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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Merit Medical Systems First Quarter 2020 Earnings Call. (Operator Instructions) Please be advised that today's conference may be recorded. (Operator Instructions)

I'd now like to hand the conference over to your host today, Mr. Fred Lampropoulos, Chairman and Chief Executive Officer. Please go ahead, sir.

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

Good afternoon, ladies and gentlemen. This is Fred Lampropoulos. I'm joined with Raul Parra; as well as our General Counsel, Brian Lloyd; and Anne-Marie Wright, our Vice President of Corporate Communications. A little unusual today because normally, we have many, many people in this room. The 4 of us are all that you have today, but our staff is listening in.

Again, thank you for joining us. I'd like to start by asking Brian Lloyd to offer our safe harbor provision. Brian?

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

Thank you, Fred. I'd like to remind everyone that this presentation contains forward-looking statements that receive safe harbor protection under the federal securities laws. Although we believe these forward-looking statements are based upon reasonable assumptions, they are subject to known and unknown risks and uncertainties. The realization of any of these risks or uncertainties, including the unpredictable effect of the COVID-19 coronavirus outbreak, which is negatively affecting public health, financial markets and global economic activity can cause actual results to differ materially from those currently anticipated. In addition, any forward-looking statements represent our views only as of today, April 23, 2020, and should not be relied upon as representing our views as of any other date. We specifically disclaim any obligation to update such statements.

Please refer to the section entitled Disclosure regarding forward-looking statements in today's presentation for important information regarding such statements. Please also refer to our most recent filings with the SEC for a detailed discussion of the factors that could cause actual results to differ from these forward-looking statements. This presentation also contains certain non-GAAP measures. Reconciliation of non-GAAP measures to the most directly comparable U.S. GAAP measures are included in today's release and presentation furnished to the SEC under Form 8-K. Both today's preliminary earnings release and presentation are available on our company's website.

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

Brian, thank you very much. Ladies and gentlemen, once again, thank you for joining us. A reminder that a slide deck is available on our website, and we would ask you to refer to that if you have interest. We have a lot of financial metrics today. And so I'm going to be relatively brief and discuss some of the highlights that I think you have most likely already read. But that being said, let me start out by saying that we had a positive year-over-year result in terms of our revenues. And I find that extraordinarily rewarding in light of the fact



that we started seeing some early evidence of slowdown in China starting in late January, almost going to 0 by the end of February and March. Subsequent to that, we have seen a rebound of China's revenues as we have moved into the month of April.

We also saw about the last 2 weeks of the quarter, a slowdown in U.S. and I think these are things that you've been hearing from everybody. I think we were hit early with China. However, as we move now into the second quarter, that will be a positive, at least coming back to an area that we felt like we would accomplish in our forecast. I think another advantage that we have, if there is to be one, is that we have had our heads down and arms and legs moving for several months. We've been in the process of reducing expenses, planning on the movement of 14 new products and consolidation of facilities. We've been looking at revenue. We've been looking at inputs, outputs. We've been balancing the expenses along with those revenues. And we've taken a number of steps that would include a reduction in management pay, the use of furloughs while still keep it intact, our sales force because we believe that's an important asset in our company. We have reduced some headcount and those are the things that are not pleasant to do.

Discretionary spending and CapEx and those things, Raul will talk about in just a few minutes. We've also taken and condensed our R&D efforts and also balanced that in terms of some short-term furloughs, effectively reducing the amount of time worked by 25%. That being said, it's important to understand that our R&D pipeline, even though it's condensed, is very full. And at some point, when hospitals are receiving salespeople and things return to whatever the new sense of normalcy is, we believe that these products are going to have a major play in safety and efficiency for physicians and health care workers. We've also been using this time to do a lot of training. As you all know, Merit has a very, very broad product line. And in many ways, that has been very helpful with these events. We've had pluses, and those have been things like peritoneal dialysis, it would be our hemodynamic monitoring and other products that have been helpful in the treating of COVID-19 patients. But we've also had those products that would be so-called elective.

And really, I have to tell you that I never thought that treatment of angina and other types of things would be considered elective, but that's how it's worked. Just yesterday in meeting with the Governor of the State of Utah, he announced that they were opening up elective procedures starting the first week of May. We're hearing that across the board, but anywhere from early May through the month of May. We're hearing it from health care professionals, from administrators and from clinicians. We've been using this time also to train. I think you would all agree, and you're using these tools now that there's a lot of things, and we've learned how to conduct business. I would have to say that in terms of use of Teams, which is on our Microsoft platform, that's been very, very effective in terms of communication, training, and we've trained literally hundreds. I said in my press release, 100, but it's more than that. In terms of the use of doing procedures for peritoneal dialysis catheters, many of those being done laparoscopically and now being done percutaneously and moving over to the IR docs. That's been very helpful. So this time, it has been helpful for us to consolidate our training and our understanding.

Now I also want to just briefly address the supply chain. Over the last several weeks, I've had many calls and many people who have asked, how are you doing with supply chain? Do you see any disruptions? The answer is it's been minimal. One of the things that you're all aware of is that Merit is very much vertically integrated. That includes our molding, it includes our extrusion, it includes our sensors, many of the things that we do ourselves. Recently, I saw a report that indicated that the 24,000 purchase parts. And incidentally, that would be instructions for use. It would be boxing, packaging, springs, coils, all kinds of things. We had only 14 that were in jeopardy, and they were not meaningful to the business. I think just that in of itself is an extraordinary accomplishment.

We also have been able to look at new things. Just yesterday, we talked about our new nasopharyngeal swabs. It was something -- there was a press release out on, and you can read that. Let me just give you a little more color. We were approached by the governor of the State of Utah, who talked about the shortages that they had, and they needed somebody to step up. I presented it to our R&D staff, and within a day or 2, they had developed a plan that would allow us to get into production within 2 or 3 weeks. And as I speak to you today, we are in production. We believe right now, we can produce approximately 10,000 a day. We have an order from the State of Utah, as you have read, for 400,000, but this very day, I've received requests and people talking about another couple of million. Well, it's going to take us quite a bit of time. And although we believe that at some point that this will turn down, will not always be at these levels. This is going to be something that's going to be around for a long time, at least a reasonable period of time.

And Merit believes that we will be able to ramp up over the next few months to 50,000 units a day. And we think that this is a great opportunity. And also, I think, equally important, fills the gap where our employees and where we've seen slowdown in other areas, it fills a gap. And although I never want to say there are advantages to these horrible things that are going on this planet right now. One of the



things that is going to be a benefit to the company is the reduction of the pressure that we've seen for labor. There'll be plenty of people looking for work, and Merit will have plenty of jobs for them down the road. And so there are some things that are -- that help the business. At the same time, it's important for us to help our fellow human beings, and I think we're doing that. Anyway, I think that pretty well covers the things that I wanted to say, and I'm going to turn the time over now to Raul. Raul, you've got a lot of things to talk about, very interesting things.

And so I'll let you pick it up from here.

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

Great. Thank you, Fred. I'll start on the revenue front and then work my way down the P&L. So revenue for the first quarter was approximately \$244 million as reported, an approximate 2.2% increase over the comparable period of 2019 and approximately 3% on an organic constant currency basis. Key puts and takes on these results include FX headwinds of approximately \$2.8 million for the quarter. Peripheral interventions sales were up approximately \$2.4 million or 2.9% from the corresponding period. Driven by our access in drainage product, which saw increased demand, offset partially by decreased sales of angiography and vertebral compression fracture products. Custom Procedure Solutions sales were up approximately \$1.8 million or 3.8% from the corresponding period, driven by our trays and critical care products, many of which saw increased demand due to COVID-19, offset partially by decreased kit sales.

OEM sales were up approximately \$800,000 or 3% from the corresponding period, driven by our Custom Procedural Solutions and cardiac intervention products, offset partially by decreased sensor sales. Endoscopy sales were favorably affected by sales of our AEROMini and EndoMAXX fully covered esophageal stents. COVID-19 impact for the first quarter was approximately \$16 million, which was within our previously given guidance. The negative impact was partially offset by \$6 million in EMEA and U.S. regions that were tracking ahead of plan in Q1 until COVID impacted sales in the last 2 weeks of March. The COVID-19 impact was as follows: APAC impact was approximately \$9.2 million, with China accounting for \$8.4 million, with the remaining balances coming from EMEA at \$1.3 million and U.S. regions at \$5 million. Our revenue contributions by sales division based on an organic constant currency basis were as follows: EMEA, up 15%; U.S. direct up 3%; OEM up 3%; Endotek up 2%; and worldwide dealers down by 7%.

We did roll out our new revenue reporting as disclosed in the press release and Form 8-K. This was filed on April 3, with historical numbers for those that missed it.

Operating margin. Our Q1 operating margin on a non-GAAP basis was 12.7% in the quarter, a 70 basis point improvement over the comparable period. As we discussed during our Q4 call, over the last 6 to 9 months, we have been working on getting leaner, and we saw a \$1.7 million reduction in operating expenses from Q1 over the comparable period. This makes it 2 consecutive quarters with operating expense reductions. The operating expense reduction was offset by a decrease in gross margin of 70 basis points, which was due to lower sales in China, which is a higher gross margin market for us.

Overall, we are pleased with how our operating margin improvement plan is going, and it was nice to be able to deliver continued cost savings. Those cost savings, as Fred mentioned, came from -- principally from our San Jose office consolidation, a leaner R&D process, reduced headcount and lower discretionary expenses, including travel and trade shows. In addition, we continue to evaluate our headcount and footprint to increase our operational efficiencies. We will continue to take that approach as we continue to deliver on our operational efficiency programs in 2020. The tax rate on a non-GAAP basis was 23.8% for the quarter compared to 20.9% for the comparable period. The difference in the tax rate was primarily driven by a decrease in stock option exercise as compared to the comparable period.

On the earnings front, non-GAAP earnings were \$0.38 for the quarter as compared to \$0.37 for the comparable period. Again, we are happy with how our operating margin improvement plan is going, and we believe our results on the bottom line show evidence that our cost control efforts are materializing even with the impact of COVID-19 on our revenue.

To wrap up, let me hit a few balance sheet and cash flow items and some more color on COVID-19 for everyone. Debt balance was \$446 million, and our cash balance was \$50.1 million, putting us at a 2.92 net leverage ratio on an adjusted basis. Available borrowing capacity on a net basis was approximately \$147 million. Our cost of debt is approximately 2.8%. As we discussed, we have given guidance

on free cash flow for 2020 and is an area of targeted improvement for us. We are happy to report that we had free cash flow for Q1 of approximately \$15 million. Working capital was \$297 million. And we do not expect to pay any material contingent payments for the remainder of the year. CapEx for the quarter came in at \$14 million, D&A of approximately \$23 million and stock compensation expense of \$3 million.

A little more color on COVID-19. The decline in procedure volumes observed in the first quarter is expected to continue to create a headwind in 2020, but we are also seeing some tailwinds. Visibility for procedures for the remainder of the year is limited, and we are not able to predict when or how quickly procedure volumes will recover, nor do we expect the tailwinds to outpace the headwinds. Accordingly, as we mentioned in our press release, we are withdrawing our annual financial guidance for 2020. Our decision to withdraw our guidance is centered on the unpredictability, resulting from the volume of data points and wide variations within these data points, feeding into our models. We feel our broad product portfolio is particularly well suited to weather the storm, but we also cannot be precise on the pace of the recovery. Models from some of our markets at more advanced states in the process, give us some optimism as we try to estimate the timing and impact of the pandemic on our operations and financial results. However, we can't predict how long it will take to see the rebound, but we know this is a very fluid situation.

And with some areas of our business down, we also have some areas with higher than normal sales. Having said that, it is our current belief, based on the information we have reviewed, that sales will see a gradual U-shape return to normal through the remainder of the year. However, with the fluctuation in models and underlying assumptions, we are not in a position to make any concrete forecast. As we continue to manage through the impact of COVID-19, and as we start to see some markets stabilize, our models will continue to improve. In the meantime, we have taken the following steps: Continued execution on previously disclosed operational efficiencies, please reference the slide deck for an update on previously disclosed plans, implementing salary reductions for our executive officers and most non-production employees, furloughs for certain sales and R&D employees, controlling discretionary spend across the organization, including travel, trade shows and events, deferring and/or controlling capital and project spend, adjusting manufacturing capacity based on demand, while ensuring sufficient inventory levels to support current demand. And finally, we also believe that given the challenges we experienced in Q2 and Q3 of 2019, that we have a very robust plan on leaning out the business and have been focused on delivering on those plans. We believe this has given us a head start and an advantage in the current situation.

Fred?

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

Well, Raul, that's a lot. And I think the point is this is that, it's not over for us. We continue to work on becoming more efficient and challenging product lines, locations and strategies. So we continue to look at that. But I do believe that with our pipeline and with the interest that we've created, and incidentally, we've done this and provided, as you pointed out, a number of areas that were in high demand, but we've done it at fair pricing. We've not gouged anybody. We have run the business as we always have, and that's with integrity. And I think our customers really appreciate that. So when the time comes when those procedures and things get back to whatever sense that they will, Merit is probably uniquely positioned to take advantage and to have the business grow at higher rates. So I'm really looking forward to the challenge. And I really want to thank the staff, the endless hours. I was joking with someone the other day saying, I need us to get back to normal, so I can get some rest. We start usually at 5 in the morning, we'll go to 9:00 at night.

Everybody has been working hard. Everybody has been planning and thinking and executing. And it's really rewarding to see a team and staff. I think on the free cash flow, to go from a centrally neutral or flat in the fourth quarter, which was an improvement to \$15 million, it's a big swing. And I think that takes attention, and I think we've executed on a number of areas that you will see in this. And yet, we understand that there's this abyss, if you will, that we'll see. That being said, I have absolute confidence in the future of the company, the products, some of the really exciting things like the Rhapsody. There are a lot of things that we have that patients need and that physicians need to treat those patients and make their lives easier. So we want to, again, thank you for your time. Raul and I will be here for the next several hours to clarify things. And we appreciate and support your interest.

And with that being said, we'll go ahead and turn the time over to our administrator and we'll start taking questions. Thank you very much for joining us.



QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Larry Biegelsen with Wells Fargo.

Shagun Singh Chadha *Wells Fargo Securities, LLC, Research Division - Associate Analyst*

This is Shagun in for Larry. Fred, Raul, could you share with us what was the growth that you saw in January and February? Was it in line with guidance? And what was the exit growth rate in March? And I'm also curious to get your thoughts on what kind of growth you're seeing in April and how that has informed your expectation for the remainder of Q2 and the rest of the year? If you could provide any color by segment or geography, it will be very helpful.

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

Yes. So as far as our guidance, we were essentially at or slightly above through February on the higher end of our guidance. So the 5% to 7% on core growth. We were doing really well. And as a matter of fact, as we looked out for our forecast for March, we felt pretty confident that we'd have a strong revenue number. Obviously, the second week of March that kind of tailed off for our U.S. and EMEA regions.

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

I think in terms of China, we talked about a little bit, we started seeing signs of weakness in January. I think the good news is as we enter this quarter, we've seen it rebound. Initially, we were saying 75% to 80%. At least through this point, we're seeing it almost back to normal. But that being said, I was reading more information today about some other things that have popped up in China. So we're cautiously optimistic about China. The Nordics, if we take a look at the Nordics, they've been very, very strong even through all of this. And of course, the biggest concern in our biggest market is the U.S., and that's why I think we're -- we'll look forward to watching the pace in the release as the procedures come back online. So that's kind of the best we can answer your question. But thank you very much for that question.

Shagun Singh Chadha *Wells Fargo Securities, LLC, Research Division - Associate Analyst*

If I could just follow-up. Can you give us directional color on the impact by business segment, which ones do you expect will be hit more materially? And where do you see increased utilization or potential offsets? Any range there would be helpful.

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

I'll really just talk more about the areas. I think our critical care business that we talked about has been very, very busy in Singapore. I think we have seen segments or products in our peripheral group where there's a lot of demand. Most of those, though, associated with hospital wide types of needs as well as our infection control product. So I think all of those areas, collection, drainage, pericardiocentesis, and they kind of go across a number of the product lines, some of them in the cardiac area, some of them the peripheral. But again, not enough to offset the -- some of the declines in the procedures. Then OEM has also been very strong going forward. So that's the best color I can give you right now. Thank you very much.

Operator

Our next question comes from Mike Matson with Needham & Company.

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

I guess, first, I just want to ask about kind of what you were seeing in the last few weeks of the quarter. I know you quantified the impact. And I want to make sure I got the numbers right here, but I think you said that the COVID impact for the full quarter was \$16 million and that there was about \$9 million of that in Asia Pacific. One -- just over \$1 million in Europe, EMEA, I guess, and then about \$5 million in the U.S., is that right? And then is it safe to assume that the EMEA and U.S. impacts were pretty late in the quarter, kind of, in the last few weeks, in particular?



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

Yes. I think that's a fair statement. We started seeing it tail off. Usually in Europe, you have -- after the first of the year, you have a little bit of a slow start-up as well. So it's a little slower to start, started gaining some momentum. And then, of course, we saw the fall offs. It's kind of a sequence of events. Raul, do you want to add to that?

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

Yes. It was really in the last 2 weeks, I'd say, of March. I think on a net basis, really, the impact was about \$10 million. So we had some areas like EMEA, OEM, U.S. Direct that were doing really well through February.

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

Okay. And is there any way -- I mean, I guess, just in terms of modeling the second quarter, should we kind of look at those impacts and try to look at the run rate you were at the tail end of the quarter and project that into the second quarter? I know you're not giving guidance, but I guess I'm just trying to figure out what you're seeing kind of what you were seeing from a growth perspective at the very end of the quarter and in the early part of the second quarter, if you can comment on that? I understand that it may or may not last through the entire second quarter, though.

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

Yes. Mike, listen, I think we want to stay on track in terms of what we said. I think what we did see, and I think the more important part of this is what we saw at the beginning of the year prior to this falling off the strength in the business. And then we saw the last couple of weeks. So I think we don't want to wander up and I think our statement stands. I'm not trying to be evasive, but like you trying to figure it out, we're trying -- not just to figure out, but we're watching things every day and watching softness here, strength there. It's unlike anything any of us have ever seen. I mean, we get to see it on a day-by-day basis. But I think we're just going to have to stay with our previously -- our statements that we've made, just stay on track, so we don't cross into FDA issues and things that we shouldn't be talking about.

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

All right. That's fine. Fair enough. And then just had one on Rhapsody, and then I'll let someone else get on. So just with Rhapsody, I think you're expecting a CE Mark this year potentially, so can you talk about your confidence in that? I mean, can you talk about the market opportunity, maybe the size of the potential market, both in the U.S. and in Europe. And then you adjust the competitive landscape there, are there any competing products? I think Becton Dickinson has a stent graft called Covera, I didn't know if that was a direct competitor or not.

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

Yes. Thanks, Mike. Listen, we believe that the Rhapsody is the most exciting product that Merit has ever had. It's taken us 7.5 years. We've conducted a first-in-man study in Europe, very successful. We are just weeks away. And when I say weeks, 1 or 2 of submitting our application for an IDE with the U.S. Government than they've worked, and you've seen the breakthrough designations that we have. In terms of the CE Mark, we believe that we have -- and we have, in fact, submitted all the documentation that's required, answered questions. And we believe that our product will be going to staff within a week, and we'll be going to panel in the next few weeks. So it's possible that we could have the CE Mark sometime in May. Now as you know, everything in Europe, they've moved some things out with MDR, and there's this and there's that. There are just a lot of unknowns. I think we're confident in the data. And we're confident in the process.

So we think it's a big deal for the company. And rather than just talking about the initial indications, which are important. I think it's really talking about the technology and its broad use initially in the outflow circuits for dialysis patients and the central veins. Those are areas in which we have some indications that others do not have. It does compete with Covera. There are some other products, but nothing really quite like this. And I believe the data will show and at the appropriate time, that will come forward, that it is a product that we believe is superior to anything in the marketplace. And there's a lot of reasons for that. But all that being said, we think that this will come, hopefully, in the next 30 days or less. Now that one of the other questions that will be very interesting is that the access, both in starting up the trial, we've been working during this period of time of getting all of the work done of



(technical difficulty)

So that's one of the things this has allowed us to do. But we have inventory. We're ready to go in Europe. If it's not in Europe, then we're ready to swing. And we can run both of these simultaneously going forward in terms of both the European release, which then will also lead to other areas that we will file on in Canada, Australia, and I think we're already approved in New Zealand. So I think we have done everything that we can -- we'll just sit in cross our fingers for the next few weeks and see how that shakes out. The much bigger market, of course, is in the -- on the peripheral side and when you start talking about iliacs and some of the areas that we're talking about. Those are just great opportunities. The market size depending on who you talk to, and I'm just talking about on label use now, \$100 million, \$150 million globally. One of the things we tried to do, Mike, is when we went into this, we wanted to go in and get to the market the fastest way we could and develop the technology. Even that took 7 years.

So it's been a long time, and we're looking forward to the business. And depending -- we should hopefully will come out in a very specific layout markets strategies, those that we can release will talk about separately into a press release and a conference -- press conference, the days shortly following the approvals, and we'll make those announcements should they come. Now if they don't come from Europe, then we'll -- we're ready to start the IDE and then work towards the PMA approval. So we're on track. We've built all that product right here in Salt Lake City, and it's very exciting for the future. The technology, the broad area of the technology is something that we'll be doing for many, many years to come.

Operator

Our next question comes from Matthew O'Brien with Piper Sandler.

Matthew Oliver O'Brien Piper Sandler & Co., Research Division - MD and Senior Research Analyst

Fred and Raul, can we just start with Utah specifically? I know it's a smaller U.S. market, specifically from a state perspective. But you based there, you've had this conversation with the Governor yesterday about opening things back up. I think the moratorium on elective procedures started roughly a month ago, I think it was March 23. So can you talk about what you saw? I mean, is your elective business down 70%-, 80%-ish in the first 3 weeks of the quarter, expect things to maybe stabilize a little bit next month? And then maybe get back to a little bit of growth in June? Is that a fair way to think about how the quarter can kind of play out just in Utah alone?

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

Yes. I said that I would kind of stay on track. I would tell you that I saw the very same things that many saw in the Johnson & Johnson and some of these other reports. Our business is not seeing those kinds of declines or anywhere close to those. Raul, I'm going to let you maybe talk about this, so I can stay out of trouble, but then you can get yourself into trouble.

Raul Parra Merit Medical Systems, Inc. - CFO & Treasurer

I'll give you guys some color because I think I'm going to try and dance around this a little bit, Matt, because obviously, we want to make sure that we don't -- the reality is that there's a lot of variables, and I'll get into those here in a minute. But I think if you look at our OEM business, which is roughly 10% of our business that seems to be stable. Okay, so you can pull that off the table from whatever you projected for that. I think the Nordics is around a \$20 million business for us. That seems to be either stable or just a little bit above what we forecasted. So that's stable business. China, you guys know, is about 11% of our business. That seems to be coming back a little bit, right? But Fred mentioned it. There was news today that maybe things are picking up again. So that's -- and I think the hard part about this is that you've got China, which gives us a very good footprint of what to expect. The problem is that the rest of the world is not going to act like China, we don't think because, one, the government in China can force certain narratives and certain processes. What you have with the rest of the world is that you've got individual countries at different parts of the curve. You've got different states here in the U.S. at different parts of the curve. You've got countries and states that have different policies. And then you have the added component of patients and how they're going to react to either, a, not wanting to go to the hospital or going to the hospital. And so, it's just -- there's just a ton of moving parts. And so it's hard to, kind of, give you anything more than that.

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

And, Matt, we've had a lot of calls and a lot of people or everybody is asking the same questions. I made a comment, and I believe this. I believe our business will respond faster than others. And the reason I say that is because there's not the orthopedic part of it, no offense



to my orthopedic friends. These are things that have been growth areas. Our peripheral business has been the strongest area, and many of those IR docs have been pulled down into critical care or emergency room care. And many of those are coming back on. I was talking to a physician back East, who is going to be back in his lab next Monday. It's just the pace of working the patients up. And very candidly, it's like a football team or basketball team that hasn't played for a couple of months. And it's going to take time. But I think in terms of our product, our mix, our breadth and our geography that we, in my view, will respond probably, at least -- again, this is my own opinion, but I believe that will respond in faster than most, it's just our belief. So I don't know if that does answer your question, but that's the best I can do.

Matthew Oliver O'Brien Piper Sandler & Co., Research Division - MD and Senior Research Analyst

No, it does. But it also dovetails into another one that I had, which is just you might kill me for asking this, but just people are trying to get a sense for what '21 is going to look like coming out of this. And so is it fair to say because of the breadth of your products, because of the geographies and the dispersion there, that '21 most likely will end better than '19 -- excuse me, 2019 did. Is that a fair way of kind of thinking about it?

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

I'm just going to stick with my previous statement. Merit will rebound. Again, the other part of this is we have a number of new products that were launched in January that didn't get launched. So we have all of that. We have the OEM part of it. We have the critical care. We think it's going to continue to grow. We think these other procedures will come back. And then we've been continuing to work on our R&D projects and focused on bringing more things to the market. So we're loaded, and we've been using the time as we talked about, to train, but maybe equally important, one of the other things, and I know we've said peritoneal dialysis, but there's a lot of interest out there from physicians and the President, prior to this, had talked about how he wanted to move and have, I think, 50% of procedures in dialysis by 2025. We're seeing tremendous interest in training and very candidly, revenues in these areas. So I think that you're going to see this company rebound faster, leaner, and I think what we try to do is protect the sales force.

One of the questions will be, well, what is the sales force? And are they going to have access? And are you going to be able to do these things? I think the things that we've learned is of the training that we can do online. And by the way, when we talk about that training, we're talking about physicians training other physicians online. And we had one today, where we had 150, and this was to do pericardiocentesis, which is one of these factors as a complication of COVID-19. So this has taught us a lot. It's also created a lot of opportunity. There'll be a lot of products that come out of this that we've already developed. One of them is the swab in the test kits. That's going to go on for quite some time. That's not over. And there's not been much question on that, and that's fine. But it's -- there are a lot of things that are really -- Merit can respond to very quickly.

So Matt, my expectation is I can't specifically say what I'll do, I'll just say it's my belief that it will be faster than most and that we have a full pipeline of products. And I think we've used this time very effectively with our sales force while keeping them intact. But at the same time, reducing the expense, and that was through having a furlough. And so, we've run that, I think, very effectively, where we've only furloughed half of our team for a week, then -- I won't go through all the details, but we've reduced the cost by about 25% while using that time to train and to get ready to get back out there as soon as we're allowed to. So that's the best way I can answer that.

Matthew Oliver O'Brien Piper Sandler & Co., Research Division - MD and Senior Research Analyst

That's very helpful. Can I sneak in one more for Raul, real quick?

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

Sure.

Matthew Oliver O'Brien Piper Sandler & Co., Research Division - MD and Senior Research Analyst

Just the free cash flow number in the quarter was great to see. I just -- I know, Raul, you did make some comments about the full year projection pre-COVID, I wasn't sure if I caught what you said during the script as far as what you think free cash flow will look like this year. Are you still expecting I think it was the \$40 million to \$50 million range this year even with the COVID impact?

Raul Parra Merit Medical Systems, Inc. - CFO & Treasurer

We're not going to give that color, Matt. I will say that we're in -- we've got some initiatives in place that we talked about. And we were excited about the \$15 million, and we'll just leave it at that.

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

Well, but I will say this, we made improvements from third to fourth quarter. We brought it back to neutral. We were able to bring \$15 million worth of free cash flow. And I think under normal terms, you will see the things that we put into place will help. Now the question becomes a lot of other parts of the business that is difficult to predict. But I think the initiative and the momentum that you're seeing is something that we would expect to continue. I mean it's what we get paid on. It's what we're looking at, and we're spending our time on. And more importantly, it's the right thing for the business. So I just think -- hope that you'll just look at the momentum that we've created and what we've done to turn that, I think, speaks volumes.

Operator

Our next question comes from Jayson Bedford with Raymond James.

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

I hope everyone is safe and healthy. I have a couple of follow-up questions and then a more original question. But just on China in the ramp, at what point do you think China will be flat on a year-over-year basis? Is that some sign in 2Q? Is that a 3Q or 4Q event?

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

Well, that's a tough question. I don't know that I -- what I can tell you is we saw it fall off, as you know -- and what were we to forecast for the first quarter, Raul?

Raul Parra Merit Medical Systems, Inc. - CFO & Treasurer

Well, we were down year-over-year, we were down about 17%.

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

17% down year-over-year. And then what we're seeing as we start this quarter and here it is the 23rd that we're at forecast. So we've come back, and that forecast would have been above neutral. And we're seeing that now. We're also seeing that the rest of Southeast Asia has not come back to that effect. That's probably at 50% at this point, but starting to come back. We're starting to see Taiwan, Vietnam. But some of those other places just haven't started ramping back up yet. So -- but the big number is China. And that has ramped up. And there's one other part of China, our business there that's really interesting. And that is -- and this is -- well, I'll just blurt it out. And that is our critical care business has not been a big factor in China. But what we have seen is an example, one of our distributors over there orders about 5,000 of a product at \$20 a quarter. Just 2 or 3 weeks ago, that very same distributor, again, this is just one data point, ordered 60,000 units at \$20. So I mean, that's a huge delta to go from 5,000 to 60,000, in order of magnitude.

And so we think there's some other things that are coming out of China for the long term, they're going to be to our benefit in our critical care business. And these are products that are better than 50% gross margin. Even though they're coming out of our critical care division, which is generally lower margin. So there's a lot of things that we see positive. And maybe one of the more -- another little subtle point is particularly in the treatment of HCC. We've seen a huge upsurge, which tell me that there was a lot of pent-up demand for drug loadable embolics, which are approved in China. And we've been seeing a big upswing in that treatment, which tells me there's a huge backlog of patients that have to be treated for HCC. And that's one of our most, if not our most profitable product in the company. So those are all kind of the positive signs, Jayson, we see in China.

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

Okay. That's helpful. When we look at the 5 reported segments in your revenue line, in which segment do you expect to see the biggest impact from COVID? Is it -- is there one division that we're going to see more of a hit than others?



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

Yes. That's in the endoscopy. And that's because it's elective, but it's also the smallest part. So that's one that was up in the first quarter is going to be down. It's going to probably be the biggest one just simply because it's one of those where they just shut that whole thing off. So it's not zero, but it's the one that will have the biggest. But in terms of impact on the business, it will be the smallest impact of any of the groups because of that. Raul, do you want to talk maybe about the others, if you have some thoughts there?

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

Yes. Just maybe a little bit more color. So as we mentioned, OEM seems to continue to be staying in the fight. Custom procedural solutions, as Fred mentioned, we're seeing demand in that area. And then we've got takes and puts in CI and PI. So -- but obviously, the headwinds there are not going to -- they're not going to outpace the headwinds -- they're going to be outpaced by the tailwind, so I mean that's just...

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

So yes, I mean, we're going to see -- listen, there's no question, I think, from anybody that's in the industry, you guys know this, you've been listening to everybody. Those areas are going to be down, but they won't be down for very long, because we're at the point now where they're going to come back. So we expect to start seeing probably in June. I know people are saying May, but it'll start-up in May, but I think it will be rather slow as they get back into gear and they loosen up their arms and start going through spring training, so to speak. And then we expect that we'll see a pretty dramatic increase. I will say this. We are hearing -- these are administrators, hospitals talking about procedures being at 125% to 150% of normal. We're getting phone calls from customers saying, are you ready for this?

Now I guess the next question is, do we believe it? I don't. I believe that it will resume, I believe that there'll be those things. I just think it's going to be a little slower. I don't expect to see 125% or 150%. But it is interesting to see customers call and ask us if we're ready. I think in my prepared comments, one of the things I tried to talk about, we've sized the business for what we are doing. But because of the really unique nature of this company, and its vertical integration, our supply lines to be able to respond to this are really, really short. We do our own molding. We do all the things -- a lot of things ourselves and our ability to get back to full speed or above that very quickly is, I think, something that gives us the confidence that we'll have a faster rebound than most because of our ability to respond to it.

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

Okay, okay. That's all helpful. Just last quick one from me. What's the timing on the transition to Mexico for the 14 products? And then just similar, the consolidation of the 4 facilities?

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

Yes. So we believe that, that will be through the balance of the year. So we have some things moving this week. We have things moving from Salt Lake, from Melbourne, from other locations. So the 14 are things that we've talked about through the year. Now someone said, well, with all this, can't you accelerate those? And the answer is, we have less people today, we have a lot of other things to deal with in terms of just internally with safety for our employees, for sizing the business and so on and so forth. So again, our statement, I think, has been very consistent. It's for the balance of this year.

All of the 4 facilities, I think now the decisions have been made for 3 of the 4 and are in process and will be completed. One of the facilities, which is probably the smallest one in terms of the impact is one that we are planning on producing our testing swabs and kits. And depending on that demand, it may stay open a little bit more, a little longer. But I think we have that lease that's through for about another 6 months. So we could still either move that into an existing facility. It's unique and it's manufacturing because of bristols and this and that. So the point is you'll really see all of that in 2021. You'll see that some of these things will have a big effect, though, we think, on both gross margins and our expenses. So we think the decisions that we've made will help make the business much more efficient going forward. But it really is still on the original plan. It has not accelerated, but it has not slowed down. And our plan, I think the message has been very consistent. Raul?

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

Yes. I mean, we're on pace...



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

We're on pace.

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

I mean, I think our slide deck kind of says that, and it's one of the things that we continue to focus on.

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

Now was that the original question, Jayson? You said you had an original question. I didn't -- was that it?

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

It hadn't been asked, and so that's what made it original.

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

Okay.

Operator

Our next question comes from Steven Lichtman with Oppenheimer.

Steven Michael Lichtman *Oppenheimer & Co. Inc., Research Division - MD and Senior Analyst*

Just one clarification and then just 2 quick questions. Raul, I think you mentioned a \$10 million figure for impact during 1Q. Was that the worldwide impact of COVID in sort of the last part of March? Is that what you were referring to?

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

Yes. I mean, the COVID-19 impact is \$16 million, but the business was doing pretty good through February. And so on a net basis, it ended up being about \$10 million. But I guess what I'm trying to say is that we were on pace to do a \$16 million more, but because of COVID-19, we weren't able to get to that. So we were able to reduce it by about \$6 million on a net basis.

Steven Michael Lichtman *Oppenheimer & Co. Inc., Research Division - MD and Senior Analyst*

Okay, okay. Great. And actually, that dovetails to my next question, which was, and I apologize if you mentioned this, but what were some of the lines that were running ahead of plan, if you could talk qualitatively, what were some of the things that were going better-than-expected as you march to the first couple of months?

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

Yes. If we look at our -- again, our critical care business, which would include our hemodynamic monitoring. These are products that are used in ICUs to measure blood pressure. Whenever you see the pressure wave forms, those are because of these products, things like our pressure infuser bags. These are the things that we build in Mexico. I would say that business is probably up 50% to 70%. It's a small -- when I say small product line, it's under \$10 million, but it's a nice profitable product line. And even today, right where we are right now, not just in the first quarter, but as we're moving forward. There -- that business continues to increase. And we're getting large orders from the National Health Service in Great Britain. We have a number of countries. And these are being -- these are pretty good-sized orders, 25,000 units, 40,000 units, 10,000 units. And this is for a product that's about \$14. And but it's a nice product. And then you take a look at peritoneal dialysis. I talked a lot about that. That business has got to be approaching 25% to 50% above -- probably closer to 50% above of our previous sales levels.

And again, something that we'll continue to see. I think what this does is kind of give a jump to an initiative that was already in place to move in that direction. And I think with the training of the physicians to do it percutaneously rather than through laparoscopy. By the way, the reason they did that is you could do this in a cath lab and you could send the patient home without an overnight stay, and then you can do dialysis at home. Think of all the advantages of that with no higher morbidity or mortality. So when you start thinking about, this is something that probably should have been done a long time ago. I mean, places like Thailand or Canada in some of the places, 80% of all the procedures are done, and this is a product line that Merit produces totally in-house and one that we'll continue to see. So those are the 3 that come to mind or 4. Raul, do you have anything else you want to add to that?



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

No, I was going to say access, products, drainage, you covered.

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

Yes, drainage. There's another one. Like I said, pericardiocentesis, any of the centesis again, you've been reading about all these complications that come from COVID-19, and there's a lot of our products there that have accelerated because of that need. We had one customer who's one of the larger medical device companies that increase their orders that we produce for them by almost 50%. So things like that have been very helpful to pick up some of the slack in some of the elective procedures.

Steven Michael Lichtman *Oppenheimer & Co. Inc., Research Division - MD and Senior Analyst*

Great. And then just last quick one. I know, obviously, not providing guidance, including on free cash flow. But can you talk to your CapEx expectations? Obviously, that's a little more controllable in this environment. How are you thinking about that relative to your prior thoughts?

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

Well, I think we're definitely looking at it, right? Just from a liquidity standpoint, making sure that anything that we can defer or things that are just not high priority right now. We're either pushing them out or really just kind of stopping them. So I think we're definitely going to pull back on CapEx where we can. But again, we've got certain products that we just feel that we need to invest dollars in. And from a long-term perspective, we're not going to cut in those areas. But to the extent we can, we'll push things out.

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

Let me maybe give a little color on that, too. So as you heard us say that in our R&D projects, we have condensed those, and we've reduced the amount of labor that's going to those by 25%. So we probably cut the number of projects across the board by about almost 50%. And now please be reminded that these -- when I say 50%, we just -- we're focusing by putting more resources on less products, but that means that you don't have all those other capital expenditures for all the others. And then you pull back on the time, and there's just one area. And then you also find when you go through these things, which I think is helpful, like all of us has found out, we can all do more with less. In every aspect of our businesses and our lives. We've all learned that.

And as Raul pointed out, and as we've commented, we kind of had a head start on this. We started working on this last year. We stumbled. We -- and everybody knows the story. So we've had our heads down. And so some things that -- and again, I'm not picking on others. I'm just simply saying that some people are just getting started on some things, these are things that we were well down on the road and had in place or were initiating months and months ago. So it was just kind of -- it wasn't unusual or shocking. We just -- I think, it was to our advantage, and I think you'll continue to see that as we move through the year, that we've done the things that needed to be done. There's more to be done, and we will do that as well.

Operator

Our next question comes from Jason Mills with Canaccord.

Cecilia E. Furlong *Canaccord Genuity Corp., Research Division - Associate*

Fred and Raul, this is Cecilia on for Jason. I was hoping, Fred, maybe could you provide a bit more color just around your decision-making process that you thought about R&D? What you're prioritizing? Maybe not specifics, but just on a generalized basis, what you're prioritizing today? And how you're thinking about this in light of your expectations for '21 and going forward?

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

Yes, Cecilia. As you know, one of the commitments that Raul and I made was to leverage all aspects of the income statement. In the past, we've essentially utilized all of the increases in sales would be the percentage that we would hand over to R&D. I think as we look at it and thought about how are we going to -- we can't do those things and get leverage particularly on that top line, if you're not getting the leverage on the gross margin, what would you do? And so we really made a commitment that all the way through. Gross margins, you'll see those. And in fact, I think it is important to point out that despite all of this, we saw sequentially a 20 basis point improvement from the fourth quarter to the first in gross margin. But I think we looked at all of those, and we put a specific plan together in the SG&A side



and the R&D as well as up on the gross margin side, say, what about manufacturing efficiencies? What can we do to cut costs here? And our commitment was is to improve operating margins and profits. And in order to do that, we had to hit all of these. So that's what we've done.

And again, we've been doing it now for several months. And we continue to do that. It's, by the way, painful but necessary, and that's what we've done. I think in terms of what priorities that we have, again, at any given time, we kind of sit down and look at the projects and say, okay, what's hot and what's not? What's changed from our original thinking? What's coming in? What's going on? Data changes, like, for instance, again, I'm sorry to have to be so redundant on things, but like the centesis product. We have 2 or 3 centesis products in R&D. The reason that's important is we think that's an area that's going to continue to grow. And in fact, it has. So we try to take a look at what will the world look like and what will people focus on going forward?

And I think those are the areas we say that, look, learning from this, looking at the previous trends and what -- I'll give you an example of one. Anything that aerolises into the air. In drawing out a sample of fluid, close to systems that you can prove do not hit the atmosphere and will protect the health care worker and the patients. It's pretty important stuff as we are all reading and hearing every day. So we have products like that and things that we would accelerate or that we would put more focus on that because we think, again, not only do we think those products are going to be demand, but it's what it does for health care workers. It's what we hear every night. It's what we know as a great sacrifice. These are great heroes all over the world. We've got to do more things that protect them and the people that are around and working in hospitals. So I think those kinds of things, that's not just a trend for now. It's going to be a trend forever in the future.

What are we doing? How are we doing it? And how can we improve to minimize risk to people around there. Again, with all of these folks helping us and treating us, it's not going to be a fun picture. So I think that's what we have spent our time is really focusing on areas that we think are going to grow. So infection control, our caps, other areas that we think there are products that we have in development are the things we're spending time on because it's not just about COVID, it's about the next COVID. It's about the next thing. And what have we learned from all of this, and that's what we're working on. So that's how we've looked at this. What's safer, more convenient, what gives you better results? I mean, I know that sounds maybe pretty primitive, but it's -- I think it's allowed us to stop and say, okay, why are we doing this? What result? And how does this fit? And does it fit with the new mantra that we see? Again, this is not the last time that the human race will be affected. We saw MERS. We saw SARS. We've seen COVID-19, and there's just another one just around the corner. And I think those are the kinds of product, safety products, those sorts of things that will help us to grow the business and provide the great services that we hope to do.

Cecilia E. Furlong *Canaccord Genuity Corp., Research Division - Associate*

But your comments dovetail kind of into my next question, which was you talked about a few times on the call, getting back to a new normal, whatever that happens to be. And I just like your perspective on what does the hospital landscape or rep access or treatment sites? What does the hospital landscape look like coming out of this period? And I know you just commented on a few components, but just as you're thinking about structuring your business today for the future, what are the key areas you're focused on?

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

I think it's preparation. I think if we look back today, and we look at how everybody is hustling to get these products that are not necessarily complex but is streamlining both states federal government and hospitals to be in a better position to respond to these sorts of things. I think we've all looked at this and said, why -- and again, this is what you're hearing on the National news. Businesses are going to come back to America. Companies are going to produce more and be maybe less concerned about getting something offshore or cheap to get something that you can respond quickly that you have short supply chain and provide the needs. So I think that's going to be part of -- I've got a lot of people, we're hearing administrators talk to us, and we're starting -- people are already talking the medical association, for instance, had a meeting through our professional associations with MDMA and people are talking about what would we do differently than we did? And it's not about finger pointing or blaming. It's just take the facts, look at them. And then what are we going to do in the future?

So I think one of the things you will see are more supplies, more reserves, more preparation is what I'm hearing. Now will it change disease states and those sorts of things? I don't think so. The question then becomes, like we're seeing now, orthopedics and what's



necessary and what's not necessary. So I think there will be a lot more scrutiny on -- if someone has -- and again, a lot of people have bad knees or a bad hip, but is that going to be where the health care system is spending their time and their resources, I think it's going to be on more diagnostics, more testing, more preparation and then more safety. I think that's where Merit's looking at. And every product and everything we talk about kind of focuses around, does it meet the needs -- we call it a user spec. What does the user want? And our job is to meet those needs and to identify them. And I think that's where we're going to spend our time.

Operator

Our next question comes from Mike Petusky with Barrington Research.

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

Raul, on the CapEx commentary, you said sort of pulled back. You guys did \$14 million in the first quarter CapEx. And you sort of said, I think \$20 million to \$25 million down from last year's \$78-ish million originally. When you say pull back, you're talking about pulling back from sort of the current run rate of \$56 million? Or are you talking about just you're pulling back from \$78 million to sort of mid \$50 million as was already planned?

Raul Parra Merit Medical Systems, Inc. - CFO & Treasurer

Yes. I mean, I think we gave guidance on CapEx. And so I think one of the things that we saw during the Q1, we did have some building costs from the building we were finishing out. We'll have a little bit of that coming into Q2. But again, I think it's too early. I think we're trying to -- we're pushing things out right now. And as we see what happens in the business, we'll decide how we treat that original guidance on CapEx.

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

Okay, but when you say pull back, is that commentary relative to your -- I mean, the sort of the guidance of mid \$50 million? Or are you saying that's what I'm trying to get at. I mean, is there downward likely -- I guess, is it likely to be less than the current run rate?

Raul Parra Merit Medical Systems, Inc. - CFO & Treasurer

Yes.

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

Okay.

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

I like the way you did that, yes.

Raul Parra Merit Medical Systems, Inc. - CFO & Treasurer

I had to think of it.

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

Okay. And then in terms of...

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

Mike, can I jump in for a second. One of the other things that we are doing here is we are running monthly meetings on CapEx. And it's not just, let's see where we are at, "Oh, my gosh, we went over." We are looking at each decision, each month, where we stand against our budget, what we're going to push off and what we're going to do to make sure we hit our numbers. So I think the way that we're approaching it is dramatically different than what we've ever done in the company's history. So we pull all these things up. We look at the products that are online and the things that demand capital. And if something pops in, then something has to pop out. So I think setting the priorities is very important. I think we've been doing that to have the discipline, more importantly, to have the data so that we can make sure that we know where we are. And I think that's been a big improvement in our thing. And the other thing, listen, so many people are focused on the day-to-day work, keeping people healthy. And all of our facilities are producing. We know we're an essential provider.



But we've had to do a lot of things for division and safety and separation. So a lot of the other things that we might have done are being deferred, and a lot of these or a lot less. So I would agree with what he said is that we're just not in the mode of big grandiose we're going to live with what we have or less. And that's kind of, I think, the theme that we've been working on for some time now. When I say sometime, we've spent a lot of money to build this business, but I think we're just doing the things that we need. You think about our lives. We're out there. When we used to need to go do this, and we used to need to go do that. Well, none of us are doing that anymore. Are we? We're not going to the dry cleaners every day. We're not going out to dinner. We're not doing this and going on. We're doing things differently, but we're doing those things in the business as well.

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

Okay, great. Raul, I guess on the free cash generation, which was excellent. Was there anything sort of unusual in that number that benefited you guys that was sort of a timing you really caught some favorable timing on a collectible or some kind of AR? Or can you just speak to that?

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

Well, receivables helped us. Obviously, we're managing. One of the metrics that we put out there when we were forecasting our free cash flow was our working capital and receivables and payables. So we benefited from receivables collected from some customers in the Middle East specifically, saw large dollars flow in from there. So...

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

Was there a really unusual element to that or one big...

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

There was no unusual elements, I would say.

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

Okay, okay. Is there any -- just for consideration, if there's any way you guys can put in cash flow statement in your news release that would be awesome if you consider that.

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

Okay.

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

All right. And I did want to ask about the \$3.9 million impairment. Can you just sort of walk us through what that's all about?

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

Yes, that was just a -- it was a purchase option that we had in place. Obviously, under the current circumstances, we didn't think it was the right thing to do. And so obviously, from an accounting perspective, you have a value assigned to that purchase option, and we walked away from it.

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

All right. And then just last one for Fred. Fred, I think you alluded to your -- and nobody has a crystal ball, and I know you're not absolutely projecting this, but your gut tells you that you see sort of a U-shape recovery and then some commentary that you've made during this call seems to indicate that your view would be that maybe the bottom of that U is sort of late second quarter. Is that a fair characterization of your thinking?

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

Yes. I think that is fair. Because here we are -- April is done, here we are -- as we move into May, we'll start to see procedures come back online. You'll see -- I think, Raul, he's over here grinning at me. So I have to -- he calls it the Nike swoosh. I'm going to go ahead and say it's kind of like that. It will come back up. And then I think we'll see. Interestingly enough in the summer quarter. That's the interesting part of this because historically, it's always our slowest quarter. People go on vacation, and people do this and go to beaches and everybody checks out. I think it's going to be a little different this year.



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

Maybe the folks in France will actually stay in the office in August.

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

Yes. They have been -- yes. Well, let's not pick on the France. We have a facility there. So I'll be getting -- we're going to say, you got to stop Petusky, not say things like that.

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

Sorry. That's me. They can call me with their complaints. All right.

Operator

Our next question comes from Jim Sidoti with Sidoti & Company.

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

Quick question on the collection kits that you announced earlier this week. Are those specific to any manufacturer's device? Or are those good for any of the diagnostic systems that are out there?

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

Yes. No, this will work in anybody's diagnostic system. There are many of them that are out there, too, including the Abbott system. There's -- this will work with any of those. And again, we just think it's an opportunity that will be around for a long time. There'll be a lot of testing going on for a long time.

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

And you said you have one order already with your state, but are you talking with the other 49 states about this?

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

Well, one of the things you always got to be careful about is my commitment was to the state of Utah and to the Governor. And he's the guy that came to us and said, we got to have these, and nobody else can get them here. Can you help me? And I sat down with Jim Mottola, R&D and his team, and we sat down and we said, yes, we can help you. And we worked with a state lab and a whole bunch of folks, and you saw the order. By the way, Jim, this is all taking place in 3 weeks. So that's how quickly we've responded. We'll be producing starting Monday. What we're producing today, 10,000 units a day, 50,000 units a day within 30 days. So that means that in -- to fill an order of 400,000, that's 8 production days. So we will have capacity and opportunity, and I'm getting calls from everybody in the country. It's amazing to me. And it goes back to one of the questions that was asked by one of our folks earlier about what do you see differently?

And one of the things you will see, you'll see a lot of more of these supplies that will be stationed, so people can respond to this. I think you'll never see a shortage in PPE or in some of these things, again, because people respond, you may even have overcapacity, that pendulum will swing. Anyway, there's a lot of opportunity there. And we'll just -- I want to make sure that just saying that we're going to go do this and go do that. I want to get this order done, measure where I am, and then I'll start talking. I'm talking, they're calling me every day, I had a call from Texas, one from Pennsylvania, one from Ohio, one Nebraska, Idaho, I could go on and on. I mean, that press release hit a lot of people, and there's a big need out there. And it hasn't been filled. We'll be -- hopefully, that we can help. And it's one of those products, Jim, that makes a difference. It's a big deal. You're helping a global cause. And so the answer is there will be a lot of opportunity. But as it presents itself and we can meet it, then we'll talk about that kind of after the fact, not in front of the fact.

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

All right. And then last one for me. You -- well, you said you are at around a 2.9 leverage ratio right now. Are there any covenants that you're close to at this point?

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

No, no. We feel pretty comfortable where we're at. And yes, we feel good.

Operator

I'm showing no further questions in queue at this time. I'd like to turn the call back to Mr. Lampropoulos for closing remarks.

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

Well, Liz, thank you very much for your help today. And to all of you, thank you for your time. Interesting times. We look forward to -- when we have some visibility, we'll come back and we'll talk to you, and we'll keep you up-to-date just so that you know that we are deeply engaged every day in this business, and we have a great business and one that we're very excited about looking forward. So we'll get over a few bumps that everybody is going to hit, and we'll go from there. Thank you for your attendance. Raul and I will be around for a few hours. And we look forward to your calls and clarifications. Bless you all, good health. And good night. Thank you.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.

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