CHECKPOINT

Substrate AI   BUY

Numbers pointing in the right direction

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Substrate AI has just released their advanced 2022 results with headline Revenues of €4.0 million (vs €2.0 million in 2021) and negative Ebitda of €1.7 million (vs negative €0.69 million in 2021). The company releases results on a semester basis, allowed under BME Growth listing rules.

Their first semester results (1H22) had Revenues of €1.2 million and Ebitda of -€1.2 million. These were first announced in July 2022 and audited numbers in published October 2022.

Comparable 2H22 numbers reveal Revenues of €2.1 million and Ebitda (cash) of -€0.7 million. To make them comparable we have excluded from our calculation non-cash R&D capitalized expenses and an estimated share-based employee incentive scheme, not present in 1H22 numbers.

2H22 numbers are twice as good in Revenue terms and half the Ebitda loss compared to 1H22, in line with our expectations. We therefore maintain our 2023 and 2024 estimates unchanged.

From a valuation perspective and despite the recent bounce in the share price, SAI.MC still trades at a discount to its BME Growth comparables on most valuation metrics.

We maintain our BUY recommendation and a 12-month price target of €1.35 per share.

We believe that Substrate AI could be trading at 5x EV/Revenues next year, based on our estimates of strong revenue growth which we would consider a validation of the effectiveness of their AI algorithms.
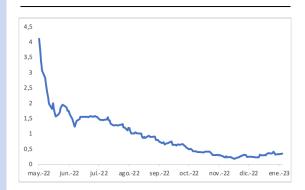
Equities

BME Growth Technology

Price (4pm 23/1/23): €0.34
Ticker: SAI.MC
Target Price (12-18 m): €1.35

52-Wk range (€):	4,10 - 0,17
Cap. Bur. (€ millones):	8.0
No. Shares (millions):	23.6
Avg. daily Vol. (€,12m):	70k
Daily volatility (avg. LTM):	9.8%

Price Chart (since IPO: May 17th)

(€ millions)	2021	2022e	2023e	2024e
Turnover	**1,6**	**3,3**	**5,9**	**8,0**
Ebitda	-0,5	-1,7	1,3	2,4
Ebitda (cash)	-0,9	-2,5	-0,9	0,2
Net Profit	-0,6	-15,9	-0,6	0,5
EPS	**-0,03**	**-0,71**	**-0,02**	**0,02**
EV/Sales (x)	**5,5**	**2,7**	**1,5**	**1,1**
EV/Ebitda (x)	n.m.	n.m.	6,9	3,7
EV/Ebitda cash (x)	n.m.	n.m.	n.m.	51,5
P/E (x)	**n.m.**	**n.m.**	**n.m.**	**17,1**
CFY	n.m.	n.m.	n.m.	0%

Substrate AI: current comparative valuations

	EV/sales (x)			EV/Ebitda - cash (x)			P/E (x)			FCY (%)		
	2021 (€ m)	2022e (€ m)	2023e (€ m)	2021 (€ m)	2022e (€ m)	2023e (€ m)	2021 (€ m)	2022e (€ m)	2023e (€ m)	2021 (€ m)	2022e (€ m)	2023e (€ m)
Lleida.Net	2,3	1,8	1,6	25,9	22,8	13,5	38,1	39,5	18,6	3,3	4,1	6,4
Substrate AI	5,5	2,7	1,5	-	-	-	-	-	-	-	-	-
Catenon	3,3	2,4	2,0	16,4	8,7	6,9	21,5	10,7	9,4	5,4	9,9	10,3
480	2,9	2,5	1,7	22,8	18,7	35,9	99,5	-	-	3,0	4,2	-
Facephi	4,8	3,9	3,4	-	-	-	-	-	962,8	-	-	-
Tier1	1,4	1,4	1,2	13,7	12,4	10,0	21,2	21,8	17,5	5,8	6,1	7,2
	2,9	2,2	1,9	47,6	73,9	24,5	93,4	-	46,8	1,9	0,4	2,6
Agile Content	2,5	1,5	1,3	-	25,8	25,4	-	-	-	-	2,8	3,1
Netex	2,9	2,3	2,0	30,6	19,5	17,0	42,7	73,2	92,7	4,3	6,1	6,7
	2,6	1,6	1,4	-	23,9	21,8	-	-	-	-	3,5	3,9
Altia	1,4	1,2	1,1	13,4	9,8	9,2	21,1	19,3	17,4	5,9	7,3	8,0
Izertis	3,2	2,4	1,8	29,3	19,1	15,2	527,9	100,9	73,4	2,5	3,9	5,1
Sngular	3,4	2,6	2,2	23,9	16,7	13,6	32,8	29,5	20,7	3,2	5,1	5,9
	2,3	1,9	1,7	20,5	14,6	12,7	38,0	31,8	25,3	3,8	4,8	5,9
Commcenter	0,6	0,6	0,5	9,9	18,9	20,5	23,2	-	-	16,2	9,3	9,5
Gigas	3,1	2,4	2,1	18,3	11,0	9,4	-	-	-	6,2	10,0	11,7
	2,0	1,6	1,4	16,2	11,8	10,8	-	-	-	7,3	9,9	11,5
Total	2,4	1,8	1,6	25,9	17,4	14,4	129,0	-	42,9	3,2	4,5	5,8

	Turnover			Ebitda (cash)			Net Profit			Cash Flow		
	2021 (€ m)	2022e (€ m)	2023e (€ m)	2021 (€ m)	2022e (€ m)	2023e (€ m)	2021 (€ m)	2022e (€ m)	2023e (€ m)	2021 (€ m)	2022e (€ m)	2023e (€ m)
Lleida.Net	18,0	22,6	26,1	1,6	1,8	3,1	0,9	0,8	1,8	1,4	1,7	2,6
Substrate AI	1,6	3,3	5,9	-0,9	-2,5	-0,9	-0,6	-15,9	-0,6	-0,7	-2,2	-1,0
Catenon	8,7	11,3	13,0	1,8	3,1	3,7	1,3	2,6	2,9	1,5	2,7	2,8
480	14,8	17,7	21,3	1,6	0,8	1,3	-0,6	-2,1	-1,7	1,2	-0,1	0,4
Facephi	12,7	15,9	17,8	-1,4	-2,6	-1,3	-0,2	-0,7	0,1	-1,4	-2,9	-1,8
Tier1	17,1	18,2	19,8	1,8	1,8	2,0	1,2	1,1	1,2	1,5	1,4	1,5
	72,9	88,9	103,8	4,4	2,5	7,7	2,0	-14,2	3,7	3,5	0,7	4,6
Agile Content	54,9	91,8	105,5	-1,2	5,2	5,6	-5,8	-4,3	-1,8	-3,3	3,0	3,4
Netex	12,2	19,8	22,8	1,2	2,3	2,7	0,6	0,4	0,3	1,2	1,7	1,8
	67,2	111,6	128,3	0,0	7,5	8,3	-5,1	-3,9	-1,5	-2,1	4,7	5,2
Altia	125,9	141,0	152,3	12,8	16,9	17,6	8,7	9,6	10,6	11,0	13,5	14,7
Izertis	65,0	87,6	115,2	7,2	11,0	13,8	0,4	1,9	2,6	4,8	7,6	9,9
Sngular	59,2	85,8	98,7	8,4	13,4	16,3	6,5	7,2	10,3	6,5	7,2	10,3
	250,2	314,5	366,2	28,4	41,4	47,8	15,6	18,7	23,5	22,3	28,3	34,9
Commcenter	46,0	55,3	59,1	3,0	1,6	1,4	0,6	-0,9	-1,0	2,4	1,4	1,4
Gigas	52,1	65,7	73,6	8,9	14,5	16,2	-5,0	-1,3	-0,5	7,4	11,8	13,9
	98,2	120,9	132,7	11,9	16,1	17,7	-4,3	-2,2	-1,5	9,7	13,1	15,3
Total	488,4	636,0	731,1	44,7	67,6	81,4	8,1	-1,6	24,1	33,3	46,8	60,0

Source: Checkpoint Partners

Substrate AI: a peek into the last 12-weeks valuation ratios

The following charts show the, absolute and relative, changes in the valuation ratios of Substrate AI during the last 12 weeks of trading. The share price has traded between a high of €0.41 and a low of €0.17, hence the strong changes in both the absolute and relative valuation ratios. At present, the stock is trading at €0.34.

Chart 1: Substrate AI, last 12-weeks of prices and weekly volumes traded (€ millions)

Source: BME Growth

We omit the EV/Ebitda and PE ratios given that Substrate AI is still a loss making company and negative values make comparisons less meaningful.

The candle chart is a standard one, where bars reveal the first and last valuation ratio of the trading week and the lines show the high-low range. The orange bar means a decline and the blue color an increase in the valuation multiples.
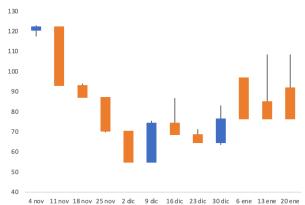
Chart 2: EV/Revenues and EV/Revenues relative to ICT sector (BME Growth, 100=Avg.)

During the last 12 trading weeks Substrate EV/Revenues ratio has been as high as 1.9x and as low as 0.9x, which on a relative basis means the stock has traded to as much as a 29% premium and as much as a 38% discount to the average EV/ Revenues valuations of the ICT sector in BME Growth. At present, Substrate AI is trading at a multiple of 1.5x versus a sector average of 1.8x.
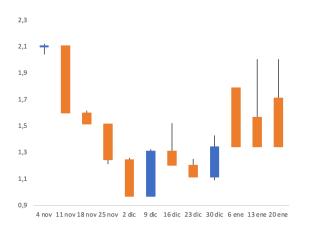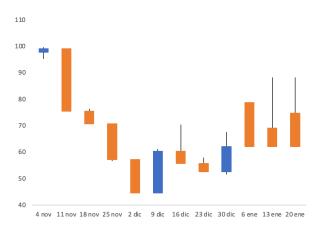
Source: Checkpoint Partners

Chart 3: EV/Gross Profits and EV/Gross Profits relative to ICT sector (BME Growth, 100=Avg.)

During the last 12 trading weeks Substrate EV/Gross Profits ratio has been as high as 2.2x and as low as 1.1x, which on a relative basis means the stock has traded to as much as a 6% premium and as much as a 50% discount to the average EV/Gross Profits valuations of the ICT sector in BME Growth. At present, Substrate AI is trading at a multiple of 1.8x versus a sector average of 2.2x

We use the EV/Gross Profits ratio as a complementary ratio to EV/Revenues to make high and low Gross Margin businesses more comparable. In our sample of ICT stocks, we come across Gross Margins of between 50% and 94% (2022e) and Substrate AI stands at an estimated 85%, a higher Gross Margin that the 72% average in our sample.
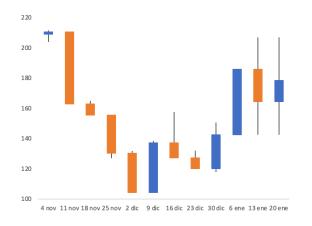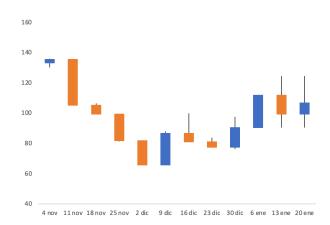

Source: Checkpoint Partners

<u>Chart 4: EV/Employee ('€000) and EV/Employee relative to ICT sector (BME Growth, 100=Avg.)</u>

During the last 12 trading weeks Substrate EV/Employee ratio has been as high as €220k and as low as €104k, which on a relative basis means the stock has traded to as much as a 36% premium and as low as a 34% discount to the average EV/Employee ratios of the ICT sector of BME Growth. At present, Substrate AI is trading at an EV/Employee €178k versus a sector average of €168k.

We find this ratio a useful reference in what it is essentially a peoples business, given that in the ICT sector there is virtually no CapEx and the bulk of spending goes directly or indirectly to personnel costs.

Source: Checkpoint Partners

Substrate AI: where we think valuations should be

We look in Substrate AI for 79% and 36% Revenue growth for 2023 and 2024 versus an ICT sector growth expectation of 14% and 11% respectively.

(€ million)	Revenues			y-o-y growth	
	2022e	**2023e**	**2024e**	**23/22**	**23/24**
AI	0,4	1,2	1,6	231%	41%
MedTech	1,1	2,0	2,5	90%	25%
Energy	0,0	0,1	0,3	n.a.	220%
FinTech	0,9	1,2	1,6	30%	30%
HR	0,7	0,9	1,2	30%	25%
AgriTech	0,3	0,5	0,9	100%	70%
Total	**3,3**	**5,9**	**8,0**	**79%**	**36%**

Source: Checkpoint Partners

On an EV/Revenues (2023e) basis we maintain our view of a 5x target multiple (a the target price of €1.35 per share).

The ICT sector is currently trading at a multiple of 1.6x and based on our sector market forecasts, there is potential for a re-rating to 2.0x over the next 12 months (25% upside). Substrate AI would then be at a 150% premium over the sector.

On top of the short term growth expectations, we believe the operational leverage of the AI product (and its effect on its participated companies) combined with the proprietary nature of its algorithms, warrant a substantial premium over some of the more service oriented peers.

As Substrate AI continues to deliver on its business plan (in our forecasts) we believe the market will continue to reward it with additional appreciation of its market value. In our November report, we pointed towards the uncertainty of a capital increase (to fund the negative cash flows) as one of the main holdbacks of value in the short term. We maintain our view and we expect that once the uncertainly is removed, we will see the share price heading closer to our projected target price.

Substrate AI: financials and forecasts

PROFIT AND LOSS ACCOUNT

Euros (000´)	2021	2022e	2023e	2024e
Net turnover	**1.600**	**3.205**	**5.874**	**8.003**
Cost of goods sold	-2	-486	-872	-1.122
Other operating income	27	67	30	35
Gross margin	**1.625**	**2.786**	**5.033**	**6.916**
% margin	*100%*	*85%*	*85%*	*86%*
Capitalization of R&D expenses	408	750	2.250	2.250
Personnel expenses	-1.374	-3.218	-3.620	-4.112
Other operating expenses	-1.352	-2.038	-2.352	-2.629
Depreciation of fixed assets	-305	-2.600	-1.750	-1.780
Subsidies and others	172	0	0	0
Gain/losses on write-downs	6	-11.534	0	0
Operating Profits	**-819**	**-15.854**	**-440**	**645**
% margin	*-51%*	*-495%*	*-7%*	*8%*
Ebitda	**-521**	**-1.720**	**1.310**	**2.425**
% margin	*-33%*	*-54%*	*22%*	*30%*
Ebitda (cash)	**-929**	**-2.470**	**-940**	**175**
% margin	*-58%*	*-77%*	*-16%*	*2%*
Financial expenses	-6	-48	-114	-158
+/- value of fin. instruments	107	0	0	0
FX differences	-7	25	0	0
+/- on sale of fin. instruments	8	7	0	0
Net Financial expenses	**101**	**-16**	**-114**	**-158**
Profit before Tax	**-718**	**-15.870**	**-554**	**487**
Income taxes	91	0	0	0
Consolidated Net Profit	**-627**	**-15.870**	**-554**	**487**
Profit attributable parent company	-607	-15.553	-543	477
Minority interests	-21	-63	-55	29

Source: Substrate AI and Checkpoint estimates

BALANCE SHEET

Euros (000´)	2021	2022e	2023e	2024e
NON-CURRENT ASSETS	**30.864**	**17.732**	**18.328**	**19.013**
Intangible assets	29.461	16.852	17.582	18.236
Tangible fixed assets	117	158	221	309
L/T financial investments and other	984	412	183	91
Deferred tax assets	302	311	342	376
CURRENT ASSETS	**1.322**	**1.812**	**2.446**	**2.831**
Inventories	0	337	438	569
Trade and other receivables	638	1.212	1.576	1.734
S/T financial investments and other	408	82	98	117
Cash and cash equivalents	268	180	333	409
TOTAL ASSETS	**32.186**	**19.544**	**20.774**	**21.843**
EQUITY	**26.632**	**16.775**	**17.122**	**17.859**
Capital	2.029	2.232	2.407	2.407
Share premium	26.656	34.267	34.742	34.742
Reserves and other	-2.032	-19.824	-20.127	-19.391
NON-CURRENT LIABILITIES	**430**	**1.075**	**967**	**1.064**
Long-term liabilities	430	1.075	967	1.064
CURRENT LIABILITIES	**5.123**	**1.694**	**2.684**	**2.921**
Short-term financial debts	4.855	1.081	2.041	2.245
Trade and other payables	268	612	643	675
TOTAL LIABILITIES	**33.356**	**19.544**	**20.774**	**21.843**
Working Capital	373	938	1.372	1.628
Debtor Turnover (days)	122	105	87	75
Creditor Turnover (days)	44	64	71	64
Cash	676	262	431	527
Short Fiancial Debt	4.855	481	2.041	2.245
Long Term Financial Debt	430	1.075	967	1.064
Net debt	**4.610**	**1.295**	**2.578**	**2.783**

Source: Substrate AI and Checkpoint estimates

Checkpoint recommendation System

The Checkpoint Recommendation System is based on absolute returns, measured by the upside potential (including dividends and capital reimbursement) over a 12-month time horizon. Checkpoint recommendations (or ratings) for each stock comprises 3 categories: Buy (B), Neutral (N) and Sell (S).

Buy: the stock is expected to generate total return of over 15% during the next 12 months time horizon
Neutral: the stock is expected to generate total return of -15% to +15% during the next 12 months time
Sell: the stock is expected to generate total return under -15% during the next 12 months time horizon.

History of Checkpoint recommendations (last 12 months)

Date	Stock	Recommen.	Price (€)	Target P.(€)	Period	Analyst
11.11.2021	LLN	BUY	4.38	9.00	12m	Guillermo Serrano
22.02.2022	LLN	BUY	3.24	9.00	12m	Guillermo Serrano
04.05.2022	LLN	BUY	4.06	9.00	12m	Guillermo Serrano
11.08.2022	LLN	BUY	2.50	7.50	12m	Guillermo Serrano
25.10.2022	LLN	BUY	1.84	6.00	12m	Guillermo Serrano
23.11.2022	SAI	BUY	0.22	1.35	12m	Guillermo Serrano
24.01.2023	SAI	BUY	0.34	1.35	12m	Guillermo Serrano

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Frequency of analyst reports: at present Checkpoint has committed to a quarterly update of Substrate AI financial and operational performance.

Investment horizon: our reports focus mainly on small capitalization and illiquid stocks where standard Venture Capital investment criteria should apply. An investment into a small market capitalization stock should be done on a 3-5 year time horizon in order to realized the full potential of the investment opportunity.

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