

Omni Bridgeway Limited

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Issuer Outline

Omni Bridgeway Limited (OBL) (formerly IMF Bentham Limited [IMF], but assuming the name of Omni Bridgeway Limited after a merger with the namesake in late-2019) was established in 2001 and is the largest litigation funder in Australia and the first to be listed on the Australian Securities Exchange (ASX code: OBL).

OBL is an investor in and manager of funds that invest in litigation dispute resolution assets. Its principal activities are the investigation, management and funding of litigation claims. OBL does not provide legal advice. The key business driver is to manage and fund the litigation to a successful conclusion. Although OBL's business began in Australia, OBL offers its services in other jurisdictions, including the US, Canada, Europe, New Zealand and Asia. OBL offers funding for commercial litigation, insolvency cases, class actions and arbitration cases.

OBL's investor clients include large sophisticated international hedge funds; insurance groups, family office and pension/endowment organisations; the litigation financed clients include multinational corporations, ASX-listed companies, small- and medium-sized enterprises, individuals and insolvency practitioners.

Security
AUD72m 5.65% Jan 2026

ISIN
AU3CB0269397

Currency
AUD

Type
Senior Secured

Key Financials (AUDm)*

LTM (31 Dec)	2020
Income	119.0
EBITDA	4.1
NPAT	(133.6)
Cash & Equivalents	167.9
Intangible Assets**	525.8
Debt	143.8
Debt / Current Resources	98%

Source: Company, FIIG Securities

* Consolidated accounts

**Intangible assets are litigation cases in progress

Key Terms

Coupon Type	Fixed	Minimum Amount	AUD10,000
Rate	5.65%	Denomination	AUD1,000
Frequency	Quarterly	Issuer Credit Rating	Not Rated
Domicile	Australia	Issue Credit Rating	Not Rated
Amount Issued/Outstanding	AUD72m/AUD72m	AU Withholding Tax Exempt	Yes

Key Dates

Issue Date	20 December 2019	Maturity Date	8 January 2026
Call Dates	8 January 2022 @ 102%, 8 January 2023 @ 101.5, 8 January 2024 @ 101 and at par anytime within the last six months prior to maturity		

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Strengths

- **Market leader and a successful track record:** OBL has been operating in various forms since 2001 and is a market leader in litigation funding. It has the longest operating history and track record of any litigation funder in Australia and globally. It has a demonstrated history of maintaining a strong portfolio and performance. OBL's legacy IMF Bentham operations (which still account for the majority of cases and revenues for the consolidated operations) has reported a 89% success rate (dating back to 2001), generating AUD3.1bn in revenues and a return on invested capital of 128%.
- **OBL has a strong investment portfolio:** As at 30 June 2020, OBL's case portfolio--comprising 277 funded cases--stood at AUD13.5bn of estimated claim value. Total cases including conditional funded and approved but not yet funded stood at 304 with an estimated claim value of AUD15.8bn. OBL has historically achieved gross revenue of 15% across its investments. Funding applications, a measure of demand for OBL's services, increased by 33% during the full year.
- **OBL continues to diversify its portfolio:** OBL continues to diversify its portfolio over time by increasing the number (of smaller size) and variety of cases it funds. At the same time, OBL has moved away from funding investment cases on balance sheet, instead relying on the stable of funds it has launched over the past three years. In our view, this broad strategy is aimed at de-risking OBL's investment portfolio, as off-balance sheet funding is non-recourse. This also diversifies OBL's risks via a larger investment portfolio, while reducing its exposure to large, idiosyncratic risks. The strategy should also smooth out some of the 'lumpiness' seen in OBL's recent financial performance and provide a smoother earnings profile going forward, in part from management fees that OBL will earn over time, as well as the structure of certain funds whereby OBL will earn returns on capital deployed concurrently with returns paid to the third party investors.
- **OBL has a strong balance sheet and is in a net cash position:** The consolidated operations of OBL held cash of AUD167.9m against AUD143.8m of total debt as at 31 December 2020. The AUD72m 5.65% Jan 2026 senior secured notes (Notes) are secured by the assets of the parent entity and have the benefit from guarantees from certain OBL wholly-owned subsidiaries.

The abridged parent entity accounts are disclosed in the audited annual report as detailed below:

Omni Bridgeway Ltd. Summary Balance Sheet (AUD'000)	FY17	FY18	FY19	FY20
Current assets	180,789	147,673	151,920	201,473
Total assets	356,326	372,511	453,535	564,818
Current liabilities	(39,897)	(72,233)	(103,995)	(21,524)
Total liabilities	(178,501)	(156,552)	(179,262)	(165,826)
Net assets	177,825	215,959	274,273	398,992
Issued capital	123,654	127,630	204,553	345,548
Retained earnings	40,975	68,165	46,190	25,449
Reserves	13,196	20,164	23,530	27,995
Total shareholders' equity	177,825	215,959	273,273	398,992
Profit or loss of the Parent	23,104	39,261	(20,476)	(13,315)
Total comprehensive income of the Parent	23,104	39,261	(20,476)	(13,315)

Source: Company reports

- **Risk management:** Risk management processes are key to OBL's strong track record and include case selection, investment committee review and ongoing case management. Nothing material has changed in the risk management process since OBL's inception, which has resulted in a 89% success rate on a large number of cases (excluding withdrawals).

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Case selection must meet minimum legal, factual and commercial criteria before a recommendation is made to the investment committee. A rigorous investment committee process has been established to challenge legal and factual issues by an internal group comprising of experienced litigators and commercial staff. Case management is undertaken by experienced investment managers (former legal practitioners and counsel).

- **Strong management & governance:** OBL's senior management and board is a key strength of the business, recognising that the company's ongoing success will be contingent on the continued rigour in case selection and ongoing management. Members of OBL's senior management and its investment committee have been associated with the company for a significant period of time (seven years on average for board members and over 10 years for investment committee members). We view this long tenure as supportive given the highly technical and complex nature of IMF's business, hence this continuity provides for the maintenance of a long corporate history. We also believe that senior management (and the board) has significant expertise and experience in the fields that are relevant to IMF.
- **The litigation funding sector is relatively uncorrelated to general economic conditions:** Litigation funding is a niche sector with financial performance that is relatively uncorrelated to general economic conditions. Arguably it provides a natural hedge to weaker economic activity in that we would expect a larger number of cases related to insolvency if economic activity deteriorates.
- **Covenants:** The Notes benefit from a range of protections, such as security over all assets of the parent entity of OBL and guarantees provided by certain OBL wholly-owned subsidiaries. It should be noted that the guarantees are provided on an unsecured basis, i.e. these entities are not pledging their own assets to support the guarantees and the Notes, noting that the subsidiaries have agreed not to pledge their assets to other lenders. In addition, the Notes are benefiting from an incurrence covenant (i.e. tested when new debt is raised) requiring OBL to maintain current resources at least equal to 75% of the group's debt. Current resources encapsulate cash, cash equivalents, fixed term investments and receivables.
- **Demonstrated access to debt and equity market:** In recent years, OBL has demonstrated its financial flexibility by raising both equity and debt (listed and unlisted). Bank funding is largely closed to OBL, as it is regularly funding actions against the banks.

Risks

- **Revenues and cashflows can be unpredictable:** OBL's revenues and expenses are directly related to the outcomes of the cases that it funds. The cases often span many years and hence timing of profitability can be unpredictable. OBL's future financial performance depends on a number of controllable factors (such as case selection and risk management) and a number of uncontrollable factors (such as timing of settlements, court decisions and appeals processes). Under accounting standards, OBL is also required to defer recognition of income until recovery is certain. As such, OBL's periodic earnings may display significant volatility relative to a standard corporate business. A weak period of earnings may not necessarily be a cause for concern in itself, for the reasons outlined above; however a consistent stretch of poor earnings performance would be of greater concern.

For example, revenue in FY19 was AUD5.7m. In FY20, revenue was ~AUD278m, with a further AUD80m pending from cases completed prior to 30 June 2020. This dropped in 1H21 to AUD16.1m due to low case completion (and a weak EBITDA for the period due to an adverse decision on the Westgem case which led to OBL recording a large non-cash impairment which would be reversed if OBL's appeal is successful).

- **Unfavourable outcomes for balance sheet cases:** While OBL has moved to an off balance sheet model which limits its risks to the amount of capital committed to each fund, OBL continues to manage legacy cases that were funded on balance sheet. In particular, OBL has two historical cases (Wivenhoe and Westgem) which the Company has flagged that any negative outcome would have a material adverse impact on the group's profit & loss and cash position.

While Wivenhoe was recently declared in favour of OBL, it remains subject to appeal. Westgem was recently dismissed, although OBL has since appealed. Indicatively, the company has estimated the actual cash impact of an ultimate lost could be in the region of AUD10m, reflecting an adverse cost claim.

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- **Risks specific to OBL legacy cases:** These include poor case selection, continuing in unsuccessful cases (i.e. not withdrawing and incurring additional loss), time and expense, inability of defendants to pay judgements, lost cases and changes in the law. We also note OBL's success depends substantially on its executive directors, senior management and key personnel.
- **Adverse costs:** In certain jurisdictions such as Australia, OBL may be liable for adverse costs to the successful party in respect of costs incurred during the period of funding for unsuccessful cases. In general terms, an award of adverse costs to a defendant will approximate to 40%-70% of the amount paid by the plaintiff to pursue the litigation (although in some cases there may be more than one defendant which could lead to a higher percentage).
- **Risks associated with aggressive growth in offshore locations:** OBL has been aggressively growing its portfolio, particularly into the US market. OBL has agreed to fund cases offshore in the US, Singapore and Hong Kong and is likely to target significant growth in Europe after the merger with the then Omni Bridgeway). OBL may agree to fund other cases in these and other jurisdictions. The selection and management of such cases can be more difficult than the selection and management of Australian cases and any mismanagement may cause loss to OBL. In addition, OBL has less of an established track record in jurisdictions outside of Australia and there is no guarantee OBL can continue to sustain its strong track record of performance in other jurisdictions.
- **Risks associated with joint ventures:** There can be no assurance that any joint venture arrangements will be successful. OBL may be unable to control the actions of its joint venture partners and therefore cannot guarantee that the joint venture arrangements will be operated or managed in accordance with OBL's preferred direction or strategy. Joint venture partners may default on their obligations or the joint venture arrangement may be terminated in circumstances outside the control of OBL, either of which may have a materially adverse impact on the value of OBL's interest in the joint venture arrangement. In addition, OBL may not be able to fulfil its obligations under the applicable joint venture arrangements which may result in a joint venture partner being able to compulsorily purchase OBL's interests in the applicable joint venture arrangement.
- **Currency risk:** The value of OBL's investment portfolio and associated potential revenues may decrease with a strengthening Australian dollar, given the increased weighting of the portfolio towards overseas funded matters. OBL does not enter into foreign currency arrangements given the difficulty with forecasting cashflows, and its key foreign currency exposure is to US dollars given the growing US investment portfolio. Increased growth internationally will also lead to an increasing unhedged foreign currency exposure, which adds to the uncertainty when forecasting cashflows.
- **Potential changes to regulation of the litigation funding industry:** The Australian Law Reform Commission (ALRC)'s Inquiry into Class Action Proceedings and Third-Party Litigation Funders was recently completed. The aim of the inquiry was to ensure that the costs of class actions are 'appropriate and proportionate and that the interests of plaintiffs and class members are protected'. A final report with recommendations was published in late 2018. A response from the government generally follows in due course, although the length of time for response can be lengthy (one review completed in 2010 is still waiting a government response).

Along broadly similar lines, a High Court decision in late-2019 determined that courts do not have the power to make common fund orders (a common fund order requires all potential members of a class action group to pay a shared commission to litigation funders from the proceeds of the claim).

- **OBL can incur further secured indebtedness:** OBL may issue further notes and may incur further secured indebtedness, which may include, without limitation, debt instruments on similar terms to the Notes, which will rank equally with the Notes. The issue of further secured indebtedness by OBL may have the effect of reducing the amount that Noteholders would receive on a winding up and may have an adverse effect on the market price or liquidity of the Notes.

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Other Risks

- **Call risk:** A decision to call the bonds ahead of the maturity date depends on a number of factors, including the relative cost of entering new debt financing, the company's liquidity position, and the availability and attractiveness of new funding opportunities at the call date.
- **Duration risk:** The OBL AUD 5.65% senior secured notes mature in January 2026 and carry a modest level of duration risk.
- **Interest deferral/cancellation:** Not applicable
- **Non-viability trigger:** Not applicable

Summary

Omni Bridgeway Limited is the largest litigation funder in Australia. Its principal activities are the investigation, management and funding of litigation claims (pre- and post-judgment). The OBL AUD72m 5.65% senior secured notes maturing in January 2026 offer investors a fixed, high yield local currency exposure whose performance is relatively uncorrelated to general economic conditions. Although revenues and cashflows can be unpredictable and subject to externalities outside of the control of the company, the shift toward off-balance sheet funding of litigation claims with no recourse should improve the predictability of earnings over time.

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Financials

The financial summary below represents the consolidated operations of Omni Bridgeway Limited.

FYE 30 June (AUDm)	FY18	FY19	FY20
Profit and loss			
Income	23.1	5.7	157.4
Corporate costs	(30.8)	(52.6)	(91.4)
EBITDA	(7.7)	(46.9)	66.0
Depreciation expense	(0.6)	(0.7)	(17.4)
Finance Costs	(0.1)	(0.1)	(1.3)
Net profit before tax	(8.4)	(47.7)	33.5
Net profit after tax	(7.8)	(36.1)	17.6
Balance Sheet			
Cash	160.2	226.5	194.4
Intangible assets (cases in progress)	321.3	427.0	627.9
Debt	120.5	144.0	143.8
Cashflow Statement			
Cashflows (cases won)	94.9	43.2	171.0
Investment in new cases	(113.4)	(123.7)	(214.2)
Other costs	(63.6)	(36.8)	(50.9)
3rd party fund investment	114.9	121.8	69.1
3rd party fund return	(9.7)	(28.3)	(64.1)
Other inflows / outflows	(5.0)	(9.6)	(1.8)
Net cash flows	18.0	(33.3)	(91.0)
Debt issuance	-	23.0	(2.2)
Share issuance	-	73.9	132.2
Acquisition	-	-	(31.9)
Dividends	(8.1)	-	(41.1)
Net cash movements	9.9	63.5	(34.0)

Source: Company, FIIG Securities

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