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Specialist Energy Group – recent corporate manoeuvres creates value anomaly?

Ewan Lloyd-Baker, Chief Executive Officer of newly formed Specialist Energy Group (AIM:SEGR) has already learnt a harsh lesson on the realities of being a listed company on London's Alternative Investment Market (AIM).

Specialist Energy Group was formed through the reverse takeover of Southbank UK Plc, a Channel Island Stock Exchange (CISX) listed company by AIM listed Nviro Cleantech, an environmental technology company. Since completing the reverse takeover and relisting on AIM in January, shares in Specialist Energy Group have fallen sharply - predominately on low volume – as shareholders mainly from Nviro Cleantech head for the door. There is little a company can do about this, but it is a cold reality that when one company acquires another, it also acquires new shareholders, increasing the risk of creating an overhang in the market.

Meeting with Lloyd-Baker - who owns a fraction under 10% of the equity - at the company's offices in London last week, there is clearly disbelief about the recent performance of the shares, despite the company reporting that 100% owned subsidiary, Hayward Tyler, is continuing to perform in line with management expectations.

Hayward Tyler, unlike Specialist Energy Group, has been around for a very long time indeed. Acquired in 2006 from private equity group 3i (LSE:III) for £17.2 million, Hayward Tyler is one of the oldest engineering companies in the United Kingdom. It manufactures and services mission critical pumps and motors which go into power stations and has a worldwide market share of around 60%. Around 40% of the company's revenues are generated from selling pumps to new power station developments, with the remaining 60% emanating from servicing current installations around the world. More recently, the company has also expanded into submersible motors for use in deep and ultra-deep oil and gas fields, which could be an additional driver of growth in the future.

This certainly gives the company 'defensive' qualities as its revenues from manufacturing are geared towards power developments across the globe – which are only going one way – and it also benefits from recurring revenues from services contracts. What the company has unfortunately not been able to control as well is currency fluctuations, as it generates a significant slice of its revenues outside the United Kingdom, and higher raw material costs, notably steel in 2008, as its products require high performance materials.

This is reflected in financial results from Hayward Tyler in recent years. In 2007, the company reported revenues of £25.7 million and a net loss of £0.4 million on gross margins of 22%. The following year revenues rose strongly to £32.3 million, but net losses widened substantially to £4.7 million as margins were hammered, falling to 15%.

2009 revenues, reported this morning, were considerably better, with revenues climbing again, to £36.8 million and gross margins rebounding to 29%, allowing the company to post a net profit of £1.6 million. House broker Fairfax is forecasting good revenue growth for 2010, to £40.6 million and gross margins of 31% which will lift net profits to £1.9 million (EPS 7.4 pence).

Price: 43.00p

Market Cap: £10.51m

1 Year Share Price Graph



Share Information

Code:	SEGR	
Listing:	AIM	
52 week	High	Low
	91.25	33.50
Sector:	Manufacturing	
Website:	http://segrouplc.com	

Company Synopsis:

Specialist Energy Group plc (SEG plc), a niche engineering and manufacturing group, was formed through the reverse of Southbank UK plc and Nviro Cleantech plc. Through its main operating subsidiary Hayward Tyler Group Limited, the worldwide market leaders in boiler circulating pumps, its focus is on the energy sector.

Author:

Ian McLelland +44(0)1202 770386
action@proactiveinvestors.com



In a recent interview on CNBC, Lloyd-Baker pointed out that Hayward Tyler is ideally positioned to continue benefiting from the emergence of India and China as economic powerhouses, and is still gaining business from other more developed countries like the U.K. and U.S which have plans to replace their ageing nuclear plants (and nuclear submarines). Hayward Tyler's already has installed equipment in 70% of the nuclear power stations in North America so is well placed for the growth of an additional 400 nuclear power station due to be built by 2030.

In 2008 total group sales were spread between USA (34%), Europe (28%), China (20%) with the remaining 18% spread across a number of other countries. Going forward, revenues are expected to accelerate strongly in Asia.

There is one blotch on the SEGR balance sheet however. The company came to the market with a net debt position of £8.9 million after paying down some of the debt with Nviro's £2.6 million cash pile and a placing of new shares which raised a further £3.1 million (net) from a number of 'blue-chip' financial institutions. There is also a pension fund which requires annual payments, though at the moment they aren't hefty.

Looking past the debt, on Fairfax's forecast 2010 earnings per share of 7.4 pence, the recent demise of the share price has clearly thrown up a value anomaly, the question now is can Lloyd-Baker deliver strong revenues generation, maintain profitability and increase working capital to support growth. If he can, the market valuation will better reflect this in time. Full year results from SEGR this morning certainly suggest this, and the market has noticed, pushing the company 28% higher by 10am.

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Contact us ■ +44 (0)1202 770386 ■ action@proactiveinvestors.com ■

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