Research as a Service

Millennium Services Group Ltd

Secure balance sheet, positioned for growth

Human Services

15 December 2020

Millennium Services Group Ltd (ASX:MIL) is a market leading provider of cleaning & security services, predominantly to tier-1 property trusts and retailers (~75% of revenue in FY20). The business employs more than 5,000 people and it is the coordination and utilisation of these people across the group's contracted facilities that determines group profitability. Between FY16 and FY18 the fundamentals of people management slipped, resulting in labour inefficiencies, poor tendering practices, a bulging cost structure and higher debt via an acquisition which ultimately failed to deliver on acquired metrics. In November 2018, these problems were acknowledged, and new management installed to fix them. Fast forward 18-months and significant progress has been made, albeit a little muddied (and aided) by COVID. Debt has been refinanced and reduced by $20m since June 30, $7m has been reduced from the cost base (with $4m to come) and ~70% of the workforce migrated to new rostering technology. The entire workforce has been moved to modern award wages, and compliance and disclosure (including financial) has improved markedly. Legacy contracts have been renewed at more sustainable rates or discontinued and relationships within new sectors being formed for future opportunities. Key financial metrics such as GP% are improving as a result with more gains expected over FY21.

Business model

MIL is essentially a human services business, bidding for predominantly fixed rate contracts, with opportunities for volume gains and adhoc services, across the essential services of cleaning & security for durations of 3-5 years with large corporates. Satisfying contractual obligations utilising a vast workforce and procuring consumables for the jobs within the contacted price is the key to profitability. Historically focusing on cleaning and security services within major shopping centres, MIL is looking to de-risk the retail exposure by moving into new sectors including Aviation, Aged care, Education and Government.

Cleanup largely complete

It is said that a problem cannot be dealt with until a problem is acknowledged, and in November 2018 widespread legacy issues were acknowledged by a new MIL board and senior management with a view to resolving them. They ranged from a lack of accountability across all layers of the business, an overhead cost structure that was too high, the bidding/winning of tenders at lower than historical gross profit margins, rostering and labour inefficiencies leading to non-recoverable overtime payments and the incorrect application of some EBA allowances. Overlay high debt levels and an earnings hole was created. Fast forward 18-months and overhead costs have been reduced by $7m, contracts have been renewed with all but $20m (5%-6%) in business retained (with most of the business foregone low margin or loss-making), new technology is being employed across the group to improve labour management which incorporates compliance with all modern awards, and mostly importantly debt has been reduced by $20m and facilities refinanced since June 30. Despite COVID (which has been a cashflow benefit but a business disruption), underlying gross margins and EBITDA improved in FY20, with further progress forecast for FY21.

Look to people heavy businesses for peer comparison

Millennium is a people intensive business which marks up labour costs to cover group overheads and achieve a targeted return. This is no different to human services businesses providing accounting, legal, construction or mining services. Key differences between these industries and firms that service them will centre around cyclicality, the level of "value add" or "differentiation" and the base salary from which the service is being marked-up. ASX listed peers we look to include electrical & facilities manager Tempo Australia (ASX:TPP), workforce management group People Infrastructure (ASX:PPE), contractors such as Decmil (ASX: DCG) and engineering services company Logicamms (ASX:LCM).

Historical earnings and ratios (in A$m unless otherwise stated)

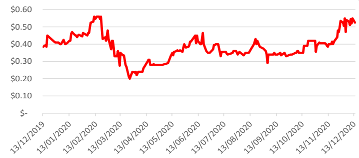
Year end	Revenue (A$m)	Gross Profit (A$m)	EBITDA Adj. (A$m)	NPAT Adj.* (A$m)	EPS Adj.*(c)	Net Debt (A$m)
06/17a	228.5	40.0	14.1	5.0	0.11	20.8
06/18a	283.6	42.5	8.7	(0.8)	(0.02)	24.3
06/19a	294.7	30.1	0.1	(14.3)	(0.31)	27.1
06//20a	257.3	30.8	4.0	0.3	0.01	34.6

Source: Company data *EBITDA and NPAT adj for one-time, non-cash items

Share details

ASX Code	MIL
Share price (14 Dec)	$0.525
Market Capitalisation	$24.1M
Shares on issue	45.9M
Free float	31.5%

Share performance (12 months)



Upside Case

- Rostering systems improve GP%
- Successfully diversify industry exposure to aviation, government, education, aged care
- Generate free cashflow to reduce debt

Downside Case

- Fail to roll key contracts on the margins required to generate targeted returns
- Debt load limits the company's ability to fund growth initiatives
- Workforce does not utilise new rostering

Catalysts/upcoming events

1H21 result: Looking for insight into the Group's sustainable revenue/cost structure of the group. Further contract renewals.

Comparable companies (Aust/NZ)

People Infrastructure (ASX:PPE) Decmil (ASX:DCG); Tempo (ASX:TPP); Logicamms (ASX:LCM)

Board of Directors

Roger Smeed	Chairman
Darren Boyd	Chief Executive Officer
Stuart Grimshaw	Non-Executive Director
Rohan Garnett	Non-Executive Director
Royce Galea	Executive Director

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FINANCIAL SERVICES GUIDE

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