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CEO on FY2012 Results & Outlook

Open Briefing interview with CEO Sam Hupert

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Pro Medicus Limited
450 Swan Street
Richmond VIC 3121

In this Open Briefing[®], Sam discusses:

- Improvement in continuing business earnings and cash flow
- High value achieved from Amira sale provides balance sheet flexibility
- Outlook for core radiology product sales

Record of interview:

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Pro Medicus Limited today reported net profit after tax of \$0.76 million for its continuing operations in the year ended 30 June 2012, compared with a loss \$0.69 million for the previous year. Revenue of \$11.31 million was up 2 percent. The result excludes \$1.04 million after tax profit from the Amira business, which you sold in July, and suggests Amira was a significant contributor to profit in the past. How confident are you that the remaining business can generate sustainable profits and growth in the absence of Amira?

CEO Sam Hupert

There's no question Amira has been a good asset for us, but it was in a limited market that was facing increasing competition. We believe our new generation radiology products: our new radiology information system (RIS) and the Visage 3D picture archiving communications systems (PACS) have more opportunities and far greater growth potential. We also feel we're now in a better position to experience that growth, and moving our continuing business from a \$0.7 million loss to a \$0.8 million gain is evidence we're heading in the right direction!

Also bear in mind the price we got for Amira – equivalent to 14 times earnings – is unlikely to be repeated. This was a unique opportunity where the asset, and importantly the timing of the sale, was of significant strategic value to the acquirer, which is the reason we got the multiple we did. So even taking into account the loss of the Amira revenue and the fact that our core business is still in ramp-up phase, we saw the sale as our best opportunity to maximise the value of the asset. The sale has given us a high degree of balance sheet flexibility and we're confident we've made the right decision for the long run.

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Pro Medicus had cash in hand of \$5.19 million as at 30 June, up from \$3.26 million a year earlier. Since the end of the year you've received EU12.1 million (about AUD14.1 million) from the sale of Amira, bringing cash to around \$20 million. How much of this cash do you plan to retain? Are you actively seeking acquisitions?

CEO Sam Hupert

We're very pleased our retained earnings have been building back up. After tax, the cash we'll receive from the sale of Amira will be approximately \$10 million. Adding this to our current retained earnings, we should have around \$15 million cash, a record for us. Certainly it's good to have that buffer.

As we've said previously, there are three options we're considering for our additional cash: returning part of it to shareholders; reinvesting in the business which is important given the growth profile we see in our RIS and 3D PACS products; and keeping some cash available for potential future acquisitions.

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In FY2012, your PACS sales totalled \$5.47 million, up 25 percent, while sales of RIS were down 18 percent to \$4.03 million. How indicative are these trends of the expected future trend in sales? What have been the key drivers of the growth in PACS sales?

CEO Sam Hupert

The growth in PACS sales is off a low base and yes, we believe it's indicative of the future trend in sales. We believe the Visage product addresses a far larger percentage of the radiology market globally and we're just starting to see some of the expected upward momentum in sales. However, I stress that it's early days and that the industry as a whole faces headwinds: there's a lot of nervousness surrounding healthcare spending globally, but particularly in Europe and the US, and as a consequence decisions are being delayed.

In RIS, customers are waiting for the release of our new product before making any decisions, and until it comes out we're in a hiatus. We expect sales to turn around and start increasing as the new RIS comes out.

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Your Australian business booked EBIT of \$0.51 million for FY2012, versus a loss of \$1.04 million in the previous year. Revenue was \$5.43 million, down 7 percent, which you've attributed to the delay in the launch of the new RIS. When will the product be released and what are your expectations for the new RIS going forward?

CEO Sam Hupert

We've had the product in pre-release for some time now and believe its full commercialisation is imminent. Once it's released, we'll be able to upgrade the products of our existing client base. It will also open up the opportunity for new sales as many potential customers have been waiting to try the product. We're confident we'll see an uptrend in revenue once the RIS is released but like all new products it will take time to get full market traction.

We'll be showcasing our new technology platform at the Australian College of Radiology meeting in Sydney later this month as well as the large Radiological Society of North America (RSNA) conference in Chicago in November which will give it a fair bit of exposure.

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The European business booked EBIT of \$0.62 million, down 16 percent, on revenue of \$3.63 million, up 25 percent. Margin fell to 17.2 percent from 25.6 percent. What was behind the revenue growth and consequent fall in margin? Given Amira appears to have made the biggest contribution to your European business, how will the remaining business be impacted by the sale of Amira?

CEO Sam Hupert

We have two divisions in Europe, one that sells our Visage PACS directly to customers and one that sells embedded, or OEM, technology. The latter is a lower margin business but did particularly well in FY2012. Amira's biggest contribution was in Europe, but we're confident that over time we can replace its revenue stream with our core products, which we see as having more upside. Following the sale of Amira, the important thing for us in Europe is to get more traction in the higher-margin Visage side of the business which has continued to grow, again off a very low base.

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In North America, you made an EBIT loss of \$0.18 million, versus a loss of \$0.81 million in the previous year. Revenue was \$2.26 million, down 4 percent. You've significantly cut costs in North America. What factors explain the drop in revenue and how are you positioned to grow the business in this region after the reduction in the cost base?

CEO Sam Hupert

On a constant currency basis, our revenue from North America was pretty much flat, with the exchange rate accounting for the 4 percent difference. We've reduced costs and got the business to pretty much breakeven. But more important than the reduction in costs is that we've totally changed the management team: we've got a far more effectual team with the added advantage of a lower cost overhead. Structurally we're far better positioned to take the North American business forward than we were say 12 or 14 months ago and we believe we'll see the benefits of that over time.

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Investment in product development (excluding investment relating to Amira) totalled \$2.70 million in FY2012, down from \$3.34 million in the previous year. This is equivalent to 24 percent of sales, down from 30 percent. To what extent is this level of investment necessary for Pro Medicus to remain competitive? How is product development investment expected to trend in the current year?

CEO Sam Hupert

The level of product development investment at the moment is significant and we don't see substantial increases from these levels. However, as a percentage of total revenue, we'd expect it to fall from the current relatively high level as revenue builds. Continued investment in our products is important to us: even where the product is doing well you always have to be ahead of the game to generate sustainable revenue growth.

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Cash flow from operations was \$5.88 million in FY2012, up slightly from \$5.78 million in the previous year. After investment, including in product development, free cash flow was \$2.47 million, up from \$1.71 million. What will be the drivers of any material increase in free cash flow in the future?

CEO Sam Hupert

The cash flow figures were skewed by a one-off charge relating to tax payments in Europe: we'd previously been paying tax yearly in arrears, but now we're required to pay quarterly in advance. Adjusting for those tax timing issues, operating cash flow would have been \$7.70 million in FY2012, up from \$5.19 million in FY2011.

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Pro Medicus has declared a fully franked final dividend of 1 cent per share, bringing the full-year payment to 1.5 cents per share, equivalent to a payout of 84 percent of reported profit. What is the outlook for dividends in the current year in light of your renewed focus on reinvesting in the business post the Amira sale?

CEO Sam Hupert

We never pre-empt the board's decision on the dividend given it's based on what's best for the business at the time. However it's fair to say we're very pleased to be able to go back to paying dividends, although our decision in the previous year not to pay a dividend proved to be a sound one. Now we have a stronger level of retained earnings and of course the funds from Amira, we have far greater flexibility in terms of capital management which is always a good position to be in.

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Thank you Sam.

For more information about Pro Medicus Limited, visit www.promedicus.com or call Sam Hupert on (+61 3) 9429 8800.

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