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CORPORATE PARTICIPANTS

Brian G. Lloyd *Merit Medical Systems, Inc. - Chief Legal Officer & Corporate Secretary*
Fred P. Lampropoulos *Merit Medical Systems, Inc. - Chairman, CEO & President*
Raul Parra *Merit Medical Systems, Inc. - CFO & Treasurer*

CONFERENCE CALL PARTICIPANTS

Doug Free
James Philip Sidoti *Sidoti & Company, LLC - Research Analyst*
Jayson Tyler Bedford *Raymond James & Associates, Inc., Research Division - Senior Medical Supplies and Devices Analyst*
Michael John Petusky *Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst*
Michael Stephen Matson *Needham & Company, LLC, Research Division - Senior Analyst*
Steven Michael Lichtman *Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst*

PRESENTATION

Operator

Good afternoon, ladies and gentlemen, and welcome to the Fourth Quarter 2020 Earnings Conference Call for Merit Medical Systems, Inc. (Operator Instructions) Please note that this conference call is being recorded, and that the recording will be available on the company's website for replay shortly. I would now like to turn the call over to Mr. Fred Lampropoulos, Merit Medical Systems Founder, Chairman and Chief Executive Officer. Please go ahead, sir.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Thank you, Liz, and welcome, everyone, to Merit Medical's Fourth Quarter 2020 Earnings Conference Call. I'm joined on the call today by Raul Parra, our Chief Financial Officer and Treasurer; and Brian Lloyd, our Chief Legal Officer and Corporate Secretary. Brian, would you mind taking us through the safe harbor provisions, please?

Brian G. Lloyd ***Merit Medical Systems, Inc. - Chief Legal Officer & Corporate Secretary***

Thank you, Fred. Before we get started, I would like to remind everyone that this presentation contains forward-looking statements that receive safe harbor protection under federal securities laws. Although we believe these forward-looking statements are based upon reasonable assumptions, they are subject to unknown risks and uncertainties. The realization of any of these risks or uncertainties, including the unpredictable effect of the ongoing COVID-19 pandemic as well as extraordinary events or transactions impacting our company could cause actual results to differ materially from those currently anticipated.

In addition, any forward-looking statements represent our views only as of today, February 24, 2021, and should not be relied upon as representing our views as of any other date. We specifically disclaim any obligation to update such statements, except as required by applicable law. Please refer to the section entitled disclosure regarding forward-looking statements in today's presentation for important information regarding such statements. Please also refer to our most recent filings with the SEC for a discussion of factors that could cause actual results to differ from these forward-looking statements. Our financial statements are prepared in accordance with accounting principles which are generally accepted in the United States. However, we believe certain non-GAAP financial measures provide investors with useful information regarding the underlying business trends and performance of our ongoing operations and can be useful for period-over-period comparisons of such operations. This presentation also contains certain non-GAAP financial measures.

Reconciliation of non-GAAP financial measures to the most directly comparable U.S. GAAP measures is included in today's press release and presentation furnished to the SEC under Form 8-K. Please refer to the sections of our presentation entitled non-GAAP financial measures and notes to non-GAAP financial measures, for important information regarding non-GAAP financial measures discussed on this call. Readers consider non-GAAP financial measures in addition to, not as a substitute for financial reporting measures prepared in accordance with GAAP. Please note that these calculations may not be comparable with similarly titled measures of other companies. Both today's press release and our presentation are available on the investors page of our website.

I will now turn the call back to Fred.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Thank you, Brian. And let me start with a brief agenda of what we will cover during our prepared remarks today. I will start with an overview of our revenue performance in the fourth quarter, including the business trends we experienced during the quarter and the areas of our business that performed well despite the challenging operating environment. I will then provide an update on our operating progress and highlights during the fourth quarter. After my opening remarks, Raul will provide you with a more in-depth review of our quarterly financial results in the formal financial guidance for 2021 that we introduced in this afternoon's press release as well as a summary of our balance sheet and financial conditions. Then we will open the call to your questions.

Now beginning with a review of the fourth quarter revenue performance. We reported total GAAP revenues of $250 million in quarter 4, essentially flat compared to the prior year period and above the high end of our guidance range, which called for fourth quarter revenue to decline 2% to 5% year-over-year in quarter 4. Total quarter revenue on a constant currency basis declined 1% year-over-year, reflecting the benefit to our GAAP revenue results as a result of changes in exchange rates compared to the prior year period. Our total GAAP revenue growth performance was driven by a 0.3% growth in sales of our cardiovascular products, which was partially offset by a 7% decrease in sales of our endoscopy products compared to the prior year. Both of these results exceeded the high end of our guidance ranges which called for the sales decline of 1 to 16 -- 1% and 16% year-over-year, respectively, in quarter 4.

Our revenue results increased 6% on a quarter-over-quarter basis, which reflects the overall improvement in business trends that we've experienced in recent months. Importantly, this sequential growth was above expectations and exceeded the high end of our guidance range, which called for sequential growth of flat to up 4% which we discussed in, of course, our third quarter conference call. I want to take a minute now and dig into the underlying trends we experienced during the fourth quarter as I think it may be helpful for investors that are gauging the pace of recovery in Merit Medical's business. First, we continue to see notable variation in the pace of recovery across regions of the world where we do business, and we continue to see variation within certain geographic regions. By way of reminder, roughly 60% of our total revenues come from business in the U.S., and sales in the U.S. decreased 1% year-over-year in the fourth quarter.

Understandably, the recovery from the pandemic has been more rapid in our U.S. direct business, where sales were up 1.7% year-over-year in quarter 4, fueled in part by improving elective procedure trends and overall demand for our peripheral intervention products like our SCOUT Access guide in November and December. While strong demand for our peripheral intervention products helped drive our total U.S. revenue to the higher end of guidance range in quarter 4, we continue to see the overall operating environment challenge our revenue results in other areas of our U.S. businesses.

Similar to what we experienced in the third quarter, the recovery in our cardiac intervention business has continued to lag. And while we reported a 14% increase in U.S. sales of CPS products in quarter 4, excluding sales of our Cultura swabs, our U.S. CPS business declined in the low single digits year-over-year in quarter 4. While our OEM sales trends reflect strong improvements in growth trends on a quarter-over-quarter basis, our OEM business continues to be slower to recover as a result of inventory management as our customers adjust to product demand in response to COVID-19. In quarter 4, sales to U.S. OEM customers decreased 5% year-over-year.

Now turning to a brief review of our sales results outside the U.S. Total international sales in the fourth quarter increased 1.2% on a reported basis and decreased 2.5% on a constant currency basis. Our 2 largest regions outside the U.S. are APAC and EMEA, representing approximately 49% and 44% of our total international sales, respectively, in the fourth quarter. The 2.5% OUS constant currency decline in the fourth quarter was driven by a 1.2% decrease year-over-year in APAC sales, a 5.5% decrease year-over-year in EMEA sales and a 7.6% increase year-over-year in the sales to the rest of the world region. All international regions continue to see material impacts from COVID-19 and are still in the early stages of recovery. Restrictions and lockdowns are changing constantly across regions, causing limitations to sales contact and lower demand for elective procedures. We were pleased with our performance in the APAC region this quarter as we saw strong demand from China and strong sales of critical care products to customers in Japan, and Australia, New Zealand. These stronger sales trends partially offset year-over-year sales decline in all other APAC regions due to COVID related hospital restrictions of elective procedures and sales rep access.

We saw a significant rise in COVID-19 cases across Europe and emerging markets in the fourth quarter. However, sales in emerging markets were notably more challenged. Despite the pronounced uptick in cases in quarter 4, sales in Europe held up well relative to quarter 2 and 3, as governments adopted less stringent lockdown measures relative to the first wave of infections. Demand for critical care products remained strong throughout Europe in the fourth quarter. Weak demand in emerging markets is primarily due to challenging conditions in Saudi Arabia, Russia, Iraq, Iran and Egypt as governments have diverted health care budgets to fight COVID-19 and the overall weaker demand for elective procedures led to tenders being postponed or canceled.

Now turning to a brief review of our recent operating progress during the fourth quarter. During 2020, we moved production of 23 product lines to our facilities in Mexico or Texas, and we closed manufacturing operations in Temecula, California, Melbourne, Pennsylvania and in West Jordan, Utah. We have closed our PAC business in operations in Australia and successfully transferred the related lease obligation. Our R&D efforts are ongoing, and we expect to continue our track record of new product introductions going forward.

On November 6, 2020, we acquired all of the outstanding membership interest of KA Medical LLC, a company founded by Dr. Kurt Amplatz, for a total consideration of approximately $15 million, comprised of $10.4 million in cash at closing and a $4 million payment deferred until 2021. As a result, we have added KA Medical's Micro Plug Set to our embolic product portfolio. The Micro Plug Set is a self-expanding night nonvascular occlusion device, used for arterial embolization, which is FDA-cleared and CE-marked. We have successfully initiated our first clinical trial site for the WAVE IDE and 4 other sites are confirmed for late February, early March. This is for our WRAPSODY product line. We continue to target enrollment of the first patients by the end of this -- the first quarter of '21, and we are awaiting CMS approval at this time.

With that, let me go ahead and turn the time over to Raul, who will take you through a detailed review of our fourth quarter financial results and our 2021 financial guidance, which we introduced in this afternoon's press release. Raul?

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Thank you, Fred. Given Fred's detailed review of our revenue results, I will begin with a review of our financial performance across the rest of the P&L. For the avoidance of doubt, unless otherwise noted, my commentary will focus on the company's non-GAAP results during the fourth quarter of 2020. We have included full reconciliations from our GAAP reported results to the related non-GAAP item in our press release this afternoon. Gross profit decreased approximately 1% year-over-year in the fourth quarter. Our gross margin was 47.9% compared to 48.3% in the prior year period. The approximate 40 basis point decline in gross margin year-over-year was driven primarily by changes in product mix, partially offset by improvements in manufacturing efficiencies.

Fourth quarter operating expenses decreased 9% year-over-year. Total operating profit increased $7.7 million or 23% year-over-year to $40.5 million. Our operating margin was 15.7% compared to 12.7% in the prior year period. The year-over-year improvement in operating margin was driven by a 10% decrease in SG&A expenses and, to a lesser extent, a 7% decrease in R&D expenses compared to the prior year period. The reduction in SG&A expenses were a result of cost-cutting initiatives and other cost management efforts related to COVID-19 pandemic including layoffs, targeted furloughs and temporary salary reductions and lower discretionary spending as a result of reduced travel, training and shows and conventions among other items.

The reduction in R&D expenses was largely due to lower compensation expenses, lower discretionary expenses as a result of cost-cutting initiatives and the COVID-19 pandemic and a more focused research and development program. Our fourth quarter GAAP operating expenses included 2 noncash expense items that I wanted to call out as well. The first is approximately $8.2 million of noncash intangible asset impairment expense, this is due to changes in revenue expectations associated with an acquired product line. The second noncash item impacting our GAAP operating expenses in the fourth quarter, was a contingent consideration benefit of $8.8 million from changes in the estimated fair value of our contingent consideration obligations stemming from our previously disclosed business acquisitions.

Fourth quarter net income was $30.8 million or $0.54 per share compared to $22.1 million or $0.40 per share in the prior year period. We are very pleased with our profitability performance in the fourth quarter, where we reported growth in net income and diluted earnings per share of 39% and 37% year-over-year, respectively, in a quarter where our sales were essentially flat compared to the prior year period.

Turning to a review of our balance sheet and financial condition as of December 31, 2020. Our strong profitability performance in the fourth quarter, combined with strong working capital efficiency, resulted in strong operating cash flow generation in the fourth quarter of $36.9 million, an increase of 37% year-over-year. Our efforts to control our capital expenditures resulted in a year-over-year decrease in CapEx of roughly 48%, which fueled very strong free cash flow generation of more than $26 million in the fourth quarter. Our year-to-date free cash flow generation is a result of great execution from the team and, importantly, early evidence that we are clearly focused on enhancing the profitability and cash flow profile of our company going forward. As of December 31, 2020, our cash on hand of approximately $56.9 million, long-term debt obligations of approximately $352 million and $389 million of available borrowing capacity, compared to cash on hand of approximately $44.3 million long-term debt obligations of approximately $440 million and available borrowing capacity of $134 million as of December 31, 2019. Our net leverage ratio as of December 31 was 1.72x on an adjusted basis.

Turning to a review of our fiscal year 2021 guidance, which we introduced in this afternoon's earnings release. For the 12 months ended December 31, 2021, the company expects GAAP net revenue in the range of $990 million and $1.01 billion, representing an increase of approximately 3% to 5% year-over-year as compared to net revenue of $963.9 million for the 12 months ended December 31, 2020. The fiscal year 2020 GAAP revenue guidance range assumes GAAP net revenue from the cardiovascular segment of between $959.3 million and $978.6 million, representing an increase of approximately 3% to 5% year-over-year as compared to net revenue of $934.2 million for the 12 months ended December 31, 2020. GAAP net revenue from the endoscopy segment of between $30.8 million and $31.9 million, representing an increase of approximately 4% to 7% year-over-year as compared to net revenue of $29.7 million for the 12 months ended December 31, 2020.

We expect our GAAP net revenue for the 12 months ended December 31, 2021, to include a benefit of approximately $4 million from changes in foreign exchange rates, representing a tailwind of approximately 40 basis points to our GAAP growth rate this year. GAAP net income in the range of $47.3 to $55.9 million for $0.83 to $0.98 per share compared to GAAP net loss of $9.8 million or $0.18 per share for the 12 months ended December 31, 2020.

Non-GAAP net income in the range of $104.8 to $112.7 million or $1.84 to $1.98 per share compared to non-GAAP net income of $93.3 million or $1.65 per share for the 12 months ended December 31, 2020. For modeling purposes, our fiscal year 2021 financial guidance assumes Q4 non-GAAP gross margins in the range of approximately 48.5% to 49.8% and modest increase in our non-GAAP operating expenses, largely driven by higher selling and marketing expenses related to increase in sales as well as phasing out of temporary salary reductions, partially offset by prudent G&A expense management and approximately $8 million of other expenses, largely driven by lower interest expense as a result of the reduction in debt obligations outstanding as compared to the prior year. A non-GAAP tax rate in the range of approximately 24% to 25% and approximately 56.8 million diluted shares outstanding.

Lastly, given the continued COVID-related headwinds we expect throughout the first quarter of 2021, we expect our total revenue to decline approximately 5% year-over-year on a GAAP basis and declined approximately 6% year-over-year on a constant currency basis in Q1 '21.

With that, I'll turn the call back to Fred.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Okay, Raul, well, that's a lot to digest, and I want to thank you. Before we open the call to questions, I wanted to provide a few considerations and key assumptions for the investment community to bear in mind as they evaluate our 2021 revenue guidance. We have 2 items to call out as contributors to our 2020 revenue results that represent material headwinds to the growth rates our guidance assumes in 2021. We also have a key assumption impacting our 2021 revenue expectations over the second half of 2021. And let me give you some additional color. Regarding the 2 areas that represent headwinds to our 2021 revenue expectations, first, as we discussed in prior calls and disclosed in filings during fiscal year 2020, we announced strategic decisions to exit 3 businesses: the suspension of Merit's distribution agreement with NinePoint Medical in the first quarter of 2020, the closure of the ITL Healthcare procedure pack business in our Australian facility and the disposition of assets related to the manufacturing of Merit's Hypotube product in August 2020. Together, these businesses contributed revenue of approximately 11.1% -- excuse me, $11.1 million during the fiscal year 2020 and will not contribute to our revenue results in 2021.

Second, our 2020 revenue results benefited from the sales of Cultura nasopharyngeal swab and test kits used to collect and transport samples for COVID-19 testing which we developed, manufactured and distributed beginning in the second quarter of 2020 in response to the critical need as a result of the COVID-19 pandemic. The Cultura swab initiative was a direct response by our organization to help the state of Utah and our neighbors and to prepare for a swab shortage in April of last year, as we quickly directed resources to the development of this kit and our engineers, technicians and marketers and production staff worked tirelessly, weekends, holidays, to bring this important product to market in 30 days. We believe this represents a great example of not only Merit's strong R&D and manufacturing capabilities, but our ability to adapt quickly to the changes in our markets and to respond to time-sensitive demand from our customers. Importantly, Cultura is not a core product line for merit going forward and we expect to gain approximately $1 million to $2 million in sales from this product line in 2021 compared to more than $19 million in 2020. This represents a material headwind to our year-over-year revenue profile for 2021.

The third item I wanted to highlight for investors to consider when evaluating our 2021 revenue growth profile is the key assumption that impacts our APAC revenue over the second half of 2021. Our revenue guidance includes approximately $11 million to $12 million of headwind related to lower pricing as a result of tenders over the second half of 2021. Overall, we expect our total revenue in China to increase in the low single digits year-over-year in 2021, despite the expected pricing headwind as a result of strong unit growth during the year. While we are pleased to see the strong demand driving unit growth such that we were able to offset the expected pricing headwind related to tenders this year, we note that the $11 million to $12 million of lower pricing represents approximately 120 basis points headwind to our total company constant currency growth.

Now I'd just add a little color here. This is, of course, China, and these are the various issues that have to do with more local sourcing and a number of the other initiatives by the Chinese government. We've built them into our forecast -- whether they come or not, we don't know, but we thought it was really important for us to put this and to talk about this because there's a lot of discussion about these kinds of issues. Not only have we heard this, but from other companies. Now excluding the revenue contributions in 2020 from exited businesses and the sales of Cultura as well as the expected pricing headwinds from China tenders over the second half, our total revenue guidance for fiscal year 2021 reflects growth in the range of 6.5% to 8.5% year-over-year on a constant currency basis. Now while we expect to see measured improvements in our operating environment as we move through 2021, fueled by the wider availability of vaccines and an increasing percentage of vaccinated Americans, our guidance assumes no material improvement in the operating environment, access to patient elective procedures over the first half of 2021. As Raul outlined earlier, while we expect first quarter revenue to decline 5% year-over-year on a GAAP basis and 6% on a constant currency basis, the low end of our guidance still assumes constant currency revenue growth, excluding the impacts of the 3 items we discussed above, a 5.5% year-over-year over the first half of 2021. Our guidance assumes progressive improvements in these headwinds and a return to normalized year-over-year growth trends in the third quarter of 2021.

We also expect to report improving non-GAAP gross and operating margins and strong free cash flow for 2021, driven by a strong execution and contributions from our multi-year strategic initiatives related to the foundations for growth program.

That's a lot of information, but that kind of wraps it up. And at this time, we'd like to turn the time over to Liz, and we'd now like to open it up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question will come from Mike Matson with Needham & Company.

Michael Stephen Matson ***Needham & Company, LLC, Research Division - Senior Analyst***

So I guess I'll start with the tenders you're assuming in China, is this based on tenders that you're aware are actually going to be happening? Are you just kind of putting some cushion in there in case they do happen? And then do you expect this to be kind of an ongoing thing that recurs every year over time and maybe rotate through different product categories? Or is this more of a one-and-done type of thing?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. Thanks, Mike. Well, listen, what we've seen from other players, particularly in PTCA balloons and other types of things are these types of decreases that I think people like Medtronic and other companies have announced. So looking at this and understanding that they've basically focused on cardiovascular products, we thought it prudent to be able to go through and make sure that we're not making excuses. We don't want to have to be explaining this on the back end of the year when we felt like this is a possibility. So again, governments and changes in administration can change lots of things. We thought it wise, based on what we're hearing, what we see, but it's not something that we have a tender that's pending or a directive that we've received. But with so much chatter and the local sourcing going on and what they call the single invoice program, we thought we'd be wise to do this. And so we budgeted this way for the year, and that's the basis for talking about this today.

Michael Stephen Matson ***Needham & Company, LLC, Research Division - Senior Analyst***

Okay. And then your guidance also include -- your revenue guidance also includes some of the divestitures, the 3 that you mentioned or, I guess, business exits that you mentioned in 2020. But what about in 2021? Are you planning to do any more of that sort of activity? I know that you're -- the long-range plan that you laid out kind of contemplated some of that. So will we see more of that in '21? And will that potentially lead to guidance revisions if it does happen? Or would it have more of an effect in '22?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. Mike, we're not talking about that in advance. But it's really part of our 3-year plan and our foundations for growth. So as you know, that's a 3-year plan. We're 2 months into that. We will be moving a number of products to Mexico as part of our foundations for growth this year. And that will be an ongoing, but we're not going into all of that at this point. If it was imminent or something like that, we had something on the table, we'd certainly lay it out there. But this is really just part of our 3-year plan. There will be more things to come, but nothing to announce or discuss today.

Operator

Our next question comes from Matt O'Brien with Piper Sandler.

Unidentified Analyst

This is [Gerome] on for Matt. I just wanted to start out a little bit on COVID. Appreciate the commentary on both the Q4 trends domestically and outside the U.S. We've heard fairly mixed things across medtech as far as Q1. So maybe you could kind of give us a flavor of whether things have gotten a little bit better, a little bit worse since last quarter.

And then you mentioned not assuming any material improvements to the operating environment. I assume you mean from a patient throughput perspective, is that correct? And then just how material of a drag are you assuming in your guidance for that? .

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. Well, listen, we saw business soften somewhat in December and ahead of expectations through the first 2 months of the quarter, they're still locked down. They announced further lockdown in Ireland and this and that and the other. So I think in part of the COVID issue, we still see these locations, particularly in some of the emerging countries. So I think in looking at this, we do have confidence in the second half of the year. We're seeing -- I mean, some of this is, of course, anecdotal, but like, for instance, we're seeing lower cases, and I think this is part of the national discussion, lower amounts of COVID cases, more people getting vaccinated. But outside the U.S., there's still a lot of this lockdown there, and some people are talking about initiating even more. So I think that's kind of the way that we looked at it COVID. But -- so it's bumpy. It's -- there's pockets, but it's still not back to the point where it's totally under control, as we all know, and it's going to be a while.

And incidentally, if we could, [Steve,] I think this has kind of been the way we've been thinking about for a long time. We talked about this last year that we saw -- in the second half of '21.

And one other thing that we also saw is the issues in the February weather. So we got hit reasons, not hard, but we suffered somewhat down in Texas. Our plant was shut down. We had employees. We had to keep people away from work. We all watched this on the news last week, well we have a facility there, and that affects our ability to deliver. So that was another part of this, that we wanted to make sure that we contemplated as we considered the numbers that we wanted to use. Raul, do you want to add anything to that?

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

No. I mean I think you kind of see our reaction to it, right? I mean, for Q1, we've essentially said 5% down year-over-year. A lot -- a big portion of that is, obviously, the COVID related impact. And as Fred mentioned, the weather. So we're, I think, yes, we're expecting it.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. Does that answer your question, [Steve?]

Unidentified Analyst

Yes, absolutely. And then on your foundations for growth call a couple of months ago, you were a little bit hesitant to provide a lot of detail on the margin cadence. But now, I guess, with guidance out there, maybe you could help us understand in a little bit more detail. I think the gross margin improvement was the big focus in the near term. So maybe you could just kind of give us an idea of what you're baking into your 2021 guidance on the gross margin side?

And then on the SKU rationalization, that's obviously a big component of it, have you started that process? And I guess, how far along are you and how much more do you have baked in for 2021?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. I'll answer the question in terms of we started it. The answer is yes, we have. We have met -- first of all, it was a lot of work done in the initial assessment part of that program. It's being driven internally by various teams and silo leaders. They've met with me. We've agreed on how we were going to proceed. It's aggressive but necessary and something we've been needing to do. I will be meeting with them in a couple of weeks to get an update. So it is in full momentum in terms of SKU rationalization in a number of our business segments. So I'll answer that part, and then I'll turn the rest of it over to Raul to answer the other.

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Yes. So on the gross margin, I think maybe to give you some color on how we get to the gross margin guidance for the year. There's really kind of 2 components of revenue mix. And the initial contributions from the FfG initiatives, including the ITL and Malvern activities. So on the revenue mix, obviously, we're expecting, as the elective procedures come back, higher margins. And we've seen that essentially quarter-over-quarter since the bottom.

In addition, geographic revenue mix, the U.S. is growing faster than OUS in 2021. So that contributes. So I guess, if you kind of break down those 2 items -- at the lower end of the range, roughly 140, 150 basis points, roughly half of it is related to mix. And then the other half is related to FfG or foundations for growth. Obviously, the upper end would be driven by higher sales mix benefits.

Operator

Our next question comes from Steven Lichtman with Oppenheimer.

Steven Michael Lichtman ***Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst***

So obviously, as you think about the pipeline, and I appreciate, Fred, the update on WAVE that remains a big long-term target. Wondering in the near term, what are some of the product lines that you're looking to in terms of sort of above corporate average growth here over the next 12 to 18 months?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. Thank you. Listen, 1 of the things that we've continued to do during this process is to keep our R&D going. And we have, I think -- and I hate to say this, but we have about 10 products right now that have to do with inflation devices, electrophysiology products, vascular access and others that are part of things, but it's hard to get to the back committees. It's hard to get into the hospitals. There's still a lot of restrictions. The good news is the products are -- have regulatory approvals, the products, either CE or the FDA, they have first [locks to stock.] The other side is we don't want to build inventories until we know that these products can get out there. So we've not started that, and we expect that, I think I'm just trying to think about the number but let me just say that it would be in cadence, what we've done in previous years of additional new products that are being developed. So we haven't stopped. We think once these things start to lift, it's going to be a very, very exciting time for the business, which is why we're optimistic, as we said in the second half of the year, because we believe at least our present belief is as things open up, that Merit is going to be in a -- just a terrific position with these new products.

The WRAPSODY itself in Europe is selling and selling well. And then, of course, as I mentioned in our comments, that we hope that in the next few weeks, we will start the trial. We have at least 4 hospitals that are ready to go, another 4 in the queue and many, many more after that for our WAVE study. And we'll be ready to go relatively soon.

So we'll give you more detail on that as we treat our first patient. Raul, do you want to comment?

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

No, no. Just -- I think our next announcement will be when we start enrolling. We'll let out a press release...

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

As soon as that first patient hits the deck and -- which is very soon -- then we'll go ahead and we'll -- and that's kind of a monumental thing because as you all know, we think a lot of this product and its future at Merit. So it's a big opportunity.

Steven Michael Lichtman ***Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst***

Great. And then just quickly, Raul, on free cash flow, obviously, again, solid in 2020. What kind of range do you think we could see in 2021 if you're able to provide it or anything relative to inputs, if not, that you can provide in terms of CapEx or anything like that?

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Yes. I mean, look, I think for Capex, I think we were -- we kind of announced maybe a 3-year plan, right? So about $50 million per year, $35 million maintenance, $15 million for FfG related items. I think for free cash flow, we're going to go for approximately $90 million in 2021. We think that's a good number. I know if you kind of compare it 2020, obviously, we had a big impact from working capital just because we did take inventory down as sales slowed, we didn't want to overbuild. So just as a heads up.

Operator

Our next question comes from Jim Sidoti with Sidoti & Company.

James Philip Sidoti ***Sidoti & Company, LLC - Research Analyst***

I hope you're all well. Just a couple more details on the quarter. I think you said for the year, the sales of the swab were around $19 million. And I'm looking back in my notes, I think you did about $4 million in the second quarter, about $9 million in the third. So am I safe to assume that fourth quarter for that was about $5 million to $6 million?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

You are.

James Philip Sidoti ***Sidoti & Company, LLC - Research Analyst***

All right. And then you talked about it a little bit, and you mentioned it in the press release, there was an acquisition you did in the fourth quarter related to the embolic product line. Can you just give me a little more detail as to what that was? And do you think that's something that will pull-through sales of embolic as well as the device you acquired?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. Thanks for asking, Jim. Listen, as you know, Merit is one of the leaders in Embospheres, QuadraSphere. These are really very, very small spheres that are used to embolize for UFEs and PAEs and so on and so forth. There are, however, larger areas and larger vessels that have to be blocked off. You could have, for instance, in a trauma case, splenic artery bleed. I mean this is a critical issue, and you've got to get in there and you've got to block off that vessel. And you need a larger device. What people are doing today, as they oftentimes will take coils, and they will have to take one at a time, and you could see 10 coils in a patient. Well, that takes time, and each one has to be individually moved.

We bought this company that was founded by Kurt Amplatz. Dr. Amplatz -- well, first of all, the Amplatz name in medicine is the Amplatz Goose Neck Snare, the Amplatz Wire, the Amplatz catheter. And mean he was a tremendous innovator and physician, passed away about 15 to 16 months ago. And he had this small company in which he had licensed out of AGA. Some of you will recall, Jim, that AGA was a company that had PFO devices and others that were sold to St. Jude for over $1 billion. But they licensed back some of these smaller devices and that's what we bought. So it's a license, which now is from Abbott because they acquired St. Jude, for these devices that would be used for instance, if you're doing Y90, that is an isotope. If those things get into the stomach, the cure is worse than the disease.

So these are -- and you can go to the website, KA Medical, and look at them, and these are these micro -- these very, very small plugs that you would then deploy into these larger vessels and they go from 3 to 6 millimeters. And it takes one, and it usually will block that vessel off in 1 or 2 minutes. So again, these are things that are used by an interventional radiologist, the same person that uses PVA, our EmboCube, our Torpedos and our Embosphere. And it's a tool that allows them to really get a larger part of this whole embolic market. So we're quite excited about the opportunity here. And it will be something you'll be hearing more about as we go down the road in terms of how it fits in that hole. And yes, it will pull-through other opportunities, microcatheters, guidewires and other embolics. Because sometimes, they'll use this as a primary and then they'll chase it with, let's say, with PVA or with gelfoam. So you got me pretty excited about, as you can see, I know a lot about the product, and I worked hard on this acquisition. But we've kept it really kind of quiet until we get the product on the market, but it is a great technology.

James Philip Sidoti ***Sidoti & Company, LLC - Research Analyst***

And is it fair to assume that the gross margin on this product is above the corporate average?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

I think it would be safe to assume that it's well above the corporate average.

James Philip Sidoti ***Sidoti & Company, LLC - Research Analyst***

And that seems to be the trend. If you look at the guidance for 2021, you're forecasting about 15% EPS growth on about 3% to 5% top line growth with most of that coming from gross margin. Is that the way we should think about Merit going forward? Is it a company in that mid-single-digit top line rate, but much better bottom line rate because of gross margin improvement?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. I think, Jim, you hit the nail on the head. I'm going to let -- Raul, I want to make sure I'll let you go ahead and fire that one.

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Well, I think just -- I mean, we set out a 3-year target, right? Foundations for growth contemplate the 5% to 7% CAGR. So just wanted to get that out there, Jim, obviously, 18% to 21% operating margins, I think we gave details there on how we get there. But yes, I mean, I think it's 5% to 7% is a slightly slower growth rate than we've historically had. And again, we're very focused on making sure we're profitable.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

But I think the midpoint of 15% earnings increase is right on target.

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

That's right.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes.

James Philip Sidoti ***Sidoti & Company, LLC - Research Analyst***

All right. And just to be clear, for this year, you had about $30 million of discontinued products or products that have been phased out and then you have the issue in China. So without that, your top line rate would have been closer to 6% or 7%?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

That's correct.

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

That's correct.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Thank you, Jim.

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Yes, 6.5% to 8.5%.

Operator

Next question comes from Jayson Bedford with Raymond James.

Jayson Tyler Bedford ***Raymond James & Associates, Inc., Research Division - Senior Medical Supplies and Devices Analyst***

I guess just to follow-up on a few of the growth comments. First, and I apologize if I missed this role. What's the assumption for FX in '21 on the top line?

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

It's about $4 million -- 40 to 50 basis points.

Jayson Tyler Bedford ***Raymond James & Associates, Inc., Research Division - Senior Medical Supplies and Devices Analyst***

Okay. And then in terms of just getting back to the China dynamic, or let's say, the headwinds that you've disclosed, the strategic divestitures, the COVID-related revenue that's not going to recur. And then is the China dynamic factored into guidance?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. And let me give you a little more color on that one, Jayson. These situations really had to do with PTCA, as I mentioned. And of course, one of the things we're concerned about is we're a big inflation device player. Now nothing's come down, nothing's been pronounced. But if you're going to see it on this side, you may see it on the other side that capability on inflation devices, of which we're a very big player over there. So we wanted to make sure that we just didn't put our head in the sand and that we were wise about this. So we weren't trying to explain why we didn't do it later on. So we just said in our guidance, we're going to take that particular aspect. Whether it comes or not, if it comes, we'll be prepared. If it doesn't, then it will just be to our advantage, and it will be more of the icing on the cake, so to speak.

Jayson Tyler Bedford ***Raymond James & Associates, Inc., Research Division - Senior Medical Supplies and Devices Analyst***

Okay. And the impact that I thought I heard was 120 basis points.

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Yes. Yes, roughly $11 million to $12 million, Jayson.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

And we're just trying to be transparent, so you can glean these things. Yes, that's all. I mean we're...

Jayson Tyler Bedford ***Raymond James & Associates, Inc., Research Division - Senior Medical Supplies and Devices Analyst***

Appreciated. I guess just the timing on when we'll know? It sounds like the tender hasn't been set. So I'm just kind of curious as to when will we know?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

So our China management and leadership have indicated that if we see it, it could come in the second half of the year, and that's how we've kind of planned it going forward.

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Yes.

And then also, Jayson, just on our slide deck, there's a reconciliation to the items we talked about that are impacting the revenue growth. So just as a heads up.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

And again, as you already know, these are not things that have happened, but these are things that we're just trying to get ready for in case they do.

Operator

Our next question comes from Larry Biegelsen with Wells Fargo.

Unidentified Analyst

It's [Wei] calling in for Larry. I want to start by asking you, I think you mentioned in response to an earlier question that the first couple of months of the year has been ahead of expectations. Can you give a little more color on that in terms of relative -- is that relative to December relative -- relative to your expectation for Q1? And if there's any color on which business segments have been outperforming.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes, I'm going to go ahead and let Raul answer that one.

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

We're not -- I mean, I think if you look at our guidance for the first 4 months, I mean, it implies 5% decline year-over-year, 6% on a constant currency. So we are seeing softness in our business and have accounted for it. In addition to the item that we mentioned on the weather impact in February.

Unidentified Analyst

Okay. And then my second question is just looking at the revenue cadence for the year. So you talked about COVID headwind in the first half, normalized growth in second half, but there's the potential for the China tender impact in the second half. In that context, can we see sequential revenue growth through the year?

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Yes. I mean, I think if you look at our growth, it essentially implies that, right? I think if you look at our growth for the first half of the year, it implies essentially some growth in Q2. So I think we're -- we do expect that growth to kind of get back to normal as we head out of Q1 and into Q2 and then Q3 and Q4 kind of normalize. And that's based on today's environment, right? So we'll have to see how that plays out.

Unidentified Analyst

And that's, again, assuming the China tender impact is in second half, you would still see that normalized growth?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

That's correct.

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Yes. I think -- yes, I mean, we'll -- yes.

Operator

(Operator Instructions) Our next question comes from Mike Petusky with Barrington Research.

Michael John Petusky ***Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst***

I may have missed this earlier, but Raul, did you give a D&A expense for the quarter and stock comp for the quarter by any chance?

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Yes, I can. Just give me a minute here, my computer went to sleep on me for a bit. But I have it here for you for a second here. So let's see. So on D&A, we've got -- let's see.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Mike, while he looks at that. If you have a second -- another question?

Michael John Petusky ***Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst***

Sure. Yes, I do. So I was just curious, and again, I may have missed this because I think it was touched on twice. The Texas facility, how many days was that down for? And is there an estimate of like a quantification of the impact?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. I think we're back up and running now. We did have some disruption, of course, of employees who had damage in their homes, and that sort of thing. So I'm going to say it was approximately 5 to 7 days of production.

Michael John Petusky ***Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst***

Okay. I mean, does that actually then show up in the quarter? Or is that just something you catch up on and you move forward?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Well, no, I mean, if you're not producing product, you'll catch up with it down the road. But in the quarter, you -- I mean, we'll catch up on it down the road, but it's going to show in the quarter.

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Yes. I mean, we're trying to make it up. I mean, it is an impact in Q1. Yes. Mike, it was obviously right in front of me, which is why I couldn't find it. So 23.5 on the D&A and then $4.1 million in stock comp.

Michael John Petusky ***Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst***

And I'm sorry, what was CapEx also?

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

CapEx was $10.4 million.

Michael John Petusky ***Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst***

$10.4 million. And did I hear free cash was $26 million in the quarter, correct?

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Yes, $26.5 million, roughly.

Michael John Petusky ***Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst***

And then, Fred, I think you guys mentioned strong demand in China, sort of offsetting the otherwise negative APAC region. Can you quantify that? I mean, was it up 10%? Or can you just talk about what you saw in China specifically?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. I don't have the number in front of me.

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

But -- give me a second, here we go. China was up 7% year-over-year on a constant currency basis.

Michael John Petusky ***Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst***

In the fourth quarter or for the year?

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

For the fourth quarter. Is that right Fred?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. Yes, 7% in the fourth quarter.

Michael John Petusky ***Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst***

Okay. And then since I'm at the end here, I'm going to ask one more question. Fred, in terms of M&A, as you think out the next 12 months, next even 3 years, what's your appetite? Obviously, you guys are generating a lot of free cash now and it feels like there's more flexibility to do things, but obviously, you want to be prudent. Can you just sort of generally talk about what you're seeing out there and sort of your appetite, et cetera?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. Well, first of all, you're right. We've, I think, really improved our balance sheet. We've taken this free cash flow and paid down our debt. And you also have seen the commitments that we've made over the next 3 years as part of our foundations for growth. We really like the little situations. And so that was part of the -- KA Medical seemed to be right in our wheelhouse for a product that's in our existing silos.

Things are pretty expensive out there. We've had a couple of things that have been shown to us. And some of them that have gone to other companies, but they're very expensive, and they haven't been attractive to us. I will say that although we were resting for about a year, that we do have our eyes open. There are some, but I think the key is that they have to be able to be bought properly, they have to be able to fit into our global footprint. And they have to be something that we feel will give us an advantage, but we're certainly not going to go chasing anything. And like I mentioned, with WRAPSODY coming down the road with what we see as improving business trends. Remember last year, Mike, we were the guys that weren't talking about a hockey stick. We were talking about this gradual improvement. And in our performance, you've seen that. And again, and we've said that we will see it a little bit the first and second quarter, but for the year, and really, I think, substantially improving in the second half of the year, even with these headwinds. So we have -- we're fine with the growth and the things we're doing but we will be opportunistic for the right deal at the right price, but we don't feel like we have to do anything. If the right thing is around, and we think it fits our long-term strategies then we certainly have going to spend some time and more now than we would have a year ago.

Michael John Petusky ***Barrington Research Associates, Inc., Research Division - MD & Senior Investment Analyst***

Congratulations on managing through a very challenging year. You guys have really performed well.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Thank you, Mike. Appreciate it.

Raul Parra ***Merit Medical Systems, Inc. - CFO & Treasurer***

Thanks, Mike.

Operator

Our next question comes from Doug Free with World Capital Group.

Doug Free

So regarding China, you mentioned the single invoice program and more local sourcing as kind of a headwind to consider, along with government initiatives, et cetera. To what extent have you explored increased partnerships or joint ventures with local market participants to be viewed more as a local solution through a Chinese partner?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. It's a good question, Doug. Listen, I mean, listen, we could spend a lot of time talking about China. The way that we've chosen to approach in the past is to make sure that the products that we registered were products that had really good IP, and they were really innovative. You think of our SwiftNinja steerable microcatheter, that's approved. And now we've launched that, and we've also done the Amplatz, speaking of the Amplatz name again, our Amplatz guidewires and some other guidewires over there that are not easy to do and not generally available in the marketplace. So that's what we've done, which is -- these have been looking backwards.

I've always been concerned about partnerships. And I've always been concerned about our IP, and I could go on and on about this stuff, but I'm going to hold back a bit. We've been resistant or reluctant, I think, to look at these other issues because of the fear of losing our intellectual property and our know-how. I think, though, as in all conditions and in all fairness to your question, I think we have to reexamine that and then take a look if there's ways that we can partner with Chinese companies and be part of a solution to meet the needs of that economy. So we'll probably look at that more [than] the past. But again, the things that I've discussed about my concerns in the areas to protect the company for the long-term are also things that have to be considered. So we'll probably spend more time at that now. Someone might say, well, why didn't you do it in the past? And I think I've answered the question. And listen, we've grown very nicely over there for years, and our model has worked just fine. Now you have these pricing issues. And Merit is probably as good as anybody at adapting to the marketplace and pivoting, but not pivoting wildly. In other words, we're not just going to say, okay, now everything is going to be produced in China, but we will spend time evaluating this. Joe Wright, who oversees that area for us and Leon Lam, who is our resident General Manager for the area, and I have spent some time together and we'll be looking and spending more time trying to evaluating this and looking for opportunities going forward.

Doug Free

As a quick follow-up. And I agree with you. That's a high consideration is protecting the IP. So regarding China, the current revenue contribution by Asia PAC is about 36% of the U.S. revenues. What is your target or guidance on market penetration into the China market in the next 12 to 24 months?

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Yes. Doug, we don't respond. I mean, we just don't comment on that. Other than China has always been important to us, but so has all of APAC. So I'm just unfortunately not going to be able to answer that in any detail.

Operator

I'm showing no further questions in queue at this time. I'd like to turn the call back for closing remarks.

Fred P. Lampropoulos ***Merit Medical Systems, Inc. - Chairman, CEO & President***

Liz, thank you very much. Well, listen, thank you very much. I know there's a lot of stuff out there, a lot of meetings going on and you've had to jump in and jump out. Raul and I are here. We have scheduled calls. We will do the best to give you color that's appropriate to give on the -- from each of you. We'll be here for the next, I think, 3 hours. So thank you very much. We're looking forward another year of improvement. And we're always, as you always know and have known forever, we're always engaged and excited about this business. Thank you for your support, and we look forward to talking to you soon. Thank you very much, and good night.

Operator

That does conclude our conference call for today. Thank you for your participation.