Stock Market Review

Crimsonwing plc aims for strong turnaround this year

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The March 2012 full-year financial statements published last week by Crimsonwing plc point to another disappointing result as the IT services group registered a loss of €0.53 million despite a six per cent growth in revenues to €15.2 million.

Crimsonwing has been in an overall loss-making position for the past four consecutive years as the challenging conditions in the aftermath of the international financial crisis in late 2008 and early 2009, coupled with the significant decline in the value of sterling until December 2008, negatively impacted Crimsonwing's performance. This was also accentuated by the dismal track record of the Netherlands-based VDA business which was acquired in 2008.

For the second consecutive year, all business units within the Crimsonwing Group were profitable but the sharp losses at VDA pushed the entire group into a loss-making situation. During the 12-month period to March 31, the VDA business in the Netherlands suffered a loss of €0.77 million following a similar result in the previous financial year.

Crimsonwing's chief executive David Walsh took direct responsibility for the significant restructuring necessary in the Netherlands and this involved some substantial costs to downsize the number of employees. After what the CEO had described as a "perfect storm" in the Netherlands and a frustratingly long process to carry out the necessary measures,

Mr Walsh confirmed at a meeting last week that the headcount at VDA has been reduced from 27 to 12 employees. The company also managed to negotiate a significant reduction in rent of its office premises as part of a new five-year lease agreement starting from July 1.

The CEO explained that the full benefits of the restructuring process will show up in the current financial year to March 31, 2013. The substantial cost savings which started to materialise from the start of the new financial year on April 1 is expected to be the main factor behind the turnaround across the entire group which is anticipated this year. The CEO noted that the financial performance during the first quarter of the year confirms this trend.

In a separate announcement last week to the publication of the March 2012 annual report, Crimsonwing also issued its interim directors' statement. During the first quarter of its new financial year between April 1 and June 30, group revenues grew by 14 per cent to €4.3 million. More importantly, the EBITDA generation jumped to €395,000 compared to €164,000 in the same period last year.

Apart from the significant losses incurred in the Netherlands business, Crimsonwing Group's performance during the past financial year was also impacted by costs which were booked during the year, mainly relating to two significant bids in which the company was involved.

In this respect, on February 16, Crimsonwing had reported that they were selected as a strategic partner by an international retailer for a global e-commerce rollout across several countries.

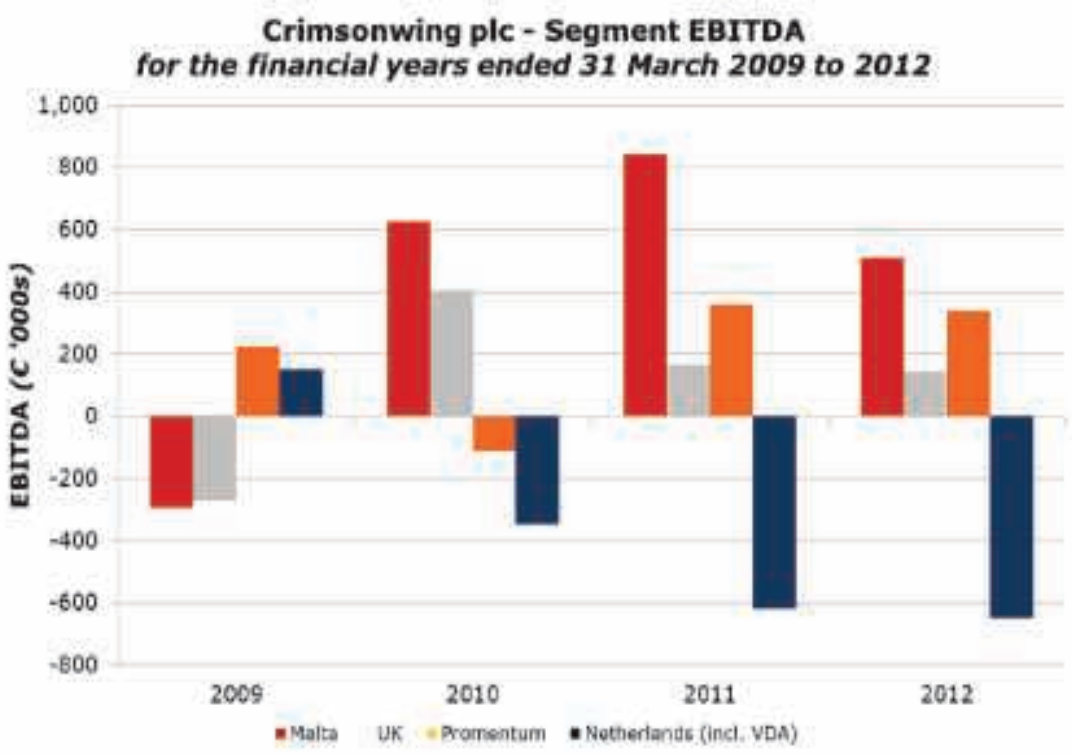
The CEO noted that the project initially includes the implementation of 35 e-commerce solutions for various franchisees in different parts of the world and this could potentially rise to a maximum of 110 solutions over time. Mr Walsh indicated that a one-time payment is to be received upon implementation of each e-commerce platform, with annual revenue to cover 24x7 support services.

Meanwhile, despite the substantial work and costs involved in the bidding process by some of Crimsonwing's executives, the decision on the other large-scale tender has been delayed until December.

Crimsonwing's CEO explained last week that the turnaround for the group this year is not only expected to materialise following the restructuring at the VDA business and the non-occurrence of some one-off costs, but also from some new long-term major contracts which will start having a positive benefit from September.

Apart from the global e-commerce rollout, Crimsonwing was successfully awarded two other material contracts and some preliminary details of these new contracts were provided to the financial community at last week's meeting.

However, the official press releases by Crimsonwing's large multinational clients are expected to be issued over the coming months.



The CEO also provided an update on the pending acquisition of the minority shareholding in Promentum, the other Netherlands-based business. This had been formally communicated to the market last May confirming that Crimsonwing will be acquiring the 49 per cent shareholding which it currently does not hold. The acquisition will be partly financed through the allotment of 2.94 million new Crimsonwing shares to the minority shareholders of Promentum. Before this announcement, Crimsonwing's share price had sunk to an all-time low of €0.16 per share.

> **Crimsonwing needs to make every effort to provide frequent guidance to the market on progress being achieved this year and any new contracts being awarded**

However, the news that the additional shares to be issued to the minority shareholders of Promentum will be at a price of €0.30 per share had helped the equity recovery strongly to this level immediately following the announcement.

The acquisition of a shareholding in a company through the issuance of additional shares had also been adopted by Island Hotels Group Holdings plc and 6pm Holdings plc in recent years.

Mr Walsh revealed that a circular to all shareholders explaining the transaction is being finalised and will shortly be mailed to shareholders ahead of the annual general meeting scheduled for October 17.

In last year's annual report (March 2011), Crimsonwing had indicated that its aim was to achieve an overall turnover level of €20 million which is an important benchmark in the IT industry. At last week's meeting, Mr Walsh again confirmed this objective and revealed that the forecasted revenue during the current year to March 2013 should push the group closer towards this figure.

Apart from the top-line growth, the CEO noted that following the restructuring at the VDA business and the new long-term contracts awarded to the group, the focus is now on achieving an overall profitable situation similar to the situation in 2008 and prior years. Interestingly, the last profitable full-year for Crimsonwing was that for the period ended March 31, 2008, when a profit of €800,000 was registered.

The full-year financial statements published by Crimsonwing last week also made reference to some valuation multiples used in testing the impairment of the Promentum business in the Netherlands.

It was stated that this impairment assessment was based on a price-to-sales ratio of between one to 1.2 times and a price/earnings multiple of 15 times, which they claim to be the industry norm for valuations of IT software companies.

Currently, it would be incorrect to use the price to earnings multiple as a valuation metric for Crimsonwing since it suffered a loss in the last financial year and the company has as yet not issued an official forecast for the current financial year. The p/e multiple of 15 times could instead be an interesting benchmark for the other IT companies listed on the local exchange.

In order to ensure continuing shareholder loyalty after four very disappointing years, Crimsonwing needs to make every effort to provide frequent guidance to the market on progress being achieved this year and any new contracts being awarded. It would also need to return to a meaningful profitable situation this year to maintain such loyalty from the market.

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