Henry Schein, Inc. (HSIC) CEO Stanley Bergman on Q3 2019 Results - Earnings Call Transcript

Nov. 5, 2019 3:25 PM ET | 3 Likes
by: SA Transcripts

Q3: 11-05-19 Earnings Summary

Press Release SEC *10-Q*

EPS of $0.9 beats by $0.04 | Revenue of $2.51B (-23.51% Y/Y) misses by $-8.48M

Earning Call Audio

Subscribers Only

0:00:00 -1:04:32

Henry Schein, Inc. (NASDAQ:HSIC) Q3 2019 Results Earnings Conference Call
November 5, 2019 10:00 AM ET

Company Participants

Carolynne Borders - Vice President of Investor Relations

Stanley Bergman - Chairman of the Board, Chief Executive Officer

Steven Paladino - Executive Vice President, Chief Financial Officer

Conference Call Participants

Glen Santangelo - Guggenheim

Jon Block - Stifel

Jeff Johnson - Baird

Courtney Owens - William Blair

Nathan Rich - Goldman Sachs

Operator

Good morning ladies and gentlemen and welcome to the Henry Schein third quarter 2019 conference call. All lines have been placed on mute. All participants are in listen-only mode. Later, we will conduct a question-and-answer session and instructions will follow at that time. [Operator Instructions]. As a reminder, this call is being recorded.

I would now like to introduce your host for today's call, Carolynne Borders, Henry Schein's Vice President of Investor Relations. Please go ahead, Carolynne.

Carolynne Borders

Thank you Holly. Before I begin, I want to make sure that we no longer have that background noise. It sounds like it is now muted. Thank you. Thanks to each of you for joining us to discuss Henry Schein's results for the 2019 third quarter. With me on the call today are Stanley Bergman, Chairman of the Board and Chief Executive Officer of Henry Schein and Steven Paladino, Executive Vice President and Chief Financial Officer.

Before we begin, I would like to state that certain comments made during this call will include information that is forward-looking. As you know, risks and uncertainties involved in the company's business may affect the matters referenced to in forward-looking statements. As a result, the company's performance may materially differ from those expressed in or indicated by such forward-looking statements.

These forward-looking statements are qualified in their entirety by the cautionary statements contained in Henry Schein's filings with the Securities and Exchange Commission, including in the Risk Factors section of our Annual Report on Form 10-K. In addition, all comments about the markets we serve, including end-market growth rates and market share, are based upon the company's internal analysis and estimates.

Our conference call remarks will include both GAAP and non-GAAP results. We believe the non-GAAP financial measures provide investors with useful supplemental information about the financial performance of our business, enable the comparison of financial results between periods where certain items may vary independently of business performance and allow for greater transparency with respect to key metrics used by management in operating our business.

These non-GAAP financial measures are presented solely for information and comparative purposes and should not be regarded as a replacement for the corresponding GAAP measures. These reconciliations can be found in the supplemental info section of our Investor Relations website and in Exhibit B of today's press release which is available in the Investor Relations section of our website.

The content of this conference call contains time-sensitive information that is accurate only as of the date of the live broadcast, November 5, 2019. Henry Schein undertakes no obligation to revise or update any forward-looking statements to reflect events or circumstances after the date of this call. Please limit yourself to a single question and a follow-up during Q&A to allow as many listeners as possible to ask a question within the one hour we have allotted for this call.

With that said, I would like to turn the call over to Stanley Bergman.

Stanley Bergman

Thank you Carolynne. Good morning everyone and thank you for joining us. We are pleased that we reported solid third quarter financial results with increases in diluted EPS from continuing operations of 54.2% on a GAAP basis and 15.4% on a non-GAAP basis. We continue to make progress in growing organically with a focus on sales of higher-margin products while making strategic investments to supplement growth in the years ahead. Today, we are tightening our guidance range for 2019 non-GAAP EPS from continuing operations, which reflects growth of 8% to 9% compared to 2018 results.

Steven will discuss this in greater detail in a moment but note that we continue to believe that global dental and medical markets that we serve are growing. We are executing well on our 2018 to 2020 strategic plan, especially in the slow-growing U.S. dental consumable market. As we progress with our strategic plan, we are confident that we are well positioned to gain further market share in all our businesses, leading to increased EPS.

We are particularly pleased this quarter with the performance in our international businesses as well as our dental specialties, technology and value-added services and U.S. medical businesses.

As you listen to our call today and of course read our filings, I hope that our investors appreciate that we are making solid progress in driving the composition of our operating margin towards higher margin products, including our specialty brands, suppliers who value the services we provide and of course efficiencies in the business. While we are investing heavily in additional value-added services and digital signal technology, both in our distribution, manufacturing and Henry Schein One businesses as well as human capital, our number one assets and of course continue to advance satisfying and in fact, exceeding the needs of our customers in environments where all businesses are faced with increased expectations by customers.

So I hope that I believe we provided the information needed for our investors to come to the conclusion that I just outlined. So at this time, I will hand the call over to Steven to review our financial results and guidance and then I will provide some additional commentary on our recent business performance and accomplishments as well as a number of other matters. Thank you. Steven?

Steven Paladino

Okay. Thank you Stanley and good morning to all. As we begin, I would like to point out that I will be discussing our results from continuing operations as reported on a GAAP basis and also on a non-GAAP basis.

Our Q3 2019 and Q3 2018 non-GAAP results exclude certain costs that are detailed in Exhibit B of today's press release and in the supplemental information section of our Investor Relations website. Please note that as with the first half of the year, we have again included a corporate sales category for Q3 that represents sales to Covetrus under the transition services agreement. There product related TSAs are currently scheduled to run through August 2020.

It should also be noted that in October 2019, we sold our minority equity interest in Hu-Friedy, a manufacturer of dental instruments and infection prevention solutions. This minority investment sale will result in a significant fourth quarter gain in 2019. However, at this time, we are still quantifying the exact amount of the gain due to certain contingent consideration included in the transaction. I will also note that this investment was a non-controlling investment and we were not involved in running the business. We also had no representation on the company's Board of Directors. This was a financial investment. We have had an excellent relationship over many years with Hu-Friedy as one of their key distribute distribution partners, in particular helping them build share in the international markets.

So now turning to our Q3 results. Net sales from continuing operations for the quarter ended September 28, 2019, were $2.5 billion, reflecting a 6.5% increase compared with the third quarter of 2018, with internally generated sales growth in local currencies of 3.9%. When excluding the sales to Covetrus under the TSA, internal sales growth in local currencies was 3.0%. The details of our sales growth are contained in Exhibit A of our earnings press release that was issued earlier this morning.

On a GAAP basis, operating margin for the third quarter of 2019 was 7.5% and increased 223 basis points compared with the third quarter of 2018. On a non-GAAP basis, which excludes restructuring costs in both periods and also excludes the litigation settlement expense in the prior year, our operating margin was 7.4% and increased 20 basis points on a year-over-year basis, mainly due to lower expenses as a percentage of sales. Of that 20 basis point increase in operating margin, acquisitions contributed 12 basis points. You can find a reconciliation of GAAP operating margin to non-GAAP operating margin in the supplemental info page on the Investor Relations page of our website.

Turning to taxes. Our reported GAAP effective tax rate for the third quarter of 2019 was 23.5%. This compares with 15.7% GAAP effective tax rate for the third quarter of 2018. However, on non-GAAP basis, our effective tax rate was 23% and 0.5% and this compares with the prior year non-GAAP effective tax rate of 22.5% in the same period last year. Again, look at the supplemental info page on the Investor Relations page of our website for a reconciliation of GAAP to non-GAAP taxes. We estimate that our full year effective tax rate will be in the 24% range, both on a GAAP and non-GAAP basis.

Moving on, net income from continuing operations attributable to Henry Schein, Inc. for Q3 of 2019 was $134.9 million or $0.91 per diluted share. And this compares with the prior-year GAAP net income from continuing operations of $90.8 million or $0.59 per share. Third quarter 2019 results include a pretax reduction in the estimated restructuring cost that we previously have accrued of about $800,000 or $0.01 per diluted share. Again, those restructuring cost were originally accrued in earlier period and this was a small change in estimate for those costs. Excluding the reduction in restructuring cost, non-GAAP net income from continuing operations for the third quarter of 2019 was $134.3 million or $0.90 per diluted share and this compares with non-GAAP net income from continuing operations of $120 million or $0.78 per diluted share for the third quarter of 2018. This represents growth of 12% and 15.4%, respectively.

If we are looking at provide some additional detail on our results from continuing operations, it's important to note that amortization from acquired intangible assets for Q3 2019 was $29.5 million pretax or $0.15 per diluted share. This compares with $19 million pretax or $0.09 per diluted share for the same period last year. For the first nine months of the year, the amortization was $79.6 million pretax or $0.40 per diluted share and that compares to the nine months of $56.2 million pretax or $0.20 per diluted share in the same period last year. I will also note, in Q3 of this year, foreign exchange currency negatively impacted our diluted EPS by approximately 1% for the quarter.

Let me now provide some detail on the sales results for the quarter. Our dental sales were $1.5 billion, an increase of 2.1% compared with the prior year with internal growth in local currencies of 1.7%. North American internal sales in local currencies was down 0.2% and included 1.2% growth in sales of dental consumable merchandise. This growth was primarily driven by strong sales of dental specialty products and is also against a difficult comparison in the prior year as internal sales growth for dental consumables last year was 4.3%.

Our dental equipment sales and service revenues included internal sales that decreased 4.5% in local currencies. That's partially related to deferral of sales orders in anticipation of the Dentsply Sirona World sales event which was held in October this year and was held in Q3 last year. That contributed to a decline in high-tech equipment sales. This decline was mostly driven by lower CAD/CAM sales because of that selling event. I will also note that our current dental equipment backlog is very solid.

International dental internal sales growth in local currencies was 5.0%. This included 4.1% growth in sales of dental consumable merchandise. Our growth in international consumable merchandise sales was driven by broad-based sales growth across Europe and other international markets, including strong dental specialty sales in our international markets. The international dental equipment sales and service revenue internal growth in local currencies was 7.9%, including very strong CAD/CAM sales. Note that our change in our business model in Brazil had very little impact on the international dental equipment sales in the current quarter.

Medical sales were $804 million in the third quarter, an increase of 11.3% with internally generated sales growth in local currencies of 5.3%. The 5.3% internal growth in local currencies was the same number in both North America and internationally. Our medical sales results once again are driven by both solid organic growth along with a contribution of acquisitions sales growth from North American Rescue acquisition. We believe our medical group is well-positioned with large group practices, independent physician offices and alternate sites of care with strong customer relationships in each category contributing to our growth.

Our technology and value-added services sales from continuing operations were $137 million in the third quarter, an increase of 15.1% with internally generated sales growth in local currencies of 4.9%. In North America, technology internal sales growth in local currencies was 4.5% on an as reported basis. Our technology sales in Q3 2019 were bolstered by a billing related to the U.S. Department of Defense contract which was approximately $9 million in the current quarter and that compares to $6.3 million in the same period last year. This was partially offset by lower financial services revenue related to the lower dental equipment sales we experienced in the third quarter. Internationally, technology and value-added services internal sales growth increased by 7.35% in local currencies.

We continued to repurchase common stock in the open market during the third quarter buying 1.6 million shares at an average price of $62.48 for a total of approximately $98 million. The impact of the repurchase of shares on our third quarter diluted EPS was immaterial. Also note, on October 31, 2019, we announced that our Board of Directors authorized the repurchase of up to $400 million of shares and that's on top of the $75 million that we have available at the end of the quarter. So in total, we have $475 million available for future stock repurchases.

Let's take a brief look at some of the highlights of our cash flow. We had strong operating cash flow from continuing operations for the quarter. It was $226.4 million and that compared to $157.5 million in the third quarter of last year. We continue to believe we will have strong operating cash flow for the year. We also note that we plan on implementing a new restructuring initiative in 2020. The goal of that initiative is two-fold. One is to help mitigate stranded cost from some of the expiring transitional services agreements related to the Animal Health Spin-off as well as to continue to look for more opportunities to save costs and drive operating efficiencies. At this time, we do not have specific details on this initiative since they are in process of being developed but we will provide additional details on future earnings calls.

I will conclude my remarks by noting that we are tightening our guidance range for 2019 non-GAAP diluted EPS. At this time, we are not providing GAAP guidance as we are unable to provide an accurate estimate of the gain on the minority equity investment tat we just talked about that. That will be recorded in the fourth quarter. Again, this gain is subject to certain contingent consideration related to the transaction, which makes calculating it a little bit more difficult. This guidance supersedes both our GAAP and non-GAAP guidance previously issued.

Our 2019 non-GAAP diluted EPS from continuing operations attributable to Henry Schein, Inc. is now expected to be in the range of $3.41 to $3.47, reflecting growth of 8% to 9% compared with the 2018 non-GAAP diluted EPS from continuing operations which was $3.17. The outlook for 2019 non-GAAP diluted EPS from continuing operations excludes $0.08 of estimated restructuring expenses and $0.01 credit to income tax expense related to the Animal Health Spin-off. Non-GAAP guidance also excludes the gain on sales of minority equity investment which will be recorded in Q4 and also our non-GAAP diluted

EPS from continuing operations for 2018 exclude certain expenses and benefits, netting to a charge of $0.37 per diluted share and you could see that as reflected on our previous earnings releases for 2018.

Turning to 2020. We are introducing non-GAAP diluted EPS for 2020. At this time, again, we will not be providing GAAP diluted EPS as we are unable to provide an accurate estimate of costs related to the restructuring that I mentioned earlier. 2020 non-GAAP diluted EPS from continuing operations attributable to Henry Schein is expected to be in the range of $3.65 to $3.75 and that reflects growth of 6% to 9% compared with the midpoint of our 2019 non-GAAP diluted EPS from continuing operations, which was $3.44.

Our guidance for both 2019 and 2020 GAAP and non-GAAP diluted EPS attributable to Henry Schein, Inc. is for current operations as well as any completed or previously announced acquisitions but does not include the impact of potential future acquisitions, if any, or the restructuring expenses. Guidance assumes foreign exchange rates are generally consistent with current levels. And the guidance also assumes that end markets remain stable and are consistent with current market conditions.

I will also note that our guidance assumes certain continued IT investment in three areas. One is CRM. The second is European ERP. And the third is our web interface development. We will continue to make investments in those three areas in 2020.

With that said, I would like to now turn the call back over to Stanley.

Stanley Bergman

Thank you Steven. Let's begin with a review of our third quarter dental business highlights. During the quarter, the North American dental consumable merchandise internal sales grew by 1.2% in local currencies as we reported earlier on. As Steven mentioned, this despite a difficult comparison to the third quarter last year when we reported growth of more than 4%. In the third quarter, we believe Henry Schein grew slightly faster than the end markets.

Internationally, dental consumables internal sales in local currencies grew 4.1%. This was also faster than our estimates for the end market growth driven by broad-based sales across the entire business, in part driven by strong dental specialty sales as well. And the third quarter internal sales of global dental specialty products increased 9.3% in local currencies and we did particularly well in the areas of implants and bone regeneration products and endodontic products of our own brands.

In dental equipment, internal sales in the third quarter in North America declined 4.5% in local currencies, primarily related to decline in high-tech equipment revenue. Traditional equipment sales grew at a healthy rate of 4.8%. We are particularly pleased with our performance on the equipment sales in general.

As you may know, one of our large dental manufacturing partners, Dentsply Sirona, there was a key sales event early in the fourth quarter and we believe a portion of practices in the U.S. held off on equipment purchases in anticipation of show promotions. Last year, this event was in the third quarter of 2018. This was an excellent sales event for Henry Schein, particularly for sales of high tech equipment and specifically CAD/CAM and extraoral imaging products.

More than twice as many of our dental customers attended the Dentsply Sirona World compared to last year and we believe the strong participation should translate into incremental dental equipment sales for Henry Schein in the fourth quarter and beyond that even. As Steven mentioned, our current dental equipment backlog suggests improved fourth quarter dental equipment sales.

International dental equipment internal sales had a robust growth of 8% in local currencies in the third quarter. This was particularly encouraging given the economies in certain of the markets that we operate showing that dentists are prepared to invest in their practices when the investment results in improved profitability of the practice, while at the same time providing better quality care for the patients that the practitioner is treating. We know that investing in new dental equipment and digital technology can transform a dental practice through enhanced capabilities, greater efficiency and increased patient satisfaction. We look forward to working with strategic supplier partners to build mutual market share for those manufacturers who continue to innovate and address practice opportunities and challenges and who understand and appreciate the value that Henry Schein can bring to those manufacturers who are bringing their products to market.

We continue to see opportunities to advance interoperability between Henry Schein One and equipment manufactures. This is really important. A key part of the strategy of Henry Schein One is to integrate specifically digital dental equipment into the electronic medical record and from there also advance better quality of care and patient demand generation. Over time, we believe that key demographic trends including among the aging population in the developed world and expanding middle class in the developing world as well as greater awareness of the link between oral care and oral health will all drive dental market growth. And specifically with certain products and specifically in the specialty products and digital dentistry.

We have built our portfolio of solutions around helping dental professionals manage more efficient practices, enabling our customers to improve the overall health and well-being of their patients, help to educate patients about the oral systemic connection. The connection between good oral care and good health care in general. There is a huge amount of data that has been published in the last decade specifically in the last few years connecting the notion of good oral care with good health care in general.

We believe education will invigorate the dental practice with new wellness services and reinforce the value of prevention and regular oral care as with general population understands that wellness and prevention lead to a better life, a quality of life, and, of course, lower cost of healthcare in general. The requirements have moved from sick care to health care, which is a good segue into our medical business, which is focused in the ultimate care section of medicine with a high focus on wellness and prevention.

We delivered solid internal growth in the third quarter of 5.3% in local currencies. Our medical team has built a reputation for excellence in serving small and large scale physician practices with a goal of enhancing patient care. We have made many investments in our solutions and systems to optimize what oftentimes are highly complicated supply chain systems. The needs of the office-based practitioner of the ultimate care sites are quite unique and we believe we satisfy these customers in a rather unique way.

Our goal is to think ahead of an evolving medical landscape to best support patient focus care across the sub-acute spectrum. And in this connection, we continue to invest in technology to support these customers' unique needs. A great example of our forward thinking is our announcement several months ago of the availability of Medpod MobileDoc 2, integrated with Uber Health. This platform is designed to enable health care practitioners to conduct remote telemedicine examinations for patients in nontraditional care settings, such as homes, offices and schools.

We provide the vital signs monitoring equipment in the vehicle so that the practitioner is able to read and gauge the vital signs of the patients in the field. We are helping to seek practices transform and improve relationships with patients looking for convenient access to care, a key requirement of the younger generation. As we invest in our teams, systems and product offerings, we believe we will remain a trusted valued partner to small physician practices, large group medical practice, specialties practices, general practices and urgent care and ambulatory care centers as they promote increased wellness and prevention for their patients while at the same time servicing the ambulatory surgical center in a rather unique way.

Now let's move to our technology and value-added services business. Henry Schein continues to evolve as a provider, as a service provider shall we say, as well as a resource for unmatched selection of products and services. Henry Schein One is an important strategic asset, not only in the day-to-day management of practices, but also to drive both existing and prospective patients into our customer's practices. Over the years, we have successfully expanded our services beyond our world-class distribution platform and practice management software into building a model to help practitioners better engage with and market their practices to patients and serve these practices more efficiently and effectively. In other words, positioning our customers to provide better healthcare, providing better tools to provide better healthcare while bringing that to the attention of the public and their patients in general.

The Henry Schein One platform exemplifies our service-oriented solutions and last quarter, we delivered several new functional enhancements. In practice management, we introduced electronic forms of consents as well as new practice workflow tools. In patient engagement and patient acquisitions, we launched an expressed chick-in solution as well as a powerful new full appointment to allow practices book open appointment slots to help dentists manage practices and maintain a full schedule and prioritize the procedures in conformity with the practitioners' needs. We also offer online appointment booking through Dentrix Ascend. This is our successful cloud-based system and soon through Dentrix, our traditional Windows-based system, allowing patients to book appointments on their practice website as well as through links in emails and text appointment reminders. We have a significant text reminder business around the world and actually quite uniquely in our international markets.

I mentioned last quarter that we are looking for new opportunities to cross sell our software solutions with practitioners who purchase our consumable merchandise and equipment. Our Henry Schein One and Henry Schein dental teams are increasingly engaged and working collaboratively to support our customers across our business. Although it's barely a year old, we continue to believe that Henry Schein One represents a significant opportunity over the short, medium and long term and we expect to continue to enhance our product offering.

Before we open the call to questions, I would like to comment on two important developments related to litigation. First, with regard to the recent decision by the FTC, we are gratified that the Chief Administrative Law Judge dismissed claims that Henry Schein conspired with competitors to avoid providing discounts to buying groups representing dental practitioners which we publicly denied from the start and are happy to do business with dentists in any form, have been committed to doing that for decades.

Secondly, we announced that in the case of opioid litigation involving Summit County, Ohio, presently before the U.S. District Court for the Northern District of Ohio, the plaintiff has agreed to dismiss Henry Schein with prejudice as a defendant. The opioid crisis is a terrible national tragedy and we believe that all segments of society must come together to address this crisis. Even before this litigation, we have played a constructive role and look forward to continue to play a constructive role in helping to advance solutions that put an end to the tragic opioid addiction crisis.

As such, Henry Schein will make $1 million donation to establish an educational foundation in Summit County to develop best practices regarding the proper use of prescription opioids. We believe this will in the end be a benefit to practitioners in dental and medical and society in general. Working with Summit County, we will make the donation to a Pain Management Education Foundation dedicated to making grants supporting and aggregating research around best practices for pain management, including the prescription of opioids and alternatives, educating dentists, physicians, clinical associates, patients and patient networks on those best practices along with the risks of opioid addictions and alternative pain management treatment, opioid options for key indications.

Henry Schein will also pay $250,000 of Summit County expenses. Henry Schein has a long-standing commitment to doing well by doing good and operating our business in an ethical manner wherever we might operate throughout the world. Team Schein looks forward to continuing to serve all our customers and suppliers with excellence and integrity that is expected from us and at the same time serving the needs of our investors and indeed society in general.

With that, operator, we look forward to opening the call for questions.

Question-and-Answer Session

Operator

[Operator Instructions]. Our first question is going to come from the line of Glen Santangelo, Guggenheim.

Glen Santangelo

Hi. Yes. Thanks for taking my question. I just wanted to comment on underlying market growth rate trends in the North American dental business. It looks this quarter that the consumable business obviously was facing a difficult 4%-plus comp last year and the equipment business was obviously impacted by the timing of the Dentsply event. But as we look to the balance of the year, have you seen any change in those underlying trends in either of those two businesses? And where would you sort of peg the growth rates at for each?

Stanley Bergman

Yes. Glen, I think it's hard to be precise within basis points. I mean they are in a very narrow trading range. But if you kind of look at on the consumable side, what we did in 2018, what we did in 2019, you divide by two, it's something like that. Maybe a little lower, maybe a little higher but it's some deflation, not a lot. The unit growth is about stable in general, quite well with pretty good growth in the specialty areas and the number of procedures. So on balance, it's very hard to be precise.

On equipment, the market is quite healthy and we often caution investors not to look at one or two quarters but to take a look at a 12-month, four quarter, something like that. This quarter was a particularly unusual quarter. We actually had very good traditional equipment sales. One or two vendors did well. One or two vendors were somewhat challenged. We had some challenges with the CAD/CAM and the extraoral imaging products. But in that regard, a lot of that is related to a particular supplier, Dentsply who held a convention in the third quarter and we have reported that we have a pretty solid backlog of equipment going into the fourth quarter.

So I think it's very, very hard to be precise within basis points. But generally, I think these markets are positive with equipment being quite good. I am not saying we were surprised with the positive developments on the traditional equipment side, but I think that's an indication that practitioners are prepared to invest in their practice and by the way, this is not only in the United States but in Europe also. With the surprisingly challenging economy in most of our major markets, we have done quite well. And I think we did pick up market share. But the bottom line is practitioners are investing in their practices.

Glen Santangelo

I appreciate the comments, Stan. Steve, maybe if I could just follow-up on the initial fiscal 2020 guide. I was kind of just curious, are you assuming any trend changes in any of those underlying markets? I know you specifically did not include any capital deployment in your guidance and you sort of called out the IT investments. I just wonder if you could maybe size that? And any sort of high level commentary to help us think about that initial guidance would be helpful. Thanks.

Steven Paladino

Sure. So the 2020 guidance assumes that market conditions are pretty much consistent with what we are currently experiencing. So we are still expecting U.S. consumable merchandise growth to be modest. We are expecting a little bit of pickup on overall equipment. Again, we think Q3 was negatively impacted by, again, the Dentsply Sirona World sales event. But we do have a little bit of headwinds in a couple of areas.

One is in stranded costs. Stranded cost in 2020 are expected to be greater than 2019. Right now, we are estimating that they could be at the high-end of the range, could be $10 million to $12 million. But we are working very diligently on reducing those stranded costs. But there is still more work to be done to see how far we can reduce them. But again, right now, the estimate is in the $10 million to $12 million range.

And there were also increased investments in the technology investments. We are not quantifying exactly how much that is, but certainly it's in the millions of dollars range of increased IT investments. Part of that is going to be ongoing because some of those IT investments are not a one-year event. They are multiple year events. So I think the step-up is in 2020. And hopefully they won't as significant a step-up in future years.

We also assume from the effective tax rate, that the tax rate will be approximately equal to or slightly less than what we currently are experiencing. So at the 24% range or slightly below 24%. And we are assuming a little bit, not the full amount, a little bit of stock buyback in our guidance. We are not assuming the full amount that was authorized since it's difficult to predict exactly how much we will buyback in any given year.

Operator

Our next question will come from the line of Jon Block, Stifel.

Jon Block

Great. Thanks guys. Good morning. Nice quarter. I am actually going to start with the specialty consumable number. Stan, I thought you gave a number around 9% or even over 9%. That's a big number. So was that predominantly or all driven by implants? Are there any incremental revenues coming from some of your other initiatives like I guess what I am alluding to would be clear aligners and do you that high single digit number from specialty can be maintained as we look forward?

Stanley Bergman

Thanks. Jon, that's a very good question. I think we have outlined to Wall Street on many occasions that our goal is, of course, to continue to make our distribution business a core business more efficient, continue to grow market share, satisfy the complexities of our customers, they are growing, some of them, even the small customers have great demand today for our value-added services. But we have two key programs, well three key initiatives to mitigate margin compression.

The first is specialty products. I will cover that in a minute. The second is value-added services. And the third is expense mitigation, in other words, driving efficiency in the practice business. A slight bonus in that, a challenge in that, because we had the Covetrus -- sorry.

Steven Paladino

TSA sales.

Stanley Bergman

TSA sales and the stranded costs that we have to deal with. But now if you go into specialty businesses, we have a relatively small market share. And what we have shown to be successful is to combine the specialty products, the niche products with the general merchandise and equipment we sell and bundle that with the practice management software where we have leading positions in several of the specialty areas. So yes, we believe we can continue to grow our specialty product businesses in the niche products as well as the general consumables and equipment and software.

Returning to the niche products. We believe we have a small market share, relatively small market share, in implants and bone regeneration. Yet, these are important positions. We have great platform. We have very good know-how. We have excellent facilities. The management is really superb. And we believe we can continue. Now I cannot guarantee. Of course, no one can that we will have double digit growth in implants and bone regeneration products going forward.

And at the same time, I think we have a relatively small position in the worldwide endodontic market. We certainly work with certain branded manufacturers and hope to continue to do that. But we also have our own brand products that are doing quite well and have also returned somewhere around double digit growth. Orthodontics is a bit more challenging, shall we say. We have a very small business in wires and brackets. I think there is an opportunity there. We have some unique products and we are doing well with the unique products. That market is not growing significantly, although it's probably somewhere between stable and a slight decrease.

On the aligner side, I think we have a good product. We have had a soft launch. I think the product actually works and is pretty good. I wouldn't want to make claims on this call but I am told by our KOLs that it's a very good product. And we are sharpening the related software for those areas to support the aligner, the various kinds of software to support the aligner and really believe we have a very good solution for the GPs in particular because there is actually no reason to go to a direct to consumer company if you can get a great product, a really outstanding product provided by clinician at a slightly higher price, not much higher.

So we believe we will do well eventually over time with the GPs and I believe the specialists are starting to appreciate our offering, which is a little bit different to any of the market offerings out there. And we are not really looking to be a generic compared to anyone out there. We are looking to create our own demand for our own products in the specialty area.

So yes, we do remain quite optimistic about the specialties areas and who knows exactly. It's not possible to predict. But we believe that a greater part of Henry Schein's profits over the next few years, at least the next three, four, five, seven years will come from these specialty products under our brand as well as working with certain branded manufacturers who are increasing their demand, their sales of certain specialty products.

Jon Block

Great. Fantastic color. Thanks for that. And with the second question, I will just pivot over to the medical business. The 5% change in total was still well above industry. But the two-year stack was about 10%, the past tow years in 2017 and 2018, the two years stacks were a lot closer to midteens. So should we just think about the rate of your market share gain is starting to diminish a bit? And maybe that mid single digit plus type of number for medical is the better neighborhood to be in? Thanks for your time, guys.

Stanley Bergman

Yes. Glen, I think we have mentioned this before with respect to medical. You can't judge one particular quarter. First, I think we will continue to invest in additional businesses in the medical field to expand our offering. So that will bring us acquisition growth, but that offering will also bring us internal growth. NAR, for example, is a very nice product offering. We have got acquisition growth but it will result in internal growth.

One also has to be careful in looking at any one quarter. There are so many variables. You take flu, for example. One year, there is a demand for flu test. The other year there is not. One year, a flu vaccine is delivered in the third quarter. One year, it's delivered in the fourth quarter. So I think what's important here is to look at our business over a three, four quarter basis and again, we don't have a crystal ball but we are pretty comfortable that we are positioned to deal with the service, the transfer of procedures from the acute care setting to the office-based or the surgery center environments or even the urgent center environment and to gain further market share in that area.

And those are reasonably fast growing markets and we are quite comfortable in that. We have got a really outstanding management team there too. They are investing in software, unique software for those markets. And so with the acquisitions, we will expect to have greater internal growth, acquisition growth and continue to gain market share in a he market that is growing. So it's hard to gauge one quarter at a time and hard to talk about whether it is going to be double digit growth or not, but it is going to be a decent market growth and sales growth and will continue to add to our profitability in combination with all the other strategies we just outlined.

Operator

Our next question will come from the line of Jeff Johnson, Baird.

Jeff Johnson

Thank you. Good morning guys. Stanley, I want to follow up on a comment you made earlier about the dental equipment business and looking at it over more than a single quarter. If I look over the last 12 months, it seems like your North American dental equipment revenue is kind of flat, maybe even down a little bit from the 12 month period prior to that. So if I take that longer term view, what has been the change in cadence of equipment demand or selling on your part over the last few quarters relative to maybe a year or two ago where we were?

Stanley Bergman

Yes. Jeff, it's a very good question. I am glad you asked it. So in the quarters after we added CEREC, in particular Sirona, but CEREC in particular, we had a significant bulge in pent-up demand that we satisfied. That initial demand bulge has kind of faded out. But at the same time, we are starting to gain, I think, market share within that category from customers that we are introducing the CEREC and related lines to. So I think that's number one.

Number two is and I think we have mentioned in the past, there has been quite a bit of deflation with certain 2-D and 3-D imaging equipment, not units. I am pretty sure, I can't say for sure, but that market has now stabilized. And actually, I believe that as manufacturers come out with unique technology or improve on their offering, the price is likely to go up. So taking those two into account and looking at an aggregation of the average of, say, four quarters, I think we are in positive territory. And I do believe that practitioners are investing in their practices here and abroad and that technology can help practitioners operate a more efficient practice, increase the profitability of the practice while providing better clinical care. And yes, there is also a little bit price compression on scanners, sensors, but overall I think this is a very good market and I believe that we continue to gain market share in all the markets we are in.

Jeff Johnson

Great. That's helpful. And Steve, maybe as a follow-up, just on 2020 guidance, 6% to 9% EPS growth. It would imply, I am assuming anyway, a little bit of leverage in the model in addition to maybe some repo and other helpers below the revenue line as well. But I guess what I am trying to get or hoping you can provide some color on is, how should we think about margin gating next year? I know you don't guide on margin, but if there is some leverage to be had in the model, we have got business mix as an issue, ERP investments, restructuring. Is it going to be mainly come through OpEx where that margin can go up next year a bit and we should think about gross margins closer to how we have may be seen it here in the current quarter?

Steven Paladino

Yes. Let me provide some color. So first, when you look at our Q3 reported gross margin, it's down 33 basis points. But when you exclude the very low margin sales to Covetrus under the TSAs, it's only down about nine basis points. So that's why we are providing that level of detail, Jeff, on the TSA sales so people can look at our margins with and without the Covetrus. So really, all of our margin expansion in the current quarter is coming from leveraging expenses and getting lower expenses as a percentage of sales. I think that we would expect that to continue in 2020. But I would caution that we are not expecting the full 20 basis points or more in 2020 of operating margin expansion because of some of the things we just talked about, stranded cost and other things. We do believe that longer term, we can get back to that type of margin expansion but right now in 2020, we really don't expect that we expect a more modest operating margin expansion. And that's why we are looking to do more restructuring in 2020 because it will help us accelerate eliminating or mitigating those stranded costs as well as taking more cost out of the system to help offset some of the slight gross margin decline.

Jeff Johnson

Very helpful. Thanks guys.

Operator

Our next question will come from the line of Courtney Owens, William Blair.

Courtney Owens

Hi guys. So my first question is on Henry Schein One. So it appears to still be driving meaningful growth and experiencing good customer uptick. I guess, from your vantage point, what do guys really think differentiate the product at this point and given kind of feedback from customers thus far from other competitor's offering? Thanks.

Stanley Bergman

Well, it's very hard to do this on a telephone call and this is an area where investors are interested and I really would investors would be interested. The best thing would be to attend a briefing at one of the dental shows where we can show the product. But clearly, we had a very unique cloud-based system that is based on Ascend, that is based on Dentrix, the leading Windows-based system which is richer with features, I believe, that there is no other system that has all these features.

The system is, also both those systems, together with the three, actually four specialty software systems that we have for ortho, endo and oral surgery and the unique systems we have that service dental schools. I think 90%-plus of dental schools use our software, the military, a large DSO, all of these unique needs of these customers, in one way or another, are satisfied by the software.

In addition, we have quite unique electronic medical record software that is interoperable with many suppliers, not all suppliers yet because some supplies are still having challenges developing a software to connect. But most of, many of the leading suppliers are interoperable with us already in the areas of imaging and to some extent of digital prosthetics.

And then you move into the various kinds of digital exchange of information, whether it's credit card processing, patient financing and a big area where we, I think, have a quite an important market share is in various forms of demand generation, including risk mitigation software, website management design, it is a large offering in an area that I think is highly factionalized from a competitive point of view.

I am not sure if there is any one competitor that has anywhere near the aggregation of opportunities that we present dentists with. And that is, of course, not only in the U.S., which is what I just covered but also in international markets where we have different software covering most of what I just described.

Steven Paladino

Let me just add, Courtney, that on the Henry Schein website, the Investor Relations section of our website, we hosted a webinar for certain investors that were looking for more information on Henry Schein One and that webinar is still up on the website. So people can view that. It gives a lot of great detail on what these services and solutions are. And so I would invite investors who are really interested to take a look at it and if you have follow-up questions, call us and we will be happy to answer those questions. We could also, if people want more detail on it, we could also set something up separately for a group of investors it that's what's wanted.

The other thing I just want to add to what Stanley said is, I would say that no one has, it was kind of at the end of Stanley's remarks, I just don't want to lose it, no competitor has the breadth and level of services that we have. Some people may just have a cloud-based system. Other people may have patient engagement tools. But we really have all of the tools under one roof and they all connect with each other very seamlessly. Some of the new products are still being connected better. But I think that really differentiates us that we really can go to customers and all of their technology services and solutions can be provided by Henry Schein One.

Operator

And we have time for one final question. Our last question for today will come from the line of Nathan Rich, Goldman Sachs of Nathan Rich, Goldman Sachs.

Nathan Rich

Great. Thanks. Two quick ones, if I could. Steve, first on the updated 2019 guidance, it implies a 4Q EPS number that's roughly flat sequentially. I think in 4Q, you usually see a bit of a sequential growth just with it being a higher volume quarter and you also have the DS World shift this year. So could you maybe just talk about what's driving your expectations there as we think about the cadence for 4Q?

Steven Paladino

Yes. I would say that Q4 is impacted, Q3, let me say it this way. Q3 had a significant amount of favorable timing things that happens in Q3 that will not repeat in Q4. So let me give some more details to that. So one is this Department of Defense contract that happened in Q3. We were expecting it to happen in Q4. Two is, there is little bit higher stranded cost in Q4 versus Q3. Three, we did restructuring last year in Q4 of 2018 and we won't have that same year-over-year benefit in 2019 because we are not doing restructuring in Q3 and Q4. So there is a little bit of foreign exchange headwind. So there is a number of items but I would characterize it all as largely timing between Q3 and Q4. And that's why we maintained other than tightening the range for just one quarter left in the year, we basically maintained our full year guidance.

Nathan Rich

Okay. Great. That makes sense. And then just lastly, Steve, as we kind of look out to 2020, are there any large kind of customer renewals especially on the dental side that we should have in mind? And maybe more broadly, just can you maybe talk about what you are seeing from these customers in terms of purchasing behavior and have you been able to kind of penetrate those customers, especially products? And what's driving some of the strength in the specialty businesses that you guys cited earlier?

Steven Paladino

Sure. So again, we have elected not to put out press releases and publicly talk about every time we renew or win a contract with large DSOs. But I will say that even in 2019, we renewed a couple of contracts. So we are happy with that. There is really not big activity expected in 2020 for renewals or things like that. So that should not be anything that we are concerned about. We are looking to add customers in the DSO side. So I would say that our belief is that could be next year, slightly more upside than downside. Of course, when we are working with these large DSOs on renewals, we always have to sharpen our pencil a little bit on pricing but that's expected. And I would just conclude by saying that I think our service and relationships with these large DSOs is really superb and I don't think that people want to move for very small modest financial gains because it's difficult to switch and again there is risk that service levels from others won't be as strong as ours. So we feel we are in good shape and we feel that we will continue to have a very strong market position on DSOs going forward. But there is always renewals each year that are coming up. Again 2019 included at least two renewals that I am aware of.

Stanley Bergman

And we do continue to add new accounts, both in the large account area and the midsize practices.

Operator

Thank you. I would now like to turn the call back over to Stanley Bergman for any final remarks.

Stanley Bergman

Thank you operator. As we close today's call, I would like to underscore that we believe we are executing well on our growth initiatives as our strategy and value proposition continue to resonate with our customers. It is not a strategy that came together quickly. It's a strategy, a deliberate strategy that we have been executing on for the last three strategic plans, each a three-year plan and we are half, almost two-thirds of the way through 2018, 2019 and 2020 plan. We will shortly start preparing the plan for 2021, 2022, 2023.

Yesterday marked the 2fourth anniversary of our IPO. On a compound annual growth basis through the end of 2018, we grew sales by 13% and non-GAAP EPS from continuing operations by 14%. We have also provided a return on investment of 13% on a compound annual growth basis.

If you have any further questions, please contact Carolynne Borders and Investor Relations at 631-390-8105. We believe that we are well positioned, as I noted, for the future. We have a good track record, I believe an outstanding management team with a deep bench, 19,000 committed Team Schein members around the world and we look forward very much to the future.

We will be at the Credit Suisse Healthcare Conference in Phoenix and at the Greater New York Dental Show, both in November. For our investors in Europe, we hope to see you at the NASDAQ Investor Conference in London in early December. So there will be ample opportunity to meet our executives in the field. But if you have any questions, please feel free to call Carolynne with specific questions or actually visit our website. So thank you for joining us today and look forward to speaking to you on the next call. Thank you.

Operator

Thank you. That will conclude today's Henry Schein conference call. We appreciate your participation and ask that you please disconnect.