Arterra Bioscience

Sector: Biotech

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Getting ready to change gear

Arterra Bioscience is an Italian research-based biotech company listed on AIM Italia in November 2019. It develops innovative molecules and leverages its expertise to manufacture bio-active ingredients for the cosmetics industry, with ready-to-go applications also for nutraceutics, medical devices and agrochemicals.

Fair Value (€)	**5.30**
Market Price (€)(*)	**3.66**
Market Cap. (€m)	**24.0**

FY20 above expectations

Despite Covid-19 outbreak, Arterra reported +19% YoY top line growth (+15% vs our estimates), driven by massive growth on Vitalab sales (+67% YoY) and rising R&D tax credits (+48%) due to favourable changes in legislation, which counterbalanced 9% decrease of sales to Intercos. EBITDA margin improved to 37% (34% in 2019), supported by contribution from tax credit which offset higher operating expenses from greater use of outsourcing. Net cash position remained almost unchanged at €4.1mn, despite material cash absorbed by capex and higher Net Working Capital.

In better shape to face the future

Reduced business activity allowed Arterra to strengthen the team, complete reorganization and planned investments on production capacity in order to face stronger demand and product diversification expected from 2022.

Also, in April 2021 Arterra has announced a partnership with ADL Farmaceutica for the production of medical devices. Albeit the small size of partner seems to limit boost to Arterra sales, the agreement is strategically relevant as it represents Arterra's first step outside the cosmetic business.

Recovery takes times: top line estimates revised down, FCF upward

Business recovery and product diversification in 2021 will come at slower pace than initially expected. As an effect, we revised downward our estimates: -15%/-25% revenues from sales 2021E-2022E. Yet, EBITDA margin is expected to rise up to 40% by 2023E, thanks to higher than expected benefits from reorganization and efficiency improvements carried during 2020 and Net Financial Position is foreseen to benefit from the higher OpFcF a.t. (€3.7mn over 3yrs), reaching €7.7mn net cash by 2023E.

Fair value at €5.3 (from €4.2)

At current stock market price (€3.7), Arterra trades at 3.4x EV/Sales 2021E, versus 8.3x EV/Sales median of all the peers considered.

We revise upward our fair value per share to €5.3 (vs previous €4.2), derived as the average between DCF model and peers' multiple relative valuation. At fair value, stock would trade at 5.9-5.1x EV/Sales and 15.6x-13.1x EV/EBITDA for 2021E-22E, implying a discount of over 25% vs peers.

KEY FINANCIALS (€m)	2020A	2021E	2022E
REVENUES	4.3	4.3	4.7
EBITDA	1.6	1.6	1.8
EBIT .	1.2	1.2	1.5
NET PROFIT ADJ.	1.2	1.2	1.3
OPFCF a.t.	0.0	1.4	1.5
NET INV. CAP	4.1	3.8	3.6
EQUITY	8.2	9.3	10.5
NET CASH POS.	4.1	5.5	7.0

Source: Arterra (historical figures), ITA GAAP
Value Track (2021E-22E estimates)

RATIOS & MULTIPLES	2020A	2021E	2022E
EBITDA MARGIN (%)	37.2%	37.9%	39.0%
EBIT MARGIN ADJ. (%)	27.9%	28.7%	30.7%
NET DEBT / EBITDA (x)	n.m.	n.m.	n.m.
NET DEBT / EQUITY (%)	n.m.	n.m.	n.m.
EV/SALES (x)	3.8	3.4	2.8
EV/EBITDA (x)	10.2	9.1	7.3
P/E ADJ. (x)	19.7	19.8	18.4
DIV YIELD (%)	0.0	0.0	1.4

Source: Arterra (historical figures), ITA GAAP
Value Track (2021E-22E estimates)

STOCK DATA	
FAIR VALUE (€)	5.3
MARKET PRICE (€)	3.7
SHS. OUT. (m)	6.5
MARKET CAP. (€m)	24.0
FREE FLOAT (%)	26.9
AVG. -20D VOL. (#)	29,393
RIC / BBG	ABS.MI / ABS IM
52 WK RANGE	2.72 – 4.30

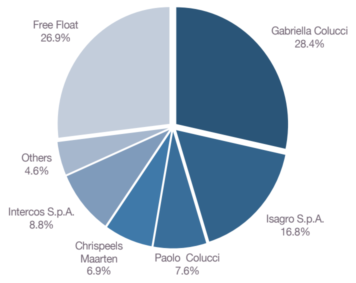
Source: Stock Market Data
(*) Stock Price at April 21th

Business Description

Arterra Bioscience is an Italian research-based biotech company ("PMI Innovativa") focused on developing innovative molecules and leveraging its expertise to manufacture bio-active ingredients for the cosmetics industry, with ready-to-go applications also for nutraceutics and agrochemicals.

Although today Cosmetics represent 100% of manufacturing revenues towards the exclusive partner Intercos Group, Arterra presents a strong growth potential due to the diversification into new end markets, as nutraceuticals and medical devices, and new partnerships through a flexible business model.

Shareholders Structure



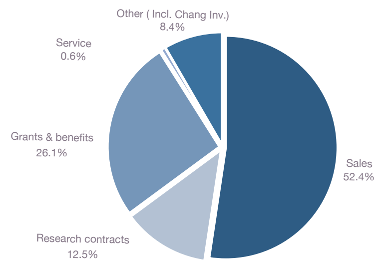
Source: Arterra SpA

Key Financials

€'000	2019A	2020A	2021E	2022E
Total Revenues (VoP)	**3,627**	**4,309**	**4,323**	**4,726**
Chg. % YoY	22%	18.8%	0.3%	9.3%
EBITDA	**1,236**	**1,602**	**1,637**	**1,843**
EBITDA Margin (% of Revenues)	34.1%	37.2%	37.9%	39.0%
EBIT	**940**	**1,202**	**1,241**	**1,453**
EBIT Margin (% of Revenues)	25.9%	27.9%	28.7%	30.7%
Net Profit	**857**	**1,109**	**1,102**	**1,195**
Chg. % YoY	-17.9%	29.3%	-0.6%	8.4%
Adjusted Net Profit	**967**	**1,219**	**1,212**	**1,305**
Chg. % YoY	-7.4%	26.0%	-0.5%	7.7%
Net Fin. Position	**4,007**	**4,066**	**5,483**	**6,956**
Net Fin. Pos. / EBITDA (x)	n.m	nm	nm	nm
Capex	-1,618	-437.9	-308.0	-314.4
OpFCF b.t.	**209**	**134**	**1,518**	**1,730**
OpFCF b.t. as % of EBITDA	17%	8.4%	92.7%	93.9%

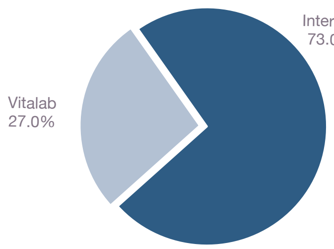
Source: Arterra (historical figures), Value Track (estimates)

Revenues breakdown 2020



Source: Arterra SpA

Cosmetic Sales breakdown 2020



Source: Arterra SpA

Investment Case

Strengths / Opportunities

- Cosmetic industry with existing partnership and growth in the Prestige category;
- New end markets with ready-to-go applications for medical devices, nutraceutics and agrochemicals;
- Diversified business model via IP model when direct production does not suit.

Weaknesses / Risks

- A slower than expected post Covid-19 recovery may reduce growth and profitability in the short term;
- Most of the revenues from sales depend on Intercos Group;
- The cosmetic business remains volatile and difficult to plan.

Stock multiples @ €5.3 Fair Value

	2021E	2022E
EV / SALES (x)	5.9	5.1
EV / EBITDA (x)	15.6	13.1
EV / CAP.EMP. (x)	6.7	6.8
OpFCF Yield (%)	6.8	8.4
P / E (x)	28.6	26.6
P / BV (x)	3.7	3.3
Div. Yield. (%)	0.0	0.9

Source: Value Track

FY2020 results

Arterra came out with 2020 financial results better than our forecasts, albeit Covid-19 outbreak and the dramatic fall of travellers have slowed down the company's growth. Moreover, reduced business activity allowed Arterra management to strenghen the team, complete processes reorganization and investments on tangible assets in order to increase production capacity. All this is hinstrumental to face the stronger demand and product diversification expected from 2022. In short Arterra reported:

- Top line ca. 15% higher than expected, mainly due to the remarkable Vitalab growth and increase of R&D tax credit, now structurally higher thanks to the change of legislative framework;
- EBITDA margin at 37.2% vs ca. 29% forecasted, benefitting also from ca. €1.3mn grants and tax credits received in the year;
- Net Cash position at ca. €4.1mn, slightly lower than expected and due to higher net working capital (stocks and R&D tax credits).

Arterra: 2020A vs VT 2020E

(€mn)	2020		
	Expected	Actual	A vs. E - Δ(%)
Total Revenues (VoP)	**3,756**	**4,309**	**14.7%**
EBITDA	**1,087**	**1,602**	**47.4%**
EBITDA margin (%)	28.9%	37.2%	n.m.
EBIT	**733**	**1,202**	**64.1%**
EBIT margin (%)	19.5%	27.9%	n.m.
Net Profit	**696**	**1,109**	**59.4%**
Adjusted Net Profit	**806**	**1,219**	**51.3%**
OpFCF b.t.	**456**	**134**	**-70.6%**
Net Cash Position	**4,426**	**4,066**	**-8.1%**

Source: Value Track Analysis

Profit & Loss

Revenues evolution

Overall, Total Revenues increased significantly year on year (ca. +19%), reaching a new peak at €4.3mn vs €3.6mn in 2019, with revenues from sales slightly improved (+4% YoY), despite of adverse conditions, and tax credits unprecedently higher. More in details, it is worthy to note that:

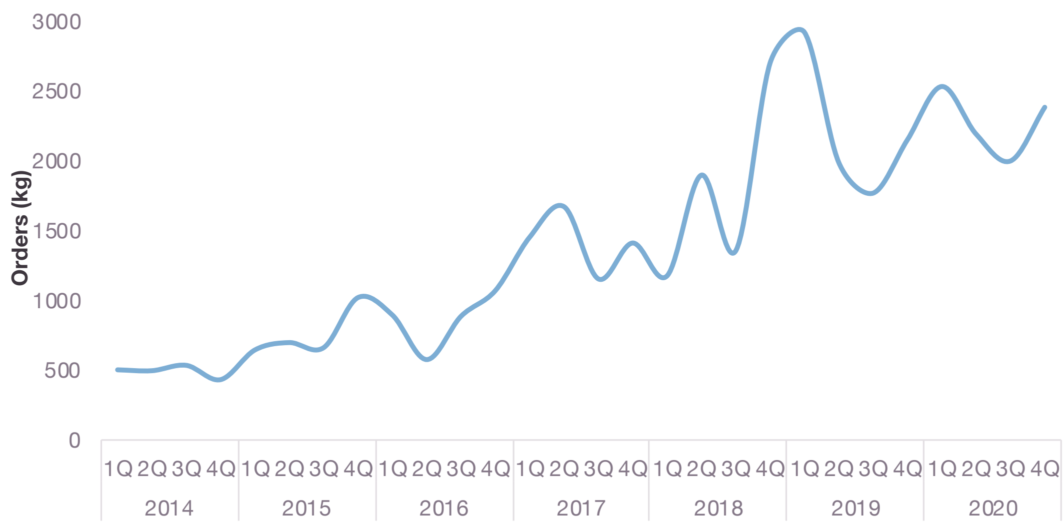
- Vitalab sales impressively increased (+67 % YoY) thanks to sizeable orders from its main client, i.e. Estee Lauder;
- Intercos sales fall by 9% YoY as the leader in the make-up segment suffered from forced closure of retail stores worldwide;
- Grants & Fiscal benefits rose by ca. 48 % YoY, thanks to higher R&D tax credit also due to favourable changes in legislative framework.

Arterra: Revenues Breakdown 2019A and 2020A

€'000	2019FY	2020FY	Change YoY (%)
Sales - Intercos	1,795	1,632	-9.0%
Sales - Vitalab	372	624	67.6%
Total Sales	**2,167**	**2,257**	**4.1%**
Research Grants & Fiscal benefits	763	1,126	47.6%
Research Contracts	516.7	539.5	4.4%
Services and others (incl. other tax credits)	180	386	115.1%
Total Revenues (VoP)	**3,627**	**4,309**	**18.8%**

Source: Arterra, Value Track Analysis

Arterra: Quarterly Orders in Kg (2014-2020)



Source: Arterra, Value Track Analysis

Below the top line we note **EBITDA margin stood at 37% vs 34% in 2019**, strongly supported by contribution from tax credits and despite operating expenses temporarily increased over the year:

- Raw materials costs increased by 15% YoY due to greater use of outsourcing services to Demetra s.r.l. in order to build inventories and face potential and sudden increase in workload in a highly volatile demand outlook;
- Services costs rose by 20% YoY mainly attributable to advisory and other costs for AIM listing;
- Labour costs lifted up as Arterra hired a total of 4 full time employees and a part time one.

Reported **EBIT increased by ca. 28%, mirroring EBITDA growth** and in spite of higher D&A, inflated by amortization of IPO costs and PP&E acquired over the year. Adjusting for amortization of listing costs, EBIT stood at €1.4mn (+24% YoY), with margin up by 100bps vs 2019.

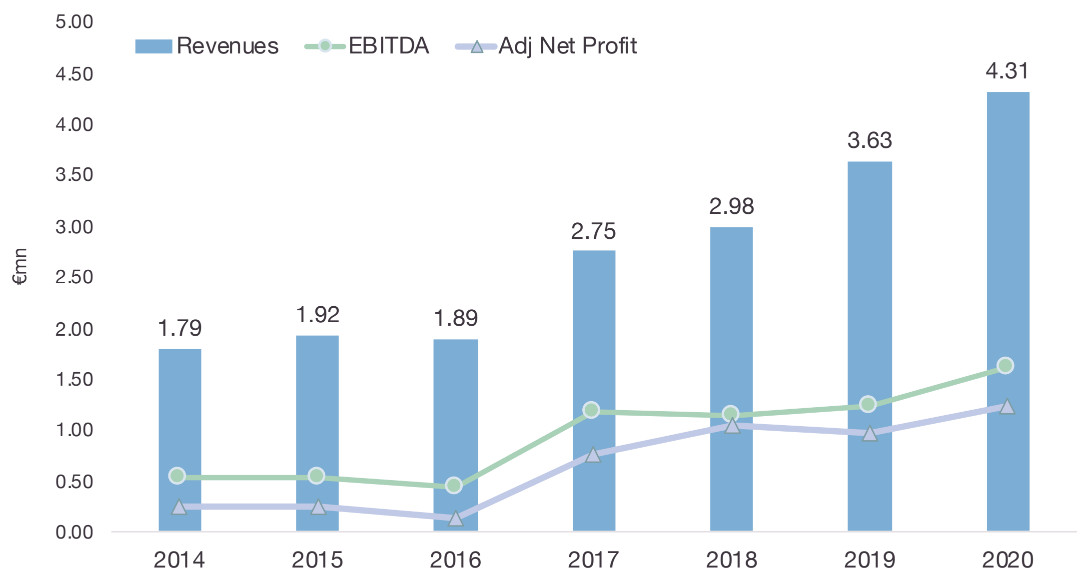
As a result, **Net profit rose by 29% YoY** (€1.1mn vs €0.9mn in 2019), mirroring EBIT growth.

Arterra: Profit & Loss 2019FY and 2020FY

€'000	2019FY	2020FY	Change YoY (%)
Total Revenues (VoP)	**3,627**	**4,309**	**18.8%**
Raw Materials	-455	-525	15.4%
Services	-726	-873	20.2%
Gross Profit	**2,445**	**2,910**	**19.0%**
Gross margin %	67%	68%	100bps
Cost of Labour	-1,025	-1,128	10.0%
Others op. costs	-184	-181	-1.7%
EBITDA	**1,236**	**1,602**	**29.6%**
EBITDA margin %	**34%**	**37%**	**300bps**
D&A	-296	-400	34.8%
EBIT	**940**	**1,202**	**27.9%**
EBIT Adj.	**1,094**	**1,357**	**24.0%**
EBIT margin Adj. %	30%	31%	100bps
Net Financial result (incl. div. from Vitalab)	-154	-158	2.5%
Pre-tax Profit	**940**	**1,199**	**27.5%**
Pre-tax margin %	31%	26%	-16.1%
Taxes	-83	-91	9.0%
Net Profit	**857**	**1,109**	**29.3%**
Net Profit Adj.	**967**	**1,219**	**26.0%**

Source: Arterra, Value Track Analysis

Arterra: 2014 – 2020 Profitability evolution



Source: Arterra, Value Track Analysis.

Balance Sheet and Cash Flow Statement

At Balance Sheet level, **Net Financial Position remains almost flat at ca. €4.1mn**, despite material cash absorbed by:

- All-time-high Net Working Capital, which grew by ca. €1mn, mainly driven by increase in receivables (and tax credits) as well as inventories at above-the-average level;
- More than €400k Capital Expenditures, mainly attributable to PP&E investments in order to face expanding business and support the faster growth ahead.

As an effect, Arterra generated ca. €43k of operating free cashflow after tax in front of €1.6mn EBITDA, maintaining Net financial position almost unchanged.

Arterra: 2019 – 2020 Balance Sheet structure

€'000	FY2019	FY2020
Working Capital	1,171	2,218
Net Fixed Assets	2,437	2,419
Provisions	504	522
Total Capital Employed	**3,103**	**4,115**
Group Net Equity	**7,110**	**8,181**
Net Fin. Position [i.e. Net Debt (-) Cash (+)]	**4,007**	**4,066**

Source: Arterra, Value Track Analysis.

Arterra: 2019 – 2020 Cash Flow analysis

€'000	FY2019	FY2020
EBITDA	**1,236**	**1,602**
Op. WC requirements	717	-1,048
Capex (incl. IPO costs capitalization)	-1,618	-438
Change in Provisions	-127	18
OpFCF b.t.	**209**	**134**
Cash Taxes	-83	-91
OpFCF a.t.	**125**	**43**
Net Financial Charges	1	-2
Others	0	18
Capital Injections (gross)	4,000	0
Dividends paid	-300	0
Change in Net Fin. Position	**3,832**	**59**
Net Cash (Debt)	**4,007**	**4,066**

Source: Arterra, Value Track Analysis.

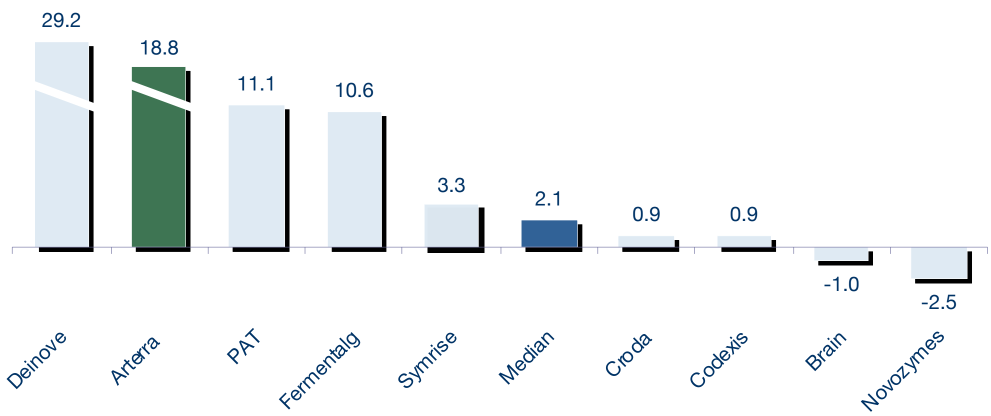
Benchmarking analysis: Arterra results vs selected peers

Comparing Arterra performances with selected peers in the biotech segment, we notice that it's positioned among the top performers of the year.

Overall, albeit pandemic severely hit most of industries, the whole biotech industry showed a good level of business resiliency to external shocks. More in detail, we note that:

- Smaller firms, i.e. Deinove, PAT and Fermentalg, experienced a noticeable top line growth (all above +10% YoY), supported by their small size, niche positioning and/or strong strategic partnerships with global players;
- Larger selected peers reported flattish top line, as they were directly exposed to Covid-19-induced slippages in consumer demand, albeit some of them (e.g. Symrise) counterbalanced it thanks to an unexpected high demand for hygiene products.

Arterra: Peers' 2020 Sales Growth YoY (%)



Source: Arterra, Companies' web sites, Value Track Analysis.

If we compare Arterra to main players in the cosmetic industry – as a benchmark within Arterra end market – it again positions itself quite well:

- The larger names in the personal care sector – e.g. Estee Lauder, Beiersdorf, L'Oreal, Shiseido - reported top line down by 4-18% YoY – generally supported by the skin-care segment and by the Asian markets (China in particular);
- All of them are expecting positive top line growth in coming quarters, also due to renewed marketing and distribution policies, increased push on online channels and product innovation.

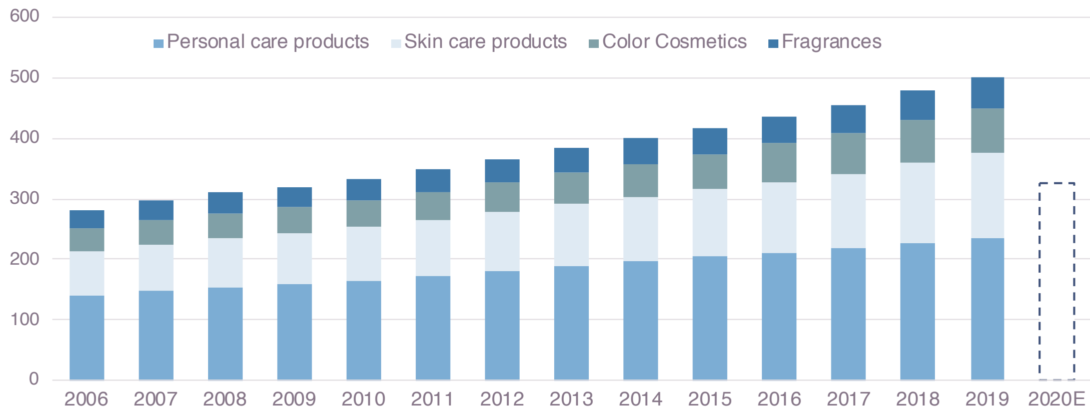
Forecasts 2021-2023

The picture in the cosmetic sector

The luxury sector and the global beauty industry have been shocked by the pandemic: with in-store shopping as the main sales' channel, the lack of travelling and continuous lockdowns are expected to drive 2020 US beauty-industry revenues down by 35% with respect the previous year (McKinsey report).

However, the industry reacted promptly to the disruptive event, with brands temporarily switching their manufacturing to produce hand sanitizers and cleaning agents, but also with a flourish of brands' online stores.

Global beauty retails sales 2006 – 2020E

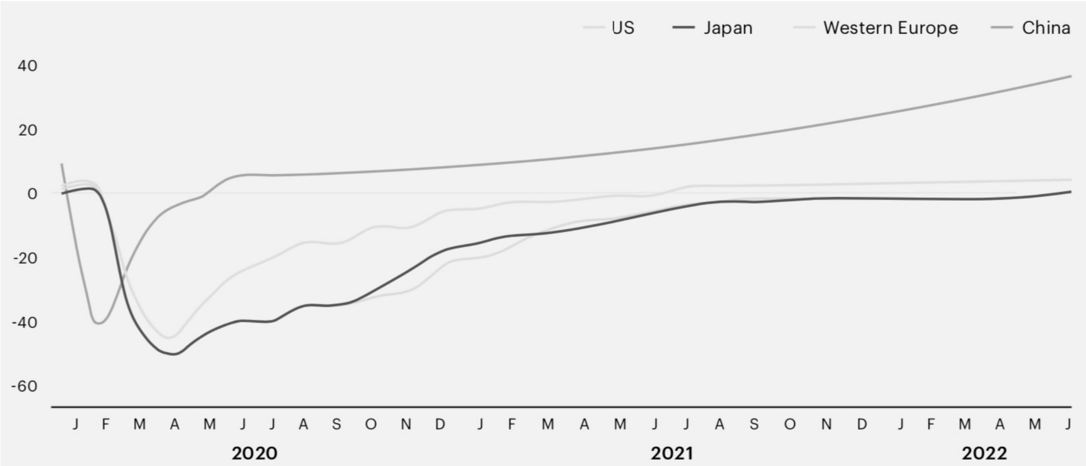


Source: McKinsey, Euromonitor

According to Mckinsey "The State of Fashion 2021" report, global beauty market will recover quickly and surpass 2019 levels in 2021, confirming again its resiliency versus macroeconomic framework and versus the fashion industry, expected not to recover until 2022. However, industry growth would differentiate according to regions' features:

- **Chinese sales rebounded:** China in 2020 already surpassed 2019 beauty sales and is expected to grow by 8-10% between 2019 and 2021. This reflects the high e-commerce penetration, with online sales accounting for more than 40% of total sales in pre-Covid era. L'Oréal reported a boost of digital sales over 2020 (+62% YoY)
- **US on track to recover:** digitalisation will play a pivotal role on the recovery of US beauty sales too. In 2019 online stores accounted for 20% of the beauty market and with e-commerce penetration increasing from 20% in 2019 to 35%, McKinsey estimates US market to fully recover by the first half of 2021 and to grow by 3-4% in 2019-2021E
- **Europe and Japan lagging behind:** European and Japan beauty markets suffered the most from the restrictions, as they showed the lowest e-commerce penetration compared to other developed countries. As an effect, they are expected to recover their 2019 sales only at the end of 2021.

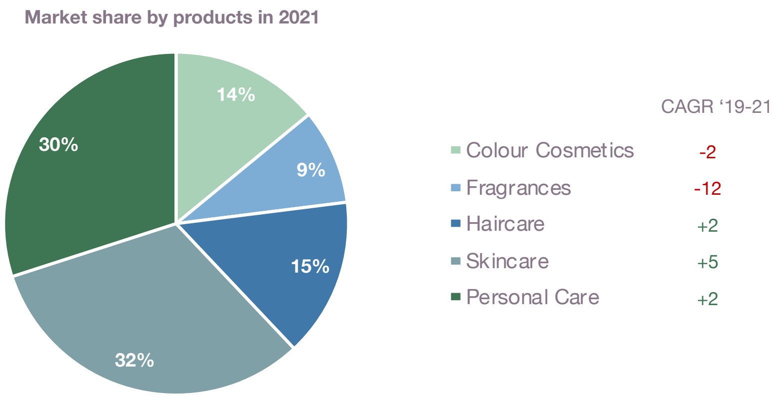
Beauty market size year-on-year performance vs. 2019 (%)



Source: McKinsey – The State of Fashion 2021.

Looking at the industry growth by product, skin care is expected to report the highest growth rate due to the rising demand for skin care products, particularly those with anti-inflammation properties, followed by Haircare and Personal Care products, while interest for Fragrances and make-up and colour cosmetics are expected to reduce also due to the use of masks.

Beauty market in 2021 by segment (%)



Source: McKinsey – The State of Fashion 2021.

Here below we report some forward looking statements released from leading cosmetics companies:

- **Kao Corporation** – according to 2020 results published on February 3, 2021, cosmetics sales decreased by 22% with respect to the previous year, mainly due to a contraction on make-up and other colour cosmetics products. On the earning call, top management confirmed its optimism for cosmetics industry which is seen as the growth driver and their strong commitment towards digitalisation and e-commerce, which recorded a 20% increase YoY.
- **Estee Lauder** – On Feb 5, 2021 Estee Lauder announced Q2 results which reported a 5% increase in sales (+2% on a like-for-like basis), as "the Asian/Pacific region travel retail and global online

net sales growth was partially offset by lower foot traffic in open stores and, to a lesser extent, temporary retail store closures, attributable to Covid-19". Skin care net sales grew across most regions – with great performances by *Estee Lauder, La Mer* and *Clinique* – but lead by mainland China, while Makeup and Fragrance sales decreased also due to the lack of sensorial experiences in person, as it occurred in 1Q. Top management remain confident in the long-term opportunities for global prestige beauty and in the pivotal role of hero products, innovation and online channel and expect double digit top line growth for 3Q (ending March 31, 2021).

- **Shiseido** – On February 9, 2021, during the release of 2020 Result, Shiseido highlighted the remarkable growth in e-commerce, mainly in the Prestige segment (+55% globally), with skin beauty brand to drive the growth. Looking forward, the Company remarked the increasing awareness of healthy skin from customers and its greater focus on skin beauty products as expected to grow at 5-6%% in 2021.

Major news for Arterra partners

Isagro Tender Offer

Isagro is a listed agro-food company, which has been a partner for Arterra – especially in its early start-up phase - and still owns a 16.8% stake.

Back as of March 7th, 2021, **Gowan Company LLC announced the intention to launch a public tender offer** for the whole amount of Isagro shares not held. The transaction values the equity of Isagro at €106.9mn, with a Tender Offer price set at €2.76 per share (ca. 118% M&A premium), corresponding to 0.8x EV/Sale 2020A-21E, 3.2x – 9.8x EV/EBITDA 2020A-21E and 9.1x P/E 2021E. The offer will be **completed within the third quarter of 2021.**

The purpose of the Transaction is the integration of Isagro within Gowan Group, US Group active in developing, marketing and processing agricultural products such as fertilizers, seeds and so on. As for the potential implications of such a deal, this is not clear yet:

- In terms of business **we see no downside risk**, as the two companies have not major commercial agreements, supply contracts or R&D projects;
- In terms of **strategic opportunities**, we believe this will also depend on the strategy of Gowan for its Italian asset, i.e. on Gowan's intention to continue on the *green deal* announced by Isagro back in 2019, when it decided a gradual exit from traditional chemical molecules to bio-solutions and bio-copper;
- In terms of **liquidity** for the Arterra stock, we are not aware of the new shareholder's intention as for Isagro minor holdings, albeit we cannot rule out that they may go for a simplification of the group structure and disposal of peripheral assets, if not considered strategic. This in turn could be seen as a positive as it would materially improve the stock liquidity, driving the free float above 40%.

Intercos Group facing Covid-19 headwinds

We expect Intercos to report a negative top line performance in 2020, mostly due to the negative impact of pandemic on the colour make-up segment. The Italian cosmetic industry – which manufactures ca 55% of the global make-up products – is seen to report a 11.6% decrease in revenues to €10.5bn (according to Cosmetica Italia) and we would expect Intercos, one of the leading players, to perform broadly in line with sector.

The negative momentum and uncertainties linked to recovery post Covid-19 have also halted Intercos' listing project: pending news about the planned listing, financial investor GIC (Singapore) entered the Intercos holdings' capital with an interest corresponding to ca.9% of the operating company.

Arterra direct sales to Intercos were ca. 9% lower than 2019, supported by the skincare line, but affected by a weaker demand of active components for the so-called functional make-up. As for 2021 Intercos has not provided any guidance or indications about expected demand.

A new partner in medical devices

On April 7th, 2021 Arterra announced a **partnership with ADL Farmaceutica** for the production of new medical devices. Albeit the partnership is strategically relevant as it represents **Arterra's first step outside the cosmetic business** (if we exclude R&D activities), the small size of the partner and its limited distribution network, may suggest this agreement will not bring immediate and material boost to Arterra sales, but rather we expect the two companies may develop together new products, leveraging on respective strengths. Arterra may provide ADL a number of services (i.e. not only active principles as raw material), but also IPs and R&D services for example.

New vs old forecasts

Despite the FY2020 results have been very much in line with expectations, we see the **expected recovery unlikely to take place in 2021, at least not at the pace we initially expected**. Also, the diversification process, the launch of new products outside the cosmetic industry as well as the widening of the client base of Vitalab are all proceeding at a pace that is much slower than expected.

Hence, **we assume a slower recovery for 2021-22E** as first half 2021 is still very much affected by reduced international travelling and widespread retail closures or limits, and as social distancing and limited social life persist in most of developed world. Given the persisting low visibility we further cut our estimates of revenues from sales for 2021E and even more for 2022E - by almost 15% and 25% respectively - and we now assume:

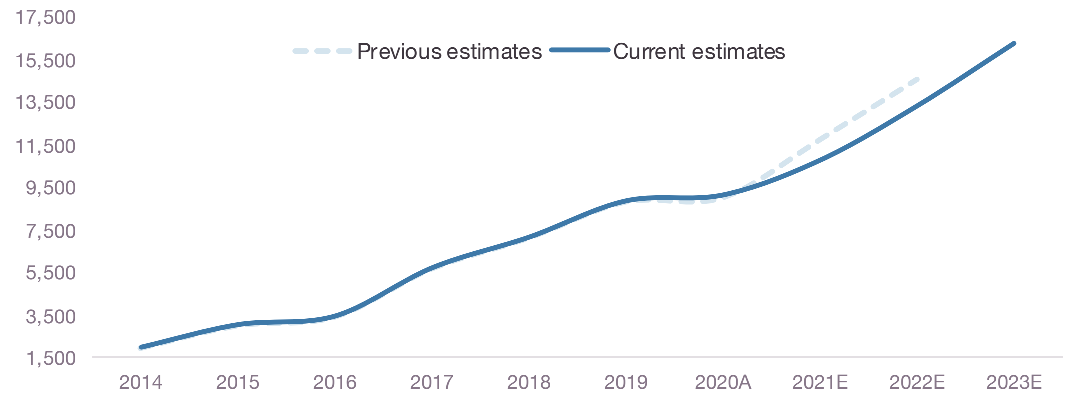
- **Volumes** to grow over 2021E and 2022E at 18-25% respectively. After booming 2020 volumes for Vitalab, we assume still double digit growth in current year and in the next, while we assume still a negative trend in revenues to Intercos in 2021E and a recovery from 2022E;
- **Revenues from Sales** despite the downgrade are still expected to growth at 17% CAGR 20-22E;
- **As for R&D tax credits,** while we expect these revenues to fall relative to 2020, we now expect these to be much higher than previously assumed over 2021E-22E, given the more favourable legislation.

Arterra: 2021E-2022E Top-line drivers

	2020A			2021E			2022E		
€'000	Est.	Actual	Δ(%)	Old	New	Δ(%)	Old	New	Δ(%)
Total Volumes, kg	9,033	9,117	0.9%	12,174	10,773	-11.5%	17,087	13,521	-20.9%
Avg. price €/kg	244	248	1.3%	242	233	-3.7%	241	229	-4.6%
Total Sales	**2,207**	**2,257**	**2.2%**	**2,948**	**2,511**	**-14.8%**	**4,111**	**3,103**	**-24.5%**
Change YoY (%)	2%	4%	--	34%	11%	--	39%	24%	--
Grants & fiscal benefits	756	1,126	49.0%	762	1,043	36.9%	768	849	10.5%
Research contracts	522	540	3.4%	527	550	4.4%	532	556	4.4%
Services	25	25	0.0%	26	26	0.0%	26	26	0.0%
Other (incl. change in inventories)	246	361	47.0%	143	193	35.0%	143	193	35.0%
Total Revenues (VoP)	**3,756**	**4,309**	**14.7%**	**4,405**	**4,323**	**-1.9%**	**5,580**	**4,726**	**-15.3%**
Change YoY (%)	4%	19%	--	17%	0%	--	27%	9%	--

Source: Value Track estimates

Arterra: Volumes sold in cosmetic active ingredients (kg)



Source: Arterra, Value Track Analysis.

- **As for margins**, we believe that the reorganization and efficiency improvements carried during 2020 will bring benefits from 2021 onwards. Lower use of outsourcing services will a) reduce operating cost; b) increase raw materials quality and hence c) permit more efficient production process and improving operating leverage.

In addition, the increased production and R&D capacity and the strengthened headcount with the acquisition of few key people have put Arterra in much better conditions to exploit growth as soon as the international picture normalises post pandemic.

Arterra: New vs Old estimates

	2021E			2022E		
€'000	Old	New	Δ(%)	Old	New	Δ(%)
Total Revenues (VoP)	**4,405**	**4,323**	**-1.9%**	**5,580**	**4,726**	**-15.3%**
EBITDA	1,372	1,637	19.4%	1,961	1,843	-6.0%
EBITDA margin (%)	31.1%	37.9%	6.7%	35.1%	39.0%	3.9%
EBIT	**983**	**1,241**	**26.3%**	**1,551**	**1,453**	**-6.3%**
EBIT margin (%)	22.3%	28.7%	6.4%	27.8%	30.7%	3.0%
Net Profit	956	1,102	15.3%	1,358	1,195	-12.0%
Adjusted Net Profit	**1,066**	**1,212**	**13.7%**	**1,468**	**1,305**	**-11.1%**
OpFCF b.t.	604	1,518	151.4%	964	1,730	79.5%
Net Cash Position	**5,003**	**5,483**	**9.6%**	**5,775**	**6,956**	**20.4%**

Source: Value Track (estimates)

Overall, we foresee

- Total **Revenues** to grow at **8% CAGR 2020-23E**, supported by increasing Sales revenues, expected to grow at 19% CAGR 2020-23E;
- **EBITDA margin to reach 39%** level by the end of 2023E thanks to current excess production capacity which would generate its benefits as long as volumes increase;
- **Net profit** to mirror EBITDA growth and to reach **€1.5mn by the end of 2023E.**

Arterra: P&L 2020A-23E

€'000	2020A	2021E	2022E	2023E
Total Revenues	**4,309**	**4,323**	**4,726**	**5,449**
Change YoY (%)	19%	0%	9%	15%
OPEX	1,838	1,838	1,838	1,838
EBITDA	**1,602**	**1,637**	**1,843**	**2,124**
EBITDA margin (%)	37.2%	37.9%	39.0%	39.0%
Depreciation & Amortization	-400	-397	-390	-391
EBIT	**1,202**	**1,241**	**1,453**	**1,733**
EBIT Adj.	1,357	1,396	1,608	1,888
EBIT margin Adj. (%)	31.5%	32.3%	34.0%	34.6%
Net Financial Charges	-158	-151	-146	10
Pre-tax Profit	**1,199**	**1,244**	**1,461**	**1,897**
Taxes	-91	-142	-266	-418
Net Profit	**1,109**	**1,102**	**1,195**	**1,480**
Adjusted Net Profit	**1,219**	**1,212**	**1,305**	**1,590**

Source: Arterra (historical figures), Value Track (estimates)

At Balance Sheet / Cashflow level, we foresee Arterra to generate ca. €4.7mn cumulated OpFCF between 2021E-23E, with Net Cash Position reaching €7.8mn by the end of forecasted period. More in details, we see:

- **Net Fixed Assets** to progressively decrease from €2.4mn in 2020 to €2.2mn by 2023E as the investments completed over the last year equipped the company with enough production capacity to face the expected rising demand without requiring material investments;
- **Net Working Capital** to expand in absolute terms, following company business growth, but decreasing as percentage of revenues from peak 51% witnessed in 2020 to 44% in 2023E (these levels compare to average 50% of NWC/Revenues over 2018-2019 which we see as not sustainable as a) inventories at the time were extremely low production was under pressure and b) increasing revenues from R&D tax credits bring risk of longer payment terms;
- **Net Financial Position** to grow by ca.€1-1.4mn per year and to move from €4.0mn as of Dec. 2020 to €7.8mn by 2023E, assuming return to dividend only in year 2023 (on 2022E earnings) as well as some cash in of dividends from Vitalab (again from 2023E).

Arterra: Balance Sheet figures 2020A-2023E

€'000	2020A	2021E	2022E	2023E
Net Working Capital	2,218	2,121	1,946	2,423
Net Fixed Assets	2,419	2,330	2,254	2,177
Provisions	522	613	640	705
Total Capital Employed	**4,115**	**3,838**	**3,560**	**3,894**
Group Net Equity	**8,181**	**9,321**	**10,516**	**11,669**
Net fin. Position [i.e. Net debt(-) cash (+)]	**4,066**	**5,483**	**6,956**	**7,775**

Source: Arterra (historical figures), Value Track (estimates)

Arterra: 2020 – 2023E Cash Flow analysis

€'000	2020A	2021E	2022E	2023E
EBITDA	**1,602**	**1,637**	**1,843**	**2,124**
Op. WC requirements	-1,048	97	175	-477
Capex	-438	-308	-314	-313
Change in Provisions	18	91	26	65
OpFCF b.t.	**134**	**1,518**	**1,730**	**1,399**
Cash Taxes	-91	-142	-266	-418
Net Financial Charges	-2	3	8	13
Capital Injections (gross)	0	0	0	0
Dividends paid	0	0	0	-326
Others and dividend from Vitalab	18	38	0	151
Change in Net Fin. Position	**59**	**1,417**	**1,472**	**820**

Source: Arterra (historical figures), Value Track (estimates)

In the above forecasts **we do not factor any major M&A, partnership or diversification** move and, as for the agreement just announced with ADL, our updated model incorporates negligible revenues over the forecast horizon: virtually zero for 2021, €50k for 2022E and €150k for 2023E, with margins aligned to the cosmetic business - supported by the fact that these revenues will come from a mix of sales of active ingredients and royalties (revenues sharing).

This is for the time being and pending more details by the company. In short at this point we have virtually no revenues streams from diversification until 2024, as compared to initial projections pre Covid-19, all diversification plans have been postponed by two years.

On the other hand the solid financial situation (Net Cash in excess of €5mn in 2021E) and visible FCF (€1.2-1.4 per year) provide management a **very good flexibility to exploit future opportunities**.

Valuation

At current €3.66 stock market price, Arterra trades at 3.4x/2.8x EV/Sales multiples based on our 2021/2022 estimates, implying a material discount to all peers considered.

Based on our revised estimates, updated sector ratings and following a set of reassuring FY2020 results, **we increase our fair value per share to €5.3** - as the average of our DCF's model and peers' multiple relative valuation - up 26% from our previous €4.2. At fair value, stock would trade at 5.9 EV/Sales 21E, 15.7x EV/EBITDA and 29.0x P/E for 2021E, implying an 27% discount on EV/EBITDA vs larger peers (i.e. those with positive margins) and 30% discount on EV/Sales vs all peers.

Discounted Cash Flow

We rerun our DCF model which gives a fair value of €5.1 per share due to a lower WACC (driven by lower ERP) and estimates revision.

It is worthy that our model assumes a net cash position over the entire considered period and, consequently, may factor only in part the Company's full potential which can be unlocked with further business development and diversification. Here below our key assumptions:

- **Arterra has a 24.99% stake in Vitalab** and **an option to take over** an additional 15.01% (overall potential holding: 40%). In our model we consider both the 24.99% stake and the option as peripheral assets, valued in line with the whole business;
- **Net Cash Position in the projected 2021E-29E period**. Therefore, **WACC** and Cost of Equity coincide throughout the model time horizon, with an estimated value of 10.9%;
- **December 2021E as reference point for valuation,** explicit projections into 2029E and terminal value at 2029E obtained **applying a 2.5% Perpetuity Growth Rate (PGR).**

Arterra: WACC calculation

Risk free	2.0%
Risk Premium (Damodaran, Jan 2021)	6.9%
Credit spread	2.5%
Beta Unlevered (Damodaran; avg of Biotechnology Drugs, Specialty Chemicals, Healthcare Products)	0.9
Small Cap Risk Premium	2.0%
Cost of Equity = WACC	**10.9%**

Source: Value Track Analysis

Arterra: DCF model outcome

	€ '000
PV of future Cash flow FY 2022E-28E	6,542
PV of Terminal Value with PGR at 2.5%	18,126
Enterprise Value	**24,668**
Implied EV/EBITDA 21E	15.1
Peripheral assets: Vitalab stake and option	3,621
Net Cash Position 2021YE	5,483
Equity Value	**33,772**
Shares (mn)	6.5
Equity Value p. s. (€)	**5.16**

Source: Value Track Analysis

Arterra: DCF Sensitivity Analysis - Equity Value (€ per share)

		Perpetuity Growth Rate				
		1.50%	2.00%	2.50%	3.00%	3.50%
WACC	11.9%	4.4	4.6	4.8	5.0	5.3
	11.4%	4.6	4.7	4.9	5.2	5.4
	10.9%	4.7	4.9	**5.1**	5.3	5.6
	10.4%	4.8	5.0	5.2	5.4	5.7
	9.9%	4.9	5.1	5.3	5.6	5.9

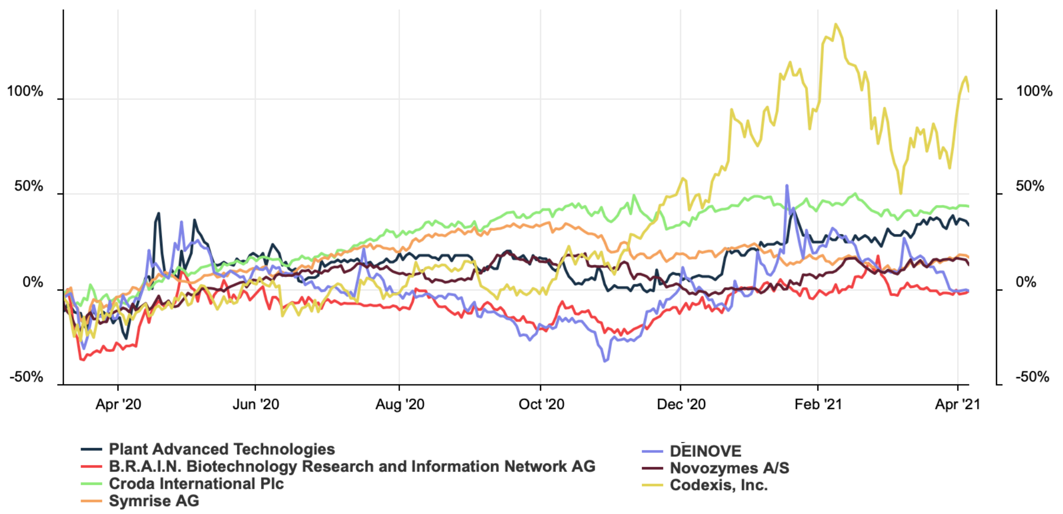
Source: Value Track Analysis

Peers Analysis

Being some of selected peers relatively young and loss-making companies, we reiterate EV/Sales as the most appropriate multiple for the relative valuation: at current stock price, Arterra trades at material discount vs the selected European middle-size players. However, it is worthy to note that all peers reported rising multiples from our previous update and due to:

- Downward estimates revision for most of selected peers, more pronounced on smaller companies;
- Rebounding stock prices which now embed positive news flow from vaccination campaign and account for a certain level of optimism about the economic recovery.

Arterra: peers 9 March 2020 – 07 April 2021



Source: Arterra, Value Track Analysis.

As an effect, all peers' trading multiples have risen up, albeit spread out on a wide range of 4.0x – 16x of EV/Sales (excluding Deinove), with smaller peers now trading at very expensive multiples. Deinove, the smallest peer, trades at out-of-range and likely not meaningful EV/Sales multiples and thus we report its ratings below, but do not include them in the fair multiple calculation.

Peers' Analysis: EV/Sales 2021-22E summary table

EV / Sales (x)	2021E	2022E
Brain	4.5	4.0
Croda	6.1	5.8
Symrise	4.2	3.9
PAT	16.0	7.1
Deinove	38.9	25.9
Fermentalg	16.0	7.3
Novozymes	8.3	7.9
Codexis	16.3	13.9
Median (*)	**8.3**	**7.2**
Arterra	**3.6**	**3.0**

Source: Value Track Analysis (*) Excl. Deinove as multiples not meaningful

Given Arterra's size and still relevant execution risk on business growth and diversification opportunities, we apply a 25% discount to peers' Median and obtain a **6.2x 2021E EV/Sales fair multiple**. This implies a **€27mn Enterprise Value and €5.5 fair equity value per share**, which includes the €5.5mn Net Cash at the end of 2021E and a value of €3.6mn for Arterra's stake in Vitalab.

Peers' Analysis: EV/Sales Valuation

	€mn
Arterra Sales 2021E	4.3
EV/Sales multiple (x)	6.2
Arterra EV	**26.9**
Peripheral assets: Vitalab (incl. option)	3.5
Net Cash Position 2021E	5.5
Equity Value	**35.9**
Equity Value p.s. (€)	**5.5**

Source: Value Track Analysis

Scale-up peers valuation

Given wide range of trading multiples, we believe Enterprise Value in absolute terms can provide a useful indication too. In the table below we report main metrics used and outcome.

Arterra: Absolute valuations of smaller peers

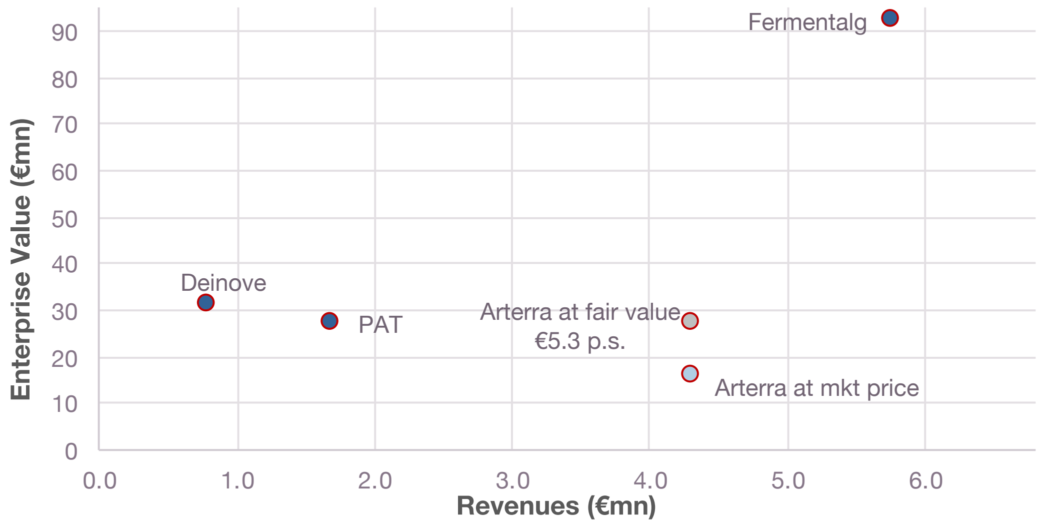
(€mn)	Mkt Cap	Net Debt 21 & adj.(*)	EV	Revenues 2021
PAT	24.3	2.9	27.2	1.7
Deinove	16.2	14.9	31.1	0.8
Fermentalg	74.3	17.8	92.1	5.8
Average			**50.1**	**2.8**
Arterra at mkt price	**26.4**	**-8.7**	**17.8**	**4.3**
Arterra at fair value	**35.6**	**-8.7**	**26.9**	**4.3**

Source: Value Track Analysis (*) The stake in Vitalab is valued at book

We note a positive correlation between Enterprise Value and Total Revenues among smaller peers, i.e. revenues below €2mn corresponding to €27mn – 31mn EV, hence

- at current market price (€3.8 p.s.) Arterra reports a €16 EV which we believe not to factor the ca. €4.3mn Revenues for 2021E and suggests a material discount to selected peers;
- at €5.3 fair equity value per share, Arterra would still show a total enterprise value close to Deinove and PAT peers, despite its larger size.

Arterra: Enterprise Value vs Revenues 2021E



Source: Arterra, Value Track Analysis.

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