STOCKS DOWN UNDER

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ASX Top 200 Stocks Down Under

"Intellectual property is the oil of the 21st century."

- Mark Getty (b. 1960), Chairman & co-founder of Getty Images

IPH

In a lucrative space

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Stocks Down Under rating: ★★★★

ASX: IPH
Market cap: A$2.0BN

52-week range: A$6.86 / A$10.42
Share price: A$9.34

We'll admit that this isn't the first time we've used a quote along the lines of saying an industry is 'the oil of the 21st century'. But intellectual property is a peculiar space to be in with no shortage of companies working on the next big thing in their industry, seeking to protect what they're working on (or just want to work on someday). And IPH (ASX: IPH) is one of the few ways ASX investors can gain exposure to this space.

Share price chart

Source: Tradingview

Turning a brilliant past into an even better future

IPH is a patent and trademark law firm that listed in November 2014 at $2.10 a share. At the time it listed, it was just a holding company for Spruson & Ferguson, an IP firm with offices in Sydney, Singapore, Kuala Lumpur and Shanghai and traced its origins back to the 1880s. Since then, the company has made a name for itself through roughly a dozen acquisitions. Some of the most notable include then fellow ASX listee such as Xenith, which it competed with other companies for, and more recently Canadian firm Smart & Biggar. The latter was its first outside the Asia-Pacific region. IPH is well and truly covered Down Under, boasting a 35% market share.

It has not been all smooth sailing for the company's share price since listing, but it has been in recent months, up 6% while the ASX 200 is down 8%. Why has it held up? We think there are two key reasons. First, the perception by investors that it is inflation proof. Many companies on the ASX face the no-win situation of raising prices but losing customers or keeping prices (and customers) while losing profit margins. Professional services firms such as IPH do not have this problem as they can just raise prices. And for would-be clients it's a case of 'take it or leave it'. Go for the former option and the process of filing and being granted a patent typically takes 2.5-3.5 years. Being inflation-proof has contributed to the second reason why IPH stock has held up: The company had a pretty impressive FY22 result.

Costs and earnings are growing, but the latter is stronger

IPH delivered revenue of $385.1m (up 6%) and EBITDA of $115.9m (up 2%). Its statutory NPAT was $42.6m which was actually down 2%, although underlying NPAT was 14% higher at $86.7m. The difference between the two was a non-cash write down of two brands, one which was integrated and the other that was divested. It declared at 16cps dividend which was 3% higher than FY21. In an environment where many other companies were hit by rising costs, particularly as Dominos (ASX: DMP) and Kogan (ASX: KGN), these results were good enough. Growth was stronger in Asia, including in China (but excluding Hong Kong).

IPH's future outlook was good as well. Although the company did not issue formal guidance for FY23, it unveiled the Smart & Biggar deal and hinted at more acquisitions in the long term, targeting fragmented markets. In media interviews, CEO Andrew Blattman mentioned Canada, South America and Africa, as candidates but not the USA.

IPH's is trading at 13.4x EV/EBITDA and 21.7x P/E for FY23 which are above average but not excessively. Consensus estimates suggest solid growth for FY23 with $491.9m revenue and $159.7m EBITDA which would be up 28% and 38% from FY22. Looking to FY24, $533.7m revenue and $169.7m EBITDA which is more moderate but still 6.2% and 8.5% respectively. The company's PEG ratio does look excessive and suggest it is over-valued relative to its growth at 3.5x. But its EV/EBITDA to EBITDA growth ratio is just 0.49x which suggests it is under-valued relative to its growth.

Our verdict

There are plenty of things in IPH's favor. Clearly the company is in a lucrative industry and has managed acquisitions and their integration well even though there's been a significant volume of them. It is evidently resilient in the face of inflationary pressures and is expecting significant growth in the years ahead.

Nonetheless, there are risks that investors should be aware of. Of course, these future markets IPH has alluded to could be lucrative opportunities, but certain jurisdictions could come with significant sovereign risk. It is also possible that the company could be hit by degraded economic conditions or potentially government cuts to the sciences because this will disincentivize investment in this space. In the company's favor is that it has not issued formal guidance but there could be a reaction if it significantly misses consensus estimates. One other thing to be aware of is that Andrew Blattman recently sold 400,000 shares for $3.6m. The excuse was a tax bill after being issued shares under the Company's Long Term Incentive Plan, one that is reasonable in its own right, but investors should still be aware of that. He still owns 2.1m shares, worth 0.98% of issued capital along, with ~340k performance rights, and made the sale after its results.

But we think IPH has been de-risked by its performance in FY22, a period where inflation has begun, and it has proven that it is a company resilient to economic conditions. And clearly, the company thinks through its acquisitions very well, not just buying other companies for the sake of planting its flags in the ground. So, it's four stars from us.

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