Cake Box Holdings Plc

Growth outlook remains sweet

25th November 2019

Cake Box, which announced strong interim results today, benefits from a unique value for money fresh Devon cream egg-free cake product offering, unusually visible growth and high returns on capital associated with its franchise model. The company should continue to add value as a brand manager, food manufacturer, and franchise retailer, with excellent execution.

Cake Box Holdings Plc released interim results today. Total sales were 6.0% higher with an 8.0% increase in gross profit. However, costs associated with important raised investment in the administrative team were a drag on profitability. More positively, net cash increased by £0.8m, which should reduce H2 finance costs, and new store openings maintained a good momentum to be on-track for the full year.

Cake Box's fresh Devon cream egg-free cakes clearly boast strong customer appeal. Its cakes represent affordable indulgences that are well suited to its franchisees' retail locations and customer bases. As special occasion and "treat" purchases, its products seem unlikely to fall foul of any health issues prevalent in UK consumer goods right now. Moreover, egg-free has appeal to a wide range of religious and dietary groups. Today, approximately 1 person in 20 in the UK has some form of egg allergy.

Cake Box's organic sales growth should remain brisk and visible. The company looks to open new franchise stores at a rate of around 24 per year. The ambition is to take its current franchised estate of 122 up to 250 in the next few years. Overall, the market for cakes and indulgences continues to grow. In this report, we also identify key UK regions which are ripe for footprint expansion.

Cake Box's franchise model massively uplifts shareholder value creation, through superior returns on capital employed and free cash flow generation. In contrast to "owned and managed" store operators, there is no cash drain that arises as a result of new openings. Return on capital employed and return on net equity in FY2019 were of the order of 40% and 48% respectively.

Share price weakness since the company's 14th October 2019 trading statement leaves the company's stock attractively valued, in our view. Based on valuation relative to an eclectic peer group, we argue a 170p share price makes sense, a potential uplift of 21%. This implies 3.2x EV/sales, 12x EV/EBITDA and a 17x P/E – i.e. arguably undemanding valuation multiples given Cake Box's capital light/brisk growth status.

Key financials

	2017A	2018A	2019A	2020E	2021E
Sales revenue (£m)	8.7	12.7	16.9	20.0	23.6
EBITDA adj (£m)	2.3	3.7	4.4	5.3	6.2
EV/sales (x)	6.2	4.2	3.2	2.7	2.3
EV/EBITDA (x)	23.5	14.4	12.0	10.0	8.6
EPS basic adj (p)	4.1	7.0	9.0	10.0	11.5
P/E (x)	34.7	20.3	15.7	14.1	12.2

Sources: Company accounts data and Equity Development estimates

Company Data

EPIC	CBOX
Price (last close)	141p
52 week Hi/Lo	188p/137p
Market cap	£56m

Share Price, p

Source: ADVFN

Description

Cake Box Holdings is a franchise retailer and manufacturer of egg-free cakes with a growing store base across the UK.

The company specialises in making high quality, affordable, bespoke and personalised fresh cream cakes for immediate purchase and for advanced orders, both on-premise and online.

Chris Wickham (Analyst)
0207 065 2690
chris@equitydevelopment.co.uk

Hannah Crowe
0207 065 2692
hannah@equitydevelopment.co.uk

Contents

Investment case

The central investment case for Cake Box is demand growth for its affordable, delicious and personalised fresh Devon cream egg-free celebration cakes, driven by ample room for geographic expansion and overall growth in its addressable market, with a financial performance underpinned by the company's franchise model. Near term profit growth and cash-flow prospects look attractive.

Egg-free cakes that appeal to everyone including lacto vegetarians but which, in our view, clearly lose none of their taste appeal to the end-customer, are central to Cake Box's offering. With the egg-free sponge base established as a unique selling proposition, the company distinguishes itself further by adding in layers of personalisation.

Cake Box effectively markets low price point indulgences. Starting at a selling price of £2.50 for a single slice of fresh, delicious and indulgent Devon cream product, its cakes are clearly affordable, good value for money and underpin the company's success in growing a business in a large number of lower income suburban locations. The concept is well-proven.

However, price elasticity for Cake Box cakes and treats is probably lower than for mainstream food items. In particular, cake consumption remains central to celebration and special occasions. The conspicuous nature of such occasions encourages generosity, helping to make the business more recession resistant.

The total addressable market for celebration cakes appears set to grow. As health and social pressures reduce demand for items such as high fat content/high calorie food, there is significant scope for occasional treats and indulgences to take up the slack. Fresh cream cakes can be part of a healthy diet because they tend only to be consumed occasionally.

Cake Box enjoys substantial scope to enlarge its geographical footprint within the UK. Currently, the company sells through 122 franchisee run stores. The target is 250 stores "over the next few years." We assume a new franchised store opening rate of at least 24 a year.

Salient under-represented, but appropriate regions include North West England, Wales and Scotland. We also view commitment to new products positively – examples include vegan products, gluten free cakes and egg free macaroons.

Cake Box's franchise model benefits both returns on capital and free cash flow. In contrast to retailers with "owned and managed" stores, the company faces no cash drain during its premises expansion period. Rather, any costs associated with new store openings should be more than compensated for by the franchisees paying sign-on fees. Sales of sponge and other essential materials to franchisees are the dominant source of group revenue.

Interim results released today reconfirmed the company's 14th October 2019 trading update, which reported a 6.0% increase in overall sales and a 6.9% gain in like-for-like sales. While profit numbers recorded a decline due to higher administrative costs, the net cash position improved and dividends increased by 33%. New store openings remain on track with 14 so far in FY2020 – 9 in the first half and a further 5 in the subsequent 8 weeks.

Valuation looks attractive. Relative to an eclectic peer group, we argue that a 170p share price makes sense. This would imply 3.2x EV/sales, 12x EV/EBITDA and a 17x P/E. These are arguably undemanding valuation multiples, given Cake Box's capital light/brisk growth status, recession resistance, and clear commitment to a progressive dividend payout.

Growth Outlook Remains Sweet

Overview

Cake Box is a celebration cake and indulgences retailer, which operates through 122 franchised outlets. The company distinguishes itself by offering a wide range of delicious, fresh Devon cream egg-free cakes, which satiate end-customers' needs for either celebration or immediate indulgence. To date, sales growth has been brisk.

The business, which is headquartered in Enfield, Greater London, was founded in 2008 and listed on AIM in June 2018. Its brisk growth reflects both product attractiveness and quality, and the positive cash flow dynamics of its franchise model. So far, funding has not proved a constraint on Cake Box's expansion, nor should it become one.

This report look firsts at the Cake Box offering and its inherent attractions (effectively proof of concept) before confirming the growth outlook for its total addressable market and taking a closer look at the financial workings of its franchise model. Overall, our view is that Cake Box is well positioned to grow its business sustainably on a shareholder value creating basis.

The Cake Box Offering – inherently attractive concept

Egg free cakes

Cake Box's unique selling proposition is that all of the company's cakes are egg-free. As a result, they appeal immediately to lacto vegetarians – i.e. individuals who are prohibited from consuming eggs on religious grounds, or exclude themselves voluntarily for other dietary reasons, while not barred from consuming dairy products. It is also estimated that around 1 person in 20 in the UK population has some form of egg allergy. Investors should note that, egg-free is so much in the "DNA" of the business that its web address is www.eggfreecake.co.uk rather than one based on the Cake Box brand name.

However, lack of egg in the base sponge – i.e. the essential component of a traditional layer cake – is clearly not a taste deterrent. Cake Box's cakes enjoy a deliciousness that can be attributed to being sweet and generously decorated with fresh Devon cream. The latter point is an important distinction from cakes that typically use buttermilk as a fresh cream alternative. In our view, fresh cream is significantly more indulgent.

The company's decision to produce egg-free has its origins in relation to its appeal to certain religious groups. Indeed, the concept was born out of the preference of many of the founders' family members, who follow strict lacto vegetarian diets.

However, in our view investors should look further ahead when assessing the impact of the company's egg-free strategy on shareholder value. Given the increasing popularity of new forms of "free from" diets, notably plant based and vegan, Cake Box's record as a pioneer is important. Indeed, this reputation was enhanced by the launch of vegan loaf cakes. As new fashions and trends emerge within UK food, the company should respond well.

Affordable prices

Cake Box sells its products at what are clearly affordable prices. Entry level indulgences currently include cup-cakes at £2.00 per item and single slice fresh Devon cream cakes at £2.50, which clearly represents good value for money for the end consumer. A simple bespoke, monogrammed birthday cake is on offer for around £20.00. Moreover, even the company's premium wedding cakes are available for a maximum of £249.00.

These prices' affordability can be inferred from the location of Cake Box's franchised outlets. The company's locations tend to be in heavily populated suburbs, which boast significant numbers of residents in the C2, D and E consumer categories, rather than being targeted at the super-affluent.

Moreover, while all online prices are set centrally and franchisees charge customers at the recommended retail price, there is some scope for franchisee flexibility in terms of the offering. Different regions and locations will inevitably lead to variations in product demand and affordability. We summarise key price points in Figure 1.

Figure 1 – Cake Box - Summary of Key Retail Offerings by Price

Product	Serves	Retail price
Cake slice	1 to 2	£2.50
Loaf cake (420g)	4 to 6	£4.99
Cheese Cake	8	£16.99
Fruit Gateaux	8	£19.99
Black Forest Gateaux	8	£22.99
Platter Cake	64	£69.99
Wedding Cake		£249.00

Source: Company data

Franchise based business

In our view a combination of profitable group revenue growth, historic expansion in outlet numbers and apparent ease of attracting new franchisees suggests that the model works well. It enjoys proof of concept. We summarise the model overall, look at historic growth in outlet numbers and comment briefly on recruitment in this section.

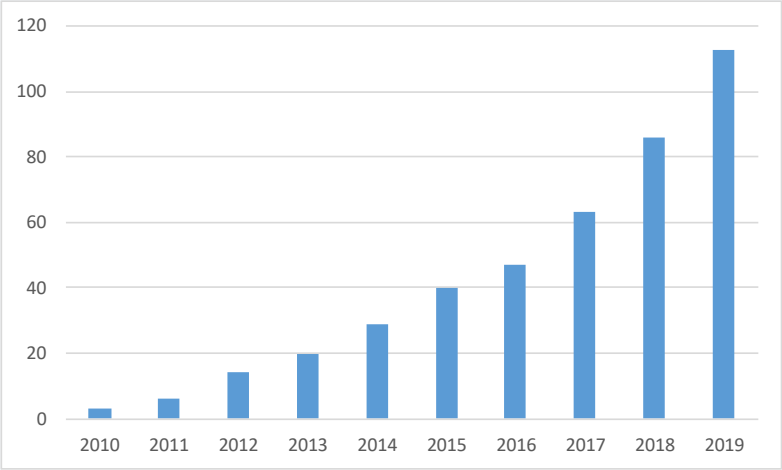
Cake Box's franchise model ensures that individual store operators become the main customer for the group's centrally manufactured sponges, and are also the high street brand ambassadors. The central mechanism – which we cover in more detail in our "look under the hood" section – is that franchisees, who apply to become store operators and receive significant training, pay a signing on fee to the group and then buy-in key materials.

As a result, ongoing revenue generated from the franchisees comprises purchases of sponge from the company's centrally located bakery in Enfield and other supplies, which include packaging materials, fresh cream, fruit and toppings.

Efficacy of the franchise model itself tends to be confirmed by historic growth in the number of outlets, which in turn supports the case for the group achieving its near term target of 250 outlets based on an average of 24 new stores annually. We summarise progress of new openings through to March 2019 in Figure 2.

This growth is arguably all the more remarkable given that Cake Box does not actively recruit new franchisees with any identifiable programme – for example, attendance at trade fairs or advertisements in trade press, franchise focused websites. Rather, the company currently receives 80 to 100 new franchisee enquiries each month.

Figure 2 – Historic growth in number of Cake Box outlets



Source: Company data

Addressable market – three clear routes to growth

Expanding outlets

Cake Box's current plans are to expand the number of outlets at a run rate of 24 new outlets per annum. Based on the close of FY2019, this implies a 21% increase in stores by end FY2020. Moreover, there is plenty of headroom for outlet number growth before the group achieves its 250 stores near term target. The company is on track to meet this number in FY2025 so long as the current momentum continues.

Scope to meet that objective without compromising the quality of the retail franchise is, in our view, clear. In particular, the estate's current "heat map" reveals a number of areas where the group is arguably under-represented relative to population. Furthermore, the argument that Cake Box thrives best *outside* super affluent areas supports its growth case.

The company enjoys ample scope to increase outlet numbers in the northern parts of England that boast large urban and sub-urban populations and are well within the company's target demography. In Figure 3, we compare Cake Box's current estate with UK population sizes by region. What is clear is that the estate has ample scope to grow even if only a few heavily populated regions meet what might be considered to be the expected number of outlets.

What Figure 3 highlights is that the company is currently well represented in London, the South East, West Midlands and East Midlands. At end-March 2019, 91 of the group's outlets were in these four regions – i.e. 83.2% of the estate. However while large, these regions were only home to 43.5% of the UK population.

Hence, there are some clear gaps to be filled. As new franchises open, so Cake Box's addressable market will grow. Notable gaps based on population appear to include the North West, Wales, East (mainly East Anglia) and Scotland. A UK map is shown in Figure 8.

Figure 3 - Cake Box Franchise and UK Population by Region

	CakeBox stores	% of estate	People m	% of population	Stores/ m people
Greater London (within M25)	38	33.6%	8.9	13.4%	4.3
South East	26	23.0%	9.3	14.0%	2.8
West Midlands	17	15.0%	5.9	8.9%	2.9
East Midlands	13	11.5%	4.8	7.2%	2.7
Yorkshire	10	8.8%	5.5	8.3%	1.8
North West	5	4.4%	7.3	11.0%	0.7
Scotland	1	0.9%	5.4	8.2%	0.2
North East	2	1.8%	2.7	4.0%	0.8
South West	1	0.9%	5.6	8.4%	0.2
East	0	0.0%	6.2	9.3%	0.0
Northern Ireland	0	0.0%	1.9	2.8%	0.0
Wales	0	0.0%	3.1	4.7%	0.0
Total	113	100.0%	66.6	100.0%	1.7

Note: Store locations refer to Cake Box definitions while population locations use ONS definitions. These definitions broadly match.

Sources: Company data, Office for National Statistics data

Sweet treats and indulgences – underlying demand growth

Cake Box sells into a category that is not only large, but in contrast to a number of consumables sub-segments, has scope to enjoy volume growth. Its products are designed to be eaten as indulgences and treats. They are geared towards celebrations and special occasions rather than to be part of staple diets.

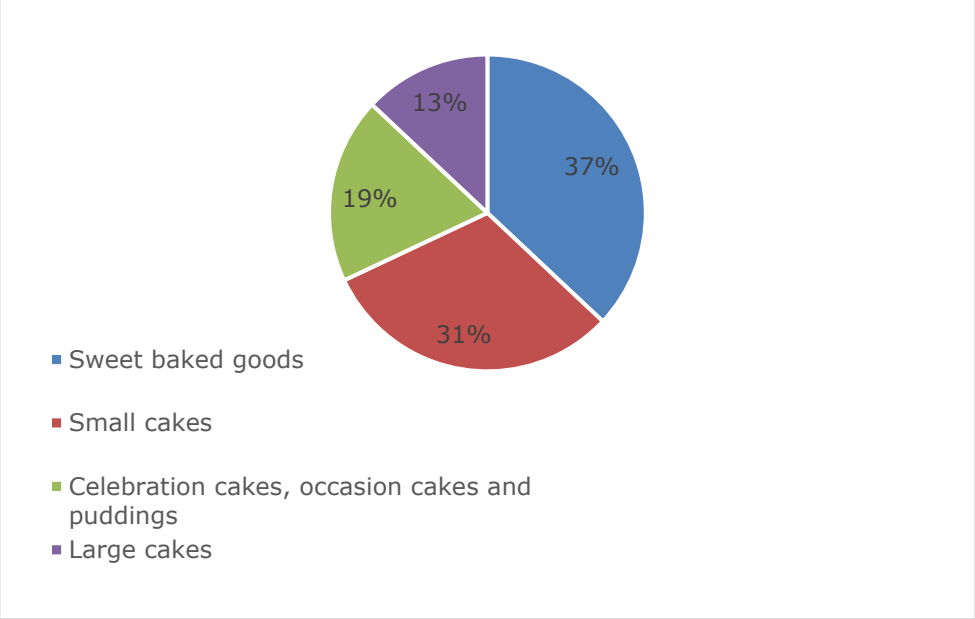
As a result, demand for indulgent cakes should benefit from underlying increases in living standards and consumer expenditure while largely escaping any negative feedback from the health lobby. The most obvious contrast in our view is carbonated soft drinks, where the size of the market and high profile of the brand manufacturers led to their relatively high sugar content products being singled out for a special Government measures – i.e. the sugar tax.

In the first half of Cake Box's 2019 financial year, the UK ambient cake market grew by 2% to £1,047m according to IRI data. **The broader UK retail market for cakes, cake bars and sweet baked goods was estimated in 2017 to be of the order of £2,200m**. According to IRI and Mintel data, both markets recorded modest but steady growth in the past decade.

We infer cakes and cake bars advanced at around a 1% clip with sweet treats faster at 3%, which implies that, against a steady market backdrop, Cake Box gained market share.

Importantly, Cake Box's franchisees offer bespoke services to customers at speed while maintaining competitive price points. Cakes can be personalised on-premise with free messages added. Moreover, the product ranges are broad and, in contrast to food multiples, the cakes themselves benefit from being freshly baked by the franchisee. We summarise cake market segmentation in Figure 4. Cake Box benefits from being able to operate across the range with the added benefit of having an online distribution extension.

Figure 4 – UK cake market by sub-segment in 2018



Source: Mintel, March 2018

The UK consumer

Despite a decade that, by the time it ends, will have included four general elections and three major referendums, UK consumer expenditure has proved resilient in the past ten years. The country's nominal sterling GDP advanced at a 3.4% compound annual growth rate, according to Office of National Statistics data and Price Waterhouse Coopers forecasts for 2019, while consumer spending progressed at a slightly faster 3.6% pace.

In 2020, PWC expects both economic indicators to advance by 1.3% - i.e. slower than 1.4% and 1.6% expected for the whole economy and consumer spending respectively in 2019. Given the business started to grow from its outset in 2008, it is arguably recession proof.

What matters about the consumption backdrop for Cake Box is that it is selling an affordable luxury service into growing overall consumer demand. So long as the offering is correct for its target demographic, which the bulk of sales growth and market share evidence proves that it is, there is no reason why, having taken into account the headroom for new franchises and the inherent popularity of cakes, the company's sales revenue growth should stall.

Cake Box's Franchising Model – A closer look

The purpose of this section is to look more closely at Cake Box's franchising model. We believe that the investor should be interested in how the lines of demarcation work, what the key processes are in and around new store openings and how the financials are structured.

Cake Box franchising – lines of demarcation

Cake Box's franchisees play a pivotal role in identifying incremental regional opportunities, finding new sites, recruiting staff and end-manufacturing the group's cakes. At end of 2019, there were 62 individual franchisees in the system. Of these, 20 were multiple store operators and 2 franchisees owned at least 7 stores each. What is clear is that there is scalable potential for franchisees as well as for the group itself.

Cake Box and its franchises work closely and on a complementary basis, both ahead of stores opening and in their continuing operation. These processes are summarised in Figure 5. What is important to note is that responsibility for expansion funding, ownership of the retail estate and the bulk of incremental employment rests squarely with the franchisee.

Figure 5 - Cake Box Plc and its Franchisees - Lines of Demarcation

	Franchisee	Cake Box
Pre-Opening Activities		
Site identification	Identifies potential sites in allocated area	Rigorous approval and due diligence on business/site
Funding	£125K of which £35K is cash and max £90K from debt	Debt facilitation
Lease agreement	Franchisee's lawyers negotiate lease in franchisee's name	Assist with negotiations
Franchise agreement	5-year franchise agreement/right to renew	Right to terminate if infractions committed
Store fit-out	Not involved	Project manage and fit out using 3rd party contractors
Staffing/training	Staff recruitment	Franchisee and staff trained by Cake Box
	Franchisee	**Cake Box**
Post Opening Activities		
Store operation	General store management, opening hours	Guides on menu, pricing and opening hours
Cake production	Makes, decorates and personalises cakes	Manufactures and supplies sponges and ingredients
Other cakes	Pre-packaged cakes also sold in-store	Bakes & packages ambient cakes in-house
Ancillary products	Candles, balloons etc. purchased from Cake Box	Procured and distributed by the group
Compliance & reporting	Responsible for food safety & hygiene, health & safety	Monthly shop audits which use 130 point check list
Ongoing training	Responsible for ongoing training of own staff	Workshops, online franchise forum, use of intranet

Source: Company data

Franchisee model – financial effects

The primary financial benefit of the franchisee model is that it renders Cake Box capital light as a whole. While it is clear that the company will need to invest in new capital equipment for manufacturing as its business expands, the cash strain which store numbers expansion might place on a retail driven operation does not apply in the instance of Cake Box. The franchisees fund the expansion of the retail estate.

It is important also to understand the build-up of group sales revenue in relation to the franchise system's sales revenues.

In Figure 6, we illustrate the relationship between total franchise system sales and Cake Box's own sales revenue line, which is a function of the 8 components of group sales. These figures, which are to some extent illustrative, are based on what we infer from FY2018 data.

Figure 6 - Cake Box Revenue Build-Up - FY2018 example

	Sales in £m	% Cake Box Sales
Franchisee sales	**23.60**	
Capture rate	54.4%	
Cake Box sales	**12.83**	**100.0%**
Sponge & confectionery sales	5.06	39.4%
Supplies	5.02	39.1%
Recharges of equipment	0.23	1.8%
Franchise packing fee	0.59	4.6%
Shop set-up fees	1.61	12.5%
Online sales	0.18	1.4%
Rental income	0.09	0.7%
Other income	0.05	0.4%

Source CakeBox

The direct relationship between organic sales growth and the franchisees' sales growth rests firmly with sponge and confectionery sales and other supplies. Cake Box sells these items to its franchisees in order to generate around 80% of group sales. The other franchisee related revenue components include recharges of equipment, franchise package fees and shop set-up fees. The shop set-up fees importantly **reduce any cash flow strain** that might be associated with store numbers expansion.

On-line sales are currently small in relation to overall group net sales revenue. We assume that they will continue to be less than 5% of the total for some time. However, it would be strategically remiss in our view for Cake Box not to have some form of online presence. Moreover, the online business – where group sales are charged as a commission - dovetails into the franchise system for click & collect.

Management and Strategy

Management

Cake Box's leadership team is dominated by its founders who are rich in both food manufacturing and retail experience. As a result, they are well practised in relevant industry-based decision making and what works specifically for the group.

Cake Box's founders are **Sukh Chamdal and Pardip Dass** who are the incumbent CEO and CFO respectively. The third executive director is Dr Jaswir Singh who acts as COO. All other Directors including the chair are non-executive.

Sukh Chamdal, who opened the first Cake Box store in 2008 and co-founded the franchise business in 2009, boasts over 35 years relevant experience in both food manufacturing and

food retailing. In addition, he had an equally relevant consulting role – given the sponge business – in a food equipment company that specialised in high volume food production.

Pardip Dass, whose background includes time at Starbucks, Masala Zone and Group Chez Gerard, was the other co-founder in 2009. He balances Sukh Chamdal's manufacturing skills with knowledge of both retailing and franchising.

Dr Jaswir Singh joined the business slightly later in March 2010 having enjoyed an extensive career in clothing retail and 9 years in charge of his own restaurant business.

We summarise the Board of Directors in Figure 7.

Figure 7 - Cake Box Plc Board of Directors

Officer	Role	Age
Neil Sachdev	Non-Executive Chair	63
Sukh Chamdal	Co-founder and CEO	57
Pardip Dass	Co-founder and CFO	47
Dr Jaswir Singh	Chief Operating Officer	62
Martin Blair	Non-Executive Director	61
Adam Batty	Non-Executive Director	47

Source: Cake Box Plc Annual Report & Accounts 2019

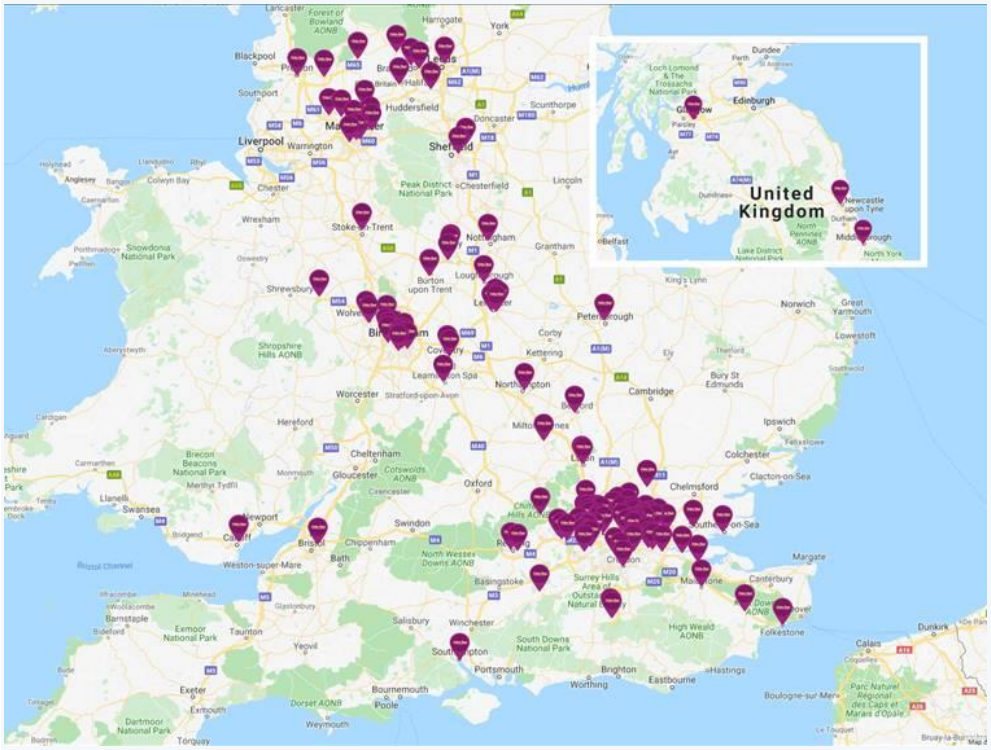
Strategy

Group strategy remains tightly focused on managing the organic expansion of the franchised estate while maintaining high standards of product quality for both the franchisees to buy in and end customers to enjoy. The company's ability to combine a capital light business with both visible growth and clear barriers to entry tends to confirm strength of management and strategic clarity.

A visual idea of potential gaps in the company's geographic coverage – discussed earlier – can be gleamed from Figure 8, which shows franchised store locations as at June 2018. It tells a similar story to Figure 3 – i.e. expansion opportunity for the retail estate.

We also note the company's commitment to new product development as a support for same store sales growth. Cake Box looks to launch more vegan products as well as gluten free and egg-free macaroons.

Figure 8 – Franchised Store Locations – June 2018



Source: Company data

Financials

Interim results announcement

Cake Box announced interim results on 25th November that included a 6% increase in group net revenue and an 8% rise in gross profit. However, both EBITDA and pre-tax profit suffered setbacks due to an increase in administration costs from £1.7m to £2.2m. Adjusted EPS fell by a more stark 16%.

However, it is important for investors to note that the rise in administration costs was a function of increased investment in the company's operational team. It was consistent with confidence in and commitment to future growth and, in our view, should be viewed favourably.

Underlying positives in the first half included an improved net cash position, yet full to be reflected in net finance costs which were higher, and a sustained pace of new store openings. The company's net cash rose by £0.8m to £3.2m. New store openings numbered 9 in the first half in relation to a target of 24 for the year. So far in FY2020 H2, the rate has picked up with 5 new openings to date. The company fully expects to meet its full year target of new openings. We summarise interim results highlights in Figure 9.

Figure 9 - Interim Results highlights

£m	FY2019 H1	FY2020 H1	Increase
Revenue	8.28	8.77	6%
Gross profit	3.67	3.95	8%
EBITDA	2.18	1.97	-9%
Adjusted pre-tax profit	1.97	1.74	-12%
Net cash	2.40	3.22	34%
EPS - unadjusted (pence)	2.85	3.67	30%
EPS - adjusted (pence)	4.35	3.67	-16%
Interim dividend (pence)	1.2	1.6	33%

Source: Company data

Despite the first half profit decrease, the board announced a 33% increase in the interim dividend, which augurs well for the full year. Stated dividend policy is for one third of the full year dividend to be paid out at the interim stage. Importantly, the company's capital light structure and positive free cash flow should support future dividend growth.

Relative valuation

Listed food companies that combine manufacturing, retail, franchising and brand management are the key comparators in our view for CakeBox. We include three other members of this eclectic group in Figure 10. Key out-takes are that Cake Box trades in line with the group on EV/sales at around 3x, which seems reasonable for a capital light company with visible growth, and that its earnings based measures imply a notable discount. At its current share price, the company appears undervalued on a relative basis.

There is clear headroom for Cake Box's shares to achieve a higher valuation based on the multiples shown below. Should the company achieve 3.2x EV/sales, 12x EV/EBITDA and a 17x P/E, which seem to be reasonable multiples given its low capital/brisk growth status, the shares should increase to 170p.

Figure 10 - CakeBox - Relative Valuation

Company	Share price (p)	Shares o/s (m)	Market cap (£m)	Debt (£m)	EV (£m)	Sales 2020 (£m)	EV/sales 2020 x	EPS 2020 (p)	EPS 2021 (p)	P/E 2020 x	P/E 2021 x	EBITDA 2020 (£m)	EV/EBITDA 2020 x
CakeBox	141	40.0	56	-3	53	20	2.7	10.0	11.5	14.1	12.2	5	10.0
Domino's Pizza	299	462.2	1382	371	1753	646	2.7	16.4	18.1	18.2	16.5	114	15.4
Greggs	2041	101.2	2065	87	2152	1229	1.8	92.9	100.0	22.0	20.4	205	10.5
Hotel Chocolat	435	112.8	491	20	511	150	3.4	10.7	12.4	40.7	35.1	23	22.2
Average							2.6			23.7	21.1		14.5

Note: share prices refer to closing price 22nd November 2019

Source: Company data, ADVFN, marketscreener.com, ED estimates

Forecasts

Our income statement projections are based on the earlier mentioned assumption that the company will open 24 new stores annually and that average revenue per store drops by 3% in FY2020 and by ½% to 1% thereafter. It seems inevitable in our view that this metric will be under pressure given the company's need to assimilate new stores into the system.

A discrete revenue model is included in Figure 11, which shows our store number revenue per store assumptions. We apply historic trends for the translation of sales per store franchised revenue into group revenue. We hold this inferred "capture rate" at around 55%.

Brisk organic sales growth are thus a salient feature of our income statement projections. Net finance costs turn to negative as the company generates positive free cash flow and moves to an overall net cash position on its balance sheet.

Cake Box's capital light franchising model explains the relatively benign movements on both working capital and debt in its balance sheet as well as relatively low levels of fixed investment expenditure in the free cash flow forecasts. However, we would expect the centre to incur increased investment in P, P & E as demands on its sponge production facilities increase due to higher overall sales.

Figure 11 – Revenue Drivers

End March year-end	2017A	2018A	2019A	2020E	2021E
All figures in £'000s					
Basic drivers					
Franchise stores end-period	63	86	113	138	163
Newly opened stores	16	23	27	24	24
% increase in stores	34.0%	36.5%	31.4%	22.1%	18.1%
Franchise stores (average)	55	75	100	126	151
% increase in avge stores	26.4%	35.5%	33.6%	26.1%	19.9%
Revenue per store	365	317	306	296	290
% increase in revenue/store	9.6%	-13.3%	-3.6%	-3.1%	-2.0%
Total franchise revenue	20,100	23,600	30,400	37,148	43,645
% increase in franchise revenue	38.6%	17.4%	28.8%	22.2%	17.5%
Inferred capture rate (%)	43.1%	54.0%	55.6%	53.9%	54.1%
Sales revenue	8,664	12,739	16,909	20,023	23,612

Source: Company data and ED estimates

Figure 12 – Income statement

End-March year end All figures in £'000s	2017A	2018A	2019A	2020E	2021E
Revenue	8,664	12,739	16,909	20,023	23,612
% increase in revenue	54.9%	47.0%	32.7%	18.4%	17.9%
Cost of sales	-5,015	-7,263	-9,189	-10,812	-12,750
Gross margin (%)	42.1%	43.0%	45.7%	46.0%	46.0%
Total operating costs	-1,661	-2,095	-3,271	-4,398	-5,231
EBIT - adjusted	1,987	3,381	4,449	4,812	5,631
EBIT margin (%)	22.9%	26.5%	26.3%	24.0%	23.8%
EBITDA - adjusted	2,268	3,700	4,435	5,322	6,232
EBITDA margin - adjusted	26.2%	29.0%	26.2%	26.6%	26.4%
Net financial income	-63	-46	-42	60	128
Pre-tax profit adjusted	1,924	3,336	4,407	4,872	5,759
Taxation	-299	-568	-806	-877	-1,152
Tax rate (%)	-15.5%	-17.0%	-18.3%	-18.0%	-20.0%
After tax income - adjusted	1,625	2,768	3,601	3,995	4,607
EPS - basic adjusted	4.1	7.0	9.0	10.0	11.5
DPS - total	1.6	1.6	3.6	5.0	5.8
Dividend pay-out ratio (%)	31.0%	23.0%	48.0%	50.0%	50.0%

Source: Company data and ED estimates

Figure 13 – Balance sheet

End-March year end	2017A	2018A	2019A	2020E	2021E
All figures in £'000s					
Assets					
Property, plant & equipment	3,334	3,341	5,048	5,190	5,249
Investment property	322	343	-	-	-
Trade and other receivables	43	259	53	63	74
Total non-current assets	3,699	3,943	5,101	5,253	5,322
Inventories	55	709	910	1,077	1,270
Trade and other receivables	1,153	1,301	1,532	1,815	2,140
Cash and cash equivalents	476	2,506	3,082	5,212	7,606
Non-current assets held for sale			650		
Total current assets	2,184	4,516	6,174	8,104	11,017
Total assets	5,883	8,458	11,275	13,356	16,339
Equity & liabilities					
Share capital	0	0	400	400	400
Capital redemption reserve	0	0	0	0	0
Revaluation reserve	438	455	821	821	821
Retained earnings	1,960	4,205	5,402	7,400	9,703
Total equity	2,398	4,661	6,623	8,621	10,924
Trade and other payables	1,091	1,493	1,532	1,814	2,139
Short term borrowings	197	186	212	212	212
Corporation tax liabilities	297	520	747	522	876
Total current liabilities	1,586	2,198	2,492	2,548	3,227
Borrowings	1,724	1,457	1,938	1,938	1,938
Deferred tax liability	175	141	222	250	250
Total non-current liabilities	1,898	1,599	2,160	2,188	2,188
Total liabilities	3,485	3,797	4,652	4,735	5,415
Total equity & liabilities	5,883	8,458	11,275	13,356	16,339

Source: Company data and ED estimates

Figure 14 – Free cash flow

End-March year end	2017A	2018A	2019A	2020E	2021E
All figures in £'000s					
Pre-tax profit (reported)	1924	3336	3809	4872	5759
Depreciation	281	319	431	510	601
Profit on disposal	0	-5	-3	0	0
Increase in inventories	-30	-154	-201	-168	-193
Increase in receivables	-785	-364	-25	-272	-314
Increase in payables	-671	402	39	282	325
Net fair value gain	0	0	-444	0	0
Finance income	-0	-1	-7	0	0
Cash generated in operations	719	3532	3598	5224	6178
Finance costs	63	47	49	0	0
Taxation paid	-180	-363	-497	-877	-1152
Net cash from operating activities	602	3216	3149	4347	5026
Cash flows from investing activities					
Sale of investment properties	0	190	140	0	0
Purchases of PP&E	-264	-531	-567	-652	-660
Purchases of assets under construction	0	0	-1571	0	0
Purchase of investment properties	-137	0	0	0	0
Sale of investment properties	0	0	0	0	0
Interest received	0	1	7	0	0
Net cash used in investing activities	-400	-340	-1991	-652	-660
Cash flows from financing activities					
Interest paid	-63	-47	-49	60	128
Free cash flow before dividends/buybacks	139	2830	1110	3755	4494
Dividends paid	-70	-522	-1040	-1625	-2099
Share buybacks	0	0	0	0	0
Free cash flow after dividends/buybacks	69	2308	70	2130	2395

Source: Company data and ED estimates

Investor Access

Hannah Crowe
Direct: 0207 065 2692
Tel: 0207 065 2690
hannah@equitydevelopment.co.uk

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www.equitydevelopment.co.uk

Equity Development, 15 Eldon Street, London, EC2M 7LD. Contact: info@equitydevelopment.co.uk 0207 065 2690