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# EDITED TRANSCRIPT

Q2 2018 Merit Medical Systems Inc Earnings Call

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## PRESENTATION

### Operator

Good day, ladies and gentlemen, and welcome to the Merit Medical Systems 2018 Q2 earnings call. (Operator Instructions) And as a reminder, this conference call is being recorded. I would now like to introduce your host for today's conference, Mr. Fred Lampropoulos. Sir, you may begin.

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### Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President

Good afternoon, ladies and gentlemen. This is Fred Lampropoulos, broadcasting from Salt Lake City. Thank you for taking the time today. We're excited to report our results to you. But before we do that, Brian Lloyd, our Chief Legal Officer, will read our safe harbor provision. Brian?

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### Brian G. Lloyd Merit Medical Systems, Inc. - Chief Legal Officer & Corporate Secretary

Thank you, Fred. During our discussion today, reference may be made to projections, anticipated events or other information, which is not purely historical. Please be aware that statements made in this call, which are not purely historical, may be considered forward-looking statements.

We caution you that all forward-looking statements involve risks, unanticipated events and uncertainties that could cause our actual results to differ materially from those anticipated in such statements. Many of these risks are discussed in our annual report on Form 10-K and other reports and filings with the Securities and Exchange Commission available on our website.

Any forward-looking statements made in this call are made only as of today's date. And except as required by law or regulation, we do not assume any obligation to update any such statements, whether as a result of new information, future events or otherwise. Please refer to the section of our presentation entitled Disclosure Regarding Forward-looking Statements for important information regarding such statements.

Our financial statements are prepared in accordance with accounting principles, which are generally accepted in The United States. However, we believe certain non-GAAP financial measures provide investors with useful information regarding the underlying business trends and performance of our ongoing operations and can be useful for period-over-period comparisons of such operations. The tables included in our release and discussed on this call set forth supplemental financial data and corresponding reconciliations to GAAP financial statements.

Please refer to the sections of our presentation entitled Non-GAAP Financial Measures and Notes To Non-GAAP Financial Measures for important information regarding non-GAAP financial measures discussed on this call.

Readers should consider non-GAAP measures in addition to, not as a substitute for, financial reporting measures prepared in accordance



with GAAP. These non-GAAP financial measures include -- exclude some items that affect net income.

Finally, these calculations may not be comparable with similarly titled measures of other companies.

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Thanks, Brian. And again, welcome everybody. We're assembled here with our staff, and we again, appreciate during earnings season, your attendance and interest in the company.

The first thing I'd like to do is introduce Raul Parra. Raul has worked for Merit for approximately 9 years and in that role, he has been the Corporate Controller and the Vice President of Accounting. The statements you have been seeing for many years have been prepared by Raul. Prior to his employment with Merit, he was an auditor for Deloitte & Touche. So he knows the business, he knows it well and, Raul, this is your first call. We've had the opportunity to go out and meet with some shareholders and investors out in the field, and I think in Denver and Kansas City, but this is your first one. So introduce yourself, and we'll get on with it.

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**Raul Parra Merit Medical Systems, Inc. - CFO**

Yes. I'm excited to be here. Thank you for the opportunity.

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Okay, great. Well, by the way, I think Raul has done a really good job. He stepped in. We haven't missed a beat. I'm getting the information I need as well as our board, and so again, Raul, thank you very much, and we appreciate it.

So let's talk about this press release now for a moment. And there's a lot of details to talk about and a lot of interesting things going on with the company. But as you can see, we beat the consensus number for revenues by about \$10 million. We also did that in the first quarter. And so I think it would be -- it's fair to say that the business is robust, it's coming globally, but I think the thing to do now is, Raul, I'm going to ask you to weigh in here early and maybe talk about where the revenues are coming from and then maybe go through the numbers for the listeners on the call. So, Raul, here you go.

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**Raul Parra Merit Medical Systems, Inc. - CFO**

Sure. So Q2 2018 revenue was approximately \$225 million as reported, a 20.5% increase over the comparable period of 2017. Organic growth was 11.7% or 9.8% on a constant currency basis. Some highlights include: world-wide dealers up 22.5%, EMEA up 10.5% and OEM up 11.5% on an organic constant currency basis.

Moving on to the margin for Q2. Non-GAAP margin was 48.9% compared to 48.3% for the comparable period, a 60 basis improvement over the comparable period of 2017 and a 140 basis improvement from Q1 2018. I'd like to point out that this was the first sequential improvement in margins since Q4 of 2016.

The improvements came from improved production variances, obsolescence and product mix, and we expect to see continued sequential improvement in the margin for the back half of the year and are committed to keeping the focus on growing our margins.

Q2 2018 total operating expenses as a percentage of revenue were approximately 35%, in line with our expectations. And on the EPS side, our Q2 non-GAAP EPS was \$0.43 compared to \$0.36 for the comparable period of 2017.

Better-than-expected top line revenue, improved margins and cost discipline continued to help our EPS growth.

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Well, thank you. Listen, just again, to reiterate, the core growth, I think we guided 7.5% to 8.5% and we came in at 9.8%. I'm going to give you some color on that. We've received a number of orders that have come from the Middle East from distributors for our legacy products. They are not as profitable and have lower margins than some of the product, but there's a lot of demand for Merit products globally, and we expect to continue to see that demand as we go forward.



I think the 140 basis point improvement on gross margins from the first quarter is significant, and I want to make sure that you understood what Raul said when he said that we expect to continue to have sequential growth in gross margins through the balance of this year. Now we'll explain a little bit further in a moment about why we're kind of lowering a little bit but again, I think that you would agree, I hope that you would agree, that there really aren't any multiples put on gross margins. It's one of the factors to show that you can bring more to the bottom line. But I think the \$10 million first quarter, \$10 million the second quarter and the fact that I believe the consensus number on earnings was \$0.40. So we beat the top, we beat the bottom, we've had nice improvement in the gross margins. But as we look forward, there is a bunch of opportunities and other issues on business we think it's important and will have a long-term effect on the business positively that we need to be involved in. So we'll come back to that in just a moment.

So I think overall, the financial performance in my view is satisfactory. In fact, I think as I mentioned, we beat top and bottom line numbers.

So let's go on, if we could for a minute, and talk about some other recent developments. These are not what I'll call material issues, but a few little things that will be of interest to you. You're all familiar, of course, with the NinePoint agreement, and we're already starting to see the benefits of NinePoint Medical and that OCT technology along with our sales force. And you will see for the quarter and for the year, that our revenues now have made a very, very nice move in terms of the growth in the business, and we expect to continue to see this. They are playing off each other very, very, very well. And we've closed some recent accounts at Mass General, the VA in Houston and other accounts where we're getting the benefit of this technology along with Merit's existing products. Merit recently purchased the assets or the distribution rights from a company called Direct Access. And these assets or these products, which are approved in the marketplace are for the high-pressure PTA balloons that are used specifically when you're doing work with fistulas, where you have blockages and you need to open up the areas around the anastomosis. It's a business of about \$2.5 million or \$3 million. They really had a very, very small sales force, a couple of people and working through distributors. And that will now go into our entire peripheral sales force, along with a number of other complementary products that go along with it, so we're excited about that. And then we became the exclusive worldwide distributor for the Q50 PLUS Stent Graft Balloon. And this is a product that we buy from QX Medical. It has above-average gross margins, corporate average. It is being sold by a third-party, one of the larger companies who decided to either bring it in-house or have somebody else produce it. They've been selling it to them for 9 years. It's well accepted in the marketplace. I'm not aware that there's a lot of international business, but with our footprint, we think that we can do a nice job and we're already seeing this business play out very nicely. The other business was doing, by our records, about \$6.5 million to \$7 million a year. And again, our goal is to go out and meet the needs of existing customers who can't get that product any longer and who are buying it from us.

So these are things that fit into our long-term strategy and we're very excited about it.

I want to talk for a minute about the legacy products and some further color on tenders. We recently participated in a tender in the Middle East. Last year, that tender was about \$1.5 million of business. This year, we received rights or at least, opportunity for \$6.75 million. Now, that's a significant opportunity. And in these tenders, being present, having your products in place is really significant for the long-term. Again, these are the legacy products, so you might get a little bit lower gross margins, but we think that it's better to do that than have to establish the business through other products like, for instance, the HeRO. Other than that they're high margin, but having a presence there is important. So again, we have modified our gross margins and lowered them simply because we believe having these opportunities are important for the business over the intermediate long-term.

And I think that if you really understand this, and I'm trying to do that, that you will agree that as I mentioned earlier that, that top line and then the ability to maintain those expenses in the middle are very, very important.

So I want to assure everybody of our discipline, that everything is in place, that we're committed to growing the business. I think you all know that, but I think in some ways, it's been -- gross margin's growing and that's all it's been, and I don't think that's the proper way to look at it. At the same time, we are not abandoning our gross margin goals, we just think there's a mix. Now, Raul, I'm going to ask maybe if you want to add just maybe a little color to this, just from an accounting point of view, because there's some cost and expenses in there. Why don't you speak to this?

**Raul Parra Merit Medical Systems, Inc. - CFO**

Yes. I just think the mix has changed and so we need to adjust our margin because of it. And we're also seeing some additional costs like shipping and labor costs that are impacting our margin as we look forward. And we have some opportunities on a customer that you're going to -- or a competitor that you're going to talk about, that will impact that too. So as we look forward, we just want to make sure that we got it properly and then move. We're just -- people understand what's going on.

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

So let me move to that then with those comments, and that is that there has been a disruption in the marketplace. I want to go back a few years to a previous disruption, and I think there was a lot of concern about how much of this you're going to get and then are you going to be able to keep it. It's really interesting to note that, that business grew very nicely and then it kind of topped out. Interestingly enough, instead of going down, it actually continued its growth. I believe last year, it was up 18% or 19% and for the first 6 months of the year this year, the Impress catheters which were part of that recall that you're all aware of, have now grown over 21%. And we expect that to continue and very likely to accelerate as we look at that product line.

So I think in some ways, as someone mentioned though, this is somewhat the straw. And by that, I mean, this particularly competitor, which is a great company but they've stubbed their toe. And the interesting part for Merit is this covers our microcatheters, we have 3 or 4 of them, a new one recently introduced called the Pursue, which you will be hearing more about in the future, along with the SwiftNinja and the Maestro that affects our Sheath business and not just the new IDeal or the Ease, but even the ones that Merit has been selling for a very long time, for over 15 years. There is a huge disruption and we are seeing demand globally.

We're seeing that for our guide wires, our hydrophilic guide wires. Along with those guide wires, we're also seeing uptake for our InQwire guide wires. We have seen these radial sheaths that I've mentioned also pick up the Sync business. So literally, the closure products that Merit introduced some 6 months ago has almost tripled in demand just in the last few weeks. Now in the first quarter -- or excuse me, second quarter, there were only about 2 weeks of this disruption. This quarter, this summer quarter, we'll see that and I think what's appropriate, there is some of this disruption in this improved forecast. But I think we've also been very conservative like we were with Cook. You will recall, we've said that we think it could be good for that and we'll update you. I will tell you that business is robust, all -- a number of factories in Texas, in Ireland, in Salt Lake City are literally working 24 hours a day and working weekends, over time. We are very, very, very busy in our entire business. It's not just this disruption, but it covers a lot of products. So as time goes on, we will keep you briefed. You'll see the results of that in the third quarter report, and it's a significant opportunity for Merit to sell all of our products.

So I think there's enough said about that and, with that being said, listen, a great quarter revenues, earnings and slight adjustment because of mix and some other issues. And now, I'm going to turn some time over. We've talked a little bit about guidance, but I want to get specific about that. And Raul, why don't you go through our guidance and maybe a little color on where we're going?

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**Raul Parra Merit Medical Systems, Inc. - CFO**

Yes, I'll just recap it real quick so everybody has the opportunity hear it. Our revised revenue is between \$870 million to \$880 million, a 20% to 21% increase over the reported revenue of 2017. Gross margin on a GAAP basis will be between 45% and 45.5% and gross margin on a non-GAAP basis will be between 40.9% and 49.4%, an 80 to 130 basis point improvement over 2017.

On the earnings side, EPS GAAP will range between \$0.80 to \$0.90 for 2018. On a non-GAAP basis, the range will be between \$1.60 and \$1.70. For our tax rate, we are still forecasting our rate to be between 25% to 27% for the back half of '18.

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Well, listen, I think by any measure, the business is growing extraordinarily. I mean, it's doing well, it's robust, we're busy. It's a summer quarter. Generally in the summer, we guide down. I think most of the consensus is guiding down and we're going to leave it there. But depending on how all this other stuff works out, it will be interesting to look at this third quarter report. Well, listen, I think we've covered it, revenues, opportunities. Yes, haven't talked about new product pipeline, but it's full and new products coming out. Our distribution globally is a huge advantage. I know everybody gets all riled up about tariffs and this and that and we've chosen to ignore all of this. Our customers want our products, we have the capability to produce them, it's all hands on deck, and we'll look forward -- first of all, of

answering your questions on this quarter, and we look forward in the subsequent quarters of reporting the numbers to you.

Again, thank you for your time, and I think what we'll do now is turn the time back over to our administrator, and we'll take your calls as well as Raul and I will be here for a couple of hours after to make clarifications, not to add any new information, but to make clarifications on the data that's in our press release. So that said, let's turn it back over the administrator.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Our first question comes from the line of Jim Sidoti with Sidoti & Company.

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### James Philip Sidoti *Sidoti & Company, LLC - Research Analyst*

Just to start right out with the issue brought up towards the end about some production issues at one of your competitors. If I look at Slide 14 of your deck, it looks like those affecting the microcatheters, the catheters and the compression devices. So just couple of questions. First, can you confirm, was that Terumo, that competitor?

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### Fred P. Lampropoulos *Merit Medical Systems, Inc. - Chairman, CEO & President*

The answer is yes.

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### James Philip Sidoti *Sidoti & Company, LLC - Research Analyst*

Okay. And do you have any sense on how much business they're doing with those products?

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### Fred P. Lampropoulos *Merit Medical Systems, Inc. - Chairman, CEO & President*

Yes, Jim, listen, this reminds me a lot of the Cook situation. However, in this situation, if you look at both Slides 13 and 14, you will see that this covers a number of Merit products, from guide wires to sheaths to microcatheters, closure devices, and so on and so forth. So they made an announcement, they talked to -- sent a letter out to their customers. They -- in that letter, they actually referred them to Merit -- or customers to Merit. They've talked about being back on the market in a press release, publicly stated in August. But what we're seeing -- I'm just telling you at the -- you asked the question, I'll tell you that our best guesstimate, and this is just a guesstimate, there is about \$0.5 billion worth of market opportunity out there. Merit is currently doing about \$50 million in these products, and I would just simply say that there's a lot of opportunity. I will tell you from what I'm seeing and what's on the order desk and the activities globally, and I think that goes back to one of the issues on margins and the things that we wanted to be cautious about. We have to fill a global pipeline here. So we're seeing it in Europe, we're seeing it in Australia, we see it in Canada, we're seeing it in Brazil, everywhere. And so, we have to fill those. Like any of these situations, it's my belief that what this really helps to create is an opportunity where ideas in the past of having a single source, I think, are really old ideas. Hospitals have to make sure they can treat patients and have to be able to deliver those products. To my belief, Merit -- a number of people who have bits and pieces of these products, but Merit has the broadest product line in my estimation for the ability to fill these needs globally. So we essentially have everything that's on that list of products to fill, whether it be -- and some of these by the way, are the Impress catheters but it really goes to the hydrophilic catheters, closure devices, microcatheters and the big ones, the sheaths and guide wires. So it's the biggest opportunity that very candidly, I've ever seen in the 37 years I have been in this business. And I think once that window is open, it will help us across the board globally. So we are -- I think I use the term -- I have a guy sitting in the room from the Navy. And when I said all hands on deck, he got all fired up and was giving me thumbs up. But we have another way to say it the Army, but we'll stay with Navy terms. All hands are on deck and we're very, very busy out here, Jim.

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### James Philip Sidoti *Sidoti & Company, LLC - Research Analyst*

So if you look, you beat the quarter by about \$10 million in revenue. You raised your guidance by about \$30 million. So should I assume that delta, the bulk of that is related to this production issue?

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### Fred P. Lampropoulos *Merit Medical Systems, Inc. - Chairman, CEO & President*

Yes. Actually, I think I'm looking at the numbers here, but I think the guidance number, and Raul is confirming this. I don't think it's \$30 million for the balance of the year, it's less than that, Jim. But let me go to say that it's a summer quarter and summer quarters, as you

know, can be interesting. But with the momentum we're seeing, there is part of that that's in that number. And so Raul, before I go to that, what is the...

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**Raul Parra *Merit Medical Systems, Inc. - CFO***

We've been comparing it to prior year, I believe is what he said.

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**Fred P. Lampropoulos *Merit Medical Systems, Inc. - Chairman, CEO & President***

Oh, you're looking at prior year, okay. Yes, we're just talking that's why I think in the balance for the year, we put about another \$16 million or so in our forecast. So then, I think you're asking if we did 10-10 and then to the last half of the year, you say you're going to do a thing, does that lay (inaudible) any upside? And the answer is, if this continues to play the way it has played now for 1.5 months, then I suppose that's where the upside opportunity is. But again, it's our forecast, it's one of the new, but I think that there is upside even to that. But again, it's always hard for me to raise things into a summer quarter, just because it's so unpredictable. This one though, is a little bit different from anyone we've ever seen. So I don't know how else to answer to your, Jim, other than to say that there is not a whole lot in the second half of the year that's really attributable. There is some but not a whole lot, but I think that's where the upside will come, if it materializes. (inaudible) as well.

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**James Philip Sidoti *Sidoti & Company, LLC - Research Analyst***

So you indicated this about a \$500 million market, you're doing about \$50 million in revenue, so you have about 10% of the market. Where do you think that number can grow to?

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**Fred P. Lampropoulos *Merit Medical Systems, Inc. - Chairman, CEO & President***

Boy, that's a tough question. Listen, is there \$25 million to \$50 million worth of opportunity for us on an annual basis looking out a full year? And the answer is yes. Is it more than that, less than that? If I were just looking at it and we've had the benefit of looking at this now for about 1.5 months, it really depends on how quickly they can fill the pipeline. Again, but much like other situations we've seen, they've already extended out a month beyond what they originally said. But I think maybe the more important issue is not what they do. I think that as I mentioned, I think they stubbed their toe and the opportunity will be for us to go and ensure that we have options. We have microcatheters, we have devices, we have the sheaths and fortunately, for us, we have the PreludeEASE and we have the Prelude IDeal. So these are the best-in-class. So we don't just have other products, we have great products to compete here, and I think it's going to make a huge difference. And by the way, these are existing customers but it really opens up the opportunities in a lot of areas for us, Jim. So it's a great opportunity but again, much like the Cook, we're trying to restrain ourselves but we're really busy.

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**James Philip Sidoti *Sidoti & Company, LLC - Research Analyst***

And you think you have capacity to be able to handle it?

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**Fred P. Lampropoulos *Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes, that's another a really -- geez, Jim, come on, give me a break. Listen, we're putting additional capacity in place already. We are already in the order to meet the demand working overtime. But you have to fill the front end of it with raw materials and you have to move these products out. Like I said, in Texas, in Ireland, in Salt Lake City, it's all hands on deck, and we will be able to meet -- now, we have other competitors out there who are also trying to meet the needs. But for some of them might just have a catheter or a wire, but I don't believe there's anybody else out there that has the mix and the breadth of product line that Merit has. So I can say I think, with reasonable confidence, that Merit is going to be the big benefactor here. We simply have the goods and again, if you look at our slide deck on our website, I think it will become very apparent to you about what the opportunity is for Merit products.

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**James Philip Sidoti *Sidoti & Company, LLC - Research Analyst***

All right. Well, it sounds like you got a lot of work to do, Fred, so I'll let you go.

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**Fred P. Lampropoulos *Merit Medical Systems, Inc. - Chairman, CEO & President***

Good to hear your voice. Thank you.

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**Operator**

Your next question comes from the line of Bruce Nudell with SunTrust.



**Bruce M. Nudell SunTrust Robinson Humphrey, Inc., Research Division - MD**

Fred, the guide increases \$20 million to \$30 million on the year and I know some of that occurred this quarter. But of what remains, you threw out some numbers for the distribution agreements, as well as the Middle East tender, as well as the potential for retaining -- garnering and retaining share from Terumo, and some was undoubtedly organic strength. Could you just apportion how much the raise in the guide is to those various factors, organic spread, the supplier woes, the inorganic adds through distribution and the Middle East tender?

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Yes. Let me start with the deals that we talked about. You probably have seen in the last half of the year, \$3 million to \$4 million, that would be my guesstimate for those add-ons. Again, we're already halfway through the year. Some of that business is in place and by the way, this will go in general growth, not organic. So I think that's one thing I want to clarify that, it will be in overall growth and not the organic side. On the distributors and by that I mean, the tenders and things like this, those are all delivered -- scheduled to be delivered during this year. That's just again, incremental business we've had in the past. However, a few years ago, when oil prices were dropping, we had orders like that, and they canceled them and moved them into the following year. Now, I don't anticipate that, that will happen but these things are always interesting to watch and there are factors that come into play from time to time. As I would look at it today based on what I see economically and with oil prices, all of that should be delivered before the end of the year. So I think Bruce, so that's the distributors, that's the other mark, doesn't leave a whole lot more if you take just to look at organic growth and then you take a look at this opportunity. So again and listen, there's no question that our forecast in my view is conservative. But again, remember, we're going into this, into a summer quarter and last year, I think we missed it by a couple of million dollars. So we have not put a lot of this opportunity into the balance of the year. There are some additional costs as I said. You've got some of these are new products, so they're ramping up and they're not at full margin, but all of this business helps us. I mentioned one about the Sync. The Sync is a product that's not part of this recall -- or excuse me, it's not a recall. I'm sorry, I misstated that, but it's a shortage. But the Sync goes with every one of the sheaths that are part of this issue. And that has just -- so we've added additional capacity. Fortunately, we saw a lot of this coming just for general demand for the product. We saw -- so we have planned on the IDeal and the Sync to be big growers this year simply because they're better products than our competitors. And fortunately, equipment and these things were already in place but still has to be brought online. So again, not very much from this and we'll keep you -- we'll keep everybody briefed on this. I mean, I wish we can almost give you a weekly report because it's that dynamic, but we can't, so -- but what I can say is from when it first started, it's accelerating. I don't see it slowing down and the size of the market and the opportunity is substantial for Merit. And that's the best way I can say it, and we'll just have to let it play out and report it, but that's the best I can do.

**Bruce M. Nudell SunTrust Robinson Humphrey, Inc., Research Division - MD**

And Fred, like when you look at the valuation of the company, you guys clearly outperform on the sales metric. On the EBITA metric, it's been a work in progress. And just with valuation in mind, is there any lever that could be pulled next year now that you've laid the groundwork for these tenders and incremental sources of business where you can kind of make up some of the lost margin progression that you volitionally gave up this year and maybe make up -- make it back up so you can get back on the trajectory that you articulated before?

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Yes. And I think it's a really good question, and I appreciate it. Look, we were 140 basis points sequentially and I think Raul pointed out that it was the first time that we've had consecutive quarters we didn't have a fall-off. And it's our commitment to continue to grow gross margin. And I think to be very candid with you, that as these products come on and absorb and we start to see more and more overheads covered, variances, as I think we call them here, those are all going to flow once you pay those bills. So I think that we have to hire people. So I'm just giving you an example, I mean, we hired 32 new people today, we hired 40 new people in Ireland last week, just in those 2 plants just in 1 week to keep up with this demand. So as you look at that sort of stuff, you're going to have these. But would we not do that and not take advantage of the opportunity? The answer is, of course, we wouldn't. So I do believe that with mix, with absorption, with higher margin products and these -- all of these products, because of the volume, particularly in some of the new sheaths and those sorts of things, even the guide wires, will absorb more and our margins will actually improve on these with these volumes. I mean, I think that's the economics that we always look at, is improvements in volume to absorb the overheads. So the answer to your question is, yes, I do believe that we'll see continued gross margin improvement and that's our goal. I mean, we know that that's

what everybody's concerned about. On the other side of the coin, and I pointed this out in my earlier remarks, we can get higher gross margins and not worry about revenues. Is that the right thing for the business? Sure, that's nice for a short period of time. This is a growth business, this is a business that is managed professionally. We'll control those below the line expenses and we will continue to deliver, in my view, above average performance in earnings. So again, tomorrow good morning, everybody is going to be sweating this stuff and that's your job. My business and my job is to do all of these things, grow that top line, and I think we did an extraordinary job to continue to manage lowering of costs and improvements and efficiency and then bring those bottom line numbers, and look to the future to make sure that it's not just last year and this year, but into the future. So I know, again, the past as you've looked at it, this is a long answer but people said oh, well, they can do this but they can't do that. The answer is, we can do all of it and we will continue to do that. That's our commitment, everybody sitting in this room, and they know what we need to do. But you don't have opportunities like this pop up very often and you've also had this and I don't want to -- you've had FX. So looking at the latter half of the year, we're going to get really no benefit as we look at it, to maybe \$2 million down on FX. On the front end of the year, I believe we had almost \$9 million of positive FX, so we tried to account for that. So okay, that helped us, it might be flat or slightly down at other half. We don't know, but that's how we've done it in our forecast. We've got increased expenses in labor, we have a 3.1% unemployment. Listen, you're familiar with all of these. You have the cost, the fuel. All of that being said, we believe that the momentum of the business, the acceptance of Merit products overrides all of this and will give us the returns that we're excited about reporting as we look forward, Bruce.

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**Operator**

And our next question comes from the line of Larry Biegelsen with Wells Fargo.

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**Lawrence H. Biegelsen Wells Fargo Securities, LLC, Research Division - Senior Analyst**

Raul, congratulations on the promotion. On the organic growth guidance of 7.5% to 8.5%. I didn't hear an update on that. Did you raise that, Raul?

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**Raul Parra Merit Medical Systems, Inc. - CFO**

Yes, it's going to be 10% to 11%.

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**Lawrence H. Biegelsen Wells Fargo Securities, LLC, Research Division - Senior Analyst**

So your new guidance is 10% to 11% organic. So that's excluding currency and excluding M&A? Is that correct?

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**Raul Parra Merit Medical Systems, Inc. - CFO**

That's right. Core growth on a constant currency basis.

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

For the year.

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**Raul Parra Merit Medical Systems, Inc. - CFO**

For the year, yes, for the year.

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**Lawrence H. Biegelsen Wells Fargo Securities, LLC, Research Division - Senior Analyst**

That's helpful. So year-to-date, by my math, that was about 8.5%, Raul, and so you're implying a pretty big acceleration in the second half. Is that fair?

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**Raul Parra Merit Medical Systems, Inc. - CFO**

That's fair.

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**Lawrence H. Biegelsen Wells Fargo Securities, LLC, Research Division - Senior Analyst**

Okay. And Fred, I hate to come back to this, but the Terumo contribution in the guidance, I mean, you threw out a number, Fred, of \$16 million, I think, earlier. There were a lot of moving parts here on these new distribution agreements to tenders. Is that the right way to think about how much you're assuming in the second half benefit from Terumo? Or did I mishear? I'm just trying to get a little bit more precise.

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Yes. So again, in our last half of the year, we raised guidance by about \$16 million. Some of that are these distribution deals. It's not a big part of it. Some of it are some tenders. Some of it is just our standard growth. But listen, Larry, I mean, we did \$20 million in the first half of growth above our forecast. We're saying \$16 million in the back, and we've got this opportunity not just for this product but our new products that we're introducing. That's where the upside comes from. And I mean, we're just trying to be conservative and not get out there too far and say, okay -- I don't know how to say it other than that because...

**Raul Parra Merit Medical Systems, Inc. - CFO**

We've got 2 weeks of visibility.

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Yes, we have 2 weeks in the quarter and we've got almost 1 month here. And looking at this, I mean, it's fair to say that, I mean, if we're ramping, we've got people we've hired. So we're not doing that because we think it's a fluke or it's short term. That being said, it has to materialize and I have to have a number. So I'm not going to come out and say it could be \$25 million this year. On the other hand, that's where the upside comes, I think, for the balance of the year. So we see strong growth, strong organic growth. And all of this other stuff, we're not defining it maybe as much as you'd like us to because we don't want to be wrong. But listen, from what I'm seeing every day, and I've watched this now for about 30 business days, it just keeps accelerating. And we're also then seeing those customers that with the original orders much like Cook, are reordering. And that's the business we're in, is meet customer needs, and that's what we're seeing. So if it -- I mean, I will say this, that if it gets to a point where we have to adjust it, we will do that because I don't want to be getting to the end of the next quarter and have something that is way out of -- we blew it out. On the other side of the coin, it's summer, Larry. It's summer and you never know what to expect. But I'll tell you what, looking at July and the momentum that we're in, it's an exciting time for the company. That's the best way I can say it. And as it continues to materialize, we will do our best to keep shareholders informed.

**Lawrence H. Biegelsen Wells Fargo Securities, LLC, Research Division - Senior Analyst**

That's helpful. And then -- I did have. So what are you assuming, Fred, on when they'll be back to the market? One question on the Q2. Did you see a benefit from Terumo in Q2? When are you assuming that will come back to the market? And that's it from me.

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Thanks, Larry. So we only had a couple of weeks. The last 2 weeks of the quarter, this started popping up. And we saw we had some business from there. Of course, it's continued to accelerate almost every day since that time. Now what they said originally is they'll be back in July. That's changed to August. But as these things generally go, they have a tendency, and I'm talking about Merit's own experience. They have a tendency to take longer than you think they do. But listen, if it stopped next week or in a month, the opportunity has still presented itself. Merit will continue to benefit from this for years. For years, okay.

**Operator**

And our next question comes from the line of Matthew O'Brien with Piper Jaffray.

**Matthew Oliver O'Brien Piper Jaffray Companies, Research Division - MD and Senior Research Analyst**

I'd like to also add my congratulations to Raul on the permanent CFO position. Sorry to keep harping on this, Fred. I'd like to kind of split the performance in the quarter or the question here between as far as the top line growth goes between both organic performance and what really drove that, which is really, really good because you raised that quite a bit. If you can just tease that out a little bit more. And then I think you said you hired 40 people in Ireland and 32 people this week. I think that was primarily for Terumo specifically. Were those temps or permanent hires? And doesn't -- if they're either of them, I guess, wouldn't that kind of suggest that you're thinking that the impact of that opportunity could be significant for the back half of this and then for years to come? If you can just talk a little bit more about how to kind of frame that up.

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Okay. Let me start with the employment, and then I'll let Raul address the issue. And let me add one more to it because not only is it in Salt Lake City, where we added 32 new employees today, and the new employees that we hired in Ireland. We've also hired new



employees in Texas. So the number is probably bigger than that. Generally, it depends on the area. We do hire, in fact, some temps from time to time, not a lot, but we do use it as a tool. But I will say this, that because of the labor pool, we're looking for permanent employees all the time. And so the employment issue is one that we will use the temporary thing, like I said, but it's a very small percentage. We're looking for full-time employees to work at Merit. Now on the -- and as I pointed out, and this is what I believe, this is not just an opportunity for this month or next month or for the balance of the year. This is an opportunity for many, many years to come. Why? Why do I say that? And the answer is -- and I made comments earlier about this, but to maybe reconfirm those, hospitals realized they cannot allow themselves to get into a position just to rely on one party. If you do that, that's an -- in manufacturing, you have to have alternate vendors. You have to have backups, plan A, B and C. And hospitals, I think, are going to figure out that after the Cook situation and with this, that they have to rethink what they're doing. And that's why I believe this is a long-term situation where people are going to have to think about their sources and how do they make sure they can treat patients. So it's a long-term opportunity. Now Raul, I'm going to let you talk a little bit about where the organic products came from. Do you want to go ahead and address that?

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**Raul Parra Merit Medical Systems, Inc. - CFO**

Yes. We really saw it across all regions. If you look, worldwide dealers was up, like we mentioned. What was that? Worldwide dealers was up 22.5. EMEA was up 10.5. OEM was up 11.5. So across all regions, we're seeing a lot of strong sales on the products, organic constant currency. Some of the contributors were in catheters, about 19%. EP recovered nicely. As you remember, last quarter was kind of flat. And this quarter, it's 17.3%. Inflation devices were up 13%, and standalone devices were up about 13.5%. So really we're seeing it across all product lines and across all regions.

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

And I should also mention, Matt, that our business for Catheter Connections, our [intercepted] cath, are up 46% this year. Our business is up on our Argon critical care business. So our business is up essentially, as Raul pointed out, across the board. So it's everywhere. And a couple of you guys -- again, I have to make an apology here to Raul. Over the weekend, Raul was appointed as our Chief Financial Officer and the interim went away. It was a unanimous decision by the board, and I think it was one that I supported as well. In fact, it's one that I recommended. So just so we can get that, I think it's in our 8-K today and you'll see it there so that we have that all cleared up. So Matt, does that answer your question?

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**Matthew Oliver O'Brien Piper Jaffray Companies, Research Division - MD and Senior Research Analyst**

Yes. Very helpful. And as my second question, just you guided down about 100 basis points here on the gross margin line. And Fred, that you're thinking about top line growth and driving things there makes total sense to me, and we're seeing it on the organic side. But can you just -- maybe you or Raul, just tease out where that 100 basis points guide down for the year comes from, be it the tenders -- or I'm sorry, the stocking that you got in the Middle East or the additional labor and shipping costs? And then as we think forward on the 3-year outlook for the business you committed to, 100 to 150 basis point improvement in that metric, is that still on the table?

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Yes. Let me just weigh in this a little bit before Raul goes. So I want to make sure because it's the second time I've ever said the 3-year plan. That was the original plan, and we had 2 years, not 3. And we said that our goal was to grow the business 7% to 9%, grow gross margins by 100 to 150 and grow the bottom line 13% to 15%. So those were those goals. And we thought it was the appropriate thing to do to extend those out. Well, now we see these opportunities come up, and of course, nothing stays the same. I mean, nobody thought that oil prices would be up \$70, \$70 a barrel and those were -- and labor, labor cost. Those are legitimate issues in all of our facilities worldwide, and they will continue to be. So I should say that we'll continue to move additional product lines to Mexico. We will continue to bring more and more automation in and do those sorts of things to drive margins. But Raul, why don't you go ahead and let you take it from there.

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**Raul Parra Merit Medical Systems, Inc. - CFO**

Yes, Matt, I think it's easier to talk about it on a yearly basis. So basically, what we're guiding now is 80 to 130 basis improvement year-over-year. And we see about 20 to 60 coming from organic, essentially manufacturing efficiency. And then the remainder is going to be 60 to 70 basis points from the biopsy and drainage, and that includes some of the integration expenses. So we're netting that down



a little bit. We previously had guided about 60 to 120, 130 basis points there. So we're bringing that down based on some of the integration expenses that we've had and then some of the expenses that we see in the fourth quarter as we start to manufacture our own product. Hopefully that...

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**Matthew Oliver O'Brien Piper Jaffray Companies, Research Division - MD and Senior Research Analyst**

Okay. But just to be -- yes, it's very helpful, Raul. Appreciate it. But just to be specific on the outward year, should we still think about the gross margin improving versus this year close to that 100 basis point level or something below that?

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

It will be our goal to have our gross margins at that level, yes.

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**Raul Parra Merit Medical Systems, Inc. - CFO**

Yes. We're not shying away from that. I think what we said it several times.

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

I think that's really important that it's not the end of the parade here.

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**Raul Parra Merit Medical Systems, Inc. - CFO**

Yes.

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

There's a lot more to go. Again, once these products and the sales -- we get the efficiencies of manufacturing these products and get those costs out and don't have to pay overtime, don't have to -- I mean, we're literally shipping product, guys, almost every day by air, all over the world. I mean, we normally would put it on the sea or there would be a weekly. But in order to take advantage of the opportunity, we're spending the money. And that's going to cost money. That being said, I want to remind you we're going to be up sequentially next quarter in gross margins and the following quarter. So we will continue to move even though we have these. And what's helping us there is this top line, and the upside is the opportunity. So that's the best way I can explain it.

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**Operator**

And our next question comes from the line of Jason Mills with Canaccord Genuity.

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**Jason Richard Mills Canaccord Genuity Limited, Research Division - MD of Research & Analyst**

Just adding my two cents, Fred. So we're all asking about revenue and gross margin separately. And in parts of the call, you talked about the revenue growth, Fred, the organic core revenue growth expectation has increased markedly. You're still expecting gross margin expansion, just maybe not quite as much, and I think we all understand that. So perhaps that's -- if you could, Fred, talk about gross profit dollars because obviously, that will combine the 2. And what I'm hearing, just back of the envelope math, is that your expectation for gross profit dollar growth has increased markedly, perhaps even as much as 300 basis points over what you were expecting before this quarter if we took your prior core revenue growth guidance and your prior gross margin guidance. And I'd like -- maybe, Raul, if you could level set me on those numbers. And if you would be either thinking about, over the next couple of years, your business in those terms, in terms of gross profit dollar growth, which will balance both the opportunities you hope to capture on the top line and the gross margin expectations you have to see expansion but perhaps not quite as much as you thought before. However, at the end of the day, your gross profit dollar growth expectations seemed to have moved up. Could you talk a little bit about that?

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**Raul Parra Merit Medical Systems, Inc. - CFO**

Jason, I think you said it best. I mean, we see that, too. The gross profit dollars are definitely there. It's just the percentage won't be there. So I agree with you. I don't think there's much more I can add other than that we expect those gross margin dollars to be there. And also, I'd like to point out that we expect to be operating -- our gross margin should be operating in the range that we have previously provided. So that 49.7 to 50.8, we expect the back half of that -- of the year to be operating around those areas. And you're right, we're getting the gross margin dollars.

**Jason Richard Mills *Canaccord Genuity Limited, Research Division - MD of Research & Analyst***

Okay. Got it. And Fred, I want to go back to that statement you made about Merit will benefit from this competitor issue for several years. Could you talk about that a little bit more because that's interesting, right. I mean, you're just -- you're not seeing it -- you're not expecting to just see it for a couple of months, that notwithstanding Terumo was talked about being back in July, now August and even if it's September, they're going to come back. It sounds like that's your expectation, that they're going to come back, which month doesn't really matter. It seemed to matter to the comment you made about benefiting from this for several years. So help us understand a little bit more about how you think that's going to benefit you over the next couple of years. I know you said, if I could caveat just a little bit more, that hospitals may move away from single source to multisource. Maybe you could give us a bit more granularity there in terms of what geographies you've seen single source being used most often. And perhaps you could explain to us whether or not those are the areas that you expect to see the greatest growth, those geographies in particular because it seems like in the United States, hospitals are fairly sophisticated and have been for a while with respect to dual sourcing a lot of products. So maybe you could just give us a bit more color there.

**Fred P. Lampropoulos *Merit Medical Systems, Inc. - Chairman, CEO & President***

Well, I'm going to start with your last comment because I think there is, in fact, a lack of sophistication in the United States. This is, again, a personal opinion. I mean, when you saw the situation with Cook, they really weren't set up. They were single-source opportunities there. That's changed. So -- and when you have buying groups that are looking to try to make value propositions, they drive a lot of this type of stuff. I think, again, if you're a hospital administrator -- in fact, we have a couple of members of our board that had been chairpeople of 2 hospital systems here in the Intermountain West. And as we talk to them and talk about these issues, I think more and more people are thinking, wait a second, who are the 2 top players here and who can provide the product? So I just can't give the credit to the systems because there are a lot of other factors like buying groups, CPOs and so on and so forth that play into that. But I want to go back to maybe some comments that -- on the radial revolution that we've talked about for a long time. And if you look back in Europe, as you're well aware, we have radial procedures that in many cases can be up to 80% and in some countries, up to 90%. That situation started growing. I was told that I was nuts 5 or 6 years ago when it was 5%. And I said this will grow to 80%. That has come out and supported that these procedures are less expensive into the thousands of dollars. And you have better mobility, and maybe more important, the customer preference is to have something where you're not messing around with somebody's groin. Those are the facts of the marketplace, and we've continued to see that. Many of the products that are part of this are, in fact, products that are radial. But what we've seen is it's starting to spill over to all of our standard sheaths. It's spilling over not just to guide wires that are hydrophilic but all of our guide wires. Now again, it's early, but we're starting to see those kinds of trends. But here's the bottom line, if you look at the PreludeEASE and the Prelude IDeal, those are products that in my view are better. We've been told by physicians they're better than the Terumo products. And Terumo is a great company. So in my view, it's having a better product but the opportunity to show the product. That's how it's selling, is you got to have a center you put in the door. Once you're there, you can show how you can solve problems and how you can broaden the product offering. So I think it has to do with -- on Slide 13 on our website, if you look at this, I think it's compelling and supports the argument. You take a look at the sheaths. You take a look at the guide wires. You take a look at the microcatheters. This includes the SwiftNinja. I mentioned that we have the new Pursue and we have the Maestro. So all of these -- we are doing everything we can to meet this demand. And then we throw some of these things outside of that like the SYNC and the Impress hydrophilic. So it's not just the Impress catheters, but Terumo had a big market share for hydrophilic diagnostic catheters, which get about a 3x pricing over your standard catheter. Those are also in this product. So again, it's as broad as an opportunity as I've ever seen. Now let's talk about geography. I don't want to get into tactics and strategies, but let me just say that people in their movements and trying to solve problems employ various types of tactics and strategies, and so does Merit. We're seeing, for instance, in Europe, a much higher demand for sheaths and guide wires than we are seeing in the U.S. Now in the U.S., we're starting to see some of those trends. So people were moving around. This is not an indictment of any sort, but people were trying to fill holes. And so initially, we saw this in Europe. Then we've seen it in the U.S. Now we see it pretty well -- pretty much everywhere. So we're seeing it across the board geographically, and it started out with something being really strong. And maybe even products move. Listen, we move products from time to time between -- let's say, in the U.S., if we have shortages, we'll move products to fill those needs, let's say, in Europe or in China. So we're seeing from very interesting issues. Fortunately for Merit, we have manufacturing in these locations, and we have this broad product line. So it's changing daily, and we see shortages, and we see little things pop up that work as hot. But what it tells me is if you look across, they're doing the best they can to manage their business with what inventories they have. I don't know when they get back, but I'll stand by what I said. This is something that's going to be beneficial for Merit for years to come because we now -- it's like the kid



that's sitting on the bench. Remember that guy by the name of Lou Gehrig. He was sitting on the bench Monday, a guy couldn't play. And then Lou Gehrig played for the rest of his career. And I think this is something like where now the new kids on the block are formidable. We have the product. We have the breadth and something else. And I'm sorry to keep going on with this stuff, but I had someone say to me the other day, Jason, "I understand your business for the first time." Well, this is a guy that's owned Merit stock and had been involved with us for 15 years. I said I thought we have done a bad job if you're just trying to figure it out. He said, "When I look at this and compare it against that, I can now see why all of these little things that you did really add up to something big." And so if anything, I think it is better knowledge of the breadth and the strategy that Merit has employed for its corporate history of building out product lines. And that is the benefit of time. Merit has taken the time to build the business and build it correctly. And so when something like this pops up, we're ready to respond to it. And not very many can, not like we can, but just don't have the breadth of products that we do. So that's the best way I can answer your question.

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**Operator**

And our next question comes from the line of Jayson Bedford with Raymond James.

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**Jayson Tyler Bedford Raymond James & Associates, Inc., Research Division - Senior Medical Supplies and Devices Analyst**

Just a couple of questions. I realize we're bumping up against time here. But just to come back to 2Q sales, competitor recall occurred in late June. You talked about the impact on the business accelerating. I'm still little unclear as to the impact in 2Q. Was there a material impact on revenue in 2Q from this competitive dynamic?

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Yes. First of all, it wasn't a recall. It's called a shortage or unavailable. We're not aware that there's a recall. So I want to make that clear. We saw the last couple of weeks it had no material impact on the quarter whatsoever. They were stopped there, but it started -- the tide started rolling so to speak. And then it just continues to accelerate essentially every day since. So we already started getting reorders and new orders. So you'll see the effect of it, of course, a big effect of it in this quarter and going forward.

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**Jayson Tyler Bedford Raymond James & Associates, Inc., Research Division - Senior Medical Supplies and Devices Analyst**

Okay. And just to be clear, if in 2 weeks, your competitor comes back to market with whole supply, you're still comfortable with the guidance you laid out?

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Yes. First of all, they said they'd be back in August. I think it's the end of -- everything is like with my staff. It's never the 1st of August. It's the end of August. And I don't even know if they will come back, but it really won't make any difference. We're very, very, comfortable. And I think that's the thing we try to do, Jayson, say, look, here's what we see. I have my own personal view on this. We're staffing because, as I mentioned, this is, in my view, a long-term opportunity. And we will see benefits for this for years to come, not just for weeks to come.

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**Jayson Tyler Bedford Raymond James & Associates, Inc., Research Division - Senior Medical Supplies and Devices Analyst**

Okay. That's helpful. And then just finally from me, what's the expected revenue contribution from the acquired BD assets? It looked like acquired revenue came in a bit higher than we're expecting in 2Q. Just out of curiosity, how is that business tracking? And have your expectations changed for that contribution in '18?

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**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Well, in fact -- go ahead. Go ahead, Raul.

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**Raul Parra Merit Medical Systems, Inc. - CFO**

Yes. It's \$40 million to \$43 million now, is what we are seeing for the year. I think we have previously disclosed \$38 million to \$42 million. So just to give you a general idea.

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**Operator**

And our next question comes from the line of Mike Petusky with Barrington Research.



**Michael John Petusky Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst**

So I just briefly want to touch, again, on gross margin and really specifically dialing it on sort of the second half guidance and the sequential growth that you guys see there, which to me, it needs to be fairly material from -- versus the first half to even get to the lower end of your full year guidance. And I guess just if you go can walk me through just real quickly the 2 or 3 things that sort of drive that sequential improvement in the third and fourth quarters.

**Raul Parra Merit Medical Systems, Inc. - CFO**

Yes. It's going to be obviously the biopsy and drainage product lines. It will be manufacturing efficiencies. We expected 4 manufacturing efficiencies, but as we've discussed, there's couple of headwinds that are going to slow it down just a little bit. And that's really what's driving it. And again, we expect to be operating in the 49.7 to 50.8 range later half of the year.

**Michael John Petusky Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst**

All right. Great. And then, Raul, if you could just start to dig in, in your cash flow statement there for the D&A, stock comp and CapEx for the quarter, that would really be helpful. And I'll -- go ahead. If you have it, that's great.

**Raul Parra Merit Medical Systems, Inc. - CFO**

17.5 on depreciation and amortization for Q2, and 1.6 million stock comp.

**Michael John Petusky Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst**

What about CapEx?

**Raul Parra Merit Medical Systems, Inc. - CFO**

CapEx was \$15 million.

**Michael John Petusky Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst**

All right. Great. And then just one last question. Fred, what can you say, if you can say anything? Legal expense continues to sort of -- \$1.5 million here, \$1.5 million there starts to add up to real dollars. I'm just curious if you have any update that you can share there or what you...

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

No, Mike, I wish I did. Nothing. I mean, we continue to comply whenever they ask for something, and we've heard nothing. And that's the whole truth and nothing but the truth. There you go.

**Michael John Petusky Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst**

Okay. So no sense of when this might wrap or it's just open ended?

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

No. Yes, it's -- yes. I mean, we could spend hours on this, but I should keep quiet.

**Operator**

And our next question comes from the line of Mike Matson with Needham and Company.

**Michael Stephen Matson Needham & Company, LLC, Research Division - Senior Analyst**

I guess, Fred, you made a comment about guiding down for the summer quarter. And I think what you were talking about was the sequential revenue from Q2 to Q3, it's normally down, I guess. But were you -- it seems like you're almost saying that the revenues could be up from Q2 to Q3. I mean, am I interpreting your comments the right way there?

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

I think historically, Mike, we have always guided down because of Europe and lots of places, I mean, I think historically, it's sound. So we have always guided down. I think right now, the guidance from the second quarter to the third quarter is what, Raul?

**Raul Parra Merit Medical Systems, Inc. - CFO**

\$210 million.

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Okay. But what's the number? I mean...

**Raul Parra Merit Medical Systems, Inc. - CFO**

\$210 million.

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Okay. That's for the -- that's our guidance?

**Raul Parra Merit Medical Systems, Inc. - CFO**

No, it's history.

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Okay. So the point is we almost always guide down. Now that being said, we have this opportunity in front of us, and we'll just have to see how that plays out. So under our new guide -- well, we don't guide quarterly.

**Raul Parra Merit Medical Systems, Inc. - CFO**

We don't guide by quarter. But we are saying that it's going to -- we expect to have lower sales than did in Q2.

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

Yes.

**Raul Parra Merit Medical Systems, Inc. - CFO**

Historically, that's what's happened.

**Fred P. Lampropoulos Merit Medical Systems, Inc. - Chairman, CEO & President**

That's historically what's happened.

**Michael Stephen Matson Needham & Company, LLC, Research Division - Senior Analyst**

All right. And then, Raul, can you just comment on the integration expenses? So how much of that is included in the adjusted EPS number or adjusted margins, I guess? Can you -- maybe in terms of basis points, if you can put it in basis points, it will be helpful, either in terms of the gross margin or operating margin. Or are you stripping all that out from the adjusted numbers?

**Raul Parra Merit Medical Systems, Inc. - CFO**

We're stripping that out from the adjusted numbers. That's right. Lower. 60 to 70 basis points. Right. So we're seeing about approximately 30 basis points is what the impact is on margin. Now we have some operating...

**Michael Stephen Matson Needham & Company, LLC, Research Division - Senior Analyst**

30 basis points on a GAAP basis or on an adjusted basis?

**Raul Parra Merit Medical Systems, Inc. - CFO**

Adjusted basis.

**Michael Stephen Matson Needham & Company, LLC, Research Division - Senior Analyst**

Okay. So there's still 30 basis points in there from acquisition-related stuff?

**Raul Parra Merit Medical Systems, Inc. - CFO**

That's right.



**Michael Stephen Matson *Needham & Company, LLC, Research Division - Senior Analyst***

Okay. All right. And then I just wanted to go back. Fred, it sounds like you're not too worried about the China potential trade war, but I just wanted to get maybe a little more detail there around your thinking on that. And I know that -- I guess there's been some tariffs on devices coming back to the U.S., but I don't think that that's really the case with your supply chain. But what's the risk if China puts tariffs on some of the products that you're selling, I guess? Or are you making those all in China locally?

**Fred P. Lampropoulos *Merit Medical Systems, Inc. - Chairman, CEO & President***

Well, as you know, Mike, we were looking back here and we started talking about the border tax several, what was that, 18 months ago. I mean, I answered a lot of questions and the answer was I have no idea. We're not seeing anything that limits our ability to do business in China. They want to do joint ventures. They have preference to local. But that's not any different from where it's been in the past. And in fact, I believe, Joe, if this is correct, did we not grow at about 30% last quarter?

**Joseph C. Wright *Merit Medical Systems, Inc. - President of International Division***

Yes.

**Fred P. Lampropoulos *Merit Medical Systems, Inc. - Chairman, CEO & President***

Okay. So I mean, business continues to be very, very robust. I'll also say that this situation that we're talking about with a competitor actually helps us there as well because I think in many cases, they prefer to do business with American company. So I think there's opportunity for us to grow there as well. So listen, we could spend a lot of time in what ifs and whatnot. We just don't see anything that's affecting our business today, and that's the best answer I can give because that's -- we just don't see anything. We read the news. We listen to the news like you guys do, but we just don't see anything that affects our business at all at this point.

Okay. Listen, ladies and gentlemen, this has been a long call. I hope we have clarified it. Let me just summarize by saying this. Revenues were up almost \$10 million, above, I think, consensus. It's almost \$20 million year-to-date. We believe that we have a lot of tailwinds. There are some headwinds. We talked about some expenses, labor, please don't overlook the cost of labor, and fuel and the filling of the pipeline, those issues that are there.

That being said, please do not forget our commitment to growing gross margins, maintaining the discipline in expenses. I mean, what's been interesting on this call is nobody's really asked about Becton, Dickinson, which is -- other than the one question, and no one's really asked about the bottom line. Everybody is concentrating on all this other stuff. But please take a look at what this means. We've increased our bottom line, and we think that there's upside to a number of these issues based on the circumstances that we've talked to you about. If those all play out, then there are going to be extraordinary opportunities for value here.

So again, let's keep our eye on the ball. We are. But let's keep our eye on really the important things. And again, as I said in my comments, they don't put multiples on gross margins. It's important. Please don't misunderstand me. I am not diminishing it. What I'm telling you is that we think that given this quarter to get through these expansions, then it's going to have a long-term positive impact on the business in addition to everything else we're doing. I think when you -- listen, 10% to 11% organic growth, that's terrific. My staff is sitting here. I think it's terrific. We're making more money, and we'll continue to make more money.

So I hope -- again, we'll look at the reports. And we appreciate all of the interest. The business is fine. It's growing. It's accelerating. We have tailwinds with just a slight breeze in our face. So that being said, I thank you for your time, for your questions, an hour -- almost an hour of questions. We'll be around. You haven't even worn us out yet. We're going to wear you guys out. So give us a call. We're here and we'll see what we can do to clarify it. Thanks again for joining us, and good night from Salt Lake City.

**Operator**

Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program, and you may all disconnect. Everyone, have a great day.



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