THE UK SHAREHOLDERS' ASSOCIATION INVESTIGATES AIM COMPANIES' ANNUAL REPORTS

Park Group plc – Number 98 in Investors Chronicle 'AIM 100' April 2016

Annual Report for year ended 31 March 2016

INTRODUCTION

Park Group "*is the UK's leading multi-retailer gift voucher and prepaid gift card business.*" The company was started by Peter Johnson in 1966 as a savings scheme for Christmas hampers and has, somewhat erratically, built on that base to reach a revenue total of £302.5m and pre-tax profits of £11.9m. The original hampers business is now only 2% of the total but the same principles apply – a major part of the business is focused on the Christmas period and the customer, by choice or necessity, pays up front with the funds held in trust. The business breaks down into two roughly equal halves, firstly a direct relationship with the consumer and, secondly, through company reward schemes. Marketing is via advertising, social media, agents and companies (reward schemes) although information given in the report is sketchy. The operating profit margin of 9.4% comes from the discount negotiated by the company with each of the participating retailers. Interest earned on customers' deposits is treated as finance income. Cash conversion is good, leading to a steadily increasing dividend, currently yielding 3.7%.

HISTORY

The report opens on page 1 with commendable bar charts showing the 5 year performance history, starting in 2012. The dilemma arising here is that there are two measures of sales, 'billings' and 'revenue'. The Chairman says "*As highlighted in previous reports, we consider billings to be a more appropriate measure…than revenue.*" So, to find out, it is necessary to go back to 2011 when the company introduced a prepaid cash card, 'flexecash', for customers who do not own a credit card. The amount spent on the card is included in billings but only the margin goes into revenue, the latter being the figure used by the auditors.

In his review, the Chief Executive (CEO) talks of '*a steady rise in billings'* but this is contradicted by the record which shows a setback in 2014 due to weakness in the retail sector. He then uses six years, from 2011, and quotes a rise in billings of close to 30%; the rise in the reported 5 years was 17%.

It is puzzling to find that having been in business for 50 years and having made aggregate pre tax profits of £50m in the last 5 years, there is a retained earnings deficit on the balance sheet of £3m and shareholders' funds are only £6.4m. Turning to the long term history, the earliest figures readily available are for 1999 when there was a retained earnings deficit of almost £10m (following goodwill write offs) with revenue at £209m. In 2000 the company started what turned out to be a disastrous foray into the home lending (and, later, mortgage) market which took the deficit to £40m in 2006 when the plug was pulled. Since then Park has concentrated on developing its core activities in the face of a constantly changing market.

THE REPORT

Congratulations to the company on sending a hard copy of the report promptly. Including covers, the document has 76 glossy white pages, of which 3 are blank. As we note with every review, the front cover says 2016 and it is not till later – in this case in the Chairman's statement on page 10 - that the year end is specified as 31 March. Presentation could be classed as good, were it not for a major problem, the use of a small, grey typeface throughout the report; this makes it difficult to read, particularly online. On page 1 the bars on the charts showing the historical record are light grey with tiny white numbers superimposed – almost impossible to decipher.

Pages 3 and 4 attempt to show a breakdown of billings,

- Page 1 gives the 'official' figure of £385m broken down later in the report into £211.5m consumer and £173.5m corporate.
- Page 3 shows a full page breakdown of billings by category which totals £790m.
- Page 4. A slightly different full page breakdown of billings totals £727m with, alongside it, a pie chart totaling £385.0m.

Your scribe has spent sleepless nights trying to puzzle this out, without success. The only way to stay sane seems to be to ignore pages 3/4.

Pages 8 and 9 show, in ascending steps, the major favourable milestones in the company's progression since it was started in 1966; as we have seen, the true picture is less rosy.

The reports by the Chairman, CEO, and Finance Director (FD) are (except for the comments above) straightforward and give a fair picture of the current state of the business.

Strategy, key performance indicators and risk analysis are all dealt with comprehensively. To the outsider there seem to be two long term threats. Firstly, there is the possibility of individual retailers negotiating down the discount or even refusing to work with Park. Secondly, whilst the flexecard and most of the vouchers can be used online, the company's demographic sector could be reducing in size and is probably happier on the declining high street than online. These threats are being countered by additional offerings, such as extending the range of prepaid cards and expanding into additional sectors, such as holidays and travel

The Directors', Corporate Governance and Remuneration reports are brief, helped by the fact that the only incentives are SAYE options and long term incentive plan.

THE ACCOUNTS

As stated earlier, the gross profit margin is 9.4% (£28.5m) so this is actually quite a small business, making a 3.4% (£10.4m) operating profit on revenue. Finance income from customer deposits is significant (£1.5m) although this seems likely to fall with reducing interest rates – or even go negative, a risk which is not mentioned.

The balance sheet assets include £75.2m held in trust (details of the trust are given in a note with a link to the company's web site for further information) against customer accounts and £28.8m (2015, £23.2m) of net free cash. There is goodwill of £1.3m and capitalised software of £3.0m; the latter is reducing slightly as amortisation is at a slightly higher rate than new additions. On the liability side, total current and non-current liabilities are £126.7m, being principally provisions for unclaimed vouchers, trade payables for goods ordered for future delivery (where the voucher provision has been released) and agents' commissions. A defined benefit pension scheme is closed to new members and there is an accounting deficit of £1.7m. These lumpy figures are supported by shareholders' funds of £6.4m.

DIRECTORS, EMPLOYEES & SHAREHOLDERS

The founder/chairman has just retired, selling his total shareholding, and the board now has 6 members, 3 non-executives including the new female chairman and 3 male executives. The CEO joined the board in 2000 as the FD, became MD in 2004 (succeeded as FD by the present incumbent) and CEO in 2012 when the founder stepped back from executive responsibilities. The third executive has been with Park since 1980, joined the board in 2001 and runs one of the divisions. The executive directors and selected employees have a modest new SAYE option scheme plus a long term scheme. The earnings of the executive directors, including incentive plans, were a generous £1.6m and the non-execs £0.2m.

There were 344 (314) employees with average earnings of £37k (£39K).

Institutions hold 82% of the shares and the board 1.7% plus a further 1% in options/incentives.

CONCLUSION

Park Group had little to show for its first 40 years of existence, as a result of unsatisfactory acquisitions and failed attempts to diversify. It is fruitless to try to apportion the blame but better to look at the last 10 years which have seen lessons learned, the ship steadied and the skeletons thrown overboard. The introduction of the flexecard seven years ago is seen by the board as a major turning point with the group now in a position to steer a steady course through what are likely to be choppy waters.

In the next report it would be good to see a comprehensible breakdown of billings and a more extensive explanation of sales and marketing activities.

HPB 16/09/2016