EDISON

International Greetings

Final results

Many happy returns

Care & household goods

International Greetings has delivered strong growth in earnings, ended its financial year with net debt below previous estimates and returned to the dividend list a year ahead of earlier expectations. While underlying markets provide little stimulus, there remains plenty of scope for the group to grow its top line through increase in market share, particularly in the large US market, leveraging its highly efficient manufacturing production and strengths in global sourcing. The share price is now recognising some of the achievement to date, but not necessarily the ongoing opportunities.

Year end	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
03/14	224.5	8.1	9.1	0.0	14.0	N/A
03/15	229.0	9.6	11.8	1.0	10.8	0.8
03/16e	233.5	10.1	12.2	2.0	10.4	1.6
03/17e	237.0	11.1	12.8	3.0	9.9	2.4

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

US market key to top-line growth

Two years into its three year plan, International Greetings (IGR) has dedicated considerable capex into upgrading its manufacturing facilities in China, the Netherlands and Wales. These are all performing, at the very least, in line with targets and are driving progress on margin. Tackling the considerable opportunity in the US has been delayed by the sad death of the US CEO last year, but the new incumbent (appointed in April 2015), is already outlining the strategy to build market share within new customer categories, as well as looking at opportunities in other markets. Continuing product innovation and new product licences agreed with Disney and Universal Studios should also put a shine on performance, which remains on track to meet management's ongoing target of double-digit cumulative average growth in earnings per share. Management bandwidth has freed up post the US appointment and the finishing of the main capex projects, and acquisitions to broaden the offer in adjacent categories, or strategic deals, such as last year's Enper purchase, are now more likely, subject to meeting stringent payback hurdles.

Leverage greatly reduced

Performance on net debt was even better than the previous ambitious target of £30m, helped by tight working capital management, particularly in the US. The newly-stated aim is to reduce average net debt from the current 4x to 2.5x by FY19. Our model shows year-end net debt reducing to £26m at end FY16 and £22.5m for FY17. The group has declared the intention to pay a 1p dividend, rising thereafter.

Valuation: Further upside potential

The share price has performed well over the last quarter, as the market has started to believe that the group's progress is both real and sustainable. With forecasts edged very slightly ahead, the valuation framework has shifted up. A share price in the 145-164p range, based on a broad peer group and DCF calculations, would not look particularly stretched.

24 June 2015

Price	**127p**
Market cap	**£74m**
Net debt (£m) at end-2015	29.4
Shares in issue	58.2m
Free float	50.8%
Code	IGR
Primary exchange	AIM
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	7.2	67.1	66.0
Rel (local)	9.9	70.3	61.5
52-week high/low		131.5p	68.5p

Business description

International Greetings (IGR) is one of the world's leading designers, manufacturers, importers and distributors of gift packaging and greetings, social expression giftware, stationery and creative play products.

Next events

AGM	16 September 2015
H1 Results	2 December 2015

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International Greetings is a research client of Edison Investment Research Limited

Investment summary

Company description: Supplier of social stationery

International Greetings is a leading global designer, manufacturer, importer and distributor of gift packaging and greetings, social expressions giftware, stationery and creative play products. It has both manufacturing and sourcing expertise, with its manufactured products accounting for 46% of group revenues. It supplies goods for both the Christmas and everyday markets, encompassing trade/generic and customer own-brand and has a very broad range of customers right through from the large discount retailers, through the multiple grocers and drugstores to the upscale and niche retailers. Around 15% of product bears character or other licensing. The UK is the core manufacturing base of the group, but it has other manufacturing facilities in China, the Netherlands and the US, with the UK, US, Australia and other European countries being important trading areas. Having inherited a legacy of a balance sheet overburdened by an earlier buy-and-build strategy, management has considerably reduced levels of debt within the business, despite instituting a substantial investment programme in upgrading the manufacturing facilities, with the full support of the group's banks. Markets are and will remain highly competitive, so optimising manufacturing efficiency while providing exemplary customer service are prerequisites to running a profitable business. Top-line growth is more dependent on increasing the addressable market.

Valuation: Further potential upside

The valuation has now moved from one of scepticism and wariness of the heavy debt to one that is starting to reflect the achievements of the management team to date, as well as the opportunities to push for profitable growth despite little overall positive movement from the market. Looking at a current-year earnings multiple for a broad group of some peers, albeit not directly in the same market segment, and comparing with a DCF based on very modest top-line growth with some margin improvement, we suggest that a share price range of 145-164p would not look stretched.

Financials: Margin growth, reducing debt

The full-year results to the end of March were as outlined in April's trading update, with an even better performance on net debt than expected. Operating margins are beginning to show the benefits of investment (despite a somewhat disappointing performance from the Australian JV), with further benefits still to accrue. Our forecasts for FY16 have been edged very slightly ahead (+2% at the EPS level) and we have published our first thoughts on FY17, showing EPS growth in the year of 5%, despite a rising tax charge as profitability improves in the US and in Australia where corporation tax rates exceed the UK. Leverage reduced through the longstanding target of 2x in the year just reported, triggering the reinstatement of a dividend, which is set to rise towards cover of 3x, subject to competing requirements of further capex projects or acquisitions.

Sensitivities: Currency, competition, seasonality

The US dollar and the euro are important group currencies, with raw material costs predominantly in local currency, US dollars and in renminbi for goods sourced in China. Underlying consumer demand is a constant issue and customers are relentless in their pursuit of value, and deflation will remain an issue at the commodity end of the scale. There is little growth in underlying markets, but longstanding trading relationships help visibility. Small acquisitions, such as Enper, can extend the customer reach. Raw material, freight and energy costs are key inputs. In such competitive markets, optimising manufacturing efficiency and procurement is essential, and the best way to protect market share is by ensuring exemplary customer service and innovative design. While growth is targeted at everyday product, Christmas product is of key importance.

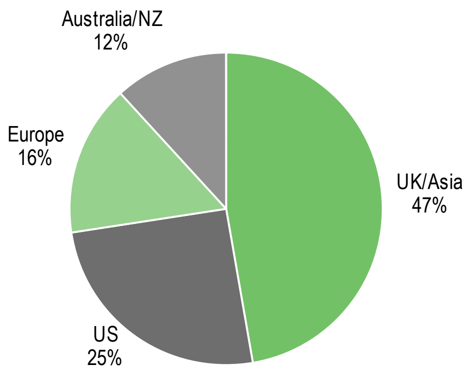
Company description: Package deal

IGR is a global supplier of social stationery across a range of categories, principally gift packaging (which constitutes the bulk of sales), greetings-related product (73% of group revenues) and stationery and creative play products (27%). Its core strengths are in design, innovation, manufacturing and sourcing, giving its customers (multiple retailers) a one-stop-shop option.

The group supplies its product into an exceptionally broad range of retail customers, from the mass market brands in the US such as Costco, Target and Walmart, through the major traditional multiple grocers and the discounters in the UK, the discount/dollar stores, regional retailers as well as niche and upscale retailer groups and online retailers. The group's products are sold in 80 countries, with long-term (not necessarily contractual) relationships with over 5,000 customers, the largest of which represents around 8% of sales.

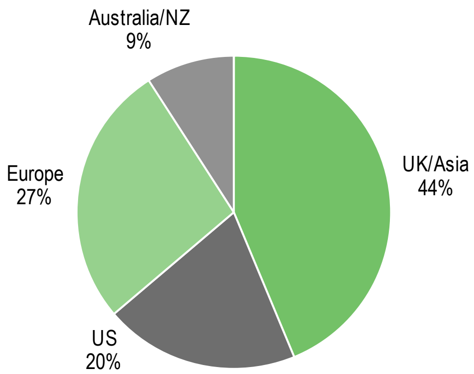
IGR has manufacturing facilities in the UK, China, the Netherlands and the US and its major trading geographies are shown below. The Asian figures are reported within a larger UK/Asian category as this covers procurement activities, which it would be misleading to separate out. By destination, the UK remains the largest market at 33% of revenues, closely followed by the US at 32%, Europe at 21%, Australia/New Zealand at 12% and the rest of the World at 2%. On average, the group employs just under 1,700 people, principally in China, the UK (the two largest manufacturing geographies), the Netherlands and the US. Common IT infrastructure is facilitating the use of the main design studios across the group's global manufacturing and sourcing, as well as giving the more obvious benefits in sales and CRM.

Exhibit 1: Revenue by geography FY14



Source: International Greetings

Exhibit 2: Operating profit by geography FY14



Source: International Greetings

Social expressions stationery supplier

IGR originated as a gift-wrap printing company established in Wales in the late 1970s by Anders Hedlund (whose family interests still account for 40% of the group's equity, 38% on a diluted basis). By the 1990s, the group had expanded to include other seasonally related products, selling predominantly to UK wholesalers. The strategy then shifted toward supplying the major UK retailers, as they moved to an aggressive market share grab of the national purse. The group also made its first major overseas move, buying a US-based manufacturer of ribbons and bows. The group floated on AIM in 1996, at which point sales were around 90% in the UK, 90% in buyers' own-brand and 90% oriented to the Christmas season, with a buy-and-build strategy.

A number of acquisitions expanded the group's sales base, but the internal disciplines and structures necessary to support the larger top-line were lacking and the weaknesses were exposed when markets softened in 2007. The balance sheet had become significantly overstrained, with gearing reaching 168% at end FY09. A new finance director specialising in restructuring and control implementation was appointed and in January 2009 Paul Fineman was appointed group CEO, having joined the group in 2007 with the acquisition of Anker (a UK-based supplier of stationery and children's activity kits). Since taking up the role, Paul has focused on instilling commercial disciplines on a group that had been expanded somewhat opportunistically. He has many years of experience in the industry, having joined his family firm, Anker, after college. Anthony Lawrinson took over as CFO in October 2011, joining from Reliance Security Group, with prior experience in a range of sectors including O2 and Hickson International.

Tight financial management has seen the gearing situation first brought under control then actively managed down and at a notably faster pace than we had anticipated. The result is that the group has strong support from its banking network, with facilities renegotiated on improved terms last year. More importantly, the strict discipline on cash management has given the executive team the comparative freedom to be able to make operational decisions (in particular the significant capital investment programme) in the interests of building the group's future rather than simply focusing on paying back the debt. In FY09, the group had gearing of 168%. EBITA was roughly the same level as the interest bill, EBITDA at 2.3x interest and the market was understandably sceptical that the group could pull through in a dull underlying market. Six years on and net gearing has reduced to 47%, with EBITDA 6.0x the interest bill in FY15.

Licensed product across the group makes up around 15% of group revenues, but concentrated down to a relatively narrow and focused portfolio. This principally consists of perennial properties, but with some 'hotter' additional licences such as *Frozen*, *Minions* and *Marvel Avengers*, which, despite being fairly recent or current, have potential 'staying power'. The retail segment has become increasingly risk averse in its stock decisions, but many of the Disney or Universal properties have the momentum to drive sales even in dull markets.

Driving manufacturing efficiency

IGR is a major global supplier of social stationery, with over half of group revenues earned outside the UK. It operates within a highly fragmented market and has built a more even balance of business between everyday and Christmas sales (44%:56%), and between manufactured and sourced product (FY15: 54% outsourced, 46% manufactured). The group has undertaken a significant investment programme, which started in China with the factory relocation three years ago. This provided additional capacity and greater efficiency, with a higher degree of automation. New investment should more than double the number of gift bags produced to around 20 million units post investment. The next stage of the main capex programme was the upgrade of manufacturing facilities in Hoomark in The Netherlands in H113. The Hoomark gift-wrap printing presses were upgraded to high-speed, high-definition, double-width, flexographic presses using water-based inks, with considerably faster run times, quicker turnaround between runs and greatly reduced wastage – a precursor to the programme carried out at the main UK manufacturing facility in Wales and providing a useful route map for the larger project. The Welsh project was finished to time and to budget and has delivered initial productivity benefits sooner than had been anticipated. The revamped Welsh facility was reopened by HM The Queen in summer 2014.

IGR holds Royal Warrants for crackers and now gift wrap, a valuable marketing advantage internationally, particularly in the US. The exemplary handling of these substantial projects on time and on budget is testament to management's planning skills and discipline.

Branded product and close customer relationships

IGR supplies a wide product range within the social expressions stationery and creative play SKUs, predominantly low ticket items that give some degree of recession-resilience. It has generic, licensed and customer-bespoke items, with a strong internal design capability in dedicated studio facilities in Wales and elsewhere, with a common IT platform and digital asset management system that facilitates the group producing or sourcing product wherever it makes economic sense to do so. It has a very large customer base, with a strong presence in the value sector, in particular the dollar stores in North America, as a result of a proactive sales focus over the last few years. However, it also has significant upscale business, some of which is within the well-known **Tom Smith** branding. Branded product (including Tom Smith, Kids Create and the new ‘B’ Unique [Aus and US]) accounted for around £90m of group revenues.

The group has long-term relationships, maintained by delivering well-designed products and paying close attention to customer service as well as to product quality. The majority of the customer base has traded with the group for more than 10 years. For many customers, compliance is of increasing importance, with the integrity and environmental impact of the supply chain becoming a key issue. Particularly for those sourcing from China, this can prove problematic. By switching away from solvent-based printing to water-based inks and by paying close attention to its own supply chain, and with a resource of 20 people on the ground in China overseeing suppliers’ investment and innovation, IGR continues to push itself up preferred supplier lists and create barriers to entry despite commoditised markets. Licensors are also demanding ever-higher standards, having greater levels of brand equity at reputational risk.

Levers of growth for the next stage

With the core manufacturing upgrade in place and beginning to deliver the benefits on operating efficiencies, the focus is shifting to the levers of growth for the next stage of the group’s development. These include:

- Broadening the product range, giving customers an ‘easy’ ordering option – and crucially dependent on relationships of mutual trust. This is not simply a matter of having the relevant product lines, but having good design that resonates with the ultimate consumers, continuing innovation to maintain consumer interest (and to manage input costs through product re-engineering) and scrupulous attention to customer service. Partyware is a possible adjacent product category, often with the same buyers as the existing range. The stationery and creative play elements of the business are key areas identified for growth, using existing expertise in design and sourcing, and putting additional investment into the group’s generic brands.
- More generally, management intends to grow the branded product offering, principally IGR brands, but also licensed brands where satisfactory terms can be achieved. This can de-risk the stock position and also has margin advantages.
- Appointing category champions across the group, driving product development, innovation and consistency and getting the most out of the supplier base for externally-sourced product. The approved supplier list is being concentrated to optimise pricing and to facilitate the monitoring of compliance. These moves should be seen as underpinning, rather than enhancing, margin.
- Bolt-on and/or infill acquisitions, such as that of Enper, with complementary customer bases.
- Increasing the proportion of everyday product to reduce seasonality and ease working capital surges, as well as managing the physical implications of warehousing and freight usage.
- Developing new channels to market.
- Continuing to drive down debt to give greater management flexibility.

The big potential win is getting the US business to perform optimally. Progress was affected by the tragic sudden death of the US CEO last year. A new CEO, Gideon Schlessinger, was appointed in April 2015, and brings extensive retail experience across a variety of categories. He has a strong profile in the regional supermarkets and drug stores, which will extend the group’s reach, as well as detailed knowledge of Latin and South American markets. Gideon’s appointment and refreshing the US management team has also freed up central management bandwidth.

Investment continues

With the positive handling of the debt position, the group has been able to be more proactive about its growth strategy. Management has also been able to take decisions in the longer-term interests of the group, such as upgrading the manufacturing facilities. While this delayed the pay-down of the outstanding debt, the returns from improved efficiency are helping to rebuild margins, as well as giving greater environmental reassurance to the customer base. The group's bankers have been very supportive of the investment programme, adjusting terms to the group's advantage (Exhibit 7).

The US manufacturing facility is now the only one that has not benefited from a significant investment programme and this is now scheduled to proceed through a further two phases. Phase I is additional conversion capacity at a likely cost of around $2.5m, on a very quick payback. Phase II is a more substantial investment in printing, which is currently being evaluated in detail. We have built in suggested capex of $5.5-6m in FY16 and FY17 to our financial model.

In June 2014, IGR acquired the trade and assets of Enper, a manufacturer of gift wrap in the Netherlands, for €1.9m. This was to some extent an opportunistic move, with Enper having around €3m of revenues and finding itself struggling to maintain both sales and margin. It has given IGR a good opportunity to maximise the synergies, which have started to come through ahead of earlier expectations, contributing to the stronger performance of the European business in the year just reported.

Remains a large, flat and fragmented market

There are limited statistics available on the specific market segments in which IGR is involved. According to the latest Marketline report, the global wrapping and paper packaging market was worth US$210.3bn in 2013, having grown at 6.2% CAGR between 2009 and 2013, which implies a marked slowdown in 2013. Volumes grew by 2.7% CAGR, with price appreciation of 3.4%. The vast majority of the market is in categories other than gift wrap, particularly food and beverage packaging. The report indicates growth of 5.3% CAGR over 2013-18, taking the overall market to US$272.3bn. The US National Greetings Card Association values the greeting card market at US$7-8bn (ahead of IBISWorld's market estimate of $6.1bn); 6.5 billion cards at an average price of c US$1.15, figures unchanged on the previous year. Everyday cards make up 67%, with Christmas the largest 'occasion' (25%).

IBISWorld's latest report estimates that the online segment is worth c $234m, at a CAGR of 1.8% for 2010-15, around 3% of the total US market. In the UK, the Greetings Card Association's 2014 report sizes the market at £1.29bn (down from £1.4bn in 2013), with everyday cards at £1.02bn and an average retail price of £1.44. On average, people in the UK send 31 cards per year, 85% of which are purchased by women. Wholesale value is typically around 40% of the retail value. Online is mostly simply an alternative route to market, although there are online-only suppliers such as Moonpig (PE-owned). WHSmith brand Funky Pigeon is reported to be continuing to perform well, with a recent brand extension into party ware. From a customer perspective, the key attractions are convenience and the ability to personalise. The online segment has grown to 3-4% of the greeting card market, similar levels to the US.

IGR's market segment is grouped together as 'social expressions' stationery, which it estimates to have a global value around £3bn, giving it c 7% market share. At retail, this is roughly equivalent to £10bn. The market is characterised by a very large number of small players (there are estimated to be around 3,000 greeting card publishers in the US alone), together with a handful of more substantial companies such as Hallmark and American Greetings, making for an intensively competitive trading environment. IGR has now overtaken CSS to become the third largest player in its relevant markets. While design is the most obvious distinction (and what draws most participants to the industry in the first place), success or failure is more likely to depend on a supplier's commerciality – customer service, payment terms and other concessions to the retail customer market, such as marketing support or category management under long-term agreements.

Cost is the key driver to delivering acceptable returns in commoditised markets, which means good sourcing and continuing product engineering, both areas in which IGR has underlying strengths.

Sensitivities

Currency. The group's larger currency risk is on purchases, with the main exposure being to the US dollar and the Chinese renminbi. On sales, key currencies are sterling, the US dollar and the euro, and IGR hedges against expected future sales for which there are firm commitments. With around half revenues generated outside the UK, there is a translation exposure, which in the year just reported was limited to £0.2m at the net profit level due to matching of costs and funding at like-for-like translation. The transactional impact of exchange rates will be felt more keenly this year due to the significant weakness in the AU$:US$ and €:US$ rates, with translational impact against sterling also a factor. We have attempted to reflect these moves within our FY16 forecasts.

The group's financial performance is subject to a number of sensitivities, most particularly **underlying consumer demand**, itself a factor of economic confidence. This will obviously vary across the economies in which the group operates and we assume little fundamental growth in markets. Given that people are unlikely to stop wanting to give each other presents, having attractive design for their presentation, product that is widely available and at the right price is crucial to maximising market share. High service standards need to be (at least) maintained to protect share in a competitive marketplace, while innovation skills help to retain retailer interest and also help recoup margin lost through a deflationary trading environment.

The group has a very **broad spread of customers**, so concentration of revenue is not an especial issue. The largest customer on a group-wide basis accounts for around 8% of group sales. Small acquisitions, such as that of Enper, broaden the customer reach. Online competition has had limited impact on the market to date, taking an estimated 3-4% share in developed markets, with online retailers being customers in their own right for gift-wrapped shipments. As described elsewhere, the market is heavily populated and highly competitive.

Licence management. IGR has longstanding formal relationships with key brand owners including Disney, historically an important entry ticket to obtaining other key licences. The group has recently gained additional licences for Universal Studios and *Star Wars* (now Disney-owned), adding to the stable of perennial properties. Licences for *Despicable Me* and for *Frozen* have performed very strongly recently. Rates vary by player and generally have minimum guarantees attached.

Seasonality. While there are other smaller peaks during the year, Christmas is the group's key selling period and a poor Christmas would have a notable impact in the financial outturn. Working capital climbs from July, peaking in November, before falling sharply in December and January as seasonal debtors settle their accounts. The group's intention is to work at increasing the proportion of everyday product to partially offset the effect. The benefit of having substantial Christmas business is the visibility it affords, allowing for efficient scheduling of work through the factories.

As for all manufacturers, **raw material and energy costs** are a perennial concern, with paper the largest element of cost, followed by labour. Continuous improvements to the efficiency of manufacturing will help to offset inflationary input costs. Moving to more modern machinery also lowers the environmental impact, particularly the transition away from solvents to water-based inks.

The group's pension schemes are all defined contribution and there are no especial issues here.

Valuation

There is no one obvious valuation methodology. Therefore, we continue to look at it from three perspectives: peer comparison, a DCF basis and underlying asset value. None of these methods provides a definitive valuation, but in combination they give a context for the pricing of the stock.

Down to one quoted peer

There are no directly comparable quoted peers in the UK and the overall competition is highly fragmented. The most substantial international operators are:

- Hallmark Cards, a privately-owned US company with 2014 revenues estimated by Forbes to be $3.5bn (down in each of the last three years). Hallmark has rationalised its manufacturing base, going from three to two production facilities in the US and closing its greeting card and gift-wrap manufacturing in Bradford, UK.
- American Greetings Corporation, which was quoted on NYSE until being taken private by the Weiss family in 2013. It generated revenues of $2.0bn in the year to February 2015, up 2.1% on the prior year. Its last 10-k refers to higher sales of greetings cards, gift packaging and party goods, and a $21.9m impairment charge on the Clinton Cards brand. Operating profits were down in retail and international social expression products, partly offset by better performance in North American social expressions. Due to the Weiss family's position, the take-out price of 0.5x EV/TTM revenues and 7x EV/2013 EBITDA was a poor proxy for the business's value.
- CSS Industries, again a US firm but still quoted and on a smaller scale, with historic sales of $313m, down 2% year-on-year. CSS has a bias to Christmas product at 30% of revenues and there are no publicly available forecasts.

Given that there is no direct peer group, we have cast our net a little wider and looked at three other US-based manufacturers and distributors of relatively low-ticket consumer goods/gifts; Blyth (candles, photo frames); Lifetime Brands (kitchen gadgets); and JAKKS Pacific (toys, consumer licensed products). With these comparators, IGR is now trading broadly in line on historic EV/revenue and EV/EBITDA and at a discount on a current year P/E basis of 14%. Closing this discount implies a share price of 145p.

Exhibit 3: IGR and broad peer group summary valuation metrics

	Price	Market cap	EV/revenue (x)	EV/EBITDA (x)	P/E (x)	P/E 1 (x)	P/E 2 (x)	P/CF
IGR	127.0p	£71m	0.44	6.3	10.8	10.4	9.9	4.4
CSS	$28.86	$270m	0.75	8.8	16.0			8.2
Blyth	$6.69	$108m	0.18	3.3	N/A			N/A
Lifetime Brands	$14.87	$206m	0.57	8.2	41.2	12.2	9.8	9.2
JAKKS	$8.81	$206m	0.38	5.0	22.2	11.9	10.7	4.0
Average (excl. IGR)			0.47	6.3	26.4	12.1	10.3	7.1

Source: Company accounts, Thomson Reuters, Edison Investment Research. Note: Prices at 18 June 2015.

DCF

Exhibit 4: DCF under varying terminal growth and WACC assumptions

		Terminal growth rate				
		-2%	-1%	0%	1%	2%
WACC	13%	103.4	105.5	108.0	110.9	114.3
	12%	115.5	118.3	121.5	125.3	129.9
	11%	129.6	133.2	137.5	142.7	149.0
	10%	146.2	151.0	156.8	163.8	172.6
	9%	165.9	172.4	180.3	190.2	203.0
	8%	189.7	198.6	209.8	224.1	243.2
Break-even WACC		11.5%	11.7%	11.9%	12.2%	12.5%

Source: Edison Investment Research

Running a DCF has some relevance in industries that are long established and still growing but at a modest underlying rate, but comes with usual provisos regarding the sensitivity of the model to the underlying assumptions. Taking a terminal growth rate of 1%, the market is currently attributing a very high WACC of 12.2%. A 1% terminal growth rate and a 10% WACC give an equivalent share price of 164p, 29% higher than the current market valuation, ahead of the broad peer group.

Solid asset-backing

On the basis of the balance sheet as at the end of March 2015, the value of the net assets attributable to the owners of the parent company was worth 107.5p per share, or 102.5p after minorities, giving asset backing of 85% of the current share price.

Financials

The final results for FY15 have come in broadly as expected following April's pre-close statement, when our adjustments reflected how the good operating performance at the EBITDA level was magnified at the pre-tax level, given the sharply reduced net interest charge. The further reduction in blended tax rate and the reduced minority charge amplified the benefit at the EPS level. We regard our FY16 numbers as relatively cautious, given the current currency headwinds the group is facing and we are now publishing our first thoughts on FY17, again based on very modest top-line growth assumptions.

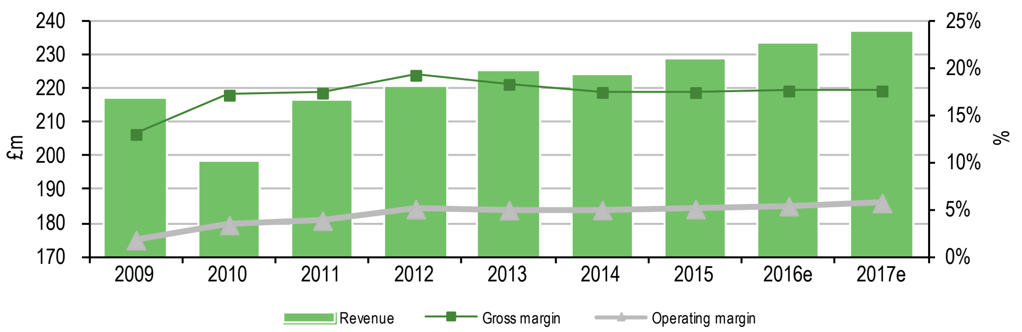
Exhibit 5: Minor revisions to forecasts

	EPS (p)			PBT (£m)			EBITDA (£m)		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
2015	11.7	11.8	+1	9.7	9.8	+1	16.2	16.9	+4
2016e	12.0	12.2	+2	10.0	10.1	+1	16.5	17.2	+4
2017e	-	12.8	N/A	-	11.1	N/A	-	18.2	N/A

Source: Company accounts, Edison Investment Research Note: FY15 New = actual

IGR does not operate in what might be categorised as growth markets. With perpetual pressure on pricing and a demanding customer base, achieving any top-line growth is creditable. The acquisition of Enper will have added roughly €3m of revenues. However, revenue growth of 2% in FY15 was affected by currency movements and like-for-like revenue growth was c 4.5%. The gross margin was constrained by the higher volumes of FOB business, but this does not fall through to the net margin and is not, of itself, an issue. Operating margin falls in the US and Australia were more closely allied to operational issues and forex, with the former being tackled post management strengthening. Close control of overheads (-8%) led to an improvement in EBITDA and operating margin, with reduced financing costs contributing to the strong growth in PBT (before exceptional items and the cost of the LTIP). The impact of the capex programme to date should benefit operating margins in both forecast years.

Exhibit 6: Revenue, gross margin and operating margin record and projections



Source: International Greetings, Edison Investment Research

The tax charge should increase over the next two years to reflect the improved profitability in the US and in Australia (although the latter is a 50:50 JV, so having less of an impact on EPS). The 2014-17 group LTIP is based on achieving three-year CAGR in diluted EPS (post LTIP) of over 10%, with the maximum under the scheme vesting at 20% CAGR. Our model shows this being achieved in 2013-16 and slightly undershooting in 2014-17. It may be the case that hitting the LTIP in the medium to longer term would necessitate further earnings-enhancing deals.

Having hit the published leverage target a year ahead of expectations, the group will now pursue a progressive dividend policy, subject to the competing requirements of internal capex investment opportunities and any M&A, with a general goal of moving towards three times cover.

Inventory focus improves cash conversion

The group's cash tax rate remains below the 'expected' rate, with further unrecognised tax losses of £0.3m in the UK and £1.7m in the US, but the more substantial contributor to FY15 positive cash flow was the working capital performance. A specific drive on the stock position in the US has taken out £4.0m of gross stock, partly offset by volume-related increases in Europe and Australia (where the effect was magnified by forex). Of the exceptional items taken in the year of £1.2m (relating to the Welsh investment programme, restructuring of the US management team and the Enper acquisition), £1.1m was in cash. We are not anticipating further exceptional charges in the current year.

Capital expenditure plans are now targeted at the US, although the detail and extent are still under evaluation. A relatively modest project in high-speed paper conversion, with payback of less than two years, is under way and a larger-scale project in printing is currently being formally evaluated. Our model anticipates capex of around £5.5-6.0m in FY16 and FY17.

Much improved balance sheet

Net debt at the end of March is at the lowest point in the annual cycle and the amount owing followed a similar pattern through the year as the prior year, reflecting the naturally inherent cyclicality of the business. The current funding arrangements are as illustrated below. With these results, the group has also disclosed the average leverage figure over the year – 4.0x, against 4.4x in FY14 and reduced from 5.5x in FY09. The target set is that average leverage should reduce to 2.5x EBITDA in FY19, which would imply a year-end leverage of less than one times.

Exhibit 7: Funding facilities at June 2015

Lender	Due	Facility, £m	Margin	Margin in prior year	Covenant/notes
HSBC					
– Medium-term loan	2018	21.5	2.60%	2.95-3.35% u/c	Interest cover; debt cover; cash flow cover; leverage
– Asset-backed lending	2016	34.5	1.85%	2.05%	
– HP agreement	2021	3	3.95% fixed	3.95% fixed	
– RCF and overdraft	Annual	6.5-17.5	2.65-3.0%	3.20-3.50%	
Sun Trust					
– Asset-backed lending	2017	24	1.75%	2.00%	Debt service cover
ING					
– Mortgage	2028	6	1.50%	1.50%	Debt service cover
– Asset-backed lending	2017	8	1.50%	1.50%	
– Finance Lease	2019	2	4.75% fixed	4.75%	
– Overdraft	Annual	2	2.00%	2.00%	
Westpac					
– Overdraft	Annual	6	0.85%	0.85%	Interest cover; capital ratio
Total		**113.5-124.5**			

Source: International Greetings

The stated target has been to reduce the year-end debt level to twice EBITDA and this has been more than achieved in the year just reported, at 1.8x EBITDA, well ahead of the original schedule and triggering the promised intention to pay out a dividend a year ahead of plan.

The group's fixed assets of £31.7m include £2.7m-worth of freehold land and buildings on two sites in Wales 'that may become available for sale in the future', one of which should comfortably realise in excess of book value. One is part covered by a call option to a power generating company. No benefit from realisation is currently built into our model.

Exhibit 8: Financial summary

£'000s	2013	2014	2015	2016e	2017e
Year end 31 March	IFRS	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS					
Revenue	225,211	224,462	229,025	233,500	237,000
Cost of Sales	(183,941)	(185,244)	(189,048)	(192,347)	(195,240)
Gross Profit	41,270	39,218	39,977	41,152	41,759
EBITDA	15,069	16,352	16,850	17,180	18,163
Operating Profit (before amort and except)	11,262	11,320	12,315	12,645	13,628
Intangible Amortisation	(494)	(576)	(428)	(410)	(400)
Exceptionals	(1,603)	(2,298)	(1,235)	0	0
Share-based payments	(22)	(82)	(623)	(600)	(750)
Operating Profit	9,143	8,364	10,029	11,635	12,478
Net Interest	(3,466)	(3,177)	(2,726)	(2,500)	(2,500)
Profit Before Tax (norm)	7,796	8,143	9,589	10,145	11,128
Profit Before Tax (FRS 3)	5,677	5,269	7,926	9,735	10,728
Tax	(1,601)	(1,582)	(1,346)	(2,133)	(2,644)
Profit After Tax (norm)	6,195	6,561	8,243	8,012	8,484
Profit After Tax (FRS 3)	4,076	3,687	6,580	7,602	8,084
Average Number of Shares Outstanding (m)	56.2	57.5	58.1	58.8	58.8
EPS - normalised (p)	9.3	9.4	12.1	12.4	13.1
EPS - normalised fully diluted (p)	8.7	9.1	11.8	12.2	12.8
EPS - (IFRS) (p)	6.0	5.2	10.7	12.1	12.9
Dividend per share (p)	0.0	0.0	1.0	2.0	3.0
Gross Margin (%)	18.3	17.5	17.5	17.6	17.6
EBITDA Margin (%)	6.7	7.3	7.4	7.4	7.7
Operating Margin (before GW and except.) (%)	5.0	5.0	5.4	5.4	5.8
BALANCE SHEET					
Fixed Assets	67,038	67,664	65,688	70,238	69,485
Intangible Assets	32,795	31,950	31,692	34,350	34,966
Tangible Assets	34,243	35,714	33,996	35,888	34,519
Investments	0	0	0	0	0
Current Assets	75,700	76,261	71,312	74,333	74,928
Stocks	50,114	48,460	46,162	46,593	48,001
Debtors	23,285	19,690	22,304	22,740	23,427
Cash	2,301	8,111	2,846	5,000	3,500
Other	0	0	0	0	0
Current Liabilities	(52,693)	(51,965)	(45,722)	(44,800)	(43,443)
Creditors	(39,273)	(39,139)	(39,982)	(39,800)	(39,443)
Short term borrowings	(13,420)	(12,826)	(5,740)	(5,000)	(4,000)
Long Term Liabilities	(33,473)	(34,799)	(28,694)	(30,356)	(26,356)
Long term borrowings	(31,019)	(32,232)	(26,479)	(26,000)	(22,000)
Other long term liabilities	(2,454)	(2,567)	(2,215)	(4,356)	(4,356)
Net Assets	56,572	57,161	62,584	69,415	74,613
CASH FLOW					
Operating Cash Flow	7,533	13,724	17,851	15,800	16,750
Net Interest	(3,285)	(3,221)	(2,775)	(2,500)	(2,500)
Tax	(937)	(60)	(1,263)	(1,940)	(2,639)
Capex	(1,705)	(5,291)	(2,100)	(6,000)	(5,500)
Acquisitions/disposals	0	140	(1,451)	0	0
Financing/Other	159	1,225	(1,347)	0	0
Dividends	(968)	(1,014)	(829)	(1,340)	(1,930)
Net Cash Flow	797	5,503	8,086	4,020	4,181
Opening net debt/(cash)	41,854	42,138	36,947	29,373	26,000
HP finance leases initiated	(1,649)	296	0	0	0
Other	568	(608)	(512)	(647)	(681)
Closing net debt/(cash)	42,138	36,947	29,373	26,000	22,500

Source: Company accounts, Edison Investment Research

Contact details	Revenue by geography
No 7 Water End Barns, Water End Eversholt Bedfordshire MK27 9EA UK +44 (0) 1525 887310 www.internationalgreetings.co.uk	See page 3

Management team	
CEO: Paul Fineman	**CFO: Anthony Lawrinson**
Paul joined the board in May 2005 as CEO of Anker, a UK subsidiary. He was appointed group MD in January 2008 then group CEO in January 2009.	Anthony joined the group in October 2011. His former roles included group FD of Reliance Security Group, CFO at O2 Airwave and group treasurer at O2 plc and Hickson International.
Chairman: John Charlton	
John joined the board in April 2010 and was appointed chairman in September 2011. He was previously senior VP for American Greetings and CEO of UK Greetings.	

Principal shareholders	(%)
Hedlund Family	40.5
Miton Asset Management	20.4
Paul Fineman	7.3
Diverse Income Trust	5.9
Close Private Asset Management	4.0
Hargreave Hale	3.9

Companies named in this report
CSS (NYSE:CSS) ; Blyth (NYSE:BTH) ; Lifetime Brands, (NASDAQ-GS: LCUT); JAKKS Pacific (NASDAQ: JAKK)