EDISON

The Pebble Group

Initiation of coverage

Differentiated positions in promotional products

Media

The Pebble Group operates within the large, global promotional products market, estimated by management at $50bn, under a highly experienced team. The group combines two operations: a fast-growing, high-margin SaaS business supplying independent distributors of promotional goods; and a dependable and expanding international business supporting brand engagement programmes for major global brands. The group has a strong balance sheet, with end FY21 net cash (excluding leases) of £12.1m, set to be exceeded in the current year. The share price does not, in our opinion, reflect the group's positioning or opportunities.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	EV/EBITDA (x)
12/20	82.4	5.5	2.7	0.0	29.6	13.7
12/21	115.1	10.0	4.7	0.0	17.0	8.7
12/22e	133.0	11.9	5.6	0.0	14.4	7.6
12/23e	142.5	13.5	6.1	0.0	13.3	7.0
12/24e	147.0	14.1	6.3	0.0	12.7	6.8

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

Scale opportunities at Facilisgroup

Facilisgroup (12% H122 revenues, 44% adjusted EBITDA) is a SaaS business with a target market of North American promotional product distributors, processing $1.3bn of Gross Merchandise Value (GMV) and generating very strong EBITDA margins of 55–60%. It helps its Partners (customers) grow through efficient order workflow and driving purchasing through its preferred supplier base. Growth in H122 was robust, with GMV up 38%, with 54% more spend put with preferred suppliers. Commercio, Facilisgroup's new all-in-one e-commerce solution, greatly expands its addressable market, enabling distributors to manage their own online stores. Launched in June 2022, it is now being rolled out, with 45 customers contracted to date. The ambition is to build towards $50m of recurring revenues, from our FY22e estimate of $21m.

Brand Addition anticipates record year

Brand Addition (88% of H122 revenues, 56% of adjusted EBITDA) is a solid business with an enviable client roster, widely spread across sector verticals and geographies. Its growth comes from winning additional global brand business and expanding the revenues with its existing client base. H122 revenues were up 29% on H121 and gross margins improved to 29.9% (H121: 28.2%). The adjusted EBITDA margin was 8.3%, up from 6.1% in H121. Momentum at Brand Addition looks positive and if there is outperformance of FY22 consensus (guided up at the half-year) it is likely to come from this part of the group.

Valuation: Facilisgroup already the larger element

We have looked at an earnings-based sum-of-the-parts and used a DCF methodology. The former is based on the peer group EV/EBITDA multiples of US SaaS companies capitalised below $1.5bn for Facilisgroup and of marketing services companies for Brand Addition. These methods both give an implied share price of 133p, with Facilisgroup roughly half the value inherent in the group.

1 November 2022

Price	**80p**
Market cap	**£134m**
	$1.182£
Net cash at 5 September 2022 (£m), excluding leases	2.5
Shares in issue	167.5m
Free float	93.2%
Code	PEBB
Primary exchange	AIM
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	(14.5)	(18.5)	(47.9)
Rel (local)	(15.3)	(14.1)	(44.1)
52-week high/low		153p	78p

Business description

The Pebble Group provides digital commerce, products and related services to the global promotional products industry through two focused, complementary and differentiated businesses: Brand Addition and Facilisgroup.

Next events

Year-end trading update	December 2022

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Edison profile page

The Pebble Group is a research client of Edison Investment Research Limited

Investment summary

Company description: Promoting promotional products

The Pebble Group comprises two businesses both operating within the global promotional products space. These are Facilisgroup and Brand Addition. Facilisgroup is a software-as-a-service (SaaS) business supporting North American distributors in the promotional products market with software that helps them manage their workflow and increase efficiency by channelling orders through a network of preferred suppliers. This is for monthly fees based on prior year revenue throughput. Facilisgroup has recently launched a new software platform, Commercio, which provides distributors with an industry-bespoke e-commerce solution. This is being offered to both existing Facilisgroup customers and out to the wider market. Brand Addition works with global brands fulfilling their complex needs around design, sourcing and delivery of their corporate programmes and consumer product promotions. The business has maintained long-term relationships with its clients through both engaging their target audience with attractive product and ensuring that their brand equity is protected through sourcing that aligns with their ESG objectives. Revenues are generated through taking a margin on the revenue throughput. Management has extensive experience in the sector and ESG considerations are integrated through the business to protect both Pebble's brands and those of its customers.

Valuation: Value opportunity versus peers and DCF

Pebble is two complementary businesses in one, so it is appropriate to value them separately and then combine, making an adjustment for central costs. We have looked at Facilisgroup, which operates in North America, with the US SaaS sector capitalised below $1.5bn and at Brand Addition in comparison with other small- and mid-sized marketing services companies. Using EV/EBITDA multiples for the current year implies a value of 142.2p, and for FY23 of 123.5p, with the two figures averaging at 132.9p. The DCF also points to a similar number, 133.1p, using a WACC of 10% and a terminal growth rate of 2%, but based on only a moderate improvement in the combined EBITDA margin across the modelling horizon. If Commercio takes off, then the Facilisgroup contribution to the whole will be higher, driving up group margins. For the current year, Facilisgroup has built to just below half the combined value of the group. By FY23e, this has built to 55% based on our modelling.

Financials: Growing and cash generative

Facilisgroup is set to be the group's main revenue driver over the short to medium term. Brand Addition generates steady mid- to high-single-digit growth, while Facilisgroup has the potential to deliver a much greater pace of expansion, having increased its H122 revenues by 32% over the prior year. Nearly all of this is in recurring revenue, giving very good visibility of earnings. The group's working capital is almost entirely Brand Addition's. It has a well-documented in-year cycle, peaking in the summer months and with a low point in December. Management's target is to build Facilisgroup annual recurring revenue (ARR) to $50m from the expected $21m in FY22e. While the business is in an investment phase, margins were nevertheless strong at 47.3% in H122 (FY21: 59.6%). Increased amortisation in H122 from the investment into scaling up ARR resulted in operating margin at 23.0%, down from 40.7% in FY21.This investment could have a significant payback as, if ARR approaches management's $50m target, operating margins should be well above 40%. Therefore, the priority for capital allocation is currently firmly on building Facilisgroup, increasing its offering and expanding its target market. M&A remains a possibility but is more likely to be of the bolt-on, in-fill variety. The payment of dividends is considered by the board on a six-monthly basis, with the appetite to move to the 30% of post-tax earnings indicated in the prospectus

liable to increase as the group's cash resources grow. Excluding leases, we anticipate end FY22e net cash of £14.4m (FY21: £12.1m).

Sensitivities: Currency, inflation and supply chain influencing factors

The reported financial results will be impacted by the currency outturn for the year, the main component being the translational impact of Facilisgroup (44% H122 adjusted EBITDA), which trades mainly in US dollars. With sterling weakness, this is likely to be beneficial to both the income statement and the balance sheet. The performance of the US economy and the small business sector also looks to be more resilient than the UK and some European markets, which is beneficial to the performance of Facilisgroup, being North American focused, and with 22% of Brand Addition revenues generated in the US in H122. The worst of the supply chain issues are now easing, with Brand Addition managing the challenges of FY21 and FY22 well. It also has the flexibility to mitigate the impact of inflation through substitution and product re-engineering, as can be seen by the stability of gross margins in H122 of 29.9% (H121: 28.2%).

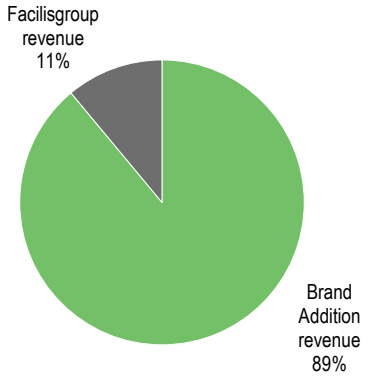
Company description: Promotional product sector expertise

The Pebble Group provides digital commerce, products and related services to the global promotional products sector. It consists of two separate but complementary enterprises: Facilisgroup, which is a SaaS business, supporting North American distributors of promotional goods with digital commerce technology: and Brand Addition, which supplies global brands, under contract, with promotional products and related services.

The original business was founded in 1986, with Brand Addition established by current management from three businesses within 4imprint in 2010. This was then bought out by management, supported by private equity (PE), a couple of years later. In 2014, Brand Addition extended its operations into China, followed in 2016 by the expansion to North America with the acquisition of Gateway CDI, which then became Brand Addition North America. There was a secondary PE-backed management buyout the following year, and the purchase of Facilisgroup in late 2018. It was at this point that The Pebble Group was set up, giving a group setting for these differentiated businesses operating within the large, promotional products sector.

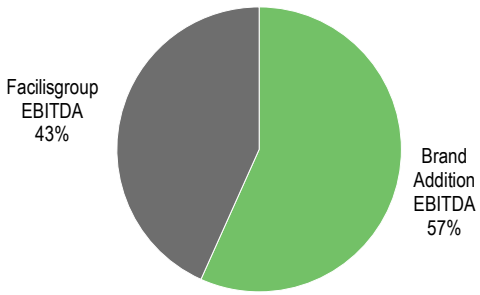
The Pebble Group was admitted to the AIM market in December 2019, via a placing of 129.0m shares at an issue price of 105p, of which 75.4m were new shares, raising £79.2m of capital for the group. The group's management team held c 10% of the group's shares at IPO and all Board Directors have only added to their holdings since listing.

Exhibit 1: FY21 revenue by business



Source: The Pebble Group

Exhibit 2: FY21 EBITDA by business



Source: The Pebble Group

We describe the two constituent businesses below.

Facilisgroup: Software solutions for the promotional products market

Facilisgroup provides SaaS solutions for companies, currently SME distributors in North America, operating in the promotional products space, providing technology solutions that are custom-built for their needs, rather than adapted from existing off-the-shelf systems.

It charges subscriptions for the use of its technology platform and fees for its supply chain management activities. With high retention rates, the company has significant levels of ARR, typically over 95% of the total (94% in H122).

Facilisgroup's customers, which it refers to as Partners, are typically SME distributors with revenues in the range of $3m to $30m. With over 200 Partners, Facilisgroup processes GMV of around US$1.3bn (estimated at just over 5% of the US promotional products market). Its core offering, Syncore, which has been the basis of growth of the business to date, comprises two income streams:

- **Subscriptions for order workflow** (65% of FY21 ARR). Paid by the Partners, this SaaS offering handles the process from enquiry through to invoice, encompassing CRM, product search and order processing.
  Fees are fixed at the beginning of each year, based on the prior year's GMV and are paid monthly.
- **Marketing fund** (35% of FY21 ARR). It is to the advantage of the Partners that Syncore consolidates their combined buying power to achieve pricing support with suppliers. The business has built a cohort of around 100 preferred suppliers through which to channel product purchases. These preferred suppliers then pay fees based on the value of Partner purchases in the year, paid half-yearly.

Exhibit 3: Business model

Source: The Pebble Group H122 management presentation

The projected growth for each of these areas is discussed in the Financials section, below.

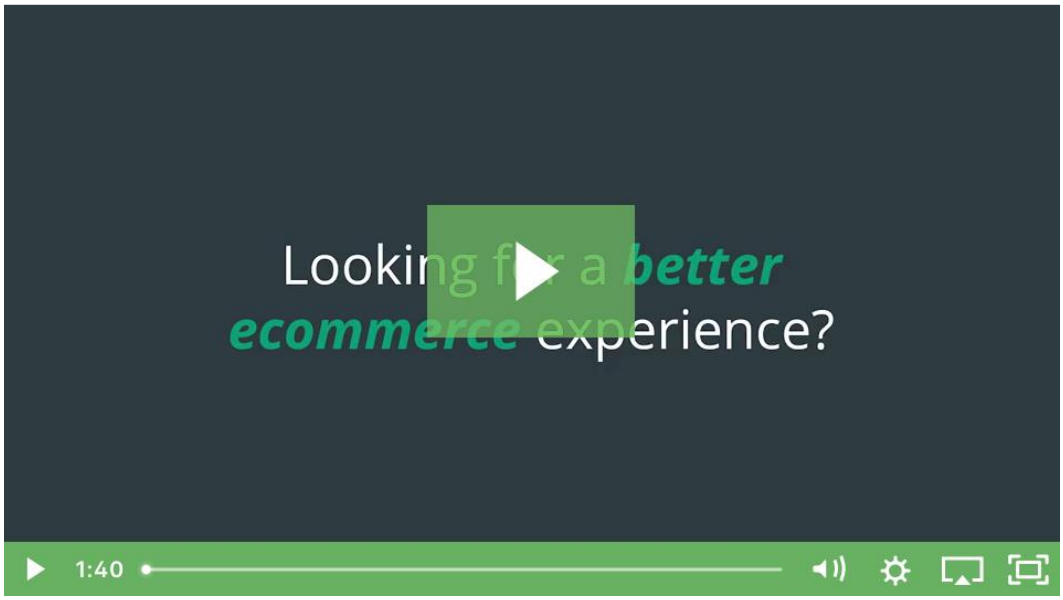
Commercio grows the addressable market

Commercio was launched in June 2022 so is in its very early stages of commercialisation. Initially developed in response to the needs of a Partner, utilising Syncore, the concept is to allow smaller

distributors to have their own e-commerce offering using storefronts built on the Commercio platform. E-commerce is an increasingly important route to market and management estimates that around 25% of the market value is already transacted on this channel. There are many pitfalls for Partners and SME distributors trying to develop an efficient online store and other products and platforms available in the market, such as Shopify, may not fully address the specific requirements of promotional products distributors, which are dealing with the combination of personalisation and complex order submissions. Facilisgroup has developed Commercio with the aim of fulfilling this need.

Initial pricing is a monthly fee of $200 plus a fee per store of $100 (a distributor generally has multiple stores addressing different customers, with existing Partners estimated to each have around 10). For the distributor, the integration with the existing Syncore offering should enable a friction-free process from order to fulfilment, with all the necessary paperwork documented along the way.

Exhibit 4: Commercio sales reel



Source: www.commercio.com

Management estimates that there around 22k suitable potential customers beyond those currently served by Syncore. These potential customers will typically be members of trade associations so can be reached through tradeshows, websites and newsletters, etc, rather than necessitating 'cold' outreach.

Strategy: Build scale, reach and recurring revenues

The group is continuing to invest in, and show progress against, the medium-term growth plan for Facilisgroup, targeting $50m of ARR by the end of FY24 (the route to this is shown below in the Financials section). Its aim is to be the industry leader in digital commerce for the promotional products industry, providing a range of integrated solutions to support growing, entrepreneurial businesses in the sector. Attracting new Partners is key to building the revenue from the core Syncore offering.

The addition of the Commercio e-commerce platform to the portfolio significantly enhances the addressable market, extending beyond the existing customer base and into the wider promotional products market.

For smaller distributors in the market (revenues of under $2m), Facilisgroup is developing an order workflow product more appropriate to their needs than Syncore, which is scheduled to launch in FY23.

Brand Addition: Trusted by for global brands

Brand Addition has two activities, Corporate Programmes and Consumer Promotions, described below. Revenues are well diversified by sector and by geography. In FY21, it generated 26% of revenues in the UK, 38% in Europe, 20% in the United States and 16% in the rest of the World.

It generates its revenues from taking a margin on goods supplied to its clients.

Clients are exclusively large brands, including many of the world's best-known brands, which work with Brand Addition over the long-term, with three- to five-year contract periods to provide promotional products in the form of merchandise supporting brand awareness (Corporate Programmes), and 'gift with purchase' (Consumer Promotions), intended to promote brands and drive incremental revenues. Brand Addition;

- designs products and product ranges, to drive emotional engagement with the client's target market,
- ensures high quality and ethical/compliant purchasing all through the supply chain
- delivers internationally to its clients with consistent high service levels, leading to long-term commercial relationships,
- provides integrated technology solutions that support client retention.

Exhibit 5: Typical Corporate Programme product

Source: Brand Addition

Exhibit 6: Typical branded consumer promotion

Source: Brand Addition

Corporate Programmes (55% FY21 Brand Addition revenues)

In the Corporate Programme division, Brand Addition is almost always the single preferred supplier to its clients and will both hold the stock and supply directly from a supplier. Holding the inventory allows its clients to received approved product quickly, while larger bespoke product needs can be fulfilled with the support of an experienced account management team. Inventory is underwritten by the client, meaning that should brand imagery or intended programmes change, Brand Addition cannot be left with redundant stock and associated write-downs.

Relevant individuals within the client firms access stock through web stores, designed and operated by Brand Addition and often integrated into the client's internal procurement websites or portals. Brand Addition therefore also has considerable expertise in building and operating multi-lingual and multi-currency e-commerce operations, as well as in the fulfilment required.

This is a relatively sophisticated operation, best suited to large, global brands with extensive marketing programmes. The group works with over 120 clients, some of which are mentioned below. Many others will be covered by non-disclosure agreements.

Consumer Promotions (45% FY21 Brand Addition revenues)

In the Consumer Promotion division, Brand Addition is the single or a preferred supplier to its global client base, providing bespoke branded product, which then forms part of a gift with purchase alongside the client's retail products, to support promotional activities.

As with the Corporate Programmes, Brand Addition designs and samples products for clients, which, on approval, it then sources. This is done ensuring all relevant compliance with the highest standards of materials and production, with quality control as a matter of course. Products are delivered into the client's own distribution networks to be packaged alongside the client's own retail goods, driving their own sales. Contracts are negotiated on a framework basis, with Brand Addition fulfilling multiple campaigns each year.

Examples of verticals and clients are given below. The largest clients are transacting millions of pounds of revenue, with the top 20 clients typically generating 60–70% of business revenue. In FY21, the top 10 clients represented 72% of revenue, up from 59% in FY20, but this is more a reflection of a slower pace of recovery among the smaller customers than an inherent increase in concentration.

Exhibit 7: Sample verticals and clients

Automotive	Charities	Engineering	Financial services	FMCG	Health & beauty	Sports	Technology & communications
Nissan	BBC Children in Need	ABB	RBS	Unilever	Clarins	Stars Group	Google
Michelin	Macmillan	SKF	Visa	Nestlé Group	GHD	Premier League	Indeed
Cadillac		Exxon Mobile	HSBC	Heineken		Manchester Utd FC	BT
Enterprise		Caterpillar	JP Morgan			Chelsea FC	Schneider Electric
Arnold Clark		Stanley Black + Decker	Zurich				Cisco
		JCB					

Source: Brand Addition website

Brand Addition's management outlines low levels of client churn, with the management of what is effectively in-house e-commerce and international fulfilment (often supporting its clients through relatively small call-offs of orders), which is difficult to replicate for competitors without the scale and reach of Brand Addition. The business's design expertise, which often initiates concepts to fit clients' needs, rather than simply meeting the brief, is a further barrier to competition, but probably the greatest moat relates to the longstanding relationships. Brand Addition protects its clients' brand equity through its focus on leading ESG practises and ethical sourcing.

Interview with CEO, Chris Lee

We recently talked to Chris Lee, CEO, about how The Pebble Group fits within the promotional products landscape and the opportunities that the group has to grow revenues and margins.

Exhibit 8: ETV with Chris Lee, October 2022

Source: Edison Group

Strategy: Win, grow, retain, repeat

Winning new, substantial clients is the most efficient expansionary strategy for Brand Addition and the group disclosed its success in attracting new global contracts in FY20 and FY21. Growing these contracts geographically and/or widening across their brand portfolios are further routes to growth within existing clients.

Retaining contracts is key to supporting overall growth. Three- to five-year framework contracts are in place but Brand Addition's intention is to manage the contracts in a manner that reinforces long-term relationships. The business has an excellent track record of client retention.

Repeating this cycle of focussing exclusively on large international brands that value the complex services delivered by Brand Addition has benefited the business. Management estimates that this sub-sector of the promotional products market is valued at around $2bn, meaning there is a large runway of opportunity ahead.

ESG integrated across the business

Management sets the bar high when it comes to ESG, integrating ESG into every level of the group's internal and external relationships. Four cornerstones are specified:

- The impact of the group's business on the environment and its communities. This is evidenced through responsible sourcing and prioritising sustainable products and a focus on reducing the group's carbon impact, using carbon-neutral delivery options wherever practicable. Management targets a 50% reduction in Scope 1 and 2 emissions by 2030.
- Diversity, health, wellbeing and engagement. The engagement brief is partly fulfilled with the creation of products to help brands engage with their own audiences. On diversity, management acknowledges that a diverse workforce and leadership team is important for the long-term success of the group.
- Board independence, ethics and leadership. Open and transparent engagement and alignment with best practice are pre-requisites to achieve a positive outcome.

- Responsible business practices. This is at the core of the operations. Pebble is not just responsible for the curation of its own brands; it is responsible for the brand equity and reputations of its clients.

In October 2022 the group published its 2nd annual ESG report, reiterating the principles of the journey to which the group is committed, and detailing examples of the progress that has been made including the completion of its Scope 3 evaluation and the implementation of the reporting framework for energy and carbon usage across the group.

The group was shortlisted twice in the AIM Awards 2022 for Best Investor Communications and AIM Corporate Governance, winning in the latter category.

Management with extensive industry experience

CEO Chris Lee has been with the group for 22 years, driving the two buyouts in 2012 and 2017 and leading the listing of the group on AIM in December 2019. He also engineered the purchases of Gateway CDI (which formed Brand Addition North America) in 2016 and Facilisgroup in 2018. The group CFO is Claire Thomson, who joined 14 years ago and took over as CFO ahead of the management buyout (MBO) in 2012. Prior to joining Brand Addition, as it was before the formation of The Pebble Group, Claire was at PricewaterhouseCoopers.

The operational teams are headed by Ashley McCune at Facilisgroup and Karl Whiteside at Brand Addition. Ashley has been with Facilisgroup more or less since its inception and was promoted to president following the departure of the legacy owners post its acquisition by The Pebble Group. Karl joined in 2017 from holding senior roles at Staples Promotional Products, a major player in the North American markets particularly in corporate programmes.

The group's management team held circa 10% of the shares at IPO and all Board Directors have only added to their holdings since listing. Management is additionally incentivised through an annual bonus scheme based on an adjusted EBITDA target, capped at 100% of salary. 42.5% was paid out in respect of the FY21 performance. There is also a long-term incentive plan in place with targets based on earnings per share and total shareholder return.

A large and diverse addressable market

There has been plenty of research over the years about the efficacy of promotional products as a marketing tool, particularly when combined with other tools for brand awareness, such as advertising. North American industry body the Advertising Specialty Institute (ASI) cites 86% recall rates for advertisers who gave out promotional gifts, while Promotional Products Association International (PPAI) research shows that 94% of respondents liked getting promotional products, with three out of four kept simply because they are useful.

The promotional products industry is a highly competitive landscape, but the distributor participants are predominantly small and locally active. The most thorough statistics are available for the North American market, estimated by industry body PPAI to be valued at around $24bn in FY21, with management estimating that the aggregate size of the European market is a little smaller and the global market is worth in the order of $50bn.

The largest participant in the North American market, in terms of FY21 revenues, was Halo Branded Solutions, with sales of $822m. It has a markedly different business model, being based on regional field salesforces travelling around the client pool. It has been active in the M&A field, adding another top 40 distributor (terms undisclosed). 4imprint (a client of Edison Investment Research) is the second largest distributor, with a strong recovery post a steep decline in revenues

during the pandemic. It does not operate within the corporate programme or large consumer product markets. Third placed is Staples Promotional Products, based on the PPAI estimates (Staples is privately owned). The difficulty in measuring value here is that promotional goods are sold alongside other office products. Staples is particularly heavily weighted to corporate programmes and mostly operates in the US.

Sensitivities

There are a number of sensitivities that could affect the financial performance of the group. These include:

- The general macroeconomic environment. The promotional products market is broadly resilient because of its utility as an advertising medium and because the eventual recipients like the products and receiving them as gifts. It should be noted that the SaaS model of Facilisgroup (44% of H122 adjusted EBITDA) experienced uninterrupted growth and zero Partner attrition during FY20 as Partners continued to utilise Facilisgroup technology to manage their businesses. Additionally in Brand Addition, there is good diversity of both sector vertical and geography, with 64% of revenues derived from Europe and 20% from North America in FY21.
- Pandemic specific issues. While most lockdowns have now been lifted, there are still some residual issues in China, which may continue to have an impact on supply chain efficiency.
- Supply chain. Getting hold of stock and getting it shipped to the right destination, on time, has been more difficult over the last two to three years. These are industry-wide issues, though, and the secret to managing client and supplier relationships is always communication and setting expectations. Close and long-standing relationships with clients are helpful here.
- Inflation. Again, an industry-wide issue, but, again, with good client relationships there are opportunities to mitigate the impacts of inflation through substitution and redesign to engineer out costs. People costs can be harder to offset through pricing.
- Reputational risks. Particularly with Brand Addition, there has to be a high degree of trust that product bearing a client's brand will uphold the values of that brand and its owner. The maintenance of high standards of oversight over the full supply chain is essential to ensure ethical purchasing and sustainability criteria, as well as strict quality control to ensure that the product looks and feels as specified and is incremental rather than detrimental to the value of the brand.
- Client concentration. In FY21, 71.6% of Brand Addition revenue was generated from the top 10 clients. However, the risk is mitigated by the blue-chip nature of the client base, as can be seen from the sample given in Exhibit 5, above.
- Execution risk on Commercio. The successful roll-out of Commercio is key to driving the outlined Facilisgroup revenue scale and for building the basis from which EBITDA margin expansion can happen. If customers are not brought onboard at the anticipated pace or the technical functionality of the offering does not meet customer expectations, then management's internal aspirations will not be met.
- Currency. With a global customer base and a global supply chain, the group has exposure to multiple currencies. Facilisgroup generates revenues predominantly in US dollars (with some Canadian dollar exposure also). Sterling weakness boosts operating profits and the value of the net assets. The accounts quantify this, with a 10% downward movement in sterling increasing operating profit by £0.5m and net assets by £2.5m.
- IT. IT risks will include systemic risks and those surrounding the relationship of trust and integrity over the curation of sensitive client data.

Valuation

We have looked at The Pebble Group's valuation on two bases. Firstly, predicated on earnings, while acknowledging that Facilisgroup and Brand Addition have different attributes and dynamics, so therefore using a sum-of-the-parts approach. Secondly, we have looked at a discounted cash flow (DCF), albeit that this has substantial sensitivities to the input assumptions, particularly around the achievable margins on a group basis, given that they are a blend. These two approaches give us a valuation range of 130–133p per share. Using an earnings-based approach, the value attributed to Facilisgroup has climbed through 50% of the group mark.

Sum of the parts on earnings basis

Firstly, we look at Facilisgroup next to a set of US-based SaaS stocks, capitalised below $1.5bn.

Exhibit 9: Facilis Group peer comparison

	EV/sales 1	EV/EBITDA 1	EV/EBITDA 2
SolarWinds Corp	3.5	8.9	8.1
Meridianlink Inc	5.5	14.0	12.8
Model N Inc	5.9	39.1	32.8
Olo Inc	4.6		
Everbridge Inc	3.5	36.5	21.4
Momentive Global Inc	2.3	20.0	13.3
Docebo Inc	5.0		
HealthStream Inc	2.3	12.0	11.1
ChannelAdvisor Corp	3.3	15.5	13.8
LivePerson Inc	1.9		14.6
Eventbrite Inc	1.1	17.1	8.6
Yext Inc	1.0	57.5	13.2
Ebix Inc	1.2	7.4	6.3
Bandwidth Inc	1.1	20.4	14.7
Brightcove Inc	1.2	12.3	10.2
Veritone Inc	1.4		21.2
Upland Software Inc	1.9	6.2	5.8
Benefitfocus Inc	1.4	8.2	8.3
SolarWinds Corp	3.5	8.9	8.1
Median US SaaS	**2.1**	**14.8**	**13.0**
EV of Facilisgroup on US SaaS multiples, £m	31.8	128.8	127.9

Source: Refinitiv, Edison Investment Research Note: Prices as at 28 October 2022

We then appraise Brand Addition in comparison to a set of relevant UK-listed but international marketing services businesses.

Exhibit 10: Brand Addition peer comparison

	EV/sales 1	EV/EBITDA 1	EV/EBITDA 2
M&C Saatchi	0.7	4.1	3.6
4imprint	1.1	12.0	10.4
Kin and Carta	1.6	12.5	10.0
Next Fifteen	1.7	7.0	6.0
Altitude	1.1	13.0	9.7
The MISSION Group	0.7	4.4	4.0
Dianomi	0.8	13.0	8.8
Median marketing services	**1.1**	**12.0**	**8.8**
EV of Brand Addition on marketing services multiples, £m	123.7	136.7	106.3

Source: Refinitiv, Edison Investment Research Note: Prices as at 28 October 2022

We have then combined the two elements and made an adjustment for central costs at a 12.0x multiple for FY1 and an 11.0x multiple for FY2 and used the latest disclosed balance sheet position of net cash of £2.5m to move from enterprise value to market capitalisation.

Exhibit 11: Sum of the parts

Based on	EV/Sales 1	EV/EBITDA 1	EV/EBITDA 2
EV Facilisgroup (£m)	31.8	128.8	127.9
EV Brand Addition (£m)	123.7	136.7	106.3
Total (£m)	155.5	265.5	234.1
Central cost multiple (x)		12.0	11.0
less central costs (£m)		(29.9)	(29.8)
The Pebble Group implied EV (£m)	155.5	235.6	204.3
The Pebble Group implied Mkt Cap (£m)	**158.0**	**238.1**	**206.8**
Implied share price (p)	**94.4**	**142.2**	**123.5**

Source: Edison Investment Research

As the business is both profitable and growing, we prefer to value The Pebble Group on the basis of the comparative EV/EBITDA multiples. This derives a value based on the current financial year of 142.2p and a value of 123.5p based on FY23. Averaging these two gives a value per share of 132.9p.

It is interesting to note that for the current year, the value attributed to Facilisgroup is already close to that of Brand Addition, outstripping it in FY23 to represent building to 55% of the combined value on the basis of our current forecasts.

DCF context

We have also valued The Pebble Group (on a group basis) using a DCF approach.

Exhibit 12: DCF at varying WACC and terminal growth rate assumptions

p/share		Terminal growth rate				
		0.00%	1.00%	2.00%	3.00%	4.00%
WACC	12.50%	85.26	89.38	94.30	100.24	107.59
	12.00%	90.08	94.76	100.38	107.25	115.83
	11.50%	95.38	100.71	107.17	115.14	125.24
	11.00%	101.22	107.32	114.77	124.09	136.08
	10.50%	107.68	114.70	123.36	134.33	148.67
	10.00%	114.87	122.97	**133.10**	146.12	163.48
	9.50%	122.89	132.31	144.23	159.83	181.09
	9.00%	131.90	142.91	157.07	175.95	202.37
	8.50%	142.07	155.04	172.00	195.14	228.55
	8.00%	153.62	169.03	189.57	218.33	261.47

Source: Edison Investment Research

In compiling this DCF, we have made conservative assumptions on the development of EBITDA margin, which is based on the mix within the business of Facilisgroup and Brand Addition. Beyond the end of our modelling horizon (to FY24), we have conservatively assumed a gradual step up of 100bp per year. If the group was to achieve growth anywhere close to its internal ambitions, the assumptions would be significantly beaten.

On a WACC of 10.0% and a 2% terminal growth rate, this modelling suggests a valuation per share of 133.1p, in line with the value implied by earnings, above, and 67% above the current market valuation.

Financials

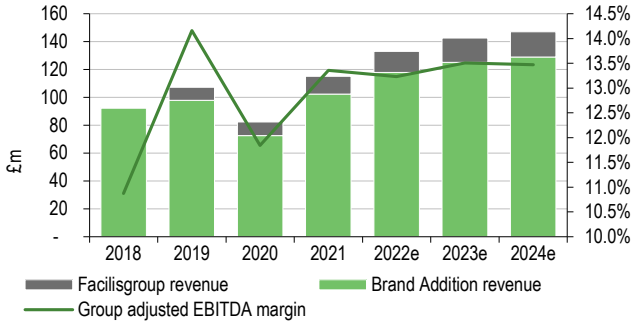
Earnings blend two different business dynamics

At its simplest, The Pebble Group combines:

- Facilisgroup: an innovative software business with consistent revenue growth and a high proportion of recurring revenue (c 95% of FY21 revenue), a growing customer base and high EBITDA margins (59.6% in FY21). Scaling this business would add significant value to the group; and

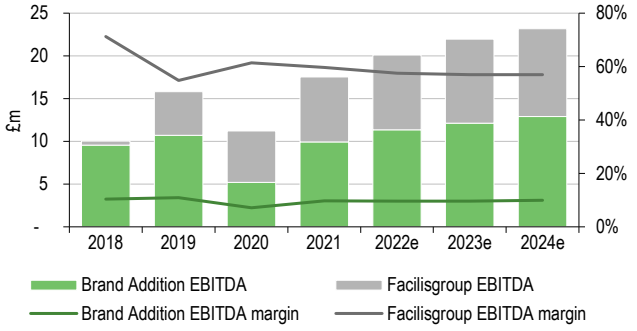
- Brand Addition: a relatively high-volume, lower EBITDA margin business (up to 11% historically), reliable (pandemic-excepted) business, with steady-growing revenue and a high-quality client roster with a low rate of churn.

Exhibit 13: Group revenue and EBITDA margin record and Edison forecasts



Source: The Pebble Group accounts, Edison Investment Research

Exhibit 14: Group EBITDA record and Edison forecasts

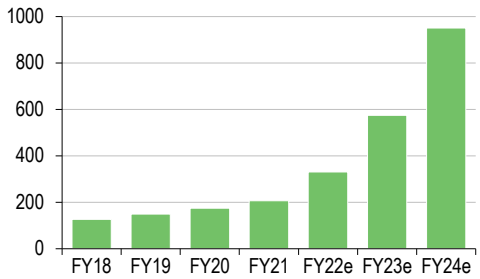


Source: The Pebble Group accounts, Edison Investment Research

Facilisgroup contributed 11% of FY21 revenue and 43% of group adjusted EBITDA

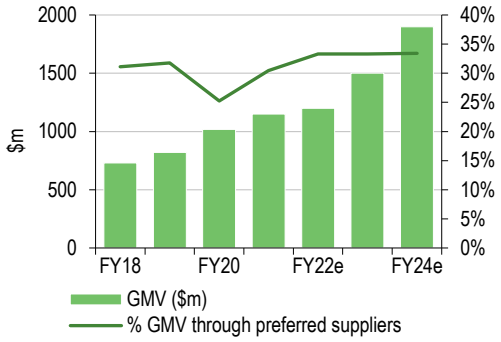
Facilisgroup revenues are driven forward by the growing numbers of Partners and the value of their spend with the group's preferred supplier base, as shown below. It should be noted that the figures for FY20 are distorted by the pivot within the industry to supplying PPE during the heights of the pandemic. For Facilisgroup, this was $249m of GMV, which was 24% of the total for the year. Excluding this, GMV would have been down 6% year-on-year, which represents a resilient result. The bounce back in FY21 would be 50% with this stripped out, rather than the 13% improvement posted.

Exhibit 15: Facilisgroup targeted customer numbers



Source: Facilisgroup

Exhibit 16: Facilisgroup targeted GMV



Source: Facilisgroup. Note: FY20 GMV includes $249m of PPE.

H122 results show a further uplift in Partner numbers, with 210 contracted and an additional eight in progress as at end June, from 200 with six in progress at the 2021 year-end. GMV was up 38% year-on-year at $630m, meaning on a rolling twelve-month basis, $1.3bn of Partner sales have been processed through Facilisgroup technology.

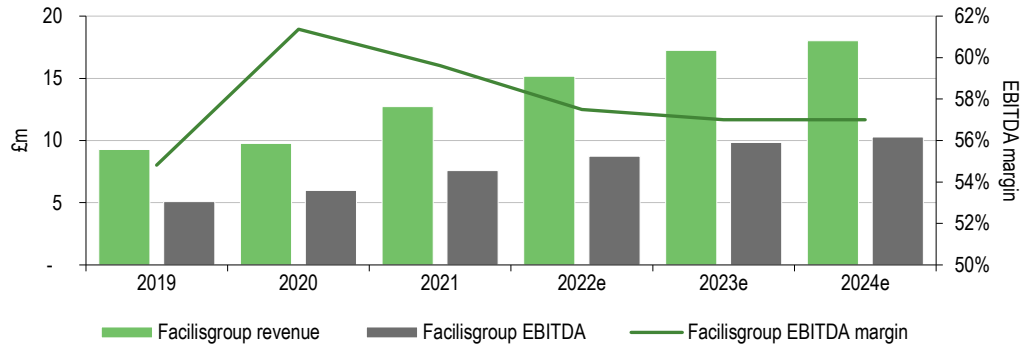
The exhibits above show the record to date and management's internal aspirations, which appear to us to be demanding but achievable. As of 5 September, customer numbers were at 263, leaving a fair bit to do to reach the year-end target of 330. This figure includes the first 45 customers for Commercio, 31 of which were already Syncore customers and 14 of which are new to the group.

The conversion of existing Partners should be the lower-hanging fruit, with the targets illustrated above predicated on also winning at least as many entirely new customers.

The GMV at 5 September was well ahead at $1.3bn, beyond the end FY22 target of $1.2bn and making headway towards the FY23 goal of $1.5bn. The amount spent with preferred suppliers was also already meeting the year-end target of $0.4bn, with over 50% of purchases being spent with the preferred supplier base.

Facilisgroup has high profit margins and excellent cash generation. It is using this foundation to invest in its sales and marketing activities as well as its technology products to drive its growth. This investment for revenue scale, has an impact on the adjusted EBITDA margin in the short term, as shown in the exhibit below. We have been cautious in our assumptions on this rebuilding, with the higher investment levels likely to continue through FY23, meaning there is potential for upside on our margin assumption for FY24.

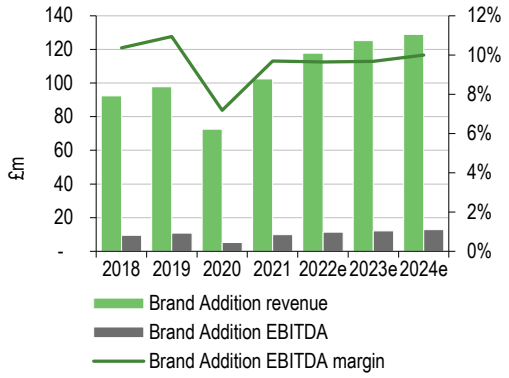
Exhibit 17: Facilisgroup record and projections



Source: The Pebble Group, Edison Investment Research

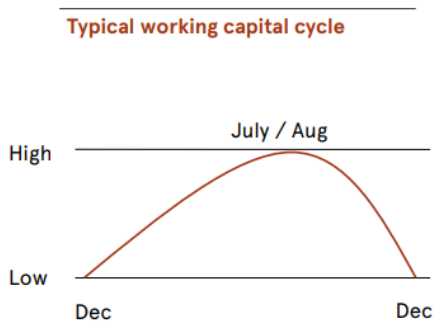
Brand Addition contributed 89% of FY21 revenue and 57% of group adjusted EBITDA

Exhibit 18: Brand Addition's record and Edison projections



Source: The Pebble Group accounts, Edison Investment Research

Exhibit 19: Brand Addition's typical working capital cycle



Source: The Pebble Group

The trading record for Brand Addition shows a revenue CAGR from 2016 through 2021 of 6.7%. Revenues were affected during the pandemic by lockdowns and working from home, as well as the suspension of large events such as trade shows. The Consumer Promotions division held steady at £29m of revenue in FY19 and FY20, while the Corporate Programmes division was more affected, with like-for-like sales falling from £69m to £41m. There was some amelioration with £3m of new business, which limited the reduction in Brand Addition revenues to 26% in FY20. There was, though, an immediate and full recovery of revenues in FY21 to £102m (FY19: £98m). This resulted

from growth in the Consumer Promotions, division, up 59% to £46m, with the Corporate Programme division benefiting from new client wins and some recovery in the FY19 like-for-like revenues. These new clients are helping build revenues in the current year as they become more established, while the resumption of more stabilised working patterns is supporting client confidence in planning its marketing activities.

Beyond the demand side of the equation, there has been some minor impact on gross margins due to one-off costs in FY21 associated with Brexit and the sudden escalation of freight costs in 2021 (FY19: 31.5%, FY21 28.6%), but these are now tracking back towards management's stated long-term guidance of 30%, with 29.9% posted for H122.

The adjusted EBITDA margin dipped to 7.2% in FY20, from 10.9% in FY19, reflecting the difficult trading backdrop, recovering to 9.7% in FY21. We have been cautious in our modelling assumptions given the underlying market cost inflation, assuming a gentle climb back to the 10.0% level by FY24e. This is based on 15% revenue growth in the current year, buoyed by the new business won in FY20 and FY21. H122 revenue growth was 29%, so this implies more modest second half progress of 6%, closer to the longer-term trend. We have modelled a similar rate for FY23e.

Group cash flow inherently positive

The group's cash flow is naturally a weaving together of the different dynamics of the two constituent business models. The key elements relate to the working capital flows within Brand Addition and the capital spent on developing the technology offering of Facilisgroup.

The exhibit below shows the development of free cash flow to date and how our model suggests that it plays out over the next couple of years.

FY20 was obviously not a typical year, either for Pebble or for its markets, and it is difficult to draw any meaningful conclusions beyond that that the group managed itself well. In FY20, Pebble remained profitable with adjusted EBITDA of around £10m and still generated free cash flow while investing into the future of Facilisgroup, despite the difficult market circumstances. We expect Pebble to continue to be healthily cash generative.

Exhibit 20: Summary free cash flow, historical and forecast

£000s	2020	2021	2022e	2023e
Adjusted EBITDA	9,755	15,378	17,600	19,250
Change in working capital	(1,747)	(2,861)	(1,818)	(1,096)
Tax	(1,313)	(521)	(2,323)	(3,101)
Capex	(5,677)	(5,282)	(8,800)	(9,050)
Free cash flow	1,018	6,714	4,659	6,002

Source: The Pebble Group accounts, Edison Investment Research

This propensity to generate cash naturally raises the question of priorities for the uses of capital. Directors have previously outlined a dividend policy of a pay-out of 30% of post-tax profits. Implementation of this, though, is currently in abeyance. The opportunities that the board sees for investing in and supporting the growth of Facilisgroup as it builds towards its target revenues are taking precedence for the time being. This position is being reviewed with each half-year results. However, for now, we have not included the payment of dividends in our modelling.

The period since the initial public offering has hardly been a typical trading pattern, given the impact of the COVID-19 pandemic, so M&A has clearly not been a priority. Facilisgroup was bought in December 2018, a year prior to the listing. We regard it as likely, given the directors' experience, that Pebble would be in the frame for other M&A opportunities in the promotional products sector, particularly in the United States or in Europe.

Cash positive balance sheet

Net debt at the half year end was minimal, at £0.1m, from a net cash position, excluding leases, at the previous year-end of £12.1m, with the H1 outflow following the normal seasonal pattern of Brand Addition. By 5 September, when the half year results were reported, the balance sheet had turned net cash positive, with a balance of £2.5m.

Borrowings are incurred by Brand Addition reflecting the timing of its clients ordering and stock call-off, with no requirement for debt funding at Facilisgroup, as would be expected for a software business. Brand Addition's working capital cycle typically peaks around July or August, with orders for major Consumer Promotions received and placed with manufacturers in Q1, manufactured, delivered and invoiced in Q2 and Q3, with the cash coming in in Q4. Corporate Programmes sales are more evenly spread across the year, but with orders more likely to increase through H2. None of this working capital is speculative and all is backed by the genuinely blue-chip client roster.

Our model suggests a year-end net cash figure, excluding leases, of £14.4m, building to £18.2m over the course of FY23 and to £22.8m the following year. Based on bank borrowing only, we expect there to be no debt at the year end, as was the case at end FY21, when cash was £12.1m.

Exhibit 21: Financial summary

£000s	2020	2021	2022e	2023e	2024e
Year end 31 December	IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT					
Revenue	82,374	115,101	133,000	142,500	147,000
Cost of Sales	(51,382)	(73,128)	(83,651)	(88,918)	(91,573)
Gross Profit	30,992	41,973	49,349	53,582	55,426.6
EBITDA	9,755	15,378	17,600	19,250	19,800
Normalised operating profit	6,225	10,581	12,400	13,950	14,450
Amortisation of acquired intangibles	0	0	0	0	0.0
Exceptionals	(542)	0	0	0	0
Share-based payments	(14)	(715)	(1,100)	(1,100)	(1,100)
Reported operating profit	5,669	9,866	11,300	12,850	13,350
Net Interest	(700)	(549)	(497)	(445)	(393)
Joint ventures & associates (post tax)	0	0	0	0	0
Exceptionals	0	0	0	0	0
Profit Before Tax (norm)	5,525	10,032	11,903	13,505	14,057
Profit Before Tax (reported)	4,969	9,317	10,803	12,405	12,957
Reported tax	(889)	(1,970)	(2,323)	(3,101)	(3,239)
Profit After Tax (norm)	4,531	7,875	9,344	10,128	10,543
Profit After Tax (reported)	4,080	7,347	8,480	9,303	9,718
Minority interests	0	0	0	0	0
Discontinued operations	0	0	0	0	0
Net income (normalised)	4,531	7,875	9,344	10,128	10,543
Net income (reported)	4,080	7,347	8,480	9,303	9,718
Basic average number of shares outstanding (m)	167	167	167	167	167
EPS - basic normalised (p)	2.71	4.70	5.58	6.05	6.30
EPS - diluted normalised (p)	2.71	4.69	5.57	6.04	6.28
EPS - basic reported (p)	2.44	4.39	5.06	5.56	5.80
Dividend (p)	0.00	0.00	0.00	0.00	0.00
Revenue growth (%)	(23.1)	39.7	15.6	7.1	3.2
Gross Margin (%)	37.6	36.5	37.1	37.6	37.7
EBITDA Margin (%)	11.8	13.4	13.2	13.5	13.5
Normalised Operating Margin	7.6	9.2	9.3	9.8	9.8
BALANCE SHEET					
Fixed Assets	63,611	63,900	69,300	74,850	80,600
Intangible Assets	54,016	55,673	60,273	65,073	70,073
Tangible Assets	9,102	7,927	8,727	9,477	10,227
Investments & other	493	300	300	300	300
Current Assets	40,992	51,566	60,073	67,092	73,252
Stocks	12,109	10,093	11,663	12,496	12,890
Debtors	20,988	29,422	33,997	36,426	37,576
Cash & cash equivalents	7,066	12,051	14,413	18,171	22,786
Other	829	0	0	0	0
Current Liabilities/ leases	27,109	31,469	35,795	37,961	39,052
Creditors	25,775	30,065	34,391	36,557	37,648
Tax and social security	0	20	20	20	20
Short term borrowings/ leases	1,334	1,384	1,384	1,384	1,384
Other	0	0	0	0	0
Long Term Liabilities	11,212	9,423	9,423	9,423	9,423
Long term borrowings/ leases	7,645	6,388	6,388	6,388	6,388
Other long term liabilities	3,567	3,035	3,035	3,035	3,035
Net Assets	66,282	74,574	84,155	94,558	105,376
Minority interests	0	0	0	0	0
Shareholders' equity	66,282	74,574	84,155	94,558	105,376
CASH FLOW					
EBITDA	9,212	15,378	17,600	19,250	19,800
Working capital	(1,747)	(2,861)	(1,818)	(1,096)	(453)
Exceptional & other	0	(13)	0	0	0
Tax	(1,313)	(521)	(2,323)	(3,101)	(3,239)
Net operating cash flow	6,152	11,983	13,459	15,052	16,108
Capex	(5,677)	(5,282)	(8,800)	(9,050)	(9,300)
Acquisitions/disposals	0	0	0	0	0
Net interest	(700)	(549)	(497)	(445)	(393)
Equity financing	0	0	0	0	0
Dividends	0	0	0	0	0
Other	(1,141)	(1,360)	(1,800)	(1,800)	(1,800)
Net Cash Flow	(1,366)	4,792	2,362	3,757	4,615
Opening net debt including leases/(cash)	(2,521)	1,913	(4,279)	(6,641)	(10,398)
FX	(429)	193	0	0	0
Other non-cash movements	(2,639)	1,207	0	0	0
Closing net debt including leases/(cash)	1,913	(4,279)	(6,641)	(10,398)	(15,013)

Source: company accounts, Edison Investment Research

Contact details	Revenue by geography
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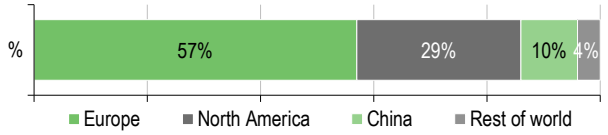

Management team

Chairman: Richard Law	CEO: Christopher Lee
Richard has broad senior management and board experience of business, engineering, corporate finance, technology and governance spanning 40 years. Richard retired as chief executive officer of AIM-quoted GB Group in 2017, having led the company from a market capitalisation of £5m to £500m, and took up a portfolio role investing in and chairing both public and private companies. As well as chairing The Pebble Group, Richard is currently the chairman of Vypr (a product intelligence and performance accelerator) and chairman designate of SmartSearch (a provider of online compliance solutions).	Chris has been with the group for 22 years and led the private equity backed management buyouts of Brand Addition in 2012 and in 2017, as well as the acquisitions of Gateway CDI and Facilisgroup in 2016 and 2018 respectively. He also led the listing of The Pebble Group on AIM in 2019.
CFO: Claire Thomson	
Claire has led the finance, banking, legal and compliance aspects of the businesses that now comprise The Pebble Group for over 13 years, taking the role of chief financial officer following the management buyout in 2012. Claire is a qualified chartered accountant and, prior to joining the group, spent 11 years in audit at PricewaterhouseCoopers, having joined in 1997.	

Principal shareholders	(%)
Liontrust AM	20.9
BlackRock IM	13.2
FIL Inv Intl	8.9
Capital Intl UK	8.0
Amati Global Investors	6.4
River & Mercantile	4.2
Aegon NV	4.1
Chris Lee (CEO)	3.6
Janus Henderson	3.4
BMO Global Investors	3.3
Chelverton AM	3.1

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