WHITE DIAMOND RESEARCH

REWALK ROBOTICS WILL "REWALK" BACK TO SINGLE DIGITS

December 30, 2015

RESEARCH SUMMARY

ReWalk's (RWLK) Veterans Affairs (VA) coverage was expected from the last two earnings calls and already partially priced in.

No sell-side analyst showed excitement on the coverage news. Barclay's analyst raised the PT from $9 to $11, 25% below the current price.

A negative catalyst is coming up: With only $25M in cash, and $6M per quarter cash burn, RWLK is filed and ready to do a large share dilution soon.

Due to a low gross profit margin, RWLK needs to sell at least 2,000 exoskeletons per year to break even. It will only sell about 70 in 2015.

RWLK's President and Founder resigned last month. He previously criticized their exoskeleton as being "too bulky".

Lack of scale will prevent RWLK from expanding to many other countries.

ReWalk Robotics (RWLK) has risen 150% since news that the US Department of Veterans Affairs (VA) will start covering its exoskeleton for certain eligible disabled veterans. This is the typical news that gets the stock bid up by ignorant retail investors. It's an easy to understand tech story that retail investors think can make them a lot of money and help disabled veterans at the same time. However, looking past the surface, the company's economics and the product show a bleaker story.

This video from Fox News reveals a lot of the truth about the product. A US army veteran and ReWalk customer does a walking demonstration with his ReWalk exoskeleton. He tries walking twice, and both times the exoskeleton doesn't start moving. Then when on the third try he finally gets it walking, it's an awkward, jerking movement, making a sound like Robocop walking. And he said that he's been training to use it for 4 or 5 months. Wouldn't it be much easier to just glide around on wheels? This is a big reason why insurance companies don't want to cover it.

It's no wonder why the founder and President, Dr. Amit Goffer, resigned from the company in November, and had called RWLK's exoskeleton: "bulky and slow".

Recent Bearish RWLK Twitter Quotes

The following are tweets that describe the reality of RWLK's situation.

On 12/17/15 @NeelNY tweeted:

"I dont know how companies like these ever raise enough funds for a legit IPO, really a .01% chance this ever works out"

This is an insightful quote. Due to the bull market, a lot of recent IPOs were of companies that likely won't ever make it. RWLK was one of these IPOs.

On 12/17/15 @LordWindsor tweeted: **$RWLK** $128M shelf hanging overhead, COGS exceeding revenues, & growing compliance costs. Nice headline but company is wasteland.

On 12/22/15 @LordWindsor tweeted: "**$RWLK** case of sentiment trumps truth, handily won December's annoying trade award."

The above tweets show that stock analyst/traders have been getting squeezed shorting too early. This makes it a good time to get in short now that the squeeze is over.

Veteran Affairs Coverage Was Expected And Is Overhyped

In its Q315 earnings call and the Q215 earnings call , the company already spoke in great detail about the VA study and their interest in the exoskeleton. They said the VA was planning to buy some exoskeletons, and put much effort into working with RWLK. Therefore, the coverage news was expected and should have already been partially priced into the share price.

From the Q215 earnings call:

Larry Jasinski, CEO – *So the others that have enquired have simply held back a little bit until this policy statement that we are aware that the VA is working on is issued on a national basis so they know how and where and when to go get a ReWalk.*

They have asked us for a great deal of input, have indicated a lot of the progress that they have made, and my *understanding is that it is being reviewed now at the highest levels of the VA but I can't forecast the timing of the government beyond that.*

From the Q315 earnings call:

Larry Jasinski, CEO – *The VA is currently in the process of setting up the centers and securing equipment for the study. The study is occurring in parallel with additional VA plans to provide units for veterans and we continue to work with the VA to support establishing a standard operating procedure for individuals that are located in areas that will not be included in the study.*

The coverage news doesn't go into specifics. The VA never said RWLK would be its exclusive provider of exoskeletons and it didn't say the veterans would all be covered by insurance. Also, there aren't many US veterans that are actually eligible to use ReWalk's exoskeleton. From this article:

About 42,000 veterans are paralyzed. Of them, a fraction would meet the requirement for an exoskeleton. The apparatus requires specific height and weight requirements and works for paraplegics but not for quadriplegics. A supportive belt around the patient's waist keeps the suit in place, and a backpack holds the computer and rechargeable battery. Crutches are used for stability, and the FDA requires an assistant be nearby.

The company said it has evaluated 45 paralyzed veterans who meet the height and weight requirements for the technology

Assuming all 45 veterans that the company evaluated as eligible get an exoskeleton, at $77K per exoskeleton, that would only provide RWLK with $3.5M in revenues from the VA coverage. However, the stock has gained over $100M in market cap on the news!

Sell-side Analysts Are Not That Impressed By The VA News

Barclays analyst Matthew Taylor views the VA news as a positive but believes implementation will be slow and doesn't expect the announcement to lead to significant incremental 2016 revenue. On 11/6/15, Barclays lowered PT to $9 from $10. At the time, the stock was trading at about $8 per share. Now, RWLK is trading at over $15 per share, and Barclays increased its price target to $11, 30% below the current share price.

Upcoming Negative Catalyst: Share Dilution

RWLK is getting ready to do a share offering very soon. The company filed a $128M shelf on 12/4/15. The EFFECT for this shelf was filed on 12/8/15. $28M of this shelf is for current shareholders who want to unload stock. Last quarter Q315, RWLK burned $6M in cash and ended with $25M in cash and no debt. The company needs cash or will be broke within a year. Now is the best time for the company to do a share dilution while the trading volume is still high.

ReWalk Needs To Sell At Least 2,000 Exoskeletons Per Year To Break Even

RWLK's exoskeleton product isn't a drug with a gross profit margin of 80-90%. It's a medical device that has much lower profit margins. It costs RWLK a lot to manufacture each exoskeleton and provide training. RWLK's current gross profit margin is only 10%. Assuming that gets to 20% with more economies of scale, but also assuming operating expenses increase, in order to break even, RWLK conservatively needs at least $150M in sales per year. At an ASP of $77k apiece, that comes out to 2000 exoskeletons per year.

In the first nine months of 2015, RWLK only sold 48 exoskeletons. In the earnings calls, the CEO mentions how many leads the company has generated, and it is still in the 100s. It will be a long time to ever get to 1,000 unit sales per year, let alone 2,000.

Lack Of Scale Limits RWLK's Expansion Options

RWLK bulls can forget about expanding to many other countries. RWLK sells its exoskeleton only in the US and Germany, and there aren't many other countries where it's financially sound to sell them due to lack of scale. There might not even be the scale necessary for RWLK to be profitable in the US and Germany. The clinics that sell RWLK's exoskeletons are specialized and need to properly evaluate and train patients to use them. This is an endeavor that requires lots of upfront investment and constant maintenance, including marketing and training. The country needs to have a sufficient amount of eligible paraplegic prospects who can afford the exoskeleton in order to make it worth the investment for RWLK.

RWLK's President And Founder Retired In November

The President and founder of RWLK, Amit Goffer, doesn't want to have anything to do with the company anymore. At only age 62, he "retires" and won't even be on the Board Of Directors. He had criticisms of ReWalk's exoskeleton, in 2012 he said:

"The more advanced one we're selling for personal use is still in my opinion too bulky," he continues. "It should be possible to wear it easily and it should be faster – and that's where we're going."

Dr. Goffer can now sell his entire position without having to report it. Usually, founders of companies leave when the stock reaches its peak. Reported from the Dow Jones Newswire, on 12/23, Dr. Goffer registered 55,900 shares of RWLK to sell.

Technical Reasons That Suggest RWLK Will Fade

RWLK traded at a range of $8.55 to a low of $5.55 between 10/21/15 to 12/11/15. This shows that investors aren't willing to prop up the price over $10 even if they like the product. That shows RWLK isn't like ONVO (a scam that investors are willing to keep at a $200M+ market cap).

Also, when there isn't any significant news, RWLK only has a trading volume of on average about 30k shares per day. That shows there isn't a strong cult following interested in this stock. Also, institutions that buy RWLK's upcoming dilution will likely sell quickly for a quick flip because after the recent news gets stale the stock will go back to only trading 30k shares per day, which will make it hard for them to unload their shares.

Competition

ReWalk doesn't have a monopoly on the industry. It needs to keep spending R&D and keep its prices affordable to compete with the competition. Ekso Bionics (EKSO) is a competitor and just raised funds. Parker Hannifin has created an exoskeleton called Indego and is working with various medical institutions.

The Bull Case – Plan To Grow Eligible Customer Base

Since it's impossible that ReWalk will ever be profitable just selling to paraplegics, bulls discuss the future possibilities of expanding customer conditions. Possible future customers for RWLK are those with multiple sclerosis (affecting 400k people in the US). Other potential areas include stroke, quadriplegia, and cerebral palsy.

With “story stocks” like RWLK, the bulls love to dream about new markets on grandiose scales. The truth is, RWLK isn’t even thinking about expanding to those other areas right now. That would require considerably more R&D spending and RWLK is decreasing its R&D expense. R&D was only $1.3M in Q315 and $1.4M in Q215, compared to $5.2M in Q314 and $1.076M in Q215.

RWLK already has trouble selling its exoskeleton to paraplegics. Moving to other more challenging and debilitating conditions is a far away fantasy.

Disclaimer: White Diamond Research has clients short RWLK.