Tanfield Group Plc

PETERHOUSE RESEARCH

Finger on the Triggers

13th April 2015

Following the disposal of Smith Electric Vehicles in 2010, and of the Snorkel division in Q4 2013, Tanfield is now an investment company with two passive investments – a 5.76% shareholding in Smith and 49% of Snorkel LLP. The current valuation of the Group does not accurately reflect either the values of these shareholdings, or the prospects for these investments.

Smith Electric Vehicles Corp is a leading designer and producer of all-electric commercial vehicles for short haul urban fleets, and was established in the North East of England in the 1920s, but it now principally manufactures in Kansas City. Smith produces zero-emission vehicles that deliver a significantly superior performance to traditional diesel trucks, at greater operational efficiency and significantly lower cost. As of January 2015 the carrying value of the stake in Smith (excluding warrants) was put at **US$10.73m**, representing approximately **5p** per share.

Snorkel is a global producer of self-propelled, towable and push-around aerial lifts, including diesel and electric scissor lifts, mast lifts, telescopic boom lifts and articulating booms, offering safe, efficient working at heights of between 3 and 40m. the carrying value of the Snorkel stake and its preferred interest holding (a loan note) was **US$60.1m**, or approximately **27p** per share.

The combined carrying value of these investments of **US$70.83m** represents approximately **32p** per share, compared with the current market valuation of Tanfield of £30m, or 21p per share.

Smith has received a US$42m commitment from China-based Sinopoly Battery Ltd and is about to pull the trigger on a listing via a reverse takeover on the OTCBB, followed after the statutory 180 days by listing on NYSE or NASDAQ. The strategic investment is strengthening Smith's position in the fast growing commercial EV market in China, as well as making it more cost competitive in its current markets.

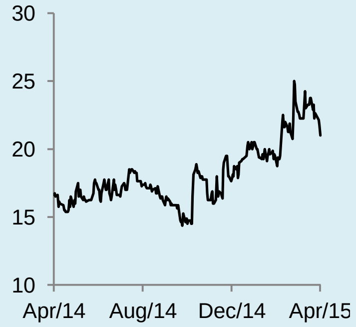
A recovery in Snorkel's market, and the investment and restructuring by Xtreme, the joint owner, can be expected to raise EBITDA until the trigger point is reached for Tanfield to realise its investment in Snorkel - US$25m EBITDA over a prior 12 month period.

With a listing for Smith imminent and the trigger point for Snorkel in the foreseeable future, Tanfield does not warrant the discount of over 30% to the carrying values of its investments, and probably deserves a premium.

Company Data

EPIC	TAN
Price (last close)	21p
52 week Hi/Lo	25p/14.5p
Market cap	£30m

Share Price, p



Source: ADVFN

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Background – Tanfield Timeline

Early Years

The Tanfield Group was founded in 1996 by Roy Stanley, as a manufacturing company with a turnover of around £50,000 per annum and nine employees, and by March 2003 the Group had grown by acquisition and organically into a manufacturing group providing advanced technical and assembly solutions with a turnover of almost £10 million and 178 employees.

2003-2004 comeleon reverse acquisition

Tanfield was reverse-required by comeleon, a company that had floated in late 2000, in December 2003. comeleon had the technology to apply full colour images on to three dimensional components and targeted the market for personalized mobile phone covers – a market that did not materialise.

2004

Tanfield acquired Smith Electric Vehicles in October 2004. As part of this transaction, £4m was raised in new equity (before expenses), and a second round of fundraising was completed in December 2004 raising a further £3m (before expenses.

2005

In the course of 2005, Tanfield developed a portfolio of businesses focused on providing zero emission vehicles and zero emission industrial products to customers operating in closed urban and industrial environments. The Group comprised:

Smith Electric Vehicles, which had become the largest manufacturer worldwide of road going electric vehicles with a customer base of over 500 operating both in the private and public sectors.

Norquip, a leading manufacturer of airport service vehicles and passenger transfer units.

JumboTugs, a manufacturer of electric powered tow tractors and platform trucks used predominantly in the Airport and Industrial sectors.

Aerial Access,a manufacturer with a recognized leadership position in the design and manufacture of high quality electrically powered aerial lifts and access platforms.

Tanfield Engineering Systems,an engineering business that supported the Group's product range and provided complex integrated systems to third party blue chip customers.

2007

Operations are now grouped into two divisions: Zero Emission Vehicles and Powered Access, with both divisions underpinned by the Group's Engineering capabilities.

Tanfield acquired Snorkel, the St Joseph, Missouri based manufacturer of self- propelled boom and scissor lifts. The combination of Snorkel and Powered Access' UpRight activity put it among the leading global manufacturers of aerial work platforms.

2008

After a profitable first half of the year, the Group encountered a downturn in its end markets in the second half of 2008 as the global economy entered its dramatic downturn.

The Powered Access Division was impacted by the swift decline in the economy, which led to a blanket suspension of fleet replacement and expansion programmes by major equipment rental companies, along with the almost complete withdrawal of financing globally for new aerial work platforms.

The Zero Emission Vehicles Division experienced some supply chain constraints in 2008, coupled with several order postponements.

During that year, Tanfield entered into Heads of Terms for a joint venture, Smith Electric Vehicles US Corporation (SEV US Corp) to assemble commercial electric vehicles for the North American market. Tanfield held a 49% equity stake in SEV US Corp, with the rest held by private US investors. The first US production model made in the Kansas City, Mo, facility was the Smith Newton truck.

2009

Tanfield received a non-binding, conditional offer from SEVUS for the Smith Electric Vehicle division, with completion of the sale announced on 1 January 2011. The assets of the UK entity were sold to SEVUS for US$15m.

2011

Powered Access & Engineering noted a significant recovery in end-user demand that outstripped its manufacturing capacity, impaired by weakness in the industry's supply chain.

2013 – Snorkel acquired by Xtreme

In the year ended 31 December 2012, the losses of the **Snorkel Division** were approximately £14.6m and it had net assets of £23.5m. To meet the funding requirements of a Snorkel recovery plan, a staged sale was agreed to Xtreme, a Nevada, USA, based manufacturer of high quality telescopic material handlers. These machines are widely used by the construction, mining, resources, and agricultural sectors for lifting materials. Xtreme, via its holding in SKL Holdings, proposed a staged acquisition of the Snorkel Division, via the creation of Snorkel International Holdings, in which Tanfield will retain a holding until the consideration terms are fully met.

Don F. Ahern, as trustee of the DFA Separate Property Trust, owns 96.6% of Xtreme and 97% of Ahern Rentals, Inc.

Ahern is one of the largest privately held equipment rental companies in the world, and purchases a significant number of aerial work platforms annually. Ahern was a major customer of Snorkel.

Smith Electric temporarily suspended production in Q4 2013 in order to transition its supply chain to Tier 1 suppliers, allowing production cost reductions. Production was resumed at the beginning of January 2015.

Separately, Tanfield disposed of the loss-making **Tanfield Engineering Services** in December 2013.

Smith Electric Vehicles

The Business

Smith Electric Vehicles manufactures and markets zero-emission commercial electric vehicles that are designed to be a superior-performing alternative to traditional diesel trucks due to higher efficiency and lower total cost of ownership.

Smith is the leading global producer of all-electric medium-duty commercial vehicles, and customers include many of the world's largest fleet operators, including **PepsiCo's Frito-Lay division, Staples, TNT, Sainsbury's, Coca-Cola, DHL, FedEx and the U.S. Military.**

Smith currently designs, produces and sells two vehicle platforms, the Smith Newton and the Smith Edison, both of which can be configured for multiple applications. The company is headquartered in Kansas City, Missouri, and has manufacturing facilities in Kansas City, Missouri, New York City, New York, and has a research and development site near Newcastle, England.

The Smith Edison truck/van/coach versions are based on a Ford Transit chassis with payload 700-2300 kg in a variety of configurations. It has a 90 kW motor with 36-51 kWh lithium-ion iron phosphate battery pack, giving it a range of 90 to 180 km. **This is probably the world's most widely-sold light commercial EV**.

In the USA Smith produces the Newton truck with 2.8 to 7 tonnes payload and varied wheelbases. The Newton is currently powered by a 120 kW motor with 80-120 kWh lithium-ion iron phosphate battery pack, providing a range of between 50 and 240 km.

The range of both the Edison and Newton types depends on the size of battery pack and driving conditions. They offer good road performance, with top speeds of up to 70mph. Being battery-powered, they are zero emission at the point of use.

The product range is designed for intra-urban back-to-base applications such as home shopping delivery, parcel and mail delivery, logistics, construction, utilities, airports and public sector operations. As they are operate within a radius and return to base for recharging, range-anxiety is a negligible issue, if at all.

In the UK Smith vehicles are in operation within vehicle fleets, including those of the **Royal Mail, Sainsbury's, BSkyB, Parcelforce, DHL, TNT, Scottish & Southern Energy and Balfour Beatty.**

The Smith Newton™, (two variants are illustrated above and below), is deployed in several countries across a variety of applications, including parcel, food, beverage and equipment delivery and student and personnel transport.

Financials

Smith reported to Tanfield in January 2015 that the business has an order book taking it through the first half of 2015 and continued positive enquiry levels for orders beyond that from its existing customer base and new customers in USA, Europe and Latin America. Federal Government, State and city subsidies for electric vehicles are prevalent, with California providing up to US$65,000 per vehicle.

With the resumption of production Smith has converted the majority of its supply chain to Tier 1 suppliers, which is expected to realize cost savings, as well as enhanced manufacturing quality, reliability and capacity. Smith also secured a US42m commitment from a major Chinese battery and EV company, as reviewed below.

Tanfield Group holds 5.76% of the equity of Smith (excluding warrants). The carrying value of the holding is US$10.73m (£7.1m). This represents approximately 5p per share.

Strategic investment - FDG

Smith announced in May 2014 that it had secured a US$42m commitment from Sinopoly Battery Limited, a Hong Kong headquartered major player in the research, development, production, distribution and sale of Lithium-ion batteries and related EV products. The initial US$2m funding will be followed by two tranches pending milestones to be achieved by both companies. By January 2015, US$13m had been invested.

This investment makes Sinopoly as a strategic shareholder in Smith Electric. Under the agreement, Sinopoly will become Smith Electric's exclusive supplier for batteries in vehicle applications that are compatible with Smith Electric's platforms and customer requirements. Sinopoly will also become a preferred supplier for certain electric vehicle components that can be manufactured in its Hangzhou facility.

FDG Electric Vehicles, Limited, the resulting joint venture between Smith and Sinopoly, should be strongly positioned for the rapidly growing commercial EV markets in China and the U.S. The company's strategic relationship with FDG is critical in terms of reducing manufacturing costs. The supply of batteries from FDG at substantially lower cost is expected to be implemented in 2015. As the battery constitutes over 40% of the cost of the vehicle this would have a major impact on the cost of the vehicles and allow a sustainable positive gross margin on vehicle sales.

US listing

In July 2014, Smith announced that it had acquired American Business Services, Inc (ABSR), an Over the Counter Bulletin Board, OTCBB, company, by acquiring 85% of the common stock of ABSR. Smith closed its Series E funding round in November 2014, raising US$20m converting all investment debt to equity. On the closing of the series E funding round the first tranche of Tanfield warrants have become due with an exercise price of US$0.31.

The warrants will be exercisable within 6 months of issuance and carry a term of 2 years. In aggregate the total number of warrants to be issued to Tanfield are expected to amount to just over 2% of the issued share capital at the time of the OTCBB, listing.

The Smith Board has confirmed (in the January 2015 announcement) that the 2012, 2013, and 2014 audit reviews, required for its OTC reverse merger, are progressing as planned and the company aims to file the super 8k required for its listing on the US OTC market. This will start the process of a full listing on a public US exchange.

From Tanfield's perspective, it could have a tradable investment in a NYSE or NASDAQ listed stock in ABSR after the 180 day lock- in expires from the date that Smith becomes a publicly traded company on the OTCBB. A listing on one of the main exchanges could see an appreciable increase in the valuation of Smith.

Commercial EV Markets

Electric Vehicles have received government support in many countries over the past decade, targeting city pollution and de-carbonising the transportation sector. Automotive manufacturers with demanding average fleet emission targets to meet are developing EVs to offset the relatively high emitting luxury car brands.

An international Electric Vehicles Initiative was launched in October 2010 at the Paris Motor Show by a consortium which included:

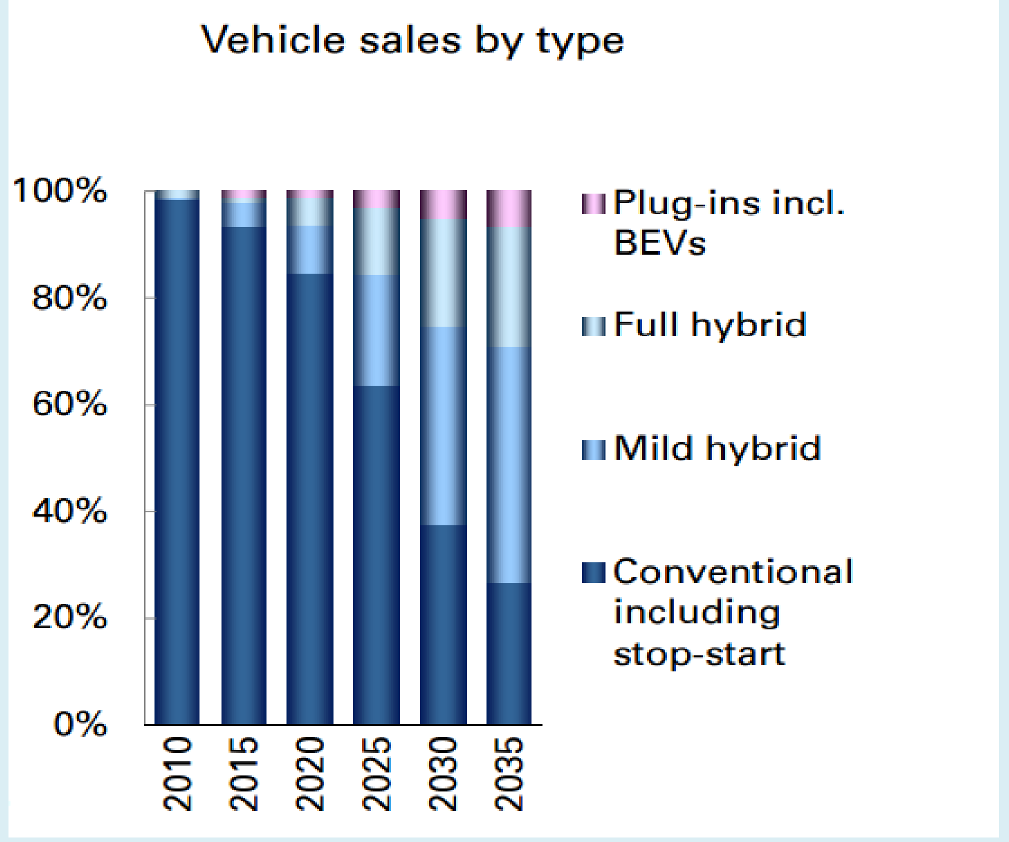
- The OECD International Energy Agency (IEA)
- China,
- France,
- Germany,
- Japan,
- South Africa,
- Spain,
- Sweden
- The United States.

The Initiative aimed to achieve rapid market development of electric and plug-in hybrid electric vehicles (EV/PHEVs) around the world, targeting about 20 million EVs and PHEVs on the road by 2020. This was forecast by the IEA to lead to over 200 million EV/PHEVs on the road by 2030, and 1,000 million by 2050. Whether the growth trajectory of EV/PHEVs will reach this remains to be seen.

At the start of 2014, IHS Automotive estimates that there were 405,000 on the road, including 174,000 in the US, 68,000 in Japan and 45,000 in China. **The Chinese government has a target of putting 500,000 EV and PHEVs on the road by 2016.** Already China has the largest fleet of battery-electric bicycles, with more than 150 million on the road and an annual production rate of around 36 million.

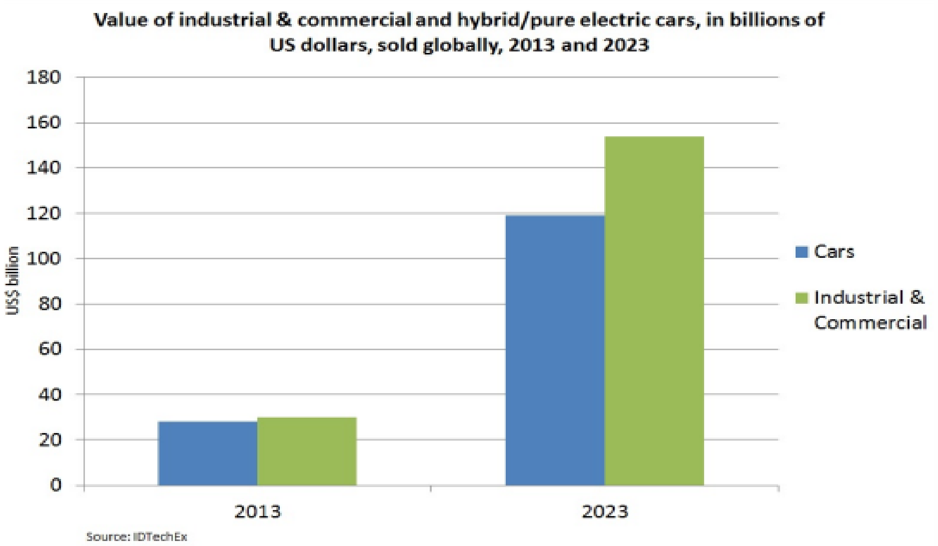
BP, in its 2014 "Energy Outlook 2035" report, forecast a dramatic fall in conventionally powered vehicle by share of sales, a rise in the EV share, but the majority of sales comprising hybrid technologies:

Energy Outlook



Source: BP

Electric hybrid vehicles are now being used in commercial applications where the improved technology offers major benefits for specific drive cycles that involve city driving in stop-start traffic. Consequently, IDTechEx forecasts strong growth in both electric car and commercial vehicles, with commercial being the larger market by 2023:



In a new 2015 report (Electric Drive Trucks and Buses), Navigant Research forecasts that global sales of electric drive and electric-assisted medium- and heavy-duty commercial vehicles (MHDV, Classes 3 to 8) will grow from less than 16,000 in 2014 to nearly 160,000 in 2023, representing a compound annual growth rate (CAGR) of 29.3%. Powertrain types included in the report are hybrid-electric, plug-in hybrid electric, and battery electric.

Navigant sees the Asia Pacific region as likely to provide the majority of the volume, but also expects sales in both North America and Western Europe to be significant. However, Navigant also notes that global penetration will likely remain low, increasing from 0.4% in 2014 to 2.9% in 2023.

Navigant expects the Western European market to be the region with the greatest penetration of the technology in 2023, with 9.6% of new MHDVs expected to feature electric or electric-assisted drive.

The importance of the China market is clear, and thus the strategic investment in Smith by Sinopoly puts FDG Electric Vehicles in a strong position in that market, and allows Smith to be cost-competitive in other key markets.

Snorkel

The Business

Snorkel is a leading global manufacturer of aerial work platforms, designed for use on a broad range of surfaces and applications. Snorkel produces one of the widest ranges of aerial lifts in the industry, with more than 35 machines available at platform heights from 2m-40m, including scissor lifts, booms, towable lifts, push-arounds and low-level access platforms.

Examples are shown here :

Financials

The company’s report to Tanfield, January 2015, gave estimated 2014 revenue of approximately US$100m and a forecast figure of approximately US$150m in 2015.

The order book rose substantially through 2014 compared to 2013, and there has been a working capital investment of over US$45m. This has meant that supplier constraints have been reduced and the spares business has improved dramatically. This is important in that it means that Snorkel can more effectively support its machines in the field, which it had considerable difficulty doing in the previous year due to cash restraints**.**

Ahern Rental, a related company through ownership of Snorkel, has absorbed the full costs of certain Snorkel assembly and distribution centres. Also a number of functions have been consolidated onto one site. This strategic restructuring has had the benefit of extending Ahern's reach whilst maintaining Snorkel distribution at much reduced cost.

These and other cost-reduction actions have reduced the breakeven level of turnover of the business.

Markets

By 2012/13 the aerial work platform (AWP) market recovery was well underway, led by the return of purchasing by the rental fleets. Growth in emerging markets like China has lent further support to this recovery. IPAF (International Powered Access Federation) research shows 20% annual growth rates in China, compared to around 6% in the US, and overall European growth, which has been negligible in 2013/2014.

There are now over 1 million mobile aerial work platforms (AWPs), in the worldwide rental fleet. This represents an annual 6% increase in the past two years, mainly driven by growth in Asia and Latin America (IPAF).

Reports from other key players in the industry indicate the market is still growing, with JLG (Oshkosh Industries), for example, expecting growth to continue in 2015 (J.P. Morgan Aviation, Transportation & Industrials Conference, March 5, 2015).

The Paris-listed Haulotte Group, a people and material lifting equipment company, reported full year 2014 consolidated sales of € 412.6m against €342.7m in 2013, an increase of 20%. Haulotte finds growth remaining strong in all areas apart from Latin America: 33% in Asia-Pacific, 29% in Europe, and 28% in North America.

The Xtreme/Snorkel Deal

Xtreme Manufacturing (Xtreme) and Tanfield both hold shares in Snorkel International Holdings, a Nevada limited liability company. Tanfield will retain an initial interest in 49% of Snorkel International Holdings and a preferred interest position of US$50m, in exchange for Xtreme's controlling interest in Snorkel International Holdings.

Xtreme has committed to making significant working capital facilities (estimated at between US$35m and US$50m) available to Snorkel International Holdings to deliver its growth forecast, and to deliver other strategic benefits and synergies to Snorkel International Holdings.

Subject to the Snorkel Division reaching an annualised trailing EBITDA of at least US$25m (meaning when over $2 million EBITDA is achieved in a month) within 5 years of Closing, Tanfield can demand payment of the preferred interest, which would be paid when Snorkel International Holdings is able to fund such payment, and its net debt/EBITDA ratio is less than 2, utlimately reducing Tanfield's interest in Snorkel International Holdings to 30%.

Subject to the payment of the preferred interest, and within 5 years of Closing, Tanfield has a "put" option on this remaining holding, whereby SKL Holdings will be obliged to purchase the remaining interest held by Tanfield at an agreed multiple of 5.5 times EBITDA earnings, as at the date of the put, again subject to Snorkel International Holdings being able to fund. SKL Holdings has a call option on the same commercial terms.

Given the measures Xtreme is taking to enhance the competitivity and profitability of Snorkel, the trigger event for the realisation of the Snorkel investment (when the company has achieved an annualised trailing EBITDA of US$25m) can be expected to be reached in the foreseeable future.

Conclusion

The current market valuation of Tanfield is around 30% below the carrying value of its two investments, which represent 32p per share as at the latest valuation of the respective holdings (January 2015). An imminent OTCBB listing for SEVUS and then transition to the NYSE or NASDAQ after the 180-day lock-in period opens the way to significant upward revaluation on the strength of a listing on a major exchange and the bolstered finances at SEVUS following the strategic investment by Sinopoly.

There is also the trigger for the sale of some or all of Tanfield's holding in Snorkel International Holdings, releasing outstanding preferred interest, on payment of which, in addition 30% of the value of Snorkel International.

We would expect either or both of these events to yield significant upside for the value of Tanfield shares.

Group Financials

The income statement and balance sheet reflect Tanfield's transition from a holding company to an investing company (with no direct revenues):

Income Statement £'000s		
Year to 31 December	**2013A**	**2014E**
Revenue	2,223	
Staff costs	-2,606	-115
Depreciation and amortisation		
Other operating income		20
Other operating expenses	-679	-123
Loss before impairments	-1,062	-218
Impairment of investments	-1,357	
Intercompany loan forgiveness	-17,141	
Adjustments to fair value of investments	26,984	
Profit after impairments	7,424	-218
Finance expense	-80	-280
Finance income	48	15
Net finance income	-32	-265
Profit before tax	7,392	-483
Tax	0	0
Net profit	**7,392**	**-483**
EPS basic, p	**5.40**	**-0.34**
EPS diluted, p	**5.29**	**-0.34**

Source: Company historic data, analyst estimates

The non-current investments below comprise the holdings in SEVUS (£1.28m) and Snorkel International Holdings LLC(£36.283m)

Balance Sheet £'000s		
6 months to 30 June	**2013A**	**2014A**
Non-current assets		
Non-current investments		37,563
Investments in subsidiaries	11,965	
	11,965	37,563
Current assets		
Trade and other receivables	19,719	2,574
Deferred consideration	339	341
Cash and cash equivalents	380	257
	20,438	3,172
Total assets	**32,403**	**40,735**
Current liabilities		
Trade and other payables	624	1,581
	624	1,581
Non-current liabilities		
Deferred tax		
Total liabilities	**624**	**1581**
Equity		
Share capital	6,975	7,086
Share premium	16,262	16,262
Share option reserve	1,966	862
Special reserve	66,837	66,837
Merger reserve	1,534	1,534
Retained earnings	-61,796	-53,427
Total equity	**31,778**	**39,154**
Total equity and total liabilities	**32,402**	**40,735**

Source: Company historic data

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