

SPRINGFIELD PROPERTIES

HOME CONSTRUCTION

19 July 2023

SPR.L

64.5p

Market Cap: £76.4m

SHARE PRICE (p)



12m high/low 135p/64p

Source: LSE Data (priced as at prior close)

KEY DATA

Net (Debt)/Cash	£(63.0)m (at 31/05/23)
Enterprise value	£139.4m
Index/market	AIM
Next news	FY23 results, Sep (TBC)
Shares in Issue (m)	118.5
Chairman	Sandy Adam
CEO	Innes Smith
CFO	Iain Logan

COMPANY DESCRIPTION

Springfield Properties, Scotland's only quoted housebuilder, is focused on delivering private and affordable housing.

www.springfield.co.uk

SPRINGFIELD PROPERTIES IS A RESEARCH CLIENT OF PROGRESSIVE

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'In-line' results in face of multiple challenges

Springfield's FY23E period-end trading update confirms that profits will be in line with expectations despite challenging UK economic conditions and specific headwinds in the affordable housing and private rental sectors in Scotland. However, the group has cautioned on the near-term outlook in the private sales market. For now, we maintain our FY24E forecasts until greater visibility emerges at the September results on the private market and, possibly, more supportive policy on affordable housing.

- **'In-line' FY23E guidance.** Revenue for the year to 31 May 2023 increased by 28% to a record c.£330m, driven by full-year contributions from the Tulloch Homes and Mactaggart & Mickel Homes acquisitions. Adjusted PBT is expected to be in line with market expectations and achieved despite the impact on private reservations of the mini-budget in late September. Net debt was £68m, slightly below our estimate (page 2).
- **FY24E forecasts maintained for now.** The group 'remains cautious about the near-term outlook'. We intend to re-examine our FY24E estimates at the results in September, when we believe greater clarity may emerge on private demand and also affordable housing policy.
- **Private sales uncertain.** We believe the current slowdown in transactions, widely reported by UK housebuilders, could be temporary – as was the case following the mini-budget (page 3). That hiatus lasted for some three months, followed by improving demand until around late April. The key uncertainty for us is how long the current cycle of rate tightening deters buyers: our sense is around three to six months. We suspect there could be more clarity on the direction of travel at the results in September. Any pause in FY24E, however, could feed through to delayed demand in FY25E.
- **Affordable housing boost.** Conversely, a potential positive for FY24E could be further evidence by the time of the results that the Scottish Government has relaxed its stance on payments for affordable housing work. Springfield temporarily halted entering new long-term affordable housing contracts; Scotland's new housing minister has since raised the 'benchmark' (level of grant paid towards the delivery of new affordable homes) by 16.9%. One less clear factor that we await news on is the rent cap, which led to a suspension of private rental sector (PRS) work.
- **Unique multi-tenure model.** Springfield provides private, affordable rental and PRS homes, in its distinctive 'Village' communities (page 8).

FYE MAY (£M)	2020	2021	2022	2023E	2024E
Revenue	143.5	216.7	257.1	332.6	290.9
Fully Adj PBT	10.2	18.5	20.8	16.8	20.2
Fully Adj EPS (p)	8.2	14.2	15.2	11.2	12.5
Dividend per share (p)	2.00	5.75	6.20	3.10	5.10
PER (x)	0.0x	4.6x	4.2x	5.8x	5.2x
Dividend yield (%)	3.1%	8.9%	9.6%	4.8%	7.9%
EV/EBITDA (x)	10.2x	6.4x	5.7x	5.9x	5.4x

Source: Company Information and Progressive Equity Research estimates.

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No change to FY24E estimates until greater clarity emerges on sales market and administrative backdrop at September results

Cautious sales outlook offset by affordable housing fillip

Springfield's period-end trading update, in our view, demonstrates resilient performance against a challenging backdrop of a UK-wide cost-of-living crisis and rising mortgage costs, and more specific obstacles in Scottish policy on affordable housing and rents. We believe it will take a few months for greater clarity to emerge on all three issues, and are thus waiting until the results in September to revisit our FY24E estimates. However, in this note we examine the potential economic and political drivers.

- **Results in-line.** Revenue for the 12 months to 31 May is expected to increase by 28% to c.£330m (Progressive estimate: £340m), largely reflecting full-year contributions from the Tulloch Homes and Mactaggart & Mickel Homes acquisitions. Adjusted PBT is expected to be in line with market expectations and we are shaving only 1% off our estimate to £16.8m (FY22E: £20.8m). The decline in profitability, as previously announced, reflects the impact from significant build-cost inflation, particularly on fixed-price contracts in affordable housing. Net debt, pre-IFRS 16 leases, was £63.0m, below our estimate of £70.7m, due to tight control of working capital, in our view.
- **Decisive response.** The group took decisive action in response to the 'challenging' market backdrop. It temporarily halted entering new large long-term affordable housing contracts and adopted a cautious approach to new site launches in private housing. Other actions include: reducing land-buying activity to retain capital; pausing recruitment and reducing staffing levels in areas most impacted by the market downturn; and maintaining tight cost control. These moves will deliver future savings of c.£3.0m on an annualised basis. Springfield also made a strategic land sale during the year to a national housebuilder, as previously announced, and 'will consider further opportunities where the terms and price are desirable'.
- **Awaiting clarity on FY24E outlook.** The private sales market has clearly weakened since Springfield's 31 May year-end, but we believe there is unlikely to be sufficient clarity on the potential outlook for volumes until the latest bout of mortgage rises (which may be plateauing, in our view) have fed through, possibly at the results in late September. Meanwhile, there are more encouraging signs for the affordable housing business. On pages 3 and 4, we explore what we believe is a temporary pause in private housing demand, at least partially offset by more profitable affordable housing conditions. We also speculate on the potentially positive impact on investor sentiment in PRS as the market adjusts to the rent cap in place.
- **New CFO announced.** Last week Springfield announced that Iain Logan, interim CFO since March, had been confirmed to the permanent role. Mr Logan, aged 49, has held the positions of Finance Director and Group Financial Controller over the last three years. He was responsible for leading all aspects of financial operations and reporting, and for managing the group's banking relationships. He also played a key role in the group's acquisition, and integration, of Tulloch Homes in December 2021 and the Scottish housebuilding division of MacTaggart & Mickel in June 2022. Prior to joining Springfield, he was Group Financial Controller of AIM-quoted Omega Diagnostics Group, a specialist medical diagnostics company, for nine years. He is a Chartered Accountant with the Institute of Chartered Accountants of Scotland and began his career at PwC in Edinburgh.

Evidence suggests slowdown in transaction volumes will be temporary

Sales rates quickly improved after mortgage rates settled following an initial hike in the aftermath of the mini-budget

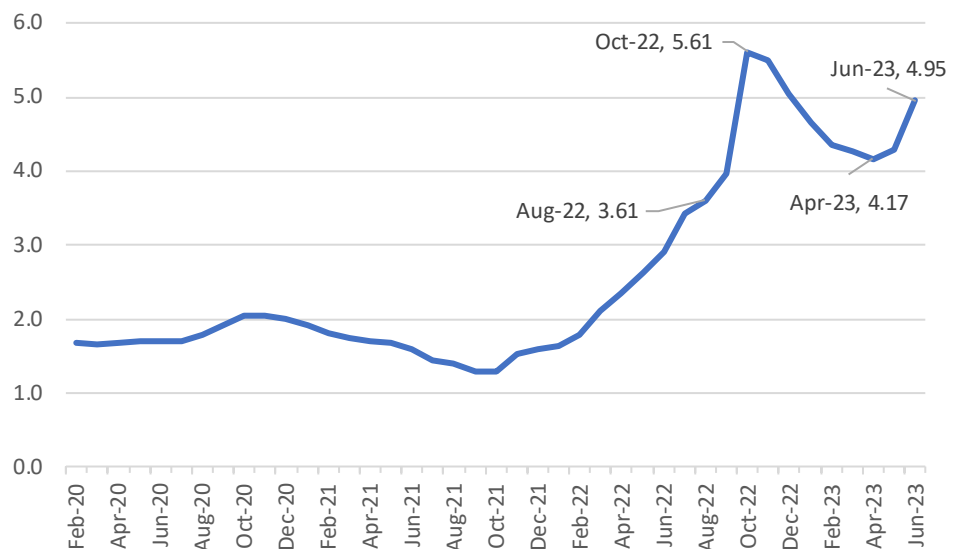
Private housing: how temporary a slowdown?

We believe that housing market activity is less dependent on the absolute level of interest rates, *per se*, than the perceived direction of travel. It has been widely acknowledged by housebuilders, estate agents and other commentators that there was a sudden slowdown in the availability of mortgages and buyer demand following the 23 September mini-budget, which saw a large number of fixed rate loans – now the most popular mortgage products – withdrawn and repriced upwards. This led to the rate on 75% LTV rising from 3.61% immediately prior to then-Chancellor Kwasi Kwarteng’s ill-fated statement to 5.61% in October, according to the [Bank of England](#). By the time rates began retreating again, it was the run-up to Christmas – when the housing market traditionally slows down.

However, most housebuilders’ statements from around the turn of the year referred to progressively improving sales rates (but not meaningful house price reductions), as fixed rate deals began to become cheaper – driven by falling two- and five-year swap rates, as well as competition between lenders. This lasted for about four months. The latest weakness in demand followed the higher-than-expected core inflation data in the last two sets of government inflation data and subsequent 50bp increase in the Official Bank Rate.

The Bank of England data (Figure 1) is published monthly. Rightmove provides [weekly data](#) on a range of fixed-rate deals. The latest shows average rates displaying some signs of flattening out: the 90% LTV product rose by only 1bp to 5.81%, following a 13bp rise the week before; rates for 85% loans edged up by 4bps to 5.69% after a preceding 15bp rise. Rightmove also highlights the degree of competition among lenders, evident in the spread between average and lowest rates – 32bps below the averages for both 85% and 90% LTVs.

Figure 1: Average fixed-rate mortgage interest, 5-years, 75% LTV (%)



Source: Bank of England

Results announcement in September should provide greater insight into the market post-holidays

Scottish Government increases the prices it will pay for affordable homes, to stimulate building programmes

First dedicated Scottish housing minister welcomed as having 'worked collaboratively' with housing industry

Housebuilders south of the border report demand among investors for PRS assets

More clarity in September?

With the obvious caveat that a further reversal in mortgage rates will largely depend on more favourable inflation data, we would not be surprised if the current market weakness lasts around three to six months from the turnaround point in April. If so, there could be sufficient evidence – including the period after the summer holidays when traditionally the market picks up again – when Springfield announces its FY23 results in late September. The key question from Springfield's private housing perspective is how long this hiatus – if that is what it is – will have lasted. The risks on our current estimates for the division are presumably on the downside, particularly H1 to November, but to what extent will be a factor of the length of the market pause. A lengthy slowdown, however, could build up a backlog of demand, which could support a rebound in FY25E. (We intend to introduce FY25E estimates with the results announcement.)

Affordable housing: a more positive stance from government

One more positive factor highlighted in the trading update is that the Scottish Government has increased its affordable housing investment benchmarks, the level of grant available to support delivery of new social rented homes, by 16.9%. This was considered necessary to meet the government's affordable housing targets. Cost inflation on a small number of fixed-price contracts entered into in the immediate aftermath of lockdowns reduced profitability in the division. As a result, Springfield adopted a cautious approach to entering into further new long-term affordable housing contracts, which it has maintained since year-end. All of the historic contracts are expected to be completed by later this year.

With a more pragmatic approach to costing by the Scottish Government and high demand for affordable housing, we believe there could be scope for affordable housing division results to partly mitigate any temporary weakness in private housing we have referenced.

PRS: Investor appetite poised for return?

Another important factor is the current 3% pa cap on public and private rents. The Scottish Government imposed a six-month freeze from September 2022 to March 2023, in light of cost-of-living pressures. It replaced this with the 3% ceiling until September 2023. The initial rent freeze led to Springfield's partner Sigma Capital suspending its PRS agreement with the housebuilder (page 8). In April, the Holyrood administration appointed Paul McLennan as its first dedicated minister for housing since 2021, who is viewed as being 'collaborative' by the Chartered Institute of Building.

Barratt, Gleeson and other housebuilders south of the border have recently announced bulk sales of parts of their pipelines to institutional PRS investors. We anticipate a recovery in PRS activities with Sigma as investors adjust to the current policy, allowing a degree of 'de-risking' and debt reduction.

Figure 2: Revenue by division

Year-end May (£m)	2019	2020	2021	2022	2023E	2024E
Private Housing						
Completions	630	419	559	712	860	870
YoY change (%)	37.0%	-33.5%	33.4%	27.4%	20.8%	1.2%
ASP (£000)	227.0	236.0	248.0	245.0	294.2	275.7
YoY change (%)	2.5%	4.0%	5.1%	-1.2%	20.1%	-6.3%
Revenue	143.3	98.9	138.6	174.4	253.1	240.0
Affordable Housing						
Completions	322	308	363	405	330	250
YoY change (%)	3.9%	-4.3%	17.9%	11.6%	-18.5%	-24.3%
ASP (£000)	133.0	138.0	145.8	158.6	165.1	164.0
YoY change (%)	10.6%	3.8%	5.7%	8.8%	4.1%	-0.7%
Revenue	42.9	42.5	52.9	64.3	54.5	41.0
Contracting						
Completions			51	125	120	35
YoY change (%)				145.1%	-4.0%	-70.8%
ASP (£000)			159.6	132.0	162.3	142.3
YoY change (%)				-17.3%	23.0%	-12.3%
Revenue		-	8.1	16.5	19.5	5.0
Total completions	952	727	973	1,242	1,310	1,155
YoY change (%)	23.6%	-23.6%	33.8%	27.6%	5.5%	-11.8%
Total ASP (£000)	195.6	194.5	205.3	205.5	249.6	247.5
YoY change (%)	8.2%	-0.5%	5.5%	0.1%	21.5%	-0.9%
Other revenue	4.6	2.1	17.0	1.9	5.5	5.0
Total revenue	190.8	143.5	216.7	257.1	332.6	290.9
YoY change (%)	35.6%	-24.8%	51.0%	18.6%	29.4%	-12.5%

Source: Company Information and Progressive Equity Research estimates.

Figure 3: Profit and per share summary

Year-end May (£m)	2019	2020	2021	2022	2023E	2024E
Total revenue	190.8	143.5	216.7	257.1	332.6	290.9
Gross profit	34.3	27.4	38.8	43.1	49.0	53.5
Admin, other income	(17.3)	(16.1)	(19.0)	(20.6)	(27.5)	(29.5)
Share in PBT of JV	0.6	0.9	-	-	-	-
Total op profit	17.6	12.1	19.8	22.6	21.5	24.0
Exceptionals	(0.6)	(0.4)	(0.6)	(1.1)	(0.7)	-
Net interest	(1.1)	(2.0)	(1.2)	(1.8)	(4.7)	(3.8)
PBT, reported	16.0	9.7	17.9	19.7	16.1	20.2
<i>U-lying tax rate (%)</i>	<i>18.8</i>	<i>20.6</i>	<i>22.6</i>	<i>18.2</i>	<i>19.0</i>	<i>25.0</i>
Reported tax	(3.1)	(2.1)	(4.2)	(3.652)	(3.0)	(5.1)
Net attrib. profit	12.8	7.6	13.7	16.1	13.0	15.2
Adj PBT	16.5	10.2	18.5	20.8	16.8	20.2
Wtd. ave (million)	96.3	96.9	99.4	109.0	118.5	118.5
Diluted (million)	97.3	97.9	101.2	111.8	121.3	121.3
EPS, basic (p)	13.34	7.89	13.79	14.74	10.98	12.81
Adj EPS, (p)	13.92	8.34	14.41	15.63	11.45	12.81
Adj EPS, dil. (p)	13.79	8.25	14.16	15.24	11.19	12.51
DPS - declared (p)	4.4	2.0	5.75	6.2	3.1	5.1
Dividend cover (x)	3.2	4.2	2.5	2.5	3.7	2.5
NAV (p)	91.9	98.0	109.0	121.2	127.4	135.4
TNAV (p)	90.2	96.3	107.4	116.3	122.6	130.6

Source: Company Information and Progressive Equity Research estimates.

Figure 4: Cashflow and balance sheet

Year-end May (£m)	2019	2020	2021	2022	2023E	2024E
Adjusted cash flow statement						
Group op profit inc exc.	16.5	10.8	19.1	21.5	20.8	24.0
Depreciation	1.6	2.4	2.2	1.7	2.0	2.0
Intangible amortisation	-	0.0	-	-	-	-
Other	0.6	2.4	0.5	12.4	-	-
Working capital changes	(2.7)	(42.2)	35.2	(16.5)	(17.0)	19.5
Operating cash flow	16.0	(26.6)	57.0	19.1	5.8	45.5
Capex	(1.2)	(0.5)	0.0	(0.1)	(0.2)	(0.1)
Interest	(1.2)	(1.6)	(1.3)	(1.6)	(4.7)	(3.8)
Tax	(2.9)	(3.1)	(4.2)	(3.5)	(3.0)	(5.1)
Free cashflow	10.7	(31.8)	51.5	13.8	(2.2)	36.5
Acquisitions, net	(20.9)	(3.2)	0.3	(44.0)	(22.2)	(14.2)
Dividends - paid	(3.8)	(3.1)	(3.3)	(6.3)	(5.6)	(5.7)
Financing	4.9	36.5	(34.2)	37.1	-	-
Chg cash/net cash, f-cast	(9.0)	(1.5)	14.3	0.6	(29.9)	16.6
Summary balance sheet						
Intangible fixed assets	1.6	1.6	1.6	5.8	5.8	5.8
Tangible fixed assets	5.0	6.3	4.5	5.8	4.0	2.1
Investments	2.4	5.3	6.0	8.3	8.3	8.3
Working capital	125.1	162.8	128.8	182.9	204.9	180.4
Provisions, others	(16.0)	(9.3)	(8.9)	(21.2)	1.0	15.2
Net cash/(debt) – IFRS16	(29.6)	(70.9)	(20.8)	(38.1)	(68.0)	(51.3)
Net assets	88.6	95.9	111.2	143.5	151.0	160.5
<i>Net debt – pre IFRS16</i>			(18.2)	(34.1)	(63.0) ¹	(46.3) ¹

Source: Company Information and Progressive Equity Research estimates. ¹ £5m of lease liabilities, including the electric car fleet

Scottish market underpinned by long-term growth prospects and a distinctive home-buying model. Springfield offers a differentiated and lower-risk model

Springfield in brief: distinctive model in growth market

Springfield was transformed into a housebuilder by current chairman Sandy Adam in the 1990s and it was admitted to AIM in October 2017. We continue to believe that economic and political dynamics are likely to support growth in housebuilding volumes and prices in Scotland, where values have lagged most of the UK. In our view, Springfield benefits from a distinctive business model, and we believe strategically important acquisitions and expansion of innovative multi-tenure rental partnerships since floating are supportive of a return to growth. See our [Springfield research section](#) on Progressive's website.

- **Long term, a more attractive market?** While there are challenges across the UK housing market, we remain upbeat on Scottish opportunities. Scotland lags England in the proportion of homes owned privately and the Scottish Government has pledged to build 110,000 affordable homes by 2031-32, with almost £3.5bn earmarked through to March 2026. House prices in Scotland are more affordable in relation to household incomes than in any other region of the UK's mainland.
- **Scottish missive system.** With buyers legally bound much earlier than in England and Wales, the missive system offers high revenue visibility and a secure income stream.
- **A distinctive model.** Springfield has a differentiated business model that focuses on two differing markets, both of which have high demand and, arguably, a lower risk profile: family housing and affordable housing (the latter is provided both as part of planning requirements in the private housing division as well as in its own right in the affordable housing division). The group buys land mainly 'off market' at more attractive prices than in the mainstream market, preferring more complex long-term projects, demonstrated particularly in its Village sites.
- **Distinctive Village communities.** A cornerstone of Springfield's strategy is its focus on its mid-sized Village communities. All of these are set in a rural context but close to fast-growing cities, located in Dundee, Perth, Stirling, Livingston and Elgin. A factor in Springfield's success in securing these sites has been its close co-operation with local councils and other stakeholders; a key differentiator for the group, in our view.
- **Smart deals.** Mactaggart & Mickel was Springfield's fifth strategic acquisition and continues its record of regional expansion in Scotland with, in our view, innovative deal structures allowing payment as homes are sold. Tulloch, in December 2021, strengthened the group's presence in the Highlands. This followed Dawn Homes in 2018 in the West of Scotland, while Walker Group in 2019 focused on popular commuter areas around Edinburgh, with higher-priced homes and stronger gross margins than Springfield's then-existing private housing division. The 2011 acquisition of Redrow's Scottish business took Springfield into central Scotland, a step change for revenue.
- **Private rental initiative.** In early 2021, Springfield commenced its first PRS development with specialist Sigma Capital. The site, for 75 family homes at Bertha Park, will be the first development of single-family homes for the private rented sector in Scotland. A number of existing Springfield sites, primarily in its Village developments, have been identified as potential sites for PRS development when the market returns.
- **Evolving ESG credentials.** Springfield has had a longstanding commitment to ESG, recognised in recent top industry awards (see our [note](#)). The group published its first ESG Strategy alongside its annual results in September 2022. The strategy includes setting a route map for net zero by at least 2045 and objectives to further evolve solutions in energy saving, biodiversity, water management and waste reduction. On the social side, the group has an active training programme for employees and strong engagement with local communities. Timber-frame has a lower carbon footprint than traditional construction and a second factory reduces road miles.

Financial Summary: Springfield Properties

Year end: May (£m unless shown)

	2020	2021	2022	2023E	2024E
PROFIT & LOSS					
Revenue	143.5	216.7	257.1	332.6	290.9
Adj EBITDA	13.6	21.9	24.3	23.5	26.0
Adj EBIT	12.1	19.8	22.6	21.5	24.0
Reported PBT	9.7	17.9	19.7	16.1	20.2
Fully Adj PBT	10.2	18.5	20.8	16.8	20.2
NOPAT	8.9	15.3	18.5	17.4	18.0
Reported EPS (p)	7.9	13.8	14.7	11.0	12.8
Fully Adj EPS (p)	8.2	14.2	15.2	11.2	12.5
Dividend per share (p)	2.0	5.8	6.2	3.1	5.1
CASH FLOW & BALANCE SHEET					
Operating cash flow	(26.6)	57.0	19.1	5.8	45.5
Free Cash flow	(31.8)	51.5	13.8	(2.2)	36.5
FCF per share (p)	(32.8)	51.8	12.7	(1.8)	30.8
Acquisitions	(3.2)	0.3	(44.0)	(22.2)	(14.2)
Disposals					
Net cash flow	(1.5)	14.3	0.6	(29.9)	16.6
Overdrafts / borrowings	72.4	36.6	54.4		
Cash & equivalents	1.5	15.8	16.4		
Net (Debt)/Cash, post-IFRS 16	(70.9)	(20.8)	(38.1)	(68.0)	(51.3)
Net (Debt)/Cash, pre-IFRS 16		(18.2)	(34.1)	(63.0)	(46.3)
NAV AND RETURNS					
Net asset value	95.9	111.2	143.5	151.0	160.5
NAV/share (p)	98.0	109.0	121.2	127.4	135.4
Net Tangible Asset Value	94.2	109.6	137.8	145.2	154.7
NTAV/share (p)	96.3	107.4	116.3	122.6	130.6
Average equity	83.8	92.2	103.5	127.4	147.2
Post-tax ROE (%)	9.1%	14.9%	15.5%	10.2%	10.3%
METRICS					
Revenue growth		51.0%	18.6%	29.4%	(12.5%)
Adj EBITDA growth		60.9%	10.9%	(3.5%)	11.0%
Adj EBIT growth		63.1%	14.3%	(5.0%)	12.0%
Adj PBT growth		82.1%	12.5%	(19.6%)	20.8%
Adj EPS growth			7.6%	(26.6%)	11.8%
Dividend growth		187.5%	7.8%	(50.0%)	64.5%
Adj EBIT margins	8.4%	9.1%	8.8%	6.5%	8.3%
VALUATION					
EV/Sales (x)	1.0	0.6	0.5	0.4	0.5
EV/EBITDA (x)	10.2	6.4	5.7	5.9	5.4
PER (x)		4.6	4.2	5.8	5.2
Dividend yield (%)	3.1%	8.9%	9.6%	4.8%	7.9%
P/NAV (x)		0.59	0.53	0.51	0.48
FCF yield		80.3%	19.6%	(2.8%)	47.8%

Source: Company information and Progressive Equity Research estimates

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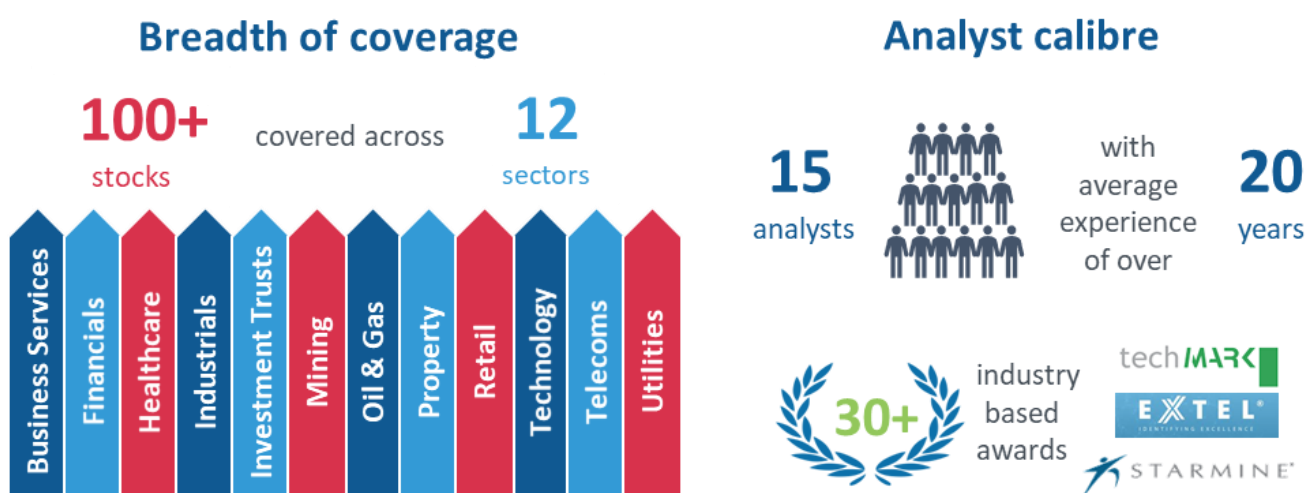
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