Accolade

They are who we thought they were

Reiterate Rating: BUY | PO: 16.00 USD | Price: 11.62 USD

09 January 2024

Equity

Growing demand, 20% revenue growth, scalable model

Accolade continues to execute in FY3Q with another quarterly beat driven by strong demand across its major businesses, with forward guidance (FY4Q24 + FY25) supported by strong bookings growth. Accolade's decision to raise its FY29 EBITDA profitability targets from 10-15% (announced in May 2023) to 15-20% highlights the operating leverage embedded in the model. Accolade's core navigation and broader integrated platform continue to represent one of the biggest opportunities in digital health, supported by positive channel checks surrounding navigation. Overall, we remain optimistic about Accolade's ability to drive new customer growth through its core navigation businesses and view its success in cross-selling driving both top-line growth and gross margin expansion over time. Accolade should also capture additional operating leverage both from the natural scale of its B2B business as well as scaling AI tools (both on the provider side and the member side). Care navigation continues to be a bright spot in our conversations with healthcare brokers and consultants, supporting our view that Accolade can continue to grow revenue above health IT peers. We reiterate our Buy rating and $16 PO, representing ~2.4x CY24 revenue.

Adjusting our estimates on the path to profitability

Following results, we are increasing our FY24E revenue from $413.1MM to $414.0MM and increasing our adj. EBITDA estimate from ($10.2MM) to ($7.8MM). For FY25E, we are touching up our revenue estimate from $502.3MM to $502.6MM and increasing our adj. EBITDA estimate from $11.8MM to $12.2MM. We believe ACCD could grow its top line at ~20%+ in FY25 and continue to model ACCD reaching EBITDA profitability by FY25, in-line with guidance.

Upcoming events and catalysts

We continue to track trends in the ongoing execution of new customer wins, the labor market, and any news around the TRICARE program. Of all of these, the employment market in particular would likely have the biggest swing factors to ongoing sentiment.

Estimates (Feb) (US$)	2022A	2023A	2024E	2025E	2026E
EPS	(2.14)	(2.15)	(1.52)	(1.53)	(1.28)
GAAP EPS	(2.01)	1.56	(1.88)	(1.95)	(1.72)
EPS Change (YoY)	-65.9%	-0.5%	29.3%	-0.7%	16.3%
Consensus EPS (Bloomberg)			(0.69)	(0.64)	(0.60)
DPS	0	0	0	0	0
Valuation (Feb)					
GAAP P/E	NM	7.4x	NM	NM	NM
EV / EBITDA*	NM	NM	NM	75.4x	24.0x
Free Cash Flow Yield*	-7.2%	-4.8%	1.1%	2.9%	5.8%

* For full definitions of *iQmethod* SM measures, see page 9.

Key Changes

(US$)	Previous	Current
2024E EPS	-1.65	-1.52
2025E EPS	-1.56	-1.53
2026E EPS	-1.33	-1.28
2024E EBITDA (m)	-10.2	-7.8
2025E EBITDA (m)	11.8	12.2
2026E EBITDA (m)	36.4	38.2

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Stock Data

Price	11.62 USD
Price Objective	16.00 USD
Date Established	5-Oct-2023
Investment Opinion	C-1-9
52-Week Range	6.33 USD - 17.01 USD
Mrkt Val (mn) / Shares Out (mn)	899 USD / 77.4
Free Float	90.1%
Average Daily Value (mn)	7.01 USD
BofA Ticker / Exchange	ACCD / NAS
Bloomberg / Reuters	ACCD US / ACCD.OQ
ROE (2024E)	-25.5%
Net Dbt to Eqty (Feb-2023A)	-8.2%
ESGMeter™	Medium

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BofA ESGMeter Methodology".

iQprofile SM Accolade

iQ**method* SM **– Bus Performance

(US$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	-9.4%	-7.6%	-6.1%	-5.2%	-2.0%
Return on Equity	-22.4%	-23.0%	-25.5%	-29.0%	-26.8%
Operating Margin	-16.9%	-108.4%	-13.3%	-9.9%	-4.5%
Free Cash Flow	(65)	(43)	10	26	52

iQ**method* SM **– Quality of Earnings

(US$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	NM	NM	NM	NM	NM
Asset Replacement Ratio	0.1x	0x	0.1x	0.1x	0.1x
Tax Rate	13.1%	2.5%	NM	NM	NM
Net Debt-to-Equity Ratio	-10.0%	-8.2%	-2.6%	0.5%	-2.9%
Interest Cover	-29.3x	NM	NA	NA	NA

Income Statement Data (Feb)

(US$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	310	362	414	503	584
% Change	82.0%	16.7%	14.4%	21.4%	16.3%
Gross Profit	144	169	198	251	298
% Change	85.7%	17.0%	17.3%	26.7%	18.9%
EBITDA	(42)	(38)	(8)	12	38
% Change	-57.6%	10.7%	79.4%	NM	213.9%
Net Interest & Other Income	(76)	(72)	(59)	(76)	(82)
Net Income (Adjusted)	**(140)**	**(153)**	**(115)**	**(118)**	**(100)**
% Change	**-185.7%**	**-9.1%**	**25.0%**	**-2.7%**	**14.6%**

Free Cash Flow Data (Feb)

(US$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	(140)	(153)	(115)	(118)	(100)
Depreciation & Amortization	43	46	47	54	57
Change in Working Capital	(7)	3	15	21	20
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	41	62	66	73	81
Capital Expenditure	(3)	(2)	(3)	(4)	(5)
Free Cash Flow	**-65**	**-43**	**10**	**26**	**52**
% Change	**-138.3%**	**34.0%**	**NM**	**155.4%**	**99.0%**
Share / Issue Repurchase	13	5	3	3	3
Cost of Dividends Paid	0	0	0	0	0
Change in Debt	288	0	(66)	0	(17)

Balance Sheet Data (Feb)

(US$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	366	321	227	215	211
Trade Receivables	21	23	26	31	35
Other Current Assets	22	21	23	25	26
Property, Plant & Equipment	12	15	15	16	17
Other Non-Current Assets	865	522	519	513	504
Total Assets	**1,286**	**903**	**811**	**800**	**793**
Short-Term Debt	0	0	0	0	0
Other Current Liabilities	112	119	139	167	192
Long-Term Debt	281	282	217	217	200
Other Non-Current Liabilities	37	28	29	33	35
Total Liabilities	**430**	**429**	**384**	**416**	**427**
Total Equity	**856**	**474**	**427**	**384**	**365**
Total Equity & Liabilities	**1,286**	**903**	**811**	**800**	**793**

* For full definitions of *iQmethod* SM measures, see page 9.

Company Sector

Healthcare Technology & Distribution

Company Description

Accolade provides navigation services, helping individuals coordinate care while supporting interventions in order to help employers manage cost and quality trends. The company primarily services the self-insured employer market, offering a high-touch tech-enabled service that leads to 4% savings on average in the first year of engagement. The company has dual headquarters in Seattle and outside Philadelphia.

Investment Rationale

We see ACCD's ability to steer its members through the healthcare continuum as aiding both clinical and financial outcomes for themselves and their employers, driven by strong engagement rates and a high-touch tech-enabled model. And while still being unprofitable, the near-term (and accelerating path) to EBITDA/FCF breakeven should position ACCD for upside potential, leading to our Buy rating.

Stock Data

Average Daily Volume	602,874

Quarterly Earnings Estimates

	2023	2024
Q1	-0.62A	-0.52A
Q2	-0.61A	-0.44A
Q3	-0.55A	-0.40A
Q4	-0.36A	-0.18E

FY3Q'24 call takeaways

Prepared Remarks

- ACCD exceeded both top and bottom line guidance in FY3Q
- Continues to execute consistently across the business
- Strategy yielded sustainable market differentiation resulting in strong bookings growth
- Raising profitability target on 5 year outlook
- On the strength of new bookings and the utilization trends ACCD is raising guidance for FY24 and affirming expectation for ~20% revenue growth and Adjusted EBITDA between 2%-4% in FY25
- Well positioned to execute on long-term objectives
- Selling season now rolls throughout the year, particularly around newer offerings
- Booking strength and diversification reflects strength of Advocacy for customers looking to manage costs
- Utilization of artificial intelligence (AI) examples
    - Front line care team
    - Clinical intelligence
    - Analytics

Financials

- FY3Q revenue of $99.4MM
    - Due to early recognition of $2MM of performance based revenue
- FY3Q net loss of $(21.1)MM
- FY3Q adj. EBITDA of $(4.6)MM
- FY3Q adj. gross profit of $46.0MM representing adj. gross margin of 46.3%
- Reflects revenue outperformance and cost reductions from workforce realignment initiatives
- Repurchased convertible notes at a discount in the quarter
- 4Q Guidance
    - Revenue of $121.5MM-$125.5MM
    - Adjusted EBITDA of $16MM-$20MM
    - Recognized $2MM of performance guarantee in FY3Q (from FY4Q)
    - First $100MM revenue quarter, a tangible milestone for the company
    - First significantly positive adj. EBITDA quarter

- FY4Q revenue ramp
  - Recognition of cost savings performance guarantees (aligns with calendar year); given access to claims data, ACCD has a high degree of visibility into performance guarantees
  - January 1st go-live dates for new bookings
- FY24 Guidance
  - Revenue of $411MM-$415MM
  - Adjusted EBITDA of $(6)MM-$(10)MM
- FY25 Guidance
  - Reaffirming preliminary revenue and adj. EBITDA
  - Revenue growth of 20%
  - Adjusted EBITDA between 2%-4% of revenue; approximately $10MM-$20MM
- Upwardly revising 5 year plans to call for 15-20% adj. EBITDA margins in FY29
  - Prior guide called for 200-300bps improvement each year after turning profitable next year
  - Now seeing impact of cost reductions, efficiencies from AI, tech-innovations, and incremental margin impact of customers implementing multiple offerings
  - Now believes ACCD can deliver annual improvement of 300-400bps over the horizon of FY29

Q&A

- Ability to drive intra-year sales (ACCD Care, ExpertMD, leveraging health plan partnerships, etc.)
  - Have a base of Advocacy customers that are targets due to the nature of customer relationships for incremental ACCD services that can be layered on well past the beginning of a plan year
  - Also see opportunity to grow usage of existing services, but ACCD has yet to drive engagement levels
  - Opportunity in things like Blue Shield and drive utilization up on a m/m basis is in the context of in-year sales
  - These all provide opportunities to grow beyond the bookings number
- With regard to the 20% growth for 2025, how do the different businesses build to that growth?
  - Expect each of core businesses to grow in the 20% range
  - Expect business has opportunities to see incremental usage (variable usage offering) which gives potential upside to the 20%

  - Continuing demonstration of a broad set of capabilities, seeing advocacy business show up in a strong way

- Utilization trends
  - Seeing utilization of the Expert Medical Opinion (EMO) offering has been strong
  - Continued growth in utilization based revenues
  - Looking out to next year, the 20% growth rate is achievable due to strength in bookings and continued strong utilization

- Comments around bookings and selling season and any impact on the sales cycle related to GLP-1s
  - Had another strong selling season, ahead of last year
  - Consistency of sales cycle and delivery of new bookings on a y/y basis is reflective of strong demand in the environment and differentiation
  - Beginning to see the first inklings of the pipeline of evaluations happening in 2024

- Plushcare growth drivers and expectations for growth
  - Have seen extraordinary uptake of advocacy customers taking advantage of services
  - Strong adoption due to solving the physician gap
  - Primary care practice that deals with multiple conditions including weight loss
  - GLP-1s is another factor driving consistent growth rate
  - Seeing that uptake grow as ACCD rolls out to new customers and drive higher utilization rates

- Color on the shape of primary care revenue growth in FY25
  - Performance Guarantee (PG) recognition – assume needing the full year to earn those PGs
  - Expect to launch new customers on January 1
  - In April, with provide more formal guidance around the shape of that

- Revised long-term targets on margins
  - Increase in guide in the five year outlook
  - As ACCD is 2-3 quarters into the year since the investor day, found cost actions yielded great results and were able to be more efficient and realize more cost savings
  - The way ACCD is leveraging technology and innovation, AI capabilities making care teams more efficient
  - This all nets out to gross margin expansion over the next several years

- What's embedded in the increase of profitability targets? Path to margin expansion per year
    - Gross margin expansion and overall economic expansion: Advocacy customers taking advantage of incremental services
    - Taking advantage of strong unit economics offerings
    - With each cohort that comes on, drives better unit economics and profitability
    - Investments in technology that can drive efficiencies in the business
    - Tools and capabilities that ACCD is using today and begun to demonstrate the ability to achieve, but not reach the full benefit over the next several years
    - Based upon tools that ACCD is in the earlier stages of deploying to drive incremental usage based revenues
- Automation opportunity vs. potential opportunity to not dilute other offerings
    - In the context of millions of interactions per year, it requires understanding the member's needs/building a relationship and following up with that transaction
    - Capacity to summarize what occurred in that transaction and following up with that transaction
    - Incrementally where the company spends a lot of time is assessing the quality of transaction by understanding follow-up and time taken to follow up, strength of data collected
    - AI and traditional tech can play a significant role
    - Huge slice of the pie left where automation and AI can deliver value is going to be very interesting to ACCD
- Updates on the Tricare contract and assumptions within guidance
    - Government business – autism care continues to grow well
    - Tricare contract is not resolved at this point
    - ACCD is reluctant to give guidance on when it will be resolved
    - No material assumptions are baked into the out-year guide
    - Baked in rational assumptions knowing ACCD cannot control when the government appeal will be finalized
- Pro forma growth rate excluding the loss of the large customer
    - 17% growth rate on a pro-forma basis for 3Q
- Mix shift in bookings over the past few months
    - When ACCD values a booking on a utilization basis

- Will sometimes see upside in terms of revenues realize as the customer matures
- Now have a few years of bundled offerings and seeing that be fairly consistent with customers that have bundles

Price objective basis & risk

Accolade (ACCD)

Our $16.00 price objective is based on about 2.4x our CY24 EV/revenue estimate. We utilize the group of high-growth health IT companies as our universe, which all have a mix of software/internet-deployed capabilities alongside incremental high-touch services. Our valuation assumes a premium to the non-telehealth HCIT universe trading at about 2.1x sales due to its significant total addressable market (TAM), strong growth potential (even if on a revenue basis below some of the other names), and combination of both recent margin capture and incremental margin opportunity over time.

Downside risks are member attrition due to increased unemployment (in particular the two large airline customers), the ability to deliver on new customer wins, incremental spending in order to support new customer growth, delivering on its cost savings targets (particularly for the portion of at-risk revenue), maximizing the benefits from the 2nd.MD acquisition, and competition both from other standalone tech-enabled players and traditional carriers. Upside risks are better upsell to the Total Health & Benefits offering, capitalizing on expansion outside of the traditional self-insured employer market, and faster-than-expected demand for new employer customers.

Analyst Certification

I, Allen Lutz, CFA, 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 specific recommendations or view expressed in this research report.

US - Healthcare Technology & Distribution Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Accolade	ACCD	ACCD US	Allen Lutz, CFA
	American Well Corp	AMWL	AMWL US	Allen Lutz, CFA
	Cencora Inc	COR	COR US	Allen Lutz, CFA
	CVS Health	CVS	CVS US	Allen Lutz, CFA
	Definitive Healthcare Corp	DH	DH US	Allen Lutz, CFA
	dentalcorp	YDNTL	DNTL CN	Allen Lutz, CFA
	Envista	NVST	NVST US	Allen Lutz, CFA
	HealthEquity Inc	HQY	HQY US	Allen Lutz, CFA
	Hims & Hers	HIMS	HIMS US	Allen Lutz, CFA
	McKesson	MCK	MCK US	Allen Lutz, CFA
	Omnicell Inc.	OMCL	OMCL US	Allen Lutz, CFA
	Patterson Companies	PDCO	PDCO US	Allen Lutz, CFA
	Progyny	PGNY	PGNY US	Allen Lutz, CFA
	R1 RCM	RCM	RCM US	Allen Lutz, CFA
NEUTRAL				
	Cardinal Health	CAH	CAH US	Allen Lutz, CFA
	Dentsply Sirona, Inc.	XRAY	XRAY US	Allen Lutz, CFA
	Doximity Inc	DOCS	DOCS US	Allen Lutz, CFA
	Teladoc Health	TDOC	TDOC US	Allen Lutz, CFA
UNDERPERFORM				
	GoodRx	GDRX	GDRX US	Allen Lutz, CFA
	Henry Schein	HSIC	HSIC US	Allen Lutz, CFA
	Owens & Minor	OMI	OMI US	Allen Lutz, CFA
	Premier, Inc.	PINC	PINC US	Allen Lutz, CFA
	Walgreens Boots Alliance	WBA	WBA US	Allen Lutz, CFA

*iQ*method SM Measures Definitions

Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5 Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A

Quality of Earnings	Numerator	Denominator
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt – Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense

Valuation Toolkit	Numerator	Denominator
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap = Current Share Price × Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price × Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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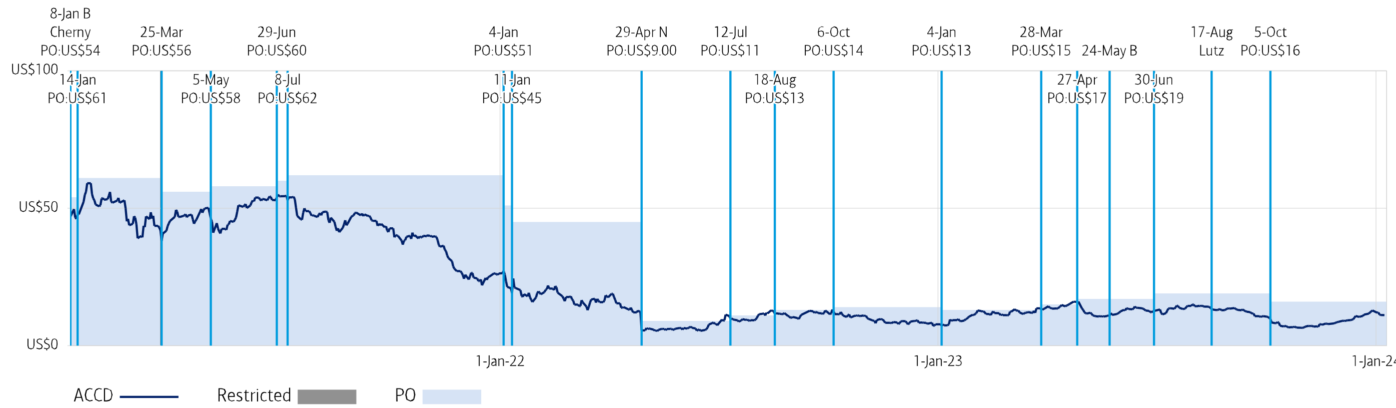
Disclosures

Important Disclosures

Accolade (ACCD) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Health Care Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	234	60.94%	Buy	115	49.15%
Hold	80	20.83%	Hold	36	45.00%
Sell	70	18.23%	Sell	29	41.43%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

[R1] Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster [R2]
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

[R2] Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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