Integra LifeSciences (IART)

$47.96 (As of 08/20/20)

Price Target (6-12 Months): **$50.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 06/25/20) Prior Recommendation: Underperform	**Neutral**
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**3-Hold**
	Zacks Style Scores:	VGM:B
	Value: B | Growth: D | Momentum: A	

Summary

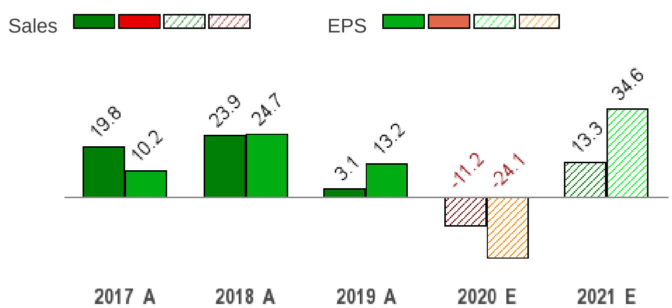
Integra exited the second quarter with better-than-expected earnings and revenues. However, the company registered disappointing segmental performances due to coronavirus-led business disruptions. Demand for both the company's OTT and CSS products declined significantly. Management is currently unable to gauge the magnitude of total loss it has to bear due to the pandemic-led economic damages. Hence, the company has not provided any financial guidance for the year. On a positive note, the ongoing recovery within the company's business looks encouraging. The company is currently confident about a sequential revenue growth in third quarter, although still expects this to be below the 2019 level. Internationally, the company performed better than its U.S. business. Overall, Integra has underperformed the industry in the past six months.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$64.24 - $34.21**
20 Day Average Volume (sh)	**354,802**
Market Cap	**$4.0 B**
YTD Price Change	**-17.7%**
Beta	**1.07**
Dividend / Div Yld	**$0.00 / 0.0%**
Industry	**[Medical - Instruments]**
Zacks Industry Rank	**Bottom 36% (161 out of 252)**
Last EPS Surprise	**312.5%**
Last Sales Surprise	**1.4%**
EPS F1 Est- 4 week change	**19.9%**
Expected Report Date	**10/22/2020**
Earnings ESP	**0.0%**
P/E TTM	**22.1**
P/E F1	**23.1**
PEG F1	**1.8**
P/S TTM	**2.9**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates **(millions of $)**

	Q1	Q2	Q3	Q4	Annual*
2021	370 E	377 E	396 E	408 E	1,527 E
2020	354 A	259 A	343 E	392 E	1,348 E
2019	360 A	384 A	379 A	395 A	1,518 A

EPS Estimates

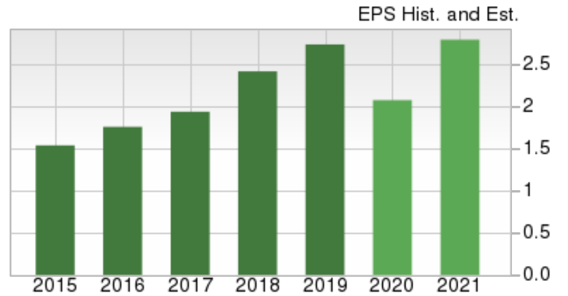
	Q1	Q2	Q3	Q4	Annual*
2021	$0.63 E	$0.65 E	$0.73 E	$0.82 E	$2.80 E
2020	$0.48 A	$0.33 A	$0.54 E	$0.71 E	$2.08 E
2019	$0.65 A	$0.73 A	$0.68 A	$0.68 A	$2.74 A

*Quarterly figures may not add up to annual.

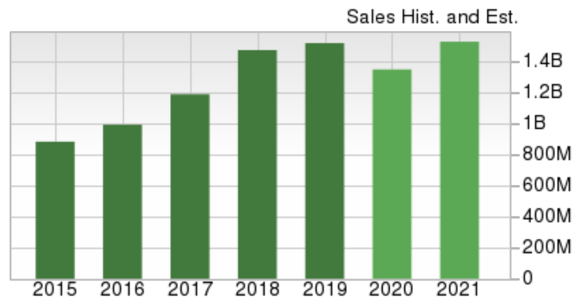
The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/20/2020. The reports text is as of 08/21/2020.

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:

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

▲ **Sales Rebound Visible**: As expected, Integra's second quarter of 2020 witnessed the hardest impact of the pandemic-led economic crisis. Surgical procedure volumes across the industry declined materially as essential resources were reallocated to treat COVID patients. Total sales declined 311% year over year. However, looking at the monthly sequential trends, sales in June improved to a decline of approximately 13% from the prior year's average daily rate for the second quarter. In the third quarter, the company already had a good start in July, showing a sequential improvement over June. The gradual business recovery is clearly visible now. The company is currently confident about a sequential revenue improvement in third quarter, but still expects this to be below the 2019 level. More encouragingly, it expects revenue returning to 2019 levels in the fourth quarter. However, this depends on recovery rates in Integra's capital and instruments businesses, which rely upon the availability of capital funds at hospitals and healthcare systems.

The company is confident that once the environment returns to growth, the actions Integra is taking and the plans it has in place, will position it for outperformance over the long term.

▲ **CSS Holds Strong Prospect**: Despite the slowdown within the CSS segment, there was steady monthly improvement throughout the second quarter with sales in June down only by 13%. Global neurosurgery sales performed better than the segment average with a decline of approximately 26% in the second quarter with each franchise showing sequential monthly improvement since the April lows. International sales in CSS, although down year over year, did better than the segmental average on a strong performance in Japan. In this region, revenues grew double-digits year-over-year on a moderate impact from COVID-19 as well as the company's recent investments including the successful 2019 launch of DuraGen.

Notably, 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.

▲ **OTT Segment Holds Strong Potential**: In the reported quarter, within OTT, there was steady rebound visible in this segment with sales in the month of June down by only 13%. Second quarter sales in Wound Reconstruction declined 31% year over year. However, for the month of June, sales in Wound Reconstruction improved to a decline of mere 10%. Recovery rates were particularly strong in chronic wound product line as well as nerve repair business.

Currently, the company 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.

▲ **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 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.

▲ **Strong Solvency But Leveraged**: Integra exited the second quarter of 2020 with cash and cash equivalents of $361 million compared with $358 million in the fiirst quarter of 2020. Meanwhile, total debt came up to $1.66 billion in the second quarter, down from $1.69 billion in the sequentially last reported quarter. This figure is much higher than the quarter-end cash and cash equivalent level indicating weak solvency. However, if we go by the company's near-term payable debt level, that is just $24 million now, insignificant as compared to the current cash holdings, indicating strong solvency. At least, during the year of coronavirus mayhem, when majority of the corporate sector is imposed with production and supply halt, the company is holding sufficient cash for its short-term debt repayment. Debt comparison with the industry is, favorable as well, as industry's total debt of $2.88 billion, stands much higher to the company's debt level.

The quarter's total debt-to-capital of 55.1% represented a sequential rise from 55.7% at the end of the first quarter. However, it stands at a moderately high level indicating a leveraged balance sheet. Further, this compares unfavorably with the total debt-to-capital of the industry which stands at a lower level of 37%.

The times interest earned for the company stands at 1.2%, which is sequentially low. This, too, compares unfavorably with the times interest earned for the industry which stands at a slightly higher level of 6.3%.

Reasons To Sell:

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.

- **Share Price Performance**: Integra has underperformed the industry in the past six months. The stock has lost 18.2% against the industry's 15.5% gain. In the second quarter, Integra registered disappointing overall and segmental performances due to coronavirus-led business disruptions.

  Integra LifeSciences strongly expects the ongoing impact from restrictions on surgical procedures and the U.S. Government's newly-implemented shelter-in-place policies to significantly dampen its third-quarter performance as well. The company expects third-quarter revenues to be lower than the year-ago levels due to the pandemic-led fall in non-emergent surgical procedures. Further, the company does not expect the recovery rates for all its markets and product lines to be the same, thus leading to uncertainties about revenues. Management is currently unable to gauge the magnitude of total loss it has to bear due to the pandemic-led economic damages. Hence, the company has not provided any financial guidance for the year.

- **COVID-19-led Postponement of Surgical Procedures Dent Sales**: Integra management noted that during the first two months of the quarter, sales were in line with the expectations. However, since March, as the pandemic took a graver form, demand for the company's surgical procedures declined significantly. This was because healthcare providers started to reallocate resources to address the surging demand caused by the COVID-19 outbreak. According to Integra, there was a dramatic sales decline that occurred as soon as surgical procedures were postponed on a wide scale.

  In the third quarter, Integra still projects year-over-year declines, although not at the same rate as in the second quarter as many procedures in which its products are employed cannot be deferred for more than 90 days.

- **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., Acelity 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.

Last Earnings Report

Integra's Q2 Earnings Beat Estimates, Margins Down

Quarter Ending	06/2020
Report Date	**Aug 10, 2020**
Sales Surprise	**1.44%**
EPS Surprise	**312.50%**
Quarterly EPS	**0.33**
Annual EPS (TTM)	**2.17**

Integra LifeSciences delivered adjusted earnings per share of 33 cents in the second quarter of 2020, down 54.8% from a year ago. The metric, however, surpassed the Zacks Consensus Estimate by a stupendous 312.5%.

The adjustment excludes the impact of certain non-recurring charges like structural optimization, acquisition and integration-related, COVID-19 and intangible asset amortization expenses, among others.

GAAP earnings per share for the second quarter was at a break-even level, compared with the year-ago quarter's earnings per share of 34 cents.

Revenue Discussion

Total revenues in the reported quarter declined 32.6% year over year to $258.7 million. However, the metric exceeded the Zacks Consensus Estimate by 1.4%. Organically, revenues dropped 31.3% year over year.

The revenue decline can be attributed to lower surgical procedures related to COVID-19.

Notably, despite the fall in revenues due to the pandemic-led impacts, it exceeded the company's expectation of $254-$256 million which was provided along with the preliminary results announced early last month.

Segmental Details

Coming to product categories, revenues from the **CSS** segment fell 31.9% to $169.8 million (organically, decline was 30%). However, the segment witnessed steady monthly improvement throughout the quarter. The global neurosurgery sales were better than the segment's average sales during the quarter. Although neurosurgery sales were down mid-single digits in June, a strong recovery in neuromonitoring, CFS management, and dural access and repair was registered as these products are used in urgent procedures.

International sales in CSS, although lower, performed better than the segment average, led by strength in Japan. Also, a more moderate impact of the pandemic and investments made over the past year in Japan (including the successful launch of DuraGen in 2019) contributed to the top line.

OTT revenues totaled $88.9 million in the second quarter, down 33.9% year over year. Organically, the segment fell 34%. Although the OTT segment recorded a fall in revenues, it has started to recover. The recovery is being led by sales of the company's shoulder solutions.

Margin Trend

In the reported quarter, gross profit totaled $153.2 million. Gross margin contracted 333 basis points (bps) to 59.2% on a 36.2% fall in gross profit. Per the company, adjusted gross margin was 66.2%, down 120 bps.

Selling, general and administrative expenses contracted 29.8% to $116.1 million in the quarter under review, while research and development expenses fell 15.4% to $14.9 million.

Overall, adjusted operating profit was $22.2 million, down 61.1% year over year. Adjusted operating margin saw a 628-bp contraction year over year to 8.6%.

Financial Position

Integra exited the second quarter of 2020 with cash and cash equivalents of $360.9 million, up from $357.7 million at the end of the first quarter.

Cumulative net cash flow from operating activities at the end of the second quarter was $53.9 million compared with $78 million in the year-ago quarter.

2020 Outlook

Given the current economic situation due to the pandemic, Integra is unable to assess the magnitude of its impact on its financial results. Hence, the company has not provided any financial guidance for the year.

However, the company expects third-quarter revenues to be lower than the year-ago levels due to the pandemic-led fall in non-emergent surgical procedures. Further, the company does not expect the recovery rates for all its markets and product lines to be the same, thus leading to uncertainties about revenues.

Recent News

FDA Nod for Neurosurgery Indication for CUSA Clarity: Jul 22, 2020

Integra has received FDA approval for a specific indication for neurosurgery for its CUSA Clarity Ultrasonic Surgical Aspirator System.

Upper Management Churn: May 21, 2020

Integra LifeSciences noted changes to its executive leadership team. Michael McBreen, the company's present the corporate vice president and president of the international business, has been promoted to executive vice president and president, CSS, effective June 8, 2020. Mr. McBreen replaces Dan Reuvers, who will be leaving Integra to become chief executive officer of Tactile Systems Technology, Inc.

Valuation

Integra shares are down 17.7% in the year-to-date period and down 22% in the trailing 12-month periods. Stocks in the Zacks sub-industry are up 17.6% while the Zacks Medical sector rose 0.7% in the year-to-date period. Over the past year, the Zacks sub-industry is up 22.8% and sector is up 8.5%.

The S&P 500 index is up 5.1% in the year-to-date period and rose 16.1% in the past year.

The stock is currently trading at 18.9X Forward 12-months earnings, which compares to 38.4X for the Zacks sub-industry, 22.3X for the Zacks sector and 22.8X for the S&P 500 index.

Over the past five years, the stock has traded as high as 26.8X and as low as 11.8X, with a 5-year median 20.9X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our $50 price target reflects 19.7X 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	18.90	38.40	22.28	22.83
	5-Year High	26.78	41.71	23.17	22.83
	5-Year Low	11.83	23.21	15.89	15.25
	5-Year Median	20.97	28.06	18.97	17.58
P/S F12M	Current	2.77	4.45	2.81	3.71
	5-Year High	3.86	4.45	3.41	3.71
	5-Year Low	1.96	2.52	2.22	2.53
	5-Year Median	2.91	3.09	2.89	3.05
P/B TTM	Current	3.02	5.45	3.77	4.55
	5-Year High	5.32	5.50	5.07	4.56
	5-Year Low	2.22	2.75	2.94	2.83
	5-Year Median	3.67	3.90	4.28	3.75

As of 08/20/2020

Industry Analysis Zacks Industry Rank: Bottom 36% (161 out of 252)

Top Peers

Company (Ticker)	Rec	Rank
Hologic, Inc. **(HOLX)**	Outperform	1
OPKO Health, Inc. **(OPK)**	Outperform	2
ConforMIS, Inc. **(CFMS)**	Neutral	3
Cantel Medical Corp. **(CMD)**	Neutral	3
DexCom, Inc. **(DXCM)**	Neutral	3
Integer Holdings Corporation **(ITGR)**	Underperform	5
LivaNova PLC **(LIVN)**	Underperform	5
Medtronic PLC **(MDT)**	Underperform	3

Industry Comparison Industry: Medical - Instruments

Industry Peers

	IART	X Industry	S&P 500	CFMS	HOLX	MDT
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Outperform	Underperform
Zacks Rank (Short Term)	3	-	-	3	1	3
VGM Score	B	-	-	B	D	C
Market Cap	4.04 B	147.32 M	23.46 B	51.19 M	17.37 B	134.71 B
# of Analysts	6	2	14	3	9	13
Dividend Yield	0.00%	0.00%	1.65%	0.00%	0.00%	2.31%
Value Score	B	-	-	D	D	C
Cash/Price	0.08	0.12	0.07	0.33	0.04	0.08
EV/EBITDA	23.24	-1.56	13.34	-2.92	55.97	18.67
PEG Ratio	1.77	4.27	3.00	NA	1.46	3.68
Price/Book (P/B)	3.02	3.66	3.12	5.59	7.69	2.64
Price/Cash Flow (P/CF)	11.69	23.22	12.60	NA	15.98	15.15
P/E (F1)	22.69	48.23	21.61	NA	22.53	28.48
Price/Sales (P/S)	2.91	4.38	2.44	0.70	5.27	4.66
Earnings Yield	4.34%	-3.93%	4.43%	-68.18%	4.44%	3.51%
Debt/Equity	1.22	0.13	0.76	3.45	1.22	0.43
Cash Flow ($/share)	4.10	-0.13	6.93	-0.35	4.20	6.62
Growth Score	D	-	-	A	D	B
Hist. EPS Growth (3-5 yrs)	13.34%	10.12%	10.44%	NA	8.58%	5.13%
Proj. EPS Growth (F1/F0)	-24.15%	7.56%	-5.53%	-1.52%	22.54%	-23.29%
Curr. Cash Flow Growth	9.92%	5.04%	5.20%	-25.47%	2.17%	-9.02%
Hist. Cash Flow Growth (3-5 yrs)	19.16%	10.65%	8.52%	7.63%	3.55%	7.68%
Current Ratio	4.55	2.94	1.33	1.59	1.47	2.13
Debt/Capital	54.86%	18.18%	44.50%	77.51%	54.90%	30.21%
Net Margin	-0.25%	-25.57%	10.13%	-35.03%	20.03%	16.56%
Return on Equity	13.64%	-17.25%	14.67%	-189.08%	31.40%	12.17%
Sales/Assets	0.41	0.53	0.51	1.06	0.50	0.32
Proj. Sales Growth (F1/F0)	-11.18%	0.00%	-1.54%	-10.80%	1.70%	-4.77%
Momentum Score	A	-	-	A	C	C
Daily Price Chg	-2.76%	-0.07%	-0.59%	0.76%	0.06%	-0.54%
1 Week Price Chg	6.57%	-0.09%	1.09%	-0.23%	-2.54%	0.66%
4 Week Price Chg	-2.50%	-0.18%	1.91%	-15.60%	8.30%	3.84%
12 Week Price Chg	-8.05%	1.63%	6.82%	-35.29%	28.21%	2.18%
52 Week Price Chg	-22.04%	0.53%	1.47%	-67.33%	34.56%	-7.00%
20 Day Average Volume	354,802	252,469	1,873,576	666,824	2,243,926	4,165,135
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	3.11%
(F1) EPS Est 4 week change	19.90%	5.06%	1.79%	12.42%	29.66%	3.23%
(F1) EPS Est 12 week change	20.60%	4.63%	3.35%	15.19%	30.29%	-9.04%
(Q1) EPS Est Mthly Chg	9.59%	5.74%	0.42%	-8.00%	41.70%	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

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	D
Momentum Score	A
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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