UP Global Sourcing Holdings PLC

Brisk growth rate supports higher valuation

6th July 2020

The ongoing pandemic only serves to underline business models that are robust, and those that aren't. This morning's trading update from UPGS puts them firmly in the winners' category. As the company approaches the final weeks of FY2020, it not only reports "better than expected progress" against an uncertain business backdrop, but also that revenue and key profit measures for the year should be ahead of current market expectations. Furthermore, online as a portion of total business should record a fourth consecutive increase, providing additional flexibility and strength in the case of a second wave.

Brisk growth, higher online sales and demonstrable management flexibility is overdue more recognition from investors and a higher valuation for the business.

The unscheduled trading update released today includes three important upgrades. Revenue for the year ending 31st July 2020 is now expected to be above £111m, which compares with our most recent £105m forecast that we published in an 8th June 2020 report "Equity Development - Satisfying customer demand". New EBITDA and underlying pre-tax profits expectations also represent upgrades from our most recent forecasts: rising from £7.9m to above £9.6m and from £5.9m to above £7.4m, respectively.

UPGS's flexibility – a key component of its ability to deal with the economic uncertainty associated with Covid19 - is reflected in a higher portion of sales transacted online. We infer that the company is on-track to meet its 20% target for online sales sooner than expected. In the first half of the year online was 11.3% of sales compared with 9.3% in the same period as last year.

Despite the Covid-19 pandemic, UPGS's attractions as a growth story remain intact. Underlying demand growth for the company's "feel good" branded product is brisk having recorded 12% compound growth rate in the 5-years to FY2020, based on revised expectations. Moreover, the company's management should be highly commended for simultaneously continuing to source product out of China and growing end-market sales revenue despite the prevalence of lockdown in its key European markets.

A combination of brisk sales growth, an increased online portion of business and clear demonstration of agile management all argue in our view for a significantly higher valuation.

The company's 0.6x EV sales ratio appears surprisingly low given its ability to grow sales rapidly and profitably on a cash positive basis. Moreover, based on our revised estimates EV/EBITDA and the P/E ratios also look good value. Given the company's proven track record, we see a 1.0x EV/sales ratio, 10.4x EV/EBITDA and a 14.0x P/E ratio as being more appropriate.

The implied share price at these multiples is 100p.

Company Data

EPIC	UPGS
Price (last close)	68p
52 weeks Hi/Lo	99p/28p
Market cap	£56m
Net debt	£8m

Share Price, p

Source: ADVFN

Description

UP Global Sourcing Holding (UPGS) develops new, innovative concepts and brings professional, sought-after products to the mass market.

Their offices span two continents, with headquarters in the UK, a sourcing office and showroom in Guangzhou, as well as a showroom in Germany.

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Brisk growth rate augurs well for valuation

This report updates our forecasts for FY2020. We revise them upwards to be in line with the newly released guidance. In addition, we highlight the growth of online and discuss the case for a higher valuation in more detail.

Forecast revisions

We summarise our forecast revisions in Figure 1 below. The sales revenue estimate implies around £3m in new, and likely to be fulfilled, orders since the company previously released an RNS on 8th June 2020.

At that stage, total invoiced revenue for the FY2020 period was £97.2m and there were a further £10.6m of orders for the remainder of the year. This implied £107.8m in total. We raise our overall sales forecast by £6m with the bulk of additional revenue assumed to be spread evenly between the UK and Germany, as well as applying some increase in respect of the rest of Europe.

A combination of some gross margin benefits from online and operational gearing benefits should result in higher EBITDA margins than in our most recent forecasts. **We raise forecasts for all three of EBITDA, underlying pre-tax profits and EPS.**

Figure 1 – Revisions to FY2020 forecasts

£'000s	Old	New	Change (%)
Sales Revenue	105,000	111,000	5.7
EBITDA (underlying)	7,874	9,600	21.9
Pre-tax profit (underlying)	5,852	7,400	26.5
EPS basic adjusted (pence)	5.6	7.1	26.8

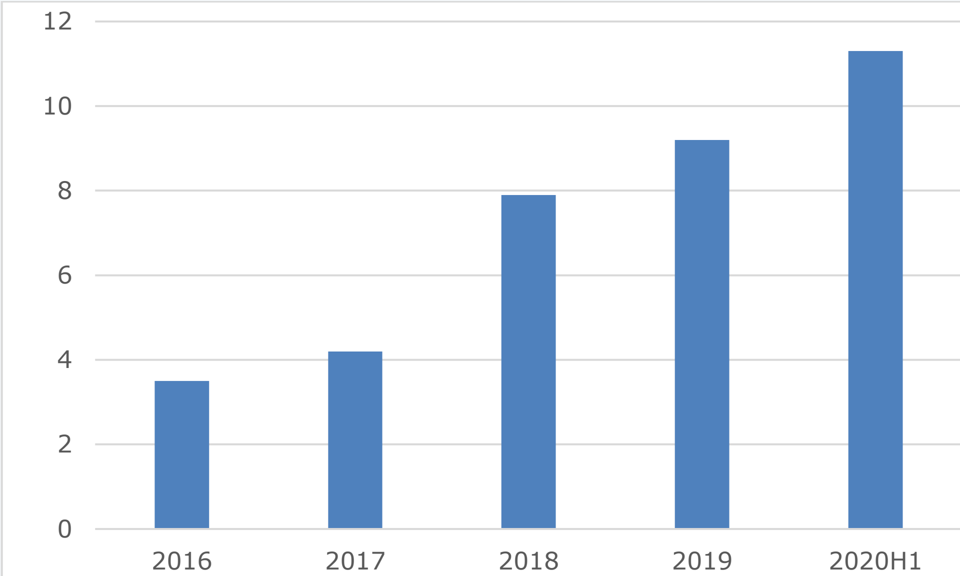
Source: Equity Development estimates

Targeting online

UPGS remains committed to expanding its online sales as a portion of total business to 20%. In the first half of FY2020 the number was 11.3% having been 9.3% in the same period a year earlier. Moreover, the progress of online as a portion of overall sales has been consistently positive. To illustrate the pace of growth, 5 years ago it was a relatively small proportion at 3.5%.

Online gives the company greater control over its end-distribution, which was notably important during the pandemic crisis and associated closures of non-essential stores. Further ahead, online has positive implications for working capital as well as (as mentioned above), gross margins. In Figure 2 we show recent yearly progress of online as a portion of total sales.

Figure 2 – Online as a portion of total sales (%)



Source: Company data and Equity Development estimates

Relative valuation

Based on recent commercial performance UPGS should in our view be regarded and valued as a growth company which has demonstrated both resilience and flexibility. Moreover, with a steady increase in the online portion of revenue there is an argument that its business should be perceived as being of a **better quality** than peers, and as such rated more highly in terms of key multiples.

Yet for now, as Figure 3 shows, UPGS continues to be valued at the lower end in terms of these multiples. The most reliable comparators are arguably EV/sales and EV/EBITDA. By both measures UPGS trades comfortably beneath our selected peer group averages. As a result, we argue that there is scope given the current tailwind of favourable newsflow for the shares to trade higher, with a return to **100p** as a first stop and well supported by ratings at that level.

Figure 3 – Comparative Valuation

	Share price (p)	Shares (m)	Mkt cap (£m)	Net debt (£m)	EV (£m)	Sales 2020 (£m)	EV/sales (x)	EBITDA 2020 (£m)	EV/EBITDA (x)	EPS 2020 (p)	P/E 2020 (x)
Accrol Group	**46**	**195**	90	189	279	133	2.1	7.8	35.7	n/a	n/a
Gear4Music	380	21	52	3	55	143	0.4	10.3	5.3	19.4	19.6
Luceco	100	161	161	18	179	138	1.3	15.2	11.8	2.0	50.0
Portmeirion Group	365	11	39	19	58	102	0.6	n/a	n/a	60.5	6.0
UPGS	**68**	**82**	**82**	**8**	**90**	**111**	**0.8**	**9.6**	**9.4**	**7.1**	**9.5**
Warpaint	70	77	54	-4	50	51	1.0	6.4	7.6	n/a	n/a
Average							1.0		14.0		21.3

Source: Company data, financial websites and Equity Development estimates

Investor Access

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