Agilent Technologies Second Quarter Fiscal 2023
Conference Call Prepared Remarks

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Thank you, and welcome everyone to Agilent's conference call for the second quarter of Fiscal Year 2023. 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 second 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. Our guidance is based on forecasted currency exchange rates.

During this call 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.

In our call today, I'd like to first cover our second quarter results. I will then, provide some insight into the recent market dynamics that we are seeing and how this has translated into lower expectations for the second half of this year. I will then turn things over to Bob for more detail on the quarter and outlook before returning for some brief closing comments.

In an increasingly challenging market environment, the Agilent team delivered very solid results in the second quarter. Revenues of 1.72 billion dollars are up 9.5 percent core, above our expectations, with growth across all end markets and regions. Our results are driven by an innovative and broad portfolio, a differentiated customer experience, and outstanding execution by the Agilent team.

Operating margins for the quarter are 25.6 percent, up 30 basis points.

Earnings per share of $1.27, are up 12 percent.

Highlights from an end market perspective include our two largest markets, pharma and chemicals and advanced materials performing very well in the quarter.

Our pharma business grew six percent on top of 13 percent growth last year. Pharma was led by biopharma which grew 16 percent driven by lab services, consumables, and our NASD business, while small molecule declined 1 percent.

In previous calls we've talked about the small molecule replacement cycle and that the exceptional double-digit growth rates we've seen the past two years would eventually moderate, which is what we started to see this quarter.

Our chemicals and advanced materials business delivered strong results once again, growing 16 percent. The advanced materials segment grew more than 20 percent and the chemicals and energy segment grew double digits.

On a geographic basis, 32 percent growth in China exceeded our high expectations. While the compare was an easier one, even adjusting for the COVID lockdowns in Shanghai a year ago, we still achieved double digit growth in China. In addition, Europe delivered 5 percent core growth while the Americas grew 3 percent, albeit against a tough compare of 13 percent a year ago.

Looking at our performance by business unit, the **Life Sciences and Applied Markets Group** delivered revenues of 968 million dollars, up 10 percent core. Our strong results were aided by backlog conversion across our instrument platforms.

Our LC and LCMS products continued to lead the way with 16 percent growth in the quarter, with strength across all end markets. Continued demand for lab consumables led to 13 percent growth in that business as well.

During the quarter, we added additional strength to our LCMS product line by acquiring e-MSion, and their innovative electron capture technology. E-MSion technology allows researchers to develop biotherapeutic products more quickly for treating disease.

Agilent's LSAG team continued to bring several innovative new products to market, including enhancements to our Bravo NGS automation, Cary UV-Vis, and cell analysis NovoCyte systems. Many of these enhancements are specifically focused on serving our customers in the biopharma market.

The **Agilent CrossLab Group** posted revenue of 387 million dollars. This is up 13 percent core driven by strong revenues from service contracts. ACG's growth was broad-based, representing ongoing resilient demand for our services.

We continue to see many opportunities for future growth given our services portfolio. In particular, the benefits of our service offerings as they help customers drive productivity in the lab, are even more relevant in today's challenging environment. Our strong and trusted customer support is also helping us to drive share gains and acquire new enterprise customers.

The **Diagnostics and Genomics Group** delivered revenues of 362 million dollars, up 3 percent core. Strength in our pathology and NASD businesses drove growth, partially offset by general industry-wide weakness in genomics.

NASD posted another strong quarter growing in the high 20s. Our Train B manufacturing expansion remains on-track to come online later this quarter while construction has already started on the next phase of expansion.

Overall, we wrapped up Agilent's first half of fiscal 2023, with double digit core growth in both revenue and earnings per share.

However, continued macro-economic uncertainty coupled with stresses in the banking system have accelerated a more conservative approach from our customers across the globe. This has primarily affected CapEx-related instrument spending across most end-markets but is centered mainly in the pharma markets in the U.S. and China.

Early-stage biotech customers, while a small part of our revenues, dramatically scaled back purchases as funding and liquidity challenges drove cash conservation.

Outside of these early stage biotechs, the order funnel continues to be healthy, but it is taking a longer time for orders to be approved, slowing deal velocity and generation of new orders.

We expect this constrained capital environment to remain in place throughout the course of our fiscal year.

Because of these factors, we are taking a more cautious approach to the second half and have revised our forecast downward.

As a result, we now expect core revenue growth to be in the range of 3 to 4.5 percent with EPS growing faster than revenue at 7 to 8 percent.

Our operating margins increased in the first half of the year, and we're doubling down on delivering cost efficiencies and increasing productivity to drive more leveraged earnings growth in the second half. As we've done in the past, we'll generate additional cost savings so we can continue to invest in innovative new solutions and support for our customers as we enable future profitable growth.

We have an unstoppable One Agilent team that is battle-tested. They consistently execute at an extremely high level and are well-prepared to deal with any challenges they may face.

Bob will provide the details on our outlook for Q3 and the full year, but overall, we remain convinced our strategic focus, customer service and unmatched execution by the Agilent team remain the keys to our continued success.

After Bob delivers his comments, I will be back to provide some closing remarks. And now, Bob, over to you.

Bob McMahon

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

Q2 revenue was 1.72 billion dollars, exceeding our expectations. Revenues were up 9.5 percent core and up 6.8 percent on a reported basis. Currency was a 2.8-point headwind, while the M&A contribution was minor, as expected. In Q2, we continued to leverage our backlog and exited the quarter with our backlog at a normalized level.

As Mike mentioned, our 2 largest end markets performed well in the quarter. **Pharma** our largest end market, posted 6 percent growth led by biopharma, while small molecule declined slightly.

Chemicals and advanced materials continued to drive strong secular growth of 16 percent during the quarter on top of 9 percent growth last year. The chemical and energy sub-segments of the market are doing well, with the advanced materials market continuing to lead the way. As in past quarters, semiconductors and batteries are driving demand in this space.

Looking at the rest of the end markets, the **food** market grew an impressive 21 percent during the quarter, driven by very strong growth in China. We also saw strong results in the Americas and Europe.

The **academia and government** market was up 11 percent led by China and Europe as the funding environment continues to be constructive.

Our business in the **diagnostics and clinical** market grew 6 percent on top of 5 percent growth last year. Pathology again led the way for us here, partially offset by genomics.

The **environmental and forensics** business grew two percent led by China and the Americas while Europe declined. The Americas slowed after a very strong Q1, but still delivered mid-single digit growth.

On a geographic basis, the China team exceeded our expectations, delivering 32 percent growth following last year's COVID lockdowns in Shanghai. As we mentioned last year, the COVID related lockdowns deferred roughly $55 million in Q2 from last year into the third and fourth quarters. So, while Q2 is an easier compare, we will have much tougher compares in China going forward.

Taking out the effects of the lockdown this quarter, we estimate China still grew double digits, so very solid results by our China team. The rest of Asia grew high single digits, better than expected.

The Americas grew 3 percent with growth across all end markets. From a group perspective, both ACG and DGG grew while LSAG unexpectedly declined low single digits as we started to see the accelerated effects of the slowing capex environment.

Europe grew 5 percent, in line with expectations led by pharma and CAM.

Now moving down the P&L, second quarter gross margin was 55.3 percent, down 40 basis points from a year ago, largely due to an unfavorable product mix. The benefit of pricing was as expected. Below gross margin, we had good cost discipline in SG&A which drove our operating margin to 25.6 percent, up 30 basis points from last year.

Below the line, we benefited from higher than planned interest income due to higher interest rates and strong cash flow. Our tax rate was 13.75 percent for the quarter, and we had 297 million diluted shares outstanding, both as expected.

Putting it all together, Q2 earnings per share were $1.27, up 12 percent from a year ago – a very good result combined with our 9.5 percent core topline growth.

During the quarter, operating cash flow was very strong, generating $398 million dollars. This result was helped in part by deferring estimated U.S. tax payments of roughly 60 million dollars to our fiscal fourth quarter. This is due to the payment deferral relief made available by the IRS to taxpayers in designated counties affected by the winter storms in California.

We returned $151 million to shareholders - $66 million through dividends and repurchased shares worth 85 million dollars, while also investing 57 million dollars in CapEx, continuing our successful, balanced approach to capital deployment.

Our strong balance sheet is even more of an asset in this market environment and remains very healthy as we ended the quarter with a net leverage ratio of 0.7 times.

And earlier this month. Moody's upgraded Agilent's investment grade rating on our corporate long-term debt to Baa1. This action is an important recognition of Agilent's financial strength.

Now on to the revised outlook for the year and guidance for Q3. For the full year, we now expect revenue in the range of 6.93 to 7.03 billion dollars. This represents reported growth of 1.2 to 2.7 percent and core growth of 3.0 to 4.5 percent. Currency is expected to be a headwind of 1.9 points while M&A will contribute 0.1 points of growth.

In addition to revising our guidance, we have increased our guidance range for the second half of the year to reflect a wider range of possible outcomes. For modeling purposes, I would encourage you to use the midpoint of our guide.

Our updated guidance reflects a more constrained capital market, primarily impacting our instrument business. The outlook for our recurring revenue businesses remains largely unchanged. From an end market perspective, the market most impacted is pharma where we are now expecting full year growth of low single digits, down from high single digits. And from a geographic perspective we see impacts focused in the US and China.

With the change in revenue, we now expect full year fiscal 2023 non-GAAP earnings per share to be between $5.60 and $5.65, representing growth of 7 to 8 percent. As with revenue, I encourage you to model at the midpoint of our guidance.

Now turning to Q3, we expect revenue in the range of 1.640 to 1.675 billion dollars. This represents a decline of 4.5 percent to a decline of 2.5 percent for both reported and core revenue. This is on top of a tough compare of 13 percent growth last year. Adjusting for the China deferral in Q3 of last year would add roughly 200 basis points to both reported and core growth in the quarter. Currency and M&A impact in Q3 are minimal and are expected to offset each other.

Third quarter non-GAAP earnings per share are expected to be between $1.36 and $1.38, representing growth of 1.5 to 3.0 percent versus the prior year.

We are pleased with the first half performance and while we are facing a more difficult market environment than we were estimating a quarter ago, I am confident our team will continue to deliver for our customers.

Thanks for being on the call. And now, I will turn over things back to Mike for some closing comments before we take your questions. Mike?

Mike McMullen

Thanks Bob.

During our Q4 ’22 call in November, I shared with you that I believe, “Agilent has the right growth strategies, the right team and right culture to continue delivering strong, above market results.” My belief remains unchanged. Our customers know we are reliable, resilient, and extremely quick in reacting to meet their needs. The Agilent team continues to work hard to earn their trust.

While the near-term outlook points to continuing challenges in the market, we remain confident in the long-term growth prospects in our end markets and in our ability to continue to grow faster than the market. Agilent is a trusted partner that our customers know they can rely on.

Despite the current market environment, I remain confident in our ability to deliver on our shareholder value creation model.

Our core values and approach haven't changed. Our focus on investing for growth, providing the industry's best customer support, our innovation prowess and being a great place for our team to work with a differentiated company culture, are here to stay. They remain Agilent's formula for long-term success.

Thank you. And now over to you Parmeet to lead the question-and-answer session. Parmeet?

Parmeet Ahuja

Thanks Mike. Sarah if you could please provide instructions for the Q&A now.

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