

Strong Q3 for Nutrition and Genetics

10 September 2021

Benchmark Holdings' recent Q3 (March-June) results showed strong revenue and profit growth in its Nutrition and Genetics divisions, driven by a recovery in the end-markets for salmon and shrimp from the lockdown-affected levels of the past year. Attention is, however, largely focussed on the new Ectosan[®]Vet sea lice treatment, which saw its commercial launch just after the period end in August. We have revised our financial model to reflect a more conservative trajectory for the new business based on current information and expectations. This was offset by other changes so the net effect on fair value was negligible and remains at £550m or 82p/share.

- Q3 results:** Nutrition revenues rose by 15% driven by Artemia (+21%) and diets (+27%), while genetics revenues increased by 21%, with 5% growth in the important salmon eggs segment. Underlying profit contribution (AEBITDA) was up strongly in nutrition (+65%) as well as genetics, excluding fair value adjustments in biological assets (+37%). Group sales and AEBITDA were up 15% at £28.4m and by 110% at £4.4m respectively.
- Ectosan[®]Vet launch in August:** Benchmark management remains outwardly confident about Ectosan[®]Vet/CleanTreat prospects following the launch in August. The first vessel is fully booked out and a second vessel is due to come on stream imminently. The new business is, however, likely only to make a modest contribution in the fourth quarter and may face challenges longer term with a more restricted label and possible caution on the part of customers while the Maximum Residue Limit (MRL) is under review by the EU Commission.
- EU issues remain a concern:** The EU Commission has yet to respond to the European Parliament's request of 10 June to remove or modify the MRL on imidacloprid which, if it were to occur, could have significant negative consequences for the Ectosan[®]Vet business. Any such a change would be highly controversial, however, as the MRL was arrived at through a thorough scientific review process by EU bodies and has been adopted into law in EU member states (as well as EEA members such as Norway). It is entirely possible (and probably likely) that the Commission will take no action at all. Nonetheless, the situation represents an uncertainty whilst the timing and outcome of any resolution remains difficult to predict.
- Financial forecasts:** We have updated our model based on the reported Q3 figures and assumed a slightly more conservative forecast of the ramp up of the Ectosan[®]Vet/CleanTreat business over time. New figures shown in the table below (prior forecasts for sales and AEBITDA are shown in parentheses).
- Valuation:** Our model update has, however, had no impact on the fair value of Benchmark, which remains at **82p/share**. A bull and bear case described later could add/subtract 15-25% to this figure in our view.

Company Data

EPIC	BMK
Price (last close)	60p
52 weeks High/Low	68p/40p
Market cap	£405m
Net debt (LBSD)	£76.1m
ED Fair value/share	82p
Sector	Pharma & Biotech

Share Price, p



Source: ADVFN

Description

Benchmark Holdings is a UK-headquartered company that provides advanced genetics, health and nutrition products to the global aquaculture industry. These products are designed to help customers manage productivity and animal health/welfare, while reducing environmental impact.

Benchmark has market leadership positions in the supply of salmon eggs and in live feed (Artemia) used in shrimp farming.

Summary forecasts

y/e 30 Sept, £m	FY20	FY21e	FY22e	FY23e
Sales	105.6	115.6 (115.0)	138.5 (151.7)	158.7 (196.5)
AEBITDA*	(14.5)	13.0 (13.5)	26.9 (37.5)	37.3 (52.3)
Net cash/(debt)	-37.6	-93.9	-117.7	-127.7
EV/Sales	4.1	3.5	3.1	2.9

Source: Company historic data/Equity Development forecasts * Adjusted earnings before interest, tax, depreciation, amortisation, exceptional items, and acquisition related expenditure

Robin Davison (Analyst)

0207 065 2690
robin@equitydevelopment.co.uk

Hannah Crowe

0207 065 2692
hannah@equitydevelopment.co.uk

Investment thesis

Benchmark offers investors exposure indirectly to an important sector of the economy that provides a sustainable source of protein (fish and crustaceans) for human consumption.

The group has two businesses with global leadership positions - salmon eggs and live feed (Artemia) for shrimp farming –and is developing a new business that provides an environmentally-responsible solution to eliminate sea lice in salmon farming. Farmed fish/crustaceans have been growing their share of total protein for human consumption driven by favourable health and economic trends. Farmed fish have a higher feed conversion rate and lower environmental impact than other major protein sources for human consumption (beef, pork, poultry, dairy etc). Benchmark aspires to operate to high ESG standards and thus it may be a choice for this type of investor. We illustrate three investment cases:

- **Base case:** Benchmark's Genetics and Nutrition businesses recover to pre-Covid levels and grow in line with the markets, while the new business ventures (tilapia, SPR shrimp etc) develop in accordance with business plans. Ectosan/CleanTreat adoption is consistent with currently articulated goals with no new regulatory impediments.
- **Bull case:** Benchmark's key salmon egg/Artemia businesses gain share and increase profitability through operating leverage, and new business ventures are successful. An effective public engagement campaign builds support for use of Ectosan/CleanTreat, resulting in faster adoption and entry into new markets. Under this scenario, Benchmark could become attractive as M&A target.
- **Bear case:** Profitability in the salmon egg, diets or Artemia businesses stagnate or deteriorate for competitive or other reasons and/or new business ventures struggle to achieve projections. Ectosan[®]Vet faces regulatory impediments and/or anti-fish farming activists' arguments affect consumers, such that adoption is slowed or not possible at all.

Sensitivities/risks

Key upside/downside risks are illustrated in bull and bear cases above. We highlight the principal risk facing the company currently with potentially large downside to the investment case is if the European Commission were to change or even remove the MRL for imidacloprid in the EU. This could effectively mean Ectosan[®]Vet could not be used in Norway. Other risks are operational (e.g. currency exposure) and financial (ability to refinance the NOK855m/~\$95m senior bond, which matures in June 2023) are considered by Equity Development to be modest.

Valuation

Our base case (see above) suggests a fair value of Benchmark is £550m or 82p/share, based on a WACC of 11% and long-term growth rate of 2.5%. The bull case illustrated above could add 15-25% to this figure, in our view, whereas the bear case would be a similar proportion below this. Our model suggests Benchmark's debt peaks in 2023 and thereafter falls, which should have a positive geared effect on valuation.

Financials

Benchmark is emerging from an investment/restructuring phase but has yet to reach sustainable profitability, which our model suggests will occur in FY2024. Our model suggests debt (excluding leases, mostly associated with CleanTreat vessels) will peak in FY2023 at £90m and is within the capital available to the company. We expect the company to be able to refinance its bond in 2023 and may choose to do so earlier if finance can be obtained at a lower cost.

Q3 results update

Benchmark Holdings' recent Q3 (March-June) results showed strong revenue and underlying profit growth in its Nutrition and Genetics divisions. Health also showed revenue growth although remains at a loss, after a heavy investment phase. Nutrition revenues were up by 15% driven by Artemia (+21%) and diets (+27%), while genetics revenues increased by 21%, with 5% growth in the important salmon eggs segment. Growth rates in these two divisions were flattered by comparison lockdown depressed figures last year, although at the same time there was a headwind from foreign exchange movements, especially in Nutrition.

Underlying profit contribution (adjusted EBITDA or AEBITDA) was up strongly in Nutrition (+65%) and Genetics (+83%), although much of the latter reflected fair value adjustments to biological assets. Group sales and AEBITDA were up 15% at £28.4m and by 110% at £4.4m respectively. We have updated our financial model, Net debt at 30 June was £76.1m or £52.7m excluding lease liabilities.

Exhibit 1: Q3 Results summary

	Q3 2021	% change (CER)
Revenue	£m	
Advanced Nutrition	18.4	15% (+29%)
<i>of which Artemia</i>	7.9	21%
... Diets	8.5	27%
Health	2.0	56%
Genetics	8.7	21% (+18%)
<i>of which salmon eggs</i>	5.9	5%
Health	1.2	20% (+20%)
Group Revenue	28.4	15% (+25%)
AEBITDA		
Advanced Nutrition	3.9	39% (+57%)
Genetics	2.2	83% (+75%)
<i>of which FV of bio assets</i>	1.90	-10% (-14%)
<i>excl. FV adjustment</i>	0.3	N/M
Health	-1.2	8% (+8%)
Group AEBITDA	4.4	110% (+123%)
Group AEBITDA (exc. FV adjustment)	4.1	37% (47%)

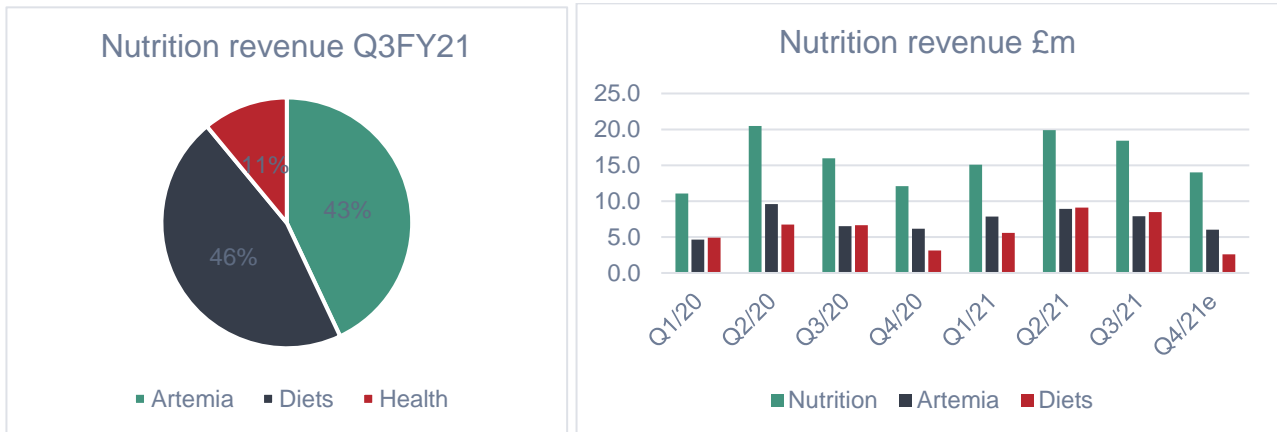
Notes: % change is compared with restated 2020 figures adjusted to reflect current businesses, CER compared with restated figures at constant exchange rates. % change for Artemia, Diets and salmon eggs businesses calculated by Equity Development.

Exhibit 2: Updated divisional P&L forecasts

	FY 2021e	FY2022e	FY 2023e
Revenue			
Advanced Nutrition	67.4	74.2	81.6
Genetics	43.8	45.6	47.9
Health	4.3	30.0	45.2
Adjusted EBITDA			
Advanced Nutrition	13.1	15.6	17.9
Genetics	11.6	11.9	14.4
Health	-0.3	5.9	12.4

Source: Equity Development forecasts. Note Divisional AEBITDA figures do not exactly sum to Group forecast figures, because of intra-group sales and eliminations.

Exhibit 3: Advanced Nutrition profile

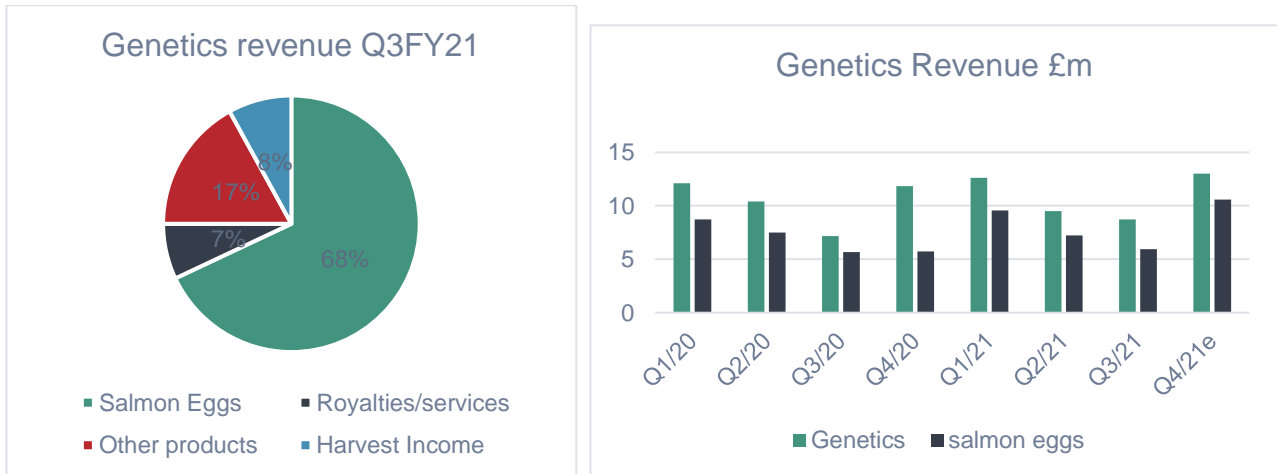


Highlights

- Salmon performed well and maintained a strong market position in the northern hemisphere. Salmon market was positive with price recovery and favourable demand/supply dynamic.
- Market share regained in Artemia with a drop in price.
- Shrimp market recovering with potential to bounce back to pre-Covid levels, although conditions in some shrimp producing countries (e.g. India) remain difficult.
- Stronger market position in diets and health.
- Recovery in seabass/seabream markets.
- Asia performed strongly but Americas remain challenging because of pandemic-related/logistical difficulties.

Source: Historic figures and Equity Development forecasts.

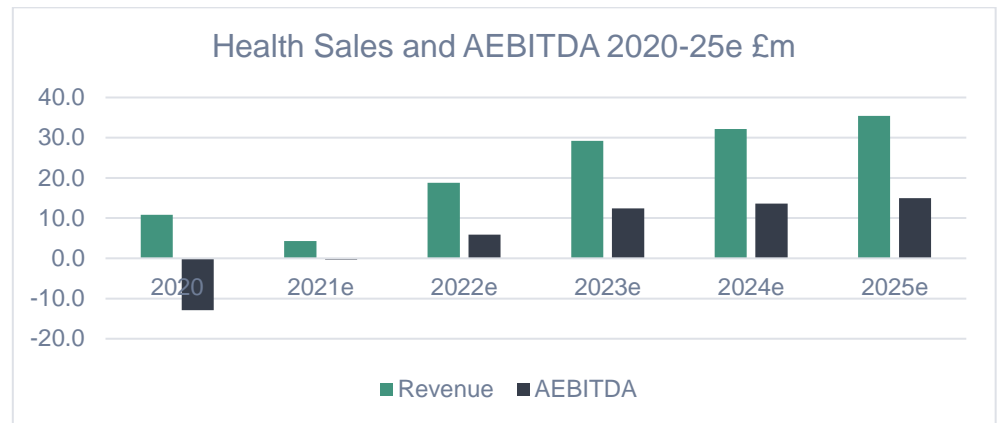
Exhibit 4: Genetics profile



Highlights

- Growth in salmon egg, despite strong Q3 2020 sales from spike in Scotland.
- Current capacity in salmon eggs from facilities in Norway and Iceland sold out for the year. Expansion of Salten, Norway facility from 100m to 150m proceeding according to plan.
- New contracts won for future delivery for land-based salmon. Expansion of the incubation facility in Iceland progressing.
- First sales of locally produced salmon eggs in Chile.
- Test marketing of the SPR shrimp continues. Expansion of Fellsmere, Florida facility progressing to plan. Business plan envisage a phased entry for SPR shrimp into the Asian markets.
- Tilapia business remains focussed on achieving profitability and optimising scale for sustainable profitability.
- Expansion of salmon incubation capacity in Iceland progressing.

Source: Historic figures and Equity Development forecasts. Note RHS chart shows Total Genetics and salmon eggs.

Exhibit 5: Health segment sales and EBITDA forecast

Highlights

- First CleanTreat vessel is fully booked out, the second vessel is coming on stream imminently.
- Two large customers were signed up at launch.
- Norwegian market for EctosanVet/Cleantreat is forecast by Benchmark at £50m at peak with EBITDA margins of 25-30% post-launch, rising to 60% at full utilisation.
- Marketing authorisation (MA) covers 85% of Norwegian salmon farms. The restrictions (which are understood to relate to the location and size of the customer only) are expected to be addressed over time. Any studies required can be conducted as part of the commercial roll-out.

Source: Historic figures and Equity Development forecasts

Exhibit 6: Group quarterly/annual sales and EBITDA forecast


Source: Historic figures and Equity Development forecasts

The following tables show our financial model outputs from 2021-23 (estimates shown above beyond 2023 should be considered illustrative).

Exhibit 7: Income Statement

y/e 30 Sept, £'000s	2020	2021E	2022E	2023E
Revenues	105,565	115,545	138,489	158,684
Cost of goods sold	-50,603	-56,270	-63,748	-71,792
Gross Profit	54,962	59,275	74,741	86,892
Admin Expenses	-33,337	-37,425	-40,247	-41,150
Share based payments	-1,669	-1,376	-1,376	-1,376
R&D	-7,282	-7,700	-6,400	-7,375
EBITDA	12,379	12,220	26,949	37,252
Adjusted EBITDA	14,493	12,979	26,949	37,252
Operating Loss	-10,874	-10,659	4,748	14,733
Depreciation	-6,640	-6,733	-7,792	-7,792
Amortisation	-16,613	-16,145	-14,409	-14,727
Interest income	-11,697	95	-8,051	-8,302
Loss before tax	-22,571	-10,564	-3,302	6,431
Adj. PBT	9,928	21,945	66,176	78,326
Current tax income	-204	-70	-512	-997
Net loss from discontinued operations	-9,174	0	0	0
Adj. net income	-4,048	6,270	10,594	20,161
Net loss continuing operations	-31,949	-10,634	-3,814	5,434
EPS (p)	-5.3	-1.6	-0.6	0.8

Source: Company historic figures/Equity Development estimates.

Exhibit 8: Balance Sheet

y/e 30 Sept, £'000s	2020	2021E	2022E	2023E
Current assets	145,750	118,266	112,521	119,826
Cash/cash equivalents	71,605	34,303	17,556	14,464
Accounts receivable	39,371	43,093	51,650	59,182
Inventories	18,926	20,260	22,705	25,570
Biological assets	15,848	20,610	20,610	20,610
Non-current assets	343,285	342,074	341,283	335,912
Property, plant & equipment	65,601	75,920	85,179	90,176
right of use assets	10,347	25,306	25,306	25,306
Intangible assets	247,003	220,433	210,383	200,015
Equity investees	3,690	3,281	3,281	3,281
Other non-current assets	16,644	17,134	17,134	17,134
Current liabilities	-55,375	-56,614	-63,127	-68,859
Short-term debt	-2,856	-10,491	-10,491	-10,491
Lease liabilities	-2,483	-8,886	-8,886	-8,886
Accounts payable	-45,692	-32,798	-39,311	-45,043
Other current liabilities	-4,344	-4,439	-4,439	-4,439
Non-current liabilities	-138,220	-139,214	-146,214	-153,214
Long-term debt	-95,863	-94,278	-94,278	-94,278
Lease liabilities	-7,956	-14,551	-21,551	-28,551
Other non-current liabilities	-34,401	-30,385	-30,385	-30,385
Equity	295,440	252,010	244,464	233,665

Source: Company historic figures/Equity Development estimates

Exhibit 9: Cashflow statement

y/e 30 Sept, £'000s	2020	2021E	2022E	2023E
Operating cash flow	-4,056	6,792	11,993	21,385
Profit before tax	-31,949	-10,659	4,748	14,733
Tax credit	314	-77	0	0
Non-cash adjustments inc impairment	14,496	21,314	20,297	20,615
Change in working capital	5,475	-49	-4,489	-4,664
Interest paid	9,695	-1,650	-8,051	-8,302
Taxes paid	-2,087	-2,086	-512	-997
Investing cash flow	30,376	-28,159	-21,740	-17,477
CAPEX on tangible assets	-5,851	-17,052	-17,052	-12,789
CAPEX on intangible assets/capitalised R&D	-5,563	-4,359	-4,359	-4,359
Acquisitions/disposals	42,201	-734	0	0
Other investing cash flows	-411	-6,014	-329	-329
Financing cash flow	30,133	-11,786	-7,000	-7,000
Proceeds from equity	41,666	689	0	0
Increase in loans	-1,754	-2,696	0	0
Other financing cash flow, lease liabilities	-9,779	-9,779	-7,000	-7,000
Net increase in cash	56,453	-33,075	-16,747	-3,092
Exchange rate effects	-899	-4,227	0	0
Cash at start of year	16,051	71,605	34,303	17,556
Cash at end of year	71,605	34,303	17,556	14,464
Net cash/(debt) at end of year excl. lease liabilities	-27,114	-70,466	-87,213	-90,305
Net cash/(debt) at end of year	-37,553	-93,903	-117,650	-127,742

Source: Company historic figures/Equity Development estimates



Contacts

Hannah Crowe

Direct: 0207 065 2692

Tel: 0207 065 2690

hannah@equitydevelopment.co.uk

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More information is available on our website www.equitydevelopment.co.uk

Equity Development, 15 Eldon Street, London, EC2M 7LD

Contact: info@equitydevelopment.co.uk | 020 7065 2690