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OSUR - Q2 2013 OraSure Technologies, Inc. Earnings Conference Call

EVENT DATE/TIME: AUGUST 07, 2013 / 9:00PM GMT



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PRESENTATION

Operator

Good afternoon, everyone, and welcome to OraSure Technologies 2013 Second Quarter Financial Results Conference Call and simultaneous webcast. As a reminder, today's conference is being recorded. All lines have been placed on mute to prevent any background noise. After the speaker's remarks, there will be a question and answer period. (Operator Instructions)

OraSure Technologies issued a press release at approximately 4.00 PM Eastern Time today regarding its 2013 second quarter results and certain other matters. The press release is available to you on our website at www.OraSure.com or by calling 610-882-1820. If you go to our website, the press release can be found by opening the Investor Relations page and clicking on the link for press releases.

This call is also available real time on our website and will be archived there for seven days. Alternatively, you can listen to an archive of this call until midnight August 14 by calling 855-859-2056 for domestic or 404-537-3406 for international. The access code is 19672741.

With us today are Doug Michels, President and Chief Executive Officer, Ron Spair, Chief Operating Officer and Chief Financial Officer, and Kathy Weber, Senior Vice President and General Manager of Consumer Products. Doug and Ron will begin with opening statements, which will be followed with a question and answer session.

Before I turn the call over to Doug, you should know that this call may contain certain forward-looking statements, including statements with respect to revenues, expenses, profitability, earnings or loss per share, and other financial performance, product development, performance, shipments and markets, and regulatory filings and approvals. Actual results could be significantly different. Factors that could affect the results are discussed more fully in the Company's SEC filings including its registration statements, its annual report on Form 10K for the year ended December 31, 2012, its quarterly reports on Form 10Q, and its other SEC filings.

Although forward-looking statements help to provide complete information about future prospects, listeners should keep in mind that forward-looking statements may not be reliable. The Company undertakes no obligation to update any forward-looking statements to reflect events or circumstances after this call.

With that, I would like to turn the call over to Doug Michels.



Doug Michels - *OraSure Technologies - President, CEO*

Thank you, Judy. Good afternoon everyone and welcome to our call. The Company delivered solid results for the second quarter. Both our top and bottom line results were better than expected and exceeded our guidance for the period. Consolidated net revenues were up 8% compared to 2012 and one reason for this growth was a 15% increase in our infectious disease sales, primarily due to the contribution from our OraQuick In-Home HIV test. Our focus continues to be on implementing the most effective and efficient strategies for building awareness and demand for this new product.

In addition, our molecular collection systems business delivered a very strong quarter with almost 40% growth compared to the year ago period. This part of the business is now up about 30% for the first six months of this year.

We are especially pleased with the performance of our molecular collections system subsidiary, DNA Genotek, which reported record revenues. DNA Genotek delivered not only year over year growth for Q2, but also sequential growth from the first quarter. We expect continued strong growth from DNA Genotek for the rest of this year.

Ron will now provide a more detailed overview of our second quarter financial performance along with guidance for Q3. I will then give a business update, and we will open the floor for your questions.

So, with that let me now turn the call over to Ron.

Ron Spair - *OraSure Technologies - COO, CFO*

Thanks, Doug, and good afternoon, everyone.

Our second quarter 2013 consolidated revenues were \$24.3 million, compared to \$22.6 million reported in 2012. Our consolidated product revenues increased 8% as a result of the record sales from our molecular collection systems segment and higher sales of our infectious disease testing products. These increases were partially offset by lower sales of our substance abuse testing, cryosurgical systems, and insurance risk assessment products.

Our infectious disease testing revenues were \$12 million in the second quarter of 2013, compared to \$10.4 million in the second quarter of 2012. The overall 15% increase was primarily a result of \$2 million in net sales of our OraQuick In-Home HIV test, which we began selling in the fourth quarter of 2012.

During the current quarter, gross sales of our OraQuick In-Home HIV test were \$2.1 million which were offset by \$133,000 in customer allowances, including cooperative advertising, cash discounts and other allowances. Net sales of this product included approximately \$255,000 of direct sales to public health customers. We anticipate that some public health entities may choose to use a portion of their funding to purchase our over-the-counter product in lieu of our or a competitor's professional product.

The increase in net revenues from our OraQuick In-Home HIV test was partially offset by a decline in sales of our OraQuick HIV and HCV professional products. Second quarter domestic HIV revenues were down \$344,000, or 4%, due to timing of customer purchases and reductions in government funding. Second quarter HCV revenues decreased 2% largely as a result of the variability in the ordering patterns of our customers.

Our molecular collection systems revenues, primarily representing sales of the Oragene product line, increased to \$4.7 million in the second quarter of 2013 compared to \$3.3 million in 2012. This 39% increase was the result of higher sales in the commercial market primarily due to new orders received from an existing customer who did not purchase product in the same period of 2012. This increase was partially offset by a decline in the academic research market which continues to be negatively impacted by constrained research funding, primarily in North America.



Our second quarter 2013 cryosurgical revenues decreased 7% to \$4.2 million from \$4.5 million the second quarter of 2012, primarily as a result of lower professional sales in the domestic marketplace. This reduction largely resulted from higher distributor purchases made in the fourth quarter of 2012 in anticipation of price increases implemented in early January 2013 as well as a decline in sales to the military as a result of the US withdrawal of troops overseas.

Substance abuse testing revenues decreased to \$2.1 million in the second quarter of 2013 from \$2.9 million in the second quarter of 2012, primarily as a result of lower Intercept sales. This decrease resulted from reductions in purchases by a former domestic lab distributor and our UK distributor, both of which have begun selling their own competing oral specimen collection devices.

Turning to gross margin, our overall margin for Q2 of 2013 was 60% compared to 65% reported for the second quarter of 2012. The lower 2013 margin was primarily a result of higher royalties paid on sales of our OraQuick products and a change in product mix.

Our consolidated operating expenses for the second quarter of 2013 increased \$1.8 million, or 10%, compared to the second quarter of 2012. This increase is largely due to higher spending associated with advertising and promotional activities for our OraQuick In-Home HIV test. Advertising and promotional costs for this product were \$5.4 million in the second quarter of 2013, compared to \$1.6 million spent in the second quarter of 2012.

R&D expense for the second quarter declined to \$2.7 million from \$3.1 million due to lower staffing costs, supplies, and prototype expenses. G&A expense declined to \$5 million from \$6.1 million in the second quarter of 2012 due to lower legal and consulting expenses.

From a bottom line perspective, we reported a net loss of \$5.3 million, or \$0.10 per share, for the second quarter of 2013, compared to a net loss of \$3.6 million, or \$0.07 a share, for the same period of 2012.

Turning briefly to our balance sheet and cash flow, our cash balance at June 30, 2013 was \$77 million compared to \$87.9 million at December 31, 2012. Cash used in operating activities in the second quarter of 2013 was \$1.6 million compared to \$940,000 used in the second quarter of 2012.

So, as we look forward to the third quarter of 2013, we are projecting consolidated net revenues of approximately \$24 million to \$24.5 million and a consolidated net loss per share of approximately \$0.09 to \$0.10.

With that, I will now turn the call back over to Doug.

Doug Michels - *OraSure Technologies - President, CEO*

Thanks, Ron.

As stated earlier, sales of our OraQuick In-Home HIV test were \$2 million for the second quarter which was an increase of 38% over the first quarter. Our advertising and promotional spend for this product during the second quarter of \$5.4 million represents a \$1.5 million reduction from Q1 and reflects the impact of more efficient marketing strategies and some shifting of promotional spend to the back half of 2013.

Sales growth during the second quarter came from several sources. First, the national retail chains carrying our product increased sales, and we are now beginning to recognize revenues from small independent drug stores. As you may know, retail outlets with less than \$1 million in total sales are not included in publicly available data such as the information reported by Nielsen, which many investors use to track retail sales of the In-Home HIV test.

Because of the difficulty in tracking sales through these small outlets, we had not previously been able to recognize sales to this segment of the market. However, we have recently developed an approach to recognize at least a portion of the sales to these small outlets consistent with revenue recognized from the larger retail chains reported by Nielsen.



The second growth area has come from the dot-com, or e-commerce portion of our business, as several new internet sales sites were added during the quarter. E-commerce sales by retailers increased 16% during Q2 compared to the first quarter, and total online sales, including sales through our own OraQuick.com site, now represent about 9% of our HIV over-the-counter business.

The third area of growth has come from third party agencies and customers in the public health market. These organizations continue to purchase our professional OraQuick product, but now some of these are looking to incorporate our OraQuick In-Home HIV test as a way of expanding their testing programs. Sales to these customers were \$255,000 for the second quarter.

We are encouraged by the growth in the over-the-counter business and by the fact that our growth has been driven by interest across multiple channels. However, Q2 sales were below our expectations and consequently we have executed several critical studies to understand opportunities for improvement.

A key goal of our marketing program is to drive product awareness within our target populations. We recently completed an awareness tracking study to measure our achievement against goal. This study revealed that while our awareness is building, our unaided, or top of mind awareness levels with key targets are below expectations at this point in our launch. Unaided awareness levels range from 6% to 12% depending on the consumer target measured. To understand the slower than expected awareness build, we thoroughly reviewed both our messaging strategy and execution and our media buying approach. We are making modifications to both which I will discuss in a minute.

This same study also revealed that interest in our product remains very high within all of our key target groups. These include MSM, or men who have sex with men, African-Americans, Hispanic Americans, and sexually active adults 18 to 34 years old. Interest among members of the MSM and African-American communities remains the highest and all of this is consistent with our prior research and continues to be very encouraging.

We also continue to analyze the demographics of our top selling stores and markets for both retail purchases and e-commerce sales. This review shows that our sales are skewed towards several of our primary target populations, including the MSM and African-American populations. So, while our overall awareness is lower than we hoped, we are connecting well with our intended consumers.

Not surprisingly, our sales are more concentrated in higher HIV prevalence markets, with the top 15 of these markets representing approximately 50% of sales. As you know, we have also been working with our retailers to improve retail conditions, and we have seen chain-wide increases in store level inventory and a reduction in out-of-stock situations. We continue to work with retailers to optimize the level of inventory in the stores based on product movement. Some retailers continue to place the product behind the counter or have attached security devices as a theft deterrent. Our research has shown that this remains a significant barrier to higher consumer purchases and we are continuing to work with these retailers to identify and test creative solutions to these challenges.

A final area of focus has been understanding the effectiveness of our promotional activities. Our promotional efforts have included TV, radio, digital and print advertising, local events such as promotions in bars, gay pride festivals, and churches, and retail store level promotion. Although all of these programs have contributed to product sales, they have done so in varying degrees, and we have been evaluating which specific programs provide the greatest return on our investment.

We have already made adjustments based on this analysis. For example, we have launched a revised 15 second commercial, which connects better with our target audiences at a lower cost, and we have shifted our media strategy to incorporate more predictable and measurable media weight. We are also further refining our messaging by target audience and we're planning to shift more promotional support to key markets.

Going forward, we believe the most effective use of our promotional dollars continues to be a combination of local level promotions, national TV advertising, and strong digital and online presence.

Turning briefly to our consumer support center, this part of the business continues to perform exceptionally well and is meeting or exceeding all of our service level goals. In addition, the product seems to continue to perform well in the field, as our consumer complaint rate is very low and below industry standards.



So, as we look forward to the rest of the year and beyond, our focus remains on building awareness among our target consumers through more focused messaging and a more effective and efficient media strategy. We will also continue addressing the barriers to purchase at retail.

We will be implementing refinements to our strategy throughout the 3rd quarter, and we expect to somewhat moderate the level of our promotional spending during this period. This will likely result in a sequential decline in retail sales in that quarter compared to Q2. We would expect sales growth to resume in the 4th quarter as the full implementation of our revised approach starts to be realized.

Finally, discussions are underway with potential collaborators to expand our OraQuick In-Home HIV test sales in international markets. Interest is high and we are looking at multiple foreign jurisdictions. We hope to have something more to announce on this in the relatively near future.

Turning next to our OraQuick HCV test, as Ron indicated, total HCV sales were down slightly for the current quarter compared to last year. However, second quarter sales of our OraQuick HCV test were up sequentially over the first quarter, and we continued to add new customers. Importantly, we expect that sequential growth will continue at least for the rest of 2013. A major contributor to this growth will be a significant international NGO, which has already placed a large order for the third quarter and may place similar orders in future periods.

There have also been significant positive developments on the hepatitis front since our last call. In June the US Preventive Services Task Force issued final recommendations giving HCV screening for both at-risk individuals and baby boomers a B grade. As you may know, under the Affordable Care Act, preventive services that receive an A or B grade from the Task Force are expected to be covered by insurance without cost sharing. The B grade for screening baby boomers represents an improvement from the Task Force's initial draft recommendations issued late last year, which had proposed a C grade for screening of this type. Although the Task Force's final recommendations do not take effect until next year, we believe they will help drive expanded HCV testing, including with our OraQuick HCV product.

In addition, the New York state legislature recently passed a law that would require that doctors offer Hepatitis C testing as a routine part of healthcare provided to baby boomers. This law is consistent with the CDC's recommendations on HCV testing and is now on the Governor's desk for signature. Assuming the Governor signs this into law, the statute would be applicable to take effect in 2014 and would represent another positive development supporting expanded HCV testing. So, we remain very optimistic about the long-term prospects for our rapid Hepatitis C product.

A final area I want to address is our molecular collections systems business. Most of DNA Genotek's record-setting revenues this quarter reflect significant growth in commercial customers' use of the FDA-cleared Oragene saliva collection product line for DNA testing. In particular, we continue to see healthy activity and purchasing by commercial customers using these products for clinical and pharmacogenomic testing, consumer testing and commercial research. Gains in the commercial market more than offset a decline in DNA Genotek's academic research revenue, which recently has been trending below quarterly levels seen in prior years. We expect DNA Genotek's commercial revenue to continue to grow for the remainder of 2013 and to offset weakness in the academic market due to constrained research funding primarily in North America.

So, in summary, I am pleased with our performance for the second quarter. The contribution from our OraQuick In-Home HIV test and the record revenues at DNA Genotek are welcomed additions to the Company. We are excited about future opportunities for growth, and I look forward to reporting on our progress in future calls.

So, with that, I will now open the floor to your questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Amit Bhalla, Citi.



Nick Nolan - *Citi - Analyst*

Good afternoon. This is [Nick Nolan] in for Amit. First, I want to talk a little bit about HIV and the spending there. One of the things you guys talked about, diversifying that strategy and how you expect to moderate spending, what kind of moderation could we expect in spending in 3Q and what kind of impact should we expect that to have on sales in the quarter?

Ron Spair - *OraSure Technologies - COO, CFO*

Hi, Nick. It's Ron here. We had talked about the spending in Q2 being about \$5.4 million for advertising and promotional spend. Our current estimates are that the Q3 spend should be in the neighborhood of about \$3.5 million, \$3.6 million for advertising and promotional spend activities in the third quarter.

And as Doug pointed out within the composition of our revenues generated in Q2, we did have included in there approximately \$255,000 worth of sales into public health. So, you really have to look at the true retail consumption, net of that public health revenue and we are estimating that as we work through this refinement phase of our strategy and are reducing our expenditures during that time that we will see a slight drop in revenues at the retail consumption.

Nick Nolan - *Citi - Analyst*

What do you expect full year spending to be for the product?

Ron Spair - *OraSure Technologies - COO, CFO*

We think we're anticipating that the previously discussed targeting spend levels in advertising and promotional in the high teens and millions will still be met. As we get through this phase and then initiate the spending associated with the new roll out of the different components we should be back up in the high teens of millions, so \$19 million to \$20 million worth of spending.

Nick Nolan - *Citi - Analyst*

Then I want to follow-up with maybe your studying to see what your advertising is the most effective. Have you done any studies to see on the price sensitivity of customers to see if there's an impact of potentially a lower price and how the market will respond to that?

Kathy Weber - *OraSure Technologies - SVP, GM, Consumer Products*

This is Kathy. We have included price in pretty much every piece of research we do, we ask consumers for their perceptions around price. So, including the awareness tracking study that Doug referenced, we asked questions about price. Price does not seem to be a major barrier. Very consistent with the earlier research, our price is appealing to a large segment of the population. So, we haven't seen anything consistent on price from prior research and we don't believe it's a barrier.

Operator

Peter Lawson, Mizuho Securities.

Peter Lawson - *Mizuho Securities - Analyst*

I may have missed this but what was the strength in the DNA collection business, which customer groups?



Ron Spair - *OraSure Technologies - COO, CFO*

It's primarily in the commercial area, Peter. We haven't identified specifically what customer or customers represented that but generally overall just an uptick in volumes in the commercial side of the business as opposed to the academic side.

Doug Michels - *OraSure Technologies - President, CEO*

I think -- Peter, just to expand on that a little bit, obviously we continue with 23andMe and with Ancestry which we've talked about, two of our larger commercial customers but we're seeing additional customers and growth and repeat purchases across all of our commercial customers really and that includes customers that are operating in the pharmacogenomics space where the product's used in evaluating pain or psychiatry, neurology, ophthalmology. We're seeing continued purchases in reproduction on the commercial front where a product is used in pregnancy genetics. So, overall, the commercial business just performed very well and we obviously are participating in multiple segments there which diversifies our business in that segment and gives us a lot of confidence and optimism for the future.

Peter Lawson - *Mizuho Securities - Analyst*

Were there any stock in orders for that business?

Ron Spair - *OraSure Technologies - COO, CFO*

I would say none of any significance that would skew our Q2 results. We expect sequential growth in Q3 and strong growth through the remainder of the year.

Peter Lawson - *Mizuho Securities - Analyst*

Then the pull back on the R&D spend, should we think about that kind of trend happening or that \$2.7 million number for Q3 and Q4 or is that a one-time blip?

Ron Spair - *OraSure Technologies - COO, CFO*

I think the level of expenditure will be in and around that range for the balance of the year.

Operator

Spencer Nam, Janney Capital.

Spencer Nam - *Janney Capital - Analyst*

Maybe I'll start off with a comment that was made, I believe it was Doug. You made this comment on the third quarter over-the-counter HIV test, the revenue may be slightly below the levels we saw in second quarter. Did I hear that correctly? I know you guys are trying to calibrate the marketing strategies and so forth but I'm curious if the volume is really tied to the marketing strategy or that the different types of marketing efforts? And does that mean going forward whether that we should expect some sort of a function of how much marketing dollars you guys put into this effort versus how much you're going to get out of the revenue lines? How do you think about all those issues, given the comment that you gave?



Doug Michels - *OraSure Technologies - President, CEO*

I'll let Kathy speak to some of the specifics that we believe are going to increase the effectiveness of our marketing spend. Obviously it is a function of spending but we have a wonderful opportunity based on the research to spend more efficiently and consequently more effectively as well. And we believe that's what these refinements to our activities are actually going to represent. I'll let Kathy talk about some of the specifics.

Kathy Weber - *OraSure Technologies - SVP, GM, Consumer Products*

I think, Spencer, what we've been doing, as you know we've put a lot of different tools out in the marketplace. We have TV advertising, local radio, national radio, event marketing, PR, many different marketing elements out there. And what we've been doing now that we've completed this six market tour and have six months of the year under our belt we've been evaluating every program relative to sales to understand which programs deliver the highest lift and the highest ROI.

And the short story there is that our local programs seem to be delivering very effectively for us. They have some of the highest ROI. Our national advertising has improved with the changes we've made to our copy and to our media buying approach. And then we've also learned some things about the target consumers where we're building the most traction. As Doug said we appear to be building traction with MSM and African-Americans but also because we're below expectations from an awareness standpoint we need to refine our messaging. We need to get a little bit tighter into those communities and have more insight based messaging.

So, what we're doing right now is spending a little bit less, just during the very, very short-term, spending in the areas where we see good ROI and developing optimized messaging, renegotiating some of our media so that we can come out of the third quarter and then into the fourth quarter in a stronger place with better messaging, better media strategy, focusing really in on those things that have popped us the highest ROI investments. To Doug's point, the whole purpose is to continue doing what drives the business and hold back where we weren't seeing the kind of turn we wanted to.

Spencer Nam - *Janney Capital - Analyst*

I think I get that clearly. So, if you think about third quarter and just thinking about what kind of revenue trajectory we could expect out of over-the-counter HIV, is it going to be a lot less than what we saw in second quarter or is it going to be slightly down? Qualitatively how should we think about that?

Ron Spair - *OraSure Technologies - COO, CFO*

Spencer, I would say at this point we would think it would be slightly down. As I mentioned earlier in my remarks to more or less the same question, included in the revenues for the second quarter were approximately \$255,000 of revenues from public health placements of the OTC HIV kit. So, you have to take that into consideration when you're looking at what the Q3 number could be. So, we're basically communicating that that \$2 million is not likely to be achieved in the third quarter here. It will be down slightly.

Spencer Nam - *Janney Capital - Analyst*

Got it. Then on the second quarter number, the HIV number, Doug, I think you also mentioned in your prepared remark that it was below your expectations. What were you guys expecting? Can you guys tell us that?

Doug Michels - *OraSure Technologies - President, CEO*

We haven't given that level of granularity but obviously we anticipated a strong awareness level amongst our targeted consumers. And awareness is going to drive the individuals to retail or online to purchase the product. I don't know if Kathy wants to add anything additional to that?

Kathy Weber - *OraSure Technologies - SVP, GM, Consumer Products*

Yes. In terms of how we have diagnosed the source of the lower revenue, awareness was a big piece of it and that's driven by we think the messaging and the media strategy. We have good fixes in place for that. The second piece we haven't really talked about is the retail environment.

As we've spoken on some of the calls, as many of you have raised to us, we had some suboptimal retail environments out there in terms of inventory levels at store level and also the theft deterrent devices, the BTC and the spider wires that were put on the product. The good news is we've made good progress on the inventory front. If you think about where we were in the second quarter we had -- the beginning of the second quarter we had some chain-wide out-of-stock levels at the 8% to 10% range. Those are down now to 2% to 3% range for chain level.

What we've been doing is spending a fair amount of time looking at the retail POS data and looking at store level data to understand -- it may look 2% chain-wide but how does it look when you look at your high volume stores, your medium volume stores, your low volume stores? And we're seeing opportunities to continue to improve the inventory load in the stores dependent on their volume. And there's some very good insights we've discovered. We're taking it back to the retailers. The retailers remain very strong partners with us and we're working with them on that. So, to the comment on the lower than expected revenues, we believe we know why and we're making good progress and putting the fixes in place.

Operator

Jose Haresco, JMP Securities.

Jose Haresco - *JMP Securities - Analyst*

Good afternoon. I wanted to quickly switch gears to HCV for a second. From what I'm hearing there's a backlog of HCV patients for lack of a better term being warehoused. They're all waiting for the approval of a new drug later this year. Have you given any thought to perhaps about how should you truly think about what would happen to your quick HCV business if and when that drug is approved. It seems to be it would be in Gilead's best interest to find as many of the HCV patients out there beyond those that have been warehoused right now.

Doug Michels - *OraSure Technologies - President, CEO*

I think that's absolutely the case and the exciting thing about some of these new therapies is that the treatment duration is going to be much shorter and so it's likely that they'll work through that warehoused patient population quickly and in order to really capitalize on the opportunity of therapy we're going to have to diagnose a whole lot more patients very quickly. Obviously with the new task force recommendation, the CDC recommendation to test all baby boomers where there's the highest percentage of chronically infected Hepatitis C patients, a one-time test for Hepatitis C sets itself up ideally for the use of a rapid test.

Clearly once these new therapies are available and promoted and physicians understand that they can cure these patients, there's going to more Hepatitis C testing broadly so it's going to benefit everybody in the diagnostic space. We think we're very well positioned to capitalize on the opportunity.

Jose Haresco - *JMP Securities - Analyst*

Are you hearing any specific feedback? I know it's still four months away from that approval but are you hearing any specific feedback from your customers in terms of how the test will integrate into that treatment paradigm?



Doug Michels - *OraSure Technologies - President, CEO*

Absolutely. All these developments in the marketplace are creating a lot of buzz and excitement about Hepatitis C diagnostics. We're seeing increased numbers of customers coming into the queue with first time orders and repeat orders and we plan to capitalize on this both in the physician office market as well as in the public health market.

Operator

(Operator Instructions) Mark Massaro, Canaccord.

Mark Massaro - *Canaccord Genuity - Analyst*

I'm intrigued with the New York state legislature and the law requiring doctors to offer an HCV test. Can you maybe provide timing? Would that go into effect potentially January 1? And secondly, are you in any other discussions with any other state legislatures?

Doug Michels - *OraSure Technologies - President, CEO*

I believe that should the government sign it, it would be effective in the first quarter of 2014. And we know that there are other legislatures that are in other states that are evaluating that same opportunity to put a law in place encouraging or mandating routine testing for Hepatitis C among the baby boomer population.

Mark Massaro - *Canaccord Genuity - Analyst*

And maybe as a follow-up with respect to the international NGO could you give us maybe a little flavor of what type of entity this is and similarly are you in other discussions with NGOs?

Doug Michels - *OraSure Technologies - President, CEO*

We are, not just on the international front but here in the United States. And given the new recommendations, there's a number of public health jurisdictions and other agencies that are looking at adopting routine Hepatitis C testing alongside the work that they're doing with rapid HIV testing and we're having discussions on multiple fronts and I believe that they're going to bear fruit in the quarters to come.

Relative to this international NGO it's an organization that operates really globally and in multiple countries both in Europe, Eastern Europe as well as in Asia and they provide medical services to generally the underserved. Well funded. They've been providing not only HCV testing but also HIV and other diagnostic services to a significant population for some time. So, this is a well established program. And actually they're going to begin using our HCV test based on its superior performance as demonstrated in clinical studies both here in the United States as well as around the world. So, it's a really wonderful win for the Company and we believe it's going to be a nice contributor in the third quarter and beyond.

Mark Massaro - *Canaccord Genuity - Analyst*

Maybe just one last follow-up. The DNA Genotek business is performing well. Can you maybe provide a little more color with respect to the pipeline of commercial customers or conversations? I know you called out pharmacogenetics, pregnancy, genetics, and the like but it seems to me that the business has an opportunity to rise as a result of the overall uplift in molecular diagnostics as a whole. Maybe could you just shed some light on discussions you're having with potential customers?



Doug Michels - *OraSure Technologies - President, CEO*

We completely agree. And I tried to highlight some of the areas in which the Company's operating. Pain for example, there's genetic markers which can help physicians determine how a patient is going to respond to different types of pain medications, can help with dosing decisions. The same applies with psychiatry, neurology, ophthalmology, and the like. There's multiple commercial opportunities in each one of those areas that the Company's pursuing. We don't see any governors right now on the number of opportunities nor the size of opportunities and the companies pursuing them.

I think it's important also to understand that the academic market continues to be very important to DNA Genotek and despite the fact that that is under funding pressures primarily here in the United States and that's impacted our revenues somewhat, the number of orders received from the academic research customers continues to grow. We were up 30% sequentially in terms of orders in the academic research area which says interest continues to be very high amongst that community in our product offering.

One of the things that this funding issue is causing us a challenge with is we're seeing fewer large orders coming from the academic research space. We define large orders in the academic research space as orders in excess of \$10,000. And actually the number of orders in excess of \$10,000 that we received during the quarter was down about 20%. And so it's not that customers aren't ordering. They just don't have the funds to fund as large of studies as they have previously.

So, how we're going to respond to that is we're going to continue to press in the academic research market. Obviously there's interest in the product and so we're going to continue to look to expand not just in Europe or the United States but in rest of world where we're making some good progress and we continue to seek regulatory approvals in some very key markets. Russia is a good example. And in the second quarter we also received approval to begin selling in China.

So, a lot of excitement both in the academic space as well as on the commercial front, great results from DNA Genotek in the quarter and we're looking forward to a real great year from them.

Operator

Shaun Rodriguez, Cowen.

Shaun K. Rodriguez - *Cowen & Co. - Analyst*

Can you talk about the impact on the competitive landscape of the Alere announcement -- I guess that was late last week that they're developing their own HIV professional test. Maybe more specifically to the extent you've viewed some incremental competitive challenges coming from the DPP product if it ever gets CLIA waiver on the oral indication, does at least the potential uncertainty in terms of who will be marketing that many push out any potential impact you see or is this a non-event in your eyes?

Doug Michels - *OraSure Technologies - President, CEO*

Shaun, it's very difficult to comment on the specifics of that announcement. I don't know what Alere's obligations were to Chembio, what the timing arrangements were in terms of their obligation and the like. I think those questions would be better directed to Alere and Chembio.

We've been dealing with the competitors in the rapid HIV space for years. The better part of five to seven years I think. There's multiple FDA approved rapid HIV tests in the marketplace. We continue to differentiate our product offering and continue to compete very effectively. We'll see how their relationship develops, whether it unwinds or what happens. Once we've got better clarity on that we'll give you our perspective on it.

Shaun K. Rodriguez - Cowen & Co. - Analyst

Fair enough. Thank you. On HIV-OTC, on the \$250,000 or so in public health revenues for that product, I understand and appreciate why you called it out as something we should think about in Q2 and also Q3 but I'm curious where those kits went? Why the OTC kits were sold into that versus the professional? Really just trying to understand whether that's a one-timer thing or whether that could pop up from time to time?

Doug Michels - OraSure Technologies - President, CEO

That \$255,000 in revenue actually went to quite a number of public health jurisdictions. There were a few large purchases at either the city or state level and these jurisdictions planned to integrate the at-home HIV test into their testing programs.

I think at this point in time it's a little early to make predictions as to how effective those strategies are going to be and whether they're sustained in future periods but I can tell you that we're also in active discussions with other jurisdictions today that are considering similar kinds of purchases. What the timing of those might be and what the magnitude of those might be is a TBD. And we'll try to give you visibility both to the effectiveness of the programs that have already purchased and are using the product as well as we identify and secure additional purchases from other jurisdictions what those might be and how the product might be used.

It's exciting. I think that we've got extraordinary support from the HIV-AIDS community, from our professional customers, from medical providers that use our rapid HIV test on the professional front and they see a utility for the over-the-counter test.

As Kathy said, the over-the-counter product continues to perform very well in the hands of consumers. And we know that consumers are testing positive. They call our call center looking for a referral and the like. We've had meetings with the CDC and FDA to talk about our positive experience with the product and I think there's a growing appreciation that this is a valuable contributor in the fight against HIV and AIDS.

Shaun K. Rodriguez - Cowen & Co. - Analyst

That's interesting. Thank you. Lastly, I apologize if you covered this on the call, but on HCV I think you said in the past in 2012 about 200 customers have ordered. I think you said over 40 new customers last quarter. I think you mentioned that you continue to add customers in the quarter. But can you be more specific on this? Any notable reorder trends or anything that popped up in the quarter just in thinking about how many of these new customers actually turn into more consistent customers?

Doug Michels - OraSure Technologies - President, CEO

We track that as best we can both on the physician office front as well as in public health. And for the quarter, just an example, for the quarter on the physician office side of the orders received about two-thirds of the orders were first time customers. So, new customers deciding to test. A third of them were from repeat orders and 50% of those repeat orders were orders that had ordered within the previous three months. They ran through the tests and they're reordering.

We're capturing that kind of information. About two-thirds of our business on the public health line on HCV were from repeat customers. About a third were new customers. So, this is something we're tracking and we'll try to give you as good of color as we have on it in future calls.

Operator

Nicholas Jansen, Raymond James.



Nicholas Jansen - *Raymond James - Analyst*

Maybe following up on one of Shaun's questions in terms of selling the OTC. Are you effectively just losing the business in one area and then picking it up in the other area? Maybe just try to walk me through how that revenue dynamic played out. Just trying to get a sense of if that strategy picks up steam how should we think about the domestic core professional business being down 4% in the quarter and how should we think about that modeling going forward particularly in light of government reimbursement challenges? Thanks.

Doug Michels - *OraSure Technologies - President, CEO*

I think it's too early to tell to be quite honest. The sales of the OTC kit were quite small relative to our HIV professional business. You're accurate in saying that HIV professional was down, approximately 4%. If you subtract out the HIV-OTC from our total infectious disease it was like you said about 3.7%. You look at that on the total revenues of HIV professional it's a few hundred thousand dollars. That can be one order from a public health customer in a quarter. You know those can shift from quarter to quarter.

So, I think it further supports what we've said previously, that we believe our HIV professional is stabilized. I don't think that we're going to see the over-the-counter product really cannibalize our HIV professional business to any great extent. I don't see public health programs adopting over-the-counter testing broadly at the expense of their HIV professional, their routine testing that they're doing out in the community or in clinics.

I think it's a supplemental strategy. They use it for partner testing, when somebody tests positive in the clinic and one of their key strategies is to reach out to that individual's social network because obviously if they can connect with those individuals and get them tested, they generally find a high yield of positive test results from testing that social network. A lot of times people within that social network are reluctant to come forward and a confidential home HIV test can become a valuable tool in helping those individuals learn their HIV status. That's just one example of how the product could be used.

Nicholas Jansen - *Raymond James - Analyst*

That's helpful. Just one on DNA Genotek, thinking about 23andMe came out with a press release yesterday or maybe earlier this week regarding going after a national TV advertising campaign. I just wanted to get a sense of if that kind of ramps up quite nicely for them how do you think about it in context your manufacturing capacity to meet the demand that perhaps could be or if that's a home run advertising strategy?

Doug Michels - *OraSure Technologies - President, CEO*

I sent Ian Curry, our President, a note that he better get his capacity up. It remains to be seen what the impact of that advertising is going to have. But it certainly isn't going to be a negative. It will be a positive. And I looked at the campaign. I think it's clever. And to the extent that it's effective, it will have a very positive impact on our business we would expect.

Operator

Amit Bhalla, Citi.

Nick Nolan - *Citi - Analyst*

This is Nick again. Following up on HCV. Do you guys have any updates on partnership opportunities there? And also is there any opportunity from a co marketing perspective on the HIV front to accelerate OTC sales?

Doug Michels - *OraSure Technologies - President, CEO*

Relative to pharma discussions, you should know we're engaged on multiple fronts and in discussions with certainly more than one of the relevant pharmaceutical organizations. We are discussing collaborations that are pretty broad, ranging from possible collaboration on discreet programs and events to broader longer-term types of initiatives. And these discussions span both domestic as well as international opportunities.

It's not appropriate right now to get into more detail than that but you should know that we're having multiple discussions ongoing and I think it highlights what we've been saying and what some of you guys have said on tonight's call, that it's an exciting time. There's clearly a lot of excitement about the new therapies and there's a broad recognition that diagnostics are going to be key to realizing the full potential of these new drugs as they become available.

Operator

Thank you for your questions. I will now turn the conference to Doug Michels for closing remarks.

Doug Michels - *OraSure Technologies - President, CEO*

I just want to thank you for joining us on the call this afternoon and this evening. We look forward to speaking with you again after the third quarter. Appreciate all your support. Have a good night, everyone.

Operator

Ladies and gentlemen, thank you for your participation in today's conference. This does conclude the program. You may all disconnect at this time.

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