Update

Edison investment research

21 April 2009

Next Fifteen Communications

Year End	Revenue (£m)	PBT* (£m)	EPS* (p)	DPS (p)	P/E (x)	Yield (%)
07/07	59.3	5.6	7.0	1.5	4.7	4.5
07/08	63.1	6.6	8.5	1.7	3.9	5.2
07/09e	63.5	4.5	5.5	1.7	6.0	5.2
07/10e	64.5	6.0	7.7	1.8	4.3	5.4

Note: * PBT and diluted EPS are normalised, excluding exceptional items. IFRS: 2007-2010.

Investment summary: Lower H2, rebound FY10

Today Next Fifteen (NFC) reported its interim results, which were a mixed blessing. Revenues rose 10% at £33.5m and the adjusted pre-tax margin improved to 10.6%. While the group continues to see a healthy new-business climate, many clients have reset their 2009 budgets, which the group believes will lead to a 10% revenue decline in the second half. In anticipation of this, headcount has been reduced by some 12%. We have lowered our estimates to reflect these conditions.

Strong first half

Revenues were a record half year in the group's history at £33.5m (versus £30.4m) and the adjusted pre-tax margin improved to 10.6%, up from a comparative 10.1%. Reported pre-tax profit of £1.44m included one-off items of £2.1m, primarily the previously announced adverse movement in fair value of the group's FX and interest hedges of £1.3m, staff reduction costs of £0.6m and office closure costs of £0.1m.

Reducing estimates – FY10 profit/EPS rebound expected

Despite the group continuing to see a healthy new-business climate, many clients have reset their 2009 budgets. The group is now expecting revenues in the second half to decline some 10% versus the first half. We have reduced our estimates accordingly. However, we expect a strong EPS rebound in FY10 with just modest organic growth and the absence of the adverse FX hedging costs suffered in FY09.

Positive operating cash flow keeps balance sheet solid

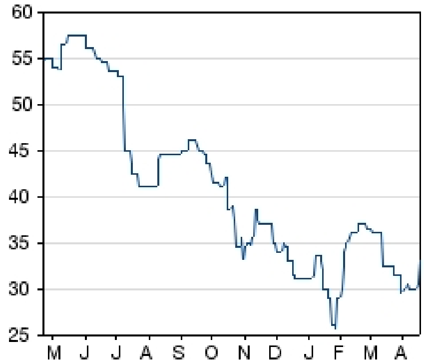
Positive cash flow from operations helped maintain the group's solid balance sheet. After the cash element of acquisitions of £4.4m during the half year, the group ended the period with modest net debt of £0.8m. NAV now stands at 48p.

Valuation: Good value despite 2009 lull

A prospective 6.0x P/E and 5.2% yield is an undemanding rating for a company with a history of strong client retention and good medium-term organic growth prospects, especially as we believe that profits should rebound in FY10 provided US dollar and euro exchange rates remain similar to current levels and minimal FX hedging is put in place. In addition, the group has a solid balance sheet and a price to book of 69%.

Price	33p
Market Cap	£18m

Share price graph



Share details

Code	NFC
Listing	AIM
Sector	Media
Shares in issue	54.1m

Price

52 week	High	Low
	57.5p	25p

Balance Sheet as at 31 January 2009

Debt/Equity (%)	3%
NAV per share (p)	48
Net borrowings (£m)	0.8

Business

Next Fifteen Communications is a global public and press relations consultancy group with world leading and autonomous PR, media research and marketing subsidiaries, predominately servicing clients in the technology sector.

Valuation

	2008	2009e	2010e
P/E relative	87%	142%	117%
P/CF	4.5	11.6	5.4
EV/Sales	0.6	0.6	0.6
ROE	23%	12%	14%

Geography based on revenues (H109)

UK	Europe	US	Other
27%	15%	46%	12%

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Next Fifteen Communications is a research client of Edison Investment Research Limited

Investment summary: Lower H2, rebound FY10

Company description: Global tech PR specialist

Founded in 1981, Next Fifteen Communications is a global public and press relations consultancy group with world leading and autonomous PR, media research and marketing subsidiaries, predominately servicing clients in the technology sector. Over the past six years, a series of accretive acquisitions has been successfully integrated into the group: Applied Communications and OutCast Communications in the US and Lexis Public Relations in the UK, as well as a number of smaller specialist firms to fill out the group's offering. The group is currently in discussions with a handful of companies outside the UK that are considered potential acquisitions.

The group has more than 300 clients serviced by 36 offices in 18 countries around the world and employs over 800 staff. Dependence on key clients is reducing, with the group's top 10 clients generating 33% of revenue, down from 35% a year ago. Of these, eight have worked with the group for over four years, four for over eight years and two for more than 16 years. The group continues to increase the number of international clients. At present, 33% of clients are international, representing 66% of revenue.

Once the imminent merger of Inferno into Bite UK is completed, the group will have three principal technology PR subsidiaries – Text 100, Bite and OutCast – that address the technology industry with over half of the world's top 25 technology businesses being clients, including Cisco, IBM, Microsoft, NXP and Sun Microsystems. The group's expertise in technology enables it to exploit the expansion in social media, such as blogs and social networking sites. On the non-technology front, Next Fifteen now fully owns Lexis, which operates in the UK and primarily addresses the consumer sector. The remaining equity in Panther Communications, the parent of Lexis, was acquired in October 2008.

Valuation: Good value despite 2009 lull

A prospective adjusted P/E of 6.0x and a well covered yield of 5.2% is not a demanding rating for a company with a history of strong client retention and good organic growth prospects, especially as we believe that profitability and EPS should rebound in FY10 provided US dollar and euro exchange rates remain similar to current levels and minimal FX hedging is put in place. In addition, the group has a solid balance sheet and a price to book value ratio of 69%.

Sensitivities

Our base case scenario includes four key assumptions:

- Major clients are retained. (NB: Oracle bid for Sun Microsystems yesterday).
- The US dollar and euro do not weaken or strengthen significantly.
- Technology industry growth stays robust.
- Key employees are retained.

A material change in any of these could surprise either on the upside or on the downside.

Financials: Solid balance sheet and low price to book

Positive cash flow from operations helped maintain the group's healthy balance sheet. After the cash element of acquisitions of £4.4m during the half year, the group ended the period with modest net debt of £0.8m. NAV now stands at 48p, giving a price to book ratio of 69%.

Interim results to 31 January 2009

Next Fifteen had a record half year with revenues of £33.5m, versus £30.4m in the first half of last year. The adjusted pre-tax margin improved to 10.6%, up from a comparative 10.1%. Reported pre-tax profit of £1.44m included one-off items of £2.1m, primarily the previously announced adverse movement in fair value of the group's FX and interest hedges of £1.3m, staff reduction costs of £0.6m and office closure costs of £0.1m. After a higher tax rate of 35.5%, primarily as a result of the currency contracts expiring before the end of FY09, reported EPS declined to 1.7p, down from 2.5p. Excluding the above one-off items, adjusted EPS rose 11% to 4.5p.

Business climate

As previously foreshadowed in its AGM trading update in January, management did not expect to be immune from the uncertain economic climate and responded by lowering ongoing operating costs with headcount reduced by 9% and the Seattle and Dublin offices closed down. Despite the group continuing to see a healthy new-business climate in all the main markets (adding such clients as Skype, SanDisk and Intuit), many clients have reduced their 2009 PR budgets. Nevertheless, a number of clients, including AMD, IBM and Cisco, did expand their relationships with the group.

Balance sheet continues to be healthy after acquisition costs

Positive cash flow from operations helped maintain the group's healthy balance sheet. After the cash element of acquisitions of £4.4m during the half year, the group ended the period with modest net debt of £0.8m. While we expect further positive cash flow from operations in the second half, a modest increase in net debt, to £1.5m at the end of FY09, is likely as both last year's final and this year's interim dividend (in total £0.9m) and corporate tax (£1.0m) are due to be paid in the second half. The remaining payment of £0.2m to OutCast shareholders is due soon after the FY09 year-end. The healthy balance sheet gives the group some firepower, together with renewed banking facilities, to target selective and earnings accretive acquisitions.

Reducing FY09 estimate to reflect 2009 lull

Despite trading showing some signs of improvement, management is now expecting revenues in the second half to decline some 10% versus the first half and has further reduced its staff numbers since January. We have reformulated our numbers accordingly, with our FY09 EPS estimate reduced to 5.5p from 6.6p. We also conservatively suggest a held final dividend for the year, though management is hopeful that the progressive dividend policy of recent years may be continued. The substantial decline in profitability for FY09 is down to the previously reported impact, estimated at £2.2m at current FX and US interest rates, of the crystallisation of the in-place hedging contracts, most of which expire at the end of this fiscal year. Without this charge, profits would have likely risen year-on-year, though EPS down slightly on the estimated higher tax charge.

Expecting strong EPS rebound in FY10

With the visibility of and the decline in many clients' PR budgets now evident over the past three months and the uncertain timing of a return to confidence, we are now estimating just modest organic growth in FY10. However, we expect a strong rebound in FY10 EPS to 7.7p (versus our previous estimate of 9.9p), aided by the absence of the substantial hedging costs suffered in FY09 and a projected return to the 2008 tax rate of 30%.

Exhibit 1: Financials

Year-ending 31 July	£'000s	2006	2007	2008	2009e	2010e
Accounting basis		UK GAAP	IFRS	IFRS	IFRS	IFRS
PROFIT & LOSS						
Billings		63,278	69,422	73,916	75,000	76,000
Revenues		56,007	59,268	63,107	63,500	64,500
EBITDA		5,970	7,302	8,022	5,765	7,100
Operating Profit (before GW and except.)		4,521	5,837	6,706	4,565	5,900
Goodwill Amortisation		(727)	0	0	0	0
Exceptionals		(700)	(458)	(1,066)	(1,990)	0
Other		174	56	117	275	225
Operating Profit		3,268	5,435	5,757	2,850	6,125
Net Interest		(265)	(313)	(241)	(350)	(100)
Profit Before Tax (norm)		4,430	5,580	6,582	4,490	6,025
Profit Before Tax (FRS 3)		3,003	5,122	5,516	2,500	6,025
Tax		(1,494)	(1,781)	(1,655)	(900)	(1,825)
Profit After Tax (norm)		2,649	3,713	4,657	3,000	4,200
Profit After Tax (FRS 3)		1,509	3,341	3,861	1,600	4,200
Average Number of Shares Outstanding (m)		46.5	49.0	51.7	53.7	54.1
EPS - normalised (p)		5.3	7.1	8.6	5.5	7.8
EPS - normalised fully diluted (p)		5.1	7.0	8.5	5.5	7.7
EPS - FRS 3 (p)		2.9	6.3	7.1	2.9	7.8
Dividend per share (p)		1.4	1.5	1.7	1.7	1.8
EBITDA Margin		9%	11%	11%	8%	9%
Operating Margin (before GW and except.)		8%	10%	11%	7%	9%
BALANCE SHEET						
Non-current assets		14,343	18,442	20,206	24,435	24,660
Intangible Assets		11,188	13,507	15,462	19,294	19,194
Tangible Assets		3,063	2,162	2,435	1,985	2,085
Other non-current assets		92	2,773	2,309	3,156	3,381
Current Assets		19,787	20,894	25,946	23,416	27,341
Debtors		15,769	15,060	16,421	17,873	18,673
Cash		4,018	5,834	9,525	5,543	8,668
Current Liabilities		(12,554)	(15,670)	(20,643)	(15,715)	(16,365)
Creditors		(11,739)	(14,958)	(20,228)	(15,300)	(15,950)
Short term borrowings		(815)	(712)	(415)	(415)	(415)
Long Term Liabilities		(6,834)	(8,684)	(5,871)	(6,665)	(6,665)
Long term borrowings		(4,642)	(5,190)	(5,700)	(6,633)	(6,633)
Other long term liabilities		(2,192)	(3,494)	(171)	(32)	(32)
Net Assets		14,742	14,982	19,638	25,471	28,971
CASH FLOW						
Operating Cash Flow		4,948	7,203	9,599	3,744	7,900
Net Interest		(325)	(311)	(240)	(350)	(100)
Tax		(2,430)	(1,992)	(1,090)	(1,000)	(2,175)
Capex		(1,203)	(1,246)	(2,153)	(665)	(1,500)
Acquisitions/disposals		(2,354)	(1,959)	(829)	(4,500)	0
Equity financing		232	953	(994)	(311)	0
Dividends		(590)	(691)	(807)	(900)	(1,000)
Other		0	0	0	0	0
Net Cash Flow		(1,722)	1,957	3,486	(3,982)	3,125
Opening net debt/(cash)		(2,449)	1,439	68	(3,410)	1,505
Finance leases		(20)	(299)	(217)	(242)	0
Other		(2,146)	(287)	209	(691)	0
Closing net debt/(cash)		1,439	68	(3,410)	1,505	(1,620)

Source: Company accounts, Edison Investment Research