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12 October 2018

Phil Oakley's Weekly Round-Up

This week I ask whether all potential good news is priced in for Bioventix and examine the outlook for Vertu Motors. I also explain why I like the business models at Hollywood Bowl and Greggs, and assess Marston's ability to manage its debts.

Alpha Production Editor: Sameera Hai Baig

The companies mentioned this week are:
- Bioventix
- Vertu Motors
- Hollywood Bowl
- Greggs
- Marston's
- Patisserie Valerie

Bioventix

I'll say this straight away: I think **Bioventix (BVXP)** is a really good business.

The company makes and supplies sheep antibodies for use in blood testing machines. These machines are supplied to hospitals and healthcare facilities across the world by big international companies such as Siemens and Roche. The antibodies are used in a variety of medical diagnostic tests in areas such as vitamin D deficiency, thyroid problems and heart problems.

Bioventix makes money from two main sources. It sells antibodies to customers (around 10 grammes per year with a list price of $550 per mg) but the bulk of its revenues (about 70 per cent) comes from royalty payments. These payments are received when its customers sell diagnostic products based on Bioventix's antibodies.

Bioventix has been very successful in recent years and is an extremely profitable business – one of the most profitable businesses listed on the stock exchange. Its products and revenues are generated by a team of just 12 scientists working in a laboratory in Farnham, Surrey, although the company does have partnerships with other companies in developing new antibodies.

The fact that the company has a fixed cost base and very little need to invest in any fixed assets means that the scal-

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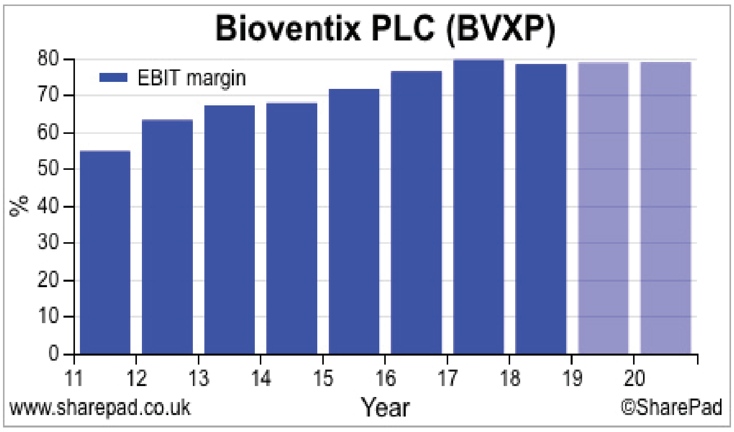
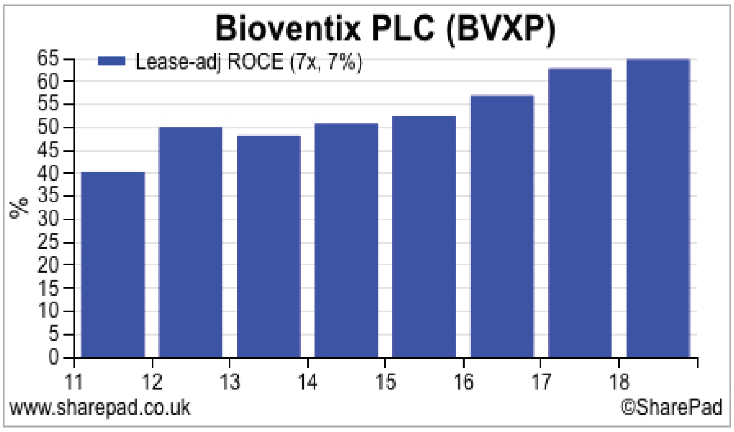
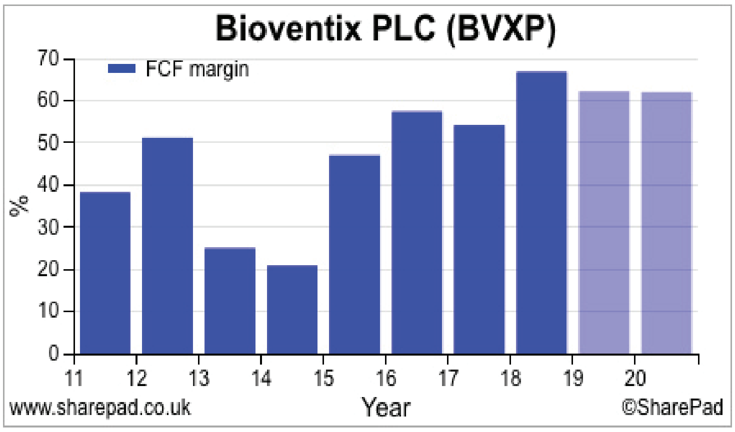
ing up of revenues over the years has made it extremely profitable and cash-generative.







One of the main advantages Bioventix has is that its customers tend to keep using its antibodies once they have started working with them as long as the product is still doing what they want it to do. This gives rise to reasonably reliable income streams that can be viewed as being very valuable from an investor's point of view.

The company is also very open and honest about what its products are capable of delivering in the future. It has the admirable quality of having under-promised and over-delivered to its investors.

The year to June 2018 has been another good one, with underlying revenues (excluding a back dated royalty payment) up by just over 10 per cent and trading profits (again excluding the back dated royalty payment which I have assumed to be pure profit) was up by 6 per cent.

Bioventix revenues by product (£m)	2018	change
Vitamin D	3.4	23%
NtProBNp	1.05	72%
Testosterone	0.66	15%
Drug testing	0.64	32%
T3	0.46	9%
Progesterone	0.4	125%
Estradiol	0.29	13%

Source: Company report

Revenues are dominated by vitamin D antibodies which saw unexpectedly good growth. This growth is likely to moderate in 2018/19 as the company believes that the market for this product has plateaued, although it should still see some growth as smaller customers launch new products.

The key issues with Bioventix are how can it keep on growing and how vulnerable is it to competition? Growing is not easy as it takes between four and 10 years from starting work on a new antibody for it to turn into revenues if the research creates a commercially viable new product.

A lot of hope for growth is being placed on the troponin antibody that can be used to detect whether someone has had a heart attack. The company has an exclusive agreement with Siemens and remains hopeful that significant revenues will materialise, despite last year's sales being small and lower than expected.

The company also has research projects for new antibodies to help detect other heart problems and dementia.

It seems that some investors have been spooked somewhat by Bioventix's reference to a competitor on troponin in its results statement and this could reduce expectations for sales:

"One of Siemens competitors, Beckman Coulter also offers a new high sensitivity troponin assay. It is known through access to FDA data that this new assay also features a sheep monoclonal antibody"

The antibody concerned was developed by a Bioventix licensee so it will get some future revenue from it.

The company also mentioned the competitive threat from rabbit antibodies, which could reduce future opportunities for sheep antibodies. There is also a lesser threat from synthetic antibodies. Time will tell whether these competitive threats materialise, but perhaps they are a

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reminder to bulls of the company who may believe it to be immune from competition.

Despite decent results, an increased dividend and a special dividend, Bioventix shares have sold off by 13 per cent so far this week (I am writing this on Wednesday afternoon). Some of this will be due to the sell-off in expensive shares across the market in general, but perhaps some investors are thinking a bit more deeply about the company's competitive position and growth prospects.

Troponin should give the company a decent source of growth, which will offset the decline in revenue from the very profitable NtProBNP (a heart failure antibody) in 2021. Analysts still expect the company to keep on growing modestly in 2019 before a step up in growth in 2020 – presumably when meaningful troponin sales kick in.

There's a lot to like about this business, but even after the sell-off in the shares a lot of good news appears to be priced into its shares which, at 2800p, still trade on a one-year forecast rolling PE of 24 times. Much of the company's ongoing research is not expected to produce any meaningful revenues until 2022-30.

Bioventix PLC (BVXP)

FORECASTS — £ millions unless stated

Year	2019		2020	
Turnover	9.0	+2.8%	10.0	+11.1%
EBITDA	7.1	+2.5%	8.0	+12.7%
EBIT	7.1	+3.4%	7.9	+11.3%
Pre-tax profit	7.1	+3.4%	7.9	+11.3%
Post-tax profit	5.9	+4.2%	6.6	+11.9%
EPS (p)	112.4	+3.8%	126.7	+12.7%
Dividend (p)	73.0	+19.7%	87.0	+19.2%
CAPEX	-		-	
Free cash flow	5.6	-4.2%	6.2	+10.7%
Net borrowing	-6.4		-8.6	

Source: Sharepad

Vertu Motors

The share prices of the UK's quoted motor dealerships have been depressed for a while now as the sector has had to cope with many challenges. These range from the increased cost of imported cars, a decline in the demand for diesel cars and changes to emissions legislations. Then there is the backdrop of the credit fuelled new car-buying binge that can sometimes give the impression that everyone can own a new car. This, in my opinion, cannot last.

The thing is, in terms of profitability, selling new cars has never been the be-all and end-all for car dealerships. Yes, the long-term sustainability of their businesses requires a stable and growing car parc, but new cars have always been sold on low profit margins. The real money is made in servicing and spare parts and also the selling of used cars. The table below, showing the gross profit margins of **Vertu Motors (VTU)** by business area, highlights this.

CONDENSED CONSOLIDATED BALANCE SHEET (UNAUDITED)

As at 31 August 2018

	Note	31 August 2018 £'000	31 August 2017 £'000	28 February 2018 £'000
Non-current assets				
Goodwill and other indefinite life assets	11	105,564	94,595	94,381
Other intangible assets		1,086	1,504	1,316
Retirement benefit asset	8	6,887	5,704	6,551
Property, plant and equipment		218,798	190,468	198,004
Derivative financial instruments		63	-	-
		332,398	**292,271**	**300,252**
Current assets				
Inventories		507,662	502,585	558,386
Trade and other receivables		46,698	63,007	66,272
Cash and cash equivalents		46,912	44,158	41,709
		601,272	**609,750**	**666,367**
Property assets held for sale		1,079	-	2,449
Total current assets		**602,351**	**609,750**	668,816
Total assets		**934,749**	**902,021**	**969,068**
Current liabilities				
Trade and other payables		(582,343)	(592,050)	(663,404)
Deferred consideration		(1,500)	(1,540)	-
Current tax liabilities		(5,436)	(5,632)	(3,304)
Borrowings		(19,153)	(13,597)	(12,811)
Total current liabilities		**(608,432)**	**(612,819)**	**(679,519)**
Non-current liabilities				
Borrowings		(36,426)	(9,794)	(9,585)
Derivative financial instruments		(63)	-	(92)
Deferred consideration		(100)	(267)	(100)
Deferred income tax liabilities		(7,069)	(6,267)	(6,477)
Deferred income		(9,507)	(8,254)	(8,877)
		(53,165)	**(24,582)**	**(25,131)**
Total liabilities		**(661,597)**	**(637,401)**	**(704,650)**
Net assets		**273,152**	**264,620**	**264,418**

Source: Company report

Vertu has not done too badly during the first six months of its trading year despite the headwinds in the sector.

	2018 Core	2018 Acquired[4]	2018 Total	2017 Total[5]	2017 Core	Total % Variance	Like-for-like % Variance
Used retail vehicles	**43,249**	**574**	**43,823**	**41,599**	**40,864**	**5.3%**	**5.8%**
New retail cars	19,756	152	19,908	19,069	18,684	4.4%	5.7%
Motability cars	5,228	93	5,321	5,747	5,577	(7.4%)	(6.3%)
Fleet and commercial vehicles	17,117	264	17,381	17,690	17,619	(1.7%)	(2.8%)
Total New vehicles	**42,101**	**509**	**42,610**	**42,506**	**41,880**	**0.2%**	**0.5%**
Total vehicles	**85,350**	**1,083**	**86,433**	**84,105**	**82,744**	**2.8%**	**3.1%**

Source: Company report

It has sold more new and used cars and has made more money – expressed in gross profit – from doing so. Its more profitable aftersales business also made more money, albeit at the expense of a slightly lower profit margin.

However, despite this and the impact of an acquisition, higher operating costs meant that operating profits fell slightly from £21.4m to £19.4m. Profit margins remained wafer thin at 1.2 per cent, compared with 1.5 per cent last year. These margins can disappear very quickly in a recession and show why these kinds of businesses are very risky investments. This, in turn, explains why the stock market does not value car dealers at a very high multiple of their profits.

Car dealerships are quite capital-intensive and tend to have substantial property value tied up in their showrooms and workshops. Vertu is no exception here with a property, plant and equipment value of £218.8m at the end of August. This compares with a current market capitalisation for the company of £144.9m at the time of writing.

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Source: Company report

Inventory levels of cars also need to be watched as they represent a major risk to profits if the company has too many and has to slash prices in order to sell them. Vertu has controlled its stock levels well and reduced them by more than £50m since the end of February. Most of these stocks are financed by credit as highlighted by the large trade payables number on the balance sheet.

Turning stock into cash in a profitable way is the order of the day and Vertu has done a good job in the first half of the year compared with last year due to a minimal increase in working capital. This has seen a big improvement in cash generation, which is good to see.

Investment in new assets remains quite high, but has peaked and should start falling in the coming year. As long as operating cash flows are not reduced by working capital, this should see a meaningful increase in the amount of free cash flow generated by Vertu.

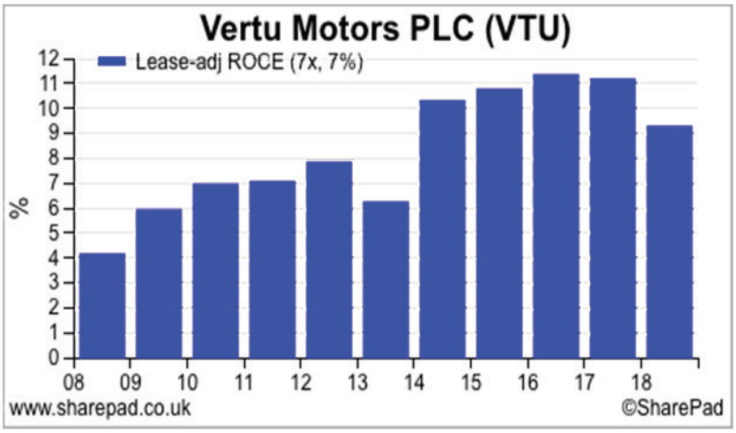
CONDENSED CONSOLIDATED CASH FLOW STATEMENT (UNAUDITED)

For the six months ended 31 August 2018

	Note	Six months ended 31 August 2018 £'000	Six months ended 31 August 2017 £'000	Year ended 28 February 2018 £'000
Operating profit		18,648	24,694	32,345
Profit on sale of property, plant and equipment		(564)	(4,149)	(3,529)
Amortisation of intangible assets		275	313	614
Depreciation of property, plant and equipment		5,515	4,726	9,714
Impairment charges		-	-	512
Movement in working capital	10	552	(24,393)	(13,332)
Share based payments charge		429	497	954
Cash generated from operations		**24,855**	**1,688**	**27,279**
Tax received		69	344	350
Tax paid		(2,336)	(3,079)	(6,468)
Finance income received		46	42	14
Finance costs paid		(1,605)	(823)	(2,321)
Net cash inflow/(outflow) from operating activities		**21,029**	**(1,828)**	**18,854**
Cash flows from investing activities				
Acquisition of businesses, net of cash, overdrafts and borrowings acquired		(23,739)	-	(1,181)
Acquisition of freehold land and buildings		(8,982)	-	(4,346)
Proceeds from disposal of business (net of cash, overdrafts and borrowings)		-	167	1,528
Purchases of intangible assets		(44)	(301)	(411)
Purchases of property, plant and equipment		(13,516)	(8,031)	(19,802)
Proceeds from sale and leaseback transactions		-	14,150	14,150
Proceeds from disposal of property, plant and equipment		3,285	-	165
Net cash (outflow)/inflow from investing activities		**(42,996)**	**5,985**	**(9,897)**
Cash flows from financing activities				
Proceeds from borrowings	7	33,342	4,926	4,140
Repayment of borrowings	7	-	-	(166)
Sale of treasury shares		49	-	62
Repurchase of own shares		(2,634)	(1,212)	(5,451)
Dividends paid to equity shareholders		(3,587)	(3,558)	(5,678)
Net cash inflow/(outflow) from financing activities		**27,170**	**156**	**(7,093)**

Source: Company report

Vertu is doing reasonably well in a tough market and is taking market share, but I still find it difficult to like the shares despite how depressed they look. This is a low margin, low ROCE, cyclical business that faces a hard time delivering meaningful organic growth in my opinion.



Based on current forecasts, the shares trade on a one-year forecast rolling PE of 7.7 times at a share price of 38.35p, whilst offering a reasonable prospective dividend yield of 4.2 per cent.

Vertu Motors PLC (VTU)

FORECASTS £ millions unless stated

Year	2019		2020		2021	
Turnover	2,776.9	-0.7%	2,720.0	-2.0%	2,713.5	-0.2%
EBITDA	34.1	-13.9%	38.5	+12.9%	40.7	+5.7%
EBIT	24.6	-16.0%	28.8	+17.1%	30.6	+6.3%
Pre-tax profit	22.1	-19.1%	26.3	+19.0%	28.0	+6.5%
Post-tax profit	22.1	-1.1%	26.3	+19.0%	28.0	+6.5%
EPS (p)	4.4	-21.4%	5.3	+20.5%	5.6	+5.7%
Dividend (p)	1.6	+6.7%	1.7	+6.3%	1.8	+5.9%
CAPEX	39.4	+60.4%	15.5	-60.7%	15.5	0.0%
Free cash flow	-10.6		18.6		19.6	+5.4%
Net borrowing	26.3		20.1	-23.6%	11.2	-44.3%

Source: Sharepad

There is an argument for saying this is an undervalued company based on its property backed balance sheet, but at the end of the day it is profits growth that is needed to get the shares moving again.

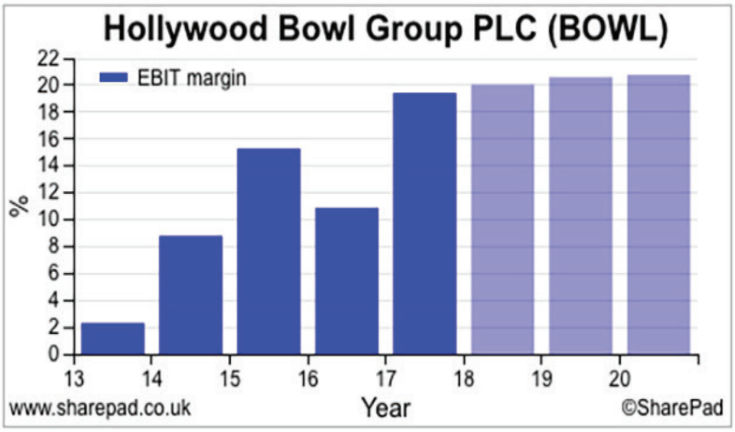
New car profit margins are expected to fall further as the cost of importing them increases. Price increases and long lead times for new petrol models won't help this market in the short-term either. I also remain highly sceptical of the credit driven nature of both the used and new car markets, but think that used cars could do relatively well as existing three-year personal contract plans (PCPs) expire and some consumers buy used instead of new.

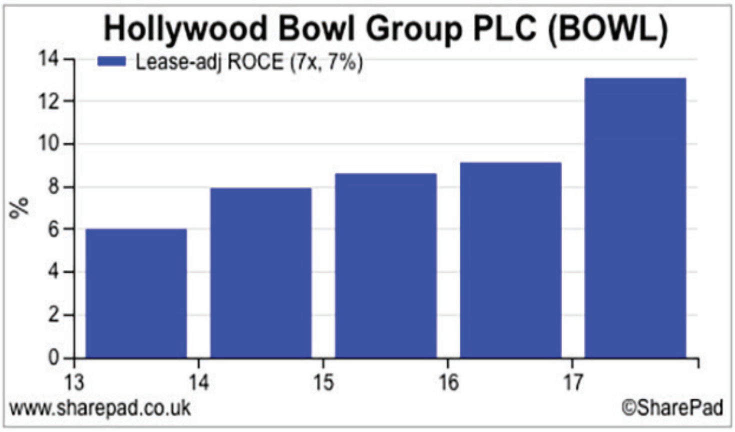
Strong sales of new cars in recent years should support revenues of the after-sales servicing business, but this is a slow burn. Costs remain a concern in this area, as mechanics are spending an increasing amount of time on diagnosing technical problems, which is less efficient and less profitable than regular maintenance jobs. Overheads in the dealerships look too high and are weighing on profits.

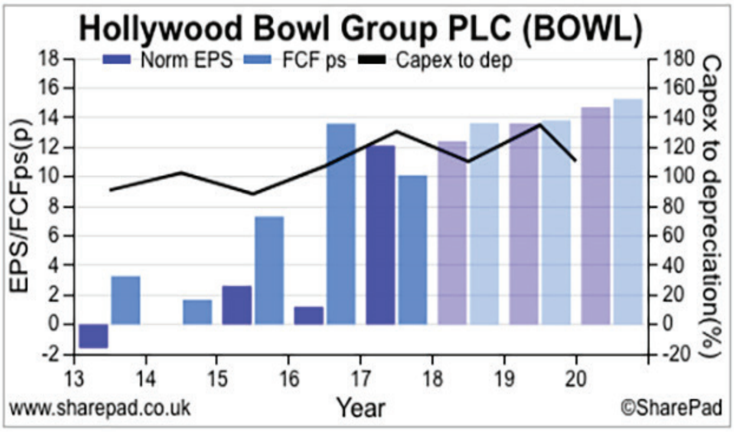
Hollywood Bowl

It's easy to dismiss 10-pin bowling as an outdated leisure activity in an age of digital home entertainment. **Hollywood Bowl (BOWL)** has proven that it is not. It has followed a very sensible strategy of making its bowling centres nicer places to visit, whilst keeping the experience affordable and good value for money.

A focus on prime locations with good footfall – often near cinemas – whilst avoiding opening up too many new locations is paying off. The company has been improving profit margins, ROCE and cash flows in recent years and still offers more room for improvement in my view.







The business is very seasonal and makes most of its money between September and March when the weather doesn't tend to be very good. It also has a lot of fixed costs, which means that sales growth leads to decent growth in profits.

The company's refurbishment plan has paid off handsomely in recent years and has driven four years of consecutive like-for-like sales growth. The rate of LFL sales growth slowed from 3.5 per cent last year to 1.8 per cent for the year that has just ended. Overall sales growth of 5.8 per cent has fed through to pre-tax profit growth of 10 per cent.

If you wanted to quibble with the trading update then the LFL sales figure for the year as a whole does imply that H2 LFL sales were negative to the tune of about 0.4 per cent. That said, I do not find this too concerning as given how hot the summer was, I am surprised many people went bowling at all.

One of the things I really like about this business is that its improvements in profitability are backed by improved cash flows. Last year the company achieved a very creditable cash return on cash capital invested (CROCCI) of 18.6 per cent. It will have come very close to ungearing its balance sheet from the end of last year, despite paying a special dividend. This is the kind of financial position that lots of businesses would love to have.

A further special dividend looks to be on the cards in the next few months as well.

This company is in a very good place just now. Its new centres have started trading well and the company continues to outperform the industry as a whole. It is very sensibly-managed and its profits and cash flows should prove to be quite defensive given that a family outing to the bowling alley is cheaper than going to the cinema.

Hollywood Bowl Group PLC (BOWL)

FORECASTS £ millions unless stated

Year	2018		2019		2020	
Turnover	122.7	+7.6%	129.1	+5.3%	136.3	+5.6%
EBITDA	35.9	+10.0%	38.1	+6.1%	40.5	+6.4%
EBIT	24.6	+11.1%	26.6	+8.2%	28.3	+6.4%
Pre-tax profit	23.6	+11.9%	25.7	+9.2%	27.5	+6.7%
Post-tax profit	18.5	+1.6%	20.4	+10.1%	21.8	+6.9%
EPS (p)	12.4	+2.5%	13.6	+9.7%	14.7	+8.1%
Dividend (p)	6.9	+20.0%	7.4	+7.2%	8.0	+8.1%
CAPEX	12.5	-9.1%	15.5	+24.0%	13.5	-12.9%
Free cash flow	20.5	+34.9%	20.7	+1.4%	22.9	+10.5%
Net borrowing	4.8	-37.4%	-3.6		-12.3	

Source: Sharepad

The shares are not desperately cheap on a one-year forecast rolling PE of 15.4 times, at a share price of 210p, nor should they be. In a UK leisure sector, which has a lot of unexceptional and struggling businesses, Hollywood Bowl is a standout performer. It has a simple and effective business model and generates very good cash returns on the money it invests. The business looks well placed to go from strength to strength, in my view.

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Greggs

High street bakery chain **Greggs (GRG)** used to be a very reliable share to own. In recent years, it has had to face up to changing shopping trends and eating habits and adjust its business accordingly. It seems to be doing a good job if its recent trading performance is anything to go by.

The company's strategy has been based around moving its shops away from the high street towards areas such as train stations, service stations, airports and university campuses where footfall levels are higher. It is also franchising stores which could end up developing a very profitable stream of royalties, as well as demand for its own bakeries. The move towards healthier food, coffee and a focus on breakfast also seems to be going down well with customers.

Greggs is trading well with third-quarter like-for-like sales accelerating to 3.2 per cent, compared with 1.5 per cent at the half-year stage in June and up against a tough comparative from last year of 5 per cent. LFL sales for the year as a whole are now running at 2.1 per cent, which is nothing stellar, but good enough to keep the company on course to meet City analysts' current forecasts.

Greggs PLC (GRG)

FORECASTS — £ millions unless stated

Year	2018		2019		2020	
Turnover	1,019.0	+6.2%	1,082.8	+6.3%	1,143.0	+5.6%
EBITDA	136.5	+8.5%	146.7	+7.4%	156.5	+6.7%
EBIT	80.5	+11.2%	87.1	+8.3%	93.7	+7.5%
Pre-tax profit	81.6	+13.7%	87.4	+7.2%	93.4	+6.8%
Post-tax profit	64.4	+13.5%	69.2	+7.5%	74.7	+7.9%
EPS (p)	63.1	+13.7%	67.3	+6.7%	72.0	+7.0%
Dividend (p)	32.0	-0.9%	34.2	+6.9%	36.7	+7.3%
CAPEX	88.2	+21.5%	92.2	+4.6%	81.8	-11.3%
Free cash flow	27.6	-38.1%	41.0	+48.6%	65.3	+59.3%
Net borrowing	-47.8		-49.5		-75.9	

Source: Sharepad

Greggs remains a much better business than any of the UK supermarkets in my opinion. It has much higher profit margins (just under 8 per cent) and a ROCE adjusted for rented shops of 15 per cent, which is pretty good.

Excluding rented shops – where the assets and debt liabilities will go on the balance sheet next year – the company is debt-free with good underlying cash generation. Capex spending at the moment is quite high, but it is significantly improving the quality of the business. As a result, sales and profits should be able to keep moving higher.

Like most shares in recent weeks, Greggs' stock market valuation has come down. That said, the shares still trade on a one-year forecast rolling PE of 16.2 times, which may not be low enough to make for an attractive buying level. As a high-quality food retailer, its shares would not be too out of place on investors' watchlists.

Marston's

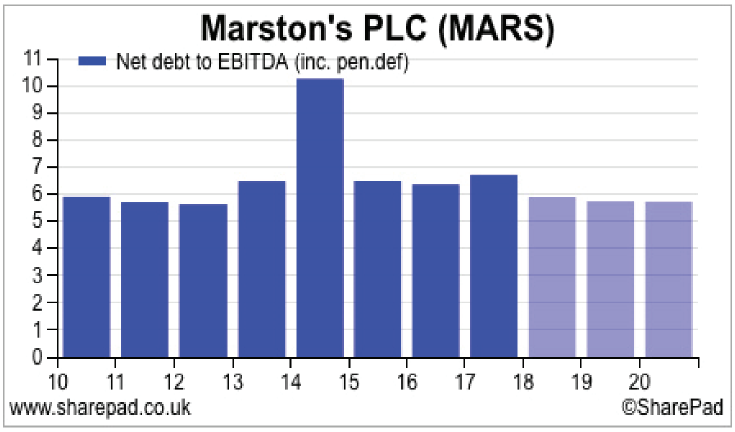
Pub chain and brewer **Marston's (MARS)** is regularly cited by some commentators as a cheap share. Trading on a one year forward rolling PE of just 6.8 times and offering a forecast yield of 7.7 per cent this is undoubtedly true.

The shares have been cheap for a long time, but this hasn't stopped them falling in price by nearly 13 per cent so far this year. This is largely due to the fact that it is very hard to grow the profits of existing pubs due to rising cost inflation.

Like-for-like sales growth of between 2 per cent and 4 per cent is what seems to be needed according to various pub chains in order to maintain current levels of profitability. Pubs managed by Marston's only achieved 0.6 per cent LFL growth last year. Profits growth is coming from opening new pubs and lodges as well as buying parcels of pubs from other pub chains such as Mitchells & Butlers.

The group's tenanted pubs (taverns) are trading reasonably well and remain a good source of cash flow. The Brewing business has also had a good year and is winning new business.

Marston's big problem has not changed for years – it has far too much debt. Its debt pile – as measured by the net debt to Ebitda ratio – looks like one that belongs to a water or electric utility and remains too high for a business that faces challenging markets.



Higher interest charges held back profit growth this year and remain a real risk to shareholders if trading profits were to fall. Cash interest payments are currently eating up around one third of Marston's operating cash flow, whilst heavy capex spending means that free cash flow is weak. I think it needs to pay down debt and with the current dividend costing nearly £50m, that does not look like happening if you look at current forecasts.

Marston's PLC (MARS)

FORECASTS £ millions unless stated

Year	2018		2019		2020	
Turnover	1,073.4	+6.1%	1,106.5	+3.1%	1,134.8	+2.6%
EBITDA	228.0	+5.1%	234.3	+2.8%	241.7	+3.2%
EBIT	184.2	+3.7%	189.8	+3.0%	196.2	+3.4%
Pre-tax profit	107.0	+4.0%	112.6	+5.2%	116.5	+3.5%
Post-tax profit	88.9	+2.3%	92.6	+4.1%	96.4	+4.1%
EPS (p)	13.9	-4.1%	14.5	+4.3%	15.0	+3.4%
Dividend (p)	7.6	+1.3%	7.8	+2.6%	7.9	+1.3%
CAPEX	156.3	-20.4%	135.5	-13.3%	136.3	+0.6%
Free cash flow	26.7		38.5	+44.2%	46.1	+19.8%
Net borrowing	1,344.6	-7.2%	1,347.1	+0.2%	1,383.2	+2.7%

Source: Sharepad

Arguably, capex and the dividend may have to be cut. This would not be good for Marston's competitive positioning or the yield attraction of its shares. Add these concerns to an underperforming managed pub business with rising costs and I think there are good grounds for viewing Marston's as a value trap.

Patisserie Holdings

Wednesday was a day to forget for **Patisserie (CAKE)** shareholders. At 7:30 in the morning, the company stated: "Patisserie Holdings plc announces that, during the course of 9 October 2018, the board of directors of the Company has been notified of significant, and potentially fraudulent, accounting irregularities and therefore a potential material mis-statement of the Company's accounts.

"This has significantly impacted the Company's cash position and may lead to a material change in its overall financial position. As a result, the Company has requested that its shares be suspended from trading on the Alternative Investment Market, while it conducts a full investigation with its legal and professional advisers into its true financial position.

"In the meantime, Chris Marsh, the chief financial officer, has been suspended from his role."

Later on, at 13:53pm, it further updated the stock market: "Patisserie Holdings plc announces that, further to the Company's announcement made earlier today, the board of directors of the Company has today become aware that a winding up petition in respect of Stonebeach Limited was filed at The High Court of Justice, Companies Court on 14 September 2018. Stonebeach is the Company's principal trading subsidiary.

The petition relates to sums due to HM Revenue & Customs (HMRC) of approximately GBP 1.14m with a hearing date listed for 31 October 2018. The petition was advertised in the London Gazette on 5 October 2018. The Company and its advisors are in communication with HMRC with the objective of addressing the petition."

Then, just before you thought things couldn't get any worse, an announcement on Thursday afternoon stated that the company was effectively bankrupt without a fresh injection of capital:

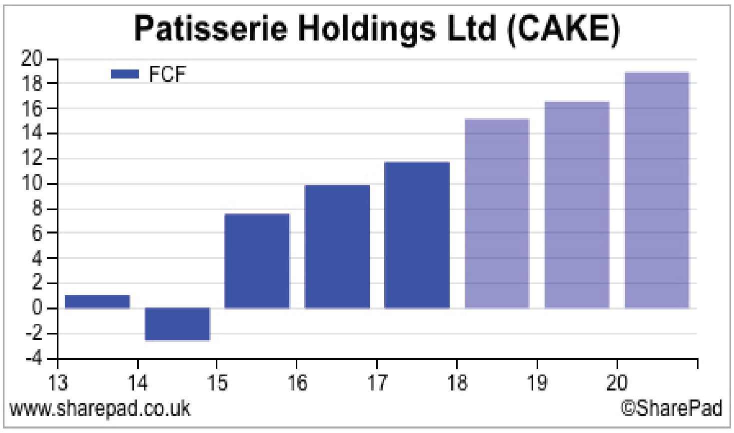
"Patisserie Holdings plc announces that the Company, in conjunction with its professional advisers, has during the last twenty-four hours, undertaken further investigation into the financial status of the Company. The Board has now reached the conclusion that there is a material shortfall between the reported financial status and the current financial status of the business.

"Without an immediate injection of capital, the Directors are of the view that there is no scope for the business to continue trading in its current form.

"As a consequence, the directors and the Company's professional advisers are assessing all options available to the business to keep it trading and will update the market in due course."

I was absolutely gobsmacked to read these announcements. Along with everybody else, I was left thinking, " how could any outside investor have spotted this?"

Based on the financial statements of the group, all had seemed well. Despite opening up lots of new shops, the company had been generating increasing amounts of free cash flow in recent years and supposedly had £28m of net cash at the end of March 2018.



There are lots of warning signs out there for outside investors such as poor cash conversion, but this was not a red flag with Patisserie Valerie. There was also an absence of big liabilities on the balance sheet with outstanding trade creditors of just over £5m at the end of March.

In terms of hidden debts such as rents, the annual rent bill of £14m was covered 2.6 times by the past 12 month's trading cash flow.

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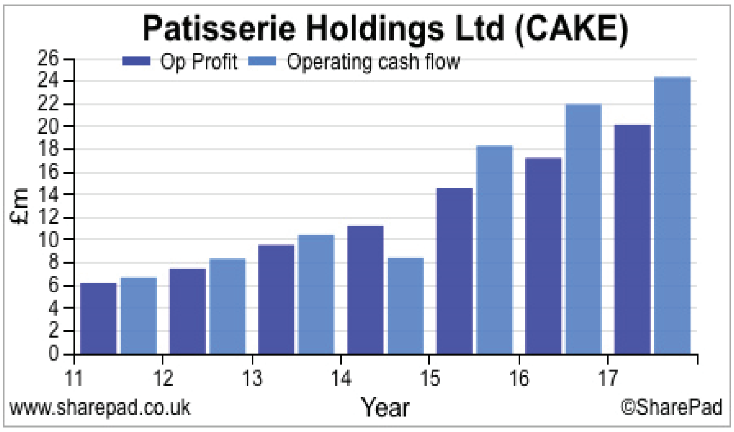

The truth is that it was probably impossible for any outsider to spot if a fraud was being committed.

In just over 24 hours, the company has gone from being a highly regarded growing business to one that is effectively dead.

What is clear is that there has been a complete breach of trust between the company and its shareholders. There is a harsh reminder for all outside investors that numbers in accounts may not be what they seem. Thankfully, most companies' accounts are trustworthy, but it is always worth reminding yourself that the numbers you are reading in accounts are for a group of companies. You do not get to see how those numbers are made up from lots of different subsidiary companies within it. This is where most of the potential for financial shenanigans exists.

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