

GEAR4MUSIC

CONSUMER DISCRETIONARY

20 June 2023

G4M.L

103p

Market Cap: £21.5m

SHARE PRICE (p)



12m high/low

183p/83p

Source: LSE Data (priced as at prior close)

KEY DATA

Net (Debt)/Cash	£(14.5)m (at 31/03/23)
Enterprise value	£36m
Index/market	AIM
Next news	AGM - September
Shares in Issue (m)	21.0
Chairman	Ken Ford
Chief Executive	Andrew Wass
CFO	Chris Scott

COMPANY DESCRIPTION

Gear4music is a leading international online retailer of musical instruments and equipment.

www.gear4musicplc.com

GEAR4MUSIC IS A RESEARCH CLIENT OF
PROGRESSIVE

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Adopting a balanced approach for FY24E

G4M delivered FY23 full year results in line with the guidance given in its April trading update. EBITDA came in at £7.4m with year-end net debt of £14.5m. The consumer backdrop remains challenging, especially for retailers of primarily discretionary items. In March, G4M launched its second-hand platform, which plays to both customer service and convenience as well as to its own circular economy credentials. This enhanced margin service will be expanded in terms of product and geographic coverage over the coming year.

- FY23 results – disciplined approach to FY24E.** The decline in FY23 EBITDA was driven by the combination of weaker than expected sales growth at the tail end of the year, a 220bps decline in gross margin percentage, and a 6% increase in the operating cost base. The business is to prioritise its focus in FY24E on product margins, overhead cost reduction, and efficiency ahead of revenue growth. Initiatives to support product margins, over and above the second-hand service, include significant own-brand product launches, licensing agreements and system improvements. G4M will also target further net debt reduction through inventory optimisation and disciplined investment in terms of capital expenditure and development costs.
- Net debt – RCF renewed.** Inventory levels and net debt were both successfully reduced by significant levels of £11m and £10m respectively in FY23 as planned at the beginning of the year. On the back of this performance, G4M has renewed its committed borrowing facility with HSBC for a further three years. This has been agreed at £30m with a positive directional reduction of £5m from the previous facility of £35m.
- Outlook – forecasts unchanged.** The softer trading conditions seen in the last two months of FY23 have continued into the current financial year. At this early stage of the year and given the importance of the Q3 peak trading period (October to December) to the full year outturn, we are leaving our forecasts unchanged at this point from the revisions made in the wake of the April FY23 full year trading update. It is not inconceivable that the shape of our forecasts could flex between top line generation, gross margin percentage and operating costs, with G4M having many levers it can adjust dependent on the trading environment and economic backdrop. We shall review forecasts on the basis of company newsflow, with the first trading update due alongside the AGM in September (TBC).

FYE MAR (£M)	2021	2022	2023	2024E	2025E
Revenue	157.5	147.6	152.0	161.1	174.0
Adj EBITDA	19.8	11.2	7.4	10.0	12.0
Fully Adj PBT	14.6	5.0	-0.4	1.4	2.7
Fully Adj EPS (p)	59.7	17.3	-3.0	4.9	9.3
EV/Sales (x)	0.2x	0.2x	0.2x	0.2x	0.2x
EV/EBITDA (x)	1.8x	3.2x	4.9x	3.6x	3.0x
PER (x)	1.7x	5.9x	N/A	21.0x	11.0x

Source: Company Information and Progressive Equity Research estimates.

This publication should not be seen as an inducement under MiFID II regulations.

Please refer to important disclosures at the end of the document.

Building long-term growth initiatives

G4M is to adopt a balanced approach to FY24E, given the continuing weakness of trading conditions seen in Q4 FY23, most notably the final two months of February and March. Consumer demand across its geographic markets is described as remaining volatile and difficult to predict. Against this backdrop, it is unsurprising that cost control and disciplined investment will continue as priorities in FY24E with the aim of returning the group to profitability during H2 FY24E. The key drivers within this will be product margins, which have fallen back over the past two years from the Covid lockdown high in FY21, improvements to efficiency to overall productivity and efficiency, and overhead cost reduction.

It is important however to note that these measures will be prioritised ahead of revenue growth rather than at the expense of revenue growth. Several business and service initiatives are in the early days of development and have yet to gain meaningful or fully optimised traction in terms of revenue and profit generation. We would point to three specific examples:

- The recent launch of a second-hand platform
- AV.com
- Incremental distribution capacity and capabilities in Europe

Second-hand platform

G4M describes this platform and customer service proposition as its largest and most ambitious development project to date. This description underscores the potential G4M sees in this development. Given that the second-hand platform only had its soft launch in March, it is clearly early days in terms of revenue generation. It not only offers customers a quick and easy way to sell their pre-loved instruments, but it gives existing and new/potential customers more reasons to visit G4M's proprietary platform. As such, it can help to drive website traffic and reinforce brand loyalty.

The system simplifies the process of selling an instrument for customers by offering them an instant trade-in price across thousands of products. As of 3 April, this stood at 7,500 products, but has risen steadily since to currently stand at 12,000 products available for trade-in.

In business terms, the service should deliver gross margins more akin to own brand product margins and therefore be margin enhancing at the group level. It remains to be seen if there might be a sales cannibalisation effect, in the sense that potential customers in the market for a new instrument could be attracted instead by a second-hand product through the new platform. This said, there are trading-up or replacement selling opportunities to customers selling their instruments through the platform. The platform offers selling customers an attractive cash price or an enhanced account credit value which can be put towards the customer's next purchase. To date, the majority of sellers have chosen the credit option rather than the cash price option.

The platform has traded over 1,000 products in its first three months, which represents an encouraging start. The initial launch period has been limited to what are perceived as safer products in order to de-risk the launch phase. The platform's soft launch has been limited to the UK but will be rolled out on further European websites over the coming months, with AV.com to also follow in FY24.

The project ensures that product lifespans are maximised, whilst offering enhanced margin opportunities for the group and contributing to its endeavours on the ESG front.

AV.com

As with most business acquisitions, especially those integrated into a new ecosystem, rather than operating as previously on a standalone business, it can take time for them to find their feet. This has probably been the case to a certain extent with AV.com in our view, which boasts an estimated addressable European market of £2.7bn.

From a relatively subdued start, we believe growth rates should have improved markedly from a low base, especially given the combination of an improved proposition with better curation, supported by some good people hires into the business. The group is now building and improving the search side of the business to drive better customer traction. Following the UK launch in January 2022, AV.com was launched in Europe in FY23, which should deliver incremental sales growth in FY24E.

AV.com currently lists some 6,300 SKUs through online representation of 195 brands. Since its acquisition, AV.com has new management, content & merchandising teams in place, which has galvanised the development of the customer proposition and the upgrading of the Bacup warehouse facility, doubling the previous storage capacity. AV.com can also dispatch from other group warehouses, increasing flexibility and speed of delivery. The onsite showroom in Bacup has also been upgraded to showcase and support new brands added to the range, with a showroom in Germany also slated for Q4 to help underpin European sales growth.

European distribution network

The opening of two extra distribution centres (DCs) in The Republic of Ireland and Spain to support the existing DCs in Sweden and Germany has clearly already benefitted the group, by adding incremental distribution capacity within the EU territories. This is borne out by the revenue growth of 8% in International sales (primarily the EU) in FY23, compared with the small decline in UK sales. The new DCs have become better established within their local markets, whereby they now offer a considerably more attractive and localised customer proposition, notably in the area of speed and cost of delivery using local couriers.

There is considerable capacity within the European DC network to underpin future growth. The four units have a combined sales capacity of £155m, more than double the turnover generated in FY23. This compares with the current UK DC sales capacity of £125m. While G4M is better known, more established and with a higher market share in its home market, even with a lower market share penetration across the totality of the main European markets, G4M's European turnover should overtake that of the UK over the medium- to long-term.

Other initiatives

G4M has many other projects and initiatives underway in addition to these three highlighted here. These include third party fulfilment, which will leverage its distribution and logistics capabilities, with a scheduled launch in Q2 FY24, and agency sales with a scheduled system release in FY25. This points to the group's longer-term goals of profitable sales growth not being put aside, even when near-term challenges necessitate a firmer hand on the wheel in terms of cost control and efficiency, as highlighted by G4M for FY24E.

FY23 results

The key highlights and figures for the FY23 period had already been outlined in the April full-year trading update. Publication of the full-year results gives greater insight into the composite parts of the profit & loss account at all levels, together with more detailed cash flow and balance sheet elements.

The following table presents a more detailed summary overview of the results. We have included figures for the past four years from FY20, this being the last year before the intervention of Covid and its ramifications on the wider economy. It can clearly be seen from the FY21 figures that G4M was one of the minority of commercial enterprises to have been a beneficiary on Covid and its accompanying lockdowns. For this reason, we, like the company itself, compare the FY23 results both to the prior FY22 year and to FY20, representing the conditions prevailing in pre-pandemic trading.

Overview of FY22 results, compared with FY22, FY21 and FY20 (£m unless otherwise stated)

	FY20	FY21	FY22	FY23	FY23 change		FY23 change	
					on FY22	on FY22 (%)	on FY20	on FY20 (%)
UK sales	61.8	78.7	82.6	82.1	-0.5	(1%)	20.3	33%
International sales	58.5	78.8	65.0	70.0	5.0	8%	11.5	20%
Total sales	120.3	157.5	147.6	152.0	4.4	3%	31.7	26%
Product sales	114.8	149.6	140.6	145.1	4.5	(6%)	30.3	22%
Product gross profit	35.1	50.9	45.2	43.6	(1.6)	(11%)	8.5	29%
<i>Product gross margin</i>	<i>30.5%</i>	<i>34.1%</i>	<i>32.1%</i>	<i>30.0%</i>	<i>-210bps</i>		<i>-50bps</i>	
Gross profit	31.2	46.4	41.1	39.0	(2.1)	(10%)	7.8	45%
<i>Gross margin</i>	<i>25.9%</i>	<i>29.4%</i>	<i>27.9%</i>	<i>25.7%</i>	<i>-220bps</i>		<i>-20bps</i>	
Operating costs :								
Marketing	(9.3)	(9.2)	(10.8)	(10.6)	0.2	(2%)	(1.3)	14%
Labour	(9.7)	(12.3)	(13.1)	(14.4)	(1.3)	10%	(4.7)	48%
Europe/other	(4.4)	(5.1)	(6.0)	(6.7)	(0.7)	12%	(2.3)	52%
Total opex	(23.4)	(26.6)	(29.9)	(31.7)	(1.8)	6%	(8.3)	35%
EBITDA	7.8	19.8	11.2	7.4	(3.8)	(34%)	(0.4)	(5%)
<i>EBITDA margin</i>	<i>6.4%</i>	<i>12.6%</i>	<i>7.6%</i>	<i>4.8%</i>	<i>-270bps</i>		<i>-160bps</i>	
Total DA	3.7	4.4	5.1	6.1	1.0	18%	2.4	65%
Operating profit	4.1	15.4	6.1	1.3	(4.8)		(2.8)	
<i>Operating profit margin</i>	<i>3.4%</i>	<i>9.8%</i>	<i>4.1%</i>	<i>0.8%</i>	<i>-330bps</i>		<i>-260bps</i>	
Financial expenses	(1.0)	(0.8)	(1.1)	(1.7)	(0.6)		(0.7)	
Pre tax profit	3.1	14.6	5.0	(0.4)	(5.4)	(108%)	(3.5)	(113%)
Diluted EPS (p)	12.2	59.7	17.3	(3.1)	(20.4)	(118%)	(15.3)	(125%)

Source: Gear4music, Progressive Equity Research

Against the April EBITDA range guidance of £7.3m to £7.8m, G4M delivered EBITDA of £7.4m, with EBITDA margin falling back some 270bps from FY22's outturn to 4.8%. While turnover rose by 3%, the combination of lower absolute gross profit, with gross margins some 210bps lower, and a 6% (£1.8m) increase on operating costs drove the decline at the EBITDA level.

Development of total turnover and product sales – FY18 to FY23 (£m)

	FY18	FY19	FY20	FY21	FY22	FY23
Reported own brand sales	20.947	31.289	35.432	45.368	38.121	38.860
Reported third party brand sales	56.075	82.125	79.416	104.199	102.473	106.189
Reported product sales	77.022	113.414	114.848	149.567	140.594	145.049
Warranty income	0.302	0.296	0.337	0.545	0.483	0.452
Finance commissions	0.112	0.240	0.285	0.204	0.287	0.351
Carriage receipts	2.664	4.205	4.856	7.135	6.266	6.187
Total other income	3.078	4.741	5.478	7.884	7.036	6.990
Total turnover	80.100	118.155	120.326	157.451	147.630	152.039

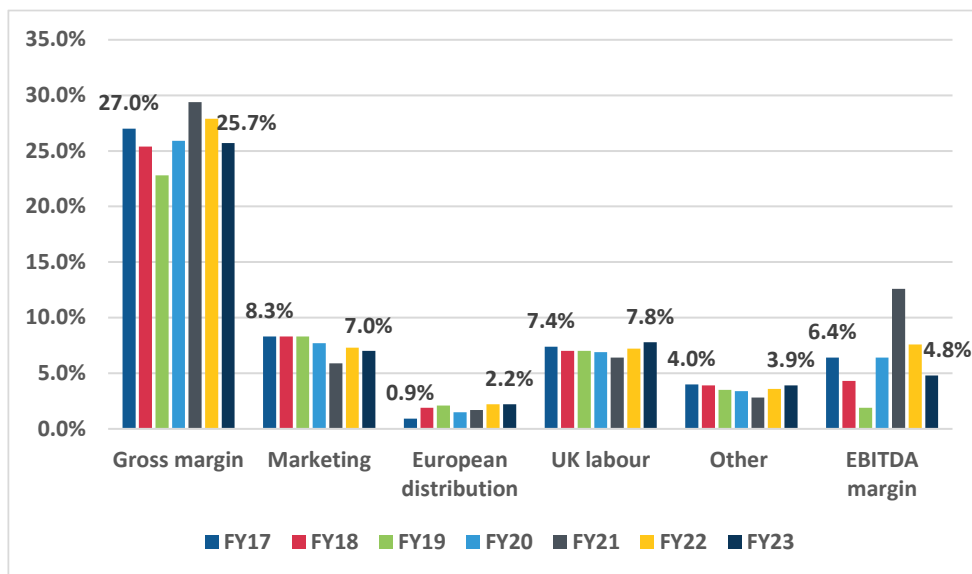
Source: Gear4music, Progressive Equity Research

G4M successfully delivered on its stated ambition of reducing its net debt, with FY23 year-end net debt of £14.5m some £9.7m less than the year-end figure for FY22 (£24.2m). With interest rates also rising, it was important to show a disciplined approach to cost management and inventories. The 2% reduction in marketing spend was a major factor in helping to hold down the overall increase to 6% in the operating cost base (excluding depreciation and amortisation), given the double digit increases in labour and other costs. There has been significant inflationary pressure in marketing, labour and energy in this latest financial period, which look set to continue into FY24E.

Having invested in higher levels of inventory both to take advantage of commercial opportunities and to provide stock continuity against a backdrop of supply chain disruption in FY22, the rapid increase in interest rates exacerbated the costs of holding stock against a backdrop of falling consumer confidence and lower levels of discretionary spending. G4M's profitability has been adversely impacted by the active and planned reduction in its inventory level. Combined with a period of weak demand, this destocking resulted in a lower than planned product (and overall) gross margin. FY23 year-end balance sheet inventory stood at £34.4m, some £11m lower than the FY22 figure of £45.5m. This reduction has largely unwound the £17m inventory investment made in FY22. The current level of inventories compares more favourably with the £28.4m at the end of FY21 and is both sufficient and better aligned with the near-term trading outlook and prospects in our view.

The following chart shows the bridge from gross margin down to EBITDA margin from FY17 to FY22. This clearly shows the impact of the record year of FY21 in terms of gross and EBITDA margins, together with leveraged cost ratio efficiencies. It also shows the reset to focus on profitable growth, rather than just top-line growth, made after FY19 trading period. Product gross margin in FY23 of 30.0% is some 50bps below the level achieved in FY20 (albeit some 220bps ahead of the FY19 nadir). With the increased level of own brand stockkeeping units (SKUs) which command a higher gross margin percentage, revamped entry level and premium ranges, and expanded Premier ranges, we believe the product gross margin should see some recovery in FY24E.

Historical bridge from gross margin to EBITDA margin – FY17 to FY23 (%)



Source: Gear4music, Progressive Equity Research

Since the year-end, G4M has renewed its banking facilities with HSBC. This provides a committed facility of £30m until 2026, which represents a £5m reduction from the previous arrangement. This is a positive directional move, especially when paying non-utilisation fees on undrawn facilities, and will help to mitigate overall financial charges, despite a rising interest rate environment.

Key performance indicators (KPIs) and metrics

The following sections provide an overview of G4M’s KPIs and other operating metrics.

Website users and conversion rates

The major success story in terms of this important area over recent years has been the increase in the conversion rate. This had increased from 3.3% in FY20 to 4.1% in FY22. This dropped back marginally in FY23, but still stands at just over 4%. The FY23 conversion rate is some 66bps ahead of the FY20 figure and more than double the FY15 figure of 1.96%.

The mobile user mix saw a dramatic increase of almost twenty percentage points to 72%. Combined with a 53bps decline in mobile conversion, this was a contributory factor to the overall marginal decline in the total conversion rate. In terms of conversion rate by geography, the UK saw a 99bps decline to 4.5%, while Europe enjoyed a 56bps increase to 3.5%.

The number of unique website users fell again in FY23, following the understandable decline from the FY21 Covid-driven peak, with declines in both UK and international users of 5% and 9% respectively. This said, the total number of pages viewed registered an increase of 4% to 149m.

Website utilisation and conversion rates

	FY20	FY21	FY22	FY23	FY23 % change	
					on FY22	on FY20
Unique website users (m)	28.4	36.0	28.8	26.5	(8%)	(7%)
Total pages viewed (m)	150	170	143	149	4%	(1%)
UK users (m)	11.0	14.4	13.1	12.5	(5%)	19%
International users (m)	16.6	20.8	15.1	13.7	(9%)	(17%)
Mobile user mix	56.0%	55.0%	53.0%	72.0%	+1900bps	+1600bps
Organic/direct traffic	39.0%	42.0%	49.0%	47.0%	-200bps	+800bps
Conversion rates:						
UK	4.8%	5.5%	5.5%	4.5%	-99bps	-27bps
Europe	2.4%	2.6%	2.9%	3.5%	+56bps	+112bps
Mobile	2.4%	2.7%	3.2%	2.7%	-53bps	+30bps
Total	3.3%	3.7%	4.1%	4.0%	-11bps	+66bps

Source: Gear4music, Progressive Equity Research

Customer base metrics

The number of customers served fell by 6% in FY23 to 865,000 but remains some 7% higher than the FY20 figure of 807,000. A similar pattern can be seen with regard to new customer numbers. These fell by 7% to 738,000 in FY23, but this remains some 5% higher than the FY20 figure. The number of repeat customers nudged back marginally in FY23 to 172,000, thereby showing a 1% increase over the FY20 figure.

Customer metrics

	FY20	FY21	FY22	FY23	FY23 % change	
					on FY22	on FY20
Customers served ('000)	807	1,064	921	865	(6%)	7%
New customers ('000)	704	947	793	738	(7%)	5%
Repeat customers	170	206	174	172	(1%)	1%
Email subscriber database ('000)	650	980	1,280	1,650	29%	154%
Average order value	£117	£116	£125	£150	20%	28%

Source: Gear4music, Progressive Equity Research

Great strides continue to be made with the email subscriber base, which recorded just under a 30% increase to 1.65m subscribers. This is a million higher than the FY20 figure, representing an increase of over 150% over the period.

The average order value (AOV) rose by an impressive 20% in FY23 to £150, such that the AOV is now almost 30% higher than the FY20 figure of £117. This increase has been driven by a combination of price increases in both own and third party brands, and sales mix.

The gross profit per transaction stood at £36 (FY22: £33, FY21: £32, FY20: £30) compared with a new customer acquisition cost of £14 (FY22: £14 FY21: £9, FY20: £12). This underlines the fact that G4M is profitable from the very first customer transaction, unlike companies in other product sectors such as clothing and groceries. The lifetime sales value of customers increased by 25% to £302, compared with £241 in FY22 and £212 in FY20.

Product range development

A consistent factor contributing to G4M's rising turnover line has been the unrelenting expansion of the product offer, as shown through the total number of SKUs. The range saw a further 3% growth in FY23 to 64,200 SKUs. This figure is 10,000 (18%) higher than the line count in FY20.

Product range development – total and own brand

	FY20	FY21	FY22	FY23	FY23 % change	
					on FY22	on FY20
Total number of SKU's	54,200	57,900	62,400	64,200	3%	18%
Brands listed	880	900	1,080	1,130	5%	28%
Own brand performance :						
Own brand SKU's	3,400	3,800	4,200	4,900	17%	44%
Own brand SKU mix	6.3%	6.6%	6.7%	7.6%	+90bps	+136bps
Own brand sales mix (total sales)	29.4%	28.8%	25.8%	25.6%	-26bps	-389bps
Own brand sales mix (product sales)	30.9%	30.3%	27.1%	26.8%	-32bps	-406bps

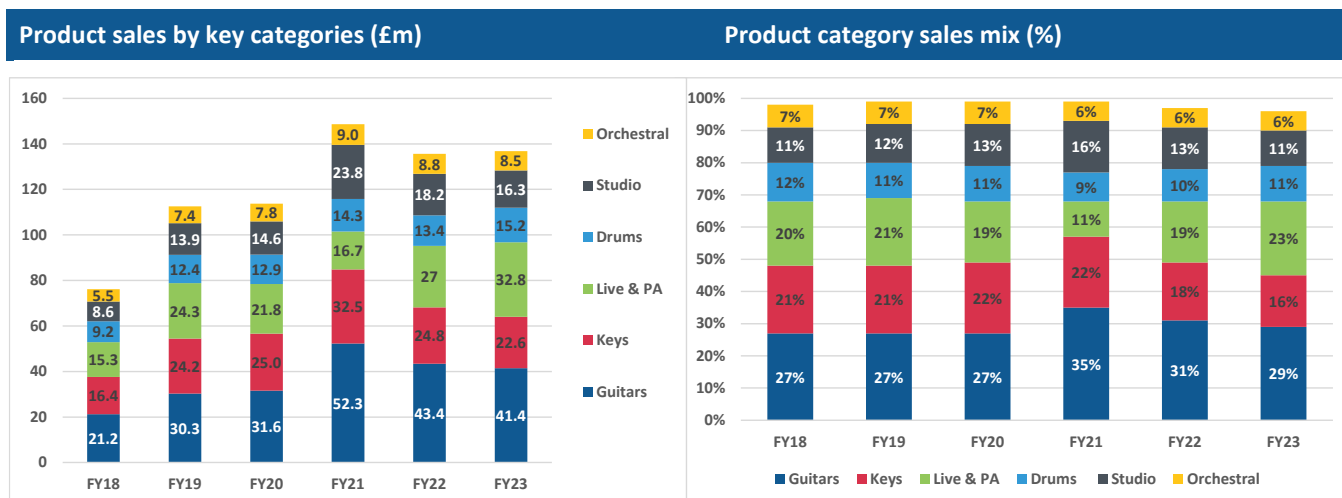
Source: Gear4music, Progressive Equity Research

Within its range proposition, own brands remain an important point of differentiation for the group, offering quality products at advantageous prices to customers, whilst also delivering a much superior gross margin percentage compared with third party brands. The gross margin differential has historically been between 15 and 20 percentage points higher than for third party brands. Own brand products therefore outperform in terms of turnover and gross profit contribution compared with third party products. In FY23, own brand products represented 7.6% of total SKUs, while delivering 25.6% of total product sales.

This said, the own brand sales mix has been declining since FY20 when it stood at just under 31%. This partly reflects a marked post-Covid slowdown in demand for entry level products, which has long been a traditional strength of G4M. Another factor has been the channel shift of some Far East manufacturers to selling direct into Europe via Amazon, thereby increasing competition in this market. G4M has responded by both increasing its own brand SKU count, as well as revamping not only entry levels but also its more premium ranges.

FY24E will see some significant own brand product launches. These include the G4M brand, offering great value, premium music gear. This is due to launch on 29 June, with a total of over 130 new products launching this year. The company has also launched a value driven brand, Vision, covering a number of categories including drums, guitars and keyboards. Vision is designed to compete with third party Amazon sellers. The Premier premium drums and percussion brand has seen a positive sales reaction to new product launches in FY23. This momentum should continue in the current financial year, and G4M has concluded a licence agreement to sell the Premier brand into the USA market.

The chart below shows the absolute sales value and sale mix participation of the major categories sold by G4M. The impact of Covid can clearly be seen in the mix participation (and implicit directional sales movement) of various categories. In FY21, with people spending more time at home taking up new or revisiting old pastimes and hobbies, this resulted in substantial growth of categories such as guitars and studio, mirrored by a substantial decline in the Live & PA category. Subsequently, with the advent of more normal living and social conditions in FY22, there was some unwinding of those most marked movements seen in FY21.



Source: Gear4music, Progressive Equity Research

Against an overall increase of just over 3% for product sales in FY23, only two of the major categories detailed by G4M delivered a higher level of sales increase. These were Live & PA (+21.5%) and drums (+13.4%) and this outperformance is reflected in the growth of their share within the product sales mix. The increase in Live & PA continues the trend emerging last year, which reversed the substantial decline caused by the lockdowns during the pandemic, as live performances and social gatherings resumed apace. All other categories recorded declines of between 3% (Orchestral) and 10% (Studio).

Forecasts

We have left our forecasts unchanged at this early stage of the year. These therefore reflect the revisions made at the time of the April year-end trading update, following the softer than expected trading conditions experienced in Q4, most notably in February and March.

The outlook statement clearly points to no change in the challenging consumer environment since April. The company is taking what it describes as appropriate and necessary actions to ensure the business is configured appropriately for longer term commercial success, alongside an implicit indication in our view that it will not shy from actions to protect shorter-term commercial returns and its ambition to return to profitability during H2 FY24.

This will involve a balance of measures between top line revenues, and operating costs and efficiencies. The company has a number of levers at its disposal to this end, including product pricing and gross margins; labour productivity; flexing marketing spend to drive a higher return on investment (ROI); and potentially reducing development costs and capex.

We also believe there are specific areas of operating costs that G4M will seek to address and mitigate, such as the £0.5m (24%) increase in card processing costs seen in FY23. Following the UK's withdrawal from the EU, in October 2021 Visa and Mastercard increased cross-border interchange fees. Fees increased from 0.2 per cent to 1.15 per cent for debit cards and 0.3 per cent to 1.5 per cent for credit card transactions, thereby considerably increasing costs to G4M and other businesses operating cross borders between the UK and the EEA (European Economic Area). A solution to reduce and mitigate these increased costs could entail an UK/EU entity split at some stage.

Forecast summary and 2-year CAGR to FY25E

	FY22	FY23	FY24E	FY25E	2-yr CAGR
Revenue	147.6	152.0	161.1	174.0	4.6%
Gross profit	41.1	39.0	43.0	47.3	6.6%
Gross margin (%)	27.9%	25.7%	26.7%	27.2%	
Operating costs (exc DA)	29.9	31.7	33.1	35.4	3.7%
Opex as % of turnover	20.3%	20.8%	20.5%	20.3%	
EBITDA	11.2	7.4	10.0	12.0	17.5%
EBITDA margin (%)	7.6%	4.8%	6.2%	6.9%	
Operating profit	6.1	1.3	2.9	4.2	48.6%
Operating margin (%)	4.1%	0.8%	1.8%	2.4%	
Adjusted pre-tax profit	5.0	(0.4)	1.4	2.7	
Adjusted diluted EPS (p)	17.3	(3.0)	4.9	9.3	
Net cash/(debt)	(24.2)	(14.5)	(12.5)	(11.0)	

Source: Gear4music, Progressive Equity Research

We believe that G4M will focus on driving a higher level of EBITDA and a return to profitability during H2 FY24E. To that end, there could possibly be a reshaping to our forecasts, especially if there was protracted weakness in consumer confidence and discretionary spending. This will depend on the pattern of trading in forthcoming updates, the first of which accompany the AGM around the beginning of September (TBC).

Our forecast summary above includes the 2-year compound annual growth (CAGR) figure for key measures from the reported FY23 base. More detailed forecasts for P&L, cash flow and balance sheet are shown in the following tables.

Summary of profit & loss account and cash flow forecasts

Profit and loss account	IFRS16	IFRS16	IFRS16	IFRS16	IFRS16	IFRS16
Year to March	FY20	FY21	FY22	FY23	FY24E	FY25E
Revenue	120.3	157.5	147.6	152.0	161.1	174.0
Cost of sales	(89.2)	(111.1)	(106.5)	(113.0)	(118.1)	(126.7)
Gross profit	31.2	46.4	41.1	39.0	43.0	47.3
<i>Gross margin (GM) (%)</i>	<i>25.9%</i>	<i>29.4%</i>	<i>27.9%</i>	<i>25.7%</i>	<i>26.7%</i>	<i>27.2%</i>
Operating costs	(27.1)	(30.9)	(35.1)	(37.8)	(40.1)	(43.1)
Operating profit	4.1	15.4	6.1	1.3	2.9	4.2
<i>Operating profit margin (%)</i>	<i>3.4%</i>	<i>9.8%</i>	<i>4.1%</i>	<i>0.8%</i>	<i>1.8%</i>	<i>2.4%</i>
Depreciation and amortisation	(3.7)	(4.4)	(5.1)	(6.1)	(7.0)	(7.7)
EBITDA	7.8	19.8	11.2	7.4	10.0	12.0
<i>EBITDA margin (%)</i>	<i>6.4%</i>	<i>12.6%</i>	<i>7.6%</i>	<i>4.8%</i>	<i>6.2%</i>	<i>6.9%</i>
Interest charge	(1.0)	(0.8)	(1.1)	(1.7)	(1.5)	(1.5)
Adjusted PBT	3.1	14.6	5.0	(0.4)	1.4	2.7
Exceptional charges	0.0	0.0	0.0	0.0	0.0	0.0
Profit before tax	3.1	14.6	5.0	(0.4)	1.4	2.7
Adjusted diluted EPS (p)	12.2	59.7	17.3	(3.0)	4.9	9.3
Diluted EPS (p)	12.2	59.7	17.3	(3.0)	4.9	9.3
Dividend (p)	0.0	0.0	0.0	0.0	0.0	0.0
Cash flow	FY20	FY21	FY22	FY23	FY24E	FY25E
Year to March						
Operating profit	4.1	15.4	6.1	1.3	2.9	4.2
Depreciation and amortisation	3.7	4.4	5.1	6.1	7.0	7.7
Inventory (increase)/decrease	(3.4)	(6.4)	(14.2)	11.1	3.0	1.0
Debtors (increase)/decrease	(0.8)	(1.2)	0.3	0.0	0.3	(0.2)
Creditors increase/(decrease)	3.3	2.7	(2.2)	1.9	(0.7)	(0.9)
Other	0.4	0.1	0.8	(0.2)	0.0	0.0
Operating cash flow	7.2	15.0	(4.1)	20.2	12.5	11.9
Interest	(0.8)	(0.8)	(1.1)	(1.7)	(1.5)	(1.5)
Tax	0.5	(0.0)	(2.7)	(0.5)	(0.4)	(0.7)
Dividends	0.0	0.0	0.0	0.0	0.0	0.0
Deferred tax	0.0	0.0	0.0	0.0	0.0	0.0
Capital expenditure	(3.6)	(4.4)	(6.2)	(6.3)	(7.0)	(6.5)
Trading cash flow	3.3	9.8	(14.1)	11.6	3.6	3.1
Acquisition of businesses	(0.4)	(0.2)	(10.4)	(0.4)	0.0	0.0
Disposal of businesses	0.0	0.0	0.0	0.0	0.0	0.0
Share issues	0.0	0.0	0.0	0.0	0.0	0.0
Currency effects, other	(1.0)	(1.3)	(2.4)	(1.6)	(1.6)	(1.6)
Net cash inflow/(outflow)	2.0	8.3	(26.9)	9.6	2.0	1.6
Net (debt)/cash	(5.5)	2.7	(24.2)	(14.5)	(12.5)	(11.0)

Source: Gear4music, Progressive Equity Research

Summary of balance sheet forecasts

Balance sheet	IFRS16	IFRS16	IFRS16	IFRS16	IFRS16	IFRS16
Year to March	FY20	FY21	FY22	FY23	FY24E	FY25E
Tangible fixed assets	20.2	19.1	21.2	19.2	17.8	15.6
Intangible fixed assets	9.1	10.4	19.8	22.0	23.5	24.4
Investments and other	0.0	0.0	0.0	0.0	0.0	0.0
Total fixed assets	29.3	29.5	41.0	41.3	41.2	40.0
Stock	22.0	28.4	45.5	34.4	31.4	30.4
Trade and other debtors	2.5	3.6	3.8	4.5	4.2	4.3
Deferred tax	0.0	0.0	0.0	0.0	0.0	0.0
Cash and short term deposits	7.8	6.2	3.9	4.5	3.0	4.0
Current assets	32.4	38.3	53.3	43.3	38.6	38.8
Total assets	61.6	67.7	94.3	84.6	79.8	78.8
Trade and other payables	(14.4)	(18.9)	(16.2)	(17.6)	(16.9)	(16.0)
Borrowings	(9.9)	(0.6)	0.0	0.0	0.0	0.0
Other current liabilities	(1.1)	(1.1)	(1.2)	(1.1)	(1.1)	(1.1)
Current liabilities	(25.5)	(20.6)	(17.4)	(18.8)	(18.0)	(17.1)
Borrowings	(3.4)	(2.9)	(28.0)	(19.0)	(15.5)	(15.0)
Other non-current liabilities	(11.0)	(9.9)	(10.8)	(9.6)	(9.6)	(9.6)
Non-current liabilities	(14.5)	(12.8)	(38.9)	(28.6)	(25.1)	(24.6)
Total liabilities	(40.0)	(33.4)	(56.3)	(47.4)	(43.1)	(41.7)
Net assets	21.6	34.3	38.0	37.2	36.7	37.1

Source: Gear4music, Progressive Equity Research

Financial Summary: Gear4music

Year end: March (£m unless shown)

	2021	2022	2023	2024E	2025E
PROFIT & LOSS					
Revenue	157.5	147.6	152.0	161.1	174.0
Adj EBITDA	19.8	11.2	7.4	10.0	12.0
Adj EBIT	15.5	6.1	1.3	3.0	4.3
Reported PBT	14.6	5.0	(0.4)	1.4	2.7
Fully Adj PBT	14.6	5.0	(0.4)	1.4	2.7
NOPAT	13.4	4.6	2.1	2.2	3.2
Reported EPS (p)	59.7	17.3	(3.0)	4.9	9.3
Fully Adj EPS (p)	59.7	17.3	(3.0)	4.9	9.3
Dividend per share (p)	0.0	0.0	0.0	0.0	0.0
CASH FLOW & BALANCE SHEET					
Operating cash flow	15.0	(4.1)	20.2	12.5	11.9
Free Cash flow	9.8	(14.1)	11.6	3.6	3.1
FCF per share (p)	46.8	(67.2)	55.4	17.3	15.0
Acquisitions	(0.2)	(10.4)	(0.4)	0.0	0.0
Disposals	0.0	0.0	0.0	0.0	0.0
Shares issued	0.0	0.0	0.0	0.0	0.0
Net cash flow	8.3	(26.9)	9.6	2.0	1.6
Overdrafts / borrowings	(3.5)	(28.0)	(19.0)	(15.5)	(15.0)
Cash & equivalents	6.2	3.9	4.5	3.0	4.0
Net (Debt)/Cash	2.7	(24.2)	(14.5)	(12.5)	(11.0)
NAV AND RETURNS					
Net asset value	34.3	38.0	37.2	36.7	37.1
NAV/share (p)	163.8	181.5	177.5	174.9	176.9
Net Tangible Asset Value	23.9	18.2	15.2	13.2	12.7
NTAV/share (p)	114.2	87.0	72.4	63.0	60.8
Average equity	28.0	36.2	37.6	37.8	39.3
Post-tax ROE (%)	17.9%	(1.1%)	3.8%	7.2%	0.0%
METRICS					
Revenue growth		(6.2%)	3.0%	6.0%	8.0%
Adj EBITDA growth		(43.3%)	(34.3%)	35.1%	20.1%
Adj EBIT growth		(60.3%)	(78.4%)	123.2%	43.9%
Adj PBT growth		(65.8%)	(108.1%)	(449.3%)	91.4%
Adj EPS growth		(71.1%)	(117.3%)	(263.0%)	91.4%
Dividend growth		N/A	N/A	N/A	N/A
Adj EBIT margins		4.2%	0.9%	1.8%	2.4%
VALUATION					
EV/Sales (x)	0.2	0.2	0.2	0.2	0.2
EV/EBITDA (x)	1.8	3.2	4.9	3.6	3.0
EV/NOPAT (x)	2.7	7.9	17.1	16.4	11.4
PER (x)	1.7	5.9	N/A	21.0	11.0
Dividend yield	N/A	N/A	N/A	N/A	N/A
FCF yield	45.6%	(65.5%)	54.0%	16.9%	14.6%

Source: Company information and Progressive Equity Research estimates

Disclaimers and Disclosures

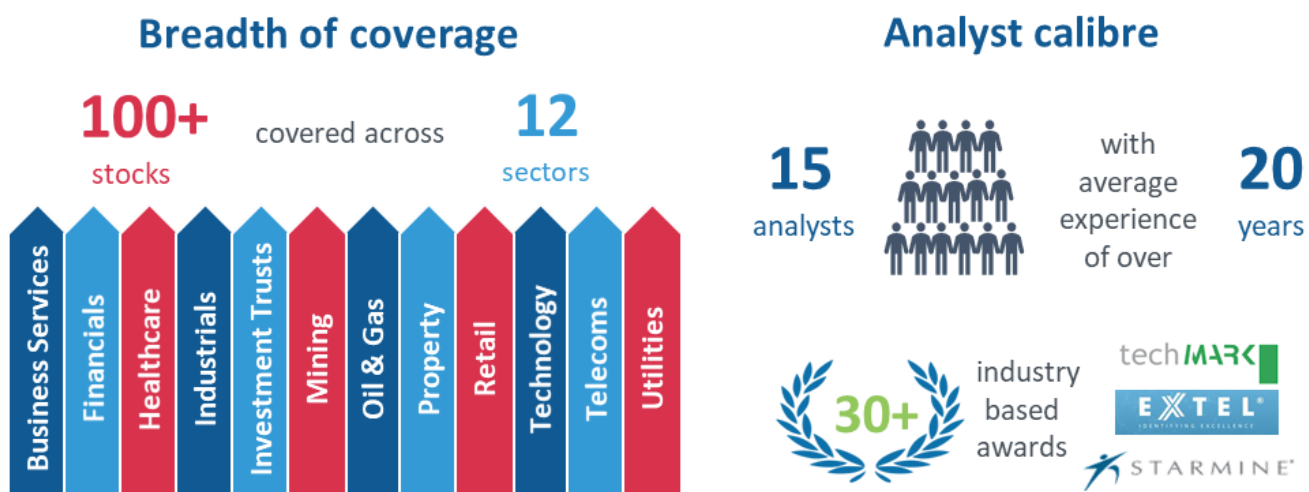
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