

21st May 2020

## New COVID-19 workplace testing service

When in doubt about pandemics, ask an expert. One of the best being former FDA Commissioner Dr Scott Gottlieb (non-exec director of Pfizer & Illumina), who has been calling for widespread COVID-19 [workplace testing](#) for some time.

Today came news that there is now one such test available for all American businesses, freelancers, 'gig' workers &/or sole traders. This new tech-enabled solution is powered by CLSU's [ClearContact](#), [ClearID](#) and [Virtual Badge \(strategic partnership\)](#) applications, in conjunction with [Clinical Reference Laboratory's](#) (CRL) expertise in blood/antibody & saliva tests.

## Potential game changer and 1<sup>st</sup>-of-its kind soln,...

Indeed from 1<sup>st</sup> June, any ClearStar client will be able to access this seamless solution, using the same process as their existing drug & clinical screening programmes. The kits will be shipped either in bulk to the employer or direct to the employee (or job applicant), with the samples being returned to CRL for analysis. After which, the results should be available within 24 hours - a substantial improvement on the timescales that currently exist.

CEO Robert Vale adding "**Balancing the important goals of getting people back to work and ensuring their safety is top priority for employers. We are proud to be able to assist our customers in this process with the launch our new COVID-19 testing service, and by partnering with Clinical Reference Laboratory, whose tests are easy to administer, reliable and provide a quick turnaround.**"

## that could help America safely get back to work

In terms of magnitude, it is impossible at this stage to put any concrete numbers on the opportunity, albeit we understand CLSU performs approx 7,000 medical screens per month. So at a price point of say between \$100-\$175/unit, the solution (once fully rolled out) hypothetically might generate incremental revenues of between \$0.5m-\$1.0m/month. Excluding any new clients, who may also be attracted to the service.

What's more, **this type of fully automated coronavirus product could well be the first-of-its-kind nationwide.** The three big diagnostic labs (Quest, LabCorp and Abbott) will undoubtedly follow suit, but they don't yet appear to possess the straight through processing capability that ClearStar offers.

But that's not all.

### Company Data

EPIC	AIM: CLSU
Share price	41p
52 week Hi/Lo	73p/38p
Market cap	£14.9m
Sharecount	36.3m
Net debt 5 <sup>th</sup> May	\$1.0m
ED valuation / share	Withdrawn

### Share Price, p



Source: Share Cast

### Description

Floated at 54p/share in July'14, ClearStar is a tech-enabled Human Capital Integrity specialist serving the \$4bn global background & medical (MIS) screening market, which is growing at c. 4%-7% pa.

The firm is HQ'd in Georgia (99% US facing), and derives the majority of its revenues from high volume, low cost, 'everyday repeat' screens. Hence providing robust forward visibility and downside resilience.

**LFL growth** is being driven by multiple factors, including the rise of the gig economy, government crackdowns on illegal workers, legalisation of cannabis for recreational use and 'MIS & Direct'.

**Next News:** AGM June 2020

### Paul Hill (Analyst)\*

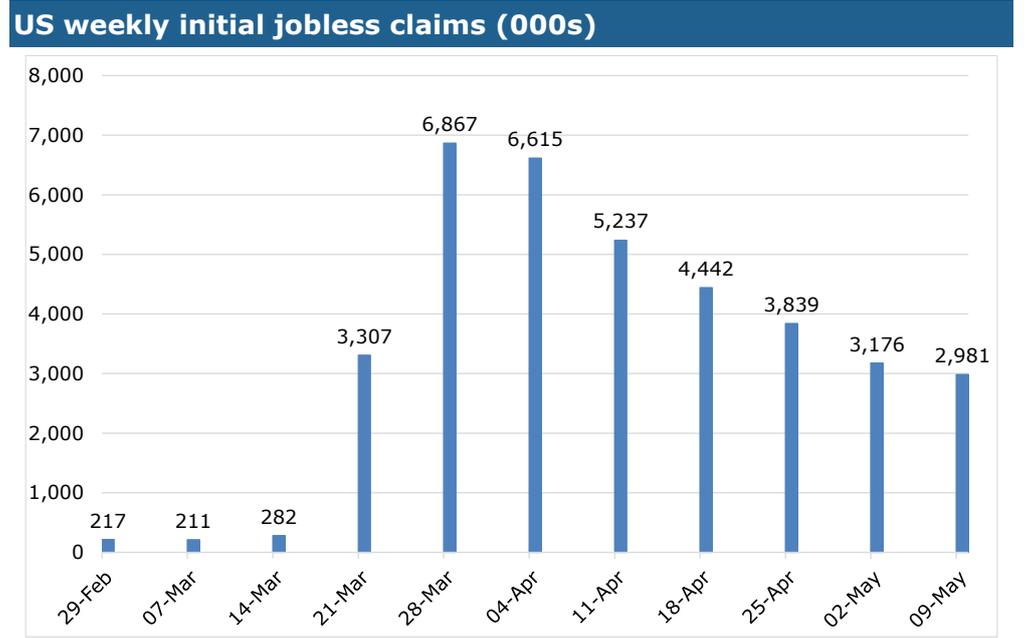
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\*Paul Hill is a shareholder in CLSU

## H2 demand surge anticipated as US reopens

Equally significant is that almost all [50 US states are now beginning to remove stay-at-home orders and gradually reboot](#) their regional economies. Housing activity is improving, restaurants, bars & non-grocery stores are reopening, and Congress has tabled another \$3 trillion stimulus package - with President Trump vowing to lift lockdowns "vaccine or no vaccine".

Meaning at some point, there is likely to be the 'mother-of-all-rehiring' sprees after the recent loss of 36m jobs (see below). Many of which should be slowly reabsorbed back into society.



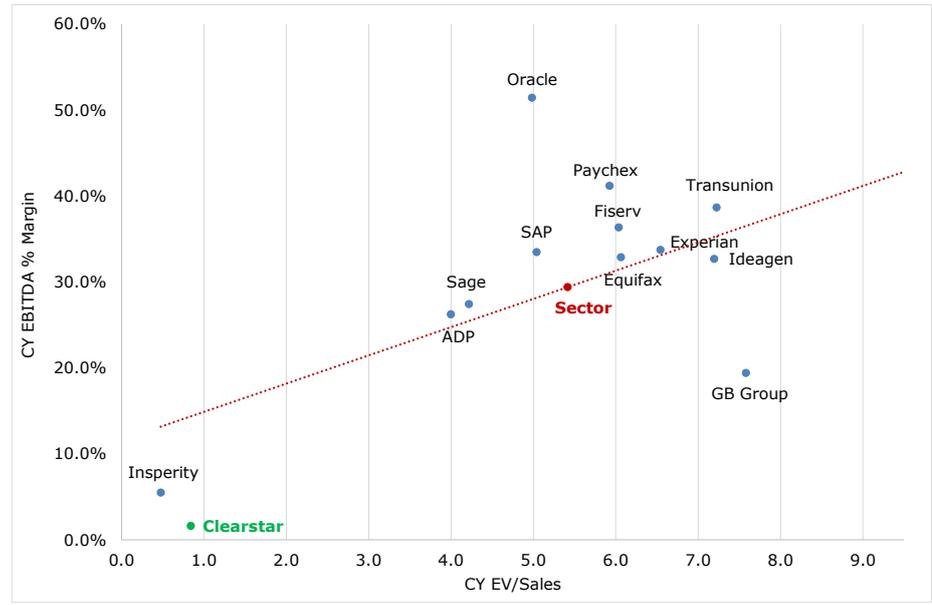
Source: Equity Development. US Dept of Labor,

## Stock appears materially undervalued

In turn, boosting employment screening providers like ClearStar. Sure turnover is presently being impacted (April down 50%), yet I suspect Q2'20 will prove to be the bottom. Thereafter the temporary 'lull' could quickly transform into a 1-2 year demand surge. Augmented too by any future ongoing requirements for employers to test staff for COVID-19 &/or any other contagious disease.

Lastly in terms of valuation, the shares (at 41p) trade on a modest 2019 EV/revs of 0.8x vs peers (pre coronavirus) at 2.5x – 3.5x.

**Current Year EV/sales multiple vs EBITDA margin**



Source: Equity Development. ClearStar & GB Group use 2019 numbers.

**Range of sector valuation benchmarks pre COVID-19 crisis**

Valuation benchmarks	ClearStar 2019 Trailing	Typical HR screening multiples pre COVID-19 crisis	
		Low	High
EV/Revenues	0.8	2.5	3.5
EV/EBITDA		12.5	14.0
EV/EBIT		15.0	16.5
PER		18.8	20.6
EBITDA margins	1.6%	20.0%	25.0%

Source: Equity Development

## Summary financials

<b>ClearStar (December yearend)</b>	<b>Act'14 \$'000s</b>	<b>Act'15 \$'000s</b>	<b>Act'16 \$'000s</b>	<b>Act'17 \$'000s</b>	<b>Act'18 \$'000s</b>	<b>Act'19 \$'000s</b>
Channel partners (non MIS)	6,554	6,980	7,387	7,475	7,056	6,468
Medical/drug testing - channel	3,890	4,770	4,850	5,610	7,055	8,567
Direct services (incl 15% medical)	477	3,766	3,795	4,700	6,002	7,918
<b>Turnover</b>	<b>10,921</b>	<b>15,516</b>	<b>16,032</b>	<b>17,785</b>	<b>20,113</b>	<b>22,953</b>
<i>MIS &amp; Direct % of group</i>	<i>40.0%</i>	<i>55.0%</i>	<i>53.9%</i>	<i>58.0%</i>	<i>64.9%</i>	<i>71.8%</i>
<i>Channel partners (non MIS)</i>	<i>-13.4%</i>	<i>6.5%</i>	<i>5.8%</i>	<i>1.2%</i>	<i>-5.6%</i>	<i>-8.3%</i>
<i>Medical/drug testing - channel</i>		<i>22.6%</i>	<i>1.7%</i>	<i>15.7%</i>	<i>25.8%</i>	<i>21.4%</i>
<i>Direct services (incl 15% medical)</i>	<i>59.0%</i>	<i>689.5%</i>	<i>0.8%</i>	<i>23.8%</i>	<i>27.7%</i>	<i>31.9%</i>
<b>% total growth</b>	<b>37.0%</b>	<b>42.1%</b>	<b>3.3%</b>	<b>10.9%</b>	<b>13.1%</b>	<b>14.1%</b>
<b>Gross Profit</b>	<b>6,331</b>	<b>9,493</b>	<b>9,835</b>	<b>10,349</b>	<b>11,340</b>	<b>12,410</b>
<i>% margin</i>	<i>58.0%</i>	<i>61.2%</i>	<i>61.3%</i>	<i>58.2%</i>	<i>56.4%</i>	<i>54.1%</i>
<b>EBITDA (post SBPs)</b>	<b>-1,267</b>	<b>-956</b>	<b>-666</b>	<b>-462</b>	<b>-108</b>	<b>370</b>
<i>% Margin</i>	<i>-11.6%</i>	<i>-6.2%</i>	<i>-4.2%</i>	<i>-2.6%</i>	<i>-0.5%</i>	<i>1.6%</i>
<b>Adj. EBITDA (pre SBPs)</b>	<b>-1,267</b>	<b>-956</b>	<b>-542</b>	<b>-398</b>	<b>157</b>	<b>381</b>
Opex	-8,071	-11,736	-11,930	-12,281	-12,674	-13,095
<i>Opex growth</i>			<i>1.7%</i>	<i>2.9%</i>	<i>3.2%</i>	<i>3.3%</i>
<b>Adj. EBIT (post SBPs)</b>	<b>-1,740</b>	<b>-2,243</b>	<b>-2,095</b>	<b>-1,932</b>	<b>-1,334</b>	<b>-685</b>
<i>% Margin</i>	<i>-15.9%</i>	<i>-14.5%</i>	<i>-13.1%</i>	<i>-10.9%</i>	<i>-6.6%</i>	<i>-3.0%</i>
Net interest	-17	-22	-16	-17	-68	-171
<b>Adj. Profit before Tax</b>	<b>-1,757</b>	<b>-2,265</b>	<b>-2,111</b>	<b>-1,949</b>	<b>-1,402</b>	<b>-856</b>
<b>Adjusted EPS (cents)</b>	<b>-4.8</b>	<b>-6.1</b>	<b>-5.6</b>	<b>-5.4</b>	<b>-4.0</b>	<b>-2.4</b>
<i>EPS growth rate</i>		<i>-26.2%</i>	<i>7.3%</i>	<i>4.5%</i>	<i>25.1%</i>	<i>40.5%</i>
Dividend (cents)						
<i>Yield</i>						
<b>Valuation benchmarks</b>						
<i>P/E ratio</i>						<i>-21.0</i>
<i>EV/Sales</i>	<i>1.8</i>	<i>1.2</i>	<i>1.2</i>	<i>1.1</i>	<i>1.0</i>	<i>0.8</i>
<i>EV/EBITDA</i>					<i>-179.1</i>	<i>52.3</i>
<i>EV / adj EBIT</i>					<i>-14.5</i>	<i>-28.2</i>
<i>Implied EBITDA drop through rates</i>		<i>6.8%</i>	<i>56.2%</i>	<i>11.6%</i>	<i>15.2%</i>	<i>16.8%</i>
<i>Adjusted tax rate</i>	<i>-0.2%</i>	<i>-2.3%</i>	<i>-2.9%</i>	<i>0.0%</i>	<i>0.0%</i>	<i>0.0%</i>
<i>Cash conversion (ie (EBTDA - Cap R&amp;D - W/Cap)/EBIT)</i>						
<i>PEG ratio</i>						
<b>Net cash/(debt)</b>	<b>6,124</b>	<b>3,630</b>	<b>2,253</b>	<b>1,240</b>	<b>923</b>	<b>-346</b>
Net debt : EBITDA						0.94
Capitalised NPD	-803	-1,396	-886	-712	-665	-1,422
Depreciation & amortisation	-473	-1,287	-1,429	-1,470	-1,226	-1,055
R&D + capitalised NPD as % sales	-8.8%	-14.2%	-15.9%	-14.6%	-11.5%	-12.0%
Sharecount (Ks)	36,303	36,303	36,303	36,303	36,303	36,363
<b>Shareprice (p)</b>	<b>41.0p</b>					

Source: Equity Development estimates, Company historic data. NB. Singlesource was acquired in December 2014

Note: As at 31st December 2019, CLSU had \$10,193k of unutilised tax losses, which can be utilised in future periods. These carry forwards however will begin to expire in 2023, but last until 2038.

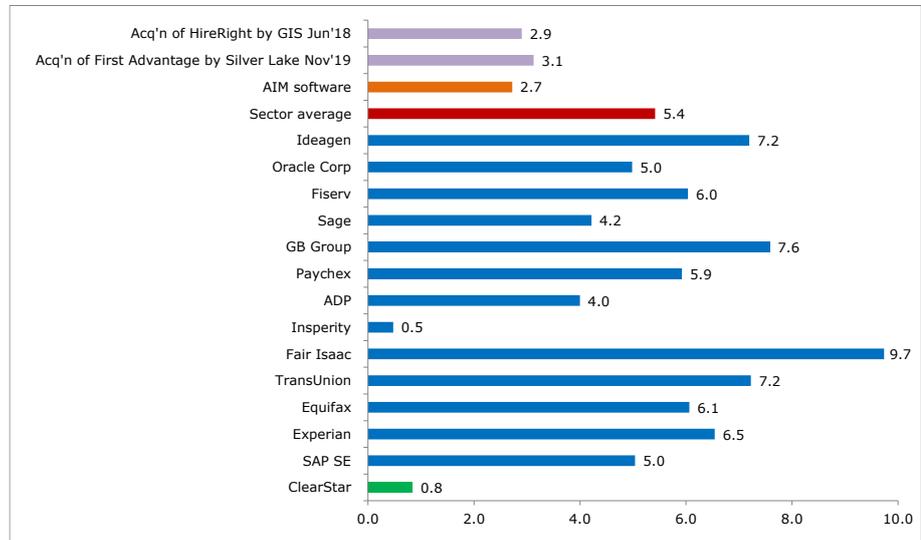
## Key risks

- Impact of a future recession on employment screening, although medical services should be far less affected by any economic downturn.
- Customer concentration, with the biggest account generating 11% of 2019 sales. This is a long term relationship with churn typically occurring only when a client is taken-over.
- Possible increase in bad debts due to COVID-19 induced downturn.

- Foreign exchange fluctuations for UK holders, given that >90% of turnover is derived from America.
- Being relatively small, ClearStar could get squeezed by its larger rivals, especially if there is further industry consolidation.
- The firm is presently loss making - hence it is important that sufficient resources continue to be made available. In the event more funding is required, then it is not certain that future capital would be available at commercial rates.
- Generic risks of greater competition, retention/recruitment of key staff, etc. Albeit this goes with the territory in the small-cap arena.
- Disruption caused to ClearStar's cloud based "Aurora & Sphere" platforms, such as from service outages, security breaches, etc.
- Supplier concentration. In 2019, CLSU bought \$5.7m of services from two vendors, representing 54% of group purchases.
- Possible adverse changes in employment law and local recruitment practises.
- ClearStar is registered in the Cayman Islands, and therefore does not fall under the UK Takeover Panel if it was ever approached by a third party.
- Protection of minorities, given that 49% of the shares are still held by directors/co-founders.

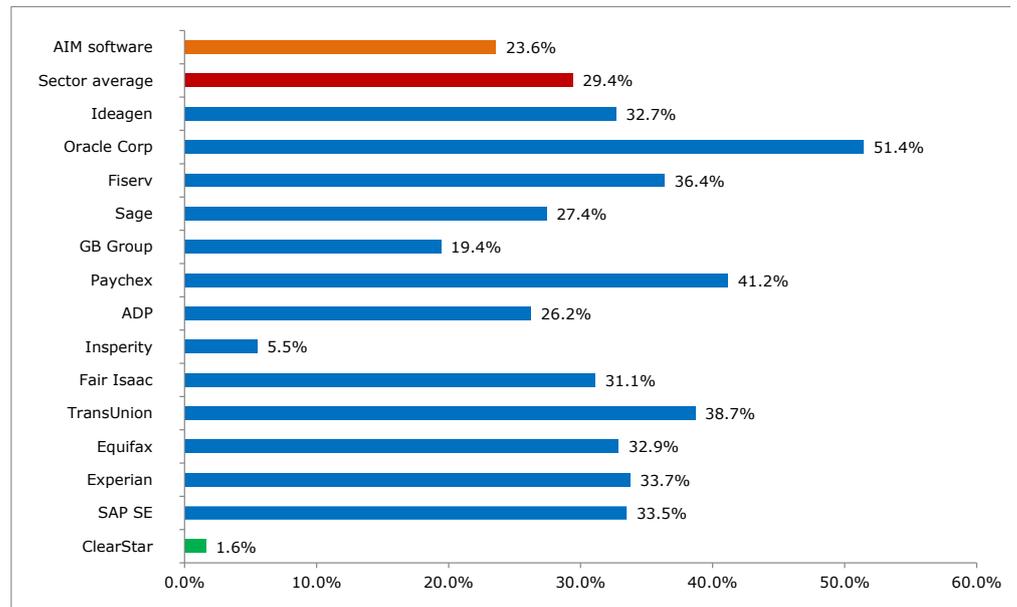
## Appendices - Sector valuation metrics and KPIs

### Current Year EV/revenue multiples



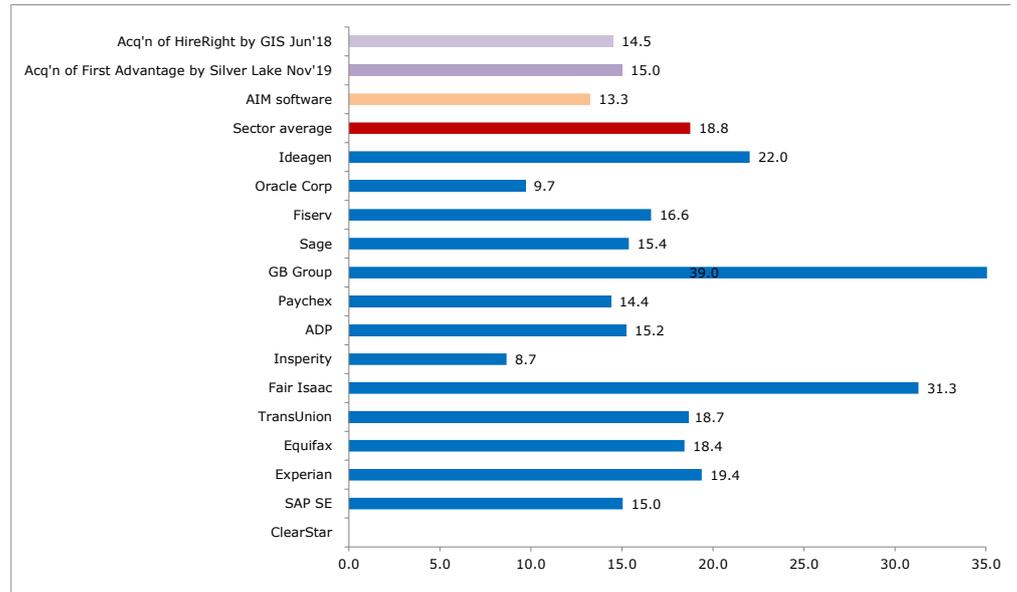
Source: Equity Development. ClearStar & GB Group use 2019 numbers

### Current Year EBITDA margins (post SBPs)



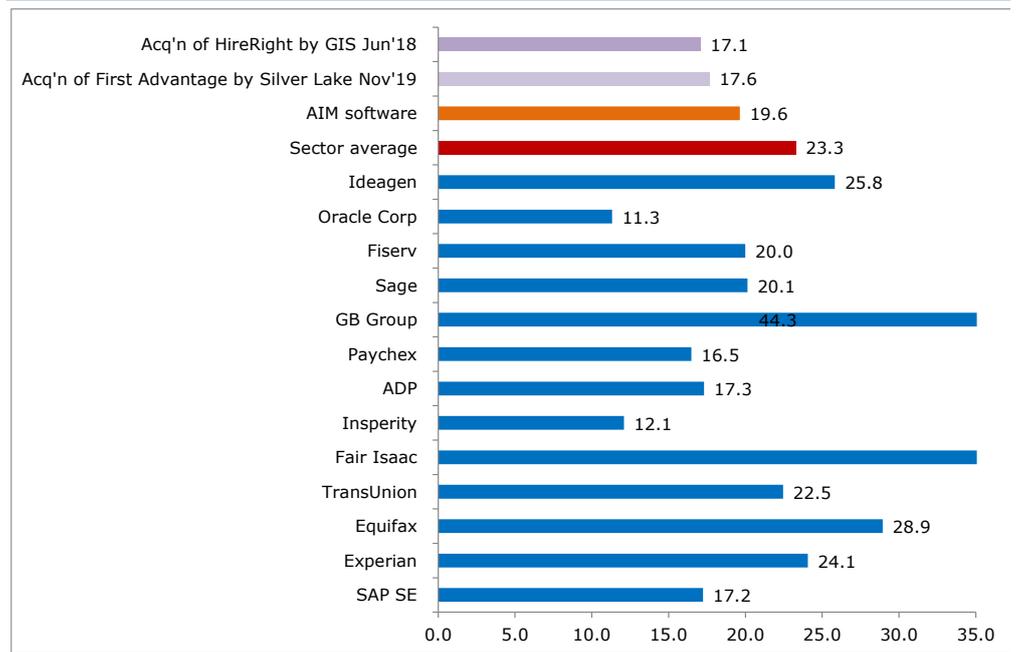
Source: Equity Development, arithmetic average for sector

### Current Year EV/EBITDA multiples



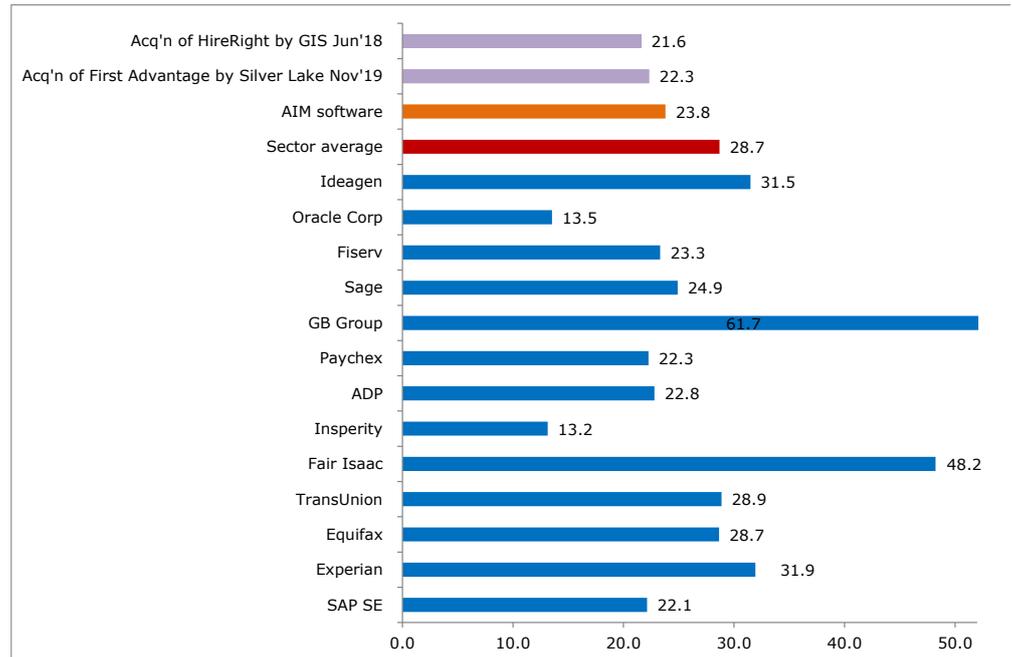
Source: Equity Development, arithmetic average for sector. 2019 numbers for GB Group

### Current Year EV/EBIT multiples



Source: Equity Development, arithmetic average for sector. 2019 numbers for GB Group

### Current Year PERs



Source: Equity Development, arithmetic average for sector. 2019 numbers for GB Group

### Market capitalisation of peers

	Description	Shareprice	Mrk Cap (Millions)	CY Net cash / (debt) Millions	Enterprise Value (Millions)
ClearStar	Tech-enabled employment & medical screening services	41p	£14.9	-£0.8	£15.7
SAP SE	ERP, accounting & HR software	€ 110	€ 130,900	-€ 10,586	€ 141,486
Experian	Credit checking & info services	\$33.21	\$30,221	-\$3,835	\$34,056
Equifax	Credit checking & info services	\$149	\$18,089	-\$2,980	\$21,069
TransUnion	Credit checking & info services	\$82	\$15,482	-\$3,383	\$18,865
Fair Isaac	Credit checking & info services	\$380	\$11,077	-\$781	\$11,858
Insperity	HR services	\$48	\$1,968	-\$161	\$2,129
ADP	Payroll services	\$135	\$58,104	-\$498	\$58,602
Paychex	Payroll services	\$67	\$24,120	-\$84	\$24,204
GB Group	ID verification	660p	£1,282	-£42	£1,323
Sage	ERP, accounting & HR software	675p	£7,358	-£394	£7,752
Fiserv	Financial services	\$104	\$71,240	-\$21,006	\$92,246
Oracle Corp	ERP, accounting & HR software	€ 52.50	€ 170,625	-€ 27,818	€ 198,443
Ideagen	Regulatory software	170p	£384.9	-£18.0	£402.9

Source: Equity Development



## Investor Access

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