

Lok'nStore Group 63.5p
Value in Store

9 November 2009

Share Price: 63.5p



Shares in Issue: 25m fully diluted

12m High: 80p

12m Low: 34.5p

Market Cap: 15.9m

NAV/Share: 207p with properties at valuation

Gearing: 59.8% with properties at valuation

Interest Cover: 2.5X

EPIC Code: LOK.L

Sector: Support Services

Market: London AIM

Broker: Arbutnot Securities

PR: Financial Dynamics

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Description: Lok'nStore is the fourth largest self-storage group in the UK with a c. 5% market share. It owns 23 self-storage centres in the affluent South East of England, 21 of which are open. The freehold/leasehold sq ft split is 64/36. The household/business revenue (£) split is 62/38.

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Lok'nStore has produced credible full year results despite extraordinarily tough trading conditions and it is encouraging to note that the recovery in enquiries, reservations and occupancy seen in H2 has continued into the current 2010 financial year. Key points from the FY results are:

- Although lower than the previous year, both revenue (£10.03m) and group EBITDA (£2.45m) were ahead of our expectations.
- The final dividend of 1p/share restores the 2008 full year payout and clearly signals management's confidence in future prospects.
- Central costs have been reduced by 6.6% and this has protected margins.
- Occupancy, a key indicator, finished the year up 1.7% to 561,000 sq ft (52% of total lettable space).
- Cash generation remains strong with net cash flows from operating activities increasing by 21% to £1.7m.
- Net debt has risen from £22.8m to £24.9m due to the capex spend on Harlow but the all-in cost of the group's debt, at 3.4%, has more than halved. This has benefited the p & l and cash flows.
- Gearing based on properties at valuation is a comfortable 60% and Lok'nStore has working capital headroom of £12m on facilities which run through to 2012.
- The 15% decline in adjusted NAV to 207p per share compares favourably both to the current share price and the declines seen in other property sectors.
- The new 69,000 sq ft Harlow store has launched well and is operating at cash flow breakeven after just seven months.
- All four stores in the development pipeline - Portsmouth North Harbour, Maidenhead and the two replacement stores in Southampton and Reading – now have planning permission. Nonetheless, with the extent of the economic recovery still uncertain, our estimates model assumes capital spending will remain at a modest level in 2010.

We have upgraded our 2010 estimates and expect revenue and profits to rise sharply in 2011. At the current share price, Lok'nStore is trading at a 69% discount to NAV. This is significantly greater than the discount afforded to larger comparators Safestore (31%) and Big Yellow (16%) and in our view fails to recognise the current value of the portfolio, strong cashflow generation, future growth potential of the development pipeline and favourable long-term trends for the self storage industry.

Y/E	Group Sales	Group EBITDA	Declared Profit/(Loss)	Adjusted Profit/(Loss)	Adjusted EPS	Mkt Cap/ EBITDA	Divi	Yield
July	£m	£m	£m	£m	P	X	P	%
2008A	10.83	2.73	(0.74)	(0.31)	(1.5)	5.8	1.00	1.6
2009A	10.01	2.45	(0.66)	(0.66)	(2.4)	6.5	1.00	1.6
2010E	10.30	2.56	0.10	0.10	0.4	6.2	1.00	1.6
2011E	11.11	3.13	0.55	0.55	2.19	5.1	1.00	1.6

The Full Year Results – A Tale of Two Halves

The year to 31 July 2009 was a mixed one for Lok'nStore. Against a backdrop of the financial crisis and ensuing collapse in consumer confidence, the first half of the year (July 08 – January 09) saw occupancy rates decline and EBITDA decrease by 20%. Management responded quickly and effectively to the downturn, ramping up promotional activity, driving ancillary income, curtailing capex and cutting costs. These actions coincided with an improvement in trading conditions across the sector from January and the start of six consecutive months of occupancy growth - a trend which has continued into 2010.

The FY results showed revenue of £10.03m, a 7.6% decline on the previous year but slightly ahead of our £9.96m forecast. Whilst y/e occupancy was up 1.7% y-on-y part of this growth was achieved at the expense of pricing which declined by 2.3% to £17.50 per sq ft. Having arrested the decline in occupancy, prices are now on the rise again with plenty of scope for future gains against a sector average price of £21.08.

Group EBITDA benefited from the 6.6% reduction in operating costs, finishing the year down 10.6% to £2.45m (vs. our forecast of £2.32m). Notably store EBITDA margins in the 17 established stores over five years old were virtually unchanged at 41.5% and the two larger purpose-built freehold stores in Farnborough and Crayford, accounting for 12% of total lettable space, continued to trade well, generating EBITDA margins of 53.5%.

Due to the material reduction in interest rates the average all-in cost of the group's debt more than halved, to 3.37%. So whilst net debt increased, from £22.8m to £24.9m, interest on the group's loans reduced by £0.55m. This reduction in the interest charge together with the progress made on reducing costs delivered a boost to cash generation, with net cash from operating activities increasing by 21% to £1.7m.

The y/e external property valuation gave an adjusted NAV per share of 207p, 15% below the previous year but 3.5% ahead of the directors' valuation of 200p/share at end Jan 2009.

Outlook and Forecasts - Better Year in Prospect

With annualised sales running at £10.3m and the group benefiting from a reduction in operating and interest costs we are maintaining our full year turnover estimate of £10.3m but upgrading our adjusted pre-tax profit estimate to £0.1m (vs. our previous forecast of £(0.56)m) and our dividend per share estimate from zero to 1p/share. For 2011, we expect revenue and pre-tax profit to move sharply higher to £11.1m and £0.56m respectively because by then the economic recovery ought to be on a more stable footing. Whilst all of the data on enquiries, reservations, occupancy, and more recently pricing continue to show forward movement uncertainty remains about the extent of the UK recovery in 2010 and consequently we think it unlikely that any of the four stores in the development pipeline will open before H2 2011. Consequently, we expect net debt to fall to £24m in the current year.

Valuation – Current Discount to NAV Difficult to Justify

	Lok'nStore	Safestore	Big Yellow
Financial Year End	July 2009	Oct 09	March 09
Current Share Price (p)	64p	134p	385p
NAV per share (p)	207p	194.2p	457p
Premium/(Discount) to NAV	-69%	-31%	-16%

The table above shows that at the current share price Lok'nStore is trading at a discount to NAV that is twice the size of the discount afforded to Safestore and four times that of Big Yellow. Both Safestore and Big Yellow are considerably larger operators than Lok'nStore and have also reported better progress on key KPI's (occupancy, pricing, new store openings) than Lok'nStore in recent months, albeit for shorter trading periods. This may go some way towards explaining the yawning valuation gap. Nonetheless, the current Lok'nStore rating clearly fails to recognise the current value of the portfolio, more optimistic trading outlook, strong cashflow generation and future potential for growth. Placing the shares on a more reasonable 40% discount to adjusted NAV would imply a share price of 124p, almost double the current 63.5p.

Store EBITDA margins, cushioned by cost cuts, have held up well during the downturn

We are upgrading our 2010 numbers

Placing the shares at a 40% discount to NAV would suggest a share price twice the current level

Lok'nStore Group

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Management	Major Shareholders
<p>Chairman: Simon Thomas</p> <p>Chief Executive Officer: Andrew Jacobs</p> <p>Finance Director: Ray Davies</p> <p>Acquisitions Director: Colin Jacobs</p> <p>Non-Executive Director: Richard Holmes</p> <p>Non-Executive Director: Robert Jackson</p> <p>Non-Executive Director: Edward Luker</p> <p>Non-Executive Director: Charles Peal</p>	<p>Andrew Jacobs: 20.74%</p> <p>Audley Capital: 16.64%</p> <p>Simon Thomas: 8.38%</p> <p>Montanaro Investment Managers: 6.05%</p> <p>Oliver Bernard Ellingham: 5.19%</p> <p>Charles Stanley 4.03%</p>
Key Dates	Key Milestones
<p>Annual General Meeting: 11 December 2009</p>	<p>April 1997: Floated on OFEX raising £1.1m at 38p</p> <p>March 2008: Second fundraising raised £1.15m at 60p/share</p> <p>November 1999: Takeover approach from ACCESS rejected. ACCESS takes 29% stake in co for £4.8m</p> <p>June 2000: Lok'nStore moved to AIM</p> <p>July 2002: Share placing at 155p per share raises £10m</p> <p>January 2004: Second cash bid at 115p/share rejected</p> <p>February 2007: First purpose-build freehold store opened in Farnborough.</p> <p>March 2007: Kingston unit sold to a residential developer for £10m (NBV: £0.98m)</p> <p>January 2008: Residential planning permission granted for existing Reading store.</p> <p>April 2009: Confirms an early stage expression of interest in the group from a third party</p> <p>July 2009: Offer talks terminated</p>

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