
NCC Group plc

Interim Results

for the six months ended 30 November 2018

24 January 2019

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Adam Palser
Chief Executive Officer

Tim Kowalski
Chief Financial Officer

Adam Palser
Chief Executive Officer

Adam Palser
Chief Executive Officer

Overview

Financial highlights

- Solid revenue growth at a time of operational transformation
- Assurance revenue grew by double digits; Escrow slightly down
- Gross Margin improved; Adjusted EBIT margin down like-for-like
- Temporary spike in working capital to reverse by year end

Operational highlights

- ✓ Strong growth in the US
- ✓ Encouraging growth in Europe and APAC
- ✓ Continued world-leading capability and research
- x Weaker than expected performance in UK
- Transformation accelerating to create next version of NCC Group

Outlook

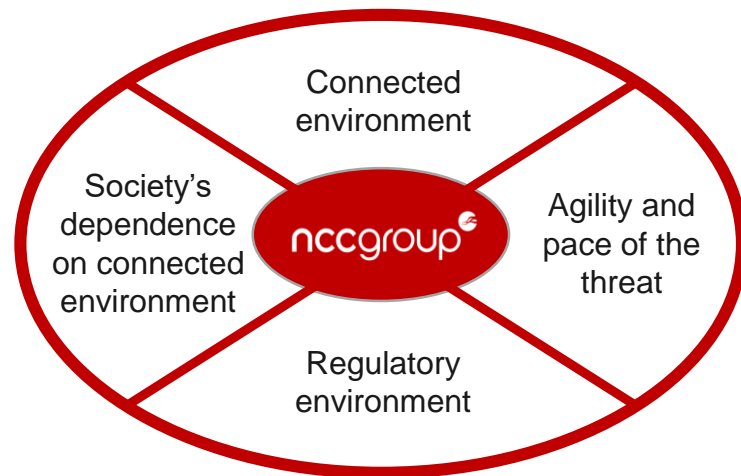
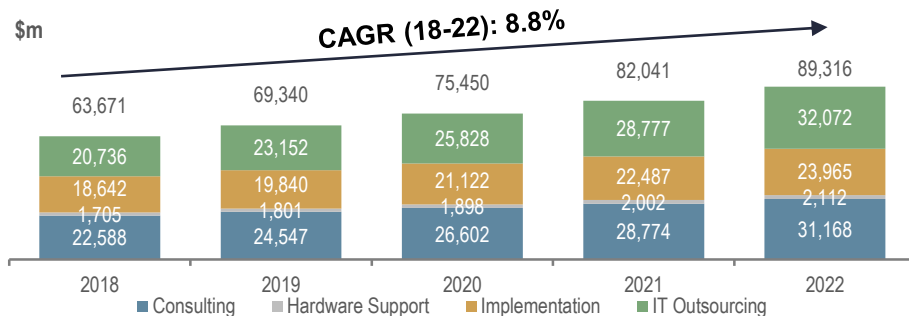
- Following a slower start to H2 in UK Assurance, full-year Adjusted EBIT is expected to be around £34m

Demand continues to grow

Key Themes*	
Increasing demand for managed, hosted and cloud-based security services	30% of organisations expect to increase security services spend to access more skills and capacity <small>FROST & SULLIVAN</small>
SMBs increasingly being targeted by attackers	Most SMBs feel overwhelmed and are unprepared to deal with the magnitude of cybersecurity... Proactive SMBs will increasingly turn to MSSPs for expertise and solutions <small>SMB GROUP</small>
Incremental spending shifting to cloud	We estimate that spending on security for cloud workloads will drive incremental security spend upwards of \$11B in spending by 2020 <small>WALL STREET RESEARCH</small>
Penalties under new regulatory framework increase cost of data breach	GDPR is likely to catalyze a review of firm's security posture across the spectrum – we imagine this review will span governance, control, organization, processes, sourcing, and technology <small>CREDIT SUISSE</small>
Cybersecurity has evolved to a board / CEO level strategic consideration	There are two types of companies: those that have been hacked, and those who don't know they have been hacked <small>JOHN CHAMBERS, EX-CEO CISCO</small>

- Cyber risk services demand growing with increasing threat and consequent impact of historical underspend
- Globally, security services market size to grow to 2022 at CAGR of +8.8%
- “Busy” market challenges include scarcity of competent resources and significant competition from continued investment in the sector

Security Services Enterprise Spending (2018-2022)¹

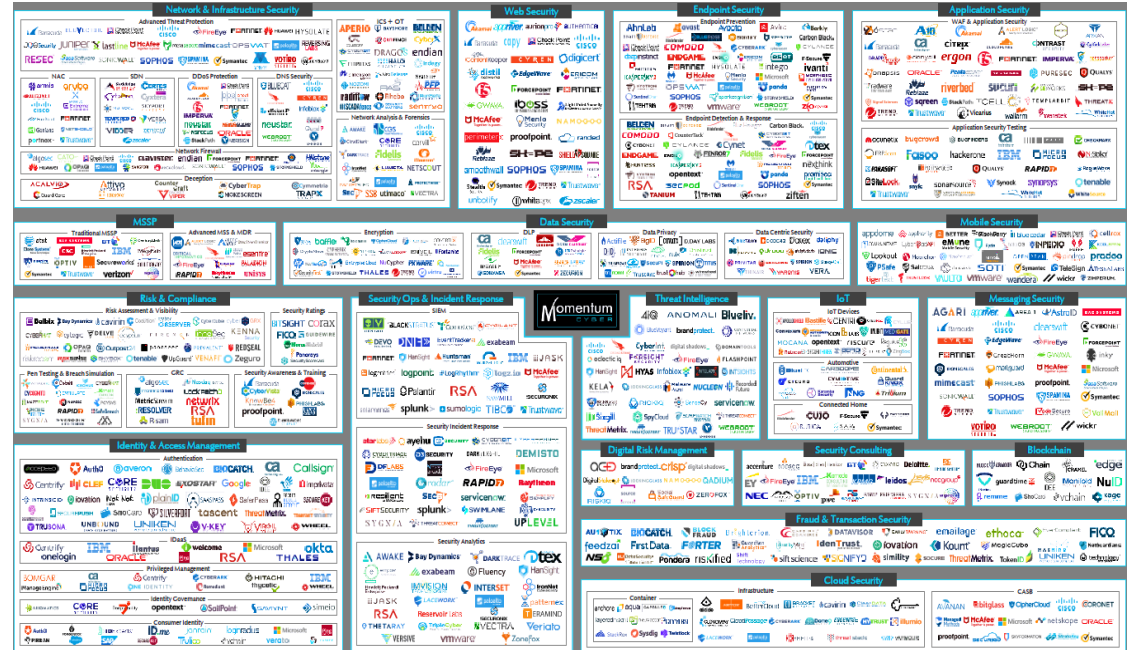


Market dynamics continue to benefit NCC

Source:
* Gartner, Broker reports, Technavio, company filings
1 As per Gartner report. Forecast by constant currency

Cyber landscape

- Busy fragmented market
- Confusing for some clients
- Competition for talent



Source: <https://momentumcyber.com/docs/CYBERScape.pdf>

Our Transformation: Securing Growth Together

The **leading** cyber security advisor globally. Sought-after for our complete **people-led, technology enabled** cyber security solutions that enable individuals, businesses & society to **thrive**. Trusted to protect our customers' **critical assets**

- Low-value transactional business model
- Fragmented organisation
- Weak systems and processes
- Command & Control culture

Securing
Growth
Together

- Higher value relationship sales model
- Unified agile global delivery
- Robust and scalable platform for growth
- Empowerment with measurement

Progress:

- Good momentum in our three year Securing Growth Together transformation since the launch in May 2018 of its five core workstreams (**Lead, Win, Deliver, Support** and **People**)
- Mission, Vision, Strategy and Values have been defined and embedded
- Continued strengthening of the leadership team; new appointments include CFO, MD Assurance UK & APAC, and Interim Chief People Officer
- North America: empowered business; development of higher-value relationships
- Major systems implementation are committed, scoped and under contract
- Engagement across the Group

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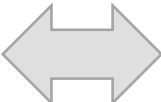


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Financial highlights – continuing operations

 <p>Revenue^{*1} (£m) (H1 2018: £116.8m) £126.0m</p>	 <p>Adjusted EBIT^{*1*2} (£m) (H1 2018: £13.8m) £14.8m</p>	 <p>Operating profit^{*1} (£m) (H1 2018: £6.3m) £9.5m</p>
 <p>Gross Margin% 40.2% (H1 2018: 39.6%) +0.6%pt</p>	 <p>Assurance GM% 34.3% (H1 2018: 32.2%) +2.1%pts</p>	 <p>Escrow GM% 74.1% (H1 2018: 77.1%) -3.0%pts</p>
 <p>Adjusted EBIT Margin % (H1 2018: 12%) 12%</p>	 <p>Cash conversion ratio^{*4} (H1 2018: 72%) 33%</p>	 <p>Net Debt^{*3} (£m) (H1 2018: £44.4m) £45.1m</p>

Growing revenue and profit. Temporary decline in cash conversion

^{*1} References to the Group's results, unless stated to the contrary, are to continuing operations only and exclude the performance of businesses sold or discontinued in the prior year (principally Web Performance and Software Testing).

^{*2} Adjusted EBIT excludes individually significant items, share based payments, unwinding of discounts on deferred consideration and amortisation of acquired intangible assets. This is an Alternative Performance Measure (APM) for which a reconciliation to the equivalent GAAP measure can be found in Note 2 of the RNS.

^{*3} Net debt is defined as total borrowings less cash and cash equivalents. As an APM, it is detailed in Note 2

^{*4} Cash conversion ratio is a measure of how effectively Adjusted operating profit is converted into cash. It is detailed in Note 2

Financial performance: income statement

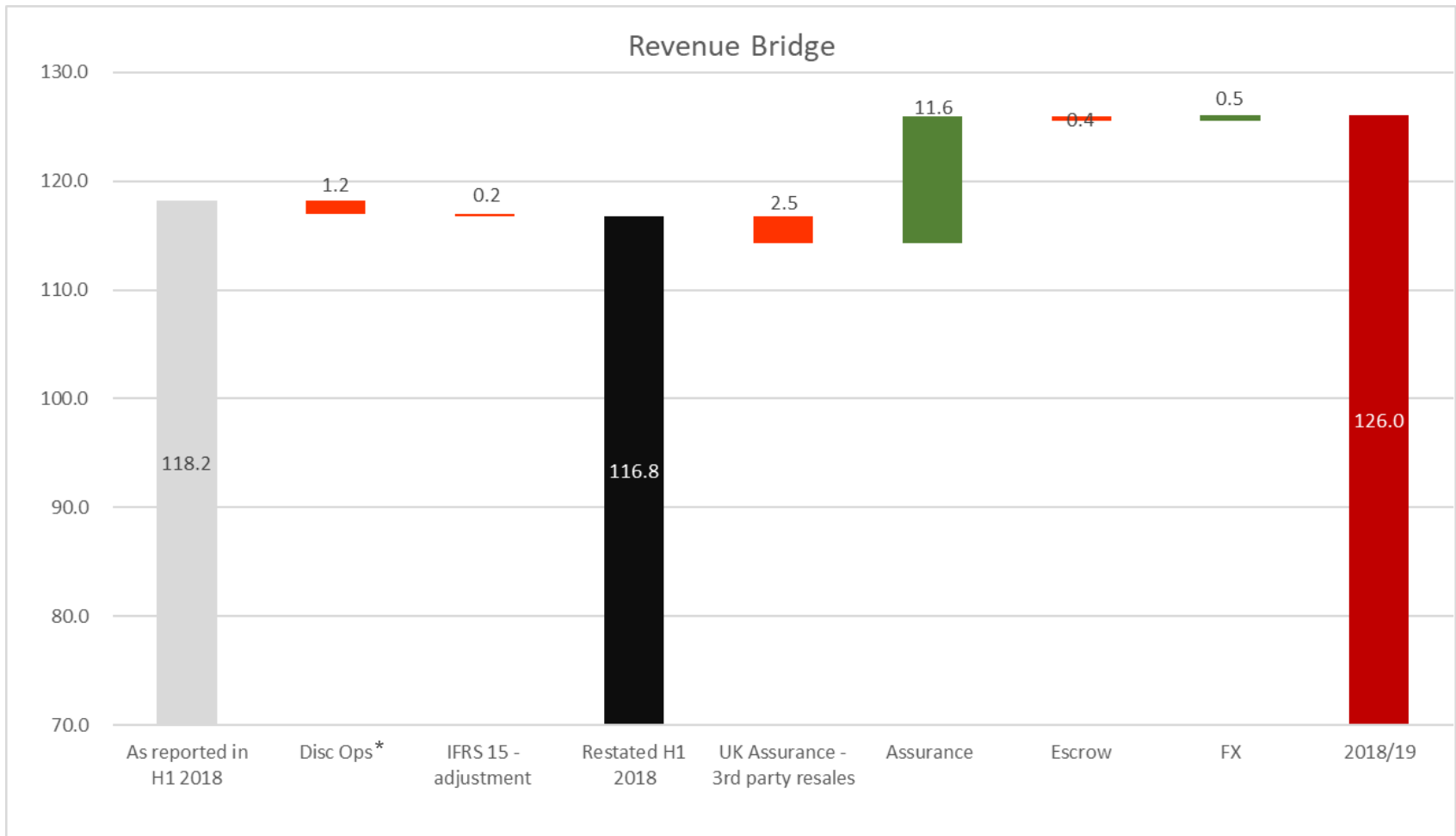
Continuing operations	HY2019 (£m)	HY 2018* (£m)
Revenue	126.0	116.8
Cost of Sales	(75.4)	(70.6)
Gross Margin	50.6	46.2
<i>Gross Margin %</i>	<i>40.2%</i>	<i>39.6%</i>
G&A before adjusting items	(35.8)	(32.4)
Adjusted EBIT	14.8	13.8
<i>Adjusted EBIT Margin %</i>	<i>12%</i>	<i>12%</i>
Adjusting items	(5.3)	(7.5)
Reported EBIT	9.5	6.3
Financing costs	(0.8)	(0.6)
Discount on acquisition consideration	-	(0.2)
Taxation	(1.9)	(2.5)
Profit after tax - discontinued	-	0.8
Profit / (Loss) after tax	6.8	3.8
Adjusted Basic EPS (pence)	3.9p	3.7p

- Strong revenue growth in US for both Assurance and Escrow
- Challenges within UK Assurance and UK Escrow
- GM% growth within Assurance of +2.1%
- G&A cost increases reflect historic under-investment in people
- Adjusted EBIT broadly in line with last year when adjusted for onerous contract for H1 2018 of £1.1m
- Adjusting items lower as Individual Significant Items are net £nil (£2.6m in H1 2018)
- Tax - benefit from US federal rate cut, Adjusted Effective Tax Rate 22.9%

Profits growing year on year

* Restated for the impact of IFRS 15 and prior year discontinued activities

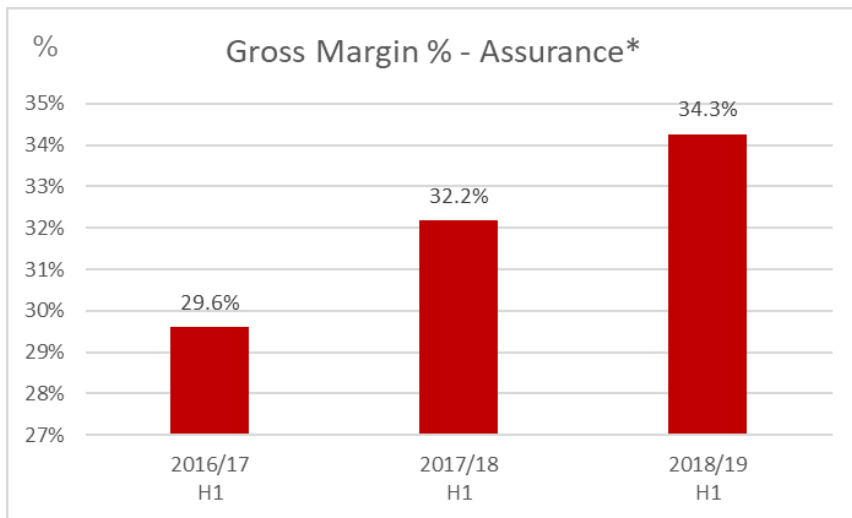
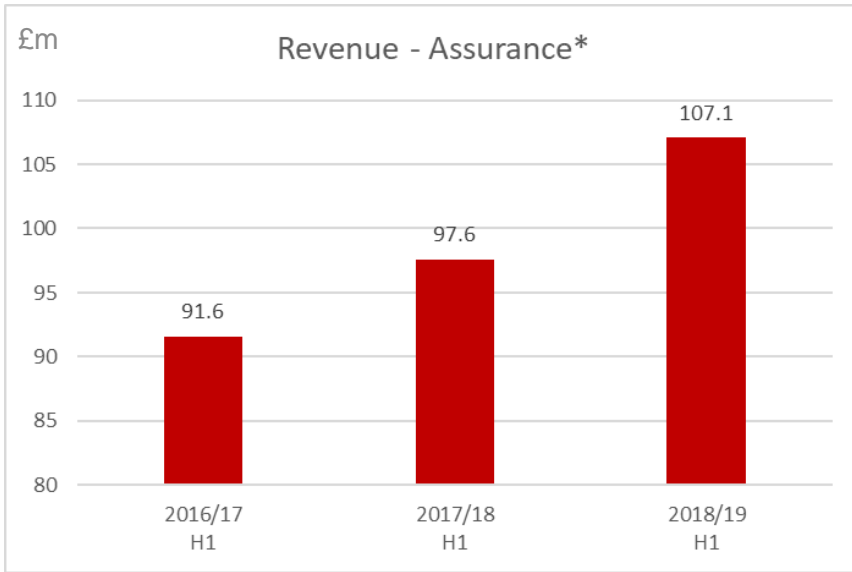
Financial performance: group revenue bridge



Solid growth primarily in Assurance of 9.7%

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Financial performance: Assurance

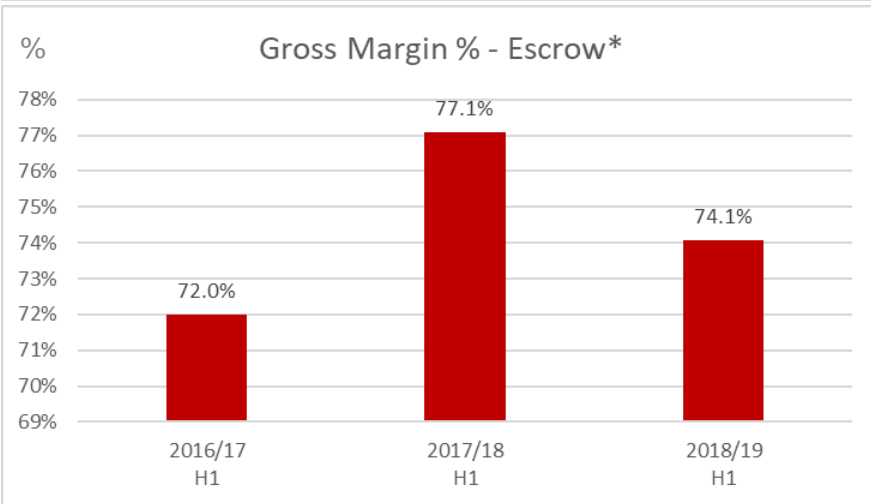
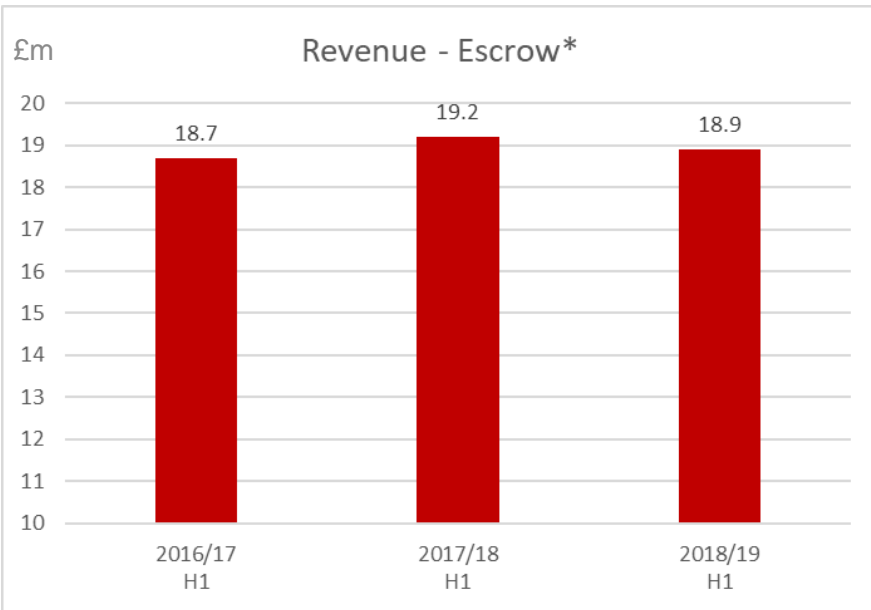


- Sales growth in all territories
 - Particularly strong in US: +20.4%
 - Weaker in UK +1.1% (around +6% excluding reselling)
 - Europe & APAC: +11.8%
- GM% grew by +2.1% pts – combination of mix and utilisation
 - Utilisation of technical consulting increased from 78.7% to 81.9% across combined UK and US
- In the US, earn-out periods for the PSC and VSR acquisitions finished (December 2018) and integration commenced

Assurance*	HY2019	HY2018
Revenue £m	107.1	97.6
Gross profit £m	36.7	31.4
GM%	34.3%	32.2%
Adjusted EBIT £m	10.7	6.4
Adjusted EBIT Margin %	10.0%	6.6%

* H1 2017/18 restated for the impact of IFRS 15 and prior year discontinued activities

Financial performance: Escrow

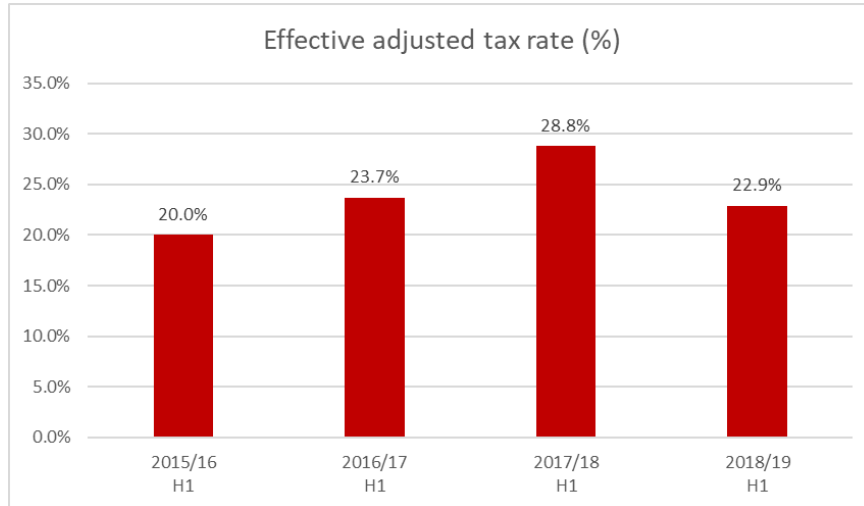


- Good growth in US revenue +10.5% (2018 : -5%) as we increase our presence there
- UK disappointing with revenue contraction of -4.4% as a result of operational challenges
- Decline in new UK on-premise agreements in a mature market largely offset by increasing verification testing
- Renewal rates remain firm at 89% (2018: 89%)
- Global portfolio gives us confidence in ability to return the division to revenue growth
- Gross margin lower as a result of investment in international growth
- EBIT margin lower as result of GM and more prudent bad debt provisioning

Escrow*	HY2019	HY2018
Revenue £m	18.9	19.2
Gross profit £m	14.0	14.8
GM%	74.1%	77.1%
Adjusted EBIT £m	8.8	10.3
Adjusted EBIT Margin %	46.6%	53.6%

* H1 2017/18 restated for the impact of IFRS 15 and prior year discontinued activities

Financial performance: tax and dividends



Tax

- Effective tax rate attributable to adjusted profits and continuing operations is 22.9% (H1 2018: 28.8%)
- Fall in effective tax rate attributable to the decrease in US federal tax rate from 35% to 21%, effective 1 January 2018

Dividends

- HY dividend in line with the prior year

Financial performance: cash flow and net debt

	HY2019 (£m)	HY2018 (£m)
Cash flow before working capital	20.3	18.5
Movement in working capital	(8.7)	(0.7)
Operating cash pre interest / tax	11.6	17.8
Net interest paid	(0.9)	(0.7)
Tax paid	(4.1)	(2.4)
Net cash from operations	6.6	14.7
Acquisitions (net)	(9.9)	(1.0)
Proceeds from sale of subsidiaries	0.1	-
Tangible capex (net)	(1.8)	(6.0)
Software capex	(1.5)	(1.1)
Capitalised development costs	(0.9)	(1.4)
Dividends	(8.7)	(8.7)
Share issue	0.2	1.1
FX	(1.4)	1.7
Change in net debt	(17.3)	(0.7)
Closing net debt	(45.1)	(44.4)

- Temporary increase in working capital
- Acquisitions relates to final deferred consideration for Fox of £9.9m in June 2018
- Tangible capex reduced due to last year's Head Office move
- Software capex includes Securing Growth Together
- FX adverse swing due to the US Dollar rate

Net debt impacted by deferred consideration payment and temporary increase of working capital

Financial performance: working capital

	HY2019 (£m)	HY2018 (£m)
Increase in Trade/other debtors	(4.1)	(1.1)
Decrease in Trade/other creditors	(4.6)	0.4
	(8.7)	(0.7)

Issues		Action
Trade Debtors	<ul style="list-style-type: none"> - Legacy systems hard to use - Credit control team turnover high in last 18 months - Sales team reorganisation 	<ul style="list-style-type: none"> - New Sidetrade system implemented - Improved processes rolled out and taking effect - Now stabilised with proper leadership - Changes in incentive plans
Trade Creditors	<ul style="list-style-type: none"> - Normalising payment terms 	<ul style="list-style-type: none"> - Procurement being professionalised and improved cash culture

Temporary increase in working capital caused by disruption and expected to reverse by year end

Financial performance: Securing Growth Together programme

SGT programme	FY19 (£m)	FY20 (£m)	FY21 (£m)	FY22 (£m)	Total
Operating expense (Opex)	0.8	0.3	0.2	-	1.3
Capital expense (Capex)	4.3	6.7	4.0	2.0	17.0
Total	5.1	7.0	4.2	2.0	18.3
Prior transformation guidance – Opex	(4.0)	(4.0)	npdp*	npdp*	(8.0)
FY18 historical annual software spend – Capex	(2.5)	(2.5)	(2.5)	(2.5)	(10.0)
Net difference - cash	1.4	(0.5)	(1.7)	0.5	(0.3)
Write-offs – non cash	(4.0)	-	-	-	(4.0)
Overall net difference	(2.6)	(0.5)	(1.7)	0.5	(4.3)

- Notable benefits of the programme:
 - Global visibility and coordination of consulting resources
 - Connected and easily accessible MI
 - Improved profitability through decreased indirect costs
 - Write-off to occur in H2 2019

Extra cost of programme is £4.3m - mostly non cash from write-off

* Not publicly disclosed previously

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Appendix I: Half Year

Appendix II: About NCC Group

Assurance

“The leading cyber security advisor globally. Sought-after for our complete **people-led, technology enabled** cyber security solutions that enable individuals, businesses & society to **thrive.**”

Our goal: continued double-digit growth globally, steady margin improvement, improved cash flow

Region	Dynamics	Actioned	Ongoing action
<p>USA</p> <p>Revenue (+20.4%)</p>	<ul style="list-style-type: none"> Major contract wins Penetration of tech market 	<ul style="list-style-type: none"> Embracement of higher value relationship sales Key hires and reorg for an empowered business 	<ul style="list-style-type: none"> Focus on retention and resourcing Continued push to take market share
<p>UK</p> <p>Revenue (+1.1%)</p> <p>(around +6% w/o reselling)</p>	<ul style="list-style-type: none"> Softer demand growth Deliberate £2.5m reduction in 3rd party resales Resource shortages 	<ul style="list-style-type: none"> New MD appointed Mid-cycle reward reset after benchmarking Utilisation in technical consulting 86% (2018: 83%) 	<ul style="list-style-type: none"> Focus on operational performance Extensive recruitment Coaching/development of sales teams/systems Market-facing sectors
<p>Europe/ ROW</p> <p>Revenue (+11.8%)</p>	<ul style="list-style-type: none"> Strong consulting growth in FortConsult and APAC Fox-IT growth lower at +3.4% 	<ul style="list-style-type: none"> Active co-ordination of Europe and APAC opportunities Fox-IT restructured into 3 divisions; new leadership 	<ul style="list-style-type: none"> Fox-IT portfolio development New multi-year strategic partnership signed with Dutch MoD (€4.1m p.a.)

Escrow

“Trusted to protect our customers’ *critical assets*.”

Our goal: to return Escrow to confident growth (> GDP growth)

Region	Dynamics	Actioned	Ongoing action
UK Revenue (-4.4%) GM = 75%	<ul style="list-style-type: none">• Sales team churn• Smaller sales team• Dependence on on-premise software base	<ul style="list-style-type: none">• Initial operational review completed• Focus to stabilise sales team• Initial cloud sales achieved	<ul style="list-style-type: none">• Investment to boost sales team• Launch of refined cloud offering expected by FY end
USA Revenue (+10.5%) GM = 67%	<ul style="list-style-type: none">• Encouraging initial return from our investment in sales capacity and staff	<ul style="list-style-type: none">• Transfer of senior management to US• Sales recruitment	<ul style="list-style-type: none">• Continued investment in sales and push to take market share
EU/ ROW Revenue (-5.3%) GM = 83%	<ul style="list-style-type: none">• Good progress in Netherlands• Challenges in Germany and Switzerland	<ul style="list-style-type: none">• Europe lead appointed• Active recruitment across the European regions	<ul style="list-style-type: none">• Continued investment in sales and push to take market share

Our transformation

Lead the Market

- Lead the market through our thought leadership, industry content and research
- Promote NCC Group as employer of choice

Win Business

- Increase the quality and quantity of orders through better client relationships
- Value selling; sales skills development

Deliver Excellence

- Leverage global delivery capability/capacity
- Consistent ways of working: “one firm, one way” single planning and delivery management system for HR and Finance

Support Growth

- Unified core processes and systems to better leverage our data
- Discipline in process with accurate and timely MI

Develop Our People

- Commitment to single mission, vision and set of values
- Attract, nurture and retain talent; promote technical and commercial excellence
- Leadership development programme / graduate & apprentice scheme

Unified systems (48 to 10)

New			Marketing Automation								
Old	 	 									

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Summary and outlook

Summary

- Excellent US performance in our core markets of cyber security and risk
- Weaker than expected UK growth
- Accelerating transformation programme towards unified global business

Outlook

- Grow Assurance revenue at double digits
- Generate growth in Escrow this year and confident growth (>GDP) in future years
- To grow Adjusted EBIT margin by 2%pts in aggregate by the end of FY21
- Full year Adjusted EBIT expected to be around £34m

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Financial performance: individually significant items (“ISI’s”)

Charges (continuing operations)	HY2019 (£m)	HY2018 (£m)
Deferred/contingent consideration	-	(0.6)
Restructuring costs	-	(1.1)
Property relocation costs	-	(0.7)
Market related/acquisition costs	-	(0.2)
Total	-	(2.6)

- HY2019 is £nil albeit adjustments to deferred and contingent consideration were in respect of FX movements and legal fees offset by a reduction in the estimate of contingent consideration payable

ISI's are net £nil

Financial performance: balance sheet

	HY2019 (£m)	HY2018 (£m)
Intangible assets	239.3	247.8
PPE	18.1	20.3
Investments	0.3	0.4
Net assets in business for sale	-	10.7
Inventory	0.8	0.7
Trade and other debtors	73.8	63.0
Trade creditors and Deferred income	(64.5)	(59.1)
Net working capital	10.1	4.6
Tax receivable / (payable)	0.3	(3.7)
Provisions	(8.3)	(6.2)
Net deferred tax liabilities	(4.5)	(9.1)
Deferred/contingent consideration	(1.7)	(13.9)
Net debt	(45.1)	(44.4)
Net assets	208.5	206.5

- Fall in intangibles mainly from amortisation charges of £6.7m offset by additions of £2.4m
- Net working capital increase from short term increase in debtor levels plus lower level of trade payables referred to earlier
- Provisions increase from onerous leases and loss making contract made at FY 2018
- Fox final deferred payment £9.9m paid during period. Expect to pay final PSC and VSR contingent consideration in full FY 2019
- Deferred tax liability fall driven by cut in US Federal tax rate

Financial performance: non-GAAP reconciliation

non-GAAP reconciliation*	HY2019 (£m)	HY2018 (£m)
Adjusted EBITDA	20.0	19.6
Depreciation of tangibles	(3.0)	(3.0)
Amortisation of intangibles	(2.2)	(2.8)
Adjusted EBIT	14.8	13.8
Share based payments	(0.9)	-
Amortisation acquired intangibles	(4.5)	(4.9)
Profit on sale of subsidiaries	0.1	-
Individually significant items	-	(2.6)
Reported EBIT	9.5	6.3

* Restated for the impact of IFRS 15 and prior year discontinued activities

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