

Morning Meeting Notes

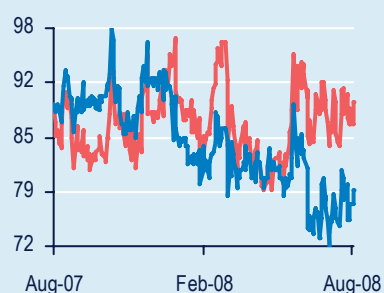
Buy **79p**

Potential upside **13%**

Target price **89p**

Market cap £128m
 12m high / low 98p/72p
 Average daily volume (000s) 175
 Sector Food Producers
 Index FTSE Small Cap
 RIC / Bloomberg DVO.L / DVO LN
 Implications for forecasts ▲

Share price performance



	1m	3m	12m
Price	5.0	(2.8)	(10.5)
Rel. All Share	2.6	8.1	3.1
Rel. Sector (not shown)	2.8	7.8	(0.8)

Source: JCF Group

Devro

Solid 1H progress

Devro has reported solid progress in 1H, with EBIT up 16%. Volumes have continued to grow, particularly in emerging markets, and the group is making good progress in securing price increases in line with its new strategy. There is some uncertainty over energy costs in 2H, but we still feel comfortable in increasing our profit forecast. After a higher tax charge EPS forecasts increase by 3%.

Key Forecasts

UNDER REVIEW - previous forecasts below

Year end: 31 December	2007	2008E	2009E
Turnover (£m)	156.3	160.9	164.5
PBT (normalised) (£m)	15.6	15.8	16.6
EPS (norm, continuing) - FD (p)	7.1	6.9	7.3
DPS (p)	4.45	4.45	4.45
PE (normalised) (x)	11.1	11.4	10.8
EV/EBITDA (x)	5.6	5.5	5.3
FCF yield (%)	4.6	2.7	5.8
Dividend yield (%)	5.7	5.7	5.7

Source: Company accounts/Investec Securities estimates

- Devro has reported a solid set of interim numbers showing good progress on all levels. The pre-tax (pre exceptional) number is £7.89m which was 19% up on last year, and compared to our forecast of £7.25m. H1 last year was a difficult period, but nevertheless there have been some sound improvements in the business behind these numbers. EPS (adj) were 3.3p and the dividend was maintained at 1.425p.
- An exceptional charge of £2.9m was made in the period which reflects a £3.1m non-cash charge for the proposed closure of Korenov in the Czech Republic, partially offset by some property profits. In 2H, there will be a further £0.6m charge to reflect the cash closure costs. The closure should result in annual savings of £2m from 2010. The Jilemnice plant will receive £5m of investment to allow it to absorb the volume from the 100 yr old Korenov site.
- The group registered volume growth of 2.7% overall (4% for edible collagen), which is a little below the long-term target, but this includes the last impact from the US where volumes declined as a result of a major customer switching to collagen gel. By region, the emerging markets provided the main driver to volume - Eastern Europe was ahead by 9% and Asia Pacific overall up by 11%. However, there was also some recovery in some of the group's more mature markets, including the UK.
- Price showed a 2.2% advance clean of any exchange movements, which is comfortably in line with the group's expectation of securing 2-2.5% price increases by the end of the year. Bearing in mind the group only began this process part way through 1H, we believe this is a good start and there are more

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regions where price increases have been agreed but which will only become effective in 2H.

- Exchange rates have been particularly helpful to sales in the period (+8.5%), benefiting from weaker sterling. However, at the EBIT level exchange factors overall marginally impacted on profits to the tune of £0.3m. Hence, for the group to show a percentage margin increase is all the more commendable, in our view. EBIT margins increased from 10.8% to 11.1%.
- Devro closed the half year with net debt of £34.5m, which was in line with our expectations. At the full year we expect the group to be able to marginally improve on last year's debt number of £27.5m. The extra capex for Jilemnice will fall into 2009.
- For the second half, we expect the group to show a similar volume advance. The US drag factor will fall out of the equation, but we do have tougher volume comparatives from the previous year. Price we are assuming contributes slightly more than 1H, but FX is expected to be less helpful on sales. Overall, we could still see a sales advance in the 5-10% range.
- The group is facing higher input costs in 2H – notably energy where cost increases are currently estimated at £2m versus a 1H increase of £0.4m, although the tariffs are changing constantly. With the help of pricing improvements, the group is hopeful of maintaining cash margins in 2H, but the % margin might slip back due to the inflationary impact of exchange rates on revenues but no assistance to EBIT. However, this still translates through to a profit forecast upgrade of £1.2m to £16.95m (+7%). EPS increase from 7.0p to 7.2p (+3%) after a higher tax rate assumption. We lift our target price (based on EV/EBITDA) correspondingly to 89p from 86p. Buy.

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Definition of research ratings

	Expected 12m performance
Buy	Appreciation of 10% or more
Hold	Appreciation or depreciation of less than 10%
Sell	Depreciation of 10% or more

UK stock ratings distribution

	Coverage universe		Investment banking clients	
	Count	% of total	Count	% of total
Buy	121	57%	30	25%
Hold	70	33%	9	13%
Sell	23	11%	1	4%

Source: Investec Securities

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Devro Ratings Plotter as at 28 Aug 08



Source: JCF Group/Investec Securities

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