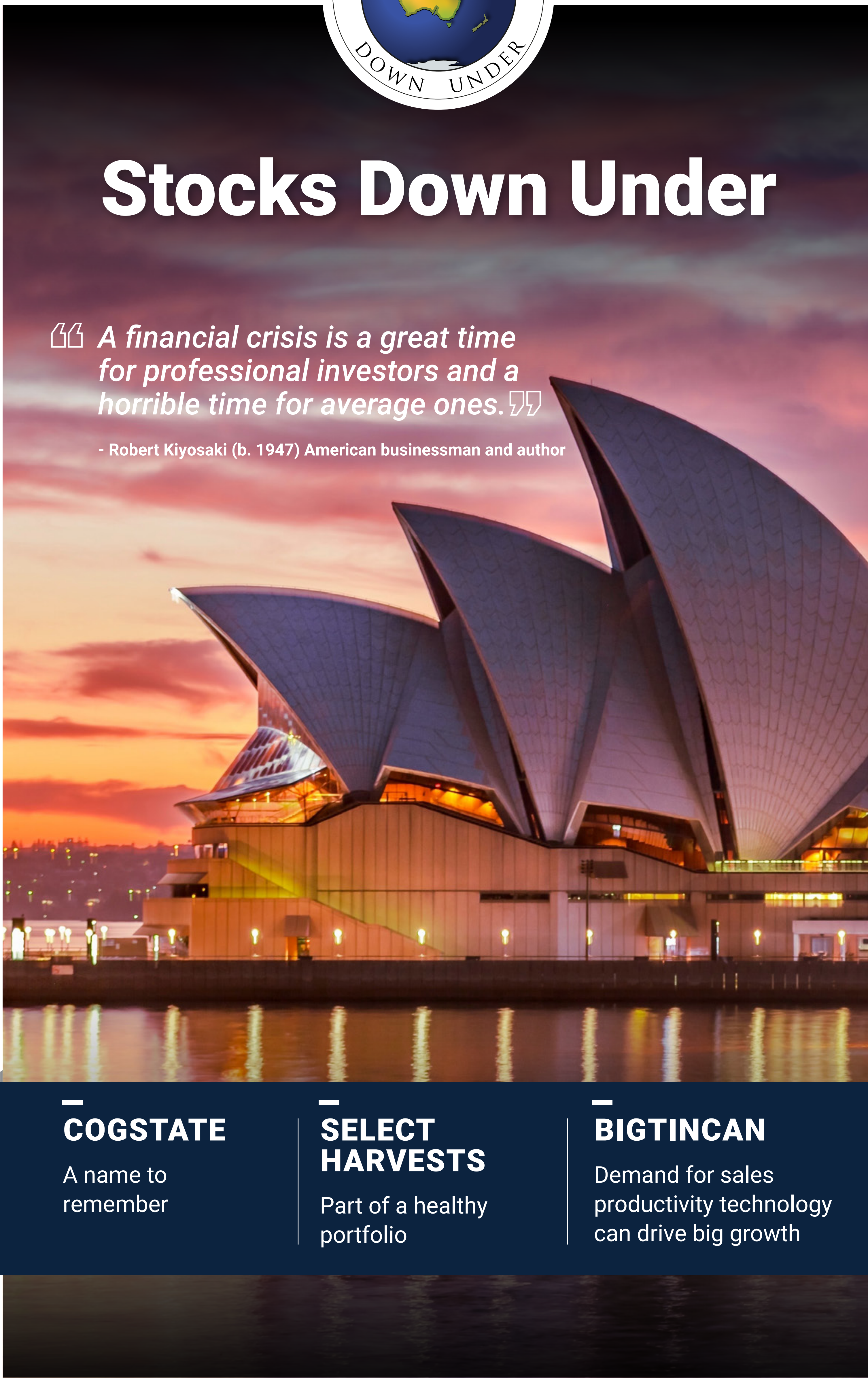
16 MARCH 2020

Stocks Down Under



A financial crisis is a great time for professional investors and a horrible time for average ones.

- Robert Kiyosaki (b. 1947) American businessman and author

COGSTATE

A name to remember

SELECT HARVESTS

Part of a healthy portfolio

BIGTINCAN

Demand for sales productivity technology can drive big growth

COGSTATE

A name to remember

Stocks Down Under rating: ★★★★

ASX: CGS
Share price: A$ 0.395
Market cap: A$ 66.7m

For more than 20 years, Cogstate, a leader in neuroscience and computerized cognitive testing based in Melbourne, has been on the cutting edge of enhancing brain health. Perfected through hundreds of clinical trials, Cogstate's technology studies behavioural, memory and social-emotional patterns within patients. And with electronic clinical outcome assessments (eCOAs) making diagnosis more accurate and affordable, Cogstate has positioned itself at the heart of a market that's poised for exponential growth. And while investors are just starting to pay attention – with the stock surging off its July lows – we believe now is the time to book your appointment.

READ MORE

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Stocks Down Under rating: ★★★★

ASX: SHV
Share price: A$ 5.68
Market cap: A$ 546m

As an affordable 'superfood,' almonds are a great source of protein, fibre, healthy fats and Vitamin E. And it's been proven – eating a handful each day can improve heart-health. However, over the last month, shares of Select Harvests, a vertically integrated producer of natural health foods based in Melbourne, have been driving investors nuts. The stock hit a four-year high of $9.24 on 7 February 2020, only to plunge by 31% in the weeks to follow. But with the coronavirus overshadowing the company's strong fundamentals, we believe Select Harvests is the perfect snack to add to your portfolio.

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BIGTINCAN

Demand for sales productivity technology can drive big growth

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ASX: BTH
Share price: A$ 0.50
Market cap: A$ 153M

Sydney-based software company Bigtincan has a growth story that is as interesting as its name. It provides an AI-powered platform that helps sales reps worldwide more effectively engage with customers and prospects. Its sales enablement automation tools are being rapidly adopted by a wide range of sectors including energy, financial, government, life sciences, manufacturing, retail, technology and telecommunications. After reaching its all-time high of $1.01 on 14 February the share price has been abruptly cut in half. The can-half-full investor, however, will recognize that the growth prospects remain strong.

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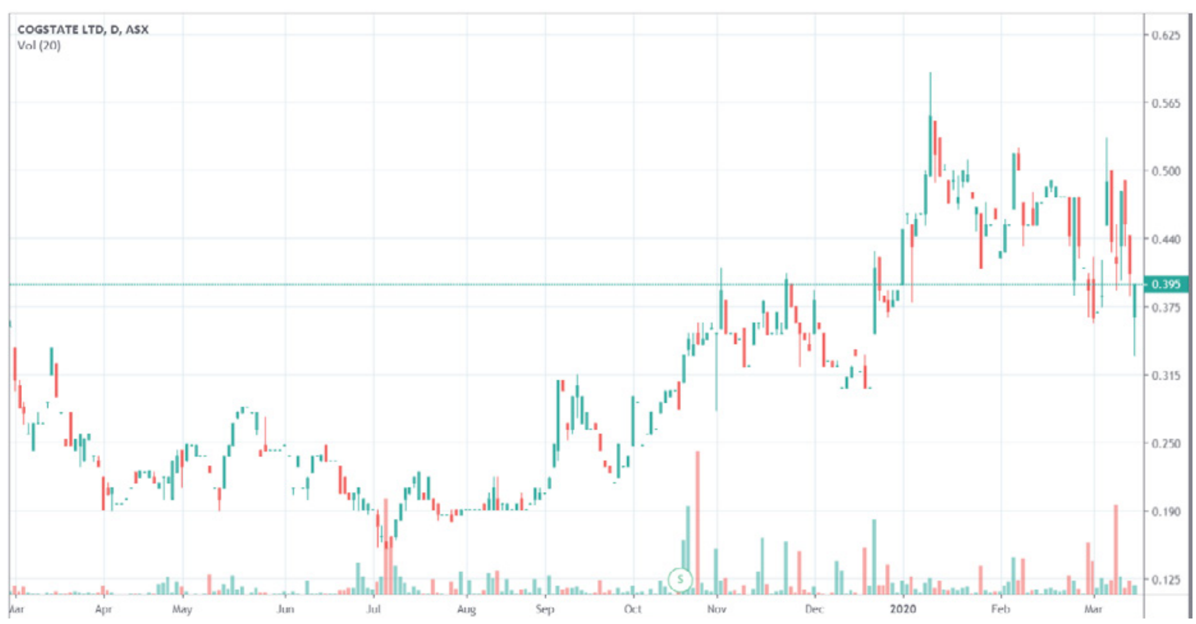

Source: Tradingview

Evaluating, diagnosing and treating the portfolio

In FY19, Cogstate's business struggled – with revenue declining across all segments and EBITDA continuing to decelerate. To stem the tide, CEO Brad O'Connor increased R&D spending within Cogstate's clinical trial's division, dissolved the firm's Cognigram commercial team and sourced partners to develop more advanced screening technology. The strategic pivot paid off, as phase three trials – which compare clinical results to treatments currently on the market – of over 1,700 patients with treatment-resistant depression delivered positive results. And within Cogstate's paediatric and rare disease clinical trials, the firm succeeded with seven multi-study programs – while it also plans to address Parkinson's disease and other degenerative diseases in the near future.

Partnering with the Alzheimer's Drug Discovery Foundation (ADDF) in 2020, an American non-profit organization based in New York, Cogstate helped develop a smartphone application that administers tests on iOS and Android devices. Once the app goes live – which is expected by the end of 2020 – Cogstate will pay a 4% royalty to the ADDF on the first $150m in revenue and 2.5% thereafter. However, the firm was also reimbursed $1.36m by the ADDF for its role in the development and scientific validation process.

Clinically proven demand

As baby boomers transition into the latter stages of their life, early detection of cognitive impairment has become a top priority for both individuals and governments. Moreover, the global cognitive assessment and training market continues to expand, with the World Health Organization (WHO), a specialised agency of the United Nations, reporting that 50 million people suffer from dementia, while 10 million new cases are reported each year. And with Cogstate leading the way in monitoring and assessing the developments, the firm is poised to be a top solutions-provider for years to come.

Cogstate's esteemed reputation has also caught the attention of environmental, social and governance (ESG) investors. On 8 July 2019, Australian Ethical, a wealth management firm based in Sydney, purchased $4m in shares through a private placement. On 2 September 2019, Eisai, a global health-care network based in Tokyo, Japan, invested $2.86m. The capital raises not only shored up Cogstate's balance sheet, but the proceeds were used to increase the company's footprint in Japan and to develop new healthcare technology. On 24 September 2019, Cogstate signed a licensing deal with Eisai – which allows the Japanese firm to use Cogstate's technology for cognitive screening across the country. Eisai will also pay Cogstate an upfront royalty of US$1m to finance future product development and fund commercial expansion across Japan.

Show me the money

On 25 February 2020, the company released its H1 FY20 results. Clinical trial contracts increased by 169% to US$26.9m, with sales more than doubling in the December quarter. However, consolidated revenue fell 12.8% to US$9.69m, while NPAT fell 4.6% to US$2.06m. But capitalizing on the Eisai partnership, healthcare revenue increased by 457% to US$1.3m, while research solutions increased by 16.4% to US$136k. Management also decreased overhead costs by US$1.5m, while contract revenue – which is received up front but recognized in future periods – hit US$37.2m at the end of the period. The strong backlog tells us that demand is picking up for Cogstate's services.

We expect clinical trial revenue to expand significantly in FY21. Rare disease indicators continue to spur growth, while its Alzheimer's division is poised for a strong rebound. And with a diversified pipeline of services and a growing list of domains supporting its computerized cognitive tests, Cogstate has competitive advantages that few competitors can rival.

Furthermore, its real-time data capture is essential for biopharmaceutical and academic research, which only increases its future earnings prospects. We're bullish on Cogstate. And with the stock down by 61% since its 2017 high of $1.16 – we believe now is the perfect entry point.

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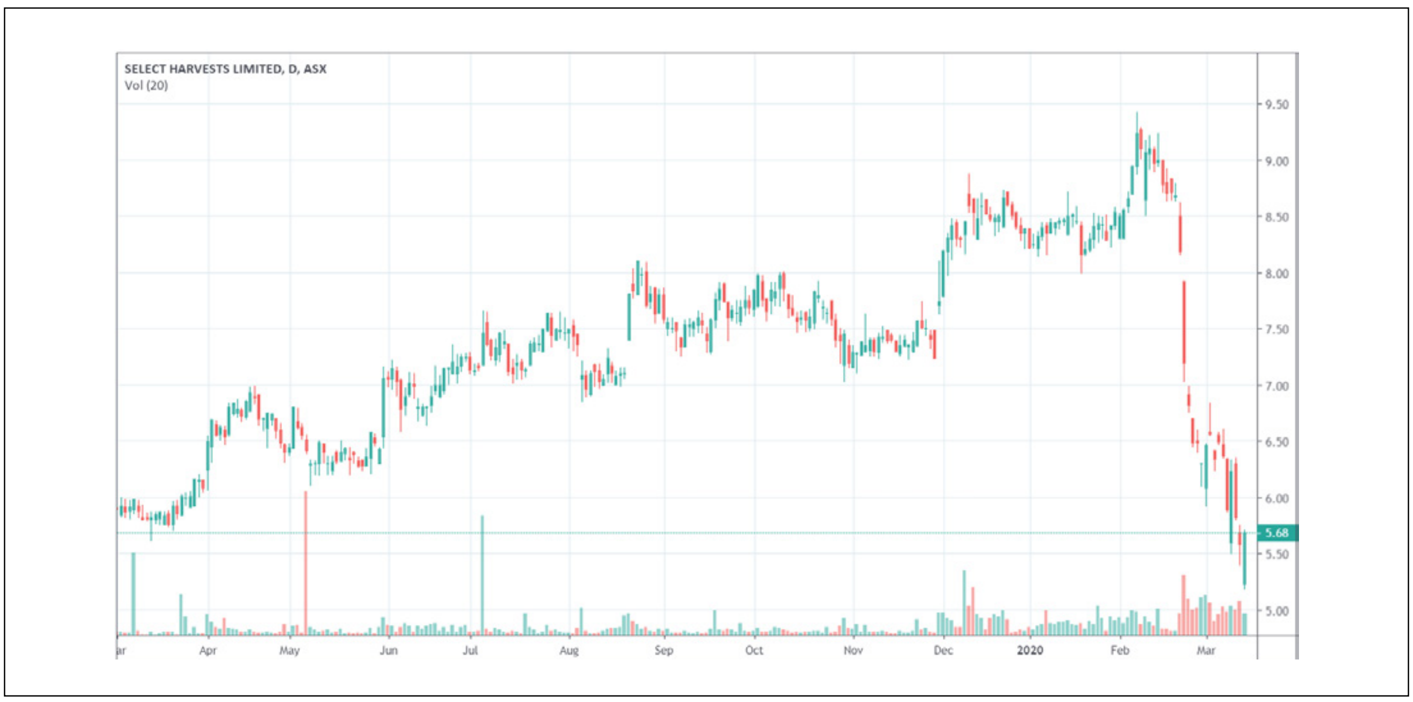

Source: Tradingview

An almond a day keeps the doctor away

According to Harvard University, an American Ivy League research institution based in Cambridge, Massachusetts, general almond intake decreases inflammation, improves insulin resistance and promotes healthy blood circulation. And by reducing low-density lipoprotein (LDL) – also known as "bad' cholesterol – almonds also lower the risk of heart disease. Researchers in Sweden found that patients who consumed almonds twice per-week, saw a 20% reduction in heart-failure risk.

And with consumers becoming more health-conscious, the Australian nut industry is expected to grow by 4.5% p.a. over the next five years. The Almond Board of Australia reported that almond exports hit a record 60,895 tonnes in FY19, with Asian countries – China, India, Vietnam, Thailand, Indonesia and Japan – showing increased appetites for healthy snacks. Capitalizing on the strong demand, Select Harvests increased its footprint within these regions and built material relationships with trade partners and governments. Also driving consumption, the Australian Nut Industry Council continues to educate consumers on the health benefits of almond milk. As a dairy-free alternative, almond milk is low in calories, low in sugar and provides a gluten-free option for vegans and vegetarians.

The market in a nutshell

Aligned within a growing industry, Australia is the world's second largest almond producer – at 7% of global production – ahead of Spain, Iran and Italy. And due to ongoing trade tensions between the United States and China, Australia has become the go-to choice for Chinese consumers. And given that 95% of Chinese almond imports come from the U.S., the supply-chain shift will be a significant tailwind for Select Harvests in the coming years. During its crop update on 21 August 2019, Select Harvests told investors that it has 7,697 hectares of Australian almond orchards, with 35% of the territory primed for harvest over the next eight years. Moreover, almond demand was robust in FY19 – with volume up 44.5% to 22,690 tonnes – and the average price per kilogram increasing by 6.8% to $8.60.

At its AGM on 21 February 2020, Select Harvests announced it may expand its macadamia nut operations. Providing synergies with its Lucky brand – which already offers macadamia nuts within its baking and cooking products – the prospective expansion could add another layer of growth to the company's core portfolio. And like almonds, China has a limited supply of macadamias. So, if its trade relationship with the U.S. continues to deteriorate, we believe Select Harvests will be a significant beneficiary.

But still confronted with macro issues, management warned on 14 February 2020 that the coronavirus could hurt almond demand in FY20. However, they emphasized that there haven't been any disruptions to Select Harvests' business. Inventory is strong, harvests remain on-schedule, and its 2020 marketing campaign has commenced across India, the Middle East and Europe.

The numbers tell the true story

In FY19 – which compares the 12 months ended 30 September to the 12 months ended 30 June – revenue increased by 37.7% to $289.5m, while NPAT more than doubled to $53m. Costs declined by 16%, while Select Harvests' EBITDA margin increased from 24.6% to 31.9%. The balance sheet remained strong, with the company reducing net debt by more than 50%, while operating cash flow came in at $80.3m.

Because of this, we believe February's sell-off was a technical blip that doesn't reflect Select Harvests' underlying fundamentals. The company is poised to capture significant market share in the coming years and the weakness in the Australian dollar only fuels demand for future exports.

Furthermore, Select Harvests continues to expand its B2B partnerships and its P/E of 15x (NTM) offers an attractive entry point for potential investors, in our view. But most importantly, Select Harvests' balance sheet remains as healthy as its products – which will allow the company to weather any potential disruption from the coronavirus.

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Share price chart

Source: Tradingview

Strong revenue growth and value-added acquisitions

The bar was set high after achieving 51% revenue growth in FY19 while releasing 100 versions of its software and implementing 125 product enhancements. BTH posted a net loss as a result of heavy investments in product development and infrastructure support, but the loss narrowed to $4.1m on $19.9m in revenue.

Revenue again jumped 51% in 1H FY20 to $14.3m including remarkable 72% growth in its key North American market, which accounts for more than 80% of overall revenue. Annual recurring revenue (ARR), the key performance metric of the business, increased 55% and the customer retention rate improved from 87% to 89%. The performance was also highlighted by some big contract wins including a three-year, $2.8m agreement with global beauty retailer Sephora USA. Sephora enlisted Bigtincan's Zunos product to build a mobile learning platform for its retail sales team. It also secured a two-year, $6.2m deal with U.S. IT services company DXC Technology Services.

Aside from the strong organic growth, the company has expanded its reach by making several value-added acquisitions. In 2018, it acquired microlearning and training technology specialist Zunos and expanded vertically by acquiring FatStax, an SKU-based dynamic catalogue tool used in manufacturing and retail. Last year it bought U.S. inside sales technology firm Veelo, which instantly added approximately $1.1m in annual recurring revenue (ARR). It also acquired U.S. mobile service enablement company Asdeq Labs to enhance its Australian market position, and most recently, U.S. document automation provider Xinnovation to augment its growth opportunities in the financial sector.

More IT spending going towards sales enablement tools

According to Aragon Research, the global sales enablement platform market is expected to reach US$5bn by 2021. The market is a subset of the broader global sales technology market that includes customer relationship management (CRM), content management (CM) and cloud office suites, which is forecast to become a US$80bn market by next year. By this time 15% of all sales technology spending is expected to go towards sales enablement technology, more than twice the allocation seen in 2017.

Not only does Bigtincan have a fantastic revenue mix from many different end markets, but over 90% of revenue comes from subscription and support licenses. As these contracts are typically made 12 months in advance, this provides a well-known, diversified ARR stream that is an ideal trait for Tech investors.

Management has projected organic revenue growth of 30% to 40% for the remainder of FY20 driven by new contract wins and strong execution of its business strategy across all geographies and industries. It should also start to benefit significantly from its new partnership with U.S. data analytics company Databricks. Databricks offers a market leading data science and AI technology platform and will bring value to Bigtincan's platform by adding machine learning models that can be tailored to its enterprise customers.

Growing customer base of major global companies

Bigtincan has over 400 customers around the world including major companies like Anheuser Busch, ANZ Bank, AT&T, Mastercard, Merck and Nike. It has an established business in North America and a developing presence in the U.K. and Europe that has brought its licensed user based to over 200,000.

Further growth at Bigtincan will come from enhanced platform capabilities and more licensed users across its well diversified industry mix. The company is very well positioned to benefit from the rapid growth in the sales enablement technology market driven by strong demand from organizations that want to improve their sales team performance.

Given the strength of the company's recurring revenue business model, it shouldn't be much longer before revenue outpaces expenses and positive bottom line growth begins. Shares of Bigtincan are trading around 4x EV/Revenue, a multiple we believe is warranted given the company's superior growth profile.

Pitt Street Research Pty Ltd

95 Pitt Street, Sydney, NSW 2000, Australia

Pitt Street Research Pty Ltd provides issuer-sponsored research for Small & Mid Cap companies and is founded on more than 40 years of combined experience researching companies in a range of different sectors.