RBG HOLDINGS
PROFESSIONAL SERVICES

13 September 2022

RBGP.L

88p

Market Cap: £83.9m

SHARE PRICE (p)

12m high/low	144p/84p

Source: LSE Data (priced as at prior close)

KEY DATA

Net (Debt)/Cash	£(17.3)m *(at 30/06/22)*
Enterprise value	£101.2m
Index/market	AIM
Next news	Trading update Jan 23
Shares in Issue (m)	95.3
Chairman	Keith Hamill
Chief Executive	Nicola Foulston
Finance Director	Robert Parker

COMPANY DESCRIPTION

RBG is a unique professional services group, with a diversified revenue base and commercially driven management team.

www.rbgholdings.co.uk

RBG HOLDINGS IS A RESEARCH CLIENT OF PROGRESSIVE

ANALYSTS

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Solid first half shows resilience of model

RBG has reported a solid set of results for H1 22, in line with its July trading update, with strong performance in the core professional services businesses. The group remains on track against our FY22 estimates (revenue of £55.0m and adjusted EBITDA of £16.9m), with an expected positive skew in H2 from Convex and Lionfish. The integration of Memery Crystal (MC) is complete and the group's diversified professional services revenue model has proved resilient against a continued backdrop of uncertainty. Demand for services across all three businesses remains buoyant, and management is optimistic in its outlook for the year and beyond, despite economic uncertainty. In our view, the valuation appears undemanding given forecast growth, both organic and through bolt-ons, coupled with the significant upside potential from contingent work and litigation finance.

- **Strong financial performance**. Revenue (including gains from litigation) increased 44.8% to £26.6m, at a gross margin of 40.2%. EBITDA increased 31.8% to £6.8m. The EBITDA margin, as expected, was 25.6% (H1 21: 28.1%), reflecting the skew towards fee-paying legal services rather than dispute resolution following the acquisition of MC. Net Debt at the period end was £17.3m, up from £14.4m at the end of December 2021, including payment of £2.2m for the deferred consideration of MC.

- **Delivering on strategy.** RBG is a well-diversified professional services group delivering high margins, with further margin improvement expected this year. The group is confident it can achieve its medium-term target of an EBITDA margin of 35% or above.

- **RBG remains on track to meet current forecasts for the full year.** With consistent demand for all group services, and significant strategic progress, RBG has entered the second half with good momentum. Strong demand for legal services is continuing and contributions from Convex and Lionfish are expected to be second-half weighted, underpinning management's confidence in current market expectations.

The outlook statement strikes a confident tone, both in terms of current trading, despite the economic backdrop, and medium-term growth plans. In our view, some investor misperception around the investment strategy has weighed on the shares. However, we view the business model as simple. The core business of legal services (90% of revenue) is profitable and cash-generative, allowing investment in related, higher-margin areas (Convex and Lionfish). This also means that shares easily qualify for Inheritance Tax relief (IHT). We look forward to further positive updates in due course.

FYE DEC (£M)	2019	2020	2021	2022E	2023E
Revenue	23.7	25.3	47.2	55.0	59.6
Adj EBITDA	9.4	7.2	13.8	16.9	20.0
Fully Adj PBT	7.6	4.8	10.1	12.3	15.7
Fully Adj Dil EPS (p)	7.5	4.2	8.5	9.8	12.7
EV/Sales (x)	4.3x	4.0x	2.1x	1.8x	1.7x
EV/EBITDA (x)	10.7x	14.0x	7.3x	5.9x	5.0x
PER (x)	11.7x	20.9x	10.4x	8.9x	6.9x

Source: Company Information and Progressive Equity Research estimates.

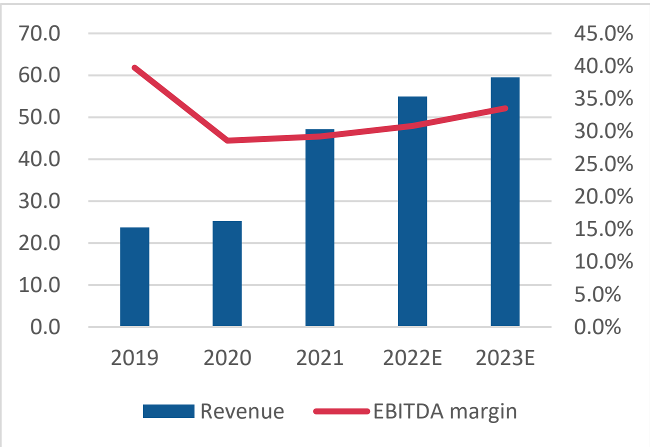
Robust results – strategic progress drives growth

RBG’s solid H1 results contained no significant surprises, following the trading update issued in mid-July. Revenue for H1, including gains from litigation assets, increased by 44.8% to £26.6m (H1 21: £18.3m) and EBITDA by 31.8% to £6.8m (H1 21: £5.2m). Net Debt at the period end was £17.3m, up from £14.4m at the end of December 2021, including payment of £2.2m for the deferred consideration of MC.

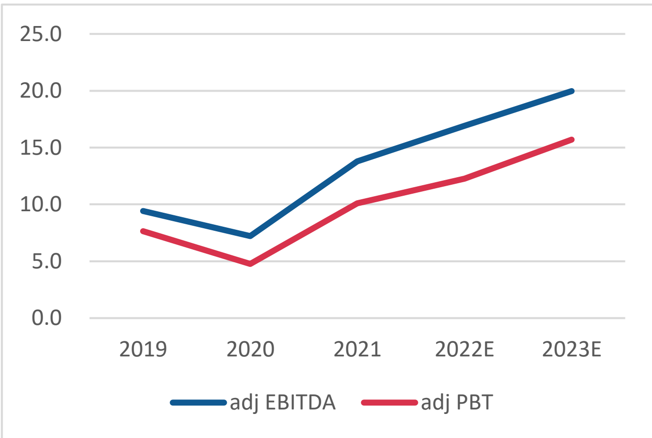
The core legal services business continues to drive profitable top-line growth. The medium- and long-term drivers to RBG’s growth appear fully intact, with strong demand for legal services continuing and contributions from Convex and Lionfish expected to be second-half weighted, underpinning management’s confidence in current market expectations.

In our view, the group’s strategy since it floated in 2018 remains clear: to build a professional services group of complementary, specialist, high-margin businesses that are experts in their respective fields. The track record suggests that this strategy is delivering.

Revenue (£m) and adj EBITDA margin (%)



Adj PBT and adj EBITDA (£m)



Source: RBG, Progressive Equity Research

In our view, investor misperception surrounding the investment strategy and how the businesses hang together has weighed on the share price. However, we believe that the business model is simple. The core business of legal services (90% of revenue) is profitable and cash-generative, allowing investment into closely related, higher-margin areas (Convex and Lionfish). This also means that shares easily qualify for Inheritance Tax relief.

RBG’s expertise in dispute resolution is being leveraged to maximise potential returns by selectively investing in contingent asset classes such as litigation, both in-house and third party via Lionfish. Meaningful progress has been made over the past year in terms of adding scale and breadth to RBG Legal Services via the Memery Crystal acquisition.

LionFish recently developed a new flexible capital arrangement to support its growth rather than using the group’s balance sheet and is currently funding 11 active cases. We would expect a settlement to drop through in the second half of the year based on the average duration two to three years. Convex Capital, the M&A advisory business, is benefitting from strong levels of M&A activity, with good visibility on transactions going into the second half and nine deals at various stages of completion.

Balance sheet and cashflows

As at 30 June, RBG had Net Debt of £17.3m, up from £9.8m the year before and £14.4m at the year-end. This includes the deferred consideration from MC of £2.4m. The group has a revolving credit facility of £15m and an acquisition term loan of £10m repayable over five years, with £2m already paid down.

Cash conversion in 1H 22 was strong. The group's measure of cash conversion, which is underlying profit after tax into free cash flow, improved to 90% (H1 21: 71%) for the six-month period. This increase is ahead of management's target of 75% due to the strong focus on cash conversion coupled with stronger first-half trading, which historically is back-end loaded.

The commitment to dividend growth remains. The interim dividend of 2.0p has been held flat on FY21's interim payment, reflecting expectations of the second-half weighting. The FY21 full-year dividend was 5p per share; we are forecasting 6p per share for FY22, giving a forecast yield of 7.1%.

Since RBG floated in 2018, management has used equity participation to part finance acquisitions with long-term lock-ins, with potential for employees to significantly increase earnings through a combination of basic salary, dividends and, at the right exit point, capital appreciation. RBG is therefore perhaps a stock that investors should regard as relatively well-protected from the scourge of inflation.

Operating expenses

Management continues to limit the impact of inflation. H1-on-H1 overheads increased from £13.2m to £19.8m, with higher staff costs being one of the primary drivers. Total staff costs for the first half of 2022 were £15.9m (H1 21: £10.6m), which includes £2.1m for Convex (£0.7m in relation to the Directors bonus scheme of completed deals), £0.3m for LionFish and £12.3m for RBGLS. The average number of employees was 216 (H1 21: 121). We regard this as a very creditable result given the increase in employees following the MC acquisition.

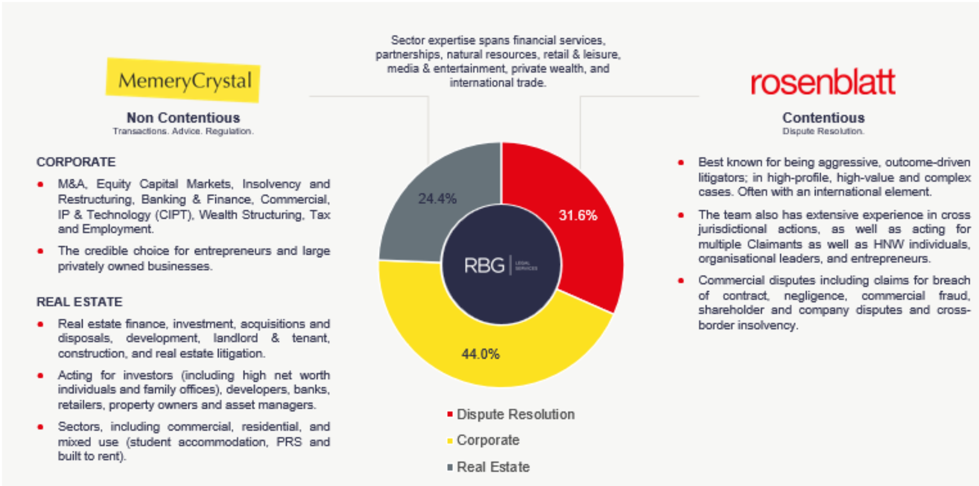
RBG Legal Services Limited (RBGLS)

Given strong demand for legal services, revenue (including gains on the sale of litigation assets) was up 74.2% to £22.3m (H1 21: £12.8 million), benefitting from a full six months of MC. The consolidated business has helped diversify the legal services business, which was heavily skewed to dispute resolution rather than regular fee-paying work. The business is now much more balanced, with Dispute Resolution at 31.6% (H1 21: 63.3%) of RBGLS's revenue, Real Estate at 24.4% (H1 21: 17.2%) and Corporate at 44.0% (H1 21: 19.5%).

The average revenue per fee earner was £363k (H1 21: £375k) and remains one of the highest in the industry. The slight reduction reflects the changing business mix highlighted above. This provides a natural hedge to the group's dispute resolution activities, which, while more profitable, are also more contingent.

Based on historical performance, we would expect dispute resolution, the most profitable area of RBGLS, to increase its relative contribution in the second half. It is worth noting that all three areas currently have good momentum; however, in more difficult economic times dispute resolution often experiences an uptick in demand as businesses look to alleviate economic damage through, for example, insurance claims and insolvency disputes.

Legal Services Divisional Split of Business, as at 30 June 2022



Source: RBG

In line with its strategy, RBGLS has increased the amount of contingent work it has taken on, enabled by the group's bigger balance sheet, albeit with bread-and-butter fee-paying work the priority. This is through alternative billing arrangements (ABAs) and direct billing arrangements (DBAs), which generate incremental margins on a successful case outcome. This offers profitable upside to revenue projections, with 13 such cases currently 'live' and contingent WIP of £12.5m as at the half year.

Convex Capital Limited

The acquisition of Convex Capital was part of the Board's strategy to focus on other high-margin professional service areas. Convex Capital is an entrepreneurial, cash-generative business operating across the UK and Europe, and will provide the group with further funds for reinvestment into other high-margin areas.

As at 30 June 2022, Convex Capital had completed five deals and delivered £4.2m of revenue (H1 22: £5.2m). It is worth remembering that this business saw a strong bounce-back result post Covid, making FY21 comparators more difficult.

The strength of its pipeline has enabled Convex Capital to maintain deals through an uncertain first half. The average size of deal is also creeping upwards, at £750k, significantly above the industry average due to the off-market nature of the business. As at 13 September 2021, Convex Capital had 36 active deals, with good visibility on H2 revenue given that nine of these are at various stages of completion.

LionFish Litigation Finance Limited

LionFish was established in 2020 to finance litigation matters being run by other solicitors, in return for a significant return on the outcome of those cases. As such, the group now has two types of litigation investments: RBGLS's own client matters and litigation matters run by third-party solicitors.

The recent flexible capital arrangement provides an alternative source of funding to using the group's balance sheet, with 11 active cases currently funded. We would expect a settlement to drop through in the second half of the year based on the average time to settle of two to three years.

To date, LionFish has sold a percentage of its invested assets, which has generated a profit since inception. We believe LionFish is now at an inflexion point, poised to make considerable returns. However, in our view, the potential future value isn't reflected in RBG's current share price due to the lumpy nature and unpredictable timing. Once further settlements start to flow through (the first was achieved at the targeted 2x investment threshold), we see this as a catalyst to the share price. We also view Lionfish as a potentially attractive investment proposition for a litigation finance competitor.

We believe the market has viewed LionFish as adding complexity to RBG's group strategy. However, we firmly believe that Lionfish represents an opportunity to extract further value from the group's legal and commercial expertise and diversify its sources of income.

Maintaining estimates – shares appear undervalued

The trading outlook restates the message from the July update that RBG is on track to meet full-year market expectations, in line with our current FY22E estimates of revenue at £55.0m and adjusted EBITDA at £16.9m. Taking comfort from these solid interim results, we are maintaining our estimates for FY23, albeit with a second-half weighting.

While acknowledging the volatility of current macroeconomic conditions, management remains optimistic about the remainder of the financial year and the long-term prospects for the group.

Convex has made a positive start to the year and FY22 will benefit from a first 12-month contribution from Memery Crystal, while LionFish will increase in scale under its new investment arrangement and we expect further settlements to come to fruition.

In our view, the current valuation appears undemanding given forecast growth, both organic and through bolt-ons, coupled with the significant upside potential from contingent work and litigation finance. We believe that the business model is simple and effective. The core business of legal services (90% of revenue) is profitable and cash-generative, allowing investment into closely related, higher-margin areas such as Convex and Lionfish. This also means that shares easily qualify for Inheritance Tax relief.

We believe that RBG's diversified revenue model means it is well-positioned to face macroeconomic uncertainty while continuing to deliver growth. We look forward to further positive newsflow from the group.

Financial Summary: RBG Holdings

Year end: December (£m unless shown)

PROFIT & LOSS	**2019**	**2020**	**2021**	**2022E**	**2023E**
Revenue	23.7	25.3	47.2	55.0	59.6
Adj EBITDA	9.4	7.2	13.8	16.9	20.0
Adj EBIT	7.9	5.1	10.8	13.4	16.8
Reported PBT	7.6	7.4	9.2	12.3	15.7
Fully Adj PBT	7.6	4.8	10.1	12.3	15.7
NOPAT	6.3	6.8	7.9	10.6	13.3
Reported EPS (p)	7.5	7.3	7.6	9.8	12.7
Fully Adj Dil EPS (p)	7.5	4.2	8.5	9.8	12.7
Dividend per share (p)	2.0	5.0	5.0	6.0	6.5
CASH FLOW & BALANCE SHEET	**2019**	**2020**	**2021**	**2022E**	**2023E**
Operating cash flow	1.5	9.6	7.2	8.5	14.7
Free Cash flow	(0.7)	6.6	5.7	4.8	10.3
FCF per share (p)	(0.8)	7.7	6.2	5.0	10.8
Acquisitions	(6.0)	(3.0)	(16.6)	0.0	0.0
Disposals	0.0	0.0	0.0	0.0	0.0
Shares issued	0.0	0.0	0.0	0.0	0.0
Net cash flow	(11.4)	11.6	(8.8)	(1.6)	3.2
Overdrafts / borrowings	0.0	10.0	19.1	0.0	0.0
Cash & equivalents	1.9	13.5	4.8	0.0	0.0
Net (Debt)/Cash	1.9	3.5	(14.4)	(16.0)	(12.8)
NAV AND RETURNS	**2019**	**2020**	**2021**	**2022E**	**2023E**
Net asset value	42.4	47.0	60.8	65.3	71.7
NAV/share (p)	51.5	54.9	66.5	68.5	75.2
Net Tangible Asset Value	7.4	6.3	18.5	16.0	13.9
NTAV/share (p)	9.0	7.4	20.2	16.8	14.6
Average equity	38.7	44.7	53.9	63.0	68.5
Post-tax ROE (%)	16.0%	8.0%	14.4%	14.9%	17.7%
METRICS	**2019**	**2020**	**2021**	**2022E**	**2023E**
Revenue growth	90.0%	6.4%	86.7%	16.4%	8.4%
Adj EBITDA growth	119.0%	(23.5%)	91.0%	22.8%	18.0%
Adj EBIT growth	195.6%	(34.7%)	111.2%	23.9%	25.4%
Adj PBT growth	191.6%	(37.7%)	111.7%	21.5%	28.1%
Adj EPS growth	182.9%	(44.0%)	102.3%	15.9%	29.0%
Dividend growth	N/A	150.0%	–	20.0%	8.3%
Adj EBIT margins	32.1%	20.3%	23.0%	24.5%	28.3%
VALUATION	**2019**	**2020**	**2021**	**2022E**	**2023E**
EV/Sales (x)	4.3	4.0	2.1	1.8	1.7
EV/EBITDA (x)	10.7	14.0	7.3	5.9	5.0
EV/NOPAT (x)	15.9	15.0	12.9	9.5	7.6
PER (x)	11.7	20.9	10.4	8.9	6.9
Dividend yield	2.3%	5.7%	5.7%	6.8%	7.4%
FCF yield	(0.9%)	8.8%	7.1%	5.7%	12.4%

Source: Company information and Progressive Equity Research estimates

13 September 2022

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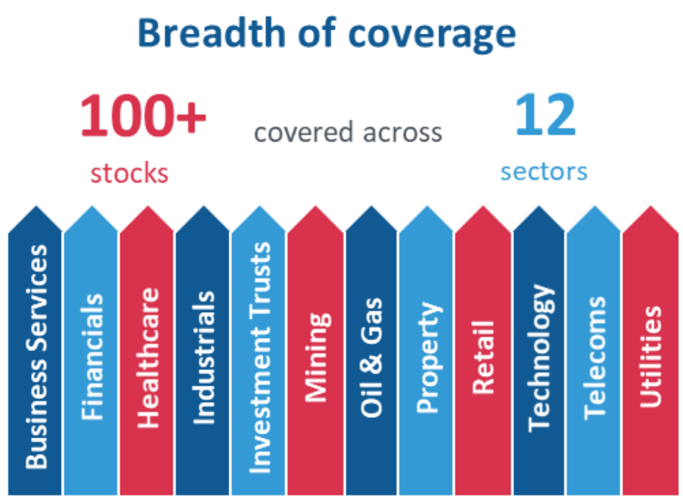

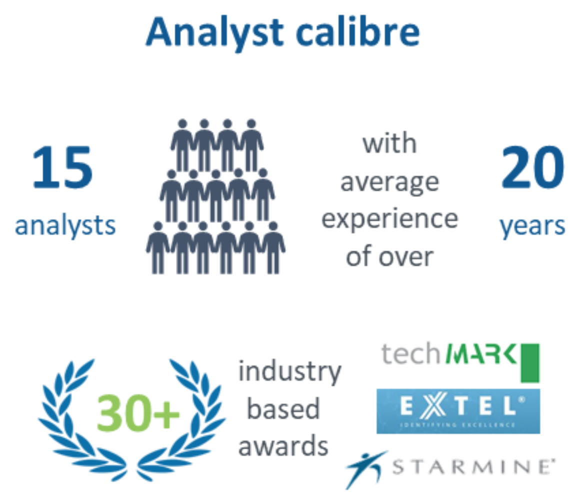

To arrange a meeting with the management team, or for further information about Progressive, please contact:
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