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April 23, 2024

RS Group plc (LSE:RS1)

Long recommendation

Price target (MoS): £10.4 (31%)

Margin of safety (MOS)		**31%**	**Rationale:**	**Upside (down.)**	**Upside / down. Ratio**		
Target Price	£	10.4	14x normalized EV/EBIT (@12.5% adj. margin)	46%	1.5x	52-w high	£ 10.4
Downside Price	£	5.9	10x normalized EV/EBIT (@10.0% adj. margin)	-18%	0.8x	52-week low	£ 5.5
Target Entry Price	£	7.3	30% Margin of Safety			Price/52w high	69%

(£ in GBP millions except per share)			2019A	2020A	2021A	2022A	2023A	LTM Sept-23	2024E	2025E	2026E	2027E	2028E
Stock Price: (4/23/24)	**£ 7.1**	**Total revenue**	**1,884**	**1,954**	**2,003**	**2,554**	**2,982**	**2,971**	**3,033**	**3,295**	**3,509**	**3,737**	**3,980**
Diluted shares (mn)	472.8	% growth	10.5%	3.7%	2.5%	27.5%	16.8%	-0.8%	1.7%	8.6%	6.5%	6.5%	6.5%
Market Cap	**3,362**	**Adj. EBIT**	**205.4**	**210.7**	**174.2**	**320.4**	**399.6**	**354.9**	**361.1**	**409.3**	**449.6**	**492.6**	**535.7**
(+) Debt	805	Adj. EBIT Margin	10.9%	10.8%	8.7%	12.5%	13.4%	11.9%	11.9%	12.4%	12.8%	13.2%	13.5%
(-) Cash	379	EV/EBIT (adj.)	13.0x	12.2x	28.7x	16.7x	11.6x	10.7x	10.5x	9.3x	8.4x	7.7x	7.1x
(+) Minority interest	0.7	**EPS**	**£ 0.33**	**£ 0.35**	**£ 0.27**	**£ 0.49**	**£ 0.60**	**£ 0.50**	**£ 0.51**	**£ 0.58**	**£ 0.65**	**£ 0.74**	**£ 0.83**
Firm Value	**3,788**	P/E	16.8x	14.9x	35.9x	22.2x	15.1x	14.2x	14.0x	12.2x	10.9x	9.7x	8.6x
EV/EBITDA (LTM)	9.3x	Diluted shares o/s (mm)	446	448	456	473	473	473	474	476	477	479	480
Price/Book Value	2.4x	Capex	51	75	55	18	19	16	49	86	91	97	103
Dividend Yield (FY23)	2.9%	% of sales	2.7%	3.8%	2.7%	0.7%	0.6%	0.5%	1.6%	2.6%	2.6%	2.6%	2.6%
Avg ROIC (5Y / post-tax)	20%	**FCF (CFO - Capex) /Share**	**£ 0.17**	**£ 0.16**	**£ 0.29**	**£ 0.39**	**£ 0.61**	**£ 0.43**	**£ 0.59**	**£ 0.57**	**£ 0.55**	**£ 0.65**	**£ 0.72**
Avg ROTC (5Y / post-tax)	28%	FCF Yield	2.7%	2.4%	2.7%	4.7%	7.6%	6.0%	8.2%	8.0%	7.8%	9.2%	10.1%
		ROIC (post-tax)	**22.8%**	**18.8%**	**13.3%**	**21.1%**	**22.1%**	**13.9%**	**16.4%**	**16.6%**	**17.5%**	**18.5%**	**19.4%**
Debt/Capital	37%	**ROTC (post-tax)**	**29.8%**	**24.8%**	**18.6%**	**31.5%**	**34.1%**	**27.4%**	**29.3%**	**30.9%**	**30.3%**	**30.1%**	**29.8%**
Net Debt/EBITDA	1.0x												
EBIT/Interest Expense	14.0x	**Growth (CAGR)**	**5Y A**	**10Y A**									
Avg 3M Daily Volume($mn)	2.3	Revenues	11.8%	9.2%									
Shares Short (mm)	-	EBIT	17.3%	15.3%									

Long recommendation: I recommend buying RS Group shares at £7.1 with a £10.4 target price. At this price, the stock has 46% upside, 18% downside, and 31% margin of safety.

Executive Summary: RS Group plc is a B2B distributor specializing in industrial and electronic MRO products. It has a long-term ROIC averaging 20%, and they've achieved 9% revenue and 15% EBIT growth over the past decade. What drives this business is their pricing power, derived from serving industrial clients with a wide range of products in small and frequent orders (around £250 every month). These crucial products support manufacturing operations, requiring rapid one-day delivery and technical sales assistance because downtime cost is extremely expensive for their customers, making availability rather than price the key factor.

My investment thesis is the following:

1. Ongoing transition from product provider to solution provider, leading to increased customer captivity. Currently, 25% and 63% of revenues come from services and digital channels, respectively, far outperforming peers.
2. Although adj. EBIT [1] margins are retreating from record highs (13.4% to 11.9%) following supply chain bottlenecks, they should improve in the medium term due to higher private label penetration (13% now to 20% in 2028E, which would improve gross margins by 140 bps) and operating leverage as fixed costs (70% of SG&A expenses) are diluted per unit, implying a margin expansion of 30 bps per year if the business grows revenues by 10%.
3. Continued consolidation and pricing power from larger players in a highly fragmented industry with a huge TAM opportunity ($500bn), allowing RS Group to grow revenues 300-400 bps above the industry's organic growth rate (4-6%).
4. Fears over recent management changes (CEO, CFO + others) after a successful cycle have raised doubts. I believe the new management team will succeed in implementing the strategy set by the former CEO.

Key Questions / Factors:

- The market expects 2004 FY to be difficult, which has led to a sharp drop in the share price. To what extent has this affected price vs value? Is there substantial upside from a margin expansion perspective after the correction?
- Will the new management team be able to continue the success cycle of the last CEO?

Valuation: I valued the stock at £10.4 in my base case. I arrived at this value using a 14x forward EV/EBIT (adj.) multiple and normalized adj. EBIT margin of 12.5%.

[1] Adj. EBIT = EBIT + Amortization of intangibles from M&A.

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The multiple used is reasonable for two reasons: i) it is consistent with RS Group's historical average of 14.2x EV/EBIT forward (2013 - 2023), and ii) it is conservative for a company that compounds NOPAT at high rates - ~13% estimated CAGR if they can reinvest 50% of adj. NOPAT - and has high returns on invested capital (~20%).

I estimate that buying the stock at the current price of £10.4 has a 26% 5-year IRR in my base case (19% IRR without multiple expansion). Interestingly, the market is giving you attractive growth for free, as the stock trades in line with its earnings power value, estimated at £7.0 / share.

Peers are trading at a median of 16.9x trailing EV/EBIT, while RS Group trades at 11.3x trailing EV/EBIT (vs average of 16.3x), so today's multiple sits at the bottom of the observed range. Note that RS Group has better margins and returns on capital than the average peer group.

In summary, the stock looks cheap when valued from different angles, has high upside potential and limited risk from a downside perspective.

Business and Industry Description:

RS Group plc (formerly Electrocomponents) is a high service B2B distributor of industrial and electronic products. They provide the link between suppliers and industrial customers who buy many different products in small volumes for the maintenance, repair, and operation (MRO) of their businesses. RS Group also offers service solutions for industrial customers (25% of revenues) and has a strong presence in e-commerce (63% of revenues vs 20% industry-wide), helping clients to simplify their purchasing process and manage inventory more efficiently. Additionally, its private label brand – RS Pro – accounts for 17% of the revenues. Headquartered in London, the company operates in around 30 countries. EMEA accounts for 59% of revenues (40% of that in the UK), the Americas division 32% (most of it in the US) and Asia-Pacific 9%. Its end-users are mainly design engineers and panel builders at OEM's R&D departments, and production, procurement, and maintenance managers at MROs. End-markets are correlated to the PMI index.

The B2B industrial distribution industry is highly fragmented (top 50 players have 30% - 40% market share only), is growing at rates of 4 – 6% (above developed countries GDP) and is seeing recent consolidation from larger players that have been able to grow 3 – 5pp above the organic growth rate because they can outgun the small guys from a cost perspective. The global TAM is somewhere between \$500 – \$1,000 bn, so that leaves **RS Group with a market share below 0.5%** (their highest market share is in the UK with 5%). Large players - who still have a low market share - usually **enjoy returns well above their cost of capital**. Companies don't target the entire TAM, but rather focus on a few specific end-users (e.g., manufacturing, OEMs, commercial, electronics, electrical, food packaging, safety, healthcare, plumbing, among others). They source products from multiple suppliers and have very low customer concentration.

One of the advantages of the company is having a consistent strategy, which has allowed them to execute with a long-term vision and build long-lasting client relationships. The main pillars of the strategy are the following: i) gain scale in the MRO business, lowering exposure to electronics (which tends to be much more cyclical), ii) improve digitalization and customer experience, and iii) expand their product and service solutions (currently 700k SKUs in inventory + >2M products distributed directly from supplier's inventory).

The competitive advantages of the company stem from how the industry operates, meaning that they are shared by the larger players. This is how it works:

- **Having the products in stock and available when the customers need them is the key to winning the game**, so the competition is on availability, not price, even though the products themselves are commoditized. RS Group excels at this, as mentioned by a former executive: "*In the US you can place your order up to 10pm and have it delivered the next day 8am.*"
- Customers have a heavy IT integration with vendors. For example, with e-procurement tools customers order directly from their ERP software. Therefore, they prefer to work with 2 or 3 vendors maximum, who try to maximize the wallet-share from that customer. **This creates a very sticky relationship with high switching costs,** with no space for a 3rd or 4th vendor entry in that business relationship.
- To have your products always available, you need to invest in a large inventory from various suppliers, distribution centers, online platforms and rely on regional sales and technical reps to build long-lasting business relationships. **Economies of scale are present** because as you put more volume into the business, you can purchase at lower prices from suppliers, dilute your fixed costs and leverage the network of sales reps. We observe larger players having a lower SG&A / revenues ratio.
- Companies have been shifting towards complementary services (e.g., strategic sourcing, transactional processing, inventory optimization) to **increase customer captivity** and cross-selling.

Investment thesis

IT #1: Ongoing transition from product to a solutions provider leading to higher customer captivity.

One trend in the industry is customers looking for digitalized options that can make their inventory management easier, eliminating labor costs from low value and repetitive processes that can be automated. As RS Group continuously shifts their focus from being a product distributor to becoming an omni-channel end-to-end one stop specialist product and value-added service (VAS) provider, they will enhance customer stickiness and boost their wallet-share capture. A study conducted by the company with UK customers shows that when they purchase a VAS, the revenue growth rate from that client increases by 1pp (approximately 4% revenue growth without VAS, 5% with 1 VASs and 6% with 2 VASs). Currently, 75% of customers don't have a VAS, leaving plenty of space for deployment.

IT #2: Private label penetration plus operating leverage should improve operating margins.

One of the company's initiatives is to increase the penetration of RS Pro, a private label brand of MRO products of identical quality to branded products, but at a much lower price. This brand has experienced faster growth than the branded products. The company does not disclose differentiated gross margins for RS Pro versus branded products, but my primary research suggests that **RS Pro has a gross margin of ~60%**, while the group figure last year was 45.3%. In addition, revenue excluding services appears to have a gross margin of ~40%, so I could also get an estimate of gross margins for services solutions. They may not be extremely accurate, but they are probably heading in the right direction. Also, since RS Pro was recently launched in the US, it has very low penetration (1%), so catching up with the other geographic segments plus some continued growth in other regions should **boost gross margins by 140 bps over normalized levels by 2028.**

			Private label share	
	2023A Rev.	Rev. Share	Actual	Target '28
EMEA	1,769	59%	19%	22%
America	946	32%	1%	15%
Asia - Pac	268	9%	14%	17%
TOTAL	2,982	100%	13%	19%

Gross margin analysis	2023 Gross margin	Adjustment	Norm. Gross mg.	2023 Rev. Breakdown	2028E Gross mg.	2028E rev. breakdown
Private label	60.0%	-1.1%	58.9%	13%	58.9%	19%
Non private label	36.5%	-1.1%	35.4%	63%	35.4%	56%
Products	40.5%		39.4%	75%	41.3%	75%
Service solutions	60.2%	-1.1%	59.1%	25%	59.1%	25%
Company	**45.3%**		**44.2%**	**100%**	**45.7%**	**100%**
Improvement			-1.1%		1.4%	

Secondly, the company has had an operating leverage of 1.7x on average during the last 10 years. This translates into 60bps of EBIT margin improvement every 10% growth in revenues. To exclude the effect of change in gross profits, one can look at the history of SG&A expenses over revenues. **The ratio has been decreasing since 2006 by 60bps per year on average.** I've assumed only 30bps in my projections to be conservative.

Larger peers like W.W. Grainger, Ferguson and Bunzl have a much lower ratio of SG&A / Revenues (~20%). Given RS Group lower revenue base, I don't expect them to reach that figure, but we should see improvements.

Overall, I expect adj. EBIT margins to normalize at 11.9% in FY'24 (from 13.4% in FY'23) and then to reach 13.5% in FY'28.

IT #3: Further consolidation and pricing power will enable growth above the industry's organic growth rate.

Because pricing ranks low in customers' order of importance (top 3 that came up in primary research were range of products, product availability, and customer service), they should be able to grow above inflation just by rising prices. Organic real growth should also be above the industry's because they generate substantial operating cash flow that can be invested in new distribution centers and extended inventory. Also, customers are increasingly preferring larger companies that can better serve their needs with a broad set of solutions.

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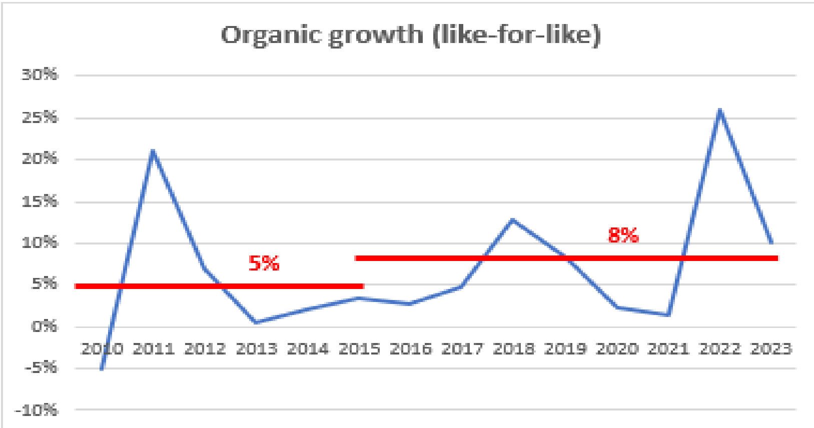

During Lindsley Ruth's tenure leading the company, organic revenue grew 8%. I believe they can conservatively grow organic revenue at a 7.0% rate, assuming the lower end of industry growth and market share growth (4% and 3%, respectively), by investing in inventory, new distribution centers, expanding the customer network and gaining share of wallet.

In addition to organic growth, the sector has experienced some consolidation by the major players and this is likely to continue. This seems logical in a highly fragmented industry with high returns on capital by the large operators.

RS Group started doing M&A in 2019, totaling £850M since then. When talking with a former M&A associate of RS Group, he described the company as very intentional when dealing with M&A, placing fit before financial considerations, and excellent at operational integration. This intentionality even led them to be too slow when performing due-diligence and letting many opportunities go (he described the work to be frustrating many times because of the slow pace). Although my financial forecast don't consider any M&A as the excess cash flows go to pay down debt, I'd expect the company to grow revenues inorganically at a rate of 3% - 4%.

IT#4: New management team fears are oversold.

During the last two years, there's been numerous changes in senior management, including the CEO, CFO, COO, CFO APAC, and President of RS Americas. This has naturally affected the stock price as it's perceived as a generalized turmoil inside the company. Even though it was unfortunate to see the former CEO Lindsley Ruth depart after a successful management cycle, I believe that i) Simon Pryce, the new CEO, knows the company extremely well, has the competence to lead the business and the ability to execute the sound long-term strategy the company has in place, and ii) that all the management changes were independent issues (although some for better reasons than others).

To put it in context Lindsley Ruth arrived in 2015 when the company was underperforming – i.e., low EBIT margins (~7%) and almost no topline growth during the last 4 years **(although ROIC was still considerably above cost of capital)** – and he put into place the Performance Improvement Plan. He completely changed the culture of the company, aligned incentives by rewarding employee outperformance, and substantially improved the financial results.

Unfortunately, he abruptly decided to resign because of work/life balance stress and some medical issues. I was able to confirm this when talking to a former employee who is a close friend of Lindsley's son. On top of that, the CFO resigned over a relationship with a colleague, the COO after a McKinsey internal study that concluded the regional operational structure made the global COO role redundant, and the President of RS Americas after he received an offer to become the CEO of a pesticide / herbicide distributor. Although not great news for the company, it lowers the probability that something generalized had occurred that is not public knowledge.

In April 2023, Simon Pryce was appointed as the new CEO. At that time, he had been a non-executive board member for 6 years at RS Group, so he knew the company quite well. He is a seasoned leader of global industrial manufacturing and service companies. Most recently, Pryce was CEO of Ultra Electronic Holdings plc for four years, which was acquired by Advent in August 2022. Ultra was a client of RS Group, so Pryce also knew the company from the customer's perspective. During his tenure, the company increased EBIT margins from 10.2% to 13.3% and grew it at a 13% CAGR after being stagnant for more than 7 years, while the stock went from ~$15 to ~$35. The company had a long-term history of terrible acquisitions, and he did none of them, focusing on organic growth and cost efficiencies. On an interview with Mckensey in 2021 he said *"Growth, for me, is about taking managed risks in areas where you are truly expert and competitive. It's no more complicated than the much-used Warren Buffett analogy of castles and moats."* Prior to Ultra, he held the role of CEO at BBA Aviation plc for 10 years.

On other key positions, Douglas Moodey was appointed as President of RS Americas in November 2022, promoted from Chief Services Officer. A primary research quote from a former executive mentioned *"He is a stud - he's exactly what RS Americas needs from a strategic perspective as they progress towards an end-to-end industrial solutions provider"*. Also, Kate Ringrose was appointed as CFO

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in October 2023, after being the CFO for 2 years at Centrica plc, an $8bn publicly listed energy company. She worked 19 years at the company.

Risks

- New management execution risk: Potential misallocation of capital by the new CEO and the risk of key talent departing with the leadership changes.

- Slower-than-expected end-user market growth impacting on volumes and margins over the next two years.

- Disruption risks: While supplier disintermediation and Amazon's entry into the market are possibilities, they remain unlikely due to suppliers' limitations in dealing with numerous small customers and Amazon's inability to provide the necessary industrial client service and customization, proving unsuccessful since they tried to enter the market in 2010. Additionally, the effort required for Amazon to capture some market share in a fragmented industry may not be worthwhile for a company with $550 billion in revenues.

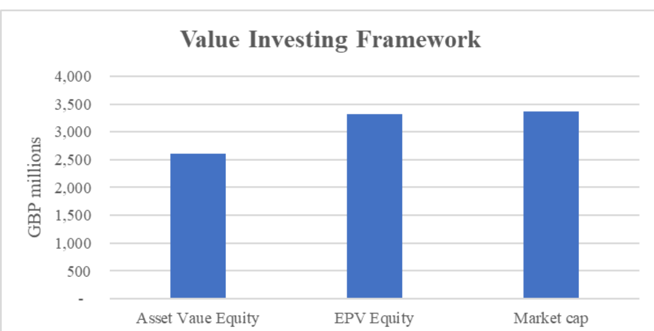
Pre-mortem – where I can be wrong:

Too optimistic: i) Assuming that margins will trend upwards once stabilized, ii) Amazon not having a chance in this business, iii) this will be a story of GDP-like growth only, and iv) management lack of skin in the game leads to underperforming.

Too pessimistic: i) SG&A / revenues ratio improving just marginally and not even close to best-in-class peers, ii) not considering M&A given they have a dedicated team and a successful track record of integration, and iii) projecting organic growth below last management's cycle and target of 11.2% for performance bonus.

Bear case: EBIT margins stabilize at 10% and organic growth of 3.0% from 2024 onwards, while the stock derates to 10x EV/EBIT (adj.), implying a price of £5.9 and 18% downside.

Applying the Value Investing framework



Return component	Base case	Downside case	Upside case
Distribution yield	3.8%	4.7%	2.9%
Organic growth	4.0%	4.0%	4.0%
Inorganic growth	9.4%	3.4%	13.2%
Multiple	6.7%	-3.9%	12.9%
Expected return (unl.)	**24.0%**	**8.2%**	**33.0%**
Expected return (lev.)	**26.2%**	**9.0%**	**36.2%**
Plowback ratio	50.0%	40.0%	60.0%
ROIC	18.8%	8.5%	22.0%
Exit EV/EBIT multiple	14.0x	8.8x	18.0x

By looking at the chart in the left, we can conclude two things:

1. Confirm that RS Group has barriers to entry as shown by earnings power value above asset value.
2. Observe the attractiveness of the investment opportunity since the market gives us growth for free when the company is well positioned to continue deploying capital at high rates of return.

The table below the chart shows my return estimates for the next 5 years. The current EV/EBIT forward multiple is 10.5x.

My base case conservatively assumes a plowback ratio slightly below the historical average (50% vs 60%), ROIC in line with the period 2018 – 2023, and the stock rerating to 14x EBIT, for a 24% and 26% unlevered and equity return respectively.

My downside case assumes ROIC = cost of capital, and multiple derating to 8.8x EBIT, the lowest observation in the last 10 years. The distribution yield slightly improves as I use a lower plowback ratio. **This scenario shows robust downside protection, as even under poor assumptions we obtain a 9% equity return.**

* Refer to appendix 4 for a detailed analysis of AV and EPV.

Sources of information: VAR (two interviews with former M&A associate and head of e-commerce Asia-Pacific), Tegus industry experts' interviews with RS Group and W.W Grainger, earnings reports transcripts, CIQ and IR official files.

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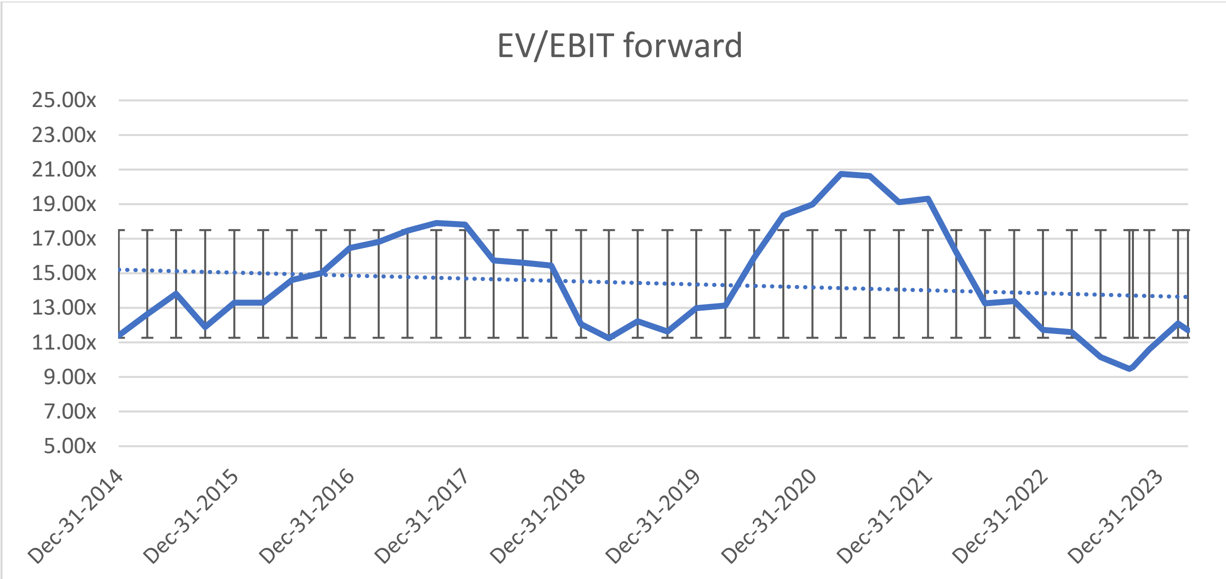
Appendix

Appendix 1: Valuation multiples and peer analysis



	2023 A					Last 5 years average		
Company name		**Revenues**	**Gross margin**	**EBIT margin**	**ROIC b/tax**	**Gross margin**	**EBIT margin**	**ROIC b/tax**
W.W. Grainger	$	16,547	39.5%	15.5%	45.0%	37.7%	13.2%	36.7%
Bunzl plc	£	11,926	25.3%	7.6%	14.1%	24.9%	6.3%	8.9%
Diploma plc	£	1,200	38.1%	16.3%	16.8%	36.8%	14.8%	18.2%
DCC plc	£	20,984	10.8%	2.6%	9.6%	11.7%	2.8%	9.7%
DKSH Holding AG	$	11,356	8.3%	2.8%	12.3%	8.1%	2.5%	11.8%
Fastenal Co	$	7,347	45.6%	20.8%	37.8%	46.1%	20.4%	35.9%
MSC Industrial Direct	$	4,009	41.0%	12.3%	23.2%	41.8%	11.8%	20.5%
Azelis Group	$	4,231	22.9%	9.7%	9.8%	22.2%	8.0%	8.1%
Ferguson	$	29,511	22.9%	9.1%	27.7%	30.3%	8.4%	24.0%
Mean		11,901	28.3%	10.7%	21.8%	28.9%	9.8%	19.3%
Median		**11,356**	**25.3%**	**9.7%**	**16.8%**	**30.3%**	**8.4%**	**18.2%**
High		29,511	45.6%	20.8%	45.0%	46.1%	20.4%	36.7%
Low		1,200	8.3%	2.6%	9.6%	8.1%	2.5%	8.1%
RS Group plc		**2,982**	**45.3%**	**12.8%**	**24.5%**	**44.1%**	**10.9%**	**22.0%**

Company name	**Ticker**		**Market cap**		**EV**	**Avg ROIC 5 years b/tax**	**EV/EBIT trailing**	**EV/EBIT forward**	**EV/EBIT avg 10y**	**% 52-week high**
W.W. Grainger	NYSE: GWW	$	47,765	$	50,207	36.7%	19.6x	18.5x	14.2x	93.1%
Bunzl plc	LSE: BNZL	£	10,366	£	12,021	8.9%	13.3x	13.0x	17.7x	93.4%
Diploma plc	LSE: DPLM	£	4,800	£	5,141	18.2%	26.3x	19.5x	24.0x	92.6%
DCC plc	LSE: DCC	£	5,399	£	6,995	9.7%	12.6x	10.2x	17.7x	93.3%
DKSH Holding AG	SWX: DKSH	$	3,998	$	4,384	11.8%	13.9x	12.6x	16.6x	85.6%
Fastenal Co	Nasdaq: FAST	$	39,005	$	39,318	35.9%	25.7x	24.0x	19.6x	86.3%
MSC Industrial Direct	NYSE: MSM	$	5,250	$	5,824	20.5%	11.8x	12.0x	12.7x	88.0%
Azelis Group	ENXTBR:AZE	$	5,375	$	6,898	8.1%	16.9x	16.2x	N/A	95.1%
Ferguson	NYSE: FERG	$	42,787	$	47,307	24.0%	17.6x	16.8x	13.7x	93.7%
Mean						19.3%	17.5x	15.9x	17.0x	91.2%
Median						**18.2%**	**16.9x**	**16.2x**	**17.2x**	**93.1%**
High						36.7%	26.3x	24.0x	24.0x	95.1%
Low						8.1%	11.8x	10.2x	12.7x	85.6%
RS Group plc	**LSE: RS1**		**3,362**		**3,788**	**22.0%**	**9.9x**	**11.3x**	**16.7x**	**66.8%**

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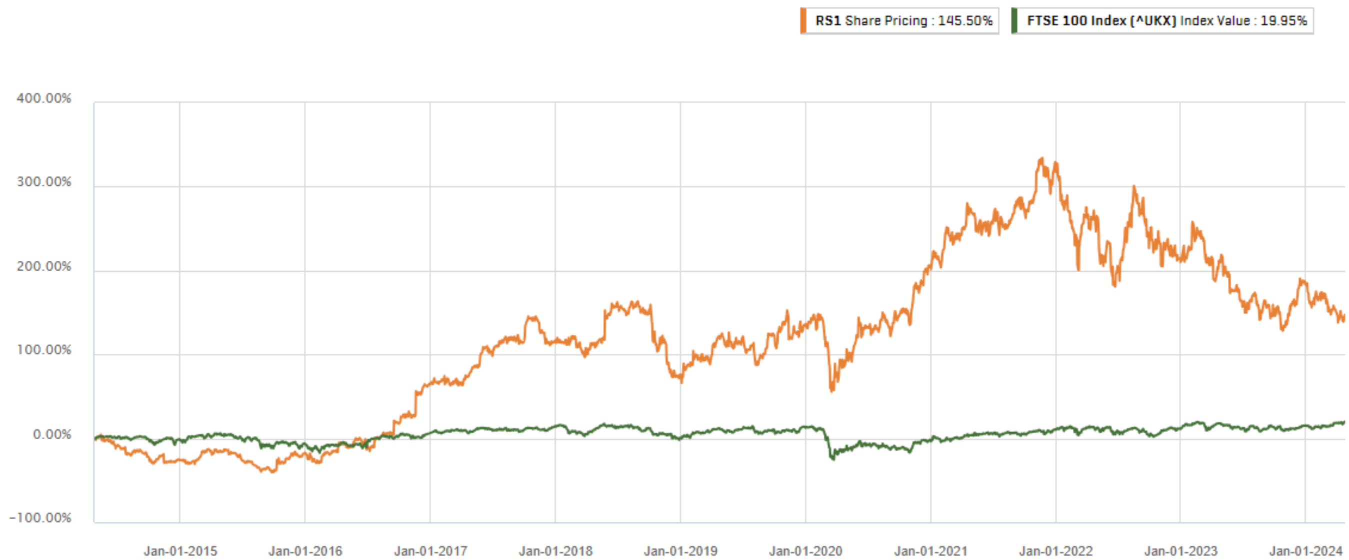
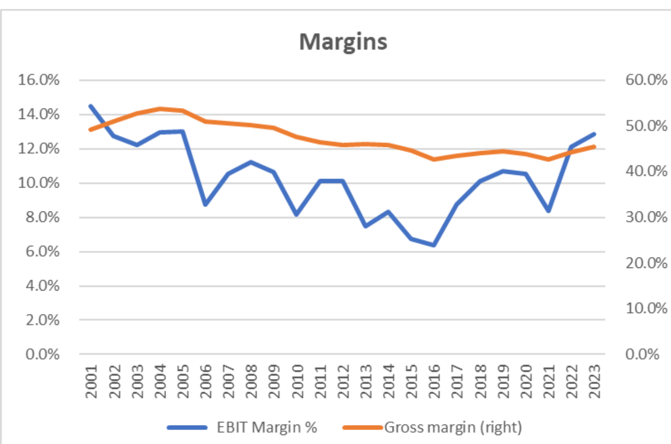
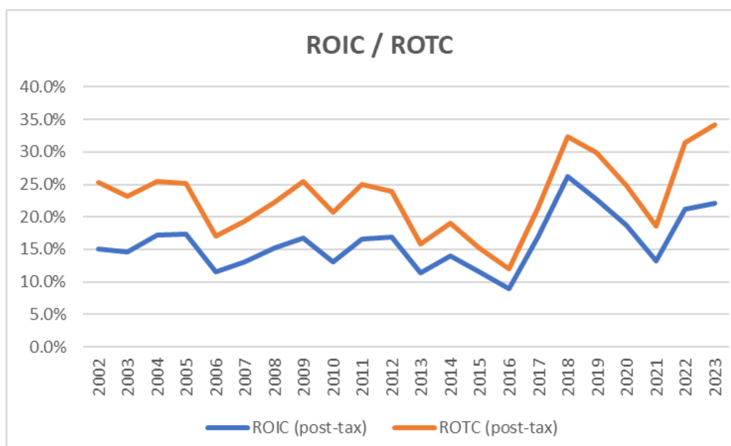
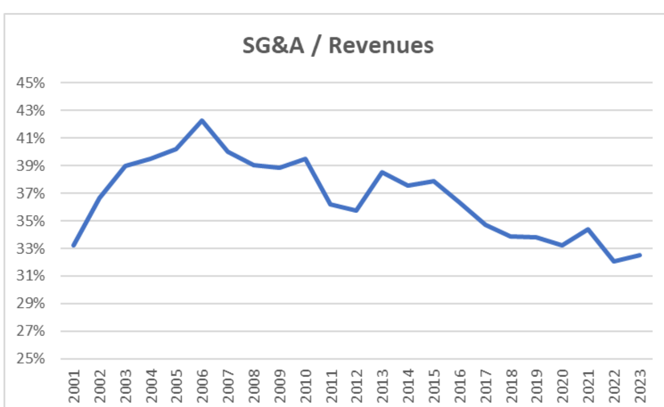
Appendix 2: Stock performance



Appendix 3: Margins and returns on capital







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Appendix 4: Value Investing Framework (AV and EPV)

Asset Value

Item	GBP mn	Rationale
Book value of equity	1,396	As of 9/30/2023
PPE adj.	-	No required adjustments
Inventory adj.	-	No required adjustments
Brand value	1,182	15 years amortization period. Mkt expense capitalized at 8.6% WACC
Product portfolio	391	4 years amortization period.
Goodwill adj.	(365)	Maintained Risoul and Distrelec's goodwill as they are recent acquisitions.
AV of equity	**2,605**	

Earnings Power Value

		Rationale
Revenues (trailing)	2,982	2023 A
Revenue growth (t+1)	1.7%	2024 revenue growth rate estimate
Revenues (forward)	3,033	
Norm. EBIT margin	11.0%	Average last 5 years
Norm. EBIT	334	
(+) Amort intangibles M&A	30	2024 E. Accounting cost (not economic)
(+) Growth marketing exp	18	15 years brand amortization period
(+) Growth R&D exp	57	4 years R&D amortization period
Maint Capex adj.	(14)	1.3x depreciation
Adj. EBIT	425	
Tax rate	25%	Consistent with future estimates
Adj. NOPAT	319	
Discount rate	8.5%	
EPV Assets	3,750	
(-) Debt	805	
(+) Cash	379	
(-) Minority interest	1	
EPV Equity	3,324	
Diluted shares	473	
EPV stock	7.0	

Appendix 5: Management compensation and Insiders Holdings

Symon Price (CEO) has bought 0.6 mn pounds of shares during 2023, owning 1.0 mn pounds in total. Although he has little stake in the game compared to his salary, this is natural, as he was recently appointed CEO (April 2023). He is obliged to own shares worth 400% of his base salary, so I would like to see him more aggressive with the current valuation.

CEO compensation:

- Basic salary: £750,191 per annum.
- Annual bonus: a maximum bonus opportunity of 150% of basic salary. A third of the total bonus payment will be delivered in the form of deferred shares in the Company. Formula for annual bonus as below:

Component	Weight	Target
Like-for-like revenue growth	35%	11.2%
Adjusted free cash flow	10%	£186.6
Net promoter score (customer satisfaction index)	10%	50.5
CO2 reduction	10%	8%
Adjusted profit before taxes	35%	£361.6

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- Long Term Incentive Plan: up to 250% of basic salary, vesting after three years.
  - Components are: 50% EPS and 50% TSR (shareholder return vs peers)
  - **If ROCE is lower than 20%, the committee has the discretion to reduce the incentive.**
- J2G LTIP Award: Up to 355k shares in 2025 (£2.2mn at the current stock price). Subject to similar rules than the Long-Term Incentive Plan, although EPS weight 70%.

Appendix 6: Financial projections (projections don't consider M&A to be conservative)

Financial Model Figures in GBP million	Unit	2019A	2020A	2021A	2022A	2023A	2024E	2025E	2026E	2027E	2028E
Income Statement											
Revenues		1,884	1,954	2,003	2,554	2,982	3,033	3,295	3,509	3,737	3,980
COGS		(1,046)	(1,099)	(1,147)	(1,426)	(1,630)	(1,693)	(1,828)	(1,937)	(2,051)	(2,173)
Gross profit		839	855	856	1,128	1,352	1,341	1,466	1,572	1,685	1,807
Dist. & marketing		(580)	(596)	(630)	(756)	(890)	(925)	(1,000)	(1,060)	(1,123)	(1,190)
G&A		(58)	(53)	(59)	(64)	(80)	(85)	(87)	(88)	(88)	(88)
EBIT		201	205	167	309	383	331	379	425	475	529
EBT		195	200	161	302	372	318	370	420	476	539
Income tax exp.		(47)	(45)	(35)	(72)	(87)	(76)	(92)	(109)	(124)	(140)
Net profit		**148**	**155**	**126**	**230**	**285**	**241**	**277**	**311**	**352**	**399**
Avg # diluted shares	M	446	447	456	473	473	474	476	477	479	480
EPS diluted	x100	33.2	34.6	28	49	60	51	58	65	74	83
EBITDA		233	256	224	373	448	422	475	520	567	615
Amort. of acq. Intang.		4	5	7	12	17	30	30	25	18	6
Adj. EBIT		205	211	174	320	400	361	409	450	493	536
YoY Growth											
Revenues			3.7%	2.5%	27.5%	16.8%	1.7%	8.6%	6.5%	6.5%	6.5%
EBIT			2.1%	-18.6%	84.7%	24.0%	-13.7%	14.6%	12.1%	11.8%	11.5%
Net income			4.5%	-18.9%	83.3%	23.8%	-15.3%	14.9%	12.0%	13.4%	13.2%
Margins											
Gross		44.5%	43.7%	42.7%	44.2%	45.3%	44.2%	44.5%	44.8%	45.1%	45.4%
EBIT		10.7%	10.5%	8.3%	12.1%	12.8%	10.9%	11.5%	12.1%	12.7%	13.3%
Adj. EBIT		10.9%	10.8%	8.7%	12.5%	13.4%	11.9%	12.4%	12.8%	13.2%	13.5%
EBITDA		12.4%	13.1%	11.2%	14.6%	15.0%	13.9%	14.4%	14.8%	15.2%	15.5%
Net income		7.9%	7.9%	6.3%	9.0%	9.5%	8.0%	8.4%	8.9%	9.4%	10.0%
Cash Flow Statement											
EBITDA		233	256	224	373	448	422	475	520	567	615
(-) Net cash interest exp.		(6)	(6)	(8)	(7)	(13)	(14)	(10)	(5)	1	9
(-) Cash taxes		(51)	(75)	(35)	(57)	(94)	(76)	(92)	(109)	(124)	(140)
(-) WK Inv.		(65)	(50)	29	(102)	(110)	(17)	(30)	(65)	(52)	(57)
(+) Share-based comp.		8	3	7	10	14	12	14	16	18	20
Estimated CFO		**119**	**129**	**216**	**217**	**246**	**326**	**357**	**356**	**410**	**448**
Other adjustments		8	18	(28)	(14)	61	-	-	-	-	-
Reported CFO		**127**	**147**	**188**	**203**	**307**	**326**	**357**	**356**	**410**	**448**
Acquisitions		(33)	(0)	(136)	2	(225)	(365)	-	-	-	-
Capex		(51)	(75)	(55)	(43)	(19)	(49)	(86)	(91)	(97)	(103)
Intangible inv.		-	-	-	-	(28)	-	-	-	-	-
Sale of PP&E		-	-	-	-	0	-	-	-	-	-
CFI		**(84)**	**(75)**	**(190)**	**(40)**	**(271)**	**(414)**	**(86)**	**(91)**	**(97)**	**(103)**
Capital issuance		3	2	180	3	5	-	-	-	-	-
Share repurchases		(2)	(1)	(2)	(3)	(2)	(2)	(2)	(2)	(3)	(3)
Debt issuance		98	163	-	-	83	100	(70)	(78)	(81)	(92)
Debt payment		(71)	(193)	(41)	(19)	(77)	-	-	-	-	-
Dividends		(59)	(69)	(71)	(76)	(89)	(95)	(109)	(122)	(138)	(156)
Other		-	3	-	-	-	-	-	-	-	-
CFF		**(31)**	**(96)**	**66**	**(95)**	**(80)**	**4**	**(181)**	**(202)**	**(222)**	**(251)**
Free cash flow		77	72	133	161	260	278	271	265	313	344
FCF/share		0.17	0.16	0.29	0.34	0.55	0.59	0.57	0.55	0.65	0.72

RS Group plc (LSE:RS1)

Long recommendation

Price target (MoS): £10.4 (31%)

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April 23, 2024

Financial Model											
Figures in GBP million	Unit	2019A	2020A	2021A	2022A	2023A	2024E	2025E	2026E	2027E	2028E
Balance Sheet											
Current assets						232					
Cash & equivalents		129	201	198	258	260	177	267	329	420	513
Inventories		387	419	420	530	616	649	676	690	731	774
Receivables		415	407	494	594	692	706	722	769	819	872
Derivative assets		3	4	2	2	2	2	2	2	2	2
Income tax receivables		2	14	21	12	20	20	20	20	20	20
Total current assets		**936**	**1,044**	**1,135**	**1,395**	**1,590**	**1,554**	**1,687**	**1,810**	**1,991**	**2,181**
Non-current assets											
Intangibles		321	330	466	473	705	1,015	958	905	857	819
PP&E net		120	168	170	177	186	198	245	294	346	402
Right-of-use assets		-	54	59	46	47	47	47	47	47	47
JV investments		1	1	1	1	2	2	3	4	4	5
Deferred tax assets		16	17	10	5	7	7	7	7	7	7
Other		6	4	5	3	7	7	7	7	7	7
Total non-current assets		**463**	**573**	**711**	**706**	**954**	**1,277**	**1,267**	**1,264**	**1,269**	**1,287**
Total assets		**1,399**	**1,618**	**1,846**	**2,101**	**2,544**	**2,831**	**2,954**	**3,073**	**3,260**	**3,467**
Current liabilities											
Payables		385	359	475	584	659	689	701	697	735	775
ST debt		78	174	112	100	140	170	142	111	78	42
Operating leases		-	15	17	17	15	15	15	15	15	15
Income tax liabilities		17	18	20	20	22	22	22	22	22	22
Other		8	5	7	6	4	4	4	4	4	4
Total current liabilities		**488**	**570**	**632**	**726**	**839**	**899**	**883**	**848**	**854**	**857**
Non-current liabilities											
Other payables		11	6	7	7	9	9	9	9	9	9
Retirement benefit oblig.		84	58	57	13	37	37	37	37	37	37
LT debt		175	162	147	152	185	255	213	166	117	62
Operating leases		-	41	44	32	34	34	34	34	34	34
Provisions		2	2	2	3	5	5	5	5	5	5
Deferred tax liabilities		50	59	58	60	90	90	90	90	90	90
Total non-current liabilities		**323**	**327**	**315**	**267**	**360**	**430**	**388**	**342**	**293**	**238**
Total liabilities		**810**	**898**	**946**	**993**	**1,199**	**1,329**	**1,272**	**1,189**	**1,147**	**1,095**
Total equity		**589**	**720**	**899**	**1,109**	**1,345**	**1,502**	**1,682**	**1,884**	**2,113**	**2,372**
Total liabilities + equity		**1,399**	**1,618**	**1,846**	**2,101**	**2,544**	**2,831**	**2,954**	**3,073**	**3,260**	**3,467**
Check		-	-	-	-	-	-	-	-	-	-
Debt		253	335	260	251	324	425	354	277	196	104
Net debt		124	135	62	(7)	64	248	88	(53)	(224)	(409)
Net debt / EBITDA			0.5x	0.4x	0.1x	0.1x	0.4x	0.4x	0.0x	-0.2x	-0.5x
Invested capital		770	913	1,021	1,178	1,498	1,840	1,869	1,937	2,001	2,083
Tangible capital		573	688	665	781	921	952	1,036	1,157	1,269	1,388