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# EDITED TRANSCRIPT

WMGI - Wright Medical Group NV at JPMorgan Healthcare Conference

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## CORPORATE PARTICIPANTS

**Bob Palmisano** *Wright Medical Group N.V. - President, CEO*

## CONFERENCE CALL PARTICIPANTS

**Andrew Hanover** *JPMorgan - Analyst*

## PRESENTATION

**Andrew Hanover** - *JPMorgan - Analyst*

Good morning, everyone. We're going to go ahead and get started. I'm Andrew Hanover from the JPMorgan med tech team and it's my pleasure to introduce this morning, from Wright Medical, the Company's President and CEO, Bob Palmisano.

Following Bob's presentation, we'll have a breakout session down the hall in the Yorkshire room, and if everybody can just remember, if they don't mind, turning off or silencing your cell phones, I would appreciate it. Bob?

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**Bob Palmisano** - *Wright Medical Group N.V. - President, CEO*

Thank you, Andrew. It's great to be here this morning and tell you a little bit about Wright Medical, positioned to accelerate, which is an important distinction we have.

I'm not going to read through all the forward-looking statements. These are on our website, or Julie Tracy, who is here, would be happy to go through these with you.

So, where are we? We are a company that has transitioned itself, transformed itself, to be in three really good markets, really the fastest-growing markets in orthopedics, upper extremities, lower extremities, and biologics. These are huge markets, about $8 billion of opportunity, and we are in the markets that we are in growing about two times the market.

So, last year at this time, we talked about -- a lot about a merger that we had just completed with almost an equal size company, Tornier, which had major presence in the upper extremity business. So where are we? What have we accomplished in the last year? I'm well aware of the fact that most of these integrations don't go well and the roadside is littered with the carcasses of CEOs who did not do well at these. But I think that we have really come through this pretty well.

We completed over 80% of our integration milestones in the first year. We completely integrated our global sales force, really with minimal disruptions. We colocated our major international markets' facilities and consolidated them into a single ERP system. We enjoyed better-than-expected timing of our revenue dyssynergies. We had said that we thought we were going to have $25 million to $30 million in revenue dyssynergies in the first two years. We lowered that to $25 million, and in 2016, it amounted to about $15 million. We are ahead of schedule with our cost synergies, and as we said on our third-quarter call, we anticipate $25 million in 2016 out of a total of $40 million to $45 million. So, really on track regarding the financial parameters of the integration.

In addition to that, we've materially improved our balance sheet, and I'll talk about that later. We have significant opportunities to continue to improve our balance sheet, improve inventory, instrument set utilization, as well as DSOs. We successfully completed the sale of our European hip and knee business. This is the second hip and knee business that we have sold. I have nothing against hip and knees, I assure you, but they just don't fit into what we want to accomplish in the Company, being in high-growth markets.

We also got through, to a great extent, the litigation issue that has been hanging over the Company for a period of time and reached a master settlement agreement.

We did all this at the same time growing two times the market. So it was a great job, I think, by the people who actually do the work at Wright Medical. That's not me. That's the other folks.

So, differentiation matters. This is an important tenet. That's why we decided to focus on these high-growth markets. So we are in markets that we can differentiate ourselves from competitors large or small. We are really the recognized leader in the extremities and bio markets. I don't think that's really much in dispute at this point.

We have a global footprint with the largest specialized direct sales force. You might recall a couple years ago in our lower extremity business, we terminated our agreements with most of our distributors and went direct. The Tornier business is about half direct and about half distributor, and around the world, most of our big subsidiary markets are also direct.

We have leading technologies which play a powerful role in differentiating us from our competitors. We have a strong R&D pipeline that I'm going to go through, and we have a strong emphasis on the fundamentals of running a medical device company, that being medical education.

So 2017, what are our priorities? Revenue growth and cash. That's our priorities, pretty simple stuff.

How are we going to do that? We are going to selectively expand our US sales force. We're going to be adding about 85 new direct quota-carrying reps. This is because we have the opportunity in front of us and we want to grasp it. Now of the 85, only about one-third of these are new hires. The remaining two-thirds of these 85 are people that are associate sales reps in our training and medical education area that will move up to quota-carrying reps.

So -- but we will have 85 additional quota-carrying reps mixed more heavily towards the lower side than the upper extremity side, but also a lot in the -- and we will take full advantage of that and get the productivity levels up as fast as we can.

We also -- important in our growth is products, new products. The PERFORM REVERSED glenoid launch, which is being launched in the first half of this year, is a big deal. It's a real big deal. It fits anatomies that are as smooth and as reproducible as the regular PERFORM products treat and we will then have an additional lead.

And additional to that, we will continue the launch of the AUGMENT Bone Graft, which got off to a great start in 2016 and is on a great trajectory, I think, as we go forward.

Regarding cash, we will complete the integration and realize the cost synergies that we've been talking about. We will improve inventory, instruments, and DSOs -- DSO efficiency. Big opportunity on our balance sheet. It's a target-rich environment and I think that we have really the mindset to go after this full bore. We will leverage our SG&A and this will -- and parts of this will grow at significantly less than the sales growth that we were anticipating and we'll be able to get additional leverage.

So the key financial objectives are the same as we said when we announced the transaction almost two years ago. It is that we will have a company that's growing mid-teens, we will have high 70% margins, and we will be a 20% EBITDA company two or three years after the close.

So, where are we? In our upper extremity businesses, we've extended our leadership position in shoulder with new product launches and increased sales force productivity. This is a great market. We have a significant lead technology-wise, and we'll get into some of that as we go on, but these are, again, a big market. The market is growing fast, 8% to 9%, and we are growing about double that.

Regarding on the lower extremity side, particularly foot and ankle side is that the market is a little bit less mature, growing at 8% to 10%. Again, we are growing about two times the market.

And in bio, bio, led by AUGMENT, is the fastest growth area of our Company, and it has been and I think it will be for a period of time as we get into the future, and we really like bio in that it acts like -- you don't have all the working capital restraints you do in the orthopedic hardware business.

So we have a strong product pipeline that is growing our opportunities, upper. We launched SIMPLICITI last year and it's in rollout and is going gangbusters. We launched -- we are launching PERFORM, the PERFORM REVERSED. The market is moving more from anatomic to reversed. This is a very important product and will be launched in the first half of this year.

BLUEPRINT, enabling technology. One thing that I talk about a lot is on our major products is that one of the things that differentiates us is that we not only launch great hardware implant products, we launch and have enabling technologies that make the use of these products easier for the physician, have side benefits such as taking less time, etc., and this -- and preplanning these surgeries that help us in terms of bringing in a lot fewer implants into a surgery because the doctor knows what he's going to need or she is going to need before doing the surgery.

Lower extremities, we'll continue the INFINITY launch, which is going gangbusters. SALVATION limb salvage system is in rollout. We had great success with that last year. It's a fast growth area for us. We're launching line extensions in this in the second half of this year.

We will be launching the INVISION system, which is kind of the last frontier here in total ankle in terms of having doctors being more comfortable doing total ankle replacements in that they do have a bona fide revision system that if they need to explant that product and put another one in, they have a product specifically designed to do that, and we are in the lead on that, I believe, also. Also in our core foot and ankle business is that we will be launching a low-profile ORTHOLOC 3Di product later in the year.

Biologics, Bone Graft is in rollout. We are in the midst of working with the FDA to launch an additional product in the AUGMENT family, which is an injectable form of AUGMENT. We are on a PMA supplement track with a -- on a panel track. It doesn't mean necessarily that there will be a panel, but that's the track that we are on in terms of the AUGMENT injectable.

Just to refresh your memory, SIMPLICITI shoulder, it's a stemless or short stem design. It's a bone-sparing product, and it's designed for early intervention for people that have the need, but perhaps are younger and the doctor thinks it's really important to spare as much bone. It's a simple design, simpler to implant than most of the other products.

The market is a little bit behind us here. Competitors will at some point in time get into this market, but I think that we will have additional products in the market by then. And again, it opens up a new opportunity in this category specifically for younger patients.

Our product pipeline in upper is pretty rich. We launched the PERFORM+ glenoid last year and it is a very strong product launch. In the first half of this year, we'll be launching the PERFORM+ Reversed. Again, as I said, the market is moving towards reversed more and more all the time, and we now have an additional product to offer.

BLUEPRINT is a big deal. It is an enabling technology. It will enable the doctor to plan the surgery and what instrumentation is needed, what implants are needed, and will allow for more accurate positioning of the glenoid implant before -- to see that before the surgery.

We also have a terrific material with -- in an implant that's under -- part of an IDE study, called PyroCarbon. It's very smooth. It's resistant to articulating -- it's a wear-resistant articulating surface that has the potential to last much longer as an implant than normal metal implants.

And this is four out of 30. I couldn't go through all of them.

Regarding the lower extremity, we have a full complement of products. We have INBONE, which is used for more difficult cases, deformities, etc. We launched INFINITY about two years ago. INFINITY has transformed the market. These products are designed to give patients -- not only to relieve pain, but to give patients mobility and they do it really, really, really well.

PROPHECY, enabling technology. I talked about BLUEPRINT being an enabling technology. PROPHECY, about 70% of our total ankle cases involve PROPHECY, which is a patient-specific guide that, again, helps plan the surgery for the physician ahead of time.

PROPHECY cases, there was a paper that I saw recently by a well-respected group of surgeons. PROPHECY cases take about 40 minutes less to do than non-PROPHECY cases. This is important. Time is money, as we always say, and doctors and hospitals, emergency rooms, think that this is really important. I think, again, we have a lead here. I don't think any other company I know of has these enabling technologies.

INVISION, the revision option that I've talked about before. So why do I -- why am I so enthusiastic about our product portfolio? We have a full suite of products. We have a continuum of care, and I think other companies that are in this business to some extent or another have a product, maybe, and here we are with a full suite of care. We take this area really seriously.

SALVATION, I just want to go back to that (inaudible). This is a big market. Currently, it's about $90 million. It's a big market. And we are most of that. You take us out of this, this is a pretty small market. You put us in it, it's a substantial market.

But that's the current market. The potential market is about $0.5 billion, and how you get there is that almost about 90% of the cases that are currently fused are candidates that could be treated with total ankles and give the patient mobility. So this is a fast-growing market and has a lot of opportunities in front of us.

The product pipeline -- SALVATION, again, a big market, $60 million to $80 million. We are the only company that's cleared by the FDA with a total system to treat this. It is a very good market. The pricing is very stable in this market. We are the company, I think, that has the lead in that. We spend a lot of time training physicians in this, and this is a last resort option for doctors and patients regarding limb salvage.

AUGMENT, we talked a lot about AUGMENT over the years. Very happy with it. It has a great potential. It got off to a great start in the periods that we reported on in 2016. We've done a great job of getting through the VAC committees and that, as time goes on, we will be reaping even more of the rewards of that process.

Our product pipeline in the lower extremities, again very strong. SALVATION, I talked about. We have line extensions in SALVATION. INVISION in Q3 of this year should give a real boost, I think, to the conversion rate of doctors that don't do a lot of total ankles. The core foot and ankle products of ORTHOLOC will be getting some really aggressive help in terms of new products with ORTHOLOC and AUGMENT; the pipeline on that is the injectable form.

We have injectable in some countries; we have injectable in Australia and in Canada. When we introduced injectable, the injectable form of the product, in Australia, our sales in the same -- jumped about 30%. Now I don't know what's going to happen in the US when we get it, but we think it has an opportunity of really helping.

So we have a -- how do we get to 20% EBITDA? And we're going to sustain our revenue growth. We are going to be a mid-teens growth company. We're very committed to that and have a pretty good line of vision to that. We are going to deliver on our cost synergies of $40 million to $45 million and we're going to be able to leverage existing resources. We are going to have, again, very high gross margins, in the high 70s.

And as we look ahead in 2017 in terms of dyssynergies, I would say that we have about $10 million left of the dyssynergies that come with putting the two sales organizations together. We said $25 million to $30 million. We did in 2016 about $15 million. But we also have an additional $4 million -- I just want to draw your attention to that -- that has to do with the loss of the SALTO business, which was the Tornier Total Ankle in Europe. When the Justice Department insisted that we divest of SALTO, we did the US, and as part of the agreement we had to give Integra the option on the European business, which is about $4 million.

So our cost synergies are well underway. We've attacked this vigorously, but we've got more than we thought we would get. In 2016, at the end of the third quarter when we talked publicly, we said that we thought we would have about $25 million and I think that's a terrific, terrific performance.

Leverage, I get asked a lot about this. If you look at the key drivers, AUGMENT expansion, sales force, medical education, [hubs], etc., that's money spent. We've already done that. That's not -- that's money that we have invested.

If you look at the opportunity, look at -- in terms of where our costs are located, we have about 14% on depreciation and amortization. Again, not an EBITDA measure, but that's where about 14% of our costs go.

We have about 30% in R&D and sales force. This 30% will grow at probably the rate of sales. We intend to maintain about a 7% to 8% R&D spend in the sales force. The way they are commissioned and everything will grow at the rate of sales.

The rest of it, the remaining 56%, will grow significantly less, probably at inflationary kinds of growth, sales management, marketing, medical education, distribution, and G&A. So when we talk about SG&A, S is one thing, G&A is another. G&A we can control and we want to control and that's an inflationary kind of growth. Sales we are going to grow at the rate of revenue growth.

So this is how we see the leverage opportunity, and we already saw it starting to get good leverage in 2016 through the first three quarters.

We also have significant opportunity on the balance sheet. As I said, a target-rich environment. We just attacked the Wright side, the legacy Wright business, in 2016. We knocked off through the first three quarters of the year about 100 days of inventory, which was very significant. We got about $6 million of reduction in capital -- instruments and capital spend and we took 7.5 days. We said we projected for the year about 7.5 days of DSO. This is just the Wright side of the business. We have more opportunity here, significantly more opportunity, and we have a whole lot more opportunity on the legacy Tornier side.

So we are advancing towards our goal. Through three quarters of the year that we announced I think it was in October is that we had a 12% growth rate, and that does not include the dyssynergies. It includes the dyssynergies. So if you take the synergies out of that, we had growth of about 14% for the first three quarters of -- looking at the dyssynergies.

So our mid-teens growth rate, we took out the dyssynergies that we talked about from the beginning were there. We have an adjusted gross margin of over 78%. Again, we said we're going to have high 70% gross margins and I think that we are there.

And we are starting to see the real turnaround and the upswing on EBITDA, and this is the important thing, and we feel very confident about getting to this 20% EBITDA number in the next two, three years.

So, we are -- we think we are very well positioned, positioned to perform. As we said in the beginning, on the first slide, positioned to accelerate. We are in a great trajectory. I don't think -- and all the fundamentals are sound. The new products, the launches, the sales force, the integration, all that has gone well.

So we see ourselves continuing to grow at two times the market. We have multiple growth drivers in new products, as well as expanded sales force. We have -- our momentum is strong and growing and we are on a faster path to profitability with stronger financial profiles, actually, than we thought we would be at this time a year ago.

So thank you all very much and we'll see you at the breakout session. Thank you.