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Arch Therapeutics (OTCqb: ARTH) - Neutral Rated

October 30, 2023

A Bridge to an Uplist, Commercialization Building

Arch raised capital as a bridge to an uplisting to a major exchange. This combined with receipt of recent CMS reimbursement codes should pave the way for AC5 commercialization to build traction. AC5 is cleared by the Food and Drug Administration for the management of partial and full-thickness wounds, such as pressure sores, leg ulcers, diabetic ulcers, and surgical wounds.

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AC5 Commercialization Update: The average monthly order volume for AC5 is building. Arch confirms reimbursement through paid claims is happening - in various regions of the country and continues to make progress on its efforts to expand coverage and optimize payment policies with both commercial payors and contracting administrators for CMS. We view this as a key step in Arch's commercialization therapy.

What's Next? Uplisting. In September Arch announced that it completed a private placement with institutional and accredited individuals as a Bridge Offering preceding an uplisting to a planned national exchange. The private placement consisted of the issuance of common stock, at \$0.275 per share and an accompanying common warrant to purchase two shares of common stock (or pre-funded warrants at a purchase price of \$0.274 per pre-funded warrant and accompanying common warrant to purchase two shares of common stock) with total gross proceeds of approximately \$2.6 million. We note that Dawson James is acting as Arch's banker.

An Effective Barrier and Scaffold that Promotes Healing. The company's flagship product is based on its AC5 self-assembling peptide (SAP) technology platform. The platform includes AC5 Advanced Wound System and AC5 Topical Hemostat, which have received marketing authorization as medical devices in the United States and Europe, respectively, and which are intended for skin applications, such as the management of complicated chronic wounds or acute surgical wounds. The AC5 platform is a biocompatible peptide that is synthesized from proteogenic, naturally occurring L-amino acids. Unlike products that contain traditional peptide sequences, when applied to a wound, AC5-based products intercalate into the interstices of the connective tissue and self-assemble into a protective physical-mechanical nanoscale structure that can provide a barrier to leaking substances, such as blood, while also acting as a biodegradable scaffold that enables healing. Self-assembly is a central component of the mechanism of action.

Valuation: We have lowered our rating from Buy to Neutral and for the moment removed our price target. We have updated our revenue assumptions in our model. We assume a royalty model – 30% net to Arch. We apply a 30% risk rate in our Free Cash Flow to the Firm (FCFF), discounted EPS (dEPS), and Sum-of-the-Parts (SOP) models, which are then equal-weighted and averaged and rounded to the nearest whole number to derive our target valuation.

Risks to our thesis include: (1) commercial; (2) financial; (3) intellectual property; and (4) OEM and/or manufacturing. We review these risks in the Risks Analysis section of this report.



Source: Arch			
52-Week Range	\$0.39	-	\$10.80
Shares Outstanding (mil.)	4.7		
Market Capitalization (mil.)	\$3		
Enterprise Value (mil.)	\$3		
Debt to Capital	0%		
Book Value/Share	\$2.90		
Price/Book	-		
Average Three Months Trading Volume (K)	0		
Insider Ownership	45.2%		
Institutional Ownership	9.7%		
Short interest (mil.)	-		
Dividend / Yield	\$0.00/0.0%		



Risk Analysis

Commercial risk. The focus of the company is on successfully developing its products and bringing them to the market. Competition may be intense from external players as well as customers who choose to “build it themselves”.

Financial risk. The company may need to raise capital in the marketplace relatively soon. There can be no assurance that the company will be able to raise capital and do so on favorable terms successfully.

Intellectual property risk. The company may have to defend its patents and technical know-how, and there can be no assurances that the patents will not be infringed or will be held as valid if challenged, and the company may infringe on third parties' patents.

OEM and or manufacturing risk. Original Equipment Manufacturers (OEMs) may decide to make products themselves, and, as such, terminate production contracts before completion, creating revenue shortfalls. Manufacturing risks include the ability to produce and do so in a competitive, timely, and efficient way.

Exhibit 1. Income Statement

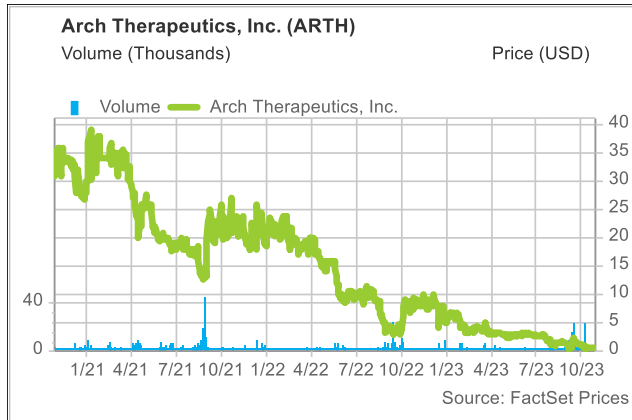
Arch Therapeutics, Inc.: Income Statement (\$000)		Oct-Dec	Jan-Mar	Apr-Jun	Jul-Sep										
Arch Therapeutics, Inc.: YE September 30		2022A	1Q23A	2Q23A	3Q23E	4Q23E	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E	2031E
Product sales															
AC5 Revenues		15,652	6	13	1,200	1,400	5,000	10,739	21,704	32,898	44,324	55,988	67,891	80,038	92,433
		-	-	-	-	-	-	-	-	-	-	-	-	-	-
		-	-	-	-	-	-	-	-	-	-	-	-	-	-
		-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total Product Sales		15,652	6	13	1,200	1,400	5,000	137,998	221,950	328,879	44,324	55,988	67,891	80,038	92,433
Expenses															
Cost of Goods Sold		51,489	18	19	120	140	500	13,800	22,195	32,888	4,432	5,599	6,789	8,004	9,243
	%COGS	10%	10%	10%	10%	10%	10%	10%	10%	10%	10%	10%	10%	10%	10%
Research and Development		1,153	161	139	303	291	1,211	1,574	2,047	2,661	3,459	3,632	3,813	4,004	4,204
	%R&D														
General and Administrative		4,520	1,103	870	1,186	1,139	4,746	4,556	4,374	4,199	4,325	4,454	4,677	4,911	5,156
	%SG&A														
Total expenses		57,162	1,282	1,028	1,609	1,570	6,457	19,930	28,615	39,747	12,216	13,685	15,279	16,919	18,604
Operating Income (Loss)		(5,709)	(1,276)	(1,014)	(409)	(170)	(1,457)	118,069	193,335	289,132	32,109	42,303	52,611	63,119	73,829
Interest expense		(567)	(524)	(809)											
Fair value of derivative liabilities in excess of proceeds		1,000													
Gain on exercise of warrants															
Loss on warrant derivative modification															
Loss on issuance of warrants															
Adjustments of fair value of derivative															
Other income															
Total other income		433	(524)	(809)	-	-	-	-	-	-	-	-	-	-	-
Pretax Income		(5,276)	(1,800)	(1,823)	(409)	(170)	(1,457)	118,069	193,335	289,132	32,109	42,303	52,611	63,119	73,829
Income Tax Benefit (Provision)								11,807	23,200	40,479	6,422	10,153	14,731	18,936	23,625
Tax Rate		5%	0%	0%	0%	0%	0%	10%	12%	14%	30%	34%	36%	38%	38%
GAAP Net Income (loss)		(5,276)	(1,800)	(1,823)	(409)	(170)	(1,457)	106,262	170,135	248,654	25,687	32,150	37,880	44,184	50,204
GAAP-EPS		(0.02)	(1.44)	(1.42)	(0.32)	(0.13)	(3.31)	24.77	39.50	57.51	5.92	7.38	8.66	10.06	11.38
GAAP EPS (dil)		(0.02)	(1.44)	(1.42)	(0.32)	(0.13)	(1.14)	24.77	10.39	15.13	1.56	1.94	2.28	2.65	2.99
Wgtd Avg Shrs (Bas) - '000s		239,915	1,249	1,279	1,280	1,282	1,273	4,289	4,306	4,324	4,341	4,358	4,376	4,393	4,411
Wgtd Avg Shrs (Dil) - '000s		239,915	1,249	1,279	1,280	1,282	1,273	4,289	16,373	16,438	16,504	16,570	16,637	16,703	16,770

Source: Company reports and Dawson James

Companies mentioned in this report:

Important Disclosures:

Price Chart:



Price target and ratings changes over the past three years:

- Initiated – Buy – May 5, 2021 – Price Target \$3.00
- Update Report – Buy – December 17, 2021 – Price Target \$3.00
- Update Report – Buy – March 15, 2022 – Price Target \$3.00
- Update Report – Buy – June 24, 2022 – Price Target \$3.00
- Update Report – Buy – September 9, 2022 – Price Target \$3.00
- Rating Change – Buy to Neutral – January 18, 2023 – Price Target NA
- Update Report – Neutral – March 6, 2023 – Price Target NA
- Update Report – Neutral – October 30, 2023 – Price Target NA

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- 1) **Buy:** The analyst believes the price of the stock will appreciate and produce a total return of at least 20% over the next 12-18 months.
- 2) **Neutral:** The analyst believes the price of the stock is fairly valued for the next 12-18 months.
- 3) **Sell:** The analyst believes the price of the stock will decline by at least 20% over the next 12-18 months and should be sold.

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Current as of 27-Sep-23

	Company Coverage		Investment Banking	
Ratings Distribution	# of Companies	% of Total	# of Companies	% of Totals
Market Outperform (Buy)	22	64.70%	3	8.80%
Market Perform (Neutral)	12	35.30%	3	8.80%
Market Underperform (Sell)	0	0%	0	0%
Total	34	100%	6	17.60%

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