



SomnoMed announces 2018 full year results and the consolidation of the RSS operations.

22nd August 2018, SomnoMed Limited (ASX:SOM) announced today full year group revenues of \$63.6 million (unaudited), representing growth of 29% over prior year. SomnoMed core revenues were \$52.4 million, up 10% from 2017 and Renew Sleep Solutions (“RSS”) revenues were \$11.2 million, and up from \$1.6 million in 2017. The Group EBITDA loss (unaudited) for the year is \$6.5 million. SomnoMed’s core division contributed a positive \$3.9m to this result (+65%), with RSS’s annual loss at \$10.4 million.

SomnoMed’s “Direct to Patient” business, RSS, is now nineteen months old and management has learnt a significant amount regarding the key drivers of success for the “Direct to Patient” model. After careful analysis of the performance of the centres opened to date and a better understanding of the key drivers of the business, it has been decided to reduce its operations from 12 metropolitan areas to 8, to provide the business with a stronger platform for near and long term success.

“Since first launching the RSS initiative we have learnt a considerable amount in how to make these treatment centres successful. Firstly, it is key to provide exceptional patient care and a more seamless customer experience. This we have succeeded in, as reflected by our outstanding on-line patient satisfaction scores. You also need to be able to effectively deal with the complex business of accreditation, insurance claims and case management and build an effective revenue cycle team, which we have also done. It is also critical to attract sufficient patients in as cost-effective manner as possible so as to make the whole model work. This is a combination of targeted multi-layer and efficient consumer marketing, being able to manage the distinct but shifting seasonality, plus finding the right kind of insurance landscape, which can positively influence marketing efficiency and patient acquisition costs,” commented Mr Derek Smith, CEO SomnoMed.

“Consolidating our operations to those cities where we believe we can build a successful business, while further developing the model and identifying future expansion opportunities is the right thing to do today. The smaller footprint we are left with enables us to focus on optimising a core number of centres in favourable markets, show we can operate these profitably and provide a solid platform from which to grow in the future. While RSS has not had the trajectory we envisaged only 6 months ago, it remains a key part of our business and strategy,” added Mr Smith.

SomnoMed core

The SomnoMed core business made good progress through the year delivering encouraging sales growth in Europe and APAC, as well as achieving improved revenue performance in the North American business in the second half. The European business delivered 26% full year revenue growth, with the second half accelerating to 28%. The key drivers of growth have been positive performance in France, as well as continued strong growth in our Benelux and Scandinavian markets.

In APAC, SomnoMed experienced an acceleration in the second half with the business growing at 10%, which is attributable to changes in the go-to-market operations in Australia. SomnoMed core North America posted improved second half revenue results (-2% over prior year second half against first half -16%) as the business implements the adjusted sales strategy to overcome the RSS effect on direct sales.

EBITDA in SomnoMed core business grew 65% year on year to \$3.9m, a margin of 7.4%.

The long term opportunity for the SomnoMed core business remains significant and investment is being made to further enhance its competitive advantages with a focus on its digital supply chain, digital product development, further clinical studies and re-imbursement efforts in those countries where it does not exist.

Renew Sleep Solutions

From inception, the RSS business approached the roll out of treatment centres based on encouraging results from Simple Sleep Services in Dallas/Fort Worth and the early results from the first four centres that RSS opened. However, as the newer centres began to mature and their results were below expectations, it became clear there was a significant level of variation in operating performance. Through ongoing and extensive analysis it became apparent that the “Direct to Patient” model is more complex than was previously anticipated. Market entry into each geographic area is extremely nuanced with key variables of success ranging from re-imbursement levels, the insurance landscape and differing advertising efficacy. These learnings have now provided a much clearer understanding of which markets are favourable to the current RSS model, which ones are not and what to do about those markets that are favourable, but are still underperforming. These learnings, coupled with the goal to manage cash flow more tightly, have led to a decision to reduce the number of cities in which RSS operates in from 12 metropolitan areas to 8, thus reducing the number of RSS centres from 16 to 8 from October 2018.

RSS will continue to have an operational base in the markets which are favourable to the current RSS model, where a successful business can be built in the future with a lower cash burden to the overall SomnoMed business. The long term opportunity to treat patients is significant and a smaller number of centres will provide RSS with the best opportunity to deliver treatments to patients over the long term.

The expected revenue growth over FY18 will still be strong and the EBITDA loss for FY19 will be significantly less than FY18’s actual result. The anticipated one-off cash cost to close these centres will be in the region of \$400k, although on-going premises lease costs will be a drag on the business until these facilities can be either sub-leased or exited. The rescaled size of the RSS operations will reduce the downside risk in cash flow. The financial impact will be to contain the RSS cash requirements to within SomnoMed’s cash availability.

Despite the challenges the RSS business presents and the complexity in developing a vertically integrated “Direct to Patient” business, RSS remains a critical part of the SomnoMed strategy.

Group

In summary, the SomnoMed Group posted strong revenue growth for FY18 but disappointing group EBITDA results due to RSS. The core business is making good progress with good revenue growth and margin expansion led mainly by Europe, with improving results in both North America and APAC. The RSS business concluded the year with 16 opened treatment centres with encouraging first cohort results, but with disappointing and varied results thereafter. This has led to the rescaling of the RSS operations from October, thus reducing the downside cash burn and losses to provide a successful base for further expansion into the future.

Net operating cash flow for the year was a negative \$9.5 million, after the investment made in RSS for the year at \$13 million, indicating a positive cash year for SomnoMed's core business of \$3.5 million. Cash held at 30 June 2018 was \$13.4 million.

Based on this the guidance for FY19 is as follows:

SomnoMed core business

- Revenue growth of 15%+ to A\$60m+
- EBITDA between A\$5m – A\$5.5m

RSS business

- Revenue growth between 25%-35% to between A\$14-15m
- EBITDA loss of between \$5–6m, representing a conservative guidance given the current risk (effective run rate loss of between \$4-5m when excluding the Q1 costs incurred in FY19 of those centres to be closed on 1 October 2018 but including rental expenses of closed centres)

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About SomnoMed

SomnoMed is a public company providing diagnostic and treatment solutions for sleep-related breathing disorders including obstructive sleep apnea, snoring and bruxism. SomnoMed was commercialized on the basis of extensive clinical research. Supporting independent clinical research, continuous innovation and instituting medical manufacturing standards has resulted in SomnoDent[®] becoming the state-of-the-art and clinically proven medical oral appliance therapy for obstructive sleep apnea. SomnoDent[®] is the most comfortable and effective design and treatment solution for now over 430,000 patients in 28 countries.

For additional information, visit SomnoMed at <http://www.somnomed.com.au>