Stockdale

14 July 2016

Buy

Sabien Technology*

Pilot programme showing promise

The key elements of the interims in our view are that 30 UK pilots have been agreed for this heating season and that the sales pipeline has increased to £6.4m from the last-reported £5.8m. As anticipated the adj. LBT increased to £1.0m in the first half due to the extra costs incurred in increasing the pilot programme. It is encouraging that the company still anticipates meeting expectations for FY2016. With no changes in our forecast of the move towards profitability in FY2017 we reiterate our 50p DCF-derived TP and Buy.

Current price
5p

Target price
50p

Market cap
£2.1m

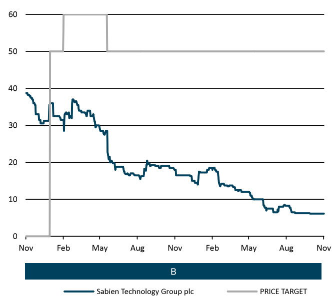
Key forecasts

Year to Jun	Sales £m	PBT £m	EPS p	EPS growth %	DPS p	Dividend yield %	P/E x	EV/EBITDA x	ROIC %
2015A	1.7	-0.6	-2.2	188.9	0.0	0.0	na	-0.8	-19.8
2016E	2.2	-1.2	-2.7	18.4	0.0	0.0	na	-1.2	-51.4
2017E	3.6	-0.2	-0.4	-86.0	0.0	0.0	na	-10.0	-9.3
2018E	4.8	0.6	1.2	-436.7	0.0	0.0	3.9	1.8	22.1

Source: Stockdale estimates, company data

Price performance

	Stock	All-Share
1 month:	-7.1%	-5.1%
3 month:	-20.4%	-7.8%
12 month:	-73.7%	-12.8%



New "free" pilot strategy implemented

Up until last summer Sabien charged c.£20k to run pilots for a potential customers. These involved fitting an M2G device on to at least three of their boilers to demonstrate a 10-25% reduction in gas usage via a report including substantial data analysis. While the proposition should have been compelling it inevitably led to delays as the charge meant that public sector clients typically needed to undergo a tender process first. To take advantage of the substantial level of interest it has built in its boiler optimisation technology and counteract the inertia due to the £20k charge Sabien now includes the cost of the pilot into a roll-out. Importantly, the qualification criteria remain – chiefly a minimum spend of £0.25m, good asset log data and the client's willingness to devote some of its engineering resource to the pilot programme. To increase the number of pilots it is capable of running, Sabien has increased its headcount by 50% to 24 and has secured 30 UK pilots of its up to 35 pilots in total targeted for FY2016.

Increased sales pipeline

The main reason for introducing the more aggressive piloting strategy was to stimulate a meaningful increase in the sales pipeline. We forecast this to grow from the £6.4m reported in the interim results to £10.8m for the beginning of FY2017. We have used the historical rate of 87% of M2G pilots converting into the sales pipeline and then 69% to an estate-wide roll-out. We have then based our headline forecasts for the sales pipeline and sales on the minimum £0.25m spend. If the historical average of £0.4m spend per client were realised, then profitability would be achieved in FY2017. The company has set itself a five-year target of a sales pipeline of £25m.

DCF valuation captures benefits of the new strategy

In addition to the sales pipeline target of £25m, management also set a five-year revenue target of £8m and EBITDA margin of 25%. With no meaningful profitability forecasts in the next two financial years in our base case forecasts we continue to use a DCF analysis to derive our target price. Our 50p DCF per share assumes a WACC of 12% and a 2% long-term growth rate, both of which are conservative in our view. While we consider FY2016 to be "a year of investment" we are most encouraged by the recent £0.3m order and hope to see news of further orders and building sales pipeline start to drive the share price higher.

Last results
Interims, 9 Feb 16

Next results
Finals, Oct 16

Next event
Finals, Oct 16

Reuters / BBG
SNT.L / SNT LN

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FTSE AIM

Priced at close
8 Feb 2016

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Stockdale

Overview

Company activities

Sabien Technology Group (Sabien) is a fabless provider of energy efficiency technology for commercial organisations in the public and private sectors. Based upon established technology, Sabien's M2G product is proven to reduce carbon emissions and energy consumption by between 10% and 25%, with typical payback in less than two years. The company is based in Watford. To date, Sabien has over 150 customers utilising M2G technology. It sells directly as well as developing an increasingly important indirect sales channel.

Key issues on which investors must take a view

The key issue relates to the success of the more aggressive piloting programmes. By having a more substantial sales pipeline Sabien's revenues and profits should be less influenced by possible contract delays. The other key issue is how quickly some of the channel partners start to deliver meaningful sales volumes.

Likely direction of consensus revisions

Our forecasts reflect the company's order book (visibility of around six months) and a discounted return from the company's sales prospects pipeline. Our estimates do not include the likelihood of new large-scale (c.£1.0m to £2.5m) contracts being secured and we assume historical conversion rates on the sales pipeline to revenue. Despite H2 bias to the FY2016 numbers, given the size and lumpiness of the growing sales pipeline we think earnings upside is now possible in future years.

Valuation and reason behind target price

We believe our DCF-derived 50p target price can be interpreted as discounting relatively modest growth. Our immediate projections are based on Sabien's order book and the size of its sales prospects pipeline which was last reported at £6.4m. While the timing of the increase in the sales pipeline and its conversion rate remains uncertain following the adoption of the more aggressive piloting programmes, we believe that it will deliver a significant uplift in revenue in due course.

Risks to our view

While Sabien is still not at the stage of establishing sustained and growing group profitability, we are encouraged by the more aggressive piloting model. The degree of success of this will influence our view either negatively or positively.

Assumptions

Table 1 shows that we have made no changes to our assumptions post the interim results and we continue to factor in the sales pipeline building to £10.84m at the start of FY2017 from the £6.4m reported at the time of the interim results. In our base case forecasts we assume an average spend of £250k a client (based on the minimum spend required to qualify for a "free" pilot) vs. the historical average spend of £400k. Table 2 shows the effect on our forecasts if we assume revenues were at the historic average of £400k - Sabien would achieve profitability in FY2017E rather than our current assumption of FY2018E.

Table 1: Assumptions

Year-end June (£'000)		2015A	2016E	2017E	2018E	2019E	2020E
Max. no. of Pilots		8	35	40	50	60	70
Pilots converting to Pipeline		?	26	30	37	45	52
Addition to Pipeline at min £'000	**250**	**?**	**?**	**6,500**	**7,500**	**9,250**	**11,250**
Addition to Pipeline at average £'000	400	?	?	10,400	12,000	14,800	18,000
Pipeline at start year (min)		**6,900**	**6,200**	**10,840**	**15,088**	**19,812**	**25,118**
Pipeline at start year (average)		6,900	6,200	14,740	19,588	25,362	31,868
Revenue at 30% conversion (min)		1,744	1,860	3,252	4,526	5,943	7,535
Revenue at 30% conversion (average)		1,744	1,860	4,422	5,876	7,608	9,560
Remaining pipeline (min)		5,156	4,340	7,588	10,562	13,868	17,583
Remaining pipeline (average)		5,156	4,340	10,318	13,712	17,753	22,308
Revenue from trials		1,744	1,860	3,252	4,526	5,943	7,535
% increase		*-18.5*	*6.7*	*74.8*	*39.2*	*31.3*	*26.8*
Revenue (other)		0	300	300	300	300	300
Total Revenue		**1,744**	**2,160**	**3,552**	**4,826**	**6,243**	**7,835**
Cost of sales		(513)	(648)	(1,066)	(1,448)	(1,873)	(2,351)
% revenue		*-30.0*	*-30.0*	*-30.0*	*-30.0*	*-30.0*	*-30.0*
Gross profit		**1,231**	**1,512**	**2,486**	**3,378**	**4,370**	**5,485**
% margin		*70.6*	*70.0*	*70.0*	*70.0*	*70.0*	*70.0*
Operating expenses		(1,812)	(2,678)	(2,678)	(2,732)	(2,787)	(2,842)
% rev and then increase from 2017		*-101.5*	*-144.0*	*1.0*	*1.0*	*1.0*	*1.0*
Total EBIT		**(581)**	**(1,166)**	**(192)**	**647**	**1,584**	**2,642**
% margin		*-33.3*	*-62.7*	*-5.9*	*14.3*	*26.6*	*35.1*

Source: Company data, Stockdale estimates

Table 2: Sensitivity analysis based on an average spend of £400k per client

Year-end June (£'000)	2015A	2016E	2017E	2018E	2019E	2020E
Revenue from trials	1,744	1,860	4,422	5,876	7,608	9,560
% increase	*-18.5*	*6.7*	*137.7*	*32.9*	*29.5*	*25.7*
Revenue (other)	0	300	300	300	300	300
Total Revenue	**1,744**	**2,160**	**4,722**	**6,176**	**7,908**	**9,860**
Cost of sales	(513)	(648)	(1,417)	(1,853)	(2,373)	(2,958)
% revenue	*-30.0*	*-30.0*	*-30.0*	*-30.0*	*-30.0*	*-30.0*
Gross profit	**1,231**	**1,512**	**3,305**	**4,323**	**5,536**	**6,902**
% margin	*70.6*	*70.0*	*70.0*	*70.0*	*70.0*	*70.0*
Operating expenses	(1,812)	(2,678)	(2,678)	(2,732)	(2,787)	(2,842)
% rev and then increase from 2017	*-101.5*	*-144.0*	*1.0*	*1.0*	*1.0*	*1.0*
Total EBIT	**(581)**	**(1,166)**	**627**	**1,592**	**2,749**	**4,060**
% margin	*-33.3*	*-62.7*	*14.2*	*27.1*	*36.1*	*42.5*

Source: Company data, Stockdale estimates

Valuation

We believe that a DCF analysis remains the most appropriate way to value Sabien and given we have made no changes to any of our forecasts our DCF per share continues to be 50p. In the analysis we continue to assume a WACC of 12% and a long-term growth rate of 2%, both of which we view as conservative. In FY2016 we believe that investors will focus on whether management hits the KPIs in terms of number of pilots and, more importantly, increasing the sales pipeline to £10.8m for the beginning of FY2017.

Table 3: Valuation summary

Year-end June (£m)		Value	Proportion (%)
NPV cash flow 2014-2026		8.3	39.7
Cash flow @ 2026	4.9		
Terminal multiple	10.0		
Terminal EV	49.1		
PV of terminal EV		12.6	60.3
Total PV (EV)		20.9	
Plus net cash FY2015		1.1	
DCF equity value (£m)		**22.0**	
Fully-diluted no. of shares (m)		44.0	
DCF per share (p)		50.0	
Assumptions:			
L-T perpetuity growth rate (%)	*2.0*		
WACC (%)	*12.0*		

Source: Company data, Stockdale estimates

For illustrative purposes, in Table 4 below we have again included some companies which investors might consider to have some similar characteristics as Sabien. Unfortunately, there continues to be little meaningful data, not least because we are now forecasting Sabien to be loss-making for the next two years in our base case forecasts.

Table 4: Peer group analysis

Calendarised data	Price	Market cap	P/E		EV/EBITDA		EV/sales	
to June year end	(p)	(£m)	2016E	2017E	2016E	2017E	2016E	2017E
Sabien Technology	**4.9**	**2.2**	**nm**	**nm**	**nm**	**nm**	**0.7**	**0.5**
APC Technology Group	8.9	8.1	na	na	na	na	na	na
Flowgroup	13.8	43.7	na	na	na	na	na	na
Smart Metering Systems	390.3	336.0	na	na	na	na	na	na
Linear average			na	na	na	na	0.7	0.5

Source: Stockdale estimates, Factset. Priced at close: 8 February 2016

Financials

Table 5: Income statement

Year end June (£ 000)	2015A	2016E	2017E	2018E
Revenues	**1,744**	**2,160**	**3,552**	**4,826**
% increase	*-18.5*	*23.9*	*64.4*	*35.9*
Cost of sales	-513	-648	-1,066	-1,448
% group revenues	*29.4*	*30.0*	*30.0*	*30.0*
% increase	*-19.0*	*26.3*	*64.4*	*35.9*
Gross profit	**1,231**	**1,512**	**2,486**	**3,378**
% group revenues	*70.6*	*70.0*	*70.0*	*70.0*
Operating expenses	-1,812	-2,678	-2,678	-2,732
% group revenues	*103.9*	*124.0*	*75.4*	*56.6*
Operating profit (pre-x)	**-581**	**-1,166**	**-192**	**647**
% group revenues	*-33.3*	*-54.0*	*-5.4*	*13.4*
Exceptional/non-recurring items	-	-	-	-
% gross profit	-	-	-	-
Operating profit	-581	-1,166	-192	647
% group revenues	*-33.3*	*-54.0*	*-5.4*	*13.4*
Net interest inc/(chrg)	13	-	-	-
Other financial items	-	-	-	-
Net financial items	13	-	-	-
Net interest % net debt	*1.1*	-	-	-
PBT	-568	-1,166	-192	647
% group revenues	*-32.6*	*-54.0*	*-5.4*	*13.4*
PBT (pre-x)	**-568**	**-1,166**	**-192**	**647**
Tax	-215	-	29	-97
% PBT	-	-	*15.0*	*15.0*
% pre-exceptional PBT	-	-	*15.0*	*15.0*
Deferred tax on pensions	-	-	-	-
Total tax charge	-215	-	29	-97
Net profit	-783	-1,166	-163	550
% group revenues	*-44.9*	*-54.0*	*-4.6*	*11.4*
Net profit (pre-x)	**-783**	**-1,166**	**-163**	**550**
% group revenues	*-44.9*	*-54.0*	*-4.6*	*11.4*
RoE	*-40.0*	*-72.8*	*-11.2*	*27.0*
Basic EPS (p)	-2.4	-2.7	-0.4	1.2
% increase	*nm*	*nm*	*nm*	*nm*
EPS (pre-x) (p)	**-2.2**	**-2.7**	**-0.4**	**1.2**
% increase	*nm*	*nm*	*nm*	*nm*

Source: Company data, Stockdale estimates

Table 6: Cash flow

Year end June (£ 000)	2015A	2016E	2017E	2018E
Operating profit	**-581**	**-1,166**	**-192**	**647**
Depreciation reversal	45	24	25	23
Amortisation	47	47	47	47
Impairments	-	-	-	-
Tax reversal	-	-	-	-
Reversal of non-cash exceptionals in P&L	-	-	-	-
Change in core working capital	**220**	**-50**	**-166**	**-152**
(Profit)/loss on sale of FA	-	-	-	-
Cash tax (paid)/received	-	-	29	-97
Changes in provisions	-	-	-	-
Cost of equity employee share schemes/bonuses	-	-	-	-
Foreign exchange	-	-	-	-
Share based payments	2	24	24	24
Other items	-	-	-	-
Changes in provisions	-	-	-	-
Cost of equity employee share schemes/bonuses	-	-	-	-
Gross cash flow (as stated)	-267	-1,121	-233	492
Net interest (paid)/received	13	-	-	-
Gross cash flow	**-254**	**-1,121**	**-233**	**492**
Gross TFA capex	-20	-20	-20	-20
Proceeds from TFA disposals	-	-	-	-
Net capex on TFA	-7	-20	-20	-20
% group revenues	*0.4*	*0.9*	*0.6*	*0.4*
Intangible fixed assets expenditure	-	-	-	-
Disposal of businesses	-	-	-	-
Issue of ordinary shares	98	700	-	-
Debt	-	-	-	-
Dividends paid	-91	-	-	-
Balancing item	-	-	-	-
Change in cash	**-254**	**-441**	**-253**	**472**
Net cash/(debt)	**1,171**	**730**	**477**	**948**

Source: Company data, Stockdale estimates

Table 7: Balance sheet

Year end June (£ 000)	2015A	2016E	2017E	2018E
Assets				
Tangible fixed assets	68	64	59	56
Goodwill/intangibles	508	461	414	367
Deferred tax assets	-	-	-	-
Non-interest bearing investments	-	-	-	-
Non-current assets	**576**	**525**	**473**	**423**
Inventories	207	256	422	573
Trade and other receivables (debtors)	282	349	574	780
Gross cash (and equivalents)	1,171	730	477	948
Current assets	**1,660**	**1,336**	**1,473**	**2,302**
Total assets	**2,236**	**1,861**	**1,946**	**2,725**
Liabilities				
Provisions	-	-	-	-
Deferred tax liabilities	-	89	89	89
Gross debt (and equivalents)	-	-	-	-
Non-current liabilities	**-**	**89**	**89**	**89**
Provisions	-	-	-	-
Trade and other payables (creditors)	-281	-348	-572	-778
Tax liabilities	-	-	-	-
Current liabilities	**-281**	**-348**	**-572**	**-778**
Total liabilities	**-281**	**-259**	**-483**	**-689**
Equity				
Share capital	1,650	2,200	2,200	2,200
Equity reserve	-	-	-	-
Share premium	-	-	-	-
Other reserve	187	332	332	332
Retained earnings	118	-930	-1,070	-496
Shareholders' funds	1,955	1,602	1,463	2,036
Minority interests	-	-	-	-
Equity capital	**1,955**	**1,602**	**1,463**	**2,036**

Source: Company data, Stockdale estimates

SECTION BREAK (DO NOT DELETE)

Explanation of recommendations

Each structure below is based on total shareholder return defined as the absolute rise in share price plus dividend payment over a 12-month period

Stockdale recommendation structure		Stockdale recommendation proportions in last quarter			
		All stocks excluding AIM		Corporate stocks excluding AIM	
Buy	+20% or more	Buy	72.0%	Buy	94.4%
Add	+10% to +20%	Add	4.0%	Add	0.0%
Neutral	(+/-) 10%	Neutral	24.0%	Neutral	1.3%
Sell	-10% or more	Sell	0.0%	Sell	0.0%

Source: Stockdale

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