EDISON

GB Group

Excellent first half underpins outlook

Interim results

Software & comp services

The year-on-year doubling of EBITA in H118 reflects continued strong underlying organic growth at GB Group (GBG), boosted by recent acquisitions and a perpetual licence deal. H2 has started well and forecasts, which are largely unchanged, appear comfortably underpinned. GBG's consistent organic performance and increasing product innovation support its current rating, meanwhile its buy and build strategy could support further earnings-driven share price upside.

Year end	Revenue (£m)	EBITA (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
03/16	73.4	13.4	13.2	8.2	2.1	53.0	0.5
03/17	87.5	17.0	16.5	9.9	2.4	43.9	0.6
03/18e	117.1	23.3	22.6	11.8	2.5	36.9	0.6
03/19e	133.4	27.0	26.4	13.5	2.8	32.2	0.6

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

Excellent first half result

H1 results were as preannounced in October's trading update. Revenues increased 40% y-o-y and EBITA of £10.4m doubled. The strong performance reflects the initial contribution from the acquisition of PCA Predict in May and a full six months from ID Scan, both of which continue to perform ahead of management's expectations. Headline organic growth of 18% and EBITA margins of 19.8%, which were up 6pp on last year, were boosted by a £3.5m licensing deal. Backing this out, the underlying organic growth rate remains a consistent 12%, and margins were broadly flat year on year. Cash conversion at 92% remains high.

Forecasts comfortably underpinned

Bar the consumer engagement services (renamed to Building Relationships), growth was strong across all product lines, particularly so in fraud, risk and compliance as well as in the enlarged location intelligence segment (which includes Matchcode 360, Loqate and PCA Predict). H2 is reported to have started well and with 70% of revenues recurring in nature and a 53% increase in the deferred revenue balance, our forecasts for the full year appear comfortably underpinned.

Valuation: Momentum, investment and market

The revenue visibility and operational gearing characteristics of GBG could support a higher EBITA margin. However, management intends to manage the margin to approximately 20% over the next few years. This is enabling it to reinvest a widening margin in innovation, data sets and international expansion. It is also bolstering resources dedicated to improving customer services. These initiatives, together with the supportive market backdrop from the rising requirement for security, compliance and data management demanded by a globalising online community, should support a continued strong organic performance for the group and GBG's 32.2x P/E rating (in line with cyber security peers). Meanwhile, its active M&A pipeline has the potential to support earnings-driven share price upside.

28 November 2017

Price	**435p**
Market cap	**£663m**

Net cash (£m) at 30 September	4.1
Shares in issue	152.5m
Free float	97%
Code	GBG
Primary exchange	AIM
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	1.2	13.4	87.7
Rel (local)	2.7	13.4	72.1
52-week high/low		455p	230p

Business description

GB Group (GBG) 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 17 countries and generates 30% of revenues internationally.

Next events

Trading update	April 2018

Analysts

Bridie Barrett +44 (0)20 3077 5700

Dan Ridsdale +44 (0)20 3077 5729

tech@edisongroup.com

Edison profile page

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H1 results summary

Revenues increased by 40% to £52.6m, of which organic growth accounted for 18%, or 12% when adjusting for the impact of the sale of a perpetual licence within IDScan to a European bank. PCA Predict (acquired 9 May 2017) and IDScan (acquired 9 June 2016) together accounted for 22% of growth.

We understand that the licensing deal was from a leading European bank, which had previously bought the product from IDScan on this basis (before its acquisition by GB Group in June 2016).The company's focus and incentive structures remain strongly weighted towards recurring revenues, which accounted for c 70% of revenues in FY17. However, this customer had allocated the spend to capex and was not prepared to reverse this. The full £3.5m was received in H1.

Adjusted EBITA of £10.4m increased by 101% and the adjusted EBITA margin increased by c 6pp to 19.8%. Backing out the impact of the licence implies an underlying margin of 14.1%, in line with that reported in H117. Despite the impact of a higher effective tax rate (13% vs 8% in H117), adjusted diluted EPS increased by 71% to 6.0p.

On a reported basis, net earnings of £2.4m (+98%) were affected by a higher charge for amortisation of acquired intangibles (£3.8m), £1.1m of share-based payments and a £1.7m exceptional charge related to the acquisitions.

Operating cash flow of £10.5m equates to a 92% cash conversion (H117: 77%). Cash conversion has benefited in part due to the upfront payment of this licence, as well as from the inclusion of the PCA business, which has a prepayment business model, as well as the implementation of a wholly owned foreign enterprise (WOFE) in order to shorten the receivables cycle in Chinese business. After the £62.9m paid for PCA Predict (net of cash acquired) and £56.3m net proceeds from the placing in May, net cash of £4.1m was reported (from net cash of £5.2m at March 2017).

Exhibit 1: Summary H118 results

£m	H116	FY16	H117	FY17e	H118	y-o-y change	FY18e
Revenues	**32.4**	**73.4**	**37.5**	**87.5**	**52.6**	**40%**	**117.1**
Share of full year total from H1	44%	100%	43%	100%	45%		100%
Gross profit	24.6	55.8	28.9	67.2	41.3	43%	88.6
Gross profit margin	75.9%	76.0%	77.0%	76.8%	78.6%		75.6%
EBITA	**4.5**	**13.4**	**5.2**	**17.0**	**10.4**	**101%**	**23.3**
EBITA margin	14.0%	18.3%	13.9%	19.4%	19.8%		19.9%
Amortisation of acquired intangibles	(1.3)	(2.5)	(1.8)	(4.0)	(3.8)	117%	(3.5)
Share-based payments	(0.6)	(1.2)	(0.7)	(1.0)	(1.1)	67%	(1.8)
Exceptional items	(0.0)	(0.1)	(1.0)	(1.4)	(1.7)	75%	(2.2)
Reported operating profit	2.7	9.6	1.8	10.6	3.8	111%	15.9
Net financing costs	(0.1)	(0.3)	(0.2)	(0.5)	(0.3)	17%	(0.8)
Adjusted PBT	4.4	13.2	5.0	16.5	10.2	105%	22.6
Reported PBT	2.6	9.3	1.6	10.1	3.5	125%	15.1
Tax	(0.3)	(0.2)	(0.3)	0.7	(1.1)	228%	(4.5)
PAT – adjusted	4.1	13.0	4.6	17.2	9.1	96%	18.0
PAT – reported	2.3	9.1	1.2	10.8	2.4	98%	10.6
Adjusted diluted EPS (p)		8.2	3.5	9.9	6.0	71%	11.6

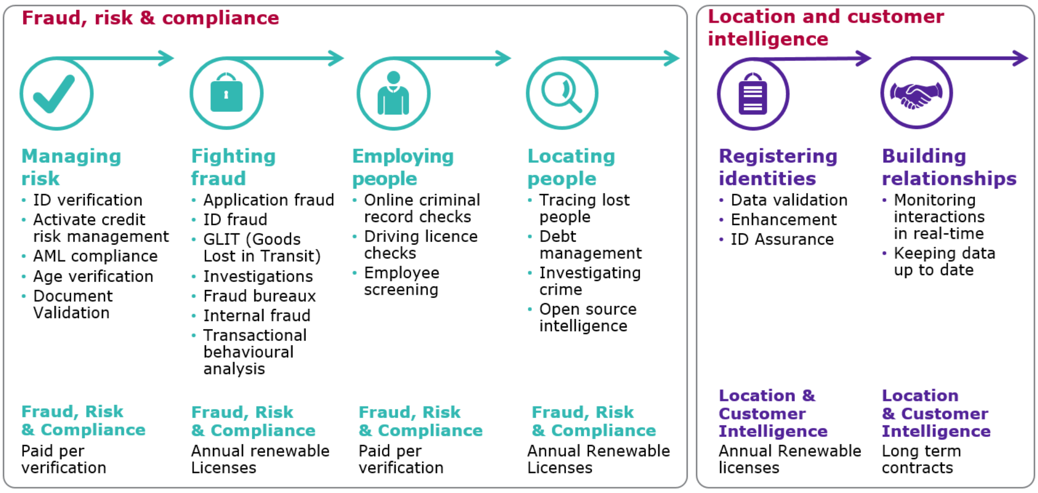
Source: GB Group (historics), Edison Investment Research (forecasts)

New divisional classification

Having made 10 acquisitions over the last six years, the group structure has changed considerably, and management has reclassified its divisions to more appropriately reflect the end markets for their services as well as to provide more intuitive names for its service lines.

Identity Proofing (IDP) becomes Fraud, Risk and Compliance (FRC), and Identity Solutions (IDS) becomes Location and Customer Intelligence (LCI). Within these classifications, the Trace and Investigate service is now classified within Fraud, Risk and Compliance. Exhibit 2 details the new divisional structure.

Exhibit 2: New divisional classification



Source: GB Group

Divisional performance

The Fraud, Risk and Compliance (FRC) division saw revenues increase by 35% to £32.1m with EBITA margins of 24.0% (H117: 18.6%) resulting in a 74% increase in EBITA to £7.7m. Location and Customer Intelligence (LCI) revenues increased by 50% to £20.6m and EBITA margins almost doubled y-o-y to 16.7% resulting in a near doubling of EBITA to £3.4m.

Fraud, risk and compliance: 12% of revenue growth relates to the inclusion of IDScan (within managing risk) for a full six months. The organic growth of 27% in part reflects the aforementioned sale of a perpetual licence. Backing this out, underlying divisional organic growth was 12%. All product lines performed well, particularly the fraud and risk management products.

The licence sale added £3.5m to divisional EBITA and accounts for the 5.4pp increase in margins to 24.0%. On an underlying basis, margins in this division were approximately 14.6%, down on last year's 18.6%, consistent with management's strategy to increase the pace of investment in this division in order to support the international growth plan, deepening of data sets and investment in capabilities. It also continues to absorb losses from GBG's gov.uk/verify platform, which has had a slower uptake than initially anticipated.

Location and Customer Intelligence: Organic growth was 2% and the acquisition impact from PCA Predict 48%. Whereas the consumer engagement services continue to feel the effects of competitive pressure (revenues down 9%), Identity Registration services increased revenues by 77%. We estimate that the acquisition of PCA Predict accounts for c 70% of this growth, which means 7% organic growth from these services; PCA Predict, which provides type ahead look up functionality to SMEs, provides an excellent complement to GBG's other address intelligence services: Loqate and Matchcode 360. This acquisition (which we looked at in more detail in our May report, PCA acquisition an excellent fit) has given the group a market-leading position in the address intelligence market. The integration is on track; first half profits and revenues are ahead of management's expectations and it has accelerated its plans to expand in the US and Germany (with Australia to follow). Moving forward, the three product sets within the registering identities segment will be moved to a common brand, and more of GBG's wider data sets integrated. The integration of PCA Predict underpinned the near doubling of margins in this division to 16.7%.

Exhibit 3 presents the divisional performance in H118. Given the new classification of divisions, we also include some historical information under the new segmentation.

Exhibit 3: Divisional performance – new classification (£000s)

Revenues	2015	H116	2016	H117	2017	H118
Managing risk	14,900	9,600	19,800	12,354	27,614	18,555
Locating people	8,600	4,000	9,900	4,800	11,000	5,000
Fraud management	6,000	3,300	7,700	3,700	10,300	5,400
Employ and comply	4,300	2,500	5,000	2,900	5,900	3,100
Total: Fraud, Risk & Compliance	**33,800**	**19,400**	**42,400**	**23,754**	**54,814**	**32,055**
Registering identities	13,500	7,500	18,000	9,300	22,172	16,471
Building relationships	10,100	5,400	13,000	4,500	10,500	4,100
Total: Location & Customer Intelligence	**23,600**	**12,900**	**31,000**	**13,758**	**32,672**	**20,571**
Total revenue	**57,283**	**32,368**	**73,401**	**37,512**	**87,468**	**52,626**
Revenue growth						
Managing risk	26%	43%	33%	29%	39%	50%
Locating people (Trace and investigate)	19%	21%	15%	20%	11%	4%
Fraud management		27%	28%	12%	34%	46%
Employ and comply	30%	25%	16%	16%	18%	6%
Total: Fraud, Risk & Compliance	**52%**	**33%**	**25%**	**22%**	**29%**	**35%**
Registering identities	4%	32%	33%	24%	23%	78%
Building relationships	58%	80%	29%	-17%	-19%	-10%
Total: Location & Customer Intelligence	**21%**	**50%**	**31%**	**7%**	**5%**	**50%**
Total revenue growth	37%	39%	28%	16%	19%	40%
EBITA margins						
Fraud, Risk & Compliance	19.5%	22.2%	24.3%	18.6%	23.6%	24.0%
Location & Customer Intelligence	20.3%	5.4%	12.9%	8.5%	14.6%	16.7%
Group (post group costs)	18.8%	14.0%	18.3%	13.9%	19.4%	19.8%

Source: GB Group

Outlook: On track to meet FY18 expectations

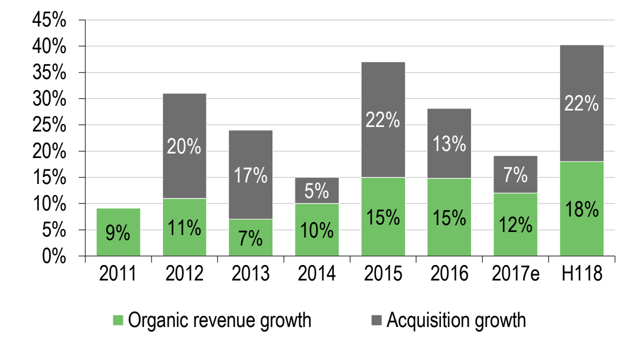
Bar the consumer marketing services, all of GBG's product lines are growing strongly, as are the recent acquisitions: GBG DecTec, GBG Loqate, ID Scan and PCA Predict. H2 has reportedly started well, with good growth both from the UK and internationally (now accounting for 30% of revenues or 33% adjusting for PCA).

The recognition of 100% of the revenues from the perpetual licence sale means this year will be more H1 weighted than typical. However, the underlying organic growth of 12% is consistent with our FY estimates, and recent periods and our full year forecast look very well underpinned; approximately 70% of revenues are recurring in nature, and the H118 deferred revenue balance has increased 53% y-o-y to £23.7m (covering 20% of our FY18 revenue forecast, vs 18% this time last year).

With a target EBIT margin of c 20%, this good visibility and high operational gearing is enabling the group to invest a widening margin in expanding and improving its product sets, international expansion as well as increasing its focus on customer service, further supporting future growth.

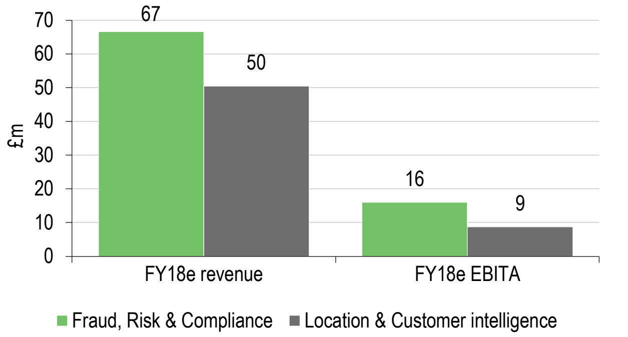
We leave our estimates for adjusted net profit. However, we make some changes to our forecast for amortisation of acquired intangibles following the recent acquisitions and make some small changes to our estimates for share based payments and the diluted share count. These changes result in a slight reduction to our adjusted EPS (2% in FY18e) and reduce our forecasts for reported EPS by 48% in FY18 to 3.7p and 35% in FY19 to 7.0p.

Exhibit 4: Trend of organic vs acquisition growth



Source: GB Group

Exhibit 5: New divisional revenue and EBIT split FY18e



Source: Edison Investment Research

Valuation

On an EV/EBITA of 28.3x FY18 (March year-end) and 24.4x in FY19, and P/E multiples of 36.9x and 32.2x, respectively, the shares are already factoring in the group's superior growth prospects to other identity management groups such as Experian and Equifax (average of 19.0x FY17 EV/EBIT, 17.3x FY18 EBIT). With approximately 60% of revenues now derived from the fast-growing Fraud, Risk and Compliance services and a further 30% from the high-growth services for Registering Identities and Location Intelligence, we believe it appropriate to benchmark GBG against the wider internet security peer set, which shares similar organic growth and margin characteristics as GBG. This peer set trades on an average EV/EBITA of 26.0x this year and 21.8x next year and on P/Es of 41.7x and 30.5x, respectively, in line with GBG.

We believe this rating is supported by the group's organic growth prospects. By way of illustration, a reverse DCF (8.4% WACC, 3% perpetuity growth after 10 years) implies that the current share price is discounting organic revenue growth of approximately 13% over the next 10 years, assuming a stable EBITDA margin (in line with management's current policy).

GBG's growing scale, widened product sets and international presence should support the current level of organic growth over the medium term, and the investments made in product and customer have the potential to add new revenue streams further down the line.

We see potential for share price upside to be driven through management's active M&A strategy. GBG has made 10 acquisitions over the last five years, adding capabilities, data sets and client reach, as well as driving revenue and cost synergies; most recently, it acquired PCA Predict, which is expected to be earnings accretive in its first year despite a planned increase in investment. The global market for identity data intelligence services remains fragmented, which should provide GBG with a steady pipeline of acquisition opportunities.

Exhibit 6: DCF scenarios (p/share)

		EBITDA margin							
		20.0%	**21.0%**	**22.0%**	**23.0%**	**24.0%**	**25.0%**	**26.0%**	**27.0%**
Revenue growth	**3.0%**	35	36	38	40	41	43	45	47
	5.0%	98	103	109	115	121	128	135	142
	7.5%	176	186	197	209	221	233	247	261
	10.0%	254	270	286	302	320	339	359	380
	12.5%	349	370	**392**	**415**	440	466	494	523
	15.0%	411	436	462	490	520	551	583	618

Source: Edison Investment Research

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Exhibit 7: Financial summary

£000s	2014	2015	2016	2017	2018e	2019e
Year end March	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Revenue	41,835	57,283	73,401	87,468	117,093	133,352
Cost of Sales	(14,473)	(16,448)	(17,606)	(20,302)	(28,538)	(32,461)
Gross Profit	27,362	40,835	55,795	67,166	88,555	100,890
EBITDA	7,849	11,844	14,772	18,734	25,300	29,270
Operating Profit (before amort. and except.)	7,164	10,790	13,428	17,006	23,300	27,000
Acquired intangible amortisation	(1,110)	(1,986)	(2,501)	(4,022)	(8,000)	(8,000)
Exceptionals	(1,080)	(1,629)	(94)	(1,410)	(2,200)	0
Share of associate	(159)	(10)	0	0	0	0
Share based payments	(747)	(971)	(1,245)	(994)	(2,300)	(2,500)
Operating Profit	4,068	6,194	9,588	10,580	10,800	16,500
Net Interest	(79)	(266)	(270)	(498)	(600)	(500)
Profit Before Tax (norm)	7,085	10,524	13,158	16,508	22,700	26,500
Profit Before Tax (FRS 3)	3,989	5,928	9,318	10,082	10,200	16,000
Tax	(474)	(1,127)	(178)	668	(4,540)	(5,300)
Profit After Tax (norm)	5,597	8,314	10,395	13,206	18,160	21,200
Profit After Tax (FRS 3)	3,515	4,801	9,140	10,750	5,660	10,700
Average Number of Shares Outstanding (m)	109.6	119.1	122.7	131.6	151.0	152.8
EPS - normalised (p)	5.1	7.0	8.5	10.0	12.0	13.9
EPS - normalised and fully diluted (p)	4.8	6.7	8.2	9.9	11.8	13.5
EPS - (IFRS) (p)	3.2	4.0	7.4	8.2	3.7	7.0
Dividend per share (p)	1.7	1.9	2.1	2.4	2.5	2.8
Gross Margin (%)	65.4	71.3	76.0	76.8	75.6	75.7
EBITDA Margin (%)	18.8	20.7	20.1	21.4	21.6	21.9
Operating Margin (before GW and except.) (%)	17.1	18.8	18.3	19.4	19.9	20.2
BALANCE SHEET						
Fixed Assets	26,985	51,238	59,364	105,653	172,353	164,733
Intangible Assets	23,329	45,296	54,113	98,753	164,653	156,503
Tangible Assets	1,519	2,829	2,234	2,856	3,656	4,186
Other fixed assets	2,137	3,113	3,017	4,044	4,044	4,044
Current Assets	23,775	33,186	36,189	48,187	66,461	84,785
Debtors	11,929	17,408	23,774	30,569	49,815	57,394
Cash	11,846	15,778	12,415	17,618	16,646	27,391
Other	0	0	0	0	0	0
Current Liabilities	(17,861)	(30,784)	(32,559)	(44,444)	(61,190)	(66,469)
Creditors	(17,861)	(24,305)	(30,927)	(36,436)	(53,182)	(58,461)
Contingent consideration	0	(5,733)	(1,050)	(7,122)	(7,122)	(7,122)
Short term borrowings	0	(746)	(582)	(886)	(886)	(886)
Long Term Liabilities	(2,066)	(7,506)	(6,593)	(15,940)	(23,040)	(19,040)
Long term borrowings	0	(3,643)	(3,160)	(11,499)	(18,599)	(14,599)
Contingent consideration	0	(895)	0	0	0	0
Other long term liabilities	(2,066)	(2,968)	(3,433)	(4,441)	(4,441)	(4,441)
Net Assets	30,833	46,134	56,401	93,456	154,584	164,009
CASH FLOW						
Operating Cash Flow	9,355	11,684	13,397	16,305	20,600	26,970
Net Interest	(79)	(266)	(282)	(498)	(600)	(500)
Tax	65	(337)	(248)	(2,193)	(4,540)	(5,300)
Capex	(1,144)	(2,011)	(1,762)	(2,227)	(2,700)	(2,650)
Acquisitions/disposals	(1,443)	(18,672)	(12,263)	(36,840)	(74,000)	0
Financing	416	10,954	790	24,755	56,261	0
Dividends	(1,632)	(1,955)	(2,277)	(2,775)	(3,093)	(3,775)
Net Cash Flow	5,538	(603)	(2,645)	(3,473)	(8,072)	14,745
Opening net debt/(cash)	(6,308)	(11,846)	(11,389)	(8,673)	(5,233)	2,839
HP finance leases initiated	0	0	0	0	0	0
Other	0	146	(71)	33	0	0
Closing net debt/(cash)	(11,846)	(11,389)	(8,673)	(5,233)	2,839	(11,906)

Source: GB Group (historic), Edison Investment Research (forecast)

Frankfurt +49 (0)69 78 8076 960
Schumannstrasse 34b
60325 Frankfurt
Germany

London +44 (0)20 3077 5700
280 High Holborn
London, WC1V 7EE
United Kingdom

New York +1 646 653 7026
295 Madison Avenue, 18th Floor
10017, New York
US

Sydney +61 (0)2 8249 8342
Level 12, Office 1205
95 Pitt Street, Sydney
NSW 2000, Australia