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Millennium Services Group Ltd

Q3 FY23 Trading Update

Contract wins now evident in the numbers

Millennium Services Group Ltd (ASX:MIL) has announced an update on Q3 FY23 revenue and cash flow from operating activities. MIL achieved the first positive quarterly revenue growth since Q1 FY22 at +3.5%, while contract revenue growth was ~+12.6% on the pcp (excludes ad-hoc revenue). The COVID-related ad-hoc revenue has now all but cycled out of the quarterly numbers while new contract wins cycle in. Looking forward, we expect 9.6% total revenue growth in Q4 FY23 and our forecast remains unchanged for 6.5% H2 FY23 revenue growth. Q3 FY23 cash flow suggests our H2 FY23 adjusted EBITDA assumption of $6.8m (vs H1 FY23 of $2.8m) is on-track, which implies gross margins have at least held their Q2 FY23 levels. MIL continues to trade at a 60% discount to our assessed peer group on FY23f EV/EBITDA estimates. A multiple equal to the peer group would imply a share price of $1.05/share. As a sense check our DCF is $1.15/share.

Business model

MIL is a human services business with a focus on the essential services of cleaning and security, bidding for predominantly long-term contracts that have annual contract adjustments to protect MIL from movements in labour resource costs. Additional volumes over and above those contracted can be gained from ad-hoc services, which represent ~10% of group revenue at a higher average margin. Satisfying contractual obligations utilising a vast workforce and procuring consumables for the jobs within the contracted price is 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. An increased focus on compliance (Fair Work, Modern Slavery Act and Labour Hire regulations), and utilising the ASX-listed nature of the business to demonstrate transparency in these important areas (which most large private companies can't achieve), will be keys in this push.

New business evident in Q3 FY23 revenue, EBITDA on track

We noted in our H1 FY23 MIL result note that new contract wins totalling ~$25m-$30m (or ~14% of the existing contracted revenue base) were not evident in the numbers to date due to distortions from: (1) The loss of the QIC contract; and (2) COVID related ad-hoc business. These wins are now becoming evident with Q3 FY23 total revenue growth of 3.5% and contract revenue growth closer to ~12.6%. With high ad-hoc revenue cycling out in Q4 we expect an acceleration in total revenue growth to 9.6% in Q4 FY23. Importantly adjusted EBITDA looks on-track to hit our $6.8m estimate for H2 FY23 (vs $2.8m H1) using key data released in the Q3 FY23 4C as a guide to the P&L.

Relative EV/EBITDA implies a $1.05/share valuation

Our assessed peer group average FY23f EV/EBITDA multiple implies a $1.05/share valuation using MIL's FY23 estimates (5.3x EV/EBITDA). We see no reason why this business does not deserve multiples closer to the peer average given average contract length (three-five years), relatively low working capital, low capex intensity and market consolidation opportunities. To sense check, our DCF valuation is $1.15/share.

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

Year end	Adj. revenue	Adj. EBITDA	NPAT rep.	EPS adj. (c)	P/E (x)	EV/Adj. EBITDA
06/21a	273.7	11.6	2.2	0.07	5.1	1.5
06/22a	260.6	11.1	2.3	0.09	4.5	1.9
06/23f	266.8	9.6	2.2	0.06	6.3	2.0
06/24f	281.8	12.3	5.2	0.11	3.4	1.2

Source: Company data, RaaS estimates for FY23f and FY24f

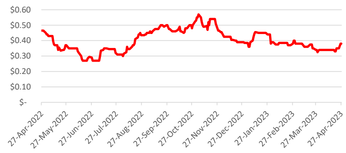
Human Services

28 April 2023

Share Details

ASX code	MIL
Share price (27-Apr)	$0.38
Market capitalisation	$17.5M
Shares on issue	45.9M
Net debt at 31-Mar-23 (excl. debtor finance)	$3.5M
Free float	~31.5%

Share Performance (12 months)



Upside Case

- Converting a portion of the tender pipeline
- Successfully diversify industry exposure to include government, education and aged care
- EPS accretive/complementary acquisitions

Downside Case

- Competitive margin pressures re-emerge
- Sizable contract loss
- Timing of wages growth vs contracts clauses

Board of Directors

Stuart Grimshaw	Chairman
Royce Galea	CEO
Rohan Garnett	Non-Executive Director
Darren Perry	Non-Executive Director

Company Contacts

Royce Galea (CEO) +61 412 660 006
royce.galea@millenniumsg.com

RaaS Contacts

John Burgess* +61 410 439 723
john.burgess@raasgroup.com

Finola Burke +61 414 354 712
finola.burke@raasgroup.com

*The analyst owns shares

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Q3 FY23 Quarterly Highlights

Revenue

- **Total revenue growth was 3.5%, the first quarter of positive growth since Q1 FY22** despite still being impacted by lower ad-hoc revenues relative to Q3 FY22**.**
- **Underlying contract revenue growth** was ~+12.6% on the back of a number of new contract wins including ISPT, Newcastle Airport and JVL Investment Group.
- **Contract/ad-hoc revenue mix back to 91%/9%** against the pcp of 84%/16% which was aided by COVID-related security work**.**
- **H2 FY23 RaaS forecast on track at $137.2m,** implying $69m in revenue for Q4 FY23.

Exhibit 1: MIL quarterly revenue history (in A$m unless otherwise stated)

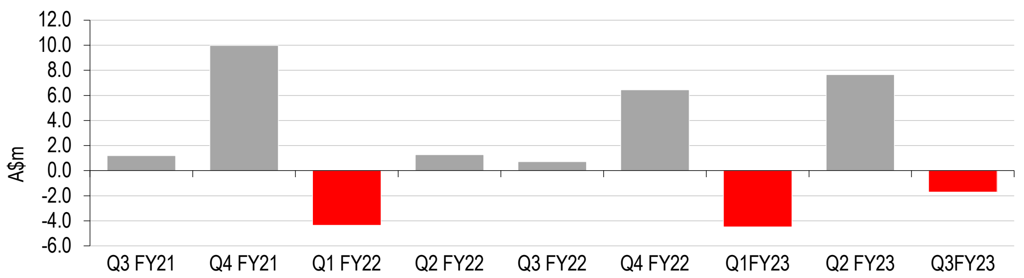
	Q3 FY22	Q4 FY22	Q1 FY23	Q2 FY23	Q3 FY23
Revenue	**65.9**	**63.0**	**63.3**	**66.2**	**68.2**
Contract	55.4	55.9	58.2	60.2	62.4
Ad-hoc	10.5	7.0	5.1	6.0	5.8
% growth					
Contract	(8.0)	(6.9)	4.1	9.9	12.6
Total	(5.0)	(9.1)	(3.5)	0.1	3.5
Mix (%)					
Contract	84	89	92	91	91
Ad-hoc	16	11	8	9	9

Source: Company announcements

Cash flow from operating activities

- **Negative cash flow of $1.7m,** with an additional fortnight's wages included in Q3 totalling $6.2m. For these reasons MIL's quarterly cash-flow numbers are volatile quarter-to-quarter as the chart below demonstrates.

Exhibit 2: MIL quarterly cash-flow history



Source: Company announcements

- **Net debt (excluding trade financing) of $3.5m**. The current finance facility has been extended to February 2024, and the group has $9.9m in unused debt facilities.
- **H2 FY23 RaaS EBITDA forecast of $6.8m (vs $2.8m in H1 FY23) looks on-track** using the data disclosed in the Q3 FY23 4C as a guide for the P&L. We estimate an adjusted EBITDA of $3.6m for Q3 FY23 (before any additional WC movements) adjusting reported operating cash outflow for tax, interest, one-offs, the additional fortnight's pay and estimated accruals for the extra fortnight.

Exhibit 3: Q3 FY23 4C to P&L reconciliation

Variable	A$M
Cash from operating activities (4C)	**(1.7)**
Add tax paid (4C)	0.5
Add interest expense (4C)	0.5
Add one-offs (4C)	0.1
Add extra fortnight's pay (4C)	6.2
Less accruals for extra fortnight (RaaS estimate)	(2.0)
Adj. EBITDA before other WC movements (P&L est.)	**3.6**

Source: RaaS estimates

Outlook

Revenue

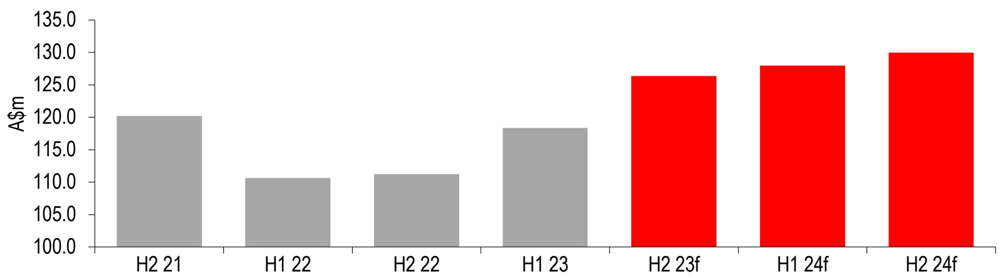
Management is targeting 8%-10% organic contract revenue growth and tracking above this based on recent contract wins and quarterly results. This is not apparent in reported revenue to date due to the cycling of:

- **The QIC contract loss,** which cycled out of the numbers in Q1 FY23; and
- **Lower ad-hoc revenue** from COVID-related work with the Victorian Department of Health, which will cycle out of the numbers in Q3 FY23.

Just looking at contracted revenue we saw significant improvement in H1 FY23, and further improvement in Q3 FY23 which will continue into Q4 FY23 and FY24.

As a result, we are forecasting 6.5% H2 FY23 group revenue growth against the 1.6% decline in H1 FY23. Into FY24 we are forecasting 5.6% revenue growth driven by contracted revenue.

Exhibit 4: MIL half-yearly contracted revenue



Source: Company announcements and RaaS estimates

Relative Peer Group Valuation

We compare MIL to other listed small-cap players that rely heavily on human resources and to a lesser extent equipment to deliver their services to typically larger clients.

The table below summarises forecast FY23 metrics across a wide range of variables together with a range of FY22 actual variables.

MIL currently trades at a material (60%) discount to the FY23f EV/EBITDA peer average of 5.3x despite generally better contract terms, similar gross margins, and lower working capital/capex requirements.

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Exhibit 5: Peer group financial comparison – FY22a (in A$m unless otherwise stated)

Company name	Ticker	Share price (cps)	Mkt. cap.	Net debt(cash) (Dec-22)	Adj. FY23f EBITDA	FY23f revenue	GP%	FY22 Working capital/sales %	EV/ Sales (x)	EV/ EBITDA
GR Engineering	GNG	1.88	292	(97.8)	40.0	515	12	(1)	0.38	4.8
PeopleIn	PPE	2.92	293	45.7	62.7	1,215	15	8	0.28	5.4
Licopodium	LYL	10.15	403	(99.4)	64.9	321	27	10	0.95	4.7
Southern Cross Electrical	SXE	0.63	164	(53.1)	35.3	450	16	7	0.25	3.1
Ashley Services	ASH	0.71	102	3.6	24.1	530	16	5	0.20	4.4
MCS Services	MCS	0.03	7	0.1	0.7	40	17	3	0.17	9.6
AVERAGE							17	6	0.37	5.3
Millennium	MIL	0.38	17	4.0	9.6	267	15	1	0.08	2.2

Sources: Company financials, Refinitiv, RaaS estimates

Outlook And Investment Case

- The group operates in markets worth an estimated $11.7b (cleaning) and $9.8b (investigation and security services), according to IBISWorld. In the cleaning business (~83% of MIL revenue) MIL has less than 2% market share in a market where the top-four largest players have less than 10% of the market, offering significant market-share opportunities.
- The group's growth strategy will look to use the current balance sheet, ASX listing and trading history to increase "value-add" services, participate in industry rationalisation, and use technology such as rostering and traffic-flow systems and robotics to improve operating efficiencies.
- The acquisition of 49% of Codee Cleaning Services in December 2021 overlays industry consolidation with an increasing focus on ESG.
- Net debt was just $3.5m as at March 2023 (excluding trade finance), providing a solid base from which to grow and/or acquire while looking at capital management options. MIL has undrawn banking facilities of $9.9m.
- Gross margins were back to "targeted" levels in Q2 FY23 following a timing issue in Q1 FY23 and based on historical and peer analysis we feel these margins are sustainable at ~15%-16% and EBITDA margins 4.0%-5.0%.
- A change in debt covenants would pave the way for the resumption of dividends. Based on FY23 RaaS adjusted EPS forecasts, a 50% pay-out ratio at current prices would imply a dividend yield of 8%.
- Recent M&A transactions of similar businesses add valuation support to MIL, namely the 75% purchase of Linc Personnel by Ashley Services for 3.4x EBITDA, and the 100% acquisition of BIC by Bidvest for ~8.8x EBITDA.

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Exhibit 6: Financial Summary (in A$m unless otherwise stated)

Millennium Services (ASX.MIL)					
Profit and Loss (A$m)					
Y/E 30 June	**FY20A**	**FY21A**	**FY22A**	**FY23F**	**FY24F**
Revenue	257.3	273.7	260.6	266.8	281.8
Gross profit	30.8	40.8	39.8	39.9	43.5
GP margin %	12.0%	14.9%	15.3%	15.0%	15.4%
Underlying EBITDA	4.0	11.6	11.1	9.6	12.3
Depn	(5.9)	(4.9)	(4.6)	(4.2)	(3.8)
Minorities (AT)	0.0	0.0	0.1	0.1	0.1
EBIT	(1.9)	6.8	6.7	5.6	8.6
Interest	(3.2)	(1.8)	(1.2)	(1.7)	(1.2)
Tax	5.3	(1.6)	(1.6)	(1.1)	(2.2)
NPAT (adj)	**0.3**	**3.4**	**3.9**	**2.8**	**5.2**
Adjustments	1.7	(1.2)	(1.6)	(0.6)	0.0
NPAT	**2.0**	**2.2**	**2.3**	**2.2**	**5.2**
Abnormals (net)	14.5	15.2	0.0	0.0	0.0
NPAT (reported)	**16.5**	**17.4**	**2.3**	**2.2**	**5.2**
Cash flow (A$m)					
Y/E 30 June	**FY20A**	**FY21A**	**FY22A**	**FY23F**	**FY24F**
EBITDA (inc cash rent/JK)	19.4	29.3	10.0	8.6	11.1
Interest	(3.2)	(1.8)	(1.2)	(1.7)	(1.2)
Tax	0.5	(0.1)	(2.4)	(1.1)	(2.2)
Working capital changes	(16.6)	12.9	(1.6)	(0.2)	(0.2)
Operating cash flow	**0.1**	**40.3**	**4.8**	**5.5**	**7.6**
Mtce capex	(2.2)	(2.2)	(1.8)	(2.5)	(2.1)
Free cash flow	**(2.1)**	**38.1**	**3.0**	**3.0**	**5.4**
Growth capex	0.0	0.0	0.0	0.0	0.0
Acquisitions/Disposals	0.0	0.0	0.0	0.0	0.0
Other	(1.7)	(2.1)	(2.2)	(1.0)	(1.0)
Cash flow pre financing	(3.8)	36.0	0.8	2.0	4.4
Equity	0.0	0.0	0.0	0.0	0.0
Debt drawdown/(repay)	1.6	(21.4)	(2.0)	(2.0)	(2.6)
Net Dividends paid	0.0	0.0	0.0	0.0	0.0
Net cash flow for year	**(2.2)**	**14.6**	**(1.2)**	**(0.0)**	**1.8**
Balance sheet (A$m)					
Y/E 30 June	**FY20A**	**FY21A**	**FY22A**	**FY23F**	**FY24F**
Cash	1.8	7.3	1.9	1.8	3.6
Accounts receivable	29.8	18.0	17.3	18.9	20.0
Inventory	1.2	1.1	1.2	1.3	1.3
Other current assets	2.6	2.3	1.9	3.0	3.1
Total current assets	*35.5*	*28.8*	*22.3*	*25.0*	*27.9*
PPE	8.6	7.0	6.8	6.2	5.6
Goodwill	7.5	7.5	7.5	7.5	7.5
Right of use asset	2.9	3.0	1.7	1.7	1.7
Deferred tax asset	7.4	8.5	7.8	7.8	7.8
Equity accounted Investee	0.0	0.0	1.3	1.3	1.3
Total non current assets	*26.4*	*26.0*	*25.0*	*24.4*	*23.9*
Total Assets	61.9	54.9	47.4	49.4	51.8
Accounts payable	16.3	17.3	15.0	16.4	17.4
Short term debt	36.4	5.5	4.7	2.7	0.1
Provisions	22.4	22.6	20.0	20.4	21.6
Lease liabilities/other	0.8	5.5	3.4	3.4	3.4
Total current liabilities	*76.0*	*50.9*	*43.1*	*43.0*	*42.4*
Long term debt	0.0	2.1	1.2	1.2	1.2
Other non current liabs	5.8	4.1	2.7	2.7	2.7
Total long term liabilities	*5.8*	*6.2*	*3.9*	*3.9*	*3.9*
Total Liabilities	81.8	57.1	47.0	46.9	46.3
Net Assets	**(19.9)**	**(2.3)**	**0.4**	**2.5**	**5.5**
Share capital	19.0	19.1	19.1	19.1	19.1
Reserves	(8.5)	(8.3)	(7.9)	(7.9)	(7.9)
Retained Earnings	(30.3)	(13.1)	(10.8)	(8.6)	(5.7)
Minorities	0.0	0.0	0.0	0.0	0.0
Total Shareholder funds	**(19.9)**	**(2.4)**	**0.4**	**2.6**	**5.5**

Share price (27 April 2023)						A$	0.380
Interim (A$m)		**H122A**	**H222A**	**H123A**	**H223F**	**H124F**	**H224F**
Revenue		131.7	128.9	129.6	137.2	139.1	142.7
EBITDA		6.7	4.4	2.8	6.8	5.7	7.2
EBIT		4.4	2.2	0.6	4.9	3.8	5.3
NPAT (normalised)		**2.7**	**1.0**	**(0.1)**	**2.9**	**2.2**	**3.3**
Minorities (AT)		0.0	0.1	0.1	0.1	0.1	0.1
NPAT (reported)		**1.9**	**0.2**	**(0.7)**	**2.9**	**2.2**	**3.3**
EPS (normalised)		0.041	0.005	(0.016)	0.062	0.048	0.071
EPS (reported)		0.041	0.005	(0.016)	0.062	0.048	0.071
Dividend (cps)		0.000	0.000	0.000	0.000	0.000	0.020
Imputation							
Operating cash flow		na	na	na	na	na	na
Free Cash flow		na	na	na	na	na	na
Divisionals		**H122A**	**H222A**	**H123A**	**H223F**	**H124F**	**H224F**
Cleaning		99.6	103.5	107.7	114.9	116.3	119.5
Security		32.1	25.3	21.9	22.3	22.8	23.2
(Other)		-	-	-	-	-	-
Total Revenue		**131.7**	**128.9**	**129.6**	**137.2**	**139.1**	**142.7**
Gross profit		21.0	18.8	18.1	21.8	21.4	22.6
Underlying GP Margin %		15.9%	14.6%	14.0%	15.9%	15.4%	15.8%
Operating Costs							
Employment		8.8	8.9	9.7	9.3	10.0	9.6
Other		5.5	5.5	5.6	5.7	5.8	5.9
Exceptional		-	-	-	-	-	-
Total costs		**14.3**	**14.4**	**15.3**	**15.0**	**15.8**	**15.5**
EBITDA		**6.7**	**4.4**	**2.8**	**6.8**	**5.7**	**7.2**
EBITDA margin %		5.1%	3.4%	2.2%	5.0%	4.1%	5.0%
Margins, Leverage, Returns			**FY20A**	**FY21A**	**FY22A**	**FY23F**	**FY24F**
EBITDA margin %			1.6%	4.3%	4.3%	3.6%	4.3%
EBIT margin %			(0.7%)	2.5%	2.6%	2.1%	3.0%
NPAT margin (pre significant items)			0.8%	0.8%	0.9%	0.8%	1.8%
Net Debt (Cash)			34.6	0.3	4.0	2.1	-2.3
Net debt/EBITDA (x)	(x)		8.6 x	0.0 x	0.4 x	0.2 x	-0.2 x
ND/ND+Equity (%)	(%)		63.5%	11.5%	111.7%	(429.8%)	29.1%
EBIT interest cover (x)	(x)		n/a	0.3x	0.2x	0.3x	0.1x
ROA			(6.0%)	11.6%	13.1%	11.6%	17.0%
ROE			nm	nm	nm	nm	nm
ROIC			nm	nm	nm	nm	nm
NTA (per share)			-0.60	-0.21	-0.15	-0.11	-0.04
Working capital			14.8	1.9	3.5	3.7	4.0
WC/Sales (%)			**5.7%**	**0.7%**	**1.3%**	**1.4%**	**1.4%**
Revenue growth			(12.7%)	6.4%	(4.8%)	2.4%	5.6%
EBIT growth pa			nm	(463.7%)	(1.1%)	(16.3%)	53.4%
Pricing			**FY20A**	**FY21A**	**FY22A**	**FY23F**	**FY24F**
No of shares (y/e)	(m)		45.9	45.9	45.9	45.9	45.9
Weighted Av Dil Shares	(m)		45.9	45.9	45.9	45.9	45.9
EPS Reported	cps		0.359	0.379	0.049	0.047	0.113
EPS Adjusted	cps		0.006	0.074	0.085	0.060	0.113
EPS growth (norm/dil)			nm	nm	14%	-29%	88%
DPS	cps		0.000	0.000	0.000	0.000	0.020
DPS Growth			n/a	n/a	n/a	n/a	n/a
Dividend yield			0.0%	0.0%	0.0%	0.0%	5.3%
Dividend imputation			30	30	30	30	30
PER Adjusted (x)			nm	5.1	4.5	6.3	3.4
PE market			15	15	15	15	15
Premium/(discount)			nm	(66.0%)	(70.2%)	(57.9%)	(77.7%)
EV/EBITDA			12.9	1.5	1.9	2.0	1.2
FCF/Share	cps		-4.5	83.0	4.9	6.5	11.9
Price/FCF share			-8.4	0.5	7.8	5.9	3.2
Free Cash flow Yield			(11.9%)	218.5%	12.9%	17.1%	31.2%

Source: RaaS estimates

FINANCIAL SERVICES GUIDE

RaaS Advisory Pty Ltd

ABN 99 614 783 363

Corporate Authorised Representative, number 1248415

of

BR SECURITIES AUSTRALIA PTY LTD

ABN   92 168 734 530

AFSL 456663

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Contact Details, BR and RaaS
BR Head Office: Suite 5GB, Level 5, 33 Queen Street, Brisbane, QLD, 4000
RaaS. 20 Halls Road Arcadia, NSW 2159
P: +61 414 354712
E: finola.burke@raasgroup.com

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If you have a complaint about our service you should contact your representative and tell them about your complaint. The representative will follow BR's internal dispute resolution policy, which includes sending you a copy of the policy when required to. If you aren't satisfied with an outcome, you may contact AFCA, see below. BR is a member of the Australian Financial Complaints Authority (AFCA). AFCA provide fair and independent financial services complaint resolution that is free to consumers.
Website: www.afca.org.au; Email: info@afca.org.au; Telephone: 1800931678 (free call)
In writing to: Australian Financial Complaints Authority, GPO Box 3, Melbourne, VIC, 3001.

Professional Indemnity Insurance

BR has in place Professional Indemnity Insurance which satisfies the requirements for compensation under s912B of the Corporations Act and that covers our authorized representatives.

DISCLAIMERS and DISCLOSURES