

16th December 2010

Analyst: Tom Winnifrith
Email: tom.winnifrith@t1ps.com
Tel: 01624 676 848

Designcapital* - 2011 the Year of Transformation: Strong Buy at 13.5p - Price Target increased from 27p to 39.1p

2010 was a year when Designcapital established the foundations for creating a profitable growth business. The AIM listed Investment Company, specialising in luxury high end furniture design and distribution, managed to end an eighteen month process of bringing its two French subsidiaries Artelano and Forum out of the equivalent of Chapter 11 on June 24th and sales improved steadily thereafter to the point where, we believe, the company moved into profit by December. 2011 will be a year when the company builds on that platform, expanding both its retail unit (Artelano) but, more significantly the Forum B2B contract supply business aggressively. The company is also in the process of creating an e-procurement platform allowing architects, decorators, space planners and builders to procure high quality branded design furniture at "trade" prices and this - while not contributing greatly to 2011 numbers should accelerate growth from 2012 onwards as should the opening of a London showroom in March 2011.

| Key Data | |
|-----------------|--|
| EPIC | DESC |
| Share Price | 13.5p |
| Spread | 12p - 15p |
| Shares in Issue | 65,300,847 |
| Market Cap | £8.8 million |
| 12 Month Range | 11p - 14p |
| Market | AIM |
| Website | www.designcapitalplc.com |
| Sector | Speciality Finance |
| Contact | Frederic Bobo - 020 7554 8555 |

In November 2010 Designcapital raised £190,000 in a placing at 11p which allowed it to sign the tenancy on its new London site. The company is likely to generate additional cash in the coming months as warrants from its IPO are exercised at 10p and, we believe, that this will be used to fund the purchase of more retail showrooms, almost certainly from forced sellers, and expansion of the Forum sales team and the launch of the e-procurement platform. The company is therefore fully funded to take it into a trajectory of accelerating profitability, starting from 2011.

We have assumed that the new London showroom and the procurement offering make a minimal profits contribution in 2011 but do start to contribute materially from 2012 and that no acquisitions are made during 2011, something we regard as unlikely. The management of Designcapital believes that within five years, the group (driven largely by the European expansion of Forum and by the new procurement business) can be generating a 10% EBIT margin on revenues of £100 million and given that the current market capitalisation is less than £9 million that potential provides obvious investment appeal. However we value the business on the basis of 2013 EBITDA and believe that for a company now firmly established on the growth trajectory a 2013 EV/EBITDA multiple of 8 is not unreasonable and consequently, at 13.5p, we reiterate our stance of strong buy but increase the price target from 27p to 39.1p.

| Year to 31st December | Revenue (£million) | Pre-Tax Profit Excluding Amortisation (£ million) | EBITDA (£ million) | Earnings Per Share (Excluding Amortisation) (p) | Price Earnings Ratio | EV/EBITDA Multiple |
|-----------------------------|-----------------------|---|--------------------------|---|----------------------------|-----------------------|
| 2009A | 8.1 | (4.0) | (3.5) | (6.4) | n/a | n/a |
| 2010E | 6.2 | (2.47) | (2.0) | (3.78) | n/a | n/a |
| 2011E | 10.0 | 0.9 | 1.5 | 1.37 | 9.85 | 6.67 |
| 2012E | 15.0 | 1.41 | 2.0 | 2.15 | 6.28 | 5.0 |
| 2013E | 23.0 | 2.44 | 3.05 | 3.72 | 3.63 | 3.29 |

**Designcapital is a corporate client of Rivington Street Corporate Finance which is owned by Rivington Street Holdings (RSH), the ultimate owner of GE&CR. A second RSH subsidiary manages funds which own Designcapital shares, as does RSH itself.*

Background

Designcapital is the sole AIM listed play on the luxury branded high end “design” furniture market. Although its operations are still largely based in France, and most of its managers are French, it is a British company. Run by a team with extensive experience of the retail and investment worlds it was established in June 2007 with the intention of acting as a consolidator in the highly fragmented European portion of a global market which is worth c.€20 billion per annum and which is estimated to be growing at a rate of 6-8% a year.

The company listed on AIM at 10p on January 21st 2008, raising £5.5 million, and it still retains the possibility to call on £1.3 million deferred subscriptions, priced at 10p, not drawn down at Admission although those investors must exercise their rights or lose them by January 31st 2011.

Within four months it had made its first two acquisitions - Artelano, a creator of high end furniture founded in Paris in 1972 and Forum a wholesaler of a broad range of design products which was established in 1982. Turning round these two troubled enterprises was a lengthy process as a result of the complexities of French employment and creditor protection laws, known as “redressement judiciaire”. However, that process allowed Designcapital to both deal with the creditors of the business and to reduce overheads and was completed on June 24th 2010. Inevitably the process also impacted on sales but since the completion of the redressement, turnover has increased across the group and we believe that in the final month of 2010 the company moved into profit.

With the platform for profits and growth now firmly established, the company can move ahead with its business plan which is to act as a consolidator within the European design space. The recession, lack of credit for smaller businesses and the fact that the entrepreneurs behind many businesses started in the late 1960s and 1970s are now reaching retirement age without natural successors means that in a fragmented market there are numerous opportunities. However, the company stresses that while it seeks to buy 7-10 high end to luxury brands, and up to 40 large high street multi-brand show-rooms of luxury design furniture, which face special situations (succession issue, balance sheet problems, etc) and so can be bought at attractive prices, the process is lengthy and the average transaction will take 12-24 months to complete. Once bought - for a combination of cash and equity - and once complex European employment legislation can be overcome which may take 6 to 12 months, new companies can be quickly integrated into the Designcapital infrastructure so allowing the group to boost margins significantly as a result of increased buying power and the rationalisation of central office functions. The group is now at a stage where additional turnover - whether generated organically or as a result of acquisition - should, post rationalisation, generating an operating margin of 45%.

The company will launch a London showroom for Artelano in Dover Street in London's West End in March of 2011. This will target the 300,000 expatriate French community in London. It will also provide a UK base for Forum helping it to expand its business outside France without increasing its overhead materially.

Designcapital is also seeking to boost sales (and thus its purchasing power and margins) with the launch of a B2B e-procurement platform tapping into the 100 million Euro space of purchases of high end furniture required by architects, decorators, space planners and builders throughout France. This platform should be first launched in France in the second quarter of 2011, then rapidly rolled out on selected markets of the EU, including the UK, and can be run off the existing Forum overhead. The company expects French sales of no more than £1 million in 2011 but that turnover will grow rapidly thereafter, up to possibly 25% of the group's consolidated turnover. The actual margin on this operation on a stand-alone basis will not be huge but by boosting the volumes purchased from brands and suppliers by Forum the effect on the group margin will be material from this year onwards.

Operations

The first business bought by Designcapital, in February 2008, was **Artelano** (www.artelano.com) a creator of high end design/contemporary furniture. Created in 1972, Artelano is one of the most renowned French brand of high end contemporary furniture.

Artelano works closely with world class designers such as Patricia Urquiola, Piero Lissoni, Christophe Pillet, Olivier Gagnère, Marco Zanuso Jr., Eric Gizard, Shin Azumi, Qiong-er Jiang, Francesc Rifé, Carlo Tamborini and Marc Krusin, and others. Since the Design team took control it has added other "signatures" to its portfolio including product from Ora Ito and Patrick Naggar. Its collections include tables, chairs, sofas and other pieces of furniture. It should be noted that Artelano is not a manufacturer - the Designcapital model is based on outsourcing all manufacturing.

The manufacturing of Artelano's products is thus sub-contracted in France or in Italy, in limited series, to skilled craftsmen who bring high quality finishing to the creative mix of the collections. Moreover, over the years, the company has fostered an unconditional policy of fine materials selection and demanding quality control processes. Artelano products are mostly distributed in

France, from the company's show-room located in Paris, and through a selected network of partner show-rooms located in more than forty countries worldwide. The dedicated London showroom marks a step change in terms of international expansion.

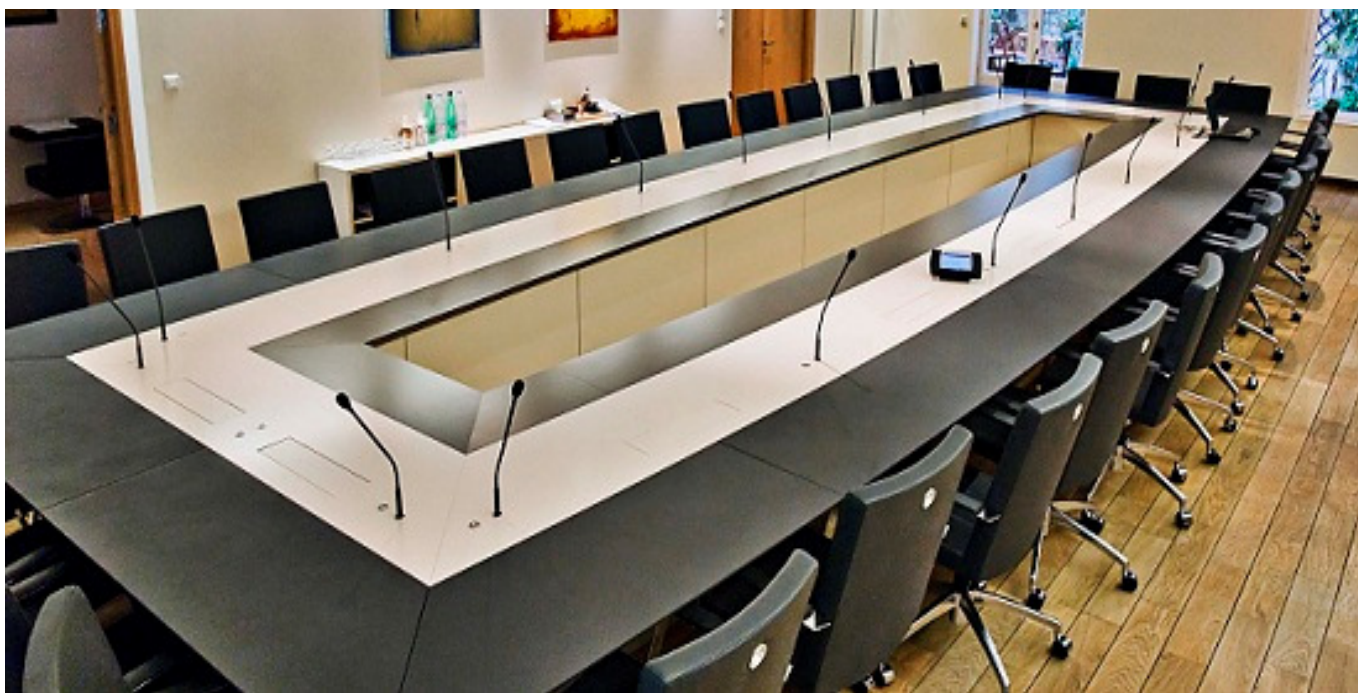
Artelano has won a large number of international awards such as the ICFF Editors Award, le Nombre d'Or, Elle Decoration, Marie Claire Maison, etc.

The price paid in 2008 was €1.65 million and in 2008 it generated a €1 million EBITDA loss on sales of €2.65 million. However - with the assistance of a €1 million shareholder loan, using the French equivalent of Chapter 11, the company has now been restructured with costs taken out and lower margin commodity lines discontinued. The disruption caused by the redressement should not be under-estimated. The restructuring process was completed in the first half of 2010 with the closure of a number of small Parisian concession outlets which were loss making. The effect of these closures was to move the business into loss in the first half - as there was a time lag on taking out related costs - but the smaller more focussed business that remains is now, we believe, operating at close to break even on a monthly basis and is starting to grow its sales once again - a process that will be enhanced by the opening of the London showroom.

Forum Diffusion (www.forumdiffusion.com) was bought for a token €1 - it is a Paris based retailer established in 1982, located nearby the "Arc de Triomphe".

In 2008, Forum Diffusion and Forum Development, the two companies acquired, generated consolidated sales of €16 million and managed to lose €1.6 million at the EBITDA level. Again a management loan (of €900,000) was utilised for a restructuring which saw 48% of staff lose their jobs as Forum Diffusion again entered the equivalent of Chapter 11.

In its interims for 2009, Designcapital reported that Forum was already trading at a cashflow positive level albeit on markedly lower sales. The bulk of Forum's sales have always been to corporate customers rather than to individuals and in recognising this the company sold the Forum showroom in July 2010 for €1.1 million and is now aggressively engaged in tapping the lucrative corporate contracts market serving customers including HSBC, ING, Deutsche Bank, Aéroports de Paris and the French Government.



Offices fitted by Forum Diffusion

On 4th November 2010 the company announced that it had won an order worth €845,166 (potentially €1.1 million in due course) from the French Ministry of Foreign Affairs and with lead times between orders being placed and delivered (and thus revenues being booked) being up to four months the division has a good visibility of earnings. Our discussions with the management indicate that the business is now covering its fixed costs on a monthly basis and moved into the black at the end of 2011.

Although we do not expect it to have generated revenues of greatly in excess of £5 million in calendar 2010 it will be the engine of growth going forward and the company believes that sales should match pre-redressement levels by 2013. Sales growth is critically important in that increased volumes give Forum increased purchasing power with designers so have a clear impact on gross margins. The addition of the procurement operation should accelerate volume growth and hence margin improvement across the company.

Management

The management team collectively has years of experience in both furniture industry and in investment banking. They have large personal holdings in the Designcapital equity - the board owns 67.7% of the shares in issue.

Frédéric Bobo, Executive Chairman. A French national with 25 years of experience in investment banking and in corporate advisory services. Bobo has directly led and managed over 150 corporate advisory transactions including privatisations, corporate sales, IPOs, industrial restructurings, cross border M&A, joint-ventures and direct investment schemes. In 2001 he created his own venture, Stunning Partners & Co, which provides corporate finance and strategic advisory services to companies and high profile managers. He is the founder of Designcapital and owns 28.7% of the company.

Philippe Hervé, Executive Director. A French national, Herve has 30 years of experience in the retailing and furniture industries. He started his career in the Darty Group before holding senior positions at a subsidiary of the Nouvelles Galeries Group and at Cauval Industries. In 2006 Herve acquired a controlling capital stake in Omoté Futons, a retail chain specializing in Asian furniture (now sold).

Mike Hosie , Finance Director. A British national, Hosie has more than 25 years experience in general management and as finance director. Hosie is also contracted to Verdes Management plc as Finance Director, a company that he helped float on AIM in late 2005.

David Henderson-Stewart non-Executive Director. A New Zealand national, Henderson-Stewart is a member of the Paris bar. Since 2005, he has held the position of Managing Director of International Affairs and Member of the Board of the International Industrial Bank-Mejprombank (zao Mejdunarodny Promishleny Bank). He is also member of the board of United Industrial Corporation-OPK, zao Obyedinionaya Promishlenaya Korporatsia, and the trustee of OPK Trust Company Limited.

Pierre Rainero, non-Executive Director. A French National, Rainero started his career in advertising in 1980 at Ogilvy and Mather. He has since then worked at Cartier gaining an insight into luxury goods and is now a member of the board of directors of Cartier S.A. and Hexagram (which is involved in the production of computerised images).

Frédéric Michel-Verdier, non-Executive Director. A French national expatriated in London, he is an Investment Director with Industry Funds Management (UK) Limited, one of the largest global investors in infrastructure assets.

Major Shareholdings

There are 65,300,847 shares in issue with 1,727,272 million warrants and options outstanding priced at 11p. Those holding more than 3% are:

| | | |
|--------------------|------------|---------|
| Luxadvor S.A. | 22,841,000 | 34.98 % |
| Frédéric Bobo* | 19,790,650 | 28.75 % |
| L.A. Finances S.A. | 9,817,400 | 15.03 % |

** inclusive of the number of shares held by Stunning Partners L.L.C., a company in which Mr Bobo is interested.*

Conclusion and Valuation

Results for calendar 2010 will clearly not look that impressive. The process of restructuring the operations at both divisions has been costly and the results will have shown through only in the final months of the year. We are comfortable with our 2010 forecasts but they are not the real story. The point is that Designcapital is now profitable at an operating level and enjoying increased sales volumes in both divisions, but notably at Forum. The pipeline of business for Forum is strong and we are confident that at a PLC level this business will be profitable and cash generative from the start of 2011. The Dover Street opening and launch of the procurement business will not make a direct impact on profitability in 2011 but by boosting volumes they should increase the purchasing power of the enlarged group and so widen margins. The real ramp up in profitability will take place

from 2012 onwards as operational gearing kicks in.

There are risks to our forecasts both ways. We have reservations about the strength of economic recovery in Europe and this may dent sales growth. But it should be noted that our forecasts only assume that the company only starts to surpass pre-redressement sales levels by 2013 and so we do not regard them as unduly optimistic. Moreover with a lowly geared balance sheet (the net financial debt is exclusively a shareholder's loan from Luxadvor) and with a number of funding options open we do expect that Design will accelerate its sales (and thus margin) growth with selected acquisitions, something not discounted in our estimates.

The management of Designcapital believes that within five years, the group (driven largely by Forum and to a lesser extent by the new procurement business) can be generating a 10% EBIT margin on revenues of £100 million and given that the current market capitalisation is less than £9 million that potential provides obvious investment appeal. Even if those targets are missed by 50% it would imply huge long term upside.

However we value the business on the basis of 2013 EBITDA and believe that for a company now firmly established on the growth trajectory a 2013 EV/EBITDA multiple of 8 is not unreasonable and consequently, at 13.5p, we reiterate our stance of strong buy but increase the price target from 27p to 39.1p.

| Year to 31st December | Revenue (£million) | Pre-Tax Profit Excluding Amortisation (£ million) | EBITDA (£ million) | Earnings Per Share (Excluding Amortisation) (p) | Price Earnings Ratio | EV/EBITDA Multiple |
|-----------------------------|-----------------------|---|--------------------------|---|----------------------------|-----------------------|
| 2009A | 8.1 | (4.0) | (3.5) | (6.4) | n/a | n/a |
| 2010E | 6.2 | (2.47) | (2.0) | (3.78) | n/a | n/a |
| 2011E | 10.0 | 0.9 | 1.5 | 1.37 | 9.85 | 6.67 |
| 2012E | 15.0 | 1.41 | 2.0 | 2.15 | 6.28 | 5.0 |
| 2013E | 23.0 | 2.44 | 3.05 | 3.72 | 3.63 | 3.29 |

**Designcapital is a corporate client of Rivington Street Corporate Finance which is owned by Rivington Street Holdings (RSH), the ultimate owner of GE&CR. A second RSH subsidiary manages funds which own Designcapital shares, as does RSH itself.*

This research note cannot be regarded as impartial as GE&CR has been commissioned to produce it by Designcapital, it should be regarded as a marketing communication.

The information in this document has been obtained from sources believed to be reliable, but cannot be guaranteed. Growth Equity & Company Research is owned by T1ps.com Limited which is commissioned to produce research material under the GE&CR label. However the estimates and content of the reports are, in all cases those of T1ps.com Limited and not of the companies concerned.

This research report is for general guidance only and T1ps.com Limited cannot assume legal liability for any errors or omissions it might contain.

The value of investments can go down as well as up and you may not get back all of the money you invested; You should also be aware that the past is not necessarily a guide to the future performance. Finally, some of the shares that are written about are smaller company shares and often the market in these shares is not particularly liquid which may result in significant trading spreads and sometimes may lead to difficulties in opening and/or closing positions. Before investing, readers should seek professional advice from a Financial Services Authorised stockbroker or financial adviser.

T1ps.com Limited is authorised and regulated by the Financial Services Authority (FSA Registration no. 192801) and can be contacted at 3rd Floor, 3 London Wall Buildings, London, EC2M 5SY

email philip.morrish@gecr.co.uk - fax 020 7628 3815 tel 0207 562 3371