EDISON

QuickView

Solid State

Acquisition of Pacer Technologies

Solid State has announced the acquisition of Pacer Technologies, a value-added distributor of opto-electronic components and displays, for c £3.7m cash. Although the transaction is earnings enhancing, triggering a 4.0% uplift in the FY20 consensus EPS, the share price has not moved materially in response to the news and we believe the shares continue to trade at a significant discount to peers.

Highly complementary to existing business

Pacer is headquartered near Reading, UK with a satellite sales office in Florida, providing a base from which the group can address the US market. Pacer's Weymouth operation, which is where its design capability is centred, includes a small Class 100 cleanroom where opto-electronic sub-systems are currently assembled, potentially extending the value-added offer provided by the rest of the group, in our view. Pacer was founded in 1989 and has expanded its portfolio from photonics-based components to include displays, sensors, LEDs and a wide range of other light-based components and systems. Like Solid State's value-added distribution division, Pacer's offer is based on a highly informed technical sale. If an off-the-shelf solution does not exist, Pacer will design and build a tailor-made one, which is similar in philosophy to Solid State's manufacturing division. Around 40% of Pacer's revenues are derived from exports.

Immediately earnings enhancing

Pacer reported £15.2m revenues for the year ended March 2018 and £0.4m profit before tax. Net debt, which will be assumed by Solid State, totalled £1.5m at the end of March 2018. The c £3.7m consideration is primarily being settled through £6.0m new term loans, payable over three years. The group has also put a £3.5m revolving credit facility in place to cover increased working capital requirements. Consensus estimates model incremental revenues and profits from the transaction at the levels reported for the year ended March 2018, giving scope for upgrades as the integration of the new operation progresses.

Valuation: Trading at a discount to peers

Solid State's share price has not moved materially in response to the news of the transaction. At current levels, the shares continue to trade on prospective consensus P/E multiples that are at a discount to the mean for both our sample of specialist manufacturing companies (11.5x for Solid State vs 17.9x for peers) and our sample of value-added distributors (11.5x vs 18.3x). This indicates there is potential for share price upside, especially if the earnings upgrade potential of this transaction is realised.

Consensus estimates

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
03/17	40.0	3.1	31.4	12.0	10.1	3.8
03/18	46.3	3.0	30.9	12.0	10.3	3.8
03/19e	53.2	2.7	27.7	12.0	11.5	3.8
03/20e	65.0	2.9	28.5	12.1	11.2	3.8

Source: Company data, broker consensus. Note: *Adjusted for exceptionals, share-based payments and amortisation of acquisition intangibles.

Technology

13 November 2018

Price	**318p**
Market cap	**£27m**

Share price graph

Share details

Code	SOLI
Listing	AIM
Shares in issue	8.5m

Business description

Solid State is a high value-add manufacturer and specialist design-in distributor to the electronics industry. It has expertise in industrial/ruggedised computers, electronic components, antennas, microwave systems, secure communications systems and battery power solutions.

Bull

- Pacer's opto-electronics and display portfolio adds to the range offered by Solid State's value-added distribution business with little overlap.
- Increased scale should enable the Distribution division to attract higher value franchises.
- Acquisition substantially strengthens group presence in medical vertical.

Bear

- Pacer's US operation is still very small.
- Outgoing management had invested for growth over next three years, so Pacer's EBIT margin is low even though gross margin is higher than Solid State's Distribution division.
- Interest on new loan to fund transaction a drag on profits.

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