

SA company's gold-tinged rise up the share market

VALERINA CHANGARATHIL



UNCOVERING GROWTH: Codan chief executive Donald McGurk with landmine detectors at Codan in Mawson Lakes. Picture: STEPHEN LAFFER

IT HAS the makings of a gripping tale of corporate crime and greed, but for Adelaide's publicly listed manufacturer Codan, fighting copycat criminals in China has been a hard slog that is now delivering strong results.

The share price of the Mawson Lakes business is now nearly double what it was a year ago, up from around just under \$3 to \$5.51 yesterday.

With a market capitalisation of just over \$1 billion, more than \$37 million in cash at the end of June and a steady dividend payout, the debt-free company has caught the eye of investors, analysts and fund managers.

Founded in 1959, Codan manufactures rugged electronics solutions – mainly radio communications, metal detectors and tracking solutions – for government, corporate, NGO and other clients.

With 450 employees in Australia, Canada, US, Ireland, USA, Brazil and South Africa, the business is heavily skewed towards exports, which account for 85 per cent of its sales.

At the end of June this year, the company posted a record net profit after tax of \$45.7 million and record revenues of \$270.8 million, paying out a full year dividend of 9c.

But it nearly went all pearshaped in 2011 when Codan started receiving faulty gold detectors – stamped with a Codan logo but with inferior parts the company couldn't recognise – into its service centre.

Chief executive Donald McGurk saw sales and prices of detectors collapse amid a gold rush in Africa.

Codan was forced to slash the price of its gold detectors from around \$4000-\$5000 to around \$2500 to compete. At the end of June 2014, Codan's net profit had collapsed to \$9.2 million.

The problem, discovered through private investigators, was counterfeit products.

A Codan employee's laptop had been hacked into during a business trip to China a couple of years previously.

Codan subsequently found 12 separate companies manufacturing fake Codan gold detectors of "varying quality" but which looked and felt like Minelab gold detectors. Some illegally carried Codan's Minelab trademark

International legal action followed, including jail for the directors of three Chinese manufacturers, after some high-level lobbying in China.

Importantly, it focused the company's attention to protecting its turf through the use of encryption and hacking prevention and other security measures.

While Mr McGurk has previously likened to "playing Whack-A-Mole", the return to record profits and revenues is a good sign.

Unley Morgans private client adviser Tom Boorman has a "hold" recommendation on Codan. The upcoming release of Codan's GPZ 7000 metal detector is an attraction.

"That (it) could find gold approximately 20cm deeper would create a new gold rush for the company as prospectors had virgin ground again," Mr Boorman said. "In recent years the company's struggling Minetec division which provides efficiencies and oversight of the location and activity of personnel on mine sites has finally started to gain genuine traction.

"This could become a driver for the share price in the years ahead as it continues to innovate and release more products in the metal detector space and in their radio communication business.

"With the gold price trading around the \$US1500 mark, the company has had significant tail winds in the metal detector division," he said.

With its current market cap and share price, Codan is trading on 22 times last year's earnings. "The current price the company looks fully valued when taking into account the earnings variability that has occurred in the past 10 years, however it is clear that the company is performing very well, the management and board are highly competent and if profits continue to exceed forecasts this will provide support for the share price.

"The company has openly stated that the sector does move cyclically and that the last few years of sales should be considered as above average profits for the division," Mr Boorman said.

Canaccord Australia's research head Aaron Muller had Codan on its Focus List in July.

"Given the strong performance of the Codan share price recently, we have downgraded our rating to a hold. "It's up 68 per cent since the inclusion in our Focus List in July. We remain positive on the outlook for Codan," Mr Muller said.

"New product development in recent years across its three divisions has helped diversity revenue, improve earnings visibility and inject growth into the overall group. Some of these new products have large addressable markets, which should underpin future growth.

"Codan also generates a large percentage of revenue and profitability from its world leading metal detection products and the gold price strength has likely helped demand.

"We're expecting this to flow through into 1H20, albeit they are cycling a strong period for metal detection sales in 1H19."

Mr Muller said the company's cashed up position with no debt was a positive.

"(It) puts them in a great position to grow the business via acquisition. They should also benefit from a weaker AUD/USD this year compared to last. The key risks are probably the gold price and any fluctuations in its top of the range gold detector, the GPZ7000. Being a high margin product, small changes in volumes can have an impact on earnings."

Investment management firm Ophir Asset Management has invested in Codan.

"Codan is becoming a household name on the ASX. It is a true South Australian success story on the global market," Ophir Asset Management's senior portfolio manager Andrew Mitchell said.

"They have invested heavily in new product development in gold detectors and the coin and treasure detector market and are now reaping the benefits," Mr Mitchell said.

"The company is sitting on a significant heap of cash ready to deploy in technology based acquisitions."