Time Finance plc

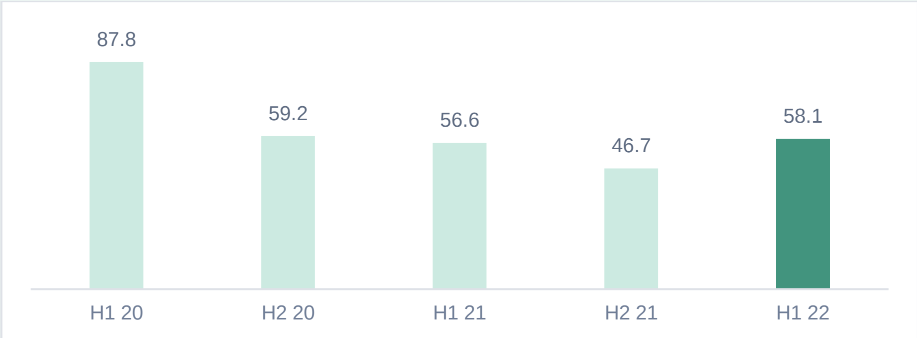
Early strategic progress not reflected in valuation

20 January 2022

H1 22 results (to 30 Nov 21) show steady progress on key metrics, with signs that Time's refined strategy under the leadership of CEO Ed Rimmer (appointed 1 Jun 21) is resulting in a return to growth, following the Covid-induced pullbacks in lending markets in 2020 and 2021.

£58.1m of new loans were originated in H1 22, up 25% over H2 21 (£46.7m), and 3% y-o-y (H1 21 £56.6). The gross loan book increased 4% from £115.7m on 31 May 21 to £120.5m.

Loan originations start recovering from pandemic pullbacks, £m



Source: Company reports, ED analysis

Revenue was flat y-o-y (£11.8m v £11.9m in H1 21), with Profit Before Tax slightly down at £1.20m vs £1.35m. However, the H1 21 figures benefitted from £0.17m of non-recurring furlough income, therefore PBT would be 1% up y-o-y if this is excluded.

Time's balance sheet remained strong, with Net Tangible Assets increasing from £28.4m on 31 May 21 to £29.6m, and it maintained a healthy cash and equivalents position of £9.6m.

In our view, Time Finance remains deeply undervalued

Our fundamental value**,** based on Time meeting its longer-term strategic objectives, **is 45p per share**, not far from double the current share price. In addition, Time's price-to-book ratio is **0.41** compared to a peer median of **1.41**; its market cap of £23.3m represents a **20% discount to Net Tangible Assets**; and its **PER of 12.7** (and forward PER of 11.0) is undemanding.

Key Financials

Year end 31 May	FY 20A	*H1 21A*	FY 21A	*H1 22A*	FY 22E	FY 23E
Loan originations, £m	147	*57*	103	*58*	118	143
Gross lending book*, £m	123	*122*	116	*121*	129	155
Revenue, £m	29.2	*11.9*	24.2	*11.8*	24.8	29.6
Admin exp, £m	12.8	*5.8*	11.5	*6.2*	12.9	14.5
Bad debt provisions,£m	5.1	*5.1*	5.1	*N/A*	5.2	4.9
PBTE**, £m	3.0	*1.6*	3.1	*1.3*	2.7	4.3
EPS basic, p	1.8	*1.2*	2.0	*1.1*	2.3	3.5
Price Earnings Ratio	14.4	*10.4*	12.7	*11.8*	11.0	7.3
Price to Book Ratio	0.42	*0.41*	0.41	*0.40*	0.39	0.37
Net tangible assets***, £m	26.5	*27.8*	28.4	*29.6*	30.5	33.6
Net assets, £m	55.2	*56.6*	57.1	*58.2*	59.2	62.3

Source: Company Historic Data, ED estimates. PER and PBT based on share price of: ***25.25p***
**incl. unearned interest, ** profit before tax, exceptional items & share-based pmnts ***excl. goodwill*

Company Data

EPIC	TIME
Price (last close)	25.25p
52 weeks Hi/Lo	32p / 20p
Market cap	£23.3m
Net Tangible Assets	£29.6m
Avg. daily volume	107k
ED Fair Value / share	45p

Share Price, p

Source: ADVFN

Description

Time Finance, established in 1998, is a non-bank lender and broker. It has four operating divisions:

Asset finance: for SMEs to purchase hard and soft assets;

Invoice finance: for SMEs to borrow against debtors books;

Loans: commercial and SME loans;

Brokerage: for SMEs and consumers to purchase commercial or private vehicles, and consumer property loans.

Most asset, invoice, and SME loans are written to 'own-book'. Consumer and vehicle loans are 'broked-on'.

Next Event:

FY22 trading update, 21 Jun 22

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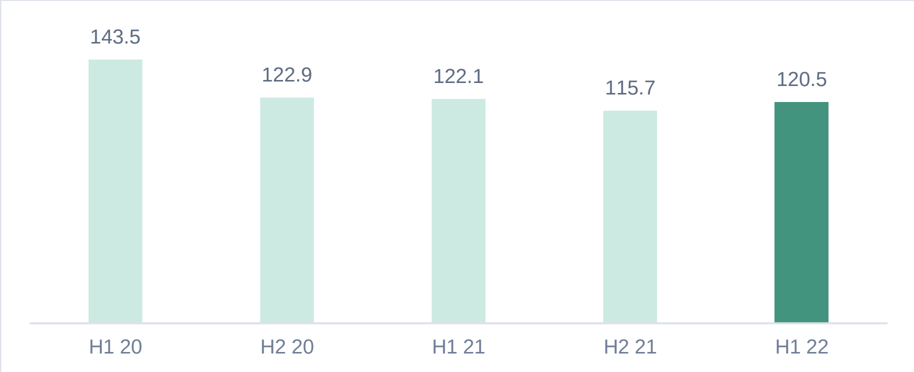
H1 22 Results

Loan book returns to growth

The growth in originations to £58.1m in H1 has also resulted in a return to growth of the overall loan book, which increased to £120.5m on 30 Nov 21 (£115.7m on 31 May 21).

Gross loan book, £m



Source: Company reports, ED analysis
Values show size of loan gross loan book at the end of each period

Comparable revenue & profits up

While accounting revenue and gross profit in H1 22 were largely flat y-o-y (revenue £11.8m in H1 22 vs £11.9m in H1 21; gross profit £7.6m vs £7.5m), profit before tax was down slightly (£1.2m H1 22 vs £1.35m in H1 21). Government grants (furlough payments), which Time no longer has access to, skew prior period results upwards and should probably be excluded from like-for-like comparisons to obtain the most direct comparisons between current and prior periods.

If government grants are excluded from comparisons, Time's H1 22 gross profit and PBT are slightly up on a y-o-y comparison and substantially up when compared to H2 21 (the 6m period immediately prior to these results).

Summary Income statement comparison, excluding furlough pmts, £m

	H1 22 6m to 30/11/21	H2 21 6m to 31/5/21	H1 21 6m to 30/11/20
Revenue	11.8 (-3%*)	12.1	11.7
Gross Profit**	7.6 (+8%*)	7.0	7.4
Gross Margin	64%	58%	63%
Profit Before Tax	1.2 (+200%*)	0.4	1.2

Source: Company
**percentages show comparison between 6m to 30/11/21 (H1 22) and 6m to 31/5/21 (H2 21)*
***Gross Profit = profit after net credit loss charges, funding facility interest charges and introducer commissions*
Note: H2 21 and H1 21 each exclude approximately £200k of government grants (furlough payments)

Basic EPS was 1.07p for the HY (H1 21: 1.21p) and diluted EPS 0.99p (H1 21: 0.99p).

It is also worth highlighting some observations from two other key cost lines in the income statement: bad debts and administrative expenses.

While Time does not disclose details of bad debt provisions in its interim results (increases or decreases in bad debt provisions and net write offs are included in the cost-of-sales line), **signs are encouraging that bad debt provisions have reduced and that the loan repayment environment is improving**:

- gross profit and gross margin have increased from the prior 6m period, likely to be explained in part by a reduction in bad debt provisions;
- deals in forbearance have dropped from £0.8m on 31 May 21 to zero on £30 Nov 21;
- deals in arrears have dropped from 14% of gross loan book to 9%; and
- net write offs have remained static at 2% of gross loan book.

Administrative expenses grew 7% y-o-y from £5.8m in H1 21 to £6.2m in H1 22. However, as flagged in in our 21 Sep 21 note, management had identified an **opportunity to recruit additional experienced and skilled sales staff in the latter half of 2021 (as a result of other lenders contracting), who would help drive the reinvigorated organic growth strategy**, and as such, we expect admin expenses to increase in H2 as the full-period employment costs of these new hires will be accounted for.

Balance sheet and cash position strong

The balance sheet remained strong, with Net Assets increasing over the 6m period from £57.1m (on 31 May 21) to £58.2m (on 30 Nov 21). Net Tangible Assets increased from £28.4m to £29.6m.

Time maintains a healthy cash position with £5.9m of cash (31 May 21: £8.0m) but its cash, cash equivalents and convertible 'paper' stood at £9.6m.

Divisional performance

Invoice financing remained the strongest performing division during the pandemic, generating £3.8m of revenue in H1 22 (14% up y-o-y), and £1.8m of profit before tax (+29%).

The asset finance and broking divisions experienced sluggish activity levels, recording H1 revenues of £5.5m (-12%) and £1.6m (-6%) respectively (both impacted by disruptions to the supply of equipment and vehicles), while the loan division (SME loans, including CBILS and its 'successor', the Recovery Loan Scheme or 'RLS') grew revenue sharply (+51%) off a small base to £0.96m.

Summary divisional Income statements, £'000s

	Asset	Invoice	Loans	Brokerage	Other*	TOTAL
6m to 30 Nov 21						
Revenue	5,520	3,772	964	1,562	-	**11,782**
Profit Before Tax	934	1,767	244	(122)	(1,622)	**1,201**
6m to 30 Nov 20						
Revenue	6,250	3,380	640	1,651	10	**11,863**
Profit Before Tax	1,463	1,374	60	(75)	(1,471)	**1,351**

Source: Company
**Primarily 'central' overhead costs*

Strategy and outlook

We remind readers that in mid-2021, Time announced:

- its primary focus will be on **organic growth** (it previously employed a 'buy and build' strategy);
- priority will be placed on **growing 'own-book'** business-to-business offerings of asset, loan and invoice finance, while maintaining its broking activities to provide flexibility;
- an ambition to **double its gross lending book to around £250m over four years**.
- to **exceed pre-Covid levels of revenue (>£30m) and PBTE (~£8m)** over the same period;

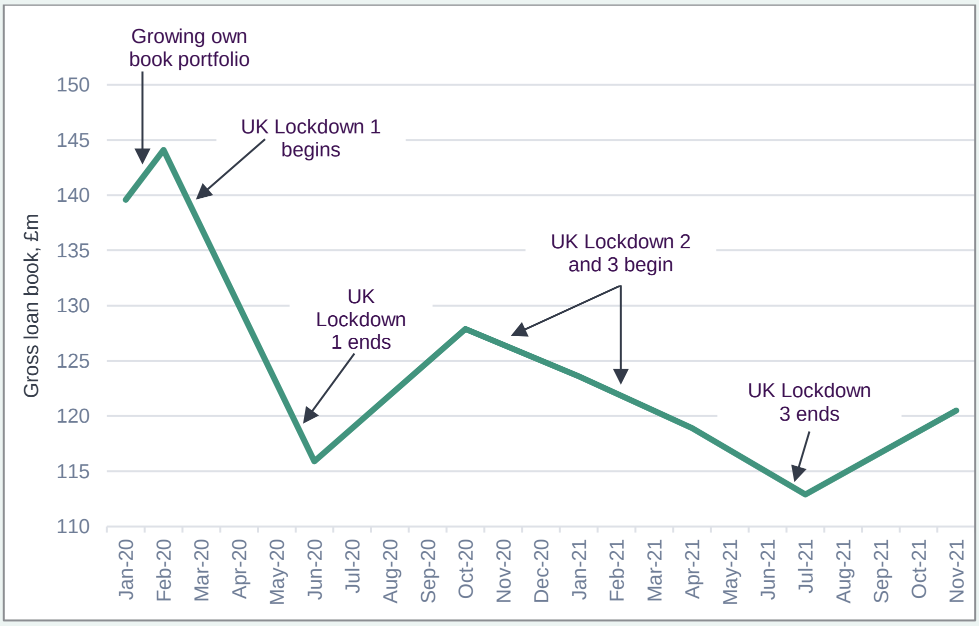
The logic of prioritising own-book lending over broking is that the lending book is a key driver of revenue and profit growth over the medium term (loans originated today will still produce income in future years, according to the duration of the loan).

While Time's brokerage business can deliver short term revenue and profits, these tend to be far more volatile as they are almost wholly dependent on fee and commission income linked to origination levels.

If we were to describe where Time is postioned on this new strategic journey, we would say that its latest results indicate that it is in the **early stages of a return to growth**. Over the last few years, its core markets have been heavily impacted by Covid lockdowns, and to illustrate this point, Time has produced a chart (below) which shows how rapidly its business has been negatively impacted by lockdowns, and how rapidly it starts to recover (although the recoveries have not been as rapid as the declines).

The chart plots the size of its loan book over time, but contains data points at key lockdown and end-of-lockdown dates (which do not match financial reporting periods, hence the nuance of these 'lockdown impacts' are not fully captured by half-year financial reporting intervals).

The impact of lockdowns on Time's gross lending book



Source: Company

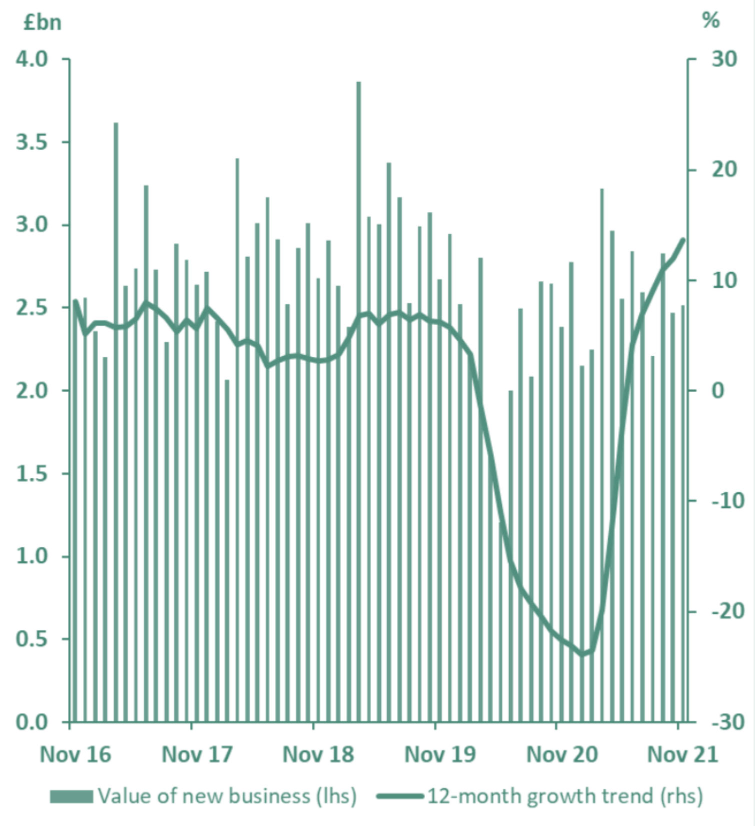
With the UK steering clear of lockdowns in reaction to the Omicron Covid wave (and in particular, England's 'light touch' restrictions appearing to be relatively successful), the chances of further lockdowns appear to have reduced significantly, and **we are relatively bullish that Time's growth trajectory can continue**.

In support of this view, macro-economic and asset finance outlooks are also relatively optimistic.

GDP growth forecasts for the UK in 2022 are robust, with an average forecast of 4.7% (HM Treasury, Forecasts for the UK economy: a comparison of independent forecasts, Dec 21).

In terms of **asset finance**, Time's largest market, the latest figures released by the Finance & Leasing Association (FLA) show that in the eleven months to November 2021, total asset finance new business was 16% higher than in the same period in 2020, and that the **recovery is continuing**. It did however flag that the growth trend was inconsistent within asset fiannce - plant and machinery finance and commercial vehicle finance were relatively buoyant, while business equipment finance and IT equipment finance were weak (with equipment shortages cited as a key as a key reason for this).

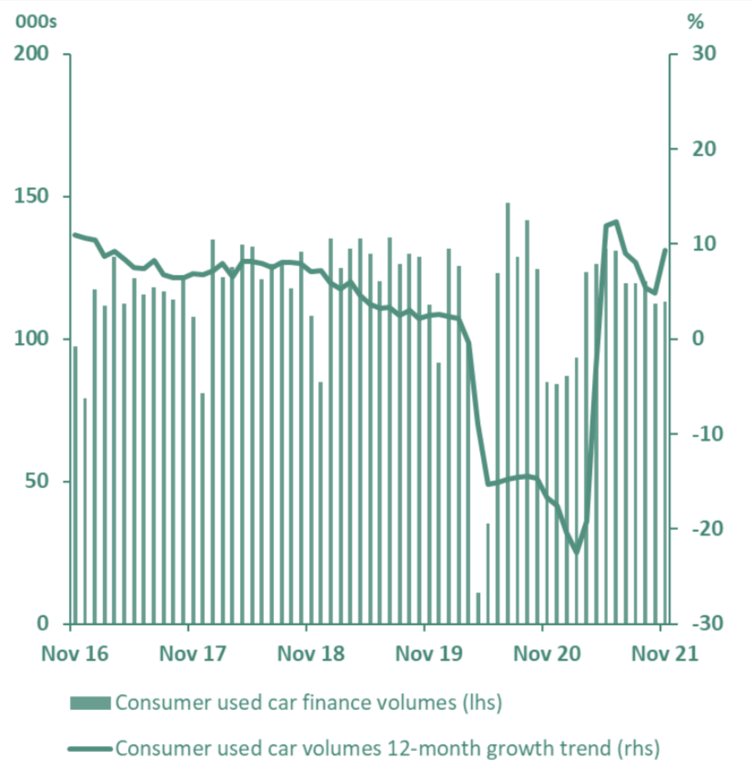
FLA asset finance new business trends



Source: Finance and Leasing Association (FLA)

In terms of **used car finance**, Time's largest broking market, the FLA has flagged ongoing supply side shortages and the 'increasing squeeze on household disposable incomes from higher inflation and interest rates' as inhibitors to growth, with current new business volumes being around 12% less than at the onset of the pandemic.

FLA consumer used car finance new business trends



Source: Finance and Leasing Association (FLA)

Other factors which indicate that Time is well postioned to continue its recovery include:

- its **accreditation from the British Business Bank to provide the Recovery Loan Scheme** ("RLS") to SMEs;
- a **new three-year, £50m Invoice Finance funding facility** being agreed at improved terms, which will support Time's strongest growing division;
- **significant recent investments in sales and marketing staff** which should translate to an uptick in new business in the coming months; and
- a **strong cash position** which can be deployed to pursue growth opportunities.

Valuation

We have considered Time's valuation from a number of perspectives, and in our opinion **we believe Time remains deeply undervalued:**

1. Fundamental valuation:

Our fundamental valuation is based on a successful execution of Time's growth strategy, i.e. doubling its gross lending book to around £250m over four years and exceeding pre-Covid levels of revenue (~£30m) and PBTE (~£8m) over the same period..

We have then applied the following valuation methodology:

- forecasting the future minimum Net Tangible Asset requirements based on the target loan book growth profile (above) and Time's debt covenant requirements to support that growth [Time's funders require maximum gearing ratio of 6X NTA – we assume that Time maintains a gearing ratio of around 5X NTA];
- forecasting actual NTA levels based on the current NTA level and adding forecast net income;
- calculating the difference between actual NTA and minimum NTA to give a 'free cash flow' available to equity holders (which could also be thought of as surplus capital);
- calculating a terminal value following year five, assuming 2.5% growth in perpetuity;
- discounting the above free cash flows at the cost of equity which we have calculated to be 11.5%, based on a risk-free rate of 1.2%, an equity market risk premium of 5.75%, and a beta of 2.2.

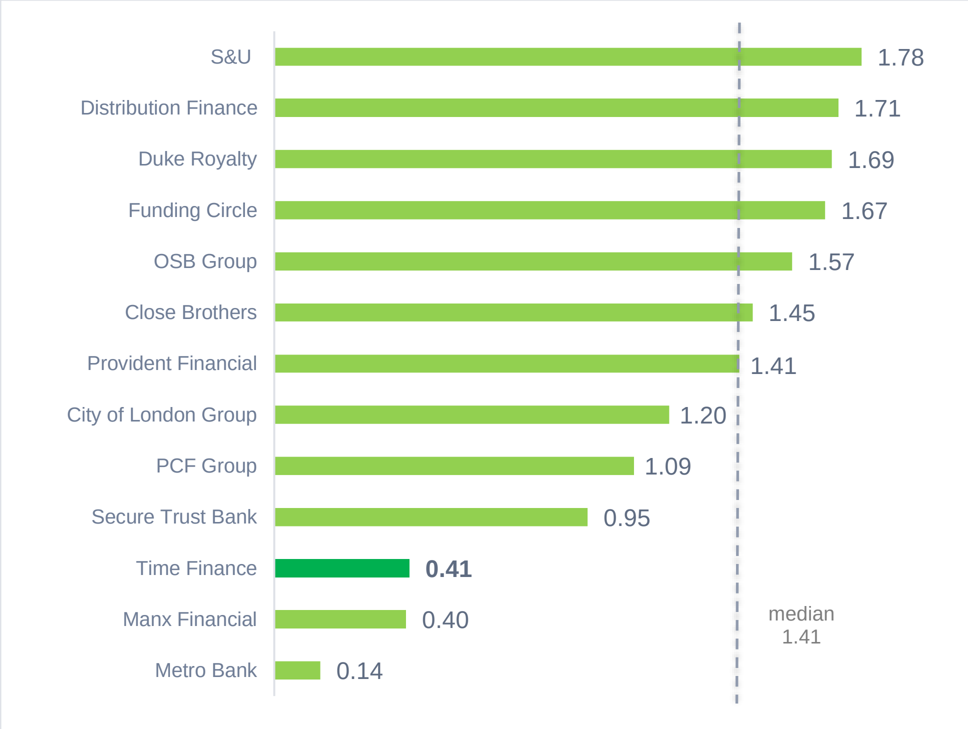
This methodology produces a per share fundamental value of 45p, just under double the current share price of 25.25p.

2. Peer Comparison: price-to book

Price-to-book ratios are also a commonly used metric to value lenders. The group Time is compared to all have parts of their businesses that overlap with Time's activities, and while there are limitations in terms of direct comparisons (the comparator group is a mix of bank and non-bank lenders, has a range of market capitalisations, and differing year-ends making Covid-impact comparisons difficult) the analysis does produce some telling insights.

Most notably, the median price-to-book ratio of the peer group of lenders is 1.41, more than 3 times the 0.41 of Time, which supports the conclusion from our fundamental valuation.

Peer Comparison: price-to-book ratios



Source: ADFVN, ED analysis, as at 18 Jan 2022

3. Other valuation benchmarks

A price-earnings ratio comparison is not particulary meaningful at the moment, as many peers are making losses due to pandemic-related write-downs and falls in business volumes, and different reporting periods skew PE ratios because of the timing of these write-downs and falls.

However, it is worth noting that Time's historic **PER of 12.7** (and forward PER of 11.0) is undemanding, given its ongoing recovery prospects and its future growth prospects.

Lastly, it is also worth highlighting that Time's market cap of £23.3m represents a **20% discount to Net Tangible Assets**,

As all of these valuation methodologies point to a significant undervaluation of Time Finance. If progress towards its new strategic objectives remains on track, we see scope for a significant rerating.

Appendix: Historical and Forecast Financials

Consolidated Income Statement + Forecasts						
12 m to end May, £'000s	**FY20A**	**H1 21 A**	**FY21A**	**H1 22 A**	**FY22E**	**FY23E**
Revenue	29,062	11,698	23,799	11,774	24,769	29,593
Other income	182	165	425	8	-	-
Total Revenue	**29,244**	**11,863**	**24,224**	**11,782**	**24,769**	**29,593**
Cost of sales	(13,319)	(4,315)	(9,362)	(4,196)	(8,889)	(10,485)
Gross Profit	**15,925**	**7,548**	**14,862**	**7,586**	**15,880**	**19,108**
Administrative expenses	(12,793)	(5,794)	(11,475)	(6,210)	(12,934)	(14,465)
Exceptional items	(909)	(224)	(843)	(47)	(100)	(279)
Share-based payments	(31)	-	(277)	(33)	(66)	(150)
Operating profit	**2,192**	**1,530**	**2,267**	**1,296**	**2,780**	**4,215**
Finance costs	(181)	(179)	(250)	(95)	(200)	(350)
Finance income	9	-	3	-	3	4
Profit before tax	**2,020**	**1,351**	**2,020**	**1,201**	**2,583**	**3,868**
Income tax	(465)	(257)	(243)	(228)	(491)	(735)
Profit after tax	**1,555**	**1,094**	**1,777**	**973**	**2,093**	**3,133**
PBTE: Adjusted earnings before interest, tax, exceptional items and share-based payments						
Statutory PBT	**2,020**	**1,351**	**2,020**	**1,201**	**2,583**	**3,868**
Add back:						
Exceptional items	(909)	(224)	(843)	(47)	(100)	(279)
Share-based payments	(31)	-	(277)	(33)	(66)	(150)
PBTE	**2,960**	**1,575**	**3,140**	**1,281**	**2,749**	**4,297**

Source: Group report & accounts and ED estimates

Consolidated Balance Sheet + Forecasts						
As at 31 May, £'000s	FY20A	H1 21A	FY21A	H1 22A	FY22E	FY23E
Assets						
Non current assets	**77,063**	**80,006**	**74,633**	**73,471**	**79,440**	**89,510**
Goodwill	28,241	28,241	28,241	28,241	28,241	28,241
Intangible assets	526	507	476	358	476	476
Property, plant and equipment	767	570	551	839	551	551
Right of use property, plant & equip.	428	338	224	137	27	830
Trade and other receivables	46,157	49,397	44,335	43,012	49,339	58,606
Deferred tax	944	953	806	884	806	806
Current assets	**61,527**	**60,267**	**63,155**	**68,557**	**69,230**	**80,078**
Inventories	-	-	-	-	-	-
Trade and other receivables	60,038	57,182	55,073	62,492	62,580	76,479
Tax receivable	185	-	113	160	113	113
Cash and cash equivalents	1,304	3,085	7,969	5,905	6,538	3,485
Total assets	**138,590**	**140,273**	**137,788**	**142,028**	**148,670**	**169,587**
Liabilities						
non-current liabilities	**28,877**	**24,808**	**37,162**	**36,200**	**40,177**	**46,890**
Trade and other payables	28,639	24,657	33,749	33,320	37,505	44,460
Financial liabiities - borrowings	-	-	3,369	2,877	2,734	2,099
Provisions	-	-	-	-	-	-
Lease liability	238	151	44	3	(63)	331
current liabilities	**54,490**	**58,907**	**43,507**	**47,662**	**49,282**	**60,352**
Trade and other payables	51,052	54,202	41,692	45,615	47,326	57,758
Financial liabiities - borrowings	2,407	4,343	1,634	1,500	1,634	1,634
Tax payable	287	176	-	-	248	492
Provisions	546	-	-	-	-	-
Lease liability	198	186	181	126	75	468
Total liabilities	**83,367**	**83,715**	**80,669**	**83,862**	**89,459**	**107,242**
Equity						
Called up share capital	8,899	9,037	9,252	9,252	9,252	9,252
Share premium	25,360	25,543	25,543	25,543	25,543	25,543
Employee shares	-	-	63	96	63	63
Treasury shares	(310)	(390)	(790)	(749)	(790)	(790)
Retained earnings	21,274	22,368	23,051	24,024	25,144	28,277
Total equity	**55,223**	**56,558**	**57,119**	**58,166**	**59,212**	**62,345**
Total equity and liabilities	**138,590**	**140,273**	**137,788**	**142,028**	**148,670**	**169,587**

Consolidated Statement of Cash Flows + Forecasts						
12 months to end May, £'000s	**FY20A**	**H1 21 A**	**FY21A**	**H1 22 A**	**FY22E**	**FY23E**
Cash generated from operations						
Profit before tax	2,020	1,351	2,020	1,201	2,583	3,868
Depreciation & amortisation	883	380	754	203	951	951
Finance costs	181	179	165	95	200	350
Finance income	(9)	-	(3)	-	(3)	(4)
(Gain) on disposal of property plant & equip.	-	-	-	-	-	-
Decr./(incr.) in inventory	-	-	-	-	-	-
Decr./(incr.) in trade & other receivables	18,947	(384)	6,787	(6,095)	(12,511)	(23,166)
(Decr.)/incr. in trade & other payables	(17,677)	(833)	(4,248)	3,495	9,390	17,387
Movement in other non-cash items	612	933	745	(374)	-	-
Cash flows from operating activities						
Interest paid	(181)	(179)	(165)	(95)	(200)	(350)
Tax paid	(1,488)	(368)	(397)	(258)	(243)	(491)
Tax received	-	-	-	-	-	-
Net cash flows from / (used in) operations	**3,288**	**1,079**	**5,658**	**(1,828)**	**167**	**(1,454)**
Investing activities						
Acquisition of subsidiaries	(500)	-	-	-	-	-
Purchase of software, property, plant & equip.	(375)	(119)	(314)	(45)	(754)	(754)
Proceeds from sale of fixed assets	-	-	-	-	-	-
Contingent consideration paid	(565)	(197)	(197)	-	-	-
Interest received	9	-	3	-	3	4
Net cash flows from / (used in) invest. activit	**(1,431)**	**(316)**	**(508)**	**(45)**	**(751)**	**(750)**
Financing activities						
Payment of lease liabilities	(218)	(107)	(213)	(103)	(213)	(213)
Loan repayments in the year	(991)	(435)	(635)	(323)	(635)	(635)
Loans issued in the year	-	3,100	4,100	-	-	-
Purchase of own shares in EBT	-	(80)	-	-	-	-
Proceeds from issue of share capital	-	-	-	-	-	-
Transactions costs related to share issue	-	-	-	-	-	-
Change in overdrafts (Invoice Finance)	(349)	(729)	(869)	118	-	-
Dividends paid to equity holders	(498)	-	-	-	-	-
Net cash flows from / (used in) fin. activities	**(2,056)**	**1,750**	**2,383**	**(308)**	**(848)**	**(848)**
	-	-	-	-	-	-
Net incr. / (Decr.) in cash and equivalents	**(199)**	**2,513**	**7,533**	**(2,181)**	**(1,431)**	**(3,052)**
Cash and cash equivalents brought forward	331	132	132	7,665	7,665	6,234
Cash and cash equivalents carried forward	**132**	**2,645**	**7,665**	**5,484**	**6,234**	**3,181**

Source: Group report & accounts and ED estimates

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