



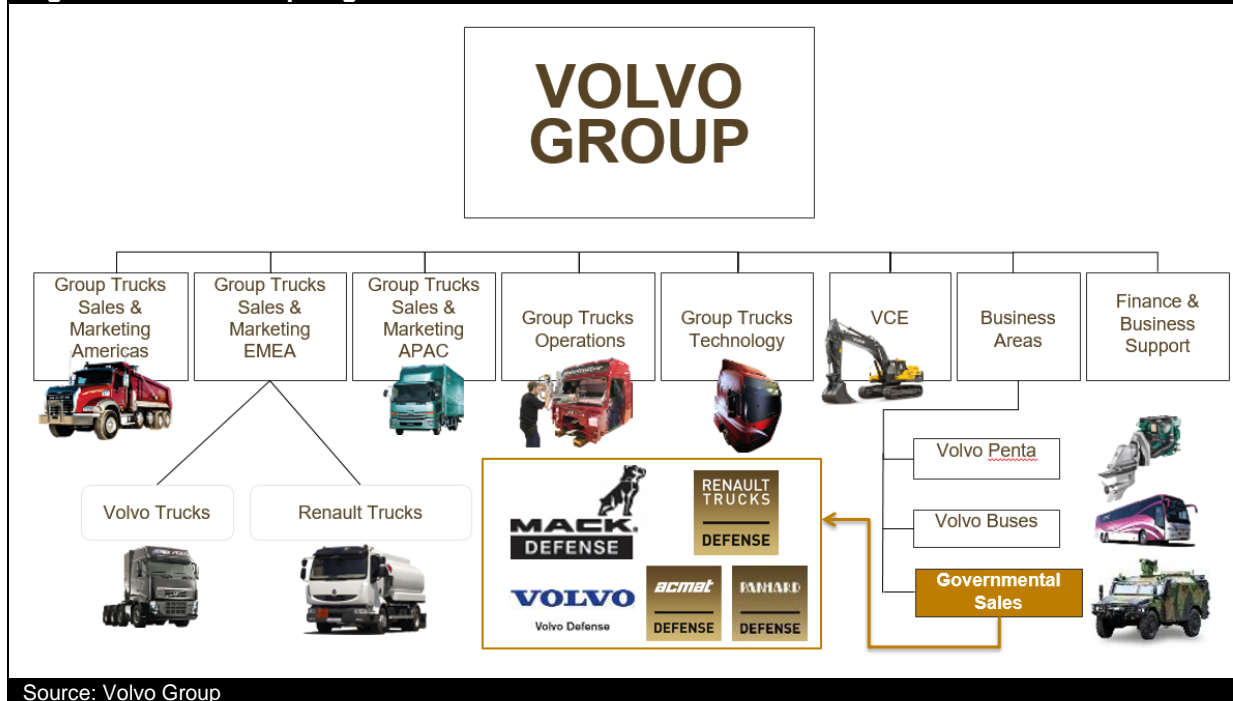
Company Analysis

Renault Trucks Defense valued at 772 million of euros?

OVERVIEW

With more than a century of mastery in armoured military vehicle manufacturing, Renault Trucks Defense's (RTD) know-how stems from its long-lasting cooperation through its various brands with the French Armed Forces. Even though Renault was involved in military production from the dawn of World War I, the group's defence activities were merged with their miscellaneous civilian activities. The military activities were later on assumed by Renault Véhicules Industriels (RVI) alongside the group's truck production. Created in 1978 following a core restructuring, RVI coincided with an era of commercial expansion for Renault military products with the flagship success of the VAB and its 5,000 units delivered worldwide. In 2001, Renault sold ownership of RVI (which consequently became Renault Trucks) to Volvo Group, with its pertaining defence activities renamed Renault Trucks Defense (RTD). Since then under Swedish leadership, RTD initiated a growth strategy based on the purchase of several sector competitors such as ACMAT in 2006 and Panhard in 2012. This strategic shift towards a more diverse commercial offering strengthened RTD's market position, influencing a consolidation of the land defence industry in Europe.

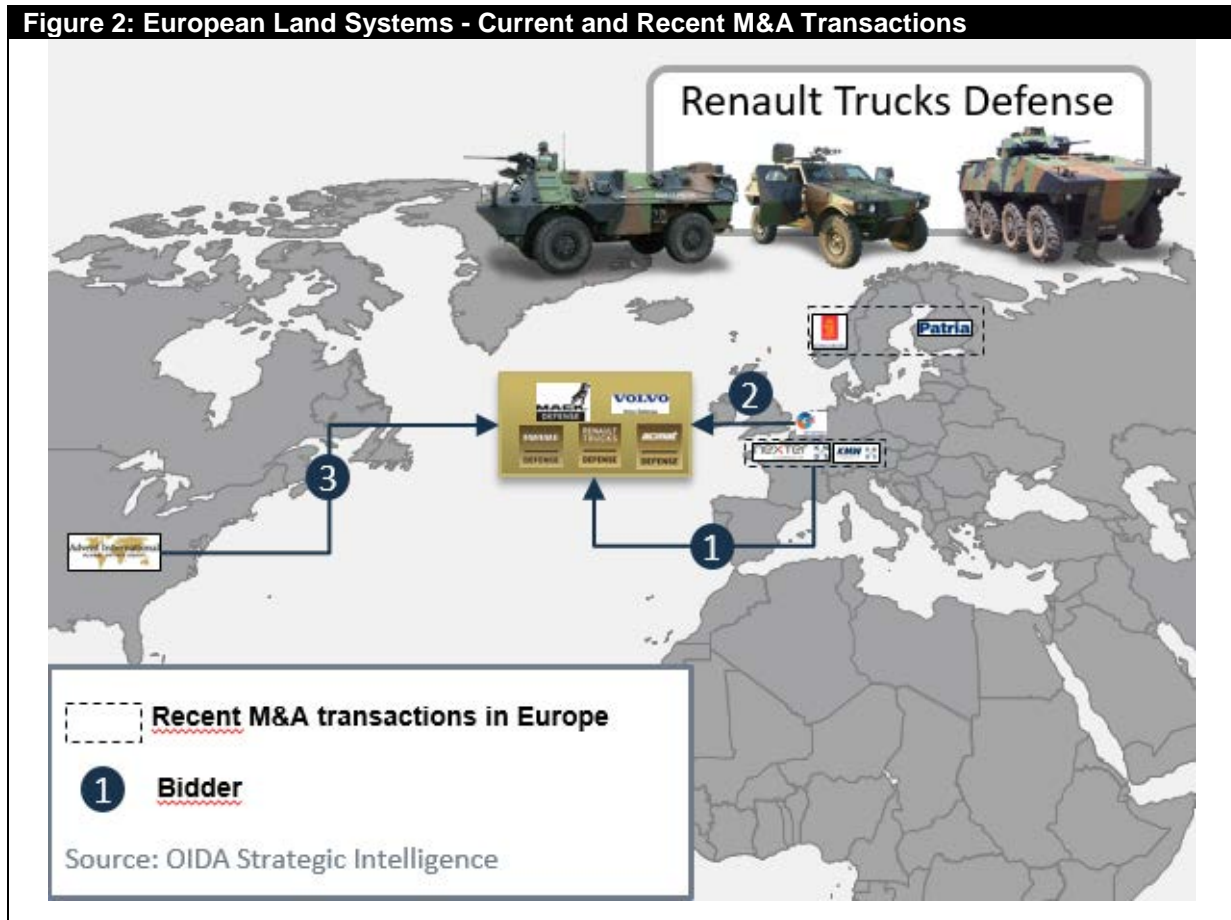
Figure 1: Volvo Group Organization



Indeed, the past years have witnessed a wave of mergers and purchases in the sector with the rapprochement of Nexter and Krauss-Maffei Wegmann in 2015 as the most obvious example. In this macro market trend, RTD is to switch from buyer to primary role player due to Volvo's decision to divest itself of its governmental sales subsidiary (disclosed in early November 2016). On June 2, RTD retained the interest of three bidders: the French-German KNDS specialising in the land defence industry, Belgian CMI, and the private equity fund Advent International.

Advent seems to be the underdog of this bidders triad due to the reluctance of the French state to see a non-industrial stakeholder taking over RTD while the Scorpion programme, of key importance for the French Armies, is soon to be launched. Nevertheless, both CMI and KNDS are thought to be a step ahead because they are involved in the Scorpion programme and able to assert several decades of experience in building military vehicles and dedicated weaponry. However on July 26, Advent withdrew from the contest claiming to focus solely on its on-going Morpho-Oberthur merger before tackling a challenge of this size.

Figure 2: European Land Systems - Current and Recent M&A Transactions



ANALYSIS – COMPANY VALUATION EXPLANATION

Establishing a reliable valuation for RTD is a challenge as the company is a Volvo Group subsidiary and as a result financial statements are scarce and further, RTD is not listed on the stock exchange. To undertake this valuation analysis, we did not choose a methodology that relied principally upon financial data, but rather a discounted cash flow (DCF) analysis. This provides a sharper picture of the company’s operating cycle and better time value of money regarding multiple years’ cash flow forecast. However, ignoring financial data proved to be impossible thus we picked up a few financial figures from what was deemed the closest baseline to settle our analysis. As RTD is a fully owned subsidiary of Volvo Group, deriving RTD equity related figures from its Swedish mother’s was the least risky alternative. Indeed, we cannot guarantee an absolute reliability to the following analysis even though the margin of error is small and the ins and outs of our analytical choices thoroughly justified through the following stages.

Free Cash Flow Establishment

Forecasting the yearly growth rate for RTD's sales was the cornerstone of our DCF analysis. Thoroughly analysing the company's strategic environment and competitive position is of crucial importance so that the overall future cash flow and the terminal value stands for the most accurate prediction of the company's wealth generation.

The decision to project excess returns for RTD over an entire decade was motivated by the company's sound competitive position and optimistic commercial prospects. Indeed, the special features (R&D expenses, trust and capital intertwining with state stakeholders, etc.) of the military vehicle market raise high barriers to entry for underdogs. Besides this, RTD and its own trademarks ACMAT and Panhard have historically maintained a long-lasting strategic cooperation with the French state (dating back to the FT17 of World War II) and still rely heavily on French procurements (50% of turnover in 2015). Thus, RTD has been directly or indirectly a part of every French Army vehicle development programme ever since and can assert its sales prospects in the light of the looming and in-depth renewal of French Army vehicle stock.

The spearhead of this new vehicle procurement is the Scorpion programme, which encompasses two new multipurpose light and heavy combat and reconnaissance vehicles - Griffon and Jaguar, with an initial delivery scheduled for 2018 and running until 2031. Given the fact that Belgium recently disclosed its participation in the deal, this procurement programme represents a once-off opportunity for RTD to benefit from the 2,085 Griffons and 308 Jaguars to be built to date, standing for an expected turnover of €3.3 billion for RTD alone (42% share of the Scorpion programme along with Nexter and Thales). Additionally, RTD and Panhard chalked up a bunch of other domestic and export contracts including the Sherpa deliveries to the French Special Forces (241 light and 202 heavy vehicles), Kuwaiti Forces (300 units) for about €670 million, and the P-4 heir the VLTP-NP produced by ACMAT in Saint-Nazaire with 3,700 units ordered at a price of €500 million.

This new material procurement pushing to retire the VAB, AMX10, and other last generation vehicles along with the VBCI's, will also bring about MCO services that will inflate the expected outcome for RTD's revenue. Besides this, if one gets on the slippery ground of forecasting the fallouts of the incoming RTD purchase, the new owner of RTD will basically consent to pay a premium to takeover because it expects to collect on results from forecasted synergies once RTD is purchased. Whether implying further investment, new management nomination, or better resource allocation the new owner of RTD will strive to expend the company's growth to reach its synergies prediction and consequently will buttress our sales growth model.

As RTD's sales hallmark for the incoming years, we set our revenue growth forecast model on the Scorpion programme's timeline, which expects first unit deliveries in 2018 with full rate production threshold reached in 2020. Hence, we implemented a sturdy growth ratio model increasing rapidly up to 15% in 2020 and decreasing afterward to stabilise at 5%. It must be mentioned that the expected French GDP average growth rate was fixed by the INSEE at 1.9%.

Figure 3: Scorpion Programme's Vehicles



Source: Nexter / Renault Trucks Defense / Thales

RTD's net sales for the year 2016 was assumed to be at a one-off level giving the cash input stemming from the sale of 100 VAB Mark3 and 100 Sherpa armoured transport vehicle package for an amount estimated at €350 million. This one time turnover does not bear any consequence for our long-term revenue calculation as from 2016 included, it is calculated on the forecasted growth prevision pattern onto which the €350 million only pertains to the 2016 fiscal year.

Figure 4: VAB Mk3 from RTD



Figure 5: Sherpa Light Scout from RTD



Source: Renault Trucks Defense

With regards to the establishment of the free cash flow calculation items, facing the lack of detailed annual reports and suitable business plans, several assumptions were required to fill in the gaps.

First, we decided to consider the operating margin as stable during the study period, basing this conjecture on the former years of RTD's income statements, which show this ratio staying put from 2012 to 2015. Therefore, we endorsed the assumption of RTD having a sound operational management strategy under which the operating costs would remain the same and the RTD EBITDA would only grow proportionally to the estimated company net sales growth over the studied decade.

- Moreover, with regards to the various items subtracted from the EBITDA basis, the tax on EBIT calculation was undertaken with the theoretical French corporate tax rate of 33.3% from 2016-19 and then 28% from 2020 due to a scheduled French tax reform.
- Just as numerous other RTD accounting items, Net Capex was not found in the company statements. Thus, we had to extrapolate the figure from the Volvo Group's overall cash flow statement and weighted RTD's part for the year 2015. For the investment forecast starting from 2016, we took the medium investment value carried out by Volvo Group from 2011 to 2015 and weighted RTD's part in order to mitigate the volatility to set a "normalized" baseline for a more accurate projection. From the 2016 starting point, Capex grows by 10% a year outrunning the net sales growth rate during the Scorpion programme implementation (2016 to 2019) before reaching the full rate production threshold from 2020 and slipping to a cruising yearly growth rate of 2% until 2025.

- Working capital was deemed particularly high in 2015 (standing at 14% of net sales). Despite this, we decided to keep this 14% ratio as a rule of thumb for the forecast in the absence of a publicly disclosed in-house business plan.

Discount Rate Calculation

To obtain the present value of the future free cash flow, one may discount the cash generated by the company after deducting fiscal expenses and those needed to maintain or develop its productive might by the weighted average cost of capital (WACC). The use of this discount rate has the advantage of tackling the return required by all stakeholders, including both equity and debt holders.

To calculate the RTD cost of equity we had recourse to the capital assets pricing model applied, once again, to Volvo Group values as RTD's equity is fully owned by Volvo Group. To dig into the details, the risk-free rate we used was the one of a 2015 French 10 year bond (OAT 10 ans), the expected market return was taken from the OMX Stockholm index investment data, and the beta, once again, had to be elicited from Volvo Group financials.

As for the cost of debt, it was estimated through a RTD financial document analysis. Likewise, we managed to calculate the market value of debt and equity from RTD's own statement analysis. The outcome of this analysis was a WACC of 5.63% for RTD.

Terminal Value and Company Valuation

Once the entire set of ten years cash flow listed, the last one was used to evaluate the company's terminal value, i.e. the value that will allegedly be brought by RTD's activity over a perpetual timescale after 2025 with an infinite cash flow growth rate. As we expect RTD to continue performing rather well until at least 2031, at the end of the deliveries related to the Scorpion programme and regardless of future commercial prospects and new programmes to come, we set a perpetual growth rate at 3%. Even though it might be a guessing game, this assumption does not appear to be overambitious as RTD's environment is believed to remain favourable and the company set to continue performing well buoyed by its long-term public contracts bringing revenue stability. Hence, applying the Gordon Growth Model and further discounting it at our WACC rate, we ended up with a discounted terminal value of €631,242,474, which added to the 2016-2025 discounted cash flow sum gives a RTD enterprise value of **€771,698,125**.

Whoever the buyer will be, the assumed worth of its target is about €770 million and one may speculate about a purchasing price closer to €800 million. Even if the French state dreams of reinforcing the French side (Nexter) of KNDS, Volvo Group would inevitably desire a better trade-off achievable from the bidding competition.

Table 1: Cash Flow Forecast (N+10 in €)						
	2015	2016	2017	2018	2019	2020
Forecasted Revenue Growth		3%	5%	7%	12%	15%
RTD Net Sales	362,892,000	723,778,760	392,467,698	419,940,437	470,333,289	540,883,283
RTD EBIT	12,737,000	25,403,619	13,775,066	14,739,320	16,508,038	18,984,244
EBITDA	26,768,000	53,388,085	28,949,592	30,976,063	34,693,191	39,897,170
(-) Tax on EBIT	4,245,667	8,467,873	4,591,688	4,913,107	5,502,680	5,315,588
(-) Net Capex	808,800	9,537,547	10,491,302	11,540,432	12,694,475	12,948,365
Working Capital	50,625,000	101,329,026	54,945,478	58,791,661	65,846,660	75,723,660
(-) Changes in WC	17,275,000	50,704,026	-46,383,549	3,846,183	7,054,999	9,876,999
Free Cash Flow (FCF)	4,438,533	-15,321,359	60,250,150	10,676,341	9,441,037	16,437,200
Discounted Free CF (DFCF)		-14,504,742	53,998,734	9,058,590	7,583,516	11,833,253
	2021	2022	2023	2024	2025	
Forecasted Revenue Growth	12%	5%	5%	5%	5%	
RTD Net Sales	605,789,277	636,078,740	667,882,677	70,1276,811	736,340,652	
RTD EBIT	21,262,354	22,325,471	23,441,745	24,613,832	25,844,524	
EBITDA	44,684,830	46,919,072	49,265,025	51,728,276	54,314,690	
(-) Tax on EBIT	5,953,459	6,251,132	6,563,689	6,891,873	7,236,467	
(-) Net Capex	13,207,332	13,471,478	13,740,908	14,015,726	14,296,041	
Working Capital	84,810,499	89,051,024	93,503,575	98,178,754	103,087,691	
(-) Changes in WC	9,086,839	4,240,525	4,452,551	4,675,179	4,908,938	
FCF	16,437,200	22,955,936	24,507,877	26,145,498	27,873,245	
DFCF	11,833,253	15,645,306	15,812,752	15,970,239	16,118,133	

Source: Annual Report, Company Website, Primary and Secondary Research

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Table 2: Cost of Capital	
Cost of Debt	2.46%
Cost of Equity	7.40%
WACC	5.63%
Perpetual CF Growth Rate	3.00%

Source:

OIDA Strategic Intelligence

Table 3: Company Valuation (in €)	
Terminal Value	1,091,613,785
Discounted Terminal Value	631,242,474
RTD Enterprise Value	771,698,125

Source:

OIDA Strategic Intelligence

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APPENDIX

Table 4: Main Contracts of RTD Group by Country 1998-2017 (Part 1)

Country	Brand	Platform	Year	Units	Amount	Commentary
Belgium	Renault Trucks Defense	Griffon (VBMR)	2017	417	€1.1 bn	To replace Dingo II and Piranha III vehicles in the time period 2025-2030.
		Jaguar (EBRC)	2017	60		
Botswana	Panhard	VBL	-	64	-	
	ACMAT	VLRA	2004	128		
Brazil	Renault Trucks Defense	Sherpa Light APC	2015	3	BRL 5.25 m	For the Federal Police.
Canada	Mack Defense	Kerax 8x8 + 300 trailers + 150 Armour Protection Systems	2015	1,500	\$CAD 725 m	For the Medium Support Vehicle System (MSVS) Standard Military Pattern (SMP) programme and to provide an initial five years of In-Service Support (ISS) for the SMP fleet. Deliveries started in 2017. A further option exists for 650 more vehicles.
Cameroon	ACMAT	Bastion APC	2015	15	-	Offered by the U.S. DoD through an order (62 for \$25 million) to Mack Defense for the African Union Mission in Somalia (AMISOM).
Chad	ACMAT	Bastion APC	2012	≈20		
Colombia	Renault Trucks Defense	MIDS	2014	3	\$1.8 m	For the National Police.
Congo-Brazzaville	ACMAT	ALTV	2012	14	-	For the National Police.
		Bastion	2012	2	-	
		VLRA	2012	1	-	
Cyprus	ACMAT	VLRA	1990s	120		For the MoD.
Ivory Coast	ACMAT	ALTV	2012	519	€46 m	For the National Police and the Gendarmerie as well as for Presidential security.
		Bastion APC	2012			
		VLRA	2012			
Egypt	Renault Trucks Defense	Sherpa Scout	2012	-	€400 m	For the Armed Forces (roughly 1,500 vehicles).
		Sherpa Light Station Wagon	2012	-		
		Kerax 8x8	2012	-		
		MIDS	2012	-		For the police force.
Equatorial Guinea	ACMAT	ALTV	2011	48		For border control.
Estonia	Volvo Defense	FMX trucks	2014	-	-	For the Armed Forces.
Ethiopia	ACMAT	Bastion APC	2015	12	-	Offered by the U.S. DoD through an order (62 for \$25 million) to Mack Defense for the African Union Mission in Somalia (AMISOM).
France	ACMAT	VLRA	2003	40	€4.6 m	For the Armed Forces.
	Panhard	VPS	2005	51	-	For the French Special Operations Command.
	Renault Trucks Defense	-	2007	570	-	Since 2007, the French public procurement grouping (UGAP) has ordered 570 trucks to carry out logistical duties for the Armed Forces (Army, Navy, Air Force, DGA).
	Renault Trucks Defense	Sherpa 3	2008	90	-	For the Gendarmerie Nationale.
	Renault Trucks Defense	Sherpa 5 6x6	2008	72	-	For equipping the Nexter Caesar 155 mm/52-cal artillery systems of the French Army.
	Renault Trucks Defense	VBCI	2008	116	-	Built with Nexter for the French Army.
	Panhard	PVP	2008	933	-	
	Renault Trucks Defense	20 Armour Protection Systems for Kerax 8x8	2008	20	-	For operation in Afghanistan for the Armed Forces Fuel Service (SEA).

Source: Annual Reports, Company Website, Primary and Secondary Research

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Table 5: Main Contracts of RTD Group by Country 1998-2017 (Part 2)

Country	Brand	Platform	Year	Units	Amount	Commentary
France	Renault Trucks Defense	Sherpa 3	2009	33	-	In order to transport transmission units for Communication Systems Syracuse 3.
	Renault Trucks Defense	VBCI	2009	332	-	Built with Nexter for the French Army.
	Renault Trucks Defense	Army trucks	2011	-	€25 m	Contract to RTD for service and support for 8,000 Army trucks.
	Renault Trucks Defense	Sherpa 5 6x6	2012	30	-	For the French Armed Forces Fuel Service (SEA).
	Renault Trucks Defense	PLFS (Sherpa)	2015	202	-	Major order to supply 443 new patrol vehicles for France's special forces.
	Panhard	VLFS	2015	241	-	
	Panhard	PVP	2015	5	-	For the RAID (French Police Unit).
	Panhard	PVP	2015	4	-	For the BRI (French Police Unit).
	ACMAT	VLTP-NP	2016	3,700	€500 m	
	Renault Trucks Defense	Griffon (VBMR)	2017	319	≥ €5 bn	1,722 VBMR vehicles are expected.
Renault Trucks Defense	Jaguar (EBRC)	2017	20	248 EBRC vehicles are expected.		
Gabon	ACMAT	ALTV	2015	12		For French contractors Sovereign Global, which trains Gabonese forces to integrate MINUSCA forces in Central Africa.
Indonesia	Renault Trucks Defense	-	2006	32	€22.4 m	For equipping a peacekeeping contingent in Lebanon.
		Sherpa 3A	2011	92	-	Built with PT Pindad for the Indonesian Army.
		Sherpa 5 6x6	2012	36	-	For equipping the Nexter Caesar 155 mm/52-cal artillery systems.
			2017	18	-	
Kuwait	Renault Trucks Defense	Sherpa Scout	2015	120	-	For the National Guard.
	Renault Trucks Defense	Sherpa Scout	2016	300	€270 m	For Armed Forces.
Mali	ACMAT	Bastion APC	2016	-	-	For Mali's armed forces.
Morocco	ACMAT	-	2008	600		
NATO	Renault Trucks Defense	Sherpa 3	2009	17		Have been delivered to the American company Globecom Systems Inc. for Signal Battalions.
Qatar	Renault Trucks Defense	Higuard	2011	22	-	For Qatar's Internal Security Forces.
		Sherpa Light	2011	5	-	
		Sherpa Light	2013	5		
Romania	Panhard	PVP	2012	16	-	The LAORV version specific to the Romanian Army offers a number of new developments.
Saudi Arabia	ACMAT	VLRA	2006			
	ACMAT	Bastion Patsas	-	-		
	Renault Trucks Defense	VAB Mk3	2014	100		Initially part of 2014's \$3 billion in military aid to Lebanon in the DONAS contract. Since, renamed SFMC (Saudi Fransi Military Contract).
	Renault Trucks Defense	Sherpa Light	2014	100	≈ €350 m	
Singapore	Renault Trucks Defense	Higuard	2015	-	-	Designated Peacekeeper in Singapore.
Sweden	ACMAT	Bastion APC	2015			For Sweden's Särskilda Operationsgruppen (Special Operations Task Group/SOTG).
Tanzania	ACMAT	Bastion APC	2014	≈100		To be leased from the UN for peacekeeping operations.
	ACMAT	VLRA 2	2014			
Togo	ACMAT	ALTV	2012	44	-	For the police force.
		Bastion APC	2014	≈30	-	For the armed forces.

Source: Annual Reports, Company Website, Primary and Secondary Research

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Table 6: Main Contracts of RTD Group by Country 1998-2017 (Part 3)

Country	Brand	Platform	Year	Units	Amount	Commentary
Tunisia	ACMAT	Bastion APC	2015	4	-	Offered by the U.S. DoD through an order (62 for \$25 million) to Mack Defense for the African Union Mission in Somalia (AMISOM).
Uganda	ACMAT	Bastion APC	2015	17	-	Offered by the U.S. DoD through an order (62 for \$25 million) to Mack Defense for the African Union Mission in Somalia (AMISOM).
Zambia	ACMAT	VLRA	2004	20		


Source: Annual Reports, Company Website, Primary and Secondary Research


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