EDISON

Ebiquity

Improving growth profile

FY17 results; forecasts reduced

Media

Headwinds in the US affected overall performance in FY17 and we pare back FY18 EPS forecasts by 5%. However, remedial action has been taken, activity in H2 has picked up and we continue to forecast an acceleration in like-for-like revenue growth in FY18. Ebiquity's (EBQ's) growth profile should be further improved by the proposed divestment of AdIntel, paving the way for an unwinding of its discount to the peer group. An in-line EV/EBIT rating would point to a value of around 90p.

Year end	Revenue (£m)	EBIT* (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
12/16	83.6	13.0	11.8	11.3	0.65	6.5	0.9
12/17	87.4	12.0	11.0	9.4	0.71	7.8	1.0
12/18e	91.2	11.3	10.2	8.9	0.78	8.2	1.1
12/19e	96.5	12.1	11.2	9.7	0.84	7.6	1.2

Note: *Normalised and diluted , excluding amortisation of acquired intangibles, exceptional items and share-based payments.

Pick-up in growth in H2

As indicated in the pre-close trading update, group like-for-like revenue growth of 0.8% continued to be affected by headwinds in the US with a consequential impact on operating margins. In MVM (+9.3% revenue growth), this was more than compensated for by an excellent performance from its contract compliance business, FirmDecisions, which continues to benefit from increasing demand for media transparency. However, within MPO, despite a strong performance outside the US, client churn in the US-based Multi-Channel Analytics (MCA) practice resulted in a 2.3% decrease in revenues. In MI, revenues decreased by 0.9%.

New leadership teams have now been put in place in both the US Media and the US MCA practice. In the US, H2 revenues in MCA improved over H1 and we forecast an acceleration in like-for-like revenue growth in FY18 and FY19.

AdIntel disposal transforms the profile of the group

On 13 February, EBQ announced the disposal of its Advertising Intelligence (AdIntel) practice, subject to UK Competition and Markets Authority (CMA) approval. The disposal will enable the group to focus resources on the areas of its business with greatest growth potential and higher margins, in line with management's Growth Acceleration Plan. The £26m sale proceeds will reduce the pro forma net debt/EBITDA ratio from 2.1x to 1.0x at December 2017, adding flexibility to invest in enhancing the group's tech-enabled consultancy offering.

Valuation: AdIntel disposal could trigger re-rating

The shares trade on 8.2x P/E and 7.3x EV/EBIT in FY18e. At a c 25% discount to UK agency peers, we believe this rating undervalues the growth potential of the MPO and MVM businesses. This is more evident on a pro-forma basis, where the shares would be on similar multiples despite the much improved growth outlook and balance sheet. Assuming the divestment of AdIntel, on this pro forma basis an FY18e peer average EBIT multiple of 10.0x would suggest a share price of 90p.

21 March 2018

Price	**73p**
Market cap	**£57m**
Net debt (£m) at end FY17	28.9
Shares in issue	78.4m
Free float	99%
Code	EBQ
Primary exchange	AIM
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(11.7)	(26.3)	(36.0)
Rel (local)	(9.8)	(22.1)	(33.8)
52-week high/low		123.50p	74.5p

Business description

Ebiquity is an independent marketing analytics specialist providing a range of business-critical data, analysis and consultancy services to advertisers and media owners on an international basis. It operates across three divisions: MPO (Marketing Performance Optimisation), MVM (Media Value Measurement) and MI (Market Intelligence).

Next events

Interim results	September 2018

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Edison profile page

Ebiquity is a research client of Edison Investment Research Limited

FY17 results

Ebiquity's revenues increased by 4.6% to £87.4m, of which 3.4% of growth is accounted for by currency movements and 0.4% from the September acquisition of Australian digital analytics business, Digital Balance (for up to A$5m subject to performance hurdles to 31 December 2021). The mix of revenue growth is consistent with the first half; a strong performance from the MVM practice outside the US was offset by the US MCA and US media business, with MI stable overall. Like-for-like constant currency growth of 0.8% signifies a better underlying growth rate in the second half.

EBITA margins decreased by 2pp to 13.8%, in part a result of the group's strategy to invest an increasing share of revenues in enabling its consultants with market-leading technology, and in part owing to continued weakness from its US businesses. Consequently, normalised PBT decreased by 7% to £11.0m. Reported PBT of £4.5m includes £6.5m of one-off or non-cash items. These relate to acquisitions and restructuring costs (£3.8m), deferred consideration and share-based payments (£0.7m), and amortisation of acquired intangibles (£1.9m).

Underlying cash conversion from operating profits remains strong at 93% and the board is proposing a dividend of 0.71p (+10% y-o-y). Year-end net debt remained broadly stable at £28.9m, 2.1x EBITDA.

In February, Michael Higgins, chairman for 12 years, announced his retirement with effect from 9 May 2018. He will be replaced by Rob Woodward, who has significant experience in the TMT industry. Rob was CEO of STV Group for 11 years to January 2018, prior to which he was commercial director at Channel 4 Television. Earlier in his career he was MD with UBS Corporate Finance and the lead partner for Deloitte's TMT industry group in Europe. Rob is also non-executive chairman at AIM-listed Blancco Technology Group.

Exhibit 1: Summary FY17 results vs forecasts

£000s	FY16	FY17 (forecast)	FY17 (reported)	Y-o-y growth (%)	Change vs forecasts (%)
MVM	47,161	51,105	51,482	9	1
MI	23,360	24,828	23,146	(1)	(7)
MPO	13,048	13,700	12,746	(2)	(7)
Total revenues	**83,569**	**89,633**	**87,374**	**5**	**(3)**
Operating profit:					
MVM	12,124	13,287	14,037	16	6
MI	3,902	3,724	3,163	(19)	(15)
MPO	3,739	2,603	1,646	(56)	(37)
Central costs	(6,806)	(6,900)	(6,820)	0	(1)
Total normalised operating profit	**12,959**	**12,715**	**12,026**	**(7)**	**(5)**
Operating margin					
MVM	25.7%	26.0%	27.3%		
MI	16.7%	15.0%	13.7%		
MPO	28.7%	19.0%	12.9%		
Total operating margin	**15.5%**	**14.2%**	**13.8%**		
Highlighted items	(5,202)	(5,000)	(6,491)	25	30
Reported operating profit	7,757	7,715	5,535	(29)	(28)
Net finance cost	(1,132)	(1,000)	(1,044)	(8)	4
Share of associates					
PBT (adjusted)	**11,827**	**11,715**	**10,982**	**(7)**	**(6)**
Tax	(2,570)	(3,046)	(2,897)*	13	(5)
Net profit	9,257	8,669	8,085	(13)	(7)
MI	(245)	(525)	(384)	57	(27)
Adj. diluted EPS (p)	11.3	10.1	9.4	(17)	(7)

Source: Ebiquity (actuals), Edison Investment Research (forecasts). Note: *£0.9m of FY17 tax relates to tax on highlighted items and the movement on deferred liabilities.

Divisional performance: US headwinds to growth

Excluding the MI division, which contains the soon to be divested AdIntel business, like-for-like revenue growth was 5.5% in H217, compared to 2.3% across the year.

MPO (15% group revenues, 20% FY18 pro forma revenues): total revenues decreased 2.3% y-o-y (7.7% like-for-like) and the weakness in MCA had a material impact on margins, which decreased to 12.9% (FY16: 28.7%).

- US MCA business: as flagged at the interim results, the US-based MCA business, which has a high concentration of revenues with its largest clients, saw a number of these clients reduce spend and opt to bring services in house during 2017. After three years of 50%+ CAGR in revenues, US revenues decreased by 19.8%. A new leadership team has now been put in place and there are early signs that this US practice is getting back on track; Q4 includes a significant new client (Citibank), and H2 revenues were up slightly on H1, although still down year-on-year.
- Outside the US, revenues increased by 6.4%, with the UK Marketing Effectiveness (ME) business performing particularly well (+17.1%). The roll-out of ME services, previously only available in the UK and Spain, to the US, France, Australia and Singapore, is underway and should start to make a more meaningful contribution to revenues from 2018. The acquisition of Digital Balance further strengthens capabilities in Asia Pacific.

MVM (59% group revenues, 80% FY18 pro forma revenues): revenues increased by 9.3% (5.2% like-for-like) with an operating margin of 27.3% broadly as expected. In a continuation of the trend seen in H1, the contract compliance division, FirmDecisions, performed very well, benefiting from the visible step-up in the group's marketing efforts and the industry's increased engagement on the issue of media transparency. The media benchmarking business outside the US also performed well, but the US business continues to be under pressure from lower overall media spend and the trend towards zero-based budgeting. During Q417 and Q118 a new leadership team was recruited to re-energise the US Media practice.

MI (26% group revenues, 0% FY18 pro forma revenues): revenues decreased by 0.9% (3.1% like-for-like), reflecting stability in the AdIntel business and continued declines in the project-based reputation business, which now accounts for only £1.3m of revenues. This reputation business has subsequently been divested.

Divesting AdIntel releases headwind to growth

In February EBQ announced the proposed sale of its Advertising Intelligence business (AdIntel) to Nielsen for £26m in cash before taxes and transaction costs. The transaction is expected to complete during Q218. However, as CMA approval is required, this could be delayed to Q4 should it require a more detailed Phase 2 investigation.

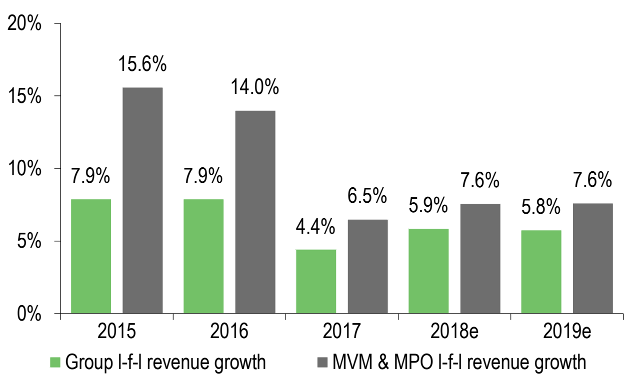
The AdIntel business accounted for the majority of EBQ's MI division, comprising £21m revenues and £4.4m EBITA (before central overhead allocation).

In 2016 management presented its plan to accelerate growth, principally by investing in the faster growing MVM and MPO practices. The proposed divestment of AdIntel is entirely consistent with this strategy, leaving a more focused group with the balance sheet flexibility to accelerate growth opportunistically:

Faster growth profile: over the last few years, the AdIntel division has struggled in the face of pricing pressure and the rapid rise in digital advertising. An upgrade to the Portfolio platform was introduced last year and, to complement its services in traditional media, in H117 it launched its

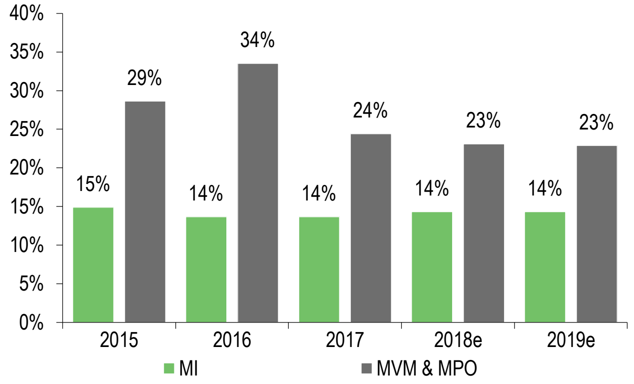
Digital platform. Although this has helped stabilise divisional revenues, the growth outlook remains inferior to MPO and MVM, as do the operating margins (see Exhibits 2 and 3 below).

Exhibit 2: Like-for-like revenue growth



Source: Ebiquity (historic), Edison Investment research (forecasts)

Exhibit 3: Operating margins (pre-central costs)



Source: Ebiquity (historic), Edison Investment research (forecasts)

Streamlined business: the divestment would enable a simpler group structure, focused on the higher-growth consulting services, which operate similar relationship-based business models. As well as simplifying the overall business model, management sees the potential to reduce central overheads by up to £0.7m over time. Reflecting the more aligned structure, EBQ is rebranding its divisions as Ebiquity Media (MVM), Ebiquity Analytics (MPO) and Ebiquity Tech.

Strengthened balance sheet: the pro forma net debt to EBITDA gearing of the group would reduce from 2.0x at December 2017 to 1.0x, providing flexibility to invest to accelerate growth in MVM and MPO; in particular in terms of its data science capabilities.

Forecasts and pro forma forecasts

Much of the 3pp revenue shortfall compared to our forecasts came through the MPO division. While the US MCA issues knocked growth off course during 2017, the client losses appear fairly isolated, action has been taken to bring the US back on track and the performance of the division outside the US remains strong. We rebase our forecasts for FY17 results, but maintain our 10% revenue growth forecast in this division in FY18 and 7% in MVM. Net of small changes to tax (24%) and finance costs, we reduce our FY18 adjusted diluted EPS forecast by 5% to 8.9p. We also introduce forecasts for FY19, which assume a similar growth rate in revenues and margins.

Given the uncertainty on timing of the divestment of the AdIntel business, at this stage we have not carved it out of our forecasts, but present FY18 and FY19 pro forma figures in Exhibit 4 to demonstrate the shape of the business assuming it is divested as of 1 January 2018.

On a pro forma basis, the sale of AdIntel translates to a c 2pp uplift to our revenue growth rate in each year. In our pro forma operating margins, we assume that a full £0.7m of savings is achieved by 2019. Despite this saving, allocating higher central costs to a smaller business means that we believe pro forma operating margins of c 11.6% are achievable in 2019, approximately 1pp below our forecast for the ongoing business.

Exhibit 4: Forecasts and pro forma forecasts					
£000s	FY17 (reported)	FY18e	FY19e	FY18e pro forma	FY19e pro forma
MVM	51,482	55,086	58,942	55,086	58,942
MI	23,146	22,100	22,100		
MPO	12,746	14,021	15,423	14,021	15,423
Total revenues	**87,374**	**91,206**	**96,464**	**69,106**	**74,364**
Operating profit:					
MVM	14,037	13,496	14,293	13,496	14,293
MI	3,163	3,163	3,163		
MPO	1,646	2,454	2,714	2,454	2,714
Central costs	(6,820)	(7,800)	(8,112)	(8,450)	(8,354)
Total normalised operating profit	**12,026**	**11,313**	**12,058**	**7,500**	**8,654**
Operating margin					
MVM	27.3%	24.5%	24.3%	24.5%	24.3%
MI	13.7%	14.3%	14.3%		
MPO	12.9%	17.5%	17.6%	17.5%	17.6%
Total operating margin	**13.8%**	**12.4%**	**12.5%**	**10.9%**	**11.6%**
Highlighted items	(6,491)	(4,550)	(2,900)	(3,830)	(2,230)
Reported operating profit	5,535	6,763	9,158	3,670	6,424
Net finance cost	(1,044)	(1,100)	(808)	(400)	(250)
Share of associates	0.0%				
PBT (adjusted)	**10,982**	**10,213**	**11,250**	**7,100**	**8,404**
Tax	(2,897)	(2,451)	(2,700)	(1,704)	(2,017)
Net profit	8,085	7,762	8,550	5,396	6,387
MI	(384)	(585)	(600)	(585)	(600)
Adj diluted EPS (p)	9.4	8.9	9.7	6.0	7.0

Source: Ebiquity (historic), Edison Investment Research (forecasts)

Valuation

The difficult trading environment in the US, paired with a declining margin, has weighed on the shares' performance over the last year and the shares now trade at a c 25% discount to small-cap agency peers. However, we believe this rating undervalues the MPO and MVM practices, where we forecast a pick-up in like-for-like revenue growth in FY18. Should the divestment of the slower growing, lower-margin AdIntel division proceed as proposed, we expect the overall growth profile of the group to improve, in which case an in-line rating may be more appropriate. A 10x EV/EBIT multiple (broadly in line with the peer average) applied to FY18e pro forma earnings would suggest a share value of c 90p.

Exhibit 5: Peer comparison															
Name	Market cap (m)	Year end	Sales growth (%)		EBITDA margin (%)	EBIT margin (%)	EV/Sales (x)		EV/EBITDA (x)		EV/EBIT (x)		PE (x)	
			FY1	FY2	FY1	FY1	1FY	FY2	FY1	FY2	FY1	FY2	FY1	FY2
Ebiquity	56	12/2017	4.4	5.8	14.9	12.4	1.0	0.9	6.5	6.1	7.7	7.3	8.2	7.5
M&C Saatchi	326	12/2016	12.7	6.1	11.9	10.7	1.3	1.3	11.2	10.1	12.5	11.3	17.0	15.9
Huntsworth	324	12/2017	6.8	5.1	15.6	13.8	1.7	1.6	10.9	10.1	12.4	11.5	15.1	13.6
Next Fifteen	344	01/2017	14.9	12.2	17.8	15.3	1.9	1.7	10.5	8.9	12.2	10.4	16.6	14.5
MMG	36	12/2016	NA	4.9	14.4	11.9	0.7	0.6	4.6	4.2	5.6	5.1	6.1	5.4
Cello	129	12/2016	3.8	2.9	7.9	6.8	0.8	0.8	10.0	9.4	11.7	10.9	15.4	14.7
Reply	1,899	12/2017	10.7	8.7	14.3	12.9	1.9	1.7	13.2	12.1	14.5	13.3	21.5	19.5
Peer average			**(0.6)**	**6.7**	**13.6**	**11.9**	**1.4**	**1.3**	**10.1**	**9.1**	**11.5**	**10.4**	**17.3**	**15.7**

Source: Bloomberg. Note: Prices as at 20 March 2018.

Exhibit 6: Financial summary

£'k	2015	2016	2017	2018e	2019e
31-December	IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT	31-Dec	31-Dec	31-Dec	31-Dec	31-Dec
Revenue	76,584	83,569	87,374	91,206	96,464
EBITDA	14,161	14,574	14,035	13,556	14,458
Normalised operating profit	12,411	12,959	12,026	11,313	12,058
Amortisation of acquired intangibles	(1,327)	(1,865)	(1,952)	(1,950)	(1,900)
Exceptionals	(6,541)	(2,777)	(3,801)	(1,600)	0
Share-based payments	(900)	(560)	(738)	(1,000)	(1,000)
Reported operating profit	3,643	7,757	5,535	6,763	9,158
Net Interest	(1,199)	(1,132)	(1,044)	(1,100)	(808)
Joint ventures & associates (post tax)	18	0	0	0	0
Exceptionals	0	0	0	0	0
Profit Before Tax (norm)	11,230	11,827	10,982	10,213	11,250
Profit Before Tax (reported)	3,135	6,625	4,491	5,663	8,350
Reported tax	(2,497)	(2,230)	(2,043)	(2,451)	(2,700)
Profit After Tax (norm)	8,733	9,257	8,085	7,762	8,550
Profit After Tax (reported)	638	4,395	2,448	3,212	5,650
Minority interests	(229)	(245)	(384)	(585)	(600)
Discontinued operations	0	0	0	0	0
Net income (normalised)	8,504	9,012	7,701	7,177	7,950
Net income (reported)	409	4,150	2,064	2,627	5,050
Basic average number of shares outstanding (m)	76.8	77.2	77.9	78.1	78.9
EPS - basic normalised (p)	11.1	11.7	9.7	9.2	10.1
EPS - diluted normalised (p)	10.8	11.3	9.4	8.9	9.7
EPS - basic reported (p)	0.5	5.4	2.7	3.4	6.4
Dividend per share (p)	0.40	0.65	0.71	0.78	0.84
EBITDA Margin (%)	18.5	17.4	16.1	14.9	15.0
Normalised Operating Margin	16.2	15.5	13.8	12.4	12.5
BALANCE SHEET					
Fixed Assets	73,594	75,855	75,771	74,978	73,878
Intangible Assets	68,354	72,079	72,440	71,947	71,197
Tangible Assets	2,928	2,438	1,829	1,529	1,179
Investments & other	2,312	1,338	1,502	1,502	1,502
Current Assets	33,073	35,078	37,241	40,638	47,972
Stocks	0	0	0	0	0
Debtors	16,283	19,291	20,978	21,607	22,256
Cash & cash equivalents	8,755	6,662	4,732	7,500	14,186
Other	8,035	9,125	11,531	11,531	11,531
Current Liabilities	(27,473)	(25,912)	(24,549)	(24,771)	(25,000)
Creditors	(20,672)	(17,809)	(20,066)	(20,288)	(20,517)
Tax and social security	(2,000)	(1,850)	(1,598)	(1,598)	(1,598)
Short term borrowings	(4,801)	(4,476)	(1,572)	(1,572)	(1,572)
Other	0	(1,777)	(1,313)	(1,313)	(1,313)
Long Term Liabilities	(36,785)	(32,728)	(35,481)	(34,231)	(34,231)
Long term borrowings	(32,615)	(30,210)	(32,000)	(30,750)	(30,750)
Other long term liabilities	(4,170)	(2,518)	(3,481)	(3,481)	(3,481)
Net Assets	42,409	52,293	52,982	56,614	62,620
Minority interests	808	761	1,040	1,040	1,040
Shareholders' equity	43,217	53,054	54,022	57,654	63,660
CASH FLOW					
Op Cash Flow before WC and tax	14,161	14,574	14,035	13,556	14,458
Working capital	(871)	(2,835)	(2,002)	(407)	(420)
Exceptional & other	(1,775)	(957)	(4,085)	(1,600)	0
Tax	(1,062)	(166)	(2,207)	(2,451)	(2,700)
Net operating cash flow	10,453	10,616	5,741	9,097	11,339
Capex	(1,976)	(2,351)	(2,231)	(2,500)	(2,600)
Acquisitions/disposals	(4,530)	(4,431)	(3,082)	(900)	(600)
Net interest	(999)	(1,074)	(921)	(1,100)	(808)
Equity financing	224	26	160	0	0
Dividends	(291)	(838)	(495)	(580)	(644)
Other	(178)	(1,017)	(46)	0	0
Net Cash Flow	2,703	931	(874)	4,018	6,686
Opening net debt/(cash)	31,248	28,661	28,024	28,840	24,822
FX	(116)	(633)	58	0	0
Other non-cash movements	0	339	0	0	0
Closing net debt/(cash)	28,661	28,024	28,840	24,822	18,136.1

Source: Ebiquity (historic), Edison Investment Research (forecasts). Note: Reported net debt differs slightly from cash net debt due to the inclusion of loan arrangement fees which have been paid but which are amortised over the life of the facility.

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