

Inno-Gene S.A.



FV: PLN 4.10-PLN 5.30

Initiating Coverage

Rating: n.a.

Inno-Gene is a holding that supports and commercializes innovative biotech projects. Its main asset, Centrum Badan DNA Sp. z o.o (CBDNA), is a leader in the area of diagnostic genetics in Poland. While providing services such as DNA sequencing to different scientific institutions, CBDNA also develops own diagnostic tests, which it sells to health and veterinary facilities, law enforcement agencies and private individuals.

Inno-Gene's subsidiary CBDNA is currently offering >100 own and 300 third-party tests e.g. for diagnostics of microbiological infections and genetic pre-conditions, which are distributed by the company itself (own sales team & online shop) and its distribution partners. These tests, which are analyzed in CBDNA's own research lab, allow diagnosing illnesses more accurately and quickly, thus saving lives and reducing health costs.

According to Koncept Analytics, the global market for genetic diagnostics was worth USD 5.6bn in 2013 (+17% y-o-y). The US health insurer UnitedHealth expects that it will grow to USD 25bn by 2023, which would correspond to a CAGR of 16.1%. Based on our discussions with industry experts, we estimate the value of the Polish market at c. PLN 80m, which should however grow at a rate of >50% in the near future as it is only at a very early stage of development.

In 9M/14, Inno-Gene had consolidated revenues of PLN 3.4m (58.2% y-o-y), which were almost as high as in whole 2013 (PLN 3.5m). In our view, this mainly stemmed from strong sales of the new oncological panel 170 Plus, which according to many Polish scientists is revolutionary as it allows detecting genetic predispositions to >20 cancer types. In 9M/14, net profit equaled PLN 0.3m vs. PLN -56k last year. Between January and September 2014, Inno-Gene generated an operating cash flow of PLN 0.5m (9M/13: PLN 0.4m), while its net cash position amounted to PLN 0.5m (EVRe).

We initiate coverage of Inno-Gene with a fair value range of PLN 4.10-PLN 5.30 per share based on three different scenarios. Due to its strong market position and product portfolio we believe that the company could be a major beneficiary of the fast-growing genetic diagnostics market. Also, we expect a positive impact on results from new kinds of tests e.g. NIPT and an increasing share of foreign sales, which now equals c. 5%.

in PLNm	2012	2013	2014E	2015E	2016E	2017E
Net sales	2.45	3.50	5.25	6.82	10.13	14.51
EBITDA	0.11	-0.14	1.04	1.36	2.04	2.93
EBIT	-0.26	-0.55	0.46	0.61	0.91	1.32
Net income	-0.15	-0.46	0.42	0.85	0.99	1.37
EPS	-0.03	-0.09	0.08	0.16	0.19	0.26
DPS	0.00	0.00	0.00	0.00	0.00	0.00
Dividend yield	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
RoE	-20.69%	-47.45%	14.14%	8.05%	6.00%	7.77%
Net gearing	-6.54%	-73.71%	-42.94%	-87.97%	-97.26%	-102.21%
EV/Sales	6.65x	4.64x	3.10x	2.39x	1.61x	1.12x
EV/EBITDA	153.89x	-118.29x	15.58x	11.93x	7.99x	5.55x
P/E	-121.29x	-39.87x	44.48x	21.76x	18.69x	13.48x

Company profile

Inno-Gene S.A. is a holding company, which invests in and markets innovative products in the area of biotechnology.

Website	www.inno-gene.eu
Sector	Biotechnology
Country	Poland
ISIN	PLINNGN00015
Reuters	IGNP.WA
Bloomberg	IGN PW

Share information

Last price	3.55
Number of shares (m)	5.20
Market cap. (PLNm)	18.47
Market cap. (EURm)	4.44
52-weeks range	PLN 3.90 / PLN 2.01
Average volume	1,307

Performance

4-weeks	3.80%
13-weeks	19.53%
26-weeks	24.56%
52-weeks	70.67%
YTD	-8.97%

Shareholder structure

Jacek Wojciechowicz	48.41%
MOONROCK Enterprise S.A.	14.50%
PZU TFI	6.60%
Michal Obszanski	5.17%
Michal Kaszuba	0.97%
Free float	24.34%

Financial calendar

Q4 2014 results	February 14, 2015
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Investment Case

- The origins of Inno-Gene go back to 2005, when two scientists from the Polish Academy of Science (PAN) founded a company in order to commercialize scientific research in the area of biotechnology. Today, Inno-Gene acts as a holding, which invests in and supports promising projects in the area of diagnostic genetics. With an offering of >400 tests including >100 own ones, its 100% shareholding Centrum Badan DNA Sp. z o.o is one of the leading players on the Polish market.
- Through two direct and three indirect subsidiaries, Inno-Gene provides a full scope of services relating to diagnostic testing e.g. tests for medical and veterinary facilities, law enforcement agencies as well as private individuals, DNA sequencing for scientific institutions, research on new tests in own labs funded by EU subsidies, trainings, test analysis with respective software. Its most promising test, which is considered revolutionary by many Polish scientists, is a universal diagnostic panel that allows detecting genetic predispositions to >20 kinds of cancer.
- According to independent market research firms, the global market for genetic diagnostics is set to grow at a fast pace in the coming years as these tests can potentially save lives and significantly reduce health costs. Market forecasts show the total market value at USD 5.6-6.9bn and the yearly growth rate in the coming years at 16.1%-17.5%. Based on our discussions with industry experts, for Poland we estimate the total market value at c. PLN 80m, however forecast a much faster growth going forward of >50% y-o-y due to the early-stage character of the market.
- In 9M/14, Inno-Gene's results showed very solid growth, with sales (PLN 3.4m; +58.2% y-o-y) reaching almost the figure which was reported for full-year 2013. In contrast to last year, EBIT (PLN 0.3m) and net income (PLN 0.3m) were in the positive territory as the company sold more of its high-margin tests e.g. the panel for testing predispositions to different cancer types and to sepsis. In our base case scenario, we expect that by 2023 the number of sold diagnostic tests will grow at a CAGR of 19.9%. Due to a higher share of high-margin products the average price should grow at 5.4% per year, resulting in an improvement of the EBIT margin from 8.8% to 9.1%-9.4% in the long run. For full-year 2014, we estimate IGN's revenues at PLN 5.3m (13,300 tests sold), EBIT at PLN 0.5m and net income at PLN 0.4m.
- We have determined a fair value range for Inno-Gene's shares of PLN 4.10-PLN 5.30 based on three different scenarios. While our pessimistic scenario assumes an increase of sold tests similar to forecasts for the global market, we believe that the Polish market for diagnostic genetics will grow at a faster pace as it is less developed than Western markets. As one of the market leaders, Inno-Gene should be able to benefit from that growth significantly, especially given its attractive product portfolio and the planned introduction of new tests such as NIPT (Non-Invasive Prenatal Test). Moreover, we expect the company to increase foreign sales, which currently only make up c. 5% of its yearly turnover. The most serious risk to our growth assumptions is that the public health insurance NFZ, which accounts for c. 65% of total health spending in Poland, will not support the area of genetic diagnostics.

SWOT Analysis

Strengths

- Fully-owned subsidiary Centrum Badan DNA Sp. z o.o is one of only three companies in its segment in PL; it offers >400 diagnostic tests (thereof >100 own ones) for different kinds of cancer, microbiological infections, genetical pre-conditions; also, parental and criminal checks as well DNA sequentiation, which can be used in medical, veterinary and scientific facilities
- High market entry barriers relating to prices, costs and genetical differences e.g. between Asians and Europeans
- Own research lab and high success rate in applying for EU subsidies (EVRe: PLN 16m granted so far)
- Three patents plus >15 pending

Weaknesses

- Very small size
- Listing in the illiquid NewConnect segment
- Inno-Gene uses Polish Accounting Standards

Opportunities

- Increasing sales of especially high-margin tests e.g. for detecting predispositions to sepsis, different cancer types as well as tests for ticks; also, introduction of new ones e.g. NIPT (Non-Invasive Prenatal Test e.g. for testing the down syndrome), which are currently not conducted in PL
- Increasing share of foreign sales, especially in Western Europe and the US
- According to Frost & Sullivan, predictive medicine, pharmacogenomics, prenatal and newborn screening will experience significant growth over the next years; all of them make up the genetic diagnostics segment
- Market research firms expect the global genetic testing market to grow at a CAGR of 16.1%-17.5% from USD 5.6bn-PLN 6.9bn last year; the Polish market, which was worth c. PLN 80m in 2013, could grow at >50% y-o-y
- Takeover by a large healthcare company

Threats

- Risks relating to financing of diagnostic tests by public insurer NFZ, which accounts for c. 65% of total health spending in Poland
- Loss of key employees and problems to find qualified personnel
- Risks associated with exchange rate fluctuations as Inno-Gene generates most sales in PL, but buys equipment abroad
- Legal limitation of diagnostic tests due to ethical reasons

Valuation

Due to the company's early-stage character we have decided to value Inno-Gene by using a DCF approach only. Our three scenarios result in a fair value range for the company's shares of PLN 4.10-PLN 5.30.

DCF model (Pessimistic scenario)

in PLNm	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Net sales	6.62	9.75	13.75	17.34	21.50	25.99	29.50	33.17	36.95
(y-o-y change)	26.2%	47.1%	41.0%	26.1%	24.0%	20.9%	13.5%	12.5%	11.4%
EBIT	0.59	0.87	1.24	1.58	1.97	2.40	2.70	3.00	3.31
(operating margin)	8.9%	9.0%	9.0%	9.1%	9.2%	9.3%	9.2%	9.1%	9.0%
NOPLAT	0.48	0.71	1.00	1.28	1.60	1.95	2.19	2.43	2.68
+ Depreciation & amortisation	0.74	1.08	1.53	1.92	2.39	2.88	3.27	3.68	4.10
= Net operating cash flow	1.21	1.79	2.53	3.20	3.98	4.83	5.46	6.11	6.78
- Total investments (Capex and WC)	-0.16	-1.05	-1.47	-1.86	-2.29	-2.76	-3.16	-3.55	-4.06
Capital expenditure	-0.90	-1.42	-1.93	-2.27	-2.77	-3.28	-3.57	-3.98	-4.39
Working capital	0.74	0.36	0.46	0.42	0.48	0.52	0.41	0.43	0.34
= Free cash flow (FCF)	1.05	0.73	1.07	1.34	1.69	2.07	2.30	2.56	2.73
PV of FCFs	0.94	0.58	0.75	0.84	0.94	1.02	1.00	0.99	0.94
PV of FCFs in explicit period	8.00								
PV of FCFs in terminal period	9.78								
Enterprise value (EV)	17.78								
+ Net cash / - net debt	2.20								
+ investments / - minorities	-1.07								
Shareholder value	18.91								
Number of shares outstanding (m)	5.20								
Terminal EBIT margin									
WACC	12.8%		6.0%	7.0%	8.0%	9.0%	10.0%	11.0%	12.0%
Cost of equity	12.8%	8.8%	5.65	6.20	6.74	7.29	7.84	8.39	8.94
Pre-tax cost of debt	10.0%	9.8%	4.84	5.27	5.70	6.13	6.56	6.99	7.42
Normal tax rate	19.0%	10.8%	4.24	4.58	4.93	5.27	5.62	5.97	6.31
After-tax cost of debt	8.1%	11.8%	3.77	4.05	4.33	4.62	4.90	5.18	5.47
Share of equity	100.0%	12.8%	3.39	3.63	3.86	4.10	4.33	4.57	4.80
Share of debt	0.0%	13.8%	3.09	3.29	3.48	3.68	3.88	4.07	4.27
Fair value per share in PLN (today)	3.63	14.8%	2.84	3.00	3.17	3.34	3.50	3.67	3.84
Fair value per share in PLN (in 12 months)	4.10								

Source: Company information, East Value Research GmbH

DCF model (Base Case scenario)

in PLNm	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Net sales	6.82	10.13	14.51	18.64	23.56	28.79	33.35	37.94	43.15
(y-o-y change)	29.9%	48.5%	43.2%	28.5%	26.4%	22.2%	15.9%	13.7%	13.7%
EBIT	0.61	0.91	1.32	1.72	2.19	2.71	3.10	3.49	3.93
(operating margin)	8.9%	9.0%	9.1%	9.2%	9.3%	9.4%	9.3%	9.2%	9.1%
NOPLAT	0.49	0.74	1.07	1.39	1.78	2.19	2.51	2.83	3.18
+ Depreciation & amortisation	0.76	1.12	1.61	2.07	2.62	3.20	3.70	4.21	4.79
= Net operating cash flow	1.25	1.86	2.68	3.46	4.39	5.39	6.21	7.04	7.97
- Total investments (Capex and WC)	-0.18	-1.09	-1.54	-1.99	-2.50	-3.05	-3.55	-4.04	-4.70
Capital expenditure	-0.94	-1.48	-2.05	-2.47	-3.07	-3.65	-4.08	-4.57	-5.19
Working capital	0.76	0.38	0.51	0.48	0.57	0.60	0.53	0.53	0.49
= Free cash flow (FCF)	1.07	0.77	1.14	1.47	1.89	2.34	2.66	2.99	3.27
PV of FCFs	0.96	0.61	0.80	0.92	1.05	1.15	1.16	1.16	1.12
PV of FCFs in explicit period	8.94								
PV of FCFs in terminal period	11.61								
Enterprise value (EV)	20.55								
+ Net cash / - net debt	2.20								
+ investments / - minorities	-1.07								
Shareholder value	21.68								
Number of shares outstanding (m)	5.20								
WACC	12.8%								
Cost of equity	12.8%								
Pre-tax cost of debt	10.0%								
Normal tax rate	19.0%								
After-tax cost of debt	8.1%								
Share of equity	100.0%								
Share of debt	0.0%								
Fair value per share in PLN (today)	4.17								
Fair value per share in PLN (in 12 months)	4.70								

Source: Company information, East Value Research GmbH

DCF model (Optimistic scenario)

in PLNm	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E
Net sales	7.09	10.63	15.47	20.24	25.99	32.08	37.91	43.59	49.21
(y-o-y change)	35.1%	49.8%	45.6%	30.8%	28.4%	23.4%	18.2%	15.0%	12.9%
EBIT	0.63	0.96	1.42	1.88	2.44	3.05	3.56	4.05	4.51
(operating margin)	8.9%	9.0%	9.2%	9.3%	9.4%	9.5%	9.4%	9.3%	9.2%
NOPLAT	0.51	0.78	1.15	1.52	1.98	2.47	2.89	3.28	3.65
+ Depreciation & amortisation	0.79	1.18	1.72	2.25	2.88	3.56	4.21	4.84	5.46
= Net operating cash flow	1.30	1.96	2.87	3.77	4.86	6.03	7.09	8.11	9.11
- Total investments (Capex and WC)	-0.21	-1.14	-1.64	-2.15	-2.74	-3.38	-4.01	-4.63	-5.36
Capital expenditure	-1.00	-1.55	-2.20	-2.70	-3.41	-4.09	-4.69	-5.28	-5.88
Working capital	0.79	0.41	0.56	0.55	0.67	0.71	0.67	0.66	0.52
= Free cash flow (FCF)	1.09	0.82	1.23	1.62	2.12	2.65	3.08	3.49	3.75
PV of FCFs	0.98	0.65	0.87	1.01	1.18	1.30	1.34	1.35	1.29
PV of FCFs in explicit period	9.97								
PV of FCFs in terminal period	13.34								
Enterprise value (EV)	23.31								
+ Net cash / - net debt	2.20								
+ investments / - minorities	-1.07								
Shareholder value	24.44								
Number of shares outstanding (m)	5.20								
WACC	12.8%								
Cost of equity	12.8%								
Pre-tax cost of debt	10.0%								
Normal tax rate	19.0%								
After-tax cost of debt	8.1%								
Share of equity	100.0%								
Share of debt	0.0%								
Fair value per share in PLN (today)	4.70								
Fair value per share in PLN (in 12 months)	5.30								

Source: Company information, East Value Research GmbH

Peer Group Analysis

Below are 11 companies, which according to our research operate in the area of diagnostic genetics, however mostly in Western markets and Asia. Apart from some public health facilities, which conduct genetic tests, there are only two private companies in Poland, which compete with Inno-Gene: Genomed S.A. and Centrum Medyczne Medgen Sp. z.o.o from Warsaw.

- (1) *Genomed S.A.*: Genomed, which is listed in the NewConnect segment of the WSE, is the Polish market leader in the area of services relating to DNA analysis and diagnostics of genetic illnesses. The company provides DNA sequencing to >300 research centers, biotech firms and medical institutions. The technology, on which Genomed is working, allows reading and analyzing all known 6,500 genes that are related to genetic illnesses. Moreover, it is able to analyze gene sequences in order to find all changes relating to inherited illnesses. In 2013, Genomed generated revenues of PLN 5m and an EBITDA margin of 5.9%. Around 5% of its total sales stemmed from abroad.
- (2) *Centrum Medyczne MEDGEN Sp. z.o.o*: MEDGEN's doctors, diagnostic specialists, molecular biologists and medical analysts cooperate with companies and research institutions in Poland and abroad. The company offers genetic consultancy as well as treatment of many different kinds of genetic illnesses and preconditions.
- (3) *Seegene Inc.*: Seegene, which is headquartered in Seoul/Korea, is engaged in the development of molecular diagnostic reagents. In particular, the company provides inspection products such as allergic respiratory pathogens, sexually transmitted diseases pathogens, human papilloma virus (HPV) and drug resistance inspection products, among others. Also, it supplies automatic real-time detection instruments. In 2013, Seegene had revenues of KRW 56bn and an EBITDA margin of 29.4%. It has a distribution agreement with Inno-Gene's former subsidiary NewLab Systems Sp. z.o.o (was sold in October 2014 to its CEO for PLN 100k) relating to market introduction of its products in the CEE region.

According to Thomson Reuters Eikon, Seegene is trading at an EV/Sales 2015E of 12x and EV/EBITDA 2015E of 41.1x.

- (4) *Illumina Inc.*: Headquartered in San Diego/US, Illumina is a developer and manufacturer of life science tools and integrated systems for the analysis of genetic variations and functions. The company is organized in two business segments: Life Sciences and Diagnostics. The Life Sciences business unit includes all products and services relating to its sequencing, BeadArray, VeraCode, and real-time PCR technologies, while its Diagnostics segment focuses on molecular diagnostics. Illumina's customers include genomic research centers, academic institutions, government laboratories, and clinical research organizations, as well as pharmaceutical, biotechnology, agrigenomics, and consumer genomics companies. In 2013, Illumina generated total sales of USD 1.4bn and an EBITDA margin of 24.8%.

According to Thomson Reuters Eikon, Illumina is trading at an EV/Sales 2015E of 12.1x and EV/EBITDA 2015E of 36x.

- (5) *Life Technologies Corporation/Thermo Fisher Scientific Inc.*: Life Technologies was taken over in Q1/14 by Waltham/US-based Thermo Fisher Scientific for USD 13.6bn. Thermo Fisher Scientific is the world leader in the area of services that accelerate life sciences research, solve complex analytical problems, improve patient diagnostics and laboratory productivity. Life Technologies, which manufactures serums and other cell growth media e.g. enzymes as well as diagnostic products such as standard plates and tubes, is now part of the segments "Life Sciences Solutions" and "Specialty Diagnostics". In 2013, Life Technologies had revenues of USD 3.9bn, while Thermo Fisher Scientific reported sales of USD 13.1bn and an EBITDA margin of 21.3%.

According to Thomson Reuters Eikon, Thermo Fisher Scientific is trading at an EV/Sales 2015E of 3.6x and EV/EBITDA 2015E of 14.6x.

- (6) *Quest Diagnostics Inc.*: Quest Diagnostics, which is based in Madison/US, is a provider of diagnostic testing services. The company offers access to diagnostic testing services through its network of laboratories and own service centers. It provides clinical testing, including gene-based and esoteric testing and anatomic pathology services e.g. for doctors, individual patients, biotech companies and law enforcement agencies as well as risk assessment services for the life insurance industry. In 2013, Quest Diagnostics generated sales of USD 7.1bn and an EBITDA margin of 19.6%.

According to Thomson Reuters Eikon, Quest Diagnostics is trading at an EV/Sales 2015E of 1.8x and EV/EBITDA 2015E of 8.8x.

- (7) *Laboratory Corp. of America Holdings Inc.:* Laboratory Corporation of America Holdings, which is headquartered in Burlington/US, is a clinical laboratory company. Through a national network of laboratories, it offers a range of testing services used by healthcare practitioners in testing, patient diagnosis, and in the monitoring and treatment of disease. In addition, it has developed specialty and niche operations based on certain types of specialized testing capabilities and client requirements, such as oncology testing, human immunodeficiency virus (HIV) genotyping and phenotyping, diagnostic genetics and clinical research trials. In 2013, Laboratory Corp. of America Holdings generated total revenues of USD 5.8bn and an EBITDA margin of 21.4%.

According to Thomson Reuters Eikon, Laboratory Corp. is trading at an EV/Sales 2015E of 2.2x and EV/EBITDA 2015E of 10.6x.

- (8) *Genomic Health Inc.:* Genomic Health, which is based in Redwood City/US, is a molecular diagnostics company focused on the development and commercialization of genomic-based clinical laboratory services that analyze the underlying biology of cancer. In 2013, it generated revenues of USD 261.6m and an EBITDA margin of -2.1%.

According to Thomson Reuters Eikon, Genomic Health is trading at an EV/Sales 2015E of 2.9x.

- (9) *Myriad Genetics Inc.:* Myriad Genetics, which is headquartered in Salt Lake City/US, is a molecular diagnostic company. It is focused on developing and marketing predictive medicine, personalized medicine and prognostic medicine tests. Its technologies include those for biomarker discovery, high-throughput deoxyribo nucleic acid (DNA) sequencing, ribo nucleic acid (RNA) expression and multiplex protein analysis. In fiscal-year 2013/14, it had revenues of USD 778.2m at an EBITDA margin of 37%.

According to Thomson Reuters Eikon, Myriad Genetics is trading at an EV/Sales 2015E of 3x and EV/EBITDA 2015E of 10.6x.

- (10) *Sequenom Inc.:* Sequenom, which is based in San Diego/US, is a molecular diagnostic testing and genetics analysis company. Its development and commercialization efforts in various diagnostic areas include noninvasive women's health-related and prenatal diagnostics, ophthalmology, oncology, infectious diseases and autoimmunity. In 2013, it generated sales of USD 162.4m and an EBITDA margin of -47.6%.

According to Thomson Reuters Eikon, Sequenom is trading at an EV/Sales 2015E of 2.5x and EV/EBITDA 2015E of 70.5x.

(11) *Roche Holding AG*: Roche, which is based in Basel/Switzerland, is the world market leader in biotech, oncology, in-vitro diagnostics and hospital markets. In 2013, it had total sales of CHF 46.8bn, thereof CHF 10.5bn in the segment Diagnostics, which generated an EBIT margin of 20.8%. Molecular Diagnostics made up 15% of total diagnostic sales or CHF 1.6bn.

According to Thomson Reuters Eikon, Roche is trading at an EV/Sales 2015E of 4.9x and EV/EBITDA 2015E of 11.9x.

Recent results

Revenues and Profitability

In 9M/14, Inno-Gene generated total revenues of PLN 3.4m compared to PLN 2.1m last year. In our view, the reasons for the increase were strong sales of the new panel for detecting predisposition to >20 different kinds of cancer as well as a test for sepsis. We think that between January and September Inno-Gene sold c. 10,000 tests at an average price of PLN 338.

in PLNm	9M/14	9M/13	change (%)
Net sales	3.38	2.14	58.2%
EBITDA	0.68	0.24	185.9%
<i>EBITDA margin</i>	<i>20.0%</i>	<i>11.1%</i>	
EBIT	0.30	-0.10	-385.3%
<i>EBIT margin</i>	<i>8.8%</i>	<i>-4.9%</i>	
Net income	0.27	-0.06	-575.7%
<i>Net margin</i>	<i>7.9%</i>	<i>-2.6%</i>	

Source: Company information, East Value Research GmbH

Inno-Gene's profitability improved even more than sales, with EBIT and net income reaching positive territory. This reasons were (1) higher share of higher-margin diagnostic tests and (2) significantly lower share of CoGS (55.3% vs. 61.4%), personnel expenses (23.6% vs. 31.2%) and D&A (11.2% vs. 16%) in total sales.

Balance sheet and Cash flow

At the end of September 2014, Inno-Gene had equity of PLN 1m compared to PLN 1.1m last year, which resulted from a net loss in full-year 2013. Property, plant and equipment, which mainly comprise laboratory equipment, equaled PLN 2.9m (9M/13: PLN 2.7m), while intangible assets (software and three patents) amounted to PLN 535k (PLN 710k). As Inno-Gene uses Polish Accounting Standards, its goodwill went down compared to 9M/13 from PLN 28k to PLN 12k due to yearly amortization.

Working capital equaled PLN -9.1m compared to PLN -2.7m last year. It was negative as before completion of R&D Inno-Gene books the respective EU subsidies under short-term liabilities. Over the last years, the company received in total PLN 16m of research grants.

Due to much better net income y-o-y Inno-Gene's operating cash flow increased from PLN 386k in 9M/13 to PLN 479k. Cash flow from investing and financing amounted to PLN -613k (PLN -189k), respectively PLN 85k (PLN 0k). In total, the company's cash position went down since January 2014 by PLN 49k to PLN 784k.

Financial forecasts

Revenues and Profitability

We have calculated three scenarios for Inno-Gene dependent on assumptions relating to the share of high-margin products in total sales. Our revenue model only takes into account sales of diagnostic tests. For full-year 2014, we have assumed that Inno-Gene will sell in total 13,300 tests at an average price of PLN 395, resulting in revenues of PLN 5.3m. At the same time, EBIT margin should remain the same as in 9M/14: 8.8%. On the net profit level, we expect PLN 415k (7.9% margin).

Although Inno-Gene currently has >400 test in its offering, we expect that from 2015 it will concentrate its distribution efforts on the 30 most profitable ones, especially the new universal panel for detecting preconditions to >20 cancer types and tests for detecting sepsis and ticks. We think that on the one hand this will increase the average sales price and on the other also improve the efficiency of the sales process, which should positively impact operating margins.

Base Case scenario: Number of sold tests – CAGR 14-23E = 19.9%; Average price per test - CAGR 14-23E = 5.4%; Increase of the EBIT margin: from 8.8% in 2014 to 9.1-9.4% in the long run.

Base case scenario	2014E	2015E	2016E	2017E
Genetic diagnostic tests	5.25	6.82	10.13	14.51
(change y-o-y)	49.8%	29.9%	48.5%	43.2%
Gross margin	50.0%	51.0%	51.1%	51.2%
Units	13,300	16,359	23,066	31,370
Average price per unit	395	417	439	463
Total revenues	5.25	6.82	10.13	14.51
(change y-o-y)	49.8%	29.9%	48.5%	43.2%

Source: East Value Research GmbH

Optimistic scenario: Number of sold tests - CAGR 14-23E = 21.4%; Average price per test: CAGR 14-23E = 5.6%; Increase of the EBIT margin: from 8.8% in 2014 to 9.2-9.5% in the long run.

Optimistic scenario	2014E	2015E	2016E	2017E
Genetic diagnostic tests	5.25	7.09	10.63	15.47
(change y-o-y)	49.8%	35.1%	49.8%	45.6%
Gross margin	50.0%	52.0%	52.2%	52.4%
Units	13,300	16,891	23,985	33,100
Average price per unit	395	420	443	467
Total revenues	5.25	7.09	10.63	15.47
(change y-o-y)	49.8%	35.1%	49.8%	45.6%

Source: East Value Research GmbH

Pessimistic scenario: Number of sold tests - CAGR 14-23E = 18.2%; Average price per test - CAGR 14-23E = 5.1%; Increase of the EBIT margin - from 8.8% in 2014 to 9-9.3% in the long run.

Pessimistic scenario	2014E	2015E	2016E	2017E
Genetic diagnostic tests	5.25	6.62	9.75	13.75
(change y-o-y)	49.8%	26.2%	47.1%	41.0%
Gross margin	50.0%	50.0%	50.1%	50.1%
Units	13,300	15,960	22,344	29,986
Average price per unit	395	415	436	458
Total revenues	5.25	6.62	9.75	13.75
(change y-o-y)	49.8%	26.2%	47.1%	41.0%

Source: East Value Research GmbH

in PLNm	Q1/12	Q2/12	Q3/12	Q4/12	2012	Q1/13	Q2/13	Q3/13	Q4/13	2013
Net sales	0.79	0.42	0.57	0.68	2.45	0.82	0.67	0.66	1.37	3.50
y-o-y change	n.a	n.a	n.a	n.a	n.a	3.6%	60.1%	15.6%	102.3%	43.2%
EBITDA	0.16	-0.19	0.06	0.08	0.11	0.31	-0.02	-0.05	-0.37	-0.14
EBITDA margin	20.1%	-45.4%	10.8%	11.2%	4.3%	38.4%	-3.7%	-7.9%	-27.4%	-3.9%
EBIT	0.12	-0.27	-0.03	-0.08	-0.26	0.25	-0.18	-0.17	-0.44	-0.55
EBIT margin	15.4%	-64.2%	-4.5%	-12.6%	-10.5%	30.1%	-27.7%	-25.2%	-32.3%	-15.6%
Net income	0.14	-0.37	-0.01	0.08	-0.15	0.19	-0.06	-0.19	-0.41	-0.46
Net margin	18.4%	-89.1%	-1.4%	12.1%	-6.2%	23.9%	-9.0%	-29.0%	-29.8%	-13.2%

in PLNm	Q1/14	Q2/14	Q3/14	Q4/14E	2014E
Net sales	0.55	1.20	1.63	1.87	5.25
y-o-y change	-32.3%	80.2%	148.2%	36.8%	49.8%
EBITDA	-0.30	0.31	0.66	0.37	1.04
EBITDA margin	-53.6%	25.8%	40.6%	19.7%	19.9%
EBIT	-0.39	0.18	0.51	0.16	0.46
EBIT margin	-71.4%	14.9%	31.5%	8.8%	8.8%
Net income	-0.28	0.15	0.39	0.15	0.42
Net margin	-50.4%	12.5%	24.2%	8.0%	7.9%

Source: Company information, East Value Research GmbH

CAPEX and Working capital

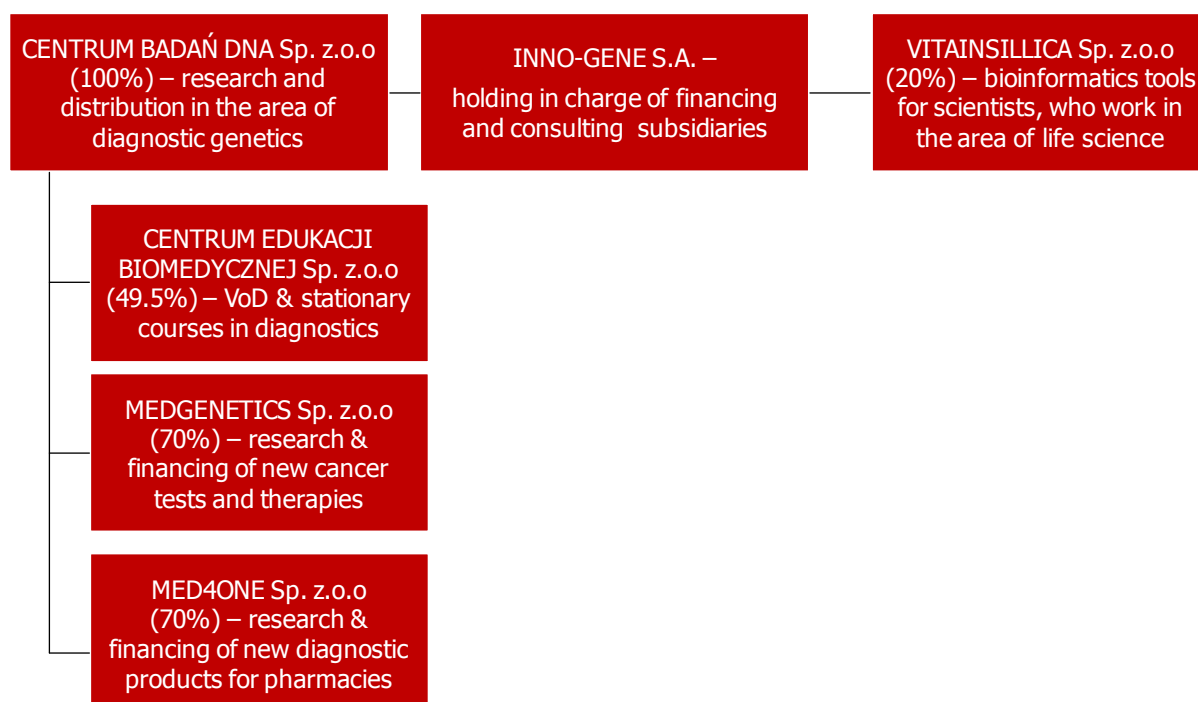
In our model, we have assumed a share of gross CAPEX in total sales of 13-14.6%, which in our opinion will mainly increase intangible assets (patents, software, licenses). We expect that working capital investments will equal >11% of total sales in the long run and the cash conversion cycle will remain at a similar level to 2013 (30 days).

Business description

Inno-Gene S.A., which is based in Poznan, is a holding company, which invests in innovative biotech companies in order to commercialize their R&D. Through two direct and three indirect shareholdings, Inno-Gene provides research, distribution and consulting services to public, private and scientific institutions as well as private individuals.

Inno-Gene's main asset is Centrum Badan DNA Sp. z.o.o (CBDNA). CBDA is currently distributing more than 400 diagnostic tests (thereof >100 own ones), which allow to determine whether a patient (or animal) has a certain genetic precondition e.g. if there is a risk that he will be diagnosed with cancer.

Organizational structure



Source: Company information, East Value Research GmbH

Company history

- 2006: Foundation of Centrum Badan DNA Sp. z.o.o by Michal Kaszuba and Jacek Wojciechowicz (now CEO of Inno-Gene).
- 2007: First test is one for finding diseases that are caused by ticks. Within two months, it generates sales of PLN 250k.
- 2009: Development of additional tests e.g. against sepsis, for finding susceptibility to cancer of large intestine and prostate as well as for determining paternity.
- 2010: Blumerang Pre-IPO/MOONROCK Enterprise invests in Inno-Gene S.A. The company lists its shares in the NewConnect segment of the Warsaw Stock Exchange.
- 2013: Inno-Gene's subsidiary NewLab Systems Sp. z.o.o (distributor of devices for diagnostic testing; was sold in October 2014 to its CEO Mr Kaszuba for PLN 100k) signs a distribution agreement with Korean company Seegene Inc.

Service offering

Sale of own and third-party diagnostic tests: In the last years, Inno-Gene's subsidiary CBDNA has developed c. 100 own tests, which were mostly co-financed by EU subsidies. They are conducted by using all available methods e.g. cDNA sequencing, real-time PCR or NGD (provides very fast and accurate test results). Some of the tests e.g. one testing for HIV have not been accepted by the market, while others – one testing for paternity, sepsis, diseases caused by ticks, different kinds of cancers – have been very well received by customers. CBDNA has been offering the tests to public and private medical and veterinary facilities, law enforcement agencies as well as private individuals for a one-off fee, which according to our research can range between PLN 70 and PLN 10,000 dependent on the complexity level of the respective test. In order to obtain test results, the patient has to provide a sample of his blood, bone marrow or the smear from his oral cavity and send it to CBDNA's own research lab in Poznan, where the sample will be analyzed within a few days.

In the short run, CBDNA plans to start offering a new NIPT test (Non-Invasive Prenatal Test), which will be conducted on equipment from the leading provider of testing devices Life Technology Inc. (CBDNA's lab is the first one in Poland, which has been authorized by them). CBDNA will receive the CE IVD European certificate for these tests.

DNA sequencing: DNA sequencing is the process of determining the precise order of nucleotides within a DNA molecule, meaning the order of the four bases—adenine, guanine, cytosine, and thymine—in a strand of DNA. The method has greatly accelerated biological and medical research in various fields such as diagnostic, biotechnology, forensic biology, virology and biological systematics. Its areas of application include

- Food: for the precise identification of bacterial flora, which the respective product contains; required for patent application among others.
- Forestry: for analyzing species and the share of respective micro-organisms in earth or water; also, for observation of the impact of changes in their structure or mutation on plant growth.
- Bioenergy: for analyzing the content of species as well as characteristics of micro-organisms, which are used in bio-gas plants as well as their impact on the effectiveness of processing organic material into gas.

Inno-Gene's subsidiary CBDNA provides such services to scientific facilities.

Video-on-Demand and stationary training: Since 2013, CBDNA has offered courses and training on genetic diagnostics for scientists, health practitioners and individual patients for a one-off fee.

Bioinformatics: Inno-Gene provides software analytics of genetic material through its 20% shareholding Vitainsillica Sp. z.o.o.

Management

Jacek Wojciechowicz (CEO): Mr Wojciechowicz is Managing Director of Centrum Badan DNA and CEO of Inno-Gene. He graduated from the University Warminsko-Mazurski in Olsztyn with a degree in Biotechnology and Computer Science. In addition, he has a degree in Science and Technology Commercialisation from the University of Lodz and Institute IC2 of the University of Texas. Mr Wojciechowicz is co-author of scientific papers and patents relating to genetic samples for the identification of pathogens as well as genetic diseases.

Cezary Ziarkowski (Vice President of the Board): Mr Ziarkowski became Inno-Gene's Vice President of the Board at the end of October 2014. He is the person in charge of investor relations and sales activities in Poland and abroad. Previously, he was Investment Director at Moonrock Enterprise S.A, which is Inno-Gene's shareholder. Mr Ziarkowski has a Master's degree in Mechanical Engineering from the Agricultural and Technical Academy in Bydgoszcz.

Market environment

The global market for genetic diagnostics

According to research firm Boston Biomedical Consultants, molecular diagnostics (= genetic testing) emerged in response to a need for more rapid, sensitive and specific diagnostic tests than with traditional techniques such as immunoassays. According to Koncept Analytics, the global market was worth USD 5.6bn in 2013. The US health insurer UnitedHealth and BCC Research forecast that it will grow at a CAGR of 16.1%-17.5% over the next years. This will result from the fact that genetic tests have become much cheaper and much easier to perform. As the main growth drivers Frost & Sullivan sees the rapid growth of preventive and personalized medicine, which according to PwC could grow even 10 fold by 2015 compared to 2009. While prenatal, newborn, and reproductive screening are the largest segments in the market, predictive medicine (especially cancer diagnostic tests) are set to experience the fastest growth.

The market for genetic diagnostics in Poland

Based on our discussions with industry experts, we estimate the value of the genetic diagnostics segment in Poland at c. PLN 80m. According to PZH, there are currently >350k cancer patients in Poland (>1m including family members) and 140k new ones per year. They expect that by 2025 the number of new cancer patients will increase by 40%, which should positively impact the demand for respective diagnostic tests. Market participants in Poland forecast that the growth CAGR in the coming years could even reach >50% due to (1) still relatively low use of diagnostic research in PL compared to Western markets and (2) increasing wealth of the population.

Factors, which drive the growth of genetic diagnostics

Trinity Investment Research has identified the following growth drivers:

Expanded Human Genetic Testing: Especially since 2003, when the mapping of the human genome was completed, scientists have made tremendous advances in the understanding of the role genes play in diseases. This has led to the emergence of human genetic tests.

Pharmaco-genomics: There is growing recognition of the role that genetics plays in how well individuals tolerate and respond to many drugs. As a result, it is likely that genetic testing will be increasingly used to guide personalized medicine.

Protein Testing: The introduction of more sensitive technologies is expected to enable physicians to detect target proteins at lower concentrations than can be detected using traditional techniques. This should expand the market for tests associated with existing biomarkers.

Convergence of Genomic and Protein Testing: There is growing medical understanding of the inter-relationship between genetics and proteins in disease states.

Profit and loss statement

in PLNm	2012	2013	2014E	2015E	2016E	2017E
Revenues	2.45	3.50	5.25	6.82	10.13	14.51
Cost of goods sold	-1.67	-2.61	-2.63	-3.34	-4.95	-7.08
Gross profit	0.77	0.89	2.63	3.48	5.18	7.43
Other operating income	0.40	0.32	0.35	0.37	0.39	0.41
Personnel expenses	-0.93	-0.81	-1.23	-1.60	-2.37	-3.40
Other operating expenses	-0.14	-0.54	-0.70	-0.89	-1.16	-1.51
EBITDA	0.11	-0.14	1.04	1.36	2.04	2.93
Depreciation & amortisation	-0.36	-0.41	-0.58	-0.76	-1.12	-1.61
Operating income	-0.26	-0.55	0.46	0.61	0.91	1.32
Net financial result	-0.01	-0.11	-0.12	0.34	0.48	0.56
Write-downs	-0.02	-0.02	-0.02	-0.01	0.00	0.00
EBT	-0.28	-0.67	0.33	0.94	1.39	1.88
Income taxes	0.13	-0.01	-0.06	-0.18	-0.26	-0.36
Minorities	0.00	0.22	0.15	0.09	-0.14	-0.15
Net income / loss	-0.15	-0.46	0.42	0.85	0.99	1.37
EPS	-0.03	-0.09	0.08	0.16	0.19	0.26
DPS	0.00	0.00	0.00	0.00	0.00	0.00
Share in total sales						
Revenues	100.00 %	100.00 %	100.00 %	100.00 %	100.00 %	100.00 %
Cost of goods sold	-68.44 %	-74.59 %	-50.00 %	-49.00 %	-48.90 %	-48.80 %
Gross profit	31.56 %	25.41 %	50.00 %	51.00 %	51.10 %	51.20 %
Other operating income	16.51 %	9.02 %	6.67 %	5.39 %	3.81 %	2.79 %
Personnel expenses	-37.88 %	-22.97 %	-23.40 %	-23.40 %	-23.40 %	-23.40 %
Other operating expenses	-5.87 %	-15.38 %	-13.37 %	-12.99 %	-11.41 %	-10.39 %
EBITDA	4.32 %	-3.93 %	19.90 %	20.00 %	20.10 %	20.20 %
Depreciation & amortisation	-14.81 %	-11.67 %	-11.10 %	-11.10 %	-11.10 %	-11.10 %
Operating income	-10.49 %	-15.59 %	8.80 %	8.90 %	9.00 %	9.10 %
Net financial result	-0.47 %	-3.21 %	-2.29 %	4.98 %	4.74 %	3.86 %
Write-downs	-0.66 %	-0.46 %	-0.31 %	-0.12 %	0.00 %	0.00 %
EBT	-11.62 %	-19.26 %	6.21 %	13.77 %	13.74 %	12.96 %
Income taxes	5.39 %	-0.35 %	-1.18 %	-2.62 %	-2.61 %	-2.46 %
Minorities	0.00 %	6.40 %	2.88 %	1.29 %	-1.37 %	-1.06 %
Net income / loss	-6.22 %	-13.22 %	7.91 %	12.44 %	9.75 %	9.44 %

Balance Sheet

in PLNm	2012	2013	2014E	2015E	2016E	2017E
Cash and equivalents	0.25	0.83	2.22	14.08	16.54	18.80
Financial assets	0.04	0.01	0.02	0.03	0.04	0.06
Inventories	0.72	0.61	0.89	0.69	0.96	1.28
Trade accounts and notes receivables	0.39	0.30	0.70	0.56	0.83	1.19
Other current assets	1.32	0.76	0.66	0.86	1.27	1.82
Current assets, total	2.72	2.53	4.50	16.22	19.65	23.16
Property, plant and equipment	2.99	2.66	2.86	2.91	2.96	3.01
Other intangible assets	0.78	0.67	0.52	0.66	0.96	1.35
Goodwill	0.04	0.02	0.01	0.00	0.00	0.00
Other assets	0.05	4.30	7.10	7.24	7.39	7.53
Deferred tax assets	0.15	0.14	0.06	0.00	0.00	0.00
Non-current assets, total	4.01	7.81	10.55	10.81	11.31	11.89
Total assets	6.73	10.33	15.05	27.03	30.96	35.05
Trade payables	1.48	1.83	0.58	0.69	0.96	1.28
Other short-term liabilities	0.82	1.13	1.70	2.21	3.28	4.70
Short-term financial debt	0.09	0.19	0.00	0.00	0.00	0.00
Pension provisions	0.03	0.03	0.05	0.06	0.09	0.13
Provisions	0.02	0.04	0.06	0.08	0.11	0.16
Current liabilities, total	2.44	3.23	2.39	3.04	4.45	6.27
Long-term financial debt	0.10	0.07	0.00	0.00	0.00	0.00
Other long-term liabilities	2.97	5.02	6.47	7.05	8.44	9.18
Deferred tax liabilities	0.03	0.04	0.00	0.00	0.00	0.00
Long-term liabilities, total	3.10	5.12	6.47	7.05	8.44	9.18
Total liabilities	5.54	8.36	8.86	10.09	12.89	15.46
Shareholders equity, total	1.19	0.76	5.12	15.96	16.95	18.32
Minority interests	0.00	1.22	1.07	0.98	1.12	1.27
Total liabilities and equity	6.73	10.33	15.05	27.03	30.96	35.05

Cash Flow Statement

in PLNm	2012	2013	2014E	2015E	2016E	2017E
Net income / loss	-0.15	-0.46	0.42	0.85	0.99	1.37
Depreciation & amortisation	0.36	0.41	0.58	0.76	1.12	1.61
Change of working capital	-0.19	1.42	-1.26	0.76	0.38	0.51
Others	0.22	0.03	0.06	0.08	0.04	0.05
Net operating cash flow	0.24	1.40	-0.20	2.44	2.53	3.54
Cash flow from investing	-1.01	0.04	-0.61	-0.94	-1.48	-2.05
Free cash flow	-0.77	1.44	-0.81	1.50	1.06	1.49
Cash flow from financing	0.39	-0.86	2.20	10.35	1.40	0.77
Change of cash	-0.38	0.58	1.39	11.86	2.46	2.26
Cash at the beginning of the period	0.63	0.25	0.83	2.22	14.08	16.54
Cash at the end of the period	0.25	0.83	2.22	14.08	16.54	18.80

Financial ratios

Fiscal year	2012	2013	2014E	2015E	2016E	2017E	2018E	2019E
Profitability and balance sheet quality								
Gross margin	31.56%	25.41%	50.00%	51.00%	51.10%	51.20%	51.30%	51.40%
EBITDA margin	4.32%	-3.93%	19.90%	20.00%	20.10%	20.20%	20.30%	20.40%
EBIT margin	-10.49%	-15.59%	8.80%	8.90%	9.00%	9.10%	9.20%	9.30%
Net margin	-6.22%	-13.22%	7.91%	12.44%	9.75%	9.44%	9.33%	9.00%
Return on equity (ROE)	-20.69%	-47.45%	14.14%	8.05%	6.00%	7.77%	9.06%	10.04%
Return on assets (ROA)	-2.09%	-3.39%	3.56%	1.88%	1.64%	2.31%	2.79%	3.34%
Return on capital employed (ROCE)	-3.20%	-7.83%	2.96%	2.05%	2.79%	3.72%	4.42%	5.22%
Economic Value Added (in PLN)	-0.69	-1.46	-1.24	-2.57	-2.65	-2.61	-2.63	-2.57
Net debt (in PLNm)	-0.08	-0.56	-2.20	-14.04	-16.49	-18.73	-21.36	-23.96
Net gearing	-6.54%	-73.71%	-42.94%	-87.97%	-97.26%	-102.21%	-106.50%	-108.00%
Equity ratio	17.75%	7.33%	34.00%	59.05%	54.76%	52.27%	50.96%	50.56%
Current ratio	1.12	0.78	1.88	5.33	4.42	3.69	3.39	3.12
Quick ratio	0.28	0.35	1.23	4.82	3.91	3.20	2.91	2.65
Net interest cover	-22.45	-4.86	3.85	-1.79	-1.90	-2.36	-2.68	-3.35
Net debt/EBITDA	-0.74	4.06	-2.10	-10.29	-8.10	-6.39	-5.64	-4.98
Tangible BVPS	0.22	0.14	0.98	3.07	3.26	3.52	3.86	4.26
CAPEX/Sales	63.27%	-1.14%	11.60%	13.80%	14.56%	14.11%	13.23%	13.01%
Working capital/Sales	5.46%	-36.85%	-0.58%	-11.58%	-11.58%	-11.58%	-11.58%	-11.58%
Cash Conversion Cycle (in days)	58	31	30	30	30	30	30	30
Trading multiples								
EV/Sales	6.65	4.64	3.10	2.39	1.61	1.12	0.87	0.69
EV/EBITDA	153.89	-118.29	15.58	11.93	7.99	5.55	4.30	3.39
EV/EBIT	-63.41	-29.79	35.22	26.80	17.85	12.32	9.49	7.43
P/Tangible BVPS	16.00	25.18	3.62	1.16	1.09	1.01	0.92	0.83
P/E	-121.29	-39.87	44.48	21.76	18.69	13.48	10.62	8.71
P/FCF	-23.96	12.84	-22.82	12.28	17.46	12.40	6.75	6.07

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The respective supervisory authority is:

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