



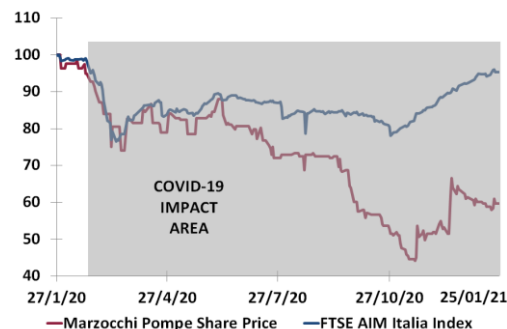
FLASH NOTE

OUTPERFORM

Current Share Price (€): 2.78

Target Price (€): 3.61

Marzocchi Pompe - 1Y Performance



Source: S&P Capital IQ - Note: 27/01/2020=100

Company data

ISIN number	IT0004376858
Bloomberg code	MARP IM
Reuters code	MARP.MI
Industry	Pumps & pumping equipment
Stock market	AIM Italia
Share Price (€)	2.78
Date of Price	25/01/2021
Shares Outstanding (m)	6.5
Market Cap (€m)	18.2
Market Float (%)	23.2%
Daily Volume	0
Avg Daily Volume YTD	4,375
Target Price (€)	3.61
Upside (%)	30%
Recommendation	OUTPERFORM

Share price performance

	1M	3M	1Y
Marzocchi Pompe - Absolute (%)	-6%	13%	-38%
FTSE AIM Italia (%)	4%	18%	-6%
1Y Range H/L (€)	4.66	2.06	
YTD Change (€) / %	-0.08	-3%	

Source: S&P Capital IQ

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Accelerating performance in H2 supports a brightened outlook

High performance in H2 2020: Revenues up to pre-Covid levels and cut of debt depict a change of pace

Marzocchi Pompe sales had a jump in H2 2020 (+19% on H1 2020), over expectations for the six months and for the full year. Automotive sales grew +56% on H1 2020 and +40% on H2 2019, core business sales (Industrial, Mobile and Sales Network) progressed with +6% on H1 2020. Exports grew as a result of the recovery in the North American market.

Anticipating FY20 outcome: ahead of our last estimates

FY20 unaudited pre-closing consolidated figures unveiled:

- €34.2m Revenues (-13% YoY), with exports at 77.5% of sales vs. 75% in FY19
- €9.6m Net financial debt as of year-end 2020 (from €11.2m as of June 2020 and €12.5m as of year-end 2019)

Marzocchi's business in 2020 performed ahead of our estimates, which we had conservatively revised last October, reflecting the slowdown in H1 orders due to the global pandemic impact on operations of end-markets. Pre-closing FY20 revenues at €34.2m vs. our guidance at €31.8m, while year-end financial debt at €9.6m is overall in line with our estimate at €9.2m, benefitting from sound cash generation.

Business update

Marzocchi in H2 2020 has carried on working on efficiency, R&D and market penetration programs. In the same period, a China branch in joint-venture with its local distributor "Marzocchi Symbridge Hydraulic (Shangai) Co. Ltd" was established, with the aim of increasing penetration of its core business products in China.

Target Price €3.61 per share (from €2.90), OUTPERFORM rating (from NEUTRAL)

We note that, despite the current scenario, Marzocchi has retained its dynamic market penetration and operations management profile and had no harm, other than temporary, on its solid balance sheet and cash generation ability.

Pre-closing figures are overall consistent with our last estimates, which have been just shifted to the next three years. The updated valuation suggests a target price of €3.61 per share, from €2.90, 30% upside on current share price. We assign an OUTPERFORM rating on the stock (from NEUTRAL), in view of a lower risk profile.

Key financials and estimates

€m	2017	2018	2019	2020PC	2021E	2022E	2023E
Revenues	38.6	42.7	39.3	34.2	36.5	39.6	44.3
EBITDA	6.8	7.5	6.3	3.9	5.8	6.8	7.7
<i>Margin</i>	<i>17.6%</i>	<i>17.6%</i>	<i>16.0%</i>	<i>11.5%</i>	<i>15.8%</i>	<i>17.3%</i>	<i>17.4%</i>
Net (Debt) Cash	(14.4)	(19.2)	(12.5)	(9.6)	(8.9)	(5.5)	(2.7)

Source: Company data 2017A-2020PC (EBITDA 2020 EnVent estimate), EnVent Research 2021-23E

Investment Case

Company

Marzocchi Pompe S.p.A. (Marzocchi) is an Italian designer and producer of a wide range of high performance external gear pumps, whose reference market is the wider Power Transmission and Motion Control (PTMC) industry. Marzocchi products are extensively used in motion related applications in which reliability and precision are critical.

Customers vary across sectors: industrial (textile machines, machine tools, plastic injection machines, medical equipment, energy, etc.), mobile (agricultural machines, forklift trucks, etc.) and automotive (transmissions, power steering, attitude adjusters, etc.). Marzocchi serves Original Equipment Manufacturers (OEM) customers as Tier 1 supplier and large Tier 1 suppliers in the industry as Tier 2 supplier.

Key figures (2020)

- Revenues €34m - 4% CAGR 2014-20
- Geographical breakdown: Foreign markets 77.5% - Italy 22.5%
- 2 production plants and 2 international branches

Revenue drivers

Revenues are generated by continuing relationships in the Power Transmission and Motion Control industry based on the reputation of technical excellence. A significant portion of revenues is generated by long-term contracts as sole supplier of high performance components for Tier 1 large multinational customers. Marzocchi's business model relies on a partnership model and joint engineering for the development of ad hoc motion control technology with customers based on their needs. As such, Marzocchi has high visibility on revenues, of which a major portion comes from recurring customers.

Drivers

Industry drivers

Motion control and innovation technology. The global Power Transmission Motion Control market is driven by general macro-economic growth, the rapid pace of globalization and developments in automation technologies. The availability of advanced applications has fostered the rising demand for motion control in the medical, food and beverage, electrical, automotive and machinery industries.

Industrial power transmission, a huge global industry. The global PTMC industry generated \$200bn sales in 2018. Main segments: mechanical power transmission; motors and generators; adjustable speed drives. The Motion control segment in which Marzocchi competes would be worth \$100bn globally in 2018 based on historical ratios.

Motion control products tend to be higher margin than power transmission products due to a greater use of technology and leverage in end markets with more attractive technological trends. The global PTMC industry, in which Marzocchi competes, is highly fragmented, with over 1,000 small manufacturers and relatively few players of scale. Smaller companies tend to focus on regional niche markets with narrow product lines, larger players that generate annual revenue of over \$100m generally offer a broader range of products and provide global sales and service capabilities. (Source: Altra website). Marzocchi matches such global standing profile, despite its somewhat lower level of sales.

Automation - reference markets trends all up. According to UBS, automation market size is around \$170bn growing on average by 3-4% from 2010 till 2017. Automation is

increasingly used outside automotive industry, which provides a growth opportunity for automation equipment manufacturers. The need for improving efficiency, flexibility, quality and productivity of manufacturing industries is driving the growth of the global industrial automation market. (Source: UBS, Longer term investments, 2018)

Automation growth impacts fluid power market trend. The fluid power market is the first sector that benefits from automation needs. Hydraulic end-use market is forecasted to grow constantly with an average rate of 3% worldwide for the period 2018-22 (Source: National Fluid Power association and Oxford Economics, Strong outlook but risks are brewing, 2018).

Advanced Driver Assistance Systems (ADAS) to fuel additional growth. According to McKinsey, most industry experts agree on substantial revenues and double-digit growth for Advanced Driver Assistance Systems in the years to come. This is likely to give the segment one of the highest growth rates in the automotive sector and related industries. Within the automotive sector, a large end-user of hydraulic components, the rising demand for advanced systems such as drowsiness monitoring, night vision, and road sign recognition system is expected to impact the overall industry and the Hydraulic segment itself. A progressive scenario from McKinsey estimates around 50% of vehicles sold in 2030 being highly autonomous and around 15% being fully autonomous (Source: McKinsey, Automotive revolution - perspective towards 2030, 2016).

Company drivers

Flexible business model based on teamwork and partnerships with customers. Marzocchi Pompe's business model relies on R&D and new product development, in partnership with its OEM or global supply chain Tier 1 customers, meeting their technology and product quality demands. Standing of customers and recurring sales volumes of engineered specialty products is evidence that Marzocchi is a preferred supplier to top automotive and industrial machinery customers that addresses their needs effectively.

Wide and diversified product portfolio. Marzocchi product portfolio includes a vast range of engineered high-technology external gear pumps, covering the needs of most applications. Products include a significant number of unique and customized parts based on customers' needs. Marzocchi is also specialized in micro-hydraulics, such as low displacement pumps, which require technologically advanced production processes.

Development and innovation skills, state-of-the-art manufacturing. Marzocchi has the expertise and capabilities to lead the full deployment of a development program, from the conceptual and simulation phase to the full production of gear pumps. Application-engineering skills and aptitude to innovation drive new and repeat sales, proven by an established history of technology development protected through active patents such as that of ELIKA pump.

Strong and long-standing relationships with world class customers generate recurring revenues. In an industry where technology content, reliability, technical support and responsive customer service are key competitive factors, relationships standing from decades and long-term contracts as sole supplier of high performance components for Tier 1 large multinational customers, prove that Marzocchi has competitive advantages among world class competitors, which in turn generated and continue to generate recurring revenue with repeat customers.

Ability to develop custom solutions for complex customer requirements. Large Tier 1 customers incorporate Marzocchi products into the designs of their equipment, through a joint engineering development of an application which will have a long lifecycle. This implies the convenience of having Marzocchi as sole supplier for the entire lifecycle due to high switching costs and a partnership aptitude, which in turn leads to fair pricing.

Global presence. Marzocchi has global presence: two production plants in Italy and two subsidiaries in the US and China. Operating in the proximity of local customers is a key trait of the industry. This means optimizing the supply chain and developing new technologies in partnership with customers.

Visibility of revenues in the mid-term and solid backlog. The customer partnership model allows for high visibility of the top-line, given that the industry standard long-term agreements generally last a minimum of three years. As such, a substantial portion of revenues over the years comes consistently from its loyal customers who assign repeat engagements. This has permitted Marzocchi to gain the status of strategic supplier of those prominent customers who consider its products and services to be crucial for their performance.

Risk management aptitude. The geographical and end markets diversification of revenues and procurement, with low concentration among customers and suppliers, is a major risk management tool to face the cyclicity inherent in most industry segments. Equally effective are quality and performance requirements necessary to monitor and maintain world-class manufacturing standards imposed by customers and in turn dictated to suppliers.

Challenges

Cyclicity in end markets. Some of the markets served by Marzocchi are highly cyclical, such as the machinery, industrial and automotive equipment.

High rivalry in the competitive hydraulic gear pumps industry. Competition in the industry is based on several factors, including product quality, performance, reliability and innovation, technology, design and engineering capabilities, service and timely delivery. As in all industries, companies are committed to reduce costs, and this, in turn, is reverted to suppliers. As such, the ability to compete in the industry depends also on the ability to generate cost savings.

International markets exposure. Revenues coming from foreign operations account for a large portion of revenues. International operations are generally subject to risks, such as political and economic instability, local labor markets, trade relations, imposition of tariffs and other trade restrictions, etc. In addition, foreign operations outside the Euro-area can impact the financial position due to fluctuations in currency exchange rates.

Acquisition and integration risk. As in most industries, size matters and Marzocchi could consider that living in a world of giants may require a larger size. Acquisitions may be pursued to achieve scale growth, diversification, acquire know-how and technology, expand product and customer portfolio. The achievement of expected benefits and synergies requires integration of manufacturing, engineering, administrative, sales and marketing, distribution, information systems platforms and processes. Targeting acquisitions and integration all require additional competencies.

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NEUTRAL: stocks are expected to have a performance consistent with market or industry trend and appear less attractive than Outperform rated stocks;

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The stock price indicated is the reference price on the day indicated as “Date of Price” in the table on the front page of this publication.

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Date	Recommendation	Target Price (€)	Share Price (€)
07/10/2019	OUTPERFORM	6.42	4.63
03/04/2020	NEUTRAL	4.27	3.80
20/10/2020	NEUTRAL	2.90	2.60
25/01/2021	OUTPERFORM	3.61	2.78

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