



23 January 2017

Investment Ideas

Integral Diagnostics (IDX): Set for Market Rebound

Off the back of a disappointing FY16 which proved to be a tough market for the Australian diagnostic imaging industry, we believe that IDX looks set to improve as short term headwinds pass.

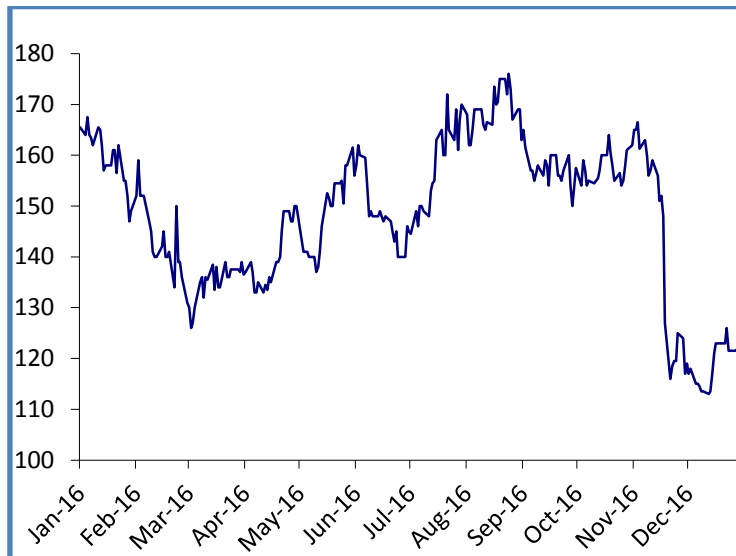
The IRESS consensus target price of \$1.53 indicates some 24% upside potential relative to IDX's current share price of \$1.23. When added to an IRESS consensus dividend yield of ~6%, we calculate that IDX offers total potential upside of around 30%.

Challenging Market Conditions:

- **Integral Diagnostics reported FY16 results which were well below prospectus forecasts, however in line with revised guidance. While overall performance was subdued, IDX still managed to outperform the key markets in which it operates.**
 - o Patient examinations grew 4.8% against industry growth of 3.7% in the states it operates, highlighting IDX's geographical advantage and brand awareness.
 - o Potential changes to the Government regulatory framework was cited as a key driver for slowed industry growth.
 - As over three quarters of IDX's patients are reimbursed by the government, changes to the bulk-billing system are likely to have a material impact on revenue, should they eventuate.
 - Delays to any changes have been postponed until a formal review of the system has been carried out which is expected to provide a greater level of certainty.

A Bright Future:

- The overall trend for diagnostic imaging is rising, and Medicare data from 1 July 2016 to 30 November 2016 indicates that overall 1H17 patient numbers (both nationwide and within IDX's addressable market) are likely to exceed previous half years.
 - o Following recent trends, IDX looks well placed to capitalise on the recent growth in patient numbers by its strong industry position which contributed to above market growth in FY16.
 - o As IDX relies on referrals from medical professionals, increased competition may potentially impact patient growth numbers despite the rising demand for diagnostic imaging services.
- The recent acquisitions of Western District Radiology and the remaining 50% stake of its joint venture in South West MRI in May 2016 are expected to generate revenues of \$4.3m and EBITDA of \$1.2m. The acquisitions are earnings accretive from FY17.
- In November 2016 IDX renewed and expanded its contract with Western Australian Country Health Services to provide radiology services in regional WA. The renewal will add revenue of \$49.8m during the life of the 5 year contract.
 - o The acquisitions and contract renewal will continue to enhance IDX's competitive advantage by geographical location and scale advantages.
- In the longer term, the overall Australian healthcare industry is set to benefit from tailwinds on the back of an aging Australian population and rising levels of chronic disease.

IDX share price history (23 January 2016 - Present) (A\$cps)


IDX's share price has not yet recovered from its decline off the back of lower than expected industry demand. Despite short term headwinds, industry demand looks to be recovering despite being lower than historical averages. Being the largest pure play diagnostic imaging provider in Australia, IDX looks well positioned to capitalise on the demand, however increased competition may potentially impact IDX's patient referrals.

IDX currently trades on an FY17 PE ratio of 11.17x relative to a peer average of 14.41x based on IRESS consensus estimates.

Source: IRESS, State One Stockbroking

Investment Data	
Share Price (\$)	1.24
Ord Shares (m)	145
Market Cap (\$'m)	179.9
EV (\$'m)	224.8
Net Debt (\$'m)	44.9
Average Daily Vol (6 mths)	89,099

EPS Data	FY16	FY17F	FY18F	FY19F
EPS (c)	11.90	11.17	12.08	12.98
PER (X)	10.42	11.10	10.26	9.55
DPS (c)	4.00	7.75	8.15	9.17
DPS yield (%)	3.23	6.25	6.57	7.40

Substantial Shareholders (%)	
Investors Mutual Limited	8.12
SG Hiscock & Company	6.20
Adam Smith Asset Management	5.83
IOOF Holdings Limited	5.70
Regal Funds Management Pty Limited	5.53

Source: IRESS, State One Stockbroking



Warnings and Disclosures

These Research products and their contents at all times remain the property of State One Stockbroking Ltd ("State One") and as such cannot be reprinted, distributed, copied, posted on the internet, in part or whole, without written prior approval from State One. The contents of this document constitute General Advice and have been prepared without taking account of your investment objectives, financial situation or needs. Because of that you should, before taking any action to acquire or deal in, or follow a recommendation (if any) in respect of any of the financial products or information mentioned in these documents, consult your own investment advisor to consider whether that is appropriate having regard to your own objectives, financial situation and needs. While State One believes information contained in these documents are based on information which is believed to be reliable, their accuracy and completeness are not guaranteed and no warranty of accuracy or reliability is given or implied and no responsibility for any loss or damage arising in any way for any representation, act or omission is accepted by State One or any officer, agent or employee of State One. If applicable, you should obtain the Product Disclosure Statement relating to any relevant financial product mentioned in this document (which contains full details of the terms and conditions of the relevant financial product) and consider it before making any decision about whether to acquire the financial product. The directors and associated persons of State One may have a long or short interest in the financial products discussed in these documents and they may earn brokerage, commissions, fees and advantages, pecuniary or otherwise, in connection with the making of a recommendation or dealing by a client in such financial products. Additionally, State One may earn fees due to having been appointed advisors to, or may be undertaking or about to commence research relating to any of the companies mentioned here.

Alan Hill
Executive Chairman
Phone: +61 8 9288 3388
ahill@stateone.com.au

Morris Levitzke
Equities Advisor
Phone: +61 8 9288 3315
mlevitzke@stateone.com.au

Alexander Bax
Equities Advisor
Phone +61 8 9288 3340
abax@stateone.com.au

Ric Heydon
Equities & Derivatives Advisor
Phone: +61 8 9288 3307
rheydon@stateone.com.au

Graeme Johnson
Equities & Derivatives Advisor
Phone: +61 8 9288 3316
gjohnson@stateone.com.au

Daniel Chiew
Analyst
Phone: +61 8 9288 3349
dchiew@stateone.com.au

Mark Sullivan
Institutional Dealer
Phone: +61 2 9024 9134
msullivan@stateone.com.au

Yitz Barber
Equities Advisor
Phone: +61 2 9024 9107
ybarber@stateone.com.au

David Zhang
Equities Advisor
Phone: +61 2 9024 9130
dzhang@stateone.com.au

Thomas Tan
Equities Advisor
Phone: +61 2 9024 9131
ttan@stateone.com.au

Tammie Wong
Equities Advisor
Phone: +61 2 9024 9133
twong@stateone.com.au

David Brennan
Senior Investment Analyst
Phone: +61 2 9024 9142
dbrennan@stateone.com.au