



# Biotech Daily

Friday October 20, 2023

*Daily news on ASX-listed biotechnology companies*

## Dr Boreham's Crucible: Pro Medicus

**By TIM BOREHAM**

**ASX code:** PME

**Share price:** \$78.16

**Market cap:** \$8.16 billion

**Shares on issue:** 104,455,279

**Chief executive officer and co-founder:** Dr Sam Hupert

**Board:** Peter Kempen (chair), Dr Hupert, Anthony Hall (co-founder), Anthony Glenning, Dr Leigh Farrell, Deena Shiff, Alice Williams

**Financials (Year to June 30 2023):** revenue \$124.9 million (up 33.6%), underlying profit before tax \$83.88 million (up 34.5%), net profit \$121.5 million (up 36.5%), full year dividend per share 30 cents (up 36%), cash and investments \$76.2 million (up 23%)

**Identifiable major shareholders:** Dr Sam Hupert 25.03%, Anthony Hall 25%.

When it comes to investor perceptions of Pro Medicus, chief executive and co-founder Sam Hupert often feels he can't win.

According to Dr Hupert, the US-focused diagnostic imaging company did things backwards by first winning a swathe of 'sandstone' academic hospitals - names such as Mayo Clinic, Yale, New York University, University of California and Harvard Medical School's Massachusetts General Hospital.

“Most companies start off small and then get a few regional sites and maybe they get one or two of those really top names,” he says.

Investors then had the impression that Pro Medicus didn't do much outside of the 'sandstones' - especially among the integrated delivery networks (IDNs) that account for the lion's share of US hospitals.

“The market said ‘you only work in the big end of town’ but then we won a whole lot in the middle market. They then said ‘have the big ones gone’?”

The company last month assuaged the doubters by signing its biggest client to date, the Texas-based IDN Baylor Scott & White Health (BSWH) in a \$140 million deal over 10 years.

The company's first Texan client, BSWH has 5,000 licensed beds at 51 hospitals.

In reality, the difference between a 'sandstone' client and a not-for-profit IDN is not black and white. “An IDN can be large and sophisticated, the only difference is they aren't part of a university medical teaching school,” Dr Hupert says.

No matter the definition, Pro Medicus has hit a purple patch, winning four IDNs in the last 12 months and all of them for more than one product.

The jobs are characterised by software-as-a-service and annuity revenue based on minimum transaction levels.

The 'sandstones' aren't forgotten, either: in July, Pro Medicus signed Memorial Sloan Kettering Cancer Centre in a \$24 million, seven-year deal, by which the New York house of healing uses the full suite of the company's offerings.

## **A home-grown hero**

Pro Medicus provides diagnostic imaging, practice management and image archiving software to radiology practices.

The company was founded by Melbourne general practitioner Dr Hupert and his technologist friend Anthony Hall in 1983.

The company is mainly involved in the 'viewing' part of the chain: enabling clinicians to call up the images quickly and make better use of them.

Pro Medicus has surfed the burgeoning data requirements for modern imaging techniques such as high-density multi-slice computed tomography (CT) scans, high density breast tomo-synthesis, opto-acoustic breast ultrasounds and total body scans.

The company's key products are Visage RIS (as in radiology information system) and the cornerstone Visage 7 (enabling users to consolidate information requiring multiple views into a customized single platform).

The image storage tool Visage Open Archive was introduced in 2017, with Visage Workflow Management emerging in 2020.

In 2019, Pro Medicus acquired the California based Visage Imaging for a knock-down \$5 million. Executed during the global financial crisis, this deal turned out to be the bargain of the century as the Visage products are now the company's core offering.

## **Finances and performance**

In a year of records, Pro Medicus posted a net profit of \$60.6 million, 36 percent higher, on revenue of \$125 million (33.6 percent higher).

Of the revenue, \$97.3 million (or 78 percent) derived from capital sales, compared with only \$67.5 million the previous year. The US accounted for 83 percent of revenue. The minor components of support and services income are growing less quickly, but the company cites forward revenue of \$468 million over five years.

The BSWH contract is worth \$140 million over 10 years and a minimum \$14 million a year, which broker Goldman Sachs estimates is more than five times the size of the average contracts won by the company to date.

Broker Wilsons coos that BSWH is the "perfect example" of a new client: "a not-for-profit health network, with a prominent market position, in metropolitan centres [and], demonstrating willingness to invest in [information technology] infrastructure."

More of a gesture than anything, the company dispensed a final dividend of 17 cents per share, taking the full year payout to 30 cents (36 percent higher).

With no debt and \$121 million in cash and investments, Pro Medicus won't be carrying out a capital raising any time soon.

The Pro Medicus share price has grown steadily over the last five years, having been \$1.45 in 2015 when Biotech Daily first began covering the company and around \$10 in October 2018. The shares were around \$52 in October last year and peaked at \$83.91 on October 2 this year.

The company listed in October 2000 – yep, October is a big month for the company - at \$1.15 apiece.

## **Head in the clouds**

Depending on the sector, Pro Medicus competes with a range of competitors but the company rarely sees its ASX-listed peer, Mach7, vying for the same jobs.

Traditional rivals include equipment vendors such as GE Health, Siemens and Philips and the erstwhile camera film makers Agfa, Fujifilm and Carestream.

Dr Hupert says Visage can be adapted to suit different clients of different sizes and is the only genuine internet cloud-based tool available. He believes the company has not made an on-premises installation (that is, of traditional hardware) over the last three years.

“Three or four years ago in the US if you mentioned ‘cloud’, everyone would look at you blankly,” he says. “The whole argument has flipped on its head, because people now realise the cloud is not only more scalable, but far more secure.”

## **Supporting cardiology**

In its first promised expansion into the ‘ologies,’ Pro Medicus expects to release a cardiology product - in effect a tweaking of Visage - “in the next few months”.

In field-testing phase, the tool will support cardiac ultrasounds.

“The company has been able to fill-in the feature functions over and above what radiologists require,” Dr Hupert says. “We do literally millions of ultrasounds a year, but the highly specific cardiac ones require a super set of measurements.”

He also notes the increased popularity of cardiac computer tomography (CT), as an alternative to a stress test (putting the patient on a treadmill or bike) or an invasive cardiac angiogram.

“X-ray type modalities and equipment are being used more and more in cardiology,” he says.

While radiology and cardiology systems are separate, there is much crossover in terms of who does what.

“Radiologists often do cardiac CTs ... so it makes sense that the one system can be used ubiquitously across both disciplines,” Dr Hupert says.

## **Futurologist didn’t predict getting it wrong**

Ironically, a fear of artificial intelligence (AI) has created an acute global shortage of radiologists.

“Five years ago, a futurologist predicted there would be no need for radiologists in five years’ time and - guess what - he was wrong,” Dr Hupert says.

He attributes the dearth of radiologists to fewer doctors taking radiology training, for fear they won’t have a job when they have qualified. Others are suffering burnout because of the huge increase in imaging volumes.

Dr Hupert says AI has created both hype and fear in the profession.

“We are now at the tail end of the disappointment phase that always follows a hype phase,” he says. “Reality is setting in. We will see practical uses for AI in diagnostic imaging, but then the question is how to commercialise it. There’s limited reimbursement at this point, but that will change.”

Dr Hupert says by “good fortune or foresight” Visage is the only fully AI capable platform of its peers.

## **Putting AI to use**

Pro Medicus already has a breast density algorithm, which has been cleared by the US Food and Drug Administration and should be commercialised in the next few months.

Imaging of ‘dense’ breasts is far more difficult than scanning ‘fatty’ breasts because both the tumor and the background come out as white on the image. It’s like finding the proverbial rabbit in a snowstorm.

“Data shows that algorithms can be just as accurate as a human, if not more accurate,” Dr Hupert says.

In Australia and Europe, all breast screening is read by two separate radiologists, with a third radiologist adjudicating if there’s a difference of opinion.

In the US, it’s up to the one radiologist. So, AI can eliminate the need for a second human reading here, or become a reassuring tool for US breast radiologists.

Another use for AI is in procedures such as ultrasound and chest x-rays: if the patient moves, the AI will deem the image to be substandard and either correct it, or notify the operator.

“Those sorts of use-cases are very compelling and AI is becoming sophisticated and accurate enough to be used in the not-too-distant future,” Dr Hupert says.

## **Glass half full?**

Pro Medicus currently boasts ‘only’ a seven percent share of the US market, as measured by the 500 million or so exams carried out there annually.

“We may only have seven percent of the market but it is all about the clients who make up this seven percent - including nine of the top 20 teaching hospitals,” Dr Hupert says.

Dr Hupert notes emerging activity in the private hospital sector, which has been in “deep freeze” because of the large number of merges and acquisitions.

“We have a strong pipeline with a variety of opportunity across different markets and different sized clients,” he says.

Pro Medicus also has a weather eye on Europe, especially in Germany where it conducts research and development for Visage.

Dr Hupert says most health services in Europe are government-funded and very bureaucratic. European hospitals are less advanced in embracing the internet 'cloud' "but we think that will change and that could be an entry point for us."

In Australia, Pro Medicus sells its original RIS (radiology information system) to the private sector, having signed contracts with Lumus (Primary Healthcare and I-Med.

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

With an \$8.7 billion market valuation, Pro Medicus eventually may rival the ASX life sciences Three Big Caps - CSL, Resmed and Cochlear - in size.

(The smallest, Cochlear, has a \$16 billion market capitalization.)

Not everyone is convinced about the company's growth prospects. Research house Morningstar claims Pro Medicus should be worth less than half its current value.

The normally diplomatic Morningstar says Visage 7 has been popular with academic hospitals "with large endowments and greater interest in advanced visualisations and AI".

The trouble is, these features are "largely superfluous outside of the academic hospitals market and [we] expect wider adoption to continue to be slow".

Fair enough - but the Baylor Scott & White Health deal suggests that, outside of the 'sandstones' Pro Medicus' prospects remain bigger than Texas.

In the meantime, Dr Hupert says Pro Medicus won't rest on its laurels in terms of rolling out new products to new markets.

"In software there are only two states: quick and dead and you don't want to be dead."

***Disclosure: Dr Boreham is not a qualified medical practitioner and does not possess a doctorate of any sort. He's not particularly quick but is happy to report he still has a pulse.***