

Advanced Power Components

CORPORATE

First half results - Recovery underway

8.75p[#]

Year-end August	2008A	2009A	2010E	2011E
Revenues (£m)	12.2	14.1	13.4	14.0
EBITDA (£m)	0.9	(0.3)	0.4	0.5
Adj. Pre-tax Profit (£m)	0.8	(0.5)	0.2	0.4
Adj. EPS (p)	0.2	(1.7)	1.0	1.4
Net Cash/(Debt) (£m)	0.3	(2.2)	(1.7)	(1.4)
P/E (x)	2.7	(5.3)	8.5	6.1
Dividend yield (%)	n.a.	n.a.	n.a.	n.a.
EV/EBITDA (x)	2.0	(14.5)	8.5	7.7

Key Data	
Ticker	APC.L
Shares in issue	24.4m
Market cap	£2.1m
12-mth price range	6.5p – 15.5p
Net debt	£1.7m
Next event	Dec Prelims

Source: Astaire Securities estimates

[#]Priced at market close, 07 May 2010

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APC returned to profit in H1 FY10 with a PBT of £42k (H1 FY09 loss £281K) on sales of £6.5m (FY09 H1 £6.8m), below last year but slightly ahead of budget. This is a good performance against a sector that has provided no relief so far and where visibility remains poor. Against this background APC has controlled its overheads, kept ahead of budget and strengthened its balance sheet. APC has also been developing new business which should bear fruit in H2 and in 2011. We are marginally increasing our forecast FY10 PBT from £202k to £220k and for 2011 from £289k to £320k. Our EPS forecast remains 1.0p in 2010 and increases to 1.4p in 2011, giving a PER of 8.5x for 2011 and 6.1x for 2011.

- * **Costs are under control:** APC budgeted for lower sales and introduced cost saving measures to align overheads to the anticipated level of business.
- * **Deferred consideration for the 2008 acquisitions is now paid:** This was a significant strain on cash flow in 2009 and H1 FY10 but will no longer be a factor in H2, so we expect a further improvement in cash flow for the full year.
- * **Senior management has been strengthened:** The appointment of an experienced CFO gives APC a stronger executive management team and addresses the shortcomings that contributed to last year's losses. FX controls are in place to ensure no repetition of the large currency loss in H1 FY09 and KPIs are reported monthly to ensure budget variances are addressed promptly.
- * **New lines should start to boost sales and earnings:** This boost could come as early as the second half of this year and more fully in 2011, which should leave room for further revisions to forecasts.

Company description

Advanced Power Components (APC) distributes specialised electronic components, including high reliability power components where component failure is not an option, essentially defence and aerospace and some medical applications. APC differentiates itself by selling components requiring a high degree of product and industry knowledge. APC is organised into eight semi-autonomous sales teams each concentrating on a specialised technology or industry group. Currently defence and aerospace account for about 40% of sales and transport around 35%.

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Investment Appraisal

APC has been through a torrid year but there is evidence that it has put the difficulties it faced with poor internal controls behind it. Management has been strengthened with the appointment of an experienced CFO and measures have been put in place to avoid the currency losses that plagued the first half of 2009 and to ensure that overhead expenses are appropriate for the level of trading that APC has budgeted. This has driven the return to profitability in FY10 H1.

Management has been strengthened

Profit is still modest but trading is improving and gross margins appear to have stabilised. APC has strengthened its sales effort with an increased focus on technical selling; getting the components APC distributes designed into customer programmes at an early stage. APC has started a training and hiring programme to enhance this effort, reflecting management's confidence in the future. This, coupled with efforts to expand the organic growth of the business by increasing the number of lines distributed and developing further opportunities, should lead to increased revenues both in the second half and in FY11. Administrative overheads should not need to increase above current levels to support the higher revenues although there will be some increase associated with strengthening the sales effort.

...increased focus on technical selling

Payment of the outstanding deferred consideration for the acquisition of Novacom will reduce demands on cash and APC should be able to reduce its indebtedness in the coming year.

Recovery at APC is just starting, adjusted PBT of £350k gives EPS for FY11 of 1.4p giving a relatively modest PER of 6.1x. While the level of gearing and APC's micro-cap status dictate a discount to market, there should be scope for further upwards revisions to earnings both as the recovery picks up pace and the increased sales effort bears fruit.

2010 H1 results

APC had budgeted for lower sales this first half, down about 7%. In the event H1 revenues came in slightly ahead of budget - down 4.4% at £6.5m. More importantly, APC took cost reduction measures last year and during this period to deliver a return to profitability.

Sales are lower but ahead of budget....while admin costs are 24% lower

The last six months has continued to be a difficult time for the electronic components sector; visibility has not really improved and margins have remained under pressure. APC has kept gross margins roughly in line with the figure for the full year 2009 at 30%, down from 31.8% in the first half of 2009.

APC had budgeted for this level of gross margin and controlled administrative expenses tightly. Admin expenses at £1.8m for the first half were 24% lower than in the comparable period last year at 28% of sales (2009: 35%) and this helped deliver an operating profit of £138k compared with a loss of £227k in the first half of 2009. Finance costs have increased to £96k from £54k due to the issue of loan stock and arranging a new loan facility.

2009's losses were primarily due to failures of process within APC, namely the FX losses arising from failure to cover foreign currency liabilities when they were recognised and the failure to provide timely reporting of management accounting information. The return to profit in H1 2010 despite lower sales and a lower gross margin is evidence that management has addressed those failings head on.

2009 losses due to failure of process rather than markets

Business development

Management reports that although economic conditions have not fully recovered trading is improving and is expected to continue to do so. Gross margin will probably remain flat at around 30% but the cost saving measures that have been implemented will allow overheads to be kept in line. Furthermore new reporting systems put in place by the accounting team with detailed monthly KPIs will alert management quickly to any deterioration and allow remedial action to be taken swiftly. Against this background management is guardedly optimistic about the future.

Trading is improving

We stated that we expected profit for the year to be mostly apparent in H2 and the modest profit in H1 bears out that argument. Historically H2 is stronger for APC and we expect 2010 to be no different.

Historically H2 is stronger for APC

In addition a great deal of effort has been focused on the sales team, improving technical knowledge and placing greater emphasis on ensuring the products APC distributes are designed into customer systems at an early stage. We expect this to bear fruit in H2 and in 2011. APC has also been working to secure new product to distribute. In particular Novacom and Hero have been active in this respect.

We expect that Novacom will be able to announce a potentially significant new agreement, perhaps as early as the International Microwave Symposium in Anaheim at the end of May. Hero is concentrating on key markets and hoping to develop a presence in LED lighting.

APC has been developing a range of energy saving equipment. The product called the imop (inductive motor optimisation panel) is a device intended to be installed as near as possible to motors or any other equipment relying on a magnetic field for its operation. The device is designed to optimise inductive load and make the motor run as efficiently as possible. APC has the manufacturing rights outside of North America and has been finalising designs, installing demonstration equipment and negotiating to sign up distributors. Although significant interest is being shown in this device, its design is finalised and it already qualifies for installation under the Carbon Trust's interest free loan scheme, it is still too early to assess either the scale of interest or the likely timescale. We have therefore not included imop in our forecasts.

A range of energy saving equipment has been developed but is not in our forecasts yet.

Forecasts

We anticipate a further pick up in H2 seeing a slight improvement in sales for the full year from our earlier forecast of £13.1m to £13.4m with a corresponding improvement in adjusted PBT from £232k to £250k.

We anticipate a further pick up in H2

Looking further out to FY11 we are forecasting an improvement to £14m in revenues and an adjusted PBT of £350k, giving an EPS of 1.4p. These forecasts assume that gross profit margin stays flat at 30% and that growth is solely organic from existing product lines. If as we believe is likely, APC is able to develop

distribution agreements for new product lines we would expect there to be scope for further upwards revisions to our numbers.

Changes to Forecasts

Year-end August (£000's)	2009A	2010E old	2010E new	2011 old	2011E new
Turnover	14,091	13,105	13,386	13,760	14,022
Operating profit	(406)	347	368	420	451
EBITDA	(302)	442	439	520	524
PBT (reported)	(491)	202	220	289	320
PBT (adjusted)	(461)	232	250	319	350
Adjusted EPS	(1.6)	1.0	1.0	1.3	1.4

Source: Company, Astaire Securities Estimates:

Balance Sheet

Although APC remains significantly geared it has taken measures to improve the strength of its balance sheet. In the course of the last six months, debtor days have been reduced and the finance department continues to track these, inventory levels are reduced and creditors are being paid more promptly. The company has renegotiated its bank facilities and has a lower balance on its invoice discounting facility. We expect progress to continue to be made to lower borrowing.





APC: KEY DATA

Company Description

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Website

www.apc-plc.co.uk

Management

William David	Chairman
Mark Robinson	CEO
Rob Smith	FD
Philip Lancaster	Operations
Joe Stelzer	Non-exec

Major Shareholders

Robinson Family Trusts	25.86%
J.A. Mitchell Family Trusts	19.04%
Other Directors and Officers	5.79%

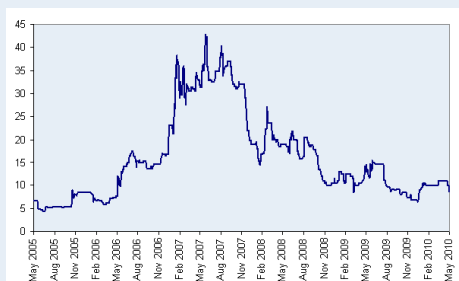
Recent News

08-Mar	Rob Smith appointed CFO
08-Jan	Conversion of loan notes

Financial Diary

17-Dec	Prelims
22-Jan	AGM

Share Price



Source: Datastream

Year-end August Key Profit & Loss Data (£000)	2008A	2009A	2010E	2011E
Turnover	12,164	14,091	13,386	14,022
Operating profit	808	(406)	368	451
<i>Operating profit margin (%)</i>	6.6%	-2.9%	2.7%	3.2%
EBITDA	899	(302)	437	524
<i>EBITDA margin (%)</i>	7.4%	-2.1%	3.3%	3.7%
PBT (reported)	732	(491)	220	320
PBT (adjusted)	816	(461)	250	350
Tax rate (%)	-3.6%	-12.4%	0.0%	0.0%
PAT (reported)	706	(430)	220	320
PAT (adjusted)	790	(400)	250	350
Adj. EPS (p)	3.2	(2)	1.0	1.4
DPS (p)	-	-	-	-
Key Cash Flow Data (£000)	2008A	2009A	2010E	2011E
Operating profit	808	(406)	368	451
Gross operating cash flow	1,660	(1,509)	596	437
Net operating cash flow	1,568	(1,707)	448	306
Capex	(767)	(946)	(50)	(87)
Free cash flow	801	(2,653)	398	219
Cash flow from investing	(767)	(946)	(50)	(87)
Cash flow from financing	(770)	1,985	140	-
<i>Incr/(Decr) in net cash</i>	31	(668)	539	219
Key Balance Sheet Data (£000)	2008A	2009A	2010E	2011E
Fixed assets	3,066	2,951	2,932	2,946
Current assets	4,664	4,250	4,585	4,993
Current liabilities	(4,796)	(4,350)	(4,276)	(4,348)
Net current assets/(liabilities)	-132	-100	310	645
Total assets less current liabilities	2,934	2,851	3,241	3,591
Long-term liabilities	(83)	(385)	(385)	(385)
Closing net assets	2,851	2,466	2,856	3,206
NAV per share (p)	11.7	10.1	11.7	13.1
Valuation	2008A	2009A	2010E	2011E
P/E (x)	2.7	-5.3	8.6	6.1
Div. yield (%)	0.0%	0.0%	0.0%	0.0%
EV/EBITDA (x)	2.1	(15.8)	9.7	7.7
FCF Yield (%)	37.5%	(124.1%)	18.6%	10.2%

Source: Astaire Securities estimates, company reports

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