

## ITL Group Limited

**Update October 2006**

### FY07 Guidance of 15% Revenue Growth to \$36m

#### Core Business:

The ITL Group (ASX:ITD) develops, manufactures and commercialises consumable medical products. ITL is focused on surgical procedure kits and also innovative medical devices for blood collection.

- **Procedure Kits:** ITL's Procedural Kit Division prepares and commercialises surgical procedure kits. These kits contain the required gowns, drapes and other consumable medical equipment required for a specific surgical procedure. It holds an inventory of over 6000 components, constantly being supplemented with new items to meet customers' changing requirements. Sales are mainly in Australia.
- **Innovative Products:** ITL's Innovative Products Division designs, manufactures and commercialises medical devices for the blood collection and medical consumable markets. Products include DonorCare (blood collection bags) and SampLok Sampling Kit (a consumable for the transfer of platelet samples for bacteria detection testing). Development is also being undertaken in next generation products for the whole blood collection, apheresis and dialysis sectors.

**Manufacturing Capability:** ITL has fully accredited manufacturing facilities in Ipoh (Malaysia) and Melbourne (Australia). The Ipoh facility manufactures medical consumables. The Melbourne facility produces surgical procedure kits.

#### Financials:

In the year ending 30 June 2006, revenues were \$31.2m, up 29% on the previous corresponding period (pcp). Profit was \$3.3m, up from a loss in FY05. Sales were driven by strong demand for pre-packaged surgical kits. The company declared a final (and maiden) dividend of 1 cent per share (cps).

#### Key Drivers:

- ITL has witnessed strong growth for the full year ending June 2006. Revenue growth of 25% pa for at least three years is expected as the market is immature.
- There is a trend towards the increased use of disposable drapes, gowns and other medical consumables. In Australia about 7% of the surgical procedures use consumable kits. In comparison, in the US the proportion is 90%. Presently, ITL has 30% of the Australian market.
- Sterilisation of drapes, gowns and other consumable equipment is a bottleneck in Australia hospitals. Purchasing pre-packaged kits has time and cost advantages for hospitals.

#### Recommendation:

We expect the company to experience strong sales growth. It generated its first profit in the half year ending December 2005. The full year profit of \$3.3m was higher than previous company guidance. The company is trading at a FY06 PE of 13.1 times and an expected FY07 and FY08 PE ratios of 10.4 and 6.6 times respectively. Given ITL's products are in the growth phase of the product life cycle and the company's stock is inexpensive relative to other industrial companies, we recommend ITL as a Buy

	Jun-05a	Jun-06a	Jun-07e	Jun-08e	Jun-09e
Revenues [adjusted] (\$)	24.0	31.1	37.3	44.8	53.7
EBITDA (\$)	0.7	4.8	6.5	9.4	13.7
EBIT (\$)	(0.5)	3.7	5.2	8.0	12.1
NPAT (\$)	(0.0)	3.3	4.1	6.4	9.8
EBIT Multiple	(79.6)	11.5	8.2	5.4	3.5
FCF Multiple	(78.7)	8.4	7.3	5.1	3.9
PER	(1,225.9)	13.1	10.4	6.6	4.4
EV/BV [adjusted]	2.9	3.2	2.9	2.0	1.2
EV/EBIT	(71.4)	10.7	8.1	4.9	2.8
Diluted EPS (¢)	(0.0)	3.0	3.8	6.0	9.1
FCFPS (¢)	(0.5)	4.7	5.5	7.8	10.2
Dividend per share (¢)	0.0	1.0	1.5	2.0	2.5
NTA per share (¢)	12.4	11.6	13.8	18.3	26.0

Price	\$0.40
Recommendation	Buy
Stock Code	ITD
12-Month Target Price	\$0.59

#### STOCK SUMMARY

Market Capitalisation	\$42.6m
12 Month Price Range	\$0.22 - \$0.45
Monthly Share Turnover	3.6m
Issued Shares	106.5m
Restricted Shares	Nil
Options	Nil

#### DIRECTORS

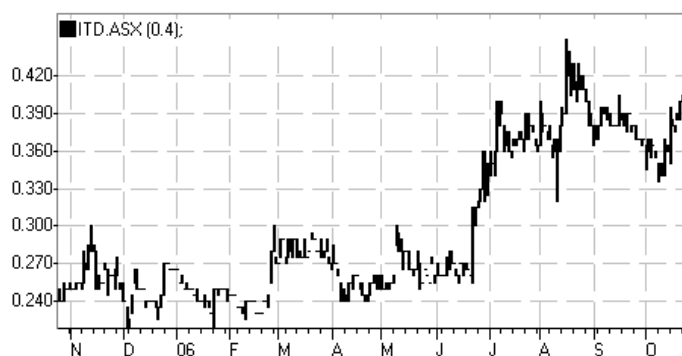
Julian Gosse	Chairman
Bill Mobbs	Chief Executive Officer
Roy Rose	Non Executive Director
Richard England	Non Executive Director

#### MAJOR SHAREHOLDERS @ 30 June 2006

Bilbo Holdings Pty Ltd	22.0%
Mandill Pty Ltd	11.5%
ANZ Nominees Ltd	4.6%
National Nominees Ltd	3.3%
Dr J Dillon & Mrs K Dillon	3.1%
Mr C Carr & Mrs B Carr	2.0%
Invia Custodian (WAM Capital)	1.8%
Talston Pty Ltd	1.5%

#### PREVIOUS INTERSUISSE RESEARCH

Medical Supplier - 25% Revenue	June 2006
Growth Forecast	



## ITL's Strategic Goals

At the 2006 AGM, the company reiterated it would aim for revenue growth of 15% or \$36m. We believe that this is a conservative estimate given the company achieved Q107 revenue of \$9.8m. We estimate the company would achieve revenue of \$37.3m generating an NPAT of \$4.1m

ITL's Directors have set a five-year corporate goal to create a company with revenues of \$100m and NPAT of \$10m.

This would be achieved by a combination of organic growth, acquisitions, new product pipeline and innovation; as well as continuing to extract efficiencies in the group's operations.

The company's first acquisition was in 2003, when the group acquired CWP Design, an industrial design company. This acquisition has resulted in an integrated design-development-manufacture-market service. Upon listing in 2003, ITL acquired Surgicare, a 25 year-old company that assembled and supplied medical procedure kits. The company experienced issues with the Surgicare acquisition, which were rectified 1½ years ago.

We are confident that the company will achieve this objective given the exhibited strategic intent in the acquisitions, contracts and growth in the last 12 months. Key highlights were;

- A new facility in Melbourne is being commissioned, providing the company three times its existing surgical kit preparation capability.
- A new facility in Malaysia is being constructed, which will increase production capacity of the medical consumable products.
- A new design facility was established at Sydney Technology Park
- A sales and marketing office was established in Washington DC.
- The Heal Marketing Sdn Bhd acquisition has been completed and has allowed the company access into the SE Asian hospital market.
- Various new contracts signed.
- There is also significant potential for procedure kits to be sold in South East Asia through Heal Marketing.

## Products

### Blood Banking Products

Focused on client demands, the Blood Banking Product unit manufactures a range of products for blood collection and processing companies, such as bioMérieux, Héma-Québec, the American Red Cross, and the like.

Remaining focused on a growth sub-sector of the medical consumable market, the company has learnt design and manufacturing skills, not easily replicated by a 'general' medical consumable manufacturer. This focus also allowed the company to build its brand and reputation within the blood collection market. This strategic focus has allowed the company to gain a dominant position as an OEM within the blood collection market.

ITL's products are used in over 95% of whole blood collections in USA, UK and Australia and have a strong presence in developed countries worldwide.



*Examples of three items manufactured by the company. From left to right, these three items above are the SampLok® Sampling Kit, the SampLok® Tube Holder and the SnapLok® Adaptor Cap. These consumables are routinely used in blood and plasma collection.*

An example of the strength of remaining focused on a sub-sector for the medical consumable market is demonstrated by the recent bioMérieux service contract.

ITL announced a five year supply agreement with bioMérieux for ITL's new SampLok® Blood Collection Adapter for use with the BacT/ALERT® product line.

The deal is positive for two reasons.

- 1) Firstly, focusing on blood-collection allowed ITL to be a reliable and known OEM to major specialist equipment suppliers.

The BacT/ALERT® system is installed in 85% of the blood banks in the United States. The US market is considered saturated. The BacT/ALERT® system also has a growing presence in the EU, with countries coming on line as respective governments adopt EU blood directive guidelines.

During the fiscal year ending June 2005, bioMérieux reported an 8% CAGR in bacteriology sales, including the sales of 50 million bottles for the BacT/ALERT® system. ITL is capable of producing 50 million blood collection clips and locks, but would require further CapEx on tooling.

It is noteworthy that bioMérieux is the sixth largest company in the diagnostic market. The company is chiefly focused on bacteria detection and is number two in that field.

In March 2004, US blood centres were directed to comply with an American Association of Blood Banks standard, which requires all platelets to be tested for bacteria. This directive has resulted in BacT/ALERT® attracting almost all the market share. The main competitor Scansys® has limited access to the US market.

- 2) Secondly, the deal puts the product into the hospitals as opposed to the blood banks. This is a much larger available market.

### Hospital and Monitoring Kits & Accessories

ITL's range of products for hospitals is aimed at improving the safety of healthcare workers. These are low margin / high volume products.

### Customised Procedure Packs

Under the Surgicare banner, the company assembles custom assembled surgical kits designed specifically to each surgeon's specifications.

### Standardised Procedure packs

Under the Clinical Choices banner, the company assembles standardised surgical kits for a number of surgical procedures. Examples include the; Arthroscopy pack, Basic Set-up pack, Caesarean Section Set-up pack, Laparoscopic Set-up pack and the Ophthalmic pack



*The layout and contents of a Standard Procedure Surgical Kit*

## ITL's Manufacturing Capabilities

### Surgical Kits

ITL's surgical kit business has outgrown the company's existing Melbourne facilities, forcing the company to expand. The new facility has Class 3500 Clean Rooms, allowing kits to be prepared under appropriate regulatory conditions.

### Medical Consumables

ITL has full in-house manufacturing capabilities based in Malaysia. The plant houses a fully certified class 8 clean-room, certified to ISO 9001, ISO 13485 and TUV accredited for CE marking. In other words, the facilities are certified for Australian, Asian and European sales.

The medical consumable products are manufactured at this site

## Design and Development Capabilities

### Medical Consumable Design

ITL design facility is based in Sydney, where engineers design and develop products for markets in the US, Europe, Australia and Asia. The company relies upon market pull-pressure in designing new product, allowing customer demand to drive product innovation.

The designers and engineers use CAD, rapid prototypes, finite element analysis, animations and ISO quality documentation and procedures to bring product ideas to fruition. Seamless integration with ITL's testing and manufacturing facilities ensure all designs are transformed into production products quickly.

## Directors

**Julian Gosse (Chairman)** has public company experience and is currently a director and secretary of Mariner Wealth Management Ltd, Wilson Leaders Ltd and Wilson Investment Fund and a director of Clime Capital Ltd.

Mr Gosse is also an executive director of Advanced Management Planning Ltd.

**William Mobbs (Chief Executive Officer)** is a co-founder of the ITL Group and has over 12 years experience in the international medical and healthcare industry.

**Richard England (Non-Executive Director)** is a professional company director and insolvency specialist. Until June 1994 he was a Partner of Ernst and Young and its National Director of Corporate Recovery and Insolvency. Mr England has over 30 years experience, specialising in capital and debt reconstructions for corporations and monitoring businesses in financial difficulties on behalf of lenders.

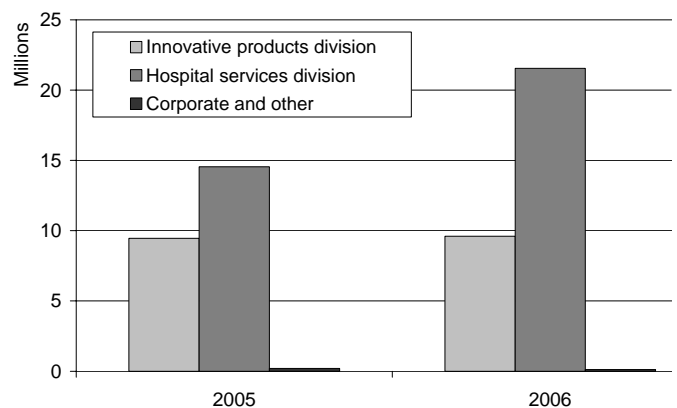
Mr England is Chairman of Gropep Ltd and Ruralco Holdings Ltd and is a director of Healthscope Ltd, St George Bank Ltd, Allianz Insurance Group and Choiseul Investments Ltd.

**Roy Rose (Non-Executive Director)** is a chemist and has 30 years experience specialising in general management, operations/production management, international sales and marketing, technology management and corporate governance holding various roles at Orica Ltd (formally ICI Australia).

He is the President of the Australian Industrial Research Group and is a member of the boards of the Cooperative Research Centre for Environmental Bio-technology and Genos Pty Ltd.

## Key Market Driver

ITL's fastest growing division is the custom and standard pack preparation. The Australian market has strong potential for growth.



*Segmented revenue for fiscal years 2005 and 2006.*

In Australia, about 7% of Hospitals use customised surgical kits. ITL currently holds around 30% to 35% of the customised kit market. In comparison, 90% of the US market uses disposable drape and gown kits. The trend in the Australian Market is moving towards a US style utilisation.

An operational issue for hospitals is the time and cost of sterilising reusable equipment. Sterilisation, though a standard procedure carries the cost of operating and maintaining an autoclave(s), labour and sterilisation takes about 120 minutes. Freeing sterilisation facilities for non-disposable equipment has time and cost advantages for hospitals.

The main competitor is Cardinal Healthcare Australia (100% subsidiary of Cardinal Healthcare). Anecdotal evidence suggests that ITL is growing the market and taking market share from Cardinal Healthcare. However, as the sales data of Cardinal Healthcare's Hospital kits is not public there is no quantitative data to support this observation.

Other competitors in the surgical kit sector include Multigate, DeFries, Uno Medical, Logikal Health Products and Smith & Nephew. Multigate, DeFries, Uno Medical and Logikal are private companies so the earnings achieved from the sale of surgical kits is unknown. Likewise, the sale of surgical kits by Smith & Nephew (Australia) is also unknown. Therefore, the estimate of ITL's market share is supple.

Packaged kits have cost and time advantages for hospitals, thus we see a transition of surgical kits from being unitised items to commoditised items within 5-6 years. After this period, revenue from the pre-packaged kit sector would come from repeat sales.

## Financials

### Historic Financials

The company reported a FY06 profit of \$3.3m, above the \$3.0m guidance the company gave to the market. Revenue was also above the \$30.0m guidance at \$31.3m. The company capitalised production development and tools and a grant of \$2.0m was treated as a liability on the balance sheet. The free cash flow for FY06 was calculated at \$5.1m.

### Important Information

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#### Disclosure

Intersuisse Limited, and Intersuisse Corporate Pty Ltd (an associate company of Intersuisse Limited), their directors and associates disclose that they do not have a relevant interest in the securities mentioned in this document.

Prepared by Darren John Grubb PhD;

Authorised by Peter Russell

25<sup>th</sup> October 2006

Sales were up 29.2% and the company is expected to experience revenue growth of about 25% per annum for the next 3 years.

The company has about \$3.7m in franking credits and declared a 1csp maiden dividend. We expect the dividend to grow around 0.5cps per annum.

To assist with growth, the company implemented a dividend reinvestment plan. Under the plan, the subscription price for DRP Shares to be issued under Plan is \$0.35. The discount rate set by the Directors for this dividend is 10%.

### Forecast Financials

The company gave guidance that the FY07 revenue would be about \$36m. We estimate the revenue (excluding the impact of any potential acquisitions) to be \$37.3m. We further estimate the FY07 and FY08 NPAT to be \$4.1m and \$6.4m respectively.

These estimates place the company on a FY07 and FY08 PE ratio of 10.4 and 6.6 times respectively.

The FCF multiple for the FY07 and FY08 period was calculated at 7.3 and 5.1 times respectively.

The dividend yield for the FY07 and FY08 period was estimated at 3.8% and 5.0% respectively.

## Recommendation and Valuation

Intersuisse assessed the fair value of the company by four valuation techniques. All these techniques indicate that the company is undervalued. Prior to the FY 2006 report we estimated the company to have a valuation fair value of 51.5cps.

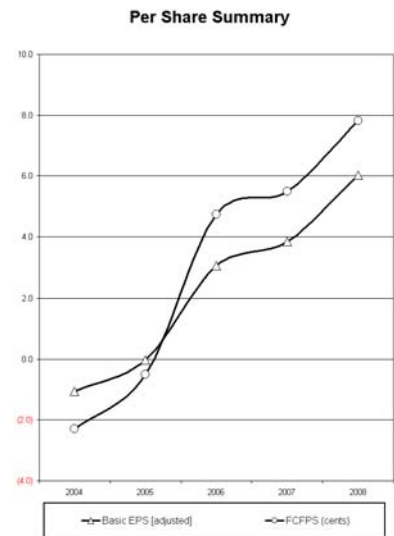
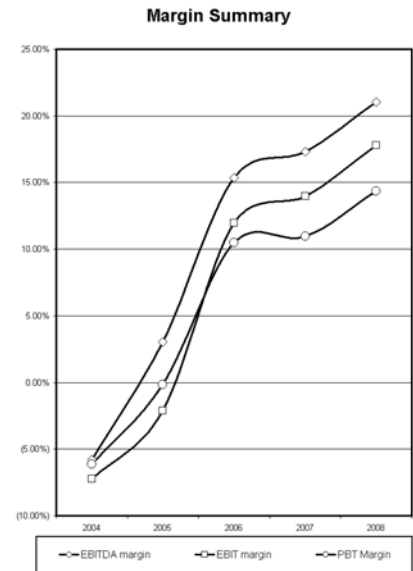
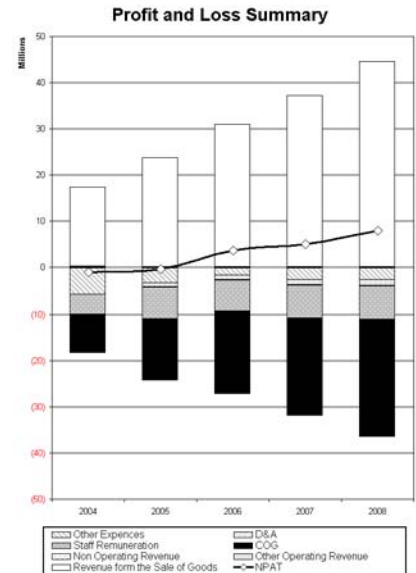
After the above FY06 guidance reported NPAT and the FY06 revenue guidance we have upgraded our 12 Month Price Target to 59cps.

Strong earnings growth, plant and capacity expansion, plus competent management who have learned from previous mistakes allow us to extend our BUY recommendation.

## Financial Summary

ITD	Jun-05	Jun-06	Jun-07	Jun-08	Jun-09
	Actual	Actual	Forecast	Forecast	Forecast
<b>Per share (cents)</b>					
Number of Shares (millions)	99.6	106.5	106.5	106.5	106.5
Basic EPS [adjusted]	(0.0)	3.1	3.8	6.0	9.2
Diluted EPS [adjusted]	(0.0)	3.0	3.8	6.0	9.1
Operating Cash per share	(0.5)	4.7	5.5	7.8	10.2
FCFPS (cents)	(0.5)	4.7	5.5	7.8	10.2
Dividend per share	0.0	1.0	1.5	2.0	2.5
NTA [adjusted] per share	12.4	11.6	13.8	18.3	26.0
<b>Profit &amp; Loss (A\$ m)</b>					
Revenues [adjusted]	24.0	31.1	37.3	44.8	53.7
Sales of Goods	23.8	31.0	37.2	44.6	53.5
Gross Profit Margin	43%	43%	43%	43%	43%
EBITDARD	0.7	4.8	6.5	9.4	13.7
Expensed R&D	0.0	0.0	0.0	0.0	0.0
EBITDA	0.7	4.8	6.5	9.4	13.7
EBIT	(0.5)	3.7	5.2	8.0	12.1
NPBT	(0.4)	3.7	5.1	8.0	12.2
Tax Credits / (Expense)	0.3	(0.4)	(1.0)	(1.6)	(2.4)
Minority interests	0.0	0.0	0.0	0.0	0.0
NPAT	(0.0)	3.3	4.1	6.4	9.8
NPAT [adjusted]	(0.0)	3.3	4.1	6.4	9.8
<b>Operating free cash flow (A\$ m)</b>					
NPAT	(0.0)	3.3	4.1	6.4	9.8
Depreciation and Amortisation	1.0	1.0	1.6	1.9	2.2
Working Capital	(2.0)	1.3	2.0	2.1	1.6
Others	0.6	(0.6)	(1.9)	(2.1)	(2.7)
Acquisitions and Disposals	0.0	0.0	0.0	0.0	0.0
<b>Operating Cash Flow</b>	(0.5)	5.1	5.8	8.3	10.9
Maintenance CapEx	0.0	0.0	0.0	0.0	0.0
<b>Free Cash Flow At End of Period</b>	(0.5)	5.1	5.8	8.3	10.9
<b>Investing Cash Flow</b>	(2.3)	(5.8)	(4.2)	(3.2)	(3.3)
<b>Financing Cash Flow</b>	(0.5)	(0.0)	(0.2)	1.1	1.9
Change in Cash	(3.3)	(0.8)	1.5	6.2	9.5
<b>Cash At End of Period</b>	4.2	3.4	4.9	11.1	20.6
<b>Balance sheet (A\$ m)</b>					
Net Cash and Short Investments	4.4	5.4	1.8	4.2	9.8
Current Debtors	4.5	7.4	8.7	10.4	12.3
Inventory	5.2	7.7	8.8	10.7	12.7
Other Current Assets	0.6	0.6	1.7	2.5	3.3
Current Creditors	4.6	6.7	6.5	7.7	8.4
Current Borrowings	0.5	2.2	1.5	1.1	1.0
Other Current Liabilities	(0.6)	0.6	0.5	0.6	0.6
<b>Net Current Assets</b>	10.2	11.5	12.5	18.3	28.2
<b>Net Current Assets [adjusted]</b>	9.2	11.6	12.4	18.3	28.2
PP&E	2.6	3.8	3.7	3.5	3.1
Non Current Assets	0.4	0.0	0.0	0.0	0.0
Capitalised Product Development	4.5	6.4	8.1	9.8	11.4
Intangibles	8.6	10.3	10.3	10.2	10.0
Non Current Liabilities	0.3	2.1	1.1	2.1	3.5
Non Current Borrowings	0.4	0.9	0.3	0.2	0.1
<b>Net Assets</b>	25.4	29.0	33.1	39.4	49.1
<b>Net Tangible Assets [adjusted]</b>	12.3	12.4	14.7	19.5	27.7
Minority interests	0.0	0.0	0.0	0.0	0.0
Convertible and Preference Shares	0.0	0.0	0.0	0.0	0.0
<b>Shareholders Equity</b>	25.4	29.0	33.1	39.4	49.1

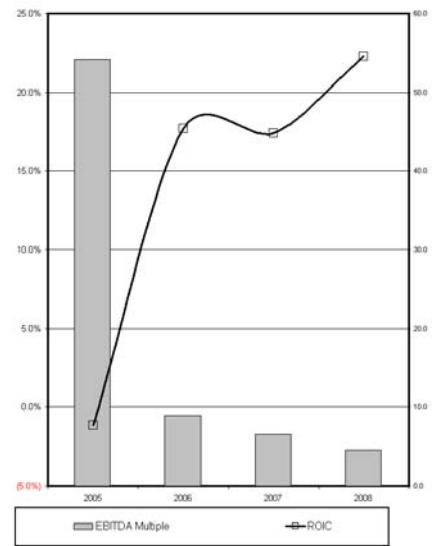
Balance Sheet adjustments exclude unrealised taxation assets  
Revenue adjustments exclude interest income



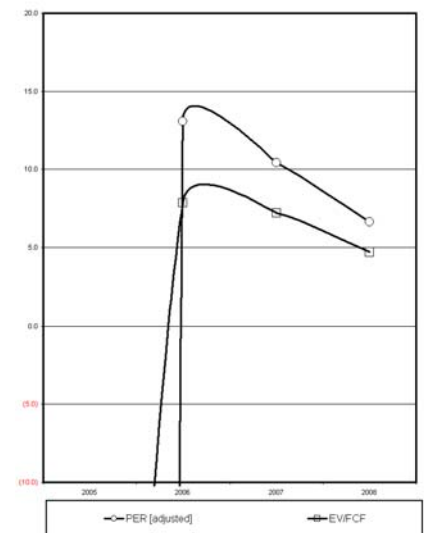
## Financial Analysis

ITD	Jun-05	Jun-06	Jun-07	Jun-08	Jun-09
	Actual	Forecast	Forecast	Forecast	Forecast
<b>Stock, Debt, Credit (Days)</b>					
Stock Turnover	79.1	90.8	86.6	87.3	86.9
Debtors' Turnover	69.0	87.1	85.7	84.9	84.2
Creditors' Turnover	123.1	135.6	112.5	111.3	101.1
Working Capital [basic]	25.0	42.3	59.8	60.9	70.0
<b>Gearing (Percentage)</b>					
Gearing [adjusted]	3%	7%	2%	1%	0%
Gearing II [adjusted]	3%	6%	2%	1%	0%
<b>Dividends</b>					
Dividend Cover	NA	3.1	2.6	3.0	3.7
Dividend Yield	0%	3%	4%	5%	6%
<b>Profitability Matrices</b>					
EBITDA margin	0.0	0.2	0.2	0.2	0.3
EBIT margin	(0.0)	0.1	0.1	0.2	0.2
PBT Margin	(0.0)	0.1	0.1	0.1	0.2
Current Ratio	3.3	2.2	2.5	2.9	3.8
Current Ratio [adjusted]	2.7	2.2	2.5	2.9	3.8
ROWC [adjusted, basic]	(0.1)	0.3	0.4	0.4	0.4
ROCE [adjusted, basic]	(0.0)	0.3	0.3	0.3	0.4
ROTA [adjusted, basic]	(0.0)	0.3	0.4	0.4	0.4
ROFA	(0.2)	1.0	1.4	2.3	3.8
ROIC	(0.0)	0.2	0.2	0.2	0.3
ROE [adjusted] (Basic)	(0.0)	0.3	0.3	0.3	0.4
ROE (DuPont)	(0.0)	0.2	0.2	0.2	0.0
ROA (DuPont)	(0.0)	0.1	0.2	0.2	0.0
Interest cover (Times)	(3.5)	20.3	20.9	51.9	104.0
<b>Productivity Matrices</b>					
Labour / Sales	0.3	0.2	0.2	0.2	0.1
Expensed R&D / Sales	0.0	0.0	0.0	0.0	0.0
Depreciation / Sales	0.0	0.0	0.0	0.0	0.0
Marketing / Sales	0.0	0.0	0.0	0.0	0.0
Profession Fees / Sales	0.0	0.0	0.0	0.0	0.0
<b>Growth Matrices</b>					
Revenue growth	0.4	0.3	0.2	0.2	0.2
EBIT growth	(0.6)	(8.4)	0.4	0.5	0.5
Basic EPS growth (cents) [adjusted]	1.0	(94.7)	0.3	0.6	0.5
Dividend growth	NA	NA	0.5	0.3	0.3
<b>Valuation Matrices</b>					
Market Cap (A\$ m) @ Current Price	39.8	42.6	42.6	42.6	42.6
EV	35.8	39.7	42.1	39.1	33.3
EV/BV [adjusted]	2.9	3.2	2.9	2.0	1.2
EV/Sales of Goods	1.5	1.3	1.1	0.9	0.6
EV/EBITDA	48.6	8.3	6.5	4.2	2.4
EV/EBIT	(71.4)	10.7	8.1	4.9	2.8
EV/FCF	(70.6)	7.8	7.2	4.7	3.1
FCF Multiple	(78.7)	8.4	7.3	5.1	3.9
EBITDA Multiple	54.2	8.9	6.6	4.5	3.1
EBIT Multiple	(79.6)	11.5	8.2	5.4	3.5
PER	(1,225.9)	13.1	10.4	6.6	4.4
PER [adjusted]	(1,225.9)	13.1	10.4	6.6	4.4
PEG [adjusted]	(12.6)	(0.0)	0.4	0.1	0.1
PEGY [adjusted]	NA	NA	NA	NA	NA
<b>Valuation</b>					
FCF Valuation @ 15.49% WACC					\$1.03
EVA Valuation @ 15.49% WACC					\$0.99
DCF (Five Year) Valuation @ 15.49% Disc. Rate					\$1.14
Future Maintainable Earning					\$0.59

### Profitability Summary



### Value Summary



### Asset Utility Summary

