

# Support Services

## Trading Comments - HYDG

### **HYDROGEN GROUP+** (HYDG, House Stock, 66.5p) FY Results, Growth, Cash, Dividends...

**FY2018A, an excellent performance.** The recruitment specialist has issued positive FY results this morning, confirming the detailed guidance given in the trading update for the year ending December 2018 on 25 January. The highlights of the results are a strong performance across the group's operating territories (with that in the USA particularly notable, in our view), a strong cash performance (with further acquisitions now actively being considered to leverage growth), and a strong operating model in evidence incentivising staff to build and progress operations – delivering momentum across the group's vertical market exposures. The results have come in a little ahead of our January 2019 upgraded expectations overall, we retain our current forecast stance for the current year at the operating level noting a good start to the first half period; our EPS does rise a little, however, reflecting lower tax guidance at this stage.

**Results.** Group revenues grew by 8% to £135.7m with Net Fee Income (NFI) at £30.5m as anticipated up 34% over the year. This performance reflected the FY2017 acquisition of Argyll Scott, but also a pro-forma improvement of 14% - we believe very pleasing in the context of the operating environment. EBITA at £2.5m compares to £0.4m for FY2017A, reflecting the material improvement in profit conversion, reflecting positive operating leverage. Adjusted PBT at c£3.0m was as forecast, up from £0.9m in FY2017A. Adjusted EPS, reflecting a lower tax rate on our adjusted diluted basis grew from 3.2p to 7.4p (+123%). The underlying EPS pre-dilution and minorities from the operating model is at 8.0p. The cash performance was equally robust with operating cash flow up to £6.1m against £2.5m in FY2007A. This saw a net debt position of £0.4m become a net cash position of £4.9m at the end of December 2018 – this after dividend payments of £0.4m and share purchases of £0.2m. The FY dividend rises to 1.5p (our forecast 1.3p) against the 0.8p for FY2017A.

**A strong operating model.** Hydrogen incentivises its teams to seek out niche growth opportunities across its regions and vertical markets, categorising these as being in an 'incubator' stage, 'fast growth' or a 'market leading business'. The success of the model through FY2018A is reflected in promoting a total of 20 business teams from the incubator stage to fast growth and from fast growth to market leading status. Discipline in capital and HR resource allocation is evident in the closure of 11 incubator teams, moving this resource to alternate areas. Hydrogen is currently operating c70 niche teams in the group.

Looking to the regional performances, the UK continues to dominate EMEA, here NFI grew by 7% to £17.6m, a creditable performance in our view, with a strong legal practice notable in particular. APAC saw sustained strong growth with the benefits of the FY2017A acquisition of Argyll Scott clearly visible. On a proforma basis, NFI here grew by 15% (+17% on a constant currency basis) to £11.0m and

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was broad based . In the USA, albeit from a low base, NFI grew to £1.9m, by 118% on a constant currency basis, accelerating as the year progressed and building a strong foundation for further progress in FY2019F. starting with an office in Houston in early 2018, offices were opened in Austin and in San Diego; a further office has opened in 2019 in Charlotte.

**Outlook.** Hydrogen is increasingly well positioned to deliver sustained growth, in our view, delivering upon its strategic objectives. Indeed, we note that many of the FY2020F targets set out in FY2016A, including growth in NFI by 10%+ p.a., with PBT to NFI conversion of over 10% and targeting EPS of in excess of 6.8p, have already now been exceeded. The current year appears to us to have started strongly and we retain our January 2019 upgraded forecasts, with EPS trending a little higher on lower tax assumptions (EPS of 7.5p goes to 7.8p, now growing by c11% over FY2018A). Hydrogen does highlight the potential challenge from current Brexit uncertainty upon its clients, but also identifies potential opportunities. Clearly the much improved balance sheet underpins prospects for potential enhancement from acquisitions, as well as supporting organic opportunities.

**Valuation thoughts.** We continue to see potential for forecast upgrades as the year progresses, from both the operating environment and acquisitions delivering positive leverage. The group trades on a FY2019F PER of 8.5x (EV/EBITDA 4.4x) falling in FY2020F to a PER of 7.8x (EV/EBITDA3.6x) generating a free cash flow yield in FY2019F of c11.2% with a dividend yield of 2.5%. Pre-acquisitions we expect the cash position to continue to grow post a 10% increase in the dividend this year – to £6.1m. We conclude that Hydrogen is well positioned to make further progress therefore.

HOUSE STOCK.

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