

Integra LifeSciences (IART)

\$60.51 (As of 02/20/20)

Price Target (6-12 Months): **\$64.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 03/04/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: B

Growth: B

Momentum: B

Summary

Integra exited fourth-quarter 2019 on a mixed note as its adjusted EPS beat the consensus mark but revenues lagged the same. The CSS segment benefitted from integration activities from the Codman acquisition, and venturing into faster-growing markets like China and Japan. Global sales in CSS in the fourth quarter were led by core neurosurgery portfolio, including product launches, strengths across Europe, and robust growth in China and Japan. Global performance in OTT is expected to improve due to benefits from the combination of new products. Expansion of both margins is encouraging as well. The 2020 guidance for organic revenue growth and adjusted EPS appears strong. Overall, Integra has outperformed the industry in the past month. However, weaker sales in outpatient settings and the effects of supply constraints in the reported quarter are concerning.

Data Overview

52 Week High-Low	\$65.09 - \$46.07
20 Day Average Volume (sh)	576,209
Market Cap	\$5.2 B
YTD Price Change	3.8%
Beta	1.14
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Medical - Instruments
Zacks Industry Rank	Top 29% (73 out of 255)

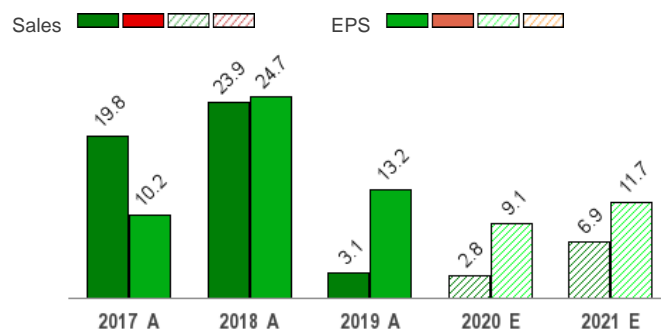
Last EPS Surprise	1.5%
Last Sales Surprise	-0.6%
EPS F1 Est- 4 week change	1.0%
Expected Report Date	04/22/2020
Earnings ESP	-1.7%

P/E TTM	22.1
P/E F1	20.2
PEG F1	1.6
P/S TTM	3.4

Price, Consensus & Surprise



Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	398 E	424 E	425 E	449 E	1,668 E
2020	372 E	394 E	396 E	416 E	1,561 E
2019	360 A	384 A	379 A	395 A	1,518 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.78 E	\$0.90 E	\$0.86 E	\$0.85 E	\$3.34 E
2020	\$0.67 E	\$0.78 E	\$0.76 E	\$0.80 E	\$2.99 E
2019	\$0.65 A	\$0.73 A	\$0.68 A	\$0.68 A	\$2.74 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 02/20/2020. The reports text is as of 02/21/2020.

Overview

Headquartered in Plainsboro NJ, Integra LifeSciences is one of the world leaders in regenerative medicine. The company develops, manufactures and markets cost-effective surgical implants and medical instruments. The company now manufactures and sells products in the following two global reportable business segments: **Codman Specialty Surgical (CSS)** and **Orthopedics and Tissue Technologies (OTT)**.

The **CSS** business (65.6% of revenues in 2019, organic growth of 5.6% in 2019), previously known as Specialty Surgical Solutions, offers global, market-leading technologies, brands and instrumentation. The acquisition of Codman Neurosurgery from Johnson & Johnson increased the global direct sales representation and international presence.

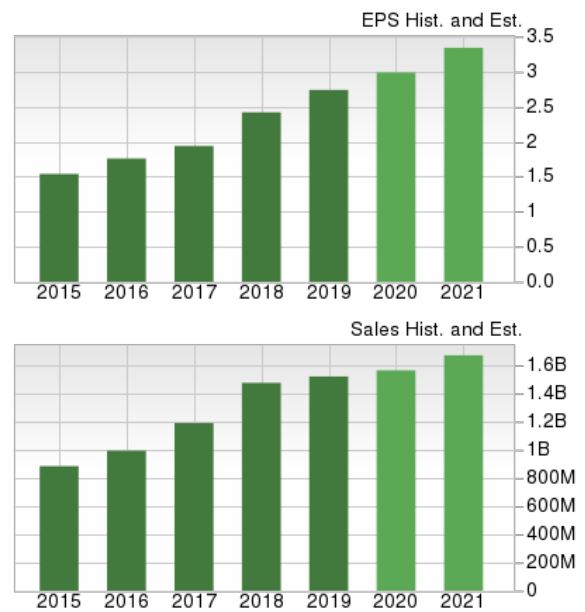
The global commercial network includes clinical specialists, a large direct global sales force and strategic partnerships and distributors that serve hospitals, integrated health networks, group purchasing organizations, clinicians, surgery centers and health care providers in North America, South America, Europe, Asia Pacific, Middle East and Africa.

In 2019, the segment registered 3.3% growth from 2018.

The **OTT** segment (34.4%, 1.6%) includes specialty metal implants for surgery of the upper and lower extremities, skin and wound repair products and bone grafts and nerve and tendon repair products.

The acquisition of Derma Sciences in 2017 provides the company with a relevant scale in outpatient wound care, doubling the sales force in the United States and broadening its business base with advanced products such as Medihoney, weight offloading and amniotic tissue. It also creates opportunities to further expand footprint in the plastic and reconstructive surgery segments.

In 2019 the segment registered 2.5% growth from 2018.



Reasons To Buy:

▲ **Share Price Performance:** Integra has outperformed the industry in the past month. The stock has climbed 3.6% compared with the industry's 1.4% rise. In the fourth quarter, the company registered balanced segmental growth. The Codman Specialty Surgical segment rose 4.1%, whereas Orthopedics and Tissue Technologies revenues grew 1.3%. The strong fourth-quarter performance of DuraGen in Japan, following its launch in the third quarter, instills optimism. We are also upbeat about the longer-term revenue contributions from the Arkis Biosciences and Rebound Therapeutics acquisitions completed in the third quarter. Expansion of both margins also contributed to the share price rally. The 2020 guidance for organic revenue growth and adjusted EPS appears strong.

A series of product introductions, particularly in Extremities franchise and strong overseas expansion are expected to add value going ahead.

▲ **CSS Segment Holds Potential:** At the end of the fourth quarter, revenues from the Codman Specialty Surgical segment rose 4.1% (organic growth was 5.6%). The upside was driven by the substantial completion of all integration activities related to the Codman acquisition, scale expansion, product launches, and venturing into faster-growing markets like China and Japan.

In 2019, the company acquired two early-stage technology platforms, which were anti-thrombus coding technology (to reduce catheter obstructions) and a technology platform for minimally invasive neuro surgery. These two technologies added to its portfolio, thus creating clinical opportunities for expansion into new larger and faster-growing markets, including intracerebral hemorrhage and minimally invasive neurosurgery. Currently, the company is investing in the two technologies, and aligning the development and clinical progress with its commercialization plans.

International sales in CSS grew in the fourth quarter on product introductions within the company's core neurosurgery portfolio, strengths across Europe, and robust growth in China and Japan.

▲ **OTT Segment Strong:** In the reported quarter, the OTT segment registered a 1.3% growth year over year. Organically, the segment grew 1.6%, owing to sales uptick in wound reconstruction. Wound reconstruction, in turn, rose due to the company's performance in inpatient and plastics and reconstructive portfolios, partially offset by weaker sales in outpatient settings.

Currently, it is focusing on capacity expansion at various facilities manufacturing regenerative products for reconstructive procedures. The company is positioning itself to meet the rising demand and regulatory requirements expected for the segment through manufacturing investments. After stabilizing the orthopedic franchise in 2019, it also witnessed a positive momentum in both ankle and shoulder portfolios, which registered robust growth.

Integra expects an improvement in its international performance on benefits from the combination of new products like the ankle revision and small post baseplate along with the expansion of its established commercial team.

▲ **Solid Growth in International Business:** In spite of facing foreign exchange fluctuations across its international business, Integra successfully saw through certain key developments on the overseas front. International sales within Codman Specialty Surgical have been strong in recent times driven by growth in core neurosurgery business and strength in certain key markets such as Europe, Canada, China, and Japan. Per Integra, the acquisition of Codman is effectively doubling the company's international business within this segment.

Integra is looking forward to investment opportunities in the Asian market in order to grow business much faster than the United States and also certain parts of its international businesses. In line with this, the company is preparing to launch several products in China and Japan. The strong fourth-quarter performance of DuraGen in Japan, after its launch in the third quarter, buoys optimism.

▲ **Near-term Objectives to Add Value:** Integra has adopted several near-term objectives to align with its 4-pillar strategy viz. 1) building an execution-focused culture 2) achieving relevant scale, 3) improving agility and innovation and 4) leading in customer excellence. These include investments in innovative product development which should result in a multi-generational pipeline for the company's key products; geographic expansion outside the United States, given that most large medical device companies earn around half of their revenues internationally; and strategic acquisition of new products and businesses to develop the company's operations. The company recently introduced the Titan Press-Fit Reverse Shoulder for Fracture and also announced the full commercial availability of the Cadence Total Ankle. The Cadence coupled with Integra Lifesciences' Salto ankle makes the most competitive ankle arthroplasty portfolio.

Management also expects to gain market share through strategic partnerships and acquisitions. The company noted that, by sharpening focus on areas mentioned under the 4-pillar strategy through improved planning and communication, optimization of the infrastructure and strategically aligned tuck-in acquisitions, it can build scale, increase competitiveness and achieve long-term goals.

Reasons To Sell:

- ▼ **Natural Calamities Might Hamper Business Process:** Many of Integra's manufacturing, development or research facilities are vulnerable to natural disasters or unwanted events, which depending on the extent of its severity, might force the company to cease development and manufacturing of some or all of its products. In particular, Integra's San Diego and Irvine, CA facilities are susceptible to earthquake damage, wildfire damage and power losses from electrical shortages as are other businesses in Southern California. Integra's Añasco, Puerto Rico plant, where it manufactures collagen, silicone and its private label products, is vulnerable to hurricane, storm, earthquake and wind damage. Further, Integra LifeSciences' Plainsboro, NJ facility is prone to hurricane damage. Although the company maintains property damage and business interruption insurance coverage for these facilities, management fears insurance might not cover for all losses in the event of such dire circumstances. Also, the company may not be able to renew or obtain such insurance in the future on acceptable terms with adequate coverage or at reasonable costs.
- ▼ **Competition:** Integra faces significant competition in the surgical implants and medical instruments market. The company needs to be innovative on the product front in order to keep up with the competition. Moreover, consolidation trends in the industry could lead to intense pricing pressure and further competition in this niche. The primary competitors in specialty surgical solutions are the Aesculap division of B. Braun Medical, Inc., Johnson & Johnson, Medtronic, Inc., Stryker Corporation, Becton, Dickinson and Company, and C.R. Bard, Inc. In addition, the company competes with many smaller specialized companies and larger companies that do not otherwise focus on specialty surgical solutions. Other major players in orthopedics and tissue technologies includes the DePuy/Synthes business of Johnson & Johnson, Stryker Corporation, Wright Medical Group, N.V., Smith & Nephew plc, MiMedx Group, Inc., Acclivity L.P. Inc., a subsidiary of Allergan PLC, and Zimmer Biomet Holdings, Inc.
- ▼ **Foreign Exchange Woes Stay:** Integra generates significant revenues outside the U.S., a portion of which are U.S. dollar-denominated transactions conducted with customers who generate revenue in currencies other than the U.S. dollar. As a result, currency fluctuations between the U.S. dollar and the currencies in which those customers do business may have an impact on the demand for the company's products in foreign countries. With the recent upward trend observed in the value of the U.S. dollar, further acceleration expected by analysts in this value will cause the company's revenues to face a tough situation overseas.

Uncertain natural calamities might force Integra to stop production in one or more of its manufacturing or research facilities. The stock faces stiff competition as well as foreign exchange fluctuation.

Last Earnings Report

Integra's Q4 Earnings Surpass Estimates, Margins Up

Integra delivered adjusted earnings per share of 68 cents in the fourth quarter of 2019, up 4.6% from a year ago. The metric surpassed the Zacks Consensus Estimate by 1.5%.

GAAP earnings per share for the fourth quarter was 18 cents, reflecting a dip of 37.9% from the year-ago period due to expenses related to the Rebound Therapeutics Corporation acquisition and tax benefits received in the year-ago quarter.

Adjusted earnings per share was \$2.74 for the year, reflecting a 13.2% increase from the year-ago period. However, the company lagged the Zacks Consensus Estimate by 8.4%.

Quarter Ending **12/2019**

Report Date	Feb 19, 2020
Sales Surprise	-0.58%
EPS Surprise	1.49%
Quarterly EPS	0.68
Annual EPS (TTM)	2.74

Revenue Discussion

Total revenues in the reported quarter moved up 3.1% year over year to \$395.1 million, which lagged the Zacks Consensus Estimate by 0.6%. Organically, the company's revenues grew 4.6% year over year.

Revenues for the year were \$1.52 billion, reflecting a 3.1% increase from the year-ago period. The metric was in line with the Zacks Consensus Estimate. Organically, the company's revenues grew 4.8% for the year.

Segmental Details

Coming to product categories, revenues from the **Codman Specialty Surgical** segment rose 4.1% to \$259.4 million (organic growth was 5.6%). The upside was driven by the substantial completion of all integration activities related to the Codman acquisition, scale expansion, product launches, and venturing into faster growing markets like China and Japan.

Orthopedics and Tissue Technologies revenues totaled \$135.7 million in the fourth quarter, up 1.3% year over year. Organically, the segment grew 1.6%, owing to sales uptick in wound reconstruction. Wound reconstruction, in turn, rose due to the company's solid performance in inpatient and plastics and reconstructive portfolios, partially offset by weaker sales in outpatient settings. However, wound reconstruction sales were affected by supply constraints in the reported quarter.

Margin Trend

In the reported quarter, gross profit totaled \$245.7 million. Gross margin expanded 38 basis points (bps) to 62.2% on a 3.7% rise in gross profit.

Selling, general and administrative expenses contracted 1.7% to \$174.3 million in the quarter under review, while research and development expenses rose 21.4% to \$24.6 million. In the quarter, the company incurred in-process research and development expenses of \$5 million.

Overall adjusted operating profit was \$41.8 million, up 6.2% year over year. Adjusted operating margin saw a 31-bps expansion year over year to 10.6%.

Financial Position

Integra exited the year with cash and cash equivalents of \$198.9 million, up from \$138.8 million at the end of 2018.

Cumulative cash flow from operating activities was \$231.4 million at the end of 2019 compared with \$199.7 million at the end of 2018.

2020 Outlook

For the year, Integra reiterated its guidance (issued on Jan 14). Revenues are expected between \$1.55 billion and \$1.57 billion, representing a reported growth of 3%. The Zacks Consensus Estimate for the metric is pegged at \$1.56 billion.

For 2020, organic sales growth (excluding the effects of foreign currency, acquisitions, divestitures and discontinued products) is projected to be 5%.

GAAP earnings per share is expected between \$1.40 and \$1.45 for 2020.

Adjusted earnings per share is expected between \$3.00 and \$3.05 for 2020. The Zacks Consensus Estimate for the metric stands at \$2.99.

Valuation

Integra shares are up 3.8% in the year-to-date period and up 10.3% in the trailing 12-month periods. Stocks in the Zacks sub-industry are up 5.6% while the Zacks Medical sector rose 2.2% in the year-to-date period. Over the past year, the Zacks sub-industry is up 12.2% and sector is up 4.1%.

The S&P 500 index is up 5% in the year-to-date period and increased 22.6% in the past year.

The stock is currently trading at 19.9X Forward 12-months earnings, which compares to 34.8X for the Zacks sub-industry, 21.4X for the Zacks sector and 19.3X for the S&P 500 index.

Over the past five years, the stock has traded as high as 26.8X and as low as 15.9X, with a 5-year median 20.7X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$64 price target reflects 21.1x forward 12-months earnings.

The table below shows summary valuation data for IART

Valuation Multiples - IART					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	19.95	34.83	21.38	19.31
	5-Year High	26.78	34.83	21.38	19.34
	5-Year Low	15.95	23.22	15.83	15.18
	5-Year Median	20.65	27.46	18.89	17.47
P/S F12M	Current	3.26	3.77	2.84	3.56
	5-Year High	3.86	3.77	3.83	3.56
	5-Year Low	1.90	2.17	2.45	2.54
	5-Year Median	2.87	2.52	2.97	3.00
P/B TTM	Current	3.75	4.33	4.62	4.67
	5-Year High	5.32	4.35	5.04	4.68
	5-Year Low	2.66	2.54	3.44	2.85
	5-Year Median	3.67	3.33	4.31	3.62

As of 02/20/2020

Industry Analysis Zacks Industry Rank: Top 29% (73 out of 255)



Top Peers

ConforMIS, Inc. (CFMS)	Neutral
DexCom, Inc. (DXCM)	Neutral
Integer Holdings Corporation (ITGR)	Neutral
LivaNova PLC (LIVN)	Neutral
Medtronic PLC (MDT)	Neutral
OPKO Health, Inc. (OPK)	Neutral
RTI Surgical, Inc. (RTIX)	Neutral
Cantel Medical Corp. (CMD)	Underperform

Industry Comparison Industry: Medical - Instruments				Industry Peers		
	IART Neutral	X Industry	S&P 500	CFMS Neutral	MDT Neutral	RTIX Neutral
VGM Score	B	-	-	C	C	C
Market Cap	5.20 B	105.49 M	24.34 B	75.58 M	152.62 B	365.38 M
# of Analysts	7	2	13	3	14	1
Dividend Yield	0.00%	0.00%	1.78%	0.00%	1.90%	0.00%
Value Score	B	-	-	F	B	C
Cash/Price	0.04	0.09	0.04	0.44	0.07	NA
EV/EBITDA	27.06	-0.55	14.18	-2.83	17.95	NA
PEG Ratio	1.55	2.87	2.09	NA	2.74	NA
Price/Book (P/B)	3.75	4.33	3.30	3.80	2.94	1.71
Price/Cash Flow (P/CF)	19.65	23.65	13.49	NA	15.66	16.25
P/E (F1)	19.87	31.83	19.28	NA	20.21	495.00
Price/Sales (P/S)	3.42	3.60	2.68	0.95	4.91	1.22
Earnings Yield	4.94%	-0.55%	5.17%	-33.64%	4.95%	0.20%
Debt/Equity	1.07	0.10	0.70	1.83	0.48	NA
Cash Flow (\$/share)	3.08	-0.06	7.03	-0.51	7.27	0.30
Growth Score	B	-	-	A	C	B
Hist. EPS Growth (3-5 yrs)	13.71%	13.63%	10.84%	NA	6.06%	-18.71%
Proj. EPS Growth (F1/F0)	9.07%	19.85%	7.09%	20.29%	7.95%	NA
Curr. Cash Flow Growth	-17.49%	8.15%	6.72%	-34.56%	6.26%	18.36%
Hist. Cash Flow Growth (3-5 yrs)	25.48%	7.88%	8.25%	5.23%	15.58%	27.78%
Current Ratio	2.92	2.66	1.22	3.11	2.75	NA
Debt/Capital	51.67%	17.32%	42.37%	64.60%	32.25%	NA
Net Margin	3.31%	-18.08%	11.56%	-41.36%	17.11%	-3.72%
Return on Equity	16.94%	-23.03%	16.80%	-115.71%	14.76%	1.75%
Sales/Assets	0.46	0.60	0.55	1.20	0.34	0.83
Proj. Sales Growth (F1/F0)	4.33%	10.47%	3.90%	4.57%	2.57%	NA
Momentum Score	B	-	-	C	C	D
Daily Price Chg	-0.87%	0.00%	0.01%	14.22%	0.08%	4.21%
1 Week Price Chg	2.59%	0.00%	1.65%	-5.01%	-1.36%	7.26%
4 Week Price Chg	7.71%	0.00%	0.36%	2.80%	-5.88%	19.57%
12 Week Price Chg	-1.35%	3.04%	4.39%	-38.89%	1.24%	171.98%
52 Week Price Chg	8.87%	-15.40%	15.29%	-19.71%	22.95%	8.08%
20 Day Average Volume	576,209	132,072	1,992,841	616,869	4,677,268	312,638
(F1) EPS Est 1 week change	0.98%	0.00%	0.00%	0.00%	0.63%	0.00%
(F1) EPS Est 4 week change	0.98%	0.00%	-0.02%	-1.85%	0.63%	0.00%
(F1) EPS Est 12 week change	0.55%	0.00%	-0.17%	-3.77%	0.63%	-88.89%
(Q1) EPS Est Mthly Chg	-1.09%	0.00%	-0.48%	NA	-1.18%	NA

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	B
Growth Score	B
Momentum Score	B
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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