CentralNic Group

Interim results

Digital model delivers resilient growth

Software & comp services

CentralNic's H120 interims show revenue growth well ahead of our estimates (US$111.3m vs US$99.1m), with adjusted EBITDA marginally ahead (US$15.1m vs US$14.6m), driven by strong growth in the Indirect and Monetisation businesses, supported by the acquisitions completed in FY19. The group also delivered like-for-like organic growth of 18% in H120. The fall in gross margin from 40% to 32% reflects the change in business mix due to the strong performance of Indirect + Monetisation vs Direct (SME + Corporate), rather than margin pressure. Management reconfirmed its confidence in the full year results, noting a strong M&A pipeline and continuing organic growth. Accordingly, we have raised our FY20 revenue estimate by c 8% to US$218m from US$202m, while paring back gross margin expectations (new: 32.5%, old: 33.0%) and EBITDA margins (new: 14.1%, old: 15.1%). The valuation continues to look attractive.

Year end	Revenue (US$m)	PBT* (US$m)	EPS* (c)	DPS (c)	P/E (x)	Yield (%)
12/18	56.0	7.4	5.83	0.0	18.9	N/A
12/19	109.2	12.8	8.16	0.0	13.5	N/A
12/20e	217.8	17.4	6.20	0.0	17.7	N/A
12/21e	230.8	19.6	7.43	0.0	14.8	N/A

Note: *PBT and EPS are normalised, excluding amortisation of acquired intangibles, exceptional items and share-based payments.

H120 results: Strong top-line growth

CentralNic H120 revenue increased by 124% to US$111.3m (H119: US$49.7m), driven by contributions from the four acquisitions made in H219, Team Internet (Monetisation), Ideegeo (Direct), Hexonet and TPP Wholesale (both Indirect). Gross profit rose by 78% to US$35.2m (H119: US$19.7m), while gross margins fell from 40% to 32%, reflecting the change in business mix (each individual segment maintained its margins). Adjusted EBITDA increased by 64% to US$15.1m (H119: US$9.2m), a margin of 13.6% down from 18.6% in H119. Net debt was broadly flat at US$76.4m compared to US$76.8m at 31 March 2020.

Outlook: Growth, M&A and recurring revenues

Although as a group CentralNic achieved 18% pro forma revenue growth, the performance of the business segments differed materially. On a pro forma basis, Monetisation grew 38%, driven by a 33% higher RPM, Indirect rose 9% supported by an improved performance from TPP Wholesale and Hexonet under CentralNic's ownership, while Direct, which suffered most from a COVID-19 related slowdown, fell by 1%. Nevertheless, management remains confident in the outlook for FY20, given the group's high recurring revenues, strong cash conversion, continuing organic growth and a full pipeline of potential future deals.

Valuation: Discount unjustified given growth record

Despite its impressive historical (and continuing) track record of growth (five-year revenue CAGR of 69%), CentralNic trades on an FY20e P/E of 17.7x, a 21% discount to its global peers. As CentralNic consolidates a fragmented market of sub-scale, cash-generative businesses, we would expect earnings accretive M&A to bring multiples down further.

3 September 2020

Price	**82.0p**
Market cap	**£157m**
	£1.34/US$
Net debt (US$m) at 30 June 2020	76.4
Shares in issue	192.1m
Free float	46.1%
Code	CNIC
Primary exchange	AIM
Secondary exchange	N/A

Share price performance

%	1m	3m	12m
Abs	1.9	(4.4)	49.1
Rel (local)	2.5	(1.1)	78.6
52-week high/low		95.0p	40.0p

Business description

CentralNic Group is a leading global domain name services provider, operating through three divisions: Reseller (number two globally); Corporate; and SME. Services include domain name reselling, hosting, website building, security certification and website monetisation (added at the end of 2019).

Next events

Q3 trading update	December 2020
FY trading update	February 2021
FY20 results	April 2021

Analysts

Richard Williamson +44 (0)20 3077 5700

Russell Pointon +44 (0)20 3077 5757

tech@edisongroup.com

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H120 interim results

Strong top-line growth, margins lower on business mix

H120 revenue increased by 124% to US$111.3m (H119: US$49.7m), driven by contributions from the four acquisitions made in H219, Team Internet (Monetisation segment), Ideegeo (Direct segment), Hexonet and TPP Wholesale (both Indirect segment), with gross profit increasing by 78% to US$35.2m (H119: US$19.7m). Gross margins fell from 40% to 32%, reflecting the change in business mix, as each individual segment maintained its margins. Adjusted EBITDA increased by 64% to US$15.1m (H119: US$9.2m), a margin of 13.6% down from 18.6% in H119. Operating profit increased by 12% to US$3.2m (H119: US$2.9m), with a loss after tax of US$2.7m (H119: US$2.5m). The group reported adjusted EPS of 4.4 cents (H119: 3.9 cents).

H120 operating cashflow was US$5.7m (H119: outflow of US$1.4m) with net debt remaining broadly flat at US$76.4m (gross debt of US$104.0m, cash of US$27.6m) compared to net debt of US$76.8m at 31 March 2020. The company noted Q220 cash conversion of c 138%, higher than the historical average of 100% in what is typically a weaker quarter for cash conversion.

Impact of COVID-19: Demonstrable digital resilience

As has been noted, the group reported like-for-like organic growth of 18% in H120, with healthy demand driving growth in the Indirect and Monetisation segments, although the Direct segment did experience a slowdown in new business, leading to a small fall in like-for-like revenues. However, management took the necessary precautions to preserve cash and review its financing plans. The group experienced no major business interruptions from the pandemic, with staff transitioning to remote working painlessly. As a provider of online subscription services for digital products, serving a global customer base, the group does not anticipate any major impact from COVID-19. Management continues to monitor global developments carefully.

Organic growth: H120 pro forma growth of 18%

Alongside its H120 results, management also calculated pro forma H119 figures to highlight the underlying organic growth of the business. Based on these figures, revenue grew by 18%, gross profit increased by 14% and adjusted EBITDA rose by 16%.

As management has previously provided guidance based around its estimated organic growth of c 6%, it is notable that CentralNic achieved 18% growth on a pro forma basis in H120 (a period where the business has been affected by COVID-19), which is consistent with and updates the 15% pro forma growth estimate for Q119–Q120 discussed at the capital markets day. The group's auditors are expected to report on organic growth later in the year to provide a better estimate of historical organic growth rates and we look forward to the conclusion of this exercise.

Segmental analysis: Indirect, Direct and Monetisation

Reflecting the new shape of the business following the acquisitions in FY19, the group has reorganised around three segments as outlined at the Capital Markets Day in July: 1) Indirect, replacing the Reseller division and incorporating CentralNic's wholesale and registry business selling to domain name retailers; 2) Direct (the former Small Business and Corporate segments), retailing domain names and value-added services direct to businesses; and 3) Monetisation, the new domain monetisation business for domain investors acquired with Team Internet.

- **Indirect**: The Indirect segment grew significantly following the acquisitions of TPP Wholesale and Hexonet in FY19. The segment reported revenues of US$41.2m, a 62% increase over H119 (H119: US$25.5m), with 9% organic growth reported on a pro forma basis.
- **Direct**: Revenue in the Direct segment decreased by 11% to US$21.6m (H119: US$24.2m), despite a positive contribution from the acquisition of Ideegeo, with the data centre business moved to Indirect and Monetisation broken out separately. On a pro forma basis, the segment saw a 1% fall in organic growth. Given its healthy client pipeline, management is confident that the segment will return to growth in H220.
- **Monetisation**: Monetisation was the fastest growing segment with revenue rising 38% to US$48.5m (H119: US$35.0m), driven by a 33% increase in the average yield (revenue per thousand impressions (RPM)). The higher RPM reflected both higher-quality traffic following CentralNic's cleansing of the business on acquisition, as well as the implementation of Team Internet's new SSL monetisation technology.

Update to our estimates: Higher revenue growth, lower margins

As we indicated in our Flash note at the start of August, we proposed to review our estimates after the H120 interim results. We had previously factored in a slowdown in our estimates in Q220 over Q120 due to the impact of the COVID-19 pandemic, particularly affecting Team Internet's ad-driven revenues. However, now that we have seen the business breakdown, Team Internet's growth has remained robust, with the Direct segment pausing over the pandemic.

Nevertheless, the balance of both strong organic growth and a significant contribution from acquisitions left revenue well ahead of our old H120 estimates (US$111.3m vs US$99.1m), with adjusted EBITDA marginally ahead (US$15.1m vs US$14.6m), reflecting the fall in blended EBITDA margin.

As such, we are revising our estimates, reflecting the following principal changes:

- **Revenue growth** – with the strong H120 revenue performance implying a simple annualised revenue run-rate of US$223m, we have conservatively increased our FY20 revenue estimate by c 8% to US$218m. Retaining management's 6% organic growth estimate, FY21 and FY22 revenue estimates increase to US$231m and US$245m, respectively.
- **Gross margin** – with gross margins falling to c 32% in H120, due to the particular business mix, with the lower-margin segments out-performing the higher-margin Direct segment, we have adjusted our FY20e gross margins to 32.5%, assuming a return to growth in the Direct segment in H220, rising to 33% in FY21e and FY22e.
- **EBITDA and EBITDA margins** – H120 EBITDA of US$15.1m was c 3% ahead of our H120 estimate (US$14.6m), as the H120 business mix affected EBITDA margins. We have chosen to leave our EBITDA estimate for FY20 broadly as is, reflecting a lower margin assumption for the year than previously. Our FY20e EBITDA margin correspondingly falls from 15.1% to 14.1%, rising to 14.3% in FY21 and 14.6% in FY22 (previously 14.9% and 15.0%, respectively).
- **Working capital** – with significant changes to the business over the past 12 months, including the acquisitions in H219, the anticipated working capital picture has been slightly unclear. We have taken advantage of the change in our estimates to bring our working capital assumptions into line with the H120 interim balance sheet now that the business has settled.

Exhibit 1: Edison's revised estimates

Year end 31 December US$'000	Old 2020e	H120a	H220e	New 2020e	*Change*	Old 2021e	New 2021e	*Change*	Old 2022e	New 2022e	*Change*
Revenue	202,480	111,251	106,572	217,823	7.6%	214,406	230,824	8%	227,225	244,709	8%
Gross profit	66,818	35,199	35,593	70,792	6%	70,754	76,172	8%	74,984	80,754	8%
EBITDA	30,670	15,096	15,574	30,670	-	31,952	32,944	3%	34,156	35,832	5%
Normalised operating profit	31,815	14,125	16,277	30,402	(4)%	31,476	27,908	(11)%	32,964	29,204	(11)%
Profit before tax (norm)	18,936	9,470	7,953	17,423	(8)%	23,399	19,628	(16)%	25,188	21,326	(15)%
Profit before tax (reported)	9,482	(1,418)	3,887	2,469		13,773	10,021	(27)%	15,381	11,523	(25)%
Reported tax	(5,043)	(1,313)	(2,240)	(2,729)		(5,171)	(3,857)		(5,628)	(4,278)	
Net income (normalised)	12,752	5,808	5,808	11,617	(9)%	17,055	14,265	(16)%	18,199	15,379	(15)%
Shares outstanding (m)	185,428	184,435	187,269	187,269	1%	188,370	192,052	2%	188,370	192,052	2%
EPS - basic normalised (c)	6.87	3.15	3.10	6.20	(10)%	9.05	7.43	(18)%	9.66	8.01	(17)%
Revenue growth (%)	85.4	75.3	155.9	99.5		5.9	6.0		6.0	6.0	
Gross margin (%)	33.0	31.6	33.4	32.5		33.0	33.0		33.0	33.0	
EBITDA margin (%)	15.1	13.6	14.6	14.1		14.9	14.3		15.0	14.6	
Normalised operating margin (%)	15.7	12.7	15.3	14.0		14.7	12.1		14.5	11.9	
Capex	(3,037)	(180)	(2,107)	(2,287)	(25)%	(3,216)	(3,001)	(7)%	(3,408)	(3,181)	(7)%
Closing net debt/(cash)	69,967	76,428	75,991	75,991	9%	59,441	69,925	18%	46,196	62,640	36%

Source: CentralNic accounts, Edison Investment Research

Valuation: Persistent discount to peer group

CentralNic continues to trade at a material discount to its peers. Disregarding Verisign, which we include for completeness, the peer group in Exhibit 2 trades at average EV/sales multiples of 3.1x for FY1 and 2.9x for FY2 and EV/EBITDA multiples of 13.5x for FY1 and 12.2x for FY2. In terms of P/E, the peer group trades at 22x for FY1 and 29x for FY2. CentralNic is displaying the strongest growth in the group and yet trades on an FY20 P/E multiple of 17.7x and an FY21 P/E multiple of 14.8x, a discount to the peer group average of 21% and 48% respectively.

Exhibit 2: Peer group table

Company	Year end	Share price	Quoted Ccy	EV ($m)	Sales Growth FY1 (%)	Gross margin FY1 (%)	EBITDA margin FY1 (%)	EBIT margin FY1 (%)	EV/ sales FY1(x)	EV/ sales FY2 (x)	EV/ EBITDA FY1 (x)	EV/ EBITDA FY2 (x)	P/E 1FY (x)	P/E 2FY (x)
Verisign Inc	Dec-20	214.8	US$	25,265	2.4	85.7	69.4	65.2	20.0	18.8	28.9	26.9	31.8	36.7
GoDaddy Inc	Dec-20	83.7	US$	15,674	10.1	64.6	20.6	7.2	4.8	4.3	23.1	19.3	NM	52.2
Endurance International Inc	Dec-20	6.5	US$	2,431	(1.1)	58.1	27.4	13.3	2.2	2.1	8.1	8.0	NM	NM
iomart group PLC	Mar-21	360.0	GBp	602	3.4	61.0	37.9	21.5	3.9	3.7	10.2	9.7	21.8	20.7
IMImobile PLC	Mar-21	410.0	GBp	484	1.3	49.6	12.9	9.1	2.1	2.0	16.2	14.7	30.9	27.8
R22 SA	Jun-21	33.1	PLN	173	20.0	NULL	27.1	19.2	2.7	2.5	10.1	9.2	14.3	14.1
Mean (ex Verisign)					**6.7**	**58.3**	**25.2**	**14.1**	**3.1**	**2.9**	**13.5**	**12.2**	**22.3**	**28.7**
Mean					**6.0**	**63.8**	**32.6**	**22.6**	**5.9**	**5.6**	**16.1**	**14.7**	**24.7**	**30.3**
Median					**2.9**	**61.0**	**27.3**	**16.2**	**3.3**	**3.1**	**13.2**	**12.2**	**26.4**	**27.8**
CentralNic Group Plc	Dec-20	82.0	GBp	286.3	99.5	32.5	14.1	7.1	1.3	1.2	9.3	8.7	17.7	14.8
CNIC Discount/(Premium) to Mean (ex Verisign)									58%	58%	31%	29%	21%	48%

Source: Refinitiv data as at 2 September 2020, CentralNic Edison Investment Research estimates

Outlook

Based on CentralNic's H120 figures, management restated its confidence in the full year results, noting a strong pipeline of future deals and continuing organic growth. Management also believes that the net debt position is sustainable given the profitability of the group (with high recurring revenues and strong cash conversion) and the expected continuing positive contribution from the FY19 acquisitions.

Exhibit 3: Financial summary

	2018	2019*	2020e	2021e	2022e
Year end 31 December	IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT	US$'000	US$'000	US$'000	US$'000	US$'000
Revenue	55,991	109,194	217,823	230,824	244,709
Cost of Sales	(30,080)	(66,419)	(147,031)	(154,652)	(163,955)
Gross Profit	25,911	42,775	70,792	76,172	80,754
EBITDA	9,146	17,920	30,670	32,944	35,832
Normalised operating profit	8,820	16,614	30,402	27,908	29,204
Amortisation of acquired intangibles	(5,600)	(8,299)	(9,423)	(9,607)	(9,803)
Exceptionals	(6,362)	(7,431)	(2,797)	-	-
Share-based payments	(469)	(2,878)	(2,734)	-	-
Reported operating profit	(3,611)	(1,994)	15,448	18,300	19,401
Net Interest	(1,430)	(3,869)	(7,179)	(7,280)	(7,178)
Joint ventures & associates (post tax)	45	74	-	-	-
Exceptionals	-	-	(5,800)	(1,000)	(700)
Profit Before Tax (norm)	7,435	12,819	17,423	19,628	21,326
Profit Before Tax (reported)	(4,996)	(5,789)	2,469	10,021	11,523
Reported tax	(1,428)	39	(2,729)	(3,857)	(4,278)
Profit After Tax (norm)	7,435	14,227	11,617	14,265	15,379
Profit After Tax (reported)	(6,424)	(5,750)	(260)	6,163	7,245
Minority interests	5	64	-	-	-
Discontinued operations	-	-	-	-	-
Net income (normalised)	7,440	14,291	11,617	14,265	15,379
Net income (reported)	(6,419)	(5,686)	(260)	6,163	7,245
Basic average number of shares outstanding (m)	127,515	127,515	175,084	187,269	192,052
EPS - basic normalised (c)	5.83	8.16	6.20	7.43	8.01
EPS - diluted normalised (c)	5.56	7.92	6.03	7.22	7.79
EPS - basic reported (c)	(5.03)	(3.25)	(0.14)	3.21	3.77
Dividend (c)	0.00	0.00	0.00	0.00	0.00
Revenue growth (%)	75.3	155.9	99.5	6.0	6.0
Gross Margin (%)	46.3	39.2	32.5	33.0	33.0
EBITDA Margin (%)	16.3	16.4	14.1	14.3	14.6
Normalised Operating Margin	15.8	15.2	14.0	12.1	11.9
BALANCE SHEET					
Fixed Assets	132,321	217,544	212,697	204,893	197,001
Intangible Assets	127,267	206,055	198,260	190,961	183,605
Tangible and Right-of-use Assets	931	6,427	10,014	9,509	8,973
Investments & other	4,123	5,062	4,423	4,423	4,423
Current Assets	51,378	67,433	66,296	79,264	93,701
Stocks	3,906	491	545	1,154	1,224
Debtors	24,382	40,760	37,683	43,976	51,059
Cash & cash equivalents	23,090	26,182	28,068	34,134	41,419
Other	-	-	-	-	-
Current Liabilities	(62,443)	(78,767)	(74,984)	(75,039)	(75,098)
Creditors	(59,719)	(75,683)	(68,394)	(68,394)	(68,394)
Tax and social security	(452)	-	-	-	-
Short term borrowings	(2,272)	(3,084)	(6,590)	(6,645)	(6,704)
Other	-	-	-	-	-
Long Term Liabilities	(43,188)	(129,206)	(128,384)	(129,864)	(131,444)
Long term borrowings	(22,933)	(102,799)	(101,616)	(101,809)	(102,014)
Other long term liabilities	(20,255)	(26,407)	(26,768)	(28,055)	(29,430)
Net Assets	78,068	77,004	75,625	79,254	84,160
Minority interests	(5)	69	-	-	-
Shareholders' equity	78,063	77,073	75,625	79,254	84,160
CASH FLOW					
PBT	(4,996)	(5,789)	2,469	10,021	11,523
Depreciation and amortisation	5,926	9,605	10,553	10,805	11,073
Share-based payments	469	2,878	-	-	-
Working capital	7,783	8,136	(4,266)	(6,902)	(7,152)
Exceptional & other	2,650	3,795	7,179	7,280	7,178
Tax	(3,015)	(2,309)	(2,729)	(3,857)	(4,278)
Net operating cash flow	8,817	16,316	13,206	17,346	18,344
Capex	(4,920)	(15,497)	(2,287)	(3,001)	(3,181)
Acquisitions/disposals	(27,568)	(63,840)	(5,800)	(1,000)	(700)
Net interest	(682)	(1,970)	(7,179)	(7,280)	(7,178)
Equity financing	30,869	2,133	4	-	-
Dividends	-	-	-	-	-
Other	-	-	-	-	-
Net Cash Flow	6,516	(62,858)	(2,056)	6,066	7,285
Opening net debt/(cash)	8,667	2,115	74,998	75,991	69,925
FX	(1,374)	(10,974)	1,063	-	-
Other non-cash movements	1,410	949	-	-	-
Closing net debt/(cash)	2,115	74,998	75,991	69,925	62,640

Source: Company accounts, Edison Investment Research. Note: *FY19 figures have been restated to reclassify FX on borrowings and administrative expenses to finance costs and other income respectively.

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Frankfurt +49 (0)69 78 8076 960
Schumannstrasse 34b
60325 Frankfurt
Germany

London +44 (0)20 3077 5700
280 High Holborn
London, WC1V 7EE
United Kingdom

New York +1 646 653 7026
1,185 Avenue of the Americas
3rd Floor, New York, NY 10036
United States of America

Sydney +61 (0)2 8249 8342
Level 4, Office 1205
95 Pitt Street, Sydney
NSW 2000, Australia