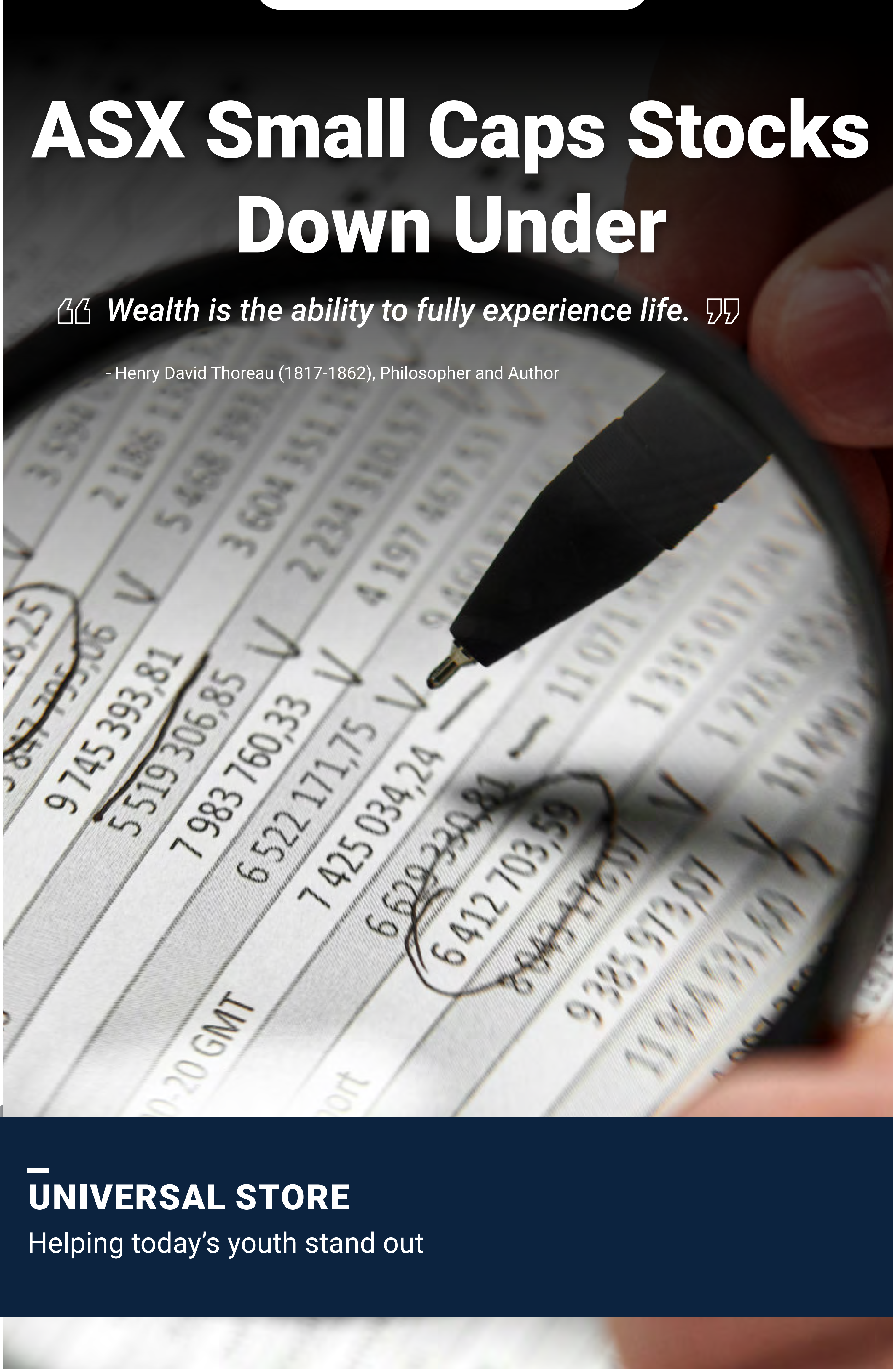
STOCKS DOWN UNDER

23 SEP 2022

ASX Small Caps Stocks Down Under

> *Wealth is the ability to fully experience life.*

- Henry David Thoreau (1817-1862), Philosopher and Author



UNIVERSAL STORE

Helping today's youth stand out

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Stocks Down Under rating: ★★★★

ASX: UNI
Market cap: A$360.9M

52-week range: A$3.37 / A$8.56
Share price: A$5.02

There's no shortage of fashion outlets on the ASX, but Universal Store (ASX:UNI) is one of the newest and most peculiar. Its focus is casual youth apparel, targeting millennials and Gen Z customers. The stock has traded above its IPO price for virtually all of its listed life, but has slipped this year as inflation has risen and the growth in eCommerce has cooled. Has talk of the demise of Universal's customers been greatly exaggerated?

Share price chart

Source: Tradingview

Just for Millennials and Gen Z

Universal Store listed in November 2020, having raised $48.5m at $3.80 per share. After rising on debut and spending a few months above $8 per share during 2021, the shares retreated, but have mostly been above the IPO price.

The company's history dates back to 1999 and it spent nearly two decades in the hands of its founders, before being sold for $100m to a buyout consortium led by private equity firm Five V Capital. Five V Capital have since exited, but Brett Blundy's company retains a 16% ownership. Another significant owner worth noting is CEO Alice Barbery, who has a stake of just over 3%.

By the time the company listed, it had an enterprise value of $290m, which is now just over $400m. Evidently, this company must be doing something right. It services 16-35 year old customers, a demographic that is underestimated by investors, even some in that very demographic, because they lack the income of older generations. But this can sometimes be to particular companies' advantages. AfterPay is arguably the best example, but Universal Store is another. This demographic isn't unwilling to spend money, but is looking to get the most out of it. Young people are online and socially active, using fashion as a key mechanism to this end. They come to choose attire for birthdays, music festivals, holidays and even for working from home.

Universal has 78 stores across the nation that tend to be in major shopping centres, and it has an online presence. It is ultimately aiming for more than 100 stores across Australia and New Zealand. There are no stores in New Zealand right now, but Universal is aiming to break that market eventually.

It sells both curated third-party products and its own private brand products, although its revenue is skewed two thirds to the former. Also helping the company's appeal is that it is profitable and its solid technology, which allows it to automatically order stock that is popular with consumers instead of what management thinks might be popular several months down the track. Fashion retailer Zara has a similar system.

A mixed FY22 to be followed by an uncertain FY23

Now to the bad news. Lockdowns in the past couple of years naturally impacted sales. And arguably, investors feared that millennials would tighten their belts and cut back on spending. For FY22, the 12 months to 30 June 2022, the company recorded $208m in sales, down 1.4% from FY21, underlying EBITDA of $35.7m (down 27%) and an NPAT of $21.1m (down 21%). Its sales margin fell from 14.4% to 10.1%. And bear in mind that FY22 included new stores that were not open in FY21 – like-for-like sales experienced a bigger decrease, 3% overall and 9.5% across brick-and-mortar stores specifically. The company estimated 3,192 trading days were lost, resulting in a sales impact of ~$20m.

There were some silver linings, though. Online sales grew 39% compared to FY21 and were 163% higher than FY20. They also accounted for 17.2% of overall sales, a share that has almost doubled in two years. And it paid a dividend of 21.5c per share, representing a 4.2% yield.

So, what does FY23 hold? The company noted that sales in the first 8 weeks were 55% higher than the year before, although FY22's first eight weeks included lockdowns. The company did not provide FY23 guidance. Consensus estimates call for $243.1m in revenue and $68.4m in EBITDA for FY23, up 17% and 92%. For FY24, the market expects $266.6m in revenue and $76.7m in EBITDA, which would be up 9% and 12% from FY23. Universal's multiples for FY24 are very reasonable, at 5.9x EV/EBITDA, 13.5x P/E and 0.6x PEG.

Can Universal Store weather the current environment?

If it can achieve the above figures, the company will undoubtedly re-rate. But the question is whether or not it can? Clearly the biggest threat is the risk of inflation on its consumer cohort, which is why the company did not provide FY23 guidance. There is also the risk of competition. Universal has itself acknowledged that its customers shop across multiple brands, seeking what is new, and that BNPL products and even parents support spending capacity.

But, even if Universal's sales do decline, the company will likely not be caught up with a glut of inventory, like Kogan (ASX: KGN) earlier this year. And bear in mind that it has several features that help it stand out, including same day delivery, personalisation in its web experience and its high-end womenswear brand Perfect Stranger. Perfect Stranger began in 2014 as just another one of its labels. But now, Perfect Stranger is the largest brand and Universal has even opened one store that just sells Perfect Stranger attire. The company's plan is to have four by December 2022. And ultimately, Universal sells clothing for major events, many of which were postponed during COVID, but have been back into full swing in 2022.

As a demographic that has lost so much of their lives in two years, Universal's customers will be keen to make up for lost time. So, notwithstanding the risk of inflation, we are prepared to give Universal Store the benefit of the doubt, and four stars, for all the reasons above.

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