

# ClearDebt



Company Description: ClearDebt offers debt resolution services, primarily IVAs and DMPs, using a state-of-the-art web-based system for initial contact and individual supervision of all the later stages in the process, resulting in a higher success rate and lower overall costs than its competitors.

## ClearDebt

### CLEA.L

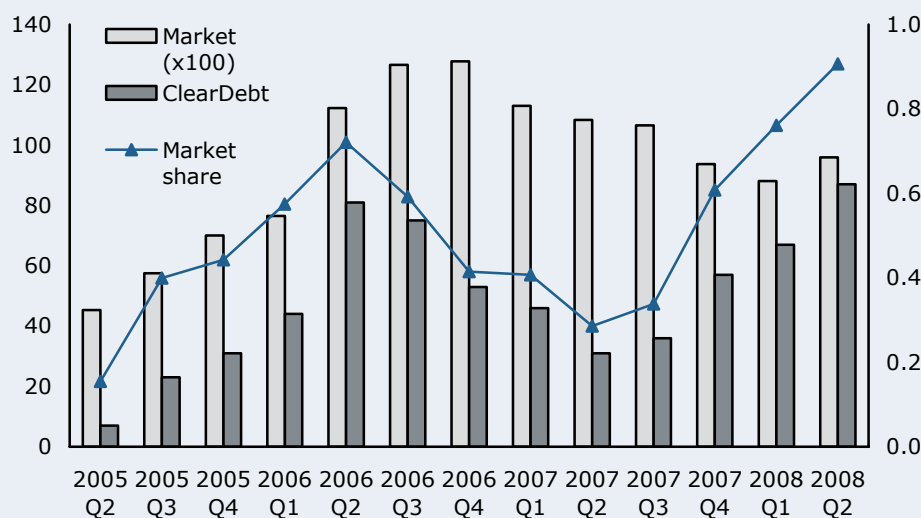
<b>Date:</b>	<b>18.11.08</b>
<b>Share price p</b>	<b>0.375</b>
52 week High/Low p	2.125/0.375
<b>Issued share cap</b>	<b>304.5906</b>
Market cap £m	1.1
NAV p	1.3
<b>Period to end-June</b>	<b>PBT £m</b>
2007	(0.66)
2008	(1.12)
2009 est	0.58

<b>Period to end-June</b>	<b>Earnings</b>	<b>PER</b>
2007	(0.24)	
2008	(0.20)	n/a
2009 est	0.15	2.50

**ClearDebt is one of the few companies for whom the current economic climate is favourable and with both divisions now trading profitably and growing it can look forward with confidence while several rivals are struggling.** Its low-cost high quality model enables it to help clients by providing IVAs even in cases that most of its competitors would turn down as uneconomic and to have a lower failure rate (less than 13% of cases to date). Consequently its market share of IVAs is growing: the number of IVAs passed for ClearDebt rose throughout 2007-8, more than doubling, although the national total was falling until the last quarter and the "book" of cases under supervision has been growing continuously.

The Chief Executive reports that, since its year-end, ClearDebt Ltd has twice set new monthly records for the numbers of IVAs approved and is now profitable, as is Abacus, and group cash flow is positive.

**Figure 1: New IVA approvals: ClearDebt and the overall market**



Its move into profit has been delayed by a year-and-a-half by the "Creditors' strike" that led to a fall in IVAs approved when demand was rising sharply in early 2007. This continued until the first quarter of 2008 and has had an on-going impact in reducing the number of IVAs that ClearDebt is supervising (and in a record number of consumers declaring themselves bankrupt – the number last quarter was 49% higher than for the whole of 1997). The repeatedly-delayed introduction of the SIVA (now expected in April 2009) has not helped.

The combination of the direct impact on the IVAs approved and the indirect impacts on the number under supervision and the cost of advertising as the largest IVA producers competed for "leads", combined with internal factors: the reorganisation and move following the acquisition of Abacus, and setting up referrer network and services to clients led to an increased loss in 2007-8.

ClearDebt is quoted on AIM and investors should be aware that shares traded on AIM are subject to lighter due diligence than shares quoted on the main market and are therefore more likely to carry a higher degree of risk than main market companies.

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**Table 1: Preliminary results for 2007-8**

<b>Year to end-June</b>	<b>2007</b>	<b>2008</b>	<b>Change</b>
	<b>£000</b>	<b>£000</b>	<b>%</b>
Turnover	421.0	1,869.2	344.0%
Cost of sales	(647.5)	(1,761.4)	172.0%
Gross profit	(226.5)	107.8	-147.6%
Other operating expenses	(468.5)	(1,139.8)	143.3%
Operating profit/(loss)	(695.0)	(1,032.0)	48.5%
Net interest received/(paid)	37.5	(89.9)	-339.5%
Headline (loss) before tax	(657.5)	(1,121.9)	70.6%
Provision		(100.0)	n/a
IFRS loss before tax	(657.5)	(1,221.9)	n/a
Tax		524.6	n/a
(Loss) after tax	(657.5)	(697.3)	n/a
Headline loss per share (p)	(0.24)	(0.20)	-18.4%
Ave shares in issue m	273.01	303.90	

*Company*

The provision (which is for the possibility that the defendants in a court case may not reimburse all of ClearDebt's legal costs) is excluded from Headline earnings.

Apart from the ending of "creditors' strike" by an agreement brokered by the Insolvency Service and the British Bankers' Association finalised in February 2008, the main feature of 2007-8 was the acquisition of Abacus, which markets and administers Debt Management Plans ("DMP"s) in July 2007.

This has obvious synergies of which cross-referral is the largest – since many indebted consumers do not understand the options available a majority of those approaching ClearDebt are advised that they would be better suited to a DMP or should re-mortgage or go bankrupt rather than take out an IVA and many approaching Abacus need an IVA rather than a DMP. Since advertising/acquisition of leads is the largest single cost for the debt resolution sector, combining a DMP and an IVA provider significantly improves, while not quite halving, the cost/benefit ratio for advertising.

The more-than-quadrupling of revenue was due to the inclusion of Abacus (that of the insolvency business grew 16%) as was most of the increase in cost of sales and administrative costs and the swing to net interest paid as the group borrowed £1.6m to cover the purchase of Abacus (including associated costs), of which £0.4m had been repaid by end-December 2007.

Following the acquisition first Abacus and then ClearDebt Ltd moved into the group's new offices which inevitably increased extra costs at the time but is expected to yield considerable savings in the current year and future. Both were loss-making during 2007-8 but moved into profit in the first quarter of 2008-9 and rising volumes with low marginal administrative costs should lead to steadily growing profits.

The development of a Partner Programme with mortgage brokers and financial advisers and new product development (including for the oft-delayed SIVA) have also added to the costs and reported losses in 2007-8 but should generate income in future years.

The auditors' decision to recognise a deferred tax asset because they expect the group to earn enough profits this year and the near future to utilise it, although it does flatter the improvement in reported eps to (0.04p) in the second half from (0.16p) in the first, is a confirmation of the turn-round.

The group is now seeking to provide unemployment protection insurance for all those taking out DMPs through Abacus as ClearDebt does for its IVA clients (a rare but admirable case where the creditor, as beneficiary, pays the premium) and a prepaid debit card that clients can use over the internet or where the amount is too large for cash to be convenient without using credit, together with a bill payment and standing order facility.

The future depends marginally more on the group than the environment but the latter remains a critical factor. Although the increase in those losing employment and unable to regain it will push some into bankruptcy rather than DMPs or IVAs, many will have some equity in their houses so an IVA will remain the better option and for those able to regain employment in the foreseeable future a DMP will be suitable; the belated introduction of SIVAs (renamed "Fast-track IVAs") should also help. So demand for the group's products is bound to increase.

In four-and-one-third months to November 11<sup>th</sup> the number of IVAs approved was 38% higher than in the six months to December 2007 and the number of DMPs managed by Abacus had risen by 32% since the end of June.

For both divisions, the growth in the "book" of business (and insurance policies reduce drop-out rates) will gradually lead to substantially higher profits as marketing costs are entirely, and administrative costs are heavily, front-end loaded; continuing cases generate profits from which initial costs can be recouped

Any forecast for 2008-9 remains tentative with the single most significant unknown being just how much the cost of advertising falls, followed by the number of referrals from ClearDebt's Partner programme. I should prefer to say that pre-tax profit should be within the range £0.25m to £1m, but if required to make a central forecast, £0.58m pre-tax leading to earnings per share of 0.15p.

**At Friday's closing price of 0.375p ClearDebt is on a PFER of less than 3x on my central forecast (6.4x at the bottom of the range). As it is one of the few recession-proof companies seeing real growth in its business, this seems to be an exceptional degree of undervaluation.**

I certify that this report represents my own opinions  
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