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MDRX - Q3 2019 Allscripts Healthcare Solutions Inc Earnings Call

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OVERVIEW:

Co. reported 3Q19 GAAP revenue of $444m, GAAP loss per share of $0.03 and non-GAAP EPS = $0.17. Expects 2019 GAAP EPS to be $0.67-0.70. Expects 4Q19 non-GAAP revenue to be $460-470m and GAAP EPS to be $0.17-0.20.

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PRESENTATION

Operator

Greetings, and welcome to Allscripts' Third Quarter 2019 Earnings Conference Call. (Operator Instructions) As a reminder, this conference is being recorded.

It is now my pleasure to turn the conference over to your host, Stephen Shulstein, Vice President, Investor Relations. Thank you. You may begin.

Stephen M. Shulstein - *Allscripts Healthcare Solutions, Inc. - VP of IR*

Thank you very much. Good afternoon, and welcome to the Allscripts Third Quarter 2019 Earnings Conference Call. Our speakers today are Paul Black, Allscripts' Chief Executive Officer; Rick Poulton, our President; and Dennis Olis, our Chief Financial Officer.

We'll be making a number of forward-looking statements during the presentation and the Q&A part of the call. These statements are based on current expectations and involve a number of risks and uncertainties that can cause our actual results to vary materially. We undertake no obligation to revise these forward-looking statements in light of new information or future events. Please refer to our earnings release and SEC filings for more detailed description of the risk factors that may affect our results. Please reference the GAAP and non-GAAP financial statements as well as the non-GAAP tables in our earnings release and the supplemental workbook that are both available on our Investor Relations website.

And with that, I'm going to hand the call over to Rick Poulton.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Okay. Thanks, Stephen. Good afternoon, everybody. Thanks for joining our call today. As always, we appreciate both your time and your interest in Allscripts. In order to allow more time for the questions that are on your mind, we'll keep our prepared remarks shorter than we traditionally have on these calls.

So let me briefly summarize our operational performance. We reported a strong third quarter with bookings of $236 million. This was up 19% from last year's third quarter, and we are also up 19% on a year-to-date basis. The sales momentum was broad-based and balanced across our inpatient, outpatient and Veradigm franchises. Equally important, our pipeline of new deals remain strong heading into the fourth quarter, and we remain comfortable with our bookings guidance for 2019, which, as you will recall, we increased during last quarter.

In the inpatient market, we had a very strong quarter, and we saw strength across both the Sunrise and Paragon customer bases. We saw significant scope expansions at several clients and a good number of clients electing to take upgrades as well. Both of these are core solid leading indicators of their commitment to Allscripts.

But perhaps the biggest news we had in the quarter is the progress we made with our largest client, Northwell. As previewed on this call last quarter, we've been negotiating some long-term extensions of our existing business with them as well as talking to them about expanding our relationship into an exciting new area. I'm happy to report that we completed the extension of our Sunrise platform at Northwell through 2027. This renewal follows the extension of the TouchWorks agreement that we signed with them last year, and we are close to securing the extension of the last significant piece of business that we have with them, which is our managed services contract, and this should be finalized by the end of this year.

In addition, we announced that we entered into a joint development agreement with Northwell to develop and commercialize the next-generation EHR. We plan to codevelop this EHR using our technology and development expertise, combined with Northwell's clinical and operational excellence. We'll keep you updated as this project progresses over the next several quarters.

Moving to the ambulatory market, we had a great quarter, winning some new market share as we signed 15 new clients. We are seeing new opportunities as groups of independent physicians combine and look to consolidate vendors. An example of this is Orthopedic Centers of Colorado, which combined a number of physician groups and saw value in adopting our full ambulatory suite of technology for their larger organization. This displaced a number of our competitors, and we expect additional groups of providers to join Orthopedic Centers of Colorado, which will allow us to continue to expand our footprint there going forward. Looking ahead in this market, our pipeline for new clinical tools, revenue cycle services and patient engagement tools, feels very strong to me.

Finally, with Veradigm, I remain very happy with the balanced approach we are using to both achieve our near-term growth targets while simultaneously investing in areas to support long-term growth. An example of the latter is the long-term strategic partnership with Komodo Health that we announced during the third quarter. Initially, the partnership will focus on linking Allscripts' industry-leading ambulatory EHR data set with Komodo's health care map. And this will contain encounter data for more than 150 private and public payers. The collaboration will enable Veradigm to provide the world's largest linked dataset containing a complete longitudinal view of nearly 50 million uniquely identified patients. The market is clearly demanding linked EHR and claims data for research, and this partnership will enable our clients to perform both clinical and economic analyses as well as fill in EHR data gaps. We believe this differentiates Veradigm even further from our competitors, and we are seeing significant interest from our clients in this.

So with that, let me turn the call over to Dennis to go through more of the financial details for the third quarter and our outlook for the balance of the year.

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Great. Thanks, Rick. As we review this quarter's results, please reference the schedules in the earnings release as well as the supplemental data workbook available on the Allscripts Investor Relations website. For clarity purposes, let me make a few opening remarks before diving into the results. First, my comments on the income statement will largely focus on non-GAAP metrics unless otherwise stated. Full reconciliations of GAAP and non-GAAP figures are available in the earnings release. And second, the third quarter results do not include any impact of year-over-year transactions as we have exceeded the 1-year mark on all of our recent acquisitions and divestitures.

Now let's turn to the results for the third quarter. As Rick noted, bookings were strong in the quarter totaling $236 million, up 19% year-over-year as the momentum from the first half continued. Our reported backlog now stands at $3.9 billion. This reflects both the impact of bookings as well as renewals in the quarter that are not included in the bookings metric. Year-to-date bookings of $798 million also represents a 19% year-over-year increase as we have seen strength across our entire portfolio.

Turning to the income statement. Third quarter non-GAAP revenue totaled $445 million, within our guidance range and up 1% year-over-year. As we mentioned on the last call, we expect the year-over-year revenue growth to improve as we entered the back half of 2019. We saw this in the third quarter, and we expect our fourth quarter year-over-year organic revenue growth to improve by approximately 5% versus the same period a year ago. This reflects the continuation of the strong bookings trend we have seen in 2019 and is consistent with the multiyear guidance that we communicated earlier in the year.

Non-GAAP revenue reflected less than $1 million in acquisition-related deferred revenue adjustments in the third quarter of 2019. In the third quarter of 2018, such adjustments totaled $7 million. Q3 2019 GAAP revenue was $444 million, up 3% year-over-year.

Looking at our total revenue split, total recurring revenue was flat versus the same period last year and sequentially. Nonrecurring revenue was up 6% versus Q3 2018 as we benefited from a higher amount of upfront software license sales, thus, our total recurring revenue mix came in at 79%. We continue to expect recurring revenue to trend in the high-70s to the low-80% range for the balance of 2019.

Moving to non-GAAP gross margin. Total Allscripts gross margin was 43.2% in the third quarter of 2019 compared with 45.4% in the third quarter of 2018 and 44.1% in the second quarter of 2019. Gross margins came in slightly below our expectations in the quarter as a result of higher-than-expected transition cost in our hosting business and additional investments in the building out of the data infrastructure in the Veradigm business. We expect gross margins to improve sequentially in the fourth quarter.

Looking at operating expenses. Non-GAAP SG&A totaled $86 million, a $4 million decline from a year ago as we benefited from actions taken to drive transaction-related synergies as well as overall expense management. The non-GAAP SG&A figure excludes transaction-related and other expenses.

Non-GAAP R&D was $62 million, up slightly year-over-year. Recall that non-GAAP R&D also excludes transaction-related and other expenses. Our gross software capitalization rate was 32%, up slightly as we continue to invest in new functionality across our portfolio.

Adjusted EBITDA totaled $74 million, which equates to 17% adjusted EBITDA margin. Adjusted EBITDA margin was impacted by the decline in gross margins, as I discussed earlier, partially offset by the leverage on the SG&A line. We expect margins to improve in the fourth quarter as we benefit from cost savings, related to our data center migration, additional services revenue due to planned upgrades, faster growth in the high-margin Veradigm business and overall leverage on SG&A and R&D expenses.

Looking below the line. Total cash interest decreased to $7 million, which compares to $9 million from a year ago. GAAP loss per share in the quarter was $0.03 and includes transaction, legal and other costs of $16 million.

Finally, excluding noncash adjustments and transaction-related and other expenses, non-GAAP net income attributed to Allscripts totaled $28 million, and non-GAAP EPS was $0.17 for the quarter. We ended the quarter with a principal balance of $585 million in secured debt and $345 million of convertible senior notes. Our leverage ratio, defined as net debt divided by trailing 12 months' EBITDA, was 2.7 at the end of the quarter, up slightly from 2.4 at the end of Q2 2019 primarily due to borrowings related to share repurchases in the quarter. The strength of our balance sheet gives us significant flexibility for additional investments in high-growth areas and the continued return of capital to shareholders.

Share repurchases totaled $46 million in the third quarter of 2019. Allscripts currently has $102 million remaining under its existing stock repurchase program. We expect to be opportunistic with additional share repurchases going forward with our prior practice.

Turning to cash. Q3 operating cash flow totaled $36 million compared with $15 million a year ago. Days sales outstanding, or DSO, totaled 88 days in the third quarter, flat sequentially and down from 93 during the third quarter of 2018 as we benefited from higher revenue and improved collections. Q3 free cash flow totaled $1 million after accounting for capitalized software and capital expenditures. As we've noted in the past, cash flow will vary from quarter-to-quarter. We expect full year 2019 cash flow to improve from 2018 levels as onetime cash costs related to transactions have decreased throughout 2019.

Turning to our outlook. We expect bookings in 2019 of between $1.05 billion and $1.1 billion, consistent with our prior outlook and reflecting an 11% year-over-year increase at the midpoint. This reflects continued strength in both our Provider and Veradigm businesses. We expect revenue growth to accelerate in the fourth quarter as we benefit from the strong bookings that we've seen so far in 2019. As a result, we are also affirming our prior non-GAAP revenue guidance for the fourth quarter of between $460 million and $470 million, which reflects an approximate 5.5% growth year-over-year at the midpoint of the fourth quarter outlook.

Finally, we are narrowing our outlook for full year non-GAAP earnings per share by raising the low end based on performance to date and our outlook for the fourth quarter. We now expect GAAP earnings per share between $0.67 and $0.70 for 2019, implying $0.17 to $0.20 per share for the fourth quarter. This outlook reflects a non-GAAP effective tax rate of 24% for 2019.

And with that, I'll turn it over to Paul.

Paul M. Black - *Allscripts Healthcare Solutions, Inc. - CEO & Director*

Thanks, Dennis. First, I'm pleased with the results for the third quarter and year-to-date. We've had strong bookings performance all year long. This will help drive anticipated mid-single-digit organic revenue growth in the fourth quarter. Consistent with prior years, we work as a team to meet our commitments to shareholders and to our clients. Our leadership team, the most experienced of the publicly traded companies in our market, is using its knowledge and experience to meet or exceed our obligations.

Our long-term vision and strategic investments have driven performance in 2019, and we're confident this will continue for the long term. Our strategy is to place Allscripts where the health care marketplace is going in the future, while also focusing on the needs of our current clients. To this end, we are offering interoperable solutions that connect and optimize today's health care organizations and engage consumers. We have combined this strategy with Veradigm, and our payer and pharma clients are responding.

The investments we've made in our platforms and human capital position us to address the most crucial needs in health care today. Through our EHRs and other solutions, bolstered by our first-hand clinical expertise, we are extending our clinical relevance, driving results from precision medicine and expanded offerings. We're also serving the rapidly growing digital strategies embraced by the payer and life sciences markets. Allscripts is delivering on the increasing global demand for all of these solutions.

Our solutions are embraced by clients and are recognized as best in market. We see this in the long-term extension of our Sunrise platform by our largest client, Northwell Health. Our solutions are all recognized in by best-in-class by the industry Black Book, named us the #1 of 68 EHR solution providers in the global user satisfaction survey. Black Book also named Allscripts Sunrise as a top overall inpatient EHR, the large hospitals across the United States in 2019. In addition, Frost & Sullivan awarded the Ambulatory Revenue Cycle Company of the Year to Allscripts' revenue cycle business unit.

Last month, we held our Allscripts Client Experience Meeting, or ACE, in Dallas. Over 500 of our Sunrise, TouchWorks, Paragon and revenue cycle clients were in attendance. Topics included going all-in with the latest upgrade through digital front door creation in precision medicine.

Looking ahead at the end of this year and in 2020, we will focus on organic revenue growth, increasing margins as we leverage our scale and generating free cash flow. This will allow us to execute on our long-term capital deployment priorities of prudent R&D investments, strategic and accretive M&A opportunities and opportunistic share buybacks. All of this will allow us to better serve our clients and will benefit associates and shareholders.

With that summary, let's open it up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Michael Cherny with Bank of America.

Michael Aaron Cherny - *BofA Merrill Lynch, Research Division - Director*

So first, maybe on the Northwell expansion and the new product development. Can you maybe talk to us about what are some of the milestones we should be looking for as you work on these product developments, as you work with commercialization efforts? And how we should think about the economics, at least in terms of how it rolls through the model and, even better, how it ties to your multiyear growth targets? And it -- was this actually contemplated in those targets you put out earlier this year?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. Mike, thanks for the question. I think with respect to the first part of your question, time-wise, I think you should continue to expect, maybe not every quarter, but the work toward design and that's really with a focus on user interface and workflows, will really get worked on hard, I'd say, over the next 6 months or so. And then we'll do a little bit more work on building. We've done a lot of work on the chassis of this solution already. And so we'll have a little bit of work to do to build. And then of course, Northwell will be a lab for us, if you will, for commercializing. So they'll become a user of it.

So that's the big-picture plan. As we work through that, we'll communicate what's relevant as we go through that. I think it starts, though -- again, really to the rest of your question, with an understanding that there is very low user satisfaction in every EHR on the market today. And so we see a big opening for an opportunity that uses modern technology to really build a solution by the users. So kind of a tool for physicians, built by physicians is the way we're thinking about it. And we're excited about it.

We -- yes, it's incorporated into our growth aspirations that we've already talked about. As we commercialize it further and we see what kind of share shift we get with it, we'll obviously revise those outlooks as appropriate.

Michael Aaron Cherny - *BofA Merrill Lynch, Research Division - Director*

And then just one quick one for Dennis. You talked about the expectations for gross margin step-up into the fourth quarter. How much -- is that simply tied to the better revenue growth? Or are there other elements in there in terms of mix or other components that drive that? Maybe any details on how that compares to the 3Q gross margins you reported.

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Yes, Michael. We do expect the gross margin to improve sequentially in the fourth quarter. Part of it is just the overall revenue growth, as noted, that we expect to see pretty significant growth from Q3 to Q4 in top line revenue. Some of that being software, which has high margins. We also are seeing pretty strong growth across all the different products within our Veradigm platform. So we expect that business to grow. And that typically has higher margins than what we see in the provider space.

And then the last item is, we expect to see -- to complete the data center consolidations, which had some incremental costs that we incurred in the third quarter. We expect the final data center conversion to be completed by the end of the year, which should bring higher margins as we go into the end of Q4 and into 2020.

Operator

Our next question comes from Charles Rhyee with Cowen and Company.

Charles Rhyee - *Cowen and Company, LLC, Research Division - MD & Senior Research Analyst*

Just a question. I don't know if I missed it, but maybe if you can kind of give a sense for Veradigm's performance specific in the quarter. Is there a revenue number you kind of going to share with us or at least a little bit more in terms of the growth characteristics of Veradigm? And then secondly, Dennis and Rick, you talked about sort of 5% -- 5.5% midpoint of revenue growth in the fourth quarter. This quarter, we kind of came at the low end -- the lower end of the guidance range that you had kind of set out before. Anything -- can you talk about sort of the bookings that -- obviously, strong bookings throughout the course of the year so far. Anything in those that you're already seeing implemented that you're already seeing coming in for the fourth quarter? Or just maybe a little bit on sort of what kind of might have happened between this quarter and what you're seeing for next quarter?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. So Charles, I mean, we'll file our Q tomorrow with segment disclosures, et cetera. But you should think of Veradigm as -- is a business today that's in the $150 million to $175 million a year, annual range. We continue to believe its best days are still ahead of it. So I'll reiterate the comments I made earlier about -- I'm happy to see us hitting our near-term numbers but also making investments and the progress on what I think are longer-term growth opportunities for that business. So we remain excited about it, and I think we'll have lots to talk about that in the future as we go.

As far as the revenue -- sequential revenue uptick. There's a little bit of seasonality that Veradigm experiences, and they tend to have a strong fourth quarter. So you have a little bit of that factor. But I think beyond that, it's really what you surmised. We've had some strong sales for several quarters in a row now, and we're starting to see that come to fruition in the revenue line.

Charles Rhyee - *Cowen and Company, LLC, Research Division - MD & Senior Research Analyst*

So just to clarify, it's just a little bit more of that, the strong bookings we saw early in the year, it just took a little while for it to start to get implemented and ramping into the numbers themselves?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. I mean there is some of that. There's some previous sales that are coming in. Again, there's some seasonality patterns that we have at Veradigm and then also, our outlook for pipeline that will convert to sales in the fourth quarter and what some of the other revenue implications of those deals are that are in front of us. So it's a little mix of all the above.

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

We've also had some strong bookings in the first half in HealthGrid and at revenue cycle management, which takes a little while to get up and convert that into revenue. So we're starting to see the benefit of that as we go into Q4.

Operator

Our next question comes from Robert Jones with Goldman Sachs.

Jack Rogoff - *Goldman Sachs Group Inc., Research Division - Research Analyst*

This is Jack Rogoff on for Bob. So it was encouraging to see free cash flow get to positive territory in the quarter. But I think your commentary has been for 80% plus of net income headed into 2020. So my question is, what gets you incrementally closer to that goal? And is that still within your range of expectations given the step-up in capitalized software in the quarter?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. Thanks, Jack. So as we presented our results for the third quarter, if you look at it from a year-over-year basis, free cash flow was up $24 million year-over-year. $40 million sequentially from second quarter. So we've seen improvements in our free cash flow and our operating cash flow, both year-over-year and sequentially.

Going forward, we'll continue to focus on -- the data center moves will be behind us for the most part, which has been an expense we've incurred during 2019 that will be -- like I said, that we will complete the last action at the end of the year. We've also seen some significant improvements in our DSO, going from 93 down to 88. We'll continue to work that and drive better receivables performance.

Some of our retention programs that we've had in the past are all behind us now. So that won't be a burden that will carry forward into the future. And as we look to manage our overall spend across the company, both in SG&A, where we've seen benefits throughout the year, we expect to see those benefits continue into next year. We'll also look to reduce our overall gross R&D where it makes sense and shift some of those dollars to more revenue-generating projects.

Jack Rogoff - *Goldman Sachs Group Inc., Research Division - Research Analyst*

Got it. That's helpful. And then regarding Northwell, does your joint development efforts involve any increases in R&D spending versus what we would normally expect?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

At this point, I would not expect that.

Operator

Our next question comes from David Windley with Jefferies.

David Howard Windley - *Jefferies LLC, Research Division - Equity Analyst*

In the -- focusing on Veradigm. In the Veradigm business, and particularly the data provision for payers and life science, are you productizing that data into kind of granular-specific products? Or is it more kind of a lump sum data provision of EMR data from yourselves and NextGen to the customer to do with it as they will?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

There are restrictions in use of that information whenever we have it. And the -- whether it's a onetime feed or a feed that's getting updated or refreshed on some kind of regular basis will vary by client need. So I think you should think of it more as a product than it is just a pool that people can wander around it.

David Howard Windley - *Jefferies LLC, Research Division - Equity Analyst*

Okay. And is the traction that you're seeing -- you mentioned kind of the seasonality in the fourth quarter, I think that applies to this business as well. Is the traction more life sciences these days? Or pretty balanced between life science and payer?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. I mean -- so again, Veradigm is more than just a data business. Veradigm has...

David Howard Windley - *Jefferies LLC, Research Division - Equity Analyst*

Sure. Understood.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Okay. And so it appeals very much to payers as well as life science companies and life science company surrogates like CROs. And so we have client depth and breadth across all those major areas. And I think it's fair to say that the interest, enthusiasm and activity we're seeing is growing in all of those areas.

David Howard Windley - *Jefferies LLC, Research Division - Equity Analyst*

Okay. And then maybe finally, and I'll let this go, but your deal with NextGen certainly augments the breadth of that data. I think you've talked about maybe at least being in discussions with some other sources of data. Could you comment on either the volume of those discussions or the progress in those discussions as it relates to growing the data set?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Well, I'll start by just saying, we're off to a good start with NextGen, and that's progressing largely as everybody expected. We're seeing some revenue come in from that now. But I would expect that to scale up much more significantly as we get into the later part of second quarter of next year.

Yes, we are continuing to have dialogue with other industry EHR competitors who see the scale we've created and see the opportunity to partner with us there. Nothing finalized on that front yet. So obviously, as we finalize anything, we'll have more to say at that time. But right now, I'd just say, the discussions continue.

Operator

Our next question comes from Donald Hooker with KeyBanc Capital Markets.

Donald Houghton Hooker - *KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst*

Great. Is there any update on that Practice Fusion settlement from the other -- that you talked about last quarter? I think you had hoped for some maybe some offsetting recoveries from some third parties.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. So let's just -- I mean, we'll parse that question. We continue to work very constructively with the Department of Justice on finalizing that settlement that we had reached. So that has to obviously be documented and formalized and we are doing that. We're working with them, and we're still hoping that that will be wrapped up by the end of this year. There's been no change at all to the material terms of what we -- when we announced the settlement last quarter on this call. What was the second part of your question? What?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Recoveries?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Recoveries? Yes. So recoveries. We mentioned that at the time we do have a variety of third parties. We expect to have a portion of recoveries from. But I think that's going to happen -- play out through 2020, possibly even beyond. But it's going to -- that'll be down the road a little more. Remember, we have not paid out dollar one yet either, so just so we're clear.

Donald Houghton Hooker - *KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst*

Yes. Yes. Sure, sure, sure. And so as we start thinking about 2020 now, how are you thinking about maybe guiding The Street in terms of -- are you going to give sort of a forward quarter revenue? Or are you going to give kind of -- it seems like a lot of your business is recurring at this point. So it feels like there's some decent predictability here. Are you going to give us kind of a full year outlook? Or how are you thinking about guiding The Street going forward from an investor relations standpoint?

Paul M. Black - *Allscripts Healthcare Solutions, Inc. - CEO & Director*

We'll tell you in January. How does that sound?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Look, I mean, I think our quarterly approach this year, while perhaps a little unorthodox, I think frankly, has worked well. It's -- we've had, I think, the tightest conversation so far with The Street in terms of performance versus expectations, and I attribute that to that.

The simple truth is, even with a business model that's now largely 80% recurring revenue, some of that recurring revenue still has upfront revenue consideration when you put it through the accounting standards that we operate it under today. So predicting quarterly numbers down to the last 1% of quarterly revenue or 2% of quarterly revenue, it's a challenge even when we just put quarterly ranges out there. To put an annual range out, I think, leaves a lot of space for potentially a disconnect between what the company is expecting and what The Street is expecting.

So we'll continue to monitor through the year, but I guess that was a little commercial for -- and we think even though it's a little unorthodox this year, it'll probably work pretty well. And we will continue to take input from you guys. And we'll make a decision in January.

Donald Houghton Hooker - *KeyBanc Capital Markets Inc., Research Division - VP and Equity Research Analyst*

Okay. And maybe one last real quick one. Are there any nice pickup in revenues in Q4? And are there any kind of onetime revenue items there with these renewals, this Northwell renewal? Or any kind of bolus of sort of revenue associated with that?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

No. There's nothing -- no bolus at all for Northwell. And the only thing that might even qualify for the word bolus is some of the seasonality I mentioned earlier.

Operator

Our next question comes from Eric Percher with Nephron Research.

Eric R. Percher - *Nephron Research LLC - Research Analyst*

Rick, maybe to follow on with the prior question. As we look at the strengthening revenue number for next quarter and strengthening gross margin, before we get too carried away looking out to 2020, I wonder, is there anything relative to the long-term guidance? There are clearly elements that kept you from reaching that earlier in the year. As we look forward, is there anything you would call out with respect to the last year we should keep in mind?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. Eric, I don't think there's anything that's particularly noteworthy. I mean we are -- look, we put out an ambitious goal, or what we felt was an ambitious goal, last -- beginning of this year for what we would do on an organic and potentially even on an inorganic basis, or what we expect to do over the next 3 years. As you point out, through 3 quarters, we're certainly below that range. We know that. We also expected to come out of the gate a little slower. So I think Q4 feels like a good outlook, and it's right in the middle of the fairway of what we were expecting when we put out our guidance for this year. But -- and so I wouldn't say that there's any reason to be thinking a lot differently right now. If we feel that it's appropriate to think differently, we'll be the first one to tell you. But I think fourth quarter is more, for me, a testament that we weren't crazy when we put out some of the aspirations we did in January.

Eric R. Percher - *Nephron Research LLC - Research Analyst*

That's good context. And then lastly, on the gross margin, can you give us some indication of how we're trending without Veradigm or in the remaining business?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Well, again, when we do, we will provide some of those details tomorrow. But from a gross margin standpoint, we had said on the call last quarter that we expected to end the year in the 44% range for the fourth quarter. And I would still reaffirm that range as we go into Q4.

As far as 2020 goes, we'll provide some additional guidance on that in the next quarter's announcement. But for right now, I'd say we should expect to see an improvement from Q3 into Q4, and up to about the 44% range.

Operator

The next question comes from Jeff Garro with William Blair.

Jeffrey Robert Garro - *William Blair & Company L.L.C., Research Division - Research Analyst*

Maybe a couple more on bookings. So first, just looking for clarity on exactly which quarter Northwell hits. And then maybe any broad color you could give on the -- just kind of generally, the order of magnitude of that extension relative to the rest of the bookings results?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. I'm really, really glad you said that question because I want to make it really clear. The Northwell extensions contributed 0 to bookings, okay? We define and have always have defined bookings as incremental business. So if you're just renewing business we already have, while that business obviously goes into our backlog, it does not count in bookings. So Northwell contributed nothing to that.

The extension, as I said in my comments, is through 2027. So it's a 7-year extension on what we have, and it matches the 7-year extension they signed last year with TouchWorks. And again, as I indicated, we're in the process of wrapping up a managed services extension with them. But none of those extensions drive bookings activity.

Jeffrey Robert Garro - *William Blair & Company L.L.C., Research Division - Research Analyst*

Very helpful. I guess the follow-up would be the end-of-quarter backlog number, that would include an impact from the extension? Is that something that we should look for in the year-end results?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Yes. That backlog does include the extension. And as Rick noted, when we complete the managed service agreement, that balance will roll in the backlog as well.

Jeffrey Robert Garro - *William Blair & Company L.L.C., Research Division - Research Analyst*

Got it. And one more for me on bookings. The kind of implied fourth quarter bookings would be a pretty strong result relative to the rest of the quarters and the year on an absolute basis, but maybe a lower level of year-over-year growth. So maybe you can provide some detail on comparison quarters and how we should think about the impact of that and maybe just the thought process behind changing versus not changing the full year bookings outlook given the momentum year-to-date?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Well, your math -- your observation is right. I'll point out, we had a really bang-up record quarter last year -- fourth quarter of last year. So the absolute dollars, I think, are strong for Q4. What we're implying in our -- just the guidance we continue to have out in front of you, but it won't have the same year-over-year lift. Historically, Q4 was always the biggest in -- quarter for everybody. Some of that buying pattern has changed a little bit, we've seen in more recent years. But last year, we certainly had a very big fourth quarter. So with that comp, I don't think you can expect 19% year-over-year growth. But we'll see. We've got a nice pipeline.

Operator

Our next question comes from Sandy Draper with SunTrust.

Alexander Yearley Draper - *SunTrust Robinson Humphrey, Inc., Research Division - MD of Equity Research*

I guess a technology question on the partnership with Northwell. When I think about what you're planning on, are you trying to get to a single instant, multi-tenant design? Or are you really moving just the front-end interface into the cloud and the back end is going to be the same?

And then I guess the follow-up is, is it a separate technology path for TouchWorks versus Sunrise? Or does this have the opportunity to bring TouchWorks and Sunrise together and more integrated?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

So Sandy, we're definitely single database multi-tenant pure cloud technology. The focus is on ambulatory outpatient, and so the workflows that go with that. So this is not an exercise to effectively integrate TouchWorks and Sunrise as we know them today. But this is a recognition that the user base would like a more user-friendly tool and we think they should do that with modern technology. That's what we're doing.

Alexander Yearley Draper - *SunTrust Robinson Humphrey, Inc., Research Division - MD of Equity Research*

Okay. That's helpful. And then maybe a quick follow-up. As mentioned earlier about the recurring revenue being flat, year-over-year flat sequentially, but you've had some good bookings out here that -- like revenue cycle management can take a while. I'm just ticking off the good bookings. What are the puts and takes that have happened that have led to recurring revenue being flat at this point and not seeing an uplift yet?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Well, I mean, I think, overall revenue has been largely flat, right, Sandy. So I mean we're going in and out of a conversation about what's happened in the last 3 quarters versus what's -- what we're out seeing for Q4. Q4, we're expecting a nice lift in year-over-year revenue. And -- but for the first 3 quarters, to be fair, it's been pretty flat. So I think what you're just seeing is the same composition of that relatively flat revenue.

As the revenue grows, yes, I think there's a possibility to see that ratio uptick a little bit, but it's going to be slow. You're talking off of a really big base, obviously. So it's not going to change dramatically in 1 quarter. But I think with revenue growth, you will see that start to creep up again towards more recurring.

Operator

Our next question comes from Stephanie Demko with Citi.

Stephanie July Demko - *Citigroup Inc, Research Division - VP & Senior Analyst*

I'll continue on that train of thought about the Northwell partnership. If you and Northwell had to start from a blank slate to create an EHR, what would differ from what exists in the market today? And with the idea that they are helping develop and commercialize this product, what sort of economics are you working with Northwell in order to give them the exchange for this assistance?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

You might have to help me with the second part of that question a little better. But I mean, I think the first part -- I mean, Stephanie, at the risk of being repetitive, I think the one thing everybody in the industry could agree on very quickly is that user satisfaction of today's tools is extremely low.

Stephanie July Demko - *Citigroup Inc, Research Division - VP & Senior Analyst*

Too many clicks?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

I'm sorry?

Stephanie July Demko - *Citigroup Inc, Research Division - VP & Senior Analyst*

I said too many clicks.

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. Lots of clicks, physician burnout, you know it. You know all the stories. So to be able to use modern technology and -- again, the first generation of EHRs, if I go back again, was really -- the focus was digitizing what were pay per forms, for the most part. So now you're talking about reimagining the clinical experience and trying to build workflows and user interfaces that make a physician's job easier rather than more difficult. So that's the blank space we start with. And that's the work we're doing, and that's why we partnered with Northwell. EHR vendors cannot do that effectively on their own, in our view.

The second part of your question, I think you mentioned something about economics. I apologize. I don't think I really followed.

Stephanie July Demko - *Citigroup Inc, Research Division - VP & Senior Analyst*

Yes. Just the economics given Northwell is helping you guys develop this. How should we think about their economics versus what it would look like in the broader market?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

You know what, Northwell's our largest customer by far. And Northwell has business relationships with us that reflect the size and scale that they represent to us. That said, there's significant economic incentive for them to make this work as well because moving from -- they host all their own technology today or the technology of ours that they run. There's some pretty significant costs that they could avoid by having a cloud-based solution. So there's lots of economic motivation for them to participate in this. But again, I think the economics are -- from their perspective, economics are secondary to physician satisfaction and trying to really take the lead in the industry of trying to reckon with this problem and do something about it. And so that's what's really motivating them much more so than economics.

Stephanie July Demko - *Citigroup Inc, Research Division - VP & Senior Analyst*

Understood. And one last quick one for Dennis. Are you guys wrong on the convert?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

Well, as you know, the convert became current in July of this year. It continues -- it holds a very attractive coupon rate of 1.25%. So we've got a lot of different debt -- the debt capital markets available to us, and we're looking at all the different options that we have available that allows us to maintain flexibility within our capital structure and keeping our debt cost low. So I would expect that we would act on that sometime in the coming weeks or months, it's very soon. Perhaps even before the end of the year, we would have been able to come to market with their -- with what our plans are. But we've got a lot of different options available to us, and we'll be coming to everybody here fairly soon.

Operator

Our next question comes from Matthew Gillmor with Robert W. Baird.

Matthew Dale Gillmor - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Dennis had mentioned some incremental costs associated with the data center conversions. Would you mind giving us a sense for the magnitude of these costs? And I know there's always puts and takes with the quarter and the year, but I was curious if those were costs that were contemplated in the outlook or is that a drag that you're overcoming?

Dennis M. Olis - *Allscripts Healthcare Solutions, Inc. - CFO*

So we had costs contemplated in the previous outlook that we had given. The costs that we actually incurred in the quarter came out to be single-digit million dollars more than what we had anticipated. So again, as we close off that final data center here this year, those costs will not carry forward in 2020.

Operator

Our next question comes from Jamie Stockton with Wells Fargo.

James John Stockton - *Wells Fargo Securities, LLC, Research Division - Director & Senior Equity Research Analyst*

Maybe just a quick one on capital allocation from here. You guys have $102 million, I think, Dennis said, left on the buyback. I think you'll probably burn through that in the next 2 or 3 quarters. Once you get that done, is the kind of the thought process from there, M&A is the primary use of cash from here?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

No. I mean Jamie, as we've shown you in the past, I mean, we can work with our Board on reauthorizing more under the buyback if we're all in agreement with that. And you know from past conversations that we've had that our view of the discount we trade at, relative to some of our industry peers is ridiculous in our view. And it's because of that we've been pretty aggressive with the share repurchases. So I think our decisions on capital allocation can be a function of what's the environment we're in. We have taken our foot off the gas of M&A a little bit the last 15 months or so. Part of that's a reflection of we wanted to make sure we digested what we already owned and make sure it was working effectively. But part of it was clearly a function of how we were being valued in the marketplace. So we'll continue to look at those levers, and then we'll make smart capital allocation decisions. And I think that's hopefully what everybody would expect of us.

Operator

Our next question comes from George Hill with Deutsche Bank.

George Robert Hill - *Deutsche Bank AG, Research Division - MD & Equity Research Analyst*

I guess one quick follow-up on Northwell. When a new product is developed, it seems like there's going to be a revenue share component. I don't know if you can talk about that at all. And then given that they were your largest client and the renewal, I suspect probably either taking effect in the fourth quarter or at the beginning of next year. Can you say whether new -- whether or not revenue from [the client] should be expected to go up or go down?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

I think -- sorry, George, you cut out a little bit, so you may have to clarify something. But I mean on the second part of your question, the extensions we've had with Northwell are a lot about the footprint we already have with them. So I think maybe around the edges, there's a little bit extra opportunities. We are talking to them about a couple of solutions they're not running today. So there's some things around the edges. But the bulk, when we talk about renewals, that's really a renewal for what they have today. So it doesn't change a lot.

But recognize, this is -- Northwell is an organization that has been growing tremendously and still has aspirations and continue to grow further. So as they grow, we obviously grow with them. I don't think -- like I said, you cut out a little. So I didn't really hear the first part of your question, George. So if you're still there, you may want to re-ask that.

George Robert Hill - *Deutsche Bank AG, Research Division - MD & Equity Research Analyst*

Yes. So I guess it sounds like the co-development with Northwell, like a product that you guys will market together, I guess, should we just think of the economics of that as like a 50-50 split? And then just to clarify the second part of the question. Well, I guess, extension or renewal. I guess what I was just wondering is, were you guys able to maintain the current pricing levels on the relationship on the extension or given that they're your largest kind of...

Paul M. Black - *Allscripts Healthcare Solutions, Inc. - CEO & Director*

Got it. The economics...

George Robert Hill - *Deutsche Bank AG, Research Division - MD & Equity Research Analyst*

Or should we assume price compression?

Paul M. Black - *Allscripts Healthcare Solutions, Inc. - CEO & Director*

Yes. No. We preserve current economics in these renewals. We do not have significant discounting on it. So no deterioration on that. And with respect to the platform we're talking about, your presumption of some kind of 50-50 split is not accurate. But why don't we just -- let's do this. Let's get the platform built and get it in place, and then we'll talk more about for the economic side.

Operator

The next question comes from Richard Close with Canaccord Genuity.

Richard Collamer Close - *Canaccord Genuity Corp., Research Division - MD & Senior Analyst*

Great. Congratulations on bookings and Northwell. So a lot of talk about Cerner shifting Millennium towards AWS longer term. I'm just curious your thoughts, do you guys see this as an opportunity for Allscripts to pick up market share at all? Or does this put you guys at any sort of competitive disadvantage? Just want to gain your thoughts in and around their announcement.

Paul M. Black - *Allscripts Healthcare Solutions, Inc. - CEO & Director*

From a cloud perspective, we have a substantial number of our applications that already run in the cloud. So when you think about anything that's not core EHR, we actually -- that's where most of those run. We have some of our electronic medical records actually already running in the cloud. And we've been working very aggressively with Microsoft Azure to talk about how we can move what we have from where we are today as a cloud-hosted opportunity in the future.

From a competitive standpoint, I would just make a comment that our competitiveness has increased substantially over the course of the last 4 to 5 years. We have a complete electronic health record that spans everything that you'd want to do in an inpatient standpoint, from a clinical standpoint, from an outpatient standpoint, from a revenue cycle in the inpatient and revenue cycle in the outpatient. So we see our overall competitive positioning to be as good as it's been since we all have been here over the last 7-plus years.

Anytime anybody does a platform switch or announces some sort of new technology that does potentially offer an opportunity for us to participate in an RFP that may be mandated by the Board of that institution, if, in fact, there's a large switching costs. So that has historically been an opportunity for people in this marketplace when somebody goes through an event like that. It's not a "Flip the switch one day, and it's fixed the next." It just doesn't work that way.

Richard Collamer Close - *Canaccord Genuity Corp., Research Division - MD & Senior Analyst*

Great. That's good perspectives. And then, Paul, maybe you mentioned a couple of points that you're focusing in on organic growth and increasing margins. Just curious your thoughts in and around what the main levers in terms of -- on the margin side, where you guys hope to get the benefits going forward?

Paul M. Black - *Allscripts Healthcare Solutions, Inc. - CEO & Director*

Yes. I think we always are looking at our costs and infrastructure of the company and how we evaluate that compared to our peers, but also compared to what we need to do in order to drive the EPS targets that we need to have for 2020 and beyond. So that's an important pile that we go through each and every year, so there's opportunities there. There's opportunities that come out of some of the synergies that we've been expecting and has been realizing as a result of some of the other organizations that have become part of the Allscripts family that will continue to be something that we focus on.

And then the third thing that you mentioned, that I referred to, that I mentioned in my comments, are around new business and what we can and should be doing in that regard to generate new footprint to our company. Those are always pretty -- very profitable when we get them. And again, because of our competitive nature and our competitiveness increased over time in the global marketplace, where we've been doing quite well, we expect to get results out of that on a going-forward basis.

Operator

Next question comes from Gene Mannheimer with Dougherty & Company.

Eugene Mark Mannheimer - *Dougherty & Company LLC, Research Division - Senior Research Analyst of Healthcare*

One more with respect to the Northwell collaboration, do you anticipate a step-up in the R&D expense related to that collaboration?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. Gene, I get that question a little bit earlier. At this point, we should not expect that, I think, at least in terms of what our overall spend levels are right now. If our outlook on that changes, we'll certainly communicate that. But right now, I don't expect overall enterprise R&D spending to change much.

Eugene Mark Mannheimer - *Dougherty & Company LLC, Research Division - Senior Research Analyst of Healthcare*

Okay. Sorry if that was asked before. So are you leveraging a lot of the work you've done with Avenel with this project so a lot of the R&D spend was made?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

We're using that infrastructure? Yes, as starting point, Gene. And so that is correct. We've got a fair amount of investment already into what we're having.

Eugene Mark Mannheimer - *Dougherty & Company LLC, Research Division - Senior Research Analyst of Healthcare*

Got you. Okay. And let's say, we're coming up on about 2 years since the McKesson EIS acquisition. How would you rate that deal today? And are you pleased with the retention rates in that business? Or asked differently, is it reasonable to say you are growing that business?

Richard J. Poulton - *Allscripts Healthcare Solutions, Inc. - President*

Yes. So Gene, let me -- I'll start by reminding you, one of the first things we did after acquiring it was we sold off a piece of it, called OneContent. That recouped more than our entire investment in the business, right? So we -- so from a financial standpoint, it would be impossible to not feel good about the return from that transaction.

I'd say putting that piece aside, yes. I mean we had to make a bet or an estimate, I should say, upfront, which was how much embedded attrition was already in the client base that was coming over. And we did that. And I'd say that has largely played out as expected. So that part, I think we did a good job of estimating that. And what happened is we knew that was going to happen, but we've been seeing some of that. So part of the answer as to why revenue has been slow to lift off is because we had a bunch of embedded attrition. That is kind of leaked away over the course of the last 18 months. And it just becomes a little more of a headwind that we have to overcome when we start looking at year-over-year results.

We're not complaining about it because, I mean, we knew that was going to happen. But that's just the reality of that. And so with those clients -- and some clients we're able to persuade to actually change their mind and stay around. But with the balance, particularly with the upgrades they've done to the latest version of the Paragon thing, we think customer satisfaction is going up considerably. And we have seen some customers who probably outgrew the capabilities of Paragon, make a nice transition to Sunrise, which is a fuller feature set than the Paragon offering is.

So we've seen people trade up, and that's been good to kind of keep them in the family as well. So I know your question, that's a long-winded answer to your question. But overall, we feel good about that transaction. And I think it's created good collective scale to our hospital and health system organization internally.

Operator

We have reached the end of the question-and-answer session. I would now like to turn the call over to Paul Black for closing comments.

Paul M. Black - *Allscripts Healthcare Solutions, Inc. - CEO & Director*

Thank you, everyone, for your interest in Allscripts. Q3 historically has been a challenging quarter. I'm glad to see the company pull through with a pretty solid quarter this time. But importantly, a full year outlook is in line with what we talked about when we were at the JPMorgan conference in January. As you all know and you've heard today, there's always a lot of things that can happen. And I'm proud of what we've been able to accomplish, and I'm also very proud of what we've been able to do on behalf of our clients.

So with that, I end the call, and thank you very much for your interest in our company and look forward to talking to you again soon.

Operator

This concludes today's conference. You may disconnect your lines at this time, and we thank you for your participation.
