would be 4.9p for FY26E and 14.6p, a PER of 9.2x, for FY27E.

Our second scenario assumes 20% growth in revenue for both years, taking it to £96.6m by FY27E. If gross margins were to edge up slightly to 14.8% and then 15.0%, EPS would rise to 10.9p then 28.0p over the same period, a PER of only 4.8x for the final year.

Figure 1: P&L and per share data

Year-end September (£m)	FY21	FY22	FY23	FY24E	FY25E	H1 23	H2 23	H1 24	H2 24E
Group revenue	**77.3**	**98.4**	**88.7**	**55.9**	**67.1**	**51.0**	**37.7**	**25.8**	**30.0**
COGS	(71.3)	(88.5)	(82.7)	(48.3)	(57.5)	(45.3)	(37.5)	(22.3)	(25.9)
Gross profit	**6.0**	**9.9**	**6.0**	**7.6**	**9.6**	**5.8**	**0.2**	**3.5**	**4.1**
Operating expenses	(8.6)	(10.2)	(10.8)	(9.3)	(9.8)	(5.7)	(5.1)	(4.8)	(4.5)
Operating profit	**(2.6)**	**(0.3)**	**(4.8)**	**(1.7)**	**(0.2)**	**0.1**	**(4.9)**	**(1.3)**	**(0.4)**
Exceptionals	1.3	-	(3.6)	(0.3)	-	-	(3.6)	-	(0.3)
Interest	(0.4)	(0.6)	(0.2)	(0.7)	(0.3)	(0.0)	(0.1)	(0.2)	(0.5)
PBT, reported	**(1.7)**	**(0.9)**	**(8.5)**	**(2.7)**	**(0.5)**	**0.0**	**(8.6)**	**(1.5)**	**(1.2)**
Tax	(0.1)	(0.1)	0.0	0.0	0.1	-	0.0	0.0	-
Discontinued	4.8	3.7	67.3	-	-	67.3	-	-	-
Net attrib. profit	**3.0**	**2.7**	**58.8**	**(2.6)**	**(0.4)**	**67.3**	**(8.5)**	**(1.4)**	**(1.2)**
PBT, pre-exceptionals	**(3.0)**	**(0.9)**	**(5.0)**	**(2.4)**	**(0.5)**	**0.0**	**(5.0)**	**(1.5)**	**(0.9)**
EBITDA	**(1.0)**	**1.7**	**(2.5)**	**1.1**	**2.7**	**1.4**	**(3.8)**	**0.1**	**1.0**
Diluted shares (million)	46.3	46.1	24.6	9.0	9.0	40.3		9.0	
EPS, basic (p)	6.6	6.0	239.0	(29.2)	(4.5)	167.3		(15.9)	
EPS, pre-exc, cont. (p)	**(3.9)**	**(2.2)**	**(34.5)**	**(25.8)**	**(4.5)**	**0.1**		**(15.9)**	
DPS - declared (p)	2.0	1.0	3.0	3.0	3.5	1.0	2.0	1.0	2.0
Dividend cover (x)	na	na	na	(8.6)	(1.3)				
NAV (p)	70.8	74.9	365.4	333.2	324.9	461.0		349.5	
TNAV (p)	65.6	69.8	339.2	307.1	298.8	434.8		323.3	
FCFPS (p)	(8.9)	21.0	(30.9)	(47.0)	(3.0)	(15.9)		(51.2)	
Change in revenue, Y/Y (%)		27.2%	-9.9%	-37.0%	20.0%	9.3%	-27.2%	-49.4%	-20.3%
Gross margin (%)	*7.8%*	*10.1%*	*6.7%*	13.6%	14.3%	*11.3%*	*0.6%*	*13.5%*	13.6%
Operating margin (%)	*-3.3%*	*-0.3%*	*-5.4%*	-3.0%	-0.4%	*0.1%*	*-12.9%*	*-4.9%*	-1.4%

Source: Company Information and Progressive Equity Research estimates.

Figure 2: Cash Flow and Balance Sheet

Year-end September (£m)	FY21	FY22	FY23	FY24E	FY25E	H1 23	H2 23	H1 24	H2 24E
Adjusted cash flow statement									
Group operating profit	(2.6)	(0.3)	(4.8)	(2.0)	(0.2)	0.1	(4.9)	(1.3)	(0.7)
Depreciation	1.6	2.0	2.3	2.8	2.9	1.3	1.1	1.4	1.4
Other, non-cash	6.1	4.7	(3.5)	(0.1)	-	0.5	(3.9)	(0.1)	-
Working capital	(1.7)	(8.9)	(1.3)	(4.0)	(2.0)	(7.8)	6.5	(4.6)	0.6
Operating cash flow	**3.4**	**(2.4)**	**(7.3)**	**(3.3)**	**0.7**	**(6.0)**	**(1.3)**	**(4.6)**	**1.3**
Capex	(5.8)	12.8	(0.4)	(0.3)	(0.8)	(0.0)	(0.4)	(0.1)	(0.2)
Interest	(0.4)	(0.2)	(0.2)	(0.7)	(0.3)	0.0	(0.2)	0.1	(0.8)
Tax	(0.3)	(0.6)	0.2	0.0	0.1	(0.4)	0.6	-	0.0
Free cashflow	**(4.0)**	**9.6**	**(7.6)**	**(4.2)**	**(0.3)**	**(6.4)**	**(1.2)**	**(4.6)**	**0.4**
(Acquisitions)/disposals	0.0	-	60.2	-	-	60.2	-	-	-
Dividends - paid	(0.3)	(1.1)	(0.1)	(0.3)	(0.3)	(0.1)	-	-	(0.3)
Share (purchase)/proceeds	0.0	0.0	(60.5)	-	-	(60.5)	-	-	-
Other financing	0.7	(13.8)	(1.5)	(0.8)	-	(1.4)	(0.1)	(0.775)	-
Change in cash	**(3.6)**	**(5.3)**	**(9.5)**	**(5.3)**	**(0.6)**	**(8.2)**	**(1.3)**	**(5.4)**	**0.1**
Summary balance sheet									
Intangible fixed assets	2.4	2.4	2.4	2.4	2.4	2.4		2.4	
Tangible fixed assets	19.6	18.1	16.8	14.3	12.2	17.6		15.7	
Working capital	(7.6)	13.3	10.9	14.9	16.9	17.9		15.4	
Provisions, others	(0.3)	(12.5)	(11.7)	(11.7)	(11.7)	(12.2)		(11.1)	
Retirement benefits	-	-	-	-	-	-		-	
Net cash/(debt), pre-leases	18.1	4.6	14.6	10.2	9.6	16.0		9.2	
Discontinued	-	8.3	-	-	-	-		-	
Net assets	**32.1**	**34.1**	**33.0**	**30.1**	**29.4**	**41.6**		**31.6**	
Net cash/(debt), inc leases	*15.5*	*(7.9)*	*3.0*	*(1.4)*	*(2.0)*	*3.8*		*(1.9)*	

Source: Company Information and Progressive Equity Research estimates.

Progressive EQUITY RESEARCH

Financial Summary: Nexus Infrastructure

Year end: September (£m unless shown)

PROFIT & LOSS	**2021**	**2022**	**2023**	**2024E**	**2025E**
Revenue	77.3	98.4	88.7	55.9	67.1
Adj EBITDA	(1.0)	1.7	(2.5)	1.1	2.7
Adj EBIT	(2.6)	(0.3)	(4.8)	(1.7)	(0.2)
Reported PBT	(1.7)	(0.9)	(8.5)	(2.7)	(0.5)
Fully Adj PBT	(3.0)	(0.9)	(5.0)	(2.4)	(0.5)
NOPAT	(2.6)	(0.3)	(4.8)	(1.7)	(0.2)
Reported EPS (p)	6.6	6.0	239.0	(29.2)	(4.5)
Fully Adj EPS (p)	(3.9)	(2.2)	(34.5)	(25.8)	(4.5)
Dividend per share (p)	2.0	1.0	3.0	3.0	3.5
CASH FLOW & BALANCE SHEET	**2021**	**2022**	**2023**	**2024E**	**2025E**
Operating cash flow	3.4	(2.4)	(7.3)	(3.3)	0.7
Free Cash flow	(4.0)	9.6	(7.6)	(4.2)	(0.3)
FCF per share (p)	(8.9)	21.0	(30.9)	(47.0)	(3.0)
Acquisitions	0.0	0.0	0.0	0.0	0.0
Disposals	0.0	0.0	60.2	0.0	0.0
Shares issued/(purchased)	0.0	0.0	(60.5)	0.0	0.0
Net cash flow	(3.6)	(5.3)	(9.5)	(5.3)	(0.6)
Net (debt)/cash, post IFRS16	15.5	(7.9)	3.0	(1.4)	(2.0)
Cash & equivalents	29.5	4.6	14.6	9.3	8.7
Net (debt)/cash, pre-IFRS 16	18.1	4.6	14.6	10.2	9.6
NAV AND RETURNS	**2021**	**2022**	**2023**	**2024E**	**2025E**
Net asset value	32.1	34.1	33.0	30.1	29.4
NAV/share (p)	70.8	74.9	365.4	333.2	324.9
Net Tangible Asset Value	29.8	31.8	30.6	27.7	27.0
NTAV/share (p)	65.6	69.8	339.2	307.1	298.8
Average equity	32.1	33.1	33.6	31.6	29.7
Post-tax ROE (%)	9.3%	8.2%	175.1%	(8.3%)	(1.4%)
METRICS	**2021**	**2022**	**2023**	**2024E**	**2025E**
Revenue growth	N/A	27.2%	(9.9%)	(37.0%)	20.0%
Adj EBITDA growth	N/A	N/A	N/A	N/A	138.7%
Adj EBIT growth	N/A	(87.8%)	N/A	N/A	N/A
Adj PBT growth	N/A	(69.3%)	N/A	(52.2%)	N/A
Adj EPS growth	N/A	(43.3%)	N/A	(25.2%)	N/A
Dividend growth	N/A	(50.0%)	N/A	0.0%	16.7%
Adj EBIT margins	(3.3%)	(0.3%)	(5.4%)	(3.0%)	(0.4%)
VALUATION	**2021**	**2022**	**2023**	**2024E**	**2025E**
EV/Sales (x)	0.04	0.03	0.03	0.05	0.04
EV/EBITDA (x)	-3.1	1.7	-1.2	2.7	1.1
EV/NOPAT (x)	-1.2	-9.5	-0.6	-1.8	-12.2
PER (x)	N/A	N/A	N/A	N/A	N/A
Dividend yield	1.5%	0.7%	2.2%	2.2%	2.6%
FCF yield	(6.6%)	15.6%	(22.9%)	(34.8%)	(2.2%)

Source: Company information and Progressive Equity Research estimates

24 September 2024

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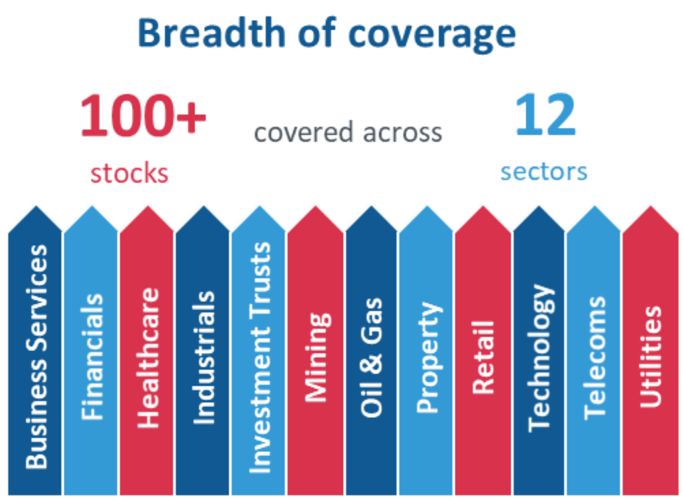

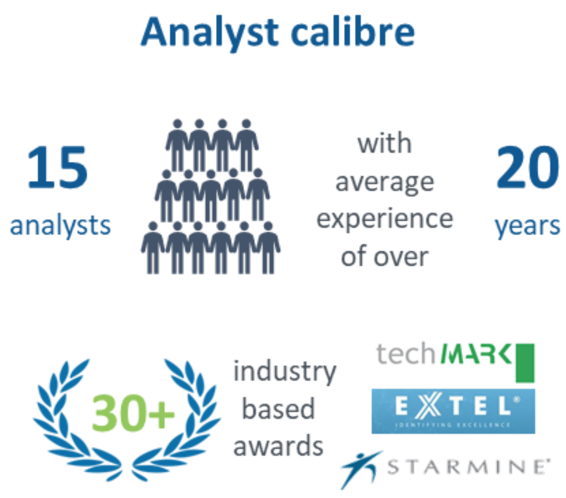

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