

Gear4music Holdings

Placing

European horizons open up

Gear4music's continued market share gains in the UK, and triple-digit growth in Europe, give line of sight to a significantly larger business with enhanced investment returns. Institutional investors have demonstrated their confidence in the company's growth strategy with the recent placing, but that has not been sufficient to address a market that continues to focus on higher value based on increasing market share.

Year end	Revenue (£m)	EBITDA (£m)	PBT* (£m)	EPS* (p)	P/E (x)	EV/EBITDA (x)
02/16	35.5	1.7	0.6	3.1	244.3	92.9
02/17	56.1	3.7	2.7	11.6	65.7	45.0
02/18e	79.7	4.1	2.4	10.0	76.4	40.2
02/19e	102.1	5.1	3.3	13.3	57.3	32.0

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

Expansion through European market share gains

G4M is on a path to major expansion. Its success in the UK, applying 21st century retail technology to disrupt a fragmented industry, is giving way to the prospect of a significantly larger presence on the continent. In FY17, European sales grew 124%, and G4M has opened distribution hubs in Sweden and Germany. Separately, it plans a US website, which should provide a platform for own-brand sales there. It is also acquiring a £5.3m freehold, catering for its medium-term head office needs.

Funding for investment opportunities

G4M has funded additional growth opportunities by raising £4.2m before expenses through a placing of 610,000 shares. It plans to invest the proceeds in the IT platform, international expansion, supply chain development, inventory investment, further enhancement of the marketing offering, the fit out of the new UK head office and further development of the German and Scandinavian hubs. The directors also placed 839,000 of their own shares and the CEO, who retains 34.3% of the shares, has undertaken not to sell further shares for one year.

Forecasts materially unchanged

As the placing represents only a 3.5% increase in share capital, there is no material change to our forecasts.

Valuation: Focus on the European opportunity

The placing was oversubscribed at 690p and the share price continues to demonstrate significant investor demand. The market is clearly focusing on the European opportunity. Based on a multiple of 2x sales, typical of pure-play online retailers, the current share price implies only a 2% revenue share of a European musical instrument and equipment market valued at £4.3bn, compared with G4M's 0.5% share now and its major competitor's 14% share. In the UK, G4M has already taken a 20% share, growing that at around 5% pa over the last three years. Thus, for G4M to reach a 2% European penetration looks achievable, and any over-achievement would give grounds for future upside.

Retail

5 June 2017

Price **764p**
Market cap **£159m**

Net cash (£m) at end February 2017	0.4
Shares in issue	20.9m
Free float	64%
Code	G4M
Primary exchange	AIM
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	43.6	13.2	468.0
Rel (local)	38.8	10.0	368.6
52-week high/low	808.5p	99.5p	

Business description

Gear4music is the largest dedicated, UK-based online retailer of musical instruments and music equipment. It sells branded instruments and equipment, alongside its own brand products, to customers ranging from beginners to professionals, in the UK and into Europe and the rest of the world.

Next events

AGM trading statement	July 2017
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**Gear4music Holdings is a
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Exhibit 1: Financial summary

	£'000	2016	2017	2018e	2019e	2020e
Year end: February		IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT						
Revenue		35,489	56,128	79,728	102,116	127,347
Cost of Sales		(26,303)	(40,983)	(58,615)	(74,875)	(93,382)
Gross Profit		9,186	15,145	21,114	27,242	33,965
EBITDA		1,688	3,650	4,092	5,133	6,649
Operating profit (before amort. and except.)		903	2,655	2,648	3,590	4,747
Amortisation of acquired intangibles		0	0	0	0	0
Exceptionals		(606)	0	0	0	0
Share-based payments		(8)	(39)	(73)	(66)	(83)
Reported operating profit		289	2,616	2,575	3,524	4,663
Net Interest		(283)	20	(289)	(265)	(264)
Joint ventures & associates (post tax)		0	0	0	0	0
Exceptionals		0	0	0	0	0
Profit Before Tax (norm)		620	2,675	2,360	3,325	4,482
Profit Before Tax (reported)		6	2,636	2,286	3,259	4,399
Reported tax		(49)	(322)	(283)	(532)	(717)
Profit After Tax (norm)		571	2,353	2,076	2,793	3,765
Profit After Tax (reported)		(43)	2,314	2,003	2,727	3,682
Minority interests		0	0	0	0	0
Discontinued operations		0	0	0	0	0
Net income (normalised)		571	2,353	2,076	2,793	3,765
Net income (reported)		(43)	2,314	2,003	2,727	3,682
Basic average number of shares outstanding (m)		18.2	20.2	20.7	20.9	20.9
EPS - basic normalised (p)		3.1	11.7	10.0	13.4	18.0
EPS - normalised (p)		3.1	11.6	10.0	13.3	18.0
EPS - basic reported (p)		(0.2)	11.5	9.7	13.1	17.6
Dividend per share (p)		0.00	0.00	0.00	0.00	0.00
Revenue growth (%)		46.4	58.2	42.0	28.1	24.7
Gross Margin (%)		25.9	27.0	26.5	26.7	26.7
EBITDA Margin (%)		4.8	6.5	5.1	5.0	5.2
Normalised Operating Margin		2.5	4.7	3.3	3.5	3.7
BALANCE SHEET						
Fixed Assets		4,477	7,102	14,067	15,124	16,255
Intangible Assets		3,238	5,537	6,432	6,971	7,465
Tangible Assets		1,239	1,565	7,634	8,153	8,790
Investments & other		0	0	0	0	0
Current Assets		11,194	16,035	24,687	28,821	34,099
Stocks		6,906	11,686	15,060	19,068	23,307
Debtors		740	1,348	1,915	2,452	3,058
Cash & cash equivalents		3,548	3,001	7,712	7,301	7,734
Other		0	0	0	0	0
Current Liabilities		(6,022)	(10,000)	(14,940)	(18,028)	(21,511)
Creditors		(5,188)	(7,379)	(10,722)	(13,710)	(17,096)
Tax and social security		0	0	0	0	3
Short term borrowings		(834)	(2,621)	(4,219)	(4,319)	(4,419)
Other		0	0	0	0	0
Long Term Liabilities		(290)	(1,415)	(4,368)	(4,154)	(3,804)
Long term borrowings		(127)	(24)	(4,278)	(4,064)	(3,714)
Other long term liabilities		(163)	(1,391)	(90)	(90)	(90)
Net Assets		9,359	11,722	19,445	21,763	25,039
Minority interests		0	0	0	0	3
Shareholders' equity		9,359	11,722	19,445	21,763	25,042
CASH FLOW						
Op Cash Flow before WC and tax		1,688	3,656	4,092	5,133	6,649
Working capital		(1,416)	(3,618)	(598)	(1,558)	(1,459)
Exceptional & other		(607)	28	(73)	(66)	(83)
Tax		0	(104)	(283)	(532)	(717)
Net operating cash flow		(335)	(38)	3,137	2,978	4,390
Capex		(1,509)	(2,195)	(7,680)	(2,601)	(3,034)
Acquisition: deferred payments		0	0	(409)	(409)	(409)
Net interest		(130)	(47)	(289)	(265)	(264)
Equity financing		9,535	0	0	0	0
Dividends		0	0	0	0	0
Other		0	0	0	0	0
Net Cash Flow		7,561	(2,280)	(5,240)	(297)	683
Opening net debt/(cash)		4,974	(2,587)	(356)	4,884	5,181
FX		0	0	0	0	0
Other non-cash movements		0	49	0	0	0
Closing net debt/(cash)		(2,587)	(356)	4,884	5,181	4,498

Source: Company accounts, Edison Investment Research

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