

15 August 2022

Record sales and profits in FY2022

A 13% increase in net sales revenue to a record £154.2m, a 41% increase in EBITDA to £18.8m (also a record) and an underlying 1.3x net debt/EBITDA ratio were notable features of a pre-close trading update released by UPGS today. Moreover, FY2023 appears to have started well. With strong momentum in both reported sales and profits, as well as significant tangible progress within group operations, we maintain our fair value assessment of 250p per share.

While UPGS's reported sales revenue growth benefited significantly from the acquisition of Salter in June 2021, the company's 1% organic growth (which lapped a tough comparison in FY2021 when houseware sales benefited from COVID19 related lockdowns) should be seen positively. In addition, the company continues to make important progress in the supermarket channel where its success as a brand manager is arguably more critical.

UPGS's profitability benefited not only from the acquisition of Salter but also from improved margins, which we infer to be a combination of higher gross margins and a better overheads performance. Key financials of the Salter acquisition were highlighted in our 25 June 2021 report [UPGS acquires UK's oldest housewares brand](#). Importantly, the company remains committed to operating at best practice in terms of cost management.

Supermarkets were reported to be the stand-out performer of UPGS's four strategic pillars of distribution. But as the well-recognised supply chain headwinds facing importers of manufactured consumer goods ease, **scope for online to return to growth should improve**: this is consistent with comments from our 22 June 2022 report [Reinforcing the online offering](#).

UPGS boasts significant underlying business momentum both in terms of its brands and an opportunity to scale up the business. This is reflected in the company's strong start to the year and confidence in meeting market expectations in FY2023, as well as in the significant headroom for growth offered by Online and International.

Undervaluation

The current share price fails to reflect three salient growth drivers of the business, in our view. These include UPGS's ability both to manage and acquire key brands, the development of more supermarket and online business and its international opportunity. The company's proven ability to cope with external headwinds should also be noted.

We base our 250p fair value on an FY2023 EV/sales ratio of 1.5x and 12x EV/EBITDA.

Key Financials					
Year to 31st July	2019A	2020A	2021A	2022E	2023E
Revenue (£'000)	123,257	115,684	136,367	154,200	163,452
Revenue change (%)	40.8%	-6.1%	17.9%	13.1%	6.0%
EBITDA (£'000) (adj)	10,720	10,363	13,291	18,800	20,176
EPS adjusted (p)	8.3	8.3	11.1	14.5	15.3
DPS (p)	4.1	4.0	5.0	7.3	7.7
EV/EBITDA (x)	12.3	12.7	9.9	7.0	6.5
P/E ratio (x)	15.1	15.2	11.3	8.7	8.2
Yield (%)	3.2%	3.1%	4.0%	5.8%	6.1%

Source: ED estimates, Company historic data

Company Data

EPIC	UPGS
Price (last close)	126p
52 weeks Hi/Lo	230p/105p
Market cap	£107m
ED Fair Value / share	250p

Share Price, p



Source: ADVFN

Description

UP Global Sourcing Holdings plc (UPGS) develops new, innovative concepts and brings professional, sought-after products to the mass market.

Their offices span two continents, with headquarters in the UK, a sourcing office and showroom in Guangzhou, as well as a showroom in Germany.

Key owned brands include **Salter, Beldray, Progress, Kleeneze, Petra and Intempo**. The company also markets non-electrical Russell Hobbs products under licence.

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UPGS's trading update confirms that the company should be well positioned to resume its underlying pace of organic sales growth – i.e. around 6% - in FY2023. We take this view on the company's combination of strong "feel good" brands, success in the faster growing distribution channels of online and supermarkets and meaningful progress internationally. In FY2022 UPGS delivered record levels of both sales and profitability.

Sales growth

UPGS's sales revenue increased by 13% to a record £154.2m in FY2022 which was largely attributable to the acquisition of Salter. Underlying organic growth was 1% as the company lapped an unusually strong 18% growth rate in FY2021 when sales benefited significantly from COVID19 related lockdowns. Excluding Salter, sales grew at a compound annual rate of 5% in the five years to FY2022 despite a challenging start year in FY2017 when sales spiked by 39%.

We summarise today's trading update's highlights in Figure 1. Full Year 2022 financial results are due for release on 3 November 2022.

Figure 1 - UPGS FY2022 trading update highlights

All figures in £m	FY2021	FY2022	Change
Revenues	136.4	154.2	13%
Underlying EBITDA	13.3	18.8	41%
Underlying EBITDA margin	9.8%	12.2%	2.4 percentage points
Pre-tax profit	11.2	15.8	42%
Net bank debt/underlying EBITDA	1.4x	1.3x	-0.1x improvement

Source: Company data and ED calculations

Profitability

UPGS's profit growth benefited from both the Salter acquisition and underlying efficiencies within the business. In our 21 June 2022 report, we estimated that incremental underlying EBITDA and pre-tax profits from the ownership of Salter outright would be £4.6m and £4.0m respectively. **Both profit measures increased by more than these amounts.**

The company's reduction in net debt to EBITDA ratio **from 1.4x to 1.3x** is consistent with a commitment to converting underlying profits into free cash flow. The strength of UPGS's financial position is highlighted by maintenance of comfortable levels of headroom within its banking facilities. These improved from £16.2m on 31 July 2021 to £17.8m at the end of the latest financial year.

Well positioned for growth

Strategic pillars

UPGS's transition from being a sourcing to a brand ownership company has been a consistent theme of our recent published reports about the company. By acquiring brands, notably outright ownership of Salter and the purchase of Petra, and managing the existing portfolio better, the company has positioned itself more effectively to grow in the competitive and arguably more "level playing field" for brands distribution channels of supermarkets and online.

Today's statement described sales growth in supermarkets as particularly strong. The channel is now UPGS's largest within its four strategic pillars, having superseded discounters in FY2022.

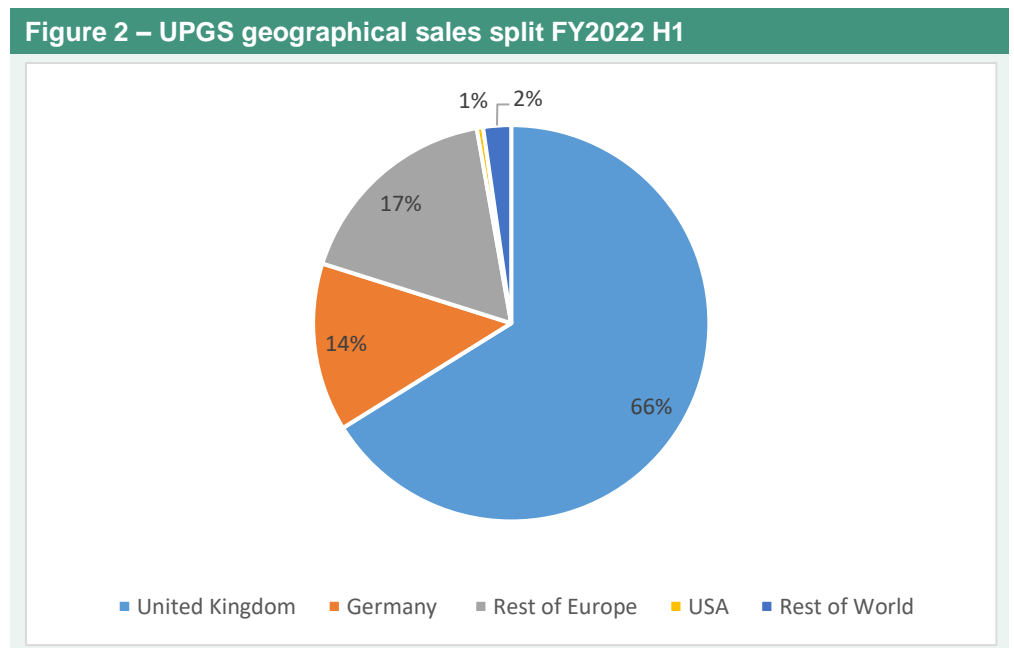
Online remains an important target area for growth. The stated target is for the channel to represent 30% of group sales revenue. On 22 June 2022 the company announced that it had bought the Salter.com domain name and was in the process of implementing a significant re-vamp of the Beldray.com website.

International

In UPGS's FY2022 interim results statement, released on 29 April 2022 and commented on in our report [Shareholder value at its core](#), the company stated that international sales revenue was equivalent to 34% of sales, compared with 31% a year earlier. Germany recorded a sharp increase in importance from 10% to 14% of sales revenue and represents the most significant opportunity based on the size of its economy and the relatively recent acquisition of the Petra kitchenware brand.

Furthermore, the appointment of Simon Hathway as an external adviser to the European business on 14 June 2022 should be seen, in our view, as a significant step forward for the company's international business given that he is an experienced independent adviser, consultant and non-executive director with over 25 years' experience in international retail.

The geographical split of UPGS's sales revenue in FY2022's H1 is summarised in Figure 2.



Source: Company data

Financials and valuation

Relative valuation

A relative valuation for UPGS based on a peer group of companies is shown in Figure 3. The company trades in line with this peer group on both EV/sales and EV/EBITDA but at a meaningful discount in terms of both P/E and dividend yield. UPGS's ability to generate cash and reward shareholders with a 50% dividend pay-out ratio is an important supplement to the investment case, in our view. **We base our 250p fair value assumption on an FY2023 EV/sales ratio of 1.5x and 12x EV/EBITDA.**

Figure 3 - Relative valuation

	Share price (p)	Mkt cap £m	Net debt £m	EV £m	Sales 2022 £m	EV/Sales (x)	EBITDA 2022 £m	EV/EBITDA (x)	EPS 2022 (p)	P/E 2022 (x)	DPS 2022 (p)	Yield (%)
Accrol (ACRL)	26	83	35	118	159	0.7	9.0	13.2	0.3	94.7	0.1	0.3%
Gear4Music (G4M) *	158	33	19	52	166	0.3	11.9	4.4	14.5	10.9		
Luceco (LUCE)	100	154	45	199	216	0.9	33.1	6.0	12.3	8.1	6.1	6.1%
Portmeirion (PMP)	403	55	1	56	110	0.5	14.0	4.0	56.6	7.1	18.8	4.7%
Procook (PROC)	42	42	20	62	69	0.9	11.9	5.2	3.5	12.0	1.5	3.6%
UPGS (UPGS)	126	107	24	132	154	0.8	18.8	7.0	14.5	8.7	7.3	5.8%
Warpaint (W7L)	122	93	-4	89	58	1.5	9.4	9.5	8.8	13.8	6.4	5.3%
Average						0.8		7.0		22.2		4.3%
Share prices are at 12 August 2022 close		* Refers to FY2023 data										

Source: ADVFN (prices), MarketScreener (debt, sales, EBITDA), Stockopedia (EPS, dividends) and Equity Development estimates (UPGS forecasts)

Financial forecasts

We maintain our belief that the underlying sales growth rate for UPGS is 6% in our forecasts, with due regard for external inflationary influences. However, given that the £154m outcome in FY2022 compared with our most recent forecast of £159m, we have adjusted our numbers in FY2023 and FY2024 to grow sales from a lower base.

We have also altered the basis of our earnings per share calculation to exclude the 4.1m shares held by the UPGS Employee Benefit Trust, which we treat as treasury shares in these forecasts.

Our income statement, balance sheet and free cash flow projections appear in Figures 4, 5 and 6 respectively which include actual figures for sales revenue, adjusted EBITDA, adjusted pre-tax profits and inferred net debt in FY2022.

Figure 4 - Income statement

All figures in £'000s 31st July year end	2020A	2021A	2022E	2023E	2024E
Revenue	115,684	136,367	154,200	163,452	173,259
% Change in revenue	-6.1%	17.9%	13.1%	6.0%	6.0%
Gross profit	26,600	30,231	38,153	40,606	43,215
Gross margin	23.0%	22.2%	24.7%	24.8%	24.9%
EBITDA - adjusted	10,363	13,291	18,800	20,176	21,680
EBITDA margin - adjusted	9.0%	9.7%	12.2%	12.3%	12.5%
Net financial expense	-753	-518	-1,000	-1,102	-978
Pre-tax profit - adjusted	8,163	11,150	15,800	17,024	18,602
Taxation	-1,747	-2,195	-3,435	-3,958	-5,069
Tax rate (%) - adjusted	21.4%	19.7%	21.7%	23.3%	27.3%
Net income - adjusted	6,504	8,727	12,365	13,066	13,533
EPS - basic adjusted (p)	8.3	11.1	14.5	15.3	15.9
Dividend per share (pence)	4.0	5.0	7.3	7.7	7.9

Source: ED estimates, Company historic data

Figure 5 - Balance sheet

All figures in £'000s

31st July year end	2020A	2021A	2022E	2023E
Assets				
Intangible assets	86	27,253	27,253	27,253
Goodwill		9,676	9,660	9,644
Property, plant and equipment	5,065	5,719	5,235	4,761
Deferred tax	106			
Total non-current assets	5,257	42,648	42,148	41,658
Inventories	16,022	21,674	25,500	27,380
Trade and other receivables	18,495	26,544	34,600	37,026
Derivatives	53	384		
Current tax		62		
Cash and cash equivalents	329	133	133	133
Total current assets	34,899	48,797	60,233	64,539
Total assets	40,156	91,445	102,381	106,197
Liabilities				
Share capital	205	223	223	223
Share premium account	2	14,334	14,334	14,334
Employee benefit trust reserve	-2,155	-2,152	-2,152	-2,152
Share-based payment reserve	796	1,024	1,252	1,480
Hedging reserve and other reserves	-961	-162	578	572
Retained earnings	15,527	18,788	26,272	32,812
Total equity	13,414	32,055	40,507	47,269
Trade and other payables	17,614	29,451	29,000	28,840
Derivative financial instruments	1,342	220		
Current tax	280			
Borrowings	3,903	7,951	14,757	13,711
Lease liabilities	710	771		
Deferred consideration		990	990	
Total current liabilities	23,849	39,383	44,747	42,551
Borrowings (negative => cash)	89	10,847	9,847	9,847
Deferred tax		6,147	6,000	6,000
Deferred consideration		983		
Lease liabilities	2,804	2,030	1,280	530
Total non-current liabilities	2,893	20,007	17,127	16,377
Total equity and liabilities	40,156	91,445	102,381	106,197

Source: ED estimates, Company historic data

Figure 6 - Free cash flow

All figures in £'000s

31st July year-end	2020A	2021A	2022E	2023E
Profit for the period	6,615	7,313	12,137	12,838
Adjustments for:				
Finance costs (net)	753	518	1,000	1,102
Income tax expense	1,747	2,195	3,435	3,958
Depreciation and impairment	1,417	1,563	1,984	2,034
Amortisation	12	16	16	16
Loss on disposal of a current asset	18	44		
Derivative financial instruments	324	-678		
Share based payments	267	228	228	228
Income taxes paid	-2,255	-2,566	-3,373	-3,958
Operating free cash flow	8,898	8,633	15,427	16,218
Working capital adjustments				
(Increase)/decrease in inventories	4,377	-368	-3,826	-1,880
Decrease/(increase) in receivables	150	-8,091	-8,056	-2,426
(Decrease)/increase in payables	2,339	9,031	-451	-160
Total	6,866	572	-12,333	-4,466
Net cash from operations	15,764	9,205	3,094	11,752
Cash flows used in investing activities				
Acquisition of a business		-30,578	-1,000	-1,000
Purchase of intangible assets				
PP&E	-601	-2,263	-1,500	-1,560
Proceeds from P, P & E disposals	12	3	3	4
Finance income				
Repayment of lease liabilities			-750	-750
Total	-589	-32,949	-3,247	-3,306
Free cash flow before financing	15,175	-23,744	-153	8,446
Interest paid	-698	-335	-1,000	-1,102
Free cash flow before dividends etc	14,477	-9,729	-1,153	7,344
Dividends paid	-2,307	-4,409	-4,653	-6,298
Purchase of own shares (EBT)	-506			
Free cash flow after dividends etc	11,664	-14,136	-5,806	1,046

Source: ED estimates, company historic data



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