

Orthofix Medical Inc. NasdaqGS:OFIX

FQ4 2022 Earnings Call Transcripts

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S&P Global Market Intelligence Estimates

	-FQ4 2022-			-FY 2022-			-FY 2023-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS
EPS Normalized	0.34	0.19	▼ (44.12 %)	0.44	0.30	▼ (33.33 %)	(1.66)
Revenue (mm)	122.18	122.23	▲ 0.04	460.66	460.71	▲ 0.01	752.50

Currency: USD

Consensus as of Jan-25-2023 11:09 PM GMT

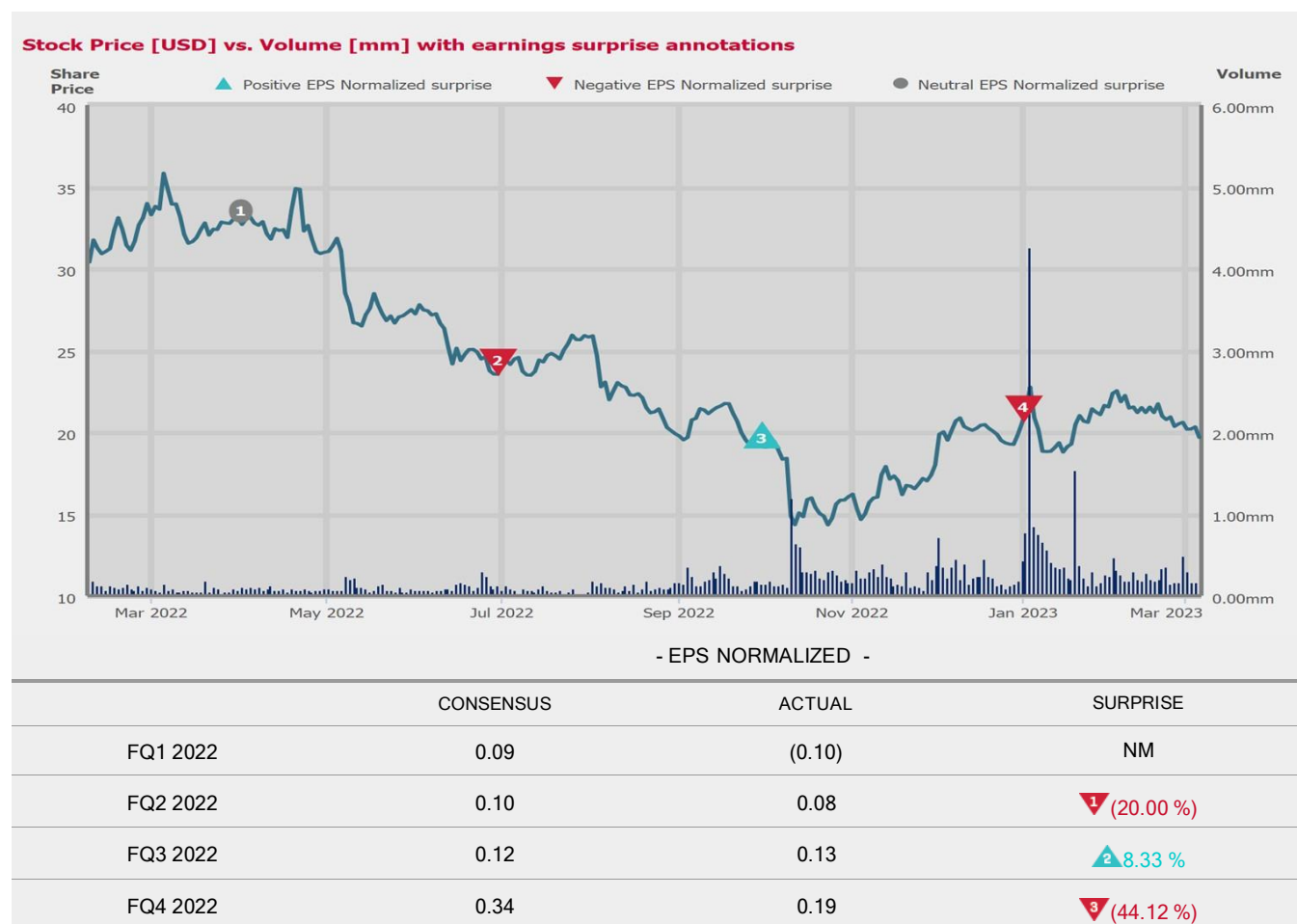


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Call Participants

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Presentation

Operator

Good afternoon, and welcome to Orthofix Medical's Q4 and Full Year 2022 Earnings Call. [Operator Instructions] As a reminder, this conference call is being recorded.

I would now like to turn the call over to Alexa Huerta, Senior Director of Investor Relations. Thank you. Please go ahead.

Alexa Huerta

Thank you, operator, and good afternoon, everyone. Welcome to the Orthofix Fourth Quarter 2022 Earnings Call. Joining me on the call today are President and Chief Executive Officer, Keith Valentine; and Chief Financial Officer, Jon Serbousek, as well as our Executive Chairman of the Board; and Orthofix's former Chief Executive Officer; Jon Serbousek; and former Chief Financial Officer, Doug Rice.

During this call, we will be making forward-looking statements that involve risks and uncertainties. All statements other than those of historical facts are forward-looking statements, including any financial guidance we provide and any statements about our plans, beliefs, strategies, expectations, goals or objectives. Investors are cautioned not to place undue reliance on such forward-looking statements as there is no assurance that the matter contained in such statements will occur. The forward-looking statements we will make on today's call are based on our beliefs and expectations as of today, March 6, 2023. We do not undertake any obligation to revise or update such forward-looking statements.

Some factors that could cause actual results to be materially different from the forward-looking statements made by us on the call include the risk factors disclosed under the heading Risk Factors in our Form 10-K for the year ended December 31, 2022, filed this afternoon, March 6, 2023 as well as additional SEC filings we make in the future. If you need copies of these documents, please contact my office at Orthofix in Lewisville, Texas.

In addition, on today's call, we will refer to various non-GAAP financial measures. We believe that in order to properly understand our short-term and long-term financial trends, investors may wish to review these measures as a supplement to the financial measures determined in accordance with U.S. GAAP. Please refer to today's press release announcing our fourth quarter and full year 2022 results for reconciliations of these non-GAAP financial measures to our U.S. GAAP financial results.

We will begin today's call with commentary from Keith Valentine and Jon Serbousek on standalone SeaSpine fourth quarter results, followed by Jon Serbousek and Doug Rice, who will speak to the standalone Orthofix fourth quarter results. Keith will conclude the call with information on the newly combined company, including 2023 revenue guidance and some additional future-looking commentary from Orthofix.

At this point, I will turn the call over to Keith.

Keith C. Valentine *President, CEO & Director*

Thank you, Alexa, and thank you, everyone, for joining us this afternoon. Before we get into each company's standalone results, I'd like to take a moment to highlight the recent closing of the merger of equals between Orthofix and SeaSpine. This merger significantly advances our objective to become a surgeon's partner of choice in their efforts to increase patient mobility and quality of life. Together we will continue to develop creative, quality-driven procedural solutions through expanded commercial access and commitment to innovation.

The new Orthofix has an improved profile of scale, growth and potential operating leverage in addition to a highly complementary portfolio, expanded commercial reach and the capacity to make meaningful investments in organic and inorganic innovation. We believe our comprehensive product offering puts us in a highly differentiated position in the spine market by combining lead bone growth therapies, enabling technologies, spinal fixation, motion preservation and biologics. We see this combined company as a transformative organization in the musculoskeletal space that will address unmet clinical needs to improve the lives of patients worldwide.

Turning to the results. SeaSpine had a strong year marked by the consistent execution of our growth strategy, capturing a market share and the announcement of the pivotal merger with Orthofix. We are excited by the momentum coming out of our fourth quarter results and the work our teams have done since the business combination on January 5. SeaSpine's revenue for the fourth quarter was \$63.4

million, representing 14% growth over the prior year. Additionally, we posted full year revenue of \$237.5 million, up 24% year-over-year.

U.S. Spinal Implants and Orthobiologics revenue grew 23% and 20%, respectively, in the fourth quarter over the prior year, primarily from new products and expanded distribution as a result of our efforts in recent years to partner with larger, more focused distributors. As for the enabling technologies platform, we placed 30 units of the 7D surgical FLASH navigation systems throughout 2022, achieved our 100th unit placement milestone and expanded our installed base into 6 new countries, a testament to our commitment for increased competitiveness across global markets. In the fourth quarter placed a record 12 units, 5 in the U.S. and 7 outside the U.S. Of those placed in the U.S., 3 were earnout arrangements, the largest quarterly placement of earnouts since we acquired the technology.

As you may recall, these earnout agreements are a capital-efficient way for hospital systems to acquire a 7D unit in return for a minimum annual contractual revenue commitment for our spinal implant or biologics products for 3 to 4 years, typically at a rate of \$600,000 to \$800,000 per year. To date, we have executed 7 earnouts that represent approximately \$4 million in aggregate annual revenue commitments.

I'd also like to call out the company's successful execution of further portfolio expansion through differentiated solutions across a broad spectrum of products and services in the fourth quarter such as the launch of the first component of our [Inside Suite] planning software for preoperative screw planning and the full commercialization of our percutaneous procedure support software enabled through the 7D FLASH navigation system. Additionally, we recently announced the full commercial launch and first patient cases of Mariner deformity system, which was built upon the strength and versatility of SeaSpine's modular Mariner pedicle screw system to address the unique clinical requirements of complex adult deformity spine cases while also reducing the number of surgical trays in the operating room suite.

These portfolio advancements are indicative of our commitment to restoring mobility and quality of life to patients. And we are very much looking forward to further integrating the 2 highly complementary organizations to establish an industry leader in spine and orthopedic technology.

I will now turn the call over to Jon Serbousek to review the standalone SeaSpine financial results for the fourth quarter and full year 2022.

Jon Serbousek
Chief Financial Officer

Thanks, Keith, and good afternoon, everyone. As Keith noted earlier, SeaSpine's total revenue for the fourth quarter of 2022 was \$63.4 million a 14% increase over the prior year. In the U.S., we posted 16% growth. U.S. Spinal Implant and Enabling Technologies revenue in the fourth quarter increased 12%. Within that category, U.S. Spinal Implant revenue increased by more than 23%. Products launched or enhanced via line extensions within the past 5 years continue to grow revenue and accounted for 82% of U.S. Spinal Implant revenue in the fourth quarter of 2022.

International's spinal implant sales were down 57% in the fourth quarter due to our recent exit from the European Spinal Implant market in the third quarter of 2022. U.S. Biologics revenue in the fourth quarter increased 20% and continues to be driven by growth in the OsteoStrand Plus Demineralized Bone Fibers product family. Our U.S. Spinal Implant surgery volumes increased 23% compared to the fourth quarter of 2021, while revenue per case increased 4% compared to the prior year. Utilization of our spinal implant systems and orthobiologics products increased over 9% to 2.3 per procedure in the fourth quarter of 2022 compared to 2.1 a year ago. We experienced mid-single-digit average price declines in spinal implants and no price declines in biologics.

As a reminder, the substantial majority of SeaSpine's revenue was generated in U.S. dollars, so foreign currency exchange rate changes did not have any meaningful impact on our reported growth rates. GAAP gross margin for the fourth quarter of 2022 was 62.5% compared to 53.7% for the fourth quarter of 2021. Adjusted gross margin was 64% for the fourth quarter of 2022 compared to 61.8% for the fourth quarter of 2021. The increase in adjusted gross margin was primarily due to the greater relative growth in higher gross margin domestic spinal implants revenue, the reduction in OUS spinal implants revenue as a result of the recent European market exit and continued efficiencies realized in the manufacturing of our biologics product lines.

Operating expenses for the fourth quarter of 2022 totaled \$59.8 million, a \$10.9 million increase compared to the fourth quarter of 2021. The increase in operating expenses was driven primarily by \$5.3 million in higher selling and marketing expenses attributable to increased commissions and freight and logistics costs associated with the revenue growth and \$5.2 million in higher general and administrative expenses due primarily to increased headcount-related compensation expenses, increased legal and other professional fees incurred in preparation for the merger with Orthofix.

Net loss for the fourth quarter of 2022 was \$19 million compared to a net loss of \$18.8 million for the fourth quarter of 2021. Adjusted EBITDA loss for the fourth quarter of 2022 was \$5.7 million, an improvement compared to a loss of \$6.7 million for the fourth quarter of 2021. Adjusted gross margin and adjusted EBITDA loss are non-GAAP financial measures that we believe provide valuable information on our operating results by facilitating comparability of our core operating performance from period to period and against other companies in our industry.

The calculation of adjusted gross margin and a reconciliation of GAAP net loss to adjusted EBITDA loss are presented in the financial tables of the press release we issued this afternoon. Cash and cash equivalents on December 31, 2022, totaled \$29 million and included \$26 million of outstanding borrowings under the SeaSpine credit facility, which we subsequently paid off in full on January 5 in connection with the merger with Orthofix.

Our free cash flow burn, which includes operating cash flows and purchases of property and equipment, was \$16.7 million for the fourth quarter of 2022 and \$75.9 million for the full year 2022. This spent is consistent with a large amount of inventory and set build capital expenditures necessary to support the recent and upcoming full product launches as well as our above-market U.S. revenue growth. As for additional detail on the full year revenue results that Keith mentioned earlier, 2022 revenue was \$238 million, a 24% increase over 2021. U.S. revenue grew 19%, international revenue increased by 66% and was driven primarily by the final stocking orders to distributors in connection with SeaSpine's exit from the European Spinal Implants market in the third quarter of 2022 and from significant revenue growth from the Enabling Technologies franchise.

U.S. orthobiologics revenue grew 17% year-over-year in 2022. The U.S. Spinal Implant surgery volumes increased 23% compared to full year 2021 as revenue per case increased 4% over the prior year. Utilization of our spinal implant systems and orthobiologics products increased to 2.2% per procedure in 2022 compared to 2.1% in 2021.

I'd now like to turn the call over to Jon Serbousek to provide highlights on Orthofix's standalone 2022 results.

Jon C. Serbousek
Executive Chairman

Thank you, John. As announced earlier in January, total revenue in the quarter was \$122.2 million, decreasing 2% over 2021 on a reported basis and flat to 2021 on a constant currency basis. Strategic investments in our commercial channel and new products are paying off as global orthopedics and bone growth therapies continued their strong performance through the fourth quarter.

Specific to innovation, we are encouraged by several new products we introduced in 2022. The AccelStim bone-healing therapy for fresh fracture and nonunion fractures, TrueLok EVO, which added radiolucent rings and struts to our market-leading ring fixation system, and Galaxy Gemini, our next-generation pin-to-bar system have all been well received in the marketplace. We've also launched 2 new biologic solutions in 2022 with our partnership with MTF Biologics, the Virtuos Lyograft, a shelf stable complete autograph substitute and legacy, it can mineralize bone matrix.

Turning to the performance of each of our product categories, starting with Bone Growth Therapies or BGT. Sales for the quarter were \$51 million, up 3% on both a reported and constant currency basis compared to the fourth quarter of 2021. Growth was driven by revenue from a AccelStim, our most recent bone-growth therapy solution with a new indication for fresh fracture care, which grew almost 50% sequentially over the third quarter of 2022 as we continued our commercial rollout.

Moving to spinal implants, which includes both spinal fixation and motion preservation. Revenue was down approximately 7% on both a reported and constant currency basis compared to the fourth quarter of 2021. The decline is driven mainly by continued global competitive headwinds at our motion preservation area as well as a decline in procedural ASPs in the spine fixation on flat volumes in the U.S. We did see an encouraging 20% sequential increase in surgeon training for the U.S. M6-C artificial cervical disc in the fourth quarter of 2022.

Turning to our Biologics portfolio. Revenue was down 9% on a reported and constant currency basis compared to 2021. We saw declines coming from some of our Trinity accounts driven primarily by sales channel disruption and offset somewhat by sales from our newer biologic solutions. The results from the merger will help growth initiatives in these franchises going forward as we will be able to offer new innovation solutions to our customers as well as additional options for our surgeon partners.

In our global orthopedics business, revenue for the fourth quarter was down 2% on a reported basis and up 6% on a constant currency basis over 2021. Growth at constant currency in both our U.S. and international businesses was driven by strategic investments in our commercial channels and momentum from new product introductions mentioned earlier.

Now moving on to a few highlights from our strategic initiatives. Let's start with product innovation and differentiation. In the fourth quarter, we continue to see AccelStim bone healing therapies gain traction. We are seeing a high rate of physician interest and now have access to new prescribing doctors. We are encouraged by our 2022 commercial rollout and revenue results. We have increased the number of sales reps 4% and added additional sales management to help grow our fracture channel with both fresh and nonunion fracture indications. Currently our payer coverage for AccelStim includes over 80 million lives, and we expect that positive trajectory to continue.

Turning to our second initiative. The ongoing development of our commercial channel to expand patient and surgeon access to our products worldwide. In 2022, we have continued to invest in our development and optimization of our fracture channel and our orthopedic channel investments have paid off both in the U.S. and internationally to support continued growth.

Now I'll turn the call over to Doug to review Orthofix's fourth quarter 2022 financial performance. Doug?

Douglas Rice

Thanks, Jon, and good afternoon, everyone. As many of the financial measures covered in today's call are on a non-GAAP basis, please refer to today's earnings release for further information regarding our non-GAAP reconciliations and disclosures.

Starting with revenue. As Jon noted earlier, total net sales in the quarter were \$122.2 million, reflecting flat sales at constant currency when compared to the fourth quarter of 2021. In the U.S., total net sales were \$95.7 million or 78% of total revenue, down approximately 2% versus the prior year. The primary drivers were declines coming from competitive pressure in biologics and spinal implants as well as decreased procedural ASPs in spinal implants, offset somewhat by growth coming from the BGT new product introduction of AccelStim and continued momentum in orthopedics.

International total net sales were \$26.6 million or 22% of total revenue, up 6% in constant currency over the fourth quarter of 2021 as a result of strong growth from strategic investments in the commercial channel and momentum coming from new product introductions. Full year revenue came in at \$460.7 million, up 1% at constant currency and down 1% as reported. The highlight for 2022 was 11% constant currency growth in our Global Orthopedics segment as a result of the strategic investments we made in our commercial channels and new product momentum.

GAAP gross margin in the fourth quarter of 2022 was 73%, which was consistent with the prior year period despite changes in sales mix and volumes. GAAP sales and marketing expenses in the fourth quarter were 49% of net sales, up from 46% in the fourth quarter of 2021. This increase is primarily driven by an increase in event spending due to the timing of trade shows as well as an increase in marketing and sales training spend to bring on new commercial distribution.

GAAP G&A expenses in the fourth quarter were 21% of net sales, up from 15% in the prior year period. The increase reflects higher spending on legal and professional fees primarily related to the recent merger with SeaSpine. GAAP R&D expenses for the fourth quarter stayed flat at 11% of net sales compared to the prior year period. Our focus on R&D continues to be on bringing innovative and differentiated new products to the market. Adjusted EBITDA margin in the fourth quarter was 13% of net sales, down slightly from 14% of net sales compared to the same quarter of 2021. On a dollar basis, adjusted EBITDA in the fourth quarter was \$15.8 million, down from \$17 million in the fourth quarter of the prior year.

Now turning to tax. We reported GAAP income tax expense of \$75,000 or 1% of the loss before income taxes in the quarter as compared to the prior year expense of \$23.2 million or a 242% of loss before income taxes in the same period of 2021. The tax rate in both periods is driven by timing of earnings as well as GAAP losses without a corresponding tax benefit. In particular, we fully reserved our U.S. deferred tax assets in the fourth quarter of 2021, which was a significant component of the disproportionately high reported GAAP tax rate last year.

For the fourth quarter, we reported a GAAP loss of \$0.35 per share as compared to a GAAP loss of \$1.65 per share in the fourth quarter of 2021. After adjusting for certain items and when normalizing for tax using our non-GAAP long-term effective tax rate of 28%, adjusted EPS for the fourth quarter of 2022 was \$0.19 as compared to an adjusted EPS of \$0.27 in the fourth quarter of 2021.

Regarding cash, our liquidity position remains strong with \$51 million in cash at December 31, 2022, and nearly \$100 million of current borrowing capacity under the Orthofix credit facility. Our free cash flow burn was \$34.7 million for the full year 2022 and included strategic investments in inventory and Spinal Implant set builds and over \$5 million in contractual milestone payments related to our partnerships with IGEA, CGBio, FITBONE and MTF to accelerate new product innovation to support revenue growth as well as merger and integration costs and \$23 million in CapEx for spine implant set builds and leasehold improvements to our Lewisville, Texas headquarters building.

As of December 31, 2022, Orthofix had no borrowings under its \$300 million secured revolving credit facility. However, on January 3, 2023, Orthofix borrowed \$30 million under this credit facility, in part to fund the full repayment of SeaSpine's \$26.2 million outstanding borrowing against its credit facility as well as for working capital purposes and for certain merger-related expenses. Furthermore, on March 3, 2023, Orthofix borrowed an additional \$15 million under the credit agreement for continued working capital purposes and to help fund merger integration-related costs.

I'll now turn the call over to Keith to provide closing comments and 2023 guidance.

Keith C. Valentine
President, CEO & Director

Thanks, Doug. As you've heard today, we are excited about the momentum, both standalone companies generated coming out of 2022 and are very much looking forward to building a leading global spine and orthopedics company in the years to come. The combination of these 2 innovative and ambitious organizations is incredibly energizing. The combined company will ultimately and most importantly, provides surgeons with the best resources, technologies, products and procedures needed to improve patient outcomes. We believe that the combined product portfolios are very complementary and that we can leverage the best-in-class technologies for each organization to offer the most innovative solutions along the continuum of care, pre and postoperatively.

Orthofix will be hosting an analyst teach-in on March 13 at our Lewisville facility, where our business unit presidents will provide additional color on these complementary product portfolios, our planned commercial strategies and expected future growth drivers within each segment and franchise. We invite investors to join us via webcast.

In terms of financial guidance, at this point, we are providing a revenue range for the full year 2023 between \$743 million to \$753 million, which represents 7% to 9% year-over-year constant currency growth compared to the approximately \$701 million of pro forma combined company revenue for full year 2022 after giving effect to anticipated reclassifications to conform SeaSpine's revenue reporting to that of Orthofix.

Because we are still very early in the integration phase, we suggest that investors and analysts set their expectations towards the low end of that range until we can provide more clarity later this year on how effectively we are managing the approximately \$20 million of revenue dis-synergy risk and how quickly we can take advantage of the greater than \$25 million of cross-selling opportunities in 2023. So far, we are very pleased with our ability to manage and mitigate those possible revenue dis-synergies.

Additionally, we expect first quarter 2023 revenues in the range of \$166 million to \$170 million, which represents 7% to 10% year-over-year constant currency growth compared to the approximately \$158 million of pro forma combined company revenue for the first quarter 2022. After giving effect to anticipated reclassifications to conform SeaSpine's revenue reporting to that of Orthofix.

We do not plan to provide quarterly revenue guidance going forward. However, since the first quarter of 2023 is more than 2/3 completed and because we are providing a fairly wide initial revenue range for the full year, we wanted to provide that additional data point on this call. Also note that any sales generated by SeaSpine for the premerger period of January 1 through January 4, 2023, will not be included in the combined company's first quarter or full year 2023 revenue results.

We are still on track with initially reported expectations to generate approximately \$40 million of operating expense synergies by year 3 post merger. With the bulk of those synergies coming from redundant corporate overhead included in G&A, redundant headcount and program spending and Spinal Implant's R&D, sales and marketing and from a meaningful reduction in IT system-related costs as we integrate a portfolio very common and in many cases overlapping IT systems. Cost to achieve those synergies are expected to be around \$40 million, but the majority of that spend occurring in 2023, 20% incurred in 2024 and the remainder in 2025. And as we get further into the integration process, we will provide additional reporting and guidance metrics.

Before closing out my prepared remarks, I would like to highlight the upcoming change to our Board of Directors. Jon Serbousek, our Executive Chairman, will not stand for reelection as a Director of Orthofix at the company's 2023 Annual Stockholders Meeting coming up in June of this year. He will remain an employee of the company through July 5, 2023. We are very appreciative of the years of leadership and the contributions from John. And I look forward to maintaining our friendship going forward.

I'm extraordinarily excited about the prospects for Orthofix. And I know our team is already making great strides to create one of the broadest biologics and regenerative technology portfolios in the industry.

At this point, operator, please open up the line for questions.

Question and Answer

Operator

[Operator Instructions] Our first question comes from Mathew Blackman from Stifel.

Mathew Justin Blackman

Stifel, Nicolaus & Company, Incorporated, Research Division

Let me start with the -- and I appreciate the topline guidance for 1Q in 2023. But maybe it would be helpful for both you, Keith and John, we've obviously worked with you before. We know your philosophy on guidance from your time at SeaSpine. But how should we think about your views now on guidance sitting in this new seat, in particular, guiding during an integration? Is your philosophy you put out guidance, we can hit, guidance we can beat? Is there any cushion in there perhaps for the unknown?

And then just a quick follow-up on that. I just want to be clear. It sounds like in the commentary from the press release at least that there are no revenue -- or no material revenue synergies baked into the '23 guide. Is that full \$20 million of dis-synergies baked into that guide? And if so, does that manifest largely in the global spine business on the Spinal Implant business? And then I've got one follow-up question.

Jon Serbousek

Chief Financial Officer

All right. That's a lot to unpack. First question, on the guidance, the Q1 number, obviously, we're more than 2/3 of the way through the quarter. So we feel pretty good about how things are shaping up and really pleased to see the growth across just about all portfolios on both companies in those Q1 numbers. So I think that speaks to the confidence we have in mitigating the dis-synergy risk that seemed to be a lot of concerns when we first talked about the merger.

For the full year number, I think Keith's comments were spot on that we'd expect everybody to kind of set expectations towards the low end of that range because it is still early, and that's why we gave a fairly wide range for the full year is to kind of set a baseline. And yes, you know us, Matt, and our historical practice of wanting to make sure we set a realistic bar that we're not going to come under. And so far, the success we've had with managing that dis-synergy risk, we feel really good about that 2 months into the merger. The fact that all the portfolios on both sides of the company are growing in the first quarter, I think, is a good trend for the full year. But yes, we do want to be cautious about setting full year expectations for such a wide time frame because there is still the potential for dis-synergy risk.

We think the timing of when we'll get Spinal Implant sets to create some of the upside revenue synergy opportunities is fairly extended lead times, which will probably be most impactful later in the year, Q4 to set a realistic time frame. So we still need to manage those dis-synergy risks, and we don't see a lot of near-term opportunity on the revenue upside for the synergies. So we are being cautious about setting full year guidance. And as Keith said, right, we expect everybody to start on the low end, and hopefully, we'll have opportunities to raise that as the year goes by and we get past more of those revenue dis-synergy risks and continue to mitigate those. But also have better clarity as to what the upside can be for the full year on the revenue synergy possibility as we get delivery of some of those sets that we've ordered on the Spinal Implant side.

So I think that addressed everything you're asking.

Mathew Justin Blackman

Stifel, Nicolaus & Company, Incorporated, Research Division

John, I'll try to make this follow-up a little bit shorter. Just curious, and I think you've sort of touched on it here, early days still, but maybe dis-synergies tracking as expected. Just any commentary on sales force stability in 4Q after the announced deal and now into 1Q '23? Just any sort of early commentary on retaining the folks you want to retain and any discussions going on with distributors moving into more exclusive or pulling in new distributors entirely? Just any color on that would be helpful, appreciated.

Keith C. Valentine

President, CEO & Director

Yes. You bet, Matt. So we're very excited how Q1 has kicked off. I mean, we gave some color to being 2 months in. And part of that is because there is a great deal of strength just as we had anticipated when we did our first kind of quarterly review of what

overlap would be. We're really excited about the lack of concerning overlap, if you will, but more importantly, the opportunity for real

synergy. And so we're already seeing cross cases. We're already seeing cases that go on that are using both legacy original company products together as a true merged company, including 7D as part of that as well.

And I think that's a testament to how we're approaching it also from a sales management perspective. I think the sales management process and the selections we've made and what the team looks like is a nice combination of leadership that also brings with it, I think, a good deal of stability to those sales teams. And without a doubt, we're excited about what's going on in the marketplace right now. There is a number of, I think, very interesting opportunities for us to take advantage of even greater sales penetration due to other opportunities out there from other companies merging.

Operator

Our next question comes from Jeffrey Cohen from Ladenburg Thalmann.

Jeffrey Scott Cohen
Ladenburg Thalmann & Co. Inc., Research Division

Congrats on the call and the merger. So I guess, firstly, John, you knew this one was coming, but I wanted to ask about segmentation reporting going forward. How are you going to look at that? Is that going to be U.S. international? Is it going to be hardware biologics, et cetera?

Jon Serbousek
Chief Financial Officer

Yes. We're still in the evaluation phase of what the reportable segments will be like because we got to figure out right, how we're going to run the business internally, along portfolio line. So we'll definitely plan to give more color as to the segment reporting once we've made those final decisions. And I think we'll have those by the first quarter reporting deadline. So no decisions made at this point yet, but clearly something we're evaluating as we go forward and look at how we want to run the business.

Jeffrey Scott Cohen
Ladenburg Thalmann & Co. Inc., Research Division

And then can you give us a sense of some of the G&A expenditures forwarding some of the synergies that you talked about? It looked like Q4 had about \$9 million higher on G&A from plus 3 plus 6 from each side? And how should we think about that for Q1 and the balance of the year before some of these synergies start kicking in, at least on the G&A front?

Jon Serbousek
Chief Financial Officer

So you're asking about how Q1 will compare to Q4 and expectations for deal costs?

Jeffrey Scott Cohen
Ladenburg Thalmann & Co. Inc., Research Division

Yes. I think as you're -- it looks talk about \$9 million spent in the fourth quarter. So does that tail off in the first quarter swiftly or not swiftly? Or is it going to take a few quarters?

Jon Serbousek
Chief Financial Officer

So deal-specific costs will probably be another heavy quarter in Q1 in terms of spend, right? Because there's still ongoing legal fees kind of right up to the end, a lot of the banker fees will get paid post-closing. So that's a that's a Q1 transaction time line. Then we'll shift to more cost to achieve the synergies. As Keith mentioned in his scripted comments, right, the severance costs will increase and be probably most heavy in the middle part of this year. So we'll transition from what I call, deal setup and closing costs to now cost onetime cost to achieve the synergies, the bulk of which this year will likely be IT system integration costs and headcount costs occurring over Q3 -- Q2 and Q3 probably.

Operator

[Operator Instructions] Our next question comes from Dave Turkaly from JMP Securities.

David Louis Turkaly

Maybe one for Bos. I don't want to put him on the spot here, but I guess what I'm trying to look at here is either range or targeted area for either free cash flow or earnings. I imagine you're not going to want to comment on that, and I understand. But how about even timing? When do you think we'll be ready to sort of put this together and have sort of directionally some bottom line targets as well?

Jon Serbousek
Chief Financial Officer

Yes. It's clearly a focus for the first quarter to be able to get through the integration and now we're running our annual operating plan for the combined company and digesting the synergies, going through what we built into the deal model. So I think we have a good sense at a high level and talk about some high-level financial metrics and expectations that were built in the deal model. But yes, we're just not in a position to give any kind of clarity beyond the topline because we're still working through that first combined company operating plan. But I suspect we'll be in a better position to give more color down the P&L and in terms of big picture cash flow on our first quarter call in early May.

David Louis Turkaly
JMP Securities LLC, Research Division

And then I know that both the companies have worked on the commercial expanding the teams. I think SeaSpine said, they focus on larger distributors of late. Will you guys combine be able to take advantage of all the changes you've made both on the OpEx and the SeaSpine side? I think you said not a lot of overlap, but even some of these new changes, would that be true that you'll be able to maintain some of the new choices you've made both sides?

Keith C. Valentine
President, CEO & Director

I do. I think that there's even opportunities were already in some discussions of current territories that even there's light overlap and how they can combine together. I think there's been -- we're fortunate. I think we're fortunate that we have a distribution teams that are excited about what the company's new portfolio is and how broad it is. And they want to be part of this growth profile.

So I do feel very comfortable that the continued innovation will drive excitement for them as well because they see the future. They see the future is not just what the company looks like today, but we have a 2 to 3-year plan of even more innovation that will be exciting for the marketplace.

David Louis Turkaly
JMP Securities LLC, Research Division

And maybe one last one, if I could just squeeze one in. You mentioned on the SeaSpine part, the exit from Europe and I know if it works to fix, it's been some of the legacy sort of geography that certainly, at least in Italy and some other places was important. Is that -- when you combine do you wind up, the Orthofix still stays there and you cross-sell with them? Or what are your thoughts on Europe specifically, if you had just recently, I think, exited at least for some of your products?

Keith C. Valentine
President, CEO & Director

Yes. I think Europe is a complicated challenge right now, to be frank. There's a lot of regulation. Some of it's getting pushed down the road, but still creates a great deal of, I would say, not even additional. It's dramatic expense to how you're going to promote and be able to market a product and sell a product in Europe. I think we're very fortunate that the traditional orthopedic business that's based out of Verona has been in place for a very long time. And they're in a different situation than I would categorize what Spinal Implants, specifically has to deal with.

And so we'll continue to evaluate. We'll continue to evaluate how the European regulatory groups drive forward with some new plans that they're promising. But at this time, we wanted to be cost effective, a profitable venture for Spinal Implants in Europe. And we'll continue to pursue it in such a way.

Operator

We have no further questions in queue. I would like to turn the call back over to Keith Valentine for closing remarks.

Keith C. Valentine
President, CEO & Director

So thank you again for joining us this afternoon. I'd like to save some over 1,500 dedicated employees in the Orthofix family. We appreciate your interest in the call and joining us today. We look forward to speaking to many of you throughout the rest of 2023 and hope you all have the opportunity to join us online at the teaching event coming up on March 13. Have a great evening.

Operator

This concludes today's conference call. Thank you for your participation. You may now disconnect.

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