Scale research report - Update

Edel

Media

8 July 2020

Mixed media markets

Edel's H120 figures showed a 3% uplift in revenues versus H119, but at a slightly lower gross margin reflecting the shift in mix. Kontor New Media is benefiting from the continued growth of streaming and the book and vinyl markets have continued to perform well. However, sales of CDs, DVDs and Blu-ray are still under pressure, exacerbated by the closure of physical retail outlets due to COVID-19. The shares trade at a discount to global entertainment content and publishing stocks on historical EV/EBITDA and EV/sales multiples, in part due to limited liquidity.

Continued shift to digital, rights ownership

Edel is exhibiting some resilience in the face of difficult markets, having invested both in its digital media offering, Kontor New Media, and in the physical production and distribution facilities of optimal media. Fees and licensing costs increased by 21% versus H119 (Kontor acts as an aggregator between rights owners and platform providers). However, a swift move to a shorter working week and cost control measures gave a degree of protection to H120 EBIT margins, which decreased from 5.5% in H119 to 5.0%. As anticipated, capital spend was markedly less in the period at €2.7m from €6.6m in H119. The pandemic may have increased the group's opportunities to extend its physical business, particularly in book publishing and through developing non-traditional routes to market. It is also looking to increase its owned-rights library, particularly in music, film and TV.

Outlook complicated by COVID-19

FY20 guidance was for sales to be 'slightly lower' than in 2019, with net income at around the FY19 level of €2.2m. There is no specific update with the half-year figures, but the degree of uncertainty is greater, given the impact of COVID-19 on consumer spending and choices and the closure of physical retail outlets. This may affect the group more in H2 if utilisation dips at optimal media and/or if pricing comes under pressure. Management has drawn down additional lines of debt to give it flexibility, with net debt at the half year stage of €52.7m, from €51.9m at end FY19. The report also refers to potential tax liabilities that may arise from the application of trade taxes on additional licences and from the treatment of revenues derived from pursuing those that have illegally abused rights.

Valuation: Discount to content, publishing

We have maintained the same valuation approach as previously, comparing Edel's rating with the global media subsectors of entertainment content and publishing. The shares trade at a significant discount on EV/sales, most likely reflecting the manufacturing element. Uncertainty regarding the potential tax liabilities may also be acting as a drag on the share price. While the lower EPS has lifted the P/E multiple to around the level of peers, the discount on historical EV/EBITDA is 39%.

Key financials

Year end	Revenue (€m)	PBT (€m)	Adjusted EPS (€)	DPS (€)	P/E (x)	Yield (%)
09/18	209.2	6.6	0.16	0.10	10.5	6.0
09/19	209.5	4.4	0.08	0.10	21.0	6.0

Source: Edel accounts

Price	€1.68
Market cap	€38m

Share price graph

Share details

Code	EDL
Listing	Deutsche Börse Scale
Shares in issue	22.73m
Last reported net debt at 31 March 2020	€52.74m

Business description

Edel is one of Europe's leading independent media groups. It is both a publisher and a producer. Edel offers the music, film and book industries a unique full-service model, covering marketing and production as well as the distribution of audio content, video content and books.

Bull

- Diversity of revenue streams.
- Full-service, third-party offering.
- Resurgence of vinyl.

Bear

- Difficult CD, DVD and Blu-ray markets.
- Small free float.
- Spotify's dominance in streaming.

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Edison profile page

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Financials

The group published its full year report to end September 2019 in February and has now updated on the results for the half-year to end March.

Exhibit 1: Half year to 31 March 2020 vs H119

€000s	H119	H120	%
Year end 30 September	HGB/German GAAP	HGB/German GAAP	change
Income statement			
Revenue	108,074	111,408	3
EBITDA	10,469	10,222	-2
EBITDA margin (%)	9.7	9.2	
Profit before tax (as reported)	4,904	4,590	-6
Net income (as reported), before minority interest	3,211	3,008	-6

Source: Edel accounts

No breakdown of revenue by activity is given at the half year stage, although the management report outlines a continued growth in the digital activities of the group. Sales from optimal media (which prints books, presses vinyl, CDs and DVDs, and packages and distributes for international clients, including Universal Music and Warner Music) were reportedly slightly ahead of the prior year with an improved margin. Books and vinyl (now also including vinyl made from 100% recycled PVC) performed well, but sales of CDs, DVDs and Blu-ray discs continued to decline. Optimal media benefited from a major investment programme in FY17–19 and is now highly efficient. Kontor New Media was the major contributor to the group's growth in the period.

The shift in mix led to a slight dip in group gross margin from 49% to 48%. Personnel costs decreased as a percentage of revenues from 25% in H119 to 22% in H120. With the higher fee and licensing costs, EBITDA decreased by 2%.

The COVID-19 pandemic may continue to have an impact on both sales and profitability in H220, with much depending on the scale and speed of the reopening of the physical retail economy. While the popularity and growth of streaming is positive for Kontor New Media, if lacklustre demand continues for physical product due to restrictions on routes to market, utilisation and efficiency at optimal new media will be compromised. Management has drawn down credit lines to give it the flexibility to react. While period end net debt of €52.7m is little changed from end FY19 figure of €51.9m, Edel now has cash and cash equivalents of €29.8m on the balance sheet, from €9.6m at end September 2019.

Valuation

Our valuation framework for Edel is unchanged from our previous note. Analysis is complicated by the range of Edel's activities, from pressing CDs for third parties through to children's animated TV, to being the market-leading publisher of cookery books and handling logistics and services for the world's largest music publishers. Any peer group comparison is therefore inevitably limited. Given these constraints, rather than selecting a set of inadequate peers, we have looked globally across the main subsectors in which Edel operates, particularly entertainment content and publishing, to examine key valuation metrics based on consensus forecasts. We have stripped out unprofitable companies from our EV/EBITDA and P/E calculations, as well as any obvious distortive outliers.

Exhibit 2: Sectoral valuations for related activities

	P/E (x)			EV/sales (x)			EV/EBITDA (x)		
	Last	FY1	FY2	Last	FY1	FY2	Last	FY1	FY2
Publishing	16.6	16.3	15.0	1.7	1.3	1.1	8.4	7.9	8.1
Broadcast & Entertainment	21.0	21.7	18.0	2.4	2.9	2.3	9.9	14.2	9.9
Edel	20.0	N/A	N/A	0.4	N/A	N/A	5.6	N/A	N/A

Source: Refinitiv Note: Prices as at 3 July 2020.

We would expect that the multiple to sales for Edel would be lower than the comparator groups due to the large volumes of third-party revenues that it handles, which will also distort margin comparisons. The change in the group's legal identity to a partnership limited by shares in March 2019 (deemed more appropriate for the family-based group structure) reduces the potential influence of minority shareholders and so also has valuation implications. The founding family retains a 64% stake.

The reduction in group profitability over recent periods has lifted the historical P/E ratio broadly into line with peers. Nevertheless, Edel's share price appears to be well below the global market on both EV/sales and EV/EBITDA multiples, in part due to its comparatively modest size and limited liquidity, given the family shareholding. At the current price, Edel's historical EV/EBITDA multiple is at a 39% discount to peers.

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