Company Note

Finals

4 March 2021

Corporate

Current price	**101.5p**
Sector	**General Retailers**
Code	**FRAN.L**
AIM	**AIM**

Share Performance

	1m	3m	12m
FRAN.L	-4%	-1%	-16%

Source: Thomson Reuters, Allenby Capital

Share Data		
Market Cap (£m)		**97.2**
Shares in issue (m)		**95.8**
52 weeks	High	Low
	151.5p	**83.5p**
Financial year end		**December**

Source: Company Data, Allenby Capital

Key Shareholders	
Nigel Wray (NED)	23.36%
Stephen Hemsley (Exec. Chair)	23.14%
Cannacord Genuity	7.03%
Slater Investments	6.27%
Gresham House AM	5.69%
David Poutney (NED)	3.81%

Source: Company Data, Allenby Capital

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Equity Research

Franchise Brands plc (FRAN.L)

Resilient 2020 & new ambitious growth strategy

Franchise Brands' results for the full year can be characterised as resilience in adversity with adjusted EBITDA, profit before tax, EPS, dividend and net cash all comfortably ahead of forecasts, the latter boosted by a placing in 2020 raising £13.6m net. Faced by COVID restrictions, quick reactions by management resulted in a decline in B2B and B2C EBITDA of just 0.7%, against a fall in fee income of 15% while direct labour income increased by 71% reflecting a full year from Willow Pumps. Having achieved a CAGR in adjusted EBITDA and dividends of 47% and 59% respectively since listing, the Board has now set out a new growth strategy which seeks a run-rate in revenues of £100m and adjusted EBITDA of £15m by the end of 2023. Earnings enhancing acquisitions and a better outcome from existing activities, points to the prospect of another strong year ahead.

- **Results ahead of our forecasts** – Like for like revenue declined by 8% to £36.9m but overall Group sales, including a full year of Willow Pumps, increased by 12% to £49.3m. Both adjusted EBITDA (£6.6m) and adjusted profit before tax (£4.8m) were higher than forecast by 5% and 8% respectively. EPS, after a slightly higher than anticipated tax charge, came in at 4.35p against our forecast of 4.03p and a final dividend of 0.8p has been proposed compared to our forecast of 0.65p making a total of 1.1p for the year (+16%). Adjusted net cash at the year-end stood at £6.7m, again higher than our estimate of £4.7m and boosted by the successful fund raise in 2020.
- **System sales were resilient across the year** – System sales from Metro Rod and Metro Plumb fell by just 2% over the year but disguised a COVID-related volatility in demand which saw a 19% increase in Q1 followed by a decrease of 23% in Q2 and a gradual recovery from then onwards with Q4 achieving a 4% yoy rise. Despite the difficulties, 11 franchisees achieved yoy growth of over 10% with 17 achieving sales of over £1m.
- **B2C more severely impacted by Q2 lockdown** – While the most of the B2B businesses were considered essential services and continued to trade, the B2C division consisting of ChipsAway, Ovenclean and Barking Mad, were all effectively closed for business through the Spring lockdown but have since shown good recovery albeit the smallest business, Barking Mad is still being impacted by restrictions on travel.
- **Willow Pumps now fully integrated** – Willow Pumps, which was consolidated for a full year against just three months of 2019, saw revenues decline by 23% although the decline in gross profit was limited to just 4% due to a change in the business mix. The business has now been fully integrated into the Group.
- **Another year of strong growth in prospect** – The Group has made a good start to 2021 and the Board's confidence in the future has prompted us to raise FY2021 EBITDA and EPS forecasts modestly to £7.9m and 5.1p respectively against earlier expectations of £7.75m and 4.8p. We have also included FY2022 forecast for the first time which sees EBITDA rise by a further 18% over FY2021 and EPS by 23%.

Year End: December

£m	2019A	2020A	2021E	2022E
ADJUSTED EBITDA	5.2	6.6	7.9	9.3
ADJUSTED PBT	4.1	4.8	6.1	7.4
ADJUSTED EPS (p)	4.34	4.35	5.13	6.33
DIVIDEND (p)	0.95	1.10	1.40	1.80
ADJ NET (DEBT)/CASH	-9.2	6.5	9.1	13.0
PER (x)	23.4	23.3	19.8	16.0

Source: Franchise Brands plc, Allenby Capital. Allenby Capital acts as Nomad and joint broker to Franchise Brands plc

Please refer to the last page of this communication for all required disclosures and risk warnings.

Operational Review

B2B division

Water in. Waste out

The B2B division comprises the franchise operations of Metro Rod and Metro Plumb, together with the Direct Labour Organisations (DLOs) activities of Willow Pumps and Metro Rod/Plumb corporate franchises, providing a "Water In. Waste Out" range of national drainage, plumbing and pumps services.

Most businesses classed as essential services

The majority of activities in this division were designated by the government as essential services to ensure the smooth running of the health service, public utilities and other key businesses during the lockdown. As most of the work is reactive, there has been continuing demand, and the businesses have continued to operate effectively, albeit at considerably lower volumes.

Metro Rod and Metro Plumb

c.60 territories run by 42 franchisees

Metro Rod is a leading provider of commercial drain clearance and maintenance services delivered on a largely reactive basis. These services are provided from around 60 territories by 42 franchisees with geographical coverage across the whole of the UK. The business was acquired by Franchise Brands in April 2017.

33 franchisees at Metro Plumb

Metro Plumb, part of the original Metro Rod Group, was established in 2016 and is a national cold-water plumbing business serviced through a network of 33 franchisees. 25 of these are run by Metro Rod franchisees, 5 are independent territories and three are operated corporately by Kemac.

System sales recover strongly in Q4 with 5% yoy increase after a COVID-impacted 29% decline in Q2

Both Metro Rod and Metro Plumb started the year strongly with system sales[1] in Q1 up by 19% yoy. However, in Q2 the first national lockdown restricted business activity to the servicing of critical establishments such as hospitals and supermarkets. Consequently, system sales in Q2 reported a decline of 29% against the comparative period. Thereafter, activity levels gradually improved resulting in system sales being just 5% lower yoy in Q3 and 5% higher yoy in Q4.

EXHIBIT 1: B2B QUARTERLY SYSTEM SALES YOY % CHANGES

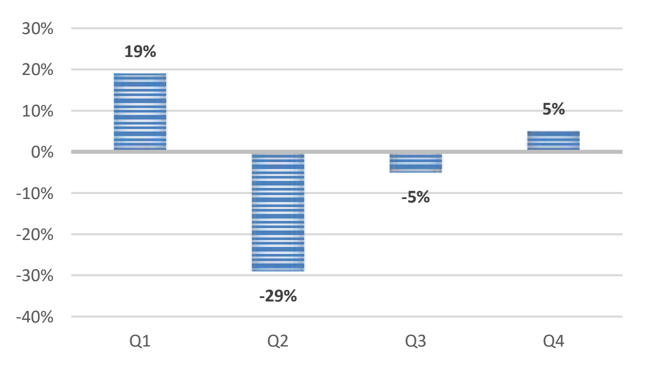
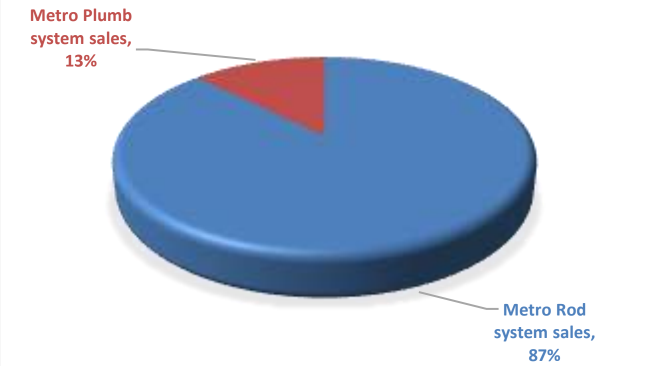


EXHIBIT 2: CONTRIBUTION TO SYSTEM SALES BY BUSINESS



Source: Franchise Brands

Overall, system sales declined by just 1.6% to £40.6m with Metro Rod sales down by around 2.3% at £35.5m and Metro Plumb up 3% at just over £5m.

[1] System sales are gross sales made by Metro Rod and Metro Plumb franchisees before the deduction of management service fees.

A surprisingly robust system sales outcome

In our opinion, system sales were surprisingly robust given the potential for business disruption and much of this resilience was due to the continued support of franchisees from the Support Centre staff where previous investment in cloud-based IT systems and the automation of repetitive labour-intensive processes allowed staff to work from home very effectively.

No franchisee failures over the lockdown period

Over the difficult COVID-impacted months the Group provided advice to franchisees to prepare them for the anticipated downturn in business activity and assistance where necessary to help cashflow. Most importantly, there were no franchisee failures and most of the assistance provided by the Centre has funded expansion of their businesses, for example, helping purchase new equipment.

Indeed, management makes the point that as a result of extensive scenario planning it had anticipated a potential decline in sales of up to 40% and had prepared cost-saving initiatives to mitigate this, the objective being to continue to provide effective services to customers whilst maintaining an element of profitability and positive cashflow. In the event the downturn was not as steep as feared, a fact which together with the lower overhead resulted in stronger than expected profitability.

11 franchisees achieve yoy system sales growth of over 10%

This support and guidance given to franchisees, in part, resulted in 11 of the 43 Metro Rod franchisees achieving yoy growth in system sales of over 10% and 17 franchisees achieving sales of over £1m.

Responsibility for some territories transferred to Willow Pumps…

Since 2019, the Group had operated two Metro Rod territories as DLOs but following the acquisition of Willow Pumps (a Kent based company), responsibility for the Kent & Sussex and Exeter territories was transferred to the Willow Pumps field service team, both to improve the local management of the business and give Willow Pumps direct hands-on experience of a Metro Rod territory.

…with great success

The transfer of the business has been very effective and resulted in a significant increase in both turnover and profitability and it is now the intention to expand this operation and to establish a joint Metro Rod/Willow Pumps depot in the South West.

Prior to the effects of the pandemic the Group commenced a process to develop Metro Plumb as a separate franchise rather than an add-on to the larger Metro Rod franchise. Some initial success was achieved with two new franchisees being signed up during 2020.

Management is now beginning to recruit more independent franchisees while at the same time offering any Metro Rod franchisee the opportunity to exit the Metro Plumb business and to sell it to new franchisees. This should result in a new cadre of entrepreneurial franchisees who are dedicated to building their business and with the aid of the Group's Central Support functions, offer a broader range of plumbing services.

While COVID temporarily slowed down this initiative, management has confirmed that the Group intends to focus significant additional sales, marketing and recruitment resources on developing the Metro Plumb franchise in the coming year.

Willow Pumps

First full year contribution from Willow Pumps

Willow Pumps, a leading pump supply, installation and servicing business with an above and below-ground capability, was acquired in October 2019 and has thus contributed its first full year as a Group subsidiary company.

Strong start to 2020 but impacted by COVID in Q2

As with Metro Rod, activity levels in Q1 were strong showing yoy sales growth of 15%. At the start of the Spring lockdown, Willow Pumps management took swift action to reduce costs and right-size the business resulting in 36% of the staff being furloughed. Two of its key customer segments were the hotel and construction industries and although these were effectively closed during lockdown, activities including pump service and repair work for essential service providers such as supermarkets remained resilient. As a result, the amount of lower volume/higher margin supply and installation (S&I) work began to diminish and led to more reliance on higher margin but lower volume emergency pump work.

Revenue fell by 56% yoy in Q2 leading to sales for the year falling by 23% although the gross profit decline was only 4%

Consequently, revenue declined in Q2 by 56% yoy although gross margins only declined by 37% due to changes in the business mix. This remained the case in H2 and although S&I work recovered, volumes were lower and routine service and emergency work predominated. Consequently, sales for the full year were 23% lower yoy although gross profit was much more robust showing a reduction of just 4% due to the business mix.

Operating as a DLO rather than a franchise business, Willow Pumps offers the Metro Rod franchisees an opportunity to enlarge the scope of the services offered to their commercial customers by including the capability to add pump supply and servicing to their existing draining expertise. A number of Metro Rod engineers have since been trained in the basic skills required to work safely on pump maintenance and the resumption of this training, effectively halted during lockdown, is likely to resume in the current year.

B2C Division

B2C brands formed into an integrated division during 2019

The B2C division comprises ChipsAway, Ovenclean and Barking Mad. To facilitate future acquisitions and improve operational efficiency, they were formed into an integrated division of the Group during 2019. Thus, the division is now set up to be able to facilitate the addition of complimentary new B2C brands through acquisition where a meaningful element of the overhead can be absorbed by the Group’s central support function.

Businesses effectively shut down for periods of 2020 due to the pandemic…

Whereas significant elements of the B2B division were able to continue trading to varying degrees throughout the lockdown period, the B2C division was heavily impacted with no trading being undertaken during the period from end March to the end of June.

…leading to fee and recruitment income falling by 14%

Thus, for the year to December 2020, fee and recruitment income in the B2C division fell by 14% to £5.8m with adjusted EBITDA showing a reduction of 15% to £2.1m. Consequently, around 85% of the team were furloughed in Q2 while franchisee fees and charges, other than those necessary to maintain skeleton operations, were reduced or suspended. Due to the prompt actions taken and despite the significant drop in income, the division traded at breakeven over that period.

Recovery from June onwards with ChipsAway leading the improvement

Following the ending of the Q2 lockdown, the two principal brands, ChipsAway and Ovenclean, began to recover. ChipsAway, which is the largest brand accounting for around 88% of the division’s EBITDA, demonstrated the quickest recovery allowing the franchisees to achieve pre-COVID levels of activity relatively quickly.

Ovenclean also demonstrated a commendable return to earlier activity levels although given the need to enter customer’s homes and the requirement for social distancing the recovery was not quite as rapid as that achieved by ChipsAway. Unfortunately, Barking Mad continued to suffer very low demand as people were unable to take the holidays that would normally generate demand for dog home boarding. This is however a relatively small business in relation to other Group activities.

Strong franchisee recruitment given the difficult circumstances

27 new franchisees (1H 2019: 34) were recruited in the B2C division during the first half with this number rising to 58 for the full year, an excellent performance given the difficult circumstances. 18 of these recruits joined in Q1 and a further 9 in Q2, the reduction being impacted by the lockdown. However, given the trading difficulties experienced by some B2C franchisees, mainly in the Barking Mad network, there has been a reduction in the total number of franchisees in the B2C network at the year-end to 386 from 404 at the end of 2019.

Process and customer interaction automation

New strategy for Metro Rod instigated in 2017…

After being acquired by the Group in 2017 and following a prolonged period of corporate and private equity ownership, the Board concluded that Metro Rod required a new strategy centred on the development of the franchisees as entrepreneurs and the corresponding systems that they needed to grow their businesses.

…to return the franchisees to the centre of the business and help them grow local sales and take more responsibility…

The goal of this new strategic thrust was to return the franchisee to the centre of the business and to help them grow local sales, reduce their reliance on over-complicated manual systems and lessen the intervention from the Support Centre. The strategy necessitated creating new systems and ways of working that passed back to the franchisees greater responsibility for looking after customers and their own businesses.

Encapsulated in "Vision 2023" strategy

This new strategy was originally presented at a conference in November 2017, as a five-year growth plan named "Vision 2023". Implementation of most of the proposed strategic and operational changes commenced in January 2018 and has continued apace over the intervening period culminating in the completion of a new works management system "Vision" which has been rolled out to all Metro Rod and Metro Plumb franchisees during 2020, on time and to budget.

The system has been designed to provide improvements in efficiency and productivity that have begun to benefit the business through the second half of the year and will do so more fully into 2021.

Vision has not only been designed to enhance customer service and thereby increase sales, but also improve corporate and franchisee efficiency and thereby reduce costs. Together, management anticipates that this will allow the Group to grow profits, improve productivity, and maintain competitiveness in an ever more demanding environment.

Management now embarking on a more ambitious 3-year digital transformation of the business…

Now that this initial strategic objective has been attained and the basic infrastructure has been put into place, management is now embarking on a further, more ambitious three-year journey that will eventually see jobs booked on-line, deployed to an engineer, reported to the customer, and billed with the minimum of human intervention. The business will also have the facility to integrate all this information and functionality directly into customers' systems.

…beginning with "Connect"

The first element of these enhancements, a customer portal branded "Connect", has just been launched. This provides customers with near real-time, online visibility of every job, including status, costs, and photographs. Franchise Brands believes that Metro Rod is one of the first drainage company in the UK to offer this functionality to customers.

Increased investment to total £1.5m over the period

This increased investment in the accelerated digital transformation of the business is projected to amount to an additional £1.5m over the next three years and will lead to additional sales, overhead savings and operational efficiencies that will enhance run-rate EBITDA.

Financial review

EXHIBIT 3: SUMMARY FINANCIALS			
	2020	**2019**	***change***
	£000	**£000**	
INCOME STATEMENT			
Statutory revenue	49,287	44,013	*12.0%*
Franchisee payments	-19,898	-19,612	*1.5%*
Fee income	29,389	24,401	*20.4%*
margin	*59.6%*	*55.4%*	*7.6%*
Gross profit	20,925	16,382	*27.7%*
margin as a % of fee income	*71.2%*	*67.1%*	*6.1%*
Adjusted EBITDA	**6,640**	**5,182**	*28.1%*
margin as a % of fee income	*22.6%*	*21.2%*	*6.4%*
Adjusted PBT	**4,836**	**4,069**	*18.8%*
Adjusted EPS (p)	**3.09**	**3.48**	*-11.2%*
Adjusted net cash/(debt)	**6,666**	**-9,180**	
BALANCE SHEET			
Non-current assets	39,198	39,837	*-1.6%*
Current assets (excluding cash)	16,001	17,529	*-8.7%*
Cash	13,203	1,682	*685.0%*
Total current assets	29,204	19,211	*52.0%*
Total assets	**68,402**	**59,048**	*15.8%*
Current liabilities	-14,256	-18,276	*-22.0%*
Non-current liabilities	-10,303	-12,913	*-20.2%*
Total liabilities	**-24,559**	**-31,189**	*-21.3%*
Net current assets	**14,948**	**935**	*1498.7%*
Net assets	**43,843**	**27,859**	*57.4%*
CASH FLOW			
Operating cash flow before working capital movements	6,623	5,182	*27.8%*
Net movement in working capital	-651	-519	*25.4%*
Tax	-745	-147	*406.8%*
Net cash from operating activities	**5,227**	**4,516**	*15.7%*
Net cash used in investing activities	**-811**	**-5,660**	*-85.7%*
Net cash used in financing activities	**7,088**	**-114**	-
Net increase/(decrease) in cash	**11,504**	**-1,258**	-
Cash at start of year	1,682	2,940	*-42.8%*
Cash at end of year	**13,186**	**1,682**	*683.9%*

Source: Franchise Brands

EPS restricted by the increase in the number of shares in issue post the successful placing in 2020

Note. A fuller version of Franchise Brands' financial results is shown on pages 14-16. Growth in EPS was restricted in 2020 due to the increase in the number of shares as a result of the successful placing in 2020. As a result the average number of shares in issue increased by 16%.

A strong start to the year which was then impacted by COVID. Management responded quickly with tight cost controls

The year was characterised by a very strong first quarter followed by the reduction in activity caused by the COVID-19 lockdown. Tight cost controls were initiated which reduced the impact at the bottom line. Costs were strictly controlled through use of the furlough scheme which was utilised for 118 of the Group's 290 employees allowing the

Group to trade profitably through the impacted period. In June, the number of staff furloughed reduced to 89 and all staff were reinstated by the end of August.

Focus is on fee income – as a franchise business, revenue is not a KPI

As a predominantly franchise business, the Group's headline focus is on fee income rather than revenue, as the latter reflects the level of system sales relating to the individual brands as well as revenue from the DLOs. Fee income (excluding payments to franchisees) and DLO income are analysed as follows.

EXHIBIT 4: FEE AND DIRECT LABOUR INCOME

	2020 £000	*as a % of total*	*% change*	2019 £000	*as a % of total*
Management service fee income	10,694	*36.4%*	*-4.6%*	11,207	*45.9%*
Area sales	1,607	*5.5%*	*-19.9%*	2,006	*8.2%*
Product sales	758	*2.6%*	*-16.9%*	912	*3.7%*
Direct labour income	15,547	*52.9%*	*70.9%*	9,097	*37.3%*
National advertising funds	783	*2.7%*	*-33.6%*	1,179	*4.8%*
Total fee and direct labour income	29,389	*100.0%*	*20.4%*	24,401	*100.0%*

Source: Franchise Brands

Management Service Fee (MSF)

Income derived from the MSF is generated either from fixed monthly fees charged to the franchisees or from income based on a percentage of their sales.

MSF declined by 5% yoy due to COVID

Over the financial year, the Group continued to incentivise Metro Rod's management franchisees to grow their businesses through a series of MSF discounts and schemes designed to encourage sales growth and investment in a broader range of equipment and people. In the B2C division, fixed monthly fees continued to be the most effective method of generating income given the large number of franchisees and the lower level of individual sales. Overall, the MSF declined by 5% to £10.7m.

Area sales

Area sales down 20% yoy

Represents income from the sale of new franchise areas or a percentage of the resale value of existing areas to new franchisees. Fees generated in 2020 from the sale (or resale) of franchise territories were 20% lower than in 2019. Management believes that in the circumstances, franchise recruitment in the B2C division was robust, with 58 recruits in 2020 (2019: 61). Most of the reduction in recruitment income resulted from fewer Metro Rod franchises changing hands which generated income of £73,000 compared to £328,000 in the prior year. Area sales for the year were down 20% at £1.6m.

Product sales – Income derived from the sale to franchisees of products supplied to them from the Group's Central Support function.

DLO income up 71% due to Willow Pumps being in for a full year

Direct Labour Organisations – Income generated from DLOs within the Group, (i.e. non-franchise operations) namely Willow Pumps and the Metro Rod/Metro Plumb corporate franchises. The increase in 2020 over 2019 reflects the fact that Willow Pumps was consolidated for a full year rather than the 3 months of contribution in the comparative period. DLO income was up 71% to £15.5m as a result of Willow Pumps being consolidated for a full year.

National Advertising Funds

Income generated through deductions from franchisees to fund and support national and regional brand advertising. These funds are used exclusively to promote the system sales of those brands and the Group does not generate any profit from these activities.

EXHIBIT 5: ANALYSIS OF ADJUSTED EBITDA

	2020	2019	%
	£000	£000	*change*
B2B - Franchisor	3,722	3,184	*16.9%*
B2B - DLO	1,844	492	*274.8%*
B2C Division	2,132	2,531	*-15.8%*
Group overheads	-1,058	-1,026	*3.1%*
Total adjusted EBITDA	**6,640**	**5,182**	*28.1%*

Source: Franchise Brands

Adjusted EBITDA ahead by 28%

Adjusted EBITDA (stated before share-based payments and exceptional items) grew by 28% yoy, the growth attained by virtue of the inclusion of a full year contribution from Willow Pumps and strong control of overheads. The B2B activities relate to a) Franchisor - being Metro Rod and Metro Plumb and b) DLO - being Willow Pumps and corporate-run franchise territories. The B2C division consists of ChipsAway, Ovenclean and Barking Mad.

Tight cost controls instigated at the start of the pandemic, some of which have resulted in permanent cost savings

Tight cost controls throughout the year resulted in adjusted EBITDA at B2B-Franchisor rising by 17% to £3.7m. This represented an increase in operating margin from 26% to 36%. Management makes the important point that as the business returned to pre-COVID levels, it was cautious in re-introducing costs and have therefore realised permanent cost savings through new ways of working.

As noted earlier in this report, initiatives taken towards the end of 2019 to further develop Metro Plumb as a separate franchise has also started well and helped to grow EBITDA in the business alongside growth in system sales.

While the B2B - DLO EBITDA rose as a consequence of the inclusion of Willow Pumps for a full 12 months there was an additional contribution from Willow Pumps from its assumption of day-to-day responsibility for the two Metro Rod franchise territories of Kent & Sussex and Exeter which reacted positively under the new management team following poor performances in 2019. We note that the Metro Plumb corporate franchises also did well under a new management team.

B2C impacted badly during Q2 but have since recovered strongly and remain cash generative

With regards to the B2C division EBITDA slipped by 16% yoy as the impact of the earlier lockdown effectively shut down operations through Q2 before beginning to recover from June 2020 onwards. The division is strongly cash generative and remained so during the year helping to service the Group's debt.

EXHIBIT 6: RECONCILIATION OF ADJUSTED AND STATUTORY FINANCIALS

	2020	2019	*change*
	£m	£m	
Adjusted EBITDA	**6.64**	**5.18**	*28.1%*
D&A	-1.36	-0.76	*79.7%*
Finance	-0.45	-0.36	*24.9%*
Adjusted PBT	**4.84**	**4.07**	*18.8%*
Amortisation of acquired intangibles	-0.39	-0.26	*51.2%*
Share based charges	-0.21	-0.24	*-13.9%*
COVID-19 and other one-off costs	-0.71	-0.27	*161.5%*
Other gains and losses	0.15	-0.00	-
Statutory PBT	**3.68**	**3.28**	*12.5%*

Source: Franchise Brands

COVID-19 charge

COVID-related charge estimate reduced from £1.3m to £0.5m

Given the likely impact of the crisis on certain customers, management believed it prudent to expect that a number would fail as government support schemes began to unwind.

At the time of the Placing in April 2020, management stated that it would take a COVID-19 related charge of £1.3m to provide for these potential credit losses. Since then, a detailed internal analysis of debtors has been undertaken which resulted in a charge of a much lower £0.5m being provided for these potential credit losses. In addition, the Group also took a £0.2m charge in relation to the closure of its Barking Mad office and redundancy costs.

Cash and debt

Placing during 2020 raised a net £13.6m putting the Group in a strong financial position

The placing in 2020 which raised a net £13.6m, had a transformative impact on the Group's balance sheet with all net debt being eliminated and replaced by an adjusted net cash position of £6.7m. The Board took the decision not to repay the Term loan of £5.3m so as to maximise the Group's immediately available liquidity. Cash conversion as a percentage of adjusted EBITDA was 79% (2019: 87%) due to the impact of COVID-19 on the business.

At the year-end cash stood at £13.2m (2019: £1.7m) and undrawn bank facilities of £7.0m giving the Group over £20m of cash and available facilities.

Due to the introduction of IFRS16 the Group has recognised obligations in relation to operating leases. However, it notes that as its banking arrangements determine its interest rate margin and covenant compliance, it uses adjusted net debt as its KPI, as shown in the table below.

EXHIBIT 7: ANALYSIS OF NET CASH/(DEBT)

	2020	**2019**	***change***
	£m	**£m**	
Cash	13.23	1.68	*685.0%*
Term loan	-5.23	-6.40	*-18.4%*
RCF	0.00	-3.00	-
Loan fee	0.10	0.13	*-25.6%*
Hire purchase debt	-1.41	-1.59	*-11.3%*
Adjusted net cash/(debt)	**6.47**	**-9.18**	**-**
Other lease debt	-1.72	-1.89	*-19.9%*
Net cash/(debt)	**4.94**	**-11.08**	-

Source: Franchise Brands

Dividends

FY 2020 Dividend increased to 1.1p and covered 3.9x by adjusted post-tax profit

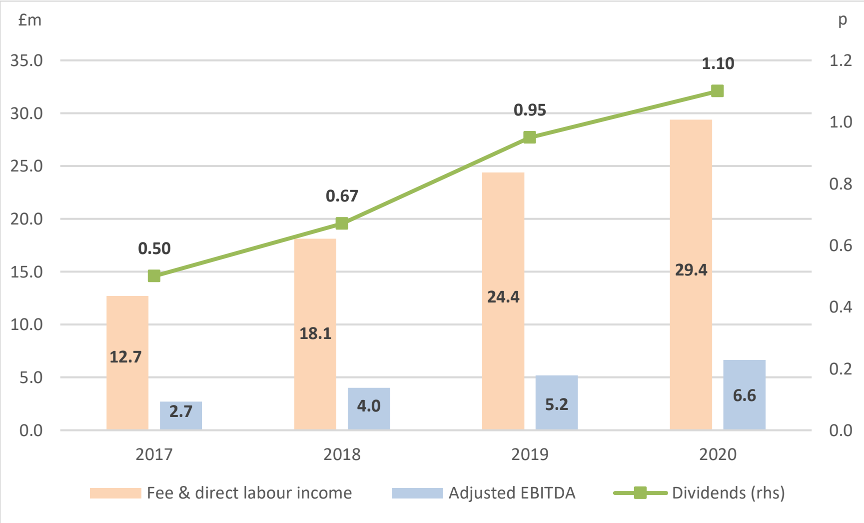
The Board has proposed a final dividend of 0.8p per share which together with the interim dividend of 0.3p per share gives a total dividend for the year of 1.1p (2019: 0.95p) an increase of 16% reflecting the improved H2 trading and strong balance sheet. The cost of the final dividend is covered 2.8 times by statutory profit after tax and 3.9 times by adjusted profit after tax.

New growth strategy targets

Compound growth of 47% in EBITDA and 59% in dividends since admission

Since admission to AIM in 2016 Franchise Brands has delivered strong performance and developed a market-leading portfolio of brands through organic growth and targeted earnings-enhancing acquisitions and have generated compound annual growth in adjusted EBITDA of 47% and a 59% compound annual growth in dividends, as shown in Exhibit 8 below.

EXHIBIT 8: SELECTED GROWTH METRICS SINCE LISTING IN 2016



Source: Franchise Brands

Co-incident with the Franchise Brands' three-year digital transformation objectives (see page 5) that have been designed to reduce to a minimum the requirement for human intervention in back-office processes, is the instigation of a new medium-term growth strategy for the Group.

This has been designed based on the Vision 2023 strategy at Metro Rod and Metro Plumb, the acceleration of design-led supply & installation work at Willow Pumps and growth from earnings-enhancing acquisitions in both the B2B and B2C divisions.

New 3-year strategy to achieve run-rate revenues of £100m and adjusted EBITDA of £15m by end 2023

The Board has therefore set out, for the first time, its strategic financial targets of run-rate revenues of £100m and adjusted EBITDA of £15m by the end of 2023. Based on the results to December 2020, this targeted run-rate if achieved, would result in revenue growth of 103% and 126%.

This target is expected to be partly supported through the increased investment that the Group is making in the accelerated digital transformation of the business which is designed to increase sales, overhead savings and operational efficiencies that will enhance the EBITDA run-rate.

Acquisition strategy

Acquisitions to date:

01/11/16 – Barking Mad – consideration £0.9m

11/4/17 – Metro Rod – consideration £28m

07/10/19 – Willow Pumps – maximum consideration £12.5m

The Board continues to seek earnings-enhancing acquisitions..

The Group has continued to selectively seek earnings-enhancing acquisitions of complementary B2C franchise businesses where it can leverage the existing divisional structure and high-quality shared support services. Having visibility of both franchisees' and franchisors' longer-term viability following the COVID-19 crisis is a key factor and management is understandably taking a cautious approach.

The Board also remains interested in the acquisition of complementary B2B businesses that will assist in expanding the range of services offered by its existing B2B franchisees as well as seeking additional franchise businesses of scale that could create a third division of the Group.

The search has proven to be protracted to date (Willow Pumps was the last acquisition which was concluded in October 2019) but we remain confident that management will continue to take a cautious and considered approach and will not be rushed into an injudicious acquisition that would not fit into the Group's strategic goals.

…which will be largely funded from existing facilities, with the caveat that larger scale franchise businesses may need to be funded through additional shareholder financing but would be additive to the run-rate targets noted above

In addition, the Board is of the view that complementary acquisitions will be largely funded from existing facilities (which, following the successful fund raise in 2020 now amounts to £20m) without the need for additional equity capital other than to incentivise and lock-in the management of acquired businesses.

The caveat is that the Board will continue to evaluate the acquisition of franchise businesses of scale that may require additional shareholder financing but would be additive to the run-rate targets noted above.

Forecasts

Franchise Brands' management team weathered the COVID -storm remarkably well

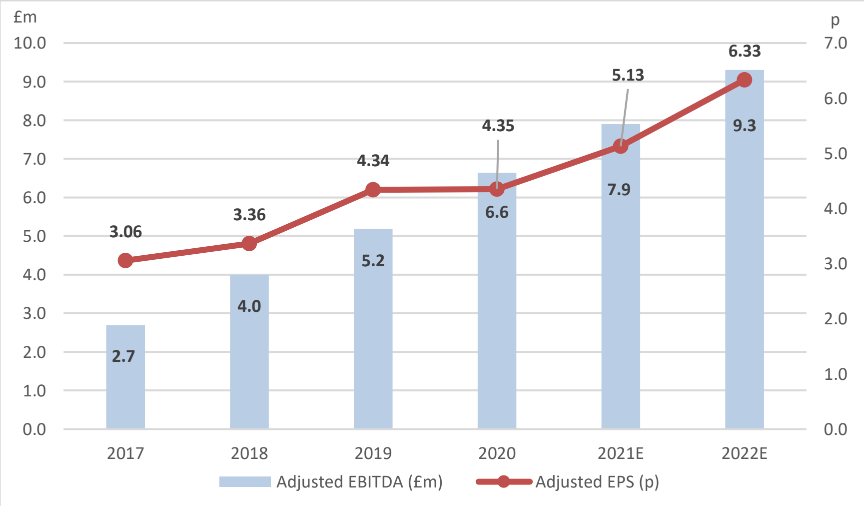
As with many companies, Franchise Brands' results for 2020 were affected by the impact on trading of the COVID-19 pandemic. However, unlike many companies the Group managed to weather the storm remarkably well helped by the fact that many of its businesses were considered essential services and were allowed to continue trading, but also from swift and timely intervention by management to control costs in those parts of the business most impacted by the lockdowns.

[Insert Here] Positive start to the year has prompted us to raise forecasts for FY2021 together with forecasts for FY2022

A positive start to the new financial year has prompted us to raise our forecasts modestly from adjusted EBITDA of £7.75m to £7.9m and adjusted EPS from 4.8p to 5.1p. We have also included, for the first time, forecasts for the year to December 2022. At this stage they assume fee and direct labour come growth (against FY2021E) of 11% to £35.3m, adjusted EBITDA growth of 18% to £9.3m, adjusted profit before tax growth of 22% to £7.4m and adjusted EPS growth of 24% to 6.3p.

We have also assumed a 29% increase in the total dividend to 1.8p which would be covered 3.5x by adjusted earnings after tax. Our forecasts also project an increase in cash to £16.5m from an estimated FY2021 level of £14.4m.

EXHIBIT 9: HISTORIC AND FORECAST ADJSUTED EBITDA AND EPS



Source: Source: Franchise Brands; Allenby Capital

Group remains in good shape to generate strong organic growth and utilise a strengthened balance sheet to help fund acquisitions

We believe the Group remains in good shape to resume strong organic growth and now has the added benefit of a strengthened balance sheet with substantial unutilised facilities to both grow the business internally and to help fund the cost of any future acquisitions.

Conclusion

The Chairman concludes his outlook statement accompanying the full year results with the following observation:

"We have made a strong start to 2021 as a result of resilient sales in the B2B division, robust recruitment in the B2C division and the enduring legacy of some of the cost saving measures implemented at the start of the pandemic. We therefore look forward to 2021 with confidence."

The strength of the balance sheet, with £20m of available financing in the form of cash and unutilised facilities, leaves the Group well placed to take advantage of opportunities to grow the business organically and through earnings enhancing acquisitions in the post-pandemic recovery.

The shares are currently trading at 101.5p, still a third below their February 2020 peak of 151.5p and are selling on a forward PER of 19.8x earnings, falling to 16x for 2022, offering good value in a fast growing and dynamic company with quality management and a track record of delivering strong earnings growth. This later has of course been recently emphasised by the Board's end-2023 target of achieving a run-rate in revenue of £100m and adjusted EBITDA of £15m.

An exceptionally well run and well managed business positioned to deliver strong growth for the foreseeable future

Franchise Brands is an exceptionally well run and well managed business with an experienced Board and operational management team that is positioned to continue to deliver strong revenue growth, cash generation and earnings for the foreseeable future. In consequence we believe the shares will deliver above average capital growth for its stakeholders.

Income Statement & Forecasts

EXHIBIT 10: INCOME STATEMENT

	£m	£m	£m	£m
Y/E December	**2019A**	**2020**	**2021E**	**2022E**
ADJUSTED				
Revenue	44.0	49.3	57.2	62.0
Franchisee payments	-19.6	-19.9	-25.8	-26.8
Fee and direct labour income	24.4	29.4	31.8	35.3
Fee income margin	*55.4%*	*59.6%*	*55.6%*	*56.9%*
Other cost of sales	-8.0	-8.5	-8.9	-10.2
Gross profit	**16.4**	**20.9**	**23.0**	**25.1**
Gross profit margin	*37.2%*	*42.5%*	*40.1%*	*40.4%*
Administrative expense before D&A, share based charges and exceptional items	-11.2	-14.3	-15.1	-15.8
as a % of revenue	*25.4%*	*29.0%*	*26.3%*	*25.4%*
Adjusted EBITDA	**5.2**	**6.6**	**7.9**	**9.3**
margin	*11.8%*	*13.5%*	*13.8%*	*15.0%*
Depreciation	-0.6	-1.1	-1.4	-1.5
Amortisation of software	-0.1	-0.2	-0.2	-0.2
Adjusted operating profit	**4.4**	**5.3**	**6.4**	**7.7**
Operating margin	18.1%	18.0%	20.0%	21.8%
Finance expense	-0.4	-0.4	-0.3	-0.3
Adjusted profit before tax	**4.1**	**4.8**	**6.1**	**7.4**
Tax	-0.7	-0.9	-1.2	-1.3
Tax rate	*16.9%*	*18.6%*	*19.0%*	*17.9%*
Adjusted post tax profit	**3.4**	**3.9**	**4.9**	**6.1**
STATUTORY				
Adjusted operating profit	4.4	5.3	6.4	7.7
Share based charges	-0.2	-0.2	-0.2	-0.3
Acquisition of acquired intangibles	-0.3	-0.4	-0.4	-0.4
Cost of acquisition	-0.3	-0.7	0.0	0.0
Exceptional items	0.0	0.2	-0.1	0.0
Statutory operating profit	**3.6**	**4.1**	**5.7**	**7.0**
Operating margin	14.9%	14.0%	17.9%	19.9%
Finance expense	-0.4	-0.4	-0.3	-0.3
Statutory profit before tax	**3.3**	**3.7**	**5.4**	**6.7**
Tax	-0.6	-0.9	-1.2	-1.3
Tax rate	*17.3%*	*24.1%*	*21.3%*	*19.6%*
Statutory post tax profit	**2.7**	**2.8**	**4.2**	**5.4**
Shares				
Basic, weighted average (m)	77.948	90.463	95.758	95.758
Diluted, weighted average (m)	79.139	92.112	97.407	97.407
Shares in issue at year end (m)	79.314	95.758	95.758	95.758
EPS				
Basic adjusted (p)	**4.34**	**4.35**	**5.13**	**6.33**
Basic statutory (p)	3.48	3.09	4.43	5.65
Dividend				
Interim (p)	0.30	0.30	0.46	0.60
Final (p)	0.65	0.80	0.94	1.20
Total dividend per share (p)	**0.95**	**1.10**	**1.40**	**1.80**

Source: Franchise Brands; Allenby Capital

Balance Sheet & Forecasts

EXHIBIT 11: BALANCE SHEET

	£m	£m	£m	£m
Y/E December	**2019A**	**2020A**	**2021E**	**2022E**
Assets				
Non-current assets				
Intangible assets	35.1	34.8	34.4	34.1
Property, Plant & Equipment	1.2	1.3	1.5	1.7
Right-of-use assets	3.5	3.2	2.0	0.8
Total non-current assets	**39.8**	**39.2**	**37.9**	**36.6**
Current assets				
Inventories	0.6	0.7	0.7	0.7
Trade and other receivables	16.9	15.3	16.9	20.1
Cash and Cash equivalents	1.7	13.2	14.1	15.9
Total current assets	**19.2**	**29.2**	**31.7**	**36.7**
Total Assets	**59.0**	**68.4**	**69.6**	**73.3**
Liabilities				
Current liabilities				
Trade and other payables	-12.7	-10.8	-12.3	-13.2
Loans and borrowings	-4.1	-2.1	0.0	0.0
Obligations under finance leases	-0.9	-1.0	-0.9	-0.9
Current tax liability	-0.6	-0.4	-0.9	-0.9
Total current liabilities	**-18.3**	**-14.5**	**-14.1**	**-15.1**
Non-current liabilities				
Loans and borrowings	-5.2	-3.0	-2.5	-0.3
Obligations under finance leases	-2.6	-2.1	-3.1	-3.1
Contingent consideration	-3.6	-3.5	-3.2	-2.9
Deferred tax liability	-1.5	-1.8	-1.2	-1.2
Total non-current liabilities	**-12.9**	**-10.3**	**-10.0**	**-7.5**
Total liabilities	**-31.2**	**-24.8**	**-24.1**	**-22.5**
Net current assets	**0.9**	**14.7**	**17.6**	**21.6**
Net Assets	**27.9**	**43.6**	**45.5**	**50.8**

BALANCE SHEET RATIOS

	£m	£m	£m	£m
Y/E December	**2019A**	**2020A**	**2021E**	**2022E**
Long-term financial (debts) including IFRS 16 leases	-7.8	-5.1	-5.6	-3.4
Short term financial (debts) including IFRS 16 leases	-5.0	-3.2	-0.9	-0.9
Gross (debt) including IFRS16 leases	-12.8	-8.3	-6.6	-4.4
Cash and cash equivalents	1.7	13.2	14.1	15.9
Net (debt)/cash including IFRS16 leases	**-11.1**	**4.9**	**7.6**	**11.5**
Other lease debt	1.9	1.5	1.5	1.5
Adjusted net debt	**-9.2**	**6.5**	**9.1**	**13.0**
Acid test (Current Assets - inventory / Current Liabilities)	1.0	2.0	2.2	2.4

Source: Franchise Brands; Allenby Capital

Cash Flow & Forecasts

EXHIBIT 12: CASH FLOW

	£m	£m	£m	£m
Y/E December	**2019A**	**2020**	**2021E**	**2022E**
Operating cash flow:				
Post tax profit after exceptional costs	2.7	2.8	4.2	5.4
Depreciation	0.6	1.1	1.5	1.5
Amortisation	0.1	0.2	0.2	0.2
Amortisation of acquired intangibles	0.3	0.4	0.4	0.4
Acquisition related costs	0.3	0.7	0.0	0.0
Finance expense	0.4	0.4	0.3	0.3
Other	0.0	-0.2	0.0	0.0
Income tax expense	0.6	0.9	1.2	1.3
Share Based charges	0.2	0.2	0.2	0.3
Operating cash flow before changes in working capital & provisions	**5.2**	**6.6**	**8.0**	**9.2**
Decrease/(increase) in inventories	*0.0*	*0.0*	*0.0*	*0.0*
Decrease/(increase) in trade receivables	*-1.5*	*0.9*	*-1.6*	*-3.2*
Increase (decrease) in trade and other payables	*1.0*	*-1.5*	*1.5*	*1.0*
Net movement in working capital	***-0.5***	***-0.7***	***-0.1***	***-2.2***
Net cash inflow/(outflow) from operating activities	4.7	6.0	7.8	7.0
Income tax paid	-0.1	-0.7	-1.2	-1.2
Net cash (outflow)/inflow from operating activities	**4.5**	**5.2**	**6.6**	**5.8**
Investing Activities:				
Purchase of intangible assets	-0.8	-0.3	-0.3	-0.3
Purchase of property, plant and equipment	-0.9	-0.5	-0.5	-0.5
Acquisition of subsidiary	-4.0	0.0	-0.3	-0.3
Net cash inflow/(outflow) from investing activities	**-5.7**	**-0.8**	**-1.1**	**-1.1**
Financing Activities:				
New term loan	4.0	0.0	0.0	0.0
Repayment of term loan	-2.5	-4.2	-2.2	-2.2
Other loans made	-0.0	-0.2	0.0	0.0
Interest charges	-0.4	-0.4	-0.5	-0.1
Receipts from share issue net of costs	0.4	13.7	0.0	0.0
Purchase of treasury shares	-0.3	0.0	-0.3	-0.3
Dividend payments	-0.6	-0.5	-1.3	0.0
Funds supplied to EBT	0.0	-0.2	0.0	0.0
Capital element of finance lease repaid	-0.7	-1.1	-0.5	-0.5
Net cash inflow/(outflow) from financing activities	**-0.1**	**7.1**	**-4.7**	**-3.0**
Total net increase/(decrease) in cash and cash equivalents	**-1.3**	**11.5**	**0.9**	**1.7**
Cash and cash equivalents at start of period	2.9	1.7	13.2	14.1
Cash and cash equivalents at end of period	**1.7**	**13.2**	**14.1**	**15.9**

Source: Franchise Brands; Allenby Capital

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