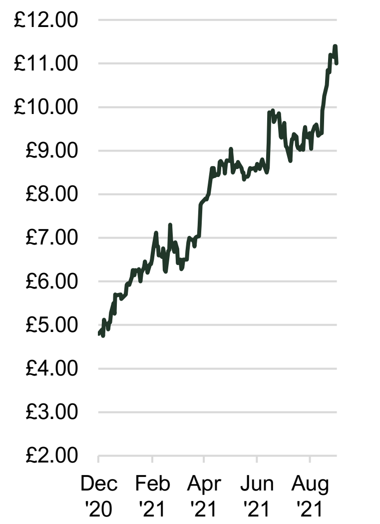
Next Fifteen Communications Group PLC

NFC | AIM | Media | 1100p | £1,057m

Q2 trading update – 5% revenue / PBT upgrade

1 Year Chart



13th September 2021

Iain Daly

id@radnorcp.com
+44 (0) 203 897 1832

Next Fifteen Communications Group PLC is a research client of Radnor Capital Partners Ltd.

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

Albeit against weak comparatives, Next Fifteen has released a strongly positive Q2 trading update with headline revenue growth +40% in Q2, of which organic growth was +29%. We saw in Q1 that organic growth momentum had started to equalise across both the B2B and B2C components of the portfolio and this trend has been maintained through Q2 and is likely to continue through H2. Margins continue to be strong; benefiting both from prior period cost actions / property rationalisation and also positive revenue and mix momentum. The trend of earnings upgrades has been maintained and we are ticking up our estimates accordingly (+5% revenue / PBT). The company has flagged both the increasing strength of prior year comparatives and higher levels of investment back into the business. This re-affirms our view that although margins will continue to improve the majority of immediate gains have been secured.

Next Fifteen shares have continued their strong run through the year with company now breaking through the £1bn market cap barrier. Unsurprisingly given the tone of trading commentary and the pace of earning upgrades, the forward PE multiple has expanded to 22.3x. Despite this upward re-rating (delivering +117% share price return YTD), Next Fifteens remains at a material discount to others in the peer group.

- **Revenue mix:** In a similar vein to the Q1 update, revenue momentum continues to be positive across the group. Under the new reporting structure, the Customer Engagement and Customer Insight divisions, the most exposed to the initial pandemic hit, have now fully recovered their lost ground. The Customer Delivery segment continues to be the standout performer, with Business Transformation growing fast off a relatively small base.
- **Internal investment to drive future scalability:** Other than re-affirming shorter term net revenue momentum, the standout comment in the trading update referred to the investments now being made across the group. There are two aspects here; firstly the addition of extra capacity and talent (a perrenial challenge) and secondly, investment in productisation. We discuss this in more detail below but this represents an interesting medium term opportunity.
- **Comparatives are getting tougher:** Given the pandemic timing, we fully expect the YoY growth rates to moderate for NFC through course of the second half. However, on a sequential basis we expect to see continued growth, both headline and organic.
- **Estimate upgrades:** We are upgrading our revenue and adjusted PBT estimates for FY22 by +5% respectively. An increased minorities charge drops through to a +2% EPS upgrade.

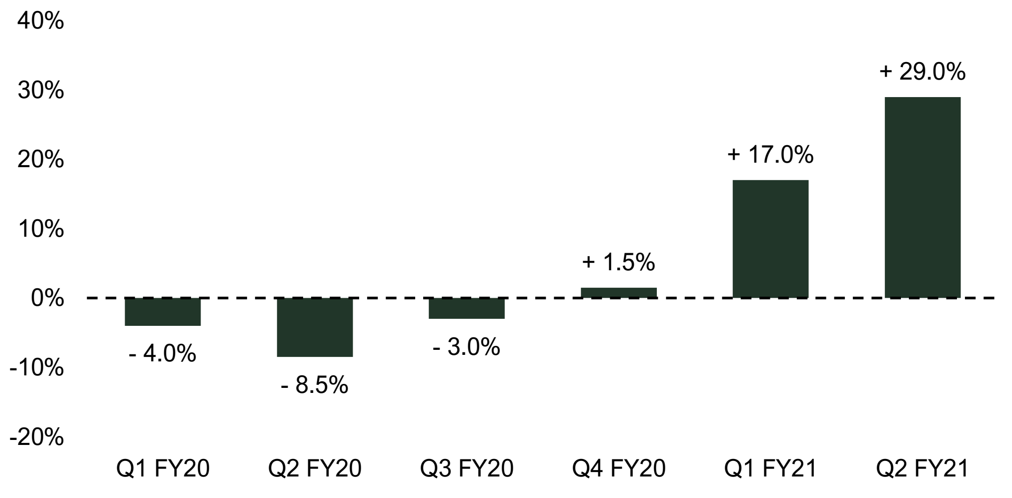
Y/E January, £m	Sales	PBT adj	EPS (p)	Div (p)	Net Cash	Fiscal PER x	Yield %
FY 2020A	248.5	40.2	34.8	2.5	-9.4	31.6	0.2
FY 2021A	266.9	49.1	40.7	7.0	14.0	27.0	0.6
FY 2022E	*329.7*	*65.1*	*49.2*	*10.3*	*22.0*	*22.3*	*0.9*
FY 2023E	*353.9*	*69.8*	*52.2*	*11.6*	*46.3*	*21.1*	*1.1*
FY 2024E	*376.4*	*75.7*	*56.6*	*12.6*	*87.2*	*19.4*	*1.1*

Source: Radnor Capital Partners

Organic growth has moved beyond recovery

In Figure 1 below, we show the quarterly progression of organic revenue growth by quarter through the course of FY'21 and into FY'22.

Figure 1: Quarterly organic revenue growth through FY'21

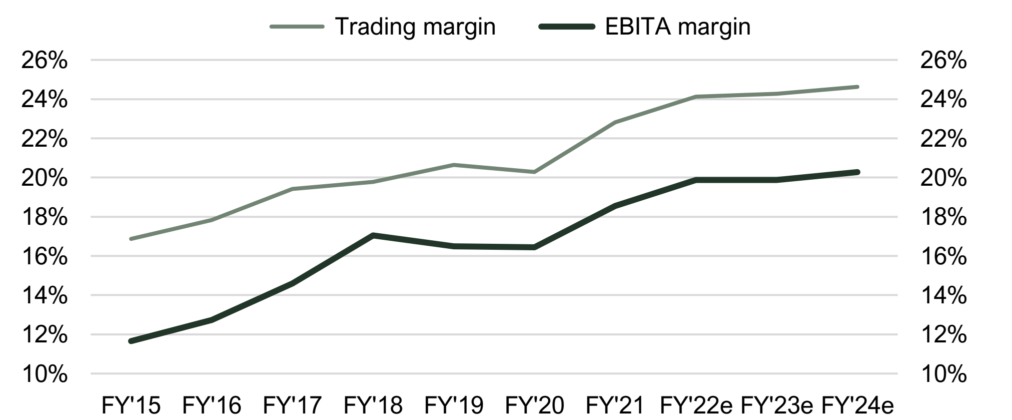


Source: Company, Radnor

It is now clear that NFC has moved beyond recovering the ground lost due to Covid. Anecdotal evidence from other companies in the sector (listed and private) confirms the strength of the current spending environment. If we look back to our pre-Covid FY22e revenue estimate, we had been looking for £281m of revenue. If we adjust this for the acquisitions of Shopper Media and Mach49 in the intervening period (c.£20m of acquired revenue), our current FY22e revenue estimate of £329.7m is now c.10% ahead.

The other interesting comparison with pre Covid estimates is at the margin line. Again, if we look back at our last pre-Covid estimate for FY22e, we had been looking for EBITA margins (pre-central overhead) of 22.3%, some 260 basis points below our latest estimate of 24.6%. According to our internal calculations, acquisitions represent c.50 basis points of this improvement with the combination of property cost savings and net revenue drop through accounting for the balance.

Figure 2: Group pre and post central overhead EBITA margins, FY15 to FY24E



Source: Company, Radnor

Business mix and profile

Next Fifteen's historic roots lie in public relations (albeit with a heavy North American and technology bias). However, this has changed markedly with all acquisitions over the last six years focused on digital marketing and technology agencies encompassing specialisms such as web design & build, online market research, specialist content marketing, innovation consulting, corporate venturing, sales activation and lead generation. Historically, Next Fifteen had segmented itself into three silos; **Brand Marketing**, **Data & Analytics** and **Creative Technology**, with the former representing the original PR and marketing core. However, this segmentation did not accurately reflect the diversity of the group's parts, nor the likely future direction of M&A investment.

NFC had previously highlighted the adoption of a new reporting structure to better capture the full diversity of the group's activities. Alongside the Q2 update, NFC has provided a more detailed breakdown of the historic comparatives according to the new reporting structure. We have re-aligned our estimates into this new format.

Figure 3: New group segmentation

Customer Insight		Customer Engagement		Customer Delivery		Business Transformation	
Analytics, data and research led. Enabling clients to make better marketing & product decisions		*Content, strategy and message creation and delivery.*		*Sales delivery through the application of technology and data*		*Organisational value maximisation through investment and transformation*	
FY21 Revenue	**£33.1m**	*FY21 Revenue*	**£166.5m**	*FY21 Revenue*	**£49.6m**	*FY21 Revenue*	**£17.7m**
FY21 EBITA	**£4.9m**	*FY21 EBITA*	**£36.9m**	*FY21 EBITA*	**£15.2m**	*FY21 EBITA*	**£3.9m**
FY21 Margin	**14.7%**	*Margin*	**22.1%**	*Margin*	**30.7%**	*Margin*	**22.0%**
Organic growth	**5% - 10%**	*Organic growth*	**3% - 7%**	*Organic growth*	**10% - 15%**	*Organic growth*	**10% - 15%**

Source: Company

- **Customer Engagement** is most analogous to the historic **Brand Marketing** segment and includes the larger US agencies Archetype and M Booth. Also included within Engagement will be content marketing agencies such as Publitek.

- **Customer Insight** represents the research and analytics businesses such as Savanta. The 15% FY21 contribution margin was depressed by pandemic impacts as clients in this segment are typically more B2C focused. We expect Insight to see margins trend into the high teens as normalised trading fully annualises.

- **Customer Delivery** is based around the concept of demand, lead and sales generation through the use of technology or data insights. This is the fastest growing and highest margin part of the group and has proven to be the most insulated against the worst impacts of the pandemic. Newer businesses within the Next Fifteen portfolio such as Activate and Agent3 sit within this segment.

- **Business Transformation** is based around the concept of digital transformation and corporate value enhancement and is the furthest away from the traditional marketing universe. Mach49 and Palladium are focused on helping established businesses combat disruptive threats through corporate venturing and VC style investing. Elsewhere, the IPO / IR agency, Blueshirt, will sit within this segment.

- **Future M&A focus** is likely to revolve around Insight, Delivery and Transform. These are the areas that are most data led and aligned with client growth and value ambitions. In this sense, we do not see a marked departure from the established M&A model which has focused on areas outside the traditional communications arena. Not only are margins structurally superior but businesses tend to be less mature and offer faster growth.

- **Productisation is a new theme.** The comment in the Q2 update that most caught our attention was around the growing investment in productisation. Historically, much of NFC's component agency economics revolved around consultancy and time / materials delivery. Whilst offering attractive margins by traditional sector standards (c.15% - 20% pre-central overhead) they are naturally scale bound.

A number of the newer businesses within NFC have the clear potential to offer data driven product opportunities (build one, sell many); especially from within the Business Transformation and Customer Delivery segments. This is unlikely to be a material short term opportunity but has the potential to be more meaningful over the medium term. The attraction here is in the inherent scalability of product margins; particularly those that are based on data and insight propositions.

Estimate Revisions: PBT +6% for FY 2022, +6% for FY 2023

We have revisited our forecast model and have made the following changes:

Figure 4: Radnor estimate revisions

		Previous		New		*Change, %*	
£m	FY21A	2022E	2023E	**2022E**	**2023E**	**2022E**	**2023E**
Customer Engagement	166.5			199.8	211.8		
Customer Delivery	49.6			61.9	68.1		
Customer Insight	33.1			41.3	44.6		
Business Transformation	17.7			26.6	29.2		
Revenue	**266.9**	**314.7**	**333.1**	**329.7**	**353.9**	***+ 5%***	***+ 6%***
Customer Engagement	36.9			46.6	49.6		
Customer Delivery	15.2			19.8	21.9		
Customer Insight	4.9			7.0	7.7		
Business Transformation	3.9			6.1	6.7		
Central Overhead	-11.4	-13.4	-14.2	-14.0	-15.6	*+ 5%*	*+ 10%*
EBITA	**49.5**	**61.7**	**66.0**	**65.5**	**70.3**	***+ 6%***	***+ 7%***
- margin %	*18.5%*	*19.6%*	*19.8%*	*19.9%*	*19.9%*		
Adj. PBT	**49.1**	**61.9**	**66.3**	**65.1**	**69.8**	***+ 5%***	***+ 5%***
Adj. EPS (p)	**40.7**	**48.5**	**51.5**	**49.2**	**52.2**	***+ 2%***	***+ 1%***
Dividend (p)	7.0	11.0	12.9	10.3	11.6	*- 7%*	*- 10%*
Net Cash (Debt)	**14.0**	**18.4**	**44.3**	**22.0**	**46.3**		

Source: Radnor

Valuation

Figure 5: Next Fifteen FY2 **PE**

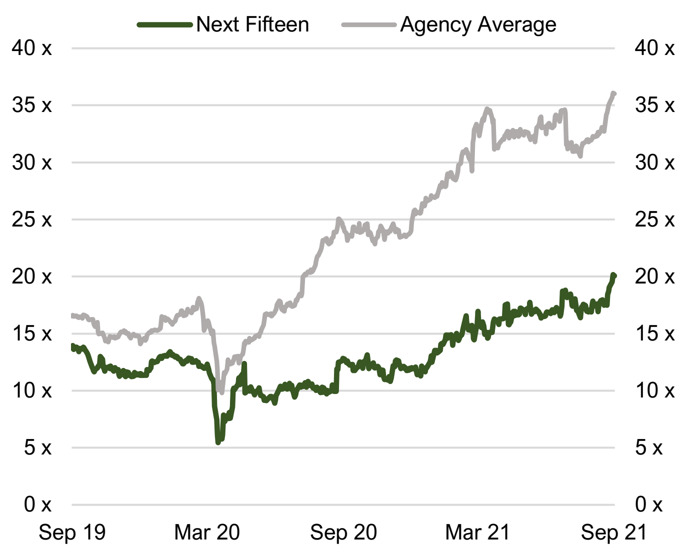
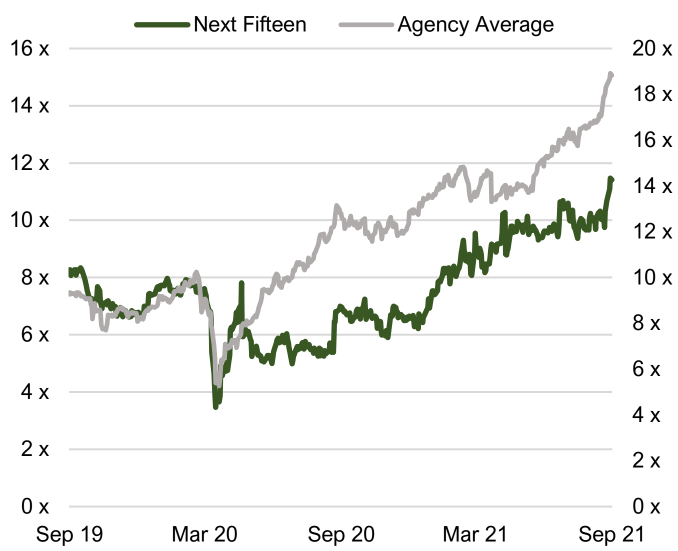


Figure 6: Next Fifteen FY2 **EV/EBITDA**



Source: FactSet, Radnor

In Figures 5 & 6 above, we show the evolution of the Next Fifteen FY2 PE and EV/EBITDA multiple over the last two years, compared to the Small Cap Agency average. We have focused on FY2 earnings as short-term earnings volatility is clearly pronounced in the current year and we believe investors have now moved beyond their initial focus on near term security and are looking through to the 2022 earnings outlook.

In Figures 7 and 8 below, we compare Next Fifteen to the peer group and Small Cap Media average in terms of PE vs Revenue Growth and PE vs EBITDA margins. On both measures we can see that Next Fifteen sits well ahead of the peer group averages in terms of both growth and margin, yet still does not command the premium multiples shown by a number of peers.

Figure 7: Next Fifteen FY2 **PE**

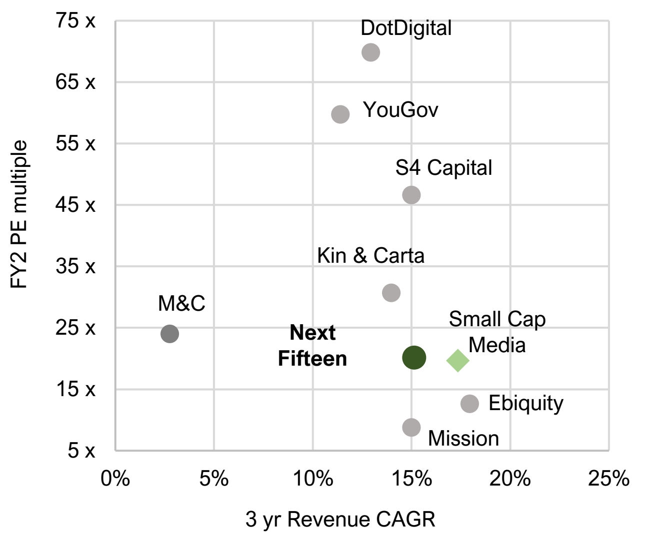
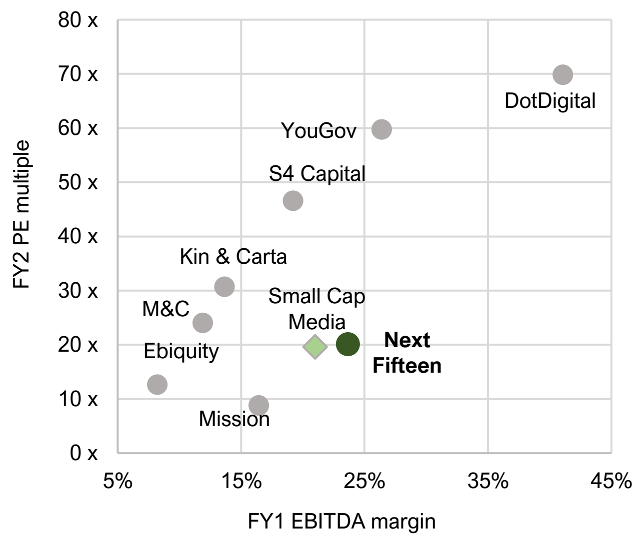


Figure 8: Next Fifteen FY2 **EV/EBITDA**



Source: FactSet, Radnor

Next Fifteen Communications PLC

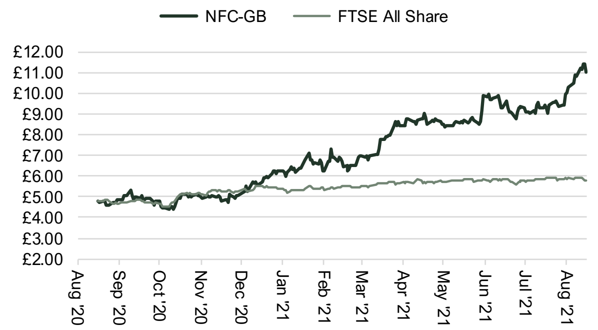
Iain Daly
+44 203 897 1832
id@radnorcp.com

Price (p):	**1100 p**
Market Cap:	1,057 m
EV:	1,043 m

PROFIT & LOSS

Year to 31 January, £m	FY18	FY19	FY20	FY21	FY22e	FY23e	FY24e
Customer Engagement				*166.5*	*199.8*	*211.8*	*222.4*
Customer Delivery				*49.6*	*61.9*	*68.1*	*73.6*
Customer Insight				*33.1*	*41.3*	*44.6*	*48.2*
Business Transformation				*17.7*	*26.6*	*29.2*	*32.2*
Group Net Revenue	**196.8**	**224.1**	**248.5**	**266.9**	**329.7**	**353.9**	**376.4**
Customer Engagement				*36.9*	*46.6*	*49.6*	*52.9*
Customer Delivery				*15.2*	*19.8*	*21.9*	*23.9*
Customer Insight				*4.9*	*7.0*	*7.7*	*8.4*
Business Transformation				*3.9*	*6.1*	*6.7*	*7.4*
Head Office	*(8.9)*	*(9.3)*	*(9.5)*	*(11.4)*	*(14.0)*	*(15.6)*	*(16.4)*
EBITA - Adjusted	**30.0**	**37.0**	**40.9**	**49.5**	**65.5**	**70.3**	**76.3**
Associates & JV's	0.0	0.1	0.2	0.4	0.2	-	-
Net Bank Interest	(0.7)	(1.0)	(0.8)	(0.8)	(0.6)	(0.6)	(0.6)
PBT - Adjusted	**32.8**	**36.0**	**40.2**	**49.1**	**65.1**	**69.8**	**75.7**
Non Operating Items	(12.8)	(16.3)	(23.0)	(37.2)	(22.8)	(23.2)	(20.0)
Other Financial Items	(3.2)	(0.9)	(11.6)	(13.2)	(10.5)	(10.0)	(10.0)
PBT - IFRS	**13.3**	**18.8**	**5.6**	**(1.3)**	**30.4**	**35.2**	**44.3**
Tax	(4.0)	(4.3)	(2.7)	(2.6)	(6.2)	(8.8)	(11.1)
Tax - Adjusted	(5.9)	(7.2)	(8.0)	(9.9)	(15.3)	(16.7)	(18.2)
Tax rate - Adjusted	*17.9%*	*20.0%*	*20.0%*	*20.2%*	*23.5%*	*24.0%*	*24.0%*
Minority interests	0.7	0.6	0.6	1.0	3.6	4.0	4.5
No. shares m	74.3	79.2	85.3	89.4	89.4	89.4	89.4
No. shares m, diluted	82.1	85.0	90.9	93.8	93.8	93.8	93.8
IFRS EPS (p)	11.6	17.5	2.7	(5.5)	23.0	25.0	32.2
Adj EPS (p), diluted	**32.1**	**33.1**	**34.8**	**40.7**	**49.2**	**52.2**	**56.6**
Total DPS (p)	6.3	7.6	2.5	7.0	10.3	11.6	12.6

PRICE CHART - 1 YEAR ABSOLUTE vs FTSE ALL SHARE



Source: FactSet

SHAREHOLDERS

	% of ord. Share capital
Octopus Investments	13.4%
Liontrust Investment Partners	11.8%
Aviva Investors	9.3%
Aberdeen Stan Life	8.1%
Directors	6.5%
BlackRock	6.2%
Canaccord Wealth	4.9%
Herald Inv Mgmt	4.5%
	64.7%

CASH FLOW

Year to 31 January, £m	FY18	FY19	FY20	FY21	FY22e	FY23e	FY24e
Net Profit: (add back)	9.3	14.5	2.8	(3.9)	24.2	26.4	33.2
Depreciation & Amortisation	*11.4*	*13.8*	*26.4*	*28.0*	*27.6*	*28.0*	*28.3*
Net Finance costs	*4.0*	*1.9*	*14.1*	*15.4*	*12.5*	*12.0*	*12.0*
Tax	*4.0*	*4.3*	*2.7*	*2.6*	*6.2*	*8.8*	*11.1*
Working Capital	(4.2)	1.2	(3.3)	6.6	(5.2)	(5.2)	(0.7)
Other	4.4	2.6	6.8	24.3	8.8	9.0	9.0
Cash from Ops	**28.9**	**38.4**	**49.5**	**72.9**	**74.1**	**78.9**	**93.0**
Cash Tax	(4.3)	(6.2)	(6.0)	(8.4)	(6.2)	(8.8)	(11.1)
Tangible Capex	(3.0)	(5.6)	(3.5)	(2.0)	(4.0)	(4.0)	(4.0)
Intangible Capex	(1.2)	(2.4)	(1.8)	(2.1)	(2.0)	(2.0)	(2.0)
Free Cashflow	**20.4**	**24.1**	**38.2**	**60.4**	**61.9**	**64.1**	**75.9**
Dividends	(5.7)	(6.6)	(7.5)	(0.7)	(7.3)	(10.2)	(11.4)
Acquisitions & Inv.	(15.4)	(29.6)	(24.2)	(23.6)	(34.0)	(17.0)	(11.0)
Financing	3.8	7.7	1.8	(37.7)	(12.7)	(12.7)	(12.7)
Net Cashflow	**3.1**	**(4.4)**	**8.3**	**(1.6)**	**7.9**	**24.3**	**40.9**
Net Cash (Debt)	(11.6)	(5.2)	(9.4)	14.0	22.0	46.3	87.2

Announcements

Date	Event
August 2021	Trading update
April 2021	Final results (y/e Jan 2021)
April 2021	Acquisition of Shopper Media for £15m
January 2021	Trading update
September 2020	Trading update
September 2020	Acquisition of Mach49 for $2.7m
April 2020	Final results (y/e Jan 2020)

RATIOS

	FY20	FY21	FY22e	FY23e	FY24e
RoE	28.1%	32.7%	33.4%	30.6%	27.8%
RoCE	33.6%	48.5%	56.4%	61.7%	73.8%
Asset Turnover (x)	0.9x	0.8x	0.6x	0.6x	0.5x
NWC % Revenue	41.2%	42.4%	29.4%	26.7%	24.9%
Op Cash % EBITA	121.2%	147.4%	113.1%	112.2%	121.9%
Net Debt / EBITDA	0.1x	-	-	-	-

BALANCE SHEET

Year to 31 January, £m	FY18	FY19	FY20	FY21	FY22e	FY23e	FY24e
Intangibles	94.8	126.1	155.4	163.8	164.8	168.8	166.8
P,P+E	13.6	15.9	14.2	8.9	13.3	12.3	11.0
Tax Asset & Other	11.7	13.0	54.7	43.4	35.4	27.4	19.4
Total Fixed Assets	**120.1**	**155.0**	**224.4**	**216.1**	**213.4**	**208.5**	**197.1**
Net Working Capital	(32.2)	(38.4)	(102.3)	(113.2)	(96.9)	(94.4)	(93.7)
Capital Employed	**87.9**	**116.6**	**122.1**	**102.9**	**116.5**	**114.1**	**103.4**
Net Funds	(11.6)	(5.2)	(9.4)	14.0	22.0	46.3	87.2
Net Assets	**76.3**	**111.5**	**112.7**	**116.9**	**138.5**	**160.3**	**190.6**

VALUATION

Fiscal	FY20	FY21	FY22e	FY23e	FY24e
P/E	31.6x	27.0x	22.3x	21.1x	19.4x
EV/EBITDA	15.2x	13.5x	15.9x	14.8x	13.7x
Div Yield	0.2%	0.6%	0.9%	1.1%	1.1%
FCF Yield	3.7%	5.8%	5.9%	6.1%	7.3%
EPS growth	4.9%	17.1%	20.9%	6.1%	8.3%
DPS growth	-66.9%	180.0%	46.5%	13.2%	8.3%

REGULATORY DISCLOSURES

Radnor Capital Partners Ltd is authorised and regulated by the Financial Conduct Authority.

Radnor Capital Partners Ltd
1 King Street
London
EC2V 8AU

www.radnorcp.com

DISCLAIMER

This report is not intended as a solicitation or inducement to buy, sell, subscribe or underwrite 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. However, Radnor Capital Partners Ltd does have strict rules relating to personal dealings by individuals employed or instructed to help prepare investment research. A copy of these rules is available upon request. Radnor Capital Partners Ltd 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 contracted persons or entities may have a position in any or related securities mentioned in this report. Radnor Capital Partners Ltd, 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 can be subject to volatility. In addition, it may be difficult to 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. To the maximum extent permitted by law, Radnor Capital Partners Ltd, or its affiliates and their respective directors, officers and employees will not be held liable for any loss or damage 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.