

# 'ITQ' – on a niche profits quest

Niche IT recruiter InterQuest has remained resolutely profitable throughout the recession and looks well placed to resume good growth, says James Crux

**F**ounded in 2001 and flourishing in the notoriously cyclical staffing sector, sales and profits progression at IT staffing company InterQuest, which had enjoyed several years of unfettered growth, was unsurprisingly interrupted by the savage economic downturn.

However, its proven management team, led by energetic business builder Gary Ashworth, had seen that some short-term pain was on the way and cut costs quickly to protect profitability. This action, allied to the group's focus on specific market niches, as well as a contract recruitment bias, buffering the business from the downturn's worst, meant that InterQuest remained resolutely profitable and cash generative and is now leaner and likely to resume good growth.

Throughout the market's darkest hours, management continued to invest in and broaden the business and pleased investors with robust 2009 financials. InterQuest is now seeing tentative recovery signs in its specialist markets and even began hiring fee earners again as business came back towards the end of last year.

Curiously, in the face of all these positives, InterQuest's shares appear to be less well loved than those of quoted peers whose prospects are perhaps not as bright. Once the economic tailwind picks up, the shares should receive a strong rerating and are well worth considering. As

Ashworth, CEO and major shareholder, asserts, 'We are a capital growth stock and are yielding 4 per cent at this level.'

## Strategy

City based and with an AIM listing, InterQuest's strategy is all about delivering profitable growth – organically and via a partnership programme, as well as through careful acquisition – by leveraging the niche market expertise of its diverse batch of businesses.

Providing contract and permanent recruitment services across the UK and Europe through seven separately branded divisions, InterQuest caters to clients spanning the public sector and the SAP, Customer Relationship Management (CRM) testing, banking, retail, media and pharmaceuticals sectors, while the ambitious Ashworth would most certainly like to make greater inroads into the insurance and Oracle markets.

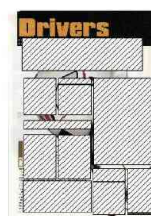
'We have lots of different businesses with lots of different names,' he explains, pointing out that one definite advantage of having a number of different specialist brands, as opposed to a single all-encompassing one, is higher margins. Each highly focused individual business is well known and trusted in its niche, and can charge accordingly.

To give but a flavour of the spread, group businesses include the public sector-focused Sand Resources,

recently awarded two national framework contracts for the NHS. Another, Genesis, boasts financial behemoths Fidelity, Goldman Sachs and HSBC as clients. SBS, focused on the public sector, SAP and telecoms arenas, lists the likes of the Bank of England, Sky and the FSA on its customer roster, while Intellect's clients include Royal Bank of Scotland and Marks & Spencer.

Not unexpectedly, sales and profits have lately been lowered due to economic pressures. Yet under Ashworth the company has pushed on with its growth strategy, continuing to invest for growth and further broadening the business base.

Last year, besides establishing two specialist house brands, five new businesses were launched – Sapien, Korus IT and Lanborne Associates being but three – via the 'IQ Equity' division established at the end of 2008. IQ Equity's strategic brief is to back teams of recruiters wanting a stake in their own businesses, with InterQuest providing training, finance and infrastructure support. Though investment in these start-ups, each bossed by a seasoned specialist, pegged back InterQuest's returns in 2009, these businesses should



contribute to profits this year and help fuel long-term growth.

When discussing strategy, it would be remiss not to mention the deliberate bias towards contract recruitment, usually repeat business, which has helped the company put in such a creditable performance during the low point of the cycle. Holding up far better than permanent recruitment, always severely affected by a recessionary hiring freeze, Ashworth says this bent insulated the business from the worst of the downturn.

Whereas gross profit from contractors fell by a manageable 8 per cent last year, permanent placement declined by 46 per cent, bearing out the merits of the business mix and further shifting the emphasis towards contractors, now representing 80 per cent of gross profits, up from 71 per cent a year ago.

## Management

Renowned recruitment sector mover and shaker Gary Ashworth, executive chairman as well as CEO, is the group's co-founder and majority shareholder. He is an entrepreneur of undoubted value-creation credentials, having founded Abacus Recruitment in the early 1980s and floated the business on AIM at 20p in 1995, the same year the junior market was created.

Abacus was the fastest-growing AIM venture in 1996 and 1997 and was eventually sold for £16.8 million cash, a 1,000 per cent share price premium, to Michael Ashcroft's Carlisle Group.

Never a man to sit still, Ashworth sat on the board of the Assembly Rooms in Edinburgh for five years, having previously rescued the venue from bankruptcy; and the theatre-loving entrepreneur, who even manages actors, singers and comedians, has previously produced plays at London's Donmar Warehouse and other West End venues.

An InterQuest man since February 2004, straight-talking Michael Joyce, formerly financial controller of technology group Rebus, is the company's finance director and rules over the finances of its many businesses

with an iron fist. Well versed in all matters recruitment-related, having previously worked as a member of the finance team at Robert Walters, he earned his accountancy spurs with Coopers & Lybrand.

The most high-profile name among the group's non-executive directors is that of InterQuest co-founder Luke Johnson, the business and media figure who currently chairs Channel 4 and Signature Restaurants. Johnson, who graduated in medicine from Oxford University and also had a spell as an equities analyst at investment bank

Kleinwort Benson, holds a number of other non-executive directorships.

## Prospects

Though the timing of economic recovery is uncertain, InterQuest's growth prospects are strongly underpinned by its healthy competitive positioning.

Most of its businesses are well established in their niche IT areas and the blue-chip clients the company serves prefer to trade with bigger agencies boasting robust balance sheets that aren't going to go

low point for profitability for a venture that addressed its cost base in a tough financial year. Calendar-year numbers for 2009 showcased the resilience of the group's business model of 'championing' niche recruitment operations across a variety of sectors while making a very acceptable return in the most testing of recruitment markets.

Revenue fell by 8 per cent to £97.4 million and gross profits by almost 20 per cent to £12.4 million. However, cost cutting meant that the company remained resolutely profitable, even though (adjusted) pre-tax profits dropped from £4.8 million to £2.9 million, with earnings reducing by 40 per cent to 6.6p.

Generating a very healthy £3.3 million of net cash from operations, InterQuest pared net debt from £5.5 million at the start of the year to £3 million by the end of 2009, slashing its interest bill and no doubt supporting a doubling of the final dividend to 2p, paid out in February.

In another positive prospects indicator, management has flagged up signs of recent market strengthening, with permanent recruitment up by 40 per cent in the fourth quarter, compared with the average in the first three quarters of 2009. InterQuest, which stripped down its own staffing levels 'to the core' last year, has begun hiring new fee earners through its own training academy.

Meanwhile, the company has highlighted renewed contract recruitment business in the first two months of 2010, with the number of contractors out on assignment 6 per cent up on the number in mid-December.

## Valuation

House broker Cenkos sees pre-tax profits recovering strongly to £3.6 million this year, ahead of a further forecast rise to £3.9 million for 2011. Earnings are expected to rebound from 6.6p to 8p, before a further climb to 8.8p next year, while investors should look for further progression in the dividend to 2.2p and 2.3p over the next two years.

SHAREHOLDERS	
<b>Directors:</b>	
Gary Ashworth	41.02%
Luke Johnson	12.43%
Other management	7.90%
Ross Eades	5.25%
<b>Institutions:</b>	
Chase Nominees	8.03%
Waterhouse Nominees	3.74%

bust overnight.

There is every indication that prospective investors are buying in at the right time, with 2009 marking the

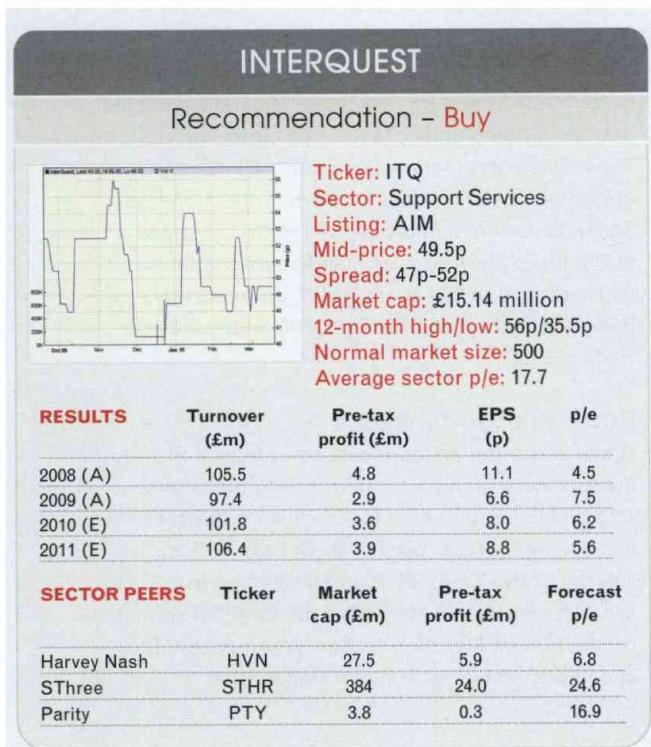
Based on these estimates, the shares, which have plummeted from the 150p level at which they traded on AIM at the beginning of 2007 to 49.5p, are selling for a modest 6.2 times this year's likely earnings, falling to 5.6 times earnings for 2011.

Now, these miserly multiples may reflect wider sector worries about the threat of a double-dip recession, but they leave InterQuest trading at a large and undeserved discount to related peers such as SThree and Parity, whose

shares sell for around 25 times and 17 times forecast earnings respectively.

All things considered, we view the present rating as being far too low, with InterQuest having passed through the cyclical low point and now primed to capitalise on the recovery. And as Ashworth opined earlier, the shares, which we consider a good long-term buy, offer investors the added attraction of a strong and sustainable yield of 4 per cent plus.

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CEO Gary Ashworth has pushed on with **InterQuest's** growth strategy



**INTERQUEST NEWS FLOW**



**02/03/2010:** InterQuest unveils resilient financials for 2009, remaining in profit to the tune of £2.9 million at the adjusted pre-tax level in a tough market, on revenue down 8 per cent to £97.4 million. A healthy £3.3 million of cash is generated, enabling significant reduction in net debt

**15/02/2010:** The AIM-traded group says its Sand Resources business has been awarded a place on a second NHS framework agreement, strengthening its position as a leading provider of recruitment services to the public sector

**15/09/09:** Reasonably robust financials are delivered for a challenging first half of 2009, with pre-tax profits falling by 55 per cent to £913,000, with InterQuest insulated from the worst of the downturn by its niche IT focus and bias towards contract recruitment