

Well placed to weather even the harshest of storms

30th March 2023

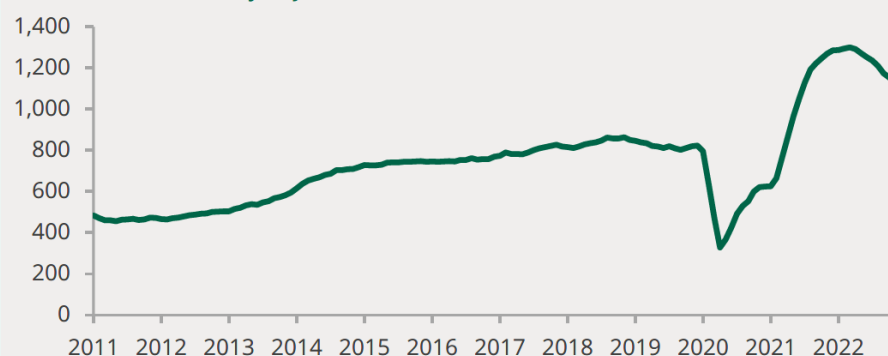
Despite the recent banking crisis, sticky inflation and the ongoing war in Ukraine, the global economy nonetheless continues to chug along at a 3% clip on the back of low unemployment, plentiful jobs, China reopening and the need to rebuild vital infrastructure.

Many high profile software firms are trimming headcount to protect margins & improve efficiency. Yet equally, this is a function of shedding excess pandemic 'fat', as opposed to wholesale trench warfare.

Likewise, **the UK recruitment market** – especially for STEM disciplines – **remains solid** (see below charts). This is **underpinned by robust demand for specialist engineering talent** across the infrastructure (HS2, smart motorways, Rail, Highways, etc), defence (land, air & sea) and energy (e.g. offshore wind and O&G) verticals, more than compensating for some tech softness.

UK job vacancies remain above pre-pandemic levels

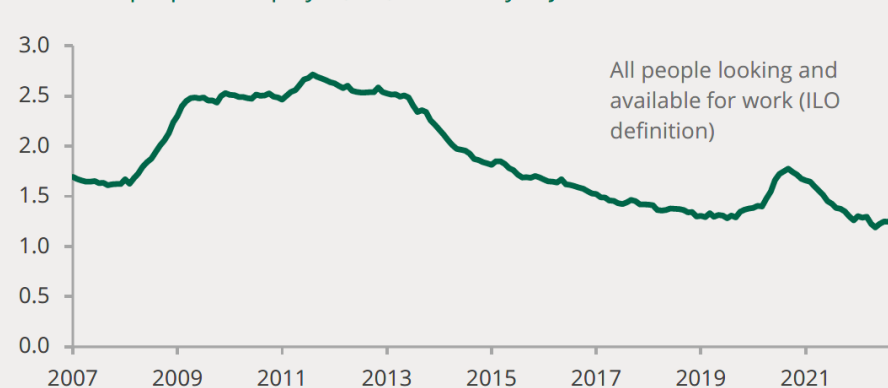
Thousands, seasonally adjusted



Source: ONS

Historically low levels of unemployment (3.7%)

Millions of people unemployed, UK, seasonally adjusted



Source: ONS

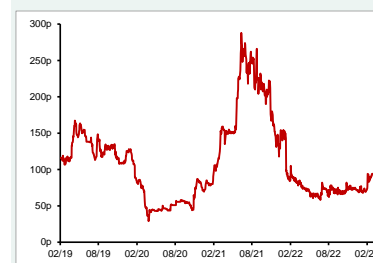
'In line' H1'23 results supported by solid demand

This industry-wide resilience is panning out at specialist STEM recruiter Gattaca – who today reported **in line H1'23 results** (6M ending Jan'23). Underlying NFI climbed **+5.2% to £22.7m** (£21.6m LY) thanks to **two new client wins** and **strategic price initiatives** (+9% contract & 6% perm).

Company Data

EPIC	AIM:GATC
Price (last close)	78p
52 week Hi / Lo	95p/55p
Market cap	£25.2m
Jan'23 statutory net cash (post IFRS16 & £7.0m of non-recourse debt)	£20.9m
Share count	32.3m
ED valuation / share	130p
TNAV/share (Jan'23)	86p

Share Price, p



Source: Yahoo

Description

Gattaca is a specialist STEM (re Science, Technology, Engineering & Mathematics) staffing solutions business. In FY'22, it delivered NFI up 5% to £44.1m (94% UK vs 6% overseas). 67% of NFI comes from temporary assignments (5,150 contractors) with the rest from permanent placements.

Jan'23 headcount was 497, of which 69% were sales related.

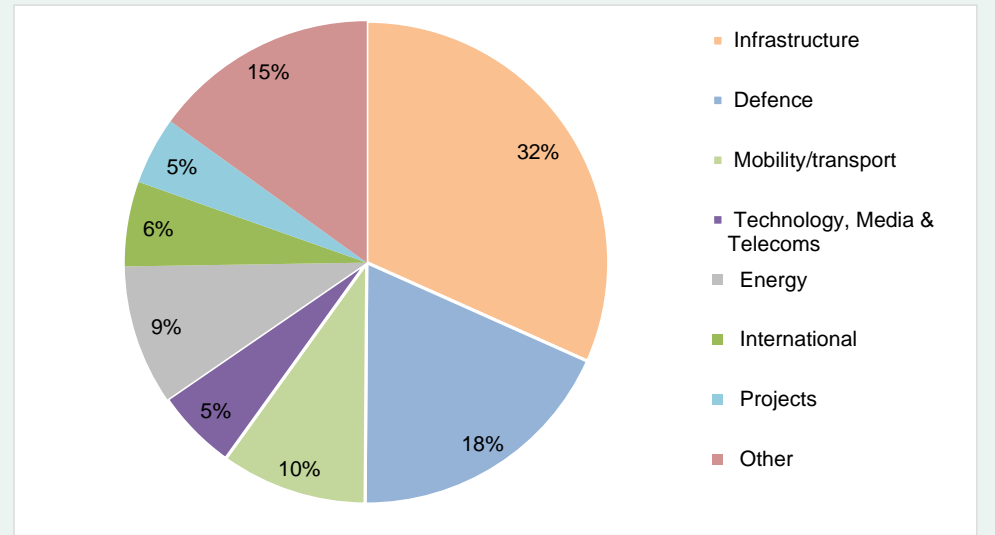
Next news: Y/E trading update Aug'23

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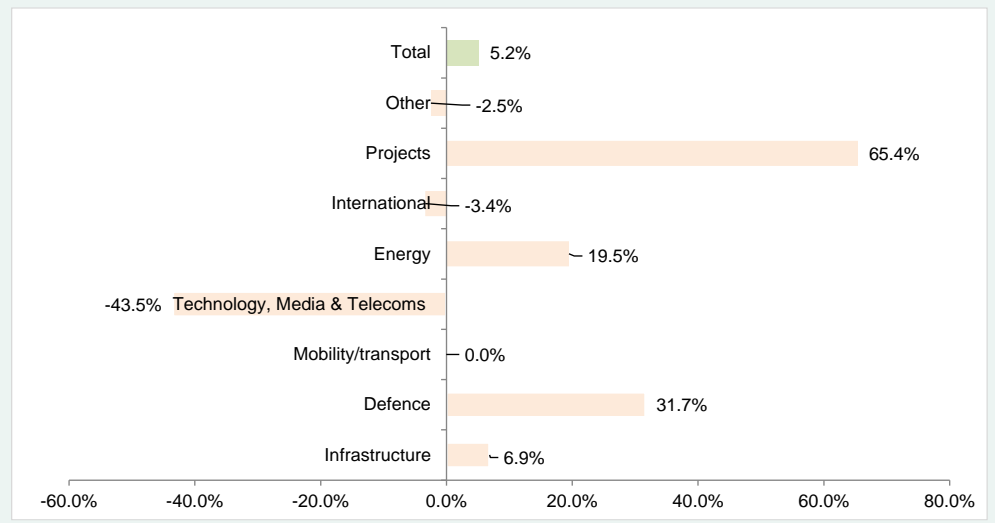
On top, there were **standout performances** (see below) from **defence** (+32%), **energy** (20%) and **infrastructure** (7%) - partly offset by the **shedding of low margin business** (re 2 large accounts) and a not surprisingly less buoyant TMT backdrop (-43.5%, tough YoY comps).

Gattaca H1'23 NFI (£22.7m) sector breakdown



Source: Equity Development

Gattaca H1'23 NFI (£22.7m) sector YoY growth rates



Source: Equity Development

Fortress balance sheet & margin recovery

Importantly too, we believe **the group remains on track** to achieve both its **ongoing turnaround** and **longer-term targets**, after raising fee earner productivity (+14% revs/head), employee engagement and EBIT/NFI margins to +4.2% (-0.5% LY). This has delivered an **H1'23 adjusted PBT and diluted EPS of £0.9m** (-£0.3m LY) & **2.0p** (-0.8p) respectively.

Elsewhere, overheads (eg property, systems, heads, etc) are being centralised, with the associated cost savings (43 fewer heads YoY to 497) being sensibly re-invested into sustainable & profitable growth. For instance, the ratio of sales to support staff closed the period at 69:31 vs 73:27 LY, with the company aiming to ultimately increase this to 75%+.

But that's not all.

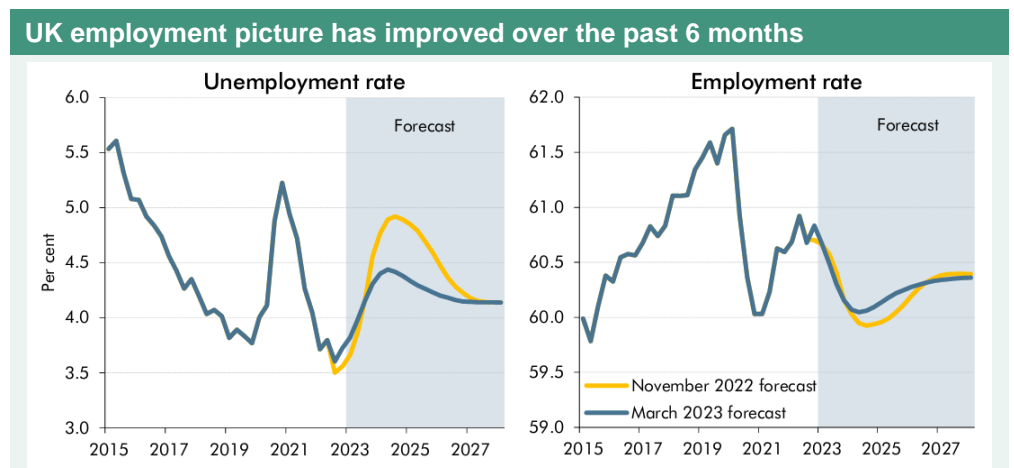
In today's higher interest rate world, **'Cash is King'** again. And in this context, **H1'23 OCF came in at an impressive +£8.8m**, due to improved sales mix (Re turnover was 4% lower at £194.7m) – which likewise nudged up contractor margins to 8.1%. All told, this leaves **net funds** (excluding IFRS16 leases & non-recourse debt) **at £24.0m** (+£4.81m LY) – equivalent to **73p per diluted share**.

Meaning there is **scope to pay a progressive dividend**, once earnings have reached a sustainable footing.

Albeit, the Board are presently conscious of the *"macro-economic uncertainty"* and have seen *"a marginal lengthening of lead times & some hesitation on offers, as clients and candidates become nervous of a potential UK recession in early 2023"*. Hence a **decision to reinstate the dividend will be made at the year-end** (ED Est 1.4p vs 0.0p).

Nevertheless, even in the event of a harder than anticipated slowdown, **we still think Gattaca should be able to outperform its peers**, given its greater STEM & contractor exposure. In fact, this is exactly what happened during and immediately after the 2008-9 GFC.

A hard landing though isn't our base case. In contrast only 2 weeks ago, the Office of Budget Responsibility predicted UK unemployment would peak at 4.4% next year (see below) with the UK avoiding a technical recession (see overleaf).



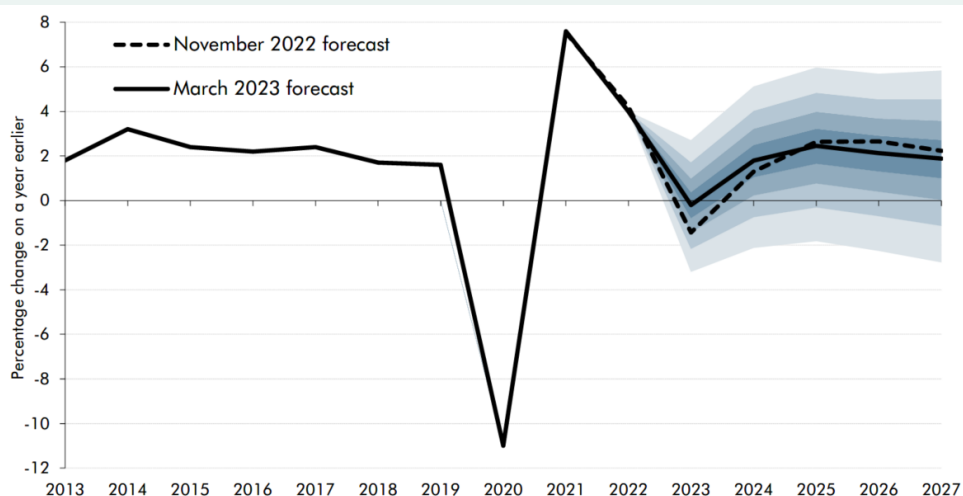
So what does this all mean?

Well, despite the 'windier' economic conditions, we've held our conservative **FY'23 and FY'24 PBT forecasts at £1.8m** (£256k LY) and **£4.25m** respectively on NFI up 5.3% (£46.5m) and 8.9% (£50.6m), along with **reiterating the valuation of 130p/share**.

CEO Matthew Wragg adds: ***"As we continue to build to our full potential, the improvements in culture, staff retention and productivity are signs that we are on the right track to be a stronger business."***

"We continue to remain conscious of the macro-economic environment, which will have naturally slowed our speed of recovery and the markets that we operate in."

Latest UK real GDP forecast



Note: Successive pairs of lighter-shaded areas around our baseline forecast (black line) represent 20 per cent probability bands.

Source: OBR, ONS

Gattaca H1 vs H2 results

£'000s (continuing) - July y/e	Act H1'22	Act H2'22	Act FY22	Act H1'23	Est H2'23	Est FY23
UK	8.9%	5.8%	7.3%	5.8%	5.5%	5.7%
International	-29.8%	-11.2%	-21.2%	-3.4%	4.6%	0.8%
Total underlying NFI	5.3%	4.5%	4.9%	5.2%	5.5%	5.3%
NFI	21,606	22,534	44,140	22,733	23,767	46,500
Adjusted EBITDA	887	1,828	2,715	1,680	2,120	3,800
Adjusted EBIT	-108	613	505	946	1,054	2,000
<i>EBIT/NFI margin</i>	-0.5%	2.7%	1.1%	4.2%	4.4%	4.3%
Underlying overheads	21,714	21,921	43,635	21,787	22,713	44,500
U/L admin as % NFI	100.5%	97.3%	98.9%	95.8%	95.6%	95.7%
Adjusted PBT	-261	517	256	936	864	1,800
Tax	0	-154	-154	-271	-125	-396
Underlying PAT	-261	363	102	665	739	1,404
Adjusted EPS (diluted)	-0.8p	1.1p	0.3p	2.0p	2.3p	4.3p
NFI (LTM) / head (£ks)			81.9			93.6
Overheads / head (£Ks)			81.0			89.5
Headcount	540		539	497		497
<i>U/L tax rate</i>			-60.2%			-22.0%
Non-recourse invoice discounting	-10,400	-9,600	-9,600	-7,000	-7,000	-7,000
Deferred VAT	0	0	0	0	0	0
Cash / (recourse debt) - pre IFRS 16	4,841	15,967	15,967	23,962	19,200	19,200

Source: Equity Development.

Summary projections (£'000s)

Gattaca (continuing operations) (July yearend)	2020 Act £'000s	2021 Act £'000s	2022 Act £'000s	2023 Est £'000s	2024 Est £'000s	2025 Est £'000s
Net Fee Income (NFI) : Gross profit						
UK Engineering & Technology	47,779	38,552	41,361	43,700	47,398	50,869
International	4,977	3,528	2,779	2,800	3,240	3,494
Total	52,756	42,080	44,140	46,500	50,638	54,363
NFI growth rate						
<i>UK Engineering & Technology</i>	10.5%	-19.3%	7.3%	5.7%	8.5%	7.3%
<i>UK Technology</i>	-23.5%					
<i>International</i>	-15.9%	-29.1%	-21.2%	0.8%	15.7%	7.8%
Total NFI growth rate	-21.2%	-20.2%	4.9%	5.3%	8.9%	7.4%
EBITDA	9,413	4,432	2,715	3,800	6,211	8,203
<i>EBITDA/NFI conversion %</i>	17.8%	10.5%	6.2%	8.2%	12.3%	15.1%
UK Engineering & Technology	20,913	12,178	15,463	18,000	19,142	21,284
UK Technology	7,061					
International	1,319	-1,923	-625	-1,000	486	699
Central overheads	-23,125	-12,502	-14,333	-15,000	-15,228	-15,609
Adjusted EBIT	6,168	2,247	505	2,000	4,400	6,374
<i>Total Opex as % NFI</i>	-88.3%	-94.7%	-98.9%	-95.7%	-91.3%	-88.3%
<i>EBIT / NFI margin</i>	11.7%	5.3%	1.1%	4.3%	8.7%	11.7%
Net interest	-1,389	-412	-249	-200	-150	-100
Adjusted PBT	4,779	1,835	256	1,800	4,250	6,274
Tax	-995	-132	-154	-396	-1,063	-1,569
Minorities	0	0	0	0	0	0
Adjusted PAT	3,784	1,703	102	1,404	3,188	4,706
Adjusted diluted EPS	11.7p	5.3p	0.3p	4.3p	9.7p	14.3p
<i>Adjusted EPS growth rate</i>	-57.6%	-55.0%			125.9%	46.9%
Dividend (p)	0.0	1.5	0.0	1.4	3.3	4.8
<i>Dividend yield</i>	0.0%	1.9%	0.0%	1.8%	4.2%	6.1%
Valuation benchmarks						
<i>P/E ratio (diluted)</i>	6.7	14.8		18.1	8.0	5.5
<i>EV/NFI</i>	0.25	0.31	0.29	0.28	0.26	0.24
<i>EV/EBITDA</i>	1.4	2.9	4.8	3.4	2.1	1.6
<i>EV/EBITA (diluted)</i>	2.1	5.8		6.5	3.0	2.0
<i>PEG ratio</i>	-0.12	-0.27			0.06	0.12
<i>Adjusted corporate tax rate</i>	-20.8%	-7.2%		-22.0%	-25.0%	-25.0%
<i>Adj ROACE</i>	8.7%	3.3%	0.8%	3.2%	6.9%	9.7%
<i>EBITDA drop through rate as % NFI</i>				46.0%	58.3%	53.5%
Statutory net cash/(debt) post IFRS 16	19,605	14,129	12,342	16,139	20,004	23,961
Net recourse cash/(debt) pre IFRS 16	27,341	19,890	15,967	19,200	23,065	27,022
Non recourse invoice factoring (off Balance Sheet)	-13,800	-14,200	-9,600	-7,000	-7,000	-7,000
IFRS leases	-7,736	-5,761	-3,625	-3,061	-3,061	-3,061
<i>Diluted sharecount</i>	32,353	32,358	32,500	32,665	32,828	32,991
<i>Shareprice (p)</i>	78p					

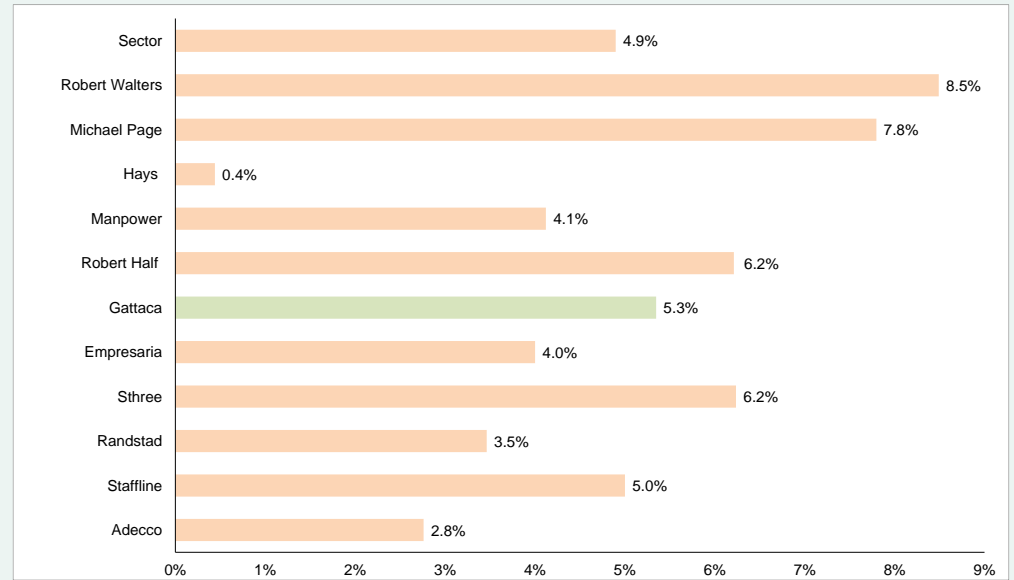
Source: Equity Development

Key risks

- General economic downturn affecting engineering and technology recruitment.
- Greater competition, especially from new technology platforms (eg LinkedIn, Monster).
- Remote risk of US Department of Justice action relating to certain Networkers International activities prior to its 2015 acquisition.

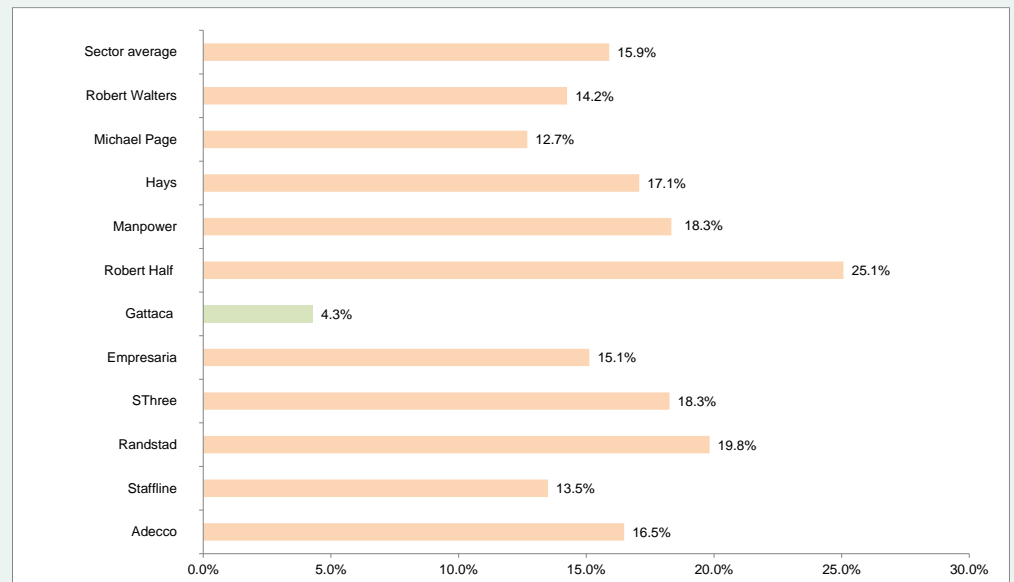
Appendices - sector valuation metrics and KPIs

Current year NFI growth (%) vs peers



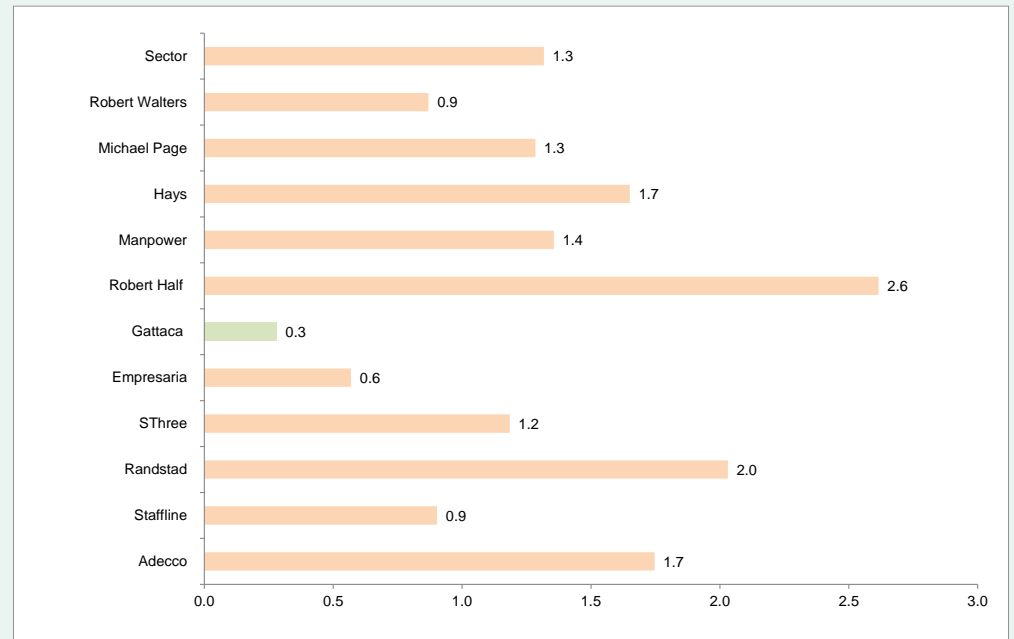
Source: Equity Development

Current Year (CY) EBIT / NFI conversion rates



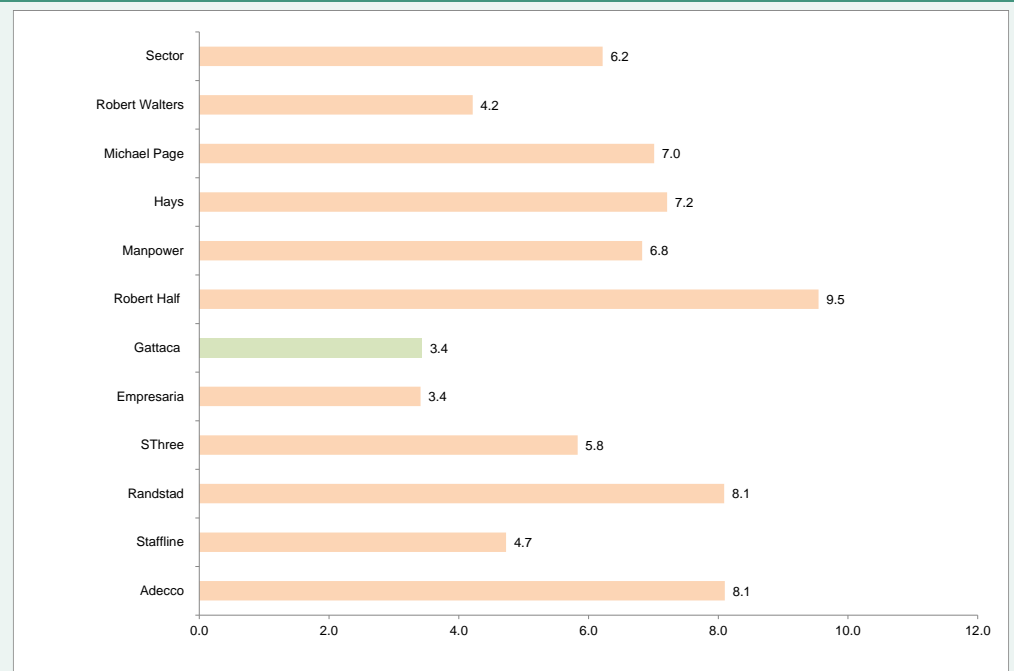
Source: Equity Development

Current Year (CY) EV/NFI multiples vs peers



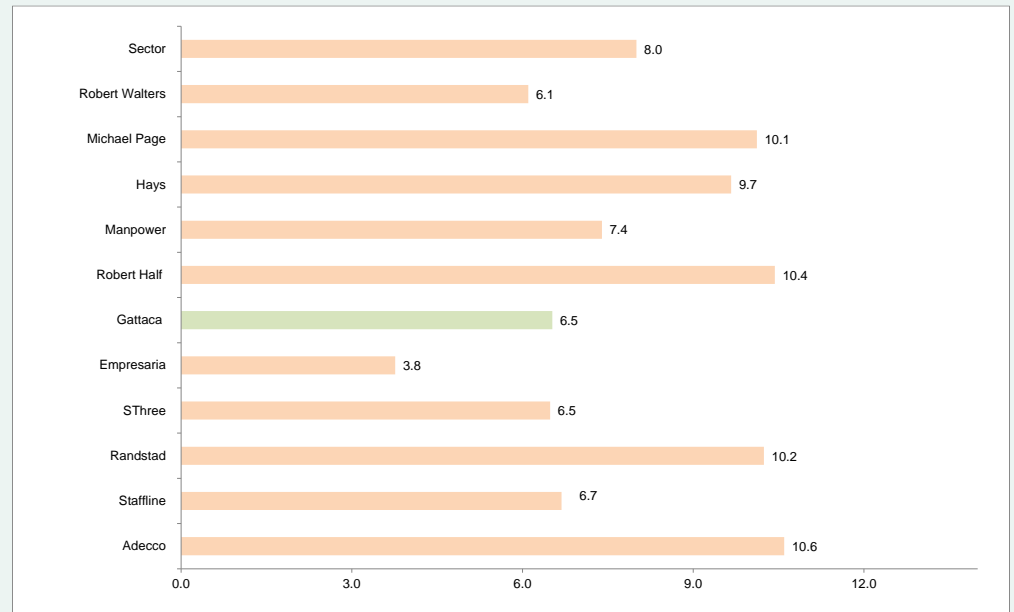
Source: Equity Development

CY EV/EBITDA multiples vs peers



Source: Equity Development

CY EV/EBIT multiples vs peers

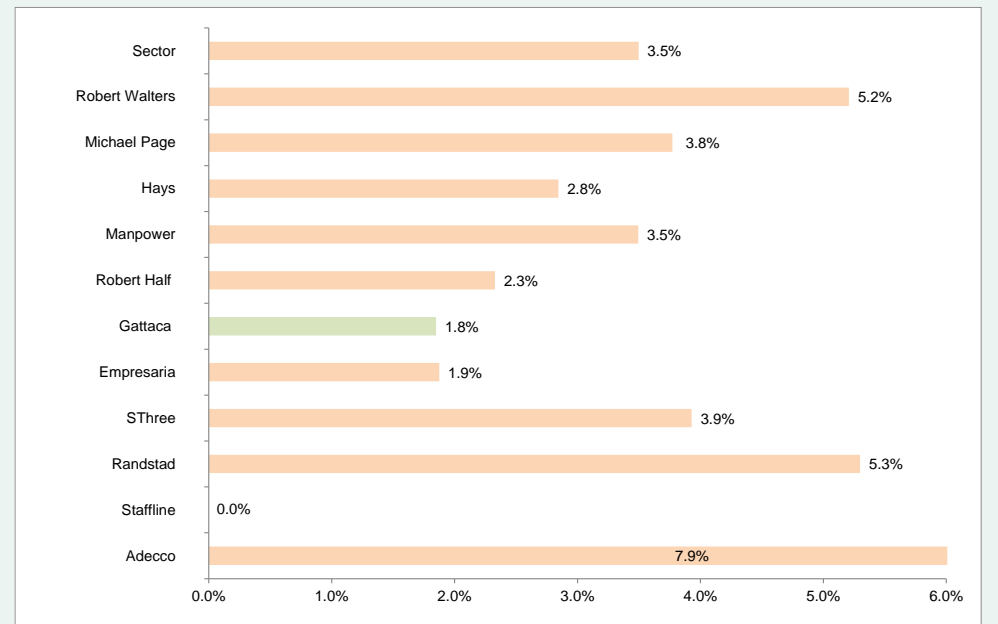


Source: Equity Development

CY PERs multiples vs peers



Source: Equity Development

CY dividend yield (%)


Source: Equity Development

Market capitalisation of peers

	Shareprice	Mrk Cap (Millions)	CY net cash / (debt) Millions	Enterprise Value (Millions)
Adecco	€ 31.8	€ 5,498	-€ 2,918	€ 8,416
Staffline	35p	£58.8	-£7.4	£66.2
Randstad	€ 57.0	€ 10,448	-€ 870	€ 11,318
SThree	420p	£562	£30	£532
Empresaria	64p	£32.0	-£7.9	£39.9
Gattaca	78p	£25.2	£12.2	£13.0
Robert Half	\$76.0	\$8,109	\$806	\$7,303
Manpower	\$79.0	\$4,013	-\$62	\$4,075
Hays	109p	£1,940	£55	£1,885
Michael Page	448p	£1,438	£22	£1,416
Robert Walters	480p	£360	£30	£330

Source: Equity Development



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