

## On track for a transformative 2017

*Novacyt's strong momentum in 2H16 has continued into 1Q17, with sales of NovaPrep up 45% and Lab21 products up 15% YoY, and the additional contribution of PrimerDesign sales (acquired May 2016) boosting group revenue growth to 70% YoY. In our view, 2017 is likely to be a transformative year for the company, as the highly profitable PrimerDesign business drives strong margin improvement, supported by good organic growth of NovaPrep sales and a return to growth of Lab21 product sales. The company remains on track to deliver its target of being breakeven on an EBITDA level by the end of 2017, and in our view, remains significantly undervalued.*

**On track for a transformative year.** Novacyt has reported its 2016 results, with double-digit revenue growth of 25% on a reported basis (38% at CER) for 2016 to €11.1m and reduced losses at the EBITDA level to €2.3m (€1.7m loss on a proforma basis, versus €2.9m loss for 2015). Crucially, the company is progressing towards profitability, with an EBITDA loss of €0.7m in 2H16 compared with €1.6m in 1H16. Marginally higher than expected finance costs and amortisation led to a total net loss of €5.7m for 2016. Gross margin of 55% (48% in 2015) was boosted by the addition of the profitable PrimerDesign business (59% on a proforma basis), and is expected to improve over the course of 2017. Novacyt finished 2016 with cash of €2.9m, having raised €8.1m in cash and €3m in bonds during the year.

**Strong start to 2017.** Building on the momentum of 2016, Novacyt has also announced a strong start to 2017, with 1Q17 sales up 70%, driven by the PrimerDesign acquisition and strong organic growth from NovaPrep and Lab21 products. Sales of NovaPrep were up 45% in 1Q17, driven by growth in the AsiaPac region (117% growth in 2016), with distribution in key South American markets expected to drive further growth in 2H17. Lab21 has continued to return to growth since a slow down in 2016, with 10% growth in sales in 2H16 and 15% YoY growth in 1Q17. New commercial heads and additional sales personnel should further support sales growth during the year, whilst an improving product mix should drive a 100-200bp gross margin improvement.

**Progressing to profitability.** On our revised forecasts (overleaf) Novacyt is expected to reach break-even point on an EBITDA level in 1H17, with a small profit in 2H17. We believe the acquisition of PrimerDesign in May 2016 has transformed the company's prospects in terms of profitability, supported by improving organic growth in NovaPrep sales and a return to growth for Lab21 product sales. In light of its prospects for 2017 we believe the company remains significantly undervalued and reiterate our Buy rating.

Price (27 April 2017)		€0.94
<b>Changes</b>	<b>Previous</b>	<b>Current</b>
Rating	-	BUY
Target Price	-	€2.34

### Share price performance (indexed)



### Key data

Bloomberg/Reuters codes:	ALNOV FP / ALNOV.PA
Market cap (€m)	13
CAC	5,278
1mth perf (%)	2.2
3mths perf (%)	(16.2)
12mths perf (%)	(36.3)
12mth high-low (€)	2 - 1
Free float (%)	77

### Key financials

Year to Dec	2015A	2016E	2017E
Sales (€)	8.9	11.1	15.3
EBIT adj	(3.24)	(3.18)	(0.44)
EBIT margin (%)	(145.7)	(35.8)	(8.1)
EPS adj (c)	(204.9)	(50.5)	(15.1)
EV/EBITDA (x)	0.5	1.7	238.2
PE adj (x)	NA	NA	NA
Div yield (%)	0	0	0
DPS	0	0	0
FCF yield (%)	0	0	0

Prices are as of 11:35AM 27 April 2017

All sources unless otherwise stated: Company data, FactSet, Stifel estimates

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Completed: 27 April 2017 08:06EDT  
Disseminated: 27 April 2017 08:06EDT

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Key data<sup>1</sup>

Key valuation ratios (x)				
	2015A	2016E	2017E	2018E
PE adj (x)	NA	NA	NA	NA
Div yield (%)	0	0	0	0
Key profit and loss data (€)				
	2015A	2016E	2017E	2018E
Sales (€)	8.9	11.1	15.3	18.3
EBITDA adj	(3.0)	(2.8)	(0.0)	0.8
EBIT adj	(3.24)	(3.18)	(0.44)	0.28
EBIT adj margin (%)	(36.2)	(28.6)	(2.9)	1.5
Net income	(13.9)	(5.7)	(2.6)	(0.8)
EPS adj (c)	(204.9)	(50.5)	(15.1)	(4.6)
DPS (c)	0	0	0	0
Key cash flow data (€)				
	2015A	2016E	2017E	2018E
Operating profit	(13.0)	(4.0)	(1.2)	0.1
Operating cash flow	(5.3)	(4.8)	(2.0)	(0.8)
Taxes paid	0	0	0	0
Net interest	(0.7)	(1.2)	(0.9)	(0.9)
Capex	(0.8)	(0.7)	(0.9)	(1.0)
Free cash flow	(6.9)	(6.7)	(3.8)	(2.7)
Dividends	0	0	0	0
Change in cash	(1)	1	(5)	(6)
Net debt	(1.5)	(4.9)	(9.7)	(12.7)
Key balance sheet (€)				
	2015A	2016E	2017E	2018E
Cash	2	3	(2)	(8)
Net assets	11	19	17	16

## Key information

## Target price methodology/risks

Our target price for Novacyt of €2.34 is based on our belief that shares can trade on a forward EV/Sales of 2.5x.

Risks to the achievement of our target price include market acceptance of the NovaPrep system failing to materialise, gross margins failing to improve as anticipated, and potential changes to reimbursement policy.

## Business description

Novacyt develops, manufactures and supplies diagnostic tests for infectious diseases and cancer screening cytology to diagnostic laboratories.

## Senior management

Graham Mullis (CEO)

Anthony Dyer (CFO)

Jean-Pierre Crinelli (COO)

Eric Peltier (CIO)

## Key dates

2Q17 - Launch of Zika virus CE-IVD

27 June 2017 - AGM

20 July 2017 - 1H17 revenues

26 October 2017 - 1H17 results

## Major shareholders

SAS Cup 92 (founders) - 19.9%

Aurinvest Capital - 9.9%

Merlin residual investment Ltd - 8.1%

## Website

[www.novacyt.com](http://www.novacyt.com)

<sup>1</sup> Year end December

Data in millions, except per share and percentages  
Source: Company data, FactSet, Stifel estimates

## On track for a transformative year

### Momentum towards near-term EBITDA profitability

Novacyt has reported its 2016 results, demonstrating significant progress towards its goal of transforming the company into a multi-platform, global clinical diagnostics company. The company reported revenue growth of 25% on a reported basis (38% at CER) in 2016 to €11.1m, and reduced losses at the EBITDA level to €2.3m (€1.7m on a proforma basis, versus €2.9m for 2015). Crucially, the company is progressing towards profitability, with an EBITDA loss of €0.7m in 2H16 compared with €1.6m in 1H16. Similarly, Novacyt's gross margin of 55% (59% on a proforma basis) was boosted by the addition of the profitable PrimerDesign business (PrimerDesign margin is in excess of 80%) and is expected to continue improving over the course of 2017 and beyond. Marginally higher than expected finance costs and amortisation led to a total net loss of €5.7m for 2016, and the company finished 2016 with cash of €2.9m, following a successful private equity placement raising €2.9m in an over-subscribed issue.

### Strong start to 2017

Building on the momentum of 2016, Novacyt has also announced a strong start to 2017. Group sales growth of 70% YoY in 1Q17 were driven by the contribution of PrimerDesign sales (acquired May 2016), as well as strong organic growth from NovaPrep and Lab21 products. Sales of NovaPrep were up 45%, driven by growth in the AsiaPac region (117% growth in 2016), with distribution in key South American markets expected to drive further growth in 2H17. Lab21 has continued to return to growth since a slowdown in 2016, with 10% growth in sales in 2H16 and 15% YoY growth in 1Q17. New commercial heads and additional sales personnel should further support sales growth during the year – Dr Ruth Powell and Phil Sefton joined in April 2017 to lead the NovaPrep and Lab21 divisions respectively, both of whom have strong commercial and general management experience from blue-chip IVD manufacturers such as Thermofisher, Abbott and Qiagen.

### Acquisitive growth

The acquisition of PrimerDesign during 2016 for 2.4x transformed Novacyt's prospects, as a business with a consistent gross margin >80% with the potential to offer significant synergies and expansion opportunities. Novacyt continues to review acquisition opportunities in the NovaPrep and PrimerDesign divisions, with a focus on distribution and manufacturing to accelerate the company's sales growth. We would expect any future acquisition is expected to be immediately earnings accretive.

## NovaPrep

NovaPrep sales were up 24% in 2016, and have started 2017 exceptionally well, with growth of 45% YoY. Double-digit growth rates in 2016 were driven by geographic expansion and further investments in commercial infrastructure, and are expected to continue over the course of 2017. As a reminder, the total addressable market for cervical cancer screening is estimated to be worth over \$3.6bn, with NovaPrep offering an improved vial and operating system over currently marketed products.

### AsiaPac driving growth

Geographical expansion has been key to NovaPrep's strong performance over the last six to eight months, having launched in 10 new territories in 2016 (including Turkey, Qatar, Israel, Malaysia and Australia). Growth of 117% in Asia Pacific and 65% in the Middle East in 2016 is expected to continue in 2017. Novacyt's distribution partnership with Cepheid Inc is also expected to further boost growth of NovaPrep in 2H17, as approvals are achieved in key South American markets.

### Approvals in US and China

Following regulatory approvals in [China and the US in 1Q17](#), Novacyt is also well placed to identify suitable partners to leverage sales in these areas, as well as evaluating the market potential for NovaPrep in Japan. We expect an update on commercial plans in these key regions over the course of 2017.

## PrimerDesign

### Sales set to accelerate in 2017

PrimerDesign has contributed to group sales since its acquisition in May 2016, but, more importantly, has made a meaningful impact on profitability, with a high-margin business that is expected to drive gross margin for Novacyt above 60% in 2017. Sales were marginally lower than expected in 2016 as a

result of a) currency headwinds and b) the conclusion of development work for two large contracts. The core business reagent sales continued to grow strongly, with growth of 71% in South America, 67% in Asia Pacific and 28% in North America, and sales of molecular kits also grew from 17% to 60%, particularly in crucial markets such as the UK and US. Novacyt's current investment in clinical commercial infrastructure is expected to drive clinical market revenues, as well as adding new B2B sales during 2017.

**First clinically  
validated assay  
launching in 2Q17**

Following the acquisition of PrimerDesign, Novacyt identified the key products in its current catalogue of 450 products that would be suitable for conversion to a clinically approved in vitro diagnostic (IVD) assay over the next five years. The molecular market is one of the fastest growing sectors of the IVD market, with marketsandmarkets.com estimating the market to be worth €6.0bn, growing at a CAGR of 9.1%. Novacyt remains on track to launch the first of these products, a clinically validated assay for the Zika virus, in 2Q17, which is likely to aid sales growth.

## Lab21

Novacyt's profitable Lab21 products division returned to growth in 2H16, with 10% growth YoY (2016 sales of €6.2m were down 8% YoY), having been affected by a delay in tenders being awarded in 2016, which remain outstanding. This encouraging sales growth in 2016 reflected the launch of products into new territories such as Brazil, and the addition of 10 new products into the catalogue. Crucially, 1Q17 sales were up 15% YoY, demonstrating the momentum of the division, despite also recovering from some supply chain issues experienced in 2016.

Our revised forecasts for the company following its 2016 results are presented overleaf.

## Forecasts

Figure 1: Novacyt Income statement (€m)

Year ending December	2015	2016E	2017E	2017E	2017E	2018E	2019E
€m			H1	H2			
Lab 21	7.6	6.2	3.2	3.7	6.9	7.7	8.3
Novacyt	1.3	1.6	1.0	1.2	2.2	3.0	3.7
Primerdesign		3.3	3.0	3.2	6.2	7.6	9.8
<b>Total revenues</b>	<b>8.9</b>	<b>11.1</b>	<b>7.2</b>	<b>8.1</b>	<b>15.3</b>	<b>18.3</b>	<b>21.9</b>
<i>Growth</i>	<i>97%</i>	<i>24%</i>	<i>45%</i>	<i>32%</i>	<i>38%</i>	<i>20%</i>	<i>19%</i>
COGS (€m)	-4.7	-5.0	-2.8	-3.0	-5.8	-6.6	-7.6
<b>Gross profit (€m)</b>	<b>4.3</b>	<b>6.1</b>	<b>4.3</b>	<b>5.2</b>	<b>9.5</b>	<b>11.7</b>	<b>14.3</b>
<i>Gross margin</i>	<i>48%</i>	<i>55%</i>	<i>60%</i>	<i>64%</i>	<i>62%</i>	<i>64%</i>	<i>65%</i>
General and admin	-4.8	-4.5	-2.2	-2.4	-4.6	-4.7	-4.8
Sales and marketing	-2.3	-2.5	-1.3	-1.4	-2.7	-3.1	-3.5
R&D	-0.6	-0.6	-0.3	-0.3	-0.6	-0.8	-0.9
Primerdesign costs		-1.8	-1.1	-1.1	-2.2	-3.0	-3.7
Subsidies	0.1	0.2	0.1	0.1	0.2	0.2	0.2
<b>Total operating expenses</b>	<b>-7.5</b>	<b>-9.3</b>	<b>-4.8</b>	<b>-5.1</b>	<b>-9.9</b>	<b>-11.4</b>	<b>-12.8</b>
<b>EBITA (pre-exceptional)</b>	<b>-3.2</b>	<b>-3.2</b>	<b>-0.5</b>	<b>0.1</b>	<b>-0.4</b>	<b>0.3</b>	<b>1.5</b>
Operating margin						1.5%	7.1%
Amortisation	-9.8	-0.8	-0.4	-0.4	-0.8	-0.2	-0.2
<b>EBIT (pre-exceptional)</b>	<b>-13.0</b>	<b>-4.0</b>	<b>-0.9</b>	<b>-0.3</b>	<b>-1.2</b>	<b>0.1</b>	<b>1.3</b>
Exceptional							
Other income/expense	-0.2	-0.5	-0.2	-0.3	-0.5	0.0	0.0
Finance costs	-0.7	-1.2	-0.4	-0.5	-0.9	-0.9	-0.4
<b>Pre-tax (loss) profit</b>	<b>-13.9</b>	<b>-5.7</b>	<b>-1.5</b>	<b>-1.1</b>	<b>-2.6</b>	<b>-0.8</b>	<b>0.9</b>
Tax	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Net income</b>	<b>-13.9</b>	<b>-5.7</b>	<b>-1.5</b>	<b>-1.1</b>	<b>-2.6</b>	<b>-0.8</b>	<b>0.9</b>
NOSH	6.8	11.3	17.3	17.3	17.3	17.3	17.3
EPS (€)	-2.0	-0.50	-0.09	-0.06	-0.15	-0.05	0.05
<b>EBITDA</b>	<b>-3.0</b>	<b>-2.3</b>	<b>-0.3</b>	<b>0.3</b>	<b>0.0</b>	<b>0.8</b>	<b>2.1</b>
G&A as % of sales	53.6%	40.5%			30.0%	25.6%	21.8%
S&M as % sales	25.6%	22.5%			17.6%	16.9%	16.0%
R&D as % sales	6.6%	5.4%			3.9%	4.4%	4.1%

Source: Company data, Stifel estimates

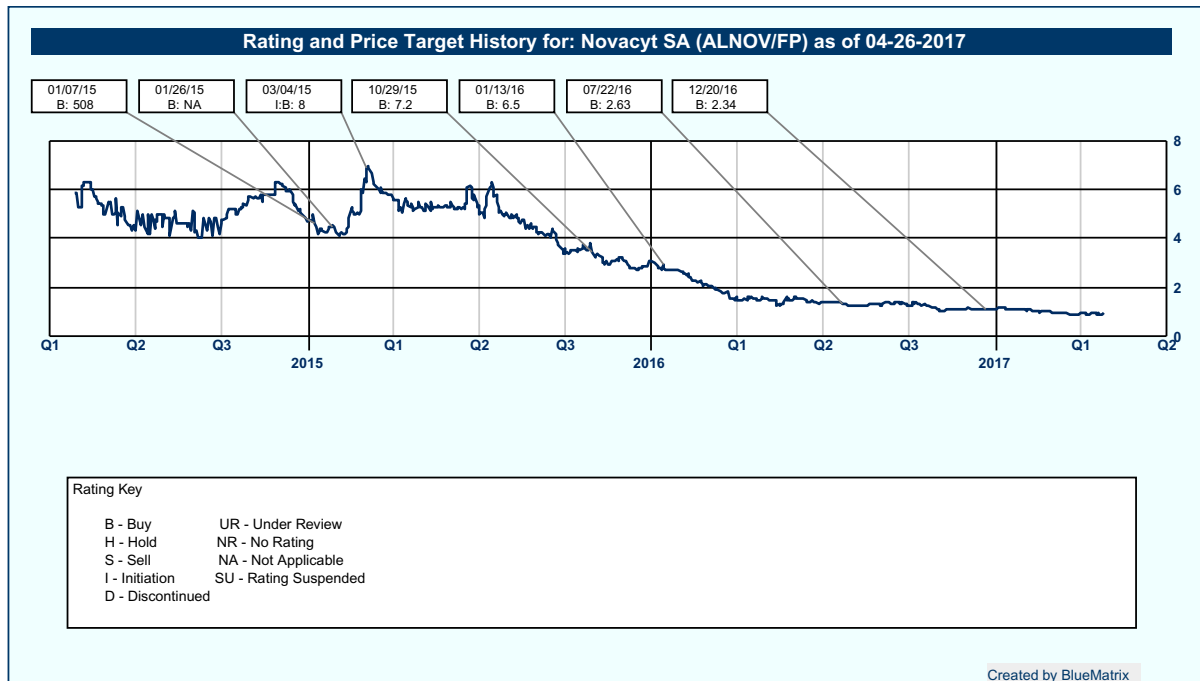
Figure 2: Novacyt cash flow forecasts (€m)

Year ending Dec	2015	2016E	2017E	2017E	2017E	2018E	2019E
€m			H1	H2			
<b>Net income</b>	<b>-13.9</b>	<b>-5.7</b>	<b>-1.5</b>	<b>-1.1</b>	<b>-2.6</b>	<b>-0.8</b>	<b>0.9</b>
Depreciation	0.3	0.4	0.2	0.2	0.4	0.5	0.6
Amortisation	9.8	0.8	0.4	0.4	0.8	0.2	0.2
(Increase)/decrease in inventory	-0.1	-0.3	-0.2	-0.2	-0.4	-0.5	-0.5
(Increase)/decrease receivables	-0.1	-0.5	-0.3	-0.4	-0.7	-0.7	-0.7
Increase/(decrease) in creditors	-1.7	0.5	0.2	0.3	0.5	0.5	0.5
Change in working capital	-1.9	-0.3	-0.3	-0.3	-0.6	-0.7	-0.7
Other	0.4	0.0	0.0	0.0	0.0	0.0	0.0
<b>Operating cashflow</b>	<b>-5.3</b>	<b>-4.8</b>	<b>-1.2</b>	<b>-0.8</b>	<b>-2.0</b>	<b>-0.8</b>	<b>1.0</b>
Capital expenditure	-0.8	-0.7	-0.4	-0.5	-0.9	-1	-1.1
Transaction costs	-0.3	0.0	0.0	0.0	0.0	0.0	0.0
Acquisition		-6.6	-0.6	-1.2	-1.8	-1.2	0.0
<b>Cashflow before financing</b>	<b>-6.4</b>	<b>-12.1</b>	<b>-2.2</b>	<b>-2.5</b>	<b>-4.7</b>	<b>-3.0</b>	<b>-0.1</b>
Capital increase	4.2	8.7	0.0	0.0	0.0	0.0	0.0
Issue/Repayment of debt	1.5	4.5	0.0	0.0	0.0	-3.5	-3.0
<b>Change in cash</b>	<b>-0.6</b>	<b>1.0</b>	<b>-2.2</b>	<b>-2.5</b>	<b>-4.7</b>	<b>-6.5</b>	<b>-3.1</b>
Cash at start of period	2.5	1.8	2.9	0.0	2.9	-1.8	-8.3
<b>Cash at end of period</b>	<b>1.8</b>	<b>2.9</b>	<b>0.7</b>	<b>-2.5</b>	<b>-1.8</b>	<b>-8.3</b>	<b>-11.4</b>
Debt	3.4	7.82	7.82	7.1	7.82	4.3	1.3
<b>Net cash/(debt)</b>	<b>-1.5</b>	<b>-4.9</b>	<b>-7.1</b>	<b>-2.5</b>	<b>-9.7</b>	<b>-12.7</b>	<b>-12.7</b>

Source: Company data, Stifel estimates

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The recommendation contained in this report was produced at 27 April 2017 08:06EDT and disseminated at 27 April 2017 08:06EDT.

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