



# Mossberg's Investor Digest

## Idea Profile

HearUSA (AMEX: EAR)

### DESCRIPTION:

Headquartered in West Palm Beach, Florida, HearUSA provides hearing aids and diagnostic services through 195 company-owned hearing care centers and online via [www.hearingshop.com](http://www.hearingshop.com). In addition, the company is recognized as the market leader of managed hearing care. EAR sponsors a network of approximately 1,900 credentialed audiology providers that participate in selected hearing benefit programs contracted by the company with more than 400+ payors, including agreements with 8 of the top 10 of U.S. health insurers.

### KEY INVESTMENT CONSIDERATIONS:

**Opportunity to be the clear leader in a highly fragmented industry** – The top 5 players only compromise 44% of the overall market. The remaining 56% is made up of 9,000 independent practitioners. EAR has an active acquisition program to aggregate these practitioners; gaining operating efficiencies and economies of scale in the process. Since the beginning of the program in 2005, the company has acquired 79 centers, representing \$38.3 million in annual revenue.

**Favorable demographic trends** – As the Baby Boomer population ages (now 44 to 62 years old), the size of the hearing aid market should increase. In fact, 94% of hearing aids are sold to people over 50 years of age. However, it appears the Boomers haven't been in a hurry to get the assistance they need. According to the Better Hearing Institute, 1 in 10 Americans (31 million) has significant hearing loss and could benefit from using a hearing aid. Of that population, only about 20% to 25% utilizes hearing aids. While it may be a challenge for the industry to change the perception of hearing aids as less of an optional luxury item to more of a medical necessity, it also represents a significant growth opportunity for the industry. One way to help encourage the use of hearing aids is a proposed \$500 tax credit, which is currently being contemplated by Congress.

**Strategic financing from Siemens** – The company enjoys an attractive form of vendor financing from Siemens. Siemens provides HearUSA with a \$50 million line of credit for use in making acquisitions and working capital financing. Provided that HearUSA's hearing aids sold are more than 90% Siemens, principal and interest payments are forgiven. Since 2002, more than \$25 million of principal and interest has been forgiven.

### KEY RISKS:

**Acquisitive growth** - Integrating operations, employees, and cultures is difficult and could cause significant disruption.

**Limited trading volume** – Limited float and low daily trading make the stock susceptible to price fluctuations.

### CATALYST:

**New relationship with AARP could be "Watershed opportunity"** – Last week, EAR signed an agreement to provide discounts on hearing aids and related services to members of AARP, one of the most influential advocates for the senior population. Of the U.S. population 50 years and older, 42%, or 39 million people, belong to AARP. To put the agreement into some perspective, 6 million AARP members admitted to having hearing loss. EAR sold just 60,000 hearing aids last year.

The agreement will call for EAR to pay a \$7.4 million annual license fee and direct a portion of its existing marketing efforts to promote the relationship. Also, in a unique arrangement, the company will work with other manufacturers and other competing distributors as part of the agreement. While management works out the economic details, they have suspended earnings guidance. An update is expected when EAR releases third quarter results.

### VALUATION:

The company trades at approximately 9.0x the lone analysts 2009 EPS estimate of \$0.17. Even assuming conversion of a portion of Siemens debt to equity, as is provided in their agreement, the strategic financing provides significant boost to EAR's return on equity. As the company turns profitable and begins producing even low single digit net margins, ROE should expand significantly. In turn, valuation multiples should reflect the higher returns and high growth expectations.

<b>(AMEX: EAR)</b>	
Investment Data (as of 8/17/08)	
<b>Recent Price</b>	<b>\$1.54</b>
52-Week Range	1.04 - 1.82
Fiscal Year End	Dec
Dividend	NA
Yield	NA
Shares Outstanding	38.0 MM
Average Trading Volume (3 mos)	83,500
<b>Market Capitalization</b>	<b>58.5 MM</b>
Cash	3.5 MM
Long Term Debt	51.1 MM
Enterprise Value (EV)	106.1 MM
LT Debt/ Equity	1.5
Tangible BV/ Share	N/A
TTM Revenue	107.9 MM
<b>EV/ Revenue</b>	<b>1.0x</b>
TTM EPS	-0.09
<b>P/ EPS</b>	<b>NA</b>
TTM EBITDA	9.5 MM
<b>EV/ TTM EBITDA</b>	<b>11.2x</b>

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