NEWMARK SECURITY PLC (LON:NWT)

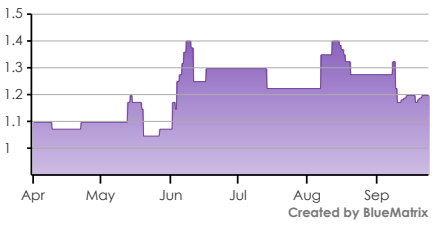
28 September 2020

proactive research

Consumer Electronics

52-WEEK HIGH	**1.7p**
52-WEEK LOW	**0.6p**
PRICE	**1.2p**
MARKET CAP MLN	£5.34

Share Price



Major Shareholders

Shares in issue	468,732,316
Avg Three-month trading volume	344,619
Primary Index	LSE
Next Key Announcement	Yr end Dec

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Newmark Security :Clocking on

Strong market position in all core segments

Newmark Security (AIM:NWT) specialises in products and services in the security and data sectors. The company has two operating divisions:

1) People & Data Management consists of two sub-segments – Human Capital Management and Access Control

The Human Capital Management (HCM) segment provides edge devices, also known as timeclocks, for time and attendance capture and general workforce management applications. This business segment has achieved strong revenue growth in recent years, and we argue this could be the main driver of financial performance for the group in the coming years. Human Capital Management now represents 49% of group revenues.

The timeclock is an essential piece of apparatus in a wide variety of workplace environments. Newmark has developed a high quality and highly flexible suite of timeclock solutions, backed by a responsive customer service capability. This has resulted in substantial market share gains in recent years. In the US in particular Newmark has achieved a sevenfold increase in revenues over three years.

The Human Capital Management (HCM) business also has further opportunity to increase value capture via a software-as-a-service (SaaS) offering of hardware and software that is being rolled out. We examine the HCM business in detail in this report.

The other segment within People and Data Management is Access Control. This business has a strong market position in electronic building entry systems. During the last year, Access Control benefited from new product launches and remains well-positioned for future growth.

2) Physical Security Solutions:

The Physical Security Solutions division provides security products and services for a global customer base. Newmark operates under the Safetell brand, which is a trusted name in safety-critical applications, with customers including government agencies and major global corporations.

Current trading, and valuation

The company reports that COVID-19 has had an impact on operations with some projects being delayed; however, with measures undertaken to address these conditions, we believe that Newmark is well-positioned to come out of the pandemic in good shape.

We argue that the current share price represents a deep discount valuation. We examine this on p8 in terms of operating cash flow yield and Enterprise Value (EV)/Sales, and we argue that the current valuation represents an interesting entry point.

Year end Apr 30	Current	2018	2019	2020
Revenue (£mln)	16.0	16.0	19.6	18.8
Gross Profit (£mln)	4.5	5.1	7.7	7.5
EBITDA margin (%)	99.0	99.0	99.0	99.0

Marie-Claire Dwek, chief executive officer (CEO)

Marie-Claire Dwek has been CEO of Newmark Security PLC since 2013. Before this, she spent more than a decade in real estate investment & management. She gained experience of the security technology sector as marketing director for an electronic security provider.

Graham Feltham - finance director

Graham Feltham joined Newmark Security PLC in September 2019. He qualified as a chartered accountant with Ernst & Young in 2000 and since then has held financial roles within Belron and StatPro Group PLC.

Investment summary

Newmark Security PLC (AIM:NWT) is a company focussed on the provision of products and services in the security and data sectors, with its principal operating bases in the UK and the US. The company has two divisions: People & Data Management and Physical Security Solutions.

The People and Data Management division operates under the Grosvenor Technology brand and has two areas of activity. Human Capital Management is focused on edge devices, also called timeclocks, used for time and attendance capture and broader workforce management applications, as well as related software and services. The other activity — Access Control — provides electronic solutions for site access as well as related services.

The Physical Security Solutions division provides products and services for enhanced security for businesses and government agencies, with products including reinforced glass installations for cashiers, and protective doors and partitions.

The People and Data Management division has been the main driver of growth for Newmark Security in recent years with a compound annualised growth rate (CAGR) of 23% over the last three years.

The following diagram summarises the two divisions:

Two divisions covering three product categories

Newmark business overview



Source: Proactive Research

We expect the People and Data Management business to continue growing strongly and to drive revenue growth for the group as a whole.

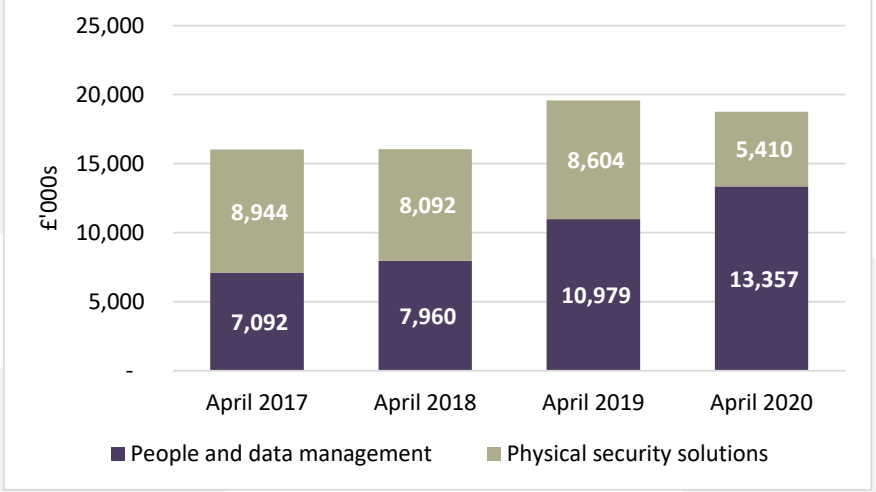
Within People and Data Management the Human Capital Management business has particularly compelling drivers including:

- Continuous market share gains in recent years that support our thesis that Newmark has developed a unique product and service offering
- An SaaS offering entering the mix, which has the potential to drive additional revenue and enhance revenue visibility

The following chart shows recent revenue progress across the two divisions:

The People and Data Management unit has been the growth driver

Revenue history



Source: Newmark Security data

Market presence

Across the two divisions, Newmark has a customer base that includes hundreds of the world's most recognised brands. The following diagram illustrates some of these:

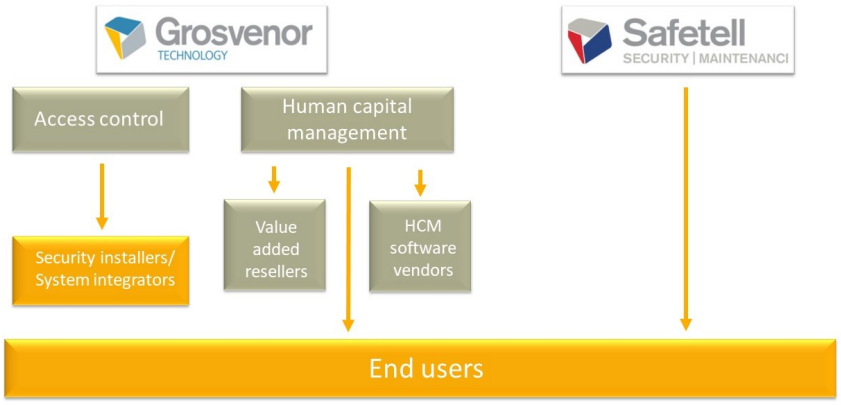
End customer base



Source: Newmark Security

In terms of routes-to-market this varies across the different product lines. The People and Data Management business, under the Grosvenor Technology brand, sells its edge devices through human resources (HR) software vendors, value-added resellers, and also direct to end customers. The Access Control business sells mainly through security installers and integrators. The other division, Physical Security Solutions, trading under the Safetell brand sells mainly directly to end-users. The following diagram illustrates the routes to market:

Routes to market



Source: Newmark Security

Market share gains have been driven by a responsive approach to customer requirements

The recent success of Grosvenor Technology reflects Newmark's deep relationships with the customer value chain, which has allowed the company to respond to customer demands including:

- Sophisticated device interfaces including contactless and biometric ID options
- Bespoke modular system configurations tailored to the customer
- Highly responsive customer support and service

Some legacy vendors of timeclock hardware do not see the clock as their core activity. This has created an opportunity that Newmark continues to build on.

Overall we argue that Newmark Security offers an exciting investment proposition based on:

- Strong market positions and a highly differentiated offering of products and services
- Compelling growth drivers for hardware and software revenue
- Significant potential profit growth on a 2-5 year view

People and Data Management

The main growth driver for Newmark in recent years has been the Human Capital Management segment of the People and Data Management division.

The HCM segment

The edge device (timeclock) is an essential tool to customers

In Human Capital Management, Newmark has built a comprehensive offering of products and services around its core hardware application: timeclocks for an employee to sign in and out of his or her shift. These are sold under the brand Grosvenor Technology, and in the US under the shortened version GT Clocks. The following illustration shows some of the hardware:

Grosvenor clocks



Source: Newmark Security

The Grosvenor Technology range of hardware solutions designed to be "always on" in a high usage setting and able to operate in the harshest environments. Longevity is designed-in, using high spec components and a US and Europe based supply chain.

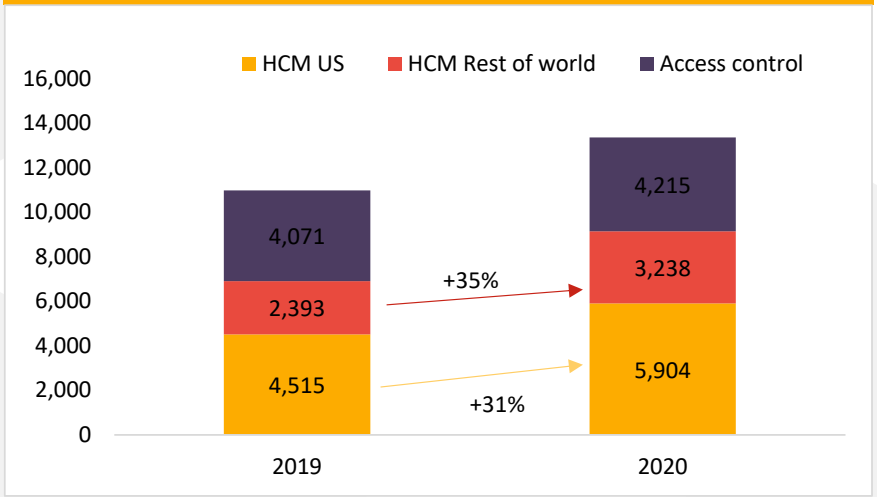
The hardware is supported by a proprietary suite of software that is an important part of the product offering (more detail on p6)

Dramatic market share gain in North America

In recent years Newmark has achieved strong growth in HCM. In the US in particular GT Clocks has grown from just over US$1mln of revenue in 2016 to US $7.3mln in the full-year to April 2020 (FY 2020).

The following diagram illustrates the growth of the People and Data Management division in FY 2020 by segment:

Revenue growth for Human Capital Management



Source: Newmark Security data

Revenue growth has been driven by market share gain at the expense of legacy vendors some of whom do not consider clock hardware a strategic focus. In spite of market share gains, we estimate that Newmark has only 1-2% share in the US timeclock market. As such, there is essentially almost unlimited headroom for continued growth.

Edge devices are sometimes sold direct to the end-user, or through value-added resellers, but the biggest route to market is via HR software vendors. One significant change in the last year has been the merger between two US software houses Kronos and Ultimate Software, which was announced in February 2020. This means that Ultimate Software will now have an in-house provider of edge device (timeclock) hardware. It is not clear at this stage if this means that Ultimate will switch all of its device purchases to its in-house supplier, or whether the hardware business will have a lower priority within the merged group.

Looking at the total market space, we conclude that Newmark has a broad range of potential and existing routes to market in the US and we expect the company will achieve continued growth.

Two revenue models extend the service offering in timeclocks

A current initiative – the SaaS offering

Another growth driver for Newmark in Human Capital Management will be the provision of software under a subscription model. This consists of two revenue models that will make up an increasing part of the mix going forward:

Under the software-as-a-service (SaaS) model the customer makes an upfront purchase of the hardware and receives the software by subscription.

Under the "clock-as-a-service" (ClaaS) model, both hardware and software are provided on a subscription basis.

Both models are delivered through the cloud, via platforms such as Microsoft Azure. In this sense, the new business models move in step with customer preferences, which have evolved from on-premise to cloud-first to cloud-only systems.

Newmark's proprietary software is a key element of the offering to customers

Software is already an important part of the Grosvenor Technology offering. The software provides:

- Remote diagnostics and recovery

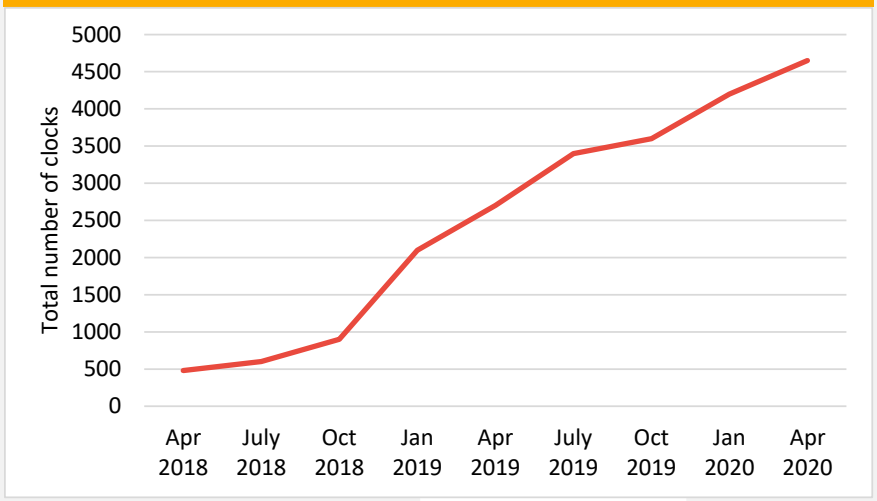
- Global estate management
- Clock-to-cloud integration middleware
- People Data (PII) template distribution
- People data consent and compliance

The Newmark team of developers have a high level of expertise in providing flexible bespoke solutions allowing Grosvenor hardware to be applied on any HR software platform.

The transition to SaaS will allow Newmark to create additional value from hardware post-deployment, and to benefit from increased revenue visibility. Currently, recurring revenue represents only around 5% of People and Data Management divisional total, but we expect this to grow rapidly. The following chart shows the estate of clocks currently under service contracts.

Growth in the number of clocks under service contracts

The clock estate



Source: Newmark Security data, and Proactive Research estimates

We expect the number of clocks under service contracts to continue to grow.

In access control Newmark offers an extensive suite of capabilities for a security management system

Access Control:

The other part of the PDM business is Access Control. Access control systems are an integral part of end-users' building management system. Grosvenor Technology Access Control offers a full suite of capabilities to deliver a modern 'security management system'.

The business offers two software platforms, 'Sateon Advance' and 'Janus C4', which cover requirements from a single door system to an enterprise covering many buildings and thousands of employees. Both platforms share a range of modular hardware that provides scalable solutions, which can be mixed and matched to be deployed in either single or multi-controllers. The hardware can also be easily integrated into other existing Access Control software platforms, creating a further recurring revenue opportunity for the business.

In FY 2020 the company achieved 4% revenue growth in the access control business. This was driven partly by the rollout of Janus C4. This new platform is designed for an evolving market, with customers moving away from stand-alone Access Control solutions, towards integrated Access Control, Intruder, CCTV (closed-circuit television), Fire and Building Management within a single platform.

The success of the new platform together with a favourable pricing environment in the industry led to a strong performance in the 2020 financial year, and we expect Access Control to continue to contribute to the growth of the PDM division.

High quality security solutions for the public and private sectors

Physical Security Solutions

The Physical Security Solutions division operates through the Safetell brand and provides high-quality security solutions across a public and private sector customer base. Safetell designs, develops, installs and maintains physical security systems.

Products include:

- Hammer proof and bulletproof cash counters, windows and movable screens
- Secure portals and revolving doors
- Remote locking systems
- Bulletproof doors and partitions
- Interlocking door air locks

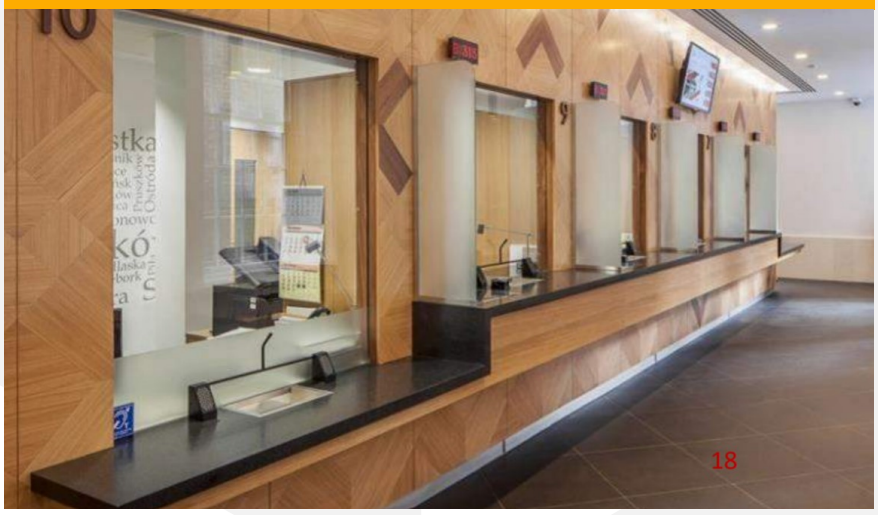
Services include:

- Installation and maintenance
- Consulting services for bespoke physical security products
- Counter-terrorism and target-hardening solutions for government agencies and businesses

The following image shows an example of a Safetell product:

Image shows reinforced tellers' stations

A Safetell product

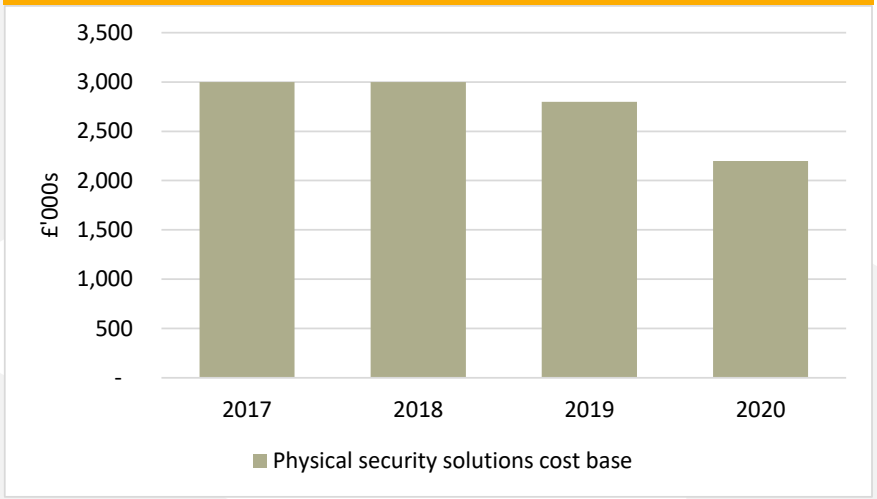


Source: Newmark Security

Safetell experienced a decline in revenues in FY April 2020, partly reflecting a structural decline in cash handling high street businesses, for example, bookmakers moving online and banks consolidating branch networks. This led to a decline in profits for the PSS division, with a small negative (£12,000) reported for the year. The company undertook restructuring, leading to cost savings of £1.3mln. The following chart illustrates the reduction in the cost base:

A big reduction in overhead costs achieved through the restructuring programme

Physical Security Solutions overhead reductions, our estimates



Source: Proactive Research

We have based our estimates on the reported profit and revenues of the division, and our estimate of the split of overheads versus cost-of-goods-sold.

We believe that the restructuring has aligned Safetell to a reduced demand environment. Looking forward we believe that there will remain a demand for Safetell products and services. Governments and enterprises will always have facilities and employees that need to be protected from threats of crime and terrorism. We expect the Physical Security Solutions division to return to profitability.

Financials

Newmark has reported that COVID-19 had an impact on business in the final months of FY April 2020, and continues to have an impact in the current year with some projects being delayed as a result of pandemic measures. We expect the pandemic to have a material impact on FY April 2021.

In spite of the current impact of coronavirus, fundamentals remain strong

Looking ahead, we believe fundamental demand drivers remain intact and we expect Newmark to make a full recovery and resume growth. We note that some product offerings may also experience lasting benefit from a focus on employee health and hygiene, such as contactless timeclocks and entry systems, and hygiene screens as an added revenue driver in PSS (orders have already been received).

We believe it's too early to make financial forecasts for FY April 2021, but we are confident that Newmark remains well-positioned for resumed growth going forward.

Valuation:

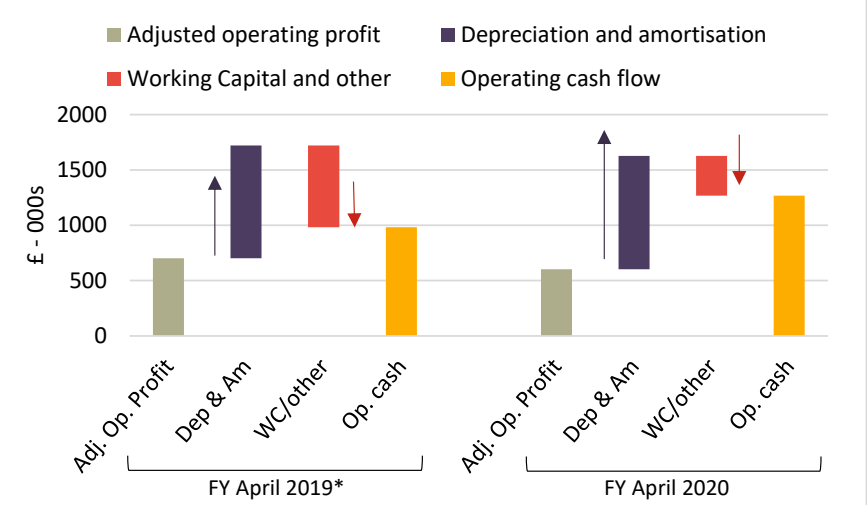
In terms of valuation, we consider some metrics based on recent historical performance.

Operating cash flow metrics

Newmark has generated strong operating cash flows in the last two years. The following chart shows operating cash flow in relation to profit before tax (PBT). For this purpose both PBT and operating cash flow are before exceptional items such as restructuring. The 2019 figures are restated to apply accounting standard IFRS 16 for comparability with 2020:

Over £2mln of cash generation over two years

Operating cash flow



Source: Proactive Research *2019 restated to apply IFRS 16

The average cash flow over the last two years was £1.1mln. Compared to the current enterprise value of £4.7mln, this gives a multiple of 4.2x or a cash flow yield of 24%. We argue that this represents a low valuation.

EV/Sales

Another alternative is to look at the enterprise value (EV) to sales multiple. On FY 2020 revenue of £18.8mln, the current EV/Sale multiple stands at 0.25x. We argue that this is a very conservative valuation multiple for company with good prospective growth and profitability.

Quality revenue growth driven by market share gains. Low share price valuation

Conclusions

We argue that Newmark Security offers a compelling investment proposition based on:

- Revenue growth based on market share gains, particularly in the Human Capital Management business and in the US market
- A strong basis for a return to return profitability in the Physical Security Solutions business
- Valuation multiples that offer an attractive entry point for investors

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