cityconfidential

sorting the bulls from the bears

In This Issue

Novacyt

Melrose Industries

Senior

Investec

Plus

Aggressive Growth Portfolio

Monthly News Highlights

cityconfidential
sorting the bulls from the bears

ISSUE JUNE 2021

Testing times for Novacyt?

There is no disputing the fact that 2020 was a phenomenal year for AIM-listed Novacyt (338.5p). The company ended 2019 with a share price of 13p but it was able to move quickly to secure substantial revenues from Covid-19 related products and this saw net assets multiply in value within a few months. Potential investors must decide whether this was a one-off phenomenon or a platform from which the business can develop further.

In the year ended 31 December 2020 revenue was £277.2m versus £11.5m in 2019. Profit after tax was £132.4m compared with a loss of £5.7m in 2019 and cash held as at the period end was £91.8m, up from £1.5m a year earlier.

On 9 April 2021, Novacyt announced that it was in dispute with the DHSC in relation to its second supply contract. This primarily relates to revenue in the final quarter of 2020 amounting to £129.1m in respect of a specific product supplied to the NHS. Of the revenue in the final quarter of 2020, invoices amounting to £24.0m in respect of product delivered to the DHSC remain outstanding and recovery is dependent on the outcome of the dispute. In addition, a further £49.0m of product delivered and invoiced to the DHSC in 2021 remains unpaid and is now also part of the dispute. The unpaid invoices total £73.0m including VAT.

For the five months ended 31 May 2021, sales were £88.4m compared to £40.8m for the same period in 2020. The £88.4m figure includes £40.7m of sales to the DHSC, which are part of the dispute. Excluding the DHSC, sales were over £10m a month in the first quarter of 2021, which fell to around £7m per month in April and May. This was a repeat of the trend seen in 2020 as relevant countries moved into the summer period and the spread of Covid-19 declined.

Looking forward, strong growth in private testing is anticipated as markets and travel re-open, which could lead to higher infection rates. An increase in testing is also forecast to return in the final quarter of 2021. The company expects to see significant new growth from the launch of new products during the second half of 2021, including an expansion of its lateral flow antigen testing portfolio for both professional and home use. If demand is in line with expectations, the company currently expects to see full year sales of approximately £100m, excluding the sales to the DHSC which are in dispute. The shares are a SPECULATIVE BUY.

Many happy returns to Melrose shareholders

Melrose Industries (162.4p) has announced the completion of the £2.62bn disposal of its Nortek Air Management Division to Madison Industries LLC and confirmed the proposed return of approximately £730m in cash to shareholders, the equivalent of 15p per share. It has also been confirmed that trading has remained in line with expectations as outlined in a trading statement at the time of the AGM on 6 May.

Both the Automotive and Powder Metallurgy Divisions have seen recovery in the automotive sector, although this has been held back by the impact of the global semi-conductor shortage. Some green shoots have also been seen in the Aerospace Division and some recovery could be in sight. All these divisions have been significantly cash generative during Melrose's ownership. Since acquisition the GKN businesses have generated over £0.5bn of total free cashflow after all restructuring costs. On the basis that the sector recoveries continue, the company expects to be able to make another significant return of capital to shareholders next year. It has been relatively conservative with cash returns in the near term given the ongoing impact of Covid-19.

The disposal of Brush, a leading independent provider of turbogenerators, transformers and switchgear and associated services, was also completed recently for a net cash consideration of £100m. Brush is the final business to be sold from the FKI acquisition in 2008 and it has delivered a 2.6x return on shareholders' initial equity, equivalent to an IRR of 29%.

The return of capital will be accompanied by a consolidation of the ordinary share capital to minimise any impact on the market price of the shares and ensure that shareholders retain the same pro rata interest in the company after the return of capital is completed. We believe that the shares represent good value and see strong capital gains for shareholders in the coming years. BUY.

Senior

SECTOR – AEROSPACE AND DEFENCE

Senior has been in the spotlight recently having been the subject of unwanted attention from US private equity firm Lone Star Global Acquisitions. The latter eventually made a final possible takeover offer of 200p per share but the former's Board felt that this fundamentally undervalued Senior and its future prospects. The offer, the latest of five proposals, was seen as being opportunistic given the timing and the relative share price weakness. It also came at a time when the company's end-markets are showing signs of recovery. This meant that the offer has not been recommended to shareholders. However, the gap between this valuation and the current share price may mean that there is potentially an opportunity to buy in now for a quick return. Trading prospects appear to be improving so it could be a good time to consider investing, even if there is no corporate activity.

The company is an engineering solutions provider. It designs, manufactures and markets high-technology components and systems for principal original equipment producers in the worldwide aerospace, defence, land vehicle and power & energy markets. Safe and innovative products are provided for demanding thermal management and fluid conveyance applications. Senior aims to be a trusted and collaborative high value-added engineering and manufacturing company which produces sustainable growth in operating profit, cash flow and shareholder value.

Results for the year ended 31 December 2020 were released on 8 March. Revenue slumped from £1,111m to £734m due to the Covid-19 pandemic and the ongoing impact of the grounding of the Boeing 737 MAX fleet. An adjusted loss before tax of £6.2m was incurred versus a profit before tax of £78.5m a year earlier. This translated into an adjusted loss per share of 0.84p (2019: adjusted earnings per share of 16.17p). The reported loss before tax was £191.8m (2019: £28.7m profit). The basic loss per share was 38.2p (2019: basic earnings per share of 7.04p).

Free cash flow was £46.5m (2019: £58.3m) and net debt as at 31 December 2020 was £205.9m (including capitalised leases of £76.5m), a reduction of £23.7m from 31 December 2019 after taking into account favourable currency movements of £2.4m and £1.9m increase for lease movements. For the period ended 31 December 2020, net debt to EBITDA was 2.8x and interest cover was 6.1x, both well within agreed covenant limits (which are on a frozen GAAP, pre-IFRS 16 basis). No final dividend was declared.

In Aerospace, sales fell 36.6% year-on-year on a constant currency basis, with sales from civil aerospace down 50.5%, partly offset by 6.5% growth in sales from defence. On a quarterly basis, Aerospace sales were down 22% in Q1, 40% in Q2, 45% in Q3 and 39% in Q4 year-on-year. In Flexonics, sales were 23.5% lower year-on-year on a constant currency basis. On a quarterly basis, Flexonics sales were down 23% in Q1, 33% in Q2, 25% in Q3 and 13% in Q4 year-on-year.

An in-line trading update was released on 23 April, to coincide with the company's AGM. In Aerospace, on a quarterly basis, sales fell 25% in the first quarter of 2021. In Flexonics, sales declined 4% in Q1 year-on-year. Revenue in Q1 was helped by recovery in heavy-duty truck and off-highway markets, partially offset by a decline in oil & gas and the closure of the Senior Flexonics business in Malaysia.

On 22 June the company made an announcement that it would not be recommending a Final Conditional Proposal from Lone Star to shareholders. It was seen to be highly opportunistic, fundamentally undervaluing Senior and its future prospects. There is a focused strategy to achieve growth and create value for shareholders over the medium term. Essentially the company believes that it has been hit by some exceptional events in the near term and that the offer has been timed to take advantage of the fact that the value of the business will ultimately prove to be far higher than the current share price suggests.

A trading update was also provided on 22 June. Trading in the five months ended May 2021 was ahead of management expectations. Sales were 15% lower than the equivalent period in the prior year on a constant currency basis. Net debt (excluding capitalised leases of £74m) as at 31 May 2021 was £101m, reflecting net cash proceeds received from the disposal of Senior Aerospace Connecticut. A restructuring programme delivered cumulative savings of £36m to the end of 2020 and the savings are expecting to increase to £45m by the end of 2021, with £50m of annualised savings from 2022. The company's differentiated offering in fluid conveyance and thermal management products, along with its investment in low carbon and advanced manufacturing technology means that it is well positioned for the longer term. Its global footprint, strong track record and position in attractive and diverse end markets means that the company is confident that it will thrive again as the recovery continues. A post-close trading update is scheduled for 9 July then interim results will be announced on 2 August, at which time a full market and strategy update will be provided. There will also be a capital markets day in October 2021 on the theme of fluid conveyance and thermal management strategy.

The interest from Lone Star adds some spice to an interesting recovery story. It could also flush out other bidders, which could potentially crystalise a capital gain for shareholders within a short space of time. Looking at fundamentals there is scope for the valuation of Senior to grow considerably from the current level over time. There must also be a chance of either Lone Star or another party making an offer above 200p per share. Many commentators have pointed to the fact that the valuation placed on listed companies in the UK has fallen to bargain basement levels relative to those in the US, which means that corporate activity may well be on the cards at some time in the not too distant future. However the value is unlocked, the shares appear to be cheap and we put forward a BUY recommendation.

Share Price: 149.3p
Market Capitalisation: £626m
2020/21 Share Price Range: 165.7p/42.86p
Website: www.seniorplc.com

Year Ending 31 December	Turnover (£m)	Adjusted Pre-Tax Profit (£m)	Adjusted Earnings Per Share (p)	P/E Ratio	Net Dividend (p)	Net Yield (%)
2020	734	(6.2)	(0.8)	-	-	-
2021 (est)	664	(8.3)	(1.5)	-	-	-
2022 (est)	739	14.9	3.0	49.8	-	-

Aggressive Growth Portfolio VIII

It is a little disappointing to have to report that the Aggressive Growth Portfolio has fallen in value for the first time since the new portfolio was started in January. Coincidentally, the decline in the value of the portfolio of 1.4%, is the same as the fall in the FTSE AIM All-Share Index over the last five weeks. The other two benchmark indices have both risen by 0.1%. It is worth pointing out though that the portfolio has risen in value so far this year by 19.7%!

Shares in Logistics Development Group have been disappointing since purchase to be fair and they have now fallen through the stop-loss limit of 10p. The sale of our holding of 25,200 shares at 10p has therefore raised net proceeds of £2,495 for a loss of £1,005. We have then decided to take the profit on our holding of TT Electronics and have sold 1,875 shares at a price of 261.5p. This has raised net proceeds of £4,854 for a gain £857. Readers may recall that these were purchased in January at 210p and the net gain is 21.4%.

A number of companies have made announcements during the period, and these include Hargreaves Services, Tandem Group, Capita, Manx Financial Group, Serco Group, Clinigen, Essentra and Funding Circle. These have been covered in News Highlights or on the website in the normal way.

The portfolio has received a number of dividends during the period and these were from Lloyds Banking Group (£55), TT Electronics (£88), Serco (£36) and Essentra (£35). Following the purchases of both Senior and Investec, there is £1,789 left on deposit pending investment.

Performance summary

	22 June 2021	18 May 2021	Gain/(Loss) %
Portfolio Value	£59,849	£60,725	(1.4)
FTSE 100 Share Index	7,090.01	7,034.24	0.1
FTSE All Share Index	4,046.87	4,007.57	0.1
FTSE AIM All Share Index	1,222.15	1,239.75	(1.4)

	Security	Buying Price (p)	Total Cost (£)	Current Price (p)	Value (£)	Stop-Loss Limit (p)
3,160	ITV	109.15	3,500	128.1	4,048	80
1,315	Hargreaves Services	264	3,507	425.5	5,595	280
725	Tandem Group	480	3,515	595	4,314	450
1,235	Xeros Technology	281	3,505	233	2,878	200
9,575	Lloyds Banking Group	36	3,498	46.765	4,478	33
9,375	Capita	36.75	3,496	39.82	3,733	27.5
39,600	Manx Financial Group	8.75	3,500	8	3,168	6.5
2,600	Serco Group	125.4	3,309	132.9	3,455	105
315	Vitec Group	1120	3,581	1295	4,079	850
450	Clinigen	750.5	3,411	628	2,826	575
1,075	Essentra	298	3,251	326.5	3,510	240
2,000	Funding Circle	157	3,187	154.6	3,092	115
1,850	Premier Miton	163.5	3,054	172.5	3,191	130
1,550	Mears	187	2,942	189	2,930	145
2,350	Senior	149.3	3,562	149.3	3,509	115
1,100	Investec	295.8	3,303	295.8	3,254	250
£1,789	Cash	-	-		1,789	
				TOTAL	**£59,849**	

Start date: 19 January 2021 with £50,000. Cash includes dividends received of £275.

INVP

295.8p

INVESTEC

SECTOR - BANKS

Final results from Investec, released last month, demonstrated the strength of the business. In March 2020 the demerger of Ninety One, formerly known as Investec Asset Management, was completed and it was interesting to digest numbers for a full year of trading as the revised entity. The shares are rated modestly and given the prospective yield of over 6%, they must be of interest for those seeking income from equities.

In the first half of the year ended 31 March 2021 performance was hampered by volatile market and economic conditions due to the impact of Covid-19 and related restrictions but the second half saw strong earnings recovery. Positive momentum has continued into the new financial year. For the year to 31 March 2021 adjusted earnings per share from continuing operations were 28.9p, down 14.7% on the prior year. However, second half earnings were 58.1% ahead of the first half. The tangible net asset value per share increased by 12.7% to 425.7p and this allowed a final dividend of 7.5p per share to be declared, taking the full year dividend to 13.0p per share.

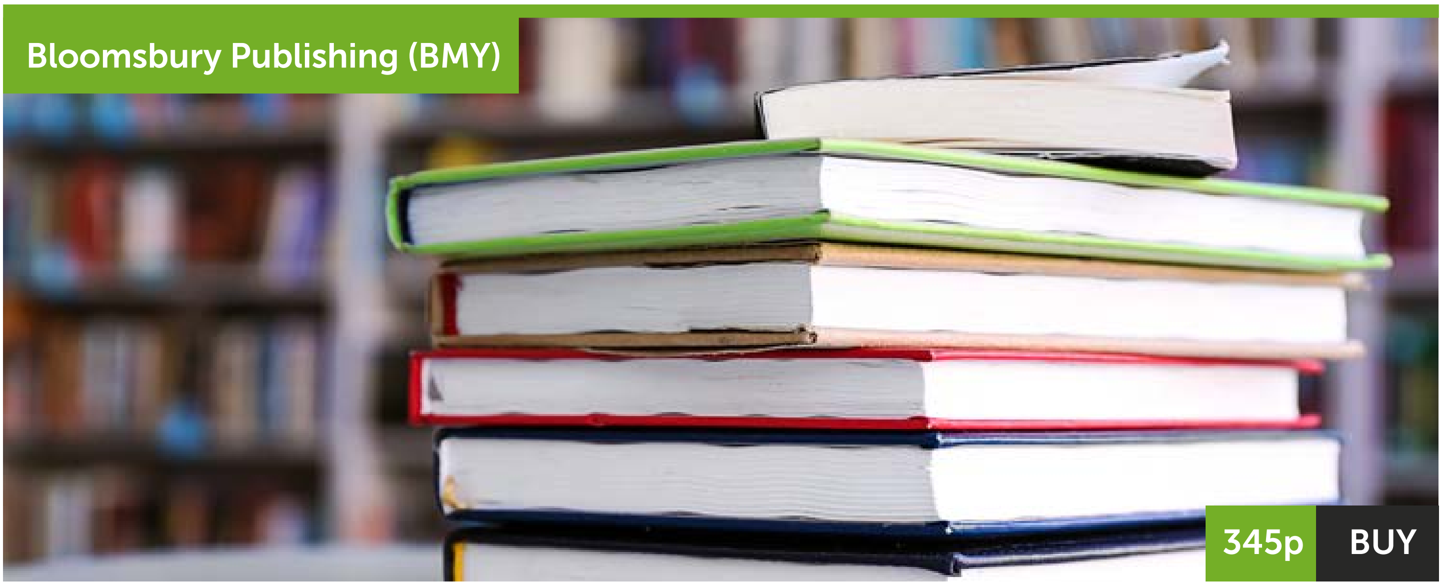
The Wealth & Investment business reported growth in funds under management of over 30% to £58bn (2020: £45bn), reflecting market recovery, good investment performance and continued net inflows of £1.1bn. Lending franchises reported positive book growth in the second half, ending the year with core loans of £26.4bn (2020: £24.9bn). The Private Banking franchise reported higher core loans, supported by strong lending book growth in the second half. The corporate lending book ended lower than the previous year. Solid client acquisition in South Africa and the UK saw a 6.9% increase in deposits. Client activity within the Specialist Banking business is said to have increased since December 2020.

This is a steady business which is unlikely to produce spectacular returns for shareholders given its nature. However, the downside also looks limited with the shares trading at a significant discount to the net asset value. The key attraction to buying the shares is the well-covered yield and with growth in dividends likely in the coming years, income seekers should certainly consider adding Investec to their portfolio. BUY FOR INCOME.

Share Price: 295.8p
Market Capitalisation: £2,059m
2020/21 Share Price Range: 311.8p/127.5p
Website: www.investec.com

Year Ending 31 March	Turnover (£m)	Adjusted Pre-Tax Profit (£m)	Adjusted Earnings Per Share (p)	P/E Ratio	Net Dividend (p)	Net Yield (%)
2021	1,641	332	28.9	10.2	13.0	4.4
2022 (est)	1,764	505	38.1	7.8	18.1	6.1
2023 (est)	1,887	592	45.2	6.5	21.4	7.2

News Highlights



As subscribers will know, we update the website with news that involves the companies that we follow, but we have highlighted what we regard as the most important news here.

Bloomsbury Publishing – 345p

The international publishing group has issued its annual results for the year ended 28 February 2021. These have revealed that revenue for the year rose by 14% to £185.1m (2020: £162.8m) with adjusted profit before tax increasing by 22% to £19.2m (2020: £15.7m). Adjusted diluted earnings per share were up 15% to 18.68p (2020: 16.23p) and a final dividend of 7.58p was declared as well as a special dividend of 9.78p per share. This has taken the total dividend for the year to 18.64p meaning that including the special dividend the shares are yielding 5.4%. The strong cash generation at the group meant that net cash was £54.5m as at 28 February 2021 (2020: £31.4m). The company has also announced the acquisition of Head of Zeus Limited, an independent publisher of fiction, non-fiction and children's books. Authors of the latter include Dan Jones, Victoria Hislop and Cixin Liu, the science fiction author. This is to cost £8.45m, with £5.5m being paid in cash on completion and the balance payable in later instalments. In the year ended 31 December 2020 Head of Zeus generated £8.6m of revenue and profit before tax of £0.3m, with net assets of £4.6m. With further strong growth on the cards we rate the shares as a BUY.

DWF Group – 98p

The global legal and business services group has announced a positive trading update covering the year to 30 April, with strong activity levels seen in the second half of the financial year. As a result, group revenues have risen by over 13% to £338m during the year with all divisions doing better than last year. Adjusted pre-tax profits have come in well above expectations at £34m with earnings per share on the same basis likely to be around 8.5p. A final dividend of 3p is expected which would take the total for the year to 4.5p. Despite one-off payments of £17m during the year for deferred consideration and acquisition related payments, net debt still declined slightly to £61m (2020: £65m) and, with only £7m of such payments due in the new financial year, this should continue to reduce unless further acquisitions are made. The company has made two bolt-on acquisitions since the year end at a total cost of £4m with part of this to be funded by the issue of shares in the company. With further growth forecast for the current year, we maintain our recommendation of BUY.

LPA Group – 72p

AIM-listed LPA Group has announced results covering the six months ended 31 March 2021. The company, which is a high reliability LED lighting, electronic and electro-mechanical system designer and manufacturer, reported revenue of £9.3m versus £10.8m in 2020. As previously reported the company has suffered from project delays as customers have deferred orders due to the pandemic. Underlying pre-tax profit was £0.12m (2020: £0.19m) and diluted earnings per share were 1.62p (2020: 2.01p). No interim dividend was declared. Net debt was reduced to £1.77m (2020: £3.17m), which saw gearing almost halved to 13.5% (2020: 25.6%). The order book increased 6% to £26.2m (2020: £24.7m) which is clearly very promising looking ahead. Since the announcement of the results, the group has announced a new contract to supply LED lighting systems for 165 new build carriages for the UK's East Midlands Railway Aurora InterCity Fleet. This award adds to the group's order book which already stands at a record level. Despite the impact of the pandemic, no business has been lost and the group is optimistic that business will recover over the next year. The shares are a LONG-TERM BUY.

Synectics – 127.5p

The supplier of advanced security and surveillance systems has issued a trading update for the six-month period to 31 May and this has confirmed that trading has been subdued, much as expected. Although the company has made progress in the public infrastructure and transportation sectors, the restriction on travel has reduced demand for the group's products in the gaming and casino sectors. The latter were the group's most important markets pre-Covid and, although there are some signs of increased activity in both the US and Far East, demand remains muted. The company is therefore focusing on the infrastructure and transportation business where it has had success in both London and Berlin and these projects have generated further interest from elsewhere. Revenues for the period fell to £22m from £23m last year although the operating loss was reduced to £0.8m (2020: loss of £2.0m) thanks to cost cutting measures. Net cash of £3.5m at the period compares with £4.5m at the end of February and so the group remains in a sound financial position. Interim results are due on 13 July and these will provide further guidance on prospects - with recovery in the gaming and casinos business likely to pick up in the second half, the current price is an attractive entry point for long term investors. The shares are a LONG-TERM BUY.

cityconfidential
sorting the bulls from the bears

cityconfidential is published by Independent Financial Publications, which is authorised and regulated by the Financial Conduct Authority. Independent Financial Publications has taken every step to ensure the accuracy of the information contained in this publication but cannot accept any liability for any errors or any loss arising from the use of this publication or its contents. Independent Financial Publications or individuals associated with it may have a position or engage in transactions in any of the securities mentioned. The price of investments and the income derived from them can fall as well as rise and investments in smaller companies have a higher risk factor. Past performance is not necessarily a guide to future performance. The investments in this publication are not suitable for everyone. Before taking any action you should obtain expert advice from your adviser.

VAT No: GB 607 1818 48

Independent Financial Publications, 1 Skipton Road, Ilkley, West Yorkshire, LS29 9EH

Designed and published by Westbrook Agency © 2021
www.westbrookagency.co.uk

Thanks for reading
Next issue out 22nd July

RETURN TO THE WEBSITE >