Medical Technology
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AEGIS CAPITAL CORP

Initiating Coverage

November 30, 2016

Key Metrics

GMED - NYSE	$21.71
Pricing Date	Nov 29 2016
Price Target	$31.00
52-Week Range	$19.25 - $28.60
Shares Outstanding (mm)	95.8
Market Capitalization (mm)	$2,079.8
3-Mo Average Daily Volume	802,319
Institutional Ownership	97%
Book Value/Share	8.46
Price/Book	2.6x

EPS FY: December

	2015A	Prior 2016E	Curr. 2016E	Prior 2017E	Curr. 2017E
1Q-Mar	0.26	--	0.29A	--	0.29E
2Q-Jun	0.25	--	0.29A	--	0.30E
3Q-Sep	0.28	--	0.27A	--	0.30E
4Q-Dec	0.32	--	0.31E	--	0.33E
FY	1.10	--	1.15E	--	1.22E
P/E	19.74x		18.88x		17.80x

REVENUE

	2015A	Prior 2016E	Curr. 2016E	Prior 2017E	Curr. 2017E
1Q-Mar	131.6	--	139.3A	--	147.6E
2Q-Jun	133.6	--	137.5A	--	152.6E
3Q-Sep	137.0	--	135.7A	--	156.0E
4Q-Dec	142.6	--	148.3E	--	169.0E
FY	544.8	--	560.7E	--	625.3E

Company Description:
Globus Medical is a global medical device company focused on the design, development, and commercialization of products that promote healing in patients with spine disorders and injuries. The company addresses a broad range of spinal disorders, and is preparing to enter the trauma and robotics market.

Globus Medical

Rating: Buy

Initiating with a Buy and $31 PT: Looking to 2017

Investment Highlights:

We are initiating on GMED with a Buy and $31 PT. Sales force recruitment issues have thrown the company off course in 2016, but we are anticipating a recovery in 2017. We may be early with this call, as we are not expecting a recovery to be apparent until mid-2017, but we think at current valuations low expectations are priced in, and the company continues to show good margin control despite increased investment. Longer-term, the company remains well positioned with the most competitive and diverse product offering, and still has a large footprint of business to go after. 2017 will also see market entry into trauma and robotics, and while we are only projecting a modest $10 million in revenues for 2017 from these opportunities, they represent significant breakout opportunities and upside to our outer years.

Core Business: 2016 growth is expected to be in line with the market, but we anticipate a recovery in 2017 to above market growth. We expect a gradual return to the high single-digit to low double-digit growth of the past in 2017 (2H loaded), though at a lower starting point than previously expected. Globus still offers the most competitive and diverse product offering, and we expect management to put significant focus on its sales force efforts.

Pipeline: Emerging technologies, including its robotics platform and trauma, should begin contributing in 2017 and by 2020 managements expects it to make up less than 15% of sales, which may then include other adjacent market expansion opportunities. We are projecting $10 million in contributions for 2017, with robot approval expected by the end of 2Q and trauma build out beginning in 2H17.

Valuation: We are applying a 12-13x EV/EBITDA multiple to our 2017 estimate and adding back cash to get a $31 target price. We believe GMED can return to generating high single-digit revenue growth and see GMED as considerably less expensive than NUVA. We see the 12-13x range appropriate for small-cap med-tech companies.

Exhibit 1: Peer Group Valuation Metrics

Company	Ticker	Market Cap	EV (MM)	EV/SALES TTM	EV/SALES 2016	EV/SALES 2017	EV/EBITDA TTM	EV/EBITDA 2016	EV/EBITDA 2017
Globus Medical	**GMED**	**$2,071**	**$1,813**	**3.3x**	**3.2x**	**2.9x**	**8.8x**	**8.8x**	**8.5x**
Integra LifeSciences	IART	$3,095	$3,674	3.8x	3.7x	3.4x	21.9x	15.8x	14.1x
NuVasive	NUVA	$3,226	$3,709	4.1x	3.9x	3.5x	19.6x	15.4x	13.1x
Wright Medical Group	WMGI	$2,411	$2,868	4.2x	4.2x	3.8x	-	62.2x	36.9x
K2M Group	KTWO	$807	$834	3.6x	3.6x	3.1x	-	695.0x	54.9x
Average		$2,322	$2,580	3.8x	3.7x	3.3x	16.8x	159.4x	25.5x

Source: Aegis Capital Corp estimates and FactSet **Priced as of 11/29/2016*

Risk: Risks to the achievement of our target price include (1) increased competition from larger players with more resources or smaller players with more focused portfolios, (2) slower than expected market uptake on key products, (3) sales force hiring and training slower than expected and (4) spine market instability.

The Disclosure section may be found on pages 6 - 7 of this report.

Core Business: FY2016 growth is now expected to be in line with the market. We are anticipating a recovery in 2017—preliminary company guidance assumes 5.5% organic growth. This is above market indicating a return to share gains, but at a pace still below the consistent low double digit growth of the past -- our assumption is that sales improvements will be more evident in 2H17 and the company can end the year approaching past rates. Our checks indicate that the competition has in fact improved its game, driving some sales force recruitment competition, but that GMED remains a top choice. Specifically, they still offer the most competitive and diverse product offering, and with ~6% market share and a 1:5 sales force ratio versus market leader MDT, they offer much larger territories with the highest commission rates among the full service players with no pay caps. The company is slowly migrating to a more direct model since their in IPO in 2012, from a 40% direct/60% distributor model to a 60% direct/40% distributor model, keeping with industry trends, though admittedly potentially disruptive. Adding to it's appeal the company also continues to churn out new products at a faster pace than any one else, and for 2017 the most incremental will be the launch of a stem cell product to compete with NUVA's OsteoCel (NUVA $65.43, BUY) — while this market has become increasingly crowded, bringing on pricing pressure, it's a notable hole in GMED's product offering and we anticipate at least an incremental revenue opportunity among its own customer base.

Margins and long-term outlook: Despite top-line disappointments in 2016, the company has been able to maintain EBITDA margins of approximately 37% and EPS of $0.27 for 3Q. We expect greater investment in 2017, but still expect Globus to hold margins in the mid 30% range. At their analyst meeting in February, management showcased their plan for 2020 -- double top-line sales to $1 billion (13% CAGR) while having bottom-line growth exceed top-line growth (14% CAGR, back-end loaded with mid-high single-digit growth in near term and mid-teens after) and maintaining best-in-class EBITDA margins of 35% (mid 30's or 33%-37%). This assumed spine would continue to grow in the double digits, with a 9% CAGR for the US and 22% internationally—this of course does not appear to be materializing in 2016 due to the sales force issues. Emerging technologies, including the robotics platform and trauma, should begin contributing in 2017 and by 2020 are expected to make up less than 15% of sales, which by then may include other adjacent market expansion opportunities. On the margin side, pricing pressures (low single digits) and increased biologics mix will pressure gross margins, offset by about $18 million in savings from the Branch manufacturing acquisition. Currently about 25% of products are made in house by Branch, though that is expected to increase to 50% by 2017, with likely more room to grow after that. Management also expects some SG&A leverage (the sales force is straight commission) with scale and continued lean design approach, but the biggest leverage is likely its tax rate (currently 35%), which should improve with a greater overseas mix and new tax initiatives being put in place in 2016, with impact beginning in 2017.

Trauma: While we are still a year away from a meaningful contribution (2017), we think the Trauma market is the perfect market for GMED to go after. Trauma is a $5.7 billion market with strong reimbursement coverage and consistent high single-digit growth -- roughly 2-3x faster than the spine market. The market has traditionally been dominated by JNJ/Synthes, which still has 45% market share, but the merger has defocused the company and created share gain opportunities just as it had in the Spine market (SYK has already seen a bump to its trauma business as a result). We think the opportunity may be even more exaggerated in Trauma, since post-merger, the company has de-emphasized its ties to its non-profit educational organization the AO (Arbeitsgemeinschaft für Osteosynthesefragen). The AO not only drove significant market share for Synthes, as it was instrumental in training the majority of trauma surgeons worldwide, but was also an important driver of product innovation – post-merger, this appears to have dropped off significantly. GMED management, including CEO David Paul, who prior to founding GMED was head of product development for Synthes spine business with some overlap in the trauma market, clearly see this as an opening and an opportunity to apply the same strategy used in spine to build a successful trauma business – specifically, combining a comprehensive portfolio with rapid innovation and iteration to upset the lack of innovation in the marketplace, something few investors would doubt GMED is uniquely positioned to execute on (though clearly they are starting from scratch in terms of infrastructure and product offerings). The initial rollout plan currently has 7 products under development to provide a comprehensive Trauma portfolio, and FDA submission and sales force buildup is expected to begin 2H17, with a modest revenue contribution in 2017 (~$5 million). Management is still considering an acquisition to kickstart trauma, but is focusing primarily on the tuck-in type, and does not have a specific target yet in mind, nor has an acquisition been built into their current forecast mentioned above.

Robotics Platform: The initial focus for the upcoming robotics platform will be pedicle screw placement, providing pre-op CT, intra-op CT, and fluoroscopy-guided imaging with full feature navigation (locked path but adjustable using the 'bracelet') via a robotic arm and without the need for k-wires, creating significant ease of use and time savings. They see this system as a competitor to Medtronic's O-Arm with Stealth Station navigation, which are navigation systems that don't include robotic assistance and retail for $1 million plus — GMED will look to charge a premium due to its added functionality. They believe there are about 900 O-Arms installed worldwide, and see many of these users as early adopters of technology and potential customers. GMED believes its system will save time and money and add a layer of predictability and accuracy (and of course significantly reduce fluoro exposure), which they intend to demonstrate through clinical studies. This will be especially important for MIS procedures, which account for 25% of procedures, though Globus expects MIS to grow to 70% by 2025 through the adoption of robotic techniques. It's also a platform technology that they intend to expand into other areas with, including neurosurgery and other orthopedic markets. The company is submitting the product for FDA clearance in 1H17, and expects a modest revenue contribution for 2017 — we are expecting about $5 million in revenues.

Alphatec's international business acquisition: The company purchased all of ATEC's international business for $80 million, plus a $30 million loan (which will generate interest, though not specifically used in management's guidance)—arguably just over 1x sales, but on a declining base. ATEC's international business generated $75 million in 2015, but at its current run rate is only expected to only generate $60 million this year and after accounting for dis-synergies GMED is anticipating only $40 million in 2017. The deal closed in September and should be neutral to 2016, accretive to 2017 and add $0.08 per share in 2018 and beyond. During this period, GMED will phase out ATEC products and substitute its own. Strategically, this doubles GMED's footprint internationally and provides infrastructure and a jump on entering the lucrative Japanese market (second largest in size) quicker than previously thought possible.

Globus Medical Inc. Revenue

	2014A	2015A				2015A	2016E				2016E	2017E				2017E	2018E
	Year	Q1A	Q2A	Q3A	Q4A	Year	Q1A	Q2A	Q3A	Q4E	Year	Q1E	Q2E	Q3E	Q4E	Year	Year
Innovative Fusion	**270.9**	**70.4**	**71.6**	**72.5**	**73.6**	**288.1**	**70.0**	**69.4**	**68.5**	**76.6**	**284.5**	**75.6**	**78.4**	**78.8**	**86.5**	**319.4**	**345.0**
%	6.6%	5.4%	8.7%	7.1%	4.4%	6.4%	-0.5%	-3.0%	-5.5%	4.0%	-1.2%	8.0%	13.0%	15.0%	13.0%	12.3%	8.0%
Disruptive Technology	**203.5**	**61.2**	**62.0**	**64.5**	**69.0**	**256.7**	**69.2**	**68.0**	**67.2**	**71.7**	**276.1**	**72.0**	**74.2**	**77.2**	**82.5**	**305.9**	**342.6**
%	12.8%	29.1%	29.9%	28.7%	18.3%	26.1%	13.0%	9.8%	4.1%	4.0%	7.6%	4.0%	9.0%	15.0%	15.0%	10.8%	12.0%
Total Revenues	**474.4**	**131.6**	**133.6**	**137.0**	**142.6**	**544.8**	**139.3**	**137.5**	**135.7**	**148.3**	**560.7**	**147.6**	**152.6**	**156.0**	**169.0**	**625.3**	**687.5**
%	9.2%	15.2%	17.6%	16.3%	10.7%	14.8%	5.8%	2.9%	-1.0%	4.0%	2.9%	6.0%	11.0%	15.0%	14.0%	11.5%	10.0%
US Sales	**427.1**	**120.0**	**121.5**	**125.7**	**131.1**	**498.2**	**127.6**	**124.7**	**120.5**	**129.1**	**501.8**	**126.9**	**127.2**	**127.7**	**135.5**	**526.9**	**562.2**
%	7.7%	18.0%	19.6%	17.9%	11.8%	16.6%	6.3%	2.7%	-4.1%	-1.5%	0.7%	-0.5%	2.0%	6.0%	5.0%	5.0%	6.7%
OUS Sales	**47.3**	**11.6**	**12.1**	**11.3**	**11.5**	**46.6**	**11.7**	**12.7**	**15.2**	**19.2**	**58.8**	**20.7**	**25.4**	**28.3**	**33.5**	**98.3**	**125.3**
%	24.9%	-7.0%	1.2%	1.0%	-0.8%	-1.5%	0.7%	5.4%	34.1%	66.5%	26.3%	77.0%	99.5%	86.4%	74.2%	*67%*	*27%*
Total Revenues	**474.4**	**131.6**	**133.6**	**137.0**	**142.6**	**544.8**	**139.3**	**137.4**	**135.7**	**148.3**	**560.7**	**147.6**	**152.6**	**156.0**	**169.0**	**625.3**	**687.5**

Source: Company reports and Aegis Capital Corp. Estimates

Globus Medical Inc. Income Statement

(Fiscal Years Ending December 31; $ millions)

	2014A	2015A				2015A	2016E				2016E	2017E				2017E	2018E
	Year	Q1A	Q2A	Q3A	Q4A	Year	Q1A	Q2A	Q3A	Q4E	Year	Q1E	Q2E	Q3E	Q4E	Year	Year
Net sales	$474.4	$131.6	$133.6	$137.0	$142.6	$544.8	$139.3	$137.5	$135.7	$148.3	$560.7	$147.6	$152.6	$156.0	$169.0	$625.3	$687.5
Cost of goods sold	$110.9	$32.1	$32.6	$33.1	$35.1	$132.8	$31.6	$32.9	$31.5	$34.1	$130.1	$34.7	$35.9	$36.7	$39.7	$146.9	$159.5
Gross profit	$363.5	$99.5	$101.0	$103.9	$107.5	$412.0	$107.6	$104.6	$104.2	$114.2	$430.6	$112.9	$116.8	$119.3	$129.3	$478.3	$528.0
Operating expenses:																	
R&D	$31.7	$8.7	$9.1	$9.4	$9.8	$37.0	$10.2	$11.3	$10.3	$11.1	$42.8	$11.4	$11.8	$12.0	$13.0	$48.1	$51.6
SG&A	$187.8	$52.3	$54.5	$53.8	$53.4	$214.0	$54.6	$52.9	$54.2	$57.8	$219.5	$59.1	$61.0	$62.4	$67.6	$250.1	$281.9
Other	$5.7	$0.0	$0.4	$0.0	($11.7)	($11.3)	$0.0	$0.0	$2.1	$0.0	$2.1	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Total operating costs	$225.2	$61.0	$64.0	$63.3	$51.5	$239.7	$64.8	$64.2	$66.5	$69.0	$264.5	$70.4	$72.8	$74.4	$80.6	$298.2	$333.4
Operating income (loss)	$138.4	$38.5	$37.0	$40.7	$56.0	$172.2	$42.8	$40.5	$37.7	$45.2	$166.2	$42.5	$44.0	$44.9	$48.7	$180.1	$194.6
Interest income/(expense)	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Other, net	$0.3	($0.3)	$0.4	$0.3	$0.2	$0.6	$0.8	$0.4	$1.2	$0.0	$2.4	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Total other	$0.3	($0.3)	$0.4	$0.3	$0.2	$0.6	$0.8	$0.4	$1.2	$0.0	$2.4	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Pretax income	$138.6	$38.2	$37.5	$40.9	$56.2	$172.8	$43.6	$40.9	$38.9	$45.2	$168.5	$42.5	$44.0	$44.9	$48.7	$180.1	$194.6
Income tax provision	$46.2	$13.5	$13.4	$14.4	$18.6	$60.0	$15.6	$13.4	$12.6	$15.7	$57.3	$14.5	$14.9	$15.3	$16.5	$61.2	$65.2
Net income	$92.5	$24.6	$24.1	$26.5	$37.6	$112.8	$28.0	$27.5	$26.2	$29.5	$111.2	$28.1	$29.0	$29.7	$32.1	$118.8	$129.4
EPS - Fully Diluted	**$0.97**	**$0.26**	**$0.25**	**$0.28**	**$0.39**	**$1.17**	**$0.29**	**$0.29**	**$0.27**	**$0.31**	**$1.15**	**$0.29**	**$0.30**	**$0.30**	**$0.33**	**$1.22**	**$1.36**
Litigation Impact to NI	$3.7	$0.0	$0.2	$0.0	($7.3)	($7.0)	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
EPS - Non GAAP Fully Diluted	**$1.01**	**$0.26**	**$0.25**	**$0.28**	**$0.32**	**$1.10**	**$0.29**	**$0.29**	**$0.27**	**$0.31**	**$1.15**	**$0.29**	**$0.30**	**$0.30**	**$0.33**	**$1.22**	**$1.36**
Average FD shares outstanding	95.5	95.9	96.0	96.1	96.2	96.1	96.2	96.4	96.5	96.7	96.5	96.9	97.2	97.4	97.6	97.3	95.0
Depreciation and Amort	$21.8	$5.7	$5.9	$6.1	$6.4	$24.1	$6.7	$7.0	$7.8	$6.3	$27.8	$6.3	$6.3	$6.3	$6.3	$25.0	$25.0
Stock Based Compensation	$7.1	$2.1	$2.5	$2.3	$2.7	$9.6	$1.8	$2.9	$2.7	$1.8	$9.2	$2.3	$2.3	$2.3	$2.3	$9.2	$9.2
Other	$3.9	$0.3	$0.8	$1.2	($11.6)	($9.2)	$0.0	($0.6)	$0.7	$0.0	$0.1	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Adjusted EBITDA	**$171.4**	**$46.3**	**$46.7**	**$50.5**	**$53.7**	**$197.3**	**$52.0**	**$50.2**	**$50.1**	**$53.2**	**$205.6**	**$51.1**	**$52.5**	**$53.5**	**$57.2**	**$214.2**	**$228.7**
Year-over-Year Change																	
Product revenue	9.2%	15.2%	17.6%	16.3%	10.7%	14.8%	5.8%	2.9%	-1.0%	4.0%	2.9%	6.0%	11.0%	15.0%	14.0%	11.5%	10.0%
Cost of goods sold	10.5%	26.8%	22.6%	19.4%	12.1%	19.8%	-1.4%	0.9%	-4.8%	-2.7%	-2.1%	9.6%	9.2%	16.6%	16.4%	13.0%	8.6%
R&D	17.9%	16.3%	18.0%	15.5%	17.0%	16.7%	17.8%	23.9%	9.1%	13.1%	4.5%	11.5%	4.4%	17.0%	17.0%	11.1%	10.4%
SG&A	2.9%	12.0%	17.4%	14.6%	11.9%	14.0%	4.4%	-2.9%	0.7%	8.3%	2.6%	8.2%	15.3%	15.1%	16.9%	13.9%	12.7%
Operating expense	-3.1%	7.6%	15.4%	14.7%	-11.0%	6.5%	6.3%	0.3%	5.2%	33.8%	10.3%	8.7%	13.4%	11.8%	16.9%	12.8%	11.8%
Operating income	36.1%	19.5%	17.4%	16.5%	41.2%	24.5%	11.2%	9.2%	-7.4%	-19.2%	-3.5%	-0.7%	8.6%	19.3%	7.6%	8.4%	8.0%
Pretax income	35.9%	17.5%	17.5%	17.6%	42.4%	24.6%	14.2%	9.1%	-5.1%	-19.6%	-2.5%	-2.4%	7.5%	15.6%	7.6%	6.8%	8.0%
Net income	34.8%	16.6%	16.5%	14.8%	36.0%	21.9%	13.5%	14.3%	-1.0%	-21.5%	-1.4%	0.3%	5.5%	13.1%	8.8%	6.8%	8.9%
EPS Fully Diluted	**12.5%**	**7.4%**	**12.3%**	**14.0%**	**4.8%**	**9.3%**	**13.0%**	**12.7%**	**-1.4%**	**-3.1%**	**4.7%**	**-0.4%**	**4.7%**	**12.0%**	**7.8%**	**6.0%**	**11.4%**
Margin Analysis																	
Gross Margin	76.6%	75.6%	75.6%	75.9%	75.4%	75.6%	77.3%	76.1%	76.8%	77.0%	76.8%	76.5%	76.5%	76.5%	76.5%	76.5%	76.8%
R&D	6.7%	6.6%	6.8%	6.9%	6.9%	6.8%	7.3%	8.2%	7.6%	7.5%	7.6%	7.7%	7.7%	7.7%	7.7%	7.7%	7.5%
SG&A	39.6%	39.7%	40.8%	39.3%	37.4%	39.3%	39.2%	38.5%	40.0%	39.0%	39.2%	40.0%	40.0%	40.0%	40.0%	40.0%	41.0%
Operating Margin	29.2%	29.3%	27.7%	29.7%	39.3%	31.6%	30.7%	29.4%	27.8%	30.5%	29.6%	28.8%	28.8%	28.8%	28.8%	28.8%	28.3%
Adjusted EBITDA Margin	36.1%	35.2%	35.0%	36.9%	37.7%	36.2%	37.3%	36.5%	37.0%	35.9%	36.7%	34.6%	34.4%	34.3%	33.9%	34.3%	33.3%
Pretax Margin	29.2%	29.0%	28.1%	29.9%	39.4%	31.7%	31.3%	29.7%	28.6%	30.5%	30.1%	28.8%	28.8%	28.8%	28.8%	28.8%	28.3%
Tax Rate	33.3%	35.4%	35.8%	35.3%	33.1%	34.7%	35.8%	32.7%	32.5%	34.7%	34.0%	34.0%	34.0%	34.0%	34.0%	34.0%	33.5%
Net Margin	19.5%	18.7%	18.0%	19.3%	26.4%	20.7%	20.1%	20.0%	19.3%	19.9%	19.8%	19.0%	19.0%	19.0%	19.0%	19.0%	18.8%

Source: Company reports and Aegis Capital Corp. Estimates

Required Disclosures

Price Target

$31

Valuation Methodology

Valuation: We are applying a 12-13x EV/EBITDA multiple to our 2017 estimate and adding back cash to get a $31 target price. We believe GMED can return to generating high single-digit revenue growth and see GMED as considerably less expensive than NUVA. We see the 12-13x range appropriate for small-cap med-tech companies.

Risk Factors

Risk: Risks to the achievement of our target price include (1) increased competition from larger players with more resources or smaller players with more focused portfolios, (2) slower than expected market uptake on key products, (3) sales force hiring and training slower than expected and (4) spine market instability.

For important disclosures go to www.aegiscap.com.

We, Jason Wittes and Evan Wang, hereby certify that the views expressed in this research report accurately reflect our personal views about the subject companies and their securities. We also certify that We have not been, do not, and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendations in this report.

Research analyst compensation is not dependent upon investment banking revenues received by Aegis Capital Corp.

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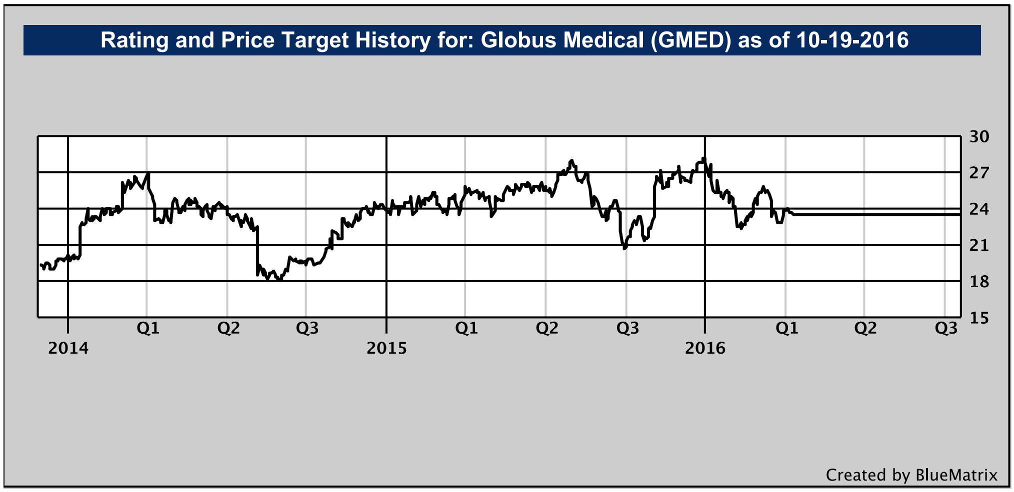
Neither the research analyst who prepared this report or a member of the research analyst’s household has a financial position in the debt or equity securities of the subject company.



Rating	Percent	Investment Banking Services/Past 12 Mos. Percent
BUY [BUY]	85.85	37.36
HOLD [HOLD]	14.15	20.00
SELL [SELL]	0.00	0.00

Meaning of Ratings

A) A Buy rating is assigned when we do not believe the stock price adequately reflects a company's prospects over 12-18 months.

B) A Hold rating is assigned when we believe the stock price adequately reflects a company's prospects over 12-18 months.

C) A Sell rating is assigned when we believe the stock price more than adequately reflects a company's prospects over 12-18 months.

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