Sanderson Group (SND)

AIM - Software & Comp. Services

Today's announcement that the group has successfully concluded its refinancing ahead of schedule is clearly good news. HSBC has replaced Royal Bank of Scotland as the group's banker and has advanced a four year term facility of £7.4m together with a £1m working capital facility. The new arrangements are expected to save the group around £300,000 per annum.

Sanderson has also commented on current trading where the group continues to experience good trading momentum in its Manufacturing and Multi-Channel businesses, although the high street Retail market is more challenging. The group continues to invest in new products and in its sales and marketing activities and this is helping it to win new business from both existing and new customers. Another pleasing feature of the group's progress is that it continues to increase the level of recurring revenues. As a result, it has maintained a strong order book and full year pre-tax profits, before an exceptional finance charge relating to the refinancing, are expected to be in line with expectations. The group's strong cash flow has meant that debt has steadily reduced and this is expected to fall further going forward.

We have increased our forecasts for 2012 to reflect the benefits of the new finance arrangements. Although the shares have moved up from 27.5p in May when we last issued a note, the shares still stand on a modest prospective p/e ratio. Assuming a relatively modest p/e ratio of 10x 2012 earnings, the share price would rise to 58p, providing upside of 55%. We believe that there is still scope for a significant re-rating of the shares.

Activities

Sanderson Group operates as a supplier of innovative software solutions and IT services. There is a heavy bias towards the UK market, specifically the multi-channel retail and manufacturing sectors. Long term relationships are built with clients, who tend to be organisations with turnover between £5m and £250m.

Multi-Channel Retail - the group has a wide range of IT solutions, products and services which are aimed at businesses that sell via retail stores, mail order, wholesale and online. These include EPoS systems, retail management systems, e-commerce software, multi-channel software, mail order management and wholesale IT systems. A new internet retail product has also been successfully introduced as has a new module for hospital catering. Services include maintenance and support, IT and managed services, hardware and installation. Customers include Harrods, Selfridges, French Connection and Salford Royal NHS Foundation Trust.

Manufacturing - software solutions have been created for manufacturing, with some applications designed specifically for the print and food sectors. The Unity ERP (enterprise resource planning) system has been developed using the group's experience in dealing with the manufacturing sector. Formul8 is designed to manage all aspects of food production and distribution and Unity MIS (management information system) is a modern print business system. Unity SBE improves the management and planning of internal resources of smaller businesses.

Results and Consensus Forecasts

Year to 30th September	Revenue (£m)	Pre-Tax Profit* (£m)	Earnings per share* (p)	P/E Ratio	Net Dividend (p)	Net Yield (%)
2009A	24.9	1.07	4.0	9.4	0.4	1.1
2010A	27.0	1.91	3.9	9.6	0.6	1.6
2011E	27.5	2.40	5.2	7.2	0.8	2.1
2012E	28.5	3.10	5.8	6.5	1.0	2.7

* before amortisation of acquisition-related intangibles, exceptional costs, impairment of goodwill and share-based payment charge

KEY DATA

Share Price:	37.5p
Prospective p/e ratio:	7.2x
Prospective net yield:	2.1%
Market Capitalisation:	£16.3m
Next Results Due (Fins):	NOV
Gearing:	39%

SHARE PRICE PERFORMANCE

2010/11 High/Low: 41.5p/18p

BULLET POINTS

- Current trading in line with expectations
- Successful refinancing of bank facilities achieved ahead of schedule
- Significant cost savings made due to the refinancing
- Net debt continuing to fall
- Strong order book
- Progressive dividend policy
- Shares on low p/e ratio

Date of Report : 2 August 2011

COMPANY DATA

Stockbrokers:
Charles Stanley

Significant Shareholdings:

C Winn Esq, Chairman - 29.97%
AXA Framlington IM - 9.21%
ISIS EP LLP - 6.92%
Hargreave Hale & Co - 6.49%
Chelverton AM - 6.29%
Unicorn Asset Management - 3.55%

Contact Address:
Sanderson House
Manor Road
Coventry
CV1 2GF

www.sanderson.com

Information:
Christopher Winn - Chairman
Adrian Frost - Finance Director
t - 02476 555466

Interim Results

The group's latest results cover the six months to 31 March and these were announced in May. These showed that the company continued to make progress despite the slow pace of recovery in the UK economy. The was a factor in the slight decline in revenue for the period to £13.1m (2010: £13.3m), although an improvement in gross margins to 70.6% (2010: 67.1%) led to operating profit before exceptionals increasing to £1.47m (2010: £1.38m). It was pleasing to see that recurring revenues from software licences and support/service contracts increased once again, so that in the first half they rose by 6% to £7.1m (2010: £6.7m), representing 54% of total revenues (2010: 51%).

Pre-tax profits before exceptional items increased to £1.08m (2010: £0.75m) whilst earnings per share on the same basis emerged at 2.3p (2010: 1.7p). The interim dividend was raised to 0.30p (2010: 0.25p). Continued strong cash generation led to another fall in net debt to £7.2m (2010: £9.0m) and this continues the trend of debt reduction, with net debt falling by over 40% since it peaked in March 2008.

In the multi-channel retail business, revenues declined slightly to £10.1m (2010: £10.2m), although operating profit before exceptionals increased to £941k (2010: £840k). The group has developed a new module within its retail offering enabling customers to achieve savings and efficiencies in catering management and this is also being used in hospital catering. Eleven new customers were gained in the period including Shaws Drapers and Yorkshire Trading Company, whilst large orders were received from existing customers including discount retailer Wilkinson and Lakeland.

Revenue at the manufacturing business was slightly down at £3.0m (2010: £3.1m) although those of a recurring nature account for 58% of the total. Operating profit before exceptionals was also slightly lower at £527k (2010: £536k). Two new customers were gained in the period and a large surge in orders in March meant that the business started the second half with order books of £860k, an increase of 88%.over the previous year (2010: £457k).

Prospects

Although trading conditions remain challenging on the high street, the group has managed to maintain strong trading momentum helped by good performances from its Manufacturing and Multi-Channel businesses. The order book remains strong and full year pre-tax profits are expected to be in line with current market expectations, before an exceptional finance charge of £400,000 relating to the group's refinancing. As stated earlier, the new banking arrangements are expected to save the group around £300,000 per annum, whilst also providing the group with additional flexibility to improve its competitive position.

The group continues to invest in product development as well as its sales and marketing initiatives in order to improve its competitiveness. New products and services include Business Assurance, Factory Automation, latest etailing and ecommerce software, a suite of Green IT solutions and, most recently, offerings based on 'Software as a Service' and Cloud delivery models.

The group continues to enjoy strong cash flows and these should allow borrowings to fall further going forward, whilst there is also a commitment to increase the dividend. Although the shares have risen sharply since our last note of 18 May, when the share price was 27.5p, we still believe that they have scope to make further progress and have increased our medium term share price target to 58p.

1 Skipton Road
Ilkley
West Yorkshire
LS29 9EH

Tel : 01943 886602
Fax : 01943 886601
Email : info@brokerlink.co.uk
www.brokerlink.co.uk

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