

Phil Oakley's Weekly Roundup



Exclusively for SharePad and ShareScope

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Market Overview

No.	Name	Price	%chg 1w	%chg 1m	%chg 1y	1y high	1y low	Date 1y high	Date 1y low
1	FTSE 100	7175.64	▼-1.06	▼-4.2	▼-2.81	7778.64	7092.43	12/1/18	9/2/18
2	FTSE 250	19551.7	▼-0.934	▼-3.14	▲3	20932.6	18832.9	5/1/18	22/3/17
3	FTSE SmallCap	5738.4	▲0.485	▼-2.21	▲7.08	6038.69	5348.3	15/1/18	9/3/17
4	FTSE AIM 100	5326.75	▼-1.15	▼-3.74	▲21.4	5550.39	4389.33	29/1/18	1/3/17
5	FTSE All-Share	3953.28	▼-0.98	▼-3.95	▼-1.53	4268.89	3902.85	12/1/18	9/2/18
6	S&P 500	2713.83	▲0.365	▼-3.83	▲13.3	2872.87	2328.95	26/1/18	13/4/17
7	Brent Oil Spot \$	\$65.332	▼-1.33	▼-6.34	▲16.1	\$70.72	\$44.785	24/1/18	21/6/17
8	Gold Spot \$ per oz	\$1318.79	▼-0.888	▼-2.22	▲5.73	\$1356.22	\$1200.05	24/1/18	9/3/17
9	GBP/USD - US Dollar per British Pound	1.37464	▼-1.47	▼-3.64	▲12	1.42661	1.21561	1/2/18	9/3/17
10	GBP/EUR - Euros per British Pound	1.1253	▼-0.583	▼-1.33	▼-3.38	1.1972	1.0795	18/4/17	29/8/17

Top FTSE All-Share risers

No.	TIDM	Name	%chg 1w
1	LRD	Laird PLC	▲77.7
2	PFG	Provident Financial PLC	▲49.2
3	SKY	Sky PLC	▲25
4	ZTF	Zotefoams PLC	▲15.1
5	FSJ	Fisher (James) & Sons PLC	▲14.2
6	ARW	Arrow Global Group PLC	▲13.6
7	COA	Coats Group PLC	▲13.2
8	SXX	Sirius Minerals PLC	▲13.1
9	DRX	Drax Group PLC	▲10
10	MTRO	Metro Bank PLC	▲9.99

Top FTSE All-Share fallers

No.	TIDM	Name	%chg 1w
1	AVV	Aveva Group PLC	▼-38.8
2	MTC	Mothercare PLC	▼-28.8
3	CPR	Carpetright PLC	▼-22.7
4	IRV	Interserve PLC	▼-13.2
5	EMG	Man Group PLC	▼-12.1
6	AA	AA Ltd	▼-12
7	RTO	Rentokil Initial PLC	▼-10.3
8	TPK	Travis Perkins PLC	▼-10.3
9	FRES	Fresnillo PLC	▼-10.3
10	MONY	Moneysupermarket.com Group...	▼-9.41

ITV (LSE:ITV)



Share price: 154p

Mkt Cap: £6.4bn

EMS: 10,000

No of analysts: 22

There is no doubt that ITV is a better and more resilient business than it was a decade ago. It has reduced its dependence on advertising revenue and has built a sizeable broadcast content business in ITV Studios.

The company ticks a lot of boxes in terms of financial performance. It has high profit margins, high returns on capital employed (ROCE) and is fairly good at turning its profits into cash. Yet for the last couple of years it has lacked the magic ingredient needed to propel its share price upwards - profits growth.

Wednesday's announcement of full year results for 2017 did not bring much in the way of comfort for shareholders. In fact the results showed again that as far as profitability is concerned advertising still matters a great deal.

In the core ITV broadcasting business, advertising revenue still accounts for more than three quarters of its revenue. It fell by £81m or 5% last year and, despite some growth from online revenues, operating profit for this business fell by £43m. The broadcasting business has considerable fixed costs which means that changes in revenues have a big impact on profits. This is a big risk that investors need to be aware of.

ITV Studios saw some decent growth in revenue but profits did not grow at all as costs increased significantly from building up its US drama content.

An 8% hike in the dividend is welcome but no special dividend has been announced this year as the company has quite a lot of debt now.

ITV has presented its debt position in a very helpful way as it shows all its debts including operating leases and pension fund deficits as well as deferred considerations for previous acquisitions which are often overlooked.

Twelve months to 31 December	2017 GBPm	2016 GBPm
Net debt	(912)	(637)
Expected contingent payments on acquisitions	(292)	(328)
Net pension deficit	(83)	(328)
Operating leases*	(143)	(344)
Adjusted net debt	(1,430)	(1,637)
Adjusted net debt to adjusted EBITDA	1.6x	1.8x
Reported net debt to adjusted EBITDA	1.0x	0.7x

Lease debt and the pension deficit are down substantially which is a good sign but net borrowings are significantly higher due to much weaker operating and free cash flows. Net debt to EBITDA of 1.6 times is lower than a year ago but is high enough in my opinion given the significance and cyclicity of ITV's advertising revenues.

I would encourage all investors to look at a company's cash flow statement as it is where that they are more likely to find the truth of what is going on with a company's financial performance.

ITV's operating cash flow fell by £168m last year to £689m. This compares with its adjusted EBIT of £842m. Note the cash outflows from exceptional items. These are the items that companies want you to ignore when weighing up its profitability. However, as you can see below these are often real cash costs which lead to cash flowing out of a business. In plain simple terms they represent a reduction in value and should not be ignored.

Consolidated Statement of Cash Flows

For the year ended 31 December	Note	2017 GBPm	2016 GBPm
Cash flows from operating activities			
Cash generated from operations before exceptional items	2.1	795	870
Cash flow relating to operating exceptional items:			
Operating exceptional items	2.2	(153)	(164)
Increase in exceptional payables		(18)	71
Decrease in exceptional prepayments and other receivables		45	66
Cash outflow from exceptional items		(126)	(27)
Operating cash flow from discontinued operation	2.5	-	(6)
Cash generated from operations		669	837
Defined benefit pension deficit funding		(80)	(80)
Interest received		21	38
Interest paid on bank and other loans		(59)	(58)
Net taxation paid		(95)	(90)
		(213)	(190)
Net cash inflow from operating activities		456	647

ITV is not a bad business but I struggle to see how it can meaningfully grow the profits of its Broadcasting business given that it is so dependent on advertising revenues. The company continues to go on about how it can deliver mass audiences that advertisers want but I feel that advertising in general is in crisis.

Many consumers hate the intrusion of advertising and are increasingly prepared to pay to avoid it. ITV is addressing this with a paid version of its ITV Hub catch up TV service which gets rid of adverts. That said, my view is that ITV cannot compete with the content of subscription services such as Netflix and Amazon Prime - which also show ITV content - that are relatively inexpensive for households to buy and free of adverts.

The key question is can ITV replace advertising revenue with another source of more reliable income? To do so it may have to move to some kind of subscription service which may not be an easy or quick solution.

ITV has long been touted as a takeover target, mainly due to a near 10% shareholding by Liberty Media which owns Virgin Media in the UK. Personally, I don't see this happening due to the huge reliance on advertising of the business. I also think that Liberty would have launched a bid by now as the weakness in ITV's share price has given it plenty of opportunity to do so.

I still see ITV as quite a risky business albeit one with some decent assets. Future profit growth may not be easy though. The company has said that 2018 has started well but I think the risks to profit forecasts are on the downside. Schedule costs in broadcasting are increasing this year and next which may make the company even more vulnerable to any further weaknesses in advertising revenues.

The shares are inexpensive on just over 11 times rolling one year forecast EPS and offer a decent yield of 5% but I think that's about right.

Greggs (LSE:GRG)



Share price: 94p

Mkt Cap: £94m

EMS: 1000

No of analysts: 3

I like Greggs as a business. I think it offers outstanding value for money to its customers and also like the fact that it makes a lot of its own products. For a food retailer, it is significantly more profitable than a supermarket with lease-adjusted ROCE of nearly 15%.

However, it is also a business that is now relatively mature having opened up lots of shops in the UK over the years. It is still continuing to grow its shop numbers but is having to relocate many of its existing ones from high streets - where fewer people are visiting - to areas such as train stations, university campuses and service stations where it can attract more customers. This costs significant amounts of money.

From a sales perspective 2017 was reasonable with its company owned shops (it has franchised shops as well) growing like-for-like sales by 3.7%. Higher costs have held back profits growth. Pre-tax profits nudged up from £80.3m to £81.8m as profit margins fell from 9% to 8.6%.

Greggs remains a very good generator of operating cash flow which is significantly higher than its operating profits. This is always a good sign but one that should be expected from a company with a significant non-cash depreciation expense.

Consolidated statement of cashflows

for the 52 weeks ended 30 December 2017 (2016: 52 weeks ended 31 December 2016)

	2017 GBP'000	2016 GBP'000
Operating activities		
Cash generated from operations (see below)	134,470	133,773
Income tax paid	(17,602)	(16,157)
Net cash inflow from operating activities	116,868	117,616
Investing activities		
Acquisition of property, plant and equipment	(68,646)	(74,016)
Acquisition of intangible assets	(3,918)	(6,106)
Proceeds from sale of property, plant and equipment	2,171	4,698
Interest received	249	124
Net cash outflow from investing activities	(70,144)	(75,300)
Financing activities		
Sale of own shares	5,358	4,063
Purchase of own shares	(11,352)	(12,398)
Dividends paid	(32,187)	(30,936)
Net cash outflow from financing activities	(38,181)	(39,271)
Net increase in cash and cash equivalents	8,543	3,045

Operating cash flow was largely unchanged but you can see that Greggs is reinvesting a lot of it - more than half - back into the business. The money is being spent refurbishing existing shops, opening new ones, upgrading its IT systems and expanding its food manufacturing.

At the moment it looks as if this money is being spent well as ROCE is still pretty decent. 2018 will see a sharp rise in investment (capex) to £95m; after that it should fall back.

Greggs PLC (GRG)

FORECASTS

£ millions unless stated

Year	2018		2019		2020	
Turnover	1,021.9	+6.4%	1,105.4	+8.2%	1,147.0	+3.8%
EBITDA	140.9	+12.0%	158.2	+12.2%	168.0	+6.2%
EBIT	85.5	+18.2%	98.3	+14.9%	103.6	+5.4%
Pre-tax profit	86.8	+17.2%	96.3	+10.9%	103.5	+7.5%
Post-tax profit	68.9	+16.7%	77.5	+12.5%	81.8	+5.5%
EPS (p)	66.7	+15.5%	73.3	+9.9%	80.2	+9.4%
Dividend (p)	33.9	+5.0%	37.1	+9.4%	40.3	+8.6%
CAPEX	83.0	+14.4%	74.0	-10.8%	65.0	-12.2%
Free cash flow	47.4	+6.5%	68.3	+43.9%	78.2	+14.6%
Net borrowing	-52.5	-3.7%	-73.0	+39.0%	-118.9	+63.0%

Greggs is a pretty resilient business given its value for money products and the location of its shops in higher footfall areas. It is also doing a good job of growing sales from areas such as breakfasts and coffee. Competition will remain fierce but Greggs is one of the most cost efficient operators out there and could benefit from any trading down from places such as Costa Coffee.

Costs are a concern - food, wages and business rates - and the 2018 forecast could be quite difficult to achieve in my opinion given 2017's modest growth in profits. The growth figures look a tad on the bullish side.

Greggs is a dependable, quality business that has rewarded long-term shareholders. Its shares currently carry a high price tag of 19 times forecast rolling EPS. It needs to be able to meet what seem to be quite bullish analysts' forecasts to warrant this kind of valuation in my opinion. If it can't then its shares will probably start to head lower

Safestyle (LSE:SFE)



Share price: 94p

Mkt Cap: £94m

EMS: 1000

No of analysts: 3

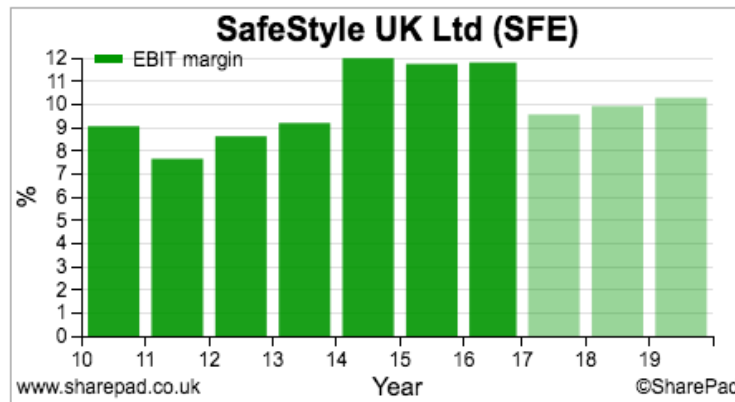
Wednesday morning saw the announcement of yet another profit warning from replacement doors and window company Safestyle. Coming so soon after the last warning in December has helped to push the share price to an all time low at the time of writing. It said:

*“The Group announced on 13 December 2017 that it had seen a continuing deterioration in the market resulting from declining consumer confidence and the Board expected market conditions to continue to be very challenging in 2018. **The activities of an aggressive new market entrant have added to an already competitive landscape and impacted the Group in certain areas of its operations. As a result, the Group’s order intake in 2018 to date has been disappointing and below our expectations.**” ...*

*“Guidance for the year ended 31 December 2017 remains unchanged. The Board now expects Group revenues and **underlying profit before tax for the year ending 31 December 2018 to be materially below 2017 levels and current market expectations.**”*

This is pretty savage stuff and doesn't really surprise me. Replacement doors and windows are essentially commoditized products with no end of businesses out there supplying them. The problem that all of them face is that so many homes now have these fitted that the demand is shrinking.

The citing of a new market entrant is probably the most worrying part of the profit warning. Safestyle has been earning reasonably high profit margins in recent years. This has been in part due to its efficient operating model but it now seems that those margins have attracted significant new competition.



This is telling investors a very simple but powerful truth about Safestyle's business - it has no moat to protect it.

SafeStyle UK Ltd (SFE)

FORECASTS

£ millions unless stated

Year	2017	2018	2019
Turnover	158.8	158.2	162.8
EBITDA	16.4	17.4	18.5
EBIT	15.2	15.7	16.7
Pre-tax profit	14.9	15.7	16.8
Post-tax profit	12.2	12.7	13.9
EPS (p)	14.4	15.3	16.4
Dividend (p)	11.3	11.3	11.6
CAPEX	5.4	1.6	1.6
Free cash flow	7.8	12.9	13.8
Net borrowing	-11.9	-14.6	-18.1
NAV	37.0	38.5	40.8

Analysts will be taking a knife to their forecasts for 2018. It wouldn't surprise me if at least 20% was sliced off which would give EPS of just over 12p. This would then suggest that a dividend cut is a distinct possibility. But will the damage end there?

It's difficult to say but I've seen businesses in this kind of industry unravel pretty quickly. Many local companies went bust in the last recession due to cash flow problems. I also remember back in my City days covering a conservatory roofing business called Ultraframe which went from being supremely profitable to near bankruptcy in a couple of years.

I don't see Safestyle going bust any time soon but I could envisage a scenario where this company earns 5% operating margins. This would imply that profits could still have some way to fall, especially if consumer confidence weakens.

The shares will undoubtedly attract the attention of bargain hunters but Safestyle looks like a case of the proverbial falling knife to me.

Croda (LSE:CRDA)



Share price: 4589p

Mkt Cap: £6.1bn

EMS: 500

No of analysts: 19

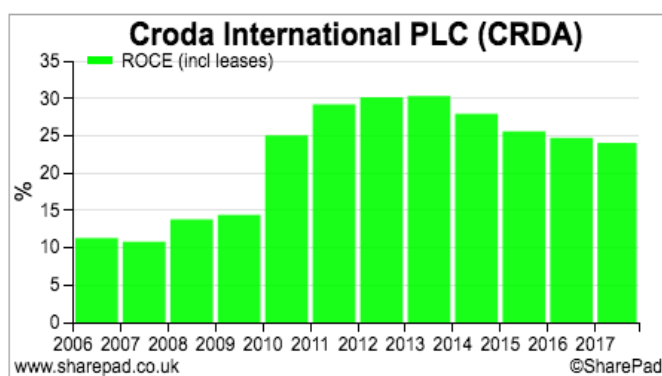
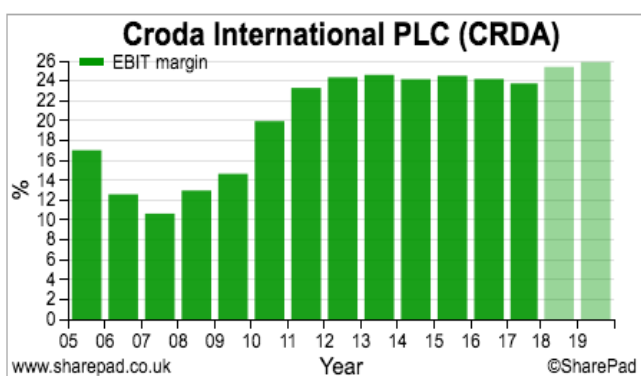
Disclosure: I currently owns shares in Croda

Croda is a speciality chemicals business. It focuses on making and selling niche, value added and problem solving products to its customers. It has three main businesses:

- **Personal Care** - Skin and hair products, sun protection and coloured cosmetics.
- **Life Sciences** - Crop protection, healthcare and seed enhancements.
- **Performance Technologies** - niche industrial products such as lubricants, coatings and high end plastics.

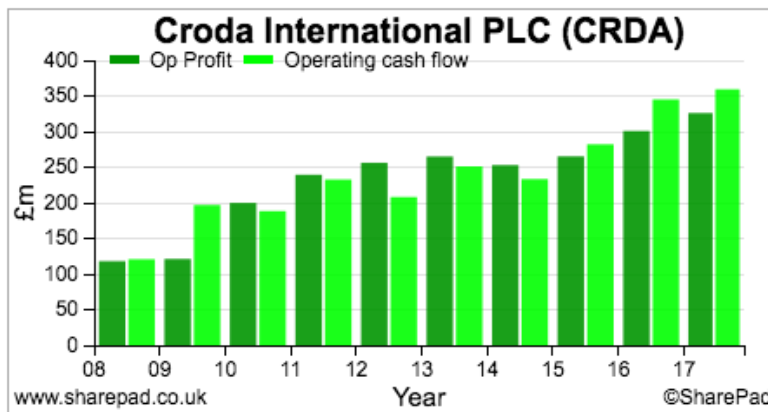
The company has a good track record for investing and creating innovative new products that help to keep sales and profits growing.

Financial returns have been pretty good in recent years. Profit margins and ROCE are high.

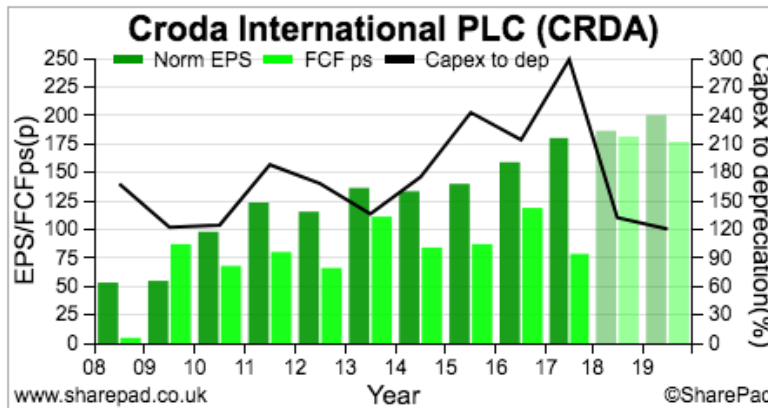


ROCE has been on a downwards trend as the company has been investing heavily in new manufacturing capabilities such as a biosurfactant plant. This will make environmentally friendly products from bio-ethanol which allows Croda to align itself with changing consumer preferences.

Cash conversion from operating profits to operating cash flow has been reasonable.



The same cannot be said for free cash flow conversion as the company has been investing heavily with capex spending significantly higher than its depreciation expense. As you can see, analysts expect the capex to depreciation ratio to fall over the next couple of years as capex has peaked with an improvement in free cash flow as an expected result.



As I have pointed out with ITV earlier, having high margins and returns is all well and good but it is usually the case that profits growth is also needed to provide the basis of the company's shares to be a good investment.

Croda is doing alright in this respect. Sales in 2017 were up by 10.4% with operating profits up by 11.4%. This was helped by favourable exchange rates as 95% of sales come from outside the UK. At constant currencies, sales were up by 4.6% and profits by 6.5%. That's a solid performance rather than a very good one.

Looking closer at the divisions, constant currency sales growth is reasonable. Profit growth at Life Sciences and Performance Technologies was very good. Personal Care - the biggest contributor to profits - saw a disappointing rate of profit growth at just over 3%.

2017 reported	Constant	2016		currency change	Restated [1] GBPm
		currency	Year on year change		
		GBPm			
Sales					
Personal Care		466.6	+10.9%	+5.3%	420.6
Life Sciences		322.6	+10.4%	+4.6%	292.2
Performance Technologies		456.9	+12.6%	+6.6%	405.6
Core Business		1,246.1	+11.4%	+5.6%	1,118.4
Industrial Chemicals		127.0	+1.4%	(4.0)%	125.2
Group		1,373.1	+10.4%	+4.6%	1,243.6
		2017 reported		Constant	2016
		currency		currency	
			Year		Restated [1]
		GBPm	on year		GBPm
			change		
Adjusted profit					
Personal Care		155.5	+8.7%	+3.3%	143.1
Life Sciences		97.0	+18.3%	+14.0%	82.0
Performance Technologies		75.4	+13.2%	+10.7%	66.6
Core Business		327.9	+12.4%	+8.0%	291.7
Industrial Chemicals		4.3	(33.8)%	(40.0)%	6.5
Operating profit		332.2	+11.4%	+6.9%	298.2
Net interest		(11.9)	+20.2%	+19.2%	(9.9)
Profit before tax		320.3	+11.1%	+6.5%	288.3

A closer look at Personal Care does show some encouraging trends. Investment in innovation seems to be paying off with new and protected products (NPPs) now accounting for 40% of sales on the back of a strong performance in active beauty products. The return to sales growth with big multinational customers is also a welcome development. Margins were down slightly due to a change in sales mix but still remained very high at just over 33%.

The seeds enhancement business in Life Sciences is doing well whilst sales of Crop Protection products picked up in the second half of the year. Profit margins increased nicely here from 28% to 30%.

The Performance Technologies business had a very good year with the strategy on premium, value added products paying off. Profit margins increased to 16.5% from 15.2%. Croda is targeting 20% profit margins for this business in the next few years.

Profits growth has been backed up with a decent cash flow performance with operating profits converted into operating cash flow.

	Note	2017 GBPm	2016 GBPm
Cash generated from operations			
Adjusted operating profit		332.2	298.2
Exceptional items		(1.7)	(8.4)
Acquisition costs and amortisation of intangible assets arising on acquisition		(4.5)	(4.2)
Operating profit		326.0	285.6
Adjustments for:			
Depreciation and amortisation		53.3	49.2
Loss on disposal of property, plant and equipment		1.5	0.9
Share of loss of associate		0.1	-
Net provisions charged		1.3	4.3
Cash paid against operating provisions		(2.2)	(0.7)
Movement in inventories		(31.0)	8.4
Movement in receivables		(14.4)	(10.9)
Movement in payables		12.1	9.7
Non-cash pension expense		3.4	(10.9)
Share based payments		9.2	9.5
Cash generated by continuing operations		359.3	345.1
Interest paid		(13.9)	(11.1)
Tax paid		(82.9)	(70.2)
Net cash generated from operating activities		262.5	263.8

Note that there was a £31m cash outflow from a build up of inventories to fulfil orders after the year end. This is a good reason for a stock build up rather than a worrying sign of falling demand. This led to a £39.4m negative swing in trading cash flow for the year. I would expect that this effect may not be as negative in 2018 but that will depend on the timing of orders and sales.

Croda International PLC (CRDA)						
FORECASTS			£ millions unless stated			
Year	2018		2019		2020	
Turnover	1,397.3	+1.8%	1,456.6	+4.3%	1,518.5	+4.2%
EBITDA	410.6	+8.2%	437.4	+6.5%	464.0	+6.1%
EBIT	355.0	+8.9%	377.2	+6.2%	400.1	+6.1%
Pre-tax profit	339.1	+7.4%	365.3	+7.7%	387.6	+6.1%
Post-tax profit	266.0	+11.5%	268.2	+0.8%	286.4	+6.8%
EPS (p)	186.5	+3.5%	200.2	+7.3%	216.1	+7.9%
Dividend (p)	90.8	+12.1%	107.3	+18.2%	149.4	+39.2%
CAPEX	73.4	-53.9%	72.6	-1.1%	73.4	+1.2%
Free cash flow	240.0	+131.2%	233.8	-2.6%	253.7	+8.5%
Net borrowing	145.0	-62.0%	222.0	+53.1%	312.5	+40.8%

Going forward, the company has built up a portfolio of new products to sell to its customers such as anti-ageing skin and sun protection products as well as new crop protection and seed enhancement products. In Performance Technologies, a new antimicrobial coatings product has been launched.

2018 will also see its biosurfactant plant start churning out eco friendly products.

The company is also stepping up its investment in research & development as the growth of NPPs has slowed down and is below the target of twice the rate of non-NPP sales. The company doesn't perform all its own research but partners with universities and specialist research laboratories. It also co-invests with technology businesses.

I like this approach but it does need to produce results in the form of higher sales and profits.

2018 is going to see the effects of favourable exchange rates probably disappear. Given that assumption, sales and profit growth may be quite low.

I'm a fan of this business and like its strategy but it needs to step things up a bit in my view. I think it is a very high quality business but the price tag of 24 times one year forecast rolling EPS is quite rich.

Gocompare.com (LSE:GOCO)

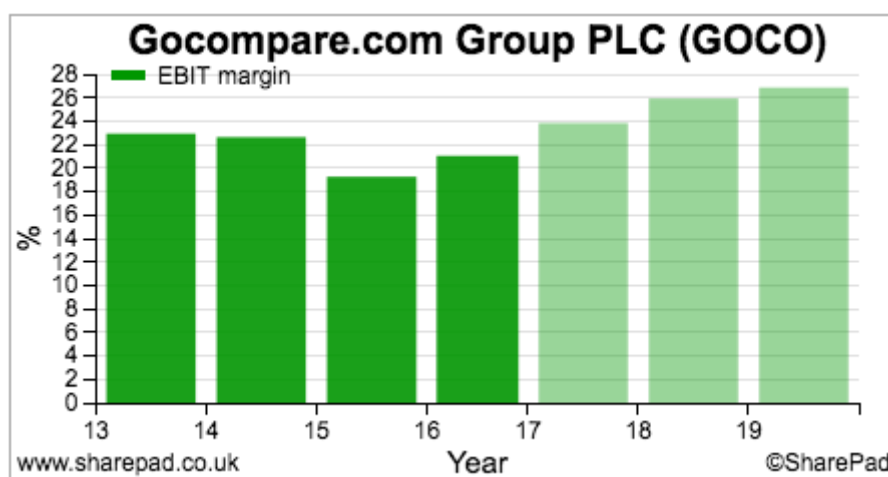


If you watch television then it's highly unlikely that you haven't heard of the price comparison website Gocompare. Its adverts are quite possibly the most irritating you have ever seen but as an example of a company getting its name in people's heads they are a masterstroke.

The company was split off from esure in 2016 and largely specialises in the price comparison of insurance products. It has recently bought a business selling voucher codes in order to diversify its revenue stream and cross sell products to its customer base.

Businesses based around websites can be very attractive propositions for investors. Once set up, they tend to not require large amounts of capital investment to maintain. If they can attract enough customers and generate meaningful revenues they can be very profitable. You only have to look at businesses such as Rightmove and Just Eat to see what can be achieved.

Gocompare is also a very profitable business with very high profit margins which analysts expect to go higher.



2017 was a decent year for the company with revenue up 5.1% as average revenue per transaction (the commission paid to the company by insurance companies) increased by 4.9% to £4.67 and the number of customer interactions increased by 0.8% to 32.2 million.

Given the high amount of fixed costs and operational gearing this led to operating profits being up by nearly 20%. As you can see, the company's costs barely changed in 2017.

Marketing costs and marketing margin

	2017 GBPm	2016 GBPm	Movement GBPm	Movement %
Cost of sales	42.5	41.2	1.3	3.1
Distribution costs	46.3	46.5	(0.2)	(0.4)
Total marketing spend	88.8	87.7	1.1	1.3
Marketing margin	40.5%	38.3%	+2.2%pts	

One of the important points to understand about price comparison websites is that they need to spend huge amounts of money on marketing their services to stay competitive. Gocompare spent nearly 60% of its revenues on marketing.

That is a huge amount of money but still very profitable if you look at the company's marketing margin (calculated as sales less marketing cost as a percentage of sales). It is also a possible sign of a large barrier to entry in this market. A new entrant would need to spend millions in order to gain a foothold in this market and take business of the existing players.

The marketing requirements may also explain why Gocompare was recently bid for by ZPG, the owner of the Zoopla and Uswitch websites. The profit gains from merging Uswitch and Gocompare and pooling the respective marketing budgets would probably be very attractive. This in turn probably explains why Gocompare rejected the bid saying it undervalued the business.

A look at the cash flow statement shows how cash generative Gocompare is as a business.

Only £2.3m was spent on investment (capex) in 2017 or around 7% of operating cash flow.

	Note	2017 GBPm	2016 GBPm
Cash flows from operating activities			
Profit for the year before tax		30.7	21.6
Adjustments for:			
Depreciation of property, plant and equipment	13	0.5	0.4
Amortisation of intangible assets	12	0.6	1.2
Loss on disposal of tangible assets	13	0.1	-
Share-based payment charge	24	2.7	0.1
Net finance costs	8	2.3	0.3
Changes in working capital:			
(Increase) in trade and other receivables	14	(2.0)	(1.0)
(Decrease) / increase in trade and other payables	16	(3.4)	10.4
Income tax paid		(6.1)	(4.8)
Net cash generated from operating activities		25.4	28.2
Cash flows from investing activities			
Purchase of property, plant and equipment	13	(0.8)	(0.4)
Purchase of intangible assets	12	(1.5)	(0.9)
Interest received	8	0.0	0.1
Purchase of equity investments	11	(2.5)	-
Net cash used in from investing activities		(4.8)	(1.2)
Cash flows from financing activities			
Proceeds from issuance of ordinary shares		-	0.1
Proceeds from borrowings, net of transaction costs	17	-	73.1
Repayments of borrowings	17	(10.0)	-
Interest paid		(1.6)	(0.4)
Dividends paid	25	(2.9)	(85.8)
Net cash used in financing activities		(14.5)	(13.0)
Net increase in cash and cash equivalents		6.1	14.0

Free cash flow for shareholders fell from £26.6m to £21.5m due to swings in working capital cash flows, mainly explained by a reduction in other payables. This equates to a free cash flow conversion ratio of 88% which is pretty decent.

From a financial performance point of view, Gocompare is a good business. However, it is not one without risks and growth challenges.

Its main weakness is its almost total reliance on insurance products. This can be good when insurance premiums are rising as it tends to encourage more switching activity but the company really does need to diversify.

The company has splashed out £36.5m to buy voucher codes business myvouchercode.co.uk. It will send emails to Gocompare customers offering them vouchers and discounts for products and will get commissions back from the businesses involved. This looks like a useful complementary business and taps into the existing money saving rationale of the company's customer proposition.

FORECASTS		£ millions unless stated				
Year	2018		2019		2020	
Turnover	171.4	+14.9%	182.7	+6.6%	197.4	+8.0%
EBITDA	47.2	+38.5%	52.4	+11.1%	57.7	+10.1%
EBIT	44.8	+35.6%	49.7	+11.1%	55.8	+12.2%
Pre-tax profit	41.9	+31.8%	47.3	+12.9%	53.4	+12.8%
Post-tax profit	34.2	+33.6%	39.0	+13.9%	45.3	+16.2%
EPS (p)	8.0	+33.8%	9.1	+13.7%	10.2	+12.1%
Dividend (p)	2.2	+214.3%	2.6	+18.2%	2.7	+3.8%
CAPEX	1.9	-19.3%	1.9	+4.3%	2.2	+12.3%
Free cash flow	34.1	+58.5%	38.6	+13.3%	43.9	+13.8%
Net borrowing	49.2	+25.1%	20.5	-58.3%	-17.2	
NAV	-9.8	-71.3%	16.9		47.6	+181.7%

The shares are not expensive on a rolling one year forecast rolling PE of 14.1 times given the current levels of expected profits growth. It is also possible that ZPG or another company may launch another bid for the company - particularly one that needs to beef up its insurance offer.

Howden Joinery (LSE:HWDN)



Share price: 113p

Mkt Cap: £477m

EMS: 5000

No of analysts: 7

Kitchen maker and seller Howden Joinery announced slightly better than expected profits on Thursday morning. That said, profits still fell slightly year on year due to the higher costs of imported supplies and the extra costs of a 53rd week.

The core UK depot business has performed well with like-for-like sales up by a healthy 5.2%. The company has been more open than many retailers by explaining that some of this growth is simply due to the maturation of depots opened in the last couple of years. It seems that growth picked up in the second half of the year but this should be interpreted in the context of the weak growth seen in the second half of 2016.

The company's French business performed well but is not big enough to be a significant driver of Howdens profits or share price at the moment.

Operating cash flow was also lower year on year. Investors should always be wary of increases in stock levels as it may be a sign of weakening demand or aggressive accounting (as overhead costs can be capitalised in some manufactured stock items which can boost profits) .

Consolidated cash flow statement		53 weeks to 30 December 2017 GBPm	52 weeks to 24 December 2016 GBPm
	Notes		
Group operating profit before tax and interest		234.4	237.2
Adjustments for:			
Depreciation and amortisation included in operating profit		28.0	24.0
Share-based payments charge		4.0	4.0
Loss/(profit) on disposal of property, plant and equipment, and intangible assets		0.2	(0.1)
Operating cash flows before movements in working capital		266.6	265.1
Movements in working capital			
Increase in stock		(24.6)	(6.6)
Increase in trade and other receivables		(1.9)	(6.4)
(Decrease)/increase in trade and other payables, and provisions		(0.4)	14.5
Difference between pensions operating charge and cash paid		(21.2)	(30.6)
		(48.1)	(29.1)
Cash generated from operations		218.5	236.0
Tax paid		(41.8)	(41.5)
Tax refund received		-	12.7
Net cash flow from operating activities		176.7	207.2

Howden saw a cash outflow of £24.6m due stock building which it has said was attributable to the launch of new product ranges. The company is also making extra payments into its final salary pension scheme to try and plug the deficit. The cash paid into the scheme was £21.2m greater than the pension expense in the income statement.

Despite capex being £15m lower than last year, free cash flow fell from £143.7m to £128.2m . This amounted to 69% of post tax profits.

Howden still has a very strong balance sheet. Even after spending £48m on share buybacks, there was still a £14.5m increase in cash balances to £241.1m. The company has no borrowings whatsoever but does have a pension fund deficit of £109m.

I like this prudent approach to financing by Howden. Kitchens are a cyclical business with demand highly dependent on consumer confidence and the strength of the economy. This company is very well placed to absorb any downturn in trading in the future.

Howden Joinery Group PLC (HWDN)

FORECASTS		£ millions unless stated				
Year	2017		2018		2019	
Turnover	1,385.9	+6.0%	1,450.1	+4.6%	1,525.0	+5.2%
EBITDA	257.0	-1.6%	270.9	+5.4%	290.5	+7.3%
EBIT	228.4	-3.7%	239.5	+4.8%	257.3	+7.4%
Pre-tax profit	226.7	-4.3%	236.8	+4.5%	253.5	+7.0%
Post-tax profit	179.7	-3.1%	187.3	+4.2%	201.4	+7.5%
EPS (p)	29.0	-1.3%	31.0	+6.9%	33.5	+8.1%
Dividend (p)	11.3	+5.6%	12.0	+6.2%	12.8	+6.7%
CAPEX	64.6	+1.7%	49.9	-22.8%	48.2	-3.3%
Free cash flow	116.4	-19.4%	153.7	+32.1%	166.2	+8.1%
Net borrowing	-215.3	+54.5%	-251.2	+16.7%	-323.1	+28.6%
NAV	453.9	+14.3%	504.1	+11.1%	565.0	+12.1%

Current trading seems to be very good. Sales growth for the first two months of 2018 is up by 12.5%. Average annual sales growth on a two year basis is also very healthy at 7.9%. What is encouraging is that the growth seen in the early weeks of 2018 has all come from selling more products as prices have not been increased.

The company is set to open 30 new depots this year and still thinks that there is room for another 140 in the UK which would take the total up to 800.

Costs are still expected to be an issue in 2018. Opening more depots will cost more money than in 2017. The company has also said that its cost of goods sold will increase and there will be an extra £20m of costs from IT, distribution and depreciation.

Given the current strength of sales this should not be a problem and seems to suggest that profits will start growing again in 2018. Whether that is by more than current forecasts remains to be seen.

I continue to believe that Howden Joinery is a high quality and well managed business with high profit margins and good returns on capital. The shares trade on a rolling forecast one year PE of just over 14 times which is not expensive in absolute terms.

I do however have some concerns that the business is vulnerable to a decline in consumer spending and house prices. After a long period of favourable economic conditions it may become harder for it to keep growing. That said, current trading suggests that all is well for now.

Longer term, I think that Howden is a valuable asset that could lead to it being taken over. Howden has essentially eaten Kingfisher's (LSE:KGF) lunch in kitchens but I think that a merger of Howdens and Screwfix would make a lot of sense and could create a very high quality trade focused company.

XP Power (LSE:XPP)



Share price: 3190p

Mkt Cap: £602m

EMS: 150

No of analysts: 3

XP Power, the manufacturer of power control components continues to grow at an impressive rate. I think it has many of the hallmarks of an excellent business (see my analysis of the company [here](#)).

2017 was a great year for the business as underlying pre-tax profits grew by 26%. The order intake increased by an impressive 38%. Operating cash flow increased by much lower rate of 11.9%. This is due to £3.3m of acquisition costs being excluded (fair enough in my opinion) from underlying profits.

XP Power Limited Consolidated Statement of Cash Flows For the financial year ended 31 December 2017			
GBP Millions	Note	2017	2016
Cash flows from operating activities			
Profit after tax		28.6	21.5
Adjustments for			
-Income tax expense		3.6	6.3
-Amortisation and depreciation		5.9	4.6
-Finance charge		0.3	0.2
-Equity award charges, net of tax		0.4	0.3
-Fair value (gain)/loss of derivative financial instruments		(0.5)	0.2
-Unrealised currency translation (gain)/loss		(2.9)	5.0
Change in working capital, net of effects from acquisitions:			
-Inventories		(2.5)	(3.5)
-Trade and other receivables		(1.6)	(4.0)
-Trade and other payables		5.3	1.5
-Provision for liabilities and other charges		(0.8)	(0.1)
Cash generated from operations		35.8	32.0

The business seems to be doing well across most markets and geographies. However, after a series of profit forecast upgrades over the last year it seems that this source of share price momentum has disappeared given the tone of the outlook statement.

“We have started the new financial year well with continuing momentum in new orders and revenue. We intend to invest further capital expenditure in our business in key areas such as supply chain, manufacturing and systems to support the anticipated growth of our business. We currently anticipate that orders and revenue in 2018 will be above the level seen in 2017.”

That said, good levels of profit growth are still expected in 2018.

XPP is a good business but I do wonder how long the good times can last. Its financial reports constantly cite the growing threat of low cost competition in Asia. So far, the company has been able to respond with new value added products and moving to lower cost manufacturing countries such as Vietnam.

XP Power Ltd (XPP)						
FORECASTS			£ millions unless stated			
Year	2017	2018	2019			
Turnover	166.8	+28.5%	182.2	+9.2%	190.5	+4.5%
EBITDA	40.9	+24.8%	43.9	+7.2%	47.4	+8.0%
EBIT	35.9	+27.4%	39.4	+9.5%	42.6	+8.3%
Pre-tax profit	35.6	+26.2%	38.8	+9.0%	42.1	+8.5%
Post-tax profit	27.3	+25.8%	30.4	+11.2%	34.5	+13.7%
EPS (p)	141.5	+24.9%	158.4	+11.9%	178.1	+12.4%
Dividend (p)	76.7	+8.0%	81.0	+5.6%	86.0	+6.2%
CAPEX	9.0	+32.4%	10.3	+14.4%	8.9	-13.6%
Free cash flow	16.2	-21.7%	19.9	+22.5%	24.9	+25.7%
Net borrowing	11.2		7.3	-35.0%	-	
NAV	117.9	+11.1%	131.2	+11.3%	-	

But profit margins of nearly 22% are bound to continue to attract new entrants into XPP’s markets in my opinion. This and the cyclical nature of the capital equipment industry which it sells to is the main risk to future profits.

The share price has fallen back since the highs of last year and the forecast PE ratio has come down. The shares now trade on just under 20 times rolling one year forecast EPS. Despite XPP currently being very profitable, I’m not convinced that its shares will be re-rated upwards again as they were last year.

Nichols (LSE:NICL)



Share price: 1535p

Mkt Cap: £575m

EMS: 200

No of analysts: 4

I recently analysed [Nichols](#) in one of my stock watch articles. I think it's a very good business but have concerns that it is far too reliant on its Vimto brand and is struggling to deliver meaningful profits growth.

Nichols PLC (NICL)

FORECASTS

£ millions unless stated

Year	2017		2018		2019	
Turnover	128.2	+9.3%	135.3	+5.5%	140.1	+3.5%
EBITDA	32.3	+2.7%	33.7	+4.4%	35.2	+4.4%
EBIT	31.0	+2.3%	32.3	+4.1%	33.7	+4.4%
Pre-tax profit	31.1	+2.2%	32.4	+4.2%	33.8	+4.4%
Post-tax profit	25.4	+4.0%	26.8	+5.7%	28.1	+4.7%
EPS (p)	67.8	+2.6%	71.1	+4.9%	74.4	+4.6%
Dividend (p)	31.1	+6.1%	33.2	+6.8%	35.3	+6.3%
CAPEX	2.8	+12.6%	1.8	-36.4%	1.8	0.0%
Free cash flow	21.8	+21.6%	23.9	+9.8%	25.2	+5.4%
Net borrowing	-44.2	+11.2%	-56.4	+27.6%	-66.9	+18.7%

Full year adjusted profits before tax for 2017 came in slightly below expectations at £30.5m and showed virtually no growth compared with 2016. This was in line with the tone of the company's trading statement just before Christmas.

Profit margins have fallen from 26% to 23% due to industry cost pressures and the well flagged slowdown of trading in the Middle East.

Sales of Vimto have continued to be very strong as the company has refused to discount the product. Growth of 9% was far in excess of the UK soft drinks market where sales increased by

2.2%. Nichols may be very reliant on Vimto but with growth like this it isn't a problem at the moment.

The outlook statement is encouraging from a sales growth point of view - particularly for Vimto in the UK - but the profit outlook looks to be quite soft:

“In 2018, we expect to maintain the positive sales trend in the UK with the Vimto brand being supported by a new marketing campaign launching in the spring. In addition, we are well prepared for the introduction of the Sugar Levy with 100% of the Vimto and Feel Good brands portfolio already exempt from the levy.

In our international business, we are confident of continued sales growth in Africa, however, the current conflict in the Yemen coupled with a slowdown in the Saudi economy, suggests that sales to the Middle East region will soften in 2018.

In summary, the Group remains highly profitable and our diversified business model, strong balance sheet, and the resilience of the Vimto brand will continue to support the expected sales growth in 2018.”

My view on Nichols therefore remains the same as it was a few weeks ago. It's a good business but its shares are fairly priced given the modest profits outlook.