VIAVID

communications simplified.

VieMed

Third Quarter 2019 Earnings Call

November 5, 2019

C O R P O R A T E P A R T I C I P A N T S

Todd Zehnder, *Chief Operating Officer & Director*

Casey Hoyt, *Chief Executive Officer & Director*

C O N F E R E N C E C A L L P A R T I C I P A N T S

Sarah James, *Piper Jaffray Companies*

Brooks O'Neil, *Lake Street Capital Markets*

Nick Corcoran, *Acumen Capital*

Doug Cooper, *Beacon Securities Limited*

John Ricodo, *Current Asset Management*

P R E S E N T A T I O N

Operator:

Good day, everyone. Welcome to the Viemed Third Quarter 2019 Earnings Call. Today's conference is being recorded. At this time, I'd like to turn the call over to Mr. Todd Zehnder, Chief Operating Officer. Please go ahead, sir.

Todd Zehnder:

Thank you. Good morning, everyone. Please note that our remarks in this conference call may include forward-looking statements under the U.S. federal security laws or forward-looking information under applicable Canadian securities legislation, which we collectively refer to as forward-looking statements. Such statements reflect the Company's current views and intentions, with respect to future results or events, and are subject to certain risks and uncertainties which could cause actual results or events to vary from those indicated in our forward-looking statements. Examples of such risks and uncertainties are discussed in our disclosure documents filed with the SEC or the securities regulatory authorities in certain provinces of Canada. Because of these risks and uncertainties, investors should not place undue reliance on forward-looking statements.

The forward-looking statements made in this conference call are made as of the date of hereof, and the Company undertakes no obligation to update or revise any forward-looking statements except as required by law.

The third quarter financial results news release, including the related financial statements, is available on the SEC's website.

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

Casey Hoyt:

Good morning, everyone, and thank you for joining our call today. Before I get going, I'd like to take some time to directly thank our 407 VieMed employees across the country for their continued commitment to our mission. Our team's constant passion for care allows us to make a difference in so many of our patients' lives. We take treating our people right seriously over here at VieMed, for without them, we would not be able to drive quality of life for our patients within the communities that we serve. The VieMed family and culture is second to none and remains at the cornerstone for our continued success.

Moving on to the progress made in the third quarter, I'll begin with our ongoing geographical expansion. The compliance department finished the quarter having us license new business in 47 states, Medicare approved in 46, and with the addition of Utah and Illinois, now conducting business in 31 states.

Our efforts to get positioned in the Lower 48 to ready ourselves for competitive bidding coverage are on track. We are actively positioning ourselves with clinicians and salespeople in more major metropolitan areas throughout our coverage area.

There's nothing new to report on the competitive bidding front other than we have officially submitted our bids in third quarter. Now we will wait and see as CMS decides to include noninvasive ventilation in the 2021 competitive bidding program. Operationally, we are growing in the same way that we always have, and we'll be ready to support our targeted areas that we have submitted bids.

Our sales managers and recruiters brought on seven new reps to cover seven new areas in the third quarter. This brings our year-to-date total to 31 new reps hired in 2019. Our new inside sales force, which we call the customer service representative program, has been evolving. We launched this program in the second quarter, with the intent of having some of the administrative tasks handled inside to help keep our salespeople selling in the field.

While this initiative has proven to work, it has evolved into something way more powerful. We are seeing our CSRs help our top reps with improving conversion rates on initial orders through creating efficiencies in processing paperwork. They are also helping with more frequent communication between our referral sources and clinicians in the field. I am personally most excited about the lead generation efforts that the program is providing. Our CSRs are morphing into an inside sales force that can schedule appointments in advance for our field reps. With each day that passes, our CSRs are figuring out ways to help us be more efficient. An initiative is underway for us to provide more resources to this department, and I'm excited to see just how impactful these folks can be through our experienced and new sales reps in the field.

While we did achieve mild growth in Q3, it was not a quarter of growth that we are used to experiencing at VieMed. After much reflection and analysis, we found that the manufacturers were experiencing the same trend. This industry-wide growth rate all points back to just having less patients coming out of the hospitals in the warmer months of the year. For the past few years, we've expanded through the seasonality factors of this business, which seem to catch up to us in Q3 2019. With that being said, we prepared our people to ready themselves for the colder months that Q4 brings, which are common to produce more respiratory related issues.

The summer months did not slow down our Managers from continuing to develop our ancillary home-based product lines. We saw expansions in our offerings of Oxygen, Lymphedema pumps, vest, and now our new offering, multifunction vents.

The multifunction vent is a ventilator that functions as a vent, oxygen concentrator, cough assist, suction and nebulizer. These are five machines that are all found in the homes of more severe patients all rolled up into one unit. Patients typically struggling with neuromuscular diseases, as well as our pediatric patients, are good candidates for this therapy. Our sales people are thrilled to have this new clinical offering to help open more doors inside the ALS and children's hospital communities.

We've also captured another incremental opportunity inside of the VA. We assigned a veterans' care agreement that will allow us to access to treat many New Mexico veterans that cannot access VA care. Our role will be to provide respiratory assessments, in-home pulmonary rehab and provide respiratory care plans for rural VA patients. This agreement has been put in place for the next three years as the only provider of in-home respiratory services for the Albuquerque facility. While this is not a visit-wise win that we've been searching for, it's certainly a nice win and one that we can build out for other areas around the country. We are also moving along with our clinical trial study inside of the VA as the pilot continues to move forward with the VA physicians.

Speaking of studies, Dr. Fraser worked very hard in the third quarter to produce a poster presentation at the PRECISION and Harvard Medical School study, and he presented at the world's largest pulmonary conference, CHEST. The results he presented were similar to clinical results for our KPMG study, however, the time period of patients analyzed went from six months to one year. The major findings of the study was that the patients who go on NIV therapy had a 12% reduction in mortality, which means that our number needed to treat, or our NNT, went to eight patients to save a life. The KPMG study showed over 15,000 patients, and this new PRECISION study showed over 36,000 patients, making it more statistical by a landslide. When you reflect on how doctors need to put 71 patients on Lipitor to save a life or put 1,000 patients on flu shots to the save one life, our six to eight number needed to treat to save a life that KPMG and now PRECISION shows is a major clinical needle mover. This new study will now become a huge part of our value proposition to physicians across the country.

Q3 was the best-ever quarter for our network development department with the addition of 44 new commercial Medicare Advantage, Managed Medicaid and one major national payer, eight major regional networks and several other high-priority payers. These wins also translate into us having access to market growth with over 9.6 million additional covered lives. Payers are more engaged than ever to form relationships with ACOs who are truly set up to save money. We are positioned with our data and service to be the value-based provider that these collaborations need to succeed. We were very active in the third quarter with our conversations on how to partner with a handful of ACOs around the country.

One of the hot topics with payers right now is remote patient monitoring and having the ability to report back on outcomes with their customers. These conversations reaffirm our position to invest in technology last year, and our traction in this department is gaining at the perfect time. Our tech team has been piloting our new patient engagement portal with a handful of patients around the country. They have tested the usability of the product and have confirmed that our patients will not only use the tablets in the home, but they prefer the interaction. We expect to roll the tablets to many of our new patients in Q4, and we'll begin monitoring length of stay. This movement to remote care will not only help us form stronger payer relationships, but it comes at a perfect time, which will allow us to manage more rural patients efficiently.

Todd and I were also active in the third quarter with speaking to as many investors as possible. We've marketed in New York and presented at the Lake Street Conference on many different fronts. We want to make ourselves as available as possible, speak to as many investors as we can in the U.S. and in Canada to build our liquidity on the NASDAQ.

With more on that and to present the financial results of the third quarter, I will now turn the call over to our Chief Operating Officer, Todd Zehnder. Todd?

Todd Zehnder:

All right. Thank you, Casey. In reviewing the financial results, all figures are in U.S. dollars and the full results are available on the SEC website, as well as SEDAR.

We generated revenue of $23.5 million during the third quarter of 2019 as compared to revenues of $17.1 million in the third quarter of 2018, which equates to a 37% increase. Our revenues came in just below previously guided range for third quarter revenues.

While our vent patient growth was still solid and we exited with 7,419 patients, the summer season proved to be more challenging for the respiratory industry than we have previously seen.

Our gross margin percentage was 73% as compared to 76% in the prior year's third quarter. Adjusted EBITDA totalled $5 million for the quarter, which is a 21% margin. Our continued efforts into growing new regions, new products, new payer sources and new departmental strength, such as technology and marketing, has suppressed our margins as compared to prior years, but the investments are sound and setting up for more robust growth in the future. We have funded our growth by redeploying our Adjusted EBITDA during the current quarter, as our medical cap ex totalled $4.2 million for the third quarter of 2019, primarily driven by new vent purchases to support our growing patient base, as well as growth from our newer products like vest and Oxygen that we have begun to sell in higher quantities.

We are now showing all of our medical equipment as property, plant and equipment versus having some in our inventory line item. Therefore, the implied quarterly cap ex is higher as a result of this accounting reclass.

Our SG&A totalled approximately $13.3 million as compared to $9.5 million in the prior year. As in prior quarters, we will continue to make investments into our growth of the Company around the country, as well as in our home office in Lafayette. As we have moved more into a multi-product and multi-payer company, we find ourselves investing into more back-office items. Our marketing and technology investments have been significant, and we are excited that we are in pilot test of our patient engagement platform and are close to rolling out a new e-commerce solution. We have consistently discussed why these investments are important to the future of our business and are excited to see the positive impact for our patients, our employees and ultimately, our revenues, as these items are effectively rolled into our daily operations.

As in prior quarters, we once again have a very solid balance sheet with approximately $12.6 million in cash at quarter end, $11.7 million of AR, and an overall working capital balance of roughly $4.5 million. Our AR was still slightly higher than year end, as our revenues are increasing dramatically every month and the conversion into our new workflow and billing software implementation impacted the timing of our collections. Cash collections were significantly higher in the third quarter than the prior two quarters, as our team has worked through the integration issues, and we are operating much more efficiently now that we have been in the new system for a few quarters.

The higher bad debt expense in the quarter also reduced our AR, as our team is getting more accustomed to the new workflow system and have been able to spend more time on detailed accounts and looking back at balance that still remains from the conversion. As I've stated in the past, these types of investments and changes are crucial as we continue our rapid growth around the country.

Our long-term debt is approximately $10.9 million and being serviced with operating cash flow. The majority of this balance is due to the new headquarters purchase, our recent term loan taking out to boost our liquidity as we have been growing new product so aggressively, and the vendor financing that we use from time to time to manage our cash flows for new equipment purchases. From an ongoing capital perspective, we will continue to use our internally generated cash flow and capital leases with our major vendors, and we believe that we will be able to fund our future growth using the same financial instruments. With all of that said, we still have a fully undrawn $10 million line of credit that we have available.

Moving on to the fourth quarter, we have provided revenue guidance in the $24.7 million to $25.2 million range and have also guided to net revenue of $21.8 million to $22.2 million. We're moving towards showing our revenues net of any adjustments going forward versus showing some as revenue adjustments and some as bad debt expense within the SG&A line item. This presentation is seen more commonly in the U.S. reporting peer group so we feel like adopting that in the fourth quarter makes most sense. Note that this has no impact on EBITDA or net income margins, only a reclass on the P&L that will impact our gross margins in the future. We feel that our Adjusted EBITDA percentages will be materially similar as the first few quarters, depending on our variable compensation plans. We once again expect all this growth to be organic, and we are very excited to see multiple product lines contribute to the significant growth that we are experiencing. As in the prior quarters, we expect to reinvest most of our Adjusted EBITDA into capital expenditures.

As we wrapped up our first quarter as a NASDAQ-listed company, we are very proud that we continued our growth story and have met with many new U.S. investors. We know that it will take some time for our average daily liquidity to grow on the U.S. exchange, but we are committed to continuing our road efforts to U.S. fronts. We will continue our marketing efforts to both buy and sell-side alike and are excited to keep posting organic revenue and profit growth.

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

Casey Hoyt:

Thanks, Todd. We've regularly stated that the major opportunity inside of our business is with the patients that qualify but cannot access our care. The new Medicare utilization numbers were presented in the third quarter, and they reflected that we still only had 60,000 beneficiaries on non-invasive ventilation service. With an estimated 25 million COPD patients in the country and only 16 million diagnosed, we have always said that there are roughly 1.25 million at Stage 4 who qualify for our care. Our Company still believes we're at less than 5% market penetration number for an industry. We must have more data, more studies and more people to help the 95% of folks that are returning to the hospital without a home solution in hand. Our country has to embrace home-based providers to care for the masses of patients that are headed our way.

Payers, physicians, providers and patients all know this and are seeking out these solutions. At VieMed, we have the solution and the recipe for success, and we are riding the tailwinds that will ultimately lead us to being the largest home respiratory company in the country.

This concludes our prepared remarks. We'll now open up the floor for questions.

Operator:

Thank you, sir. If you would like to ask a question, please signal at this time by pressing star, one on your telephone keypad. If you're using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Once again, that is star, one if you would like to ask a question.

Your first question comes from the line of Sarah James with Piper Jaffray.

Sarah James:

(Inaudible)

Casey Hoyt:

Sarah, we lost you there. I don't know, we have some feedback.

Operator:

Yes. We'll move on to another question in the meantime. Ms. James, if you would try reconnecting, that might help. We'll now go to Brooks O'Neil with Lake Street Capital Markets.

Brooks O'Neil:

Good morning, guys. Congratulations on your results. I was hoping you could talk just a little bit more about the growth initiatives and the results you're seeing. Obviously you're picking up new market growth, in some cases going to some larger metropolitan areas. I'm curious if you've seen sort of the traditional VieMed growth trajectory in those new markets? Or if you're seeing anything different than normal?

Todd Zehnder:

Yes. We've learned a lot of fast track into these metropolitan areas, Brooks. I mean, your payer relationships are so much more important in the bigger cities than they are in the rural markets. You find a lot more heavy Medicare business out in the rural markets, a lot more COPD. The growth rate is a little bit slower as you learn the landscape in the metro areas. That still doesn't mean that we're not going to be in those areas. We're actually just kind of beefing up our network development efforts, which is why you see so much growth in that division.

As far as all the other initiatives, we're looking at all sorts of different strategies to expand our sales force, expand our recruiting efforts, beef up the recruiting efforts, beef up the trading programs, have a group of cold-blooded sales people type of Fortune 500 training folks that are coming out of different industries. We're opening that up a little bit to broaden our scope of who we can get in here for recruiting. We expect that to pick up here in Q4.

Brooks O'Neil:

Todd, you said no real update on competitive bidding. But can you just refresh our memory on what the timeline you expect is in terms of the sequence of response from CMS, et cetera?

Todd Zehnder:

Yes, so we submitted—like Casey's prepared remarks said, we submitted all of our bids in September, and there's a process that you just had to go through to qualify your bids and we're ongoing with doing that. While there's no exact dates given by CMS, we are expecting to hear maybe late spring or in the summertime as to the winning bids for the regions. We have not been fully educated as to—are they going to announce the rate for each region that wins first? Or are they actually going to announce the providers? We're hearing a little bit of differences on that. It's still a little early to give some concrete information. I'm sure, as people are seeing out there, there are different groups out there and there's some legislative efforts in place right now to try to get competitive bidding to—or to get NIB out of competitive bidding for the 2021 round. We, as the third largest provider of this service in the country, are ready for it, but there are quite a few patient advocacy groups who see the problems of this going into competitive bidding. We're following that as well. But as of now, think of that as sometime late spring, early summer, we start figuring something out.

Brooks O'Neil:

Talked a little bit, Todd, about the summer seasonality and a little bit slower discharge activity related to warm weather. Is that something you've seen before? Or something you think might become an annual thing? Or how do you react to that?

Todd Zehnder:

It's been a long time since we've seen a seasonality effect, Brooks. I mean, for me, being in the industry since ‘06, it’s been since four, five years ago, we used to experience slowdowns in summer months. But we've kind of always outgrown that. This quarter was—we felt it and it wasn't just that, it was our—the competitors that we've spoken to, the manufacturers of all our different product lines, all just chalked it up because warmer months, less respiratory issues, less patients coming out of the hospital. Be that as it may, we still don't accept that. We look into ways that we can look in the mirror and see if there's anything else that we could be doing. That's what we're doing right now. But all things are pointing that, we just had a bad seasonality quarter right there in those warmer months.

Brooks O'Neil:

I think you mentioned that bad debt expense popped up a little bit during this quarter as well. Is there anything that you think drove that? Or is it something you think is going to remain sort of at this level? Or do you think it's more likely to go back into historical ranges?

Todd Zehnder:

Yes. I mean, the short answer is I expect it to go back down into a lower range within the historical average that I always quote of 9% to 13% but we have generally hung out at the lower to middle end of that. If you look at the full year, we should be somewhere—it looks like between 10.5% and 11%. What happened this year, which was unique, and I've talked about it on a couple of the calls, is that we completely revamped our workflow system in the field, and that translates into a new billing and intake system as well.

Truthfully, when you're servicing 20,000 patients almost and having an infinite amount of insurances between primary, secondary and patients, there are just glitches that happen. Our staff was very dedicated to making sure that bills were sent out and making sure that glitches were worked on, and they did a fantastic job in the first six months.

But while we were spending time on that, we weren't working individual patient balances as fastly as we normally do. That kind of got back in play in the third quarter. It's why our third quarter collections were so much greater than the first two and October has been a record collection month on a cash basis. We're converting those receivables at a faster pace like we used to do.

When I look at it, the third quarter is somewhat of an anomaly for a variety of different reasons, mainly the integration. But all is fine. We're still going to be living within that range. Once again, I will reiterate that we expect to be on the lower end of the range that the DME industry is used to, which is that 12% to 13%. I want to get this back down to high-single digits or right at the low double digits.

Brooks O'Neil:

Obviously, you're investing heavily in sales and marketing. How do you feel about the rest of your infrastructure? Do you think you're set for continued growth and eventual operating leverage in the business model?

Todd Zehnder:

Absolutely. We're making some investments now, and we've been very open that there are great investments between the marketing and technology groups. Casey talked about it, the fact that our patient engagement platform has been in testing mode, and then we're going to try to go into a pilot this quarter. The feedback that we're getting from patients is outstanding. We're starting to see that, and then our e-commerce solution that our marketing team is developing, and just the fact that we've been investing in items to really continue to be able to deliver these double-digit quarterly growth that we all expect.

I mean, it's a lot of numbers. Every quarter that we get bigger, it gets harder to grow, but it doesn't mean that our expectation means we're going to slow down our growth rate. We had a slower quarter. We're still on track roughly to have a 40% annualized growth rate. It was more stacked up in the front end of the year. We recognize that. But what we're working on is setting ourselves up for these 40% growth years for years to come. That's why these investments are so critical to it.

Brooks O'Neil:

Good results.

Todd Zehnder:

Thanks, Brooks.

Operator:

All right, next we move to Nick Corcoran with Acumen Capital.

Nick Corcoran:

Good morning, and congratulations on a great quarter. Just a couple of questions for me. The first is on the competitive bidding, you say that there is some patient advocacy groups that are against the idea of competitive bidding. What do you think the chances of the NIB being excluded are?

Casey Hoyt:

It's hard to say. In general, CMS's position, from what we can see, is that this is going to continue forward, and that's what we're planning for. We've always said that this has springboarded our initiatives to go into these larger metropolitan areas. We had historically just grown 60 miles down the road and have not been springing to get into all these areas. We see it as an ability for our Company to expand faster and to get into some areas that we probably wouldn't have had in the next 18 months. With all that said, it's—we don't—I would hate to throw a percentage out there because I really don't know. We're planning for NIB to be there. We're hopeful that we win every bid we submitted. We're ready to go. If it's in, it's in; if it's not, then we'll adjust accordingly.

Nick Corcoran:

Great. Then you mentioned that there's a new multifunction vents. Are those at a significantly higher rate than your traditional vent?

Casey Hoyt:

Yes, they're a little bit more expensive, and there's a separate code that the reimbursement is a little bit higher than the non-invasive vent but you have to be billing for at least two of the functions, two of the five functions on the vent. It's a really great product for our ALS and pediatric patients. If you can think about a patient that is vent dependent, and they have to take their tube out and plug-in a cough assist or another device and produce a cough, those seconds and moment in time when you transfer from one machine to the next are very critical and present a lot of anxiety in the home with caretakers and patients. Now we could do this with the push of a button on the machine. Our clinicians in this company are just super pumped about this offering.

We've got a really great relationship with the manufacturer, and they identify that VieMed is a company that's very patient-centric driven and their clinical mission is sound. They are helping us expand into newer markets, newer ALS markets that we haven't been in as a result of this—of having this product offering now. We're very excited about it.

Nick Corcoran:

Can you give any indication what percent of your overall patients are ALS or children that might be able to use this product?

Todd Zehnder:

ALS is less than 5% of our patient base, and paediatrics, we can count on two hands or maybe four hands, maybe facing on both of our hands. It's a pretty small patient base currently. But like Casey said, this gives us the avenue to become much more of a solution when it comes to some of these ALS clinics around the country. Then there's also the quadriplegic community that could benefit from this. We're starting to look into calling on some of those centers as well. While it doesn't make up a huge part of our business right now, we see it as a really good solution for the patients and one that could help us with our growth rate.

Casey Hoyt:

The pediatric program, Nick, has assisted us with getting in with more payers around the country. We probably got 40 different payer contracts as a result of just having a pediatric offering. We had a clinical mission in hand, we wanted to take care of this, the toughest batch of patients, which were the kids, but we also had a business mission at hand, too, and that was to get in, build more deeper relationships with other payers around the country.

Nick Corcoran:

Great. Then the last question for me is just looking at your Q4 guidance, it looks that your implied bad debt expense about 10% to 13.5%. Am I thinking about that the right way?

Todd Zehnder:

Yes, that is correct. That's sort of the midpoint of our range, we would expect to come in somewhere in there.

Nick Corcoran:

Okay, that's great. Thanks again for your time.

Todd Zehnder:

All right. Thanks.

Operator:

Once again, everyone, that's star, one if you would like to ask a question.

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

Doug Cooper:

Good morning, guys. Casey, let me just start. I think I might have missed something at the very beginning. You said you're in 46 states for Medicare approval, 31 states are currently doing business, and you started out saying something about 47 states, but I missed that.

Casey Hoyt:

We're licensed to do business with 47 states, we're Medicare approved in 46 states. The first step is always just getting in with the Secretary of State and fulfilling the State requirement. The second phase is fulfilling Medicare's requirements to where you're accredited, and if they require a facility, then you have that facility. If not, we can usually move a little bit faster. But once we get Medicare approval, then we're ready to really start recruiting in that State. Basically, what that means, Doug, is that we're recruiting in 46 states right now. We're actually conducting business with patients and therapists and salespeople in 31 states. We added Utah and Illinois this past quarter.

Doug Cooper:

There's no impediment from a regulatory perspective now for moving from the 31 you're currently doing business to the 46, and that was just recruiting employees and so forth. Is that correct?

Casey Hoyt:

That's correct. We needed to be in those states to submit our competitive bids as well.

Doug Cooper:

Okay. Just on the competitive bidding, can you share with us how many areas you submitted a bid for?

Casey Hoyt:

It would have been 46 states.

Todd Zehnder:

Yes. There's like 124, I believe, of the 130 roughly, somewhere—it was over 120, but we were never planning on going to Honolulu, and there were a couple of states that we weren't able to get licensed and bid in and so on.

Doug Cooper:

Should we think of that, that's 124 cities or regions? Or how should we think about that?

Todd Zehnder:

Yes, you should think about it as generally cities, competitive bid areas are a cluster of zip codes to be technical, but it's the—so there are some areas that have multiple CBAs within a same, which you would consider a city. But generally, think about the 130 largest concentrations of people around the country.

Doug Cooper:

Can you maybe help us put this in perspective, so you finished the quarter with 7,421, I think, vent patients? How many vent patients would be in those 124 competitive bid areas?

Todd Zehnder:

When we first ran the numbers, it was about 25% of our patient base were in the CBAs, which were Medicare patients within that. We don't say if you're a commercial patient and a CBA, we're not going to throw that in that number. About 25% of our patient bases were Medicare patients in a CBA.

Doug Cooper:

Okay. I guess, what I'm trying to understand is what's the opportunity if you were to win, I should say 100 of 124 areas, how many potential patients—new patients, would you be actively recruiting for?

Todd Zehnder:

Well, generally, it just puts you in that area as marketing for that. It's not as though the people servicing those patients couldn't continue to service them until they expire. If we lose an area that we have patients, we continue to service those patients. We just can't take on new Medicare patients within that zip code range. What it does is it just—it's really spring boarded, like I said, when I was answering one of Brook's questions. It just pushed us to get into some of these larger areas faster, and it's just really compressing the time line that we had that we wanted to be in metropolitan areas. It's not like—it won't be January 1, we all of a sudden end up with 1,000 new patients.

Casey Hoyt:

Doug, we don't have the numbers on Medicare patients in specific zip codes. We go off of the top line of 1.25 million patients that are out there and only 16,000 of those guys are on Medicare. You can back into how significant the metropolitan areas are in the 95% of patients that need us right now. It's going to be a significant amount of patients that are available to us.

Doug Cooper:

Right. Well, I guess, that sort of gets us to the—my next question on the Pulmonary conference and the CHEST Conference. This really is the key to driving those 1.25 million patients that could be applicable for NIB therapy to the therapy. How long would it take, do you think? I'm assuming the data is starting to convince some physicians. How long is the selling process, do you think, for these new doctors to get comfortable with the therapy?

Todd Zehnder:

It takes quite some time. I mean, just seeing what—how long it took with KPMG. We have positive momentum with our existing referral sources. That's actually the lowest hanging fruit. I mean, first thing we do is we go, we bring the data to our existing referral sources. But the next phase is really getting out to the educational communities, the educational health systems that are doing all the research and having a publishable study being presented to them through these American Thoracic Societies, COPD foundation. CHEST was the first step in that direction. But it takes doc getting out there and presenting that data in those communities and circles in order to really get to the 95% of folks faster. I mean, we're naturally going to have the momentum in our—with our own—our sales force in the way that we're presenting to our guys. But the real market opportunity is to get to the folks that aren't doing business with us today. That's just getting through the industry. I mean, the industry trade shows and conference panels.

Doug Cooper:

Todd, my final question is just on EBITDA margin. You were up a couple of hundred basis points, I guess, versus Q2 despite the increase in bad debt provision, what do you foresee for Q4 EBITDA margin or into 2020?

Todd Zehnder:

We've historically said we're going to try to get back up to those historical margins. I think that we're growing into that. There's a lot of variability from quarter-to-quarter and expenses that are either going to push things up or down, listing costs, investments into new groups, the variable compensation plan. I think, over time, we will push the margins up again. But right now, we've been so aggressive in investing into the future of the Company that we have been not concerned as much about the margin as we are getting the growth rate to continue. I think fourth quarter, I mean, just roughly, I said that we would expect it to be materially consistent with the first three quarters of the year, hopefully a little bit higher and then I think in 2020, generally, as we continue to grow this company, a lot of the costs that we've made are not going to have to be scaled along with that revenue growth. A long-winded answer for me to say that I do expect them to go up over time.

Doug Cooper:

Okay, great. Thanks very much, guys.

Todd Zehnder:

Thanks, Doug.

Operator:

All right, moving on. We'll next go through to Sarah James with Piper Jaffray.

Sarah James:

Thank you. Apologies for the technical issues earlier. First, wanted to follow up on that last question. I understand why the investments now to support growth and future margin expansion. I guess I'm just looking for a little bit more clarification on the level of growth investments that you may make in ‘20 versus '19, and if there's any difference there, if you're thinking that it's going to be sort of a flat margin year? Or if you're already at the point where you would be getting some return on investments for the ‘19 spend so it would be a little bit better than flat in ‘20?

Todd Zehnder:

In general, I would say that the technology and marketing departments are hitting more of a steady state right now. Obviously, if we get into a pretty major deployment of our patient engagement platform, that may take some additional costs, although nowhere near the materiality of the ramp that we've had this year. I would say the same thing for marketing. We're looking for marketing to deliver on the e-commerce solutions, along with some of the other branding and inside sales that we're doing. I think that the ramp on ‘19 versus ‘18 is going to be much more material even with successful solutions in both of those departments. They won't scale like they did this year.

That comes back to if we continue to deliver the growth that we've done in the past, and we haven't started talking about 2020 yet, but we continually discuss how we are going to keep growing, and I think operating leverage will come with that. Just generally, I'll restate kind of what I did to Doug, we should have higher margins in the future, all things being equal, as we continue to grow into some of these investments.

Sarah James:

Okay, that's great. On the new patient platform monitoring pilot, I know it's really early, they’ve just done a few tests, I guess, but are you able to even anecdotally give us any insight on outcomes that you're generating? Then with the 3Q rollout, are you thinking about that as payer agnostic? Or is it focused around collaboration and discussions that you're having with any particular payer?

Todd Zehnder:

Well, we're having discussions with all of our payers about the patient engagement platform right now. The preliminary data that we're seeing is that eight out of 10 of our patients in the pilot are adhering to the tablet and are actually interacting with it. They prefer to use it, which is an astounding number to me. I was thrilled to see that because you're dealing with an elderly patient, but you're finding that they're just a little bit bored at home, and the tablet gives them something to do and they're inputting their data on a daily basis. Those things are just encouraging from just a usability standpoint.

But we are very open to building out customizations with each payer. We're finding that payers are requesting of us to—can we do this? Can we do that? Well, sure, we'll do whatever you want. I mean, we're building this thing first to increase our length of stay, to make our RTs more efficient in the home, and we're totally set up to bolt-on another piece of equipment that has Bluetooth connectivity or another feature for a payer, a data point that they would like to start capturing. That way, we can just be more useful and build more of a partnership with each one of these guys through our technology solutions.

Yes, we're seeing some of those customization requests. Because we're in pilot, we're just kind of saying, yes, but let's go ahead and get past the pilot program before we can take it to the next level. But the encouraging thing is that these guys are very, very excited that we're building out this program, and I see it being us adding major value for their organization down the road.

Sarah James:

It sounds like a fantastic growth opportunity ahead for you guys. Last question here is on the Oxygen sales. You talked about last quarter, doing a rollout nationally during 3Q and perhaps that's driving towards a 20% bump in sales. Just wondering how that ended up and how the rollout is going?

Todd Zehnder:

Yes, once we rolled out O2 into the entire country, it looks like, quarter-over-quarter, sales were about double, although a very small base, and it won't impact all of our overall revenue metric, it's working. While we don't have exact percentages, we're seeing a lot of our oxygen patients are getting vents as well. We're starting to track that. The program is working. We're offering a great solution. Our service is second to none around the country with our RTs in the home. It's all about improving the customer experience, using the best technology and trying to be a full-service provider.

Sarah James:

All right. Thank you.

Todd Zehnder:

Thanks, Sarah.

Operator:

All right. Once again, everyone, that is star, one if you would like to enter the question queue.

We'll next go to John Ricodo (phon) with Current Asset Management.

John Ricodo:

Hey, guys.

Todd Zehnder:

Hey, John.

John Ricodo:

Hey. Thanks for taking my question. Can you just give us a little bit of color on puts and takes for the lower gross margin for this quarter?

Todd Zehnder:

Yes, it's a couple of things, primarily two. As the other products are starting to become more material, that will, over time, maybe put some pressure, just although oxygen is material and our sleep business isn't individually material just yet, they have lower gross margins. As we continue to grow those at a higher pace than vents, that will put a little bit of pressure. Then the other thing is that as we've geographically expanded, we do have RTs in cities that don't have the traditional patient base of, call it, the 50 to 60 patients that we like to have each RT have. We've got some labor cost waiting for the ramp in some of these cities as we've grown around the country. Those are probably the two most—the most material items to change, and look, we're going to bounce around 100 basis points from quarter-to-quarter. We had a 73% gross margin quarter, sometime in 2018. I don't see this trend going down. I think as we get more patients in some of these areas where we have the labor force, they'll continue to pop back up.

John Ricodo:

Okay. That was quite helpful. That’s it for me. Thanks, guys.

Todd Zehnder:

Okay, John. Thanks, again.

Operator:

It looks like we have no further questions at this time. I'd like to turn it back over to our speakers for any additional or closing remarks.

Todd Zehnder:

All right. We’d like to thank everybody for your time this morning, and please follow up if you have any additional questions.

Operator:

That does conclude today's conference. We thank everyone again for their participation.