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EDITED TRANSCRIPT

MDRX - Q2 2018 Allscripts Healthcare Solutions Inc Earnings Call

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OVERVIEW:

Co. reported GAAP revenue of \$526m, non-GAAP net income attributed to Co. of \$33m and GAAP EPS of \$0.36. Expects 2018 non-GAAP revenue to be \$2.15-2.25b and non-GAAP diluted EPS to be \$0.72-0.82.



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PRESENTATION**Operator**

Greetings, and welcome to Allscripts Second Quarter 2018 Earnings Call. (Operator Instructions) As a reminder, this conference is being recorded. I would now like to turn the conference over to your host, Stephen Shulstein. Thank you. You may begin.

Stephen Shulstein - *Allscripts Healthcare Solutions, Inc. - VP, Investor Relations*

Thank you very much. Good afternoon, and welcome to the Allscripts Second Quarter 2018 Earnings Conference Call. Our speakers today are Paul Black, Allscripts Chief Executive Officer; Rick Poulton, our President; and Dennis Olis, our Chief Financial Officer.

We'll be making a number of forward-looking statements during this presentation and the Q&A part of the call.

These statements are based on current expectations and involve a number of risks and uncertainties that could cause our actual results to vary materially.

We undertake no obligation to revise these forward-looking statements in light of new information or future events.

Please refer to our earnings release and SEC filings for more detailed descriptions of the risk factors that may affect our results.

Please reference the GAAP and non-GAAP financial statements as well as the non-GAAP tables in our earnings release and the supplemental workbook that are both available on our Investor Relations website.

And with that, I'm going to hand the call over to Rick Poulton.



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Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Okay. Thanks, Stephen. Good afternoon, everybody, and thanks for joining our call today. We appreciate your time and your interest in Allscripts.

I'm going to cover two key topics today. First, I'll make some summary comments on second quarter performance and highlight some important achievements we saw in the quarter, and then I'll make a couple of comments and thoughts around our current portfolio.

So let's start with the second quarter results. We're pleased with our strong revenue and earnings performance. On a year-over-year basis, we reported 23% growth in GAAP revenue to \$526 million, 25% growth in non-GAAP revenue to \$536 million and 20% growth in non-GAAP earnings per share to \$0.18 a share.

Our recurring revenue was 80% of total revenue in the quarter, and this is the third quarter in a row at or above this level. So it provides us with a significant amount of revenue visibility over the near and medium term and lessens our reliance on in-year new bookings.

Speaking of bookings, while we faced tough bookings comps year-over-year, which would have presented a difficulty under any circumstances, we were a bit disappointed with this quarter's booking results of \$278 million. As you've seen and heard as well from some of our competitors, no regulatory event forcing buying behavior here in the U.S. The market has moved to ROI-driven demand. This is an inherently longer sales cycle and more difficult to predict.

Additionally, in international markets, budget processes and layers of government approvals also make the timing of deals very difficult to predict. So we remain very confident in our pipeline of opportunities, but we should continue to expect to see some quarter-to-quarter volatility in bookings.

Combined with our record first-quarter performance in bookings, our year-to-date numbers are largely in line with our revenue growth expectations for the year.

So now let me highlight some client activity during the quarter. In the hospital and health system market, we signed a multiyear deal for full IT outsourcing for a multi-facility hospital in Maine. This client looked to Allscripts to optimize their IT performance and centralize services. This is the first managed services deal with an EIS client since we completed the acquisition.

We also signed a five-year deal with Clark Memorial Hospital to extend our business with the addition of Sunrise surgical and anesthesia modules. And we believe we're well positioned there to extend our relationship even further.

We saw the benefits of cross-selling our above-the-EHR solutions, and we have a good example at Genesis, which is a 500-doctor practice, which is part of Ascension. Genesis invested in our 2bPrecise solution, and the physicians are incredibly excited to be able to leverage this precision medicine technology to determine best practice protocols and deliver the best possible care. We believe this is just scratching the surface of the capabilities we'll be able to provide and deploy, and we are aggressively marketing 2bPrecise inside and outside of our EHR client base.

Turning to the ambulatory market. We also had a number of wins I'd like to highlight. Grants Pass, an existing TouchWorks EHR client, displaced a competitor's practice management solution and adopted Allscripts PM, along with our revenue cycle management services. We're very pleased to announce that on June 15, we released a new version of Allscripts PM that delivers on our promise of continued automation and enhanced users efficiencies. Client feedback has been extremely positive, and this release has allowed Concentra to accelerate their rollout of Allscripts PM to over 530 of their urgent care centers.

Also in the ambulatory market, Practice Fusion has achieved and enrolled tens of thousands of subscription sign-ups. Overall, has exceeded our expectations. As a reminder, we acquired Practice Fusion in the first quarter, and we moved to the subscription model on June 1.

In our Payer and Life Sciences business, we experienced strong results for our pharma and CRO activity, and we see this trend continuing for the foreseeable future. As our PLS business now approaches 10% of enterprise revenue, we believe we are building critical mass high-growth sector of the market our strategy to invest in this area, and we continue to see some very strong results.

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Our Payer and Life Sciences team are successfully our direct-to-biopharma strategy to address the evolving health care ecosystem needs, including use of real-world data derived from the point of care, transforming clinical trial management to accelerate and effectively reduce costs.

On the payer front, we signed a significant deal with Blue Cross Blue Shield Association for two plans, which collectively represent 7.5 million members, to more efficiently connect them to their network of physicians at the point of care. We've got a great opportunity to expand this into the broader BCBS plan network.

On the consumer front, we closed the acquisition of HealthGrid in the second quarter. HealthGrid is a very innovative way to reach a very large patient population. They are an award-winning consumer engagement platform, and we have a very widely deployed consumer engagement solution through FollowMyHealth. Combining these new capabilities with this existing footprint is exactly what the market needs right now.

If you look at overall patient engagement across the U.S. today, it's been primarily focused on patient portals. But when you dig into patient portals, the adoption rate is fairly low. We see 15% to 20% of the overall population actually using that tool.

HealthGrid expands on this and expands on our approach to patient engagement and will communicate with you no matter where you are and no matter what device you're on. If you're at home, they'll use interactive voice solutions. If you're on your cell phone, they'll communicate via your cell phone. We see a meaningful opportunity to engage patients and grow this platform with our FollowMyHealth clients as well as selling it outside of our customer base.

On the international front, we are pleased to announce a new client as Maidstone and Turnbridge Wells NHS Trust selected the Allscripts Sunrise solution as its Electronic Health Record. This is a move that significantly strengthens the company's position in the southeast of England. This trust, which runs two major hospitals and a specialist cancer service, already uses the Allscripts Patient Administration System, following a go-live last October and now it'll rollout the Sunrise clinical suite in a phased deployment.

And finally, in the post-acute market, Netsmart experienced continued strong new customer acquisitions, including more than 40 on its new cloud platform that I mentioned last quarter called myUnity. Overall, growth at Netsmart continues to be driven by new client wins and expanding services to existing clients.

Also in the quarter, Netsmart closed the acquisition of the home care and hospice solutions of Change Healthcare. This was a deal we had previewed for you last quarter. As we discussed at that time, this acquisition now cements Netsmart as a leading provider of solutions for the home care and hospice markets, adding to the leadership position they have long held in behavioral health and human services.

So seizing on the momentum we've created at Netsmart, during the quarter, we took further steps to position ourselves to unlock value for shareholders through monetizing our investment in Netsmart. After researching and discussing several possible alternatives, we began detailed negotiations with multiple parties on the sale of our interests. We have signed a letter of intent, and buyer diligence currently continues. Based on the work accomplished to date, we expect to enter a definitive documentation on the sale during the third quarter. We will continue to update you on any progress on these discussions. Obviously, to the extent we conclude a transaction, we will cease to consolidate Netsmart in our financial results. And so accordingly, we will update our financial guidance as close timing becomes more apparent.

So with that, I'll now turn the call back over to Dennis to go through more of the financial details for the quarter.

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Thanks, Rick. As we review this quarter's numbers, please reference the schedules in the earnings release as well as the supplemental data workbook available on the Allscripts Investor Relations website.

For clarity purposes, let me make a few opening remarks before diving into the results.

First, my comments on the income statement will largely focus on non-GAAP metrics unless otherwise stated.

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Full reconciliations of GAAP and non-GAAP figures are available in the earnings release.

Second, effective January 1, 2018, we adopted the new 606 revenue recognition standard using the modified retrospective approach. The adoption of the new standard resulted in a mid-single-digit adjustment to revenue and income and therefore, did not materially impact our second quarter results. As such, all references to our current results are made after applying revenue recognition standard. Please review our 10-Q for further disclosures around the new standard.

Third, as a reminder, we closed the Practice Fusion transaction on February 15 of this year and began consolidating the results as of that date. Q2 includes a full quarter contribution from both Practice Fusion and from EIS, which closed back in October of 2017.

Lastly, the divestiture of our OneContent business closed on April 2 of this year, and therefore, our Q2 results do not include a financial data from this business unit.

As Rick noted, Q2 bookings totaled \$278 million in the quarter. As a result, our backlog now stands at a record \$4.8 billion. This reflects both the impact of bookings as well as a substantial number of renewals in the quarter that are not included in the bookings metric.

Turning to the income statement. Second quarter non-GAAP revenue totaled \$536 million, an increase of \$108 million or 25% versus Q2 of 2017. Non-GAAP revenue added \$10 million in acquisition-related deferred adjustments in the second quarter of 2018. In the second quarter of 2017, this adjustment totaled \$2 million, and therefore, the Q2 2018 GAAP revenue of \$526 million represents a 23% growth versus the second quarter of a year ago.

Netsmart's Q2 non-GAAP revenue totaled \$87 million in the quarter, growing 9% year-over-year. EIS contributed non-GAAP revenue of \$72 million in the quarter. As a reminder, this excludes OneContent and is in line with our expectations for the EIS business. This also includes the EIS portion of the acquisition-related deferred revenue adjustment of \$8.5 million.

Looking at our total revenue split. Total recurring revenue grew 31%, and nonrecurring revenue grew 6% versus the same period a year ago. Thus, our total recurring revenue mix came in at 80%. As discussed in the previous couple of quarters, as we incorporate the 606 revenue recognition changes in our 2018 reporting, there will be some volatility in this measurement throughout the year. However, we expand to trend in the high 70% to low 80% range during 2018.

Looking at revenue results by line item. Total software revenue in Q2 increased 24% year-over-year and now totals \$341 million. Recurring software revenue, consisting of subscriptions, recurring transactions, support and new maintenance, increased 32% year-over-year. A large portion of this growth was driven by the consolidation of the EIS business.

In the quarter, nonrecurring software revenue decreased 13% year-over-year.

Turning to client services. Consolidated non-GAAP revenue grew 28% year-over-year to \$194 million in Q2. Recurring service revenue increased 29% year-over-year, driven by revenue cycle services and other multiyear service offerings and the addition of EIS. Similar offerings from Netsmart such as hosting, revenue cycle services and managed services also contributed to this increase. Allscripts nonrecurring service revenue increased 26% year-over-year, driven primarily by the EIS acquisition.

Moving to non-GAAP gross margin. Total gross margin was down 100 basis points year-over-year, primarily attributed to acquisitions in our core business and at Netsmart. Our gross margin was down 30 basis points sequentially as we removed the high-margin OneContent business from our portfolio. This, in part, offsets some of the additional synergies we are seeing from the EIS acquisition. We still anticipate that we will see gross margin expand sequentially in the back half of the year.

Analyzing margin by component, software gross margin decreased by 60 basis points year-over-year, and client services gross margin decreased 80 basis points from the same period.

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Looking at operating expenses. Non-GAAP SG&A totaled \$122 million, a 27% increase year-over-year. The non-GAAP SG&A figure excludes transactions related and other expenses. The increase in SG&A is primarily a function of the additional acquired expenses from EIS, Practice Fusion and HealthGrid.

Non-GAAP gross R&D was \$99 million in the quarter, up 36% year-over-year, reflecting the additional R&D expenses attributed to acquisitions at Netsmart and Allscripts. Non-GAAP R&D also excludes the transaction related and other expenses.

Our software capitalization rate in the quarter was 31%, within our expectation to be in the low 30% range in 2018.

Adjusted EBITDA totaled \$97 million, a 9% year-over-year increase. This equates to an 18% adjusted EBITDA margin. As Rick already noted last October when we made the acquisition, the EIS integration efforts will extend through 2018, and we would expect EBITDA margins to trend upward throughout the balance of the year. Netsmart adjusted EBITDA is trending in the mid-20% range as a percentage of Allscripts total reported EBITDA in line with our expectations and on track for 2018 guidance range of between \$110 million and \$120 million.

Looking below the line. Total cash interest increased 37% to \$22 million, which compares to \$16 million from a year ago. The largest contributor to this increase is the financing required to fund the EIS and Practice Fusion acquisitions.

GAAP EPS in the quarter was \$0.36 and reflects the gain associated with the OneContent divestiture less transaction related and other costs. Please note that GAAP results this quarter included transaction-related costs, severance fees and other costs of \$45 million.

Finally, excluding noncash adjustments and transaction related and other expenses, non-GAAP net income attributed to Allscripts totaled \$33 million, and total non-GAAP EPS was \$0.18 for the quarter. As a reminder, non-GAAP EPS is calculated net of noncontrolling interest to reflect Allscripts ownership portion of the partially owned, controlled and consolidated businesses.

Non-GAAP net income and attributed to Allscripts Healthcare Solutions grew approximately 20% year-over-year. We ended the quarter with a principal balance of \$694 million in secure debt and \$345 million on convertible senior notes, an \$85 million decrease in long-term debt quarter-over-quarter. The decrease reflects payments on our senior secured credit facility.

Netsmart's total debt, which is nonrecourse to Allscripts but reported for consolidation purposes, totaled \$645 million, down slightly quarter-over-quarter due to required repayments.

Turning to cash. Q2 operating cash flow totaled \$8 million compared with \$34 million a year ago. Q2 free cash flow totaled a negative \$37 million after adjusting for capital expenditures, capital software and purchased software. Our free cash flow was negatively impacted in the quarter by onetime acquisition-related payments as well as the timing of certain receivables related to the EIS business as a substantial number of EIS contracts are structured to receive payment in the first and fourth quarters.

As we've noted in the past, cash flow will vary from quarter-to-quarter. As we move into the back half of 2018, we expect free cash flow to improve as contractually timed collections from the EIS business tend to increase in the fourth quarter.

In the second quarter of this year, we repurchased \$44 million of stock. For the first half of the year, we collectively have purchased \$102 million of stock or 7.7 million shares at an average price of \$13.28. As noted earlier, we announced today that our Board approved a new stock repurchase program authorizing the company to repurchase up to \$250 million in common stock through 2020. This program replaces the previous existing program, which had been announced in 2016.

Also in the second quarter, we closed the sale of the OneContent business to Hyland for \$260 million. As a reminder, we acquired this business as part of the EIS acquisition in Q4. As a result of the sale, we realized a gain of \$178 million in the quarter.

Turning to our outlook. We are maintaining our 2018 guidance, which reflects the first half performance as well as our outlook for the back half of the year. Specifically, non-GAAP revenue of between \$2.15 billion and \$2.25 billion; adjusted EBITDA to be between \$420 million and \$460 million.



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Excluding Netsmart, adjusted EBITDA will be between \$310 million and \$340 million; and finally, non-GAAP earnings per share of between \$0.72 and \$0.82 per diluted share.

And finally, as a reminder, we continue to expect a tax rate of 27% for the full year.

And with that, I'll turn it over to Paul.

Paul M. Black - *Allscripts Healthcare Solutions, Inc. - CEO & Director*

Thanks, Dennis. Let me begin by commenting on bookings and providing additional context. We continue to generate strong double-digit revenue growth.

Our earnings per share in the second quarter of 2018 are the highest they've ever been under this management team. Our backlog stands at a record \$4.8 billion. As we've noted in the past, quarterly bookings can fluctuate.

I want to highlight a record quarterly bookings in 12 of the last 14 quarters, the last record being Q1 of 2018. While this quarter's bookings result did not meet our expectations, we remain confident in the strength of our offerings. Allscripts portfolio has tremendous depth and breadth, and our formidable software and services offerings rivals any in the industry.

This includes service solutions that provide significant and durable value to Allscripts clients who operate in a very cost-conscious and ROI-focused environment. As we continue to invest in R&D, extend our capabilities and reposition ourselves in the market, I am confident that we will win our share of new clients going forward.

We remain focused on growing our core EHR offerings. We see significant opportunities in cross-selling our solutions to our EIS-installed base, increasing our presence in international markets, maintaining our strong momentum in Payer and Life Sciences and driving adoption of our patient engagement platforms. We continue to invest in R&D for cloud offerings to enable more solutions for our clients. We believe this will help drive growth going forward.

Our open software and network communities continue to advantage our clients. Last week, the Allscripts open API platform crossed the 4 billion data share milestone. This reveals just how many Allscripts clients and certified third-party software developers are embracing open API innovation every day. They are using open APIs to achieve the functionality they want and need without ripping and replacing what they already have.

Today, more than 8,000 registered developers have accounts on Allscripts developer portal. Over 2,600 clients use these third-party applications. This vibrant community of entrepreneurs and their collective innovation creates a competitive advantage for Allscripts.

We have a proven, successful track record of identifying, integrating and growing strategic acquisitions, which drives substantial value for our company and our shareholders. We have enhanced our core EHR offering with the EIS acquisition. These assets have enabled us to better serve our clients, increasing our scale to further drive our investment in innovation. Our acquisition of HealthGrid strongly positions us in the rapidly growing consumer side of the market. We look forward to the cross-selling of this platform across the base and to new clients.

As Rick mentioned, our investment in the post-acute space through Netsmart has already generated significant value. We look forward to recognizing that value on behalf of our shareholders.

Finally, our Payer and Life Sciences business continues to demonstrate strong growth. We are extremely pleased with Practice Fusion's performance as they converted their service to a subscription model. Thousands of doctors being convinced to pay for what was previously a free offering demonstrates both the platform's value and the leadership of this seasoned team.

On the data analytics side, we look forward to our unique offerings driving additional value from our pharmaceutical clients. Overall, our acquisitions, recent divestiture of OneContent and investments in R&D allow us to create significant value for our clients and shareholders. We will continue to



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deploy a balanced capital allocation strategy as we will invest capital to drive profitable growth as well as return capital to shareholders. We remain committed to the future growth opportunities in Allscripts strategy going forward. I want to thank our associates for their hard work, our clients for their loyalty and shareholders for your confidence. We expect to reward all three stakeholders with performance.

With that summary, let's open the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question is from Michael Cherny with Bank of America Merrill Lynch.

Unidentified Analyst

This is Allan for Mike. On software delivery bookings, Rick, you mentioned the market's moving to this ROI model so the sales cycle is longer. Has this intensified over the recent quarter? Or is it more the same dynamic we've seen over the past year?

Richard J. Poulton - Allscripts Healthcare Solutions, Inc. - President

I think it's a trending -- I wouldn't say it was an acute part of intensity per se in the quarter, but I think directionally for these last several quarters you see more and more ROI focused, and I would say with that has come less predictability on both cycles, and we've had more things pushing than we would have expected.

Unidentified Analyst

Got it. And then a follow-up to that. What does Allscripts see as its highest ROI products? And are there any IT services the company's focusing on expanding where the ROI to hospitals and the physicians is relatively high?

Richard J. Poulton - Allscripts Healthcare Solutions, Inc. - President

We have tremendous ROI benefits in our solutions. So we feel great about that. Software, in general, still a great business, and our -- when we convince a client, they usually get a good reward off of it because you're automating something that was manual or otherwise had some embedded inefficiencies in it. But it's good return for us as well on the software side. So those are clearly where our best margins are. But we have some service opportunities that also provide very high returns to clients. Our rev cycle services, for instance, have high returns to them, and they don't have carried software margins, but they carry pretty good return to us as well. So we're very, very anxious to continue to grow that.

Operator

Our next question is from George Hill with RBC Capital Markets. Okay. We'll move on to the next, which is Steven Halper with Cantor Fitzgerald.

Steven Paul Halper - Cantor Fitzgerald & Co., Research Division - Analyst

Yes, just a couple of questions on the potential monetization of the Netsmart stake. Would there be tax implications on that? And then ultimately, what are the plans for the proceeds on that?



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Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. So, Steve, I mean, we're progressing through conversations, and so in that regard, that's why I brought it up but obviously, we've got to get to the end game first. But assuming we got to a deal that was a cash transaction, yes, it would trigger some tax implications. But between bases, we have some tax shield that we have unutilized. We think it's a fairly efficient transaction from a tax perspective. So we're -- more to come on amounts when we get to an end game. But it's a fairly efficient transaction for us. And proceeds would be -- I think we're interesting -- interested in bringing down our debt levels a little bit and probably share repurchase as well.

Steven Paul Halper - *Cantor Fitzgerald & Co., Research Division - Analyst*

And presumably, all that debt attributed to Netsmart on your balance sheet, that would go away?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Yes.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

It all goes away. Our balance sheet would look massively different than it does today.

Operator

Our next question is from Ross Muken with Evercore ISI.

Unidentified Analyst

Question. Just wanted to get a little bit more color on the bookings in the quarter, particularly on the software delivery side. So it looks like off the back of a strong first quarter, you're tracking pretty much in line for the first half versus last year. Is there any color regarding the level of buying activity that you could provide? And then what you're expecting for the second half relative to the back half last year?

Paul M. Black - *Allscripts Healthcare Solutions, Inc. - CEO & Director*

This is Paul. There's a number of decent sized or large transactions that are out there that we continue to go after, that we continue to work with over the course of the next, I'll say, four quarters. And those things are the things that take at times longer to process or get through. So there's a fair number of sizable transactions that we would expect to close over the course of the next, I'll just call it, four quarters versus the rest of the year. But I'm pleased with that pipeline of opportunity that sits out there. There's also a fair number of cross-sell opportunities, both EIS solutions into the Allscripts space as well as Allscripts solutions into the EIS space. So as an example, there's a lot of large multihospital organizations that don't have our CareInMotion solutions that are interested in that, and again there are some specific departmental solutions that we have with the EIS acquisition that our traditional Allscripts Sunrise clients would be interested in. The strength of the performance continues with the Payer and Life Sciences component, and the strength that we're seeing in the marketplace also has been very robust. And lastly, I'll just say parenthetically that the Sunrise new business opportunities that we're working on as well as some Sunrise movements, if you will, from an existing client to additional Sunrise footprints probably is the largest, if you will, suite of opportunities that we've been staring at for quite a while. Those aren't closed, but I just want -- I look at what the pipeline looks like, that creates a fair amount of encouragement for us to continue to do what we did today, which is reaffirm guidance.



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Operator

Our next question is from Richard Close with Canaccord Genuity.

Richard Collamer Close - *Canaccord Genuity Limited, Research Division - MD & Senior Analyst*

You hit on the life sciences and the activity there. I think you said 10% and you said enterprise. So is that 10% of overall revenue? And then I just wonder if you could just drill down into some of those products, elaborate a little exactly what you've got going there, what seems to be going. And then how big of a business can that area be for you guys going forward?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Richard, the -- so 10% of -- yes, enterprise meant companywide. So that's the answer to that question. What are we bringing? I mean, we fundamentally offer the following value propositions to these clients. For life science companies or CROs, we are using the longitudinal clinical data set that we've captured over a period of time. And that data set is quite helpful to them in doing some of their follow-on testing that they have to do or follow-on trials that they have to do. There's a whole number of uses for some of that clinical data information. We also can help them more efficiently recruit patients for trials that they're running. So think of it as that's the primary for the pharma CRO set. And then on the payer side, what you do -- the payers have a lot of inefficiencies today in trying to connect to the clinical point of care. And we can help eliminate a lot of those inefficiencies, which obviously saves them a lot of money. So that shows up in several different products that we actually -- our product ties to, but that's the core value proposition that we bring to them.

Richard Collamer Close - *Canaccord Genuity Limited, Research Division - MD & Senior Analyst*

So as a follow-up to that, is that area experiencing any of the delays that the provider side, hospital and ambulatory side is experienced -- experiencing now?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

I think the financial situation of those end market customers is different than providers and allows them to make decisions in shorter time periods.

Operator

Our next question is from Anne Samuel with JPMorgan.

Anne Elizabeth Samuel - *JP Morgan Chase & Co, Research Division - Analyst*

Great. I was hoping maybe you could speak a little bit to the competitive environment. Some of your competitors have spoken to heightened competition. Just wondering are you seeing anything new or different in the marketplace?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

I wouldn't say anything new or different. I mean, we, I think, have been talking before anybody in the industry about how the market here in the U.S., certainly for electronic health records and revenue cycle systems is what I think we'd all consider to be mature market, and mature markets create higher levels of competitive intensity. That's not necessarily the case for some of the above-the-EHR opportunities and certainly, not the case in international markets right now. So for those of us who have access to those markets, I think it lessens some of that. But yes, if you're in the business of just electronic health records and PM systems, that's a pretty competitive market right now.



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Anne Elizabeth Samuel - *JP Morgan Chase & Co, Research Division - Analyst*

Okay, great. And then you spoke about a lack of regulatory events out of Washington. What do you think is necessary to catalyze industry growth?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Well, the Washington environment may continue to dictate new requirements at some point. It's just saying right now, we're in a little bit of a lull. So I don't think you should walk away thinking that nothing else will come out of the regulatory world. But, will it catalyzed growth? I mean, look, at the end of the day, I think our -- what we believe we have to offer to the provider base is a way for them to help reduce their costs. Either our software tools help them become more efficient or our services tend to be lower cost and they can do it for themselves. And so as providers continue to struggle with more and more financial pressures, we actually think our value proposition gets stronger and stronger. But that said, it takes them longer and longer to kind of think through their alternatives and make decisions sometimes.

Operator

Our next question is from Eric Percher with Nephron Research.

Unidentified Analyst

This is (inaudible) on for Eric. As we look forward to Q3, I think we're looking -- I think you're lapping some strong software revenues from last year. So two questions like one, how should we view the organic growth going into Q3? And two, from a total growth perspective, do you continue to see that the attrition in the EIS business has bottomed out?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Yes, this is Dennis. I'll take that. So again, we don't provide specific guidance on a quarterly basis. But what I can do is help provide some clarity in Q2. So we've already provided you some information to help you get to an organic growth number, right? We've given you the Netsmart revenue, and we've given you the EIS revenues for the quarter. The only major other piece that you would need to back into an organic growth number is the Practice Fusion revenue number, which the acquired Practice Fusion revenue is in the mid-teens in the second quarter of the year. So if you adjust for those components, our organic growth in the quarter would be approximately 4% versus the same period a year ago, the impact of acquisitions. So again, that's how I look at Q2. When we look at the second half of the year, I think you could do the same math for the full year relative to the guidance we provided. We think that as we said last quarter, and I think it's consistent again this quarter that the EIS revenue, the number that I spoke, the \$72 million in the quarter I think will be representative of what we would expect to get in second half of the year.

Operator

Our next question is from Stephanie Demko with Citi.

Stephanie July Demko - *Citigroup Inc, Research Division - VP & Senior Analyst*

So first one I noticed is when we ask you about the uses of cash for Netsmart, M&A was noticeably missing. Does this kind of mark a bit of a shift in your use of cash strategy? Or is that just not an interest in buying a large-size acquisition?

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Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

No. I mean, look, I mean, M&A has never been our strategy. Our strategy is to when we find targets that we think help achieve -- we can get synergies from either by giving us greater scale or leverage our distribution footprint, that's what we've usually jumped on. And so that's driven some of the activity you've seen over the last six months, but it's not indicative of a M&A as a core part of our strategy. That said, we'll continue -- nothing will change with regard to us looking to continue to build a vibrant franchise for the long term. So if we see something like, we'll buy it. This clearly a transaction like this, if we get it done and completed, we'll reload the balance sheet and we'll have plenty of power to do what we want to do.

Stephanie July Demko - *Citigroup Inc, Research Division - VP & Senior Analyst*

All right. Good to hear. Good to hear on that. And then just to follow up on the organic growth question you had before. The 4% organic growth is a pretty meaningful pickup from kind of your recent rate. Is that -- is it safe to assume that, that is a healthy level of forward top line organic growth? Or are there any one timers in the quarter to call out?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

We're pleased with the 4%. We think that's a good number in Q2 in terms of going forward. We're going to -- obviously as Paul mentioned, there's opportunities to grow that number. At this point, we're not providing any additional guidance above what we provided in terms of our annual guidance.

Operator

(Operator Instructions) Our next question is Ricky Goldwasser with Morgan Stanley.

Mark Lewis Rosenblum - *Morgan Stanley, Research Division - Research Associate*

This is Mark on for Ricky. I just had a question on just the general market environment. You've seen a bit of slowdown in demand. Should we think about this as a new normal? Or is there going to be a point where it kind of the bookings softness laps over the next year or two?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Well, let's just be clear what we said. What we've said is it's an ROI driven demand, not regulatory. And as a result, it's a little less predictable on sales cycles and timing. So that's what we're saying. And we've never been into giving guidance on bookings and so we won't start that now, but I think what you should take away is we feel good about our pipeline. We feel good about our solutions that we're offering, but it's a changing demand environment, which is a little less predictable than it used to be.

Mark Lewis Rosenblum - *Morgan Stanley, Research Division - Research Associate*

Got you, okay. That's helpful, and is there any specific pockets? Is it more on the ambulatory side, more on the hospital side? Just any color.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

I'd say the hospital side is probably the least predictable at this point because sales cycles tend to be longer there.



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Operator

Our next question is from Charles Rhyee with Cowen and Company.

Charles Rhyee - *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

Yes. Just wanted to follow up on Netsmart here, and I understand you're saying you want to monetize value for shareholders here. It seems like if I recall correctly several quarters, the post-acute space has been a great. Obviously, a lot of care is moving outside the four walls of hospitals, and the alternate sites of care seems to be where a lot of volume is going to. Can you talk about sort of the thought process maybe of not acquiring the rest of Netsmart? Is there something about that, that was not attractive to you? Maybe you can just explain a little bit more about some of the thinking behind it.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Charles, we entered into the ownership structure we have today with all of the beliefs that you stated at the beginning, that it was a good space, it was going to grow faster, et cetera. And 2+ years later, we're happy to sit back and watch how we've created tremendous value off of that intuition. So we feel good about it. From the beginning, we set up an ownership structure that was not sustainable for the long term. It meant we were either going to be a seller or a buyer, ultimately, of the rest of that. And so what our shareholders are clearly telling us today is they don't put a lot of value on our ownership in that today based on where our stock is. And you're probably pretty familiar with what's happening in some of the post-acute assets right now, which are trading at very high numbers. And so we think it's in the best interest of our shareholders to let somebody who values this more, own it, and we'll reward our shareholders with the benefits of that. It's really been more of a financial asset than a strategic asset for us, and I think it's the right thing for us to do.

Charles Rhyee - *Cowen and Company, LLC, Research Division - MD and Senior Research Analyst*

That's helpful. So then when we think about -- and just to follow up on someone else question, the earlier question about the M&A strategy going forward, is -- does it still make sense to move further into adjacencies where care is going? How should we think about your strategy going forward now that you'll sort of clear up the balance sheet here and have more capital deployed going forward?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Look, it continues to make sense to leverage the strategic assets we have for value. And so our assets are our solutions, our footprint, our distribution network, and we think our brand as well, and we'll continue to leverage them in different ways for more value. And I'm sure there will be some more acquisition behavior in the future, but that's not what's triggering what we're telling you today about Netsmart. And that's again not a strategy in and of itself. It's something that we'll use to augment the broader strategy. So we'll keep talking to you how we're going to position the company as we go forward, but it's incumbent on all of us in the industry to find opportunities that go beyond just being an EHR provider. We want to be a full suite healthcare IT company.

Operator

Our next question is from Sandy Draper with SunTrust.

Alexander Yearley Draper - *SunTrust Robinson Humphrey, Inc., Research Division - MD*

Just wanted to follow up maybe on, Paul, some of your comments. I wasn't quite clear, and I was jumping on a little bit late about the -- some of the activity around Sunrise being at a higher level. I just wanted to sort of flesh that out a little bit and understand what sort of -- what's driving



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that? Is that really what opportunity within existing Sunrise customers to expand? Or was that potential new footprints? I missed some of that, and it sounded interesting.

Paul M. Black - *Allscripts Healthcare Solutions, Inc. - CEO & Director*

Yes. Thanks, Sandy. It's a little bit of both in that we have going through the forecast meetings that we've been through, and tracking some new clients. So these would be well, new logos, new acquisitions of folks that are interested in us while we are in contract negotiations or some advanced state of work with them. And there's a large number of them, one of the highest that we've been looking at for a while. It's not 3x what we've been doing in the past, but it feels comfortable. Again when you think about what that means to the forecast what it means to the full year component that, that piece of the business drives to our overall guidance, that makes me feel comfortable. There's also a fair number, actually even a larger number of EIS clients that are looking at Sunrise, which is a nice additional benefit of that base, we're probably not necessarily planning on. You expect it just from an executive management standpoint, but that was not baked into any of the projections that we had when we bought the business some of those clients we're going to be moving from where they are today to Sunrise, and we're seeing a pretty nice uptick from those folks. And just so you know when we do that, it's typically the playbook, which is Sunrise, it's hosting, it's managed services. In some cases, it's a fair amount of outsourcing. So those deals, if you will, are decent in size. And those are all long-term engagements.

Operator

Our next question is from George Hill with RBC Capital Markets.

George Robert Hill - *RBC Capital Markets, LLC, Research Division - Analyst*

I guess, Paul and Rick, can you talk about the opportunity that's been created by some of the instability at some of your competitors? You had kind of one competitor in the sale process, a couple having a guy having re-platforming, a guy having a regulatory issue. I guess, are they -- do you feel like those are providing attractive sales opportunities? Or are those clients proving stickier than you expected?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

A little bit of both, George. I mean, yes, it's providing opportunities. I don't know if you got to hear all of our prepared remarks, but I talked about us knocking out a PM client at one of the companies you're referring to. And that's indicative of what we think is some good, new turf to go after because you're right. There is different degrees of chaos going on at several of our competitors. So I think it does create an opportunity. But I mean, it's not just like a day at the spa to switch out your IT solutions. So it takes a little bit of work, too.

George Robert Hill - *RBC Capital Markets, LLC, Research Division - Analyst*

Okay. And then maybe I don't know if it came up earlier on the call, I was also bouncing around the like churn within Allscripts, I guess, can you talk a little bit about client stability and what you guys are seeing there?

Paul M. Black - *Allscripts Healthcare Solutions, Inc. - CEO & Director*

Yes, adding to what Rick just said, the appetite for people to go make a switch is typically driven by the fact that you're not performing well for them or in some cases, they got acquired by somebody else. So our overall, if you will, hygiene on that topic, George, is pretty good. We're pleased with that. The multiyear investment we've made in electronic medical records, whether it's Pro, TouchWorks or Sunrise, has created a bit of a moat around some reasons why historically, people would leave. We still continue to spend a lot of money on R&D to show them a future road map and the reasons why they should stay with Allscripts. So we're giving them lots and lots of reasons to continue to believe in us. We think, quite frankly, this cleanup of the balance sheet on the Netsmart thing will actually, interestingly, create a little bit of momentum with regard to that spend on



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new business side, somewhat at times a concern or a question mark just because of the overall debt when, unfortunately, people roll everything up and not give us credit from the nonrecourse nature of what that actually represented. So all in, combined with your prior question of what's going on with the other guys, you don't get in a mature market a lot of times this much instability. So it's up to our guys to take full advantage of that and make sure that we're out having the appropriate conversations with people that would drive new logos.

Operator

Our next question is from Richard Close with Canaccord Genuity.

Richard Collamer Close - *Canaccord Genuity Limited, Research Division - MD & Senior Analyst*

Just back on the life sciences, having it be 10%, what has that grown from, I guess, maybe in '17? And what do you think the total addressable market can be in that life sciences area and payers?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

So Richard, I'm not going to say what it's doing year-over-year, but let's just say in our tenure as running the company, it's probably fourfold what it was when it got here. So it's gone up nicely. Certainly, the addition of Practice Fusion has accelerated some of that. So if I did give you year-over-year numbers, they would be significant growth. But overall, it's grown very nicely organically and with that acquisition. The answer to the second part of your question is, the answer is these markets are huge. Payers and life science companies and CROs spend a ton of money trying to do trials and follow-up trial work and trying to connect to the point of care and communicate effectively with their providers that are in their networks in the case of payers. So these are very large markets.

Operator

Ladies and gentlemen, we have reached the end of our question-and-answer session. I would like to turn the call back over to Stephen for closing remarks.

Stephen Shulstein - *Allscripts Healthcare Solutions, Inc. - VP, Investor Relations*

Thank you. As a reminder, we've made a number of forward-looking statements during this call. These statements include, but aren't limited to, our outlook related to non-GAAP revenue, adjusted EBITDA and non-GAAP EPS as well as statements related to growth outside of our core businesses and in our international footprint, the timing of integration of businesses recently acquired by us and the anticipated sale of our ownership in the Netsmart joint venture, including our ability to enter into and complete the transaction and the expected timing and use of proceeds related to the transaction. Thanks, everyone, for joining, and have a great evening.

Operator

This concludes today's conference. You may disconnect your lines at this time, and thank you for your participation.



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