

14 September 2011

## Avingtrans

Year End	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
05/10	28.6	0.6	3.0	0.0	18.8	N/A
05/11	36.3	1.6	5.6	0.4	10.1	0.7
05/12e	41.4	2.1	6.2	0.9	9.1	1.6
05/13e	46.0	2.7	7.9	1.2	7.2	2.1

Note: \*PBT and EPS are normalised, excluding intangible amortisation and exceptional items.

### Investment summary: Benefits of a global view

Avingtrans' results demonstrate the clear benefits of the global strategy both in terms of target markets, global customers and manufacturing approach. With the group having emerged from the difficulties during the recession in a much stronger position, we feel the results vindicate the belief that OEMs are searching for strategic partners who can support them on a global stage. With many customers shared across divisions, Avingtrans has shown itself to be an increasingly important part of that supply base, in our view. While we are not complacent regarding the potential economic challenges that lie ahead, and hence are easing our forecasts to reflect the potentially slowing environment, the group appears well placed for the future.

### Results demonstrate good progress

Revenues increased by 27% to £36.3m (2012: £28.6m), in line with our forecasts, while gross profit margins improved to 29% (2010: 26%) and operating profit more than doubled to £1.7m (2010: £0.8m). With tax benefits arising from R&D credits and US tax losses, EPS came in ahead of our expectations at 5.6p (Edison 4.2p). Encouragingly, cash outperformed with net debt reducing by 15% to £6.6m leaving gearing of 29%. Given the encouraging performance, the board reintroduced a final dividend of 0.4p with a progressive policy thereafter.

### Market opportunity focused on global growth

The results show that Avingtrans' strategy to support global OEMs provides a significant opportunity. With emergent concerns regarding the economic outlook once again, we highlight the strong and growing presence in China and the increasing value of long-term contracts being supplied by the group. With end markets providing structural growth, we feel the business is well placed for the future.

### Valuation: Promising signals

We believe these results provide a number of promising signals that support a view that Avingtrans is a long-term growth play. However, we feel that the current rating of 9.5x CY11 EPS does not fully reflect this. Our SOTP valuation has eased to 80p/share, reflecting lower peer multiples.

Price 56.5p  
Market Cap £14m

#### Share price graph



#### Share details

Code AVG  
Listing AIM  
Sector Industrial Engineering  
Shares in issue 25.5m

#### Price

52 week High 70.0p Low 39.5p

#### Balance Sheet as at 31 May 2011

Net debt/Equity (%) 28.9  
NAV per share (p) 89.7  
Net debt (£m) 6.6

#### Business

Avingtrans (AVG) is a supplier of highly engineered components and services to the energy, medical, scientific and research communities, traffic management, automation and aerospace industries worldwide.

#### Valuation

	2011	2012e	2013e
P/E relative	96%	100%	87%
P/CF	4.8	4.0	3.2
EV/Sales	0.6	0.5	0.4
ROE	6%	6%	8%

#### Geography based on revenues (2011)\*

UK	Europe	US	Other
70%	21%	6%	3%

\*Note:excludes eliminations

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## Prelims highlight benefits of the global model

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The prelims demonstrate that the model of supplying into global OEMs was bearing fruit and provides a resilience to wider economic concerns in the West. With a strong recovery underpinned not just from a recessionary bounce but also by new long-term contracts, we feel Avingtrans is now better positioned to ride any future turbulence than was previously the case. With new opportunities being discussed, target markets set for structural growth, and potential M&A activity being considered, we believe that continued progress should be achievable.

### Financials

The prelims showed a good recovery in line with our forecasts, with revenues up 27% to £36.3m (2010: £28.6m), while gross profit margins increased to 29% (2010: 26%), operating profit more than doubled to £1.7m (2010: £0.8m) and EBITDA increased by 32% to £3.2m (2010: £2.5m). With tax benefitting from UK R&D credits and tax losses in the US, the effective rate was just 11.3% and hence adjusted EPS came in at 5.6p, ahead of our 4.2p estimate.

The most impressive thing in our view was the cash performance, with net debt at the year-end down 15% to £6.6m (2010: £7.8m) and gearing continuing its downward trend, standing at 29% (36% at 31 May 2010). Given the confidence of the board, a final dividend of 0.4p was reinstated and a progressive dividend policy was announced.

### Divisional performance encouraging

While there were variances in business stream performance driven predominantly by differing budgetary pressures, we feel that this demonstrates the strength of the combined model.

#### **Aerospace (35% of 2011 revenue)**

Both Sigma and C&H had their best year yet, with sales up 32% to £12.7m (2010: £9.6m). Importantly in our view, Sigma China contributed a small profit for the year as a whole and this is set to be a key growth driver over the coming years as further work flows through China. Likewise, Sigma in the UK benefited from the long-term contracts signed with Eaton, Meggitt and ITA, while C&H's £5m contract extension with Rolls-Royce provided momentum and is identifying further opportunities. As a result of the improving performance, operating margins progressed to 8% (2010: 1%) generating an operating profit of £1.0m.

**OUTLOOK:** Given the structural growth nature of the Civil Aerospace market and the significant backlogs at Boeing and Airbus to support that, we view the environment for the Aerospace division as robust for a sustained period of time. We are forecasting 16% growth in revenues for FY12, followed by a further 10% in FY13, with a steady margin progression into double-digit levels.

With opportunities to expand relationships with existing long-term partners and new opportunities through further manufacturing in China, we feel that growth prospects remain undiminished. As global OEMs seek suppliers to take on larger packages of work, we believe Avingtrans' growth, global presence and importantly delivery record, should make it a supplier of choice. To enhance this further, Avingtrans is seeking to gain a presence for Sigma in the US market over the next 12-18 months, which would then provide it with a presence in all major existing and, through China, developing aerospace markets.

### Energy & Medical (36% of revenue)

Performance in Energy & Medical was more mixed, with recovery taking longer than in other divisions, although we note that the performance of Metalcraft was much improved during H2 with sales up 19% in H2 vs H1. With Crown providing a significant drag it was therefore pleasing to see the division post a 6% increase in turnover to £13.0m (2010: £12.2m) while margins progressed to c 2% from a small loss in 2010, generating an operating profit of £0.2m.

OUTLOOK: There are a number of promising factors across the division, with the benefits of the Cummins contract now starting to come through and opportunities in the wider medical market also supporting the international growth agenda. As a result, we view the future as promising.

While the progress being made in Metalcraft is encouraging, the slower ramp-up of the new MRI products for Siemens, combined with the ongoing uncertainty surrounding Crown, has caused us to take a more cautious view of progress and we have eased back our forecasts. Despite this, we estimate growth of c 17% in FY12 and FY13, but a slower pace of margin progression.

### Industrial Products (29% of revenue)

JenaTec has been the division that has rebounded strongest from the recession with a broad-based recovery generating accelerating orders throughout the year, allowing an increase in revenues of 56% to £10.6m (2010: £6.8m). Given this strong recovery and the previous cost cutting measures implemented, operating margins surged to 10% (2010: 1%) and operating profit of £1.0m was earned. While recovery was general, there were important areas of progress that demonstrate why the business is better placed in the long term with the “vertical integration” strategy highlighted by further orders for Avingtrans’ actuation products and geographic expansion continuing in the US. In another signal of widening applications, JenaTec won its largest single medical contract with a three-year, £1.8m award from a European medical equipment manufacturer.

OUTLOOK: While JenaTec saw a strong recovery in 2011, there have been some early signs of a slowing order intake thus far as the catch-up slows down. With the early months of the fiscal year coinciding with summer, the period is traditionally quieter. Whether this becomes more enduring due to economic uncertainties remains to be seen. As a result, we maintain our prudent forecast for growth in FY12 and FY13 of 9% and 5% respectively, with double-digit margins.

## Forecasts

While 2011 results came in slightly ahead of our forecasts, we recognise that economic uncertainty has increased since our original [outlook note](#) and, as a result, we feel it is prudent to reflect this in our forecasts as shown in Exhibit 1. We are also instigating FY13 forecasts with 11% top line growth and, with further operational improvement and lower debt, EPS growth of 27%.

### Exhibit 1: Edison forecast amendments

Note: Figures in £m except per share data.

	EPS			PBT			EBITDA		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
2011	4.2	5.6	+33	1.5	1.6	+4	3.3	3.1	-6
2012e	6.7	6.2	-8	2.4	2.1	-13	4.5	4.0	-11
2013e	N/A	7.9	N/A	N/A	2.7	N/A	N/A	5.0	N/A

Source: Edison Investment Research

**Exhibit 2: Financials**

	£'000s	2009	2010	2011	2012 <sup>a</sup>	2013 <sup>e</sup>
Year end 31 May		IFRS	IFRS	IFRS	IFRS	IFRS
<b>PROFIT &amp; LOSS</b>						
<b>Revenue</b>		<b>37,559</b>	<b>28,578</b>	<b>36,260</b>	<b>41,400</b>	<b>46,000</b>
Cost of Sales		(27,427)	(21,124)	(25,609)	(29,322)	(32,694)
Gross Profit		10,132	7,454	10,651	12,078	13,306
<b>EBITDA</b>		<b>4,087</b>	<b>2,334</b>	<b>3,050</b>	<b>4,036</b>	<b>5,006</b>
<b>Operating Profit (before amort and except)</b>		<b>2,653</b>	<b>947</b>	<b>1,897</b>	<b>2,536</b>	<b>3,206</b>
Intangible Amortisation		(137)	(137)	(137)	(147)	(147)
Exceptionals		(94)	(19)	(28)	(34)	(34)
Other		0	0	0	0	0
<b>Operating Profit</b>		<b>2,422</b>	<b>791</b>	<b>1,732</b>	<b>2,355</b>	<b>3,025</b>
Net Interest		(593)	(321)	(310)	(440)	(520)
<b>Profit Before Tax (norm)</b>		<b>2,060</b>	<b>626</b>	<b>1,587</b>	<b>2,096</b>	<b>2,686</b>
<b>Profit Before Tax (FRS 3)</b>		<b>1,829</b>	<b>470</b>	<b>1,422</b>	<b>1,915</b>	<b>2,505</b>
Tax		(701)	137	(161)	(525)	(680)
<b>Profit After Tax (norm)</b>		<b>1,359</b>	<b>763</b>	<b>1,426</b>	<b>1,571</b>	<b>2,006</b>
<b>Profit After Tax (FRS 3)</b>		<b>1,128</b>	<b>607</b>	<b>1,261</b>	<b>1,390</b>	<b>1,825</b>
Average Number of Shares Outstanding (m)		21.9	25.5	25.5	25.5	25.5
EPS - normalised (p)		6.2	3.0	5.6	6.2	7.9
EPS - normalised and fully diluted (p)		6.2	3.0	5.5	6.2	7.9
EPS - (IFRS) (p)		5.1	2.4	4.9	5.5	7.2
Dividend per share (p)		0.0	0.0	0.4	0.9	1.2
Gross Margin (%)		27.0	26.1	29.4	29.2	28.9
EBITDA Margin (%)		10.9	8.2	8.4	9.7	10.9
Operating Margin (before GW and except.) (%)		7.1	3.3	5.2	6.1	7.0
<b>BALANCE SHEET</b>						
<b>Fixed Assets</b>		<b>23,748</b>	<b>23,240</b>	<b>23,066</b>	<b>23,619</b>	<b>24,372</b>
Intangible Assets		12,183	12,292	12,225	12,278	12,331
Tangible Assets		11,308	10,090	9,983	10,483	11,183
Investments		257	858	858	858	858
<b>Current Assets</b>		<b>16,821</b>	<b>15,274</b>	<b>18,512</b>	<b>18,212</b>	<b>18,012</b>
Stocks		6,952	6,634	7,820	8,120	8,520
Debtors		8,914	7,479	8,854	8,254	7,654
Cash		634	1,097	1,716	1,716	1,716
Other		321	64	122	122	122
<b>Current Liabilities</b>		<b>(11,872)</b>	<b>(10,178)</b>	<b>(12,739)</b>	<b>(11,914)</b>	<b>(11,244)</b>
Creditors		(7,082)	(6,328)	(9,114)	(8,289)	(7,619)
Short term borrowings		(4,790)	(3,850)	(3,625)	(3,625)	(3,625)
<b>Long Term Liabilities</b>		<b>(7,629)</b>	<b>(6,650)</b>	<b>(5,981)</b>	<b>(5,624)</b>	<b>(4,973)</b>
Long term borrowings		(5,993)	(5,083)	(4,704)	(4,347)	(3,696)
Other long term liabilities		(1,636)	(1,567)	(1,277)	(1,277)	(1,277)
<b>Net Assets</b>		<b>21,068</b>	<b>21,686</b>	<b>22,858</b>	<b>24,293</b>	<b>26,168</b>
<b>CASH FLOW</b>						
<b>Operating Cash Flow</b>		<b>356</b>	<b>3,756</b>	<b>2,984</b>	<b>3,573</b>	<b>4,443</b>
Net Interest		(595)	(321)	(310)	(400)	(450)
Tax		(145)	94	(37)	(450)	(450)
Capex		(2,003)	(788)	(910)	(2,000)	(2,500)
Acquisitions/disposals		(420)	(448)	(353)	(200)	(200)
Financing		3,654	0	0	0	0
Dividends		(132)	0	0	(166)	(191)
Net Cash Flow		715	2,293	1,374	357	652
<b>Opening net debt/(cash)</b>		<b>10,801</b>	<b>10,149</b>	<b>7,836</b>	<b>6,613</b>	<b>6,256</b>
HP finance leases initiated		0	0	0	0	0
Other		(63)	20	(151)	0	0
<b>Closing net debt/(cash)</b>		<b>10,149</b>	<b>7,836</b>	<b>6,613</b>	<b>6,256</b>	<b>5,605</b>

Source: Edison Investment Research, company accounts

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