

Result Focus

Osprey Medical Inc. (OSP.ASX)



Thursday, 19 July 2018

Growth rebounds with proof of concept reinforced

Recommendation: Positive

Last price **\$0.20**

Valuation **\$0.48**

TSR

Upside to valuation	141.0%
Dividend yield	0.0%
Expected total SH return	141.0%

OSP.ASX share price history v XJO.ASX

Source: EAP Research, IRESS



Trading Data

Last Price	\$0.20
Valuation	\$0.48
12 month range	\$0.14 - \$0.48
Market Cap	\$68m
Free Float	\$34m (50%)
12 month return (historical)	(58.1%)

Earnings revisions

	FY18	% chg	FY19	% chg
REVENUE (\$m)	3	0.7%	8	0.5%
EBITDA (\$m)	(14)	(2.4%)	(14)	6.2%
Adj. EPS (c)	(4.3)	(2.3%)	(4.3)	6.7%
Val	\$0.48	2.6%		

Unit Growth rebounds across the portfolio

The 2Q18 result beat our revenue and unit sales estimate by +5.7% and +8.6% respectively. Sales growth increased 23.1% with unit sales up 28.3% vs 1Q18. This growth was recorded across the portfolio with San Antonio rebounding back to +33% growth albeit off lower base. Excluding San Antonio which had a soft 1Q18, the rest of OSP sales territories grew at ~+23% which was impressive considering the sales force headcount was flat at 23. Penetration from existing hospitals is clearly growing as further clinical data emerges on the ability for DyeVert Plus to reduce the incidence of Contrast Induced Acute Kidney Injuries (CI-AKI). Recent published data suggests that hospitals using DyeVert Plus in Texas and West Virginia were successful in reducing the rate of CI-AKI by 22% and 25% respectively.

National agreements to supplement growth

Purchasing hospitals grew in number by 10 (+8.8%) to 124 in 2Q18 which was encouraging given this did not include any of the 250 additional hospitals accessible through the national agreements signed with 3 US multi-hospital systems. The national agreements are expected to significantly reduce the purchase lead time from 4 months to 2 months (between sample and purchase) and with Osprey's current sales territories covering ~80% of these 250 hospitals, the opportunity to increase number of purchasing hospitals is clear and meaningful. We expect these agreements to generate a ramp up of unit sales across quarters as opposed to an immediate acceleration, given the multi hurdle process in dealing with hospitals purchasing departments. Nonetheless, with hospitals under national contracts already sampling DyeVert Plus, there is risk to the upside to our near term sales estimates of 23% unit growth in 3Q18 vs 2Q18.

Undervalued as proof of concept becoming more established

The 2Q18 result helped highlight that the investment case for Osprey remains intact. With its pilot territory rebounding as well as the emergence of additional efficacy data plus agreements with multi-hospital systems, OSP's proof of concept is once again re-enforced. Stock is well positioned for a re-rate particularly if 2Q18 momentum is sustainable. Maintain *Positive* recommendation.

Earnings Forecasts

Yr to December	15A	16A	17A	18E	19E	20E
EBITDA (\$m)	(12)	(12)	(14)	(14)	(14)	(6)
Rep NPAT (\$m)	(12)	(12)	(14)	(15)	(15)	(7)
Adj NPAT (\$m)	(12)	(12)	(14)	(15)	(15)	(7)
Adj. EPS (c)	(7.9)	(6.2)	(5.0)	(4.3)	(4.3)	(1.9)
Adj. EPS Gth (%)	-	21.2	19.1	13.8	0.5	56.2
PER (x)	NM	NM	NM	NM	NM	NM
PEG Ratio (x)	-	-	-	-	-	-
DPS (c)	-	-	-	-	-	-
Yield (%)	-	-	-	-	-	-
Franking (%)	0.0	0.0	0.0	0.0	0.0	0.0
ROE (%)	(106.9)	(70.5)	(53.1)	(58.9)	(141.7)	(92.5)
EV/EBITDA (x)	NM	NM	NM	NM	NM	NM
Net Debt/EBITDA (x)	1.0	1.9	2.3	1.1	0.1	1.5
Int. Cover (x)	-	-	-	-	-	-
Valuation (DCF)						\$0.48

Source: EAP Research

EARNINGS REVISIONS

Table 1. Earnings Revisions

Source: Company disclosures, E&P estimates

Metric Yr to June	Units			Sales (\$m)			EBITDA (\$m)			NPAT (\$m)		
	Old	New	% Chg	Old	New	% Chg	Old	New	% Chg	Old	New	% Chg
2018E	8,664	8,992	3.8%	3.0	3.0	0.7%	(14.1)	(14.5)	(2.4%)	(14.4)	(14.7)	(2.3%)
2019E	24,179	25,213	4.3%	8.4	8.5	0.5%	(15.4)	(14.4)	6.2%	(15.7)	(14.6)	6.7%
2020E	54,593	57,245	4.9%	18.9	19.1	1.1%	(6.5)	(6.4)	1.8%	(6.9)	(6.6)	3.0%
DCF Valuation							\$0.47	\$0.48	2.6%			

The 2Q18 unit sales result of 1955 units was a beat to our estimates of 1801 units (by 8.6%), with DyeVert Plus and DyeTect coming ahead by +6.0% and +46.2% respectively. The recovery in San Antonio (+33% growth vs 1Q18) and the multi hospital agreements with Global Purchasing Organisations (GPOs) and Integrated Delivery Networks (IDNs) providing access to an additional 250 hospitals are the key drivers to our earnings revisions. We step these out in further detail below.

Sales

Looking forward to the remainder of FY18 (Jul18-Dec18), **we forecast sequential unit growth of ~+26% QoQ** primarily from OSP's 15 sales territories that have yet to break even. Excluding San Antonio, the rest of OSP's territories grew at ~+23% which was impressive considering OSP's sales force headcount was flat at 23 (18 sales reps and 5 sales specialists).

We conservatively reduce our ASP forecast for DyeVert Plus. The additional administrative fee of 3%-5% to the multi-hospital system we expect will be partially borne by OSP. As management increasingly focuses on large national GPO contracts, we have started to anticipate some level of volume based discounting

It is worth highlighting that we have not included any sales from foreign territories (Italy and Germany) which are risks to the upside should these eventuate in 3Q18 and 4Q18.

EBITDA

We rebase our cash burn for FY18 following management's guidance for 3Q18 cashflows to mirror that of 2Q18 (-\$4.3m) with 4Q18 expected to start stepping down. The investment into the additional sales headcount (4 sales reps and 4 clinical specialists by 4Q18) is expected to offset the step up in sales keeping the cash burn relatively flat sequentially in 3Q18.

GAINING ACCESS TO AN ADDITIONAL 250 HOSPITALS

OSP signed 3 US multi hospital systems (GPOs/IDNs) in the latter part of 2Q18. We understand these GPOs and IDNs will provide OSP access to an additional 250 hospitals which account for ~10% of the Chronic Kidney Disease (CKD) population. 80% of these 250 hospitals are within OSP's current 18 sales territories. The additional sales reps that are earmarked to be hired by 4Q18 help provide sales support to some of these hospitals as well as additional cities that will help demonstrate appropriate levels of sales support to facilitate further GPO/IDN contracts.

The value proposition for OSP as part of these agreements is a reduction in lead time between sampling to purchasing from 4 months to 2 months. The cost of this is a 3% to 5% administrative fee which we expect will be partially borne by OSP and has been incorporated into our forecasts.

FINANCIAL SUMMARY

Osprey Medical Inc.		OSP.ASX									
As at:	19/07/2018	Recommendation:				Positive	Share Price: \$0.20				
Year end	December	2017A	2018E	2019E	2020E	Year end	December	2017A	2018E	2019E	2020E
INCOME STATEMENT						VALUATION METRICS					
Sales revenue	\$m	2	3	8	19	PER	x	NM	NM	NM	NM
EBITDA	\$m	(14)	(14)	(14)	(6)	Dividend Yield	%	-	-	-	-
Depreciation	\$m	0	0	0	0	EV/EBITDA	x	NM	NM	NM	NM
EBIT (ex associates)	\$m	(14)	(15)	(15)	(7)	EV/EBIT	x	NM	NM	NM	NM
Equity accounted profits	\$m	-	-	-	-	P/FCF	x	NM	NM	NM	NM
EBIT (incl associates)	\$m	(14)	(15)	(15)	(7)	P/BV	x	2.1	3.8	22.6	6.4
Net interest	\$m	0	0	0	0	BLENDED VALUATION					
Pre-tax profit	\$m	(14)	(15)	(15)	(7)	Discounted Cash Flow	\$/sh	0.48	100.0%		
Tax expense	\$m	0	0	0	0	EAP Valuation	\$/sh	0.48	100.0%		
Net profit	\$m	(14)	(15)	(15)	(7)	EARNINGS					
Oth./Outside equity interests	\$m	0	0	0	0	Closing shares on issue	m	340	340	340	365
NPAT attributable to s'hers	\$m	(14)	(15)	(15)	(7)	EFPOWA	m	285	340	340	352
Net abnormal items	\$m	0	0	0	0	Adj. EPS	c	(5.0)	(4.3)	(4.3)	(1.9)
Reported NPAT	\$m	(14)	(15)	(15)	(7)	DPS	c	-	-	-	-
BALANCE SHEET						FINANCIAL RATIOS					
Assets						Sales Growth	%	178.7	84.4	181.1	125.9
Cash	\$m	32	16	2	10	EBITDA Growth	%	(22.6)	(1.7)	0.5	55.9
Working Capital	\$m	1	2	3	7	EBIT Growth	%	(22.9)	(1.9)	0.5	54.6
PP&E	\$m	1	1	1	1	Adj. EPS Growth	%	(19.1)	(13.8)	0.5	56.2
Intangibles	\$m	0	0	0	0	Tax Rate	%	0.0	0.0	0.0	0.0
Investments	\$m	-	-	-	-	EBITDA Margin	%	(873.6)	(482.0)	(170.6)	(33.3)
Other	\$m	0	0	0	0	EBIT Margin	%	(885.7)	(489.5)	(173.2)	(34.8)
Total Assets	\$m	34	20	6	17	ROA	%	(50.6)	(54.8)	(113.3)	(57.1)
Liabilities						ROE	%	(53.1)	(58.9)	(141.7)	(92.5)
Debt	\$m	0	0	0	0	ROCE	%	(394,676)	(1,952.2)	(1,220.4)	(447.3)
Working Capital	\$m	1	1	2	4	Net Debt (cash)	\$m	(32)	(16)	(2)	(10)
Other	\$m	1	1	1	1	Net Debt/Equity	%	(99.3)	(92.7)	(63.0)	(83.7)
Total Liabilities	\$m	2	2	3	6	Net Debt/Debt + Equity	%	(14,348)	(1,274.8)	(169.9)	(511.8)
Net Assets	\$m	32	18	3	11	Net Debt/EBITDA	x	2.3	1.1	0.1	1.5
Ordinary Equity	\$m	32	18	3	11	Working Capital/Sales	%	31.6	51.0	16.4	11.1
Minority Interests	\$m	-	-	-	-	D&A/PP&E	%	29.0	30.4	30.2	39.8
Total Shareholders' Funds	\$m	32	18	3	11	EBIT Interest Cover	x	-	-	-	-
Capital Employed	\$m	0	1	1	2	CASH FLOW					
EBITDA						EBITDA	\$m	(14)	(14)	(14)	(6)
Change in Working Capital						Change in Working Capital	\$m	0	(1)	0	(1)
Other						Other	\$m	1	0	0	0
Gross Operating Cash Flow						Gross Operating Cash Flow	\$m	(14)	(16)	(14)	(7)
Net interest paid						Net interest paid	\$m	0	0	0	0
Tax paid						Tax paid	\$m	0	0	0	0
Net Operating Cash Flow						Net Operating Cash Flow	\$m	(14)	(16)	(14)	(7)
Maintenance capex						Maintenance capex	\$m	0	0	0	0
Free Cash Flow						Free Cash Flow	\$m	(14)	(16)	(14)	(7)
Dividends paid						Dividends paid	\$m	-	-	-	-
Net acquisitions/Growth capex						Net acquisitions/Growth capex	\$m	0	0	0	0
Equity raisings/Buybacks						Equity raisings/Buybacks	\$m	24	0	0	15
Net borrowings						Net borrowings	\$m	0	0	0	0
Other						Other	\$m	0	0	0	0
Net change in cash						Net change in cash	\$m	10	(16)	(14)	8
GOCF/EBITDA						GOCF/EBITDA	%	97.2	107.0	99.0	111.6
Total Capex/Sales						Total Capex/Sales	%	19.7	8.8	2.4	1.6
Total Capex/Depreciation						Total Capex/Depreciation	x	1.6	1.2	0.9	1.0

Source: Company data, E&P estimates

RESEARCH RECOMMENDATION DEFINITIONS

Positive	Stock is expected to outperform the S&P/ASX 200 over the coming 24 months
Neutral	Stock expected to perform in line with the S&P/ASX 200 over the coming 24 months
Negative	Stock is expected to underperform the S&P/ASX 200 over the coming 24 months
Speculative Buy	Stock has limited history from which to derive a fundamental investment view or its prospects are highly dependent on event risk, <i>eg.</i> Successful exploration, scientific breakthrough, high commodity prices, regulatory change, etc.
Suspended	Stock is temporarily suspended due to compliance with applicable regulatory and/or Evans & Partners policies in circumstances where Evans & Partners is acting in an advisory capacity.
Not Rated	Stock is not included in our investment research universe.

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Recommendations are primarily determined with reference to how a stock ranks relative to the S&P/ASX 200 on the following criteria:

Valuation	Composite of Rolling 12 month prospective multiples and discounted cash flow (DCF), or DCF for resource stocks.
Earnings Outlook	Forecast 2 year EPS growth.
Earnings Momentum	Percentage change in the current consensus EPS estimate for the stock (rolling 1 year forward basis) over the consensus EPS estimate for the stock 3 months ago.
Shareholder Returns	Composite of forecast ROE (rolling 1 year forward basis) and the percentage change in ROE over 2 years.
Debt Servicing Capacity	Rolling 12 month EBIT Interest Cover ratio.
Cyclical Risk	Qualitative assessment of the 2 year outlook for a stock/industry's profit cycle.
Industry Quality	Qualitative assessment of an industry's growth/returns potential and company specific management capability.
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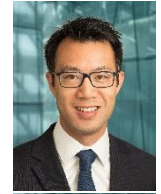
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FSREC IV	<p>The Responsible Entity (RE) and Fund Administrator of Fort Street Real Estate Capital Fund IV (FSREC IV), the Trustee of FSREC IV's primary underlying investment, Fort Street Real Estate Capital Trust IV (the Trust) and Evans and Partners Pty Ltd are wholly owned subsidiaries of Evans Dixon Ltd and related bodies corporate. The Investment Manager (IM) of FSREC IV is partially owned by a related body corporate of Evans and Partners. Each of the RE, Fund Administrator, Trustee and IM will receive fees for services provided to FSREC IV and/or the Trust. Directors or employees of Evans Dixon and/or its related bodies corporate are directors of the RE, Fund Administrator and/or Trustee of FSREC IV and/or the Trust. Each individual receives remuneration from Evans Dixon and/or its related entities.</p>
JLG	<p>Evans and Partners has arranged, managed or co-managed an offering of securities of the company or its affiliates in the past 12 months, for which it received a fee.</p>
LE.US	<p>A director of Evans Dixon Limited, the ultimate holding company of Evans and Partners Pty Ltd, is a director of Lands' End Inc.</p>
LLC	<p>A director of Evans Dixon Limited, the ultimate holding company of Evans and Partners Pty Ltd, is a director of Lendlease Group.</p>

LSF	Evans and Partners has arranged, managed or co-managed an offering of securities of the company or its affiliates in the past 12 months, for which it received a fee.
MGP	Evans and Partners has arranged, managed or co-managed an offering of securities of the company or its affiliates in the past 12 months, for which it received a fee.
MQG	Evans and Partners has arranged, managed or co-managed an offering of securities of the company or its affiliates in the past 12 months, for which it received a fee.
NEW	The Responsible Entity (RE) and the Investment Manager (IM) of New Energy Solar (NES) and Evans and Partners Pty Ltd are wholly owned subsidiaries of Evans Dixon Ltd and related bodies corporate. The RE and IM will receive fees for acting as RE and IM of NES. Directors or employees of Evans Dixon and/or its related bodies corporate are directors of the RE and/or IM of NES. Each individual receives remuneration from Evans Dixon and/or its related entities. Evans and Partners has arranged, managed or co-managed an offering of securities of the company or its affiliates in the past 12 months, for which it received a fee.
OSP	Evans and Partners has arranged, managed or co-managed an offering of securities of the company or its affiliates in the past 12 months, for which it received a fee.
PMV	A director of Evans Dixon Limited, the ultimate holding company of Evans and Partners Pty Ltd, is a director of Premier Investments Limited.
SOHS.US	A director of Evans Dixon Limited, the ultimate holding company of Evans and Partners Pty Ltd, is a director of Sears Hometown & Outlet Stores Inc.
SUN	A director of Evans Dixon Limited, the ultimate holding company of Evans and Partners Pty Ltd, is a director of Suncorp Group Limited.
SWM	A director of Evans and Partners Pty Ltd is a director of Seven West Media Limited.
S32	A director of Evans Dixon Limited, the ultimate holding company of Evans and Partners Pty Ltd, is a director of South32 Ltd.
URF	The Responsible Entity (RE) and Investment Manager (IM) of US Masters Residential Property Fund (URF), other entities that provide services to URF and Evans and Partners Pty Ltd are wholly owned subsidiaries of Evans Dixon Ltd and related bodies corporate. Each of the RE, IM and other related entities will receive fees for services provided to URF. Directors or employees of Evans Dixon and/or its related bodies corporate are directors of the RE, IM of URF and/or other related entities that provide services to URF. A director of Evans and Partners Pty Ltd is a director of URF's primary underlying investment, US Masters Residential Property (USA) Fund (US REIT). Each individual receives remuneration from Evans Dixon and/or its related entities.
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WBC	Evans and Partners has arranged, managed or co-managed an offering of securities of the company or its affiliates in the past 12 months, for which it received a fee.

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I, Steve Wheen, hereby certify that all the views expressed in this report accurately reflect my personal views about the subject investment theme and/or company securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

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