



Sales Perspectives

Seven for Summer

Issue No: 2

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Introduction

► Seven for Summer

Welcome to the second issue of finnCap's Sales Perspectives. The first issue was dedicated to the stocks that my team and I believe will perform strongly across the year. Later on, we review our performance so far, reemphasising the stocks we believe continue to offer value, and the likely triggers to a re-rating.

This issue, however, is focused on the best companies we have met this Spring. These are trading ideas which we believe are actionable right now. As always, these are stocks we know well and ones we believe can outperform in testing market conditions. We warned in issue one that market conditions would be tough, and they certainly did not let us down! With further concerns on the strength of global economies, particularly weakening demand in the UK, and fears of a US slowdown, on top of Brexit anxiety, we do not expect more favourable markets to appear until later in the year. Therefore, good stock picking remains as important as ever.

We have attempted to include a range of ideas in this publication, whether it is a stock with a strong MOAT that can grow rapidly, recovery plays that are on the turn, value opportunities that have the potential to re-rate, or income providers with ever increasing cash flows. Please have a read of each idea, and let us know your thoughts, as feedback is always incredibly useful, both positive and negative. We wish this document to be as useful as possible and only by understanding your requirements can this be achieved. In addition, if you wish to meet any of the companies featured, do let me, or your direct sales contact know.

Now is probably a good time to introduce you to our new recruit. I am very happy to announce that Stephen Joseph has joined finnCap as a senior salesman. I'm sure many of you know Stephen, but if you don't, he has great small cap pedigree having worked at both Numis and Bank of America Merrill Lynch, prior to becoming Head of Investor Relations at Watchstone Group (its previous name already banned on these pages!). I'm sure Stephen will help promote our ideas/corporates further, and you will get to meet him in short order.

With all the pleasantries done, it leaves me to wish you happy hunting in terms of performance and I look forward to speaking to you about these ideas over the next few weeks.

Rhys

Note: The views expressed in 'Sales Perspectives' are solely those of the finnCap sales team.

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Performance Review

► Review of Issue 1

Looking at the performance of our 2016 key recommendations, if we were marking ourselves out of 10, I believe we would get a solid 7, this being the number of stocks in absolute positive territory since publication on the 22nd January. In terms of the spread of performance, Petra Diamonds leads the way, up a whopping 58% in the last 3 months or so, whilst at the foot of the table is Castleton Technology, which is down a not too disastrous 11%.

Company	Price (p)	Mid Price (p)	% Change
Petra Diamonds	70.8	112.5	58.90%
Skyepharma	365.25	472.125	29.26%
Somero	130	154	18.46%
Utilitywise	145	166	14.48%
Communis	40.3	43	6.70%
CityFibre	58.5	60	2.56%
Norcros	175	178.5	2.00%
dotDigital	48	47.5	-1.04%
Constellation Healthcare	146.5	141.5	-3.41%
Castleton Technology	77.5	68.5	-11.61%

► **Petra** – benefiting from a stabilising diamond price in the first half, and with growing production coming on-stream, leading to improving cash generation, it continues to offer good value.

► **Skyepharma** – up substantially on the back of its merger with Vectura. The combination is creating a powerhouse in respiratory product development with multiple value drivers. However, until the transaction completes there is little impetus for the share price to rise.

► **Somero** – the stock is up nicely on a good 2015 performance and positive start to 2016. We believe the company is well placed, with a wider product range and multiple market growth prospects.

► **Utilitywise** – improving terms from its suppliers, and a new management team getting to grips with the business, Utilitywise remains great value.

► **Communis** – the stock has yet to have recovered following the profit warning at the end of last year. It remains cheap, but what is the trigger to a re-rating? Not obvious at this point.

► **CityFibre** – following its transformational transaction in January, we expect increased newsflow on new contracts to drive interest. Long term, it offers huge value, definitely a core recommendation.

► **Norcros** – despite stating in a trading update that results are likely to come in marginally ahead of expectations, it remains ridiculously cheap, which maybe is an overhang from its large pension deficit. Again, the trigger for a re-rating remains hard to call currently, even after agreeing a new payment agreement with the pension trustees.

► **dotDigital** – marginally down in the last 3 months, but with a strong record of growth and operating in a fantastic area (marketing automation), where it has a leading product suite and growing international aspirations.

► **Constellation Healthcare** – Having announced good results for last year, the stock has underperformed on the back of one seller. With management over this month to meet investors, we believe the stock will recover strongly as the year progresses.

► **Castleton Technology** – Underlying performance by the group has been good, recently announcing that results will be ‘comfortably in line with expectations’. The rating is high, but so is its growth rate, and further expansion into new overseas territories increase the opportunity for the group.



4imprint

► Scope for further returns to investors

4imprint supplies merchandise, which is customised with the logo or name of an organisation to promote a brand, service or product. The majority of its sales are in the large and highly fragmented North American market, worth c.\$23bn per annum. We believe 4imprint has a strong economic MOAT, allowing it to continue to grow rapidly. The outcome of this growth, we believe, will increase free cash flow, and lead to ever larger dividend returns to shareholders.

The North American promotional merchandise market is highly fragmented, with over 20,000 distributors operating in total, and yet only 885 distributors sales of \$2.5m per annum or more. 4imprint believe they have just over 1% share of the total market, and yet it is the largest operator by a factor. Not only are many of the smaller distributors limited in terms of geographical coverage, product range or marketing spend, but its 4imprint's clever use of data analytics that allows it to effectively target customers, offering the potential for substantial market share gains, even in a flat market.

Marketing is central to driving organic growth and the company uses a combination of catalogue marketing, internet search optimisation and e-mail campaigns to grow sales. The Group uses its sophisticated data techniques and extensive database to target existing customers with e-mails, special mini catalogues, offers and even free samples.

The result of this investment has been 4imprint's ability to double sales in the last 4 years against a sluggish market growth rate (c.10% over the same period). Given the size of the North American market, 4imprint should continue to enjoy high revenue growth as the group pushes out this proven marketing model.

However, management state that due to the above and an increasing operating expense line, operating margins should be stable. They have, however, risen from 5.9% to 6.7% over the past two years, alongside average sales growth of 23% per annum. In our forecasts, we look for further margin expansion, reaching 7.1% in FY18, whilst targeting 12% revenue growth per annum for the next 3 years.

4imprint's cash generation, though strong, has been held back historically by its significant pension deficit payments. These payments substantially reduce this financial year, and with net cash on the balance sheet already, this leaves the company in an enviable position. With no sizeable competitors to acquire for synergy benefits, the widest product range in the market already and reducing bolt on activity, M&A opportunities looks non-existent. Therefore, we predict the company to increase returns to shareholders. We expect surplus cash to be used to supplement dividend payments, and that these can grow substantially over the next couple of years. In FY17 we forecast

FCF of \$28m, and a dividend payment of \$14m, leaving excess cash of \$14m – could the majority of this be returned too?

4imprint has a proven track record of gaining share in a large and highly fragmented market. With a clean balance sheet, now unencumbered by pension payments and already sitting on net cash, we believe the group is well placed to produce strong earnings growth and enhanced dividend payments. Trading on an attractive rating for a growth stock of only 20x, this has plenty of upside potential.

Leading direct marketer of promotional products in the USA, Canada, UK and Ireland



‘Operations are focused around a highly developed direct marketing business model’

4imprint

► BUY

Ticker	FOUR	%	1M	3M	12M
Price	1,344.0p	Actual	+6.6	+13.1	+26.8
Target Price	1,540.0p	Relative	+6.6	+9.6	+42.1
Upside	15.0%				
Market Cap	£377.5m				
Index	FTSE All Share				
Sector	Media				
Net Cash	\$18.4m				
Shares in Issue	28.1m				
Next Results	H1 - July 2016				

Share Price Performance



Source: Thomson Reuters

Year ending December (\$m)

Data	2014A	2015A	2016E	2017E	2018E
Sales (\$m)	415.8	497.2	560.4	632.7	714.3
Adj EBITDA (\$m)	29.5	35.5	41.4	47.1	53.4
Adj PBT (\$m)	27.9	33.5	38.4	44.1	50.4
Tax rate (%)	28	27	28	29	30
Adj EPS (FD) (c)	71.5	87.5	97.6	109.8	122.8
DPS (c)	32.4	38.9	44.9	51.6	59.4

Ratios

EV/Sales (x)	1.3	1.1	0.9	0.8	0.7
EV/EBITDA (x)	18.0	14.9	12.8	11.3	9.9
P/E (x)	27.3	22.3	20.0	17.8	15.9
Yield (%)	1.7	2.0	2.3	2.6	3.0
Cash flow yield (%)	2.7	1.9	4.5	5.1	5.8
EPS growth (%)	n/a	22.3	11.5	12.5	11.9

Source: finnCap estimates



Expert content and insight, engaging events, smart digital technology

Centaur Media

► Poised to exploit its evolving marketplace

Centaur is a London based B2B magazine and digital publishing group which operates in the following segments: digital and print publishing; event and information; research data and analysis; exhibitions; digital information; training and event activities, as well as provision of agency services.

Historically, the company has focused on magazine publishing, with the majority of its revenue derived from advertising and events. The business was highly segmented with very little communication between brands. Over the past two years, under the direction of its new CEO, the company has focused on developing itself into more of a content manager than a publisher, and increasing its digital presence. It has consolidated its businesses, getting the brands to share costs, whilst also investing heavily to develop a single platform, enabling its customers to access its content however they wish, including via smartphones and tablets.

The company is migrating its revenue to 'paid-for content' (subscriptions for the digital content, and access to events) versus the advertising income it has historically relied on. This is creating a more even revenue model on better margins and providing greater visibility. The move to subscription sales also enables Centaur to focus on the reader, increasing the quality of its content, and therefore increasing brand awareness and improving its reputation. In the past, advertising

accounted for c. 50% of total revenue. For FY15, this has reduced to c.33%, and the combination of subscription and event revenue has grown to c.67% from c.48% three years ago. The company believes it has turned the corner with the 'heavy lifting' done leaving it well placed to exploit its changing market place.

However results for FY15 were disappointing, and this has seen the share price decline by 25% year to date. Its cash conversion was well below expectations, at only 31% of operating profit, compared to its usual 100%+. This also saw its net debt increase to £17.9m (£14.7m). We believe the issue came from the move to its new platform, leading to a delay and backlog in chasing payments. However, management say this issue has now been fixed, with the company guiding for operating cash conversion of 120-130% for FY16, helping to underpin its attractive dividend policy.

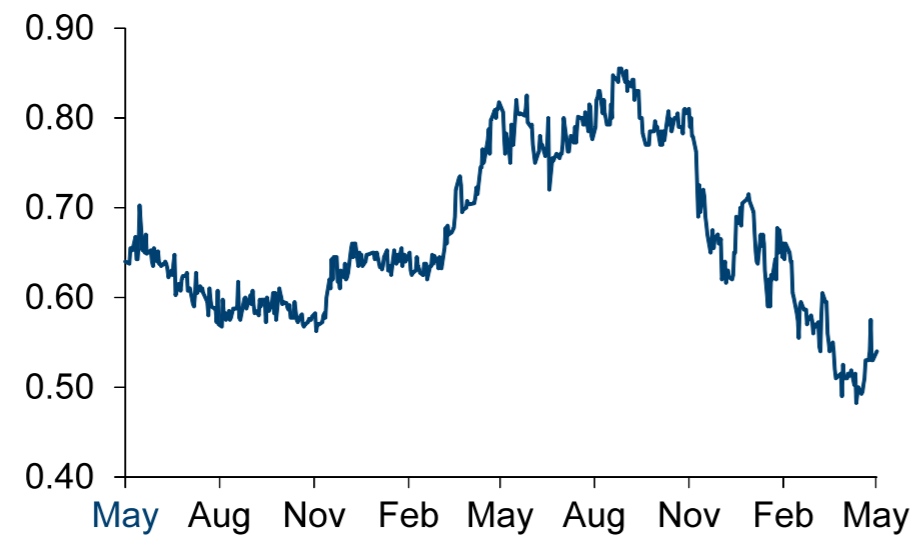
We think Centaur is an interesting story of evolution of a publishing company led by a credible CEO. The company owns a portfolio of powerful brands, an enhanced product offering, (hopefully!) strong cash generation and consequently a good platform for potential organic and acquisitive growth. We believe that market sentiment is low following last year's hiccup, putting the stock on a very attractive 9.5x rating, and offering a yield of over 6%. With a trading update out next week, it is time to buy now.

Centaur Media

► BUY

Ticker	CAU	%	1M	3M	12M
Price	50.25p	Actual	+2.9	-20.3	-30.3
Target price	76p	Relative	+2.9	-22.8	-21.9
Upside	41%				
Market Cap	£75.1m				
Index	FTSE All Share				
Sector	Media				
Net Debt	£17.9m				
Shares in Issue	143.7m				
Next Results	28-Jul-16				

Share Price Performance



Source: Thomson Reuters

‘An interesting story of evolution of a publishing company led by a credible CEO’

Year ending March (£m)

Data	2014A	2015A	2016E	2017E
Sales (£m)	72.9	70.5	73.8	77
Adj EBITDA (£m)	9.9	10.5	14.7	15.7
Adj PBT (£m)	6.9	6.9	10.4	11.4
Tax rate (%)	18.8	18.8	-	-
Adj EPS (FD) (p)	5.0	4.0	6.0	6.0
DPS (p)	3.0	3.2	3.3	3.5

Ratios

EV/Sales (x)	1.23	1.33	1.02	0.98
EV/EBITDA (x)	9.1	5.2	7.2	6.6
P/E (x)	10.5	13.1	8.7	8.7
Yield (%)	5.7	5.7	5.7	5.7
Cash flow yield (%)	22.58	6%	-	-
EPS growth (%)	150	-20	50	0.0

Source: consensus estimates

Finsbury Food

► Outperforming in a difficult market



Finsbury Food is one of the largest speciality bakery groups in the UK. The business is the second largest ambient cake maker in the UK after Mr Kipling, making premium and event cakes which are sold both whole, and in small snacking cake formats. The company also makes a comprehensive range of healthy eating artisan breads, as well as morning goods, which are available either fresh or frozen. The company owns bakeries in multiple locations around the UK and also own 50% of an overseas operation called Lightbody Stretz. It has a large and diversified customer base in the grocery retail market as well as the 'out of home eating' foodservice sector.

Finsbury used to be a business suffering from an over-burdened balance sheet, general lack of focus in its operations, a weak management team and margins that were firmly in the doldrums. A new management team headed by John Duffy (CEO) and Steve Boyd (FD) took over and set about putting a plan for recovery into place, primarily focused on sorting out the product ranges, streamlining operations and getting back to cash generation to both reduce debt and give the business the capability to expand through acquisition.

Following a placing in November 2012, and the receipt of £21m from the sale of their 'Free From' joint venture, the company invested in new packing lines at the Lightbody facility in Hamilton, Scotland, as well as new product development and automation at the Memory Lane site in Cardiff. In addition, sensible price increases, better structured contracts, and more appealing product ranges helped the business return to growth and boost profit margins. The balance sheet was completely transformed.

Leading speciality bakery group targeted at growing channels and market niches

This allowed management to enter the foodservice market through the acquisition of Fletchers. A segment worth c.£900m per annum, where 70% of sales is in morning goods, and 58% of product is sold through coffee shops, the transaction radically diversified Finsbury's customer base away from the large grocery chains.

The latest results led to upgrades, and showed continuing progress across the board, especially in Fletchers. Group revenue rose 46%, reflecting acquisitions, though underlying organic growth was a healthy +7.4%. Further efficiencies came through higher production volumes, with pre-tax profits ahead by 84%. EPS rose 38% to 4.4p and the dividend went up by 12% to 0.9p. In the outlook statement management believe that they had laid down strong foundations, that the first half was a good result and 'we expect this to continue into the second half'. On consensus numbers Finsbury trades on 12.9x, and with a dividend yield of 2.4%. This looks good value for what is an excellent company, executing a strategy based around continuing to do more of the same, which is delivering improving net returns to its shareholders.



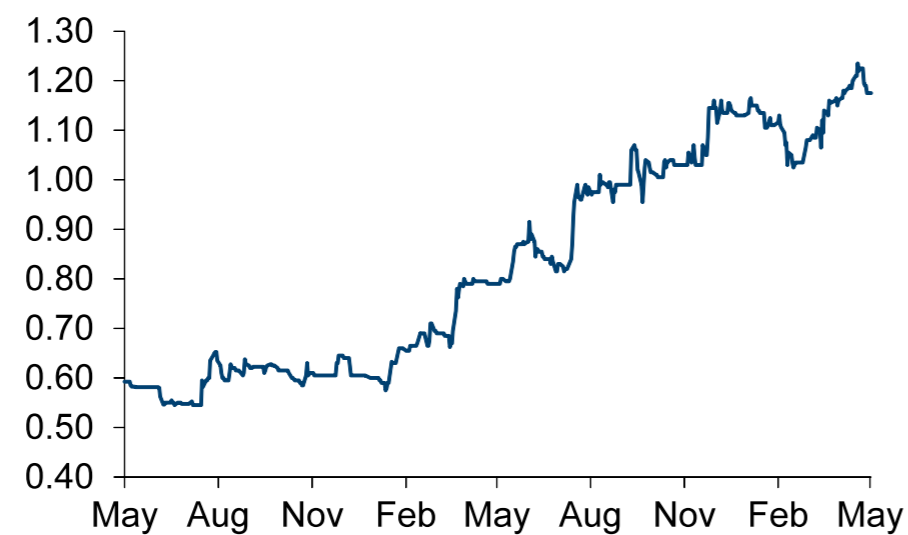
‘The acquisition of Fletchers has radically diversified the customer base’

Finsbury Food

► BUY

Ticker	FIF	%	1M	3M	12M
Price	116p	Actual	+2.2	+5.9	+47.8
Target price	127p	Relative	+2.2	+2.5	+65.7
Upside	9%				
Market Cap	£151m				
Index	FTSE AIM All Share				
Sector	Food Producers				
Net Debt	£21.1m				
Shares in Issue	130.4m				
Next Results	21-Sep-16				

Share Price Performance



Source: Thomson Reuters

Year ending March (£m)

Data	2014A	2015A	2016E	2017E
Sales (£m)	175.7	256.2	310	313
Adj EBITDA (£m)	10.7	15	24.2	25.7
Adj PBT (£m)	6.6	11.6	16.1	16.3
Tax rate (%)	22.7	21.6	20.6	19.6
Adj EPS (FD) (p)	7.3	7.7	9.1	9.3
DPS (p)	1.0	2.5	2.8	3.0
Ratios				
EV/Sales (x)	0.9	0.66	0.54	0.53
EV/EBITDA (x)	14.7	9.3	6.9	6.6
P/E (x)	15.9	15.1	12.7	12.5
Yield (%)	0.9	2.2	2.4	2.5
Cash flow yield (%)	-1.03	6.81	-	-
EPS growth (%)		5.50	18.60	1.90

Source: consensus estimates



UK's leading distributor of technical fluid power products

Flowtech Fluidpower

► A leading consolidator in niche markets

The group is a leading player in the fragmented UK fluid power distribution market, with a small market share and acquisition opportunities in both the UK and Europe. It has a unique position in its market as a super-distributor, selling almost entirely to other distributors, and sitting between OEMs and resellers and distributors. Its product catalogue is viewed as the 'fluid power bible' and also helps support Flowtech's unique position. Management have an exciting growth plan in place, based on acquisitive growth, organic growth and margin expansion.

The group is targeting three distinct verticals in its channel development, which are OEM accounts, distributor end-users, and on-site maintenance customers. Each will leverage the group's central services and offer the group substantial growth prospects. Management have a proven track record in acquisitions, having made and integrated several already since float, and has an active pipeline lined up. We estimate that the group has firepower of c.£10m in hand.

Management has a strict approach to acquisitions, with a clear view of what is good value in the sector and what synergies and integration benefits can be generated. It has paid between 3x and 6x EBIT for recent acquisitions and we believe that this is a reasonable rule-of-thumb for future acquisitions.

In addition, management are also targeting organic growth, and has a number of drivers in place. This includes product range expansion, opportunities to extend geographic coverage, and new customer contract wins, enhanced by the new trading agreement with EATON Corp. In addition, market share gains will be targeted through the group's online sales strategy. The group sells 64% of its catalogue of products through online and electronic means, with a multi-currency, multi-lingual online sales platform offering scope to scale up sales without significant additional cost. This sales platform, plus its China sourcing, offers a platform on which to build overseas sales.

The group's strategy is to remain a niche provider, rather than a general distributor. It also differentiates itself by offering a technical sell, thereby offering a value-add proposition. This positioning offers the prospects of higher margins, and also more margin protection than most general distributors.

Its Chinese sourcing, allied to increasing its own-brand offering should assist gross margins. Increasing revenues will enable increased overhead recovery rates – this should provide a decent drop-through to profitability too.

We think Flowtech offers an interesting proposition, despite tough current underlying trading conditions. It has a number of levers to use and we believe the group will be substantially larger in the medium term. It is also on a highly attractive rating of 9x for FY16, whilst offering a 4% yield. Expect acquisitive growth to drive the share price in the second half of the year.

‘The group’s strategy is to remain a niche provider rather than a general distributor’

Flowtech Fluidpower

► BUY

Ticker	FLO	%	1M	3M	12M
Price	139.3p	Actual	+10.7	+29.5	+16.2
Target Price	187.0p	Relative	+10.8	+25.4	+30.2
Upside	34.0%				
Market Cap	£60.0m				
Index	FTSE AIM All Share				
Sector	Industrial Engineering				
Net Debt	£9.0m				
Shares in Issue	43.1m				
Next Results	Interims October				

Share Price Performance



Source: Thomson Reuters

Year ending December (£m)

Data

	2014A	2015A	2016E	2017E
Sales (£m)	37.8	44.8	54.7	57.5
Adj EBITDA (£m)	6.6	7.4	8.9	9.4
Adj PBT (£m)	4.2	6.7	8.0	8.5
Tax rate (%)	28	16	19	20
Adj EPS (FD) (p)	11.6	12.9	14.9	15.8
DPS (p)	5.0	5.3	5.5	5.8

Ratios

EV/Sales (x)	1.8	1.5	1.3	1.2
EV/EBITDA (x)	10.4	9.4	7.8	7.3
P/E (x)	12.0	10.8	9.4	8.8
Yield (%)	3.6	3.8	3.9	4.2
Cash flow yield (%)	2.4	8.3	5.4	9.7
EPS growth (%)	n/a	11.2	15.4	5.8

Source: finnCap estimates

Solid State

► A niche player in a nascent market

Solid State is a manufacturer and design-in distributor to the electronics industry. It focuses on providing specialist components and systems to niche markets including aerospace, environmental, government, oil & gas and transportation markets. The group has had a mixed last 12 months, following the loss of a significant contract, but with its market cap down to £30m, and trading on a single digit rating, we believe Solid State offers great value for a growing business with expansion potential across multiple industries.

Solid State operates through two divisions: Solid State Supplies, which distributes components to UK OEMs, including semiconductors, control and communications switches, power management units and specialist LED lighting; Steatite, which designs and manufactures products and solutions, including bespoke lithium battery packs, rugged mobile computing/radio solutions, microwave antennae, and industrial computer hardware and software.

Solid State's diversity allows it to outperform challenging markets, since its revenues are not predicated on any one industry. In addition, as products become more electronic based, it sees substantial demand drivers for what it offers. Another key aspect we like is its high barriers to entry, ranging from regulatory and permission requirements all the way up to IP protected products. The group has UN approval for shipping hazardous material including lithium batteries, whilst the company is one of only a handful that can work with the MOD regarding encrypted data.

However, 2015 was a difficult year for the group. Having seen the shares double on the news of winning a major Ministry of Justice contract, the group's performance was impacted by first a delay to the contract roll out, and then again, when the contract was terminated (through no fault of its own). Whilst the company is expecting a large compensation payment from this, it also has a solid underlying business, as highlighted in its last trading update. The company stated it was trading in line with market expectations, whilst also reporting a healthy order book of some £15.3m.

We also believe the group will boost underlying performance through further acquisitions, and that it has a pipeline of opportunities it is working on. Future transactions may include adding further product capability, adding additional production capability, or the ability to enter a new niche market. Management look to acquire on a 3 year weighted post tax profit multiple of 6x or less, making each deal earnings enhancing. In addition, it has debt facilities of £5.5m, of which c.£2.5m is drawn – pre MOJ compensation cheque - so it has the ability to acquire without seeking shareholder capital.

Solid State has a diverse and global customer base that should allow it to grow steadily over the medium term. It also has a strong record of expansion through acquisition, and we see this continuing. Operating in niche markets, its reputation, product knowledge or IP and regulatory clearance provide key attractions. Trading on a FY17 P/E of 9.4x, 8.5x EBITDA and offering a 3.7% dividend yield, the shares look good value. With prelims planned early in July, we expect the shares to recover into H2 as investor demand grows.



High value-add manufacturer and specialist design-in distributor to the electronics industry

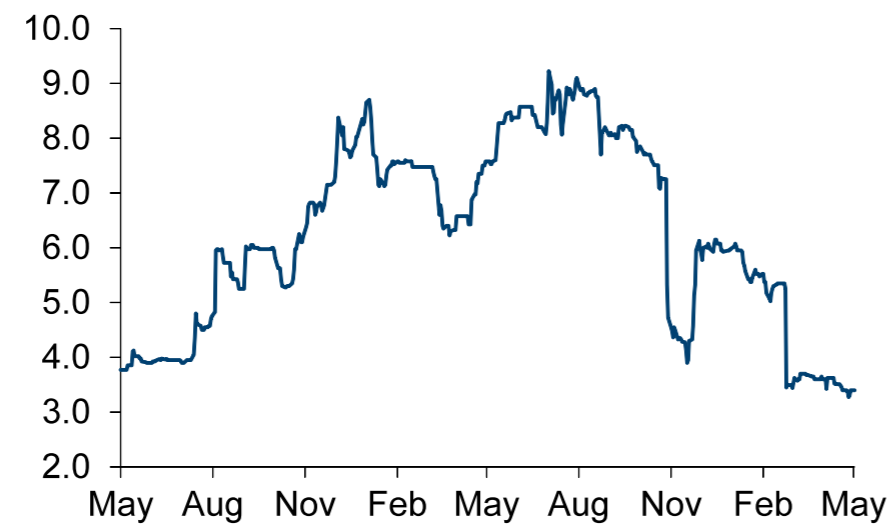
‘Solid State’s
diversity allows
it to outperform
challenging
markets’

Solid State

► BUY

Ticker	SOLI	%	1M	3M	12M
Price	328p	Actual	-6.8	-38.5	-51.3
Target price	420p	Relative	-6.8	-40.4	-45.4
Upside	26.80%				
Market Cap	£27.7m				
Index	Aim All Share				
Sector	Electronics and components				
Net Cash	£4m				
Shares in Issue	8.4m				
Next Results	05-Jul-16				

Share Price Performance



Source: Thomson Reuters

Year ending March (£m)

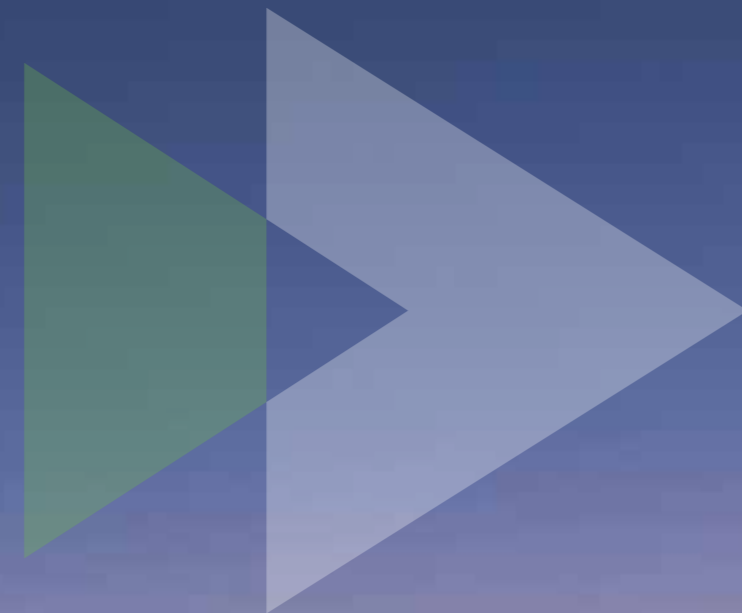
Data	2014A	2015A	2016E	2017E
Sales (£m)	32.1	36.6	43.9	41.8
Adj EBITDA (£m)	5.6	3.6	3.8	4.0
Adj PBT (£m)	2.2	3.0	3.2	3.4
Tax rate (%)	0.3	0.1	-	-
Adj EPS (FD) (p)	25.3	34.9	34.9	36
DPS (p)	9.0	12.0	12.0	13.0

Ratios

EV/Sales (x)	0.94	0.83	0.63	0.66
EV/EBITDA (x)	5.4	8.4	7.3	6.9
P/E (x)	13.2	9.5	9.5	9.2
Yield (%)	2.7	3.6	3.6	3.9
Cash flow yield (%)	0.48	0.48		
EPS growth (%)	13%	40%	0%	3%

Source: consensus estimate

Multi-utility supplier,
delivering gas, electricity,
landline, broadband
and mobile services to
residences and businesses



Telecom Plus

► A high yielder set for a return to growth

Telecom Plus trades as Utility Warehouse, a discount club which sells competitively priced bundles of electricity, gas, broadband, and fixed and mobile telephony to predominantly residential customers. The group relies on satisfied customers to spread the word, and approximately 10% of customers become 'partners' creating what is currently a 45,000-strong self-employed salesforce. This allows them to keep marketing costs low, and focus on their key differentiating factors; fair and consistent pricing, a single utility bill, and exceptional customer service. It is this ethos that has driven subscribers to 595,000, taking on average just over 3 services each.

Sentiment has however been dampened by a disappointing outcome from the regulatory review by the Competition & Markets Authority (CMA) in mid-April. The review failed to cap the practice of offering discounts to new customers at the expense of existing customers (who are on higher tariffs) – a structure commonly used by the Big 6 Energy players. A cap would have made Telecom Plus' offering more competitive, effectively stopping the Big 6 from using their scale to outcompete.

Yet, the review did offer proposals to remove restrictions on discounts, bundling, and the number of tariffs each supplier can offer. This will permit Telecom Plus to offer more options on bundled packages – something that will become increasing crucial as they broaden their offering this summer with the introduction of insurance as an additional service. There are also plans to introduce a water service when the market is deregulated.

These new services, we believe, will help boost average revenue per user (ARPU), which slipped to £107 in the year to 31 March 2015, from £113 in 2013, as a result of the low energy price environment. In addition, with falling energy prices now coming to an end, and the company expecting the first of the Big 6 to make initial price increases later this year, our analyst, Andrew Darley, is forecasting monthly ARPU to begin rising again, to £125 in the second half of 2016.

Meanwhile, the unfavourable energy price environment pushed Telecom Plus to explore other initiatives to drive growth. This includes programs such as replacing all light bulbs in new customers' homes with energy efficient LED bulbs for free. This offer is available to customers that apply for at least five services for a minimum of four years, and roughly 45% of new customers have been signing up for this; so they are spending more and are locked into a longer contract term. This effectively increases margins and provides more visibility of revenue.

This better quality revenue, coupled with an expected return to growth in ARPU, makes Telecom Plus look exceedingly good value, trading on a market rating despite its more positive growth outlook. In addition, it already offers a very attractive yield of 5%, and with the company targeting a weighty 80% pay-out ratio going forward, this has room for substantial improvement.

‘New customers are spending more and are locked into a longer contract term’

Telecom Plus

► BUY

Ticker	TEP	%	1M	3M	12M
Price	936.5p	Actual	+1.7	-4.9	+16.3
Target Price	1,230.0p	Relative	+1.8	-7.9	+30.4
Upside	31.0%				
Market Cap	£751.6m				
Index	FTSE All Share				
Sector	Fixed Line Telecommunications				
Net Debt	£52.5m				
Shares in Issue	80.3m				
Next Results	June 14th prelims				

Share Price Performance



Source: Thomson Reuters

Year ending March (£m)	2014A	2015A	2016E	2017E
Data				
Sales (£m)	659.7	729.2	736.2	801.8
Adj EBITDA (£m)	39.9	49.7	52.6	56.0
Adj PBT (£m)	42.5	51.9	54.1	57.5
Tax rate (%)	17	19	16	15
Adj EPS (FD) (p)	47.7	52.5	56.0	60.1
DPS (p)	35.0	40.0	46.0	49.0
Ratios				
EV/Sales (x)	1.2	1.1	1.1	1.0
EV/EBITDA (x)	20.1	16.2	15.3	14.4
P/E (x)	19.6	17.9	16.7	15.6
Yield (%)	3.7	4.3	4.9	5.2
Cash flow yield (%)	-2.9	3.5	6.7	11.3
EPS growth (%)	21.0	9.9	6.8	7.3

Source: finnCap estimates

Victoria

► Consolidating the European carpet sector

If it's good enough for Warren Buffet, then it's good enough for Geoff Wilding, the CEO of the UK's largest carpet manufacturing business Victoria. Back in 2001, when everyone else was looking at the dot coms, Warren Buffet set about buying up a selection of dowdy flooring businesses culminating in his biggest non-insurance purchase ever – Shaw Industries. The attraction? Cashflow, and lots of it, given plants tend to be relatively inexpensive and last for years. Roll forward 15 years and with 5 acquisitions under his belt Geoff is midway through his plans to consolidate the UK, Australian and hopefully soon, the European carpet markets. As it stands today, the business is set to generate sales of £256m and profits before tax of £17m for the year end March '16.

The plan, and the management team is very open about it, is to carry on acquiring strong, well-positioned businesses in an attempt to reach 'scale' (sales of c.\$1bn or £700m) so that they attract the attention of the likes of Shaw, and eventually get bought. Indeed, Shaw and its rival Mowhawk, tried growing organically in the UK before, but failed and exited. Both Shaw and Mowhawk already enjoy high market shares in the US, and so the only way for them to achieve meaningful growth is likely through overseas acquisition. All seems sensible.

The price? Geoff thinks somewhere between 10-12x EBITDA for a fully formed pan-continent platform, and here's the rub; Victoria has historically paid a very low 5-6x EBITDA for the 5 deals done to date, or 4-5x post a working capital turn. So shareholders should substantially benefit from an arbitrage on the valuation uplift from private to public ownership, before enjoying a sizeable take out premium.

The big question is can this continue? Even in light of the failed Belgium Lano acquisition we think it can. This view is predicated on the fact that the market is highly fragmented with c.300 suppliers in the UK and Europe, enough to fill up a pipeline for some time to come. Many of these businesses were also founded in the 1980's DIY boom with owners close to retirement; Victoria are the only buyers in town. We're given further comfort from the company's disciplined approach to acquisitions, from price paid to a clear business integration plan/modelling of synergies. Acquisitions aside, the business remains in excellent health with its last trading update leading to upgrades, and we expect more upside to come. Trading on a FY17 rating of 13x, it is not expensive and we think the stock can continue to advance from here.



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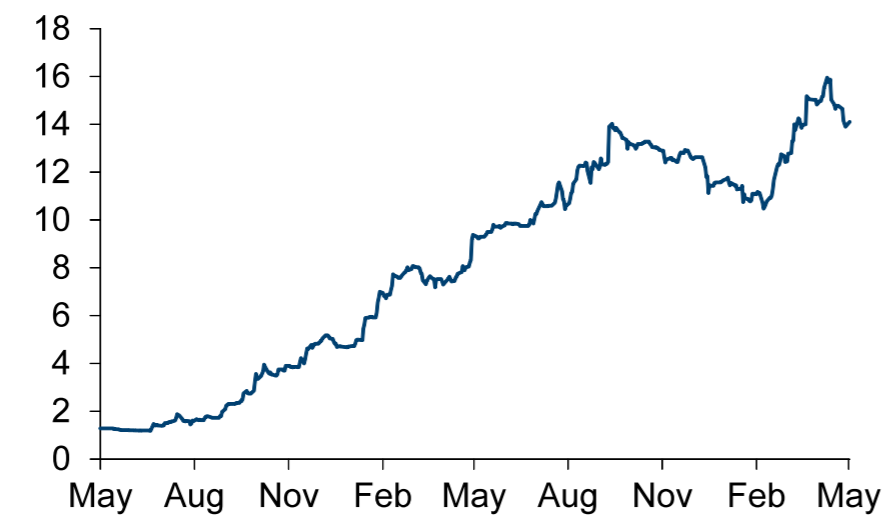
‘The business remains in excellent health with its last update leading to upgrades’

Victoria

► BUY

Ticker	VCP	%	1M	3M	12M
Price	1,445p	Actual	-6.2	+30.9	+80.2
Target price	1,817p	Relative	-6.1	+26.7	+102.0
Upside	26%				
Market Cap	£262.9m				
Index	Aim 100 Index				
Sector	Household Goods				
Net Debt	£81.1m				
Shares in Issue	18.2m				
Next Results	01-Aug-16				

Share Price Performance



Source: Thomson Reuters

Year ending March (£m)

Data

	2014A	2015A	2016E	2017E
Sales (£m)	71.4	128.3	256	311.5
Adj EBITDA (£m)	5.1	11.8	24.7	34.6
Adj PBT (£m)	2.3	-2.95	16.9	25.7
Tax rate (%)	0.7	1.6	-	-
Adj EPS (FD) (p)	32	45	80	109
DPS (p)	8.0	0.0	-	10.0

Ratios

EV/Sales (x)	3.7	2.33	1.03	0.84
EV/EBITDA (x)	51.8	25.3	10.6	7.6
P/E (x)	45.1	32.1	18	13.2
Yield (%)	0.1	0.0	-	0.7
Cash flow yield (%)	0.46	0.5	-	-
EPS growth (%)	-	40.6	77.8	36.3

Source: consensus estimates



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The recommendation system used for this research is as follows. We expect the indicated target price relative to the FT All Share Index to be achieved within 12 months of the date of this publication. A 'Hold' indicates expected performance relative to this index of +/-10%, a 'Buy' indicates expected outperformance >10% and a 'Sell' indicates expected underperformance of >10%.

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