

GB Group

Business as usual

FY17 results

Following April's trading update, GB Group's (GBG) FY17 results held no major surprises, with the fraud, risk management and location services continuing to underpin strong growth. The incoming CEO plans to continue to execute the group's internationalisation strategy and investment will be managed to maintain EBITA margins at c 20% over the medium term; while marginally lower than our FY19 assumption, we raise our EPS forecasts by c 4% in FY18 and c 2% in FY19 reflecting a lower expected tax rate.

Year end	Revenue (£m)	EBITA* (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
03/16	73.4	13.4	13.2	8.2	2.1	47.4	0.5
03/17	87.5	17.0	16.5	9.9	2.4	39.2	0.6
03/18e	117.1	23.3	22.6	12.0	2.5	32.4	0.6
03/19e	133.4	27.0	26.4	13.6	2.8	28.6	0.7

Note: *EBIT, PBT and EPS (fully diluted) are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

Tax boost to FY17 earnings

Revenues of £87.5m (+19% y-o-y, of which 12% was organic) and EBITA of £17.0m (+27%) were in line with April's trading update. The group benefited from a tax credit (versus the 21% tax charge we had forecast) as a result of movements to its deferred tax asset and the increased use of patent box tax relief, which boosted the group's earnings; adjusting for this, adjusted EPS was in line with our forecast. All service lines – bar ID Engage, which is experiencing some competitive pressure – grew strongly, particularly the fraud and risk management products. A dividend of 2.35p (+13% y-o-y) has been proposed.

Incoming CEO; global aspects unique

CEO Chris Clark joined GBG in April, replacing Richard Law. Although early in his tenure, he outlined his initial views on the group and its strategy, which is unlikely to see a major change in direction, with the focus remaining on driving the globalised nature of both the data sets and customer base, features he considers unique to the group. Management plans to hold EBITA margins at the 20% level as it steps up investment to integrate the product offerings and expand its capabilities in the faster growing segments; we update our forecasts to reflect this although, net of a slightly lower tax rate, we increase our FY18 and FY19 EPS forecasts by c 4% and c 2% respectively.

Valuation: Organic and acquisition prospects

43% of GBG's revenues are coming from fraud and risk management services. On an FY18e P/E of 32x, the shares are already factoring in the group's superior growth prospects to other identity management groups (average FY17 P/E of 25x), but trade at a discount to the wider internet security peer set (average FY17 P/E of 45x). We believe the organic opportunities open to the group support the rating at these levels and, with an active acquisition strategy and a strong M&A track record, there is room for further growth-driven share price upside.

Software & comp services

8 June 2017

Price 388.50p
Market cap £590m

Net cash (£m) 31 March 2017	5.2
Shares in issue	151.8m
Free float	97%
Code	GBG
Primary exchange	AIM
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	9.4	28.4	22.9
Rel (local)	7.3	25.5	3.8
52-week high/low	406.0p	215.0p	

Business description

GB Group (GBG) has complementary identity data intelligence offerings of verification, capture, maintenance and analysis, enabling companies to identify and understand their customers.

Next events

AGM	26 June 2017
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FY17 results summary – tax benefit boosts earnings

Revenue growth of 19% to £87.5m and adjusted EBITA of £17.0m, up 27%, had been pre-announced in April's trading update.

Net of £498k finance costs, adjusted PBT of £16.5m (up 25% y-o-y) was in line with our forecasts. However, GBG's adjusted EPS of 13.1p (up 24% y-o-y), which was considerably ahead of our forecast (9.7p) was flattered by a £668k tax credit as a result of changes to deferred tax entitlements, R&D and patent box tax relief (which allows companies to apply for a lower rate of corporation tax for earnings related to its patented inventions). In our calculation of adjusted EPS for FY17 we use an adjusted tax rate of 21%, which implies an adjusted EPS of 9.9p (+20% y-o-y). Although our measure of EPS is conservative, we believe it gives a more meaningful picture of the group's underlying longer-term earnings pattern.

Reported PBT of £10.1m (up 8% y-o-y) captures a higher charge for amortisation of acquired intangibles of £4.0m following the acquisition of ID Scan during the year, as well as associated exceptional costs relating to its acquisition of £1.4m and share-based payments of £1.0m.

Operating cash flow of £16.3m (FY16: £13.4m) equates to an 87% cash conversion, slightly down on FY16 (91%) owing to the strong growth experienced in Asia and from the financial services sector where payment cycles tend to be longer. The group is setting up a wholly foreign-owned enterprise (WFOE) in the region, which should improve the payment cycles (as the organisation would be registered in China and can deal in local currencies).

Exhibit 1: Summary financials

£000s	2016a	2017 forecast	2017 actual	Variance to forecast (%)	% change (y-o-y)
Total revenue	73,401	87,500	87,468	0	19
Gross profit	55,795	66,926	67,166	0	20
Gross margin	76.0%	76.5%	76.8%	0	
EBITDA	14,772	19,200	18,734	(2)	27
Total EBITA	13,428	17,000	17,006	0	27
EBITA margin	18.3%	19.4%	19.4%	0	6
Amortisation of acquired intangibles	(2,501)	(2,540)	(4,022)	58	61
Share based payments	(1,245)	(1,600)	(994)	(38)	(20)
Exceptional items	(94)	(1,200)	(1,410)	18	NM
Share of associate	-	-	-	-	-
Reported operating profit	9,588	11,660	10,580	(9)	10
Finance charges	(270)	(500)	(498)	0	84
PBT - adjusted	13,158	16,500	16,508	0	25
PBT - reported	9,318	11,160	10,082	(10)	8
tax	(178)	(3,630)	668		
FX	1,096	-	3,685		236
Net profit	10,236	7,530	14,435	92	41
EPS (p) - adjusted, diluted (Edison basis)	8.2	9.7	9.9	2	20
EPS (p) - adjusted, diluted (GBG basis)	10.6	9.7	13.1	35	24
EPS (p) - reported, basic	7.4	5.9	8.2	38	13
Net cash	8,673	2,490	5,181	108	(40)

Source: GB Group (actuals), Edison Investment Research

Divisional analysis and outlook

Total revenue growth of 19% reflects very strong 33% growth from IDP (Identity Proofing) and a solid 8% growth from IDS (ID Solutions). Across the portfolio fraud and risk management (which was also boosted by the acquisition of ID Scan) continue to perform very strongly, as did Identify Registration and Loqate solutions. The ID Engage services were the only area of weakness during the year, affected by an intense competitive climate. Adjusting for the prior year revenues related to Gov.uk/verify and the impact of acquisitions (Loqate and ID Scan), organic growth was 12% across the year.

EBITA margin of 19.4% increased y-o-y despite the £2m losses from GBG's recently launched Gov.uk/verify service, which has been slower to take off than initially expected. Excluding this investment, underlying EBITA margins were closer to 21.8%.

Exhibit 2: Divisional revenues					
£m	2016a	2017 forecast	2017 actual	Variance to forecast (%)	% change (y-o-y)
Risk management	19.8		27.6		39
Fraud management	8.4		10.8		29
Employment checks	5		5.9		18
Total IDP	33.2	44.5	44.2	(1)	33
Registering identities	18		21.8		21
Building relationships (engage)	12.3		10.4		(15)
Locating people	9.9		11.0		11
Total IDS	40.2	43.0	43.3	1	8
Total revenues	73.4	87.5	87.5	0	19
Adjustment for organic growth calculations:					
Acquisition impact: Loqate and ID Scan			(6.7)		
Gov.uk/verify	(1.6)		(0.1)		
Adjusted organic revenues	71.8		80.7		12
IDP EBITA	6.6	8.8	8.4	(5)	26
IDP EBITA margin	20.0%	19.7%	18.9%		
IDS EBITA	7.7	9.3	9.3	1	21
IDP EBITA margin	10.5%	10.6%	10.7%		
Group/other)	(0.9)	(1.0)	(0.7)	(33)	(24)
Total EBITA	13.4	17.0	17.0	0	27
EBITA margin	18.3%	19.4%	19.4%	0	6

Source: GB Group

Outlook and forecasts

Chris Clark, the incoming CEO replacing Richard Law, joined the group in April. Although still early in his tenure, his initial assessment is that the group should continue to build on its core strengths, in particular:

- Further expanding the international footprint by rolling out more of its product sets on a wider basis; three of GBG's products are currently available internationally and revenues from outside the UK increased to 31% in FY17 (26% in FY16).
- Continuing to expand its access to global data sets, increasingly important for companies as they internationalise and already a unique feature of the group; GBG draws on 426 data sets (FY16: 338) across 190 markets.
- Adding capabilities, both organically and by acquisition.

Chris Clark also sees an opportunity to strengthen GBG's brand awareness and, by improving the integration of its product portfolio and technologies, extend the cross-sell of services into its customer base. Once the group reaches its targeted 20% EBITA margin (which we forecast during FY18), it intends to maintain margins at around this level by stepping up investment in these areas, as well as expanding its capabilities in the faster growing areas of fraud and risk management.

With the exception of ID Engage (which accounted for 12% of revenues in FY17), we expect the other product areas to continue to grow strongly. No specific guidance has been provided, although 70% of GBG's revenues recurring in nature, organic growth remained strong in H217 and the deferred income balance of £19m increased 38% y-o-y (of which 19% is from the acquisition of ID Scan), consistent with continued solid growth.

We make no changes to our revenue forecasts, although we trim our FY19 EBITA margin forecast in FY19 from 20.5% to approximately 20% to reflect a slightly higher level of R&D expense. We also lower our notional tax charge from 21% to 19% to take account of the likely ongoing benefit from the patent box tax relief, which means overall a slight increase to our EPS forecast in FY18 (4%) and FY19 (2%). We summarise our forecast changes in Exhibit 3 below and present forecasts in full at the back of this report.

Exhibit 3: Summary forecast changes

£000s	2018e			2019e		
	Previous	New	Change (%)	Previous	New	Change (%)
Revenues	117,093	117,093	0.0	133,352	133,352	0.0
EBITA	23,300	23,300	0.0	27,300	27,000	(1.1)
PBT	22,550	22,550	0.0	26,700	26,400	(1.1)
EPS (p) - normalised, diluted	11.5	12.0	4.4	13.4	13.6	1.8
EPS (p) - reported	7.5	7.2	(4.4)	10.9	10.8	(1.0)

Source: Edison Investment Research

Valuation: Widening opportunities underpins P/E premium

The shares performed strongly over the last three months and now trade on P/Es of 32.4x FY18e and 28.6x FY19e, and an EV/EBITA of 25.1x and 21.6x respectively. While the shares are already factoring in the group's superior growth prospects to other identity management groups (which trade on an average P/E of 25x FY1), with 43% of revenues now coming from fraud and risk management services we believe this rating should be taken in the context of the wider internet security peer set, which trades on an average P/E of 45x FY1.

Investors should also bear in mind the group's acquisition strategy and track record. GBG has made 10 acquisitions over the last five years, adding capabilities, data sets and client reach, as well as driving revenue and cost synergies; DecTech (acquired in April 2014), for instance, has seen growth accelerate from 5-10% to 20-30% since acquisition, and has facilitated the launch of new products internationally (eg the fraud bureaus). The acquisition of ID Scan (June 2016) was also in line with this strategy and ID Scan reports an enlarged pipeline since it has been integrated into the group and was earnings accretive in its first full year. More recently, PCA Predict, which complements GBG's existing address intelligence services, is also expected to be earnings accretive in its first year despite a planned increase in investment.

The global market for identity data intelligence services remains fragmented, which we believe will provide GBG with a steady pipeline of acquisition opportunities. At the year-end GBG reported £5.2m of net cash. Since the year-end it has paid £66m (cash) for PCA Predict (please see our [May update note](#) for more information on this acquisition), financed in part with a £58m share placing. In addition, during FY18 it will satisfy earnouts related to the ID Scan acquisition of approximately £7m. Inclusive of these payments we forecast year-end net debt of £0.1m. The group also has undrawn bank facilities in place of approximately £40m.

Exhibit 4: Financial summary

	£'000s	2014	2015	2016	2017	2018e	2019e
March		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS							
Revenue		41,835	57,283	73,401	87,468	117,093	133,352
Cost of Sales		(14,473)	(16,448)	(17,606)	(20,302)	(28,822)	(32,797)
Gross Profit		27,362	40,835	55,795	67,166	88,271	100,554
EBITDA		7,849	11,844	14,772	18,734	26,200	30,305
Operating Profit (before amort. and except.)		7,164	10,790	13,428	17,006	23,300	27,000
Acquired intangible amortisation		(1,110)	(1,986)	(2,501)	(4,022)	(3,500)	(3,000)
Exceptionals		(1,080)	(1,629)	(94)	(1,410)	(2,200)	0
Share of associate		(159)	(10)	0	0	0	0
Share based payments		(747)	(971)	(1,245)	(994)	(1,750)	(1,699)
Operating Profit		4,068	6,194	9,588	10,580	15,850	22,301
Net Interest		(79)	(266)	(270)	(498)	(750)	(600)
Profit Before Tax (norm)		7,085	10,524	13,158	16,508	22,550	26,400
Profit Before Tax (FRS 3)		3,989	5,928	9,318	10,082	15,100	21,701
Tax		(474)	(1,127)	(178)	668	(4,510)	(5,280)
Profit After Tax (norm)		5,597	8,314	10,395	13,206	18,040	21,120
Profit After Tax (FRS 3)		3,515	4,801	9,140	10,750	10,590	16,421
Average Number of Shares Outstanding (m)		109.6	119.1	122.7	131.6	147.6	152.5
EPS - normalised (p)		5.1	7.0	8.5	10.0	12.2	13.8
EPS - normalised and fully diluted (p)		4.8	6.7	8.2	9.9	12.0	13.6
EPS - (IFRS) (p)		3.2	4.0	7.4	8.2	7.2	10.8
Dividend per share (p)		1.7	1.9	2.1	2.4	2.5	2.8
Gross Margin (%)		65.4	71.3	76.0	76.8	75.4	75.4
EBITDA Margin (%)		18.8	20.7	20.1	21.4	22.4	22.7
Operating Margin (before GW and except.) (%)		17.1	18.8	18.3	19.4	19.9	20.2
BALANCE SHEET							
Fixed Assets		26,985	51,238	59,364	105,653	175,953	172,298
Intangible Assets		23,329	45,296	54,113	98,753	169,153	166,003
Tangible Assets		1,519	2,829	2,234	2,856	2,756	2,251
Other fixed assets		2,137	3,113	3,017	4,044	4,044	4,044
Current Assets		23,775	33,186	36,189	48,187	66,455	85,443
Debtors		11,929	17,408	23,774	30,569	47,290	54,493
Cash		11,846	15,778	12,415	17,618	19,165	30,949
Other		0	0	0	0	0	0
Current Liabilities		(17,861)	(30,784)	(32,559)	(44,444)	(58,665)	(63,568)
Creditors		(17,861)	(24,305)	(30,927)	(36,436)	(50,657)	(55,560)
Contingent consideration		0	(5,733)	(1,050)	(7,122)	(7,122)	(7,122)
Short term borrowings		0	(746)	(582)	(886)	(886)	(886)
Long Term Liabilities		(2,066)	(7,506)	(6,593)	(15,940)	(23,040)	(19,040)
Long term borrowings		0	(3,643)	(3,160)	(11,499)	(18,599)	(14,599)
Contingent consideration		0	(895)	0	0	0	0
Other long term liabilities		(2,066)	(2,968)	(3,433)	(4,441)	(4,441)	(4,441)
Net Assets		30,833	46,134	56,401	93,456	160,703	175,132
CASH FLOW							
Operating Cash Flow		9,355	11,684	13,397	16,305	21,500	28,005
Net Interest		(79)	(266)	(282)	(498)	(750)	(600)
Tax		65	(337)	(248)	(2,193)	(4,510)	(5,280)
Capex		(1,144)	(2,011)	(1,762)	(2,227)	(2,700)	(2,650)
Acquisitions/disposals		(1,443)	(18,672)	(12,263)	(36,840)	(74,000)	0
Financing		416	10,954	790	24,788	58,000	0
Dividends		(1,632)	(1,955)	(2,277)	(2,775)	(3,093)	(3,691)
Net Cash Flow		5,538	(603)	(2,645)	(3,440)	(5,553)	15,784
Opening net debt/(cash)		(6,308)	(11,846)	(11,389)	(8,673)	(5,233)	320
HP finance leases initiated		0	0	0	0	0	0
Other		0	146	(71)	0	0	0
Closing net debt/(cash)		(11,846)	(11,389)	(8,673)	(5,233)	320	(15,464)

Source: GB Group (historics), Edison Investment Research (forecasts)

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