

TERN PLC

SOFTWARE AND COMPUTER SERVICES

23 September 2022

TERN.L

10.3p

Market Cap: £36.1m

SHARE PRICE (p)



12m high/low 23.3p/9.9p

Source: LSE Data (priced as at prior close)

KEY DATA

Net (Debt)/Cash	£0.3m (at 30/06/22)
Enterprise value	£35.8m
Index/market	AIM
Next news	Trading Update Jan 23
Shares in Issue (m)	352.1
Chairman	Ian Ritchie
Chief Executive	Albert E Sisto
Finance Director	Sarah Payne

COMPANY DESCRIPTION

Tern predominantly invests in software companies, with proven technology, based in the UK but with global ambition.

www.ternplc.com

TERN PLC IS A RESEARCH CLIENT OF PROGRESSIVE

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Repeat licencing revenue a highlight of H1 22

Tern has delivered a solid set of first-half results and further positive developments post-period. The portfolio is at an inflexion point, with configuration work turning to repeat licencing revenue and aggregated monthly recurring revenues (MMR) increasing 112% in H1. Recent third-party investments and uplifts in value recognised in 2021 and early 2022, coupled with the 35% net asset growth accomplished in 2021, are critical proof points that Tern's model is delivering. The first Series B round was also successfully completed in the period for FundamentalVR. While the termination of the potentially transformative Pires deal was disappointing, we see significant value creation from Tern's hybrid VC model and organic growth potential. We believe that recurring revenue growth will attract additional strategic interest and look forward to further positive newsflow.

- **Significant increase in MMR.** Aggregated MRR increased by 112% in H1, reflecting the shift from configuration work to a licencing model. This transition has, however, had a short-term impact as development revenue tends to be more upfront with MRR recognised over a longer period, leading to a 12% drop in H1 reported revenue versus H1 21.
- **Improvement in key growth metrics.** The increase in number of employees across the portfolio was 52% in H1 22 (H1 21: 14%), supported by an increase in MRR per employee of 40%.
- **Overall uplift in NAV impacted by Wyld share price weakness.** The fair value of FundamentalVR increased by £1.2m following its successful Series B fundraise, and the fair value of Device Authority increased by £1.6m due to US Dollar weakness. However, the global sell-off in technology stocks saw these gains offset by a £4m reduction in the fair value of Wyld.
- **First Series B round completed by FundamentalVR.** This represents proof of concept that the change in investment strategy adopted in 2017 is progressing as planned. Unlike in the traditional VC model, Tern provides more than just funding: it proactively supports the growth of its portfolio.

Tern's portfolio companies have made substantial progress in pivoting their business models away from one-off licence fees to monthly recurring revenues. Although regular equity raises have the perception of being dilutive, the track record for Tern suggests that they have been accretive over time, with third parties supporting the placements and Tern also able to participate, and incremental value being created, allowing Tern to benefit from further upside potential.

TERN'S NETWORK OF COMPANIES



DEVICE
AUTHORITY

FUNDAMENTALVR



Wyld Networks

KONEKTIO



Talking Medicines

Source: Company Information.

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Financial highlights for H1

The aggregated MRR for Tern’s network of companies increased by 112% in H1 22, reflecting the transition from configuration work to a licencing model. This transition has, however, had a short-term impact as development revenue tends to be more upfront with MRR recognised over a longer period, leading to a 12% drop in H1 reported revenue versus H1 21. The increase in number of employees across the portfolio was 52% in H1 22 (H1 21: 14%), supported by an increase in MRR per employee of 40%.

Tern invested £0.8m to support the growth of its portfolio companies in H1 (H1 21: £0.7m), including £0.1m into the Sure Valley Ventures UK Software Technology Fund (SVV). Tern had net cash of £0.3m as at 30 June 2022, and post period agreed a short-term loan of £0.4m, due by the end of December 2022 or to be settled by a call option on 320,455 Wyld shares.

Assets under management were £30.2m, up 33% (H1 21: £22.7m) but comparable to the year-end position (FY21: £30.6m), consisting of the £0.8m investment and a £1.2m fair value loss. The Wyld share price decreased amid the global sell-off in technology stocks, which caused a fair value decrease of £4m, offsetting valuation increases in Device Authority of £1.6m and FundamentalVR of £1.2m. It should be noted that as at December 2021 Wyld reported a £4.7m gain, therefore the decrease represents a reversal, with signs that the share price is recovering.

The NAV per share of 8.5p as at 30 June 2022 was above 7.1p as at 30 June 2021, but below 9.2p at the year-end, predominantly because of the Wyld share price fall, as detailed above. Tern recorded a loss of £2.4m in H1 22, compared with a loss £0.7m in H1 21.

During the period, Talking Medicines completed a Series A fundraise for £1.59m at a 62% uplift, while Wyld Networks received approximately £2m from the exercise of 98.6% of its T01 warrants. Also, FundamentalVR completed a Series B fundraise for £7m at a 35% uplift, followed by an additional Series B £5m tranche post-period.

Tern Investment Strategy

Investment Sector

- Disruptive IoT tech
- In key new “Fourth wave” areas
- Artificial Intelligence
- VR/AR Immersive Tech /Metaverse
- Machine Learning
- Security (e.g. Cyber/Info)

Creating Value

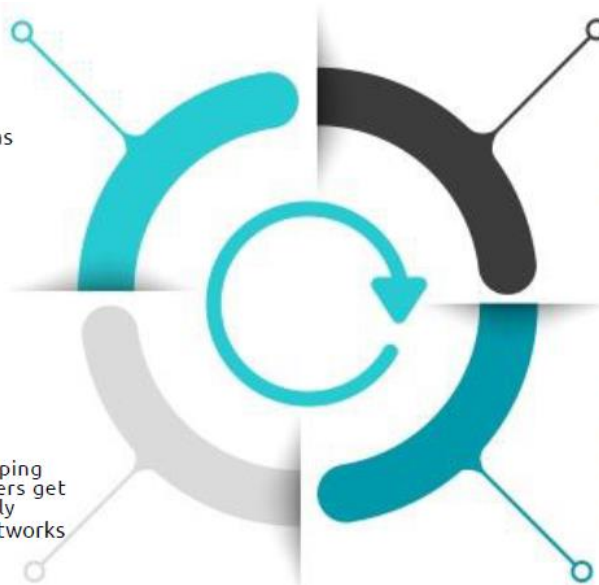
- Value Add through hands on approach
- Focused on helping and developing portfolio companies and Founders get to scaling industry metrics rapidly
- Leveraging our contacts and Networks

Investment Stage

- Initial investments at the Late Seed A round stage
- Lead deals at attractive valuations
- Bring in other leading VCs at scaling rounds at higher valuations and follow-on

Geography & Origination

- Focused on UK companies
- Experienced Leadership teams
- Tern team are based in London and Silicon Valley
- Data driven strategy used
- For origination across UK



Source: Company, Progressive Equity Research

Portfolio highlights

Device Authority (53.8%, £16.3m NAV) – automates the provision of secure platforms for IoT devices, and has seen good progress, particularly in the US following the US\$1.25m strategic investment from Venafi (owned by Thoma Bravo) in December 2021. This is part of a broader US\$2.91m funding package for Device Authority, which includes a follow-on US\$1.25m investment from Tern alongside US\$0.41m from existing Device Authority shareholders as part of a Series A round. We understand that Device Authority has material growth in its monthly recurring revenues from its subscription base and its modularised licence platform, KSaaS (KeyScaler software as a service), which is built on Microsoft’s Azure Cloud

FundamentalVR (20.0%, reducing to 16.58% post-period, £4.8m NAV) – provides a software simulation environment allowing surgeons’ accuracy to be measured objectively for the first time. Social distancing and the reduction in elective surgeries as a result of Covid have accelerated the adoption of FundamentalVR’s solutions. As a result, FundamentalVR recently attracted new investors to raise £7m in a Series B round at a much higher valuation, resulting in a 35% uplift to the year-end book value. This was followed by an additional £5m tranche of the Series B in early Q3 2022.

Talking Medicines (23.8%, £1.8m NAV) – has developed a next-generation data platform, PatientMetRx, to deliver insights on patient experience for pharmaceutical drug brands. Its cloud-based SaaS service is driven by artificial intelligence models processing real-world data collection at a scale that is transformational versus traditional research. Talking Medicines has just broken into the US market, which means, in our view, that it is too early to look for an exit as the company has excellent prospects. It raised a total of £1.59m (£0.40m from Tern) in January in a late-seed round to support its planned expansion in the US, representing an uplift of approximately 62% on the amount invested by Tern since November 2020. Boston-based life science investor Mark Bamforth invested alongside Tern.

InVMA (36.8%, £2.2m NAV) – is now trading as Konektio following its £2.1m late-seed investment round in December 2021, led by fund managers Foresight and Mercia, at a 44% uplift. Konektio’s Industrial IoT connected asset software as a service (SaaS) product, AssetMinder, is in ever-increasing demand from customers and it is continuing to build MRRs. AssetMinder assesses the effectiveness and efficiencies of entire operations, factory floors and processes, putting customers in control of their assets and therefore directly impacting productivity, efficiency and business outcomes.

Wyld Networks (49.2%, £5.0m NAV) – was floated on the NASDAQ First North Growth Market in Stockholm in 2021, with Tern retaining a majority stake. The IPO has also provided a route to exit to maximise value for Tern shareholders. Wyld completed the hardware development of Wyld Connect and Wyld Fusion in preparation for the commercial launch of its end-to-end satellite IoT solution, planned for later this year. The company also expanded its strategic industry positioning by entering into connectivity partnerships with Eutelsat Communications, Senet Inc and TrakAssure to form the Multimodal IoT Infrastructure Consortium (MMIIC). Wyld Networks raised approximately SEK 25.2m (c.£2.0m) upon exercise of 98.6% of its outstanding T01 Warrants.

Growth drivers and value creation

Tern provides a unique proposition, creating value via access to disruptive start-ups not generally available to AIM investors. It operates a hybrid Venture Capital (VC) model, with all shareholders acting as effective Limited Partners. This business model change was actioned in February 2017 following the acquisition of Device Authority Inc.

Although the termination of the Pires acquisition can be seen as a setback for Tern, we believe that the market reaction reflects a lack of understanding about the model created by management and the group's long-term ability to create value from its portfolio.

Unlike in the traditional VC model, Tern provides more than just funding: it proactively supports the growth of its portfolio companies. In our view, Tern could be considered an 'evergreen' VC fund: open-ended, with no termination date, meaning capital can be raised, repaid or transferred on an ongoing basis. This model provides a very efficient use of capital, and Tern has an excellent track record of building value that attracts new investors at higher multiples. Evergreen funds have more flexibility and the ability to raise more capital, meaning that they can truly focus on long-term capital appreciation for investors.

Tern's companies are benefitting from the acceleration of business digital transformation. FundamentalVR is at the forefront, having recently closed a Series B funding round that included significant additional third-party capital with minimal participation from Tern. Wyld has demonstrated a proven realisation of value, now being listed on the NASDAQ First North Growth Market in Stockholm as of July 2021, raising over £2m in the IPO. Tern continues to have an influential holding, enabling the company to benefit in the growth of the business.

Tern is generating value creation in a timely manner. The model is both working and accelerating. Tern's management team has pivoted the company such that the business is squarely at the centre of the IoT opportunity, with a very focused investment management strategy. Although regular equity raises have the perception of being dilutive, the track record for Tern suggests that they have been accretive over time, with third parties supporting the placements and Tern also able to participate, and incremental value being created, allowing Tern to benefit from further upside potential.

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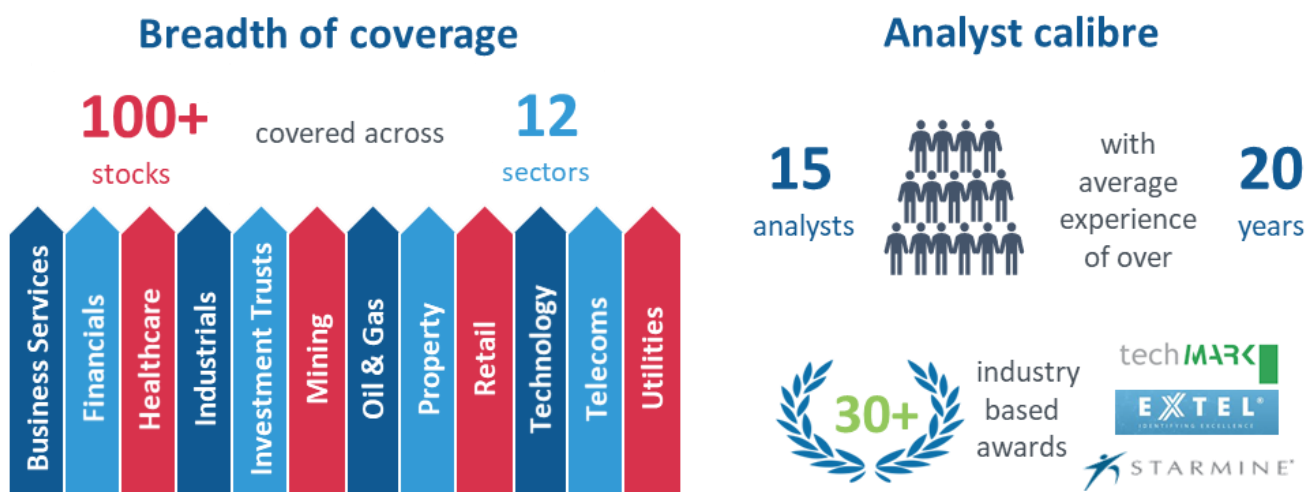
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