



## **Agilent Technologies Third Quarter Fiscal 2014 Conference Call Prepared Remarks**

ALICIA RODRIGUEZ

Thank you and welcome everyone to Agilent's Third Quarter Conference Call for Fiscal Year 2014. With me are Bill Sullivan, Agilent president and CEO; Ron Nersesian, Keysight president and CEO; and Didier Hirsch, Agilent senior vice president and CFO.

Joining in the Q&A after Didier's comments will be the Presidents of Agilent's Life Sciences, Diagnostics and Applied Markets or LDA businesses, Mike McMullen and Fred Strohmeier. Also joining from Keysight will be Neil Dougherty, CFO, and Guy Séné, senior vice president of Measurement Solutions and Worldwide Sales.

You can find the press release and information to supplement today's discussion on our website at [www.investor.agilent.com](http://www.investor.agilent.com).

While there, please click on the link for "financial results" under the "Financial Information" tab. There, you will find an investor presentation along with revenue breakouts, 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 Bill, Ron and Didier will refer to non-GAAP financial measures. You will find the most directly comparable GAAP financial metrics and reconciliations on our website.

We will make forward-looking statements about the financial performance of the company and the separation of the electronic measurement business. 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.

Lastly, we expect this to be the final quarter in which we conduct a joint conference call for both Agilent and Keysight. We expect the company separation to be finalized in early November, after which Keysight will operate and report as an independent company.

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

BILL SULLIVAN

Thanks Alicia, and hello everyone.

Today, Agilent reported third-quarter revenues of \$1.77 billion, an increase of 7 percent versus last year, and above the high end of guidance. Orders of \$1.74 billion were up 9 percent over a year ago.

Adjusted earnings of 78 cents per share also exceeded the high end of guidance, and increased 15 percent over last year. Operating margin was 19.2 percent, up 90 basis points from the third quarter of fiscal 2013.

Both Keysight and LDA delivered on revenue and earnings commitments. In most end markets, we saw continued improvement and good order growth across both businesses.

Our work to split the company continues to go very well. On August 1, Keysight began operating as a wholly owned subsidiary of Agilent. We expect the separation of the company to be completed by early November as planned.

Today, I will share performance highlights for LDA or the life science, diagnostics and applied market businesses that comprise Agilent moving forward.

Following my remarks, Ron will share performance highlights for Keysight. Finally, Didier will provide a more detailed discussion of Agilent's overall financial results, as well as our guidance for the fiscal fourth quarter.

Turning to LDA, third-quarter revenues came in at \$1.01 billion, up 6 percent over a year ago, or 5 percent on a core basis. Orders grew 10 percent to \$1.02 billion, or 9 percent on a core basis. Operating margin was 19 percent, up 50 basis points from last year.

In our Diagnostics and Clinical markets, revenue grew 6 percent, with strength in array CGH and target enrichment, as well as demand for pathology products in the US and Europe.

Revenue from Analytical Laboratory markets also grew 6 percent in Q3. We were pleased with the growth we saw across our instruments, services and consumables portfolio, fueled by new offerings to the market place.

Within the Life Sciences and Applied markets that make up Analytical Laboratories, Pharma/Biotech was up 8 percent, led by mid-sized and specialized Pharma customers. Life Sciences Research was up 4 percent, posting the best year-over-year growth in two years. Results were driven by increased government spending on capital equipment in the U.S. and Europe.

Government spending was also the catalyst behind 16 percent growth in Environmental and 12 percent growth in Forensics. In Food, revenues were up 4 percent over last year, as results from the U.S. and Europe were offset by the impact of FDA restructuring in China.

Chemical and Energy revenues were relatively flat, growing 1 percent, largely due to softer demand from China versus a year ago.

Geographically, economic recovery and government funding drove growth in the Americas and Europe, up 6 percent and 8 percent respectively. Asia Pacific grew 4 percent, as China continues to work through government agency reorganizations, which is resulting in longer approval cycles.

Turning to the business segments within LDA, Life Sciences and Diagnostics Group revenues grew 5 percent. Orders grew 11 percent, with broad strength

across LDG products. Operating margin was almost 16 percent, down slightly from last year and up 260 basis points from last quarter.

LDG introduced a number of new products in the quarter. One highlight was the 6495 LC Triple Quad Mass Spectrometer, which provides higher sensitivity, robustness and reliability, particularly for the food and environmental markets.

Another highlight was the introduction of the IQ FISH workflow for bone marrow and custom FISH service through Sure Design. Both FISH products provide high quality results with significantly shorter turnaround times – from 16 hours to 2.5 hours in the case of the IQ FISH.

LDG also signed a development and commercialization agreement with Merck & Co. for a companion diagnostic device, using Dako's IHC solutions with Merck & Co's anti PD-L1 cancer drug.

In the Chemical Analysis Group, revenues and orders increased 8 percent. Operating margin was over 23 percent, up 180 basis points from a year ago.

CAG announced the 5100 ICP-OES in July. The new product runs analyses 55 percent faster, and uses 50 percent less gas per sample than competitive systems. The 5100 is suited to applications in Environmental, Food, Energy and Pharmaceutical markets.

CAG's recently introduced 7010 GC Triple-Quad Mass Spectrometer, targeted for the Food Safety market, lowers cost and improves ease of use compared to current

high-resolution MS systems. The 7010 significantly strengthens Agilent's market position with a range of pricing options, performance and productivity benefits.

In July, the Cary 700 Universal Spectrophotometer was named a 2014 R&D 100 Award winner. The award recognizes the 100 most technologically significant products introduced into the marketplace over the past year.

This award marks the third consecutive year Agilent spectrophotometers have been recognized as R&D 100 Award recipients. In 2013, the Agilent 8800 Triple-Quad ICP-MS won the award, and the Agilent 4100 Microwave Plasma-Atomic Emission Spectrophotometer won in 2012. These awards demonstrate the benefit of our investment in spectroscopy.

Looking forward to Q4, we expect mid-single-digit growth across LDA as we continue to build on order momentum, gain traction with new products, and drive manufacturing cost reduction. We remain committed to creating shareholder value through:

1. Increasing our organic growth rate, by leveraging Agilent's strength in the Analytical Lab into fast-growing genomics and diagnostic market;
2. Continuing to differentiate through best-in-class tools, workflow solutions and customer experience; and
3. Expanding operating margins and return on invested capital, consistent with our long-term operating model.

Turning to guidance, LDA revenues for the fiscal fourth quarter of 2014 are expected to be between \$1.07 billion and \$1.09 billion, or 6.2 percent core growth at the midpoint. We expect operating margins at the midpoint of 21.1 percent.

For the full year, we expect LDA revenue to range from \$4.07 to \$4.09 billion, with operating margins at the midpoint of 19.0 percent. Didier will provide additional details in his remarks.

Thank you for being on the call. I will now turn it over to Ron to talk about Keysight and the Electronic Measurement business.

### RON NERSESIAN

Thank you, Bill, and hello everyone.

I am pleased to report that Keysight had a very good quarter, and we continue to focus on returning to market growth rates while meeting operating margin expectations.

Turning to our performance, I will start by highlighting three headlines from Keysight's third quarter.

- First, Q3 revenues came in at the top end of our guidance range and operating margins were above expectations.
- Second, our overall outlook and forecast for the second half remains unchanged, despite the potential disruption from geopolitical, macroeconomic, and company separation risks.
- And third, as Bill mentioned, we began operating as Keysight Technologies on August 1 and remain on track to be fully separate from Agilent in November.

Now, let's move to the specifics. Keysight revenues of \$757 million increased 8 percent year-over-year, while orders of \$722 million were up 7 percent, resulting in a book-to-bill ratio of 0.95. Keysight continues to deliver solid profit margins, generating operating profit of \$149 million for the quarter, which corresponds to an operating margin of 20 percent.

Last quarter, we highlighted the operational separation of Keysight that occurred on August 1. This was a massive step that had the potential to impact the timing of customer shipments. In fact, some customers requested earlier deliveries to ensure no delays during our transition and this moved some revenue from Q4 into Q3.

As we have consistently noted throughout this year, we expected our Aerospace and Defense and Communications markets to grow in the second half. These markets were the drivers of Keysight's Q3 growth, but strength in these markets was offset by weakness in the Industrial and Computer markets.

Aerospace and Defense revenue grew 13 percent this quarter with strength in both government and prime contractor business, as well as regional strength in the Americas and Asia.

Communications revenue grew 16 percent in Q3. Wireless basestation and component manufacturing were strong. However, handset manufacturing was weak as customer buying power and increased competition accelerated price erosion in that business.



Industrial, Computers, and Semiconductor revenue was flat year-over-year. Continued strength in semiconductor end markets was offset by softer computer business.

On a regional basis, revenues grew year-over-year in all regions with the exception of Japan. Europe grew 16 percent versus a soft compare last year. Asia Pacific, excluding Japan, improved 11 percent with positive growth across nearly all segments. The Americas grew 8 percent, while Japan declined 13 percent, due to declines in government and Aerospace Defense spending.

Overall, Keysight continues to invest in the transformation of our product portfolio, with a focus on modular, software, and certain wireless solutions.

Aligned with this focus, in Q3, Keysight was awarded the Global Frost & Sullivan Award for Growth Excellence Leadership in the PXI instrumentation market. We also announced a strategic partnership to collaborate in early 5G research with China Mobile, the world's largest mobile network operator, and announced participation in the Korea 5G Forum.

Keysight introduced new products in the quarter, including our modular Bit Error Rate Tester which provides a new level of scalability and flexibility for the fast-paced, high-speed digital markets. In addition, in July we began volume shipments of our PXI vector signal analyzer. It is the world's fastest and most accurate microwave vector signal analyzer that significantly reduces test times across a wide range of applications and markets.

As you know, Keysight began operating as a subsidiary of Agilent on August 1, and we expect to complete the spin-off in early November. Our focus throughout this journey is to make this significant transition as seamless as possible for our customers. Our successful results to date are due to the hard work of our employees, who are implementing a separation plan that includes working closely with customers to coordinate our shipment and delivery plans in this transition period. I am very pleased by our achievements so far.

Turning to the outlook for the remainder of the year, we are facing several headwinds in a handful of areas, most notably in Russia. Our sales to Russia have represented about 3 percent of Keysight's total revenue. The volatile political environment as well as new export restrictions on certain products may halt growth in one of our faster growing regions.

Despite the geopolitical, macroeconomic, and company separation risks, we are reiterating our second half and annual guidance. We expect FY14 revenues in the range of \$2.91 to \$2.95 billion, which represents 2 percent core growth at the midpoint. We have tightened the range, but the midpoint is the same as communicated last quarter. Similarly, our expectation for full-year operating margin remains unchanged at 18.9 percent at the midpoint.

This implies Q4 revenues are expected to be in the range of \$740 to \$780 million with operating margins at the midpoint of 20.5 percent.

I will now turn it over to Didier to provide the details of Agilent's overall financial results.

## DIDIER HIRSCH

Thank you, Ron, and hello, everyone.

To recap the quarter, orders grew 9% year-over-year, revenues 7%, and our revenue of \$1.766B, OM of 19.2% and EPS of 78 cents were all higher than the high end of our guidance.

Please note that Q3 core revenue growth by segment and by geography is reported on the slide deck posted on our website.

This quarter, currency added about 0.6 percentage points to our year-over-year revenue growth, and acquisitions had no material impact. We bought back \$50M of stock in Q3, redeemed \$500M of debt, and generated \$28M in Operating Cash Flow. This is lower than traditional, for three main reasons:

1. We prepaid about \$60M of supplier invoices at the end of July, as we will not make any payment in the early part of August
2. We paid \$29M for the redemption of the 2015 notes and also prepaid the current interest.
3. Pre-separation expenses amounted to over \$60M

I will now turn to the guidance for our fourth quarter

We expect Q4 revenues of \$1.81B to \$1.85B and EPS of 87 to 91 cents. At midpoint, revenue will grow 6.5% and EPS 10%. Our 21.0% projected OM at midpoint will be 180 bps higher than Q3 FY14 and 60 bps higher than Q4 of last

year. While we are maintaining our spending discipline, we are also investing in key growth initiatives. We expect to generate over \$300M of operating cash flow in Q4 and incur about \$60M of pre-separation costs.

Now to the Fiscal Year 2014

The FY14 guidance, at mid-point, as previously communicated, with a narrower range. We expect FY14 revenues to range from \$6.99B to \$7.03B and FY14 EPS to range from \$3.04 to \$3.08.

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