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Transcript of DarioHealth Third Quarter 2016 Earnings Conference Call November 11, 2016

Participants

Rob Fink – Hayden IR
Erez Raphael, Chief Executive Officer
Zvi Ben-David, Chief Financial Officer

Presentation

Operator

Good day, everyone, and welcome to today's DarioHealth Third Quarter 2016 Earnings Call. At this time, all participants are in a listen-only mode. Later you will have the opportunity to ask questions during the question-and-answer session. [Operator instructions].

It is now my pleasure to turn today's conference over to Rob Fink of Hayden IR. Please go ahead, sir.

Rob Fink – Investor Relations

Thank you, operator. I would like to welcome everyone to DarioHealth Third Quarter 2016 Earnings Conference Call. Hosting the call today are Erez Raphael, Chief Executive Officer, and Zvi Ben-David, Chief Financial Officer. Before I turn the call over to management, I'd like to remind everyone that this conference call may contain projections, and other forward-looking statements regarding future events or the future performance of the company. DarioHealth does not assume any obligations to update that information. Actual events or results may differ materially from those projected as a result of changing market trends, reduced demand and the competitive nature of DarioHealth Industry, as well as other risks identified in the documents filed with the Securities and Exchange Commission.

With that, I would now like to introduce Erez Raphael, Chief Executive Officer, and turn the call over to him. Erez, the call is yours.

Erez Raphael – Chief Executive Officer

Thanks, Rob, and good morning, and welcome to DarioHealth third quarterly earning call in more than two years. Thank you all for joining us today. During the third quarter, we materially advanced and launched DarioHealth in the United States and delivered quarterly revenues and significantly increased our sales of devices. We also increased the amount of users that we have and subscribers, the current users, and we feel that we are in a position to keep increasing our sales and increasing the margins as we move forward into Q4 of 2016, and also into 2017.

Another positive sign this quarter was the fact that we have gross profit that is positive for the first time. We are encouraged by the traction we had in the US market in the last few months. We launched on a soft launch by the beginning of March, and we started to impact in June. We got a lot of very, very good comments from users, and we're looking forward to keep expanding the US market as we move forward. Also, with the Android clearance in the near future.

Before we get into more detailed review of our quarter, since this is our first earning call in some time, I'd like to take a moment to provide everyone, and particularly those who may be new to our company with a brief overview of our business and some insight into our market. I would like also to highlight key catalysts that we believe will drive sustainable long-term growth for our company.

So, DarioHealth Corporation creates innovative mobile and digital tool that involves and engage users to lead healthier lives. Our approach and strategy is positioning the company as a player in the medical and mobile health and the digital health industry. This is an industry that as of today, according to research to guidance, is a \$10 billion industry, and is going to grow to \$31 billion by 2020. In addition the glucose monitoring industry is \$18 billion market in total.

We see that the connectivity and mobile disrupted a lot of industry in the world. We see the same thing with the transportation industry. We've seen it in other industry that is related to real estate, hotels. It didn't happen yet in the health industry. There are few reasons for that. Some of the reasons related to the market that is highly regulated. Some of the reasons related to a market that is being impacted by fails [ph], by consumers, by healthcare professionals, but we're seeing that this disruptions of a connectivity and mobile will happen also in the healthcare industry.

If we're looking in the last few years, we can see new industry developing where we have on one hand companies that are coming from the wellness industry. We see companies like FitBit, companies like Misfit [ph], Jawbones and others that created very user-centric solutions. These user-centric solutions have created a very engaging solution, and when we are looking on the traditional medical device industry, we have seen an industry that is very oriented by healthcare professionals.

We think that in the future this new industry will be merged, and we think the value is well positioned to gain from these two worlds as our product is highly user-centric, but at the same time, it's also high quality and all the regulations, cleared by four regulation bodies, and also, reimbursed in a few countries, in Europe, this is including Europe, Australia and Canada.

As we move forward into this industry, we think that solutions that we'll be able to create something different in the market are solutions that has on one-hand improvement of clinical outcomes, solutions that has very user-friendly controls and also, solutions that will enable cost reduction. And we feel with that value, we have all these three pieces.

Okay, now in investor's presentation, we're showing Dario solutions that we have. So, in slide 6 and 7, for those that are holding the investor's presentation, you can see that in our solution, we are having an overall handset and a glucose monitor that is coupled into the smartphone. In fact this is the most advanced solution that we have at the moment in the market, because we are in fact turning the smartphone to be a glucose monitor, and we are not connecting, or we are not creating our own solution, but extending an existing smartphone.

In addition, we also two other very important pieces to our overall solution. The first piece, the state of the application that helps users manage their chronic condition. And in addition, we have also a very advanced solution of the cloud mobile. So, if we are looking on the overall Dario solution, you can bet a hardware solution, a [indiscernible] solution, and it connects all the stakeholders around managing chronic condition.

One is the user and the consumer, two is the healthcare professionals entail and three is the family members and others that can help user get the right support.

In slide 11, we are showing the revenue strengths that we have in value. This is a very important slide and a very important thing to understand. Our business is split into three pillars, three revenue streams. The first one is what we are calling the My DARIO. My DARIO is the solution that provides the application and also, the hardware, including the disposables, which are the test strips [ph]. The disposables create a monthly and yearly revenue stream for Dario. This is a very powerful engine to keep ourselves going, and as we move forward, we believe that we can grow in a more intensive way having this disposable key element.

The second pillar is the pillar that's related to how we integrate with healthcare professionals, and how we can ramp up the treatment from the single user to the overall population, whether it's in the level of clinician, or it's in the level of the whole industry. In addition, we have the third pillar, which is the data that we are capturing. Because Dario is the [indiscernible] mobile solution, which means that it's running on the smartphone itself, it doesn't depend on the Bluetooth connectivity, and it doesn't depend on the willingness of the user to sync the data. It means that all the data is captured to the smartphone, and everything is communicated with the cloud. And it's not just the blood glucose data, it's also other data points that's related to exercising, to food. We are connected to a very big food database with more than half million different types of food, and everything is communicated with the cloud, which is very powerful and can help us create elements of predictive analytics that will help gain a very small features for our users.

So, as of today with the features that are related to estimation of the mobile A1C, which is the measure that people with diabetes are using in order to understand whether they're maintaining their current condition over three months. Other elements that are related to connectivity, we have features that help users issue alerts with a location link to their location if they're in a threat of getting into hyperglycemia. All these feature make our solution unique and different, and with the data that we're capturing, we can keep developing features that will create our solution more than a glucose monitor.

So, a FitBit is a solution that is more than a pedometer. We think that Dario, and this is a comment that we are getting from our users, Dario makes the transformation of this industry from a monitor and glucose monitoring into diabetes management. This is what we are selling. We are selling diabetes management that is backed by very powerful technology that is native mobile, running on the mobile whether it's an iOS or Android.

In the last two years, we did a lot of progress in creating a company that is very global, which means that we are acting in main markets like UK, Canada, Australia, Italy, and in the US as well. It's very important to operate in few markets. It means that our ability to grow the revenue, and to spread the risk around a few different territories makes us more comfortable that we can grow our revenue as we move forward.

In the US, the Dario diabetes management system was cleared by the FDA on December 2015 for the iOS, which means the Apple devices only. As we move forward, we launched on the soft launch by the beginning of March, and we started to end up the sales of the device in June, and as we reported a few weeks ago also, in this quarterly results, we see a significant increase in the sales of our device. The feedback that we are getting from users is very, very good.

And we start to see some kind of viral element of users that are approaching our website and buying our device. But we are providing in the space is a very unique model that we are providing the opportunity to subscribe on our services, and by subscribing, users can get the device and the test strips, especially the test strips, for a very comparative price. Which means, once we are collecting subscribers, we can guarantee revenue as we move forward to the next quarter, and build our revenue stream also toward 2017.

So, finally, the target market is the United States with almost 30 million people that have diabetes, and almost 1.4 million that are diagnosed every year. If we are looking forward, how we can keep improving and growing the sales as we move forward, there are a few dimensions for new opportunities for growth. The first one is to extend into more territories. The second one is to provide additional services both support on top of the platform, and we're looking forward to launch next year also the capabilities of coaching on top of the platform. We think that at the end of the day, we want to provide payers with the opportunity to buy one monthly subscription with combined with the device and test strips, but also, a coaching program where eventually, we will be able to provide clinical outcomes and improvements.

As we move forward, we have the technology, and we are working on expanding the technology, both with the support of other chronic conditions, and also to support added applications that is related to people with diabetes. For example, we think that we can create a tailored solution for gestational diabetes. We can create tailored solution for pre-diabetes, and all this kind of different applications that are running on the same infrastructure can help us expand our service, and grow even it in a more and fast way than we're doing as of today.

To summarize what we are having and what we feel the market needs is—I'll say the market today becomes very user-centric. Because of solutions that exist in the market, and because the mobile revolution in the wellness industry which is growing, there is a need to have a solution that is very user-centric. I'm very proud that we have this kind of solution big time for our users, and this is what we are getting from the comments. The solution that we have is very user-centric.

The other element is improvement of clinical outcomes, because we are selling more than glucose monitors, we are selling also a management platform and on top of that, next year we're going to have also the coaching. We feel that clinical outcomes is something that our overall platform will have, and it will also enable us to scale the treatment up so payers will eventually pay less, which is the third element that is very important in order to be successful in a scaled up way in this market.

So, with that, I would now like to turn the call over to Zvi Ben-David for more detailed review of our financial results. So, Zvi, go ahead.

Zvi Ben-David - Chief Financial Officer

Thank you, Erez. As we have already disclosed, and as Erez looked at the revenue at the end of the third quarter, we sold more than 10,000 value all in one smart glucose meter devices to consumers in the United States. In the first 6 months, since its launch in March, more than 5,500 of these 10,000 devices were purchased in the third quarter, doubling our market presence over the past 3 months, a trend that we expect to continue.

At the end of the third quarter, we had more than 10,900 users registered from our servers, more than doubling the numbers that we had on June 30, and out of these users, more than 10,000 have already ordered strips. During the third quarter, the strip quantities we have sold were 85% higher than the quantities that were sold in the second quarter. About 65% of the total strips sold since launch were purchased by users under our subscription plan. While in the third quarter only, this number was around 70%.

Turning to the third quarter, the results, revenues, for the third quarter at end of Sept 30, were \$728,000, a 166% increase from the \$273,000 for the quarter ended September 30, 2015. This, also, is an increase of 9%, compared to the second quarter of this year where our revenues were \$659,000. Out of the \$728,000 in revenues, about \$490,000 were generated from Dario sales in the US. And \$82,000 was generated in Australia from added sales to consumers and whole-sellers that started to ramp up gradually during the third quarter after the conditions [indiscernible] that we had in this market.

Revenues in the third quarter of 2016 include those sold product sales to distributors in the United States, UK, Italy, Canada, New Zealand and Israel; 75% of our quarterly revenues are derived from the sale of test strips and other consumer goods.

For the nine months ended September 30, 2016, the revenues were almost \$2 million, a 281% increase from the \$515,000 for the nine months ended September 30, 2015. Gross profit of \$76,000 was recorded in the third quarter of 2016, an increase of \$207,000 compared to the gross loss of \$131,000 in the third quarter of 2015, and compared to a gross loss of \$157,000 in the second quarter of 2016. The increase in the gross profit recorded in the third quarter of this year is the result of the following: first of all, increase in our sales level; the higher ASB [ph] for the value all-on-one device resulting from direct sales in Australia and the US, which improved our margin; and the fact that we did not have to write down the value of the device inventory at quarter-end put [indiscernible] value. In the last sale, the increased share of revenues from strips and other consumer goods, which generate the higher gross margin.

Gross profit for the nine months improved by \$413,000 to a loss of \$180,000 in the nine months ended September 30, 2016, compared to \$596,000 gross margin, gross loss in the nine months at ended September 30, 2015.

Operating expense for the third quarter ended September 30, increased by \$381,000 to \$2.8 million in total as compared to \$2.4 million of operating expenses in the third quarter of last year, and also, increased by \$330,000 compared to the second quarter of this year. This is mainly due to the increase in our added market expenses in the US, and also in Australia.

Operating loss for third quarter increased by \$174,000 to \$2.7 million as compared to \$2.5 million operating loss in the third quarter of last year. This increase is mainly due to the increase in the sale of marketing expenses [indiscernible] offset by a reduction of our general and administrative expenses. Operating loss for the nine months ended September 30, 2016 increased by \$1.8 million to \$7.1 million as compared to \$5.2 million operating loss in nine months of last year. This increase is also a result of our increased investment in sales and marketing partially offset by a reduction in our R&D expenses.

Net loss was \$2 million in the third quarter of 2016 compared to \$1.6 million in the third quarter of 2015. An important note about our balance sheet, about 973,700 warrants was weighted leverage onto [indiscernible] the liability on our balance sheet since the issuance, in 2012, expired on October 26, 2016. We had recorded income of \$2.7 million for the nine months ended September 30 related to the gradual devaluation of the value of this warrant.

Thank you for listening, and now, back to you, Erez.

Erez Raphael – Chief Executive Officer

Thanks, Zvi. As you can see, we made meaningful progress against our long-term growth strategy during the third quarter. Looking forward, we will continue to focus on our value to consumer strategy, and further enhance our wide positive customer acquisition efforts in the United States, and also in other key markets. We expect that the FDA clearance for the Android will push more even more significantly the growth in the US market. Just to remind you in the rest of the market, the Android is available. So, we have the technology. We already submitted the Android to the FDA. So, it's just a matter of getting it cleared, and start the commercialization of the Android as well. Users are very excited about our device and our overall solution, and they keep asking when they are going to get the Android, and I'm very positive that it should happen in the next few months.

We believe that our subscription program that was launched in the US provides a compelling value into the market, and we're encouraged by the conversion rate we have seen so far. As we grow, our subscriber list will increase high margin reoccurring stream, which we believe will provide the strong foundation for growth in 2017.

With that said, I will now like to open the call for questions.

Operator

Thank you. [Operator instructions]. We will pause for a moment to allow any questions to queue.

It appears we have no questions at this time. I'd like to turn the conference over to Erez Raphael for any additional or closing remarks.

Erez Raphael – Chief Executive Officer

So, I'd like to thank everyone for joining us for this quarterly call. I'm looking forward to getting on the call again in the next quarter, and keep updating you on the progress that we are making. Thanks, everyone, and have a good day.