Agilent Technologies Second Quarter Fiscal 2015 Conference Call Prepared Remarks

ALICIA RODRIGUEZ

Thank you and welcome everyone to Agilent's Second Quarter Conference Call for Fiscal Year 2015. With me are Mike McMullen, Agilent's president and CEO, and Didier Hirsch, Agilent senior vice president and CFO.

Joining in the Q&A after Didier's comments will be Patrick Kaltenbach, president of Agilent's Life Sciences and Applied Markets Group; Jacob Thaysen, president of Agilent's Diagnostics and Genomics Group; and Mark Doak, president of the Agilent CrossLab Group.

You can find the press release and information to supplement today's discussion on our website at www.investor.agilent.com.

While there, please click on the link for "financial results" under the "Financial Information" tab. You will find an investor presentation along with revenue breakouts and currency impacts, business segment results and historical financials for Agilent's operations. We will also post a copy of the prepared remarks following this call.

Today’s comments by Mike and Didier will refer to non-GAAP financial measures. You will find the most directly comparable GAAP financial metrics and reconciliations on our website.

Unless otherwise noted, all references to increases or decreases in financial metrics are year over year. As a reminder, we will talk about core growth, which reflects growth without the effects of currency and M&A within the past 12 months.

We will also make forward-looking statements about the financial performance of the company. These statements are subject to risks and uncertainties, and are only valid as of today. The company assumes no obligation to update them.

Please look at the company's recent SEC filings for a more complete picture of our risks and other factors.

Before turning the call over to Mike, I would like to remind you that Agilent will host its annual analyst and investor meeting in New York City on May 28th. Details about the meeting and webcast are available on the Agilent investor website.

And now, I’d like to turn the call over to Mike.

MIKE MCMULLEN

Thanks Alicia, and hello everyone. Thank you for joining us today for our Q2 call, my first as CEO of the new Agilent.

I will start with a summary of our Q2 operating and financial performance. Next, I will cover our progress on operating margin expansion and stock repurchases. Finally, I will close with an update on our current guidance.

I'm pleased to report that Agilent delivered solid earnings within guidance. I am even more pleased to share the story of our "top line" order growth. This growth is driven by continued strong market acceptance of our new offerings... and the effectiveness of our new sales structure.

Let me start with four major operational highlights.

First, our "Agile Agilent" program launched last quarter. This program is successfully removing cost from the business… and allowing us to aggressively build a more nimble and streamlined company.

Second, we addressed manufacturing-driven backlog issues in our nucleic acid businesses, by adding capacity. As a result, we have returned that business to double-digit profitability.

A third operational highlight is some very good news. After a lot hard work and significant investment, our FDA warning letter was lifted six months earlier than expected.

Finally, we strengthened Agilent's portfolio by divesting our XRD business.

Now, let me review Agilent's financials for the second fiscal quarter.

Our Q2 revenue was down 3 percent and grew 4 percent on a core – or currency-adjusted – basis, to $963 million. Reported orders grew 1 percent and were up 8 percent on a core basis to $1.04 billion.

Excluding the divested businesses of NMR and XRD, core revenue growth was 5 percent and core order growth was 10 percent. Book to bill increased to 1.08, as we were unable to convert all of this order strength into revenue within the quarter.

Let me provide some additional detail.

First, we had a lot of orders come in later in the quarter. Second, shipping challenges at our new Americas logistics center delayed some customer shipments until Q3.

The shipping issue was a "start-up" issue and is being addressed. However, the order timing and shipping challenges account for approximately $30 million of revenue that was pushed from Q2 to Q3.

The strengthening dollar also had an impact, reducing reported revenue by $6 million versus our guidance.

Despite the revenue recognition delay, we are quite pleased with our "bottom-line" performance. Operating margin, adjusted for Keysight billings, was 18.3 percent, up 140 basis points over a year ago. Earnings per share were 38 cents, with both the operating margin and EPS results matching prior guidance.

Moving on to the results by business group…

The Life Sciences and Applied Markets Group or "LSAG," as a reminder, brings together Agilent's analytical laboratory instruments and informatics. Core revenue growth was 1 percent, or 2 percent excluding NMR.

Growth was led by LC, microfluidics, mass spec, ICP-OES and software. Orders were strong across the group, up 6 percent on a core basis and up 10 percent excluding NMR.

As an aside, the previously communicated exit of the NMR hardware business continues to proceed as planned. Operating margin for the quarter was 15.8 percent.

We saw excellent growth in LC systems in the second quarter. The new 1290 Infinity II system, which we launched in Q4, continues to be well received by the market. This system sets new benchmarks in analytical efficiency, quality, ease of use and integration. We expect the 1290 Infinity II product portfolio to deliver double-digit growth through fiscal year 2015.

We shipped the new 6545 LC/MS Q-TOF, with a formal launch scheduled for the ASMS conference at the beginning of June. The 6545 addresses the core Q-TOF market with better performance, increased uptime and robustness, and improved ease of use for small-molecule applications.

We released OpenLAB ELN 5.0. The new electronic lab notebook adds several core feature enhancements, including an iPAD mobile client.

Next, the Agilent CrossLab Group or “ACG,” combines our analytical laboratory services and consumables businesses under a new Agilent brand. ACG delivered outstanding results. Core revenues were up 7 percent, while core orders grew 12 percent in the quarter. Operating margin was 21.5 percent.

In consumables, we expanded the Poroshell 120 family to include a new 4-micron particle size. Sales of this family have exceeded expectations, and are contributing to continued growth in the Poroshell family.

We released the AdvanceBIO Sample Prep Kit, which adds to our separation and manual sample prep technologies. Our recently introduced A-Line supplies portfolio is ramping well above expectations. And customers have responded very favorably to our new RFID Inventory Management Service Solution.

Finally, the Diagnostics and Genomics Group, or “DGG,” is comprised of three divisions: the former Dako business, Genomics and Nucleic Acid Solutions.

DGG recovered nicely in Q2, as previously guided, delivering strong core revenue growth of 10 percent versus a year ago. Dako and the Nucleic Acid businesses led DGG’s results. Orders grew 5 percent on a core basis. DGG returned to double-digit operating margins, delivering 15 percent in Q2.

In April, we announced that the U.S. FDA lifted its warning letter on Agilent’s Dako, Denmark, subsidiary earlier than expected. We are on track for the remaining remediation efforts to be completed by Q3.

And our companion diagnostics engagement with Merck continues to make progress. In April, Merck submitted a biologics license application to the FDA for the treatment of lung cancer.

Omnis instruments continued to gain customer traction, setting a new quarterly record for instrument placements. And SureFISH again saw strong growth, driven by sales through the pathology channel.

This is just one example of the synergy that we are able to leverage across the new Agilent. Our expertise and experience in analytical labs continues to drive further penetration into adjacent clinical and diagnostics laboratories. We expect these types of synergies to be characteristic of the new Agilent.

In keeping with our strategy of executing bolt-on acquisitions of complementary growth businesses, earlier this month we announced our acquisition of Cartagenia for 60 million Euros. Cartagenia is a leading provider of software and services for clinical genetics and molecular pathology labs.

Now, let’s take a brief look at Agilent’s end market performance on a core basis.

Pharmaceutical revenue grew strongly, with broad-based results across customers and products. We also saw excellent demand in Clinical and Diagnostics, with revenue growing solidly during the quarter. Growth in Food and Environmental revenue was more modest, led by demand from China.

Academia and Government revenue decreased slightly, due to some delayed budgets and order backlog build. Chemical and Energy saw a similar decrease from lower oil prices, as expected. The decline in oil production and exploration was partially offset by refining and chemical demand.

Geographically, we saw excellent core revenue growth in the Americas, with moderate growth in Europe and Asia excluding China and Japan. Greater China orders were strong, though not yet reflected in revenue. Similarly, Japan core revenue declined but saw single-digit core growth in orders.

As you know, we completed the CEO transition at the March 18th shareholder meeting, and our new leadership team is fully in place. During our Q1 call, I highlighted three focus areas where we are working as a team to drive shareholder value. As a reminder, they are:

1. Accelerate organic growth
2. Expand operating margin
3. Deploy capital for long term shareholder value

Turning from the report-out of the momentum in our core growth, let me update you on operating margin improvement initiatives and Q2 capital deployment actions.

We are executing our multi-year “Agile Agilent” program, re-engineering the company to be more efficient, nimble and externally focused. Our previously announced restructuring is underway. The new sales channel and divisional structure are fully-implemented.

We continue to look for opportunities to streamline and re-think our legacy business models. The recent closing of our U.S. Government Affairs office is just one example.

We have already delivered $24 million of the expected gross savings of $50 million in 2015 from our combined actions. We remain committed to achieving a 22-percent operating margin by FY17.

As previously guided, this year we are on track to return $500 million to shareholders in the form of dividends and buy backs. In Q2 we repurchased $162 million of stock, bringing our year-to-date repurchases to $168 million.

In our Q1 call, we raised our core growth guidance, and committed to offset 5 cents of negative FX impact through cost controls and other actions. We are confirming this full-year EPS guidance. Didier will provide further details in his remarks.

As the new CEO, it gives me great pleasure to announce that Forbes has identified Agilent as one of "America's Best Employers" in its first-ever ranking. We were rated as the top employer in the "Healthcare Equipment and Services" industry category. Part of my mission will be to make us even better.

We look forward to seeing you at our May 28th analyst meeting in New York. We'll take that opportunity to discuss Agilent's businesses in more detail. I look forward to sharing more about the steps we are taking to reach the goals we have set – to drive long-term shareholder value through accelerated growth, operating margin expansion, and optimal capital allocation.

Thank you for joining our call today. I will now turn it over to Didier, who will provide a more detailed discussion of Agilent's financial results and guidance.

DIDIER HIRSCH

Thank you, Mike, and hello, everyone.

To recap the quarter, our core order and revenue growth, excluding the impact of closed and divested businesses, were respectively 10% and 5%. As Mike stated, about $30M of revenues was carried over into Q3, due to late incoming orders and some start up issues with the transfer of our US distribution center. Those issues have now been stabilized and they will be fixed this quarter.

Although revenues ended up $32M under the midpoint of our guidance, adjusted operating margin was 18.3%, 10 bps higher than guidance and 140 bps higher than last year on 2.5% lower nominal revenues. This quarter, currency subtracted about 6.8 percentage points from our year-over-year revenue growth. Finally, we bought back $162M of stock in Q2 and generated $183M in operating cash flow.

I will now turn to the guidance for our third quarter. We expect Q3 revenues of $995M to $1.015B and EPS of 38 to 42 cents. At midpoint, revenue will grow 7% on a core basis. Our 18.3% adjusted OM at midpoint will be equal to this quarter's OM. We expect to continue our disciplined buyback program and reach the planned $365M repurchases by year-end.

Now to the guidance for Fiscal Year 2015. Versus our previous guidance, currency is forecasted to have a $10M negative impact on revenue. We are adjusting our revenue guidance for that impact but we are not modifying our EPS guidance. We expect FY15 revenues to range from $4.05B to $4.11B and FY15 EPS to range from $1.67 to $1.73.

With that, I will turn it over to Alicia for the Q&A