

Focusing on core areas and liquidity

17 January 2020

While Benchmark generated good FY19 performance in its Genetics and Animal Health divisions, previously flagged challenging conditions in Advanced Nutrition contributed to the acceleration of a restructuring process. This includes a vigorous review of non-core assets with a view to their disposal or closure, helping ensure the Group's ongoing financial liquidity. Factoring in disposals and efficiencies, our new forecasts indicate liquidity within its NOK bond-lending covenant terms, supporting our 2020-22 sales CAGR estimate of 12%. Sales will be driven by launches of BMK's innovative sea lice treatment BMK08, shrimp genetics products and sustained underlying performance.

BMK has identified as non-core the Knowledge Services and Veterinary Services (part of Animal Health) divisions, now set for disposal to generate cash for the Group (FY19 contribution from discontinued operations: £21m of revenue and £2m of EBITDA). It is also re-prioritising its R&D expenditure and targets increased efficiencies at its in-house trial facilities. Challenging conditions in the **Advanced Nutrition** division related to a widespread downturn in production in shrimp markets, compounded by pricing pressures in Artemia as well as economic factors affecting Mediterranean farmed-fish markets. These factors contributed to a 10% fall in FY19 revenues for the division to £77m. Weakness is set to continue into 2020. Favourable conditions in the salmon markets are expected to continue.

Animal Health sales, including discontinued non-core Veterinary services, rose 5% to £17m from £16.2m in FY18. Successful outcomes from commercial scale field trials of BMK's next generation sea lice treatment, BMK08, which showed 99% efficacy and a high sustainability score, support the use of the product along with its CleanTreat® proprietary technology. This will help alleviate the high cost of sea lice to the industry while minimising environmental contamination, a key differentiator for the product. Launch of BMK08, which has peak sales estimate of £45m, is planned for H12021 CY subject to regulatory approval.

Genetics sales grew 11% from £35m to £39m as the scaling up of production for the Salten land-based salmon ova facility kicked in, providing an uplift in margins and production volumes. BMK is making good progress towards launching its disease-resistant SPR shrimp targeted at the Asian markets (peak sales estimate; £40m). Reviewing forecasts, stripping out discontinued operations and taking a conservative view on prospects, our net debt forecasts still indicate no additional recourse to funding and are well within the liquidity levels under the NOK Bond covenant. Moving past current challenges, prospects are underpinned by the significance of sustainability to the industry and the disruptive potential of the Company's new products.

Summary Financials

y/e 30 Sept, £m	FY18	FY19	FY20e	FY21e	FY22e
Sales	131.6	127.3	140.9	155.0	180.1
Adjusted EBITDA*	19.1	12.1	10.2	17.0	29.4
Net cash/(debt)	-55.7	-87.1	-85.7	-98.9	-99.4

Source: company historic figures/ED forecasts/ Earnings before interest, tax, depreciation, amortisation, exceptional items and acquisition related expenditure*

Company Data

EPIC	BMK
Price	45p
52 week Hi/Lo	58p / 39.5p
Market cap	£254m

Share Price, p



Source: ADVFN

Description

Benchmark Holdings (BMK) helps deliver improved healthcare products and services to the Aquaculture industry.

Rising demand from clients for its products and services to manage sustainability practice in worldwide production and supply chains underlines BMK's opportunity for significant organic and external growth.

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FY19 Group Financials summary

After the Company experienced very challenging trading conditions in Advanced Nutrition markets, it is set to make transformational changes to the business to ensure ongoing liquidity, improve efficiency and focus on its core products. Notably these include the near term launch of potentially transformational products, which are core to the industry challenges, meet sustainability goals and improve production yield. BMK restructured its management team with new CFO Septima Maguire (ex-Dechra Pharmaceuticals) now fully transitioned into the role and pharma industry veteran and Executive Chair Peter George engaged in discussions to appoint a new CEO.

BMK's Genetics and Health divisions both grew revenues, yet a 10% fall in Advanced Nutrition revenues, which represents over 50% of Group sales at £76.8m in FY19, led total revenues including discontinued operations to fall 2% from £151.5m to £148.7m in FY18 and EBITDA from £17m to £13.7m.

Stripping out FY19 discontinued revenues of £21m and EBITDA of £2m from non-core Knowledge Services and Veterinary Services (part of Animal Health), FY19 Continuing Operations generated £127.3m of revenue, down c 3% from £131.6m in FY18 and EBITDA fell from £19.1m to £12.1m. These divisions have been earmarked for disposal to generate cost savings and liquidity for the Company with late-stage discussions ongoing in this respect. Gross margin remained steady at 52% as BMK broadly maintained pricing in the face of challenging markets.

Operating costs rose 10% from £30.7m to £40m, while R&D spend increased 7% from £19.2m to £20.5m, including both the expensed element to cover pipeline products, notably in Genetics and Advanced Nutrition, and capitalised expenditure for products close to launch such as BMK08 + CleanTreat®. These costs were partly offset by one-off income FY19 of £1.8m derived from R&D credits and receipts from IP infringement cases.

After a £44.8m impairment related to INVE (Advanced Nutrition) as a result of the market outlook in shrimp as well as an impairment related to discontinued assets, FY19 post tax loss from continuing operations was £73.3m, vs a profit of £0.5m in FY18.

Group net debt at the end of September 2019 stood at £87.1m, including £16.1m of cash and £103.2m of debt, composed principally of the Group's NOK 850m bond (£75.9m). Total liquidity, measured as cash and the Group's undrawn \$15m Revolving Credit Facility, stood at £28.2m, well above the £10m minimum set out under the covenants of the NOK bond.

FY19 divisional trading summary

Genetics sales grew 11% from £35m to £39.7m as the Salten land-based salmon ova facility production scale-up kicked in, providing an uplift in pricing and production volumes of the company's genetically rich salmon ova, enabling revenues to grow ahead of the estimated market growth rate of 6%.

BMK made good progress towards launching its specific pathogen-resistant SPR shrimp (company peak sales estimate of £40m) targeted at the Asian markets, establishing a production facility in Florida as well as a JV in Thailand for local multiplication and distribution in preparation for launch into the key South East Asian regions from 2020.

The company dissolved its Chilean salmon egg JV with AquaChile and replaced this with its fully owned salmon egg hatchery at Ensenada from which it will establish local production.

All funds invested into the JV have now been received, including a final £6.9m instalment received post year-end, and are being reinvested into Ensenada. Both gross margin and adjusted EBITDA margin grew year-on-year, up from 58.6% to 63.8% and from 22% to 25% from £7.9m to £10.1m in FY19.

In the **Advanced Nutrition** segment, the widespread downturn in shrimp production impacted demand for the company's products, compounded by pricing pressures in Artemia markets. Conditions in Mediterranean seabass and bream markets were also challenging affected by economic factors as well as over-supply, leading to a knock-on effect on pricing and a contraction in production. Specialist diets and health products (probiotics) remained relatively resilient vs live feed markets and the Company will expand sales channels to facilitate further growth of these high margin products. There was a 10% fall in FY19 revenues for the division to £76.8m from £85.7m in FY18 while adjusted EBITDA fell from £21.6 to £15.4m. Trading conditions in Artemia in particular, which accounts for over 50% of division's sales, remain difficult with prospects of a partial recovery in 2020 driven by salmon markets.

Animal Health sales, including discontinued non-core Veterinary services, increased 10% to £17.7m from £16.2m in FY18, driven by demand for the company's sea lice treatment Salmosan. On a continuing basis, revenues increased 14% from £10.7m to £12.2m. Successful outcomes from field trials of BMK's next generation sea lice treatment BMK08 included 99% efficacy and a high sustainability score, clearly a key factor in positioning the product to meet acute unmet need in global salmon aquaculture markets. The estimated annual loss is of tens of thousands of tonnes of salmon costing the industry over \$500m per annum.

Launch of BMK08 is anticipated in H12021 CY subject to regulatory approval and the medicinal treatment will be used in conjunction with BMK's proprietary CleanTreat® technology. The Company is evaluating the optimal strategy for commercialising and scaling up CleanTreat® ahead of launch given the capital investment required in order to maximise the commercial prospects of BMK08. The potentially ground-breaking treatment has estimated peak sales of £45m and has been extensively and successfully used to treat over 35,000 tonnes of salmon, creating significant interest from industry ahead of the anticipated launch. CleanTreat® was winner of the 2019 Aquaculture Innovation Award and its positive welfare and sustainability benefits are key factors supporting commercial prospects.

BMK reviewed and reprioritised its health pipeline assets during FY19 to focus on its core aquaculture vaccines. The Company is in discussions to out-license its companion animal products. As a feature of its ongoing cost control it initiated streamlining of its R&D spend and has identified a series of efficiencies within its clinical trial facilities.

There have been some delays in initiating animal health trials of certain vaccines which will impact on revenue forecasts launch estimates for these products.

Forecasts: restructuring to provide liquidity

We have reviewed our FY20/21 forecasts which are expressed on a continuing basis, taking a conservative approach and assuming that BMK disposes of non-core businesses in FY20 as per its restructuring plan. We have therefore stripped out £21.4m of FY19 discontinued revenues including £15.1m of Knowledge Services and £6.3m of Animal Health revenues.

Divisional forecast changes			
y/e 30 Sept, £m		FY20	FY21
<u>Advanced Nutrition</u>			
Old	Rev	84.3	100.4
	Adj EBITDA	22.4	28.4
New	Rev	85.0	88.0
Change		1%	-12%
	Adj EBITDA	14.3	15.8
Change		-36%	-44%
<u>Genetics</u>			
Old	Rev	46.4	50.6
	Adj EBITDA	10.9	13.6
New	Rev	44.1	48.5
Change		-5%	-4%
	Adj EBITDA	10.6	10.7
Change		-2.7%	-21%
<u>Animal Health</u>			
Old*	Rev	29.1	43.3
	Adj EBITDA	-9.8	0.9
New**	Rev	13.7	20.4
Change		-53%	-53%
	Adj EBITDA	-10.8	-7.9
Change		-11%	-965%

Source: Equity Development / *includes discontinued revenues / **excludes discontinued revenues

Other key changes include lowering our Advanced Nutrition division FY21 revenue forecast based on the sustained weakness in shrimp markets from £100m to £88m. We have amended our FY20 and FY21 gross margin estimates from 53% down to 48% and 49% respectively, due to sustained pricing pressure in shrimp, as well as higher Opex investment in technical support for new diets which leads to 36% and 44% drop in our adjusted EBITDA forecasts for the division.

In Animal Health we take a more cautious view on FY20/21 revenues. This is due to BMK08 launch timing of H12021CY as well as delayed launch of vaccines and lower revenue from clinical trials of BMK08. We also strip out discontinued revenues.

In Genetics we factor in a slightly slower ramp-up in sales, with the key driver being continuing expansion capacity at Salten and the Ensenada facilities. The SPR shrimp roll-out is likely to be gradual and on a country-by-country basis. Therefore, we build estimates over a period of 6-to-8 years given the need for education and acceptance.

While pricing remains resilient and costs contained, lower revenues lead to a 2.7% and 21% drop in FY20 and FY21 for our adjusted EBITDA margin estimates.

At a Group level, the summary of changes is shown as follows and for clarity we add in the total and continuing figures for FY19 to provide a like-for-like comparison.

Summary of Group forecast changes			
y/e 30 Sept, £m	FY19	FY20e	FY21e
Old			
Sales total	148.7	177.3	213.4
Total Opex (before exceptional items)		-65.8	-70.1
Adjusted EBITDA	13.7	22.6	42.7
Net cash/(debt)		-93.0	-80.9
New			
Sales continuing	127.3	140.9	155.0
Total Opex (before exceptional items)		-59.9	-62.9
Adjusted EBITDA	12.1	10.2	17.0
Net cash/(debt)		-85.7	-98.9
Change			
Sales		-20.5%	-27.4%
Adjusted EBITDA		-54.6%	-60.2%
Net cash/(debt)		8%	-22%

Source: Equity Development forecasts/company historic figures

Our expensed operating cost estimates are significantly lower after the amendments shown. In aggregate, assuming disposals are executed (£20m of estimated proceeds), our new group net debt forecast is 8% lower at £85.7m at the end of September 2020, rising to £98.9m in FY21.

Group forecasts

We expect a significant scale-up in revenue from FY22 based on the rapid roll out of CleanTreat® BMK08, with a material contribution in FY22 after initial launch in FY21, assuming a timely marketing approval, leading to a revenue increase of 16% from £155m in FY21 to £180.1m (including ED Animal Health FY22 revenue estimate of £30.6m).

BMK is set to maintain Advanced Nutrition products as strategic and commercially significant, central to the diversification and cross-selling prospects of its other divisions, although aiming to diversify its portfolio into higher margin diets and probiotics and to provide increasing presence in the grow-out segment to complement its early stage segment. Included below is a summary of our divisional forecasts including FY22.

Summary of divisional forecasts			
y/e 30 Sept, £m	FY20e	FY21e	FY22e
<u>Advanced Nutrition</u>			
Revenue	85.0	88.0	95.0
Growth	11%	4%	8%
Gross Profit	40.7	43.1	46.6
Gross Margin	48%	49%	49%
Adjusted EBITDA	14.3	15.8	17.0
Adjusted EBITDA Margin	17%	18%	18%
<u>Genetics</u>			
Revenue	44.1	48.5	54.3
Growth	11%	10%	12%
Gross Profit	26.4	29.3	32.6
Gross Margin	60%	60%	60%
Adjusted EBITDA	10.6	10.7	11.5
Adjusted EBITDA Margin	24%	22%	21%
<u>Animal Health</u>			
Revenue	13.7	20.4	30.6
Growth	12%	49%	50%
Gross Profit	3.3	7.8	16.8
Gross Margin	24%	38%	55%
Adjusted EBITDA	-10.8	-7.9	-1.8
Adjusted EBITDA Margin	-79%	-39%	-6%

Source: Equity Development

At Group level these new forecasts translate as follows, starting with the income statement.

Income statement					
y/e 30 Sept, £000s	2018*	2019*	2020e	2021e	2022e
Revenues	131,643	127,343	140,900	155,023	180,091
Cost of goods sold	-63,150	-61,348	-70,788	-75,131	-83,967
Gross Profit	68,493	65,995	70,112	79,892	96,124
Admin Expenses	-37,012	-40,700	-46,921	-47,474	-51,289
Other expenses/income	0	0	0	0	0
Share based payments	-1,511	-1,181	-1,216	-1,280	-1,344
R&D	-12,040	-12,830	-12,957	-15,402	-15,427
Share of profit / loss equity-accounted investees - net	-362	-414	0	0	0
Exceptional items	0	0	-500	0	0
Acquisition related costs	-1,239	-581	0	0	0
EBITDA	17,840	11,470	9,734	17,017	29,408
Adjusted EBITDA	19,079	12,051	10,234	17,017	29,408
Operating Loss	-3,831	-61,250	-12,866	-6,083	6,808
Depreciation	-4,869	-8,466	-6,102	-6,237	-6,102
Amortisation	-16,802	-64,254	-16,498	-16,863	-16,498
Interest income	-4,595	-12,054	-6,125	-6,050	-6,221
Loss before tax	-8,426	-73,304	-18,991	-12,133	587
Current tax income	8,906	13	-4,000	-4,000	-4,000
Net loss discontinued operations	-4,869	-9,789	0	0	0
Net loss continuing operations	-4,389	-83,080	-22,991	-16,133	-3,413
EPS (p)	- 0.94	- 5.03	-4.12	- 2.89	- 0.61
Average no. of shares	532	558	559	559	559
Gross margin	52%	52%	50%	52%	53%
EBITDA margin	14%	9%	7%	11%	16%
Adjusted EBITDA margin	14%	9%	7%	11%	16%

Source: Company historical figures/Equity Development forecasts/*historical figures are rebased continuing basis

Balance sheet

Working capital is forecast to remain in line with growth as revenues stabilise, unwinding the large increases seen in FY19. Our FY20-22 cash forecasts are £17.5m, £4.3m and £3.8m including disposal proceeds. If, in reality, timing or amount of proceeds differ, BMK has stated its options include reprioritising expenditure or seeking alternative forms of financing.

Balance Sheet summary					
y/e 30 Sept, £000s	2018	2019	2020e	2021e	2022e
Current assets	97,802	122,790	114,598	108,149	115,134
Cash and cash equivalents	24,090	16,051	17,512	4,317	3,752
Assets held for sale	0	15,970	0	0	0
Accounts receivable	41,337	52,136	54,044	59,461	64,142
Inventories	20,483	22,609	25,018	26,347	29,216
Biological & agricultural assets	11,892	16,024	18,024	18,024	18,024
Non-current assets	455,046	380,591	357,391	351,755	346,539
Property, plant & equipment	99,527	88,900	90,798	94,061	97,459
Intangible assets	325,386	275,744	253,146	244,247	235,633
Equity-accounted investees	17,457	3,453	953	953	953
Other non-current assets	12,676	12,494	12,494	12,494	12,494
Current liabilities	-49,277	-52,207	-42,590	-45,357	-49,196
Short-term debt	-898	-3,231	-3,231	-3,231	-3,231
Liabilities re assets held for sale		-10,634			
Accounts payable	-45,680	-35,235	-36,252	-39,019	-42,858
Other current liabilities	-2,699	-3,107	-3,107	-3,107	-3,107
Non-current liabilities	-121,724	-140,708	-140,708	-140,708	-140,708
Long-term debt	-78,868	-99,961	-99,961	-99,961	-99,961
Other non-current liabilities	-42,856	-40,747	-40,747	-40,747	-40,747
Equity	381,847	310,466	288,691	273,839	271,769
Share capital	557	559	559	559	559
Other	381,290	309,907	288,132	273,280	271,210

Source: Company historical figures/Equity Development forecasts

Cash flows

Our CAPEX forecasts are driven by the scale-up of CleanTreat® projected over the next 12 to 18 months. Our new estimates of total R&D FY20-21 including the expensed and capitalised portion are for 15% of revenues falling to 13% in FY22 higher as a proportion of revenue previously 10%/11% but broadly stable in real terms.

With disposal of non-core assets included in our forecasts, we conservatively include a low-end exit value of c. 1x sales of £20m. Therefore, on our forecasts, the Group maintains liquidity and fulfils its NOK bond covenant terms.

Cashflow summary					
y/e 30 Sept, £000s	2018	2019	2020e	2021e	2022e
Operating cash flow	-3,741	-9,211	-2,475	4,269	16,820
Profit before tax	-4,389	-83,080	-12,866	-6,083	6,808
Tax credit	-9,270	111	0	0	0
Non-cash adj./impairment	26,682	89,652	23,816	24,380	23,944
Change in working capital	-13,298	-19,414	-3,301	-3,978	-3,711
Interest paid	2,432	7,773	-6,125	-6,050	-6,221
Taxes paid	-5,898	-4,253	-4,000	-4,000	-4,000
Investing cash flow	-38,515	-15,321	3,936	-17,464	-17,384
CAPEX on tangible assets	-25,072	-7,850	-13,000	-9,500	-9,500
CAPEX on intangible assets/capitalised R&D	-7,581	-7,964	-7,964	-7,964	-7,884
Acquisitions/disposals	233	7,066	26,900	0	0
Other investing cash flows	-6,095	-6,573	-2,000	0	0
Financing cashflow	47,120	15,985	0	0	0
Proceeds from equity	18,498	2	0	0	0
Increase in loans	31,315	21,354	0	0	0
Other financing	-2,693	-5,371	0	0	0
Net increase in cash	4,864	-8,547	1,461	-13,195	-565
Exchange rate	447	508	0	0	0
Cash at start of year	18,779	24,090	16,051	17,512	4,317
Cash at end of year	24,090	16,051	17,512	4,317	3,752
Net cash/(debt) at end of year	-55,676	-87,141	-85,680	-98,875	-99,440

Source: Company historical figures/Equity Development forecasts

Conclusions

Our new DCF valuation of BMK is **£382m or 68 pence per share**, after using an 11% discount rate and 2.5% long-term growth rate. This is down from our previous valuation of £514m following changes to forecasts and rolling forwards. With key product launches in sight, the Group's prospects are underpinned by the growing importance of sustainability and environmental, social and governance (ESG) factors.

With a refreshed management team in place led by the experienced Peter George (Executive Chairman) and Septima Maguire (CFO) plus a new CEO to come, the Group will now focus on monetising its research and product portfolio.



Investor Access

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