

SANDERSON DESIGN GROUP

CONSUMER DISCRETIONARY

11 October 2022

SDG.L

97p

Market Cap: £68.9m

SHARE PRICE (p)



12m high/low

211p/88p

Source: LSE Data (priced as at prior close)

KEY DATA

Net (Debt)/Cash	£15.0m (at 31/07/22)
Enterprise value	£53.9m
Index/market	AIM
Next news	Update - January '23
Shares in Issue (m)	71.0
Chairman	Dame Dianne Thompson
Chief Executive	Lisa Montague
Finance Director	Mike Woodcock

COMPANY DESCRIPTION

Sanderson Design Group is a luxury interior furnishings company, specialising in wallpapers, fabrics and paints.

www.sandersondesign.group

SANDERSON DESIGN GROUP IS A RESEARCH CLIENT OF PROGRESSIVE

ANALYSTS

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Resilient interim results in uncertain times

Sanderson Design Group (SDG) delivered an impressive 12.5% increase in adjusted underlying profit before tax to £6.3m for H1 FY23 from the previously disclosed 0.7% increase in group revenue. Strong performances from the higher-margin activities of the North American market, licensing and the Morris & Co brand were the keys drivers of a significant gross margin expansion, also supported by price increases. A good start to H2 underpins the group's anticipation to meet the Board's expectations for the year, while simultaneously expressing caution in light of the various headwinds buffeting businesses globally. We are prudently reining back our forecasts to reflect that caution, while expecting the group to mitigate cost pressures and further benefit from its brand pricing power.

- Robust interim results – with profit growth outstripping revenue growth.** SDG delivered a strong set of interim results from a modest level of revenue growth, with a small reduction in overall sales volumes. This reflects adherence to the group's well-defined strategy, a good level of pricing power across its brand portfolio, and active management to mitigate cost pressures, supported by its in-house manufacturing facilities. The declared interim dividend of 0.75p was flat on last year, and period-end net cash of £15.0m, compared with £19.1m at the 31 January year-end, reflected strategic inventory investment to ensure availability of best-selling lines.
- Operational developments – including significant licence renewals.** Morris and Co delivered a reported 15.5% revenue increase and the North American market saw a 12.8% reported increase, but the star of the show was Licensing, which delivered a 90% increase to £3.8m, driven by accelerated income of £1.9m (from £0.5m) under IFRS15, reflecting both new and extended licences. H1 agreements signed included a three-year renewal with Bedeck covering several group brands and a renewal with NEXT for Morris & Co womenswear. Licensing momentum has continued in H2, with agreements with Disney (for a Sanderson collaboration) and an extension of the Williams Sonoma kitchenware partnership.
- Outlook and forecasts – adopting a more cautious approach.** In light of the caution expressed by the group given the uncertain global backdrop, we believe it is appropriate to adopt a more prudent stance across our forecast horizon. Our new figures are summarised below, with further details given within our note.

FYE JAN (£M)	2021	2022	2023E	2024E	2025E
Revenue	93.8	112.2	115.0	120.4	125.8
Adj EBITDA	13.5	18.2	18.9	19.0	19.3
Fully Adj PBT	7.0	12.6	12.7	12.5	12.6
Fully Adj Dil EPS (p)	7.7	13.6	14.3	14.1	13.8
EV/Sales (x)	0.6x	0.5x	0.5x	0.4x	0.4x
EV/EBITDA (x)	4.0x	3.0x	2.9x	2.8x	2.8x
PER (x)	12.6x	7.1x	6.8x	6.9x	7.0x

Source: Company Information and Progressive Equity Research estimates.

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Please refer to important disclosures at the end of the document.

Interim results overview and outlook

Sanderson Design Group delivered a resiliently robust performance against what remains an uncertain macroeconomic backdrop with a number of accompanying challenges. The strength of the interim figures was driven by outperformance in three areas, namely Morris & Co, Licensing and the North American market. These are also the most profitable areas within the group's operations. This factor, supported by price increases in February, drove a year-on-year 335bps increase in the achieved gross margin to 65.8%.

While a further price increase should help to offset various inflationary pressures over the remainder of FY23E, including energy and the group's commitment to the Real Living Wage, with the group anticipating that it will meet Board expectations for the year we feel it prudent to rein back our forecasts. In our view, this marries with the caution expressed by the group. We have therefore trimmed our FY23E estimates from our previous high-end-of-range figures, and are now forecasting effectively flat adjusted profit before tax in the outer years of FY24E and FY25E from the adjusted base of FY23E.

Interim results

The following table summarises the interim results compared with last year's equivalent period, which reflected a rebuilding of customer activities following the reduced level of business in the previous year that had been adversely affected by the global pandemic.

Overview of interim results (£m unless otherwise stated)

	H1 FY23	H1 FY22	% change
Revenue:			
- Brands	42.2	43.2	-2%
- Manufacturing	11.9	12.2	-3%
- Licensing	3.8	2.0	88%
Total	57.9	57.5	1%
Gross profit	38.1	35.9	6%
<i>Gross margin (%)</i>	<i>65.8%</i>	<i>62.5%</i>	<i>+335bps</i>
Distribution and selling costs	(10.4)	(10.0)	4%
Administration costs	(22.4)	(21.0)	6%
Total operating costs	(32.8)	(31.0)	6%
Operating profit	5.4	4.9	9%
Reported PBT	5.5	4.9	11%
Adjusted PBT	6.3	5.6	13%
Adjusted diluted EPS (p)	6.82	5.97	14%
Dividend (p)	0.75	0.75	n.a.

Source: Sanderson Design Group, Progressive Equity Research

Group sales rose 1% on a reported basis to £57.9m and were flat on a constant current (CC) basis. Broken down into business segments, Brand product revenue was down 3% on a reported and CC basis. Adjusting for the loss of £0.8m of sales from ceasing to trade in Russia this year, and the £0.6m benefit to H1 sales last year from delayed FY21 dispatches following Brexit, the underlying Brand product revenue performance translates to a 1% increase on a reported basis (and flat in CC terms). External Manufacturing sales nudged down 3% to £11.9m against last year's tough comparator, when customers began restocking after emerging from the pandemic and retail lockdowns

Licensing was the star of the show, as outlined above, and as a 100% gross margin business stream it was strongly supportive of the H1 performance. This was also a major contributor to the 335bps improvement in the gross margin to 65.8%. However, it should also be noted, that pure product gross margin, supported by price increases, saw a 230bps increase in its own right to 63.4%.

The following table gives the slightly updated performance by reporting segment compared with the trading update, including the reported and constant currency (CC) changes to one decimal point.

H1 revenue performance by reporting segment – FY23 and FY22

	H1 revenues (£m)		% change	
	FY23	FY22	Reported	CC basis
Brand product				
- UK	22.1	22.3	(0.9%)	(0.9%)
-Northern Europe	5.5	6.9	(20.3%)	(16.8%)
-North America	9.7	8.6	12.8%	3.3%
-Rest of World	4.9	5.5	(10.9%)	(9.6%)
Total Brand product revenue	42.2	43.3	(2.5%)	(3.5%)
Manufacturing				
-External	11.9	12.2	(2.5%)	
-Internal	9.8	8.8	11.4%	
Total Manufacturing revenue	21.7	21.0	3.3%	
Licensing				
Total Licence revenue	3.8	2.0	90.0%	89.3%
Group revenue	57.9	57.5	0.7%	0.0%

Source: Sanderson Design Group, Progressive Equity Research

Costs continue to be well managed by the group, with the overall cost increase, net of other income, held to just 6%. The group continues to benefit from a fixed price contract for gas running until October 2023. The group's fixed-term price contract for electricity was due for renewal on 1 October 2022, but the group is now paying for this at the capped rate, which nonetheless still represents a £700,000 per annum increase. Without this government support, the group's electricity bills would increase by a further £2m. The group continues to undertake a range of mitigating factors to reduce future energy costs, including the planned installation of solar panels at its Standfast & Barracks fabric printing facility (covering 3,000 square metres), the widespread introduction of LED lighting and a further shift to a higher participation of digital printing within its manufacturing activities.

The following table shows the revenues achieved by brand compared with the first-half period last year. The total Brands revenue shown excludes Licensing revenues. This underlines the very strong performance of Morris & Co, with all other core brands showing year-on-year declines. We would stress, however, that individual brand performances varied across key markets. Further details of brand performances within selected key territories (and on a reported and constant currency basis) are provided within the group's interim results announcement.

Revenues by brand (£m - in reported currency)

	H1 FY23	H1 FY22	% change
Clarke & Clarke	11.828	12.582	(6%)
Morris & Co	9.462	8.192	16%
Harlequin	8.277	9.098	(9%)
Sanderson	7.174	7.504	(4%)
Zoffany	4.247	4.485	(5%)
Scion	0.997	1.204	(17%)
Other brands	0.185	0.174	6%
Total Brands	42.170	43.239	(2%)

Source: Sanderson Design Group, Progressive Equity Research

Trading was softer in August, but current trading in the opening weeks of H2 has been in positive territory, with the key autumn selling weeks in October and November important to the full-year outturn. This encouraging start has underpinned the group's expectations for the full FY23E outturn, notwithstanding ongoing vigilance with regard to external factors and the caution that commands.

Forecast changes

As outlined above, we have decided to undertake a more prudent stance with regard to our forecasts. This prudence is reflected primarily through a lower level of sales growth across our forecast period, offset to a degree by small increases in the gross margin percentage.

Summary of estimate changes – FY23E-FY25E

£m unless stated	FY23E			FY24E			FY25E		
	Old	New	Change (%)	Old	New	Change (%)	Old	New	YOY inc (%)
Revenue	119.1	115.0	(3.5%)	128.4	120.4	(6.3%)	138.4	125.8	(9.2%)
Adj EBITDA	19.4	18.9	(2.9%)	20.7	19.0	(8.1%)	22.1	19.3	(12.8%)
Reported PBT	10.7	10.6	(0.6%)	11.7	10.4	(11.0%)	12.9	10.5	(18.8%)
Fully adj PBT	13.0	12.7	(2.0%)	14.0	12.5	(10.6%)	15.2	12.6	(17.3%)
Reported EPS (p)	11.4	11.4	(0.6%)	12.2	10.9	(11.0%)	13.5	10.9	(18.8%)
Fully adj Dil EPS (p)	14.6	14.3	(2.4%)	15.8	14.1	(10.8%)	16.7	13.8	(17.5%)

Source: Progressive Equity Research estimates

We are forecasting operating costs to rise at a faster rate than turnover growth, resulting in decreased EBITDA, operating and PBT margins. However, it should be noted that our forecasts for adjusted PBT and dividends remain broadly flat within our new forecasts, which is a testament to the ongoing strategy and strengths of the group, supported by its strong balance sheet.

Summary profit & loss account and cash flow forecasts (£m unless otherwise stated)

Profit and loss account					
Year to January	FY21	FY22	FY23E	FY24E	FY25E
Divisional turnover					
- Brands	72.6	84.1	85.8	90.1	94.6
- Manufacturing (net)	17.5	22.9	23.2	23.9	24.3
- Licensing	3.7	5.2	6.0	6.4	6.8
Group turnover	93.8	112.2	115.0	120.4	125.8
Cost of sales	(36.9)	(38.4)	(39.0)	(41.0)	(42.9)
Gross profit	56.9	73.8	76.0	79.3	82.9
<i>Gross margin (GM) (%)</i>	<i>60.7%</i>	<i>65.8%</i>	<i>66.1%</i>	<i>65.9%</i>	<i>65.9%</i>
Distribution and selling costs	(15.3)	(20.7)	(21.7)	(22.9)	(24.1)
Administration costs	(36.5)	(42.8)	(43.8)	(46.0)	(48.3)
Operating profit	5.1	10.3	10.5	10.4	10.5
<i>Operating profit margin (%)</i>	<i>5.4%</i>	<i>9.2%</i>	<i>9.1%</i>	<i>8.7%</i>	<i>8.3%</i>
Depreciation and amortisation	(7.4)	(6.8)	(7.4)	(7.6)	(7.8)
EBITDA	12.5	17.1	17.9	18.0	18.3
<i>EBITDA margin (%)</i>	<i>13.4%</i>	<i>15.3%</i>	<i>15.6%</i>	<i>15.0%</i>	<i>14.6%</i>
Interest charge	(0.2)	0.0	0.1	0.0	0.0
PBT	4.9	10.4	10.6	10.4	10.5
Exceptional/adjusting items	(2.1)	(2.2)	(2.1)	(2.1)	(2.1)
Adjusted profit before tax	7.0	12.6	12.7	12.5	12.6
<i>Adjusted PBT margin (%)</i>	<i>7.5%</i>	<i>11.2%</i>	<i>11.1%</i>	<i>10.4%</i>	<i>10.0%</i>
Adjusted diluted EPS (p)	7.7	13.6	14.3	14.1	13.8
Diluted reported EPS (p)	5.3	10.8	11.4	10.9	10.9
Dividend (p)	0.0	3.5	3.5	3.5	3.6
Adjusted EBITDA	13.5	18.2	18.9	19.0	19.3
Adjusted operating profit	7.2	12.5	12.6	12.5	12.6
Cash flow					
Year to January	FY21	FY22	FY23E	FY24E	FY25E
Operating profit	5.1	10.3	10.5	10.4	10.5
Depreciation and amortisation	7.4	6.8	7.4	7.6	7.8
Inventory (increase)/decrease	8.1	(3.0)	(3.8)	(0.6)	(0.6)
Debtors (increase)/decrease	2.3	(0.7)	(0.0)	(0.3)	(0.6)
Creditors increase/(decrease)	(3.5)	0.7	0.5	0.5	0.9
Pension, other	(1.6)	(1.0)	(2.4)	(2.4)	(2.4)
Operating cash flow	17.8	13.1	12.1	15.1	15.6
Interest	(0.3)	(0.1)	0.1	0.0	0.0
Dividends	0.0	(0.5)	(2.5)	(2.5)	(2.5)
Tax	(0.0)	(3.8)	(2.4)	(2.6)	(2.6)
Deferred tax	0.0	0.0	0.0	0.0	0.0
Capital expenditure	(1.1)	(2.1)	(7.0)	(6.5)	(6.5)
Trading cash flow	16.4	6.7	0.3	3.5	4.0
Short term investments	0.4	0.0	0.0	0.0	0.0
Sale of fixed assets	0.1	0.0	0.0	0.0	0.0
Acquisition/disposal of businesses	0.0	0.0	0.0	0.0	0.0
Share issues	0.0	0.0	0.0	0.0	0.0
Currency effects, leases, other	(3.1)	(2.7)	(2.8)	(2.6)	(2.5)
Net cash inflow/(outflow)	13.8	3.9	(2.4)	0.9	1.5
Net (debt)/cash exc leases	15.1	19.0	16.6	17.5	19.1

Source: Sanderson Design Group, Progressive Equity Research estimates

Summary balance sheet forecasts (£m)

Balance sheet					
Year to January	FY21	FY22	FY23E	FY24E	FY25E
Tangible fixed assets	17.8	15.2	16.5	17.2	17.6
Intangible fixed assets	28.3	27.0	25.2	23.5	21.7
Investments and other	0.0	4.2	4.2	4.2	4.2
Total fixed assets	46.2	46.4	46.0	44.9	43.6
Stock	20.4	22.7	26.4	27.1	27.7
Trade and other debtors	18.3	17.7	17.7	18.0	18.6
Deferred tax	0.0	0.0	0.0	0.0	0.0
Cash and short term deposits	15.5	19.1	16.6	17.5	19.1
Current assets	54.2	59.4	60.7	62.6	65.4
Total assets	100.4	105.7	106.7	107.5	108.9
Trade and other payables	(20.5)	(20.1)	(20.6)	(21.1)	(22.0)
Borrowings	(0.4)	0.0	0.0	0.0	0.0
Other/lease liabilities	(2.7)	(2.0)	(2.0)	(2.0)	(2.0)
Current liabilities	(23.6)	(22.1)	(22.6)	(23.0)	(24.0)
Borrowings	0.0	0.0	0.0	0.0	0.0
Pension provisions	(5.6)	0.0	0.0	0.0	0.0
Deferred tax liabilities	(0.5)	(2.0)	(2.0)	(2.0)	(2.0)
Other/lease liabilities	(3.2)	(1.9)	(1.9)	(1.9)	(1.9)
Non-current liabilities	(9.4)	(3.9)	(3.9)	(3.9)	(3.9)
Total liabilities	(32.9)	(26.0)	(26.5)	(27.0)	(27.9)
Net assets	67.5	79.7	80.2	80.5	81.0

Source: Sanderson Design Group, Progressive Equity Research estimates

Financial Summary: Sanderson Design Group

Year end: January (£m unless shown)

	2021	2022	2023E	2024E	2025E
PROFIT & LOSS					
Revenue	93.8	112.2	115.0	120.4	125.8
Adj EBITDA	13.5	18.2	18.9	19.0	19.3
Adj EBIT	7.2	12.5	12.6	12.5	12.6
Reported PBT	4.9	10.4	10.6	10.4	10.5
Fully Adj PBT	7.0	12.6	12.7	12.5	12.6
NOPAT	5.5	9.3	9.8	9.8	9.5
Reported EPS (p)	5.3	10.8	11.4	10.9	10.9
Fully Adj Dil EPS (p)	7.7	13.6	14.3	14.1	13.8
Dividend per share (p)	0.0	3.5	3.5	3.5	3.6
CASH FLOW & BALANCE SHEET					
Operating cash flow	17.8	13.1	12.1	15.1	15.6
Free Cash flow	16.4	6.7	0.3	3.5	4.0
FCF per share (p)	23.2	9.4	0.4	5.0	5.6
Acquisitions	0.0	0.0	0.0	0.0	0.0
Disposals	0.0	0.0	0.0	0.0	0.0
Shares issued	0.0	0.0	0.0	0.0	0.0
Net cash flow	13.8	3.9	(2.4)	0.9	1.5
Overdrafts / borrowings	(0.4)	0.0	0.0	0.0	0.0
Cash & equivalents	15.5	19.1	16.6	17.5	19.1
Net (Debt)/Cash	15.1	19.1	16.6	17.5	19.1
NAV AND RETURNS					
Net asset value	67.5	79.7	80.2	80.5	81.0
NAV/share (p)	95.1	112.3	113.0	113.5	114.1
Net Tangible Asset Value	39.2	52.7	55.0	57.1	59.3
NTAV/share (p)	55.2	74.3	77.5	80.4	83.5
Average equity	66.2	69.7	73.5	76.3	79.1
Post-tax ROE (%)	10.6%	18.0%	17.3%	16.4%	15.9%
METRICS					
Revenue growth	N/A	19.7%	2.5%	4.7%	4.5%
Adj EBITDA growth	N/A	35.0%	3.7%	0.7%	1.5%
Adj EBIT growth	N/A	74.9%	0.7%	(0.7%)	0.5%
Adj PBT growth	N/A	79.4%	1.3%	(1.5%)	0.5%
Adj EPS growth	N/A	76.2%	4.9%	(1.5%)	(2.0%)
Dividend growth	N/A	N/A	0.0%	0.0%	2.9%
Adj EBIT margins	7.6%	11.2%	11.0%	10.4%	10.0%
VALUATION					
EV/Sales (x)	0.6	0.5	0.5	0.4	0.4
EV/EBITDA (x)	4.0	3.0	2.9	2.8	2.8
EV/NOPAT (x)	9.8	5.8	5.5	5.5	5.6
PER (x)	12.6	7.1	6.8	6.9	7.0
Dividend yield	N/A	3.6%	3.6%	3.6%	3.7%
FCF yield	23.9%	9.7%	0.5%	5.2%	5.8%

Source: Company information and Progressive Equity Research estimates

Disclaimers and Disclosures

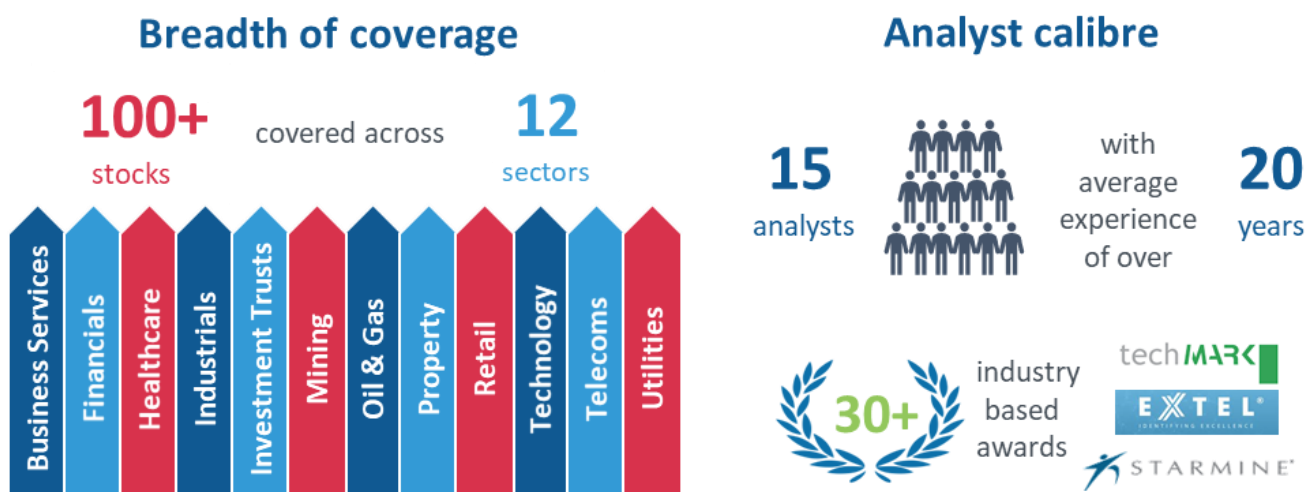
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