Begbies Traynor Group

Building service breadth, market share and margins

19 July 2022

We see two stand-out messages from strong FY22 results which were, as had already been flagged, well ahead of original market expectations.

First, they demonstrate once again that BEG can find ways to push up revenues and margins without any material assistance from higher numbers of insolvency appointments. The latter remains the major metric for the business, and total UK insolvency volumes are back to pre-pandemic levels. But a pick-up in larger, more complex (and higher value) administrations has yet to appear.

The second takeaway is reiteration that acquisitions are core to the growth strategy. Management has demonstrated its ability to identify, secure and successfully integrate substantial additions. With respect to the FY22 result, 24% out of 31% revenue growth was acquisition related and operating profit margins grew from 14.8% to 16.9%. We see this ability to steadily ratchet the performance of both divisions at the core of BEG's brand as an investment. Our forecasts are entirely organic, but management remains committed to securing further acquisitions. BEG is cash generative. It ended the period with £4.5m net cash (FY12: £3.0m) despite sizeable, deferred consideration payments.

According to the statement, FY23 has begun positively. The group is confident that it will record further growth as it builds on a solidly performing base. Approx. 70% of the business remains geared towards insolvency work, a contracyclical input, so BEG is positioned to capitalise on the UK's current economic struggles.

Valuation and forecasts based upon conservative assumptions

We regard our forecasts as conservative. As the timing of full restoration of a 'normal' UK insolvency cycle is unpredictable, we have essentially ignored both that and further acquisitions. We have, however, adjusted figures for sensitivities related to a tough economic and operating backdrop for the non-cyclical operations. Despite that, we continue to anticipate ongoing growth, further margin improvement and cash generation.

Although recovery in higher value insolvency work is a clear catalyst, we have not yet changed our assumptions in that respect. Our forecasts incorporate 4% organic revenue growth and a small increase in margins, with potential for recent and new acquisitions to continue to advance both divisions' prospects, and insolvency appointments to add further momentum over the next 12-18 months. BEG intends to capitalise on the increased breadth of its complementary professional services portfolio over the next few years.

On the back of the group's increased scale and service breadth we have increased our fair value estimate to 175p / share. That's equivalent to 18.2x FY23e PER and reflects our deliberately conservative view, confined to organic growth. At that price the shares would yield a prospective 2.1% (2.6x covered by adjusted earnings).

Summary forecasts

Year end 30 April	2020A	2021A	2022A	2023E
Revenue (£m)	70.5	83.7	110.0	114.5
Adjusted PBT £m)	9.2	11.5	17.8	19.0
Adjusted EPS (p)	5.7	6.9	9.1	9.6
Dividend per share (p)	2.8	3.0	3.5	3.7
Yield on distribution	2.1%	2.2%	2.4%	2.6%

Source: Group report & accounts and ED estimates

Company Data

EPIC	BEG
Price (last close)	144p
52 weeks Hi/Lo	156p/97p
Market cap	£219m
ED Fair Value / share	175p

Share Price, p

Source:ADVFN

Description

Begbies Traynor (BEG) is a leading UK business recovery, financial advisory and property services consultancy. It handles the largest number of corporate appointments in the UK, and principally serves the mid-market and smaller companies.

Its other services include corporate finance, valuation and sale of properties, businesses and other assets, and property consultancy, planning and management.

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Results to end April 2022

BEG alerted in May that the FY22 results would be well ahead of original market expectations. The detail is impressive. Revenues were 31% up y-o-y to £110.0m (7% organic) and adjusted PBT 55% higher, at £17.8m. Adjusted basic EPS was 32% up at 9.1p. A headline basic loss per share of 0.3p (FY21: 0.1p earnings), reflected a one-off non-cash deferred tax charge.

Increased capacity and breadth of service offering driving margins

This performance was particularly strong as UK insolvency volumes, a key influence for c 70% of group operations, were still only tracking back up towards pre-pandemic levels. The anticipated pick-up in high value administration appointments is yet to emerge (we comment briefly on the latest UK Insolvency Service data on page 4). It remains a principal pivot for *future* growth but did not stop all divisions performing well.

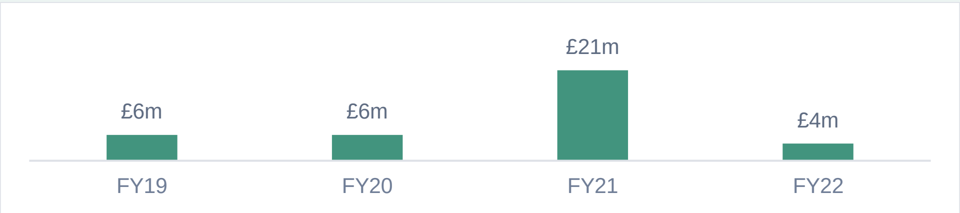
Summary results

Y/E 30 April	2022	2021
Revenue	£110.0m	£83.8m
Operating profit (before amortisation and transaction costs)	£18.6m	£12.4m
Margin	*16.9%*	*14.8%*
Adjusted PBT	£17.8m	£11.5m
Adjusted basic EPS	9.1p	6.9p
Dividend per share	3.5p	3.0p
Net cash	£4.7m	£3.0m

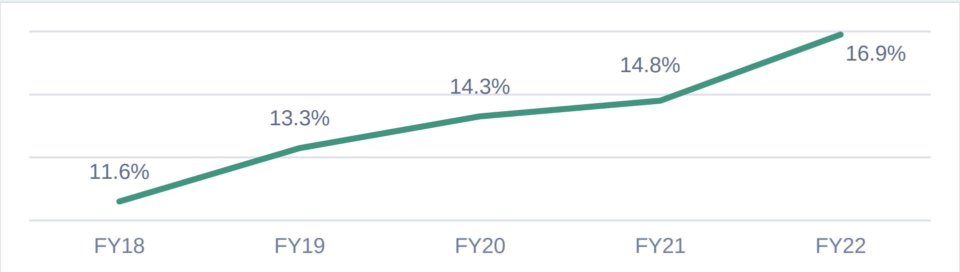
Source: BEG FY22 results

The major driver of FY22 and, indeed, prior years' growth was the impact of recent acquisitions. These materially increased the scale and breadth of the group's service offerings, and their smooth implementation helped build the operating margin to 16.9% (FY21: 14.8%). We see this as demonstration of BEG's ability to identify suitable additions, negotiate attractive terms and complete successful integrations. The chart below illustrates why we expect acquisitions to remain a core pillar of the growth strategy with the underlying benefits reflected in increases in the operating margin over the last four years.

Acquired revenue of £37m – by year of acquisition



Operating margin (Consolidated Group)



Source: BEG FY22 results

Track record and outlook

Over the last few years results have tracked increases in scale and service range. Each series of additions to the complement has been followed by a ratchet in net returns. The table below shows that the growth rate of underlying profitability at both divisions outstripped revenues. As a new subsidiary is integrated, BEG seeks to drive growth organically. It considers whether further in-fill acquisitions will help extract full potential, and capture synergies that capitalise both on the performance of existing and new components.

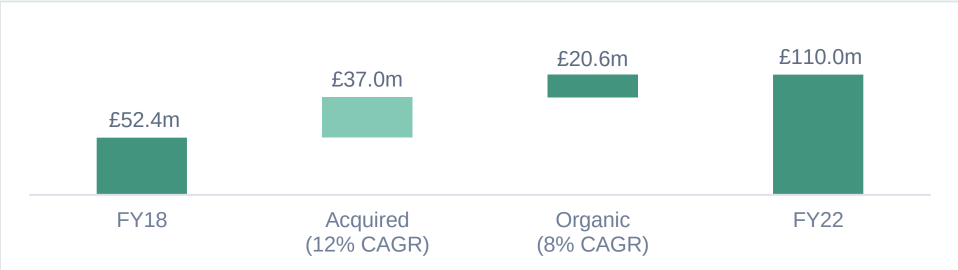
Segmental revenues and profit

	Revenue			Profit		
£m	**2022**	**2021**	**growth**	**2022**	**2021**	**growth**
Business recovery and financial advisory	81.4	59.7	36%	21.0	14.7	43%
Property advisory and transactional services	28.6	24.1	19%	4.8	3.9	23%
Shared and central costs				(7.2)	(6.2)	17%
Total	**110.0**	**83.8**	**31%**	**18.6**	**12.4**	**50%**

Source: BEG FY22 results

That's further illustrated by the combined performance over the last four years, shown below. **Revenue has grown from £52m to £110m since FY18, underpinned by 8% pa (CAGR) organic growth and 12% acquired. Over that period operating margins have increased impressively from 11.6% to 16.9%.**

Group revenues



Source: BEG FY22 results

This illustrates why BEG is committed to maintaining the momentum of its acquisition growth strategy. As revenues have built, adjusted PBT has grown from £5.6m to £17.8m, adjusted EPS from 4.0p to 9.1p.

Three acquisitions in FY22

An £8.2m net cash outflow comprised £2.9m of current year and £5.3m of prior year acquisitions. A gain of £2m was recognised within FY22 transaction costs as the value of net assets acquired exceeded the accounting value of consideration, as elements of consideration were accounted as deemed remuneration.

Additions during FY22

May 2021	**MAF Property Ltd**	£3m initial consideration (£2m cash, £1m shares, cash and debt free). Potential earn out: up to £8.75m based on profits in four-years post-acquisition	FY20 revenue £3.1m, normalised PTP £0.3m reported on same basis as the group
Oct 2021	**Fernie Greaves Chartered Survs.**	£0.25m consideration for team acquisition	
Jan 2022	**Daniells Harrison Surveyors LLP**	£1m initial consideration (£0.75m cash, £0.25m shares, cash and debt free); contingent consideration £1m. Potential earn out: up to £1.25m subject to performance in four-years post-acquisition	Reported revenue £2.1m (FY to end Mar 21), normalised PTP £0.4m reported on same basis as the group

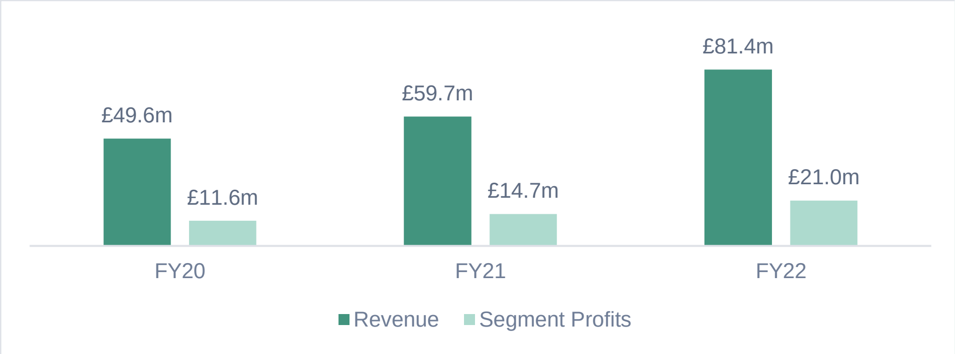
Source: BEG FY22 results

Business Recovery and Financial Advisory

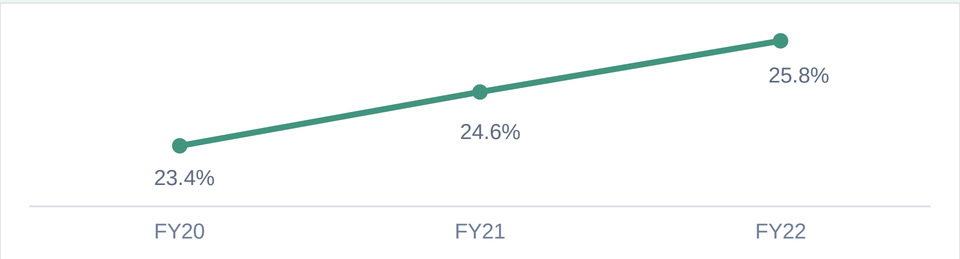
Business Recovery's FY22 performance reflects two acquisitions completed late in FY21: CVR Global and David Rubin & Partners, which made their first full contributions. This was supplemented by organic growth. As government pandemic support measures were gradually withdrawn, UK insolvency numbers returned to pre-pandemic levels and BEG increased its market share by volume. Additionally, the acquisition of finance broker MAF Finance Group in early FY21 was another spur for the division's growth.

These contributed materially to the increase in divisional revenues to £81.4m (FY21: £59.7m). Operating margins were 25.8% (FY21: 24.6%), segmental profits 43% ahead at £21.0m (2021: £14.7m).

Business Recovery & Financial Advisory - revenue & profit growth



Divisional margin



Source: BEG FY22 results

The division successfully integrated acquisitions and reported higher activity across a full range of case sizes, as it capitalised upon its extensive regional network and digital marketing expertise. It also confirmed an increase in its order book of committed future insolvency revenue to £29.5m (FY21: £28.3m), which sets it up for further growth in the current year.

UK insolvency volumes remain a key component of underlying potential and the valuation. The group remains the UK market leader (by volume of insolvency appointments) and increased its market share due to organic development from 12% to 14% during the period.

Insolvency market data

There were 1,691 registered company insolvencies (England and Wales) in June 2022. That figure was 40% above June 2021 and 15% up on the pre-pandemic number for June 2019. There were 1,456 Creditors' Voluntary Liquidations (CVLs) up 30% and 44% on the same basis.

A cyclical upturn in market volumes is firmly underway, although the precise timing of any specific component of this remains uncertain. UK government measures introduced to protect companies during the pandemic have gradually been removed and headline UK insolvency numbers returned to pre-pandemic levels during the period, well ahead of historic lows during much of the prior year.

This is undeniably positive but, so far, the 50% recorded increase in corporate insolvencies (Insolvency Service stats) nationally has been driven by liquidations. These are typically routine insolvencies of smaller companies, not the larger, more complex administrations instructions most valuable to this division.

Numbers of other types of company insolvencies, such as compulsory liquidations, were still below the pre-pandemic figure, although there were 3.6 times as many compulsory liquidations in June 2022 than in June 2021, and numbers of administrations were 2.3 times higher over the same period. This suggests that the cyclical uptick should extend to the larger, more complex administrations of most value to the group.

A possible caveat, however, is the opportunity for government intervention. It is apparent that discussions are underway with the Treasury for a new £6bn business loan scheme which is intended to be used to ease pressure on UK businesses. A longer-term successor to the Recovery Loan Scheme (RLS), which ended on 30 June, is expected to be signed off by the Treasury and the business department. The loan guarantee scheme, dubbed RLS2, will be less generous than its predecessor but still aim to provide up to £3bn pa over at least two years. Whilst such a measure is neither unreasonable nor unexpected, unintended consequences may include some distortion of the underlying trend of corporate insolvencies.

According to media coverage Whitehall sources expect the new loan scheme to be signed off by the Treasury shortly. It will provide another source of inexpensive debt to companies to help them survive the impending downturn. The first RLS offered a 70% government guarantee for loans of up to £2m to small and medium-sized firms. Anecdotally, small businesses are reporting that available and affordable credit is becoming harder to access. Although c £80bn of debt was issued under the initial Covid loan schemes, just £1bn was covered by the RLS.

The Bank of England has warned that we should expect corporate casualties in sectors exposed to soaring fuel costs and a slump in consumer spending. It sees manufacturing, transport and household goods sectors particularly likely to find their finances squeezed by the above factors and a UK recession.

Financial Advisory

The acquisition of finance broker MAF Finance Group (MAF) at the beginning of the reported period contributed to a positive result.

MAF arranges facilities for investment in new asset purchases and refinance and restructures existing facilities. Finance broking complements the group’s other advisory and transactional services and deepens its existing relationships with banks and other lenders.

The business traded well in its first year as part of the group and has grown profits in line with its earn out targets. It increased total lending arranged for clients from £150m to £330m in FY22, reflecting further development of its healthcare and renewables financing expertise and growth in asset and property finance solutions.

Its corporate finance team reported a successful year, providing buy and sell-side advice and benefitting from an active M&A market.

Property Advisory and Transactional Services

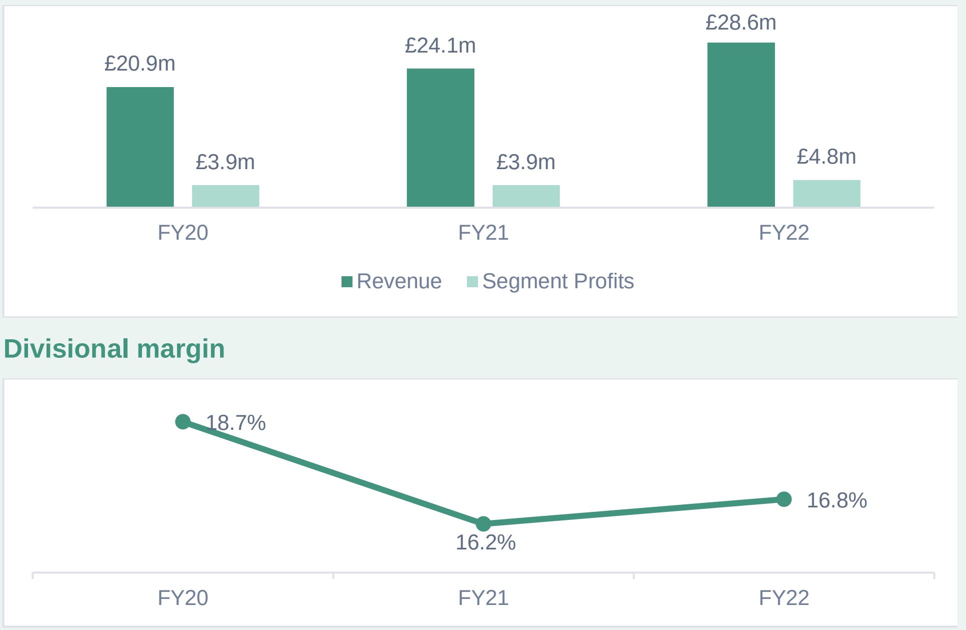
Property services also recorded higher revenue and operating margins. It continued its progressive recovery vs the lockdown affected prior period, reflected in a 19% y-o-y (10% organic) increase in revenues to £28.6m (FY21: £24.1m).

It reported organic growth within key service lines and initial contributions from acquisitions. FY21 saw greater provision of real estate valuation services to secured lenders, a direct benefit of recent investment. The operation operates a national practice which provides services to clearing banks and a broad range of specialist lenders. It reported an increased number of instructions at a higher average fee.

The Building Consultancy team grew its national offering to the education sector and other corporate clients. There has also been a sustained recovery in business sales agency, commercial property agency, valuation and auction businesses vs the lockdown impacted prior period.

The 17.8% increase in operating costs from £23.8m (2021: £20.2m) was mainly the costs of acquired businesses. Segmental profits, at £4.8m (FY21: £3.9m) reflected an increase in the divisional operating margin to 16.8% (FY21: 16.2%).

Property Advisory and Transactional Services



Source: Company, ED

Acquisitions

Two acquisitions were Daniel Harrison (January 2022) and a team from Fernie Greaves Chartered Surveyors (October 2021). Daniells Harrison is a valuation and property consultancy practice which adds the south coast of England to the group coverage. Fernie Greaves team joins the group's Sheffield team and extends its coverage in South Yorkshire.

This division has grown substantially since its creation via an initial acquisition (Eddisons) in December 2014. Annual revenue has since increased from c £13m to over £30m (current annualised run rate), with profitability improving.

Outlook and valuation metrics

The statement included a confident outlook which anticipates that revenues will build organically on a strong base. UK insolvency market volumes have returned to pre-pandemic activity levels and are expected to increase further this year and beyond. We expect that growth to be enhanced by further strategic acquisitions.

The advisory team has confirmed an encouraging pipeline of organic growth and acquisition opportunities, which points to further development of its business during the current financial year. The property division anticipates further progress as it develops its broad services portfolio via organic growth and acquisitions. It completed the purchase of Budworth Hardcastle in June 2022.

A strong balance sheet and cash generation underpins capacity for both acquisitions and organic growth initiatives.

The group ended FY21 with £4.7m net cash (FY21: £3.0m) despite £8.2m of acquisition and deferred consideration payments, and £4.6m of dividends. It has proposed a 17% increase in the total FY22 dividend, ahead of our forecasts.

Cash generation

£m	2022	2021
Free cash flow	**14.0**	**12.3**
Net proceeds from share issues	0.5	20.9
Acquisition and deferred consideration payments	(8.2)	(23.9)
Dividends	(4.6)	(3.6)
Increase in net cash	**1.7**	**5.7**
Net cash	4.7	3.0

Source: BEG FY22 results

Forecasts

We have forecast a relatively conservative 4% pa revenue growth for the next two years. That ignores contributions from new (unannounced) acquisitions and does not incorporate any material recovery in the kind of larger, complex, and profitable insolvency appointments the group seeks. That simply takes a view on the inherently uncertain timing of that cyclical recovery, which we still anticipate is on its way.

Over the last four years BEG has achieved steady growth, without compromising its underlying financial strength. It recommended a 17% increase in the total dividend for FY22 to 3.5p/share (FY21: 3.0p).

That is its fifth consecutive year of dividend growth, a period during which it has also steadily increased earnings cover.

Valuation metrics

Y/e 30 Apr	Net cash /(debt) £m	Adj. Basic EPS (p)	Dividend (p)	Dividend cover (x)
FY18	(7.5)	4.0	2.4	1.7
FY19	(6.0)	4.8	2.6	1.8
FY20	(2.8)	5.7	2.8	2.0
FY21	3.0	6.9	3.0	2.3
FY22	4.7	9.1	3.5	2.6

Source: BEG financial statements

FINANCIALS

Consolidated statement of comprehensive income					
Y/E 30 April, £m	**2019**	**2020**	**2021**	**2022**	**2023E**
Revenue	**60.1**	**70.5**	**83.8**	**110.0**	**114.5**
Direct costs	(34.3)	(40.3)	(48.3)	(62.2)	(64.7)
Gross profit	**25.8**	**30.2**	**35.6**	**47.8**	**50.3**
Other operating income	0.4	0.4	0.2	0.2	0.2
Administrative expenses	(22.2)	(26.7)	(32.9)	(43.1)	(45.0)
Operating profit	**4.0**	**3.9**	**2.8**	**4.9**	**5.5**
Adj. Operating profit (before amortisation and transaction costs)	**7.6**	**10.1**	**12.4**	**18.6**	**19.8**
Transaction costs	(1.2)	(3.2)	(6.5)	(8.2)	(9.0)
Amortisation of intangible assets arising on acquisitions	(2.4)	(3.1)	(3.1)	(5.5)	(5.3)
Operating profit	**4.0**	**3.9**	**2.8**	**4.9**	**5.5**
Finance costs	(0.5)	(1.0)	(0.9)	(0.8)	(0.8)
Profit before tax	**3.5**	**2.9**	**1.9**	**4.0**	**4.7**
Adjusted PBT	**7.1**	**9.2**	**11.5**	**17.8**	**19.0**
Tax	(1.1)	(2.0)	(1.8)	(2.7)	(1.0)
Profit after tax	**2.4**	**0.9**	**0.2**	**(0.5)**	**3.7**
Earnings per share					
Adjusted EPS - basic	4.8p	5.7p	6.9p	9.1p	9.6p
- diluted	4.7p	5.7p	6.7p	8.8p	9.3p

Source: Group financial statements, ED estimates

Balance sheet

Y/E 30 April, £m	2019	2020	2021	2022	2023E
Non-current assets					
Intangible assets	59.4	59.4	77.9	75.3	75.3
Property, plant and equipment	1.8	1.8	2.1	2.0	2.5
Right of use assets	0.0	7.0	7.5	5.5	5.5
Trade and other receivables	3.2	4.6	4.0	4.2	5.0
	64.4	**72.8**	**91.4**	**86.9**	**88.3**
Current assets					
Trade and other receivables	32.7	36.5	44.9	49.7	52.0
Cash and cash equivalents	4.0	7.2	8.0	9.7	7.0
	36.7	**43.7**	**52.8**	**59.4**	**59.0**
Total assets	**101.0**	**116.6**	**144.3**	**146.3**	**147.3**
Current liabilities					
Trade and other payables	(22.7)	(22.2)	(32.9)	(37.2)	(37.0)
Current tax liabilities	(2.0)	(1.9)	(2.6)	(1.8)	(2.0)
Lease liabilities	0.0	(2.2)	(3.0)	(1.7)	(1.5)
Provisions	(0.6)	(0.9)	(0.6)	(1.5)	(1.5)
	(25.2)	**(27.2)**	**(39.0)**	**(42.2)**	**(42.0)**
Net current assets	**11.4**	**16.5**	**13.8**	**17.2**	**17.0**
Non-current liabilities					
Trade and other payables	0.0	0.0	0.0	0.0	0.0
Lease liabilities	0.0	(6.1)	(5.8)	(4.6)	(4.0)
Borrowings	(10.0)	(10.0)	(5.0)	(5.0)	(5.0)
Provisions	(0.8)	(1.9)	(2.6)	(2.0)	(2.0)
Deferred tax	(5.3)	(5.7)	(5.5)	(8.0)	(8.0)
	(16.1)	**(23.8)**	**(19.0)**	**(19.6)**	**(19.0)**
Total liabilities	(41.3)	(51.0)	(58.0)	(61.8)	(61.0)
Net assets	**59.7**	**65.6**	**86.3**	**84.5**	**86.3**

Source: Group financial statements, ED estimates

Consolidated cash flow statement					
Y/E 30 April, £m	**2019**	**2020**	**2021**	**2022**	**2023E**
Cash flows from operating activities					
Cash generated by operations	8.0	4.7	16.2	14.2	13.6
Income taxes paid	(1.4)	(2.2)	(2.3)	(3.6)	(6.3)
Interest paid on borrowings	(0.5)	(0.4)	(0.3)	(0.3)	(0.4)
Interest paid on lease liabilities	(0.5)	(0.5)	(0.5)	(0.5)	(0.5)
Net cash from operating activities	**5.7**	**1.7**	**13.0**	**9.8**	**6.5**
Investing activities					
Purchase of intangible fixed assets	(0.2)	(0.7)	(1.0)	(0.9)	0.0
Purchase of property, plant and equipment	(0.8)	(0.1)	(0.3)	(0.2)	(0.8)
Deferred consideration payments	0.0	(0.7)	(0.2)	(0.0)	(0.0)
Acquisition of businesses (net of cash acquired)	(1.8)	(3.0)	(22.0)	(0.3)	(0.8)
Cash from acquired businesses	3.4	3.4	1.5	0.4	0.0
Net cash used in investing activities	**0.6**	**(1.1)**	**(22.0)**	**(0.9)**	**(1.5)**
Financing activities					
Dividends paid	(2.6)	(3.2)	(3.6)	(4.6)	(5.6)
Net proceeds on issue of shares	0.0	7.8	20.9	0.5	0.0
Repayment of obligations under leases	0.0	(1.9)	(2.7)	(3.2)	(2.0)
Proceeds on issue of SIP scheme shares	0.0	0.0	0.0	0.0	0.0
Repayment of loans	(1.0)	0.0	(5.0)	0.0	0.0
Net cash used in financing activities	**(5.8)**	**2.7**	**9.7**	**(7.2)**	**(7.6)**
Net increase (decrease) in cash and cash equivalents	0.5	3.2	0.7	1.7	(2.7)
Cash at beginning of year	**3.5**	**4.0**	**7.2**	**8.0**	**9.7**
Cash at year end	**4.0**	**7.2**	**8.0**	**9.7**	**7.0**

Source: Group financial statements, ED estimates

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