NUVASIVE INC
Form 10-Q
May 01, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2018

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission File Number: 000-50744

NUVASIVE, INC.

(Exact name of registrant as specified in its charter)

Delaware	33-0768598
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

7475 Lusk Boulevard

San Diego, CA 92121

(Address of principal executive offices)

(858) 909-1800

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period than the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a small reporting company)	Small reporting company
Emerging growth company		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of April 29, 2018 there were 51,259,919 shares of the registrant's common stock (par value $0.001 per share) outstanding.

NuVasive, Inc.

Quarterly Report on Form 10-Q

March 31, 2018

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

NUVASIVE, INC.

CONSOLIDATED BALANCE SHEETS

(in thousands, except par values and share amounts)

	March 31, 2018 (Unaudited)	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$73,741	$72,803
Restricted cash and investments	—	3,901
Accounts receivable, net of allowances of $14,734 and $13,026, respectively	188,107	200,220
Inventory, net	257,982	247,138
Prepaid income taxes	16,877	17,209
Prepaid expenses and other current assets	21,102	18,792
Total current assets	557,809	560,063
Property and equipment, net	227,573	215,326
Intangible assets, net	287,600	280,774
Goodwill	563,046	536,926
Deferred tax assets	5,277	6,440
Restricted cash and investments	2,394	1,494
Other assets	27,433	39,117
Total assets	$1,671,132	$1,640,140
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	$83,136	$75,767
Contingent consideration liabilities	11,670	18,952
Accrued payroll and related expenses	39,369	55,618
Litigation liabilities	38,190	8,150
Short-term borrowings	55,000	—
Income tax liabilities	3,899	2,908
Total current liabilities	231,264	161,395
Long-term senior convertible notes	587,716	582,920
Deferred and income tax liabilities, non-current	4,900	18,870
Other long-term liabilities	84,856	77,539
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $0.001 par value; 5,000,000 shares authorized, none outstanding	—	—
Common stock, $0.001 par value; 120,000,000 shares authorized at March 31, 2018 and December 31, 2017, 56,335,550 and 56,164,060 issued and outstanding at March 31, 2018 and December 31, 2017, respectively	60	60
Additional paid-in capital	1,358,759	1,363,549

Accumulated other comprehensive loss	(4,353)	(6,933)
(Accumulated deficit) retained earnings	(22,370)	4,762
Treasury stock at cost; 5,077,543 shares and 5,001,886 shares at March 31, 2018 and December 31, 2017, respectively	(569,700)	(565,867)
Total NuVasive, Inc. stockholders' equity	762,396	795,571
Non-controlling interest	—	3,845
Total equity	762,396	799,416
Total liabilities and equity	$1,671,132	$1,640,140

See accompanying Notes to Unaudited Consolidated Financial Statements.

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NUVASIVE, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

(unaudited)	Three Months Ended March 31, 2018	2017
Revenue		
Product revenue	$233,515	$224,955
Service revenue	27,007	24,058
Total revenue	260,522	249,013
Cost of revenue (excluding below amortization of intangible assets)		
Cost of products sold	55,191	45,901
Cost of services	18,623	15,542
Total cost of revenue	73,814	61,443
Gross profit	186,708	187,570
Operating expenses:		
Sales, marketing and administrative	146,766	140,368
Research and development	14,491	12,414
Amortization of intangible assets	12,425	12,061
Litigation liability loss	28,995	—
Business transition costs	2,253	55
Total operating expenses	204,930	164,898
Interest and other expense, net:		
Interest income	134	137
Interest expense	(9,467)	(9,799)
Other (expense) income, net	(9,703)	258
Total interest and other expense, net	(19,036)	(9,404)
(Loss) income before income taxes	(37,258)	13,268
Income tax benefit (expense)	10,126	(1,285)
Consolidated net (loss) income	$(27,132)	$11,983
Add back net loss attributable to non-controlling interest	$—	$(443)
Net (loss) income attributable to NuVasive, Inc.	$(27,132)	$12,426
Net (loss) income per share attributable to NuVasive, Inc.:		
Basic	$(0.53)	$0.25
Diluted	$(0.53)	$0.22
Weighted average shares outstanding:		
Basic	51,226	50,566
Diluted	51,226	57,786

See accompanying Notes to Unaudited Consolidated Financial Statements.

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NUVASIVE, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME

(in thousands)

(unaudited)	Three Months Ended March 31, 2018	2017
Consolidated net (loss) income	$(27,132)	$11,983
Other comprehensive income:		
Unrealized loss on marketable securities, net of tax	—	(2)
Translation adjustments, net of tax	2,579	1,859
Other comprehensive income	2,579	1,857
Total consolidated comprehensive (loss) income	(24,553)	13,840
Net loss attributable to non-controlling interest	—	(443)
Comprehensive (loss) income attributable to NuVasive, Inc.	$(24,553)	$14,283

See accompanying Notes to Unaudited Consolidated Financial Statements.

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NUVASIVE, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)	Three Months Ended March 31, 2018	2017
Operating activities:		
Consolidated net (loss) income	$(27,132)	$11,983
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation and amortization	32,090	29,510
Impairment of strategic investment	9,003	—
Amortization of non-cash interest	4,925	5,369
Stock-based compensation	4,134	7,017
Reserves on current assets	4,080	(1,998)
Other non-cash adjustments	4,456	3,013
Deferred income taxes	(12,671)	1,440
Changes in operating assets and liabilities, net of effects from acquisitions:		
Accounts receivable	16,933	1,719
Inventory	(12,126)	(13,800)
Prepaid expenses and other current assets	(1,737)	(2,614)
Accounts payable and accrued liabilities	1,579	550
Accrued payroll and related expenses	(18,493)	(12,721)
Litigation liability	30,040	—
Income taxes	1,294	(1,298)
Net cash provided by operating activities	36,375	28,170
Investing activities:		
Acquisitions and investments	(51,794)	(2,500)
Purchases of intangible assets	(2,657)	(1,249)
Purchases of property and equipment	(29,109)	(34,545)
Net cash used in investing activities	(83,560)	(38,294)
Financing activities:		
Proceeds from the issuance of common stock	336	410
Purchase of treasury stock	(2,155)	(10,356)
Payment of contingent consideration	(8,900)	—
Proceeds from revolving line of credit	65,000	—
Repayments on revolving line of credit	(10,000)	—
Other financing activities	(141)	(181)
Net cash provided by (used in) financing activities	44,140	(10,127)
Effect of exchange rate changes on cash	982	758
Decrease in cash, cash equivalents and restricted cash	(2,063)	(19,493)
Cash, cash equivalents and restricted cash at beginning of period	78,198	161,048
Cash, cash equivalents and restricted cash at end of period	$76,135	$141,555

The following table provides a reconciliation of cash, cash equivalents, and restricted cash reported on our Unaudited Consolidated Statements of Cash Flows for the periods presented:

	Three Months Ended March 31,	
	2018	2017
Cash and cash equivalents	$73,741	$134,008
Restricted cash and investments	2,394	7,547
Total cash, cash equivalents and restricted cash shown in the Unaudited Consolidated Statement of Cash Flows	$76,135	$141,555

See accompanying Notes to Unaudited Consolidated Financial Statements.

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NUVASIVE, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. Description of Business and Basis of Presentation

Description of Business

NuVasive, Inc. (the “Company” or “NuVasive”) was incorporated in Delaware on July 21, 1997, and began commercializing its products in 2001. The Company’s principal product offering includes a minimally-disruptive surgical platform called Maximum Access Surgery, or MAS. The MAS platform combines three categories of solutions that collectively minimize soft tissue disruption during spine fusion surgery, provide maximum visualization and are designed to enable safe and reproducible outcomes for the surgeon and the patient. The platform includes the Company’s proprietary software-driven nerve detection and avoidance systems and Intraoperative Monitoring (“IOM”) services and support; MaXcess, an integrated split-blade retractor system; and a wide variety of specialized implants and biologics. To assist with surgical procedures the Company offers a technology platform called Integrated Global Alignment (“iGA”); in which products and computer assisted technology under the MAS platform help achieve more precise spinal alignment. The individual components of the MAS platform, and many of the Company’s products, can also be used in open or traditional spine surgery. The Company continues to focus research and development efforts to expand its MAS product platform and advance the applications of its unique technology into procedurally-integrated surgical solutions. The Company dedicates significant resources toward training spine surgeons on its unique technology and products.

The Company’s primary business model is to loan its MAS systems to surgeons and hospitals that purchase implants, biologics and disposables for use in individual procedures. In addition, for larger customers, the Company’s proprietary nerve monitoring systems, MaXcess and surgical instrument sets are placed with hospitals for an extended period at no up-front cost to them. The Company also offers a range of bone allograft in patented saline packaging, disposables and spine implants, which include its branded CoRoent products and fixation devices such as rods, plates and screws. The Company sells MAS instrument sets, MaXcess and nerve monitoring systems to hospitals, however, such sales are immaterial to the Company’s results of operations.

The Company also designs and sells expandable growing rod implant systems that can be non-invasively lengthened following implantation with precise, incremental adjustments via an external remote controller using magnetic technology called MAGnetic External Control, or MAGEC, which allows for the minimally invasive treatment of early-onset and adolescent scoliosis. This technology is also the basis for the Company’s PRECICE limb lengthening system, which allows for the correction of long bone limb length discrepancy, as well as enhanced bone healing in patients that have experienced traumatic injury.

The Company intends to continue development on a wide variety of projects intended to broaden surgical applications for greater procedural integration of its MAS techniques and additional applications of the MAGEC technology. Such applications include tumor, trauma, and deformity, as well as increased fixation options, sagittal alignment products, imaging and navigation. The Company also expects to continue expanding its other product and services offerings as it executes on its strategy to offer customers an end-to-end, integrated procedural solution for spine surgery. The Company intends to continue to pursue business and technology acquisition targets and strategic partnerships.

Basis of Presentation and Principles of Consolidation

The accompanying Unaudited Consolidated Financial Statements include the accounts of the Company and its majority-owned or controlled subsidiaries, collectively referred to as either NuVasive or the Company. The Company translates the financial statements of its foreign subsidiaries using end-of-period exchange rates for assets and liabilities and average exchange rates during each reporting period for results of operations. When there is a portion of equity in an acquired subsidiary not attributable, directly or indirectly, to the respective parent entity, the Company records the fair value of the non-controlling interest at the acquisition date and classifies the amounts attributable to non-controlling interest separately in equity in the Company's Consolidated Financial Statements. Any subsequent changes in a parent's ownership interest while the parent retains its controlling financial interest in its subsidiary are accounted for as equity transactions. All significant intercompany balances and transactions have been eliminated in consolidation.

The accompanying Unaudited Consolidated Financial Statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”). Pursuant to these rules and regulations, the Company has condensed or omitted certain information and footnote disclosures it normally includes in its annual Consolidated Financial Statements prepared in accordance with generally accepted accounting principles in the United States (“GAAP”). Operating results for the three months ended March 31, 2018 are not necessarily indicative of the results that may be expected for any other interim period or for the full year. These Unaudited Consolidated Financial Statements should be read in conjunction with the audited Consolidated Financial Statements and notes thereto for the year ended December 31, 2017 included in the Company’s Annual Report on Form 10-K filed with the SEC. In the opinion of management, the Unaudited Consolidated Financial Statements and notes thereto include all adjustments that are of a normal and recurring nature that are necessary for the fair presentation of the Company’s financial position and of the results of operations and cash flows for the periods presented.

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The Company has reclassified historically presented revenue and cost of revenue to conform to the current year presentation, which now reflects revenue and costs allocated to the Company’s product and service offerings. These reclassifications had no impact on previously reported results of operations. Additionally, as required by Accounting Standards Update 2014-09 Revenue from Contracts with Customers (“ASU 2014-09”), on January 1, 2018 the Company adopted Accounting Standards Codification 606 Revenue from Contracts with Customers (“ASC 606”), electing full retrospective method of adoption.

Use of Estimates

To prepare financial statements in conformity with GAAP, management must make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Recent Accounting Pronouncements Not Yet Adopted

In February 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update No. 2016-02, Leases, which outlines a comprehensive lease accounting model and supersedes the current lease guidance. The new accounting standard requires lessees to recognize lease liabilities and corresponding right-of-use assets for all leases with lease terms of greater than twelve months. It also changes the definition of a lease and expands the disclosure requirements of lease arrangements. The new accounting standard must be adopted using the modified retrospective approach and will be effective for the Company starting in the first quarter of fiscal 2019. Early adoption is permitted. The Company believes the adoption will modify its analyses and disclosures of lease agreements considering operating leases are a significant portion of the Company’s total lease commitments. The Company is in the process of determining the impact the adoption will have on its Consolidated Financial Statements.

In June 2016, the FASB issued Accounting Standards Update No. 2016-13, Financial Instruments – Credit Losses, which changes the accounting for recognizing impairments of financial assets. Under the new guidance, credit losses for certain types of financial instruments will be estimated based on expected losses. The new guidance also modifies the impairment models for available-for-sale debt securities and for purchased financial assets with credit deterioration since their origination. The new guidance will be effective for the Company starting in the first quarter of fiscal 2021. Early adoption is permitted starting in the first quarter of fiscal 2020. The Company believes the adoption will modify the way the Company analyzes financial instruments, but it does not anticipate a material impact on results of operations. The Company is in the process of determining the effects the adoption will have on its Consolidated Financial Statements as well as whether to early adopt the new guidance.

In January 2017, the FASB issued Accounting Standards Update No. 2017-04, Intangibles – Goodwill and Other, which eliminates the requirement to calculate the implied fair value of goodwill to measure a goodwill impairment charge. Instead, entities will record an impairment charge based on the excess of a reporting unit’s carrying amount over its fair value. The standard has tiered effective dates, starting in 2020 for calendar-year public business entities that meet the definition of an SEC filer. Early adoption is permitted for annual and interim goodwill impairment testing dates after January 1, 2017. The Company is in the process of determining the effects the adoption will have on its Consolidated Financial Statements as well as whether to early adopt the new guidance.

In July 2017, the FASB issued Accounting Standards Update No. 2017-11, Earnings Per Share, Distinguishing Liabilities from Equity, Derivatives and Hedging, which changes the accounting treatment and the earnings per share calculation for certain instruments with down round features. The amendments in this update should be applied using a cumulative-effect adjustment as of the beginning of the fiscal year of adoption or retrospective adjustment to each period presented. This update is effective for annual periods beginning after December 15, 2018, and interim periods within those periods and early adoption is permitted. The Company is in the process of determining the impact the adoption will have on its Consolidated Financial Statements as well as whether to early adopt the new guidance.

In August 2017, the FASB issued Accounting Standards Update No. 2017-12, Derivatives and Hedging, which is intended to more closely align hedge accounting with companies' risk management strategies, simplify the application of hedge accounting and increase transparency as to the scope and results of hedging programs. The amendments in this update will be applied using a cumulative-effect adjustment as of the beginning of the fiscal year of adoption. This update is effective for annual periods beginning after December 15, 2018, and interim periods within those periods and early adoption is permitted. The Company is in the process of determining the impact the adoption will have on its Consolidated Financial Statements as well as whether to early adopt the new guidance.

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Recently Adopted Accounting Standards

In May 2014, the FASB issued Accounting Standard Update No. 2014-09 Revenue from Contracts with Customers (“ASU 2014-09”), an updated standard on revenue recognition. The standard effectively replaces Accounting Standards Codification 605 Revenue Recognition (“ASC 605”) with Accounting Standards Codification 606