

Transcript of DarioHealth Corporation Second Quarter 2019 Earnings Call August 13, 2019

Note: Due to some accented speakers this was a very difficult call to transcribe and not everything could be captured as a result.

Participants

Erez Raphael – Chief Executive Officer
Olivier Jarry – President and CCO
Zvi Ben-David – Chief Financial Officer

Analysts

Alex Nowak – Craig-Hallum Capital Group
Steven Wardell – Chardan Capital
Benjamin Haynor – Alliance Global

Presentation

Operator

Good day, ladies and gentlemen, and welcome to DarioHealth's Second Quarter 2019 Earnings Call. Hosting the call today are Erez Raphael, Chief Executive Officer; Olivier Jarry, President and Chief Commercial Officer; and Zvi Ben-David, Chief Financial Officer.

Before I turn the call over to management, I'd like to remind everyone that during the course of this call, management will express and implied forward-looking statements within the Private Securities Litigation Reform Act of 1995, and other US Federal Securities laws. DarioHealth does not assume any obligation 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's industry. Such forward-looking statements and their implications involve known and unknown risks, uncertainties and other factors that may cause actual results or performance to differ materially from those projected.

The forward-looking statements discussed on this call are subject to other risks and uncertainties, including those discussed in the Risk Factors section and elsewhere in the company's Annual Report on Form 10-K for the year ended December 31, 2018 filed with the Securities and Exchange Commission. In addition, certain non-GAAP financial measures will be discussed during this call. These non-GAAP measures are used by management to make strategic decisions, forecast future results and evaluate the company's current performance. Management believes the presentation of these non-GAAP financial measures is useful to investors understanding and assessment of the company's ongoing core operations and prospects for the future. A reconciliation of these non-GAAP measures to the most comparable GAAP measures is included in today's press release regarding our quarterly results.

And with that, I'd now like to introduce Erez Raphael, Chief Executive Officer of DarioHealth. Mr. Raphael, the floor is yours.

Erez Raphael – Chief Executive Officer

Welcome and thank you for joining our call today. I would like to thank our stakeholders, including vendors, strategic partners, shareholders and our Board of Directors for their contribution to the success in driving the business forward this quarter.

In addition, I would like to congratulate the DarioHealth's team, for the time intelligence and passion, as we work hard together to continue to transform value into digital therapeutics company, well-positioned for success in chronic disease management.

This transformation including both our product offering, and our channel strategy. As mentioned in Q1 earnings call, we began an evolution of the product offerings from a medical device to a software driven model. We believe the software solution with an open platform is superior to one of the required specific device, as it allows patients to choose the device, the company to quickly deploy a greater technology, and create the opportunity for the company to have a higher active margin profile overtime.

This product evolution also continues to show signs of progress in terms of having a better solution for patients as evidenced by recent clinical data we will highlight later in this presentation. This evolution will continue in the second half of 2019 and beyond, as we will always walk for improving our solution for patients who seek help from Dario's to manage to their chronic diseases.

In addition, our company evolution includes how and to whom we sell our products as well. This evolution started from a model that focused solely on the direct-to-consumer channel, to one that spends and more of its resources, both human and financial capital, on the business-to-business channel. As previously stated, we believe the B2B channel will be the big part of Dario's future, complimenting on our best-in-class direct-to-consumer strategy, and driving results going forward.

Dario initial strategy focus on direct-to-consumer allowed us to gain valuable insights, while building an industry leading platform. Unique in its robustness, global scope and evidence of improved clinical outcomes. We continue to see superior user engagement, which is essential to our strong clinical efficacy, and likely fair adoption for reimbursement. In addition, we continue to experience strong customer retention, indicating the patients like the platform and are committed to using it for healthier management of their chronic condition.

Finally, we position Dario membership for higher average revenue per user, ARPU, with the launch of the hypertension and the expansion into the B2B channel. The interest of employers, payers and healthcare providers in our chronic illness management platform has been aided by the growing pool of data evidenced demonstrating improvement in clinical outcomes on the behavioral modification that occurs using our Dario solution.

Dario published at the ADA of 2019, the results of a study of 38,838 active Dario type 2 diabetes users over two years, 2017 and 2018. It shows 19.3% reduction in the average ratio of hypoglycemic events, and an increase of 11.3% in normal range readings. The most significant shift in results, 14% decrease in higher ratings, occurred after only one month of usage and this lower level was maintained through the remainder of the user alone [ph] subscription period.

Most importantly, we published the study in 2019 that allows number of valid users with type 2 diabetes can lower their average blood glucose to equivalent of 3 diabetes level, which is 140 milligrams per deciliter. Thirty percent of type 2 users using Dario without coaching published [ph] ADA 2019 and 45% of type 2 users, while receiving additional support from Dario coach, AADE 2019.

But why all of these clinical results would use by Dario system is so important for all healthcare, stakeholders, patient provider and players? HbA1c levels are marker [ph] for diagnosing and analyzing the treatment of type 2

diabetes patients. It is well-known that when patients are compliant with the physician instructions, i.e., high engagement of managing the disease, they can meaningfully reduce HbA1c level. It is also well-known that 1% or one point growth in Hemoglobin A1C, HbA1c levels can decrease diabetes related death by 21%, decrease [ph] micro vascular complications by 37% and decrease a myocardial infarctions [ph] by 14%. Dario high engagement digital therapeutics platform can help them achieve the slower HbA1c levels and the associated health benefits.

Notably, type 2 diabetes patients are asymptomatic until [indiscernible] develop later in the disease progression. But it becomes very expensive and difficult to meaningful reverse the progression or simply manage the disease. Unfortunately, even the asymptomatic nature of early type 2 diabetes, patients often don't manage their disease well while only directed by the physician. They don't see a visible reason to skipping an insulin injection that would keep the blood sugar levels in the healthy range since you have no noticeable implications [ph]. And skipping one injection may reinforce the concept of non-compliance of insulin therapy, is okay. Resulting in the behavioral of skipping insulin injection.

For example imagine, putting a mandate on warrant one that you can't see, why would you do it or even consider it being necessary? However, by ignoring the disease or physician care instruction, type 2 diabetes progresses with each and needed missed insulin injection. I think this understandable [ph], reasonable patient behavior is where Dario can be most useful. We believe this is where Dario is essential to patients' health. DarioHealth patients recognize and quantify the disease and the management of it. It helps patients understand their implications of being noncompliant with the physician care instructions and it helps complements physicians instructions in between patient appointments, which mean they missed reschedule or scheduled to fall apart, Dario reinforces overall patient care for type 2 diabetes patient.

If Dario is able to stop the decline from pre-diabetes to asymptomatic diabetes or symptomatic diabetes or reverse the progression of disease altogether, not only would we provide the patient better health life, we would also reduce healthcare system costs. There could be a few diabetes related events and related to acute care provider visits. There could a few diabetes comorbidities [ph] to manage and related physician appointment there maybe a few prescriptions and we could help provide those managed patients between in person appointment as a result or we might be fewer in office appointment. All this would lead to a lower healthcare system costs, something very valuable for both private and public players.

Our scalable digital therapy platform also enables us to move beyond diabetes management into additional chronic condition field. The first of this is our entering into the hypertension management field, with a release of Dario Blood Pressure Monitoring system, with 73% occurrence of hypertension among diabetes patients, this is a natural transition for Dario. And it's expected to further drive users' engagement and ARPU.

By synchronizing the Dario Blood Pressure Monitoring system data with the Dario mobile app, users can track their blood pressure, variety of first markers, together with the daily action of stimuli that influence them. Utilizing the Dario Blood Pressure Monitoring system together with the Dario Blood Glucose Monitoring system creates a harmonized digital therapeutic solution, enabling users to better monitor their health and making firm data driven choices. Together with Dario software and professional coaching, we expect that users with hypertension and diabetes will benefit from a clear growth picture of the condition in a user friendly format on the iPhone or Android mobile devices.

A key competitive advantage of Dario of value driver for our platform, is our global footprint with CE Mark in Europe, recently introduced basic connectivity ensures compatibility with our latest Android devices, allowing reengagement with value users with new smart phone who were previously incomparable. An estimated 60 million in Europe suffers from diabetes and this is an important milestone and re-informs our leadership position in the region.

During quarter two, the Dario platform was adopted by three major clinic systems and dozens of smaller clinics, through our existing alliances and with our new ones under negotiation. We expect to gain access to a series of midsized sales and a number of employers and several hundreds of clinic. In addition, Dario being evaluated by four life science companies looking for a digital therapeutics companion for their product.

Going forward, we are going to leverage our market leadership and growing users' base, to meet certain demands for digital therapeutics and value based healthcare in reducing effects of chronic illness.

Now, I would like Olivier to share more details and early progress from Dario's D2C and B2B, channel strategy. Olivier?

Olivier Jarry - President and CCO

Thank you, Erez. Indeed, in digital therapeutics, we show growing interest from business-to-business clients, because they want clinically proven results. There are many digital companies trying to sell some kind of digital health program, particularly to employers, virtually none of them can demonstrate values remarkable level of clinical outcomes in diabetes, previously mentioned by Erez.

I would like to take the following moments to share more information about the different channels, we will be setting values offering through. First, we continue to be excited about the large direct-to-consumer market opportunity. Patients are becoming more informed over time about their treatment options, taking control over the management of their illnesses. We benefit from this markets tailwind and we will continue to refine our strategy with higher year to our marketing dollars over time.

Regarding employers and payers, Dario can report positive traction with two major payers that are covering several dozen million lives and have approved Dario's DTx solution. Now that we are approved on their platforms, we are working with them to penetrate their patient population. We have also just signed a large employer, and we are finalizing agreements with a couple others. We anticipate a similar process here with [indiscernible] approval, followed by patient pool penetration. Employers and payers will remain a major focus in Q3 from signing agreements to building the user base.

Clinics in North America continue to show a very strong interest in Dario, such as at the 2019 conferences of the American Diabetes Association, and the American Association of Diabetes Educators, AADE, where we received dozens of expressions of interest. As a reminder of the reason for this interest, Dario is the only digital therapeutics company that connects healthcare professionals to the entire lifestyle data of their patients via the Dario cloud, in real time, and through a browser. The latter a major argument these are cyber security protocols. Of note, we are not competitors to clinics, but rather complement our management of chronic disease in a favorable way that results in positive clinical outcomes.

At retailers, we are converting our offering from the classical meters and strips to what we call membership in a box. Users will be able to buy from their favorite retailer, install on the internet the same three months membership that they may buy today from Dario's internet channels. Being able to see the actual product physically displayed and explain in pharmacies will be an important factor for users to make that choice along with a blood pressure meter connected to Dario. New large retailers, like the fresh approach from Dario and are evaluating it. Retailers also like that when visiting the store, patients interested in Dario will drive and see their store [ph] purchases.

On the strategic side, we are in advanced discussions with the hospitals and pharmaceutical, nutrition and medical devices companies. They realize that their products will be much more successful if they are part of a digital therapeutic solution that will enhance awareness, education, engagement and loyalty from their users. And

importantly, Dario will provide intimate insights, the identified [ph] about very large numbers of users. Such patient insights are quite inaccessible today, for these life sciences companies.

I would like to turn the call back over to Erez to discuss Dario's quarterly financial performance.

Erez Raphael – Chief Executive Officer

Thank you, Olivier. Before highlighting specific quarter two results, I would like to make some high level comments on our performance and what you should expect of Dario in the future. In general, our new products are being sold to direct-to-consumer channel, need an investment from intent to grow the revenues. With those investments as will fall, this is the reality of the direct-to-consumer channel.

Now we experience during the second quarter was consistent with that reality, we invested less in direct-to-consumer activities during this quarter, and as a result, anticipate a lower direct-to-consumer sales levels. However, we're willing to sacrifice this and with this sales [ph] as we focused on our broader strategic operating plan.

As we strategically shifted focus by reallocating resources and investments to our more lucrative and less expensive business-to-business channel, we saw expenses decline materially while the timing and the size of B2B sales are initially less predictable. The cost of pursuing sales in these categories is less expensive, since it's involved in negotiation and education, but not significant in the individualized marketing spend.

Dario anticipate lower expenses this quarter, and benefited from that B2B reality. We envision that lower expenses structure will continue in the second half of this year and also in the future.

While we did not yet achieve significant revenues related to a higher focus on the B2B channel in Q2 of 2019, because of the shortfall in the D2C sales, we do anticipate our investment in the business-to-business channel producing revenue in the second half of this year. Overtime this strategy in these wins will produce attractive [indiscernible] cash flow streams from large patient pools managing their chronic diseases, covered by employer or payers.

Now I'd like to hand over the call to Zvi Ben-David for a few highlights on our second quarter of 2019. Zvi?

Zvi Ben-David – Chief Financial Officer

Thank you, Erez. Here are some highlights from the second quarter of 2019. Revenues for the second quarter ended June 30, '19, were \$1,651,000, a 25% decrease from revenues of \$2,242,000 in the first quarter ended March 31, 2019.

In addition, in the second quarter, we recorded an increase of \$102,000 in our deferred revenues. Deferred revenues were generated from sales of our membership offering to our customers in the United States and Australia.

Gross profit in the second quarter of 2019 was \$326,000 compared with gross profit of \$558,000 in the first quarter of 2019, and compared to a gross profit \$522,000 in the second quarter of 2018. The decrease in our gross profit in the second quarter was attributed to lower sales, and one-time expense write-off of our old cartridge production load [ph] for \$82,000.

Operating loss for the second quarter ended June 30, '19 decreased by \$431,000 to \$5,360,000 compared to \$5,800,000 in the second quarter ended June 30, 2018. This decrease is mainly due to the decrease in our operating expenses.

Net loss attributable to holders of common stock decreased also by \$456,000 to \$4.5 million in the second quarter of 2019 compared to \$5.8 million in the second quarter of 2018. As of June 30, 2019 cash and cash equivalents totaled approximately \$8 million.

I'll now turn the call back to Erez for some concluding remarks.

Erez Raphael – Chief Executive Officer

In conclusion, Dario has developed a software driven digital therapeutics platform that engages patients to be more focused and systematic about managing their chronic disease. This treatment compliance helps patients achieve happier, healthier lives and with healthier lives all healthcare stakeholders benefit from a lower cost.

In this quarter, Dario expanded and improved its digital therapeutics platform while pushing forward its strategic operating plan through the next stage. We are proud of the progress we made, as we assess the global healthcare market and the Dario place in it, we are more confident that over that we have built a platform technology which will deliver better care and lower cost for patients with chronic diseases.

We are excited to share more developments from the B2B channel strategy over the remainder of the year and we believe the test development will generate double-digit top line growth in combination with much lower losses, creating significant value for our shareholders.

To conclude our prepared remarks, I would now open the call for questions. Operator?

Operator

Absolutely. Ladies and gentlemen, the floor is now open for questions. [Operator instructions]. And our first question comes from Alex Nowak, from DarioHealth. Please state your question.

Q: I'm actually from Craig-Hallum Capital Group. Erez, can you provide a bit more color on the revenue shortfall this quarter. I understand shifting initiatives away from the DTC to the partnership model. But then did the DTC side of the business experience a higher churn than previously, in prior quarters. I understand you probably didn't sign up as many DTC customers this quarter but shouldn't the existing DTC users stay in the platform and continue to generate consistent revenue going forward?

Erez Raphael – Chief Executive Officer

Alex, thank you for the question. This is an important one. So, looking on the revenue, there are two reasons why we see this shortfall. Number one is accounting reason. Not every user that we are signing up as a member, we can recognize the revenue immediately. So this is something that provide out of the reason for the, I think, in some ways the optic issue.

The second issue is, that when we are having DTC users, we have two types of users. We have those that are members and members are still having a very high retention, actually, we are improving the retention, we're improving the outflow of those that are members. And we have users that are what we are calling them, device users. They are getting on the platform, we are interesting [ph] them with the device and we are then converting them to be members.

The revenue of users that are coming as a new device holders and are not signing up yet on the membership, this is something that was reduced as we will do less buying from the mid of this quarter, when we started this transformation. So, practically we see a reduction in those that are one timers, we don't see a reduction in the members. Actually the members are still providing the high ARPU, and we are improving this ARPU. And we think that it will be improved over time. And because of the nature of the accounting plus the fact that the

members are still on the platform, we do think that moving forward into Q3 and Q4, we're going to see a recovery of the revenues back to higher numbers because of these two reasons.

Just also another reminder, we started to sell yearly membership only in early Q3 last year, and we're going to see all these renewals getting back to the platform and renewed in Q3. So Q3 will change this optic reality to be more positive.

And I think that the when we are talking about the product, its stickiness, the average revenue per user, plus the churn, I think that for our members it's improving. And just to remind you, when we are selling B2B, we are selling mainly memberships, which means that if the product is good as an improving, we're going to see much higher ARPU and we will start intensively selling on the B2B part.

So, the one timers that are buying devices, this is something that we'll selling less. Members is still sustainable and actually we haven't seen a decline in our number of members on the platform.

Q: Okay, got it. So, understood, [indiscernible] going through a bit of a transition here. When should you complete the transition to B2B, or maybe asked a better way is, when will the B2B offset the DTC declines?

Erez Raphael – Chief Executive Officer

Thanks for the question, so first of all we're not going to shut off the D2C, we think that the strategy of the company staying on DTC keep selling and I mean the DTC is where you all confronting with your users and you need to make them happy. If they are not happy they are not buying your device, your membership. And this is where I think this is what makes us a very good organization that is improving the offering quarter-to-quarter. So this is something that will stay and will be sustained and grow not in the same intensity that we had so far.

With regards to the B2B, we believe that moving forward Q3 and Q4 we're going to see the beginning of the growth and we think that the offset will be done in the next two quarters. So while we will get back to some kind of growth. And as I stated in my script, we think that we're going to see the double-digit growth this year. But in parallel, I think that we can be much more efficient in terms of our losses and I think that we're going to improve in a very drastic way our bottom line in the next two quarter.

So, on one hand we will get back to the trajectory of growing and on the other hand we will do it in a much lower cost structure, which will reduce our losses and we believe we will provide value for shareholders, because we didn't feel very comfortable with the high burn rate that we had and we had to do something that will change it. We don't see it yet in Q2, because all transformation was done now, but in Q3 and Q4 we're going to see it big time and we think that it's a very positive change that we did and it will provide the right value to shareholders.

Q: Okay got it, and what are the metrics we should use here to help benchmark your move into the B2B model? Can you say how many partners do you have in total with clinics or employers that you're involved with? Just any metrics that help us get comfortable over the coming quarters that Dario is exceeding in its pivot towards B2B?

Erez Raphael – Chief Executive Officer

Yes, absolutely. We think that moving forward we will focus more on the number of clients, we can talk in terms of number of payers or employers. We already have in the pipeline, we're going to see the first user getting on the platform practically as we speak. So this is something that we feel comfortable. We have a nice pipeline of client that already signed with us, when we are in implementation [ph] stage.

We need to feel more comfortable and to see that it's getting into more sustainable and more robustness in terms of clients and we think that within the next two quarters we will start publish information on the number of clients

and then we can start create metrics that related to clients and number of members, B2B and DTC and it will be much easier to provide sustainable metrics. I think we will do it in the next two quarter absolutely.

Q: Okay, that's helpful. And then Olivier, you mentioned you got approved with two payers. Can provide some more color on what that means? Are they actively paying for your solution to their members and is this a pilot phase with the payers or is this a full program?

Olivier Jarry - President and CCO

That's another good question. One of the payers is what we would call a tier 2 very significant, very innovative payer. They are actually now working on lists of users that at some point should come to Dario. So we consider these very concrete and hopefully we see the results in this Q3 if not delayed to the early Q4, but Q3 should be the time when these come to the platform.

The other one I mentioned is a large one and their model is a bit different, they are taking into their own clients, employers. And we have to teach to these employers in order to then get the employees in turn. So, we have a number of these multi-level cases that take more time, but with the support of the organization we signed with, we get lot of interest from the next level, so just a lot of work.

Q: Okay got it. And then just last question for me and a little bit of follow-up to Erez your previous comment there. But, when should the existing cash last you through given the switch to B2B in the lower burn that you mentioned?

Erez Raphael – Chief Executive Officer

Yes, according to the report that we published, we stated that really is well the cash will be sufficient for [ph].

Q: Sorry, you say through breakeven or through the end of 2020? I missed it.

Erez Raphael – Chief Executive Officer

We said until April next year.

Operator

[Operator instructions]. And our next question comes from Steven Wardell. Please state your question, Steven.

Q: So, I'd just like to know, can you go over with us where do you see the growth coming from in the next 12 months? So, what product or products, what region or regions, what sales channel or channels do you see the growth coming from? Thanks.

Erez Raphael – Chief Executive Officer

Thanks, Steven, we see the growth coming from in terms of regions, mainly from the United States and from the UK. And in terms of the channels, the majority of the growth will come from the B2B accounts. And with regards to the offering it's going to be a membership for Dario digital therapeutics, which is what we are selling now indirect to consumer which is transforming into B2B as well, with a higher pricing because we are selling a premium membership. And the membership includes application, unlimited strips [ph], the coaching, and all the digital intervention capabilities that we are providing through the app.

This is something that we already see the first members getting on the platform as we speak. And we think that this is where we're going to get the majority of the revenue, and this is something that will be supported by the DTC that will also contribute some level of sustainability or growth and store growth supporting the B2B. So it's mainly B2B US, mainly from sales [ph].

Operator

Thank you. And our next question comes from Ben Haynor. Please state your question, Ben.

Q: First off for me is, the membership in a box, that sounds like an intriguing offering. Just curious on what the reception has been with potential pharmacies, retailers, etc., in terms of being able to get shelf space and the receptiveness to it?

Olivier Jarry - President and CCO

Actually [overlapping voices]. Yes, no, I was going to take this one. Actually, interestingly, it's one of the very large chains. When we expose the way that we work and kind of offering we have also DTC that told us and it's a very large one. And we [ph] told us, guys, why should you continue selling meters and strips, this is way, way more interesting. And I want to see more, I want to see mockups, I want to see how it looks on the shelves. And we've started to work with them on this.

And we were almost surprised by the quality of its reception. We made another presentation that two days ago to another chain that also received very, very positively and the one that we publicized a couple of months ago, we are converting them as well and they say guys, well, it's almost like why did you wait, this is really making a difference. And they say it as a kind of a renewal rejuvenation of this diabetes space.

That is a little bit of that section of the store today where you have all these big meters that all look the same. And they are cumbersome and very key [ph] and you have to carry them around. And when you have these very attractive things that catch your attention first, and then you realize that it's not only your meter, it's really the entire benefits of the digital advice behind it in terms of nutrition, exercise and controlling your weight, your blood pressure. So it's much more than a meter. And it's a convenience of the membership. You don't even have to think about, you are becoming short of strips, for example, for your blood glucose meter. So I would say we're almost surprised how positive they were to convert to membership in the box.

Q: That's great, very helpful. And then lastly for me, what's been the reception to adding the blood pressure monitor and hypertension management tools to the B2B customers thus far?

Olivier Jarry - President and CCO

A little bit of the same.

Q: More potential customers, I guess as well.

Erez Raphael – Chief Executive Officer

Go ahead, David [ph].

Zvi Ben-David – Chief Financial Officer

No. Go ahead.

Olivier Jarry - President and CCO

Yes, for them, it's going into a holistic way of managing the patient. And if you go today to a drug store, you'll see the section as I said, of blood glucose meters, you walk a few steps, you'll see another section of blood pressure meters, it's not much more fun and attractive. And it's disconnected. And what we now explain through our marketing materials is with high comorbidity of hypertension and high blood glucose, and you should manage both, and you have these two devices that connect to Dario and then the app, gives you all the means to manage both together.

So for them, it's a continues [ph] of a previous story. It's not a piece of devices here and where people don't really know what to do, it's seeing [ph] that our input of data into an app that is really going to help them. So, we see it as almost like a needed addition because there're so many people with diabetes, but also have hypertension, more than half, closer to three quarters.

Operator

And there appear to be no further questions at this time.

Erez Raphael – Chief Executive Officer

Thank you so much, and have a good day.

Operator

Thank you. Ladies and gentlemen, this does conclude today's teleconference. We thank you for your participation. You may disconnect your lines at this time and have a great day.