

# INSTEM

## SOFTWARE AND COMPUTER SERVICES

**INS.L**

294p

Market Cap: £46.7m

**SHARE PRICE (p)**


12m high/low

330p/141p

Source: LSE Data

**KEY INFORMATION**

Enterprise value	£43.6m
Index/market	AIM
Next news	Interims, Sep-18
Gearing	N/A
Interest cover	N/A

 INSTEM IS A RESEARCH CLIENT OF  
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**ANALYSTS**

Gareth Evans  
 +44 (0) 20 7781 5301  
 gevens@progressive-research.com

Blaine Tatum  
 +44 (0) 20 7781 5309  
 btatum@progressive-research.com

## FY 18E has started well, SEND accelerating

Instem's trading update for the six months ending June 2018 reveals that FY 18E has started well and that the board is confident that their full-year expectations will be met. Most businesses made a positive contribution to group financial performance. SEND was the standout performer, orders more than doubled during the period. In our view, the overall tone of the update is optimistic and the outlook statement positive. We make no changes to estimates following the release.

- H1 18 trading in line, on track for the full-year:** H1 18 trading was in line with management's expectations. Closing net cash was confirmed at £3.7m. This is £2.5m higher than H1 17 and a £600k improvement on FY 17. For H2 18E, management signalled their expectation that the volume and value of SEND contracts will increase in the second half and are expected to be "significantly" ahead of H2 17. The SEND market is benefitting from the US FDA's decision to require all Investigational New Drug ("IND") studies to be SEND compliant from Dec-17 onwards. The strong pipeline for H2, alongside continuing growth in outsourced services revenues, make management confident in meeting their FY 18E expectations. With the ongoing shift towards SaaS delivery, earnings visibility is also expected to improve.
- Positive contribution from most business areas, SEND a highlight:** The announcement reveals positive contributions from most business areas, and several new contract wins - note the Jun-18 Samarind RMS contract win with a Fortune 500 customer. Instem is also increasing investment in the Alphadas suite to improve its competitive positioning. However, for us, SEND performance is a highlight of the announcement.
- SEND volumes are accelerating...H1 18 saw 103 orders won for SEND, vs 47 and 65 for H1 and H2 17 respectively.** H1 18 also saw more SEND outsourced-service deals signed than the whole of FY 17. The group is also seeing increasing success in adding new clients. The new contracts came from 50 unique clients (vs 32 in H1 17) and will contribute to group financials from H2 18 onwards.
- ...and so are contract values:** H1 18 total contracted value of SEND-related new business was up 190% YoY, with outsourced services particularly strong. The group is seeing commercial traction with customers looking for long-term outsourcing capacity, and also short-term catch up projects. In this note we provide further detail on Instem's SEND positioning and the market opportunity.

FYE DEC (€M)	2016	2017	2018E	2019E	2020E
Revenue	18.3	21.7	23.0	25.2	27.4
Adj EBITDA	1.3	3.0	3.6	4.5	5.0
Fully adj PBT	0.5	2.2	2.6	3.4	3.8
Fully adj EPS	2.0	10.1	11.5	15.3	17.0
EV/Sales	2.4	2.0	1.9	1.7	1.6
EV/EBITDA	34.8	14.7	12.2	9.6	8.6
PER	145.5	29.2	25.6	19.2	17.3

Source: Company Information and Progressive Equity Research estimates

## Impressive track record and market position in SEND

In our view, Instem's SEND performance is a major highlight of the trading update. Instem has an impressive track record in winning SEND business. Following over ten years of development and investment, the group goes to market with a strong product offering and has leveraged its platform into a leading market position. The market opportunity remains vast and Instem seems well-placed to capture emerging growth opportunities.

### About SEND

The Standard for Exchange of Nonclinical Data ("SEND") specifies the method to present the results of studies of non-clinical data in a consistent format to the US Food and Drug Administration ("FDA"). SEND is the required format for studies that commenced after December 17, 2016 that support the New Drug Application ("NDA") phase of drug development.

In December 2017, the FDA extended the requirement for SEND compliance to all new Investigational New Drug ("IND") applications. As noted in today's announcement, management believe this has driven additional demand for SEND Services.

Failure to comply with the SEND Mandate can result in the FDA's technical rejection or refusal to file a submission

### The Instem product offering

With a product suite that has been under continuous development since 2005 and having first commercially launched in 2006, Instem has a broad offering in SEND. The group's software range includes tools to manage, create, analyse and visualise SEND datasets, which underpin a broad range of services designed to further assist study management.

Key software products include:

- **SEND Submit™**, a suite of integrated tools and services for the creation and management of SEND datasets.
- **SEND View™**, an application to facilitate the review of SEND datasets
- **SEND Explorer™**, a web-based application providing advanced single and multi-study visualization and analysis
- **SEND Trial™**, a tool to reduce trial design time

Instem has a broad product offering in SEND services, with solutions tailored for each stage of the SEND lifecycle. This is summarised in the following table.

## Instem – SEND services offering

Client type:	Education	Planning	Selection & Implementation	Live with SEND
	Organisations that are still learning about the standard and understanding the potential impact SEND will have on their processes	SEND is understood, internal work groups have been formed, requirements for addressing the standard are being developed	Organisational requirements are finalised, SEND providers are being evaluated, studies identified for conversion, solution deployment is underway	Solutions for creating, managing and storing SEND data have been implemented in the form of software, services or a mix of both
<b>Services:</b>				
SEND training courses	●			
SENDReady™ Organisational Consulting		●		
Study Conversion Services			●	●
SEND Dataset Verifications			●	●
General SEND Consultancy	●	●	●	●
Complete SEND Outsourcing	●	●	●	●

Source: Company data

## Impressive track record and market position in SEND

In our view Instem has an impressive track record of new business wins in SEND. As a result, it has established a strong market position in the space.

As noted in the FY 17 results release (*March 2018*) and re-iterated in today's trading update, management believe the group continues to dominate the SEND technology market and take the majority of new business placed in SEND services contracts. At the time of the FY 17 results, the group announced a total of 92 customers for its SEND technology and/or out-sourced services. This includes nine of the top ten preclinical Clinical Research Organisations ("CRO"s) and 20 of the world's top 25 global pharmaceutical companies. In total, clients at 45 sites across 15 countries have implemented Instem's SEND software offering. With around four months having elapsed since the FY 17 results release, we believe the customer base and the number of active sites to be higher than the figures reported at that time.

Positive commentary on the SEND business and market opportunity has been a feature of recent announcements from Instem. The following table summarises news flow from the company on the topic.

## Instem – recent SEND news flow

DATE	ANNOUNCEMENT
23/7/2018	<p><b>Trading Update</b></p> <p>103 orders won in H1 18 vs 47 in H1 17</p> <p>Total contracted value of SEND-related new business grew c190% over H1 17</p> <p>More SEND outsourced services deals signed in H1 18 than for entire FY 17.</p> <p>“The Company continues to win the overwhelming majority of all new business quoted for”</p>
26/03/2018	<p><b>Final Results, SEND Contract Extension</b></p> <p>"Instem continues to dominate the SEND technology market"</p> <p>"We have won the majority of out-sourced services contracts"</p> <p>92 customers for SEND technology and/or out-sourced services.</p> <p>Top-5 pre-clinical CRO extends 2018 SEND outsourced services contract</p>
26/03/2018	<p><b>SEND Contract Extension &amp; Update</b></p> <p><i>Top five preclinical CRO extends 2018 SEND outsourced Services contract to over \$0.5 million</i></p> <p>25 orders for technology-enabled SEND services during the two-month period ended 28 February 2018, compared with 6 orders for the equivalent period in 2017</p>
16/01/2018	<p><b>Contract Win</b></p> <p>SEND outsourced services contract win with a top five global nonclinical CRO.</p>
16/01/2018	<p><b>Trading Statement</b></p> <p>SEND standard now in force, stimulated demand for more technology-enabled outsourced service orders.</p>
26/09/2017	<p><b>Half Yearly Report</b></p> <p>"Continued increase in market share in SEND services, winning the majority of technology and outsourced services contracts"</p> <p>54 orders from 38 organisations received during the first seven months of 2017, of which 19 were first-time Instem customers. Now 71 SEND customers.</p>
28/03/2017	<p><b>Final results</b></p> <p>"Secured the majority of SEND-related technology and outsourced services contracts placed in the market"</p> <p>Over 50 SEND-related contracts secured in 2016</p>
16/01/2017	<p><b>Post Period End Update</b></p> <p>The Company won over 30 SEND-related contracts for its software solutions and technology-enabled out-sourced services during the second half of 2016. The largest of these wins was with a top 10 global pharmaceutical company, which has purchased Instem's entire submit™ solution suite.</p>

**Source: Company data**

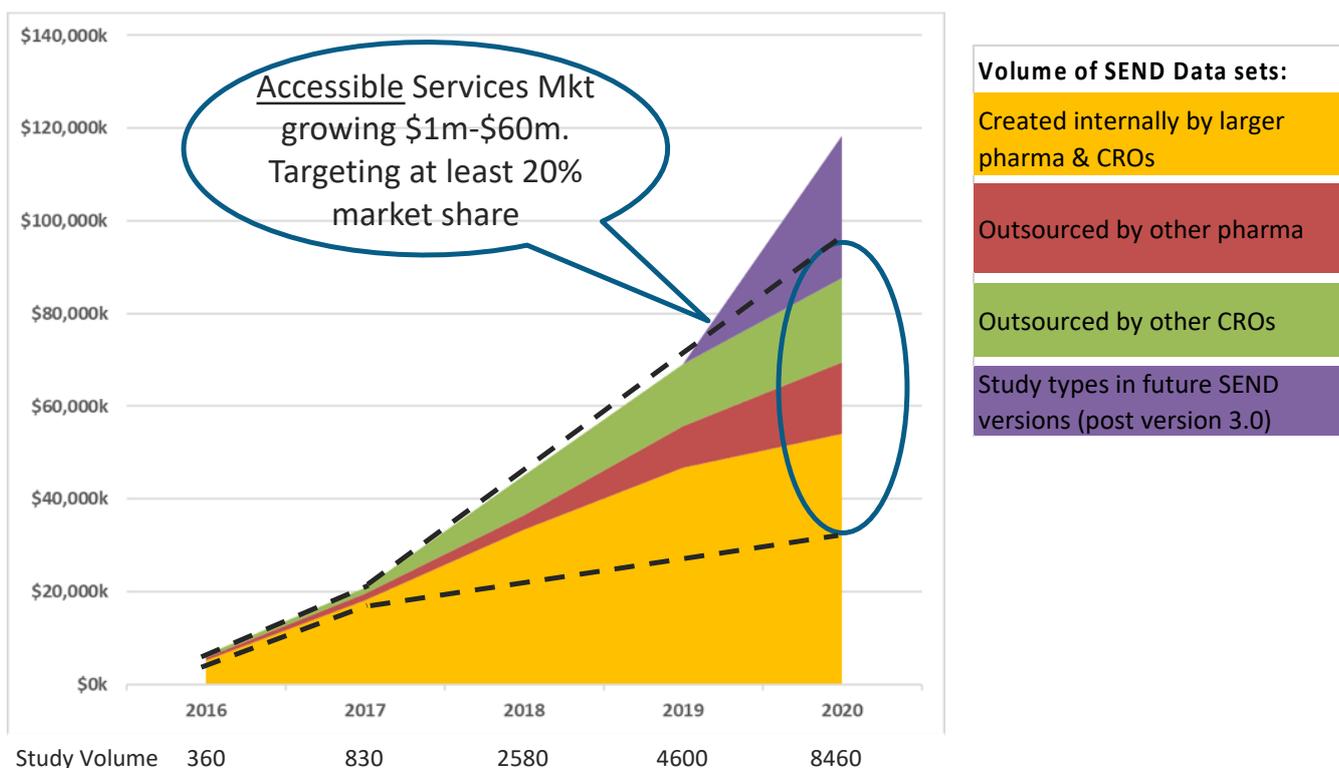
## A vast opportunity

Instem's management believe the size of the SEND services opportunity could be considerable, and significantly greater than the market for SEND- related (software) tools.

Below we present a summary of Instem's current estimate of the market size.

### Instem – estimates of SEND study volume and market spend

#### Market Spend



Source: Company data

Management forecast the number of SEND-compliant studies submitted to the FDA will grow to nearly 8,500 by 2020, versus 360 in 2016. This reflects the standard becoming mandatory for *all* NDA & IND trials starting after December 2017 (which was not the case historically) and also ongoing growth in the global drug R&D pipeline, which grew to over 15,200 compounds in Q1 2018 (source *Pharmaprojects*)

As the graphic demonstrates, the SEND services market is therefore expected to grow rapidly. In monetary terms, annual demand for SEND creation services anticipated to grow from c\$6m in 2016 to almost \$120m in 2020.

Management believe the accessible SEND services market will reach around \$60m annually by 2020, around 50% of the \$120m total. With an Instem target of 20% market share, there is clearly a material market opportunity for Instem. The 50% accessible market reflects management's view that larger CROs and pharma companies will continue to manage some or all of their studies in house.

## Financial Summary: Instem

Year end: December (£m unless shown)

<b>PROFIT &amp; LOSS</b>	<b>2016</b>	<b>2017</b>	<b>2018E</b>	<b>2019E</b>	<b>2020E</b>
Revenue	18.3	21.7	23.0	25.2	27.4
Adj EBITDA	1.3	3.0	3.6	4.5	5.0
Adj EBIT	0.7	2.3	2.6	3.4	3.8
Reported PBT	0.0	0.8	1.6	2.4	2.8
Fully adj PBT	0.5	2.2	2.6	3.4	3.8
NOPAT	0.5	1.7	1.9	2.6	2.8
Reported EPS	6.8	6.8	6.0	9.4	10.8
Fully adj EPS	2.0	10.1	11.5	15.3	17.0
Dividend per share	0.0	0.0	0.0	0.0	0.0
<b>CASH FLOW &amp; BALANCE SHEET</b>	<b>2016</b>	<b>2017</b>	<b>2018E</b>	<b>2019E</b>	<b>2020E</b>
Operating cash flow	1.3	1.9	3.8	4.5	5.2
Free Cash flow	(0.2)	0.1	2.0	2.4	2.9
FCF per share	(1.2)	0.6	11.9	14.1	17.5
Acquisitions	(3.3)	(0.7)	(0.2)	0.0	0.0
Disposals	0.0	0.0	0.0	0.0	0.0
Capex	(1.0)	(1.6)	(1.3)	(1.3)	(1.3)
Shares issued	4.8	0.0	0.0	0.0	0.0
Net cash flow	1.3	(0.8)	1.8	2.4	2.9
Cash & equivalents	4.2	3.1	4.9	7.2	10.2
Net (Debt)/Cash	4.2	3.1	4.9	7.2	10.2
<b>NAV AND RETURNS</b>	<b>2016</b>	<b>2017</b>	<b>2018E</b>	<b>2019E</b>	<b>2020E</b>
Net asset value	12.8	14.2	18.0	19.5	22.4
NAV/share	82.0	91.2	115.2	125.2	143.3
Net Tangible Asset Value	(4.8)	(3.2)	1.3	3.8	5.5
NTAV/share	(30.9)	(20.6)	8.2	24.2	35.4
Average equity	9.7	13.5	16.1	18.7	20.9
Post-tax ROE (%)	10.9%	8.1%	6.3%	8.4%	8.7%
<b>METRICS</b>	<b>2016</b>	<b>2017</b>	<b>2018E</b>	<b>2019E</b>	<b>2020E</b>
Revenue growth	12.2%	18.3%	6.4%	9.4%	8.6%
Adj EBITDA growth	(50.0%)	136.4%	20.5%	27.5%	10.9%
Adj EBIT growth	(63.7%)	221.2%	11.4%	33.2%	10.8%
Adj PBT growth	(73.5%)	381.4%	18.6%	33.2%	11.0%
Adj EPS growth	N/A	N/A	14.1%	33.2%	11.0%
Dividend growth	N/A	N/A	N/A	N/A	N/A
Adj EBIT margins	3.9%	10.6%	11.1%	13.5%	13.8%
<b>VALUATION</b>	<b>2016</b>	<b>2017</b>	<b>2018E</b>	<b>2019E</b>	<b>2020E</b>
EV/Sales	2.4	2.0	1.9	1.7	1.6
EV/EBITDA	34.8	14.7	12.2	9.6	8.6
EV/NOPAT	87.0	25.3	22.7	17.0	15.4
PER	145.5	29.2	25.6	19.2	17.3
Dividend yield	N/A	N/A	N/A	N/A	N/A
FCF yield	(0.4%)	0.2%	4.0%	4.8%	6.0%

Source: Company information and Progressive Equity Research estimates

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