1pm plc

Give credit where it is due

1pm's IFRS9 update highlighted the conservatism in current provisioning, with a minimal impact from adopting the new standard. We have taken the opportunity to review credit and present a range of scenarios (from maintaining current low losses through to a hard recession) and the impact each would have on 1pm's earnings. The key business message is that, in almost all our scenarios, 2019E profit would be well above the 2017 level. A hard-landing scenario, with losses 1.5x the current IFRS9 worst-case scenario and 4.3x the current level, would see EPS 19% below the 2017 level, and the P/E would be 10x for bottom-of-the-cycle earnings.

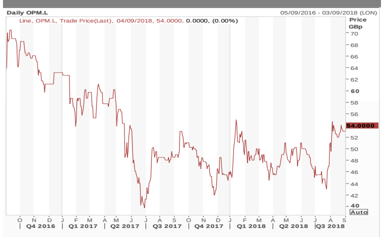
- **IFRS9 impact:** On 5 September, 1pm advised that its adoption of IFRS9 would increase provisions from 1.5% to 1.6%. The impact on equity is 0.25%, compared with 1.5% at Orchard Finance, ca 5%-6% at NSF and MCL, 13% at Amigo and 34% at Provident Financial. This reflects 1pm's historical conservatism.
- **Credit review:** We provide a range of scenarios, and their impact, against 2017 EPS. These include current impairments continuing (EPS up 38%), our base case (EPS up 28%), impairments at the IFRS9 worst-case level (EPS 1% lower) and impairments at 4.3x current levels (1.5x IFRS9 worst-case, EPS down 19%).
- **Risks:** Credit risk is a key factor and is managed by each business unit according to its own specific characteristics, with a group overview of controls. Funding is widely diversified and at least matches the duration of lending. Acquisitions would appear well priced, and delivery of synergies provides earnings upside.
- **Valuation:** We detailed the assumptions in our valuation approaches in our initiation note, "Financing powerhouse: a lunchtime treat". The GGM indicates 103p and the DDM 73p (DDM normal payout 81p). The 2019E P/E (6.4x) and P/B (0.8x) appear an anomaly with 1pm's profitability, growth and downside risk.
- **Investment summary:** 1pm offers strong earnings growth, in an attractive market, where management is tightly controlling risk. Targets to more than double the market capitalisation appear credible, with triggers to a re-rating being both fundamental (delivery of earnings growth, proof of cross-selling) and sentiment-driven (payback for management actively engaging the investor community). Profitable, growing companies generally trade well above NAV.

Financial summary and valuation

Year-end May (£000)	2015	2016E	2017E	2018E	2019E
Revenue	5,534	12,554	16,944	29,596	32,946
Cost of sales	-2,503	-4,480	-6,094	-9,849	-10,820
Admin. expenses	-1,394	-4,290	-6,469	-10,834	-11,983
Operating profit	1,637	3,418	4,121	8,619	9,822
Pre-tax profit	1,620	3,346	4,080	7,946	9,048
Adj. EPS (p)	3.7	6.5	6.5	7.9	8.3
Total receivables	24,991	56,061	73,955	150,893	169,000
Eq. to receivables	49%	43%	39%	32%	33%
Shares in issue (m)	36.9	52.5	54.9	86.4	88.5
P/adj. earnings (x)	14.1	8.1	8.1	6.7	6.3
P/B (x)	1.6	1.2	1.0	0.9	0.8
Dividend yield	0.7%	1.0%	1.0%	1.2%	1.6%

Source: Hardman & Co Research

Financials



Source: Eikon Thomson Reuters

Market data

EPIC/TKR	**OPM**
Price (p)	52.5
12m High (p)	55.0
12m Low (p)	42.0
Shares (m)	83.8
Mkt Cap (£m)	44.0
EV (£m)	43.1
Free Float*	51%
Market	AIM

**As defined by AIM Rule 26*

Description

1pm is a finance company/broker providing over 16k UK SMEs with a variety of products, including loans, lease, hire purchase, vehicle and invoice finance. Advances range from £1k-£500k. The company distributes directly, via finance brokers and vendor suppliers.

Company information

CEO	Ian Smith
CFO	James Roberts
Chairman	John Newman

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www.1pm.co.uk

Key shareholders

Lombard Odier (31/5/18)	22.84%
Sapia Partners (31/5/18)	12.66%
Ronald Russell (director 27/10/17)	12.25%
Mike Nolan (director 31/5/18)	6.30%
Charles Stanley (31/5/18)	3.53%

Diary

12 Sep	FY'18 results

Analyst

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IFRS9 impact

Overall impact minimal. IAS39 stock of provisions 1.5%, IFRS9 stock 1.6%.

On 5 September 2018, 1pm announced that "had the Standard applied to the year ended 31 May 2018, the estimated impact on the Group's financial results would have been negligible." It further advised that, as at 31 May 2018, the group held IAS39 impairment provisions equal to 1.5% of the entire lending portfolio. Had IFRS9 been adopted, a provision of 1.6% of the portfolio would have been required, derived from a range of scenarios of between 1.3% and 2.8% in the group's best- and worst-case scenario modelling. As the probability of the worst-case scenario is small, the level of required provisions is not that sensitive to this scenario. For most growing businesses, the move to IFRS9 has seen an increase in provisions (in both the balance sheet and the profit & loss), as IFRS9 impairment provisions are recognised on the inception of any lending and based on the probability of expected default. This has not been the case for 1pm, because:

Conservative general provisioning

- The group currently adopts the prudent policy of maintaining and, where deemed appropriate, increasing an additional general provision for potential future losses. 1pm has not historically disclosed the level of this "incurred but not yet reported" (IBNR) provision, but the fact that the stock of provisions was rising at a time of good credit conditions means it should not be a surprise.

Prudent in specific provisions shown by high recovery levels

- Management has also been prudent when taking specific impairments. It has historically reported material recovery rates, which would support the assertion of conservatism. In essence, it has been taking provisions upfront and then releasing them later, but this has had the effect of increasing the ongoing stock of provisions. We understand that the recovery rate under personal guarantees is ca.75% over time. This is materially better than the mainstream banking market, and reflects the fact that most loans are small and so payments under personal guarantees are still manageable for the borrowers. On current policies, the full amount would be provided, with the recovery under personal guarantees being recognised only when payments have been received.

IFRS9 accelerates impairment to loan origination but also accelerates recoveries

- IFRS9 requires the recognition of impairments on client receivables through an expected loss model. This differs from IAS39, which follows an incurred loss model, with specific provisions being reflected when there is 'objective evidence of impairment'. Using an expected loss has resulted in greater value being given for the material level of recoveries that 1pm has historically achieved.

IFRS9 has more cyclicality, but recognising recoveries earlier is partial offset to this volatility

- The recognition of recoveries (based off historical experience) should also limit the cyclical nature of IFRS9. The technical calculations apply probability weightings to different scenarios, and the worst-case scenario has more weighting in a recession than it does in good conditions. As the present value of recoveries over some years will now be recognised, the scale of loss is, however, modest (the worst-case loss is 2.1x the best case).

No impact on recoveries

- We note the company's comment that there will be no impact on revenue recognition. This is in line with most non-standard lenders who have reported modest, if any, net effects on revenues from the recognition of income on impaired assets.

No change in fundamental value of group or its cashflows

It is worth emphasising that there is no change in the underlying profitability of the group, nor on its cashflows. The 2018 numbers have not been audited, but we understand that 1pm's assumptions have been made after discussions with both its auditors and also independent advisors to ensure market consistency.

Credit risk management key

Summary

Risk management tailored to specific exposures in each business, with primary responsibility in the business units

We detailed how 1pm manages credit on pages 21-26 of our initiation report, Financing powerhouse: a lunchtime treat published on 12 September 2017. Each of 1pm's risk-taking businesses finance different asset types (Onepm Finance and Academy soft assets, Bradgate hard assets), offer different products (loans, leases, invoice finance) and have a different core customer base (in credit quality terms but also by sector). There is even geographical diversity with its inherently different risks. Each business therefore adopts credit policies and underwriting processes appropriate to its own needs, as no one credit policy will fit all businesses in the group. At the group level, the Chief Operating Officer on the 1pm plc board has accountability for credit decisions, and the group Head of Credit reports to him, sitting on the group's Operating Board. The 'Platform1' digital capability project is designed to achieve 'one customer view' across the group for credit purposes. Implementation will be completed in the current calendar year.

Number of factors make 1pm below-average risk

Some above-average risk characteristics

Risk-adjusted returns look good

There are a number of factors why we believe 1pm may be considered low-risk: i) broking capacity; ii) no commercial property lending (broking only); iii) a very broad portfolio of small exposures; iv) no specific sector concentration, but sectoral knowledge of smaller SMEs, including 'high-street' businesses; v) repayments by regular direct debit; vi) invoice finance requires double failure for major losses; and vii) demand and pricing are likely to increase in macro-uncertain times. There are also some factors that indicate above-average risk, including: i) Onepm Finance is wholly reliant on broker-introduced business; ii) some lending to higher-risk startups/impaired credits, but subject to appropriate security; iii) some exposure to cyclical sectors; iv) acquired assets often riskier than self-originated; v) not a bank, so no current account real-time data; and vi) rapid growth. Overall, we believe 1pm's lease and loan book are above-average risk, but this is more than compensated for by an above-average yield and the ability to broke-on for immediate cash and profits, as well as the positive mix effects of a significant invoice discounting business.

Continuing current low loss rate ca.8% profit upside vs. base case. Even at 1.5x worst-case IFRS9 loss rate (ca.4.3x current level), fall in profits is just 36%.

Less impact in 2020 as that year has full period income from 2019 lending

In this report, we provide detailed sensitivity analysis to our 2019 estimates, assuming a range of scenarios from continuing current low loss rates through to an extreme hard landing. We note that the effect on 2020 would be lower, as 2019 does not give full-year income recognition for loans and leases made that year, but it will include the impairment provision on the receivable origination. Even where impairments are 1.5x the level of the reported worst-case scenario, profits under our assumptions would fall by a modest 36%. Investors could question whether the low share price would be justified by such a limited downside risk.

Where 1pm is below-average risk

Some factors give 1pm a lower risk profile than the SME financing average because of i) broking capacity, ii) no commercial property, iii) broad portfolio of small exposures, iv) sectoral knowledge in smaller SMEs, v) repayments by direct debit, vi) invoice finance requires double failure for major losses, vii) demand likely to increase in macro-uncertain times

1pm has some characteristics that should see credit risk lower than the average for SME financing as a whole. These include:

- Having a group with broking capacity means 1pm can rapidly respond to any market deterioration and reduce its on-balance sheet incremental risk without compromising customer relationships.

- No direct exposure to commercial property (by far the single most destructive sector for the banking system).

- Broad portfolio of lending, with the maximum exposure to any specific name well under 0.5% of the group's book.

- Sectoral knowledge is likely to be greater, giving an advantage when assessing lending into areas like independently-owned restaurants, motor garages or healthcare and beauty, including a small proportion of startup businesses.

- All facilities are repaid by direct debit, meaning that most problems can be identified on the day a direct debit becomes overdue, and addressed and typically resolved within a month.

- In most cases, invoice finance receivables require a double failure (both of the invoice payer and the borrower) before losses are incurred. We note that the losses since inception at Gener8 and Positive Cashflow are exceptionally low.

- In times of macro-economic stress, mainstream bank appetite to lend typically falls – meaning that more customers become available for 1pm. There is also some ability to re-price for the higher risk. We note that non-standard consumer lenders, such as Provident Financial (2007 profit £115m, 2009 £130m) or S&U (2007 profit £6m, 2009 £6m), saw rising or stable profits, as increased demand and wider margins offset higher credit impairments.

- The historical peak losses (2010 at ca.6% of receivables) arose from the sub-prime lending model before the financial crisis which led to losses in those years. Post the financial crisis, management changed the lending model to become a prime and near-prime lender – so losses have reduced steadily since then, and this level of peak loss is highly unlikely to recur. The invoice financing portfolios in Gener8 and Positive Cashflow, whose minimal cumulative losses we highlighted above, should also reduce the group's overall stress scenario loss ratio.

- 65% of invoice financing at Gener8 and Positive Cashflow are on a "confidential" basis, where the cash is paid into a bank account in the name of the customer, but it is a trust account controlled by 1pm. This is considered by some as higher-risk than the 35% of business that is "disclosed", as 1pm is not talking to the underlying invoice payer on a daily basis. However, confidential customers tend to be bigger, better, and more established companies, and we consider the perception that this is a "riskier" business as mis-placed given the nature of the customer.

Where 1pm is above-average risk

But certain aspects give an above-average risk profile because i) Onepm Finance is a remote lender, ii) some lending is to higher-risk startups/impaired credits, iii) some exposure to cyclical sectors, iv) acquired assets often riskier than self-originated, v) no current account real-time data, vi) rapid growth

Certain aspects of 1pm's business have incremental credit risk. This is not inherently a bad thing, as it is reflected in the rates charged, but it does mean that managing credit risk is even more important. These higher-risk factors include:

- Onepm Finance (the original company) has a model based on broker-introduced business and is therefore remote from the customer. Historical experience shows, in our view, that physical proximity and direct personal knowledge of the customer are factors mitigating ultimate credit losses.

- Certain of the 1pm businesses are willing to lend to startups. While the borrower may have considerable experience in the field, there is no direct borrower track record of financial performance. In these cases, a Personal Guarantee ("PG") is always taken, and 1pm's historical data over 10 years show that 75% of the value of deals that become impaired and are written off is recovered through converting the PG into a Charging Order and collecting against that Order. There are also certain businesses that lend to historically impaired credits (but obviously not ones considered currently bad), but this is only in respect of hard assets, where there is a known second-hand value and a well-developed second-hard market, should the asset need to be recovered and re-sold.

- Certain sectors are above-average risk. Six percent of 1pm's lease portfolio is to restaurants and cafés where, on average, the life expectancy of a business is under two years. Management notes that, within this sector, its focus has been on relatively low-value cafés and sandwich bar types of customers, and not high-end restaurants or national chains with multiple outlets.

- 1pm is not a bank and therefore does not provide current accounts. These provide a lender with real-time information on customer cashflows – and therefore show early indications of problems.

- Rapid-growth businesses are typically higher-risk than slower-growth ones, as control processes can get strained to a greater degree. Mathematically, given that it takes some time for impaired balances to show, strong growth can also depress lead-indicating arrears ratios measured against book size. This feature reverses if the growth rate slows. However, in 1pm's case, we note that the acquired entities with lending portfolios were the earlier acquisitions in 2015, 2016 and early 2017, so the acquired deals have since largely been settled. The more recent acquisitions were either brokerages or the invoice finance businesses, which, as noted above, have experienced exceptionally low credit losses.

- Acquired assets often have more risk than own-originated ones. For example, during a takeover, staff may be more focused on their jobs than on credit quality. In 1pm's case, this is mitigated, however, by the point noted above regarding the earlier acquisitions being those with credit exposure.

Sensitivity analysis

In the table below, we outline a range of possible scenarios affecting our current base assumptions for 2019. We believe investors should consider both the upside of current credit conditions continuing longer than expected and a range of downside scenarios. We also highlight the impact on the whole profit and loss, and not simply the impairment line. For example, harsher credit conditions are likely to see improving yields and more customers falling into 1pm's space, providing material offsets to higher credit losses.

Sensitivity analysis

Year-end May 2019E (£000)	Base	Current provisioning continues	IFRS9 worst case	1.5x IFRS9 worst case	1.5x IFRS9 worst case + no growth	1.5x IFRS9 worst case + half spread change
Revenue	32,946	33,605	34,045	35,828	34,450	35,046
Impairments in cost of sales	-1,973	-1,724	-4,878	-7,573	-7,282	-7,573
Impairment loss as % group receiv.	-1.17%	-1.00%	-2.83%	-4.31%	-4.31%	-4.31%
Other Cost of sales	-8,847	-9,024	-9,024	-9,201	-8,847	-9,201
Gross profit	**22,126**	**22,857**	**20,143**	**19,054**	**18,321**	**18,272**
Gross profit margin	67%	68%	59%	53%	53%	52%
Administration expenses	-11,983	-12,042	-12,042	-12,162	-12,102	-12,162
Exceptional items	-321	-321	-321	-321	-321	-321
Operating profit	**9,822**	**10,494**	**7,779**	**6,571**	**5,898**	**5,789**
Finance costs	-774	-790	-798	-844	-813	-805
Profit before income tax	**9,048**	**9,704**	**6,982**	**5,727**	**5,085**	**4,984**
Income tax	-1,754	-1,844	-1,327	-1,088	-966	-947
Profit for year	**7,294**	**7,860**	**5,655**	**4,639**	**4,119**	**4,037**
Change in profit from base case		**8%**	**-22%**	**-36%**	**-44%**	**-45%**
Change in profit from 2017 actual	**122%**	**139%**	**72%**	**41%**	**25%**	**23%**
Change in EPS from 2017 actual	**28%**	**38%**	**-1%**	**-19%**	**-28%**	**-29%**
Assumptions						
Assumed loan/lease book	130,000	132,600	132,600	135,200	130,000	135,200
Book growth vs. base		2%	2%	4%	0%	4%
Yield on closing balance sheet	18.00%	18.00%	18.25%	19.00%	19.00%	18.50%
Income	23,400	23,868	24,200	25,688	24,700	25,012
Bad debt write-off rate	1.50%	1.29%	3.66%	5.55%	5.55%	5.55%
Losses in cost of sales	1,950	1,708	4,849	7,497	7,209	7,497
Assumed invoice finance book	39,000	39,780	39,780	40,560	39,000	40,560
Book growth vs. base		2%	2%	4%	0%	4%
Yield on closing balance sheet	24.48%	24.48%	24.75%	25.00%	25.00%	24.74%
Income	9,546	9,737	9,846	10,140	9,750	10,034
Bad debt write-off rate	0.06%	0.04%	0.08%	0.19%	0.19%	0.19%
Losses in cost of sales	23	16	30	76	73	76
Administration expenses vs. base		0.5%	0.5%	1.5%	1.0%	1.5%
BP increase in funds		-	11	50	53	-
Cost of funds vs. base		0%	1%	5%	5%	0%
Valuation implications						
EPS (p)	8.28	8.9	6.4	5.3	4.7	4.6
Implied P/E	6.40	5.94	8.25	10.06	11.33	11.56
Dividend (p)	0.85	0.85	0.85	0.85	0.85	0.85
Dividend cover	9.80	10.57	7.60	6.24	5.54	5.43

Source: 1pm, Hardman & Co Research

Upside scenario adds nearly 10% to profits

- For an upside scenario, we have continued the current level of impairments and assumed a slightly greater market demand for financing (and greater 1pm appetite to lend). In this scenario, the incremental profit from lower impairments (ca.£0.25m) is actually less than the additional revenue (£0.65m) from the more buoyant market.

At current worst-case IFRS9 scenario, profits 22% lower than base case (still 72% above 2017 level). EPS would still be just 1% below 2017 actual.

- Our second scenario is a downside at the level indicated by management as its IFRS9 "worst-case scenario", i.e. impairments at 2.8% of the total book. This time, we have assumed incremental lending growth as mainstream banks reduce their appetite to lend and more customers fall into 1pm's lending space. We have assumed a modest improvement in spread and a small increase in costs. Management advises that the implementation of its new front-office system should generate operational efficiencies, but that there will be higher collection costs. In this scenario, profits would still be 72% above the 2017 actual level and the EPS would be just 1% lower (the gap reflecting shares issued to fund acquisitions).

In a hard-landing scenario (1.5x worst case, ca.4.3x current losses), profits fall 36% from base case, but this would still be 41% above 2017 actual (EPS down 19%).

- We have also assumed a hard landing at ca.4.3x current losses and 1.5x the IFRS9 worst-case scenario. The losses in the loan and lease book in this scenario are broadly similar to the peak of the IAS39 impairments after the financial crisis. This should prove conservative given that the book was much more dominated by sub-prime at the time, although this may be offset by a small degree of IFRS9 cyclicality. Overall, it appears a reasonable view of a hard landing, and 2019E profits fall by 36% under our assumptions (EPS down 19% on 2017). It is probable, however, that the peak impairments would not be until 2021/2022 and the fall would be less than 36% of profits, as there would be the full period income benefit from lending in 2019 and beyond. To put these losses in context:

P/E of just 10x on bottom-of-cycle earnings

  - The fall in EPS increases the P/E from our base case of 6.4x to 10.1x. Paying only 10x for a cyclical stock at the bottom of a cycle appears highly anomalous.

Dividend cover over 6x

  - The dividend would be covered 6.2x against 9.8x in our base case.
  - The £5.6m fall in pre-tax profits (ca.£4.6m post-tax) is only just over 10% of the market capitalisation of the group.

On our most likely scenario, EPS in 2019 is 28% above 2017 levels. Maintaining current credit losses sees further ca.10% upside. Downside to a hard landing is 19%.

  - The downside risk of a 19% drop in EPS on 2017 actuals in this hard-landing scenario, with impairments at 4.3x current levels, may be compared with the 28% upside assumed in our base case (most probable outcome), with further upside if the credit environment remains stable. Investors may wish to consider the implied risk-reward that the scale and probability of these scenarios produces. We note, on our assumptions, that there is more upside and a greater probability in our base case than the downside in a hard landing.

- Our scenario tests reflect our best estimate for the impact on the group taking account of all the positive and negative influences that a recession could have. We have provided incremental sensitivity around our assumptions, noting that, should the expected improvements in yield and volume not materialise, then the downside to profits would be ca.10% more for each factor. At this stage, we cannot be certain of the impact of IFRS9 cyclicality (especially the probability applied to a worst-case scenario); nor can we be certain of whether the whole market will adopt more conservative assumptions (for example, on probability of default).

Financials

Profit and loss

We have made no changes to our estimates.

Profit and loss							
Year-end May (£000)	**2013**	**2014**	**2015**	**2016**	**2017**	**2018E**	**2019E**
Revenue	3,107	4,212	5,534	12,554	16,944	29,596	32,946
Cost of sales	-1,651	-1,994	-2,503	-4,480	-6,094	-9,849	-10,820
Gross profit	**1,455**	**2,217**	**3,031**	**8,074**	**10,850**	**19,747**	**22,126**
Other operating income	0	0	0	2	3	0	0
Administration expenses	-663	-845	-1,394	-4,290	-6,469	-10,834	-11,983
Exceptional items	0	0	0	-368	-263	-294	-321
Operating profit	**792**	**1,372**	**1,637**	**3,418**	**4,121**	**8,619**	**9,822**
Finance costs	-17	-26	-21	-74	-82	-673	-774
Finance income	0	1	4	2	41	-	-
Profit before income tax	**775**	**1,346**	**1,620**	**3,346**	**4,080**	**7,946**	**9,048**
Income tax	-172	-297	-349	-480	-794	-1,542	-1,754
Profit for year	**603**	**1,049**	**1,271**	**2,866**	**3,286**	**6,404**	**7,294**
Average number of shares (m)	23.15	29.60	34.18	48.85	**53.94**	**85.09**	**88.02**
Adjusted EPS (p)	**2.60**	**3.54**	**3.72**	**6.47**	**6.48**	**7.85**	**8.29**
Total dividend (p)	-	-	0.35	0.50	0.50	0.60	0.80
Dividend cover (adjusted EPS) (x)	n/a	n/a	10.6	12.9	13.0	13.1	10.4
Ratios (%)							
Revenue to year-end bal. sht.	24%	24%	22%	22%	23%	20%	19%
Cost of sales to revenue	-53%	-47%	-45%	-36%	-36%	-33%	-33%
Admin. costs to revenue	-21%	-20%	-25%	-34%	-38%	-37%	-36%
Finance costs to revenue	-1%	-1%	0%	-1%	0%	-2%	-2%
Finance cost as % year-end Int.-bearing liabilities	-2%	-3%	-3%	-4%	-7%	-10%	-11%
Return on net assets	13%	15%	10%	12%	12%	13%	13%

Source: 1pm, Hardman & Co Research

Balance sheet

The table below details the expected balance sheet. We have modestly increased our receivables and associated funding assumptions.

Balance sheet							
As at 31 May (£000)	**2013**	**2014**	**2015**	**2016**	**2017**	**2018E**	**2019E**
Non-current assets							
Goodwill	-	-	-	10,289	14,908	27,375	27,375
Intangible assets					84	224	224
Property, plant and equipment	41	73	239	1,251	1,744	1,700	1,700
Trade and other receivables	-	-	14,502	33,166	49,966	51,966	58,202
Deferred tax	-	-	-	208	411	611	811
Total non-current assets	**41**	**73**	**14,741**	**44,914**	**67,113**	**81,876**	**88,312**
Inventories	-	-	-	81	135	-	-
Cash and cash equivalents	13	3	12	910	2,078	2,582	1,008
Trade and other receivables	12,900	17,324	10,489	22,895	23,989	98,927	110,798
Total current assets	**12,913**	**17,327**	**10,501**	**23,886**	**26,202**	**101,509**	**111,806**
Total assets	**12,953**	**17,400**	**25,242**	**68,800**	**93,315**	**183,385**	**200,118**
Non-current liabilities							
Trade and other payables	3,112	4,405	5,685	19,664	32,097	67,104	73,604
Financial liabilities - borrowings	100	100	100	399	250	3,450	3,450
Deferred tax	-	-	40	-	-	-	-
Provisions (contingent consideration)	-	-	-	1,833	2,300	2,300	966
Total non-current liabilities	**3,212**	**4,505**	**5,825**	**21,896**	**34,647**	**72,854**	**78,020**
Trade and other payables	4,109	4,807	6,182	19,979	26,533	56,091	58,896
Financial liabilities - borrowings incl. bank overdrafts	520	403	357	519	-	-	-
Interest-bearing loans and borrowings	400	380	200	729	949	3,149	3,916
Provisions		-	-	1,245	1,733	1,854	1,854
Tax payable	148	297	310	543	943	943	943
Total current liabilities	**5,177**	**5,887**	**7,049**	**23,015**	**30,158**	**62,037**	**65,609**
Total liabilities	**8,390**	**10,392**	**12,874**	**44,911**	**64,805**	**134,891**	**143,629**
Share capital	2,315	2,997	3,685	5,253	5,494	8,611	8,821
Share premium	1,569	2,288	5,606	13,077	14,170	24,853	25,859
Employee share			83	90	91	291	295
Retained earnings	679	1,724	2,994	5,469	8,755	14,740	21,515
Total equity	**4,563**	**7,008**	**12,368**	**23,889**	**28,510**	**48,494**	**56,490**
Period-end no. shares (m)	23.31	29.97	36.85	52.53	54.94	86.39	88.41
NAV per share (p)	0.20	0.23	0.34	0.45	0.52	0.56	0.64
Tangible NAV per share (p)	0.20	0.23	0.34	0.26	0.25	0.24	0.33
Ratios							
Equity/total receivables	35%	40%	49%	43%	39%	32%	33%
Current trade recs. to payables	n/d	n/d	1.70	1.15	0.90	1.76	1.88

Source: 1pm, Hardman & Co Research

Investors should be aware that, when the company refers to own book loans and assets, it is referring to the gross amount due, which includes unearned interest. The accounting balance sheet line excludes this, and thus is a lower number. Similarly, when 1pm refers to drawn facilities, it includes contractual interest due, which again is a larger number than appears in the balance sheet liabilities.

Cashflow

As 1pm is a lender, we believe the cashflow needs to be treated with a degree of caution – there is likely to be positive cashflow when a business is shrinking and negative when it is growing. Investors should also be aware that, as noted above, the mix of funding between bank facilities (and so in financing activities) and block funding (in payables and so in operating activities) will affect lines within the cashflow statement, but not the overall cash position.

Cashflow							
Year-end May (£000)	**2013**	**2014**	**2015**	**2016**	**2017**	**2018E**	**2019E**
Profit before tax	775	1,346	1,620	3,346	4,080	7,946	9,048
Depreciation charges	15	23	79	354	544	758	739
Finance costs	17	26	21	74	82	673	774
Finance income	-	-1	-3	-3	-41	-	-
Increase in trade receivables	-2,787	-4,425	-7,667	-12,649	-9,134	-22,000	-18,107
Increase in trade/other payables	1,168	1,990	2,656	11,996	11,476	15,000	9,305
Total cash from operations	**-812**	**-1,039**	**-3,294**	**3,118**	**7,007**	**2,377**	**1,759**
Interest paid	-17	-26	-21	-74	-82	-673	-774
Tax paid	-	-148	-297	-637	-615	-2,393	-768
Net cash from operating activities	**-829**	**-1,213**	**-3,612**	**2,407**	**6,310**	**-689**	**217**
Acquisition of subsidiaries	-	-	-	-7,588	-3,141	-16,017	-1,300
Purchase of prop., plant & equip.	-17	-55	-246	-547	-1,089	-758	-739
Interest received	-	1	3	3	41	-	-
Net cash from investing activities	**-17**	**-55**	**-243**	**-8,132**	**-4,189**	**-16,775**	**-2,039**
New loans/loan repayments	400	-20	-180	-179	-22	5,400	767
Share issue	-	1,395	4,090	6,769	-150	12,988	-
Equity dividend paid	-	-	-	-129	-262	-419	-518
Net cash from financing activities	**400**	**1,375**	**3,910**	**6,461**	**-434**	**17,969**	**249**
Increase in cash and cash equivalents	-446	107	55	736	1,687	504	-1,574
Opening cash/cash equivalents	-61	-507	-400	-345	391	2,078	2,582
Closing cash/cash equivalents	-507	-400	-345	391	2,078	2,582	1,008

Source: 1pm, Hardman & Co Research

Valuation

Summary

Average valuation upside potential on absolute measures 67%

Our assumptions were detailed in our initiation note, Financing Powerhouse: a lunchtime treat, and these have not changed. With the revisions to forecasts, our absolute valuation techniques imply average upside potential of 67%. The limited peer group relative valuation measures would indicate between 60% and 100% upside potential.

Summary of different valuation techniques

	Implied price (p)	Upside (%)
Gordon Growth Model	103	96%
Dividend Discount Model	73	38%
Average absolute measures	**88**	67%

Source: Hardman & Co Research

Gordon Growth Model

GGM captures both value-added and growth. Upside potential more than double.

Our preferred valuation approach is to consider the value added by a business, which is captured by the Gordon Growth Model (GGM). A growing business delivering above its cost of capital should trade above book value because it is adding value. This model still indicates a value of 103p. For a business like 1pm, which is growing its equity base rapidly (partially due to our assumed low dividend payout ratio), rolling forward to a new base year will see a material increase in valuation. For example, if we used 2019E NAV, rather than 2018E, the valuation would be 117p.

Dividend Discount Model

DDM 73p, upside potential 34%; would rise to 81p if company immediately adopted long-term payout ratio.

Our Dividend Discount Model (DDM) produces a valuation of 73p, of which just 12p is in the terminal value. It is also worth noting that the short-term payout ratio is well below that we expect over the long term. If the company were to immediately adopt our long-term ratio, it would add a further 8p to the valuation under this methodology.

Peer comparisons

Closest peers indicate share price could double. Broader range suggests 60%+ upside potential.

1pm has no immediate quoted peers. Using the quoted specialist lenders on P/E or P/B measures would suggest a share price broadly double the existing one. The smaller consumer finance companies imply ca.60% upside potential. The challenger banks are more mixed, but again have upside.

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The fact that Hardman & Co is commissioned to write the research is disclosed in the disclaimer, and the research is widely available.

The full detail is on page 26 of the full directive, which can be accessed here: http://ec.europa.eu/finance/docs/level-2-measures/mifid-delegated-regulation-2016-2031.pdf

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