



# Biotech Daily

Friday November 10, 2017

*Daily news on ASX-listed biotechnology companies*

## Dr Boreham's Crucible: Nanosonics

**By TIM BOREHAM**

**ASX code:** NAN

**Share price:** \$2.92

**Shares on issue:** 299,263,438

**Market cap:** \$873.8 million

**Chief executive officer:** Michael Kavanagh

**Board:** Maurie Stang (chairman), Marie McDonald, Michael Kavanagh, Dr David Fisher, Richard England, Steven Sargent

**Financials (2016-17 year):** sales \$67.5 million (up 58%), net profit \$26.2 million (previously \$100,000), earnings per share 8.79 cents (up 2200%), cash \$63 million (up 29%)

**Identifiable Holders:** JCP Investment Partners 8.4%, Fidelity Management 7%, Maurie Stang 7.59%, Bernard Stang 6.3%, Steve Kritzler 2.85%.

The rise and rise of the Trophons sounds like something out of a Dr Who episode, but we're referring to the global adoption to date of Nanosonics' automated medical probe sterilizing units, the Trophon EPRs.

When opened, the wall-mounted units bear a passing resemblance to a urinal (or maybe that's just Crucible's lurid imagination).

The only resemblance to a Dalek is that all germs will be exterminated within seven minutes and at the press of a button.

One of Australia's greatest medical device success stories so far, Nanosonics has sold 14,100 units to date including 12,400 in the US.

The company cites a global addressable market of 140,000 units, which means that Nanosonics is only 10.07 percent into its quest to make Trophon the bug-busting standard-of-care.

### **How they work**

As with clothes pegs and Liquid Paper, simplicity is the key to the Trophon invention.

The probes are inserted into the 'urinal' and sprayed with biocidal micro droplets derived from canisters containing hydrogen peroxide.

No golden staph will live to tell the tale in this pissoir.

The process compares with the routine of taking the probes to a central facility and spraying and wiping them with a compote of toxic chemicals. They're so harmful that the room must be isolated and staff need to don hazardous clothing and even then, the part of the probe being held may not be sterilized.

In contrast, Trophons emit water and oxygen as a by-product - two elements the world could do more with, along with buttercups and daisies.

### **At the forefront of germ warfare**

Driving the take-up of the Trophon are stricter hospital infection guidelines enforced by august bodies such as the World Federation of Ultrasound in Medicine and Biology.

Yes – there really is one.

Increasingly, those in-the-know are demanding high-level disinfection to apply to all semi-critical procedures, whether bodily insertion is involved or otherwise.

This includes anything from organ and breast biopsies, tumor ablation, venous access and abscess and foreign body removal.

The company has screeds of clinical evidence, most recently pointing to a six-year Scottish study on the infection rate of patients after undergoing semi-invasive ultrasound procedures.

The gist is that those subject to probes not treated with high-level disinfection were more likely to be prescribed antibiotics because of “positive microbiological reports”.

The moral of the story? What the Scots wear under their kilts is not as important as what’s put up ’em.

## **Razor blade model**

Nanosonics sells the units outright to hospitals for about \$10,000 each as a capital item, but over time the company expects to derive more revenue from a list of consumables and accessories that would make even Apple’s product folk blush.

These include the hydrogen peroxide canisters, probe covers, printers and printer rolls, log books, wall-mounted Trophon carts and the mounts to mount the Trophon carts.

In five years’ time, the company expects about 25 percent of revenue to derive from equipment sales, with 50 percent gleaned from consumables and a further 25 percent from servicing.

In the US, the Trophons are distributed directly by the company and by GE Healthcare. In August, Nanosonics and GE inked a new re-seller agreement for a further three years after the current compact expires on June 30, 2019.

“As a result of the new agreement Nanosonics will gain a material increase in both sales and margin on consumables in North America,” the company says.

In the UK, Nanosonics has rolled out a variant called the managed equipment service (MES) model, by which the company continues to own the equipment.

The hospital pays an all-inclusive price for use and servicing, which obviates the need for the cash-strapped healing institutions to buy the equipment as a capital item.

In June, Nanosonics also struck a deal with sterilization specialist Sakura Seiki to sell its Trophons in germ-phobic Japan, the world’s second biggest healthcare market.

Nanosonics cites an addressable market of 2,000 units in Japan, with the tie-up subject to ongoing clinical trials.

## **Clean financials**

From a standing start of nil a decade ago, Nanosonics turned over \$67.5 million of revenue last year.

Having recorded small losses between 2012-’13 and 2014-’15, Nanosonics struck a maiden \$100,000 surplus in 2015-’16 and a healthy \$26 million profit for 2016-’17.

At its recent AGM, Nanosonics top brass affirmed that current (first) half sales were likely to be similar to the second (June) half uptake, but also warned that uncertainties around the US health care reform process could delay capital purchases.

UK purchases are expected to grow by 75 to 100 percent, with 90 percent of orders subject to the MES model.

Nanosonics is also about to enter the Middle Eastern market and commence pre-marketing in Japan.

### **Dr Boreham's diagnosis:**

To the naysayers, Nanosonics' \$800 million-plus market cap doesn't take into account the likelihood that the company has reaped the low-hanging fruit and that sales growth will slow.

Nanosonics stock has traded between 14 cents and \$3.60 since listing in May 2007 at 50 cents apiece. At current levels, the shares are trading on an earnings-per-share multiple of 34 times, based on 2016-'17 earnings.

Expensive? Perhaps - but not for a growth stock in the healthcare sector.

Nanosonics' fan base points to the market being only 10 percent penetrated and the disinfection guidelines that will force many hospitals to adopt the Trophons.

Nanosonics expects to spend a hefty \$14 million on research and development this year compared with \$9.5 million last year, partly on product extensions in the sterilization sector.

In fact, management targets the launch of two new products over the next two years, "subject to expected regulatory approvals".

Management is mum about the target markets, but the products could prove bigger than the Trophons.

***Disclosure: Dr Boreham is not a qualified medical practitioner and does not possess a doctorate of any sort. He does his bit for the sterilization cause by washing his hands before eating.***