

Investment option review and change: Purchase of ResMed (ASX: RMD)

Across the Australian equity component of your investor account we have bought ResMed (ASX: RMD), a global leader in the manufacture of cloud-connected medical devices primarily used to help people suffering from obstructive sleep apnea (OSA), but increasingly also chronic obstructive pulmonary disease (COPD), and other respiratory diseases like asthma. In addition, the business manufactures machine-agnostic accessories like masks and in recent years, via M&A, has expanded into the supply of business management software as a service to out-of-hospital health providers (SaaS).

The company is headquartered in San Diego, CA, has manufacturing facilities in Australia, Singapore, France, and the United States and sells their products in more than 140 countries through a combination of wholly owned subsidiaries and independent distributors.

We are attracted to ResMed for the following reasons:

- Market leading offering
- Structural growth tailwinds
- Strong free cash flow generation

Over our investment horizon the opportunity exists for value creation given:

- **Structural growth tailwinds:** Estimates of the number of people worldwide suffering from sleep apnea (>900m), COPD (~380m) and asthma (~330m) suggest a very significant addressable market, currently largely untapped. While exact figures are unclear, estimates suggest that for sleep apnea the number of sufferers treated may be as high as 10-15% in the US, around 10% in Western Europe and as low as 1 – 5% in Asia Pacific countries. This along with a better understanding of the negative health impacts of sleep and respiratory disorders as well as the benefits of treatment should help underpin mid-to-high single digit industry growth in terms of new patients over our investment horizon and beyond.
- **Significant issues for main competitor:** The sleep and respiratory care industry has a limited number of large-scale competitors - ResMed and Philips are the biggest players and combined they represent about 90% share in most markets worldwide where they participate in. Since 2021 ResMed has been able to extend its industry leadership position, gaining market share courtesy of a product recall at Philips. While the timing and success of Philips' inevitable re-entry into the US is unknown, industry data suggests it may take longer than expected. Importantly though, a larger installed base of machines should help drive sales for accessories like masks that are typically replaced twice a year.
- **Opportunity for margin expansion:** Margins are expected to improve from a combination of high-cost legacy supply contracts struck during COVID rolling off, manufacturing volumes normalizing and allowing for more cost efficient production, freight costs subsiding and new higher margin machines being fully launched. With accessories being higher margin (than machines) and replaced more regularly, product mix should also benefit margins going forward.

The key risks we see are changes to reimbursement rates by governments and/or insurers, unexpected price competition and new technologies or treatments for the diseases ResMed's products are used to treat.

The purchase of ResMed has been funded by reducing the weighting to a number of existing positions.