

Severfield

Set to outperform

Dalton site visit

Severfield's rising UK order book and improving margins set a good tone ahead of FY16 results on 15 June. A recent capital markets event served to reinforce the margin development path that the company is on, with further progress targeted. Little of this appears to be factored into the share price currently and we believe the scope for outperformance is now significant.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
03/14	231.3	4.5	1.1	0.0	47.8	N/A
03/15	201.5	8.8	2.5	0.5	20.9	1.0
03/16e	232.1	12.3	3.4	1.0	15.4	1.9
03/17e	244.1	16.2	4.5	1.3	11.6	2.5

Note: *PBT and EPS are normalised, excluding pension net finance costs, intangible amortisation and exceptional items.

Investing in sustainable margin improvement

Severfield's FY16 EBIT margin target of 5-6% (FY13: around zero underlying) has been well flagged and is clearly now seen as a staging post for further progress. In markets that remain competitive, operational efficiency improvements have been emphasized. A site visit demonstrated a more co-ordinated facility management approach, with work packages being allocated to the most efficient fabrication site, balancing respective workflows and developing site flexibility. There has also been investment in fabrication (reducing plate process cycle time with multi-station CNC machinery), supply chain (metal decking JV) and ancillary areas (providing a fleet of site safety equipment, previously bought in). There is more to come; Severfield is upgrading its production flow management software (from a bespoke platform to a StruMIS industry ERP system) across all sites. This connects front-end modelling/design, fabrication and site execution progress more effectively, links to commercial functions (eg purchasing, accounting) and enhances contract visibility at all levels.

Creating client value to enhance margins

Externally, Severfield provides combined structural and building programme design and value engineering expertise to add value to projects (ie increase efficiency, reduce risk, time and cost). This creates scope to differentiate during project development phases, drives tender success and provides opportunities to negotiate a share of any savings created. Earlier and full engagement with end-clients, main contractors and consultants offers potentially greater gains. Severfield's industry reputation for advice, engineering and project delivery generates new business and Early Contractor Involvement (ECI) with repeat clients is actively being pursued.

Valuation: Rating compressed, earnings upside

Company newsflow has been positive in our view. This has not been reflected in share price performance and the rating has compressed year to date. The FY17e P/E is now 11.6x and EV/EBITDA 6.5x. Bearing in mind that continuing order book growth would be a trigger to raise estimates, this suggests even greater value. While there may be pipeline slippage caveats, we believe that Severfield's balance of earnings risk is to the upside.

Construction & materials

3 May 2016

Price 52.25p
Market cap £155m

Net cash (£m) at end September 2015	12.9
Shares in issue	297.5m
Free float	100%
Code	SFR
Primary exchange	LSE
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	(3.2)	(12.9)	(19.6)
Rel (local)	(9.2)	(13.7)	(12.8)
52-week high/low	73.25p	51.0p	

Business description

Severfield is a leading UK structural steelwork fabricator operating across a broad range of market sectors. An Indian facility currently undertakes structural steelwork projects for the local market and is fully operational.

Next event

FY16 results	15 June 2016
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Exhibit 1: Financial summary

	£m	2010	2011	2012	2013	2014	2015	2016e	2017e	2018e
Year end 31 March		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
		12m to Dec	12m to Dec	12m to Dec	15m to Mar	12m to Mar	12m to Mar	12m to Mar	12m to Mar	12m to Mar
PROFIT & LOSS										
Revenue		266.7	267.8	256.6	318.3	231.3	201.5	232.1	244.1	256.1
Cost of Sales		(242.6)	(246.9)	(268.8)	(330.9)	(217.8)	(186.7)	(213.6)	(221.9)	(230.0)
Gross Profit		24.1	20.9	(12.2)	(12.7)	13.5	14.9	18.5	22.3	26.1
EBITDA		21.6	19.5	(13.6)	(13.6)	12.0	13.6	17.9	21.7	25.7
Operating Profit - Edison		17.1	15.0	(17.7)	(18.6)	8.4	10.0	13.7	17.2	20.9
Net Interest		(0.9)	(1.6)	(1.6)	(2.0)	(0.6)	(0.5)	(0.4)	(0.3)	(0.2)
Associates		(0.4)	(2.5)	0.2	(0.3)	(3.0)	(0.2)	(0.2)	0.0	0.0
SBP		(0.0)	(0.3)	(0.0)	(0.1)	(0.2)	(0.5)	(0.8)	(0.8)	(0.8)
Intangible Amortisation		(2.7)	(2.7)	(2.7)	(3.5)	(2.7)	(2.6)	(2.6)	(2.6)	(1.6)
Pension Net Finance Costs		(0.5)	(0.5)	(0.5)	(0.6)	(0.5)	(0.5)	(0.5)	(0.5)	(0.5)
Exceptionals		(1.4)	(0.6)	(1.0)	(3.8)	(5.3)	(5.9)	(0.3)	0.0	0.0
Profit Before Tax (norm) - Edison		15.8	10.6	(19.1)	(20.9)	4.5	8.8	12.3	16.2	20.0
Profit Before Tax (norm)		15.3	10.1	(19.6)	(21.5)	4.0	8.3	11.8	15.7	19.5
Profit Before Tax (FRS 3)		11.1	6.8	(23.3)	(28.9)	(4.1)	(0.2)	8.9	13.1	17.9
Tax		(3.5)	(0.9)	3.9	5.7	1.4	0.3	(1.8)	(2.8)	(3.4)
Profit After Tax (norm)		11.7	7.7	(16.2)	(17.9)	3.1	7.4	10.2	13.4	16.6
Profit After Tax (FRS 3)		7.6	5.8	(19.4)	(23.1)	(2.6)	0.1	7.1	10.3	14.5
Average Number of Shares Outstanding (m)		89.0	89.3	89.3	89.3	295.8	297.5	297.5	297.5	297.5
EPS - normalised (p) - Edison		6.82	4.51	(9.42)	(10.42)	1.05	2.47	3.42	4.52	5.57
EPS - normalised (p)		6.51	4.21	(9.72)	(9.45)	0.88	2.31	3.25	4.35	5.40
EPS - FRS 3 (p)		4.47	3.41	(11.33)	(13.49)	(0.89)	0.05	2.38	3.47	4.87
Dividend per share (p)		7.5	5.0	1.5	0.8	0.0	0.5	1.0	1.3	1.6
Gross Margin (%)		9.0	7.8	-4.8	-4.0	5.8	7.4	8.0	9.1	10.2
EBITDA Margin (%)		8.1	7.3	-5.3	-4.3	5.2	6.7	7.7	8.9	10.0
Operating Margin - Edison (%)		6.4	5.6	-6.9	-5.8	3.6	4.9	5.9	7.1	8.2
BALANCE SHEET										
Fixed Assets		165.0	156.9	155.6	154.9	147.7	145.1	145.9	144.1	143.3
Intangible Assets		75.2	72.9	70.4	69.8	64.6	61.8	59.0	56.3	54.7
Tangible Assets		82.9	79.6	76.2	76.1	74.1	76.6	77.2	77.7	77.9
Investments		6.9	4.4	8.9	8.9	9.0	6.7	9.7	10.2	10.7
Current Assets		88.1	100.5	69.8	80.5	72.2	76.3	83.4	96.0	110.7
Stocks		12.6	9.1	7.1	8.2	5.8	4.8	5.5	5.7	5.9
Debtors		71.9	89.2	61.2	71.6	60.8	64.6	68.1	72.1	76.0
Cash		3.6	2.3	1.4	0.7	5.5	6.9	9.8	18.3	28.8
Current Liabilities		(99.8)	(103.6)	(97.0)	(112.5)	(57.9)	(59.7)	(62.6)	(65.6)	(68.2)
Creditors		(81.2)	(70.3)	(66.1)	(70.9)	(52.7)	(59.5)	(62.6)	(65.6)	(68.2)
Short term borrowings		(18.6)	(33.3)	(30.9)	(41.7)	(5.2)	(0.2)	0.0	0.0	0.0
Long Term Liabilities		(22.3)	(21.6)	(21.7)	(20.4)	(18.5)	(21.1)	(18.3)	(18.3)	(18.3)
Long term borrowings		0.0	(0.3)	(0.3)	(0.2)	(0.0)	(0.6)	(0.6)	(0.6)	(0.6)
Other long term liabilities		(22.3)	(21.3)	(21.4)	(20.2)	(18.5)	(20.5)	(17.8)	(17.8)	(17.8)
Net Assets		130.9	132.3	106.6	102.4	143.4	140.6	148.3	156.2	167.5
CASH FLOW										
Operating Cash Flow		(5.8)	(5.4)	12.9	3.1	2.1	11.4	16.1	19.2	23.0
Net Interest		(0.8)	(2.0)	(1.3)	(1.7)	(0.8)	(0.8)	(0.4)	(0.3)	(0.2)
Tax		(5.4)	(3.7)	(2.7)	(2.3)	0.4	(1.0)	(1.1)	(1.8)	(2.8)
Capex		(2.8)	(1.5)	(0.2)	(1.4)	(1.5)	(1.3)	(4.5)	(5.0)	(5.0)
Acquisitions/disposals		(2.9)	(0)	(2)	(3.0)	(3.5)	(1.7)	(4.0)	(0.5)	(0.5)
Financing		0	0	0	0.0	44.8	0	0	0	0
Dividends		(8.9)	(3.6)	(4.5)	(4.5)	0.0	0.0	(3.0)	(3.1)	(4.0)
Net Cash Flow		(26.6)	(16.3)	1.7	(9.7)	41.5	6.7	3.1	8.5	10.5
Opening net debt/(cash)		(11.5)	15.0	31.3	31.3	41.2	(0.3)	(6.1)	(9.2)	(17.7)
HP finance leases initiated		0	0.0	0.1	0.0	(0.2)	(0.3)	(0.1)	0.0	0.0
Other		0	(0)	(0)	(0)	0.2	(0.6)	0.1	0	0
Closing net debt/(cash)		15.0	31.3	29.7	41.2	(0.3)	(6.1)	(9.2)	(17.7)	(28.2)

Source: Company accounts, Edison Investment Research

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