

Grafenia plc

Issue of Equity & notice of GM

RNS Number : 4900G
Grafenia plc
24 July 2019

24 July 2019

The information contained within this announcement is deemed by the Company to constitute inside information as stipulated under the Market Abuse Regulations (EU) No. 596/2014 ("MAR"). With the publication of this announcement via a Regulatory Information Service, this inside information is now considered to be in the public domain.

Grafenia plc

("Grafenia", the "Group" or "Company")

Issue of equity to raise approximately £4.01 million and notice of general meeting

Grafenia (AIM:GRA) is pleased to announce that it has conditionally raised approximately £4.01 million before expenses through a placing and subscription of 28,653,569 new ordinary shares of 1 pence each ("Placing Shares") at an issue price of 14 pence per share (the "Placing"). The Placing is conditional, *inter alia*, on the approval of Shareholders at a forthcoming general meeting ("General Meeting") of resolutions to provide authority to the directors of the Company ("Directors" or "Board") to issue and allot further new Ordinary Shares on a non-pre-emptive basis, further details of which are set out below.

Transaction highlights:

- Placing to raise approximately £4.01 million before expenses.
- Strong support from existing and new investors.
- The net proceeds of the Placing are intended to be used to fund further acquisitions as well as to invest in acquiring Nettl partners and franchisees, domestically and internationally.
- Whilst the Group is negotiating these acquisitions, they will utilise up to £1.5 million of the Net Proceeds to repay existing debt arrangements to save unnecessary interest payments.
- The Group plans to finance acquisitions with a prudent mix of equity and debt.
- The Placing Shares will represent approximately 25 per cent. of the issued share capital of the Company as enlarged by the issue of the Placing Shares.

Jan Mohr, Chairman of Grafenia plc: "The team at Grafenia continues to execute our transformation plan. After testing the waters in 2017, we gained more confidence during the last year in growing our Nettl partner base organically and by acquiring sign businesses. In 2019 and beyond, we will continue to scale in the UK and overseas."

Peter Gunning, CEO of Grafenia plc: "This capital raise enables us to continue executing the next part of our transformation plan. We're grateful for the continued support of existing shareholders and welcome our new investors in this round."

Notice of general meeting

The Company will shortly be posting to shareholders a circular and notice of General Meeting (the "Circular") to convene the General Meeting which will be held at the offices of Gateley plc, Ship Canal House, 98 King Street, Manchester M2 4WU at 10.00am on 12 August 2019. The Circular will also shortly be available for download from the Company's website <https://www.grafenia.com/>

Related party transactions

Langfrist and Value Focus are related parties of the Company for the purposes of the AIM Rules as they each hold more than 10 per cent. of the Existing Ordinary Shares, being 29.35 per cent. and 22.20 per cent. respectively. Langfrist will participate in the Placing in respect of 8,581,428 new Ordinary Shares and Value Focus will participate in the Placing in respect of 11,428,571 new Ordinary Shares, each such participation represents a related party transaction pursuant to Rule 13 of the AIM Rules.

The Directors, having consulted with the Company's Nominated Adviser, Allenby Capital, consider that the terms of the Related Party Transactions with Langfrist and Value Focus are fair and reasonable insofar as the Shareholders are concerned.

Total Voting Rights

Upon Admission, the Company's issued share capital will consist of 113,338,252 Ordinary Shares with one voting right each. The Company does not hold any ordinary shares in treasury. Therefore, the total number of ordinary shares and voting rights in the Company will be 113,338,252. With effect from Admission, this figure may be used by Shareholders as the denominator for the calculations by which they will determine if they are required to notify their interest in, or a change to their interest in, the share capital of the Company under the FCA's Disclosure Guidance and Transparency Rules.

Market Abuse Regulation (MAR)

MAR came into effect from 3 July 2016. Market soundings, as defined in MAR, were taken in respect of the Placing with the result that certain persons became aware of inside information, as permitted by MAR. That inside information is set out in this announcement has been disclosed as soon as possible in accordance with paragraph 7 of article 17 of MAR. Therefore, those persons that received inside information in a market sounding are no longer in possession of inside information relating to the Company and its securities.

Defined terms used in this announcement shall have the meaning ascribed to them in the Circular.

For further information:

Grafenia plc

Peter Gunning (CEO)

07973 191 632

Allenby Capital Limited (Nominated Adviser and broker)

David Hart / Liz Kirchner / Nicholas Chambers

0203 328 5656

About Grafenia

Grafenia creates software and systems which power the graphic arts industry. The Group licences its brands, software and technology to partners in the UK and internationally. It also sells and manufactures products, ranging from printed business marketing to large scale signage.

The Group has multiple routes to market, including the printing.com network. Its retail-based Nettl formula is expanding. In cities, the Group operates company-owned Nettl stores. In towns and neighbourhoods, it partners with existing businesses who 'bolt-on' the Nettl formula. Nettl mostly sells a range of 'cross-media' products and services to SMEs such as websites, apps, e-commerce, print, display, signage and exhibition marketing.

The Group is acquisitive, with its largest acquisition being Image Group in July 2017. Image Group provides clients with merchandising, retail graphics, site branding, signage, promotional advertising and exhibition solutions. The Group's strategy is to roll-up the signs industry, to create a national network of Nettl Business Superstores.

Further information can be found at <https://www.grafenial.com/>

Information to Distributors

Solely for the purposes of the product governance requirements contained within: (a) EU Directive 2014/65/EU on markets in financial instruments, as amended ("MiFID II"); (b) Articles 9 and 10 of Commission Delegated Directive (EU) 2017/593 supplementing MiFID II; and (c) local implementing measures (together, the "Product Governance Requirements"), and disclaiming all and any liability, whether arising in tort, contract or otherwise, which any "manufacturer" (for the purposes of the Product Governance Requirements) may otherwise have with respect thereto, the Placing Shares have been subject to a product approval process, which has determined that the Placing Shares are: (i) compatible with an end target market of retail investors and investors who meet the criteria of professional clients and eligible counterparties, each as defined in MiFID II; and (ii) eligible for distribution through all distribution channels as are permitted by MiFID II (the "Target Market Assessment"). Notwithstanding the Target Market Assessment, investors should note that: the price of the Placing Shares may decline and investors could lose all or part of their investment; Placing Shares offer no guaranteed income and no capital protection; and an investment in the Placing Shares is compatible only with investors who do not need a guaranteed income or capital protection, who (either alone or in conjunction with an appropriate financial or other adviser) are capable of evaluating the merits and risks of such an investment and who have sufficient resources to be able to bear any losses that may result therefrom. The Target Market Assessment is without prejudice to the requirements of any contractual, legal or regulatory selling restrictions in relation to the Placing and Subscription. Furthermore, it is noted that, notwithstanding the Target Market Assessment, only investors who have met the criteria of professional clients and eligible counterparties have been procured. For the avoidance of doubt, the Target Market Assessment does not constitute: (a) an assessment of suitability or appropriateness for the purposes of MiFID II; or (b) a recommendation to any investor or group of investors to invest in, or purchase, or take any other action whatsoever with respect to the Placing Shares.

Extracts from the Circular

The following has been extracted from, and should be read in conjunction with, the Circular, which will shortly be made available for download from the Company's website:

The Company has conditionally raised approximately £4.01 million before expenses by means of a Placing with certain new and existing institutional and other investors of 28,653,569 Placing Shares at 14 pence per share.

The Placing is conditional, *inter alia*, on the passing of the Resolutions at the General Meeting and Admission becoming effective by no later than 8.00 a.m. on 14 August 2019 (or such other time and/or date, being no later than 8.00 a.m. on 30 August 2019, as the Company and Allenby Capital agree). It is expected that the Placing Shares will be admitted to trading on AIM on or around 8.00 a.m. on 14 August 2019.

The Net Proceeds are intended to be used to fund acquisitions, investing in acquiring Nettl partners and franchisees, domestically and internationally, to repay and renegotiate certain of the Company's existing debt arrangements and for general working capital purposes as further described below.

The Board believes that raising equity finance, by way of a placing, is the most appropriate method of financing for the Group at this time. It allows the Company to raise funds relatively quickly and at a lower cost than might be possible by undertaking another form of fundraising, such as an open offer or rights issue. It also avoids the need for a prospectus to be prepared and issued, which is a costly and time-consuming process.

Background to and reasons for the Placing

The Directors believe that Grafenia is still too small to be a public company. Quite simply, the ongoing costs of being listed impact significantly upon the Group's earnings. In addition, as our traditional market has become more commoditised and margins have eroded over time, we have sought to reposition the business.

In 2016, the Directors began a strategic review to assess ways to improve shareholder value. The Board considered delisting the Company from AIM. However, this was rejected as it would result in a loss of liquidity in the Company's Ordinary Shares and would not enhance trading performance.

The market opportunity

In 2017, we announced our plans to acquire sign businesses. We like this sector for a number of reasons. It's complementary to our core business. It's highly fragmented and there are multiple acquisition targets. We've evaluated many sign businesses and have acquired three of them so far.

Our aim is to create a national sign solution capability serving SMEs by acquiring sign businesses and converting them to Nettl Business Superstores.

However, opening new Nettl Business Superstores is capital intensive. As we are currently loss-making, it would take some time to make a sufficient contribution to profitability, with just the incremental acquisition and conversion of smaller businesses alone.

That's why we're looking at acquisition opportunities in two size brackets. We'll continue to look for suitable Superstore targets - those typically have up to 10 employees and revenues of up to £500,000.

We're also looking at a second group of larger businesses. They tend to have up to 100 employees and revenues of £3 million to £5 million. These would act as regional hubs for

our network.

With the Placing, we are prioritising acquisitions of businesses in the second group. Once these are in place, we should be able to acquire smaller businesses and convert them to Nettl Business Superstores from cash-flow.

We'll discuss each in turn.

Nettl Business Superstores

The Nettl Business Superstore format combines sales, design, marketing, manufacturing and installation in one place. Stores are slightly out-of-town in 'trade counter' units, from 5,000 to 7,500 square feet.

At the front of the store there are displays to explain different ways SMEs can promote themselves. Some people have said the space looks more boutique hotel than print shop, and that's not an accident. We want our stores to be inspirational places where clients can get ideas on ways they can promote their businesses and decorate their premises.

There's a permanent design and account management team on site. Different specialists talk to clients about web, e-commerce, print and signage. We'll measure-up for signs, build e-commerce sites and design brochures all in-house.

To draw businesses in, we sell coffee and rent out meeting space.

Finally, we make signs and fit vehicle graphics. There's also a sign installation team based at the store.

Two Superstores are currently trading. The first, Nettl of Liverpool Waters, opened in March 2018 and was formed from the acquisition of ADD Signs. In March 2019, the second opened in Exeter, which was born from the combined acquisitions of Nettl of Exeter and AG Signs. The Exeter Superstore has recorded annualised peak monthly run rates of over £1 million. Our focus is on driving sales performance to consistently achieve these levels.

We also operate three other Nettl locations - a city-centre 2,000 square foot Business Store in Birmingham, a 7,000 square foot Business 'pop-up' Store in central Manchester and a small web studio in Dublin. Sales of all our product lines in company-owned stores increased to approximately £2.56 million in the year ended 31 March 2019, compared to £1.59 million the previous year.

We've learnt from operating these stores ourselves. Our systems were originally designed to deliver print and web projects, so we've had to extend our back-office to handle and invoice sign projects. There's still work to do so we can manage all aspects of sign manufacture in our process; from survey to quoting and installation.

There are 50 locations in the UK which we've identified as potential targets for a Nettl Business Store or Superstore and an abundance of sign businesses for sale. However, we are selective about which businesses to approach. Finding businesses with a cultural fit and a team with the desire to rebrand as a Nettl Business Superstore is our priority.

On two occasions so far, we've combined a sign business with a nearby Nettl partner team we've hired or acquired. That's likely to happen again. Many Nettl partners are interested in joining Grafenia as we roll-out future Superstores. Their history and behaviour as licensed partners are helpful indicators of whether we're a suitable match.

Signs and display graphics are a logical extension to the range of products that both our

company-owned and partner-operated stores sell. However, there's often a gap in knowledge and sales competence levels that can lead to a lack of confidence, which is an obstacle to sales.

We aim to help clients choose the right product, within their budget and without confusing them with jargon. We've developed marketing tools, like our "Wall of Wonder" and companion buying guide. It helps explain the options, with easy-to-follow price brackets. As we launch new products, it's important we develop design templates, technical documentation and marketing collateral to support them.

Nettl Works regional hubs

In July 2017, we acquired Image. They had sales of over £5 million and at the time, we believed they would act as our national sign hub. Since the acquisition, we've rolled out a range of printed vinyl and rigid substrates, which we sell through our company stores and licensed Nettl and printing.com partner network. Some items, like our giant deckchair is a hybrid product, with components made at Image and finished by our fabric printing hub. These 'products' can be shipped by overnight carrier and flow through our supply chain just like flyers and business cards. We'll continue to productise more items this way.

However, we've still yet to crack the conundrum of national manufacture and installation. Whilst we've won some national project work, we've found that the distance from manufacture to installation directly affects competitiveness and/or profitability.

We believe that regional hubs are part of the answer. We call them 'Nettl Works'.

When the first Nettl Business Superstore opened, we just relocated all the manufacturing equipment ADD was using. In Exeter AG Signs was subcontracting more manufacturing and so our Superstore has less equipment. Instead there's more meeting and display space.

We believe we need five Nettl Works in the UK to get sufficient geographic coverage. These hubs will manufacture sign projects, leaving Superstores to focus on sales, design and installation and printing of fast turnaround graphics.

Unlike a Superstore, hubs will retain their existing identity and continue to service their client base. We plan to implement our supply chain software and co-brand as 'Nettl Works'. Image will be the first Nettl Works.

Our current hub targets have been stable or shown growth over the past three years. Importantly, recent independent research commissioned by ISA-UK¹ has shown that optimism in the UK sign and graphics industry is high, with over half of those participating in the survey reporting an increase in business turnover in the past year. A recent report by Smithers Pira² considers that growth in the global digital textile printing market is set to continue, with the worldwide market rising to €2.83 billion in 2018, more than double its present value.

1 ISA-UK Sign Industry Survey, June 2019

2 The Future of Digital Textile Printing to 2023, published December 2018 by Smithers Pira
<https://www.smitherspira.com/industry-market-reports/printing/digital-textile-printing-to-2023>

Our investment criteria

The first stage is to acquire a profitable business, where the owner wants to stay for at least a couple of years - we call them the "remainder".

We'll consider businesses which meet our criteria:

- stable or growing, with a track record of profitability in previous four or five years;
- minimum annual turnover of £250,000;
- their top three clients represent no more than 30 per cent. of their business;
- gross profit margins above 55 per cent.;
- owner's salary expectation consistent with our Company's pay structure;
- located in a primary city target location (phase 1) or secondary location (phase 2);
- for Superstore targets, property tenure flexible (able to relocate within 24 months);
- good cultural fit (management's business ethos and circumstances i.e. must support rebranding and personal circumstances must underpin / encourage long term commitment).

We evaluate each "remainder" acquisition on its own merits as if it were to remain a standalone business.

Once we've acquired and integrated a "remainder" business, we look for another local business to roll-in. Those could also be nearby Nettle partners. For these other businesses, we target owners seeking to exit - the "leaver". Our plan is to consolidate both businesses into a single team, led by the "remainder". We aim to achieve cost savings by centralising marketing, management information systems, legal support, payroll and accounting.

Our aim is to acquire sign businesses at 2-5 times adjusted forecast EBIT.

Our progress so far

In January 2017, we acquired ADD Signs in Liverpool. We believe site selection is important. We found a suitable property and decided to relocate and build our first Nettle Superstore in March 2018. In September 2018, we hired some team members from a nearby partner. Sales have grown under our ownership although profitability has been impacted by dual occupation costs until the lease for ADD's previous premises expired in February 2019 and a doubtful debt of over £40,000 from an insolvent client. We've made changes to the team and estimate this store will break-even this year.

In July 2017, we acquired Image. Image has performed mostly as expected, although gross margin has been at the weaker end of their historic performance and overheads have increased. We used the Image team to shopfit both our Superstores. While we did these both in quiet periods and saved a significant amount compared to external sourcing, it did carry an opportunity cost for servicing new client work. We've taken action to reset the cost base and are currently combining one of Image's factories with our main Manchester production hub. This is due to be completed by the end of July 2019 and we anticipate material overhead savings, as well as an improvement in efficiency.

In December 2017, we acquired Nettle of Exeter, one of our top performing partners. One of the owners, Ashley Scott, joined the Group and moved to a central role in our partner performance team. In July 2018, we acquired AG Signs in nearby Honiton. We relocated both businesses in March 2019 to a new Superstore outside Exeter city centre. The combined business is performing well.

In March 2019, we acquired Artichoke Design. One of the owners exited and the other rolled into our Nettle of Birmingham Business Store. That business has continued to perform and we are incubating and growing a team which may be spun off into a future Superstore.

Licensing Nettle

The Nettl business model is licensed to third parties. Designers, printers and sign businesses can access our training, systems and marketing to sell websites, printing and displays to their own clients. We grant them an exclusive territory, in exchange for a licence fee of up to £2,999. We call them "Partners" and they pay a monthly subscription of typically £399. They typically contract for a minimum of three to five years.

Our Nettl partner network has grown to over 228 locations around the world. At the date of our last trading update, we had 173 active Nettl partners in the UK and Ireland, 27 in Benelux, 13 in France, eight in the USA, four in New Zealand and three in Australia. Our total subscription and licence fee income grew to approximately £1.98 million for the year ended 31 March 2019.

We launched Nettl of America on 7 March 2019. To comply with federal and state laws, we positioned Nettl as a co-brand franchise model. The compliance and registration process is now complete and we are able to grant franchises in 37 of the 50 US states. We anticipated there would be a longer gestation period to acquire franchise partners, partly down to local laws requiring cooling off periods and the disclosure processes. This has turned out to be the case. However, we are delighted to have granted eight franchises so far, in the states of Florida, Ohio and Georgia. We expect to grant more in the coming months.

Clearly, the United States is a major market. When we research launching Nettl into a new country, we estimate the number of potential locations, relative to the density of the SME population. Using that rule of thumb, we believe the US could support between 1,500 and 2,000 Nettl locations. When we launch, much of the cost is front-loaded. Although we evaluate the project as if it were an investment, we expense the costs as we incur them. This adversely affects our earnings and inflates our short-term overheads, but we are confident that the future upside is worth the management time, opportunity cost and effort.

Use of proceeds

We plan to use the net proceeds of this Placing to acquire businesses which are suitable to become Nettl Works regional hubs and for working capital requirements, while we invest in growing our Nettl partner network domestically and internationally. The actual number of acquisitions will be determined by their profitability and scale.

In the short term, however, while the Company is seeking to identify and negotiate the acquisition of these businesses, the Company will utilise up to £1.5 million of the Net Proceeds to repay certain of its existing debt arrangements to save unnecessary interest payments.

In due course, the Company plans to finance acquisitions with a prudent mix of cash-flow, equity and debt.

Current trading

Our most recent trading statement was announced on 3 July 2019 in relation to the year ended 31 March 2019. Revenue is expected to be approximately £15.75 million (*2018: £14.63 million*), with the increase partly due to a full 12 months of trading from Image, acquired part way through the comparative period on 14 July 2017. Like many businesses and most in the print sector, we have faced rising input costs, particularly with paper. This has impacted our product gross margin, although our transition to become less reliant on trade litho print sales has meant that our overall gross margin has increased in absolute terms. Our overheads have increased as we include the costs of three businesses we've acquired during the year, as well as a full year of Image, compared to a portion in the prior

year. We have also expensed costs of acquiring Nettl partners and opening stores. This will result in the Group generating negative earnings before interest, tax, depreciation and amortisation ("EBITDA") for the year ended 31 March 2019. However, it's important to note that this does not reflect our cost-base moving forward as we've taken significant steps to reduce our overheads.

As a result of these changes to our cost base, we estimate we will be breakeven on a monthly EBITDA run rate during the current financial year. We are targeting an EBITDA margin of 10-15% in the medium term, although we make decisions for the long-term sustainability of the business, rather than short-term performance. At 31 March 2019, we had cash and cash equivalents of £1.37 million (2018: £0.17 million).

Since the year-end, trading in the first quarter has been in-line with the Company's internal budgets.

Details of the Placing

The Company is proposing to raise, in aggregate, approximately £4.01 million (approximately £3.95 million net of expenses) by way of (i) a Placing of 26,153,569 new Ordinary Shares with certain new and existing investors, and (ii) a subscription for 2,500,000 new Ordinary Shares, both being conditional, *inter alia*, on Admission.

Allenby Capital has entered into the Placing Agreement with the Company under which Allenby Capital has, on the terms and subject to the conditions set out therein (including Admission), undertaken to act as settlement agent for the Placing. The Placing Agreement contains certain warranties and indemnities from the Company in favour of Allenby Capital. The Placing is not being underwritten by Allenby Capital or any other person.

The Placing is conditional, *inter alia*, on:

- the passing of the Resolutions at the General Meeting;
- Admission becoming effective by no later than 8.00 a.m. on 14 August 2019 (or such later time and/or date, being no later than 8.00 a.m. on 30 August 2019, as the Company and Allenby Capital may agree); and
- the Placing Agreement not being terminated prior to Admission.

Accordingly, if any of such conditions are not satisfied, or, if applicable, waived, the Placing will not proceed.

Application will be made to the London Stock Exchange for the Placing Shares to be admitted to trading on AIM. The Placing Shares will rank *pari passu* in all respects with the Existing Ordinary Shares, including the right to receive all dividends and other distributions declared, made or paid in respect of the Ordinary Shares following Admission. It is expected that such Admission will become effective and that dealings on AIM will commence at 8.00 a.m. on 14 August 2019.

Recommendation and voting intentions

The Directors unanimously believe that the Placing is in the best interests of the Company and its Shareholders as a whole and recommend Shareholders to vote in favour of the Resolutions, as they intend to do in respect of their own beneficial holdings of 2,791,301 Ordinary Shares, representing approximately 3.30 per cent. of the Existing Ordinary Shares.

This information is provided by RNS, the news service of the London Stock Exchange. RNS is approved by the Financial Conduct Authority to act as a Primary Information Provider in the United Kingdom. Terms and conditions relating to the use and distribution of this information may apply. For further information, please contact rns@lseg.com or visit www.rns.com.

END

IOECKNDKKBKBCOB