

Transition to new strategy on track

20 June 2019

ADAM's FY18 figures do not fully convey the successful efforts of the investment manager in restructuring the inherited portfolio. The latter is now far more coherent than it was 18 months ago, divided between stable, non-strategic assets held for sale and recently made, income-generating investments. Two attractive transactions were completed post the year-end and future reports should consequently reflect a more diversified income-focused investment strategy.

As the results predate these recent investments, they mainly reflect continued restructuring of the legacy portfolio during calendar 2018.

Valuation: shares at 54% discount to end FY18 NAV/share

NAV/share at the year-end was US\$1.13. That is significantly above the current share price, which reflects historic underperformance by the previous investment manager, uncertainty over the timing and financial scale of exits and the illiquidity of ADAM's shares.

Management expects newsflow to help deal with these issues over the next 18 months, while it plans other initiatives to help attract and build a wider shareholder base and ideally, build its equity base to finance portfolio growth.

Exiting legacy assets, reinvesting in diversified portfolio

Since its appointment as ADAM's new Investment Manager just over two years ago, Harmony Capital Investors Limited ("Harmony Capital") has restructured and stabilised the legacy portfolio, secured two new investments and built a pipeline of new potential investments across sectors that fit its revised investment policy.

The latter's focus is SME 'special situations' in Asia i.e. companies which seek growth capital but are unsuitable or too complex for traditional financing methods available in their local markets. ADAM's competitive advantages and bargaining power are derived from local networks, an experienced investment manager with a successful track record of deploying capital across Asia and the acute shortage of traditional sources of finance to many borrowers in its target Asian markets.

ADAM's remaining legacy assets are non-strategic and being readied for potential exit. The proceeds will be reinvested in a diversified portfolio of (a) established, revenue-generating companies, (b) industries strategically placed to capitalise upon major demographic trends and (c) high-growth economies throughout Asia. ADAM plans to leverage its competitive positioning to build a portfolio that supports progressive income distributions and capital gains to shareholders.

A new investment completed in FY18 and two further deals announced post the year-end illustrate the template. ADAM has a healthy pipeline of similar opportunities, which will enable it to continue to grow its portfolio, subject to securing access to capital from asset sales and new equity.

Company Data

EPIC	ADAM
Price (last close)	52c
52 week Hi/Lo	61c/44c
Market cap	US\$46m
Year-end NAV/ share	113c

Share Price, \$



Source: ADVFN

Description

Adamas Finance Asia (ADAM) aims to be the leading London-quoted pan-Asian focused diversified SME investment holding vehicle. It targets above average income and capital growth, with a stated objective to provide shareholders with unique access to a diversified portfolio with access to high-growth Asian economies.

ADAM appointed a new Investment Manager, Harmony Capital Investors Limited ("Harmony Capital"), in May 2017. Harmony Capital has a dedicated Asian focus and its staff are based in London, Hong Kong and Singapore.

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FY18 results: transition well underway

ADAM's results for the 12 months ended 31 December 2018 reflect activities at a relatively early stage in the transition to a new investment strategy under the direction of Harmony Capital, which was only appointed in 2017.

Harmony Capital has since focused its efforts on initially re-positioning the inherited portfolio, readying assets for exit and redirecting capital raised into a pipeline of new investments that fit its revised strategy. The latter concentrates on income generating assets and a diversified, pan-Asian profile, quite distinct from the prior primary focus on mainland China.

Valuation

Net Asset Value at end December 2018 was stable at US\$93.0m (FY17 US\$93.6m), equivalent to 113c/share, materially above the current share price.

The marginal NAV decline during the period reflects a US\$3.5m net operating loss (FY17: US\$11.7m net profit) offset by a US\$3.1m increase in the fair value of the holding in Hong Kong Mining Holdings (HKMH). ADAM increased its stake from 79% to 85% via its participation in a March 2018 share issue.

The portfolio at the year-end was as follows:

Principal Assets			
US\$m	Effective Interest	Instrument type	Valuation as at 31 Dec 2018
Fook Lam Moon Holdings		Convertible Bond	26.5
Hong Kong Mining Holdings Limited	84.8%	Structured Equity	42.5
Meize Energy Industrial Holdings Ltd	7.9%	Redeemable conv. pref. shs	8.2
DocDoc Pte Ltd		Convertible Bond	2.1
GCCF/Other			4.9
Cash			8.8
Total Net Asset Value			93.0

Source: Company

HKMH is the largest component of the year-end portfolio, c. 46% of net assets, which make its success pivotal to ADAM's equity valuation. ADAM indicated that it expects to be able to provide more clarity regarding this stake later this year, confirming that mine operations at the HKMH site should hopefully be back in production during the second half of 2019. During FY2018, ADAM appointed key management personal and staff who have been tasked with the restarting of operations at the mine. To facilitate the re-commencing of operations, ADAM committed up to US\$2.0 million in funds. Management have also stated that it is their intention to provide regular updates to the market regarding HKMH.

The shares currently sit at a 54% discount to NAV. That reflects, inter alia, the perceived uncertainty regarding the timing and proceeds upon exit from remaining legacy assets, but also the lack of liquidity currently available in ADAM shares.

Management regards investor communications as a pivotal component of its strategy, and improved equity liquidity and a broader shareholder base as crucial if it is to access the capital it requires to finance growth. It plans various initiatives to improve ADAM's profile with its prospective investor base.

ADAM also commenced a US\$0.5m share buyback programme in February and has extended the trading of its shares to 12 of the most popular online trading platforms in the UK. Management have also presented at various investor events to increase engagement with shareholders and investors.

Asset sales and acquisitions

ADAM's most recent investments fit its investment mandate, providing immediate attractive income. That reaffirms potential for dividends and capital growth over the medium term.

We also regard the terms agreed as confirmation of management's view regarding the acute shortage of traditional sources of finance to many borrowers in its target Asian markets. That provides it with a competitive advantage and bargaining power, and ADAM's shareholders with exposure to niche deals not normally available to European investors.

Harmony Capital's local network sources its deals and carries out detailed due diligence in conjunction with professional external advisers. So far, ADAM has provided the financing required from its existing cash resources.

Legacy sales: CPE Portfolio switched for Hong Kong assets

The sale of the CPE portfolio, principally comprising China-based private equity assets, was completed in November 2018. ADAM replaced these with an interest-bearing convertible bond issued by Fook Lam Moon Holdings (FLMH), a long-established owner of high-end restaurants in Hong Kong.

The current portfolio is shown below:

Portfolio overview

Hong Kong Mining Holdings Limited

HKMH is a natural resources company. Its primary asset is a large dolomite magnesium limestone mine in the province of Shanxi, China. HKMH expects to restart operations later this year. Workers are active on the mining site and key management personnel have been appointed. ADAM will consider all viable options to monetise this investment once operations have recommenced.

DocDoc Pte Ltd.

Singapore-headquartered online network comprising over 23,000 doctors, 600 clinics and 100 hospitals that serve a wide array of specialties. It uses artificial intelligence, cutting-edge clinical informatics and proprietary data to connect patients and doctors at an affordable price. It has partnership agreements with some of Asia's largest insurers such as the Ping An Group and Prudential Singapore.

Fook Lam Moon Holdings

Prominent Cantonese restaurant chain with over 70 years operation in Hong Kong and one location in Macau. Its eateries have been by prestigious award bodies such as San Pellegrino and Wine Spectator, and its Wan Chai and Kowloon locations and its Guo Fu Lou restaurant hold Michelin stars.

Meize Energy Industries Holdings Limited

Privately owned designer and manufacturer of blades for wind turbines. It built its order book during the year against a challenging backdrop. ADAM intends to realise this asset.

Source: Company

Post year end additions to the portfolio

So far this year ADAM has completed two new investments which meets its strategy to create a diversified portfolio of pan-Asian SME assets, build income to support distributions to shareholders and secure medium-term capital growth potential. These are outlined below.

We have covered the two investments in more detail in research updates published in December 2018 and January 2019.

Investment and structure

<p>Infinity Capital Group, Niseko Ski Resort Hokkaido, Japan</p> <p><i>Senior secured loan note</i></p>	<p>ADAM has agreed to finance the development of a premium residential project in Hirafu Village, located in the Niseko Ski Resort in Hokkaido, Japan. This resort is popular with wealthy Asian tourists, particularly from mainland China.</p> <p>This investment comprises a US\$4m senior secured loan note, fully secured by other ICG assets in Niseko. The coupon is 17.5% pa, payable in cash. ADAM also received detachable warrants that give it the right to subscribe for up to US\$4m of equity in ICG or its parent company, if either decides to undertake a liquidity event, such as an IPO.</p>
<p>PharmaJet Inc. Convertible bond</p> <p><i>Convertible bond</i></p>	<p>PharmaJet Inc. has developed innovative needle-free injectors which have received US FDA marketing clearance, CE Mark and WHO PQS certification to deliver medications and vaccines. It has established partnerships which will enable it to market and distribute its devices in over 120 markets worldwide.</p> <p>PharmaJet seeks to raise between US\$12-20m for business expansion, particularly within Asia and to move it towards a potential IPO. ADAM is the lead investor and subscribed up to US\$5m in a convertible bond and agreed a non-binding term sheet, subject to final legal documentation.</p> <p>The convertible bond has a four-year maturity and a 10% pa coupon (6% cash, 4% Payment-in-Kind). It will be drawn in tranches, the first subject to satisfaction of certain conditions including completion of legal due diligence and execution of legally binding documentation.</p> <p>Once issued, the bond will be convertible at the holders' discretion at a 40% discount to a pre-money valuation established by any 'liquidity' event which would include an IPO. PharmaJet is contemplating an IPO in Singapore and/or the NASDAQ in due course, subject to market conditions.</p> <p>This investment, in addition to DocDoc, will provide ADAM with participation in the healthcare sector via products with global reach and high relevance to Asian markets.</p>

Source: Company

Prospects

The investment manager intends to continue to leverage its proprietary deal-sourcing network to unearth high-potential SMEs with an Asian nexus to build a portfolio that is representative of the region.

Results

Summary income statement		
Year to 31 Dec, US\$'000s	2017	2018
Realised (loss)/gain on disposal of investments	(14,329)	(4)
Fair value changes on financial assets at fair value through profit or loss	33,885	216
Loan written off	0	0
Administrative expenses	(7,958)	(3,861)
Operating gain/(loss)	11,598	(3,649)
Finance income	82	148
Finance expense	0	0
Dividend income	0	0
Other income	14	0
Profit/(Loss) before taxation	11,694	(3,501)
Taxation	0	0
Profit/(Loss) for the year	11,694	(3,501)
Other comprehensive income:		
Items that will or may be reclassified to profit or loss:		
Exchange differences arising on translation of foreign operations		
Total comprehensive income/(expense) for the year	11,694	(3,501)
<u>Profit/(Loss) per share</u>		
Basic	15.23c	(4.36c)
Diluted	14.96c	(4.36c)

Source: ADAM FY18 results



Investor Access

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