Earnings Script
Conference Call
Q3 2022 – Final

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Thank you, and welcome everyone to Agilent's Conference Call for the third quarter of Fiscal Year 2022. With me are Mike McMullen, Agilent president and CEO, and Bob McMahon, Agilent senior vice president and CFO.

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

This presentation is being webcast live. The news release for our third quarter financial results, investor presentation and information to supplement today's discussion, along with a recording of this webcast, are available on our website at www.investor.agilent.com.

Today's comments by Mike and Bob will refer to non-GAAP financial measures. You'll 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 and references to revenue growth are on a core basis. Core revenue growth excludes the impact of currency, and any acquisitions and divestitures completed within the past 12 months. Guidance is based on exchange rates as of July 31.

As previously announced, beginning in the first quarter of Fiscal 2022, we implemented certain changes to our segment reporting structure. We have recast our historical segment information to reflect these changes. These changes have no impact on our company's consolidated financial statements.

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, Parmeet. And thanks everyone for joining our call today.

In the third quarter, we once again demonstrated the strength of our diversified business and the unstoppable One Agilent team. We delivered an excellent quarter – significantly exceeding our revenue and earnings expectations.

Revenues of $1.72 billion are up 13 percent core. This is on top of 21 percent core growth in Q3 of 2021.

Third quarter operating margins are 27.5 percent. Operating margins continue to expand and are up 150 basis points from last year.

Earnings per share of $1.34 are up 22 percent.

Our strong results in Q3, coupled with orders continuing to outpace revenues, highlight the ongoing strength of our diversified business. The momentum in our business continues and we are once again raising our outlook for the year.

Let's take a closer look at our Q3 results.

From an end-market perspective, our results were once again led by strength in our two largest markets, pharma and chemical and energy. Our largest market, pharma, grew 16 percent versus 27 percent a year ago. Within pharma, both the biopharma and small molecule segments grew double digits.

The momentum in our C&E market segment continues with Q3 growth of 22 percent. This is on top of 23 percent growth a year ago. The C&E market is being fueled by demand in chemicals along with strong secular demand and on-going investment within the advanced materials space.

We were also very pleased to achieve double-digit growth in the food and environmental and forensic markets, with both markets growing 11 percent.

In our last call, I shared our belief that that the business impacts of the Shanghai COVID-19 lockdown would be transitory. I also expressed that we remained confident about the ongoing strength of our business in China.

In Q3, the China team delivered 29 percent growth. These stellar results were driven by continued strong end-market demand coupled with a faster than expected recovery of production and shipment activity following the end of the Shanghai area lockdown. We are all so very pleased with this result, which highlights the customer focus, drive, and outstanding execution of the Agilent China team.

Strength in the Americas continued as we posted another quarter of double-digit growth on top of 32 growth percent last year. Our European business grew six percent against 23 percent last year, despite a two-point headwind from the curtailment of our operations in Russia.

In terms of business unit performance, the **Life Sciences and Applied Markets Group** generated revenue of $1.02 billion, up 18 percent on a core basis.

Growth was broad-based with continued strong demand for our LC and LCMS offerings where we posted high twenties growth. Our spectroscopy business grew low thirties driven by strength in the advanced materials market. Chemistries and consumables, cell analysis and our GC business each delivered double-digit growth in the quarter.

LSAG's end-market growth was broad-based, with particular strength in the pharma and chemical and energy markets. Our pharma results were driven by strength in the biopharma segment which grew more than 20 percent.

We had an excellent showing at the recent ASMS conference introducing several important LC/MS and GC/MS instruments and bio-pharma workflow solutions. These innovative and intelligent LC/MS and GC/MS systems have been designed to make the lives of our customers easier. The built-in instrument intelligence and a higher level of instrument diagnostics help maximize system uptime and improve lab productivity by allowing operators to focus on their analyses rather than on their instruments.

In addition, we introduced an industry-first hydro-inert source for GC-Single Quad and GC-Triple Quad instruments, enabling customers to seamlessly migrate from helium as a supplier gas to lower-cost hydrogen.

And rounding out the list of new products announced at ASMS, we introduced the Mass Hunter Bio Confirm 12.0 software – an integrated, compliant workflow targeted at the fast-growing oligo-based therapeutic development market.

These new products have already been well-received by customers and represent the latest addition to Agilent's history of leadership in mass spectrometry.

Our LSAG business also won some important awards during the quarter including the 6560C Ion Mobility LC/Q-TOF system winning the "Scientist Choice Award" for "Best New Spectroscopy Product."

Earlier this month, we also strengthened and broadened our advanced materials and biopharma portfolio with the acquisition of PSS -- Polymer Standards Service – a leader in polymer characterization. We're extremely pleased to welcome the PSS team and their technology to the Agilent family.

The **Agilent CrossLab Group** posted services revenue of $359 million. This is up 10 percent core. We grew 10 percent core, even as lab activity continues to ramp in China. Growth in services was again broad-based across services contracts, preventive maintenance, compliance, education and informatic enterprise services. Strong instrument placements and increased connect rates continue to be a driver for our services business as customers continue to see value in our ACG offerings.

Another critically important factor in our results is the scale and execution capability of Agilent's world class Global Service delivery organization in serving our customers to meet their needs. Agilent is seen as **<u>the</u>** trusted company to work with among our global customers.

The **Diagnostics and Genomics Group** delivered revenue of $340 million, up 3 percent core. This is versus a compare of 37 percent growth last year. The solid results in our clinical cancer testing and NGS businesses were partially offset by COVID-testing headwinds in our qPCR portfolio. In addition, the DGG business in China continues to ramp following the COVID-related shutdowns there.

NASD revenues were up modestly, in-line with expectations. As we noted last quarter, Q3 included the impact of a planned shutdown of our oligo manufacturing line in Frederick, Colorado. The shutdown in Frederick was for both routine maintenance and development of key elements of our Train B, our new manufacturing line that will increase our capacity $150 million plus, when fully ramped.

While we continue to make good progress on the construction of Train B, we have seen some supply chain related delays and are now targeting a mid-year 2023 “go-live” -- a slight delay. We see continued strong demand for Oligo based therapies as the number of approved drugs continue to increase and the pipeline of drugs in development are targeting disease states with larger patient populations. We are more confident than ever in the long-term trajectory of the market and our business.

In addition to these highlights, I’d like to also point out the recent release of Agilent’s 2021 ESG report. While we’ve always published our progress in sustainability and addressing societal needs, this year we’ve taken our approach to the next level. We address these issues in a new format that for the first time that looks specifically at our progress in the areas of environmental, social and governance issues.

We hope you have a chance to review our progress in ESG by checking out the report on the Agilent website and learning more about how we’re executing on our mission to advance the quality of life.

Agilent’s Q3 results again point to the strength of our diversified business and the outstanding execution ability of the Agilent team. We continue to bring innovative, differentiated new offerings to the marketplace. Acceleration in digital order growth continues, as well as new customer acquisition.

In addition, as we started 2022, we undertook a bold move to create a One Agilent Commercial organization to further drive customer focus and growth. The strength of our portfolio and the continued strong execution by our One Agilent Commercial organization make a powerful combination – and you see it in the results we're delivering. Customer satisfaction hit another all-time high this quarter. We continue to outgrow the market.

As a result of our strong Q3 performance and continued momentum, we are once again raising our full-year revenue and EPS guidance. Bob will share more of the specifics.

It's an exciting time at Agilent – with the best yet to come.

Thank you for being on the call today and now, I will hand the call off to Bob. Bob?

Bob McMahon

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

We are extremely pleased with our Q3 performance. Results were above expectations, and we expect that strength to continue in the fourth quarter.

Q3 revenues were $1.72 billion, up 8.4 percent on a reported basis and up 13.2 percent core. FX was a 4.8 point headwind to growth or $76 million. Pricing for the quarter contributed over 3 points of growth year on year and improved sequentially.

The performance was broad based, as all end markets and regions grew during the quarter.

As we mentioned last quarter, the COVID-related lockdowns in China deferred an estimated $50 to $55 million in revenue from Q2, and we forecasted that revenue would be recovered during the rest of the calendar year. Our team in China did a fantastic job ramping production and shipments faster than expected following the shutdowns. We estimate over half of that deferred total was delivered in Q3, exceeding our expectations. Given this strong performance, we now expect the remainder will be delivered in Q4, which is an acceleration from our thinking from last quarter.

The acceleration of the COVID-related shutdown recovery in China contributed to an already strong Q3 for the company. For perspective, we estimate the total business grew double digits, excluding the accelerated recovery.

As Mike mentioned, earnings per share of $1.34 are up 22 percent from a year ago, representing strong incremental flow-through of the better-than-expected revenue growth. This performance is against our most difficult comparison of the year as EPS grew 41 percent in Q3 of last year.

Now let me dive a little deeper into the end markets.

Our largest market, **pharma,** was up 16 percent, exceeding our expectations. Biopharma grew 18 percent and small molecule was up 14 percent. Biopharma is a focus area for us and now represents 38 percent of our overall pharma business. We expect that ratio to continue to climb over time. In addition, all three business groups grew double digits in the pharma segment. And our LC portfolio continues to perform well, growing 25 percent in this important market for us.

Chemical and energy continued to show strength growing 22 percent during the quarter, driven by the chemicals and advanced materials segments of this market. We saw strength in plastics and packaging for chemicals, and ongoing demand in advanced materials coming from the markets for semiconductors and batteries.

In the **food** segment, we achieved growth of 11 percent on top of 12 percent growth a year ago. Strength in the food market was led by the Americas and China.

Our **environmental and forensics** market also grew 11 percent during the quarter driven by the Americas and China. In the Americas, we saw increased funding to support PFAS testing while China experienced faster than expected recovery post the Shanghai shutdowns for GCs and GCMS.

The **academia and government** market grew 5 percent on top of a 12 percent comparison to last year, in line with expectations.

And rounding out the review of our end-markets, our business in the **diagnostics and clinical** market grew 2 percent against a very strong 28 percent compare versus last year. While not material at the Agilent level, this market did experience some headwinds associated with COVID-related revenues being lower than last year. Excluding this, the growth would be mid-single digits in this quarter.

On a geographic basis, China led the way with 29 percent growth, driven by underlying demand and a faster than expected recovery following the COVID-related lockdowns. And looking forward, demand in China continues to be strong.

The Americas grew 11 percent, another strong showing and Europe grew 6 percent, which exceeded expectations.

Now turning to the rest of the P&L, our team continues to execute at a very high level. Third quarter gross margin was 56.4 percent, up 50 basis points from a year ago as pricing actions, volume and productivity helped offset inflationary pressures tied to on-going supply chain challenges and higher logistics costs.

Operating expense leverage driven by the strong top line and continued attention to cost management helped deliver very healthy margin improvements. Our operating margin was 27.5 percent, up 150 basis points from last year.

Below the line, our tax rate was 14 percent for the quarter, as expected, and we had 299 million diluted shares outstanding.

Looking at cash flow and our balance sheet, we generated operating cash flow of $326 million in the quarter while investing $82 million in capital expenditures during Q3, driven by our NASD expansion.

During the quarter, we also repurchased $323 million worth of shares.

We paid out $62 million in dividends in Q3, returning a combined total of $385 million to shareholders in the quarter.

Year to date, we have purchased over $1 billion of shares. Given the on-going strength of the business, we believe this is a very good investment.

Our balance sheet continues to remain healthy with a net leverage ratio of 1.0.

Now, let's move to our outlook for the full year and fourth quarter.

We now expect revenues for the full year to be in the range of $6.750 to $6.775 billion. This takes into account our Q3 results and an improved outlook in Q4, partially offset by an additional $40 million headwind associated with the strengthening of the dollar. This represents core revenue growth of between 9.9 and 10.3 percent.

We are also raising our EPS guidance for the year to a range of $5.06 to $5.08, representing 17% growth year-on-year.

This translates to Q4 revenue in the range of $1.750 billion to $1.775 billion. Core growth is expected to be in the range of 10.3% to 11.8%, while exchange rates will be a 5-point headwind and M&A will contribute 0.1 points.

And closing out our Q4 guidance, non-GAAP EPS is expected to be in the range of $1.38 to $1.40, up 14 to 16 percent versus the prior year. This is based on a 14 percent tax rate and 299 million diluted shares outstanding.

The Agilent team once again performed extremely well in Q3, delivering strong results, driving excellent execution, and building a strong foundation for the future. Our diversified business and most importantly our team, have put us in an excellent position to again deliver strong results in Q4.

And now, back to Parmeet as we take your questions. Parmeet?

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