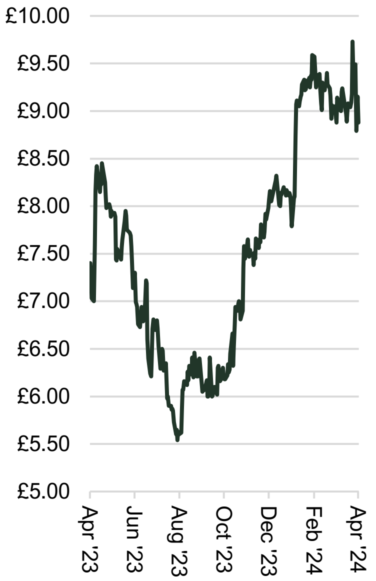
Next 15 Group PLC

NFG | AIM | Media | 888p | £881m

FY24 Final Results – Poised for an upturn

1 Year Chart



While 2.5% revenue growth and 6.1% EBIT growth is relatively pedestrian by Next 15's historic track record, we see the last year as one of the most impressive reported by Next 15. Revenue growth and margin expansion has been delivered in the face of a significant slowdown in demand from the group's historic core technology sector clients. We believe a number of factors are in play here, not least the growing diversity of Next 15's client and business mix as a result of M&A over the last three years. We also look to the de-centralised group operating structure, which prioritises subsidiary accountability for budgets and cost control.

Despite a trading backdrop that remains challenging, prospects for the current financial year look promising. Estimates for FY25E and beyond have already been scaled back (albeit at a significantly lower rate than for many peers) and do not make any real assumptions for any significant return to growth for Next 15's technology client. The mood music in the tech sector continues to improve and should this feed through to budgets, then this suggests risks to the upside. Next 15's FY25E PE of 10.5x remains undemanding both on an absolute and peer group relative basis.

- **Few surprises in the final results:** The January trading update had already flagged the key headlines. The only new news from a numbers perspective was the better then expected net debt position (£1.4m vs our estimate of £11.8m) and the $50m reduction in the Mach49 earn out liability.
- **It is all in the margin:** The 80 bps improvement in EBIT margins to 21% is even more impressive given the tough trading backdrop for much of 2023, especially within the technology sector. We see Next 15 benefiting from the combination of the breadth of its business and client mix; an operating structure that lends itself to more rigorous budgeting, and the ability to drive structural cost benefits at the group and agency level.
- **Steady outlook at this stage:** Although not out of the woods by any means, tech sector spend looks to have stabilised. Coupled with good new business activity across the rest of the group, this leaves Next 15 well positioned to benefit from any sustained tech sector recovery. We do not see any recovery currently captured within estimates.
- **Estimates:** We have updated our model to capture FY27E for the first time. Our headline estimates for FY25E / FY26E remain broadly unchanged.

Next 15 Group PLC is a research client of H2 Radnor Ltd.

MiFID II – this research is deemed to be a minor, non-monetary benefit.

22nd April 2024

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January, £m	Revenue	PBT adj	EPS (p)	Div (p)	Net Cash	PE x	Yield %
FY 2023A	563.8	112.5	80.4	14.6	26.1	11.1	1.6
FY 2024A	577.8	117.9	81.6	15.4	(1.4)	10.9	1.7
FY 2025E	*619.7*	*128.4*	*87.2*	*16.1*	*8.4*	*10.2*	*1.8*
FY 2026E	*658.2*	*140.4*	*97.6*	*17.8*	*47.3*	*9.1*	*2.0*
FY 2027E	*699.1*	*153.3*	*106.7*	*19.7*	*97.1*	*8.3*	*2.2*

Source: h2Radnor

Final Results – Year ended January 2024 – Key points

Next 15 Group has reported its final results for the year ended January 2024. These results had been pre-flagged at the full year trading update in January so there were no material surprises, other than a better than initially expected net debt position, and a reduction in the Mach49 earn out liability.

The key headlines are as follows:

- Full year reported revenue growth **+2.5%** to **£577.8m**, which breaks down into
  - → Organic growth +0.3%
  - → Acquisition contribution +3.3%
  - → FX headwind -1.1%
- Adjusted operating profit **+6.1%** to **£121.1m**, a record level for the group
- Adjusted operating margin **+80** basis points to **21.0%**
- Adjusted PBT **+4.8%** to **£117.9m**
- Reported PBT of £80.3m (FY23: £10.1m), driven by a material reduction in exceptional and adjusting items
- Fully diluted, adjusted EPS **+1.5%** to **81.6p**
- Final dividend of 10.6p (+5%), making up a full year dividend **+5%** to **15.35p** (+5% YoY)
- A better than initially expected cash performance in January led to a lower net debt position, £1.4m, than we had been expecting.
- The share buyback programme has been extended from April to July with the intent of returning £10m, of which £2.1m has been spent so far in FY25. In aggregate, Next 15 has now bought back c.£6.5m of shares at an VWAP of £7.83.

Before we run through the segmental performance in more detail, there are some broader points to draw out.

- **Margin performance is the key standout**. Unlike many of its UK agency and marketing peers, Next 15 has actually been able to deliver margin expansion in what has not been an easy market from a revenue perspective. We see this as being driven by a number of factors; diversity and resilience across the business and client mix within the group; the accountability of the group's de-centralised operating model, and finally the ability to generate material cost efficiencies from both the Engine acquisition and group shared costs such as property.
- **Growing diversity of the group client mix has proven positive.** We have already seen from other UK peers the extent to which Technology sector clients have reduced spend over the last year. Next 15, which has always offered

significant exposure to North American tech sector, has not been immune from this effect. In FY24, like for like revenue from technology clients reduced by -17%. The net result of this is that tech clients now only represent 30% (down from 39% in FY23) of group revenue. In previous years this would have had a marked effect on group performance but Next 15 has been active in diversifying its client exposure and this drove +11% growth in non technology client like for like revenue, largely offsetting the former. In this context, the acquisitions of SMG and Engine Group and their subsequent strong performance, now look even more timely.

- **Balance sheet continues to be source of strength.** The year end net debt position of £1.4m, came in c.£10m ahead of our expectations and reflects a better than expected cash collection performance in January. Against the backdrop of a business generating £150m plus of EBITDA, this leaves Next 15 with significant balance sheet flexibility and more than sufficient to fund earn out commitments, the relatively modest share buyback and a resumption of smaller scale M&A. Perhaps the only cloud on the balance sheet horizon is a potentially negative impact on future working capital absorption as tech client exposure, typically better and faster payers than FMCG clients, has reduced.

- **A return to smaller scale M&A.** A key driver of Next 15's outperformance over the last 5+ years has been its ability to acquire fast growing, higher margin businesses at attractive multiples and then de-risk and accelerate those businesses post acquisition. FY23 saw this pattern somewhat disrupted by the larger than normal Engine acquisition (a clear success in our view) and the unsuccessful bid for M&C Saatchi. However, in FY24 Next 15 has reverted to its proven M&A model, making five small acquisitions during the year, which contributed £6.5m of revenue. The cash cost of these acquisitions was £15m with all the business bought with an initial EBIT multiple range of 5x – 7x, again in line with historic norms. In our view, this smaller scale M&A is a less risky, more attractive driver of longer-term shareholder value albeit at the cost of not moving the dial as fast.

Below, we run through the key divisional headlines:

Engage – 46% group revenue; organic revenue growth -6%

Headline revenue -**4%** to £263.1m (organic growth **-6%**). Segment EBITA margins were flat YoY at 20.2%

Overall, Engage remains the largest and most mature of the segments within Next 15 and also represents the largest exposure to the more traditional communications activities within the group.

The decline in Technology client was most pronounced within this segment, with the Archetype and Outcast agencies most effected. M Booth Health and MHP (both acquired within the last three years) were the standout performers with both delivering organic revenue growth but not enough to fully offset the others.

Segment margins held steady at 20.2%, largely as a result of continued cost efficiencies being secured from the Engine acquisition.

Transformation – 26% group revenue; organic revenue growth +8%

Headline revenue **+11%** to £149.6m (organic growth **+8%**). Segment EBITA margins declined +20 basis points to 32.3%.

The slowdown in the revenue growth within this segment (FY23 revenue growth was +157% vs FY22) was entirely due to the annualisation effect of the large Mach49 contract win. Although Mach49 had a solid year, the pace of growth outside the large contract has slowed to levels more comparable to elsewhere in the group. This deceleration has been enough to trigger a reduction in the outstanding Mach49 earn out obligation by $50m to $250m.

Beyond Mach49, Business Transformation also includes the digital transformation business from Engine as well as private equity specialist, Palladium and the US capital markets focused Blueshirt Group. The Engine Transform business had a strong year with a major contract win from the Department of Education. Blueshirt is highly geared towards the US IPO market and had a quiet FY24. The early indications are that life is returning to the US IPO market (Blueshirt acted on the Reddit IPO and is mandated on a further three), which points to a more promising outlook for FY25.

Customer Delivery - 19% group revenue; organic revenue growth +5%

Headline revenue **+5%** to £107.7m (organic growth **+5%**). Segment EBITA margins decreased -260 basis points to 27.0%.

This segment is focused on using data and analytics to directly impact customer purchasing activity and generate direct new customer leads. This segment has been a very strong performer since the start of the pandemic, benefiting from a structural shift in the allocation of marketing budgets towards direct revenue generation as opposed to pure brand building.

SMG (Shopper Media Group), was the strongest performer in this segment as it built on the earlier foundational Morrisons and Boots contract wins by adding Asda during the year. Not only has SMG been a very strong revenue contributor but it offers a broader range of margin outcomes through its mix of traditional “time & materials” and contingent value pricing.

Activate, the North American B2B lead generation business, which had been a stellar performer through FY21, FY22 and FY23, had a quieter year, particularly in H2 but remains a significant margin contributor to the group.

Customer Insight - 10% group revenue; organic revenue growth +4%

Headline revenue **+11%** to £57.5m (organic growth **+4%**). Segment EBITA margins declined -330 basis points to 18.0%.

Customer Insight represents, at its core, the online market research and customer data analysis component of the Next 15 group offer. This segment has the highest proportion of B2C customer exposure, other than MHP within Engage and SMG within Delivery.

The core Savanta business had a solid year, with UK revenue +9% and US +20%. Plinc, the customer data analysis agency, has been investing heavily in its sales and marketing capacity and this was the primary contributor to the margin decline for the segment, which is expected to reverse in FY25 as this investment phase ends.

Changes to h2Radnor estimates

Off the back of this update, we are taking this opportunity to update our model and to include FY27E estimates for the first time.

Although there are a number of moving parts the net result is that our FY25E and FY26E P&L headline expectations remain broadly unchanged. We have slightly reduced a number of our segmental EBIT margin expectations but these have been more than offset by the reduction in our expectations for group central costs following the significant progress made on this front in FY24.

Below the P&L, the better than expected net debt outcome for FY24 rolls forward into a higher net cash expectation for FY25E, despite the potential for a tighter working capital outlook for the group. We have also updated our model for the revised earn out liabilities post the Mach49 earn out reduction.

In Figure 1 below, we detail our key estimate revisions.

Figure 1: h2Radnor estimate revisions

		Previous		**New**		***Change, %***	
	2024A	2025E	2026E	**2025E**	**2026E**	**2025E**	**2026E**
Customer Engagement	263.1	279.8	293.8	275.0	288.7	*- 2%*	*- 2%*
Customer Delivery	107.7	117.4	125.6	118.4	126.7	*+ 1%*	*+ 1%*
Customer Insight	57.5	64.1	69.2	63.2	68.3	*- 1%*	*- 1%*
Business Transformation	149.6	163.1	174.5	163.1	174.5	*- 0%*	*- 0%*
Revenue	**577.8**	**624.3**	**663.0**	**619.7**	**658.2**	***- 1%***	***- 1%***
Customer Engagement	53.2	60.2	65.2	58.3	62.1	*- 3%*	*- 5%*
Customer Delivery	29.1	36.4	39.6	33.7	37.4	*- 7%*	*- 6%*
Customer Insight	10.4	13.8	14.9	13.0	14.7	*- 6%*	*- 1%*
Business Transformation	48.3	47.3	49.7	48.9	52.3	*+ 3%*	*+ 5%*
Central Overhead	-19.8	-27.2	-28.5	-22.3	-24.4	*- 18%*	*- 15%*
EBITA	**121.1**	**130.4**	**140.9**	**131.6**	**142.1**	***+ 1%***	***+ 1%***
- margin %	*21.0%*	*20.9%*	*21.2%*	*21.2%*	*21.6%*		
Adj. PBT	**117.9**	**128.2**	**140.2**	**128.4**	**140.4**	***+ 0%***	***+ 0%***
Adj. EPS (p)	**81.6**	**89.4**	**97.7**	**87.2**	**97.6**	***- 3%***	***- 0%***
Dividend (p)	15.4	17.9	19.5	16.1	17.8	*- 10%*	*- 9%*
Net Cash (Debt)	**-1.4**	**5.2**	**71.8**	**8.4**	**47.3**		

Source: h2Radnor

Next 15 valuation and relative performance

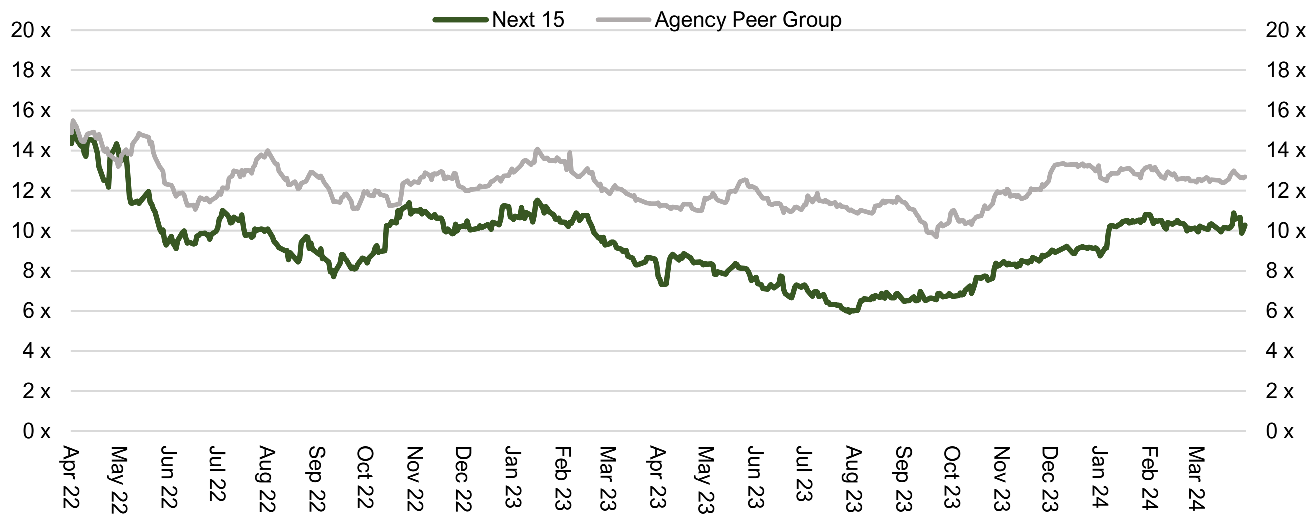
Next 15's share price has recovered strongly from its August lows (+64%). Yet we still see the current valuation as undemanding both in absolute and relative terms.

In Figure 2 below, we show the evolution of the Next 15 forward PE multiple over the last two years. We can see that from the April 2022 peak of 15x this collapsed to the

August 2023 low of 5.9x. This compares to an Agency peer group average forward PE multiple that also hit 15x in April 2022, bottoming out at 9.7x in October 2023.

This suggests that the market has taken a clear view around perceived underperformance or delivery by Next 15 through this period relative to its peers. As we show in Figures 3 & 4 below, the opposite has been true.

Figure 2: Next 15 Forward PE multiple vs Agency Peers



Source: h2Radnor, FactSet

Figures 3 & 4 show the evolution of Next 15's FY1 consensus revenue and PBT estimate since April 2022, which shows the extent to which Next 15 forward estimates have materially outperformed the peer group average.

Figure 3: Next 15 vs Peers – Consensus **Revenue**

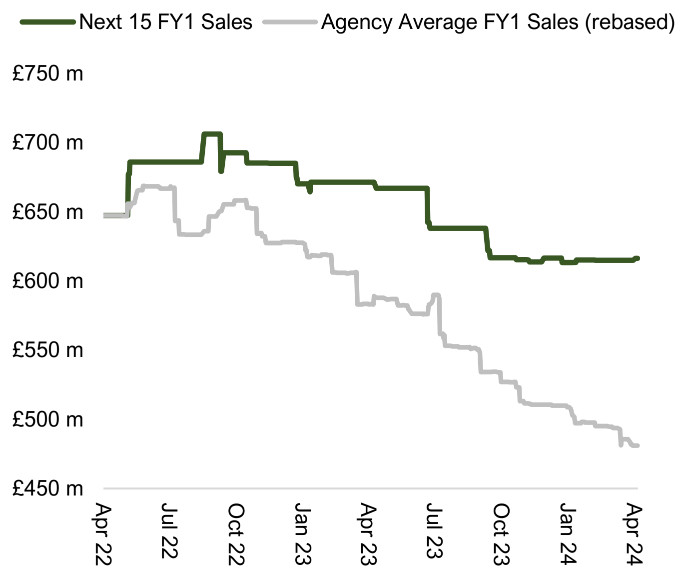
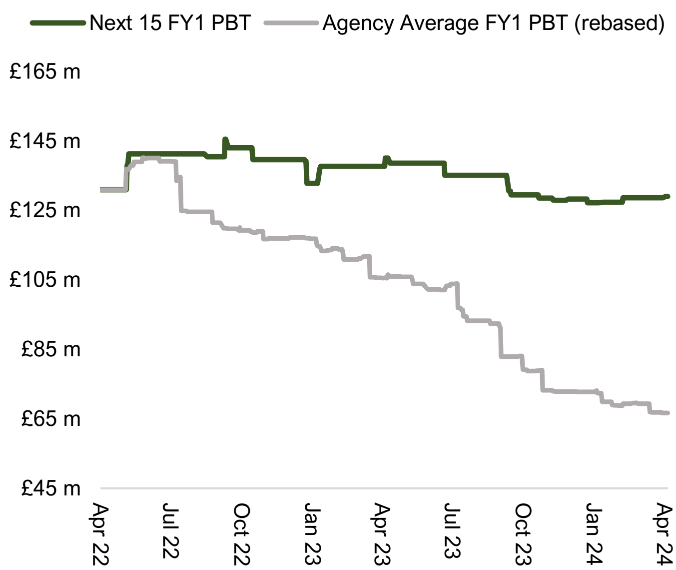


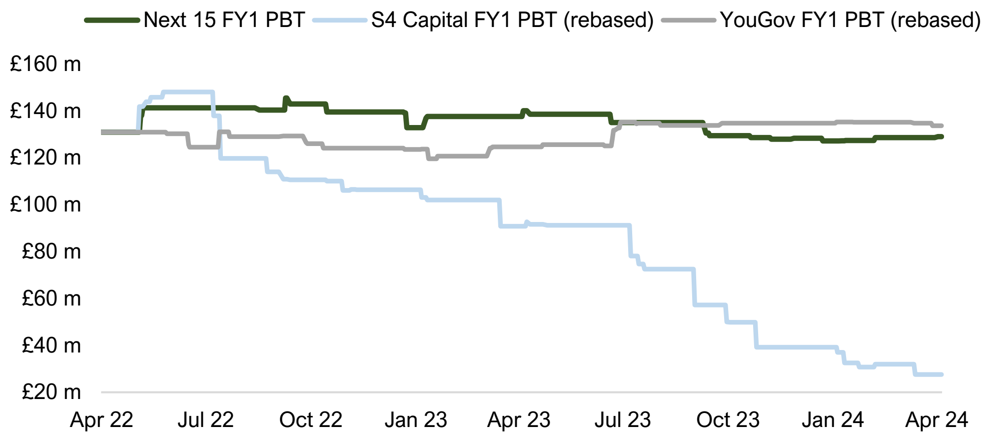
Figure 4: Next 15 vs Peers – Consensus **PBT**



Source: h2Radnor, FactSet

In Figure 5 below, we show the evolution of Next 15's FY1 consensus PBT with specific reference to YouGov and S4 Capital, which are arguably Next 15's closest natural peers in the market.

Figure 5: Next 15's FY1 PBT vs S4 Capital and YouGov

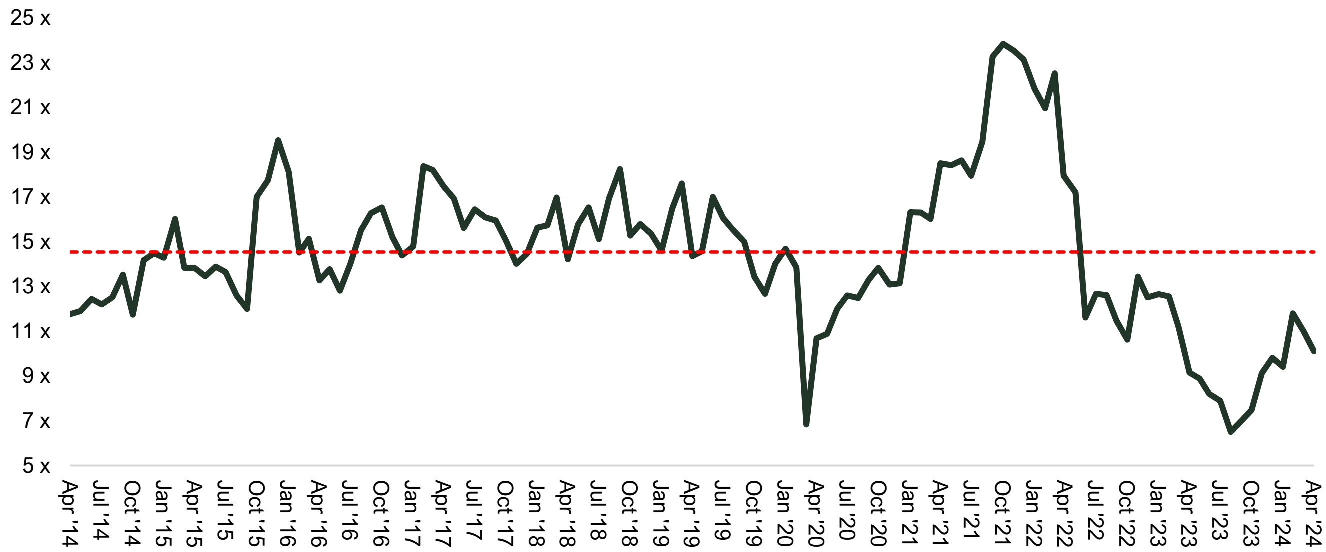


Source: FactSet, h2Radnor

We can see from Figure 5 that Next 15's FY1 PBT estimate has evolved broadly in line with YouGov, with both materially outperforming S4 Capital. We note that throughout this period the YouGov FY1 PE multiple has ranged between 19x and 30x.

Finally, to put this into its proper historic context, in Figure 6 below, we show the evolution of Next 15's FY1 PE multiple across a longer timeframe. Since April 2014, Next 15's average FY1 multiple was **14.5x** (including both the pandemic trough and early 2022 peak). If we were to apply this average this would suggest a Next 15 share price of **£12.64**, or 38% upside to the current price.

Figure 6: Long term evolution of Next 15's FY1 PE multiple



Source: FactSet, h2Radnor

Next 15 Group PLC

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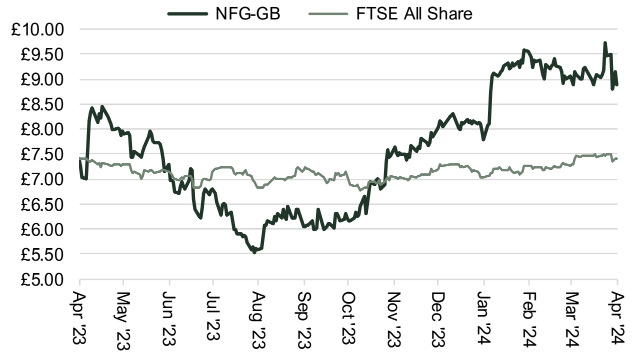
Price (p): **888 p**
Market Cap: 881 m
EV: 873 m

PROFIT & LOSS

Year to 31 January, £m	FY22	FY23	FY24	FY25e	FY26e	FY27e
Customer Engagement	*187.6*	*275.0*	*263.1*	*275.0*	*288.7*	*303.1*
Customer Delivery	*80.0*	*102.1*	*107.7*	*118.4*	*126.7*	*135.6*
Customer Insight	*42.1*	*52.0*	*57.5*	*63.2*	*68.3*	*73.7*
Business Transformation	*52.5*	*134.8*	*149.6*	*163.1*	*174.5*	*186.7*
Group Net Revenue	**362.1**	**563.8**	**577.8**	**619.7**	**658.2**	**699.1**
Customer Engagement	*40.4*	*55.4*	*53.2*	*58.3*	*62.1*	*66.7*
Customer Delivery	*28.5*	*30.2*	*29.1*	*33.7*	*37.4*	*42.0*
Customer Insight	*9.0*	*11.0*	*10.4*	*13.0*	*14.7*	*15.9*
Business Transformation	*15.2*	*43.9*	*48.3*	*48.9*	*52.3*	*56.0*
Head Office	*(13.8)*	*(26.4)*	*(19.8)*	*(22.3)*	*(24.4)*	*(26.6)*
EBITA - Adjusted	**79.3**	**114.2**	**121.1**	**131.6**	**142.1**	**154.0**
Associates & JV's	0.2	-	-	-	-	-
Net Bank Interest	(0.3)	(1.6)	(3.1)	(3.2)	(1.7)	(0.7)
PBT - Adjusted	**79.3**	**112.5**	**117.9**	**128.4**	**140.4**	**153.3**
Non Operating Items	(40.4)	(48.3)	(45.1)	(30.0)	(30.0)	(30.0)
Other Financial Items	(119.0)	(54.1)	7.5	(29.5)	(29.5)	(29.5)
PBT - IFRS	**(79.1)**	**10.1**	**80.3**	**67.8**	**79.8**	**92.7**
Tax	14.5	(7.1)	(26.4)	(18.3)	(21.6)	(25.0)
Tax - Adjusted	(17.2)	(26.3)	(31.1)	(34.7)	(37.9)	(41.4)
Tax rate - Adjusted	*21.6%*	*23.3%*	*26.3%*	*27.0%*	*27.0%*	*27.0%*
Minority interests	3.6	1.4	1.0	2.3	2.4	2.5
No. shares m	92.4	97.6	99.2	99.0	99.0	99.0
No. shares m, diluted	98.1	105.7	105.2	104.9	102.5	102.5
IFRS EPS (p)	(73.8)	1.7	53.3	47.7	56.4	65.8
Adj EPS (p), diluted	**59.7**	**80.4**	**81.6**	**87.2**	**97.6**	**106.7**
Total DPS (p)	12.0	14.6	15.4	16.1	17.8	19.4

PRICE CHART - 1 YEAR ABSOLUTE vs FTSE ALL SHARE



Source: FactSet

SHAREHOLDERS

	% of ord. Share capital
Octopus Investments	11.9%
Liontrust Investment Partners	10.0%
Aviva Investors	9.9%
Slater Investments	6.7%
Directors	5.5%
BlackRock	4.8%
JPMorgan AM	4.1%
abrdn	3.3%
	56.2%

CASH FLOW

Year to 31 January, £m	FY22	FY23	FY24	FY25e	FY26e	FY27e
Net Profit: (add back)	(64.6)	3.0	53.9	49.5	58.3	67.7
Depreciation & Amortisation	*28.8*	*37.2*	*36.6*	*37.5*	*38.0*	*38.5*
Net Finance costs	*120.3*	*57.1*	*(3.2)*	*33.8*	*32.3*	*31.3*
Tax	*(14.5)*	*7.1*	*26.4*	*18.3*	*21.6*	*25.0*
Working Capital	0.2	(24.4)	(10.7)	(15.5)	(2.1)	(2.2)
Other	19.6	15.1	2.0	(4.7)	(4.7)	(4.7)
Cash from Ops	**89.8**	**95.2**	**105.0**	**118.9**	**143.3**	**155.6**
Cash Tax	(14.1)	(20.3)	(25.4)	(18.3)	(21.6)	(25.0)
Tangible Capex	(3.1)	(3.5)	(3.7)	(4.0)	(4.0)	(4.0)
Intangible Capex	(2.7)	(3.5)	(3.4)	(3.5)	(3.5)	(3.5)
Free Cashflow	**69.9**	**67.9**	**72.5**	**93.1**	**114.3**	**123.0**
Dividends	(12.4)	(15.3)	(16.1)	(19.2)	(20.0)	(21.6)
Acquisitions & Inv.	(24.0)	(104.9)	(60.2)	(58.7)	(46.4)	(43.6)
Financing	(1.1)	38.6	1.1	(11.3)	(9.0)	(8.0)
Net Cashflow	**32.4**	**(13.7)**	**(2.6)**	**3.9**	**38.9**	**49.9**
Net Cash (Debt)	35.7	26.1	(1.4)	8.4	47.3	97.1

Announcements

Date	Event
April 2024	Final results
January 2024	Trading update
September 2023	H1 results
April 2023	Final results
January 2023	Trading update
September 2022	H1 results
May 2022	Bid for M&C Saatchi
March 2022	Engine acquisition & £50m placing

RATIOS

	FY23	FY24	FY25e	FY26e	FY27e
RoE	74.2%	54.9%	40.6%	43.1%	39.6%
RoCE	37.4%	36.9%	40.1%	48.2%	53.7%
Asset Turnover (x)	0.7x	0.7x	0.6x	0.6x	0.5x
NWC % Revenue	13.6%	8.6%	7.2%	10.4%	9.5%
Op Cash % EBITA	83.4%	86.8%	90.4%	100.8%	101.0%

BALANCE SHEET

Year to 31 January, £m	FY22	FY23	FY24	FY25e	FY26e	FY27e
Intangibles	183.1	274.1	279.3	277.4	271.4	264.4
P,P+E	7.5	10.9	10.1	9.9	9.6	9.1
Tax Asset & Other	75.6	97.2	88.4	85.4	82.4	79.4
Total Fixed Assets	**266.2**	**382.1**	**377.8**	**372.7**	**363.4**	**352.9**
Net Working Capital	(51.6)	(76.8)	(49.5)	(44.8)	(68.5)	(66.3)
Capital Employed	**214.5**	**305.3**	**328.4**	**327.9**	**294.8**	**286.6**
Earn Out Liabilities	(188.8)	(217.0)	(170.8)	(111.3)	(110.0)	(107.2)
Net Funds	35.7	26.1	(1.4)	8.4	47.3	97.1
Net Assets	**61.5**	**114.4**	**156.2**	**225.0**	**232.1**	**276.5**

VALUATION

Fiscal	FY23	FY24	FY25e	FY26e	FY27e
P/E	11.1x	10.9x	10.2x	9.1x	8.3x
EV/EBITDA	5.8x	5.5x	5.2x	4.8x	4.5x
Div Yield	1.6%	1.7%	1.8%	2.0%	2.2%
FCF Yield	7.8%	8.3%	10.7%	13.1%	14.1%
EPS growth	34.5%	1.5%	6.8%	12.0%	9.3%
DPS growth	21.7%	5.1%	5.2%	10.0%	9.3%

REGULATORY DISCLOSURES

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