Event Transcript

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Start of Transcript

Operator: Thank you for standing by and welcome to the Healius Limited investor update. All participants are in a listen-only mode. There will be a presentation followed by a question-and-answer session. If you wish to ask a question you will need to press the star key followed by the number one on your telephone keypad. I would now like to hand the conference over to Healius's CEO and Managing Director, Dr Malcolm Parmenter, please go ahead.

Malcolm Parmenter: Thank you and good afternoon, everybody. Thank you for making the time in the last few days leading up to Christmas. We apologise for making announcements like this right on the cusp of Christmas, but these sorts of things tend to have their own agenda so they happen when they happen. I'm sure you're all looking forward to a break, even if it's affected by the various travel requirements we have in place across the state.

As you would appreciate from the current COVID case numbers, particularly in New South Wales, we here at Healius are experiencing another new year period of high levels of testing in our laboratories and on that point, I'd like to take this opportunity to thank our dedicated team who've done so much and continue to do so much to help the national effort against the COVID-19 pandemic.

So it's both an exciting and a relevant moment for us to announce a transaction that will significantly grow and evolve our capabilities and portfolio, especially as a laboratory services provider. Healius has entered into a definitive agreement to acquire Agilex Biolabs, as you will have seen in our announcement today, and Agilex is one of Australia's leading bioanalytical laboratories. This is an important and strategic acquisition for Healius, that provides us with an immediate platform for growth in the clinical trials pathology sector.

Our clinical trials represent a global market made up of global biotech and pharmaceutical customers, who are required by regulators to investigate new vaccines and drugs for safety and efficacy through human trials. Bioanalytic laboratory services, such as provided by Agilex, are fundamental to the results of these trials. Over the course of this presentation we'll take you through more detail on why the clinical trials sector is attractive and why Agilex is the right platform asset for Healius to participate in this market.

I have with me today our CFO and COO, Maxine Jaquet, and General Manager of Corporate Development, Mark Ellis. We'll take you through the key transaction details, provide an overview of the business and some key market metrics. We'll also answer any questions you may have at the end of the presentation.

On page 4 of the transaction overview, as mentioned, Healius is acquiring 100% of Agilex Biolabs. This sector is an area of healthcare that I know well from my time at Sonic Healthcare. Additionally, we have spent considerable time conducting market research and commercial due diligence on the clinical trial sector over the past 12 months. Our findings have been that it's a high growth adjacency to our core laboratory business and has strong tailwinds and fundamentals.

Through the search we've found that Agilex is one of the leading and largest bioanalytical laboratories in Australia and I'll outline shortly what has specifically attracted us to Agilex. But in summary, we view this as a long-term and highly strategic acquisition for Healius. Agilex is a business that is growing fast within a market of clinical trials that is also growing fast, but globally and particularly in Australia we believe it has a strong future earnings growth potential.

Central laboratories providing clinical trials pathology services are a natural fit for a general pathology business like Healius. Along with Sonic Healthcare, a number of other laboratory businesses around the world provide these highly specialised central laboratory services, including Quest and Labcorp.

In terms of key transactional details, we're acquiring the business for cash at an enterprise value of $301.3 million. We're debt funding the acquisition from existing and new debt facilities provided by our current lender group, and we expect leverage post-completion to remain comfortable and less than 2 times Group EBITDA. We expect to complete the transaction at the end of January 2022, next month, subject to customary conditions precedents being satisfied.

On page 5 there is strategic rationale. The strategic rationale for this acquisition, we are confident that Agilex is a great business and is a great acquisition for Healius for a range of reasons. It provides an Australian platform for growth into a global clinical trials market. We believe this presents attractive growth opportunities for Healius, as we'll explain in a moment, Agilex has realised impressive growth in the last few years and has built out its capabilities and testing technology, therapeutic areas and business development to continue that growth trajectory.

Agilex is a high margin and capital-light business, which is attractive and provides a good balance with Healius's existing cash generative and mature businesses. We believe the business offers a strong and exciting platform for growth. Agilex provides some further revenue diversification for Healius and introduces a range of new customers, including global biotech, pharmaceutical and clinical research organisations. Our research tells us biotech and pharma R&D is growing and is increasingly being outsourced for speed and cost advantages. Agilex is a beneficiary of these structural trends, and we'll describe this in more detail shortly.

We think Agilex brings some important innovation and scientific R&D capabilities to Healius that adds to our existing strengths in genetics and histopathology. We believe this will not only enhance both Healius's pathology and Agilex's service offerings, but it also enhances our employee value proposition, especially for scientific and laboratory staff. In a domestic market where such labour is scarce, we don't underestimate this benefit. We also know that our doctor referrers and patients value a diagnostic service provider that is participating in cutting edge clinical research.

We see a future of precision medicine that is founded on clinical research, genomics and diagnostics and with this acquisition we are excited that Healius is on a path to build that future in Australia. We see Agilex as offering very complementary capabilities alongside our existing core pathology business. Healius can also offer Agilex a wide pool of scientific staff, laboratory operational excellence and support services. We see it aligned with our vision to be a best-in-class healthcare laboratory and diagnostics player across multiple verticals.

Now I'd like to give you a better sense of Agilex as a business, if you turn to page 7. The first thing to say is that it's a large and at scale player in a fragmented market. It is one of the leading bioanalytical labs in Australia, with over 100 scientific professionals. Agilex primarily supports biotech and pharma clients in preclinical Phase 1 and Phase 2 trials across both small molecule and large molecule work.

Agilex's capabilities span a broad range of therapeutic areas and has a particularly strong experience and exposure to oncology, which is the largest therapeutic area globally. The business has an extensive library of assays and a wealth of experience. There are returning clients, demonstrating high customer satisfaction with the laboratory services provided.

The business is primarily based in Adelaide, with additional operations in Brisbane. Importantly and as a function of growth momentum in the business, Agilex is undertaking a facility expansion with additional floorspace secured adjacent to its existing Adelaide facility.

It is well run by an experienced management team with strong scientific credentials, and we are pleased that the management team will be remaining with the business and welcome the CEO, Jason Valentine and his experienced team into the Healius Group.

Turning to page 8, Agilex is experiencing strong growth momentum in its business, as you can see from the planned work chart. Planned work includes contracted and uncontracted but verbally awarded work that Agilex is yet to deliver. Total planned work has grown substantially over the last period, highlighted by the growth from $23 million in June this year to $36 million at the end of November. Revenues have been increasing over time, as this planned work is performed.

On page 10, the global market for bioanalytical laboratory services is found within the R&D spend for pharmaceutical and biotech sponsors, so are developing new therapeutic drugs and vaccines. Those sponsors increasingly are outsourcing the project management of clinical trials to contract research organisations or CROs and the associated bioanalytical laboratory testing to service providers like Agilex.

To give you a sense of the magnitude of this market, our research indicates that global pharma R&D was over $200 billion in 2021, with around 25% of this being outsourced to CROs and clinical research labs. This outsource component has been growing at around 7% a year, as sponsors continue to pursue faster and more reliable clinical trial outcomes. Speed to regulatory approval and market is obviously key to the economics of drug development.

There is growth across many therapeutic areas, with oncology the largest segment. As you saw from the earlier page, oncology is also Agilex's largest therapeutic area, accounting for about one-third of its work. We're particularly excited about this, given the global market characteristics and we believe that Agilex is the leading Australian biolab for oncology.

Australia is an attractive destination for clinical trials, with some unique advantages, this is on page 11. Most importantly, that is speed and quality. Australia's TGA has one of the fastest regulatory processes in the world for clinical trials, four to six-week start-up times for Phase 1 trials versus up to six months in the US, which is a significant advantage for drug sponsors who are very focused on speed to market for drug development work. Additionally, Australia is fortunate to have a very high quality medical research sector and internationally recognised accreditations that are accepted by all major international regulators.

There are some cost advantages, including tax incentives, although these aren't a primary driver. It is really about speed, quality and trust and that trust can take a long time to achieve and Agilex has been on this journey for 25 years. All this is expected to translate into continued high growth over coming years for Phase 1 and Phase 2 Australian drug trial starts.

So in summary, we feel strongly that the acquisition of Agilex is a compelling strategic and operational fit for Healius. It provides Healius with a high growth platform in the clinical trial sector, a sector that we have spent considerable time researching and that we consider to be attractive and growing. It adds to Healius' innovation and scientific capabilities and provides a global orientation for the Healius network in terms of the future pathology partnerships and customer markets. We consider it to be financially compelling, given its high margin and capital light business model, offering additional revenue diversification and complementary capabilities. Thank you for listening to that and we're now happy to take any questions that you might have.

Operator: Thank you. If you wish to ask a question, please press star-one on your telephone and wait for your name to be announced. If you wish to cancel your request, please press star-two. If you're on a speakerphone, please pick up the handset to ask your question. Your first question comes from Lyanne Harrison of Bank of America. Please go ahead.

Lyanne Harrison: (Bank of America, Analyst) Good afternoon, Malcolm and Maxine. I'm going to start with revenue and the revenue profile for Agilex and on page 8, obviously some very good growth there in terms of planned work. But can you give us some colour in terms of what Agilex has achieved in terms of year-on-year revenue growth? And more particularly, obviously the 55% growth in the last five months, obviously prior to that it was very much impacted by COVID with clinical trials all but coming to a halt. Can you give us some colour on that and also what your expectations are for the next six to 12 months, particularly as Australia goes through more COVID cases?

Maxine Jaquet: Thanks, Lyanne. I'll take them and Malcolm may add. I think the best way to look at it, we look at the current win rate of work that is occurring currently, which is around about $5 million a month. Then we're looking at the - if you just took the market growth and said that's somewhere between 14% to 17%, that gives you the best guide. So we think just in terms of basic market growth we've certainly got a strong revenue trajectory and that's without even growing into some of the areas that we will be building capacity in. It's also constructive to look at the pre-COVID growth rates for this sector, which were mid-10s as well. So if you look at those 2015 to 2019 numbers, they're also sitting at around the 15% growth rate. So I think that's the best guide in terms of looking at revenue growth.

Lyanne Harrison: (Bank of America, Analyst) Okay and just to clarify, when you talk about this transaction being EPS accretive in its first year, you're assuming that it will continue to grow at that 14% to 17% rate of growth over calendar year 2022?

Maxine Jaquet: Yes, that's right.

Lyanne Harrison: (Bank of America, Analyst) Okay, thank you and then can you also talk to us about the pipeline? So obviously a very good pipeline in there in terms of current levels of planned work. What else is in the pipeline? And can you talk about probability of success when you work with some of these, whether it's existing or new customers?

Malcolm Parmenter: Yes, the really strong thing about this business is their catalogue of biomarkers and tests that they've already done. Many of the tests that they do with new compound testing, where they take on these, requires the development of a completely new bioassay to do that. That's not easy to find, that kind of skill and Agilex has one of the largest libraries of those kinds of things in Australia. So when a biotech or a pharma company is looking to set up an assay for a particular compound, then it's the speed at which you can get that up that drives the volume that you can do.

The library is critical to driving that outcome and the speed to market from the biotech's perspective is critically important as well and it's those things together that keep the work rolling in. The trials tend to be - they can be relatively short, but there is a very large number of them and it's been growing strongly for quite a long time. And all of the research that we've done around this, looking at this globally, is that the Australian market will continue to grow and will continue to drive this business forward.

Maxine Jaquet: A lot of the pipeline work is also underpinned by repeat custom as well, which makes up a fairly sustained proportion of the work as well. So there is a good confidence in delivery in the business as well. So when we look at that pipeline, we have quite a degree of confidence around that.

Lyanne Harrison: (Bank of America, Analyst) Okay, thank you and before I leave it to the other analysts, there was no mention of synergies. Can you provide some colour in terms of whether it be cost or revenue synergies?

Malcolm Parmenter: The synergies between this business and a general pathology business, it's not the sort of business that you can merge with a general laboratory. So you don't tend to get cost synergies from that perspective, in that it is a highly specialised service that is very different from anything that we've offered before. Having said that, there's a whole lot of expertise that exists in both businesses that can provide benefits both ways, in terms of specialised pathologists, in terms of their knowledge, scientific staff within our labs, genomics in terms of some of the larger molecule bioassays that are done.

So there's a whole lot of crosspollination that occurs between these two businesses that we believe will drive revenue going forward. There's a pretty decent track record worldwide of general laboratory businesses and clinical trials businesses doing exactly that. There are many general pathology businesses that also operate a clinical trials business around the world.

Lyanne Harrison: (Bank of America, Analyst) Thank you very much.

Operator: Thank you, your next question comes from Bosco Feng of Goldman Sachs. Please go ahead.

Bosco Feng: (Goldman Sachs, Analyst) Hi team, thanks for taking questions. Can you hear me?

Malcolm Parmenter: Yes.

Bosco Feng: (Goldman Sachs, Analyst) Perfect. I just had two questions today. Can I ask, firstly, what is the market share for Agilex in the bioanalytics market currently in Australia? I'm just trying to assess the scope for organic growth, both domestically and internationally, if there are any advantages in building out a global business in this particular industry.

Malcolm Parmenter: Okay, sorry, we were just discussing what the market share was. What was the second part of that question, Bosco?

Bosco Feng: (Goldman Sachs, Analyst) I'm mostly asking for the market share in order to understand the organic growth in this particular market.

Malcolm Parmenter: Our analysis suggests that the market share that Agilex has is about 33% of the clinical trials pathology market in Australia. But a lot of that work is not just trials that are being done here, a lot of that work is coming out of Asia, out of China, out of the whole Asia-Pac region and being shipped into Australia as part of that. So it's not just research that's being done here.

Bosco Feng: (Goldman Sachs, Analyst) Okay, got it, that's helpful. And finally, if I take the 14% CAGR and the volume of drug trials done in Australia and compare that to the 17% CAGR that you've disclosed for the business, I know it's of slightly different timeframes but I'm leaning roughly 3% pricing growth due to mix or otherwise. Is that a fair characterisation of this business, perhaps historically and then going forward?

Maxine Jaquet: Going forward, it's quite possible that we could see an acceleration of that beyond the 14%. It's just what we're using as a guidance around what we think it could be. We're hoping that it'll be higher than that and it'll be mainly volume, not price.

Bosco Feng: (Goldman Sachs, Analyst) Got it, that's perfect, thank you.

Operator: Thank you, your next question comes from Andrew Goodsall of MST Marquee. Please go ahead.

Andrew Goodsall: (MST Marquee, Analyst) Thanks very much and thanks for taking my questions. Just following on from the last questions, I just didn't get - it wasn't clear to me what the geographical split of the revenue is. If you could just give us a sense of Australia versus rest of the world or US as well.

Maxine Jaquet: Sure, Andrew. So if you took Asia excluding China, it's about 14%, China's about 30%, US about 30%, ANZ 17% and Europe 10%.

Andrew Goodsall: (MST Marquee, Analyst) Okay, just getting that down quickly but sorry, I missed it, 10%, was it?

Maxine Jaquet: China are about 30%, US about 30%, ANZ about 15% to 17% and Europe 10%.

Andrew Goodsall: (MST Marquee, Analyst) Okay, got it, thank you very much. I guess just on depreciation, obviously it's capital light, but just the split. If you could just help us understand the split of assets versus intangible mix within the $300 million and then perhaps whatever small impact there is on depreciation and right of use.

Maxine Jaquet: Yes, sure.

Andrew Goodsall: (MST Marquee, Analyst) Just modelling plugins, if you could.

Mark Ellis: Andrew, it's Mark Ellis here. There's about $10 million of tangible assets in the business.

Andrew Goodsall: (MST Marquee, Analyst) Right, okay, so the rest's intangible, so pretty minor impacted…

Mark Ellis: Yes.

Andrew Goodsall: (MST Marquee, Analyst) Any sense just around the A, what that's going to look like?

Maxine Jaquet: Around, sorry, the what?

Mark Ellis: A, amortisation.

Andrew Goodsall: (MST Marquee, Analyst) The amort.

Maxine Jaquet: It would be negligible.

Andrew Goodsall: (MST Marquee, Analyst) Just in terms of I noted management staying on, some time back we covered Mayne Pharma when they acquired a business that was involved in clinical trials and there seemed to be a lot of work tethered to some key personnel who, I guess, were just very, very well regarded in their industry. Would you describe this business as having characteristics like that, where the reputation of some of the individuals is a key part of the marketing or the business wins?

Malcolm Parmenter: Yes, the business has been in place for 25 years and the personnel have evolved and changed over time. But yes, there are key people within that business that keep it going. But they have been able to evolve over time and for those people, as they move to other careers to rotate that through. Adelaide has really developed some expertise around the whole clinical trials market in terms of research and has become quite a centre for that. So the business has shown an ability to recruit the right people and to stay stable over quite a long period of time, through other ownership structures indeed.

Maxine Jaquet: One of our areas - that was supported by one of the areas of commercial due diligence around surveying biotechs and also pharma companies and the reputation of Agilex, which was very, very good. So we're all really pleased about the search.

Andrew Goodsall: (MST Marquee, Analyst) Is there any earn-out or any other sort of lock-in for retention of those key personnel?

Malcolm Parmenter: Part of the consideration for the CEO is deferred over three years.

Andrew Goodsall: (MST Marquee, Analyst) Okay, so that's a payout that's measured on any particular targets?

Maxine Jaquet: It's only time based.

Malcolm Parmenter: He has equity in the business that's being sold, so part of that is routine.

Andrew Goodsall: (MST Marquee, Analyst) Okay, terrific, thank you very much. I'll get back in the queue, thank you.

Malcolm Parmenter: Thanks, Andrew.

Operator: Thank you, your next question comes from Gretel Janu of Credit Suisse. Please go ahead.

Gretel Janu: (Credit Suisse, Analyst) Yes, good afternoon, everyone. Just firstly, you've given the pre-AASB 16 EBITDA estimate. Do you have it on a post AASB 16 estimate, or have I missed it somewhere in the release?

Maxine Jaquet: No, you haven't. We haven't given it, but we don't think it's going to be materially different, Gretel. We'll get to it but we're not thinking it'll be materially different.

Gretel Janu: (Credit Suisse, Analyst) Perfect, thanks and then just in terms of the customers, can you give a little bit more detail about the number of customers, repeat versus new customers? Are you exposed to a handful of customers, does the handful make up a large proportion of the work? Just trying to understand a little bit more about that customer base.

Maxine Jaquet: It's geographically diverse. There is a good number of repeat customers, it's nicely spread, there isn't a core risk in terms of the revenue profile. Importantly, in terms of therapeutic areas, it's, as we mentioned, quite a substantial presence in oncology. A smaller but growing presence in infectious diseases and then dermo and gastro are smaller parts of the business. So a really good mix in terms of those therapeutic areas and a good diverse geographic profile.

Gretel Janu: (Credit Suisse, Analyst) Excellent and then in terms of the key areas of growth, is it just to expand more into the individual therapeutic areas? Are you planning to expand into new areas? Where should we think about the growth areas here?

Malcolm Parmenter: The business has had a focus on small molecule up until now and the vast majority of its work has been there. It has recently acquired a toxicology business which those skillsets will be able to be utilised across the whole of the Agilex business. Then a growing interest in large molecule research and starting to work more in there and we see that as definitely a growth area going forward.

But one of the big areas of growth in terms of research is in the oncology space, which is its real focus. If you look internationally, all of the indicators are that that will continue to be an area of research going forward. It isn't a business that's benefited enormously from vaccine development, for example, for COVID. So the revenue that it currently has, that is not the major contributor to where it is, it's much more in a diverse pattern of diseases and quite broad in terms of the services that it provides.

Gretel Janu: (Credit Suisse, Analyst) Great, thanks. That's all I had.

Operator: Thank you, your next question comes from John Deakin Bell of Citigroup. Please go ahead.

John Deakin-Bell: (Citigroup, Analyst) Thank you, I was just interested if you could give us a little colour on the process. Is this a competitive process or were you - this was in the newspapers a month ago or so, but just give us a sense and then I'll get to the next question, which will be about the returns, but maybe if we can just start with that.

Malcolm Parmenter: Yes, it certainly was a competitive process that went down to the wire. We're not really privy to exactly who else was there or what was offered, but it was certainly competitive.

Maxine Jaquet: You saw the 360biolabs business which we obviously participated in that process, it was competitive. Nucleus Network, although not related, but not exactly the business again, quite a competitive business and a competitive process for that business.

John Deakin-Bell: (Citigroup, Analyst) Okay and just trying to get down to an EBIT number here, you're saying that depreciation, amortisation is negligible, so let's just say for argument's sake it's the same. So you've paid 20 times, so your EBIT return on invested capital's 5%, which on our assessment is less than the cost of capital. Can you just give us your thinking behind how you justify paying that price for an asset?

Maxine Jaquet: Yes, it's the growth. Well, it's two things actually, it's the margin and the growth that we see in that business and where we see it going. We're obviously not buying it at a single point in time and we've taken a view on what market growth is, what the current capacity in the business is to deliver on that growth. The current performance around pipeline and conversion and concluded that where we think that business is going to get to even over the near term will be a very attractive asset for us to own and will produce good returns.

John Deakin-Bell: (Citigroup, Analyst) Okay and is there any CapEx? What would an ongoing CapEx be in the business? Not very much, I'm assuming.

Maxine Jaquet: It's not actually.

Malcolm Parmenter: It would be minimal, you could say probably $2 million per annum.

John Deakin-Bell: (Citigroup, Analyst) Okay, thanks very much, that's all I had.

Operator: Thank you, your next question comes from David Low of JP Morgan. Please go ahead.

David Low: (JP Morgan, Analyst) Thanks very much. Malcolm, at the beginning you said that you had a good understanding of this business from your time at Sonic. Can I get you to talk a little bit about how it compares to their operations? Are they a player in the market as well?

Malcolm Parmenter: Yes, they are, David. Sonic was the Australian agent for, I think it was Covance way back, in terms of providing central laboratory services. When Covance set up a Singapore laboratory, Sonic set up Sonic Clinical Trials here in Sydney and developed a clinical trials business from scratch. It took quite a long time and it was profitable by the time I left there. I had responsibility for that, I don't really know what's happened to it since then, but Sonic does have this capability in other locations as well, including London and perhaps the US as well.

Agilex is significantly bigger than any of those businesses that Sonic had, albeit I'm talking four years out of date here in terms of where it was back then. So these businesses, despite the fact that they have low capital requirements to set up, take a very long time to actually win the trust of the biotechs and pharma companies that are entrusting their trial to your laboratory in terms of where it is. It can take a long time to actually win customers over, because at the end of the day price is not the big issue here.

The speed to market is a much bigger factor when it comes to clinical trials pathology, which is why the margins are so much better in this space than they are elsewhere, it's not that competitive when it's all said and done. If you've got a library like Agilex has, it's very difficult for any other central laboratory to compete with that, given the speed to market, the cost of setup, how quickly you can get the trial done and get these things set up in the space of three, four, five, six weeks and have the trial operating in that period of time. That's the critical factor that drives this and it's why it's attractive for us. It's an area that's growing much more strongly than general pathology does, it's got much better margins than general pathology does and it's an area which is less competitive.

David Low: (JP Morgan, Analyst) All right, that was very useful, thank you. I would like to test on that Covance experience, so I was going to ask about CROs and then doing their own lab work. Do you worry at all about increasingly the trial work gets outsourced to CROs who can have their own capacity?

Malcolm Parmenter: It's actually not easy for CROs to do that and it's not easy for CROs to have their own lab, because they generally don't. Unless they're huge, like IQVIA or Covance, they don't generate enough work of their own to be able to operate a lab like this and to have the kind of skillset and command the personnel that you need to actually do it. You need referrals from multiple CROs and Phase 1 research units to actually do it and if you do own your own CRO, you tend to end up with a channel conflict in that space that has other CROs not willing to use you.

So where Agilex thrives is that it is nimble and can do all these small trials, whereas the IQVIAs and the Covances are signed up to large multicentre Phase 2 and 3 clinical trials that are run all around the world and they specialise in that. That doesn't mean that we could get into Phase 2 if we had labs in other jurisdictions, but right at this point in time Agilex is pretty much focused on Phase 1.

Australia has become quite a destination for that and certainly the quality of the work that's done here is what's attracting work into a nimble and as the name of the business suggests, agile laboratory that can do those smaller trials and do lots of them that are coming through from biotech. The other part that's happening in the market is the amount of capital that's available for biotechs to take their products deeper into the product development range. Twenty years ago it tended to be that biotechs would need to, or institutions with a product would need to seek out a pharma company to take their product forward and to take the risk with it.

Well these days raising capital is a lot easier for many of these organisations and they tend to run their own Phase 1 trials and they look for a CRO and then separately a laboratory to provide these services for their Phase 1 and often their Phase 2 as well, in terms of these products. So it is an area that we think will continue to grow and certainly all of the research that we've done supports that.

David Low: (JP Morgan, Analyst) All right, thanks. Can I change topics completely? We see MYEFO come out yesterday, we saw a release from the Government on COVID funding a week or two back before then. Can I just get you to talk a little bit to the implications of any funding changes please?

Malcolm Parmenter: Yes, the MYEFO statement, I don't think it was actually in the statement, but our understanding is that the fee for a COVID PCR will drop from $100 for the full fee to $85 for the full fee. Of course, we get paid 85% of that and then there's an [episode] fee and a bulk billing incentive that sits on top of that that lifts it by about another $10 or $11 above that amount. So over time the cost of doing the test has come down a bit, I think, for most providers and certainly with the volumes that we've been seeing, as we've reported on previously suggests that labs get a fair bit of efficiency with those kinds of numbers of tests coming through.

And as you might imagine with where we are now, the pressure's starting to come on again in terms of volumes and growing volumes across pathology and I'm sure all providers are experiencing that right at this point in time. So I think the margins in terms of testing will still be pretty strong at that level, given that costs come back a bit as well.

David Low: (JP Morgan, Analyst) Thanks, Malcolm. I'll just stretch it out to one more and I'm just interested in your crystal ball, so we are seeing COVID numbers rising rather rapidly. Do you worry that a lower virulent omicron strain, such as it may or may not be, could lead us to the point where we just don't care anymore and that frankly getting tested is - so many cases out there that if we stop requiring the need to test?

Malcolm Parmenter: The only thing I'd say to that is if you want to look at what happens in terms of behaviour and where it goes in terms of the virus, we've got examples in the Northern Hemisphere of exactly where that goes. So testing rates in the UK, despite rapid antigen testing being freely available, with free kits handed out at train stations and available in pharmacies and everywhere else, COVID PCR testing is still very strong in the UK and still running at just below peak levels. I haven't seen the numbers actually in the last two or three weeks of numbers really skyrocketing there again, but my guess is it's probably gone up again there.

So I think PCR testing will remain the diagnostic test. I think rapid antigen can be used for screening, but as came out on the Service New South Wales app today, a rapid antigen test is not a diagnostic test. If you're symptomatic, it's almost pointless having a rapid antigen test. If the rapid antigen test is negative, you don't know that you don't have COVID, because there are plenty of cases where it's been negative where people actually do have it. Secondly, if it is positive, you then need to go and have a PCR to have it confirmed, so you may as well have a PCR in the first place, as the advice from the New South Wales Government today says.

So I think PCR testing remains central. I don't see a situation where doctors stop looking for it. There will still be vulnerable people in the community. Omicron and whatever the next 10 variants that turn up over the next two or three years will all have their pluses and minuses to them. It may be that we get to the point where psychologically we've moved on to the point where, as individuals, we start worrying less about the virus and I hope that is the case, to be honest. But I don't see a world where doctors stop looking for COVID.

David Low: (JP Morgan, Analyst) Thanks, Malcolm, very generous.

Operator: Thank you, your next question comes from Saul Haddasin of Barrenjoey Capital. Please go ahead.

Saul Haddasin: (Barrenjoey Capital, Analyst) Thanks, good afternoon, I'll keep it to two questions. Malcolm, I'm just wondering how scalable the current Agilex lab is. I noticed there's some buildout of capacity in Adelaide. In terms of increasing that revenue base, how much higher can that revenue grow based on the current facility assets that you have in Adelaide and at the Brisbane lab too?

Malcolm Parmenter: They have taken on, as we've said in the presentation, they've taken on a considerable amount of additional space in Adelaide, which will more than double the space that they've currently got. They have acquired I think TetraQ, the toxicology business in Queensland as well. So they do need to recruit more people to get there, but they have a track record of having done that over the last 12 months and been able to deliver on the professional people that they need.

So we think its ability to continue to grow at double-digit percentages each year is absolutely there and we've convinced ourselves, looking at that business and what's planned down there and the pipeline that's coming and the market that sits there, that that will happen. That's where we've got to and that's where the valuation comes from. It's not really about its EBITDA in calendar year 2022, albeit that that's important, it's where it goes after that that drives the price being paid.

Saul Haddasin: (Barrenjoey Capital, Analyst) Just one other, in terms of the - you mentioned some inorganic opportunity as well for growth. Is that referencing potential acquisitions within Australia? Or do you see this as a potential platform to grow in terms of your physical presence into labs outside of the Australian region?

Malcolm Parmenter: Well, we're just buying into Australia now, so we're not in a rush to go out and buy internationally. But the reality is that there is an opportunity, just as BioAgilytix has done quite recently, to get into the Phase 2 clinical trials market where you have one of these labs in Europe or the UK and one of these labs in the US and those labs are then instead of harmonised, which means the equipment is quality tuned to producing the same results to have identical labs on the same laboratory information system in each of those locations linked together that can provide identical results in each of those locations. Then to go after the Phase 2 work, which are bigger trials and allow you to take on work that is significantly greater value in terms of the kind of volume that comes through with that.

So yes, there is an opportunity, absolutely there is an opportunity to do that and we have done quite a bit of work around looking at this as a platform for growth, to look at that international market in terms of what might be available, in terms of potential targets at some point down the track. But right at this point, our focus is on getting the growth out of Agilex and getting it to where we know it can go.

Saul Haddasin: (Barrenjoey Capital, Analyst) Great, thanks.

Operator: Thank you, your next question comes from John Copley of Evans and Partners. Please go ahead.

John Copley: (Evans and Partners, Analyst) Good afternoon, Malcolm and Maxine. I know there's already been a question on the multiple pay, but I was just hoping you could help us out a little with the growth prospects. So specifically whether you expect that you'll be able to grow this business ahead of the market and if so, why and what the drivers might be there. And maybe if you haven't already, just touch on the revenue and cost synergies. I know they weren't really called out but are they going to be expected to be material? Thank you.

Malcolm Parmenter: I think in terms of where the market goes, there's a few things that are driving that. It's not just the growth in the biotech and clinical trials market, it's the fact that the pathology services are being increasingly outsourced as well, that drives the laboratory component of it to grow faster than the market is growing. I think in the graphs that we've shown there you'll see the percentage that's outsourced progressively growing over time and that has quite a significant impact on where it goes. I think Agilex is ideally placed to grow at a faster rate, given its library of work.

Maxine Jaquet: We've factored in, in our view, that it will grow at market and we're obviously looking at specific therapeutic areas and what the growth is in those, which is certainly higher than that 14% to 15% which positions Agilex in a very good place. But I think in terms of setting expectations, I think if we kept it at that sort of rate then that would be a sensible assumption to use in terms of what the forward revenue would be.

John Copley: (Evans and Partners, Analyst) Thank you, noted. So they're the therapeutic areas on slide 10, right?

Maxine Jaquet: Sorry, what was that?

John Copley: (Evans and Partners, Analyst) They're the therapeutic areas on slide 10 of the presentation?

Maxine Jaquet: Yes. Oncology is obviously one of the highest growth areas and where Agilex is very strong. Also infectious diseases they do have a presence but vaccine development is also something that will be a focus for calendar year 2022 and growing our presence in that. Certainly a lot of work has come to Australia, so Australia certainly has benefited, given COVID, as a destination. Agilex hasn't been a significant beneficiary of that to date, but we believe that will be a growing area for the next at least year.

John Copley: (Evans and Partners, Analyst) Okay, thank you and if I could just sneak in one more, Virtus announced today that they'll be terminating their agreement to acquire Adora Fertility. Can you give us a little more information on why that was terminated? Specifically under the share sale agreement, what particular terms allowed Virtus to end that agreement, noting that it was originally stated to be binding and not conditional upon regulatory approval? Thank you.

Malcolm Parmenter: We don't know a lot more than you do about the real reasons for bailing on the deal ahead of the ACCC announcement. So Virtus has obviously got a few things going on right at this point in time, so I'm not sure what amongst all of those things that would be. We went through a variation of the deal about a month ago, that given the length of time that the ACCC process was likely to take, if it did go to a Federal Court, it could well take several months to get through that process before you got an outcome for that.

And there was an exit for Virtus related to a material adverse event clause that we didn't want to continue to participate in the sale process if that was still there, given the length of time that it was running for. So this mutual exit component for a short period of time before that took effect was in there and then obviously the bid from Virtus came along and they've made a decision of their own. I'm not sure, you'll need to ask them why that is, but we have other options in this space. So rather than sitting here for months doing that, we'll pursue those.

John Copley: (Evans and Partners, Analyst) Okay, sorry, I recognise I'm extending my welcome here with too many questions, but you mentioned it was mutual, the termination?

Malcolm Parmenter: Sorry, no, the termination was Virtus's decision to do that. They made that decision and notified us last night.

John Copley: (Evans and Partners, Analyst) Okay, all right, but I take it then that you're not aware of any allegations they've made about what might have been told to them about the business, then they've just decided to be able to terminate this under the share agreement based upon the terms of that agreement. Because it just seemed as though when it was originally put out that it was not conditional upon regulatory approval, that's all.

Mark Ellis: That's correct, it wasn't conditional upon regulatory approval. But in the face of an injunction from the ACCC, that binding commitment all the way effectively. So we sought to deal with that, as Malcolm has said, by the mutual ability to walk away. But it was Virtus who exercised the ability to walk away and we believe that it was primarily ACCC-driven, no other reason.

John Copley: (Evans and Partners, Analyst) Okay, thank you. That's all from me.

Operator: Thank you, your next question comes from Shane Ponraj of Morningstar. Please go ahead.

Shane Ponraj: (Morningstar, Analyst) Thank you, good afternoon. Based on the estimates for next year, you've got 40% EBITDA margin on a fairly small top line for Agilex. I guess based on your experience at Sonic, just wondering if you see much operating leverage from here and if so, what cost do you think scale?

Maxine Jaquet: I think whilst there is capacity in some of the assets that we've outlined today, there will be people that will be required to be added. So there no doubt will be some leverage, but we're assuming around that same EBITDA margin going forward. And until we own the business, I think we're focused on the growth at this point in time and making sure that we execute on that growth. That will be our primary driver and we're not seeking to look for any operational efficiencies at this point in time. But no doubt it will be certainly a business that we'll scale and it is pretty capital light, but still only fair so we'll just have to see how those margins play out over the next couple of years.

Shane Ponraj: (Morningstar, Analyst) I'm just checking the EBITDA margin, is that post-AASB 16?

Maxine Jaquet: It's not, but we don't think that's going to be a material difference.

Shane Ponraj: (Morningstar, Analyst) Okay, thanks and just back on testing, at the full year result you said you were averaging 40,000 tests a day. Just wondering what you think your capacity is.

Maxine Jaquet: We've been progressively scaling up capacity and as Malcolm, I think, may have mentioned, we are doing a bit more pooling than what we were doing before. So we've lifted our capacity materially above that and are looking at probably lifting it again in the near future, if our view is that current testing is probably going to prevail certainly for the next year.

Shane Ponraj: (Morningstar, Analyst) I missed it, but with the reimbursement rate, 85% of 85 per test, how long is that set to be in place for?

Malcolm Parmenter: 30 June.

Shane Ponraj: (Morningstar, Analyst) Okay and lastly, regarding Adora and the three day hospitals coming back, just wondering how profitability of that business has progressed and if it's meaningful at all.

Maxine Jaquet: It's actually been trading - everything's obviously been impacted by COVID, but it's actually been trading reasonably well. When there are lockdowns, it obviously gets impacted and is a community-based business and a referral-based business, so it does get a bit knocked around at times. But it's been trading pretty well.

Shane Ponraj: (Morningstar, Analyst) Okay, that's all from me, thank you.

Operator: Thank you, your next question comes from Andrew Perks of Accordius. Please go ahead.

Andrew Perks: (Accordius, Analyst) Thanks for your time. Just quickly, who was the vendor of Agilex?

Maxine Jaquet: The single largest shareholder was Dr Glenn Haifer.

Andrew Perks: (Accordius, Analyst) Okay and was there any private equity involved, or was it just a collection of individuals and founders?

Mark Ellis: Genesis Capital had a very, very small stake, less than 5%.

Andrew Perks: (Accordius, Analyst) Okay, all right and just for clarification, so if big pharma want to run a clinical trial, they outsource to a clinical research organisation which is CRO, who then outsource to laboratories like Agilex, is that correct?

Malcolm Parmenter: Yes, that's one of the ways it goes. Sometimes large pharma companies have worldwide contracts with the likes of IQVIA, but the ones, if they're looking for Phase 1, particularly Phase 1 clinical trials, then that's one way it would go. Sometimes the biotech will independently select both a pathology provider and a CRO. So the CROs don't necessarily get to control all of that, it's a result of who the pathology provider's going to be.

Andrew Perks: (Accordius, Analyst) Okay and given that you're an outsourcer and you're dependent on that work either coming direct from the pharma or from the CRO and you're maintaining a six bench effectively, what volatility in earnings should we expect from this business, given your fixed cost base and your oscillating contract award?

Malcolm Parmenter: It actually doesn't vary a lot because there's such a large number of these. They're not lumpy trials where you're getting large dollar value for each trial that comes along and the lab is up and down. Because of the number of trials coming through, that tends to keep it pretty smooth.

Andrew Perks: (Accordius, Analyst) Okay, that's great. Then just lastly on price and it was touched on earlier, Malcolm, when we bought Montserrat that wasn't making any money and it was like trust me, the growth is coming. And now we've got this acquisition which is pretty much the same. The price does seem a bit - at EPS when it's virtually not going to add much, is it really even worth doing to have another challenge on your hands?

Malcolm Parmenter: Well actually, right at this point in time what challenges do we have? As a business, the reality is we're generating cash. You saw at that 30 September result we made $250 million in the space of three months. We've got the process running pretty well around our imaging business in terms of where that goes. Yes, the hospital and the medical centre segment gets knocked around in COVID, but it comes back in terms of where that is.

We managed to sell our medical centre business, which was our biggest challenge in terms of where that goes. Montserrat's been performing well in terms of where it goes. This is a natural adjacency for pathology in terms of where it sits, it's part of our pathology business. The rest of our pathology business is doing very well, generating lots of cash in terms of where it is. But this is exactly the time to take on a challenge.

Andrew Perks: (Accordius, Analyst) Yes, I suppose you are generating lots of cash, which is awesome. It just would have been nice not to have paid 20 times, but I suppose it's like most companies making acquisitions now, it's 10% or 15% accretive and you do one that's sort of flat, you think oh gee, could you have screwed them for a better price?

Malcolm Parmenter: No, because it's a competitive process, you've seen what these are. BioAgilytix sold for 41 times last 12-month EBITDA quite recently. This is a good price. It's the market we're in unfortunately and in FY23 it's at 12 times and then 8 times and then 6 times as you go on with years and we've made that investment, given the cash flow that we have. It's exactly the time to be doing this.

Andrew Perks: (Accordius, Analyst) Okay, that's great, excellent. Thanks for your time, Malcolm, appreciate it.

Malcolm Parmenter: Okay, you're welcome.

Operator: Thank you, there are no further questions at this time. I will now hand back to Dr Parmenter for closing remarks.

Malcolm Parmenter: Thanks, everybody, for listening. All the best to all of you for Christmas and the festive season coming up. Stay safe, go to Healius pathology if you need a PCR test. Talk soon, bye.

Operator: That does conclude our conference for today. Thank you for participating, you may now disconnect.

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