17 January 2020

NON-STANDARD FINANCE PLC

Sunshine after the rain

"The focus for the next few years is on relatively modest investment and on driving return on assets towards our medium-term target of 20% for each division". So said John van Kuffeler at the 16 January 2020 *capital markets day*. After an eventful 2019, 2020 (and beyond) is now all about operational delivery, the "boring" grinding out of profit from a franchise that has seen heavy investment over many years. We welcome this focus and think it will help deliver the 84% EPS growth (2021 on 2018) in current consensus estimates. The accompanying *trading statement* indicated 2019 results would be in line with market expectations. The shares rose 15% on the day.

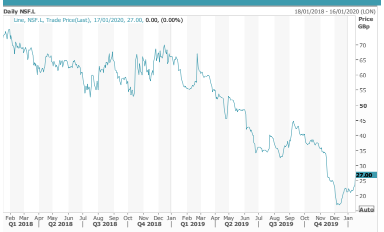
- **Trading update:** The branch-based lending business' (ELL) net loan book grew 17% and the guarantor loan division (GLD) book by 29% vs. end-2018. Home Collected Credit (HCC) saw a small fall. Impairments were 22.4% of revenue in ELL, 22.6% in GLD and 27% in HCC. Progress has been made on a cheaper, six-year, securitisation line that is expected to be £150m-£200m in size.
- **Capital Markets Day:** The presentation focused on the good current trading conditions and how the group will operationally deliver profit growth. NSF emphasised that the franchise build was largely complete and now the focus can be on delivering profit growth. The company's focus on developing the right culture to underpin long-term success was also underlined.
- **Valuation:** Our absolute approaches now indicate a range of 79p-85p. At the current price, the 2020 prospective P/E is 4.4x for a business whose impairment provisioning already reflects a significant downside scenario and where earnings could nearly double over three years. The yield is also double-digit.
- **Risks:** Credit risk is the biggest threat to profitability. NSF's model accepts more credit risk, where a higher yield justifies it. NSF is innovative, and may incur losses piloting products, distribution and customers. Regulation is a market issue; management is acting to mitigate this risk.
- **Investment summary:** Substantial value should be created, as: i) competitors have withdrawn; ii) NSF is well-funded, with committed debt funding to 2023; iii) macro drivers are positive; and iv) NSF's experienced management delivers operational efficiency without compromising the key face-to-face model. Management targets of strong loan book growth and 20% EBIT RoA appears credible. Plus, investors are paying 6.6x 2019E P/E and getting a 11.1% yield.

Financial summary and valuation

Year-end Dec (£000)	2017	2018	2019E	2020E	2021E
Reported rev./other inc.	121,682	168,128	184,249	205,651	227,785
Total impairments	-28,795	-42,688	-45,658	-52,408	-56,400
Total costs	-69,203	-89,564	-95,000	-99,726	-107,743
Normalised EBIT	23,684	35,876	43,590	53,516	63,642
Adjusted PBT	13,203	14,769	15,878	23,391	29,941
Statutory PBT	-13,021	-1,590	-19,779	20,262	28,410
Pro-forma EPS (p)	3.44	3.70	4.12	6.18	7.95
DPS (p)	2.20	2.60	3.00	3.10	3.95
P/adjusted earnings (x)	7.9	7.3	6.6	4.4	3.4
P/BV (x)	0.4	0.4	0.5	0.4	0.4
P/tangible book (x)	1.1	1.5	1.8	1.4	1.1
Dividend yield	8.1%	9.6%	11.1%	11.5%	14.6%

Source: NSF, Hardman & Co Research; all years are on IFRS 9 basis

Financials



Source: Refinitiv

Market data

EPIC/TKR	**NSF**
Price (p)	**27.0**
12m High (p)	70.0
12m Low (p)	27.0
Shares (m)	312.4
Mkt Cap (£m)	84
EV (£m)	337
Free Float	99%
Market	Main

Description

In the UK non-standard lending market, Non-Standard Finance (NSF) has the market-leading network in unsecured branch-based lending. It is number two in guarantor loans and number three in home credit.

Company information

CEO	John van Kuffeler
CFO	Nick Teunon

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Key shareholders

Alchemy	29.95%
Aberforth Partners	15.02%
Marathon Asset Mgt.	10.85%
Neil Utley	4.02%
Tosca Fund	3.90%
Basswood	3.25%

Diary

Mar'20	2019 FY results

Analyst

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Trading update

Group in line for 2019, no change in targets

"Trading in the final few months of 2019 was as anticipated and so the results for the year ended 31 December 2019 are expected to be in line with the current consensus of analyst forecasts. The Group's medium-term targets for loan book growth and impairment as a percentage of revenue are unchanged.

ELL 17% book growth, impairments 22.4% of revenue, branches up eight to 73, customers +23% to 75,400

"In branch-based lending, Everyday Loans has continued to deliver an impressive performance. At 31 December 2019 its net loan book before fair value adjustments had reached £218.3m (2018: £186.2m), a 17% increase versus the prior year. The opening of eight new branches in 2019 took the total number to 73 and this, together with improved productivity from an enlarged workforce, helped to drive customer numbers up by 23% to 75,400 (2018: 61,200). The business also collected well and impairment as a percentage of normalised revenue ended the year at 22.4% (2018: 21.1%), well within our target of 22-24%. We continue to believe that consumer demand for branch-based lending will support a network of over 100 branches in the medium-term and so plan to continue to deploy our successful formula of splitting a limited number of larger branches in order to create additional capacity for future growth.

GLD 29% loan book growth, customers +30%, impairments 22.6% of revenue

"Having taken the decision to consolidate all of our guarantor loans activities into a single location in October 2019, the net loan book increased by 29%, to £107.4m (2018: £83.1m). The number of customers also grew strongly, up by 30% to 32,600 (2018: 25,100). By continuing to develop our channels of supply and deepening our broker relationships, the volume of leads coming in to both the TrustTwo and George Banco brands remains strong and we are now focused on returning lending volumes to those achieved prior to the consolidation. A concerted effort by the collections team over the past few months meant that the rate of impairment as a percentage of normalised revenue was 22.6% (2018: 20.0%) which was lower than in the first half of 2019 and was within our medium-term target of 22-24%.

HCC small book and customer numbers decline; impairments 27% of revenue (2018 32.6%)

"In home credit, Loans at Home's performance was slightly better than expected during the peak lending period in November and December. Our drive to shorten the loan book meant that the net loan book ended the year at £39.9m (2018: £41.0m). While sales volumes to existing customers were lower than last year, new customer volumes remained strong with the result that the total number of customers at the end of 2019 was broadly flat at 92,400 (2018: 93,800). A strong collections performance and improving loan book quality meant that impairment as a percentage of normalised revenue was 27.0% (2018: 32.6%) which is below our previous guidance of 30-33%. We now expect a period of relative stability in home credit and more normalised rates of loan book growth, in line with our medium-term targets.

Six-year securitisation facility for £150m-£200m at advanced stage (due diligence completed so at final legal stages). Another announcement due shortly.

"The Group is continuing to make good progress on finalising a new £150-200m, six-year securitisation facility to help fund future loan book growth. We have signed an agreed term sheet and expect to complete the final documentation shortly. It is expected that the terms of the facility will provide a meaningful reduction in funding costs versus the Group's existing long-term funding arrangements that mature in 2023. A further announcement will be made in due course."

This statement follows the one in November that saw material downgrades to forecasts around: i) 4%-5% reduction in EBIT in 2019 from lower-than-expected guarantor loan growth due to short-term operational issues; ii) 6%-8% reduction in 2019 estimates from a revision to provisioning policy with a greater weighting to the downside scenario – with no change in customer behaviour the effect is to reduce near-term profit; and iii) lower forecast loan growth across all divisions (typically ca.10%) reflecting a more conservative outlook. We explored each of these in our note *Trading update: understand the accounting,* published on 18 November 2019. The 2021 adjusted consensus forecast EPS has fallen from 10.1p to 6.8p.

Capital Markets Day

Summary

Core market attractions, and favourable current conditions continue. Franchise significantly built so focus now on profit rather than investment.

The key thing for us about this Capital Markets Day was its tone. There was the usual highlighting of: i) the fundamental attractions of the 10m-12m non-standard finance market; ii) favourable macro conditions with low unemployment where low incomes have risen well ahead of average earnings; iii) the substantial market-leading (or near market leading) franchises, which have built over the past four years; iv) limited regulatory impact on the company's own areas of business; and v) competition reducing. These themes are a multi-year continuation of trend and should not come as surprise.

Consensus is earnings to nearly double 2021 on 2018 – all about execution from here

What was relatively new was the tone – an emphasis on profit delivery rather than growth and investment and, for example, the importance of culture in achieving this result. Despite the estimate cuts seen at the end of 2019, consensus estimates are still for earnings to nearly double 2018 to 2021, and the "boring" operational grinding out of profit is key to this.

Strategic outlook 2020-22

Attractive market to be in, good positioning within it and market share gains; risks appear muted

Management noted a significant opportunity exists to deliver attractive and sustainable long-term returns as: i) the non-standard customer in the UK remains underserved; ii) overall market competitive pressure is declining (in particular from payday lending and rent-to-own that have been the subject of a regulatory crackdown); iii) a potential recession-induced tightening of credit by mainstream lenders, can be expected to increase NSF customer volumes; iv) there is expected to be a consolidation of/exit by smaller operators (potentially regulatory and financing driven); and v) there is an increase in awareness of certain product segments (including guarantor loans). Key risks include: i) regulation, although this now appears to be approaching a more steady-state position rather than any dramatic increase in risk; ii) inability to access funding (details on new securitisation expected to be announced shortly); or iii) competition – if anything this appears to be reducing. The bias of upside to downside appears heavily geared to upside.

Divisionally different opportunities from market growth, gaining shares, payback for investment, efficiency gains and lower funding costs. Important that there are multiple levers and opportunities.

Divisionally, the key ELL opportunities include: i) splitting branches to generate additional capacity with rapid payback; ii) expanding towards 100 branches over the medium term (potentially up to 120 branches over the long term); and iii) operational efficiencies from process improvements – management is targeting a 5% increase in the current year. In GLD, there should be significant efficiencies from: i) the move to one location (having consolidated all activities at Trowbridge); ii) expanding operations and staff into new additional space in Trowbridge; and iii) further market expansion and share gains as competitors slow their pace of growth. In HCC, management will: i) continue to shorten the loan book; ii) roll out the customer portal and card payments on the doorstep; and iii) aim to make market share gains from competitors. The central/head office has already reduced operational costs and the new securitisation facility should reduce funding costs (although we do not yet know the quantum of this). We do not view these opportunities as new, they have been discussed several times before. Having significantly built the franchise and infrastructure, the key issue from here is delivering them.

Divisional highlights

In the sections below, we highlight the key issues that we took from the presentation. We have highlighted the relevant slide in the presentation.

ELL

The key slides we would highlight on Everyday loans are:

Slide 43/44 – peer comparison – key message is ELL is profitable – lower impairments from face-to-face model, costs in line with peers

When looking at the competition, we note:

- ELL is profitable while most peers lose money. On average, peers' annual losses are ca.3% of their loan book.
- One key driver to this is ELL's face-to-face model, which gives an extra layer of protection in assessing credit. ELL's impairment as a percentage of revenue is half the peer average. This was also highlighted on slide 50, which shows the waterfall of customers from application to loan (only 2% of applications actually get a loan). Critically, after the initial credit score (which uses the same data and processes available to peers) and a customer's decision to perhaps change their mind, only 16% of applicants are contacted by the branch. Of these, 11% then either fail further checks or decide that they do not wish to continue and so 5% actually attend the branch. Of these, only 2% get a loan as the face-to-face decision process uniquely declines the rest.
- On costs as a percentage of revenue, ELL is only slightly higher than the peers' average. There is a myth that online must be cheaper than branches, but this does not fully take account of: i) marketing costs; ii) constant need to upgrade technology; iii) customer retention rates (an existing customer is the cheapest new business); and iv) how much the benefit is passed to customers in lower rates.

Peer comparisons

£m	ELL	118118 Money	1st Stop Finance	Likely Loans	Bamboo
Loan Book	186	96	167	109	77
Revenue	79.6	68.3	31.7	52.6	25.7
PBT	14.1	-8.1	1.6	-4.3	-1.7
PBT as % closing loan book	8	-8	1	-4	-2
Impairments as % revenue	22	43	27	37	67

Source: Hardman & Co Research, NSF slide 43 based off latest filed accounts

Slides 53-55 – sustainability of model from controlled growth

Slides 53-55 show that the business has grown in a controlled manner with the applications to branch kept within a corridor of ca.500-650 per branch per month (per employee this works out at 100-140). Accounts per branch and per employee have been kept within similar corridors (800-1,200 and 190-260, respectively).

Slide 60 complaints very low – hard evidence that the culture of delivering good customer outcomes seen by customers too

All three divisions sought to emphasise the importance of culture and how it combined both customer service with good financial performance. To those seeking hard factual evidence that this works, we would highlight customer complaints. ELL gets 2.4 complaints per 1,000 customers, just 58% of the level of the market. The Financial Ombudsman overturns (i.e. rules against) 17% of ELL cases when the industry average is 46% (both excluding PPI). Not only does ELL get fewer complaints but a smaller proportion of the complaints are deemed as valid by the independent body overseeing the market.

Multiple levers to profit growth

In terms of franchise and profit growth, there is expected to be a further, modest (7%-10%) annual expansion in the branch network, more staff are being put in existing branches (ca.10% this year) and an annual 5% productivity improvement is targeted. The group highlighted how splitting existing, mature branches re-invigorates the growth (it allows more time for staff to focus on new business rather than existing account management). The opportunities from technology in helping to drive operational efficiency, deeper broker relationships, telephony, and management information were all noted.

GLD

The GLD section of the presentation again focused on delivering profit growth. In this case, there was integration of the back offices and control functions for the two complementary but different brands. While the basic product is the same, there are differences in distribution (George Banco is more focused on brokers while TrustTwo generates more from price comparison websites) and the resulting (modest) differences in borrower and guarantor profiles. Slide 84 shows the relative split between the brands by source, in terms of applications, decline rates and average balance size. As noted in the November 2019 trading statement, the operational integration provoked some disruption last year, especially in collections; however, management remains confident this is a short-term issue and that significant opportunities lie ahead.

Slide 89 Amigo comparisons – similar gross yield, more broker commission, better impairments, higher expense ratio (although gap falling as GLD achieves more economies of scale).

The only significant peer is Amigo compared with which GLD has: i) lower revenue yield (in this case GLD incurs more broker expenses, which are taken against revenue while Amigo has more low-cost brand recognition – the gross yields, however, are very similar); ii) much better impairments, despite a small element of lending being in personal loans, which carries above-average loss rates; iii) significantly higher expense ratio (quarterly average operating expenses ca.2.9% of average net receivables compared with 2.1% at Amigo) reflecting the significant economies of scale enjoyed by Amigo and GLD's practice of extensive discussions with borrowers and guarantors to ensure they fully appreciate the product as well as for credit assessment.

HCC

The key messages from HCC were of stable loan volumes, improving credit and so a rising risk-adjusted margin. There was considerable emphasis on the key role of the agent and of a culture which was focused on doing the right thing and remaining regulatory compliant. The group also highlighted how technology was allowing efficiency improvements (a message consistent with the other major providers).

Mature market but some share gain, as well as efficiency improvement, opportunities

The market is mature (NSF noted that the significant overall customer number reduction is due to Provident Financial losses not being fully offset by account growth elsewhere). Their current market share is estimated to be ca.8% (PFG about a third, Morses Club ca.20%). Approximately 40% of the market is still served by ca.470 smaller players where the expectation is that regulatory burdens, technology and ageing of owners is likely to see this share fall over time. NSF emphasised that it wants to be a first choice for the agents freed from such business and has a limited, and selective appetite for the acquisition of any such businesses. To support this position, NSF noted in the most recent survey, 89% of HCC employees were "proud" to be part of the company.

Central/head office

Slide 121 – funding – cheaper, longer-term, more diversified

For some time, NSF has indicated a desire to diversify and cheapen its funding while still maintaining long-term commitments. We understand a new £150m-£200m facility has been agreed and the lenders have done the due diligence so a final announcement of terms is due, hopefully in the near future, and once the legal process is completed. We understand that there may be a "meaningful" reduction in funding costs compared with existing facilities and a six-year term (current £285m term loan runs until 2023), although management resisted requests to provide any guidance on what the quantum of such a reduction might be. There is clearly an "opportunity" to repay some of the existing and more expensive facilities. The extent of any refinancing will be determined by the group at the time and will be considered in the context of wanting to ensure that the group has diversified and not concentrated funding, that there are no maturity cliff edges, as well as the need to fund future growth (our estimates £50m-£60m p.a.). We understand the term loan can be repaid without penalty at this stage. It will clearly not be fully repaid as the securitisation facility is less than the term loan.

Other news

i) director buying; and ii) Invesco overhang cleared

We note from recent RNS announcements that there has been significant director buying, with the CFO designate more than trebling his holding from 40k shares to 140k. The current CFO also increased his holding. The role will hand over post the March results. On 3 January, an NED bought a further 38k shares. We also note the Invesco overhang has cleared, Alchemy has materially increased its holding and a number of other holders have now declared holdings of more than 3% (Basswood, a NY-based hedge fund and Neil Utley, a private investor).

Financials

Our pre-tax and earnings estimates are unchanged from our latest report. There has been a small increase in loans (which feeds through to higher revenue). Impairments are a little better in 2019 but a little higher in 2020 and beyond (driven by higher loans). Costs are marginally higher.

Reported profit and loss

Year-end Dec (£000)	2015	2016	2017	2018*	2019E*	2020E*	2021E*
Business interest income	14,657	81,099	119,756	166,502	183,249	204,651	226,785
Other operating income	0	450	1,926	1,626	1,000	1,000	1,000
Fair-value unwind on acquired portfolios	-5,456	-8,342	-11,985	-7,678	-4,291	0	0
Total revenue	**9,201**	**73,207**	**109,697**	**160,450**	**179,958**	**205,651**	**227,785**
Impairments	-3,858	-23,651	-28,795	-42,688	-45,658	-52,408	-56,400
Gross profit	**5,343**	**49,556**	**80,902**	**117,762**	**134,299**	**153,243**	**171,385**
Administration expenses	-11,340	-44,074	-69,203	-89,564	-95,000	-99,726	-107,743
O/W depreciation	-198	-690	-1,497	-1,772	-4,500	-4,500	-4,500
Amortisation of intangibles	-4,030	-10,714	-7,897	-8,681	-6,092	-3,129	-1,531
Operating profit	**-10,027**	**-5,232**	**3,802**	**19,517**	**33,207**	**50,387**	**62,111**
EBITDA	**-5,799**	**6,172**	**12,518**	**29,970**	**43,799**	**58,016**	**68,142**
Exceptional items	-6,135	-626	-6,342	0	-25,274	0	0
Net finance (cost)/income	70	-3,484	-10,481	-21,107	-27,712	-30,125	-33,701
PBT	**-16,092**	**-9,342**	**-13,021**	**-1,590**	**-19,779**	**20,262**	**28,410**
Income tax	3,022	1,344	2,686	-89	-1,060	-3,560	-4,844
PAT from continuing operations	**-13,070**	**-7,998**	**-10,335**	**-1,679**	**-20,838**	**16,702**	**23,566**
Average no. shares for EPS calculation (m)	61.50	307.32	316.90	312.71	312.40	312.44	312.44
Statutory EPS (p)	-21.25	-2.60	-3.26	-0.54	-6.67	5.35	7.54
Adjusted EPS (p)		3.37	3.44	3.70	4.12	6.18	7.95
DPS (p)		1.20	2.20	2.60	3.00	3.10	3.95

*Source: NSF, Hardman & Co Research; *IFRS 9 basis*

Normalised profit and loss

Year-end Dec (£000)	2016	2017	2018*	2019*	2020E *	2021E*
Business interest income	94,674	119,756	166,502	183,249	204,651	226,785
Other operating income	450	1,926	1,626	1,000	1,000	1,000
Fair-value unwind on acquired portfolios	0	0	0	0	0	0
Total revenue	**95,124**	**121,682**	**168,128**	**184,249**	**205,651**	**227,785**
Impairments	-26,155	-28,795	-42,688	-45,658	-52,408	-56,400
Gross profit	**68,969**	**92,887**	**125,440**	**138,590**	**153,243**	**171,385**
Administration expenses	-50,290	-69,203	-89,564	-95,000	-99,726	-107,743
Operating profit	**18,679**	**23,684**	**35,876**	**43,590**	**53,516**	**63,642**
EBITDA	**19,369**	**25,181**	**37,648**	**48,090**	**58,016**	**68,142**
Net finance (cost)/income	-5,623	-10,481	-21,107	-27,712	-30,125	-33,701
PBT	**13,056**	**13,203**	**14,769**	**15,878**	**23,391**	**29,941**
Income tax	-2,688	-2,313	-3,197	-3,017	-4,094	-5,090
PAT from continuing operations	10,368	10,890	11,572	12,861	19,298	24,851

*Source: NSF, Hardman & Co Research; *IFRS 9 basis*

Balance sheet

@ 31 Dec (£000)	2015	2016	2017	2018*	2019E*	2020E*	2021E*
Non-current							
Goodwill	40,176	132,070	140,668	140,668	128,216	128,216	128,216
Intangible assets	14,119	17,412	17,205	13,431	7,339	4,210	2,679
Other assets				241	4,374	4,816	4,699
Right of use asset					11,187	10,000	8,500
Property, plant and equipment	1,718	5,459	9,434	7,723	8,441	8,441	8,441
Total non-current assets	56,013	154,941	167,307	162,063	159,557	155,683	152,535
Current assets							
Amounts receivable from customer	**28,415**	**180,413**	**268,096**	**314,614**	**365,600**	**413,276**	**474,079**
Trade and other receivables	10,275	9,709	1,551	3,967	5,000	5,000	5,750
Cash and cash equivalent	7,320	5,215	10,954	13,894	17,262	12,605	10,748
Total current assets	46,010	195,337	280,601	332,475	387,862	430,881	490,577
Total assets	**102,023**	**350,278**	**447,908**	**494,538**	**547,419**	**586,564**	**643,112**
Current liabilities							
Trade and other payables	13,803	8,005	10,353	17,242	19,242	21,242	23,242
Lease liability					1,659	1,659	1,659
Deferred tax liability	3,057	-	-	-	(1,114)	(2,299)	(2,633)
Total current liabilities	16,860	8,005	10,353	17,242	19,787	20,602	22,268
Net current (liabilities)/assets	29,150	187,332	270,248	315,233	368,076	410,280	468,309
Non-current liabilities							
Financial liabilities – borrowings	-	87,300	199,316	266,322	336,322	366,322	406,322
Lease liability					9,000	9,000	9,000
Deferred tax	-	5,890	4,996	252			
Total non-current liabilities	-	93,190	204,312	266,574	345,322	375,322	415,322
Total liabilities	16,860	101,195	214,665	283,816	365,109	395,924	437,590
Net assets	**85,163**	**249,083**	**233,243**	**210,723**	**182,311**	**190,641**	**205,522**

*Source: NSF, Hardman & Co Research; *IFRS 9 basis*

Cashflow

Year-end Dec (£000)	2015	2016	2017	2018*	2019E*	2020E*	2021E*
Profit/(loss) before and interest	-16,162	-5,858	-2,540	19,517	7,933	50,387	62,111
Taxation paid	-350	-1,341	-2,226	-1,164	-1,500	-4,000	-3,560
Depreciation	198	690	1,497	1,772	4,500	4,500	4,500
Share-based payments	0	0	291	1,157	1,157	1,157	1,157
Amortisation of intangibles	4,030	10,714	7,897	9,661	6,092	3,129	1,531
Fair-value unwind on acquired loan book	5,456	8,342	11,985	7,678	4,291	0	0
Loss on disposal of fixed assets	51	-363	-416	-35	0	0	0
Decrease in inventories	6	3	0	0	0	0	0
Increase in amounts receivable from customers (net of FV)	-5,394	-21,039	-54,437	-75,173	-55,277	-47,676	-60,803
Increase in receivables	-16,445	-7,737	-51	5,844	-680	0	-750
Increase in other assets				-241			
Increase in payables	19,078	-6,952	1,000	-4,132	2,000	2,000	2,000
Net cash inflow/(outflow) from op. activities	**-9,532**	**-23,541**	**-37,000**	**-35,116**	**-31,484**	**9,497**	**6,185**
Cashflow from investing activities							
Net purchase of fixed assets	-341	-3,514	-4,931	-5,915	-7,000	-4,500	-4,500
Purchase of subsidiaries	-81,111	-230,784	-16,442	0	0	0	0
Net cash outflow from investing activities	**-81,452**	**-234,298**	**-21,373**	**-5,915**	**-7,000**	**-4,500**	**-4,500**
Cashflows from financing activities							
Net finance income	70	-3,484	-7,974	-14,121	-19,712	-30,125	-33,701
Share capital issues/purchases	98,234	172,869	-1,357	-2,102	0	0	0
Net proceeds from borrowing	0	87,300	77,882	67,371	70,000	30,000	40,000
Dividends	0	-951	-4,439	-7,177	-8,436	-9,529	-9,842
Net cash inflow from financing activities	**98,304**	**255,734**	**64,112**	**43,971**	**41,852**	**-9,654**	**-3,543**
Net increase in cash and cash equivalents	7,320	-2,105	5,739	2,940	3,369	-4,657	-1,858
Opening cash and cash equivalents	0	7,320	5,215	10,954	13,894	17,262	12,605
Closing cash and cash equivalents	7,320	5,215	10,954	13,894	17,262	12,605	10,748

*Source: NSF, Hardman & Co Research; *IFRS9 basis*

Valuation

Significant upside potential on our valuation assumptions and models

Our absolute valuation techniques imply average upside potential of 214%. This has increased sharply following the share price fall associated with the bid situation and further falls, which we attribute to the Woodford overhang and the trading statement.

Summary of valuation approaches

	Implied price (p)	Upside potential
Gordon Growth Model (GGM)	79.3	194%
Discounted Dividend Model (DDM)	84.9	214%
Average absolute measures	82.1	204%
Sum-of-the-parts (SOTP)	50.9	89%

Source: Hardman & Co Research

GGM

We detailed our assumptions in our initiation note, Carpe Diem, published on 11 November 2016. Our assumptions are given in the table below.

GGM assumptions

	Base	+1% to RoE	+1% to CoE	+0.5% to G
RoE	31.5%	32.5%	31.5%	31.5%
CoE	11%	11%	12%	11%
Growth in equity	5.5%	5.5%	5.5%	6%
P/BV (RoE-G)/(CoE-G)	4.7	4.9	4.0	5.1
Discount re near-term perf.	-10%	-10%	-10%	-10%
P/NAV (x)	4.3	4.4	3.6	4.6
NAV 2020E (£m)	58.2	58.2	58.2	58.2
Valuation (£m)	247.7	257.2	209.6	267.2
Variance (£m)		9.5	-38.1	19.5
Valuation per share (p)	79.3	82.3	67.1	85.5

Source: Hardman & Co Research

DDM

Our DDM now indicates a value of 85p, unchanged as there is no change in estimates.

SOTP

We have not changed our ratings. A small divisional effect sees this value fall from 51.1p to 50.9p

SOTP valuation

Division	2020E earnings (£000)	Multiple (x)	Value (£000)	Comment
ELD	15,056	9.0	135,508	Rating at peer group average
GLD	3,418	5.0	17,091	Rating cut from 6x to 5x
LAH	5,938	8.0	47,507	Rating below MCL/PFG
Central	-5,115	8.0	-40,920	Unchanged
Group	19,298	8.2	159,185	
Value per share (p)			50.9	

Source: Hardman & Co Research

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