Transcript of
DarioHealth Corporation
Third Quarter 2020 Earnings Call and Webcast
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Participants

Glenn Garmont - Investor Relations
Erez Raphael - Chief Executive Officer
Rick Anderson - President & General Manager, North America
Zvi Ben-David - Chief Financial Officer

Analysts

Scott Schoenhaus - Stephens Inc.
John Vandermosten - Zacks Small Cap Research

Presentation

Operator
Good day, ladies and gentlemen, and welcome to DarioHealth Third Quarter Conference Call. As a reminder, this call is being recorded. At this time, it is my pleasure to turn the floor over to Glenn Garmont, Investor Relations. Sir, the floor is yours.

Glenn Garmont - Investor Relations
Thank you, [Dogma] [ph], and good morning, everyone. Thank you for joining us today for a discussion of DarioHealth's third quarter 2020 financial results. Leading the call today will be Erez Raphael, President and Chief Executive Officer. He will be joined by Zvi Ben-David, Chief Financial Officer; and Rick Anderson, President and General Manager of North America.

After the prepared remarks, we'll take your questions. An audio recording and webcast replay for today's conference call will also be available online as detailed in the press release invite for this call. For the benefit of those who may be listening to the replay or the archived webcast, the call is being held and recorded on November 12, 2020.

This morning, we issued a press release announcing our financial results for the third quarter 2020. A copy of the release can be found on the Investor Relations page of DarioHealth's website.

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-Q for the quarter ended September 30, 2020 filed this morning.

Additional information concerning factors that could cause results to differ materially from our forward-looking statements are described in greater detail in the company's press release issued today and in the company's filings with the SEC.

In addition, certain non-GAAP financial measures may 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 for 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 like to introduce Erez Raphael, Chief Executive Officer. Erez?

Erez Raphael - Chief Executive Officer

Thank you, Glenn, and thanks, everyone, for joining our call this morning. Also joining me today is Zvi Ben-David, who is the Chief Financial Officer, and Rick Anderson, the President and the General Manager for North America.

During the third quarter, we continued to make our progress on the 3 main pillars that we have discussed in our previous calls. The pillars that we believe that are going to pass into our leadership position in the digital therapeutics space. The first one is the transformation into a SaaS, Software-as-a-Service, where we are generating recurring high-margin revenues.

The second pillar is the expansion into multi-chronic conditions. We started with diabetes. We extended into hypertension and we keep extending into behavioral health with a comprehensive solution, state-of-the-art user experience and very engaging experience.

The third pillar is the transformation from direct-to-consumer into Business-to-Business-to-Consumer. And it's the third pillar in particular that we feel that we made the significant progress this quarter.

Rick will elaborate about it shortly and Zvi Ben-David will cover the financial aspect. But before, I'm handing over to Zvi and Rick, I want to provide few highlights.

Number one on the revenue, during the third quarter of 2020, we exceeded $2 million in revenue, compared to $1.78 million that we generated in the second quarter, which is overall 14.2% sequential increase. And while we are pleased with our progress on the revenue, we are – the story here is not that revenue impact and it's more about the opportunity that is in front of us, and particularly, in light of the transformation that we are doing on direct-to-consumer into Business-to-Business.

And we feel that we have a lot of traction that we got with employers, insurers and providers. And we believe that this something that will drive a meaningful and significant improvement in our revenue in 2021 and it's going to create value to our shareholders.

On the operating loss, during the third quarter, we generated an operating loss of $6.6 million that represents a sequential increase of $4.1 million that we had in the second quarter. So while the increase in the operating loss is something that we expected and it's because of the additional expansion that we are doing in establishing our overall operation in the U.S., specifically building our overall sales team. And we expect that as we move forward and start to generate the most significant revenue on the B2B2C, we're going to see that these expenses, so these losses are going to be deducted.

With regards to the margins, the margin declined to 26.9% in Q3, in comparison to 35.6% that we had in Q2, the decline is the result for onetime and sales that we are doing on the direct-to-consumer where we are providing specific promotions when we are selling devices. As stated in previous calls, we believe that once we are successfully making the transformation into B2B2C, we're going to see that the margins are going to get back to a positive trend of improvement. And we believe that overall, we're going to get to margins that are north to 70% for our SaaS model, selling our premium membership into the B2B2C.

Overall, on the transformation into the business-to-business, we have seen growth activities in all 3 main challenges under which we are operating, the insures, the employers and the providers. Overall, the pipeline was increasing from a $200 million that we reported in the second quarter to $350 million that we are reporting now. And overall, we see that in each of the 3 channels that I just mentioned employers, providers, and insurers. In each of them, we have deals that are either in negotiation, or in final stage of contracting. So we are very confident in our path forward.

And it's clearly that our best-in-class user experience that is reflected in multiple ways from the app store with 13,500 reviews with 4.9 stars, the Net Promoter Score of 77. This is something that resonated very well, not just among our 63,000 active paying users that we have on the platform, but also among clients that we are currently negotiating with or contracting with.

And our recently announced deals that we had with HMC in the expansion of the relationship with Vitality Group, is just 2 examples of the momentum that we are creating. Another thing that is happening in the market, and we want to give some light about that is the overall transformation of the market into digital and digital therapeutics is something that big companies that traditionally operating as a medical devices companies, pharmaceutical companies and specialty care providers are realizing that companies and the clients are looking to solutions that are much more digital. And it's not just about creating a medical device that it's connected, it's much more than that.

It's about managing the whole lifecycle of the user, managing the daily routine of the user, which is something that require a strong technology, a software centric technology that integrating device applications and also coaching. And we have seen that these giants that used to dominate the space of diabetes or hypertension are looking to make this transformation into digital. And for them it's a straightforward process to work with companies that already established with a very strong technology in the digital therapeutics space. And this is something that we consider as an opportunity for DarioHealth.

And we are having several discussions and it might create additional ability to accelerate the penetration into the 3 channels that we have by partnering with bigger companies that already have a presence to the market. So this is something that should go in parallel to what we are already doing in the 3 channels that we are penetrating.

On the balance sheet, we ended the quarter with $37 million in cash as followed to a fundraising that we did by the end of July when we raised in an oversubscribed deal $28.6 million. The use of proceeds, as discussed in previous calls is, number 1, to make sure that we will be able to implement the accounts that we are signing on establishing a very strong client success team in the United States and coaching teams and this is something that we are ready and we are already implemented.

Number 2 is growing the sales team and operating in these 3 channels in parallel in a very focused way. We put resources in each of these channels. Rick will elaborate about it later, but further penetration into employers, plans and providers is something that required strong teams that will focus on each of these channels separately. And number 3 and very important is expanding the offering and making sure that the offering will be a state-of-the-art in terms of experience, and in terms of personalization, investment into data and AI. And we feel that this is something that we know to do very well, so additional deployment of capital is going into this direction.

One more initiative that I want to mention here is the boost that – something that will boost our overall positioning as a B2B2C digital therapeutics company that is a leader in the space is the establishment of the Scientific Advisory Board under the leadership of Eric Milledge that agreed to join our Scientific Advisory Board into serve as the Chairman of the Scientific Board. Eric [float in] [ph] the healthcare industry all his career, used to work for pharmaceutical companies, medical devices companies, and build vast experience and a lot of relationship across the healthcare landscape.

Eric will work together with the Scientific Advisory Board closely with our research and development team in order to strength our roadmap and in order to implement it, specifically helping us expand our portfolio into integration with CGMs, which is something that we believe for the medium- and the long-term is important for our platform. And Eric will also work with the team in order to generate data and clinical excellence that will help us strengths and achieve potential clients on the B2B2C channel.

So overall, the primary objective behind the Scientific Advisory Board and behind Eric nomination is to create awareness in the market, and specifically help us accelerate adoption of our digital therapeutic solution into the B2B2C market.

With that, I would like to hand over to Rick – the call to Rick to elaborate on the B2B2C. Rick?

Rick Anderson - President & General Manager, North America

Thanks, Erez. In addition to our legacy direct-to-consumer model, we are pursuing 3 channels as part of our ongoing transition to a B2B2C company, health plans, self-insured employers, and remote patient monitoring with providers in health systems. And to bolster these efforts in the past quarter, we have expanded our commercial team by more than a dozen individuals. This means we now have a Dario sales team covering each channel. We believe this enhances our ability to address the strong interest that we've seen across the channels and best position as for long-term success. For example, in the third quarter, we had to reallocate sales resources from the RPM channel to cover the high level of interest we received from health plans.

I'm pleased to say, however, that we have now added 2 senior sales executives with substantial experience in the provider space to lead our sales effort in the RPM channel. We are also adding operational resources to ensure smooth and seamless onboarding processes for the new clients and members, including implementations already underway.

Let me begin the channels with self-insured employers. During the first quarter of this year, we announced that we had entered into a strategic collaboration with Vitality Group, a leading health and wellness company focused primarily on the self-insured employer market through its many employer customers, Vitality solutions touch more than 20 million people across 24 markets globally.

This collaboration represented a significant step forward in our transition into a B2B2C company. Vitality's customers have access to a curated ecosystem of wellness and health solutions for their employees. And their platform provides integrated incentives and rewards for healthy behavior.

As a data-driven platform, we regard Vitality as a perfect complement to what we're doing. As an extension of this collaboration, we recently announced that our digital therapeutics platform was selected after a rigorous evaluation by Vitality to be integrated into their new Gateway Flex offering. Gateway Flex is a new package that is designed to address the needs of a largely remote workforce. It provides simplicity to employers by bundling many benefits into a single contract, and is cost effective since employers pay only for those programs in which their employees engage.

We believe our industry leading consumer engagement metrics, combined with our open architecture that allows for seamless integration within an increasingly complex health benefits ecosystems were key factors in our selection. In light of the challenges brought on by COVID-19 and the massive impact that has had on the growth and acceptance of remote workforces. We believe the Gateway Flex will be well received and we look forward to providing future updates.

During the third quarter, we also announced a partnership with HMC Healthworks, a premier national provider of population health care management programs with a significant presence in the labor market and more than 1 million members under management. HMC is offering our digital therapeutics on both a standalone basis as well as incorporated into HMC solution. And we are already seeing customer interest through this partner. We currently completing contracts with employers that we anticipate being able to announce soon, especially for those who are including Dario in their new benefits cycle starting in January.

We are very encouraged with our success in the employer channel in 2020, including RFP wins against some of our biggest competitors. This is especially true given that we missed much of the 2020 sales cycle due to the team joining Dario only this year, and the impact of the pandemic. We look forward to having increasing traction in 2021 sales cycle begins in the first quarter.

With respect to health plans, as Erez indicated, we continue to advance discussions and contract negotiations with several large insurers. And even though the timing on some have slipped past what we had initially anticipated, we have advanced additional deals through the pipeline for a net increase in our opportunity. While the sales cycles with health plans is typically quite long. We are very encouraged by the significant traction that has gotten in this channel in just the last 4 months. We believe we are on track to announce multiple healthcare planning contract wins between now and early 2021.

Turning now to our provider-centric initiative, I am pleased to report that with the initial success that we saw in our remote patient monitoring solution last quarter, continued into the third quarter. This solution is a key differentiator for our company. Recall that effective January 2020 providers can build Medicare under several new remote patient monitoring codes for up to $1,800 per monitored patient per year. We expect physicians to continue to adopt this new technology and this new revenue stream quickly, and we anticipate RPM will be an important growth driver for our company for years to come.

As we indicated last quarter, we are seeing a strong interest in RPM as a result of the pandemic, and with case counts once against rising in many parts of the country. We expect that interest in this solution will continue to grow.

Lastly, we continue to maintain our relationships with the retailers as part of our direct-to-consumer sales channel. We do not anticipate devoting significant resources to the retail channel in the coming quarters. But we are continuing to have discussions with a few large industry players around some more strategic opportunities. Overall, we have continued to expand our sales pipeline by more than $150 million in the third quarter alone and move deals into contracting across all of our channels as prospects respond favorably to our product offering.

While COVID-19 pandemic continues to divert time and attention with some customers, we are in late-stage contracting discussions with multiple entities and we expect to have customer announcements this quarter. And we believe that we have set the stage for a more significant growth trajectory in 2021. Being able to demonstrate strong clinical outcomes data, high member engagement and high member satisfaction is key to our supporting customer adoption in all of our channels.

And I am pleased to report that we continue to expand our data in each of these areas. We added to the already significant scientific evidence supporting our solution in August, when we – when our poster titled impact of digital management on clinical outcome in patients with chronic conditions, diabetes and hypertension was accepted for presentation at the Association of

Diabetes Care and Education Specialists 2020 Annual Conference. The results from this study of people who utilize Dario digital therapeutics platform for diabetes and hypertension management demonstrates and compelling reductions in blood pressure and glucose levels, including a full stage reduction in some hypertensive patients.

That study adds to our previous presentations at the American Diabetes Association 80th scientific sessions in June 2020. In all, we now have 14 clinical studies that support the benefits of our digital therapeutics platform. These studies continue outcomes over 2 years and up to 38,000 users. These large studies with long-term outcomes data provide strong support for pair adoption with the Dario solution. The clinical results speak for themselves and improved long-term clinical outcomes drive real cost savings across the healthcare system.

At this point, I'd like to turn the call over to Zvi for a review of our financials. Zvi?

Zvi Ben-David - Chief Financial Officer
Thank you, Rick. I will now provide a brief overview of our financials. Additional details on our results can be found in our Form 10-Q filed earlier today. Revenues for the third quarter exceeded $2 million and increased from $1.78 million in the second quarter. Revenues were again derived mainly from the sales of our products and form the offering of our membership plans to our customers in the U.S. We did anticipate and are seeing more the sequential revenue growth through the back half of this year, reflecting our continued transition to a SaaS revenue model, we expect this to continue through Q4.

Gross profit for the third quarter ended September 30, 2020 was $549,000, a decrease of $324,000 or 37%. On gross profit of $873,000 for the third quarter ended September 30, 2019. Gross profit margin was 26.9% as compared to 46.7% in the third quarter of 2019, and 35.6% in the second quarter of 2020. Our non-GAAP marketing expenses for the third quarter ended September 30, 2020 was $3.1 million, as compared to $1.7 million for the third quarter ended September 30, 2019.

We used $3.8 million to fund our operations during the third quarter ended September 30, 2020, as compared to $2.6 million we used to fund our operations during the second quarter ended June 30, 2020. As of September 30, 2020, we had cash and cash equivalents totaling $37 million. This includes gross proceeds of $28.6 million from a successful private placement that we closed in July.

I will now return the call back to Erez.

Erez Raphael - Chief Executive Officer
Thank you, Zvi. So in summary, we are very pleased with the progress that we made in Q3 of this year, and also in the rest of the year. We are successfully executing on our growth strategy, we're executing on our plan and we are gaining a lot of momentum on all channels, including health plans providers and employers. And we're also very well-funded in order to execute on our plans. And we have the right talents that are joining our team. And we feel that we are very well positioned to be successful in the B2B2C space.

We also as followed to the momentum winning clients, and we believe that in the next few weeks, in the next few months, we'll be able to make more announcements on the wins that we are making. So with that, I'd like to hand over the call to the operator for the Q&A session.

Operator
Thank you. The floor is now open for questions. [Operator Instructions] Our first question comes from Scott Schoenhaus. Please state your question.

Q: Erez and team, congrats on the results and the new deal wins. My first question is for Rick actually. You mentioned in your prepared comments RFP wins against competitors and a strong pipeline.

Are these also – these strong pipeline, are these also against competitors? And what is helping you win these RFPs? Is it price, technology, combination of both? Just want to understand the competitive landscape. Thanks.

Rick Anderson - President & General Manager, North America
Sure. Thanks for that question. In terms of the pipeline on an overall basis, some of that is RFP based. Some of that is just direct sales where folks are looking at our solution. But the competitors are always in the background, whether it's an RFP process or not. We anticipate we'll see more and more RFPs, as we move into the normal cycle for sales to employers.

Starting in the first quarter, people are really right now implementing those solutions that they purchased. But in the meantime, we've also been able to move forward deals. What we're finding in the marketplace is, is that the company is well positioned from a product perspective in terms of the broadening offering that we're providing.

We have diabetes with the traditional market. We've added hypertension. We're in the process of adding weight management, pre-diabetes, and people are liking that approach. But really, a lot of the things that are resonating are the clinical data that I talked about. The reduction of A1Cs that we're seeing in those studies are best in class. People are impressed with how large those studies and the longer-term nature of those studies, because that demonstrates real world outcomes.

And the NPS score that we have, the Apple App Store, 4.9 out of 5 stars, now for more than 13,000 ratings. It keeps going up, really speaks to how much people like the solution. But also the fact that we have a direct-to-consumer business, where we have tens of thousands of people that are paying out of their pocket for this solution, just screams engagement to people.

And there's more and more recognition in the marketplace. That is engagement is important. So when people really look at it, we've got a product that, by the numbers is exceeding our competitors in the marketplace.

On the flipside to that, we are positioning the product from a price perspective in an attractive way. And the fact that we are looking to build for people that are engaged in the process, rather than just everybody, is being well received in the marketplace in an overall basis.

Q: Great. Thanks for that color, Rick. Second question is for you, Erez. Can we talk about the M&A environment for chronic digital health companies like Dario? Since the merger of the Livongo and Teladoc has now been closed, do you expect large telehealth platforms to look at acquiring digital therapeutic platforms in order to compete more effectively against Teladoc? Thank you, guys.

Erez Raphael - Chief Executive Officer
Okay. Yeah, thanks, Scott, for joining in the call and thanks for the question. Actually, we see a lot of things that are going on in the market. So the Livongo and Teladoc is one example, because when you are looking into chronic condition management, it's about surrounding the user 24/7 with a technology that is very engaging, and in fact, handing over some empowerment and responsibility to the user in order to scale up treatment.

So it was very appealing to telemedicine companies. And we feel that these companies are looking into and make more acquisitions on this chronic condition management. But it's not only them. And one of the things that I mentioned earlier on the call is also traditional medical devices companies that use to dominate diabetes space, for example, or the hypertension space that are looking into going digital as well.

So we feel that we're going to see acquisitions that are coming from this kind of players, including telemedicine or medical devices, as well as pharmaceutical companies. That's one direction. Another direction that we see is consolidation of companies that are integrating solutions together and getting a more comprehensive chronic condition management platform.

And one of the things that we built in a very smart way is a platform that is open, which means that if we want to integrate additional chronic conditions, that's something that we can do in a more easy way. And we feel that the future market, a year, 2 years from now is going to be multi-condition. And that's what the second pillar that we talked about. So we're going to see one consolidation.

And, number 2, acquisitions of big players that are acquiring, in most of the cases, those that are doing what we are doing, in most of the cases, we are relatively small players if we put aside Livongo. So we definitely think that that's the direction of the market.

Q: Great. Thank you, guys. Congrats on the results again.

Erez Raphael - Chief Executive Officer
Thanks, Scott.

Operator
Okay, our next question comes from John Vandermosten. Please state your question.

Q: Good day to everyone. And thank you for taking my question. First is on just the number of active users. Erez, I think I heard you say there were 63,000. Can you elaborate on that a bit and break that down at all? And are there any other stats on subscribers that you can provide?

Erez Raphael - Chief Executive Officer
Yeah, so actually, we had growth in the users. And as you know, on the direct-to-consumer we are – in order to sell our membership we're tell selling the device, and then we are selling users to buy the membership. So the overall proportion that we have from – between membership to device users that are generating less revenue is a proportion that is more or less the same as what we have seen in the previous quarter, of 60-40.

And as we move forward, that's something that we stated also in previous calls. We're going to look in parallel to the transformation that we are doing into B2B2C. We are looking into close the platform for membership only. So on average, moving forward, you're going to see that the revenue that is generated, the ARPU average revenue that is generated per user per month is going to get higher and higher, and as we will see more percentage of members comparing to the overall users.

So this is the growth that we had, that is in line with more or less with the overall goals that we had with the revenue. But in terms of getting a bigger portion of the membership out of the overall population, this is something that we will – again, once we are getting more traction on actual higher revenues on the B2B side.

Q: Okay. And hypertension has been available for a while. And I was wondering if you could give some early observations on how that's trending, how that's picking up.

Erez Raphael - Chief Executive Officer
Yeah, absolutely. So also here, I mean, that's something that we are commercializing now on the B2B2C. We created – I mean, this is something that we launched, I think second half of last year. And we started to create traction. We started by selling only the device and application.

In the last 4 months, we started to turn it into a membership, which is our pillar number 1, make everything SaaS and everything under membership. So this is something that is moving forward, I would estimate that around 5% to 7% of the revenue is coming from hypertension. And we feel that that's something that – is something that will get bigger percentage as we move forward into the B2B2C.

I mean, most of the cases we're having – when we are having discussions with clients, employers and friends, the hypertension portion is there. So we believe that this is something that as we move forward is going to get like 20% of the business. When we are looking on diabetes and hypertension, that is the overall expectation in the next 2 years.

Q: Okay. And is there any hypertension that stand alone or is it usually paired with diabetes?

Erez Raphael - Chief Executive Officer
Yeah, so on the direct-to-consumer, we are selling it as a standalone. It's not necessarily paired with the diabetes. Also, on the B2B2C side, we are selling it as a standalone. But one of the big advantages – and this is our big belief and philosophy, that when it comes to chronic condition management, you should provide a personalized solution.

So the big advantages that we are creating is by creating it as the comorbidity. So on the integration, diabetes and hypertension for users that are suffering from more than one chronic conditions, this is where we see more advantages. And this is something that resonates among clients that we are selling for.

And in some of the RFPs that we participated and some of the sales that we are doing, we are having discussions on – starting with diabetes and then moving into hypertension. But this is something that is a very important part of the overall value proposition, the intersection between the chronic conditions. But each of them can be sold as a standalone.

Q: Okay. Great. And last question is on the gross profit margin and that's been volatile – Zvi, I think this is probably for you. That's been pretty volatile over quarters. Is that related to a timing issue? And will that settle out in future periods?

Zvi Ben-David - Chief Financial Officer
Well, as Erez presented it earlier, currently, because we are mostly on the B2C side and we are doing those promotions. So it's a temporary effect that we, of course, expect to change as the B2B opportunities will start to translate into dollars.

Q: Great. Thank you. That's all for me.

Operator
[Operator Instructions] Okay. And it doesn't look like you have any further questions.

Erez Raphael - Chief Executive Officer
Okay, thanks, everyone for joining the call. Bye-bye.

Operator
Thank you. This concludes today's conference call. We thank you for your participation. You may disconnect your lines at this time and have a great day.