VieMed Healthcare, Inc.

Second Quarter 2018 Earnings Call

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CORPORATE PARTICIPANTS

Casey Hoyt, *Chief Executive Officer*

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CONFERENCE CALL PARTICIPANTS

Douglas Cooper, *Beacon Securities*

Brooks O'Neil, *Lake Street Capital Markets*

Michael Eisner, *Private Investor*

Christopher Olin, *Alesia Asset Management LLC*

PRESENTATION

Operator:

Good day, and welcome to the VieMed Second Quarter Earnings Call. Today's conference is being recorded.

At this time, I would like to turn the conference over to Todd Zehnder, Chief Operating Officer. Please go ahead, sir.

Todd Zehnder:

All right, thank you, Jessica.

Please note that remarks in this Conference Call regarding our expectations, future plans and intentions may constitute forward-looking information as such term is defined in applicable Canadian securities legislation. All statements other than statements of historical fact may be forward-looking information. Such statements reflect the Company's current views and intentions with respect to future events and current information available to the Company and are subject to certain risks, uncertainties and assumptions. Many factors could cause the actual results, performance or achievements that may be expressed or implied by such forward-looking information to vary from those described herein, should one or more of the risks or uncertainties materialize.

Examples of such risk factors are discussed or referred to in the Company's disclosure documents filed with security regulatory authorities in certain provinces of Canada and are available at www.sedar.com. Should any factor affect the Company in an unexpected manner, or should assumptions underlying the forward-looking information prove incorrect, the actual results or events may differ materially from the results or events predicted. Any such forward-looking information is expressly qualified in its entirety by the cautionary statement.

Moreover, the Company does not assume responsibility for the accuracy or completeness of such forward-looking information. The forward-looking information included in this conference call is made as of the date hereof, and the Company undertakes no obligation to publicly update or revise any forward-looking information, other than required by applicable law. The second quarter financial results, news release and related financial statements, and the MD&A, are now available on SEDAR.

Now I'll turn it over to Casey to get started.

Casey Hoyt:

Thank you, Todd. Good morning, thank you for joining us on our call today. My name is Casey Hoyt and I'm the CEO of VieMed. I'm pleased that Todd and I have the opportunity to be reporting on yet another record-setting quarter from our team here at VieMed.

Before I do, I'd like to first review, for our first-time listeners, an overview of our company and services. At VieMed, we treat patients with very sick lungs by providing around-the-clock care due to the placement of respiratory therapists inside the home. Our patients primarily come to us at the end stage of their lifecycle when they are most prone to burdening the healthcare system with costly hospital readmissions.

Our business is a very high touch, high service model that requires our clinician to educate, nurture and respond to our patients with a very high quality of care. We treat patients struggling with a variety of disease states, including chronic obstructive pulmonary disease, neuromuscular diseases, sleep apnea and many more. While the equipment we use in the home is on the cutting edge of technology, it is our service that separates us from our competitors.

Our marketplace is currently underserved, with only 5% market penetration across the entire industry. The market is being driven by an onslaught of baby boomers, aging at a rate of 11,000, turning 65 every day for the next 19 years. Last year, we achieved a growth rate of 42% by way of deploying our very lean, organic growth strategy into a coverage area across 25 states. We have spent the first half of this year expanding our team at a greater rate to achieve higher active patient growth. We are very pleased with the execution coming from our Management team, as they have kept the revolving door of new clinicians and salespeople coming into our organization.

With every new salesperson or clinical liaison comes a new territory for us to capture further business. Our Management team has been working tirelessly to find quality employees that exemplify passion, quality and efficiency to be added to the VieMed family. Since the beginning of the year, they have added 17 new liaisons and salespeople. They were also able to further evolve our training program for new recruits, allowing us the ability to get more people up and running at a faster rate.

The Technology department has been busy as well, as we have pulled the trigger on investing in a new platform that will allow us to capitalize on many more operational efficiencies. Aside from streamlining billing, intake and field service efficiencies, our new platform will put us into position to easily integrate with other facility and outcome databases. This will put us in a position to better report on a real-time basis to payers who choose to be better connected to their patients and suppliers.

On the payer front, our Network Development team continues to keep the momentum moving in the right direction. They have landed 18 contracts this year, which has helped us increase our conversion rate. The efforts of our team have allowed us to capture more business and contribute to keeping the salespeople morale at an all-time high.

Another thing contributing to salespeople morale are the results of the KPMG study. We have uncovered that, for every six people we put on our non-invasive ventilation therapy, we save a life. As our Medical Directors move to publishing the results of the powerful study, which will be the largest study of its kind in the U.S., we have been busy getting the message out to the docs that have been ordering with us since 2012. They are receiving the message extremely well, and it is contributing to further growth from some of our more veteran referral sources. We have recently just engaged with a healthcare PR firm, Amendola Communications, to further assist us with getting the KPMG results out to more payers, physicians and patients.

We also just completed our AGM Meeting in mid-July where we elected our new Board member, Bruce Greenstein. Bruce comes to us by way of the department of HHS, Human Health Services, where he was the Chief Technology Officer under Secretary Price and Azar. Bruce has entered the private sector recently, currently working for one of the largest home health companies in the country, LHC. We are fortunate to have Bruce on our Board as he brings both his knowledge of healthcare and technology solutions, and a better understanding of the governmental and regulatory affairs landscape. I'm very grateful to have such a helpful and balanced Board that is laser-focused on adding shareholder value.

There's been some recent activity on the regulatory front for the DME industry that is extremely positive. CMS has just announced that, beginning in January 1, 2019, they will suspend the competitive bidding program for the following two years across the country. While we have less than 5% of our product mix subject to competitive bidding rates, the real win is the relief that the DME suppliers are receiving as we see CMS move to supporting more home-based suppliers. This initiative is a signal of stability and security for our industry, and now opens us up to scaling into territories with products and services that we would have previously avoided.

We have also remained active in the second quarter, telling our story to as many financial institutions as possible. Todd and I, with the help of Bristol IR firm, have been making ourselves available to tell our story to as many institutions as we can. We were able to get out to Vancouver and Los Angeles on road shows as we look to expand our U.S. and Canada investor participation. While in L.A., we presented at the LD Micro Conference and met with many investors in a short period of time.

We also executed our uplisting in the second quarter to the Toronto Senior Exchange, and grew our market cap from CAD$120 million to CAD$175 million.

As we roll through the third quarter, our focus moves to finding more coverage and investors inside of the U.S., in an effort to drive our stock price and add further shareholder value.

At this point in time, I'd like to turn the call back over to Todd to provide a financial overview of the quarter.

Todd Zehnder:

Okay, thank you, Casey. In reviewing these financial results, all of the figures are in U.S. dollars and, once again, the full results are available on SEDAR.

We generated revenue of $15.5 million during the second quarter of 2018, as compared to revenues of $10.9 million in the second quarter of 2017, which equates to a 42% increase. Our revenues came in slightly higher than our previously guided range for the second quarter. Additionally, our gross margin percentage was 73% during the current year, as compared to 72% last year.

Adjusted EBITDA, which excludes depreciation and stock-based comp, totaled $4.1 million for the quarter, which is a 27% margin, consistent with last quarter. We once again redeployed a majority of this EBITDA during the current period, as our cap ex totaled $3.7 million, primarily driven by new vent purchases to support our growing patient base.

Our SG&A totaled approximately $7.9 million, as compared to $5.9 million in the prior year. As we have previously talked about, our 2017 results had certain items that could not be accrued until our legal spinout was made. Therefore, quarterly comparisons will have some noise in certain areas. We continue to manage our cost structure, as we are in a rapid growth mode, to assure that we can push as much growth to the bottom line. With that said, we are very aggressively setting the Company up for future growth, and we'll continue to invest in our people and our shareholders, as evidenced by our recent uplisting to the TSX Senior Exchange. We will continue to expect revenue and gross margins to increase at a higher pace than SG&A expenses.

Our balance sheet remains solid, with approximately $8.6 million in cash at year-end, $7.9 million of clean AR, and an overall working capital balance of $5.6 million. We significantly grew our cash balance during the quarter, an increase of roughly $4 million, which is almost at double during one quarter. Our AR balance was once again higher at quarter-end than our expectation going forward, as we finish off collections of our previously disclosed audit, but we have received a significant portion of the money which helps with our rapid cash growth. Our long-term debt, which is primarily made up of capital leases, is very manageable and being serviced with operating cash flow.

Moving on to the third quarter, we have provided revenue guidance in the $16.3 million to $16.7 million range, and feel that our gross margin and Adjusted EBITDA percentages will once again stay consistent with this quarter. We will reiterate that all of this expected growth is organic, and we are excited to continue to push out our therapy to as many new patients as we can every day.

From a capital perspective, we continue to use our internally generated cash flow and capital lease with our major vendors, and we believe that we will be able to fund our future growth using the same financial instruments. Once again, our line of credit with Whitney Bank remains fully undrawn and serves as an easy way to finance any excess capital needs that might arise. While we don't have a current planned use for the line, it is nice to have that excess liquidity.

We continue to meet with both the buy and sell side, as well as many bankers and industry peers, while at the front of our mind is serving our patients and ultimately doing what is best for our shareholders.

At this time, I'm going to turn it back over to Casey to wrap things up.

Casey Hoyt:

Thanks, Todd. Our history has proven that we have a recipe to expand our footprint at a high growth rate. Our results demonstrate our ability to capture market share in an efficient manner. We are leveraging our expertise and lean, scaleable business model to stay on our growth trajectory. We have a nice pipeline of sales and existing referral sources that stands to increase as we work to get our game-changing results out to our physicians on the KPMG study. This data gives us a huge head start on our competition before we publish final results for the industry to have.

Our team will not be resting during the back half of this year. As we continue to grow cash, our thoughts shift to prudent capital allocation by way of organic growth or finding strategic acquisitions here in the coming quarters. Our company has always had a track record of delivering on multiple fronts. We remain committed to putting the patient first by delivering the highest quality of care in the DME sector.

In closing, I'd like to thank the employees that make up the VieMed family. Without your commitment, passion and professionalism, none of this would be possible. Thank you for creating and being part of one of the best company cultures in the country, which most definitely is VieMed's secret sauce.

This will conclude our prepared remarks. We'll now open up the floor for Q&A. Thank you.

Operator:

Thank you. If you'd like to ask a question, please signal by pressing star, one on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star, one to ask a question.

We'll go first to Doug Cooper with Beacon Securities.

Douglas Cooper:

Hi, good morning, guys. Congratulations on a great quarter.

Let me start with the KPMG study. Can you just talk about where you stand with the marketing to the physicians, and what do you anticipate the rollout, if I can call it that, in terms of marketing to them will be, and how long, typically, between their awareness and them starting to prescribe the therapy?

Casey Hoyt:

Yes, the rollout to our existing physicians is underway, Doug. Like anything new, it takes a lot of training here in-house with our people, our managers, to make sure that the information is understood and interpreted correctly, and rolling off the tip of their tongue the right way. We've been spending a good bit of time on that.

We've got positive responses just out of the gate, but we're still building momentum, even with our existing referral sources. We're seeing up ticks and successful stories coming from around the country, but we predict that it's going to drive some organic growth with our existing guys as we get better at telling the story and get more comfortable with it.

Douglas Cooper:

Okay. Can you speak to—I think you talked about how many salespeople you've added this year. What's the total number of salespeople as it stands at the end of Q2; where do you think it might be at the end of Q3, and I think you mentioned, you're in 25 states. Is there any new states you're looking to move into before the end of the year?

Todd Zehnder:

Yes, Doug, I'll field that one. Between our Patient Care Coordinators and our Clinical Liaisons, which are both sales folks, we have it right at 65 total, currently. We still are committed to getting to that, roughly, 75 number, that we have set by the end of the year. We've been very active; we could exceed that, but I think that's still a good number, currently, to go for.

As it relates to new states, we're extremely active right now. Pretty much any state that you look at that's green on our map, or not on our map, we're probably in some phase of getting going. There's some that are probably more near-term; Colorado and Alabama and probably Michigan are real close. Pretty exciting is that we have started the process to get into Florida and California as well; it's going to take us a little while longer. We have our own internal Payer Relations, Network Development and Compliance groups running full speed ahead to be ready to go into all states.

Douglas Cooper:

Perfect. A couple further things, just on the payer side of things, because you said you added a number of payers this year. You had talked about in the past trying to work some relationship with big payers, and maybe you can just touch on—I think you had mentioned in the past, the VA or veterans—with the veterans. Any movement on those two fronts?

Casey Hoyt:

Yes. On both fronts, there's a lot of activity. I mean, the new contracts are—it's kind of like step one into building the relationship to getting to the bigger shared savings contracts that I've spoken about in the past. We've still got a handful of our four or five payers that have been going on the discussion for the past year and a half that are interested in doing shared savings programs.

We're not there yet, unfortunately same administrative hurdles to report there, but the good news is our efforts, and getting these contracts are generating more just standard contracts around the country, increasing our conversion rates of how many new orders we can now take, where we were previously denying. We've been able to really move the needle with converting more business with those new payers, if you will.

On the VA front, we are very active right now. We're kind of in the process with, I guess, getting through their red tape if you will, to be able to take business, but we're getting very close with that. We have some other balls in the air as well, strategies in place to penetrate that market. We remain very committed and excited about the VA opportunity, as it will diversify us from payer, from Medicare, to tap into a new payer source.

Then, really, at the end of the day, the patients that just are needing us right now that have no solution, it's just exciting for us to work on because we're going to fill a void that they need.

Douglas Cooper:

Okay. Final question from me, Todd, it looks like that as a percentage of revenue dropped to under 7% this quarter. Is that an anomaly, or you think that's a sort of run rate going forward? Thanks, and I'll leave it there.

Todd Zehnder:

It's a little bit—yes. It's a little lower than what we would still expect. I think our general guidance still says 9% to 13% is where we think we're comfortable, and that we hope to outperform that. The main reason we came in quite a bit lower than that is because, even though we are extremely confident and have been very clear with everybody that we intend to collect all money that was frozen, our normal processes and procedures put risk to everything, and as it gets older, it gets a little bit more provided for.

As we've collected a significant portion of that money that was frozen as of the end of last quarter, it just naturally is going to bring down our provision, and that's why you're going to be a little lower.

Douglas Cooper:

Okay. Great, that's it for me. Thank you.

Casey Hoyt:

Thanks, Doug.

Operator:

We'll now take a question from Brooks O'Neil with Lake Street Capital Markets.

Brooks O'Neil:

Oh, good morning, guys. I had a couple questions. I'm guessing you don't want to talk a whole lot about the specifics of the KPMG study, but can you just give us a sense for the scope of that study and maybe what one or two of the key findings might have been?

Casey Hoyt:

Yes. If you think about the other clinical studies that were available to us before the KPMG study was around, they both came from Europe, done about 15+ years ago, Brooks. One of them was like 120 patients, the other was roughly 90 patients, very small statistical studies.

The KPMG study has got about 15,000 patients in it. The key findings are, we're saving to the tune of $25,000 per patient per year. The mortality rates on our patients are going down 42%, and a relative mortality rate—an absolute mortality rate of 16%, that translates into, every six patients we put on therapy, we save a life.

This is big stuff for physicians to really understand, and they are the ones that are clicking on it. We've had all these guys that have done business with us since the beginning of time, that have just done business with us because it felt right and their patients have—they see the reward with their patients. Now they have something to back up all the good that they've been doing for all these years, and we're seeing at the buy end, there's even more—whenever you think about how a physician looks at helping their patients, I mean, you can use a couple of examples like the flu shot and Lipitor. For every thousand flu shots they put on someone, they'll save a life. When you look at Lipitor, for every 71 patients they put on Lipitor, you'll save a life-threatening heart attack. For us to be able to go in there and say, doc, for every six patients you put on our therapy, we can save a life; it's eye opening for these guys.

Those are some of the main key findings, as well, there's a lot of data in there showing us about how much better we're doing than our competition, but for now, it's really just about getting the big picture message out to the payer community and to our physician network. The payer community is really going to have to come after—not the payers, the Medicare community, I should say, will come after we're published. Dr. Frazier's moving towards publishing; that could take six to eight months to publish, but in the meantime, we're getting going with marketing right now.

Brooks O'Neil:

That's great. Could you just also talk a little bit about the opportunity that's opened up by the change in the DME regulations in the elimination of competitive bidding? How do you think you could take advantage of that opportunity?

Casey Hoyt:

Yes, it’s really one of the first times we’ve seen relief in a long time in our industry. I mean, we’ve got various lobbying groups and agencies that have been working hard to really fight against the competitive bidding program. We’ve all known it was broken, that it really drove out a number of different American business suppliers out of the marketplace and got to the point where it was hard to find people to take care of these patients. They’ve identified that, and it’s a signal of them backtracking a little bit, which is great for everybody involved. It just kind of shows a sign that they’re embracing treating these patients for less, in the home, through the DME industry.

Opportunities for us; we have a home sleep business and a CPAP business that is more localized here. The home sleep business is set up to be a national provider, and we can now—there’s now more margin and more areas that we can dip into with that business model; there might even be some avenues for us to expand our oxygen business as well. Those are the things that we’re a little bit excited about.

But the relief that they’re giving, the competitor bidding program, is just a signal for stability for the future of vents as well. I mean, there’s been a lot of questions that we’ve fielded along the way about, will vents ever be included in the competitive bidding process? I think this is a sign that we’re further away from that being a real threat to us.

Brooks O’Neil:

Absolutely, that’s great. Thanks for taking my questions.

Todd Zehnder:

Sure.

Casey Hoyt:

Sure thing.

Operator:

Once again, it is star, one to ask a question.

We’ll go next to Michael Eisner, a Private Investor.

Michael Eisner:

Are you guys thinking about going on the NASDAQ Exchange?

Todd Zehnder:

Yes. I mean, going to the U.S. markets is clearly something that is on our long-term goals. This year, it was all about uplisting to the big board in Toronto, and we’re doing some things internally to be ready to do that at some point down the road.

Michael Eisner:

Any timeframe or anything?

Todd Zehnder:

We haven't disclosed any timeline on that.

Michael Eisner:

Okay, thank you.

Todd Zehnder:

Sure.

Operator:

We'll now take a question from Christopher Olin with Alesia Asset Management.

Christopher Olin:

Hi, guys. Congrats on the great quarter.

Todd Zehnder:

Thank you, Chris.

Christopher Olin:

My first question is just a quick one. Can you tell us what the vent utilization rate was in the quarter?

Todd Zehnder:

We're hovering roughly around 90%. We manage our inventory accordingly, and as we've grown our patient population, as well as growing our sales and our chief staff (phon); we just generally fall in, about having 10% slack in the system.

Christopher Olin:

Okay, cool. Kind of a bigger picture question: are you guys interested in selling this business again if you got the right offer, or are you more committed to the long-term at this point?

Todd Zehnder:

Well, right now, all the good that we're doing every day and showing the growth that we have, clearly has us excited to growing this long-term and sticking with it. We've just really expanded with the work that we've done with KPMG, the cost savings that were shown in the system, the lives that we're saving. There's really no reason for us to wake up and come into work one day and say, let's sell it. We're all having fun; we've got a growth strategy in place, we've got a great team around it, so that is clearly not the intent of the business right now. I can definitively say, we have not had one serious conversation about selling our business.

Christopher Olin:

Awesome. Good to hear. Then, speaking about the long-term here, should we take the cash buildup as a signal that maybe your cash flow is running ahead of your ability to reinvest it, or is this more of a quarter-to-quarter fluctuation?

Todd Zehnder:

Well, this quarter was a little bit of an anomaly, like I spoke about in my prepared remarks, because we had the Medicare issue that was lingering and we got all that money unfrozen. It's hard for us to say if we're going to be able to reinvest all of it because it all depends on our growth rate. I mean, last year was a good proxy; we grew 42% and we reinvested most of the cash. As you get bigger, it's hard to grow the same percentages, which will yield a cash buildup, which is a great result, but you may have heard Casey speak about it at the end, we're still looking at new areas, new ways to grow faster organically, which would take more capital, and/or looking at redeploying that cash in any other way that could build shareholder value. The number one thing that comes to our mind is an acquisition.

While we've always been an organic company, we're hitting a point in our lifecycle where we're growing really fast and our balance sheet is getting to a point where we need to start seriously evaluating cash utilization. We as a Board and Management team are looking at all of our options pretty diligently right now.

Christopher Olin:

Cool, and in terms of acquisition targets, I know you've talked about before, acquiring a relatively small acquisition in the pediatric space. Is that kind of still the main option you're looking at?

Todd Zehnder:

It's one of the options. I mean, we're looking at, I guess, three different options, if you will. The pediatrics is one, and another was looking at another vent company that might be a quality provider, and then the third would just be a more strategic, complementary bolt-on acquisition, if you will, to what we're already doing.

All of those balls are in the air right now, we're just kind of—just going through to see what's going to bring the best value for the shareholders. Chris, we're by no means far along in any of those processes. We will obviously disclose if we get to a point. What we're not going to do is acquire just to acquire, but like Casey mentioned, we've got a few different strategic reasons to be looking at some of these companies. Just rest assured, we're working that at the same time as growing organically.

Christopher Olin:

All right, great. Thanks, guys. Appreciate the time.

Todd Zehnder:

All right.

Operator:

It appears there are no further questions at this time. I'd like to turn the conference back to our speakers for any additional or closing remarks.

Todd Zehnder:

All right, well, we want to thank everybody for dialing in today. Please follow-up with any follow-up questions, either through Bristol or myself or Casey. We look forward to seeing investors while we continue to make ourselves available as we travel around both the U.S. and Canada.

Operator:

This concludes today's call. Thank you for your participation. You may now disconnect.