Stealth Global Holdings

Positional paper

Going national & international

Stealth Global Holdings Ltd (ASX:SGI) is an international supply and distribution group providing a wide range of safety, industrial, workplace and healthcare consumable products and supply chain solutions to business customers across the resource, infrastructure, transport, construction and engineering sectors. SGI was listed in September 2018 after raising $12.5m at $0.20/share. The raise was predominantly for the acquisition of WA based Industrial Supply business Heatleys ($9.0m) and additional working capital. Since the IPO management has wasted no time building the business, integrating Heatleys, forming a Joint Venture with Bisley Workwear to enter the UK/European market and acquiring industrial buying group Industrial Supply Group (ISG), creating an Australian East Coast presence. Longer term the group has a target of achieving $200m in sales revenue by 2024 (~$74m in FY19). Such activity does not come without cost, with reported near-term numbers impacted by start-up and transaction costs. Even with these costs SGI is trading well below selected small cap distribution "peers" on an EV/sales and FY19 PER basis. We see both earnings and "ratings" upside for SGI over the medium-term as reported numbers and growth options are better understood.

Scope

This report has been commissioned by Stealth Global Holdings Ltd to present an explanation of the business model and to explore the value created from recent and possible future deals.

Business model

Stealth Global Holdings is a business to business distributor of a wide range of industrial, safety and workplace consumable products. In addition to traditional wholesale supply and wide range distribution, Stealth seeks to establish preferred and/or exclusive sales arrangements with suppliers and/or customers, establishing a key point of differentiation with peers. Such arrangements target new markets (such as the Bisley Workwear JV in the UK) or whole site contract logistics (such as the Capital Drilling contract in Africa). Resulting volumes offer a virtuous circle of scale, operational efficiency and margin growth. Since FY16 the group has delivered CAGR pro-forma revenue growth of 11.3%, with 1H19 growth +13%.

Base case valuation of $0.37/share or $35m

Our base case DCF valuation is $0.37/share or $35m. As a sense check the business was listed with a $20m valuation and has made an accretive acquisition (pre one-off costs) and has subsequently established an exciting JV in the UK. A distribution peer comparison check also highlights a significant discount to peers on a range of measures, albeit there is some distortions/confusion in the FY19 year for SGI, which we explain in this paper.

Historical earnings and RaaS Advisory estimates

Year end	Revenue (A$m)	EBITDA reported (A$m)	NPAT reported (A$m)	EPS* (c)	P/E (x)	EV/Sales (x)
06/18a	65.9	2.7	1.6	0.02	5.2	0.12
06/19e	74.0	1.9	1.5	0.02	5.6	0.11
06/20e	79.1	2.6	1.7	0.02	5.0	0.09
06/21e	89.8	5.2	3.3	0.03	2.6	0.07
06/22e	99.4	7.5	4.6	0.05	1.9	0.05

Source: Company data, RaaS Advisory Estimates for FY19e, FY20e, FY21e and FY22e

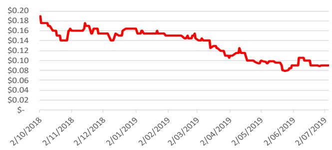
Retail and wholesale distribution

8th July 2019

Share details

ASX Code	SGI
Share price	$0.09
Market Capitalisation	$8.5M
Shares on issue	94.9M
Net cash (F) at 30 June 2019	~$0.5M
Free float	~85%

Share performance (since listing)



Upside Case

- Service based model takes market share from incumbent players
- With size comes improved gross margins from buying and mix opportunities
- The opportunity to participate in national supply contracts for the first time

Downside Case

- Acquisitions fail to deliver expected revenues and/or synergies/efficiencies.
- Larger competitors react with sharper price offerings
- Largest customer and/or supplier go direct

Board of Directors

Christopher Wharton	Non-Executive Chairman
Michael Arnold	Managing Director
Giovanni Groppoli	Non-Executive Director
Peter Unsworth	Non-Executive Director

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Table of contents

Stealth Global Holdings Limited

Stealth Global Holdings was listed in September 2018 after raising $12.5m at $0.20/share. The raise was predominantly for the acquisition of WA based Industrial Supply business Heatleys ($9.0m) and additional working capital. Since the IPO, management has wasted no time building the business, integrating Heatleys, forming a Joint Venture with Bisley Workwear to enter the UK/European market and acquiring industrial buying group ISG, strengthening the groups Australian East Coast presence. Proforma organic sales growth over 1H19 was 13%, with Australia up 18% and Africa down 4%, while pro-forma EBITDA was up 8%. The share price arguably does not reflect this progress, with investors possibly grappling with the group's seasonality, a number of "one-off" charges taken "above the line" and a generally weak "micro-cap" market. This positioning paper will explore the business model, changes to the business post IPO and the long-term potential of Stealth Global.

Investment case

In our view, Stealth Global has the opportunity for both strong earnings growth and a concurrent "re-rating" over the medium-term for the following reasons:

- The "reported" numbers of SGI for both FY19 and possibly FY20 do not reflect the true underlying and long-term potential earnings of the group, as it conservatively takes a number of initial investment costs "above the line" in the very early stages of market penetration;
- Through its procurement alliance with Capital Drilling (CAPD: LON) in Africa, Stealth has established a template and footprint that may see similar agreements put in place with large miners and/or mining services businesses. Such a deal could see a "step-change" in sales and EBITDA;
- The acquisition of the Industrial Supply Group (ISG) while small in nature offers SGI a low-cost entry into the Australia East Coast market, with its current lack of presence precluding bids on national contracts;
- Stealth/Heatleys continues to chip away at incumbents in the Australian market with a focus on service. Stealth's total sales relative to market leader Wesfarmers Industrial & Safety is estimated at 4%, and ex-African sales more like 3% providing significant market share opportunities;
- As the group increases scale private label opportunities present themselves. Currently at ~$1.3m or 1.8% of sales, management has a target of 10% of sales within 3-years. This is a gross margin opportunity that could add ~$0.3m to EBITDA on the current sales base by our estimates;
- The BSA (Bisley Workwear) JV in the UK is testament to SGI's model and vision to secure such a partner, and the early signs are encouraging with ~40 stores already stocking and >60 expected to be stocking by Q120. We expect more JV's while the BSA platform could be used to introduce complementary brands/categories to the UK;
- Despite all the near-term earnings distortions, SGI is attractively priced relative to small cap "distribution" peers across a range of measures, trading at the lowest EV/sales and PER multiple.

The above initiatives are supported by a strong board and management team that was deliberately put in-place early to manage growth ambitions and requirements.

DCF Valuation at $0.37/share (market capitalisation of $35m)

We have considered the following valuation methods:

- Discounted cash flow
- Peer EV/EBITDA, PER and EV/Sales multiples

- Expected cash flow profile implicit in the current share price

Our base case DCF is $0.37/share and reflects a CAGR in free cashflows to FY28f of 8.4%, which in our view is highly conservative given the company's growth plans and the industry outlook.

A $0.37/share price would represent 10.5x our FY21 EPS forecasts, which are free of "one-offs" and has the newly established BSA JV breakeven. On an EV/sales basis it would imply 47% of FY18 pro-forma revenue, above current loss-making peers but still well below profitable but larger peers Legend Corporations (ASX:LGD) (under takeover) and Paragon Care (ASX:PGC).

Our reverse DCF analysis suggests the current share price is factoring in a 10-year CAGR in free cashflows of negative 10.7%.

The origins of Stealth Global

Stealth Global was formed in 2014 to consolidate and supply consumables to Capital Drilling (CAPD:LON) across its operations in Africa. Capital Drilling at the time had an average fleet size of 96 rigs, 50% rig utilisation, revenue of US$98m and a gross margin of 33.5%.

The agreement was an opportunity for Stealth to establish a footprint in the industry and across the African region, and for Capital to improve supply chain efficiencies and reduce costs.

Fast forward 5-years and Stealth has built a profitable business by using the scale and experience from Capital in Africa to grow and diversify its business, while Capital has reduced its suppliers of consumables by ~74% and achieved significant operational savings. Using Capital's GP% as a guide, this metric improved to 40.8% in FY18, up from the 33.5% reported in FY14.

Stealth had an opportunity for a "step-change" in scale when acquiring the Heatleys Distribution business based in Western Australia, a business founded in 1987 with pre-existing supplier and customer relationships.

An IPO was selected as the most appropriate funding model and in September 2018 Stealth Global offered 62.5m shares at $0.20/share ($12.5m) to acquire the operations of Heatleys ($9.0m) and for additional working capital. The all-in acquisition multiple was ~3.6x EBITDA.

The Stealth Global business model

SGI is a business to business (B2B) distributor of both branded and proprietary consumable brands across a wide range of industrial & safety products. This model requires the holding of stock for customers, a physical infrastructure that supports customer sales, human support in the form of sales and technical reps, a sophisticated supply chain with systems that communicate with clients and catalogues providing product information for clients. This is very different to a procurement house which essentially operates as a middleman, holding little stock and adding a small margin to generally ad-hoc purchases, offering little ability to build relationships and add real value.

Where possible Stealth seeks to differentiate its offering by establishing preferred and/or exclusive sales arrangements with suppliers and/or customers, further strengthening the partnership/relationship.

The relationship/arrangement with Capital Drilling in Africa is a good example of preferred sales to customers, with SGI supplying most of the consumables used by the group across Africa in a "capital light" model, which has averaged 14%-18% of total Capital Drilling GOGS.

On the exclusive sales side the recently established Joint Venture with Bisley Workwear and supply into the Troy group in the UK is a good example of taking an existing product, tailoring it for a new market and entering with a strong retail/wholesale partner. The JV structure aligns the partners and ensures that if SGI does an exceptional job the business will not be taken away from them without adequate compensation.

Domestically, service levels are seen as a key differentiator, with Heatleys priding itself on returning a quote within 5-6 hours and delivery within 7-10 days.

The volume benefits and relationships from such partnerships also helps strengthen domestic buying power in the traditional business, allowing the group to better compete with incumbents such as Wesfarmers Industrial & Safety.

Greater scale and market understanding also allows the group to purse private labels where there is a perceived void in the market. Private label sales as a percentage of total sales is currently ~1.8%, with the group having a target of 10% within 3-years, offering a 200-300bps gross margin uplift on branded sales. We estimate this represents a ~$0.3m EBITDA opportunity over 3-years.

The other key plank of the group's strategy is to establish a cost-effective Australian East Coast presence in order to bid on national procurement contracts. Presently Heatleys only has operations in Western Australia and South Australia, limiting its ability to bid on national contracts. Companies such as BHP often have a local sourcing requirement where a certain percentage of supply to a mine site must come from the same state. As we discuss later, ISG is a perfect cost-effective entry point.

Stealth Global sales breakdown

SGI has a good spread of sales across product mix, regions and customer size, as the following table highlights.

Exhibit 1: FY19 Pro-forma sales breakdown

By Product	%	By Region	%	By Customer size	%
Industrial	60	Australia	71	Large	55
Safety	28	Africa	24	Medium	30
Workplace	10	UK	5	Small	15
Healthcare	2				

Sources: Company financials, 2018 Prospectus

Recent operating performance

The company released its 1H19 results on February 28, which contained both statutory (Heatleys ownership for the 3-months to December) and Pro-forma numbers (as if Heatleys had been owned for the entire period with no IPO costs).

On pro-forma basis the numbers were said to be on-track or ahead of prospectus forecasts despite representing ~30% of the FY19 EBIT forecast ($1.0m of $3.4m or a 30/70 split). It should be noted the prior year pro-forma half year EBIT split was (35/65). Organic sales growth in 1H19 was said to be +13%, with Australia +18% and Africa down 4%. Group EBITDA growth was +8%.

The table below highlights the 1H19 result against the pro-forma 1H18 base, and the implied 2H19 result required to achieve original prospectus forecasts, all else equal. Key observations include:

- Sales growth was forecast to accelerate from ~13% in 1H to ~20% in 2H on the back of new contract wins;
- Similar gross margin improvements (in bps) in the 2H to the 1H (~60bps);
- While the absolute cost base is lower in 2H, forecast growth on the PCP is similar to 1H19 (+16%).

Exhibit 2: 1H19 actual results and implied 2H19 results to achieve original prospectus

Variable	1H18	1H19	% Chg	2H18	2H19F	% Chg
Revenue	32.00	36.00	13%	33.90	40.70	20%
COGS	22.78	25.40	12%	26.52	31.60	19%
GP	9.22	10.60	15%	7.38	9.10	23%
GP%	28.8%	29.4%	0.63%	21.8%	22.4%	0.59%
Costs	8.20	9.50	16%	5.70	6.60	16%
EBITDA	1.02	1.10	8%	1.68	2.50	48%
EBIT	0.93	1.00	8%	1.60	2.60	63%

Source: Company financials and RaaS Analysis

Growth initiatives post 1H19

Since the 1H19 half year end Stealth has continued with its growth drive with two key initiatives:

- The creation of a JV with brand owner Bisley Workwear with exclusive distribution through independent buying group Troy and United Tooling Solutions (UTS);
- The acquisition of the Industrial Supply Group (ISG) for $1m cash;

Bisley UK JV

On 21 March 2019 Stealth announced the establishment of a Joint Venture agreement in the UK between itself and Australian based Bisley Workwear – BSA Brands. The JV has appointed exclusive distributors in the form of Troy UK and United Tooling Solution (UTS) to distribute the product across its ~420 trade store network.

The JV will be an integrated manufacturer to customer distribution model and develop product customised to the UK market, including a cotton-based product unique to the UK market.

Troy is the UK's largest independent buying group with 300 members representing ~400 trade retail outlets, with annual revenue of GBP155m. UTS has eight trade store branches across southern UK with a tier-1 Amazon UK ranking.

Financially the deal involves:

- The transfer of sales from SGI to the JV that were originally incorporated into original IPO forecasts ($2.8m was forecast, but the structure change will result in a lower number for FY19);
- The contribution of $1.5m by both parties ($0.75m each) over 2-years to build sales and brand awareness, which will include a deployment team, advertising and the like.
- Expectations of a positive ROI in the medium-term.

As Stealth is responsible for the operational management of BSA, it is planning to consolidate BSA earnings and recognise a non-controlling interest. This is how we have modelled the company.

We have assumed a ramp-up of stores stocking the Bisley range over the next 5-years, with an average spend per store assumed at a 35% gross margin. Comments from Stealth with regard to initial penetration rates are encouraging and in-line with our forecasts, with 44 of the 48 retail trade outlets to attend the launch placing initial orders.

Initial costs are expected to outweigh gross profit through sales and marketing efforts, with Stealth spending ~$0.82m up until June 2019. We forecast such spend to stabilise post 1H20 as the brand gains traction and repeat orders are received.

Exhibit 3: BSA store display kit

Source: Company presentation

ISG Acquisition

On 17 April 2019 Stealth announced the acquisition of Industrial Supply Group (ISG) for around $1m cash effective 1 May 2019. ISG is a coalition of major independent industrial supply companies, all privately owned, service orientated, hands on businesses operating in non-conflicting territories across Australia. Heatleys has been a member of the coalition for more than 10-years.

ISG historically earned a fee on the trading value of invoices produced between the individual members and suppliers. It is expected ISG under SGI will undertake the commercial invoicing of customers going forward, offering an uplift in revenue and earnings, together with the support to expand the existing business and win new business, all with limited HR investment as each owner/operator is responsible for this.

Key financial implications include:

- $1m cash outlay over 2-years, paid in three instalments;
- Forecast FY19 revenue of $1.3m and EBIT $0.2m (implied acquisition multiple of 5x);
- ISG targeting revenue of $2m and EBIT of $0.3m in FY20.
- Transaction costs will be taken above the line in FY19.

ISG represents a "capital light" entry into the Australian East Coast for SGI, utilising the established ISG member relationships and locations to better access and service national customers.

Impact to Prospectus FY19 forecasts

The two initiatives above have required adjustments to prospectus forecast on two fronts:

- The sales and gross profit assumptions associated with the Bisley Workwear sales
- The treatment of start-up and transaction costs through the P&L.

In the original SGI IPO forecast, Bisley's entry into the UK was forecast to generate $2.8m in revenue at a GP% of ~35%. The subsequent timing of the Bisley product launch into the UK under the BSA JV was later than IPO expectations, resulting in a launch/revenue delay of ~2-months/A$1.8m.

In addition to the launch delay both partners have invested heavily in the establishment of a launch team, point of sale, marketing and events which SGI estimates to be around A$0.82m in FY19. ISG acquisition costs of ~$0.2m will also be taken above the line.

The table below reconciles original prospectus forecasts and the changes as a result of recent initiatives.

Exhibit 4: FY19 Stealth Global Prospectus adjustments

Line item	FY19 ($m)	Comment
Prospectus EBIT forecast	3.4	Prospectus in September 2018
Less Bisley UK delays	0.6	$1.8m sales at an estimated GP% of 35%
Less Bisley start-up/ISG costs	1.0	~$0.8m BSA, ~$0.2m ISG
Revised EBIT forecast	1.8	Revised guidance as at April 17 2019

Source: Company financials and RaaS estimates

Industry growth drivers

Macro

The industrial supply, safety and workplace markets sell consumables to a wide range of major industries including:

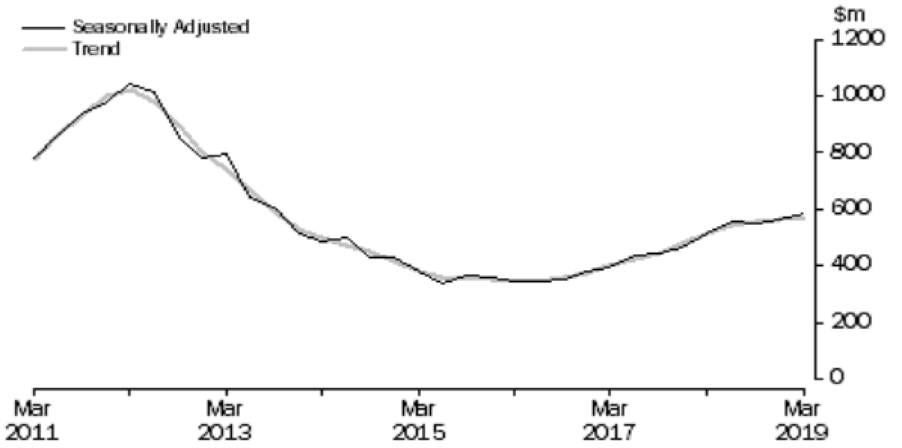
- Resources
- Transport
- Infrastructure
- Engineering
- Manufacturing
- Construction
- General trade.

The following charts provide a snapshot of the current state in some of Stealth's key markets.

While SGI is more exposed to drilling activity in Africa, mineral exploration activity in Australia provides a reasonable proxy for conditions in the resources industry.

Following a prolonged decline in exploration since the GFC, exploration growth has returned from December 2016 and has been modestly improving since.

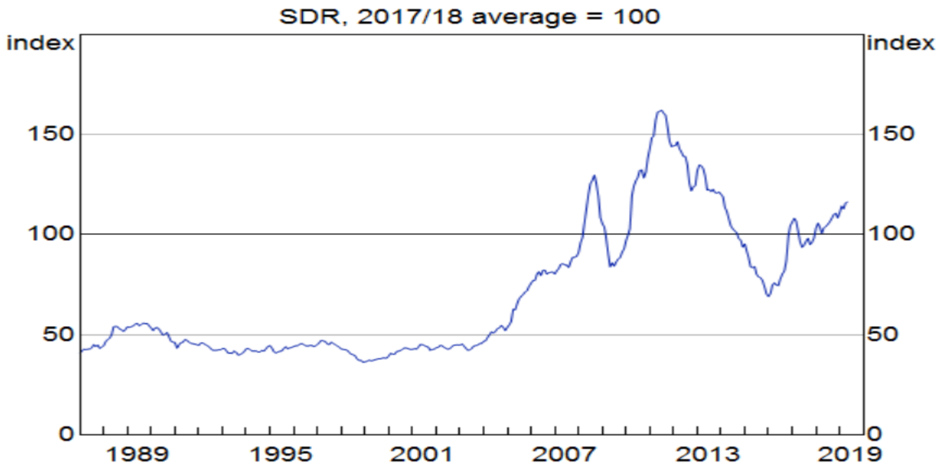
Exhibit 5: Australian Mineral Exploration Spend – seasonally adjusted & trend



Source: ABS catalogue 8412

The level of commodity prices is also a key driver of resource activity for both production and exploration. Following a prolonged downturn in commodity prices post the GFC prices have been steadily improving since mid-2015, encouraging exploration and production levels.

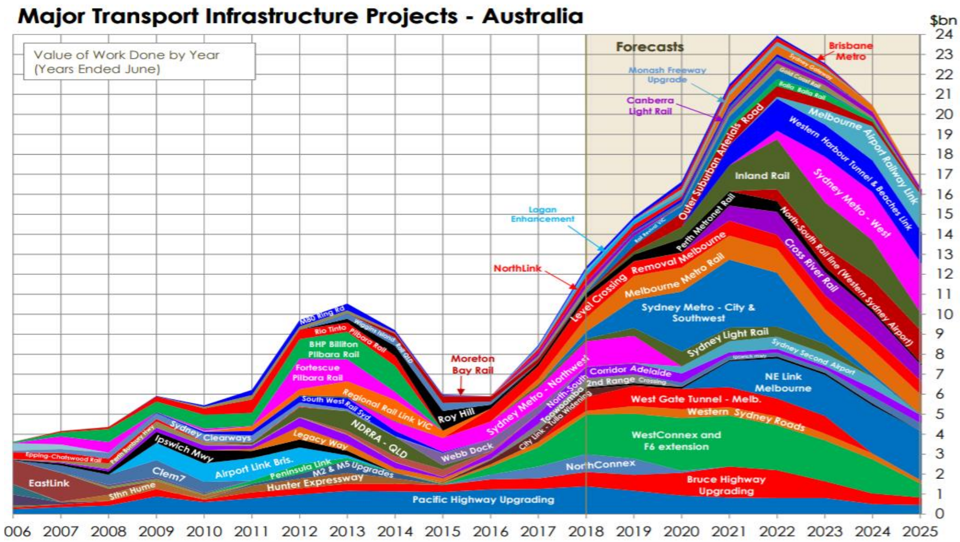
Exhibit 6: RBA Commodity price index



Source: RBA 3 June 2019 (to May 2019)

Infrastructure spend has been a focus for both state and federal governments in response to growing congestion in major capital cities. The chart from Cimic below highlights the magnitude of major transport infrastructure projects being undertaken in Australia out to 2025, with spend expected to peak at A$24bn in 2022 against a spend of ~A$12bn in 2019.

Exhibit 7: Major Transport Infrastructure Projects to 2025



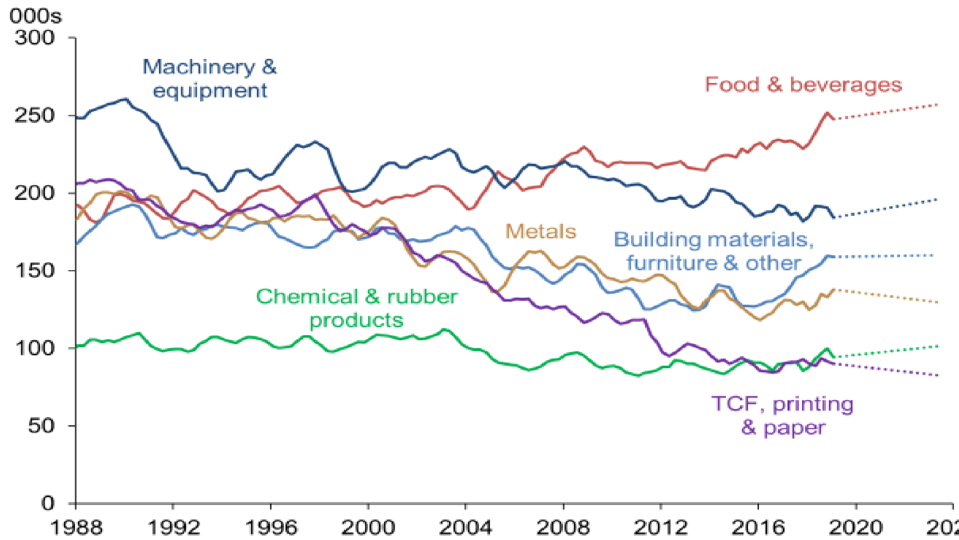
Source: Cimic 1H19 result presentation

The Department of Jobs & Small Business expects the long-term decline in Australian manufacturing to abate over the 5-years to May 2023 driven by a number of factors including:

- A lower and therefore more competitive A$
- An increased focus on value-add products/components
- The end of job shedding associated with the car industry
- Increased government spending on defence related industries.

The chart below indicates growth is expected in four of the six key employment categories, including the three largest industries by employment.

Exhibit 8: Manufacturing employment & projected employment trend – May 2019



Source: Australian Industry Group – Australian Manufacturing in 2019, local & global opportunities

RaaS Research as a Service

Micro

On the micro/customer front, Stealth/Heatleys in Australia source significant business through the likes of Downer (ASX:DOW), Monadelphous (ASX:MND), AGC (part of the AusGroup), Cape Group and Aust Minerals as a contractor to various projects.

Sales reps stay very close to these customers in order to be considered for tendering activity.

It is worth tracking the order books and work in hand of these companies for a general guide to the prospects of SGI, albeit currently confined to the West Coast (pre-ISG).

Some key outlook statements from the listed operators include:

Downer. Work in-hand rose to $43.5bn at December 2018, up from $42bn in June-18 and $39.2bn at December -17.

Monadelphous observed a "high level of tendering activity for an increasingly large number of major resource construction projects".

Key Industry Competitors

The addressable market for SGI is not easy to define given the broad nature of industries supplied and products consumed by these industries. It is somewhat similar to the "hardware" market which has continued to evolve with category expansion lead by big-box providers such as Bunnings.

Wesfarmers Industrial & Safety is by far the largest player in Australia with sales estimated at A$1.76bn in FY19, 25x the forecast revenue of Stealth Global.

We would make the following observations regarding financial metrics of WESI&S and implications for SGI:

- WESI&S sales have been weak relative to SGI over the last 3-years, with flat CAGR growth against 11% for SGI;
- Poor customer service and legacy systems/DC network have been a common denominator in management commentary over recent results presentations, the opposite of Stealth;
- The divisional ROIC of ~7.0% for WESI&S in FY19 is well below WES targets and other WES divisions, offering the possibility of divestment as was the case with the Coles Supermarkets division. This could lead to poor morale within the business and offer further market share opportunities for SGI.
- Gross margin and key working capital metrics are not available.

Exhibit 9: WESI&S divisional earnings history

Variable	2015	2016	2017	2018	2019F*
Sales	1,772.0	1,844.0	1,776.0	1,750.0	1,764.0
		4.1%	-3.7%	-1.5%	0.8%
EBITDA	108.0	105.0	158.0	159.0	139.8
D&A	38.0	42.0	43.0	41.0	41.0
EBIT	70.0	63.0	115.0	118.0	98.8
EBIT margin	4.0%	3.4%	6.5%	6.7%	5.6%
ROIC	5.5%	4.7%	8.4%	8.4%	7.0%
Invested Capital	1,271	1,338	1,363	1,394	1,420

Sources: Company financials *Annualised 1H19 sales growth rate

Privately owned ATOM Supply Group Pty Ltd is a closer competitor to Stealth, growth strongly in recent years with turnover of ~$150m in Australia.

The business has a 40-year history in Australia and prides itself on service and multiple routes to market. Service levels are boosted by a family centric franchise structure.

The group has 12 warehouse locations across 5 states/territories comprising Western Australia (4), Queensland (3), Victoria (2), NSW (2) and Northern Territory (1).

ATOM like Blackwoods (WES) and ISG prides itself on its extensive product catalogue.

Exhibit 10: ATOM catalogue promotion

Source: ATOM website

RaaS's SGI Earnings Estimates

Sales

Key sales considerations and assumptions are listed below:

- Our African sales assumptions are linked to a % of Capital Drillings COGS. Having spiked in FY18 & FY19 at ~18.5% of total COGS we forecast a return to FY17 levels of ~15%, which reduces forecast sales in FY20.
- We have assumed a total near-term sales growth rate of 10% per annum for the Australian business, slightly below recent CAGR levels but justified by solid market conditions, market share gains from incumbents and the establishment of an Australian East Coast presence via the ISG acquisition. Within this growth rate we have private label growing well above branded as the group targets 10% of total sales for private label by FY22;
- No material assumptions for acquisitions or "whole of site" procurement contracts have been made despite a high probability of this occurring.

Gross Profit

Key gross profit considerations and assumptions are listed below:

- The consolidation of BSA sales at a GP% of ~35% should boost group GP% overtime as the JV grows. As a general comment SGI is looking to allocate resources to higher GP% business;
- Capital Drilling has much lower gross margins than the group average as evidenced by the Stealth results pre-Heatleys. The mix implications of lower Capital Drilling sales will result in higher group gross margins, all else equal.
- Underlying branded margins are assumed to increase 20bps per annum as the groups growing scale offering purchasing benefits;
- We have assumed Private Label sales have a 300bps margin benefit over branded product.

Operating Costs

Key operating cost considerations and assumptions are listed below:

- There is limited cost information on a line item basis, and very little by half year. We have used references to % of sales for employees, occupancy and other costs in the prospectus as the starting point;
- We have treated "start-up" and transition costs "above the line" as is company policy, but will highlight were relevant/possible;
- We cross check line-item expenses with divisional expense assumptions across Australia, Africa and BSA.

Joint Venture(s)

We have chosen to consolidate the contribution from the BSA JV into SGI accounts.

Given the early stages of start-up and limited information available we have selected a penetration into the exclusive buying groups store network (Troy UK) as an initial guide to medium-term sales and earnings potential. Current assumptions are in-line with the early customer uptake.

The summary of our earnings forecasts for SGI are tabled below.

We would note that with a low earnings base and a number of moving parts it does not take much to move the dial on earnings either way, particularly on the cost base as we have seen in recent months. As a result, we would encourage investors to monitor sales and gross profit numbers as a guide to SGI's true progress.

Exhibit 11: RaaS's SGI divisional earnings forecasts

	2018A*	2019F*	2020F	2021F	2022F
Sales	65.9	74.0	79.1	89.8	99.4
Australia	46.5	54.2	60.3	66.3	71.6
Africa	19.4	18.8	15.3	16.4	17.2
BSA	0.0	1.0	3.5	7.1	10.6
Gross Profit	16.6	18.2	20.3	23.6	26.7
GP%	25.2%	24.7%	25.7%	26.3%	26.9%
Operating Costs	13.9	16.3	17.7	18.1	18.8
EBIT	2.5	1.7	2.3	5.0	7.2
Minority Interest	0.0	-0.4	-0.5	0.0	0.3
NPAT	1.6	1.5	1.7	3.3	4.6

Source: RaaS estimates *Pro-forma

Other Financial Commentary

Balance sheet

Key points to note with regards to the SGI balance sheet include:

- **Relatively low working capital/sales**. Ranging between 7%-10% of sales, SGI's working capital to sales is much lower than distribution peers due to their capital light model, particularly in Africa and BSA with regards to inventory. ISG is also expected to be capital light.
- **Forecast net cash position**. Despite recent acquisitions we have forecast SGI to end FY19 with a net cash position of ~$0.5m, providing further funding options for bolt-on acquisitions or new JV's.
- **Goodwill on the balance sheet** of ~$7m relates to the acquisition of Heatleys in September 2018.

Cash Flow

Key points to note with regards to the SGI cash flow include:

- **Low capex model**. Capex has averaged <1% of sales over the last two years, and we expect this trend to continue outside of establishing a larger physical presence on the East Coast.
- **Modest working capital requirements**. Given the low working capital to sales, the working capital required for grow is relatively modest.

Dividends

While the scale of future investment in existing and/or new JV's or acquisitions will ultimately determine dividend payments, we have assumed dividend payments begin in 2H20 with a 50% pay out policy.

The company does not currently have a dividend policy.

Peer Comparison

While the Industrial & Safety Division of Wesfarmers (ASX: WES) is the most comparable domestic listed business model to Stealth Global, its sheer size and limited valuation visibility within Wesfarmers make comparisons of little relevance, in our view.

In the unlisted world, ATOM Supply Group Pty Ltd is the most comparable peer, but again financial metrics are undisclosed making valuation comparisons difficult.

Globally the likes of W.W Grainger (GWW.NYS) and HD Supply (HDS.NAS) could be considered peers, but again with market caps of ~US$17bn and US$8bn respectively they are simply not comparable to a micro-cap/evolving Australian listed company.

For listed comparables we have chosen distribution businesses that are small cap in nature, have gross margins in the 30%-40% range and deal with much larger customers as a rule. They include:

Legend Corporation (ASX: LGD), supplier of products to the electrical, power, infrastructure and gas & plumbing markets that prides itself on service and being in-stock and delivering on-time. Recently received a takeover offer from Adamantem Capital for $0.365/share ($80m mkt cap, $100m EV).

Paragon Care Limited (ASX:PGC), is a supplier of a wide range of healthcare equipment and consumables to hospitals and aged care facilities. The group has grown by acquisition and is currently consolidating this position.

Funtastic (ASX:FUN), a toy, plush, tech and confectionery distributor predominantly to Discount Department Stores (DDS's) and Speciality stores across Australia. The group also has some own brands which are sold through similar channels but has not turned a profit for 5-years and undertake dilutive capital raisings in order to repay debt in conjunction with debt forgiveness.

Coventry Group (ASX:CYG), supplies a range of fastening systems, cabinet hardware systems, fluid hydraulics, lubrications, refuelling systems and other products across a range of channels. The group has three distinct businesses, Cooper Fluid Systems, Nubco and Trade Distribution, and is in "turnaround" mode.

Supply Networks (ASX:SNL) operates under the Multispares brand, and supplies truck and bus parts across Australia (~90% of revenue) and New Zealand, with a focus on "quality" components and service.

The table below summarises some key financial comparisons over FY18 and FY19 year using consensus and/or guidance where available.

Exhibit 12: Peer financial comparison

Company Name	Ticker	Share price (cps)	Mkt Cap ($m)	FY19 sales ($m)	FY19 NPAT ($m)	Net debt ($m)	FY19 PER (x)	FY18 GP%	FY18 WC/sales	Mkt Cap/sales
Supply Networks	SNL	3.550	145	120	8.4	5	17.3	41.7%	27%	125%
Paragon Healthcare	PGC	0.440	148	240	12.6	60	11.8	40.2%	31%	87%
Legend Corporation	LGD	0.375	81	114	7.3	21	11.1	42.9%	34%	90%
Coventry Group	CYG	0.915	82	230	1.3	7	nm	36.8%	27%	39%
Funtastic	FUN	0.030	7	35	nm	2	nm	36.0%	11%	26%
Stealth Global	SGI	0.090	9	74	1.5	(0.5)	5.6	24.7%	8%	11%

Sources: Company financials, Thomson Reuters, Stockopedia *Prices at 5th July 2019

Relative to Stealth we would note:

- While not necessarily an industry benchmark metric, the SGI enterprise value to sales ratio is 60% below their nearest peer (FUN) and 90% below the nearest profitable peer (LGD) ;
- SGI's Pro-forma FY18 GP% is well below peers, but has upside from private label initiatives, scale benefits, product mix and the establishment of BSA;

- Perhaps a counter to the lower GP% is a much lower working capital to sales impost, with SGI at 7% against 30-35% for profitable peers;
- On a reported basis the forecast SGI PER multiple for FY19 is at a 50% discount to profitable peers. On an adjusted basis we estimate the PER is closer to 4.6x, a 60% discount;
- SGI is the only business with a net cash position as at December 2018.

DCF valuation

We are of the view that the discounted cashflow methodology is the most appropriate methodology for valuing early stage companies despite the inherent risk in forecasting the timing and magnitude of future growth. Our DCF valuation for SGI is $0.37/share, with key assumptions listed in exhibit 13 below. Our forecasts factor in a CAGR in free cashflows to 2028 of 8.4%, which in our view is highly conservative given the industry growth drivers and SGI's ambitions.

Exhibit 13: Base Case DCF valuation

Parameters	Outcome
Discount Rate / WACC	12.6%
Beta	1.5x
Terminal growth rate assumption	2.0%
Sum of PV	17.6
PV of terminal Value	16.1
PV of Enterprise	33.8
Debt (Cash)	(1.3)
Net Value – Shareholder	35.0
No of shares on issue*	94.9
NPV	0.37

Source: RaaS estimates

Reverse DCF

A reverse DCF can be a useful cross check to demonstrate what growth rate the market is implying in the current share price. Using the same parameters as our Base Case DCF, and utilising our estimate for FY19 free cashflow, the current price implies a 10-year CAGR in free cashflows of negative 10.7%.

Exhibit 14: Reverse DCF

Parameters	Outcome
Discount Rate / WACC	12.6%
Beta	1.5x
Terminal growth rate assumption	2.0%
Sum of PV	5.8
PV of terminal Value	1.5
PV of Enterprise	**7.2**
Debt (Cash)	(1.3)
Net Value – Shareholder	8.5
No of shares on issue	94.9
NPV	0.09

Source: RaaS estimates

Sensitivity analysis

The table below highlights what we see as the key variables/assumptions in our DCF analysis. The discount rate (WACC) and domestic gross margin assumption (driven by private label and scale) are the key sensitivities to our valuation.

Exhibit 15: SGI DCF sensitivities

Variable	Current	+/-	Change (cps)	Change (%)	Comments
WACC	12.6%	1.0%	0.05	14%	Key sensitivity
Domestic GP% by FY24	30.2%	1.0%	0.04	11%	Key assumption
MT Domestic growth rate	10.0%	1.0%	0.02	5%	Australian operations
% Troy stores by FY24	35.0%	5.0%	0.01	2%	Not the only BSA assump
Capital Drilling % COGS	15.0%	1.0%	0.00	1%	Low margin limits impact

Source: RaaS estimates

SWOT analysis

In our view the strengths and opportunities for Stealth Global outweigh the weaknesses and threats.

Exhibit 16: Strengths, Weaknesses, Opportunities, Threats

Strengths	Opportunities
Nimble player without legacy systems or DC infrastructure to hinder growth/operational structure	A small player in a big pond that can chip away at market share without being noticed for some time
Capital drilling relationship and cross shareholding	Replicate the Capital Drilling model with another large Mining or Mining Service player in Africa
Strong institutional shareholder support for a micro-cap company	Use growing scale to develop Private Label products, benefiting both sales and gross margin
Highly experienced board from both a listed company and growth business perspective	Consolidate the fragmented smaller end of the market
Growing international presence, unlike Australian competitors	Establish a presence on the East Coast of Australia
	Relationship with David Gazal through Bisley Workwear likely to lead to further JV opportunities
Weaknesses	**Threats**
Small player in a fragmented marketplace, with Australia dominated by a large player (WES)	Lose the Capital Drilling business post November 2020, which currently represents ~25% of revenue
Access to funding given a relatively recent listing and current low earnings multiples	Integration risk of ISG, together with any further acquisitions undertaken
Limited track record as a listed company	Largest supplier Mincon goes direct to client

Source: RaaS analysis

Board and management

Directors

Mr Christopher Wharton, Non-Executive Chairman, is the former Chief Executive Officer of Seven West Media WA, retiring from full time work in April 2017. He was responsible for all Seven West Media assets in Western Australia, which included The West Australian, The Sunday Times, 21 West Regional mastheads, its online properties thewest.com.au and Perthnow, WA Publishers, Redwave Media (non-regional radio licences) and Channel Seven Perth.

Mr Michael Arnold, Managing Director, was previously Executive Director/Chief Operating Officer of ADG Global Supply (previously listed on the ASX) until June 2013, where he was responsible for developing business strategy, global infrastructure, business development, operational capabilities and leading growth. Prior to this he was Managing Director and Chief Executive Officer of Lakewood Logistics for nine-years (a JV company between Australia Post and Mr Arnold). Lakewood was established from start-up to be become one of Western Australia's largest 3rd party logistics companies.

Mr Giovanni (John) Groppoli, Non-Executive Director, is currently a non-executive director of Automotive Holdings Group Ltd (ASX:AHG) and a principal at Peppermint Capital (a boutique corporate advisory firm based in Perth). He was a Partner of national law firm Deacons (now Norton Rose Fulbright) from 1987 to 2004 where he specialised in franchising, mergers and acquisitions and corporate governance. He was managing partner of the Perth office of Deacons from 1998 to 2002.

Mr Peter Unsworth, Non-Executive Director, is a former chartered accountant and corporate finance specialist with extensive experience as a public and private company director, having served on the board of Gold Corporation (operator of Western Australian Government owned The Perth Mint) as a director and then chairman from 1996 to 2008. He has previously been a director of several listed companies including Westintech Innovation Corporation, Perilya Mines Limited and National 1 Limited.

Management

Mr Luke Cruskall, Chief Operating Officer, has nearly 20 years of management across public and private sector organisations including in national, general manager, chief executive officer and board level roles. He is a specialist in industrial, mining and construction products, distribution, manufacturing, and consumer sectors both domestically and internationally. Most recently Mr Cruskall held the role of chief executive officer of a privately held Australian manufacturing and product distribution group. He is a director of BSA Brands UK joint venture with Bisley and also Industrial Supply Group (ISG).

Mr Brendan Rossiter, Chief Financial Officer, has over 15-years' experience in senior finance roles. His industry experience is broad, ranging mining and mining services, retail, wholesale, fast-moving consumer goods and agriculture, telecommunications and research and development. Mr Rossiter's previous positions held were Chief Financial Officer for Powertech Pty Ltd and Chief Financial Officer and Company Secretary for Retravision (WA) Ltd.

Mr Sam Barbaro, Managing Director – Heatleys Sales has been with the Heatleys business for 30 years, working his way from store person to his current position. Mr Barbaro has an intimate understanding of the industrial and safety consumables supply industry and has worked in all aspects of the business, which has given him a vast understanding of the company and the industry in which it operates. He has been an integral part of a number of acquisitions and integration acquired by Heatley Sales and also the sale to AMP Capital in 2005.

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Exhibit 17: Financial Year Financial Summary

Stealth Global (SGI.AX)					
Profit and Loss (A$m)					
Y/E 30 June	**FY18A**	**FY19F**	**FY20F**	**FY21F**	**FY22F**
Revenue	65.9	74.0	79.1	89.8	99.4
Gross profit	16.6	18.2	20.3	23.6	26.7
GP margin %	25.2%	24.7%	25.7%	26.3%	26.9%
EBITDA	2.7	1.9	2.6	5.2	7.5
Depn	(0.2)	(0.2)	(0.2)	(0.3)	(0.3)
Amort	0.0	0.0	0.0	0.0	0.0
EBIT	2.5	1.7	2.3	5.0	7.2
Interest	(0.2)	(0.1)	(0.3)	(0.3)	(0.3)
Tax	(0.7)	(0.5)	(0.8)	(1.4)	(2.0)
Minorities	0.0	0.4	0.5	0.0	(0.3)
Equity accounted assoc	0.0	0.0	0.0	0.0	0.0
NPAT pre significant items	1.6	1.5	1.7	3.3	4.6
Significant items	0.0	0.0	0.0	0.0	0.0
NPAT (reported)	**1.6**	**1.5**	**1.7**	**3.3**	**4.6**
Cash flow (A$m)					
Y/E 30 June	**FY18A**	**FY19F**	**FY20F**	**FY21F**	**FY22F**
EBITDA	2.7	1.9	2.6	5.2	7.5
Interest	(0.2)	(0.1)	(0.3)	(0.3)	(0.3)
Tax	(0.5)	(0.6)	(0.6)	(1.1)	(1.7)
Working capital changes	(0.8)	(0.8)	(0.4)	(0.8)	(0.7)
Operating cash flow	1.3	0.4	1.2	3.0	4.8
Mtce capex	(0.2)	(0.3)	(0.4)	(0.4)	(0.5)
Free cash flow	1.1	0.1	0.8	2.6	4.3
Growth capex	0.0	0.0	0.0	0.0	0.0
Acquisitions/Disposals	0.0	(0.5)	(0.5)	0.0	0.0
Other	0.0	(0.6)	0.0	0.0	0.0
Cash flow pre financing	1.1	(1.0)	0.3	2.6	4.3
Equity	0.0	0.0	0.0	0.0	0.0
Debt	0.0	(1.0)	0.0	0.0	0.0
Net Dividends paid	(1.2)	0.0	0.0	(1.9)	(2.3)
Net cash flow for year	(0.1)	(2.0)	0.3	0.7	2.0
Balance sheet (A$m)					
Y/E 30 June	**FY18A**	**FY19F**	**FY20F**	**FY21F**	**FY22F**
Cash	3.9	2.4	3.2	3.9	5.6
Accounts receivable	11.5	12.9	13.8	15.7	17.4
Inventory	4.6	5.4	5.8	6.6	7.3
Other current assets	0.4	0.5	0.4	0.0	0.0
Total current assets	*20.5*	*21.3*	*23.2*	*26.2*	*30.3*
PPE	0.5	0.5	0.7	0.9	1.0
Goodwill	6.6	7.1	7.6	7.6	7.6
Investments	0.1	0.7	0.7	0.7	0.7
Deferred tax asset	1.2	1.2	1.2	1.2	1.2
Other non current assets	0.0	0.0	0.0	0.0	0.0
Total non current assets	*8.3*	*9.5*	*10.1*	*10.3*	*10.5*
Total Assets	28.8	30.7	33.3	36.5	40.8
Accounts payable	11.4	12.8	13.6	15.5	17.1
Short term debt	2.9	1.9	1.9	1.9	1.9
Tax payable	0.3	0.3	0.3	0.3	0.3
Other	1.1	1.1	1.1	1.1	1.1
Total current liabilities	*15.7*	*16.1*	*16.9*	*18.8*	*20.5*
Long term debt	0.1	0.1	0.1	0.1	0.1
Other non current liabs	0.2	0.2	0.2	0.2	0.5
Total long term liabilities	*0.4*	*0.3*	*0.3*	*0.3*	*0.6*
Total Liabilities	16.0	16.4	17.3	19.1	21.0
Net Assets	**12.8**	**14.3**	**16.0**	**17.4**	**19.7**
Share capital	13.2	13.2	13.2	13.2	13.2
Accumulated profits/losses	(0.6)	0.9	2.6	4.0	6.4
Reserves	0.2	0.2	0.2	0.2	0.2
Minorities	0.0	0.0	0.0	0.0	0.0
Total Shareholder funds	**12.8**	**14.3**	**16.0**	**17.4**	**19.7**

Share price (5 July 2019)					A$	0.09
Interim (A$m)	**H118A**	**H218A**	**H119**	**H219F**	**H120F**	**H220F**
Revenue	32.0	33.9	36.0	38.0	38.5	40.5
EBITDA	1.0	1.7	0.9	0.8	1.4	1.3
EBIT	0.9	1.6	0.8	0.7	1.2	1.2
NPAT (normalised)	0.6	1.1	0.6	0.7	0.9	0.9
Minorities	0.0	0.0	0.0	0.0	0.0	0.0
NPAT (reported)	0.6	1.1	0.6	0.7	0.9	0.9
EPS (normalised)	0.006	0.011	0.006	0.007	0.009	0.010
EPS (reported)	0.006	0.011	0.006	0.007	0.009	0.010
Dividend (cps)	0.000	0.000	0.000	0.000	0.000	0.010
Imputation	30.0	30.0	30.0	30.0	30.0	30.0
Operating cash flow	na	na	na	na	na	na
Free Cash flow	na	na	na	na	na	na
Divisionals	**H118A**	**H218A**	**H119F**	**H219F**	**H120F**	**H220F**
Australian Revenue	22.2	24.3	27.0	27.2	29.4	30.8
African Revenue	9.8	9.6	9.0	9.8	7.7	7.6
BSA	0.0	0.0	0.0	1.0	1.5	2.1
Total Revenue	**32.0**	**33.9**	**36.0**	**38.0**	**38.5**	**40.5**
Gross profit	9.2	7.4	10.6	7.5	11.4	8.9
Gross Profit Margin %	28.8%	21.8%	29.4%	19.8%	29.5%	22.0%
Employment	na	na	na	na	na	na
Occupancy	na	na	na	na	na	na
Other costs	na	na	na	na	na	na
Total costs	**8.2**	**5.7**	**9.7**	**6.7**	**10.0**	**7.7**
EBITDA	**1.0**	**1.7**	**0.9**	**0.8**	**1.4**	**1.3**
EBITDA margin %	3.2%	5.0%	2.4%	2.2%	3.5%	3.2%
Margins, Leverage, Returns		**FY18A**	**FY19F**	**FY20F**	**FY21F**	**FY22F**
EBITDA margin %		4.1%	2.6%	3.3%	5.8%	7.5%
EBIT margin %		3.8%	2.3%	3.0%	5.5%	7.2%
NPAT margin (pre significant items)		2.5%	2.1%	2.2%	3.6%	4.6%
Net Debt (Cash)		- 0.96	- 0.42	- 1.23	- 1.94	- 3.66
Net debt/EBITDA (x)	(x)	nm	nm	nm	nm	nm
ND/ND+Equity (%)	(%)	7.0%	2.9%	7.1%	10.0%	15.6%
EBIT interest cover (x)	(x)	7.0%	7.6%	14.1%	6.4%	4.2%
ROA		9.2%	5.8%	7.3%	14.2%	18.5%
ROE		11.7%	11.3%	11.3%	19.6%	24.8%
ROIC		19.5%	22.1%	29.9%	47.5%	55.1%
NTA (per share)		0.07	0.08	0.09	0.10	0.13
Working capital		4.8	5.6	6.0	6.8	7.5
WC/Sales (%)		**7.3%**	**7.6%**	**7.6%**	**7.6%**	**7.6%**
Revenue growth		nm	12.3%	6.9%	13.5%	10.8%
EBIT growth pa		nm	(31.8%)	36.4%	111.7%	44.2%
Pricing		**FY18A**	**FY19F**	**FY20F**	**FY21F**	**FY22F**
No of shares (y/e)	(m)	95	95	95	95	95
Weighted Av Dil Shares	(m)	95	95	95	95	95
EPS Reported	cps	0.02	0.02	0.02	0.03	0.05
EPS Normalised/Diluted	cps	0.02	0.02	0.02	0.03	0.05
EPS growth (norm/dil)		nm	-7%	12%	91%	41%
DPS	cps	0.000	0.000	0.010	0.020	0.028
DPS Growth		n/a	n/a	n/a	100%	40%
Dividend yield		0.0%	0.0%	11.1%	22.2%	31.1%
Dividend imputation		30	30	30	30	30
PE (x)		5.2	5.6	5.0	2.6	1.9
PE market		15.2	15.2	15.2	15.2	15.2
Premium/(discount)			(63.4%)	(67.3%)	(82.8%)	(87.8%)
EV/EBITDA		2.8	3.3	2.3	1.2	0.7
FCF/Share	cps	0.011	(0.006)	0.008	0.028	0.042
Price/FCF share		8.0	(16.0)	10.6	3.3	2.1
Free Cash flow Yield		12.5%	(6.3%)	9.4%	30.6%	46.7%

Source: RaaS Advisory

FINANCIAL SERVICES GUIDE

RaaS Advisory Pty Ltd

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