

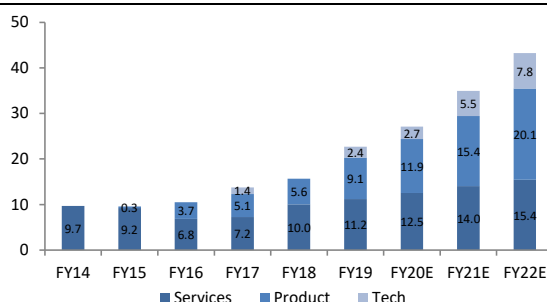
LaserBond Limited

Laser focus

We are initiating coverage on LaserBond with a fair value of \$1.50 per share.

- **Surface engineering specialists:** LaserBond specialise in the surface engineering of industrial components used in mining, steel manufacturing and other heavy industry. Surface engineering is the application of a composite coating to a component to extend its useful life. Laser cladding is the method primarily used by LaserBond with numerous advantages over alternatives. LaserBond is the largest laser cladding company in Australia.
- **Advanced technology:** LaserBond’s laser cladding extends the useful life of industrial components, such as the rollers used in steel mills, by as much as 20 times. LaserBond’s laser cladding approach is superior to many competitors: tests conducted by the company show LaserBond coatings to be longer lasting and commentary from customers and competitors supports these claims. Partners in China and the UK have licenced LaserBond’s technology - a testament to its efficacy.
- **Disrupting traditional markets:** Over the past five years LaserBond has evolved from being a repair shop to a product and technology business. One of the most promising products is Composite Carbide Steel Mill Rolls which it has started shipping to the US – an estimated \$15-20m annual revenue opportunity. The company has also developed an economic replacement to hard chrome plating – an estimated \$3bn potential market.
- **High organic growth:** LaserBond has grown sales and EBITDA organically at 29% and 98% CAGR over the past three years. We forecast 24% revenue CAGR to \$43min in FY22 vs. \$40m company guidance. We forecast most of the growth from product sales and technology licencing. Geographic expansion or M&A could provide further upside not in these forecasts.
- **Fair value \$1.50 per share:** Our DCF derived fair value is \$1.50 assuming a 25% terminal EBITDA margin.

Figure 1: LaserBond revenue by segment



Source: Veritas estimates, company data

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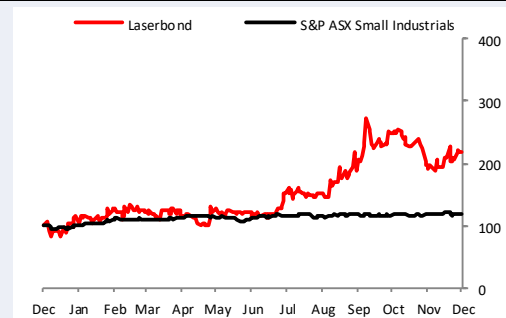
Tuesday 17 December 2019

Share Price	\$0.73
Price Target	\$1.50
Valuation Method	DCF

Market capitalisation	\$69m
Enterprise value	\$70m
GICS sector	Engineering Services
12 month price range	\$0.15 - 0.97
Average monthly t/o	1.8m
Shares in issue	94.7m
Top 20 holders	67.3m
Previous rating	Not rated

Year ended June 30		FY 19 A	FY 20 E	FY 21 E	FY 22 E
Revenue	\$m	22.7	27.1	34.9	43.2
Growth	%	44.9	19.5	29.0	23.7
EBITDA	\$m	4.9	6.2	8.1	10.2
Margin	%	21.6	22.8	23.1	23.7
NPAT	\$m	2.8	3.6	4.9	6.4
EPS	øps	3.0	3.8	5.1	6.6
CFPS	øps	4.3	4.2	4.3	5.7
DPS	øps	1.0	1.8	3.0	3.8
Franking	%	100	100	100	100
Dividend Yield	%	1.4	2.5	4.1	5.2
PER	x	24.6	19.4	14.3	11.1
Price/Cash Flow	x	16.8	17.5	17.1	12.7
EV/Revenue	x	3.1	2.6	2.0	1.6
EV/EBITDA	x	14.2	11.3	8.6	6.8
EV/EBIT	x	17.4	13.7	10.1	7.7
EV/Capital	x	6.5	5.9	4.9	4.2
Gearing (net debt: capital)	%	6	(9)	(17)	(26)
Fixed charge cover	x	5	6	7.7	10
Return on capital	%	30.5	32.8	38.6	42.3

Laserbond vs. Small Industrials Index



Source: Factset, Veritas

Laserbond is an engineering company with expertise in laser cladding and other technologies that extend the life of metal components used in mining and other industries.

<https://www.laserbond.com.au>

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EQUITY RESEARCH

LaserBond Limited

Financial Performance (A\$m)

Year ended June 30	FY17	FY18	FY19	FY20E	FY21E	FY22E
Revenue	13.8	15.6	22.7	27.1	34.9	43.2
Cost of goods	(6.6)	(8.7)	(11.9)	(14.0)	(18.0)	(22.5)
Gross profit	7.2	7.0	10.7	13.1	16.9	20.8
Operating costs	(4.7)	(4.7)	(5.8)	(6.9)	(8.8)	(10.5)
Normalised EBITDA	2.4	2.2	4.9	6.2	8.1	10.2
Depreciation and amortisation	(0.9)	(0.7)	(0.9)	(1.1)	(1.2)	(1.2)
Normalised EBIT	1.6	1.5	4.0	5.1	6.9	9.0
Associate income	0.0	0.0	0.0	0.0	0.0	0.0
Net interest	(0.1)	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)
Normalised Pre-tax Profit	1.5	1.4	3.8	4.9	6.7	8.8
Normalised tax	(0.4)	(0.4)	(1.0)	(1.4)	(1.9)	(2.4)
Profit attributable to minorities	0.0	0.0	0.0	0.0	0.0	0.0
Normalised profit to holders	1.1	1.0	2.8	3.6	4.9	6.4
One off items (post-tax)	0.0	0.0	0.0	0.0	0.0	0.0
Reported profit to holders	1.1	1.0	2.8	3.6	4.9	6.4

Cash Flow Statement (A\$m)

Year ended June 30	FY17	FY18	FY19	FY20E	FY21E	FY22E
Normalised EBITDA	2.4	2.2	4.9	6.2	8.1	10.2
Cash net interest	(0.1)	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)
Cash tax (paid)/received	(0.2)	(0.4)	(1.0)	(1.4)	(1.9)	(2.4)
Working capital/other	(0.2)	(1.3)	0.4	(0.7)	(1.9)	(2.0)
Operating Cash Flow	2.0	0.4	4.1	4.0	4.1	5.6
Capex	(0.1)	(0.3)	(3.4)	(1.5)	(1.5)	(1.8)
Free Cash Flow	1.9	0.1	0.6	2.5	2.6	3.8
Disposals/Acquisitions	0.0	0.0	0.0	0.0	0.0	0.0
Dividends paid	(0.2)	(0.3)	(0.5)	(0.7)	(1.3)	(1.8)
Equity raised/buybacks	0.0	0.0	0.0	0.0	0.0	0.0
Borrowings/(debt repayment)	0.0	0.0	0.0	0.0	0.0	0.0
Other inc. finance leases	(0.4)	(0.5)	0.7	(0.5)	(0.5)	(0.5)
Net increase/(decrease) cash	1.2	(0.6)	0.8	1.2	0.8	1.5
Cash at beginning	0.8	2.0	1.4	2.2	3.4	4.2
Cash at end (including bank deposits)	2.0	1.4	2.2	3.4	4.2	5.7

Balance Sheet (A\$m)

Year ended June 30	FY17	FY18	FY19	FY20E	FY21E	FY22E
Cash	2.0	1.4	2.2	3.4	4.2	5.7
Receivables	4.1	5.4	5.4	5.9	7.7	9.5
Inventories	1.8	2.5	2.5	3.0	3.9	4.9
Current Assets	7.9	9.2	10.1	12.4	15.8	20.1
Property, Plant & Equipment	2.5	3.1	5.9	6.3	6.7	7.3
Intangibles	0.0	0.0	0.0	0.0	0.0	0.0
Other non current assets	0.2	0.3	0.4	0.4	0.4	0.4
Non Current Assets	2.8	3.4	6.3	6.7	7.1	7.7
Total Assets	10.6	12.6	16.4	19.1	22.9	27.7
Payables	1.4	1.9	2.0	2.4	3.1	3.8
Current tax	0.1	0.2	0.4	0.4	0.4	0.4
Employee benefits	0.7	0.8	1.1	1.1	1.1	1.1
Other liabilities	0.0	0.0	0.0	0.0	0.0	0.0
Total debt	1.4	1.9	2.9	2.4	1.9	1.4
Total Liabilities	3.6	4.9	6.3	6.2	6.4	6.6
Shareholder Funds	7.0	7.8	10.1	12.9	16.5	21.1

Directors and Key Management Personnel

	Shares	Holding
Wayne Hooper	10.9m	11.5%
Greg Hooper	9.6m	10.1%
Philip Suriano	0.7m	0.7%
Matthew Twist	0.1m	0.1%

Major Shareholders (excluding nominees)

	Shares	Holding
Hooper Family	44.2m	46.7%
Peachey Family	4.9m	5.2%
Top 20 shareholders	67.3m	71.0%

Source: Company data, Veritas Research

Share Price: \$0.73 ps

Valuation: \$1.50 ps

Valuation Metrics

	Valuation
Price Target (ps)	\$1.498 105%
Share Price (ps)	\$0.730
FY20E EV/EBITDA (x)	11.3
Implied FY20 EV/EBITDA (x)	23.1 104%
Implied FY21 EV/EBITDA (x)	17.6 56%
Market Capitalisation (A\$m)	69.1
Enterprise Value (A\$m)	69.8

Valuation Multiples

Year ended June	FY17	FY18	FY19	FY20E	FY21E	FY22E
P/E (x)	59.8	70.2	24.6	19.4	14.3	11.1
Price/Cash Flow (x)	33.4	175.6	16.8	17.5	17.1	12.7
EV/Revenue (x)	5.1	4.5	3.1	2.6	2.0	1.6
EV/EBITDA (x)	28.5	31.3	14.2	11.3	8.6	6.8
EV/EBIT (x)	44.1	46.1	17.4	13.7	10.1	7.7
Equity FCF yield (%)	2.7	0.2	0.9	3.6	3.8	5.5
Dividend yield (%)	0.7	0.8	1.4	2.5	4.1	5.2
EV/capital (x)	10.9	8.4	6.5	5.9	4.9	4.2
Price to book value (x)	9.4	8.7	6.8	5.4	4.2	3.4

Per Share Data

Year ended June 30	FY17	FY18	FY19	FY20E	FY21E	FY22E
EPS diluted - adjusted (¢ps)	1.22	1.04	2.97	3.76	5.09	6.56
EPS diluted (¢ps)	1.22	1.04	2.97	3.76	5.09	6.56
Cash flow per share (¢ps)	2.19	0.42	4.35	4.18	4.28	5.74
Free cash flow per share (¢ps)	2.07	0.12	0.69	2.60	2.72	3.89
Cash (¢ps)	2.23	1.48	2.34	3.59	4.42	5.85
Net assets (¢ps)	7.80	8.35	10.72	13.59	17.22	21.62
DPS (¢ps)	0.50	0.60	1.00	1.80	3.00	3.80
Franking (%)	100	100	100	100	100	100
Shares on issue - avg. basic (m)	90	93	94	95	96	98
Shares on issue - avg. diluted (m)	90	93	94	95	96	98

Segmental revenue, EBITDA and margins

Year ended June 30	FY17	FY18	FY19	FY20E	FY21E	FY22E
Services	7.2	10.0	11.2	12.5	14.0	15.4
Product	5.1	5.6	9.1	11.9	15.4	20.1
Tech	1.4	0.0	2.4	2.7	5.5	7.8
Revenue (\$m)	13.8	15.6	22.7	27.1	34.9	43.2
Services	38.7	11.3	12.0	12.0	10.0	10.0
Product	10.5	62.8	30.0	30.0	30.0	30.0
Tech			14.3	103.7	41.2	
Revenue growth (%)	30.8	13.8	44.9	19.5	29.0	23.7
Services	1.6	2.0	2.6	3.1	3.7	4.2
Product	1.0	0.8	2.7	3.5	4.6	6.1
Tech	0.3	(0.0)	0.3	0.4	1.0	1.4
R&D	(0.4)	(0.5)	(0.7)	(0.9)	(1.1)	(1.4)
EBITDA (\$m)	2.4	2.2	4.9	6.2	8.1	10.2
Services	21.7	20.1	23.0	24.9	26.1	27.2
Product	19.5	13.4	29.1	29.3	29.5	30.3
Tech	17.7		14.5	16.6	18.1	17.6
R&D (as % of group sales)	(2.7)	(3.2)	(2.9)	(3.2)	(3.2)	(3.2)
EBITDA margin	17.8	14.3	21.6	22.8	23.1	23.7

Performance Ratios (%)

Year ended June 30	FY17A	FY18A	FY19A	FY20E	FY21E	FY22E
Gross margin	52.3	44.5	47.4	48.3	48.4	48.0
Operating cost margin	34.4	30.2	25.8	25.5	25.2	24.3
Gross profit growth		-3	54	22	29	23
Cost growth		0	23	18	28	19
Normalised EPS growth		-15	186	27	35	29
Tax rate	26.3	31.0	26.7	27.5	27.5	27.5
Return on capital	18.1	14.9	30.5	32.8	38.6	42.3

Balance Sheet Ratios

Balance Sheet (A\$m)	FY17A	FY18A	FY19A	FY20E	FY21E	FY22E
Gross debt (\$ m)	1.4	1.9	2.9	2.4	1.9	1.4
Net cash/(debt) (\$ m)	0.7	-0.5	-0.7	1.1	2.4	4.4
Gearing (net debt: capital)	-10	7	6	-9	-17	-26
Fixed charge cover (x)	14.3	2.7	5.1	6.0	7.7	9.6

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LaserBond specialise in the application of composite coatings to extend the useful life of industrial components used in mining, steel manufacturing and other heavy industry.

Specialists in surface engineering

LaserBond are specialists in surface engineering. Surface engineering is the application of a metal or metal composite coating in order to extend the life of a component. Industries such as mining and steel manufacturing require the surfaces of certain pieces of equipment to be extremely hard to avoid wear or have certain chemical properties to avoid degradation. The problem is that such materials are typically expensive. The solution is coating a substrate with a relatively thin layer of the material that has the desired properties i.e. coating a pump casing with tungsten carbide which is twice as stiff as steel. Company tests show that LaserBond products can last 3-20x longer than alternatives, saving money for the end user.

There are numerous methods for applying surface coatings. LaserBond specialise in laser cladding and thermal spraying which have significant advantages over the alternatives in situations where a high level of wear resistance is required.

LaserBond cladding

Laser cladding is increasingly used instead of Plasma Transferred Arc welding and outperforms conventional welding methods including Tungsten Inert Gas (TIG) for advanced repair applications according to laser cladding equipment supplier [Oerlikon Metco](#). Arc welding equipment was a \$7.8bn global market in 2017 according to [Persistence Market Research](#).

The primary advantages of laser cladding include: the creation of a metallurgical bond between the coating and the substrate which is less brittle than the mechanical bond obtained from thermal spraying; not distorting the substrate as Arc & PTA welding do; the ability to apply extremely thin coating layers which is particularly relevant for expensive coatings (Figure 2).

Figure 2: A comparison of the primary surface engineering techniques

Method	Distortion	Metallurgical bond	Application of layer <0.5mm	Negative impact on structural integrity of substrate
Laser cladding	No	Yes	Yes	Negligible
Arc & PTA welding	Yes	Yes	No	Some
Thermal spraying	No	No	No	Some

Source: Veritas research

Thermal spraying

Thermal spraying is an increasingly used alternative to hard chrome plating. Thermal spraying involves the application of a coating to a substrate by means of a system that propels a molten spray material at high speed. Variants of this used by LaserBond include High Velocity Oxy Fuel (HVOF), electric arc spraying and plasma arc spraying.

History

LaserBond was founded in 1992 by Greg Hooper as HVOF Australia Pty Ltd. It specialised in thermal spraying before the acquisition of its first laser in 1999. Development of the laser cladding process was completed in 2001. It listed in 1997 with a \$13m capitalisation at 20c per share. It acquired Peachey's in Gladstone, Queensland in 2008. The company raised \$2m at 23c per share in 2012 to fund a facility in South Australia which opened in June 2013. In October 2013 the Queensland facility was closed due to cost pressures and weakness in the Alumina market. LaserBond first licenced its laser cladding technology overseas in 2015.

LaserBond has been operating for 27 years and is 47% owned by the founding family.

Competitive advantages

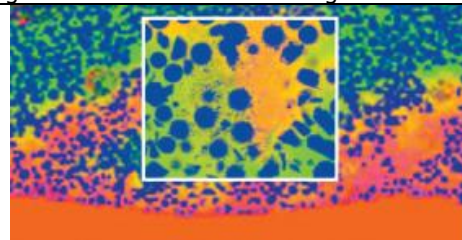
A unique process produces superior quality cladding

LaserBond produces and repairs components to a high-quality standard which we attribute to the intellectual property it has developed over the past 27 years.

LaserBond were among the early adopters of laser cladding in the late 1990's, building the necessary equipment - a combination of robots, lasers and control systems - from scratch. The DIY approach at the infancy of the technology enabled the company to develop a patented process which delivers superior functional performance to competitors.

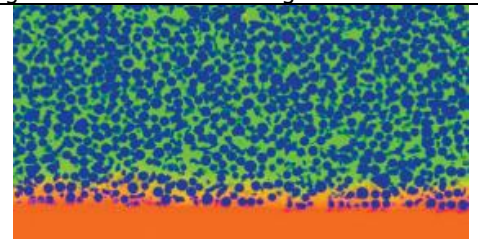
Our conversations with customers and suppliers suggest LaserBond's laser cladding often offers superior durability to competitors. We attribute this to their intellectual property in terms of laser, substrate and cladding material preparation and can be observed by comparing the synchrotron image of regular laser cladding (Figure 3) to LaserBond cladding (Figure 4). The red and orange streaks blended with the blue particles (Figure 3) are known as dilution and are structurally weaker. We believe the high quality of cladding produced by LaserBond's unique process explains why it has licenced the technology to partners in China and the UK.

Figure 3: Standard laser cladding



Source: Company

Figure 4: LaserBond cladding



Source: Company

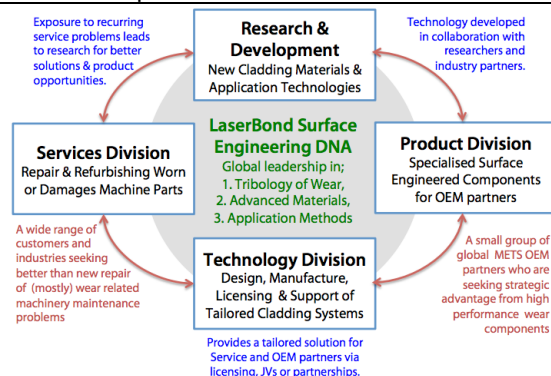
Research and development capabilities

LaserBond's foremost competitive advantage is the amount it has invested in R&D. This enabled it to become more than simply a repair business.

LaserBond began as a service business – repairing and refurbishing damaged machine parts for the end user and OEM's. Continual exposure to client problems motivated research into better solutions and led to the establishment of the Products division in FY15, which provides specialised components for OEM partners.

LaserBond began to further commercialise its unique technology by licencing its IP. It signed its second partner in FY19. Management expect to sign one licencing deal in FY20 and two deals per year from FY21. The synergies between the four segments make LaserBond unique (Figure 5). We expect that LaserBond's uniquely scientific approach toward R&D and technology will enable it to continually provide superior services and grow revenues through the invention of new applications for lasers.

Figure 5: The inter-relationship between LaserBond's business units

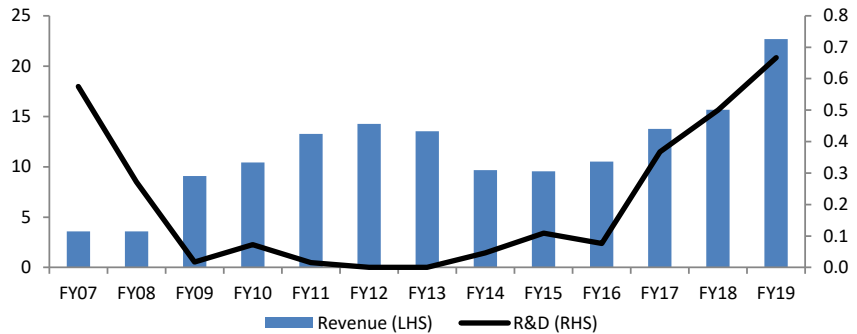


Source: Company

Most of LaserBond’s competitors don’t conduct research and development. These competitors rely on laser manufacturers such as Laserline, Trumpf and Oerlikon Metco for their laser technology. The problem with this is that the laser manufacturers are not as close to the end user applications so can be slower to adapt the configuration of the equipment to deliver the optimal results.

There is a clear historical relationship between R&D and future revenue at LaserBond (Figure 6). The increase in R&D spend since FY16 bodes well for revenue growth over coming years.

Figure 6: LaserBond group revenue (LHS, \$m) versus R&D spend (RHS, \$m)



Source: Company data

Powerful lasers

The speed at which a component can be laser clad and the quality of the coating is dependent on the power of the lasers used. During 2018 LaserBond commissioned a 16kW laser in its South Australia facility – the most powerful of its type in the Southern Hemisphere according to [Engineers Australia](#). This laser uses 60% less energy and produces less waste than the three 6kW lasers the company operated prior. LaserBond’s lasers are considerably more powerful than the two 4kW lasers employed by its major Australian competitor Hardchrome Engineering.

A significant uptick in R&D since FY16 should fuel growth over the next few years.

Opportunities

The roll-out of steel mill products to the US

"Within a time period of less than six months LaserBond has become an integral supply chain partner with our procurement and maintenance teams. In every case the carbide composite components supplied to us by LaserBond have far exceeded our expectations in terms of the service life we are now achieving."

Liberty House Group as per LaserBond ASX release on 5 December 2018

One of LaserBond's more promising products is Composite Carbide Steel Mill Rolls (Figure 7). The rolls are used in the steel manufacturing process to reduce the thickness and improve the uniformity of the manufactured steel. Standard mill rolls can wear out in as little as a few weeks. They are required to be extremely hard due to the constant exposure to friction. LaserBond use their unique laser cladding process to produce rolls with a 20 times longer life than conventional rolls according to the company's [own tests](#): saving the steel manufacturers money and reducing downtime.

Figure 7: LaserBond's branded Composite Carbide Steel Mill Rolls



Source: Company

Mill rolls generated c\$0.3m revenue for LaserBond in FY19, the vast majority of which was from Australian customers. We estimate the annual revenue opportunity in Australia is c\$1m.

Steel mill rolls in the USA could be a \$15-20m long term opportunity for LaserBond.

In FY19 the company commenced discussions with US steel mills, and we understand the company is supplying eight US steel mills at present. The 120 steel mills in the US produce c16x more steel than Australia in total according to US Government and Australian Steel Institute data. Accordingly, we estimate that the US could be a \$15-20m annual revenue opportunity for LaserBond. To put the opportunity into context, steel mill rolls could represent 66-88% of FY19 revenues.

A replacement for hard chrome plating

Since early in the 20th century hard chrome plating has been used to improve the wear and abrasion resistance of various industrial components predominantly used in aviation, oil, gas and mining applications. Most hard chroming processes involve the use of hexavalent chrome. In 1980 hexavalent chrome was listed as a human carcinogen by US authorities after research showed a higher cancer risk than asbestos and benzene at permissible exposure limits.

In recent years the negative environmental and health consequences of using hexavalent chrome have come into focus – as popularised by the film Erin Brockovich where the

protagonist successfully wages a campaign to highlight its harmful effects. In 2010 the US Department of Defence instructed all government departments to minimise the usage of hexavalent chromium. In 2017 the use of hexavalent chrome was banned in [Europe](#). The use of hexavalent chrome is still permitted in Australia. We would not be surprised if its usage should be restricted over time due to a tendency to follow European and US regulation.

Thermal spraying and laser cladding – LaserBond’s specialities - are both considered cost effective and suitable alternatives to hard chrome plating in many applications. LaserBond management claim to have achieved consumable success over FY19 in processes with wear and corrosion properties exceeding hard chrome coating for a comparable cost. This could increase the LaserBond’s addressable market. The size of the hard chrome plating market globally was USD \$3.2bn in 2003 according to [Products Finishing](#), the most recent year for which we could find reliable information.

Geographic expansion

One of the primary obstacles to LaserBond’s growth is the cost of transporting large/heavy components to and from LaserBond facilities in either Adelaide or Sydney. The natural solution to this is LaserBond building facilities that are closer to customers. Given the end market opportunities we have outlined it could make sense over to have facilities in Western Australia or the USA. Our forecasts do not include any benefit from geographical expansion.

Being closer to clients in order to win more work has proved successful for LaserBond in South Australia. We believe management have learnt from the acquisition of Peachey’s in Gladstone Queensland.

LaserBond acquired Peachey’s Engineering in Gladstone, Queensland for just over \$3m in November 2008. Peachey’s was a machining shop that did not do laser cladding with a focus on fabrication. The transaction was poorly timed. The mining boom meant rising rents and competition for skilled labour. After the GFC demand for higher margin fabrication dried up. LaserBond’s major customers in Gladstone were engaged in Alumina refining. Aluminium prices fell from a peak of \$3,200 per MT in 2008 to a low of \$1,700 in 2013. In 2012 LaserBond installed laser cladding facilities, but it was too little too late. In October 2013 LaserBond made the decision to shut the business.

Competitors

LaserBond has relatively limited competition due to the nascent nature of the laser cladding technology. LaserBond's services include laser cladding, thermal spraying, welding and machining. Welding and machining are relatively commoditised, as is thermal spraying to a lesser extent due to greater technical difficulty. LaserBond's laser cladding capability is its key point of difference. We gained an understanding of the competitive landscape by speaking with LaserBond's major competitors, suppliers and customers.

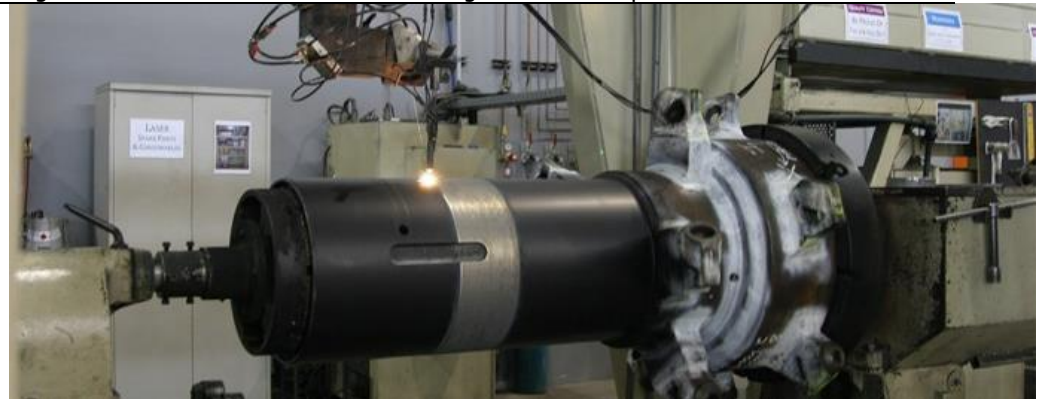
LaserBond's facilities are in Sydney and Adelaide. Its major competitors are in Melbourne and Perth.

LaserBond operates two facilities in Australia, in Smeaton Grange (South Western Sydney) and Adelaide. Our discussions with industry participants suggest that LaserBond is the largest player in the Australian laser cladding market followed by Hardchrome Engineering with a workshop in Melbourne and Brenco with facilities in Melbourne and Perth.

One of LaserBond's primary competitors is the decision of the end user to replace a component.

Roughly half of LaserBond's revenues are derived from the repair of worn-out components. One of LaserBond's primary competitors is the decision of the end user to replace a component rather than having it repaired. The decision to purchase a new component is commonly due to a lack of knowledge about how laser cladding can be used. Our discussions with competitors suggest that the end user awareness of laser cladding and its applications is improving. This may be a response to LaserBond's marketing activities, which are much more prominent in trade publications than the competition.

Figure 8: One of LaserBond's laser cladding machines in operation



Source: Company data, Veritas estimates

Hardchrome Engineering is LaserBond's closest competitor in Australia

We estimate [Hardchrome Engineering](#) is the second biggest laser cladding company in Australia after LaserBond based on our discussions with suppliers and customers. In addition to laser cladding the company also offers nickel and chrome plating and hydraulic repairs. Hardchrome Engineering was established in 1968. That LaserBond currently has a bigger laser cladding business is testament to its focus on marketing and R&D.

Brenco is the next most established laser cladding player in Australia

After Hardchrome the next biggest player in laser cladding is Brenco, which was acquired by Mogas Industries in July 2019 for an undisclosed sum. Mogas is a valve manufacturer and heavy industrial equipment servicing company based in Houston, Texas. The rationale for the acquisition was "to bring the next generation of patented laser cladding technology in-house" according to [Business Wire](#). Brenco, like LaserBond, operate a metallurgical laboratory. Our investigations suggest that Brenco has less capacity for heavy engineering (i.e. mining applications) than LaserBond.

French company Technogenia is slightly larger than LaserBond

International competitors to LaserBond vary by market and include French company Technogenia with operations in the US, UK, France and the Middle East and licenced operations in China, Singapore and Russia. According to its website Technogenia has consolidated sales of €28m (A\$46m) making it roughly twice the size of LaserBond with \$23m revenues in FY19.

International providers of laser cladding systems include Trumpf (private) and Oerlikon Metco (market cap CHF3.7bn equivalent to A\$5.5bn). These companies are not direct competitors as they mostly provide the laser cladding equipment rather than the services.

Customers

LaserBond has a wide range of heavy industrial customers.

LaserBond’s customer list reads like a who’s who of heavy industry (Figure 9). Most sales are derived from mining, mineral processing, steel milling and aluminium manufacturing.

Figure 9: LaserBond customers

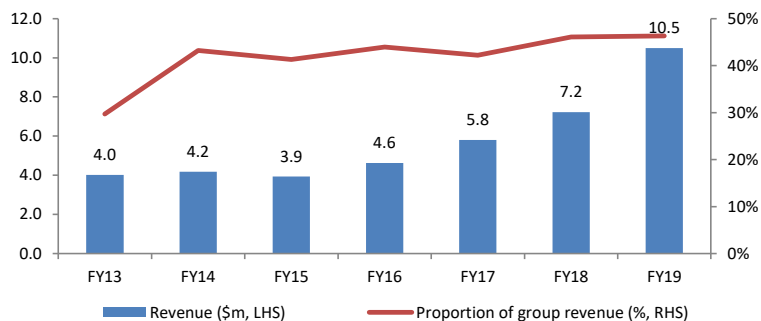


Source: Company

A high customer concentration

The customer base is relatively concentrated with two customers comprising \$10.5m or 46% of group revenue in FY19. The customer concentration has remained relatively steady since FY14 as the key customers have grown revenues in line with the group (Figure 10).

Figure 10: Significant customers as proportion of group revenue



Source: Company data. Note that significant customer revenues are from one customer prior to FY16 and two after that.

Weir Minerals is likely to be the largest customer

Weir Minerals is probably LaserBond’s largest customer

Management has not disclosed the identity of LaserBond’s two largest customers. We suspect that one of them is Weir Minerals – global leaders in the production and service of

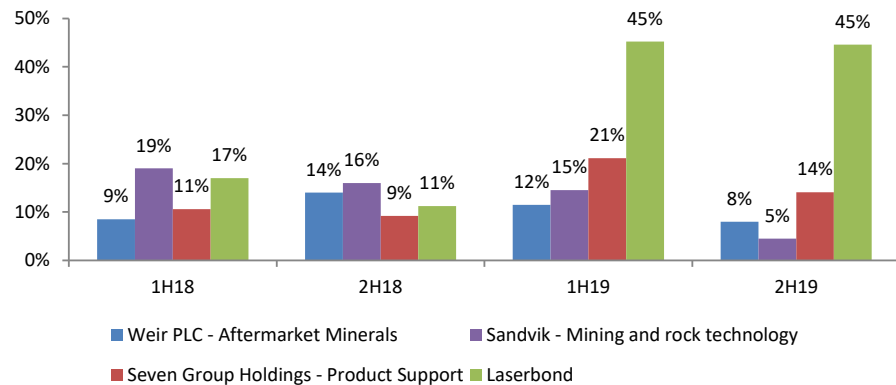
pumps used in mining applications. LaserBond signed a three-year contract with Weir Minerals Australia worth \$9.6m over three years according to the FY09 annual report. Weir was LBL's largest customer as of September 2012.

LaserBond's customers have achieved decent organic revenue growth over the past two years.

End markets are growing nicely

LaserBond's growth is a function of its customers growing and finding wider applications for laser cladding. All of LaserBond's customers that we identified with relevant segmental information have witnessed strong growth over the past two years – an indication of the underlying demand for LaserBond's products and services (Figure 10).

Figure 11: Organic revenue growth for LaserBond and certain customers (% YoY)



Source: Company data. Note: Seven Group Holding's Product Support revenues comprise mainly of Westrac parts and maintenance.

With companies like Weir, BHP, Rio Tinto, Westrac and Caterpillar representing a meaningful proportion of revenues LaserBond is exposed to the mining cycle. The decline in revenues from \$14.3m in FY12 to \$9.5m in FY15 is partly a function of this and due to the closure of the loss-making Queensland operation which had c\$4-5m of annual revenues. We expect the diversification of Laserbond since 2015 into products & technology and away from mining should make the business less cyclical in future.

Management

Founding family own c47% of the shares

The Hooper Family owns 47% of the LaserBond’s equity. Wayne and Greg Hooper are the CEO and CTO of the business respectively. We believe that the high level of management ownership means the business is more likely to be run in a way that is consistent with best interests of shareholders. We are also reassured by the long management tenure and track record: Greg and Wayne Hooper have worked for LaserBond for more than 25 years and the share price has risen by c650% over the past five years.

Wayne Hooper, Chief Executive Officer

Wayne Hooper is the CEO of LaserBond and is responsible for the sales, marketing and administration. He has worked for the company for 25 years. Prior to joining LaserBond in 1994, he held electrical engineering and marketing roles at ACI Insulation and the Electricity Commission of NSW.

Greg Hooper, Chief Technology Officer

Greg Hooper founded LaserBond in 1992 with help from his parents and a mortgage taken out on their property. The idea for the company came from Greg’s metallurgical background and exposure to cutting edge technology while working for multinational surface engineering equipment companies. Greg oversees the technical aspects of the business including technology R&D.

Philip Suriano, Non-executive chairman

Philip Suriano is the non-executive chairman of the group. Philip has more than fifteen years’ experience in the media industry including group sales director at Network Ten and National Sales Director at MCN (a JV between Foxtel and Austar).

Matthew Twist, Chief Financial Officer

Matthew Twist has been the company’s chief financial officer since 2007 and secretary since 2009. He has more than 25 years of experience in financial controlling for manufacturing companies.

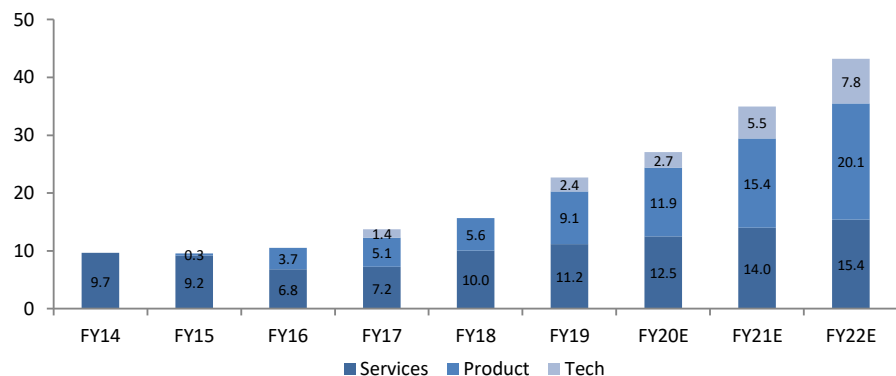
Forecasts

We forecast most of LaserBond's growth will come from product sales and technology licencing.

We forecast LaserBond revenues will grow from \$23m in FY19 to \$43m in FY22 (Figure 12). This is slightly higher than company guidance for \$40m revenue in FY22. Most of the growth should come from the Product and Technology segments which have fuelled most of the growth over the last four years.

- **Product:** Sales of Composite Carbide Steel Mill Rolls in the US and the commercialisation of new applications of laser cladding should underpin growth in the product segment.
- **Technology:** We expect the company will announce one new technology partner in FY20 and two partners per year from FY21. Revenue comprises of upfront equipment revenue, ongoing fees and the sale of consumables.
- **Services:** We expect the services segment should continue to grow steadily in line with the growth of major customers.

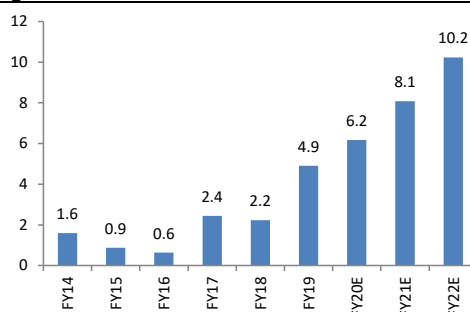
Figure 12: LaserBond Revenues by segment (\$m)



Source: Company data, Veritas estimates

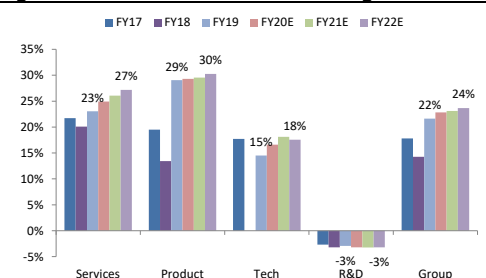
We forecast LaserBond EBITDA will more than double from \$4.9m in FY19 to \$10.2m by FY22 (Figure 13). The primary driver is our forecast that Services EBITDA margins should rise from 23% in FY19 to 27% in FY22 (Figure 14) on higher productivity from recent hiring and proportionately more production using the more efficient 16kW laser system. We expect Product EBITDA margins to be relatively steady as the company focuses on revenue growth and new applications. Technology margins should gradually improve as licenced equipment is commissioned and demand for the associated consumables grows.

Figure 13: LaserBond EBITDA



Source: Veritas, Company

Figure 14: LaserBond EBITDA margins



Source: Veritas, Company.

Fair value of \$1.50 per share

Our DCF derived fair value for LaserBond is \$1.50 per share (Figure 15). This is based on revenue growth fading to 2.7% in the terminal year, terminal capex to depreciation of 1x, a WACC of 8.5% and a terminal EBITDA margin of 25%.

Figure 15: LaserBond discounted cash flow valuation

Year end June	Units	FY20	FY21	FY22	FY23	FY24	FY25	FY26	FY27	FY28	FY29	TV
Revenue	\$m	27.1	34.9	43.2	51.9	57.1	62.8	65.9	69.2	72.7	76.3	78.4
Revenue growth	%	19.5	29.0	23.7	20.0	10.0	10.0	5.0	5.0	5.0	5.0	2.7
EBITDA	\$m	6.2	8.1	10.2	13.0	14.3	15.7	16.5	17.3	18.2	19.1	19.6
EBITDA margin	%	22.8	23.1	23.7	25.0	25.0	25.0	25.0	25.0	25.0	25.0	25.0
EBIT	\$m	5.1	6.9	9.0	11.4	12.6	13.8	14.5	15.2	16.0	16.8	17.2
Tax rate	%	27.5	27.5	27.5	27.5	27.5	27.5	27.5	27.5	27.5	27.5	27.5
NOPAT	\$m	3.7	5.0	6.5	8.3	9.1	10.0	10.5	11.0	11.6	12.2	12.5
DA	\$m	1.1	1.2	1.2	1.6	1.7	1.9	2.0	2.1	2.2	2.3	2.4
Working capital	\$m	-0.7	-1.9	-2.0	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.0
Capex	\$m	-1.5	-1.5	-1.8	-3.9	-2.6	-2.3	-2.0	-2.1	-2.2	-2.3	-2.4
Capex/D&A	x	1.4	1.3	1.5	2.5	1.5	1.2	1.0	1.0	1.0	1.0	1.0
FCF	\$m	2.6	2.7	3.9	6.1	8.4	9.8	10.6	11.1	11.7	12.2	12.5
Discount factor	%	92%	85%	78%	72%	67%	61%	56%	52%	48%	44%	
NPV of FCF	\$m	2.4	2.3	3.1	4.4	5.6	6.0	6.0	5.8	5.6	5.4	
Invested capital average		11.3	13.0	15.5	18.1	20.5	21.9	22.4	22.5	22.5	22.4	22.3
ROIC (post-tax)		33%	39%	42%	46%	45%	46%	47%	49%	52%	54%	56%
Item	Units	Value										
NPV of the forecast period	\$m	46.5										
NPV of terminal value	\$m	96.0										
NPV of cash flows	\$m	142.5										
Less: net debt	\$m	-0.7										
Fair value of equity	\$m	141.9										
Fair value of equity per share	\$ps	1.50										
Share count	m	95										
Item	Units	Value										
WACC	%	8.5										
Terminal growth	%	2.7										
Terminal EBITDA margin	%	25.0										
Terminal value nominal	\$m	217										
Terminal EV/EBITDA	x	11.1										
Terminal EV/NOPAT	x	17.4										

Source: Veritas estimates

High growth justifies a premium multiple

LaserBond currently trades on an EV/EBITDA of 8.6x in FY21 in line with the average of domestic and global peers (Figure 16). Our forecast for 28% EBITDA CAGR over the three years to FY22 is higher than the 7% sector median and justifies a higher multiple in our view. At our fair value the shares would trade on EV/EBITDA of 18x in FY21.

Figure 16: LaserBond relative valuation

Stock	Code	Price			EV	EV/EBITDA (x)			EV/Revenue (x)			P/E (x)			EBITDA Margin (%)			EBITDA Growth (%)		
		LC	LC m	LC m		19A	20E	21E	19A	20E	21E	19A	20E	21E	19A	20E	21E	19A	20E	21E
Laserbond	LBL-ASX	0.73	69	70	14.2	11.3	8.6	3.1	2.6	2.0	24.6	19.4	14.3	21.6	22.8	23.1	119.9	26.0	30.7	
Electro Optic Systems Holdings Limited	EOS-ASX	6.78	767	585	72.7	27.9	15.8	6.8	3.7	2.1	38.8	34.9	27.8	9.3	13.3	13.0	-197.0	160.9	76.2	
Korvest Ltd.	KOV-ASX	3.50	39	36	6.5	5.6	4.6	0.6	0.5	0.5	13.5	10.7	8.9	9.1	9.8	10.8	58.3	15.6	20.3	
OC Oerlikon Corporation AG	OERL-SWX	11.49	3,904	3,571	9.3	8.9	8.4	1.4	1.4	1.4	16.2	23.1	20.3	14.7	15.3	16.1	23.5	4.3	6.4	
AMG Advanced Metallurgical Group N.V.	AMG-AMS	20.36	639	1,122	6.4	10.3	8.9	1.0	1.0	1.0	7.7	28.2	13.6	15.8	10.0	11.0	69.5	-37.6	15.0	
Weir Group PLC	WEIR-LON	15.22	3,950	5,296	13.0	11.7	10.8	2.2	1.9	1.9	206.4	17.7	15.5	16.7	16.7	17.2	23.8	11.0	7.8	
Sandvik AB	SAND-OME	187.00	234,570	253,022	11.5	10.5	10.3	2.5	2.4	2.4	18.4	18.8	16.6	22.1	23.2	23.3	15.1	9.0	2.0	
Peer average					9.3	9.4	8.6	1.5	1.5	1.4	52.5	19.7	15.0	15.7	15.0	15.7	38.0	0.5	10.3	

Source: Veritas estimates, FactSet consensus. Note: Values are in domestic currencies.

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- BUY – anticipated stock return is greater than 10%
- SELL – anticipated stock return is less than -10%
- HOLD – anticipated stock return is between -10% and +10%
- SPECULATIVE – high risk with stock price likely to fluctuate by 50% or more

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