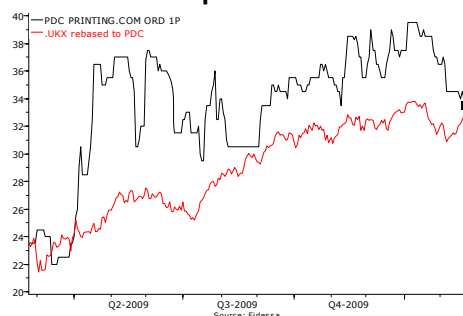


Printing.com
Looking Forward To 2012

33p

23 February 2010

Share Price: 33p



12m High: 39.5p

12m Low: 22p

Market Cap: £15m

Shares in Issue: 44.53m fully diluted

NAV/Share: 10p ex intangibles (H1'10)

Gearing: Nil. Net Cash £1.8m (H1'10)

Net Funds: (cash less lease creditor finance)
£0.6m

Interest Cover: n.a.

EPIC Code: PDC

Sector: Support Services

Market: London AIM

Broker: Brewin Dolphin

PR: Cubitt Consulting

Website: www.printing.com

Description: Printing.com provides printing for small and medium size companies (business cards, letterheads, leaflets etc) via a network of 290 franchised outlets and a wholly owned printing hub in Trafford Park.

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Yesterday's Trading Statement gave an enormous amount of reassurance about the current year outcome in spite of atrocious trading conditions. Our profit forecast is clearly in the right place. If trading can be 'broadly in line with expectations' in spite of the disruption caused by the January snows, then the business model must be close to bomb-proof. Of course the weather may have no more surprises.

During January, 'most outlets encountered some periods when they were unable to open for normal trade' and the company experienced 'the greatest disruption to the Printing.com network since its inception'. In February trading has been at 'anticipated levels'.

We leave our estimates for the year ended March 2010 unchanged. These include an uncovered dividend, something that gives us no concern because Printing.com has no debt, £1.8m cash in the bank and is also a strong cash generator. The dividend we expect shows a nominal increase on the previous year's normal dividend payout. In the previous year there was also an exceptional 2p/share 'special dividend' that was in effect a form of capital repayment to shareholders of some of the group's surplus funds.

Since our last research note, due to the general economic malaise the prospects both within the print marketplace and among Printing.com's SME customer base have deteriorated, so we are downgrading our estimates for y/e March 2011. We are cutting our sales estimate for that year by 3%, our profit estimate by 15% and also think it possible that the board may sanction a small dividend cut rather than pay an uncovered dividend for a second consecutive year.

Prospects for y/e March 2012 will look much improved. By then, enough competitors will have gone bust to have markedly changed the current cutthroat pricing environment, and also the group will lose leasing payments well into six figures, boosting cash and reducing interest in the p & l account.

Also the shares are trading at only 4.4X current year EV/EBITDA.

So there is a lot to be cheerful about.

Y/E	Group Sales	Declared Profit	Adjusted Profit	Adjusted EPS	P/E	Divi	Yield
March	£m	£m	£m	p.	X	P	%
2008A	13.5	2.4	2.4	3.5	9.4	3.00	9.1
2009A	14.5	2.1	2.1	3.3	10.0	5.15*	15.4
2010E	14.4	1.8	1.8	2.9	11.4	3.2	9.7
2011E	14.9	1.8	1.8	2.9	11.4	3.0	9.1

*2009A Dividend includes a special dividend of 2p/share

Printing.com

23 February 2010

The Impact of Winter

The poor winter weather caused Printing.com problems, particularly in early January when the issues with snow and ice were at their worst. The central printing hub at Trafford Park was effectively shut for 24 hours at one stage, with overnight snow preventing most of the new day shift arriving for work and preventing most of the previous night shift from going home. In addition, TNT, the delivery contractor, was unable to make collections.

Most of the stores, both the franchised Territory Stores and the local Bolt-On stores that are operated through the territory franchises, also encountered some periods when they were unable to open for normal trade.

Later in January and through February trading returned to 'anticipated levels', but we would warn that February is not yet over and more snow is forecast throughout the country over the next week.

In our opinion Printing.com has done well to keep trading on track in spite of the problems in January. The fact that sales have been back to normal, in spite of weather and economic conditions continuing to be dreadful, is both reassuring and encouraging for shareholders.

Price Cutting

The Trading Statement says that 'monthly offers and the like continued to be a greater part of the sales mix than in previous years'.

This is, if anything, an understatement. Printing.com's normal trading pattern is to operate a 'January sale'. Because of the January trading disruptions, management extended this sale through to the first week of February, so the good sales figures will be accompanied by tighter margins for the month. Our current year forecast, which is unchanged, was already looking for a lower Operating Margin for the full year (11.7%) than was declared at the half year (12.2%) so we are comfortable we have made sufficient allowance for this.

We note, however, that the flurry of cut price offers from Printing.com's unquoted rivals has grown into a blizzard in recent weeks. It is clear to us that the market for printing to SMEs – business cards, compliment slips, letterheads and A4 sales leaflets that are the core offerings at Printing.com – have become intensely competitive. Much of the cut price work being offered is in fact sub-standard, on poor paper stock and using machinery too old to give a quality end product. But Printing.com is going to have to trade in this environment in the new financial year that starts in April. Also the likelihood is growing of a 'double dip' recession as the post-election Government struggles to regain control over the national economy.

2011 Estimates

For the year to March 2011 we have reduced our sales estimate from £15.3m to £14.9m. We believe volumes through the central printing hub will be up, but only because of the greater number of bolt-on franchises trading. We expect sales per outlet in money terms to be down, both for the territory franchises and the bolt-on franchises. This is likely to be because of pricing pressure; volumes we expect to be pretty much unchanged. Fortunately Printing.com, because of its single central hub operating system, probably has the lowest cost base of any organisation of its type in Britain, so in strategic terms a price war in the marketplace plays straight into its hands.

We have reduced our 2011 profit estimate from £2.1m to £1.8m, because there are certain fixed costs that cannot be reduced, and because the group is unlikely to be able to bargain down the cost of its paper supplies to the same extent.

It is possible that some bolt-on franchises may fail. There are approximately 260 of these, so some attrition is inevitable, and the Printing.com offering usually only accounts for a small proportion of a bolt-on's total business so the failure of one of these franchisees is no reflection on the Printing.com business offering. In the last Annual Report trade receivables were running at £3.1m, or 11 weeks' sales and had shown little change over the previous year. Most of this was money due from franchisees. Also there were £0.2m of loans outstanding to franchisees.

Many end-customers will fail as well, but franchisees following Printing.com's policy of rarely allowing credit and insisting on payment up front should be well protected.

2012 Estimates

We can look for considerable improvement in the year to March 2012, even if the UK economy remains sick. This is for the following reasons:

- By then, two years of severe pricing pressure and poor economic conditions will have reduced the number of printers competing in the marketplace for SME print work.
- Leasing agreements for most of the equipment in the Central Hub will have ended. Depreciation charges will tail off and interest charges for operating leases of £108,000 will be saved.. Cash flow will benefit even more, because the capital element of the lease payments does not pass through the p & I account. All of the leases are traditional rather than balloon and the equipment becomes the property of Printing.com upon expiry. Because of the recession there is plenty of spare capacity at the hub, so we expect the capital expenditure, other than on the business software, programme to remain low through to and probably beyond 2012. Printing.com will become increasingly cash rich.

Overseas Franchises

The Trading Statement contained no further news on the overseas franchise situation. As we understand it, the situation is at present:

- **New Zealand.** Operating satisfactorily, but this is a small country unlikely to make a huge impact on the group short term.
- **France.** Also operating satisfactorily, but because France is using the Old Trafford central hub rather than the national franchisee operating its own hub, the costs are significant. It is unlikely to be a major profit generator until the national franchisee develops or buys its own printing facility.
- **The USA.** Only part of the country is covered by the franchise granted. The franchisee operates its own hub and is actively recruiting Bolt-on franchisees but remains in the early stages of development.

The last accounts showed £268,000 of trade receivables denominated in foreign currencies. £388,000 of revenue was from outside the UK and Ireland, and royalty income was less than £100,000.

Dividends

The dividend we forecast for the current financial year will not be fully covered by after tax earnings. We do not find this a problem because Printing.com has £1.8m of cash and no debt, and indeed last year paid an additional 2p/share 'special' dividend in order to place some of its surplus cash in the hands of shareholders. Also, cash flow was considerably stronger than profit – cash flow per share amounted to 6.2p per share before a relatively modest capex programme, so the dividend last year was roughly twice covered by cash flow and will be at least 150% covered by cash flow in the current financial year.

The situation for 2011 is not quite as simple, however. Will the directors be happy for a second consecutive year of dividend not fully covered by earnings? We point out that cash flow cover will remain strong, there will still be net cash in the company and the prospect will be for even stronger cash flow in 2012. We have taken a prudent view and assumed the 2011 dividend will be edged back to the point where it is fully covered, or virtually fully covered, by earnings.

Chief executive Tony Rafferty owns 20.7% of Printing.com's shares so other shareholders can assume that any decision to cut the dividend will not be taken lightly.

Conclusion

This remains one of the soundest, most stable companies in the small and mid cap quoted company marketplace. The shares trade at c. 6X current year cash flow, and 4.4X EV/EBITDA, with the prospect of a good boost to profit and cash flow two years out. The dividend, while it may be trimmed, is in our view safe from any serious cut. The shares have outperformed over twelve months on the basis of capital value alone, and on a Total Return basis have been huge winners. There won't be the excitement here to generate a massive share price rise short term, but medium term this company will continue to be a winner.

Y/E March £000	2008A	2009A	2010E	2011E
Sales at Quoted Company and Retail Equivalent				
Declared Transactional Turnover for Quoted Co.	13,479	14,468	14,395	14,879
Equivalent Turnover at Retail Prices	24,583	26,291	25,036	24,513
Quoted Company Declared Turnover				
Printing Revenue at Central Hub	12,924	13,563	13,288	13,689
Retailing Revenue from Wholly Owned Stores	448	529	880	1,021
Network Partners	0	0	0	0
Licence Fee Income less Commissions & Discounts	50	-12	-200	-300
International	57	388	427	469
Total Declared Turnover	13,479	14,468	14,395	14,879
Y/E March £000				
The P & L Account				
Total Sales Revenue	13,479	14,468	14,395	14,879
Changes in stock of finished goods	5	1	0	0
Other Operating Income	0	0	0	0
Material Costs	4,473	4,727	4,894	5,208
as % of Sales Revenue	33.19%	32.67%	34.00%	35.00%
Staff Costs	3,218	3,598	3,599	3,720
as % of Sales Revenue	23.9%	24.9%	25.0%	25.0%
Depreciation/Amortisation	1,378	1,334	1,334	1,334
Other Operating Charges	2,123	2,877	2,879	2,827
as % of Sales Revenue	15.8%	19.9%	20.0%	19.0%
EBITDA	3,670	3,267	3,023	3,125
EBITDA Margin	27.2%	22.6%	21.0%	21.0%
Operating Profit/-Loss	2,292	1,933	1,689	1,790
Operating Margin	17.0%	13.4%	11.7%	12.0%
Profit on sale of shops into franchises	0	0	0	0
Interest (+) In, (-) Out	129	130	100	0
Pre-tax Profit	2,421	2,063	1,789	1,790
Tax Charge (-=Credit)	789	603	501	501
Tax Charge %	33%	29%	28%	28%
After Tax Profit/Loss	1,632	1,459	1,288	1,289
Cost of Dividend	1,396	1,408	1,440	1,350
Retained Earnings	236	51	-152	-61
Average No Shares Fully Diluted	46,547	44,703	44,994	44,994
Earnings/Loss Per Share, p, Diluted, p	3.5	3.3	2.9	2.9
Dividend Per Share p.	3.0	3.2	3.2	3.0
Special Dividend Per Share p.	2	2	0	0
Goodwill amortisation	0	0	0	0
Pre-tax Profit, Adjusted	2,421	2,063	1,789	1,790
EPS, Adjusted Fully Diluted, p.	3.51	3.3	2.9	2.9

Management	Major Shareholders																		
<p>Chairman: George Hardie</p> <p>Chief Executive: Tony Rafferty</p> <p>Finance Director: Alan Roberts</p> <p>Operations Director: Peter Gunning</p> <p>Non-Executive Director: Les Wheatley</p>	<table> <tr> <td>Tony Rafferty:</td> <td>20.7%</td> </tr> <tr> <td>Brewin Dolphin:</td> <td>8.5%</td> </tr> <tr> <td>Williams de Broe:</td> <td>6.3%</td> </tr> <tr> <td>Barclays Investors:</td> <td>5.5%</td> </tr> <tr> <td>George Hardie</td> <td>3.8%</td> </tr> <tr> <td>Rathbone Investment Mgt</td> <td>3.4%</td> </tr> <tr> <td>Collins Stewart</td> <td>3.2%</td> </tr> <tr> <td>3G Capital Management</td> <td>3.1%</td> </tr> <tr> <td>Other Directors</td> <td>2.2%</td> </tr> </table>	Tony Rafferty:	20.7%	Brewin Dolphin:	8.5%	Williams de Broe:	6.3%	Barclays Investors:	5.5%	George Hardie	3.8%	Rathbone Investment Mgt	3.4%	Collins Stewart	3.2%	3G Capital Management	3.1%	Other Directors	2.2%
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Key Dates	Key Milestones																		
<p>'Pre-Close' Trading Statement: 6 April 2010</p> <p>Full year results: June 2010</p>	<p>1999: First store opened</p> <p>2002: First franchises granted</p> <p>2004: Total outlet numbers pass 100</p> <p>2007: Total outlet numbers pass 200. First international Master licence granted over New Zealand.</p> <p>2007: Launches Printing.com France and network partners initiative</p> <p>2008: Launches Printing.com USA</p> <p>2009: Announces special dividend of 2p/share</p>																		

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