OVERVIEW:

Co. reported 2Q17 non-GAAP revenues of $428m, non-GAAP net income of $27m and non-GAAP EPS of $0.15. Expects 2017 non-GAAP revenues to be $1.79-1.82b.
Greetings, and welcome to Allscripts' Q2 2017 Earnings Conference Call. (Operator Instructions) As a reminder, this conference is being recorded. I would now like to turn the conference over to your host, Seth Frank, Head of Investor Relations. Please go ahead.

Seth Frank - Allscripts Healthcare Solutions, Inc. - VP of Finance & IR

Thanks, Brock. Good afternoon, everyone, and welcome to our second quarter call and the exciting announcements we have today.

Our speakers 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 Q&A part of the call. These statements are based on current expectations and involve a number of risks and uncertainties that could cause our actual results to differ 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 descriptions of the risk factors that may affect our results.
Also, as management reviews the second quarter details, please reference both the GAAP and non-GAAP financial statements as well as our non-GAAP tables in our earnings release and supplemental data book that are available on the Investor Relations website of Allscripts.

And with that, I would like to turn the call over to Paul Black.

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

Thanks, Seth. Good afternoon, everyone, and welcome to Allscripts' Second Quarter 2017 Earnings Call.

I want to start off by expressing our condolences to Neal Patterson's family and colleagues. Neal was a friend and mentor. He dedicated his life to improving health care.

I also want to welcome Dennis Olis to the earnings call in his capacity as interim Chief Financial Officer. Dennis has been a trusted partner and a vital member of the executive team here at Allscripts since 2012. We're thrilled to have him move into the CFO role.

I'll lead off with my perspective on the quarter and current business environment. Then I will discuss the announcement today of a definitive agreement to acquire the hospital and health system business, or Enterprise Information Solutions, from McKesson Corporation. This is very exciting news, and we're pleased to announce this on the heels of great second quarter results.

Second quarter results were strong, especially as it relates to bookings. In addition, non-GAAP revenue, adjusted EBITDA and earnings per share all beat or are in line with consensus Street expectations. We are well positioned to achieve Allscripts’ 2017 financial outlook.

We take the commitments we make to the financial community in the same vein as we take the commitments we make to Allscripts' clients. They are foundational to the company's credibility and reputation.

Bookings for the second quarter of 2017 were $407 million, a new record and up 12% year-over-year. This result is notable considering the tough bookings comparison in the second quarter of 2016, when bookings grew 39% year-over-year. I am very pleased that all major end markets, inpatient, ambulatory, post-acute, showed strong activity that contributed to these results.

There are more EMR replacement opportunities and new initiatives via government entities abroad.

We expect to see a higher volume of decisions made in the back half of the year and are optimistic that we are well positioned to win our fair share of these opportunities given the momentum we have created over the past 5 years.

Allscripts has a tremendous portfolio of depth and breadth, and a formidable software and services offering rivaling anyone else in the industry. This includes service offerings that provide significant and durable value to Allscripts clients operating in a very cost-conscious environment.

Let's discuss today's McKesson Enterprise Information Solutions announcement. At the Allscripts Investor Day in March, we said we believed that we are in the best position we've ever been as a company. Rick and I have talked for some time about the need to bolster Allscripts' inpatient EHR market share. We've been doing that one RFP at a time since we arrived and have built some nice momentum both inside the U.S. and abroad.

At the same time, we constantly evaluate opportunistic scenarios to deploy capital in line with our strategy. We are committed to long-term initiatives that best serve our clients and associates, increase Allscripts' breadth, depth and scale, and to advance the company's leadership in innovation. By achieving these objectives, Allscripts shareholders will be rewarded over time.

With that perspective, we are announcing an important next step to accelerate Allscripts' long-term position in the industry we proudly serve.

The acquisition of McKesson’s hospital health system business helps us further catalyze this success by adding hundreds of new community hospitals and IDN clients to the Allscripts client base. Today adds a highly skilled team of associates and incremental solutions to the Allscripts portfolio.
This transaction is a win all around. It benefits McKesson by positioning an important asset in the hands of a strategic partner who will be an outstanding custodian on behalf of Enterprise Information Solutions clients and the company’s associates.

These solutions also benefit Allscripts by combining the hospital and health system business. Including the Paragon platform, we are adding a market-leading EHR to the community hospital segment to Allscripts.

The business also brings us a comprehensive portfolio of additional solutions that complement the current acute care offerings that we have today. This transaction is about complementary solutions and enhancing cross-sell opportunities for above-the-EHR solutions, post-acute care, population health and precision medicine.

With the multitude of service offerings we provide today, including hosting Revenue Cycle Management Services, we are confident these value-based care solutions will be of keen interest to these clients.

Big picture, this move is a consistent and sensible extension of Allscripts’ long-term strategy that embraces open platforms and the truth when it comes to health care: one size does not fit all. We believe health care is a unique business with many missions and strategies, large and small organizations, simple and complex service lines, locations in rural, suburban, academic and urban settings, operating in a diverse fabric of primary care and multiple medical and surgical specialties with care delivered in outpatient, inpatient and post-acute community-based care settings.

In addition to better meeting diverse market needs bolstering Allscripts’ offerings and providing significant cross-sell opportunities, this transaction takes Allscripts up the value chain with even greater resources for innovation and opportunities to gain scale from the existing platform we have today.

I’ll now turn the call over to Rick for more color on the quarter and on the acquisition.

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

Okay. Thanks, Paul, and thanks, everybody, for joining us today.

As Paul said, I’ll go into a little additional color on the quarter’s results and then provide some additional perspective on the acquisition as well as another transaction that we completed after quarter end.

Let me start with the largest market segment, health systems. In the hospital and health system market segment, we had several significant achievements during the quarter.

To start, we signed the largest new Sunrise agreement since 2011 with a U.S.-based nonprofit integrated delivery network. This system includes 6 hospitals and an affiliated medical foundation, plus a network of community physicians and medical practices across the regions it serves. This organization evaluated all available alternatives in the market and ultimately decided on Sunrise as the appropriate choice.

This will be a substantial project that will afford this organization significant opportunities to gain efficiencies and transform care delivery across the board.

Within our existing Sunrise space, we had a strong quarter of client expansions and renewals. Catholic Medical Center in New Hampshire, which we announced in a press release on Monday, signed a long-term extension in the quarter after evaluating its entire go-forward strategy and all other options in the market. The client is consolidating its remaining strategic IT functions onto the Sunrise platform, including the Sunrise Financial Manager module and additional ancillary systems.

Also, the University of Kentucky signed a long-term extension for Sunrise in the second quarter and as well also added some multiple software modules to their Sunrise Clinical Manager platform.
We also continue to see significant interest, dialogue and business activity around Allscripts' value-based care solutions, including the CareInMotion platform for interoperability, care coordination, cost management and patient engagement.

We took a big leap forward with the reach of our core -- of our care coordination capabilities as we announced the strategic partnership agreement with Conversa to expand our capabilities around patient engagement.

We also signed several agreements with several different academic medical centers, both inside and outside our Sunrise base, who are adopting our CarePort solution for tracking and managing patients across post-acute care transitions.

Also in the second quarter, 2bPrecise, our Allscripts EHR-agnostic cloud-based precision medicine platform, announced a technology license agreement and collaboration initiative with Mayo Clinic to research and develop genomics-based care protocols. This is the first 2bPrecise agreement outside of Allscripts EHR [base].

Finally, we saw several clients who operate mixed environments of EHRs in their inpatient and outpatient settings select FollowMyHealth as their enterprise wide patient portal. In this regard, FollowMyHealth will be the strategic glue for patient centers' engagement across their clinical network.

Moving on to the independent ambulatory market segment. Our Revenue Cycle Management Services remain a robust area of demand, and we are seeing increasing traction with large enterprise TouchWorks clients. Springfield Clinic, a longtime TouchWorks client, signed the largest multi-year Revenue Cycle Management Services agreement to date.

Also, demand for managed services and hosting were strong in this quarter as well. Most clients are realizing that a shift to a hosted infrastructure via the Allscripts cloud makes a great deal of sense for them, both financially as well as strategically.

This quarter, we signed four new TouchWorks hosting clients, including Maine General Health, illustrating the value of this offering.

One of Allscripts' largest ambulatory clients took a large leap forward this quarter with a strategic agreement to expand the CareInMotion platform across all of their markets around the country after a very successful initial pilot over the last year in one of their regions. The client uses Allscripts' TouchWorks as well as managed services for its outpatient strategy, and with this expansion has now elected to use CareInMotion as its primary population health platform for the future.

Moving to the post-acute market segment. Netsmart, which we anniversary-ed this quarter, continues to solidify its leadership position in the market, and we are exceptionally pleased with the continued progress the team there is making. Bookings were a record in the second quarter and had -- represented strong double-digit year-over-year growth in the quarter.

Now I'd like to turn my attention to 2 noteworthy events that occurred subsequent to quarter end. The first and most significant is the acquisition of McKesson's Enterprise Information Solutions business. Paul gave a very comprehensive review of the strategic rationale, and I don't want to be overly redundant. But I do want to emphasize a couple of critical points to keep in mind as you consider this transaction.

This is a transaction that is both strategically and financially accretive to Allscripts and its existing stakeholders. This transaction will give us the right product for the less complex community hospital segment of the market. In this regard, there's going to be no need to dumb down Sunrise or otherwise face resource prioritization conflicts for the different needs of different market segments.

This transaction will also double our portfolio of hospital-based EHR clients, and in this regard, will allow us to increase our investment in above-the-EHR value-based care tools.

This transaction will also give us direct ownership of important clinical modules such as lab, blood bank and content management that we currently have to rely on third parties for. And in this regard, this will give us long-term certainty on product road map for these modules as well as lower the total cost of ownership of our overall solutions.
And as Dennis will discuss in more detail later, we expect this transaction to be materially accretive to Allscripts beginning in year 1. So this will fundamentally make Allscripts a financially stronger company. We believe this is a prerequisite for long-term competitiveness in this industry as scale will increasingly matter.

And finally, our accretion modeling does not assume risky technology integration strategies or risky client migration strategies.

As Paul discussed, the marketplace is not and we have never treated it as one-size-fits-all. And you can even see from the actions of competitors that they do not believe one size fits all either.

Paragon will continue to be the go-forward community hospital offering from now on from Allscripts.

The second event that I want to mention to you relates our relationship with NantHealth. As you saw in our press release, accounting rules forced us to take a mark-to-market write-down in the quarter on our investment stake in NantHealth. Under these rules as well as some forthcoming amendments to these rules, we would be subject to earnings volatility prospectively with further mark-to-markets.

So in order to both avoid further prospective volatility as well as better align the long-term commercial interest between Allscripts and NantHealth, we have restructured the relationship between the 2 companies. We have signed an agreement to exchange our ownership interest in NantHealth for certain technology assets and client relationships that they own today as well as a large multi-year commitment to purchase software and related services from Allscripts. We think this transaction is good for stakeholders of both entities, and we expect this transaction to close in the third quarter.

And with that, Dennis will go through the quarter financial highlights and the impact of the McKesson health systems transaction on our outlook. Dennis?
Looking at revenue results by line item. Total software revenue in Q2 increased 9% year-over-year, totaling $280 million. Recurring software revenue, consisting of subscriptions, recurring transactions and support and new maintenance, increased 6% year-over-year. Nonrecurring software revenue increased 21% year-over-year, a strong performance driven by client demand for add-on software. Please understand that we will see fluctuations in this result from quarter-to-quarter and would expect to see this number trend down a bit in Q3.

Turning to client services. Consolidated non-GAAP revenue grew 6% year-over-year to $148 million in Q2, primarily attributed to growth in recurring services revenue.

Recurring services revenue increased 12% year-over-year, driven by private cloud hosting, managed services, revenue cycle services and other multi-year service offerings. Similar offerings from Netsmart such as hosting and RCMS also contributed to this increase.

Allscripts' nonrecurring service revenue decreased 3% year-over-year based on a difficult Q2 comparable. Nonrecurring services increased $3.6 million or 8% compared to Q1.

Looking at non-GAAP gross margin, total consolidated gross margin was down 10 basis points year-over-year, but increased sequentially by 50 basis points.

Analyzing revenue by component. Software gross margin declined 250 basis points year-over-year. Client service margins for Q2 increased 18% compared to 13.9% for the same period last year due to continued gains in efficiencies and scale within our managed services business.

Looking at expenses. The second quarter non-GAAP SG&A totaled $96 million, a 10% increase year-over-year, primarily due to Netsmart reporting for the full quarter and several smaller acquisitions completed in 2016.

Quarter-to-quarter, non-GAAP operating expense decreased slightly on a consolidated basis, illustrating continued efforts at discretionary expense management. We anticipate a modest increase in operating expense during the second half of the year to support ongoing business growth across the company.

Gross R&D was $77 million, up 11% year-over-year, as the company continues to invest in innovation and supporting regulatory requirements. Allscripts' software capitalization rate was 40%, an increase from the low to mid-30% range where we have been trending since early 2016. We believe Q2 will be the high watermark for software capitalization rates in 2017 based on the timings of projects driving this metric. We expect a sequential decline for the remainder of the year to close out 2017, with a mid-30% cap rate consistent with our over 30% commentary in the past.

Given the Q2 software capitalization rate, R&D expense as reported was $47 million, down $2 million from Q1.

Adjusted EBITDA totaled $90 million, a 15% year-over-year increase and the equivalent to a 21% adjusted EBITDA margin, up from 20% a year ago. Netsmart's adjusted EBITDA was strong in the quarter and is trending in the 27% to 28% range as a percentage of Allscripts' total reported EBITDA and in line with our expectations for their contribution in 2017.

Looking below the operating line. Total cash interest on a consolidated basis increased to $16 million comparable to $12 million a year ago, due to a full quarter of interest on Netsmart's non-recourse debt consolidated on Allscripts' balance sheet.

As Rick discussed, we recognized a noncash impairment charge of $144.6 million as required by GAAP. The vast majority of this impairment charge relates to Allscripts' investment at NantHealth's common stock.

In addition to the impairment charges, which is excluded from non-GAAP purposes, GAAP net income included transaction-related and other costs of $9 million. This reflects cost incurred associated with the transaction activity, legal settlements, severance and expenses associated with the acquisition of the Enterprise Information Solutions business from McKesson.

Finally, non-GAAP net income totaled $27 million and non-GAAP EPS was $0.15 for the quarter.
Non-GAAP results exclude noncash expenses, transaction and other costs. As a reminder, non-GAAP EPS is calculated net of noncontrolling interest to reflect Allscripts’ ownership portion of the partially owned consolidated businesses.

Non-GAAP net income growth, which was nominal, was impacted by $3.7 million in additional interest expense year-over-year, mostly related to Netsmart.

Allscripts ended the quarter with $453 million in secured debt and principal balance of $345 million on our convertible senior notes. Netsmart’s total debt, which is nonrecourse to Allscripts but reported due to consolidation, totaled $598 million.

Turning to cash. Operating cash flow totaled $34 million, down from Q2 of 2016, reflecting higher costs related to multiple factors, including the timing of the 2016 variable compensation payments and other working capital requirements.

Free cash flow totaled negative $14 million after adjusting for investments in software development and purchased software. As we’ve noted in the past, cash flow will vary from quarter-to-quarter, and we expect improvements in both operating and free cash flow in the second half of the year.

And finally, note that we repurchased $12 million in stock in Q2.

To sum up, let’s discuss our outlook for the remainder of the year. Given the proposed acquisition of McKesson’s hospital and health systems business, we are adjusting our outlook for 2017 as well as the 3-year outlook we provided at Investor Day. The changes to targets in the release that I will describe here reflect the following assumptions: One, the proposed acquisition closes early in the fourth quarter of calendar 2017; and two, the non-GAAP target exclude approximately $50 million in severance and transaction costs expected to be incurred beginning in the fourth quarter of 2017, which are expected to be recognized quarterly until no later than the fourth quarter of 2018. The company expects that most of these costs will be incurred in the fourth quarter of 2017 and the first quarter of 2018.

We are increasing our non-GAAP revenue outlook between $1.71 billion and $1.74 billion to a range of between $1.79 billion and $1.82 billion, reflecting 1 quarter of the Enterprise Information Systems business.

We are affirming our adjusted EBITDA of between $345 million and $365 million on a consolidated basis, and we are affirming our non-GAAP earnings per share growth of between 10% to 15% in 2017.

Moving to our 3-year CAGR targets for 2018 through 2020. The change in growth CAGR targets incorporates our anticipated contribution from the acquired McKesson business during this period.

For non-GAAP revenue, we are increasing the 3-year CAGR targets from a range of 6% to 8% to a range of 9% to 11% growth.

For non-GAAP earnings per share, we are adjusting from a target of 12% to 15% growth to a target of 17% to 20% growth. We will provide additional information as we move forward through the process, but the net result is that the revenue growth will accelerate in 2018 from the transaction, and non-GAAP earnings per share will increase annually at an accelerating rate through the 2018 through 2020 period as we fully harvest the earnings potential from the business.

And with that, we’ll turn it over and take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question today comes from Sandy Draper, SunTrust Robinson Humphrey.
Congratulations on the really nice quarter and the transaction. I guess, just the flip side of the congrats is, on one hand, it’s really an interesting opportunity; you guys are clearly excited. But this, to me, is really a really transitional quarter for you. It seems like the business is accelerating, things are improving, things are going well. And I know you addressed this a little bit, maybe Paul or Rick a little bit more. Obviously, why now? It’s partly because the McKesson business was for sale, but why add an element of uncertainty and risk when the business seems to be turning; things are getting better? What’s the comfort level of adding that element of risk when it seems like the underlying fundamentals were really starting to track forward?

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

Yes, Sandy, this is Rick. I'll start. Paul can add on. Look, Sandy, this is an industry that is going to continue to transition. You can go around the horn for both inpatient and outpatient competitors and you'd find several whom are either for sale actively, have been recently for sale or will be for sale most likely in the not-too-distant future, and those that don't necessarily have for sale signs in the front yard yet. There are several others you could question what their long-term strategic viability is. So as the market matures, consolidation is a natural occurrence and it's inevitable. And we're -- we didn't feel like we had to do anything, but we want to make it clear to the market, we're here for the long term; we will be one of the platforms. Scale does matter, and we had to consider all of that for the long term. And so this was an opportunity to get what we think -- the asset has had some near-term challenges. Those are understandable given what McKesson's gone through over the last 1.5 years in terms of exiting their overall health care IT portfolio. But underneath it is some really good core assets. And for us to pick up good core assets, increase our market share significantly in the inpatient space, and for all the elements I went through -- I don't want to repeat what I said in my script -- they are all good, strategic moves as well as good financial moves. So there's maybe never a perfect time to do significant acquisitions, but I would contrast this with other transactions from Allscripts' past. This is not a merger of equals. This is not 2 dramatic businesses coming from dramatically different segments of the market that are going to try to do some yet to be defined integration of solutions or products or things like that. This is a, I think, by all rights, a bolt-on acquisition that helps us achieve scale and value quickly, and that's what's behind it.

Operator

The next question is from Matthew Gillmor of Robert Baird.

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

Maybe just on the transaction announcement. So 2 questions. Just first, a clarification. Can you -- are you buying just Paragon and the other products that you've mentioned? Or does this also include Horizon? And then second, can you give us some sense for how that business is priced from a recurring and nonrecurring revenue standpoint?

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

So Matt, the answer to the first question, it's the entire portfolio that's left inside their Enterprise Information Solutions business, and so it does include Horizon. Horizon, as you know, was announced some time ago as a sunset product. So by the time we're close on the transaction, there will be 1 or probably 2 quarters left of wind-down there. That is -- that has never been part of the revenue base that we thought about as we look at and modeled this deal. So it's a pretty comprehensive suite of solutions that are coming our way beyond just Paragon.

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

Got it. And then did you mention on the recurring and nonrecurring revenue side?
Richard J. Poulton - Allscripts Healthcare Solutions, Inc. - President

Yes, we haven't -- we gave you overall revenue guidance, Matt. I mean, their business is, as I kind of -- similar to what I said to Sandy, the business is a lot like ours, right? I mean, it's in the same space; its technology was all built the same. So it -- we -- they don't all report recurring and nonrecurring the way we have traditionally done, so we're going to have to conform their numbers into our reporting style. So we don't have that specific guidance for you yet, but you shouldn't expect a mix there that's very different from what we have today.

Operator

The next question is from Robert Jones of Goldman Sachs.

Robert Patrick Jones - Goldman Sachs Group Inc., Research Division - VP

I guess, just sticking with the McKesson transaction, I know you guys, Rick, gave overall guidance for the year. I think McKesson had sized this business from a revenue standpoint somewhere in the $450 million to $500 million range annually. Wanted to make sure that was in the ballpark of how you guys are thinking about it. And then anything you can share on the EBITDA profile of the company as we think about building this in would be helpful.

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

Yes. So a couple of things on that, Bob. So first, yes, I know they've made some comments, maybe as recently their May quarter, on size. I think there's 2 things you have to consider above and beyond what they said. One is that included Horizon, which is a wind-down platform, so that revenue base is going down, and we expect it to go down. It's also a -- it's a business that beyond even the Horizon platform, I think, there's been uncertainty about who would own this, where this would go in the future. So there's a little bit of, I think it's fair to say, there's a little bit of client churn that is happening, and that's one of the things we're very much aware of, but also feel like we can make a pretty significant impact on it. So the figure you have is not the figure that is -- it's not that high when we talk about what our revenue range is going forward.

Robert Patrick Jones - Goldman Sachs Group Inc., Research Division - VP

Okay, I think that make sense.

Dennis M. Olis - Allscripts Healthcare Solutions, Inc. - Interim CFO and SVP of Strategic Initiatives

We will report the Horizon business as a discontinued operation going forward.

Robert Patrick Jones - Goldman Sachs Group Inc., Research Division - VP

Okay, got it. No, that helps. I guess, just one quick -- go ahead, Rick, sorry.

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

The second part, I think, of the question is what did we expect financially, I think, or EBITDA margin profile. I mean, the opportunity here is, look, we have a large platform that can be leveraged to support that business much more efficiently than they could do on their own. And so, as Dennis indicated, as we get through the integration, we expect EPS, the EPS range to be -- to grow through the 3-year time period. And we would expect, ultimately, the EBITDA acquired to be -- come in and raise our overall EBITDA margins.
Operator
The next question is from Michael Cherny of UBS.

Michael Aaron Cherny - UBS Investment Bank, Research Division - Executive Director and Healthcare Technology and Distribution Analyst

Just thinking more -- heading back to the quarter, in thinking about the bookings trends, Rick, you made some comments about -- I think it was you, Rick, and I apologize if it was Paul -- that your view of the replacement market and the outlook for the replacement market. I think we've been discussing this for a while now, but obviously D.C. has been a bit polarizing and a bit constrained in terms of what they have been doing relative to the impact it could have on your customers on a long-term basis. As you think about having those discussions and thinking about what you're selling above the EHR, how do those discussions evolve against the backdrop of the uncertain D.C. policies? And I guess, specifically related to this quarter, what do you think from a kind of macro perspective allows you to drive such strong revenue bookings growth given the comp?

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

I'll take the question. I did -- I talked about it. On the EHR side, there continues to be a decent level of replacement opportunities, whether it's somebody that's out there that has raised their arm and said, "I'm tired of the people I'm currently working with," or it's somebody who's said, "I have acquired a bunch of additional assets, and we want to put Sunrise in." That's happened to us again this quarter. Or we've got other people that are expanding the Sunrise portfolio that we have in place with them, things like surgery or ambulatory or our revenue cycle Sunrise Financial Manager. So inside of that, if you will, franchise, there's a number of things that continue to bode well for us based on the investment that we made organically in that platform. Then you think about the wraparound services of hosting, of outsourcing and of revenue cycle management. Those are all things that we have either built or are building, and those continue to have a decent uptake over the course of the last quarter. The main line items for a hospital beside labor, when you look at the IT portfolio, every hospital that we're talking to are looking for ways to do more with the same or more with less. And that opens an opportunity for us to have substantial discussions with them about hosting outsourcing revenue cycle efficiencies that maybe 3 or 4 years ago that was -- we've been talking about it, but 3 or 4 years ago was not as, if you will, acute as those discussions are today. So that's what's been going on here. On the population health management side, I think you'll see as a result of even some of the new legislation that's coming out, and even some more came out today, about the patient access and the API capability and exposure to that from not only a macro standpoint, but from some of the legislation that's coming forward from ONC and from the HHS standpoint, that leads to a relook at, in my opinion, what the consumer strategy is and how health care organizations are lined up with what might have been a check box item 3 or 4 years ago with a portal to really truly having a consumer platform. And that's why you saw us announce a couple pretty good sized FollowMyHealth systems over the course of this last 90 days. That FollowMyHealth has not been probably that topical. You haven't heard us talk about it for maybe 2 quarters prior. But you're seeing people walk into and think about using that as a platform for how they're going to connect with their consumers. And we do it differently than most of the other people because we have an EMR-agnostic strategy in that regard. Then broadly, on the last point I'll make on the dbMotion component that, that was a very large deal that we did for a very large multi-hospital IDN, who we put a pilot solution in for 90 days, and after that 90 days, we began -- and it was successful. And we then immediately begin negotiations on a system-wide acquisition, which got concluded by June 30. So that hopefully gives a little bit more color about the breadth and, if you will, the depth of the success in Q2.

Operator
The next question is from Jamie Stockton of Wells Fargo.

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

I guess, on the McKesson business, a couple. Can you talk about maybe bed size where you feel like you'll start to draw the line between Paragon and Sunrise? My guess is it's somewhere around 100, but I'd love to your thoughts on that and whether it will be really explicit. And then maybe a second question, just as a follow-up I'll go ahead and give you, is whether there is a component to this deal for you kind of like there was with the
Siemens deal for Cerner where McKesson’s got STAR and some other platforms that are in hospitals that aren’t necessarily using them for clinicals, and does that give you a footprint in some facilities that might have come to market in the next 2 or 3 years, that this would give you an inside track? If you could talk about that and maybe quantify it, that would be great.

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

So Jamie, let’s go reverse order. I mean, the answer to your second question is unequivocally yes. The STAR is a great example of that, but it doesn’t actually even end with STAR. Even their -- some of the other larger solutions they have, have hospital footprints in and outside their EHR base that give you that proverbial foot in the door, and I think it can be helpful. But certainly, the STAR presence is something we thought about and I think will be marginally beneficial to us as we think ahead. Oh, yes, you asked about size of beds, I’m sorry. So the profile of their Paragon footprint today is roughly half of their relationships are 100 beds and below, but that leaves the other half at above 100 beds. As we think about the go-to-market going forward, Jamie, we think probably -- I mean, bed size is certainly one important proxy or variable to consider, but also just what kind of complexity of service lines the hospital has as well would be another important factor. And so as we think about it, if it’s likely -- if it’s 200 beds or below and a relatively simple set of product lines or service lines that they have, Paragon will be the target solution. If it’s a larger institution than that and/or they have some complex service lines like say in oncology, then Sunrise will be the solution. So that’s the base starting point we have and I think every client will be evaluated on its own specifics and we’ll make the best choice with that based on their circumstances.

Operator

The next question is from Charles Rhyee of Cowen.

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

Rick, I want to get back to a comment you made earlier when you were talking about how as it initially consolidates, it becomes a matter of scale. When you look at some of the larger players, they’re really deploying kind of versions of the same solution set for the most part. And I hear you’re going to be selling -- well, it used to be TouchWorks and the ambulatory Sunrise in the large, and now, Paragon. When you guys talk -- when you’re thinking about scale and the benefits of scale, how are you thinking about that as you think about this new -- this combination?

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

Well, there’s different ways to achieve scale, Charles. Certainly, one piece is, and I think what you’re focused on, is about development dollars and how many platforms we’re investing in. But there’s a large aspect of scale, which is really around overhead, SG&A-type costs. And you can look at ours, you can look at anybody’s, you’d see that SG&A is a pretty good chunk of your overall cost base. And so that is a great opportunity to achieve some scale benefits, and as I said earlier, we have the opportunity now to have less reliance on third-party software as part of an overall solution set. And so those are some other examples of achieving scale. So if at the core of your comment is, hey, is one more EHR platform going to -- if you’re keeping that alive is that going to somehow undermine our aspirations for scale, the answer is unequivocally no.

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

Okay, that’s helpful. And can you talk about then when you think about the smaller end of the market, without having Paragon, so in the last few years, can you talk about sort of what, like what sort of win rate percentages were you not achieving that I think that this kind of really made the biggest sense for you? I mean, was that -- were you finding that you were missing a lot of opportunities because people felt the solution was just too complex for that they needed?
Richard J. Poulton - Allscripts Healthcare Solutions, Inc. - President

It's a big -- Paul will amplify it, Charles, but I'll just start by saying yes. I mean, at a certain hospital size level, Sunrise is a big lift, not only initially, but to maintain it going forward. And so in some cases, our cost couldn't be competitive. And in other cases, we had -- we were able to get in a competitive way, but the client still struggles to get the full value out of the system, I think, because of it. So we think for the long term, and again, I'll reiterate what I said earlier, our view on this is supported not only by our own actions, but the actions of really all of our competitors, is everybody realizes one size does not fit all. And so you need to have an effective solution for different segments.

Operator

The next question is from Sean Wieland of Piper Jaffray.

Sean William Wieland - Piper Jaffray Companies, Research Division - MD and Senior Research Analyst

So I'm still not quite clear on how this transaction is going to accelerate the growth of the business. And maybe we can first start just by helping us size what is the annualized revenue impact of the acquisition to your numbers. You raised your guidance by $80 million, so is it roughly $320 million?

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

So we're -- as we said, we've contemplated when we're closing, probably early in the fourth quarter, so we had to make some estimates of that, Sean. You heard the conversation earlier about why the number's lower than the last number McKesson shared. And there's a couple of variables at play. There are platforms that have been announced sunset that are going away, and we know entering that there is some level of active client churn. So I think we're going to work on that quickly out of the box and try to minimize that. And as we get more certainty and color on that, then we'll have more to say about our revenue guidance. But for now, we've put out both the near term and the longer-term guidance with some assumptions about where we're starting post-Horizon as well as what attrition might likely to be happening.

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

And adding to that also, cross-selling opportunities that we have with the product lines going both ways. So there's some addition there as well.

Sean William Wieland - Piper Jaffray Companies, Research Division - MD and Senior Research Analyst

So to be clear, the CAGR guidance that you gave for 2018 through 2020, is that inclusive of the inorganic growth that you'll see in '18? Like your actual revenue growth in '18 plus or minus should be probably somewhere around 20% with this inorganic contribution. Is that CAGR inclusive of that 20%, or is that CAGR intended to be what the business would grow on an organic basis?

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

CAGR over 3 years, Sean. And yes, it includes the add of this plus the organic growth. Clearly, the revenue will be lumpy as you'll get a number -- a big number in year 1, but given that we had the 3-year guidance out there, we still want people to be able to project ahead to what the absolute dollar revenue base for the company is likely to be that far out.

Sean William Wieland - Piper Jaffray Companies, Research Division - MD and Senior Research Analyst

Okay, so I'm hearing that it doesn't probably accelerate the growth rate much, if at all?
Richard J. Poulton - Allscripts Healthcare Solutions, Inc. - President

We're not predicting that right now.

Operator

The next question is from Stephanie Davis of JPMorgan.

Stephanie July Davis - JP Morgan Chase & Co, Research Division - Analyst

I know it’s early, but have you thought about any cost takeout potential or synergies for the McKesson assets, just given it's traditionally run at a discounted margin rate to your company average?

Dennis M. Olis - Allscripts Healthcare Solutions, Inc. - Interim CFO and SVP of Strategic Initiatives

Yes, this is Dennis. We've actually done quite a bit of work in that area. We do believe that there are substantial synergies. That's part of the value that we put when we looked at acquiring this asset, and we would expect to recognize those, as I said, over the course of the next 5 quarters post-close.

Stephanie July Davis - JP Morgan Chase & Co, Research Division - Analyst

So is there potential that you get similar to your company average now? Or could it still just run at a discount given some structural issues?

Dennis M. Olis - Allscripts Healthcare Solutions, Inc. - Interim CFO and SVP of Strategic Initiatives

Again, we've given the 3-year guidance, but I think it would be more in line with our existing core business, 3 years out.

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

Stephanie, just to be clear, I mean, we said earlier we would expect it to lift up enterprise EBITDA margins.

Stephanie July Davis - JP Morgan Chase & Co, Research Division - Analyst

All right. And one quick follow-up on the near NewYork-Presbyterian relationship. Can you just talk quickly about how it's -- just an overview on its financial margin contributions?

Dennis M. Olis - Allscripts Healthcare Solutions, Inc. - Interim CFO and SVP of Strategic Initiatives

That contract goes to 2022, and no decisions have been made there.

Operator

The next question is from Mohan Naidu of Oppenheimer.
Mohan A. Naidu - Oppenheimer & Co. Inc., Research Division - MD and Senior Analyst

So maybe Rick, Paul, do you see opportunity in the Horizon customers to maybe convince them to move at sunset -- or to Sunrise base as they look for changing it? Or, I guess, is that a sizeable opportunity that we should be thinking about?

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

We haven't had a chance to talk to them. We just have announced this today, and part of the process is we actually can’t go out and talk to them until we actually close. But clearly, we would want to have a conversation with people that are contemplating moving or might be in the process of moving and might have a capability of staying with the current platform, or having a chance to convince them that the platform that they’ve chosen might not be the right one given what our plans could be for them. So that would reply to not only the EMR but the patient accounting, to the content management piece, the lab information system, the supply chain. There’s a fair number of solutions that we would certainly want to talk to them about, if you will, bundled together with a more robust 5- to 10-year offering. But until we talk to them, it's going to be very difficult for us to project any sort of numbers around what that can contribute from an Allscripts solutions into that base.

Mohan A. Naidu - Oppenheimer & Co. Inc., Research Division - MD and Senior Analyst

Got it. Any number, I guess, that you could talk about, like the mix of customers who are on Horizon versus Paragon right now?

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

Again, you should think that the going concern platform is Paragon. The decision to sunset Horizon was announced some time ago. So many of those clients have already left. Those who haven’t left the platform yet, for the most part have probably made decisions to go elsewhere. But to amplify what Paul said, not -- we don’t think 100% have figured out what they’re doing yet, and we think Sunrise is a great alternative, and we will certainly do all we can to try to get into that. You should just think 2 quarters ahead from close, there’s no such thing as Horizon anymore.

Operator

The next question is from Garen Sarafian of Citi Research.

Garen Sarafian - Citigroup Inc, Research Division - VP and Healthcare Technology and Distribution Analyst

Welcome, Dennis. So just a quick follow-up at this point. On the acquisition, beyond the modules that you referenced, are there any specific call-outs on the McKesson products that you think you’ll be able to sell into the larger Sunrise business?

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

Yes, I think their lab, the blood bank, the surgery systems, depending upon where that might be inside of our organization. They have an anesthesia product. They have a really good, what they call, OneContent, which is a document and content management solution that has been very widely regarded in the marketplace. It’s in some of our clients today already. So there’s some decent reference-ability there, some knowledge on our side about how that works. They also have a supply chain solution that we have not had to sell to our clients in the past.

Operator

The next question comes from Gene Mannheimer of Dougherty & Company.
Eugene Mark Mannheimer - Dougherty & Company LLC, Research Division - Senior Research Analyst of Healthcare

I joined the call late, but did you talk about what level of churn or attrition you're contemplating in this transaction? Can you share that with us? And second, are you picking up the imaging stuff from McKesson, too? Or is that not part of this deal?

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

So Gene, we didn't talk about numbers or percents or anything like that. But we've obviously given Q4 outlook as well as a 3-year outlook, so we had to make some early assumptions about attrition, and they're reflected in the numbers that we've put out. So we've got attrition baked in, some pretty modest, as Dennis said earlier, cross-sell opportunities that slightly offset that. But we remain very optimistic that there's going to be more opportunities beyond what we've put into this so far, or guided so far.

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

Okay. And the imaging platform is not part of this, right?

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

That's correct. That went out with the Change acquisition.

Operator

The next question is from Richard Close of Canaccord Genuity.

Richard Collamer Close - Canaccord Genuity Limited, Research Division - MD and Senior Analyst

Just really quick on the bookings. Maybe if you could dive in a little bit deeper there. Was there any pull-forward in the second quarter from the second half for the year? I'm just trying to get a feel whether the strong -- whether you think you'll be able to post any growth here in the third and fourth quarters. And just curious with respect, like consensus growth is 7% in 3Q and 5% in 4Q for bookings. Just want to get comfortable with the second half of the year here.

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

Well, I mean, Richard, we obviously had a tough comp. You'll remember a year ago was when we had what at that time was a really big record Q2, in parts driven by the Optum deal that we signed a year ago. And so we're thrilled that we were able to, against that tough comp, still come on top of it. We had help around the horn, including new business and the deal I talked about earlier. Netsmart has all -- is firing on all cylinders right now, so they certainly helped as well. So we've got -- we had some good action. As you know, there's different buying cycles. Q1 and Q3 tend to be seasonally softer, certainly than Q4 and generally Q2 as well. But you asked, did we pull anything forward or anything artificial like -- that almost sounds like an artificial pull-forward. The answer is no. We were able to capitalize on the buying decisions that were going on during the quarter.

Richard Collamer Close - Canaccord Genuity Limited, Research Division - MD and Senior Analyst

Okay. So with respect to third quarter, fourth quarter, just in terms of the management managing expectations there, obviously, you guys have been performing extremely well here and outperforming in many cases versus expectations. But just curious, based on the pipeline, is there growth opportunity in 3 and 4Q?
Richard J. Poulton - Allscripts Healthcare Solutions, Inc. - President

Look, I mean, there’s -- Paul talked earlier a little bit about the international marketplace and some outlooks there. Those tend to be large deals when they happen. So I think it’s absolutely possible. We’re not providing guidance, Richard, I mean, we can’t provide guidance. You know as well as -- and you know well because you’ve followed us closely for a while, that we set a record every quarter last year. And it’s tough for people to perpetually set records, but we did not clean out the pipeline, and I think we’re -- our sales team is jumping right now.

Richard Collamer Close - Canaccord Genuity Limited, Research Division - MD and Senior Analyst

Okay. Yes, just giving you the opportunity to maybe manage some of the outliers down, so...

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

Like we just did.

Dennis M. Olis - Allscripts Healthcare Solutions, Inc. - Interim CFO and SVP of Strategic Initiatives

I appreciate that.

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

So I think there are definitely outliers that should reexamine what they’re doing.

Operator

The next question is from Nick Jansen of Raymond James.


Just 2 quick ones for me. Recurring revenue dipped sequentially. I think it’s the first time it’s dipped sequentially in some time, so just any thoughts on just timing there. And then secondarily, on free cash flow, I know it can be lumpy from Q-to-Q, but what should we expect for full year cash flow given where we are year-to-date?

Dennis M. Olis - Allscripts Healthcare Solutions, Inc. - Interim CFO and SVP of Strategic Initiatives

So from a recurring software standpoint, we did have a slight dip from quarter-to-quarter. It’s about $3 million primarily attributed to PQRS finishing off in Q1 and then having a little bit of a lull while the CMS is determining what they’re doing with MU3, which I believe some of the rulings come out as recently as today. So we do expect that to pick back up in the second half of the year, and Q2 was a bit of an anomaly as we were going through the transition from PQRS to MIPS reporting. As far as the free cash flow goes, again, we don’t give full year guidance on that. It was a tough Q2, as we had some increased software that we had from a development standpoint. We had some leasehold improvements on some of the facilities we have, particularly the new building that we have in Raleigh. And then we had some roll-off of some long-term software, third-party software agreements that we’re finishing off. So we would expect the second half, both operating and free cash flow, to be significantly better than what we saw in Q2.
Your last question today comes from Ricky Goldwasser of Morgan Stanley.

Mark Lewis Rosenblum - Morgan Stanley, Research Division - Research Associate

It's Mark Rosenblum for Ricky. I just have one quick one. Most of my questions have been answered. You guys talked about some incremental investments in the second half of the year. Could you just give a little more detail on what you guys are investing in? And any color there would be helpful.

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

You may have to, Mark, be a little more specific. I think what we talked about -- I talked about restructuring our investment in NantHealth. Dennis actually just finished saying he thinks that we'll see lower CapEx in the back half of the year than we did in the front half of the year.

Mark Lewis Rosenblum - Morgan Stanley, Research Division - Research Associate

I guess, I mean in relation to the increased operating costs that you mentioned. Maybe I'm mistaken.

Dennis M. Olis - Allscripts Healthcare Solutions, Inc. - Interim CFO and SVP of Strategic Initiatives

Yes, we do expect a slight increase in operating costs from first half to the second half, primarily due to when you look at cap year-on-year to the Netsmart acquisition, there's costs that will increase there with some of the acquisitions that they've recently announced. So we will see. That's primarily one of the larger contributors to the increase in OpEx expense in the second half of the year.

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

Thanks, everybody, for joining the call today. I know we had a lot to talk about, and we appreciate your spending the time with us this afternoon. We'll be hosting many of you next week, Tuesday, August 8, for the first day of the Allscripts Client Experience, or ACE, at the McCormick Center here in Chicago. Look forward to seeing you there, starting at high noon. Have a great evening.

Operator

This concludes today's conference. You may disconnect your lines at this time. Thank you for your participation.