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Wright Medical Group NV (WMGI)

BMO Prescriptions for Success Healthcare Conference

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MANAGEMENT DISCUSSION SECTION

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

All right. I get a thumbs up, wow, and an echo.

Good morning everybody and welcome to the BMO Healthcare Conference for 2018. I am Joanne Wuensch, the Medical Technology Analyst here at BMO Capital Markets. And we're thrilled to start the MedTech track with Wright Medical. We have Lance Berry and Julie Dewey, who are joining us here today. And for everybody who's listening on the webcast, good morning.

Are you enjoying New York?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

Oh, it's great. How to not enjoy New York in December? It's fantastic.

QUESTION AND ANSWER SECTION

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

[indiscernible] (00:00:49). All right. Let's start. Since it is a fireside chat, big picture, the extremities market. There is – walk us through how you see this market is developing, how do you think of the growth rates for the upper and the lower extremities and can we just spend a moment also on competition?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Sure. So the extremities market is a great market, been growing high single digits for a while. We expect that to continue and that's both upper and lower. The great thing about these markets is they're much earlier on in their lifecycle. Two important things about that. One, you can differentiate through innovation and you can win through product differentiation in these markets. But then also both markets still have opportunities for market expansion. And we talk a lot about total ankle. That's only 20% penetrated as far as applicable patients that could get total ankle replacement. But there's other opportunities across the foot and then even some in the shoulder area that we see as just evidence these markets are still very early on in their lifecycle, which is very exciting. And we're very focused on these markets and feel like we have a great opportunity to drive that differentiation and market expansion.

As far as competition is concerned, it's pretty similar to what it's been for the past several years, so you have larger companies, they have products in this space, but they're not real focused on this space. You hear people talk about sports extremities and trauma as a focus. Well, we're way more focused than that. We have our own upper sales force and lower sales force. We have our own upper research and development team and a lower research and development team. So we're considerably more focused on these spaces than [audio gap] (00:02:47-00:03:36) but they know who's bringing innovative technologies to the space and we feel like our differentiation from a product standpoint really drives that kind of leadership from a customer standpoint.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

One of the things that struck me is at Stryker's Analyst Meeting this year, they had an entire segment which was dedicated to extremities. Last evening, we had dinner with the management of Zimmer that was talking about – Zimmer Biomet that was talking about extremities. I mean, I feel like in the orthopedics space, extremities generally is getting a little bit more airtime.

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Well, I mean it's by far the fastest growing part of the market. So, I'm sure people are going to spend more and more time on it. That's been the case for several years. People have been talking about it. But we feel like again, our focus is kind of unmatched in these areas and feel good about our spots.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

[ph] So I think some of it (00:04:25) also maybe even moved from sort of the stabilization of a foot and ankle procedure to one in which you're allowing for more mobility given the types of procedures that are being done. I

mean is it just that the technology is also evolving to a stage that allows better surgeries and that might be driving it a little bit too?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Well, I mean I think there's definitely an evolution in these procedures and that's back to the market expansion, right. So, Cartiva is a great example. So this is – a large part of what Cartiva is doing are Synthetic Cartilage product for great toe that we just acquired. And that's cannibalizing our procedure cheilectomies, where really no company was earning any revenue off of that. It was just an instrumented procedure that surgeons would do and obviously, it didn't have really great outcomes to the patient. But it was all they had. So, that's a great example [ph] how you retain (00:05:25) motion. It's a hopefully permanent solution for the patient, but big market expansion opportunity.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

So, let's think a little bit, now that you've mentioned Cartiva, lower extremities. When I start to think about it, you have a relatively new sales force that's really come together there. You have Cartiva, you have PROstep, you have AUGMENT inject and I'm sure there's one or two other things in that bucket that I'm missing. Talk about how you think about the sales cycle of all of these different pieces and then you have one sales force selling them all or how do you think about giving your sales guys marching orders now that they have several things to talk about?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Sure. So, I mean it is in general one sales force selling the whole bag and the sales force has really come along over the past year. We really think about it in three pieces. You have the new reps that we hired, we had some reps that we promoted to be quota-carrying reps and then we had the existing quota-carrying reps. And at this point, we're really seeing good growth out of all three of those parts of the sales force, which is what we expected when we did the expansion; it just took a little longer for us to get there. So, it's good to see all three performing well.

From a product standpoint, if you think about it, we've had total ankle [ph] with PROPHECY (00:06:48) very differentiated, big market expansion opportunity. That's a high clinical intensity hospital inpatient type of surgery. SALVATION for Charcot foot, same thing, high, complex procedure in hospital inpatient and really Augment injectable is for hindfoot and ankle fusion; that's really going to be a complicated inpatient procedure as well. So we've got a lot of things to drive in that part of the market. Really, the one area where we haven't had across our whole business product differentiation is more in that forefoot/midfoot space that's done in a hospital outpatient or an Ambulatory Surgery Center setting.

I think that's what's really exciting about PROstep and Cartiva. So, Cartiva is for great toe osteoarthritis, PROstep is you can address bunions, these are two of the most common conditions, the foot and ankle specialists see pretty much all of them every week. And now we have some truly differentiated products for those conditions and in this different setting. So [ph] I think it's going to (00:07:56) be very helpful for our sales force to have at a minimum a great door opener into that setting of care, into that physician practice, for that part of that physician's practice, and then hopefully be able to pull through other products as well. So it's very exciting.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

And on every call, we always ask about the ASC. And it's a little bit nebulous of we're moving to the ASC. What does that mean?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Well, I think you just see there's a trend and this has been going on for several years where these are – these surgeons, a lot of them have ownership positions in the Ambulatory Surgery Center. They like operating there better. It's just a better environment for them. They have more control over everything basically in the Ambulatory Surgery Center than they do in the hospital. So they would prefer to do their procedures there. They can't do them all there. So the less clinically intense, the shorter OR times, healthier patients; [ph] this is what's (00:08:56) move into the Ambulatory Surgery Center and that's been going on for a while, and we think it's going to continue. So if you segment the market by setting of care, we think the ASC portion is probably going to be the fastest growing part of the foot and ankle market. It's a smaller piece right now, but it's going to be growing very quickly. So it's important for us to be able to compete well there. Just think about all the differentiated products we've been talking about for the hospital inpatient setting; it's just a different sales process. Okay. You pretty much [ph] is (00:09:31) 100% selling to the surgeon on product differentiation, the Ambulatory Surgery Center decision making is a little more complicated. They're looking for – I mean, they always say price, but what they're really looking for is how do we keep our OR full all the time, right, and how do we have the patient volume that we need so that we're keeping this – the surgery center working at optimal capacity. How do we attract the type of the healthy, honestly, private pay patients to this facility that they're looking for? So, it's a little more – it's a little different decision making process.

So, again, Cartiva and PROstep are pretty exciting, these are types of things that surgery centers can market their businesses around and can attract patients with those products to drive the type of patient amount and type of patient volumes they want. So, that's one of the things over the past year we've been working really hard to think about how do we sell better to the customer of the surgery center as opposed to just the customer or the surgeon? And you have to be able to effectively sell to both and that's not traditionally what our company's done. So, we made a lot of progress this past year, we still have a lot of ways to go, but we think we'll be able to compete very effectively there in the future and these differentiated products are really going to help.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

What percentage of the procedures are done in the ASC now do you think?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

That's a hard – it's a pretty high percentage of the procedures, but it's the lower ASP procedure.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

Okay.

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

And not necessarily because the ASC just paid less because the procedures themselves are lower ASP procedures.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Okay, so that would be the PROstep and the...

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

That's right.

A

[indiscernible] (00:11:17)

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

Yes, bunions, hammertoes, great toe osteoarthritis, those types of things.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Okay. AUGMENT inject, [ph] you 8-K'd that (00:11:25) there was a milestone payment, which was made.

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

Correct.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

So that's moving along nicely.

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

Yes.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Let's talk a little bit about at this stage of the rollout, you're I think two quarters into it. How do you think about opening new accounts versus cannibalizing your previous AUGMENT product?

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

So a lot of them in the beginning is cannibalization, but also even within the existing customer base, what we expected and what we're seeing is an increase in utilization with existing customers.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

Okay.

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

So the original formulation of AUGMENT, it's a great product. Honestly, the handling characteristics were a little cumbersome and in particular for tight spaces, it was very difficult to introduce the product into those smaller spaces. And you really almost couldn't – if you're doing arthroscopic fusion, you really couldn't use AUGMENT at all, whereas injectable kind of goes from maybe below-average handling characteristics with the original to really superior handling characteristics to pretty much anything on the market with injectables. So a surgeon can get that in pretty much any space they want to get it into. It's very easy to introduce, very easy in the OR, to get it ready to go.

And so we expect and we have seen increased utilization from existing surgeons that like the product, but really just couldn't use it on [ph] all our (00:12:51) cases. So that's step one. Step two is going back to these surgeons that really we were unable to get adoption with the original AUGMENT, show them the improved handling characteristics, really all the surgeons that have used it love the results of the original AUGMENT. So we've got a lot of good peer-to-peer feedback on that and how can we leverage that into new account. So I think you'll probably see more of that moving into 2019. 2018 reps are going to – they're going to go to the quickest, easiest, incremental revenue and that's really at this point driving more procedures with existing customers.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

And does it help you – when you get into the new accounts, pull other products through, is this your – is there a halo effect that we should be expecting next year?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Sure. I mean, any time you can get into an account that you're not in is a great opportunity, right. So, it helps the rep build relationships, build some credibility. We have great products, right. So what our reps need is just an opportunity to showcase really themselves and then also our bag. So, total ankle is fantastic for that. But honestly, not every foot and ankle surgeon is doing total ankle surgery. You have a lot bigger population that would use augmented injectable and in a much, much larger population that would use Cartiva and PROstep. So I think all those things are going to allow our reps to go effectively call on accounts where they really don't have business today. They're going to have multiple opportunities to get the meeting in 2019.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

Lower extremity sales force was rebuilt about 18 months ago. How stable is that at this stage?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

I'd say it's real stable right now. It's in a good place. Turnover is good. Lots of interest from reps inbound because of the product portfolio. I'd say we saw an uptick on that after the Cartiva announcement, which I think is a strong sign of how powerful products that that can be. So I think the sales force is in a good spot and really can continue to grow and expand from here.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

How do we think about integrating Cartiva? I mean, integration is always a tough one.

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Yeah. You have to be really focused on it and we are – we do have a fair amount of experience in this. On the scale of high or low difficulty, I would put Cartiva on the lower end. It's – outside of sales force, it's a fairly small company with not a lot of integration that needs to occur. Lots of really strong people at that company that we're hopeful to retain, keep that small location that they have and allow them to keep doing what they're doing. From a sales force standpoint, you kind of had the – kind of basic concentration in this. About half of the distributors had the vast majority of the revenue, less than 20% came from the other half.

So basic plan there is the half the distributors that didn't have much revenue, we've notified them that we won't be renewing their contracts. Their contracts run through the end of the year. And our sales force will immediately, January 1, have all of that geographic territory.

With the other distributors, what we've actually told them is, hey, there's a spot for you going forward. We want to keep you and we want to keep you for these accounts that you have right now, but we are going to narrow your territory because there's – you have a large geography and you're only really effectively selling into part of it. So we're going to take part of that away from you and we'll have our reps in that territory.

So those are all – those negotiations are ongoing right now, seem to be going really well. I think the distributors are happy to just have access to the product, which they assumed had announcement they wouldn't have. And I think that that's another interesting sign of how powerful the product is, is how happy these distributors are to have it.

So if you – really January 1 is where we're going to be in really kicking off with the expanded sales force. So getting our reps up to speed now and [ph] then of (00:17:12) January 1, they'll be able to pick up the territories where we didn't renew the contracts of the existing distributors, but then also in the territory that we freed up from the negotiations with the distributors that we are going to retain. So on January 1, we're going to have a significantly larger number of feet on the street that's selling the product and expect that will yield results pretty quickly.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

Excellent. What are you missing in your bag in your foot and ankle?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

We're not really missing anything and we have by far the broadest bag. So nothing that we say, oh, we need to go fill in this area here. It's really more – we're always looking for the next differentiated thing that we can bring to market or if someone else brings up in differentiated, Cartiva is a great example, we're going to be interested in trying to put that in our bag. So it's really more about how can we drive differentiation, market expansion opportunities, looking out for those kinds of things as opposed to gaps in the portfolio.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

We didn't talk about, I want to call it BLUEFOOT, but that's not it...

Q

Julie D. (Tracy) Dewey

Chief Communications Officer & Senior Vice President, Wright Medical Group NV

BLUEPRINT, yeah. BLUEFOOT...

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

This time last year, you bought IMASCAP.

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

Yes.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

And that brought BLUEPRINT into your family, so to speak. Walk us through what is the importance of that technology.

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

Well, I guess, first of all, we think over time that software can be a bigger differentiator than hardware, right. So if you look at a lot of the orthopedic procedures, over time the implants themselves become less differentiators. Not today. Today, the implants still are differentiators; over time that tends to be less of a competitive advantage. We think software can be a continued, sustained, competitive advantage and so that's why it's so important.

A

If you look over the past year, right now, we're in a great spot. We do have differentiated hardware; SIMPLICITI is differentiated, PERFORM Reversed is differentiated, but it's really when you pair that with the software that in the past 12 months, has been very powerful for us to convert competitive surgeons. And BLUEPRINT in particular, for the surgeon specialist community has been very powerful as a customer conversion engine and we think that's just going to continue to be the case going forward. So [indiscernible] (00:19:56) pipeline, we're thinking pipeline just as much or more in the software area as we are in the hardware area. And over the next few years, you're hopefully going to see continued enhancements to BLUEPRINT and expansion hopefully into other parts of our business and software being a bigger and bigger part of what we're doing.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Do you have a software you need, or are you going to buy [ph] red print and green print (00:20:24)...

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

We're focused on internal development at the moment.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Internal development, I like that. Okay.

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

I would say we seem to be out ahead, not chasing from behind. And so, we're really focused on internal development to try and expand that lead and keep pushing that forward.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

How do you charge for this?

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

Actually, we don't charge for it. Right now, again, it's a big differentiator. We're more interested in driving to be number one in shoulders than we are in charging a small fee for the use of BLUEPRINT. I think over time, as we – some of the things that are in our pipeline, some of the vision of what we could bring, there may be opportunities perhaps to charge for some of those; they'll have incremental value they're bringing to the customer that we could be able to monetize at some point. But right now, we're just looking for, one, we want to drive adoption of BLUEPRINT. We want as many of our customers as possible to be using it. And then we're trying to take share. We want to be number one in shoulder.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Can you quantify what percentage of your customers are using it?

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

Sure. So as on the Q3 call, we said roughly 30% of our U.S. customers and also about 30% of our U.S. cases were download BLUEPRINT, which is pretty significant in a very short period of time. [ph] We removed (00:21:49) some big barriers to adoption; it was pretty cumbersome before, say, really this summer as far as getting the scans from the scan center and getting those uploaded. It was a physical – you got to get physical beds, which is pretty antiquated. And so, we've moved it all into the – and then you had to get the software actually on the physician's physical computer. So we've now moved everything up into the cloud and the scans can be uploaded directly. So a lot – it's kind of easier front-end for the surgeon and we expect that will help a lot and hopefully see an inflection point with adoption; that was only this summer really that we've rolled that out. So hopefully, we're going to see that and we would love to have everybody using BLUEPRINT even with not charging for it. I think there's huge advantages for us.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

And you want to be number one in upper extremities. What does it take to be number one?

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

I think we've got to keep doing what we're doing. So we have this – we're the only company to have the shoulder sales force essentially. We say upper extremities, but the vast majority of our upper extremity revenue is shoulders. So, we have extreme expertise from a sales force standpoint. We have differentiated hardware and software right now. So I think two things there is one, we got to continue to – a term the team uses – play as if we're behind, not ahead. And we got to keep driving this customer conversion and we think we can get to number one pretty soon, which I think would be great, being number one in foot and ankle and shoulder.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

Do you have an estimate of your market share in foot and ankle and shoulder?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Current estimate – both of them probably in the low 20s.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

Both in the low 20s.

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Yeah. Both in the low 20s.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

And how far do you have to move to get to number one in upper extremities?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Kind of depends on who's winning and who's losing. So...

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

[ph] So again throwing that question to you (00:23:52).

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

...so we're realistically, we're going to have to get probably towards the higher 20s...

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

Okay.

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

...to get to number one.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Okay. So you have SIMPLICITI, you have...

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

PERFORM Reversed.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

...PERFORM Reversed, thank you.

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

And BLUEPRINT.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

And BLUEPRINT. You need something else?

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

I don't think we need anything else, but we are going to – we're going to bring some things to market anyway.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Okay. What are you going to bring to market?

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

And I think one thing that you'll see coming in, in the first half of the year is the revision shoulder and I think this is an interesting back to the market. This is, we view, a market expansion opportunity. So right now, there are obviously shoulder revisions that are done, but there are no true really like ground-up revision systems. So ours will be the first, including some pretty clever instruments to help with extraction of the existing implants. So we think that will be a big advantage for us. We think we're really positioned well for the revision market because we tend to do better with the shoulder specialist as opposed to the general [ph] orthoped (00:24:54) just doing shoulders and they're much more likely to be doing the revisions. The reason [indiscernible] (00:24:58) market expansion is really if you go back and look at the growth in primary shoulders 10, 12, 15 years ago, we expect as these things just kind of reach the end of their useful implantable life that we're going to see a bolus of revision. So we already think that's maybe a [ph] \$70 million-ish (00:25:19) U.S. market probably going maybe double what

A

the primary market is growing and expecting we'll see strong growth over the next couple years in that market. So, again, just an example of how the market really isn't mature and there's still opportunity there for it to expand.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

Excellent. Let's talk a little bit about, what did I not talk about, what do you want to talk about?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

I mean, you're hitting all the good things. I know you got a couple more questions...

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

Of course, I always do, but sometimes when I talk with management teams and in our conversations when we talk after a quarter like, what do you want to make sure I didn't miss, and so I'm going to ask you like sort of midstream here.

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Okay.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

What do you want to make sure that investors don't miss?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

I think we talk about it a lot. So hopefully, they already know...

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

So they should about all go home.

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

But – to reinforce, we think we're in a really good spot to continue to take market share in the extremities market and we think the extremities markets are great. So again, we're more focused on these markets than anyone else, including focus sales forces on upper and lower, which really no one else has. That focus is really is what has enabled us to have these differentiated products. And we really now have truly differentiated products in every part of our business, upper, hospital inpatient lower, hospital outpatient lower, biologics, so we're equipping that focused sales force with some really great products and then also enabling technologies. It's not just the hardware, but it's the enabling technologies to allow us to bring a solution to the customer. We feel like we're ahead in that too. We're the only company that has preoperative planning for ankles and BLUEPRINT is just kind of a unique planning software for upper. So you put all that together and we think that we really have a great advantage in what's a great market, that's what I would hope people would take away from Wright.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

A great advantage and a great market.

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

Yes.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

All right, we knew that.

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

Okay.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Okay, good. Robotics, we just published our 2019 outlook and there's an entire section on robotics and we go through general surgery and hip and knee. What about shoulder?

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

I think the safe assumption is that someday, there will be robotic applications for shoulder. Our view right now is it's probably pretty far out. There's bigger priorities for the larger companies that are focused on robotics or even some of the smaller companies that are focused on robotics. There's much larger markets for them to focus on and that's where the time and attention is. We think there's a better approach to intraoperative guidance. Intraoperative guidance, the concept is great. Having a plan and taking that plan into the OR and giving the surgeon every advantage that they can get to execute what was planned, that's a great concept. And better [ph] outcomes (00:28:31) is a concept that we talk about from R&D standpoint and software from a planning standpoint and then things to bring intraoperative guidance we think are the future. We're looking at days more like mixed reality.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

What is mixed reality?

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

So it's – you can bring goggles into the OR and you can see reality, what's there in the OR, but then also you can project images on for that reality, things that could provide intraoperative guidance through that method as opposed to robotics. It will be an alternative to robotics, probably a lower cost alternative to robotics and our efforts are more in that area. And robots aren't going away where I think for the shoulder, they're probably pretty far out and we might be able to bring something sooner that is another approach.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

So you're working on mixed reality?

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

We are working on mixed reality. That's a further-out pipeline...

A

[indiscernible] (00:29:36)

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

I won't put it in my model. Don't worry about it, but let's talk about it.

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

But I think the concept of intraoperative guidance, of bringing the plan to the OR, that's a concept that we think is a good concept and we're working on ways to do that. Right now, you can just get a physical guide, that's a way to bring the plan to the ORs. Over 70% of our total ankles are done that way. And it's been a huge benefit for our customers and for adoption of total ankle. So I mean that seems pretty, pretty simple, but that can be very powerful. But then using technology to perhaps have a virtual guide as opposed to a physical guide is something that you may see down the road.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

A lot of companies have relationships, partnerships, programs that they talk about. We get a press release occasionally. You guys don't talk about any of that kind of stuff. Should we assume this just isn't happening or is there something that you can discuss?

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

I would say right now, our efforts are focused internally.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Okay.

Q

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

Not through partnerships. I think you do have to be open to the concept of partnerships just in general. But right now, we're on a path of internal development.

A

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

Okay. We updated our model recently. And with it, we – I was going through your guidance for adjusted EBITDA in the fourth quarter of 2019. Walk me through how do we get from what you just delivered to the fourth quarter of 2019?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

So really, we've had some really solid EBITDA margin expansion for the past several years. And so it's really the same game plan as what we've had. So got great gross margins, so really strong, not really looking for those to expand per se, but just to stay high. [indiscernible] (00:31:24) great opportunities to leverage SG&A and specifically kind of what we talk about as we feel like our differentiator allows us to take share is really these focused sales forces and these differentiated products and technologies. So, we're not looking to drive any leverage there. So R&D, feet on the street, we expect to continue to reinvest generally in line with the rate of sales. If we start looking at the rest of sales and marketing, medical education, sales management, pure marketing, those are things that we can grow, but at a rate lower than the rate of sales and drive some leverage. And then we have pretty significant cost in distribution, the nature of our business, there's a lot of moving stuff around. So there's a lot of cost there and we have pretty high G&A coming out of all the pretty significant changes to the business through – we sold off half the business, we merged with a similar-sized business.

Our G&A is higher than we would like. But those things are highly leverageable [ph] and (00:32:27) really looking to keep those as flat as we possibly can while we're trying to grow revenue in the double digits. So, that's what we've been doing the past couple years. We think we continue to have opportunity for 2019 and beyond with that same game plan and then Cartiva helps as well. So Cartiva, we said at announcement, it can add about a point to our EBITDA margin expansion in 2019 on a pro forma basis. It's going to be pretty much the most profitable product in our company or is now; so now the transaction is closed. So that can help as well. So, that's [ph] just on (00:33:04) extra on top to help us drive that EBITDA margin expansion.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

And you're cash flow positive?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Yeah.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

That's sort of important.

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

It is. I would say...

[indiscernible] (00:33:16)

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

...immediately cash flow positive, excluding discontinued operations in 2018. But I expect that to make some significant improvement in 2019 and even more in 2020. So, we feel like we're really turning the corner on cash and that should be a lot better going forward.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

One of the pushbacks sometimes I get is on your balance sheet and your debt burden. Can you walk through how you think about that?

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

A

Yes. So I mean obviously, it'd be great if we had less debt on the balance sheet and we're growing EBITDA significantly, so that helps with your leverage ratio. If our strategy was, we had to go out and go buy three companies a year, our balance sheet would be pretty problematic. But that's not our game plan. We can hit our growth rates double-digit growth through organic means and we're really only looking at M&A, if it's something differentiating in our space that we think it's important we own, so Cartiva is a great example of that, right, highly differentiated, right in our call point, we wanted to own that. We're willing to use our stock to do that. And actually our stock reacted favorably when we used stock to buy that differentiated product. And so we feel good about our ability to do that going forward. So with that as context, we think the balance sheet's fine and our debt ratio is going to make massive improvement over the next couple years as we improve our EBITDA margin. And I think in a short period of time, we'll be looking at the balance sheet in a pretty different way.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Q

Sounds good. Does anyone from the room have a question? Stand up and shout it out. Excellent. Well, we are almost out of time. And so, Lance and Julie, I want to thank you so much. Enjoy the day and enjoy New York City.

Lance A. Berry

Chief Financial Officer & Senior Vice President, Wright Medical Group NV

All right. Thanks, Joanne. Glad to be here.

Julie D. (Tracy) Dewey

Chief Communications Officer & Senior Vice President, Wright Medical Group NV

Thank you.

Joanne Karen Wuensch

Analyst, BMO Capital Markets (United States)

Okay. Thank you.

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