EML Payments Ltd: Don't Buy

ASX:EML

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Date of Analysis: 5/3/2020. Idea source: Small cap, Stock screener, (more than 50M shares). Analysis date price: AUD2.65.

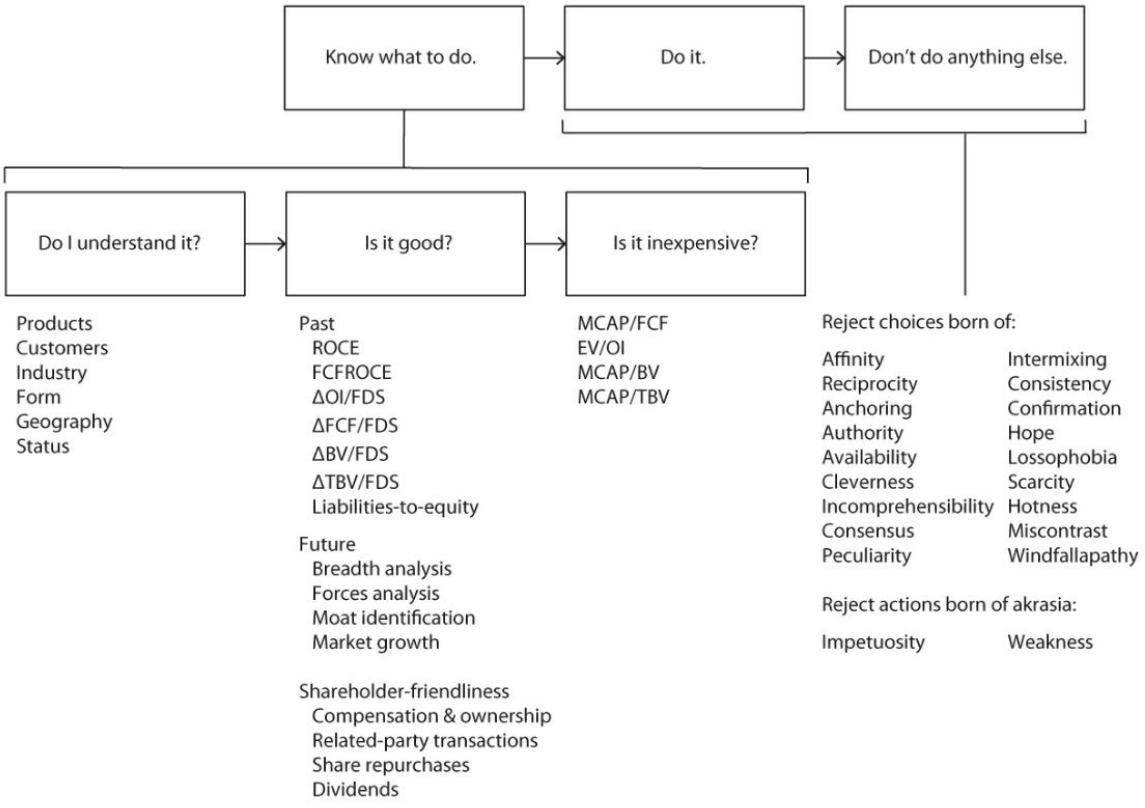
Framework outcomes

Good Stocks Cheap: The price needs to drop -86% to AUD0.36 in order to be cheap.

Growth With Value: The price is cheap and, remaining so, can still move up 271% to AUD9.83.

Contents

Framework



Marshall (2017), p. 188.

Do I Understand It? Yes:

Understanding Statement

Consumer Financial Services industry corporation EML Payments manages tailored gift card solutions for businesses around the world such as betting agencies, merchant coalitions and retailers and, despite H1 sales being up 25%, have suspended guidance due to the plague and have been regularly acquiring similar businesses.

Is it Good? No, poor past performance:

To determine if EML Payments Ltd is good, it was analysed from three perspectives:

1. Past performance, to see if they've been good stewards of their capital.
2. If the company's future is bright, considering breadth, forces, monopolies and market.
3. If the company is shareholder friendly, such as whether leaders behave like owners.

1. Does EML Payments Ltd Have Good Average Past Performance? No:

Judgement of past performance is based on averages over the past however many periods the analyst chooses to input. Table of averages:

Summary	Benchmark	Average
ROCE with cash, end of period	Should be at least 15%	-1.38%
ROCE without cash, end of period	Should be at least 15%	-1.51%
FCFROCE end of period, with cash	Should be at least 8%	4.03%
FCFROCE end of period, without cash	Should be at least 8%	4.99%
Δ OI/FDS	Should keep up with inflation, aim for 4%	56.44%
Δ FCF/FDS	Should keep up with inflation, aim for 4%	266.28%
Δ BV/FDS	Should keep up with inflation, aim for 4%	15.17%
Δ TBV/FDS	Should keep up with inflation, aim for 4%	16.96%
L/E	Should be no higher than 2, 7 if otherwise great.	230.52%

Was the performance in the most recent period good? No. Further detail by year is available in the next table.

Category	Item	Average	2019	2018	2017	2016	2015	Benchmark
Past performance	OIROCE, cash, beginning	1.0%	5.0%	3.4%	-1.5%	-2.8%		Should be at least 15%
Past performance	OIROCE, cash, end	1.4%	6.1%	4.5%	-1.9%	-3.0%		Should be at least 15%
Past performance	OIROCE, no cash, beginning	-1.4%	2.5%	2.6%	-1.3%	-1.2%	-9.4%	Should be at least 15%
Past performance	OIROCE, no cash, end	-1.5%	2.7%	3.1%	-1.7%	-1.5%	-10.1%	Should be at least 15%
Past performance	FCFROCE, cash, beginning	7.9%	12.8%	3.1%	12.6%	3.2%		Should be at least 8%
Past performance	FCFROCE, cash, end	4.0%	6.3%	2.3%	10.8%	1.4%	-0.7%	Should be at least 8%
Past performance	FCFROCE, no cash, beginning	9.7%	15.6%	4.0%	15.6%	3.4%		Should be at least 8%
Past performance	FCFROCE, no cash, end	5.0%	6.8%	2.8%	14.3%	1.7%	-0.7%	Should be at least 8%
Past performance	Δ OI/FDS	56.4%	90.1%	360.1%	4.2%	74.6%		Should keep up with inflation, aim for 4%
Past performance	Δ FCF/FDS	266.3%	445.4%	-72.2%	611.0%	506.4%		Should keep up with inflation, aim for 4%
Past performance	Δ BV/FDS	15.2%	8.3%	6.3%	-20.0%	91.0%		Should keep up with inflation, aim for 4%
Past performance	Δ TBV/FDS	17.0%	-39.6%	4.6%	0.0%	196.1%		Should keep up with inflation, aim for 4%
Past performance	L/E	N/A	231%	N/A	N/A	N/A	N/A	Should be no higher than 200%, 700% if otherwise great.
Shareholder friendli	Highest paid employee salary	N/A	#N/A					For US companies, should be less than $USD30,000,000
Shareholder friendli	Highest paid employee salary c	N/A	#N/A					Should be 5% of the lower of FCF or NI
Shareholder friendli	Highest paid outside director	N/A	#N/A					For US companies, preferably less than $USD250,000 and not more than $USD500,000
Inexpensiveness	MCAP/FCF	N/A	24.696					Should be no higher than 8
Inexpensiveness	EV/OI with cash and cash equiv	N/A	64.561					Should be no higher than 7, sell if >25
Inexpensiveness	EV/OI without cash and cash ec	N/A	61.523					Should be no higher than 7, sell if >25
Inexpensiveness	MCAP/BV	N/A	4.771					Should be no higher than 3
Inexpensiveness	MCAP/TBV	N/A	17.343					Should be no higher than 3

Is it Cheap? Maybe:

Analysis date price: AUD2.65, cheap price: AUD0.36. The price needs to drop -86% to AUD0.36 in order to be cheap.

Summary	As at 5/3/2020	Benchmark
MCAP/FCF	24.70	Should be no higher than 8
EP/OI - cash	61.52	Should be no higher than 7, sell if >25
EP/OI + cash	64.56	
MCAP/BV	4.77	Should be no higher than 3
MCAP/TBV	17.34	Should be no higher than 3

Discount Cash Flow Analysis

A discount cash flow analysis (DCF) is mentioned as a common method in How to Value a Business (Cowley, 2019). The below DCF has High Growth Period and Terminal or Stable Growth Period segments. The intrinsic values of each are summed to calculate the share price of the company that is warranted by the anticipated future cash flow, based on the geometric mean of its growth rate. A comparison between this price and the current price is another way to see how cheap the business is currently. For further details on what the below terms and numbers mean, consult Cowley (2019).

High Growth Period

Table 1. Parameters.

Parameter	Value
Investors required return or discount rate	12%
Continuing number of years	4
Arithmetic mean of ending free cashflow	0.04 per share
Compound annual growth rate of same	130%

Table 2. Cashflow for high growth period.

Year into the future	Cash flow per share	Intrinsic value
1	0.09	0.08
2	0.22	0.17
3	0.50	0.36
4	1.15	0.73

Terminal or Stable Growth Period

Table 1. Parameters.

Parameter	Value
Investors required return or discount rate	12%
Constant growth rate for stable period	5%
Cashflow from the last year of high growth	1.15 per share
Starting year of stable growth	5

Table 2. Cashflow for terminal or stable growth period.

From year	Cash flow per share	Intrinsic value
5	1.21	10.94

Table 3. Intrinsic value of the business.

Parameter	Value
Intrinsic value of the business	AUD12.29 per share
Share price at 5/3/2020	AUD2.65
Margin of safety	20%
Margin of safety status	The price is cheap and, remaining so, can still move up 271% to AUD9.83.

From this calculation we can see that, from the perspective of future cashflows, the intrinsic value of the business supports a price of AUD12.29 per share. Note that this is only true if the following assumptions are correct:

1. The business grows for the next 4 years at a high rate of 130% per year.
2. The business grows perpetually thereafter at a rate of 5% per year.

The margin of safety should guide buying decisions in case these assumptions are wrong.

Verdict: Don't Buy, Checklist:

Sl	Item	Sub Item	Check
1	**Do I understand it?**		**Yes.**
2	**Is it good?**		**No, poor past performance.**
2.1		**Has there been good past performance?**	**No.**
2.2		**Is the future bright?**	**#N/A.**
2.2.1		Is it broad with respect to customers and suppliers?	#N/A.
2.2.2		Is there, at most, one strong force?	#N/A.
2.2.3		Is there a monopoly?	#N/A.
2.2.4		Is the market growing?	#N/A.
2.3		**Is it shareholder friendly?**	**#N/A.**
2.3.1		On the numbers, is it shareholder friendly?	#N/A.
2.3.2		Overall, is it shareholder friendly?	#N/A.
3	**Is it cheap?**		**Maybe.**
3.2	Is it cheap according to Good Stocks Cheap?		No
3.2	Is the price below the margin of safety from a DCF intrinsic value analysis?		Yes.

References

1. EML Payments Ltd material: https://www.marketindex.com.au/asx/eml.
2. Wil's Value Investing Tool.
3. Cowley, Alistair (2019). How to Value a Business. Accessed 2020-03-09: https://growthwithvalue.com/intrinsic-value-ebook/.
4. Marshall, Kenneth Jeffrey (2017). Good Stocks Cheap: Value Investing with Confidence for a Lifetime of Stock Market Outperformance. McGraw-Hill Education. Kindle Edition.