Quarterly Report

Castelnau Group Limited

31 March 2022

The Figures

	2021 Q4	2022 Q1	Change
Net Assets £m	£170,945,059	£154,704,051	-9.5%
Net Assets /share	0.935	0.8408	-10.1%
Share Price	1.055	0.96	-9.0%
No. of shares	183,996,057	183,996,057	0.0%
Market Cap	£194,115,840	£176,636,215	-9.0%
Prem / Disc	12.8%	14.2%	10.5%
Assets			
Equities	£123,308,880	£115,297,475	-6.5%
Loans to Subs	£3,361,795	£5,386,795	60.2%
Cash & Equiv.	£44,614,629	£36,324,706	-18.6%
Share Price			
Dignity	£5.90	£5.05	-14.4%
Hornby	£0.42	£0.33	-21.4%
Phoenix SG	£2,385.75	£2,366.40	-0.8%
Cambium	£1,079.08	£1,047.06	-3.0%
Ownership			
Dignity	20.0%	21.0%	5.0%
Hornby	55.0%	55.0%	0.0%
Phoenix SG	55.7%	60.0%	10.4%
Cambium	19.2%	34.8%	81.3%
Rawnet	100.0%	100.0%	0.0%
Ocula	77.0%	77.0%	0.0%

Performance Overview

Net Assets declined by 9.5% in the quarter as our holdings declined in price, particularly Dignity (-14.4%) and Hornby (-21.4%). Our cash declined slightly as we added to our holdings in existing businesses, especially Cambium.

General Business Update

We have reached a stage where all our portfolio companies are either profitable or at least washing their face. Profitability is just base camp on the way to building sustainable high returns. It's not something to celebrate, but it's a prerequisite on the path to success. However, given that we started with three of our four businesses losing money, it is progress.

We are still looking for CEOs at two of the four businesses.

Update on our Transformation Work

As we set out in the 2021 Q4 report, there are four key attributes that we work to develop at our portfolio companies. These are: the right culture serving a clear purpose; competitive advantage; high returns on capital, and great management. Looking at our progress through that lens, here is an update on the four portfolio companies.

Portfolio Companies

Dignity

Dignity has just published its Annual Report for the year 2021 and there is a clear setting out of the strategy, the driving purpose, the changes being made and the new principles that will be used to define and cultivate the culture. Pages 4 to 15 of the Dignity Annual Report contain a lot of information which explains our work there and we will avoid duplication here.

Cultural change is the hardest of our challenges in any company. At Dignity we are using a methodology we have used successfully before at Cambium which is to have the company develop a set of principles internally, with some guidance, linked to a primary purpose. This exercise has taken 6 months and is explained on page 10. The new principles are published on page 11. The next stage is to keep applying these principles to decision making within the group, continually teach them and evaluate ourselves on them. This is something we do at Phoenix.

Dignity is in the first year of our transformation efforts and we are pleased with the amount of progress that has been achieved so far. In 2022 the main organisational change will be complete structurally, but it will take a few years for all the elements to come together and for Dignity to be settled into what we might call business as usual.

The senior leadership team is nearly in place and more announcements will follow in the coming quarter.

As the Dignity Annual Report explains though, the early part of the strategy is the toughest as reducing prices to regain competitiveness and investing in people and facilities to improve the offer initially reduces profits which is exacerbated by a reversal of the excess deaths during COVID. Ultimately, if the strategy is right then the virtuous circle of growth will lower unit costs and increase profits.

Dignity is also using an OKR (Objectives and Key Results) method of focusing the organisation on the most important goals which we have successfully used elsewhere.

Hornby

As Hornby has reported recently, the profitability of last year, which it would be fair to say had been temporarily boosted by lockdowns, has been built on further in the year to March 2022. These figures are yet to be released and so we can't comment on them.

We have been working on a new store concept which brings together all the underlying hobbies within the group in one exciting experiential retail destination. This quarter we have been working with one of the UK's best retailers to bring it to reality which we currently expect to do by Q4 this year.

Lyndon stepped up to the Chairman role in the quarter, but we have yet to identify a suitable CEO to take the strategy forward.

Stanley Gibbons & Showpiece

Stanley Gibbons put out a trading statement in April talking about good progress but hasn't published numbers yet and so we won't discuss those here. We still have work to do on the capital structure including the pension schemes and we would expect to finish that this year.

Showpiece, which took our collectables interests into the digital arena with fractional ownership, sold out its second item which was an Edward VIII penny coin, bought in conjunction with our coin business Baldwin's. They have just secured their third Showpiece item, which is now public and will launch in the coming quarter.

Cambium

Cambium has been dealing with a rapid return to wedding activity since restrictions were lifted last year. For a number of reasons, the period since then has proven to be a perfect storm. Some of the factors are internal and some external.

Internally, we cut headcount during the lockdown of 2020 in order to survive and to accelerate the integration of Prezola with The Wedding Shop and The Wedding Present Co. We cut headcount from 190 to 110 in 2020 but the resumption of weddings in 2021 and the growth of the underlying businesses has resulted in business activity running at more than twice its 2019 peak. We have been hiring back but in a tight labour market. At 160, headcount is well down on 2019 with twice as much activity - that's a lot of productivity growth in one leap! Our systems integration was not well implemented from a business process point of view and that has added to our internal issues.

Externally, our suppliers have been letting us down because they themselves have struggled with supply chain issues and/or they have prioritised their own direct business over ours. The impact of all of this has been unhappy customers, complaints, and bad reviews (see TrustPilot), which for a company that obsesses about delighting customers is a tragedy.

We are happy to report that a corner has been turned, backlogs have been cleared and the service level is improving. So far, the forward intake of new registrations remains at an elevated rate. The focus of the business this year is on delivering that 5-star service on which its reputation and growth has been built. This will have a negative impact on profitability in 2022 but will preserve the long-term value.

In the quarter, we announced the acquisition of a stake in a business called Hostology. The agreement is to buy 25% now and 26% in 2 years' time. Hostology was founded by Emma Hardcastle and a number of wedding venues to build software that allows venues to manage weddings including the interaction with couples, guests, and suppliers. Choosing a venue is one of the first steps of wedding planning because it sets the date. We believe a closer collaboration between our highly regarded wedding planning business, Rock My Wedding, and Hostology will improve both businesses and Emma is joining Cambium to lead that effort.

We are undertaking a capital raise for Cambium in the current quarter to clear the debt taken on to get through COVID, to fund this acquisition and a new business we intend to launch in the baby list space. Castelnau Group is underwriting that offer which could materially increase our holding in Cambium which is currently 34.8%.

Enabling Companies

Rawnet

Rawnet has seen a very strong start to 2022 in terms of both new client pipeline activity and revenue run-rates. Revenues for the full year 2022 look likely to be considerably higher than pre-COVID levels as the company has secured scarce IT Developer resources required to meet increasing client business. Headcount has grown to 57 people. We are encouraged that the quality of Rawnet's client roster is improving, mirroring the company's market reputation. The increase in client retainers and loyalty also reflect this trend.

Since the acquisition of Rawnet by Castelnau last year, we are increasingly using Rawnet's services throughout the Castelnau Group companies. Such 'Group business' now accounts for over 50% of Rawnet's revenue and is likely to remain at this elevated level as it continues to support your companies in their digital marketing revival and transformation. To support the entire group and encourage a rapid adoption of transformational digital practices, Castelnau has been underwriting Rawnet's Group business to provide its IT services to Group companies at pace.

Whilst Rawnet employs a 'cost-plus' pricing model of sorts, the 'plus' element of this equation is minimised for such group business. Such tactical inter-company arrangements can be frustrating at the start for those involved but we believe this is the smart thing to do. We can see some of the fruits of Rawnet's involvement already at Hornby in particular. This does mean though that in a year of excellent revenue growth, Rawnet will not earn its total profitability to the full extent. Importantly, this temporary under-earning should not mean that Rawnet's Intrinsic Value is impaired. The other 50% of Rawnet's business to 3rd-party clients is performing well, notwithstanding the aforementioned scarcity of IT staff and wage inflation.

Ocula

The company's headcount has grown to 18 in the quarter as it builds out its AI platform for e-commerce optimisation. Those of you who attended the Phoenix AGM in March had the opportunity to view a demonstration of the technology. The Ocula technology is currently live and adding value at both Hornby and Stanley Gibbons.

Ocula signed up its first external new customer this quarter and is in discussions with a number of others.

We believe Ocula has exciting prospects, and we are facilitating its exposure throughout the Castelnau group companies and externally. The company is in the thick of licensing discussions with internal and external clients and is in early discussions with VCs to increase market awareness and fund the necessary investment ahead of its revenue ramp in the retail analytics market.

Outlook

All of our businesses are making positive strategic progress towards our goals and there is some good momentum building, but there is a very long way to go. We still have some key people to find.

We are finding opportunities coming our way especially within the fields we are already in, End of Life, Weddings, Hobbies and Collectables.

We remain of the view that there is considerable upside not properly valued at current prices.

	Pro-Rata Castelnau "Look-Through"	listed stakes			unlisted stakes				
		Dignity	Hornby	Stanley Gibbons	Phoenix SG	Cambium	Rawnet	Ocula	Showpiece
Castelnau (CGL) Ownership stake		21%	55%	60%	60%	35%	100%	77%	100%
Employees	978	3,375	193	66		160	57	18	3
Sales annual run-rate	**£107.6m**	£312.0m	£43.6m	£9.6m		£24.6m	£4.2m	0	0
per CGL share	£0.58								
Underlying Pre-tax profit run-rate	**£4.2m**	£26.8m	-£.5m	-£3.0m		£1.0m	£.3m		
per CGL share	£0.023								
# CGL shares (m)	184								
CGL Share price (latest)	**£.96**								
CGL Market Capitalisation	£177m								
CGL NAV (31/03/2022)	£154.7m =	£52.3m	£30.m		£19.9m	£7.m	£6.1m	0	0
CGL NAV per share	**£.84**								
premium	12%								

31/03/2022

Asset	£m	% of NAV	QoQ £m
Dignity	52.3	34%	-8.2
Hornby	30.0	19%	-7.9
Phoenix Stanley Gibbons Ltd	19.9	13%	+1.7
Showpiece	0	0	0
Cambium Group	7.0	4.5%	+3.0
Rawnet	6.1	3.9%	0
Ocula	0	0	0
Total Equities	**115.3**	**75%**	**-11.3**
Loans to enabling companies	-5.4	-3%	-2.0
Cash	3.7	2%	
Short Term Bonds	32.6	21%	
Total Cash + ST Bonds	36.3		-8.2
GAV	157.0		-17.5
Accrued Liabilities	-2.3		
NAV	**154.7**		**-17.4**

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