EDISON

# Allied Minds

## Meeting of minds with shareholders

Restructuring

Alternative asset manager

13 December 2019

**Following a dialogue with shareholders, Allied Minds has announced a number of restructuring initiatives, including board changes, to cut costs and better align employee and shareholder interests. Mike Turner will step down as co-CEO, leaving Joe Pignato as CEO and CFO. The company has made amendments to the executive director compensation plan, including a reduction of the maximum bonus, elimination of the Management Incentive Plan and forfeiture of certain long-term incentive plan (LTIP) grants. These restructuring initiatives will allow recurring central costs to be cut by 20%, to $6m pa, in line with the Strategic Review announced in April 2019. Allied Minds now expects to be able to return c $40m (12.4p per share) to shareholders from the proceeds of the disposal of Hawkeye 360 ($65.6m) by early Q120.**

| Period end | Portfolio fair value (US$m) | Parent-level net cash (US$m) | NAV (US$m) | NAV/share (p) | P/NAV (x) |
|---|---|---|---|---|---|
| 12/17 | 395.6 | 84.2 | 479.8 | 150.0 | 0.29 |
| 06/18 | 350.1 | 66.0 | 416.1 | 132.4 | 0.33 |
| 12/18* | 226.7 | 50.6 | 277.3 | 88.8 | 0.50 |
| 06/19*,** | 266.1 | 31.3 | 297.3 | 91.9 | 0.48 |

Note: NAV is calculated as fair value plus net cash at the parent level. *FY18/H119 NAV is based on our estimate of fair value as this is no longer disclosed by the company. **H119 net cash and NAV are adjusted for post period-end investments.

## Board changes and restructuring

Mike Turner will step down as co-CEO effective 10 March 2020. Joe Pignato will continue in the role of CEO and CFO (previously co-CEO and CFO). Fritz Foley (non-executive director) will step down from the board with Harry Rein, the senior independent non-executive director, becoming chair of the company's audit committee in his place. Additionally, Mark Lerdal (Leaf Clean Energy, MP2 Capital, KKR Finance) has been appointed as a non-executive director with immediate effect.

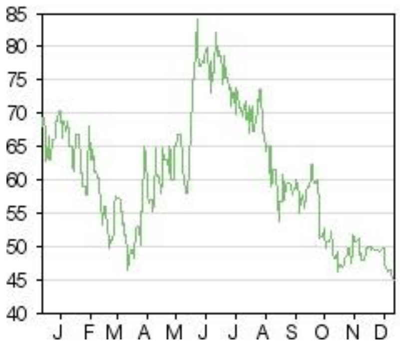
The transition to a single CEO, together with the additional cost-cutting measures announced, will allow Allied Minds to cut its central costs by an additional 20% to c $6m pa. This will allow it to increase the amount of capital to be returned to shareholders from the disposal of Hawkeye 360 to $40m (12.4p per share) from $32.8m (10.1p per share) previously, while still ensuring the company has sufficient cash to allow it to continue to invest in its existing assets and maximise the value of its portfolio over the medium term.

## Valuation: Unjustified 52% discount to NAV

Allied Minds' shares trade materially below the range of its peer group and at a 52% discount to our adjusted estimate of H119 NAV of 91.9p, or a 45% discount on a fully-diluted basis. We believe this level of discount is unwarranted with key assets recently validated by third-party strategic investors, together with the $40m (12.4p) return of capital expected in Q120. With management focused on preserving cash and delivering material cash exits from its remaining portfolio, we believe this provides a solid NAV on which Allied Minds should build over time.

| | |
|---|---|
| **Price** | **44.2p** |
| **Market cap** | **£107m** |
| | US$1.34/£ |
| Parent cash ($m) at 30 June 2019 | 46.6 |
| Shares in issue | 241.3m |
| Free float | 91% |
| Code | ALM |
| Primary exchange | LSE |
| Secondary exchange | N/A |

### Share price performance




| % | 1m | 3m | 12m |
|---|---|---|---|
| Abs | (10.2) | (24.1) | (36.4) |
| Rel (local) | (9.6) | (24.0) | (40.7) |
| 52-week high/low | | 84.2p | 44.2p |

### Business description

Allied Minds is a technology investment company with a concentrated portfolio focused on early-stage spin-outs from US federal government laboratories and universities.

### Next events

| | |
|---|---|
| Return of capital | Early Q120 |
| Trading statement | February 2020 |
| Full year results | April 2020 |

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## Board changes and restructuring

The transition to a single CEO, together with additional cost-cutting measures, will allow Allied Minds to cut its central costs by an additional 20% to c $6m per annum (in line with the Strategic Review announced in April 2019) on a recurring basis commencing 1 January 2020.

## Shareholder engagement

Following a constructive dialogue with investors, the board has announced further restructuring initiatives to reduce costs and further align employee and shareholder interests. Allied Minds' major shareholders have supported these changes and, on the basis of the announced changes, Crystal Amber Fund has also withdrawn (Requisition Withdrawal) the notice of requisition (Meeting Requisition) from 21 November 2019.

## Board changes

Mike Turner will step down as co-CEO and departs with effect from 10 March 2020. Joe Pignato will continue in the role of CEO and CFO (previously co-CEO and CFO). Fritz Foley (non-executive director) will step down from the board with Harry Rein, the senior independent non-executive director, stepping up to become Chair of the company's audit committee in his place. Additionally, Mark Lerdal (Leaf Clean Energy Company, MP2 Capital, KKR Finance) has been appointed as a non-executive director with immediate effect.

Jeff Rohr will continue as chairman of the board through to the end of his second three-year term ending in June 2020, at which point he will retire from the board.

## Executive remuneration

The company has also made amendments to the executive director compensation plan, including a reduction of the maximum bonus, elimination of the Management Incentive Plan and forfeiture of certain LTIP grants. Modifications to the Phantom Plan staff remuneration scheme will include the establishment of a threshold that must be met before any future payments are made to participants under the plan.

No further allocations under the Phantom Plan (subsequent to the Hawkeye 360 distribution) will be made until gross proceeds from future portfolio company liquidity events exceed the invested capital (the initial threshold of $109m represents the total capital invested in the technology portfolio to date). The threshold will increase as additional capital is invested into the existing portfolio.

Current employee unit holders in the Phantom Plan have agreed to an individual cap per employee following the disbursement from the sale of Hawkeye 360. As a result, excess proceeds above this cap due to employee departures will revert to the company and be available for distribution to shareholders, meaning that the percentage of net proceeds allocated to the Phantom Plan will decline over time.

Joe Pignato has voluntarily agreed to reduce his annual bonus target to 100% of base salary from 150%. After Mike Turner's resignation (10 March 2020), as the last remaining employee with an interest in the Management Incentive Plan, Joe Pignato has agreed to forfeit his interest in the plan. In addition, Joe Pignato has also forfeited his last two remaining LTIP awards subject to share performance from 2017 and 2018, which were awarded prior to him being named an executive director.

## Central costs and return of capital to shareholders

Together, these initiatives are expected to further reduce recurring HQ expenses to no more than $6.0m from 1 January 2020, in line with management's strategic review announced in April 2019 (Doubling down on the winners), representing a 20% reduction from the company's most recent guidance of $7.5m.

The additional HQ savings also allow the company to increase the amount of capital to be returned to shareholders from the disposal of Hawkeye 360. This amount is expected to increase to $40m, from the initial estimate of $32.8m, while still ensuring the company has sufficient cash to allow it to continue to invest in existing assets and maximise the value of its portfolio over the medium term, a potential three- to four-year time horizon. The company has now completed the court process and upon completion of statutory filings, management will be in a position to confirm the dates and method for returning capital to shareholders. The return of capital is expected to complete early in Q120.

## Valuation: Unjustified 52% discount to NAV

As we have noted previously, given its narrowed portfolio, Allied Minds now looks less like its patient capital and direct investment peers, as it offers look-through to a concentrated number of emerging US-based technology businesses. Given Allied Minds' focus on technology, we have chosen to exclude healthcare and life science investors from the comparator group as these are no longer relevant benchmarks.

Allied Minds' shares currently trade at a 52% discount to our adjusted estimate of H119 NAV of 91.9p (lower following the significant recent strength of sterling), or a 45% discount on a fully-diluted basis. Allied Minds' shares also trade materially below the range of its peer group (see Exhibit 1). On this basis, for investors who like the key assets in Allied Minds' portfolio, all of which have been validated by third-party investors in recent funding rounds, we believe this level of discount is unwarranted.

**Exhibit 1: Peer group comparison**

| | Price (p) | Market cap £(m) | NAV (£m) (last reported) | Cash/(debt) (£m) | NAV premium/ discount | NAV per share (p) |
|---|---|---|---|---|---|---|
| Allied Minds | 44.2 | 107 | 222* | 23 | 0.48 | 91.9 |
| Augmentum FinTech | 103.5 | 120.8 | 135 | 51 | 0.90 | 114.9 |
| Draper Esprit | 477.0 | 560.8 | 699 | 100 | 0.80 | 593.0 |
| HgCapital | 251.0 | 1,012.6 | 984 | 79 | 1.02 | 245.0 |
| IP Group | 60.4 | 637.8 | 1,172 | 71 | 0.54 | 110.6 |
| Mercia Asset Management | 25.5 | 77.1 | 125 | 38 | 0.62 | 41.3 |
| Oakley Capital | 239.5 | 483.8 | 650 | 96 | 0.74 | 317.0 |
| **Mean** | | | | | **0.70** | |
| **Median** | | | | | **0.77** | |

Source: Refinitiv data; Edison Investment Research. Note: Priced at 12 December 2019. *Edison's adjusted estimate of H119 NAV.

**Exhibit 2: Financial summary**

| $000 | 2014 | 2015 | 2016 | 2017 | 2018 |
|---|---|---|---|---|---|
| Year end 31 December | IFRS | IFRS | IFRS | IFRS | IFRS |
| **INCOME STATEMENT** | | | | | |
| Revenue | 7,715 | 3,300 | 2,664 | 5,001 | 5,561 |
| Cost of Sales | (5,416) | (3,925) | (5,563) | (5,242) | (2,827) |
| Gross Profit | 2,299 | (625) | (2,899) | (241) | 2,734 |
| Normalised operating profit | (47,510) | (89,372) | (103,925) | (94,542) | (83,583) |
| Amortisation of acquired intangibles | 0 | 0 | 0 | 0 | 0 |
| Exceptionals | (1,479) | (309) | (1,365) | (2,363) | (545) |
| Share-based payments | (8,939) | (7,041) | (8,385) | (7,562) | (7,413) |
| Reported operating profit | (57,928) | (96,722) | (113,675) | (104,467) | (91,541) |
| Net Interest | 222 | 670 | 2,318 | 305 | 1,313 |
| Joint ventures & associates (post tax) | 0 | 0 | 0 | 0 | (1,301) |
| Fair value changes | 0 | (1,937) | (17,585) | (6,953) | 138,841 |
| Profit Before Tax (norm) | (47,288) | (90,639) | (119,192) | (101,190) | 55,270 |
| Profit Before Tax (reported) | (57,706) | (97,989) | (128,942) | (111,115) | 47,312 |
| Reported tax | 0 | 0 | 0 | 0 | 0 |
| Profit After Tax (norm) | (47,288) | (90,639) | (119,192) | (101,190) | 55,270 |
| Profit After Tax (reported) | (57,706) | (97,989) | (128,942) | (111,115) | 47,312 |
| Minority interests | 12,228 | 20,192 | 32,609 | 35,337 | (7,990) |
| Discontinued operations | 0 | 0 | 0 | 0 | 0 |
| Net income (normalised) | (35,060) | (70,447) | (86,583) | (65,853) | 47,280 |
| Net income (reported) | (45,478) | (77,797) | (96,333) | (75,778) | 39,322 |
| Basic average number of shares outstanding (m) | 186 | 215 | 217 | 236 | 241 |
| EPS - basic normalised ($) | (0.19) | (0.33) | (0.40) | (0.28) | 0.20 |
| EPS - diluted normalised ($) | (0.19) | (0.33) | (0.40) | (0.28) | 0.20 |
| EPS - basic reported ($) | (0.24) | (0.36) | (0.44) | (0.32) | 0.16 |
| Dividend ($) | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Revenue growth (%) | N/A | (57.2) | (19.3) | 87.7 | 11.2 |
| Gross Margin (%) | 29.8 | N/A | N/A | N/A | 49.2 |
| Normalised Operating Margin | N/A | N/A | N/A | N/A | N/A |
| **BALANCE SHEET** | | | | | |
| Fixed Assets | 44,039 | 92,784 | 38,232 | 28,369 | 86,096 |
| Intangible Assets | 3,409 | 4,384 | 2,762 | 1,074 | 1,221 |
| Tangible Assets | 16,330 | 34,173 | 31,882 | 26,627 | 5,997 |
| Investments & other | 24,300 | 54,227 | 3,588 | 668 | 78,878 |
| Current Assets | 248,991 | 158,427 | 232,007 | 184,792 | 107,034 |
| Stocks | 2,919 | 1,511 | 2,551 | 0 | 0 |
| Debtors | 6,305 | 7,342 | 5,900 | 15,642 | 6,400 |
| Cash & cash equivalents | 224,075 | 105,555 | 209,151 | 158,075 | 100,234 |
| Cash at parent* | N/A | N/A | 136,700 | 84,200 | 50,600 |
| Other | 15,692 | 44,019 | 14,405 | 11,075 | 400 |
| Current Liabilities | (62,480) | (108,974) | (155,402) | (200,202) | (69,557) |
| Creditors | (11,339) | (14,268) | (13,941) | (14,276) | (13,030) |
| Tax and social security | (947) | (395) | (458) | (4,296) | (2,333) |
| Short term borrowings | (213) | (228) | (115) | 0 | 0 |
| Subsidiary preferred shares | (49,981) | (94,083) | (140,888) | (181,630) | (54,194) |
| Long Term Liabilities | (717) | (863) | (720) | (867) | (436) |
| Long term borrowings | (338) | (112) | 0 | 0 | 0 |
| Other long term liabilities | (379) | (751) | (720) | (867) | (436) |
| Net Assets | 229,833 | 141,374 | 114,117 | 12,092 | 123,137 |
| Minority interests | 4,946 | 10,631 | 20,797 | 59,241 | 4,490 |
| Shareholders' equity | 234,779 | 152,005 | 134,914 | 71,333 | 127,627 |
| **CASH FLOW** | | | | | |
| Op Cash Flow before WC and tax | (44,618) | (85,286) | (97,290) | (88,440) | (77,525) |
| Working capital | (981) | 2,652 | 468 | (2,477) | 6,033 |
| Exceptional & other | 0 | 0 | 0 | 0 | (283) |
| Tax | 0 | 0 | 0 | 0 | 0 |
| Net operating cash flow | (45,599) | (82,634) | (96,822) | (90,917) | (71,775) |
| Capex | (1,764) | (23,213) | (4,087) | (1,522) | (9,110) |
| Acquisitions/disposals | (38,967) | (51,786) | 74,816 | 5,853 | (18,884) |
| Net interest | 222 | 716 | 1,602 | 138 | 896 |
| Equity financing | 154,408 | 2,443 | 79,319 | 1,595 | 1,594 |
| Dividends | 0 | 0 | 0 | 0 | 0 |
| Other | 54,473 | 36,165 | 48,993 | 33,892 | 39,438 |
| Net Cash Flow | 122,773 | (118,309) | 103,821 | (50,961) | (57,841) |
| Opening net debt/(cash) | N/A | (223,524) | (105,215) | (209,036) | (158,075) |
| FX | 0 | 0 | 0 | 0 | 0 |
| Other non-cash movements | 0 | 0 | 0 | 0 | 0 |
| Closing net debt/(cash) | (223,524) | (105,215) | (209,036) | (158,075) | (100,234) |

Source: Company accounts. Note: *For clarity, cash at parent has been broken out as a separate line from cash & cash equivalents. As a line item, it does not form part of the calculation for current assets.

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