

Sigma Capital Group

Corporate outlook

Ready to deliver large-scale residential projects

Real estate

Fully re-focused on its property activities, Sigma's plans for the roll-out of large-scale residential schemes in the private rented sector (PRS) have made important steps forward. Funding for the Gatehouse joint venture is complete, allowing construction of the first phase of 927 homes to begin. A partnership with Grainger plc has also been announced, granting Grainger first option on development opportunities on 100 or more PRS units. Sigma's value resides, largely off balance sheet, in its access to a pipeline of urban regeneration projects via the current local authority JVs. With an estimated c £2bn gross development cost, these projects should be capable of delivering c £60m of revenues to Sigma, accelerated by PRS, which provides its investors with income and capital growth opportunities.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/12	2.3	(0.3)	(0.7)	0.0	N/A	N/A
12/13**	5.8	(0.5)	(1.0)	0.0	N/A	N/A
12/14e**	3.9	0.0	0.1	0.0	N/A	N/A
12/15e	4.3	1.1	1.5	0.0	41.7	N/A

Note: *PBT and EPS are normalised, excluding intangible amortisation, exceptional items and share-based payments. **2013 and 2014 revenues are inflated by development revenues of £3.7m and £0.6m respectively with largely offsetting costs.

Gatehouse (phase 1) and Grainger to begin PRS

PRS is designed to satisfy investor interest in large-scale private rented sector residential portfolios, and accelerate the development of land controlled by Sigma. The first phase of the Gatehouse JV covering 927 PRS units is now underway. Additional phases may increase this to 6,600 homes with a delivery cost value of c £700m. Grainger plc has agreed an option with Sigma for delivering development opportunities on "100 or more PRS units". Given Grainger's existing c 9,000 unit UK portfolio, we have assumed it will be more and have modelled 250.

PRS regeneration should unlock value

PRS has the potential to transform Sigma's reported financial results and boost the share of recurring asset management fee income. In return for making land available at attractive prices, local authorities should be able to increase council tax receipts and meet local housing needs faster. Sigma's existing relationships have capacity to support c 12,000 new homes, but Sigma is seeking additional local authority deals and private sector transactions that would add further capacity and increase the geographical diversification of its land sites.

Valuation: Value is off balance sheet

We estimate the net present value of Gatehouse phase 1 at 6.6p per share; at completion, the Gatehouse JV could be six or seven times larger than this, and all PRS perhaps 12x larger. In addition to a value for Sigma's existing land access, we believe investors will continue to award Sigma a goodwill premium to reflect the likely future access to additional land assets via new local authority ventures and private sector transactions.

17 December 2014

Price **62.5p**
Market cap **£38m**

Net cash (£m) as at 30 June 2014	9.2
Shares in issue	60.5m
Free float	56%
Code	SGM
Primary exchange	AIM
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	1.6	(8.8)	57.2
Rel (local)	6.1	(3.1)	61.2
52-week high/low		91.0p	39.2p

Business description

Sigma Capital Group and its subsidiaries are focused on urban regeneration, property asset management, property finance and property development.

Next event

2014 results Est. March 2015

Analyst

Martyn King +44 (0)20 3077 5745

financials@edisongroup.com

[Edison profile page](#)

Investment summary

Urban regeneration specialist

Now wholly focused on its urban regeneration, property asset management, property finance and property development activities, Sigma's plans for the roll-out of large-scale residential schemes for the private rented sector (PRS) have made important steps forward. Funding for the Gatehouse joint venture has been completed, allowing construction to start on the first phase of 927 PRS units. A partnership with Grainger plc has also been announced, granting Grainger first option on development opportunities for 100 or more PRS units (we assume more and have modelled 250). Sigma controls land that could support up to 12,000 PRS units in total.

Valuation: PRS should unlock value

Even when adjusted for discontinued venture capital activities and the impact of the now exited associated investments, we feel the historic profit and loss account and balance sheet of Sigma are a poor guide to the value of the business. Using the reported earnings and net assets, at 62.5p Sigma is trading on c 42x our estimate of normalised earnings for 2015 and 3.6x fully diluted NAV per share. Although cash positive we have not assumed dividend payments in 2015 or 2016. The real value of Sigma resides, largely off balance sheet, in its access to a pipeline of urban regeneration projects via the current local authority JVs, which Sigma estimates to have a gross development cost (GDC) of c £2bn. On a flat cost base, this should be capable of generating an average of £3m pa in operating profit on a 10-year basis. PRS provides a route to unlocking this latent value faster. We estimate the net present value of Gatehouse phase 1 at 6.6p per share; at completion, the Gatehouse JV could be six to seven times larger than this, with existing access to land for total PRS of up to 12x larger. In addition to a value for Sigma's existing land access, we believe investors will continue to award Sigma a goodwill premium to reflect the likely future access to additional land assets via new local authority ventures and private sector transactions.

Financials: PRS making a significant impact

We have used the completion of the Gatehouse phase 1 funding and the announced partnership with Grainger plc to update our reported earnings forecasts. We have been awaiting these developments to do so, given their significant impact on Sigma's near-term reported financials. As has been apparent for some time, the prolonged preparatory work on PRS has slightly negatively affected 2014e (pre-PRS) revenues and costs. We now see 2014 as being essentially break-even, including £1.0m of transaction fees from Gatehouse phase 1. We have introduced a 2015 estimate for the first time, which sees Gatehouse phase 1 contributing development fees and the Grainger partnership adding sourcing and development management fees. Our preliminary estimate published in Edison Insight on 28 November 2014 made the assumption of development opportunities for 500 units being taken up under the Grainger partnership in 2015. On reflection, we are more conservatively assuming 250 units in 2015 as the partnership becomes established. This deferral of revenue potential (for future Grainger or other PRS deliveries) brings us to a 2015 revenue forecast of £4.3m (preliminary £4.9m) and normalised PBT of £1.1m (preliminary £1.7m).

Sensitivities

- The detail and timing of urban regeneration schemes is uncertain.
- Despite mitigating actions, there are residual risks associated with development work.
- Estimates and prospects are closely linked with the successful roll-out of PRS.
- Despite a critical shortage of homes in many parts of the UK, the residential housing market is likely to remain cyclical.

Fully focused on property

Sigma Capital Group is today wholly focused on urban regeneration, property asset management, property finance and property development. Historic venture capital fund management activities have been exited and Sigma no longer has any investment in the former associate Frontier IP Group plc.

Urban regeneration

Property regeneration activities are mainly carried out through the Sigma Inpartnership subsidiary, which was acquired in August 2011. This brought three long-term partnerships into the group, each between 10 and 20 years' duration, with Liverpool City Council, Salford City Council and Solihull Metropolitan Borough Council. The partnerships hold long-term option arrangements with each of the local authorities for delivering a mix of residential, commercial, health and education projects. Each council has injected land assets into its respective partnership, with Sigma retained as development manager, rewarded as it progresses each project from inception through planning and finance, to delivery of completed developments. The entire programme has an estimated GDC of c £2bn.

Property management

Two property subsidiaries, Sigma Capital Property Ltd (SCP) and Sigma Property Asset Management Ltd (SPAM), pre-date the Inpartnership acquisition. SCP is responsible for most of the group's property management activities that fall outside of its local authority relationships. This has until recently included the management contract with Regenco Trading Ltd (a developer and major land owner) for the management of a large mixed-use development at Winchburgh, 11 miles west of Edinburgh City Centre. This contract ended on 1 October 2014, allowing Sigma to concentrate on large-scale residential (see below) and regeneration activities in England. Sigma received a £0.13m termination payment from Regenco.

The SPAM subsidiary acts as property manager for the last remaining of the group's historical property limited partnerships, Si Limited Partnership No. 7. In 2010, SPAM stepped in to provide development management services to oversee the completion of a major mixed-use development scheme following the insolvency of the original developer. Since completion, SPAM has continued to provide asset management services. Sigma has a 19.3% holding in Si Limited Partnership No. 7, which has been written down to zero since 2009.

Property finance

Since consolidating Inpartnership into the group, management has been focused on the creation and delivery of a new funding model, capable of providing substantial financing for the roll out of large-scale portfolios of rental homes in the UK. The model has the potential to greatly accelerate the development of the existing local authority partnership land bank (likely to be supplemented by additional local authority partnerships as well as private sector land site acquisition), while tapping into corporate and growing institutional interest in large, diversified residential investment portfolios as a source of low-volatility income. An important milestone in the delivery of this PRS portfolio model was reached in November 2013 with an agreement of a joint venture with Gatehouse Bank plc for the phased roll-out, over a number of years, of nearly 7,000 new rental homes. At completion this would represent one of the largest single new-build residential portfolios in the UK. Following protracted negotiations regarding the debt funding of the joint venture (Gatehouse is providing the equity), the first phase of development (the first 927 homes) is now underway.

Alongside the Gatehouse transaction, Sigma has signed an agreement with Grainger plc that grants Grainger first option over residential development opportunities controlled by Sigma that

would provide an initial 100 (or more) PRS units across the country (given Grainger's scale, we assume 250).

Strategic priorities

The roll-out of the PRS model is a key element in both determining and delivering on management's key strategic priority of growing income ahead of costs. The existing strong relationships with local authority partners and the track record in urban regeneration that Sigma has already built provided the necessary support for the launch of PRS. By providing access to funding this should accelerate the delivery of residential regeneration developments (good news for the local authority partners) as well as the emergence of income to Sigma (including recurring fee income) from the land that is already under its control. The group seeks to broaden the geographic footprint of its local authority partnerships (probably supplemented by private sector land acquisition) and also hopes to be able to extend the PRS model to other tenures such as social housing.

Management and governance

Sigma has an experienced and stable senior management team with considerable experience in all aspects of commercial and residential investment, development and finance. CEO Graham Barnet co-founded Sigma in 1997. He has a professional background in corporate finance and significant personal experience in commercial and residential property development and investment. COO Graeme Hogg has more than 25 years' experience in the property and property finance sector, with commercial and residential property development experience. He co-founded Inpartnership (with Regeneration Director Duncan Sutherland) in late 2000, before its acquisition by Sigma in 2011, and was instrumental in the creation of the three local authority partnerships at the core of Sigma's operations. Brief biographies can be found on page 12.

In all, there are eight members of the board, of whom two are non-executive. The non-executive directors, including chairman David Sigsworth, are members of the remuneration committee and the audit committee. Although Sigma is not required to do so, within the practical confines of being a small company it seeks to act in accordance with the principles of the code of best practice contained in the UK Corporate Governance Code.

Henderson Global Investors is the largest of a number of institutional shareholders, with 16.9% (summary on page 12). Management and other directors also have a significant interest in the company, aligning their interests with third-party shareholders. As at 31 December 2013 (detailed in the 2013 annual report) this was c 23%, in aggregate, of the outstanding shares at the time. CEO Graham Barnet is the largest of these with a current shareholding of 12.4%. The percentage of shares not in public hands as of 2 December 2014 is 45.0%.

Local authority partnerships are key

The August 2011 acquisition of Inpartnership brought three long-term local authority partnerships into the group. Sigma's plans for the roll-out of large-scale private rented sector developments (PRS) are based on these partnerships.

Inpartnership was founded in 2000 to create long-term, asset-backed partnerships with the public sector. The partnerships provide for delivery of around 12,000 houses, retail and health/medical centres, schools and a mix of retail/leisure facilities. The total development value of opportunities within these three partnerships is more than £2bn over the next 10-15 years. To date, Sigma has earned project management fees with performance fees based on the final development profit.

Numerous schemes and projects are currently underway and we see these continuing. However, PRS promises to significantly increase the scale and pace of progress.

The shortage of private rental accommodation is critical

Much of the country faces a critical shortage of homes. Successive governments have failed to ensure that sufficient homes have been built to meet a growing need and the situation was exacerbated by the global financial crisis. The post-crisis further slowdown in housing construction and a tightening of mortgage availability have contributed to a strong demand for rental accommodation. With renting directly from local authorities in decline, there has been a sharp increase in the size of the private rented sector (to c 16.5% of all households according to the UK government). But supply has not kept pace with demand and the common picture is of multiple applicants chasing available space. The problem is not confined to London.

The government wants to encourage the private rental sector, which contributes greatly to labour mobility, and meets a wide range of housing needs by providing flexible tenure. It believes the best way to make rents more affordable is to increase supply and has sponsored a number of initiatives to this effect.

There are measures aimed at generally stimulating the supply of new homes and measures directly targeted at the private rental sector. Builders, investors and local councils are all being encouraged to increase the supply of new homes by removing unnecessarily complex regulations and selectively providing financial support. The New Homes Bonus provides grant aid to local councils based on the amount of additional council tax raised by building new homes. Debt guarantees and equity support are also available for private rental investment. There are policies being considered that will seek to raise the standard of private sector rental accommodation, provide for longer tenancies and reduce the hidden costs of renting.

The PRS model provides finance to accelerate delivery

Sigma has designed the PRS funding model to allow a significant acceleration in the development of residential land assets from within the existing local authority partnerships. This will not only improve Sigma's financials but is also a major benefit to the local authority partners in terms of helping to meet their social agenda and address a chronic shortage of rental accommodation. Residential land assets with planning permission, sufficient to create large and diversified private rental portfolios, can be made available to the fund structures at values that are attractive relative to current market value. This should encourage the provision of the necessary development finance and in return the local councils are able to progress their regeneration ambitions and meet local needs faster, generate revenues from council tax faster, and also benefit from the government's new homes bonus. Sigma estimates that the PRS model will deliver homes at five to six times the rate as those built for sale. Two PRS agreements have been reached to date, covering the initial delivery of more than 1,000 homes (we assume 1,177 for Grainger and Gatehouse phase 1 combined). Follow-on tranches of the Gatehouse JV will lift this further and in total Sigma has existing access to development land that could supply c 12,000 PRS homes. Not all of this currently has planning permission as this only lasts for three years, making it more effective to seek permission reasonably close to the intended building date. However, Sigma says its pipeline will cover the next few years and that it is relatively confident that planning hurdles will be few. Around half of the sites are already designated housing sites and the other half have been earmarked for housing. As regeneration sites there is typically a willingness to see development proceed.

The ability to provide geographically diversified housing portfolios under PRS is an attractive feature to PRS investors, and Sigma's efforts to broaden its local authority partner footprint should support interest in future portfolios as well as providing additional land capacity. We also expect Sigma to consider private sector acquisitions to further diversify its development land resources.

A measure of the potential scale and significance of PRS is the backing that it received from both the prime minister and the UK secretary of state for business innovation and skills. Sigma reports that PRS has also attracted attention from other local authorities, with which it has begun to discuss potential regeneration and development ventures.

The Gatehouse joint venture

The Gatehouse joint venture covers the delivery, in tranches, of a potential c 6,600 homes, with a likely gross development cost of c £700m. Gatehouse is a London-based, Shariah-compliant investment bank. Construction of the first tranche of 927 homes is now underway with an expected development cost of c £100m. Barclays Bank will provide the joint venture with up to £67m of debt funding, which supplements c £47m of equity from Gatehouse. Sigma is making an equity investment alongside Gatehouse of up to £2m, the exact amount depending on final construction costs.

The new homes will comprise a mix of high-quality family homes as well as apartments and will be constructed across 14 sites in the North West. Sigma's main contributions to the JV include the sourcing of residential development sites, acting as development manager and providing asset management services. Construction is outsourced to Sigma's house building partner Countryside Properties (UK) on a fixed-price design and build contract, and a lettings strategy has been agreed with Direct Lettings, part of Shepherd Direct, a multi-discipline property services group. We expect construction to begin almost immediately and that this first tranche will be delivered over a 24-month period. This is reflected in our 2014 and 2015 estimates, but we have not yet included the impact of additional tranches. This first tranche is smaller than the 2,000 homes envisaged at the time of the initial agreement (subject to debt funding) in November 2013, but we suspect that the financing negotiations that have been ongoing since then have highlighted the attraction of delivering multiple smaller tranches with less requirement for development-stage debt funding. In this respect, we note that Sigma is exploring structures with Gatehouse for the faster delivery of additional tranches.

PRS will generate fees for Sigma through each stage of its life, including a carried interest for Sigma in the value of the fund during its post-delivery rental period:

- **Transaction fee:** This is based on the delivery cost of each tranche, and has been set with the intention of enabling Sigma to recover the costs that it has incurred to date in the creating of the JV as well as reward its efforts in bringing this to fruition. The fee is payable in full at the start of each tranche. We have assumed a fee of 1%, at the top of the 0.5-1.0% range indicated in the 2013 annual report.
- **Development management fee:** This is based on the delivery cost of each phase, spread evenly over the development period (but paid quarterly in arrears), and calculated on a site-by-site basis. We have assumed a fee of 2%, at the top end of the 1.5-2.0% range indicated in the 2013 annual report.
- **Asset management fee:** This is based on the aggregate delivery cost of all completed assets and paid quarterly in arrears. It is earned throughout the asset management phase of each site and is expected to be about four to five years. We have assumed a fee of 0.5% pa, in line with guidance in the 2013 annual report.
- **Carried interest:** Sigma will retain a share of the net disposal profits on the assets, subject to a minimum return to investors. Few details have been disclosed, but our estimates net of assumed disbursements put Sigma's net share of the gain at a little under 14% (2013 annual report guidance 15%). Sigma has conservatively indicated £2.0m for its potential share of the gross disposal profits. We believe this builds in little more than the mark up from development cost to market value. We estimate the net gain to Sigma on this basis at c £1.4m.

In Exhibit 2 (page 10) we show our estimates of the impact of the Gatehouse transaction on Sigma's profit and loss account.

The Grainger strategic partnership

On 10 November, Sigma announced it has signed an agreement with Grainger plc, granting Grainger an exclusive option to acquire residential development opportunities to provide more than 100 PRS units, sourced by Sigma. With a UK rented portfolio comprising nearly 9,000 units (of which c 90% are regulated tenancies and the balance market rented), Grainger is the largest UK-listed owner and manager of a large residential property portfolio. It has recently been giving greater focus to increasing the size of its market rented portfolio as well as geographically diversifying from its London and South-East focus. The option has an initial term of four years and covers 100 (or more) residential units sourced by Sigma, covering key cities of England (outside Greater London). Grainger will appraise each development opportunity individually and a number of sites have already been identified, which Sigma and Grainger are looking to progress.

Grainger currently expects that it will fully own the initial developments sourced by Sigma, although in future it may seek to syndicate its investment to third-party investors (possibly including Sigma). In addition to sourcing the development opportunities, Sigma expects to act as the development manager on the majority of the projects. Sigma will earn revenues based on the development profit (the difference between the cost of delivery and the market value) on each development, split into a sourcing fee and a development management fee. The level of fees has not been disclosed, but as there is no carried interest included within the transaction, we believe that it is likely to be similar to the c 3% that Sigma earns on its traditional regeneration business. Given the size of Grainger's existing portfolio (and Sigma's access to development land sites), we would expect the agreement to be more extensive than the first option grant covering development opportunities for 100 or more PRS units. For forecasting purposes, in this note we have assumed development opportunities for 250 units.

Financials

PRS should generate meaningful earnings in 2015

In this note we have updated our 2014 estimates and introduced 2015 estimates for the first time. These revised estimates incorporate Sigma's exit from its historic venture capital activities to focus entirely on its property activities. Our new forecasts include a first-time contribution from the Gatehouse JV in 2014 (and continuing through 2015), as well as an adjusted contribution from the Grainger venture in 2015. For the full year 2014, we are estimating an essentially break-even result. We expect reported revenues for 2014 to show a decline from £5.8m in 2013 to £3.9m. However, 2013 included c £0.5m of discontinued venture capital revenues while one of Sigma's property projects, North Arran Way (NAW), was accounted for as a development. The NAW accounting treatment saw the full development value (£3.7m) adding to revenues, with a significantly offsetting development cost. The similar impact on 2014 revenues is c £0.6m, all in H1.

Exhibit 1: Property gross profit development					
£000's	2013	H114	H214e	2014e	2015e
Property revenues (exc PRS)	5,342	1,761	1,095	2,856	2,270
Development costs	(3,551)	(564)	(3)	(567)	(4)
Property gross profit (exc PRS)	1,791	1,197	1,092	2,289	2,266
PRS revenues			1,000	1,000	2,000
PRS cost of sales			(100)	(100)	(133)
PRS gross profit			900	900	1,867
Total property revenues	5,342	1,761	2,095	3,856	4,270
Total property cost of sales	(3,551)	(564)	(103)	(667)	(137)
Total property gross profit	1,791	1,197	1,992	3,189	4,133

Source: Company data, Edison Investment Research

Exhibit 1 shows the development of just the property revenues, cost of sales and gross profit over 2013 to 2015e. The 2013 and H114 cost of sales represents the NAW development costs, while in

H214 and 2015, the cost of sales predominantly represents our estimate of the fees that will be paid by Sigma to introducers of the Gatehouse PRS. We have assumed 10% of transaction fees, development management fees and asset management fees.

We are looking for a significant uplift in property gross profit in 2014 from c £1.8m to c £3.2m. £0.9m of the increase is accounted for by the expected transaction fees on Gatehouse phase 1, net of the assumed commission paid to introducers. Looking just at the non-PRS activities, we are looking at increasing gross profit for the year (£2.3m versus £1.8m in 2013) but for a slowdown in H2, reflecting the diversion of management effort to getting PRS underway. We expect some upwards pressure on administrative costs for similar reasons, providing room for a decline in 2015 costs. In H2, residual costs for the exited VC operations will drop away, and a small H2 profit should leave the group broadly break-even for the year.

We expect the temporary slowdown in traditional regeneration revenues to be apparent in 2015 as well, including the discontinuation of revenues from the Winchburgh project. The transaction fee from Gatehouse phase 1 will not recur but we forecast c £1.3m in development management fees and a first, very small asset management fee contribution on the first completions. We also look for the Grainger partnership to contribute c £0.7m in revenues. Very little detail has been released for commercial reasons, but our assumptions for the Grainger contribution look for total fees equivalent to c 3% of our estimated GDC. The GDC assumes that Sigma acts as development manager and that development opportunities for 250 units are delivered, with an assumed £120k market value per unit and a 12.5% development margin. Given that the fees will include a sourcing fee and a development management fee, we assume that the majority (c 86%) will be earned in 2015 and the balance in 2016. Our preliminary estimates for the Grainger transaction in 2015 (published in Edison Insight on 28 November 2014) made the assumption of 500 units. Given Grainger's scale, we continue to believe that 500 units is possible, but given that the venture is only just beginning, we have more conservatively assumed 250 units in 2015 in this note. This change in assumption essentially defers fees of c £0.7m of fee income (and a similar amount of PBT) for potential future PRS delivery.

With increasing revenues and slightly lower costs, we are looking for 2015 EBITDA to increase to £1.1m (2014e £42k). With net cash in the balance sheet, there is a modest contribution from interest income.

The balance sheet remains strong with net cash

Sigma ended 2013 with £2.1m of net debt on its balance sheet. However, this included £3.2m of short-term development funding relating to the NAW project (see above). By the end of H114 this loan had unwound and Sigma was £9.2m cash positive. This included the c £8m proceeds of its March 2014 share placement (c 11.4m shares at 70p) aimed at bolstering the balance sheet to support (more in terms of counterparty confidence rather than financially) its planned large-scale development opportunities. We have allowed for the 2014 £2.0m equity contribution to the Gatehouse JV (it may actually be less than this) and also for the possibility of some timing differences between the anticipated earnings and cash receipts. We forecast £5.4m of net cash at the end of 2014, and only a little lower (£4.8m) at the end of 2015 despite the assumed timing differences. We have not assumed any purchases of development land, although we believe these are possible as Sigma seeks to expand and geographically diversify its access to development sites.

Valuation

Ignore reported earnings and look at development potential

Even when adjusted for discontinued venture capital activities and the impact of the now-exited associated investments, we feel the historic profit and loss account and balance sheet of Sigma are a poor guide to the value of the business.

Using the reported earnings and net assets, at 62.5p Sigma is trading on c 42x our estimate of normalised earnings for 2015 and 3.6x fully diluted NAV per share. Our forecasts continue to show positive net cash, but we expect Sigma to focus on opportunities to increase and diversify its development opportunities ahead of dividend distributions. Not only do these simple near-term P/E and P/NAV metrics fail to capture the full potential value of Sigma's business, reported earnings can be expected to be highly variable from one year to the next, depending on deal flow, even though the recurring fee element from asset management will begin to build.

The real value of Sigma resides, largely off balance sheet, in its access to a pipeline of urban regeneration projects via the current local authority JVs, with an estimated £2bn GDC. Subject to financing being available to progress these, we would expect Sigma to earn development and project management fees from the existing JVs alone, of something like 3% or £60m. In addition to a value for this existing land access, we consider that investors will continue to award Sigma a goodwill premium to reflect the likely future access to additional land assets via new local authority ventures and private sector transactions. Indeed, Sigma believes its existing land access, when applied to PRS, may be capable of delivering well in excess of the previously identified £2bn of GDC. In addition to PRS, this includes the elements of commercial development and residential for sale (neither is quantified separately).

Assuming that c £60m of fee revenue could be earned over, say, a 10-year period, with no need for any increase in the current c £3m cost base, implies a potential average c £3m pa operating profit over the period. However, under PRS funding arrangements, subject to satisfactory debt funding arrangements, we expect this future fee pool to be earned faster and, as discussed, to possibly be larger.

We have estimated the undiscounted gross value of fees to Sigma from the first phase (927 units from a potential total 6,600) of the Gatehouse JV to be c 5.5% of the gross development cost (ie greater than the traditional c 3%). Of this 5.5%, the transaction fee represents 1%, set with the intention of enabling Sigma to recover the costs it has incurred in creating the JV and reward its efforts in bringing the JV to fruition; 1.1% represents the gross undiscounted value of the estimated carried interest. This estimate uses guidance from Sigma (c £2.0m before Sigma disbursements) but seems highly conservative. It appears to factor in no more than a 10% gain in the full market value of the portfolio (from the £100m gross development cost) and little or no further capital appreciation.

We expect additional tranches of the Gatehouse JV, building to a potential gross development cost of c £700m. However, we also think it is likely there will be other variants of the model, with different fee structures. For example, we have assumed that fees on the Grainger strategic partnership are similar to the historical regeneration activities. Although set in relation to the gross development profit, we have assumed a level that is equivalent to 3% of our forecast gross development cost (with no carried interest). In all, we note that Sigma has existing land access to support the delivery of up to 12,000 PRS units in all.

Gatehouse worth up c 44p per share, total PRS up to 80p

Following the fee structure as described on page 10, in Exhibit 2, we show our estimates for the incremental profit impact from Gatehouse phase 1 over the next several years. We have assumed the project starts more or less immediately such that the transaction fee is earned in 2014, and we

expect that c 80% of the development will be completed by 18 months (100% by 24 months). Our modelling incorporates Sigma's conservative estimate of its share of the gross value of the potential carried interest (after seven years) of £2.0m. Net of our assumptions for Sigma's disbursements this is c £1.4m net to Sigma. Most of this gross gain is likely to represent the move from delivery cost value to market value at completion, while the eventual outcome may also benefit from capital value increases after completion and until sale.

This exhibit also shows our estimate of the net present value (NPV) of this first phase, using a discount rate of 10%. This is 6.6p per share (a 1% decrease/increase in the discount rate increases/decreases this value to 6.8p/6.4p). The implied NPV per share of the full Gatehouse JV plans for 6,600 units, assuming similar terms to phase 1 (and making the simplifying assumption that construction of future phases were to run coincident with the first) is c 44p (ie the 6.6p value of 927 phase 1 units multiplied by c 6.6x). But this value captures just the Gatehouse transaction.

Exhibit 2: Estimates for Gatehouse transaction phase 1

£		Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7
	2014	2015	2016	2017	2018	2019	2010	2021
Transaction fee	1,000,000	-	-	-	-	-	-	-
Development Management fee		1,300,000	700,000	-	-	-	-	-
Asset management fees		25,000	400,000	500,000	500,000	500,000	500,000	500,000
Promote fee/carried interest		-	-	-	-	-	-	1,365,000
Total revenues	1,000,000	1,325,000	1,100,000	500,000	500,000	500,000	500,000	1,865,000
Introducer fees	(100,000)	(132,500)	(110,000)	(50,000)	(50,000)	(50,000)	(50,000)	(50,000)
Sigma operating profit	900,000	1,192,500	990,000	450,000	450,000	450,000	450,000	1,815,000
Tax rate	0.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%
Tax	-	(238,500)	(198,000)	(90,000)	(90,000)	(90,000)	(90,000)	(363,000)
Net profit from JV	900,000	954,000	792,000	360,000	360,000	360,000	360,000	1,452,000
Discount factor	1.00	0.90	0.81	0.73	0.66	0.59	0.53	0.48
Discount rate	10%							
NPV of net income	900,000	858,600	641,520	262,440	236,196	212,576	191,319	694,487
Sum of NPV	3,997,138							
Number of shares (m)	60.5							
Per share value (p)	6.6							

Source: Company data, Edison Investment Research

With current access to c 12,000 potential PRS units (ie excluding additional local authority JVs or private sector land deals) on similar terms to Gatehouse 1, PRS in total could be worth up to 80p per share (12 × 6.6p). Much depends on the speed of delivery, which is uncertain. The net present value to Sigma of this potential PRS value is reduced the longer it takes to start projects. On top of PRS, including the balance on non-PRS residential for sale schemes and commercial schemes (unquantified), allowing for cash in the balance sheet (an estimated £5.4m at the end of 2014 or c 5p per share), and allowing a goodwill element for additional local authority JVs, the full value should be higher than the value of PRS alone.

Sensitivities

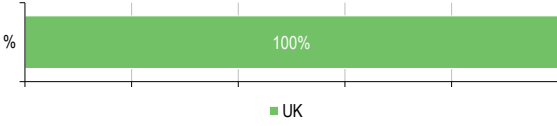
- The detail and timing of urban regeneration schemes is difficult to predict, particularly regarding finance and planning issues, and may at times be subject to political influences.
- There are risks associated with executing and delivering large commercial and residential property developments, although the team has significant project management experience.
- The fixed-cost design and build contract with Countryside Properties strictly limits the risks of cost or time over-runs on the Gatehouse JV development. It may not be possible to arrange future transactions on a similar basis.
- Sigma's prospects are highly dependent on its ability to accelerate land developments under PRS. The success of these initial transactions will be important in securing additional tranches and transactions, and the requisite funding.

- Notwithstanding a critical shortage of homes in many parts of the country, and the relative lack of volatility in residential rents, the residential housing market is likely to reflect the general economic cycle over time, potentially having an impact on investment flows into PRS over the medium term, potential fees, including asset management revenues, and the performance of any carried interest.

Exhibit 3: Financial summary

	£000s	2012	2013	2014e	2015e
Year end December		IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS					
Revenue		2,326	5,808	3,874	4,270
Cost of Sales		0	(3,551)	(667)	(137)
Gross Profit		2,326	2,257	3,207	4,134
EBITDA		(187)	(355)	42	1,097
Operating Profit (before amort. and except.)		(210)	(376)	26	1,081
D&A		(24)	(18)	(16)	(16)
Share based payments		(22)	67	(16)	(16)
Exceptionals		0	0	0	0
Operating Profit		(256)	(327)	(6)	1,049
Net Interest		22	10	12	12
Unrealised profit/(loss) on revaluation of investments		(826)	(28)	0	0
Provisions/other losses		0	(531)	0	0
Profit Before Tax (norm)		(299)	(456)	38	1,093
Profit Before Tax (FRS 3)		(1,171)	(966)	6	1,061
Tax		0	0	0	(212)
Profit After Tax (norm)		(299)	(456)	38	880
Profit After Tax (FRS 3)		(1,171)	(966)	6	848
Average Number of Shares Outstanding (m)		45.6	45.7	56.7	60.5
EPS - normalised (p)		(0.7)	(1.0)	0.1	1.5
EPS - normalised fully diluted (p)		(0.7)	(1.0)	0.1	1.5
EPS - (IFRS) (p)		(2.6)	(2.1)	0.0	1.4
Dividend per share (p)		0.0	0.0	0.0	0.0
Gross Margin (%)		100.0	38.9	82.8	96.8
EBITDA Margin (%)		-8.0	-6.1	1.1	25.7
Operating Margin (before GW and except.) (%)		-9.0	-6.5	0.7	25.3
BALANCE SHEET					
Fixed Assets		1,645	1,135	1,097	1,080
Intangible Assets		614	596	579	563
Tangible Assets		26	19	13	12
Other - investments, financial assets etc		1,005	520	505	505
Current Assets		1,833	6,723	7,350	8,231
Trading investments		45	2	2	2
Debtors		688	651	791	2,291
Cash		1,024	1,070	5,410	4,791
Other		76	5,000	1,147	1,147
Current Liabilities		(881)	(5,222)	(1,593)	(1,593)
Creditors		(881)	(2,051)	(1,593)	(1,593)
Short term borrowings		0	(3,171)	0	0
Long Term Liabilities		0	0	0	0
Long term borrowings		0	0	0	0
Other long term liabilities		0	0	0	0
Net Assets		2,597	2,636	6,854	7,718
CASH FLOW					
Operating Cash Flow		(292)	(3,665)	1,798	(404)
Net Interest		22	10	12	12
Tax		0	0	0	(212)
Capex		0	(14)	(10)	(15)
Acquisitions/disposals		29	483	(1,986)	0
Financing		0	61	7,697	0
Dividends		0	0	0	0
Net Cash Flow		(241)	(3,125)	7,511	(619)
Opening net debt/(cash)		(1,265)	(1,024)	2,101	(5,410)
HP finance leases initiated		0	0	0	0
Other		0	0	0	(0)
Closing net debt/(cash)		(1,024)	2,101	(5,410)	(4,791)

Source: Company data, Edison Investment Research

Contact details		Revenue by geography					
41 Charlotte Square Edinburgh EH2 4HQ Scotland 0131 220 9444 www.sigmacapital.co.uk							
CAGR metrics		Profitability metrics		Balance sheet metrics		Sensitivities evaluation	
EPS 2011-15e	N/A	ROCE 14e	0.8%	Gearing 14e	N/A	Litigation/regulatory	●
EPS 2013-15e	N/A	Avg ROCE 2011-15e	N/A	Interest cover 14e	N/A	Pensions	○
EBITDA 2013-15e	N/A	ROE 14e	0.6%	CA/CL 14e	4.6x	Currency	○
EBITDA 2011-15e	N/A	Gross margin 14e	82.8%	Stock days 14e	0.2	Stock overhang	●
Sales 2013-15e	14.7%	Operating margin 14e	0.7%	Debtor days 14e	74.5	Interest rates	○
Sales 2011-15e	N/A	Gr mgn / Op mgn 14e	N/A	Creditor days 14e	150	Oil/commodity prices	●
Key members of management team and board							
Chief executive officer: Graham Barnet				Finance director: Marilyn Cole			
Graham co-founded Sigma (Technology Management Ltd) in 1997. A qualified lawyer, he worked at Noble Grossart and Shepherd & Wedderburn, specialising in corporate finance, before forming his own company (Merchant Investments Ltd) in 1994.				Marilyn joined Sigma in 2000 and will retire from the company at the end of 2014. She spent her early career at Deloitte Haskins & Sells and PKF, where she specialised in corporate finance work, and was previously FD of Northamber. Malcolm Briselden, currently group financial controller, has been chosen as the new group finance director.			
Chief operating officer: Graeme Hogg				Non-executive chairman: David Sigsworth			
Graeme co-founded Sigma Inpartnership in 2000, and was instrumental in the creation of its three regeneration partnerships. He has significant experience in the property and property finance sector, and has worked on major commercial and residential development projects. He also has international experience in property development and fund management.				David spent over 10 years as a main board director of FTSE 100 utility companies, most recently on the board of Scottish and Southern Electricity. He is actively involved in the sustainable energy sector and holds several associated non-executive directorships. David is also chairman of the Sigma Sustainable Energy Fund II.			
Principal shareholders as at 2 December 2014							(%)
Henderson Global							16.9
Graham Barnet							12.4
JO Hambro Capital Management							11.3
AXA Investment Managers SA							6.1
Hargreave Hale Ltd discretionary clients							4.6
NFU Mutual Insurance Society Ltd							3.8
Barkley Ltd and Canterbury Ltd							3.7
Companies named in this report							
Sigma Capital plc, Grainger plc							

Edison, the investment intelligence firm, is the future of investor interaction with corporates. Our team of over 100 analysts and investment professionals work with leading companies, fund managers and investment banks worldwide to support their capital markets activity. We provide services to more than 400 retained corporate and investor clients from our offices in London, New York, Frankfurt, Sydney and Wellington. Edison is authorised and regulated by the Financial Conduct Authority (www.fsa.gov.uk/register/firmBasicDetails.do?sid=181584). Edison Investment Research (NZ) Limited (Edison NZ) is the New Zealand subsidiary of Edison. Edison NZ is registered on the New Zealand Financial Service Providers Register (FSP number 247505) and is registered to provide wholesale and/or generic financial adviser services only. Edison Investment Research Inc (Edison US) is the US subsidiary of Edison and is regulated by the Securities and Exchange Commission. Edison Investment Research Limited (Edison Aus) [46085869] is the Australian subsidiary of Edison and is not regulated by the Australian Securities and Investment Commission. Edison Germany is a branch entity of Edison Investment Research Limited [4794244]. www.edisongroup.com

DISCLAIMER

Copyright 2014 Edison Investment Research Limited. All rights reserved. This report has been commissioned by Sigma Capital Group and prepared and issued by Edison for publication globally. All information used in the publication of this report has been compiled from publicly available sources that are believed to be reliable, however we do not guarantee the accuracy or completeness of this report. Opinions contained in this report represent those of the research department of Edison at the time of publication. The securities described in the Investment Research may not be eligible for sale in all jurisdictions or to certain categories of investors. This research is issued in Australia by Edison Aus and any access to it, is intended only for "wholesale clients" within the meaning of the Australian Corporations Act. The Investment Research is distributed in the United States by Edison US to major US institutional investors only. Edison US is registered as an investment adviser with the Securities and Exchange Commission. Edison US relies upon the "publishers' exclusion" from the definition of investment adviser under Section 202(a)(11) of the Investment Advisers Act of 1940 and corresponding state securities laws. As such, Edison does not offer or provide personalised advice. We publish information about companies in which we believe our readers may be interested and this information reflects our sincere opinions. The information that we provide or that is derived from our website is not intended to be, and should not be construed in any manner whatsoever as, personalised advice. Also, our website and the information provided by us should not be construed by any subscriber or prospective subscriber as Edison's solicitation to effect, or attempt to effect, any transaction in a security. The research in this document is intended for New Zealand resident professional financial advisers or brokers (for use in their roles as financial advisers or brokers) and habitual investors who are "wholesale clients" for the purpose of the Financial Advisers Act 2008 (FAA) (as described in sections 5(c) (1)(a), (b) and (c) of the FAA). This is not a solicitation or inducement to buy, sell, subscribe, or underwrite any securities mentioned or in the topic of this document. This document is provided for information purposes only and should not be construed as an offer or solicitation for investment in any securities mentioned or in the topic of this document. A marketing communication under FCA Rules, this document has not been prepared in accordance with the legal requirements designed to promote the independence of investment research and is not subject to any prohibition on dealing ahead of the dissemination of investment research. Edison has a restrictive policy relating to personal dealing. Edison Group does not conduct any investment business and, accordingly, does not itself hold any positions in the securities mentioned in this report. However, the respective directors, officers, employees and contractors of Edison may have a position in any or related securities mentioned in this report. Edison or its affiliates may perform services or solicit business from any of the companies mentioned in this report. The value of securities mentioned in this report can fall as well as rise and are subject to large and sudden swings. In addition it may be difficult or not possible to buy, sell or obtain accurate information about the value of securities mentioned in this report. Past performance is not necessarily a guide to future performance. Forward-looking information or statements in this report contain information that is based on assumptions, forecasts of future results, estimates of amounts not yet determinable, and therefore involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of their subject matter to be materially different from current expectations. For the purpose of the FAA, the content of this report is of a general nature, is intended as a source of general information only and is not intended to constitute a recommendation or opinion in relation to acquiring or disposing (including refraining from acquiring or disposing) of securities. The distribution of this document is not a "personalised service" and, to the extent that it contains any financial advice, is intended only as a "class service" provided by Edison within the meaning of the FAA (ie without taking into account the particular financial situation or goals of any person). As such, it should not be relied upon in making an investment decision. To the maximum extent permitted by law, Edison, its affiliates and contractors, and their respective directors, officers and employees will not be liable for any loss or damage arising as a result of reliance being placed on any of the information contained in this report and do not guarantee the returns on investments in the products discussed in this publication. FTSE International Limited ("FTSE") © FTSE 2014. "FTSE®" is a trade mark of the London Stock Exchange Group companies and is used by FTSE International Limited under license. All rights in the FTSE indices and/or FTSE ratings vest in FTSE and/or its licensors. Neither FTSE nor its licensors accept any liability for any errors or omissions in the FTSE indices and/or FTSE ratings or underlying data. No further distribution of FTSE Data is permitted without FTSE's express written consent.

Frankfurt +49 (0)69 78 8076 960 Schumannstrasse 34b 60325 Frankfurt Germany	London +44 (0)20 3077 5700 280 High Holborn London, WC1V 7EE United Kingdom	New York +1 646 653 7026 245 Park Avenue, 39th Floor 10167, New York US	Sydney +61 (0)2 9258 1161 Level 25, Aurora Place, 88 Phillip Street, Sydney NSW 2000, Australia	Wellington +64 (0)4 8948 555 Level 15, 171 Featherston St Wellington 6011 New Zealand
--	--	--	--	--