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IDEXX Laboratories, Inc.'s (IDXX) CEO Jay Mazelsky on Q3 2019 Results - Earnings Call Transcript

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Q3: 10-31-19 Earnings Summary

Press Release SEC *10-Q*

EPS of $1.24 beats by $0.10 | Revenue of $605.3M (10.97% Y/Y) beats by $8.21M

Earning Call Audio

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IDEXX Laboratories, Inc. (NASDAQ:IDXX) Q3 2019 Results Earnings Conference Call October 31, 2019 8:30 AM ET

Company Participants

Jay Mazelsky - President and CEO

Brian McKeon - Chief Financial Officer

John Ravis - Senior Director, Investor Relations

Conference Call Participants

Michael Ryskin - Bank of America

Ryan Daniels - William Blair

Erin Wright - Credit Suisse

Nathan Rich - Goldman Sachs

David Westenberg - Guggenheim Securities

Jon Block - Stifel, Nicolaus & Co., Inc.

Mark Massaro - Canaccord

Operator

Good morning. And welcome to the IDEXX Laboratories Third Quarter 2019 Earnings Conference Call. As a reminder, today's conference is being recorded. Participating in the call this morning are Jay Mazelsky, President and Chief Executive Officer; Brian McKeon, Chief Financial Officer; and John Ravis, Senior Director, Investor Relations.

IDEXX would like to preface the discussion today with a caution regarding forward-looking statements. Listeners are reminded that our discussion during the call will include forward-looking statements that are subject to risks and uncertainties, that could cause actual results to differ materially from those discussed today.

Additional information regarding these risks and uncertainties is available under the forward-looking statements notice in our press release issued this morning, as well as in our periodic filings with the Securities and Exchange Commission, which can be obtained from the SEC or by visiting the Investor Relations section of our website, idexx.com.

During this call, we will be discussing certain financial measures not prepared in accordance with Generally Accepted Accounting Principles or GAAP. A reconciliation of these non-GAAP financial measures to the most directly comparable GAAP measures is provided in our earnings release, which may also be found by visiting the Investor Relations section of our website.

In reviewing our second quarter 2019 results, please note, all references to growth, organic growth, constant currency growth and comparable constant currency growth, refer to growth compared to the equivalent period in 2018 unless otherwise noted.

To allow broad participation in the Q&A, we ask that each participant limit his or her questions to one with one follow-up as necessary. We appreciate you may have additional questions, so please feel free to get back into the queue and if time permits we will take your additional questions.

I would now like to turn the call over to, Brian McKeon.

Brian McKeon

Good morning, everyone. And thanks for joining us on our third quarter earnings call. Today I will take you through our quarterly results and our updated outlook for the full year 2019. I will also provide an overview of our preliminary for 2020. Jay, will follow with his comments.

IDEXX delivered continued strong revenue and profit gains in Q3. In terms of highlights, revenues of $605 million grew 11% as reported and 12% organically, including over 1% of growth rate benefit from equivalent days.

CAG Diagnostic recurring revenues increased 14% organically, including nearly 2% of equivalent day growth rate benefit, reflecting double-digit gains across U.S. and international markets.

EPS of $1.24 per share increased 21% on a comparable constant currency basis, benefiting from better than expected organic revenue growth, which supported 130-basis-point improvement in constant currency operating margins.

Excellent operating results are keeping us on track towards strong full year financial performance. In terms of our 2019 revenue outlook, we are refining our full year guidance to $2,395 billion to $2405 billion, a $5 million increase million increase at midpoint, incorporating our strong Q3 performance. This reflects an updated full year organic growth of 10% to 10.5% overall and 11.5% to 12%, for CAG Diagnostic recurring revenues, both at the higher end of our previous guidance range.

We are adjusting our 2019 EPS guidance to $4.72 to $4.78 or 15% to 16% growth on a comparable constant comparable constant currency basis. This is $0.12 per share lower than our prior guidance midpoint incorporating $0.18 per share in projected Q4 charges related to our recently announced CEO transition. Adjusting for this impact, our outlook is $0.06 per share higher at midpoint and corporate benefits from our strong third quarter operating performance and lower projections for full year net interest costs.

In terms of our preliminary 2020 outlook, we are projecting revenue of $2,610 billion to $2,650 billion, reflecting organic revenue growth of 9% to 10.5%, supported by sustained high growth in CAG Diagnostic recurring revenues. Our 2020 EPS outlook is $5.30 per share to $5.46 per share or comparable constant currency EPS growth of 17% to 20%.

As we will discuss our 2020 EPS outlook incorporates $0.11 per share in projected headwinds, from year-over-year FX impacts and expectations for approximately $0.12 per share and reduced tax benefits from share-based compensation activity.

Let's begin with a review of our Q3 revenue growth performance by segment. Excellent third quarter revenue growth results were driven by continued strong momentum in our Companion Animal Group. Global CAG revenues increased 13% organically, reflecting 14% organic gains in CAG Diagnostic recurring revenues, including nearly 2% growth benefit from equivalent days in quarter.

By region, U.S. CAG Diagnostic recurring revenues increased 13% organically, including nearly 2% of growth rate benefit from equivalent days, reflecting continued strong gains in consumables and Reference Labs.

U.S. CAG recurring diagnostic growth remains primarily volume driven with net price gains continuing to trend in the 2% to 3% range. We also maintained consistent exceptionally high levels of customer retention across modalities. IDEXX U.S. CAG Diagnostic recurring revenue growth continues to outpace broader market trends, which improved in the quarter.

In Q3, total visits per practice growth was 1.4% year-on-year with clinical visits per practice growing at 2.7% and overall revenue per practice increasing 5.3%, reflecting continued solid growth trends in the U.S. Companion Animal Healthcare market.

International CAG Diagnostic recurring revenue increased 16% organically in Q3, including approximately 1.5% of equivalent day growth benefit. International consumable revenue gains normalized for approximately 2.5% of benefits from equivalent days sustained at approximately 20% and international organic revenue Reference Lab growth improved to high single-digit rates.

Globally Reference Lab and consulting service revenues grew 12% organically in Q3, supported by consistent low to mid-teen volume-driven gains in the U.S. Robust U.S. lab growth continues to be driven by strong same-store sales growth at IDEXX customers, augmented by net customer acquisition benefits and moderate net price gains.

As Jay will discuss in October we closed on the acquisition of Marshfield Laboratories, a national service provider based in Wisconsin adding to our U.S. market capabilities.

Global consumable revenues increased 18% organically in Q3, including nearly 3% of equivalent day growth benefits. These results reflected strong growth across U.S. and international markets driven by increases in diagnostic test utilization and expansion of our installed instrument base.

We had an outstanding quarter in terms of high quality instrument placements, supporting double-digit year-on-year in our Economic Value Index or EVI. Overall, premium instrument placements increased 14% year-on-year, driven by 18% year-on-year growth in catalyst placements, which supported an 18% year-on-year increase in our global catalyst installed base.

Globally we placed 1,898 catalysts in the quarter with 360 yet new and competitive accounts in North America and 910 new and competitive placements in international markets. We also achieved 965 premium hematology placements globally up 18% and 589 SediVue placements, in line with strong prior year levels.

Please note that, we have expanded the data shared in our quarterly earnings snapshot available on our Investor Relations website, to include premium instrument placements by category and region, as well as quarterly tracking of our global premium installed base.

Rapid assay revenues grew 10% organically in Q3, including nearly 3% of equivalent day growth day growth benefits, reflecting continued expansion of 4Dx plus, specialty, SNAP feline [ph] and first generation products.

Growth in high customer retention in our rapid assay business continues to benefit from expansion of our engaged SNAP Pro installed base, supported by an additional 2,683 SNAP Pro placements globally in Q3, bringing our global installed base to over 34,000.

Veterinary software services and diagnostic imaging systems revenues increased 6% organically in Q3, driven by continued strong gains in VSS recurring service revenues. Overall, segment revenue gains were constrained in Q3 by comparisons to very strong prior year digital system placement levels.

In terms of our other business segment performance in the quarter, Water business revenues grew 7% organically, supported by continued solid growth across U.S. and international markets. Livestock poultry and Livestock poultry and dairy revenue, increased nearly 10% organically. Third quarter results were driven by strong year-on-year gains in Asia-Pacific markets, which benefited from a favorable prior year comparison.

The prolonged outbreak of African swine fever continues to negatively impact the swine population in China. However, demand for new diagnostic testing programs and increased diagnostic testing for alternative poultry food sources, offset lower recurring swine testing volume levels in Q3. Health herd screening levels while down from strong prior year levels were also relatively higher than expected in the quarter.

Turning to the P&L, operating profit in Q3 increased 19%, as reported and on a constant currency basis, driven by solid profit gains across our CAG, Water and LPD segments. Operating margins increased 130 basis points on a constant currency basis, reflected solid gross margin gains and operating expense leverage on high revenue growth.

Gross profit increased 13% as reported, or 14% on a constant currency basis, in Q3. Gross margins increased 60 basis points on a constant currency basis, supported by mix benefits from strong consumable revenue growth, lab productivity gains and moderate net price increases.

Foreign exchange hedge gains, which are reflected in gross profit were approximately $3 in Q3 and approximately $7 million year-to-date.

Operating expenses in Q3 increased 9% as reported, and 10% on a constant currency basis, resulting in 70 basis points of constant currency operating margin leverage. Operating expense increases were driven by growth in R&D spending and increased costs related to our expanded global CAG commercial capability.

EPS in Q3 was $1.24 per share, including benefits of including benefits of $4 million or $0.05 per share, related to share-based compensation activity, which was approximately $0.03 per share higher than projected. On a comparable constant currency basis, EPS increased 21%. Foreign exchange net of favorable year-on-year hedge impacts had an immaterial impact on operating profit and EPS in the quarter.

Year-to-date free cash flow through the third quarter was $195 million. We continue to expect free cash flow of 60% to 65% of net income for 2019. This reflects a consistent outlook for full year capital spending of $160 million to $175 million, including approximately $70 million of combined incremental spending related to our Westbrook main headquarter expansion and our German core lab relocation.

Our strong cash flow generation supported the allocation of $91 million in capital towards the repurchase of 330,000 shares in the quarter. We have maintained a strong balance sheet with leverage ratios as a multiple of adjusted EBITDA of 1.39 times gross and 1.24 times net of cash at the end of the quarter.

We continue to maintain a 2019 full year outlook for reduction in average shares outstanding from stock repurchases of approximately 1%, which assumes that we maintain net leverage at similar multiples of EBITDA. We now project annual net interest expense of $3.5 million, an improvement of $2.5 million compared to our previous guidance.

In terms of our updated P&L outlook for 2019, as noted, we are refining our full year reported revenue guidance to $2,395 billion to $2,405 billion, reflecting an organic growth outlook of 10% to 10.5% and CAG recurring diagnostic organic revenue growth of 11.5% to 12%, both at the higher end of our prior guidance range. At midpoint, this reflects a $5 million reported revenue increase factoring in our strong third quarter performance.

In this updated outlook, modest projected benefits from our recently completed U.S. lab acquisition are offset by refined projections for FX impacts. For the full-year, we now expect a 2% headwind from FX and revenue growth.

In terms of EPS, we are lowering our 2019 full year guidance by $0.12 per share at midpoint to $4.72 per share to $4.78 per share incorporating $0.18 of impact related to the CEO transition. These results in comparable constant currency growth of 15% to 16% for 2019 including approximately 4% of growth impacts related to projected Q4 transition charges.

Costs related to the separation agreement will lower full year 2019 operating profit by an estimated $13.4 million and year-on-year operating margin improvement by approximately 55 basis points. Incorporating this impact, our updated outlook is for 55 basis points to 70 basis points in full-year constant currency operating margin improvement or 110 basis points to 125 basis points of improvement excluding the Q4 transition charge impact, which is consistent with the higher end of our prior guidance range.

Our full year operating margin outlook includes expectations for higher levels of year-on-year operating expense growth in Q4, including effects from the advancement of an additional expansion of our U.S. commercial field resources, which Jay will discuss in his comments.

Strong full year operating margin performance excluding transition charge impacts and benefits from lower projected interest costs yield approximately $0.06 per share in full year operational EPS benefit compared to previous guidance.

Our updated EPS guidance assumes a 2019 effective tax rate of approximately 20%, including approximately 1% of impact related to CEO transition costs. This tax rate also includes an updated estimate of $15 million or approximately 3% in full year projected tax rate benefit from exercise of share-based compensation, netting approximately $0.02 of upside compared to previous guidance. At the midpoint of our guidance estimates, this equates to about 17% per share and full year share-based compensation tax benefit.

Operational share-based compensation tax benefit upsides are mitigated by $0.02 per share of negative impact related to the strengthening of the U.S. dollar since our last conference call. Our 2019 EPS guidance now assumes $0.06 in negative full year impact related to FX charges net of hedge impacts and for the full year 2019, we are projecting hedge gains of $11.5 million.

As we look at 2020, we are targeting continued strong revenue and profit growth consistent with our long-term goals. Our preliminary revenue outlook is $2,610 billion to $2,650 billion, reflecting expectations for 9% to 10.5% organic revenue gains, supported by sustained high growth in CAG Diagnostic recurring revenues.

Our guidance reflects expectations for overall reported revenue growth of 9% to 10.5% with an estimated 0.5% foreign exchange headwind, related to the recent strengthening of the U.S. dollar, offset by year-on-year benefits from completed 2019 acquisitions.

Our preliminary 2020 EPS guidance of $5.30 per share to $5.46 per share incorporates expectations for operating margin improvement of 100 basis points to 150 basis points on a constant currency basis, including approximately 50 basis points of year-on-year improvement, related to lapping the Q4 2019 charges related to the CEO transition.

At rates assumed in our press release, we estimate that FX will decrease reported operating margins by approximately 30 basis points and EPS by approximately $0.11 per share, net of established hedge positions, which we estimate will result in $6 of net pre-tax gains in 2020.

Our projected 2020 effective tax rate is 21% to 22%. This outlook assumes $3 million to $5 million or approximately $0.05 per share in share-based compensation tax benefits, assuming our current share price. Note that our projections for share-based compensation tax benefits share price, incorporates timing of future option expirations.

As IDEXX transitioned from seven year to 10-year option lives in 2013, this has the effect of lowering the level of options scheduled to expire in 2020, contributing to a $0.12 reduced projected tax benefit in 2020 compared to 2019. For 2020, we are projecting a 1% reduction in shares outstanding related to share repurchases, at assumed consistent net leverage ratios and net interest expense next year of $36 million.

Adjusting for changes in currency and share-based compensation tax benefits, this 2020 EPS outlook equates to a projected 17% to 20%, comparable constant currency growth rate. We look forward to providing an update and more detailed review of our 2020 guidance in our year end conference call.

That concludes our financial review. I will now turn the discussion over to Jay.

Jay Mazelsky

Good morning, and thank you, Brian. IDEXX's third quarter results reflected solid growth, across our Companion Animal, Livestock and Water Diagnostic businesses, an outstanding achievement by our IDEXX team globally. High growth in CAG Diagnostic revenues continues to lead our performance, with attractive flow through benefits to profit, keeping us on us on track to deliver strong full year operating results. Excellent commercial execution is a key theme in our continued growth momentum and enhancing capability in this area consistently delivers a high return on investment.

In our U.S. CAG business we benefit from the increased IDEXX engagement with customers, in an underdeveloped diagnostics market, with solid growth momentum, as evidenced by the 2.7% growth in same-store clinical visits seen in the quarter.

Our U.S. commercial team remains highly productive, delivering 13% CAG Diagnostics recurring organic revenue growth in the U.S., including approximately 2% benefit from equivalent business days. Execution was excellent across the Board, resulting in both impressive revenue gains from all modalities and sustained high customer retention rates.

Increased customer engagement is helping to drive sustained, low to mid-teens organic growth in Reference Labs, led by same-store testing expansion and double-digit organic gains and consumable revenues, supported by our expanding premium instrument installed base.

Instrument placements were excellent in the quarter, led by 14% year-on-year growth in U.S. new and competitive catalyst placements. This supported a 10% year-on-year expansion of our U.S. catalyst installed base and double-digit growth in U.S. EVI.

SNAP Pro placements were also robust in Q3 with over 2,200 placed in the U.S., up 77% year-over-year. SNAP Pro bring significant workflow electronic medical record and charge capture benefits that complement our differentiated rapid assay point-of-care diagnostics. Importantly, customers who are connected to SNAP Pro are highly engaged and stay with us longer.

Our U.S. commercial team continues to make excellent progress in advancing our preventive care initiative. In Q3, we enrolled 330 new practices, bringing our total enrollees since program launched to nearly 3,500, almost two-thirds of our VDCs had at least one new customer enrollee in the quarter.

As discussed at Investor Day, a key commercial goal is to inspire customers to increase the use of medically relevant blood work and clinical visits. When we consider blood work as a representative proxy for diagnostics utilization, it was included in only about 8% of clinical wellness visits in 2018.

The increased rate of diagnostics testing with blood work and practices post enrollment in our preventive care program is notable, specifically if we take our 2017 preventive care enrollees who have now been in the program for over a year, the average annual increase in a percentage of wellness is that include blood work is approximately 1% per year since 2016.

This compares to approximately 20 to 30 basis points of annual increase for non-enrollees. These convincing early success indicators reinforce the 1% to 2% contribution to annual CAG Diagnostics recurring revenue growth potential we see from this initiative.

Our strong growth in the U.S. demonstrates that diagnostics as a category continues to grow in importance and relevance to the veterinary profession. Our customers are in turn asking our category experts to spend more time partnering with them.

The combination of increasing customer engagement and key growth initiatives like IDEXX Preventive Care, strong operating results and commercial momentum and a healthy product pipeline gives us confidence to once again expand our commercial presence in the U.S.

We are already underway with an 8% expansion in our U.S. field based professionals, which we expect to be largely in place by the beginning of Q1 2020. As with our past field expansions, these are thoughtfully planned and supported by detailed regional analytical modeling that considers a number of factors including territory size and specific geographic differences such as traffic patterns and population growth.

The most important factor is the market opportunity, as calculated by our ability to grow our installed base, expand diagnostic testing and expand category share across in-clinic and Reference Lab modalities.

While we have said this before it bears repeating. The data continues to prove out that the more time we spend with customers, the more they grow with IDEXX. This expansion will bring us to an estimated 530 field-based professionals in the U.S., up from 490 at the end of 2018. We are very excited by the opportunity this expansion affords us heading into 2020.

The category of diagnostics is increasing in importance on a global basis as well. And as a result, we are seeing the benefits from our recently completed CAG commercial expansion in international markets.

We saw 16% international CAG Diagnostics recurring revenue organic growth in Q3 including approximately 0.5 equivalent business days growth benefit. These gains were again led by international consumables growth of approximately 20% organically, normalized for equivalent business base and supported by continued expansion of our catalyst installed base, which increased 26% year-over-year.

Our international Reference Lab, showed improvement year-over-year, high single-digit growth, benefiting from the completed commercial expansion, strong commercial execution, as well as focus on customer service and IDEXX 360 programs that are increasingly multi-modal in character.

The IDEXX 360 program is gaining traction, with our international customers, supporting excellent instrument placements and double-digit growth in EVI, benefiting from a 28% year-on-year increase in placements, the new and competitive accounts internationally.

In addition to excellent commercial execution, the ongoing adoption and expansion of IDEXX differentiator’s one of our industry-leading investments and innovation, is a second key theme, supporting our strong growth performance.

Our strong reference lab growth in markets like U.S. for example, continues to be supported by high-growth in parasitology, driven by growing adoption of our proprietary fecal antigen test. In the U.S. approximately 60% of parasitology panels run in our reference lab included, PCDX antigen in the third quarter, up from approximately 50% in Q3 2018.

Our performance leading 4Dx plus franchise also continues to expand. In the U.S. in addition to sustained solid growth in clinic, we are seeing high levels of incremental growth in 4Dx plus testing in our Reference Labs, following engagement with our preventive care programs.

As we have highlighted in the past, only approximately 36% of dogs in the U.S., received a vector-borne disease test to some kind, while only approximately 15% of dogs in the U.S. receive a full vector-borne multi-analyte test. This expansion of 4Dx plus usage is a very encouraging sign, with additional long-term benefits for vector-borne disease testing.

We also continue to make excellent progress advancing SDMA as an essential element of the chemistry panel, which our reference lab customers have benefited from since 2015 and launch to our catalyst installed base in early 2018. We now have over 70% of catalyst customers globally, who have purchased Catalyst SDMA, while almost 60% have used it. This has translated into a total of 2.9 million run since its introduction on a slide.

We are also very excited about the new SDMA based chronic kidney disease staging guidelines that were issued in September by the international renal interest society. This is an expert panel of internationally renowned nephrologist, who establish evidence-based clinical practice guidelines for the evaluation and management of chronic kidney disease.

The full incorporation of SDMA into CKD staging guidelines reflects the widespread recognition that SDMA is an accurate measure of kidney function. The impairment of which may be due to kidney disease or other disease processes.

These updated SDMA base staging guidelines, are the next step in improving not only early diagnosis of CKD, but also tailoring treatment to individual patients. IDEXX SDMA has transformed the landscape of how veterinarians manage patients with impaired kidney function.

Finally, we continue to extend our capability and advantages in veterinary software, by advancing our software on multiple fronts simultaneously. Our goal is to provide a truly comprehensive technology offering that both independent practices and corporate groups around the world rely on to run their businesses.

Q3 was again a strong quarter for global placements of new Cornerstone, Neo, Adamana and Smart Flow Systems. Inclusion of software systems, on the IDEXX 360 program is accelerating commercial efforts in North America. In the U.S. practice management software placements grew 35% year-over-year.

Sticking with the U.S., we have seen it in a precedented pace of Cornerstone upgrades, the version 9.1 with more than 2,700 practices upgraded year-to-date across North America, driven by customer demand for the all new user interface and streamlined clinician experience.

We achieved yet another clinical development milestone for Cornerstone Cloud in Q3, which is now successfully running in a live environment for more a quarter. Initial customer feedback is extremely positive and we look forward to eventually making the many benefits of the cloud available to the thousands of customers that value Cornerstone as the standard bearer in practice management software.

Q3 was another strong quarter for growth for Webex with a 29% year-over-year increase in subscriptions. Our enterprise management and analytics platform for corporate groups continues to make big strides, providing a command and control center for corporate group C-suite and VetConnect plus the most widely used app in veterinary medicine had another strong quarter, growing out new functionality for sharing diagnostic results with pet parents and growing to more than 29,000 engaged practices globally.

In addition to our strides in growing our business organically, we are also pleased to highlight our recent acquisition of Marshfield Labs and the addition of their employees. Marshfield is a highly professional well-run laboratory that has a national customer base with a relatively stronger presence in the mid and upper Midwest regions. We look forward to quickly bringing our unique innovations like SDMA, Fecal Antigen and VetConnect PLUS to name just a few the Marshfield customers many of whom we work with today.

In summary, we feel very good about our business progress across a range of strategic fronts and believe we are well-positioned to build on this momentum in 2020 and deliver on our long-term financial goals.

Before I conclude and on behalf of all my IDEXX colleagues around the world, I'd like to extend our thanks to John Ravis and our best wishes for John's continued rehabilitation. John's love and affection as a preparative translated into his deeply held beliefs on the unique role that pets in their care play in our lives.

As a result, he always reminded us of what's possible and what IDEXX could contribute through our unique diagnostics and software that expand the health and wellbeing of the pets we love. It's a John's vision that IDEXX as an organization will remain committed to helping strengthen the role and relevance of the veterinarian as the key to improvement the lives of pets and animals and the people who love them. On a personal note, I am looking forward to continuing to work with John both on the Board of Directors and as a trusted adviser.

And with that, we will open it up to Q&A.

Question-and-Answer Session

Operator

[Operator Instructions] We will go to the line of Michael Ryskin with Bank of America. Please go ahead.

Michael Ryskin

Hey, guys. How you are doing?

Jay Mazelsky

Good morning, Mike.

Brian McKeon

Good morning, Mike.

Michael Ryskin

First off congrats on the quarter really solid results in Q3, but I want to ask on the 2020 outlook briefly. First on the operating margin gains, you highlighted a couple of different moving pieces with the CEO charge in the fourth quarter. But you have also seen some really strong gains in gross margins this year. How should we think about the moving pieces in the progression extra you talked about 100 bps to 150 bps operating margin constant currency? How do we think about price on the gross margin line some of the cost controls in SG&A? You also have the sales force expansion that you talked about in the U.S. So a couple of different moving pieces. So how does that all shake out? And then a follow-on just on the broader outlook for next year, slightly more conservative view for the top line organic $9 million to $10.5 million, I realize still very early on. But anything really changing in the market just high level or is this just any particular area you could point to within Reference Labs or consumables or instruments or is this just initial guide, I want to take a cautious glance at the markets?

Brian McKeon

Yeah. Let me start with the operating margin clarification. You are right. The -- we have a compare here with the CEO transition charge that we tried to highlight. So our preliminary outlook of 100 basis points to 150 basis points, we noted included 50 basis points related to the comparison or favorability related to the charge, so if you adjust for that. It’s 50 basis points to 100 basis points which is very consistent with our long-term goals and what we were indicating, what our goals were for 2020 back at Investor Day.

We are demonstrating that this is a leverageable business model that delivers a nice profit flow-through when we grow. At the rates we are targeting and have good progress with that as reflected in our Q3 results and our outlook for 2019.

I would highlight heading into next year we have a couple of factors that are built into the operating margin outlook. One is that, we have two significant new facilities that are coming online next year or new core lab in Germany, as well as our new Westbook headquarters. And we will -- that will involve a level of incremental costs and we will grow into that overtime. But initially that will be something that has the effect of moderating margin gains.

And as you pointed out, we have got the U.S. expansion, the additional expansion of U.S. commercial resources and we have a pretty healthy growth rate now in our year-on-year investment as we are fully ramped with our international expansion that we implemented a little earlier this year and we are investing in our R&D initiatives consistent with our stated goals. So we have got a healthy level of investment, some factors that will moderate kind of the upside on that. But we feel very comfortable with the underlying 50 basis points to 100 basis points of improvement outlook for next year.

On revenue the 9% to 10.5%, we noted, reflects a consistent outlook for sustaining continued strong CAG Dx recurring revenue growth which is really the main driver of our of our growth outlook. We are looking to build on the solid progress we have made on both the U.S. and international fronts on growing CAG Dx recurring revenues, which are right in line with our long-term goal ranges.

In terms of overall growth, I would highlight, we are continuing to maintain a calibrated outlook on LPD revenues. That is influenced by -- we still have some macro factors going on with African Swine fever and we are -- we didn’t know are going to be up again some tough compare on health for screening, which is a relatively smaller business for us, but we had much better-than-expected growth this year in that area and we are cautious about some potential pullback on that as dairy producers in places like Australia, New Zealand for rebuild their herds in 2020. So, it’s a smaller business for us, but at the margin that kind of reinforces to us our comfort levels with, the 9% to 10.5% overall organic growth outlook.

Jay Mazelsky

And Mike just in terms of the market itself we feel good about where the market is. As Brian indicated, we saw 2.7% clinical growth in Q3 over 5% revenue growth $5.3 million and that doesn’t include new practice formations. So our outlook assumes that the market stays in that range.

Michael Ryskin

Great. Thanks.

Operator

And we will go to the line of Ryan Daniels with William Blair. Please go ahead.

Ryan Daniels

Hey, guys. Thanks for taking the question. Jay, one for you in regards to Marshfield Labs. It's a little unique to see you purchasing lab assets, let alone in the U.S. So I am curious what the strategy was there, and then more specifically, outside of the lab network and the client base, you will get from that was there anything proprietary that can be broadened into the IDEXX labs existing network that you garner from the acquisition?

Jay Mazelsky

Yeah. Ryan, thank you for the question. We are very excited by the Marshfield acquisition. It's a high-quality, very professional laboratory, we are adding approximately 2,000 Marshfield customers. These -- some of which we already do business with.

Our focus is really on being able to maintain continuity of service, understand the needs of those customers better and introduce some of the innovations that we have like SDMA and fecal antigen and VetConnect PLUS over time to them. So it's a -- we think it's a great acquisition, it's a great laboratory and it fits in well with our overall strategy.

Ryan Daniels

Okay. And then I may have missed this, this is a different question, but in commenting on the 8% uptick in Q4 on the North American customer facing organization. Is there a specific focus of the hires you are making there, if it's VetTech, is it field sales reps, is it anything in particular that it's kind of a focus and will you be changing the territories at all or is it just on many existing territories? Thanks.

Jay Mazelsky

All right. Thank you, Ryan. Let me give you an overview of the model and I will give background on the why. Essentially, at its core, we are adding 23 territories and our model is we have a VDC per territory. So we will be going from 220 -- 227 territories to 250.

On average, the VDC today has about 110 accounts and post-implementation of the expansion will be down to about 100 and as is the case when we expand the number of VDCs, we augment the number of field service reps to support them, generally two VDCs per single FSR. So any addition to the 23 VDCs and new territories, we are adding 12 FSR. So that represents the core of the change.

And our thinking really is, when you take a look at our market. We have been growing strongly in the U.S. and the average business we do with the -- with our customers has grown. And so from both the depth and breadth standpoint, we have many customers that are 40%, 50% bigger in terms of the business they do with us just compared to three years ago.

Their expectation as they do more business with us is that they see more of us, whether it’s full staff trainings or understanding their practice better, identifying opportunities where we can help them. And then you layer on top of that initiatives like preventive care, which take relatively more time of the VDC upfront, including things like on-boarding and getting those customers calling Marshfield Labs that I mentioned and the couple thousand of new customers. There’s a real draw on the capacity of our commercial channel.

We tend to look -- there’s a couple of metrics that we look at, that sort of guide our thinking about this. One is a reach to revenue metrics, so if you take a look at Q3, we are about 90% reached the revenue, which is where, historically, we like to be. But when you take a look at reached a customer, which incorporates not just IDEXX customers, but competitive customers, we are about 75% or so. So we are a bit lower than we would like to be. We think there’s really good opportunity outside of the IDEXX installed base still. So that guided our thinking and how we implemented this.

Ryan Daniels

Okay. That’s super helpful. And I want to just wish my best to John as well. Thank you.

Jay Mazelsky

Thank you.

John Ravis

Thanks, Ryan.

Operator

And you have a question from the line of Erin Wright. Please go ahead.

Erin Wright

Great. Thanks. Do you know how much of the Marshfield customers are IDEXX customers on the point-of-care side or generally speaking, how much overlap, maybe there is, so we can think about like an opportunity for cross-selling and what does that put your U.S. lab count at now, following the Marshfield transaction? And then, can you kind of just broadly speak to the broader competitive environment across reference laboratory, are there any changes there? I know there have been some more competitive movements on the SDMA side or for kidney disease testing, I guess, how do you compare your SDMA capabilities at the reference lab compared to others? Thanks.

Jay Mazelsky

All right. So there's -- I will take a few of those. There are a number of questions in there. As I indicated, there's about 2,000 in total Marshfield customers, many of whom we do business with currently. We haven't broke out the specifics in terms of in what modality across all the modalities.

Generally speaking, most customers in the U.S. do business with us and in some fashion, whether it's rapid assay or our software products. So we do think that there's a really nice opportunity to cross-sell, our full solutions. But our focus is really first on being able to understand those customer needs and work with them.

In terms of, you had mentioned specifically competition to SDMA. In our view, there are really no comparable offerings, the SDMA in the marketplace. We continue to make excellent progress, expanding SDMA adoption is differentiated. I gave you some statistics in terms of not only the reference lab but SDMA on the slide, with our catalyst.

We are super excited by the updated guidelines of virus that Elevates SDMA, really from an adjunct or chronic care disease treatment into a primary recommended diagnostics biomarker. Alongside puratone, of course, for staging of CKD, an important thing to keep in mind, in terms of the staging guidelines is that, veterinarians rely on them to classify by the patient, severity and progression of kidney disease.

So this guides that the treatment paths that they take, it helps the market standardize on best care approaches for the patient. It drives -- we think more standardized or better outcomes for the marketplace as a whole. It assures the pet parents that their pets getting the best treatment. So we think this is a really big deal and that’s something we are excited by.

Erin Wright

Okay.

Brian McKeon

And Erin, we had 52 labs before -- in the U.S. before this and we will be adding a few additional locations, including the Core Lab for Marshfield, which we are as Jay mentioned it’s a really high quality operation.

Erin Wright

Okay. Great. And then, just generally speaking, also how would you characterize current demand trends across the veterinary market. I guess, you noted this slight acceleration in the clinical visit growth this quarter and what was driving that, you think, and is that normalized for the day impact as well? Thanks.

Jay Mazelsky

Yeah. The -- I mean, we think the market is healthy, it’s 2.7% clinical growth and that’s the important metric that we track, because it involves -- those visits involve diagnostics testing. The overall practice growth is $1.4 million in revenue at 5.3% was pretty healthy.

It's -- we think it's largely consistent with what we have seen in the past. It does tend to be some variability quarter-to-quarter. We have got a pretty good beat on the market as a result of the -- our analytics approach with 7,500 practices. We take data from five of the leading PIM systems. So we have got a nice proportional both regional and practicized representation in this data and I think what it's showing is pretty consistent, strong growth across the market.

Brian McKeon

Hey, Erin. Just on the days impact clarified. Basically, what we had in Q3 was an extra Monday. And so what that really impacted was our business, we do a lot of shipping on Monday so sees positive benefits to consumables and rapid assay, which we highlighted and actually very limited impact on labs, and it wouldn't have really impacting the market metrics in that context, it's more of a shipping dynamic.

Erin Wright

Got it. Thank you.

Operator

We will go to the line of Nathan Rich with Goldman Sachs. Please go ahead.

Nathan Rich

Thanks for the question. I wanted to follow-up on the revenue guidance, Brian. I didn't hear a range for your expectations for the CAG Diagnostic recurring growth next year. I just wanted to know if you could kind of talk about the type of growth you expect and kind of what the key factors we should have in mind that would influence on the growth outlook for next year?

Brian McKeon

Yeah. we -- in our preliminary guidance we don't get that granular. We did want to highlight that in the 9% to 10.5% outlook we are looking to sustain the high level of growth that, this year we are guiding to 11.5% to 12%.

So all indications are we are trending quite well and looking to build on that as in the U.S. right now we are about 11.5% adjusted for days year-to-date and kind of 13.5% in international and international actually improved a bit in the quarter. We had relatively better reference lab growth, which is something we have been working on.

So we are looking to build on that, and we will be sharing more specifics as we get through the finalization of our planning process and we will share that on the year-end call.

Nathan Rich

Placement numbers that you gave, it looks like you saw some nice improvement internationally specifically in new and competitive placements. Could you maybe just talk about what drove that and specifically what you are seeing in China, I think that had been a little bit of a drag earlier this year, I just wondered, if you had seen improvement there?

Jay Mazelsky

Yeah. So we saw really nice placement growth and consumables growth internationally, 20% normalized and I think if there is a couple of factors. It's clearly been an ongoing focus for us. I think the maturing of our VDC model, continuing maturing of our VDC model is helpful. We are getting nice traction with the IDEXX 360 program, with our international customer's, I think they appreciate what that brings in terms of flexibility in the ability to access our solutions.

And the products themselves, it fits our international markets really well, I think we have said in the past that Catalyst One was initially designed for international markets in terms of its cost profile and physical footprint and we just -- we continue to see that bit in our sales momentum and Brian's going to address the China question.

Brian McKeon

Yeah. China, we had a very good performance on new and competitive placements and we continue to work through the lapping of compares to prior levels where we had high levels of vet test upgrades. So the mix has shifted. We are -- that does constrain our overall revenue growth, reported revenue growth somewhat, but I think the underlying quality of the placements we are doing new and competitive accounts across regions, contributed very high quality performance from our lens in the quarter and the double-digit EVI gains that we talked about.

So, we feel good about the progress we are making across markets and that sets us up well. It’s really about expanding our global installed base, and as Jay highlighted, we are up 18% year-on-year with our catalyst installed base globally, and that really sets a solid foundation for continuing to grow our consumable revenues at high rates.

Operator

We will go to the line of David Westenberg. Please go ahead.

David Westenberg

Hey. Thanks. Hi. Thank you for taking the questions. So just first you noted customer shifting preferences to cloud based solutions. I know that PIMS has very high barriers and switching out seems it is rather on the difficult side. So are you having a lot of success in terms of switching customers or adding on that cloud -- the Cornerstone cloud solution, is that the way you kind of see the market shaking out? Can you just maybe run through competitive dynamics in that PIMS market, please?

Jay Mazelsky

Yeah. So I will take that. Thank you for the question, David. The -- our PIMS offering is very broad. So we address the market in the -- more of the advanced workflow with Cornerstone, but also those practices that may be single or mobile practices with NEO.

And what we see is our veterinary customers like all customers, whether independent of industry, you appreciate ease of use benefits, they specifically focus at workflow, does it help them address the challenges, both from a care delivery standpoint, as well as a business standpoint in the practice.

And what they are telling us with Cornerstone 9.1, which is our most recent revision, is that they really appreciate the improvements we have made in user interface and the ability to do the work that they do with fewer clicks, with just all the easiest benefits.

So we are seeing really nice placements across the Board. It's included, as I had mentioned, in our IDEXX 360 program, so more customers are deciding, choosing to go all in with us in terms of diagnostics and software, what they find is when they do that, it works better.

In terms of Cornerstone Cloud, that as I indicated, is really in field trials. At this point, we think the marketplace over time will migrate at least in part, as you had indicated. PIM systems tend to be a bit sticky, but I think customers increasingly recognize that there are some benefits that having their software in the cloud in terms of lower cost for being able to maintain the hardware in the practices.

And somewhat more quick or a number of revisions that they can expect on an ongoing basis without having to shutdown their practices for an hour, two hours, that type of thing. So lots of benefits, we think, over time, that the market will move in that direction, and we will be ready for it. Yeah, keep in mind, our NEO practice management system is already in the cloud.

David Westenberg

All right. Well, thank you very much for the color. I am just going to do one really quick housekeeping question. I really do appreciate how you call out the extra day in the quarter. So I was just wondering in terms of housekeeping. Is there an extra day or one less day then in Q4 that we need to be -- that we need to anticipate and then maybe as we look at 2020, is there any kind of growth headwind in terms of extra days there, just as a housekeeping question.

Brian McKeon

On Q4, we will have one less Monday, but we anticipate some positive benefit around the holiday week time link. So I think it's a modest net headwind. There may be some modality impacts, but we are not calling that out and the team is telling me what the next year is -- it's relative -- we get some benefit in Q1 for leap year, but I think on the full year, it's relatively neutral.

David Westenberg

Appreciate it. Thank you so much.

Brian McKeon

Yeah.

Operator

We go to the line of Jon Block. Please go ahead.

Jon Block

Great. Thanks guys. Good morning. Jay, maybe the first one for you, just curious about the increased North American sales force, I guess, why now, I think, it was a couple of quarters ago, you said, you guys are sort of good with your commercial infrastructure and I get it. It's a business that responds well to increased investments. But just curious what you are seeing in the marketplace that caused you to move now versus maybe in a couple of quarters and then I have got a follow-up.

Jay Mazelsky

Yeah. So Jon, I think, it really comes down to what I was describing earlier. A number of our customers, a large number of our customers in our territories have gotten bigger over time. And there's more demand from the VDC in terms of working with these customers. It's an expectation that they have as they use more broader and deeper.

And then when you take a look at some of these initiatives like preventive care, as I mentioned, they really do require more time upfront, in terms of getting these customers on-boarded and helping make them successful. You add in a couple of thousand more customers for Marshfield Labs.

As well as what we said at Investor Day, it's $11 billion addressable market, $3 billion in wellness business alone. So we continue to see that when we apply time with customers that they grow more and use more of our diagnostics and we do better. It really just comes down to that math.

Jon Block

Okay. Fair enough. And then Brian, maybe the second one for you on the guide, some moving parts on stock-based comp. I think largely in line, but the midpoint of revs was a tad below where we were. So I guess the question is, does this bake in what we may see from a new product standpoint in 2020, does it reflect that? And then part B that is just I thought you alluded to net interest expense of $36.5 million, which seems like a decent step-up year-over-year, despite rates continuing to go down. So I want to make sure I got the right number there and if so, why do we have a step-up? Thanks guys.

Brian McKeon

Yeah. Just on your first question, our outlook for 2020 incorporate projections for growth across the business including adoption of our current innovations and any new introductions. So that's factored in.

We feel it's very much in line with kind of how we have been trending. We always target growth, Jon, at the higher end of what we talk about, that's what we try to execute and just calibrate that appropriately. But we are looking to build on the strong growth rates and are very comfortable with the outlook in the context of our long-term goals.

And on your question related to interest expense, the -- it was $36 million and that included an assumption for -- we did not assume a change in interest rates. So I think that if there are reductions in things like variable interest rates we would there may be some modest benefit to that.

But that was our assumption and it assumes a flat net leverage ratio, so basically will -- we saw some benefit this year, reductions in interest rates, we are not projecting the underlying interest rate rejections into next year in the broader market.

Operator

Our final question will come from the line of Mark Massaro with Canaccord. Please go ahead.

Mark Massaro

Hey, guys. Thanks for the question. I guess, Brian, as we think about the 2020 guidance, I assume, you are contemplating the inclusion of Marshfield Labs. So it looks like Marshfield has about three or four Reference Labs, with particular strength in Wisconsin, Minnesota, Michigan, Ohio. One is, can you give us a sense of what your share was for Reference Lab in those regions and how you think that might bump it up? And then can you give us a sense for what level of growth you think that Marshfield could add in basis points to your reference lab line in 2020?

Brian McKeon

Yeah. So just on Marshfield, it's a lab with national customers. So we see this as adding to our national capability. Within our guidance, Mark, it is roughly $15 million, the annualized revenue we expect is about $15 million from Marshfield, that's what's baked in and it's offset by FX. So in terms of when you see our reported organic numbers those two factors offset.

So I would say, we have got that factored in. We are very excited about adding Marshfield to the IDEXX family and working with their employees and very pleased with their capabilities. And as Jay mentioned, I think there's real opportunities for us here nationally to leverage our innovations and expand our IDEXX business with those customers.

Mark Massaro

That's excellent. And so I also wanted to ask about potential expansion internationally. I believe you have over 900 people on the field globally, which is certainly a significant global infrastructure. But can you give us a sense for where you are at internationally and whether or not you are contemplating future sales hires OUS? And I guess, related to that, you have got the new lab in Germany opening up next year. Can you just speak to some of the dynamics in play both competitively and organically internally focused in Europe for 2020?

Jay Mazelsky

Yeah. So we are -- we just completed our expansion in Europe and internationally, and we are comfortable where we are. We think we have the right capacity to address the opportunity and our growth projections. So at this point, there's no additional plans to go beyond that.

It's really -- our focus at this point is really maturing out the organization. What we find is that it takes time to continue to develop deeper relationships with customers and with those deeper relationships where we are able to grow, so that's really the focus.

In terms of the Reference Lab marketplace, as Brian indicated earlier we are pleased with where we are right now. We are focused on being able to improve our reference lab performance and we think, over time, with the IDEXX 360 program and the maturing of our VDC sales organization, we can build on that. We are excited to be able to bring on the new Reference Lab in Germany, we think that, that positions us well additional capacity in the future but no other specifics at this point.

Jay Mazelsky

Okay. And okay -- so thank you. With that, we will conclude the call. I want to thank our employees for the very strong progress and performance in Q3 and the advancement of our purpose, which is enhancing the health and well-being of pets, people and livestock around the world.

Operator

And ladies and gentlemen, that does conclude our conference for today. Thank you for using AT&T Teleconference Service. You may now disconnect.