

Delivering on strategic and financial targets

26 June 2018

BMK delivered a 9% reported increase in sales in H1'18 despite FX headwinds (up 17% at constant exchange rates) to £75.7m, together with a 91% increase in adjusted EBITDA. This was driven by strong performance in Genetics and Advanced Nutrition and a higher margin product mix in these divisions. The results were accompanied by a confident message that the growth strategy is delivering, with FY18 forecasts on track.

Highlights included strong levels of interest from leading producers in BMK's innovative sea lice combination treatment **Ectosan + Cleantreat**, now undergoing commercial scale field trials in Norway. Progress in Advanced Nutrition came from growing demand for high margin specialist diets and health products in most markets, particularly in India, justifying BMK's diversification strategy.

Genetics revenues rose 11% alongside core salmon ova pricing and volumes, while investment in the Salten land-based facility is on track for a commercial production start in Q3'18 and first delivery in Q1'19. Salten provides capacity needed to meet rising demand due to industry recovery, and to projected demand from the new JV with AquaChile. Field trials of a new specific pathogen resistant (SPR) shrimp were very well received: this endorses BMK's move into new species and offers sales' potential in the huge Asian shrimp market, which has annual production of over \$13bn.

Post period end, BMK entered into an aquaculture breeding and genetics Joint Venture with Empresas AquaChile SA, the world's sixth largest salmon producer. The JV is projected to be immediately earnings enhancing in our forecasts. It is also a sound strategic move that cements BMK's presence in Chile, the second largest global producer of Atlantic salmon after Norway. BMK's £19m June gross equity placing of 34.5m shares at 55 pence per share will be used to fund the JV.

Group revenue was boosted by Advanced Nutrition Division sales which increased by 16% from £37.9m to £44.1m, including a rise in sales of higher margin diets, notably in India. The Genetics Division delivered 11% growth to £21m (H1'17 £18.8m) alongside sustained recovery in salmon markets. Animal Health revenue fell to £4.1m from £7.2m, partly due to the one-off effects of a switch to a direct sales model.

The figures were well received by market and it was encouraging to see Director's share purchases after their release. After raising our forecasts and adding in the JV earnings, then rolling forwards our DCF valuation, our new value increases to **£549m** (from £521m) or **98.5p per share** (including the new placing shares).

Summary forecasts

Y/E end 30 Sept, £m	FY18e	FY19e	FY20e
Sales	162.2	183.9	203.2
Adjusted EBITDA*	16.4	22.4	26.8
Adjusted EPS p**	1.4	1.1	2.1
Net cash/(debt)	-46.6	-56.4	-53.9

Source: ED *Adjusted for exceptional and acquisition costs **EPS pre-exceptional, acquisition costs & amortisation.

Company Data

EPIC	AIM:BMK
Price (last close)	64p
52 week Hi/Lo	80p / 36p
Market cap	£356m
ED value / share	98.5p

Share Price, p



Source: ADVFN

Description

Benchmark (BMK) helps deliver improved healthcare products and services to the Animal Health and 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.

Next news: trading statement estimated September 2018; update on SPR shrimp trials in Asia.

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Advanced Nutrition

Highlights of the period included a growing contribution from higher margin products and BMK delivered on its strategic target of diversifying the product base. This included a notable 40% increase in volume growth of specialist replacement diets, and a 27% volume increase in health product revenues, relative to an 8% jump in core artemia volume. The change in product mix led to a gross profit expansion to 52% from 50%.

Operating costs rose 9% (but fell as a proportion of revenue from 25% to 23%) and overall EBITDA increased from 22% to 26%.

Advanced Nutrition: H1'18 P&L summary

£m	H1'18	H1'17
Revenue	44.1	37.9
COGs	-21.4	-18.7
Gross profit	22.7	19.1
Gross profit %	52%	50%
R&D	-1.2	-1.5
Operating costs	-10.2	-9.4
Adjusted EBITDA	11.3	8.3
Operating profit/(loss)	3.3	-0.1

Source: Company

Genetics

The Division delivered 12% revenue growth, based on volume and price increases for core salmon ova and lumpfish volumes, taking gross profit up to 45% compared to 42% in the previous period. Operating expenses rose 38% along with increased investment in headcount to support ongoing diversification into shrimp and tilapia. The rise was also due to an FX-led credit to operating expenses in the comparative period and to costs associated with full expansion of the Salten salmon ova facility.

Overall, this led to a stable EBITDA margin of 15%.

Genetics: H1'18 P&L summary

£m	H1'18	H1'17
Revenue	21.0	18.8
COGs	-11.5	-11
Gross profit	9.5	7.9
Gross profit %	45%	42%
R&D	-1.7	-1.6
Operating costs	-4.7	-3.4
Adjusted EBITDA	3.1	2.8
Operating profit/(loss)	1.4	3.7

Source: Company

Animal Health

In H1'18 BMK delivered maiden revenues from field trials of Ectosan along with reporting strong indications of interest in the treatment from major producers. Overall, revenues fell 43% from £7.2m to £4.1m, partly because of BMK making the transition to a direct-selling model for its sea lice treatment Salmosan in Chile. While in Norway there was a one-off repurchase of inventory from a distributor in H1'18 due to an overstocking that resulted from lower use of Salmosan due to a focus on mechanical treatments.

BMK anticipates that it will redeploy the inventory in other markets based on a new approach to the use of Salmosan. While underlying sales remained stable, repurchase of inventory from distributors in these markets contributed to margin contraction in this period.

Animal Health: H1'18 P&L summary

£m	H1'18	H1'17
Revenue	4.1	7.2
COGs	-5.4	-5.9
Gross profit	-1.3	1.3
Gross profit %	-30%	20%
R&D	-2.7	-3.4
Operating costs	-3.9	-3.7
Adjusted EBITDA	-7.9	-5.8
Operating profit/(loss)	-9.1	-6.7

Source: Company

Knowledge Services revenues increased from £6.4m to £7.5m at a stable 31% gross margin.

Summary of Financials H1'18

BMK reported an H1'18 Group sales increase of 9% to £75.7m (H1'17 £69.2m), despite FX headwinds, equivalent to a 17% increase at CER. Group R&D spend increased from £7.1m to £7.8m, but remained stable as a proportion of revenue (at 10.1%) although with a larger amount of development costs capitalised vs. expensed, as products neared market launch. Operating expenses remained stable at 29% of revenue. As a result, operating loss fell from £6.7m to £6m and a one-off, non-cash tax credit of £9.2m from a deferred tax revaluation resulting from the change in tax rates in Belgium, helped drive a net profit of £3.6m.

Consequently, adjusted EBITDA grew 91% to £6.3m (H1'17 £3.3m). Ongoing planned CAPEX investment in near term projects including in field trials of sea lice treatment Ectosan and the land-based salmon ova breeding facility at Salten, Norway, took end March net debt to £41.3m. Excluding £18m of non-recourse debt meant that the net debt / adjusted EBITDA ratio stood at 1.8x, well within the covenant maximum of 3x at the end of March 2018.

Post period end

BMK's investment of £12.2m (\$16.25m) for a 49% initial stake in its JV with AquaChile enables it to participate in this huge and fast-growing market from a local, established biosecure salmon breeding facility. The JV is set to meet an Internal Rate of Return target of over 20%, driven by high demand for disease-resistant salmon in a market that is itself in a high growth phase of recovery from disease challenges.

Proceeds from the £19m (gross) equity placing will be used to fund the cash consideration in two tranches: \$7.5m (£5.5m) upfront, followed by \$8.75m (£6.4m) to be paid in December 2018. There is also a shareholder loan of \$5.4m from BMK to the JV (matched by AquaChile), which in part refinances debt and provides the JV with working capital.

Forecasts

We have increased our FY'18 revenue forecast by a net 0.1%, including an adjustment for the JV, from £162 to £162.2m. In FY'19 we increase our projected revenue by 1.2% from £181.8m to £183.9m (adding in JV revenue share).

Operating costs projections change in line with H1'18, notably by increasing the proportion of capitalised as opposed to expensed R&D in FY18/19/20 to reflect progress towards market of Ectosan and other pipeline investments. This takes total R&D expenditure to 11.7% of revenue or £19.1m in FY18 falling to 10.8% and 10.2% in FY19 and FY20 respectively.

The overall result increases the key measurement of **adjusted EBITDA** up 7.6% to £16.4m in FY'18 – and by 9.9% to £22.4m in FY'19 driven by earnings' share from the JV with AquaChile. As a reminder, we include the Company's JV earnings forecasts in the table below:

JV impact on Benchmark				
Y/E end Sept, £m	4 m to Sept '18	2019	2020	Full capacity pa
JV revenue	2.4	8.9	11.5	20.9
Net JV earnings	0.1	1	2.6	8.1
Net profit margin	4%	11%	23%	39%
BMK share of JV earnings	0.05	0.5	1.3	4
Other sources of earnings to BMK	4m to Sept'18	2019	2020	At full capacity
Additional products and services	-	0.4	0.3	0.1
Sale of eggs to JV from Iceland	-	1.5	0.9	0
IP transfer	1.8	0	0	0
Total EBITDA to BMK	1.8	2.4	2.5	4.1

Source: Company, ED

We also adjust the balance sheet for the JV, including an additional £9.5m of investment to cover the £4m loan and the upfront payment of £5.5m, and adding in a deferred consideration of £6.4m, payable in December 2018 and with adjustments to working capital to reflect the JV.

Adding the £19m gross placing proceeds (c £18.6m net) into our model, this takes our end of September 2018 net debt position to £46.6m, which then increases to £56.4m at September 2019 after the placing proceeds are used to repay the deferred consideration (in December 2018) and to £53.9m in FY20.

Effectively, our end FY19/20 net debt estimates show that BMK is operating well within its covenant of 3x Net Debt/Adj. EBITDA, excluding £18m of ring fenced debt for the Salten project.

Summary of forecast changes

Y/E 30 Sept, £m	FY18e	FY19e	FY20e
<u>OLD</u>			
Sales	162.0	181.8	200.9
EBITDA	15.2	20.4	24.6
Adjusted EBITDA	15.2	20.4	24.6
Net cash/(debt)	-54.5	-56.5	-55.7
<u>NEW</u>			
Sales	162.2	183.9	203.2
EBITDA	16.4	22.4	26.8
Adjusted EBITDA	16.4	22.4	26.8
Net cash/(debt)	-46.6	-56.4	-53.9
Net Debt/Adjusted EBITDA	2.4	1.9	1.5
<u>CHANGE</u>			
Sales	0.1%	1.2%	1.2%
EBITDA	7.6%	9.9%	8.9%
Adjusted EBITDA	7.6%	9.9%	8.9%
Net cash/(debt)	14%	0%	3%

Source: ED

Financials

INCOME STATEMENT					
Y/E Sept 30, £'000s	2016	2017	2018e	2019e	2020e
Revenues	109,375	140,172	162,179	183,911	203,222
Cost of goods sold	-58,562	-77,781	-87,577	-98,392	-108,114
Gross Profit	50,813	62,391	74,602	85,519	95,108
Admin Expenses	-29,865	-39,297	-43,227	-47,333	-51,688
Other expenses/income	0	0	0	0	0
Share based payments	-749	-1,602	-1,682	-1,766	-1,855
R&D	-11,720	-13,055	-15,013	-15,764	-16,631
Other expenses/income	0	0	0	0	0
Exceptional	0	0	0	0	0
Acquisition related costs	-13,091	5,649	0	0	0
EBITDA	-3,863	15,688	16,363	22,422	26,789
Adjusted EBITDA	9,228	10,039	16,363	22,422	26,789
Operating Profit	-20,471	-7,662	-8,701	-3,300	1,972
Depreciation & Amortisation	-16,608	-23,350	-25,063	-25,722	-24,817
Interest income	-2,186	-465	-2,013	-3,329	-2,671
Other financing costs/income	0	0	0	0	0
Exceptional	0	0	0	0	0
Profit Before Taxes	-22,384	-8,100	-10,714	-6,629	-699
Current tax income	4,038	980	900	-2,900	-2,900
Adj. net income	8221	5677	7812	6253	11599
Net Income	-18346	-7120	-9814	-9529	-3599
Adj. EPS	2.0	1.1	1.4	1.1	2.1
EPS (p)	-4.4	-1.4	-1.8	-1.7	-0.6
DPS (p)	N/A	N/A	N/A	N/A	N/A
Average no. of shares, m	418.0	522.1	539.6	556.9	556.9

Source: Company historic data, ED estimates

BALANCE SHEET

Y/E Sept 30 £'000s	2016	2017	2018e	2019e	2020e
Current assets	102,490	88,160	109,152	107,980	119,766
Cash and cash equivalents	38,140	18,779	22,082	14,252	16,759
Accounts receivable	34,288	38,530	47,099	51,394	57,904
Inventories	23,231	20,053	25,673	28,035	30,805
Biological & agricultural assets	6,831	10,798	14,298	14,298	14,298
Non-current assets	408,416	418,476	442,830	436,288	427,186
Property, plant & equipment	50,023	80,845	108,043	113,164	115,141
Intangible assets	352,538	329,137	316,631	304,968	293,889
Other non-current assets	5,855	8,494	18,156	18,156	18,156
Current liabilities	-33,714	-54,026	-88,704	-88,752	-93,181
Short-term debt	-289	-6,234	-32,234	-34,234	-34,234
Accounts payable	-31,232	-44,498	-46,780	-51,224	-55,653
Other current liabilities/deferred consideration for JV	-2,193	-3,294	-9,690	-3,294	-3,294
Non-current liabilities	-109,493	-94,205	-94,205	-94,205	-94,205
Long-term debt	-37,407	-36,453	-36,453	-36,453	-36,453
Other non-current liabilities	-72,086	-57,752	-57,752	-57,752	-57,752
Equity	367,699	358,585	369,073	361,311	359,566

Source: Company historic data, ED estimates

CASH FLOW					
Y/E Sept 30, £'000s	2016	2017	2018e	2019e	2020e
Operating cash flow	-10,532	13,379	5,024	15,745	18,222
Profit before tax	-18,346	-7,120	-8,701	-3,300	1,972
Non-cash adjustments	19,668	21,372	24,525	23,916	23,844
Change in working capital	-12,557	1,162	-11,907	-2,214	-4,851
Interest paid	6,170	1,960	207	243	157
Taxes paid	-5,467	-3,995	900	-2,900	-2,900
Investing cash flow	-211,257	-36,492	-46,341	-25,576	-15,716
CAPEX on tangible assets	-18,660	-32,740	-32,740	-15,060	-11,597
CAPEX on intangible assets/capitalised R&D	-1,523	-2,423	-4,119	-4,119	-4,119
Other investing cash flows/IRO JV	-191,074	-1,329	-9,482	-6,396	0
Financing cash flow	246,365	3,752	44,620	2,000	0
Proceeds from equity	211,834	1	18,620	0	0
Increase in loans	33,445	5,921	26,000	2,000	0
Other financing cash flow	1,086	-2,170	0	0	0
Net increase in cash	24,576	-19,361	3,303	-7,830	2,507
Exchange rate effects	0	0	0	0	0
Cash at start of year	13,564	38,140	18,779	22,082	14,252
Cash at end of year	38,140	18,779	22,082	14,252	16,759
Net cash at end of year	444	-23,908	-46,605	-56,435	-53,928

Source: Company historic data, ED estimates



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