Agilent Technologies Fourth Quarter Fiscal 2019
Conference Call Prepared Remarks

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Thank you, and welcome everyone to Agilent's fourth quarter and full year Conference Call for Fiscal Year 2019. With me are Mike McMullen, Agilent's president and CEO, and Bob McMahon, Agilent's senior vice president and CFO.

Joining in the Q&A after Bob's comments will be Jacob Thaysen, president of Agilent's Life Science and Applied Markets Group; Sam Raha, president of Agilent's Diagnostics and Genomics Group; and Mark Doak, president of the Agilent CrossLab Group.

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

Today's comments by Mike and Bob 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. References to revenue growth are on a core basis. Core revenue growth excludes the impact of currency, and the acquisitions and divestitures completed within the past 12 months. Guidance is based on exchange rates as of October 31.

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.

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

MIKE MCMULLEN

Thanks, Ankur – and thanks everyone for joining our call today.

When I became CEO, I knew we had the opportunity to become a growth company. We would do this by investing in fast growing markets with a "building and buying" approach. We also set out to create a more resilient company business model, capable of delivering strong earnings in a variety of market conditions. To accomplish this, we developed a broader base of growth and a more flexible and efficient cost structure.

As you know, transforming a decades-old company is not an easy task – but I believed in the strength and determination of the Agilent team. The fourth quarter and full year results I will share today are a testament to the commitment of the Agilent team and their ability to step up to meet this challenge.

We strongly closed our fiscal 2019, with fourth quarter results exceeding our expectations. Agilent's Q4 revenue of $1.37 billion is up 4 percent on a core basis against a 9 percent compare. And, we have momentum going into 2020 as orders outpaced revenue.

EPS of 89 cents is up 10 percent for the quarter. Both our top line revenue and EPS are above the high-end of our fourth quarter guidance. Operating margin of 25.1 percent is up 50 basis points over last year. Q4 marks the 19th consecutive quarter of adjusted operating margin expansion delivered by the Agilent team.

Our higher than expected top line is led by 10 percent core growth from our Agilent Cross Lab Group. Business is also strong for our Diagnostics and Genomics Group, delivering 7 percent core growth. Our Life Sciences and Applied Markets revenues are in-line with expectations, down 2 percent against a 9 percent growth compare.

The pharma, diagnostics and clinical, and the environmental and forensics markets continue to lead our growth. High single-digit U.S. growth is stronger than forecasted with other regions coming in as expected. Growth in China declined low single digits as expected.

Agilent's growth strategy of "building and buying" in fast growing markets is on full display in Q4. During the quarter we closed the acquisition of BioTek. This is our largest acquisition since the launch of the "new Agilent" in 2015. BioTek brings a superb team and an excellent high-growth, highly profitable business to Agilent.

The acquisition of BioTek complements our earlier acquisition this year of ACEA BioSciences. Both acquisitions are part of our growing cell analysis business serving biopharma and academic research customers. Agilent's cell analysis business is now generating more than $250 million in annual revenue, about 5 percent of company revenues, and is growing at a double-digit rate.

We are also continuing to invest internally to drive new organic growth. In Q4, we recognized the first revenue from our new oligo API manufacturing site in Frederick, Colorado. The high quality, GMP grade oligos produced at this site are key to a new class of drugs being developed by our biopharma customers. Investing in this facility is part of our overall strategy to build a larger biopharma business. We are expecting continued strong growth in this business as we ramp volume throughout the coming year.

Finally, in October, I traveled to the UK to open a new state-of-the-art facility at the Harwell Science and Innovation Campus. The site will be a major R&D hub for laser spectroscopy and will also incorporate Agilent's Raman spectroscopy business.

Our recent acquisitions and these capital investments in Colorado and the UK are very visible examples of our continued and relentless focus on investing for growth.

Let’s now shift gears and look at our full-year fiscal 2019 results.

We had a very solid year, generating $5.2 billion in revenue representing 5 percent core growth. Strength in the pharma, clinical and diagnostics, and environmental and forensics markets led the way. Regionally, the U.S. set the pace, growing in the high single-digits. The U.S. was followed by mid single-digit growth in Asia outside of China. Europe and China grew at low single digits for the year.

Full-year earnings per share grew 11 percent to $3.11. The result is another year of double-digit earnings per share growth. The full year operating margin of 23.3 percent is up 80 basis points over 2018, despite a full-year of tariff related duties.

Our investments in ACG continue to yield dividends. ACG grew a stellar 10 percent for the year. We are helping customers transform their analytical lab operations by anticipating and meeting their evolving needs.

DGG is also delivering very strong results, with 9 percent core growth for the year. We’re capturing market share in our pathology business, expanding our presence in next-gen sequencing and further building our oligo API business. During the year, DGG crossed the billion-dollar revenue threshold and now represents approximately 20 percent of Agilent’s business.

LSAG revenues declined 1 percent on a core basis as we faced some market headwinds. We remain committed to investing for future LSAG growth and market share gains.

Our new product development pipeline remains full. During the year, we introduced a number of innovative new products including the launch of a new family of ground-breaking gas chromatographs and molecular spectroscopy instruments. At this year's ASMS conference, we introduced several new differentiated LC-MS offerings, including the 6546 LC-QTOF and 6495C LC triple-quad systems.

As we head in 2020, our LSAG product portfolio and "go to customer" field team have never been stronger. Agilent continues to operate from a position of strength. We are well-positioned to capture market share.

Before I turn the call over to Bob, I want to remind you of the Agilent shareholder value creation model: deliver above market growth while expanding operating margins, along with a balanced deployment of capital with a priority on investing for growth. The result: delivery of superior earnings per share growth.

In driving value creation we've built a broader base of growth and a more resilient business model. You know, we were tested this year with economic and political uncertainties leading to subdued demand for new instrument purchases. Yet, we delivered 5 percent core growth, operating margins that improved 80 basis points and delivered another year of double-digit EPS growth. We deployed more than $1.5 billion in M&A and growth-focused capital investments.

On the M&A front, we're very pleased with the performance to-date of BioTek and ACEA BioSciences. We remain on the hunt for similar types of growth opportunities. I'm increasingly confident in the Agilent team's ability to pursue larger-scale acquisitions and deliver on value creation synergies. We continue to review potential acquisitions as part of our "building and buying" growth strategy.

Now more than ever, I'm convinced we're in an exceptionally strong position for the future. This is particularly relevant as we move into 2020 – a milestone for us at Agilent as we celebrate 20 years as an independent company. While uncertainties persist in some end-markets as we start fiscal year 2020, we're operating from a position of strength. We have built and will sustain our track record of delivering results, working as a One Agilent on behalf of our customers and shareholders.

I am very proud of the results the Agilent team delivered in the fourth quarter and throughout the year.

I know you've heard me say this before, but I truly believe the best is yet to come for Agilent, our customers and our investors.

Thank you for being on the call today and I look forward to your questions. I will now hand the call off to Bob. Bob?

<u>BOB MCMAHON</u>

Thanks Mike, and good afternoon everyone. In my remarks today, I will provide some additional revenue detail and take you through the fourth quarter income statement and some other key financial metrics. I'll then finish up with our guidance for 2020 and the first quarter. Unless otherwise noted, my remarks will focus on non-GAAP results.

As Mike indicated, our fourth quarter results were very good, with strong execution throughout the P&L.

For the quarter, revenue was $1.37 billion, reflecting core revenue growth of 4 percent. Reported growth was stronger at 6 percent. Currency negatively impacted revenue by roughly 2 points while acquisitions added 4 points to overall revenue reflecting the impact of a partial quarter of revenue from the BioTek acquisition in addition to earlier acquisitions.

From an end market perspective, Pharma, our largest market, had 7 percent core growth in the quarter, especially impressive off a tough 14 percent comparison from last year. Our large molecule biopharma business and CrossLab strength continued to drive strong results. Geographically, all regions grew with the strongest growth in the Americas and China.

And speaking of China, despite the debate regarding the pharma market and things like the "4+7" program, our pharma business in China grew double-digits this year.

Continuing, revenue in the environmental and forensics market grew 9 percent in the quarter. This is against a very tough compare of 17 percent growth last year. Growth was balanced between LSAG and ACG and continues to be driven by evolving regulations, especially concerning opioids.

Diagnostics and clinical revenue grew 7 percent during Q4 led by strength in our pathology and companion diagnostics businesses. Within pathology, continued expansion of our PD-L1 business was a key highlight.

Revenue from the chemical and energy end-market came in as expected with 1 percent growth. Declines in instruments were offset by strength in the CrossLab business.

Academia and government declined 4 percent against a tough compare of 10 percent growth last year. We still see the funding environments in academia and government remaining stable though.

And finally, consistent with expectations, food revenue declined 5 percent due to the China food market. Despite the year over year declines, we were encouraged that for the third quarter in a row, the run rate in China continues to be stable.

On a geographic basis, the Americas came in stronger than expected with 9 percent growth during the quarter led by strong results in the pharma, diagnostics and environmental markets.

Europe modestly exceeded our expectations, delivering a 4 percent growth rate with balanced strength across most markets and groups.

China came in as expected, declining in the low single digits against a very strong compare of 16 percent growth last year. Excluding food, China was up slightly. And wrapping up, Asia outside of China declined low single digits.

Now turning to the rest of the P&L, fourth quarter gross margin was 56.5 percent. This was down 120 basis points year-over-year primarily driven by product mix in LSAG, the startup costs at our Frederick, Colorado site and a higher revenue mix from ACG.

It's important to remember that while ACG gross margin is lower than the company average due to the services component, the ACG business has done a fantastic job of driving strong operating margin leverage. In fact, ACG's operating margin led the company for the quarter and the year. So ACG is not only helping to drive our recurring revenues, it is doing so at a very accretive rate.

In terms of operating margin, our fourth quarter margin was 25.1 percent, up 50 basis points driven by operating expense leverage and strong expense management. The quarter also capped off full year operating margin of 23.3 percent, an increase of 80 basis points over the prior year.

Now, wrapping up the income statement, our non-GAAP EPS for the quarter came in at 89 cents, up 10 percent versus last year and 3 cents higher than the top end of our guidance. And, as Mike mentioned, our full year earnings per share of $3.11 increased 11 percent versus last year.

Now turning to some other financial metrics. For the quarter, we generated $314 million in operating cash flow, acquired BioTek for $1.165 billion and returned $100 million to shareholders via dividends and share repurchases.

Lastly in the quarter, we took advantage of market conditions and refinanced $500 million of senior notes early, reducing our future interest costs. All in all, a very active quarter.

Before moving to next year's guidance, I want to recap how we have deployed capital this year. As we mentioned at the beginning of the year, we planned to focus our capital deployment toward growth-oriented assets and driving returns to our shareholders. To that end, we've deployed over $2.3 billion this year -- $1.4 billion in M&A for BioTek and ACEA, and more than $900 million in share repurchases and dividends. And, we ended the year with a very healthy balance sheet allowing plenty of capacity for further capital deployment.

Now, let's turn to our non-GAAP financial guidance for the 2020 fiscal year, beginning with full year guidance.

For the full year, we are expecting revenue to range from $5.50 to $5.55 billion, representing core growth of 4 to 5 percent and reported growth of 6.5 to 7.5 percent. Currency is estimated to negatively impact growth by 0.3 percentage points, with M&A contributing roughly 2.7 to 2.9 percentage points of growth for the full year.

From a group perspective, we expect ACG to sustain the momentum and deliver high single-digit growth driven by broad based strength. The DGG business is expected to grow at a high single-digit -- to low double-digit rate with our NASD Frederick facility ramping throughout the year. And, we anticipate a modest recovery for LSAG, roughly flat on a core basis.

Moving down the P&L, we expect modest operating leverage. And, also embedded in our forecast, we expect the “other income and expense” line to be $40 to $45 million in net expense, with year-over-year change driven largely by interest expense as we enter the year in a net debt position.

We expect our tax rate to improve by 50 basis points to slightly above 16 percent and our full year diluted shares outstanding to be approximately 312 million, essentially flat to Q4 of this year and reflecting only anti-dilutive share repurchases throughout the year.

All this translates to non-GAAP EPS expected to be between $3.38 and $3.43 per share, resulting in 9 to 10 percent growth on a reported basis.

Finally, we expect operating cash flow of approximately $775 -800 million. This includes a one-time tax outflow of roughly $230 million in the first quarter to transfer certain intangibles related to prior acquisitions. This tax will reduce our US transition tax dollar-for-dollar and will provide operational and tax benefits in the future.

We have also announced raising our dividend by 10 percent, continuing a streak of double-digit increases and providing another source of value to our shareholders.

Now turning to Q1 guidance.

For Q1, we are expecting revenue to range from $1.340 to $1.355 billion, representing reported growth of 4.3 to 5.5 percent and core growth of 2.5 to 3.5 percent. The lower organic growth in Q1 reflects the impact of the timing of Lunar New Year, which this year falls into our fiscal first quarter. We anticipate this adversely affecting the growth rate in the first quarter by roughly 1 point. In addition, the growth rate takes into account the Frederick site ramp that will occur over the year.

First-quarter 2020 non-GAAP earnings are expected to be in the range of 80 to 81 cents per share, representing reported growth of 5 to 7 percent. EPS growth in Q1 is lower than the full year based on the revenue growth, Frederick startup costs and certain share-based compensation costs that are expensed in the first quarter.

Before opening the call for questions, let me conclude by saying we are very pleased with the results our Agilent team was able to achieve this past year while continuing to focus on taking full advantage of opportunities in front of us. We are positioning our business toward stronger secular growth markets and driving higher recurring revenue streams. We clearly saw the results of this in 2019 and we enter fiscal year 2020 with a strong portfolio and with momentum.

With that, Ankur back to you for the Q&A.