Finance and Credit Services

Source: Refinitiv

Market data

EPIC/TKR	**APP**
Price (p)	23.0
12m high (p)	46.3
12m low (p)	21.5
Shares (m)	186.3
Mkt cap (£m)	42.9
EV (£m)	42.9
Free float*	99.91%
Country of listing	UK
Market	AIM

*As defined by AIM Rule 26

Description

APP facilitates pre-payment, gifts and engagement with staff and customers through many of the country's most popular voucher, card and e-code products. These can be spent online, or at 24,000 retail sites. The model is increasingly digital.

Company information

CEO	Ian O'Doherty
CFO	Tim Clancy
Chair	Laura Carstensen
NEDs	John Gittins, Sally Cabrini

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www.appreciategroup.co.uk

Key shareholders

Schroders	10%
Premier Miton	9%
Artemis	9%
SFM UK Management LLP	8%
Unicorn	7%
Investec WM	5%
Four other holders 3%+	15%

Diary

Jan22	Trading update

Analyst

Mark Thomas 020 3693 7075
mt@hardmanandco.com

APPRECIATE GROUP

Interim results: solid progress, digital delivering

We reviewed Appreciate's (APP) business model in our initiation, *Solid core + digital disruption = unique model*, published on 1 September. On 23 November, APP released its interim results, reporting a modest seasonal loss, in line with the nature of its business. The key takeaways were i) continued progress in the rollout of the digital model, including both distribution and efficiency, ii) reversion to more normal customer patterns of redemption and in larger corporate client behaviour, and iii) growth in redemption partners, especially in hospitality, leisure and food. The Xmas Savings business is being reinvigorated. The full-year outlook is in line with expectations.

- **Digitalisation:** With these results, not only did digital distribution show strong growth, but efficiency benefits were also visible. APP expects falling administration costs, despite inflationary pressures. Fewer staff were required to handle peak volumes, and complaints are down. The peak of investment has passed.
- **Outlook:** APP sees the full year in line with expectations. Against our pre-results forecasts, billings are down, due to a slightly slower-than-anticipated start at PayPoint, and APP choosing not to renew a low-margin contract, offset by the lower costs. As shown below, a strong profit rebound is expected in FY22.
- **Valuation:** We use a range of valuation approaches, including a Gordon Growth Model (GGM), a Discounted Dividend Model (DDM) and a peer comparison. On the assumptions we outline later in the report, the average indicative valuation is 60p. As APP is a growing business, there is upside potential moving forward the base year.
- **Risks:** FY21/22 was a challenging period for the Xmas Savings business, as lockdown restrictions impacted agent activity. The digital model is positive, but it is still being developed, and the transition is not risk-free. Anything adversely affecting redemption/distribution relationships would be negative. There is a sensitivity to macroeconomics and near-term customer behaviour.
- **Investment summary:** Combining a profitable core, decades of experience, especially in managing key partnerships, and the latest technology give APP a unique fintech strategy. It is at the early stages of the transition to a digital model but has already attracted new partners like PayPoint. Comparable models are growing explosively and are on higher valuations. The accounting rules are unhelpful to understanding the business. Any fundamental strategic change introduces risk, and there is some economic sensitivity.

Financial summary and valuation

Year-end Mar (£000)	2019	2020	2021	2022E	2023E	2024E
Billings	426,901	419,857	406,500	388,238	420,000	448,000
Revenue	110,394	112,724	106,805	99,700	103,500	106,100
Gross profit	31,277	32,822	24,336	29,139	31,050	33,952
Gross profit margin	28%	29%	23%	29%	30%	32%
Admin./dist. costs as % rev.	72%	71%	77%	71%	70%	68%
Pre-tax profit	11,304	7,700	1,253	6,793	9,347	12,007
Net cash	34,563	29,632	31,415	16,959	3,684	4,320
Shareholders' funds	14,025	16,710	18,347	17,710	20,666	24,663
EPS (p)	4.77	2.96	0.46	2.92	4.01	5.15
DPS (p)	3.20	0	1.00	1.50	2.00	2.75
P/E (x)	4.8	7.8	50.4	7.8	5.7	4.5
Dividend yield	13.9%	0.0%	4.3%	6.5%	8.7%	12.0%

Source: Hardman & Co Research

1HFY22 results summary

Financial highlights

- Billings were up 20% to £118.2m (1H21: £98.8m), in line with 1H20 (£120.2m) – the last period of normal trading prior to the pandemic. Corporate billings rose 21% to £80.5m (1H21: £66.6m, 1H20: £80.1m). Consumer billings were up 17% to £37.7m (1H21: £32.3m, down 6% on 1H20's £40.1m).

- Revenue rose 50% to £41.0m (1H21: £27.4m), benefiting from redemptions – which had been deferred as a result of lockdowns – being realised, as anticipated. Revenue was 24% higher than the pre-pandemic period (1H21: £33.2m). Corporate revenue rose 46% to £27.8m (1H21: £19.0m, 14% above 1H20's £24.3m), while consumer revenue, benefiting more from deferred redemptions, was up 59% to £13.2m (1H21: £8.3m, +48% from 1H20's £8.9m).

- There was a significant reduction in the pre-tax loss, to £2.0m (1H21: £6.2m loss, 1H20: £1.3m loss). 1H21 included £0.5m of one-off pension reorganisation costs.

- The proposed interim dividend is 0.6p (1H21: 0.4p).

- Cash balances, including cash held in trust, at 30 September 2021, were £207.1m (1H21: £227.3m). Free cash was £2.9m (1H21: £24.9m) – this is typically the low point in the cash cycle, and also reflected growth in regulatory billings (which require customer monies to be held in trust until redemption). Free cash at 31 October 2021 was £34.0m (31 October 2020: £39.1m), as monies held in trust were released as the Xmas Savings product was dispatched.

Strategic progress

- Digital helped drive i) operational improvements, with reduced use of overtime and seasonal temporary staff during the peak trading period, ii) digital billings, which were up 15.7% to £28.0m (1H21: £24.2m), while paper billings fell from 19.2% to 14.5% within the product mix, and iii) strengthened marketing, with greater use of insight and digital marketing to support further growth in digital products.

- APP continued to build awareness through PayPoint's 28,000 UK retailers and customers in the early stages of this relationship.

- Implementation of ongoing strategic plans included i) launching the first campaign specifically promoting Love2shop, the brand that underpins all Appreciate's products, ii) 54 new redemption partners, mainly in hospitality, leisure, and food, iii) reinvigorating the Xmas Savings product with enhanced advertising, marketing and engagement with agents, iv) the Enterprise Resource Planning (ERP) programme implementation phase, planned for January 2022, avoiding any disruption during peak trading, and v) further ESG commitments.

Outlook

APP has seen the usual seasonal increase in demand. 3QFY22 billings up to 21 November were £37.0m (3Q21: £39.4m, 3Q20: £43.9m), with an improvement in November to a level that is closer to the previous years. Billings are below prior-year levels, due largely to the decision not to supply low-margin business to a direct competitor (billings would have been up 3% in 3Q21 and down 2% in 3Q20 on a like-for-like basis). Some uncertainty persists as we emerge from the lockdowns. The full-year outlook is line with company expectations.

Key theme (1): digitalisation

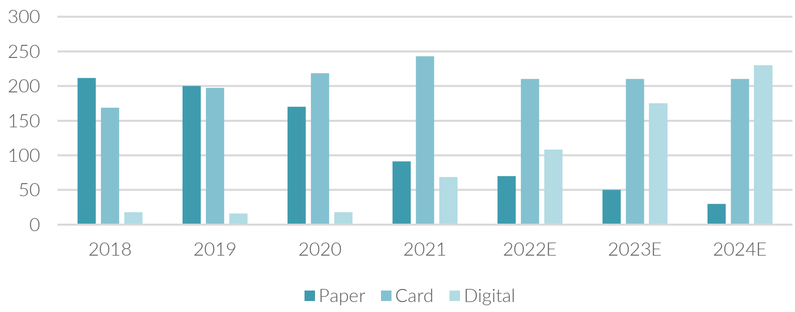
Fundamental transformation of model to a digital one reviewed in detail in our initiation

We reviewed the impact of digitalisation on APP's customers, product range, marketing and distribution, management information, redemption, efficiency, cyber security, valuation and the costs and risks in transformation in our initiation. We also reviewed it in the context of a European comparator, which is operating in line with APP's vision. The fundamental transformation after by a successful implementation of a digital strategy cannot be understated. With these results, we learnt:

Digital billings up 15.7%, despite lower free school meals and physical products available for whole period

- Digital billings increased by 15.7%, from £24.2m to £28.0m. This has been achieved despite reduced digital billings in FY22 through the free school meals initiative and a period, in FY21, when physical products could not be dispatched, leaving largely digital-only options available to customers. In 1H22, digital accounted for 24% of total billings, compared with 7% in FY20. Over the two years, paper billings saw a large fall (39% to 14%), with card billings rising from 54% to 62% over the same period.

Billings by format (£m)



Source: Appreciate, Hardman & Co Research

32% rise in HSV traffic

- Digital marketing contributed to the 32% increased traffic to the High Street Vouchers (HSV) website. We understand that the latest campaign to enhance the Love2Shop brand will include digital marketing. This should support the 2022 Xmas Savings launch (next month), using closely managed TV spend and more targeted digital expenditure.

Upgrading interfaces with redemption partners and customers

- APP's partnership strategy is designed to tailor into merchants' digital offerings directly. This is not only to enhance the end-customer experience but, by upgrading its application programming interface (API) links, APP can also be a more attractive choice for redemption partners. In essence, more of the processing can be automated if the partner and APP's technology talk to each other, and, with these results, APP highlighted the transition of its Flexecode delivery to Digital Order API. Digital is also helping to improve the customer experience, as APP knows who the recipients are and can send them notifications to use the gift card, whereas, with physical cards and vouchers, they do not know who the recipients are.

Falling costs expected, despite inflationary pressures

- With these results, APP announced that it expected administration costs to reduce to c.£20m for the current financial year (FY21: £21.1m) and to c.£19m next year. Operational improvements have led to a 13% reduction in seasonal temporary staff to handle peak volumes and a 30%+ fall in customer care calls. Most of the ERP platform investment (implementation January 2022) has been made over the past three years – so capitalised expenses are expected to fall. APP will continue to invest in its platform and develop digital products, etc., but not at the same pace as has been required to transform the business since 2018.

Theme 2: recovery from pandemic

APP faced multiple issues from the pandemic – some positive (more companies using gift cards to reward staff, instead of Xmas parties, the billings for free school meals), but a number were negative (deferred redemption, Xmas sale agents unable to meet customers, constrained corporate budgets, lockdowns in some key sectors). The table below shows that there has been some improvement through the year, but we understand that there has been considerable volatility. Billings were also affected by the supply to terminate the low-margin competitor relationship – so billings fell in October, although there was an improvement in November, to a level that is closer to that of the previous years.

Billings – corporate and gifting only (£m)

	1Q	2Q	1H excluding free school meals scheme	1H reported
FY22	£39.0m	£79.2m	£109.9m	£118.2m*
FY21	£21.3m	£77.5m	£88.5m	£98.8m*
FY20	£41.4m	£78.8m	£120.2m	£120.2m
% diff (FY22 vs. FY21)	+83.1%	+2.2%	+24.2%	+19.6%
% diff (FY22 vs. FY20)	-5.8%	+0.5%	-8.6%	-1.7%

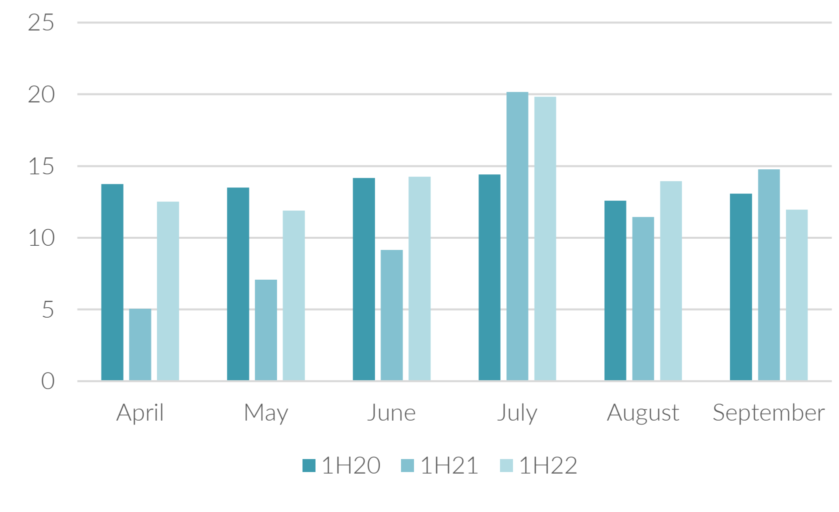
**Includes billings through free school meal scheme – 1HFY2021: £10.3m, 1H FY2022: £8.3m.*

Source: Appreciate interim release, Hardman & Co Research

Monthly billings broadly similar to 1H20

The chart below shows the monthly billings. In broad terms, 1H22 was similar to the pre-pandemic 1H20, although there has been a degree of greater volatility between the months. This volatility makes it harder to be certain of trends. As noted earlier, October was a weak month, but November has been in line with FY20.

Billings (excluding Xmas Savings) by month (£m)

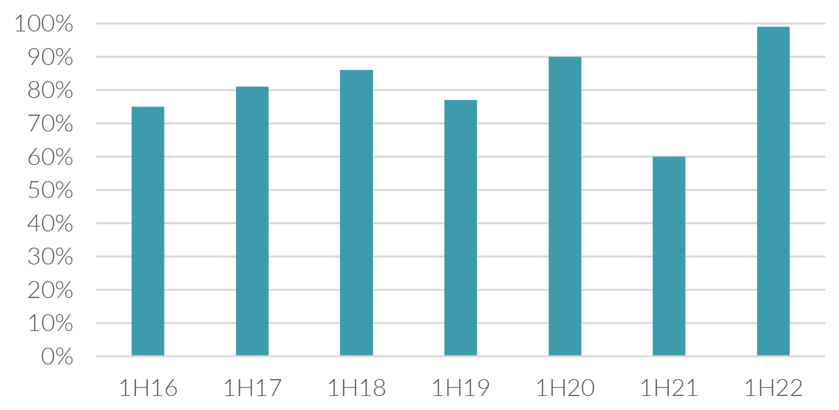


Source: Appreciate, Hardman & Co Research

Large corporates swifter to recover than smaller ones

Billings from medium to larger clients have returned to pre-COVID-19 levels, with recurring business of c.99% from clients whose orders were more than £5k (see table below). Billings from smaller clients are taking longer to recover – perhaps reflecting the degree of management stretch that the pandemic has imposed on smaller businesses. The group continued to enjoy good levels of new business, above the level seen prior to the pandemic.

Recurring business (%) - billings from clients ordering >£5K in current year and prior year



Source: Appreciate, Hardman & Co Research

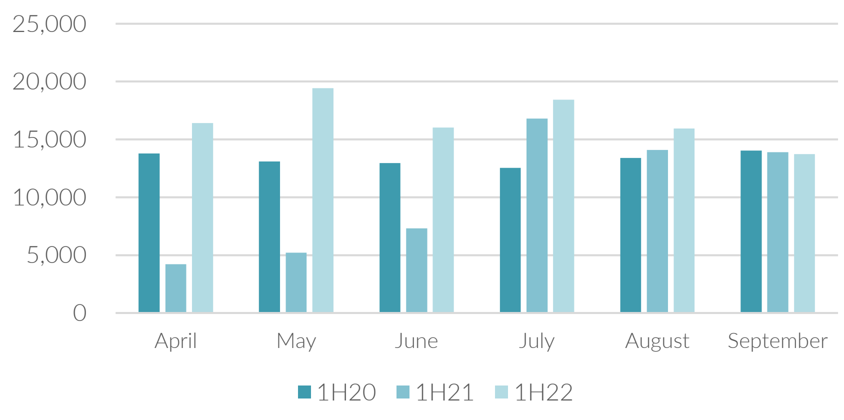
Actions taken to reinvigorate Xmas Savings business

The 2021 Xmas Savings order book has been completed (down 14% – in line with previous expectations), having been held back by lockdown restrictions impacting face-to-face agent activity in 1Q21. Although billings from Xmas Savings declined gently in the years pre-pandemic (FY21 down 10% on FY17), APP aims to reverse the trend through i) better retention of existing agents and encouraging them to recruit more of their family and friends to save through them, ii) a programme to engage agents with more training and webinars (already commenced), iii) growing the direct-to-consumer business. The campaign for Christmas 2022 gets under way in December 2021 and will use a more targeted approach to optimise media spend, combining increased social and digital focus with traditional media, including the usual TV advertising.

Redemptions returning to more normal levels

The chart below shows the redemption pattern in 1H20-1H22. While there has again been an element of monthly volatility, the key message is that 1H22 showed a similar pattern to pre-pandemic 1H20. The pattern of redemption is important, as the revenue on most products is recognised on recognition, not on the dispatch of the product (see Appendix 1)

Monthly redemptions (£m)



Source: Appreciate, Hardman & Co Research

Theme 3: other issues

Positive issues

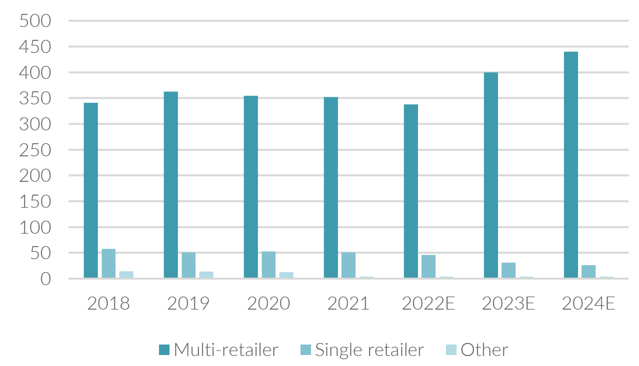
Business mix trends continuing as expected

The business mix is evolving in line with our expectations, with three key trends:

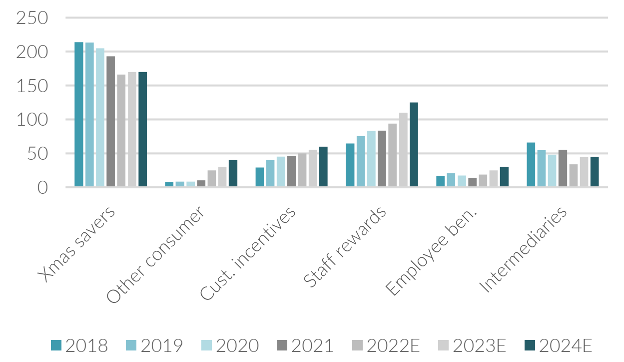
- continued growth in the more profitable multi-retailer billings (1H22 87.2% total, vs. 86.7% in 1H21 and 83.0% in 1H20) – see table below;
- continued faster growth in corporate (especially staff rewards), with more modest consumer growth; and
- continued growth in digital/cards over paper format (see chart on page 4).

These trends have implications for revenue recognition and the amount of restricted cash (see *Appendix 1*). As indicated in our initiation, we believe billings are a better reflection of the franchise growth than revenue.

Billings by multi-retailer, single store and other (£m)



Billings by market (£m)



Source: Appreciate, Hardman & Co Research

Director buying

We note there has been steady director buying, including the CEO – 200k at 27.5p on 12 August, and the NED – 15k at 32.5p on 15 July.

Neutral issues

Chair to step down

On 21 September, APP announced that Laura Carstensen had informed the board of her intention to step down as Chairman as part of the board's succession plan. The board imminently commenced a search process to appoint a successor and enable an orderly handover. Ms Carstensen will continue to serve as Chairman until the process is completed. An update will be provided in due course. Laura Carstensen has been with the company for almost eight years, having been appointed to the board as a non-executive director on 23 September 2013, before becoming Non-Executive Chairman on 3 June 2016. We note that she is also stepping down at AJ Bell.

APP's willingness to forego low-margin clients evidence of its confidence in growth opportunities in the business

We note the c£3m drop in billings associated with APP's supply to a low-margin direct competitor. We understand that this was APP's decision, having tried to adjust the pricing and the counterparty refusing to accept the new terms. It could be interpreted as reflecting confidence in the growth of the business – that this contribution to fixed costs can be foregone at this stage. We understand that the review of the whole order book does not show any other significant contracts at risk, because they are on such adverse terms.

Unclear what degree is of recurring benefit from corporates giving gifts, and not holding Xmas parties. APP working hard to retain such customers.

Last year, APP benefited when corporates decided not to have Xmas parties and offer gift cards to staff in their place. At the time of the results, APP did not have conclusive evidence for how 2021 would turn out, with some evidence of renewed voucher use and some of greater hospitality. The company has prioritised the retention of the corporate accounts (historically c.90%) and, to date, has seen a recovery from the higher attrition seen last year. The 90% retention reflects portfolio-wide experience, with no specific detail on new clients won because of the cancellation of Xmas parties. More visibility on this is unlikely to be available until mid-December.

Downsides

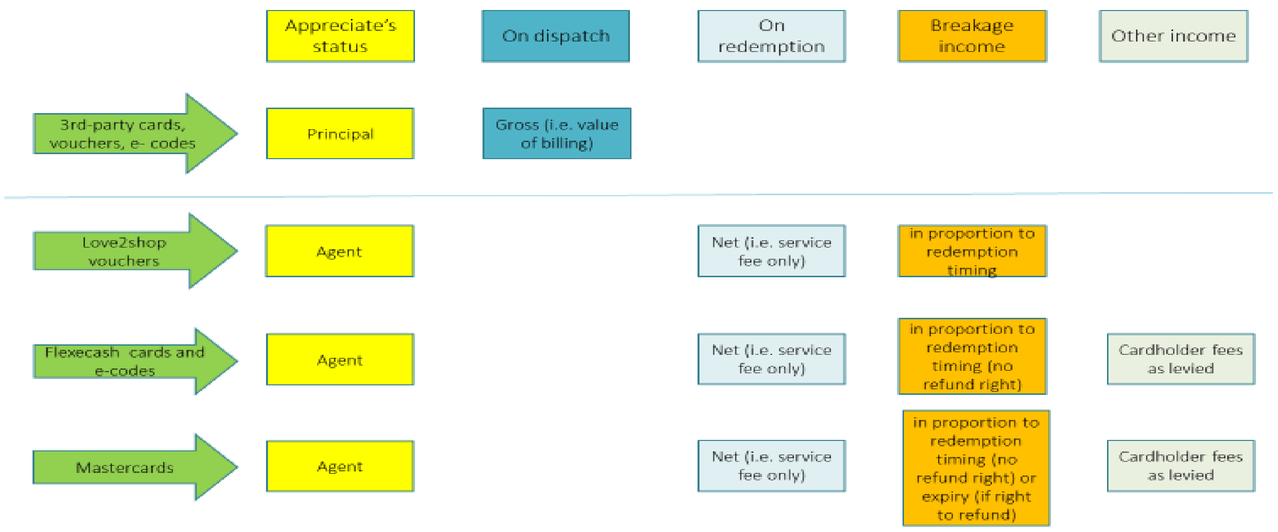
PayPoint relationship started slowly. More effort being put into franchisee relationship and communication.

We had been looking for a detailed update on how the PayPoint distribution partnership was going. It appears to have got off to a slow start since the launch in May, with APP commenting that it had "continued to build awareness through PayPoint's 28,000 UK retailers and customers and explore opportunities to enhance services offered through its network". In the analyst meeting, APP acknowledged that, to date, relatively few franchise partners had become involved, as it struggled to get the attention it had hoped for. It is still early days for the relationship, and we expect APP to test different approaches until it finds success within the 28,000-strong network. In the meantime, the main "cost" has been in management time and resource.

Appendix 1: summary of product accounting and cashflow

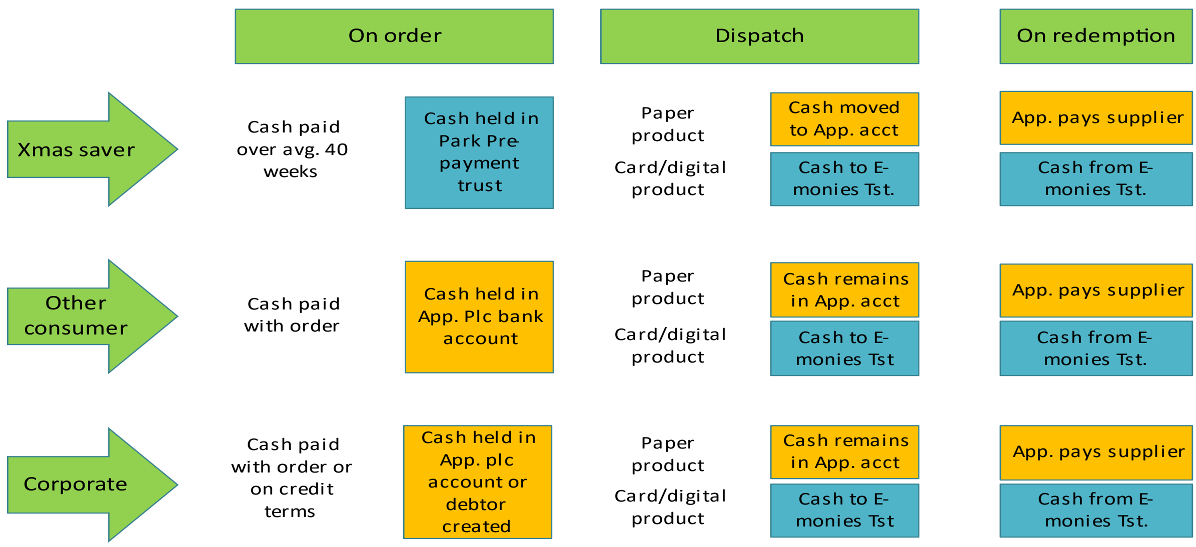
The charts below summarise the revenue and cashflow recognition by product. For a more detailed review, investors should refer to our initiation report.

Revenue – gross vs. net, timing, breakage and other, by product line



Note: yellow boxes represent APP's status, light and dark-blue boxes are for when service fee revenue is recognised, orange boxes are for breakage income, and light-green boxes are for other income.
Source: Appreciate, Hardman & Co Research

Operational cashflows (customer action green, segregated cash in blue, APP own cash orange)



Note: green boxes represent customer action, orange boxes represent when cash is in an APP corporate account, blue boxes are where it is held in a trust account outside APP.
Source: Appreciate, Hardman & Co Research

Financials

Profit and loss (£000)							
Year-end Mar	**2018**	**2019**	**2020**	**2021**	**2022E**	**2023E**	**2024E**
Consumer billings	232,635	232,096	222,207	205,300	176,000	185,000	188,000
Corporate billings	180,151	194,805	197,650	201,200	197,000	235,000	260,000
Total billings	**412,786**	**426,901**	**419,857**	**406,500**	**373,000**	**420,000**	**448,000**
Revenues							
Goods – single-retailer redemption products	60,621	55,624	62,142	78,154	46,741	56,741	56,741
Other goods	8,497	7,511	6,240	259	259	259	259
Services – multi-retailer redemption products	36,087	41,111	37,870	24,736	48,553	43,353	45,953
Other services	5,777	6,119	6,371	3,509	2,000	3,000	3,000
Other	72	29	101	147	147	147	147
Total revenue	**111,054**	**110,394**	**112,724**	**106,805**	**97,700**	**103,500**	**106,100**
Costs of sales	(79,628)	(79,117)	(79,778)	(82,055)	(68,390)	(72,450)	(72,148)
Impairment of obsolete stock	-	-	(124)	(414)	-	-	-
Gross profit	31,426	31,277	32,822	24,336	29,310	31,050	33,952
Distribution costs	(3,002)	(2,934)	(2,838)	(1,784)	(2,345)	(2,381)	(2,440)
Admin. expenses (excl. depreciation and amortisation)	(15,679)	(16,007)	(18,377)	(19,279)	(18,000)	(17,500)	(17,750)
Depreciation and amortisation	(1,428)	(1,394)	(1,659)	(1,791)	(2,085)	(2,085)	(2,085)
Impair. of prop., plant & equip.	-	(1,210)	(163)	-	-	-	-
Impair. of assets for sale	-	-	(1,650)	205	-	-	-
Impair. of goodwill	-	-	(1,316)	(218)	-	-	-
Redundancy costs	-	-	(423)	(639)	-	-	-
Operating profit	**11,317**	**9,732**	**6,396**	**830**	**6,880**	**9,085**	**11,677**
Finance income	1,274	1,572	1,481	783	500	762	830
Finance costs	(4)	-	(177)	(360)	(500)	(500)	(500)
Profit before tax	**12,587**	**11,304**	**7,700**	**1,253**	**6,880**	**9,347**	**12,007**
Tax	(2,399)	(2,422)	(2,189)	(402)	(1,376)	(1,869)	(2,401)
Attributable profit	**10,188**	**8,882**	**5,511**	**851**	**5,504**	**7,477**	**9,605**
Diluted EPS (p)	5.48	4.77	2.96	0.46	2.95	4.01	5.15
Weighted average number of shares (m)	185.9	186.1	186.3	186.3	186.3	186.3	186.3
Dividend per share (p)	3.10	3.20	0	1.00	1.50	2.00	2.75

Source: Appreciate Report and Accounts, Hardman & Co Research

Since our initiation we have reduced billings (for both the PayPoint deal and the low-margin competitor), with the lower revenue offset by lower costs. We are slightly above management guidance on the latter, given market uncertainty on inflationary pressures.

Adjusted profit and loss (£m)							
Year-end Mar	**2018**	**2019**	**2020**	**2021**	**2022E**	**2023E**	**2024E**
Consumer billings	**12.6**	**11.3**	**7.7**	**1.3**	6.9	9.3	12.0
Redundancy			0.4	0.6			
Impairment of obsolete stock			0.1	0.4			
Impairment on property, plant, equipment		1.2	0.2				
Impairment of goodwill			1.3	0.2			
Impairment of assets held for sale			1.7	(0.2)			
Adjusted profit	**12.6**	**12.5**	**11.4**	**2.3**	**6.9**	**9.3**	**12.0**
Wind-down of hamper packing business*				1.2			
Related costs now deployed elsewhere*				0.4			
Decommissioning old head office*				0.3			
FMI losses pre-disposal*				0.1			
Pre-exceptional, pre-one-off pre-tax profit				**4.3**			

**Unaudited; Source: Appreciate Report and Accounts, Hardman & Co Research*

Balance sheet (£000)

@ 31 Mar	2017	2018	2019	2020	2021	2022E	2023E	2024E
Goodwill	2,202	2,185	2,168	800	582	582	582	582
Other intangibles	2,682	2,278	2,295	4,757	8,861	10,861	12,861	14,861
Investments	0	0	0	0	0	0	0	0
Prop., plant & equip.	7,688	7,684	6,216	2,662	2,188	2,188	2,188	2,188
Deferred tax assets	654	237	0	0	0	0	0	0
Right of use assets	0	0	0	3,799	4,373	4,373	4,373	4,373
Retirement benefit asset	1,827	2,721	1,927	4,206	2,086	2,086	2,086	2,086
Total non-current assets	**15,053**	**15,105**	**12,606**	**16,224**	**18,090**	**20,090**	**22,090**	**24,090**
Inventories	2,632	3,808	4,574	2,840	3,638	3,638	3,638	3,638
Trade and other receivables	9,236	10,917	12,582	9,457	11,405	12,405	13,405	14,405
Tax receivable	0	0	0	266	738	738	738	738
Other financial assets	200	200	200	0	0	0	0	0
Monies held in trust	83,018	86,992	99,251	102,693	132,054	132,054	152,054	172,054
Cash and cash equivalents	34,236	40,311	36,868	29,632	31,415	17,029	3,684	4,320
Total current assets	129,322	142,228	153,475	144,888	179,250	165,864	173,519	195,156
Assets held for sale	0	0	0	3,1530	0	0	0	0
Total assets	**144,375**	**157,333**	**166,081**	**164,265**	**197,340**	**185,954**	**195,609**	**219,245**
Bank overdraft	-	-	(2,305)	-	-	-	-	(13,250)
Trade and other payables	(87,201)	(94,592)	(61,191)	(57,150)	(52,776)	(53,776)	(54,776)	(55,776)
Payables in respect of cards/ vouchers	0	0	(14,193)	(17,060)	(25,302)	(25,302)	(25,302)	(25,302)
Deferred income	0	0	(6,983)	(7,359)	(11,152)	(9,152)	(10,152)	(11,152)
Other payables	0	0	(5,280)	(5,294)	(7,040)	(8,698)	(7,356)	(11,015)
Tax payable	(1,272)	(704)	(580)	-	-	-	-	-
Provisions	(46,164)	(48,012)	(58,286)	(53,802)	(77,915)	(62,915)	(67,915)	(67,915)
Total current liabilities	(134,637)	(143,308)	(148,818)	(140,665)	(174,185)	(159,843)	(165,501)	(184,410)
Deferred tax liability	0	0	(553)	(1,121)	(779)	(779)	(779)	(779)
Lease liability	0	0	0	(4,132)	(4,666)	(4,666)	(4,666)	(4,666)
Retirement benefit obligation	(924)	0	0	-	-	-	-	-
Total non-current liabilities	**(924)**	**0**	**(553)**	**(5,253)**	**(5,445)**	**(5,445)**	**(5,445)**	**(5,445)**
Total equity	8,814	14,025	16,710	18,347	17,710	20,666	24,663	29,390
NAV per share (p)	4.8	7.6	9.0	9.8	9.5	11.1	13.2	15.8

Source: Appreciate Report and Accounts, Hardman & Co Research

Cashflow (£000)

Year-end Mar	2018	2019	2020	2021	2022E	2023E	2024E
Net cash generated from/(used in) op. activs.	9,270	6,795	5,642	4,752	(7,164)	(5,191)	(3,062)
Net cash (used in)/generated from invest. activs.	(1,019)	(1,152)	(5,029)	(2,627)	(4,085)	(4,085)	(4,085)
Net cash used in financing activs.	(5,370)	(5,323)	(5,544)	(342)	(3,137)	(4,069)	7,783
Net (decrease)/increase in cash and cash equivalents	**2,881**	**320**	**(4,931)**	**1,783**	**(14,386)**	**(13,345)**	**636**
Cash and cash equivalents at beginning of period	31,362	34,243	34,563	29,632	31,415	17,029	3,684
Cash and cash equivalents at end of period	34,243	34,563	29,632	31,415	17,029	3,684	4,320

Source: Appreciate Report and Accounts, Hardman & Co Research

Changes to forecast (£000)

Year-end Mar	2022E			2023E			2024E		
	Old	New	Change	Old	New	Change	Old	New	Change
Billings	388,238	373,000	-4%	435,000	420,000	-3%	470,000	448,000	-5%
Revenue	99,700	97,700	-2%	107,000	103,500	-3%	109,600	106,100	-3%
Gross profit	29,139	29,310	1%	32,100	31,050	-3%	35,072	33,952	-3%
GP margin	29%	30%	3%	30%	30%	0%	32%	32%	0%
Admin/dist. costs as % rev.	71%	70%	-1%	70%	70%	0%	68%	68%	0%
Pre-tax profit	6,793	6,880	1%	9,553	9,347	-2%	12,071	12,007	-1%
Net cash	16,959	17,029	0%	3,779	3,684	-3%	4,466	4,320	-3%
Shareholders' funds	17,710	17,710	0%	20,596	20,666	0%	24,758	24,663	0%
EPS (p)	2.92	2.95	1%	4.10	4.01	-2%	5.18	5.15	-1%

**Unaudited; Source: Appreciate Report and Accounts, Hardman & Co Research*

Valuation

Summary

Range of valuation approaches, including using European comparator, GGM and DDM. Average of all is 60p.

We applied a range of different valuation approaches in our initiation. We believe the closest comparator is the private-equity-held European comparator (on our assumptions, implied valuation of 80.1p). Also outlined below are some absolute measures, including a GGM (on our assumptions, implied valuation of 66.2p), which we believe best captures the value added and the growth potential of a business like APP, together with a DDM (on our assumptions, implied valuation of 32.7p). The mathematical average of these approaches indicates a valuation of 60p, against the current share price of 23p.

European digital comparator valuation saw substantial valuation uplift in 2021 ytd but limited information. Applying 40% of billings (reflecting business mix) gives APP valuation of 80.1p.

As noted above, there is a private-equity-backed company in Europe whose model is a comparator for APP's digital vision. The businesses are not identical, and valuing a high-growth business can present challenges. The European comparator traded at 3x the billings at a comparable stage of the development of its digital business at end-2020. It has since seen a substantial valuation uplift, but there has been no further billings disclosure. The valuations reported by the private-equity backer have consistently seen very significant uplifts on sales, and are believed to be generally conservative. If we conservatively apply 40% of billings to reflect APP's current mix of non-digital businesses, this implies a valuation of 80.1p.

UK market comparisons

We noted, in the chart in the digitalisation section in our initiation, that, in the UK market, digital companies' forward P/E ratings are usually 2x-4x the levels of non-digital businesses. Applying the average rating of the companies in the digital section of our initiation (a forward P/E of 30x) generates an implied valuation of 88p, but these companies are significantly larger, and the valuation may be conservative, as APP is at the early stages of its digital journey.

GGM

Our GGM assumptions were outlined in our initiation.

GGM and key sensitivities

	Base	+1% RoE	+1% CoE	+0.5% G
RoE	40%	41%	40%	40%
CoE, post-tax	14%	14%	15%	14%
G	7%	7%	7%	7.5%
P/BV (x)	5.0	5.2	4.3	5.3
Disc./prem. re near-term performance	0%	0%	0%	0%
P/BV (x)	5.0	5.2	4.3	5.3
BV Mar'23E (p/sh)	13.2	13.2	13.2	13.2
Valuation (p/sh)	66.2	68.2	57.5	70.5
Variance (p/sh)		2.0	-8.7	4.3

Source: Hardman & Co Research

DDM: dividend policy is to distribute just over half post-tax profits

It has been the board's policy to distribute just over half of post-tax profits as a dividend, with one third of that as an interim dividend and the remaining two thirds as a final dividend. The board intends to return to that policy as soon as it is appropriate to do so. The board recognises the importance of dividends to its shareholders, and is committed to its progressive dividend policy.

Other "peer" companies

Trade sales that support the valuation include Global Voucher Group (acquired by GoCompare in 2017 for £36.5m), Blackhawk Network (acquired by Silver Lake and P2 Capital Partners for $3.5bn in January 2018) and Mydays (see PROSIEBENSAT.1 *news release*). These deals are somewhat dated, but they do show trade appetite for companies like Appreciate.

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