

Allied Minds

NAV upside with additional 'option' value

Allied Minds made significant progress in FY19, focusing on its slimmed down portfolio of seven investee companies, with strategic funding rounds for Federated Wireless (FW) and HawkEye 360, before the sale of HawkEye 360. Recurring central costs have been cut to \$6m in FY20, with a headcount of seven. Post the period-end, FW announced partnerships with AWS and Microsoft Azure with initial revenues expected in FY20. Parent cash at 31 December 2019 was \$84.1m. The company no longer discloses NAV, but we estimate net cash at 4 June 2020 of \$31.9m (adjusted for the 12.6p special dividend, investments and costs) and NAV of 90.9p/share (78.4p/share fully diluted). Based on seemingly conservative valuations, the shares trade at a 56–62% discount to our estimated NAV.

Period end	Portfolio fair value (US\$m)	Parent-level net cash (US\$m)	NAV (US\$m)	NAV/share (p)	P/NAV (x)
06/18	350.1	66.0	416.1	132.4	0.26
12/18	226.7	50.6	277.3	88.8	0.38
06/19*	266.1	31.3	297.3	100.2	0.34
12/19*	209.0	31.9	240.8	78.4	0.44

Note: NAV is calculated as fair value plus net cash at the parent level and is based on our estimate of fair value as this is no longer disclosed by the company. *H119 and FY19 net cash and NAV are adjusted for post period-end investments.

FY19 results

FY19 results were dominated by the deconsolidation of subsidiaries (the holding in FW fell from 52.2% to 42.6% at YE19). FY19 revenues fell to \$2.7m (2018: \$5.6m) with R&D falling by 36% to \$16.1m (2018: \$44.9m). Net profit rose to \$50.3m (FY18: \$45.4m restated). Investments at fair value increased to \$61.9m (2018: \$56.5m) reflecting a \$37.5m increase in fair value adjustments, with \$22.2m from the deconsolidation of Federated Wireless. Cash and cash equivalents decreased by \$7.2m to \$90.6m (2018: \$97.7m), with \$84.1m held at the parent level (2018: \$50.6m).

Portfolio update: Core assets continue to progress

With demonstrable progress at FW (fair value unchanged) and management confident of progress at Spin Memory and BridgeComm (partners prefer progress to remain confidential), Allied Minds' remaining portfolio appears sound. The three principal investments represent 95% of fair value, while TableUp, Orbital Sidekick, Spark Insights and SciFluor offer additional option value. Recurring central costs have been cut to c \$6m pa, giving management the three- to four-year cash runway it sought to maximise returns from the remaining portfolio.

Valuation: 56%+ discount to robust NAV

Allied Minds paid a special dividend of 12.62p in Q120 (\$40m in total) from the sale of HawkEye 360. With this material cash exit validating the investment model, together with the group's focus on cash preservation, we believe this provides a solid platform for robust NAV progress over time. The 56–62% discount to NAV does not reflect the prospects of the group's streamlined portfolio – we estimate NAV per share of 90.9p (undiluted), or 78.4p fully diluted.

FY19 results update

Investment companies

9 June 2020

Price **34.13p**

Market cap **£82m**

US\$1.27/£

Parent cash (\$m) at 31 December 2019 84.1

Shares in issue 241.6m

Free float 91%

Code ALM

Primary exchange LSE

Secondary exchange N/A

Share price performance



% 1m 3m 12m

Abs 0.4 1.0 (41.5)

Rel (local) (8.4) 1.5 (34.5)

52-week high/low 87p 28p

Business description

Allied Minds is an IP commercialisation company with a concentrated investment portfolio predominantly focused on early-stage technology companies. Its portfolio companies are spinouts from US federal government laboratories and universities.

Next events

AGM June 2020

Interim results September 2020

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FY19 results summary

As with FY18, the group's results were dominated by the impact of the deconsolidation of subsidiaries (ALM's holding in FW fell from 52.2% to 42.6% at YE19, now 43.1%). Allied Minds also restated its FY18 figures to reflect valuation and accounting errors on the deconsolidation of Spin Memory and HawkEye 360, including a \$2.4m understatement of associate's losses for Spin Memory; the gain on the deconsolidation of Spin Memory was understated by \$16.4m; and the gain on the deconsolidation of HawkEye 360 was overstated by \$11.1m.

During FY19, revenues from engineering and service contracts fell to \$2.7m (2018: \$5.6m), primarily due to the deconsolidation of Federated Wireless in FY19, as well as the deconsolidation of HawkEye 360 and Spin Memory at the end of FY18. This was in part offset by new contract revenue from BridgeComm of \$1.0m.

Cost of revenue at \$1.4m in FY19 (2018: \$2.8m) fell largely in line with revenues. SG&A expenses decreased by 30%, to \$34.3m (2018: \$49.3m), with the reduction in central costs implemented in FY19, as well as restructuring charges for subsidiaries closed or deconsolidated in FY18 and FY19. For similar reasons, R&D fell by 36%, to \$16.1m (2018: \$44.9m).

Net finance income fell to \$10.0m (2018: \$92.9m) due to the deconsolidation of subsidiaries, partly offset by \$9.3m (2018: \$91.6m) from IFRS 9 fair value accounting adjustments. Other income rose to \$89.4m (2018: \$44.0m, restated), partly offset by the company's share of the \$28.9m loss from the deconsolidated entities. Together, this resulted in net profit rising to \$50.3m (FY18: \$45.4m restated).

Investments held at fair value increased to \$61.9m (2018: \$56.5m) reflecting a \$37.5m increase in fair value adjustments, with \$22.2m from the deconsolidation of Federated Wireless. The increase was offset by the sale of Allied Minds' stake in HawkEye 360 for a cash consideration of \$65.6m.

Cash and cash equivalents decreased by \$7.2m to \$90.6m (2018: \$97.7m), with net cash of \$69.8m used in operations, \$26.5m cash from investing activities and \$33.7m cash from financing activities. Of this net cash figure, \$84.1m (2018: \$50.6m) was held at the parent level.

Outlook: Portfolio progress continuing

In FY19, management largely delivered on the measures outlined in the April 2019 strategic review:

- focus remaining cash resources on key assets in the current portfolio;
- new investment on indefinite hold; and
- further cuts to central costs (to reduce opex to \$5–6m pa).

With cost efficiencies implemented including restructuring management incentive schemes, reducing headcount, subletting its HQ office space and eliminating other non-essential third-party costs, on 11 December 2019 management confirmed that recurring central costs would be approximately \$6m from 1 January 2020 (although there are expected to be incremental one-off items eg severance payments).

Allied Minds' portfolio has been shrunk to seven assets, of which only three are material, with the other four representing 'option value'. The sale of HawkEye 360 led to a subsequent \$40m (12.62p per share) return of proceeds from the disposal, paid in February 2020.

With estimated net cash of \$31.9m at 4 June 2019 (adjusted for the 12.6p special dividend, investments and costs), management expects to have sufficient cash to allow it to continue to

invest in existing assets and maximise the value of its portfolio to shareholders over a three- to four-year time horizon.

In terms of its three principal assets, Allied Minds also reiterated the key operational objectives for each over the course of FY20:

Exhibit 1: FY20 portfolio company key operational objectives

Federated Wireless

- Build a significant pipeline of annual recurring revenue
- Meet customer service level agreement and service level objective targets
- Develop and launch a scalable cloud enterprise solution

Spin Memory

- Expand the commercial relationship with Applied Materials, including securing the first turnkey magnetics licence customer
- Expand the design pipeline with Arm and secure its first macro deals
- Expand upon opportunity provided by the US government project

BridgeComm

- Successfully execute the development of applications of one-to-many (OTM) technology with Boeing HorizonX Ventures
- Expand the capacity of the global ground network through industry partnerships and ground station installations
- Expand government customer backlog

Source: Allied Minds

Portfolio: Demonstrable progress achieved in FY19 and 2020

Each of these principal assets made demonstrable progress during FY19 and post year end in FY20, but developments often remain confidential until key partners are ready to disclose progress. All valuations remain unchanged from the values established at the last major funding rounds.

Federated Wireless – ‘significant progress’ since last funding round

In February 2020, Federated Wireless announced new connectivity-as-a-service (CaaS) offerings with Microsoft Azure and Amazon Web Services (AWS), bringing to market the first private 4G/5G wireless cloud solution ([Federated Wireless moves towards commercialisation](#)). The company also announced trials with the UK government, highlighting the untapped international potential of its technology. In April 2020 Federated Wireless raised an additional \$13.7m (split equally between Allied Minds and Pennant Investors) in an extension round to the September 2019 Series-C funding round ([FW accelerates Microsoft and AWS partnerships](#)).

BridgeComm – ‘reasonable progress’ since last funding round

BridgeComm entered a joint development agreement with Boeing HorizonX Ventures (Boeing) to collaborate on its OTM technology (bi-directional, ultra-high-speed mesh connectivity for terrestrial, airborne and space systems), a development from its initial point-to-point solution. The development programme is expected to be completed in phases over the course of FY20–21. In December 2019, BridgeComm secured \$1.0m of funding by way of convertible debt from Boeing, with an additional \$1.5m committed subject to milestones. Allied Minds subsequently subscribed for \$2.0m of convertible debt on the same terms.

Spin Memory – ‘significant progress’ since last funding round

During FY19, Spin Memory achieved significant technical milestones with both Arm and Applied Materials. With Arm, Spin Memory completed the design of a prototype demonstration vehicle of Spin Memory’s Endurance Engine coupled with a working MRAM array to show an order of magnitude improvement in MRAM endurance, one of the key challenges in the industry. The demonstration vehicle will also show the performance of many other patented circuits. The prototype and test results are expected later this year. In magnetics, Spin Memory and Applied Materials also made good progress with MRAM solutions, which are expected to displace most on-chip memory, including both long-term storage (Flash) and working memory (SRAM). High-

temperature data retention (critical for long-term memory storage) was demonstrated with good yield. In FY19 Spin Memory was also awarded a 'multi-phase, multi-year, multi-million dollar' US government project as the sub-contractor to a leading US semiconductor company.

COVID-19: Slowdown in progress

The company confirmed that, with adequate cash reserves to cover central costs until 2023, COVID-19 has not had a direct impact on Allied Minds. However, as experienced by the company in the preparation of its final FY19 accounts, we would expect a slowdown in progress for a number of its portfolio companies while travel restrictions persist.

Portfolio: Condensed, with solid underpinnings

Exhibit 2 sets out our NAV estimate (as at 4 June 2020) based on the FY19 portfolio fair values.

Exhibit 2: Allied Minds' portfolio – Edison fair value estimate										
Company	Business description	Latest funding round	Latest post-money value (100%) (\$m)	Undiluted value* (\$m)	P / share	Fully diluted value* (\$m)	P / share	ALM holding 4/6/20	ALM fully diluted holding**	Basis of estimate for fair value assessment
Federated Wireless	Cloud-based SaaS business	Sep 19	215.0	92.7	30.2	78.7	25.6	43%	37%	Valuation of last round (Strategics)
Spin Memory	MRAM semiconductor memory	Apr 19	172.0	73.4	23.9	57.3	18.8	43%	33%	Valuation of last round (Strategics)
BridgeComm	Optical communications service provider	Sep 18	38.0	30.9	10.1	23.9	7.8	81%	63%	Valuation of last round (Strategics)
TableUp	Restaurant supply chain software provider	Apr 18	12.0	4.3	1.4	3.6	1.2	36%	30%	Valuation of last round
Orbital Sidekick	Space-based hyperspectral imaging and analytics	Apr 18	11.7	3.9	1.3	3.5	1.1	33%	30%	Valuation of last round (third-party)
Spark Insights	Property insurance analytics	Apr 19	3.2	2.3	0.7	1.9	0.6	71%	60%	Valuation of last round
SciFluor	Developer of a topical eye droplet treatment	Nov 19	130.7	-	-	-	-	63%	54%	Written down to zero
Special dividend (HawkEye 360)	Payable post year-end on 14 February 2020			40.0	12.6	40.0	12.6			
Portfolio fair value (year end)				247.4	80.1	209.0	67.7			
Net cash at parent company (year end)				84.1	27.4	84.1	27.4			
Post year-end adjustments										
Investments (post period end)				(9.2)	(3.0)	(9.2)	(3.0)			
Special dividend				(40.0)	(12.6)	(40.0)	(12.6)			
Cash burn				(3.0)	(1.0)	(3.0)	(1.0)			
Parent net cash (latest)				31.9	10.8	31.9	10.8			
Estimated NAV (latest)				279.3	90.9	240.8	78.4			
Estimated NAV (pence per share)					90.9		78.4			
Latest share price					34.1		34.1			
Share price discount to estimated NAV					62%		56%			

Source: Allied Minds data, Edison Investment Research. Note: *As at 31 December 2019. **As at 4 June 2020.

By way of commentary on Exhibit 2, our fair value estimate includes valuations on both an undiluted and fully diluted basis; the realisation value of any asset is likely to fall between these two values.

The FY19 net cash position includes the special dividend of 12.62p (\$40m in total) paid in February 2020 from the sale proceeds of HawkEye 360. To the \$84.1m parent cash figure, we have then deducted: 1) the \$40m special dividend; 2) post year-end investments including \$2.0m in convertible notes in BridgeComm, \$0.375m in convertible notes in SciFluor and \$6.85m in the Federated Wireless extension round; and 3) an allowance for central costs of \$3m (at a rate slightly above the \$0.5m per month targeted to allow for one-off costs).

This leads to our NAV estimate of 90.9p per share (undiluted) or 78.4p per share (fully diluted), based on historical portfolio company fair values, none of which have been updated subsequent to their last major funding rounds despite continuing positive newsflow.

Valuation: 56–62% discount to robust NAV

As a technology holding company with a narrow portfolio, Allied Minds offers exposure to a concentrated number of emerging technology businesses.

Allied Minds paid a special dividend of 12.62p in Q120 (\$40m in total) from the sale of HawkEye 360. This material cash exit helps to validate the investment model and together with the group's focus on cash preservation and reduction in operating costs, we believe it provides a solid platform for robust NAV progress over time.

With our estimated NAV of 90.9p per share (undiluted) or 78.4p per share (fully diluted) (Exhibit 2), the implied 56–62% discount to NAV does not reflect the prospects of the group's streamlined portfolio.

For reference, we also include Allied Minds' peer group NAV discounts below in Exhibit 3.

Exhibit 3: Peer group comparison						
	Price (p)	Market cap (£m)	NAV (£m) (last reported)	Cash (£m)	NAV premium/ discount (x)	NAV per share (p)
Allied Minds	34.1	82.0	191	25	0.44	78.4
Augmentum FinTech	105.0	121.2	131	29	0.92	112.2
Draper Esprit	510.0	606.5	666	79	0.91	560.0
HgCapital	235.0	958.6	963	100	1.00	236.0
IP Group	68.0	722.4	1,172	71	0.62	110.6
Mercia Asset Management	20.0	88.0	135	33	0.65	30.6
Oakley Capital	200.0	391.2	686	160	0.57	345.0
Source: Refinitiv data; Edison Investment Research. Note: Priced at 8 June 2020.						

Exhibit 4: Financial summary

	\$'000	2015	2016	2017	2018	2019
Year end 31 December		IFRS	IFRS	IFRS	IFRS	IFRS
INCOME STATEMENT						
Revenue		3,300	2,664	5,001	5,561	2,692
Cost of Sales		(3,925)	(5,563)	(5,242)	(2,827)	(1,433)
Gross Profit		(625)	(2,899)	(241)	2,734	1,259
Normalised operating profit		(89,372)	(103,925)	(94,542)	(83,583)	(49,997)
Amortisation of acquired intangibles		0	0	0	0	0
Exceptionals		(309)	(1,365)	(2,363)	(545)	(671)
Share-based payments		(7,041)	(8,385)	(7,562)	(7,413)	1,465
Reported operating profit		(96,722)	(113,675)	(104,467)	(91,541)	(49,203)
Net Interest		670	2,318	305	1,313	741
Joint ventures & associates (post tax)		0	0	0	(3,658)	(28,850)
Fair value changes		(1,937)	(17,585)	(6,953)	139,240	127,566
Profit Before Tax (norm)		(90,639)	(119,192)	(101,190)	53,312	49,460
Profit Before Tax (reported)		(97,989)	(128,942)	(111,115)	45,354	50,254
Reported tax		0	0	0	0	0
Profit After Tax (norm)		(90,639)	(119,192)	(101,190)	53,312	49,460
Profit After Tax (reported)		(97,989)	(128,942)	(111,115)	45,354	50,254
Minority interests		20,192	32,609	35,337	(7,999)	1,081
Discontinued operations		0	0	0	0	0
Net income (normalised)		(70,447)	(86,583)	(65,853)	45,313	50,541
Net income (reported)		(77,797)	(96,333)	(75,778)	37,355	51,335
Basic average number of shares outstanding (m)		215	217	236	240	241
EPS - basic normalised (\$)		(0.33)	(0.40)	(0.28)	0.19	0.21
EPS - diluted normalised (\$)		(0.33)	(0.40)	(0.28)	0.19	0.21
EPS - basic reported (\$)		(0.36)	(0.44)	(0.32)	0.16	0.21
Dividend (\$)		0.00	0.00	0.00	0.00	0.00
Revenue growth (%)		(57.2)	(19.3)	87.7	11.2	(51.6)
Gross Margin (%)		-18.9	-108.8	-4.8	49.2	46.8
Normalised Operating Margin		N/A	N/A	N/A	N/A	N/A
BALANCE SHEET						
Fixed Assets		92,784	38,232	28,369	83,739	72,695
Intangible Assets		4,384	2,762	1,074	1,221	197
Tangible Assets		34,173	31,882	26,627	5,997	1,485
Right of use assets		0	0	0	0	1,016
Investments & other		54,227	3,588	668	76,521	69,997
Current Assets		158,427	232,007	184,792	107,034	97,854
Stocks		1,511	2,551	0	0	0
Debtors		7,342	5,900	15,642	6,400	5,702
Cash & cash equivalents		105,555	209,151	158,075	100,234	90,571
Cash at parent*		N/A	136,700	84,200	50,600	84,100
Other		44,019	14,405	11,075	400	1,581
Current Liabilities		(108,974)	(155,402)	(200,202)	(69,557)	(13,159)
Creditors		(14,268)	(13,941)	(14,276)	(13,030)	(4,685)
Tax and social security		(395)	(458)	(4,296)	(2,333)	(3,457)
Short term borrowings		(228)	(115)	0	0	0
Subsidiary preferred shares		(94,083)	(140,888)	(181,630)	(54,194)	(5,017)
Long Term Liabilities		(863)	(720)	(867)	(436)	(4,819)
Long term borrowings		(112)	0	0	0	0
Lease liabilities		0	0	0	0	(2,854)
Other long-term liabilities		(751)	(720)	(867)	(436)	(1,965)
Net Assets		141,374	114,117	12,092	120,780	152,571
Minority interests		10,631	20,797	59,241	(18,484)	(115)
Shareholders' equity		152,005	134,914	71,333	102,296	152,456
CASH FLOW						
Op Cash Flow before WC and tax		(85,286)	(97,290)	(88,440)	(77,525)	(47,173)
Working capital		2,652	468	(2,477)	6,033	506
Exceptional & other		0	0	0	(1,261)	267
Tax		0	0	0	0	0
Net operating cash flow		(82,634)	(96,822)	(90,917)	(72,753)	(46,400)
Capex		(23,213)	(4,087)	(1,522)	(9,110)	(3,675)
Acquisitions/disposals		(51,786)	74,816	5,853	(18,884)	25,180
Net interest		716	1,602	138	1,313	741
Payment of lease liability		0	0	0	0	(1,540)
Equity financing		2,443	79,319	1,595	1,594	(10,069)
Dividends		0	0	0	0	0
Other		36,165	48,993	33,892	39,438	25,292
Net Cash Flow		(118,309)	103,821	(50,961)	(58,402)	(10,471)
Opening net debt/(cash)		(223,524)	(105,215)	(209,036)	(158,075)	(100,234)
FX		0	0	0	561	808
Other non-cash movements		0	0	0	0	0
Closing net debt/(cash)		(105,215)	(209,036)	(158,075)	(100,234)	(90,571)

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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