

HOLDING UPDATE - INTERPUMP SpA

Price	€52.70		
Market Cap	€4.8bn	PE FY2	25.2x
EV	€5.0bn	EV:Sales	3.5x
DY	0.6%	EBITDA Margin	23%



A COLUMBUS TOP 5 HOLDING

Both Pedro and I have known Interpump for well over a decade (actually closer to 2 decades) and we have been investors for much of this period. The reason for this is that the company consistently demonstrates the characteristics we look for in the 'high quality' investments that make up the majority of the Columbus portfolio. These are:

- Clear strategy
- Strong management team with proven ability to allocate capital - leading to
- High, unlevered returns on equity
- Evident leadership characteristics and barriers to competition - demonstrated by high margins and free cash generation
- Significant scope for further growth

I have not included valuation in this list as this is not a characteristic of the company but merely a timing issue in the investment decision.

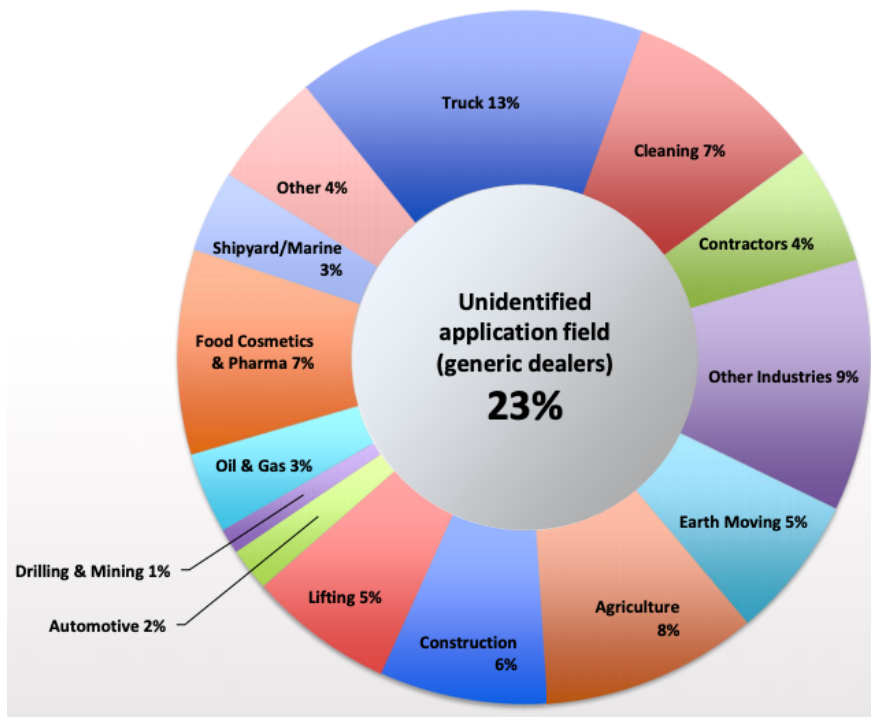
To understand Interpump, as with many quality companies, we need to look at its history.

After the company was founded in 1977 it grew quickly on the back of their highly innovative designs of high-pressure piston pumps, utilising new materials to create smaller and more efficient products than their competitors. This is the culture that the group has taken forward and which took them to be the largest producer of these pumps in the world.

The success of the company led to huge cash generation which the management team put to work acquiring small, specialist companies in engineered products in the hydraulics industry. This allowed them to benefit from their core engineering knowledge and expand into adjacent markets. Fast forward to 2021 and the Group has acquired more than 40 companies since going public in 1996 and have expanded beyond hydraulics into pressure homogenizers and fluid handling components.

By expanding into new areas, they have vastly increased their scope for acquisition as well as created significant opportunities for cross-selling. The result of this strategy has been to provide the group with highly diversified

revenues and a base of ~20,000 customers, helping to reduce the cyclicity of the revenues. It also avoids customer concentration with the largest account representing only 1.4% sales.



Revenue Split by End Market 2020

Source: Interpump IR Presentation Q1 2021

An interesting common aspect of many of the high quality companies in Europe is family ownership. In this case the founder controls close to 25% of the shares both directly and through a listed investment company. This level of family involvement has shown in many examples to lead to better long term capital allocation and investment behaviour. Owners tend to have their eyes on the longer term, rather than the annual bonus or 3 year incentive plan, and this tends to provide better long term returns. This is certainly the case at Interpump where the returns on equity over the past 5 years have averaged ~18%

Over the last decade (since FY 2011) the combination of organic and acquired growth led to a CAGR in revenues of 12% and 16.2% in EPS. This has not been achieved at the cost of the balance sheet however, as net debt:EBITDA actually declined over this period from 1.54x to 1.13, peaking at 1.66x in 2014. (The Group's focus on the financial structure of the business is reflected in the fact that the balance sheet is presented before the income statement in the annual report). Obviously then the growth is driven by the FCF and this has increased by a compound annual growth rate of ~20% over the same period. Margins have also expanded over the Group's history, with EBITDA margins rising from mid-teens in the early 2000's to 23% over the past

Revenue Split 2020



Source: [Interpump](#) IR Presentation Q1 2021

few years. One of the quirks of Interpump is that the company believes in the power of specialist brands which is why, contrary to much received wisdom in corporate finance, they do not typically integrate the companies they buy. Rather they keep them as specialists in their niche and instead provide funding and operational assistance to help them to grow. This maintains their portfolio of niche leaders and reinforces the barriers to competition.

Their M&A strategy in general is somewhat differentiated in that they refuse to buy troubled companies to turn them around, and they refuse to buy from private equity. Their aim is to find family led, niche businesses and help them to transition to a larger platform for growth. Since they do not integrate and aggressively cut costs they are seen as a 'good buyer' and are often the only bidder in the process. For investors that know Judges Scientific in the UK, it is a very similar mentality.

Valuation

It is the combination of the M&A strategy and an average organic growth of ~4% that has provided the 12% CAGR in sales achieved over the past decade. In discussions with management they are confident that they can maintain a similar pace for the foreseeable future as they continue to grow across a number of different product areas. Our model assumes a similar outlook margin in the near term with revenue growth falling quickly to 10% and then fading to a 2% terminal growth in nine years. Assuming a 7% WACC we achieve valuations around €62 per share - about 17% above the current €52.70. Having performed this exercise several times over the years I have found that my assumptions have typically been too conservative. Although the terminal growth rate is low after only 9 more years we prefer to take this approach. No company grows in perpetuity at a rate above GDP and by keeping the a higher portion of the value in the forecast period we can update our target each year and feel confident that the valuation is not slipping too far into the forever.

Benchmarking the current valuation against their closest listed peer, Eaton in the US, we find that Interpump trades at close to a 5 point discount on EV/EBITDA despite similar margins and a higher growth rate. This has typically been the case and results, I believe, partly from the higher multiples generally paid in the US, and partly due to the difference in market cap with the much larger Eaton attracting more attention from analysts.

Risks:

Key man risk - Fulvio Montipo founded the company in 1977 and remains in position as Chairman and CEO. He has overseen the expansion of the group and is a clear figurehead for the culture of the business. At 77 years old this is an obvious issue for the shares. However, we are confident that the business model and culture of the group is sustainable, even without Mr Montipo at the helm and while there may be some turbulence when he decides to leave his post we do not see this as a significant game changer for the company given the strength of the operational team he has put in place.

ESG - Although we are not aware of any significant issues on the environmental side the group would not be held up as an example of good corporate governance given the dual Chairman/CEO role held by the founder and a clear lack of gender diversification on the board. However, while we see and understand this argument we would counter that the structure has been highly successful while maintaining very positive treatment of all stakeholders. The supportive approach to M&A and the stability of the workforce (outsourced manufacturing takes the brunt of swings in demand) suggest that the group pays more attention to governance than they appear to from the outside.

M&A - obviously the majority of the growth over the past two decades has come from acquisitions so in order to maintain a similar rate of growth going forward they will need to continue this record. If for any reason the company is unable to identify and execute on acquisitions the shares would be at risk of derating.

