Lewis Charles Securities

9 April 2009

Property Management, Construction & Services (Isle of Man)

Rating NEUTRAL

Price 10.5p

Speymill plc (SYG.L)

FY'08 Prelims Mixed – On the Road to Recovery

Market Cap (£m)	**6.1**
Enterprise Value	**7.1**
'09 P/E	**8.1**
'10 P/E	**4.9**
'09 EV/Sales	**0.1**
'10 EV/Sales	**0.1**
'09 EV/Ebitda	**3.7**
'10 EV Ebitda	**2.2**

Company Website
www.speymill.com

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- **Speymill's preliminary 2008 results showed an impressive and improving performance from both Property and Investment Fund Management, however they were overshadowed by poor profitability from the UK Contracts business that produced a much larger loss than we originally expected due to several customers going into administration and further margin deterioration. . The Group loss before tax was £6.26m versus a £2.26 profit in the prior year. The UK Contracts division contributed an £11.0m loss to the group results.**

- **The Company's shares were readmitted to trading on the AIM market with the announcement of the results and, although on low volume, actually closed slightly up on the day begging the question whether the bad news is not already in the price.**

- **While we believe the Contracts division is not completely insulated from the risk of further downward surprises, it is likely that the majority of bad news is behind them. The company has a few major projects still the process of construction but believe these likely have lower risk than those that caused the downfall. We believe the company has taken appropriate steps by adding management expertise to help bring Contracts back to health.**

- **While the shares were suspended, management carried out an exercise in order to model the company's working capital adequacy under a number of adverse scenarios that included currency fluctuations, further contract weakness, and asset value declines. It also commissioned an independent study of this work by a firm of auditors. Based on these analyses the company concluded that it had adequate working capital even when factors were stressed in combination.**

- **As the group manages the Contracts division back to positive gross margins, which we believe can be done this year, the other divisions have now become larger and contribute significantly to the bottom line.**

- **We now expect pre-tax profit for this year be somewhere in a range of £1-1.5m and have rolled out our 2010 estimates. We have taken a conservative approach to estimates and believe the shares can rise significantly if the company can execute on their plan to properly manage down risk in the Contracts Division. We believe the Property and Fund Management businesses have significant value in them that can be unlocked once the overhang of potential further unexpected project losses is eroded.**

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Disclosures

Company	Code	Disclosure
Speymill	SYG	2, 6
Speymill Deutsche Immobilien Company (ORD)	SDIC	None
Speymill Deutsche Immobilien Company I	SDCC	None
Speymill Macau Property Company	MCAU	None

1. Within the past twelve months Lewis Charles has managed or co-managed a public offering for this company, for which it receives fees or the promise of fees
2. Lewis Charles acts as corporate broker to this company
3. Lewis Charles regularly hold trading positions (which may include options) in this company
4. Lewis Charles holds more than 5% of the securities of this company
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8. The author and/or an individual responsible for production of this report received or purchased shares in the issuer prior to a public offering of shares

Research Ratings

Buy – The Company is profitable, cash generative, with established operations, a credible management team and proven execution of strategy. Absolute share price return expected to increase by more than 10% over the next twelve months.
Speculative Buy – The Company has operations that are either early stage or loss-making, and/or there is uncertainty over the management's ability to deliver on its strategy. The valuation appears to reflect risks but could reward shareholders if the operations are successful. Absolute share price return expected to increase by more than 10% over the next twelve months contingent upon success of certain operations.
Neutral – Shareholders should await key developments from the company, which may have a positive or negative impact on the company's prospects. Absolute share price return expected to change by between -10% and 10% over the next twelve months.
Sell – the Company's share price and/or valuation does not reflect current underlying prospects for the company. The company may require additional funding above what can be reasonably expected to raise or the company has failed to deliver on key operations that now risk the future success of the company. Absolute share price return expected to decrease by more than 10% over the next twelve months.
Not Rated - Lewis Charles has either not initiated research on this company or is restricted from publishing a recommendation.

Balance of Ratings

Buy 67%
Neutral 33%
Sell none

Analyst Certification

I, Peter McNally, internal analyst employed by Lewis Charles hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company and its securities. I also certify that I have not been and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendations in this report.

Results Overview

Group – 2008 Group Turnover was £66.0m beating our £65.2 estimate. However, the gross margin was 20.6% versus 24.2% in the prior year, and our original 28.6% estimate. The Group loss before tax was £6.26m versus a £2.26 profit in the prior year and our £1.6m estimate. The loss included a £944k charge for goodwill impairment due to the contracts division and £422k of share-based payments, mostly from the Property and Fund Management divisions. Loss per share was 12.48p versus our 2p of earnings estimate.

Contracts – Contracts turnover was £43.2m, up +4.5% y/y, and just shy of our £44.2 estimate for a loss before tax of £11m. Profitability in the contracts division suffered from multiple customers going into administration creating a larger than expected loss for the group.

Fund Management – saw its best year yet with turnover up 54.7% to £9.9m beating our £9.8m estimate. The division benefited from its first full year of both funds being fully invested and a £1.6m performance fee from the Macau Fund. Profit before tax was £4.57m resulting in a highly impressive 46% margin.

Property Management – also had a record year for the group with both organic growth and full inclusion into Speymill Group's results post the acquisition of the outstanding 49% minority during the year. Turnover was £12.8m versus our £11.2m estimate and £4.9m last year. Headcount in the division was up to roughly 300 people versus 200 at the end of 2007. Profit before tax for the division was £741k or a 6% margin.

The Future of the UK Contracts Division

We believe the Contracts division suffered from trying to grow its business in a rapidly expanding refurbishment and property market. This resulted in a "land grab" for new business with an assumption of less risk. As the market deteriorated and prices began to fall, many developers found themselves in a negative equity position or experienced liquidity problems forcing them into administration, or with the need to abandon unfinished projects. Furthermore, the downward trajectory in prices led to a fall in final margins on many projects.

Going forward, the company is taking a more prudent approach to new business which should result in a much lower level of risk. **We think the majority of existing problems have been understood and addressed by the company.** Obviously, there are existing projects that were started last year, however the company seems to have de-risked the business as much as possible, and changed the focus from growth to profitability.

Headcount in the division has been cut by roughly one-third, and our estimates now assume a -44% yearly sequential drop in revenue. In addition there has been an increase in emphasis on project execution. John Chambers has taken on the role of Joint Managing Director and his appointment is designed to assure quality and to manage risk in the division. John is a chartered quantity surveyor with 25 years of industry experience which should contribute to an improvement in margins over the longer term. We believe a focus on risk management can bring the division back to positive gross margins by the end of the year, and positive net margins in 2010. In future, the company will now require a performance bond in certain cases for new business to insure against the risk of shocks.

Short-Term Financing

Two directors of the company have provided a short term financing facility of £3.3 for up to 18 months due to a year end net liability of £2.7m. The loan pays 12% with a 3% facility fee, and can be converted into convertible preference shares at the option of the company, as part of a public offering. Although, this is not the best position in the company to be in, we are encouraged by the participation of the two company directors to provide their own capital to further fund the business. The company also renewed a £2m overdraft with Lloyds on the same terms as in the past through the end of February 2010. In our opinion, this financing should be sufficient to help bring the company into a better position as the Contracts business is managed back to health in conjunction with the increasing contributions of the Property and Fund Management divisions.

New Estimates and Rating Philosophy

We have lowered our PTP estimate for this year to a range of £1-1.5m this year, down from £3.96, and have rolled out our 2010 estimates that only assume a slight increase over 2009, despite market forecasts of a recovery. We have chosen a range as we believe the outcome is potentially volatile given the high revenue and low profit number. While the Property and Fund Management divisions are performing better than we expected, the driver to the share price recovery in our model hinges on the Contracts division.

We have taken a conservative approach to estimates and believe the shares can rise significantly if the company can execute on their plan to properly manage down risk. We believe the Property and Fund Management businesses have significant value in them that can be unlocked once the overhang of potential further unexpected project losses is eroded.

Once we can see evidence of the company managing new projects according to their new intentions within the contracts division, and can see management execution and completion of existing ongoing business, we will look to change our rating on the shares and revise estimates.

Profit & Loss

Year to 31 December (£000s)	**2007A**	**2008A**	**2009E**	**2010E**
Construction and refurbishment	41,372	43,210	24,019	25,220
Investment fund management	6,436	9,913	8,065	8,864
Property management	4,891	12,842	16,695	17,529
Group Revenue	**52,699**	**65,965**	**48,778**	**51,613**
Gross Profit	**12,761**	**13,574**	**22,739**	**24,650**
Gross margin	*24.2%*	*20.6%*	*46.6%*	*47.8%*
EBITDA	**3,216**	**(4,468)**	**1,913**	**3,189**
EBITDA margin	*6.1%*	*-6.8%*	*3.9%*	*6.2%*
Depreciation	(124)	(312)	(403)	(423)
Impairment of Goodwill	0	*(944)*	0	0
Excpt'ls & Share-based payments	(794)	(422)	(310)	(310)
Operating Profit	**2,298**	**(6,146)**	**1,200**	**2,456**
Operating Profit (Adjusted)	**3,092**	**(4,780)**	**1,510**	**2,766**
Adj. Operating margin	*5.9%*	*-7.2%*	*3.1%*	*5.4%*
Gain on Disposals	0	0	0	0
Net Interest	(39)	(113)	(148)	(643)
Profit Before Tax	**2,259**	**(6,259)**	**1,052**	**1,813**
Profit Before Tax (Pre FRS20)	**3,053**	**(5,837)**	**1,362**	**2,123**
Profit Before Tax (Adjusted)	**3,053**	**(4,893)**	**1,362**	**2,123**
Tax	(168)	(997)	(612)	(888)
Minorities	0	0	0	0
Net Income to Shareholders	**2,091**	**(7,256)**	**440**	**925**
Average Shares - Weighted (m)	57.5	58.1	58.1	58.1
Average Shares - Diluted (m)	63.8	58.1	58.1	58.1
EPS - Basic (p)	3.63	(12.48)	0.76	1.59
EPS - Adjusted (p)	**5.01**	**(10.13)**	**1.29**	**2.12**
EPS - Adjusted & Diluted (p)	4.52	(10.13)	1.29	2.12
DPS (p)	0.50	0.00	0.00	0.32

Source: Lewis Charles Estimates

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