First Artist (FAN.L) - encouraging final results from a year of major transformation.

FAN.L

Comment by Andy Hartwill , Nov 19, 2007

Questions? Contact our analyst

2006/7 was a year of considerable transformation for the group. It's objective was to produce a revenue stream less dependent on the lumpy football business. It succeeded in that pretty much at a stroke with the acquisition of the Dewynter theatre promotion and merchandising business. Other acquisitions made over the course of the year contributed also to the achievement of that ambition.

Group sales hit £48.6m and operating profit £4.9m, pre-central overhead. Dewynter's operations (reported under the Media division) now account for 49% of group operating profit and football is reduced to 21%. The more stable revenue stream from Dewynter has contributed materially to the positive £2.2m swing in operating cashflow from negative £0.5m (in the 10m to August 2006) to £1.7m in the year to August 2007.

Although like-for-like comparisons within the results are compromised by the availability of only 10m data for the prior year, there are signs of divergent margin trends across different operations. Operating margins rose by over 250bp to 9.7% in the Events Division (producing £0.5m operating profit) and the current year should see the further positive impact of the full programme of events deliverable under the recently extended contract with the TDA.

Against that, the larger Entertainment/ Sport division reported operating down from 32% to 20% (producing £2m), largely we believe the result of timing differences in the reporting of the Scandinavian football operations.

Geographically the European operations represented 7% of group sales with margins hit also by Scandinavian football. United States operations were in for the first time (ie, no comparators) following the Dewynter acquisition. The £4.4m reported represented 9% of group total and was achieved despite the 13% depreciation of the US$ against sterling since the Dewynter acquisition. Treasury management limited the impact of that to less than £100k.

Note that the company is expecting to adopt IFRS for the interim results this year and that the £0.5m amortisation charged against last year's P&L is expected then to be reversed.

Objective Capital Limited
11-12 Tokenhouse Yard
London EC2R 7AS
Tel:+44-(0)870-080-2965
Fax: +44-(0)870-116-0839
editor@objectivecapital.com

Corporate: www.ObjectiveCapital.com
Research: www.ObjectiveCapital.co.uk

Objective's View:

Overall the results were broadly in line with our expectations at the level of turnover and operating profit. We expect that 2007/8 will be a year in which organic profit growth will be driven principally by sales growth in low double digits. Operating margins are likely to consolidate around the 10.1% achieved last year with the recognition of full-year management charges in all operations offsetting some of the expected margin enhancements still anticipated in the existing operations.

Operational highlights for the current year are expected to include: •

•

- further expansion of Dewynter's overseas activities, notably on Broadway and, through its tourism operations, in China;
- further Sponsorship Consulting deals, such as that concluded with with Unilever last year, ahead of the 2012 Olympics
- further Rights Management deals such as those over the use of The Simpsons artwork and to the Ocean Racing World Cup;
- the impact of a full schedule of some 500 events as contracted recently with the Training Development Agency. Also a full year from Yell Communications;
- growth in international sports representation – note the recent "placing" of Ruud Gullit as Manager of the LA soccer team Galaxy (of David Beckham fame).

The company is currently developing plans that could result in "own programming" alongside TV production companies and/ or programme commissioners. The plans are part of FAN's strategy to develop further its Entertainment Management operations, capitalising on its track record for developing "personality brands". If achieved it could be the most dramatic and literally visible illustration of the Group's drive for synergy benefits.

Beyond the scope for organic growth FAN sees itself as an "industry consolidator". We expect that any further acquisitions would change the scale but not, we believe, the shape of current operations. FAN is now repositioned around its three core competencies of Media (eg, Dewynter), Entertainment/ Sport and Events and we would expect that any acquisitions would be made so as only to enhance those and intra-group synergies.

The scale of acquisitions is likely to be modest compared to the transformational Dewynter deal. Interest cover in the year just ended was 3.6x and the company has indicated that the ceiling on its comfort zone is somewhere around 3x. Taking that ceiling and using current commercial interest rates, suggests to us a willingness to assume perhaps another £5m of debt towards any acquisition.
With its paper unlikely at recent levels to be used as any significant component, deferred considerations are likely to take up the slack on any larger transactions. At 31st August 2007 FAN had £7.6m in deferred consideration payable over the next five years, £3.4m in the current year.

First Artist Corporation has undergone a dramatic transformation during its last financial year. We expect 2007/8 to be somewhat calmer, reflecting a period of consolidation and the development of synergistic benefits within it's now three-divisional structure. That said, a year potentially of solid growth against a background of expected economic slowdown will be no mean achievement.