EDISON

OnTheMarket

First day of dealings/initiation

First day OnTheMarket

Media

OnTheMarket (OTM) has listed on AIM, raising £30m to build market share in the UK online property portal space. Founded as a mutual by estate agents, it is more closely aligned to their interests than the two main incumbents. The monies raised will be invested in sales and in IT, as well as funding a major marketing campaign to grow the agency network and increase brand awareness. This will push the group into loss for FY19 and FY20, with profits modelled from FY21 on. Backed by long-term agent contracts, OTM has high levels of recurring income on a scalable platform.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	EV/sales (x)
01/16	17.9	(3.1)	(8.8)	0.0	N/A	4.0
01/17	17.8	1.0	2.7	0.0	61.1	4.0
01/18e	16.0	2.2	6.2	0.0	26.1	4.4
01/19e	18.0	(21.4)	(35.3)	0.0	N/A	3.9
01/20e	35.0	(12.6)	(16.7)	0.0	N/A	2.0

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

Going for share

The UK online property market is dominated by two portals, Rightmove and ZPG/Zoopla, the former being clear market leader. While they generate high levels of traffic, prices charged to participating agencies have risen, with no respite in sight prior to OTM's arrival. OTM was set up as Agents' Mutual as an alternative, to provide a positive search experience for consumers, while acting in the interests of agents. Around 20% of participating agents' total inventory is placed exclusively on the OTM portal for a limited initial period. The flotation raised £30m gross to scale the business, step up agent recruitment and drive traffic. OTM can issue equity to attract key agents to the network on long-term contracts (not possible to model in advance), with others being attracted in with discounted or free listings.

Targeting profitability in FY21

It would be possible to deliver profits at an earlier stage by turning down the marketing tap, but that would not be in the interests of building a sustainable business. Our model indicates average revenue per partner agency (ARPA) bottoming out in the current financial year to January 2019 as new agencies are brought on board, then rising towards the level achieved by Zoopla, which is less than half that charged by Rightmove.

Valuation: Dependent on modelling of discounts

The valuation is highly dependent on the modelling of listing fee discounting and how successful it is in adding to the network. With forecast EBITDA and PBT losses (although profits at EBIT level, pre-marketing), traditional valuation metrics are unhelpful. At the 165p issue price, OnTheMarket trades at 3.9x forecast EV/revenue to January 2019, compared with Rightmove at 16.1x and ZPG at 5.2x current year published revenue (10.4x average for a broader global peer set). We have also modelled the DCF, based on a WACC of 10.2%. This derives a value of 323p per share, but, given the potential variability of outcomes, we would suggest an execution risk discount of 30% would be appropriate, indicating a price of 226p.

9 February 2018

Price	**165p**
Market cap	**£100m**

Net cash (£m) (including proceeds)	29.1m
Shares in issue	60.5m
Free float	41%
Code	OTMP
Primary exchange	AIM
Secondary exchange	N/A

Business description

OnTheMarket is an estate agent-backed company, which operates a synonymous property portal. It is the third largest UK residential property portal provider in terms of traffic.

Next events

Final results	April 2018

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Edison profile page

OnTheMarket is a research client of Edison Investment Research Limited

EDISON

Investment case: Building market share

Agents have a vested interest in OTM's success

The property portal market is unusual, as paying customers, ie the estate agents, also supply the inventory (the property listings) in order to attract the portals' consumer audiences. OnTheMarket was set up by estate agents themselves, acting as a mutual interest group, as an alternative route to market in reaction to a UK property market portal landscape which they felt was detrimental to their interests. Agents' Mutual created the OnTheMarket portal, offering member agents access to potential house purchasers at a significantly lower cost than the alternatives. Agents' Mutual demutualised during 2017 as part of the preparation for the listing on AIM.

OnTheMarket (OTM) is the third player in a market dominated by two other portal providers, Rightmove, which is the market leader and which has a business model predicated on maximising volume and using market dominance to increase pricing; and ZPG, owner of Zoopla and PrimeLocation, which has extended its online franchise into ancillary offers to homeowners, such as price comparison and switching services. By using these portals, estate agents lose ownership of their data, which they might otherwise use to drive other revenue streams for themselves. Until this fund-raise, OTM has not had the marketing firepower to grow its share aggressively. By using a combination of equity to sign up agency groups on long-term contracts and advantageous pricing packages for others, it should be able to build its market awareness and its revenue base. A successful venture will also ensure that estate agents guarantee a sensibly priced route to market over the longer term.

Management with relevant experience

Management is well versed in the segment, with the CEO, commercial director, brand director and the CTO all having been involved in the building of the PrimeLocation brand and overseeing its sale into DMGT (now part of ZPG). This team also set up OnTheMarket. The CFO's experience is from a broader range of commercial and financial businesses.

Recent performance affected by distractions

Recent financial performance has been hampered by the absorption of management time and the holding in escrow of funding resource during complex litigation over the nature and competitive implications of the 'one other portal' rule. This limited agents under contract to OTM to choose from either Rightmove or Zoopla, but not both, in addition to their OTM listings. While the Competition Appeal Tribunal found in the group's favour, the complainant has been granted the right of appeal to the Court of Appeal, although it is as yet unclear on what legal grounds the appeal has been lodged. The 'one other portal' rule has been withdrawn in any event for new contracts, for reasons unconnected with the litigation.

Flotation to boost marketing resource

The £30m gross being raised is to invest in sales and IT resource, expand the product offering and to fund an aggressive marketing programme to build awareness and recruit agency groups. The figure is lower than the £50m being discussed when flotation was first postulated, but should nevertheless provide a strong stimulus to propelling the market share which the group needs in order to benefit from the network effect. The financial modelling that Edison has carried out rests on three key metrics: agency branch recruitment, average listing fee per branch and marketing spend. On listing of the shares, the largest shareholder will be Schroder Investment Management, with 6.0%, followed by Jason Walker (founder of Victoria Plumb) with 3.1% and Albert E Sharp LLP with 3.0%.

Some differentiation in content

The outward-facing offer appears to the property buyer as fairly similar to those of the two market leaders, unsurprising given that the OTM website's build and design has been carried out by the same individuals who created the PrimeLocation website, with the benefit of the experience and of the technological improvements available since. However, the business case differs in that it rests on the system being designed to provide agents (the suppliers of the inventory, without which there is no content) with a fairly priced service, whilst still developing a profitable growth business and a platform for ongoing revenue development. The key distinction between OTM's outward offer is the 'new & exclusive' inventory, displayed at the top of the listings. Although this is not a contractual obligation for agents, it is in their interest to grant exclusivity to OTM before the properties are released to other portals (at higher charges). It also gives a clear incentive for seriously interested potential buyers to visit the website and to set up alerts aligned to their requirements (as opposed to much of the website traffic, which is simply taking an interest).

Fragmented client market

The estate agency market is highly fragmented and there is a clear opportunity to build a strong franchise to compete with the market incumbents, with relatively little regard of the short-term variations of the UK residential property market.

Company description: Online property portal

OnTheMarket represents the web presence of a group of UK estate agents, trading as Agents' Mutual. It was set up in January 2013 by a small group of agents to provide an alternative route to market, and a more attractive commercial proposition, to the large portal providers, in particular Rightmove and Zoopla. It was felt by the agents that these two firms were taking advantage of their strong market positioning in internet portals to their detriment as suppliers of the inventory. The original plans drawn up in March 2014 were for the portal to carry the content from 1,500 branches, rising to 6,500 by the end of year five of the business plan. When OnTheMarket launched in January 2015, it had 4,600 branches, which had risen to 6,000 two years later.

The Agents' Mutual proposition was for a portal that was controlled by agents themselves and that would provide an enhanced user experience to consumers searching for property while charging fair prices to agents. This concept was generally well received, particularly by a broad segment of leading UK independent and group agents, which funded the venture through loan note subscriptions and committed to listing properties with the portal once it went live on five-year contracts. These loan notes converted to equity on flotation, leaving the group in a pro-forma net cash position. There is no sell down by existing shareholders. Post listing, there will be a free float of 41%, of which agent shareholders will hold 11%. The prospectus indicates that, on admission, agents will own more than 70% of the enlarged share capital.

Fees are paid by agency branch, rather than by number of listings (with online and hybrid agencies working with a 'branch equivalent' definition, based on the relative number of listings). Agencies often commit to long-term (five year) contracts, meaning a good level of recurring income (although the absolute proportion is not yet calculable). As part of the reorganisation, member agencies were given the opportunity to enter into new five-year contracts, underpinning future revenue streams and facilitating the next stage of growth. As at the date of the publication of the prospectus, 3,039 branches had signed new five-year contracts, 1,253 were on earlier contracts with more than two years left to run, with the remaining 1,208 on shorter-term rolling contracts.

All to play for

The IPO is intended to provide the opportunity for a transformational step-change in the portal's position and for development of new consumer and agent products and services, new segments of the property market and new strategic partnerships. The reasons for the flotation are 1) to raise £30m gross (£27m net) of new funds to scale up the group; 2) to facilitate the use of equity to encourage agents to join and increase levels of inventory, in turn driving traffic; and 3) to raise the portal's profile with the house-buying public, both of which should help to gain market share against the two market majors. The proceeds are also intended to be invested in increasing sales/account management resource and to expand the technological capabilities in platform and product development.

After two years of full operation, OnTheMarket (OTM) had become the third-largest UK property portal provider, after Rightmove (the clear market leader) and ZPG. The portal's market penetration varies nationally, reflecting the geographic distribution of its founding members. A snapshot of comparative numbers of listings in various locations and property types is shown in Exhibit 1 below.

The business models of OTM, Rightmove and ZPG obviously overlap and they all operate portals that enable estate agents to publish their inventory to a broad, online audience. Although we would not normally discuss competitor business models in our reports, in this instance an understanding of the market dynamics is essential to a proper review of OTM's positioning and potential.

Exhibit 1: Comparative inventory listed

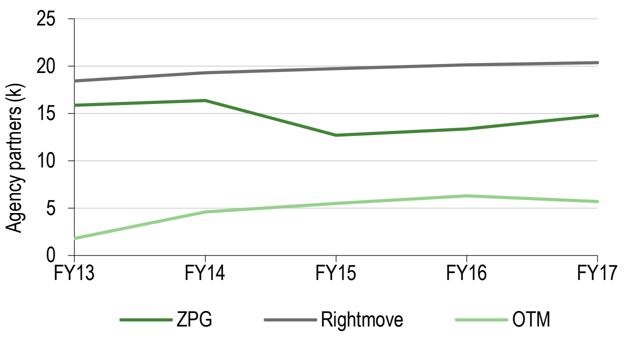
Property type	Location	Portal	No. of listings	OTM % of mkt leader
5+-bed house (to buy)	Suffolk	Rightmove	130	
		Zoopla	66	
		OTM	32	25%
1-bed flat (to rent)	London N8	Rightmove	89	
		Zoopla	112	
		OTM	23	21%
2-bed flat (to buy)	Southampton	Rightmove	295	
		Zoopla	224	
		OTM	49	17%
3-bed house (to buy)	Swansea	Rightmove	221	
		Zoopla	515	
		OTM	296	57%
2-bed flat (to rent)	Birmingham	Rightmove	948	
		Zoopla	635	
		OTM	99	10%

Source: Companies' websites as at 26 January 2018

Rightmove is a pure play portal business, which has successfully grown its agency base to 17,589 (20,358 including new home developers) at the time of its interims to end June 2017. Its market dominance has enabled it to move its ARPA ahead strongly – the CAGR over the last seven years is 18% and the last published number was £911 for H117 (up 10% from £830 in H116). **ZPG** is the holding company for assets including Zoopla and PrimeLocation. Over the years it has expanded its portfolio to include other comparison websites and consumer services of interest to householders, notably uSwitch. Property accounted for 48% of revenues in its financial year to November 2017, of which two-thirds related to property marketing, with the balance split between software and data services provided to participants in the property market. ZPG generates a lower ARPA than Rightmove in order to attract the inventory that will in turn attract the web traffic and generate leads across the service offer. This gives it a somewhat different relationship with the agency partners and it was from ZPG that OTM attracted most of its early agency partners when the 'one other portal' rule was imposed (see section below). At its recent AGM, ZPG stated that it has "signed multiple new long-term portal listing and data services agreements with some of the UK's largest estate agents and mortgage lenders" since its September year-end. ZPG's ARPA was £359 in FY17, up 3% from the prior year.

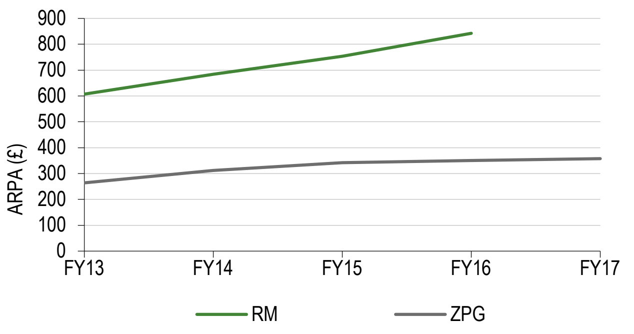
Listing property on Rightmove or ZPG portals allows those providers to take ownership of the data generated, giving a further commercial advantage to the arguments for using OTM.

Exhibit 2: Agency partners of three main UK portals



Source: Companies' accounts, presentations

Exhibit 3: Recent growth in portal ARPA



Source: Companies' presentations

Purplebricks is a hybrid estate agent, as opposed to a portal, so is not directly comparable in terms of business model. Online estate agents and hybrid agents (that use a combination of online operation and local offices, but often covering very large areas) are actual or potential customers rather than competitors.

Exhibit 4: Estate agency groups

OTM group partner agencies	Branch numbers	Rest of market	Branch numbers
Hunters (announced as on listing)	**211**	Countrywide	921
SpicerHaart Group	192	Connells	600
Savills	135	LSL	520
Arun (announced as on listing)	**112**	The Property Franchise Group	206
Knight Frank	78	Leaders/Romans	147
Winkworth	74	Belvoir	175
Strutt & Parker	64	Dexters	82
Kinleigh Folkard & Hayward	59	Andrews	67
The Property Franchise Group	56	Foxtons	67
Chancellors (announced as on listing)	**52**	Bradleys	32
Jackson-Stops	46	Pattinson	30
Acorn	42	Townends/Regents	28
Nottingham Estate Agency	38		
Chestertons	37		
Carter Jonas	36		
Humberts	27		
Dacre, Son & Hartley	25		
Goadsby	25		
Subtotal	**1,309**	**Subtotal**	**2,875**
Other firms	**c 4,562**	**Other Firms**	**9,500**
Estimated total number of agency branches in UK = 18,246			

Source: Company

Exhibit 4 above shows the distribution of estate agency groups and also shows how fragmented the overall UK property market remains. A substantial number of the branches being targeted are either entirely independent or operating in groups of three or fewer, with only 4% in organisations of over 125 branches.

The recruitment of agents will also vary by region, but the priority will be given to targeting high stock branches in areas that are already the strongest for the group, leveraging the existing brand awareness. The sales team is being increased by about four-fold post-flotation to around 60 people, with central organisation for analysis of targeting and organisation of appointments.

Adding to the offering

The property listings service offered by OTM is currently not significantly different from those of Rightmove and Zoopla ie the ability to search by region, postcode, number of bedrooms etc. They also all offer participating agents broadly similar reporting tools, which is unsurprising given that the OTM platform was built by the same people who built the PrimeLocation platform.

The ‘new & exclusive’ listings, which appear at the top of the search results grid, are valuable in driving traffic from high quality leads – benefiting from the ‘fear of missing out’. While this is not a contractual obligation, it is to the advantage of participating agents and many keep properties in this category for longer than the typical 24 to 48 hours before releasing to other portals. Around 20% of all listings on OTM first appear on the website in this form.

OTM intends to add comparables and valuation reports in the current financial year and has identified revenue opportunities in additional branding products and valuation-lead products. Given the mutual benefit between a strong performance by OTM and by its participating agents, there is potential to develop market intelligence reports through sharing of data that might otherwise be closely guarded. Other support services may also be developed.

Up to this point, OTM has not carried listings of new properties being marketed directly by property developers. This is an obvious contiguous extension of its offer that can be added easily, subject to suitable agreements being struck with the developers.

Longer term, it may be appropriate to extend to commercial property and some categories of overseas real estate.

Media strategy

The flotation of the group will inevitably increase its visibility in the market – both with partner agencies and with the property-buying public, which in turn should generate increased levels of inventory and therefore traffic to the web portal. However, throwing ‘marketing muscle’ behind the effort should make the impact more robust and encourage vacillating agents and agency groups that their objectives will be best served by joining. The removal of the ‘one other portal’ rule also removes a key obstacle to stepping up recruitment.

Management has outlined its media strategy within the supporting material. The intention is to spend up to £25m in each of year one and year two in order to maximise the impact, dropping to approximately £20m the year after. We have incorporated these figures into our modelling.

There are three elements in the mix (rough split of anticipated spend given in brackets); digital (50%); national campaigns (25%); and local campaigns (25%).

- Digital spend will focus on strengthening the paid search/SEO, as well as adding to expertise in social. The primary objective is to drive traffic on the portal and increase visitor engagement, in order to drive high quality leads back to the participating agents. The secondary objective is to increase broader brand awareness, which should in turn help to attract new property advertisers and support the existing client base.
- Building brand awareness is the primary objective of the intended national campaigns, which, again, should bring greater credibility and attract further agency partners. They should also drive traffic and leads.
- With each local property market having different players, levels of competition and influencing factors, a more targeted geographic campaign can be very effective in building brand awareness, with the same subsidiary benefits.

Individual participating agencies are required to display OTM marketing materials in their marketing collateral, in window displays, in branch and on their websites. In addition, some go much further on a voluntary basis by carrying the logo on car wraps and/or on sale boards.

‘One other portal’ rule modified

In order to build share in a competitive market with larger incumbent players, agents joining OTM committed to list with OTM and a maximum of one other competing portal – effectively a choice between Rightmove and Zoopla. This rule was challenged by an agent, Gascoigne Halman, on the grounds that it limited competition in the market. The Competition Appeal Tribunal (CAT) examined the issue closely and issued a comprehensive judgment in July 2017. The crux of the judgement was that, given the effective duopoly in the existing market, the arrangement was actually likely to lead to an improvement in the competitive landscape rather than being a restriction. Gascoigne Halman applied for leave to appeal on competition issues but this was turned down by the CAT in October 2017, whereupon they applied for leave to appeal the judgement in the Court of Appeal (which must be on grounds of point of law). The pursuit of this case occupied a considerable amount of management time, as well as the potential costs overhanging the allocation of capital to growth plans. In August 2017, the CAT returned £1.83m of court deposits to OTM, of which around £1m was spent on marketing soon after.

With the group now raising additional funds to accelerate the agent recruitment programme, the restriction is being rescinded. New contracts that have been negotiated no longer contain this stipulation. Hybrid and online agents are now also able to participate, as well as developers of newbuilds. As the relative competitive positions play out, it may be that branches choose to limit their portal partners to two anyway on economic grounds.

Management team with extensive sectoral experience

CEO Ian Springett founded PrimeLocation in 2000 and managed its sale to DMGT in 2005 for £48m. He remained with the business until 2008 when he left to pursue other interests. He joined the Agents’ Mutual venture at the start of 2013. Previously, Ian was managing director of Lombard Bank following a number of senior roles within NatWest Group.

Commercial director Helen Whiteley joined Agents’ Mutual in August 2013, having previously been sales & marketing director and part of the founding management team at PrimeLocation. Before that, Helen was marketing director at Lombard Bank, having previously worked at Citibank.

CTO Morgan Ross was originally hired at PrimeLocation (working for an outsourced company) as technical director in 2002, being brought in-house as technical director the following year, and finishing as group IT director at The Digital Property Group (2008). In 2009, he joined James Villas as IT director, where he stayed for four years before moving to be global CTO at World Trade Organisation. Morgan joined his former colleagues, Ian Springett and Helen Whiteley, at OTM in November 2013. He is responsible for portal development and operations, as well as for the technical support team.

Brand director John Milsom was also part of the PrimeLocation and OTM-founding team, joining OTM in February 2014. He previously ran his own marcomms business, as well as working for larger advertising agency groups.

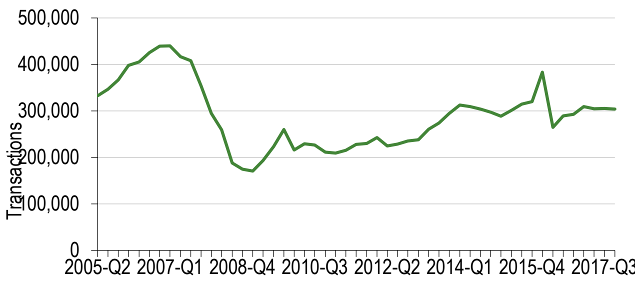
CFO Clive Beattie joined OTM in March 2017 to help shape the forward strategy and prepare the company for its IPO. He was previously CEO and CFO of both Croft Associates (a developer of packaging, storage and transportation solutions for radioactive waste) and ThruVision (a manufacturer of security screening products). Clive is ACA qualified and spent over 12 years at UBS Investment Bank following three years at PricewaterhouseCoopers.

The two independent directors are chairman Chris Bell and NED and audit chair, Ian Francis. Chris was CEO of Ladbrokes, a director of Hilton and had senior roles at Allied Lyons. Since 2015, he has been senior independent director at The Rank Group. His non-executive roles have included the chairs of XLMedia and TechFinancials, both successfully listed on AIM, alongside various other senior independent director and NED appointments. Ian is an accountant, having spent most of his career in various roles at Ernst & Young. He is an NED and audit chair at Paysafe Group and performed the same role at Umeme.

Shifting market models on subdued backdrop

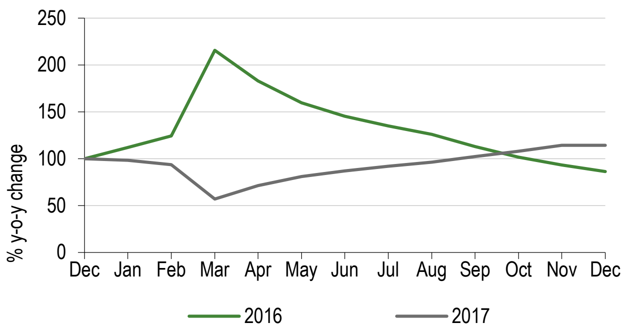
Transaction levels flattened out

Exhibit 5: Long-term UK housing transactions (seasonally adjusted)



Source: HMRC

Exhibit 6: Short-term transaction volume change in UK residential market



Source: HMRC

There has been much written regarding the health of the UK housing market and, in particular, levels of affordability. The longer-term and more recent patterns of trading volumes are shown in the Exhibits above.

The number of market transactions does not have a direct impact on OTM's financial performance, its income being a reflection of the number of member/participating agencies, rather than the number of listings that they carry or their success in driving website views to completed transactions. However, it does have an indirect impact – particularly if the stagnation is sustained. As demonstrated above, the market is highly fragmented at a national level but can also be fiercely competitive at a local level. Having an effective and efficient funnel to deliver high-quality leads should prove a competitive advantage. It is even possible that a difficult underlying market may represent a more conducive environment for growing the OTM market reach.

Sensitivities

Our financial modelling makes key assumptions regarding the level of marketing spend and the success in growing the branch agency network. Varying any of these metrics would clearly affect our earnings and balance sheet projections. Given the competitive nature of the market, pricing strategies of one of the main portal operators will have repercussions for other players in the market, including OTM. Our model assumes an initial reduction in ARPA as branch agencies are recruited to the platform in FY19, with growth from the following year moving towards the current level charged by ZPG. This growth in forecast ARPA will be allied with offering additional functionality to participating agents, particularly through the intelligent use of data.

We have also made certain assumptions regarding the success of the marketing spend in recruiting new agencies and agency networks to the OTM portal, which may or may not be reasonable.

Because of the plethora and complexity of possible outcomes, we have also made the assumption that new agency partners are attracted by discounted or lower portal listing fees. In reality, there is likely to be equity issued to some, or possibly many, new partners. The important balance will be between the inherent dilution from additional shares versus the benefit to operating profit from the additional volume/ revenue.

We have also included the growth in 'Other' revenues within our modelling, comprising add-on products for agents, revenues from advertising new homes from property developers and third-party advertising on the website attracted by increasing levels of traffic.

Outside of the sensitivities from our modelling assumptions, there are a number of internal and external potential factors that may affect the financial performance and the share price. The former would include:

- Litigation. While the Competition Appeal Tribunal ruled that the 'one other portal' rule was not anti-competitive, Gascoigne Halman was granted leave to appeal the ruling at the Court of Appeal on 20 December 2017. A date has yet to be set for the hearing. There are also outstanding claims for breach of contract against Gascoigne Halman (again, with no date set as yet). The conduct of legal cases of this type are invariably heavily time consuming for management and potentially expensive. This intensive phase is now complete. It remains possible that other agents pursue claims against OTM, but there has been no recent correspondence in this respect.
- The business model is crucially dependent on its IT systems and on its data security, failures of which also would have repercussions for the integrity of the brand. There has been zero downtime on the platform over the year to January 2018.
- Not all participating agents have entered into lock-in arrangements over their shares as part of renegotiated contracts. Around 6m shares are not covered by the general principles established in these agreements. The lock-up states that 10% of shares can only be sold on or after the first anniversary from admission, 10% on the second anniversary, and the balance following the fifth anniversary.

External factors could relate to:

- Economic, such as housing affordability and its impact on transactions;
- Geopolitical influences that may affect buyer confidence – these may be more pertinent in certain parts of the country;
- Regulatory environment ie money laundering, restrictions on certain types of letting fees, stamp duty etc; or
- Disruption to the residential property market be it through innovation such as applications of blockchain, or further technical innovation or disintermediation.

Valuation

Peer comparison context

Given the early stage of the group's development, traditional valuation metrics are not especially useful. With the scale of the planned increase in investment in personnel, IT and marketing spend, OTM will generate substantial losses at the EBITDA level over the next couple of years as the investment goes through. This effectively leaves the only income-based valuation metric it the EV/sales ratio, where OTM sits at a considerable discount to the more established players, as would be expected. OTM at flotation price is valued at an historic EV/sales ratio (based on our estimate of revenues to January 2018) of 4.4x, compared with 16.9x for Rightmove and 6.6x for ZPG. Looking at the broader global context (which, like ZPG, includes some peers with more diverse business models), the sector is trading on average multiples of 10.4x EV/sales and 21.1x EV/EBITDA.

Exhibit 7: Comparative valuations for property listing and portal stocks

Name	Price (reporting currency)	Market cap (m)	EV/sales FY1 (x)	EV/sales FY2 (x)	EV/EBITDA FY1 (x)	EV/EBITDA FY2 (x)	EV/EBIT FY1 (x)	EV/EBIT FY2 (x)	P/E FY1 (x)	P/E FY2 (x)	Div yield FY1 (x)
Rightmove (p)	43.05	3,927	16.1	14.7	21.2	19.4	21.5	19.6	27.1	24.2	1.1
ZPG (p)	3.24	1,421	5.2	4.8	13.8	12.1	16.9	14.5	18.6	16.2	2.1
Purplebricks Group (p)	4.16	1,136	10.8	5.9							0.0
Zillow Group Inc – C (US$)	43.51	8,236	7.4	6.1	33.6	24.9	62.5	47.5	83.2	50.5	0.0
REA Group Ltd (AU$)	71.17	9,374	11.8	10.4	20.8	17.9	22.9	19.5	32.6	27.4	1.6
Axel Springer SE (€)	69.40	7,493	2.6	2.6	14.1	12.4	20.3	18.8	26.8	23.6	2.8
Scout24 AG (€)	36.04	3,880	9.3	8.5	18.2	16.0	21.9	18.7	27.3	23.4	1.1
LEG Immobilien AG (€)	84.58	5,353	11.7	12.1	25.3	23.4	26.1	24.4	16.8	16.7	3.6
Domain Hdgs Australia (AU$)	3.03	1,742	5.3	4.7	16.6	14.1	22.0	17.7	34.4	27.1	1.5
Trade Me Group Ltd (NZ$)	4.40	1,748	7.3	6.8	11.2	10.5	13.3	12.6	18.0	16.9	4.4
Average			**8.7**	**7.7**	**19.4**	**16.8**	**25.3**	**21.5**	**31.6**	**25.1**	**1.8**
OnTheMarket	1.65	100	3.9	2.0	-3.6	-6.6	-3.3	-5.6	-4.7	-9.9	0.0

Source: Bloomberg, Edison Investment Research. Note: prices as at 7 February 2018. Average EV/EBIT excludes Purplebricks

While it is possible to extrapolate further and make comparisons once OTM has moved into profitability (which we estimate to happen in FY21), the degree of flex in the forecast assumptions would make any derived valuation unreliable.

We have also looked at the narrower UK market in terms of the value that the stock market accords to market reach, for which the proxy is the number of agency partners (note that this calculation is done on ZPG's number of agency partners, as opposed to its number of property partners). The discrepancy in the EVs is obviously substantial and it would be unwise to assume that OTM's EV/agency partner ratio would converge towards the others in the short term. However, the direction of travel should be clear. Even if the EV/agency partner were not to change, our modelled increase in the average number of agency partners to 8,500 and 14,750 for FY19 and FY20 respectively (NB year-end is January) works back mechanistically to a theoretical future share price of 224p and 351p respectively.

Exhibit 8: EV/market reach

	Price (p)	Mkt cap (£m)	EV (£m)	EV/sales (x)	ARPA (£)	Avg agency partners	EV/agency partner
RIGHTMOVE PLC	4305	3,927	3,905	16.9	842	20,358	£191,816
ZPG PLC	324	1,421	1,613	7.0	358	14,775	£109,171
OTM PLC	165	100	70.8	4.4	234	5,700	£12,421

Source: Bloomberg, Company reports, Edison Investment Research. Note: Prices as at 7 February 2018.

Cash flow-based valuation

Exhibit 9: Free cash flow record and forecasts

	FY15	FY16	FY17	FY18e	FY19e	FY20e	FY21e	FY22e	FY23e	FY24e	FY25e	FY26e	FY27e
Net revenue	**1,983**	**17,851**	**17,831**	**16,000**	**18,000**	**35,000**	**63,600**	**77,000**	**89,373**	**99,266**	**105,291**	**108,749**	**109,293**
Net sales revenue y-o-y growth (%)	na	800.2%	-0.1%	-10.3%	12.5%	94.4%	81.7%	21.1%	16.1%	11.1%	6.1%	3.3%	0.5%
Earnings Before Interest and Taxes (EBIT)	-2,522	-1,729	-1,182	1,500	-24,400	-12,750	16,100	28,140	31,768	34,292	35,320	35,393	34,477
EBIT margin (%)	-127%	-9.7%	-6.6%	9.4%	-136%	-36.4%	25.3%	36.5%	35.5%	34.5%	33.5%	32.5%	31.5%
Depreciation & amortisation	19	589	968	1,513	1,773	1,981	2,298	2,504	2,906	3,228	3,424	3,536	3,554
as a % of sales (%)	1.0%	3.3%	5.4%	9.5%	9.9%	5.7%	3.6%	3.3%	3.3%	3.3%	3.3%	3.3%	3.3%
Tax paid on EBIT	0	0	0	0	0	2,550	-3,220	-5,628	-6,354	-6,858	-7,064	-7,079	-6,895
Tax rate (%)	0.0%	0.0%	0.0%	0.0%	0.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%
Gross cash flow	**-2,503**	**-1,140**	**-214**	**3,013**	**-22,627**	**-8,219**	**15,178**	**25,016**	**28,321**	**30,661**	**31,680**	**31,850**	**31,135**
Decr/(incr) in net working cap	-1,309	3,509	-42	500	534	-1,263	-681	246	251	201	122	70	11
Net working capital	1,240	-2,269	-2,228	-2,728	-3,262	-1,999	-1,318	-1,563	-1,815	-2,015	-2,138	-2,208	-2,219
as a % of sales (%)	62.5%	-12.7%	-12.5%	-17.0%	-18.1%	-5.7%	-2.1%	-2.0%	-2.0%	-2.0%	-2.0%	-2.0%	-2.0%
Net capital expenditure	-1,543	-2,008	-1,623	-1,493	-2,180	-2,350	-2,636	-2,770	-3,153	-3,434	-3,569	-3,611	-3,554
as a % of sales (%)	77.8%	11.2%	9.1%	9.3%	12.1%	6.7%	4.1%	3.6%	3.5%	3.5%	3.4%	3.3%	3.3%
Change in other op. assets	655	1,394	1,352	763	0	0	0	0	0	0	0	0	0
Free cash flows	**-4,700**	**1,755**	**-527**	**2,783**	**-24,273**	**-11,832**	**11,861**	**22,492**	**25,418**	**27,428**	**28,233**	**28,309**	**27,592**

Source: Company accounts, Edison Investment Research

Given the problems inherent with earnings-based methodologies expressed above, we have also looked at valuation based on discounted cash flow. Again, this is highly dependent on the modelling, particularly with respect to the marketing spend and the return earned on it in terms of agency recruitment.

Exhibit 10: NPV calculation

Asset valuation	
Present value of forecast cash flows (2018-2027)	58,727
Present value of forecast cash flows (2028-perpetuity)	107,461
less cash	-29,182
Total valuation	195,370
NPV/share (as at 4 February 2018)	**323p**
Current share price	165p
Upside/(downside) to NPV/share	95.8%

Source: Edison Investment Research

Under our modelled scenario, with the business moving into profit from FY21, the free cash flows become substantial from that year on. We have assumed a small amount of debt is taken on during FY20e to over the funding gap before the cash flows turn positive again. Based on a WACC of 10.2% and a long-term growth rate of 0.5%, the NPV of the cash flows equates to a share price of 323p, 95.8% ahead of the issue price. A 323p share price would give an EV of £166.3m and an FY18 EV/sales multiple of 10.4x and an EV/agency partner figure of £29k. This is obviously not adjusted for any implementation risk (although it should be noted that there is also sensitivity on the upside). Setting this adjustment at 30% would indicate a share price of 226p, a 37% premium to the issue price of 165p.

We have also looked at the sensitivity of the DCF to changes to the key drivers under three alternative scenarios:

1) Marketing spend is lower at £20m in year one and in year two and at £15m in year three, but with no alteration to the number of agencies recruited or ARPA. This would increase the NPV of the cash flows to 388p.
2) ARPA grows at a slower pace, from £170 in FY19 (unchanged), to £200 in FY20, £250 in FY21 and £275 in FY22. This delivers an NPV of 290p.
3) 25% fewer branches are recruited than our core model, but other metrics are unchanged. This produces a value of 293p.

These values are all without any further adjustment for execution risk.

Financials

Earnings growth hinges on partner recruitment...

The revenues of OTM simply consist of the listing fees paid by agency partners, with other sources of income (principally listing fees of new properties) starting to build over time. These are the key drivers of our revenue model, as shown below. Revenues in the year just ended (yet to be reported) will be down on the prior year, reflecting the disruption to the business with regards to a) the demutualisation; b) the negotiations of new contracts with existing agencies; c) the absorption of management time in dealing with the litigation; and d) lack of funds / resources.

We have assumed that the number of partner agencies will now rebuild and exceed previous levels, with the first step up already established with the recruitment of three agency groups (highlighted in Exhibit 3, above) contingent on the listing of OTM shares. Between them, they bring an additional 375 agency branches to the group. It should be noted that the estate agency market remains highly fragmented and that there are a limited number of sizeable groups to target, again shown in this exhibit. Once recruited, this income stream is attractive, with high levels of recurring revenues over predominantly five-year listing agreements.

The successes in drawing agencies onto the OTM platform will depend on both the attractiveness of the equity participation (which will help with the 'stickiness' of the business brought in) and the return on the deployment of the marketing spend. To date, OTM has spent just under £20m, split 38% on TV and press campaigns, 61% on paid search and digital advertising, with the small balance on local press, radio and posters. Management intends to spend up to £25m in each of the first two years to support the 'land grab', reducing thereafter to approximately £20m in year three. We have used these figures in our modelling.

...then moving ARPA ahead

Exhibit 11: Revenue and EBIT drivers

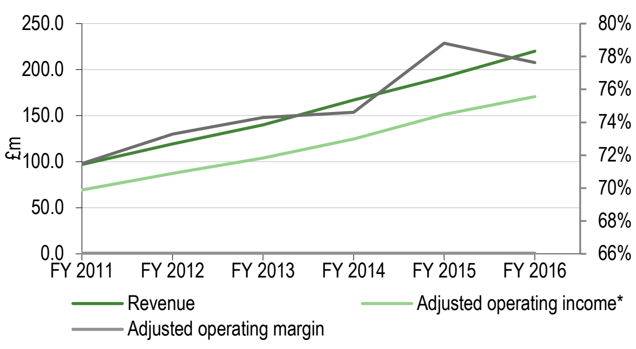
	FY2015A	FY2016A	FY2017A	FY2018F	FY2019F	FY2020F	FY2021F	FY2022F
Revenue (£'000s)	**1,983**	**17,851**	**17,831**	**16,000**	**18,000**	**35,000**	**63,600**	**77,000**
EBIT (£'000s)	**-2,522**	**-1,729**	**-1,182**	**1,500**	**-24,400**	**-12,750**	**16,100**	**28,140**
Revenue Drivers								
Revenue from listing fees (£'000s)	1983	17,851	17,831	16,000	18,000	33,300	59,600	62,000
Average number of branches	na	5,516	6,306	5,700	8,500	14,750	17,500	17,500
Net additions to branches			790	-606	2,800	6,250	2,750	0
Average listing fee per branch (£/mth)	na	270	236	234	176	188	284	295
Y-O-Y Growth (%)	na	na	-12.6%	-0.7%	-24.6%	6.6%	50.9%	4.0%
Other Income (£'000s)	0	0	0	0	0	1,700	4,000	15,000
Total Revenue (£'000s)	1,983	17,851	17,831	16,000	18,000	35,000	63,600	77,000
Overall ARPA (£/mth)	na	270	236	234	176	198	303	367
EBIT Drivers								
Staff Cost (£'000s)	-2,097	-4125	-4,353	-3,500	-9,000	-14,000	-17,961	-18,859
as a % of sales	105.7%	23.1%	24.4%	21.9%	50.0%	40.0%	28.2%	24.5%
Non-Staff Overhead (ex-Exceptional Costs) (£'000s)	-1,019	-2955	-4,154	-6,500	-8,000	-8,750	-9,539	-10,001
as a % of sales	51.4%	16.6%	23.3%	40.6%	44.4%	25.0%	15.0%	13.0%
EBIT before Marketing costs (£'000s)	-1,133	10,771	9,324	6,000	1,000	12,250	36,100	48,140
Marketing Costs (£'000s)	-1,389	-12500	-7,000	-2,500	-22,500	-24,999	-20,000	-20,000
as a % of sales	70.0%	70.0%	39.3%	15.6%	125.0%	71.4%	31.4%	26.0%
EBIT before exceptional items (£'000s)	-2,522	-1,729	2,324	3,500	-21,500	-12,750	16,100	28,140
Exceptional Items (£'000s)	0	0	-3,506	-2,000	-2,900	0	0	0
EBIT after exceptional items (£'000s)	-2,522	-1,729	-1,182	1,500	-24,400	-12,750	16,100	28,140
EBIT Margin (%)	**-127.2%**	**-9.7%**	**-6.6%**	**9.4%**	**-135.6%**	**-36.4%**	**25.3%**	**36.5%**

Source: Company accounts, Edison Investment Research

The business model is still at an early stage of development and there is little to be sensibly gleaned from the financial record to date. There was obviously rapid growth during FY16 when the first agency networks came together, followed by year of consolidation. The plan had been to continue to scale up and float the business. The process of demutualisation was a lengthy and intricate process as the participants' interests were not necessarily fully aligned. This, and the litigation described above, both absorbed a deal of resource (time and money) that would otherwise have been focused in developing and growing the business. Marketing costs were reined in and the group has fallen behind its initially planned itinerary.

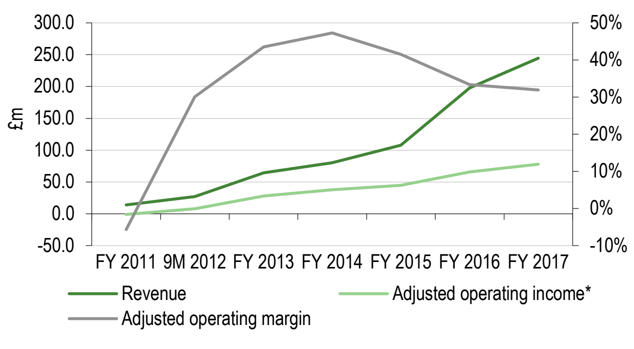
We show the revenue and operating margin history of Rightmove and ZPG to put our margin assumptions into context in the Exhibits below.

Exhibit 11: Rightmove revenue and margin history



Source: Company accounts. Note: adjusted for exceptionals, SBP.

Exhibit 12: ZPG revenue and margin history



Source: Company accounts. Note: adjusted for exceptionals, SBP.

Scaling up inevitably means additional resource and around a quarter of the flotation proceeds are to be targeted at scaling up the infrastructure, adding to the IT development and to the sales teams. Despite the higher levels of both staff costs and non-staff overhead, our model shows the business remaining EBIT positive pre-marketing costs even in FY19, where the scaling up is likely to be greatest. This investment will enable the group to build a valuable data resource which can be used to benefit both OTM and its clients, the agencies. The level and sophistication of data usage currently should be considerably enhanced, building data products of benefit to partner agencies (so driving up the ARPA by delivering greater value) and through the introduction of relevant third-party targeted advertising to the portal.

Our modelling indicates OTM moving into profit at the pre-tax level during FY21 (beyond our published forecast horizon).

Cash flow investment phase

Our cash flow modelling is shown in Exhibit 9, above. The group could choose to conserve cash by reining in the marketing spend, but this may compromise the forecast growth profile and the conversion of agents on to paying (or higher paying) contracts. On the basis shown here, OTM turns cash flow positive at both the gross and net cash level in FY21. At their last reported results, ZPG showed operating profit to cash conversion of 88% and Rightmove 101%. As OTM matures, there should be no structural reason why it should not achieve similar levels – although we have modelled a more conservative 80% in the medium term.

Balance sheet strength depends on structure of deals, spend

The £30m gross placing proceeds on flotation are below the level that market commentary indicated during the demutualisation phase in summer 2017 (reported to be £50m). We understand from management that the lower raise did not have a fundamental impact on the business plans as a £50m raise had significant headroom to deliver the strategy. OTM has to date been funded by its founding agencies in the form of loan notes, with coupons of between 7% and 15% and, most significantly, by revenues from agents' listing fees.

The loan notes have been redeemed and converted to equity on the float.

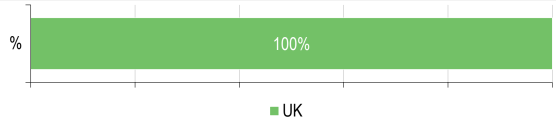
The Edison model assumes that the funding, together with ongoing revenues from agents' listing fees, is sufficient to cover the additional spending plans through FY19, with the assumption of a modest amount of debt by end FY20, before moving back into a net cash position the following year. The timing and outturn could obviously vary considerably from this scenario.

Exhibit 13: Financial summary

£'k	2015	2016	2017	2018e	2019e	2020e
31-January	IFRS	IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT						
Revenue	1,983	17,851	17,831	16,000	18,000	35,000
EBITDA	(2,503)	(1,140)	3,292	5,013	(19,727)	(10,769)
Normalised operating profit	(2,522)	(1,729)	2,324	3,500	(21,500)	(12,750)
Amortisation of acquired intangibles	0	0	0	0	0	0
Exceptionals	0	0	(3,506)	(2,000)	(2,900)	0
Share-based payments	0	0	0	0	0	0
Reported operating profit	(2,522)	(1,729)	(1,182)	1,500	(24,400)	(12,750)
Net Interest	(655)	(1,394)	(1,351)	(1,300)	146	123
Joint ventures & associates (post tax)	0	0	0	0	0	0
Exceptionals	0	0	0	0	0	0
Profit Before Tax (norm)	(3,177)	(3,123)	973	2,200	(21,354)	(12,627)
Profit Before Tax (reported)	(3,177)	(3,123)	(2,533)	200	(24,254)	(12,627)
Reported tax	0	0	0	0	0	2,525
Profit After Tax (norm)	(3,177)	(3,123)	973	2,200	(21,354)	(10,102)
Profit After Tax (reported)	(3,177)	(3,123)	(2,533)	200	(24,254)	(10,102)
Minority interests	0	0	0	0	0	0
Discontinued operations	0	0	0	0	0	0
Net income (normalised)	(3,177)	(3,123)	973	2,200	(21,354)	(10,102)
Net income (reported)	(3,177)	(3,123)	(2,533)	200	(24,254)	(10,102)
Basic average number of shares outstanding (m)	36	36	36	36	61	61
EPS - normalised (p)	(8.9)	(8.8)	2.7	6.2	(35.3)	(16.7)
EPS - normalised fully diluted (p)	(8.9)	(8.8)	2.7	6.2	(35.3)	(16.7)
EPS - basic reported (p)	(8.9)	(8.8)	(7.1)	0.6	(40.1)	(16.7)
Dividend (p)	0.0	0.0	0.0	0.0	0.0	0.0
Revenue growth (%)	N/A	899.2	98.9	88.7	111.5	193.4
EBITDA Margin (%)	-126.2	-6.4	18.5	31.3	-109.6	-30.8
Normalised Operating Margin	-127.2	-9.7	13.0	21.9	-119.4	-36.4
BALANCE SHEET						
Fixed Assets	1,527	2,946	3,601	3,581	3,988	4,357
Intangible Assets	1,449	2,874	3,556	3,483	3,787	3,964
Tangible Assets	78	72	45	98	200	393
Investments & other	0	0	0	0	0	0
Current Assets	5,356	4,200	5,972	3,770	8,503	5,998
Stocks	0	0	0	0	0	0
Debtors	3,320	638	3,709	1,419	1,578	3,998
Cash & cash equivalents	2,036	3,562	2,263	2,351	6,925	2,000
Other	0	0	0	0	0	0
Current Liabilities	(3,087)	(3,872)	(7,316)	(4,895)	(5,588)	(6,744)
Creditors	(2,080)	(2,907)	(5,937)	(4,147)	(4,840)	(5,996)
Tax and social security	0	0	0	0	0	0
Short term borrowings	(1,007)	(965)	(1,379)	(748)	(748)	(748)
Other	0	0	0	0	0	0
Long Term Liabilities	(7,139)	(9,740)	(11,256)	(11,256)	(1)	(6,810)
Long term borrowings	(7,139)	(9,740)	(11,256)	(11,256)	(1)	(6,810)
Other long term liabilities	0	0	0	0	0	0
Net Assets	(3,343)	(6,466)	(8,999)	(8,799)	6,902	(3,200)
Minority interests	0	0	0	0	0	0
Shareholders' equity	(3,343)	(6,466)	(8,999)	(8,799)	6,902	(3,200)
CASH FLOW						
Op Cash Flow before WC and tax	(2,503)	(1,140)	3,292	5,013	(19,727)	(10,769)
Working capital	(1,309)	3,509	(42)	500	534	(1,263)
Exceptional & other	0	0	(3,506)	(2,000)	(2,900)	0
Tax	0	0	0	0	0	2,525
Net operating cash flow	(3,812)	2,369	(256)	3,512	(22,093)	(9,507)
Capex	(1,543)	(2,008)	(1,623)	(1,493)	(2,180)	(2,350)
Acquisitions/disposals	0	0	0	0	0	0
Net interest	(86)	(998)	(937)	(1,394)	(1,154)	123
Equity financing	0	0	0	0	41,255	0
Dividends	0	0	0	0	0	0
Other	0	0	0	0	0	0
Net Cash Flow	(5,441)	(637)	(2,816)	626	15,828	(11,734)
Opening net (cash)/debt	273	5,714	6,747	9,976	9,423	(6,406)
FX	0	0	0	0	0	0
Other non-cash movements	0	(396)	(413)	(72)	(0)	0
Closing net (cash)/debt	5,714	6,747	9,976	9,423	(6,406)	5,328

Source: Company accounts, Edison Investment Research

EDISON

Contact details	Revenue by geography
PO Box 450 155-157 High Street Aldershot GU11 9FZ UK Phone: Website: www.onthemarket.com	

Management team

Non-Executive Chairman: Christopher Bell	CEO: Ian Springett
Chris Bell was Ladbrokes' CEO for nine years before leaving in 2010 and has over 20 years' experience in the gaming industry. He joined Ladbrokes in 1991, becoming MD in 1994 and joining the Hilton board in 2000. Chris is independent non-exec chair of XLMedia and TechFinancials, both of which listed on AIM. He is also SID at the Rank Group, and was previously SID at Quintain Estates and NED at Spirit Pub Company.	Ian founded PrimeLocation in 2000 and managed its sale to DMGT in 2005 for £48m. He remained with the business until 2008 when he left to pursue other interests. He became involved with Agents' Mutual venture in 2012, joining the group as CEO in April 2013. Previously, Ian was managing director of Lombard Bank following a number of senior roles within NatWest Group.
CFO: Clive Beattie	**Commercial Director: Helen Whiteley**
Clive joined OTM in March 2017 to help shape the forward strategy and prepare the company for its IPO. He was previously CEO & CFO of both Croft Associates (a developer of packaging, storage and transportation solutions for radioactive waste) and ThruVision (a manufacturer of security screening products). Clive is ACA qualified and spent over 12 years at UBS Investment Bank following three years at PricewaterhouseCoopers.	Helen joined Agents' Mutual in August 2013, having previously been Sales & Marketing Director and part of the founding management team at PrimeLocation. Before that, Helen was marketing director at Lombard Bank, developing the Lombard Direct brand, having previously worked at Citibank.

Principal shareholders	(%)
Schroder IM	6.0
Jason Walker	3.1
Albert E Sharp LLP	3.0

Companies named in this report

Rightmove (RMV.LN); ZPG (ZPG.LN); Purplebricks (PURP.LN); Zillow (Z.US); REA Group (REA.AU); Axel Springer (SPR.GR); Scout24 (G24.GR); LEG Immobilien (LEG.GR); Domain Holdings Australia (DHG.AU); Trade Me (TME.NZ).