Augmedix, Inc.

First Quarter 2023 Earnings Conference Call

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CORPORATE PARTICIPANTS

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CONFERENCE CALL PARTICIPANTS

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Allen Klee, *Maxim Group*

Neil Chatterji, *B. Riley Securities*

PRESENTATION

Operator

Greetings, and welcome to the Augmedix, Inc. First Quarter 2023 Earnings Conference Call. (Operator Instructions)

As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Matt Chesler, Investor Relations. Thank you. Please go ahead.

Matt Chesler

Thank you, Operator.

Joining me today from Augmedix are Manny Krakaris, Chief Executive Officer, and Paul Ginocchio, Chief Financial Officer.

This morning, Augmedix released financial results for the quarter ended March 31, 2023. We have posted a press release and an Investor presentation on our website at augmedix.com. We'll begin our call with prepared remarks to be followed by a Q&A session. This call is also being simulcast and will be archived on our website.

Before we begin, I'd like to remind you that Management will make statements during this call that include forward-looking statements within the meaning of Federal Securities Laws, which are made pursuant to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. Any statements that relate to expectations or predictions of future events, results or performance, are forward-looking statements. They are based on current estimates and various assumptions and involve material risks and uncertainties that could cause actual results or events to materially differ from those anticipated or implied. Accordingly, you should not place undue reliance on these statements.

For a list and description of the risks and uncertainties associated with our business, please refer to the Risk Factors in Management's discussion and analysis in our most recent Form 10-K and Form 10-Q filed with the Securities and Exchange Commission, and similar disclosures in subsequent reports filed with the SEC.

Also, during our call today, we may discuss non-GAAP financial measures, which adjust our GAAP results to eliminate the impact of certain items. You will find additional information regarding these financial measures and the reconciliations to GAAP measures in today's press release. This conference call contains time-sensitive information and is accurate only as of the live broadcast today, May 12, 2023. Augmedix disclaims any intention or obligation, except as required by law, to update or revise any financial projections or forward-looking statements, whether because of new information, future events or otherwise.

With that, I'll turn the call over to Manny.

Manny Krakaris

Thanks, Matt. Good morning, everyone, and welcome to our earnings call.

The start to 2023 is highlighted by strong top line growth, continued development and commercialization of our broad product offerings, strengthening of our financial position and solid momentum exiting the quarter. Last month, we concluded a landmark strategic partnership and financing with HCA Healthcare. This partnership, with one of the nation's largest and most forward-thinking healthcare providers, serves as a powerful vote of confidence in our technology and our approach to bringing technology at scale to the point of care. HCA is collaborating with us on the development of the technology underlying our Augmedix Go product that aims to transform the way patient care is documented in the acute care setting.

Alongside our largest Investor, Redmile Group, HCA also made a substantial investment in Augmedix, serving as a clear indication that we are on the right strategic path. Even prior to our HCA partnership announcement, we were experiencing increased commercial demand from clinicians, and I'm confident that our collaboration with HCA will only accelerate our commercial momentum. The need for our technology at the point of care is real, urgent, and growing. The administrative burden on practitioners is significant, leading to higher cost and physician burnout.

No healthcare professional went to medical school to manage documentation. They want to see and help their patients and practice at the top of their license. We are developing products that enable them to do just that, allowing clinicians and patients to truly connect with the point of care, improving patient access as clinicians spend less time documenting visits and improving healthcare operating efficiency. HCA fully understands this.

With the industry's increasing adoption of powerful AI tools, such as large language models, we are mindful that all of our products must engender trust among our customers if they are to be adopted at scale. That is why we take great pain to ensure our automation technology is built thoughtfully and respectfully. While others throw intrusive technology or black box AI to automate their processes, we are developing a platform modeled on practitioner workflow that provides clinicians with transparency and control. Our clinician customers will be able to see how their medical notes are built and can set their own preferences for the notes' look and feel. We believe this will instill confidence among clinicians in the finished product.

Our medical notes are presented in well-understood formats and focus just on relevant medical issues as opposed to being long and meandering transcript summarization. Beyond the medical note, data we deliver to customers is structured and formatted to be easily ingested by third-party platforms.

Finally, we don't believe a one-size-fits-all is the right product strategy. We've developed a portfolio of products as part of our platform that provide healthcare systems and clinicians, the flexibility to choose the product that best works for them and provides the highest ROI. We believe thoughtful and responsible use of AI tools, transparency and clinician control in note creation, structured output and product fungibility across a wide spectrum of care settings, are key differentiators that set us apart from other players in our space.

We generated record first quarter bookings and 38% revenue growth, demonstrating the acceleration in commercial adoption we are seeing even before Augmedix Go is released later this year. We continue to build our base of recurring revenue, adding both new customers and expanding within existing customers. Existing customer expansion is best highlighted by our dollar-based net revenue retention of 136% in the quarter, up from an already strong 133% in the first quarter of 2022. This NRR demonstrates that our land and expand strategy within our large healthcare customers is working. We are adding incremental recurring revenue with minimal increase in fixed cost at an attractive customer acquisition cost.

Importantly, we were able to deliver this 38% revenue growth, while holding operating expenses flat sequentially compared to the fourth quarter and was only a 9% increase year-over-year. The effects of high operating leverage become more evident as we scale our offering, providing clear evidence that we are moving toward cash flow sustainability. As we noted in the announcement of the HCA and Redmile transaction, we expect to reach operating cash flow breakeven as we exit 2024. Our results demonstrate that we are making solid progress towards this critical goal.

With that, I'll now turn the call over to Paul Ginocchio, our CFO, then will return with closing comments. Paul?

Paul Ginocchio

Thank you, Manny.

As stated, revenue for the three months ended March 31, 2023, was $9.6 million, a 38% increase from the $7.0 million in the same period a year ago. Growth was primarily driven by existing client expansion, new clients, and growth in our notes offering. Dollar-based net revenue retention in the first quarter of 2023 was 136% for our health enterprise customers compared to 133% in the first quarter of '22 and 126% in the fourth quarter of 2022. As many of you know, net revenue retention measures what a dollar of revenue at our existing clients a year ago grew into in this most recent quarter. It includes upsells, expansion and churn, but excludes revenue from any new logos that were added during the last 12 months. The acceleration of NRR was driven primarily by significant expansions at two of our larger health system customers. Our NRR results put us at best-in-class levels for SaaS companies.

Average clinicians in service for the first quarter of 2023 rose 43% as compared to the first quarter of 2022 and compares to 41% year-on-year growth in the fourth quarter of 2022. We define a clinician service as an individual doctor, nurse practitioner or other healthcare professional using either our live or note service. We believe the growth in the number of clinicians in service is an indicator of the performance of our business as it demonstrates our ability to penetrate the market and grow our business.

Adjusted gross margin for the first quarter of 2023 was 45.8% as compared to 45.3% in the corresponding prior year period and compares to 46.5% in the fourth quarter of 2022. The exposure to clinicians serviced out of the U.S. reduced our quarter-on-quarter gross margins, partially offset by efficiency gains. We expect gross margins to benefit later this year from the shifting of a significant number of U.S. service clinicians to outside the U.S., along with continued scale benefits and improving automation.

Total operating expenses for the first quarter of 2023 were $9.5 million, flat sequentially from the fourth quarter of 2022. Non-GAAP operating expenses, which excludes stock-based compensation and one-time items, grew 9% compared to the first quarter of 2022, a deceleration from the double-digit growth rates we reported in the past several quarters. You are beginning to see the inherent operating leverage in our model come through as we scale. We are continuing to incrementally invest in sales and marketing and engineering to drive innovation and growth, but other cost categories are largely flat outside certain costs, such as audit fees and legal fees.

Growth in gross profit outpacing OpEx growth resulted in a reduction in our quarterly operating losses for the third consecutive quarter. Adjusted EBITDA, which we calculate by adding back depreciation, amortization, taxes, interest, onetime items, and stock-based compensation to net loss, was a loss of $4.1 million in the first quarter of 2023, compared to a loss of $4.8 million in the first quarter of 2022. Along with this improvement in Adjusted EBITDA loss was a year-on-year improvement in our Adjusted EBITDA margin from negative 69% in the year-ago quarter to negative 43% in the most recent quarter.

Cash flow from operating activities was an outflow of $6.2 million in the first quarter of 2023 compared to $4.2 million last year. The first quarter is typically our largest cash burn quarter of the year due to some annual payments and bonuses. We continue to expect a reduction in cash burn in 2023 versus 2022, and cash burn will improve from these 1Q results. At March 31, 2023, we had $20.6 million of cash, cash equivalents, and restricted cash. At quarter end, we had an additional $5 million of incremental liquidity via AR line of credit. The $12 million in new equity from the financing with HCA Healthcare and Redmile Group in April at $1.60 per share, gives us pro forma cash, cash equivalents and restricted cash of nearly $33 million as of March 31.

In addition to the new equity raised, we have also agreed with Redmile to finalize a $5 million equity line of credit and we are in the final stages of putting it in place. The new equity line of credit will provide further capital certainty and give us backstop capital access even if the markets are closed. As we have said before, our expectation is that we will reach cash flow sustainability without accessing this facility.

In terms of our common share count, we had 37.5 million weighted average common shares for 1Q 2023. For modeling purposes, remember we sold another 3.125 million common shares to HCA and Redmile combined, and a combined 4.375 million prefunded warrants.

Positioning the Company to reach profitability is a top priority for our Company. With the tremendous opportunity in front of us and our technology platform, we believe we can deliver both strong revenue growth and operating leverage to reach operating cash flow breakeven, before net interest expense, as we exit 2024.

Now moving on to guidance. The positive momentum we saw coming into this year is continuing. We now expect revenue to be at least $42 million for the full year 2023.

Turning to our outlook for the second quarter of 2023, given the strength of our recent bookings and the health of our current backlog, we expect revenue in the second quarter to be approximately $10.4 million to $10.5 million. We expect GAAP gross margins to be similar to the first quarter 2023 GAAP gross margins. As you saw this quarter, we expect the overall increase in operating expenses in the coming quarters will be lower than the overall increase in revenue and gross profit. We do expect some incremental OpEx investments in 2023 and sequential OpEx growth in each of the coming quarters. We expect 8% to 10% sequential growth in OpEx into 2Q '23 from 1Q '23.

At this point, I'd like to turn the call back to Manny for closing comments.

Manny Krakaris

Thank you, Paul. Our product and technology strategies are resonating with customers, as evidenced by our strong top line growth and adoption by five of the top 10 U.S. healthcare systems. The proliferation of LLMs within the healthcare industry will inevitably level the technological playing field. However, LLMs alone are not a complete solution to the dilemma facing the industry.

Using this technology in a thoughtful and responsible manner and incorporating it into a compelling product portfolio that accommodates the widest range of clinician workflows in both the ambulatory and acute care settings, are what set Augmedix apart from others in this space. I am proud of our team's mission focus and grateful to our customers for entrusting us with this vital work.

As we look at the rest of the year and beyond, I remain very excited by the opportunity that lies in front of us. Thank you.

Operator, let's open it up to questions.

Operator

Thank you. (Operator Instructions) Today's first question is coming from Ryan Daniels of William Blair. Please go ahead.

Jared Haase

This is Jared Haase in for Ryan. Thanks for taking our questions. I wanted to start, just hoping to get maybe an update on the opportunity to unlock notes within your existing client base. It sounded like that product was a source of strength in quarter. I know you had a filing recently indicating you achieved this unlock with an existing customer, Dignity Health. Could you just speak to how you're thinking about the growth opportunity from adding this? Maybe what inning we're in, in terms of getting this unlocked across the client base? Or how penetrated you are today? Then with clients that have turned on notes, have you seen any signs of, I guess, cannibalization from live users just given the difference in pricing?

Paul Ginocchio

Let me take that. Great question. Our progress in unlocking notes across our enterprise customer base is pretty far along. I think most of them at this point are unlocked. There might be, I think, two or maybe three that are still in progress. We are very confident that they'll be unlocked as well. The second question, in terms of cannibalization, we haven't seen any cannibalization to date between notes and our live offering.

Jared Haase

Okay. Fair enough. I appreciate that color. Then one other follow-up, and Manny, you spoke a little bit to transparency and control of the product as key differentiators during the prepared remarks. I was wondering if you could provide a bit more color just to help illustrate that a bit more. Are there any sort of examples of what that means in terms of either the output or the actual clinician experience relative to maybe a more cookie-cutter black box approach?

Manny Krakaris

Sure. I'll speak specifically to our Go product, which is currently being tested at HCA and one other healthcare organization. The user interface shows the various steps that our back end goes through to create the note. It will expose the ASR by converting the audio into text. It will expose our NLP, which identifies the key elements within that transcript that our technology believes is relevant to the medical note. It will show the structured data breakdown of those key elements into significant and relevant blocks that need to be incorporated into the medical note.

It will also expose sections of the medical note, the output where the LLMs generated output for content. All of that is exposed to the customer, to the user, and they will have the ability to adjust the preferences within the structured data elements to affect the look and feel of the output. Then, of course, they can also add their own content manually to the extent they wish to do so.

Jared Haase

Okay, yes, I think that's really helpful. Thanks for the color. I'll hop back to the queue.

Operator

The next question is coming from Brooks O'Neil of Lake Street Capital. Please go ahead.

Brooks O'Neil

Good morning, guys. Congratulations on the great start to the year. I have a couple of questions. I'd like to start by just asking you a little bit about what you anticipate the workflow and sort of plan is with HCA as you can see it today.

Manny Krakaris

Hi Brooks, Manny again. We're currently testing our Go product with several doctors at HCA. We've also deployed our live solution in the emergency department, a couple of hospitals at HCA. We will add, and in process of adding, a couple more hospitals to that deployment in the emergency department. We're learning through the data that we collect from those encounters and incorporating that into our Go technology for the acute care setting. The rollout is kind of set for four hospitals at this point.

We expect that once we get a little closer in terms of finalizing the design on the Go product, we will be rolling that out much more aggressively across other hospitals. As you know, Brooks, HCA has 188—a little over 188—I think 188 hospitals in the U.S.

Brooks O'Neil

Pretty good number.

Paul Ginocchio

Brooks, the only thing I would add is that we are also hiring to accelerate the roadmap of Go. That's what's also included in our second quarter OpEx guidance.

Brooks O'Neil

Great. Can you guys say—I mean I don't follow HCA directly, obviously. Would you say there's any opportunity in working with HCA outside the acute care setting? I mean do they employ doctors in outpatient or freestanding centers across that 187-hospital network?

Manny Krakaris

Great question. They have a substantial ambulatory practice or clinical practice. They have, I think, 2,200 care centers around the U.S. outside of those 188 hospitals. Yes, we are planning to deploy outside the acute care setting. That is a separate commercial thread that we are pursuing actively with HCA today.

Brooks O'Neil

Great. I would assume you might follow the same kind of footprint. Start with a couple of facilities, a limited number of doctors, get your feet on the ground, and do the land and expand like you've done with many of your customers over time?

Manny Krakaris

Exactly. We've already identified the initial candidate hospitals or—sorry, care facilities for ambulatory. We're just setting things up right now.

Brooks O'Neil

Great. All that sounds good. I want to ask you just one more, but it's a little bit of a multipart, so I apologize for it. Just thinking about product development initiatives and opportunities, obviously, AI is a huge buzzword you mentioned in your prepared remarks. I'm curious how you're thinking about opportunities with AI. Obviously, you had a historic partnership with Google. I'm curious how you're working with them and whether, in fact, they're helping you with the HCA. Would be interesting to know. Then the last piece I'm just curious about is how you're seeing developments with the EMR, the key EMR vendors that are out there, obviously, EPIC and Oracle Cerner today? Is there anything going on there that's worth talking about? Thank you.

Manny Krakaris

Okay. Let me start with the first one, in terms of LLMs, our use of large language models in our quest to further automate the note creation process. Of course, all of this use of technology, the whole point of it, is to improve operating efficiency, improve the speed with which you can create a medical note and reduce the cost of creating that medical note and pass those cost savings on to your customers. We're very keen on incorporating that technology as much as we can. As I mentioned before, we want to do it responsibly.

We think we're on the right track in terms of earning the trust of our customers that the technology is not being used blindly by us. We've been putting in the appropriate guardrails to ensure that the product that we deliver is trustworthy. We will continue to do that.

As you mentioned, and rightly so, we do use Google's large language models today. We've been using them for a while. We are testing new ones, new releases as we speak. We've got a whole team of machine learning engineers working on that, on their latest LLM, that is specifically tailored to the healthcare environment. We're really excited to be able to deploy that commercially over the coming months.

In terms of EMR activity, we continue to have conversations with EPIC and Cerner/Oracle. I would say that the conversations are healthy. They're progressing. There's not much more to say other than that. For us, the first order of business with them is to develop as close an integration with the EMRs as possible to facilitate the deployment of our Go product.

Brooks O'Neil

All right. I appreciate all that color, and it's all fascinating and exciting. Let me ask one last one. I'm just curious if you know, I'm guessing HCA maybe has multiple EMR vendors. Do you happen to know if there's a predominant system, they use within the HCA organization? Or is it literally hospital by hospital in their world?

Manny Krakaris

Actually, it's not. It's pretty uniform and it's MEDITECH that they use. MEDITECH Magic is the particular version of MEDITECH that they have deployed.

Brooks O'Neil

Could you see yourself at some level, having discussions and integrating on some level with them?

Manny Krakaris

We're actually in the process of doing that just now. Yes. That's well underway.

Brooks O'Neil

Great, I'll follow up offline that. I'd like to learn more about it.

Manny Krakaris

Absolutely.

Operator

Thank you. The next question is coming from Allen Klee of Maxim Group. Please go ahead.

Allen Klee

Hi, good morning. Two small marketing, modeling-related questions. The gross margin declined a little sequentially. Could you address what was behind that? Then second, how much dollar amount do you think you have to increase operating expenses to build up sales and marketing for the Go launch? Thank you.

Paul Ginocchio

Yes. Allen, it's Paul. I'll take those. For the Q-on-Q change in our gross margin, the U.S. service business, which is less than 10% of our total business drove that Q-on-Q decline. That's due to the sort of normal beginning of the year payroll tax bucket refills, less holidays in the first quarter versus the fourth quarter, and then just higher healthcare costs here in the first quarter. Those were the main drivers of that sequential change in gross margin.

When it comes to sales and marketing for Go, we're doing some things that we think it's going to be a pretty efficient launch. You're seeing some OpEx increases as we accelerate the product development roadmap for Go in the acute care setting. Obviously, we feel very comfortable with both our commentary around getting to cash flow breakeven and our ability to successfully launch Go.

Allen Klee

Thank you.

Operator

Thank you. (Operator Instructions) The next question is coming from Neil Chatterji of B. Riley Securities. Please go ahead.

Neil Chatterji

Hi, good morning, guys. Thanks for taking the questions. Congrats on the quarter. Maybe just on HCA. I know you mentioned it's not an exclusive agreement. Just curious, given kind of the aggressive expansion plans, maybe across those 180-plus hospitals, just curious how much bandwidth does that leave for similar pilots or roll out for other large systems in 2023? Or is that more of a focus for '24?

Manny Krakaris

Hey, Neil, it's Manny. I think we've guided that we don't expect a significant impact to revenue from Go sales in 2023. That doesn't mean we're not going to be piloting or testing Go with other healthcare organizations this year, it just means that we've muted our expectations in terms of what commercial benefit we will expect for this current year. We have the bandwidth to deploy outside of HCA, and that is the plan.

Neil Chatterji

Got it.

Manny Krakaris

Just to keep in mind, we've been—just to add that, sorry. Several of our major enterprises have been asking for this product and want to be included in pilots. We do expect to be able to accommodate them later this year.

Neil Chatterji

Great. Great. Then just on the guidance, kind of given the strength you saw in the first quarter, record bookings, second quarter guide was pretty strong. Just curious, what gives you confidence in that? What was driving that strength?

Paul Ginocchio

Neil, it's Paul. On the bookings we saw the record bookings in the first quarter. We saw a number of health systems make incremental investments into our products that drove that strong bookings quarter. Obviously, we're guiding to a healthy increase Q-on-Q in terms of revenue growth. We feel good about our guidance for the full year and obviously, I slightly tweaked it. We'll continue to revisit as we progress through the year. We've only given that $42 million guidance less than two months ago initially. At this point in time, we're feeling really good about the year.

Neil Chatterji

Great. Just in terms of like quarterly cadence, how to think about the back half of the year, any seasonality there?

Paul Ginocchio

I think we always show nice Q-on-Q revenue growth. How one quarter grows versus the previous quarter kind of depends on the bookings over the last quarter, potentially the last two quarters. That is yet to be determined, but we continue to feel really good about at least $42 million of revenue.

Neil Chatterji

Great, that's it for me. Thanks.

Operator

Thank you. I'd like to turn the floor back over to Mr. Krakaris for closing comments.

Manny Krakaris

If there's no more questions, I want to thank everybody for participating in this earnings call. I'm sure we'll have more news to share with you as the year progresses. As I said with my closing comments, we're really excited about the year and look forward to keeping you guys updated as we progress at end of the year. Thank you very much.

Operator

Ladies and gentlemen, thank you for your participation. This concludes today's event. You may disconnect your lines or log off the webcast at this time and enjoy the rest of your day.