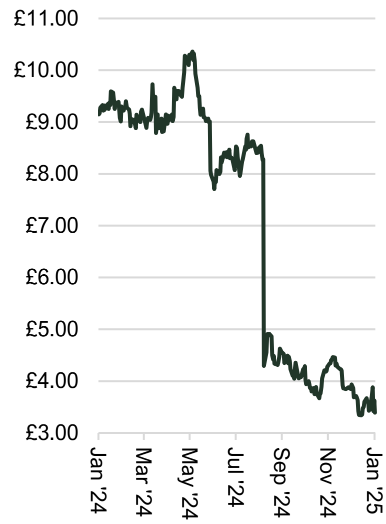
Next 15 Group PLC

NFG | AIM | Media | 323p | £326m

Full year trading update – Market remains tough but some green shoots

1 Year Chart



Despite the cautious tone of the outlook statement and a FY25E EBIT outcome towards the bottom end of the expectation range, there was enough in this full year trading update to drive a positive share price reaction on the day. The combination of good progress on cost savings; positive actions around simplifying the group operating structure, and an easing of the macro backdrop are all helpful factors.

The valuation context here is also important to recognize. The share price reaction to the Mach49 contract loss was severe and has led to NFG trading at 10 year valuation lows and seeing a valuation de-rating unmatched in the peer group. Yet, despite the scale of the contract loss, there are others who have fared worse from an estimate downgrade perspective, and where these downgrades have been more broadly spread. NFG is a portfolio of agencies, and there are a good number of these that have been showing strong momentum.

In our eyes, it would not take much to see the NFG earnings trend improve and this will put the current valuation into stark relief.

Next 15 Group PLC is a research client of H2 Radnor Ltd.

MiFID II – this research is deemed to be a minor, non-monetary benefit.

- **FY trading update** can best be characterised as mixed. The group has been able to point to good contract wins across a number of group agencies that bode well for FY26E. However, the overall pressures felt through FY25E, especially from the North American technology client base, have not fully abated and are likely to be maintained into the start of FY26E.

- **Cost savings and internal restructuring:** More positively, the cost savings announced at the H1 results look to be well on track with £9m out of a target £25m to be delivered in FY25E. A further £15m of savings have been identified (largely from a down scaling of Mach49 post the contract loss), which will help to offset revenue pressure. The group has also provided more detail on the structural shift in the group operating model away from the historic de-centralised approach.

- **Estimate Changes & Valuation:** NFG has guided towards the bottom end of the consensus range for FY25E and have signalled a degree of continuing caution around FY26E. We have reviewed our estimates accordingly and trim our FY25E revenue / PBT by -1% / -4% and FY26E by -2% / -7% respectively. Our sense is that we are now getting much closer to a positive inflection point as the macro picture, particularly out of North America, begins to improve. The 5.6x FY25E PE continues to offer 10 year plus valuation lows for a business that has a proven growth track record.

4 February 2025

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January, £m	Revenue	PBT adj	EPS (p)	Div (p)	Net Cash	PE x	Yield %
FY 2023A	563.8	112.5	80.4	14.6	26.1	4.0	4.5
FY 2024A	577.8	117.9	81.6	15.4	(1.4)	4.0	4.8
FY 2025E	*569.7*	*102.1*	*70.1*	*13.0*	*(46.1)*	*4.6*	*4.0*
FY 2026E	*520.5*	*82.3*	*57.6*	*10.5*	*(52.1)*	*5.6*	*3.2*
FY 2027E	*548.4*	*95.3*	*66.9*	*12.2*	*(41.3)*	*4.8*	*3.8*

Full Year Trading Update

NFG has issued its regular, full year trading update for the year ended 31st January 2025. The key headlines are as follows:

- Overall group profit performance likely to be at the bottom end of the consensus range of expectations (£107m to £112m based on adjusted EBIT). Although the statement is not specific, we believe that this has been led primarily by the timing of cost savings and also internal investment in strongly performing businesses like SMG, rather than being revenue led.

- Overall trading environment remains challenging, although a number of subsidiary businesses (most notably SMG, M Booth, MHP and Brandwidth) have continued to deliver "*strong growth and margins*".

- NFG remains on track to deliver £9m of operational cost savings in FY25E, with an all in annualised cost saving target of £25m to be delivered through the course of FY26E. This £25m cost saving target was announced at the H1 results.

- £14m of cost savings have been identified within Mach49 as this business downscales following the material contract loss announced earlier in 2025.

- Taken together, NFG is aiming to deliver £40m of annualised savings by the end of FY26E.

Whilst the short-term headlines will be focused on the EBIT guidance coming in at the lower end of the expectations, the positive share price reaction tells a different story.

- The outlook statement, albeit cautious in the short term, does speak to signs of improvement in client spend in certain areas.

- The £40m of total operational cost savings that has been identified is a material increase over the £25m previously communicated.

- Progress has been made in terms of the group's operating structure with a number of tech facing agencies in the US being bought together into a more cohesive whole. This will simplify the client facing proposition, enhance future efficiencies and also increase returns on investment in areas like AI.

- The group has also highlighted the potential for further, accretive M&A. This is a helpful reminder of the overall strength of the balance sheet and the cash generating capacity of the group, despite the near term earn out liabilities. Well priced, smaller scale and less risky bolt-on M&A was a key feature of NFG's success over many years and, we believe, would be welcomed by the market.

Despite the negative headlines surrounding the Mach49 contract loss, this trading update is likely to have reminded investors that the underlying strengths of the group remain undimmed. Whilst the group is not yet out of the woods, there are enough indications that the macro environment will continue to ease and that we may not be far from a positive earnings inflection point.

Changes to h2Radnor estimates

Post the trading update, we are making a number of revisions to our model. NFG has guided that the FY25E outturn is likely to be towards the bottom of the consensus range for EBIT and we react accordingly.

The group has also signalled a cautious short-term outlook around FY26E. The key dynamic here is around the lack of short-term visibility on any material rebound in technology client spend, balanced against an improving macro outlook for North America in particular, and the genuine momentum being delivered by the more B2C and public sector focussed businesses within the group.

Whilst NFG has been making better than expected progress on delivering near term cost savings, the group is also not standing still when it comes to future investments. The grouping together the more tech focussed communications agencies (Archetype, Outcast and Nectar) is in line with the previously announced changes to the group operating structure and reflects a shift away from the de-centralised model that has been a longstanding feature of the group approach. Coupled with this, NFG will be increasing its investment in AI product and service development with £5m of incremental spend highlighted for FY26E in this area alone.

Net, net we are moving our FY25E estimates in-line with company guidance. Looking out to FY26E, we are reducing our revenue estimate by -2% and our EBIT estimate by -4%. We had been looking for a material working capital release in FY26E, however industry payment terms remain tight and there is little indication that this will improve. We are taking a cautious view here and now look for a neutral working capital position in FY26E. This has driven a higher net debt estimate and corresponding interest charge.

Figure 1: h2Radnor estimate revisions

		Previous		**New**		***Change, %***	
	2024A	2025E	2026E	**2025E**	**2026E**	**2025E**	**2026E**
Customer Engagement	263.1	257.9	266.9	255.2	257.8	*- 1%*	*- 3%*
Customer Delivery	107.7	109.8	115.3	109.8	115.3	*+ 0%*	*- 0%*
Customer Insight	57.5	58.1	61.0	58.1	61.0	*- 0%*	*- 0%*
Business Transformation	149.6	149.6	88.3	146.6	86.5	*- 2%*	*- 2%*
Revenue	**577.8**	**575.4**	**531.5**	**569.7**	**520.5**	***- 1%***	***- 2%***
Customer Engagement	53.2	51.6	51.8	51.3	52.1	*- 1%*	*+ 1%*
Customer Delivery	29.1	28.5	30.0	27.7	28.8	*- 3%*	*- 4%*
Customer Insight	10.4	10.7	11.6	9.9	10.5	*- 8%*	*- 10%*
Business Transformation	48.3	41.6	21.2	39.9	19.0	*- 4%*	*- 10%*
Central Overhead	-19.8	-21.9	-23.9	-21.6	-22.9	*- 1%*	*- 4%*
EBITA	**121.1**	**110.5**	**90.7**	**107.1**	**87.5**	***- 3%***	***- 4%***
- margin %	*21.0%*	*19.2%*	*17.1%*	*18.8%*	*16.8%*		
Adj. PBT	**117.9**	**106.1**	**88.7**	**102.1**	**82.3**	***- 4%***	***- 7%***
Adj. EPS (p)	**81.6**	**71.8**	**61.3**	**70.1**	**57.6**	***- 2%***	***- 6%***
Dividend (p)	15.4	13.3	11.1	13.0	10.5	*- 2%*	*- 6%*
Net Cash (Debt)	**-1.4**	**-37.5**	**-19.7**	**-46.1**	**-52.1**		

Source: h2Radnor

In our last note, we broke down the NFG net debt / free cashflow dynamics in more detail and we refresh this analysis below.

The strength of the Next 15 balance sheet has been an important underpin to the equity story for a number of years. Despite the negative impact of working capital in both the current year and FY26E, we still expect Next 15's net debt / EBITDA multiple to be not exceed 0.5x.

In Figure 2 below, we show how our estimate of how the net debt / EBITDA multiple will evolve over the next three years based on our current EBITDA expectations and the current company guidance on outstanding earn out commitments. We also assume a 100% cash payout, although this could change should the share price improve.

Figure 2: h2Radnor earn out & net debt analysis

£m	FY25E	FY26E	FY27E
Operating Cashflow	85.1	96.1	101.6
Free Cashflow	55.1	70.5	74.1
Deferred consideration payments	(60.0)	(48.6)	(42.2)
Year End Net Cash / (Debt)	**(46.1)**	**(52.1)**	**(41.3)**
EBITDA	119.6	100.5	110.7
Net debt / EBITDA, x	**0.4**	**0.5**	**-**
Free cashflow / Earn out cover	0.9	1.5	1.8

Source: h2Radnor

Given the phased nature of the outstanding earn out commitments, we do not believe that capitalising the full value of the earn outs now gives a fair impression of the true balance sheet picture. We can see from Fig 2 that even on our revised net debt expectations, we still expect net debt / EBITDA to not exceed 0.5x over the next three years and for free cashflow to comfortably exceed earn out liabilities in FY26E and FY27E.

Even if we were to treat the outstanding F26E and FY27E earn out commitments on an "all in" basis in the current year, then the net debt / EBITDA multiple would be 1.1x, a level we still regard as comfortable.

Valuation Opportunity

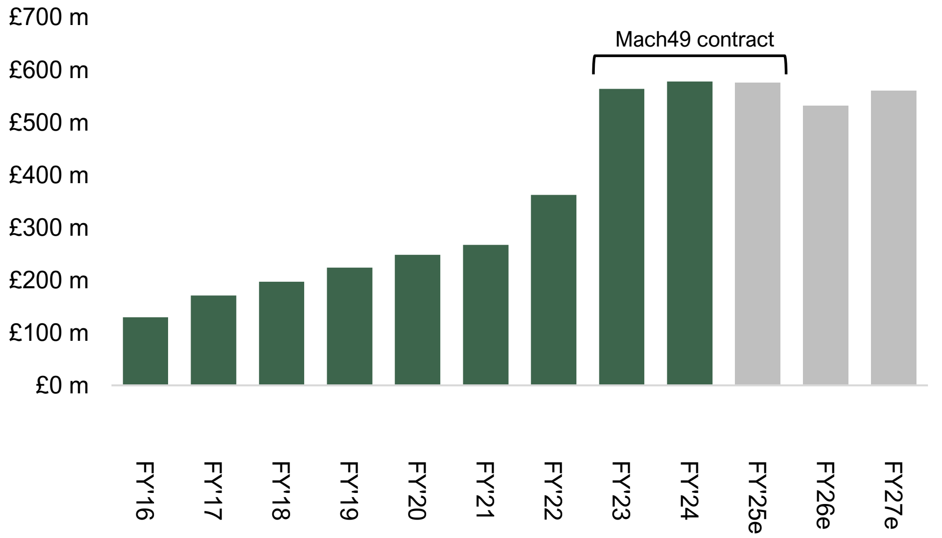
We believe the current valuation has been materially distorted by sentiment concerns around the Mach49 contract loss and a negative reaction to what was the first material downgrade for the core Next 15 business for the best part of 10 years.

We can see this distortion through the comparison between the market reaction to Next 15 and others in the peer group, who have also experienced either singular or more prolonged downgrade pressure.

Before we look at the comparative market reactions within the peer group, it is worth taking a step back and look at the broader Next 15 track record.

Figure 3: Next 15 revenue track record & CAGR

Revenue CAGRs			
FY16 → FY22	FY16 → FY24	FY16 → FY27E	FY22 → FY27
+16%	**+18%**	**+13%**	**+7%**



Source: Company, h2Radnor

Figure 3 shows the evolution of Next 15 revenue from FY16 through to the end of our current estimate period, FY27E. We can see that prior to the first full contribution from the Mach49 contract (FY23), Next 15 had delivered a FY16 – FY22 revenue CAGR of **+16%**, of which approximately half was organic and half contributed by M&A.

We can clearly see the impact of the Mach49 contract in FY23, FY24 and the current FY25E, which will be the final year of full contribution.

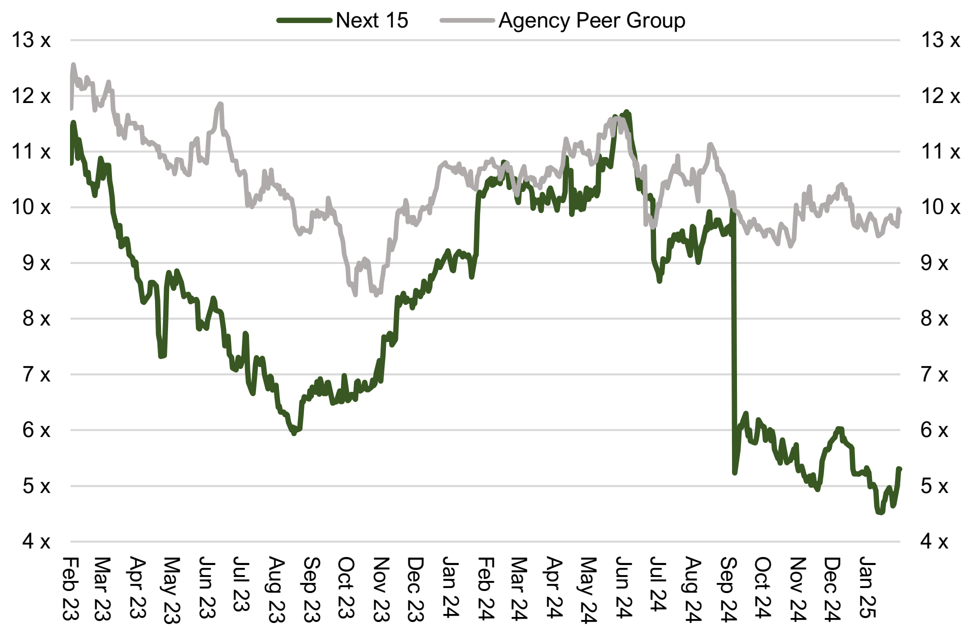
Looking through to FY27E, ie once the Mach49 contract has fully washed through, we see the FY16 to FY27E revenue CAGR fall by only 3% points to **+13%**. If we look at the more recent period of FY22 (before the full benefit of the Mach49 contract) through to FY27E, we can still see a revenue CAGR of **+7%**.

Looking back to our estimates from July 2024, pre the loss of the Mach49 contract, we had been looking at FY25E revenue of £605.1m, FY26E revenue of £642.7m and FY27E revenue of £682.6m. These all assumed a full contribution from the contract. We can therefore see a downgrade of -5%, -17% and -18% respectively. Prior to these downgrades we had been looking for a FY22 – FY27E revenue CAGR of **+11%**.

This is an important point to note. Even after we take out the contribution from the Mach49 contract, and the broader scaling back of shorter-term growth expectations to reflect the current technology driven spending squeeze, we are still expecting FY26E and FY27E revenue to be c.50% ahead of FY22. This reflects a combination of organic growth and the contributions from the Shopper Media and Engine acquisitions, both of which have delivered organic growth throughout the period.

So, against this context, how has the Next 15 valuation responded?

Figure 4: Next 15 FY1 PE vs Agency Peer Group



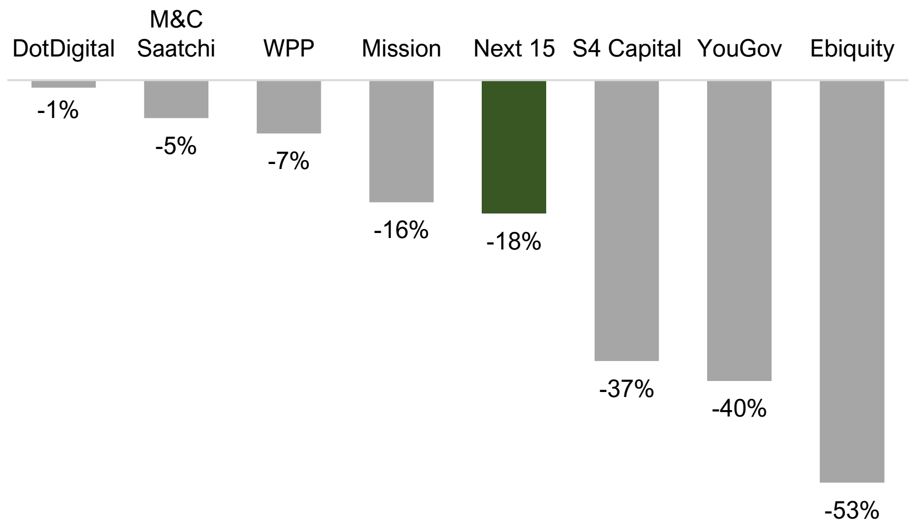
Source: h2Radnor, FactSet

We can see from Figure 4 above, the extent to which Next 15 has de-rated relative to the peer group, with both seeing FY1 PE multiples peak in early June 2024 at 11.7x.

- At the current FY1 PE multiple of 5.3x, Next 15 has seen its multiple de-rate by **-55%** from this June 2024 peak.
- At the current FY1 PE multiple of 9.9x, the Agency Peer Group has seen its multiple de-rate by **-15%** from this June peak.

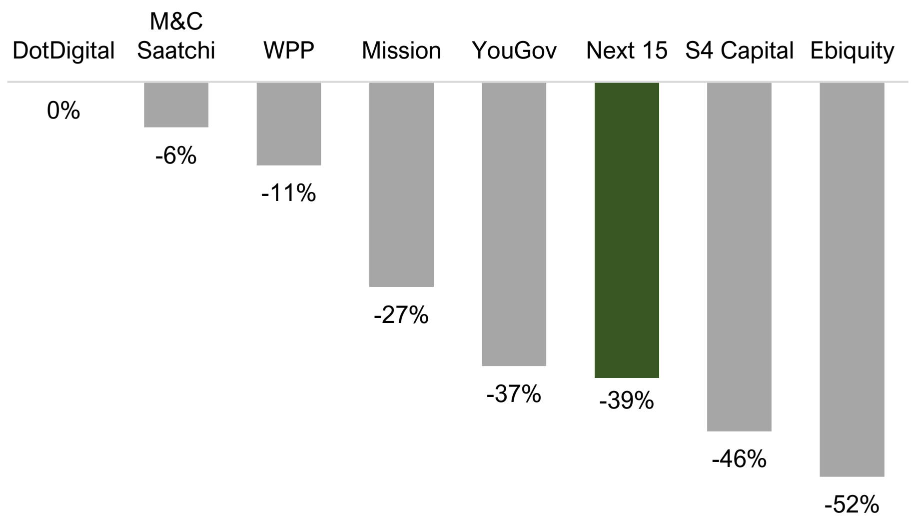
Has the extent of this Next 15 de-rating compared to its peer group been justified by materially greater downgrades? In Figures 5 and 6 below, we show the change in both FY1 and FY2 EPS estimates for all the companies in the peer group across the last 12 months.

Figure 5: Agency peer group – FY1 EPS downgrades – last 12 months



Source: h2Radnor, FactSet

Figure 6: Agency peer group – FY2 EPS downgrades – last 12 months



Source: h2Radnor, FactSet

We can see from the above that on a FY25E basis, others in the sector have seen far more significant downgrades. With the majority of the Mach49 impact falling into FY26E, Next 15 fares less well on a comparative basis, however it is still not the most downgraded stock. Even on a FY26E basis, both YouGov and S4 Capital have seen similar or more significant earnings downgrades than Next 15.

It is clear to us that the extent of the PE de-rating is less about the quantum of the downgrades and is more to do with the abrupt nature of the Mach49 contract loss. There is also no doubt that the market will have been disappointed that Next 15 has not been able to remain wholly immune from the broader trading pressures that have been facing others in the sector for some time.

Do we think this over de-rating is justified? No, is the short answer. Other than the negative surprise factor surrounding the Mach49 contract loss, we see little in the Next 15 story that has changed on a fundamental basis.

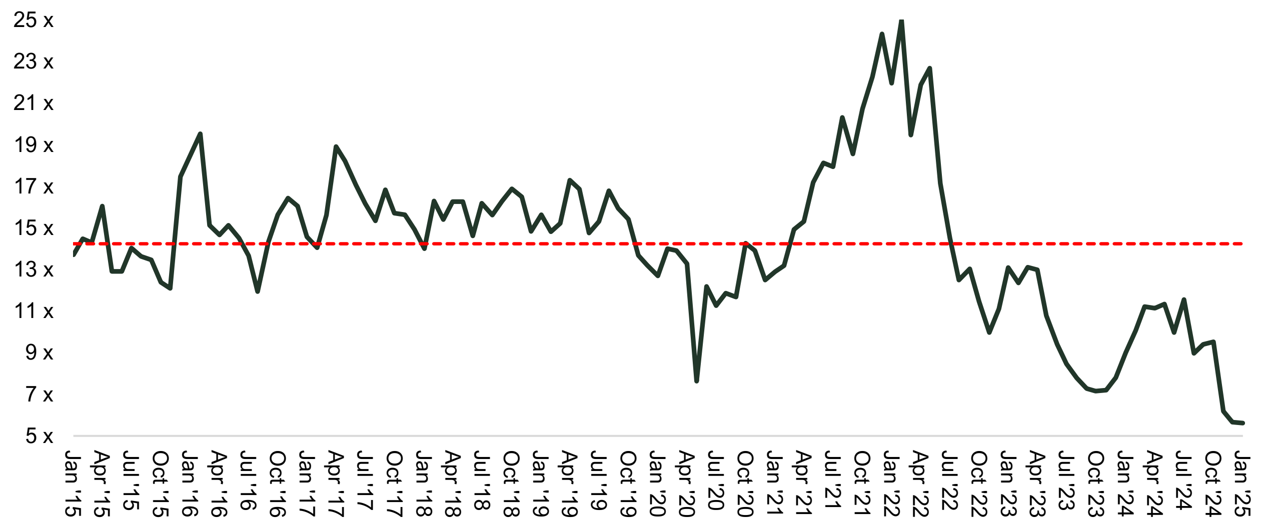
- Next 15 remains a more resilient business than many of its peers. The group portfolio effect (Next 15 is a group of multiple smaller, niche specialists) is much more significant than for others.

- The portfolio is more broadly spread now across client vertical and business discipline than at any time in the past 10 years. The historic majority exposure to the technology industry has been reduced significantly; partly through group diversification and partly through tech client spend reductions.

- Despite the recent downgrades, Next 15 is still expected to outperform its peers when it comes to margin protection.

The current valuation, at 5.4x FY1 PE, represents a 10 year low (see Figure 7 below). For those investors willing to look through the Mach49 contract loss, this represents a material opportunity to gain exposure to a company that has one of the strongest track records in the sector.

Figure 7: Next 15 10 year PE multiple



Source: h2Radnor, FactSet

Next 15 Group PLC

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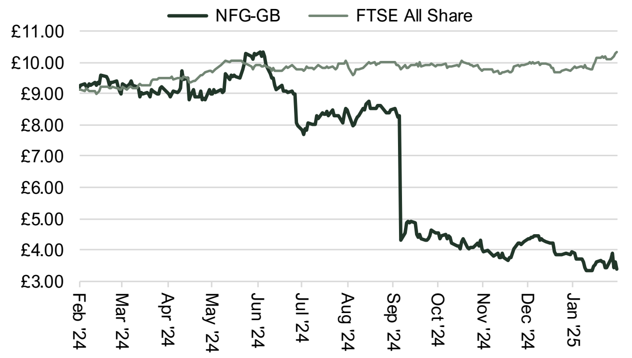
Price (p):	**323 p**
Market Cap:	326 m
EV:	372 m

PROFIT & LOSS

Year to 31 January, £m	FY22	FY23	FY24	FY25e	FY26e	FY27e
Customer Engagement	*187.6*	*275.0*	*263.1*	*255.2*	*257.8*	*270.7*
Customer Delivery	*80.0*	*102.1*	*107.7*	*109.8*	*115.3*	*121.1*
Customer Insight	*42.1*	*52.0*	*57.5*	*58.1*	*61.0*	*65.8*
Business Transformation	*52.5*	*134.8*	*149.6*	*146.6*	*86.5*	*90.8*
Group Net Revenue	**362.1**	**563.8**	**577.8**	**569.7**	**520.5**	**548.4**
Customer Engagement	*40.4*	*55.4*	*53.2*	*51.3*	*52.1*	*55.5*
Customer Delivery	*28.5*	*30.2*	*29.1*	*27.7*	*28.8*	*31.5*
Customer Insight	*9.0*	*11.0*	*10.4*	*9.9*	*10.5*	*11.8*
Business Transformation	*15.2*	*43.9*	*48.3*	*39.9*	*19.0*	*20.9*
Head Office	*(13.8)*	*(26.4)*	*(19.8)*	*(21.6)*	*(22.9)*	*(22.5)*
EBITA - Adjusted	**79.3**	**114.2**	**121.1**	**107.1**	**87.5**	**97.2**
Associates & JV's	0.2	-	-	-	-	-
Net Bank Interest	(0.3)	(1.6)	(3.1)	(5.0)	(5.2)	(1.9)
PBT - Adjusted	**79.3**	**112.5**	**117.9**	**102.1**	**82.3**	**95.3**
Non Operating Items	(40.4)	(48.3)	(45.1)	(45.0)	(30.0)	(30.0)
Other Financial Items	(119.0)	(54.1)	7.5	(29.5)	(29.5)	(29.5)
PBT - IFRS	**(79.1)**	**10.1**	**80.3**	**26.5**	**21.7**	**34.7**
Tax	14.5	(7.1)	(26.4)	(7.1)	(5.9)	(9.4)
Tax - Adjusted	(17.2)	(26.3)	(31.1)	(26.5)	(21.4)	(24.8)
Tax rate - Adjusted	*21.6%*	*23.3%*	*26.3%*	*26.0%*	*26.0%*	*26.0%*
Minority interests	3.6	1.4	1.0	2.0	1.8	2.0
No. shares m	92.4	97.6	99.2	99.0	99.0	99.0
No. shares m, diluted	98.1	105.7	105.2	104.9	102.5	102.5
IFRS EPS (p)	(73.8)	1.7	53.3	17.5	14.2	23.6
Adj EPS (p), diluted	**59.7**	**80.4**	**81.6**	**70.1**	**57.6**	**66.9**
Total DPS (p)	12.0	14.6	15.4	13.0	10.5	12.2

PRICE CHART - 1 YEAR ABSOLUTE vs FTSE ALL SHARE



Source: FactSet

SHAREHOLDERS

	% of ord. Share capital
Octopus Investments	11.9%
Liontrust Investment Partners	10.0%
Aviva Investors	9.9%
Slater Investments	6.7%
Directors	5.5%
BlackRock	4.8%
JPMorgan AM	4.1%
abrdn	3.3%
	56.2%

CASH FLOW

Year to 31 January, £m	FY22	FY23	FY24	FY25e	FY26e	FY27e
Net Profit: (add back)	(64.6)	3.0	53.9	19.3	15.8	25.3
Depreciation & Amortisation	*28.8*	*37.2*	*36.6*	*37.5*	*38.0*	*38.5*
Net Finance costs	*120.3*	*57.1*	*(3.2)*	*35.6*	*35.8*	*32.5*
Tax	*(14.5)*	*7.1*	*26.4*	*7.1*	*5.9*	*9.4*
Working Capital	0.2	(24.4)	(10.7)	(6.5)	3.6	(1.1)
Other	19.6	15.1	2.0	(8.0)	(3.0)	(3.0)
Cash from Ops	**89.8**	**95.2**	**105.0**	**85.1**	**96.1**	**101.6**
Cash Tax	(14.1)	(20.3)	(25.4)	(22.5)	(18.1)	(20.0)
Tangible Capex	(3.1)	(3.5)	(3.7)	(3.0)	(3.0)	(3.0)
Intangible Capex	(2.7)	(3.5)	(3.4)	(4.5)	(4.5)	(4.5)
Free Cashflow	**69.9**	**67.9**	**72.5**	**55.1**	**70.5**	**74.1**
Dividends	(12.4)	(15.3)	(16.1)	(17.2)	(12.8)	(10.4)
Acquisitions & Inv.	(24.0)	(104.9)	(60.2)	(65.0)	(48.6)	(42.2)
Financing	(1.1)	38.6	1.1	(23.5)	(15.0)	(10.7)
Net Cashflow	**32.4**	**(13.7)**	**(2.6)**	**(50.6)**	**(6.0)**	**10.8**
Net Cash (Debt)	35.7	26.1	(1.4)	(46.1)	(52.1)	(41.3)

Announcements

Date	Event
January 2025	Trading update
September 2024	Trading update
June 2024	AGM update
April 2024	Final results
January 2024	Trading update
September 2023	H1 results
April 2023	Final results
January 2023	Trading update

RATIOS

	FY23	FY24	FY25e	FY26e	FY27e
RoE	74.2%	54.9%	44.0%	48.4%	53.0%
RoCE	37.4%	36.9%	33.0%	30.6%	35.2%
Asset Turnover (x)	0.7x	0.7x	0.7x	0.7x	0.7x
NWC % Revenue	13.6%	8.6%	9.4%	16.0%	15.0%
Op Cash % EBITA	83.4%	86.8%	79.5%	109.8%	104.5%

BALANCE SHEET

Year to 31 January, £m	FY22	FY23	FY24	FY25e	FY26e	FY27e
Intangibles	183.1	274.1	279.3	283.8	279.5	273.1
P,P+E	7.5	10.9	10.1	8.9	7.6	6.1
Tax Asset & Other	75.6	97.2	88.4	85.4	82.4	79.4
Total Fixed Assets	**266.2**	**382.1**	**377.8**	**378.2**	**369.5**	**358.6**
Net Working Capital	(51.6)	(76.8)	(49.5)	(53.8)	(83.2)	(82.1)
Capital Employed	**214.5**	**305.3**	**328.4**	**324.4**	**286.3**	**276.5**
Earn Out Liabilities	(188.8)	(217.0)	(170.8)	(111.3)	(112.2)	(105.8)
Net Funds	35.7	26.1	(1.4)	(46.1)	(52.1)	(41.3)
Net Assets	**61.5**	**114.4**	**156.2**	**167.0**	**122.0**	**129.4**

VALUATION

Fiscal	FY23	FY24	FY25e	FY26e	FY27e
P/E	4.0x	4.0x	4.6x	5.6x	4.8x
EV/EBITDA	2.9x	2.8x	3.1x	3.7x	3.4x
Div Yield	4.5%	4.8%	4.0%	3.2%	3.8%
FCF Yield	18.3%	19.5%	14.8%	18.9%	19.9%
EPS growth	34.5%	1.5%	-14.1%	-17.7%	16.1%
DPS growth	21.7%	5.1%	-15.5%	-19.2%	16.1%

REGULATORY DISCLOSURES

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