

Entry & Exit Smiths News: Cash flows that support a +10% dividend yield

Company: Smiths News (SNWS LN) Market Cap: £80mio

Industry: Newspaper print & distributor Net Debt: £38.8mio

Country: UK Revenue: £1.1bn

Date: 6th October 2022 Net Income: £20mio (1.8%)

Dividend: £10mio (14%) Free Cash Flow: £20mio (1.8%)

Entry: £70mio Exit: £78mio

A turnaround

Smiths News is the UK's largest Newspaper & magazine print & distributor with a 55% market share. The contracts are renewed on a 5-year basis with 95% of current contracts running until 2024 and 60% until 2025. This enables stable revenues into the near future and growth potential from 2024/25 onwards. The key about the business is the declining newspaper industry which is shrinking by about 3% annually and this is why investors shun the sector and why there is value in the business... The sale of their logistics business, Tuffnells, and the winding up of the WHSmith Pension Trust has generated extra cash flows including in the current FY (£6.5mio + £7.5mio from Tuffnells, £8.1mio from WHSmith), which has helped accelerating a reduction in debt. This in turn is reducing interest expenses and ultimately makes this a compelling turnaround story. The enterprise value has mostly been around £150mio, but is currently only £110mio, which enables upside of over 50% for the equity (although given the nature of the decline in the newspaper business, my target market cap would be £100mio for now, or £130mio enterprise value in 3-6 months. Net debt is also volatile due to working capital requirements, and hence might turn out to be somewhat higher at £40-£45mio due to the early receipt of £20mio ahead of the interim results).

Smiths News: Financial turnaround



Variable	2017	2018	2019	2020	2021	2022*
Revenue	1412.2	1361.6	1303.5	1164.5	1109.6	1100
Adjusted EBITDA (excl IFRS16)	50.1	46	48.8	39.1	42.6	41
Interest expense	5.2	5.8	5.1	8	9.5	5.5
Adjusted net income	39.1	24.2	19.4	10.6	26.3	25
Bank net debt	82.1	83.4	73.9	79.5	53.2	30
Market capitalisation	276	98	89	71	96	81
Dividends per share (p)	9.80p	3.10p	1.00p	0.00p	1.65p	4.1p

*expected

Source: Smiths News

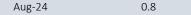
The nitty gritty of the financials

Below are two tables showing Smiths News debt repayment plan and resulting cash flows under £40mio EBITDA assumptions for 2023. With EBITDA of £40mio a £10mio dividend can be maintained while declining interest expenses can be offset with higher capital spending, which is currently at depressed levels and should eventually raise back to around £7mio. The McColl administration, however, has led to £4.4mio bad debt, which in turn would immediately eat into the dividends, if the company had not received the additional receipts from the WHSmith pension trust and the Tuffnells disposal. Therefore, the below calculation is the ideal case and hence subject to revision that could easily appear in the current macroeconomic environment.

Smiths News Debt Repayment Plan

Debt facility	Sonia+4.25% (in £mio)	
RCF	13.3	
Loans	46.9	
Repayment schedule	Facility A (£46.9mio)	
FY 2022	3	
FY 23	8	
FY 24	10	
FY 25	10	
Final bullet payment	15.9	
Repayment schedule	RCF (£13.3mio)	
Nov-22	5	
Feb-23	2.5	
Aug-23	2.5	
Feb-24	2.5	





Source: Smiths News

Smiths News 2023 Cash Flow estimate

£ mio cash flow 2023 estimate	Component
40	EBITDA
-6	Interest expense
-7	Leases
-4	Capex
-10	Dividend
-13	Bank debt repayment
0	Net cash flow

Source: Smiths News, own estimate

Early exit

When I bought shares in Smiths News I was putting a limit buy order in right at the close at high volume, expecting that not much will likely get filled. To my surprise, the entire order got filled with a size of the usual daily total volume. The liquidity of shares in Smiths News is quite low and this made me sell shares after a quick 10% gain out of fear that when volatility increases the valuation could suffer and I would be unable to sell in the current macroeconomic environment. Nonetheless, the business remains undervalued at £40mio EBITDA, which is the reason I filed this report in order to revisit it again in the future. Smiths News remains a turnaround candidate, but there is a reason why the valuation is so cheap: Margins are low and small downside in earnings would immediately affect dividend payouts and hence the valuation.





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