



19 February 2010

**AtCor Medical Holdings Limited (ACG)**

Speculative Buy

Average 1H, But CP Thematic Growing in Strength

\$0.165

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Per recent guidance, 1H10 NPAT loss was \$1.2m, down significantly on pcp (NPAT of \$0.2m).

Impacted by softer 1H product sales (down 18.2% on pcp, 13% on pcp in constant currency) and FX.

Gross margin of 90.1% was impressive, up 748bps on pcp.

Re-payment of all outstanding director loans of \$0.8m in the 2Q, with closing cash of \$1.9m.

**Summary**

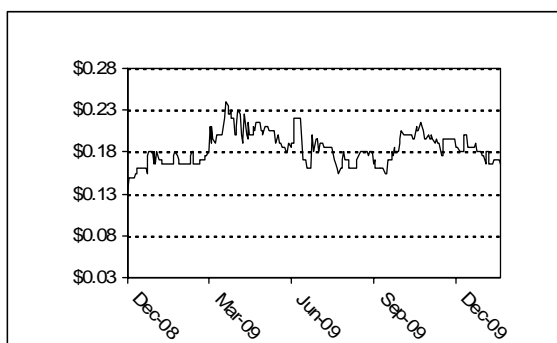
Market capitalisation (M)	\$16.6
Share price	\$0.165
Price target	\$0.43
52 week low	\$0.16
52 week high	\$0.24
Ave Monthly Vol (M)	1.871
Cash as at 31/12/09 (M)	\$2.0
NTA per share	\$0.06

**Our View**

- Average 1H, Impacted by Pharma Clinical Delays, European Decline and FX** – Per the update late Jan, the 1H result was impacted by the delay in one large pharma which is likely to be signed this month. Further, European sales were poor relative to pcp, with a 36% decline though pcp sales did benefit from one large pharma order. Asia Pacific (APAC) sales were up 20% on pcp, which was a reasonable result given Asian sales are mostly US\$ denominated. Improvement in Europe was observed late in the 1H and the Company anticipates large ex-pharma orders in the US and APAC.
- Significant Gross Margin Expansion, US Clinician Sales the Highlights** – Margins were positively impacted through a higher component of service income to clinical trial sales, COGS improvements and product mix. We do not consider this level of GM to be repeatable in the 2H, but anticipate >85% gross margins through to FY12. Sales to clinical practices in the US rose 59% on pcp, albeit off small base in our view. This sales channel is important for US national reimbursement coverage in the US, as “widespread” clinician use represents a key tenet for successful applications. We believe the growth may also be attributable to traction relating to state-based coverage in the US continuing to expand and strong outcome data. We remain hopeful the Company will file for CPT 1 coding this November.
- Expansion of Clinical Indications Apparent** – The applicability of SphygmoCor® as a predictive and monitoring tool for pre-eclampsia continues to grow, with a recent 70 patient study examining drug effects noting the benefit to arterial stiffness in a statistically significant manner. A follow up from the 2,585 Strong Heart study found central BP to be a superior predictor of left ventricular hypertrophy (major risk factor for heart failure/attack and stroke) v brachial measures alone.
- Outlook** – Mgt have re-affirmed double digit sales growth in the 2H, though have downgraded FY sales guidance from “double digit” to “FY10 sales in constant currency expected to exceed FY09”. On this basis, the stock trades on forward EV/Sales of 1.4x. We have downgraded our sales expectations to -2.6% on pcp and have increased our FY10 NPAT loss to \$1.6m (\$0.8m previous). We have revised down our FY11 and FY12 EPS estimates by 30.6% and 9.8%, respectively and our blended valuation and price target drops by 11cps to \$0.43. Despite the sluggishness of the 1H result, we are confident in the broader thematic of central pressures in cardiovascular disease management and maintain our Speculative Buy recommendation.

**Key Financials (A\$'000)**

Year End	1H10	2010	2011
	Actual	Est.	Est.
Product Sales	4,384	10,920	16,588
<b>Total Revenue</b>	<b>4,719</b>	<b>11,596</b>	<b>16,655</b>
<b>COGS</b>	<b>(432)</b>	<b>(1,430)</b>	<b>(2,306)</b>
Net Op. Rev	(1,113)	(1,415)	3,205
<b>EBITDA</b>	<b>(1,146)</b>	<b>(1,489)</b>	<b>3,139</b>
EBIT	(1,210)	(1,624)	3,001
<b>Reported Profit</b>	<b>(1,177)</b>	<b>(1,550)</b>	<b>3,067</b>
<b>Reported EPS (c)</b>	<b>(1.2)</b>	<b>(1.5)</b>	<b>3.1</b>
<b>PE Ratio (x)</b>	<b>n/a</b>	<b>n/a</b>	<b>5.4</b>
<b>ROE (%)</b>	<b>n/a</b>	<b>-40.1%</b>	<b>66.3%</b>

**Share Price Graph (A\$)**

## 1H Results Summary

Reported 1H10 NPAT loss of \$1.2m.

Impressive gross margins of 90.1%.

AtCor Medical has reported a disappointing 1H10 NPAT loss of \$1.2m, a major turnaround from a 1H09 profit of \$0.2m. While expenses in A\$ terms were flat and gross margins increased 748bps to an impressive 90.1%, this was not sufficient to compensate for the deterioration in market conditions, particularly in Europe. The result was also impacted by a delay in a major pharmaceutical contract which had been expected in the 1H and FX headwinds owing to a stronger A\$ on majority US\$ denominated sales. The result summary is shown below.

### 1H10 Results Summary

	1H10A	TC est.*	% difference	Comment
<b>Product Sales</b>	<b>4.4</b>	<b>6.2</b>	<b>41.4%</b>	Delays in major pharma orders, weak European 1H
Total Revenues	4.7	6.5	37.7%	Minor contribution from Aust. Govt grant to FY10
Marketing and Sales Expense	(3.0)	(2.1)	-31.1%	Sales drive into clinician practices, new market entries
Product Dev & Clinical Expense	(0.9)	(2.8)	224.1%	Lower than estimates as several clinical studies delayed
Administration Expense	(1.2)	(1.0)	-18.4%	
<b>EBITDA</b>	<b>(1.1)</b>	<b>(0.5)</b>	<b>-56.4%</b>	Anticipate recovery in 2H
EBIT	(1.2)	(0.5)	-58.7%	D&A expected to remain v.low
<b>NPAT</b>	<b>(1.2)</b>	<b>(0.5)</b>	<b>-57.5%</b>	Impacted by delays in pharma trial contracts, FX loss of \$0.2m v \$0.6m gain in pcp

\* Prior to Company update on Jan 28th; Source: Taylor Collison

Net cash outflow for the 1H of \$1.3m.

The Company recorded net cash outflow for the 1H of \$1.3m, which benefited from a \$0.8m re-payment by a former director of an outstanding loan obligation. All director loans have been repaid at balance date. Closing cash of just \$1.9m is concerning; however we are forecasting a much narrower net cash flow burn in the 2H owing to large pharma clinical trial orders, which typically results in a significant upfront cash component and revenue recognition over the course of the trial.

GM benefited from product mix, lower COGS and product re-certs.

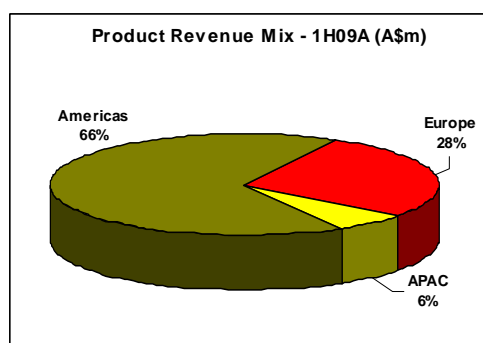
Gross margin expansion was one of two key positives to take out of the result (the other being growth in US clinician sales of 59% on pcp). As shown below, margins grew by 748bps in the 1H, via a combination of higher service income in overall product revenues, improvements in COGS and product mix such as higher value software bolt-on and product re-certifications.

\$ million	1H09A	1H10A	Change
<b>Product Sales</b>	5.4	4.4	
<i>pcp growth (%)</i>	<i>75.8%</i>	<i>-18.5%</i>	
<b>Gross Margin</b>	82.7%	90.1%	+748 bps

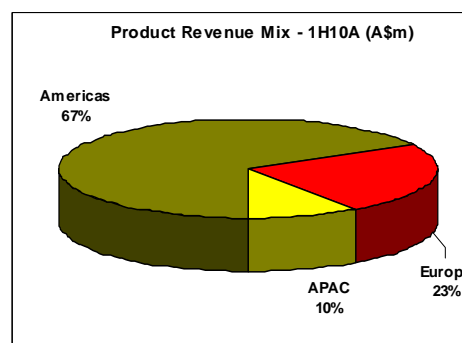
Source: Company report

The contribution of major geographical segments to product revenues is shown below. Excluding service income of \$0.8m (which was +8% on pcp) given it is predominately associated with pharmaceutical contracts originating in the US, we note the segment contribution becomes: Americas 67%, Europe 23% and APAC 10%.

Americas (US) dominates global sales.



Source: Company report, Taylor Collison



Source: Company report, Taylor Collison

While management indicated tight control over costs resulted in a slight decrease in operating expenses for the 1H (see below) we also note the FX tailwind to costs given the majority of marketing and sales (>90%) is US\$/EUR denominated. Product development and clinical trials (formally regulatory) are largely A\$ denominated.

*Expenses were flat v pcp.*

\$ million	1H09A	1H10A	Change
Marketing and Sales	(3.1)	(3.0)	-2.7%
Product Devt & Clinical Trial	(1.0)	(0.9)	-10.3%
Administration	(1.1)	(1.2)	7.8%
Other	(0.0)	(0.1)	89.2%
<b>TOTAL</b>	<b>(5.3)</b>	<b>(5.2)</b>	<b>-1.2%</b>

Source: Company report

## Outlook

*Revised sales guidance downwards.*

Mgt have re-affirmed double digit sales growth in the 2H, though have downgraded FY sales guidance from “double digit” to “FY10 sales in constant currency expected to exceed FY09”. We partially attribute this assessment on the contracting delays which may have caught mgt by surprise and represent a tighter level of cost control and diligence by pharmaceutical companies. Should this be a recurring thematic, it may make internal Company forecasting more challenging. However, investors should note as a capital equipment provider to the global pharmaceutical market, sales are expected to be lumpy. We anticipate a smoother revenue outlook from FY12 onwards, commensurate with a jump clinician sales post reimbursement.

Changes to our forecasts for FY10-FY12 are shown below.

### Changes to Forecasts

	FY10E			FY11E			FY12E		
	Previous	Revised	Change	Previous	Revised	Change	Previous	Revised	Change
Product Sales (\$m)	12.8	10.9	-14.7%	18.7	16.6	-11.3%	23.5	22.0	-6.5%
EBITDA (\$m)	(0.7)	(1.5)	124.9%	4.4	3.1	-29.0%	7.7	7.0	-9.4%
EBIT (\$m)	(0.8)	(1.6)	103.8%	4.3	3.0	-29.6%	7.5	6.8	-9.0%
NPAT (\$m)	(0.8)	(1.6)	100.1%	4.4	3.1	-29.5%	7.8	7.1	-9.4%
EPS (c)	(1.7)	(1.5)	-9.2%	4.4	3.1	-30.6%	7.8	7.0	-9.8%

Source: Taylor Collison estimates

*Maintain Speculative Buy, PT \$0.43.*

The stock currently trades on forward EV/Sales of 1.4x. We have downgraded our expectations to negligible FY revenue growth and have increased our FY10 NPAT loss to \$1.6m (\$0.8m previous). We have revised down our FY11 and FY12 EPS estimates by 30.6% and 9.8%, respectively and our blended valuation and price target drops by 11cps to \$0.43. Despite the sluggishness of the 1H result, we are confident in the broader thematic of central pressures in cardiovascular disease management and maintain our Speculative Buy recommendation.

## ACG - Summary of Forecasts

ACG \$ 0.17

PROFIT & LOSS SUMMARY (A\$000s)							
Period	FY08A	1H09A	FY09A	1H10A	FY10E	FY11E	FY12E
Product Sales	6,451	5,377	11,209	4,384	10,920	16,588	21,965
growth (%)	32.8%	75.8%	73.8%	-18.5%	-2.6%	38.0%	32.0%
<b>Total Revenue</b>	<b>7,363</b>	<b>6,507</b>	<b>12,400</b>	<b>4,719</b>	<b>11,596</b>	<b>16,655</b>	<b>22,210</b>
Cost of Goods Sold	(1,286)	(932)	(1,740)	(432)	(1,430)	(2,306)	(3,097)
Gross Margin	80.1%	82.7%	84.5%	90.1%	86.9%	86.1%	85.9%
<b>Total Operating Expenses</b>	<b>(10,942)</b>	<b>(6,203)</b>	<b>(13,908)</b>	<b>(5,832)</b>	<b>(13,011)</b>	<b>(13,450)</b>	<b>(14,989)</b>
<b>Net Operating Revenue</b>	<b>(3,579)</b>	<b>304</b>	<b>(1,508)</b>	<b>(1,113)</b>	<b>(1,415)</b>	<b>3,205</b>	<b>7,221</b>
Direct R&D Expenses	0	0	0	0	0	0	0
<b>EBITDA</b>	<b>(3,997)</b>	<b>140</b>	<b>(1,750)</b>	<b>(1,146)</b>	<b>(1,489)</b>	<b>3,139</b>	<b>6,976</b>
Dep'n/Other Amort'n	(148)	(87)	(176)	(64)	(135)	(137)	(155)
<b>EBIT</b>	<b>(4,145)</b>	<b>53</b>	<b>(1,926)</b>	<b>(1,210)</b>	<b>(1,624)</b>	<b>3,001</b>	<b>6,822</b>
Net Interest	418	164	242	33	74	66	245
<b>Pre-Tax Profit</b>	<b>(3,727)</b>	<b>217</b>	<b>(1,684)</b>	<b>(1,177)</b>	<b>(1,550)</b>	<b>3,067</b>	<b>7,066</b>
Tax Expense	(66)	(37)	(7)	0	0	0	0
Minorities	0	0	0	0	0	0	0
<b>NPAT Normalised*</b>	<b>(3,635)</b>	<b>(425)</b>	<b>(1,946)</b>	<b>(985)</b>	<b>(1,358)</b>	<b>3,067</b>	<b>7,066</b>
<b>NPAT</b>	<b>(3,793)</b>	<b>180</b>	<b>(1,691)</b>	<b>(1,177)</b>	<b>(1,550)</b>	<b>3,067</b>	<b>7,066</b>
Growth (pcp)	26.8%	110.7%	55.4%	n/a	8.3%	n/a	130.4%
Net Abnormals	0	0	0	0	0	0	0
<b>Reported Profit</b>	<b>(3,793)</b>	<b>180</b>	<b>(1,691)</b>	<b>(1,177)</b>	<b>(1,550)</b>	<b>3,067</b>	<b>7,066</b>

PER SHARE DATA							
Period	FY08A	1H09A	FY09A	1H10A	FY10E	FY11E	FY12E
<b>Reported EPS (c)</b>	<b>(3.8)</b>	<b>0.2</b>	<b>(1.7)</b>	<b>(1.2)</b>	<b>(1.5)</b>	<b>3.1</b>	<b>7.0</b>
Growth (pcp)	-26.8%	-110.7%	55.4%	n/a	8.7%	n/a	130.4%
<b>EPS Normalised (c)</b>	<b>(3.6)</b>	<b>(0.4)</b>	<b>(1.9)</b>	<b>(1.0)</b>	<b>(1.4)</b>	<b>3.1</b>	<b>7.0</b>
Growth (pcp)	-32.6%	-78.7%	46.5%	131.8%	30.5%	n/a	130.4%
Dividend (c)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Franking	0%	0%	0%	0%	0%	0%	0%
Gross CF per Share (c)	(3.5)	(0.7)	0.1	(1.3)	(1.3)	2.5	7.5
NTA per share (c)	5.7	5.9	4.5	3.6	3.0	6.0	13.1

KEY RATIOS							
Period	FY08A	1H09A	FY09A	1H10A	FY10E	FY11E	FY12E
EBITDA/Sales Margin %	-54.3%	2.2%	-14.1%	-24.3%	-12.8%	18.8%	31.4%
EBIT/Sales Margin %	-56.3%	0.8%	-15.5%	-25.6%	-14.0%	18.0%	30.7%
Current ratio (x)	2.9	3.3	2.3	2.7	2.1	2.9	4.0
Net Debt : Equity (%)	-55.6%	-47.9%	-73.5%	-53.2%	-58.6%	-67.6%	-83.4%
ROE (%)	-49.4%	n/a	-31.9%	n/a	-40.1%	66.3%	72.9%
Dividend Payout Ratio (%)	n/a	n/a	n/a	n/a	0.0%	0.0%	0.0%

VALUATION MULTIPLES							
Period	FY08A	1H09A	FY09A	1H10A	FY10E	FY11E	FY12E
PE Ratio (x)	n/a	n/a	n/a	n/a	n/a	5.4	2.3
Dividend Yield (%)	n/a	n/a	0.0%	n/a	0.0%	0.0%	0.0%
EV/Sales (x)	2.1	n/a	1.2	n/a	1.4	0.7	0.3
EV/EBITDA (x)	n/a	n/a	n/a	n/a	n/a	4.0	0.8
EV/EBIT (x)	n/a	n/a	n/a	n/a	n/a	4.1	0.8

CAPITAL RAISING ASSUMPTIONS							
Period	FY08A	1H09A	FY09A	1H10A	FY10E	FY11E	FY12E
Shares Issued (m)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Issue Price (A\$)	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Cash Raised (A\$m)	0.0	0.0	0.0	0.0	0.0	0.0	0.0

\* Excluding FX gains/losses

BALANCE SHEET SUMMARY							
Period	FY08A	1H09A	FY09A	1H10A	FY10E	FY11E	FY12E
Cash	3,316	2,924	3,416	1,972	1,814	4,167	11,036
Receivables	1,877	4,195	3,382	2,570	2,621	3,318	4,393
Pre Payments	0	0	0	0	0	0	0
Inventories	401	649	434	459	437	995	1,318
Investments	0	0	0	0	0	0	0
Other	100	159	139	170	170	170	170
<b>Total Current Assets</b>	<b>5,694</b>	<b>7,927</b>	<b>7,371</b>	<b>5,171</b>	<b>5,041</b>	<b>8,650</b>	<b>16,917</b>
Investments	0	0	0	0	0	0	0
Inventories	0	0	0	0	0	0	0
Receivables	1,684	0	0	0	0	0	0
Property Plant & Equip	350	368	352	308	373	471	512
Intangibles	222	200	177	154	133	89	45
Other	0	0	0	0	0	0	0
<b>Total Non-Current Assets</b>	<b>2,256</b>	<b>568</b>	<b>529</b>	<b>462</b>	<b>506</b>	<b>560</b>	<b>557</b>
<b>TOTAL ASSETS</b>	<b>7,950</b>	<b>8,495</b>	<b>7,900</b>	<b>5,633</b>	<b>5,547</b>	<b>9,209</b>	<b>17,474</b>
Accounts Payable	1,953	2,351	3,223	1,900	2,402	2,986	4,173
Borrowings	0	0	0	0	0	0	0
Provisions	19	20	4	0	22	33	44
Other	0	0	0	0	0	0	0
<b>Total Current Liab</b>	<b>1,972</b>	<b>2,371</b>	<b>3,227</b>	<b>1,900</b>	<b>2,424</b>	<b>3,019</b>	<b>4,217</b>
Borrowings	0	0	0	0	0	0	0
Provisions	17	20	28	28	28	28	28
Other	0	0	0	0	0	0	0
<b>Total Non-Current Liab</b>	<b>17</b>	<b>20</b>	<b>28</b>	<b>28</b>	<b>28</b>	<b>28</b>	<b>28</b>
<b>TOTAL LIABILITIES</b>	<b>1,989</b>	<b>2,391</b>	<b>3,255</b>	<b>1,928</b>	<b>2,452</b>	<b>3,047</b>	<b>4,245</b>
<b>TOTAL EQUITY</b>	<b>5,961</b>	<b>6,104</b>	<b>4,645</b>	<b>3,705</b>	<b>3,095</b>	<b>6,162</b>	<b>13,229</b>

CASH FLOW SUMMARY							
Period	FY08A	1H09A	FY09A	1H10A	FY10E	FY11E	FY12E
<b>EBIT (excl Abs/Extr)</b>	<b>(4,145)</b>	<b>53</b>	<b>(1,926)</b>	<b>(1,210)</b>	<b>(1,624)</b>	<b>3,001</b>	<b>6,822</b>
Add: Depreciation	102	65	131	52	102	108	137
Amortisation	46	22	45	12	33	29	18
Change in Pay.	(32)	398	1,270	(1,323)	(821)	584	1,187
Less: Tax paid	(66)	(37)	0	0	0	0	0
Net Interest	418	164	242	33	74	66	245
Change in Rec.	(287)	(634)	179	812	761	(697)	(1,078)
Change in Inv.	(18)	(248)	(33)	(25)	(3)	(559)	(323)
Other	504	(434)	163	340	155	(20)	565
<b>Gross Cashflows</b>	<b>(3,478)</b>	<b>(651)</b>	<b>71</b>	<b>(1,309)</b>	<b>(1,322)</b>	<b>2,513</b>	<b>7,572</b>
Capex	(168)	(82)	(132)	(15)	(160)	(160)	(200)
<b>Free Cashflows</b>	<b>(3,646)</b>	<b>(733)</b>	<b>(61)</b>	<b>(1,324)</b>	<b>(1,482)</b>	<b>2,353</b>	<b>7,372</b>
Dividends Paid	0	0	0	0	0	0	0
Exchange Rate Adjustments	(37)	341	161	(120)	(120)	0	0
<b>Net Cash Flow</b>	<b>(3,683)</b>	<b>(392)</b>	<b>100</b>	<b>(1,444)</b>	<b>(1,602)</b>	<b>2,353</b>	<b>7,372</b>

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