WHI SPY

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Marketing Communication

Your monthly guide to a range of ideas from the WH Ireland team

July 2015

STRONG BRAND GROWING SHARE IN ESSENTIAL MARKETS

Lakehouse (LAKE)

FTSE Small Cap | Share price: 96p | Market Cap: £151m

www.lakehouse.co.uk

LAKE is a strong player in the related areas of social housing maintenance and regeneration (up to 50% of revenues), compliance (for gas, fire, electricity and water), energy services and construction. Started in the 1980s, the business has built up a good franchise with a host of local authority and related clients. A good set of H1 results reported a month ago showed that the company is on track to deliver creditable FY operating margins in the 5-6% area pre-exceptionals, and these look to be sustainable. In May, LAKE strengthened its energy services business through the acquisition of Providor, a national smart meter installation and maintenance business. In recent years, it has built up a good record of acquiring complementary businesses effectively, and with a strong balance sheet (£10m-plus net cash anticipated for FY2015E), the company has the ability to generate further earnings enhancing acquisitions.

What we like

We like the regulatory drivers, notably (1) local authorities' new independence in spending their housing budgets due to the Coalition government's reforms and (2) the requirements for safe installations which the Compliance division meets. Also attractive is the visibility provided by a £500m-plus order book, coupled with the niche focus of the group, combined with the diverse range of clients and related services. The range of services the company can now supply and its strong profile with the unified underlying client base together imply strong cross-selling opportunities. The shares have performed well following flotation in March at 89p, though now trading below the 106p reached in early June.

With a long history, LAKE has shown good capabilities in navigating local authority under-currents. Though still small, the repair and maintenance element in the mix is encouraging; and Lake's record of growth by expanding market share suggests that it remains well-placed to respond to local authorities' need for cost-effectiveness. Strong forecast earnings growth for the current year is forecast to resume in FY2017E. On a 8.5x FY2015E rating, the stock is at a discount to peers, while paying an attractive 4.0%-plus yield.

Estimates to Sep	2014 (A)	2015 (E)	2016 (E)
Revenue (£m)	302.5	354.0	394.0
PBT (£m)	9.6	21.6	24.7
EPS (p)	7.0	11.9	12.1
P/E (x)	14.5	8.5	8.3
EV/EBITDA	N/A	5.7	5.0
DIV (p)	N/A	1.9	4.2
Yield (%)	N/A	1.9	4.1

Source: Company, Consensus forecasts (Bloomberg). Analyst: Nick Spoliar

CORPORATE ACTIVITY BOUNDS AHEAD

Last year was the largest for global M&A volume since the financial crisis – a massive $3.6 trillion according to financial software company Dealogic. With debt cheap, private equity firms awash with cash and overseas companies on the lookout for deals this trend has continued apace.

The first half of the current year, when including the Shell/BG deal has led to a more than doubling of the value of total deals in the UK to over $200bn. With the oil price now looking range bound there is also an expectation that larger, well financed operators will seek to acquire weakly capitalised rivals with strong assets.

In recent weeks we have seen ubiquitous confectionery firm **Thorntons** fall to Italian giant Ferrero, software group **Anite** is to be acquired by Dutch rival Keysight and well known cooker brand **AGA** is currently in talks with US giant Middleby Corporation. Moreover, **Ladbrokes** and **Coral** are in discussions to create what would be the largest bookies in the UK. Hopefully this increased interest in UK companies will help drive the equity market further in the second half of the year.

Miles Nolan
Editor

WINNER – WH Ireland Best Research Award
AIM Awards / 2014 sponsored by pwc

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Important disclaimers regarding companies that are the subject of this report can be found on the back page of this document.

EXPANSION OPPORTUNITIES IN SE ASIA

RapidCloud International*# (RCI)

FTSE AIM – Share price: 41.5p | Market Cap: £9m | www. rapidcloudinternational.com

RapidCloud is an integrated subscription-based computing products and services provider, delivering its proprietary products through all three cloud computing delivery models: Software-as-a-Service (SaaS), Platform-as-a-Service (PaaS) and Infrastructure-as-a-Service (IaaS). R&D is a key part of the company's strategy and has led to RCI amassing an impressive portfolio of proprietary products which it sells predominantly through its in-house sales team. The company currently has over 42,000 customers, ranging from small and mid-sized enterprises (SME) to large multi-national corporations and government agencies. In under two years of joining AIM, the company has made impressive progress on both operational and financial fronts, which we expect to continue.

What we like

RCI is strongly positioned for 2015 and beyond as a result of the strategic decisions made by management during the past year. These include: (i) the foray into Indonesia, the largest economy in SE Asia; and (ii) the appointment of a new sales director and subsequent formal organisation of the enterprise sales team who have recently been winning new contracts on a regular basis. The shares trade on 16x 2015 earnings, a significant discount to its peer group, declining to under 14x in 2016 and also supports a yield of 1.3%. The company recently completed a £1.7m fundraise at 54p a share, which is a 30% premium to current levels, which we believe is a reference price for RCI's shares in the near term.

Estimates to Dec	2014 (A)	2015 (E)	2016 (E)
Revenue (£m)	3.3	3.8	4.4
PBT (£m)	0.6	0.6	0.8
EPS (p)	3.82	2.55	3.03
P/E (x)	10.9	16.3	13.7
DPS (p)	0.57	0.57	0.73
Yield (%)	1.4	1.3	1.7

Source: Company, WH Ireland estimates

Analyst: Brendan D'Souza

*WH Ireland acts as NOMAD/Broker to RCI

#WH Ireland makes a market in RCI

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BOUNDING BACK INTO THE RING

WYG Group*# (WYG)

FTSE AIM – Share price: 114p | Market Cap: £78.1m | www.wyg.com

FY2015A prelims from **WYG** last month featured PBT/EPS up >30% and the order book at record levels, £105m (+21%, 50%-plus cover for the current year). A strong showing in the UK in particular drove these excellent results (UK sales +15%, UK EBITA +51%, UK margins pre central costs 9.2%). WYG's planning, design and management services businesses are market leaders here and demand is strong both immediately and fundamentally. DPS was doubled YoY to 1p. The Strategic Review concluded positively, laying out a well-defined long-term strategic growth trajectory and reaffirming the £15m 2018 PBT aspiration.

What we like

We see a lot more upside for WYG. (1) With the UK firing on all cylinders, momentum is

set to be strengthened further in the coming year by encouraging developments in the European business, following the recent completion of the Euro funding round. (2) Margins have much further to go, in our view – could double to 10% post central costs in the next few years. (3) Reaffirmation of the targets is encouraging. (4) Management have proved savvy and effective. (5) WYG focuses on high-value work with corresponding entry barriers, typically at the front end of projects. (5) We regard the shares as fundamentally undervalued – at a 30% discount for year to March 2016(E) to the Support Services sector and on a PEG ratio of well under 1.

Estimates to Mar	2015 (A)	2016 (E)	2017 (E)
Revenue (£m)	130.5	135.4	141.9
PBT (£m)	5.7	7.6	8.3
EPS (p)	8.6	10.2	10.9
P/E (x)	13.3	11.2	10.5
EV/EBITDA	8.3	6.3	5.7
DIV (p)	1.0	1.5	1.8
Yield (%)	0.9	1.3	2.2

Source: Company, WH Ireland

Analyst: Nick Spoliar

*WH Ireland acts as NOMAD/Broker to WYG

#WH Ireland makes a market in WYG

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UPDATE: CARD FACTORY (CARD)

Store rollout continues apace

Share price: 320p | Market cap: £1.1bn

Shares in **Card Factory**, the UK's leading greeting card specialist are up 39% since we highlighted its attractions last November. A recent trading update has confirmed sales in the three months to 30 April 2015 jumped 7.5% with a net 19 new store openings. Now trading from 783 outlets the medium-term target is to expand this footprint to nearer 1,200 units. Strong cash flow is helping reduce debt and when interim results are unveiled on 22 September 2015 it will issue further guidance on plans to return excess cash to shareholders. Market conditions remain strong and its vertically integrated proposition as well as exclusive designs (up to 4,000 new cards annually) provides useful barriers to entry, also helping Card Factory generate robust margins. For the year to January 2016 consensus forecasts (Source: Capital IQ) point to EBITDA of £95m and EPS of 18p. Though no longer cheap, this is a quality operator – hold on.

Analyst: Miles Nolan

TRADING IDEA

Allied Minds (ALM)

FTSE 250 – Share price: 536p | Market Cap: £1.1bn | www.alliedminds.com

Daejan Holdings (DJAN)

FTSE 250 – Share price: 5735p | Market Cap: £925m | www.daejanholdings.com

Allied Minds is a private equity firm that specialises in technology investments. Shares have trebled since floating last June but with no earnings, or the prospect of any in the near future, the gains look unjustified. Trading at around 7x book value, the shares have been buoyed by overzealous investors whose enthusiasm is a microcosm of broader bullish investor sentiment.

For reinvestment, **Daejan Holdings**, the property investment company, offers a lower risk alternative. The group invests in UK and US property, the vast majority of which are freehold and long leasehold. The portfolio is broadly split between commercial and residential property. Around 80% of it is in

the UK, predominantly Greater London, with the remainder in the eastern seaboard of the US, largely New York City. Interim results to the end of September 2014 were solid with Net Rental Income rising 43% on the year to £32.5m, a pro rata yield of 4% for the full year, boosted by new lettings at the recently refurbished Africa House and a positive outcome to the rent review at the Strand Palace Hotel. With gearing down to 24%, Net Asset Value was up 10% to £75.04p over six months, placing the equity at an unwarranted discount of 23% and making the stock attractive for value investors.

Daejan

Actuals to Dec	2012 (A)	2013 (A)	2014(A)
Revenue(£m)	107.1	111.0	112.2
PBT (£m)	41.8	111.7	164.5
NAV per share (p)	5546	6044	6815
DPS (p)	76	79	82
Yield (%)	2.5	2.2	1.7

Source: Company

Analyst: John Goodall

INCOME ATTRACTIONS

Marks & Spencer (MKS)

FTSE 100 – Share price: 540p | Market Cap: £90bn | www.marksandspencer.com

Marks & Spencer has set its stall out for the year. It is looking to grow food sales, improve performance in general merchandising through margin progression and revenue growth, and continue its strong level of cash generation. At the full year top line revenue growth was flat, with a strong contribution from Food, up 3.4% to £5.2bn. The division has worked well to differentiate itself from the competition by providing specialist ranges and has grown sales over the last 22 consecutive quarters. Performance was offset by General Merchandising (GM) where revenue declined to £4bn, down 2.5%. Margin improvement in GM was up 190 basis points to 52.6% through better product purchasing and sourcing; it also saw customers spending more.

What we like

The business has generated long term stable earnings and cash flow and in the full year free cash flow was up 22% to £524m. M&S paid a dividend of £280.7m at the full year, so remains well covered by free cash flow, which is forecast to rise to £585m by analysts in 2015/16. The projected dividend yield is 3.5%, in line with the long-term payout ratio of approximately 50% of earnings. The business continues to improve operational efficiency through distribution and this investment programme is yielding margin improvements across the group. On current valuation we feel investors are buying an excellent income stock, with capital growth if M&S can gain market share within its target audience.

Estimates to Dec	2015 (A)	2016 (E)	2017 (E)
Revenue (£m)	10,311	10,573	10,922
PBT (£m)	600	709	770
EPS (p)	29.5	35.1	38.4
P/E (x)	18.3	15.2	14.1
DPS (p)	18.0	19.0	20.5
Yield (%)	3.3	3.5	3.8

Source: Company, Consensus forecasts (Bloomberg). Analyst: Luke Tribe

UPDATE: QUANTUM PHARMA (QP.)

Strong progress post IPO

Share price: 155p | Market cap: £194m

Quantum Pharma, a manufacturer and developer of niche healthcare products has not disappointed since joining AIM at 100p a share last December. Maiden preliminary results to 31 January 2015 revealed sales up 15% to £61.7m and underlying pre-tax profits ahead by 73% to £5.7m. Its subsidiary Colonis which develops and gains licenses for niche pharmaceutical products has almost doubled its pipeline to 60 products, in addition Quantum has secured a three-year contract to supply its products to the 774 strong drugs chain Well Pharmacy (formerly Co-op Pharmacy). The recent acquisition of Greece based Lamda for €9.7m looks a smart move, bringing increased product development and access to new markets. For 2016 consensus forecasts (Source: Capital IQ) suggest EBITDA of £14.3m and EPS of 10p. We profiled the company at 115p just five months ago but even after a 35% rally, we believe the shares remain undervalued.

Analyst: Miles Nolan

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FUND MANAGER SPOTLIGHT

Mike Prentis | BlackRock | www.blackrock.com

Venture capitalist turned fund manager Mike Prentis runs the £460m **BlackRock Smaller Companies Investment Trust**. Founded in 1906, this is a fund which aims to achieve long term capital growth by investing in a wide basket of shares – currently c.180 companies.

Prentis has been at the helm since 2002 and says, "We follow a buy and hold strategy so need to fully understand the drivers and fundamental strengths of a company before we invest". The fund backs successful management teams running differentiated growth companies and focuses on those with strong balance sheets as well as a reliable record of revenue growth. He also favours those that command a competitive market position and the ability to return cash to shareholders. Every year the team (which has over 90 years of combined experience in small and mid-cap investing) meet with up to 700 companies to seek out the best opportunities.

The universe he looks in spans the Numis Smaller Companies Index and AIM – a total of 2,000 stocks, but of these about 500 are potential prospects. He tends to hold the majority by value of the portfolio in 'core holdings' with up to one-third in smaller 'non-core' positions which have the scope to deliver attractive returns.

Approximately 40% of the fund is held in FTSE 250 stocks and with c.30% of the fund in AIM stocks this is one of the highest weightings among its peers. One smaller company he highlights is US based **Lifeline Scientific** which is the world's leading provider of equipment that preserves transplanted organs during transportation.Prentis tends to focus more on the company than the sector but his largest sector position (c.27%) is in Industrials (vehicle hire business **Northgate** and rental specialist **Lavendon** for example). He has gained exposure to the US by investing in promotional goods firm **4imprint~** and building products supplier **Tyman**. On IPOs, he says, "We have participated in some recent deals such as **Fever Tree** and **Eurocell** but our main focus is on companies which have been listed for some years".

Prentis admits consumer facing companies have been doing well (he holds **Topps Tiles** and **Ted Baker** for example) but investors should not rely on government spending – this is being cut in several well documented areas. He believes company valuations look reasonable compared to history, which follows a year of outperformance from larger companies. Over five years the Net Asset Value of the fund has increased 126% with the shares also more than doubling over the same time frame. The ongoing charges ratio is 0.7% .

Analyst: Miles Nolan

~WH Ireland provides paid for research services to 4imprint

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