

IG Design Group: Priced to default, but will it?

Company:	IG Design Group	Market Cap:	£82mio
Industry:	Gift packaging/craft	Net Cash:	\$40mio
Country:	US, UK, World	Revenue:	\$1bn
Date:	5 th April 2022	Operating Income:	\$0mio (0%)
Dividend:	None	Free Cash Flow:	\$0mio (0%)
Entry:	£59mio	Target Market Cap:	£150mio

Deep, deep value

I stumbled upon IG Design Group due to its ultra-cheap market valuation. The company was valued at around £100mio after announcing challenging supply chain constraints that erode all their profits for the FY 2022 and the CFO resigning. In February 2022, the CEO also resigned and the company dropped to a £60mio market cap, yet reporting \$40mio in net cash and \$1bn in revenues. With Studio Retail Group defaulting in January 2022, caution is key and the likelihood of default would need to be weighed...

What does IG Design Group do?

IG Design Group is the world's largest consumer gift packaging, craft & stationery company with over 11,000 customers, products sold in over 210,000 stores and operations in over 80 countries worldwide. The company sources over 70% of its revenues from the US (which doubled through its 2020 acquisition of CSS Industries) and makes nearly half of its annual sales during the Christmas season. IG Design doesn't really have direct competitors, although the biggest players in the industry are American Greetings and Hallmark – despite them mainly focusing on cards. The firm is supplying the largest retailers of the world, such as Walmart (24% of sales), Aldi, Tesco, Costco, Target, Lidl or Amazon and is focusing on reducing the seasonality of the business further.

Can IG Design go into default?

In a matter of 6 months, the company's market capitalisation went from £600mio to below £100mio as operating margins fell from near 9% to 4% to 0% due to cost inflation, mainly driven by higher freight, labour and raw materials (mostly paper) prices. Nonetheless, IG Design Group currently has net cash of \$40mio, so why worry about default? As mentioned, the business is highly seasonal with major capital outflows ahead of Christmas in September/October and high capital inflows during the Christmas season. The company reports H1 for the period ending on 30th September and H2 ending on 31st March, which therefore covers the seasonality well (table below). The swings between H1 and H2 result in as much as \$150mio working capital movement. The problem with the upcoming season is that higher costs cannot immediately be offset with higher selling prices, as IG Design will have to spend more in the run up to Christmas and only then receives the main benefit of higher selling prices. On September 30th 2021 the firm had \$283.3mio of room to borrow from, which comprises of a \$95mio RCF, up to £130mio RCF during peak inventory season and \$18mio HK financing arrangement, which is dependent on receivables. Back then, around \$155mio was drawn and considering \$96mio of cash resulting in \$59mio net debt. Given that IG Design has \$40mio net cash as of 31st March (\$37mio less than prior year), input costs would need to increase at least another \$100mio for IG Design to hit the limits of their credit facilities (equivalent to 10% rise in cost of sales and expenses). This makes a default, in my opinion, unlikely.

IG Design Group's strong seasonality

H1 (in \$)	Net cash/Net debt	Revenue	Cost of Sales	Expenses	PBT	Market cap (in £)
H1 2019	-130	266	162	29	18	580
H1 2020	-106	309	198	32	21	660
H1 2021	-23	435	351	68	17	522
H1 2022	-59	484	405	58	19	244

H2 (in \$)	Net cash/Net debt	Revenue	Cost of Sales	Expenses	PBT	Market cap (in £)
H2 2019	22	583	366	64	23	613
H2 2020	52	624	530	93	-1	542
H2 2021	77	873	719	138	15	575
H2 2022 (estimated)	40	1000	850	150	0	60

Source: IG Design Group

The new CFO

On the morning of 30th March 2022, IG Design Group announced to have hired a new CFO, Paul Bal¹. I think he is the ideal candidate due to his exposure at multiple consumer brands, such as Stock Spirits, Tupperware and, especially, a 15-year stint at British American Tobacco – a company that constantly has to pass through multiple price hikes to consumers. This should help IG Design to pass through the higher input cost inflation to the consumer. Paul also purchased additional shares for himself.

US PPI at 10% & Aldi price hikes

As mentioned, prices need to climb another 10%, while selling prices would remain stable in order for IG Design hitting its credit limits this autumn. US PPI has been printing at 10% lately and this is before any price hikes related due to the Ukraine war or China's latest Covid wave. This Monday, Aldi has raised prices by 20-50% on around 400 products, citing exploding costs, especially for wheat, energy and animal feed, in the wake of the global pandemic, the rising inflation rate, transport problems, scarcity of resources and now a war in Europe². While this sounds concerning at first, IG Design Group will likely start passing on higher costs to consumers now, which could also be reflected in higher prices at retailers for their products. Important is, these are the 2nd round effects of the inflation that producers have experienced over the last year. However, these price hikes need to be monitored closely and could perhaps trigger dramatic changes in consumer behaviour...



¹ <https://2jon6lgrvv6i3llu225kv2cx-wpengine.netdna-ssl.com/wp-content/uploads/2022/03/CFOAnnouncement-FINAL-300322.pdf>

² <https://newsrnd.com/life/2022-04-03-aldi--price-shock-%E2%80%93-the-discounter-giant-will-make-around-400-products-more-expensive-from-monday.B1rdZRLQ5.html>

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