THE UK SHAREHOLDERS' ASSOCIATION INVESTIGATES AIM COMPANIES' ANNUAL REPORTS

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Annual Report for year ended 30 June 2016

INTRODUCTION

Redde works predominantly with a wide range of UK insurance companies, insurance brokers, and national vehicle fleet owners, providing a range of accident and incident management services, of which the best known is the supply of hire cars to the non-fault motorist. The Group in its present form arose from Helphire, which ran into financing problems around 2009 due to poor trading and slow payment by at-fault insurers. The Board was rejigged in 2011 and new funding was negotiated in early 2013, so that the Group is now sound and cautiously run.

So far as this commentary is concerned, the only meaningful figures are those for the last 3 years, which show good growth and high rates of cash conversion. For the year under review, revenue was £379m (2015 £249m), with profit before tax of £31.3m (£24.3m). At the year end, cash was £34.6m (£68.6m) after dividend/tax payments of £28.9m and the £41m cash cost of an acquisition.

THE REPORT

Many companies are cutting down on print runs for their accounts because demand is low; this was the case for Redde, but they did manage to find a copy fairly quickly.

The report uses a praiseworthy 72 pages (including covers - unused except for the front), with the Company figures taking up 10 pages. Presentation is clear with black print on semi-glossy white, no photographs, no jargon and no unexplained acronyms.

The report starts with a 2 pages giving the 'Highlights', Key Performance Indicators and a Business profile. The Chairman, Chief Executive (CEO) and Chief Financial Officer (CFO) give factual statements covering the results and strategy with little overlap, so they tell us all we need to know whilst only using just over 10 pages. Risks and Uncertainties are covered comprehensively; for example, despite having all its business in the UK, the Group does recognize the possibility of car price rises for the hire fleet.

One complaint, which applies not just to Redde but to many companies we review, is about the use of 'adjusted' profits; a better word would be 'inflated'. Here, the adjusted pre-tax figure is £34.6m against the final figure of £31.3m. The £3.3m of exceptionals is made up principally of,

- £1.6m amortisation of intangible assets in FMG, the acquiree. There is no justification for this treatment, since the assets are being written off over 5 and 10 years, so this will be a regular cost.
- £0.7m of share based payments. Again, this is a recurring cost.
- £1.0m of acquisition related costs. Debatable.

It is noted that half the executive bonus plan is related to adjusted earnings per share.

THE BUSINESS

The Group's stated strategy is *"…the pursuit of sustainable, profitable, cash generative business and the acquisition of businesses which meet these criteria and will provide cross fertilization….in new markets…."* within the Group's sectors. The Business profile states that *"The Group offers a comprehensive package of motor claims accident services, including vehicle replacement and repair management together with full claims handling assistance as well as legal and other bespoke services…..The Group aims to be the leading outsourcing partner for UK motor insurers…..The Group also provides specialised large fleet accident and incident management through…FMG…"* We are not given a breakdown of the activities but, from clues in the report, a reasonable estimate by revenue (with FMG annualised) would be Hire 45%, Repairs 20%, Legal 10% and FMG 25%. Redde has its own leased fleet of 7,238 vehicles at the yearend (2015, 6,041) and FMG has 300,000 fleet vehicles under management..

ACCOUNTS
Revenue in the year to 30 June 2015 for the Redde business was £249m, and this increased by 28% to £318m in the year under review; FMG (acquired late Oct 2015) added £61m to give a total of £379m. The Gross Profit for the year fell to 25.9% (30.8%), partly as a result of a large increase in lower margin repairs but also because FMG's margin was 22.9%. Earnings per share were down slightly because the Group has now returned to a normal tax charge after being able to use up the Helphire losses; there was also a small dilution due to the FMG acquisition being partly for shares at a market value of £5m. Dividends paid in the year were £28.1m against profit after tax of £25.3m.
The balance sheet shows Total Equity of £160.3m, of which £107.3m is goodwill and intangibles. The vehicle fleet is financed using a mix of operating and finance leases. Vehicles acquired under finance leases are treated as being owned by Redde and are included in fixed assets with the payment obligations in current and non-current liabilities. Depreciation of the 'owned' fleet is subjective, in that it depends on the estimated holding period and residual value on disposal; there was a loss on disposals of £0.7m, but this does not necessarily relate to motor vehicles as there were also disposals of fixtures and equipment.
Payments for vehicles acquired on operating leases came to £11.2m. The notes to the accounts tell us that payments of £6.4m on non-cancellable operating leases were due to end within one year and a further £2m within two years. These figures give an indication of the speed with which the company could reduce its fleet without incurring penalties if business turned down. Fleet utilisation was good at 82.9% (target 80%).
The Redde (as opposed to FMG) properties are leased and no disclosure is made. The Group is considering the effect of IFRS 16, Leased Assets.
Debtors rose from £84.3mm to £126.9m and creditors from £65.0m to £116.2m. Whilst these are large movements, the reasons are explained satisfactorily in over 2 pages of notes. There is a subjective element to trade debtors because of the nature of the claims settlement process and this is explained clearly.
Closing cash was £34.6m (£68.6m) after payments of £41m for FMG and dividends of £28.1m. Total obligations under Finance Leases were £39.9m (£29m) against £41.4m depreciated value.

DIRECTORS, EMPLOYEES & SHAREHOLDERS
There are 5 directors, all elected to sort out the recent trading and financing problems. The Chairman (Avril Palmer-Baunack, £200k pa) was appointed in late 2011 and her two male non-exec colleagues (£50k pa each) joined in 2009 and 2011. The CEO (Martin Ward, £815k total) joined the Group in 2005 to run a subsidiary, became Group MD in 2009 and CEO in 2011. The CFO (Stephen Oakley, £550k total) also joined in 2011. Bonus of 100% of salary (the maximum) is included in the executive remuneration above; as stated earlier, this includes an element based on adjusted earnings – our view is that this should be the real, final earnings figure. The two executive directors were also awarded a total of 978,000 share options at an exercise price of 0.1p (worth £1.7m at the current market price). In addition, they hold 10.4 million 0.1p B shares which convert into ordinaries in 2028 if certain demanding but achievable criteria are met. Nothing is said about what happens if one of them leaves before 2028. Whilst the level of remuneration for the executives is acceptable, adding generous options each year - on top of the B shares with a potential value at today's price of £18.5m – seems excessive.
Excluding the directors, the average number of employees was 1,712, with earnings of £29.3k each. Institutions, led by Invesco, Woodford and Aviva, hold 72.5% of the shares.

SUMMARY
All credit to the Chairman and her board for putting Redde onto a strong financial footing and starting on a profitable, cash flow driven growth trajectory. Without a detailed knowledge of the insurance industry it is difficult to assess the scope for internally and acquisition led growth, but the opportunities should be there for some time to come; if things do slow down, the cash flow should support good dividends. We are unhappy about the items included as 'exceptional' in the calculation of adjusted earnings and about use of this as a measure of performance, particularly when used to calculate bonuses. Another reservation – apparently not shared by the institutional shareholders – is over what we consider to be excessive grants of options to the two executive directors.

HPB 23/02/2017