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EDITED TRANSCRIPT

RMD - Q3 2020 Resmed Inc Earnings Call

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OVERVIEW:

Co. reported 3Q20 revenues of \$769m, non-GAAP net income of \$188m and non-GAAP diluted EPS of \$1.29.



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PRESENTATION

Operator

Welcome to the Q3 Fiscal Year 2020 ResMed Earnings Conference Call. My name is Diego, and I will be your operator for today's call. (Operator Instructions) Please note that this conference is being recorded. I will now turn the call over to Amy Wakeham, Vice President of Investor Relations and Corporate Communications. Thank you, Amy, you may begin.

Amy Wakeham - *ResMed Inc. - VP of IR & Corporate Communications*

Great. Thank you, Diego. Good afternoon, and good morning, everyone. Welcome to ResMed's Third Quarter Fiscal Year 2020 Earnings Call. We appreciate you joining us, and I hope you all remain healthy and safe during these times.

This call is being webcast live and the replay, along with a copy of the earnings press release and our updated investor presentation, will be available on the Investor Relations section of our corporate website later today.

Joining me on the call today to discuss our quarterly results from various remote locations across San Diego and Sydney are CEO, Mick Farrell; and CFO, Brett Sandercock; as well as other members of management who will be available during the Q&A portion of our call.

During today's call, we will discuss several non-GAAP measures. For a reconciliation of these measures, please review the notes to today's earnings press release.



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And as a reminder, our discussion today may include forward-looking statements, including, but not limited to, expectations about ResMed's future performance. We believe these statements are based on reasonable assumptions. However, our actual results may differ, particularly in light of the highly uncertain global environment we are currently operating in and the effects of the COVID-19 coronavirus on our business. You are encouraged to review our SEC filings for a discussion of the risk factors that could cause our actual results to differ materially from any forward-looking statements made today.

With that, I'd like to go ahead and now turn the call over to Mick.

Michael J. Farrell - ResMed Inc. - CEO & Director

Thanks, Amy, and thank you all for joining us today. These are unprecedented times, as Amy just noted. We are in the midst of a global pandemic, which is having profound effects on public health, particularly the most vulnerable among us.

During this time, our top 3 goals here at ResMed are simple. Goal one is the preservation of life, helping people breathe with world-class ResMed ventilators and ventilation masks, while their own immune system fights against this novel coronavirus and the disease it causes, COVID-19.

Goal two is the safety and health of our amazing team of 7,500 ReMedians, providing solutions in 140 countries worldwide, because without our people, we can't help anyone breathe better.

And goal three is the ongoing delivery of world-leading products and services to treat sleep apnea, chronic obstructive pulmonary disease and asthma as well as the ongoing production of market-leading software to take care of over 110 million people with care delivered by home medical equipment providers, skilled nursing facilities, nursing homes, hospice, and importantly, in the place where people prefer to be, their home.

I've never been more proud to call myself a ResMedian than I am today. Every one of our global team is fully engaged in the COVID-19 crisis. They are demonstrating impressive feats of ingenuity, compassion and drive to support patients, clinicians, providers, health systems and beyond. My e-mail inbox is overflowing daily with stories of ResMed heroes, including frontline workers, such as our own respiratory therapists and clinicians as well as ReMedians, who are showing up every day, using all of our updated safety procedures to source ventilator components from around the world, to produce ventilators and masks and tubing and software and deliver these life-changing solutions worldwide.

To share just one example from many is the story of a ResMed hero from our China team, actually in Wuhan, in Hubei province, who donned a full hazmat suit every day for the first 10 weeks of the corona outbreak in that region. He was setting up thousands of people on ResMed ventilators and ResMed masks, including a ventilator that we call the guardian angel or GA ventilator produced right there in China. We don't know how many lives this gentleman saved there in Hubei province, but I have the good fortune of calling him, my ResMed teammate. So to all those ResMed heroes, I say thank you and that I'm inspired by you and how you stepped up to help patients at the start of this crisis there in January and for the duration now through April and beyond.

As a global company providing solutions in over 140 countries, we have mobilized our efforts and resources to address COVID-19 as this deadly disease moves from region to region. We have accelerated production and distribution of invasive ventilators, noninvasive ventilators, including bilevel devices as well as ventilation masks for the patients who need them most, no matter where they live.

We produced over 52,000 noninvasive ventilators, including bilevels and invasive ventilators during the quarter. This is a threefold increase on our production from the same quarter in 2019, living up to the expectations that we set publicly. We have also driven a tenfold increase in our ventilation mask production, actually more than tenfold. We are aligning distribution of these ventilation products worldwide using a global ethical epidemiology-based model of ventilation needs based on our models of the surge of COVID-19 patients around the world. And our key guiding principle is the preservation of life.

We can and will do more over the coming days, weeks, months and quarters to support health care systems as COVID-19 continues to impact countries across Asia, Europe and North America and with future patient surges just starting to begin in South America, Africa, Middle East and beyond.



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We have been able to achieve these outcomes while ensuring that we always place the health, safety and wellbeing of our ResMed team at the top of our priority list. Without our people, as I said earlier, we can do nothing. Our actions have included work-from-home policies for all whose job function allows for that. We have instituted noncontact temperature screening, mask wearing policies and physical distancing protocols for all of our supply chain, production, distribution and technical service teams worldwide. While we have around 65% of our global team now working from home, these important jobs such as production, distribution and tech service just can't be done from home. We have established world-class safety and quality procedures in all of our manufacturing plants, distribution centers and offices, and we're ready to get back to work as cities and countries plan to do that.

Safety and quality are part of our DNA at all times. And today, more than ever, these capabilities enable us here at ResMed to support our customers with a sustainable supply of products, services and solutions throughout this COVID-19 crisis and beyond.

I also want to express my gratitude and appreciation for the extraordinary efforts of people beyond the boundary of ResMed, especially the frontline health care workers in hospitals worldwide. Respiratory therapists, critical care nurses, critical care doctors and many others have demonstrated extraordinary leadership and personal sacrifice at this time. These clinicians are triaging people with symptoms into various therapeutic pathways depending on the changing acuity of each individual with this novel coronavirus from CPAP therapy to bilevel therapy, to more advanced noninvasive ventilation as well as to full endotracheal intubation with invasive ventilation for the patients who need that.

These clinicians are using ResMed ventilators and ResMed ventilation masks with direct person-to-person engagement, which even with full personal protective equipment still includes significant risk for that clinician. We are working with customers worldwide to drive digital pathways to try to minimize unneeded person-to-person interaction. Examples of this include remote monitoring of ventilation devices, telehealth solutions and virtual patient population management. We have over 11 million devices with available connectivity to our cloud-based solutions, including myAir and AirView. We have over 13 million patients as well as over 6 billion nights, 6 billion nights of respiratory medical data in the cloud.

We had a running start in the field of digital health well before this COVID-19 crisis. One of the few positive benefits out of this awful crisis is that it has brought to the forefront the importance of digital health for the health and safety of respiratory therapists, respiratory nurses and critical care physicians. Digital health also brings benefits of more scalability, more cost efficiency and better outcomes for patients.

Throughout the quarter, despite all the changes brought by this coronavirus, we have continued to execute on our long-term ResMed 2025 strategy, including digital health, expanding end-to-end pathways for sleep apnea, for COPD and for asthma as well as building the world's best out-of-hospital health care software network. Fundamentally, we believe and continue to believe, through this crisis even more so, that the future of health care is outside the hospital. That's where ResMed competes today, and that's where ResMed wins today.

The COVID-19 pandemic has proved an interesting point. The more we can establish noncontact digital health pathways at scale, the better the health of therapists, nurses and physicians and the better the efficacy, the efficiency, the scale and the quality of care for patients. We have accelerated our ability to improve over 250 million lives in outside-the-hospital health care by 2025.

The fundamentals of our ResMed business is strong, even as we see uncertainty in the changing kinetics and dynamics of the COVID-19 disease as it continues to move across geographies, from Asia to Europe, to now North America and on to South America, Africa and regions worldwide. We are seeing tailwinds in our business from increased demand of our ventilators such as Astral, Stellar, Lumis as well as our noninvasive ventilators, AirCurve, Flexo and the GA. We are also seeing increased demand for ventilation mask solutions.

We do not know exactly how long the surge of demand will last for each hospital, for each city, for each country and for each region as this COVID-19 virus moves. But as patient flow surges, peaks and then flattens, we are there. And we are getting pretty good at modeling these demand curves using our global COVID-19 epidemiology model of patient flow and the learning from each city that we serve.

Currently, a lot of short-term impact also depends on our ability to keep ventilator production at its maximum capacity. And as I mentioned earlier, we are already at 3x last year's production capacity. And we are doing our best to meet the surge and peak flow in multiple geographies worldwide. A key element is -- in our ability to deliver is our ability to source critical components and ship product in response to the incredible demand as this COVID-19 virus moves around the world.



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I want to be clear on this point, though. Even as we face increased demand for our products, we are doing everything that we can to keep efficiency high and to keep our costs down. Our primary humanitarian goal is 100% locked. At ResMed, we are committed to enabling access to ventilators for COVID-19 patients in order to preserve life. We are keeping pricing steady, and we will not opportunistically increase prices or per unit profit in our response to COVID-19.

We believe that there will be lessons learned during the crisis that will enhance our ability here at ResMed to drive innovation in the coming quarters, coming years through our research and development pipeline, particularly in the fields of digital health technology as well as our product and software innovation. We are very competitively positioned in these fields today, but we think we will be even more so tomorrow.

While balancing our response to the global public health crisis, we have also been executing well in our core business. We have delivered strong growth in our sleep apnea, COPD and asthma businesses across geographies, with solid contributions from our software-as-a-service business during the quarter. In a few minutes, our CFO, Brett Sandercock, will provide the details of our third quarter financial performance, along with our outlook for the remainder of fiscal 2020. But first, I'll provide just a few financial highlights and briefly discuss execution towards our ResMed 2025 strategy along with some milestones for the quarter.

So for the third quarter of fiscal year 2020, we delivered just around \$770 million in quarterly revenue, which is up 17% year-over-year, reflecting growth and positive momentum across our product portfolio, software solutions and global markets. As part of our global COVID-19 response, we have seen tailwinds for the increased demand for invasive ventilators and noninvasive ventilators, including bilevel devices, masks and accessories, as I mentioned earlier. We estimate the incremental impact to be approximately \$35 million of COVID-19-related revenue during the quarter. So from this \$770 million in quarterly revenue, we generated a strong \$240 million in cash flow from operations during the quarter, enabling us to return cash dividends to shareholders, as declared by our Board today.

We continue to invest in the future growth of our enterprise with double-digit increases in our research and development investments during the quarter. This R&D investment includes shifting resources to ventilators and ventilation masks and clinical research and technical help people to help clinicians, physicians, inventors and people worldwide during the COVID-19 crisis as well as keeping the ongoing innovation work going for our core sleep apnea, COPD, asthma and software-as-a-service businesses.

We have set a clear path for ResMed to maintain our position as the global leader in digital health technology, transforming the way health care is delivered for those suffering from sleep apnea, COPD and asthma as well as enabling people to live healthier lives in a portfolio of settings away from the hospital.

The execution of our long-term strategy drives progress against our triple aim of: first, slowing chronic disease progression; second, reducing overall health care system costs; and third, improving the quality of life for our ultimate customer, the person who uses our products, to help them sleep better, breathe better and deliver higher quality of life away from the hospital.

We believe that when we help a person sleep better, breathe better and live a better quality of life away from acute care, this positions ResMed to help those people achieve their best health outcome in other chronic disease conditions, including cardiovascular disease, diabetes, mental health and beyond. We are forming multiple partnerships to drive these long-term health benefits, including our joint venture with Verily and many other private partnerships beyond. Watch this space.

We have 3 priorities that guide our daily focus. Number one, to grow and differentiate our core sleep apnea, COPD and asthma businesses across global markets. That's just our clear #1 priority. Number two, to deliver world-leading medical devices and digital health technology to engage physicians, providers and patients so that together, we can improve clinical outcomes, reduce costs and enhance patient experiences. That's our triple aim. And our third priority is to build the world's best software solutions network for health care that is delivered outside the hospital, and we're well on track to do that.

We have advanced on all 3 of these priorities during the quarter, and I'll briefly touch on a few recent highlights to demonstrate areas where we have momentum and are driving innovation. We had an exceptionally strong growth this quarter on a geographic and product basis, including 17% growth globally. Our team delivered strong and distributed geographic growth, including a 12% increase in the combined United States,



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Canada and Latin America regions as well as an incredibly strong constant currency increase of 27% across the combined Europe, Asia and other regions.

As discussed earlier, there was an impact from the COVID-19 surge in demand of ventilation in the quarter of around \$35 million in revenue, so that's around 4.5% of the \$770 million in revenues for the quarter. In short, our core underlying business remained robust, over and above that of the ongoing surge of demand.

On a product basis, during the last 12 months, we improved over 16 million lives by providing a person with a ResMed device or a ResMed complete mask system to help them breathe better and live a better life. Including our digital health solutions for out-of-hospital software in this number, we impacted together over 110 million lives during these last 12 months. The ability to improve these lives is supported by over 6 billion nights of respiratory medical data in the cloud. These data allow us to perform sophisticated data analytics and to drive actionable insights for the benefit of customers, including patients, physicians, providers and health care systems. This makes ResMed the global leader in digital health for our field and the partner of choice for our customers, helping them increase efficiency, reduce costs and improve outcomes.

So shifting to a discussion of our core sleep apnea business. We are seeing significant impact from the COVID-19-related lockdowns on new patient diagnoses in sleep. We have seen double-digit declines in diagnosis rates in affected markets. Many sleep clinics, especially hospital clinics are temporarily closed. And many pulmonary and critical care physicians that often work in sleep clinics are shifting their focus to treat COVID-19 patients as the surge comes to their city, their region, their state, their hospital. It is important to note that we have seen the mask and accessories resupply dimension of our business not only maintained, but actually increased during the quarter.

As we look forward, there is uncertainty and it's not clear to what extent the upsurge in ventilation device and ventilation mask revenue will offset the decline in sleep device revenue and whether sleep mask revenue will maintain its growth or decelerate somewhat. But we know these facts, number one, the sleep apnea prevalence remains incredibly high, over 936 million people worldwide. And we know, fact two, that there is a backlog of diagnostic activity for sleep apnea and COPD that many clinics and physicians are preparing to ramp up their home sleep apnea testing, both now during the crisis and in the future as lockdowns are lifted around the world.

For the on-premise or in-laboratory tests for sleep apnea, we are modeling how those will scale back up again customer-by-customer, city-by-city and country-by-country as the economy opens up and primary care physician visits and elective medical procedures come back online through telehealth and beyond. Physicians and therapists will then have to work through the backlog of undiagnosed patients that has been built through the COVID-19 lockdown in their region, with a portfolio of both home sleep apnea testing and in-lab tests.

The velocity of the diagnostic pathway return rate will depend on local regulations and behaviors and what we're calling a new normal for patient care. We have real-time experience of the opening back up in some cities in Asia and throughout Europe, and we're starting to see them open up in the U.S. And we have modeled these open-ups carefully to ensure that we can best support customers as they start their home sleep apnea test scale and their in-lab test scale over time to meet the backlog of demand.

Even today, around the world, we're working closely with our customers to accelerate these home sleep apnea testing models and remote patient setup on sleep apnea therapy where customers are pursuing those pathways as well as our ongoing remote sleep apnea patient monitoring. And I mentioned earlier, we have over 11 million, 100% cloud connectable medical devices out there in the field and more that are distributed every day.

It's important to note that these types of partnerships aren't new due to COVID-19. These are things we've been working on for years and decades in some states. And we believe these types of digital health and telehealth and remote monitoring models will only increase due to COVID-19 and as we move into a post-COVID-19 world.

In terms of digital health innovation, we have recently rolled out a new pilot telehealth over video chat so that the physician can not only access information on Air Solutions and AirView, but it can also interact directly with the patient. And we think that will reduce the need for a recovered COVID-19 patient to return to the emergency room or a physician outpatient setting. We view this as a trend that will be accelerated by a combination



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of changes in reimbursement methodologies and overall focus on safety and the preventative and health benefits for both the patient and the health care worker.

Solutions like this can provide incredible scale when leveraged across a digital health network, including over 110 million patient lives. As I noted earlier, our investments in research and development grew by double digits in the quarter, and we put these R&D monies to work to expedite the tripling of ventilator production in the quarter and tenfold capacity increase in our ventilation mask production. We have also formed partnerships with clinicians around the world to help with the COVID-19 crisis, to help create and share clinical white paper, best practice solutions in clinical practice to help with COVID-19 ventilation management, including triage between CPAP, oxygen, bilevel therapy, noninvasive ventilation therapy and invasive ventilation therapy. At the same time, though, we have continued to invest in our core businesses for future growth in sleep apnea, COPD, asthma and software-as-a-service.

As an example of this innovation in our core sleep apnea business, we introduced during the quarter the AirFit F30i. This is the first CPAP mask with a tube-up design in the full face category. This product now gives ResMed the most complete full face mask portfolio versus all our competition on the planet. So what does this tube-up design of the AirFit F30i do for customers? In essence, it gives the freedom of movement back to that ultimate customer, the patient, so they can sleep naturally in any position. The best lumber architecture follows during the night. The F30i also has an innovative cushion that prevents irritation on the nasal bridge, and it has a quick release elbow that allows users to quickly disconnect and reattach the mask from its tubing, making it very simple to start therapy at the start of the night and to stop therapy in the morning.

All this technology built into the AirFit F30i supports the third tenet of our triple aim, to improve the quality of life for the patient. If they have freedom of movement and don't wake up, that improves their sleep, it improves their day, it improves their life. Clearly, it is very early in the product life cycle for the F30i, and this product was launched amid a pretty unique global environment. However, despite some of the noise in the signal, we've been able to see good early acceptance as physicians, respiratory therapists and that ultimate customer, the patient, recognize the benefit and functionality of the innovation in the F30i.

Additionally, during the quarter, we invested \$100,000 in partnership with the not-for-profit American Thoracic Society Foundation through a research grant. The goal of the research and the study is to look at how remote monitoring can help improve the management of patients with COPD. The study aims to detect early changes in lung function from daily recordings and to notify patients and/or physicians when to commence more intensive treatment or to seek high-level medical attention.

Nearly 400 million people suffer from COPD worldwide, and we do not believe these people are well served currently by global health care systems. Our vision of better management for COPD patients through the use of digital health technologies will be accelerated from the findings of this study. It's great to partner with the nonprofit ATS Foundation to help this move forward.

As we discussed earlier, COVID-19 has accelerated the movement to fully remote care in our core sleep apnea and ventilation businesses. Looking at our growing digital health solutions for COPD and asthma, the Propeller platform continues to play an important role in keeping patients outside the hospital, out of acute care locations, leveraging the Propeller's world-leading pharmaceutical adherence technology for these diseases.

Active use of Propeller technology has actually increased during the COVID-19 crisis. We think this is due to the rising awareness of the importance of respiratory health and the fact that people just don't want to go to acute care settings, and so they're using preventative medicines more to do so. While it's not yet material to ResMed's overall revenue, we are seeing increased interest in Propeller's technology to support health systems with population health. We'll keep you updated on any significant milestones with our pharmaceutical partners as well as our work with global health care system partners throughout calendar year 2020 and 2021 as they adopt the Propeller platform for COPD, asthma and beyond.

Before I transition to a discussion of our out-of-hospital software-as-a-service business, I'd like to recap briefly why we believe that the SaaS business is critical to ResMed's long-term success and how it fits into our broader portfolio. Our consistent view of the evolution of the health care system is that care will be delivered outside the hospital. The contamination of hospitals with COVID-19 is just one of the latest examples of the types of contagions that are present in many hospital locations worldwide. Our vision is to enable a system where a patient can seamlessly transfer across a portfolio of outside hospital care settings, from home care providers to skilled nursing facilities, to home health, to independent living, assisted



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senior living and beyond. These settings have reduced costs versus the hospital as well as increased efficiency and better health outcomes than the hospital. People are simply happier and healthier in the residential setting of their choice, and the ultimate residence of choice is their home.

The SaaS business clearly leverages the global trend for seniors to want to age in place and supports ResMed's continued execution against the triple aim. Our SaaS businesses enable us to participate more deeply in broader chronic disease across a patient's life cycle, creating additional strategic growth options.

During the quarter, our software-as-a-service business grew at 12% from the period a year ago. We are integrating and optimizing this out-of-hospital SaaS portfolio to support long-term growth. We continue to believe that the long-term weighted average growth of the SaaS markets that we serve is in the high single digits. We clearly beat that growth this quarter, and we plan to exceed that rate in the long run as we execute to our SaaS strategy.

During the COVID-19 crisis, many out-of-hospital health care settings have switched their use to support overflow from hospitals. And there has also been a reduction in patient flow to these out-of-hospital facilities due to a reduction in elective surgeries at hospitals. Skilled nursing facilities and nursing home volumes have been extremely hard hit by COVID-19, and this will impact our MatrixCare business growth in the coming quarters. We expect market growth in our current portfolio of SaaS businesses that we serve to be in the mid single-digit range for the next few quarters, before its recovery to high single-digit growth in the medium to long term as the COVID-19 surge passes and people return to their primary care physicians and return to their elective surgeries and patient volume returns.

In support of the increased growth of the SaaS portfolio, during the third quarter, we completed the acquisition of a company called SnapWorx. SnapWorx provides patient contact management and workflow optimization for sleep apnea resupply for our HME customers. The combination of Brightree's technology and live call services with this new SnapWorx tech creates the largest resupply base in the industry with end-to-end workflow automation for HME customers. Resupply is an area of the HME business that has been a strong ballast in the boat during the COVID-19 lockdowns. And these types of programs, including Brightree and SnapWorx together, set up our customers for ongoing success and better patient engagement through the crisis and beyond.

In summary, the SaaS portfolio is an important driver of our long-term success and a critical enabler of our ability to impact our triple aim. We are investing for long-term growth in SaaS and leadership in this space.

Our performance across the entire ResMed portfolio during the quarter demonstrates the resiliency of our business during, what I would call, extremely challenging global times. And it highlights the dedications of ReMedians all over the world and the dedication of our customers, the clinicians, providers and health systems to deliver for the people who need our help. Looking forward, we are modeling impacts of headwinds and tailwinds from the COVID-19 crisis, with detailed scenarios of impacts by customer, by city, by region and by business line.

While we face temporary headwinds in sleep apnea diagnosis and SaaS patient business flows I just talked about, we are also seeing tailwinds from increased demand for our ventilation devices, our ventilation masks around the world. The fundamentals of our overall business is strong, but these are uncertain times and the crisis continues to unfold across geographies, and we don't know exactly how long the related headwinds and the related tailwinds will last. We don't know specifically by each city, country and region how fast they will open up, but we know they will open up. And as we have seen in Asia and Europe, as these economies open up over the coming days, weeks and months, ResMed will be there to serve them.

And we know one thing that as they start to open up, there has been and will be a backlog of patients who need the channel's help for sleep apnea, COPD, asthma and out-of-hospital health care needs. We're investing now to be ready for those realities of the open-up so that we can be there to support our customers with the best digital health solutions and the most scalable solutions to help them grow now. We are leading from the front.

The nature of the COVID-19 crisis has highlighted the importance of our digital health strategies I mentioned earlier. Our ability to improve over 250 million lives by 2025 in out-of-hospital health care is not only on track, we think it's accelerated these last 3 months. This is the one welcome benefit in what has been incredibly challenging 90 days for every company, not just ResMed in every nation, every government dealing with this



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crisis. We're glad that we have made extensive investments in remote monitoring, remote patient setup, digital health, population health management over the last 5, 10-plus years that we can now offer and bring to the market to help them when they need it.

The combination of accelerated digital health technology and the recognition of the value of remote monitoring and the projected changes that are already happening in global reimbursement models for digital health, combined with the growing acceptance of virtual diagnosis and virtual setup, represents a new and significant medium to long-term tailwind for the ResMed business. This combined with our strong pipeline of new products and digital health solutions, including sleep apnea, COPD, asthma and the out-of-hospital SaaS gives us strong confidence in our future. We think this is a unique positioning that solidifies our leadership role in global digital health in med tech, but will also support ResMed's growth over the medium to long term.

Before I hand the call over to Brett for his remarks, I'd like to commit that while we have already played a significant role providing tens of thousands of ventilators, many, many more ventilation masks and clinical support to clinicians worldwide to fight the COVID-19 crisis, we are not done. We will do even more in the coming quarter and the coming quarters to deliver more ventilators, more ventilation masks for countries as they go through the patient surge. And we will be there to support health care systems around the world in respiratory medicine and digital health not only during this COVID-19 crisis, but in what we call the new normal post-COVID-19 world that will be more digitally enabled and more digitally connected than ever before.

With that, I'll turn the call over to Brett in Sydney. Brett?

Brett A. Sandercock - ResMed Inc. - CFO

Right. Thanks, Mick. In my remarks today, I'll provide an overview of our results for the third quarter of fiscal year 2020 and some remarks for our Q4 outlook. As Mick noted, we had a strong quarter. Group revenue for the March quarter was \$769 million, an increase of 16% over the prior year quarter. In constant currency terms, revenue increased by 17% compared to the prior year quarter. Revenues for the third quarter were favorably impacted by significant sales of ventilator devices and accessories. We estimate that the incremental revenue benefit from COVID-19-related sales was in the order of \$35 million. Excluding this incremental impact, our group revenue increased by 12% in constant currency terms.

Taking a closer look at geographic distribution and excluding revenue from our software-as-a-service business, our sales in U.S., Canada and Latin America countries were \$394 million, an increase of 12% over the prior year quarter. Sales in Europe, Asia and other markets totaled \$286 million, an increase of 23% over the prior year quarter or, in constant currency terms, a 27% increase.

By product segment, U.S., Canada and Latin America device sales were \$196 million, an increase of 8% over the prior year quarter. Masks and other sales were \$197 million, an increase of 17% over the prior year quarter. In Europe, Asia and other markets, device sales totaled \$195 million, an increase of 26% over the prior year quarter or, in constant currency terms, a 29% increase. Mask and other sales in Europe, Asia and other markets were \$91 million, an increase of 18% over the prior year quarter or, in constant currency terms, a 22% increase. Globally, in constant currency terms, both device sales and masks and other sales increased by 18% over the prior year quarter.

Software-as-a-service revenue for the third quarter was \$90 million, an increase of 12% over the prior year quarter. On a non-GAAP basis, SaaS revenue increased by 9%.

During my commentary today, I will be referring to non-GAAP numbers. The non-GAAP measures adjust for the impact of amortization of acquired intangibles, the purchase accounting fair value adjustment to MatrixCare deferred revenue and an impairment of minority interest investments. We have provided a full reconciliation of the non-GAAP to GAAP numbers in our third quarter earnings press release.

Our non-GAAP gross margin improved by 70 basis points to 60% in the March quarter compared to 59.3% in the same quarter last year. The increase is predominantly attributable to favorable product mix and manufacturing efficiencies, partially offset by typical declines in average selling prices.

Moving to operating expenses. Our SG&A expenses for the third quarter were \$172 million, an increase of 5% over the prior year quarter. In constant currency terms, SG&A expenses increased by 7% compared to the prior year period. SG&A expenses as a percentage of revenue improved to 22.4%



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compared to 24.8% reported in the prior year quarter. Given the volatility in potential future revenue outcomes, I will not provide our normal guidance with respect to SG&A as a percentage of revenue. However, looking forward, we expect SG&A expenses to increase in the low single digits compared to the year ago period. R&D expenses for the quarter were \$51 million, an increase of 8% over the prior year quarter or on a constant currency basis, an increase of 11%. R&D expenses as a percentage of revenue was 6.7% compared to 7.2% in the prior year. We continue to invest in our business, particularly targeted at innovation. This is evidenced by the double-digit growth in R&D expenses in Q3. We believe our long-term commitment to innovation will deliver a sustained competitive advantage.

Looking forward, we expect R&D expenses to continue to grow in the high single digits to low double digits, reflecting our commitment to innovation through the economic cycles. Total amortization of acquired intangibles was \$20 million of the quarter, a decrease of 10% over the prior year quarter, reflecting historical intangible assets becoming fully amortized during the quarter. Stock-based compensation expense for the quarter was \$14 million. Non-GAAP operating profit for the quarter was \$238 million, an increase of 31% over the prior year quarter, reflecting strong top line growth, expansion of gross margin and well-managed operating expenses. Excluding the benefit from COVID-19 impacts, we still continue to experience solid operating leverage. Non-GAAP net income for the quarter was \$188 million, an increase of 47% over the prior year quarter. On a GAAP basis, our effective tax rate for the March quarter was 14.9%, while on a non-GAAP basis our effective tax rate for the quarter was 15.1%.

Looking forward, we estimate our effective tax rate for the fourth quarter and fiscal year 2021 will be in the range of 18% to 20%. Non-GAAP diluted earnings per share for the quarter were \$1.29, an increase of 45% over the prior year quarter. Excluding the benefit from COVID-19 impacts, we estimate our diluted earnings per share were \$1.16, an increase of 30% over the prior year quarter. Our GAAP diluted earnings per share for the quarter was \$1.12. Additionally, during the quarter, we recognized write-downs of \$9 million associated with minority equity investments. Cash flow from operations for the third quarter was \$240 million, reflecting robust underlying earnings and working capital management. Capital expenditure for the quarter was \$30 million. Depreciation and amortization for the [March] quarter totaled \$46 million. During the quarter, we paid dividends of \$56 million. During the quarter, we also completed the acquisition of our previously announced tuck-in acquisition of SnapWorx. The acquisition will be non-GAAP EPS neutral in year 1 and is expected to be accretive to non-GAAP EPS in year 2. However, overall, the impact will not be material to group earnings. We recorded equity losses of \$5 million in our income statement in the March quarter associated with the Verily joint venture. We expect to record an underlying run rate of approximately \$5 million of equity losses each quarter through fiscal year 2021, associated with the joint venture operations.

Given the unprecedented nature of current events, I would like to make some comments on our financial health. Strong balance sheet has always been a hallmark of ResMed and is most valued by investors in times of economic uncertainty. We ended the third quarter with a cash balance of \$353 million, having generated \$240 million in operating cash flow during the third quarter and \$472 million in the first 9 months of our fiscal year 2020. As of March 31, we have \$1.4 billion in gross debt and \$1 billion in net debt. We had total assets of \$4.5 billion. Our debt levels remain modest. And at March 31, we had a further \$895 million available for drawdown under our existing revolver facility.

In summary, our liquidity position is strong. However, I also want to highlight that in these times of uncertainty, we are maintaining a disciplined approach, and we are tightly managing expenses, cash flow and liquidity. Today, our Board of Directors declared a quarterly dividend of \$0.39 per share. Dividends are important to many of our shareholders, and the declaration of our dividend reflects the Board's confidence in our strong liquidity position and operating performance.

Turning to our fourth quarter outlook. At a high level, we expect to see continued strong growth in our respiratory care business and expect incremental respiratory care revenue to significantly exceed in Q3. However, we expect to see a headwind in sleep device sales in Q4 in response to a temporary reduction in the diagnosis of new patients. Masks and accessories have shown resiliency over the past 3 months, which reflects the insulating value of the large patient installed base. Like many other companies, we are experiencing high uncertainty in the current environment with circumstances and information changing almost on a daily basis. And as a result, our forecast and possible future revenue outcomes remain dynamic.

And with that, I will hand the call back to Amy.

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Amy Wakeham - ResMed Inc. - VP of IR & Corporate Communications

Great. Thanks, Brett. Thanks, Mick. (Operator Instructions) Diego, we're now ready for the Q&A portion.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our next question comes from Lyanne Harrison from Bank of America.

Lyanne Harrison - BofA Merrill Lynch, Research Division - VP

Congratulations on a great result. I'm very interested in, I guess, the uplift that you did on ventilators, and you maybe mentioned you got \$35 million tailwind for this quarter due to the threefold increase in the device production (inaudible) in ventilators by far. Can you tell me whether or not you are able to increase your volume of production of ventilators as you go through quarter 4 and to meet any increased demand in other countries?

Michael J. Farrell - ResMed Inc. - CEO & Director

Thanks, Lyanne. Thanks for the question. And yes, you're right. We had 2 separate metrics that we sort of laid out there. One that we sold an extra \$35 million worth of ventilator in the quarter. Those were from our inventory and stuff that we produced in Q2 and some in Q3 and so that was a \$35 million tailwind for our business, and we expect some of that certainly to continue as the surge continues worldwide into Q4. And then in addition to that, we tripled our production from a year ago, and we made over 52,000 noninvasive ventilators, bilevel devices and invasive ventilators. So your question of, can we continue and/or increase the production capacity? And the answer is absolutely yes. We are constrained on some key components for the invasive ventilators. So the Astral and Stellar have some significant constraints in the components that go into those invasive ventilators of the Astral and Stellar type products. Well, Astral is an invasive ventilator and Stellar is actually noninvasive ventilator. But we really don't have significant constraints to the Lumis STA other than some components around the alarms module and the extra components and the AirCurve ST. So those noninvasive ventilators can scale to 5x or 10x, and we can really scale to whatever the demand is. And so then it comes down to our ability to predict hospital-by-hospital, customer-by-customer, what those surges in demand are going to be as the virus moves around the world and to make sure that ResMed is there, getting an order and making sure we can deliver those invasive ventilators, but really importantly, those noninvasive ventilators and alternative therapies that are also used in the different levels of acuity for a patient with COVID-19. So the answer in short is, absolutely. We did all we could, and we tripled production in the quarter, and we are looking to do that and more in Q4 to deliver for the needs that continue worldwide.

Lyanne Harrison - BofA Merrill Lynch, Research Division - VP

Okay. So just to clarify, (inaudible). How much can you increase production on the ventilators (inaudible).

Michael J. Farrell - ResMed Inc. - CEO & Director

I am going to say, Lyanne, the audio wasn't fantastic during that, but I think I heard you say that how would we or how fast would we move from the sort of 3x increases to a 5x or 10x on AirCurve ST, that's going to be dependent upon our modeling of the different surges that happen city-by-city and country-by-country. And clearly, the masks are used far more rapidly because they are changed over pretty regularly certainly patient-to-patient, but often day-to-day with these non-vented ventilation masks. And so we expect the surge to continue and us to continue to be able to produce throughout Q4 and beyond for the needs as this goes -- as this virus goes around the world and continues to expand.



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Lyanne Harrison - BofA Merrill Lynch, Research Division - VP

So my question was, how much can we increase the ventilator masks (inaudible)

Michael J. Farrell - ResMed Inc. - CEO & Director

Yes, I've got to say, I can't -- I think I heard you say, can we increase the ventilation mask production? We've increased it tenfold, and we'll continue to do so. I think we should go to the next question. Sorry, Lyanne.

Operator

Our next question comes from Suraj Kalia with Northland Securities.

Suraj Kalia - Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst

Good afternoon everyone. I hope everyone is safe and healthy. Mick, just one from my side. And forgive me if you all mentioned this. Can you help characterize your investment in Nyxoah. You all are thinking about the neuromod market specifically for sleep apnea? What is the construct of ResMed's investment? That will be greatly appreciated.

Michael J. Farrell - ResMed Inc. - CEO & Director

Thanks, Suraj. It's a great question. And as you know, you followed our stock for a long time. We look at a portfolio of investments to treat sleep apnea. And around 10 years ago, we actually invested in the 3D printing of a sleep apnea dental device called Narval, and that's now a great part of our portfolio and treats a great number of patients in France and across Northern Europe. The neurostimulation market is an interesting one and Nyxoah, we think, is a leader in that space, and we decided to make a minority equity investment in them. I'll actually hand over to Jim Hollingshead, who's the President of our Global Sleep business, to talk about how neurostim, dental, CPAP and how it all fits together.

James R. Hollingshead - ResMed Inc. - President of Sleep Business

Thanks, Mick. Just very briefly, since I know we're probably short on time now. The gold standard therapy for sleep apnea continues to be CPAP therapy. And that -- we think that will continue for the foreseeable future. We get a chance to see a wide range of technologies as they emerge. And we always look very carefully at anything we think is an alternative. And as Mick mentioned, we obviously have a fantastic oral device, which we sell in Europe very successfully. The Narval device, high-tech, 3D printed, very low volume of the mouth, very comfortable. We've looked at the neurostim space for quite a long time. There have been a number of companies that have tried to succeed in the neurostim space. We think Nyxoah has a novel offer and is potentially disruptive, but it's very early days. It's a minority investment in what's effectively a start-up company. So we like the technology. We like to play, but we'll have to see how it plays out.

Operator

Thank you. Our next question comes from Chris Cooper with Goldman Sachs.

Chris Cooper - Goldman Sachs Group Inc., Research Division - Research Analyst

Mick, can you just remind us of the approximate payer mix in the sleep apnea business, please? And I appreciate this is a highly dynamic situation, but can you just share your thoughts on how you expect the higher rates of unemployment we're seeing in the U.S. to impact that business, please?



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Michael J. Farrell - *ResMed Inc. - CEO & Director*

Yes, Chris, thanks for the question. And yes, certainly, every country around the world is different. I presume you're asking about the U.S. payer mix, Chris? Maybe you're on mute, but I'll start with the U.S.

Chris Cooper - *Goldman Sachs Group Inc., Research Division - Research Analyst*

Okay, primarily, year-on-year.

Michael J. Farrell - *ResMed Inc. - CEO & Director*

Okay. So obviously, we sell in 140 countries outside the U.S. and on the reimbursed part of our business, the non-SaaS part, it's close to that 60-40 range, 60% being within the U.S. and 40% being beyond that. And if you include SaaS businesses, it's more like 65% of our global business in the U.S. So I'll start with that. So we don't have contracts directly with payers, but our portfolio of home medical equipment customers do. And there's around 5,000 customers in the U.S. home medical equipment providers, and their payer mix for the field of sleep apnea and COPD that we serve is around 20%, maybe 25% for some regions, Medicare; and around 75%, 80%, private pay. And as we've seen through the COVID-19 crisis, we have seen ongoing payments from the -- both the government and private payers through to ResMed. We are carefully watching our accounts receivable. And as Brett said, we're carefully watching our cash flow to make sure that payers pay on time and with time, but we haven't seen any issues as yet. Clearly, unemployment has increased in the country from single digits to double digits through this crisis, and it's something that all companies are looking at very carefully. But we haven't seen any issues as yet, but we are watching the cash flow very carefully to make sure that we have continuing flow of capital and cash through our business.

Operator

Our next question comes from Mike Matson with Needham and Company.

Michael Stephen Matson - *Needham & Company, LLC, Research Division - Senior Analyst*

So I guess first, I just wanted to ask about the resupply business. Wondering why you think that, that's been so strong? Is there any kind of demand pull forward happening there? Do you think that can be sustained as long as the pandemic continues?

Michael J. Farrell - *ResMed Inc. - CEO & Director*

Yes, Mike, thanks for the question. And certainly, there's -- it's quite interesting. As you know, you've followed us for a long time, too, Mike. Our installed base of CPAP patients, sleep apnea patients is a very strong part of our mask business. We're talking north of 80-plus percent of our masks sales across the U.S. are to that installed base, the diagnosed patient who loves their therapies, changed their life and they're going to go and reorder every time. I think the focus of COVID-19, and that it's a respiratory medical issue and that has raised the importance of making sure that your lungs are well taken care of and that you breathe well and your overall health is well, has increased people to make sure they get their prescriptions for everything, including heart attack. Post heart attack patients are getting more prescription pills. As I noted earlier, the Propeller side, COPD medicines and asthma medicines, we're seeing increased use of those in respiratory medical health. And we've seen a similar thing, I think, in the CPAP mask side, where when you are capable of getting a mask, you are more likely to click, yes, I would like that. And we haven't seen any reduction in people saying, "Oh the co-pay is too high or I don't want to go there." We've seen actually the reverse where people are saying, "wow, it's been 90 days, I'm due for a therapy, for a CPAP mask, tubing, et cetera." And they're clicking yes, and they're getting those devices delivered to them. So very strong ballast in the boat for our HME customers. And the HME customers themselves are really focusing on this part of their business because it's a good opportunity for them. We think -- look, there will be some deceleration if there is some sort of that surge of the sort of the toilet paper model where I'm going to over inventory, you all going to make sure I've got enough masks. That might decelerate



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somewhat, but we don't think -- we think there's a lot of ballast in that. And people who are on CPAP therapy and loving the CPAP therapy are going to want to get new masks. And through COVID and beyond, the importance of respiratory medicine will only be increased because of this. So we think that part of that business is very steady through the crisis and even stronger beyond. I think it will change behaviors that will last well beyond COVID-19 surge.

Michael Stephen Matson - *Needham & Company, LLC, Research Division - Senior Analyst*

Okay. And then just with regard to sleep diagnostic testing. Can you provide any more detail around the declines that you're seeing kind of late in the March quarter? And then to what degree could increased use of home testing kind of some sort of remote telemedicine model offset that? And are you doing anything to try to enable the CPAPs to implement -- to ramp up, I guess, their home sleep testing?

Michael J. Farrell - *ResMed Inc. - CEO & Director*

Yes. Great follow-up question, Mike. And we're doing a lot in that space. I'm focused a lot with Rob Douglas on our global task force on COVID-19 and ventilators. Jim Hollingshead, at the same time, has been running our sleep business strongly. Jim, do you want to follow up on the -- follow-up there on home sleep apnea testing and scale?

James R. Hollingshead - *ResMed Inc. - President of Sleep Business*

Sure. Thanks, Mick. I think it's very difficult to quantify the effects and the balances of decline in in-lab testing and increase of home sleep testing in general. And it's very different country by country, both because of the timing of the pandemic and then how different health care systems are structured and so on. So trying to get a quantification, I think, is quite difficult. What we do know is we have seen some decline in in-lab testing. That's not a surprise. Health care systems around the world have shifted their focus to COVID-19. Many countries have gone in lockdown. Much of the U.S. has gone in lockdown. So we know that in-lab testing has declined and dipped. We have some evidence to suggest it stabilized at a lower level. It's hard to know exactly what that level is, but we think it's potentially stabilized at this point. But in parallel, we also know there's been an increase in home sleep testing and remote testing. A number of the labs around the U.S. have increased their use of home sleep testing devices and routines. And where that's done in Europe and can be done in Europe, it continues to be done, and we think it will turn on faster in Europe. And then the final point of your question is what are we doing? We're actually working very hard to enable home sleep testing to figure out how to help our lab customers and our physician customers virtualize their model, not just to our device offerings, but through workflows, through webinars and trainings, and we're working hard to see if we can virtualize some of that with software, which will take a little bit more time. And we do think that a shift to home sleep testing is, which has been going on worldwide for years, will be accelerated by this. And just as Mick said in his prepared comments, one of the things that we think will come out of the crisis generally for the sleep business is increased adoption of our already very broad offerings, virtualized care offerings. And so we think that will accelerate through the crisis and then have a new normal coming out of the crisis.

Operator

Our next question comes from Margaret Kaczor with William Blair.

Malgorzata Maria Kaczor - *William Blair & Company L.L.C., Research Division - Research Analyst*

Just wanted to follow up on the comment you guys have on production of NIVs and LSVs. I think I heard you guys say you've produced 52,000 of those devices in the quarter, which I know you guys don't give ASPs, but it seems like it could be \$200 million or \$300 million worth of products in the device side versus the \$35 million benefit you saw in the quarter. So I guess, long and short, but the question is, were those made-to-order or in advance of demand? And how should we think about that product entering the field?



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Michael J. Farrell - ResMed Inc. - CEO & Director

Margaret, that's a great question. And yes, certainly, we did -- you heard correctly. We made 52,000 noninvasive ventilators and invasive ventilators. So that includes everything across the Astral, Stellar, Lumis, Flexo, GA and AirCurve, all those devices. So we included across all that group, 52,000, and they have very different pricing. But clearly, it's a lot more than just the \$35 million of sales in that quarter. So we are prepared for demand ahead. The only thing I'm really willing to say on a public call like this is that we have a public capability with the U.S. government through HHS and FEMA of over \$30 million contract. And so that's a fixed contract that we will fulfill, mostly in Astrals. And -- but we have many other contracts with hospitals, states, governments, nations around the world. I'm not going to go in and quantify any of those. They're usually one to one directly to those countries and directly to those hospitals. But what I can tell you is all the demand that they have and all the supply that we have, our supplies just cannot keep up with the demand as it moves around the world. And so what we're doing is maximizing production in advance and then making sure we get through the peak and through the surge, but not have an over amount of inventory at the other side. And so we're carefully managing the peak, the surge, the flattening and then making sure we get back to normal COPD, neuromuscular disease, ALS and other sales with those ventilators because those patients will be there beyond. And that's how we're looking at it, Margaret. But yes, clearly, we are preparing for more sales in the future of those ventilators and ventilation masks. That -- those tailwinds will last through Q4 and likely beyond.

Brett A. Sandercock - ResMed Inc. - CFO

Yes. I'll just add quickly, Mick. Margaret, yes, there's a lot -- there's a meaningful amount that's in transit mode so to speak, as we're trying to get those into our DCs and then ultimately to customers. So there's that -- that impacts it as well. So -- but we'll continue to produce. And as Mick said, the demand is there. It's just a matter of getting it through the logistics.

Operator

Our next question is from Steve Wheen with Evans & Partners.

Steven David Wheen - Evans & Partners Pty. Ltd., Research Division - Executive Director of Healthcare

I just had a question on the FDA in terms of its response to COVID-19. It was alluding to the use of CPAP as being something that could be utilized. Just wondered what the experience was there? And then the other item that the FDA had done was to remove ventilators from the competitive bidding process. I just -- and there has -- appears to be some pressure to delay competitive bidding in the latest round. Just any comments on any of those 3 things would be very useful.

Michael J. Farrell - ResMed Inc. - CEO & Director

Yes, Steve, those are great questions. And I've had actually quite a lot of conference calls with the FDA commissioner, Hahn; and HHS secretary, Azar, during this crisis. ResMed was part of a Defense Production Act that was put in place by the White House to secure component supply for our ventilator so that we could supply HHS, FEMA and beyond. And so I had a lot of interaction there. Look, the FDA have really been a great partner through this process. They helped us get Emergency Use Authorization, EUA, for a number of our products to be used in different context. So for instance, our noninvasive ventilators, which were very scalable. And as we talked about, we made tens of thousands this quarter. We had doctors wanting to use them in various ways, invasive ways and others. And so the doctors needed an EUA to be able to do that, and they have got that. And the FDA were very quick to us and other manufacturers in providing those Emergency Use Authorizations.

Simultaneously, Secretary, Azar, over at Health and Human Services and CMS, they did take noninvasive ventilators out of competitive bidding around 2021, and that was a very good change for our HME customers. It really took a load off for them knowing that these NIV and ventilation businesses will be good ongoing concerns for them. So we saw a good partnership from both the FDA and HHS as part of this crisis. And HHS also worked with FEMA to make sure that we got the demand, and that was the \$30-plus million contract I talked about to us, and there were 5 other manufacturers who got contracts as well. I think the government, not just in the U.S., but in all 100-plus countries that we're working with through



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this crisis, have done a great job in contacting us, working with us, helping us with supply chains and helping us with delivery of ventilators to people in the need for this crisis.

Steven David Wheen - *Evans & Partners Pty. Ltd., Research Division - Executive Director of Healthcare*

And sorry, the final part was just the pressure that's being or the attempt to delay competitive bidding, the likelihood of that?

Michael J. Farrell - *ResMed Inc. - CEO & Director*

Yes. I'll hand that over to Dave. He's got more insight on that, David Pendarvis?

David B. Pendarvis - *ResMed Inc. - Chief Administrative Officer, Global General Counsel & Secretary*

Yes. So thanks, Steve. We, along with the rest of the industry, have been suggesting to CMS that they either delay for a year the introduction of the 2021 round entirely or at least the respiratory offerings, respiratory product codes within that offering of the 2021 round of competitive bidding. We have had a dialogue with CMS on that topic, so they are listening. But I can't really handicap the likelihood that it will happen or not. I would echo what Mick said earlier, that CMS has been very responsive, and I think it has highlighted the importance of DME and home-based care in ensuring that as few people are in the hospital is not. And that's a real positive. And we hope that, that cooperative working relationship will continue.

Operator

Our next question comes from David Low with JP Morgan.

David A. Low - *JP Morgan Chase & Co, Research Division - Research Analyst*

Mick, can I just follow-up on the use of bilevel device to treat COVID-19 patients. I mean there's clearly the aerosol issue and the safety issue there. I have seen some efforts to overcome that. Do you think that's going to be on -- I mean -- and I heard your comments, excuse me, about the amount of manufacturing capacity you have. Is your expectation that there will be continued strong demand for that utilization model?

Michael J. Farrell - *ResMed Inc. - CEO & Director*

Yes. Look, it's a great question, David. And certainly, through this crisis, one of the leading countries early on this was the U.K. and the National Institute -- the National Health Service there, the NHS. And they created a protocol, which looked at the various acuity levels of COVID-19 patient because the disease -- the coronavirus gets into the lungs and then causes the COVID-19 disease, which is where mucus builds up as the alveoli react and try to fight off the virus, and it creates mucus in the lungs and builds it up. And so at different levels of buildup, different levels of acuity, different therapies are needed. And so the NHS created a very strong protocol of using both CPAP with some supplemental oxygen from the wall as well as bilevel therapy and then upgrading to more aggressive noninvasive ventilation therapy because bilevel is noninvasive positive pressure ventilation therapy. But then upgrading to higher levels of noninvasive ventilation therapy and even upgrading all the way to the full intubation through the trachea of invasive mechanical ventilation. And all those different modes can be moved up and down by the doctor as they move through the process.

Your question about -- and it was a big question and concern early on that, oh, gosh, what if we have some contagion that some of the COVID-19 will come out? Well, before you put on an invasive mechanical ventilator, if a patient coughs or sneezes, the room is already contaminated. So even with invasive inhalation, there are some contamination protocols. And so what you need is a COVID-19 ward, you need PPE for everybody and you need to establish this floor of the hospital is for COVID-19 with negative pressure and take care of it that way. And that's what they've done in the



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U.K. And actually, that moved to different parts of New York, New Jersey. And as we see this go around the world, people are learning to do that. What you have is a non-vented mask, so a ventilation mask with an inlet and outlet and then a filter on the outlet of the device. And so our Chief Medical Officer, Carlos -- Dr. Carlos Nunez, has been working with key opinion leaders worldwide, and we have a clinical white paper with best practice from Wuhan, from Milan, from London, from Munich, but they're doing it really well in Germany and from New York and around the world. And that protocol does include CPAP, it does include bilevel, it does include noninvasive ventilation with positive pressure, all with specific masks and specific circuit set up all the way up to invasive mechanical ventilation.

Now the second part of your question, after the crisis will people continue to use more noninvasive ventilation? I think the answer is yes. I think it's going to be similar to digital health, where we've had to use home sleep apnea testing, you've had to use remote patient monitoring during this crisis. And you don't want to go to a patient's home. You don't want them to have to come to a hospital. And so that's driven digital health. I think people, doctors in critical care units have seen how noninvasive ventilation, including bilevel has very well treated patients with COVID-19, why can't it very well treat COPD patients? Well, guess what? It can. So I think the adoption of NIV will increase post COVID-19 because of the learnings during COVID-19. I can't quantify that exactly. It's more a medium, long-term thing. But anyway, I hope that answers your question, David. It's a very good one. It deserves a longer answer. And I know we're 10 minutes over, we might just take 2 more questions and let everyone get back to their work day, 3 more questions. Okay.

Operator

Our next question comes from Matthew Mishan with KeyBanc.

Matthew Ian Mishan - *KeyBanc Capital Markets Inc., Research Division - VP and Senior Equity Research Analyst*

And also it's really remarkable, the efforts of you and the employees of your company to support this crisis. So thank you for that as well. I'll just leave it to 1 because most of my questions have been asked. I've heard that there's potentially long-term respiratory implications from COVID-19 exposure. How do you see that patient transition to post-acute?

Michael J. Farrell - *ResMed Inc. - CEO & Director*

Yes, it's a great question, Matthew. I'll hand that to our President and Chief Operating Officer, Rob, to talk about post COVID-19 discharge. What are the next steps, Rob?

Robert A. Douglas - *ResMed Inc. - President & COO*

Yes. Thanks, Matthew. That's a good question. It's still an uncertain world in terms of what these post protocols are going to be across the board. We're seeing different trials and tests being carried out. In some areas, we are seeing patients get discharged with oxygen, and we are noticing an uptick in demand for oxygen around the place. And in other areas, we are seeing some discharges with more CPAP. But I think it's still way too early to say, probably the earliest data we've got is in China where things are normalizing a little bit. The sleep labs aren't yet open, but we're seeing continued ongoing demand for longer-term ventilation. So it's probably leading off the dynamic, that Mick mentioned earlier, that ventilation is noninvasive ventilation and chronic ventilation is recognized as a more relevant treatment than what it had been before.

Operator

Our next question comes from Sean Laaman with Morgan Stanley.



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Sean M. Laaman - Morgan Stanley, Research Division - Australian Healthcare Analyst

Hello everybody. Well done, Mick, clearly doing a great job navigating. Sorry if I've missed it, but my question is, the \$35 million of COVID revenue, was there any geographic sort of breakup of that? And just to clarify, what's that all vent revenue?

Michael J. Farrell - ResMed Inc. - CEO & Director

Sean, that's a great question. Not comfortable going into details of where the \$35 million came from. That's sort of our global number. And it's truly an estimate. It's -- the vast majority of it is ventilation. And so it's Astrals, Stellars, Lumis, AirCurve ST types of products. I'll hand over to Brett Sandercock, our CFO, to see if he wants to provide any further detail on that \$35 million.

Brett A. Sandercock - ResMed Inc. - CFO

Yes. Thanks, Mick. I mean the only -- there is some -- there will be some mask and accessories things in that as well. You'd estimate making -- maybe that accounts for kind of 10% of that number and the rest would be devices.

Operator

Your last question comes from Gretel Janu with Crédit Suisse.

Gretel Janu - Crédit Suisse AG, Research Division - Research Analyst

So you mentioned the double-digit declines in the diagnosis rates in the quarter due to lockdowns. I'm just wondering whether you saw any slowdown in the actual fleet new patient setups in the third quarter? Or will most of that impact from the slower sleep diagnosis impact the fourth quarter?

Michael J. Farrell - ResMed Inc. - CEO & Director

Yes, Gretel, thanks a lot. Look, as you can understand, there's a lot of moving pieces going on right at the moment, and we're watching it through the quarter. And in different countries, and even in some countries in the world, we've seen that decline. Like in China, we saw that decline in January, February, and we're actually starting to pick up on the rates as we started to exit the quarter, and some regions of China starting to open up and then diagnosis is starting to open up again. But -- and similarly in South Korea and some other areas that have COVID-19 under control now. But I'll hand over to Jim Hollingshead to see if he wants to provide any further details the sort of kinetics of the double-digit reduction in diagnostics and any impact on sort of that headwind, I guess, of sleep device sales, while we have the neutral element of sleep masks continuing through. Jim?

James R. Hollingshead - ResMed Inc. - President of Sleep Business

Yes. Thanks, Mick. Thanks, Gretel. With a little bit of a lag, you can also see bit of a drop-off in new patient starts, which we have the ability through our connected solutions to see -- as I said before, I think we're seeing diagnosis stabilize a bit, and I expect some countries to start to turn back on in the near term. And we're seeing new patient starts also stabilize a bit. So hopefully, we'll -- hopefully, we get a bounce off of the floor here. It's very difficult to predict what that will look like. It will be different country-by-country and even metro area by metro area.

Michael J. Farrell - ResMed Inc. - CEO & Director

Great. Well, thanks for all the questions, and thanks to everyone for continuing the 15 minutes over here. I think we'll all agree this was a very unique quarter for not just ResMed, but for all companies worldwide. Look, I'll go with the close now, I think, here and close on up. I'd like to thank again



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to all our shareholders who've joined us for this call. I'd also like to shout out again to the 7,500 ResMedians helping people in 140 countries. You guys are also shareholders in the most part, and I want to thank you for your dedication and hard work, helping people breathe better, sleep better and live better lives outside the hospital. Thanks for all that you do all day, every day. Thanks, especially to those frontline heroes, the people making the products, distributing the products and getting those vents to those 140 countries to somebody who's suffocating and needs our help. I look forward to talking to all of our stakeholders again here in 90 days. And with that, we'll close it up. Thank you, Diego.

Amy Wakeham - ResMed Inc. - VP of IR & Corporate Communications

Great. Thanks, Mick. Thank you all again for joining us today. And just a reminder, if you have any additional questions, please don't hesitate to reach out to me or to Investor Relations. And as previously mentioned, all the documents, along with the transcript and a replay will be available on our website later today. Thanks, Diego. You can now close the call.

Operator

Thank you. This concludes ResMed's third quarter of fiscal year 2020 earnings live webcast. You may now disconnect.

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