

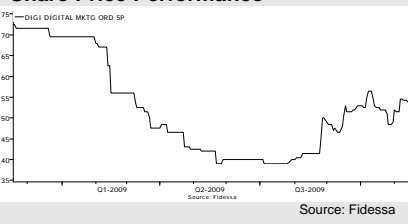
23 NOVEMBER 2009

BUY

Price at 20 Nov 2009 (GBP) 54
Price Target (GBP) 90
52-week range (GBP) 39 - 73

Reuter: DIGI.L Bloomberg: DIGI LN
Exchange: AIM Ticker: DIGI

Share Price Performance



Performance(%)	1m	3m	12m
Absolute	+2	+29	-26

Stock Data

Market cap (£m)	36.2
Shares outstanding (m)	67.4

Key Indicators

Net debt (£'m)	6.1
EBITDA margin (%)	20.6

Activities

Digital marketing services

Directors

Stephen Davidson	Chairman
Ben Langdon	CEO
Keith Sadler	CFO

Significant Share Holders

Mayfair Ltd	24.46%
G & H Stevens	10.42%
M Boddy	7.30%
A Gardner	7.30%
C Buddery	5.69%
J Riddell	5.0%
Insight Asset Management	4.31%
K Riddell	4.15%
Tudor Capital	3.13%
Total	72.1%

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INTERIM RESULTS •

Digital Marketing Group

They will not be cheap for much longer

Against a backdrop of continuing contraction in advertising spend Digital Marketing Group (DIGI) has delivered a robust set of results for the six months to September 2009.

Gross profit reduced to £17.4m from £18.7m in H2 08. The weakness relates specifically to a contraction in demand for data analytics from financial services clients. However, online marketing and direct marketing have not been as badly hit. In particular, Cybercom the e-commerce business acquired in October 2008, delivered 34% y-o-y growth. New product launches and cross-referral sales have helped reduce the impact of the recession. DIGI has seen considerable interest from the launch of its Digital Brain Search, its ppc product. This could become an important profit stream going forward given its high margins and scalability.

EBITDA contracted only marginally from £3.8m for the same period a year earlier to £3.6m as a result of aggressive cost cutting measures by management. Like-for-like costs have reduced by £4.25m from £20.8m to £16.7m mainly due to of headcount reduction. Adjusted eps was 3.2p versus 3.7p a year earlier due to higher financing costs following the acquisitions of Gasbox and Cybercom in October 2008.

We have trimmed our FY10 PBT forecasts from £7.4m to £6.5m but remain very optimistic regarding the Company's short and medium term performance. The Marketers' Internet Ad Barometer's recent findings support the well recognised fact that online spend continue to win share of the total advertising spend. This coupled with a general growth in advertising as the economy recovers creates very positive conditions for DIGI. As the number one digital marketing agency in the UK, DIGI is extremely well positioned to benefit from a recovery. Its streamlined cost base should result in an uplift in margins as well.

DIGI has also proved that it can be trusted to pay down debt and successfully integrate acquisitions. We expect the Group to finish the year with £3.8m of net debt which includes the receipt of £1m income from a partial settlement of a contractual claim.

DIGI shares trade on a PER of 9.8x March 2010 and an EV/EBITDA of 4.9x. As soon as it is clear that earnings momentum has returned we believe the stock should experience a re-rating. A rating of 15x March 2010 gives a target price of 82.5p. BUY.

Forecasts and ratios

Year End March	2008A	2009A	2010E
Gross profit (£'m)	33.1	41.6	43.0
EBITDA (£'m)	7.4	9.3	8.0
PBT (£'m)	6.3	8.0	6.5
Basic EPS (p)	7.3	8.6	6.9
Diluted EPS (p)	5.8	7.2	5.5
% Change	42	19	-24
PER (x) (Diluted eps)	6.9	5.6	9.8

Source: Cenkos securities estimates, company data

Outlook – Bright prospects

DIGI is increasingly recognised as a unified brand and a leading provider of digital marketing services in the UK and continues to win blue chip clients. We believe that DIGI's prospects are bright for four main reasons.

- DIGI will continue to benefit from the switch to digital formats. This Christmas is expected to be a particularly buoyant one for online retailers even though growth in consumer spending is expected to be subdued. This in turn will increase demand for digital advertising.
- Growth will return to the UK economy over the next year. Growth in advertising spend will return with it.
- As the largest digital marketing agency DIGI will proportionately benefit from this trend.
- DIGI is continuing to innovate and launch new products. This will enable clients to extract even more value from their digital marketing spend and help it maintain its competitive edge.

For the above reasons we are confident that earnings momentum will resume in FY 11. DIGI's shares will rise to reflect this. We re-affirm our BUY recommendation.

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