Isentia's drop an overreaction

by Roger Montgomery

Isentia recently caused the market price for its shares to stumble by more than 25%.

Isentia expanded sideways last year buying an online content business called King Content. At that time Isentia told media & marketing website Mumbrella: "For quite some time now, Isentia has been looking at how we can work across owned, earned and paid media. Our clients are already getting a lot of information from us in this space, but they are also asking us to help with their strategy…King Content are the market leader" adding, "we still see a real growing need from major brands to connect with their audiences through content marketing."

The deal, with vendors – to be paid out over a five-years – would total $48 million if all targets are hit.

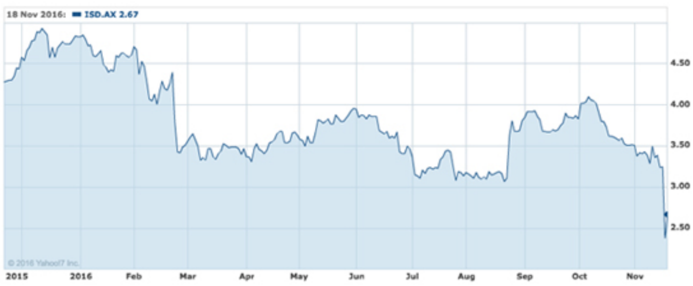
On the 17 of November, Isentia held its AGM and provided a trading update. In short, Content Marketing will report an EBITDA loss of $2 million for 1H17 however management expects a positive contribution for the 2017 financial year after a restructuring. This will result in ISD's Group 1H17 EBITDA to be below the prior corresponding period.

The announcement of the half-year loss of $2 million in the content business triggered a $175 million reduction in the Group's market capitalisation. This seems, at first blush, disproportionately large given the group's Australia and New Zealand Software-as-a-Service (SaaS) and Value Added Services (VAS) amount to 93% of EBITDA for 2016 and are performing in line with management's previous guidance.Nevertheless, prior Group guidance was for revenue and EBITDA growth of between 11-15%, guidance for revenue and EBITDA growth has now been revised lower to high single digits.

The drivers of the downgrade appear temporary, the restructure will include the implementation of a new organisational structure and CEO for King Content as well as merging the ISD & King Content sales teams.

It's worth noting that King Content represents <10% of our valuation for ISD, hence even a permanent impairment of the division's prospects would not be significant. In this context, you can see why we view the 27% decline in Isentia's share price as an overreaction. The primary driver of our valuation is growth in the company's SaaS/VAS divisions. The most recent updated guidance confirms that these business units are operating in line with management's expectations and therefore there is little impact on our valuation/recommendations for ISD.

The current market condition however is to hammer the shares of companies that miss a beat. For value investors, it is often when that which is considered temporary is treated as permanent that opportunities are presented.



Source: Yahoo!7 Finance, 21 November 2016

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