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Interview – K2M achieves scale, but seeks further expansion

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The medtech sector has seen some unusually large IPOs recently, and at £132m that of the spinal implant company K2M was one of the largest. Often in medtech a flotation is a distant second choice to a buyout, but in K2M's case an IPO was always part of the plan, Eric Major, the firm's chief executive, tells *EP Vantage*.

"We entered the public markets to build the business as well as to raise capital, and to provide more flexibility to the organisation. It will allow us to compete with the larger companies," Mr Major says. But with the orthopaedics space in a state of flux as players seek to understand the ramifications of the Zimmer-Biomet merger, it will take time to see how the newly public K2M will fit into an altered environment.

Climbing the mountain

K2M develops implants to treat complex spinal pathologies including scoliosis, deformity, trauma and tumour. It is pouring particular effort into minimally invasive technologies to decrease surgical trauma and speed recovery.

The firm will use the $120m it expects to gain after expenses to pay off its debts and – unusually – to pay dividends on its series A and B convertible stock. The rest will go to building the business, including pushing into new markets, Mr Major says.

K2M had initially planned to raise $100m by floating around 5.8 million shares priced between $16 and $18 apiece, whereas its eventual $132m haul came through offering more shares at a lower price (*Medtech convulsed by IPO frenzy, May 8, 2014*).

"This point was the right time for us to raise capital, and we felt like this was the amount that we could not only raise, but made sense for us," says Mr Major. "The final range was dictated by interest during the process. It made the most sense at the time, in terms of where the market was."

A private equity company, Welsh, Carson, Anderson & Stowe, has had a controlling interest in K2M since 2010, and such a backer would usually be expected to prefer a buyout. Mr Major insists that this is not the case here. "This is really a milestone event, it's not to do with liquidity. Our private equity partner did not take capital out – it really was to allow us to keep building a strong business."

That said, Mr Major does concede that the company could end up being bought out. "That's always a possibility – we continue to see mergers and acquisitions across medtech. But I think K2 is in a position where we have enough scale now to be a viable competitor in the marketplace.

"What we have to stay focused on is becoming the leader in this space by offering differentiated and really disruptive technology. We're at the right size now."

If the company is not an immediate takeover target, perhaps it might become an acquirer itself. Historically, the group has been "very much an organic innovator", Mr Major says, paying tribute to K2M's engineers and designers. This allows it to deliver five to eight new products or line extensions each year, he says, and it intends to maintain that rate of launches in the near future.

But this organic strength does not mean smaller buys are out of the question. "[A company] that fits our strategy and has a technology that drops into our plan to deliver minimally invasive technology for the complex spine [is possible]," Mr Major says. "We're going to stay focused on our organic plan and we're going to leave our options – the ability to look for new technologies – open."

New markets

After paying its creditors and existing shareholders, K2M will use remaining cash to increase its reach. "The capital allows us to penetrate into new markets. We're in 29 countries now, and it enables us to go deeper into those markets – and to expand globally," Mr Major says.

“In many of the markets we’re in, we’re still early,” he says, adding that, while the company intends to build on recent product approvals in Japan and continue to grow its European operations, in the future it will explore opportunities in countries such as Brazil and China.

The lure of emerging markets is well attested, but the familiar US and European orthopaedics markets are undergoing transitions from which ortho companies could profit. “We’re seeing a global change in the market. In the US, the Affordable Care Act is going to affect business. We are watching the increased access to spinal technologies in particular, and broader medtech technologies, around the world.”

But the looming megamerger will change this space further – assuming the $13.4bn deal gets the blessing of the antitrust authorities (*Zimmer and Biomet hook up for second orthopaedics megamerger, April 24, 2014*). Mr Major will not be drawn on what the deal might mean for the orthopaedics sector, though in fairness Zimmer and Biomet are active in a different segment.

“I think it’s going to have a big impact in the recon hip and knee world, and a big impact in Warsaw [Indiana], where the two companies are headquartered,” Mr Major says. “We are looking forward to watching it and finding out how it gets projected through the marketplace.”

In this, Mr Major will not be alone.

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