

GB Group

H119 results

Executing on growth strategy

GB Group's H119 results confirm that it is on track to reach its targets for 10%+ organic growth and 20%+ operating margins. As previously flagged, H119 reported growth rates are skewed by the large perpetual licence signed a year ago; adjusting for this the group achieved 11% underlying organic growth and 8% adjusted operating profit growth. We maintain our revenue and profitability forecasts, with small adjustments to our net cash forecasts.

Year end	Revenue (£m)	EBIT (£m)	PBT* (£m)	Dil. EPS* (p)	DPS (p)	P/E (x)
03/17	87.5	17.0	16.5	9.9	2.4	44.5
03/18	119.7	26.3	25.8	13.5	2.7	32.6
03/19e	136.4	27.0	26.4	13.8	3.0	31.8
03/20e	161.7	30.9	30.4	15.6	3.3	28.1

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

H119 results confirm 11% underlying organic growth

GBG reported revenue growth of 9% y-o-y and adjusted operating profit (AOP) decline of 16% y-o-y in H119, with an AOP margin of 15%. Adjusting for the £3.5m perpetual licence signed in H118, the group saw 14% revenue growth, of which 11% was organic. Underlying AOP increased 8% y-o-y, reflecting the investment the company is making in product and people to support organic growth plans. Reflecting typical seasonality and the inclusion of the Vix Veriify Global (VVG) acquisition from October, we would expect to see a stronger performance in H219. Management expects to achieve consensus revenue and profit expectations for FY19. We make no changes to our revenue and AOP forecasts, with a minor reduction in net cash to reflect exceptional costs incurred in FY19e.

Making progress with strategic priorities

The group made good progress in its strategy to drive global growth from the three core areas of identity verification, fraud and location intelligence while making acquisitions to bolster geographic reach, expertise, data sets and customers. The recent VVG acquisition strengthens eIDV and Loqate in Asia Pacific and adds new customers in financial services and gambling.

Valuation: Premium reflects growth opportunity

At 22.7x FY19e and 20.0x FY20e EBITDA, the stock trades at a premium to the UK software sector on an EV/EBITDA basis; on a P/E basis it trades at a discount in FY19 but a premium for FY20. Looking at more directly relevant sub-sectors, including global peers, the stock trades more in line with cyber-security peers, with similar levels of profitability and growth. We believe this premium rating is warranted, considering the group's historic track record of profitable growth and good cash generation combined with the opportunity from structural growth in identity data intelligence services and the potential for accretive acquisitions.

Software & comp services

27 November 2018

Price **438.5p**
Market cap **£671m**

Net cash (£m) at end H119 18.6

Shares in issue 153.1m

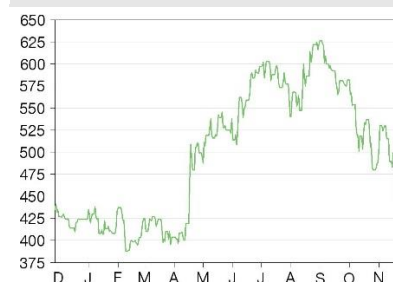
Free float 98%

Code GBG

Primary exchange AIM

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs (8.7) (29.5) 4.4

Rel (local) (10.0) (23.7) 10.2

52-week high/low 626p 388p

Business description

GB Group is a specialist in identity data intelligence. Its products and services enable its customers to better understand and verify their customers and employees, and are used across a range of fraud, risk management, compliance and customer on-boarding services. With headquarters in the UK, it operates across 24 countries and generates more than one-third of revenues internationally.

Next events

Capital markets day 13 December

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Review of H119 results

Exhibit 1: Half-year results highlights					
£m	H119	H118	Underlying H118	% y-o-y	Underlying y-o-y
Revenues	57.3	52.6	50.3	8.8%	13.9%
Gross profit	43.3	41.3		5.7%	
Gross margin	75.6%	78.6%	77%	(2.9%)	(1.4%)
Adjusted operating profit (AOP)*	8.8	10.4	8.1	(15.8%)	8%
Adjusted operating margin	15.3%	19.8%	16.1%	(4.5%)	(0.8%)
Reported operating profit	2.7	3.8		(28.4%)	
Reported operating margin	4.7%	7.2%		(2.5%)	
Normalised dil. EPS (p)	5.2	6.0		(13.3%)	0
Reported basic EPS (p)	1.3	1.6		(18.8%)	
Net cash	18.6	4.1		353.7%	

Source: GB Group. Note: *Adjusts for amortisation of acquired intangibles, share-based payments and exceptional items.

As highlighted in the recent trading update, GBG has reported revenue growth of 8.8% y-o-y for H119. Stripping out the effect of the perpetual licence signed in H118 (discussed in further detail below), and the £1.5m in revenues from the PCA Predict acquisition (a full six-month contribution versus four months a year ago), GBG generated underlying organic revenue growth of 11% y-o-y. New customers in the period included Kohl's, Abercrombie & Fitch, Hugo Boss, Aldi, Credit Harmony, PT Bank and CMBC, highlighting the international nature of the customer base.

Gross margin of 75.6% was 2.9pp lower than a year ago, again reflecting the perpetual licence signed in H118; adjusted for this, gross margin was 1.4pp lower y-o-y. Operating costs before depreciation, amortisation, share-based payments and exceptional items were 12% higher y-o-y but essentially flat h-o-h. The company incurred exceptional costs totalling £1.0m, of which £0.9m related to acquisitions and £0.1m to staff reorganisation. Tax of £0.5m equated to an effective rate of 20% of reported PBT and 6% of adjusted PBT. The group closed H119 with a net cash balance of £18.6m, up from the £4.1m reported a year ago and £13.5m at the end of FY18. Adjusted EBITDA to operating cash flow converted at a rate of 106% compared to 92% a year ago.

Divisional results skewed by prior year perpetual licence

Exhibit 2: Divisional revenues and adjusted operating profit (£m)				
Revenues	H119	H118	y-o-y	
eIDV	18.7	18.7	0%	
CAFS	6.3	5.4	17%	
T&I	5.4	5.0	10%	
E&C	3.2	3.1	5%	
Fraud, risk and compliance	33.6	32.1	5%	
Loqate	19.3	16.5	17%	
Engage	4.3	4.1	7%	
Location and customer intelligence	23.6	20.6	15%	
Total revenues	57.3	52.6	9%	
Adjusted operating profit (AOP)*				
Fraud, risk and compliance	5.6	7.7	-27%	
Location and customer intelligence	4.3	3.4	26%	
Unallocated costs	-1.1	-0.7	57%	
Group adjusted operating profit	8.8	10.4	-15%	
Adjusted operating margin				
Fraud, risk and compliance	17%	24%	-7%	
Location and customer intelligence	18%	17%	1%	
Group adjusted operating profit	15%	20%	-5%	

Source: GB Group. Note: *Adjusts for amortisation of acquired intangibles, share-based payments and exceptional items.

The table above shows H1 divisional revenue and adjusted operating profit. As previously discussed, the £3.5m perpetual licence signed in the eIDV business in H118 resulted in flat growth year-on-year for that division in H119. Treating the perpetual licence as a more typical three-year term licence would result in underlying eIDV revenues of £16.5m in H118, equating to growth of 13% y-o-y. CAFS and T&I both saw strong double-digit organic revenue growth. Excluding the £1.5m impact from the PCA acquisition, Loqate grew 8% y-o-y – the company noted that it saw strong growth in North America and plans to expand its East Coast team. Engage has contracted in recent years, so a return to growth is welcome.

The perpetual licence similarly skewed operating profit margins for eIDV and the group as a whole, with the group seeing a 5% margin decline year-on-year. Adjusting for the licence, AOP grew 8% on an underlying basis resulting in a margin of 15.3% for H119. We note that GBG reported adjusted operating profit margins of 14% in H117 and H116 and 16% in H115, reflecting the typical seasonality of the business which tends to see a higher level of licence renewals in H2. We see H119 results as reverting back to normal seasonality.

Further progress made against strategic priorities

The company has laid out its strategic priorities for the three years to 2021. We review H1 results in the context of these priorities.

Maximise growth from “3 global big bets”

The group is focused on driving growth on a global basis from the key areas of identity verification (eIDV), fraud management (CAFS) and location intelligence (Loqate). The divisional growth rates above highlight that these were the largest contributors to growth for the group during H119 and we would expect this to continue to be the case. In eIDV, GBG is focused on providing market leading solutions in its core markets (its UVP3¹ proposition). For IDScan, the company has developed a digital access model for document verification, to add to its existing on-premise scanner-based solution, and added digital tampering and liveness functionality to its digital on-boarding solution. In CAFS and Loqate, GBG has hired business development staff in the US, Germany and Asia, with total new hires of 31 for the group in H119. Loqate added seven new data suppliers during H1.

Revenue from international customers grew 31% y-o-y to make up 36% of group revenues in H119, up from 30% in H118 and 34% for FY18.

The company noted that it is going to exit the GOV.UK Verify scheme, for which government funding will stop in March 2019. We understand that this has not contributed material profits to the group so this is likely to have limited impact on our forecasts.

Optimise growth in specialist UK businesses

The T&I, E&C and Engage businesses are UK-focused and operate in lower growth markets. Management is keen to optimise the growth from these businesses and we would expect the company to be able to continue to generate mid-single digit revenue growth from each of these business lines.

Join up GBG with the customer at the centre

Since Chris Clarke joined as CEO in April 2017, the company has shifted its focus from product to customer, making it easier for the customer to access all GBG solutions that are required from one

¹ Unique Value Proposition Level Three

entry point. The three businesses involved in location intelligence are now combined into the Loqate division and the Loqate brand was launched in June to unify the products.

Use M&A to enhance reach and capability

GBG acquired Vix Verify Global in October² for £21.2m, adding further reach in Asia Pacific for identity verification and location intelligence solutions. The deal adds 400 customers and 74 employees. We expect the company to make further acquisitions, to expand functionality, expertise and geographic coverage. At the end of H119, the company had £41.1m undrawn on its credit facility. In October £10m was drawn down to fund the VVG acquisition, leaving £31.1m of group borrowing capacity for future deals to add to the post-VVG cash balance of £16.3m.

Outlook and changes to forecasts

The company expects to meet consensus revenue and profit forecasts for FY19. We make no changes to our revenue or AOP forecasts. We have revised our estimates to reflect the £1m in exceptional costs incurred in H119, an additional £0.8m in costs for H2 relating to the VVG acquisition and the £0.4m received from the issue of shares.

Exhibit 3: Changes to estimates							
£m	FY19e			FY20e			
	previous	new	change	previous	new	change	
Revenues	136,350	136,350	0.0%	161,733	161,676	0.0%	
EBITA	27,000	27,000	0.0%	30,942	30,932	0.0%	
EBITA margin (%)	19.8%	19.8%		19.1%	19.1%		
PBT	26,431	26,431	0.0%	30,362	30,352	0.0%	
EPS - normalised, diluted (p)	13.8	13.8	0.0%	15.6	15.6	(0.1%)	
EPS - reported (p)	6.9	5.7	(17.4%)	9.5	9.5	(0.1%)	
Net (cash)/debt	(7,185)	(5,697)	-20.7%	(24,746)	(23,249)	(6.1%)	

Source: Edison Investment Research

Valuation

The table below shows GBG trades compared to ID management companies, Identity Access Management software companies and more general cyber-security companies, as well as UK software peers.

Exhibit 4: Peer group financial and valuation metrics												
	Rev growth		EBITDA margin		EBIT margin		EV/Sales		EV/EBITDA		P/E	
	Yr1	Yr2	Yr1	Yr2	Yr1	Yr2	Yr1	Yr2	Yr1	Yr2	Yr1	Yr2
GBG	13.9%	18.6%	21.8%	20.8%	19.8%	19.1%	4.9	4.2	22.7	20.0	31.8	28.1
Average sub-sector:												
ID Management	8.9%	8.0%	18.8%	26.0%	13.7%	19.9%	3.6	3.6	34.5	15.2	20.8	18.3
Identity Access Management	27.7%	23.7%	-14.3%	-0.9%	-20.9%	-6.6%	7.2	5.7	21.2	16.1	34.2	27.1
Cyber Security	15.6%	12.9%	20.8%	22.4%	16.8%	18.6%	5.3	4.7	26.9	21.8	33.9	29.2
UK Software	27.3%	20.3%	17.2%	22.5%	11.2%	16.9%	6.0	4.1	21.9	12.9	34.8	20.4

Source: Edison Investment Research, Thomson Eikon (as at 26 November)

The stock trades at a premium to the UK software sector on an EV/EBITDA basis; on a P/E basis it trades at a discount in FY19 but a premium for FY20. Looking at more directly relevant sub-sectors, including global peers, the stock trades on multiples more akin to cyber-security peers, with similar levels of profitability and growth. We believe this premium rating is warranted, considering the group's historic track record of profitable growth and good cash generation combined with the

² See "[Scaling up down under](#)" and "[FY19 growth on track](#)".

opportunity from structural growth in identity data intelligence services. Using a reverse DCF, we estimate that the current share price is factoring in low-double digit revenue growth and EBITDA margins of 21.5%, in line with management's targets for organic growth of 10%+ and AOP margins of 20%+. We expect management to continue to make accretive acquisitions to boost growth, which should provide further support to the share price.

Exhibit 5: Financial summary

	£'000s	2015	2016	2017	2018	2019e	2020e
March		IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS							
Revenue		57,283	73,401	87,468	119,702	136,350	161,676
Cost of Sales		(16,448)	(17,606)	(20,302)	(27,092)	(33,910)	(39,952)
Gross Profit		40,835	55,795	67,166	92,610	102,440	121,724
EBITDA		11,844	14,772	18,734	28,741	29,675	33,689
Operating Profit (before amort. and except.)		10,790	13,428	17,006	26,311	27,000	30,932
Acquired intangible amortisation		(1,986)	(2,501)	(4,022)	(7,885)	(8,100)	(7,300)
Exceptionals		(1,629)	(94)	(1,410)	(2,143)	(1,830)	0
Share of associate		(10)	0	0	0	0	0
Share based payments		(971)	(1,245)	(994)	(2,375)	(2,500)	(2,750)
Operating Profit		6,194	9,588	10,580	13,908	14,570	20,882
Net Interest		(266)	(270)	(498)	(508)	(569)	(580)
Profit Before Tax (norm)		10,524	13,158	16,508	25,803	26,431	30,352
Profit Before Tax (FRS 3)		5,928	9,318	10,082	13,400	14,001	20,302
Tax		(1,127)	(178)	668	(2,746)	(5,286)	(5,767)
Profit After Tax (norm)		8,314	10,395	13,206	20,642	21,541	24,585
Profit After Tax (FRS 3)		4,801	9,140	10,750	10,654	8,715	14,535
Average Number of Shares Outstanding (m)		119.1	122.7	131.6	150.6	153.0	153.6
EPS - normalised (p)		7.0	8.5	10.0	13.7	14.1	16.0
EPS - normalised and fully diluted (p)		6.7	8.2	9.9	13.5	13.8	15.6
EPS - (IFRS) (p)		4.0	7.4	8.2	7.1	5.7	9.5
Dividend per share (p)		1.9	2.1	2.4	2.7	3.0	3.3
Gross Margin (%)		71.3	76.0	76.8	77.4	75.1	75.3
EBITDA Margin (%)		20.7	20.1	21.4	24.0	21.8	20.8
Operating Margin (before GW and except.) (%)		18.8	18.3	19.4	22.0	19.8	19.1
BALANCE SHEET							
Fixed Assets		51,238	59,364	105,653	170,284	183,360	176,053
Intangible Assets		45,296	54,113	98,753	161,372	173,492	165,212
Tangible Assets		2,829	2,234	2,856	4,700	5,656	6,629
Other fixed assets		3,113	3,017	4,044	4,212	4,212	4,212
Current Assets		33,186	36,189	48,914	61,121	66,606	87,941
Debtors		17,408	23,774	30,569	37,969	45,262	53,045
Cash		15,778	12,415	17,618	22,753	20,945	34,497
Other		0	0	727	399	399	399
Current Liabilities		(30,784)	(32,559)	(44,444)	(56,942)	(61,890)	(67,173)
Creditors		(24,305)	(30,927)	(36,436)	(56,100)	(61,093)	(66,376)
Contingent consideration		(5,733)	(1,050)	(7,122)	(45)	0	0
Short term borrowings		(746)	(582)	(886)	(797)	(797)	(797)
Long Term Liabilities		(7,506)	(6,593)	(15,940)	(16,711)	(22,711)	(18,711)
Long term borrowings		(3,643)	(3,160)	(11,499)	(8,451)	(14,451)	(10,451)
Contingent consideration		(895)	0	0	0	0	0
Other long term liabilities		(2,968)	(3,433)	(4,441)	(8,260)	(8,260)	(8,260)
Net Assets		46,134	56,401	94,183	157,752	165,364	178,109
CASH FLOW							
Operating Cash Flow		11,684	13,397	16,305	31,620	25,545	31,189
Net Interest		(266)	(282)	(498)	(545)	(569)	(580)
Tax		(337)	(248)	(2,193)	(3,247)	(5,286)	(5,767)
Capex		(2,011)	(1,762)	(2,227)	(2,018)	(2,650)	(2,750)
Acquisitions/disposals		(18,672)	(12,263)	(36,840)	(70,363)	(21,245)	0
Financing		10,954	790	24,755	56,668	446	0
Dividends		(1,955)	(2,277)	(2,775)	(3,582)	(4,049)	(4,540)
Net Cash Flow		(603)	(2,645)	(3,473)	8,533	(7,809)	17,552
Opening net debt/(cash)		(11,846)	(11,389)	(8,673)	(5,233)	(13,505)	(5,697)
HP finance leases initiated		0	0	0	0	0	0
Other		146	(71)	33	(261)	0	0
Closing net debt/(cash)		(11,389)	(8,673)	(5,233)	(13,505)	(5,697)	(23,249)

Source: GB Group, Edison Investment Research

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