Zacks Small-Cap Research

Sponsored – Impartial - Comprehensive

November 13, 2020

John D. Vandermosten, CFA
312-265-9588 / jvandermosten@zacks.com

scr.zacks.com **10 S. Riverside Plaza, Chicago, IL 60606**

DarioHealth Corp. (DRIO - NASDAQ)

Several New Partnerships to Drive Growth

Based on our discounted multiple of earnings model DarioHealth is valued at approximately $14.00 per share. Our model assumes rapid revenue growth and positive EPS by 2024. We apply a 25x multiple to 2024 EPS and discount to present using a 25% discount rate.

Current Price (11/11/20)	$10.92
Valuation	**$14.00**

OUTLOOK

DarioHealth is a global digital therapeutics (DTx) company that provides digital management of chronic conditions. Dario offers a blood sugar monitor and associated smartphone application which provides diabetes monitoring and advice to prompt behavioral change and disease improvement. Dario recently launched a hypertension module and will expand into other disease states including obesity.

The DTx platform is targeting multiple parties, including retail, provider, employer and health plan customers. The company's new strategy is to shift primary marketing efforts towards large health care providers which should yield greater subscriber growth and higher PMPM. Dario will also add multiple chronic condition modules to its offering which is also expected to increase the PMPM total.

This move to target large healthcare providers is complemented by a shift from the previous B2C model to a high margin SaaS model and B2B2C approach addressing multiple chronic conditions.

Dario has conducted numerous studies leveraging its user data which have demonstrated improvement in clinical parameters. We expect additional studies to be conducted supporting the use of the device on a wide scale by payors and health plans.

SUMMARY DATA

52-Week High	**$22.49**
52-Week Low	**$0.20**
One-Year Return (%)	**146**
Beta	**1.15**
Average Daily Volume (sh)	**116,384**
Shares Outstanding (mil)	**12.5**
Market Capitalization ($mil)	**$136.5**
Short Interest Ratio (days)	**0.39**
Institutional Ownership (%)	**19.2**
Insider Ownership (%)	**27.6**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**N/A**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**N/A**
P/E using 2020 Estimate	**N/A**
P/E using 2021 Estimate	**N/A**
Zacks Rank	**N/A**

Risk Level	**Above Average**
Type of Stock	**Small-Growth**
Industry	**Med-Biomed/Gene**

ZACKS ESTIMATES

Revenue
(in millions of $US)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2019	$2.2 A	$1.7 A	$1.9 A	$1.8 A	$7.6 A
2020	$1.7 A	$1.8 A	$2.0 A	$2.2 E	$7.7 E
2021					$13.6 E
2022					$26.2 E

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2019	-$2.92 A	-$2.53 A	-$1.11 A	$2.86 A	-$9.22 A
2020	-$3.61 A	-$1.16 A	-$1.02 A	-$0.61 E	-$5.02 E
2021					-$2.90 E
2022					-$1.98 E

© Copyright 2020, Zacks Investment Research. All Rights Reserved.

WHAT'S NEW

Third Quarter 2020 Operational and Financial Results

On November 12, 2020 DarioHealth Corp. (NASDAQ: DRIO) reported third quarter earnings and filed its companion 10-Q. The company also held an investor conference call summarizing achievements during the reporting period and to date. Dario reported third quarter revenues of $2.0 million, about 2% ahead of our estimate. Net loss lagged our forecasts with reported loss per share of ($1.02) as compared to our ($0.84) due to higher costs across the board. Activity during the third quarter and period to date was punctuated by multiple agreements including those with Williams Medical, HMC HealthWorks and multiple patient monitoring arrangements. Dario was also included on Vitality Group's gateway, providing preferred access to 20 million members. The company also participated in poster presentation highlighting the impact of digital health on diabetes and hypertension control. Other items of note included communicating company strategy to stakeholders with a key opinion leader event, participating in scientific conferences and raising sufficient capital to implement the company's commercialization strategy over the next few years. Another important event that positively impacted valuation metrics in the industry was the $18.5 billion merger of Livongo (LVGO) and Teladoc (TDOC) which was announced on August 5 and closed on October 30.

Dario announced the pursuit of several large opportunities in the third quarter that are anticipated to close and launch in the near term. On the conference call, management pointed to continued strength in the remote patient monitoring (RPM) effort, growth in the marketing team and continued demand from insurers, employers and providers.

Revenues of $2.042 million were divided between $1.556 million in products and $486,000 in services. Total revenues were up 9% over 3Q:19 and up 14% vs. 2Q:20. Using the alternative revenue breakdown, consumer products were $1.257 million and membership services were $785,000 in the third quarter. Gross margin was 26.9%, declining over prior year levels due to increased promotions. Management maintains its long term target of ~70% gross margins. Operational expenses were higher than expected across the board totaling $7.2 million compared to our estimate of $5.7 million. Higher costs were attributable to new hires for the sales and marketing team, increased digital marketing expenses, greater stock-based compensation, payroll, consulting and investor relations expense. Net loss for the period was ($6.6) million or ($1.02) per share based on 7.3 million average shares outstanding.

Cash and marketable securities balance was $36.9 million as of September 30, 2020. No debt is carried on the balance sheet. Cash burn for 3Q:20 was approximately ($3.8) million, only about half of net loss, predominantly due to the issuance of stock based compensation. Cash received from financing was $27.5 million related to the common stock, warrant and warrant exercises that took place in the third quarter. As of November 10, 2020, investors in the Class A preferred stock have redeemed 5,552 shares of the initial 21,375 shares sold in 4Q:19. This will reduce our future share count slightly as, once converted, the shares no longer pay a stock dividend.

Significant Events

Since July 2020, we have seen a material transformation in Dario and the digital therapeutics space. Dario was able to raise $28.6 million in cash from a private placement that will support the transition from B2C to B2B2C. Valuations and perceived value in the space have also increased as a result of the now consummated merger between Teladoc and Livongo Health.

In its July fundraising, Dario was able to tap resources from its largest existing shareholder, Nantahala Capital Management and new investors including Manchester Management Company and Soleus Capital Management. The deal also included leading Israeli institutional investors such as Phoenix insurance, Mor provident fund, Psagot investment house. The quality of the investors is high and Dario management anticipates that these will be long-term shareholders that will support the company as they advance through their growth trajectory. Based on our estimates, the funds will be sufficient to advance the commercialization effort for the next two years. This capital removes a significant risk for the fledgling company and provides certainty that the sales team can continue to grow revenues and innovate as they pursue health plans. The near $38 million now on the balance sheet also reduces dilution risk, which is often an issue when a short of cash balance sheet mixes with share price volatility.

On August 5th, Teladoc (NYSE: TDOC) announced an $18.5 billion[1] bid for Livongo, which has only been public for about a year. The now closed merger matched two of the largest players in digital therapeutics and telemedicine. There is only a small degree of overlap between the two companies, so we do not anticipate an increase in the competitive environment. Penetration for the industry is low which also suggests that this merger will not hinder Dario's efforts. We discussed deal details in a note published on August 6th. With M&A in the air, Dario becomes a potential target for acquirers that could include health plans, managed care, hospital systems or even technology players desiring exposure to this rapidly expanding space.

DarioHealth announced an RPM deal where it will make a remote monitoring platform available to healthcare professionals in the UK and Ireland through an agreement with Williams Medical. Not only does this deal provide additional revenue from an emerging growth area but it also expands Dario's reach into the British Isles. During the 3Q:20 conference call, management noted continued interest in RPM and the company's focus on making it a key differentiator in the company's product offering.

Association of Diabetes Care Poster Presentation

DarioHealth presented a poster at the Association of Diabetes Care and Education Specialists 2020 virtual conference in mid-August. The poster, entitled "Impact of Digital Management on Clinical Outcome in Patients with Chronic Conditions: Diabetes and Hypertension," provides a summary of a 345-subject study that examined the impact of the Dario digital therapeutics platform on diabetic and hypertensive populations.

The analysis showed that of patients that started the program with hypertension stage 1, 2 or crisis levels, 70% improved their systolic and diastolic blood pressure by an average of 8.4 mmHg and 6.2 mmHg respectively. The group also reduced the number of high readings (down by 33%) and a reduction in severe events by 67% after six months of the program. A subset of the diabetic population of 114 subjects that had blood glucose above 160 mg/dL improved their blood glucose levels by 14% compared to baseline.

HMC HealthWorks Partnership

DarioHealth and HMC HealthWorks announced a sales and distribution partnership in September. HMC will incorporate DarioHealth's digital therapeutics (DTx) platform into its comprehensive care management programs and offer DarioHealth's platform as a stand-alone option.

HMC HealthWorks is a healthcare management company that provides administrative and care management to smaller plans such as Taft-Hartley union plans. They provide chronic care management, behavioral health and wellness services to client plans. The group covers approximately one million lives and is in a space that other competitors such as Livongo have not yet actively pursued. The arrangement between Dario and HMC will offer Dario's full suite of services, including diabetes care, blood pressure management and coaching as well as other services as they become available.

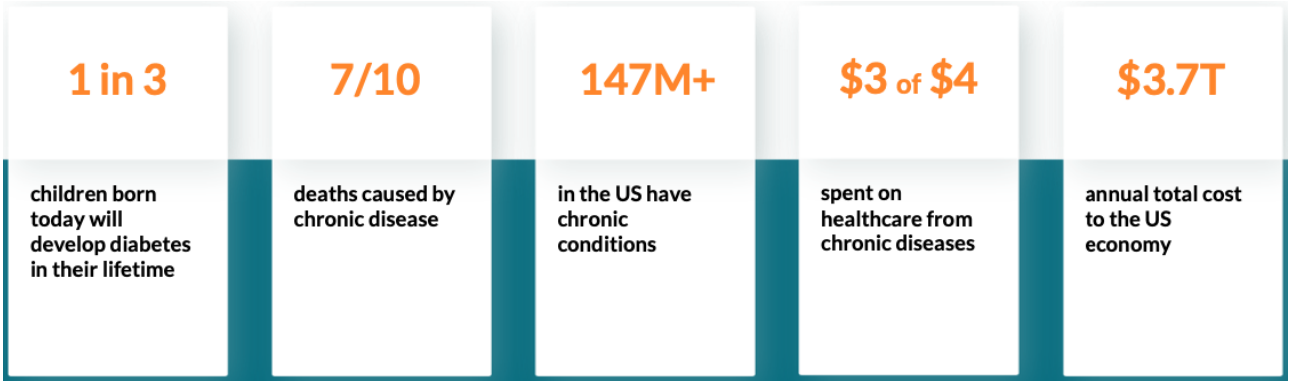
Exhibit I – DarioHealth's Platform-as-a-Service (PaaS)[2]



[1] Based on Teladoc's accounting and closing price the night before the announcement.
[2] DarioHealth Investor Presentation, September 25, 2020

Dario continues to seek and form partnerships as its overall strategy shifts from its direct-to-consumer, where it refined and vetted the DarioHealth platform, to a business-to-business-to-consumer model, targeting relationships with large care populations. The arrangement with HMC will layer on incremental lives at a $40 to $60 and higher per member per month (PMPM) rate, depending on level of services which could include diabetes management, blood pressure management and coaching. We estimate anywhere from 10% to 18% of a covered population has a chronic disease and over time we anticipate substantial penetration into this group. For a quick back of the envelope estimate at A $40 PMPM rate and 10% penetration, this equates to $48 million in annual revenues.

Exhibit II – DarioHealth Market Opportunity[3]



DTx is a burgeoning and disruptive field offering a significant addressable market where DarioHealth holds a dominant position. The DarioHealth platform can improve behavior, be an extension of the physician and monitor a patient's care in the management of chronic conditions.

The deal with HMC supports our thesis of rapidly growing expansion into the health plan market with is expected to offer higher PMPM and lower acquisition costs, providing both topline and margin leverage. While Dario's sales are predominantly in the US, we see global opportunity as the platform proves itself and we expect other regions to be added when there is a reasonable assumption that they can be developed. Please see our initiation for additional details on our investment thesis, valuation approach and the DTx space.

Summary

DarioHealth has progressed as expected, growing revenues a sequential 14% and accumulating several new deals in the pipeline. Dario's shift to focus on large health plans with higher per user revenues and lower acquisition costs is a recipe for fast growing topline and increasing margins. We anticipate additional deal closings similar to those with Vitality and HMC which suggest accelerating revenues and improving profitability in coming quarters. We are optimistic that Dario can exceed our revenue projections if the pending deals are quickly closed and members are enrolled at a reasonable pace. Expansion into other chronic diseases such as hypertension and obesity provide a longer and wider runway for future expansion. We maintain our target price for DarioHealth at $14.00 with justification for our favorable view based on the company's revenue growth, raising of sufficient cash to support operations for several years, imminent large deal closures and industry revaluation based on M&A comparisons.

[3] DarioHealth Investor Presentation, September 25, 2020

PROJECTED FINANCIALS

DarioHealth, Corp. - Income Statement

DarioHealth Corp.	2019 A	Q1 A	Q2 A	Q3 A	Q4 E	2020 E	2021 E	2022 E
Total Revenues ($US '000)	**$7,559**	**$1,667**	**$1,787**	**$2,042**	**$2,200**	**$7,696**	**$13,631**	**$26,221**
YOY Growth	2%	-26%	8%	9%	22%	2%	77%	92%
Cost of Revenues	$4,962	$888	$1,151	$1,493	$1,166	$4,698	$6,798	$10,666
Product Gross Margin	34.4%	46.7%	35.6%	26.9%	47%	39%	50%	59%
Research & Development	$3,692	$1,231	$825	$954	$1,000	$4,010	$4,732	$5,442
Sales & Marketing	$11,127	$4,091	$2,608	$3,635	$2,900	$13,234	$14,972	$16,469
General & Administrative	$5,483	$5,571	$1,326	$2,562	$2,100	$11,559	$10,200	$10,506
Income from operations	($17,705)	($10,114)	($4,123)	($6,602)	($4,966)	($25,805)	($23,070)	($16,861)
Operating Margin	-234%	-607%	-231%	-323%	-226%	-335%	-169%	-64%
Financial Expenses	$31	($222)	($117)	($52)	$0	($391)	$0	$0
Deemed Dividend	$3,155	$1,275	$786	$930	$0	$2,991	$1,100	$1,000
Pre-Tax Income	($20,891)	($11,167)	($4,792)	($7,480)	($4,966)	($28,405)	($24,170)	($17,861)
Net Income	**($20,891)**	**($11,167)**	**($4,792)**	**($7,480)**	**($4,966)**	**($28,405)**	**($24,170)**	**($17,861)**
Net Margin	-276%	-670%	-268%	-366%	-226%	-369%	-177%	-68%
Reported EPS	**($9.22)**	**($3.61)**	**($1.16)**	**($1.02)**	**($0.61)**	**($5.02)**	**($2.90)**	**($1.98)**
Basic Shares Outstanding	2,266	3,091	4,122	7,328	8,100	5,660	8,321	9,021

Source: Company Filing // Zacks Investment Research, Inc. Estimates

© Copyright 2020, Zacks Investment Research. All Rights Reserved.

HISTORICAL STOCK PRICE

DarioHealth, Corp. – Share Price Chart



© Copyright 2020, Zacks Investment Research. All Rights Reserved.

DISCLOSURES

The following disclosures relate to relationships between Zacks Small-Cap Research ("Zacks SCR"), a division of Zacks Investment Research ("ZIR"), and the issuers covered by the Zacks SCR Analysts in the Small-Cap Universe.

ANALYST DISCLOSURES

I, John Vandermosten, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the recommendations or views expressed in this research report. I believe the information used for the creation of this report has been obtained from sources I considered to be reliable, but I can neither guarantee nor represent the completeness or accuracy of the information herewith. Such information and the opinions expressed are subject to change without notice.

INVESTMENT BANKING AND FEES FOR SERVICES

Zacks SCR does not provide investment banking services nor has it received compensation for investment banking services from the issuers of the securities covered in this report or article.
Zacks SCR has received compensation from the issuer directly or from an investor relations consulting firm engaged by the issuer for providing non-investment banking services to this issuer and expects to receive additional compensation for such non-investment banking services provided to this issuer. The non-investment banking services provided to the issuer includes the preparation of this report, investor relations services, investment software, financial database analysis, organization of non-deal road shows, and attendance fees for conferences sponsored or co-sponsored by Zacks SCR. The fees for these services vary on a per-client basis and are subject to the number and types of services contracted. Fees typically range between ten thousand and fifty thousand dollars per annum. Details of fees paid by this issuer are available upon request.

POLICY DISCLOSURES

This report provides an objective valuation of the issuer today and expected valuations of the issuer at various future dates based on applying standard investment valuation methodologies to the revenue and EPS forecasts made by the SCR Analyst of the issuer's business.
SCR Analysts are restricted from holding or trading securities in the issuers that they cover. ZIR and Zacks SCR do not make a market in any security followed by SCR nor do they act as dealers in these securities. Each Zacks SCR Analyst has full discretion over the valuation of the issuer included in this report based on his or her own due diligence. SCR Analysts are paid based on the number of companies they cover. SCR Analyst compensation is not, was not, nor will be, directly or indirectly, related to the specific valuations or views expressed in any report or article.

ADDITIONAL INFORMATION

Additional information is available upon request. Zacks SCR reports and articles are based on data obtained from sources that it believes to be reliable, but are not guaranteed to be accurate nor do they purport to be complete. Because of individual financial or investment objectives and/or financial circumstances, this report or article should not be construed as advice designed to meet the particular investment needs of any investor. Investing involves risk. Any opinions expressed by Zacks SCR Analysts are subject to change without notice. Reports or articles or tweets are not to be construed as an offer or solicitation of an offer to buy or sell the securities herein mentioned.

© Copyright 2020, Zacks Investment Research. All Rights Reserved.