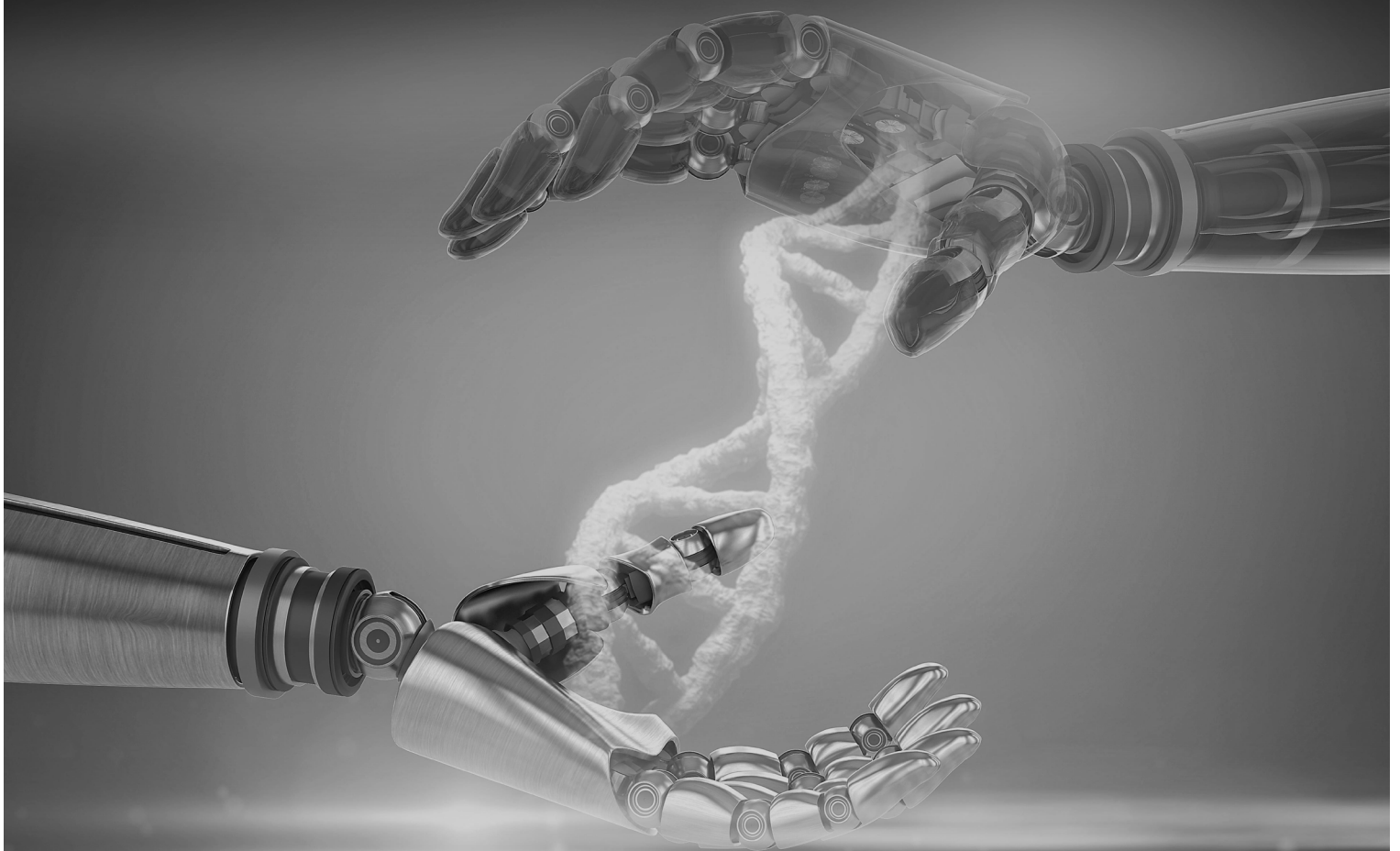




Emerging Stocks Down Under

“ In 20 years’ time, I want to look back and be realistic, and know that I have truly made a serious contribution. ”

- Fiona Wood (b. 1958), surgeon, Recell creator & 2005 Australian of the Year



AVITA MEDICAL

The ASX's other burns treatment company

AVITA MEDICAL

The ASX's other burns treatment company

Stocks Down Under rating: ★★☆☆

ASX: AVH

Market cap: A\$210.1M

52-week range: A\$1.48 / \$5.89

Share price: A\$

In 2005, the Australian of the Year award went to Professor Fiona Wood for her contribution to medicine. Just over two years earlier, her burns treatment technology saved 25 lives in the aftermath of the Bali bombings. But it took more than a decade for the FDA to take notice and approve it for use in the USA. And even now, shareholders would be forgiven for thinking the company should be further ahead than it is now.

Share price chart



Source: Tradingview

Spray-on skin

Avita's technology is known as Recell. It is a rapid cell harvesting device that enables surgeons to treat skin defects using a patient's own cells. It works as a 'spray-on' product, which can be done at the point of treatment and with a small quantity of cells. A doctor takes a biopsy on any part of the body and mixes the cells into a liquid spray. It's ready for use in 30 minutes and can cover 80 times the area of a skin graft with the same amount of material an 'ordinary' skin graft would.

Fiona Wood first used the technology in the 1990s, but it took until the Bali bombings for people to take notice. Despite winning approval in over a dozen jurisdictions between 2008 and 2018, it took until FDA approval in September 2018 and US market entry for the shares to begin taking off. Avita's initial focus was in-patient burns, but the company is also looking to other markets including out-patient burns, soft tissue reconstruction, car accidents, paediatric scalds, vitiligo (yes, the same condition that affected Michael Jackson) and skin rejuvenation markets.

A Corona Crash that has dragged on for two years

After the Corona Crash, Avita's share price has never recovered and has retreated since March 2020. Why? We think there are four reasons. First, Avita's ambitions to enter markets for other conditions are still a work in progress. Second, since it listed on the Nasdaq and made Wall Street its primary listing, we think there are

perceptions by Australian investors that the business is walking away from its Australian listing. We think the company's recent roadshow in Australia illustrates talk of its demise might have been exaggerated. We also think the fact that Australian investors still account for 60% of trading in the stock shows it would be against Avita's interests to delist from the ASX.

Third, progress has been slower than investors would have expected. People staying at home and hospitals over-run with COVID patients meant less people suffering burns, fewer opportunities for face-to-face sales meetings by company executives and elective surgery (including for many conditions Avita is aspiring to target) being postponed. And fourth, Avita is not expected to reach positive EBITDA until FY25 according to consensus estimates. As we've noted in several previous editions of late, the market has gone bearish on companies that are not profitable or at least close to it. Also remember that last week [we covered Polynovo \(ASX: PNV\)](#), which has exposure to more markets at present and has regulatory approvals as well as positive EBITDA expected sooner.

Investors know there are opportunities, but not how big they are

If you buy into Avita Medical now, what do you have to look forward to? Avita hopes to expand into soft tissue reconstruction and vitiligo in the second half of 2023 following anticipated FDA approval. It is in the middle of a pivotal trial for both. We think investors have been disregarding the size of these opportunities. These are not just a mere 10-20% expansion of its existing markets - vitiligo is 4 times larger than burns while soft tissue reconstruction is twice as large. We also think investors are disregarding two benefits its establishment in the burns market will do. First, it will make it easier to establish a presence in these markets and second, it provides cash flows in the interim to avoid the need for dilutive capital raisings.

We acknowledge it is difficult to follow this company's financials because Avita is moving its fiscal year to the calendar year. It reported full year results from 1 July 2020 to 30 June 2021, then reported results for a transitional period 1 July 2021 to 31 December 2021 and made the calendar year pivot effective from 1 January 2022. Although it has not issued formal guidance for CY22, consensus estimates predict US\$32m in revenue and -/US\$36.9m in EBITDA.

For CY23, Avita is forecast to achieve US\$44.1m in revenue (up 38%) and -/US\$32.7m in EBITDA (a 12% improvement). For CY24, the market expects US\$66.5m in revenue (up 51%) and -/US\$18.1m in EBITDA (a 44% improvement). Finally, in CY25, US\$99.6m is expected in revenue (up 50%) and \$0.06 in EPS (EBITDA has not been calculated). Its P/E for FY25 is 18.9x, while its EV/Sales is 1.5x for CY22 and 1.1x for CY23.

When we last covered Avita Medical - [in June 2020](#) - we gave it two stars purely on valuation grounds. At the time it was 21x forecast revenue and capitalised at A\$928m. Is it better now? At under 2x forecast revenue and capitalised at under A\$200m, we actually think the stock is now undervalued. You could make the case that it would be better to be invested in Polynovo (ASX: PNV) given it will be profitable and activate in more target markets sooner. But Avita is not too far behind - it expects to complete its two clinical trials in the 2nd half of CY22 and to have FDA approval within 12 months thereafter.

Assuming Avita can capitalise on these opportunities, it's four stars in our book. Although we cannot assume its success with certainty, we can have higher confidence with Avita Medical because it has already proven itself in the US market.

Pitt Street Research Pty Ltd

3 Spring Street, Sydney, NSW 2000, Australia

Stocks Down Under gives you an information advantage to better invest and trade in ASX-listed stocks!

Stocks Down Under (Pitt Street Research AFSL 1265112) provides actionable investment ideas on ASX-listed stocks. The Content is financial advice but is not (and cannot be construed or relied upon as) personal financial advice. No investment objectives, financial circumstances or needs of any individual have been taken into consideration in the preparation of the Content. Please make sure that investing in such products is suitable for your circumstances, and ensure you obtain, read and understand any applicable offer document.

Financial products are complex, entail risk of loss, may rise and fall, and are impacted by a range of unpredictable market and economic factors.

All rights reserved. No part of this publication may be reproduced or transmitted in any form or by any means, electronic, mechanical, photocopying, recording or otherwise, without prior written permission from Pitt Street Research Ltd Pty. All intellectual property relating to the Content vests with Pitt Street Research/ Stocks Down Under unless otherwise noted.

Stocks Down Under/Pitt Street Research directors and staff may own shares in the companies mentioned in our articles, videos, reports and analyses.

You are receiving this email because you subscribed to our newsletter.

