Medtronic

FINAL

Q3 FY24
Earnings call commentary

Ryan Weispfenning

Good morning, and welcome to Minnesota, where we finally have some snow. I'm Ryan Weispfenning, Vice President and Head of Medtronic Investor Relations, and I appreciate that you're joining us this morning for our fiscal '24 third quarter video earnings webcast.

Before we go inside to hear our prepared remarks, I'll share a few details about today's webcast:

- Joining me are Geoff Martha, Medtronic chairman and chief executive officer, and Karen Parkhill, Medtronic chief financial officer. Geoff and Karen will provide comments on the results of our third quarter, which ended on January 26, 2024, and our outlook for the remainder of the fiscal year. After our prepared remarks, the executive VPs covering our segments will join us, and we'll take questions from the sellside analysts that cover the company. Today's program should last about an hour.
- Earlier this morning, we issued a press release containing our financial statements and divisional and geographic revenue summaries. We also posted an earnings presentation that provides additional details on our performance. The presentation can be accessed in our earnings press release or on our website at InvestorRelations.Medtronic.com.
- During today's program, many of the statements we make may be considered forward-looking statements, and actual results may differ materially from those projected in any forward-looking statement. Additional information concerning factors that could cause actual results to differ is contained in our

periodic reports and other filings that we make with the SEC, and we do not undertake to update any forward-looking statement.

- Unless we say otherwise, all comparisons are on a year-over-year basis, and revenue comparisons are made on an organic basis, which excludes the impact of foreign currency and third quarter revenue in the current and prior year reported as "Other," which stems from prior business separations. There were no acquisitions made in the last four quarters that had a significant impact on total company or individual segment quarterly revenue growth.
- References to sequential revenue changes compare to the second quarter of fiscal '24 and are made on an "as reported" basis, and all references to share gains or losses refer to revenue share in the fourth calendar quarter of 2023 compared to fourth calendar quarter of 2022, unless otherwise stated.
- Reconciliations of all non-GAAP financial measures can be found in our earnings press release or on our website at InvestorRelations.Medtronic.com.
- And finally, our EPS guidance does not include any charges or gains that would be reported as non-GAAP adjustments to earnings during the fiscal year.

With that, let's head into the studio and hear about the quarter.

Geoff Martha

Hi everyone and thank you for joining us today. Our momentum and solid execution continued this quarter as we establish a track record of consistently delivering mid-single digit organic revenue growth. Diabetes took another step forward with double digit growth, supported by a return to growth in the US. I'd also note the particular strength we saw in multiple businesses like Core Spine, Cardiac Surgery, Structural Heart, and Cardiac Pacing. And, we had strong growth across international markets, as we expand access to our innovative healthcare technologies all around the globe.

At the same time, we've had a rapid cadence of new product approvals, and we're continuing to differentially invest in our pipeline of highest growth opportunities. We're advancing innovative core technologies like robotics, AI, and closed loop systems. And with five AI products already FDA-approved, we're leading the way in bringing the tech into medtech.

We also continue to make progress on our comprehensive transformation of the company. We're incorporating a performance-driven culture that's based on execution, speed, and playing to win. And we're leveraging our scale to drive efficiencies. So when you look at our financials this quarter, you're seeing the early results of our focus on restoring earnings power and converting our earnings into strong cash flow. And we're using that cash to both invest in high-return opportunities and return value to our shareholders.

So we're executing and delivering. And we expect to continue over the coming quarters and years given our momentum… our ongoing transformation… our breakthrough innovation… our exposure to strong, secular growth markets… and our numerous catalysts across the business.

Now before we get into the details of our Q3 results, I do want to mention that we provided a portfolio management update this morning on our Patient Monitoring and Respiratory Interventions businesses. After a comprehensive review, we have decided to exit our unprofitable ventilator product line, and retain and bring together our remaining PMRI businesses into one business, which we're calling Acute Care and Monitoring.

Now we have determined it is in the best interest of Medtronic, its stakeholders, and the ACM business, both near-and long-term, to exit vents because of its increasing unprofitability and market preference shift to lower acuity ventilators. Now as we exit vents, I want to recognize the strong legacy of our business and the Puritan Bennett™ brand. And we're committed to serving the needs of our customers and honoring our ventilator service contracts. And I also want to thank the employees in our ventilator business, who played an incredible role during the pandemic to dramatically expand production to get ventilators to the communities around the world that needed them. And while we exit, we do believe that existing manufacturers can meet the customer demand for new ventilators going forward.

Now at the same time, we decided to retain and refocus the remaining PMRI businesses. Three main factors have driven this decision. First, we have strong conviction in our ability to lead and drive growth in Acute Care & Monitoring given our improved competitive position and our ability to properly fund this business with savings from exiting vents. Second, the importance of data in this space is changing rapidly. It's becoming the basis of innovation, and this fact further improves our competitive differentiation. And lastly, as a company more broadly, we continue to prioritize profitable innovation-driven growth and category leadership, and ACM can deliver both. That does not mean we will shy away from additional portfolio moves going forward, but the bar is high for any strategic activity that dilutes our focus on our profit and growth.

So when you take these decisions together, we're able to provide increased investment for Acute Care and Monitoring – using the savings from vents and bringing two businesses together – all without creating dilution to our P&L

Now let's get into the details behind our Q3 results. We continue to look at our portfolio in three categories: Established Market Leaders, Synergistic, and Highest Growth businesses. And this quarter, all 3 grew in-line with our expected growth algorithm. Our Established Market Leader and Synergistic businesses grew mid-single digits. While our Highest Growth businesses posted high-single digit growth, and we expect their contribution to our overall growth to further accelerate in the quarters ahead.

Now looking first at the Established Market Leaders… combined, they made up just under half of our revenue and grew 4%.

Starting with **Cranial & Spinal Technologies**… we're driving consistent, above-market growth on the continued adoption of our AiBLE™ ecosystem. CST delivered high-single digit growth in Core Spine, mid-teens growth in Biologics, and high-single digit growth in Enabling Technology. We had strong, double digit unit growth in StealthStation™ navigation, O-arm™ imaging, and Mazor™ robotic systems, a leading indicator for future growth in this business. We also continue to see strong adoption of UNiD™ Adaptive Spine Intelligence, our integrated, AI-based surgical planning solution.

Now with AiBLE™, we're offering a complete, robust ecosystem of enabling technologies and associated implants for Spine surgeons. Our global footprint, which includes over 10 thousand systems, is over 4 times greater than the nearest competitor. And with this scale... and extensive and rapidly increasing install base, we're transforming the Spine industry. We are leading the way. As more surgeons adopt our integrated Spine technologies, and in an environment where there is disruption from consolidation, we're attracting the best sales teams to Medtronic to grow and expand our business.

Next, in **Surgical**, we grew 3%. Our Wound Management business won share, growing in the high-teens on the strength of our V-Loc™ barbed sutures. We also had solid, mid-single digit growth in Hernia products, as we won share in synthetic permanent mesh with our ProGrip™ platform. And as expected, our Surgical growth continued to have a modest impact from declines in bariatric surgery. Now we still believe this impact will be temporary as more patients become eligible for surgery, and as patients seek a more permanent treatment to weight loss.

To wrap up our Established Market Leaders… **Cardiac Rhythm** also grew 3%, driven by high-single digit growth in Cardiac Pacing. Our Micra™ leadless pacemakers continue to post strong results, growing 15%, driven by the launch of our next-generation Micra™ AV2 and VR2 devices. We're also benefiting from the adoption of Conduction System Pacing, an alternative to traditional single- or dual-chamber pacing. Our 3830 lead, the only one on the market approved for Conduction System Pacing, continued to grow strong double digits.

In CRM, we also began training and the limited launch of our Aurora EV-ICD™. Now we expect the EV-ICD to reaccelerate our Defibrillation Solutions growth in the coming quarters. As I've shared with you in the past, Aurora is a gamechanger in the ICD space. It delivers the benefits of a traditional ICD – including similar size, longevity, and pacing features – but without the leads in the heart or veins. And these benefits can be realized with <u>one</u> device… and only <u>one</u> implant procedure. We expect our advantages will not only displace the competitor's device, we will expand the population far beyond the existing segment and be a strong growth driver for CRM.

Now... turning to our Synergistic businesses… Combined, they grew mid-single digits in Q3, and I'll highlight some of the drivers here. Let's start with **Aortic**, which grew 13% on supply recovery and continued momentum of our Endurant™ AAA franchise. **Cardiac Surgery** grew 10%, driven by strength in perfusion and cannulae, ECLS oxygenators – given competitor quality issues – and the strong sales in international markets of our Avalus™ surgical valve. **Coronary** grew 7%, driven by double digit growth in both guide catheters and balloons... and we increased our drug-eluting stent share in the US and in Europe on the continued rollout of our Onyx Frontier™ drug-eluting stent.

Now turning to businesses in our Highest Growth Markets… As I mentioned earlier, together, these business grew in the high-single digits this quarter, and we expect their contribution to our growth to accelerate going forward.

Diabetes led the way, growing double digits on the global adoption of our game-changing MiniMed™ 780G system. We're seeing strong sequential momentum, growing 5% over the prior quarter. Our customer base is growing sequentially, and we're driving more revenue per customer.

In the US, we not only returned to growth, we grew mid-single digits, driven by nearly 50% revenue growth in insulin pumps. We doubled our new users year-over-year, attracting those on multiple daily injection as well as users of competitors' systems. Users are choosing 780G for the outcomes it delivers... with intensive-insulin users, these outcomes matter, and the 780G is highly differentiated. It's the only AID system to automatically adjust and correct sugars every 5 minutes. It offers flexible glucose targets as low as 100, and features our proprietary Meal Detection™ technology. This leads to high time-in-range for users. And this type of glycemic control is coming with less effort and burden, as users realize the relief that comes from spending more time in automation with our SmartGuard™ technology. It's worth pointing out that in a recent third-party survey of nearly 2,000 US diabetes pump users, the 780G scored #1 in overall pump satisfaction. And among type 1 CGM users, our Guardian™ 4 sensor mirrored competitors' sensors in overall satisfaction.

And during the quarter, we secured CE Mark for our Simplera Sync™ sensor for use with the 780G, and we look to begin the limited release this spring. And in the US, we're planning to submit the 780G with Simplera Sync™ to the FDA in the first half of this calendar year. Simplera Sync™ is half the size of our current sensor. It has a disposable design, and is much easier to put on.

Now we've been driving the Diabetes turnaround for some time, and I got to tell you, it certainly feels really good to return to double digit growth... but we're not finished here. There is definitely more to be done as we work to bring to market an even more robust ecosystem of differentiated technology for people living with diabetes, including next-generation durable pumps, smart pens, patch pumps, sensors, and algorithms. And as the Intensive Insulin Management space moves to using Smart

Dosing, through either AID or Smart MDI, we expect an acceleration in the growth contribution from our Diabetes business.

Now turning to **Cardiac Ablation Solutions**, we delivered 11% growth in international markets, including 9% growth in Western Europe. Our strong international growth, as well as our overall performance, continues to be driven by our leading Arctic Front™ cryo solution, as pulsed-field ablation is still in the early stages.

We're seeing, though, a lot of enthusiasm in the market for our PFA products. In Europe, we're the only company with PFA offerings for both the single-shot and the focal segments. And in single shot, we have now started the limited market release of our PulseSelect™ PFA system here in fiscal Q4. And we are seeing very efficient procedures, and after just a couple of cases, and so the learning curve is really short. The catheter handling and maneuverability has been excellent due to its small shaft and our custom 10 French bi-directional sheath. Clinicians are also reporting no noticeable muscle contraction with our PFA product, which is beneficial for patient experience.

In focal, we continue to ramp manufacturing of the Affera™ mapping system and Sphere-9™ catheter and remain in limited market release in Europe. Sphere-9™ is the only catheter that can perform both pulsed field ablation and radiofrequency ablation, and high-density mapping. It's really an all-in-one catheter.

In the US, our CAS business declined in the quarter. We faced the first full quarter of competition in the cryoablation space, which is a space we created and had been the only player. In addition, many customers actually held back purchases as they awaited the launch of our PulseSelect™ PFA catheter, which is now commercially available. We do expect to improve from here, as we roll out the recently approved next-generation Nitron CryoConsole™ and PulseSelect™, the only PFA catheter FDA approved for both paroxysmal and persistent AF. And in addition to the European feedback, clinicians have consistently commented on how well it's visualized, and how easily it connects to their mapping system.

So we're also making progress in bringing our Affera™ mapping system and Sphere-9™ catheter to the US… with the last patient follow-up in our SPHERE Per-AF pivotal trial now completed. We expect to see the results at a medical meeting in the first half of this calendar year.

You know with an $8 billion market size, expanding our share in this underpenetrated Cardiac ablation space is a big opportunity for us. We expect our growth profile to improve over time – first moving toward market growth and then winning share – as we bring our rich pipeline of innovation to patients who need this technology.

In **Neurovascular** this quarter, we grew high-single digits when you exclude sales in China where the market is subject to volume-based procurement. We continued to have strong double digit growth in Flow Diversion globally. This is being driven by our innovative Shield Technology™ for treating brain aneurysms, which is available on both Pipeline™ Flex and Vantage™ flow diverters.

In **Robotic Surgical Technologies**, we continued growing the install base for our differentiated Hugo™ robotic system in international markets. In the US, our Expand URO pivotal trial continues to enroll, and we expect to have first enrollment in our Hernia trial soon.

We expect Hugo™, equipped with advanced digital capabilities, to be a meaningful growth driver for us in the years ahead. We believe surgeon preference for our open console and modular design… our leading position in minimally invasive surgery and instrumentation… our connected digital ecosystem and data-enabled insights, along with our world-class surgical training program and partnerships, will meaningfully advance the low penetration of robotic surgery around the world.

Now turning to **Structural Heart**… we grew high-single digits in the quarter, including mid-single digits sequentially, as we see ongoing adoption of Evolut™ FX and its improved design and market-leading valve performance. In Europe, where FX was launched for the first full quarter, we grew double digits. And Japan grew in the low twenties on the continued adoption of FX.

I'm pleased to share the news today that we have submitted Evolut FX+ to the FDA for approval. FX+ has three windows in the frame to allow easy coronary access, while providing the same dependable valve performance of our Evolut platform. And we were also pleased to hear that 1-year trial results of our SMART trial will be presented as a late breaker at ACC on April 7. We're excited to see the results and are looking forward to having both FX+ and the SMART trial -- as well as the continued strength of our 4-year Low Risk data -- as catalysts for our Structural Heart business.

Now with that, let's go to Karen for a deeper look at our Q3 financial performance and our fiscal '24 guidance raise. Karen?

Karen Parkhill

So looking at our financials, our third quarter was another quarter where we delivered on our commitments. Our revenue grew 4.6%, ahead of expectations. And, adjusted EPS was $1.30, 4 cents above the midpoint of our guidance range. We attribute the beat to stronger than expected revenue growth and gross margin, offset by 4 cents from greater than anticipated currency impact, primarily from the devaluation in the Argentine Peso in December.

We're delivering durable mid-single digit revenue growth and have now for several quarters. As Geoff mentioned, international markets were an important driver for us. Our non-US developed markets grew 6%, including 8% growth in Western Europe and 7% in Japan. In fact, we had double digit growth in several of our businesses across both of those regions.

Emerging Markets grew 10%. We had high-teens growth in the Middle East & Africa, and mid-teens growth in South Asia. China grew low-double digits, as some of the VBP we expected there continues to be delayed. And Eastern Europe grew in the low-single digits, given Russian sanctions.

In the US, we grew 2%. We have several new product approvals that are in the earliest stages of their launches and expect those to positively impact our US growth over the next couple of quarters and beyond.

Looking down the P&L, we delivered a strong quarter. Both our adjusted gross and operating margins were ahead of expectations. Our adjusted gross margin of 66.1% improved year-over-year, overcoming a 60 basis point headwind from foreign exchange and continued elevated inflation. We attribute the favorability primarily to the delayed China VBP and lower freight costs. We also continue to see traction from our pricing efforts, and an early benefit from our comprehensive COGS efficiency efforts.

While our adjusted operating margin of 25.2% declined 70 basis points, it was entirely driven by currency. In fact, operating margin on a constant currency basis was up 160 basis points, from improvement in gross margin and strong SG&A leverage, as we continue to drive efficiencies across the enterprise.

Below the operating margin line, our adjusted tax rate was a little higher than anticipated, mainly due to the jurisdictional mix of profits. On the flip side, income on our investments was also a little better-than-expected with higher rates.

It's worth noting -- that while our adjusted EPS was flat year-over-year, it grew 8.5% on a constant currency basis from the leverage we drove down the P&L. We also significantly improved our free cash flow and conversion in the quarter.

Now, turning to guidance…

Given our top- and bottom-line beat and continued strength in our underlying fundamentals, we're raising our full year revenue and EPS guidance. We now expect full year organic revenue growth of 4.75 to 5%. For the fourth quarter, we're expecting organic revenue growth to be in the range of 4 to 4.5%. On a comp adjusted basis, this is an acceleration from the third quarter, as we continue to ramp our recent product launches. With the exit of ventilators that we announced today, we are moving the associated revenue to the Other segment starting in the fourth quarter. As is the case with all revenue in Other, we will exclude it from our organic revenue growth, and additional details can be found in our third quarter earnings presentation. Regarding currency, based on recent rates, we would see a full year revenue impact in the range of an unfavorable $15 million to a favorable $35 million, including an unfavorable impact of $70 to $120 million in the fourth quarter.

On the bottom line, with the beat in the third quarter, we're raising our full year EPS guidance by 4 cents at the midpoint to a new range of $5.19 to $5.21. I'd point out that, given our durable performance, we've been able to increase this guidance by 15 cents at the midpoint from where we initially started the year.

For the fourth quarter, we expect adjusted EPS of $1.44 to $1.46. And, regarding currency, based on recent rates, we're seeing an unfavorable impact of 7% on full year EPS, including an unfavorable 5% impact in the fourth quarter.

Lastly, while we'll give our fiscal year '25 guidance on our earnings call in May after we finish our planning, I want to share our early thoughts. You've seen us deliver durable revenue growth for several quarters, and we expect that to continue. Down the P&L, inflation, currency, and tax are currently headwinds to earnings growth, and we expect to continue to increase our investments in R&D. That said, we're very focused on driving offsets where we can and improving the earnings power of the company.

And, regarding the portfolio management decisions we announced today… while the Street's FY25 numbers didn't yet reflect the potential separation, with today's decision, we're able to increase investment in innovation-driven growth without near-term earnings dilution or an ongoing impact to cash flow, all with a focus on optimizing long-term shareholder value.

I want to close by expressing my sincere gratitude to all of our employees for your hard work and unwavering commitment to the Medtronic Mission. Your dedication was instrumental in achieving our results this quarter and making a difference for so many people around the world. Thank you!

Geoff -- turning it back to you to take it home.

Geoff Martha

OK. Thank you. But before I wrap up, I want to note that Tom Holloran passed away last week at the age of 94. Tom provided decades of leadership to our company, first as general counsel, then as president, and as a director on our board for many, many years. In the early 60's, Tom was one of the instrumental people who created our Medtronic Mission, together with our founder Earl Bakken. Tom was also a significant leader in the Twin Cities and beyond, and served on several company boards. Our thoughts are with Tom's family as they celebrate his life.

Now, before we go to the analysts' questions, I'll close with a few brief concluding comments on our progress. You've seen now for several quarters in a row that we're delivering on our commitments with durable, mid-single digit revenue growth. And, when you look over the last couple of quarters, we've had a rapid cadence of meaningful, innovative product approvals, many of which are just getting started, including EV-ICD, both PulseSelect™ and Affera™ in PFA, Inceptiv™ for SCS, Percept™ RC for DBS, and of course our new Simplera Sync™ sensor in Diabetes. And we can't forget Symplicity™ for hypertension. When you combine these with our investments to enter surgical robotics, along with the strong execution we're having in businesses like Spine and Diabetes, this is what gives us confidence in our ability to continue delivering durable growth.

At the same time, we've been sharing with you our efforts to restore the earnings power of the company, and we're seeing those efforts begin to show up in our financials. And the comprehensive transformation that we've been working on – streamlining our operating model, aligning incentives, revamping our capital and portfolio management activities, and instilling a performance-driven culture – well, this is also having an impact.

These changes take time, and we're certainly not done, but it's very encouraging to see our progress and where we stand today. And equally exciting are the catalysts that we see coming, which we believe will lead to significant advancements for patients, and value creation for both healthcare systems around the world and our shareholders.

So with that, let's move to Q&A where we're going to try to get as many analysts as possible, so we ask that you limit yourself to just one question, and only if needed, a related follow-up. If you have additional questions, you can reach out to Ryan and the Investor Relations team after the call.

With that, Brad, can you please give the instructions for asking a question?

Brad Welnick

For the sellside analysts that would like to ask a question, please select the "Participants" button and click "Raise Hand." If you're using the mobile app, press the "More" button and select "Raise Hand." Your lines are currently on mute. When called upon, you will receive a request to unmute your line, which you must respond to before asking your question. Lastly, please be advised that this Q&A session is being recorded.

For today's session, Geoff, Karen, and Ryan are joined by:

- Que Dallara, EVP and President of Diabetes;
- Mike Marinaro, EVP & President of the Surgical & Endoscopy Businesses;
- Sean Salmon, EVP and President of the Cardiovascular Portfolio; and
- Brett Wall, EVP and President of the Neuroscience Portfolio

We'll pause for a few seconds to assemble the queue…

Geoff Martha

OK. Thanks for the questions. We appreciate your support and continued interest in Medtronic. We hope you'll join us for our Q4 earnings broadcast – which we anticipate holding on Thursday, May 23rd – where we'll update you on our progress and how we finished the fiscal year… and look ahead to fiscal '25. So, with that, thanks for spending time with us today and have a great rest of your day.