

INTRICON, #4129895
INTRICON 2nd QUARTER 2009 RESULTS
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Chairperson: Mark Gorder (Mgmt.)

Operator: Good afternoon, ladies and gentlemen. Thank you so much for standing by, and welcome to the IntriCon Second Quarter 2009 Results conference call. During today's presentation, all parties will be in a listen-only mode. Following the presentation, the conference will be opened for questions. If you have a question, please press the star followed by the one on your touch-tone phone. Once making that choice, if you decide you'd like to withdraw your question, pressing the star followed by the two will remove your line from the queue. If you're using speaker equipment today, please note that you will need to lift up your handset prior to making your selection. As a reminder, the conference is being recorded today on Thursday, the 13th of August, 2009.

I'll now turn the conference over to Mr. Scott Longval, IntriCon's Chief Financial Officer. Please go ahead.

Scott Longval: Thank you, Operator. Joining me on today's call is Mark Gorder, IntriCon's CEO. Before we begin, I'd like to preface our remarks with the customary Safe Harbor statement.

Today's conference call contains certain forward-looking statements. These statements are based on the current estimates and assumptions of IntriCon's management, and are subject to uncertainty and changes in circumstances. Given these uncertainties, you should not place undue reliance on these forward-looking statements. Actual results may vary materially from the expectations contained in today's call. Important factors that could cause such differences include, amongst others, those set forth under the heading Risk Factors, and management's discussion and analysis of the financial conditions and results of operations in our 10-K filing for the year ended December 31st, 2008.

With that, I'd now like to introduce Mark Gorder, for a strategic look at IntriCon's second quarter.

Mark Gorder: Thank you, Scott, and thank you, everyone, for joining us today. I would like to begin by reviewing our 2009 second quarter results and key highlights for the company. Then I will discuss our strategy and growth plan, including today's announcement of the acquisition of Datrix, an Escondido California based supplier of cardiac diagnostic monitoring devices. After that, Scott will cover the financials in more detail, and then we'll open up the call for questions.

At this time, most of you have had a chance to review our second quarter press release. Second quarter conditions were consistent with what we've been experiencing over the past year. The overall selling environment remains challenging, and while we are starting to see sales improvements in some areas,

customers are cautiously working through their inventories, and delaying projects due to economic uncertainties and lower demand.

Our hearing health, and professional audio communications businesses declined year-over-year, but sequentially they grew 13.6% and 8.4% respectively for the 2008 first quarter.

A continued bright spot is our medical business, which grew more than 12.5% over the prior year. We are very pleased with this performance. Business with our two largest medical OEM customers remains strong, driving the second quarter gain in revenues for this area. The fact is that medical has been strong despite the economy. From a revenue standpoint, it's about 40% of our business, and we're looking to increase that.

In hearing health, patients continued to delay hearing aid purchases, resulting in lower sales levels. We believe that this market will show moderate growth in the second half of 2009. As we've said before, the hearing health market isn't shrinking, rather, it's an issue of timing.

In professional audio, customers continue to work through existing inventories. The company believes this business will experience sequential growth over the first half of the year, as key customers begin to replenish their inventory levels.

We feel that prospects in both professional audio communications and hearing health remain solid in the longer-term, yet sales are sluggish at this point given current economic conditions.

Our non-core electronics business continues to adversely impact the company's performance, with net sales declining 15% from the year earlier second quarter, and 26.1% from the prior year six months. In addition to reducing the cost structure of the non-core business, IntriCon is exploring all strategic options.

Looking forward to the rest of 2009, we will continue to conservatively manage our business by reducing expenses given current market conditions. To date, we have reduced our workforce, implemented temporary tiered wage decreases, suspended the company's 401(k) match, and eliminated all non-essential spending. This will reduce expenses by an estimated 1.7 million annually.

We remained focused on staying cash flow positive while prudently investing in our strategic research and development initiatives. Based on what we're seeing, we expect that customers will cautiously begin to replenish inventory levels, and re-engage projects during the remainder of 2009. This should drive modest sequential sales gains.

Earlier today, IntriCon announced the acquisition of Datrix, a supplier of patient monitoring devices with worldwide distribution to leading medical OEMs. In addition to manufacturing halter monitors, portable devices for continuously monitoring the electrical activity of the heart, Datrix also designs and

manufactures equipment for electrocardiograph, or ECG management systems, including a 12 channel handheld ECG with Wi-Fi capability.

This deal is an exciting opportunity for IntriCon. We gain entry into what we believe to be an \$80 million cardiac diagnostic monitoring, or CDM market, with a particular emphasis on the emerging biotelemetry space. We intend to leverage Datrix cardiac monitoring capabilities that incorporate IntriCon's ultra low power wireless technology to develop and launch a new wireless cardiac monitoring device that will be able to identify asymptomatic cardiac events, including atrial fibrillation, bradyarrhythmia, tachyarrhythmia, and cardiac pause.

We intend to unveil a prototype of this new CDM device, called the Mobile Patient ECG Telemetry Systems, or MPETS, at the 2009 American Heart Association Scientific Sessions, November 15th to 17th in Orlando, Florida.

The MPETS is the next generation in wireless outpatient monitoring, using the proven automatic arrhythmia detection algorithm. Additionally, IntriCon Datrix will also launch a prototype ECG telemetry acquisition over cell device, called and ETAC, that records a patient's heartbeat when a possible atypical cardiac event is experienced. The new ETAC event monitor will also have an optional wireless module.

To help finance the transaction, we signed a new credit facility with a private bank and trust company based in Minneapolis. The 11.5 million debt facility offers IntriCon the financial ability to expand and pursue new opportunities at favorable terms. The fact that we were able to secure access to capital in today's challenging environment, reflects the private bank's belief in IntriCon, and our ability to succeed.

In the biotelemetry arena, IntriCon remains active, with strategic partner Advanced Medical Electronics, AME. The company continues to work to develop devices that wirelessly transmit critical diagnostic and therapeutic information. In collaboration with AME, IntriCon has received approvals for grant funding for eight development programs, and is in the process of applying for several more.

Let's talk briefly about our plan for the remainder of 2009. IntriCon is taking definitive steps to further our position as a body worn device company. Moreover, we're committed to R&D to drive new product development, while partnering with leaders in the body worn device space, and we're acquiring the key technologies we need to succeed. And we continue to pursue our ambition of connecting people and devices in the medical hearing health and professional audio communications markets.

As I said in today's release, the future is clear. The marketplace is moving towards wireless body worn devices that offer critical monitoring capabilities. We're seeing that in all of our businesses. We intend to support OEMs in the

marketplace with new devices, and continue to prudently invest in new initiatives that we believe will fuel long-term growth.

Now I would like to turn the call back to Scott for an in-depth discussion of our financial performance. Scott?

Scott Longval:

Thank you, Mark. For the second quarter, IntriCon reported net sales of \$14 million versus net sales of 17.5 million for the 2008 second quarter. The decline was due to the factors Mark just detailed. Sequentially, however, sales increased by 4.8% in the 2009 first quarter. This gain, when combined with additional cost reductions, reduced IntriCon's sequential net loss by \$400,000 in the 2009 first quarter.

Our 2009 second quarter net loss was \$598,000 or \$0.11 per diluted share, compared with net income of \$410,000 or \$0.07 per diluted share for the year ago period.

For the quarter, the company's body worn device segment net loss, comprised of hearing health, professional audio communications, and medical, was 423,000 or \$0.08 per diluted share, which is income of 448,000 or \$0.08 per diluted share for the fiscal 2008 second quarter.

We recorded a non-core business net loss of 175,000 or \$0.03 per diluted share compared to a 2008 second quarter non-core net loss of 38,000 or \$0.01 per diluted share.

Company-wide, 2009 second quarter gross margins were 20.4% compared to 24.3% in the year ago quarter. The decline was primarily due to lower sales levels. Sequentially, however, gross margins improved 2.5 percentage points from 17.8% in the 2009 first quarter, primarily driven by higher margin medical sales. Core business gross margins improved sequentially as well, from 18.4% in the 2009 first quarter to 21% in the second quarter.

IntriCon continues to execute gross margin improvement initiatives, such as the implementation of Lean Six Sigma manufacturing principles in its various manufacturing facilities. Current efforts have driven annual savings of approximately \$160,000.

As Mark mentioned, we're starting to see glimpses of the light at the end of the tunnel, but we're certainly still being impacted by a slow selling environment, and we're taking the necessarily measures instead by controlling costs, and conserving cash while driving revenue as hard as we can.

As we announced in our first quarter conference call, we implemented a cost reduction program in the second quarter, including temporary tiered wage reductions, suspension of the 401(k) match, and elimination of all non-essential spending. This program will remain in effect until we see a marked improvement in financial results.

While it is critical that we wisely manage through the short-term, we will not lose sight on our long-term strategic growth plan. As evidenced by our acquisition of Datrix, our focus remains on growth, and our continued commitment to prudent investments, not only in our proprietary technology, but also in key strategic initiatives. That is what we believe will drive new products and future revenue growth.

For the six month period, we reported net sales of 27.3 million, and a net loss of 1.6 million, or \$0.30 per diluted share. This compares to 2008 net sales of 31, excuse me, 34.1 million, and net income of 560,000, or \$0.10 per diluted share.

The six month net loss from the company's core business was 2.1 million or \$0.23 per diluted share, with a non-core loss of 357,000 or \$0.07 per diluted share.

For the six months ended June 30th, 2008, the core net income was 655,000 or \$0.12 per diluted share. The non-core business net loss was 95,000 or \$0.02 per diluted share.

From a cash management perspective, as Mark noted, IntriCon has a new \$11.5 million debt facility with a private bank, consisting of an \$8 million revolver, and a \$3.5 million term note related to the acquisition of Datrix. As of June 2009, the company had \$3.4 million outstanding on the revolver, and 2.5 million outstanding on the note.

IntriCon has an international revolver of 1.8 million, of which 548,000 was outstanding at the end of June. They also had 2.—1.2 million of capital leases outstanding at the end of June. The total funded debt was 7.6 million at the end of June compared to 7.7 million at the end of fiscal 2008.

Non-restricted cash on hand at June 30th, 2009 was 173,000 compared to 244,000 at the end of the first quarter. The company's current ratio was 2.—was 2.0%, 2.0 at the end of June, versus 2.1 at the end of March.

With respect to our cash management metrics, our total cash cycle days was 92 days, using a three month rolling average. This is consistent with the first quarter of 2009. As a reminder, cash cycle days comprised of days sales outstanding, or DSOs, was 56 days at the end of June, plus inventory outstanding, which was 74 days at the same point, less days payable outstanding, which stood at 38 days at the end of June 30th.

Now I'd like to turn the call back over to the Operator so we can answer any of your questions.

Operator:

All right, thank you. And ladies and gentlemen, at this time we will begin the question and answer session. As a reminder, if you do have a question at this time, please press the star followed by the one on your touch-tone phone. Once you make that choice, if you decide you'd like to withdraw your question, please

press the star followed by the two. That will remove your line from the queue. And if you are using speaker equipment today, please note that you will need to lift up your handset prior to making your selection. Once again, if you do have a question at this time, please press the star followed by the one now.

And I have no questions registered. Once again, if you do have a question you wish to ask, please press the star followed by the one at this time. If you are on speaker equipment, you will need to lift your handset before making that selection.

And we do have a question from the line of Alvin Hoffman [ph] with Boenning & Scattergood. Please go ahead.

Alvin Hoffman: Yes, good afternoon. Where does your, let's say, your super-duper wireless hearing aids stand as far as being into the market in the United States, or in the 13 European countries?

Mark Gorder: Good afternoon, Alvin, it's Mark Gorder. I'll take that question. The, we've got two wireless initiatives. One is called, is a nanoLink radio that's aimed at the med-radio [ph] band, which is a 402 to 405 megahertz band in the United States that was initially directed at implants; was later amended this past year by the FCC [ph] to include sidebands to allow for non-implantable devices. There were, however, some restrictions on the sidebands that delayed using our nanoLink in the US market pending further FCC discussions.

In the European side of things, the technology is currently being used by one of our customers in the European market for a particular application, and we're intending to apply for additional applications to the European authorities, which I believe is called ETSI, E-T-S-I. It's a—I don't know the exact wording of that algorithm, but that's the—equivalent to the FCC. So we have regulatory initiatives that need to be pushed forward over the next six months to continue to move this technology into the marketplace. We feel that we've made some progress, and we have an initiative going with myself and the VP of R&D to further those efforts to get the technology in more applications.

We have an additional radio that we're calling our, it's a 2.4 megahertz radio with a, based on a Nordic radio chip, that we intend to—it has no regulatory impediments, and we're in the process of developing a series of hearing aid accessories that would operate at that frequency for use with remote microphones, with television transmission, and so forth, directly to a ear worn receiver. And we intend to have that technology on the marketplace in the first quarter of next year.

So we've got two initiatives going, both of which are low power radio technologies for the hearing aid market. One, which is experiencing some regulatory headwinds, which we ultimately think we'll be able to overcome, and the other one which we'll have products on the marketplace by Q1 on 2010.

Alvin Hoffman: And this one product that's in the market, is that a hearing aid?

Mark Gorder: Yes, it is.

Alvin Hoffman: Can you tell me the company?

Mark Gorder: I cannot.

Alvin Hoffman: It's a European [talk over]?

Mark Gorder: It's a European company.

Alvin Hoffman: Yes. Okay. Just wondered where it stood.

Mark Gorder: We also have some uses of the technology with some of our government customers, but we can't discuss anything about that. They're in uses that we're restricted from discussing.

Alvin Hoffman: I see. For people who are in the market for cardiac monitoring now, how will this company for the product you just bought, compete, let's say, [inaudible] these companies that are already in the market monitoring cardiac activity?

Mark Gorder: I don't, I don't know if you've followed the market recently, but there's been a very dynamic environment in the cardiac diagnostic monitoring as of late. If you'd followed the CardioNet [ph] attempted to do an acquisition of a company here in the Twin Cities called BioTell [ph], which is one of the three or four largest independent OEM suppliers of cardiac diagnostic monitoring devices. But ultimately that deal fell apart due to a number of circumstances.

But the environment has been created where the need for alternate sources has definitely been opened up as a result of the current dynamic environment, and we think that IntriCon's size, the technology that it brings to bear, and the fact that we can significantly lower the costs and improve the performances of these devices will make us a very formidable competitor in the OEM device market.

We have—we've already won government funding through our partner Advanced Medical Electronics for a significantly reduced and miniaturized version of a cardiac diagnostic monitor with wireless capability, and we intend to infuse the technologies that we've developed into the product lines that Datrix is working on to miniaturize these products and make them more cost effective, and make them more effective in performing their diagnostic requirements.

So we think that this is a very good market for us to enter because of the skills that we bring to bear, and Datrix being a smaller entity, is now significantly enhanced by being connected with us, and we think that's going to bode well for our future growth in that market.

Alvin Hoffman: Do you intend to market this directly or through other people already in the market?

Mark Gorder: Well we are an OEM supplier, so we would anticipate going to companies like CardioNet, Phillips Medical [ph], GE Medical [ph], and several other of the major suppliers of cardiac monitoring systems, to get them to incorporate our body worn diagnostic monitors into their cardiac systems.

Alvin Hoffman: Yes. [Unintelligible] and recently show [ph] a 20% and reduction and reimbursement, and, that—you know—[inaudible] their income dramatically?

Mark Gorder: That'll have some impact on the scanning services, but the—there are three types of devices, cardiac diagnostic devices that are sold in the market. The halter monitor is kind of the lower, the lower cost version. It doesn't have wireless capability. It's just strapped onto the patient, and used for collecting the data, which is then brought back to the clinic and analyzed. And that market's not affected by this reimbursement at all. And the product line from Datrix is primarily, at this point, halter monitors.

The, our future intent is to be a big player in the mobile cardiac outpatient telemetry market, which has been opened up by these new reimbursement codes, which, as you correctly stated, have been reduced from, I think, it was over \$1,100 per...

Alvin Hoffman: Experience?

Mark Gorder: Per experience, down to somewhere around \$700 per experience. The effect that this will have on the overall device market may shift or reduce the speed at which MCOT [ph] would be—would take up the market share, but in the long run, the market share will be split between the halter monitors, the event recorders, and the new MCOT devices. And we intend to have a position in all three of those product lines. So we feel that regardless of what happens, the market's going to grow. It's serving an aging population, and whether it's MCOT, event, or halter monitors, the number of units is going to grow.

Alvin Hoffman: I see. This is—the situation that you're competing with other manufactures rather than the people who are distributors?

Mark Gorder: Correct. We do not want to be competing with the distributors. They're going to be our customers.

Alvin Hoffman: Okay.

Mark Gorder: Our model will be strictly OEM.

Alvin Hoffman: How did Datrix distribute in the past to the market?

Mark Gorder: They did—they're just a very small company, Alvin. They have—they had sales agents, representatives that called on the OEM accounts. Occasionally, John Baron, the CEO of Datrix would assist those reps to close through their sale.

Alvin Hoffman: I see. [Inaudible] for the OEMs?

Mark Gorder: Yes.

Alvin Hoffman: Oh. And it won't change?

Mark Gorder: That won't change. Our intent is to ultimately do direct sales, and we think that's more effective for our type of OEM environment.

Alvin Hoffman: Thank you.

Operator: Thank you. Once again ladies and gentlemen, if there are any additional questions at this time, please press the star followed by the one now. Once again, if you're listening via speaker equipment, you will need to lift your handset before making that selection. Star, one with a question at this time.

And, Mr. Gorder, there are no further questions. Please continue with any closing remarks you may have.

Mark Gorder: Once again, thank you for taking time out of your day to join the call. IntriCon is taking definitive steps to further our position as a body worn device company. We are very excited about the Datrix acquisition and entrance into the cardiac diagnostic market. We believe this is a very exciting market with strong fundamentals. We're committed to R&D to drive new product development, we're partnering with leaders in the body worn device space, and we're acquiring the key technologies we need to succeed. And we continue to pursue our ambition of connecting people and devices in the medical, hearing health, and professional audio communications markets.

Thank you, again. We look forward to updating you on our progress in the future.

Operator: Thank you. And ladies and gentlemen, this concludes the IntriCon Second Quarter 2009 conference call. If you would like to listen to a replay of today's conference, you can do so by dialing 1-800-406-7325, or 303-590-3030, input the access code 4129895. ACT would like to thank you very much for your participation today, and you may now disconnect. Have a very pleasant rest of your day.

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