GECR

Sanderson Group

Update
9th June 2015

Interims

Sanderson Group has announced its interim results. The results are in-line with our expectations, reflecting further progress on an operational level, with both revenues and operating profits increasing by more than 13% during the six-month period ended 31st March 2015. The balance sheet remained strong, enabling Sanderson to maintain its progressive dividend policy and increase its dividend payment by 12.5% to 0.9p per share. The strong order book and healthy balance sheet, together with a long list of sales prospects, provides us with further confidence in our slightly amended forecasts. With the shares offering investors exposure to the high-growth Enterprise Resource Planning software market, as well as offering a decent dividend yield of 3.03%, we continue to classify the shares as a hybrid growth and income stock.

Interims

For the six-month period, revenue increased by 14% to £9.09m (H1 2014: £7.94m) and operating profit improved by 13% to £1.37m (H1 2014: £1.21m). Pre-contracted licence and ongoing support services recurring revenue grew to £4.76m (H1 2014: £4.41 million), representing 52% of total revenue. Gross margin was maintained at a robust 85% (H1 2014: 87%) and the order book remained strong, increasing to £2.84m (H1: £2.47m). After the payment of £1.80m in respect of acquired businesses, the net cash balance was £3.95m (2014: £5.07m). DPS increased by 12.5% to 0.9p per share (H1 2014: 0.8p per share), which is well covered by diluted EPS of 1.5p (H1 FY14: 1.3p). In addition, Sanderson achieved an improved intake of sales orders in the period of £4.94m, compared with £4.27m. Thirteen new customers were won (H1 2014: twelve).

Financial forecasts

To reflect a better than expected performance from Proteus on a revenue basis, we have increased our revenue forecast for FY15 to £19.00m (from £18.80m). However, maintaining gross margins at 84%, we estimate an unchanged gross profit figure of £15.98m. We continue to forecast an adjusted EBIT of £3.35m and adjusted PBT of £3.10m. We are anticipating DPS of 1.90p. For FY16, we are forecasting an unchanged revenue figure of £20.50m and gross profit of £17.43m. We are now estimating an adjusted EBIT of £3.55m (previously £3.71m) and adjusted PBT of £3.30m (previously £3.40m). We anticipate an unchanged DPS figure of 2.0p.

Valuation

Assuming Sanderson trades on a similar EV/EBITDA as its peers of 12x, we have a target price of 91p.

Table: Financial overview

Year to 30th Sep.	2013A	2014A	2015E	2016E
Revenue (£'000)	13,828	16,411	19,000	20,500
PBT* (£`000)	2,186	2,707	3,101	3,301
EPS* (p)	4.42	4.61	5.17	5.32
Dividend (p)	1.50	1.80	1.90	2.00
Yield (%)	2.27%	2.73%	2.88%	3.03%

Source: GECR and company. *Notes: *Adjusted*

Key data

Share price	66.00p
52 week high/low	74.50p/58.50p
Primary exchange	AIM
EPIC	SND
Shares in issue	54.55 m
Market Cap	£34.64 m
Sector	Software & Computer Services

Share price chart

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Interims

Sanderson Group has announced its interim results for the six months 31st March 2015. The group has made further progress during the period, with revenue increasing by 14% to £9.09m (H1 2014: £7.94m) and operating profit rising by 13% to £1.37m (H1 2014: £1.21m). Pre-contracted licence and ongoing support services recurring revenue grew to £4.76m (H1 2014: £4.41 million), representing 52% of total revenue in the period.

Gross margin has been maintained at a robust 85% (H1 2014: 87%), reflecting Sanderson's continued emphasis on the supply of its proprietary owned software and services. The order book - which gives us good visibility of future revenues and demonstrates the confidence customers have in the offerings - remained strong, increasing to £2.84m (H1: £2.47m).

The collection of a number of sales ledger balances slipped beyond the period end, with a total of £435k being received in the first week of April. After the payment of £1.80m consideration and deferred consideration in respect of acquired business, the net cash balance was £3.95m (2014: £5.07m).

The interim dividend payment increased by 12.5% to 0.9p per share (H1 2014: 0.8p per share), which is well covered by diluted EPS of 1.5p (H1 FY14: 1.3p). Payment will be made on 14th August 2015 to shareholders on the register at the close of business on 17th July 2015.

Reflecting prior and contributing investment in the group's sales and marketing capacity and capability, Sanderson achieved an improved intake of sales orders in the period of £4.94m, compared with £4.27m. Thirteen new customers were won (H1 2014: twelve).

Review of multi-channel retail

Mobile enablement and deployment continues to be a key business driver in this sector, with increasing levels of business activity. The wholesale distribution and cash and carry market has been a slower area of business during the period for the group, but Sanderson added that prospects for the second half are good, driven by the release in February 2015 of its latest enhanced version of its software. Proteus has made a steady start to being part of Sanderson and has helped to further expand the group's presence in the areas of warehousing, logistics and supply chain. A number of internal 'joint' sales opportunities are being developed.

Five new customers were gained during the period, including Anzac Wines & Spirits, Lavitta, Quba & Co and Matthew Algie. This compares with seven in the comparable period of 2014. The multi-channel retail division has also continued to gain a number of large orders from existing customers, including JD Sports, Kingtown Associates, Healthspan and Superdry,

Divisional revenue was £5.96m (H1 2014: £4.71m) and operating profit rose by just under 20% to £1.01m (H1 2014: £0.85m). The period-end order book was very strong at £1.80m (H1 2014: £1.19m) and Sanderson said that given the good sales prospects, the multi-channel retail business is well positioned to achieve its increased trading targets for the current financial year (ending 30th September 2015).

Review of manufacturing

Although the overall divisional trading performance was flat on the comparative period a year earlier, the general manufacturing business improved its trading performance compared with the first half of 2014 and Sanderson expects this improvement to continue into the second half of the current year. The group's food and drink business experienced some delays in the receipt of expected sales orders.

Eight new customers were gained during the period, including Simtom Food Products, Summit Chairs, St Marcus Fine Foods, Wine Bottling Solutions and NutriFresh. This compares with five new customers in the comparative period of 2014. Large projects with existing customers included Magnadata, Cook Trading, Food Partners and Freddy Hirsch.

The group has had some success with its entry level Unity ERP (Enterprise Resource Planning) product, which is aimed at smaller and emerging businesses and over the coming months, Sanderson expects to further develop its software and launch new products, including further cloud-based solutions, into its target manufacturing markets.

Revenue for the period was £3.14m (H1 2014: £3.23m) and operating profit was £365k (H1 2014: £367k). Recurring revenue represents >61% of total divisional revenue and covers more than three-quarters of divisional overheads. The order book is £1.04m (H1 2014: £1.28m) and Sanderson expects that together with a strong sales prospect list, the manufacturing division will achieve another improved trading result for the full-year.

Management and staff

Ian Newcombe, who has made a major contribution to the formulation of the group's strategy and who has personally driven the development of the multi-channel business, has been appointed as CEO with immediate effect.

Furthermore, David Gutteridge has been appointed as a non-executive director. David has considerable business experience, including with Financial Objects plc, Cyan Holdings plc and Sanderson Group plc as a non-executive director between IPO in 2004 up until 2012. David was Chairman of Tinglobal Limited until May 2014, when he led a successful trade sale to Singapore Listed, Declout Plc.

Strategy and Outlook

Whilst the group will continue to invest across all of its businesses, particular emphasis will be placed on further developing the range of solutions for mobile and ecommerce businesses, for the food and drink processing sector and for entry level systems in the manufacturing division. Mobile solutions continue to be developed across all of the group's target markets.

In order to augment organic growth, selective acquisition opportunities will continue to be considered. However, in the current year, management intends to focus on delivering another set of 'on target' trading results.

The board remains cautious in its approach but a strong order book and healthy balance sheet together with a long list of sales prospects, provides the board with a good level of confidence that the group will continue to make further progress and deliver trading results in line with market expectations for the current year ending 30 September 2015.

Forecasts

We have updated our forecasts slightly in light of the interim results announcement. To reflect a better than expected performance from Proteus on a revenue basis, we have increased our revenue forecast for FY15 to £19.00m (from £18.80m). However, maintaining gross margins at 84%, we estimate an unchanged gross profit figure of £15.98m. We expect the group to continue its investment in product innovation, as well as sales & marketing, and continue to forecast an adjusted EBIT of £3.35m and adjusted PBT of £3.10m. We are forecasting DPS of 1.90p.

For FY16, we are forecasting an unchanged revenue figure of £20.50m and gross profit of £17.43m. With further product innovation and sales & marketing investments anticipated, we are forecasting an adjusted EBIT of £3.55m (previously £3.71m) and adjusted PBT of £3.30m (previously £3.40m). We anticipate DPS of 2.0p, but note that this could be higher if targets are hit and cash flows remain strong.

Valuation

We continue to be impressed by the high level of recurring revenues. A strong and growing range of products and services, a growing presence in the catalogue, online sales and ecommerce markets, the strengthened balance sheet and strong cash generation all augur well for Sanderson. Accordingly, assuming Sanderson trades on a similar EV/EBITDA as its peers of 12x, we have a target price of 91p. The prospective yield of 3.03% is also attractive.

Disclaimer