

Substrate AI

BUY

Venture Building is the focus, following the SubGen AI spin-off

Analyst: Guillermo Serrano - gfs@checkpointp.com

7am, 19th September 2024*

Last July, Substrate AI offered shareholders (on the register as of 31st July 2024) 1 share of their subsidiary Subgen AI for every Class A Substrate AI share held and 1 share per 100 Class B shares held. Effectively, Substrate AI will (once the transaction is executed) reduce its stake in Subgen AI from the current 100% to below 20%.

Given that approximately half of our prior SAI.MC target price of €1.00 (May 24 report) was attributable to Subgen AI, we are now adjusting our target price to €0,60.

The Venture portfolio of Substrate AI (excluding Subgen AI) continues to do well across all its verticals and we maintain our estimate of potential value in excess of €50 million (5.3x 2024 and 3.8x 2025 estimated sales).

We estimate the equity market is currently attributing a value of just €11 million for the Medtech, HRTech, AgriTech and Fintech portfolio companies, which we consider an undervaluation.

We believe the most valuable holdings are the 70% stake in 4D Medica (MedTech) and Fleebe AI (HRTech), with a combined potential value of €39 million, according to our valuation estimates.

Substrate AI has also announced its intention to list some of its participated companies in public markets, so to provide more value visibility to its portfolio and a way to provide them access to the capital markets for growth financing.

We maintain our BUY recommendation and we introduce and introduce a new price target of €0,60.

Equities

BME Growth

Price (4pm 18/09/24): Ord. €0.11

Ticker: SAI.MC

Target Price (12-18 m): €0.60

Trading data

52-Wk range (€):	0.31 - 0,11
Mkt. Cap. FD (€ millions):	13.4
No. Ord. Shares (millions):	121.9
Avg. daily Vol. (€12m):	154K
Daily volatility (avg. LTM):	2.8%

Price Chart (last 12 months)



(€ millions)	2024e	2025e	2026e
Turnover	11,8	16,3	21,7
Ebitda	4,0	5,3	6,9
Net Profit	1,4	2,8	4,2
EPS	0,01	0,02	0,03
EV/Sales (x)	1,3	0,9	0,7
EV/Ebitda (x)	3,8	2,9	2,2
P/E (x)	9,9	4,9	3,2

Weaknesses	Threats
<p>Exposed to inorganic growth with the risks that it entails. Substrate AI partly depends on the stock market and credit markets to obtain the financial resources it needs.</p>	<p>Presence of large, well-established and well-capitalized companies may present a competitive threat in each of the markets where they operate.</p>
<p>Geographical concentration, most of its sales are in Spain and now partly in Latin America following the Binit group acquisition</p>	<p>Future capital increases to finance inorganic growth, which may dilute the shareholder.</p>
<p>Whereas we expect accounting profits in 2024, the results are still reliant on the capitalization of R&D expenses. The group still requires of capital increases to fund their operations.</p>	<p>Artificial Intelligence is a hot topic the world over and competition for talent remains strong, which may place smaller companies at a disadvantage.</p>
Strengths	Opportunities
<p>Their core asset is a proprietary Biology-Inspired next generation AI technology, developed by one of the founders and CTO, Bren Worth, alongside the Rensselaer Polytechnic Institute in NY.</p>	<p>Substrate AI, through its Subsidiary SubGen AI, has developed Serenity Star (AlaaS) and Metacontrol, two LLM based Software products with excellent potential.</p>
<p>A diversified portfolio of companies organized into six different verticals, reducing their exposure to a particular sector the economy.</p>	<p>Expected strong sales growth rate of 38% and 33% in 2025 and 2026.</p>
<p>Its smaller size gives it the agility to move more quickly in the commercial field and in the execution of projects.</p>	<p>Value creation through inorganic growth. By acquiring companies that can benefit from AI, Substrate AI stands to create critical mass.</p>
<p>A strong management team with a track record for creating value for shareholders.</p>	<p>Spain is emerging as a country with a high degree of digital talent, where Substrate AI is perfectly positioned in the short, medium and long term.</p>
<p>Access to capital through a €20 million committed line of convertible bonds, of which 30% has already been used.</p>	<p>Possibility of being acquired. Artificial Intelligence is on the rise and larger companies are looking to acquire talent and market share.</p>

SubGen AI: a spin-off to unleash the value potential of AI

The company announced on July 26th, 2024 the distribution of 1 share of SubGen AI LTD per 1 class A share of Substrate AI and 1 share of Subgen AI per 100 class B shares of Substrate AI. The distribution will be made in favor of whoever is a shareholder of the company on 31 July 2024.

There are 121.9 million Class A Shares and 139 million Class B Shares, so taking into account the distribution ratio, a maximum of 123 million Subgen AI Shares are subject to distribution out of a total of 150 million.

The remaining Subgen IA's 27 million shares will still be held by Substrate AI.

According to our prevailing target price, up until the announcement, we attribute 50% of the value of Substrate AI to the Artificial Intelligence division (namely Subgen AI) and 50% to the remaining divisions under the HRTech, MedTech, Fintech and AgriTech divisions.

All other things being equal, our current price target gets now been adjusted to €0,60 per share, made up of €0.50 attributable to the HRTech, MedTech, Fintech and AgriTech divisions together with its parent company, and some €0,10 attributable to the stake in SubGen AI.

We expect all divisions to benefit from the Artificial Intelligence software provided by Subgen AI to power sales growth going forward. We expect the combined portfolio companies to deliver €11.8 million in sales this year and some €16.3 million in 2025 (+38%). With financially sound balance sheets and positive cash flows in most of them, we expect them to continue to invest in organic growth and product development.

Over the next 12 months, we expect some of the portfolio companies to list in public markets as they gradually make their intentions public. This will provide more visibility to existing shareholders and, in the case of Subgen AI, a liquidity event for those Substrate AI shareholders who agree to receive their Subgen AI shares sometime in 4Q24. In addition, we expect the market to recognize the portfolio companies' progress with upcoming results announcements.

Substrate AI sum of the parts valuation

(€ million)	Revenues			Growth	
	2024e	2025e	2026e	25/24	26/25
Subgen AI (20%)	4,0	7,1	12,7	78%	79%
Substrate AI (parent co.)	0,9	1,2	1,3	29%	12%
MedTech (70%)	3,5	5,9	8,0	67%	36%
Fintech	0,0	0,1	0,2	<i>n.a.</i>	100%
Energy	0,9	1,0	1,2	15%	15%
HR	5,1	6,0	7,7	18%	29%
AgriTech	1,5	2,2	3,3	50%	50%
Total Venture Portfolio	11,8	16,3	21,7	38%	33%

	EV/ Sales			Target est. valuation (€ millions)
	2024e (x)	2025e (x)	2026e (x)	
Subgen AI (20%)	24,8	13,9	7,8	19,8
Substrate AI (parent co.)	2,5	1,9	1,7	2,3
MedTech (70%)	7,2	4,3	3,2	17,7
Fintech	2,3	2,0	1,7	2,0
Energy	<i>n.m.</i>	4,7	2,3	0,5
HR	4,2	3,5	2,7	21,1
AgriTech	7,5	5,0	3,3	11,2
EV	5,3	3,8	2,9	74,5
Equity Value				72,5
Per share				€ 0,60

	EV/ Sales			Current inferred valuations (€ millions)
	2024e (x)	2025e (x)	2026e (x)	
Subgen AI (20%)	2,3	1,3	0,7	4,1
Substrate AI (parent co.)	0,2	0,2	0,2	0,5
MedTech (70%)	0,7	0,4	0,3	3,7
Fintech	<i>n.m.</i>	<i>n.m.</i>	0,2	0,4
Energy	0,2	0,2	0,2	0,1
HR	0,4	0,3	0,3	4,4
AgriTech	0,7	0,5	0,3	2,3
EV	1,3	0,9	0,7	15,4
Equity Value				13,4
Per share				€ 0,11

Source: Checkpoint Partners

PROFIT AND LOSS ACCOUNT

We have excluded our estimates of Subgen AI from the consolidated numbers of Substrate AI to arrive at this “pro-forma” estimate of both the Profit and Loss Account and the Balance Sheet.

Euros (000´)	2024e	2025e	2026e	Growth	
Net turnover	11.826	16.344	21.675	38%	33%
Cost of goods sold	-5.840	-7.774	-9.720	33%	25%
Gross margin	5.986	8.570	11.955	43%	39%
<i>% margin</i>	<i>51%</i>	<i>52%</i>	<i>55%</i>		
Other Income	5.000	3.500	3.000	-30%	-14%
Personnel expenses	-4.178	-4.252	-4.978	2%	17%
Other operating expenses	-2.803	-2.531	-3.079	-10%	22%
Depreciation of fixed assets	-1.800	-1.800	-1.800	0%	0%
Subsidies and others	0	0	0	n.m.	n.m.
Gain/losses on write-downs	0	0	0	n.m.	n.m.
Operating Profits	2.205	3.487	5.098	58%	46%
<i>% margin</i>	<i>19%</i>	<i>21%</i>	<i>24%</i>		
Ebitda	4.005	5.287	6.898	32%	30%
<i>% margin</i>	<i>34%</i>	<i>32%</i>	<i>32%</i>		
Net Financial expenses	-682	-382	-331	-44%	-13%
Profit before Tax	1.523	3.106	4.767	104%	53%
Income taxes	-183	-373	-572	n.m.	n.m.
Consolidated Net Profit	1.340	2.733	4.195	104%	53%

Source: Checkpoint estimates

BALANCE SHEET

Euros (000´)	2024e	2025e	2026e
NON-CURRENT ASSETS	42.277	45.487	49.169
Intangible assets	17.711	20.368	23.423
Tangible fixed assets	322	450	630
Rights to Use	573	596	620
Investments in associated co´s	151	151	151
L/T financial investments and other	21.651	21.866	22.083
Deferred tax assets	1.868	2.055	2.261
CURRENT ASSETS	10.557	12.796	19.982
Inventories	941	1.223	1.467
Trade and other receivables	5.913	8.172	10.838
S/T financial investments and other	42	50	60
Cash and cash equivalents	3.629	3.318	7.585
TOTAL ASSETS	52.683	58.131	69.000
EQUITY	41.409	47.348	57.502
NON-CURRENT LIABILITIES	7.407	4.958	4.816
Long-term liabilities	5.748	3.272	3.101
CURRENT LIABILITIES	3.866	5.824	6.683
Short-term financial debts	1.062	1.533	1.427
Trade and other payables	2.593	4.122	5.120
TOTAL LIABILITIES	52.683	58.131	69.000

Source: 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
09.03.2023	LLN	BUY	2.27	5.00	12m	Guillermo Serrano
10.05.2023	LLN	BUY	1.64	5.00	12m	Guillermo Serrano
05.09.2023	LLN	BUY	1.15	3.00	12m	Guillermo Serrano
20.11.2023	SAI	BUY	0.20	1.00	12m	Guillermo Serrano
12.12.2023	LLN	BUY	0.80	3.00	12m	Guillermo Serrano
06.05.2024	LLN	BUY	1.10	3.00	12m	Guillermo Serrano
27.05.2024	LLN	BUY	1.32	3.00	12m	Guillermo Serrano
28.05.2023	SAI	BUY	0.16	1.00	12m	Guillermo Serrano
19.09.2023	SAI	BUY	0.11	0.60	12m	Guillermo Serrano

Checkpoint does and seeks to do business with companies covered in its research reports. As a result, investors may take the view this could affect the objectivity of the report and therefore should consider this report as only a single factor in making their investment decision.

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.

Disclaimer:

Checkpoint Partners (Spain) SLU [Checkpoint] is a financial advisory firm primarily specializing in the technology sector. Further information can be obtained from our website www.checkpointp.com or by writing to us at gfs@checkpointp.com.

All third party information has been checked to the best of Checkpoint's professional expertise and accuracy, however it has not been independently verified and Checkpoint makes no warranty, express or implied, as to the accuracy, reliability, timeliness or completeness of the information.

Furthermore, this report has been drawn up in accordance with the Commission's Delegated Regulation (EU) 2016/958 of 9 March 2016 supplementing Regulation (EU) 596/2014 of the European Parliament and of the Council as regards regulatory technical standards for the objective presentation of investment recommendations or other information recommending or suggesting an investment strategy and for the disclosure of particular interests or indications of conflicts of interest.

Checkpoint has no conflicts of interest in relation to the drafting of this research report within the meaning of Article 6. 1 of the regulations, as Checkpoint does not hold a net long or short position exceeding the threshold of 0.5% of the total issued share capital of the issuer mentioned in this report and the person preparing the report is not a market maker or liquidity provider of the issuer's financial instruments, has not been lead or co-manager during the twelve months preceding any offering of financial instruments of the issuer, is not a party to an agreement with the issuer relating to the provision of investment firm services set out in Sections A and B of Annex I to Directive 2014/65/EU of the European Parliament and of the Council.

Checkpoint is remunerated for the drafting of this report by the firm under review and may be, or seeking to be, engaged by the companies described in this report for other types of financial services. The investor should take this fact into consideration and assume that Checkpoint may have a conflict of interest that could affect its objectivity. Accordingly, this report should be considered only as one element in making investment decisions.

Checkpoint does not provide advice on legal and tax matters. This should be referred to appropriate professionals. Past performance is not a guarantee of future returns. Investments denominated in foreign currencies are subject to fluctuations in exchange rates that could have an effect on investor returns. Investment prices may fluctuate and, therefore, you may not get back some or all of your original investment. Neither this report nor any accompanying documents or information may be reproduced in whole or in part, or used for any purpose other than that for which they are presented, without the prior written consent of Checkpoint.

CHECKPOINT