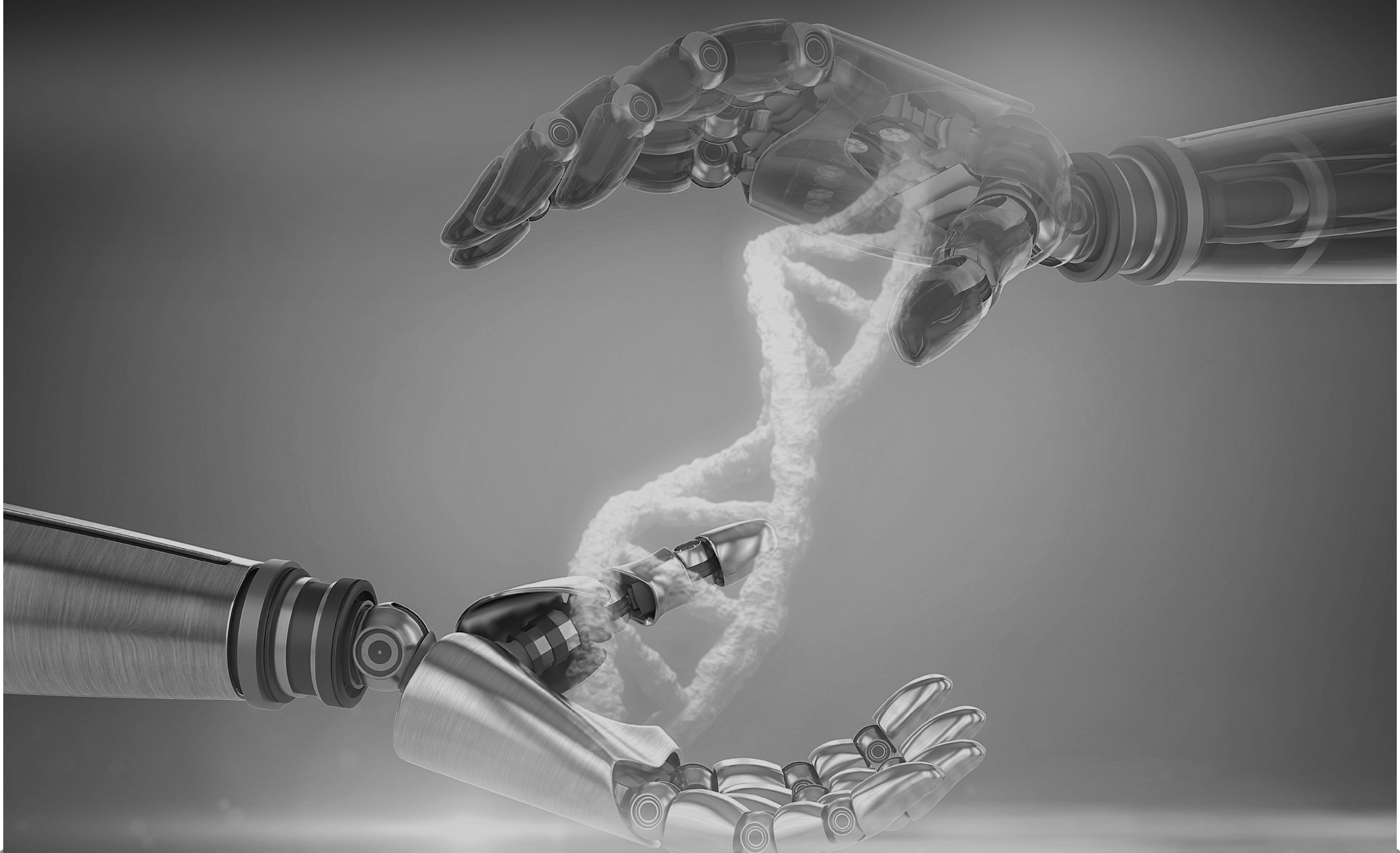
STOCKS DOWN UNDER

11 JANUARY 2022

Emerging Stocks Down Under

I made a fortune getting out too soon.

- J.P. Morgan (1837 - 1913), American financier and banker



ZOOM2U TECHNOLOGIES
Zooming on all cylinders

RESAPP HEALTH
The goal is in sight

NOVA EYE MEDICAL
Shedding losses like a snake sheds skin

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Stocks Down Under rating: ★★★★

ASX: Z2U
Market cap: A$66.7M

52-week range: A$0.33 / A$0.835
Share price: A$0.385

If you think couriers are just for Business to Business (B2B), Zoom2u's performance in COVID-19 has proved you dead wrong. Headquartered in Sydney, Zoom2u was originally founded as a courier service but has grown to include Locate2u, Shred2u and 2uEnterprises. This company experienced sharp revenue growth in both FY20 and FY21. With $7.8m in cash, and a 55.6% increase in 1Q22 revenue compared to 4Q21, we think Zoom2u will keep on zooming.

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ASX: RAP
Market cap: A$53.3M

52-week range: A$0.04 / A$0.103
Share price: A$0.06

Brisbane-based ResApp Health's stock had a crazy ride in 2021, with the stock going through four significant price increases, followed by sharp price collapses. This should come as no surprise, since the company encompasses two of the most volatile industries on the ASX: healthcare and software development. This company is in the process of developing and gaining regulatory approval for three smartphone-based medical diagnosis applications.

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Adelaide-based Nova Eye Medical has recently undergone a significant transformation, divesting a large part of its business and changing its name. Sure, total revenue has declined compared to the pre-divestment situation, but the company reduced its EBITDA loss by 42.5% in FY21. Now that Nova is more focused, the company has made a number of advancements in its two core focuses, glaucoma and AMD. Considering that the entire company is valued at just under $60m, we believe this progress is worth a punt.

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Share price chart

Source: Tradingview

A lot has changed, but the focus remains the same

Zoom2u was founded in 2014 by CEO Steve Orenstein as a courier service after he found inefficiencies in what is now his competition. The company has changed a lot since it was first launched, going from a majority small customer-based revenue business to focusing on larger enterprise customers. The company has also expanded its offerings to include VIP, 3-hour, same day, interstate and large freight delivery services.

Let's dive into the transition to larger enterprise customers a little more, but first we need to explain 'Gross Marketplace Value (GMV)'. To put it simply, GMV is the total price of all deliveries after accounting for cancellations and fees paid to Zoom2u, and after removing GST. It is important to remember that GMV will always be higher than revenue, which only accounts for fees directly paid to Zoom2u. In other words, GMV gives more insights into Zoom2u's customer base than revenue will.

We already said Zoom2u started with a focus on small customers, and that was no exaggeration. In FY15 (first year of operations), Zoom2u generated 80% of its revenue from customers with a GMV of less than $1,000 annually. By FY18, this had been reduced to 27% of its customers, and by FY21 it was only 22%. In FY21, 21% of customers had a GMV between $1,000 and $10,000, and 57% of customers had over $10,000 in GMV. This perfectly illustrates the changing customer dynamic of Zoom2u. It's no longer focused on Small and Medium Enterprises (SME) and individual consumers, although they still play an important part. The company now mostly caters to more demand stable enterprise customers and 1Q22 saw the company win some big customers.

Starting FY22 off with a bang

As of 1Q22, Zoom2u has over 18,000 active customers and 8,600 registered drivers, driving 156% revenue growth versus 4Q21 and 81% year-over-year ($5.7m). A large part of this growth was winning four major clients for Zoom2u: Bing Lee, Telstra, PricewaterhouseCoopers and 99 Bikes. The company's emerging division Locate2u also won its first enterprise customer, Amart Furniture. Locate2u is an all-in-one business delivery platform that helps companies track the vehicles it has on the road, deliveries and services in progress, general sharing of location, etc. This division is not yet a large part of Zoom2u's earnings, but in 1Q22, the company made a vertical acquisition that we believe will help the company expand operations outside of Zoom2u.

On 9 December 2021, Zoom announced it was acquiring Local Delivery Shopify App (yes, that's its name) for $880,000 in cash. With this app, based on the platform of Shopify (NYSE: SHOP), e-commerce businesses can allow customers to request a delivery date and time at checkout. The app is currently used by approximately 270 customers in North America, 50 in the United Kingdom and 60 in Australia and New Zealand, generating $145,000 in Annual Recurring Revenue (ARR). The Local Delivery acquisition provides an up-sell and cross-sell opportunity for Zoom2u's existing Locate2u and Zoom2u software products.

Valuation far below the company's velocity

Zoom2u is currently trading at a trailing 12-month EV/Revenue multiple of 7.7x. After its September 2021 IPO raised $8m, the company is fully cashed up ($7.8m as of 30 September 2021) and, in our view, is unlikely to dilute shareholders through a capital raise for at least the next year, but probably longer (barring an additional acquisition). With this risk off the table and with the company's main operation (courier service) firing on all cylinders, we believe Zoom2u's valuation is ripe for the picking. Despite Covid lockdowns being (we hope) gone for good in Australia, we believe the return to the office will provide Zoom2u more business in the future, not less. And that's without accounting for the company's three sidekick businesses, which show promise but have yet to prove themselves viable. It is clear to us that Zoom2u is zooming on all cylinders. Four stars.

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We feel the need, the need for ease

There have been many lessons to learn from the COVID-19 Pandemic, and with that Pandemic not over yet, there are surely a lot more to come. One of the more significant lessons was the value of technology in increasing efficiency, decreasing costs and providing greater availability of care in the field of medicine. And yet, for many like Associate Professor Udantha Abeyratne, this was far from a reason to stop the presses. You see, Professor Abyratne had founded ResApp in September 2014, intending to commercialise the technology he had developed that uses sound to diagnose respiratory disease. To fulfil that goal, ResApp was taken public in 2015 and has since focused entirely on using the advanced microphones in smartphones to diagnose different conditions based on the original sound-based technology.

Before we continue, it is important to note that ResApp is still pre-revenue. This is far from surprising when you consider the complexity of coding the base technology and how long it takes to receive regulatory approval.

There's an app for that

In 2009 Apple (NASDAQ: AAPL) first used the phrase now synonymous with the modern age of smartphones, "there's an app for that". If you ever questioned just how right Apple would become, look no further than ResApp's three main products under development to diagnose, test and track: sleep apnoea, Chronic Obstructive Pulmonary Disease (COPD) and Asthma, and respiratory disease.

The base technology behind ResApp was designed to listen to a patient's cough and breathing sounds in order to diagnose and measure a wide range of respiratory diseases, including pneumonia, asthma, bronchiolitis and COPD. Due to the power of modern smartphone microphones, the application works without the need for additional hardware. There is clearly a need for a system like this, as most doctors still use a stethoscope to listen to the lungs for indications of respiratory problems. Doctors are highly trained but limited by human biology and simple human error. This is one reason why ResApp's automated approach holds so much promise. Combine that with the fact that the application does not require physical contact with the patient, markedly improving safety and delverability, and you've potentially got a world-class device.

Sleep apnoea is a shockingly common sleep breathing disorder that affects approximately three in every ten men and two in every ten women. In a nutshell, the condition stops the airflow to a patient's lungs for ten seconds or longer during sleep, occurring over 30 times an hour in some extreme cases. And yet, many studies have reported as high as 80% of cases are undiagnosed. Using its sound diagnostic technology, ResApp is developing a smartphone application that can easily screen for sleep apnoea simply by monitoring a patient's breathing and snoring sounds overnight in the comfort of their own home. The application has gone through a 308-patient clinical study for Obstructive Sleep Apnoea (OSA is one type of sleep apnoea) and passed with flying colours. Compared to simultaneous at-home comprehensive sleep studies, the application correctly identified patients with OSA across the three AHI thresholds of 5/h, 15/h and 30/h, with a sensitivity of 85%, 83% and 83%, respectively.

More than enough volatility to go around

As we mentioned in our introduction, ResApp's stock has had intense volatility in 2021 due to a relatively constant stream of announcements. We would point out that these announcements have represented solid progress for the most part, and the pullbacks seem to be profit-taking after those announcements.

For a good example, consider the 29 November 2021 announcement. ResApp told the market that it had received Australian Therapeutics Good Administration (TGA) clearance and CE Mark certification of the cough counter smartphone application. This is the first time such an application has been regulatory-approved anywhere in the world. Thanks to these approvals, the application is now listed on the Australian Register of Therapeutic Goods (ARTG) and sold in Europe as a class I medical device. Another important announcement, released on 22 December 2021, told the market that ResApp had signed an agreement with Sanrai International to promote, market, and sell ResAppDx in the Middle East, South America, South Asia, Central America, and the Caribbean.

Yes, ResApp has more than its fair share of volatility, and at its pre-revenue stage of development, the company still has significant risks. However, we believe investors can finally see the light at the end of the tunnel of commercialisation, especially with the cough counter approval and the Sanrai agreement. With a wide range of potential markets for the current products under development (and that doesn't even include how the technology can be expanded), we believe a valuation of $53.3m makes ResApp well worth the risk given the potential upside. Four stars.

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Share price chart

Source: Tradingview

Like a snake changing its skin

For many, the snake can be a symbol of evil, but snakes don't have nearly that bad a reputation in the field of medicine. In fact, the international symbol for medicine is the Caduceus, a rod with two snakes wrapped around the shaft. These are the type of snakes we want you to keep in mind. And much like those snakes, Nova Eye Medical shedded its skin in 2020 when it divested its Ellex Laser and Ultrasound business, changed its name from Ellex Medical Lasers, and buckled down to focus on glaucoma and intermediate Age-Related Macular Degeneration (iAMD).

In our view this was the right call, as Nova Eye Medical's remaining operations are strong and have plenty of room for expansion. Out of the two focuses of the company, only the glaucoma division has products for sale. Nova Eye Medical's main product is iTrack, which uses 'microcatheters' – like regular catheters only tiny, measuring just 0.7mm and 1.3mm in diameter – to remove the need for stents in gluacoma treatment. The iTrack product does not limit future treatment options and it comes with insurance coverage in the US. After iTrack, Nova's second product is Molteno3, a glaucoma drainage device. It's a relatively recent addition to the portfolio, having been bought in July 2020. As with iTrack, Molteno3 is reimbursed in the US. It's proven to generate a long-term reduction in intraocular pressure in advanced or complex glaucoma cases.

Glaucoma is where the action is for Nova right now. iAMD is where Nova would like to become a player. iAMD is the leading cause of blindness in the developed world for people over 50 and currently there's no cure, with only vitamins and supplements really making any noticeable difference. Nova hopes to change all that with 2RT, a technology that has been in development since early 2000 and uses a nanosecond laser pulse and pixelated laser beam profile to slow the progress of AMD patients. A six-year study across 292 patients, from 2012 through to 2018, with follow-up in 2020, found 76% of patients had a 77% reduction in their progression to late-stage AMD. The study saw the patients undertake a 36-month course of 2RT treatment, with that benefit lasting for 24-months after treatment stopped. Nova Eye Medical is currently waiting for the United States Food and Drug Administration (FDA) to grant an Investigational Device Exemption Approval that would allow the company to progress 2RT to a pivotal United States study, one of the final major hurdles in the approval process.

Strategic cost-cutting and acquisitions are the way forward

In FY21, Nova generated $13.6m in revenue, 6.3% better than FY20. However, the real kicker was the company's cost-cutting strategy paying off, facilitating a 38.6% decline in the company's EBITDA loss to $3.5m.

Nova Eye Medical is expanding its product offerings through a combination of research and development and acquisitions. On 26 August 2021, the company announced it had acquired a glaucoma treatment patent portfolio from United States-based Innovative Glaucoma Solution for US$2m and 1,736,653 shares. While we were not provided with a significant amount of information, Nova Eye did say at the time that the portfolio will "facilitate the future introduction of new products and additional indications" and "the future products will address glaucoma patients with mid-stage disease". This important point explains Nova Eye Medical's interest in the patent portfolio as its current products, iTrack and Molteno3 address glaucoma's early and late stages, respectively. Therefore, the patent portfolio acquisition will speed up the process of Nova Eye Medical filling its mid-stage product gap considerably.

The name of the game is profitability

We believe management's restructuring plan was the right call, and FY21's results proved that it was the way towards profitability. Yes, Nova Eye Medical is not yet profitable, and the company only grew its revenue 6.3% in FY21, but it reduced its EBITDA loss 38.6% to $3.5m. So, while the trailing 12-month EV/Revenue multiple of 2.6x might seem high based on 6.3% growth, we believe the company is likely only a few years away from finally crossing into EBITDA profitability. Therefore, when we combine the success of 2RT in its moves towards approval in the United States with the light of profitability finally visible, we believe 2.6x is a fair valuation. Four stars.

Pitt Street Research Pty Ltd

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