



# Biotech Daily

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*Daily news on ASX-listed biotechnology companies*

## Dr Boreham's Crucible: Pro Medicus

**By TIM BOREHAM**

**ASX code:** PME

**Share price:** \$151.49

**Shares on issue:** 104,424,882

**Market cap:** \$15.82 billion

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

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

**Financials (year to June 30, 2024):** revenue \$161.5 million (up 29%), net profit \$82.8 million (up 36.5%), earnings per share 79.1 cents (up 36%), cash and investments \$155.5 million (up 28%)

**Identifiable major shareholders:** Dr Sam Hupert 24.07%, Anthony Hall 24.11%

The home-grown, giant-killing radiology software outfit is proving that its technologies are suitable for more than just the 'sandstone' academic hospital institutions from which it first gained its foothold in the US market.

All up, in the year to June 30, 2024 the company won nine new contracts with a total contract value of \$245 million. This includes the biggest to date, the Dallas, Texas based integrated delivery network (IDN) Baylor, Scott and White Health.

A recent omnibus of five contract wins was notable not just for the value - a collective combined minimum of \$45 million - but for the varied nature of the clients. These included paediatric hospitals in Ohio and Florida, private radiology chains and Florida's Moffitt Cancer Centre.

The jobs are characterized by software-as-a-service (annuity) revenue based on minimum transaction levels.

Despite chatter that the company is priced to perfection, Pro Medicus shares soared 13 percent in the two trading days after the August 14 disclosure of a 36 percent full-year profit surge, to \$82.79 million.

CEO and co-founder Dr Sam Hupert describes a "record year in all metrics, not just revenue and profit but also in terms of new sales and completed implementations".

He says the company's products are proving suitable for "virtually all segments of the market" from smaller groups to some of the largest IDNs and academic medical centres.

"It has been the most successful year in the company's history on all fronts," he chimes.

### **Coming from the clouds**

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

Rather like cloud-based, book-keeping pioneer Xero, Pro Medicus claims to be the only genuine internet-based provider, in a profession that still likes its pencils and clipboards.

The company was founded by Melbourne general practitioner Dr Hupert and his technologist friend Anthony Hall in 1983. Back then clouds came in three key varieties: cirrus, cumulus and stratus.

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.

### **Not the America's Cup, but better**

At the height of the global financial crisis, Pro Medicus acquired the California-based Visage Imaging for a knock-down \$5 million.

It was the company's 'Alan Bond' moment (a reference to Kerry Packer buying back his Nine Network from the failed Perth mogul for a knock-down sum).

The purchase price was quickly validated, because Pro Medicus shed Visage Imaging's unwanted research arm shortly after for \$15 million.

Dr Hupert says the company was in the right place at the right time. (But you make your own luck, don't you?)

## **Size counts**

A key driver for the company is the burgeoning need for more data capacity for imaging procedures.

For example, 300 megabytes used to be adequate for a mammography, but today, a high-definition version needs eight to 10 gigabytes per study. The same goes for a full-body positron emission tomography (PET) scan, while a high-definition, multi-slice computed tomography (CT) scan might require more than 10,000 images.

Traditionally, a scan produces a file which is compressed and sent to a highly-configured work station, where the image is enhanced and manipulated.

"The trouble is that the files are getting too big and it takes too long to open them and do the manipulation locally," Dr Hupert says.

"Our model allows the files to go to a single back-end server. All of the sophisticated enhancements are done in real time and the pixels are streamed to the radiologist or clinician.

"The two huge advantages are that it is instant - one second or less - and the radiologist's work station doesn't have to be highly configured. When you have hundreds or thousands of these screens, it is a huge cost saving."

## **Finances and performance**

Last week's full-year numbers show the company is on a roll, with revenue increasing 29.3 percent to \$161.5 million.

It wasn't profitless growth either, with earnings up 36 percent in both net profit (to \$82.8 million) and diluted earnings per share terms (79.1 cents per share).

"We have contained our cost base so margins have grown further from last year as our footprint increases," Dr Hupert says.

The company cites forward revenue of \$608 million over five years.

"Most contracts are delivered as software-as-a-service, with minimum amounts," Dr Hupert says.

Investors were rewarded with a 22 cents a share final dividend, up 33 percent, although suffice to say they are unlikely to be in the stock just for the paltry yield.

Of the revenue, 85 percent derived from the US. North American turnover rose 34 percent, while Australian revenue gained a more sedate 5.9 percent. European revenue declined seven percent, if only because of a chunky German sale in the previous period.

The company has cash (and financial investments) of \$155 million and no debt.

Over the last 12 months Pro Medicus shares have ranged between \$70.80 (mid-August last year) and the August 16, 2024 peak of \$150.67.

Five years ago, the shares were worth \$26 and ten years ago they could be bought for less than a dollar (these days, a dollar won't even buy a dim sim).

Last November, Dr Hupert and Mr Hall both sold one million shares - approximately four percent of their personal holdings - at \$88 apiece in response to an approach from an individual fund.

At the time they said they did not intend to sell any more shares "in the foreseeable future".

In March this year the stock was elevated to the ASX100 index.

## **Coming up**

Dr Hupert cites an increasing flow of requests for proposals, overwhelmingly for cloud-based upgrades often mandated by health regulators.

"We believe we are one of the few companies - if not the only one - that can provide a true cloud-based implementation of scale," he says.

The company has a long-standing interest in expanding into the 'ologies', with a cardiology extension product in development.

Dr Hupert says Pro Medicus is close to a cardiology "version 1.0", but there are nuances involved over and above the quality of the actual imaging (such as reporting requirements).

Following US Food and Drug Administration approval, Pro Medicus last year commercialized an algorithm to measure breast density, the problem being that 'dense' breasts are harder to scan than 'fatty' breasts because both the tumor and the background come out as white on the image.

"We are confident it is highly accurate and will be the more consistent result than humans reading the same mammogram," Dr Hupert says.

## **A.I. is coming**

Dr Hupert says healthcare is perfectly suited to artificial intelligence (A.I.) and has been one of the first sectors to embrace the brave new world. Not that radiologists need to be too afraid (see below).

“Interestingly, 80 percent of FDA-approved healthcare algorithms are in diagnostic imaging,” Dr Hupert says.

To date, the artificial intelligence has been embedded in imaging equipment.

“If someone moves during a [scan], AI may be able to improve the image or warn the technologists they may need to take another exam,” Dr Hupert says.

Artificial intelligence can prioritize which images should be viewed first in emergency settings and act as a “second set of eyes” in breast cancer and lung screening.

Dr Hupert believes automated diagnosis is some way off - and even A.I. agrees.

According to Chat GPT: “A.I. has the potential to significantly enhance radiology by improving efficiency and accuracy, but it is unlikely to fully replace radiologists in the foreseeable future.”

Meanwhile Dr Hupert says the acute global shortage of real-life radiologists - partly caused by high burnout - isn't getting any better. And the shortage will take years to ameliorate, because it takes three to five years to train a radiologist.

“Tele-radiology groups used to fighting for clients are now freezing new work and some groups are even giving back contracts they can't service adequately,” he says.

## **Sizing the rivals**

Depending on the sector, Pro Medicus competes with GE Health, Siemens and Philips and the erstwhile camera film makers Agfa, Fujifilm and Carestream. It also bumps into smaller ASX-listed peer Mach7 in the US market, although they tend to run their own race.

Pro Medicus claims to be winning share because it is nimbler than its more lumbering peers and can offer a full suite of products.

“We are confident we are number one in the three areas that count: speed, functionality and scalability,” Dr Hupert says.

He doesn't mention ‘cheapness’: Pro Medicus tends to have most expensive products but with the best claimed return on investment and clinical accuracy.

“We allow radiologists to do what they otherwise couldn't do, or if they could it would take too long to do.”

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

Despite its seemingly endless roll call of new and expanded clients, Pro Medicus lays claim to only seven percent of the US market of 650 million annual exams.

The company believes it can access 85 percent of this market "from a commercial perspective".

Goldman Sachs expects a market share of 13 percent by 2030 as more hospitals creak and groan into the modern era.

Investors might wonder whether Pro Medicus is ignoring the rest of the world, but the truth is that the US offers the best reimbursement relative to, say, the European market.

As the company grows its client book, the rules of mathematics dictate that such heady growth rates will be harder to maintain.

"Clearly, maintaining growth rates of 30 percent-plus year-on-year gets harder as our base gets bigger," Dr Hupert says.

"But we believe we can maintain our trajectory with strong, profitable growth. Our clients are growing well above the industry average and if they grow, we grow."

On broker estimates the company trades on an earnings multiple of around 130 times. While they love the company to bits, the prevailing view is the stock is priced to perfection.

The trouble is, you columnist opined the same things seven years ago - when the stock traded at \$5.00.

***Disclosure: Dr Boreham is not a qualified medical practitioner and does not possess a doctorate of any sort. Or a decent crystal ball, for that matter.***