

October 28, 2021

HOLD (no change)

Stock code:	SOM AU
Price:	A\$2.58
12-month target price:	A\$2.61
Previous target price:	A\$2.61
Up/downside to target price:	1.2%
Dividend yield:	0.00%
12-month TSR*:	1.2%
Market cap:	A\$213.5m
Average daily turnover:	A\$0.07m
Index inclusion:	N/A

* Total stock return – Up/downside to target price + 12-month forward dividend yield.

Price performance

(%)	1M	3M	12M	3Y
Absolute	7.5	7.9	25.9	90.2
Rel ASX/S&P200	6.6	7.7	2.8	58.7



Financial summary

	Jun-21A	Jun-22F	Jun-23F	Jun-24F
Revenue (A\$m)	62.7	74.7	85.6	102.5
EBITDA Norm (A\$m)	2.74	-0.46	6.95	10.43
Net Profit (A\$m)	-0.96	-2.79	2.20	4.64
EPS Norm (A\$)	-0.012	-0.034	0.026	0.056
EPS Growth Norm (%)	119%	190%		112%
P/E Norm (x)	NA	NA	97.56	46.11
DPS (A\$)	0.000	0.000	0.000	0.000
Dividend Yield (%)	0%	0%	0%	0%
EV/EBITDA (x)	71.32	NA	28.88	18.97
Gearing (Net Debt/EBITDA)	-6.85	26.19	-1.92	-1.57

Source: Company data, Morgans estimates

Related research

[SOM \(HOLD - TP A\\$2.61\) - 24 Aug 2021](#)

[SOM \(HOLD - TP A\\$2.55\) - 15 Jun 2021](#)

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– N/A

SomnoMed

Lying in wait

- SOM has released its 1Q22 cashflow report which is currently tracking in-line with our FY22 forecasts on a revised run-rate basis.
- Outlook commentary is increasingly positive, with a new technology expected to be released early CY22 and business conditions continue to improve as markets and access to clinics normalise.
- Guidance for FY22 remains in line with our forecasts with sales growth of at least 15% YoY growth and EBITDA breakeven.
- While we make no changes to our forecasts and Hold recommendation, we continue to look out for opportunities on weakness ahead of potentially strong sales prints and further news flow around the technology piece. No change to price target of A\$2.61 and Hold recommendation retained.

1Q report tracking in line

- SOM reported unaudited revenues of A\$15.6m (+14% on pcp, down 4% QoQ). Based on updated seasonality mix (ex RSS) of around 20.5% quarterly sales splits, SOM is tracking broadly in-line with our FY22 forecasts.
- The North American channel (~33% of sales) was a standout with a solid sign of turnaround with +3% growth QoQ and +13% on pcp, driven by a re-activation of its sales channel team and demand for the flagship Advance Elite product.
- Europe (~60% of sales), while volatile and continues to vary market to market, continues to be the engine room for growth, delivering strong YoY growth (+17% on pcp) despite ongoing COVID factors, led by strong rebounds (+25% on pcp) in sales across its major jurisdictions with high reimbursement rates.
- The company recorded A\$2.2m in operating cash outflow and closed the period with A\$17m in cash.

Seasonality traits have evolved – FY22 run-rate on track

- Based on historical splits (1Q ~22.7% of FY sales), 1Q22 revenues would indicate the Company is on target for ~A\$68.7m in sales (vs MorgansE A\$74.3m), and tracking ~7.5% below our forecasts – which would have been a cause for concern.
- However, excluding the historical direct to consumer RSS venture from sales and a higher weighting toward European seasonality, we have calculated 1Q splits to now sit at 20.5% of FY sales.
- Based on this and potential impact from the new technology piece in early 2H22, we remain comfortable on sales progression to date, sitting at ~A\$76.1m FY run-rate and slightly above our forecasts of A\$74.3m.

What do we know about the new technological innovation?

- Not a whole lot but from discussions with management, the level of R&D investment, and sentiment around this new piece in recent announcements, it's clear that the company is placing a high value and anticipation around the potential long-term impacts the innovation will bring.
- A hinderance to higher adoption rates for COAT devices has been the difficulty in obtaining quantitative and longitudinal data outside of clinical studies to show compliance rates over alternative therapies. This is due to the lack of connectivity and feedback inherent in these devices.
- As such, we view the advancements address this issue and likely some form of electronic eco-system which works around the products to track both condition monitoring and compliance – a huge advantage to both patients and the payors. If so, we can understand management's excitement. More details to come.

Investment view

- We have made no changes to our forecasts or recommendations at this stage although look to take advantage of opportunities on weakness.
- Given the unknowns, we reserve upside potential based on the release of further details on the new technology opportunity. Formal launch is expected around early CY22 but we look to the AGM for further detail and a potential 2Q sales progress.

Risks

- Downside risk to our target is slower-than-expected growth in the core markets.
- Upside risks lie in potential corporate interest and faster stabilisation in EU/US.

SomnoMed

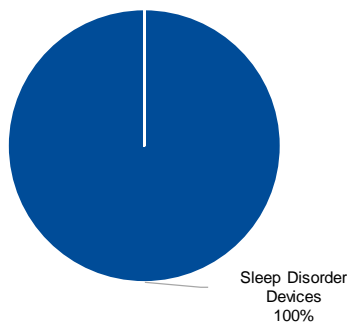
as at October 28, 2021

Rating	HOLD	Price (A\$):	2.58
Market cap (A\$m):	213.5	12-month target price (A\$):	2.61
Shares outstanding (m):	83.02	Up/downside to target price (%):	1.2
Free float (%):	67.1	Dividend yield (%):	0.00

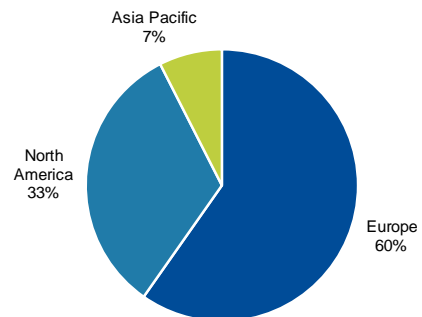
Company description

SomnoMed Limited (SOM) provides treatment solutions for sleep-related breathing disorders including obstructive sleep apnea, snoring and bruxism. The SomnoDent® product range involves a custom fitted, comfortable, clinically researched oral appliance worn at night to treat obstructive sleep apnea. The SomnoDent® product has a number of innovative designs including a Avant, Fusion Flex and Classic. The SomnoDent® is designed for the patients who suffers from mild to moderate OSA and includes the proprietary BFlex soft inner liner for unparalleled comfort and retention.

Business segmentation by revenue



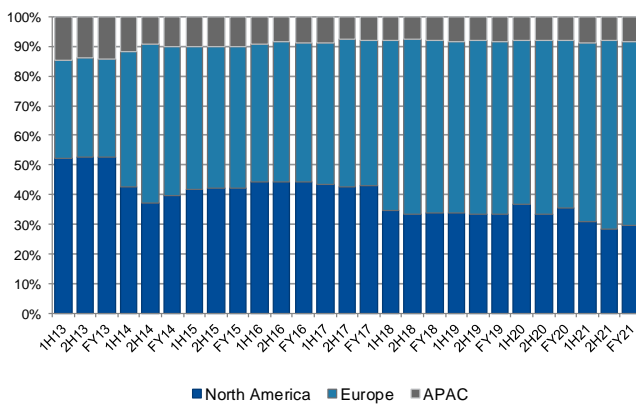
Geographical segmentation by revenue



Source: Morgans estimates, company data

Source: Morgans estimates, company data

Revenue splits by geography (core business)



Source: Morgans estimates, company data

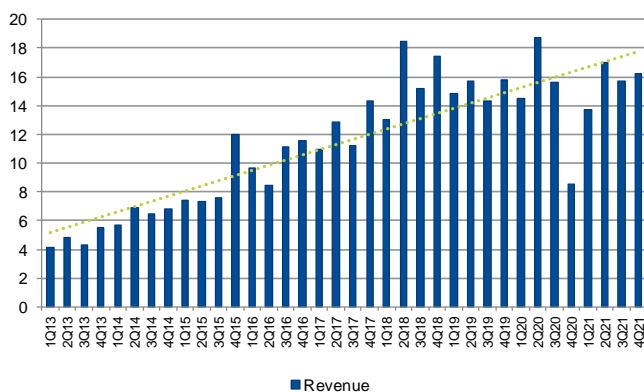
COVID-19 RISKS

The specific risks associated with the Coronavirus (COVID 19) event are:

- Patients not being able to seek diagnosis and obtain treatment and people not wanting or able to visit dentists
- Inability to collect accounts receivable from customers whose practices have been temporarily closed
- Manufacturing risk such that there is an inability to have technicians physically able to come to work and perform their duties
- Third party supply disruption of necessary raw material
- Executive management contracting COVID 19 and remaining sick or no longer being able to fulfil their duties in any capacity
- Prolonged periods of lock down in SomnoMed's sales markets
- Ongoing support of current finance providers

Source: Morgans estimates, company data

Quarterly sales revenue



Source: Morgans estimates, company data

Key drivers / risks

Key Drivers

- Compliance** - Higher compliance rates (80% for COAT vs <50% for CPAP) and lower cost than CPAP competitors.
- Expansion** - European expansion continuing to show strong growth. Underserved market for treatment modality
- Turnaround** - Watching for evidence of a US turnaround after a direct retail channel move was received poorly by existing wholesale customers.

Key risks:

- FX** - Majority of revenues generated outside of Australia.
- Substitution** - A number of new and existing alternative products exist in the sleep apnea space which may impact SOM's ability to gain market share.
- Reimbursement** - Risk that insurance companies/governments which partially or fully subsidise the products reduce or exclude the reimbursement for the treatment.

Source: Morgans estimates, company data

Figure 1: Financial summary

Income statement						Valuation metrics										
	FY20A	FY21F	FY22F	FY23F	FY24F						Price Target (A\$)	\$2.61				
Total revenue	57.3	62.7	74.7	85.6	102.5	DCF valuation inputs										
EBITDA	4.7	2.7	-0.5	7.0	10.4	Rf	3.00%	10-year rate					3.00%			
Associate income	0.0	0.0	0.0	0.0	0.0	Rm-Rf	6.00%	Margin					2.0%			
Depreciation	-3.1	-3.8	-3.8	-3.8	-3.8	Beta	1.27	Kd					3.50%			
EBITA	1.6	-1.1	-4.3	3.1	6.6	CAPM (Rf+Beta(Rm-Rf))						10.6%				
Amortisation/impairment	0.0	0.0	0.0	0.0	0.0	Equity (E/EV)						60.0%				
EBIT	1.6	-1.1	-4.3	3.1	6.6	Debt (D/EV)						40.0%				
Net interest expense	-0.5	0.6	0.4	0.2	0.2	Interest rate						3.50%				
Pre-tax profit	0.7	-0.6	-4.0	3.1	6.6	Tax rate (t)						30.0%				
Income tax expense	-1.2	-0.3	1.2	-0.9	-2.0	WACC						9.4%				
After-tax profit	-0.4	-1.0	-2.8	2.2	4.6											
Minority interests	0.0	0.0	0.0	0.0	0.0											
NPAT	-0.4	-1.0	-2.8	2.2	4.6											
Significant items	-0.7	0.0	0.0	0.0	0.0											
NPAT post abnormals	-1.1	-1.0	-2.8	2.2	4.6							\$2.61				
Cash flow statement						Multiples										
	FY20A	FY21F	FY22F	FY23F	FY24F		FY20A	FY21F	FY22F	FY23F	FY24F					
EBITDA	4.7	2.7	-0.5	7.0	10.4	Enterprise value (A\$m)	158.5	144.3	137.7	138.9	141.9					
Change in working capital	9.1	-1.8	-3.1	-0.8	-1.4	EV/Sales (x)	2.8	2.3	1.8	1.6	1.4					
Net interest (pd)/rec	0.0	0.0	0.0	0.0	0.0	EV/EBITDA (x)	33.6	52.7	-297.2	20.0	13.6					
Taxes paid	1.2	0.3	-1.2	0.9	2.0	EV/EBIT (x)	96.8	-131.3	-32.0	44.6	21.5					
Other oper cash items	0.0	0.0	0.0	0.0	0.0	PE (x)	-276.0	-125.8	-43.4	55.2	26.1					
Cash flow from ops (1)	15.0	1.3	-4.7	7.1	11.1	PEG (x)	-0.4	-1.1	-0.2	-0.3	0.2					
Capex (2)	-3.1	-3.8	-3.8	-3.8	-3.8	Per share data						FY20A	FY21F	FY22F	FY23F	FY24F
Disposals/(acquisitions)	0.0	0.0	0.0	0.0	0.0	No. shares	82.8	83.0	83.0	83.0	83.0					
Other investing cash flow	0.0	0.0	0.0	0.0	0.0	EPS (cps)	-0.5	-1.2	-3.4	2.6	5.6					
Cash flow from investing (3)	-3.1	-3.8	-3.8	-3.8	-3.8	Dividend per share (c)	0.0	0.0	0.0	0.0	0.0					
Incr/(decr) in equity	0.0	0.0	0.0	0.0	0.0	Dividend payout ratio (%)	0.0%	0.0%	0.0%	0.0%	0.0%					
Incr/(decr) in debt	0.0	0.0	0.0	0.0	0.0	Dividend yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%					
Ordinary dividend paid	0.0	0.0	0.0	0.0	0.0	Growth ratios						FY20A	FY21F	FY22F	FY23F	FY24F
Preferred dividends (4)	0.0	0.0	0.0	0.0	0.0	Sales growth	-3%	9%	19%	15%	20%					
Other financing cash flow	-2.5	-2.4	0.0	0.0	0.0	Operating cost growth	-3%	14%	25%	5%	17%					
Cash flow from fin (5)	-2.5	-2.4	0.0	0.0	0.0	EBITDA growth	-5%	-42%	-117%	1601%	50%					
Forex and disc ops (6)	0.0	0.0	0.0	0.0	0.0	EBITA growth	-53%	-167%	-291%	172%	112%					
Inc/(decr) cash (1+3+5+6)	9.5	-4.9	-8.6	3.3	7.2	EBIT growth	-53%	-167%	-291%	172%	112%					
Equity FCF (1+2+4)	12.0	-2.5	-8.6	3.3	7.2	NPAT growth	-1012%	-120%	-190%	179%	112%					
						Normalised EPS growth	736%	119%	190%	-179%	112%					
Balance sheet						Operating performance										
	FY20A	FY21F	FY22F	FY23F	FY24F		FY20A	FY21F	FY22F	FY23F	FY24F					
Cash & deposits	30.2	21.1	14.5	15.7	18.8	Asset turnover (%)	29.7	26.6	36.6	45.5	50.3					
Trade debtors	7.7	10.6	9.2	10.6	12.6	EBITDA margin (%)	8.2	4.4	-0.6	8.1	10.2					
Inventory	2.2	2.3	0.0	0.0	0.0	EBIT margin (%)	2.9	-1.8	-5.8	3.6	6.4					
Other current assets	0.0	0.0	0.0	0.0	0.0	Net profit margin (%)	-0.8	-1.5	-3.7	2.6	4.5					
Goodwill	0.0	0.0	0.0	0.0	0.0	Return on net assets (%)	1.3	-14.4	-22.4	19.6	4.8					
Other intangible assets	0.0	0.0	0.0	0.0	0.0	Net debt (A\$m)	-22.7	-18.8	-12.1	-13.4	-16.4					
Fixed assets	3.9	4.7	4.7	4.7	4.7	Net debt/equity (%)	-67.1	-58.3	-42.4	-43.6	-46.9					
Investments	0.0	0.0	0.0	0.0	0.0	Net interest/EBIT cover (x)										
Other assets	17.7	17.4	17.4	17.4	17.4	Invested capital	20.3	11.6	13.4	16.5	17.3					
Total assets	61.7	56.2	45.8	48.4	53.5	ROIC (%)	-2.2	-8.3	-20.8	13.3	26.9					
Short-term borrowings	0.0	0.0	0.0	0.0	0.0	Internal liquidity						FY20A	FY21F	FY22F	FY23F	FY24F
Trade payables	8.7	10.6	3.8	4.3	5.1	Current ratio (x)	4.6	3.2	6.3	6.1	6.2					
Long-term borrowings	7.5	2.3	2.3	2.3	2.3	Receivables turnover (x)	6.2	6.8	7.5	8.7	8.8					
Other term liabilities	8.7	7.6	7.6	7.6	7.6	Payables turnover (x)	6.2	6.2	10.5	19.4	19.6					
Other liabilities	0.0	0.0	0.0	0.0	0.0											
Total liabilities	27.9	24.0	17.2	17.7	18.5											
Share capital	73.9	74.3	74.3	74.3	74.3											
Other reserves	8.6	7.8	7.8	7.8	7.8											
Retained earnings	-48.7	-49.9	-53.4	-51.4	-47.0											
Other equity	0.0	0.0	0.0	0.0	0.0											
Total equity	33.8	32.2	28.6	30.6	35.0											
Minority interest	0.0	0.0	0.0	0.0	0.0											
Total shareholders' equity	33.8	32.2	28.6	30.6	35.0											
Total liabilities & SE	61.7	56.2	45.8	48.4	53.5											

Source: Morgans estimates, company data

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