Tecan Group AG (TECN.S – CHF 283.00)

September 12, 2024*

Tecan Group AG (TECN.S) provides laboratory automation products and develops and manufactures original equipment manufacturer (OEM) instruments, components, and medical devices distributed by partner companies. Tecan's customers include biopharmaceutical, biotechnology, pharmaceutical, medical technology, and clinical diagnostic companies, academic research departments, and diagnostic laboratories, among others. Tecan was founded in 1980 and is headquartered in Männedorf, Switzerland. Its fiscal year ends on 12/31.

Thesis Summary

We are concerned weak order trends suggest certain demand weakness driven by biopharmaceutical capital expenditure trends and China weakness may persist. In our view, Paramit growth may slow more than expected as pent-up demand abates and recent growth may have benefited from work on a customer's product ahead of the recent launch. Our concerns are heightened given elevated receivable levels, specifically contract assets relative to over time revenue, highlight slower quality revenue growth. We believe depressed Q4 23 remaining performance obligation coverage of FY 24 expected revenue suggests revenue expectations may be difficult to achieve. Elevated inventory relative to product revenue suggests inventory may be overbuilt and margins may be pressured. Our earnings sustainability concerns are heightened given depressed cash flow levels, increased capitalized research and development levels, and the recent departure of the head of the Life Sciences division.

Company Data	
Country/Exchange	Swiss/SIX
Reporting currency	CHF
Accounting standard	IFRS
Shares Outstanding (mil)	12.8
Float (mil)	12.8
Average Volume (mil)	CHF 10.0
52 Week Range	CHF 251.00 – CHF 392.00
Dividend Yield	1.1%
Market Cap (bil)	CHF 3.6
Net Cash (bil)	CHF 0.1
Enterprise Value (bil)	CHF 3.5
FY 23 Rev (mil)/Rev Growth	CHF 1,074.4 / (6.1%)
FY 23 Op. Income (mil)	CHF 136.0
FY 23 GM %/Change	36.3% / (190 bps)
FY 23 Op. Margin %/Chg	12.7% / (30 bps)

Valuation (as of report date)	
NTM P/S	3.3x
NTM P/E	29.6x

Consensus Estimate Drift

In CHF	EST	1M Ago	6M Ago	1YR Ago
FY 24 Rev	1,025.3	1,056.4	1,082.0	1,201.6
FY 25 Rev	1,090.0	1,090.0	1,162.1	1,292.9
FY 24 EPS	8.30	9.54	10.66	12.48
FY 25 EPS	10.10	10.10	12.10	14.16

Peers Mentioned In This Report

Intuitive Surgical, Inc. (ISRG)

Catalysts and Timing

- Weak H2 24 results and/or FY 25 guidance.
- Biopharma capex and China weakness persist.
- Paramit growth slows more than expected.
- Inventory and/or capitalized R&D normalization drives margin pressure.

*** All research is completed as of 4:00PM – 4:15PM Eastern Time unless otherwise noted.**
Please refer to the end of this report for an updated version of *The Short List*.
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VOYANT ADVISORS

Company Background

Company description: Tecan Group AG (TECN.S) provides laboratory automation products and develops and manufactures original equipment manufacturer (OEM) instruments, components, and medical devices distributed by partner companies. Tecan's customers include biopharmaceutical, biotechnology, pharmaceutical, medical technology, and clinical diagnostic companies, academic research departments, and diagnostic laboratories, among others. Tecan was founded in 1980 and is headquartered in Männedorf, Switzerland. Its fiscal year ends on 12/31.

Background on segments: In FY 23, the Partnering Business segment accounted for 57.5% (43.3%) of segment revenue (operating profit) and the Life Sciences segment accounted for 42.5% (56.7%). The Company's largest product group comprises laboratory automation platforms, benchtop instruments, and instrument components and sub-modules.

- **Partnering Business (OEM business):** Tecan develops and manufactures OEM instruments and components that are distributed by partner companies under their own names. The Partnering Business segment business lines include Synergence (OEM system development and lifecycle management focused on the development of automated solutions for diagnostics and life sciences), Cavro (standard and customized liquid handling OEM components), and Paramit (contract development and manufacturing).

- **Life Sciences Business (end-customer business):** Tecan offers automation solutions to improve the efficiency and standardization of end customers' workflows. The solutions include laboratory instruments, software packages, application know-how, services, consumables, and spare parts. In its FY 23 Annual Report, the Company disclosed "slightly over half" of the Life Sciences Business segment revenue was generated in the life science research end market. On its JP Morgan Healthcare Conference Call on 01/10/24, the Company highlighted half of the Life Sciences business was recurring revenue and the other half was capital expenditure related instruments (in FY 23, recurring revenue accounted for 52.8% of Life Sciences revenue).

FY 23 Segments Analysis (as % of total segment)	Revenue	Operating Profit
Partnering Business	57.5%	48.3%
Life Sciences	42.5%	56.7%
Total	100.0%	100.0%

Background on revenue recognition timing: In FY 23, revenue recognized at a point in time accounted for 61.3% of revenue, while revenue recognized over time accounted for 38.6% of revenue. In its FY 23 Annual Report, the Company disclosed over time revenue was recognized based on the cost-to-cost method and over time revenue related to complex instruments, contract manufacturing, and engineering services.

Revenue Timing Analysis (as % of revenue)	FY 23
Point in time	61.3%
Over time	38.6%
Leases	0.1%
Total	100.0%

Revenue by geography: In FY 23, Americas accounted for 56.9% of revenue, Europe accounted for 27.3%, Asia accounted for 14.7%, and other countries accounted for 1.1%.

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Geography Analysis (as % of revenue)	FY 23
Americas	56.9%
Europe	27.3%
Asia	14.7%
Others	1.1%
Total	100.0%

Background on manufacturing and distribution: In its FY 23 Annual Report, the Company disclosed it had manufacturing sites in Europe, North America, and Asia. Tecan sells products directly to end users and develops and manufactures OEM instruments, components, and sub-modules.

Competition: Tecan competes with various companies including Thermo Fisher Scientific Inc. (TMO), Hamilton Company (private), Waters Corporation (WAT), Bio-Rad Laboratories, Inc. (BIO), Agilent Technologies Inc. (A), Danaher Corporation (DHR), among others.

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Voyant's Earnings Risk Assessment

We are concerned weak order trends suggest certain demand weakness driven by biopharmaceutical capital expenditure trends and China weakness may persist. In our view, Paramit growth may slow more than expected as pent-up demand abates and recent growth may have benefited from work on a customer's product ahead of the recent launch. Our concerns are heightened given elevated receivable levels, specifically contract assets relative to over time revenue, highlight slower quality revenue growth. We believe depressed Q4 23 remaining performance obligation coverage of FY 24 expected revenue suggests revenue expectations may be difficult to achieve. Elevated inventory relative to product revenue suggests inventory may be overbuilt and margins may be pressured. Our earnings sustainability concerns are heightened given depressed cash flow levels, increased capitalized research and development levels, and the recent departure of the head of the Life Sciences division.

Weak Order Trends Suggest Biopharma & China Weakness May Persist, In Our View

FY 24 guidance reduction attributed to biopharma and China weakness: In its H1 24 Interim Report, the Company reduced its FY 24 constant currency revenue growth guidance from "low-single digit growth" to "flat or a mid-single digit decline." In addition, the Company reduced its FY 24 adjusted EBITDA margin guidance from "at least" 20.0% to "18.0% to 20.0%." On its Q2 24 Conference Call on 08/12/24, the Company attributed the guidance reduction to market weakness persisting longer than expected. Specifically, the Company highlighted restructuring and reduced capital expenditure spending in the biopharmaceutical sector and a more pronounced decline in China drove the guidance revision.

> What we've seen in 2024 is that the market weakness is persisting longer than anticipated with **restructurings and reduced CapEx spending in the biopharma sector, as well as a more pronounced decline of direct and indirect sales in China**. (CEO Dr. Achim von Leoprechting, Q2 24 Conference Call, 08/12/24)

FY 24 Guidance Analysis	Constant Currency Revenue Growth/Decline	Adjusted EBITDA Margin
Guidance per FY 23 Annual Report	Low-single digit increase	At least 20.0%
Revised guidance per H1 24 Interim Report	Flat or mid-single digit decline	18.0% to 20.0%

Weak order trends highlight limited demand improvement, in our view: In H1 24, orders declined 12.0% year-over-year to CHF 472.2 million from a depressed base period (declined 10.6% in H1 23). On its Q2 24 Conference Call, the Company highlighted orders improved sequentially in Q2 24 and it experienced "initial signs" of biopharma demand despite the situation "not resolving itself." While we acknowledge the Company highlighted certain demand improvement, we are concerned persistent order weakness (H1 24 orders were the lowest since H1 21) suggests weakness may persist longer-than-expected (i.e. beyond FY 24).

> Biopharma, we're getting initial signs now that the situation is indeed easing off. It's not resolving itself. That's why I mentioned earlier the pace of recovery is slower than expected, but we're now seeing some mobility. We're getting some orders in which we are already saw ending Q2. (CEO Dr. Achim von Leoprechting, Q2 24 Conference Call, 08/12/24)

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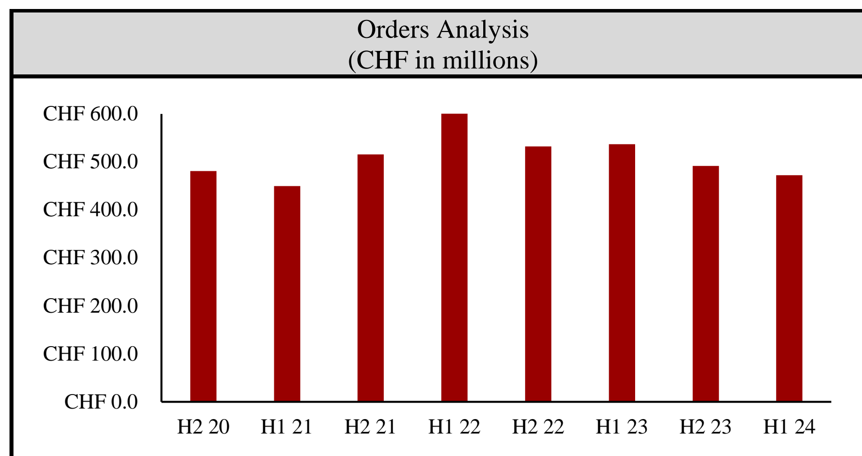

China demand may have deteriorated rapidly and/or China visibility may be limited, in our view: Previously, on its Q4 23 Conference Call, the Company represented China (direct and indirect) accounted for approximately CHF 145.0 million (13.5%) of FY 23 revenue. Further, the Company guided for FY 24 direct sales to local Chinese customers to decline in the mid-single digit percentage range and for indirect China business to also be negatively impacted but highlighted even with a China revenue decline the original FY 24 low-single digit growth guidance was attainable. Given the guidance reduction was attributed, in part, to China weakness despite prior commentary guiding for China revenue to decline, we are concerned China demand may have deteriorated rapidly and/or visibility may be limited. Therefore, we are concerned China revenue may disappoint and/or China demand weakness may persist longer than expected.

> Even in that kind of configuration of China being expected down year-over-year in 2024, in the framework that is kind of in the low-single digit growth. (CEO Dr. Achim von Leoprechting, Q4 23 Conference Call, 03/12/24)

Paramit Growth May Slow More Than Expected As Pent-Up Demand Abates

Partnering Business background: In FY 23, the Partnering Business segment accounted for 57.5% (48.3%) of revenue (operating profit). The Partnering Business segment develops and manufactures OEM instruments and components that are distributed by partner companies under their own names. The Partnering Business segment business lines include Synergence (OEM system development and lifecycle management focused on the development of automated solutions for diagnostics and life sciences), Cavro (standard and customized liquid handling OEM components), and Paramit (contract development and manufacturing, discussed next).

Paramit acquisition and revenue contribution background: In its 08/02/21 Press Release, Tecan announced it completed the acquisition of Paramit, an OEM developer and manufacturer of medical devices and life sciences instruments, for CHF 920.0 million. Tecan disclosed the acquisition extended its position in life sciences and in-vitro diagnostics and Paramit would be included in the Partnering Business segment. On its Q4 23 Conference Call, Tecan indicated Paramit accounted for approximately CHF 350.0 million (32.6%) of FY 23 revenue.

> **Analyst:** On Paramit, I guess, of course, it's getting harder to really and the sector is business from the remaining business. But nonetheless, I still was trying my luck there, for 2023 in terms of revenue number, is that something CHF 350 million, CHF 360 million a sort of a decent starting point for the revenue numbers?
>
> **CEO Dr. Achim von Leoprechting**: I would say, it's a good ballpark. It's around CHF 350 million. (Q4 23 Conference Call, 03/12/24)

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Paramit Revenue Contribution (CHF in millions)	FY 23
Paramit revenue	~CHF 350.0
Total revenue	CHF 1,074.4
Paramit as % of total	~32.6%

Outsized FY 23 Paramit growth guided to slow in FY 24 and reaccelerate in the medium term: On its Q4 23 Conference Call, the Company attributed double-digit FY 22 and FY 23 Paramit growth to (1) organic growth, (2) pent-up demand post-COVID, and (3) regional expansion. The Company guided for FY 24 Paramit revenue to increase low-single digits and reaccelerate to mid-single to high-single digit growth in the medium term.

> **Analyst:** Could you help us understand what has been driving the double-digit growth of Paramit and what level of growth is considered normally in the mid-term?
>
> **CEO Dr. Achim von Leoprechting**: I probably start off with the kind of the medical side double-digit growth. I mean, when we look back at the past periods 2022 and 2023, the medical side was growing very strong…we saw, I would say, a combination of organic growth, pent-up demand, regional expansion of our partners on the medical field during 2022, but particularly also in 2023, which were very strong years. And we expect this now to adjust on that kind of slope of growth to normalize that down to the kind of low-single digit growth in 2024. But midterm, we expect, I mean, the medical side to be in line with the growth of the group midterm outlook in the mid-single digit to high-single digit range. (Q4 23 Conference Call, 03/12/24)

H1 24 Paramit revenue may have underperformed, in our view: On its Q2 24 Conference Call, the Company represented Paramit revenue was "nearly" at the prior year level after adjusting for certain pass-through revenue in the prior year. Given guidance for Paramit to increase low-single digits in FY 24 and the recent commentary implied Paramit declined year-over-year in H1 24, we believe H1 24 Paramit revenue growth may have underperformed expectations.

> Sales in the Paramit product line, which primarily serves the medical market, were **nearly** at the high level of the prior year when adjusted for the pass-through revenues of material costs. (CFO Ms. Tania Micki, Q2 24 Conference Call, 08/12/24) [emphasis added]

Pent-up demand driven growth may portend Paramit growth pressure, in our view: As mentioned, the Company attributed certain FY 22 and FY 23 Paramit growth to pent-up demand. Accordingly, we are concerned the pent-up demand may have driven outsized growth in recent years and Paramit may continue to face challenging growth comparable periods. In our view, Paramit growth may underperform expectations as demand levels normalize (i.e. medium-term growth reacceleration may be weaker than expected).

Paramit and Intuitive Surgical have "long-term" relationship on products used in Intuitive's manufacturing: Previously, in its FY 22 Annual Report, Tecan disclosed Paramit had served as a "long-term" collaborator with Intuitive Surgical, Inc. (ISRG), a manufacturer of robots used in minimally invasive surgical procedures. Specifically, Paramit worked with Intuitive on "core products used in the manufacture" of Intuitive's surgical instruments, robotics, and training suites. Therefore, we believe Paramit worked with Intuitive to develop/manufacture the capital equipment used to manufacture Intuitive's products.

> Paramit has served as a long-term business collaborator with Intuitive, including work on several generations of **core products that are used in the manufacture of Intuitive's surgical instruments, robotics, and training suites**. (FY 22 Annual Report) [emphasis added]

Intuitive Surgical next generation robotic launch may pressure Paramit growth, in our view: In its Q2 24 10Q, Intuitive Surgical disclosed it received FDA clearance for da Vinci 5, Intuitive's next-generation multi-port robotic system in March 2024. Intuitive represented it was in the early stages of launching the da Vinci 5 system and guided for a "phased launch" over several quarters to allow it to mature its supply and manufacturing processes.

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While we acknowledge Tecan, and Paramit specifically, may continue to benefit from the new Intuitive system phased launch, we are concerned certain sell-in/work ahead of the launch may have driven outsized growth and revenue from Intuitive may slow. Our concerns are heightened given the FY 22 Annual Report disclosure suggested Paramit worked on Intuitive's capital equipment and not the robotic systems.

> In March 2024, we obtained FDA clearance for our da Vinci 5 surgical system, our next-generation multi-port robotic system, for use in all surgical specialties and procedures indicated for da Vinci Xi, except for cardiac and pediatric indications. We are in the early stages of launching da Vinci 5, and we have an installed base of 78 da Vinci 5 surgical systems as of June 30, 2024. We plan a phased launch over several quarters, giving us time to mature our supply and manufacturing processes for the new system. (ISRG Q2 24 10Q)

Elevated Receivable And Contract Asset Levels Highlight Revenue Risk

Background on contract assets and total receivable levels: In its FY 23 Annual Report, the Company disclosed contract assets were recognized for revenue earned for the installation of complex instruments, contract manufacturing, and engineering services without delivery of instruments (i.e. over time revenue recognition). Contract assets are reclassified to trade receivables to the extent they can be billed to the customer. Accordingly, we analyzed total receivable levels (i.e. DSOs) including trade receivables and contract assets.

> Contract assets are initially recognized for revenue earned for the installation of complex instruments, contract manufacturing as well as engineering services without delivery of instruments, if the contracts fulfil the criteria for revenue recognition over time. The amounts recognized as contract assets are reclassified to trade accounts receivable to the extent they can be billed to the customer. (FY 23 Annual Report)

Total receivable level surge highlights revenue risk, in our view: In H1 24, total receivables increased 4.4% year-over-year to CHF 183.0 million, while revenue declined 13.7% to CHF 467.2 million. Accordingly, total receivable DSO surged 21.7% to 71.3 days. On its Q2 24 Conference Call, the Company highlighted Company-disclosed DSO increased 10.9% year-over-year to 51.0 days (we believe Company-disclosed DSO is based on trade receivables).[1] Tecan attributed the DSO increase to certain payments from large customers arriving after the period end and indicated it was "not" concerned about receivable levels. While we acknowledge certain trade receivables may have been collected after quarter-end, we are concerned elevated total receivable DSOs may highlight (1) a back-end weighted period, (2) delayed customer payments, (3) elevated channel inventory, and/or (4) certain pulled forward over time revenue (discussed herein). In any scenario, we believe elevated total receivable levels highlight revenue risk.

> Our DSO, the day sales outstanding, was at 51 days, 5 days higher compared to the prior year period, mainly due to some payments from large customers arriving in the beginning of July and are therefore not of a concern. (CFO Ms. Tania Micki, Q2 24 Conference Call, 08/12/24)

[1] On its Q2 24 Conference Call, the Company highlighted DSOs increased five days year-over-year to 51.0 days H1 23 (i.e. base period) DSO of 46.0 days. Previously, on its Q1 23 Conference Call, the Company represented H1 23 DSO was 44.0 days. Given the updated commentary, we used 46.0 days as the H1 23 Company disclosed DSO.

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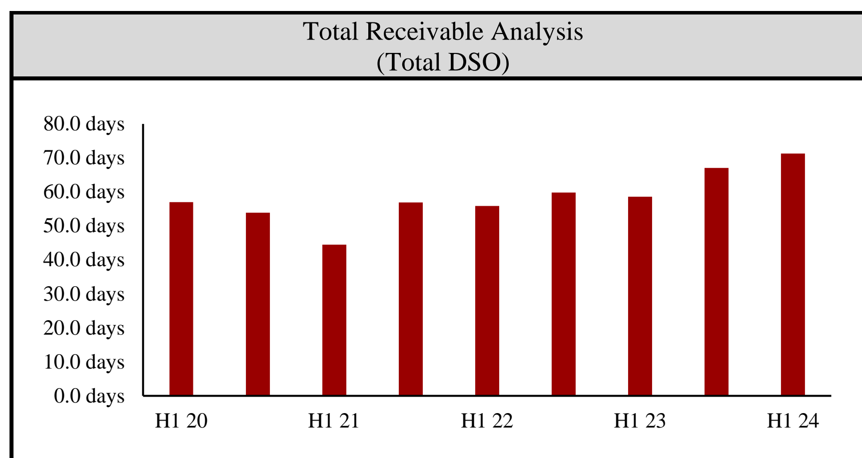

Partnering Business destocking may highlight elevated channel inventory, in our view: Previously, on its Q4 23 Conference Call on 03/12/24, the Company highlighted Cavro (a business line in the Partnering Business segment) OEM components revenue declined "substantially" due to a "significant" surge in demand in the prior year to mitigate against supply chain disruptions. On its Q2 24 Conference Call, the Company highlighted Cavro destocking persisted amidst prior over stocking and slower consumption due to an end market slowdown. Given elevated receivable levels and commentary about slowing end market Cavro demand, we are concerned certain destocking trends may persist and revenue may remain pressured.

> What we're looking at right now is a quite substantial number of Cavro component accounts, which are predominantly in the life sciences and/or biopharma segment seeing the same softness. And as you know, I mean, we are very exposed to application areas like sequencing there. And you just need to read the report of the affected companies that they've seen similar slowness of demand in that regard, more in academic and governmental account. So it's a combination of the previous stocking effect and our slower, if you want, destocking because the consumption of these existing levels of inventories is affected by the slowness of the respective end markets. (CEO Dr. Achim von Leoprechting, Q2 24 Conference Call, 08/12/24)

Revenue mix shifted to over time revenue recognition subsequent to Paramit acquisition: As mentioned, in its 08/02/21 Press Release, Tecan announced it completed the acquisition of Paramit, an OEM developer and manufacturer of medical devices and life sciences instruments, for CHF 920.0 million. Subsequent to the acquisition, over time revenue recognition increased as a percent of total. For example, in FY 20 (FY prior to acquisition) over time revenue accounted for 9.1% of revenue but in FY 22 (first full FY after acquisition) over time revenue accounted for 35.7% of revenue. Given the timing of revenue recognition shifted subsequent to the Paramit acquisition, we analyzed contract assets relative to over time revenue beginning in H2 21 (i.e. period Paramit was acquired) below.

Revenue Timing Analysis (as % of revenue)	FY 20	FY 21	FY 22	FY 23
Point in time	90.7%	80.1%	64.3%	61.3%
Over time	9.1%	19.8%	35.7%	38.6%
Leases	0.1%	0.1%	0.1%	0.1%
Total	100.0%	100.0%	100.0%	100.0%

Elevated contract assets relative to over time revenue heightens our concerns: In H1 24, contract assets surged 15.6% year-over-year to CHF 40.8 million, while over time revenue declined 0.7% to CHF 205.8 million. Accordingly, contract assets-to-over time revenue surged 16.4% to 0.198, the highest level since the Paramit acquisition. Further contract assets as a percent of total receivables increased 220 basis points to 22.3%. The Company did not discuss contract asset levels on its Q2 24 Conference Call or in its H1 24 Interim Report. We are

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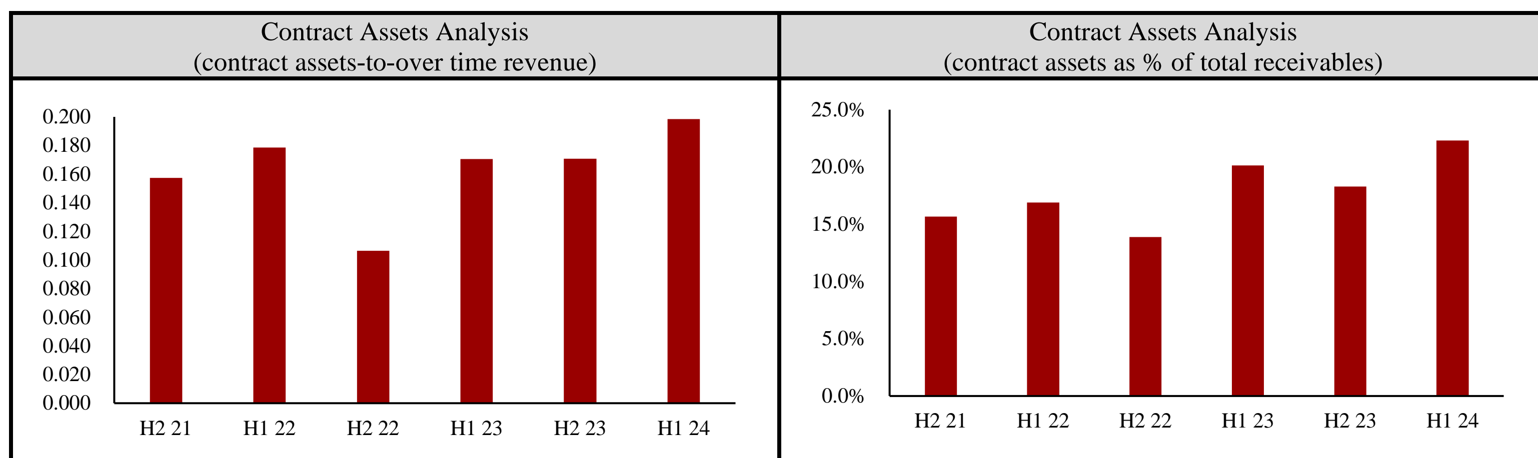
concerned the contract asset level surge may highlight pulled forward revenue and revenue growth risk may be elevated. Our concerns are heightened given evidence of weaker-than-expected/slowing Paramit growth (discussed heretofore) and we believe Paramit is more reliant on over time revenue recognition than the legacy business.



Depressed RPO Coverage Suggests Revenue Expectations May Be Difficult To Achieve

Background on remaining performance obligations: In its annual reports, the Company discloses unsatisfied or partially unsatisfied remaining performance obligations (RPO). Specifically, Tecan discloses current and non-current RPO and RPO already invoiced (i.e. contract liabilities) and RPO not yet invoiced. In H2 21, RPO surged 53.8% year-over-year to CHF 489.9 million. Accordingly, we believe the Paramit acquisition (completed in H2 21) may have driven an RPO surge and we analyzed RPO from Q4 21 through Q4 23.

Lowest RPO expected revenue coverage since acquisition suggests expectations may be difficult to achieve: In Q4 23, current RPO declined 18.5% year-over-year to CHF 358.4 million, while the consensus expects (as of the date of this publication) next-twelve-month revenue to decline 4.6% to CHF 1,025.3 million. Accordingly, Q4 23 current RPO next-twelve-month revenue coverage declined 600 basis points to 35.0%. In our view, depressed current RPO coverage suggests revenue expectation achievability may be more dependent on booked and burned revenue and revenue expectations may be difficult to achieve.

Current RPO Revenue Coverage Analysis (CHF in millions)	Q4 21	Q4 22	Q4 23
Current RPO (as of Q4)	CHF 455.3	CHF 440.0	CHF 358.4
NTM revenue (CE for FY 24 revenue)	CHF 1,144.3	CHF 1,074.4	CHF 1,025.3
Current RPO revenue coverage	39.8%	41.0%	35.0%
Change	--	*120 bps*	*(600 bps)*

Inventory May Be Overbuilt And Margins May Be Pressured, In Our View

Elevated inventory relative to product revenue suggests margins may be pressured, in our view: In H1 24, inventory declined 2.0% year-over-year to CHF 280.6 million, while product revenue declined 14.9% to CHF 388.6 million. Accordingly, inventory-to-product revenue surged 15.2% to 0.722, the highest level in four years. The Company did not discuss inventory levels on its Q2 24 Conference Call or in its H1 24 Interim Report. Given inventory levels surged to a multi-year high, we believe inventory may be overbuilt and margins may be pressured as the Company attempts to normalize inventory levels.

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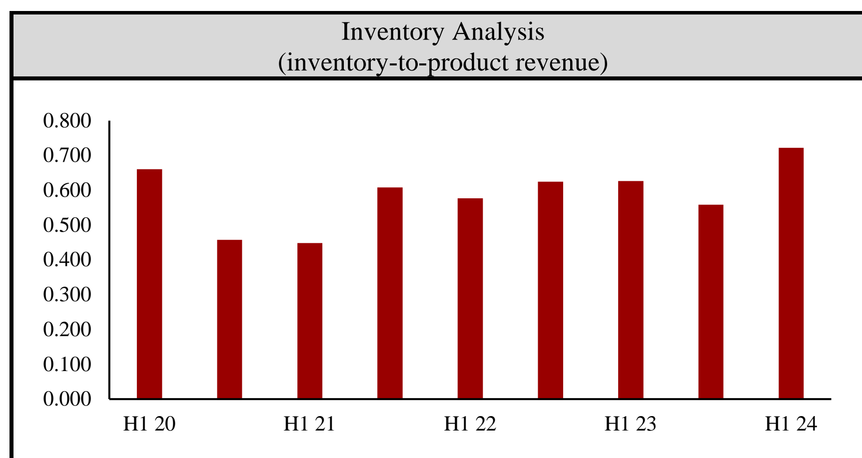
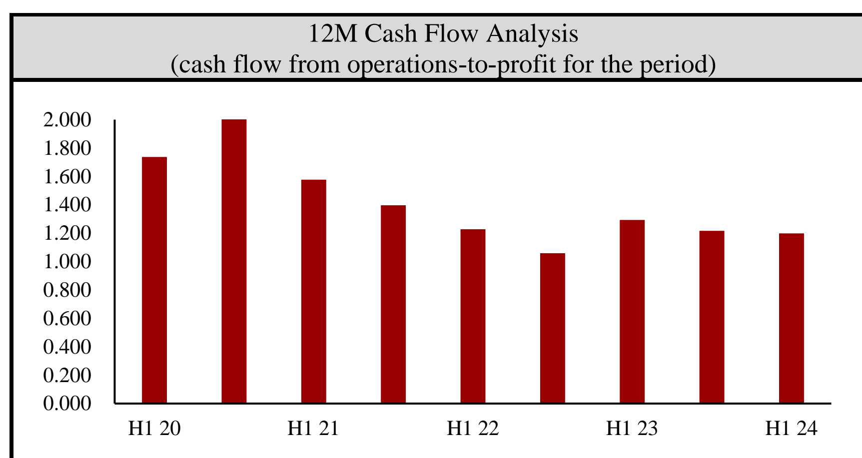


Depressed Cash Flow Relative To Profit Heightens Our Earnings Sustainability Concerns

In the twelve months ended H1 24, cash flow from operations declined 13.5% year-over-year to CHF 121.5 million, while profit for the period declined 6.7% to CHF 101.3 million. Accordingly, cash flow from operations-to-profit declined 7.2% to 1.199, the second lowest level since at least H1 20 (lowest level was H2 22). Working capital consumed CHF 28.1 million of cash during the period. Depressed cash flow levels driven, in part, by working capital cash consumption heighten our earnings sustainability concerns.



Capitalized R&D Increased To Highest Level Since Paramit Acquisition

Background on R&D disclosure and analysis: In its Annual Reports, the Company discloses gross research and development (R&D) costs incurred, the reclassification of R&D costs related to engineering services to cost of sales, capitalization of R&D in inventory, and capitalization of R&D in intangibles assets. In its FY 23 Annual Report, the Company disclosed it capitalized R&D after technical feasibility had been demonstrated until the product was ready for market launch. We analyzed capitalized R&D levels as R&D capitalized in intangible assets relative to gross R&D spend net of capitalized R&D in inventory and reclassified R&D to cost of sales.

Capitalized R&D level increase to three year high may highlight margin risk, in our view: In FY 23, gross R&D net of R&D capitalized in inventory and R&D reclassified to cost of sales declined 9.8% to CHF 65.4 million, while capitalized R&D in intangible assets increased 6.6% to CHF 12.3 million. Accordingly, capitalized R&D as a percent of gross R&D spend increased 290 basis points to 18.8%, the highest level in three years. In its FY 23 Annual Report, the Company disclosed the Partnering Business was less development-intensive. While we acknowledge capitalized R&D relative to gross R&D spend was below FY 20 and FY 19 levels, to the extent the

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Paramit acquisition (completed in H2 21) impacted R&D capitalization, we would be concerned the capitalized R&D level increase to the highest level since the acquisition may portend margin pressure. Specifically, we believe margins may be pressured as R&D capitalization levels normalize (i.e. certain recurring spend no longer qualifies for capitalization) and/or as capitalized R&D amortization ramps.

R&D Capitalization Analysis (CHF in millions)	FY 19	FY 20	FY 21	FY 22	FY 23
Gross R&D spend, net	CHF 61.3	CHF 64.0	CHF 69.4	CHF 72.5	CHF 65.4
Capitalized R&D in intangible assets	CHF 12.4	CHF 15.3	CHF 9.6	CHF 11.6	CHF 12.3
Capitalized R&D as % of gross spend	20.2%	24.0%	13.8%	15.9%	18.8%
Change	--	*370 bps*	*(1,010 bps)*	*210 bps*	*290 bps*

Recent Head Of Life Sciences Division Departure May Increase Disruption Risk

In its 06/24/24 Press Release, the Company announced Head of the Life Sciences Business Dr. Klaus Lun decided to leave the Company to pursue other opportunities (in its Press Release on 07/12/24, LRE Medical (private) announced it appointed Dr. Klaus Lun CEO effective 11/01/24.). The Company indicated Ms. Mukta Acharya would assume the position of Head of the Life Sciences Business on 08/01/24 (previously, she was President, Tecan Americas). The recent Head of Life Sciences Business departure may highlight Life Sciences demand weakness and/or increase near-term business disruption risk.

Conclusion

We are concerned weak order trends suggest certain demand weakness driven by biopharmaceutical capital expenditure trends and China weakness may persist. In our view, Paramit growth may slow more than expected as pent-up demand abates and recent growth may have benefited from work on a customer's product ahead of the recent launch. Our concerns are heightened given elevated receivable levels, specifically contract assets relative to over time revenue, highlight slower quality revenue growth. We believe depressed Q4 23 remaining performance obligation coverage of FY 24 expected revenue suggests revenue expectations may be difficult to achieve. Elevated inventory relative to product revenue suggests inventory may be overbuilt and margins may be pressured. Our earnings sustainability concerns are heightened given depressed cash flow levels, increased capitalized research and development levels, and the recent departure of the head of the Life Sciences division.

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Risks to Our Thesis & Valuation

Mid-Term Guidance, M&A Focus, Synergies, And Megatrends

Mid-term guidance to outperform the market and improve profitability: In its FY 23 Annual Report, the Company reiterated its mid-term guidance to outperform the average growth rate of its underlying end markets with average organic growth rates in the mid-to-high single digit percentage. In addition, the Company guided to "continuously" improve profitability. On its Q2 24 Conference Call, the Company reiterated its mid-term guidance and guided for adjusted EBITDA margin to increase 30 to 50 basis points annually on average. The Company guided for market normalization beginning as early as FY 25.

> 2024 has proved to be a more challenging year than expected, but we do see these effects as temporary. Because of this, we are confident in reaffirming our midterm outlook. We expect to return to sales growth that outpaces the average growth rate of the underlying end markets, anticipating in the midterm to return to average organic growth rates and in the mid to high single-digit percentage range in local currencies. This normalization of the market potentially beginning as early as 2025. (CEO Dr. Achim von Leoprechting, Q2 24 Conference Call, 08/12/24)

Capital deployment focus on mergers and acquisitions to drive inorganic growth: On its Q2 24 Conference Call, the Company highlighted it continued to focus on inorganic strategic expansion through mergers and acquisitions (M&A). Specifically, the Company represented M&A would continue to be its primary capital deployment strategy. Tecan highlighted inorganic growth allowed it to materially outgrow the market over the last decade with an organic compound annual growth rate (CAGR) 8.1%, and a CAGR of 12.8% including M&A compared to the market CAGR of 3.0% to 5.0%.

> We are also continuing to focus on leveraging our strong financial position for further inorganic strategic expansion through M&A. M&A will continue to be our primary capital deployment strategy. (CEO Dr. Achim von Leoprechting, Q2 24 Conference Call, 08/12/24)

Ten-Year CAGR Analysis	CAGR (per Q2 24 Conference Call)
Market (at midpoint)	4.0%
Tecan organic	8.1%
Tecan including M&A	12.8%

Synergies between across segments and business lines: In its FY 23 Annual Report, the Company highlighted synergies between its Life Sciences Business and Partnering Business segments. In addition, on its Q2 24 Conference Call, the Company highlighted certain new projects were secured due to synergies within its Partnering Business (i.e. between the Cavro, Synergence and Paramit business lines).

> In the Partnering Business, there has been robust project activity across all three business lines. And what we're seeing as well is the combined strengths of these where projects have been secured, for example, at Paramit because of synergies with Cavro and/or Synergence. (CEO Dr. Achim von Leoprechting, Q2 24 Conference Call, 08/12/24)

Megatrend beneficiary: In its FY 23 Annual Report, the Company highlighted certain megatrends the markets it participates in benefit from. Specifically, the Company highlighted megatrends such as population growth and ageing, high levels of healthcare investment, development of targeted pharmaceuticals and innovative surgical procedures, "explosion" of knowledge in the field of biological correlation and processes, and digitalization of processes and increased regulatory complexity. Tecan disclosed it "systematically focused" on the megatrends to obtain "significant benefits."

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Valuation Analysis

As of the date of this publication, Tecan shares traded at 29.6x next-twelve-month earnings, 6.1% above the peer group average.

Valuation Analysis	NTM P/E
Tecan Group AG (TECN.S)	29.6x
Thermo Fisher Scientific Inc. (TMO)	27.1x
Waters Corporation (WAT)	26.4x
Bio-Rad Laboratories, Inc. (BIO)	29.7x
Agilent Technologies Inc. (A)	24.3x
Danaher Corporation (DHR)	32.8x
Peer group average	28.0x
TECN.S above (below) peer group average	*5.7%*

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Disclaimer and Disclosure

This report was produced by Voyant Advisors, LLC ("Voyant"). The following Research Analysts employed by Voyant contributed to this report: Graeme Lazarus, Ryan DesJardin, Andrew Brown, Duran Sulymankhel, and Adam Yribarren. Voyant's home office is at 15373 Innovation Dr, Suite 365 San Diego, CA 92128. The firm's home office is where information about the valuations herein are located, unless otherwise indicated in the report.

At the time of this report, Voyant expects to provide updates on a quarterly or semi-annual basis depending on the frequency of when the above company discloses material financial results. We will cease providing updates if we are discontinuing research coverage as disclosed on the front page of this report in the Thesis Summary.

Voyant has not provided previous recommendations concerning the same financial instrument or issuer during the preceding twelve-month period.

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