Company: IntriCon

Conference Title: IntriCon Third Quarter 2017 Results

Conference ID: 5232505

Moderator: Scott Longval

Date: November 6, 2017

Operator: Good day everyone and welcome to the IntriCon Third Quarter 2017 Results conference call. Today's conference is being recorded. And at this time, I'd like to turn the conference over to Scott Longval, Chief Financial Officer. Please go ahead, sir.

Scott Longval: Thank you, operator. Joining me on today's call is Mark Gorder, IntriCon's CEO. Before we begin, I'd like to preface our remarks with the customary Safe Harbor statement. Today's conference call contains certain forward-looking statements. These statements are based on current estimates and assumptions of IntriCon's management, and are subject to uncertainty and changes in circumstances.

Given these uncertainties, you should not place undue reliance on these forward-looking statements. Actual results may vary materially from the expectations contained in today's call. Important factors that could cause such differences include among others, those set forth in the headings Risk Factors and Management's Discussion and Analysis of Financial Condition and Results of Operations in our 10-K filing for the year-ended December 31, 2016.

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

Mark Gorder: Thank you Scott, and thank you everyone for joining us today. I would like to begin by reviewing key highlights and results for the third quarter. After that Scott will cover the financials in more detail and then we'll take your questions.

By this time most of you had a chance to review our third quarter press release. The company reported another record quarter of net sales of $24 million, up 54.4% from $15.6 million in the prior-year period. Gains in medical and value hearing help drove the strong performance.

In addition, we are successfully cultivating a new direct to consumer channel to deliver superior outcomes based affordable hearing healthcare, meeting several key milestones during the third quarter.

Looking at our two primary businesses, our medical business increased 68.4% in the 2017 third quarter from the prior year period. The gain was primarily driven by the continued production ramp of Medtronic's MiniMed 640G and 670G wireless glucose monitoring systems. We remain very well positioned with Medtronic long-term, providing both continuous glucose monitor or CGM and sensor assembly.

As part of their earnings release on August 22, 2017, Medtronic announced strong global demand for their diabetes technology. Including the MiniMed 640G in international markets and the world’s first hybrid closed loop system MiniMed 670G in the United States.

These systems have increased their installed base and market share, driving a large increase in CGM demand. As a result, overall sensor unit demand a key component of CGMs has more than doubled, temporarily outstripping Medtronic’s production capacity. Medtronic expects to have increased sensor production capacity by the end of their fourth quarter, which we anticipate will drive significantly higher sensor assembly sales us in fiscal 2018.

Furthermore in October of 2017, Animas Corporation, one of the Johnson & Johnson Diabetes Care Companies, announced that it intends to discontinue the manufacture in sale of insulin pumps. And they selected Medtronic as its partner of choice to facilitate a seamless transition for patients, caregivers and healthcare providers.

Patients using an Animas insulin pump will be offered the option to transfer to a Medtronic pump. Approximately 90,000 patients currently use Animas pumps and products. We expect this partnership to be another driver for Medtronic growth throughout 2018.

Turning to hearing health. Sales in this business grew 53.8% from the prior-year third quarter, primarily stemming from our growing traction in value hearing health, including 94.1% growth from insurance base sales, the addition of new private label direct to consumer partners and a $1.8 million contribution from HHE, partially offset by declining conventional channel sales.

As previously announced, we acquired a 20% stake in DeKalb, Illinois-based HHE, a direct-to-consumer mail order hearing aid provider in the fourth quarter of 2016. In January 2017, we exercised our option to acquire the remaining 90% stake in HHE that is expected to close during the fourth quarter.

Since taking our initial stage in HHE, we have made substantial progress integrating and optimizing the organization. During the first part of the year, we relocated the business, hired a Vice President of direct-to-consumer sales and introduced IntriCon's digital hearing aids into the HHE portfolio.

Those activities are paying off driving key third quarter metrics over the sequential quarter, including a 49% increase into leads, a more than two-fold increase in net new hearing aid customers, 20% increase in backlog and a 38% growth in hearing aid orders.

We continued to be pleased with our HHE traction. Hearing aid orders rose 38% over the 2017 second quarter and 82% of the devices we're selling through HHE are IntriCon devices, a significant milestone given that we launched IntriCon's first device through HHE during the 2017 second quarter.

We expect continued sequential growth in the fourth quarter, and throughout 2018. Based on these metrics, we intend to increase our investment and advertising in the fourth quarter and into early 2018 to further accelerate growth.

In addition to HHE, in April 2017 we entered into an agreement to acquire a 49% stake in Soundperience, headquartered in Frankfurt, Germany. Just recently, we made our final payment on the $1.3 million investment.

We do not anticipate the Soundperience business will have a notable financial impact on operating results, but rather it will provide us with exclusive access in the United States to critical software technology.

Soundperience has designed the first psycho-acoustic way of analyzing peripheral hearing and central hearing processing, branded as the Sentibo Smart Brain System. The software is a sophisticated, self-fitting hearing aid and brain training software technology that is being used in the German market today, most notably through our previously disclosed Signison joint venture with Soundperience.

In addition to its international application, we began piloting a US cloud-based version of the Sentibo Smart Brain System during the third quarter. Incorporating self-fitting technology is a critical step in creating our high-quality, low-cost hearing healthcare ecosystem.

While it is too early to drop absolute conclusions from our US pilot, we believe Soundperience's technology harvest the potential to drastically reduce the price of hearing aids, drive greater access and increase customer satisfaction.

Looking at some of the international hearing healthcare initiatives, we continue to focus sales into the National Health Service clinics in the UK, while our efforts to make inroads to the NHS approve and to take longer than expected. During the quarter, we made we made advancements of several clinics and recently began taking initial orders.

Shifting to public policy, there have been significant developments during 2017. Legislation was signed in a law by President Donald Trump, which includes the Over-the-Counter Hearing Aid Act of 2017. The legislation is designed to enable adults with mild-to moderate-hearing loss to access OTC hearing aids without being seen by a hearing care professional.

Echoing what we have said before, this is an important step forward in hearing health. The OTC Hearing Aid Act is designed to provide greater public access to OTC hearing aids at a lower cost. We believe that this new law can remove the significant barriers today that prevent innovative hearing health solutions and provide affordable and accessible solutions to millions of unserved or underserved Americans.

By signing the OTC Hearing Aid Act into law, we've entered a new era in hearing healthcare. IntriCon is at the forefront and spearheading an effort to create innovative solutions that provide greater device access at a much lower cost. Now I'd like to turn the call over to Scott for a review of our financials.

Scott Longval: Thank you, Mark. I'll begin by reviewing our third quarter financial results in more detail. For the 2017 third quarter, the company reported net sales of $24 million, up 54.4% from $15.6 million in the prior year period. The increase was primarily due to year-over-year revenue gains from our largest medical customer as well as continued traction in our value hearing health.

IntriCon posted net income attributable to shareholders of $1.1 million or 15 cents per diluted share versus a net loss attributed to shareholders of $1.3 million or 19 cents per diluted share for the 2016 third quarter. Third quarter gross profit margins were 31.5%, up significantly from 22.7% in the prior year's third quarter.

The increase primarily stem for greater volume in the inclusion of HHE direct-to-consumer business in 2017 as well as more IntriCon devices being sold into the HHE channel. We expect this trend to continue in the fourth quarter.

Operating expenses for the third quarter were $6.1 million compared to $4.3 million in the prior year third quarter. The increase was largely due to the inclusion of HHE in 2017, and key initiatives to drive business growth.

Turning to other financial metrics. Despite significant investments in value hearing healthcare, we reduced our total debt to $7.8 million down from $9.3 million at the end of the second quarter and $9.7 million at the end of 2016.

As Mark previously mentioned, in January 2017 we exercise our option to acquire the remaining 80% stake in HHE. That is expected to close during the fourth quarter. As previously discussed on our second quarter earnings call, this part of the closing, we will likely absorb a portion of the losses allocated to the majority owner.

That amount we may have to absorb could range between $500,000 and $700,000, losses incurred by HHE to date include non-cash amortization, acquisition related cost in operating results, all of which related to prior year periods and have no future cash impact.

In terms of guidance, based on the information that's currently available, we anticipate the 2017 fourth quarter net sales to range between $22 million and $23 million compared to $17.7 million in the prior year period and positive pro forma EPS excluding the loss of 7 to 10 cents to absorb a portion of the losses previously allocated to the HHE majority owner.

For the year, we are raising our net sales guidance to range between $88.1 million and $89.1 million, compared to 86 – excuse me, compared to $68 million in 2016. Looking forward to 2018, we anticipate continued strong growth with annual revenues ranging from a $100 million to $104 million. Now I'd like to turn the call back over to the operator so we can take any questions.

Operator: Certainly. If you would like to signal for a question at this time, please do so by pressing star 1 on your telephone keypad. If you are using a speakerphone, please make sure that your mute function has been turned off to allow your signal to reach our equipment. Again, that's star 1 to any questions. We'll pause for just a moment.

And our first question will come from Andrew D'Silva, B. Riley FBR Inc. Please go ahead.

Andrew D'Silva: Hey, good afternoon. Thanks for taking my questions. First of all, glad to see you're making progress on several fronts here. So, just so I can better understand some of the dynamics that are going on internally, you noted Medtronic orders were very strong. Should we think of any sort of kind of a larger stocking order taking place during the period or is this really the new run rate we should be expecting as we close out '17 and '18?

Scott Longval: Yes, if we look through the transition we talk about Medtronic business and we really try to defer to what they've said publicly. Clearly we've seen a ramp up over the second half of the year and if you look at all commentary that they have made surrounding these products that's been very well accepted in the market place.

So, I don't want to get too far ahead of ourselves and start commenting on specific customer orders coming in, but we did made comments in the release that we anticipate a very strong 2018 coming down the pipe, and obviously they would be a contributor to that.

Andrew D'Silva: Okay, fantastic. And just moving over to the hearing side of the business, I'm glad to see that the hearing bill passed. Maybe you can give us a little bit of a sense of what needs to take place next from a regulation standpoint and perhaps what a realistic timeline is.

I know the FDA usually has about pretty large grace period here, but is there anything you're hearing or perhaps any discussions you've been involved in that help us may pinpoint at time that's more realistic than few years out?

Mark Gorder: Andrew, this is Mark. Yes, I just was out in Washington D.C. last week and meeting with all the interested parties, the FTC, the Senator Warren's office and nobody is willing to really speak to how quickly they're going to go about this actually getting the regulation done. They have three years to do.

I did get a sense that they thought that the FDA would move sooner rather than later and that the specification, draft specification could be out as soon as six months after the passage, which would put us maybe I think it passed in July.

Scott Longval: August.

Mark Gorder: August. So, we're probably looking at February, March of next year for a draft specification. And then they have to go through comment periods and people get the way in, obviously the traditional industry the oligopoly will – they have been trying to prevent this and fight it, they'll try to slow it down.

But we understand that Senator Warren has spoken to the head of the FDA and encouraged them to move quickly so that consumers will benefit from these very positive changes. So I would guess my – if you ask me, I think it will be approximately a year from the passage and they will have written the regulation.

Andrew D'Silva: Okay, great. And actually that gives me a good segue into my next question. From a strategic point, I'm just kind of interested how you see yourself setup in the macro dynamic now after a year from now or whenever this – the regulations are passed.

Obviously as you mentioned the very large players in the market, can they capitalize on this in a similar fashion that you're trying to? Are there any benefits to them or is it you guys being smaller and nimble going to help you gain market share in total over them as they're not going to be able to have the sales and market dynamic setup to be able to transfer this kind of process?

Mark Gorder: Well that's a good question, and I – our strategy has been to position ourselves in this emerging market as creating an ecosystem of care. We don't think that the OTC legislation in and of itself is sufficient to drive growth in the market. We have found that a significant customer care element exists to getting people to accept and wear hearing devices.

And we anticipate that you not only have to have and over the counter presence that a strong customer care presence providing hearing assistance to not only fitting the device but learning how to use it, and in addition follow-up care. So we see this as creating an ecosystem of care managing the patient from start to finish.

And we think that that gives us a competitive advantage over people who are coming in say from the hearable space which should be an unregulated space. And on the other end is the traditional model with the oligopoly which is really the very – the high end goals, they call it the goal standard. We think that our position is in between those two segments.

And we're building using technology to building this ecosystem of care and position ourselves carefully in between a quasi or unregulated segment to a – to the more traditional model going through the bricks and mortar audiologist.

Andrew D'Silva: Got it. One more question, sorry. On the flip side, are there any barriers that you're seeing for perhaps consumer tech companies that will make it more difficult for them to enter the market now that the regulations are expected to be changing sometime fairly soon?

Mark Gorder: Well, the regulation when it's written will still be an FDA – will have the, an FDA requirement for submittal and meeting the FDA manufacturing standards. So consumer electronics people will traditionally don't have that expertise. If they're going to sell these devices, they're going to have to put in FDA certified manufacturing facilities and be medically certified.

And that's not that they couldn't do that, but they have to take that step and in addition, you're going to have buildup audiological expertise to provide the – what we call the ecosystem of care to get people to not only wear the devices initially but to keep them. So we think that those barriers will be in there for the consumer electronics companies. They're stepping into a medical realm.

Andrew D'Silva: Okay.

Mark Gorder: Now, many of them, there are some that are interested in doing that like Amazon. But we still think this customer care is going to be critical.

Andrew D'Silva: That's very interesting. Okay, well thank you very much. Good luck going forward.

Mark Gorder: Thank you.

Operator: And as a reminder, that's star 1 to signal for a question at this time. We'll hear next from Dick Ryan with Dougherty. Please go ahead.

Dick Ryan: Thank you. Congratulations guys on a strong quarter. Say Mark, the commentary on Medtronic, the capacity issues that has nothing to do with you but I'm wondering with the hurricanes and their Puerto Rican operations if anything there kind of impacts the CGM side of their business.

Scott Longval: Dick, this is Scott. We really can't comment on that, they came out publically I believe it was last month and put out a piece we're communicating on, their facilities were impacted by the hurricane but they had them up and running by early October. But we really can't comment on that as well on what that means to us or to them.

Really we're just kind of waiting and seeing and getting the real time information from them.

Mark Gorder: However, Dick, in the guidance that we built into the press release, we anticipate strong growth in 2018 year-over-year in spite of any short-term issues that they may or may not have in Puerto Rico. So we anticipate no major impact on us.

Dick Ryan: Okay. And Mark, you mentioned an 82% of the devices from HHE were IntriCon's, can you – is it too early to give a sense of the success of the digital units coming through?

Mark Gorder: It's probably a little too early. First of all the transition from analog to digital we're having to train everybody down there on how to do that. We've had a few difficulties initially in getting the right settings on the IntriCon devices sold into this new channel but we're learning very quickly and we're adapting and making some of those changes.

I would sense that by certainly during the first quarter of next year we should have enough data to give you a sense of how that is going. But we do anticipate that it should be a positive impact.

Dick Ryan: Okay. And on the NHS side, you said you're making progress on the clinics. I think on the last call you were hoping to get - I can't remember the number - thousands or something by the end of October, November and do that on a monthly basis. Any current thoughts on the NHS ramp opportunity?

Mark Gorder: Well, we're not moving along as quickly as thought but we did have a decent order already from one of the clinics and we're starting to make progress with several others. So, even though this is a slow take up, it's still the largest single purchase or a hearing aid in the global market, so we feel we got to be there and we had to tough it out but we are making progress and we expect to continue to make progress.

Dick Ryan: Okay. Scott, do you have the stock based comp, I don't think I saw the depreciation amortization numbers.

Scott Longval: Stock based comp was $210,000 and depreciation amortization was $555,000.

Dick Ryan: Great. What was Medtronic in the quarter?

Scott Longval: Medtronic revenue in the quarter was $12.2 million.

Dick Ryan: Okay, great. Thank you.

Scott Longval: Thanks.

Mark Gorder: Thanks Dick.

Operator: Thank you. If you find your question has been answered you may remove yourself from the queue at any time by pressing star 2 on your telephone keypad. And, again, that is star 1 if you would like to signal for a question. We'll go next to Larry Haimovitch with HMTC. Please go ahead.

Larry Haimovitch: Good afternoon Scott and Mark.

Mark Gorder: Hey Larry.

Larry Haimovitch: Congratulations, obviously a very good quarter. The gross margin was up significantly beat all of our estimates. Is this the best gross margin quarter you've ever had in terms of percentage?

Mark Gorder: Since I've been here for 12 years, it is.

Larry Haimovitch: Okay. You didn't talk much on the call about what it was that drove the gross margins. Obviously volume helps gross margins. We all know that, that's easy. Could you go a little into, little more detail Scott, give us a little more color on the gross margin story?

Scott Longval: Sure, and we've been talking about this Larry for quite some time even when our gross margins were in the low 20s that we needed volume to fill up these facilities because we had the excess capacity. And largely what you're seeing is just greater volume.

But on top of that, we're also seeing greater margins coming through from our hearing health express business. Those margins are in the 70 plus range. So that business continues to grow and becomes a larger piece of the overall revenue make up we are going to get some expansion on the margin.

So those are really the two big components to driving margin this quarter.

Larry Haimovitch: Scott as Mark – as sale was continue to grow, should we expect gross margins to further expand?

Scott Longval: Yes.

Larry Haimovitch: Where is – where do you think the upper limit is in, meaning reasonable sense, where would you think you could – you can get?

Scott Longval: I would say in our current facility footprint with the business that we have today and the makeup that we have today, eventually we think we can get into the upper 30s.

Larry Haimovitch: Upper 30s.

Scott Longval: For gross margin.

Larry Haimovitch: That would have some really nice leverage on the income statement wouldn't it?

Scott Longval: Correct.

Larry Haimovitch: Last call we talked about raising money, you guys said you didn't think you wanted to do it at this point. I think we would all anticipate tomorrow the stock will move up and may continue to move up in anticipation of strong fourth quarter and the guidance you're provided for 2018.

Do you still feel that an offering is not in your best interest at this point that either you're looking for a better stock price or you just feel like you can run the business very well without needing to raise more money?

Mark Gorder: I would say Larry short-term we still feel that we're in a good position in what we're doing. But we're always looking at all our alternatives to see what the best approach would be. And I think we've said in past calls that we feel at some point that we want to find a branding partner to help us in accelerate growth in our emerging hearing health business.

But in the short-term we're, as you can see, we're in pretty good shape, whatever we'll do would be strategic and it would depend on opportunities that come across about here over the next six to 12 months.

Larry Haimovitch: Thanks. And Mark, I'm not a duck hunter, I've never been to Minnesota to duck hunt, but I understand the duck hunters up there have the very, very thoughtful saying which is, if the ducks are quacking, feed them.

Mark Gorder: Well, that's kind of what we feel about the advertising at HHE. We know that if we spend more money in advertising at HHE, we'll continue to drive revenue.

Larry Haimovitch: Okay, I'll leave you on that side. Thanks again for …

(Crosstalk)

Larry Haimovitch: … a great performance.

Scott Longval: Thank you Larry.

Operator: Thank you. We'll take our next question from George Marema, Pareto Ventures. Please go ahead.

George Marema: Hi, thanks for taking my questions. First question I kind of eco the last caller on the business model going forward on the value hearing aid business. I'm kind of understand what happens over the next one to five years in that to the model and then you talked a branding partner.

I'm not sure I fully understand what that means. What would that look like and how would that – how would that feather into your current facilities and I'm trying to understanding the business model if I look out years ahead what this looks like.

Mark Gorder: Well, I maybe just break that into two parts. The – in the short-term, the next few years, we can gain a lot of traction just continuing to build our HHE model, and driving advertising, there is a huge untapped market which we estimate about 20% of the total hearing health market in the US is underserved or unserved.

And simply by continuing to work on our ecosystem of care with HHE, we anticipate that continue to drive very strong growth there over the next few years. In addition to that, we're anticipating that at some point, it makes sense to accelerate what we're doing, what we've demonstrated that we've got a scale of the model that can be taken to a much higher level.

So for example, you may be familiar with companies like Warby Parker where they've gone direct with the manufacture, with the consumer in eyeglasses. The exact nature of the model of treating elderly hearing patients is going to be different than what Warby Parker is doing, but we anticipated that at some point there will be an opportunity to expand or scale our model to the next level.

At that point it would be helpful to have somebody who had experience in doing that working with us. So, we think that as we mentioned in the prior call that there is a strong customer care element here. There may also be a service element that's required where you have places where people can go to get service in addition to a direct-to-consumer online or direct mail approach.

And we've seen that watching Warby Parker that they started out all direct to consumer but they've segued into adding bricks and mortar service centers in several areas around the country, I don't know how many they've got now in total but some of the people that I'm talking to, think that that kind of a model maybe required if I looked toward a five to six years down the road.

This is not something we're going to do in the next one to three years, but that's kind of my take on it.

George Marema: So, and then in your 2018 guidance, are you – is this mostly driven by HHE growth or half and half with the medical side or what's your growth mostly coming from in for '18?

Mark Gorder: It would be very similar to 2017, there'd be a huge component of Medtronic but also very strong contribution from HHE, our private label partners and our direct to insurance model, all three of those will contribute it on the hearing health side and then Medtronic. So, be strong contributions from all of those.

George Marema: Okay. And then also to eco the cash concerns, on your debt, what are the covenants for the minimum cash balance requirements to stay in good standing?

Mark Gorder: We don't have any covenants for minimum cash, the only covenants that we have relate to a leverage ratio and a fixed charge ratio. And we are well in balance with those covenants.

George Marema: Okay. Yeah, I would like to see more cash on a balance sheet for safety but I understand you're profitable and all but it'd be nice to have more cash investment business in my thoughts. But, well, anyway. Well, thank you. Good quarter and I look forward to the next. Thank you.

Scott Longval: Thank you. Thank you, George.

Operator: Thank you. We'll go to our question from Scott Billeadeau with Walrus Partners. Please go ahead.

Scott Billeadeau: Hi guys, a couple of my questions have been asked, but – and I missed a little bit of the earlier part of the call so you may have went over this. But, I was just wondering if – so, you have full ownership of HHE now so that – did that impact Q3 or will impact Q4 or I should say the next quarter? Can you kind of update me on that Scott?

Scott Longval: Sure. So Scott, we will be closing on hearing health express in this quarter, so the impact of that transaction will happen in the fourth quarter.

Scott Billeadeau: Okay, and then you'll carry the full expense burden then …

Scott Longval: Right.

Scott Billeadeau: …of HHE, okay. And I think you mentioned was that, did you – did I hear you say something about 7 cents for Q4 if that was going to be or was I hearing something different?

Scott Longval: The range would be 7 and 10 cents in the fourth quarter.

Scott Billeadeau: Seven and 10 cents. Okay. Great. And then another question, this, you know, little of a big picture on, you know, as you strategize about how to build your kind of the service model or the ecosystem, will there be – will this kind of be a leveraged, because you're still going to need an audio – even though it's over the counter, you will need an audiologist?

Mark Gorder: Scott, with the new legislation, the OTC Act of 2017, you don't need to use a professional to fit an over the hearing counter aid. So what we would anticipate in the direct to consumer model is you would have two categories of devices that we would be dispensing. One would be the OTC model and the other would be the traditional hearing aids that we are already dispensing.

In the case of OTC, you would not need a professional and what we're excited about there is that, as we anticipate implementing this self-fitting software, a consumer could fit themselves using this technology in the convenience of their home or other remote location once we put that in place, without having a professional involved.

In the case of the traditional hearing aids, we still need the professional but – so the use of that technology in the traditional market would be not yet determined. But, don't necessarily need a professional depending on the type of device that you're dispensing.

Scott Billeadeau: Okay. I just wondered, but they could, like you say from a service perspective or from a good outcomes perspective even having someone or some type of center, whether it's …

Mark Gorder: Yes, yes.

Scott Billeadeau: …Warby Parker that you were talking about or have. I can see someone could build a business model on providing that service …

Mark Gorder: And you were correct Scott …

Scott Billeadeau: …you know …

(Crosstalk)

Scott Billeadeau: … without having to go and get a audiology, without having to be a doctor to do it, right. I mean that's a very different – there's a different model that could be built there.

Mark Gorder: Yeah, and in either case, whether it would be the OTC or the traditional hearing aid coming through our HHE model, in both cases we would be providing strong customer care.

Scott Billeadeau: Yes. Great. All right, I think that that's all I got. Thanks guys.

Scott Longval: Thanks, Scott.

Mark Gorder: Thanks, Scott.

Operator: Thank you. And our next question will come from Beth Lilly, Crocus Hill Partners. Please go ahead.

Beth Lilly: Good afternoon Mark and Scott.

Mark Gorder: Hi Beth.

Scott Longval: Hi Beth.

Beth Lilly: I had a question in terms of the self-fitting technology and you talked about piloting the US cloud-based version. Can you say a little bit more in terms of the pilots and then when do you think it's going to be ready to be commercialized?

Mark Gorder: Well, we have two initiatives going on. The main one is in Germany with Soundperience and Signison. What we're doing there is, because the technology was invented in Germany and the gentlemen that created it is local there, we thought it would be easier to pilot it in Germany because we still considered a technology in progress. And we wanted to make sure we debug that in a manner that was very efficient so we decided to start there.

He is making good progress in using it through Signison in the German market. We were just over at a trade show in Europe called the European Hearing Aid Congress and he has made good progress there but it does take a lot of handholding to get people to figure out how to use it. So he goes and visits the shops and he is actually putting it in through shops.

And because in both Germany and the US, the regulation has not yet been passed in the US, you still need a professional involved to use this fitting technology. So we – what we're doing in the US, is we're piloting it through our Hearing Health Express, we call it HHP which is a professional outlet, it's staffed by audiologists and dispensers in DeKalb, Illinois. And we're using the fitting technology there under the supervision of a licensed audiologist or dispenser.

Once the OTC legislation is passed, we can then use this in a way where we don't need a licensed dispenser or audiologist oversee the process. So right today we're still debugging the technology with the oversight of a licensed professional.

Beth Lilly: Great. And so can you, and I know we spoken about this, but let's just fast forward to nine months from now and let's suppose the legislation is passed and it's – and so you're able to get hearing aids OTC. Can you walk us through then how this technology works for a consumer? Let's suppose I need to get a pair of hearing aids?

Mark Gorder: Well, the kind of patient that we would intend to attack first here would be ones that are elderly but also tech savvy. And the way the initial launch would go is we would send out an iPad with the device and we would – and there'd be training materials and videos along with it and you would sit down in an iPad.

The iPad would wirelessly interface with your hearing aids through a low energy Bluetooth connection. And as you were walking through the questionnaire that you would get on the iPad as well as listening to sounds generated from the iPad, you would manipulate the screen to produce a – in your estimation it gives you the best result.

And when you're done going through this entire process, you actually have a prescription for your hearing loss based on how you answered the questionnaire manipulated the dials. And you simply then need to hit the fit sequence and you self-fit your hearing aids.

So that's the way this would work initially is we would zero in on tech savvy hearing loss patients probably more likely between the ages of 55 and 75, send them an iPad and then assist them to walk through the training process.

But this could only happen once the OTC legislation passes and the devices would be within the category designated by the FTC – FDA as OTC hearing aids.

Beth Lilly: And is the hope then eventually that you don't have to send out a hearing aid – an iPad with the hearing aids, maybe they could tap on an App or something like that?

Mark Gorder: Yes. Well, there'd be an App on here but the problem you've got is standardizing your access into someone's home with a system that's easy to use. And if you allow too many variables, it becomes almost impossible for elderly people to figure that out, we know that it has to be simple. So tech savvy is all relative.

Beth Lilly: Yes.

Mark Gorder: So it's going to be a challenge for us to pilot this and figure out what is the right combination of simplicity and technology to allow it to be effectively used.

Beth Lilly: Yes. Okay. That is very, very helpful. Thank you very much.

Mark Gorder: You're welcome Beth.

Operator: Thank you. That will conclude our question and answer session for today. For closing remarks, I would like to turn the conference over to Mark Gorder, CEO.

Mark Gorder: Well, thank you again for all the great questions and taking the time out of your day to join our call. In closing, I'd like to reiterate that I'm excited with the direction we're headed. We've never been in a better position to drive growth in both our value hearing health and medical business.

Our medical business is thriving with tremendous long-term prospects, and additionally we continue to gain momentum in the value hearing health space, meeting critical milestones, driving sales and positioning the business for success. Thank you again.

Operator: That will conclude today's conference. Thank you all for joining. And you may now disconnect.