

# 2016 CEO Letter to Shareholders

Making life's important moments possible — one breath at a time®.

## To our Shareholders



Electromed delivered strong organic growth, improved profitability, and positive returns for our shareholders in fiscal 2016, reflecting our ongoing commitment to continuous product innovation and superior patient support in the high frequency chest wall oscillation (“HFCWO”) device market. Our patient-centric mission of *making life's important moments possible—one breath at a time®* lies at the heart of Electromed's recent success and is woven into the fabric of our entire organization.

### Fiscal 2016 financial highlights:

- > Net revenues increased 18.5% to \$23.0 million from \$19.4 million in fiscal 2015;
- > Gross profit rose 31.4% to \$17.9 million, or 77.7% of sales, from \$13.6 million, or 70.1% of sales, in fiscal 2015;
- > Net income grew 102.5% to \$2.2 million, from \$1.1 million in fiscal 2015;
- > Earnings per share more than doubled to \$0.27, from \$0.13 in fiscal 2015; and
- > Cash flow from operations exceeded \$2.1 million.

As this year's results attest, we met our primary goal for fiscal 2016 of continued profitable growth. We also achieved each of the other key fiscal 2016 strategic objectives that I shared with you in my last annual shareholders letter.

- > **We intensified our sales and marketing** efforts to capitalize on the significant domestic market opportunity among bronchiectasis patients in addition to the patients with cystic fibrosis and neuromuscular disorders. We recruited and hired John Kowalczyk, an accomplished former Medtronic, Inc. sales executive, as our new Vice President of Sales, and enhanced and expanded our sales team to 27 direct sales people.
- > **We expanded our third party payer contracts**, adding more covered lives during the year and remain licensed in all 50 states.
- > **We drove continuous improvement** throughout the organization, further lowering SmartVest® SQL® manufacturing costs and enhancing key operating metrics. We also achieved greater referral to approval percentage, faster approval cycle times, higher average reimbursement price, and an increase in the total number of referrals.
- > **We're investing in clinical studies** and compiling more formal evidence of the benefits of using SmartVest therapy. The SmartVest Airway Clearance System is designed for patient comfort and ease of use, which promotes compliance with prescribed treatment schedules, and leads to improved airway clearance and enhanced respiratory function. In September 2016, *Respiratory Therapy* magazine featured a manuscript that summarized outcomes for bronchiectasis patients who used SmartVest for at least one year. A group of 59 patients that we tracked over the course of one year registered a 60% decrease in emergency room visits, six-fold reduction in steroid use, and 57% fewer antibiotic prescriptions compared to the

## Revenue

(in millions)



## Operating Income

(in millions)



## Operating Cash Flow

(in millions)



## 2016 CEO Letter to Shareholders, continued

year prior to commencing use of SmartVest. These outcomes present a compelling argument for SmartVest's benefit for patients with bronchiectasis.

Earlier this year we engaged an independent engineering firm to evaluate oscillatory trough pressure of our SmartVest SQL system. The detailed third-party study of competing devices further validated the positive anecdotal feedback we routinely hear from patients and clinicians regarding the ease of use and comfort of our SmartVest SQL system, which is the lightest and quietest HFCWO device on the market. In the study, SmartVest SQL consistently delivered the lowest oscillatory trough pressure and greatest average decompression, which together may facilitate patient breathing during therapy, promoting greater comfort, improved therapy adherence, and better health outcomes. These key strategic objectives all aligned to strengthen and grow our core business in fiscal 2016.

### Looking Ahead

We made significant strides this past year, and, while quarter-to-quarter variability can be expected due to the nature of our business, I believe we enter fiscal 2017 in one of the strongest positions in Electromed's history.

Among our objectives for fiscal 2017, we aim to deliver another year of profitable organic growth, increase quality referrals, raise our rate of reimbursement on referrals and maintain the highest standards of integrity, respect and privacy. To achieve these goals our team will be dedicated to offering continuous innovation in HFCWO device features, enhancing our superior service and world-class reimbursement support, increasing lead generation with a primary focus on patients diagnosed with bronchiectasis and with the symptoms of bronchiectasis, sales force expansion, maximizing therapy adherence, executing broader third party payer coverage, and growing our institutional market share to support home care growth.

Our team is excited about the significant opportunity to serve the aging United States population, which is experiencing higher incidences of chronic lung diseases, including approximately 24 million cases of COPD. Although Medicare does not recognize COPD alone as a reimbursable condition for HFCWO, we work with physicians to identify those patients with COPD who may require further testing to diagnose additional diseases or conditions, such as bronchiectasis, that do qualify for HFCWO reimbursement. Our sales, marketing, and reimbursement teams are intently focused on the large, growing and underpenetrated population of bronchiectasis patients. We believe that approximately 15% of an estimated 370,000 Medicare patients diagnosed with bronchiectasis in the U.S. have a prescription for HFCWO therapy. Consistently using an HFCWO device like SmartVest is an effective clinical therapy that helps clear the lungs of excess secretions, reducing the risk of respiratory infections and hospitalizations.

With our upgraded sales force, meaningful product innovations on the horizon, ongoing leadership positions in reimbursement support and customer care, and increasing institutional market share to support home care expansion, we are well positioned to profitably grow Electromed's business and create long term value for our shareholders.

We have come a long way since I wrote my first annual shareholders letter to you three years ago. Our successes in fiscal 2016 reflect the hard work of our employees, who diligently serve our patients each day, and the dedication of our shareholders. I thank you for your continued support and look forward to updating you on our progress in the coming year.

Sincerely,



Kathleen S. Skarvan  
President and CEO

### Forward-Looking Statements

Statements contained in this letter that are not statements of historical fact should be considered forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include, but are not limited to, the future challenges and uncertainties we may face and our resulting performance, our market opportunities, delivery and market recognition of our value proposition, and goals for fiscal 2017. Words such as "believe," "continue," "estimate," "expected," "may," "will," "goal," "ongoing," "would," and similar expressions, including the negative of these terms, are intended to identify forward-looking statements but are not the exclusive means of identifying such statements. Although we believe these forward-looking statements are reasonable, they involve risks and uncertainties that may cause actual results to differ materially from those projected by such statements. Such statements involve known and unknown risks, uncertainties and other factors that may cause our actual results or our industry's actual results, levels of activity, performance or achievements to be materially different from the information expressed or implied by the forward-looking statements.

Factors that could cause actual results to differ from those discussed in the forward-looking statements include, but are not limited to: the competitive nature of our market; risks associated with expansion into international markets; changes to Medicare, Medicaid, or private insurance reimbursement policies; new drug or pharmaceutical discoveries; changes to health care laws; changes affecting the medical device industry; our need to maintain regulatory compliance and to gain future regulatory approvals and clearances; our ability to protect and expand our intellectual property portfolio; our ability to renew our line of credit or obtain additional credit as necessary; and general economic and business conditions, as well as other factors described from time to time in our reports to the Securities and Exchange Commission. Investors should not consider any list of such factors to be an exhaustive statement of all of the risks, uncertainties or potentially inaccurate assumptions investors should take into account when making investment decisions. Shareholders and other readers should not place undue reliance on "forward-looking statements," as such statements speak only as of the date on which they are made.

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