

## Corporate

 Current price **1.5p**

 Sector **Support Services**

 Code **REAT.L**

 AIM **AIM**

### Share Performance



Source: Thomson Reuters, Allenby Capital

### Share Data

 Market Cap (£m) **7.5**

 Shares in issue (m) **498.5**

52 weeks	High	Low
	<b>1.8p</b>	<b>0.55p</b>

 Financial year end **September**

Source: Company Data, Allenby Capital

### Key Shareholders

 Octopus Investments Noms **17.14%**

 Helium Rising Stars Fund **16.17%**

 Premier Miton **8.10%**

 Jonathan Whitmore **5.29%**

 George Stavrinidis **3.32%**

Source: Company Data, Allenby Capital

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## REACT Group plc (REAT.L)

### *A year of strong growth and sustainable profitability*

REACT Group plc (REACT), the specialists in deep cleaning services for customers in the public and private sectors, has announced encouraging full year results, marginally ahead of our increased forecasts and a significant turnaround from the losses reported in previous years. Cash balances at the year-end were also substantially higher than forecast at £1.8m. The new management team has delivered on its promises in what has been a challenging year and we continue to remain very positive on the prospects for the Group. We have introduced forecasts for FY2021 but at this stage, with so much uncertainty we have set our expectations prudently. Nevertheless, the year has started strongly and our projections, supported by a high level of recurring revenue and margin improvement, still anticipates a more than doubling of EBITDA and could be raised as REACT progresses through the year.

- A year of promises delivered** – Under its new management team, REACT has delivered a strong set of results for the year ended September 2020. Previous year losses have been turned around and a maiden profit reported, driven by strong trading across all three Group segments, Contract Maintenance (CM), Contract Reactive (CR) and Ad Hoc (AH), the latter including REACT's COVID-19 decontamination work, which management has separated out and accounted for c.10% of revenue.
- Strong revenue growth and much improved margins** – With a more efficient sales and marketing process, revenues in each segment were strong with CM reporting a rise of 74%, AH (boosted by COVID work) up 136% while CR reported a more modest rise of 1% being impacted by COVID restrictions on its work. However, gross margins still improved in this segment as did margins in the other two. Overall, margins improved by 480bps to 33.2%, now more representative of likely margins going forward.
- New management team reinvigorating the business and prospects** - We would reiterate that historically, REACT had been held back by poor management and an almost complete lack of investment in sales and marketing and has therefore only scratched the surface of potential demand for its specialist services. REACT is still an early-stage company but these results give an indication of what the new team can deliver and our forecasts for 2021 reinforce this belief.
- A strong start to the year but forecasts are set prudently** – Management reports that the Group has made a strong start to the year with profit and cash generation in Q1 ahead of the same period last year. That said, with so much uncertainty around we have pitched our forecasts for FY2021 at a conservative level and these will be reviewed as we progress through the year. Nevertheless, we still anticipate a reasonable level of revenue growth, (c.18%), a further modest improvement in gross margins and a relatively flat fixed cost base. All of which lead us to anticipate EBITDA moving up from £261k to £555k with solid cash generation being achieved. We look forward to another good year from REACT.

### Year End: September

(£000)	2018A	2019A	2020A	2021E
REVENUE	3,295	3,103	4,360	5,160
EBITDA (after exceptionals)	(601)	(131)	261	555
PROFIT/(LOSS) BEFORE TAX	(614)	(178)	188	505
EPS (p)	(0.21)	(0.04)	0.04	0.10
PER (x)	-	-	34.6	14.6
NET CASH	423	440	1,783	2,012

Source: REACT Group plc; Allenby Capital. Allenby Capital acts as Nomad and Broker to REACT Group plc (REAT.L). Please refer to the last page of this communication for all required disclosures and risk warnings.

## Wholesale reversal of 2019 losses

### Provision of deep cleaning services to private and public sector

REACT Group (REACT) is a specialist provider of rapid response, deep cleaning and emergency decontamination services, providing 24/7 fast response service to a range of customers such as Hospitals, Rail, HM Prison Service, Local Authorities and UK Police Services as well as working closely with a number of facilities management companies.

### Impressive reversal of losses and the achievement of a maiden profit

In just its second trading year under the current management team and the first since the business was restructured, REACT has posted a resounding reversal of the losses reported a year ago and a maiden profit. This reversal was purely organic and was achieved despite the challenges posed by the COVID-19 pandemic and in some cases the opportunities for additional business that COVID-19 provided.

#### EXHIBIT 1: SUMMARY FINANCIALS

Years to September	2019	2020	% change
	£000	£000	
Revenue	3,103	4,360	40.5%
Gross profit	885	1,449	63.7%
GP margin	28.5%	33.2%	16.5%
Other income	0	70	
Administrative expenses	-1,011	-1,258	24.4%
as a % of revenue	32.6%	28.9%	
<b>EBITDA (after exceptionals)</b>	<b>-131</b>	<b>261</b>	
EBITDA margin	-4.2%	6.0%	
D&A	-52	-50	-3.8%
Finance	0	-23	
<b>Profit/(loss) before tax</b>	<b>-178</b>	<b>188</b>	
PBT margin	-5.7%	4.3%	
Basic EPS (p)	-0.04	0.04	
<b>Net cash</b>	<b>440</b>	<b>1,783</b>	305.2%

Source: React

### Revenues ahead by 40.5%...

Overall, revenues grew by 40.5% yoy to £4.4m with that growth driven by a number of factors including successful and stronger marketing of the Group's services, additional work from COVID-related cleaning services and the benefit of a significant element of revenues that are recurring in nature.

### ...gross profit by 63.7%...

Gross profit improved by 63.7% to £1.4m with gross margins improving by 470bps to 33.2% and are now more indicative of the sort of margins this business ought to be generating. The improvement was also generated by focussing on higher margin business opportunities and eliminating unprofitable low margin work.

Administrative expenses rose by 24.4% to £1.3m but the rate of increase was more modest than those of revenues or gross profit. As a percentage of revenues overheads fell from 32.6% to 28.9% indicating an increase in business efficiency, including the use of Company service staff rather than third party contractors together with enhanced operational gearing within the business. The new management team has also instigated a more disciplined sales process with a much greater control and understanding of the cost base which will be reflected in this and future years.

### ...leading to a maiden profit of £188k

After depreciation, amortisation and finance costs the Group ended the year generating a maiden pre-tax profit of £188,000 versus a loss of £178,000. The Group ended the year with no borrowings and with cash on the balance sheet of £1.8m, helped in part by the placing of ordinary shares in June 2020 which raised a total of £1.1m.

## Segmental analysis

EXHIBIT 2: SEGMENTATION												
	Year to Sep 2019				Year to Sep 2020							
	Contract	Contract	Ad Hoc	Total	Contract	%	Contract	%	Ad Hoc	%	Total	%
	Maintenance	Reactive			Maintenance	chg.	Reactive	chg.		chg.		chg.
	£000	£000	£000	£000	£000		£000		£000		£000	
Revenue	974	1,751	378	3,103	1,694	73.9%	1,775	1.4%	891	135.7%	4,361	40.5%
Gross profit	266	500	119	885	516	94.0%	561	12.2%	372	212.6%	1,450	63.8%
GP margin	27.3%	28.6%	31.5%	28.5%	30.5%	11.5%	31.6%	10.7%	41.8%	32.6%	33.2%	16.6%
Admin exp	-321	-603	-144	-1,068	-441	37.4%	-479	-20.6%	-318	120.8%	-1,238	15.9%
Op profit/(loss)	-55	-103	-25	-183	75		82		54		212	
OP margin	-	-	-	-	4.4%		4.6%		6.1%		4.9%	

Source: React

The Group currently operates under three main areas of business:

- **Contract Maintenance**
- **Contract Reactive, and**
- **Ad Hoc**

The first two segments, Contract Maintenance and Contract Reactive both enjoy strong **recurring** revenue while all three segments reported an increase in revenues, gross profit, gross margin and operating profit. We discuss each segment below.

EXHIBIT 3: PERCENTAGE CONTRIBUTION TO REVENUES AND GROSS PROFIT BY SEGMENT



Source: REACT

### Contract Maintenance

This segment accounted for 39% of Group revenues (2019: 31%) and 36% of gross profit (2019: 30%) and represents regular work done for customers under contracts which can run from one to five years offering good visibility and recurring revenue streams. Work done includes deep cleaning for the healthcare, rail and road sectors.

### Contract Maintenance revenues up 73.9% and gross profit 94%

In the year to September 2020 the segment grew revenues by 73.9% to £1.7m and delivered a 94% increase in gross profit to £516,000 with a gross margin of 30.5%, a 320 bps increase over the previous year.

Management noted this performance as “pleasing” in that it demonstrated the team’s ability during a challenging period to remain focused on its core objective of improving the quality and recurring nature of the business.

The process for winning new business is either through upselling to an existing customer or through a conventional bid & tender process.

#### **Contract Reactive**

This activity accounted for 41% of Group revenues (2019: 56%) and 39% of gross profit (2019: 56%) and provides deep cleaning services where REACT is the first responder to an on-call emergency response service operating under a contracted framework agreement typically on a 24/7/365 basis. This segment also enjoys recurring revenues even though it may not enjoy the same level of revenue visibility as Contract Maintenance.

Examples include the work done in the rail sector for multiple customers (e.g. deep clean following animal collisions or suicides, graffiti removal, etc.), housing associations, the judiciary (cell & vehicle cleans & decontaminations), highways to clear up after road traffic accidents, graffiti removal, fly-tip clearances, etc.

#### **Contract Reactive revenues up 1.4% but with a 12.2% increase in GP**

In the year to September 2020 the segment grew revenues by just 1.4% to £1.8m but delivered a 12.2% increase in gross profit to £561,000 with a gross margin of 31.6%, a 300 bps increase over the previous year. The reason behind the more modest increase in revenues was due to a temporary reduction in demand due to COVID restrictions.

In particular, the Group saw temporary drops in the judiciary and police sectors where it carries out a significant amount of deep cleaning work relating to cells, courts and transport vehicles. Additionally, the segment also experienced a decline in the housing sector where it would typically carry out void cleans, deep cleans and needle picks.

Management notes that although it saw an encouraging resumption of work in these sectors, this reduced once again, post year-end as lockdown restrictions intensified.

The process for winning new business here is similar to Contract Maintenance, either through upselling to an existing customer or through a conventional bid & tender process.

#### **Ad Hoc**

This activity accounted for 20% of Group revenues (2019: 12%) and 39% of gross profit (2019: 13%) and provides deep cleaning services to typically one-off situations within a framework agreement. Services can be diverse and include fly-tipping, void clearance and COVID-19 decontaminations. Revenues in this segment grew by 135% and gross profit by 213% helped in part by COVID decontamination work.

The Group took the decision that as COVID-19 work was likely to be of a relatively short/mid-term nature, revenues related to this work would be recorded under the Ad Hoc segment.

#### **Revenues up 135% in part due to COVID decontamination work and gross profit ahead by 213%**

#### **COVID decontamination work accounted for £444k of revenue or c.10% of Group revenue**

To this end it has segmented out the COVID-19 decontamination work to provide a better understating of the overall position. In the year to September 2020, COVID-related work generated £444,000 of revenue replacing some of the work lost to the temporary closure of some Contract Reactive and other Ad Hoc business.

Clearly this COVID work will not be recurring but to put it into context it only represented some 10% of total Group revenues and while we expect the business to largely disappear in the latter part of FY 2021 it will be replaced by a resumption of activity temporarily lost in the two segments referred to above.

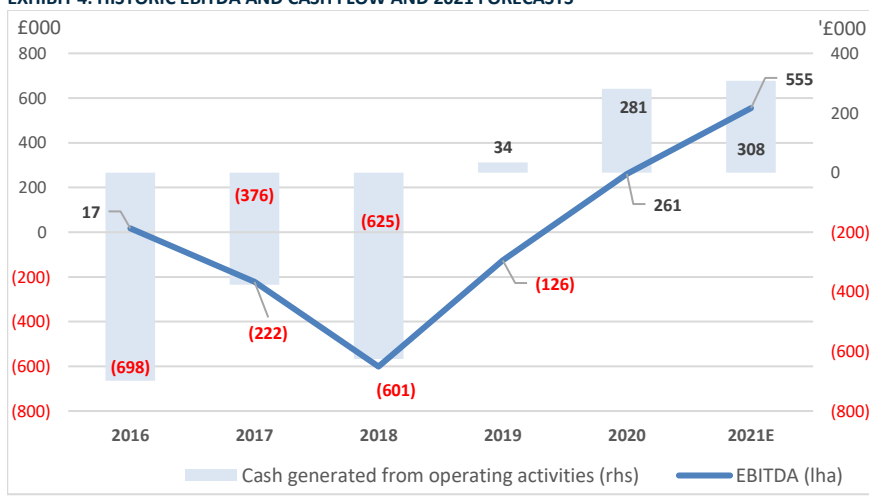
We would also point out that the professional nature and quality of service provided under the COVID decontamination regimes sowed seeds with those customers who may not have used REACT's services previously and therefore may generate growth in other areas of the Group's businesses in the future.

## Conclusion and forecasts

**A very encouraging result from the new management team**

We are greatly encouraged by the strong turnaround delivered by the new management team who were assembled variously between early 2019 and 2020. The team have made an immediate and impressive difference to the operation of the business which is now being run on sensible basis by experienced professionals. The chart below illustrates in graphic detail the impressive turnaround that the team has achieved and we are confident that there is much more to come.

**EXHIBIT 4: HISTORIC EBITDA AND CASH FLOW AND 2021 FORECASTS**



Source: REACT; Allenby

**Profit and cash generation up strongly in Q1**

The Group has made a good start to the year with profit and cash generation in the first quarter ahead of the comparative period last year, with the former running at a record level.

**Many unknowns still – hence cautious forecasts for FY2021...**

However, with so much still unknown about the future challenges and opportunities deriving from the pandemic and the likely market demand as we move out of lockdown, our forecasts at this stage must be limited to the current year only and even then, issued with a great deal of caution and prudence built in.

**...however we are still projecting a more than doubling of EBITDA...**

Even so, with a strong element of recurring revenue, we feel confident enough to project revenue growth of 18% to £5.2m, a further, but smaller, improvement in gross margin to 35.9% to give a gross profit of £1.85m and with a relatively flat fixed overhead generating EBITDA of £555,000, an increase of 113% over FY2020.

Even on these prudent forecasts, on share capital as increased by the June 2020 fund raise, we are forecasting basic EPS of 0.10p per share which at the current share price of 1.475p equates to a PER of 14.6x earnings and an EV/EBITDA of 9.6x.

**...and to be cash generative**

We believe the Company will continue to generate cash in the current financial year and corporate activity aside we are looking for cash to increase from £1.8m at September 2020 to over £2m by September 2021.

**Well positioned with more to come both organically and from potential acquisitions**

REACT is still an early-stage company but we are encouraged by the growth that has already been achieved and are confident of much more still to come. We believe management has only scratched the surface of the Group's potential and will extend its market share through organic growth going forward and possibly through strategic acquisitions as it looks to expand activities within its chosen sector.

## Detailed financials and forecasts

## EXHIBIT 5: INCOME STATEMENT AND FORECASTS

Y/E September	£000 FY 2018A	£000 FY 2019A	£000 FY 2020A	£000 FY 2021E
<b>UNDERLYING</b>				
Revenue	3,295	3,103	4,360	5,160
Cost of sales	-2,602	-2,218	-2,911	-3,310
<b>Gross profit</b>	<b>693</b>	<b>885</b>	<b>1,449</b>	<b>1,850</b>
<i>margin</i>	21.0%	28.5%	33.2%	35.9%
Administrative costs	-1,294	-1,011	-1,258	-1,295
<i>as a % of revenue</i>	39.3%	32.6%	28.9%	25.1%
<b>EBITDA (before exceptional items)</b>	<b>-601</b>	<b>-126</b>	<b>261</b>	<b>555</b>
<i>margin</i>	-18.2%	-4.1%	6.0%	10.8%
Depreciation & Amortisation	-13	-52	-50	-50
<b>Underlying operating profit/(loss)</b>	<b>-614</b>	<b>-178</b>	<b>211</b>	<b>505</b>
<i>margin</i>	-18.6%	-5.7%	4.8%	9.8%
Interest	0	0	-23	0
<b>Underlying profit/(loss) before tax</b>	<b>-614</b>	<b>-178</b>	<b>188</b>	<b>505</b>
Tax	0	0	0	0
Underlying post tax profit/(loss)	-614	-178	188	505
<b>STATUTORY</b>				
Underlying operating profit/(loss)	-614	-178	211	505
Exceptional items	-1,337	-5	0	0
Interest	0	0	-23	0
<b>Statutory profit/(loss) before tax</b>	<b>-1,951</b>	<b>-183</b>	<b>188</b>	<b>505</b>
Tax	0	0	0	0
Statutory post tax profit/(loss)	-1,951	-183	188	505
WAS (m)	287.298	415.408	441.292	498.509
WAS FD (m)	287.298	415.408	506.357	563.574
Year-end shares (m)	415.408	415.408	498.509	498.509
Underlying EPS (p)	(0.21)	(0.04)	0.04	0.10
Statutory EPS (p)	(0.68)	(0.04)	0.04	0.10

Source: React; Allenby

## EXHIBIT 6: BALANCE SHEET AND FORECASTS

	£000	£000	£000	£000
Y/E September	FY 2018A	FY 2019A	FY 2020A	FY 2021E
<b>Non-current assets</b>				
Intangible assets	174	174	174	174
PP&E	116	81	85	85
Right of use assets	0	0	27	27
<b>Total non-current assets</b>	<b>290</b>	<b>255</b>	<b>286</b>	<b>286</b>
<b>Current assets</b>				
Trade & other receivables	1,141	718	1,089	1,589
Cash	423	440	1,783	2,012
<b>Total current assets</b>	<b>1,564</b>	<b>1,158</b>	<b>2,872</b>	<b>3,601</b>
<b>Total assets</b>	<b>1,854</b>	<b>1,413</b>	<b>3,158</b>	<b>3,887</b>
<b>Current liabilities</b>				
Trade payables	-793	-535	-924	-1,174
Lease liabilities	0	0	-13	-13
<b>Total current liabilities</b>	<b>-793</b>	<b>-535</b>	<b>-937</b>	<b>-1,187</b>
<b>Non-current liabilities</b>				
Deferred tax	0	0	0	0
Lease liabilities	0	0	-30	-30
<b>Total non-current liabilities</b>	<b>0</b>	<b>0</b>	<b>-30</b>	<b>-30</b>
<b>Total liabilities</b>	<b>-793</b>	<b>-535</b>	<b>-967</b>	<b>-1,217</b>
<b>Net current assets</b>	<b>771</b>	<b>623</b>	<b>1,935</b>	<b>2,414</b>
<b>Net assets</b>	<b>1,061</b>	<b>878</b>	<b>2,191</b>	<b>2,670</b>
<b>BALANCE SHEET RATIOS</b>				
	£000	£000	£000	£000
Y/E September	FY 2018A	FY 2019A	FY 2020A	FY 2021E
Long-term financial debts	-	-	-	-
Short term financial debts	-	-	-	-
Gross (debt)	-	-	-	-
Cash and cash equivalents	423	440	1,783	2,012
Net (debt) / cash	423	440	1,783	2,012
Acid test (Current Assets less inventory / Current Liabilities)	2.0	2.2	3.1	3.0

Source: React; Allenby

## EXHIBIT 7: CASH FLOW AND FORECASTS

	£000	£000	£000	£000
Y/E September	FY 2018A	FY 2019A	FY 2020A	FY 2021E
<b>Operating profit/(loss)</b>	<b>-1,951</b>	<b>-183</b>	<b>188</b>	<b>505</b>
Depreciation	1,350	52	50	50
Share based payments	0	2	3	3
Loss on disposal of fixed assets	10	-3	1	0
<i>(Increase)/decrease in receivables</i>	<i>-649</i>	<i>441</i>	<i>-371</i>	<i>-500</i>
<i>(Decrease)/increase in payables</i>	<i>615</i>	<i>-275</i>	<i>389</i>	<i>250</i>
<b>Net change in WC</b>	<b>-34</b>	<b>166</b>	<b>18</b>	<b>-250</b>
Finance	0	0	21	0
<b>Net cash inflow/(outflow) from operating activities</b>	<b>-625</b>	<b>34</b>	<b>281</b>	<b>308</b>
Disposal of fixed assets	20	8	2	0
Capital expenditure	-38	-25	-44	-50
<b>Net cash outflow from investing activities</b>	<b>-18</b>	<b>-17</b>	<b>-42</b>	<b>-50</b>
Proceeds from share issues	420	0	1,246	0
Expense of share issues	-33	0	-113	0
Other loans	69	0	0	0
Other loan repayments	-21	0	0	0
Principal paid on lease liabilities	0	0	-29	-29
<b>Net cash inflow/(outflow) from financing activities</b>	<b>435</b>	<b>0</b>	<b>1,104</b>	<b>-29</b>
<b>Increase/(decrease) in cash</b>	<b>-208</b>	<b>17</b>	<b>1,343</b>	<b>229</b>
Cash at start of year	631	423	440	1,783
<b>Cash at end of year</b>	<b>423</b>	<b>440</b>	<b>1,783</b>	<b>2,012</b>

Source: React; Allenby



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