

Neogen Corporation (NEOG)

\$65.67 (As of 01/03/20)

Price Target (6-12 Months): **\$56.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 01/02/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:F

Value: D

Growth: C

Momentum: F

Summary

Neogen exited the second quarter of fiscal 2020 on a disappointing note, with lower-than-expected figures. Barring a sluggish Animal Safety show, strong international business and solid performance by the core Food Safety segment resulted in year-over-year revenue growth in the quarter. Key geographies like Europe, Brazil, Mexico, China, Australia and Canada reported robust growth in the quarter on strong global sales of test kits to detect food allergens as well as increased sales of products in the companion animal market. On the flip side, shares of Neogen have underperformed its industry over the past three months. Unstable economic conditions, currency issues and challenges in the animal protein market led to the disappointing performance in the Animal Safety business.

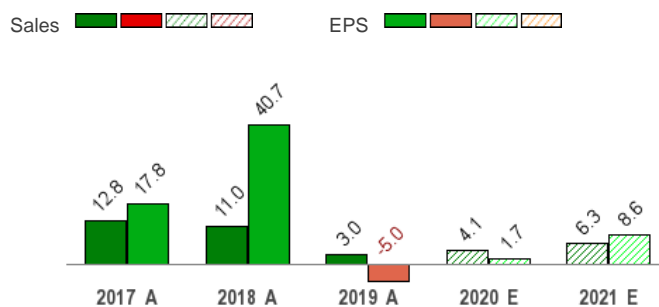
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$79.83 - \$50.60
20 Day Average Volume (sh)	209,257
Market Cap	\$3.5 B
YTD Price Change	0.6%
Beta	1.37
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Medical - Products
Zacks Industry Rank	Bottom 41% (148 out of 252)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-3.1%
Last Sales Surprise	-3.7%
EPS F1 Est- 4 week change	-2.5%
Expected Report Date	NA
Earnings ESP	-3.7%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	106 E	113 E	108 E	120 E	458 E
2020	101 A	108 A	103 E	115 E	431 E
2019	100 A	107 A	98 A	110 A	414 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.30 E	\$0.33 E	\$0.32 E	\$0.35 E	\$1.27 E
2020	\$0.28 A	\$0.31 A	\$0.27 E	\$0.31 E	\$1.17 E
2019	\$0.29 A	\$0.31 A	\$0.25 A	\$0.30 A	\$1.15 A

*Quarterly figures may not add up to annual.

P/E TTM	57.6
P/E F1	56.1
PEG F1	5.6
P/S TTM	8.3

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 01/03/2020. The reports text is as of 01/06/2020.

Overview

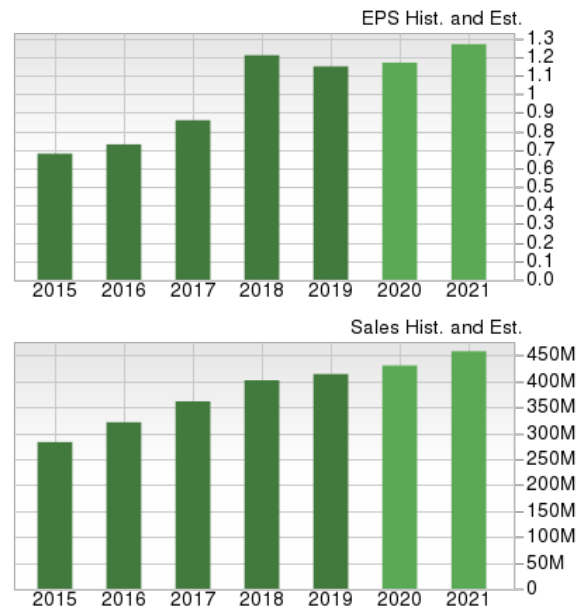
Neogen Corporation develops and markets food and animal safety products. The company's Food Safety Division markets culture media and diagnostic test kits to detect foodborne bacteria, natural toxins, food allergens, drug residues, plant diseases and sanitation concerns.

Neogen operates under two business segments — **Food Safety** and **Animal Safety**.

Food Safety (51.5% of total revenues in 2019, underlying growth rate was 9.8% from fiscal 2018): The products in the segment include tests for Mycotoxins, Food allergens, Dairy antibiotics, Foodborne pathogens, Spoilage microorganisms, Sanitation monitoring, Dehydrated culture media and Seafood contaminants. Revenues from Neogen's Food Safety segment accounted for 43.7% of the company's total revenues for fiscal 2018.

Animal Safety (48.5%, down 1.3%): The division is engaged in the development, manufacture, marketing and distribution of veterinary instruments, pharmaceuticals, vaccines, topicals, diagnostic products, rodenticides, cleaners, disinfectants, insecticides and genomics testing services for the worldwide animal safety market. The majority of these consumable products are marketed through a network of national and international distributors, as well as a number of large farm supply retail chains in the United States and Canada.

The animal safety products include Veterinary instruments, Veterinary pharmaceuticals, Veterinary biologics, Veterinary OTC products, Rodenticides, Cleaners and disinfectants, Insecticides, Animal genomics services and Life sciences. Revenues from Neogen's Animal Safety segment accounted for 51.2% of the company's total revenues for fiscal 2018.



Reasons To Sell:

- ▼ **Share Price Performance:** Shares of Neogen have underperformed its industry over the past three months. The stock has rallied 3% compared with the industry's 4.9% growth. In the last reported second quarter, the company registered lower than expected numbers. Animal protein segment declined significantly on continued soft performance in the niche market and continued inventory destocking within its distribution channels. Neogen's global financial operations has been adversely affected by the current macroeconomic environment across the globe. Fluctuating currency rates is also hampering Neogen's growth, given that it derives a substantial amount of its revenues from international markets.
- ▼ **Expensive Valuation:** Neogen's P/E (F12M) ratio is expensive in comparison to the broader industry. The company is currently trading at a forward P/E (F12M basis) ratio of 53.4 for the past year, whereas the current P/E ratio (F12 basis) for the industry it belongs to is 25.
- ▼ **Currency Headwinds:** Per Neogen, persistent weakness in the global animal protein market and strongly negative currency conversion posed as headwinds in fiscal 2019. Turbulent economic conditions in the production animal markets, U.S.-China trade tensions along with decreased sales to animal protein market distributor partners led to the disappointing performance of the Animal Safety segment. The negative currency movement effect is majorly due to weakening currencies against the dollar in Brazil and the U.K.
- ▼ **Competitive Landscape Tough:** Neogen faces intense competition from companies ranging from small businesses to divisions of large multinational companies. Some of these organizations have substantially greater financial resources than the company. Historically, Neogen has faced intense competition resulting from the development of new technologies by the company's competitor which could affect the marketability and profitability of Neogen's products.
- In this regard, we note that, in fiscal 2016, within Animal Care & Other product, the company was notified that a competitor had been granted approval on a new drug application for a competitive thyroid replacement product, effectively giving them exclusive rights to sell the product. As a result, Neogen is unable to sell its product into the domestic market effective July 2016, until it gets a similar regulatory approval.
- ▼ **Global Economic Problems Hamper Growth:** The current macroeconomic environment across the globe has adversely affected Neogen's financial operations. Governments and insurance companies continue to look for ways to contain the rising cost of healthcare. This might put pressure on players in the healthcare industry with Neogen being no exception. Moreover, fluctuating currency rates also hamper growth of companies like Neogen, given that it derives a substantial amount of its revenues from international markets. The company's sales are thus directly affected by unfavorable macroeconomic conditions. We are concerned that such macroeconomic softness might hamper the company's growth.
- Global economic issues continue to put pressure on Neogen's vast international trade. Also, tough competitive landscape and pricing pressure also weigh on the stock.

Risks

- **Long-Term Growth Strategy Progresses Well:** Neogen in its mission to be the leading company in the development and marketing of solutions for food and animal safety follows a vision or a growth strategy consisting of the following elements: increasing sales of existing products; introducing new products and product lines; expanding international sales; and acquiring businesses and forming strategic alliances.

Going by the first leg of the growth strategy, Neogen is progressing well in terms of picking the right growth markets and gaining bigger share of those markets. In terms of the second leg of the growth strategy, Neogen continues well with its strong R&D activities. With respect to the third leg of international growth, the company is expanding well in other geographies.

Regarding the fourth leg of inorganic growth, Neogen acquired Delta Genomics Centre in January 2019. Per management, the buyout is expected to boost Neogen's animal genomics business throughout Canada. The introduction of certain programs to fight a persistent sluggishness in a few Animal Safety end markets is also in Neogen's pipeline.

- **Food Safety Business on a Roll:** Neogen continues to see rising revenues from the Food Safety business. Management believes that a rising population and growing awareness about higher-quality food among the middle-class group are stimulating the niche market. Neogen's food safety business delivered impressive results in the second quarter of fiscal 2020 on rise in global sales of test kits to detect food allergens, with particularly impressive sales of gluten, milk, egg and tree nut kits. The increase in sales was supported by the introduction of a test kit for coconut in the past year.

In the fiscal second quarter, the company witnessed a 21% increase in sales of general sanitation tests. These tests include the product line to detect adenosine triphosphate (ATP) on food contact surfaces and in liquids. Sales of Neogen's line of foodborne pathogen (like Listeria and Salmonella) detection products also increased 11% in the current quarter compared with the prior-year quarter. The increase was driven by 25% rise in sales of tests to detect Listeria, including Listeria Right Now.

- **International Growth Continues:** In the second quarter of fiscal 2020, a major portion of Neogen's revenues (41%) came from international sources. After adjusting for adverse currency translations, revenues from outside of the United States increased 6% for the second quarter. Revenues for combined European operations increased 7%, Mexico-based Neogen Latino America's sales climbed 5% and Brazilian revenues rose 20% for the year. Neogen China's increase of 40% (albeit from a smaller base) whereas Neogen Australasia's quarterly revenue increased 18%. Neogen's sales performance in Brazil in the second quarter was driven by significant increases in insecticide sales to governmental agencies.
- **Genomic Business Progresses:** Neogen's worldwide animal genomics business unit recorded a double-digit revenue increase in the second quarter. Per management, this growth is attributable to significant increases in companion animal genomics business in key global markets such as the United States, Europe, Brazil and Australia.

In the second quarter, Neogen teamed up with International Genetic Solutions ("IGS"), which is a collaboration between progressive breed associations. The alliance is aimed to focus on enhancing genomic impact in the IGS platform (currently, the only available major multibreed beef genetic evaluation) and on improving research and development required to continue improving Neogen's Igenity Beef Profile. Neogen also received the AOAC Research Institute's approval for its Soleris for Enterobacteriaceae (EBAC). The test has been designed for the prevention of bacterial contamination of food, pet food, nutraceutical, pharmaceutical and cosmetic products.

Further, the company launched the Reveal Q+ MAX test to check for ergot alkaloids infection in rye and wheat. It received AOAC Research Institute's clearance for its Reveal 3-D for Peanut test to help prevent peanut residues from contaminating foods intended to be peanut-free.

Recently, the company announced the extension of its collaboration with the government of Ayr, Scotland through September 2021. Notably, the company will conduct genomics testing as part of the government's program to enhance the country's beef herd.

Last Earnings Report

Neogen's Q2 Earnings & Revenues Miss Estimates, Margin Rises

Neogen's earnings per share of 31 cents lagged the Zacks Consensus Estimate of 32 cents by 3.1% in second-quarter fiscal 2020. However, earnings per share was flat year over year.

Revenues in the quarter grew 0.7% on a year-over-year basis to \$107.8 million, missing the Zacks Consensus Estimate of \$111.9 million by 3.7%.

Per Neogen, growing revenues from key food safety products, including tests for foodborne pathogens, food allergen and general sanitation, contributed to top-line growth. Also, the newest global genomics locations in Australia and Canada contributed significantly to the company's overall genomics business. Continued double-digit growth in Neogen's global animal genomics business also boosted the top line.

The fiscal second quarter was the 111th of the last 116 quarters to mark a year-over-year revenue increase.

Revenues in Detail

Food Safety Segment: For the quarter under review, revenues in the segment totaled \$56.9 million, up 5.8% year over year. The year-over-year increase was driven by 14% rise in global sales of test kits to detect food allergens, with particularly impressive sales of gluten, milk, egg and tree nut kits. The increase in sales was supported by the introduction of a test kit for coconut in the past year.

Animal Safety Segment: During the second quarter, the segment recorded revenues of \$50.9 million, reflecting a 4.5% decline from the year-ago quarter. The downside mainly resulted from the continued soft performance of the company's animal protein markets and inventory destocking within its distribution channels.

Margin Details

Gross margin expanded 62 basis points (bps) to 47.3% in the fiscal second quarter.

In the reported quarter, operating income was \$18.3 million, which inched up 0.1% from the year-ago quarter's \$18.2 million. Operating margin contracted 9 bps to 16.9%.

Quarter Ending 11/2019

Report Date	Dec 23, 2019
Sales Surprise	-3.66%
EPS Surprise	-3.12%
Quarterly EPS	0.31
Annual EPS (TTM)	1.14

Recent News

On **Dec 19, 2019**, Neogen received approval from the AOAC Research Institute for its Soleris for Enterobacteriaceae (EBAC). The test has been designed for the prevention of bacterial contamination of food, pet food, nutraceutical, pharmaceutical and cosmetic products.

On **Dec 12, 2019**, Neogen launched the Reveal Q+ MAX test to check for ergot alkaloids infection in rye and wheat. The test, which is the first one for ergot alkaloids in the simple rapid lateral flow format, is compatible to be used with Neogen's Raptor testing platform.

On **Nov 25, 2019**, Neogen received approval from the AOAC Research Institute for its Reveal 3-D for Peanut test to check the presence of peanut in food. The test is intended to prevent peanut residues contaminating foods, which are not supposed to have it.

On **Oct 24, 2019**, Neogen launched the K-Gold Plus, a new PNPP (p-nitrophenyl phosphate) substrate that combines the ease of use of its previous PNPP substrate with an improved signal-to-background performance.

Valuation

Neogen shares are up 7.9% in the six-months period and up 14.7% in the trailing 12-month period. Stocks in the Zacks sub-industry are up 2.6% while the Zacks Medical sector rose 5.6% in the six-months period. Over the past year, the Zacks sub-industry is up 20.1% and sector is up 7.2%.

The S&P 500 index is up 9.2% in the six-months period and increased 25.6% in the past year.

The stock is currently trading at 53.4X Forward 12-months earnings, which compares to 25X for the Zacks sub-industry, 21.6X for the Zacks sector and 18.7X for the S&P 500 index.

Over the past five years, the stock has traded as high as 75.6X and as low as 37.9X, with a 5-year median 50X. Our Underperform recommendation indicates that the stock will perform below the market. Our \$56 price target reflects 45.5x forward 12-months earnings.

The table below shows summary valuation data for NEOG

Valuation Multiples - NEOG					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	53.39	25.03	21.59	18.70
	5-Year High	75.56	25.37	21.59	19.34
	5-Year Low	37.90	17.02	15.91	15.17
	5-Year Median	50.04	19.53	18.97	17.44
P/S F12M	Current	7.86	3.96	2.83	3.47
	5-Year High	11.19	3.96	3.80	3.47
	5-Year Low	4.82	2.88	2.42	2.54
	5-Year Median	6.50	3.21	2.94	3.00
P/B TTM	Current	5.01	3.11	4.56	4.42
	5-Year High	8.63	4.30	5.01	4.42
	5-Year Low	4.31	2.21	3.42	2.85
	5-Year Median	5.41	2.77	4.27	3.60

As of 01/03/2020

Industry Analysis Zacks Industry Rank: Bottom 41% (148 out of 252)



Top Peers

Bio-Rad Laboratories, Inc. (BIO)	Neutral
Elanco Animal Health Incorporated (ELAN)	Neutral
Laboratory Corporation of America Holdings (LH)	Neutral
3M Company (MMM)	Neutral
Merck & Co., Inc. (MRK)	Neutral
Phibro Animal Health Corporation (PAHC)	Neutral
Thermo Fisher Scientific Inc. (TMO)	Neutral
Zoetis Inc. (ZTS)	Neutral

Industry Comparison Industry: Medical - Products				Industry Peers		
	NEOG Underperform	X Industry	S&P 500	BIO Neutral	LH Neutral	MMM Neutral
VGM Score	F	-	-	B	A	C
Market Cap	3.46 B	299.00 M	23.66 B	10.98 B	16.24 B	102.62 B
# of Analysts	3	2	13	1	9	6
Dividend Yield	0.00%	0.00%	1.79%	0.00%	0.00%	3.23%
Value Score	D	-	-	D	A	C
Cash/Price	0.09	0.08	0.04	0.09	0.02	0.08
EV/EBITDA	35.00	0.42	13.88	19.80	10.95	13.30
PEG Ratio	5.61	2.56	1.99	2.75	1.64	1.95
Price/Book (P/B)	5.01	4.25	3.36	2.14	2.25	9.53
Price/Cash Flow (P/CF)	43.99	20.53	13.62	61.86	10.02	13.35
P/E (F1)	56.13	24.32	18.74	41.21	13.99	18.50
Price/Sales (P/S)	8.31	5.13	2.67	4.76	1.43	3.21
Earnings Yield	1.78%	0.86%	5.32%	2.43%	7.15%	5.40%
Debt/Equity	0.00	0.11	0.72	0.12	0.93	1.68
Cash Flow (\$/share)	1.49	-0.00	6.94	5.93	16.68	13.37
Growth Score	C	-	-	A	B	C
Hist. EPS Growth (3-5 yrs)	16.79%	10.04%	10.56%	16.50%	11.29%	6.54%
Proj. EPS Growth (F1/F0)	1.74%	13.97%	7.41%	23.61%	6.17%	6.57%
Curr. Cash Flow Growth	-3.00%	5.10%	14.83%	43.36%	9.98%	8.64%
Hist. Cash Flow Growth (3-5 yrs)	15.82%	9.87%	9.00%	9.81%	14.10%	5.24%
Current Ratio	12.89	2.78	1.23	4.72	1.17	2.30
Debt/Capital	0.00%	13.00%	42.92%	10.94%	48.26%	62.66%
Net Margin	0.00%	-10.65%	11.08%	16.14%	6.63%	15.48%
Return on Equity	14.35%	-7.21%	17.10%	4.30%	15.33%	54.02%
Sales/Assets	9.17%	0.64	0.55	0.34	0.66	0.81
Proj. Sales Growth (F1/F0)	0.59	11.84%	4.20%	4.01%	3.41%	5.03%
Momentum Score	F	-	-	B	B	B
Daily Price Chg	1.22%	0.00%	-0.61%	-1.45%	-0.15%	-0.86%
1 Week Price Chg	-5.71%	0.00%	0.13%	-1.19%	0.92%	1.08%
4 Week Price Chg	-3.23%	1.18%	2.60%	-0.61%	-2.19%	8.57%
12 Week Price Chg	4.82%	6.01%	8.87%	13.10%	1.66%	17.16%
52 Week Price Chg	21.25%	5.00%	29.34%	63.52%	35.19%	-2.89%
20 Day Average Volume	209,257	142,996	1,603,615	219,321	482,486	2,469,059
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-1.96%	0.00%	0.00%	0.00%	-0.03%	0.49%
(F1) EPS Est 12 week change	-2.50%	-1.76%	-0.57%	-1.11%	-1.12%	-3.61%
(Q1) EPS Est Mthly Chg	-3.84%	0.00%	0.00%	0.00%	0.00%	0.45%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	D
Growth Score	C
Momentum Score	F
VGM Score	F

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

Disclosures

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