

TERN

SOFTWARE AND COMPUTER SERVICES

21 November 2023

TERN.L

4.0p

Market Cap: £15.5m

SHARE PRICE (p)



12m high/low

12.3p/3.5p

Source: LSE Data (priced as at prior close)

KEY DATA

Net (debt)/cash	£0.7m (at 30/06/23)
Enterprise value	£14.8m
Index/market	AIM
Next news	Prelims, February
Shares in issue (m)	388.6
Chairman	Ian Ritchie
CEO	Albert E Sisto
CFO	Colin Nunn

COMPANY DESCRIPTION

Tern operates a hybrid venture capital model, providing access to disruptive IoT start-ups with proven technology.

www.ternplc.com

TERN IS A RESEARCH CLIENT OF PROGRESSIVE

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Portfolio update highlights transition period

Tern has announced an update on its portfolio activity. Individual companies are gaining commercial traction, with configuration work turning to repeat licencing as businesses move to SaaS models. As flagged, valuations across the global technology landscape have been challenged due to risk appetite and long-term value expectations. However, third-party investments remain critical proof-points that Tern's model is delivering. Tern is positioned at the confluence of IoT, data and thereby Artificial Intelligence (AI), where we see multiple opportunities in the existing portfolio; we discuss this in more detail overleaf. We note Tern's decision not to invest further in Konektio, which we see as strategically correct and perhaps a signal that the new structure is working well. We continue to look for significant value creation from Tern's hybrid VC model, with management seeking well-timed exits that maximise value 'when the market conditions are right'.

- Positive business momentum for Device Authority.** DA is making rapid progress in growing its revenue base through its modularised licence platform KeyScaler, and in 2023 launched KeyScaler software as a service (KSaaS), which has gained a growing customer base. DA has recently launched a preview of KeyScaler AI.
- Shipping of Wyld Connect Terminals started in October 2023.** Wyld has signed over 60 alliances and built a SEK 92m purchase order backlog for its IoT module and data service.
- FundamentalVR has continued to build ARR during 2023.** The company continues to build annual recurring revenues (ARR) with a healthy pipeline of customers and new client opportunities looking to deploy Fundamental Surgery, the surgical training platform that utilises its patented HapticVR technology.
- Talking Medicines is becoming a jewel in the crown,** gaining traction using its curated AI model to source patient feedback. The business is expanding the subscription base for PatientMetRx, its SaaS on-demand product, with strong interest from the Big Pharmaceutical players.
- New structure bearing fruit.** Tern has restructured its management and operations to behave more like an asset manager, with a Board and Investment Committee alongside an executive team that manages the existing assets and markets the portfolio in terms of further raises and eventual full or partial disposal. We discuss this overleaf in further detail.

FYE DEC (£M)	2018	2019	2020	2021	2022
Revenue	0.1	0.1	0.2	0.1	0.1
Adj EBITDA	0.0	0.0	0.0	0.0	0.0
Fully Adj PBT	-0.3	-0.8	0.8	4.6	-10.4
Fully Adj EPS (p)	-0.1	-0.3	0.3	1.3	-2.9
Net asset value	16.8	18.9	24.0	32.4	24.9
NAV/share (p)	7.7	7.5	8.3	9.2	6.4
PER (x)	N/A	N/A	14.5x	3.0x	N/A

Source: Company Information and Progressive Equity Research estimates.

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Please refer to important disclosures at the end of the document.

New structure in place

As mentioned, Tern recently implemented a new structure for its management and Board. The result is an organisation shaped more like a 'traditional' asset manager, with an overseeing Board of Directors (comprising a mixture of non-executive and independent directors) and a management team tasked with the active day-to-day execution of the Board's strategy and marketing the portfolio of existing assets. This marketing will target additional fundraising rounds, and eventually a full or partial disposal (as has been the case with Wyld Networks).

The group has been able to reduce costs through this process. No payments have been made for loss of office, and the management team will be focused on delivering 'material value from its current portfolio companies' before considering any new investments.

No further investment in Konektio

In one of the first major decisions executed under the new structure, Tern has elected not to make further investments in Konektio. We understand that Konektio still relies on a relatively significant hardware element to its revenue base, and Tern had been aiming to deliver a more SaaS-heavy model. Tern will continue to monitor its investment, and hopefully will be able to achieve some form of disposal in due course.

The opportunity around IoT, data and AI

No research note regarding a tech business (or portfolio of businesses) would be complete without mentioning Artificial Intelligence (AI) and the risks or rewards it might offer. The Tern portfolio has been built up around Internet of Things (IoT) – generally connected devices or inter-related operations and assets. Each of Tern's portfolio companies generates vast amounts of data:

- Device Authority – monitoring functional data from a large number of installed industrial machinery and devices.
- Wyld Networks – huge amounts of data around the operation and performance of its advanced networks and mesh technologies.
- FundamentalVR – telemetry from virtual (practice/training) medical procedures, performed by clinicians using realistic simulations to learn and test functionality.
- Talking Medicines – information from the internet (social media) about the ways in which real-life consumers are interacting with and discussing medications.

AI uses data as its raw material. The most effective AI models are likely to be 'bespoke' or 'curated' models, trained specifically on relevant, owned and cleansed data. This will reduce errors, ensure the most useful and rapid result, and allow organisations to avoid reliance on the public internet or (worse) competitors. Data therefore will become an even more valuable resource over time, in our view. IoT devices, assets and platforms create, store and analyse data already – and AI will provide an opportunity to achieve even more. We await further AI developments from the portfolio with interest.

Financial Summary: Tern

Year end: December (£m unless shown)

	2018	2019	2020	2021	2022
PROFIT & LOSS					
Revenue	0.1	0.1	0.2	0.1	0.1
Adj EBITDA	0.0	0.0	0.0	0.0	0.0
Adj EBIT	0.0	0.0	0.6	4.4	(10.5)
Reported PBT	(0.3)	(0.8)	0.8	4.6	(10.4)
Fully Adj PBT	(0.3)	(0.8)	0.8	4.6	(10.4)
NOPAT	(0.3)	(0.8)	0.8	4.6	(10.4)
Reported EPS (p)	(0.1)	(0.3)	0.3	1.3	(2.9)
Fully Adj EPS (p)	(0.1)	(0.3)	0.3	1.3	(2.9)
Dividend per share (p)	0.0	0.0	0.0	0.0	0.0
CASH FLOW & BALANCE SHEET					
Operating cash flow	(0.8)	(1.3)	(1.2)	(1.5)	(2.1)
Free Cash flow	(4.3)	(3.8)	(3.1)	(4.0)	(3.8)
FCF per share (p)	(2.0)	(1.5)	(1.0)	(1.2)	(1.1)
Acquisitions	0.0	0.0	0.0	0.0	0.0
Disposals	0.0	0.0	0.0	0.0	0.0
Shares issued	5.9	2.9	4.2	3.8	2.8
Net cash flow	1.6	(0.9)	1.1	(0.2)	(1.0)
Overdrafts / borrowings	0.0	0.0	0.0	0.0	0.0
Cash & equivalents	1.9	1.0	2.1	2.0	0.9
Net (Debt)/Cash	1.9	1.0	2.1	2.0	0.9
NAV AND RETURNS					
Net asset value	16.8	18.9	24.0	32.4	24.9
NAV/share (p)	7.7	7.5	8.3	9.2	6.4
Net Tangible Asset Value	0.0	0.0	0.0	0.0	0.0
NTAV/share (p)	0.0	0.0	0.0	0.0	0.0
Average equity	13.7	17.8	21.5	28.2	28.6
Post-tax ROE (%)	(2.3%)	(4.4%)	3.7%	16.2%	(36.5%)
METRICS					
Revenue growth	N/A	17.6%	21.5%	(57.9%)	3.5%
Adj EBITDA growth		N/A	N/A	N/A	N/A
Adj EBIT growth		N/A	N/A	638.0%	(338.9%)
Adj PBT growth		149.8%	(203.0%)	469.5%	(328.2%)
Adj EPS growth		119.2%	(189.2%)	382.8%	(319.0%)
Net asset value growth	N/A	12.9%	26.9%	35.1%	(23.3%)
NAV/share growth	N/A	(2.7%)	10.0%	11.6%	(30.6%)
VALUATION					
EV/Sales (x)	139.9	119.0	97.9	232.7	224.8
EV/EBITDA (x)	N/A	N/A	N/A	N/A	N/A
EV/NOPAT (x)	N/A	N/A	18.5	3.2	N/A
PER (x)	N/A	N/A	14.5	3.0	N/A
Dividend yield	N/A	N/A	N/A	N/A	N/A
FCF yield	(49.6%)	(38.0%)	(26.2%)	(29.3%)	(26.4%)

Source: Company information and Progressive Equity Research estimates

Disclaimers and Disclosures

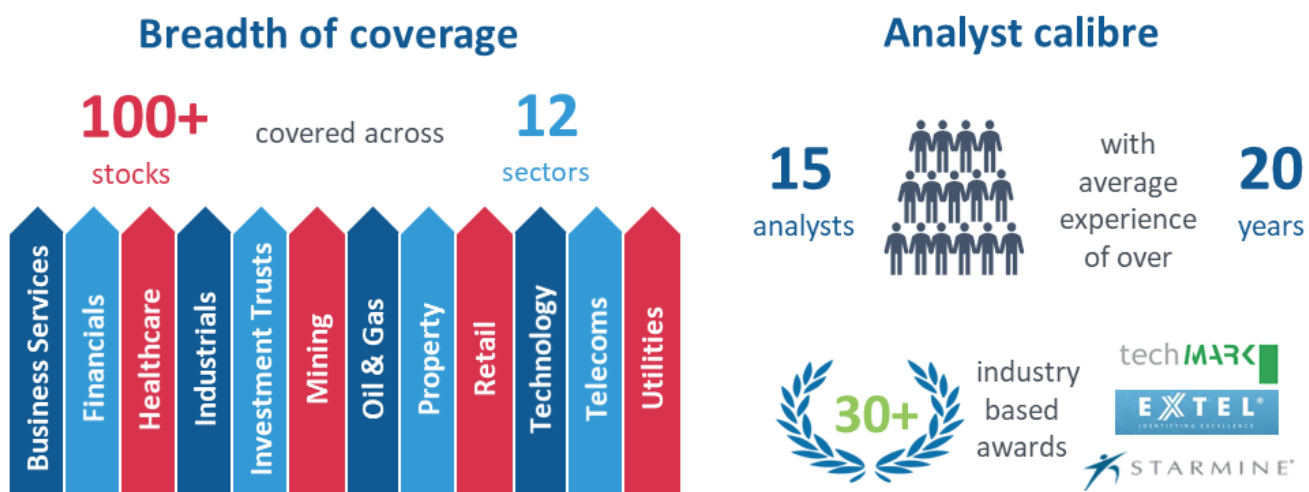
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