

27 October 2009

Industrial Transportation  
FTSE All Share

## Braemar Shipping Services

### Resilient performance in H1. S&P activity underpins H2.

Price	382.0p
Price target	530.0p
12 high/low	408.8p / 200.0p
Market cap.	£80m
Enterprise value	£58m
Free float	65%
Avg. daily volume	21k
Shares in issue	21.0m
Net cash/equity	38.9%
Company code	BMS.L

Next news	May-2010
Confidence in estimates	Medium
Expected movement in estimates	◀▶

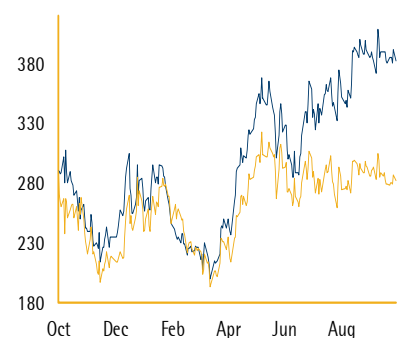
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#### Share price performance (1 year)



	1m	3m	12m
– Price	-2.1	6.6	37.7
– Rel all share	-4.0	-6.3	-0.1

Source: Thomson Datastream

■ **Event: Interims** – Braemar has announced a strong set of interims given the fundamental change in the shipping market between the first half to August 2009 and 2008. Revenues amounted to £57.1m (£69.1m) and pre-tax profit totalled £7.0m (£9.8m), comparable to H2 FY2009 PBT of £6.4m. The collapse in the shipping market at the end of 2008 caused the decline in revenues and profits, given the fall in freight rates and vessel values. Among the notable features of the interim performance was that within most segments of Shipbroking, transaction volumes have recovered to the pre-crisis levels, although values have declined. This is despite the weaker demand for oil impacting the tanker market and for finished consumer goods effecting the container market. The group's non-broking operations continue to perform well, accounting for over one-third of profits prior to central costs. The group has declared an increased interim dividend of 8.75p. Cash amounted to £9.8m.

■ **Reaction: Resilient performance given market condition** – The majority of the group's income is US\$ denominated and as such it has benefitted from the relative movement in the \$/£ exchange rate to an average of \$1.57/£ in the period compared to \$1.90. In broad terms a 10 cent swing in the rate approximates to a £2m change in shipbroking revenues. The forward order book appears little changed since the beginning of the financial year, with some notable newbuildings concluded in the period. Demand for dry bulk commodities continues to be strong, driven by the various stimulus packages in China and India. The underlying dry bulk market has rallied significantly from the lows in December due to increased iron ore imports and this looks set to continue.

■ **Impact: Upgrade** – We have upgraded our FY2010 PBT forecast by 7% to £13.2m, EPS of 44.1p and a higher full year dividend of 24.75p. The key driver has been the Shipbroking activities and the S&P desks, in particular, which delivered a record performance in terms of transaction volumes much of which will be delivered in the second half. Furthermore the group's Demolition volumes have increased, benefiting from weaker freight rates. We reiterate our Buy recommendation and price target of 530p, based upon the Industrial Transportation sector rating of 10.6x on FY2011 EPS. The shares currently stand on a PER of 8.6x for FY 2010 and a yield of 6.5%.

#### Key financial data (£m) - IFRS

Year to February	2008A	2009A	2010E	2011E	2012E
Sales	101.0	127.1	117.4	127.3	137.1
PBT normalised	14.7	16.2	13.2	14.3	15.9
EPS normalised (p)	48.76	55.83	44.17	50.00	55.83
DPS paid (p)	20.25	24.00	24.75	24.75	24.75
PER (x)	7.8	6.8	8.6	7.6	6.8
EV/EBITDA (x)	4.1	3.2	4.3	4.0	3.4
FCF yield (%)	20.6	17.4	5.0	9.0	11.1
Dividend yield (%)	5.3	6.3	6.5	6.5	6.5

## Interim performance

Comparisons between record period and current market state

Comparisons between these interim results to 31 August 2009 and the prior year reflect the shift in the market from the record conditions seen in 2008 and the subsequent fall. For the six months to 31 August 2009 group revenues declined by 17% to £57.1m (£69.1m) and pre-tax profit fell by 28% to £7.0m (£9.8m) and Basic EPS fell by 27% to 24.25p (33.51p) and the interim dividend was increased by 3% to 8.75p, with a dividend cover of 2.77x.

### Shipbroking

Revenue **£25.4m (£34.4m)** Operating profit **£5.5m (£8.9m)**.

Dry bulk market has rallied in the interim period.

#### Dry bulk

At the end of the reported period, the Baltic Dry Index stood at 2,421, having been 1,986 at the outset of the interim reporting period in February 2009. The performance of the index during the period mirrors the market, having slipped to 1,463 on 8 April and touching a peak of 4,291 on 3 June. It currently stands at 3,043. The market was driven higher by speculation about iron ore pricing which stimulated the spot market at a time when Chinese steelmakers were re-stocking/stock piling. This caused the Capesize market to recover which helped the smaller (vessel) categories to rally.

Impact of the stimulus package

The dry bulk market has flattened subsequently as iron ore pricing has been agreed which led to freight markets and trade to flatten. Demonstrably, underlying demand for raw materials remains strong as both India and China have maintained imports. One of the factors behind the continued increase in demand has been the impact of the various stimulus packages that have been enacted by the Chinese and other governments. The impact of the Chinese stimulus package of \$586bn on infrastructure spending has helped underpin annualised GDP growth of 8.9% in Q3.

Another factor which has underpinned the market over the next 12 months include crop estimates for Australia and Ukraine until Q1 2010. While the increased delivery of newbuildings over the next two-three years will have a negative impact upon freight rates, it seems likely that continued strong demand from China & India in the next 6-12 months will keep freight rates stable in the short term. However volatility is likely to persist in the freight market as Chinese raw material buying is predominantly in the spot market.

Tanker market impacted by delivery of newbuildings and fall in oil demand

#### Tankers

The deep sea tanker charter market anticipated a period of low charter rates, given the newbuildings being delivered to the market coincided with the fall in oil demand as a result of the economic slowdown. The Baltic Dirty Tanker Index is currently 580 having fluctuated between 453 and 731 over the last six months. This reflects an ominous outlook for both shipowners and operators alike. According to the results announcement, despite rates being depressed in all categories, the desk's market share has grown. In particular, the operation has increased its fixtures in the Chinese VLCC charter market and secured higher volumes of Suezmaz business in the Atlantic. The volume of fixtures has remained healthy as a result of a number of contracts of affreightment being concluded.

A reduction in refinery runs at the major refinery hubs around the world has reduced the levels of (refined) products being distributed which has affected the earnings of

all product carriers. This has also impacted the chemicals markets, especially in Europe, but the operation is underpinned by term contracts secured in prior years.

#### LPG

Secured new business in the period

The LPG markets have been affected as well but the operation has managed to secure new business in the larger vessel market which has help maintain income at comparable levels to last year. With LPG chartering and new product broking team, the operation continues to expand its client base.

#### LNG

A number of new LNG charters

The group has secured a number of LNG charters to major producers and receivers alike. It has also secured several commercial tenders with Wavespec.

#### FFA

Impacted by the decline in physical chartering

Transaction volumes within the FFA operation have been adversely impacted by the decline in physical charter volumes and as a result of market volatility. The new 'wet' desk has made good progress since establishment.

S&P has reported a "tremendously strong half"

#### Sale & Purchase

The group's Sale & Purchase operations have reported a "tremendously strong half", setting a historic record for transaction volumes. Furthermore much of this business will be delivered in the second half. It appears that a number of clients have looked to exploit falling price levels in all segments of the market. The operation has a strong market position. Furthermore within S&P, demolition volumes have increased substantially. This trend is likely to continue given weaker prevailing freight rates.

Container market depressed

#### Containers

The Container market has been depressed with most liner companies fighting for their survival and owners continuing to struggle. The market is unlikely to recover in the short term, although volumes may increase as consumer confidence improves. The group's ability to offer 'a one-stop' shop has facilitated the transaction of a number of S&P and charter transactions.

High activity levels

#### Offshore

The Offshore desk has reported high activity levels, though revenues have been impacted by lower spot rates. The forward order book is "healthy".

## Technical

Revenue £12.4m (£10.4m) Operating profit £1.6m (£1.9m).

### Braemar Falconer

(Technical, survey and consultancy services for the marine and energy sector).

H1 revenues matched comparable period last year

Braemar Falconer's revenue for the first half matched the comparable period last year, despite the adverse outlook at the start of the financial year. Significant new contracts have been secured in China and Vietnam which has offset lower rig move work which has declined since the start of the year. Engineering consultancy work was steady and although there was pressure on chargeable rates. The group continues to be busy although at a lower level than last year. Second half activity is expected to be similar to the first half.

### Braemar Steege

(Specialist loss adjusting and other expert services to the energy, marine and related industrial insurance sectors)

Continued to perform in line

Braemar Steege continues to perform in line with expectations. The London office has received a number of notable loss adjusting instructions concerning losses in the North Sea and West Africa. There has been an increase in demand for expert witness services. The Houston & Calgary offices have seen a reduction in instructions due to the quieter hurricane season in the Gulf of Mexico. The group's Latin American operations have seen a good level of client activity following expansion in the region. Singapore continues to dominate the energy adjusting sector in Asia and the office has recently been appointed to high-profile well control incident offshore of Western Australia.

### Braemar Marine

(Marine surveying and adjusting services to the hull, cargo and P&I insurance market).

Braemar Marine launched in August

Braemar Marine was launched in August to provide marine surveying and adjusting services to the hull, cargo and P&I insurance market. Initial progress has been slower than originally anticipated but following a number of recent appointments, the operation should become profitable within the next 18 months.

### Wavespec

(Design development, plan approval and construction supervision of ships of all types of vessels, with strong emphasis on ships carrying liquid cargoes in bulk. World leader in the design and construction of Liquid Natural Gas (LNG) carriers).

New office opened in Houston

Wavespec has continued to perform well over the period. It has gained significant contracts to carry out technical due diligence and support to a major financial group as it looks to take equity stakes in two LNG carriers and undertakes feasibility studies for the potential to ship gas from the Middle East to China and Europe. Wavespec has opened its first overseas office in Houston, Texas which now employs five people and provides specialised consulting services mainly for LNG Terminals and the offshore sector.

## Logistics

Revenue £16.0m (£21.6m) Operating profit £1.1m (£0.2m).

### Increased margins in the period

Cory Logistics increased margins in the period due to new project forwarding work, favourable market conditions in its import forwarding business and an expansion of its liner business. Fred Olsen Freight has been fully integrated with Cory since March 2009, bringing together 90 staff.

### Steady performance

Ship agency continued to perform steadily, maintaining volumes and increasing market share in a depressed market overall. It has benefited from its ship to ship transfer and hub service businesses. The cruise business also saw an increase in port calls and passenger take-up throughout the summer season.

## Environmental

Revenue £3.3m (£2.7m) Operating profit £0.2m (£1.9m).

### Revenues increased by 23%

Revenues increased by 23% with key contributions from established income streams as well as a number of oil spill incidents secured through existing retainer contacts. Profits were similar to last year with cost control a focus. New business has been won in domestic marine contracting together with response, consultancy and training overseas in Australia, the Middle East, North and South America.

## Financials

### Acquisitions

Deferred payments for acquisitions

During the interim period, two stage payments were made relating to Steege Kingston Partnership Limited which was acquired in March 2008. A total of £1.0m was paid together with £0.1m in respect of fair value of the net assets acquired.

Acquisition of Cagnoil

In the first half the group has acquired Cagnoil for a consideration of £0.7m with a further £0.2m due over the next two years. Net assets acquired included £0.2m of cash. It is expended £0.1m on the purchase of a shipbroking operation which specialises in LPG broking.

### Financial

Majority of group's income is US\$ denominated

The majority of the group's income is US\$ denominated and the average rate of exchange for the conversion of US\$ income in the six months to 31 August 2009 was \$1.57/ £1.90 (Interim period to 2008-2009 and \$1.85/£ - Full year 2008-2009). In broad terms a 10 cent swing in the US\$/£ exchange rate approximates to a £2m change in shipbroking revenues over a full year. The rate of translation as at 31 August was \$1.63/£.

Cash balance amounted to £9.8m.

Cash balances amounted to £9.8m as at the period end compared to net cash of £25.2m as at the year end and £11.1m in the comparable period in 2008. The group normally generates the bulk of its annual cash flow in the second half of the year. We are forecasting year end net cash of £22.2m. The reduction in cash at the interim stage reflects the payment of the annual broking bonus, acquisition consideration payments and the payment of the final dividend relating to the prior year. Capital expenditure in the interim period relates to the cost of fitting out the new Logistics premises at Felixstowe and the cost of improvements to other leasehold premises.

## Share price performance

The shares have rallied from a low point of 200p reached in April 2009 to 382p currently. The share price over the last 12 months shows an increase of 37% over the last 12 months in line with the FTSE All-Share.

Over the last three months the shares have risen by 6.6% and have yet underperformed the FTSE All-Share by 6%.

The sub-sector of shipbroking companies trades on a PER of 8.5x and 10.5x and a dividend yield range of 4.2% and 6.5%. We value the sub-sector on the basis of the broader Industrial Transportation sector which trades on a PER of 10.6x, giving a target price of 530p based upon 2011 EPS.

## Financials

### Profit & loss account (£m) - IFRS

Year to February	2008A	2009A	2010E	2011E	2012E
Shipbroking	52.8	60.4	55.0	60.5	65.3
Logistics	27.9	40.8	31.0	33.0	35.2
Technical	9.5	21.2	24.4	26.8	29.6
Environmental	10.8	4.7	7.0	7.0	7.0
<b>Sales</b>	<b>101.0</b>	<b>127.1</b>	<b>117.4</b>	<b>127.3</b>	<b>137.1</b>
Shipbroking	13.0	14.9	10.5	11.9	13.1
Logistics	1.0	0.8	1.7	1.2	1.3
Technical	0.7	3.5	3.2	3.5	3.8
Environmental	1.8	-0.2	0.3	0.2	0.2
Unallocated Common Costs	-2.5	-3.4	-3.0	-3.1	-3.1
<b>Operating profit</b>	<b>14.0</b>	<b>15.7</b>	<b>12.7</b>	<b>13.7</b>	<b>15.3</b>
Associates & other income	0.4	0.2	0.3	0.3	0.3
Finance costs	0.4	0.3	0.2	0.3	0.3
<b>PBT normalised</b>	<b>14.7</b>	<b>16.2</b>	<b>13.2</b>	<b>14.3</b>	<b>15.9</b>
Abnormal items	0.0	0.0	0.0	0.0	0.0
PBT reported	14.7	16.2	13.2	14.3	15.9
Taxation	-4.8	-4.7	-4.0	-3.9	-4.4
Minorities & preference dividends	-0.1	-0.1	-0.1	-0.1	-0.1
Profit for period (continuing)	9.4	11.2	8.8	10.0	11.2
Profit for period (discontinuing)	0.0	0.0	0.0	0.0	0.0
Profit attributable to shareholders	9.8	11.5	9.1	10.3	11.5
AWC (FD) (m)	20.1	20.6	20.6	20.6	20.6
<b>EPS normalised (p)</b>	<b>48.76</b>	<b>55.83</b>	<b>44.17</b>	<b>50.00</b>	<b>55.83</b>
EPS Reported (FD) (p)	48.76	55.83	44.17	50.00	55.83
<b>DPS paid (p)</b>	<b>20.25</b>	<b>24.00</b>	<b>24.75</b>	<b>24.75</b>	<b>24.75</b>

Source: Charles Stanley Securities

### Performance metrics

Year to February	2008A	2009A	2010E	2011E	2012E
Sales growth (%)	36.8	25.9	-7.7	8.5	7.7
EBITDA growth (%)	34.4	17.3	-25.9	8.4	11.6
EPS normalised growth (%)	54.0	14.5	-20.9	13.2	11.7
DPS growth (%)	11.0	18.5	3.1	0.0	0.0
Gross margin (%)	72.0	72.4	76.5	73.2	70.9
EBITDA margin (%)	15.0	13.9	11.2	11.2	11.6
Operating margin (%)	13.8	12.3	10.8	10.7	11.2
Interest cover (x)	na	na	na	na	na
Taxation rate normalised (%)	32.6	29.0	30.5	27.5	27.5

Source: Charles Stanley Securities

## Financials – continued

### Cash flow statement (£m) – IFRS

Year to February	2008A	2009A	2010E	2011E	2012E
Operating profit	14.0	15.7	12.7	13.7	15.3
Operating profit discontinued	0.0	0.0	0.0	0.0	0.0
Depreciation & amortisation	1.1	2.0	1.2	1.3	1.3
Other non-cash movements	0.2	0.5	0.0	0.0	0.0
Change in working capital	5.8	2.7	-3.5	-1.5	-1.5
Other cash movements	0.0	0.0	0.0	0.0	0.0
<b>Operating cash flow</b>	<b>21.0</b>	<b>20.9</b>	<b>10.3</b>	<b>13.5</b>	<b>15.1</b>
Taxation paid	-4.6	-6.2	-4.8	-4.9	-4.9
Finance costs paid	0.3	0.3	0.2	0.3	0.3
Investment income	0.0	0.0	0.0	0.0	0.0
Capital expenditure (net)	-1.0	-1.2	-1.8	-1.8	-1.8
<b>Free cash flow</b>	<b>15.8</b>	<b>13.7</b>	<b>3.9</b>	<b>7.1</b>	<b>8.7</b>
Other investing activities	0.2	0.0	0.0	0.0	0.0
(Acquisitions)/disposals	-4.3	-5.1	-2.0	0.0	0.0
Dividends paid	-4.2	-4.9	-5.0	-5.0	-5.0
Shares issued/(repurchased)	-0.7	-0.8	0.0	0.0	0.0
Other financing	0.2	0.7	0.0	0.0	0.0
<b>Movement in net cash/(debt)</b>	<b>7.0</b>	<b>3.6</b>	<b>-3.1</b>	<b>2.1</b>	<b>3.7</b>
Net cash/(debt)	21.6	25.2	22.2	24.2	28.0

Source: Charles Stanley Securities

### Balance sheet (£m) – IFRS

Year to February	2008A	2009A	2010E	2011E	2012E
Goodwill	25.8	28.1	28.1	28.1	28.1
Intangible fixed assets	2.3	3.9	2.8	3.0	3.0
Tangible fixed assets	5.8	6.2	7.3	8.3	9.4
Working capital	-13.1	-8.2	-4.7	-3.2	-1.7
<b>Assets employed</b>	<b>20.9</b>	<b>30.1</b>	<b>33.6</b>	<b>36.3</b>	<b>38.9</b>
Other assets/(liabilities)	-0.9	-0.7	2.9	3.3	3.5
Net cash/(debt)	21.6	25.2	22.2	24.2	28.0
Provisions	-0.1	-1.7	-1.7	-1.7	-1.7
<b>Net assets</b>	<b>41.5</b>	<b>53.0</b>	<b>56.9</b>	<b>62.2</b>	<b>68.6</b>
Minority interests	0.3	0.1	0.0	0.0	0.0

Source: Charles Stanley Securities

### Key ratios

Year to February	2008A	2009A	2010E	2011E	2012E
Net cash (debt)/equity (%)	52.1	47.6	38.9	39.0	40.8
ROAE (%)	45.1	37.0	26.3	27.3	28.6
Net assets per share (p)	207.50	262.38	281.68	307.92	339.60

Source: Charles Stanley Securities

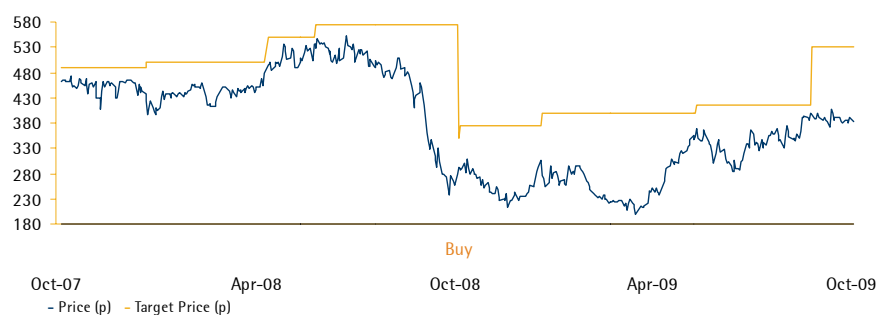
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### Share price performance



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Buy	101	44.89	Buy	26	59.09
Add	31	13.78	Add	5	11.36
Hold	73	32.44	Hold	13	29.55
Reduce	12	5.33	Reduce	0	0.00
Sell	8	3.56	Sell	0	0.00

### Charles Stanley Securities rating definitions – 12 month time scale

Buy	+20% < expected absolute change
Add	+10% < expected absolute change < +20%
Hold	-10% < expected absolute change < +10%
Reduce	-20% < expected absolute change < -10%
Sell	expected absolute change < -20%

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