12th May 2017

Titon Holdings Plc

60 percent ABV

Three score percent is a big number and even bigger when it measures 'alcohol by volume' i.e. in science 60% ABV equates to 105 proof. The latter number is also the suffix for Glenfaclas's best-in-class malt whisky; and the eponymous distillery remains in founding family hands. Titon has distilled its own 60 percenter in H1 profits and its founder still sits on the Board: absolute best value.

- **Results:** pre-tax profits in the half year to 31 March 2017 rose some 60% to £1.2 million (and this was post a £234,000 restructuring debit) - on revenue some 30% ahead at just over £14 million. EPS increased 34% after a higher tax rate and the interim dividend was raised 20% to 1.50 pence per share. South Korea, the Group's largest net contributor did very well indeed.

- **Metrics:** EBITDA margins in H1 were bottled at 8.3% (2016: 7.6%) and adjusted RONA, ROCE and Capital Turn corked 19.0%, 13.8% and 2.3x respectively. Liquidity is peerless, too, with a Quick Ratio of 1.94; plus improved net cash at £2.71 million, which is up from £2.46 million.

- **Forecasts:** such was the strength of H1, we have triple-distilled our forecasts, too, and we now expect fiscal 2017 to pour a pre-tax profit measure very close to our previous 2019 number. That said, 2017's full year EPS will be singularly impacted by a step change in the tax rate due to the geography of profit.

- **Risks:** the Chairman spoke of both Brexit and the imminent General Election creating "degrees of uncertainty" in the UK. "Nonetheless, we expect our core UK businesses to continue to grow". Despite the headlines, too, and the attendant Kim Jong-un, South Korea is set for "another strong performance" with support from the US and continental Europe. In the Group's core product market, too, the provision of quality indoor air is a major health consideration.

- **ABV:** The unique Hardman UK Building Materials Sector comprises 22 companies with a market value of £8.0 billion and a valuation of 10.1x EV/EBITDA on a trailing 12 month basis. Titon is seventh cheapest at 6.8x despite an oak-aged Total Shareholder Return of 76.7% over 12 months, which is also the Sector's best (i.e. the Sector average TSR over the past year is 29%).

Financial summary and valuation

Year-end Sept. (£m)	2014	2015	2016	2017E	2018E	2019E
Sales	19.3	22.3	23.7	27.0	29.1	30.9
EBITDA	1.70	2.13	2.33	2.40	2.56	2.68
Underlying EBIT	1.14	1.56	1.77	1.81	1.95	2.04
Statutory PTP	1.33	1.87	2.14	2.45	2.65	2.81
Underlying EPS (p)	8.5	12.6	15.2	13.6	14.6	15.6
Statutory EPS (p)	8.5	12.6	15.2	13.6	14.6	15.6
Net (debt)/cash	2.1	2.9	2.4	2.7	2.8	3.0
Shares issued	10.8	10.8	10.9	10.9	10.9	10.9
P/E (x)	19.7	13.3	11.0	12.3	11.4	10.7
EV/EBITDA (x)	9.5	7.2	6.8	6.5	6.0	5.7
DPS (p)	2.50	3.00	3.50	4.00	4.80	5.75
Yield	1.5	1.8	2.1	2.4	2.9	3.4

Source: Hardman & Co Research

Construction & Materials

Source: Eikon Thomson Reuters

Market data

EPIC/TKR	TON
Price (p)	167.5
12m High (p)	167.5
12m Low (p)	81.5
Shares (m)	10.9
Mkt Cap (£m)	18.3
EV (£m)	15.8
Free Float	97%
Market	MAIN

Description

Titon designs, manufactures and supplies a comprehensive range of passive and powered ventilation products; plus, handles, hinges and locking for doors and windows. "The home of domestic ventilation systems and door and window hardware".

Company information

Executive Chairman	Keith Ritchie
Chief Executive	David Ruffell

01206 713 800
www.titonholdings.com

Key shareholders

Rights & Issues IT	11.6%
MI Discretionary UF	7.3%
Chairman	9.0%
Other Directors	8.0%
Founder/NED	15.9%
Family	7.1%

Next event

15 May-17	UK Shareholder As.
30 Sept-17	Year end
Dec 2017	Final results

Analysts

Tony Williams 020 7194 7622
tw@hardmanandco.com

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Prologue

Prior to the introduction of scientific industrial measurement, the ability to determine actual alcohol content was difficult. Wily imbibers, however, used a trick by mixing whisky, for example, with gunpowder and then igniting it. If the flame was bright, the whisky was "proof" and the alcohol content was right. But, if the flame was bluish and weak, it was "under proof" (and if the mixture exploded, it was "over proof"). Later, it was empirically discovered that the "proof" point is around 57% alcohol by volume (ABV).

The British (but not the more simple Americans) adjusted their alcohol scale around this point (i.e. 57% is 100 proof). It is also possible to have more than 100 proof and the fabulous Glenfarclas 105 (which does what it says on the bottle) has a 60% ABV. It is also reckoned to be one of the best cask strength single malts on the Planet and, since 1865, has been produced at the Glenfarclas Distillery on Speyside. The businesses also remains truly independent being run now by the fifth and six generations of the Grant family.

60% ABV is the top of the range at Glenfarclas just as it is for Titon which distilled a 60% rise in its H1 pre-tax profit to £1.2 million (and this after a restructuring debit of £234,000). Similar to its Scottish cousin, too, Titon is still 40% or so owned by its founder, John Anderson, his family and the Directors.

The Group's top line also barrelled almost 30% to a neat £14.0 million including the UK as a comparable teetotaller with an 18% slurp while South Korea, the US and 'Other locals' poured gains of 34, 53 and 70%.

In terms of Segment profit, the UK fell 10% to just under £1 million; and with it margins slid 450 basis points to 14.0%. South Korea, however, delivered a virtual double contribution to in excess of £900,000 and with it profitability went from 14.8 to 20.2%; it is also the largest contributor to Titon's net profit. Did you hear the one about the country which recently locked up a sitting President and is on the verge of thermo-nuclear warfare with its bellicose northern neighbour? Elsewhere, the US and, what are largely exports to continental Europe, contributed more than £400,000 of profit which is more than 70% better than last time.

Group-wide the metrics are also very good with an EBITDA margin of 8.3% in the period (2016: 7.6%) and adjusted RONA, ROCE and Capital Turn of 19.0%, 13.8% and 2.3x respectively. Liquidity is peerless, too, with a Quick Ratio 1.94; plus improved net cash at £2.7 million.

Looking through the glass, the UK should bubble along while "another strong performance" is expected in South Korea; and in Q1 of this year, the Nation's GDP expanded at its fastest quarterly rate (0.9%) since Q2 2016. It was also 2.7% up on a year ago. Meantime, the US and continental Europe are also expected to grow.

On the fizz of the first half, we have triple-distilled our forecasts and we now expect the fiscal 2017 pre-tax glass (£2.45 million) which was previously our fiscal 2019 beaker, pretty much. Yes, due to the geography of profit generation, the tax charge rises sharply (from 9 to 20%) which disturbs the progression of EPS this year before normalising thereafter. Indeed, there is no glass half empty here with Titon the Sector's best performer over the past year and still seventh cheapest. ABV

Half year results to 31 March 2017

Profit & loss

In the six months ending 31 March 2017, Titon's gross and net revenue rose 30 and 29% to £14.4 and 14.0 million respectively (and the £375,000 difference is derived from Inter-segment trading exclusively in the UK). For the record, too, the net top line gain on a constant currency basis was +20%.

At the same time, the Gross Margin was sustained (near as dammit) at 28.4% (2016: 28.7%) and £4.0 million in quantum - and this showed a fulsome 28% rise in the half year (2016: £3.1 million).

Thereafter, Administration expense as a percentage of net revenue eased from 17.9 to 16.8% whilst Distribution Costs nudged the other way marginally from 3.1 to 3.5%. Meantime, R&D took 2.0% of revenue albeit down from 2.7%.

Operating profit or Earnings before Interest and Tax (EBIT) increased 56% to £0.9 million - shall I repeat that? In turn, this meant margins widened from 5.1 to 6.1%. Note, too, that this comes after a £234,000 debit to exit a nascent UK business unit (see commentary in Operations analysis)

Net interest contributed £7,000 (2015: £4,000) whilst the Group's South Korean Associate increased its contribution 75% to £320,000; and it was clearly a very good six months in the lower half of the Korean Peninsula (and there's more to come - see below and over).

In turn, Profit before Tax (PBT) soared 60.7% from £0.7 to 1.2 million (or £1.04 million in constant British Pounds i.e. +41%).

Taxation took a sharply higher 23.8% (2016: 16.3%) due to the geographical mix of profits (i.e. more outside of the UK). For example, BTS, the South Korean Minority (like its sister subsidiary) almost doubled its profits which meant a 'Non-controlling interest' debit of £237,000 (2016: £130,000). This meant that the surge in Net Profits was "only" 37% with Basic Earnings per Share (EPS) gaining 34% to 6.09 pence (i.e. there were a small number of extra shares in issue during the half year).

The Interim Dividend was increased, confidently, by 20% to 1.50 pence per share with cover at 3.7x (2016: 3.3x).

Profit and loss			
Half years to 31 March	**2016**	**2017**	**% chge**
GBP million:			
Gross revenue	11.113	14.387	30
Inter-segment	-0.263	-0.375	
Net revenue	**10.850**	**14.012**	29
Cost of sales	-7.736	-10.032	
Gross profit	**3.114**	**3.980**	28
Administration	-1.938	-2.361	
Distribution	-0.341	-0.488	
R&D	-0.295	-0.282	
Other income	0.008	0.005	
EBIT	**0.548**	**0.854**	56
Net interest	0.004	0.007	
Associate	0.183	0.320	75
Profit before tax	**0.735**	**1.181**	61
Tax	-0.120	-0.281	
Post-tax profit	0.615	0.900	46
Minorities	-0.130	-0.237	
Net profit	**0.485**	**0.663**	**37**
Dividends	-0.188	-0.245	
Other	0.024	0.013	
Retained profit	0.321	0.431	34
Basic EPS (p)	4.55	6.09	34
DPS (p)	1.25	1.50	20
No. of shares	10.663	10.879	

Source: *Company data; Hardman & Co*

Ratios		
Margins (%)	**H1 2016**	**H1 2017**
Gross	28.7	28.4
EBITDA	7.6	8.3
EBIT	5.1	6.1
PBT	6.8	8.4
Net	5.7	6.4
Retained	3.0	3.1
Tax (% rate)	*-16.3*	*-23.8*
Cover (x)	3.3	3.7
EBITDA (£m):		
EBIT	0.548	0.854
Depreciation	0.197	0.214
Amortisation	0.082	0.098
Total	**0.827**	**1.166**

Source: *Company data; Hardman & Co*

Operations analysis

The UK, with £7.2 million of Revenue, accounted for 51% of the Group total in the first half of fiscal 2017 (H1 2016: 56%) with South Korea at 32% (H1 2016: 31%). Domestic revenue was up 18% (H1 2016: -1%) whilst South Korea jumped 34% (H1 2016: -2%). Elsewhere, the US and 'Other' nations (largely in continental Europe) had excellent years with respective surges in revenue of 53 and 70%. Okay, this was from a low base but, jointly, they now account for 17% of the total (H1 2016: 13%).

The UK contributed just under £1.0 million of segment profits in H1 2017 which was 10% off year-on-year (H1 2016: -7%). At the same time, profitability drifted from 18.5 to 14.0%.

In South Korea, Segment profits were 83% higher at £913,000 (H1 2016: -25%) and this comprises two businesses: Titon Korea, is a 51% owned subsidiary; and an associate company, Browntech Sales Co. Ltd (BTS), which is 49% owned. This means that in the formal profit and loss account, South Korea is included in both the EBIT and the Associate profit lines (where it is the sole contributor); and the Nation also accounts for 100% of the Minorities charge. It is important to note, here too that 'Segment' profit for the UK is pre-unallocated expenses while for South Korea it is 'post'. In combination, subsidiary and associate, South Korea is the largest single contributor to the Group's profit after tax which rose 46% in the half year to £900,000 (H1 2016: £615,000).

Titon Korea manufactures passive ventilation products, and is the national market leader; and it had a very good six months with an almost doubling of PBT. At BTS, its contribution can be tracked through the Associate line which swelled 75% to £320,000 in H1. It distributes ventilation products in South Korea and invests in and develops schemes in the domestic residential real estate market; and it will start work on a greenfield site in a smart neighbourhood of Seoul in the current quarter.

North America added more than 10% to its segment profit to £261,000 in the half year (H1 2016: £238,000) and Titon continues to expand in distribution here; also the profit margin in H1 was nudging 25%. Finally, 'Other' *aka* continental Europe contributed £150,000 to profit with margins in double digits.

Business segment revenue and profit		
Half years to 31 March	**2016**	**2017**
GBP million:		
Revenue		
UK*	6.031	7.137
South Korea	3.365	4.520
Nth America	0.685	1.047
Other	0.769	1.308
Total*	**10.850**	**14.012**
Segment profit		
UK	1.115	0.998
South Korea^	0.499	0.913
Nth America	0.238	0.261
Other	0.000	0.150
Total	**1.852**	**2.322**
% changes in Revenue		
UK	-1	18
South Korea	-2	34
Nth America	na	53
Other	na	70
Total	**1**	**29**
% changes in Profit		
UK	-7	-10
S. Korea^	-25	83
Nth America	na	10
Other	na	na
Total	**-7**	**25**
Margins (%)		
UK	18.5	14.0
S. Korea^	14.8	20.2
Nth America	34.7	24.9
Other	na	11.5
Total	**17.1**	**16.6**
**ex Inter-segment revenue*	*0.601*	*0.750*

Source: Company data; Hardman & Co
Notes:
** inter-segment revenue pertains to UK only*
^South Korea profit includes Group share of profit from Associate BTS

Balance sheet

Net Assets including Minorities (*aka* Non-controlling Interest) rose 23% in the half year to 31 March 2017 from £12.7 to £15.6 million; and this included a rise in Net Cash from £2.46 to £2.71 million i.e. 17% of NAV versus 19% last time.

Annualised RONA or Return on Net Assets increased from 11.6 to 15.1% half-year-on-half-year although if Intangibles (around £600,000 in both periods) and Net Cash are excluded from the denominator, then the movement in RONA was from 15.1 to 19.0%.

ROCE or Return on Capital Employed on an annualised basis was 10.9% (2016: 8.6%) with annualised Capital Turn (Revenue-divided-by-Capital-Employed) at 1.8x (1.7x). We like, the relatively neglected, Capital Turn ratio because it measures how efficiently capital is utilised i.e. there are two ways to make a profit: maximise revenue and constrain costs on the one hand; and use your capital efficiently on the other; and preferably a combination of both. Capital Turn can also be used to focus management and employees on using capital efficiently, avoiding waste etc.

However, as with RONA, if ROCE excludes Intangibles and Cash, the 2017 first half return is 13.8% (2016: 11.3%); the same goes for an adjusted Capital Turn at a first class 2.3x (2016: 2.2x) on the same basis.

Turning to liquidity, we highlight the Current and Quick Ratios which are calculated by dividing current assets by current liabilities (‘Current’) and current-assets-less-stocks divided by current liabilities (‘quick’; and where above 1.0 is good). The former was 2.96 in 2016 (2016: 2.85), while at the same time, the Quick Ratio was 1.94 against 1.91. All are truly excellent.

Capital Employed

Half years to 31 March	2016	2017
GBP million:		
Ordinary shares	1.085	1.095
Share premium account	0.939	0.975
Revaluation Reserve etc.	0.056	0.056
Profit & loss account	9.440	10.910
Other	-0.053	0.578
Shareholders funds	11.467	13.614
Minorities	1.223	2.000
Provisions for liabilities	0.000	0.000
Preference Shares	0.000	0.000
Other loans/leases	0.000	0.000
Bank loans & ODs	0.000	0.000
CAPITAL EMPLOYED	**12.690**	**15.614**
Fixed assets	3.443	3.576
Investments	0.979	1.824
Stocks/WIP	3.884	4.976
Corporation tax	-0.112	-0.176
Trade debtors	5.426	6.772
Other debtors	0.000	0.000
Deferred tax	0.064	0.114
Trade creditors	-4.015	-4.706
Other creditors	0.000	0.000
Intangibles/Other	0.563	0.529
Cash	2.458	2.705
CAPITAL EMPLOYED	**12.690**	**15.614**
METRICS:		
ROCE annualised (%)	8.6	10.9
ROCE annualised (%)*	11.3	13.8
Capital turn annualised (x)	1.7	1.8
Capital turn annualised (x)*	2.2	2.3
RONA annualised (%)	11.6	15.1
RONA annualised (%)*	15.1	19.0
Current ratio	2.85	2.96
Quick ratio	1.91	1.94
Stocks as % of revenue	36	36
Creditors as % of revenue	-37	-34
(Net debt)/cash (£,000)	2.458	2.708
Net assets (£,000)	12.690	15.614
Gearing % (-ve)/+ve	19	17

Source: Company data; Hardman & Co
*Notes: *adjusted for Intangibles and Net Cash*

Cash flow

In terms of cash flow, there was a £267,000 cash inflow in the half year ending 30 March 2017 versus the previous year-end (2016: outflow of £412,000). This was primarily by higher profits and working capital; and despite higher tax/dividends.

Cash Flow

Half years to 31 March GBP million:	2016	2017
Profit before tax	0.735	1.181
Interest etc.	0.000	0.000
Depreciation	0.279	0.312
Provisions	0.000	0.000
Asset sales	-0.005	-0.007
Share issued/sold	0.094	0.042
Other	-0.183	-0.320
SOURCES	**0.920**	**1.208**
Capex	0.422	0.279
Disposals	-0.005	-0.007
Acquisitions	0.000	0.000
Stocks	0.044	0.330
Debtors	0.354	-0.024
Creditors	0.174	-0.129
Tax	0.133	0.247
Dividends	0.188	0.245
Other	0.022	0.000
USES	**1.332**	**0.941**
Surplus/(deficit)	-0.412	0.267
Adjustment	0.000	0.000
Movement (debt)/cash	**-0.412**	**0.267**
Reconciliation & Analysis of Balance Sheet Debt:	**Half Year 2015-16**	**Half Year 2016-17**
(Net debt)/cash	2.458	2.705
Net assets	12.690	15.614
Gearing % (-ve)/+ve	19	17
Consecutive six-months on six-months change	*-0.412*	*0.267*

Source: Company data; Hardman & Co

Chairman's statement

Financial performance

"I am very pleased to report a record half year for Titon, with a 61% increase in Profit before Tax and top line growth of 41%. Earnings per share also rose significantly (+34%) and the Interim Dividend is to be raised 20%. This performance would have been even better, too, without the costs associated with the Group's exit from commercial ducting fabrication in the UK referred to under Operations below.

Income Statement

In six months ended 31 March 2017, Titon's net revenue (which excludes inter-segment activity) rose 29.1% to £14.01 million. On a constant currency basis, however, the increase was 20.4%.

The Gross Margin was sustained at 28.4% (2016: a restated 28.7% due to a re-classification of Research and Development expenses). EBITDA was £1.17 million (2016: £0.83 million) while Operating Profit or EBIT (Earnings before interest and tax) rose 56% to £0.85 million with operating margins at 6.1% (2016: 5.1%).

Net interest contributed £7,000 (2016: £4,000) while the share of profits from the Group's associate soared 75% to £320,000 (2016: £183,000) resulting in Profit before Tax of £1.18 million which was an increase of 61% year-on-year (2016: £0.74 million). The weakness of the British Pound added £143,000 to Profit before Tax, which means that on a constant currency basis, it would have been £1.04 million and 41% higher year-on-year.

Earnings per share for the half year increased 34% to 6.09 pence (2016: 4.55 pence). Taxation was sharply higher at 23.8% (2016: 16.8%) due to the higher proportion of profits made outside the UK in the period while the Non-controlling Interest's share of group profits almost doubled from £130,000 to £237,000.

An Interim Dividend in respect of the six months ended 31 March 2017 of 1.50 pence per share was approved by the Directors of Titon Holdings Plc on 10 May 2017. The Interim Dividend will be payable on 24 June 2017 to shareholders on the Register at 3 June 2017. The ex-dividend date is 2 June 2017.

Balance sheet and cash flow

Total Equity rose £2.92 million to £15.61 million with net cash at £2.71 million (31 March 2016: £2.46 million) which is equivalent to 17.3% of net assets (31 March 2016: 19.4%). There was a net cash inflow in the half year of £247,000 (2016: inflow of £45,000) which was driven primarily by cash generated from operations. Total capital expenditure in the half year was £279,000 (2016: £422,000).

Net current assets were £9.57 million (2016: £7.64 million).

Operations

In the UK, the performance of our window and door hardware business has improved, with the value of sales from the Timber, PVCu and Aluminium divisions exceeding last year by 14% and also making good contributions to profits. Similarly, we have seen encouraging sales of the new hardware products which have been developed in the last few years and this should continue in the second half.

Sales in the Ventilation Systems division have continued to grow with UK revenue up 13% year on year with Export Sales more than doubling. We continue to achieve good sales of our MVHR products (Mechanical Ventilation with Heat Recovery) and the Group's increasingly wide range of such products affords a significant competitive advantage in the market place.

As already noted, sales of our core products in the UK were good in the half year. However, their profit contribution has been eroded by a decision to withdraw from a new venture which commenced some 12 months ago. Its focus was the fabrication, in partnership, of a new commercial ducting product. However, it was not embraced by the market at the prices that we had expected and would only have done so, we believe, with a greater focus on specification selling and significant investment by Titon. Both strategies would have been expensive and would have had no guarantee of success. As a result, and in conjunction with our partners, it was decided to cease our activities in this market. In turn, we have had to make provisions for stock, fixed assets and debts which we may not recover in the future totalling £234,000. This combined with the initial losses of the project means that Titon Hardware made a small loss in the first half.

The performance by our South Korean businesses, however, has been very positive in the period and Profit before Tax for Titon Korea (51% owned) nearly doubled. This reflects increased penetration, by the Company, of the domestic market in natural ventilation products and credit goes to our team on the ground. Our second South Korean business is the Associate company, Browntech Sales or BTS (49% owned) which distributes ventilation products in South Korea and invests in and develops schemes in the domestic residential real estate market. BTS recently purchased a greenfield site in an exclusive area of Seoul and expects to start work in the June quarter. We remain cognisant, of course, of both the geopolitical tensions on the Korean Peninsula at large and South Korea's complex domestic politics. Be that as it may, in Q1 of 2017, South Korea's GDP expanded at its fastest quarterly rate (0.9%) since Q2 2016. It was also 2.7% up on a year ago.

In the US, we have seen another good contribution to the Group's Profit before Tax. The US market for natural ventilation is small and the Group has developed a good domestic reputation and trades profitably. Titon also continues to develop new products specifically for the American market and new opportunities continue to emerge.

Investors

As The Group's initiative with Hardman & Co., the corporate research house, is more than a year old now and continues very satisfactorily for shareholders. Note, too, that its reports can be accessed via the London Stock Exchange Regulatory News Service or RNS (http://www.investegate.co.uk). In addition, I was interviewed by Lord John Lee, who is also a shareholder, for his programme on Share Radio. This is the first UK national radio station dedicated to business, finance and money. Later this month, too, I am due to present Titon to a group of investors at an event organised by the UK Shareholders' Association, which is the oldest shareholder campaigning organisation in the UK. Indeed, we welcome all contact with shareholders or potential shareholders.

Outlook

In the UK, both the Brexit negotiations and the imminent General Election create degrees of uncertainty. Nonetheless, we expect our core UK businesses to continue to grow in the second half. Another strong performance is also expected from South Korea and, while the US is a smaller region for Titon right now, it is doing well and we intend to commit further resources here. The same goes for the Group's exports to continental Europe.

This geographical diversity is a strength and, particularly, when it is combined with great products, great people and a strong balance sheet. I am confident that we have will have a good result for the year".

Keith Ritchie, Chairman

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Hardman & Co Research Limited (trading as Hardman & Co)
35 New Broad Street
London
EC2M 1NH
T +44 (0) 207 194 7622

Follow us on Twitter @HardmanandCo

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Hardman Team

Management Team			
+44 (0)20 7194 7622			
John Holmes	jh@hardmanandco.com	+44 (0)207 194 7629	Chairman
Keith Hiscock	kh@hardmanandco.com	+44 (0)207 194 7630	CEO

Marketing / Investor Engagement		
+44 (0)20 7194 7622		
Richard Angus	ra@hardmanandco.com	+44 (0)207 194 7635
Max Davey	md@hardmanandco.com	+44 (0)207 194 7622
Antony Gifford	ag@hardmanandco.com	+44 (0)207 194 7622
Vilma Pabilionyte	vp@hardmanandco.com	+44 (0)207 194 7637
Gavin Laidlaw	gl@hardmanandco.com	+44 (0)207 194 7627
Ann Hall	ah@hardmanandco.com	+44 (0)207 194 7622

Analysts

+44 (0)20 7194 7622

Agriculture		**Bonds**	
Doug Hawkins	dh@hardmanandco.com	Brian Moretta	bm@hardmanandco.com
Yingheng Chen	yc@hardmanandco.com	Mark Thomas	mt@hardmanandco.com
Thomas Wigglesworth	tcw@hardmanandco.com	Chris Magennis	cm@hardmanandco.com
Building & Construction		**Consumer & Leisure**	
Tony Williams	tw@hardmanandco.com	Mike Foster	mf@hardmanandco.com
Mike Foster	mf@hardmanandco.com	Steve Clapham	sc@hardmanandco.com
		Jason Streets	js@hardmanandco.com
Financials		**Life Sciences**	
Brian Moretta	bm@hardmanandco.com	Martin Hall	mh@hardmanandco.com
Mark Thomas	mt@hardmanandco.com	Gregoire Pave	gp@hardmanandco.com
		Dorothea Hill	dmh@hardmanandco.com
Media		**Mining**	
Derek Terrington	dt@hardmanandco.com	Paul Singer	if@hardmanandco.com
Oil & Gas		**Property**	
Angus McPhail	am@hardmanandco.com	Mike Foster	mf@hardmanandco.com
Services		**Special Situations**	
Mike Foster	mf@hardmanandco.com	Steve Clapham	sc@hardmanandco.com
		Paul Singer	ps@hardmanandco.com
Tax Enhanced Services		**Utilities**	
Brian Moretta	bm@hardmanandco.com	Nigel Hawkins	nh@hardmanandco.com
Chris Magennis	cm@hardmanandco.com		

Hardman & Co

35 New Broad Street
London
EC2M 1NH

Tel: +44(0)20 7194 7622

www.hardmanandco.com