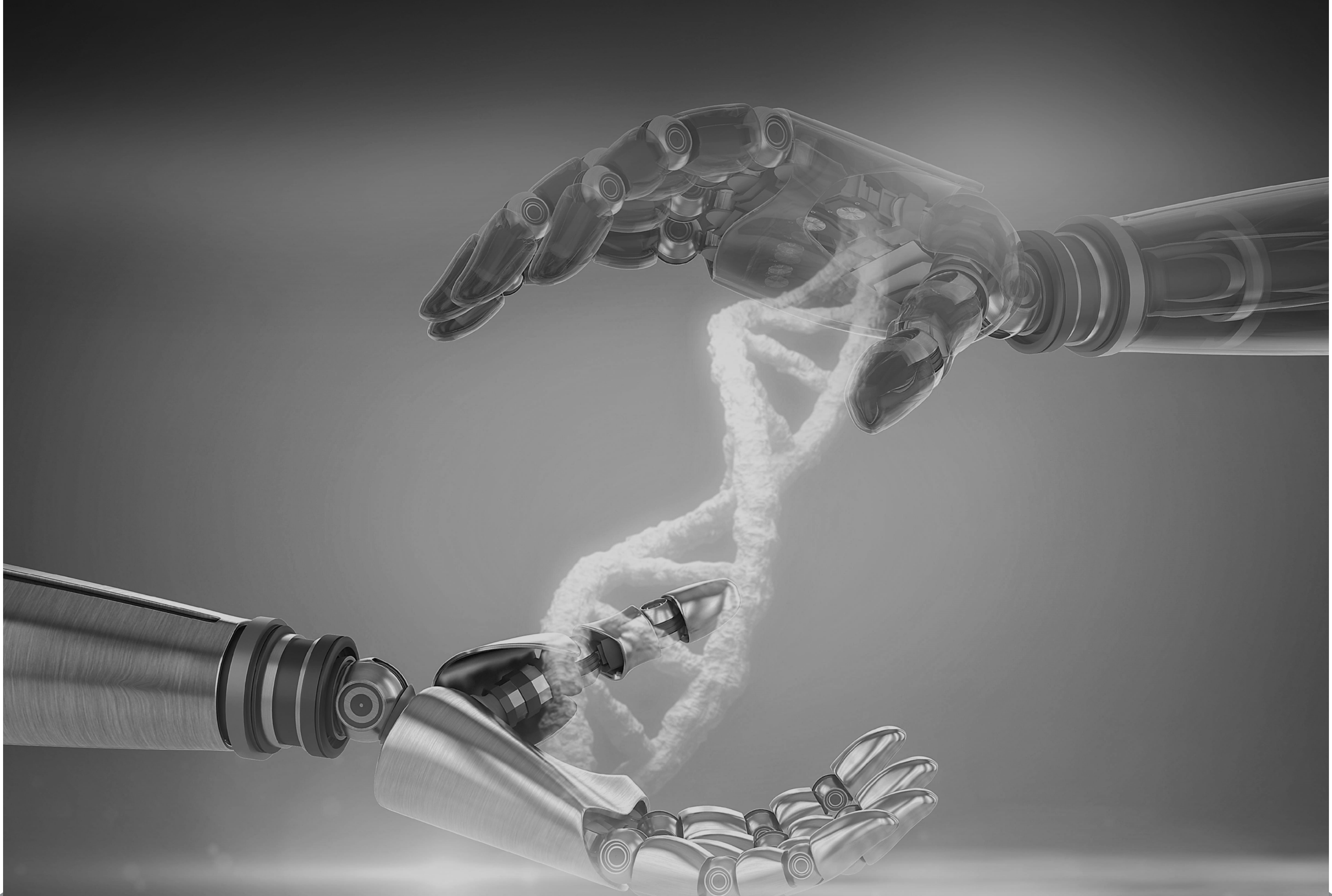
STOCKS DOWN UNDER

16 FEBRUARY 2021

Emerging Stocks Down Under

“Every type of politics could be addressed from the point of view of leaders trying to survive.”

- Bruce Bueno De Mesquita (b. 1946), Political scientist



IMRICOR MEDICAL SYSTEMS

Not missing a beat

DAMSTRA

Riding the infrastructure spending wave

ADVANCE NANOTEK

Make sure to buckle up

IMRICOR MEDICAL SYSTEMS

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Stocks Down Under rating: ★★★★

ASX: IMR
Market cap: A$ 271M

52-week range: A$0.75 / A$2.94
Share price: A$ 2.27

Imricor Medical Systems, headquartered in the world's medical device capital of Minneapolis-St Paul, USA, has developed the world's first MRI-compatible system for cardiac catheter ablation, with the system gaining CE Mark approval for Europe in January 2020. If you or someone you know are among the 12 million, or so, people worldwide that have atrial fibrillation, or some other arrhythmia problem, you may appreciate what a breakthrough Imricor has achieved. This innovative company is still in the early stages of its growth.

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ASX: DTC
Market cap: A$ 257M

52-week range: A$0.40 / A$2.44
Share price: A$ 1.41

Shareholders in workplace management solutions developer Damstra have had a difficult time the last five months as its shares declined over 40% from their October high of $2.44. Damstra operates in a more specialised segment of the workplace management industry, focusing on the mining, construction, energy, utility, government and education. Through a combination of cloud and hardware-based products and services, we believe this company's specialised segment is a strong candidate for an infrastructure-based recovery.

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Share price chart

Source: Tradingview

Of the many problems you could get with your heart in middle or old age, cardiac arrhythmias are among the more common. Arrhythmias happen where the electrical impulses that coordinate your heartbeats don't work properly, causing your heart to beat too fast, in a condition called 'tachycardia', or too slow, which is 'bradycardia'. A common arrhythmia problem is atrial fibrillation, where by chaotic electrical impulses in the atria, the heart's upper chambers, cause tachycardia. If you have atrial fibrillation or a related problem called atrial flutter, where the heartbeats are slightly more organized but still not normal, you could be in danger of having a stroke. Sometimes the arrhythmia is in the heart's lower chambers, the ventricles. Ventricular tachycardia leaves you in danger of sudden cardiac arrest.

Setting hearts aflutter on ASX

For patients with arrhythmias, Imricor Medical Systems has spent the last decade or so developing the Next Big Thing in terms of therapy. We've known for a while now that you can fix arrhythmias simply by sending a catheter to the site of the heart tissue that is causing the trouble and scarring or destroying that tissue using radiofrequency waves.

Cardiac ablation therapy works like a dream. The part that's not so simple is imaging the patient's heart so that the interventional cardiologists knows what tissue he or she is looking at in order to properly ablate it. Around 2009 Imricor used technology first developed at the legendary Johns Hopkins University to invent a cardiac catheter ablation system that was MRI-compatible, allowing the MRI machines to do the imaging. Now you know where the 'mri' in Imricor's name comes from.

Imricor may have been born and raised in Minnesota, but it found the capital to grow its new take on cardiac ablation therapy into adulthood right here in Australia. The ASX IPO raised A$13m at 83 cents per share in a deal which was completed in August 2019. The timing was perfect because in January 2020 the company gained CE Mark approval in Europe for its cardiac catheter ablation system, which it called Vision-MR. The initial indication was only atrial flutter, with other larger patient populations to come, but that was enough to propel the Imricor share price to $1.90 on 11 February 2020 before the Corona Crash pummelled it down to 75 cents by 30 March.

Resilience in a time of crisis

Since January 2020 Imricor has been on a mission to raise awareness of Vision-MR and its implementation in labs that do iCMR – that is interventional cardiovascular magnetic resonance – around the world. Stage 1 of the company's commercialisation plans have so far focussed on lab adoption in Germany enabling early clinical success and a pipeline of purchase agreements.

Despite the slow start due to COVID-19, adoption of Imricor's products has taken off since the first trial surgeries in Dresden in February 2020. Since then, the company has signed multiple purchase agreements at universities and clinics in Germany, France and The Netherlands and contracted various sites for early adoption of its iCMR labs. While these agreements are for undisclosed amounts, Imricor will get a much-needed distribution boost under its sales agreements with Phillips and Siemens to sell its equipment.

The take-up of Imricor's products has been consistent even with the spread of COVID-19 and vaccines/diagnostics dominating the healthcare scene, and though a second wave in Europe could potentially further delay iCMR approval and setup, Imricor's stock has remained resilient. The market demand for cardiac catheters is not exactly small, worth around $3-4bn in the US and Europe alone. And while the company's catheter product is only used in Type 1 atrial flutter (ablation in the right atrium) at the moment, the intention is to drive through expanding indications into atrial fibrillation and ventricular tachycardia, and beyond that to other arrhythmias.

Further growth is the main objective

For Imricor, the shift towards relatively non-invasive MRI-based procedures in a steadily aging population is what gives it an edge, but its main issue remains its funding, with commercial sales still only in the intitial stages. That said, we believe the good times are coming. Imricor's next step is the approval of its products in the US and in Australia, alongside the aforementioned expansion in the approved indications. The company raised A$28.5 in late November at $2.35 per share to fund the relevant research and development costs.

Costs aside, the company's impressive list of sales milestones and expanding geographic opportunities put it in good stead for 2021. Interestingly, Imricor is also looking at opportunities beyond cardiac ablation. In September, the company was awarded a contract for about US$400k by the US National Institute of Health (NIH) to develop an MRI-compatible myocardial biopsy system.

COVID-19's global second wave has not been great for companies looking to introduce new technologies unrelated to the pandemic. However, once the virus has been relegated to the history books there's still going to be a heck of a lot of cardiac arrythmia out there. With Imricor executing well under somewhat trying circumstances, we believe this is a four star opportunity.

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Not your average workforce management company

Damstra was founded in 2002 with a focus on Australian mining contractor management and has grown to provide products and services to many more industries. The company currently has two main platforms supported by four different product lines and we believe it's important to provide a brief overview of each so you can understand just where Damstra's opportunity in a recovering economy resides.

Damstra has its own cloud and mobile-based 'workforce management platform.' Unlike intelliHR's (ASX: IHR) platform, an overarching HR tool, Damstra focuses on worksite compliance, real-time attendance and safety management and alerts, personnel verification, supplier verification, management and registration. This is a comprehensive platform, which allows supervisors to check who is on-site, confirm an employee's certifications are up-to-date or even be alerted if an employee has fallen through its application developed for wearables (like smart watches), to name a few.

Damstra's other main platform allows for asset tracking called 'SmartAsset.' This platform allows constant monitoring of a company's assets and completes tracking of assets' warranty status and compliance with safety regulations. It can do all of this through easy and cloud-based QR and RFID integration that allows for complete and real-time tracking of an asset's maintenance and inspection schedule.

The four supporting product lines include cameras and terminals that allow for real-time information on who's in the area in question and their temperature. These terminals are also enabled for drug and alcohol testing with customised frequency and access thresholds. Next, we have Samm. This Health, Safety and Environment (HSE) risk management mobile platform allows for real-time analytics and AI-assisted custom forms, questionnaires, alerts, catalogues and inspection, etc.

For companies in need of additional workforce training, Damstra even allows for custom course design. Lastly, the company enables all the information to be collected from its platforms and products, to be easily analysed in real-time.

A recovering economy needs infrastructure spending

As the world's economy begun to recover, infrastructure spending received a shot in the arm long-before any human. As many Australian readers will know, infrastructure spending has long been a focus of any Australian economic plan. Infrastructure Partnerships Australia's 2020 Australian Infrastructure Budget Monitor estimates $225bn is slated to be invested in Australia's infrastructure over the next four years. But what you might not know, is that the rest of the world is also planning a significant building renaissance.

Looking closely at the United States, the main focus of Damstra for its growth prospects, President Biden's Clean Energy plan lists repairing and constructing infrastructure as one of the main purposes for the proposed US$2 trillion in COVID-19 recovery funding. Many other countries, from China to the European Union's member states, are planning on spending big on infrastructure to help jump-start their economies.

But the other driving force for the construction and resources sectors is the massive transition to a clean energy economy the world is currently undergoing. Going forward, we believe this spending will likely create significant demand for both of Damstra's main target industries: mining and construction, and energy and utilities.

The US is where the growth is

Damstra's operations can be classified simply as the provision of software services (processing and development), the rental of hardware equipment, card reissues and training services. The company currently derives the vast majority of its $19.6m in total FY20 revenue from Australian clients who generated $16.3m, a 22% increase year-over-year. International operations generated $3.3m during FY20, a 70% increase year-over-year. Management does not specify the specific amount but says "a significant portion of (international operations) revenue" was earned in the United States.

We currently expect the United States focused operations to continue to provide a significant portion of international revenue and at some point the US operations may overtake Australia in terms of size. To highlight this point, on 4 February 2021, Damstra announced the establishment of a North American Advisory Board whose job will be to 'identify business development opportunities and accelerate the company's organic growth in North America.'

Forget FY21, onward to FY22

We believe Damstra's products and services fit neatly within a series of industries that will see a surge in demand over the coming years. Due to FY21 still being mired in COVID-19 globally, Damstra is expected to have a lackluster FY21 and only generate $6.4m in EBITDA, a decline of 6% year-over-year.

However, during FY22, FY23 and FY24, the company is expected to generate EBITDA growth of 81%, 38% and 64%, respectively. Combine this with EV/EBITDA multiples for FY22, FY23 and FY24 of 22x, 16x and 10x respectively and we believe the market pull-back has been too far, too fast. So four stars from us.

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Source: Tradingview

Saving the world from skin cancer

Advance Nanotek was founded with one main goal, to help prevent skin cancer the world over. Managing Director, Geoff Acton, has himself had 32 skin cancer procedures since 2005 and says "these zinc based products are not just about business, it's personal". Advance Nanotek's products are organic and vegan while also allowing for Sun Protection Factor (SPF) protection in excess of 50. For future demand

Going forward it is important for the industry as a whole to develop non-toxic chemical-based sunblock technology as the world's coral reefs are suffering from the 14,000 tons of sunscreen that are estimated to wash into the oceans each year according to National Geographic. This sunscreen runoff is estimated to deposit over 82,000 different chemicals into the seas and this happens to be one of the world's leading causes of coral reef damage. Many places, like Hawaii and Palau, are taking action by banning harmful sunscreens. As these bans, and the likely issuance of others, go into effect in the coming years, we believe demand for products like Advance Nanotek's will increase.

Advance Nanotek is Australia's leading zinc oxide powder manufacturer with output of over 5,000 tonnes per year. This is the raw material for its patented vegan and organic products, i.e. mainly powders and sunscreen. The sale of these products resulted in $18m in revenue and $7.5m in EBITDA generated during FY20.

This revenue comes from two main types of Zinc Oxide technology: ZinClear XP and ZinClear IM Dispersions. ZinClear XP allows for SPF to reach in excess of 50 without the need for excess chemicals. As we mentioned above, there is significant demand for this type of sunscreen. During FY20, ZinClear represented the vast majority of total sales at $15.8m, or 88% of total revenue. The company uses this technology to create a variety of products, including powders and pourable sunscreen. ZinClear IM Dispersions, on the other hand, allows small scale manufacturers to produce their own sunscreen products. This product line generated $2.2m in revenue during FY20, or 12% of total revenue.

COVID-19: a rough year

COVID-19 was rough on many companies, but especially those in the sunscreen industry. The reason for this was that many manufacturers switched a significant amount of their production and sales to hand sanitiser. Additionally, as many people stayed home instead of traveling to the beach or exotic locations, demand for sunscreen declined significantly. Simply put, that was really bad for Advanced Nanotek.

Indeed, only around 50% of Advance Nanotek's 180 tonne stock of XP powder allocated for sale in the US (not North America) actually shipped in the four months through November 2020. European sales suffered a similar fate, declining 55% year-over-year during the five months through November 2020. While the full extent of the damage for FY21 is unclear, we believe there won't be 50% revenue growth in FY21 like there was in FY20. Management hinted this was the case when it said that this decline in demand due to COVID-19 was unlikely to "be resolved over the next two years."

There is one potential silver lining: Sunscreen has an average self-life of only two years and it is likely that manufactures and retailers will need to order more product and base ingredients to replace out-of-date stock. It is unclear how much of an impact this will have on increasing future sales, but we believe it is worth noting.

Moving is never easy

As we mentioned, management has decided that the company would be better served by transitioning its listing from the ASX to NASDAQ. This means that, likely during 2021, shareholders will receive their equivalent AUD-based ASX shares in USD-based NASDAQ shares. We believe this move may trigger some, or many, investors to sell their stock ahead of the move.

Too much risk

Due to the uncertainty osurrounding FY21's market conditions and sales as COVID-19 continues to ravage large parts of the world while vaccine efforts fall behind schedule, there are currently no market forecasts for FY21's results. However, we expect growth will be marginally lower than in FY20. Based on FY20's results, the market is currently valuing Advance Nanotek at 13x EV/Revenue and 31.5x EV/EBITDA, i.e. these metrics look back at the company's prior year results. Despite the high level of growth seen in prior years, we remain concerned about two things: COVID-19 demand issues and the move to NASDAQ. With demand likely to remain depressed for at least two more years as COVID-19 hurts beach visitations and travel, we believe it is unlikely that FY20's level of growth will come back any time soon. Throw in the uncertainty around the move to the NASDAQ and Advance Nanotek is a two star stock for us.

Pitt Street Research Pty Ltd

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Pitt Street Research Pty Ltd is founded on more than 40 years of combined experience researching companies in a range of different sectors.

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