

TERN

SOFTWARE AND COMPUTER SERVICES

30 May 2024

TERN.L

2.8p

Market Cap: £12.1m

SHARE PRICE (p)



12m high/low

8.5p/1.7p

Source: LSE Data (priced as at prior close)

KEY DATA

Net (debt)/cash	£0.3m (at 31/12/23)
Enterprise value	£11.8m
Index/market	AIM
Next news	Interims, Nov
Shares in issue (m)	432.7
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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Significantly improved KPIs

Tern's FY23 results highlight improving metrics that should attract additional strategic interest across the portfolio. All companies are gaining significant commercial traction, with configuration work turning to repeat licencing through SaaS models and growing high-profile customer bases. However, valuations across the global technology landscape remain depressed, which has flowed through to Device Authority and Wyld, as detailed overleaf. Therefore, despite the significant improvement in performance metrics, Tern has reported a £12.4m reduction in net assets. We reiterate that Tern's funding-to-exit model requires patience, with all portfolio companies now firmly into their growth stage and leaders in their targeted markets. Management continues to drive value creation from its portfolio of high-growth businesses in sectors poised for substantial growth. We look forward to positive news flow over the coming months.

- Highlights.** Device Authority raised significant new funds, enabling it to build on its partnerships with Microsoft, Entrust, Cybertrak and PTC. FundamentalVR improved revenue and gross margin, building on Apple's continued expansion of activity in the metaverse space, with Meta's global advert campaign also featuring FundamentalVR. Talking Medicines is well established in a category of artificial intelligence (AI) that is achieving 50x revenue multiples, with secured partnerships with Socialgist and Sermo Physician Community. Tern remains set to benefit from the public market valuation as Wyld enters its revenue phase, with strong relationships with the European Space Agency, Eutelsat, Bayer Crop Science and Thales.
- A decrease in valuation metrics across the global technology sector** has led to an £11.1m decrease of Terns portfolio, resulting from investment of £1.4m, disposal of assets of £1.5m, a £0.3m foreign exchange decrease and a negative movement in fair value of investments held of £10.6m. Therefore, the overall fair value of investments as at 31 December 2023 was £12.8m, a 46% decline on the previous year (£23.9m).
- Maximising ARR growth.** Tern describes its portfolio as 'not just surviving, but thriving', with the exception of Konektio, which is now written off. Annual recurring revenue (ARR) rose 50% in FY23, coupled with a rise of 51% in ARR per employee. While we do not expect any near-term rebound in valuations, we believe that Tern provides its shareholders with a diversified way to gain exposure to IoT-related assets. Independent third-party partners have recently been secured, derisking the business, and we expect the continued ARR growth to drive additional strategic interest this year as businesses enter the next phase of growth.

FYE DEC (£M)	2019	2020	2021	2022	2023
Revenue	0.1	0.2	0.1	0.1	0.2
Adj EBITDA	0.0	0.0	0.0	0.0	0.0
Fully Adj PBT	-0.8	0.8	4.6	-10.4	-12.6
Fully Adj EPS (p)	-0.3	0.3	1.3	-2.9	-3.2
Net asset value	18.9	24.0	32.4	24.9	12.3
NAV/share (p)	7.5	8.3	9.2	6.4	3.2
PER (x)	N/A	10.1x	2.1x	N/A	N/A

Source: Company Information and Progressive Equity Research estimates.

This publication should not be seen as an inducement under MiFID II regulations.

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

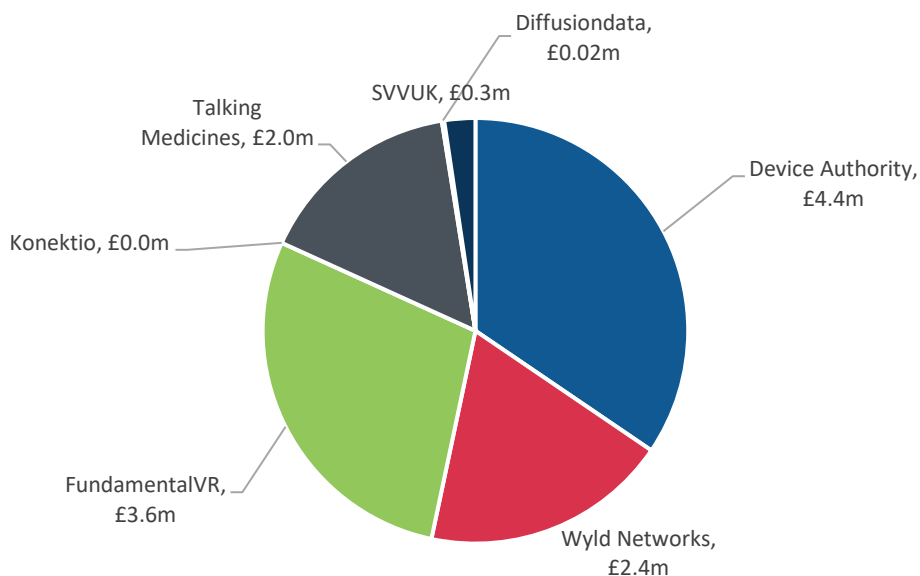
Financial highlights

Tern has built a portfolio of IoT businesses where we see multiple opportunities in sectors poised for exponential growth. We continue to look for significant value creation from Tern’s hybrid VC model, with management seeking well-timed exits that maximise value as business are prepared for harvest. Tern reported a year of further significant progress across the portfolio, delivering growth in its key performance metrics. Annual recurring revenues (ARR) increased 50% in FY23, coupled with a 51% growth in ARR per employee.

However, the continued challenging environment for the technology sector has resulted in further down valuations in Device Authority and Wyld. Therefore, Tern’s net assets were £12.5m, a 50% decline on FY22. Principally due to movements in investments held at fair value through the profit and loss (FVTPL). However, the valuation of Fundamental VR remained static at £3.6m and Talking Medicines actually increased to £2m (FY22: £1.8m). Device Authority decreased by £7.6m to £4.4m due to the latest fundraise valuation. The value of Wyld decreased to £2.4m (FY22: £6.0m), due to realisation of £1.5m in disposed shares and a reduction on Wyld’s market cap to £2.0m (and an exchange rate loss of £0.5m).

Total comprehensive loss for the year was £12.6m (FY22: loss of £10.4m), due to the net negative movement in fair value. Administration costs decreased to £1.7m (FY22: £1.8m), and other expenses decreases to £0.1m (FY22: £0.4m). The year-end cash balance was £298k (FY22: £932k). NAV fell 50% to 3.2p from 6.4p in FY22 (calculated using the year-end number of ordinary shares in issue of 389m).

Tern – NAV breakdown as at 31 December 2023



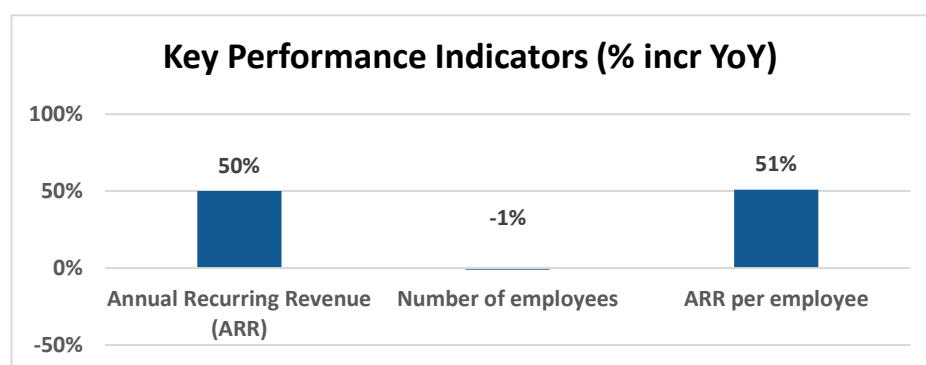
Source: Company data, Progressive Equity Research

Operational highlights

We highlighted individual company progress and customers in our note *Core Portfolio Thriving*, 2 April 2024. Organic delivery has been strong, with significant commercial traction and growing recurring revenues, a key metric in establishing value for a trade sale, IPO or secondary buyout. We summarise the key points and valuations below:

- Wyld Networks (22.5%): £2.4m valuation (FY22: £6.0m). Shipping of Wyld Terminals started in October 2023. Wyld has expanded its portfolio with the launch of Wyld Fusion, a hybrid terrestrial and satellite platform. Wyld estimates its total addressable market, which includes ISM band, NB-IoT, S-band and Wyld Fusion, to be \$4.3bn.
- Device Authority (35.7%): £4.4m valuation (FY22: £11.9m). DA has experienced material growth in ARR from its subscription base, and at the recent capital markets event, management alluded to tripling the ARR over the next year. Partnering with Ten Eleven is a significant milestone, attracting ‘intelligent growth funding’ from a partner with substantial experience and reach across the US.
- FundamentalVR (12.1%): £3.6m valuation (FY22: £3.6m). FundamentalVR has continued to build ARR during 2023, with a healthy pipeline of customers and new client opportunities looking to deploy Fundamental Surgery. It has significant traction and ‘stickiness’ with its clients, affiliated with institutions like the American Academy of Ophthalmology (AAO), the American Academy of Orthopaedic Surgeons (AAOS), and the Royal College of Surgeons of England. Meta is also showcasing FVR and its work with Orbis on eye surgery training.
- Talking Medicines (23.8%): £2.0m valuation (FY22: £1.8m). Talking Medicines is gaining traction using its curated AI model to source patient feedback and has successfully expanded into the US market. The subscription base is expanding for its SaaS on-demand product, with its Drug-GPT interface recently launched, a ChatGPT counterpart specifically for the drug development industry.
- Konektio: Nil valuation (FY22: £0.5m). The equity value of Konektio was written off as the company entered into administration.
- Diffusiondata (<1%): £0.02m valuation (FY22: £0.02m).
- SVVUK (5.9%): £0.3m valuation (FY22: £0.1m).

Tern KPIs



Source: Company data, Progressive Equity Research

Conclusion

Management has reiterated its strategy to pursue rapid, high-growth opportunities, supporting entrepreneurs by providing the necessary capital. Given the challenging economic backdrop, Tern is assisting portfolio companies to become sustainable opportunities, rather than seeking market dominance, while reducing burn rates and driving value-creating growth.

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

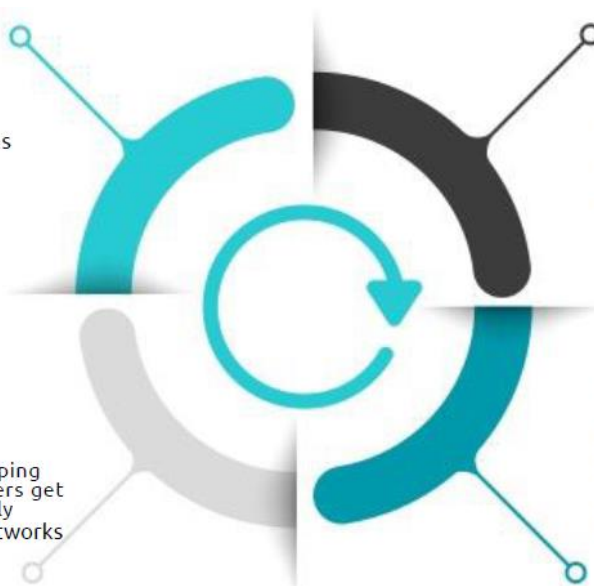
- Value Add through hands on approach
- Focused on helping and developing portfolio companies and Founders get to scaling industry metrics rapidly
- Leveraging our contacts and Networks

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

We remain optimistic about the outlook for Tern. Efforts to date have propelled the four key portfolio companies to become technology leaders, albeit with relatively limited funding. All four businesses are on a positive trajectory, with significant momentum. We see huge potential in the next phase of growth as portfolio companies work with investment partners to achieve additional recognition and scale.

The strategic importance of expanding sales operations is key to success, especially when competing with companies often backed by significant investment capital. Although Tern will where possible participate in fundraises to avoid dilution, its early entry at seed and seed plus allows it to retain a more substantial share. Tern's investment proportion has been relatively small in the most recent rounds, demonstrating that the capital requirements are reducing as the businesses become attractive to third-party investors.

We recognise that Tern's commitment extends beyond financial support as it negotiates the best deals for shareholders during engagements with new investors, with the end goal to facilitate successful exits for all shareholders in a timely and prudent manner.

Financial Summary: Tern

Year end: December (£m unless shown)

	2019	2020	2021	2022	2023
PROFIT & LOSS					
Revenue	0.1	0.2	0.1	0.1	0.2
Adj EBITDA	0.0	0.0	0.0	0.0	0.0
Adj EBIT	0.0	0.6	4.4	(10.5)	(12.7)
Reported PBT	(0.8)	0.8	4.6	(10.4)	(12.6)
Fully Adj PBT	(0.8)	0.8	4.6	(10.4)	(12.6)
NOPAT	(0.8)	0.8	4.6	(10.4)	(12.6)
Reported EPS (p)	(0.3)	0.3	1.3	(2.9)	(3.2)
Fully Adj EPS (p)	(0.3)	0.3	1.3	(2.9)	(3.2)
Dividend per share (p)	0.0	0.0	0.0	0.0	0.0
CASH FLOW & BALANCE SHEET					
Operating cash flow	(1.3)	(1.2)	(1.5)	(2.1)	(1.4)
Free Cash flow	(3.8)	(3.1)	(4.0)	(3.8)	(1.1)
FCF per share (p)	(1.5)	(1.0)	(1.2)	(1.1)	(0.3)
Acquisitions	0.0	0.0	0.0	0.0	0.0
Disposals	0.0	0.0	0.0	0.0	0.0
Shares issued	2.9	4.2	3.8	2.8	0.4
Net cash flow	(0.9)	1.1	(0.2)	(1.0)	(0.6)
Overdrafts / borrowings	0.0	0.0	0.0	(0.4)	(0.4)
Cash & equivalents	1.0	2.1	2.0	0.3	0.0
Net (Debt)/Cash	1.0	2.1	2.0	(0.1)	(0.4)
NAV AND RETURNS					
Net asset value	18.9	24.0	32.4	24.9	12.3
NAV/share (p)	7.5	8.3	9.2	6.4	3.2
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	17.8	21.5	28.2	28.6	18.6
Post-tax ROE (%)	(4.4%)	3.7%	16.2%	(36.5%)	(67.9%)
METRICS					
Revenue growth	N/A	21.5%	(57.9%)	3.5%	201.8%
Adj EBITDA growth		N/A	N/A	N/A	N/A
Adj EBIT growth		N/A	638.0%	(338.9%)	N/A
Adj PBT growth		(203.0%)	469.5%	(328.2%)	20.7%
Adj EPS growth		(189.2%)	382.8%	(319.0%)	10.8%
Net asset value growth	N/A	26.9%	35.1%	(23.3%)	(50.5%)
NAV/share growth	N/A	10.0%	11.6%	(30.6%)	(50.7%)
VALUATION					
EV/Sales (x)	94.7	78.0	185.3	179.0	59.3
EV/EBITDA (x)	N/A	N/A	N/A	N/A	N/A
EV/NOPAT (x)	N/A	14.7	2.6	N/A	N/A
PER (x)	N/A	10.1	2.1	N/A	N/A
Dividend yield	N/A	N/A	N/A	N/A	N/A
FCF yield	(54.3%)	(37.5%)	(41.9%)	(37.7%)	(9.8%)

Source: Company information and Progressive Equity Research estimates

Disclaimers and Disclosures

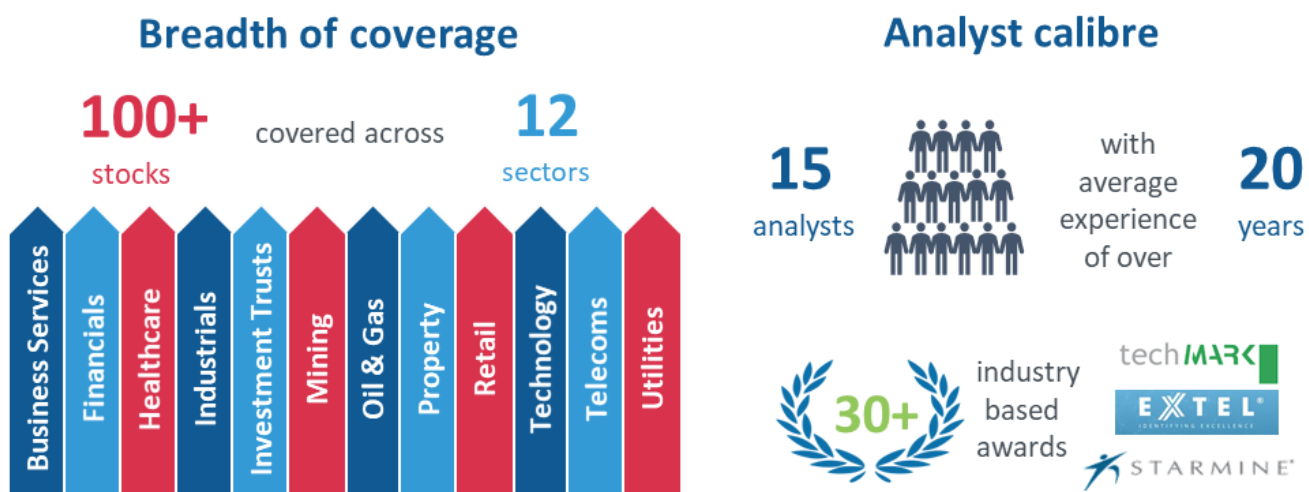
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