

Luminex Corporation

NASDAQGS:LMNX

Analyst: Pierre Gouesclou

Sector: Healthcare

BUY

Price Target: \$23.19

Key Statistics as of 03/18/2016

Market Price: \$19.24
 Industry: Medical Instruments & Supplies
 Market Cap: \$830.10 Million
 52-Week Range: \$15.47-\$22.85
 Beta: 0.18

Thesis Points:

- Luminex is a small capitalization with high growth potential
- They have an impressive low debt amount for a Medical Instruments & Supplies company
- They have a very stable product line with a cutting edge technology
- Luminex is working with the Defense threat Reduction Agency of the United-States on a defense project

Company Description:

Luminex Corporation is a company that develops, manufactures and sells biological testing technologies to pharmaceuticals and other related companies throughout the world. The company has a small product selection and uses its patented xMAP open-architecture multi-analyte platform in order to develop their products according to the need of their customers. Luminex Corporation turned public in 2000 with a share price of \$17. A small capitalization company with a nich market line and an increasing Net change in cash can be expect to have a very high probability to encounter an important growth of their stock price in the upcoming year. The companies Net change in cash went from \$-1.4 million in 2010 to \$36.9 million in 2015 du to their impressive cost and debt management across the years. Furthermore the company is established in Austin, Texas which implies that Luminex is subject to G.A.P.P. accounting rules and obligations and therefore represents a low risk of falcification regarding their financial results.



Thesis

Luminex is a company with a well-managed capital structure that has acknowledged a quick growth of their assets and revenues during the past five years. In addition to expanding their product line through research and development the company also seeks partnerships with other organizations in order to have their researches sponsored and reduce their costs overall. In 2012 Luminex has entered a partnership with the Defense Threat Agency (D.T.A.) of the United-States to research and develop a defense project for the United-States government. This partnership may become an opportunity of a true and stable source of revenue for the company if it succeeds.

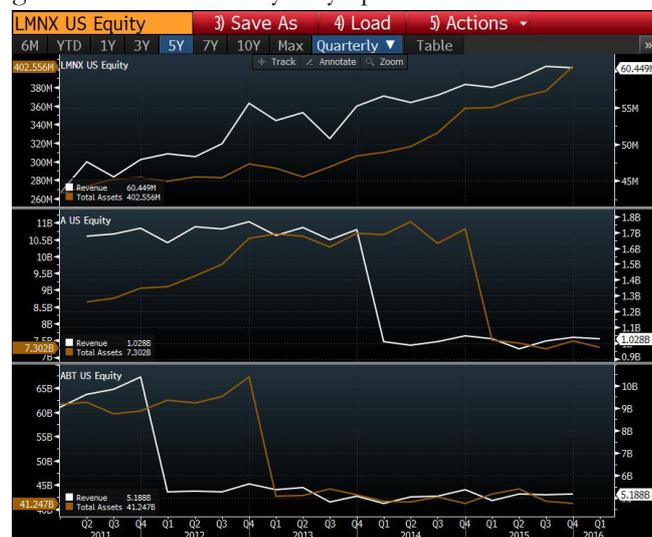
The company has an impressive capital structure considering the industry they operate in which often requires an important amount of debt to be able to operate efficiently. Luminex has a current debt to Equity ratio of 0.09 and does not carry any long-term debt. This debt management increases the capacities of the firm to pursue business without being burdened by too much debt.

Luminex Corporation also has an effective cost management that allows them to generate appropriate revenues. The operating income of the firm accounts for 16% of the revenues despite the fact that 21% of the total operation costs are used for the Research & Development of new or existing products. This cost management is even more effective given the fact that the company did not have any interest expenses in the past years.

Industry Outlook

The Medical Instruments & Supplies Industry has flourished in the past years considering the downfall of healthcare companies overall at the end of 2015. With the increase of creation of new medical treatments and drugs these companies were able to increase their sales of high technology products in order to support these innovations. In addition to the increase in technology it can be expect that the increase of demographics will enhance the growth of such industries and generated additional demand for this type of products. Furthermore private and governmental organizations have been investing important amounts of cash into this sector in the hope to enhance their efficiency. In that aspect this industry receives important external investments, which allows them to reduce their overall costs. The chart below shows the Revenue and Total Assets of Luminex compared to two of its competitors: Agilent Technologies and ABBOT. Luminex has been efficient in his operations compared to his larger and more stable competitors these last years. The firm

has been constantly increasing its total assets and revenues when its competitors acknowledged a downfall of Revenue and assets. In the last year Luminex has encountered a high growth for the Industry they operate in.



Product Line

Luminex Corporation product lines focuses mostly on three leading product lines: XMAP, XTAG and multiCode. In addition to these stable products the firm also launched their newly developed products: NxTAG and ARIES system. The ARIES system is a product that can generate IVD assays and give accurate results required in laboratories today. Globally, these products are systems that are incorporated into the machineries created by their licensed customers. Luminex pursues business directly with their customers in order to maintain a healthy relationship and be able to council more accurately their products. Outside of the license business Luminex also provides direct molecular diagnostic services to his customers. Because of their small product line the company is able to maintain a low cost of revenue.

Customer

Luminex Corporation has a small pool of customers who account for most of their sales. Labcorp is the most important of these customers and represents 18% of their revenue overall. A small customer base implies that the loss of one of their customers can uncover a risk for the company. In order to palliate that risk the firm has developed an impressive technical operation department responsible in assisting any entity equipped with Luminex products across the board. This technical assistance is available 24/7 as a remote service and can act physically if required by the customers. In addition, Luminex's International Operations accounts for around 16% of their overall revenues generated through their subsidiaries

located in Canada, Netherlands, China, Japan, Hong-Kong and Europe. The International operation is a valuable asset for a company dealing in such products and can be proven to become a competitive advantage against other smaller competitors. This segment also implies possible currency, tax and inflation risks for the company in foreign countries. Currently the company has acknowledged a strong and steady growth of their sales in the United-States.



	FY 2012	FY 2013	FY 2014	FY 2015
Revenue	202.6 100.0%	213.4 100.0%	227.0 100.0%	237.7 100.0%
United States	167.9 82.9%	178.3 83.5%	187.9 82.8%	200.4 84.3%
Europe	17.4 8.6%	16.7 7.8%	17.8 7.9%	17.0 7.2%
Asia	10.9 5.4%	12.3 5.8%	14.9 6.5%	12.8 5.4%
Other Foreign	1.7 0.8%	1.8 0.9%	2.7 1.2%	4.2 1.8%
Canada	3.8 1.9%	3.0 1.4%	3.7 1.6%	3.2 1.4%
Australia	1.0 0.5%	1.3 0.6%	-	-
Long Term Assets	166.9 100.0%	159.7 100.0%	-	-
Australia	2.6 1.5%	2.4 1.5%	-	-
Other Foreign	0.0 0.0%	0.0 0.0%	-	-
Canada	48.9 29.3%	46.5 29.1%	-	-
Asia	0.2 0.1%	0.2 0.1%	-	-
Europe	1.4 0.9%	1.0 0.6%	-	-
United States	113.7 68.1%	109.4 68.5%	-	-

Partnerships

Luminex like many companies are also expanding their Partnership projects in order to increase their output of new prototypes and product lines. Luminex has also expanded their network of Partners that are able to council and promote the products of the company. These Partners are to pay license fees to Luminex for each system they are able to provide to a potential customer.

In 2012 the company was granted \$12 million dollars by the Defense Threat Reduction Agency of the United-States. This Agency has only 47 contracts outstanding to companies and Luminex could acknowledge an increase in status if they succeed to fulfill this contract. Furthermore a possible success of this project could trigger additional governmental contracts and create new sources of investments and revenues for the company in the future.

Earlier this year Luminex enhanced their partnership with Bio-Techne regarding their product associations. Bio-Techne is a large Biotech firm with big access to international markets. This partnership consists in two specific segments. The first segment includes equipping Bio-Techne products with Xmap testing products developed by Luminex. The second segment is the distribution of Luminex systems by Bio-Techne on worldwide markets.

The most recent partnership of Luminex was signed with the Laboratory of Molecular Evolution & Bioinformatics, Biomedical Sciences Institute (University of São Paulo). The contract consists in enhancing the ability of Luminex products to foresee and detect the Zika virus that has an

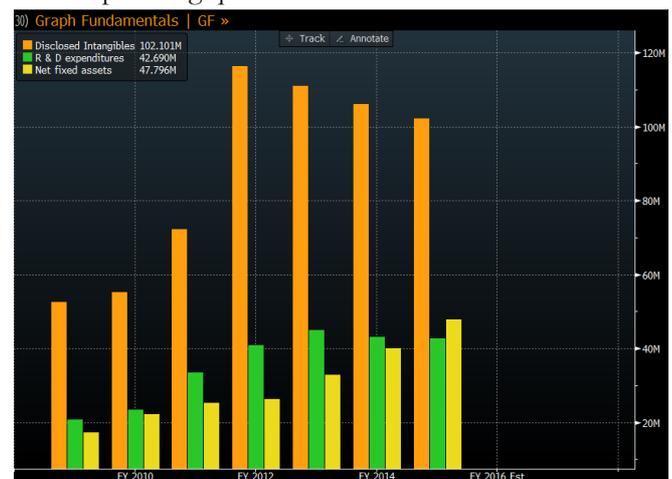
increasing presence and effect in South America. Such an agreement can prove to become a valuable asset for Luminex in the next months.

Research & Development

Between 2010 and 2015 the company has increased their R&D expenses by 59% going from \$26.8 million in 2010 to \$42.7 million in 2015. These expenses have been focused on the optimization on ARIES system; the key new product of the company. These optimizations include finding new ways to use the system but also software and consumables that could be used to enhance the application of the system itself. In addition to the investment in the ARIES system the company managed to develop in 2015 a chemistry to run multiplexed test combining other products created by the company such as xTAG and xMAP. The research and development of the company is effective given the innovations they created.

Intangibles and NPPE

In the last years the company has triggered an important purchase of Net property Plant and equipment (116% increase between 2010 and 2015) and financed this expansion by using cash issued from their operations. Luminex has also increased their purchase of other intangibles (+320%) such as patents and copyrights for their products. In the chart below is included the progression of the NPPE, intangibles and research and Development of the company. Luminex is experiencing a period of expansion and growth that is supported by their increase in Revenues overall. This aspect can prove to be a real driver towards an increase in stock price in the upcoming quarters.



Due to these increase in assets the company slightly increased their debt by 10% and their Equity by 57% thus modifying their capital structure into an Equity majority holding. The structure of their debt has also been modified in the last year turning away from long-term debt and taking over short-term

debt. As shown below the company paid of all of their debt in 2014. It is a true advantage for the small healthcare firm in the future.



Financial analysis

Luminex has had very positive results in the past years. In 5 years the company managed to increase their Net Income by more than 600% from \$5.2 million in 2010 to \$36.9 million in 2015 without taking important additional debt. On the other hand the revenues of the company increased by 68% between 2010 and 2015 implying a growth of their activities.

On the Cash flow aspect even by consequently increasing the Capital expenditures the company managed to change the Net change in Cash from \$-1.4 million to \$36.9 million in 5 years. As a result of their strategies Luminex was able to change their Retained earnings from \$-61.7 million to \$48.1 million in a period of 5 years. Overall Luminex has a stable structure and does not oppose any financial risk for the years to come. The Bloomberg chart below shows the revenue and Total Debt to Total Asset of Luminex.

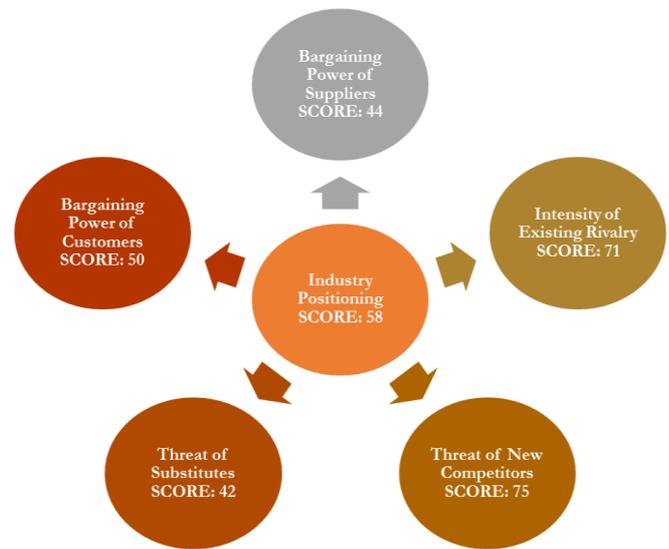


The company is currently following an increase of their revenues supported by a Total Debt to Total Asset of 0. Since the 2nd quarter of 2014 when the company deleted their debt the revenue has been increasing periodically in a seasonal way without weakening. In that aspect Luminex is

starting to shift towards a mostly Equity structure that might not be the most optimal structure but still provides more financial security. A small capitalization company with a mostly Equity structure implies a high return with a very low risk.



Porter's 5 Forces



Bargaining Power of Customers :

According to the Porter analysis Luminex has an average bargaining Power of Customer of 55. Overall the bargaining power of customer is an advantage for companies such as Luminex. This type of small company has the advantage of a very specific niche and complex product with a very narrow amount of competitors. In that aspect the bargaining power of customers is very low and the demand for the product is Inelastic. Luminex customers will be willing to pay more for their products

since they are uncommon and of importance for their own line of business.

Bargaining Power of Suppliers :

Luminex has an overall important power of Suppliers for his industry. The fact that there is a high number of substitutes and an important competition between the different suppliers decreases the dependency of the company towards one source of supply. Furthermore the volume ordered is not critical for their suppliers and implies that Luminex does not have a certain amount of supply to purchase in order to keep suppliers. The main disadvantages for Luminex is the fact that inputs have important impacts on costs for them.

Intensity of Existing Rivalry :

The industry in which operates Luminex is small and includes very little competitors for these type of products. This represents an advantage for Luminex who will encounter less opposition when it will come to selling their product. In this Industry the Exit barriers are averagely sized and the governmental control in order to limit competition exists. Biotechnologies are very advanced and lucrative, this is why governments have tendencies to watch over a nurture these companies.

Threat of New Competitors :

Threat of new competitors is very low for this type of company. In this industry the Entry barriers are very high and selective mostly because advanced technologies are required in order to thrive. Furthermore Patents are a major factor for competition limitation and brand loyalty from customers. In other words companies all have their niche products with very specific attributes that certain types of customer are looking for. In that aspect Strong brand names are not important since smaller companies protect by patents can provide higher quality products that bigger firms. The only threat of new competitors can be provoked by the attractiveness of the high earning curves of the industry Luminex operates in. Potential competitors can see a possible return on investment in taking the risk to enter this market. On the other hand the fact that there is a high switching cost of customer can counterbalance hopes of entering such an enclosed market. Overall Luminex has a low threat of New competitors given the industry they operate in.

Threat of Substitutes :

In this type of business it is primordial to acknowledge the existence and efficiency of possible substitutes.

Luminex has a very low number of substitutes to which their present customers can turn towards. In addition, the costs of switching to a substitutes will be important since the customer will have to modify most of their processes to fit this substitute. Even if the consumer decided to substitute Luminex's products he would be switching for a substitute with equal or lower attributes than the Luminex product. The products provided by Luminex are highly performant and out-perform or equal the results and efficiency of their competitor's products.

Conclusion

Overall Luminex has a stable structure and does not oppose any financial risk for the years to come. This aspect combined with a stable customer base and product line will ensure a positive future for the company. The company has been expanding both their physical and intangible presence by increasing their NPPE and intangible assets. Such purchases implies that the company is in a strong period of growth than can quickly become an opportunity to see the per share price increase at the maturity of these projects. The stock price is undervalued for the prospect of value creation behind their activities. In that aspect I recommend a Buy of LMNX with a 1 year target price of **\$23.19 (+20.53)**.

Luminex Corporation
(LMNX)

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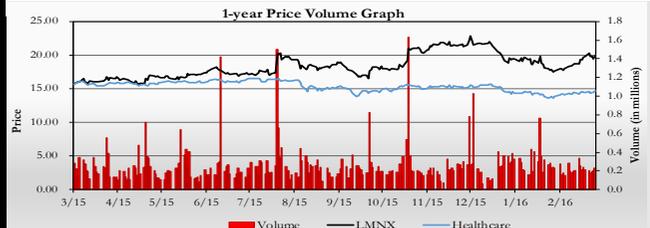
BULLISH

Analysis by Pierre Gouesclou
3/18/2016

Current Price: **\$19.24**
Divident Yield: **0.0%**

Intrinsic Value: **\$20.59**
Target Price: **\$23.19**

Target 1 year Return: 20.53%
Probability of Price Increase: 99.67%

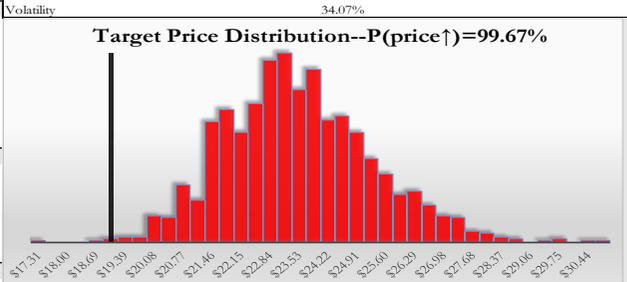


Description	
Luminex Corporation develops, manufactures, and sells proprietary biological testing technologies and products for the diagnostics, pharmaceutical, and life sciences industries worldwide.	
General Information	
Sector	Healthcare
Industry	Life Sciences Tools and Services
Last Guidance	November 3, 2015
Next earnings date	NM
Estimated Country Risk Premium	7.87%
Effective Tax rate	37%
Effective Operating Tax rate	67%

Market Data	
Market Capitalization	\$830.10
Daily volume (mil)	0.27
Shares outstanding (mil)	43.14
Diluted shares outstanding (mil)	42.64
% shares held by institutions	55%
% shares held by investments Managers	63%
% shares held by hedge funds	13%
% shares held by insiders	11.25%
Short interest	10.60%
Days to cover short interest	17.73
52 week high	\$22.85
52-week low	\$15.47
Levered Beta	0.18
Volatility	34.07%

Past Earning Surprises		
Quarter ending	Revenue	EBITDA
12/31/2014	0.22%	17.93%
3/31/2015	2.56%	6.12%
6/30/2015	3.23%	16.07%
9/30/2015	5.88%	24.60%
12/31/2015	0.38%	7.25%
Mean	2.46%	14.39%
Standard error	1.0%	3.5%

Peers	
Cepheid	
Affymetrix Inc.	
PerkinElmer Inc.	
Pacific Biosciences of California, Inc.	
Agilent Technologies, Inc.	
Sequenom Inc.	
NanoString Technologies, Inc.	
Bio-Techne Corp.	

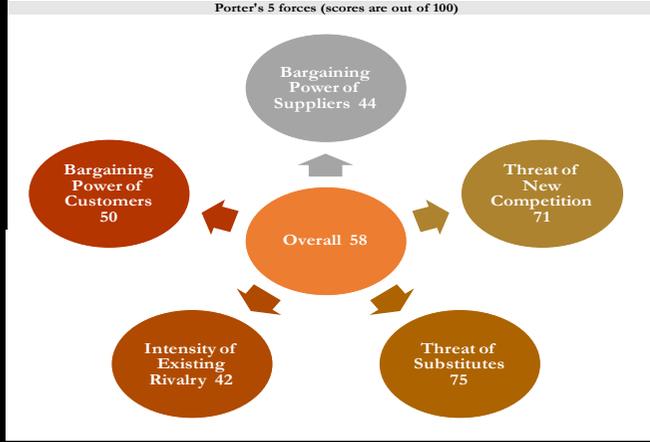
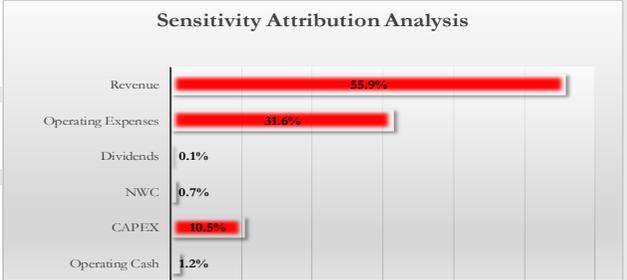


Management	Position	Total compensations growth	Total return to shareholders
Shamir, Nachum	Chief Executive Officer, Pre	N/M	0% per annum over 0y
Currie, Harriss	Chief Financial Officer, Sen	-4.89% per annum over 5y	4.6% per annum over 5y
Bradley, Russell	Chief Marketing & Sales Offi	7.68% per annum over 5y	4.6% per annum over 5y
Martin, Kendel	Vice President of Accounting	N/M	N/M
Copa, Thomas	Vice President of Technology	N/M	N/M
Rew, Richard	Senior Vice President, Gener	N/M	N/M

Profitability	LMNX (LTM)	LMNX (5 years historical average)	Industry (LTM)
ROIC	0.4%	9.25%	9.50%
NOPAT Margin	1%	9.96%	14.9%
Revenue/Invested Capital	0.75	0.93	0.64
ROE	0.4%	7.22%	10.64%
Adjusted net margin	0%	9.74%	13.3%
Revenue/Adjusted Book Value	0.72	0.74	0.80

Invested Funds	LMNX (LTM)	LMNX (5 years historical average)	Industry (LTM)
Total Cash/Total Capital	34.2%	27.9%	31%
Estimated Operating Cash/Total Capital	13.8%	15.0%	N/A
Non-cash working Capital/Total Capital	10.2%	13.7%	8%
Invested Capital/Total Capital	77.6%	85.0%	69%

Capital Structure	LMNX (LTM)	LMNX (5 years historical average)	Industry (LTM)
Total Debt/Common Equity (LTM)	0.02	0.02	0.15
Cost of Existing Debt	1.40%	4.65%	3.33%
Estimated Cost of new Borrowing	1.38%	1.38%	3.33%
CGFS Risk Rating	1.40%	AAA	B
Unlevered Beta (LTM)	0.00%	0.56	0.94
WACC	1.40%	7.33%	9.98%



Period	Revenue growth	NOPAT margin	ROIC/WACC
Base Year	4.7%	0.6%	0.10
12/31/2016	5.3%	17.0%	2.86
12/31/2017	8.1%	16.5%	2.59
12/31/2018	14.3%	14.0%	2.16
12/31/2019	12.6%	14.4%	2.08
12/31/2020	-0.7%	14.8%	1.78
12/31/2021	8.4%	15.6%	1.89
12/31/2022	5.6%	16.1%	1.82
12/31/2023	5.3%	16.7%	1.78
12/31/2024	5.0%	17.3%	1.75
12/31/2025	4.8%	17.9%	1.73
Continuing Period	3.0%	18.5%	1.68

Period	Invested Capital	Net Claims	Price per share
Base Year	\$159.93	-\$59.95	\$21.91
12/31/2016	\$207.06	-\$84.51	\$23.01
12/31/2017	\$271.77	-\$108.23	\$24.21
12/31/2018	\$293.85	-\$110.76	\$25.52
12/31/2019	\$316.57	-\$118.71	\$27.00
12/31/2020	\$318.87	-\$171.30	\$28.66
12/31/2021	\$342.91	-\$202.74	\$30.45
12/31/2022	\$369.80	-\$241.68	\$32.32
12/31/2023	\$416.40	-\$287.06	\$34.35
12/31/2024	\$465.01	-\$338.38	\$36.55
12/31/2025	\$470.52	-\$395.89	\$38.93
Continuing Period			