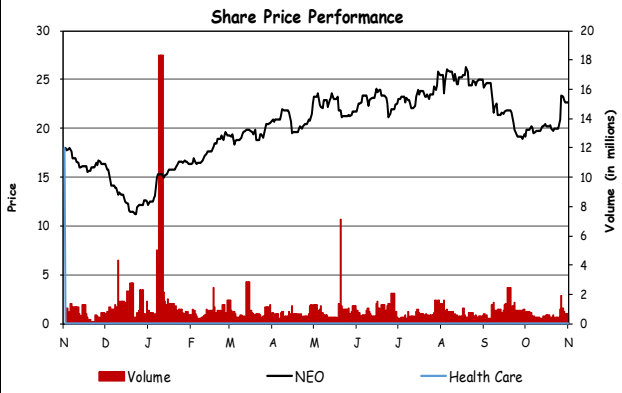
NeoGenomics, Inc.	Symbol: NEO
Analyst	Alexandros Giannakitsidis
Buy below	$19.91
Sell above	$30.79
Probability of Price Increase	50%
Last Price	$22.68
Intrinsic Value	$23.69
Target Dividends	$0.00
Target Price	$25.88



Description

NeoGenomics, Inc., together with its subsidiaries, operates a network of cancer-focused genetic testing laboratories in the United States; and laboratories in Switzerland and Singapore.

Sector	Health Care
Industry	Life Sciences Tools and Services
Last Guidance	December 11, 2018
Next earnings date	February 19, 2020

People

VanOort, Douglas, Chairman & CEO
Weiss, Lawrence, Chief Scientific Officer
Bonello, William, Chief Strategy & Corporate Development Officer
Cardoza, George, President of Pharma Services Division
Shovlin, Robert, President of Clinical Services Division
Virag, Sharon, Strategic Advisor

Top Competitors

Veracyte, Inc.	Myriad Genetics, Inc.
Natera, Inc.	Genomic Health, Inc.
Invitae Corporation	--
Teladoc Health, Inc.	--
MEDNAX, Inc.	NanoString Technologies, Inc.

Investment Thesis

UNIQUE LONG TERM GROWTH PROSPECTS AND CLINICAL TESTING GROWTH CAPACITY

I am initiating coverage of Neogenomics Inc. with a Limit BUY at 19.91and a $25.88 price target. I view NEO as a company that is a specialist in operating cancer-focused genetic testing laboratories in the United States as well as having laboratories internationally in Switzerland and Singapore. NEO is a leading provider of cancer diagnostic services to hospital pathology laboratories, hospital-affiliated pathologists, academic institutions, and office based oncologists. NEO has recently launched a new therascreen PIK3CA RGQ PCR test from QIAGEN N.V. NEO displays a high growth capacity in the biotech industry as they cater to clinical and pharmaceutical companies looking to screen and test new treatments and studies. As a rsult of NEO's expansion into international waters, it raises the ability of the company to grow their presence internationally and increase capacity for clinical tests. As a result I see NEO having long-term growth prospects because of their investments into next-gen screenings and testing facilities as well as their continued expansion and growth in the U.S. and abroad. I believe NEO offers great long-term growth prospects with increasing next-gen facilities and the expansion of testing capacity, as well as an increasing international presence.

For the long:

1. NEO currently has various assay panels that are in the process of being approved by the FDA:
Neo is currently developing a novel assay panel using NGS that is planned to be submitted for FDA approval before the end of 2019. It is speculated that the test will be focused on solid tumor and include a unique combination of DNA and RNA markers using patient tissue samples. It is also estimated that most panels being submitted for NEO's main consumer base (hospitals and pathologists) rather than direct selling to oncologists. Following approval Neo will run the tests for clients and this allows for another source of incremental revenue. At the moment any FDA approved panel has not been factored in the price of NEO's stock allowing for potential upside.

2. Expansion into foreign countries for their Pharma Services division:
At the moment Neo does not have international expansion plan for their clinical testing services division, but has started to expand for the pharma services division. With plans to expand further into China, specifically Shanghai, I believe that this will foster modest amount of revenue for the Pharma Services industry. This will only help them expand their global footprint.

3. Acquisition of Genoptix:
With the acquisition of Genoptix, NEO added 35 sales representatives, which doubles their number to 70 choosing to use this new team they expanded their focus to both institutional and oncologist customers within each region. This will only help them in having a competitive position in the emerging field of personalized medicine and a potential shift towards oncologists. With the expansion it is believed they will increase the attention to existing clients and provides an opportunity for incremental revenue, as well as an opportunity to sell solid tumor testing services withing the oncology community.

For the short:

1. Increased competition, including price competition.:
Mainly in their Clinical Services division (a large portion of revenue), there is alot of competition in the genetic and molecular testinig niche. There are many competitors in the United States and many major national medical testing laboratories, hospital laboratories, and in-house physician laboratories. Some of their competitors have greater financial resources and production capabilities. They may be better at developing services offerings or marketing it better or offer similar services at a cheaper price. This provides a potential risk for NEO.

2.Failure to develop, or acquire licenses for new or improved testing technologies :
If NEO fails to develop new testing technologies before their competitors they may be adversely affected. Competitors may introduce new tests that may decrease the demand for NEO's services. NEO's success depends on their ability to develop, acquire or license new and improved technologies on favorable terms and to obtain appropriate coverage and reimbursement for these technologies.

Key Catalysts for price change

- Getting various licenses approved by the FDA
- Expansion of Pharma Services into foreign markets.
- Increased sales force and capacity through acquisitions.

Valuation

My $25.88 price target is derived from 25% Discounted Levered Free Cash Flow estimates and a 75% EV/REV multiples.

Market Statistics

Market Capitalization (mil)	$2,355.00
Last Price per share	$22.68
52 week high	$26.89
52-week low	$11.05
Volatility	43.90%
Daily volume (mil)	0.66
Short interest	5.43%
Days to cover short interest	6.96
Beta	1.78

Ownership — Change in Ownership (over the past "12" months)

Shares outstanding (mil)	103.86	
Weighted Diluted shares outstanding (mil)	101.20	
Options and Warrants (Shares equivalent)	4.52	
% shares held by institutions	96%	27.79%
% shares held by investments Managers	78%	16.82%
% shares held by hedge funds	4.60%	2.36%
% shares held by VC/PE firms	2.568%	0.99%
% shares held by insiders	3.27%	-33.00%
Poison Pill and Type	NONE	

Financials

Profitability	**NEO (LTM)**	**NEO Historical**	**Peers' Median (LTM)**
Return on Capital	4.3%	3.08%	2.18%
Adjusted EBITDA Margin	12.0%	6.33%	4.09%
Return on Equity	2.9%	0.5%	5.7%
Adjusted Net margin	2.8%	1.1%	6.0%
Invested Funds	**NEO (LTM)**	**NEO Historical**	**Peers' Median (LTM)**
Cash/Capital	11.5%	3.5%	33.7%
NWC/Capital	9.8%	12.6%	2.8%
Operating Assets/Capital	46.4%	44.0%	44.4%
Goodwill/Capital	32.2%	40.3%	7.5%
Capital Structure	**NEO (LTM)**	**NEO Historical**	**Peers' Median (LTM)**
Total Debt/(Market Cap.+ Other Claims on Capital)	0.07	0.11	0.09
Minority Interest/(Market Cap.+ Other Claims on Capital)	0.0%	0.0%	0.0%
Preferred Equity/(Market Cap.+ Other Claims on Capital)	-3.7%	0.0%	0.0%
CGFS Credit Rating	C		CC
Credit Rating Model	b+ to bb-		b- to b
Probability of Default Model	bb to bb+		bb to bb+
Likely Current Cost of Debt	4.19%		5.19%
Likely Current Cost of Equity (Cost of Debt + MRP)	10.15%		11.15%
Likely Current WACC	9.67%		10.5%

Quarterly Earning Surprises (Actual/Median Estimates)

Revenue	**Last 5 quarters**
9/30/2018	$276.384 (4.1%)
12/31/2018	$305.9 (7.7%)
3/31/2019	$382.308 (5.5%)
6/30/2019	$406.852 (4.8%)
9/30/2019	$418.688 (5%)
History:	**Last 10 years**
Mean Surprise	1.80%
99th percentile "surprise" range	-10% to 14%
EBITDA	**Last 5 quarters**
9/30/2018	$40.176 (15.4%)
12/31/2018	$44.584 (4.7%)
3/31/2019	$46.576 (5.9%)
6/30/2019	$50.456 (-2.2%)
9/30/2019	$43.548 (-22.5%)
History:	**Last 10 years**
Mean Surprise	-6.74%
99th percentile "surprise" range	-51% to 38%

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Cost of Capital Estimates

	CGFS Credit Rating	Credit Rating Model	Probability of Default ModelModel
Implied Cost of Borrowing (NEO)	6.3%	5.6%	5.1%
Implied Cost of Borrowing (Peers)	5.6%	6.0%	5.3%

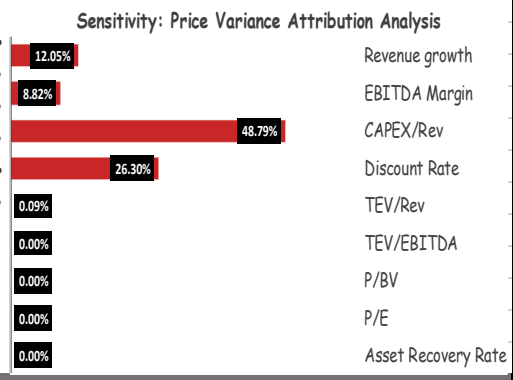
	Base Year	Explicit Period (15 years)	Continuing Period
Cost of New Debt Estimate	3.89%	4.00%	4.00%
Country Risk Premium Estimate	5.50%	5.50%	5.50%
Cost of Equity Estimate	9.39%	9.50%	9.50%
WACC Estimate	9.03%	9.14%	9.14%

Forecast Assumptions

Fiscal Year	Revenue Growth	EBITDA Margin	CAPEX/Revenue	DPR/CAPEX	Other	
Base Year (Actual)	5.44%	**11.9%**	5.2%	0.80	SBC/Revenue	2.52%
year 1	20.00%	**14.1%**	4.4%	0.78		Constant/same as LTM
year 2	18.00%	**16.0%**	4.4%	0.76	Lease term	10
year 3	15.00%	**17.5%**	4.0%	0.74	Rent Expense/Revenue	1.82%
year 4	15.00%	**17.4%**	4.0%	0.73		Tappers off to historical average
year 5	14.00%	**17.4%**	4.0%	0.71	R&D life	10
year 6	14.00%	**17.4%**	4.0%	0.69	R&D Expense/Revenue	1.08%
year 7	13.00%	**17.3%**	4.0%	0.67		Constant/same as LTM
year 8	13.00%	**17.3%**	4.0%	0.65	LIFO Reserve	Tappers off to zero
year 9	12.00%	**17.3%**	4.0%	0.63	Non-operating pension costs	Tappers off to zero
year 10	12.00%	**17.2%**	4.0%	0.61	Net financing pensions costs	Tappers off to zero
year 11	11.00%	**17.2%**	4.0%	0.59	Overfunded pension plans	Tappers off to zero
year 12	10.00%	**17.1%**	4.0%	0.58	Capitalized interests	Constant/same as LTM
year 13	8.00%	**17.1%**	4.0%	0.56	Dividends/Revenue	0.00%
year 14	6.17%	**17.1%**	4.0%	0.54	Tax Rate	28.11%
year 15	4.35%	**17.0%**	4.0%	0.52		
Continuing Period	2.52%	**17.0%**	4%	0.50		

Simulation Assumptions

Random Variables	Distribution Assumption	MAX	Likelly	MIN
Deviations in annual Revenue Growth--Expl. Per.	Triangular	1.00%	0%	-0.95%
Deviations in annual Revenue Growth --Cont. Per.	Normal	1.52%	0%	-1.52%
Deviations from EBITDA Margin base annual estimates	Triangular	3.96%	0%	-5.31%
Deviations from CAPEX/Revenue base annual estimates	Triangular	1.34%	0%	-0.21%
Deviations from Kd base annual estimates	Triangular	2.68%	0%	-0.34%
Deviations from CRP base annual estimates	Triangular	1.82%	0%	-1.92%
Deviations from TEV/Revenue base estimate	Triangular	3.88	0%	-5.03
Deviations from TEV/Revenue base estimate	Triangular	91.74	0%	-12.89
Change in P/BV (TTM)	Triangular	23.98	0%	-3.95
Change in P/E (FW)	Triangular	20.28	0%	-11.79
Recovery Rate	Triangular	10.00%	0%	-10%



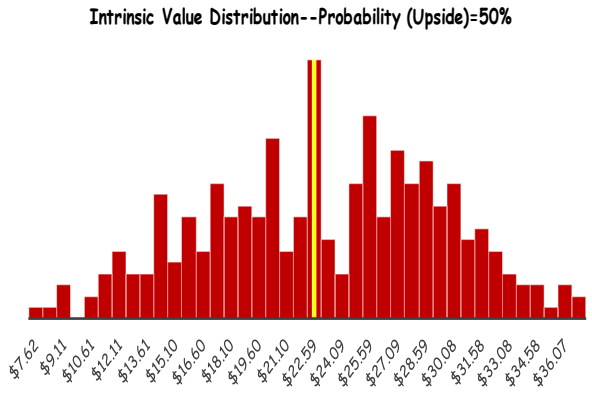
Valuation

DCF Valuation

	Base	Explicit Period (Average)	Continuing Period
Revenues	$378.44	$1,189.75	$2,209.44
Net Margin	3%	11%	11%
LFCF	-$76.05	$132.15	$252.60
Ke	9.39%	9.50%	9.50%
ROE	2.87%	19.21%	24.16%

Relative Valuation

	Median Justified Multiple	Basis	Implied Equity Value
EV/Rev (FW)	6.1x	$462.98	$2,852.02
EV/EBITDA (FW)	21.0x	$66.26	$1,399.27
P/BV (TTM)	5.3x	$525.71	$2,795.72
P/E (FW)	19.0x	$35.97	$684.74



Asset Based Valuation

Recovery Rate	60%
Capital	$2,045.62
Intangibles	$327.66
Claims	$190.37
Implied Equity Value	$840.41

Valuation Summary	Intrinsic Value	Target Price	Model Weight
DCF Valuation	$ 18.23	$ 19.71	25%
EV/Rev (FW)	$ 26.98	$ 29.41	75%
EV/EBITDA (FW)	$ 13.24	$ 14.43	0%
P/BV (TTM)	$ 26.45	$ 28.83	0%
P/E (FW)	$ 6.48	$ 7.06	0%
Asset Based Valuation	$ 7.95	$ 8.67	0%
Price per Share	$ 24.79	$ 26.99	100%