

20th June 2018

“Strong” start to the year

‘Running winners’ is simple in theory, but difficult in practice. Sure, there is nothing wrong with banking a few profits after a parabolic move, especially when a stock becomes disproportionately large within one’s portfolio. Yet for Elektron, based purely on the fundamentals, we believe this would be a mistake despite the stock’s >5-fold rise since the 2017 lows.

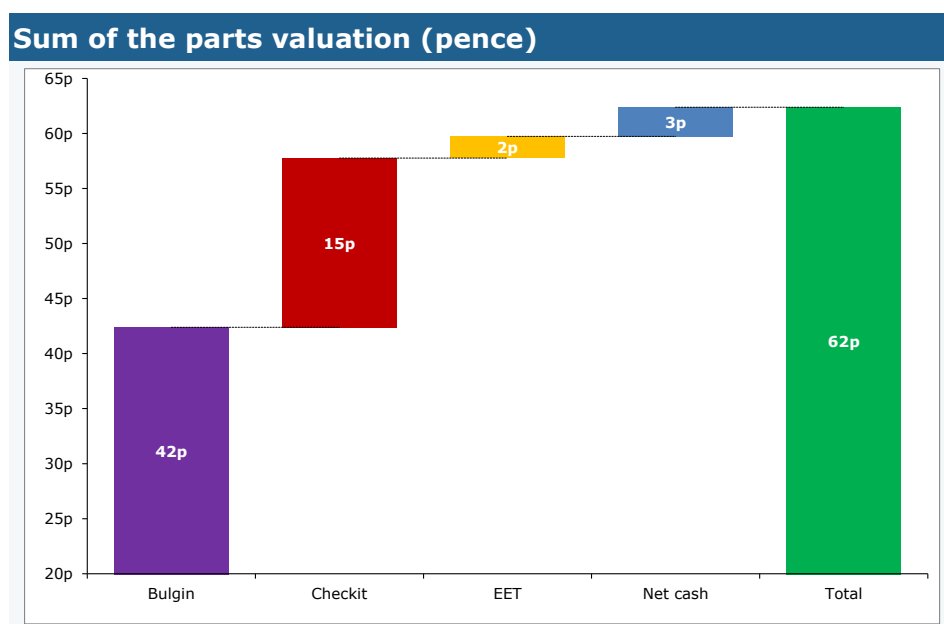
Indeed, this morning the company said that **Bulgin was continuing to experience buoyant demand**, with YTD performance ahead of plan. Supported by a ‘**record orderbook**’, driving H1 expected sales up at least 8% LFL to £13.5m (LY £12.5m).

Upgrading estimates & SOTP valuation to 62p/share

Accordingly, we have increased our FY19 turnover and EBIT forecasts for the division to £27.5m (vs £27.3 LY) and £6.9m (£7.2m) respectively. Elsewhere, **EET is making good progress too**, and tracking full year estimates. While **Checkit is in “advanced discussions”** with several global businesses to adopt its disruptive technology.

From a macro risk perspective, we understand Elektron has minimal exposure to the recently proposed ‘US-EU/Chinese’ trade tariffs, even though c.64% of revenues are generated outside the UK. Instead there may actually be a small positive forex benefit given \$ appreciation vs the £ (6%) and Tunisian Dinar (10%) over the past 2 months.

So what does this all mean? Well in terms of the group, **our FY19 EBIT climbs from £2.0m to £2.3m** – which in turn pushes the **sum-of-the-parts (SOTP) valuation 2p higher to 62p/share**:

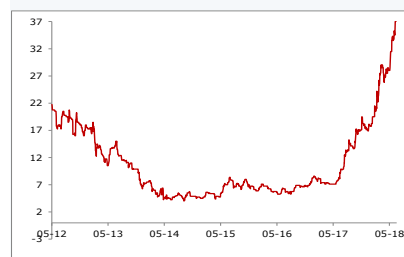


Source: Equity Development

Company Data

EPIC	AIM: EKT
Price (last close)	41p
52 week Hi/Lo	41p/9.5p
Market cap	£76m
ED SOTP valuation	62p/share
Avg. daily volume	250k

Share Price, p



Source: Web Financial

Description

Elektron (EKT) is a specialist niche product OEM and B2B operational service provider, enjoying a wide economic moat. It runs 3 separate divisions (see below), each targeting distinct markets, yet bound together by a single centre of engineering excellence located in Cambridge.

- 1) Bulgin designs and manufactures premium, fail-safe, hermetically sealed (ie air/water tight) circular connectors and electronic components.
- 2) Checkit is a hi-growth (>100%+ LFL) real-time operational management platform, that digitises, streamlines, and vastly improves the management of routine activities, providing top to bottom visibility.
- 3) EET – develops field vision and macular pigment screening devices to the ophthalmic industry.

Next News: Pre-close update in Aug’18

Paul Hill (Analyst)

0207 065 2690

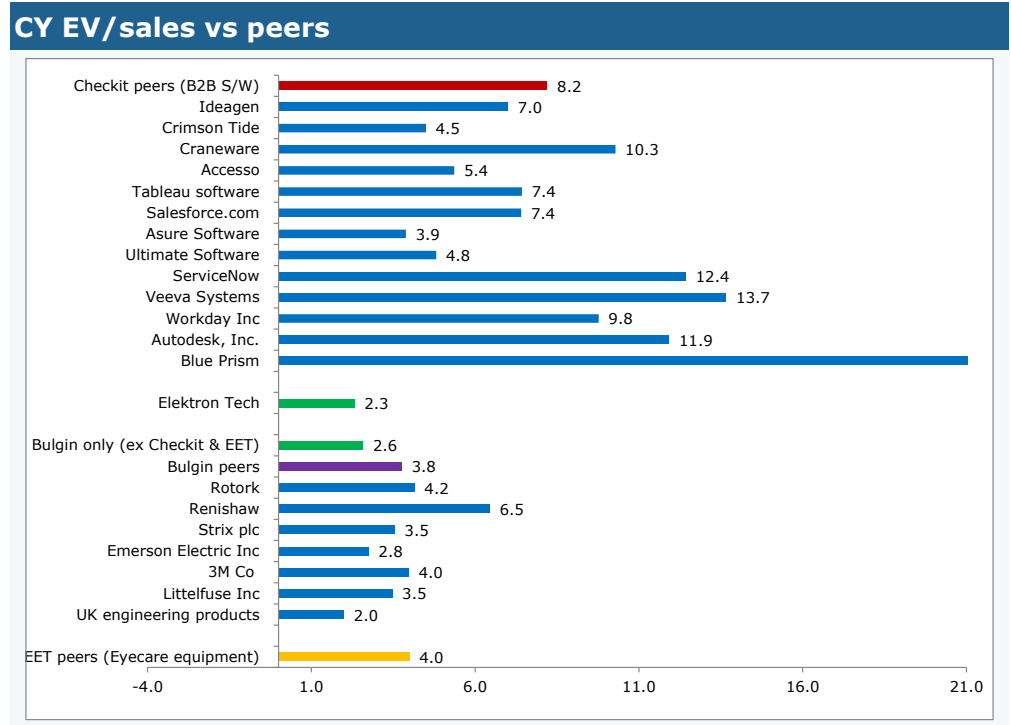
paul.hill@equitydevelopment.co.uk

Hannah Crowe

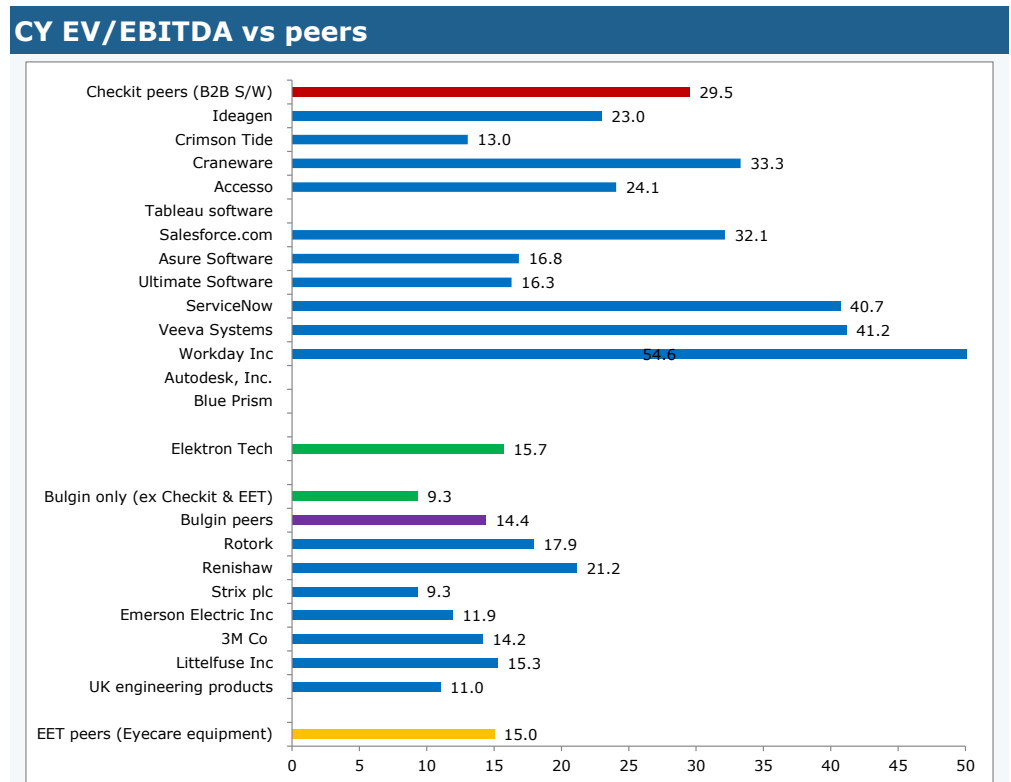
0207 065 2692

hannah@equitydevelopment.co.uk

In fact, to us at 41p **the stock still looks cheap compared to peers** – trading at a discount on most benchmarks (see below). Plus with the possibility of new client/contract wins, and the US rollout of Checkit in Q4'18 to boot, then we suspect there is scope for further upgrades as the year progresses.

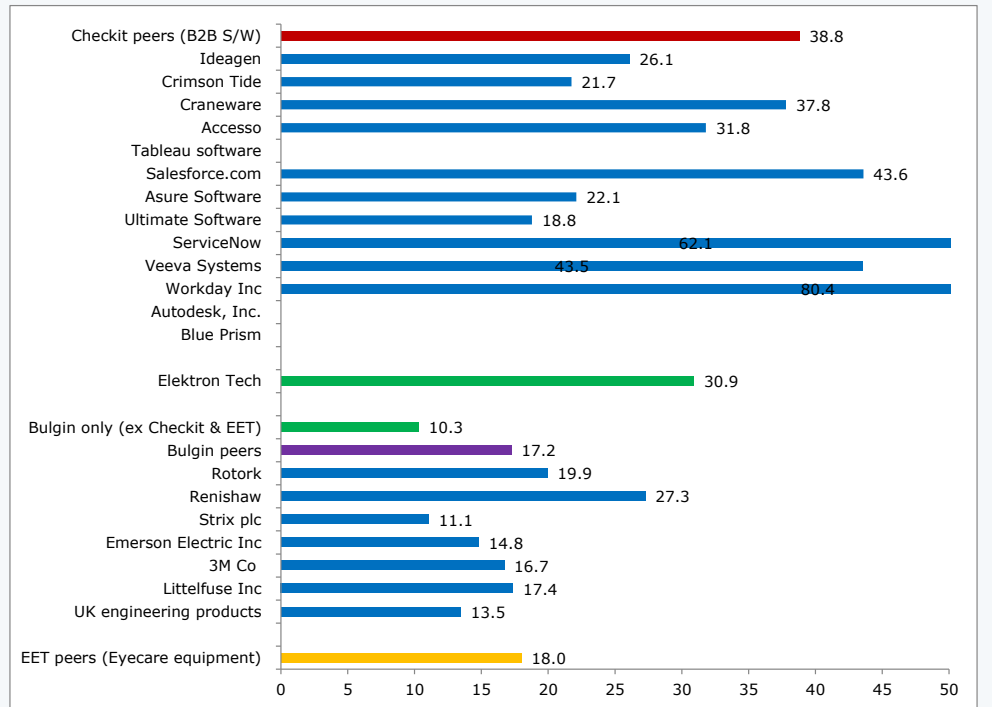


Source: Equity Development, corporate sites – closing prices as at 19th June 2018



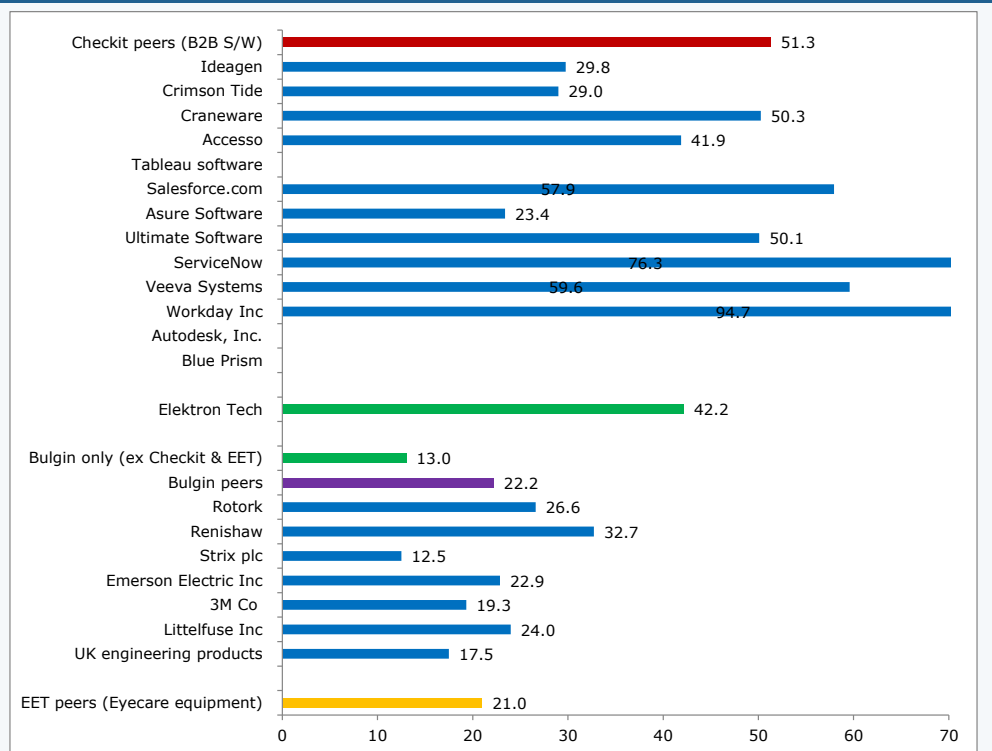
Source: Equity Development, corporate sites – closing prices as at 19th June 2018

CY EV/EBIT vs peers



Source: Equity Development – closing prices as at 19th June 2018

CY PERs vs peers



Source: Equity Development, corporate sites – closing prices as at 19th June 2018

Summary financial projections

Elektron Technology (January yearend)	2017 Act £ms	2018 Act £ms	2019 Est £ms	2020 Est £ms	2021 Est £ms	2022 Est £ms	2023 Est £ms	2024 Est £ms	2025 Est £ms
Bulgin	24.1	27.3	27.5	28.6	30.0	31.5	33.1	34.8	36.5
Checkit	0.3	0.5	1.1	2.2	4.4	7.9	12.7	19.7	29.5
EET	2.4	2.0	2.1	2.5	2.9	3.3	3.8	4.4	5.1
Turnover	26.8	29.8	30.7	33.3	37.3	42.8	49.6	58.9	71.1
<i>Bulgin</i>		13.3%	0.8%	4.0%	5.0%	5.0%	5.0%	5.0%	5.0%
<i>Checkit</i>		66.7%	110.0%	110.0%	100.0%	80.0%	60.0%	55.0%	50.0%
<i>EET</i>		-16.7%	5.0%	20.0%	15.0%	15.0%	15.0%	15.0%	15.0%
<i>% growth</i>		11.2%	2.9%	8.7%	12.0%	14.6%	16.0%	18.6%	20.8%
Gross Profit	11.2	14.8	15.5	17.0	19.4	22.5	26.5	31.8	39.0
<i>% margin</i>	41.8%	49.7%	50.7%	51.1%	51.8%	52.6%	53.3%	54.1%	54.8%
Bulgin	4.3	7.9	7.6	8.2	8.6	9.0	9.5	10.0	10.4
Checkit	-2.8	-2.7	-3.0	-2.0	-0.5	2.8	4.5	7.1	10.6
EET	-0.2	-0.1	-0.1	0.1	0.2	0.3	0.4	0.6	0.8
Adj. EBITDA	1.3	5.1	4.5	6.2	8.2	12.1	14.4	17.7	21.9
<i>Bulgin</i>	17.8%	28.9%	27.7%	28.6%	28.6%	28.6%	28.6%	28.6%	28.6%
<i>Checkit</i>	-933.3%	-540.0%	-288.1%	-92.9%	-12.4%	34.7%	35.3%	36.0%	36.0%
<i>EET</i>	-8.3%	-5.0%	-3.3%	2.2%	5.8%	9.0%	11.7%	14.1%	16.2%
% EBITDA margin	4.9%	17.1%	14.8%	18.6%	22.0%	28.2%	29.0%	30.0%	30.8%
Bulgin	3.3	7.2	6.9	7.4	7.8	8.2	8.6	9.0	9.5
Checkit	-3.5	-4.4	-4.4	-3.8	-2.7	0.3	1.7	4.1	7.1
EET	-0.4	-0.2	-0.2	-0.1	0.0	0.1	0.3	0.4	0.6
Adj. EBIT	-0.6	2.6	2.3	3.5	5.1	8.6	10.6	13.6	17.1
<i>Bulgin</i>	13.7%	26.4%	25.1%	26.0%	26.0%	26.0%	26.0%	26.0%	26.0%
<i>Checkit</i>	-1166.7%	-880.0%	-421.4%	-174.5%	-62.2%	3.2%	13.2%	21.0%	24.0%
<i>EET</i>	-16.7%	-10.0%	-8.3%	-2.8%	0.8%	4.0%	6.7%	9.1%	11.2%
% EBIT margin	-2.2%	8.7%	7.5%	10.6%	13.6%	20.1%	21.3%	23.1%	24.1%
Adj. Profit before Tax	-0.6	2.7	2.3	3.5	5.1	8.6	10.6	13.6	17.1
Adjusted EPS (p)	-0.1	1.1	1.0	1.5	2.1	3.6	4.4	5.6	7.0
<i>EPS growth rate</i>		-1939.1%	-9.0%	52.2%	43.9%	67.9%	22.3%	28.0%	25.7%
Dividend (p)	0.0	0.0	0.0	0.0	0.0	1.2	1.5	1.9	2.3
<i>Yield</i>	0.0%	0.0%	0.0%	0.0%	0.0%	2.9%	3.6%	4.5%	5.7%
Valuation benchmarks									
<i>P/E ratio</i>	-706.0	38.4	42.2	27.7	19.3	11.5	9.4	7.3	5.8
<i>EV/Sales</i>	2.7	2.4	2.3	2.1	1.9	1.7	1.4	1.2	1.0
<i>EV/EBITDA</i>	54.7	13.9	15.7	11.5	8.6	5.9	4.9	4.0	3.2
<i>EV / EBITA</i>	-118.5	27.3	30.9	20.2	14.0	8.3	6.7	5.2	4.1
<i>Adjusted tax rate</i>	-83.3%	-29.6%	-21.0%	-21.0%	-21.0%	-21.0%	-21.0%	-21.0%	-21.0%
<i>EBITDA drop through rates</i>		126.7%	-67.2%	62.4%	50.5%	70.6%	34.1%	35.2%	34.6%
<i>PEG ratio</i>		-0.02	-4.69	0.53	0.44	0.17	0.42	0.26	0.23
Net cash/(debt)	2.5	5.2	8.0	10.9	15.4	20.3	26.0	32.8	41.1
Sharecount (Ks)	172.2	177.9	187.0	188.0	188.9	189.9	190.8	191.8	192.7
Shareprice (p)	41.0								

Source: Equity Development estimates, Company historic data

Key risks

- Slowdown in global GDP which could impact EKT's end-markets. In particular, Bulgin is early-cycle with revenues amplified by distributor de/restocking.
- Forward visibility at EET and Bulgin tends to be only 8 and 12 weeks' respectively.
- Anticipated growth/profitability (eg Checkit/EET) may take longer than envisaged, cost more and/or not be fully realised.
- Foreign exchange. However this is primarily a translation risk with 64% of Elektron's FY18 turnover being generated outside the UK.
- Regulatory and tax changes.
- Competition may intensify as a function of new/existing players.
- Being relatively small, Elektron could get squeezed by larger rivals, partners and customers, particularly with regards to margins.
- Generic risks of retention/recruitment of key staff, etc.
- As with many smallcap AIM stocks, daily trading volumes can occasionally decline, particularly during seasonally quieter periods and/or between newsflow.



Head of Corporate

Gilbert Ellacombe

Direct: 0207 065 2698

Tel: 0207 065 2690

gilbert@equitydevelopment.co.uk

Investor Access

Hannah Crowe

Direct: 0207 065 2692

Tel: 0207 065 2690

hannah@equitydevelopment.co.uk

Felix Grant-Rennick

Direct: 0207 065 2693

Tel: 0207 065 2690

felix@equitydevelopment.co.uk

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Equity Development, 15 Eldon Street, London, EC2M 7LD. Contact: info@equitydevelopment.co.uk 0207 065 2690